Chapter 1  Global economic trends
Section 1  Global economic trends and risks

1. Macro economy
   (1) Overview and outlook of the global economy

The global economy is on track to recovery as a whole but the pace remains moderate. In 2016, the
global economy continued to grow by 3.1% from the previous year, but it was the second lowest
growth in the eight years since the global economic crisis in 2008 (Figure I-1-1-1-1).

In the first half of 2016, uncertainty grew over the future course of the global economy due to such
factors as the weakness of some parts of the U.S. corporate sector, concerns over the slowdown of the
Chinese economy and financial market disruptions caused by the majority vote in favor of leaving the
European Union (EU) in the U.K referendum in June. However, in the second half of the year, the
global economy recovered moderately thanks to the improvement in the U.S. employment situation,
the support provided for the Chinese economy by various policy measures, and major central banks’
prompt response to the shock triggered by the United Kingdom’s vote to leave the EU, among other
factors.

According to the International Monetary Fund (IMF), while there are both upside and downside
risks to the outlook for the global economy in 2017 and beyond, medium-term risks are skewed to the
downside. On the positive side, it is expected that fiscal stimulus measures implemented in such
countries as the United States and China will prop up their economies; that crude oil prices will be
stabilized by the agreement reached by member countries of the Organization of the Petroleum
Exporting Countries (OPEC) to reduce crude oil production; and that emerging economies will recover
as commodity prices have hit bottom. On the other hand, there remains strong downward pressure due
to structural problems, including the decline in major countries’ potential economic growth, the
stagnancy of global trade and investment, and the widening income inequality. Moreover, it is
necessary to pay close attention to the risks such as rising protectionism pressure, the impact on the
emerging economies of a faster-than-anticipated tightening in global financial conditions, and
geopolitical tensions in such regions as the Middle East and Asia. In 2017, the global economy will
maintain the momentum of recovery continuing from the latter half of 2016, but the pace is expected
to remain moderate, with the growth rate staying below the level before the global economic crisis.
The IMF projected the global GDP growth rate at 3.5% in 2017 and at 3.6% in 2018 (Table I-1-1-1-2).

Figure I-1-1-1-1   Changes in and outlook of global real GDP growth

Source: IMF World Economic Outlook, April 2017
(2) Economic trends in advanced and emerging market and developing economies

Advanced economies continued recovering moderately. In the first half of 2016, the European economy recovered moderately, led by private consumption, and the U.S. economy also got back on the growth path, supported by robust private consumption. However, the Japanese economy’s growth remained weak due to a decline in capital investment and the impact of the Kumamoto earthquakes. In the second half, the weakness of some parts of the U.S. corporate sector disappeared, while the Japanese economy recovered moderately because of a pickup in exports. The euro economy is expected to continue growing at a rate higher than its potential growth rate, but attention needs to be paid to the negotiations over the terms of the United Kingdom’s exit from the EU, the key elections scheduled to be held in major European countries and the future course of the Italian banking problem.

As for emerging market and developing economies, the situation varies from country to country. In the first half of 2016, recessions deepened in Russia and Brazil, whose economies depend heavily on natural resources. The Chinese economy slowed down due to excess production capacity, excess debts and a housing market correction. The Indian economy performed well against the backdrop of the progress in structural reforms, and the Russian and Brazilian economies are starting to show signs of overcoming their stagnancy as primary goods prices have been bottoming out since the second half of 2016.

Table I-1-1-1-2  Overview of IMF World Economic Outlook

<table>
<thead>
<tr>
<th></th>
<th>2016</th>
<th>2017 &lt;projection&gt;</th>
<th>2018 &lt;projection&gt;</th>
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<tr>
<td>UK</td>
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<tr>
<td>Canada</td>
<td>1.4</td>
<td>1.9</td>
<td>2.0</td>
</tr>
<tr>
<td>Emerging market and developing economies</td>
<td>4.1</td>
<td>4.5</td>
<td>4.8</td>
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<tr>
<td>Russia</td>
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<td>ASEAN-5*2</td>
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<tr>
<td>South Africa</td>
<td>0.3</td>
<td>0.8</td>
<td>1.6</td>
</tr>
</tbody>
</table>

Notes:
1. The figures for India are on a fiscal year basis. The growth rates are on a market price basis.
2. ASEAN 5 refers to Indonesia, Malaysia, the Philippines, Thailand, and Viet Nam.
Reference: Assumed crude oil prices: $42.84 in 2016, $55.23 in 2017, and $55.06 in 2018
Source: IMF World Economic Outlook, April 2017.

