INTERNATIONAL ECONOMY

09

9.1. Global economic and financial trends

According to the latest IMF estimates (July 2023), the global economy in 2023 will record growth of 3.0%. Advanced economies recorded a growth of 1.5%, significantly lower than in 2022 (2.7%). Among advanced economies, the IMF expected 0.9% growth in the euro area, which is a significant economic activity slowdown since the euro area growth was 3.5% in 2022, while the IMF forecast a 1.8% growth for the USA. The forecast growth in the developing economies and emerging markets will be at the same level as in 2022 (4.0%). The IMF's forecast for China point to its "jump" this year and recording 5.2% growth compared to the last year's 3.0%. The group of European emerging and developing economies, which also includes Montenegro, reported growth of 1.8% (Table 9.1%).

Table 9.1

Overview of selected global indicators, in %					
Indicator	2022 estimate	Forecasts		Difference relative to April 2023 projections, pp	
		2023	2024	2023	2024
Real GDP growth					
World	3.5	3.0	3.0	0.2	0.0
Advanced economies	2.7	1.5	1.4	0.2	0.0
USA	2.1	1.8	1.0	0.2	-0.1
Euro area	3.5	0.9	1.5	0.1	0.1
Japan	1.0	1.4	1.0	0.1	0.0
Developing countries and emerging markets	4.0	4.0	4.1	0.1	-0.1
China	3.0	5.2	4.5	0.0	0.0
India	7.2	6.1	6.3	0.2	0.0
Russia	-2.1	1.5	1.3	0.8	0.0
European developing countries and emerging markets	0.8	1.8	2.2	0.6	-0.3
Prices of stock exchange goods, average rate					
Oil	39.2	-20.7	-6.2	3.4	-0.4
Non-energy producing products	7.9	-4.8	-1.4	-2.0	-0.4
Consumer prices, average rate					
Advanced economies	7.3	4.7	2.8	0.0	0.2
Developing countries and emerging markets	9.8	8.3	6.8	-0.3	0.3

Source: IMF, July 2023

In Q2 2023, economic activity in the euro area, as per the second estimate, recorded a 0.3% rate of growth quarter-on-quarter. The largest euro area economies, Germany, France, Italy and Spain recorded growths in economic activity of 0.0%, 0.5%, -0.4%, and 0.4%, respectively. Making a comparison between Q2 2023 and the same period in 2022, economic activity in the euro area increased by 0.6%.

The U.S. economy reached a 2.1% growth quarter-on-quarter[58], while its annual growth stood at 2.5%. China's economy recorded a 0.8 rate of growth in the second quarter of 2023.

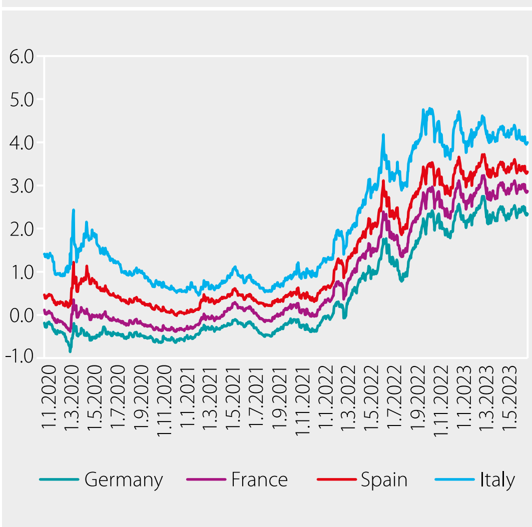
In Q2 this year, the European Central Bank continued to tighten monetary policy by increasing reference interest rated by 0.25 pp twice. The main refinancing rate reached 4.0% at end-June 2023. At the meeting this July, it decided on the new increase of 0.25 pp, thus increasing the main reference rate at 4.25%. The ECB stated that the previous interest rate increases had strong effect on financial conditions and decreased demand. Borrowing costs increased significantly and the lending slowed.

