The markets come to the fore

Markets become unsettled. There was a remarkable period of financial instability between the end of January and early February, with spikes in volatility and the main stock markets incurring losses of around 10%. This episode was mainly due to US inflation and wage growth being higher than predicted, pushing up long-term interest rates and changing expectations regarding thepace of interest rate hikes by the US Federal Reserve (Fed). We should take good note of the lessons provided by this episode. The US economy is in a very mature phase of its business cycle. Pressure on inflation and wages is therefore likely to increase even further. As long as this process is gradual, the Fed will be able to normalise monetary conditions as planned. But more upward surprises are quite possible and this could result in further episodes of volatility and stock market corrections. In fact, fears this might happen are now greater due to the various expansionary fiscal measures implemented by the Trump administration. A substantial increase in federal spending has been approved in the past month which, in addition to having considerable impact on the US public deficit, is also likely to increase pressure on inflation, at least to some extent.

But we should still be optimistic: global economic activity is speeding up. World GDP growth figures for Q4 2017 and various economic activity indicators for 2018 have been very positive. A case in point is the PMI business sentiment index which, in January, reached its highest level since March 2011. Also important is the fact that this dynamism is widespread, observed both in the advanced and emerging economies. Plus the evidence points to the continuation of the *momentum* of the global economy over the coming quarters, implying an acceleration of growth. Specifically, we expect world GDP growth to speed up from 2017's rate of 3.7% to a remarkable 3.9% this year. This figure is slightly above the average GDP growth observed in the past few decades.

Europe confirms its positive outlook. Macroeconomic indicators at the end of 2017 and beginning of 2018 certifythe euro area's good cyclical position. The strong push provided by the global economy, the continuation of accommodative monetary policies by the ECB and strong confident climate boosting job creation are the main factors supporting Europe's *momentum*. We have therefore raised our euro area growth forecast by 0.3 pp, both for 2018 and 2019, up to 2.5% and 2.0%, respectively. The latest growth figures posted by Germany and France are particularly strong. It is evident that Germany's political stalemate of the past few months has not hampered its economic performance. Now all eyes are on Italy which, after its general elections on 4 March, will have to try to form a stable government to address the structural problems still affecting its economy.

A favourable outlook for Spain and Portugal in 2018. Both countries are benefitting greatly from the economic dynamism of the world in general and the euro area in particular. Spain posted good growth figures for Q4 2017, as well as positive data in different areas and sectors (dynamic labour market, consolidation of the upward cycle in real estate and strong credit and tourist activity). We therefore expect 2.8% GDP growth for the whole of 2018, clearly outperforming the average for the advanced economies. One very important aspect of the current expansionary cycle is that it is more balanced than the previous ones, with both domestic and external demand making a considerable contribution to growth. Prospects are also highly favourable for Portugal. Its economy grew steadily in Q4 2017 (2.4% year-on-year), bringing the annual figure for 2017 to 2.7%, the highest rate for the past 17 years. The outlook for the next few years is also encouraging with growth expected to reach 2.4% in 2018 and 2.3% in 2019.