(3) Economic sentiment
The global Purchasing Managers’ Index (PMI),\(^1\) a leading economic indicator, has stayed above the boom-or-bust line of 50 for both the manufacturing and service industry since the beginning of 2016. The pace of rise was slower for emerging economies than for advanced economies (Figure I-1-1-1-3).

\(^{1}\) The Purchasing Managers’ Index is an indicator of business conditions, including production, order receipt, employment and other items, expressed as a numerical value calculated based on questionnaire surveys conducted with purchasing managers in individual business sectors. It is considered that a value of 50 means no change in the conditions, a value of below 50 means a deterioration of the conditions and a value of above 50 means an improvement of the conditions.
(4) Trade

The global trade volume, which was growing at a pace nearly double the GDP growth rate before the global economic crisis, fell steeply in 2008, but after hitting bottom in 2009, it recovered in 2010 to a level above where it had been before the crisis. However, after the recovery lost momentum due to the effects of the European debt crisis, among other factors, the so-called “slow trade” phenomenon has continued since 2012, with the growth rate of the global trade volume remaining lower than the global economic growth rate, underscoring the weakening of trade’s role as a driving force of the global economy (Figure I-1-1-1-4).

Figure I-1-1-1-4 Change in global real GDP and merchandise trade volume

Notes: Figures for the global trade volume are the average of imports and exports. The GDP growth rates are the results of WTO calculation, which are different from those by the IMF above. Source: World Trade Organization
According to the World Trade Organization (WTO), the growth rate of the global trade volume (merchandise trade volume)\(^2\) in 2016 declined by 1.3 points from 2.6% in the previous year to 1.3%, which was the lowest growth rate since 2009, immediately after the outbreak of the global economic crisis. The slowdown was mainly due to the effects of a steep decline in the growth rate of the import volume of emerging market and developing economies, including China, to 0.2% compared with the previous year. In the case of advanced economies as well, the growth rates of the import volume and the export volume dropped sharply from the previous year, to 2.0% and 1.4%, respectively. While the WTO forecasts a growth rate of 2.4% compared with the previous year for the global trade volume in 2017, it expects that the growth rate could range from 1.8% to 3.6% given the deep uncertainty over the global economy (Table I-1-1-1-5).

As downside risks that could push down the trade volume, the WTO cited a possible increase in the application of protectionist trade policies, tightening of monetary policy due to a rise in the inflation rate, an economic growth slowdown resulting from tighter monetary and fiscal policies adopted due to a rise in the inflation rate, and the future course of the negotiations over the terms of

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\(^{2}\) “Trade volume (merchandise trade volume)” as referred to by the WTO represents the average of imports and exports.
the United Kingdom's exit from the EU. 3

WTO Director-General Roberto Azevêdo said that although it is true that “trade plays a very beneficial role in the economy overall” and “drives growth, job creation and development,” the concerns of people who have lost their jobs cannot be ignored. He pointed out that “eight in ten manufacturing jobs are lost to innovative technologies and higher productivity” and that “at the domestic level, policies are needed to help support the workers of today and train the workers of tomorrow.” He expressed concerns over the recent rise of protectionism, saying: “Closing the borders to trade would only worsen the situation — it would not bring the jobs back, it would make more jobs disappear.”4

Meanwhile, the IMF pointed out that “cyclical factors,” such as the overall weakness in economic activity, in particular in investment, has been the primary factor behind the slowdown in the pace of global trade growth since 2012. In addition, the IMF observed that “structural factors,” such as the stalling of trade liberalization, the recent rise of protectionism and the decline in the growth of global value chains, are also weighing on global trade growth. The IMF noted that because global trade will remain stagnant unless growth and investment increase, individual countries should not only carry out further trade reforms but also implement policy measures that promote the diffusion of skills and know-how necessary for revitalizing trade to the people who have been affected by structural changes such as technological innovation and globalization.5

