DALLASFED Economic Update International

Global Outlook Improves

September 28, 2017

Recent data on global gross domestic product (GDP) growth point to a modest and broad-based increase in real economic activity. In the Federal Reserve Bank of Dallas' Database of Global Economic Indicators (DGEI), world GDP growth (excluding the U.S.) was 3.5 percent in the second quarter on a year-over-year basis, up from 3.1 percent in the first quarter.[1]

Global GDP Growth Broad Based

Second quarter 2017 saw positive economic expansion among almost all trade partners. Real GDP grew faster in both advanced economies (excluding the U.S.) and emerging economies, continuing a trend seen since the beginning of 2016 (*Chart 1*). Canada posted the strongest growth among advanced economies, expanding 4.5 percent on an annualized quarter-over-quarter basis. This solid performance can be attributed to a rebound in commodity prices, benefiting Canada's resource sector. The DGEI euro area grew 2.8 percent, with all nine countries showing increased economic activity. Japan's GDP picked up in the second quarter from 1.2 percent to 2.5 percent. This marks Japan's longest growth run in over a decade. The U.K. was the weakest performer at 1.2 percent, an increase from first quarter's 0.85 percent growth.

The strongest performer among the emerging economies in the second quarter was China, with a 6.7 percent annualized quarter-over-quarter increase. This is slightly less than its first-quarter growth of 7.3 percent. Mexico's GDP grew 2.3 percent, showing signs of stabilization. Growth in India slowed from 7.2 percent in the first quarter to 4.2 percent in the second as weakness in manufacturing and mining weighed on activity. Brazil continued to recover from the deepest recession in its history with a 1 percent growth rate. Russia, also emerging from a recession, grew 4.0 percent, up from the previous two quarters. South African GDP expanded 2.5 percent, its first increase since third quarter 2016.

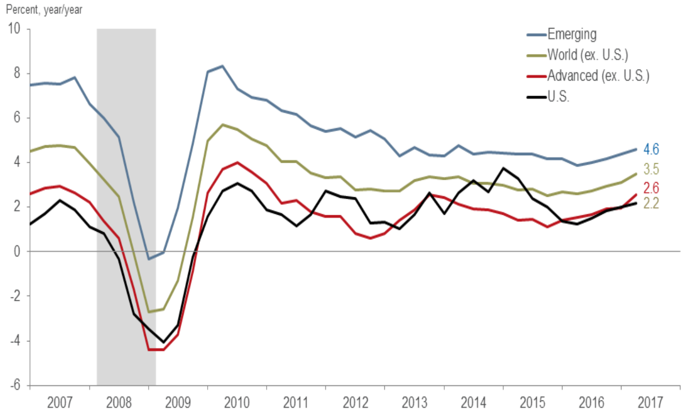
Central Banks Respond to Growth

The Bank of Canada was the only advanced-economy central bank to tighten policy rates since the last week of July, raising the overnight target rate 25 basis points to 1 percent at its Sept. 6 meeting (*Table 1*). The bank cited stronger-than-expected Canadian growth as a reason for the increase and synchronous global economic expansion, leading to higher industrial commodity prices. This hike follows the Bank of Canada's July increase of 25 basis points, the bank's first increase in seven years. The Bank of England maintained its 0.25 percent rate at its Sept. 13 meeting but implied that it will likely raise rates in coming months.

The Central Bank of Brazil reduced the SELIC overnight rate by 1 percentage point in August, followed by an additional 1 percentage-point cut at the September meeting. The central bank cited stabilization of the domestic economy, a favorable global outlook and widespread disinflation as reasons for the cut. The Reserve Bank of India voted to reduce its repo rate by 25 basis points to 6.0 percent, noting that inflation had fallen to a historic low. The Bank of Russia cut its one-week repo rate by 50 basis points to 8.5 percent at its Sept. 15 meeting.

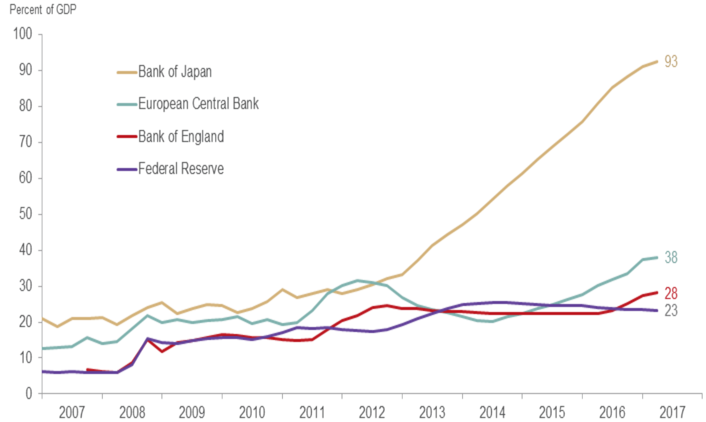
Policy rates in the U.K., Japan and Europe are still up against their effective lower bound. Shadow policy rates, which are estimates of effective policy rates not bounded by zero, further declined in recent months.[2] Shadow rates are at or near historic lows due to long-term asset purchases by central banks.