The FED continued to act in order to achieve the objectives of the monetary policy, i.e. reducing inflation to 2%. In the second quarter, it increased the reference interest rate by 0.25 pp to a range of 5.0-5.25%. On that occasion, it was stated that inflation is still high, with a moderate growth in economic activity and that the situation on the labour market is extremely favourable. In light of the problems with certain large banks, the FED stated that the banking system was "strong and resilient". In the statement, it noted that the tightened lending conditions for households and the economy would likely affect the economic activity, employment and inflation. The reference rate additionally increased by 0.25 pp in July.

Yields on German, French, Spanish and Italian ten-year government debt at end-Q2 were 2.34%, 2.87%, 3.32% and 4.00%, respectively. Compared to Q1, the spreads, i.e. the difference in the yields on ten-year government bonds of France and Italy any those on German debt decreased at the end of Q2 2023 (Graph 9.1). The same spread for the Spanish debt was lower that at Q1. These spreads amounted to 0.53 pp, 1.66 pp, and 0.98 pp, respectively. At the end of the observed period, the yield on equivalent US debt was also lower compared to Q1 and amounted to 3.74%.

Graph 9.1

Yields on 10-year government debt in the euro area, January 2020 - June 2023, in %



Source: Bloomberg

The growth of yields on German ten-year bonds during Q2 2023 was driven by market expectations and achievements in the direction of increasing the ECB reference interest rates. The yield on German bonds often followed the trend of US yields on the same debt, the FED decisions and the increase in the interest rates of the Central Bank of Australia and the Central Bank of Canada. In addition to expectations of further monetary policy tightening, the growth of bond yields resulted from the recovery of share prices in the banking sector and the better-than-expected data on the producer price index in Germany. On the other hand, less favourable intra-economic indicators – technical recession in the euro area, the decline in indices measuring investor expectations in Germany, lower-than-expected inflation, and the like affected the decrease in bond yields. Concerning the external influence, weaker Chinese economic data underscored concerns about global economic growth.

[58] The rate at the annual level - the so-called annualised growth rate.

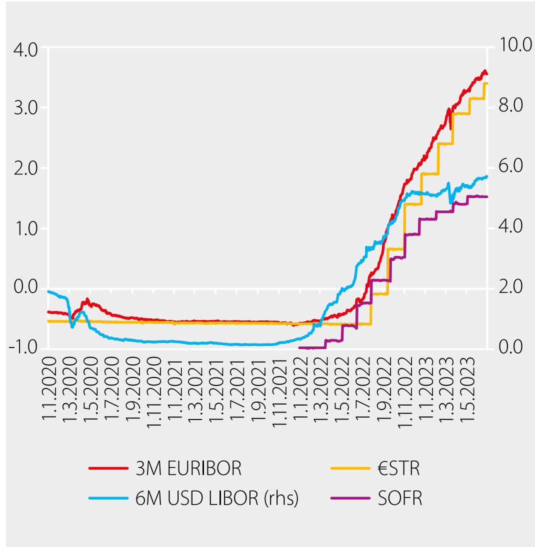
Short-term market reference interest rates mostly followed the suit of the reference interest rates of central banks (Graph 9.2). The six-month *LIBOR* increased 0.41 pp and stood at 5.72% at the end of Q2. *SOFR* grew 0.18 pp and ended the Q2 in the amount of 5.05%. The three-month *EURIBOR* continued to grow slower than in Q1, achieving a growth of 0.52 pp, and it amounted to 3.55% at end-June. At the end of the quarter, *€STR* amounted to 3.4%.

In nominal terms, the euro appreciated against the dollar (0.64%), and yen (9.27%), yet depreciated against pound (2.25%), and Swiss franc (1.53%) (Graph 9.3). During this reporting period, the euro moved on average at the level of 1.0889 dollars per euro, and the exchange rate was 1.0909 dollars per euro at the end of June. The trend of the monetary policies of the globally most influential monetary authorities were the key factors shaping the exchange rate of the euro and the dollar throughout the quarter. Problems in the US banking sector affected the euro and dollar exchange rate appreciation, especially with the data on the outflow of deposits from the "First Republic" bank and the fall of its shares. The exchange rate was shaped by generally worse economic indicators and forecasts in the USA and the euro area, especially in Germany, its largest economy. The level of American debt, moving the debt ceiling and avoiding bankruptcy attracted significant market participants' attention, which had a positive outcome after a long controversy.

