QNB Economics
economics@qnb.com
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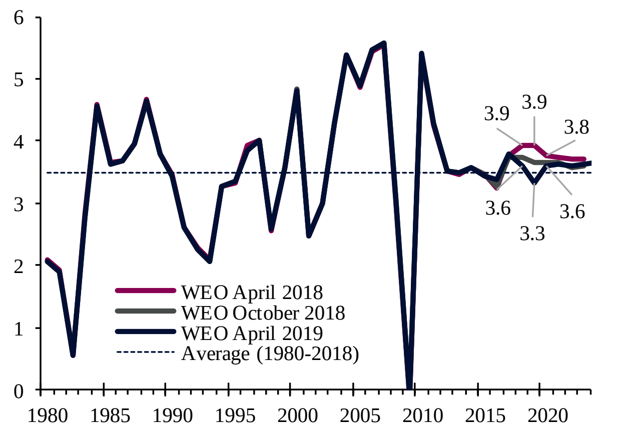
Global GDP growth is slowing but a serious crisis remains unlikely

In its latest World Economic Outlook (WEO), the International Monetary Fund (IMF) forecasts a temporary slowing in the growth rate of global economic activity (GDP) to 3.3% in 2019 from 3.6% in 2018. The IMF has been steadily revising down its estimates and forecasts for global GDP growth over the past year (see chart).

However, the IMF expects a recovery in 2020 with global GDP growth of 3.6%, driven by a continued policy stimulus in China and recent tailwinds in global financial market sentiment.

Growth rate of global economic activity (GDP)
(percent change, year-on-year)



Sources: IMF, QNB Economics analysis

The slowdown in 2018 and forecast downgrades have been caused by four main factors:

First, while the US economy posted its strongest performance in three years in 2018, up 2.9%, it started to slow by Q4 2018. GDP growth momentum is slowing due to dissipating fiscal stimulus, tighter financial conditions, slower and softening private sector confidence. Proactive policy tightening by the US Federal Reserve has helped to prevent the US economy from over-heating and has kept inflation well anchored despite low levels of unemployment.

Second, China's growth in the first quarter of 2018 declined, due to regulatory tightening to rein in shadow banking and drive financial deleveraging. This led to further decline across all GDP demand drivers, such as consumption, investment spending and external balances. Later in the year, the threat of a US-China trade war dimmed the outlook despite government intervention to spur growth through increased investment spending. Moreover, this threat of the trade war impacted adjacent Asian economies (Singapore, Malaysia, Indonesia, Vietnam, Korea and Taiwan), fading their economic outlook.

Third, the Euro area economy lost more momentum than expected as consumer and business confidence weakened, driven by several independent and country related events. Germany's automotive industry was disrupted by the introduction of the new emission standards, the "worldwide harmonized light vehicle test procedure". In France, the delay of Macron's reform agenda impacted growth. In Italy, concerns over the fiscal deficit above the Brussels convergence criteria led to widening sovereign spreads and lower investor demand to compensate for the perceived incremental risk.

Fourth, financial market sentiment worsened, with financial conditions tightening in the US and advanced economies later in the year, weighing on global demand.

Since the beginning of this year, conditions have slightly eased as the US Federal Reserve has signaled a more accommodative monetary policy stance to balance the impact of a fading fiscal stimulus. Moreover, markets became more optimistic about a partial US-China trade deal. This creates conditions for a more positive 2020 outlook. The projected pickup in 2020 is expected to be driven by an ongoing buildup of policy stimulus in China, recent improvements in global financial market sentiment, and the waning of some transitory drags on growth in the Euro area.

Any additional escalation of trade tensions and associated increases in policy uncertainty would hurt growth via a sharp deterioration in market sentiment which would imply portfolio rebalancing towards safe haven securities, and a harsher outlook for vulnerable emerging market economies.

Two other possible triggers for a sharp deterioration in market sentiment include a no-deal Brexit withdrawal of the United Kingdom from the European Union; and prolonged fiscal uncertainty with and elevated yields in Italy.

Despite these headwinds, global economic growth remains around its long-term average (see chart). The slowdown in global GDP growth is most likely to be modest and a real crisis remains unlikely. Indeed, it is quite possible that global growth could surprise favourably if trade differences are resolved quickly boosting business confidence and investor sentiment.

QNB Economics Team:

James Mason*
Senior Economist
+974-4453-4643

Luiz Pinto
Economist
+974-4453-4642

Abdulrahman Al-Jehani
Research Analyst
+974-4453-4436

* Corresponding author