BBVA Research

Global Economic Watch

April 2019

Creando Oportunidades

We lower our 2019 global growth forecast due to weaker momentum across the board, but policy measures still favour a soft landing

- World GDP growth remained weak in 4Q18, weighed by a sharper than expected slowdown in the US and persistent weakness in China and the Eurozone. For 1Q19, our BBVA-GAIN model shows a slight sequential pick up in global growth to 0.8% rate, as compared to 0.7% in 4Q18.
- We lower our 2019 global growth forecast to 3.4% from 3.5% amid persistence of idiosyncratic factors, particularly in the Eurozone, and external uncertainty driven mainly by trade protectionism and Brexit.
- In the absence of "accidents", we expect reinforced policy accommodation by the Fed and the ECB alongside a step up in policy easing measures by China to enable global growth to soft land. In this context, we maintain our 2020 global growth forecast at 3.4%.
- In the US, growth will continue to lose steam in wake of fading support from fiscal stimulus and external risks. We maintain our US GDP growth forecast at 2.5% for 2019 and at 2.0% for 2020.
- In the Eurozone, weak momentum persists in early 2019 as global headwinds and more protracted one-off factors have weighed on exports orders and the industrial sector, but there are signs of stabilization. We lower GDP growth forecast to 1.0% in 2019, but it gains some ground to 1.3% in 2020 underpinned by the strength of domestic demand.
- In China, we expect the economy to soft land and maintain our growth forecast of 6.0% for 2019 given rising prospects of trade deal with the US and policy stimulus led by tax cuts and monetary easing.
- Risks to global growth stem from a larger reduction in dynamism in the economy in China or the US, a new wave of protectionist measures and the disorderly exit of the UK from the European Union.

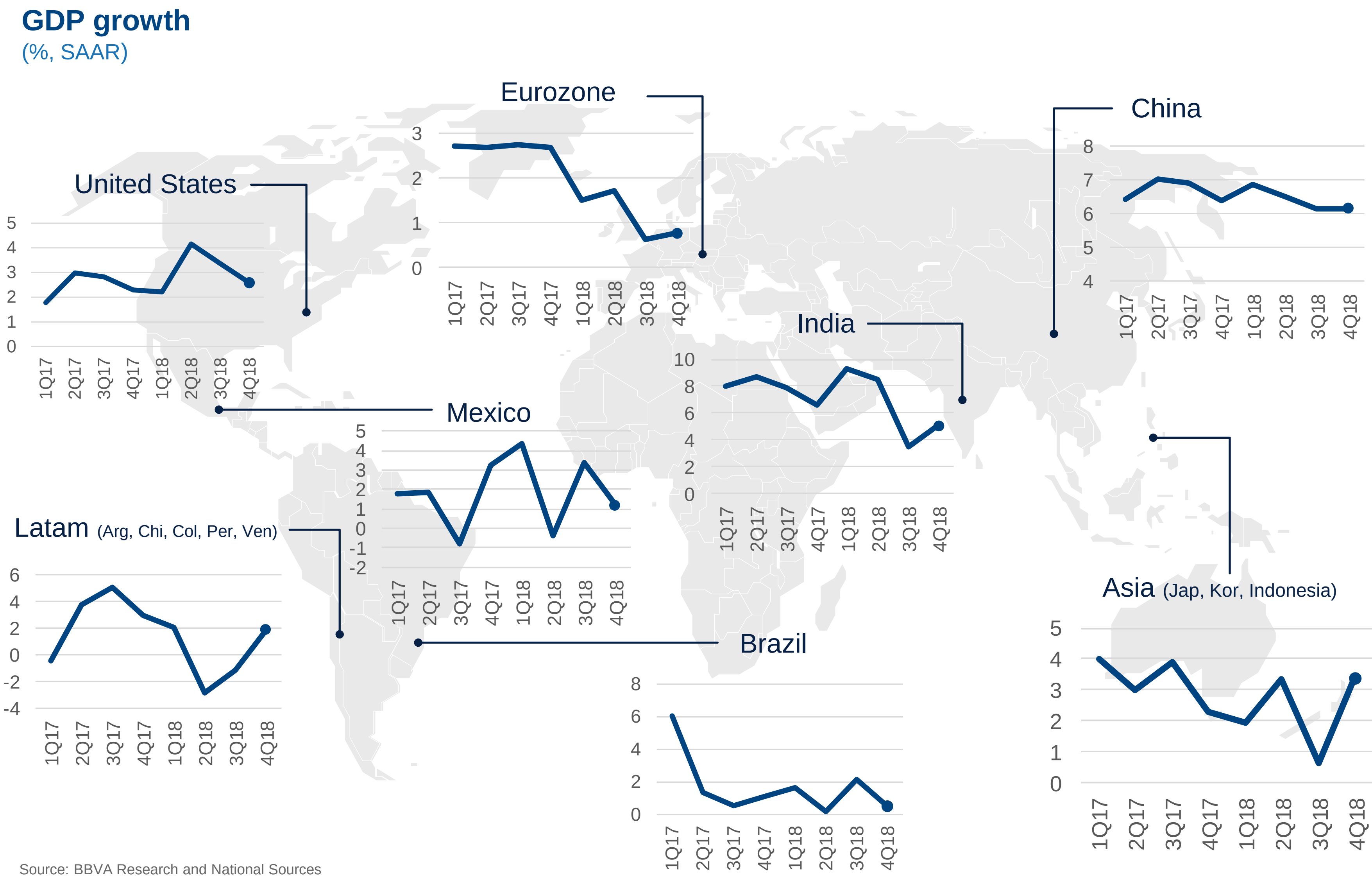
Outline

01 Short term indicators

02 New projections

01
Short term indicators

World GDP growth continued to remain weak in 4Q18 as a slowdown in the US offset a recovery in India and Japan



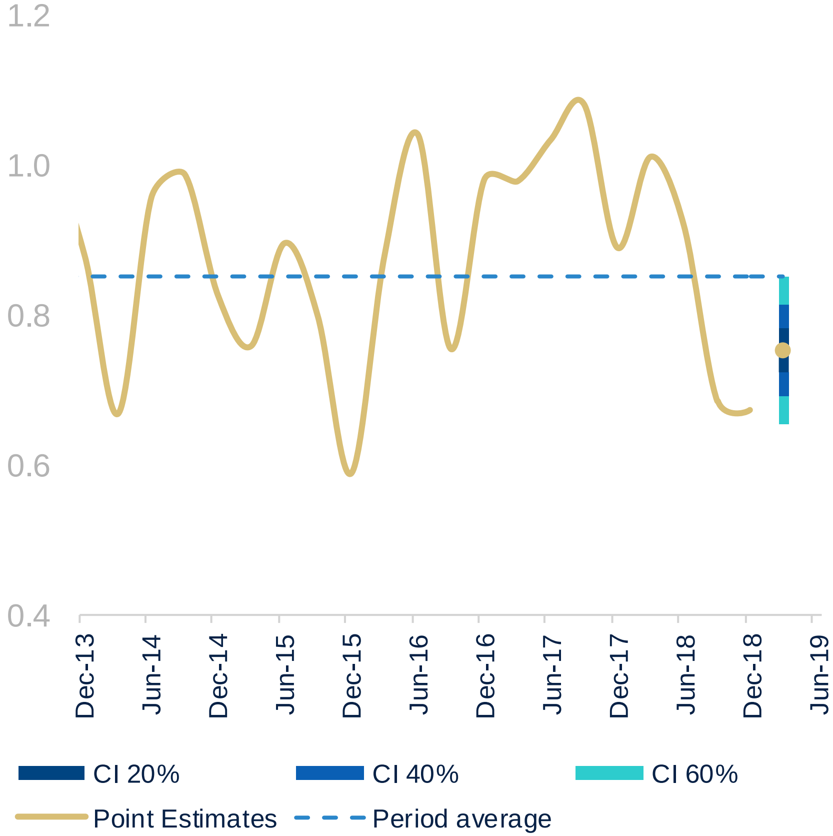
Source: BBVA Research and National Sources

While 4Q18 saw a slowdown in economic activity, our GAIN model and recent soft data seems signals a slight recovery in 1Q19

Global growth has slowed due to China's structural moderation, high uncertainty in Europe, trade protectionism and a cyclical slowdown in the US. **A recovery is possible, but activity will be less dynamic than in past years**.

