

Economic Snapshot for the G7 Countries

August 29, 2018

1. Robust domestic demand leads global growth in Q2

Global growth remained strong in the second quarter despite rising trade tensions, [higher oil prices](#) and increased volatility in the financial markets. Tightening labor markets, robust investment in key global economies and still-accommodative financial conditions propelled economic activity in Q2. Moreover, despite signs of having peaked in Q1, global trade remained relatively robust in Q2. A comprehensive GDP growth estimate for the global economy put year-on-year growth at 3.4% in Q2. While the print was a notch below last month's preliminary estimate of a 3.5% rise, it matched the result from the previous period.

Among the world's largest economies, the U.S. continued to show enviable momentum in Q2, with quarter-on-quarter seasonally-adjusted annualized growth posting the strongest reading in nearly four years. Household spending was behind Q2's solid performance due to an ever-tightening labor market and the effects of tax cuts. Non-residential investment continued to be another of the main growth engines on the back of lower corporate taxes. Although, surprisingly, net exports contributed notably to overall growth in Q2, it mostly reflected a surge in exports ahead of retaliatory tariffs from China, which came into effect on 6 July. Front-loaded shipments ahead of trade-punitive measures between China and the U.S. were also seen in parts of Asia.

In this regard, [the U.S.](#) slapped tariffs on USD 16 billion of Chinese imports on 23 August and China retaliated immediately with measures of the same magnitude. As a result, the bilateral trade affected by Chinese and U.S. levies amounts to USD 100 billion. The second round of tariffs came into force one day after both countries met for a two-day meeting in Washington to talk about trade issues. Although the meeting was the first major negotiation between the two countries since June, it ended with no major progress on how to resolve the bilateral trade war. Meanwhile, the U.S. is moving forward with its plans to impose tariffs on an additional USD 200 billion of Chinese imports. On the flip side, on 27 August, U.S. President Donald Trump announced that Mexico and the United States had reached a preliminary deal to revamp parts of the North American Free Trade Agreement (NAFTA), which includes the agreement that any automobile sold in Mexico and the United States will require 75% of the car's value to be manufactured in both countries, up from the current NAFTA level of 62.5%. The key pending questions are whether [Canada](#) will join the agreement and whether Mexican President-elect Andrés Manuel López Obrador, who will assume office on 1 December,

will fully endorse the terms of the accord.

Positive economic news also came from [Japan](#) and [the United Kingdom](#). In Japan, the economy returned to growth in SAAR terms in Q2 following a short-lived contraction in Q1. Strong wage growth, reflecting a tightening labor market and summer bonuses, boosted consumer spending. Moreover, investment expanded a healthy rate partially due to works related to the 2020 Tokyo Olympics. In the United Kingdom, economic activity accelerated in Q2 as warm weather supported consumer spending and likely boosted the construction sector. That said, Brexit uncertainty continues to weigh on the UK's economic outlook.

On the flip side, economic growth in the Euro area remained soft in Q2, expanding at the same rate as in Q1 in quarter-on-quarter terms. Although the release did not include a breakdown by components, higher inflation and subdued wage growth likely dented consumer spending.

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2.Strong H1 dynamics support this year's global outlook; risks loom on the horizon

This year's growth projections for the global economy appear to be firmly anchored. However, it mostly reflects better-than-expected economic dynamics in the first half of the year; looking forward, risks are clearly skewed to the downside. Escalating trade tensions between the United States and other major economies, especially China, represent the main destabilizing factor on the global scene. Moreover, despite being positive for some oil-exporting economies, higher oil prices are fueling inflationary pressures worldwide, threatening to erode consumer's purchasing power.

The ongoing tightening cycle by the U.S. Federal Reserve, coupled with geopolitical risks, will likely exacerbate volatility in the financial markets, in particular among emerging markets. Countries with large external debts or low foreign-exchange reserves could experience severe shocks to their balance of payments.

FocusEconomics Consensus Forecast panelists left their 2018 growth projections for the global economy at 3.4% for the seventh consecutive month. If confirmed, this would represent the strongest expansion in seven years. In 2019, the world economy is expected to expand at a slower rate of 3.2%.

This month's unchanged 2018 growth prospects for the global economy reflects stable outlooks for Canada, [the Eurozone](#), the United Kingdom and the United States. Despite rebounding in Q2, the poor start to the year weighed on [Japan's outlook](#), prompting panelists to downgrade their estimates for the country.

