

Global economy

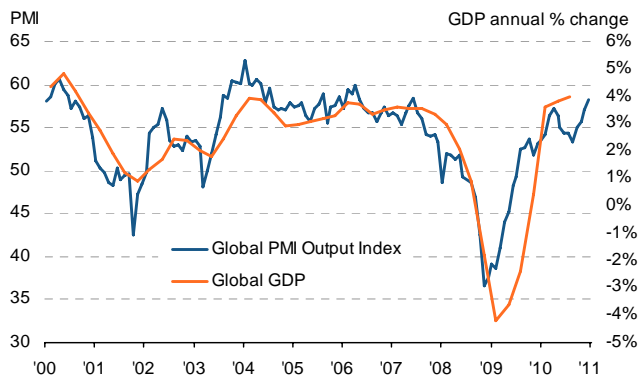
Global economic growth hits post-crisis high, led by developed markets

January saw global economic growth continue to recover strongly from the slowdown seen in the third quarter of last year. However, while fears of double-dip recessions have eased, worries about inflation have intensified, especially in emerging nations.

Global GDP surges at start of 2011

Global economic growth surged higher in January to reach the fastest since April 2006, according to the JPMorgan Global PMI (compiled by Markit). Both manufacturing and services have rebounded convincingly from slowdowns seen in the third quarter of last year. Although manufacturing growth remains below the near-record peak seen early last year, services growth was the strongest since June 2007. This encouragingly points to a more balanced global recovery than was seen in 2010.

Global economic growth



Sources: Markit, JPMorgan.

Manufacturing v. services output

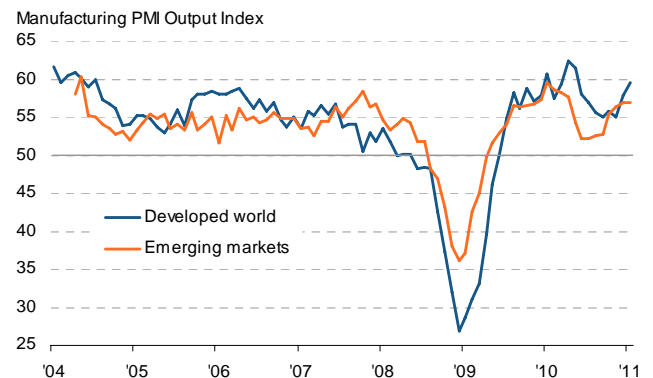


Sources: Markit, JPMorgan.

Developed markets lead global upturn

The acceleration in global growth is being driven by stronger expansions in developed economies. Growth in the developed markets picked up to a near-five year high in January, while the pace of expansion in emerging markets slowed. The divergent trend is of particular note in the manufacturing sector, as many governments in the developed world look to re-balance their economies towards production industries.

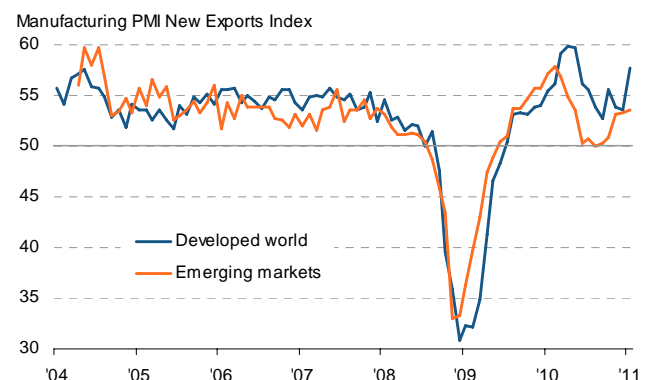
Emerging and developed market manufacturing



Source: Markit

In many developed nations, export orders are the key driver of growth. Ultra-low lending rates in a number of these nations have led to capital flows into higher yielding emerging markets, leading to an appreciation of many of their currencies. As a result, exports from developed markets have become more competitive.

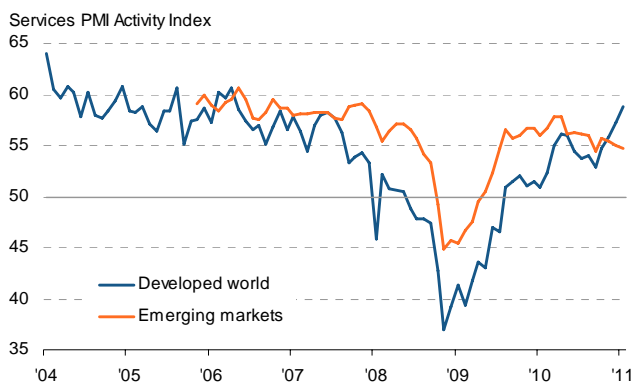
Emerging and developed market export orders



Source: Markit

The PMIs also provided evidence that differences in monetary policy are having an impact on domestic demand for services. Loose policy in the US is likely to have been the key to stronger non-manufacturing growth in recent months, helping boost the developed world's services activity growth to the fastest since April 2006. In contrast, growth slowed in the emerging markets, pulled down by the Chinese service sector in particular, where policy tightening caused activity and confidence levels to slip closer to the lows seen in the recession.

