

THE WORLD ECONOMY

Forecast summary

The global economy is expanding at its fastest pace since 2011. With momentum expected to carry into 2018, we have revised up our forecasts for growth in all of the major economies and regions.

But with many economies operating at close to full capacity, some slowdown in the pace of expansion is likely unless productivity surprises on the upside. In the medium term the outlook remains for growth of around 3½ per cent a year.

In some economies the cumulative effect of monetary easing is still at work but there are concerns that in some countries a tightening of capacity pressures may lead to increased inflationary impulses.

World economic growth is estimated to have picked up to 3.7 per cent in 2017, 0.2 percentage points stronger than we had expected in November. With considerable momentum going into the New Year, we have raised our forecasts for global growth by around ¼ percentage point to just below 4 per cent in 2018 and 2019. Importantly, the strengthening of growth has been widespread and this broad pattern is expected to remain.

Despite stronger growth and the absorption of some labour market slack, inflation remained muted in 2017. While we expect inflation to pick up a little in 2018 and 2019 in the advanced economies, the general picture remains one of continuing ‘lowflation’.

The faster pace of growth and associated reductions in unemployment may, in themselves, create an upside risk to the forecast from both momentum and confidence building. But downside risks remain present, with widespread concerns about the sustainability of asset prices and the effects of high levels of indebtedness, especially at a time when policy interest rates in the US are rising. Trade changes in the direction of protectionism are also a concern, and geo-political tensions remain a source of downside risk.

In the United States, while the FOMC’s ‘dot plot’ suggests three more policy rate increases this year, there are risks around this. A new Federal Reserve Chair, and the prospect of new committee members, adds an element of uncertainty in an environment where faster growth may lead to a pick-up in inflation. Expansionary fiscal policy and an increasingly tight labour market are likely to feature in the Federal Reserve’s discussions through the year. At the same time, however, seemingly stretched equity valuations could raise financial stability concerns.

In the Euro Area, the ending of quantitative easing looks in prospect, with growth of 2.5 per cent in 2017 marking a step up from the year before. Growth of over 2 per cent is projected for this year again and inflation is expected to move closer to the target. However, in the medium term there are risks that the various stresses within the monetary union, reflected in various imbalances across countries, may become more challenging once the ECB starts to raise interest rates, especially with policy rates having been held at very low levels for an extended period.

Growth of the Chinese economy continues to make a major contribution to the pace of world growth and is forecast to continue to do so, albeit with a slight slowing as the transition continues.

Summary of the forecast

Percentage change, year-on-year

| | World economy | | | Real GDP growth in major economies | | | | |
|------|-------------------------|--------------------------------|----------------------------|------------------------------------|-------|-------|-----------|--------|
| | Real GDP ^(a) | Consumer prices ^(b) | World trade ^(c) | US | China | Japan | Euro Area | Canada |
| 2017 | 3.7 | 2.1 | 4.3 | 2.3 | 6.9 | 1.8 | 2.5 | 2.9 |
| 2018 | 3.9 | 2.4 | 5.4 | 2.6 | 6.6 | 1.3 | 2.2 | 2.7 |
| 2019 | 3.8 | 2.3 | 4.9 | 2.5 | 6.3 | 0.9 | 1.8 | 2.3 |

(a) Based on global PPP shares. (b) OECD countries, private consumption deflator. (c) Volume of total world trade.