

Global Economic Outlook

2017

2016 has been an eventful year and one that many people will remember as being filled with considerable change and uncertainty. Throughout the last twelve months we have seen the UK vote to leave the European Union, the election of Donald Trump as President of the United States in an unprecedented victory, Europe facing a growing migrant crisis and oil prices hitting a multi-year low, all the while global growth proved to be resilient, but well below pre-crisis levels. 2017 is likely to be just as interesting as the global economy navigates its way through a new set of dynamics.

Brighter prospects for the US. Although the rate of employment growth could slow over the next 12 months as firms get closer to full labour capacity, improvements in the labour market and positive wage growth to date, combined with low interest rates should support the consumer economy in the year ahead. There remains some uncertainty as to whether the new US president Donald Trump will be able to deliver on all of his fiscal promises, but on the assumption that a moderate fiscal stimulus package is implemented this should provide the impetus for private corporates to increase investment giving a healthy boost to economic growth.

A gloomy outlook for the EU. The outlook is less optimistic for Europe, as upcoming elections across a number of western European countries, combined with the spill-over effects of Brexit and the potential threat of a banking crisis weigh on growth prospects. Given these circumstances, monetary policy is likely to remain loose and the economic outlook polarised in 2017, with stronger growth projected for Spain, the Nordics, Ireland and central European countries.

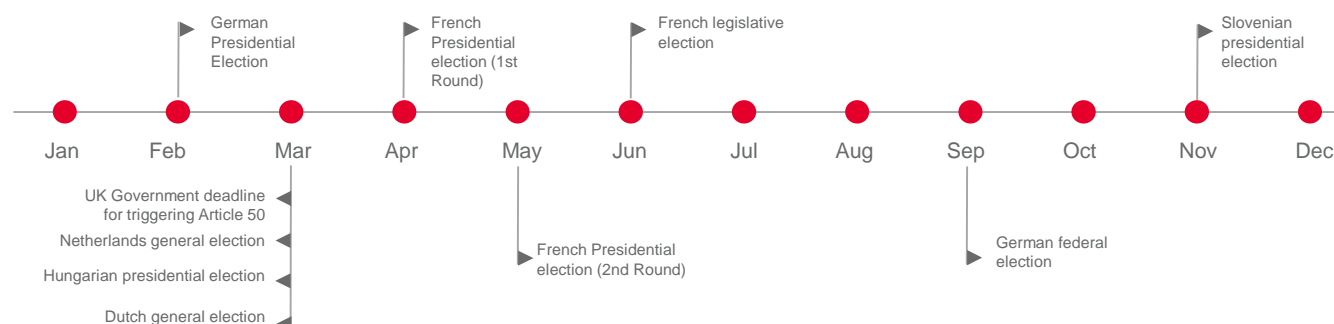
Stimulus measures to drive growth in the near term in Japan. The Bank of Japan introduced two new policy frameworks in 2016 to boost growth, this included Quantitative and Qualitative Monetary Easing (QQE) and Yield Curve Control. The aim of the former is to expand the monetary base until CPI inflation reaches 2%yoy, while the latter should give the bank greater control over short and long term interest rates. The measures are expected to support economic

growth in 2017 and help counteract the country's supply-side constraints (adverse population dynamics and labour market rigidities).

An optimistic growth outlook for the Emerging Markets. A reduction in excess supply should lift commodity prices in 2017, encouraging growth in some emerging countries. While fairer valued currencies and improvements in current account balance sheets should reduce the risks from a tightening in US monetary policy. We anticipate looser monetary policy conditions in 2017 particularly for those markets that have experienced weaker growth in recent years, which should support the short term outlook. Growth rates are unlikely to be spectacular, and below pre-crisis levels, given economic reforms to re-balance China's economy from investment-led to domestic driven growth, and former requirements to reduce high levels of private sector debt and burgeoning fiscal deficits across the emerging economies.

Still, China should contribute positively to global growth in 2017. With China and broader Asian economies making up c.40% of global GDP growth, developments in these markets will significantly influence future global growth prospects. China should deliver reasonably high rates of GDP growth in 2017 as its pre-existing fiscal framework (to stimulate growth through infrastructure spend, reduced interest rates and relaxed credit lending conditions) continue to support short term growth prospects.

Upcoming European Elections 2017





Slower growth ahead for the UK. The general public made the bold decision to leave the European Union during 2016. Despite the gloomy projections made by independent experts and economists the UK economy held up better than the doomsters had predicted, helped by a sharp fall in sterling and the resilience in consumer spend and service sector growth.