Emerging and developed market services

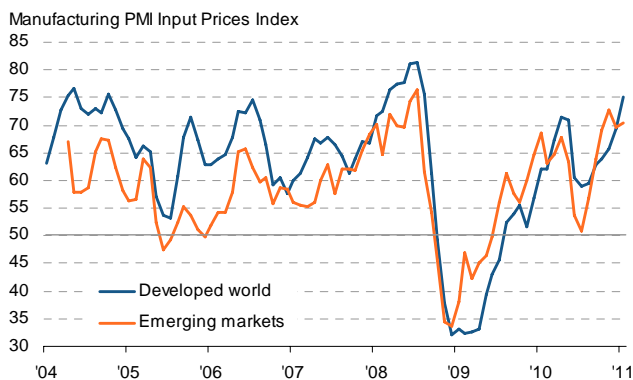


Source: Markit

Inflationary pressures build

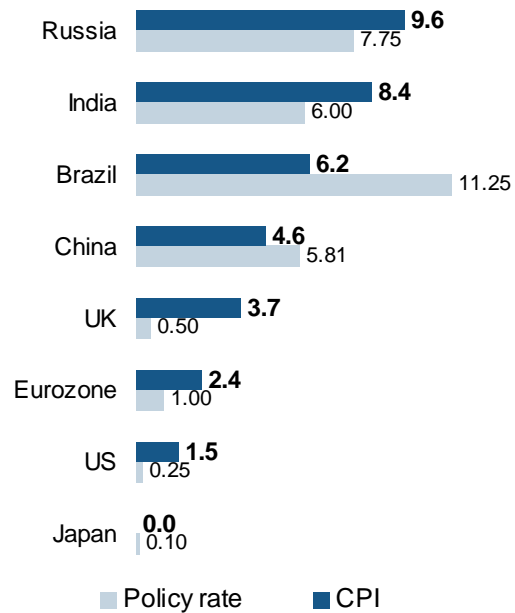
Faster growth has also brought rising price pressures, however, with the Global Manufacturing PMI's Input Prices Index hitting a two-and-a-half year peak in January. Price rises for many foods, metals and oil are feeding through to consumer price inflation, especially in emerging markets, where food accounts for a larger proportion of the retail basket. However, inflation has also jumped higher (above central bank targets) in the UK and Eurozone.

Manufacturing prices



Source: Markit

Consumer price inflation and policy rates



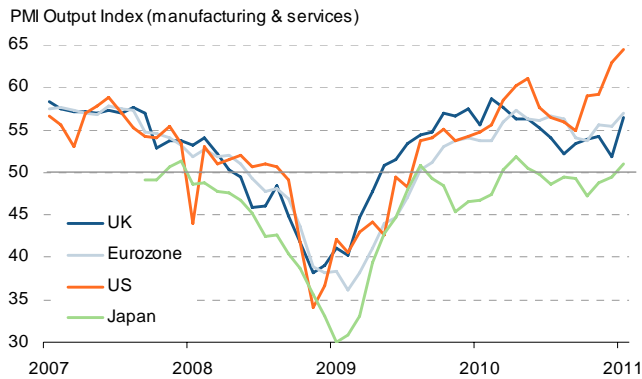
Many emerging markets' central banks, such as China, India, Indonesia and Russia, are attempting to control inflation through non-standard means other than higher interest rates, as they seek to prevent currency appreciation, which has been blamed by many for the worsening export trend compared to the developed world.

In Europe, price pressures have also risen while PMIs have moved up to levels which could trigger rate rises. While the ECB is considered unlikely to hike soon due to worries about the periphery, the expectation is growing of a hike as early as May by the Bank of England. Analysts have begun to consider a possible tightening of US policy towards the end of 2011, but in all cases, developed world policy remains far looser than in most important emerging markets as many governments struggle with stubbornly high unemployment.

US leads developed world growth

Looking at country performance in more detail, national PMIs showed that all 'G4' developed economies (the UK, the US, Japan and the Eurozone) reported stronger output growth, with the US leading by a wide margin. In fact, the pace of expansion in the US private sector was the strongest since April 2006. The UK saw a reassuring bounce-back from a snow-affected December and even Japan surfaced from contraction.

