PIIE PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS

The Economic Outlook: Global Slowdown

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The global economy is slowing

Different countries are experiencing different degrees of slowdown

The expansion is being held back by a confluence of headwinds—fading fiscal stimulus in the United States, higher trade barriers between some countries, structural issues in some countries, and uncertainty around future trade policy, Brexit, and other potential disruptions

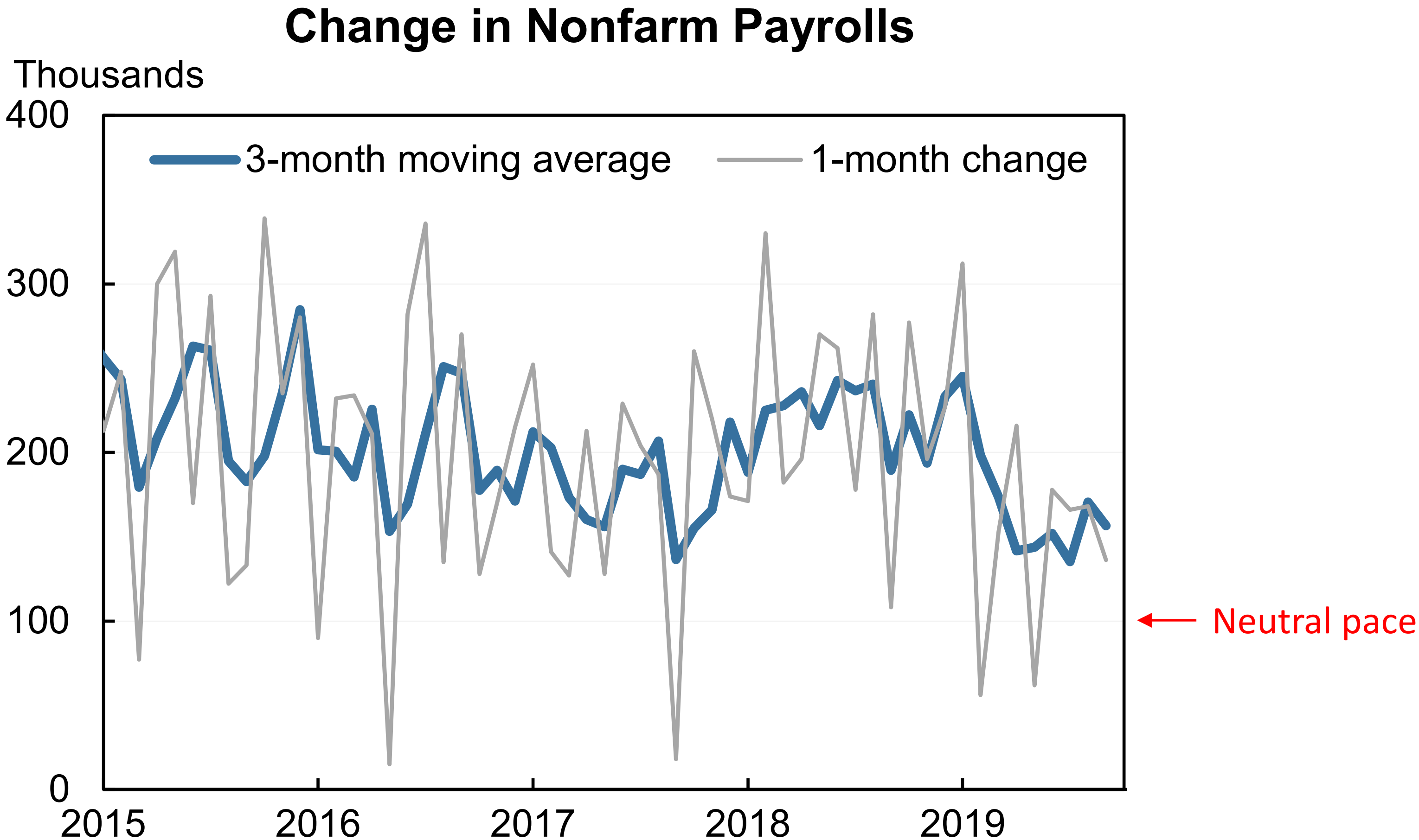
While the risk of recession is higher everywhere, growth has only stalled (or turned negative) in a couple of economies

Global outlook

Real GDP Growth (Y/Y)	2018	2019	2020
Global Output Growth (PPP weights)	**3.7**	**3.3**	**3.3**
US: expansion has moderated	2.9	2.3	1.8
Euro Area: weak spots	1.9	1.1	1.1
Japan: tax hike will be partly offset	0.8	1.2	0.8
UK: Brexit a drag	1.4	0.8	0.5
China: ongoing structural slowdown	6.6	6.1	5.9
India: brisk growth fading	6.8	6.1	6.1
Russia: sanctions weighing on growth	2.3	1.0	1.8
Brazil: recovery continues to be slow	1.1	0.7	1.2

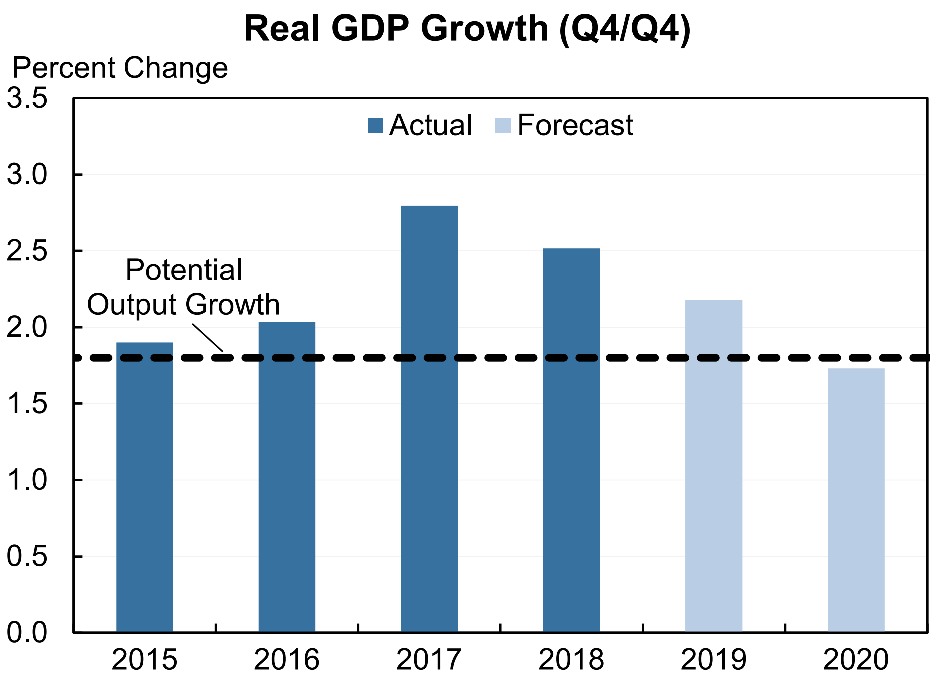
Source: Consensus Forecasts for 2018, PIIE for 2019-2020. Annual-average-over-annual-average growth rates.