Although robust domestic demand and a solid recovery in India are shoring up economic dynamics in the Asia (ex-Japan) region, rising protectionism and cooling

growth in China are titling risks to the downside. Growth in Eastern Europe is slowly sliding due to increased global financial volatility, which is impacting on some relevant countries such as Turkey, and soft economic dynamics in the region's main trading partner the European Union. Political uncertainty, a less supportive global backdrop and shocks to Argentina and Brazil's recoveries are weighing on [Latin America's outlook](#). The Middle East and North Africa region is slowly benefiting from higher oil prices, while in Sub-Saharan Africa, economic dynamics are jeopardized by perennial security concerns and large macroeconomic imbalances.

3.UNITED STATES | Economy set to post yet another strong performance in Q3

The economy recorded its best showing in almost four years in the second quarter, thanks to strong private spending and a front-loading of business activity—notably export-oriented—ahead of the implementation of reciprocal tariffs with China in early July. Signs further point to robust but slightly decelerating momentum heading into the third quarter. In July, the unemployment rate ticked down, while consumer confidence remained near historic highs and retail sales were solid, boding well for consumption. However, the ISM index eased in July after a burst of activity in June, while industrial production growth only inched up in the same month. Nevertheless, the sharp drop in inventories observed in Q2 is likely to be reversed this quarter, which could provide a sizeable boost to growth.

Economic momentum should remain robust in coming quarters—notably thanks to a sharp increase in government spending— but is expected to moderate somewhat. The rapidly deteriorating trade outlook is the main immediate downside risk. Trade-related uncertainty will likely keep weighing on business confidence and investment, while an escalation of tariff actions could strike a blow to consumer spending. Recent progress on negotiations with Mexico over NAFTA, and the resumption of talks with China could however signal an appeasement of tensions in coming months. [FocusEconomics panelists see GDP expanding 2.8% in 2018](#), unchanged from last month's estimate. In 2019, growth is seen moderating to 2.4%.

4.EURO AREA | Economic dynamics remain subdued in Q2

The Eurozone economy's soft start to the year carried over into the second quarter, with preliminary data revealing growth was unchanged at 0.4% quarter-on-quarter. The result confirmed that the economy has shifted into a lower gear after a stellar growth spell in 2017. Although a breakdown by components is not yet available, rising inflation likely took a bite out of household spending, while lower sentiment due to political and trade concerns also likely weighed on momentum. Available data for the third quarter

has also been downbeat, with economic sentiment slipping in July and the composite PMI remaining broadly unchanged in August. On the political front, the European Union and the United States reached a temporary truce in their trade spat on 27 July, pledging to work together to reduce trade barriers and to refrain from issuing any new tariffs while negotiations are ongoing. However, it is uncertain if the truce will hold, as U.S. President Donald Trump threatened again to slap tariffs on EU car manufacturers on 21 August.

Growth is expected to decelerate this year as a firm euro and geopolitical tensions dent exports, while rising inflation weighs on household spending. That said, an improving labor market and accommodative monetary policy will keep activity healthy overall. [FocusEconomics panelists project GDP to expand 2.2%](#), unchanged from last month's forecast. In 2019, the economy is seen expanding 1.8%.

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5.JAPAN | Domestic demand propels economic activity in Q2

The economy recovered vigorously in the second quarter following the contraction in the previous quarter. Private consumption benefited from summer bonuses and a tight labor market, which propelled wage growth, especially in May and June. Investment also posted significant gains in Q2, reflecting works related to the 2020 Tokyo Olympics and businesses trying to automatize processes in a context of labor shortages. On the flip side, the external sector weakened in Q2 amid growing global trade tensions. Early data for Q3 suggests solid domestic economic dynamics are supporting overall growth. In the political arena, Japan's ruling Liberal Democratic Party (LDP) will elect its new leader on 20 September. If incumbent Prime Minister Shinzo Abe wins the vote, it will pave the way for him to become Japan's longest-serving leader.

Accommodative financial conditions, a robust labor market and construction projects related to the 2020 Tokyo Olympics will bolster growth in the coming quarters.