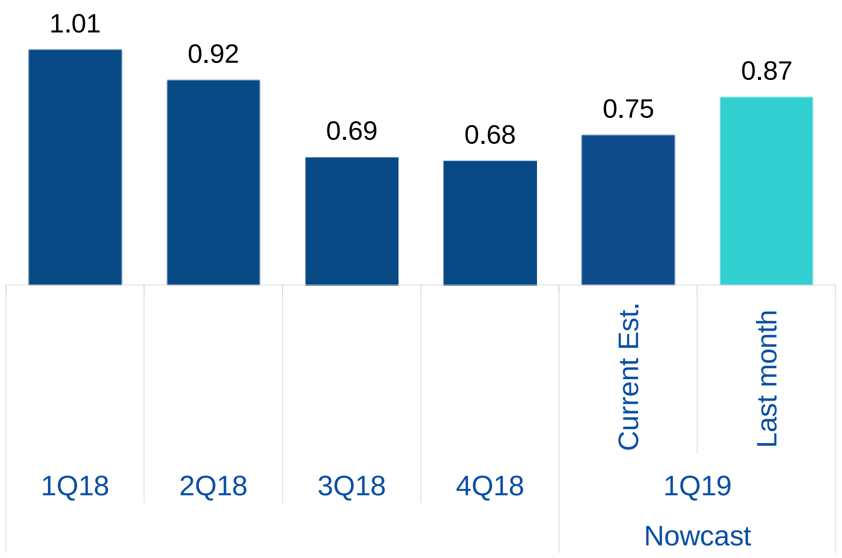
World GDP growth

(Forecast based on BBVA-GAIN (%, QoQ))



World GDP Growth

(Forecast based on BBVA-GAIN (%, QoQ))

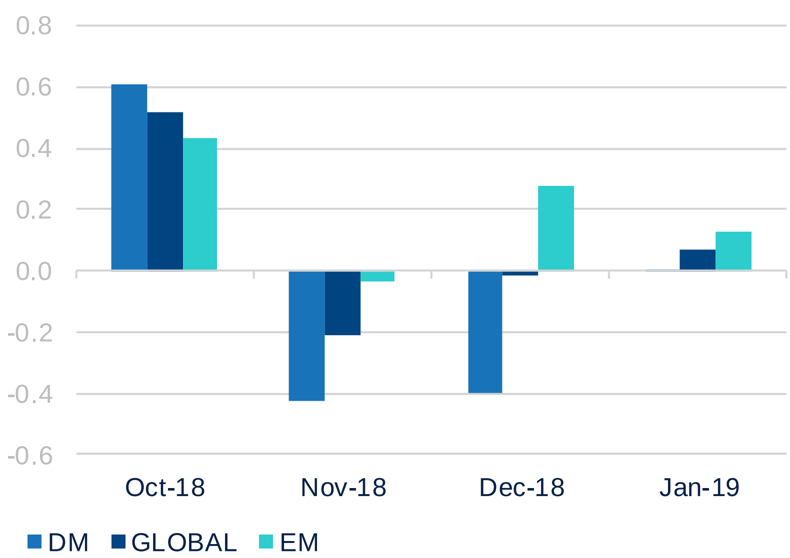


Source: BBVA Research and National Sources

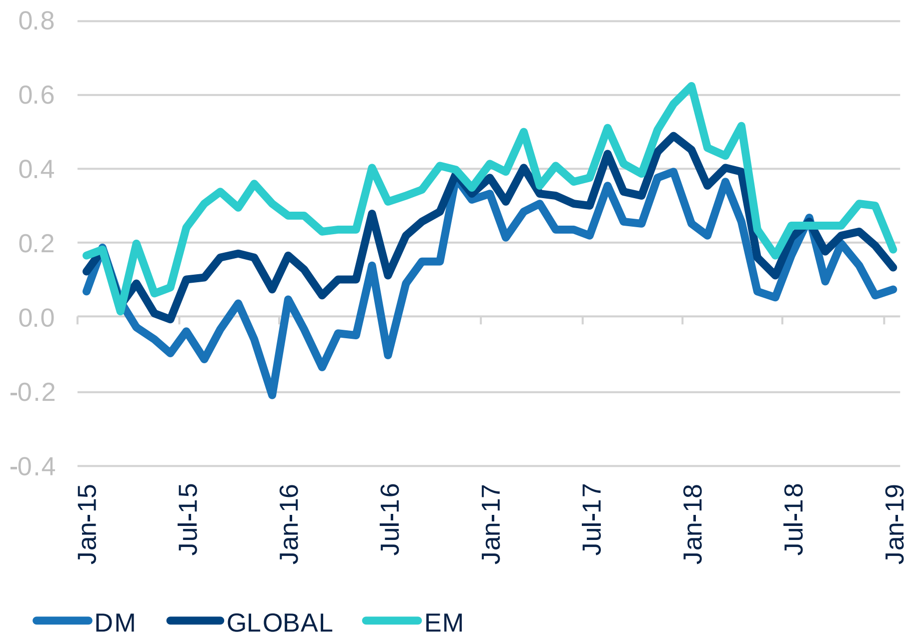
Globally, industrial production has marginally recovered, led by better performance in emerging countries

Industrial production seems to have hit the ground in developed countries but is not yet recovering. In the case of emerging countries, industrial production growth has slowed but still remains positive.

World industrial production
(%, MoM)



World industrial production
(%, 6-month moving average)



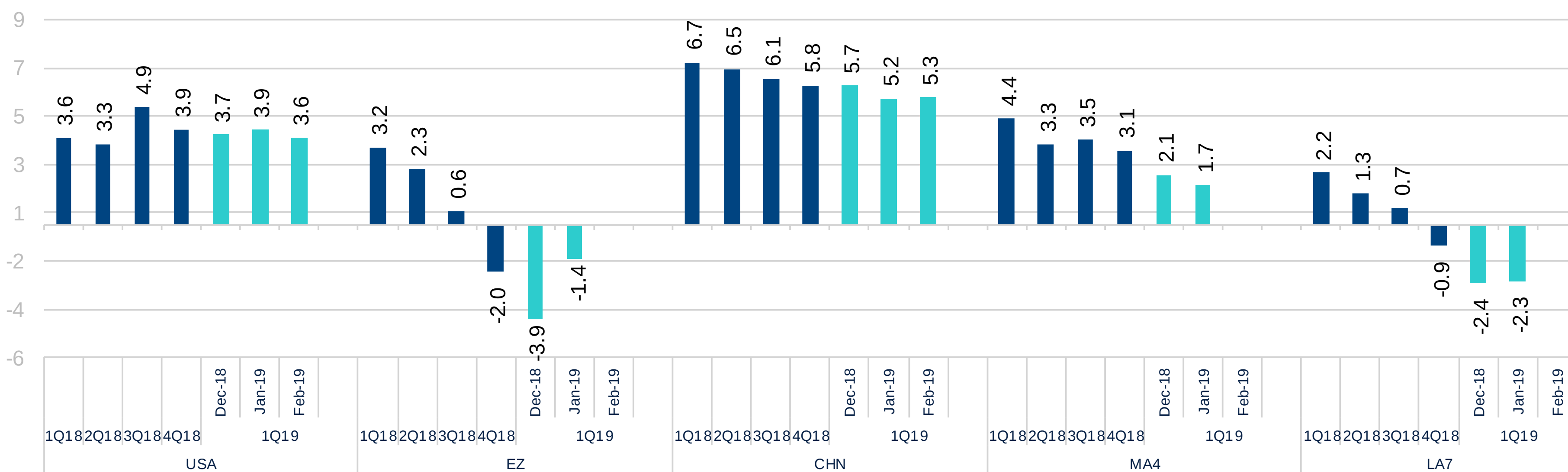
Source: BBVA Research and National Sources

