

## International

## Output and Inflation Improves Across the International Economy

June 16, 2017

The outlook for the global economy has slightly improved since early May. Global gross domestic product (GDP) growth edged up in the first quarter, with improvements in both advanced and emerging economies. Excessively low inflation experienced by advanced economies is slowly dissipating, although long-term inflation expectations portray a different view. The overall positive outlook for global growth is somewhat tempered by political uncertainty in some countries, most notably the United Kingdom and Brazil.

## Global Outlook Improves

The Federal Reserve Bank of Dallas' measure of world GDP growth (excluding U.S.) ticked up to 3.1 percent in first quarter 2017 from 2.9 percent in fourth quarter 2016 (*Chart 1*). Though emerging-market economies account for a larger share of global growth, advanced economies have steadily increased their contribution since late 2015. In first quarter 2017, advanced economies accounted for over a third of world output (ex. U.S.) growth, up from 22.9 percent in fourth quarter 2015.

Increased output growth in the euro area is responsible for much of the improvement in the advanced-economies aggregate plotted in *Chart 1*. European GDP growth improved 0.5 percentage points from its low in fourth quarter 2015 to first quarter 2017. This improvement has been broad based among euro-area countries, with the exception of Greece and Spain, where output growth has declined or slowed over the same time period.

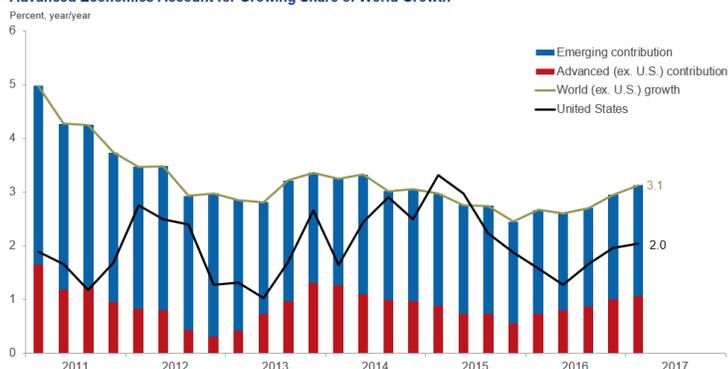
Among other advanced economies, Korean GDP growth rose markedly to 3.0 percent in first quarter 2017 from 2.4 percent in fourth quarter 2016. Growth in Canada, one of the U.S.' major trading partners, ticked up to 2.3 percent from 2.0 percent over the same period.

Changes in the emerging-economies aggregate can mostly be explained by output growth in Brazil and Mexico, both of which are major U.S. trading partners. Brazilian GDP fell 0.4 percent year over year in the first quarter—a considerable improvement from the fourth quarter 2016 decline of 2.4 percent. Mexican GDP growth improved to 2.6 percent from 2.3 percent over the same period.

## Inflation Increases in Advanced and Emerging Economies

World consumer price index (CPI) inflation (excluding

**Chart 1**  
Advanced Economies Account for Growing Share of World Growth



NOTE: Calculations are based on a representative sample of 40 countries and are aggregated using U.S. trade weights.  
SOURCES: Database of Global Economic Indicators; Haver Analytics.

**Chart 2**  
Headline Consumer Price Index Inflation Increases Slightly



NOTE: Calculations are based on a representative sample of 40 countries and are aggregated using U.S. trade weights.  
SOURCES: Database of Global Economic Indicators; Haver Analytics.

U.S.) was 3.6 percent in April 2017. Headline inflation ticked up to 1.6 percent in advanced economies (excluding U.S.) and 5.9 percent in the emerging-markets aggregate (*Chart 2*).

International inflation is felt in the U.S. through import prices. Aggregate import price year-over-year growth was 4.1 percent in April 2017. The increase was driven mostly by the price of imports from Canada, which rose 11.9 percent. More specifically, import prices from the Canadian mining sector grew 47.3 percent, likely a result of currently higher oil prices compared with 2016 lows.

Though inflation has been trending upward in advanced economies, long-term market-based measures of inflation expectations have decreased over the past four months (*Chart 3*). This decline has been accompanied by a drop in long-term yields over the same

period in these advanced economies.

Inflation expectations in the U.K. appear to be higher than in other advanced economies because U.K. inflation-protected securities are indexed to the retail price index (RPI) rather than CPI. RPI inflation tends to be about 33 percent higher than CPI inflation.

**Monetary Policy Rates Shift in Emerging Economies**  
Although monetary policy rates in recent months remained mostly unchanged in advanced economies, they have moved in a few emerging economies (*Chart 4*). On May 18, Mexico's central bank increased its overnight rate by 25 basis points. This was the sixth increase in Mexico's benchmark interest rate over the past year, raising it from 4.25 percent in June 2016 to 6.75 percent currently. The central bank stated that the increase was due to the rising inflation, which has been above the bank's target range since late 2016.

Meanwhile, the Central Bank of Brazil cut its short-term interest rate (SELIC) from 11.25 percent to 10.25 percent on May 31, marking the sixth such cut from the central bank over the past year. Cumulatively, the six cuts have taken the SELIC rate target from 14.25 percent to 10.25 percent. This accommodative monetary policy is aimed at helping Brazil in its recovery from the recent economic crisis. In addition to contracting output growth, Brazil is dealing with political turmoil and uncertainty.

### Britain's General Election Results in Some Uncertainty

No single party won enough parliamentary seats to form a majority government following the June 8 U.K. general election. The Conservative Party, which held the majority prior to this election, now holds a plurality and will seek to form a minority government with the support of the Democratic Unionist Party. With both parties being pro-Brexit, talks with the European Union are expected to continue as scheduled following the State Opening of Parliament (the beginning of the parliament session) on June 19.

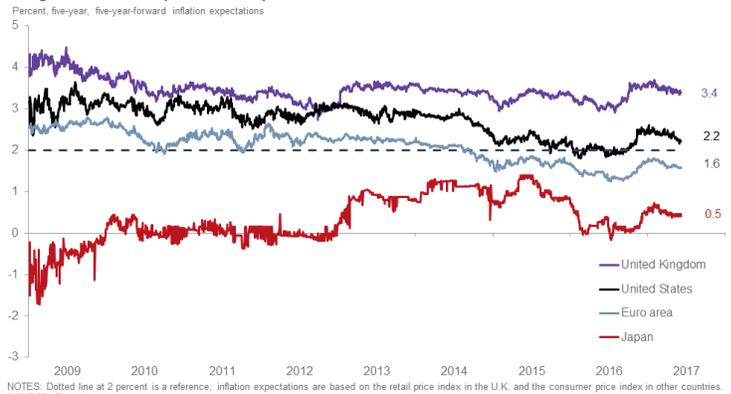
This is only the second time since World War II that the U.K. has failed to form a majority government. Financial markets seem to have responded to the heightened political uncertainty, with the British pound depreciating roughly 1 percent against the U.S. dollar.

—Kelvinder Viridi and Michael Sposi

### About the Authors

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**Chart 3**  
Long-Term Inflation Expectations Drop in Advanced Economies



**Chart 4**  
Monetary Policy Rates Remains Mostly Unchanged

