Article | 2 August 2024

THINK Ahead: To cut or to hold? Best not ask AI

Unemployment is rising and life isn't getting any easier for the central bankers. So we asked our AI overlords what they would do. The answer wasn't encouraging, so read on as we dive into next week's key macro and market movers

ING's James Smith on next week's world today

THINK Ahead: To cut or to hold? Best not ask AI

Last week I asked the pressing question of whether central banks were having a "brat summer". Just a day later, the internet declared that Charli XCX's viral "brat" phenomenon had died. Coincidence?

I'd hate to be accused of destroying any other cultural icons, so I've steered clear of the Olympic puns again this week. Mainly because I couldn't think of any. So I asked an AI chatbot and it suggested this zinger: "Why do economists love the relay race? It's all about passing the buck!"

Ouch. Maybe AI is coming for my job after all. I'm just thankful that the labour market is still pretty strong. Or is it?

This is the new question that's keeping the central bankers up at night, now that inflation is back at more palatable levels. Unemployment has started rising, and more so in countries where rate hikes have taken a bigger toll.

The increases are modest so far, but unemployment is famously a lagging indicator of economic ill health. Does that mean the central banks are too late to cut rates? Or is this nothing more than a moderation after all that post-Covid dislocation?

Fed boss Jay Powell told us this week he's in that latter camp. Not for the first time, he argues that lower vacancy and quit rates are down to more labour supply and not weaker demand for workers. And there's something in that.

Employment of foreign-born workers accounted for 60% of job growth since the start of 2023, despite making up only a fifth of the total workforce. That's by no means a perfect measure of migration, but it's a factor that does appear to be helping cool the US jobs market.

But that's not the whole story. James Knightley points to this week's surprise rise in initial jobless claims as a hint that hiring demand is potentially faltering. Rising claims could just be summer volatility, but it's worth watching. James reckons the unemployment rate could end the year at 4.5% or above, up from 4.1% currently.

Either way, this for me was the key comment from Powell this week: he said that the jobs market is no longer inflationary. And that means he's now much more attentive to downside risks to the employment side of the Fed's dual mandate.

The debate on whether the Fed cuts at all this year seems all but finished. The fight is now over how thick and fast those cuts come along, and the jobs market will be pivotal.

Across the Atlantic, the story is less clear cut. The eurozone unemployment rate is still hovering at all-time lows, though it did increase this week. But unsurprisingly this masks very different stories across the region. Germany has seen strong employment over recent years, and like the US, migration has played a role, according to our team's analysis. But German unemployment is rising quickly now, and Carsten explains that this is going hand-in-hand with fading recruitment plans and increased insolvencies.

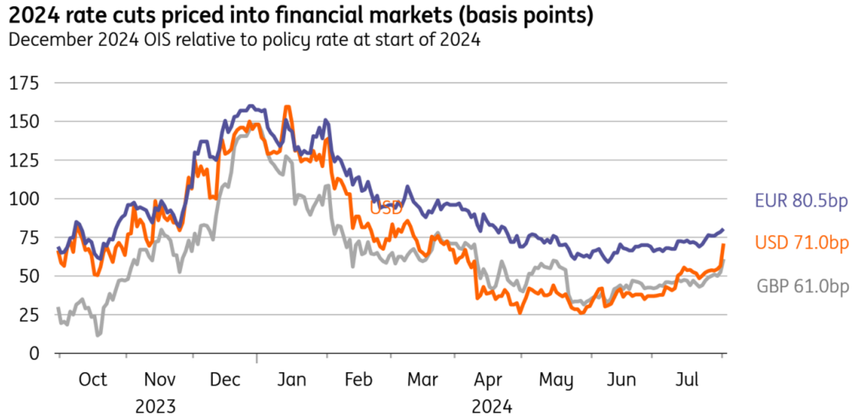
It's a stark contrast to countries like Italy and Spain where unemployment has, if anything, fallen. And there, staff shortages in the service sector are the most acute they've been in decades. Don't forget that Spain recorded another massive quarter of economic growth in the second quarter, where Germany once again contracted.

None of that makes life any easier for the ECB, particularly when you add in those stickier core inflation numbers from this week. Our team thinks a September rate cut is a close call, and you'd imagine the hawks won't give in without a fight.

