THE WORLD ECONOMY

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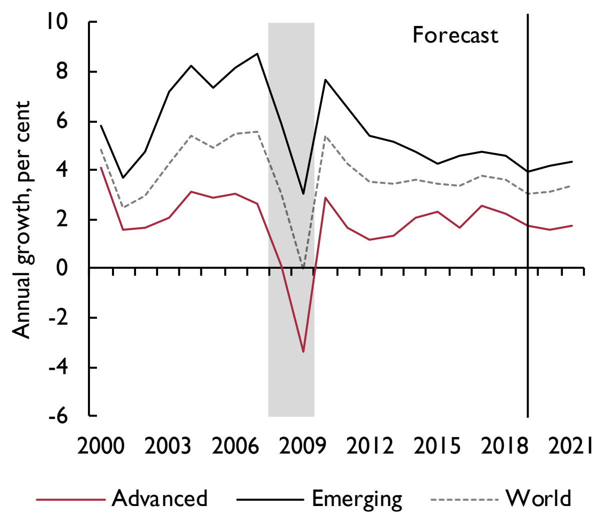
Global outlook overview

After two years during which global economic growth has slowed from a cyclical peak in 2017 to its slowest rate since 2009, we expect that the growth slowdown will halt this year. We project global GDP growth of 3 per cent this year, effectively the same as last year, and 3¼ per cent next, with these forecasts unchanged from those of three months ago.

The headwinds to output growth since 2017 have been widespread, due to several factors. With China now accounting for around 20 per cent of global GDP,[1] the reduction in GDP growth in China since 2017 as the economy has continued its adjustment path has reduced global growth by about 0.2 percentage points. The era of over 7 per cent annual economic growth in China has ended and growth last year of 6.1 per cent was the slowest for 29 years, reflecting both international factors and the phase of economic development adapting. In the US, the ending of the boost to growth from the fiscal stimulus has occurred at the same time as interest rates increased as part of monetary policy normalisation and US growth has slowed from 2.9 per cent in 2018 to 2.3 per cent in 2019. Last year the imposition of new tariffs by the US (and subsequent retaliation) and uncertainty over future tariff imposition led to disruption and uncertainty in global goods trade. In addition, disruption in the automobile market from changing regulatory and demand patterns has played a role, especially in Germany. Finally, recessions in Argentina and Turkey and slower growth in India, largely from domestic factors, have also contributed to explaining slower overall economic growth. This confluence of factors has worked to reduce global growth.

Figure 1. GDP growth in advanced and emerging economies



Source: NiGEM database and NIESR forecast.
Note: Shading denotes global financial crisis.

We expect that the waning influence of the temporary factors that have slowed growth in the past two years and monetary policy loosening in several economies, especially in the US, will support the pace of growth gradually recovering later this year and into 2021 (see figure 1). A key global uncertainty, however, is how the change in the direction of tariffs that has occurred in the past two years will develop and how it will affect the global trading system. The signing of the Phase One

*All questions and comments related to the forecast and its underlying assumptions should be addressed to Iana Liadze (i.liadze@niesr.ac.uk). We would like to thank Jagjit Chadha and Garry Young for helpful comments and Patricia Sanchez Juanino for preparing the charts and compiling the database underlying the forecast. The forecast was completed on 24 January 2020. Exchange rate, interest rate and equity price assumptions are based on information available to 16 January 2020. Unless otherwise specified, the source of all data reported in tables and figures is the NiGEM database and NIESR forecast baseline.

