THE FORWARD VIEW – GLOBAL

DECEMBER 2019

National Australia Bank

Amid conflicting trade signals, signs growth is stabilising

- Major Advanced Economy growth was little changed in Q3. However, we expect US growth to ease somewhat further and Japan's economy is set to contract in Q4, although the yoy growth rate is likely to bottom out by mid-2020.
- In contrast, growth in Emerging Market economies eased slightly in Q3. This was driven by a slowdown in China and, in particular, India which experienced its weakest rate of growth since Q1 2013. We expect EM growth to pick up from here. This is in large part based around an expected recovery in India, as well as in Latin America, but there is a high degree of uncertainty around the timing and extent of the recovery in these regions.
- Our tracking indicator of global GDP growth for Q3 is at 3.0% yoy, the same as in Q2. Moreover, our global leading indicator suggests that growth may have bottomed out, while the global manufacturing PMI has started to turn around. These indicators are consistent with our forecasts for global growth (on a yoy basis) to remain around current levels before strengthening from mid-2020. The easing in monetary policy that has occurred this year – particularly in the US and EM economies – should support global activity and there is a move towards fiscal support in some countries as well.
- Trade policy related uncertainty has been one factor weighing on global growth. At the time of writing it is unclear whether the much talked about "Phase One" trade deal between the US and China will occur, or whether the tariffs scheduled for 15 December will be deferred or come into effect. Recent announcements by the US that it will remove steel/aluminium tariff exemptions for Brazil and Argentina, and threatening to impose tariffs on France and the EU, are a reminder that trade policy tensions are likely to remain a headwind for some time to come.

Global Growth Forecasts (% change)

	2018	2019	2020	2021
US	2.9	2.3	1.7	1.8
Euro-zone	1.9	1.2	1.1	1.4
Japan	0.3	1.1	0.6	0.9
UK	1.4	1.3	1.0	1.5
Canada	1.9	1.6	1.6	1.7
China	6.6	6.1	5.9	5.8
India	7.4	5.1	6.2	7.1
Latin America	1.0	0.3	1.3	2.1
Other East Asia	4.1	3.4	3.5	3.7
Australia	2.7	1.8	2.0	2.4
NZ	2.8	2.3	2.3	2.0
Global	**3.6**	**3.0**	**3.2**	**3.5**

NAB global leading indicator

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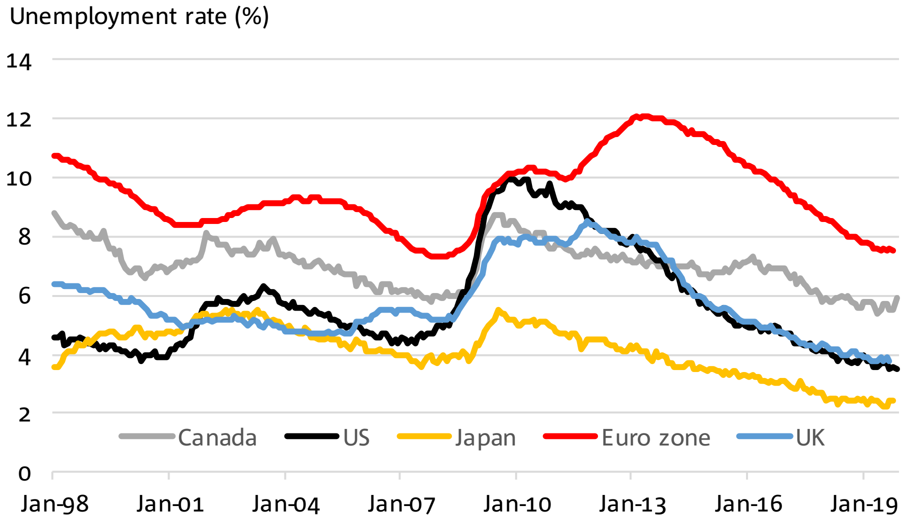
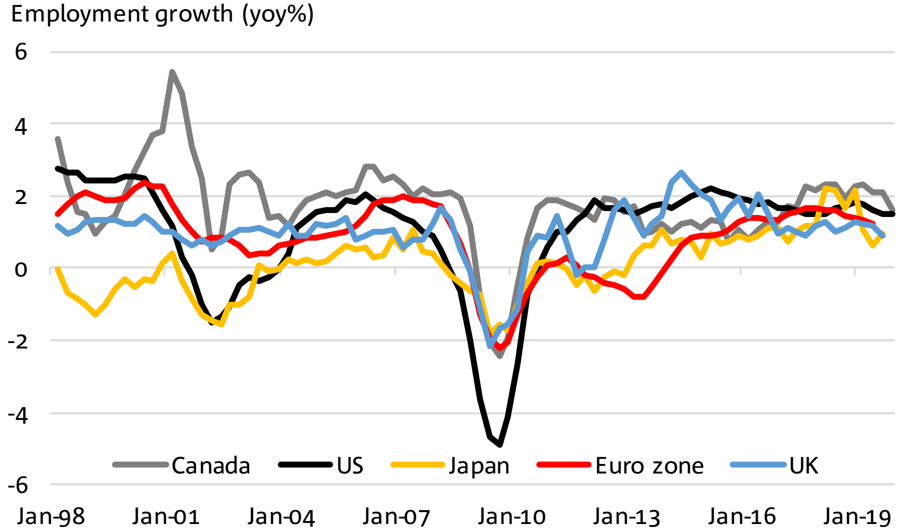
MAJOR ADVANCED ECONOMY LABOUR MARKETS HOLDING UP SO FAR