Friday's employment data confirm that the US expansion has moderated



Source: Bureau of Labor Statistics; Haver Analytics; author's calculations.

US GDP growth rate falling back to trend

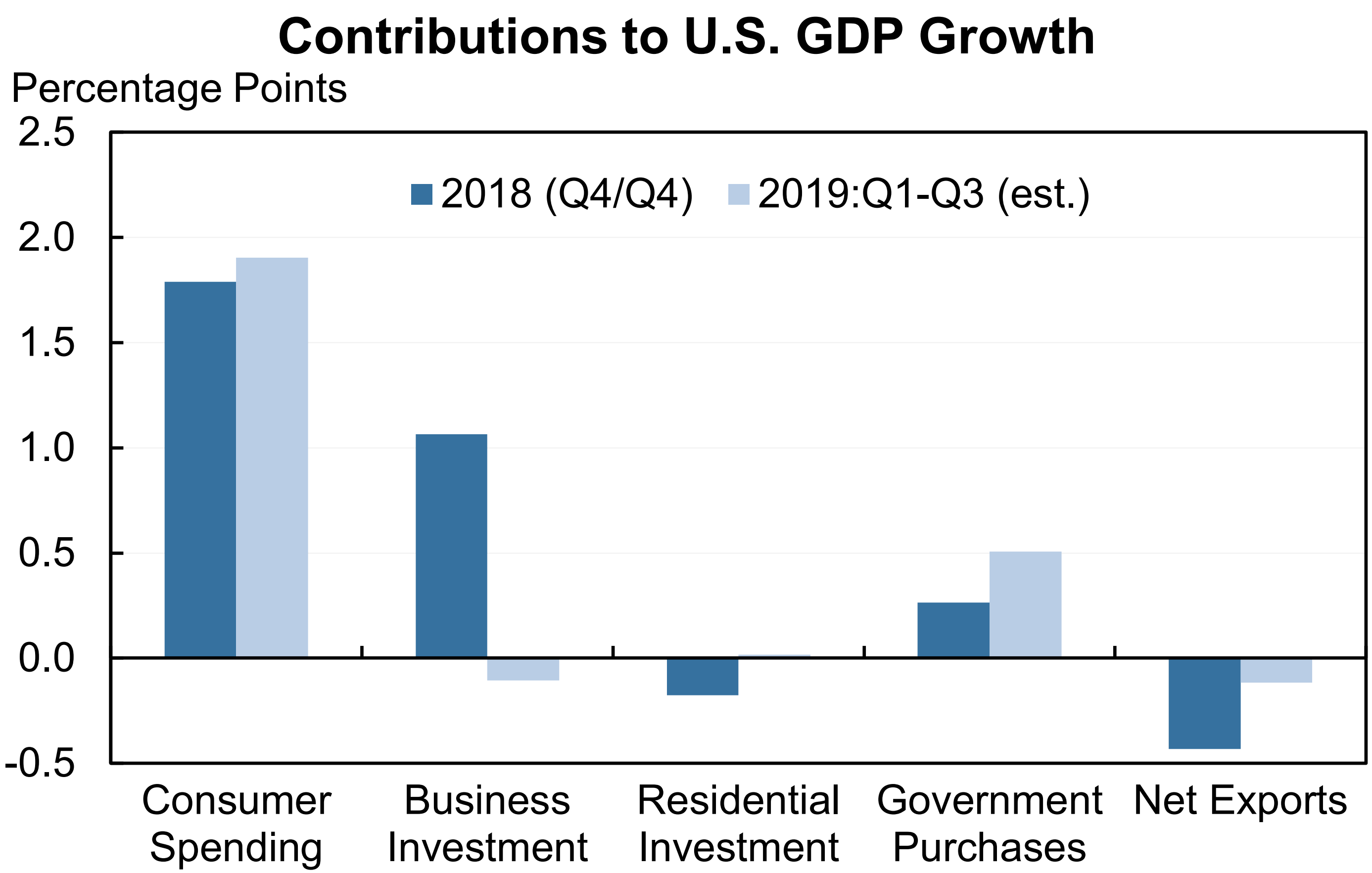


Source: Bureau of Economic Analysis; Haver Analytics; author's calculations.

	Unemployment Rate (Q4)	PCE Price Inflation (Q4/Q4)	
		Headline	Core
2016	4.8	1.5	1.8
2017	4.1	1.8	1.7
2018	3.8	1.9	1.9
2019	3.5	1.7	1.8
2020	3.6	1.9	2.0

