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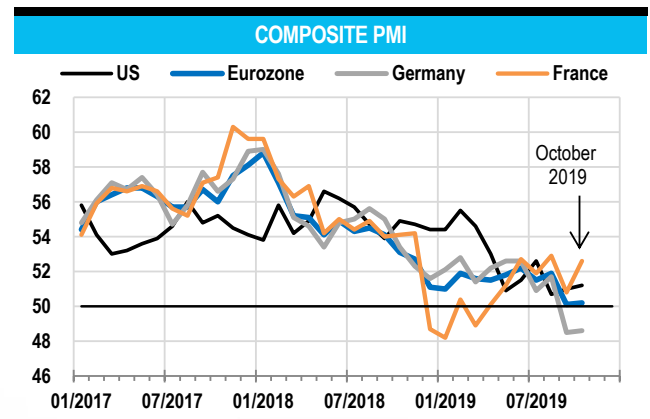
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Uncertainty: peaking or just migrating?

■ The US-China trade conflict and Brexit have been acting as a headwind for growth for a considerable time now ■ Recent developments have raised expectations that these sources of uncertainty may have peaked ■ Should it turn out to be the case, this could spur spending by unleashing pent-up demand by companies or households ■ However, in an environment of slowing global growth and, quoting the IMF, a precarious outlook for next year, we probably will see a more limited reaction, with other sources of concern taking over from the previous ones: uncertainty may have peaked in certain areas, but is likely to migrate to other.

It is tempting to argue that uncertainty has peaked. After all, two weeks ago, US and Chinese negotiators have reached an interim agreement which hopefully will lead to the signing of a trade deal before the end of the year. Concerning Brexit, which has been a major source of uncertainty for business in the UK and in Europe, it now seems that the risk of a disorderly departure from the EU has declined quite significantly. However, in both cases, there are arguments to cool down our enthusiasm. The interim agreement between the US and China is limited in scope and, thus far, has simply avoided that tariffs would be increased further. It is doubtful that this would have any economic impact to speak of and attention will probably immediately shift to what happens next: more talks or more threats? On Brexit, the possibility of new elections has caused uncertainty to increase again. In case of an orderly departure, we will see a migration of uncertainty once the negotiations about the future relationship and its economic repercussions will be grabbing headlines.

Trade disputes and Brexit are sources of exogenous uncertainty. They are distinct from the usual cyclical developments but they can severely weigh on growth. Major growth slowdowns like the one that we have been experiencing globally since last year, generate endogenous uncertainty. Doubts creep in about the validity of business plans and growth assumptions or about how bad things could turn out to be. As such, it is inherently linked to the business cycle. Exogenous uncertainty, via its negative impact on domestic and/or external demand can reinforce the endogenous uncertainty. One would assume that a reduction in exogenous uncertainty would spur spending and reduce doubts about the growth outlook, e.g. by unleashing pent-up demand: to the extent that companies have simply put investment plans on hold, they might eventually decide to implement them after all when visibility has improved. At the current juncture, they will probably not be in a rush however: global growth is slowing, the IMF describes next year's outlook as precarious, survey data for the manufacturing sector have dropped to very low levels in many countries and the services sector has ended up being impacted as well. In this respect, the stabilisation of the flash composite PMIs for October in the US, the eurozone and Germany and the ifo climate in the latter is welcome news, but their levels are low or, in Germany's case, very low. France, which saw an increase of the composite index is a welcome exception. Another development to be closely monitored is the Conference Board's index of leading indicators for the US, which has been declining for two months in a row, albeit it to a very limited extent. To conclude, uncertainty may have peaked in some areas but will quite likely migrate to others with economic agents trying to understand what is the true state of the global economy.



Source: IHS Markit, BNP Paribas

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