

Global economy

US and UK continue to drive global economic expansion

- **Global PMI hits seven-month low of 53.2 in November**
- **Strong US and UK economies contrast with malaise elsewhere**
- **Japan, euro area, China near stagnation**
- **Deepening downturns in Russia and Brazil**

Markit's worldwide PMI surveys, designed to accurately measure the pace of economic growth in advance of official data such as gross domestic product, signalled the weakest rate of global economic expansion for seven months in November.

However, divergent growth trends persisted. The US and UK markedly outperformed all other major economies, the rest of the world largely stagnating on average. Such growth divergences look set to drive exchange rate and interest rate differentials in coming months.

Global growth at seven-month low

The JPMorgan Global PMI™, compiled by Markit, fell for a fourth month running in November, down from 53.5 in October to 53.2, its lowest since April. So far, the fourth quarter of 2014 has seen the slowest average global economic growth since the final quarter of 2013, with the PMI data roughly consistent with the global economy growing at an annual rate of just over 2%.

Growth slowed closer to stagnation in China and the eurozone, business confidence in the latter being again dented by concerns over the strained relations with Russia, whose downturn deepened in November.

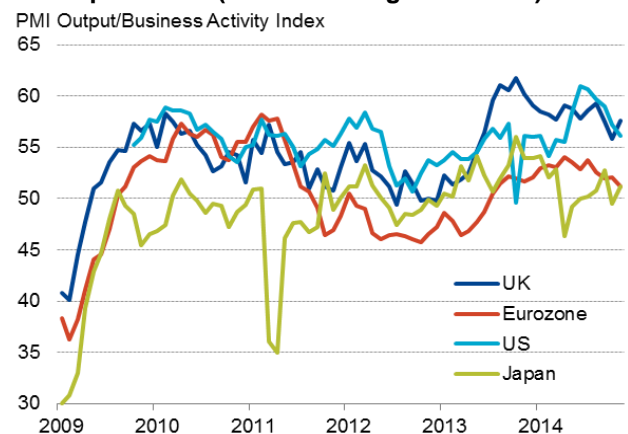
Japan meanwhile struggled to expand amid weakened domestic spending since the country's sales tax rise, and manufacturing conditions in many other Asian countries remained subdued.

The main bright lights in the global economy remained the US and the UK, though even in these countries growth has slowed compared to earlier in the year.

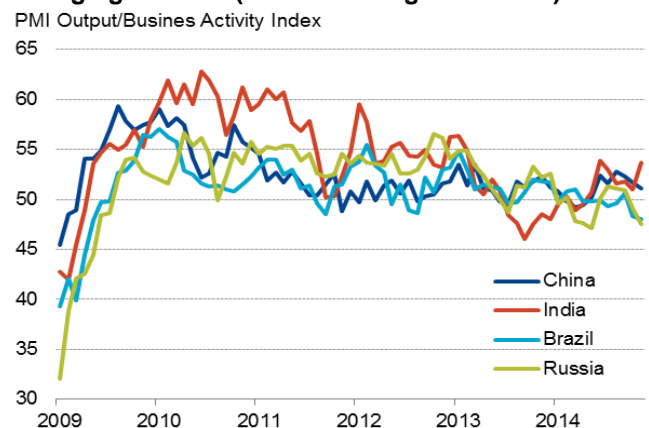
Global gross domestic product



Developed world (manufacturing & services)



Emerging markets (manufacturing & services)



Eurozone flirts with recession

The eurozone moved closer to stagnation in November, the composite PMI covering manufacturing and services sliding further to hit a 16-month low of 51.1. The PMI was more buoyant than the official data in mid-2014, but has gradually deteriorated to signal a mere 0.1% increase in GDP for the fourth quarter.

There are some bright spots within the single-currency area, notably Ireland and Spain, but the situation has deteriorated to a worrying extent in the core. France's downturn deepened further, the composite PMI falling to the lowest since February, and growth in Germany slipped to the weakest almost for a year-and-a-half. Italy is meanwhile striving unconvincingly to pull out of yet another recession, barely registering any growth in the fourth quarter so far.

Ongoing emerging market malaise

Growth in the world's main emerging markets also remained disappointing. Of the four largest emerging markets, only India saw growth pick up in November.

Growth slowed to 7.3% in China in the third quarter, its weakest since early-2009, and a fall in the weighted average of the HSBC/Markit manufacturing and services PMI surveys to a six-month low of 51.1 in November adds to the likelihood of the government failing to meet its 7.5% growth target for the year.

While Brazil pulled out of recession in the third quarter, the PMI data already point to a renewed downturn in the fourth quarter. The average PMI for manufacturing and services fell to 48.1, its lowest since May 2009.