Industrial production growth remains relatively robust in the US, weak in China and continues to contract in the Eurozone and Latam

The adverse impact of **new regulations on car emission standards on industrial production in Europe has been longer than expected.**

World industrial production: selected regions

(%, YoY)



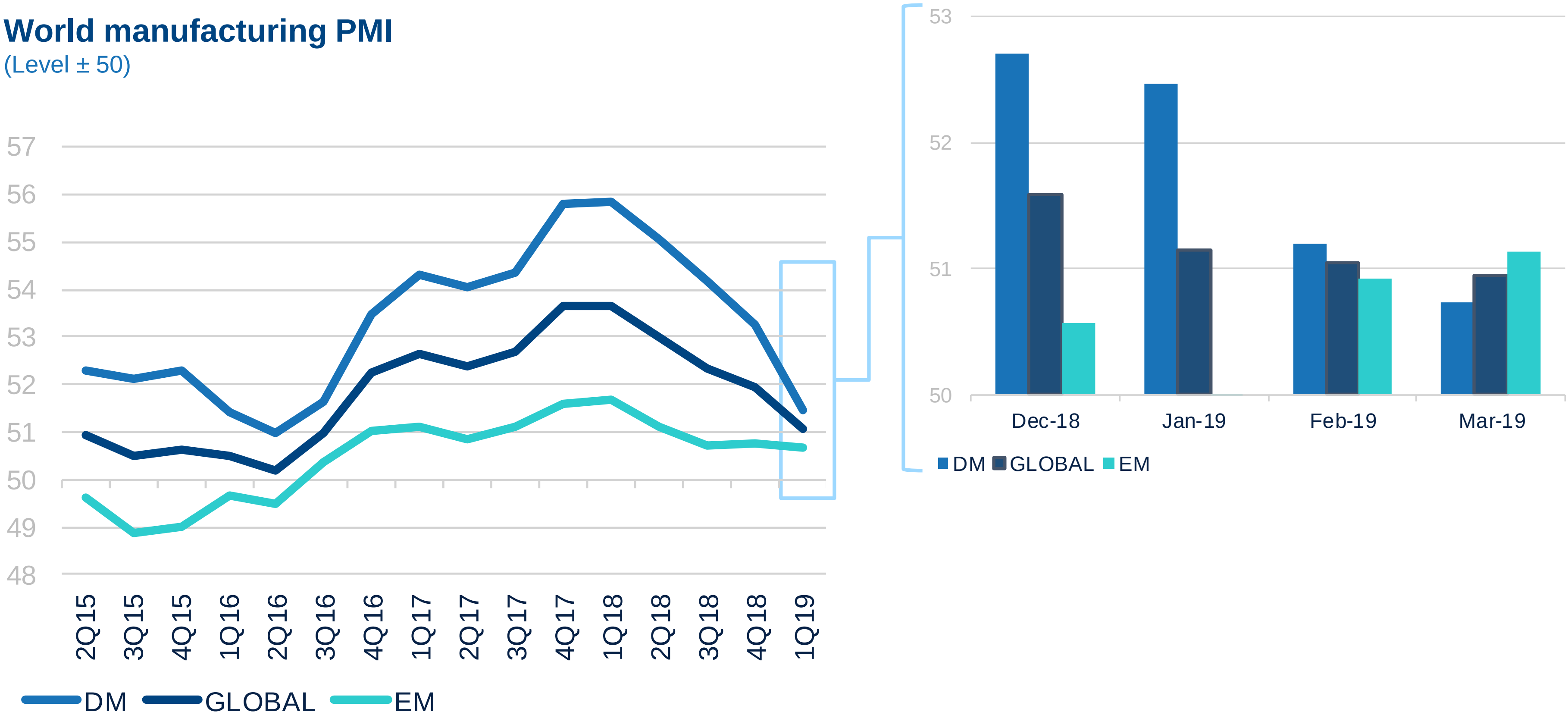
MA4: India, Indonesia, Japan and Korea

Source: BBVA Research and National Sources

Manufacturing PMIs in most developed economies continue to trend lower

Dragged mainly by slowing global demand, **most developed economies PMIs continued to trend lower. However, emerging economies saw a recovery in PMIs, led by China.**

World manufacturing PMI
(Level ± 50)



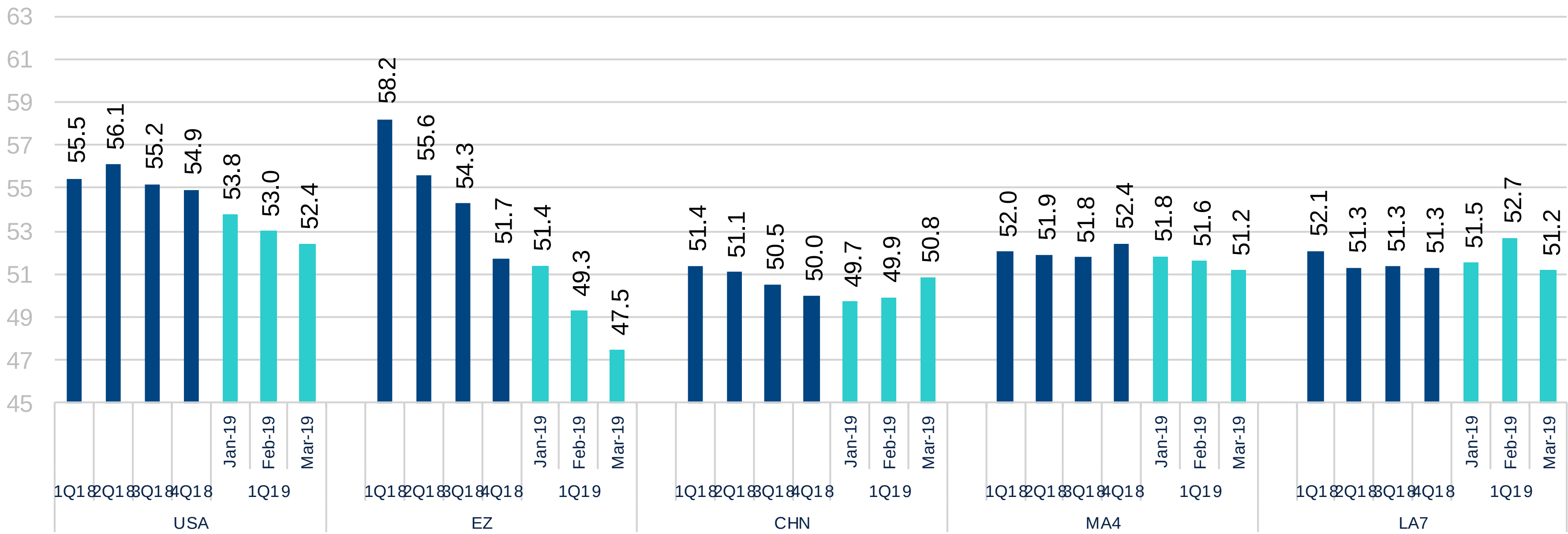
Source: BBVA Research and Markit Economics

