

Higher growth, higher uncertainty

«**Mr. President, the floor is yours**». At conferences in English, after the customary introductions, this is often how the speaker is invited to talk. The new President of the US has certainly done more than merely take the floor: he has placed himself centre stage and dominated the agenda since winning the election. What the new Trump administration's programme hopes to achieve is laudable as it aims to improve capacity to create prosperity and bring back into the system some of the people who have been hit hard by economic developments over the past few years. It is not so much the end as the means that are in question, causing considerable doubts and therefore uncertainty. One initial area of action concerns fiscal expansion, combining tax cuts with increased infrastructure spending. Such proposals make sense as US corporate tax is among the highest in the world and many of the country's infrastructures are obsolete. Nonetheless, given that the US economy is close to full employment, this expansionary fiscal policy could have limited success in terms of growth, while inflation and the trade deficit may increase more than expected. To fan the flames of debate even further regarding whether any impulse is actually needed, the US economy was markedly dynamic at year-end 2016. Growth was 1.9% year-on-year in Q4 and 1.6% for the year as a whole, although this figure conceals a weak start to the year and unmistakable acceleration in the last six months. The country has also seen its largest wage increase since 2009 and inflation is picking up, a trend that will gain traction over the coming quarters. It comes as no surprise that the latest comments by the Federal Reserve (Fed) suggest interest rate hikes may end up being more aggressive if such unwanted effects of fiscal expansion come about. In line with this view, CaixaBank Research expects three increases in the Federal funds rate in 2017. The markets, however, have tended to assume higher growth but not so much inflationary risk, as can be seen by investors expecting only two hikes in 2017.

Local policy, global tension? The second course of action proposed by the US administration is even more controversial. Under the slogan «America first», it is planning, at least rhetorically, a clear shift towards protectionism. This formula openly contradicts an irrefutable lesson from history: economic integration is a powerful way to create wealth. It was how today's advanced countries became prosperous and is the way to get large numbers of people in emerging countries out of poverty. As protectionism is such an outmoded formula,

economic analysts tend to expect the actual implementation of such an agenda to be pragmatic. Nonetheless, the profile of some of the people appointed in key positions, the first actions carried out after taking possession (the executive order pulling out of the TPP and the announcement of the renegotiation of the North American Free Trade Agreement or NAFTA) and declarations made by Trump himself have all fuelled uncertainty. Potential trade conflicts (especially with the revision of NAFTA) and diplomatic tensions (with already blatant disagreements with China and the EU) are the greatest risks.

But, even so, the economy is doing well. Fortunately this shock of uncertainty is occurring within a recovery in activity that looks like continuing. Towards the end of 2016, the growth rate speeded up in Europe and China and, as mentioned previously, remained at a reasonable rate in the US. In 2016 Q4 the euro area grew by 0.5% quarter-on-quarter (1.8% year-on-year), the UK by 0.6% quarter-on-quarter (2.2% year-on-year) and China accelerated to 6.8% year-on-year (6.7% in the three previous quarters). This good growth rate is being helped by a number of underlying global factors such as an easy money policy in most countries, the slight upward trend in oil prices and, except for some advanced countries, the lack of any inflationary tensions. All these factors will continue in 2017, and very much so. CaixaBank Research therefore predicts that, after growing by 3.1% in 2016, the world economy will expand by 3.4% in 2017.

The Spanish economy is on the verge of a moderate slowdown. After strong growth of 3.2% in 2016, the economy will grow a little more slowly in 2017 (2.6%) due to waning support from temporary factors (particularly oil prices and fiscal policy). This is nevertheless an enviable growth rate, better than most of our European partners. However, the balance of risks does not allow for complacency since external uncertainty, as we have seen, is not diminishing and there are still some sizeable domestic challenges (budget deficit, pensions, labour market, etc.). Spain should therefore focus strongly on reforms again, as the country's challenges may be medium and long-term but the time for discussion and action is now.