Slight slowdown in world activity in 2018 after a dynamic 2017

*Clément Rousset**

In 2018, world activity remained solid, at +3.9% after +4.0% in 2017 and +3.4% in 2016. Certain emerging economies – notably China and Mexico – decelerated slightly, but there was a much sharper slowdown in Turkey, where inflation rose in line with the depreciation of the lira. World trade was less buoyant in 2018 in a context of escalating trade tensions between China and the United States. Oil prices were relatively volatile and rose on average over the year, fuelling inflation slightly.

In the advanced economies, activity also slowed down a little, to +2.2% after +2.4 %, but growth remained higher than in 2016. Activity gathered pace again in the United States, driven by a strong upswing in government spending and by the tax incentives that buoyed up private investment. It lost impetus in Japan, where it was adversely affected by seismic and meteorological events. In the United Kingdom, activity also faltered: domestic demand slowed due to the wait-and-see attitude prevailing in the run-up to Brexit, and exports stagnated after being sustained in 2017 by the depreciation of the pound. In the Eurozone, activity also decelerated to +1.8% after the peak growth rate recorded in 2017 (+2.5%: the highest rate in 10 years). The European Central Bank's monetary policy remained accommodating and helped maintain the momentum of outstanding loans in the Eurozone. Nevertheless, private consumption slackened down and exports suffered from the slowdown in world trade. Imports held up better, driven by domestic demand. Disparities were apparent between the major European countries: the French economy slowed substantially in H1 before accelerating somewhat in H2. In H2, the German and Italian economies slowed down, with the latter sliding into technical recession. Spain stood out by managing to maintain a 2.6% growth rate in 2018.

Inflation rose slightly in the advanced countries

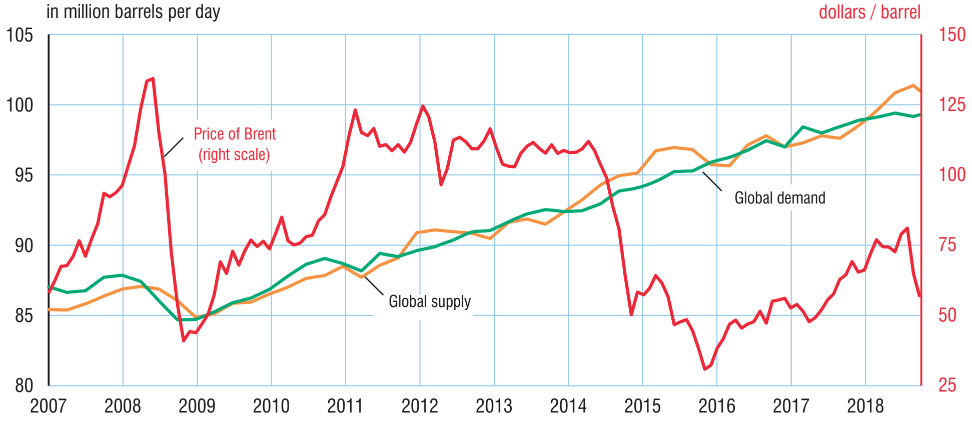
The price of a barrel of Brent increased sharply during 2018 to $71 on average, against $55 in 2017 *(Figure 1)*. Over 2017 as a whole and in early 2018, demand for oil slightly exceeded supply. The latter remained contained due notably to output limitations in the countries that signed the OPEC agreement drawn up at the end of 2016. This agreement contributed to the substantial rise in the price of Brent, topping $85 in early October. Thereafter, the increase in US and Saudi output created a supply surplus and the price of Brent began to edge down at the end of 2018, reaching $56 in December 2018.

* Clément Rousset (Insee).

This annual rise in oil prices was reflected in inflation in all the advanced economies, which reached +2.0% on average in 2018 after +1.7% in 2017 *(Figure 2)*. It gathered pace in the United States (+2.4% after +2.1%), Japan (+1.0% after +0.5%) and in the Eurozone (+1.8% after +1.5%). Conversely, it declined slightly in the United Kingdom (+2.5% after +2.7%), where it was particularly high in 2017 following the depreciation of the pound. Core inflation remained lower than headline inflation, at around 0% in Japan, +1% in the Eurozone and +2% in the United States.

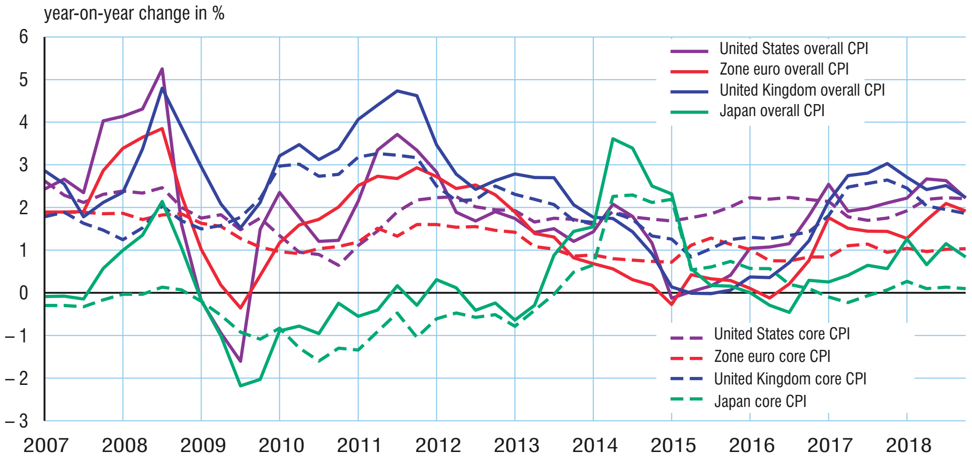
The differences in inflation between the US and UK economies and the Eurozone are partly explained by the different unemployment rates. Indeed, these rates stabilised at their lowest levels since the early 2000s in the United States and the UK *(Figure 3)*. Although the unemployment rate in the Eurozone continued to fall, it remained high, which curbed wage variations. In Japan, the unemployment rate was at its lowest level since the early 1990s, but wages barely rose.

