The global economy and the euro area: weak international trade, robust domestic demand

By Claus Michelsen, Guido Baldi, Geraldine Dany-Knedlik, Hella Engerer, Stefan Gebauer, and Malte Rieth

ABSTRACT

The current global economic environment remains harsh. Global growth rates stagnated in the fourth quarter of 2018, particularly affected by foreign trade. DIW Berlin's forecast indicates global economic growth of 3.7 percent for 2019 and 3.6 percent for 2020. Positive stimuli are expected from catch-up effects (in the European automobile industry, for example) and the continued positive development on the labor markets, which will support consumption. However, the outlook for international trade is dominated by trade conflicts, political uncertainties, and a weaker Chinese economy. Although the trade conflict between the USA and China is beginning to ease, there are signs of a dispute between the USA and the European Union over EU automobile and car part exports to the USA. In Europe, the possibility of a no-deal Brexit and the political situation in Italy are causing uncertainty. Against this backdrop, monetary policy is likely to be expansionary in the forecast period.

The global economic expansion weakened further in the final quarter of 2018 (Figure). Growth rates mostly stagnated or declined slightly in both developed and emerging market economies. A number of uncertainties likely contributed to this, and foreign trade was particularly affected. In addition, temporary factors dampened growth in some major economies.

Non-recurring effects, such as the federal government shutdown in the USA, will no longer be an issue in the forecast period (2019 and 2020). There will probably be catch-up effects, in part because the European automotive industry is likely to partially make up for last year's production losses. Domestic demand remains largely intact in most countries, and the situation on the labor markets is continuing to improve, albeit at a slower pace. In addition, lower energy prices are likely to result in increased purchasing power gains for private households in 2019.

In contrast, the global economic environment remains harsh. Trade conflicts, political uncertainties, and a weakening Chinese economy are shaping the outlook for international trade, which will probably remain weak, dampening corporate investment activity. As a result, the global production expansion is likely to slow to 3.7 percent in 2019 and to 3.6 percent in 2020 (Table).

Against this backdrop, monetary policy is likely to be expansionary in the forecast period. There are signs that central banks are shifting away from planned increases in key interest rates in both the USA and the euro area, which will provide favorable financing conditions in the two economic areas and many emerging markets. Fiscal policy will also be slightly stimulative, although the effects of the tax cuts in the USA are coming to an end and Japan has planned a consumption tax hike for 2019.

Overall, the global economy is facing a series of risks. While the trade conflict between the USA and China is cooling down, there are signs of a dispute between the USA and the European Union over EU automobile and car part exports to the USA. An escalation involving reciprocal tariff increases would burden exports and investments in both regions. In

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addition, the likelihood of a no-deal Brexit occurring at the end of March 2019 remains high, which would make trade between the two economic areas more difficult and negatively impact production. Lastly, the political situation in Italy, the third-largest economy in the euro area, is creating further uncertainties in Europe. The agreement between the EU Commission and the Italian government recently eased the situation somewhat, but the economy would be slowed down if Italian financing conditions deteriorate again.

Claus Michelsen is head of the Forecasting and Economic Policy department at DIW Berlin | cmichelsen@diw.de

Guido Baldi is a visiting researcher at the Forecasting and Economic Policy department at DIW Berlin | gbaldi@diw.de

Geraldine Dany-Knedlik is a research associate at the Forecasting and Economic Policy department at DIW Berlin | gdanyknedlik@diw.de

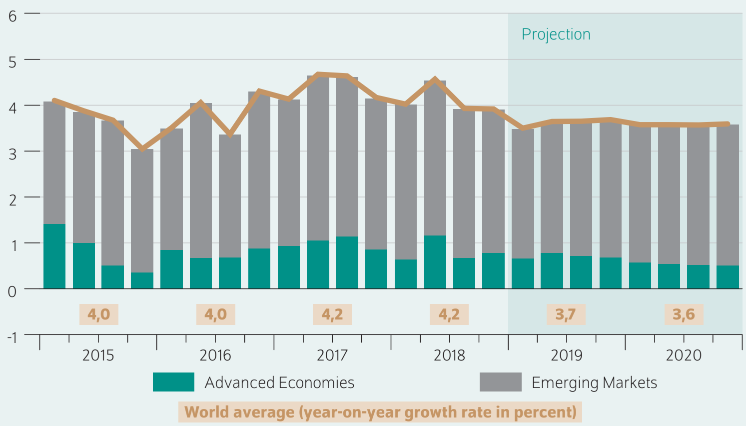
Hella Engerer is a research associate at the Forecasting and Economic Policy department at DIW Berlin | hengerer@diw.de