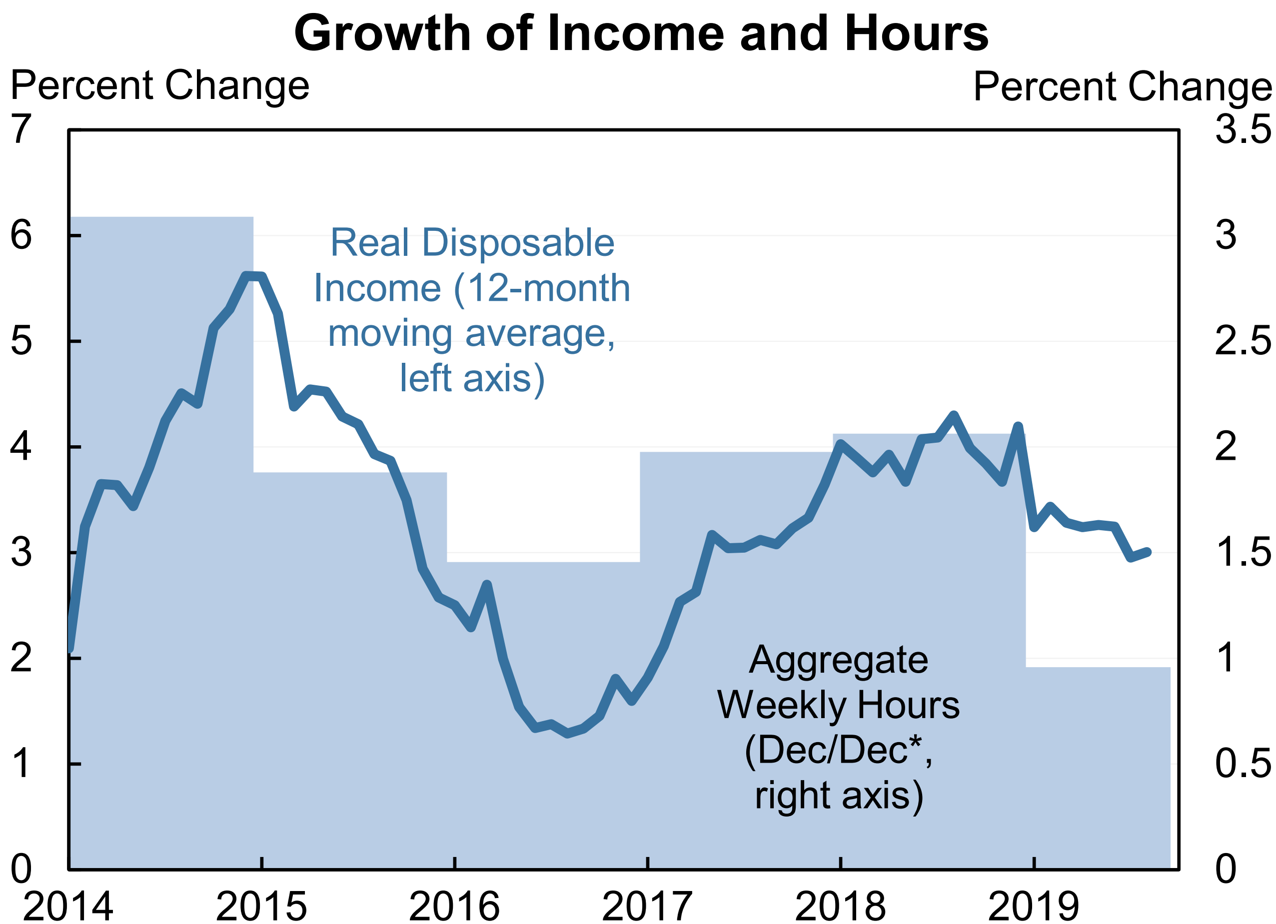
Note: Values in shaded cells are forecasts.
Source: Bureau of Economic Analysis; Bureau of Labor Statistics; Haver Analytics; author's calculations.

US growth is strongly consumer-led



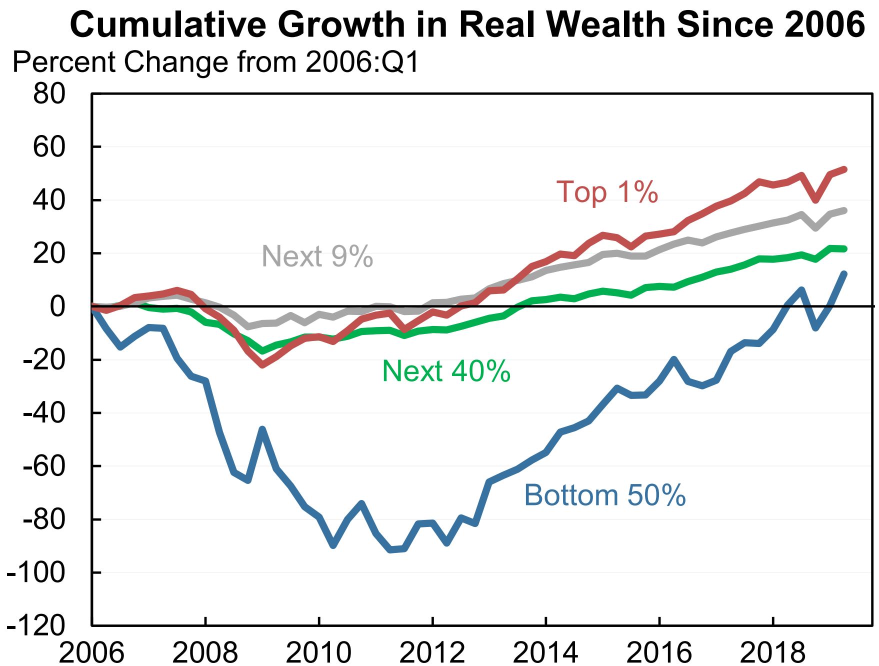
Note: 2019:Q3 is PIIE forecast.
Source: Bureau of Economic Analysis; Haver Analytics; author's calculations.

Income growth is likely to slow and lend less support to consumption in coming quarters

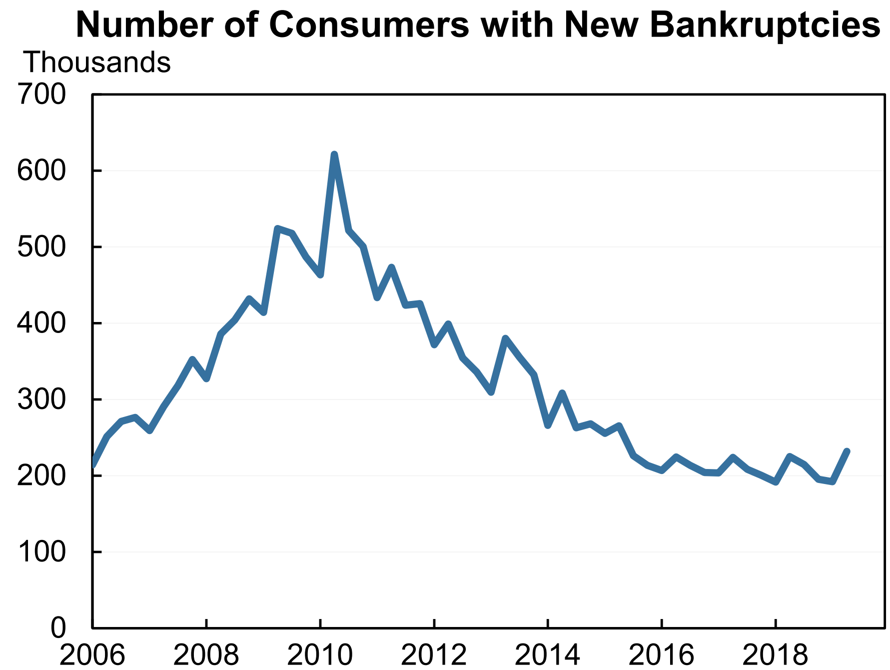


* 2019 is year-to-date at an annualized rate.
Source: Bureau of Economic Analysis; Bureau of Labor Statistics; Macrobond.

