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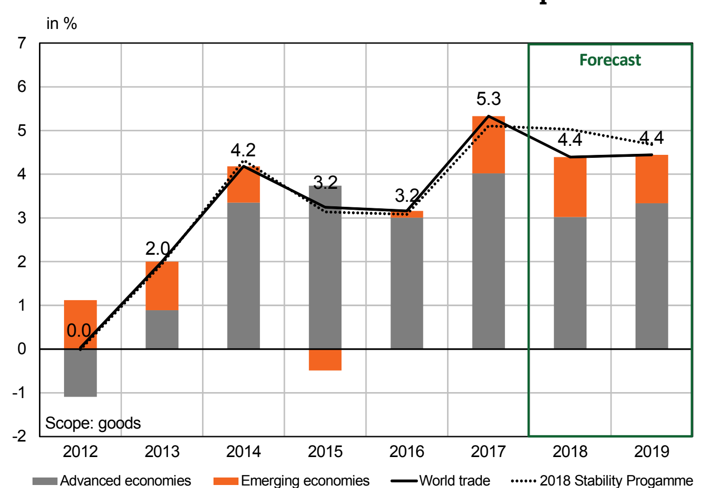
Global outlook in autumn 2018: growth still robust despite headwinds

- After a sharp climb to 3.7% in 2017, the strength of global growth is set to last throughout 2018 and 2019 (3.8%), driven by an acceleration of economic activity in the United States and many emerging countries, in spite of a downturn in the other major advanced countries.
- In the United States, the pace of growth is expected to pick up markedly in 2018 on the back of fiscal stimulus, prior to a moderate slowdown in 2019 mainly due to protectionist measures. Conversely, in the United Kingdom, the economy is set to slacken in 2018, levelling off at a more modest rate in 2019 as uncertainties surrounding Brexit weigh on investment and trade. As for Japan, GDP should slump in reaction to the slowdown in exports and a drop in housing investment.
- In the euro area, projected growth rates remain solid for 2018 and 2019, despite a downturn in the wake of growing political and trade uncertainties, a less favourable international environment than in 2017 (stronger Euro and higher oil prices), and increased labour market tension. Growth will likely be driven by buoyant global trade and strong domestic demand, underpinned by high levels of corporate and consumer confidence. Germany, Spain and Italy are the three major European countries where it is expected to decline.
- In emerging economies, growth in 2019 is set to climb in Brazil and India, remain stable overall in Russia, but fall sharply in Turkey. Chinese growth should gradually slow as measures of monetary and fiscal stimulus taper off.
- Vibrant global trade is expected to contract marginally (5.5% in 2017, 5.2% in 2018 and 4.6% in 2019), particularly under the combined effects of a slowdown in European imports and gradually weaker Asian imports. Though world demand for French goods is set to remain buoyant in 2018, it should decelerate more than global trade due to its greater exposure to the downturn in European trade.
- Uncertainties surrounding this scenario have heightened in recent months, and include: consequences of protectionist measures; Brexit negotiations; the political situation in Italy; Chinese management of fiscal and financial imbalances; risk aversion in reaction to problems in Turkey; the high level of US stock markets.

Growth in world demand for French exports*



Source: DG Trésor.

** The forecasts and data in this document were finalised on 21 August 2018.*

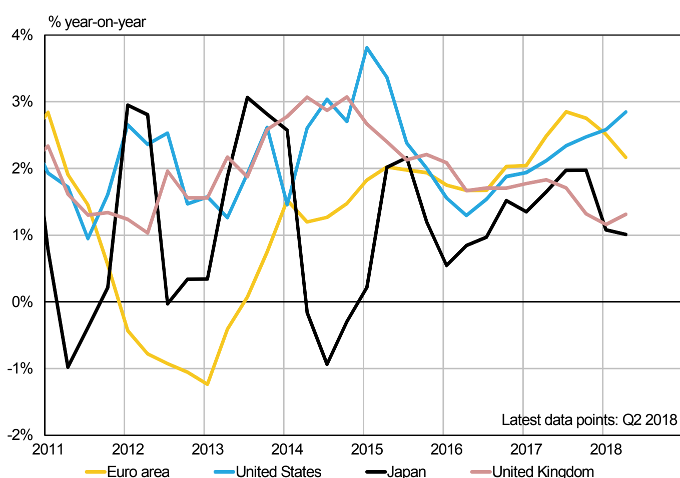
1. Global economic activity has remained strong throughout the first half of 2018, but tensions are mounting

The global economy has remained strong over recent months despite signs of a slowdown caused by the increasing tensions surrounding US trade policy, political uncertainties in Italy and over Brexit, as well as the rise in oil prices. This is mainly reflected in flagging global trade and economic activity in advanced economies, aside the United States. Investors in financial markets have reacted by a marked shift towards safe-haven securities, particularly bonds.

1.1 In advanced economies signals were less upbeat in mid-2018, but economic activity remains vibrant and the surveys are positive