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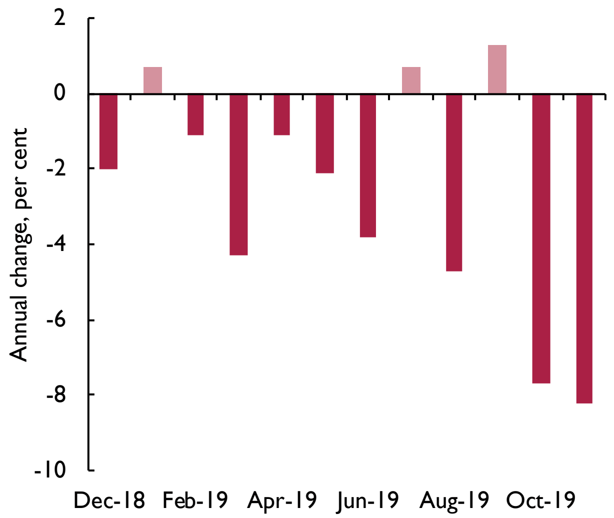
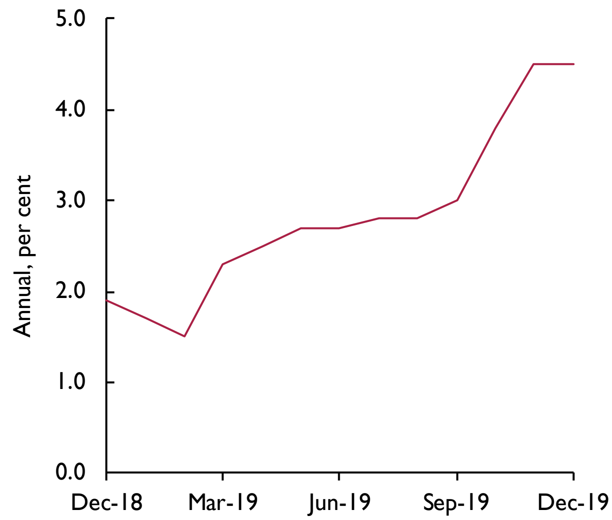
Figure 22. Japan: Industrial production



Source: METI, Japan.

Figure 23. China: Inflation



Source: NBS, China.

and November (figure 22). With the Jibun Bank Japan Manufacturing PMI drifting down at 48.4 in December 2019, the output index has been stuck in contractionary territory since May 2019.

Taking the downside risks into consideration, we forecast the Japanese economy grew by 1.1 per cent in 2019 and, with the consumption tax increase having a negative effect, expect growth of ½ per cent in 2020. Low interest rates and unemployment, together with positive spillovers from the 2020 Olympics mean that the negative impact of the tax increase should be modest. In addition, Japan is in the process of delivering a US$120 billion spending package, around 20 per cent of which will be spent by March 2020, and the rest from April 2020 to March 2021. Combined with accommodative monetary policies, we expect Japan's inflation rate to have been 0.5 per cent in 2019 but, with the effect of the consumption tax, to increase to 1¾ per cent in 2020, before falling to 1 per cent in 2021.

China

China's GDP grew annually by 6 per cent in the fourth quarter of 2019, the weakest growth rate since the first quarter of 1992. Although the annual growth rate of 6.1 per cent for 2019 as a whole was the slowest in 29 years, it was still within the government's target of 6–6.5 per cent and it also meant that the per capita Gross Domestic Product in 2019 reached US$10,276 at the average exchange rate, exceeding the US$10,000 level. There have been signs of consolidation in economic activity emerging in recent months. The 6.9 per cent year-on-year increase in industrial production in December 2019 was the fastest yearly growth since March 2019. While the monthly official non-manufacturing PMI held above 52 in 2019, the official manufacturing PMI in the last two months of 2019 was 50.2, marking a pick-up after the below par readings seen since April. The expansion in factory activities was supported by not only domestic fiscal and monetary stimulus measures but also improving factors in the external environment. The renminbi has steadily appreciated against the US dollar since last August and now stands around seven to the US dollar mark. Business confidence has been significantly boosted by the removal of China by the US Treasury Department from the list of currency manipulators and the trade war has eased with the Phase One trade deal signed this January.

China's annual inflation rate rose to 4.5 per cent in November 2019 and remained at the same rate in December. Surging pork prices caused by a prolonged African swine fever epidemic were a major contributor to the highest annual inflation rate since January 2012.

Looking ahead, we still expect the Chinese economy to continue to show rapid growth, by international comparisons, in 2020 and 2021. We forecast China's annual GDP growth rate in 2020 to be just below 6 per

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