But wealth has risen—even at the bottom—and consumer finances look good

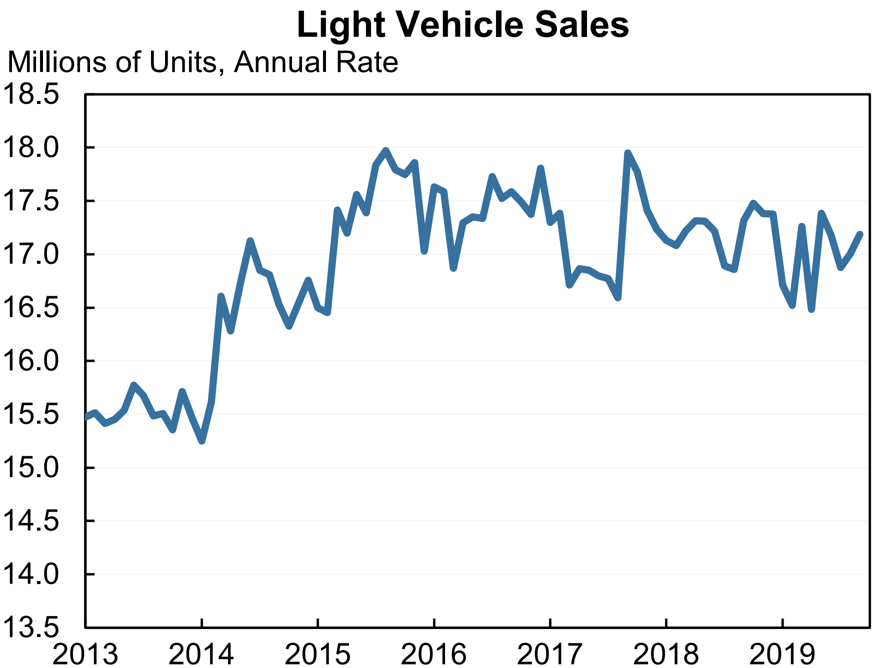


Source: Federal Reserve Board of Governors; Macrobond; author's calculations.

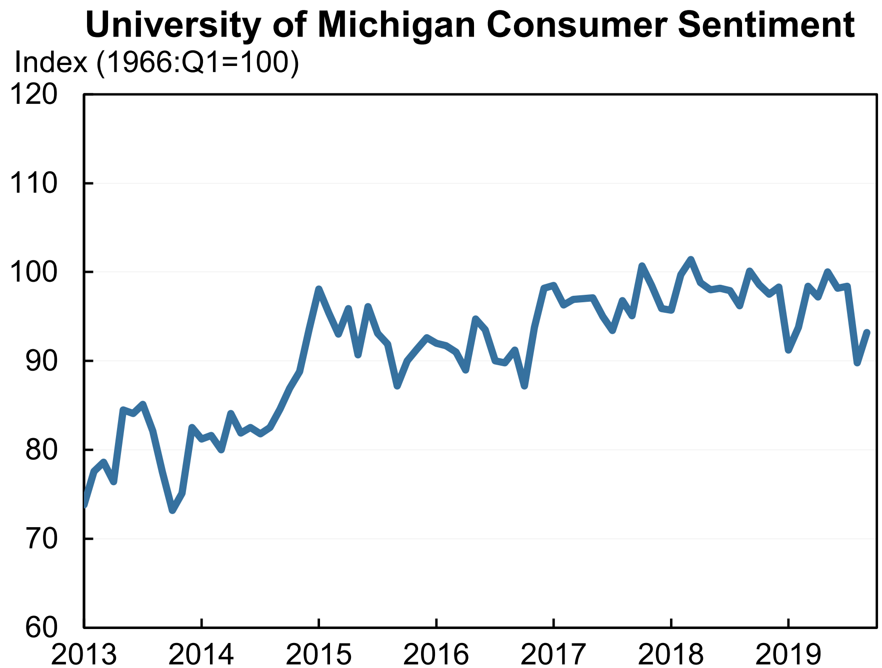


Source: Federal Reserve Bank of New York; Macrobond.

Indicators of household confidence have held up

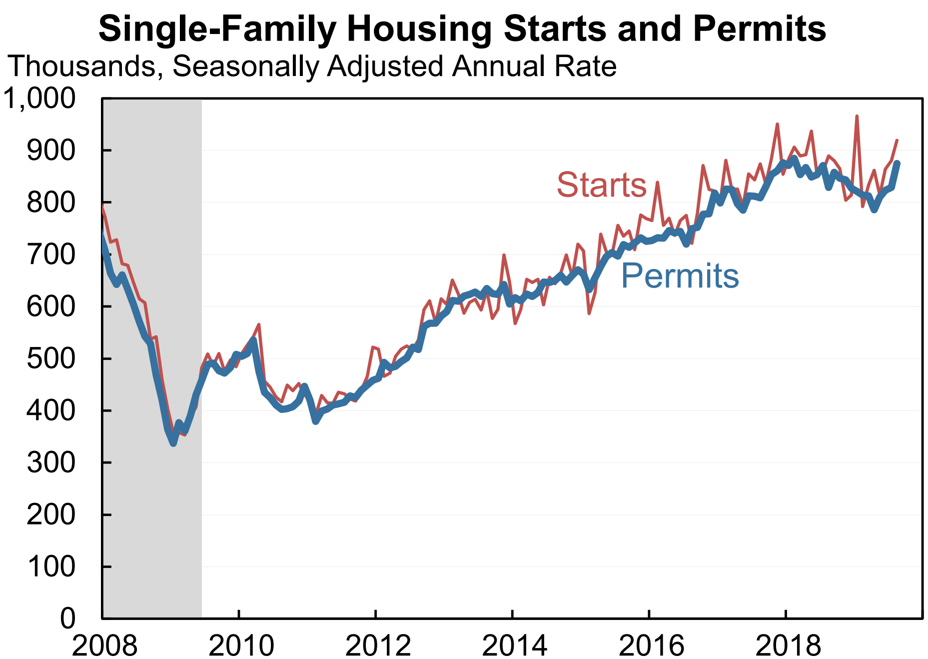


Source: Bureau of Economic Analysis; Haver Analytics.