Unemployment rates levelling out, but at low levels, while employment growth remains solid and above population growth

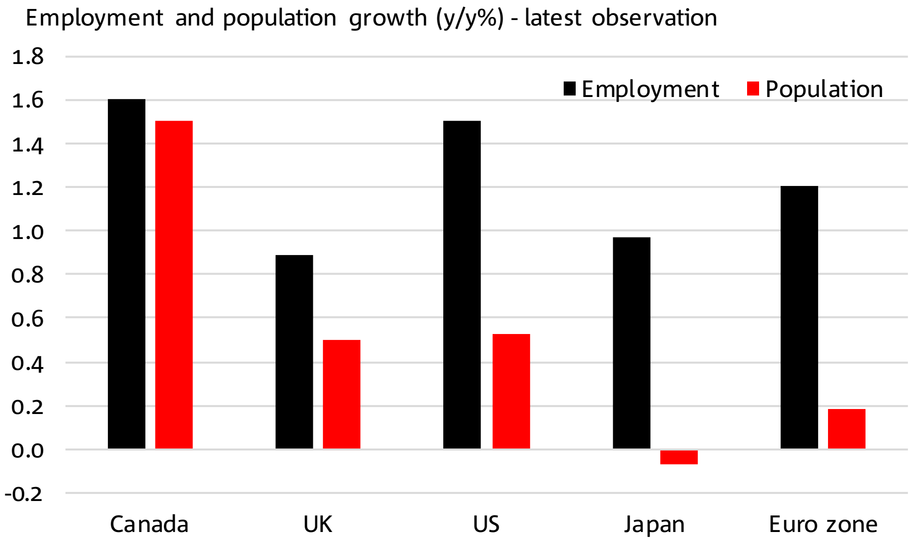
Unemployment rates levelling out low levels



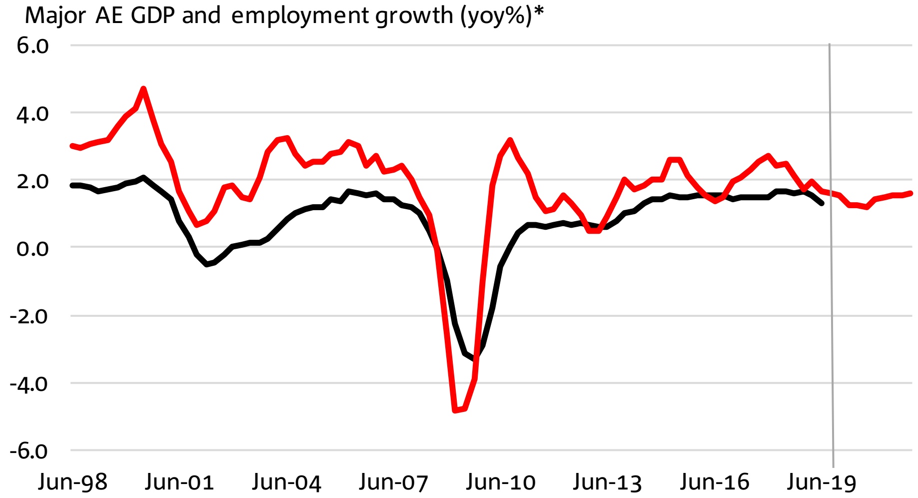
Employment growth has slowed, but only modestly



