Possibility of Global Recession

What is the issue?

- The global economy continues to be hit as one big economy after another falters on economic growth.
- This increases the likelihood of a global recession in the coming future.

What is a global recession?

- In an economy, a recession happens when output declines for two successive quarters i.e. 6 months.
- However, for a global recession, institutions such as the International Monetary Fund look at more than just a weakness in the economic growth rate.
- They look at a widespread impact in terms of employment or demand for oil, etc.
- The long-term global growth average is 3.5%. The recession threshold is 2.5%.

What is the current growth scenario globally?

- Recently, data from Germany, the world's fourth-biggest economy, showed that its GDP contracted by 0.1% in the April-June quarter (Q2).
- Ongoing trade tensions between the US and China, and the uncertainty due to Brexit have impacted German exports badly.
- Germany is the world's third-biggest trader after the US and China.
- The two biggest economies (US and China) are already in some trouble.
- The US has grown by just 2.1% in Q2 of 2019 as against 3.2% in Q1.
- China's growth has been decelerating for longer.
- Moreover, the unemployment rate in Chinese cities is now at the highest recorded level.
- Also, other key metrics such as factory production (which is the lowest since the 2008 financial crisis) have worsened.
- The Japanese economy, surprisingly, was growing at an annualised rate of 1.8% in Q2, but it, too, is fighting to ward off a recession.

What is the impact on the US?

- The Trump administration decided to defer imposing a new set of tariffs on

Chinese imports.
- But even this could not hold back the US bond (Treasury) yields from falling, as investor sentiment was so bad.
- The 30-year bond yield fell to its historic low.
- In simple terms, investors are looking for safe options, and since US bonds are one of the safest bets, more of those are being bought.
- This has led to a spike in their prices, and a fall in their yields.
- An inversion in bond yields such as this points to the likelihood of a recession in the near future.

What is the need for caution?

- Recently, researchers at Morgan Stanley, a leading investment bank, made a warning in this regard.
- Accordingly, if the US and China continue to raise tariff and non-tariff barriers over the next 4 to 6 months, the global economic growth rate will fall to a 7-year low of 2.8%.
- More worryingly, the world economy could enter a recession within the next 3 quarters i.e. 9 months.
- The last massive downward spiral in the global economy happened in the wake of the great financial crisis of 2008, and continued until 2010.

What could be an immediate trigger?

- Recently, the US declared China a “currency manipulator”.
- In other words, U.S. accused China of deliberately weakening the yuan to make Chinese exports to the US more attractive and undercut the effect of increased US tariffs.
- The intensifying trade war between the two has the potential to derail the already weak global growth, and the signs are evident.
- E.g., the global manufacturing Purchasing Managers’ Index and new orders sub-index have contracted for the second consecutive month in July; they are already at a 7-year low.
- Further, the global capital expenditure cycle has weakened.
- Since the start of 2018, there has been a sharp fall-off in nominal capital goods imports growth.
- In other words, there is a decline in capital investment in anticipation of reduced demand.

How can this lead to a global recession?

- The absolute volume of global trade has stagnated and, in terms of percentage change, trade is contracting.

- More worse is the composition of trade that is being hit and is likely to be hit further.
- According to Morgan Stanley, two-thirds of the goods being lined up for increased tariffs are consumer goods.
- Higher tariffs are not only likely to reduce demand but, crucially, hit business confidence.
- The apprehension now is that the global trade uncertainties could start a negative cycle.
- Here, businesses do not feel confident enough to invest more, given the lower demand for consumer goods.
- Reduced capital investment would reflect in fewer jobs, which, in turn, will show up in reduced wages and, eventually, lower aggregate demand in the world.
- Making things worse, the monetary policy is already loose i.e. borrowing money is cheap.
- So, a recession now will be more difficult to deal with.

What is the case with India?

- India's trade is already suffering, and jobs are being lost.
- Indian economy is struggling to find a domestic growth push as government and businesses are overextended, and household consumption is down.
- So, it is highly important that exports are given a boost.
- Domestic bottlenecks are more responsible for India's lack of competitiveness in exports than the lack of global demand and the overvalued rupee put together.
- So addressing bottlenecks such as better roads, more electricity, easier rules of doing business etc., is essential.

Source: Indian Express