However, Brexit negotiations have yet to begin, and the terms of the UK's exit from the EU will take time to be agreed; the elections across the rest of Europe are likely to stall matters while Trump's future stance towards US trade policy could cause further complications. In the interim, we expect the post-referendum optimism will fade as the repercussions of the vote start to feed through to the domestic economy. Moreover, the Prime Minister's confirmation that the UK will leave the EU single market (and the challenges this may cause) could result in the economy encountering a more persistent period of shallow growth.

Sterling's devaluation will be the key mechanism that changes the composition of economic growth from its reliance on the consumer economy towards trade and exports. Household consumption and business investment are both expected to slow in 2017. Headline inflation is forecast to rise above its 2% target by late 2017 as the effects of the weaker pound feeds through to higher CPI inflation, squeezing the real spending power of consumers and reducing the contributions to GDP from household spend.

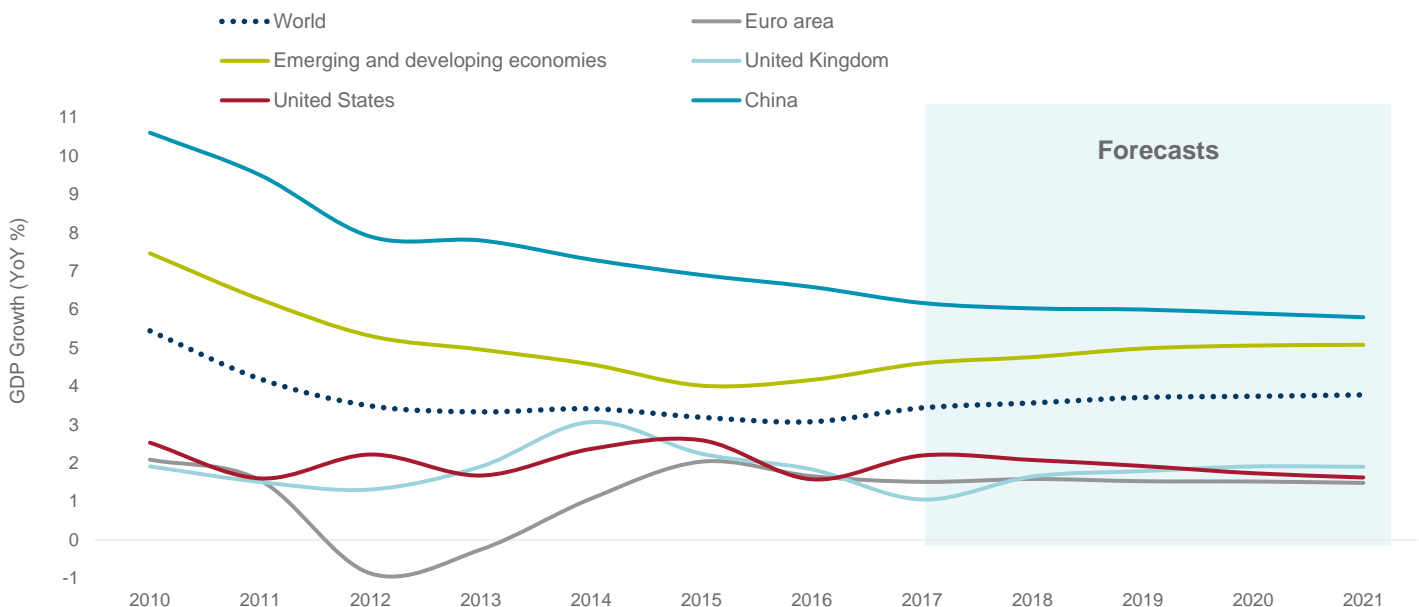
The weaker pound should provide some support to domestic exporters (given the relative price of UK's exports on an international basis), but even so, these gains could quickly diminish as the increased cost of imported components used in the production process raise exporter's cost margins.

Meanwhile, increased market uncertainty could cause businesses to err on the side of caution in the short term, as firms defer major investment plans and make cut backs to recruitment to restrain costs and protect profits. This in turn will lower employment and wage growth prospects.

Government intervention should help to cushion the economy from the challenges of Brexit over the medium term. According to the announcements from the Autumn Statement, government borrowing will increase over the next five years. Additional funding will be targeted towards the development of new infrastructure (such as roads, transport networks and housing).

Theoretically, rising inflation and a potential re-orientation towards fiscal policy to stimulate growth should increase the probability of near term interest rate hikes, but with expectations of a moderate growth outlook ahead and limited upward pressures on core inflation, we believe it is more likely that policymakers will retain a neutral stance to monetary policy in the short term.

Annual GDP Growth, Source: IMF



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