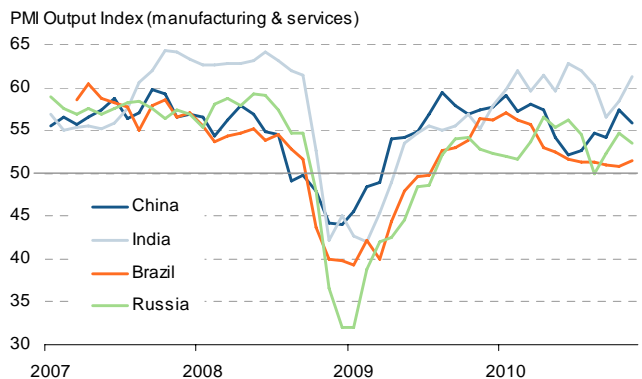
G4 economic growth



Sources: Markit, ISM.

Trends were more mixed among the emerging BRIC economies. Growth slowed in China, leaving India to report the strongest rate of increase. Although Brazil saw a slight acceleration of growth, it posted only a fractional pace of expansion that was the weakest of the BRIC nations.

BRIC economic growth

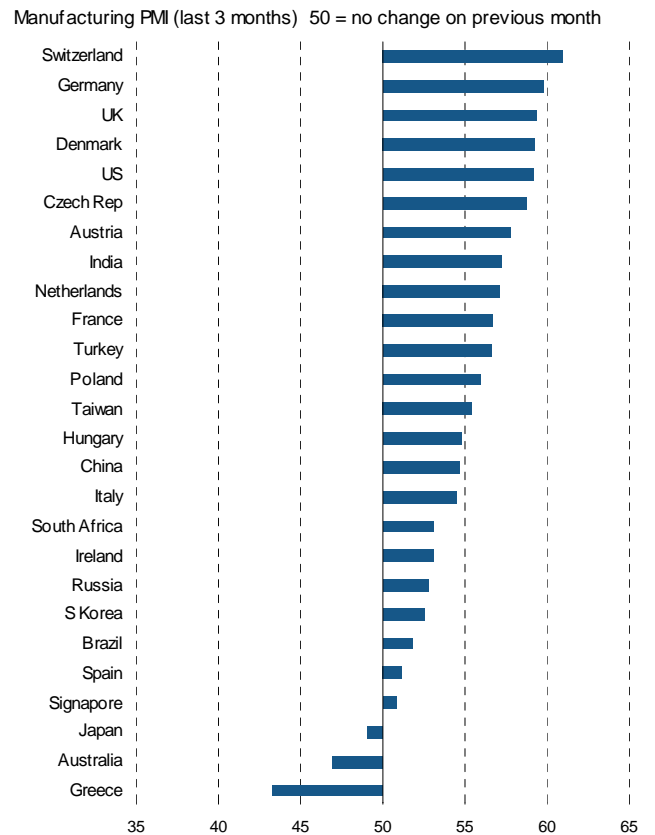


Sources: Markit, HSBC.

Manufacturing growth centred on developed markets

Reflecting the strong performances of developed nations, the top of the manufacturing growth league table was dominated by Western Europe and the US in January. The UK recorded the strongest rise in manufacturing output in 16 years, while growth in the US and Eurozone accelerated close to their post-recession peaks. Weak performances in Greece and Spain were notable exceptions to the generally improving trend in developed markets.

Manufacturing in three months to January



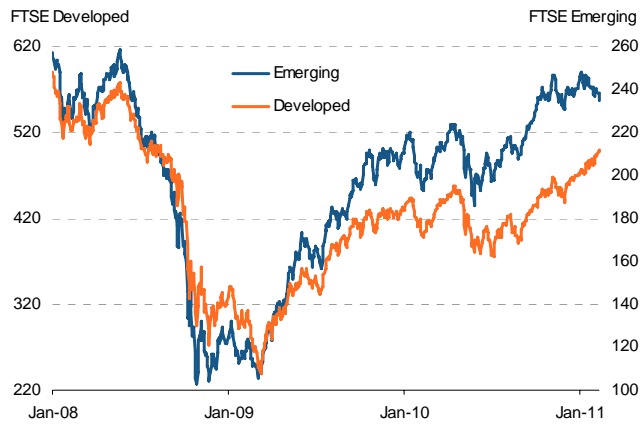
Sources: Markit, JPMorgan.

Developed world equities outperform emerging markets

The improvement in the economic news flow in January drove investors out of the safety of government bonds into equities, pushing the FTSE All-World Index to its highest level since June 2008. However, with signs that demand is cooling in emerging nations, and increasing nervousness about 'hard landings' (which could be caused if authorities are forced to ratchet up interest rates to control inflation) emerging market equities have underperformed the developed world so far this year. Bombay is down some 12% and Brazil 6%. The US, in contrast, has rallied over 4% and the Eurozone almost 7%.

According to the FTSE All-World Indices, developed world stocks are up 4.8% so far this year while emerging market stocks are down 4.6%.

FTSE Developed and emerging indexes



Source: FTSE

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