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What to watch: Companies on a trade war footing, the Fed's wishful Xmas cut and 2024 going in the books as a record year for insolvencies

Ludovic Subran
Chief Economist
ludovic.subran@allianz.com

Maxime Darmet
Senior Economist
maxime.darmet@allianz-trade.com

Françoise Huang
Senior Economist
francoise.huang@allianz-trade.com

Maria Latorre
Sector Advisor
maria.latorre@allianz-trade.com

Maxime Lemerle
Lead Advisor for Insolvency Research
maxime.lemerle@allianz-trade.com

Philippine Renaudie
Research Assistant
philippine.renaudie@allianz-trade.com

In summary

Companies on a trade war footing. Despite a brief boost as exporters rush to get in orders before higher tariffs kick in, global trade growth is likely to slow in 2025-2026. We now expect global trade in volume to grow by +2.8% in 2025 (-0.2pp from our previous forecast) and +2.3% in 2026 (-0.5pp). In USD value terms, the downside revisions to our forecasts are even larger, with growth reaching +2.3% in 2025 (-1.7pp) and +4.1% in 2026 (-0.8pp). Marine cargo and trade data confirm that exporters are frontloading shipments (Chinese exports were up +6.7% y/y in November, supported by orders from the US (+8% y/y)) and air cargo is also skyrocketing (+9.8% y/y in November). Ultimately, factors such as FX adjustments and upcoming free-trade agreements may bring a little relief to global trade but they are unlikely to neuter the impact of the renewed trade war.

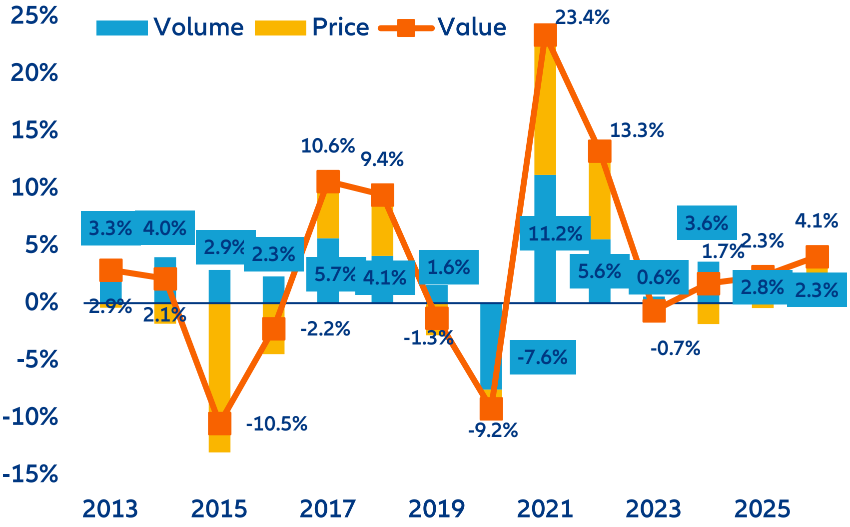
The Fed's wishful Xmas cut. Though a close call, we think the Fed will deliver its third consecutive rate cut next week. Since June, measures of underlying inflation have remained stuck at around +3.3/3.2% y/y and have even accelerated on a sequential month-on-month basis. At the same time, the unemployment rate is picking up, though primarily driven by strong labor force growth rather than weakening job growth. Persistent inflation and wage pressures suggest that the natural rate of unemployment may be a bit higher than the Fed's current estimate of 4.2%. In this context, we think the Fed will eventually have to accept a higher unemployment rate to tame inflation. Looking ahead, tight immigration policy and tariff hikes could increase inflationary pressures in 2025. We thus expect the Fed to pause rate cuts at the January meeting, before delivering a final 25bps cut for the year in March, pushing the Fed funds rate to the 4-4.25% range.

2024 going in the books as a record year for insolvencies. Insolvencies of companies with over EUR50mn in turnover hit a new record high in Q3 2024 at 127 cases, +17 compared to Q2 2024 and +42 compared to the pre-pandemic average of 82 over 2017-2019. Additionally, the combined turnover of insolvent major companies has increased by +48% y/y to EUR40bn. Western Europe leads the rebound in the number of cases, but the Americas are home to the biggest cases. In terms of sectors, services and retail have been hit the hardest, particularly in Western Europe and North America, along with construction, especially in Western Europe and Asia. With 344 cases recorded in the first three quarters, this year's total of major insolvencies already exceeds those for 2015 to 2019, 2021 and 2022. Lingering economic uncertainty, structural changes in sectors and the reshaping of supply chains and global trade could certainly push the final count of major insolvencies to a new record in 2024, raising the risk of a domino effect on suppliers and subcontractors.

