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Eswar Prasad

Global economy remains mired in swamp of low growth

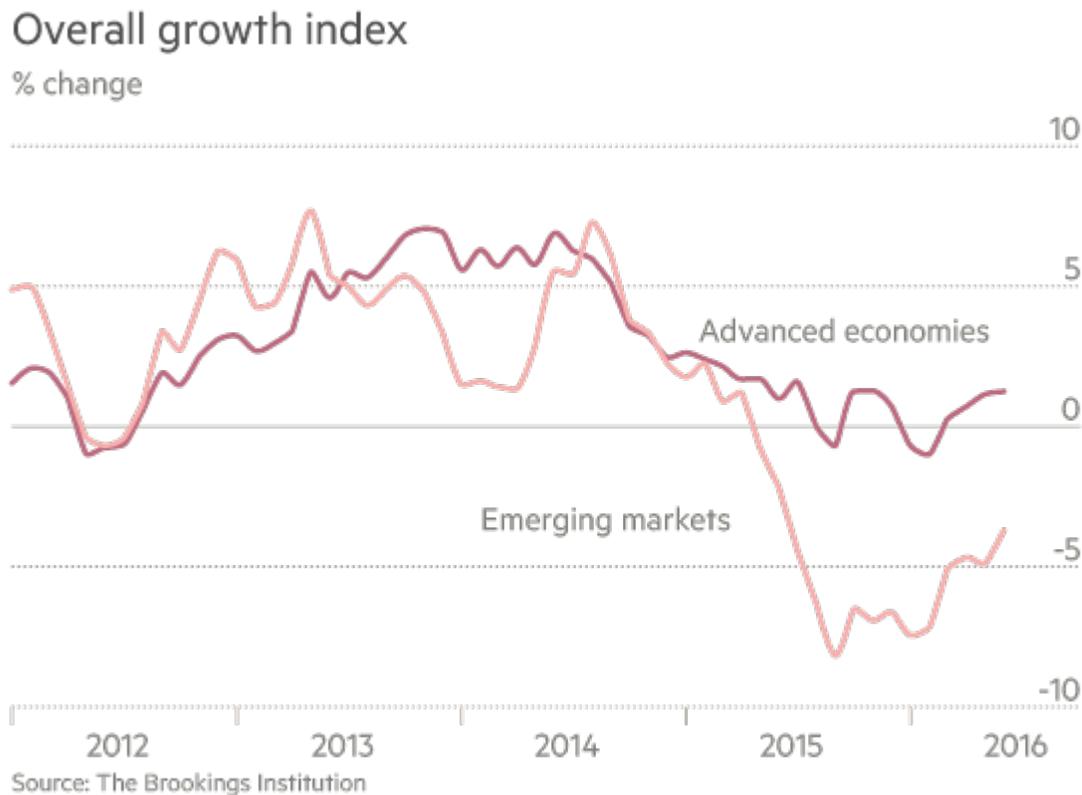
Tiger index shows despondency in the global economy with isolated signs of strength

FT Data

YESTERDAY by: Eswar Prasad and Karim Foda

In true Sisyphean fashion, the world economy is faltering yet again, unable to gain much elevation and sliding back into the low growth morass it has been stuck in for some time.

Major advanced and emerging market economies appear to be converging to a low-growth environment characterised by weak investment, stagnant productivity and tepid private sector confidence.



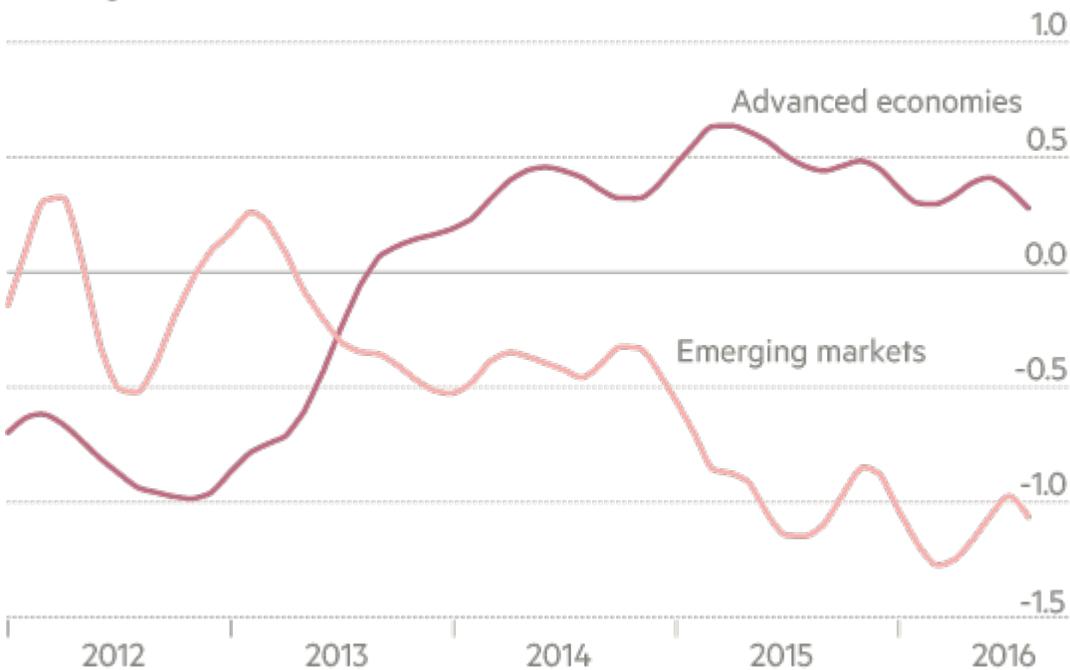
The Brookings-FT Tiger index presents a picture of general despondency in the global economy that more than offsets isolated signs of strength in some economic