1. Supply becomes excess on the physical oil market, prices drop timidly



Source: AIE.

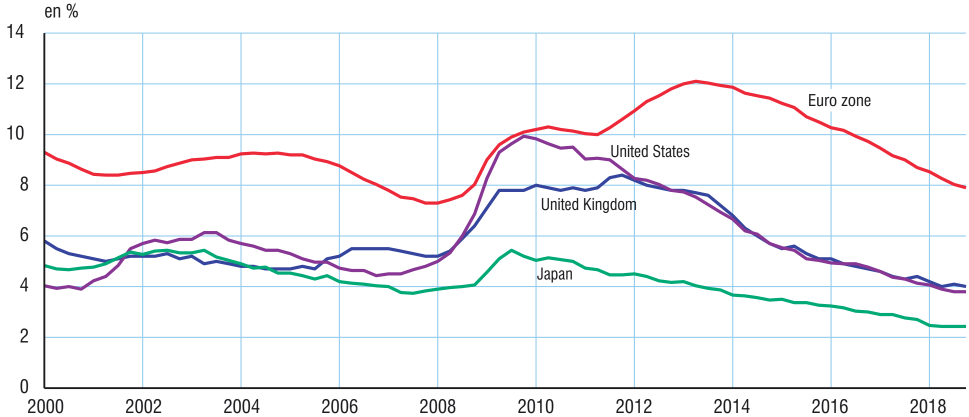
2. Inflation is accelerating sharply in the Anglo-Saxon economies



Note: the core inflation indicator calculated by INSEE is estimated by excluding the prices of energy, fresh food and public tariffs from the overall index and correcting it for tax measures and seasonal variations.

Sources: Eurostat, MIAC; ONS; U.S. Bureau of Labor Statistics.

3. Unemployment is at its lowest level since 2000 in the Anglo-Saxon economies

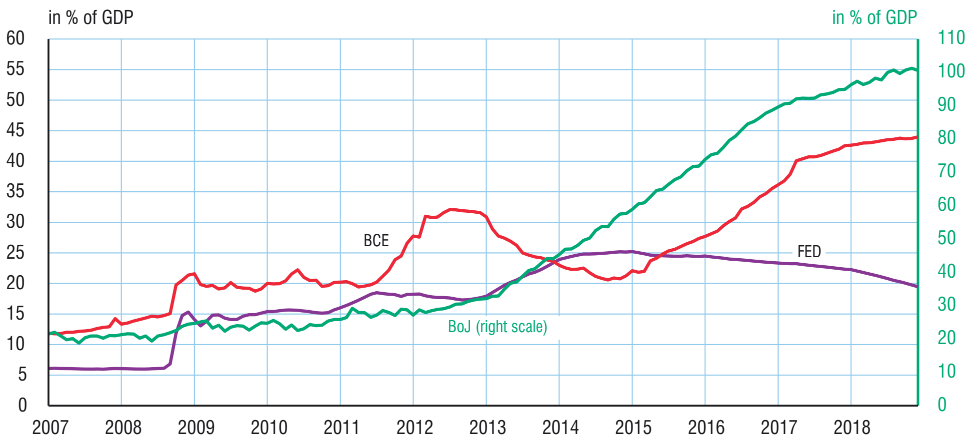


Sources: Eurostat; Japon, Statistics bureau; U.S. Bureau of Labor statistics.

European and US monetary policies continued to diverge

With inflation rising in the Eurozone mainly due to the volatility of oil prices, and in the context of a slowdown in activity, the European Central Bank (ECB) maintained an accommodating monetary policy. The rate of asset purchases slowed down in the spring of 2017 to €60 billion per month, but the purchase programme continued hroughout 2018, before ending in January 2019. This purchasing programme led to a sharp rise in the size of the ECB balance sheet *(Figure 4)*. In addition, with the ECB's base interest rate remaining at 0.0%, the interest rates applied to enterprises and households remained low.

4. The non-standard monetary policies pursued by central banks have durably raised their balance sheets



Sources: ECB; BoJ; FED.

However, in the United States, the Federal Reserve (Fed) continued its programme of progressive base rate hikes with four consecutive increases of 0.25 points in 2018. With the unemployment rate standing at its lowest level since the early 2000s, the Fed also reduced its balance sheet at the rate of $20 billion per month at the start of the year, and up to $50 billion per month at the end of 2018.

The dollar depreciated against the euro in 2018 ($1.18 to the euro on average in 2018, against $1.13 in 2017). This depreciation, which had begun in early 2017, continued and the dollar returned to its late-2014 level of $1.25 to the euro in Q1 2018. Subsequently, the tightening of US monetary conditions in relation to the other major central banks buoyed up the dollar, which ended 2018 at around $1.14 to the euro.

Financial markets were a little less buoyant than in 2017

After rising sharply in 2017, the stock market indicators of the advanced countries stabilised on average in 2018. The low interest rates and the favourable economic outlook pushed stock market indices to historically high levels at the end of January 2018. At the beginning of February, a higher than expected rise in US wages caused a correction in stock market indices accompanied by a sharp increase in volatility. The markets picked up until October when they slipped back again: NASDAQ suffered its biggest monthly drop since October 2008. Possible explanations for this downturn include higher interest rates in the United States and sometimes disappointing corporate results. On the emerging markets, the indices edged down during the course of 2018, pointing towards a reversal of capital flows.

Slight slowdown in the emerging economies

In China, growth dipped slightly to +6.6% in 2018 against +6.8% in 2017 *(Figure 5)*. The short-term outlook for China deteriorated during 2018. Domestic demand faltered, and household confidence indicators followed a downward trend: retail sales and vehicle registrations slowed. In the construction sector, investment slackened midway through the year with a deceleration in building starts. At the end of the year, the trade war with the United States strongly impacted foreign trade with downturns in exports (–2.2% in Q4 after +1.8%) and especially in imports (–9.4% after +2.5%).