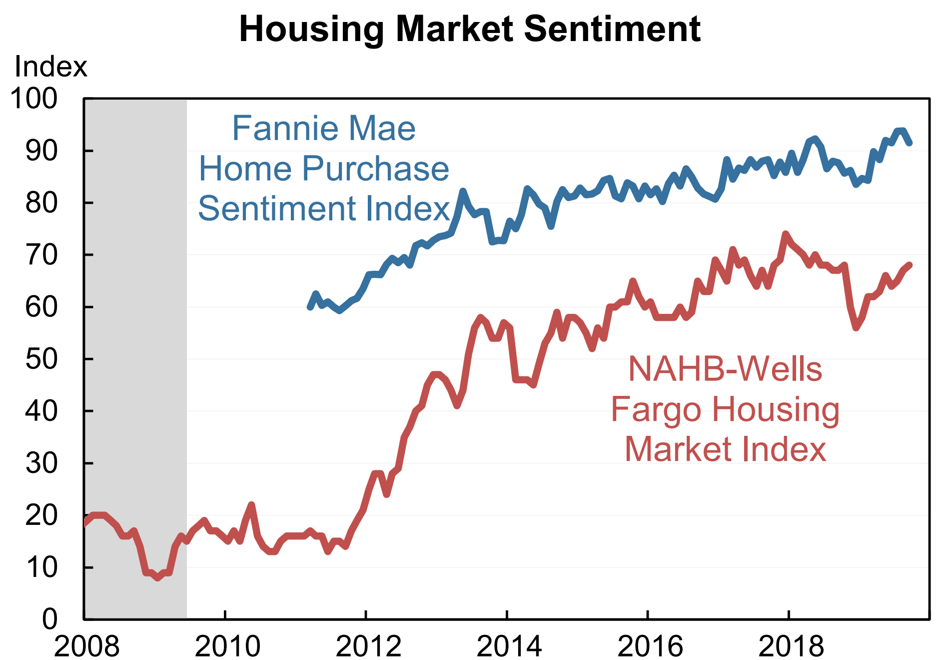


Source: University of Michigan; Haver Analytics.

Housing perking up with lower interest rates and slowing home price growth

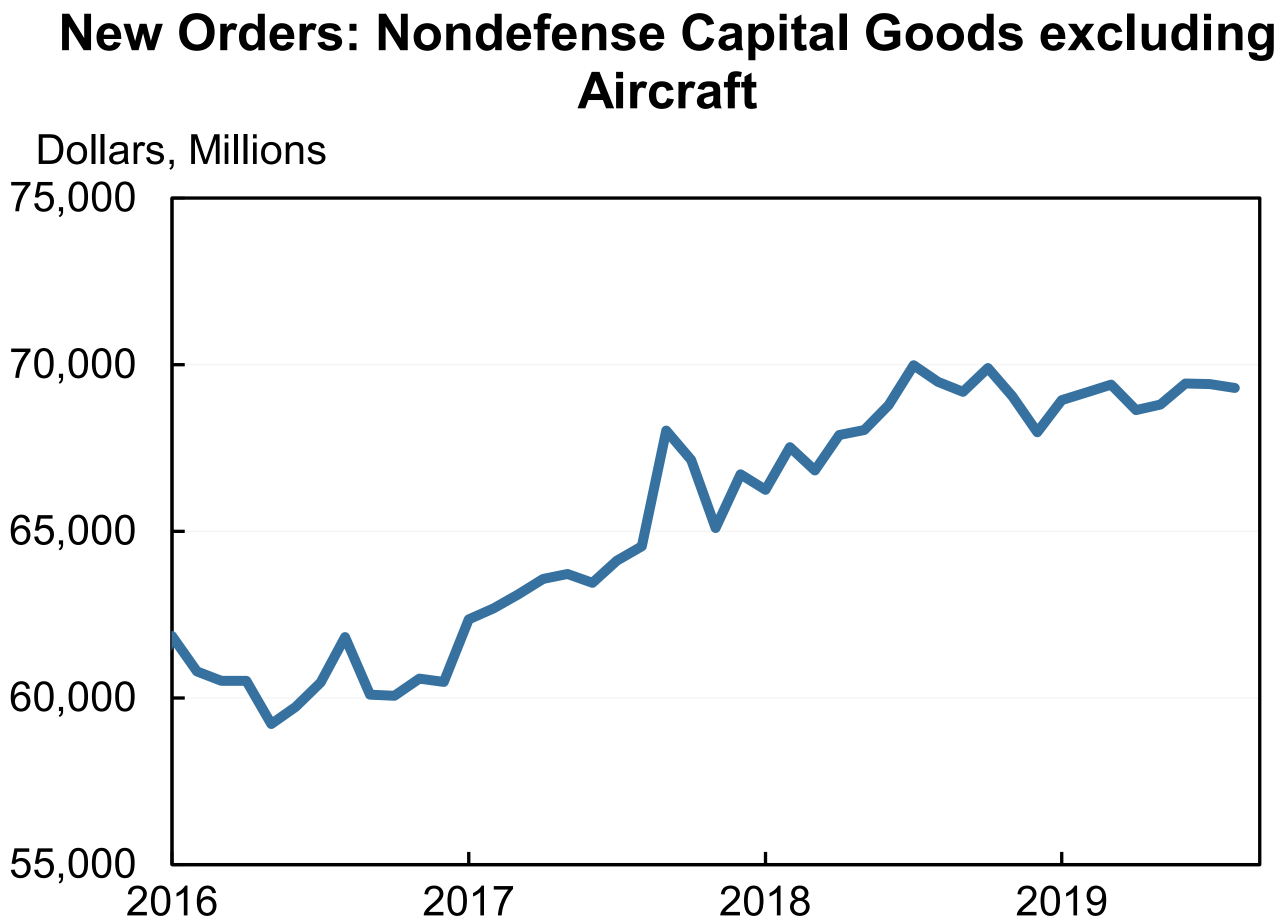


Note: Shading denotes recession.
Source: Census Bureau; Macrobond.