(5) Investment

In the mid-2000s, when the global economy was performing strongly, many companies around the world made active capital investment in emerging economies that continued to record high growth, such as China. During this period, capital investment, coupled with booming demand for resources, acted as an engine accelerating trade growth. As a result, the growth rates of the global import and investment volumes outpaced the GDP growth rate (Figure I-1-1-1-6). However, since 2011, companies have grown cautious about investment activity because of the collapse of the credit bubble in advanced economies, including the United States and European countries, and excess investment in China and other problems generated investment adjustment pressure, causing both capital investment and imports to slow down significantly. Since 2012, the growth rates of capital investment and imports have remained weak compared with the GDP growth rate. The IMF pointed out that while the slowdown in investment by emerging economies reflects the economic slowdown and rebalancing in China, the weakness of capital investment and imports by commodity exporters facing a difficult macroeconomic environment (e.g. Brazil and Russia) is also a significant factor.6

(6) Consumption

Final consumption expenditure in major countries has been on a recovery track after slumping at the time of the global economic crisis and the European debt crisis, but the situation has not been uniform (Figure I-1-1-1-7). Final consumption expenditure has generally been recovering in advanced economies since 2014, but among emerging economies, there has been a divide between India and China, where the expenditure has been robust, and Brazil, Mexico and Russia, where it has been weak. Presumably, consumer sentiment in Brazil, Mexico and Russia has been dampened by a rise in import prices due to the weakness of their currencies and the ensuing consumer price rise and interest rate hikes, among other factors.

(7) Industrial Production

The industrial production index recovered to the level before the global economic crisis in emerging economies in the autumn of 2009 and has remained firm since then. While industrial production in Asian emerging economies has been leading the overall recovery in the emerging

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3 Trade Publicity (JETRO), “Global Merchandise Trade Volume Growth Remains Low at 1.3% in 2016” (April 20, 2017)
4 Remarks by WTO Director-General Roberto Azevêdo at a WTO trade forecasts press conference (April 12, 2017)
5 World Economic Outlook, October 2016 (IMF)
6 World Economic Outlook, April 2016 (IMF)
economies, industrial production in Central and South American economies has remained on a downtrend. Meanwhile, industrial production in advanced economies has remained on the path of moderate recovery since December 2010 after going through the global economic crisis. In the United States, industrial production recovered in the second half of 2013 to the peak level before the global economic crisis and has remained flat after continuing to grow until 2014. In the euro area, although the recovery of industrial production from the global economic crisis stalled because of the deepening of the European debt crisis and remained weak for a long period of time, production has started to pick up recently. In Japan, industrial production remained weak due to such factors as the effects of the Great East Japan Earthquake, but it has recently been recovering (Figure I-1-1-1-8).

**Figure I-1-1-1-6  Changes in growth rates of global investment, import volumes, and real GDP**

Source: IMF World Economic Outlook, April 2016.

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Source: IMF World Economic Outlook, April 2016.
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Notes: Selected commodity exporters: Angola, Bahrain, Belarus, Brazil, Ecuador, Kazakhstan, Russia, Ukraine, and Venezuela.
Source: IMF World Economic Outlook, April 2016.
Figure I-1-1-1-7  Changes in growth rates of final consumption expenditures

Source: UN Data.

Source: UN Data.
Figure I-1-1-1-8  Changes in industrial production indices

Source: Data from CPB World Trade Monitor, CPB Netherlands Bureau for Economic Policy Analysis.

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According to the International Labour Organization (ILO), the global number of unemployed people increased by around 3.2 million people from the previous year to 198 million people in 2016 and is projected to rise to 201 million people in 2017. The global unemployment rate is projected to rise from 5.7% in 2016 to 5.8% in 2017. The labor market condition is deteriorating seriously in emerging and developing economies, and the deterioration is particularly acute in Central and South America (mainly Brazil) and sub-Saharan Africa. On the other hand, in advanced economies, the number of unemployed people has been decreasing and the unemployment rate is expected to decline from 6.3% in 2016 to 6.2% in 2017, but the pace of improvement is slowing down. Meanwhile, youth unemployment has become a serious problem worldwide. Although the global youth unemployment rate has been improving moderately in the past few years, it is estimated to rise to 12.8% in 2016 and to 13.7% in 2017 (Figures I-1-1-1-9 and I-1-1-1-10).
Figure I-1-1-1-9  Changes in unemployment rates in major countries

