Slow Global Expansion Continues: After A Weak 2019, 2020 Probably A Bit Stronger

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Slow Global Expansion Continues: After A Weak 2019, 2020 Probably A Bit Stronger

The global economic expansion continues: After a solid increase in 2018, global GDP growth has slowed in 2019, but it is likely to strengthen some in 2020. Measured with market exchange rates, GDP probably increased only +2.7% y/y in 2019:4Q, but we forecast an increase of +2.9% in 2020:4Q. Using PPP exchange rates, the increase is likely to be +3.1% y/y in 2019:4Q and +3.4% in 2020:4Q; see page 4 for details on the PPP forecasts.

Many unfolding developments will affect the outcome: The trade battles and Brexit have been major uncertainties this year. But the phase 1 deal between the US and China will reduce tensions some, and the British election also provides partial clarity. However, public protests in Hong Kong, France, India, Iran, Iraq, and Chile reflect ongoing difficulties.

Importantly, slower inflation and sluggish growth have led to a major easing cycle -- in both monetary and fiscal policies. The benefits of this should become apparent in 2020.
Growth Has Slowed in Both DVs and EMs

Growth in DVs has slowed and is likely to be less than +2.0% y/y in both 2019 and 2020. But easing of monetary policies has occurred in both the US and the Eurozone; Japan’s policy remains accommodative. In addition, some fiscal stimulus is being undertaken in Japan, the Eurozone, the US, and Canada.

EM economies as a group are likely to grow much faster than DVs, although a little less than +4.5% in both years.

- Central banks are generally accommodative, and there have been 65 EM easing actions in the past four months.
- EM central banks have more room to move now that the Fed has eased, reducing the risk of currency crises.
- China has implemented stimulative policies to offset trade war damage and is in a wait-and-see mode.

Of course, long-term trend growth in EMs will remain faster than in DVs as they adopt proven economic systems and deploy known technologies; in many cases they also benefit from faster population growth. Nevertheless, EM growth in aggregate will remain slower than it was in the prior decade.

The Phase 1 US-China trade agreement (a plus) is far from enough to assure that China will be a big driver of global growth in 2020.
EMs GDP in PPP Terms Now Much Larger Than DVs and Will Continue to Gain Share

In a historic shift toward the end of the previous decade, GDP in EMs became larger than DVs in PPP terms. The forecasts for 2020 show the impact: Global real GDP in PPP terms is likely to grow +3.4% y/y in 2020:4Q (after +3.1% in 2019:4Q). EMs will probably account for 75% of the global increase in 2020 (ie, +2.5 percentage points of the +3.4% total); DV growth is likely to account for only about 25% of the increase in 2020.

The biggest changes since our last global outlook are: We have increased our 2020 forecasts for US GDP to +2.5% (from +2.0% before) and for Japan to +1.0% (from the prior +0.5%). However, our forecast for India has been reduced to +6.5% (from the prior +7.4%).

<table>
<thead>
<tr>
<th>Real GDP Y/Y %</th>
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<tr>
<td>Weight</td>
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<tr>
<td>Developed</td>
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<td>Eurozone</td>
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<td>Other Developed</td>
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<td>Emerging</td>
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<tr>
<td>China</td>
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<tr>
<td>India</td>
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<td>Brazil</td>
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<tr>
<td>Russia</td>
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<tr>
<td>Other Emerging</td>
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<tr>
<td>Global</td>
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The Purchasing Power Parity (PPP) exchange rate is defined as the amount of currency that would be needed to purchase the same basket of goods and services as one unit of the reference currency, usually the US dollar.
Mixed Signals In Current Indicators

Economic indicators have been volatile across both DVs and EMs: The US composite PMI (Markit data) has trended lower in 2019 but has moved up a little recently. In the Eurozone and the UK, the PMIs also have declining trends, and the UK has fallen below the neutral 50.0%. Among EMs, composite PMIs for India and China have increased a little recently. The mfg PMI in Turkey has increased but remains below neutral at 49.5%.
Headline inflation in consumer prices in major developed economies has slowed after some acceleration on average over 2016-2018. Core PCE inflation has also slowed in the US and is under +2% y/y. US CPIs, however, are running faster at +2.0% headline and the core at +2.3% in Nov.