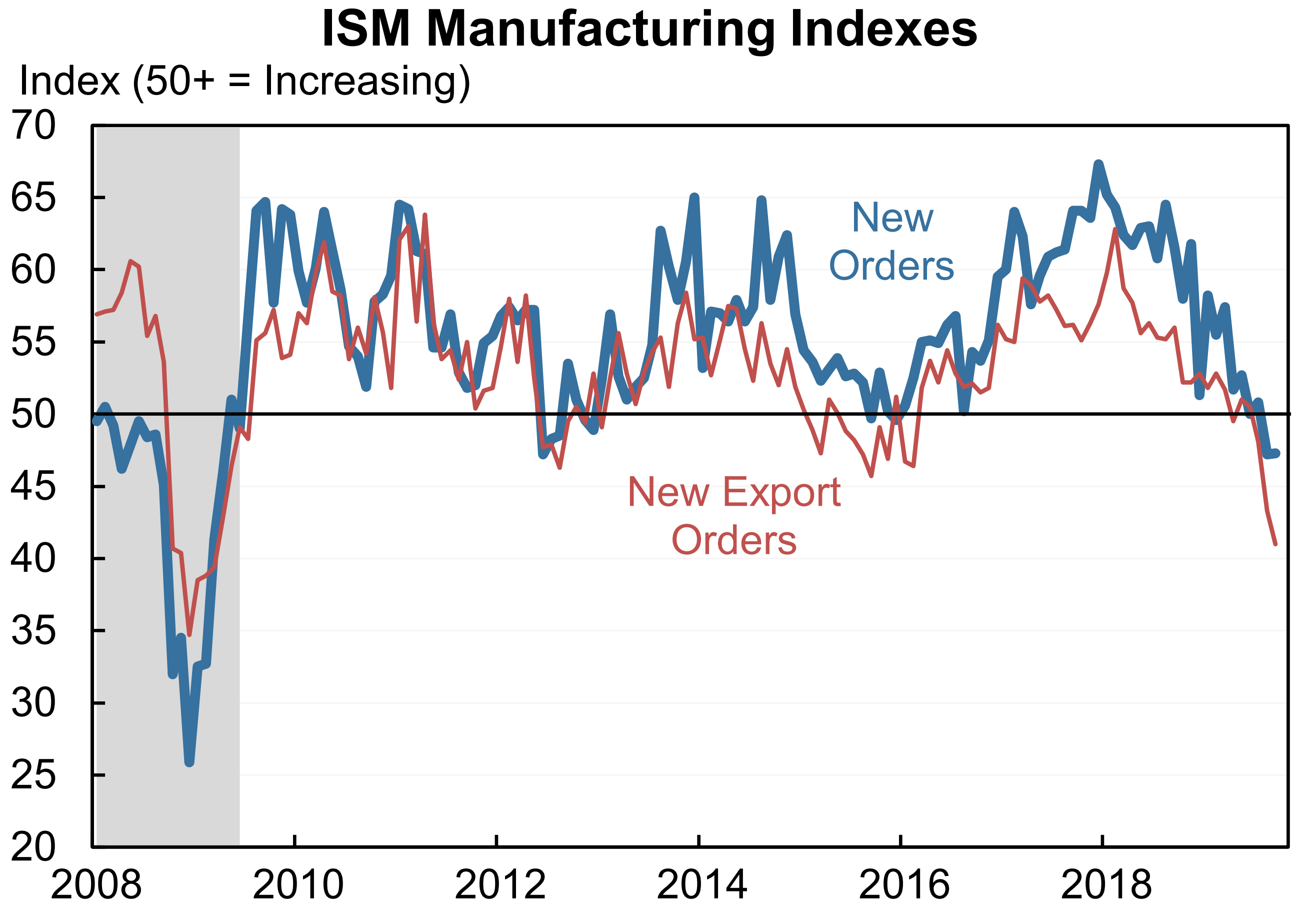
Note: Shading denotes recession.
Source: Fannie Mae; National Association of Home Builders; Macrobond.

Ongoing drag on business investment from weaker global growth and policy uncertainty



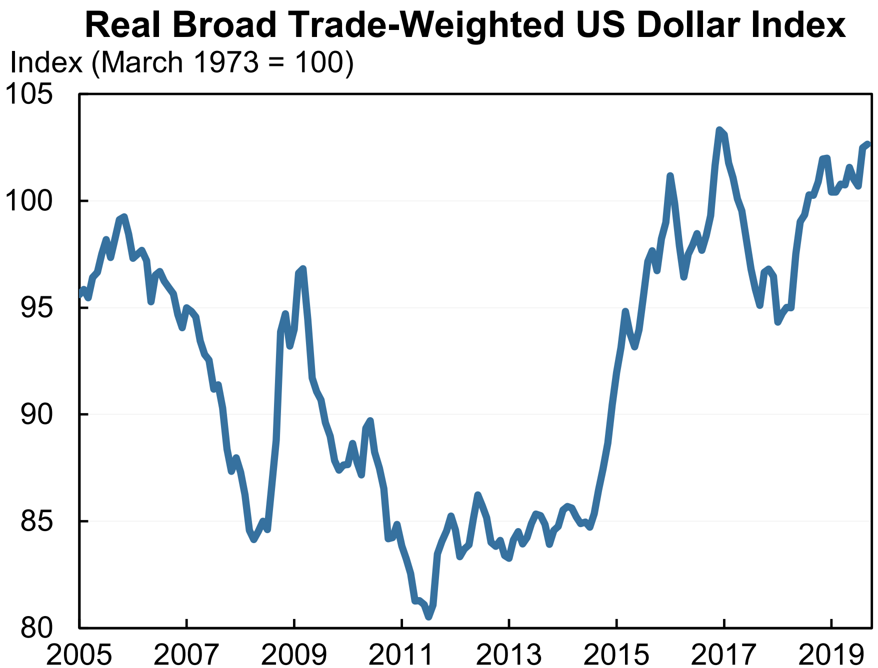
Source: Census Bureau; Haver Analytics.

Weaker global growth has been especially hard on manufacturing



Note: Shading denotes recession.
Source: Institute for Supply Management; Haver Analytics.