After two years of recession, Russian activity picked up in 2017 and ramped up again in 2018 to reach +1.9%. At the start of the year, Russian domestic demand benefited from the continued decline in inflation while mining and quarrying output was vigorous. In the summer, due to diplomatic tensions with the United States, the rouble depreciated, and inflationary pressures reappeared. In Brazil, activity grew at the same rate in both 2018 and 2017 (+1.1%). The business climate in Brazil, which also emerged from recession in 2017, reached a high level in early 2018. However, activity in the country was affected by a road transport strike in May, and then by inflationary pressures, in a context of depreciation of the real linked to political tensions surrounding the presidential elections. Turkish GDP slowed significantly in 2018. The Turkish lira suffered a substantial devaluation over the year, and the short-term indicators are negative. The country entered recession in the spring of 2018. In contrast, Indian activity accelerated. After being adversely affected by the surprise demonetisation of 500 and 1,000-rupee banknotes at the end of 2016, whose effects continued into 2017, growth picked up again in 2018. Finally, activity in the Central and Eastern European countries slowed down in 2018, held back by the decline in demand from the Eurozone.

5. Growth rate of gross domestic product

in % at previous year price

	2014	2015	2016	2017	2018
Advanced economies	**2.1**	**2.3**	**1.7**	**2.4**	**2.2**
Euro zone	1.4	2.0	1.9	2.5	1.8
Germany	2.2	1.5	2.2	2.5	1.5
Spain	1.4	3.6	3.2	3.0	2.6
France	**1.0**	**1.0**	**1.1**	**2.3**	**1.7**
Italy	0.2	0.8	1.2	1.7	0.8
Netherlands	1.4	2.0	2.1	3.0	2.6
Belgium	1.3	1.7	1.5	1.7	1.4
United States	2.5	2.9	1.6	2.2	2.9
Japan	0.3	1.3	0.6	1.9	0.8
United Kingdom	2.9	2.3	1.8	1.8	1.4
Sweden	2.7	4.2	2.5	2.4	2.4
Switzerland	2.5	1.3	1.6	1.7	2.5
Canada	2.9	0.7	1.1	3.0	1.8
Australia	2.6	2.5	2.8	2.4	2.8
South Korea	3.3	2.8	2.9	3.1	2.7
Emerging economies	**5.3**	**4.8**	**5.0**	**5.6**	**5.4**
Turkey	5.2	6.0	3.3	7.3	3.1
Russian federation	0.8	–2.5	–0.2	1.5	1.9
Brazil	0.5	–3.5	–3.3	1.1	1.1
Mexico	2.8	3.3	2.7	2.3	2.0
China	7.3	6.9	6.7	6.8	6.6
India	7.0	7.5	8.7	6.9	7.4
Indonesia	5.0	4.9	5.0	5.1	5.2

Note: seasonaly and working-day adjusted data.
Sources: FMI; Insee; National statistical Institutes.

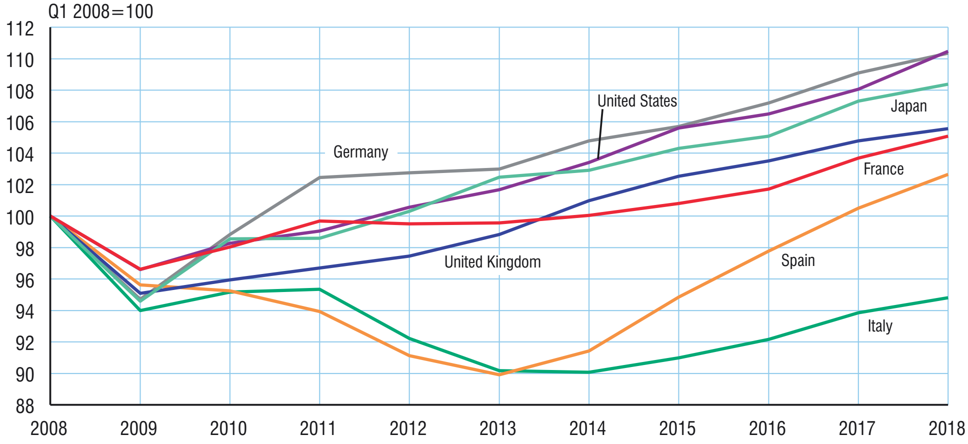
Growth slackened somewhat in the advanced economies after peaking in 2017 at its highest level since 2010

In 2018, activity decelerated slightly in all the advanced economies (+2.2% after +2.4%), impacted by factors such as the slowdown in trade. Differences persisted in terms of GDP per capita. Italy failed to return to its 2008 level, while Spain managed to do so in 2017, and built up strong momentum. GDP per inhabitant increased by around 10% in Germany and the United States but rose by only 5% in France and the United Kingdom *(Figure 6)*.

Activity ramped up in the United States

Growth in the United States accelerated in 2018 (+2.9% after +2.2% in 2017), driven by a strong upswing in government spending (+1.5% after –0.1%), in particular. Household consumption and corporate investment were boosted by the tax cuts introduced in 2018 and maintained the strong momentum built up in 2017. In the wake of investment, imports also maintained a vigorous pace (+4.5% after +4.6%). Despite the slackening of world trade, exports accelerated (+4.0% in 2017 after +3.0% in 2016). Nevertheless, at the end of the year, the federal government “shutdown” contributed to a slight slowdown in activity.

6. GDP per capita



Source: OECD.

The Brexit waiting game hampered British investment

In the United Kingdom, activity slowed in 2018 (+1.4% after +1.8% in 2017). Investment stalled (+0.2% after +3.5%). In particular, corporate investment edged down (–0.4% after +1.5%) pending the resolution of the Brexit impasse. Household consumption slackened (+1.8% after +2.2%). Household income was buoyant, and with inflation dropping slightly while remaining high (+2.5% in 2018), household purchasing power gathered pace. However, households increased their precautionary savings ratio, in anticipation of a future rise in inflation with Brexit. Exports were disappointing at the beginning of the year and declined in H1. Imports also slackened in 2018, with a downturn at the start of the year.