Chart 1
Real GDP Growth Picks Up in Second Quarter



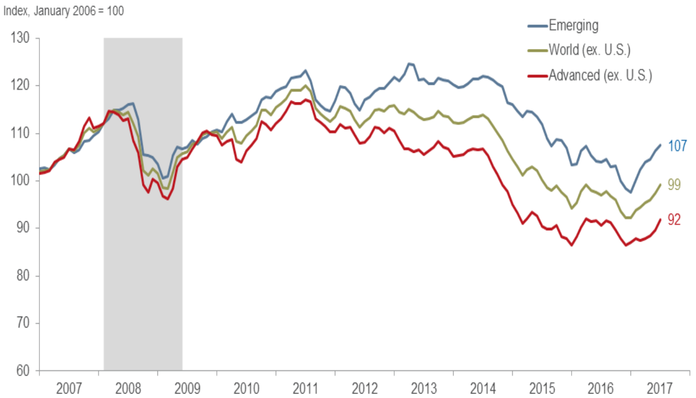
NOTES: Calculations are based on a representative sample of 40 countries and aggregated using U.S. trade weights. The last data point is second quarter 2017. The shaded bar indicates global recession.
SOURCES: Database of Global Economic Indicators; Haver Analytics.

Chart 2
Foreign Central Banks Continue Asset Purchases



NOTE: The last data point is second quarter 2017.
SOURCES: Federal Reserve Board; Bank of England; European Central Bank; Bank of Japan; Haver Analytics.

Chart 3
Global Currencies Appreciate Against the Dollar



NOTES: Calculations are based on a representative sample of 40 countries and aggregated using U.S. trade weights. An increase in the index means depreciation of the U.S. dollar against a basket of foreign currencies, and a decrease means appreciation. Shaded bar indicates global recession. Data were last updated August 2017.
SOURCES: Database of Global Economic Indicators; Federal Reserve Board; Haver Analytics; national sources.

The European Central Bank (ECB), Bank of Japan (BOJ) and Bank of England (BoE) all continued their asset purchase programs, as Chart 2 illustrates. The ECB purchased public- and private-sector securities at a rate of €60 billion per month. BOJ continued to purchase government bonds, bringing the Japanese government's 10-year yield to near zero percent as of Sept. 26. BOJ's balance sheet is approximately 90 percent of Japan's annual nominal GDP.

The Bank of England voted in August 2016 to expand the government bond purchase program by £60 billion, bringing the cap to £435 billion. At the Sept. 13 meeting, the bank decided to maintain this level. As of Sept. 20, the BoE holds £434 billion worth of gilts, bonds issued by the U.K. government. The BoE stopped purchasing corporate bonds in April 2017 but unanimously voted to continue holding the £10 billion stock of corporate bonds in September.

Global Currencies Appreciate Against the Dollar

The DGEI aggregated real exchange rate for the dollar indicates continued appreciation of other currencies against the dollar. The aggregate real exchange rate in advanced countries has grown 6.2 percent and increased 9.2 percent in emerging economies since the start of 2017 (*Chart 3*). As of Sept. 26, the Canadian dollar, euro and pound all have appreciated against the U.S. dollar since July 27.

—Daniel Crowley

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About the Author

Crowley is a research assistant at the Globalization and Monetary Policy Institute at the Federal Reserve Bank of Dallas.

Notes

1. Calculations are based on a representative sample of 40 countries aggregated using U.S. trade weights.

2. For details on methodology, see "Measuring the Macroeconomic Impact of Monetary Policy at the Zero Lower Bound," by Jing Cynthia Wu and Fan Dora Xia, *Journal of Money, Credit and Banking*, vol. 48, no. 2–3, 2016, pp. 253–91. Estimates for the U.K. and euro area are updated by Wu at the Chicago Booth School of Business, and estimates for Japan are updated by Leo Krippner at the Reserve Bank of New Zealand.

Table 1: Policy Rates

	Latest (percent)	Percentage-point change since July FOMC meeting (July 27, 2017)	Percentage-point change since last year (Sept. 6, 2016)
U.S.	1.125	0.00	0.75
World (ex. U.S.)	–	–	–
Advanced (ex. U.S.)	–	–	–
Canada	1.00	0.25	0.50
Euro area	0.00	0.00	0.00
Japan	-0.10	0.00	0.00
United Kingdom	0.25	0.00	0.00
Emerging	–	–	–
China	4.35	0.00	0.00
Mexico	7.00	0.00	2.75
India	6.00	-0.25	-0.50
Brazil	8.25	-2.00	-6.00
Russia	8.50	-0.50	-2.00
South Africa	6.75	0.00	-0.25

NOTES: The last data are from Sept. 26, 2017. Country data are arranged in descending order of trade weight. The advanced-country policy rates are: U.S. fed funds rate, Canada target rate, European Central Bank main refinancing operation rate, Japan complementary deposit facility rate, U.K. official bank rate. The emerging country policy rates are: China one-year lending rate, Mexico target rate, India repo rate, Brazil overnight SELIC target rate, Russia one-week repo auctions loan rate, South Africa average repo rate.

SOURCES: Haver Analytics; national sources.