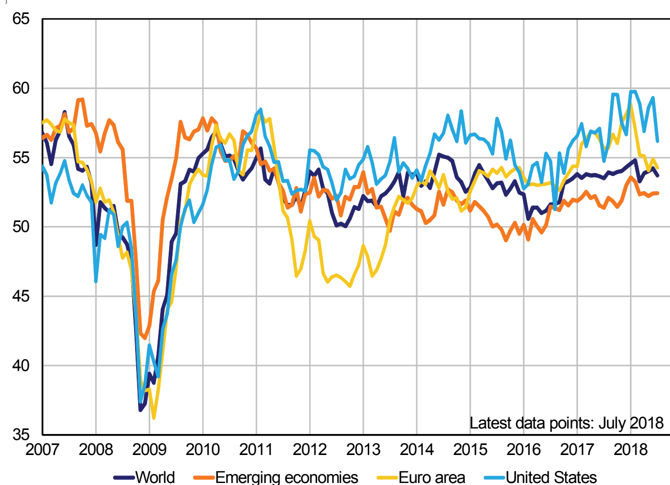
After overall acceleration in 2017, economic activity in the major advanced economies showed varying trends (see Chart 1). In the euro area, growth fell mainly owing to the slowdown in exports. Aside from temporary factors weighing on the economy, the business environment took a noticeable downturn in the first half of the year (see Chart 2), with surveys nevertheless remaining in line with solid growth levels. In the United Kingdom, activity continued to slow over the same period, due to falling trade since the start of the year and flagging investment, likely in reaction to Brexit. In Japan, growth rebounded after an unexpected downturn in the first quarter as lagging commerce with China took its toll. Growth in the United States (US) remained robust in the first half of 2018, driven by corporate investment on the back of fiscal stimulus measures, but also by the rise in oil prices for the hydrocarbon industry. Surveys remain high across the Atlantic.

Chart 1: GDP growth in the main advanced economies



Sources: National statistical institutes.

Chart 2: Business environment[a]



Sources: ISM, Markit.

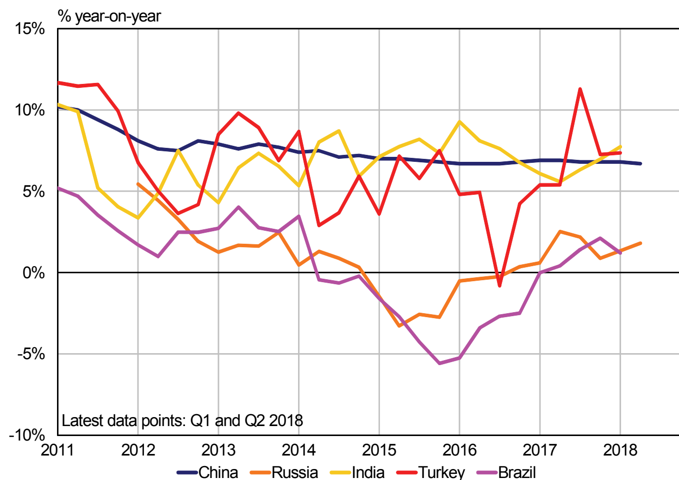
a. The PMI (Purchasing Manager's Index - Markit) for the euro area, emerging economies and the world, and the ISM index (Institute for Supply Management) for the United States.

1.2 Emerging economies have faced mounting uncertainties since the start of 2018 against a backdrop of rising interest rates and aversion to risk

Growth weathered well in emerging economies at the start of 2018 (see Chart 3). It remained strong in China, shored up by prolonged monetary and fiscal measures. Turkey also maintained robust growth at the start of the year, backed by high levels of exports and considerable fiscal stimulus prior to elections in June. After the disappointment of 2017, growth gathered pace in India largely owing to investment taking off in the wake of a rebound in credit, a backlash from the massive downturn at the beginning of 2017 brought on by the demonetisation of the 500 and 1,000 rupee banknotes in late 2016. In Russia, growth continued its modest upward trajectory, reaping the benefits of the rise in oil prices. Conversely, economic activity in Brazil fell against a backdrop of flagging investment and exports. Economic surveys point to a slight downturn. Confidence in India and China is relatively upbeat, whereas in Brazil it deteriorated throughout the first half of the year, aggravated by political uncertainties ahead of the presidential elections in autumn. It also dwindled in

Russia, mainly in reaction to further US sanctions in April. However, confidence was particularly damaged in Turkey where the lira has plummeted 50% against the dollar since the start of the year amidst growing tensions with the United States and mounting fears over the central bank losing its independence.

Chart 3: GDP growth in the main emerging economies



Source: National statistical institutes.

1.3 Oil prices have risen while financial markets reflect monetary policy returning to normal and growing political and trade uncertainties

The Brent oil price soared until spring 2018 topping $75/ barrel in May, driven mainly by strong demand, limited supply, and tensions in the Middle East (see Box 1). However, a boost to supply under the combined effects of the OPEC/non-OPEC agreement on 22 June, whereby each signatory country ramped up output by 1 Mb/d, increased US exports in June, and Libya's return to the market in July, has given rise to a hiatus followed by a gentle ease in oil prices since the summer. At the same time, demand fell, particularly in Europe, in the wake of slackening growth and the previous rise in oil prices. Lastly, rising trade tensions have also exerted downward pressure on oil prices.

Advanced economies' gradual phasing out of accommodative monetary policies continued at varying paces. In June, the European Central Bank (ECB) decided to put a progressive end to its asset purchase programme, provided the inflation outlook is confirmed. Monthly net purchases are to be scaled back from €30bn since January, to €15bn from October to December, with a view to ending the programme in 2019. The ECB also pledged not to raise key interest rates before the end of summer 2019. Against this backdrop, short and long-term rates are set to rise gradually and overall financial conditions remain accommodating in the euro area over the forecast period. Meanwhile, the US Federal Reserve (Fed) continued to tighten its monetary policy by raising its key rate by 25 basis points on two occasions (in March and June), bringing its target range up to 1.75-2%. Five more hikes at the same rate are expected before end-2019, according to the median estimate implied by the members of the Federal Open Market Committee (FOMC). Furthermore, monthly reductions to the Fed's balance sheet have increased since July from $18bn for Treasuries and $12bn for mortgage-backed securities, to $24bn and $16bn, respectively. In parallel, the Bank of England raised its key rate by 25 basis points to 0.75 % at the beginning of August. Another similar rate hike is forecast between now and end-2019; its balance sheet remains unchanged. Lastly, the Bank of Japan continues to push its highly expansionary monetary policy, maintaining its long-term yields strategy targeting almost 0% for 10-year government bonds.