Companies on a trade war footing

With the return of President Trump and a trade war looming, we now expect slower trade growth in 2025-2026. After a recession in value terms in 2023, global trade will see a moderate rebound in 2024, likely growing by +3.6% in volume terms (roughly matching the average pace over 2011-2019, Figure 1), helped by companies restocking and households renewing purchases of durable goods while reducing spending on services. The end of the year will also likely be supported by companies rushing to ship goods in anticipation of the higher tariffs likely to be imposed by the next US administration, and other potential disruptions in the coming quarters. This frontloading will likely remain a tailwind for global trade in the first half of 2025, before the effects of a renewed but contained trade war[1] are felt from the second half of 2025 and in full in 2026. As a result, we now expect global trade in volume to grow by +2.8% in 2025 (-0.2pp from our previous forecast) and +2.3% in 2026 (-0.5pp from our previous forecast). In terms of export prices in USD terms, the deflationary environment observed since 2023 will likely continue into 2025 as exporters partly take on the impact of higher tariffs to maintain their market shares. As a result, in USD value terms, the downside revisions to our forecasts are even larger, with growth reaching +2.3% in 2025 (-1.7pp) and +4.1% in 2026 (-0.8pp).

Figure 1: Global trade in goods and services, growth (%)

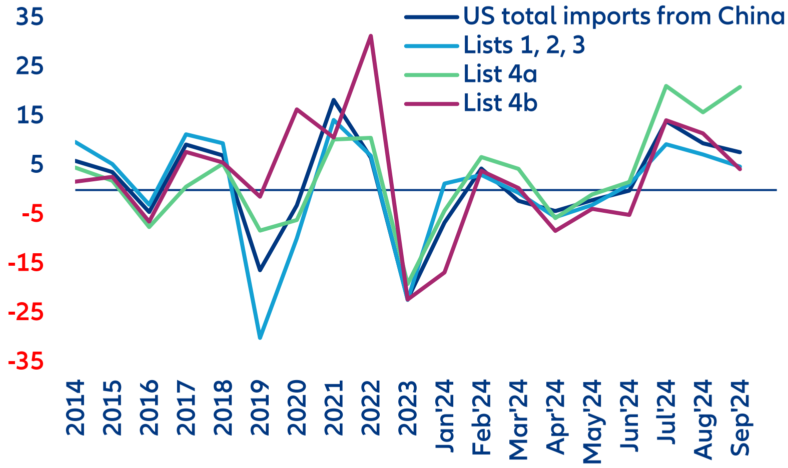


Sources: LSEG Refinitiv, Allianz Research

Marine cargo and trade data confirm that exporters are frontloading shipments ahead of the upcoming tariff hikes. Data released this week showed Chinese exports rising by a robust +6.7% y/y in November, in part supported by orders from the US (+8% y/y). In fact, US imports from China have been accelerating since this summer, rising by +10.4% y/y on average between July and September, compared with -1.8% on average in the first half of the year (Figure 2). In particular, imports of some consumer goods that were previously targeted by a tariff hike to 7.5% (still shy of the likely 25% under the new Trump administration) have outperformed, growing by nearly +20% y/y on average between July and September (vs. no growth in the first half of the year). Accordingly, since Trump's victory, shipping freight rates have increased by +14%, with companies preemptively securing deliveries in anticipation of trade uncertainty under the new US administration.

[1] *In our baseline scenario, a contained trade war consists of US measures targeted at China (with tariffs increasing to 25% on goods without critical dependencies) and modest tariff hikes on the rest of the world (to 5%), excluding Canada and Mexico.*