indicators in a few countries. A strong adverse feedback loop has set in with low growth, fragile business and consumer confidence, low interest rates, financial system stresses, trade tensions, and political instability feeding into and reinforcing each other.

In most countries, there seems little prospect of the forceful and concerted policy actions direly needed to break this loop. Instead, politicians in many countries continue to rely on external bogeymen as a cover for their own failures, feeding into protectionist and nationalistic sentiments, and thereby shooting themselves and their constituents in the foot.

Confidence index

% change



Source: The Brookings Institution

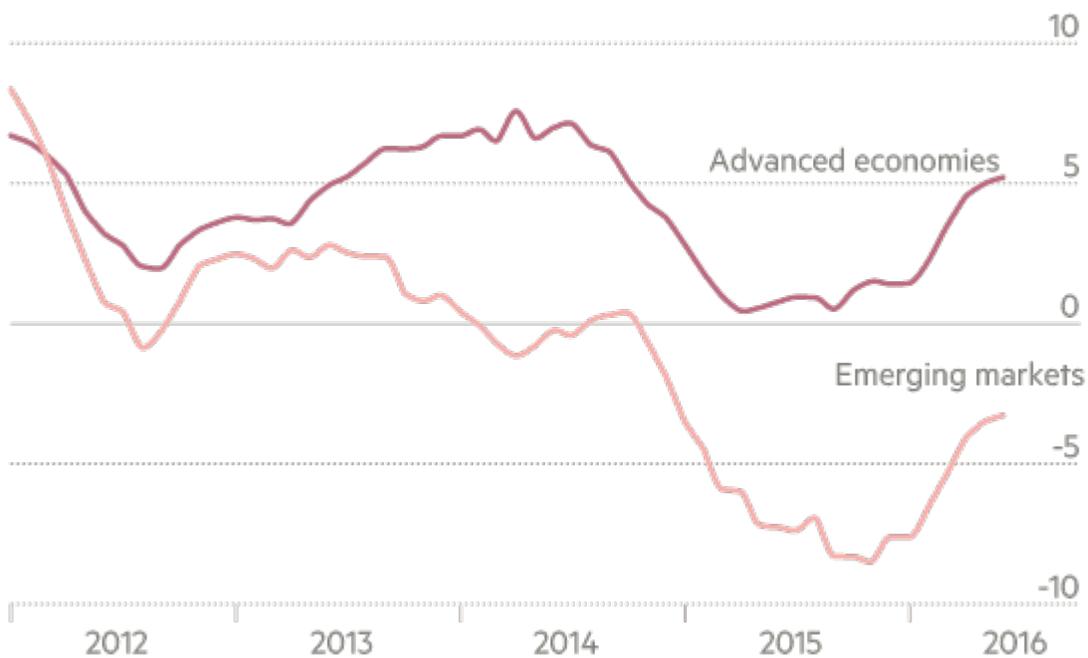
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The US economy continues to send mixed signals. Growth in GDP and industrial production have weakened slightly during the course of the year. Investment and productivity growth are also stuck in the doldrums, but the labour market is humming along.

Employment growth remains robust, labour force participation is recovering, and wage growth has picked up. The Federal Reserve appears to have boxed itself into raising rates in December if these patterns in labour market data persist. Fiscal and regulatory policies are likely to remain prisoners of political stalemates, adding to the uncertainty that has kept business and consumer confidence muted.

