

## Three scenarios for the major economies

Our economists and strategists lay out some alternative scenarios for the global economy and energy prices in 2024



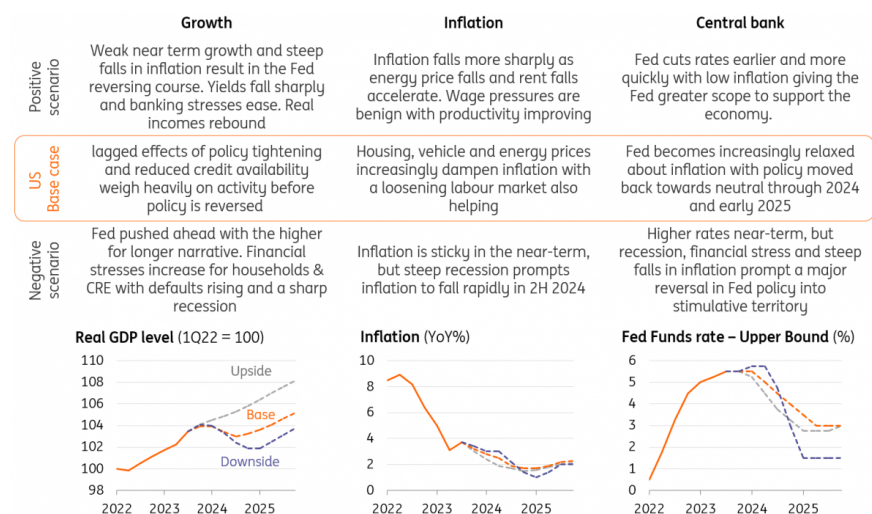
Source: Our alternative scenarios for the global economy and energy prices in 2024

### Three scenarios for the US

Our base case for the US economy sees a modest recession, a sharp fall in inflation and Federal Reserve rate cuts from the spring. But the risk is that the Fed errs on the side of caution to ensure inflation falls to 2%. In this scenario, it hikes one last time and keeps interest rates higher for longer. But if that happens, the pain for the household sector intensifies and loan defaults rise. Commercial Real Estate (CRE) pain spreads and the economy falls into a recession, dampening inflation and forcing the Fed to rapidly reverse course later on.

An upside scenario is largely the opposite, where the Fed becomes much more relaxed about inflation and moves back to a neutral interest rate setting more rapidly. That allows corporates and CRE to refinance at much lower levels, and that keeps loan losses contained. Strong productivity growth and rising labour supply from immigration keep inflation in check.

## Our US scenarios



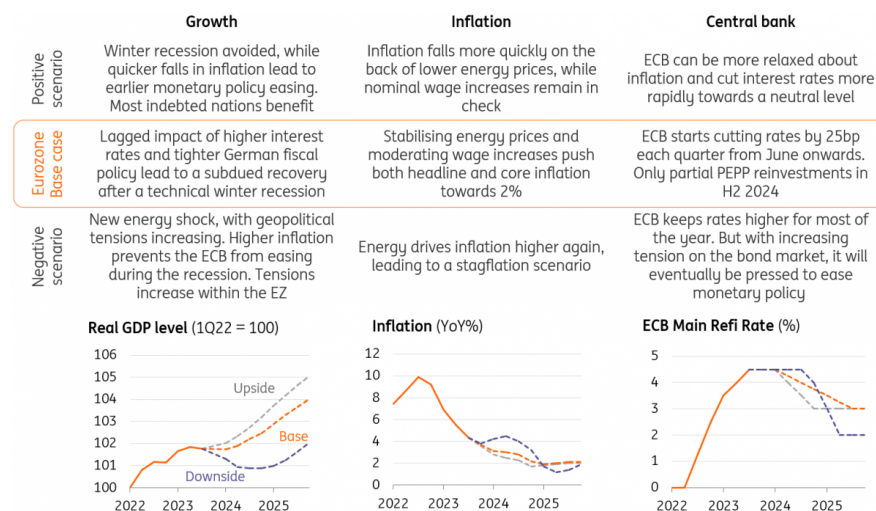
Source: ING

## Three scenarios for the eurozone

For the eurozone, our base case is that higher interest rates prompt a mild technical recession over the winter and that the European Central Bank (ECB) starts cutting rates around the same time as the Fed. The downside risks stem from higher energy prices, which would drive up inflation and push the economy into a deeper recession. In that scenario, the ECB would want to avoid the risk that higher inflation becomes entrenched and would keep rates high throughout the year. The combination of a recession with interest rates remaining high creates tension within the monetary union, driving up sovereign bond spreads.

An upside scenario sees the eurozone avoiding recession entirely and inflation falling faster than expected. This goldilocks scenario would allow the ECB to ease more quickly, with bond yields also coming down. The more indebted member states would benefit, leading to tighter bond yield spreads.