Employment still growing faster than population



Employment may yet come under further pressure as AE growth slowdown continues as employment can lag activity



* US, Euro-zone, Japan, Canada, UK. Aggregated using GDP PPP weights

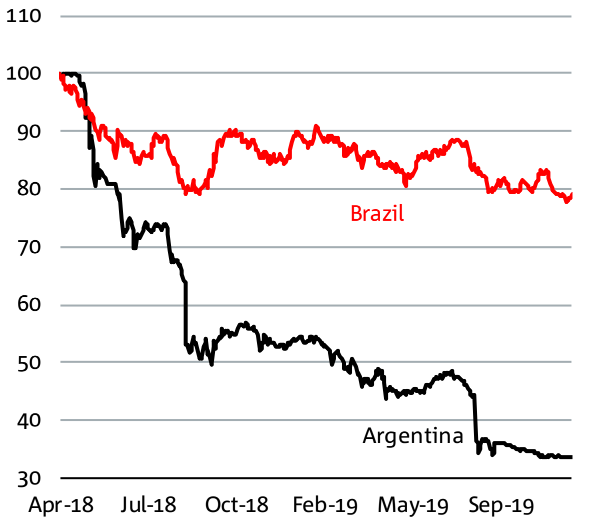
Sources: Refinitiv, IMF, NAB Economics calculations

FINANCIAL AND COMMODITY MARKETS

Limited progress on US-China trade deal, as US proposes fresh tariffs elsewhere

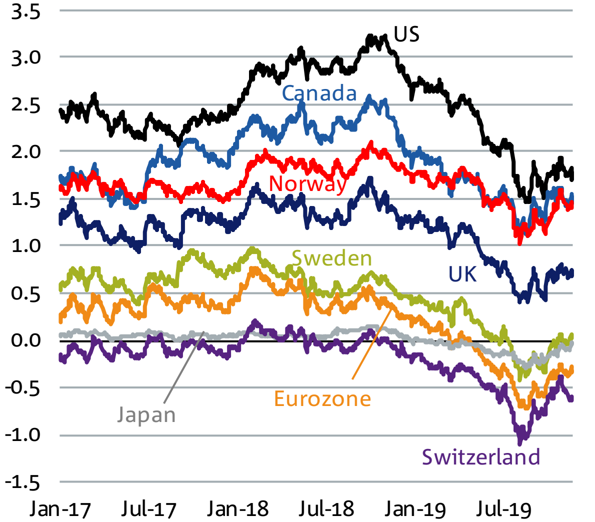
Exchange rate depreciation in Latin America has raised US ire

Emerging market currency indices (to US$) (3 April 18 = 100)



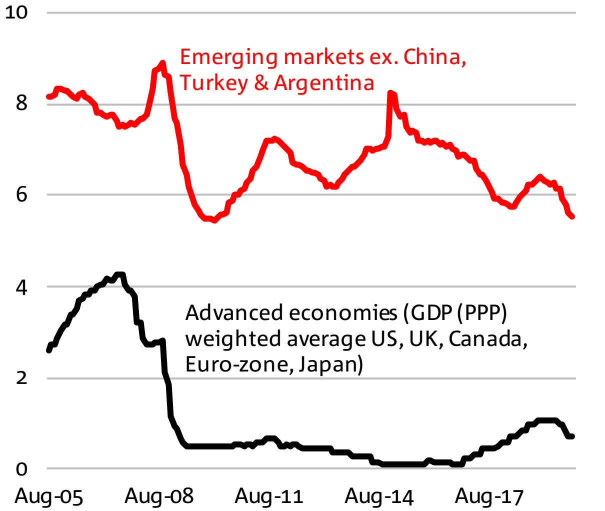
Recent rise in bond yields appears to have run out of steam

10 year government bond yields (%)