Eurozone CPI inflation was only +1.0% y/y in Nov with the core index slightly higher at +1.3%. In Japan, the CPI was +0.1% y/y in Oct, and the core index was only +0.4%.

Structural forces such as globalization, technology, and increased competition remain key restraints in all DVs.
EM inflation has generally slowed and is low for most countries by historical standards. These charts show CPIs for the EMs that we cover.

Turkey has been the main exception to the EM inflation trend. Inflation surged partly due to lira weakness and to rising food prices. Recently, the pace has receded from its peak of +25.2% y/y to +10.5%.

Inflation in Russia had accelerated in 2018-early 2019 reaching +5.2% y/y, but tight monetary policy has helped bring it down to +3.5%. Inflation has also slowed in Brazil (to +3.3%) and in Mexico (to +2.8%).

Inflation in Asia has been impacted by one-off events. The CPI in India has jumped to +5.5% on food (mainly vegetable) prices, but the core is +3.8%. China’s CPI has accelerated to +4.5%, largely due to higher prices of pork and its substitutes, pushed up by swine flu; the core is only +1.4%. Indonesia’s headline remains slow at +3.0% in Nov with the core at +3.1%.
Late last year, some DV central banks expected to raise their policy rates gradually as part of the process of normalizing monetary policy. But the combination of slower growth, trade war disruptions, and low inflation has led to a sharp turn toward easing.

The Fed has reduced the funds rate by -75bp in three steps, and the ECB cut its deposit rate to -50bp.

The balance sheets of the Fed, the ECB, and the BoJ are all now in rising trends as 2019 ends due to continued QE purchases by the BoJ, a new round of QE by the ECB, and the Fed’s program to purchase $60b of Treasury Bills per month for 6 months to insure that reserves are plentiful.
Global Easing Cycle Under Way: EMs

Many of the major EMs are now in a position to ease monetary policy because inflation is slowing (see page 8) and because the Fed has reduced the funds rate, thereby decreasing the risk that EM currencies could plunge.

India and Russia have reduced their policy rates and have indicated they are likely to ease further. Turkey has just cut its policy rate again under pressure from PM Erdogan.

Mexico and Brazil have cut their policy rates, and Indonesia may also cut again.

Don Straszheim expects little new easing action by China during 2020. China has added “flexible” as a new characteristic of monetary policy -- an indication of Beijing’s uncertainty.

Across a wide range of EMs, there have been 65 easing actions in the past four months; see page 10.
Global Easing Cycle Under Way: EMs