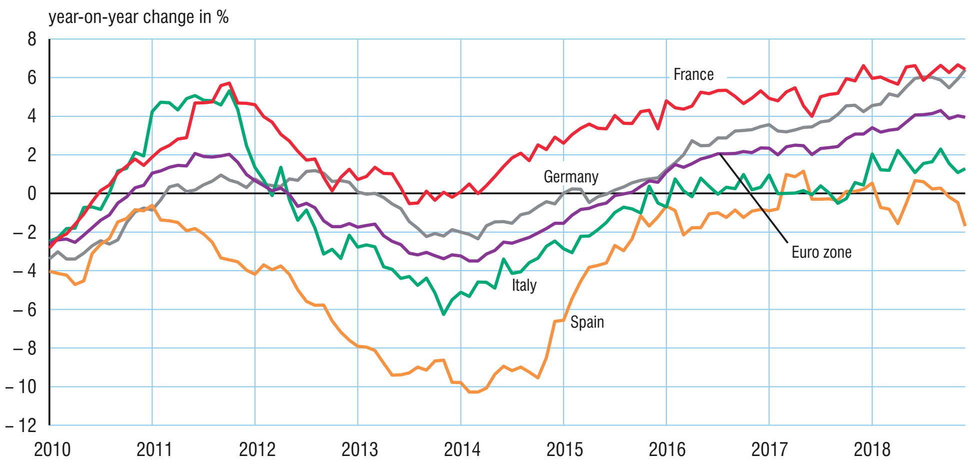
In Japan, both domestic and foreign demand slowed considerably

In the United Kingdom, activity slowed in 2018 (0.8 % after +1.9 % in 2017). Unfavourable meteorological and seismic conditions held back activity in Q1 and again in Q3. Domestic demand tailed off: only government consumption gained momentum. Private consumption slowed down (+0.4% after +1.1%), despite accelerating purchasing power. Investment was also disappointing (+1.1% after +3.0 %), due notably to the decline in public and household investment. Foreign trade stopped making a positive contribution to activity: imports remained at their 2017 rate, but exports slowed (+3.1% after +6.8%), impacted by the less buoyant world trade situation, especially with regard to Chinese imports.

In the Eurozone, corporate loans remained brisk, except in Spain

In 2018, once the results of the Italian presidential elections were known, the spread between Italian and German sovereign yields suddenly widened to 300 basis points – a level not seen since 2013. Nonetheless, the interest rates applied to enterprises and households tended to follow the European Central Bank's base rate and remained at low levels. In the Eurozone, the rates applied to enterprises varied between 1.3% in Germany and 1.8% in Spain. This low-rate environment, combined with the solid overall health of enterprises in the Eurozone, boosted the momentum of investments, and outstanding loans accelerated again (+3.8% on average over the year after +2.5% in 2017, *Figure 7*). This increase in outstanding loans was driven mainly by French and German enterprises (+6.2% and +5.6%, respectively). However, they increased more modestly in Italy (+1.6%) and slipped back in Spain (–0.3%). France stood out from its main European partners with lending to households also being more dynamic.

7. Outstanding loans to corporate have accelerated everywhere in the euro zone since 2015



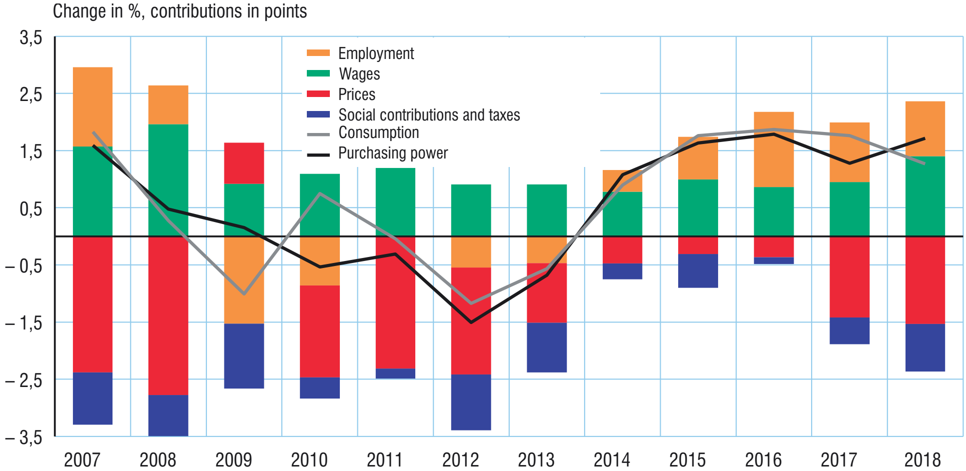
Source:ECB.

After an exceptional 2017, growth in the Eurozone tailed off

After growth of +2.5 % in 2017, activity in the Eurozone slowed to +1.8% in 2018. Household consumption decelerated (+1.3% after +1.8%). However, incomes accelerated more sharply than inflation, with the result that purchasing power increased by 1.7% overall after +1.3% in 2017 *(Figure 8)*. In this context, households in the Eurozone increased their savings ratio. Investment remained at a high level (+3.1% after +2.9%). Foreign trade also hampered growth: exports only grew by +2.2% after +5.3% in 2017, in the wake of the world trade slowdown. Imports decelerated less sharply to +3.4% after + 5.3%, favoured by the relative buoyancy of domestic demand and of investment in particular.

All the main Eurozone countries witnessed a slowdown in their economies in 2018. French GDP growth lost momentum, dropping to +1.7% after setting a record in 2017 when it reached +2.3%. Foreign trade was more supportive of growth than in 2017, but it could not compensate for the slowdown in domestic demand. Household investment slackened considerably, dropping from +5.6% to +1.9%.

