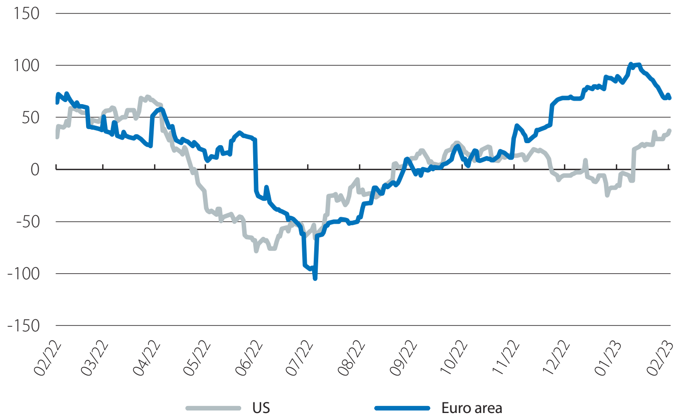
Cautiously optimistic about the international economy

The macroeconomic outlook continues to show encouraging signs in a challenging environment. Economic activity has been performing better during the winter than had been feared back in the summer. Notably, confidence continues to improve and headline inflation may already have peaked, thanks to the substantial reduction in energy prices (85% in the case of gas, versus the August highs) and the normalisation of global supply chains. Overall, the latest signs suggest that economic activity in the major developed economies and in China is holding up better during Q1 than had been anticipated a few months ago. This is obviously good news, but we should not indulge in excessive optimism. Firstly, the geopolitical risk, far from subsiding, remains ever present a year into the war in Ukraine. Moreover, the impact of the rate hikes approved by most central banks has not yet fully translated to economic activity and monetary policy will remain restrictive, given the persistence of the core inflation indices. Indeed, the strength of the latest economic activity data and the persistence of inflation in the major economies has raised the risk that interest rates could climb even higher and that they could also remain high for longer, as reflected in the change in market expectations, which we set out in the financial markets economic outlook section.

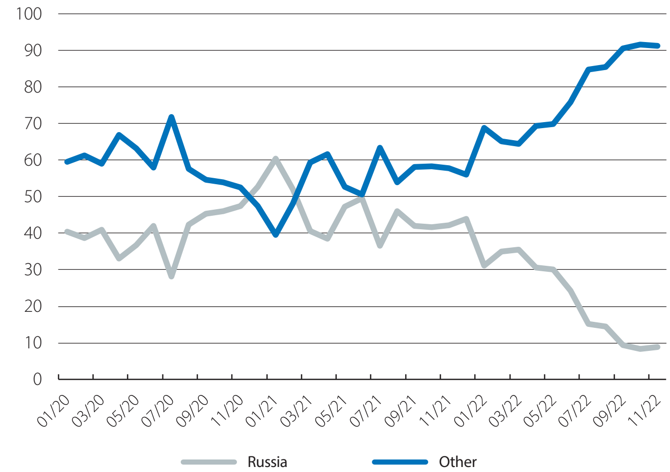
The euro area begins the year with an encouraging outlook for Q1 2023. In fact, in February the PMIs exceeded the critical 50-point threshold in the major economies (Germany, 50.7; France, 51.7; and the euro area, 52.0). This development was driven by the marked improvement in confidence in the services sector (clearly in expansionary territory), given that confidence in manufacturing fell yet again (the eighth consecutive month at contractionary levels). The PMI price component in the euro area, meanwhile, fell yet again and reached 16-month lows, although it remains very high. This reinforces the view there will be greater inertia in inflationary pressures than had been hoped for, and the data corroborate this outlook: euro area headline inflation has been falling from its October highs (10.6% vs. 8.5% in February) thanks to the decline in the energy component, while the pressures in the core components continue their slow but steady upward trickle, with core inflation (excluding energy and all food) peaking in February at 5.6%. In this context of high inflation, the growth in wage demands has stabilised at around 4.0% year-on-year at the end of last year, according to the indicator produced by the ECB. Despite the good performance of the economy in Q1 2023, it is premature to assume we will see a significant rebound in economic activity after the spring, given the major challenges the region still faces. Although gas prices have fallen substantially, they are still double their pre-war value. In addition, the ECB has made it clear that it will