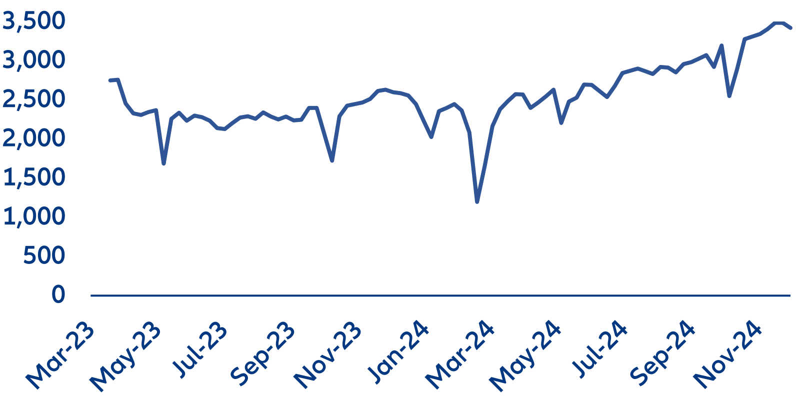
Figure 2: US imports from China %y/y



Sources: ITC, USTR, Allianz Research. Note: Lists of imports from China that were targeted during the first Trump administration: List 1 (machinery, electronics, industrial goods) with current tariff rate at 25%, List 2 (chemicals, plastics, semiconductors) at 25%, List 3 (consumer goods, furniture, textiles) at 25%, List 4a (footwear, clothing, kitchenware) at 7.5% and List 4b (smartphones, laptops, toys) at 0%.

Air cargo is also skyrocketing. The ongoing holiday season (combining both the end of the year and China's Lunar New Year in January 2025) is also traditionally the time when international cargo demand increases the most. Indeed, demand for air cargo was up +9.8% y/y in November, the 15th consecutive month of increases. Air cargo capacity grew by +5.9% overall, driven by a significant rise in international belly capacity as international air routes are experiencing exceptional traffic levels, with demand soaring +10.3% y/y. Besides the ongoing trade uncertainties and seasonality, cargo airlines have also been benefiting from rising e-commerce, evidenced in the increase in China's air cargo volume, which reached historic highs in early December, given the significant surge in its international segment (Figure 3). Between January and October of this year, international routes carried about 2.93mn tons of cargo and mail, up by a significant +48.5% from the same period in 2019, while the number of cargo flights rose by +32% y/y in early December. This growth should continue, with Chinese exports expected to accelerate in the coming months.

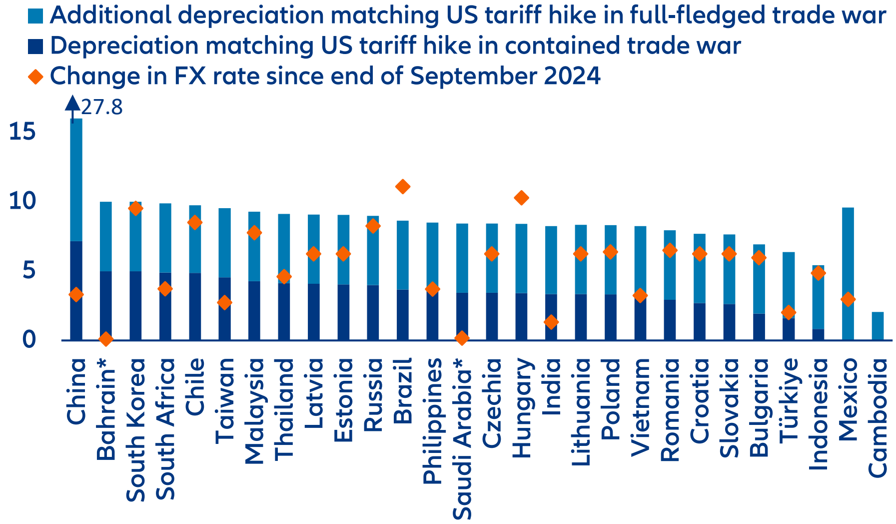
Figure 3: Number of international cargo flights in China, weekly