At the end of the second quarter of this year, the prices of stock commodities fell by an average of 8.5% compared to the end of Q1 2023. The prices of energy generating products increased by 10.9% - the price of oil fell by 4.5%, while the prices of natural gas and coal decreased by 20.8% and 27.3%, respectively. Non-energy producing products prices decreased by 6.6% - metals by 6.2%, and food and beverages by 6.9%. According to IMF forecasts from July 2023, oil prices will experience an average drop of 20.7% in 2023, while the drop in non-energy prices, as a heterogeneous group of stock exchange commodities, will amount to 4.8% (Table 9.1).

Graph 9.2

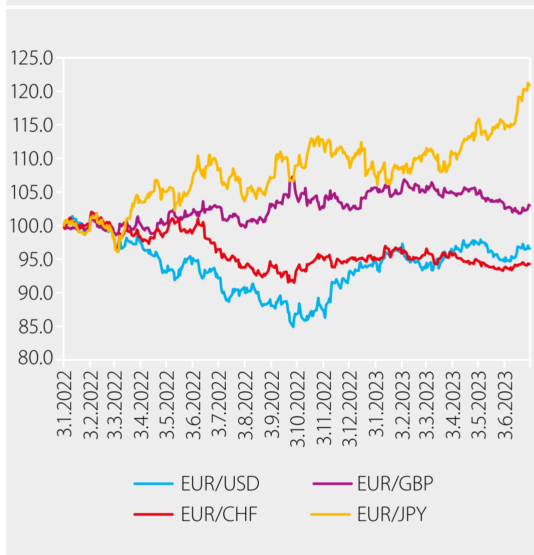
Short-term market interest rates, January 2020 - June 2023, in %



Source: Bloomberg

Graph 9.3

Nominal euro exchange rate, January 2022 - June 2023, 1 Jan 2022 = 100



Source: Bloomberg, CBCG calculations

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At the end of the reporting period, oil price was lower despite OPEC's announcements about a significant production cut. Contrary to this effort, Russia continued to produce large quantities of cheap heavy crude oil. The dollar's appreciation against a basket of currencies raised the oil price. On the other hand, the fear of a potential slowdown in the global economy lowered the price. It primarily related to concerns about the recovery of the Chinese economy, which was partially mitigated by a stimulus package and higher oil import quotas compared to last year. Nevertheless, the China National Petroleum Corporation reduced its forecasts regarding the country's demand for oil for this year from 5.1% to 3.5%, which affected the decrease in the oil price on the international market. Borrowing restrictions in the USA, problems with certain American banks and low oil stocks have significantly contributed to concerns about the global economy slowdown and the oil price. Finally, the additional monetary policy tightening by the leading central banks contributed to this market sentiment.

Looking at the *VIX*[59] index, the instability in the financial markets was low considering that the volatility of the index in the second quarter of 2023 was lower than in the previous quarter and was getting near its pre-pandemic values. Namely, the average value of the index in Q2 this year was 16.5 points, ranging from 12.9 to 20.1 points.

The price of gold, as a specific indicator of stress and risks in the global economy and financial amounted to 1,919.4 $/oz at end-quarter, recording a declining trend. At the beginning of Q2, the gold price rose due to the growing demand for safe assets and after the Fed officials' statement about the potential recession this year. In April and May, the price jumped over $2,000/oz. The new interest rate hike by the FED and the dollar's appreciation against most currencies reflected a drop in demand. The drop in this precious metal's price also resulted from reaching an agreement on raising the US borrowing limit.

At the end of Q2 this year, the global cumulative indices ended at a higher level than at the end of Q1. New York's *SPX* and Frankfurt's *DAX* were higher by 6.51% and 2.09% compared to the end of Q1 2023. The pan-European *STOXX* and the *FTSE 100* indices recorded a decline of 0.31% and 1.88%, respectively.

9.2. Euro area

In Q2 2023, the economic activity in the euro area recorded the growth of 0.1%. According to the European Commission's[60] forecast, the GDP growth rate will be 0.8% in 2023 and 1.3% in 2024. The largest euro area economies, Germany, France, Italy and Spain recorded growths in economic activity of 0.0%, 0.5%, -0.4%, and 0.4%, respectively. The highest growth in economic activity was recorded in Lithuania (2.9%), Slovenia (1.4%) and Greece (1.3%).