1. Brazil slashes rates -50bp.
2. Saudi Arabia cuts rates by -25bp.
3. UAE cuts rates by -25bp.
4. Qatar cuts rates by -25bp.
5. Bahrain cuts rates by -25bp.
6. Philippines cuts policy rate -25bp.
7. Thailand cuts rates -25bp.
8. Peru cuts policy rate -25bp.
9. Serbia cuts policy rate -25bp.
12. Mexico cuts benchmark rate -25bp.
15. Mozambique cuts policy rate -50bp.
16. Paraguay cuts policy rate -50bp.
17. Indonesia cuts rate -25bp.
18. Egypt cuts rates -150bp.
20. Jamaica cuts policy rate -25bp.
22. Dominican Republic cuts key rate -25bp.
23. Chile cuts policy rate -25bp.
24. Ukraine cuts discount rate -50bp.
25. Russia cuts key rate -25bp.
27. Turkey cuts repo rate -3.25%.
29. Brazil cuts selic rate -50bp.
30. Indonesia cuts rate -25bp.
31. Paraguay cuts policy rate -25bp.
32. Philippines cuts key rate -25bp.
33. Egypt cuts rates -100bp.
34. Mexico cuts benchmark rate -25bp.
35. India cuts policy repo rate -25bp.
36. Uganda cuts central bank rate -100bp.
37. South Korea cuts base rate -25bp.
38. Chile cuts policy rate -25bp.
39. Indonesia cuts rate -25bp.
40. Ukraine cuts discount rate -100bp.
41. Turkey cuts repo rate -2.5%.
42. Azerbaijan cuts financing rate -25bp.
43. Russia cuts key rate -50bp.
44. Brazil cuts selic rate -50bp.
45. Saudi Arabia cuts repo rate -25bp.
46. Bahrain cuts key policy rate -25bp.
47. Kuwait cuts discount rate -25bp.
49. Thailand cuts rates -25bp.
50. Belarus cuts refinancing rate -50bp.
51. Serbia cuts key policy rate -25bp.
52. Peru cuts policy rate -25bp.
53. Egypt cuts overnight deposit rate -100bp.
54. Mexico cuts overnight deposit rate -25bp.
55. Zimbabwe halves key rate to 35%.
56. Vietnam cuts deposit rate cap by -50bp.
57. China trimmed the LPR rate -5bp.
58. Indonesia cuts reserve ratio by -50bp.
59. Kenya cuts central bank rate -50bp.
60. Tajikistan cuts refinancing rate -100bp.
61. Moldova cuts base rate -200bp.
62. Brazil cuts selic rate -50bp.
63. Ukraine cuts discount rate -200bp.
64. Turkey cuts repo rate -200bp.
65. Russia cuts key rate -25bp.
Earnings Recovered In Both DVs and EMs But Have Declined Recently

Company earnings have exceeded their prior peaks in DVs (as measured by earnings in the G7). But in EMs, after their recovery, earnings have declined again recently and are down -17% from their prior peak. Commodity price moves (especially oil) are important for the earnings of both producers and importers.

Ongoing global GDP growth is likely to lift earnings in both DVs and EMs in 2020. Despite their recent weakening, EMs are likely to have stronger gains in earnings given their faster GDP growth.
DV Stock Markets Have Outperformed EMs Since 2011, But Both Are Up YTD.

Over the period 2011-2019 ytd, DV stock markets (represented by the G7) increased by +95% -- or +10.5% per year -- while EM markets were up +27% -- or +3% per year. This performance is a complete reversal from 2000-2007 when EM markets far outperformed (+17.9% per year versus +0.6% for DVs).

In 2019 ytd, stock markets are up in both the G7 and EMs, but much more on average in the former. Equity market indexes are up in all of the individual countries shown below, some sharply. Forward P/Es have increased to levels above their 15-year averages for both DVs and EMs.

<table>
<thead>
<tr>
<th>Stock Markets</th>
<th>2019 YTD%</th>
</tr>
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<tbody>
<tr>
<td>G7</td>
<td>+24.8%</td>
</tr>
<tr>
<td>US</td>
<td>+27.4%</td>
</tr>
<tr>
<td>Eurozone</td>
<td>+24.7%</td>
</tr>
<tr>
<td>Japan</td>
<td>+19.6%</td>
</tr>
<tr>
<td>UK</td>
<td>+12.2%</td>
</tr>
<tr>
<td>EM</td>
<td>+14.3%</td>
</tr>
<tr>
<td>Russia</td>
<td>+42.5%</td>
</tr>
<tr>
<td>Brazil</td>
<td>+28.7%</td>
</tr>
<tr>
<td>Turkey</td>
<td>+21.2%</td>
</tr>
<tr>
<td>China</td>
<td>+21.0%</td>
</tr>
<tr>
<td>India</td>
<td>+15.2%</td>
</tr>
<tr>
<td>Mexico</td>
<td>+7.4%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>+1.5%</td>
</tr>
</tbody>
</table>
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