Russell Investments

What three ingredients are contributing to the current strong global economy?

The need for Goldilocks conditions-

Before she revealed the recipe for the current global market strength, Ng first analyzed our current late-cycle market. She said, "When you're ten years into an economic expansion, like we are, you need Goldilocks conditions to be able to extend the expansion. So, for example, if growth gets too hot, then the Fed (the U.S. Federal Reserve) fears overheating. This could result in restrictive monetary policy, which could lead to a recession. On the other hand, if growth gets too cold, then, yes, the Fed would be accommodative."

Ng explained that growth slowdown could start a *negative-confidence spiral*, meaning that if consumers and businesses become pessimistic, then spending and hiring would likely slow, and this too could raise recession probabilities. Ng defined *just-right Goldilocks conditions* this way: "We just need the economy to hum at positive-but-mediocre, have growth be strong enough to support spending and hiring, but soft enough to keep the Fed accommodative." Ng said that right now, it looks like growth conditions could be *just right*.

Ng also mentioned seeing some *green shoots* in the global economic data, specifically in China. "Particularly for this month, industrial production accelerated sharply for March, such that the year-on-year growth rate is the highest in almost five years. And it was much higher than consensus expectations. Fixed-asset investment and also retail sales also accelerated." Ng called this "very positive news," and not just for the Chinese domestic economy. She explained: "Many companies' earnings are dependent on foreign demand and you're exactly right in saying that China's economy is one of the largest in the world, so Chinese demand has an impact on many companies' earnings."

April Flash PMI numbers: How spicy were they?

The conversation shifted to April Flash Purchasing Managers' Index numbers. When asked how spicy the numbers were compared to March numbers, Ng said, "The April update is less spicy." She explained how, on March 22, 2019, low German manufacturing numbers created a growth scare that made the U.S. Ten-Year Treasury/Three-Month Treasury yield curve briefly invert for a week. "For this April PMI report," said Ng, "It was a bit lackluster, but it was nowhere near as spicy as that previous report." She added that the bond market did not overreact.

Finally: The three ingredients

While the overall PMI report was a bit downbeat, Ng said, "We're not too concerned, because we have three ingredients in place: **One, Chinese growth seems to be stabilizing because of government stimulus. Two, central banks globally have shifted to a more dovish policy. And three, trade negotiations seem to be wrapping up and that will remove a source of friction and uncertainty.** Going forward, we still expect growth to stabilize to at-trend to maybe a little bit above trend levels."

April 19, 2019 | by Dr. Kara Ng
AIS Business Solutions Sophie Antal Gilbert was joined by Quantitative Investment Strategist, Dr. Kara Ng,