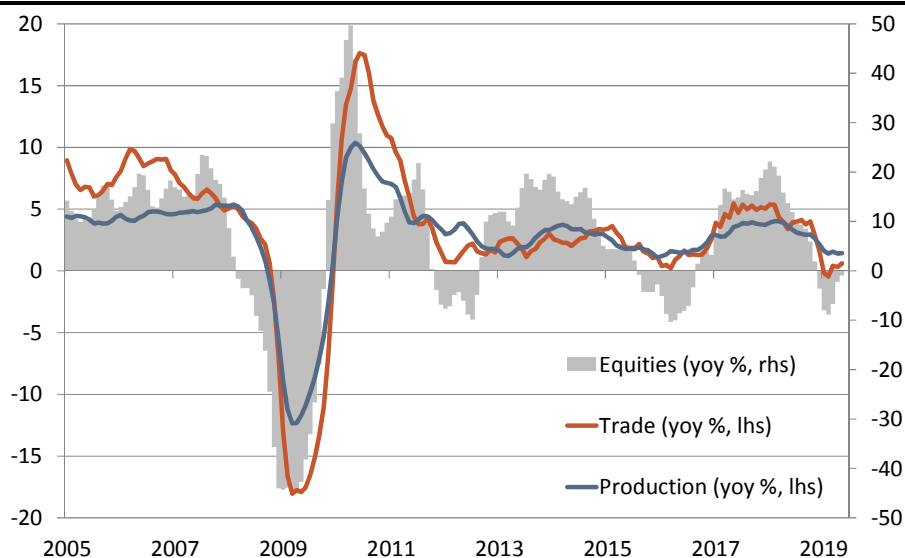


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26 July 2019

Economic crisis or a run-of-the-mill industrial slump?

Distinct cycles in trade, production and markets: so when does the next rebound come?



Three month averages. Production data is industrial production ex. construction. Global equities data is Dow Jones Global Index. Monthly data. Source: Netherlands Bureau for Economic Policy Analysis, Wall Street Journal.

- **Cycles within cycles:** When broad economic fundamentals are healthy, there is no reason to believe that a correction in one sector will tip the whole economy into a recession. In the exceptional times when that does happen, the other parts of the economy are typically primed for a downturn anyway – usually because they had built up unsustainable excesses. Our chart shows four distinct cycles in global trade, production and equities from 2005 onwards. Over that period, the only broad-based global downturn was in 2008/09 during the financial crisis. But in the ten years since, we have experienced much smaller cycles in global production and trade against a backdrop of sustained economic growth.
- **The current global industrial slump:** The current correction is nothing like the broad-based downturn of 2008/09. Instead, it is similar to the 2015/16 slide that was caused by weakness in China and the downturn in US fracking linked to the sharp drop in the oil price. Today's slump is mostly due to yet another slowdown in Chinese economic momentum and the noisy trade skirmish between the US and China.
- **China outlook:** Chinese private consumption and trade are not responding to the administration's efforts to stimulate demand through aggressive monetary easing, credit measures and tax cuts. China will therefore likely be forced to turn to more direct public spending measures. This should stabilise aggregate demand eventually. However, unlike in 2016, when Chinese private demand reacted well to the stimulus and lifted global trade volumes, the positive effects on global demand from China's recovery will probably be more moderate this time around.
- **Trade outlook:** The US-China trade spat has cast uncertainty over the global economy and trade. It weighs on confidence, production and investment. While Trump and Xi may soon broker a partial deal that includes some agriculture, industrial products and commodities such as soy and natural gas, the ongoing skirmish reflects a geopolitical rivalry between the two powers that goes way beyond trade. Further rounds of tit-for-tat remain a risk.
- **Finding a bottom:** The timing and size of a rebound in global production depends on the effectiveness of further efforts by Chinese policymakers to stabilise their economy and the resolution of the US-China trade dispute. Data on east Asian trade, which tend to lead production in export-oriented Europe by three to six months, should provide an early signal that global momentum is set to rebound. South Korean exports in June declined by 13.5% yoy – the biggest drop since January 2016. This suggests the current industrial slump has further to run and that the risks to the near-term global economic outlook remain tilted to the downside.

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