There are no easy answers, so I asked our chatbot friend from earlier. Its suggestion? How about hiking rates.

Maybe we're safe from our AI overlords after all...

Chart of the week: Markets are ramping up rate cut bets



Source: Macrobond, ING calculations

Data is based on the average rate in December - the number of cuts priced by 31 December will be slightly greater

THINK Ahead in developed markets

United States (James Knightley)

- Financial markets are now fully pricing three 25bp rate cuts from the Federal Reserve this year, with the market seeing the potential for one 50bp cut should the data soften more precipitously. The coming week has a relatively light calendar with Fed speakers likely to make appearances now that the 31 July decision is out of the way. Consumer credit, trade, jobless claims and the non-manufacturing ISM will be the data reports of note with the latter two the main focus.
- Jobless claims are clearly trending higher and this runs the risk that in an environment of rising labour supply, the unemployment rate increases more rapidly in coming months. Meanwhile, the non-manufacturing ISM is pointing to a sharp slowdown in GDP growth even if, as expected, we get a modest bounce after June's very weak outcome. Also watch out for the Federal Reserve's Senior Loan Officer survey, which will provide an update on lending appetite from the banks.

Canada (James Knightley)

- **Unemployment (Fri):** The Bank of Canada has now cut rates twice at consecutive policy meetings and another soft jobs report could make it three out of three for the next policy meeting in September. Inflation is converging on target while the unemployment rate has already risen from 4.8% to 6.4% and we see the risk of it hitting 6.5% next week.

THINK Ahead for Central and Eastern Europe

Hungary (Peter Virovacz)

- **Retail sales/Industry (Tue/Wed):** Previously released disappointing 2Q24 GDP figures make this release less relevant, but it will still help us find out which sectors were the source of the weakness. We expect retail sales to be flat year-on-year between May and June, but based on anecdotal evidence, we think industrial production plummeted, mostly due to the weak

performance in car and electrical equipment manufacturing.
- **Inflation (Thu):** After two months of encouraging monthly repricing, we expect a significant rise in month-on-month inflation in July. Food inflation could accelerate due to the end of mandatory in-store discounts and the phasing out of price caps. We estimate that fuel prices rose by more than 3% on a monthly basis. We see no reason for price pressures to ease in services, where labour cost dynamics are strong. The record-hot weather in July could also have pushed up household energy bills significantly. All in all, we see a significant acceleration in both headline and core inflation - a worrying development for monetary policy.

Czech Republic (David Havrlant)

- **Retail sales (Mon):** Real retail sales growth likely decelerated in June, with mounting uncertainty around the economic recovery taking a toll on consumer confidence. The real wage growth gains are supportive, but there's general unease about the economy and that could impact willingness to spend.
- **Industrial output/Unemployment (Tue/Thu):** Industrial performance looks sluggish and is linked to dormant demand from the main trading partners. Industrial output likely continued on a fresh downward trend. The disappointing economic performance will probably be reflected in an uptick in July’s unemployment rate.

Turkey (Muhamet Mercan)

- **Inflation (Mon):** July inflation is expected to temporarily increase following adjustments in administered prices and taxes, in addition to supply-side factors in unprocessed food prices. We expect a monthly figure of 3%, translating into a rapid decline in annual inflation to 61.4% from 71.6% a month ago, thanks to strong favourable base effects. While the month-on-month change will likely inch up, it will be limited. This is happening against an ongoing tight monetary stance and a domestic demand slowdown.