China's manufacturing PMIs re-entered expansion territory in March while activity continued to contract in the Eurozone

Eurozone manufacturing PMI remained in negative territory, indicative of contraction in activity, for the second consecutive month in March, while China managed to return to expansion territory

Manufacturing PMI: selected regions

(Level ± 50)



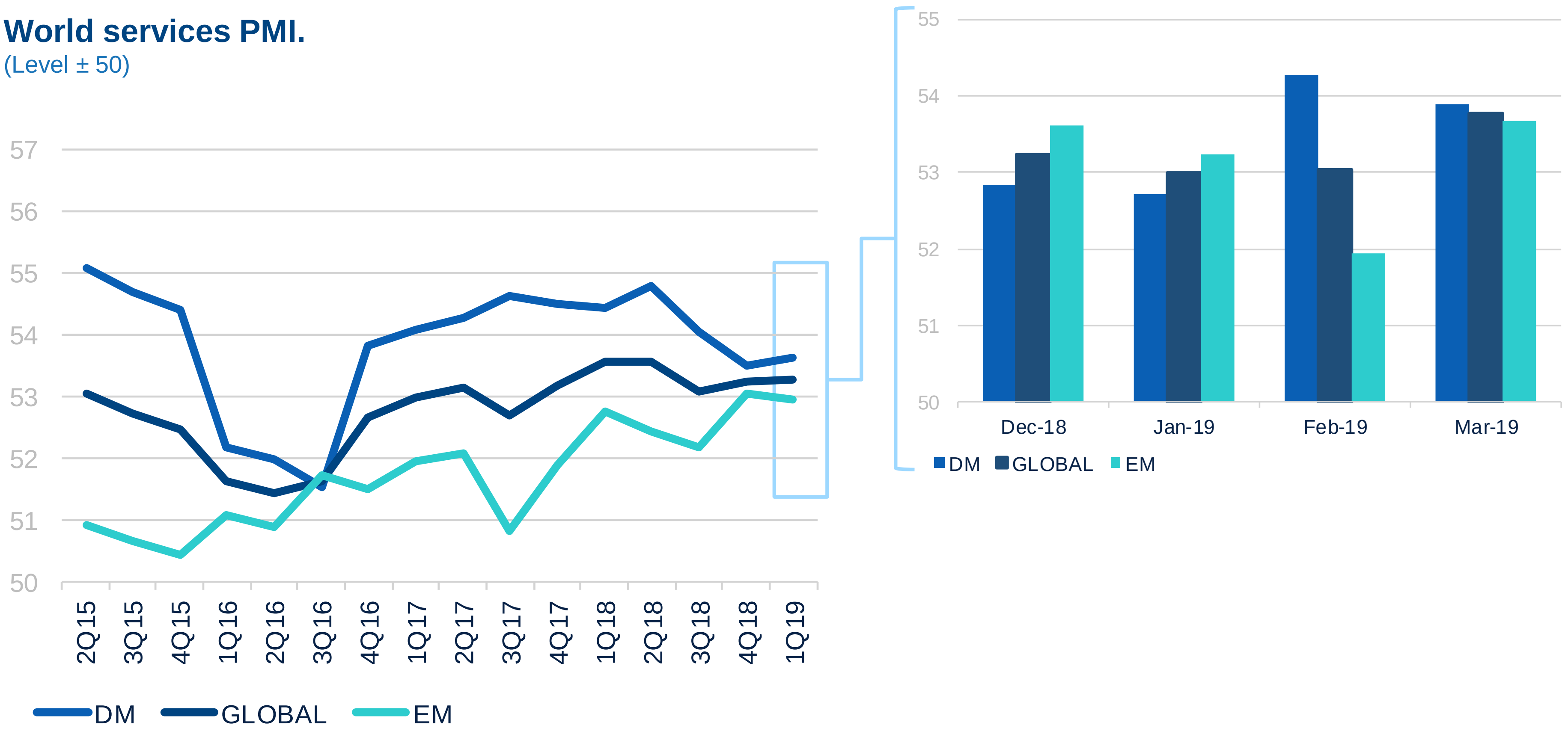
MA4: India, Indonesia, Japan and Korea

Source: BBVA Research and Markit Economics

March services PMIs fell in developed economies but picked up in emerging economies

Overall, services **PMIs still remain well above manufacturing PMIs across both economies and well within expansionary territory**, in turn reflecting resilience of the services sector.

World services PMI.
(Level ± 50)



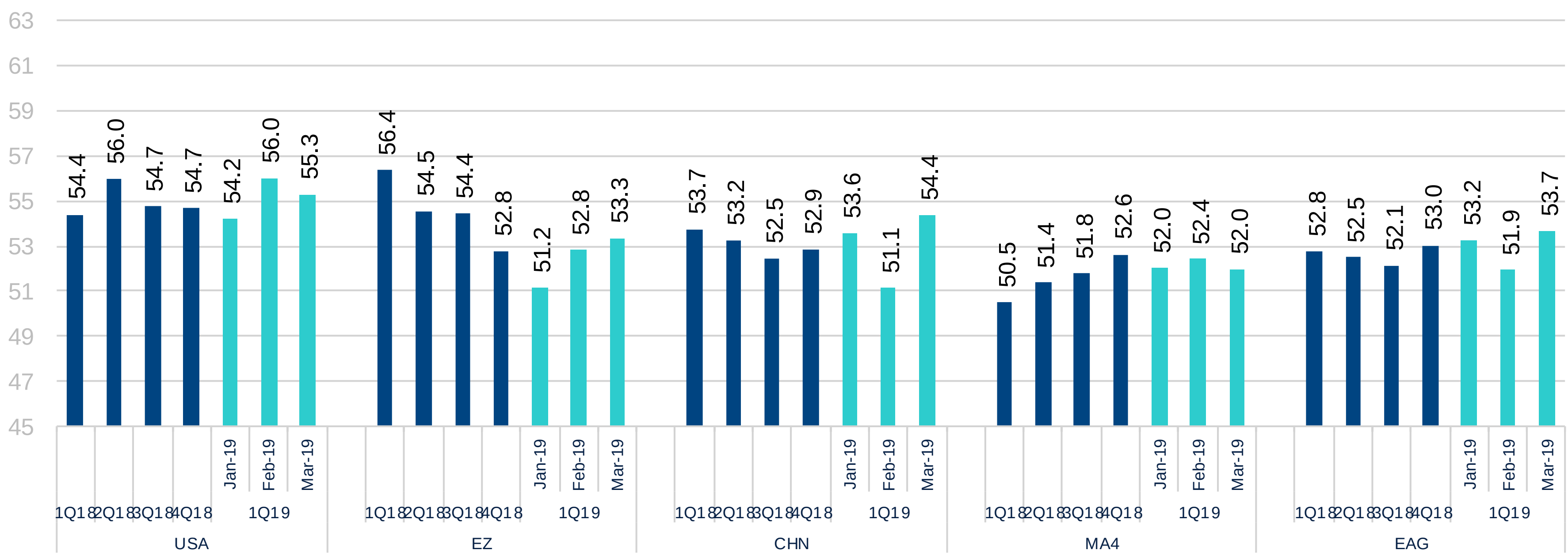
Source: BBVA Research and Markit Economics

Service PMIs rebound in China, improved further in the Eurozone but edged lower in the US

Services sector activity has held up well across most economies in wake of resilient domestic demand, with **notable rebounds seen in the China and EAG in March.** The Eurozone has seen a steady improvement.