Source: IMF World Economic Outlook, April 2017

Figure I-1-1-1-10  Changes in youth unemployment rates

(Comparison of unemployment rates between youth and all age groups)

Source: ILOSTAT.
2. **Financial market trends**

(1) **Foreign exchange rates**

Regarding foreign exchange rates, market volatility has grown since the beginning of 2016 against the backdrop of such factors as developments related to interest rate hikes in the United States, concerns over the slowdown of the Chinese economy, concerns over the soundness of the European banking sector, and an oil price decline. Since the U.S. presidential election in November of the same year, there emerged signs of U.S. interest rates rising and the dollar appreciating amid high expectations for the new Trump administration’s economic policy (Figure I-1-1-2-1).

![Changes in exchange rates](source: Thomson Reuters EIKON)
(Emerging market and developing economies)

Source: Thomson Reuters EIKON.

(2) Stock prices
In 2016, global stock prices stayed on a downtrend until the first half of February due to lower-than-expected readings of U.S. and Chinese economic indicators. However, stock prices regained the losses recorded early in the year because of a recovery in the crude oil price and receding of expectations of a U.S. interest hike. As a result of the United Kingdom’s decision at the end of June to leave the EU, stock prices plunged at various times due to concerns over the future course of the European economy but recovered from market turbulence in a short period of time. In the second half of the year, as optimism about the U.S. economy spread due to a significant improvement in the U.S. employment situation, stock prices rose from the summer onwards. However, stock prices got stuck in a narrow range at a high level amid crosscurrents of positive and cautious remarks made by officials of the U.S. Federal Reserve Board (FRB) about an interest rate hike. Moreover, in October, concerns over the global economy were rekindled by increased expectations of a U.S. interest rate hike and a decline in exports from China. In addition, the crude oil price declined because of a lack of progress in negotiations over production reduction at OPEC and uncertainty over the future grew ahead of the U.S. presidential election, causing stock prices to weaken. However, following Mr. Trump’s victory in the presidential election, expectations for an expansionary fiscal policy increased, leading to a rise in stock prices in the United States and Europe. When the crude oil price rose after OPEC reached a final agreement on production reduction at the end of November, stock prices also went up. In the first half of December, global stock prices climbed to the highest level since the beginning of the year (Figure I-1-1-2-2).
In the first half of 2016, the yields on 10-year government bonds in major countries declined, as risk aversion grew due to the slowdown of the Chinese and U.S. economies, a drop in the crude oil price and the U.K. decision to leave the EU, among other factors. However, in the second half, the yield on U.S. government bonds rose rapidly because of the recovery of the U.S. economy and the presidential election victory of Mr. Trump, who was advocating a policy of stimulating the economy through expansion of fiscal expenditure. Although the yields on 10-year government bonds in emerging economies, such as Brazil, Turkey and Mexico, were generally on a downtrend in the first half of the year, they generally rose in the second half.
year, they rose in the second half. Particularly notable was the rise in interest rates in Mexico, which is expected to be strongly affected by the Trump administration’s hardline trade and immigration policies. For the moment, the yields will remain under upward pressure amid expectations for a stimulative economic policy. However, the bond market condition is expected to calm down gradually as the actual picture of the Trump administration becomes clear (Figure I-1-1-2-3).

**Figure I-1-1-2-3  Changes in yields on 10-year government bonds**

![Graph showing changes in yields on 10-year government bonds](source: Thomson Reuters EIKON)

Source: Thomson Reuters EIKON.
(4) Policy interest rates

The global economic growth rate dropped steeply due to the effects of the global economic crisis, fueling concerns over deflationary risk in various countries. In 2012, the European debt crisis emerged, and although the U.S. and European central banks quickly implemented significant policy interest rate cuts, this move did not lead to an economic recovery. As policy interest rates reached or came close to zero in major countries, including the United States, EU and Japan, these countries introduced an accommodative monetary stance based on unconventional monetary policy (quantitative easing and credit easing) in addition to the low interest rate policy. However, in the United States, where the employment situation has improved and the economic conditions are favorable, interest rate hikes have been implemented three times, in December 2015, December 2016 and March 2017, and additional interest rate hikes are expected to be implemented twice or so by the end of 2017 in consideration of the impact on the domestic and foreign economies. In Japan, negative interest rates and the yield curve control were introduced in 2016, and the monetary easing is expected to continue for some time while the United States is moving to normalize its monetary policy.