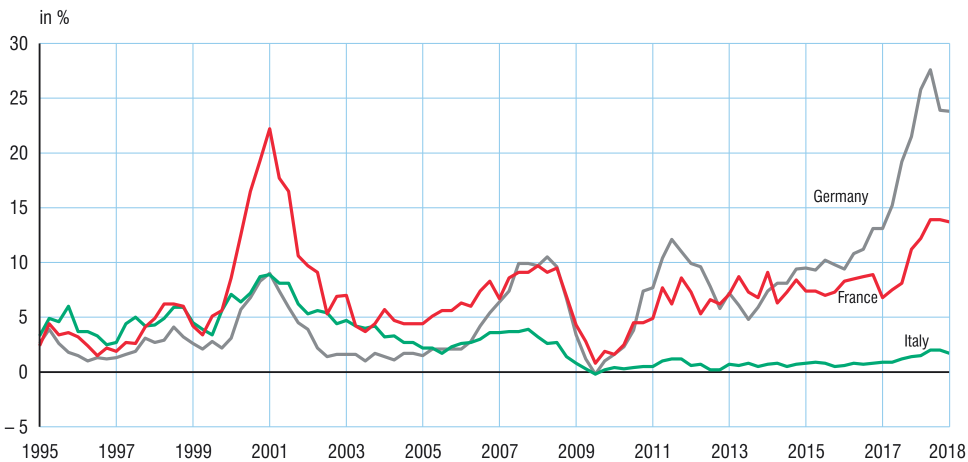
8. Household purchasing power in the euro area



Source: Eurostat.

German growth also dipped to +1.5% after +2.5%. All in all, throughout 2018, German consumption was quite sluggish, with households increasing their savings ratio by 0.7 points, despite the very low unemployment context. German exports slackened, reflecting the situation throughout the entire Eurozone. German activity slowed down, especially during H2 2018, after being initially impacted by difficulties in the automotive sector due to the implementation of the new WLTP emission standards, and subsequently by problems in the chemical and pharmaceutical sectors. German output may have peaked, as suggested by the major difficulties related to recruitment and equipment reported by business leaders in the business tendency surveys, particularly in industry *(Figure 9)*.

9. Recruiting difficulties in the industry



Note: at the end of 2018, 13.7% of French companies said they had recruitment difficulties
Source: European Commission (DG ECFIN).

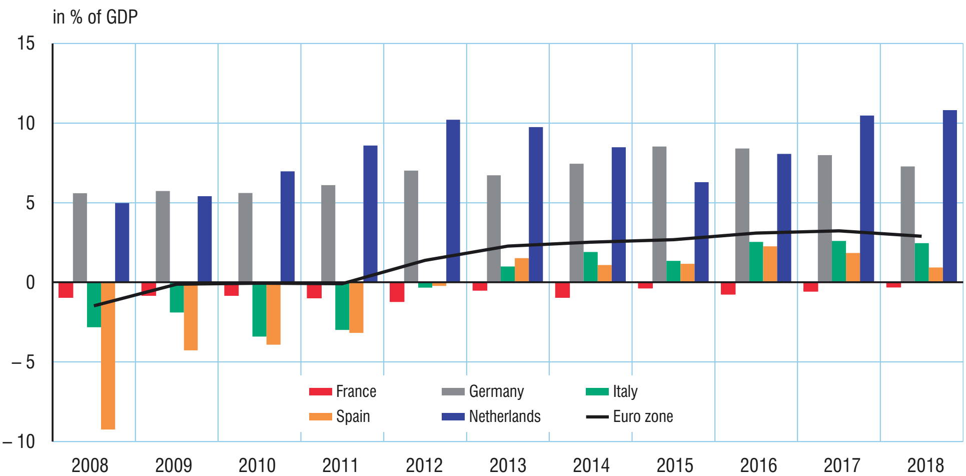
Activity decelerated markedly in Italy to +0.8% after +1.7 %. The country entered a technical recession during H2 when the internal and external growth drivers ran out of steam. On the domestic demand side, only investment in construction accelerated; the other items slowed down, especially private consumption.

Spanish activity was held up better against the general loss of momentum, growing by 2.6% after +3.0%. Domestic demand held out and foreign trade weakened somewhat, in line with world trade.

The current account surplus of the Eurozone remained high but edged down slightly

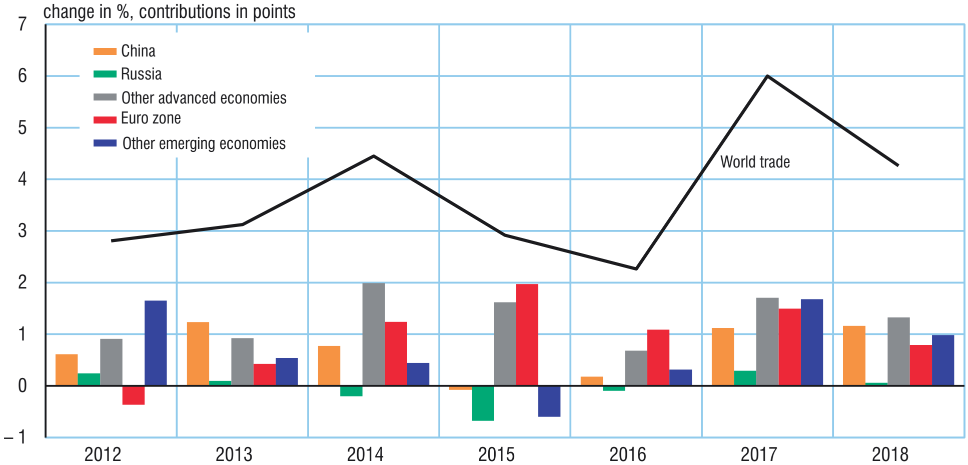
In 2018, the current account balance of the Eurozone still showed a considerable surplus. Nevertheless, it dipped slightly in relation to 2017: exports slowed more than imports, which were still driven by domestic demand. The surplus reached +3.2% of Eurozone GDP in 2017 – a record level since the creation of the single currency – and fell back to +2.9% in 2018 *(Figure 10)*. The current account surplus was very high in Germany (+7.2%; see box) and the Netherlands (+10.8%). It was also positive in Italy (+2.5%) and Spain (+0.9%): two countries that emerged from their current account deficit in 2013 and have remained in surplus ever since. The current account balance remains negative in France, although it is very close to neutral (–0.3%). These differences in relation to current account balances are inevitably reflected in the financing needs and therefore in the debt behaviours of the different institutional sectors. Consequently, French indebtedness rose, especially in the general government and corporate sectors.