Services PMI: selected regions

(Level ± 50)



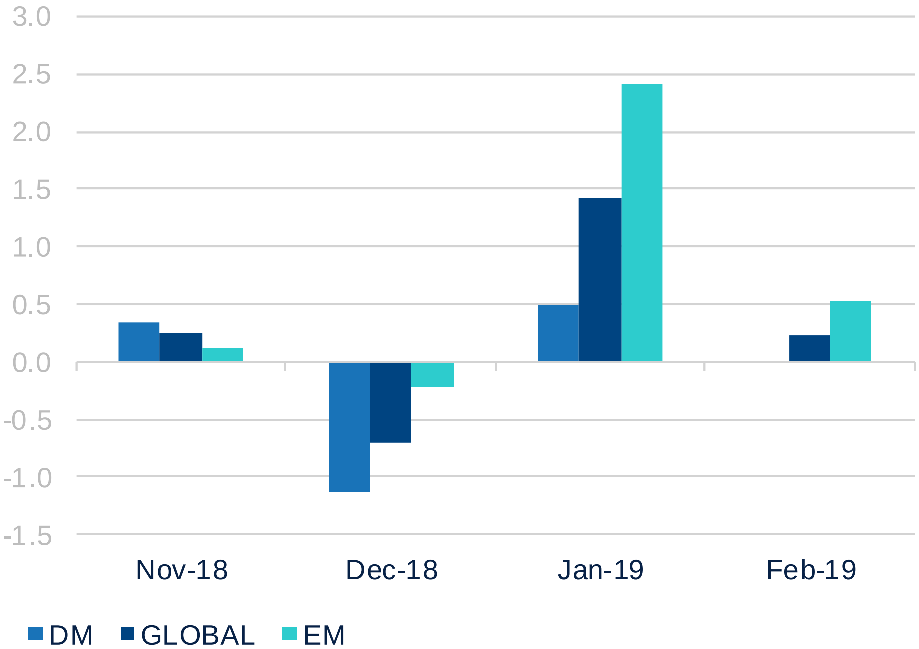
MA4: India, Indonesia, Japan and Korea
EAG: Brazil, China, Egypt, India, Indonesia, Iran, Malasya, Mexico, Philippines, Russia and Turkey.

Source: BBVA Research and Markit Economics

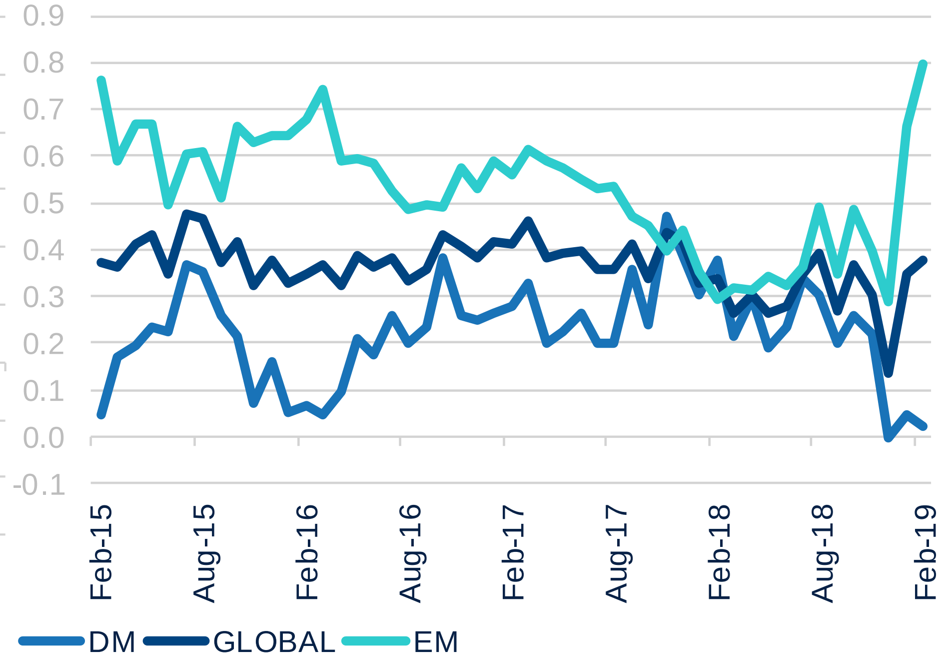
The improvement in world retail sales growth over the first two months of 2019 has been led by emerging economies

Domestic demand remains resilient despite the broader deceleration in global growth.

World retail sales
(%, MoM)



World retail sales
(%, 6-month moving average)



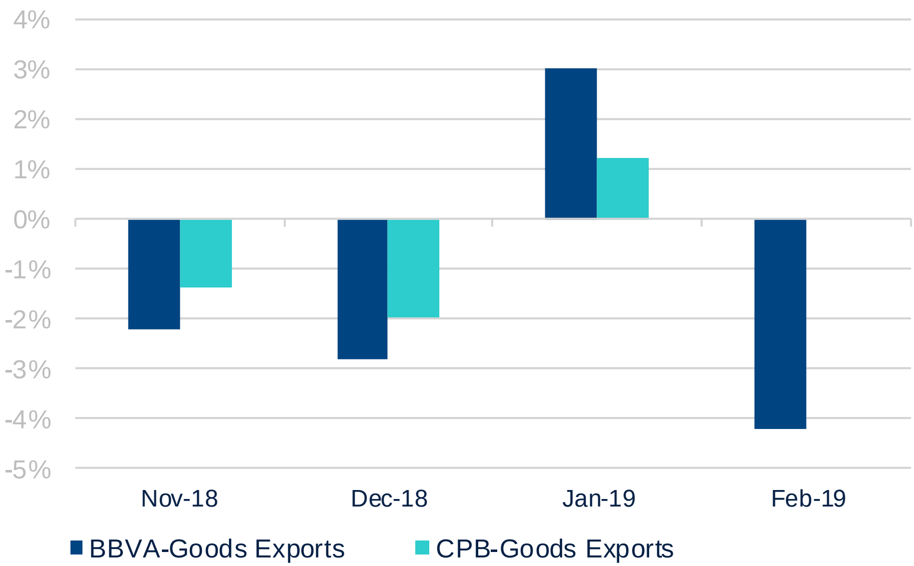
Source: BBVA Research and National Sources

Export growth rebounded in January but weakened in February. Early indicators suggest limited respite in March

The slowdown in China's economy has hampered world trade growth in recent months. **US and China are getting closer to ink a trade deal, which if it happens would provide a fillip to downbeat trade prospects**

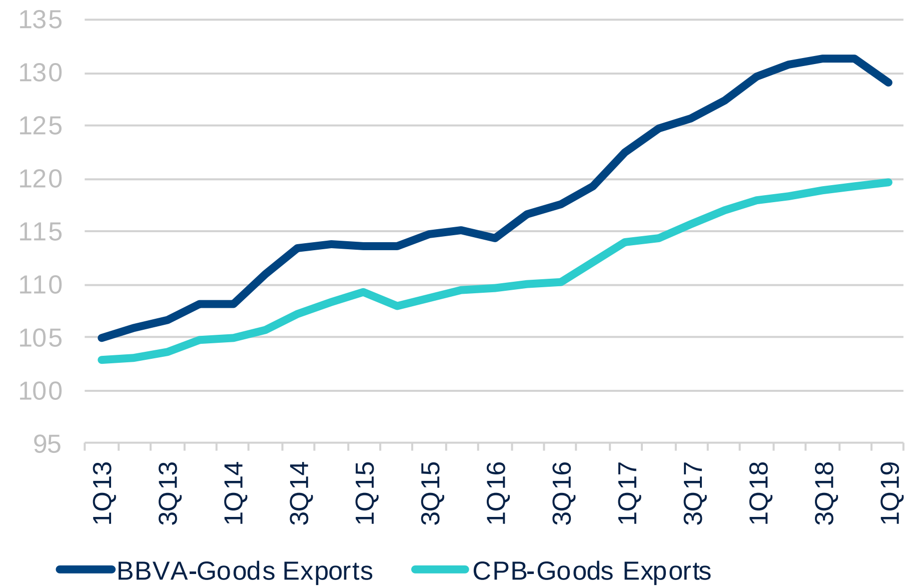
World exports of goods

(%, MoM growth, constant prices)



