- The data, in particular the sharp retrenchment in global capital and trade flows, shows that the world is facing a growing **risk of "economic derailment".** In contrast to the recent rally in the financial markets, global growth continues to lose momentum, with weak pricing pressures signalling poor world demand. This is prompting warnings from some analysts of a **world of triple zeros**: zero inflation (in high-income countries), zero productivity growth and zero per-capita GDP growth.
- Official GDP figures paint a bleak outlook, but it is almost certain that **the digital economy makes countries richer and faster growing than acknowledged by the official statistics**. In the UK, a government commissioned report estimates that, if the hidden benefits of digital services were fully taken into account, the average annual growth rate of the past ten years would have registered 0.4 – 0.7 percentage points higher.
- **Not only is GDP growth slightly higher than we think, but also we can happily live with less of it** (at least in the rich world). The reasons are twofold: (1) technology is driving down the cost of most goods and services (with the notable exception of health and education); (2) many positive developments that improve living standards (such as energy efficiency, electric vehicles, solar energy, biking rather than driving and so on) subtract from GDP growth by ultimately reducing costs. As shown by the example of Japan stagnating over the past 20 years, **GDP growth does not necessarily equate to prosperity, and prosperity does not always equate to wellbeing.**
- But in the meantime, **the productivity slowdown is all too real**. In probably the most innovative economy in the world (the US), labour productivity growth has averaged only 1.3% per year over the past ten years, half the rate of the preceding decade. While it is hard to ascertain the direction of the causal relationship, there is little doubt that this accounts for the stagnation in **real wages in high-income countries** and the prolonged deficiency in global aggregate demand.
- The Fed's decision to remove two rate hikes from its 2016 and 2017 forecast is the latest sign that **the rich world is engulfed in deflationary forces**. It tells us that the Fed doesn't see the recent uptick in US inflation as a lasting and significant move. More generally, there is no point worrying about inflation until a significant increase in real wages takes place.
- China just decided to inject more liquidity into the banking system by cutting the reserve ratio by 0.5 percentage points. This won't revive economic growth because **the country's debt overhang is clogging up the arteries of monetary transmission**. China has no other choice than (1) to deleverage, (2) to clean the balance sheets of its local governments and state-owned enterprises and (3) to engage in a massive programme of structural reforms.
- It's not because the debt problem in emerging markets hasn't yet fully developed that it won't. In China, like in most other EMs, **the weaknesses that stem from the debt boom** (in terms of quality of assets, non-performing loans caused by hard-currency debt, etc.) **will be uncovered in the early days of the post-QE workout**. This is like a slow-moving train.
- For investors, further weakness in EM does not spell disaster across all sectors, quite the opposite! The example of China is telling. As consumer spending evolves, shifting from products to services, health, wellbeing, and experiences in general take precedence. Travel & tourism offer a spectacular manifestation of this trend: **last year, despite the sharp deceleration of growth, tourism spending increased by 53%**! Similar double-digit growth figures can be found in other sectors such as personal care and services (spa & massage), organic food and so on.
- Leaving aside the immensely complex problems with which the intelligence agencies and security forces have to contend, the recent terrorist attacks in Brussels have two main implications: (1) **they make the political environment more toxic** by favouring anti-immigration sentiments and populism; and by flaming anti-EU feelings in the UK; (2) **they make it increasingly difficult to conserve "European" values** (openness, tolerance, freedom of speech and movement, etc.). But, as we argued last month, the punditry has it wrong: this will ultimately lead to further EU integration, not disintegration.
- Finland looks likely to embark on a radical experiment. By the end of the year, it may institute a universal basic income (UBI), granting every adult citizen a monthly allowance of €800. This old idea, whose time has come and which could be replicated elsewhere, would deliver several benefits: (1) **It would reinforce social cohesion** (all main Finnish parties are in favour) and reset the terms of the social contract; (2) **It would shrink the welfare state** and its bureaucracy; (3) **It would benefit growth** through higher employment by allowing citizens to take on low-paying jobs without incurring lower social benefits.
- The forthcoming bankruptcy of Peabody Energy (the world's largest private coal company) epitomizes the **risk that climate change poses to carbon-emitting companies**. They are now victims of a double-whammy: (1) less expensive and better performing sources of clean energy, (2) tougher and evermore unpredictable regulations. Banks like JP Morgan, Morgan Stanley, Citigroup, etc. have declared they will no longer finance coal-fired power plants in the rich world. The trend is incontrovertible and irreversible.
- If there was only one thing to be learnt from this month's victory of AlphaGo (a computer) over the go world champion, it is this: **over the coming years, AI (Artificial Intelligence) will progress at a much faster pace than most of us imagine**. We are not yet at the stage where the human brain can be reverse-engineered, but "deep-learning" - the ability of algorithms to make sense of what matters in large pools of information and to discern patterns - will soon revolutionize professions as different as radiology, criminology, financial services… and many more!
- In the coming weeks, "must-watch" issues include: (1) China, that remains at the epicentre of global economic and financial stress; (2) continued pressure on overleveraged EM; (3) whether the $ will continue to depreciate against EM currencies (2% so far this year), bringing much relief to their economies, (5) the extent to which the commodity price shock will affect banks (with a commodity-driven financial crisis all too possible in EM), (6) the vast array of global geopolitical and societal risks. **For real-time or in-depth analysis on any of these, and if you are interested in prediction markets to better forecast some of the risks, please contact us.**