Financial markets reacted to rising concerns over trade and politics. Thus, in Italy, government bond rates soared on the back of political uncertainty, in part driving up Spanish and Portuguese yields. Conversely, French and German debt yields dropped in the wake of an investor "flight" towards safe-haven securities, as well as weak inflation in the euro area and reassuring statements from the ECB about its accommodative policy. In the United States, long-term yields shot up on the back of monetary policy tightening, despite downward pressure from uncertainties over trade driving investors towards safe assets. The rising concerns also negatively affected stock market indexes, which took a downturn at the end of the first half of the year. On the currency markets, after a steep climb throughout 2017, the euro has remained steady overall since the Stability Programme. It fell against the dollar owing to the slowdown in economic activity and concerns over the political situation in Italy, but was shored up by the drop in the yuan and the rouble. Conversely, the dollar appreciated throughout April and May, underpinned by robust growth, and the rebound in inflation and US long-term rates.

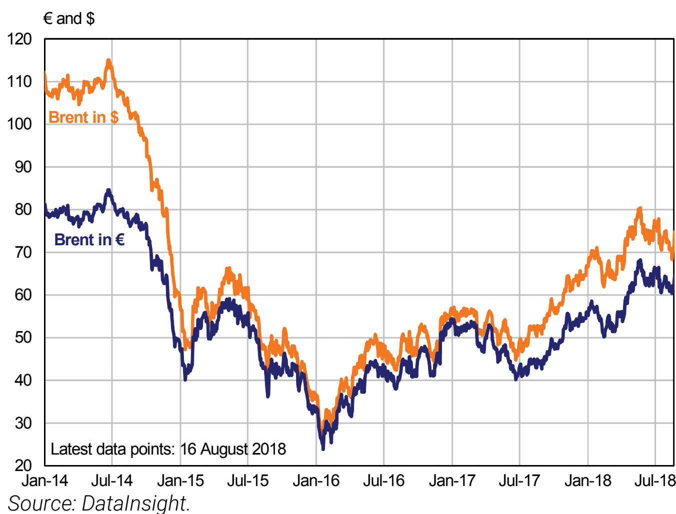
Box 1 : The effects of the rise in oil prices are expected to differ across advanced economies

The Brent oil price climbed steadily over the year up to spring 2018, breaking the highest threshold seen since the end of 2014 (see Chart 4). This was mainly attributable to a rebalancing of supply and world demand for oil. On the one hand, the strength of recent economic growth drove up demand for oil. On the other, coordinated efforts to cap production under the OPEC/non-OPEC Vienna agreement, applied at the beginning of 2017, gradually carried over into an actual decline in the daily output of these countries. Thus, oil inventories in OECD countries fell to their five-year average (see Chart 5), having been considerably higher for the two previous years. Furthermore, unforeseen interruptions to production in certain countries, particularly Venezuela and Libya, played a large part in soaring oil prices as did geopolitical tensions in the Middle East, notably the US's withdrawal from the Iranian nuclear deal.

Rising oil prices underpin inflation which in turn curbs consumption and growth in importing countries. In the short term, they weigh on purchasing power by driving up petroleum product prices. The inflationary impact on other prices is indirect and more gradual, first becoming apparent in products reliant on petroleum-intensive production. In the middle-term, it can spawn "second round effects" particularly in relation to wages. The reasons behind the rise in inflation in advanced economies since March have mainly been short-term, energy inflation having soared 7.4 points in the euro area and 5.1 points in the US between March and July, whereas core inflation has remained virtually static, (unchanged in the euro area and up 0.2 points in the United States).

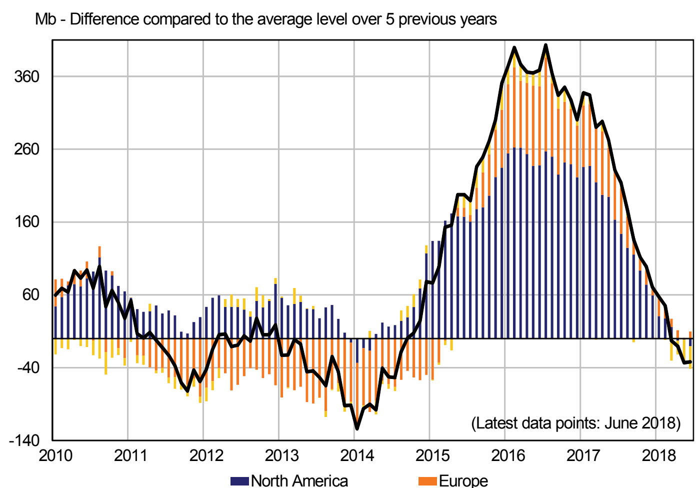
Nevertheless, contrary to euro-area economic activity, the US economy has benefitted from the rise in oil prices. Over the last ten years, the United States has considerably ramped up hydrocarbon production thanks to the development of unconventional oil extraction techniques. Total crude oil output in the United States doubled from 5 million barrels a day (Mb/d) in 2008 to just over 10 Mb/d in February 2018[a]. The United States therefore plays a growing role in the global market, despite remaining a net importing country. Against this background, the positive effects of high oil prices on the US economy are twofold: they bolster margins in the US hydrocarbon sector and stimulate investment, particularly investment in infrastructure, as drilling increases.

Chart 4: Brent oil price in dollars and euros



Source: DataInsight.

Chart 5: Petroleum product inventories held by the sector have dropped significantly in OECD countries



Source: IEA August 2018.

a. According to the US Energy Information Administration.

2. Global growth is set to remain strong in 2018 and 2019

After a marked acceleration in 2017, global growth is expected to remain robust in 2018 and 2019, driven by strong economic activity in the United States and emerging economies (see Chart 1), although a slowdown is forecast in other major advanced economies.