World exports of goods

(Index at constant prices, Jan-12=100)



Netherlands Bureau for Economic Policy Analysis (CPB) makes a world set based on 28 developed markets and 60 emerging markets covering a 97% of world trade

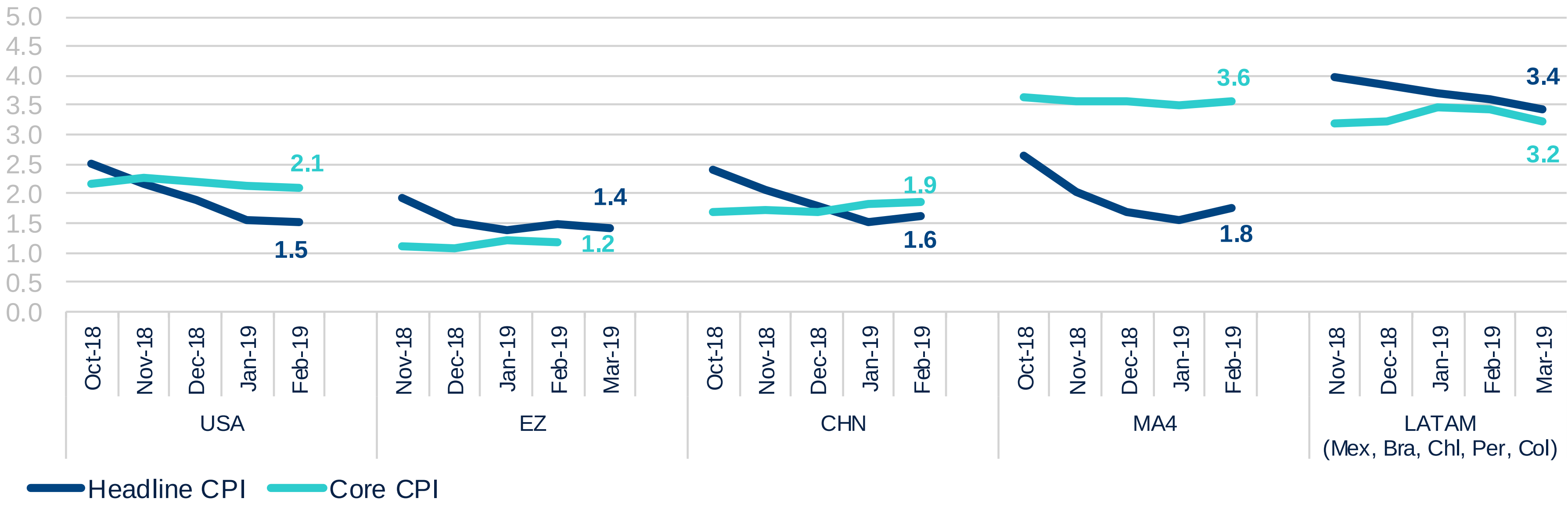
Source: BBVA Research and National Sources

Core and headline inflation rates are tending to converge following recent oil price deceleration

The price of oil has determined the latest inflation data throughout the world

Headline and core inflation: selected regions

(%, YoY)



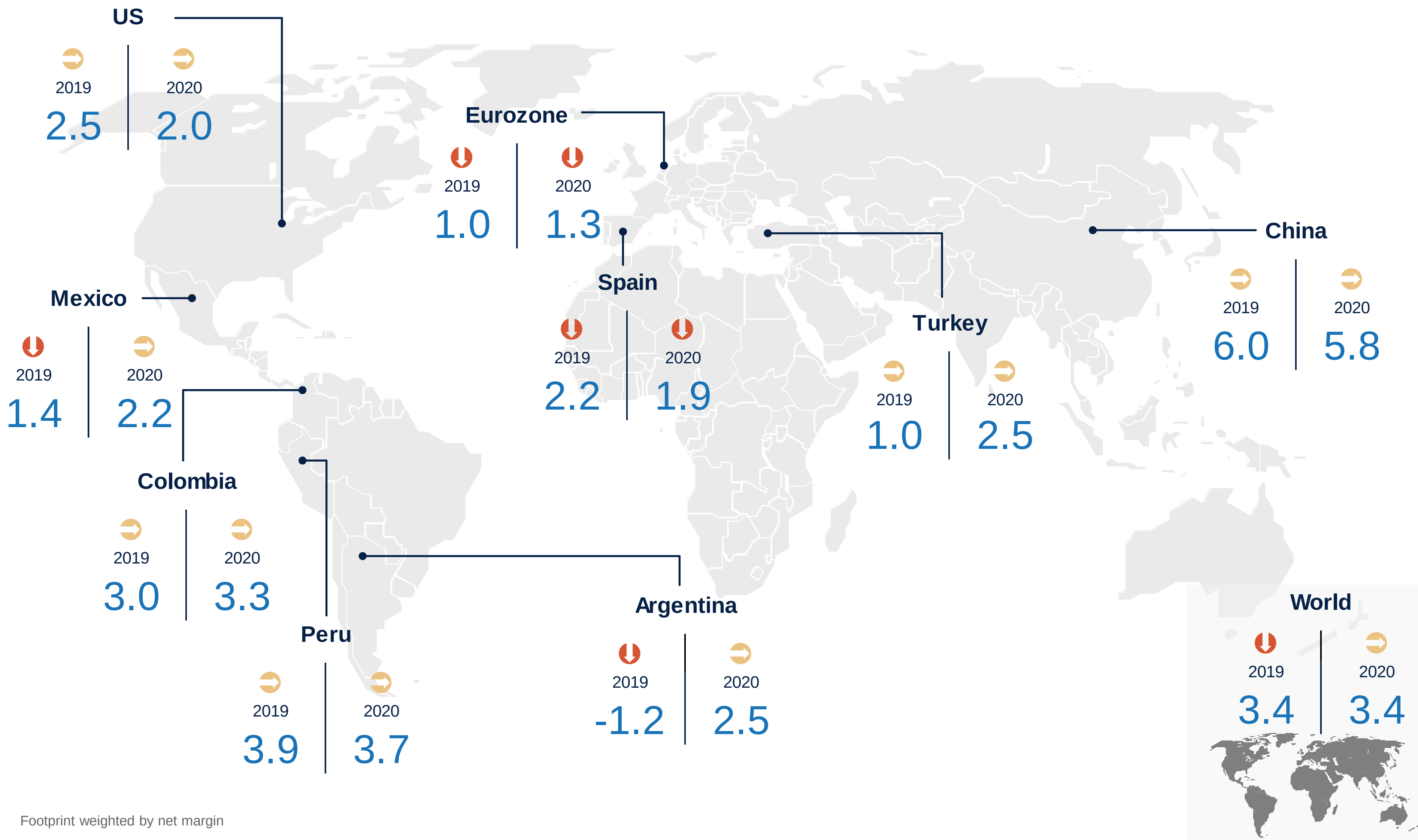
MA4: India, Indonesia, Japan and Korea

Source: BBVA Research and National Sources

02

New projections

Downgrading our global growth outlook for 2019



Footprint weighted by net margin

The number is green if the bias is upward and red if it is downward.