Sources: China's Ministry of Transport, Allianz Trade

Factors such as FX adjustments and upcoming free-trade agreements may bring a little relief to global trade in coming years but are unlikely to neuter the impact of the renewed trade war. The USD has been appreciating since the end of September, when markets started pricing in a Donald Trump victory in the US elections. In theory, a stronger USD could suggest cheaper imports for US companies and consumers. On the other hand, looming tariff hikes will increase the price tag of imports. For instance, the CNY has depreciated by -3.3% between the end of September and 11 December but it would need to depreciate by -7.2% in order to compensate for a 25% tariff applied on part of Chinese goods in the contained trade war scenario (Figure 4). Separately, for all the headlines about deglobalization and trade tensions, free-trade agreements (FTAs) continue to be negotiated and concluded around the world. For instance, since the beginning of the year, a significant number of FTAs involving China or Central Asian countries were notified to the WTO, with partners in Asia, Central and Eastern Europe and Latin America. A political agreement was also reached on the EU-Mercosur partnership on 6 December, despite France's opposition. The agreement has not yet been officially approved, but if it is, it will be the biggest FTA ever concluded by the EU, covering 780mn people and USD40-45bn in imports and exports. In addition, Costa Rica is expected to be the next candidate for the Comprehensive and Progressive agreement for Trans-Pacific Partnership (CPTPP), which now represents over 15% of the global economy. The UK will officially be joining the CPTPP on 15 December and we estimate this would generate around USD1.3bn in export gains, mainly in the machinery, automotive and pharmaceutical sectors. That being said, these gains will not offset losses from the renewed trade war, which we estimate at USD2.8bn in 2025-26 in the contained trade war scenario. The global export losses are likely to amount to USD135bn over 2025-26, or USD510bn in a full-fledged trade war (see here for more details).

Figure 4: USDLCU FX rate change since end of September 2024 and change to match tariff hikes (%)

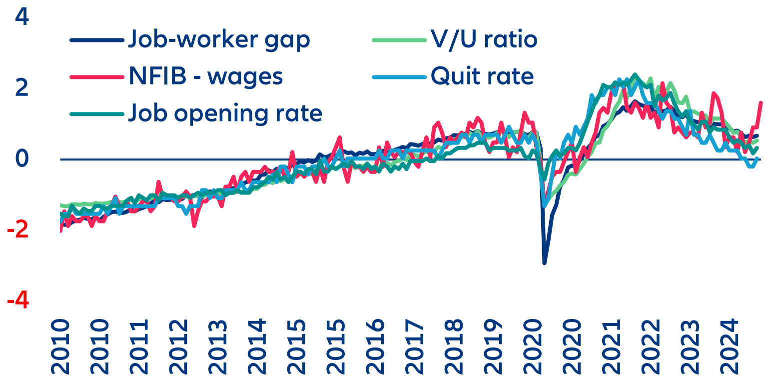


*Sources: LSEG Refinitiv, World Bank, ITC, Allianz Research. Note: Change in FX since the end of September 2024, as of 11 December 2024. * Currencies pegged to the USD*

The Fed's wishful Xmas cut

The Fed is set to deliver its third consecutive rate cut even though disinflation is stalling. The FOMC is expected to cut the Fed funds rate by 25bps to the 4.25-4.5% range next week, although we see a non-negligible risk that they pause. Financial markets are pricing in an 85% chance of a rate cut although comments from FOMC members have turned more hawkish recently. Governor Waller noted he could favor a pause if "our forecasts of slowing inflation and a moderating but still-solid economy are wrong" while Chair Powell stated that the Fed can "afford to be a little more cautious" on the speed of rate cuts. Indeed, progress on disinflation has stalled over the past couple of months. Since June, underlying measures of inflation such as core CPI inflation and the Cleveland Fed's trimmed mean CPI have remained stuck at around +3.3/3.2% y/y and have even accelerated on a sequential month-on-month basis. Moreover, the labor market looks to have stopped easing over the past couple of months (Figure 5): for instance, the private sector quit rate has stopped dropping and SMEs surveyed by the NFIB even point to higher compensation granted to employees.

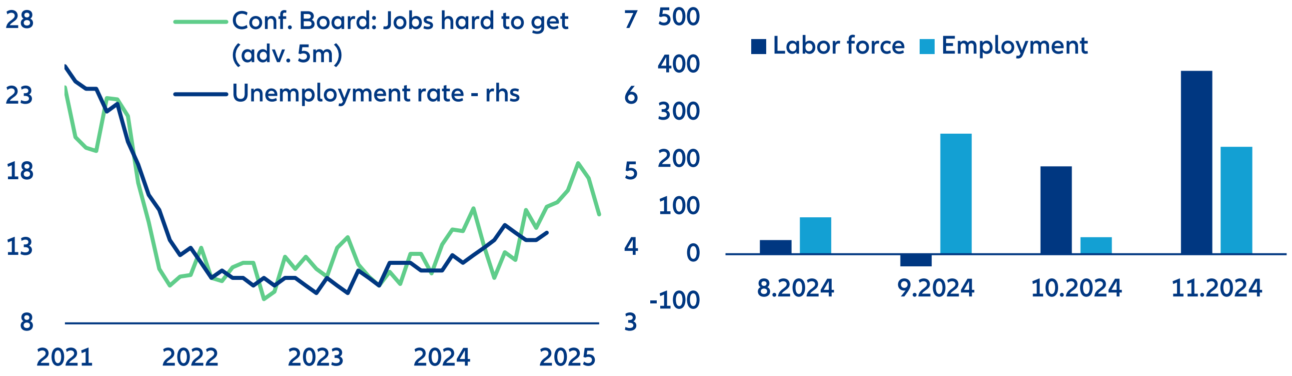
Figure 5: Measures of labor market tightness (z-score)



