Editorial

Global growth slowdown intensifies

The slowdown of global growth has gathered pace, forcing the Federal Reserve to cut the federal funds rate on two occasions, whereas the ECB has announced a comprehensive easing package. Nevertheless, the slowdown is expected to continue. Uncertainty is pervasive. Companies question the true state of demand faced with slower growth, trade disputes, Brexit worries, geopolitical risk. Corporate investment suffers and may impact households via slower employment growth. The room to boost growth via monetary policy and, in many countries, fiscal policy has become limited, and this is another factor which could weigh on confidence. Surveys of US corporate executives point towards a high concern about recession risk and the US yield curve inversion adds to the unease. However, the picture provided by a broad range of leading indicators is, at least for the time being, less bleak.

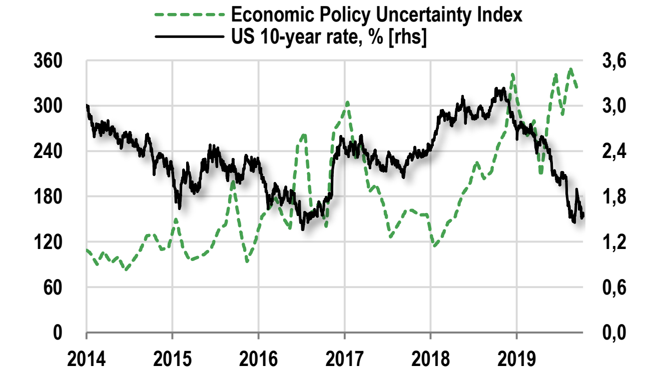
Slowdown gathers pace

The declining pace of economic growth has become a truly global phenomenon. Chinese growth continues to outpace the performance in the Western world to a very significant degree, but at 6.2% in the second quarter, it is getting close to the psychologically important 6.0% barrier. The trend towards slower growth should continue in the short run on the back of a cautious policy stance in boosting growth and a difficult international environment. The pace of growth is also slowing in the US, where corporate investment is weakening, although household consumption is resilient. As a welcome exception, Japanese growth has been stronger than expected early on this year, supported by domestic demand. Exposure to China, a subdued outlook for international trade and the fall-out from the VAT increase on consumption paint a challenging picture for the near term. In the eurozone, the good performance in the first quarter (+0.4% growth) has been followed by a meagre 0.2% growth in the second quarter. Private consumption has been resilient, underpinned by declining unemployment and dynamic wage growth. Investment has slowed, in part due to the high level of uncertainty. Within the eurozone, the divergence has increased. Germany, where the manufacturing sector is under intense pressure, is in a technical recession, whereas the French economy is very resilient. Another divergence is between industry and services, with the former suffering more given its higher exposure to international trade and to trade uncertainty.

Central banks have reacted but doubts about the effectiveness

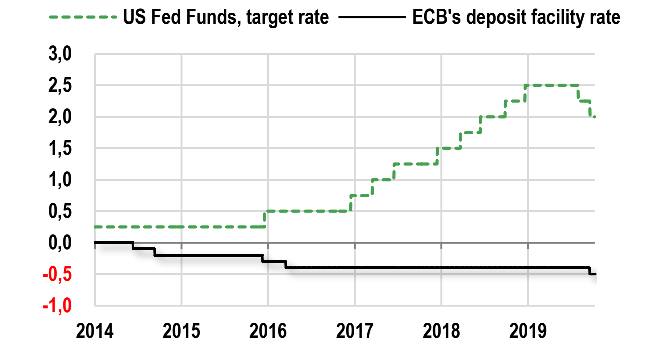
As a consequence, the Federal Reserve and the ECB have reacted by easing policy. This represents probably the biggest sea change compared to expectations about the world economy at the start of the year. Their reaction is very much proactive. In the US, the policy rate is being cut whilst the unemployment rate is at a 50 year low. In the eurozone, the labour market is still robust but concerns about the phase of soft growth lasting longer than expected, which in turn weighs on outlook for inflation and its convergence towards the target, have led the ECB Governing Council to a comprehensive easing package. Critics of this stance have become more vocal considering that the asset purchase program has been resumed. This has led to expressions of disagreement by Governing Council members. The introduction of state-dependent forward guidance, which implies that current policy is maintained (or eased further) as

1- Economic uncertainty is pervasive



Source: Economic Policy Uncertainty, Datastream, BNP Paribas

2- Central bank policy rate, %



Source: Federal Reserve, ECB, BNP Paribas

long as inflation hasn't converged sufficiently, and in a lasting way, to the target has also met criticism in some circles because it implies interest rates will remain very low and, for some, even negative for quite some time. A priori, this should support growth. Whether this will show up in the numbers depends in particular on confidence, i.e. on a much needed decline in uncertainty.

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