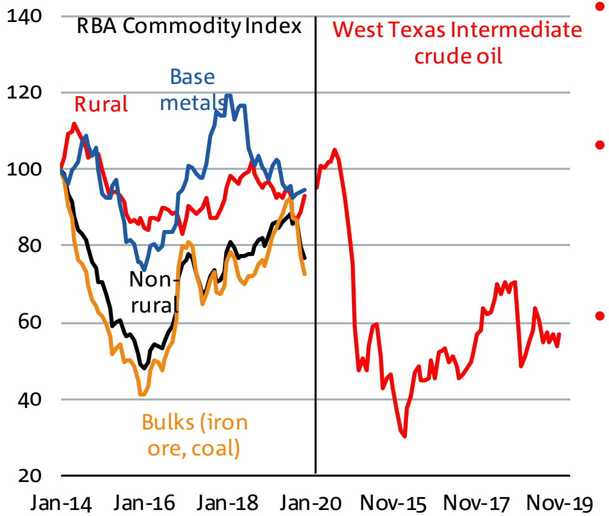
Monetary policy (particularly in EMs) has continued to ease

Average central bank policy rates (%)



Non-rural commodities prices have fallen, led by iron ore

Commodity price indices (Jan 2014 = 100)



- The international trade environment took another turn for the worse in early December, with the United States announcing it would include Brazil and Argentina in its existing steel and aluminium tariffs (with these countries among a range of US allies initially excluded). President Trump accused the two countries of exchange rate manipulation, negatively impacting US farmers in global markets. The Brazilian Real is down around 7.5% and the Argentinean Peso is down over 37% since the start of 2019, primarily due to political and financial turmoil.
- Tensions were further raised by the US threatening a 100% tariff on French luxury good imports, in retaliation to proposed digital taxes, and tariff increases on the EU in relation to aerospace subsidies.
- In addition, hopes of an imminent "Phase One" trade deal between the US and China have eroded somewhat, with President Trump stating that it may be concluded after the 2020 presidential election. However, some media reports have been more positive around prospects for a near term deal or at least deferral of the tariffs scheduled for 15 December.
- The equity market response to these new trade tensions was relatively muted – with the US S&P 500 dipping by around 2% from all-time highs in late November, along with a modest uptick in the VIX volatility index, before largely recovering. EM markets have drifted gradually lower since the start of November.
- Following a lift in yields from the Q3 2019 lows, a range of major advanced economies have seen bond yields fall somewhat since mid-November, as monetary policy expectations point to further easing (compared with a flatter outlook at the start of the month).
- The recent easing trend for monetary policy continued in November – with cuts in Brazil and Mexico bringing our weighted average of EM policy rates to its lowest point since the Global Financial Crisis. It is worth noting that reforms in some EM economies – most notably India – mean that neutral rates are lower now than in the past.
- In US dollar terms, non-rural commodity prices have fallen in recent months – with the RBA index down around 13% from its recent cycle peak in July. This decline was led by bulk commodities (primarily iron ore), as supply disruptions have begun to unwind, and demand is likely to weaken in coming months as some Chinese mills close for the winter.

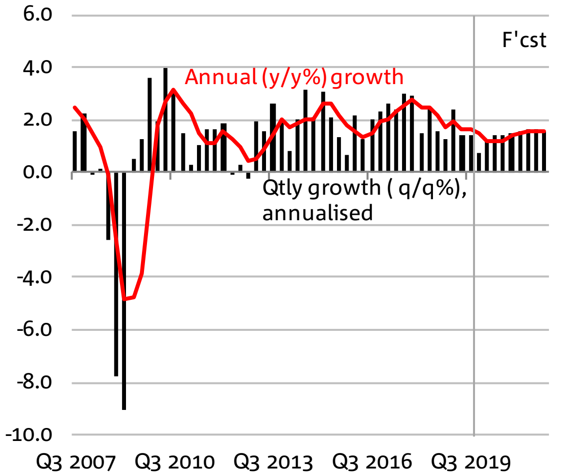
 Sources: Refinitiv, RBA, Bloomberg, NAB Economics

ADVANCED ECONOMIES

Major AE slowdown not over despite Q3 pause, but growth likely to stabilise in 2020