10. The current account balance



Sources: Insee, Trésor.

11. World trade slows down



Sources: Trésor, Insee.

World trade slowed slightly in 2018

In 2017, the imports of emerging countries – notably in Asia – bounced back sharply, and the upswing in investments in the United States contributed to the acceleration of world trade. In 2018, world trade slowed down somewhat, while remaining buoyant: +4.3% after +6.0% *(Figure 11)*. Imports lost momentum in emerging countries other than China. They also slackened in the advanced countries but remain vigorous despite repeated announcements of stronger protectionist barriers. In the summer, economic players maintained a high level of purchases in anticipation of the introduction of higher customs duties. World trade shrank at the end of 2018. ■

Box

Germany's balance of goods and services has been in surplus since 2000

*Camille Parent and Clément Rousset**

Rising constantly since 2011, the German balance of goods and services set a new record in 2017 with +€248 billion *(Figure 1)*. A similar situation applied to the Eurozone, which posted a substantial surplus of +€521 billion in 2017. Ireland (+€89 billion), the Netherlands (+€79 billion), Italy (+€50 billion) and Spain (+€34 billion) also recorded significant surpluses. In 2018, the balance edged down marginally in Germany to +€229 billion, and the Eurozone balance also fell by a similar amount. In France, the balance of goods and services has been in deficit since 2006 and amounted to €22 billion in 2018.

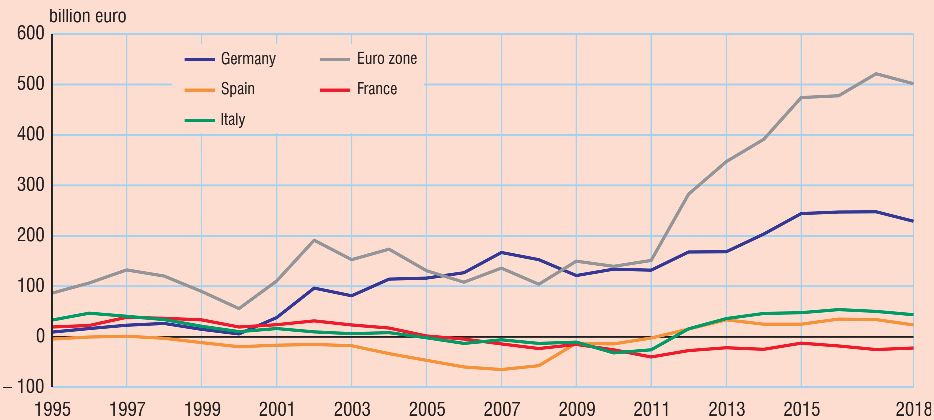
Trade was responsible for the German surplus and the French deficit

Trade in goods made the largest contribution to the Eurozone's surplus: the €510-billion surplus for trade in goods and services in 2018 broke down into +€353 billion in goods and +€148 billion in services. This phenomenon is even more pronounced in Germany where, since reunification, the balance of services has been in deficit while the balance of goods has been in constant surplus *(Figure 2)*. In 2018, the German trade surplus in goods and services of +€229 billion corresponded to +€242 billion in goods and –€13 billion in services. The slight decline in the balance of German goods and services in 2018 was due to trade in goods, despite a balance of services that is nearing equilibrium. In contrast, in France, the balance of services was positive (+€22 billion in 2018) but did not compensate for the balance of goods (–€44 billion).

The drop in the German surplus in 2018 was due to non-EU countries

In 2018, the German surplus was split equally between the European Union (+€115 billion) and non-EU countries (+€115 billion). Within the EU, Germany was in surplus vis-à-vis the Eurozone (+€8 billion) and the rest of the EU (+€67 billion). The slight downturn in the German balance of goods and services in 2018 was mainly due to trade with non-European Union countries, which had contributed substantially to the total surplus since 2012. The French economy was in deficit vis-à-vis the Eurozone (–€35 billion) and more slightly in deficit vis-à-vis non-EU countries (–€6 billion), but in surplus vis-à-vis EU countries outside the Eurozone (+€19 billion).

1. Germany and the euro zone have a large current account surplus in 2018

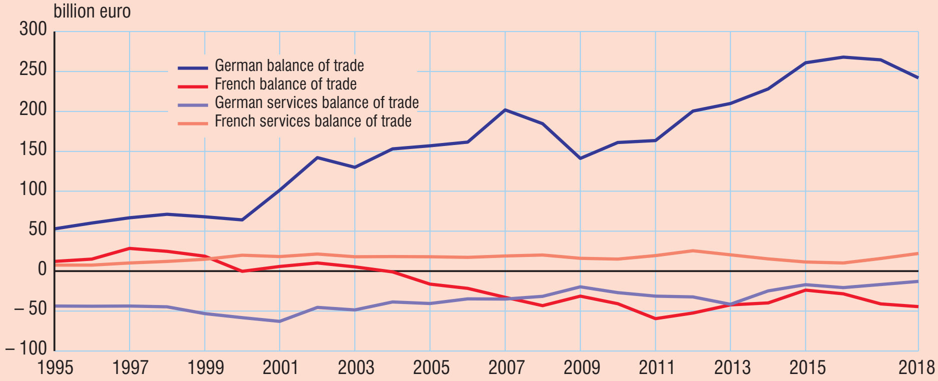


Source: Eurostat.

* Camille Parent, Clément Rousset (Insee).

Box (continued)

2. German trade largely compensates for the services deficit



Source: Eurostat.