However, risks are looming on the horizon: Rising trade protectionism could hurt Japan's all-important external sector, while mounting geopolitical risks could strengthen the yen. [FocusEconomics panelists see the economy growing 1.0% in 2018](#), which is down 0.1 percentage points from last month's forecast, and 1.0% again in 2019.

6.UNITED KINGDOM | All-important services sector continues to shore up growth in Q2

Growth accelerated somewhat in the second quarter thanks to an improved performance from the services sector and a rebound in construction. Consumer-facing service industries performed particularly well, although this was at least partly due to the prolonged period of warm weather. However, manufacturing contracted, suggesting

the short-term boost to competitiveness from the weaker pound is ebbing. Moreover, signs from the labor market were mixed; although the unemployment rate dipped to a multi-decade low, earnings growth still failed to gain traction. The economy has begun Q3 in muted fashion, suggesting a further uptick in GDP growth is unlikely. In July, both the services and manufacturing PMIs declined on slower output and new orders growth, while consumer sentiment soured.

Looking ahead, growth will be anemic, with fixed investment depressed by Brexit uncertainty and export growth slowing after the temporary boost provided last year by the weaker pound. However, a slight pick-up in government spending should provide some support. A failure to reach a Brexit agreement with the EU before the UK departs in March 2019 is a substantial downside risk. Our panelists estimate [GDP growth of 1.3% in 2018](#), unchanged from last month's forecast, and 1.4% in 2019.

7.INFLATION | Global inflation climbs in July on higher energy prices

The upward trend in global inflation remained intact in July, with both developing and emerging economies posting higher rates compared to June. According to an estimate produced by FocusEconomics, global inflation inched up from 3.0% in June to 3.1% in July, the highest reading since November 2017. The increase mostly reflected higher prices for key commodities, especially for oil. In the United States, reduced economic slack and fiscal stimulus are also putting upward pressure on inflation, while a selloff in emerging markets has led some currencies to depreciate, exerting exchange-rate pass-through effects.

In response to higher inflation, increased volatility in the financial markets and the U.S. Federal Reserve's ongoing monetary tightening, most central banks—particularly in developing economies—are tightening their monetary policies. Among developed countries, at its 31 July–1 August monetary policy meeting, the Fed decided to hold rates steady but signaled that two more rate hikes are in the pipeline for this year. At its meeting ending on 1 August, the Bank of England decided to hike its Bank Rate due to a tightening labor market and above-target inflation. In Japan, although the Central Bank kept its ultra-loose monetary policy program at its 30–31 July meeting, the BoJ announced that it will allow greater flexibility around its target of 0% for the yield on the 10-year bond.

Inflation will hover at current levels mainly due to high commodity prices, particularly for energy and to a lesser extent food. Reduced economic slack in some economies and sharp currency depreciations in others will also support prices further down the road. The FocusEconomics panel sees global inflation at 2.9% for 2018, which is unchanged from last month's estimate. Next year, the panel projects that inflation will inch down

to 2.7%. If the hyperinflation episode in Venezuela is factored in, global inflation will reach 473% in 2018 and 555% in 2019.

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Upcoming Events

Major Economies Economic News

- [**Japan: Industrial production declines for third consecutive month in July**](#)

August 31, 2018

Industrial production contracted 0.1% on a month-on-month and seasonally-adjusted basis in July, following June's 1.8% decrease.

[Read more](#)

- [**France: Inflation remains steady in August**](#)

August 31, 2018

According to preliminary data published by the Statistical Institute (INSEE) on 31 August, consumer prices rose 0.5% from the previous month, contrasting the 0.1% contraction observed in July.

[Read more](#)

- [**Japan: Consumer confidence falls to a one-year low in July**](#)

August 30, 2018

Consumer sentiment decreased from 43.7 in June to 43.3 in July.

[Read more](#)

- [**United States: Second GDP release confirms buoyant economic activity in Q2**](#)

August 29, 2018

A second GDP estimate confirmed the economy grew at the fastest pace in almost four years in the second quarter, buttressed by robust private outlays and a strong showing from the external sector, which benefited from the front-loading of export activity ahead of the implementation of reciprocal tariffs between China and the U.S. at the beginning of Q3.

[Read more](#)

- [**Germany: Slight drop in consumer confidence expected in September**](#)

August 29, 2018

The forward-looking consumer confidence indicator for September released by the GfK Group decreased slightly to 10.5 points, down from August's 10.6 points.