With the dollar likely to remain strong, net exports should continue to be a modest drag



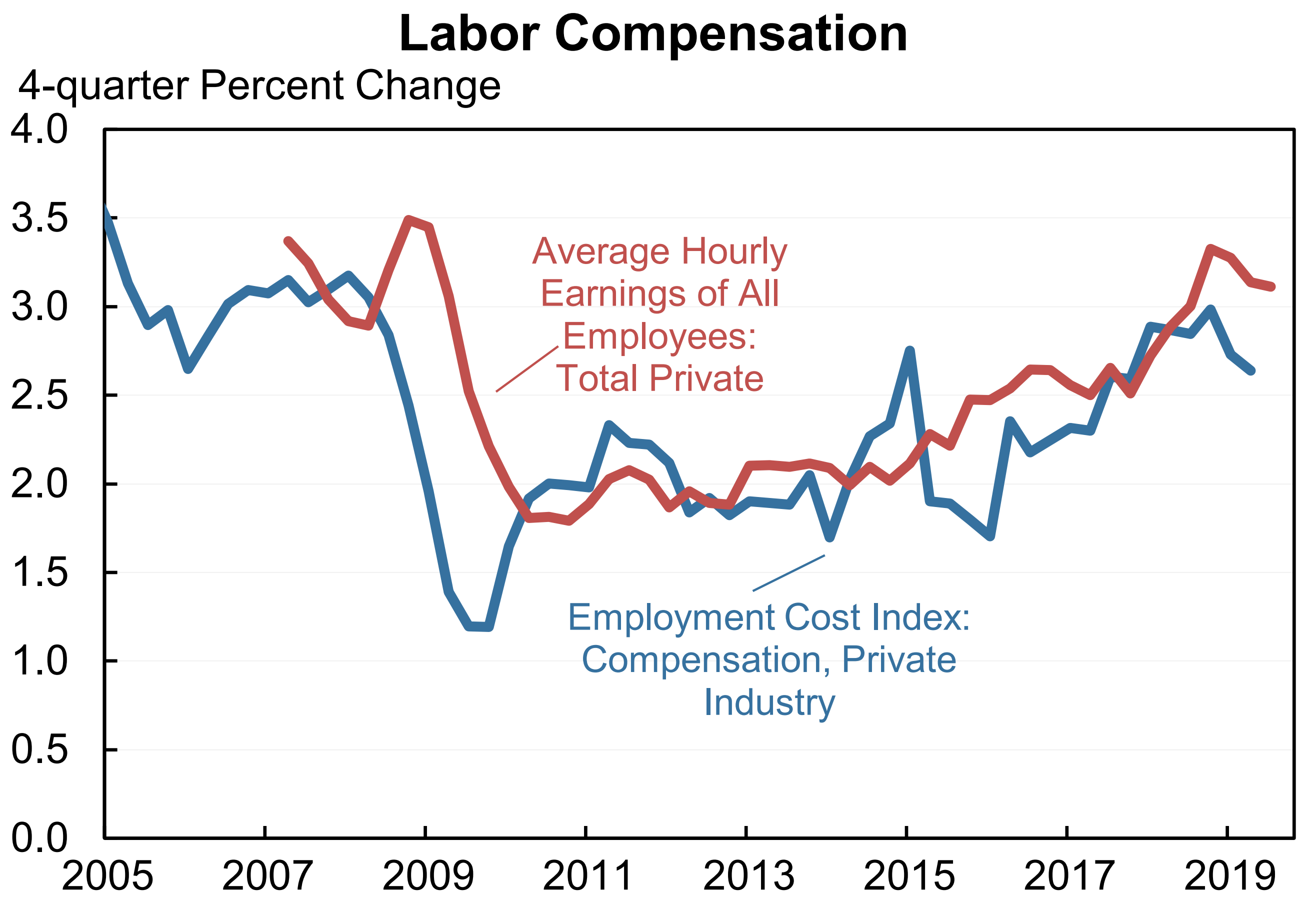
Source: Federal Reserve Board of Governors; Haver Analytics.

Contributions of Net Exports to Q4/Q4 Real GDP Growth

2017	-0.3
2018	-0.3
2019	-0.2
2020	-0.2

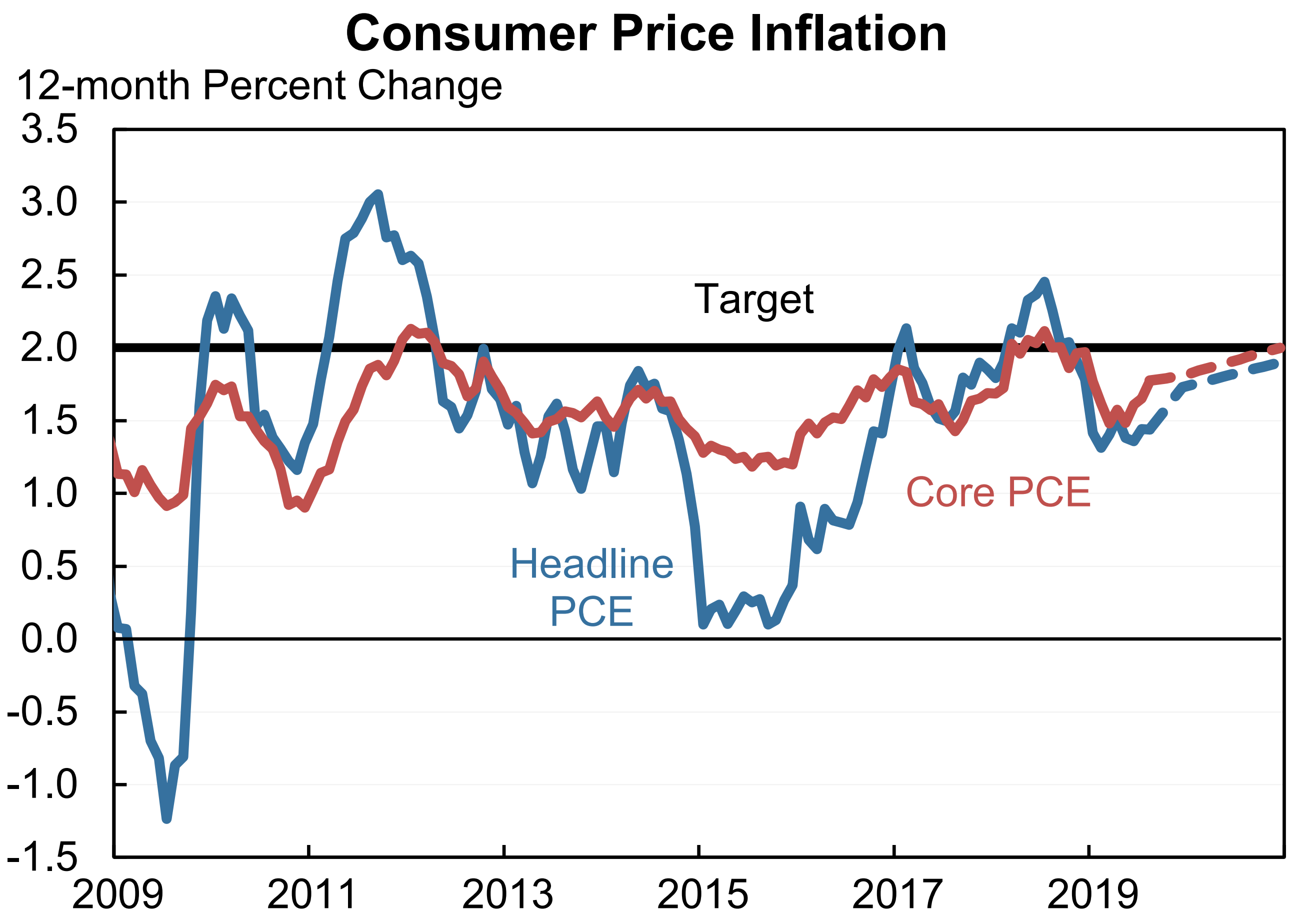
Note: Values in shaded cells are forecasts.
Source: Bureau of Economic Analysis; Haver Analytics; author's calculations.