2.1 US growth boosted by expansionary fiscal measures

In the United States, projections point to growth stepping up in 2018 (2.8% compared to 2.3% in 2017) spurred by vigorous domestic demand underpinned by fiscal stimulus, [1]thus boosting consumption and corporate investment, which is also stimulated by the rebound in oil prices (see Box 1). The labour market is beginning to show signs of tension: low unemployment levels are set to drive up wage growth, underpinning private consumption and inflation. Economic forecasts for 2019 dip marginally to 2.6%, mainly constrained by monetary policy tightening, US protectionist measures and retaliation from trading partners (see Box 2) weighing on trade. Exports are also expected to suffer from less vibrant world demand and a strengthening dollar.

In Japan, economic activity will likely drop sharply (1.0% in 2018, 1.1% in 2019, after 1.7% in 2017). Exports are expected to slow in 2018, constrained by falling sales to Asia in the first half of the year. Residential investment should slump in 2018 in reaction to the deterioration in lending conditions. Moreover, non-residential investment is set to decline as support from investment ahead of the 2020 Tokyo Olympics dwindles. Due to strong pressures on the labour market as well as a wage stimulus package,[2] wages should pick up, thereby driving core inflation.

In the United Kingdom, robust activity at the end of 2016, despite a substantial slowdown thereafter, boosted the overall positive economic results in 2017 (1.7%, after 1.8% in 2016). The downward trend was carried over into the beginning of 2018 and is set to continue throughout the year before plateauing at a modest rate in 2019 (1.3% in 2018 and 2019). Despite the gradual slide in inflation and labour-market tension, consumption should be sluggish, constrained by lagging real wages as uncertainties surrounding Brexit negotiations take their toll. Investment and trade will also likely suffer from the prospect of Brexit,[3] whereas its impact on economic activity in France and the euro area is expected to be minimal over the forecast period.[4]

Box 2 : The impact of US protectionist measures should remain moderate over the forecast period

The United States (US) has already applied additional customs duties, namely:

- Increases of between 20 and 50% on US imports of washing machines and solar panels, initiated in January 2018 and totalling around $10bn.
- Additional customs duties on US imports of steel (25%) and aluminium (10%) which came into force in March and June 2018. The proportion of US imports to which these duties apply is relatively small (in the region of $40bn, namely 0.2% of GDP). The measure will particularly affect Canadian and European Union (EU) exports, (representing $12bn and $8bn, respectively). Some US trading partners have adopted similar retaliatory measures.
- Additional duties (25%) on a list of goods totalling $50bn of imports from China which came into force in July-August 2018, prompting the Chinese government to resort to comparable retaliatory measures.

Further protectionist measures and procedures have been announced. They could apply to considerably higher amounts of trade, but have yet to be put into effect. They are:

- The terms of the North American Free Trade Agreement (NAFTA), which are currently under renegotiation.

(1) See Box 1, "US tax reform and the 2018 Bipartisan Budget Act" in Boisset L. , François L. , Hentzgen C., Lecumberry J. , Osman Y. and M. Salomé (2018), "World economic outlook in spring 2018: growth still strong", *Trésor-Economics* no. 218, March.

(2) See M. Ben Yaala (2018), "Is higher wage growth on the horizon in Japan?", *Trésor-Economics* no. 220, April.

(3) Our forecast scenario uses the conventional assumption of a transitional Brexit agreement between the United Kingdom and the European Union taking effect in March 2019, as decided by common accord between the United Kingdom and the European Union in March 2018. This is a working assumption that does not make any predictions as to the outcome of ongoing talks between the United Kingdom and the European Union.

(4) See Box 2, "What effects will Brexit have, a year after the referendum?" in Bernard J.B., François L., Gillet T., Lecumberry J., Osman Y. and M. Salomé (2017), "The global economic outlook in September 2017: signals remain upbeat," *Trésor-Economics* no. 205, September.

- President Trump has talked about charging additional tariffs on Chinese goods and services worth $200bn (even citing US imports from China in their entirety, namely $505bn in 2017, whereas Chinese imports from the US totalled $130bn). A corresponding list of the $200bn Chinese goods potentially to be subject to additional duties of 10 to 25% has been published.
- An investigation concerning the car industry is underway as further customs duties could be applied to motor vehicles and spare parts, of which US imports total about $300bn, namely 1.7% of GDP, including $60bn from the EU (and $1bn from France). Moreover, the US car production value chain is largely transnational,[a] thus ratcheting up the negative implications of these duties. Nevertheless, the precise scope of the imports concerned by possible measures (in terms of products and exporting countries) is yet to be announced. Moreover, Jean-Claude Juncker, President of the European Commission, and President Trump reached an agreement on 25 July whereby possible restrictive measures on automobile imports from the European Union to the United States were suspended.

In the very short term, the shock wave sent by US protectionism has undermined confidence and stoked uncertainties, the mounting tensions over the last few months having likely played a part in the business environment downturn in advanced economies.

Aside the tensions, the measures themselves would affect the US by driving up trading prices, thereby spurring inflation and pushing down domestic demand and exports, as US competitiveness fell. This would have an impact on US demand for European goods which could be offset in part by a transferal of China-US trade to Europe.

In the long term, repercussions will likely involve adjustment costs to global value chains and adverse effects on the productivity of the countries in question (less use of comparative advantages, returns to scale, competitiveness and dissemination of innovation). Notwithstanding, the backlash should go virtually unnoticed before 2019.

Our forecast scenario incorporates the protectionist measures already in force and the additional 10% duties on $200bn of US imports from China in 2019, as well as Chinese retaliation. These policies are expected to shrink US growth by 0.2 points in 2019.[b] Their global impact should be slight, and France in particular will likely remain virtually unscathed by the measures themselves. Even if the Trump administration adopted all the policies presently under consideration, direct consequences for France would be minimal. Damage to the euro area over the forecast period mainly lies therefore in the uncertainties associated with these measures. The main risk for Europe is large-scale escalation as a trade war would severely impair global growth. According to the Banque de France (July 2018), a widespread 10% rise in tariffs would reduce global GDP by 1.0% within two years.

a. See J. Anne-Braun (2018), "The US automotive industry: challenges and outlook", *Trésor-Economics* no. 214, January.
b. See IMF Surveillance Note for the G-20 finance ministers and central bank governors' meetings from 21-22 July 2018 (https://www.imf.org/external/np/g20/pdf/2018/071818.pdf).