Sources: LSEG Refinitiv, Allianz Research. Note: V/U ratio denotes the vacancies/unemployed ratio.

The Fed will have to accept a slightly higher rate of unemployment. The start of the Fed easing cycle in September was partially justified by perceived increasing downside risks to the labor market. Admittedly, the unemployment rate has risen steadily from 3.4% in April 2023 to 4.2% in November 2024. Moreover, surveys suggest that the unemployment rate will continue to rise in the coming months (Figure 6, left). However, the pickup of the unemployment rate is primarily driven by strong labor force growth rather than weakening job growth[2] (Figure 6, right), although the strike at Boeing and the hurricanes have caused some distortions in the employment data in recent months. Strong labor force growth looks to have been caused by a renewed surge in immigration inflows, as indicated by latest data from US Customs and Border Protection. Measures of labor market tightness as well as a low private layoff rate also indicate that the Fed should not be concerned by an increasing unemployment rate. Rather, persistent inflation and wage pressures suggest that the natural rate of unemployment (i.e. the rate that brings wage growth and inflation to their steady state) may be a bit higher than the Fed's estimate of 4.2% (in November, the unemployment rate was also 4.2%). In this context, we think the Fed will eventually have to accept a higher unemployment rate to tame inflation.

Figure 6: Unemployment rate prospect (left) and employment-labor force growth (000s, right)



Sources: LSEG Refinitiv, Allianz Research

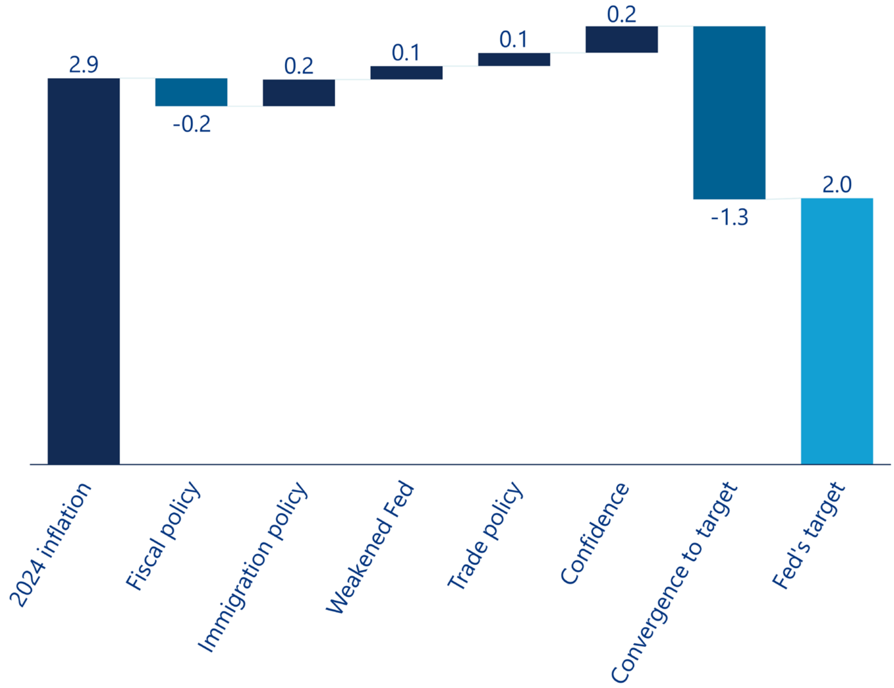
Looking ahead, we expect a persistently challenging inflation environment in 2025 to prompt the Fed to end its cutting cycle in March 2025. Some of the next administration's policies – notably tight immigration policy, tariff hikes and attacks on the independence of the Fed or attempts to influence its interest rate decisions – could contribute to keeping inflation above target in 2025[3] (Figure 7). Moreover, an expected strong economy in early 2025 buoyed by rising household confidence and loose financial conditions may also contribute to sustain inflationary pressures. On the other hand, tighter fiscal policy induced by spending cuts (tax cuts are expected in