Economic Surprise Index *
Level



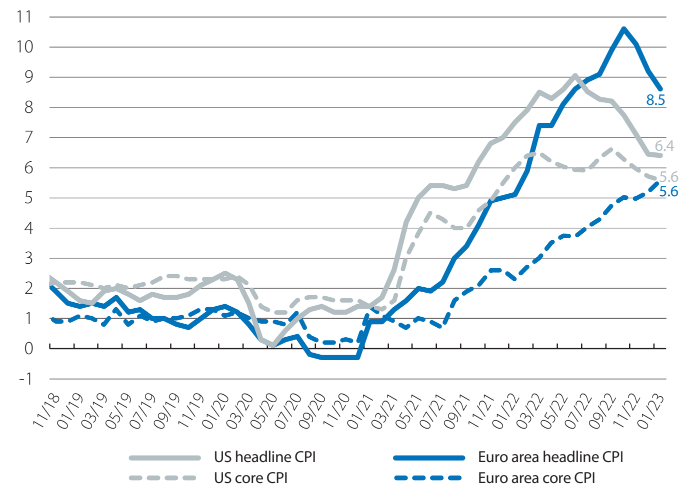
Notes: *Defined as the weighted historical standard deviations of the differences between the published data and analysts' expectations. A positive value indicates that the published data was better than expected, while a negative value suggests that the release disappointed.*
Source: *CaixaBank Research, based on data from Citigroup, via Refinitiv.*

EU: gas imports
(% of the total)



Source: *CaixaBank Research, based on data from Eurostat.*

US and euro area: CPI
Year-on-year change (%)



Source: *CaixaBank Research, based on data from Eurostat and the Bureau of Labor Statistics.*

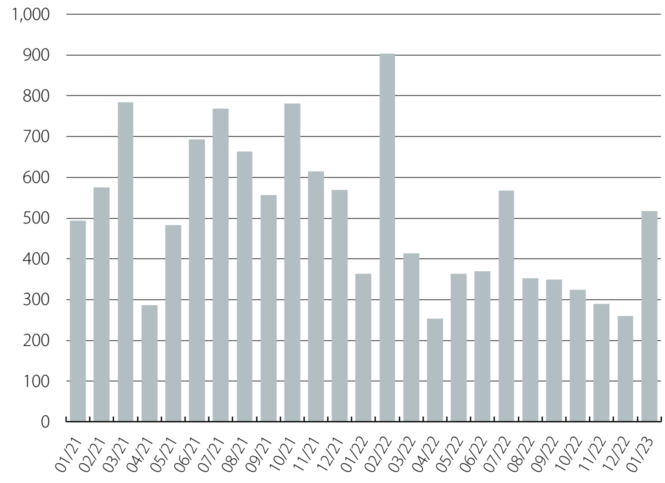
continue to raise interest rates, with the consequent restriction on activity this entails.

A surprisingly buoyant start to the year in the US. After registering a far from negligible annualised growth rate of 2.7% in Q4 2022, the latest indicators have shown significant strength at the beginning of 2023: retail sales growth in January (3.0% month-on-month) offset the cumulative decline in the previous two months; manufacturing output managed to grow by 1.0% on a monthly basis in January; the same month also saw the creation of more than 500,000 jobs, and the PMI surpassed the critical 50-point threshold in February for the first time in eight months. In this context, inflation continued to fall in January, in both the headline index (6.4%) and the core index (5.6%), albeit at a slower pace than in previous months. This scenario of positive surprises in economic activity, with inflation still at relatively high levels, helps to explain the recent messages from the Fed emphasising that interest rates will continue to rise.