Stefan Gebauer is a research associate at the Forecasting and Economic Policy department at DIW Berlin | sgebauer@diw.de

Malte Rieth is a research associate at the Macroeconomic department at DIW Berlin | mrieth@diw.de

Figure

World real GDP growth
In percent



Sources: National statistical offices; DIW spring projections 2019.

Growth rates mostly stagnated or declined slightly in the final quarter of 2018.

JEL: E32, E66, F01

Keywords: Business cycle forecast, economic outlook

Table

Real GDP, consumer price inflation, and unemployment rate in the world economy
In percent

	GDP				Consumer prices				Unemployment rate in percent			
	Change over previous year in percent											
	2017	2018*	2019	2020	2017	2018*	2019	2020	2017	2018*	2019	2020
Euro area	2.5	1.7	1.3	1.5	1.4	1.7	1.5	1.7	9.0	8.2	7.8	7.5
without Germany	2.5	1.8	1.4	1.5	1.4	1.7	1.5	1.5	11.4	10.4	10.0	9.8
France	2.3	1.5	1.5	1.5	1.1	1.8	1.5	1.5	9.4	9.1	8.7	8.4
Italy	1.6	0.8	0.4	1.0	1.3	1.2	1.0	1.1	11.3	10.6	10.4	10.3
Spain	3.0	2.5	2.3	2.0	2.0	1.7	1.7	1.6	17.2	15.3	14.3	14.1
Netherlands	3.0	2.5	1.8	1.7	1.3	1.6	2.4	1.9	4.8	3.9	3.7	3.7
United Kingdom	1.8	1.4	1.2	1.4	2.7	2.4	2.0	2.1	4.5	4.2	4.4	4.4
USA	2.2	2.9	2.4	1.8	2.1	2.4	2.0	2.0	4.4	3.9	3.7	3.5
Japan	1.9	0.7	1.0	0.9	0.6	0.8	1.1	1.2	2.8	2.4	2.4	2.4
South Korea	3.1	2.7	2.7	2.4	1.9	1.5	2.0	2.7	3.7	3.8	3.0	3.0
East-central Europe	5.0	4.5	3.6	3.3	1.7	2.2	2.4	2.8	4.6	3.7	3.4	3.3
Turkey	7.4	2.6	−0.2	2.9	11.2	16.3	15.9	12.3	10.9	10.8	11.8	11.8
Russia	1.6	2.0	1.8	1.9	3.5	3.1	4.6	4.1	5.1	4.7	4.6	4.5
China	6.8	6.6	6.2	6.0	1.4	1.7	2.3	2.4	4.0	4.0	4.0	4.0
India	6.4	7.5	6.1	5.7	3.5	3.9	5.8	6.1				
Brazil	1.1	1.2	1.0	1.1	3.4	3.7	5.3	6.5	12.8	12.3	8.4	6.2
Mexico	2.3	2.2	2.0	1.6	6.0	4.9	4.1	3.2	3.4	3.3	4.8	4.8
Developed economies	2.3	2.2	1.9	1.6	1.8	2.0	1.8	1.9	5.3	4.8	4.6	4.4
Emerging markets	5.6	5.6	5.0	4.9	2.8	3.3	4.2	4.2	5.2	5.0	4.8	4.6
World	4.2	4.2	3.7	3.6	2.4	2.8	3.2	3.3	5.3	4.9	4.7	4.5

* Based in part on preliminary data

Sources: National statistical offices; DIW spring projections 2019.

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