In Q2 2023, Industrial production in the euro area fell by 0.9% compared to the previous quarter and by 1.1% compared year-on-year. The turnover of retail trade recorded an increase of 0.2% compared to the previous quarter, yet a 2% decline compared to the same period in 2022. Construction activity achieved a quarterly decline of 1.1% and a zero y-o-y growth rate.

The unemployment rate has been declining since August 2020, when it amounted to 8.6%. At the end of the previous year, it fell to 6.7%, and to 6.6% at the end of Q1 2023. In the euro area, the unemployment rate was the lowest in Malta and Germany (2.9%), and the Netherlands (3.6%), and the highest in Spain (12.8%), Greece (11%) and Italy (7.8%).

[59] A measure of the expected volatility of the US stock prices.

[60] *European Economic Forecast, Summer 2023, European Commission.*

The annual inflation rate during 2022 continued to grow strongly, reaching its highest value in October of 10.6%, after which it moved on a downward trajectory, reaching 9.2% at the end of 2022, and 5.5% at the end of the second quarter of 2023. Observed by country, at the end of the second quarter of 2023, inflation was the highest in Croatia (8.3%), Estonia (9%) and Lithuania (8.2%), and the lowest in Luxembourg (1%). Spain and Belgium (1.6%). According to the main components of the Harmonized Index of Consumer Prices (HICP), the prices of food, alcohol and tobacco recorded a growth rate of 11.6%, energy generating products -5.6%, industrial products (non-energy producing products) 5.5%, while the prices of services increased 5.4%, while their contributions to the total inflation rate amounted to 2.35 pp, -0.57 pp, 1.42 pp, and 2.31 pp, respectively.

Fiscal deficit amounted to 3.2% of GDP in Q1 2023. Portugal was the only euro area country that achieved budget surplus of 2.8% of GDP. The largest deficits were recorded in France (5.1%), Belgium (5%) and Slovakia (3.8%). The total budget revenues of the euro area in 2022 were reduced by 0.2 pp to 47% of GDP, while budget expenses were reduced to a greater extent, by 1.8 pp, to 50.7% of GDP.

The public debt of the euro area countries at the end of Q1 2022 reduced to 91.2% of GDP (12.5 thousand billion euros) from 91.4% of GDP at the end of the previous year. Greece ran the highest public debt of 168.3%, followed by Italy with 143.5%, and Portugal with 113.8% of GDP. Besides the aforementioned countries, the public debts of Spain, France and Belgium exceeded 100% of GDP. On the other hand, the lowest levels of public debt were recorded by Estonia and Luxembourg of 17.2% and 28% of GDP, respectively. Looking at the financial instruments, the main share of the debt or as much as 83% referred to debt securities, followed by loans with 14.2%, while 2.8% were cash and deposits.

Table 9.2

ECB's macroeconomic projections for the euro area, 2022–2025, in %

	2022	2023	2024	2025
Real GDP	3.5	0.9	1.5	1.6
Private consumption	4.4	0.2	1.9	1.5
Government spending	1.4	0.0	1.1	1.4
Gross fixed capital formation	3.8	1.5	1.1	2.1
Exports	7.4	2.7	3.4	3.2
Imports	8.4	1.4	3.4	3.2
Employment	2.3	1.3	0.5	0.4
Unemployment rate, in % of labour force	6.7	6.5	6.4	6.3
HICP	8.4	5.4	3.0	2.2
HICP, excluding energy	5.1	6.4	3.1	2.3
HICP, excluding energy and food	3.9	5.1	3.0	2.3
HICP, excluding energy, food, and changes in indirect taxes	3.9	5.1	3.0	2.3
Unit labour costs	3.0	5.6	3.4	2.6
Earnings per employee	4.3	5.3	4.5	3.9
Labour productivity	1.2	-0.3	1.0	1.3
General government budget balance, % of GDP	-3.6	-3.2	-2.6	-2.5
Structural fiscal balance, % of GDP	-3.2	-3.0	-2.4	-2.3
Public debt, % of GDP	91.4	89.1	87.9	87,3
Current account balance, % of GDP	-1.1	1.1	1.5	1.6

Source: ECB, June 2023