Russia performs better than expected in 2022, despite the sanctions. The Russian statistics office announced that the economy contracted by 2.1% in 2022, which is compatible with a growth of 0.5% quarter-on-quarter in Q4 2022. However, the start of 2023 is unlikely to be so rosy as the impact of two of the sanctions imposed in December will begin to be felt, namely: the EU ban on imports of Russian oil and the cap on oil prices imposed by the G7. In order to counter these measures, Russia has significantly increased its sales of crude oil to China and, above all, to India, while announcing that it will cut production by around 500,000 barrels a day.

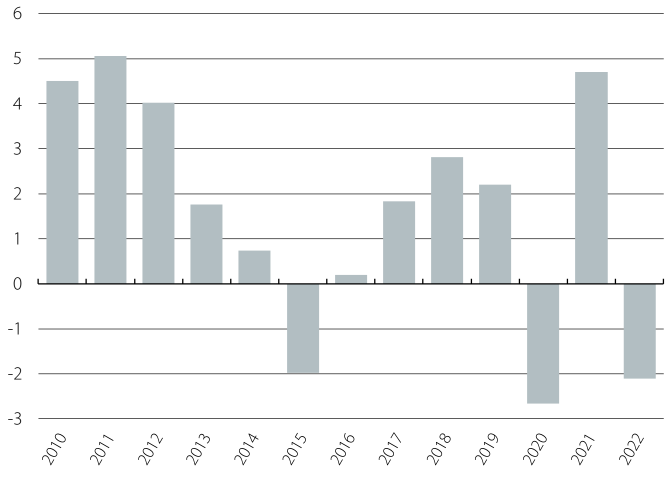
Türkiye faces the consequences of the earthquake. The recent buoyancy of the Turkish economy (it grew by 0.9% quarter-on-quarter in Q4 2022) has been abruptly interrupted by the devastating earthquake that has ravaged the south-east of the country, along the border with Syria. In addition to the irreparable cost in human lives, it has also dealt a heavy blow to economic activity, given that the area affected accounts for around 10% of Türkiye's GDP. The good news is that the damage to key infrastructure appears to be limited, and this could make it easier for the economy to make a quick and strong recovery after an initial shutdown, thanks to the reconstruction works which will cost between an estimated 6% and 10% of GDP. However, the earthquake could also have political consequences: the elections on 14 May will be held under the shadow of the earthquake's impact and the social discontent over what many consider to be a slow and inadequate reaction from Erdoğan's government. In addition, given the high number of people who have been displaced following the earthquake (some 13 million people), the feasibility of holding the elections on the planned date is beginning to be questioned.

US: non-farm payrolls
(Thousands of people)



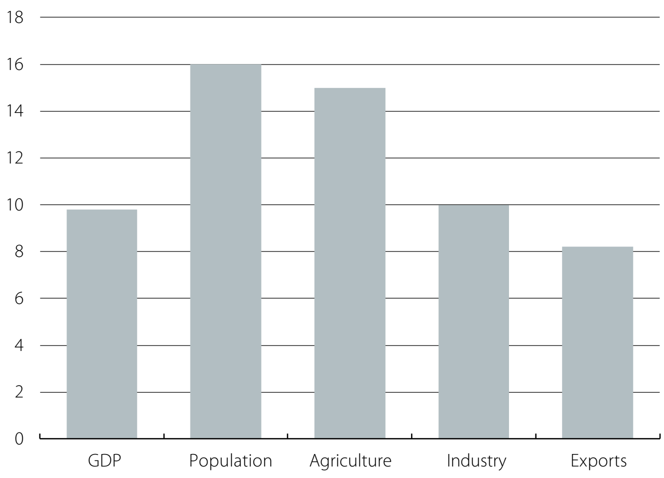
Source: *CaixaBank Research, based on data from the BLS, via Refinitiv.*

Russia: GDP
Annual change (%)



Source: *CaixaBank Research, based on data from the IMF.*

Türkiye: area affected by the earthquake
(% of country total)



Source: *CaixaBank Research, based on data published by Capital Economics.*