2.2 Euro area economic activity is set to slow, but remains upbeat

Euro area economic activity is expected to maintain strong momentum despite a moderate slowdown (2.1% in 2018 and 2019, after 2.5% in 2017). The downturn is attributed to growing trade and political concerns, a less vibrant global environment than in 2017 in the wake of the former strengthening of the euro and the rise in oil prices, as well as mounting pressures on the labour market. Strong global trade is set to underpin growth, while the sustained high levels of consumer and corporate confidence should bolster domestic demand. The stronger pace of wage growth should offset adverse effects of the gradual ease in employment on purchasing power. Investment should stay on track, backed by high production capacity utilisation rates. In all, growth is set to remain above its potential rate. Despite the levelling-off of energy prices,[5] overall prices should rise slightly in 2019 as wage growth gradually carries over into core inflation. Moreover, the partial rebalancing of labour costs across the euro area is set to continue into 2019, with slightly higher German inflation and labour costs than the euro area average.[6] Nevertheless, the scale of Germany's current account surplus will remain unchallenged by the likely moderate pace of the convergence, which should remain incomplete over the forecast period.[7]

(5) Under the conventional assumption of freezing oil prices in forecasts.
(6) See D. de Waziers (2017), "Rationale for the new wage momentum in Germany", *Trésor-Economics* no. 202, July.
(7) See Bechetoille M., Titouan B., Campagne B. and D. De Waziers (2017), "How to explain Germany's strong current account surplus", *Trésor-Economics* no. 209, November.

In Germany, growth is expected to fall slightly, weighed down by pressure on the labour market (2.0% in 2018 and 2.0% in 2019 after 2.5% in 2017).[8] Job creation is set to lag owing to the slight deceleration of the labour force and scarcity of labour in some sectors. Consequently, wages should accelerate following higher wage negotiations. Investment should continue to shore up domestic demand while fiscal policy should ease.[9] Exports should slow considerably in 2018 in the wake of the downturn in the first half of the year coinciding with waning confidence from exporting industries, but German export performance should recover gradually in 2019.

In Italy, given the high levels of uncertainty ahead of the Italian Budget Bill, we have based our scenario on a neutral fiscal policy, which has not factored in measures announced by the coalition government. The economy is forecast to slow (1.2% in 2018 and 1.1% in 2019, after 1.5% in 2017), as the social and tax measures underpinning employment and investment progressively expire. Employer exemptions from social security contributions should steadily taper off, thus undermining job creation in 2018 and 2019. Having helped stimulate employment since 2016, these exemptions have been progressively scaled back ever since. Robust investment should be sustained in 2018 but flag in 2019 with the elimination of super-amortisation measures. In all, domestic demand should drop over the forecast period.

In Spain, the economy should stay on track in 2018 (2.7% after 3.1% in 2017) and 2019 (2.6%) despite a moderate slowdown. Declining global trade and the previous strengthening of the euro should hit foreign trade while the moderate drop in employment should weaken domestic demand. Nevertheless, the Budget's new expansionary measures, mainly aimed at households, should curb the slowdown as from mid-2018 by boosting growth a ¼ of a point in 2018 and 2019. Consumption should therefore be sustained and the rate of household savings rebound after their nosedive since the financial crisis.

2.3 Growth should take a moderate upturn in emerging economies

In Brazil, growth should consolidate its vibrant recovery in 2018 and 2019, after a two-year recession in 2015 and 2016. In 2018, it should reap the benefits of weak inflation, despite prices climbing over the last few months (4.5% in July compared to 2.9% in May), and the ongoing low level of key rates (currently at 6.50% further to a drop of 775 basis points since October 2016). Nevertheless, mounting political uncertainties ahead of the presidential elections in October will likely dampen growth. As concerns abate, recovery is set to gather strength in 2019, despite fiscal tightening expected after the elections.

In India, economic activity wound down significantly in 2017 in the wake of the banknote demonetisation in November 2016 and the introduction of the Goods and Services Tax (a single national VAT) in mid-2017. As these temporary negative effects subside, growth is expected to accelerate sharply in 2018. The deteriorating quality of bank assets on account of the high and rising proportion of bad loans in the credit stock raises the risk of credit slowing in the medium term, with a knock-on effect on domestic demand, a structural driver of the Indian economy. This was the reason behind bank loans stagnating in June 2018, further to a rebound after the demonetisation. Moreover, loans to industry are sluggish. Growth should therefore level off in 2019.

In Russia, economic recovery is set to continue thanks to the recent rebound in oil prices, low inflation and the slackening pace of fiscal consolidation. The rise of the standard rate of VAT from 18% to 20%, scheduled for 1 January 2019, is expected to slow economic activity while stoking inflation and weighing on private consumption. Moreover, an ageing and shrinking population, weak investment, a high level of corruption and low level of economic diversification curb the potential rate for growth.

(8) Working-day adjusted figures. German growth in unadjusted working-day figures was 2.2% in 2017.
(9) The new government's budget confirms expansionary measures announced by the preceding administration and by the coalition agreement in March (1.5 GDP points of additional public spending and tax cuts from 2018 to 2021). The provisional distribution of the additional public spending is nevertheless concentrated towards the end of the period, thereby providing minimal support to economic activity over the period forecast here.