Among emerging economies, many Asian countries have continued accommodative monetary policy instead of following in the footsteps of the United States after its resumption of interest rate hikes. Factors behind this include the disinflation spreading amid the relative stability of exchange rates and the ensuing increase in the need for policy interest rate reduction. Indonesia opted to start lowering the policy interest rate at the beginning of 2016, as did India in October. Turkey, which is suffering from the weakness of its currency, reduced the policy interest rate in November 2016 for the first time in 33 months amid the sluggishness of the economy. Mexico has continuously implemented interest rate hikes since December 2015 in order to deal with the depreciation of its currency and rising inflation. On the other hand, Brazil has implemented interest rate reduction since October 2016 because of the recovery of its currency from depreciation and a decline in the inflation rate. Moreover, in 2017, Russia lowered the policy interest rate for two months in a row, in March and April (Figure I-1-1-2-4).

Figure I-1-1-2-4  Changes in policy interest rates

![Changes in policy interest rates](image)

Source: Thomson Reuters EIKON.

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8 The U.S. Federal Reserve Board (FRB) decided on the first interest rate hike in three months since December 2016 at a meeting of the Federal Open Market Committee (FOMC) on March 15, 2017. In the future outlook of policy interest rates that was announced at the same time, the FRB projects two additional interest rate hikes by the end of 2017.
According to the IMF, while economic activities are picking up worldwide thanks to buoyant financial markets and a cyclical recovery in manufacturing and trade, binding structural impediments, such as low productivity growth and high income inequality continue to hold back a strong recovery, and the balance of risks for global economic growth remains tilted to the downside over the medium term. The downside risks arise from the several potential factors cited below. Since these risks are interconnected and can be mutually reinforcing, close attention is needed.

- An inward shift in policies, including toward protectionism, with lower global growth caused by reduced trade and cross-border investment flows
- A faster-than-expected pace of interest rate hikes in the United States, which could trigger a more rapid tightening in global financial conditions and a sharp dollar appreciation, with adverse repercussions for vulnerable economies
- An aggressive rollback of financial regulation, which could spur excessive risk taking and increase the likelihood of future financial crises
- Financial tightening in emerging market economies, made more likely by mounting vulnerabilities in China’s financial system associated with fast credit growth and continued balance sheet weaknesses in other emerging market economies
- Adverse feedback loops against the background of weak demand, low inflation, weak balance sheets, and anemic productivity growth in some advanced economies operating with high levels of excess capacity
- Geopolitical tensions, domestic political discord, risks from weak governance and corruption, extreme weather events, and terrorism, security concerns, etc.

Source: Thomson Reuters EIKON.

3. Risk factors for global economic growth

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Source: Thomson Reuters EIKON.

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According to the IMF, while economic activities are picking up worldwide thanks to buoyant financial markets and a cyclical recovery in manufacturing and trade, binding structural impediments, such as low productivity growth and high income inequality continue to hold back a strong recovery, and the balance of risks for global economic growth remains tilted to the downside over the medium term. The downside risks arise from the several potential factors cited below. Since these risks are interconnected and can be mutually reinforcing, close attention is needed.

- An inward shift in policies, including toward protectionism, with lower global growth caused by reduced trade and cross-border investment flows
- A faster-than-expected pace of interest rate hikes in the United States, which could trigger a more rapid tightening in global financial conditions and a sharp dollar appreciation, with adverse repercussions for vulnerable economies
- An aggressive rollback of financial regulation, which could spur excessive risk taking and increase the likelihood of future financial crises
- Financial tightening in emerging market economies, made more likely by mounting vulnerabilities in China’s financial system associated with fast credit growth and continued balance sheet weaknesses in other emerging market economies
- Adverse feedback loops against the background of weak demand, low inflation, weak balance sheets, and anemic productivity growth in some advanced economies operating with high levels of excess capacity
- Geopolitical tensions, domestic political discord, risks from weak governance and corruption, extreme weather events, and terrorism, security concerns, etc.

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