

## CIO Viewpoint

# The global economy is bottoming out

### Investment Solutions

11 November 2019

Something is missing from the global economy's slowdown. [A month ago](#) we concluded that there was no risk of a near-term US recession. Recent data now suggests that globally, we have dodged a recession as the worst of an economic slowdown is already behind us.

The world economy is showing indications that it is going through a recession-free slowdown. The JPM Global Manufacturing index recorded a small, third-straight monthly rise from a July low, the worst risks of a chaotic short-term Brexit have fallen substantially and emerging markets' policy makers have followed the US Federal Reserve by implementing a wave of interest rate cuts with room for more. Crucially, there are also signs that the US and China are edging towards an understanding on trade.

The Trump administration's obsession with imposing tariffs on Chinese imports has dominated the world economy over the past 18 months. As we publish, there are news [reports](#) including some contradictory US denials that China and the US are close to an agreement to phase out tariffs. Whether or not such a 'phase one' accord is close, the development would at least indicate that further tariff escalation is over.

### Curing a trade hangover

Still, trade remains the key to fully curing the global economic hangover and the International Monetary Fund said a deal would "[improve our baseline forecast](#)" for global GDP. Tariffs on Chinese goods have been central to the Trump administration's economic policy. It has pledged to defend US manufacturing jobs from Chinese competition. Yet while US unemployment remains near a 50-year low, jobs in manufacturing are disappearing as the sector drops further into recession. This is the most obvious indication that tariffs are increasing costs and undermining business investments. That may prove politically key in US manufacturing states such as Michigan and Pennsylvania in next year's presidential race.

The US economy expanded 1.9% in the third quarter, compared with 3.4% a year earlier, supported by consumer spending which accounts for more than two-thirds of the country's output. We expect annual GDP growth next year to slow further. Although US consumers will help to prevent a recession as we move into 2020, only the end to Chinese tariffs can truly reverse the slowdown. US unemployment, inflation and wage growth are all moving sideways. While the Fed keeps [rates](#) on hold, and even has room to ease further, these metrics together with no sign that US firms are laying off labour suggest that the economic cycle will continue, rather than stall.



Stéphane Monier  
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### Key takeaways

- Data suggests the worst of the global economic slowdown is past
- The US/China trade dispute shows signs of improvement
- China has the tools to manage a stable slowdown
- While US consumer spending may help avoid a recession, it won't stop a slowdown
- Low economic growth will persist, but the end of the cycle does not look close.

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## Maturing China, Risky Germany

China's economy too is slowing as a long-anticipated result of its maturing economy's move away from manufacturing. We believe that annual economic growth of 6% is sustainable next year (from 6.1% in 2019), as stable core inflation leaves the central bank both the fiscal and monetary tools to support stable and continued expansion. China's currency management is also all about stability, and the economy still has the potential trade dispute buffer, if ever needed, of depreciating the yuan.

Turning to the eurozone, where growth is clearly falling short of its potential, one challenge is the drifting leadership that until [recently](#) we took for granted from Germany. The region's biggest economy also needs significant fiscal stimulus to improve its infrastructure, which, as we have recently argued, runs counter to Germany's budget orthodoxy. Meanwhile, although domestic demand offsets some of the trade headwinds, German car production has plummeted along with its exports to China over the past three years. The European Central Bank has reacted by cutting rates and restarted its open-ended asset purchases, locking in low bond yields and persistently low deposit rates along with its accommodative monetary conditions, through 2020. Unless the US/China tariffs were rapidly scrapped or fiscal policy suddenly much more expansive, we expect to see the region's annual GDP growth dip to 0.7-0.8% next year.

In emerging markets, we anticipate the economic conditions to be in place to strengthen growth next year after a wave of central bank rate cuts in 2019 (from Brazil and Mexico to South Korea and India) following the US Fed's easing and low inflation. This environment should continue into 2020, thanks to a stable US dollar and low oil prices that should make rate hikes unlikely. As elsewhere, a stronger rebound largely depends on whether the US and China can begin to resolve their tariff dispute.

## Recession puzzle

The monetary and credit environment in the US and Europe remains relatively sound, with job markets at healthy levels and economic support provided by consumer spending. The only significant yet-diminishing threat remains from the uncertainties around trade and its knock-on investment impact.

In this persistently low-growth environment, the puzzle of a recession-less slowdown may keep investors scratching their heads for a few more quarters. However, based on available data, the rather lacklustre outlook suggests that the end of the economic cycle is not close, and the worst of the trade-related downturn may even be over.

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