Real activity index

% change



Source: The Brookings Institution

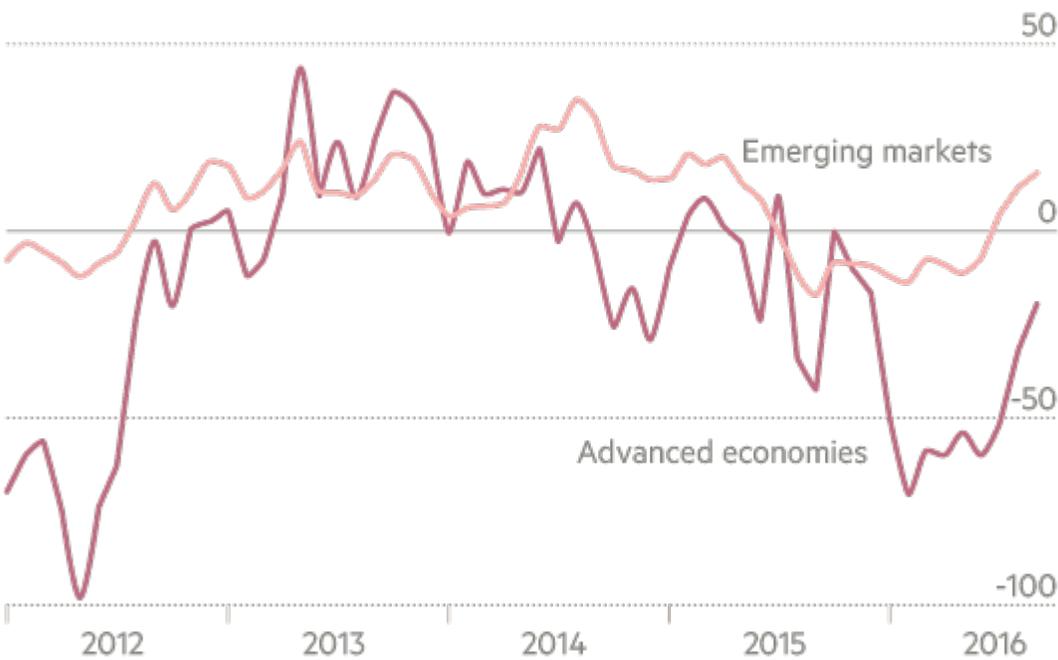
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The euro area remains a simmering cauldron of trouble. Deflationary pressures have eased slightly and growth has picked up in some countries. But the low interest rate environment, changes in regulatory structures and structural problems in the financial sector have laid bare the frailties of the European banking system, posing a serious threat to financial stability. Some countries in the region have been wracked by social and political instability, hampering business confidence and investment.

Economic activity and labour markets in Japan have strengthened modestly, but the Bank of Japan's heroic and increasingly desperate measures to weaken the yen and counter deflation have not worked.

Financial index

% change



Source: The Brookings Institution

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The UK economy appears to have survived the worst of the Brexit shock, with most financial market indicators recovering quickly from their post-referendum declines. Consumer and business confidence remain wobbly, however, and the true economic effects of the referendum outcome have yet to transpire.

Growth in emerging markets has bottomed out, with even many vulnerable economies apparently putting the worst behind them.

The latest slew of economic data from China points to a stabilisation of growth but also heightens concerns about the risks posed by an unabating investment binge. Robust retail sales are a welcome signal of firming domestic demand. The uptick in industrial production growth portends a broader base for GDP growth that is not overly dependent on the performance of the services sector. However, the continuing surges in bank loans and investment have intensified concerns about excess capacity in the economy and mounting bad loans in the banking system.

India remains a beacon of good growth. Recent positive signs, such as the implementation of a goods and services tax and the appointment of a well-respected central bank governor, have raised hopes that the Modi government is finally making a strong push on liberalisation and reforms. The Indian economy's relative resilience against external shocks reduces downside risks. But in the absence of

reforms in banking, the labour market and other deep-rooted issues, this resilience may not directly translate into sustained high growth.

Brazil and Russia remain in recession. In Brazil, the new government has stemmed the fall in consumer and business confidence, but it has its task cut out in coping with shrinking employment, retail sales and industrial production. The severity of Russia's recession has eased, with higher oil prices offering temporary relief.

The untrammelled creativity and boldness of central bankers remains the governing theme of global macroeconomic policymaking. The slaying of many sacred cows of the theory and practice of conventional central banking has boosted financial markets. But this has given most advanced economy central banks little traction in achieving their core mandates related to inflation targets or the objective of supporting growth.

The policy vacuum outside central banks has dented confidence, depressed domestic demand, hurt world trade and remains a drag on global economic activity. Fixing this imbalance calls for strong political resolve and forceful policy actions, both of which remain in short supply.

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