Quarterly

Global Economic Outlook

Clock ticking for status quo

Déjà-vu at the Fed
- Oil markets remain oversupplied and emerging economies are vulnerable to capital flight.
- In a replay of 2015, we see the first Fed hike in 2016 in December.
- Better fundamentals on oil and EM should allow the Fed to hike three times by 25pp in 2017.
- Next US recession to be in 2019; peak fed funds in this cycle just 1.625%.
- The Fed is the only central bank hitting its inflation target; that raises the price tag of waiting.

China’s bid to deleverage will be yet another bumpy road
- A bumpy path ahead as China seeks to (slowly) tackle the excess capacity problems in the SoE sector.
- The external side remains vulnerable, and we expect USD/CNY to head to 6.80 by mid-2017.
- Below consensus on Latin America; structural challenges no longer offset by a commodity boom.
- Eastern Europe has benefitted from the better performance of the euro area and low oil prices.
- Asia ex-Japan faces headwinds from China, but tailwinds from oil and US and European demand.

Above-trend growth in Japan and the euro area
- Domestic demand is set to support growth above trend in both Japan and the euro area.
- BoJ to remain on its current policy path and the ECB to taper QE between March and December 2017.
- None of the major central banks possess much dry powder without a fiscal lift.

ECB, BoJ and BoE low on dry powder (Dark side of negative)
- Near zero rates should have been “temporary”, but the longer it lasts the more costly the side effects.
- Monetary policies work best when accompanied by structural reforms and sound fiscal policies.
- New downside risks would trigger a fiscal response, supported by monetary policy. That would work.

Heightened policy uncertainty
- The logical response to an uncertain event, is to delay strategic investment and hiring decisions.
- Policy uncertainty to remain a headwind on the global economy in both 2016 and 2017.
- The risks are biased to the downside in the event a political event delivers an adverse outcome.

Picture source: iStock
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