Global Economy

2018, a year that started better than it ended

Expansión (Spain)

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After a year (2017) that had been very positive for the world economy, especially in light of the strong recovery in international trade, the start of 2018 augured well for the year thanks to the momentum from 2017 and the cyclical coming together of the three major regions, USA, Europe and China. The U.S. had recently approved a tax reform, and in February it launched an expansive spending programme which, although it was considered unnecessary given the advanced stage of its economic cycle, was to prolong growth for several more quarters. Europe had come through the dreaded 2017 electoral cycle without veering off into extremes, and still presented plenty of room for growth, with the unemployment rate above its natural level and investment needs on several fronts. At the National Congress of the Communist Party of China in October 2017, China had initiated a shift in its economic policy, placing more stress on the “quality” of growth rather than on the “quantity”, which was another way of saying concentrating more on macroeconomic imbalances and structural reforms and managing a soft landing economy.

The first half of 2018 fitted relatively well with a pattern of synchronised growth. However, problems soon arose with what was to prove one of the main recurring themes of the year, which strained relations among the three major blocs and has been one of the main sources of uncertainty: protectionist pressures from the US administration. Since the beginning of 2018, pressure on China has been increasing, with progressive rises in import duties on a growing proportion of its exports to the US, and with threats of still further increases (to 25% on more than half of all its exports) if an agreement is not reached in March 2019. Pressure on Europe, which included a threat to increase import duties on cars, was halted with the June truce between Messrs Trump and Juncker, although tensions could resurface at any time.

The second crucial factor characterising 2018 was the normalisation of monetary policy by the ECB and, especially, by the US Federal Reserve, which by raising interest rates in step with the evident cyclical improvement in the economy, led to turbulence in emerging markets in the spring. While volatility and financial tensions were at minimum levels and a degree of normalisation was more than to be expected, the impact on countries with greater external imbalances such as Argentina and Turkey was considerable, although the good news was that there was no systemic crisis in emerging markets.

The second half of the year showed signs of weakness. It had been evident since the beginning of the year that growth in Europe was not going to be able to keep up the pace of 2017, but in the third quarter of 2018 it slowed sharply, with a temporary halt in automotive production for adaptation to the new emission standards, but also due to the uncertainty associated with protectionism, reduced demand from China, unresolved problems relating to Brexit and Italy’s fiscal defiance of the European Union. China suffered a clear slowdown, difficult to quantify exactly with its statistics, but which led to the approval of repeated monetary stimulus, liquidity and fiscal measures to soften the landing. And in the US, the tax reform does not seem to have stimulated investment as its promoters hoped, and it is possible that its impact will die out earlier than hoped. The signs of slowdown became visible in the fourth quarter of the year. And on top of this reduced macroeconomic drive we have the falls in stock markets, especially in developed countries, and the safe haven effect on the safest assets in the past three months.

Many of these challenges remain for 2019: the protectionist threat, further rate hikes by the Fed without causing additional stresses, and reasonable resolution of the Brexit problem. These are all factors that may exacerbate the gradual slowdown that looks to be shaping up as the most likely scenario for the world economy in the next two years.

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