## Our eurozone scenarios

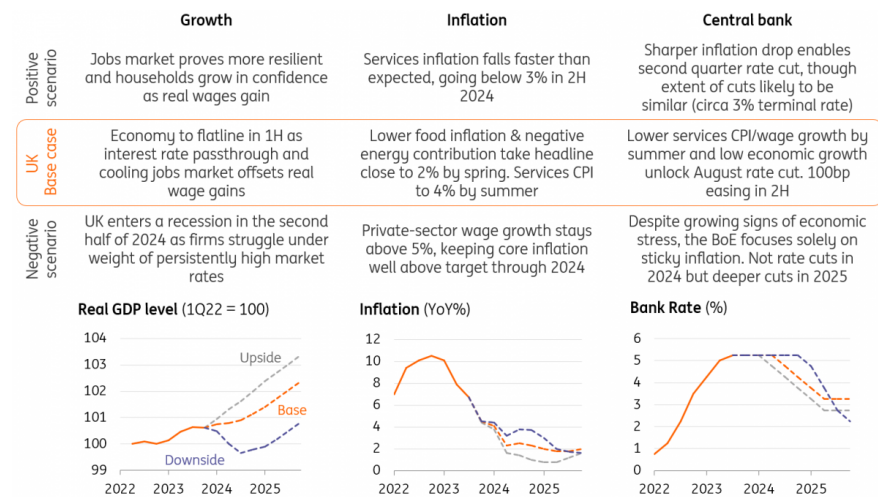


Source: ING

## Three scenarios for the UK

Our UK base case sees the economy narrowly avoiding recession but remaining stagnant for much of the next year. Services inflation should come much lower by the summer, enabling an autumn rate cut. Like the eurozone, the risk is that the impact of higher rates combined with a fresh rise in energy prices tips the economy into a downturn. The Bank of England would focus entirely on the inflation implications initially, keeping rates on hold for the whole year. But in that scenario, sharper cuts would inevitably follow.

### Our UK scenarios

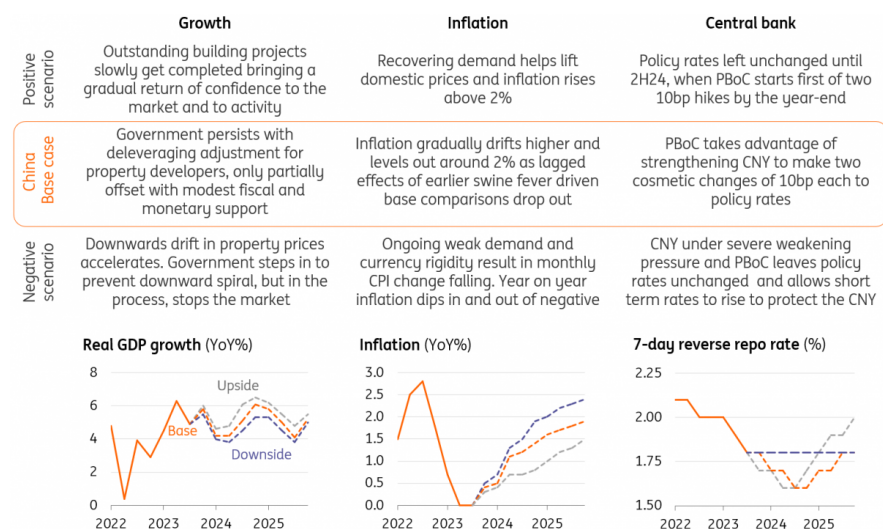


Source: ING

## Three scenarios for China

The base case for China is a continuation of the ongoing deleveraging story that rules out substantial fiscal support and focuses more on returning property to its position in line with President Xi's "Common Prosperity" theme and not an investment. This means that sectors that typically fed into the property development/construction industry – steel, glass, cement, PVV etc., will continue to struggle. Local government finances are improved due to the restructuring of debt but substantial constraints remain, preventing a big pick up in infrastructure spending from filling the void. Weak global demand and ongoing US sanctions limit the external sector's ability to pick up the slack.

## Our China scenarios



Source: ING

## Three scenarios for energy and the risks for inflation

After two major supply shocks, the most obvious risk to the global economy next year is that we get a third. Concerns about a second wave of inflation are front and centre in the minds of monetary policymakers, who are reticent to sound the all-clear after one of the most aggressive tightening cycles in recent memory. But, as we wrote in an article earlier this year, there's no inevitability to a second inflation wave – and [comparisons to the 1970s](#) are imperfect.

