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Global economic growth

The global economic recovery is for real

Advanced economies are settling into reasonable growth as emerging markets rebound

FT Data

YESTERDAY by: Guest post by **Eswar Prasad** and Karim Foda

It looks like the global economic recovery is for real. The latest update to the Brookings-FT Tiger (Tracking Indexes for the Global Economic Recovery) shows that, after numerous fits and false starts, the recovery has become broad-based and stable — if not vigorous.

The advanced economies are settling into a reasonable growth path, and the spectre of deflation has been staved off. Fast-growing emerging market economies such as China and India have emerged from a rocky period and even the more vulnerable emerging markets have turned the corner.

But the calm on the surface is belied by swirling undercurrents of political and policy uncertainty. Brexit, Donald Trump's US election victory and rising populist and nationalist tendencies in many western democracies pose significant risks to stable policymaking. The Trump administration's protectionist inclinations have injected a large dose of uncertainty into global trade. Heightened political tensions in the Middle East and in the Korean peninsula, which remain volatile powder kegs, also have the potential to destabilise both the regional and world economies.

It looks like the global economic recovery is for real

Brookings-FT Tiger composite index



Source: The Brookings Institution

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The US economy continues to enjoy a steady if unspectacular expansion, with decent GDP growth, strong retail sales and industrial production, as well as robust consumer and business confidence. US financial markets appear to have been buoyed by the prospects of weaker business regulation, tax cuts, and a fiscal boost. The debate about whether or not to tighten monetary conditions appears to have given way to a debate about how quickly the Federal Reserve should do so.

Despite all these positive developments, the underlying growth dynamics remain weak, as reflected in lacklustre growth in investment, productivity, and real wages.

Expansion gathers pace in the US

Brookings-FT Tiger composite index, US



Source: The Brookings Institution

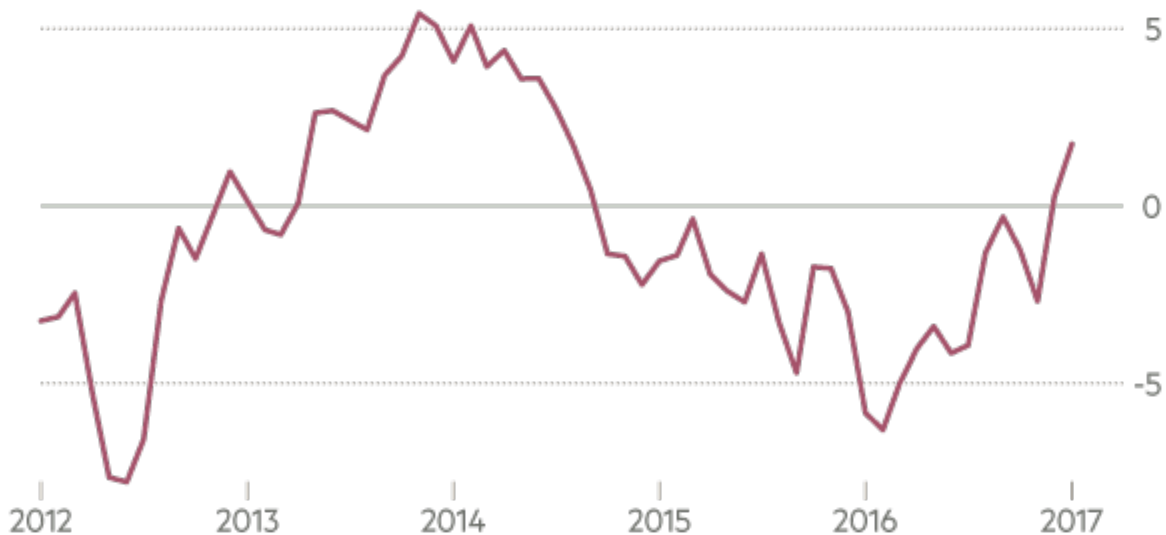
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Even the eurozone, long the laggard in terms of the recovery among advanced economies, looks set for a year of reasonable growth across the board. Deflationary pressures have eased and employment growth has picked up. Many of the underlying stresses, including banking sector weaknesses, have not been eliminated but appear to be in abeyance.

However, political uncertainties, particularly those related to election outcomes in France and Germany, continue to cloud the policy environment.

Political uncertainty in the Eurozone is holding back German recovery

Brookings-FT Tiger composite index, Germany



Source: The Brookings Institution

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The recovery in Japan appears to be on firmer footing than a year ago. Despite a recent strengthening of the yen, deflationary pressures have eased and a broad array of indicators such as GDP, employment, exports and retail sales show signs of strength. The UK economy continues to do better than expected after the Brexit vote shock. However, the reality of the exit, with Article 50 now triggered and the looming tough negotiations with the EU, portend a period of heightened uncertainty that could hurt business and consumer confidence, damping domestic demand.

UK bounces back from Brexit vote shock, growth prospects remain cloudy

Brookings-FT Tiger composite index, UK



Emerging market economies have survived fears of capital outflows and other volatility emanating from tightening monetary conditions in the US and continued monetary policy divergence among the Fed, Bank of Japan, and European Central Bank.

China seems to be locked into steady growth around its target of around 6.5 per cent. With a high-level leadership transition coming up at the end of this year, stability has become the watchword. The government is likely to maintain a tight grip on the economy and financial markets, keep a lid on capital outflows, and avoid any major reforms. Consequently, economic tensions and vulnerabilities could continue to build up, especially in the financial system, although they are unlikely to surface this year.

India remains the fastest-growing major economy in the world. Industrial output has picked up but credit growth remains weak and could constrain manufacturing growth. A big victory in a recent important state election has provided political

validation for Prime Minister Narendra Modi's demonetisation initiative, and gives him additional political capital for deep-rooted structural reforms, which remain key to unlocking India's long-term growth potential.

Indian economy surges ahead, hopes for reforms rise

Brookings-FT Tiger composite index, India



Growth in Brazil and Russia remains negative, although the two economies may be able to avoid further contractions in GDP this year if commodity prices, industrial production, and private sector sentiment hold up. Political turmoil continues to wrack many emerging market economies such as Brazil, Turkey, and Venezuela, all of which remain vulnerable to both domestic and external shocks.

This year is shaping up as one where the apparent economic calm on the surface is offset by rising economic stresses and political tensions that could bubble up and undercut the recovery in 2018 or beyond. Low investment and weak productivity growth make the recovery's durability questionable while political ferment, protectionist policies, and lack of progress on the reform agenda in most countries could hurt both the quality and sustainability of growth. 2017 is not a year to worry

about in itself but a good time to worry about what the future holds.

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