Key events in developed markets next week

Country	Time	Data/event	ING	Prev.
		Monday 5 August		
US	1445	Jul S&P Global Composite PMI Final	-	54.8
	1500	Jul ISM Non-Manufacturing PMI	52	48.8
	1900	Federal Reserve Senior Loan Officer Survey		
Germany	0855	Jul S&P Global Services PMI	52	52.0
	0855	Jul S&P Global Composite PMI Final	48.7	48.7
France	0850	Jul S&P Global Composite PMI Final	-	49.5
UK	0930	Jul S&P Global Composite PMI Final	-	52.3
Italy	0845	Jul S&P Global Composite PMI Final	-	51.3
Spain	0815	Jul S&P Global Composite PMI Final	-	55.8
Eurozone	0900	Jul S&P Global Services PMI Final	-	51.9
	0900	Jul S&P Global Composite PMI Final	-	50.1
		Tuesday 6 August		
US	1330	Jun Trade Balance (USD bn)	-73	-75.1
Germany	0700	Jun Industrial Orders (MoM%)	2.5	-1.6
Canada	1330	Jun Trade Balance (CAD bn)	-	-1.93
Switzerland	0645	Jul Unemployment Rate	-	2.3
Netherlands	0530	Jul CPI (MoM%/YoY%)	-/-	0.2/3.2
Eurozone	1000	Jun Retail Sales (MoM%/YoY%)	-/-	0.1/0.3
		Wednesday 7 August		
US	2000	Jun Consumer Credit	10	11.35
Germany	0700	Jun Industrial Output (MoM%/YoY%)	2.0/-5	-2.5/-6.7
	0700	Jun Exports	4	-3.6
	0700	Jun Imports	3.5	-6.6
	0700	Jun Trade Balance (EUR bn)	21	24.9
France	0745	Jun Trade Balance (EUR bn)	-	-7.99
		Thursday 8 August		
US	1330	Aug Initial Jobless Claims	240	249
		Friday 9 August		
Germany	0700	Jul CPI Final (MoM%/YoY%)	0.1/2.2	0.1/2.2
Italy	0900	Jul CPI Final (MoM%/YoY%)	-/-	0.1/0.8
Canada	1330	Jul Unemployment Rate	6.5	6.4
	1330	Jul Net change in employment (000s)	10	-1.4
Norway	0700	Jul CPI (MoM%/YoY%)	-/-	0.2/2.6
Netherlands	0530	Jun Manufacturing Output (MoM%)	-	-0.4

Source: Refinitiv, ING

Key events in EMEA next week

Country	Time	Data/event	ING	Prev.
		Monday 5 August		
Russia	0700	Jul S&P Global Services PMI	-	47.6
Turkey	0800	Jul CPI (MoM%/YoY%)	3.0/61.4	1.6/71.6
	0800	Jul PPI (MoM%/YoY%)	-/-	1.4/50.1
Czech Rep	0800	Jun Retail Sales (MoM%/YoY%)	-0.2/3.9	5.2/4.4
Hungary	0730	Jun P Trade Balance	1500	1001
Ukraine	1400	Q2 GDP (QoQ%/YoY%)	-/-	1.2/6.5
		Tuesday 6 August		
Czech Rep	0800	Jun Industrial Output (MoM%/YoY%)	-0.7/-8.8	-2.2/-3.2
	0800	Jun Trade Balance (CZK bn)	-	13.6
Hungary	0730	Jun Retail Sales (YoY%)	3.6	3.6
		Wednesday 7 August		
Hungary	0730	Jun Industrial Output (YoY%)	-6.9	-5.2
Romania	1300	Interest Rate Decision	6.75	6.75
		Thursday 8 August		
Czech Rep	0800	Jul Unemployment Rate	3.7	3.6
Hungary	0730	Jul Core CPI (YoY%)	4.6	4.1
	0730	Jul CPI (MoM%/YoY%)	0.7/4.1	0.0/3.7
	1000	Jul Budget Balance	156.4	-107.8
Serbia	1100	Interest Rate Decision	5.75	6.00
		Friday 9 August		
Russia	1700	Q2 GDP (YoY%)	4.0	5.4
	1700	Jul CPI (MoM%/YoY%)	1.1/9.1	0.6/8.6
Turkey	0800	Jun Industrial Output (MoM%/YoY%)	-/-	1.7/-0.1
Ukraine	1330	Jul CPI (MoM%/YoY%)	-/-	2.2/4.8

Source: Refinitiv, ING

Author

James Smith
Developed Markets Economist, UK
james.smith@ing.com

James Knightley
Chief International Economist, US
james.knightley@ing.com

Peter Virovacz
Senior Economist, Hungary
peter.virovacz@ing.com

David Havrlant
Chief Economist, Czech Republic
420 770 321 486
david.havrlant@ing.com

Muhammet Mercan
Chief Economist, Turkey
muhammet.mercan@ingbank.com.tr