2. Global outlook: more growth, greater uncertainty and long-term risks

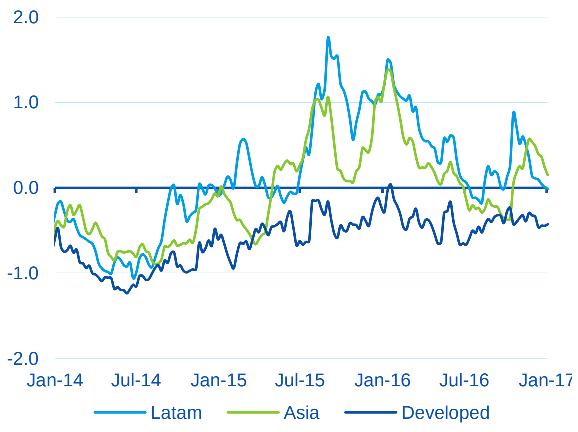
Global environment: more growth, higher uncertainty and long-term risks

The global environment improved in the last months of 2016 and is continuing to do so in early 2017. World growth accelerated in the last quarter of 2016, confidence indicators have improved clearly in all areas, and the industrial sector indicators are growing along with an incipient improvement in global trade.

Despite this acceleration, the outlook for 2017 and 2018 is fraught with uncertainties. The main one is associated with the economic policy of the new US administration, which is still largely undefined. Fiscal stimulus measures have been announced, as has deregulation in various sectors; this was welcomed by markets in the developed economies but not in those of emerging economies, which saw capital flight and currency depreciation, reflected in an increase in financial stresses at the end of 2016 (Figure 2.1). However, announcements of protectionist measures may seriously harm international trade in the medium and long term and affect confidence sooner than that, especially outside the US. Also, the lingering uncertainties about US economic policies seem to have been tempering the markets' optimism since the beginning of the year.

Figure 2.1

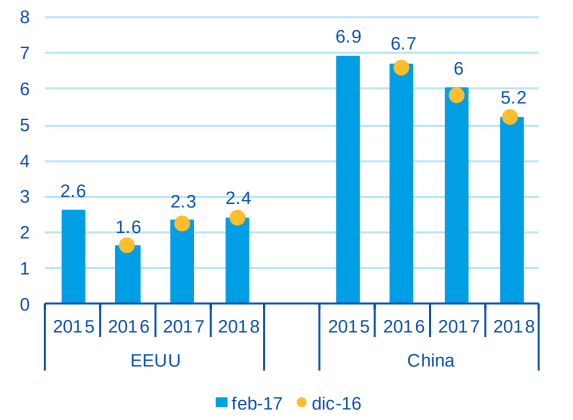
BBVA financial stress index



Source: Bloomberg and BBVA Research

Figure 2.2

GDP growth in the US and China (%)



Source: Bloomberg and BBVA Research

The magnitude of the inflationary pressures is another unknown at global level. Commodity prices, and particularly oil prices, have recovered more than expected in recent months, following the OPEC agreement and the improvement in activity. If to this we add the size of the balances accumulated by developed countries' central banks in recent years due to quantitative easing programmes and the prospects of fiscal stimulus, the result is that the risks of deflation of just a few quarters ago have been replaced by inflationary pressures in the developed economies, generating a number of questions about the reaction of their respective monetary policies.

In principle, the Federal Reserve is maintaining a cautious stance and continues to aim for a relatively slow normalisation of interest rates. Our forecast is for two rate hikes this year and two more in 2018. We expect the ECB for its part to begin the process of tapering QE in early 2018 and to decide on the first interest rate hike at the end of that year.

World growth will increase from 3% in 2016 to 3.2% in 2017 and 3.3% in 2018

Overall, our growth projections for 2017 for the major economies have not been substantially revised, although they are subject to greater uncertainty than usual. The base effect of higher growth in late 2016 and its inertia effect, together with the expected fiscal stimulus in the US, have led us to revise our forecasts for the US and Europe very slightly upwards, and for China a little more, while revising forecasts for Latin American countries downwards, mainly due to idiosyncratic factors. In particular, in the US we anticipate growth of 2.3% and 2.4% in 2017 and 2018 (Figure 2.2). In China, we are expecting growth of 6% in 2017, falling to 5.2% in 2018, given the vulnerabilities faced by the economy and an economic policy more oriented towards ensuring financial stability than maintaining growth. In this way, global economic growth should increase slightly, from 3% in 2016 to 3.2% in 2017 and 3.3% in 2018.

The risks are mainly on the downside and are dominated by the aforementioned uncertainty linked to protectionism in the US, a less welcoming attitude towards immigration and the danger that fiscal stimulus policies will have no effect on growth and will generate inflation, or that the deregulation announced in various sectors will not be managed properly. To this is added the possible reaction of other countries or regions to these protectionist moves. An unexpected rise in inflation could lead to the tightening of monetary policy by the main central banks, with global consequences. In the long term, the risk of imbalances building up in China, together with the lack of structural reforms in state-owned enterprises, may have an impact on the country's capital flows and currency and lead to an abrupt slowdown. In Europe, the political risk is high, in a year with a full electoral calendar. And in general, geopolitical risks remain high.