In China, a moderate slowdown in economic activity is expected in 2018 and 2019 as the pace of reform eases in a bid to offset the negative effects of trade tensions with the US and increased aversion to risk against a backdrop of the economic crisis in Turkey. Domestic imbalances, particularly in finance, nevertheless remain high (see Box 3) and are set to curtail medium-term growth. This scenario largely coincides with those of major international organisations.

In Turkey, economic activity is expected to slow considerably in 2018 and 2019. The tighter fiscal policy after the presidential and parliamentary elections in June 2018 should weigh on domestic demand. The sharp depreciation of the lira since the beginning of the year is set to push up inflation even further, while private investment will likely be hit by fears over restrained central bank autonomy and tensions with the US. The country, heavily reliant on foreign capital inflows, particularly those in the short term, will likely see hefty outflows of capital stemming from the substantially greater aversion to risk on the markets.

Box 3 : China accounts for a large share of the rise in emerging economy debt

Total public and private debt in emerging economies has soared since 2008, up 83 GDP points to about 205% of GDP in 2017. This raises the question of the sustainability of debt against a backdrop of monetary policy normalisation in advanced economies. In particular, the domino effect of US rate hikes could entail *(i)* a rise in the cost of capital in emerging countries if their central banks react in order to avoid too wide a spread in rates, *(ii)* capital outflow from the most vulnerable emerging markets to advanced economies proposing higher returns, thereby causing their currencies to depreciate and *(iii)* valuation effects of dollar-denominated debt, as the value of the outstanding amount and servicing costs of this debt rise owing to the depreciation of emerging market currencies.

Despite a high aggregate level of debt, risk of default is not evenly spread. Chinese debt soared from roughly 170% of GDP in 2008, to nearly 300% in 2017, making it largely responsible for the total rise in the debt of emerging economies. By removing China from the equation, the rise in emerging-economy debt over the same period is considerably lower, around 25 GDP points, at 125% of GDP in 2017, and essentially driven by India and Brazil. Foreign debt, set on a moderate upwards trajectory over the last few years, fell considerably after peaking at the end of the 1990s. Moreover, debt in emerging economies is mainly denominated in local currencies, (90% in 2017, 70% excluding China), although disparities between countries are significant; for example, more than half of Argentinian and Turkish debt is in foreign currencies.

The same observation can be made when focusing on the debt of non-financial corporations (NFC) which accounts for the lion's share of the total increase in debt (46 out of 83 points since 2008). Chinese non-financial corporation debt climbed sharply to 164% of GDP in 2017, compared to 97% in 2008. Non-financial corporation debt has risen modestly in the other emerging economies since 2008, under 10 GDP points, at 42% of GDP in 2017. Aside China, (67 GDP points), the increase is nevertheless significant in Turkey (34 GDP points), while remaining contained in the other economies under study (7 GDP points on average). A third of non-financial corporation debt in emerging economies, excluding China, is denominated in foreign currencies, thereby increasing the risk of extra charge in the event of depreciation. This share is particularly high in Mexico (73%), Turkey (54%), Indonesia (46%), South Africa (42%) and Argentina (40%), whereas it is minimal in China (5%).

Table 1: Growth forecasts*

GDP (annual average, %)	Average 2000-2007	2014	2015	2016	2017	2018 (forecasts, working-day adjusted)	2019
World growth[a]	**4.5**	**3.5**	**3.4**	**3.2**	**3.7**	**3.8**	**3.8**
Memorandum: world growth forecast in the 2018 Stability Programme	*4.5*	*3.5*	*3.4*	*3.3*	*3.7*	*3.8*	*3.8*
Advanced economies[b]	**2.6**	**2.0**	**2.3**	**1.7**	**2.4**	**2.3**	**2.2**
United States	2.7	2.5	2.9	1.6	2.2	2.8	2.6
Japan	1.5	0.3	1.4	1.0	1.7	1.0	1.1
United Kingdom	2.8	2.9	2.3	1.8	1.7	1.3	1.3
Euro area[c]	**2.2**	**1.4**	**1.9**	**1.8**	**2.5**	**2.1**	**2.1**
Germany	1.6	2.2	1.7	2.2	2.2	2.0	2.0
Italy	1.5	0.1	1.0	0.9	1.5	1.2	1.1
Spain	3.7	1.4	3.4	3.3	3.1	2.7	2.6
Other advanced economies	3.9	3.0	2.1	2.2	3.2	2.5	2.5
Emerging economies[b]	**6.6**	**4.7**	**4.3**	**4.4**	**4.7**	**4.9**	**5.0**
Brazil	3.6	0.5	−3.6	−3.5	1.0	1.5	2.0
China	10.5	7.3	6.9	6.7	6.9	6.6	6.3
India	7.1	7.4	8.2	7.1	6.2	7.4	7.4
Russia	7.2	0.7	−2.5	−0.2	1.5	1.9	1.5
Turkey	5.4	5.2	6.1	3.2	7.4	4.0	2.5
Other emerging economies	4.2	3.5	3.4	3.6	3.3	3.8	4.1
World demand for French exports[d]	6.9	4.2	3.2	3.2	5.3	4.4	4.4
World trade[e]	7.5	4.1	2.1	2.0	5.5	5.2	4.6

a. Data for 2017 is taken from national accounts and supplemented by the DG Trésor's forecasts as needed.
b. Aggregate figures for advanced economies and emerging economies are estimated using IMF forecasts, adjusted using DG Trésor forecasts covering the countries in the table above and France, and adjusted (for past figures) by revisions to the national accounts.
c. Aggregate figures for the euro area are based on quarterly accounts adjusted for working-day variations. Aggregate forecasts are extrapolated from DG Trésor forecasts for Germany, France, Italy and Spain and from the European Commission's forecasts for the other countries.
d. World demand covers 39 countries and organisations (Germany, Belgium, Italy, Spain, US, UK, OPEC, Netherlands, China, Switzerland, Japan, Russia, Poland, Turkey, Brazil, Sweden, South Korea, Hong Kong, Singapore, Canada, Morocco, Portugal, Austria, Czech Republic, Hungary, Australia, India, Malaysia, Mexico, Thailand, Ireland, Denmark, Greece, Slovakia, Norway, Taiwan, Finland, Philippines and Argentina), which receive 86% of French exports.
e. World trade covers 40 countries (the 39 listed above plus France), which receive 85% of world exports.

