Economics

TalkingEconomics: Global forecast update - growth and risks rise under Trump

We have upgraded global growth for the first time in nearly two years. Better near-term activity plus a more favourable outlook for the US, UK and emerging markets are behind the move.

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For the first time in almost two years, we have revised our forecast for global growth upwards. We now expect it to come in at 2.6% in 2016 (previously 2.3%) as better-than-expected performance in Q3 extends into Q4.

In 2017, we expect the global economy to grow at 2.8% (previously 2.6%) led by a more optimistic view on emerging markets, the UK and the US (where the benefits of looser fiscal policy begin to come through later in the year). Global growth is expected to pick up further in 2018 to 3% as US fiscal expansion fully kicks in, helping lift growth across the world economy.

Inflation is expected to rise in 2017 to 2.4% from 2% in 2016, led by oil price effects in the advanced economies. In 2018, we expect global inflation to stabilise at 2.3%, despite higher inflation in the US. Here, we believe the economy doesn't have the capacity to meet the campaign promises of the new president. In particular, efforts to create 25 million jobs are likely to result in inflation in an economy where there are only eight million registered as unemployed.

Policy impact

Stronger growth leads to higher interest rates. For the US, we still forecast that the Fed funds rate will rise to 0.75% in December 2016, and to 1.25% by end-2017. In 2018, policy rates are expected to end the year at 2.25%.

Elsewhere though, interest rates are expected to remain on hold, with the exception of China where they are expected to fall further in 2017. The Bank of Japan is expected to keep rates on hold, but maintain quantitative easing (QE). We expect the European Central Bank to extend its QE programme by six months until September next year when it will begin to taper. In the UK, the Bank of England is expected to remain on hold over the forecast period.

Scenarios

On the scenario side we have made a number of changes but the risks are still skewed toward the downside on growth with a slight tilt toward deflation rather than inflationary outcomes. Our highest risk scenario is "Trump trade wars". We have brought back "Russian rumble" (stagflation results as President Putin invades the rest of Ukraine, and oil prices and financial market volatility increase).

We have also amended three scenarios. "US recession" becomes "Bond yields surge" (bond yields rise sharply on fears of fiscal expansion, resulting in deflation). "Global reflation" becomes "US fiscal reflation" and "Brexit shakes EU" becomes "Le Pen breaks Europe".

Front National leader Marine Le Pen is expected to lose the French presidential election but we cannot rule out another surprise. If elected, we could see France leave the EU and eurozone demand and activity slump with deflationary spillovers to the rest of the world.