Slowdown in major AE growth paused in Q3 but to resume in Q4…

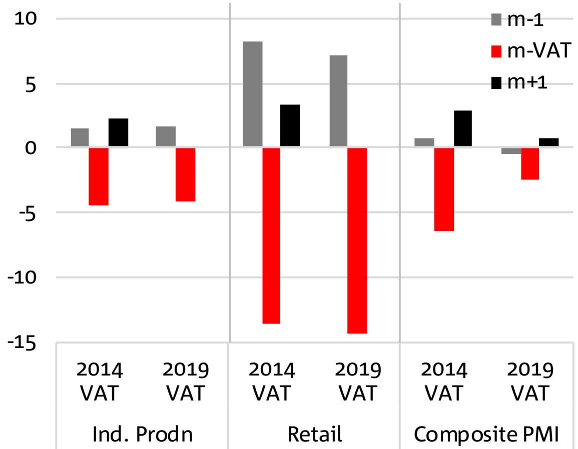
GDP growth - major AEs (yoy%)*



* US, Euro-zone, Japan, UK, Canada

…in part due to likely contraction in Japan following VAT increase

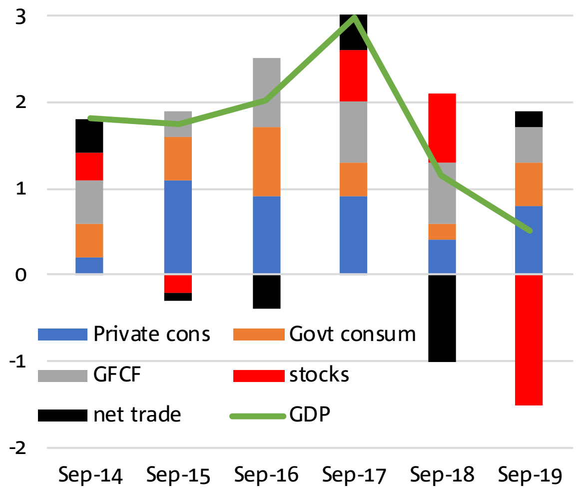
VAT increases - before and after (m/m%)*



* m-VAT is the month of the VAT increase, m-1 refers to the month before, m+1 to the month after

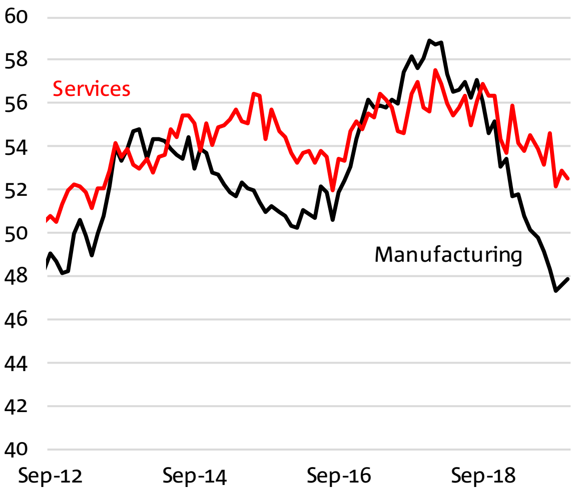
German growth woes partly due to an inventory correction

German GDP growth: contribution to y/y growth (ppts)



Surveys show signs of stabilising

Major advanced economy PMIs (50=Breakeven)



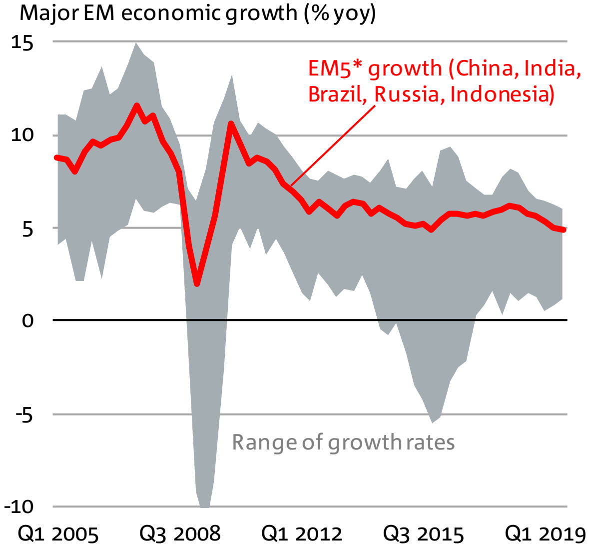
Sources: Refinitiv, Markit, ISM, NAB Economics