** These forecasts were finalised on 21 August 2018.*
Source: IMF, July 2018 WEO update; European Commission, July 2018, DG Trésor calculations and forecasts.

3. World demand for French goods, while slowing significantly, should remain robust in 2018 and 2019

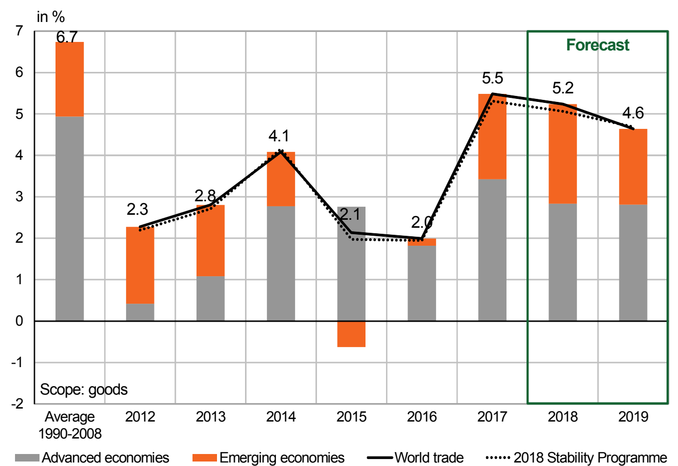
After two years of weak growth, world trade clearly accelerated in 2017, posting its highest growth since 2011 (up to 5.5% from around 2.0% in 2016). This acceleration was driven partly by global economic growth, but particularly by several factors increasing the trade content of growth: significantly higher growth in the euro area (a region of intense trade due to imports/exports among its member countries); a recovery in investment, which includes high import content; a recovery of imports in Asia, and in Russia after a three-year fall.

World trade is set to drop (see Chart 6) to 5.2% in 2018 (from 5.5% in 2017). Despite robust Asian and US imports riding the wave of fiscal stimulus, global trade will likely suffer from a decline in imports in the following countries: euro-area countries, reflecting the downturn at the start of 2018 and weaker economic activity; the United Kingdom, as the repercussions from the Brexit vote take a hold; Turkey, in the wake of tumbling economic activity; and Russia and India whose imports are expected to lag after the strong contribution they made to trade recovery in 2017. In 2019,

global trade should drop again to 4.6% mainly in the wake of the slowdown in Asian imports. In all, the elasticity of world trade to GDP growth should remain consistent with robust global growth, namely higher than 1 in 2018 and 2019 after its marked recovery in 2017.

Growth in world demand for French exports is set to remain strong at 4.4% in 2018 and 2019 (down from 5.3% in 2017). World demand for French exports should slow more sharply than world trade in 2018, French exposure to declining European trade being higher. Conversely, the adverse effects of declining trade in Asia should have a lesser effect on France in 2019 (see Chart page 1).

Chart 6: World trade and contributions by area



Source: DG Trésor.

4. Uncertainties surrounding the forecast scenario have increased in recent months

This is due to:

- Effects of US protectionist and retaliatory measures taken by other countries: the impact on economic activity of the measures already in place have so far been slight (see Box 2), but the risk of escalation is genuine (particularly between the United States and China). Yet global trade could be stronger than forecast if uncertainties over trade tensions were to die down more quickly than expected.
- The magnitude of Brexit effects, particularly owing to the progress in the negotiations over the withdrawal agreement and the future relationship between the United Kingdom and the European Union, as well as market reaction and the impact on the policy mix.
- Political situation in Italy: a marked decline in the Italian economy could affect its partners through trade and financial channels or due to an increase in uncertainties. Conversely, clarity from the new government over its policies could help dissipate uncertainties.
- Financial and fiscal imbalances in China could lead to a more brutal slowdown of its economy than forecast. Nevertheless, growth could be stronger in the event of the government increasing monetary and fiscal stimulus.
- Some emerging economies remain vulnerable to Fed rate hikes and a marked increase in aversion to risk, brought on, for example, by the growing problems in Turkey. Political and geopolitical uncertainties also constitute causes of concern.
- Oil prices could rise once more, although this could be offset by downward pressure from increased oil production (see Box 1).
- Concerns over financial markets remain high as overvalued equity presents a substantial risk in the United States.

Box 4 : Main revisions since the 2018 Stability Programme and comparisons with forecasts by international organisations

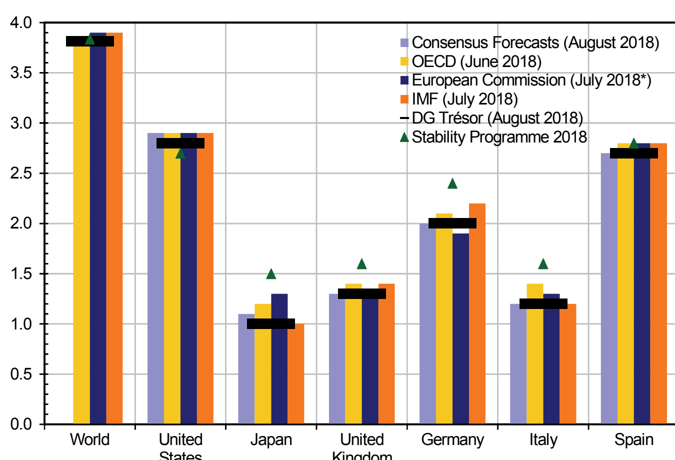
Since the scenario prepared for the Stability Programme, we have downgraded growth forecasts for advanced economies and upgraded those for emerging economies, leaving our projections for global growth unchanged.