[2] *Given the current unreliability of job data in the Household survey in capturing new immigrants, we proxy the labor force by summing job data from the Establishment survey and unemployment data from the Household survey.*

[3] *Although we expect the Fed to remain independent and committed to its dual mandate, the perceived weakening of its independence may push up inflation expectations and, in turn, actual inflation.*

2026) should provide a partial offset. In all, the return to the 2% target looks challenging in 2025, although much will depend on the timing and the exact content of the policies President Trump rolls out in his second term. We expect the Fed to pause rate cuts at the January meeting, before delivering a final 25bps cut for the year in March, pushing the Fed funds rate to the 4-4.25% range.

Figure 7: Inflation boosting and moderating factors expected in 2025 (CPI measure, annual average, %)

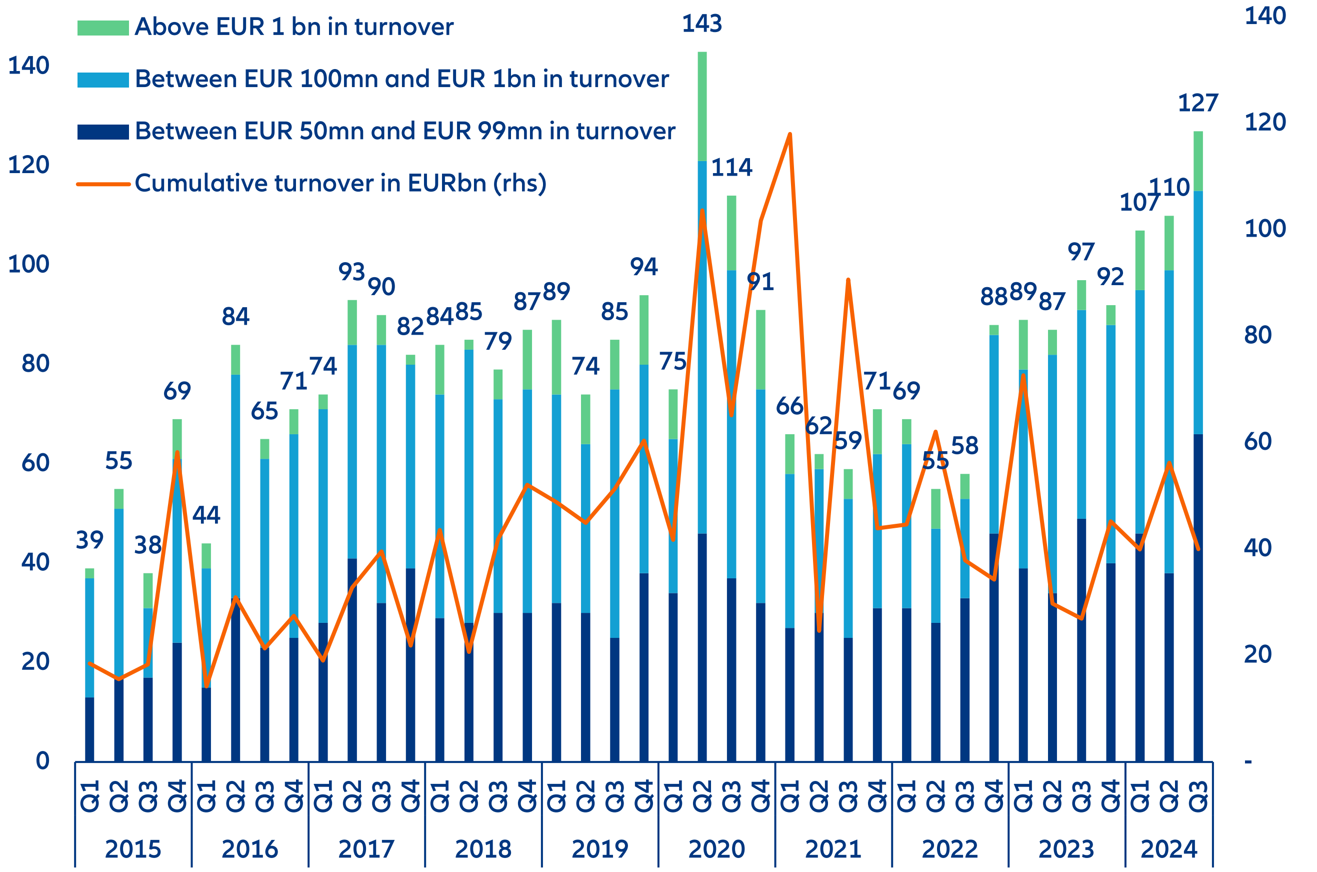


Source: Allianz Research

2024 going on the books as a record year for insolvencies

Insolvencies of companies with over EUR50mn in turnover hit a new record high in Q3 2024, with more than one case per day. The number of global major insolvencies jumped to 127 cases in Q3 2024, +17 compared to Q2 2024 and +42 compared to the pre-pandemic average of 82 over 2017-2019. This marks the second-largest quarterly total since the start of our monitoring in 2015. Year-to-date, major insolvencies have increased by +26% y/y, totaling 344 cases over the first three quarters of 2024. Additionally, the combined turnover of insolvent major companies increased by +48% y/y