- Major AE growth was little changed in Q3. However, we expect US growth to ease somewhat further and Japan's economy is set to contract in Q4. That said, absent adverse trade developments, the easing in US monetary policy since mid-year and a turn towards fiscal stimulus should help stabilise growth in 2020. Business surveys have also recently showed signs of stabilising and AE labour markets have held up well (see Charts of the Month).
- Quarterly US growth was unchanged in Q3 and while the annual growth rate again declined it remained at a reasonable level. Our forecasts allow for some further softening over coming quarters based on some easing in consumption growth and continued pressure on business investment from margin compression and the US-China trade dispute. That said, housing investment has turned the corner and October capital goods orders were more positive than they have been for a while, so the bottom is not falling out of the economy.
- Euro-zone growth has settled at a modest 1.2% yoy in the last two quarters. Germany's economy – which is highly exposed to the global trade and manufacturing downturn – has been particularly weak. Domestic final demand has held up but a trade downturn, followed by a major inventory correction, has weighed on growth. While this should fade in time, industrial production fell further in early Q4 although factory orders have stabilised.
- Brexit related uncertainty has also been an issue for the UK and, to some extent, the Euro-zone, and today's UK election may provide a clearer sign of where this headed.
- Japan's VAT increase in October is likely to lead to a contraction in Q4 GDP. Partial indicators fell sharply in October, as did the PMI. Typhoons also caused disruption and may explain why some of these indicators fell by around as much as they did post the larger 2014 VAT increase. In 2014, the contraction in growth extended over only one quarter and we expect the same outcome this time around. Japan's government has announced a fiscal stimulus package of over 2% of GDP. Although not all of this is new spending, it will provide some support to GDP growth in 2020.
- Prospective fiscal stimulus is not just limited to Japan. The platforms of the two major parties in the UK election also point to a fiscal boost and there is renewed debate about this option in Germany (but so far no actual action).

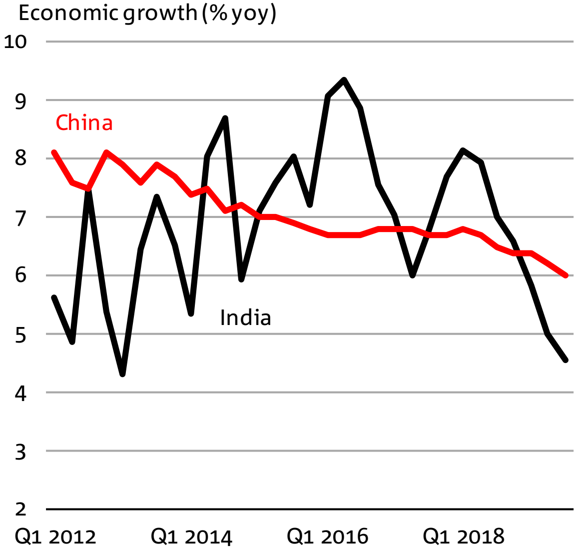
EMERGING MARKET ECONOMIES

India dragged major EM growth to a ten year low in Q3

Major EM growth slows to its lowest since 2009...

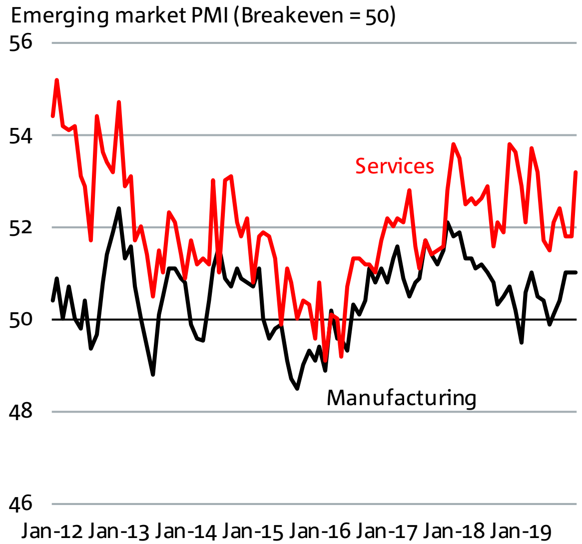


...led by slowing growth in China and India (the two largest EMs)



