RESEARCH

PROPONOMICS

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GLOBAL GROWTH – CENTRAL BANKS RESPOND

The global economy has slowed in recent quarters, but a change of stance by major central banks could result in stronger growth by the summer.

Headlines

Recent GDP figures point to a global slowdown in late 2018, with subdued conditions continuing into Q1 2019.

Central banks have now revised their guidance accordingly, and most are committed to supporting growth.

We see new momentum emerging by the summer, and property investors and occupiers will prepare for future deals.

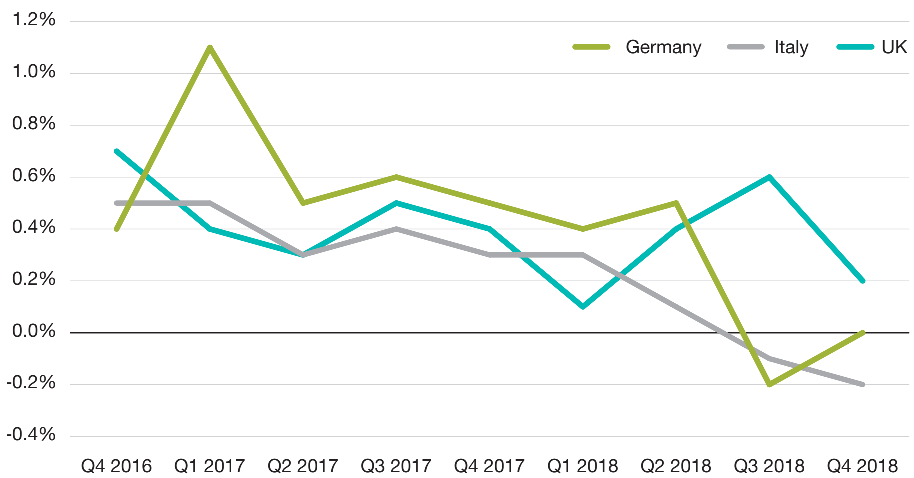
We are presently in the midst of a moderate global economic slowdown, as demonstrated by sluggish GDP figures for the UK, Germany and China for Q4 2018. The US statistics when released are expected to follow suit. Business surveys show that trading conditions remained subdued in January, especially for manufacturing firms. The global economy is certainly not tanking nor likely to do so, but the temperature has cooled.

The reasons why

Why are we seeing a slowdown? There are four key reasons –

1. Cyclical – Following the big oil price correction in late 2014, the advanced economies moved into a sweet spot of low inflation, cheap energy and easy monetary policy. Yet, by summer 2018 investors had become nervous over the long bull market for equities, reasoning that no cycle lasts forever. The notion of a ten year cycle for the economy, while debatable, is believed by some and 2018 marked a decade from the onset of the 2008/2009 recession. Slower profits growth for US corporations in Q3 2018 encouraged the view that late cycle had arrived, and investors retreated from risk.
2. Central bank guidance – 2018 was a year that began with more central banks joining the US Fed in guiding markets that they would hike rates and end Quantitative Easing (QE). However, by the autumn concerns were growing that policymakers were moving in the wrong direction, as more recent data pointed to a loss of momentum. Also, in China in 2018, action was taken to reduce lending by the shadow banking sector, which in turn slowed growth. Consequently, early 2019 has seen most central banks revise their guidance, talking down the chances of near-term rate hikes.
3. Technology upgrades – This is best illustrated by the motor industry which is experiencing seismic change. Around the world carmakers are pivoting from combustion to electric engines, which involves a mix of

FIGURE 1
GDP growth – quarter on quarter



Source: OECD

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"Policymakers are now responding to the slowdown, with leading central banks, including the Fed and the Bank of England, now talking down the likelihood of rate hikes"

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For the latest news, views and analysis on the world of property, visit Knight Frank's blog www.knightfrank.co.uk/blog new investment and shuttering old operations. Moreover, there is the problem of how much firms should invest in the models they will sell over the next few years, given the long-term trajectory is driverless.

4. Geopolitical risks – By threatening supply chains and complicating business planning, economic nationalism is adding to the global slowdown, from the risk of a no deal Brexit to the US/China trade war.

What next?

Policymakers are now responding to the slowdown, with leading central banks, including the Fed and the Bank of England, now talking down the likelihood of rate hikes. The minutes of the Fed's most recent meeting suggested that the US central bank may soon halt the unwinding of its QE purchases. Moreover, net investment by US businesses leapt in the first nine months of 2018, the impact of which should be felt in 2019. ECB officials have signalled that they could even restart QE if data continues to deteriorate.

In China, a broad-based strategy is being pursed to boost growth. The People's Bank of China has been reducing the levels of reserves banks are required to hold, in order to boost lending. Also, the government has announced tax incentives for businesses that recruit and invest. Moreover, concerns over growth appear to be encouraging pragmatism in the trade talks between China and the US.

On the technology issues raised above, recent months have seen a confluence point of disinvestment and relocations. However, over the medium to long-term introducing new technology will create growth that outweighs the losses from the preceding layoffs and shutdowns. Carmakers are expanding into artificial intelligence and electrification, which involves a huge outlay of investment.

A sudden rebound for growth is unlikely, as the above measures will take time to filter through to the economy. However, we believe that Q1 2019 probably marks the low point of this slowdown, as steps have been taken to deliver stronger growth by the summer. So what will this mean for the property market?

Slide rule time

In the coming months, both investors and occupiers are likely to reach for their slide rules to start running the numbers on potential deals, to be ready to pre-empt a market upturn. A change in outlook could be rapid for markets like the UK, where the currency is already rising. This suggests there will be a narrow window of opportunity to buy against limited competition once evidence emerges that a turning a point has been reached. The current slowdown has also highlighted the fact that Germany is not the only place in continental Europe that offers steady long-term growth. This can also be found in the Netherlands and the Nordics.

In occupier markets, the limited nature of the slowdown means that vacancy rates have continued to fall, so those with a search are encountering a sparse range of options. The London office market is already seeing a pick-up in viewings, which could result in a fresh wave of rental growth once more firms start looking for expansion space.

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