Challenges for the new economic chapter

The beginning of a new economic chapter is marked by the sensation that we may be approaching a turning point in the behaviour of the economy. The information published in recent weeks has confirmed a much better performance of the global economy in the first half of the year than had been anticipated a few quarters ago, with annualised growth of almost 3% up to June, further improvements in the deflation process and the continued strength of labour markets. In addition, the summer passed without any major upsets, and this was in spite of new focal points of geopolitical instability emerging (Sahel, etc.) and the sensation that China will have major difficulties in overcoming the middle income trap, which will have significant medium-term consequences for global growth and for the reorganisation of value chains and trade flows.

But a mill cannot grind with water that is past and that window of hope provided by the behaviour of the business cycle at the beginning of the year is already narrowing due to a confluence of factors: the dilution of tail winds (positive base effects in energy, the reopening of big economies such as China, the normalisation of the bottlenecks and of excess savings following the pandemic), the restrictive effects on demand of the monetary tightening accumulated over the past year and a half, the more than 20% increase in the price of oil in the last two months, the sharp deterioration of business expectations – especially in the industrial sector – and the difficulties experienced by China and Germany in getting to grips with this new post-COVID world. Therefore, with domestic demand weakening and with little hope of greater contribution from foreign demand (judging by the weak signals from global trade), we are heading towards a new phase of growth marked by a weakening of global economic activity. This weakening will not occur evenly, however, with a sharper slowdown anticipated in Europe than in the US, as the recent appreciation of the dollar indicates. If such a temporary bump in growth allows a new balance to be reached that helps to bring down inflation, then central banks could begin to take the pressure off after months of trying to make up for lost time. All this would translate into global growth in 2024 being around 0.3-0.4 pps below that of this year, albeit with a different profile, as the economy would pick up speed during the course of the year, unlike in the current one.

The problem is that the much-sought-after soft landing, especially when it comes to taming an inflationary process, is an unstable equilibrium situation in the face of any new negative shock. We cannot, therefore, rule out the possibility of scares along the way as we lay the foundations for growth in the second half of 2024, at which point central banks could begin to relax the tone of their monetary policy. On the supply side, it seems unlikely that there will be much positive news in the short term, judging by the pattern of energy prices this summer or the situation in China or Germany, which serve as the main barometers for industries that are adapting to the shifting patterns in demand and the rebalancing of geopolitics. The fall in inflation will certainly provide a respite for households' purchasing power in much of the OECD, but in any case this will only be a mitigating factor in the face of the weakening economic activity we can expect to see in the coming months.

In short, ahead of us lies a period of economic slowdown which should help the underlying measures of inflation to begin to consolidate in the 3%-3.5% range. This period with very weak growth – almost stagnation – and with inflation still at levels that are uncomfortable for central banks will pose a challenge for the coordination of economic policy, especially given the need for a new fiscal strategy in Europe, the costs that the war will continue to entail and the demanding electoral calendar on both sides of the Atlantic. Therefore, we are entering a new chapter in which the global economy will have to grapple with a combination of contextual and structural challenges – a situation not unlike that of the past few years.

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