Export volumes continued to slow through to September

PMI measures stronger than recent economic trends



Sources: Refinitiv, Markit, CEIC, NAB Economics

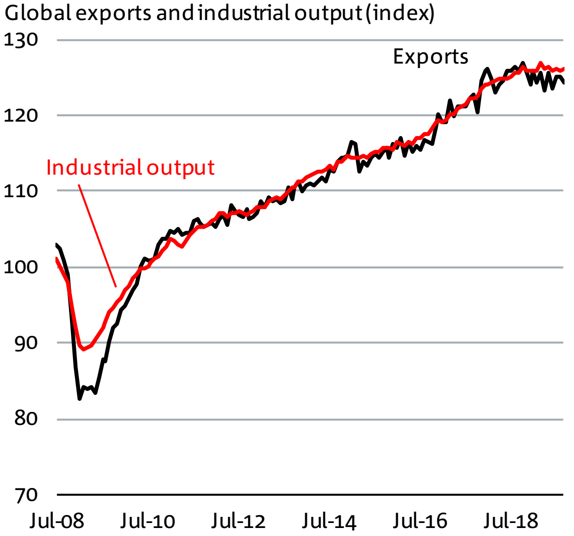
- Overall growth among the largest emerging market economies slowed in the third quarter, led by weaker conditions in China and India (respectively the largest and third largest economies in the world). Growth for the five largest EMs slowed to 4.9% yoy. While only slightly lower than in Q2, this was the weakest rate of growth since Q2 2009, when these economies started to recover from the Global Financial Crisis.
- Indian economic growth slowed further in Q3 – down to 4.5% yoy (from 5.0% yoy previously), the weakest rate of growth since Q1 2013. The downturn was largely domestically driven – growth in private consumption was marginally stronger, however investment growth slowed to 1.0% yoy, despite 135 basis points of cuts to India's monetary policy rate this year. We have revised down our forecast for Indian growth, reflecting the weaker than expected outcome in Q3 – with annual growth of 5.1% in 2019 and 6.2% in 2020.
- Growth in emerging markets is generally more trade dependent than advanced economies. On a three month moving average basis, EM export volumes fell by 1.8% yoy, with emerging Asia (excluding China) and Africa & the Middle East the main contributors to this decline.
- Although officials from both China and the United States continue to suggest that a trade deal is imminent, progress appears to have slowed. Recent statements from President Trump – indicating that the deal may not be concluded until after the 2020 US presidential election – along with tariffs imposed on Brazil, Argentina and threatened against France and the EU suggest that trade continues to present some downside risk.
- Global business surveys provide the most up-to-date indicators of economic conditions. Emerging market PMIs have strengthened in recent months – driven by a strong increase in service sector readings. In contrast, after showing some recovery, EM manufacturing surveys have been stable for the past three months.
- That said, the earlier improvement seen in manufacturing PMIs is not broad based. Much of it has been evident in China – where the strength in PMIs appears at odds with weakness in output and profit measures – while readings for countries such as Russia, Indonesia and South Africa (the latter being an economy wide measure) all remaining in negative territory.