These comparisons have, in part, been bolstered by the tensions in the Middle East and the added uncertainty for oil prices. We've outlined some scenarios below. But we have to remember that the US is energy independent, making it far less exposed to 1970s-style shocks. That was evident in the very different make-up of the recent US and European inflation waves. Europe is more vulnerable, particularly if LNG supply tightens. But with eurozone consumer energy bills still more than 20% higher than they were pre-Covid, arithmetically, the scope for a similar inflation shock to 2022 is slightly more limited – even with a large and unexpected spike in wholesale gas costs.

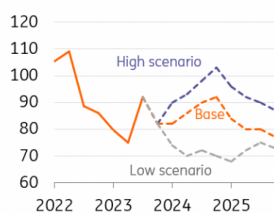
Instead, there are a number of other potential sources of upward inflationary pressure, though none in and of themselves are likely to prompt a 2022-style wave. Metals are an obvious vulnerability, and scarcity due to a lack of production capacity and/or geopolitics are important risks. Likewise, we saw last year the cross-dependency of food prices on energy costs and the ongoing risks associated with the Ukraine war and grain exports. Climate change is also creating increasingly volatile harvests, and the risk here is that this results in more protectionism as producing nations seek to protect domestic supply.

Whatever the catalyst, the lesson from the 1970s was that the economic environment also needs to be ripe for inflation to take off. And here, there are a few parallels. While labour markets are cooling, staff shortages are more prevalent than pre-Covid. Unionisation is less widespread, but worker power is arguably growing. The ability of workers to protect real wages in future inflation shocks is set to increase. Throw in concerns about US fiscal deficits, and there are reasons to think that inflation will stay higher in future years than during the 2010s.

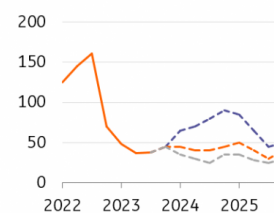
## Our energy scenarios

|                     | Oil (Brent Crude)  | Natural Gas (Dutch TTF)   |
|---------------------|--|---|
| Low price scenario  | Global oil demand disappoints in 2024, remaining largely flat. Weaker demand and less OPEC+ willingness to deepen cuts leaves the market in large surplus through 2024   | European gas demand fails to respond to weaker prices, remaining 15% below 5-year average. European storage hits 100% before 24/25 heating season         |
| Energy Base case    | Demand grows by 1m b/d in 2024. OPEC+ sticks to output targets and Saudi Arabia rolls over voluntary cuts into 1Q24. Market is balanced in 1H24 but in deficit over 2H24 | European storage ends winter above average. This makes the job of refilling storage in 2024 summer easier. Demand slowly recovers following 22/23 winter  |
| High price scenario | Middle East tensions linger and the US enforces Iran sanctions more strictly. This combined with deeper OPEC+ cuts leaves the market in deep deficit in 2024             | Remaining Russian flows stop, while increased competition for LNG leaves Europe tight. Higher prices needed to ensure LNG supplies and demand destruction |

Brent Crude (USD/bbl)



Dutch TTF gas (EUR/MWh)



Source: ING

## Growing risks in the US financial system as excess liquidity withdrawn and fiscal/real estate concerns linger

The withdrawal of excess liquidity from the US money market is a key theme ahead. The genesis of this is ongoing quantitative tightening. The most significant manifestation is the fall in idle market cash going back to the Fed on the reverse repo facility. These will head to zero, signalling a virtual end to excess liquidity by the second half of 2024. Then, bank reserves will come under downward pressure. We think it'd be best for the Federal Reserve not to push too hard on this; there's plenty of possibilities for things to go wrong.

Fiscal deficit-originated supply pressure is also impactful here, making the market a tad skittish. Already, the Treasury market has been struggling with liquidity, mostly with getting size done. This is exacerbated by a repo market that has seen better days and banks that are less market impactful. The smaller banks also have commercial real estate exposures to be concerned about and are already suffering credit card delinquency rates that are higher than experienced during the GFC. It may well be tolerable – but could be an area to watch carefully.

## Author

### James Knightley

Chief International Economist, US

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Peter Vanden Houte

Chief Economist, Belgium, Luxembourg, Eurozone

[peter.vandenhoute@ing.com](mailto:peter.vandenhoute@ing.com)

### James Smith

Developed Markets Economist, UK

[james.smith@ing.com](mailto:james.smith@ing.com)

### Robert Carnell

Regional Head of Research, Asia-Pacific

[robert.carnell@asia.ing.com](mailto:robert.carnell@asia.ing.com)

### Carsten Brzeski

Global Head of Macro

[carsten.brzeski@ing.de](mailto:carsten.brzeski@ing.de)

### Warren Patterson

Head of Commodities Strategy

[Warren.Patterson@asia.ing.com](mailto:Warren.Patterson@asia.ing.com)

### Padhraic Garvey, CFA

Regional Head of Research, Americas

[padhraic.garvey@ing.com](mailto:padhraic.garvey@ing.com)

## Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and

which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).