June 20, 2019

Global Macroeconomic Overview - 2Q2019

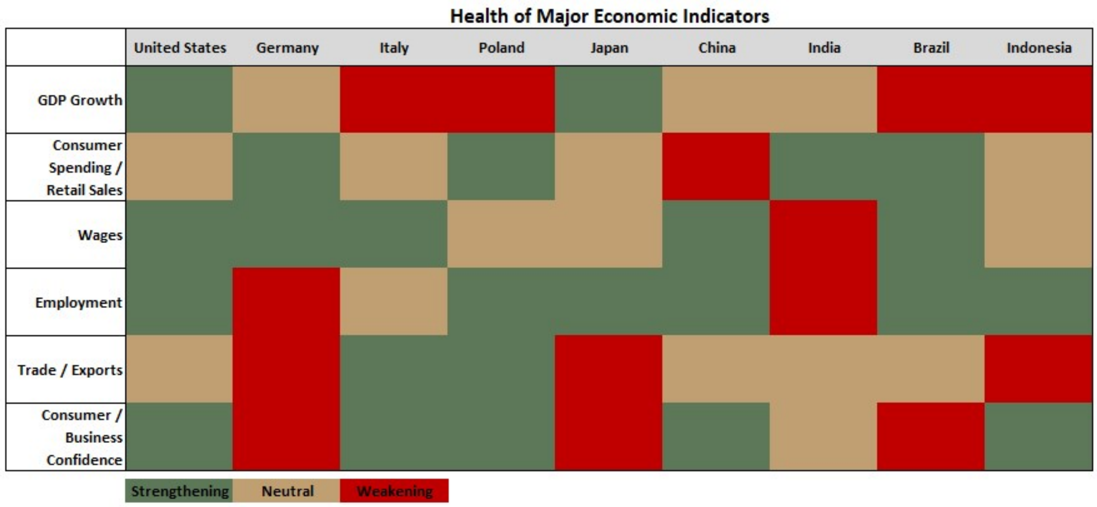
Stratas Advisors

The outlook for the global economy has weakened since our last update. Stratas Advisors now expects global GDP growth to be 3.18% in 2019 and 3.32% in 2020.

As can be seen in the heat map below, economic indicators are painting an increasingly mixed picture and chances of a 2020 slowdown are increasing in several major markets. Industrial and manufacturing sectors are starting to slow, but market services, driven by consumer spending, remains relatively robust. Equally, consumer confidence, although not as optimistic, has not switched to pervasively pessimistic. The Organisation for Economic Cooperation and Development explores this dynamic in its latest Global Economic Outlook highlighting the fact that fiscal linkages between the manufacturing and services sectors in several major economies have weakened in recent years. This provides a modicum of protection to global growth assuming that policy uncertainties and trade restrictions continue to weigh most heavily on the industrial sectors. We see this divergence in the health of consumer indicators and manufacturing indicators repeated in countries around the world. Risks remain skewed to the downside, and several significant economic issues remain unresolved. For the purposes of looking at future energy demand, a strong consumer sector will help to support demand growth. However, if uncertainty persists, and business activity continues to slow, fuel demand will be impacted. Given that the bulk of future fuel demand growth is expected in emerging markets, an economic slowdown in Asia (and to a lesser extent Latin America) would have a more significant impact than the ongoing malaise in Europe.

Although headline economic numbers are not flashing red, looking at some of the nuances of the major indicators reveals problems that could grow into larger issues. For instance, while US consumer spending remains healthy, spending on durable goods has slowed. Adding to our concern, many governments lack an effective arsenal to combat another recession. Low oil prices and accommodative monetary policy are providing some backstop against pervasive risks but there are limits to the levels of protection they can offer. Additionally, since interest rates have not been aggressively raised there is less room to lower interest rates as a reactive measure to a slowdown.

An interesting narrative emerging among traders and prognosticators seems to be that trade disputes will be fully resolved by (or early in) 2020, and markets will swiftly return to growth. With only six months left to go in 2019, and virtually no forward progress, we do not buy into this theory and think risks are actually rising for a more dramatic slowdown in 2020 in some countries. Not only have talks between China and the US stalled, but India is now applying tariffs in retaliation for losing preferential trade status. Across the pond, Brexit drags on and a no-deal exit remains a distinct possibility. This is not to say a global contraction is imminent, but instead that a return to swift growth is unlikely even if trade disputes and sanctions are suddenly resolved. Inside we explore the factors impacting our outlook for major OECD and non-OECD economies.



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