to EUR40bn, reinforcing the trend observed in Q2. Year-to-date, the combined turnover has risen +5% to EUR136bn, with the average turnover totaling slightly below EUR400mn. For comparison, between 2015 and 2019, the combined turnover reached EUR463mn. Moreover, significant cases such as HNA and Evergrande in China contributed to boosting the combined and average turnover of major insolvencies in 2020 and 2021.

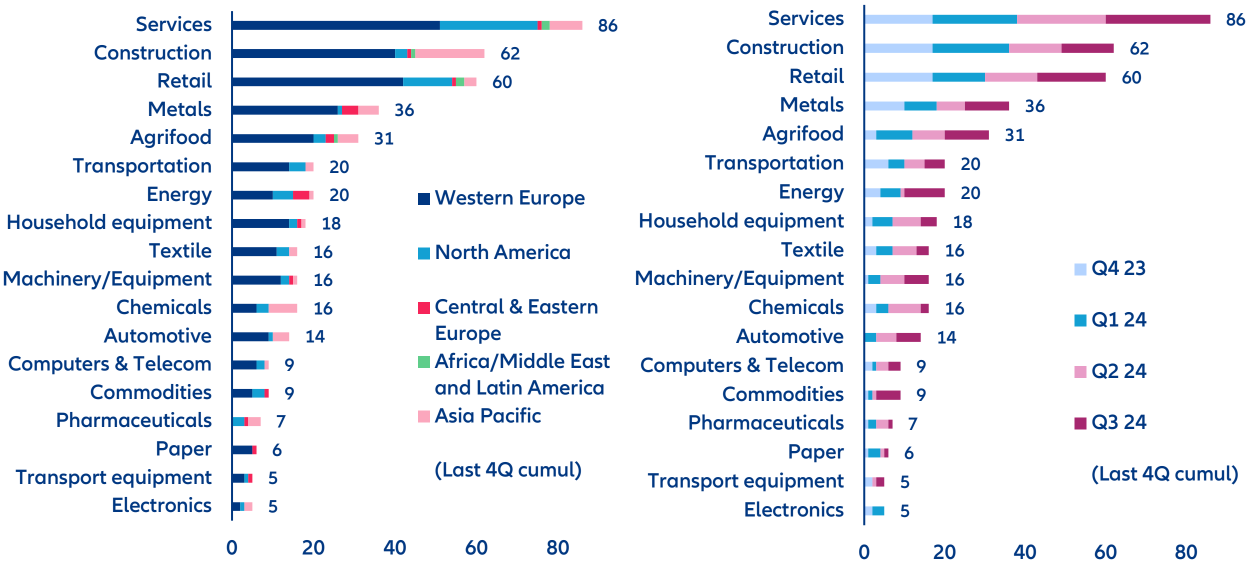
Figure 8: Major insolvencies, quarterly number, by size of turnover



Source: Allianz Trade

Western Europe leads the rebound in the number of cases, but the Americas are home to the biggest cases. In Q3, Western Europe played a key role in the rebound in major insolvencies in y/y terms (+30 cases y/y to 91). North America and Asia stand out with an almost stable number of cases y/y (both -1 to 13 and 12 cases, respectively). Year-to-date, the picture remains broadly the same, with Western Europe leading North America (+81 cases and +7, respectively), and with Central and Eastern Europe, Latin America and Asia experiencing declines (-2, -5 and -7, respectively). Western Europe accounts for six out of 10 cases overall, with 276 out of the 436 cases reported over the last four quarters, followed by North America (73) and Asia Pacific (62) as key contributors to the overall count. Notably, the US remains at the forefront with the highest number of top insolvencies, with seven out of the top 10 insolvencies in Q3 2024 and nine out of the top 20 insolvencies since the start of the year, ahead Western Europe (five) and China (five) for the second quarter in a row.