Growth moderation has caused a shift in monetary policy in the US and the Eurozone, and led China to step up stimulus measures

Fed

- **Long pause in the pace of rate increases,** but there could be a hike by the end of the year
- **The normalization (reduction) of the balance sheet will end earlier than expected** (Sep-19)

BCE

- **Postponement of monetary normalization**
- **Lower interest rates** for longer and additional liquidity (TLTRO-III)
- No refi **rate hikes** expected until Dec-20

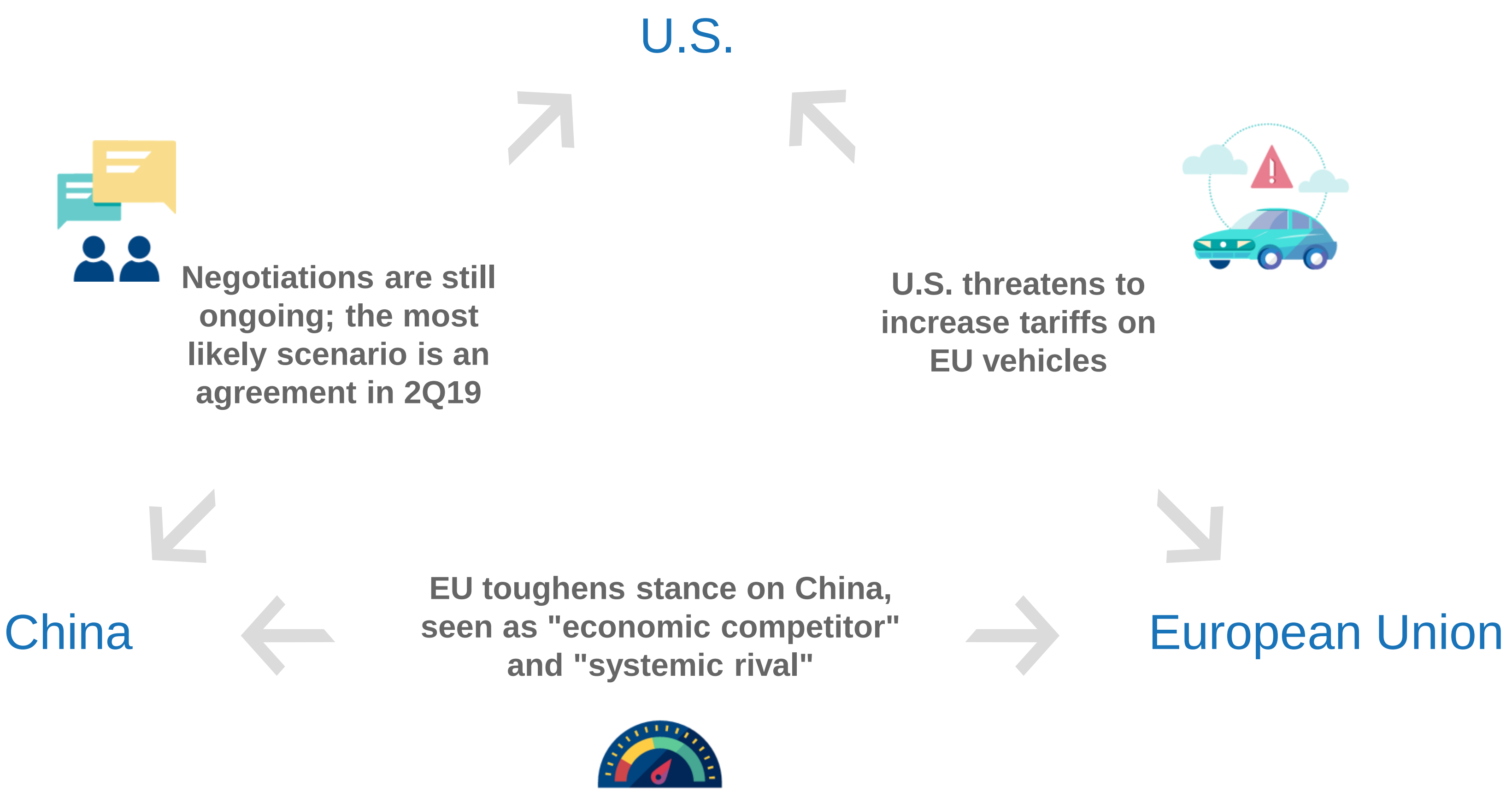
China

- **Additional monetary stimulus:** reserve requirement and lending rate reductions in 2019
- **Increase in public deficit,** to 2.8% of GDP in 2019
- **Tax cuts** (2% of GDP)

Latam and other emerging countries

- There is room for a **more dovish monetary policy**

Protectionism: US-China trade agreement delayed; meanwhile the EU begins to gain prominence as the focus of trade tensions



Action by central banks and an absence of "accidents" would enable global growth to soft-land

More signs of global slowdown

New stimulus policies

Assumption on the evolution of the global outlook: no “accidents”

01
Protectionism
An US-China trade agreement is still likely, despite the delay

02
***Brexit*:**
Greater uncertainty, for a longer time

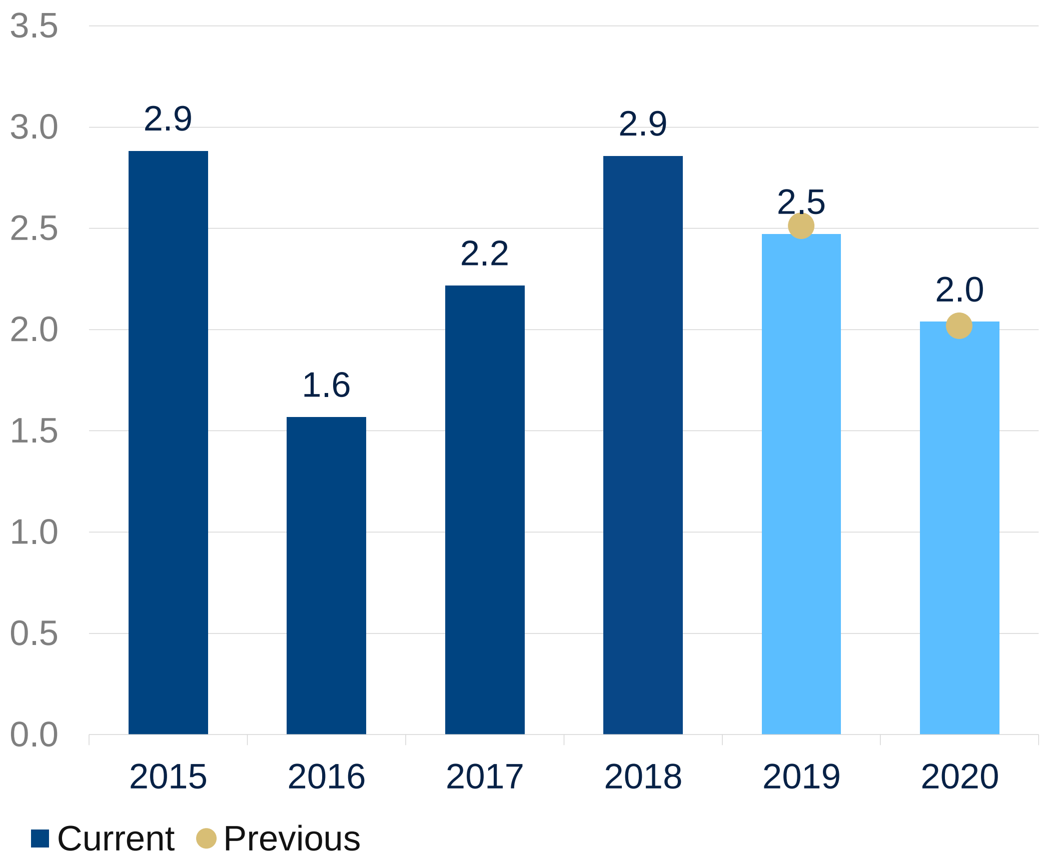
03
Financial markets:
volatility constrained by central banks’ measures