Russia's downturn also deepened, the overall PMI falling to 47.6 as service sector business contracted at the sharpest rate since May 2009. Some respite came from an increase in manufacturing production, reflecting import substitution following the sharp drop in the ruble and trade sanctions, but the country is facing the lowest business confidence since 2009.

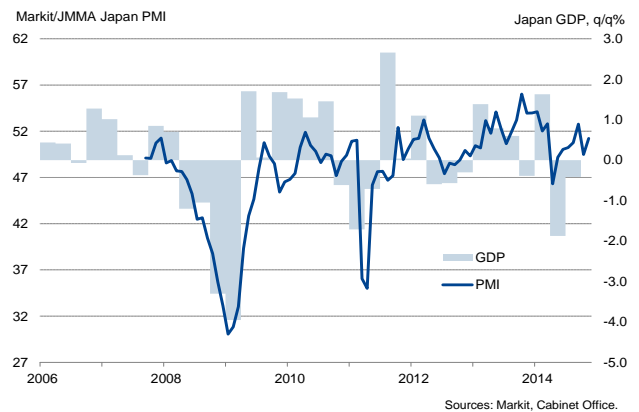
Japan flounders

Japan is meanwhile floundering after a sales tax increase tipped the country into recession. The tax hike from 5% to 8% was designed to help reduce the government deficit but proved too much for the fragile economy. Initial estimates of official data showed the economy contracting in both the second and third quarters of 2014 as spending was cut in the months following the April tax rise.

Eurozone economic growth and the PMI



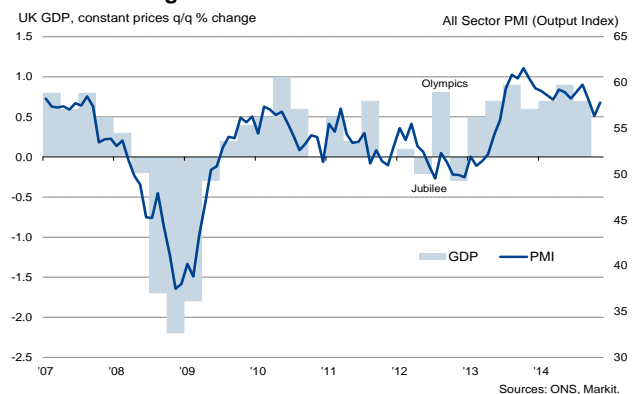
Japan economic growth and the PMI



US economic growth and the Markit PMI



UK economic growth



The PMI data have painted a brighter picture than Japan's official GDP numbers, even suggesting the economy grew in the third quarter and that manufacturing continues to expand in the fourth quarter due to exporters gaining from the weakened yen. However, the upturn is only modest and fragile. The composite PMI fell to 49.5 in October as extreme weather added to domestic consumers' headwinds, and rebounded to just 51.2 in November.

US and UK remain brightest lights

Growth therefore continues to be led by the US and the UK, with both seeing strong expansion persisting into the fourth quarter of 2014. However, in both cases growth has slowed compared to earlier in the year as the adverse global economic environment has weighed on business conditions.

After enjoying especially strong economic growth over the second and third quarters, the PMI data suggest the US economy has slowed towards the end of the year. Markit's weighted manufacturing and services PMI fell to 56.1, its lowest since April, suggesting annualised economic growth is likely to have slowed from 3.9% in the third quarter to around 2.5% in the fourth quarter. The theory that the US, with its vast domestic market and self-sufficiency on energy, has 'decoupled' from weak demand in the rest of the world is being challenged by the surveys.

In the UK, the 'all-sector' PMI rose to 57.8 after it had slumped to a 16-month low of 56.4 in October. So far, the PMI data are pointing to UK quarterly GDP growth of 0.6% in the fourth quarter (similar to the US's 2.5% annualised pace), down from 0.7% in the third quarter.

Policy divergence

Although slowing, growth in the US and UK remains robust by historical standards, meaning speculation will continue to intensify about the timing of interest rate hikes in both countries. That said, the slowdowns and recent falls in oil prices point to any initial tightening being delayed until the second half of 2015.

In contrast, the ongoing travails in the eurozone, Japan, China and other emerging markets suggest policymakers there will need to continue to seek ways to revive growth in these economies.

Such policy divergences will no doubt continue to drive exchange rate differentials, the US dollar having already strengthened sharply against the euro and yen

in particular (the dollar index has risen 11% since July, climbing to its highest since March 2009). That is unless, off course, growth continues to wane in the US and UK, as these two bright lights succumb to the headwinds of weakened demand elsewhere in the world and geopolitical risks.

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