Figure 9: Major insolvencies, last Q4 numbers, by region (left) and by sector and quarter (right)

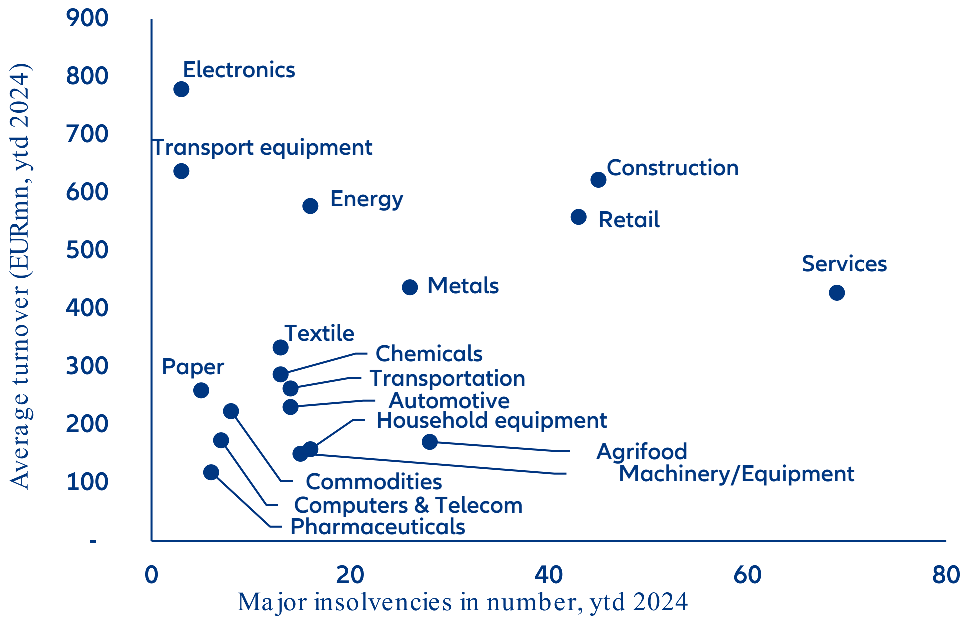


Source: Allianz Trade

Services and retail have been hit the hardest, particularly in Western Europe and North America, along with construction, especially in Western Europe and Asia. The three sectors that contributed the most to the global count were all in Western Europe: services (18 cases), retail (13), and construction (9). Asia had its largest number of cases in services (3) and construction (3), while the US recorded large insolvencies in services (3) and energy (3). Interestingly, the top affected sectors remained the same when looking at the three quarters together, with 69, 43 and 45 cases recorded globally, respectively. In Q3, insolvencies of companies with turnover exceeding EUR1bn remained elevated (12 cases, following 11 cases in Q2 2024, compared to an average of eight cases for the 2015-2023 period). Looking at the last three quarters (Figure 10), electronics stood out with the largest severity in terms of turnover (EUR779mn on average), followed by transport equipment (EUR638mn), construction (EUR623mn), and energy (EUR578mn).

2024 is already set to be a record-high year for major insolvencies. With 344 cases in the first three quarters, this year's total already exceeds those for 2015 to 2019, 2021 and 2022. A further 80 cases are now all that are needed to surpass the previous record set in 2020, which seems quite possible considering that this number is lower than the quarterly average posted since 2015 and that large companies are facing significant challenges, particularly in Europe. These include the overall economic situation but also structural changes in their sectors and the reshaping of value chains and global trade. In addition to the consequent risk of jobs being lost, this surge in large insolvencies also increases the risk of a domino effect on suppliers and subcontractors.

Figure 10: Major insolvencies by sector, number of cases (x axis) and average turnover (y axis, EURmn), year-to-date 2024 (Q1/Q2/Q3)



Source: Allianz Trade

These assessments are, as always, subject to the disclaimer provided below.