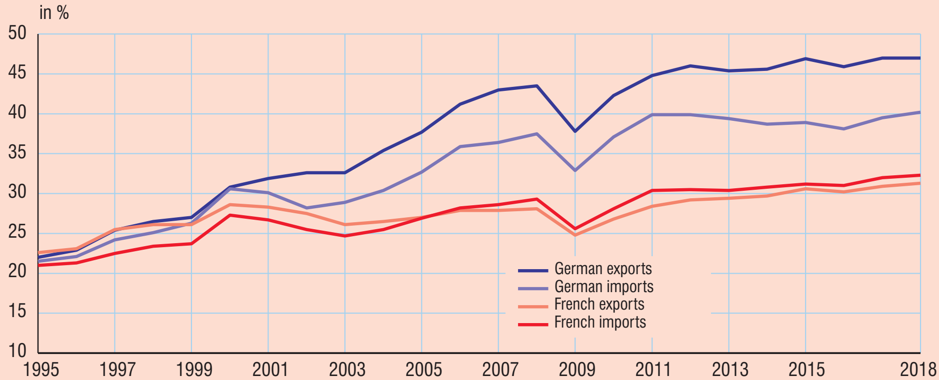
Very vigorous German exports accounted for almost half of GDP

The German surplus was due to the country's extremely vigorous exports. While German exports and imports accounted for 20% of GDP in 1993, their share of GDP has increased sharply since then, reaching 30% in 2000 *(Figure 3)*. Since then, exports have grown much more quickly than imports. In 2017, at the peak of Germany's trade surplus, exports accounted for 47.0% of GDP, against 39.5% for imports. In 2018, German exports held firm at 47.0% of GDP in 2018, while imports continued to rise, reaching 40.2% of GDP. This high proportion of exports makes Germany particularly vulnerable to the slowdown in world trade.

Since 2000, Germany has been gaining market shares

World demand for German goods has been vigorous in recent years. In addition, Germany stands out for having gained market shares since

3. The weight of exports in GDP is much higher in Germany than in France



Source: Eurostat.

Box (continued)

2000: its ratio of exports to world demand for German products increased by 10% between 2000 and 2018, whereas it declined in the other main countries in the region *(Figure 4)*. In France, this ratio fell by almost 20% between 2000 and 2018. Nonetheless, Germany's market shares have been following a downward trend after peaking in 2015.

The slowdown in private consumption has hampered imports

Conversely, imports have been meeting domestic demand. The main European countries differ structurally according to the share of imports in the different items of final demand. For example, when Germany exports a product, 38%[1] of its value, on average, has been previously imported. In France, this proportion is 32% and drops to just 30% in Italy. The imported share in investments is 29% in Germany against 24% in France. Conversely, the imported share in private consumption is higher in France (23% against 21% in Germany). The buoyancy of German exports is therefore partly reflected in imports, more strongly than in France. However, in the 2000s, imports slowed down in line with the wage moderation which held back German private consumption. Since 2011, this has tended to accelerate: the average annual growth of German consumption has risen to 1.5%, against +0.6% per year in the 2000s.

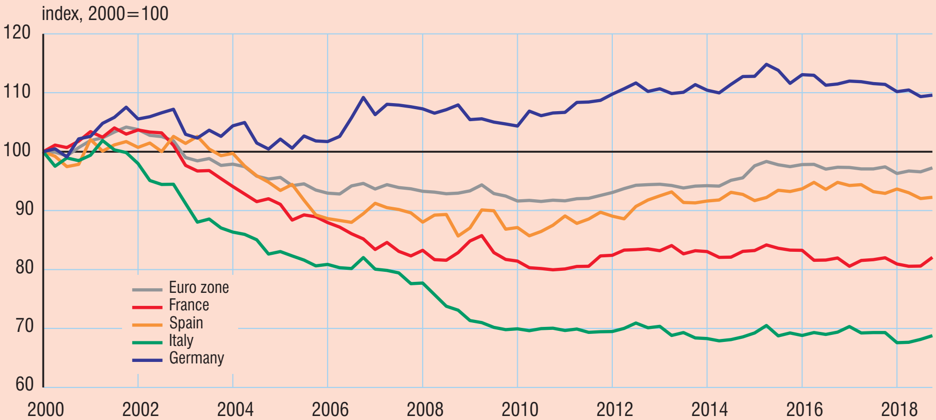
Thanks to the overall surplus, German institutional sectors are in the black

The current account surplus of a country, which corresponds to the sum of the surplus of goods and services and of current transfers and income, can be broken down, from an accounting standpoint, into the different institutional sectors. In this way, apart from financial corporations in which are in slight deficit, the German institutional sectors are all in surplus *(Figure 5)* and are therefore reducing their debts or building up assets. Conversely, in France, households are in surplus but non-financial corporations and general government are in deficit *(Figure 6)*. Spain and Italy returned to current account surpluses in 2012 and 2013 respectively: their general government sectors remain in deficit, but their non-financial corporations have returned to surplus.

Significant net financial assets in Germany

Successive annual surpluses have led to the accumulation of wealth. The most meaningful measurement of this wealth are net financial assets, which correspond to the difference between the total financial assets held and the financial liabilities. This varies from year to year, generally according to the current account balance, but it is also sensitive to revaluations of assets and liabilities (e.g. shares) and to changes

4. Since 2000, only Germany has gained market share compared to the main European countries



Sources: Eurostat; DG Trésor.