National Australia Bank

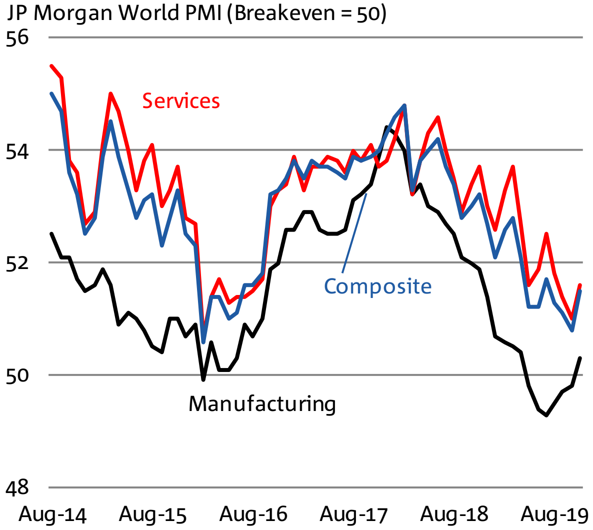
GLOBAL FORECASTS, POLICIES AND RISKS

Signs activity is stabilising amid still high trade uncertainty

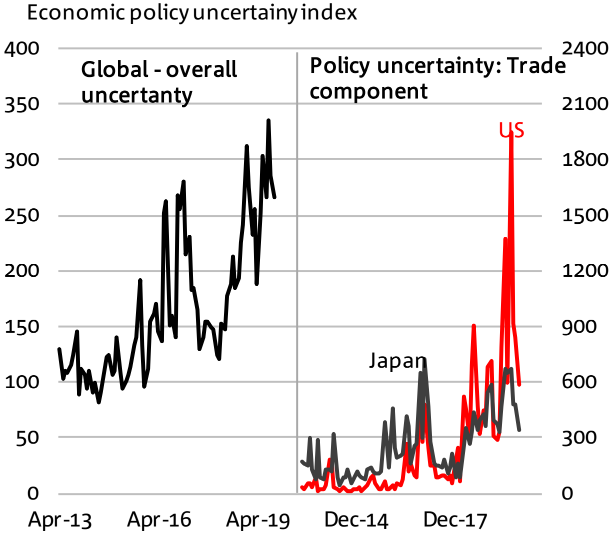
Global trade and industrial prodn. tracking sideways to September



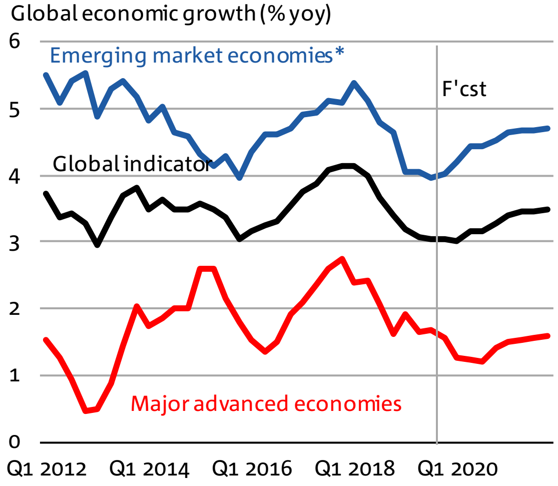
Global PMIs suggest manufact. may have turned the corner



Uncertainty caused by trade policy still elevated



EMs key driver of expected near term stabilisation in global growth



* Based on China, India, major Latin America & East Asia countries, Russia

- Data available to September indicate world trade and industrial production have been tracking sideways recently. The timelier global PMI measure suggest that this levelling out might be turning into a recovery, with the manufacturing PMI in November moving above 50 for the first time since April (although alternative indicators are not quite as strong). For the services sector, which has generally held up better than manufacturing, the trend is less clear although there was also some improvement in November.
- Trade policy related uncertainty has been one factor weighing on global growth. More recently there has been the expectation that the US-China would agree on a "Phase One" trade deal which would at least see the tariffs scheduled to come into effect on 15 December removed and possibly lead to some roll-back of existing tariffs. At the time of writing it is unclear whether this will occur, or whether the December tariffs will be deferred or come into place as scheduled.
- While the prospect of a US-China deal has boosted sentiment and financial markets, measures of trade policy uncertainty remain elevated even if they are off their recent peak. Recent announcements by the US that it will remove steel/aluminium tariff exemptions for Brazil and Argentina, and threatening to impose tariffs on France and the EU, are a reminder that trade policy tensions are not limited to US-China. Trade uncertainty is likely to remain elevated and remains one of the key risks to the global outlook.
- We have lowered our forecasts for global growth in 2020 to 3.0% (from 3.1%) due to a downgrade to our projection for India following the weak Q3 GDP outcome. Despite the India disappointment, our tracking indicator of global GDP growth for Q3 is at 3.0% yoy, the same as in Q2. Moreover, our global leading indicator (see front page) also suggests that growth may have bottomed out. In 2020, an expected recovery in India, as well as in Latin America, underpins our forecast that growth will start to strengthen, although the timing and extent of the recovery in these regions is highly uncertain.
- More generally the easing in monetary policy that has occurred this year – particularly in the US and across many EM economies – should support global activity. Fiscal policy support remains limited but has been used by China to manage the trade fall out and some AEs are moving to put in place a fiscal stimulus (Japan, UK).

Sources: Refinitiv, Markit, "Measuring Economic Policy Uncertainty" by Scott Baker, Nicholas Bloom and Steven J. Davis at www.PolicyUncertainty.com, NAB Economics

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