In advanced economies, growth forecasts were revised down for the euro area in 2018 and 2019 as economic performance fell short of projections in the first half of the year. This revision also reflects a less bright outlook in the euro area owing to *(i)* growing uncertainties and *(ii)* the rise in oil prices. We have scarcely altered our forecast for United States growth, although by factoring in protectionist measures not yet apparent at the time of the Stability Programme scenario, the forecast is lower in 2019.

In emerging economies, the eased pace of reform in China should result in a lower-than-forecast fall in growth. Projections for India remain virtually unchanged. Conversely, economic activity has been revised down in Brazil as political uncertainties dampen growth, and in Russia, since the rise in VAT this summer. The scenario for Turkey has deteriorated substantially with the slump of the lira and forecast policy of fiscal tightening.

This scenario for stable growth in 2018 and 2019, mainly underpinned by emerging economies, has reached an overall consensus (see Charts 7 and 8). It is similar to the scenario presented by the IMF in July (WEO update), by the OECD in June and by the European Commission in May. It is also in line with the Consensus Forecasts for August.

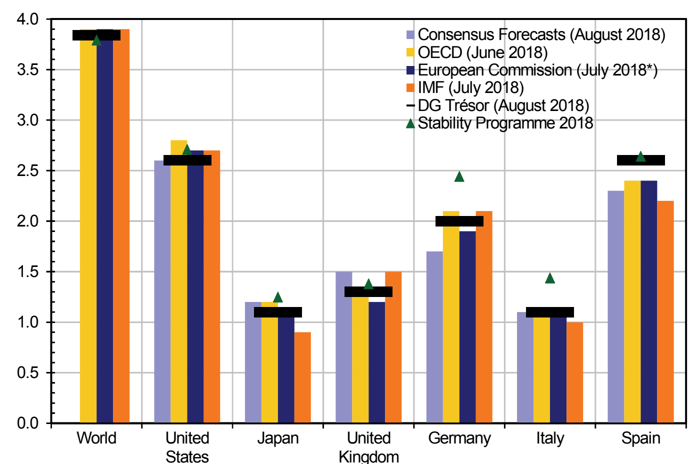
Chart 7: Growth forecasts for 2018



* Except World, United States and Japan: May 2018

Sources: IMF, OECD, European Commission, Consensus Forecasts, DG Trésor.

Chart 8: Growth forecasts for 2019



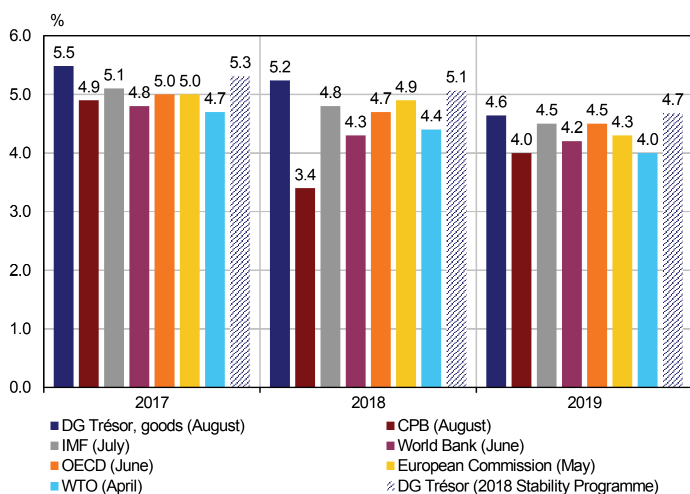
* Except World, United States and Japan: May 2018

Sources: IMF, OECD, European Commission, Consensus Forecasts, DG Trésor.

As Chinese imports outstripped first quarter expectations, they were revised up in our world trade scenario. Conversely, the trade content of growth in advanced countries was weaker at the start of the year, particularly in Europe. Our forecast for world trade is overall close to the one for the Stability Programme (up 0.2 points in 2018, unchanged in 2019). As for world demand for French goods, it has been downgraded 0.6 points in 2018 and 0.2 points in 2019 due to less support from Chinese trade and high exposure to weaker European trade. This is consistent with the average exposure of French trade.

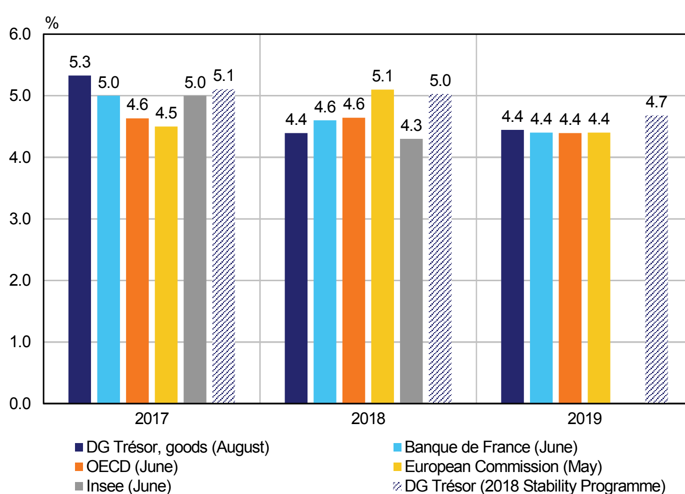
The scenario of a global trade slowdown is consensual. DG Trésor forecasts are close to those of the IMF in July, the OECD in June and the European Commission in May (see Charts 9 and 10).

Chart 9: Comparison of world trade forecasts



Sources: IMF, OECD, World Bank, CPB, European Commission, WTO, DG Trésor

Chart 10: Comparison of world demand forecasts for French exports



Sources: OECD, Banque de France, European Commission, Insee, DG Trésor.

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