1. Calculated on the basis of the 2010 input-output tables by Eurostat.

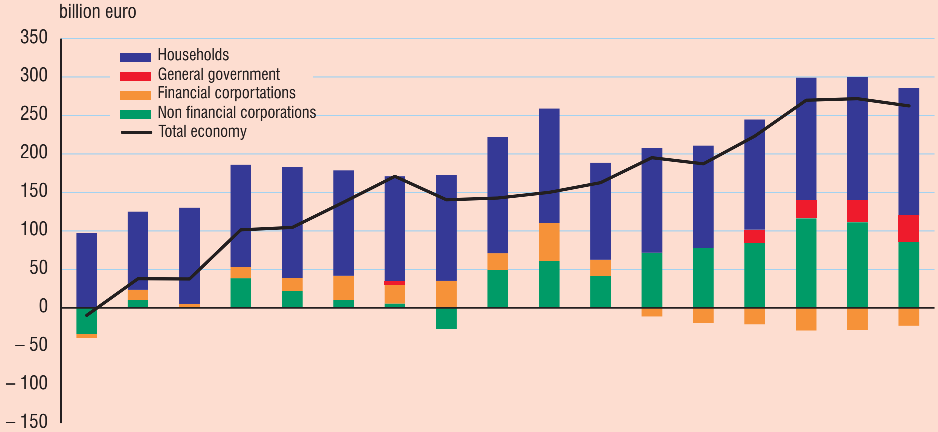
Box (continued)

in volume. As a percentage of GDP, between 2000 and 2017, the value of German net financial assets rose from –1.6% to +47.9%, whereas the opposite trend was observed in France: from +14.9% to –2.7% *(Figure 7)*. Despite an upturn in current account balances at the end of the period in Spain and Italy, the value of net financial assets in both of these countries has also been declining since 2000.

The indebtedness of non-financial corporations is low in Germany

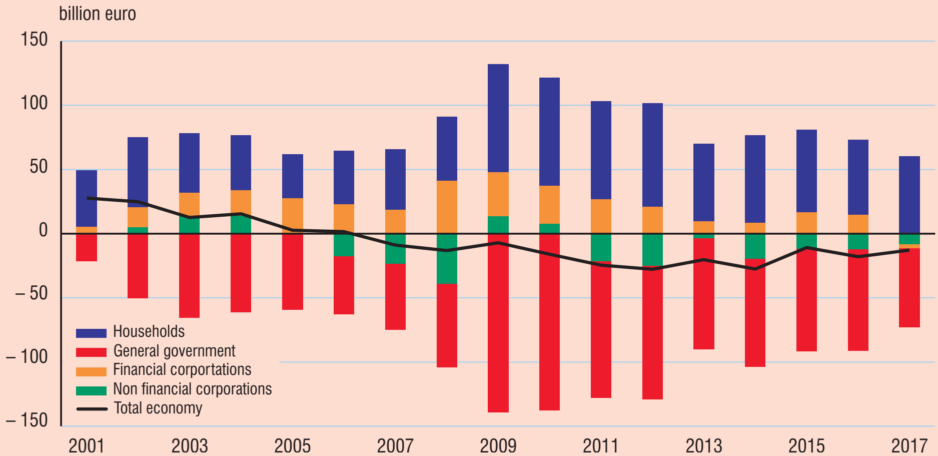
The rise in the value of net financial assets may be due to an increase in assets or a decrease in liabilities, particularly debt security liabilities and loans constituting the debt. Indeed, German non-financial corporations and general

5. In Germany, the institutional sectors are in surplus except for financial companies



Source: Eurostat.

6. In France, general government and non-financial corporations are in a recurring deficit



Source: Eurostat.

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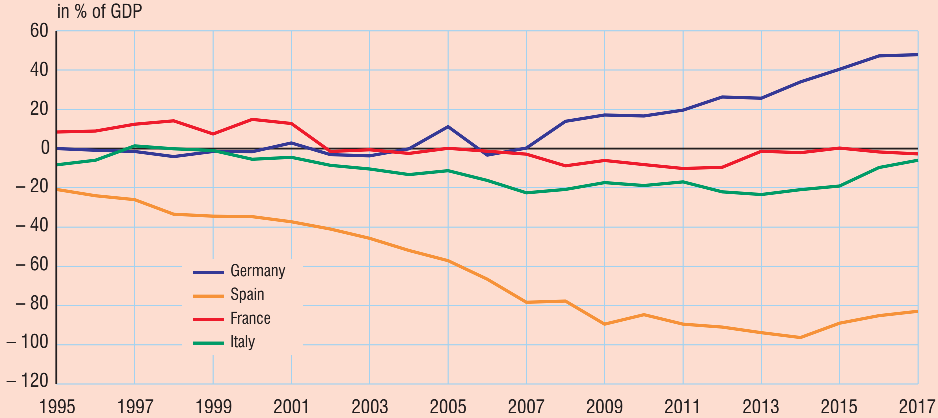
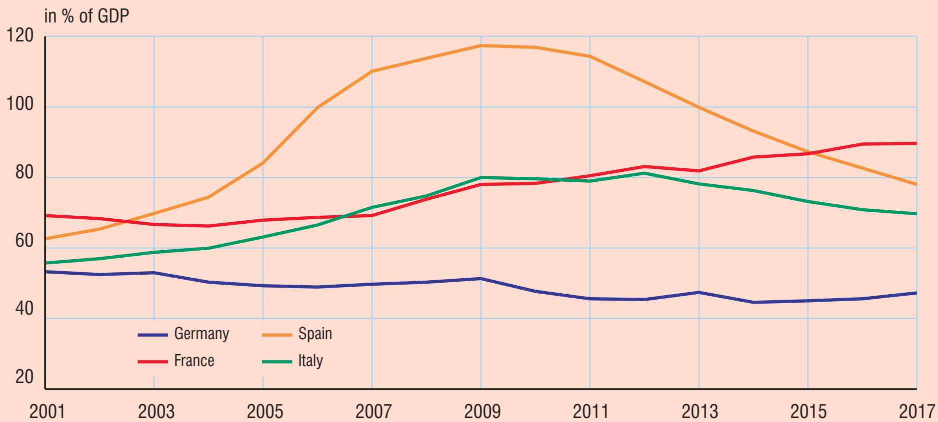
7. The German economy has been increasing its net financial value since the 2000s



Source: Eurostat.

government have a lower level of indebtedness than the other main European countries. It has dropped below 70% of GDP for general government. Similarly, German non-financial corporations have low levels of debt (less than 50% of GDP) while the indebtedness of their French counterparts has increased to 90% of GDP *(Figure 8)*, a process partly linked – in the French case – to an accumulation of liquid assets (Khder, Rousset, 2017).

8. The profil of the indebtedness of non-financial corporations in France is particularly dynamic



Source: Eurostat.

For further information

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