04
Oil:
Price moderation following the recent upturn

Global growth soft-lands

US: a cyclical activity moderation and a more patient Fed

US: GDP growth
(% y/y)

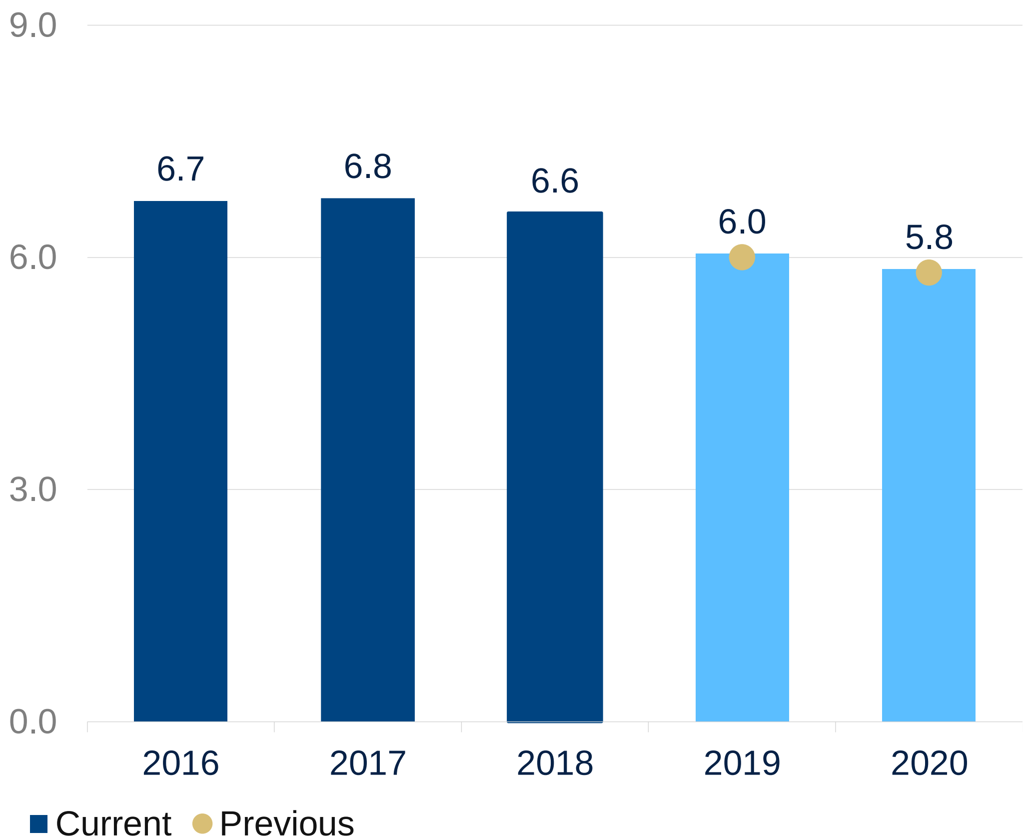


Source: BEA & BBVA Research

- Growth will continue to lose steam moving forward, converging to the potential rate
- Unchanged growth forecasts (with a downward bias), while the risk of recession remains high
- Inflation is expected to continue below the 2% mark during 2019
- Long pause in the rate hike, but we expect a hike by the end of the year
- The normalization (reduction) of the balance sheet will end earlier than expected (Sep-19)

China: a likely trade deal with the US and more supportive policies to favor a soft-landing of the economy

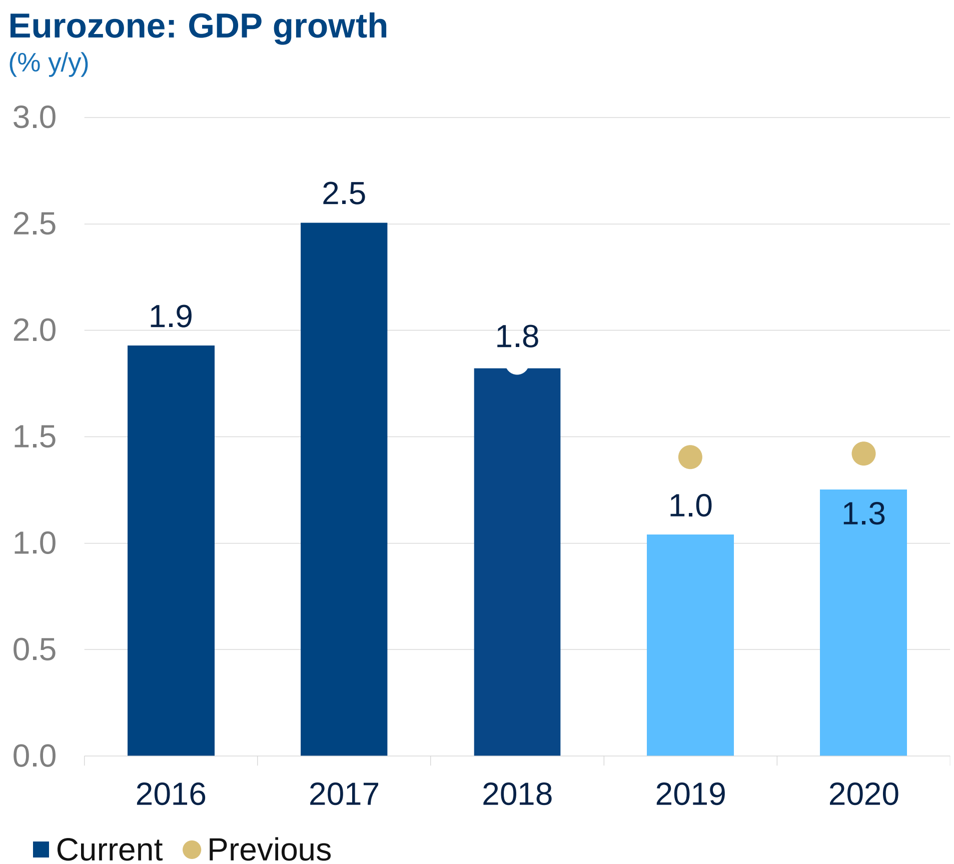
China: GDP growth
(% y/y)



Source: CNBS & BBVA Research

- The official growth target was lowered to a range between 6.0% and 6.5%
- Growth deceleration is the prime risk throughout 2019
- Monetary stimulus: expect cuts in both reserve requirements and lending rates
- Fiscal stimulus: tax cuts (mainly VAT) of 2% of GDP
- Inflation projection downward adjusted to 2.2% in 2019
- The RMB to USD exchange rate will hover around 6.7 after the US and China reach some kind of deal from trade talks

Eurozone: more prolonged activity weakness to cause lower growth in 2019, some recovery expected in 2020



Source: BBVA Research

- Downward revision of GDP growth forecasts
- Adjustment in activity expectations concentrated in exports and investment, given lower external demand and lingering uncertainties
- The euro is expected to appreciate from mid-2019 onwards, but at a more gradual pace than expected earlier
- Delay in the hiking cycle: first depo rate hike (+10bps) in June 2020 and first refi rate hike (+25bps) in December 2020.

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