Wage growth appears to have leveled off



Source: Bureau of Labor Statistics; Haver Analytics; author's calculations.

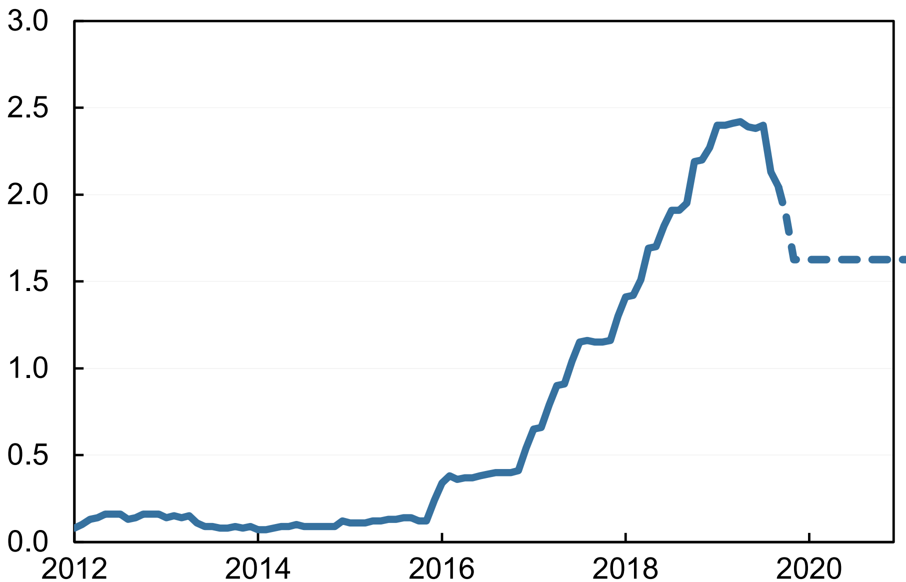
Inflation creeping back to Fed target



Note: Dashed segments represent forecasted values.
Source: Bureau of Economic Analysis; Haver Analytics; author's calculations.

Baseline forecast assumes Fed will cut once more in 2019 (25 bps) and stop there

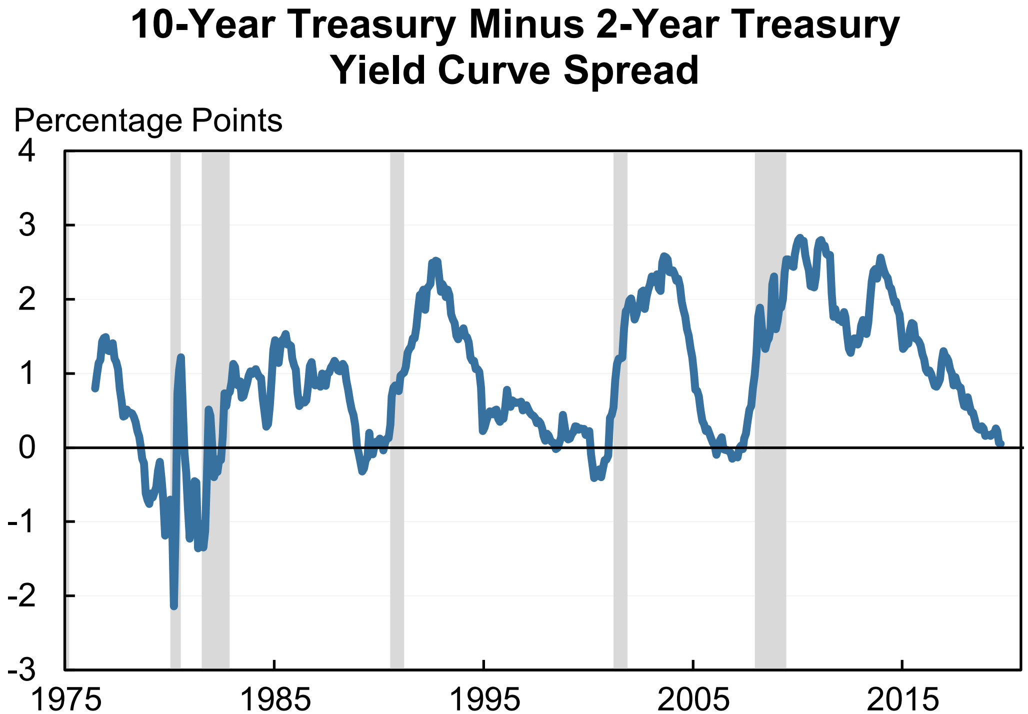
Effective Federal Funds Rate



Note: Dashed segment represents forecasted values.
Source: Federal Reserve Board of Governors; Haver Analytics; author's calculations.

Fed also likely to resume some balance sheet growth at next meeting to avoid further turbulence in funding markets

US recession risks have risen



Note: Shading denotes recession.
Source: Federal Reserve Bank of St. Louis.

Yield curve a warning signal (though not a definitive indicator)

Odds of a recession occurring in the next 12 months have risen to between 30 and 40 percent (versus 15 to 20 percent in any given year)

The United States *has limited room* to use monetary policy to fight a downturn

In recent recessions, the Fed has cut the policy rate by 5 percentage points or more (even in the relatively mild 1990-91 and 2001 downturns)

– Reducing policy rate to effective lower bound would be a cut that is only about 1/3 as large as the cuts in past recessions

– Long-term rates already low but some space to lower further and ease financial conditions more broadly through QE and forward guidance

– Fed could deploy modestly negative rates but unlikely to do so

The United States *has considerable room* to use fiscal policy to fight a downturn

About a third of the costs of any fiscal package would be offset by the higher revenues associated with the stimulative effects on economy

So the net cost of a package double the size of ARRA would be ~$1.1 trillion

That's similar to one-year's worth of federal borrowing—implies a minor shift to the debt-to-GDP projections