



World Economic and Financial Outlook

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CVIII Meeting of Central Bank Governors - CEMLA

* The opinions contained in this presentation are the sole responsibility of the author and do not represent the Banco de la República or its Board of Directors.

Risks and vulnerabilities

Trade tensions and
uncertainty



Lower global
growth

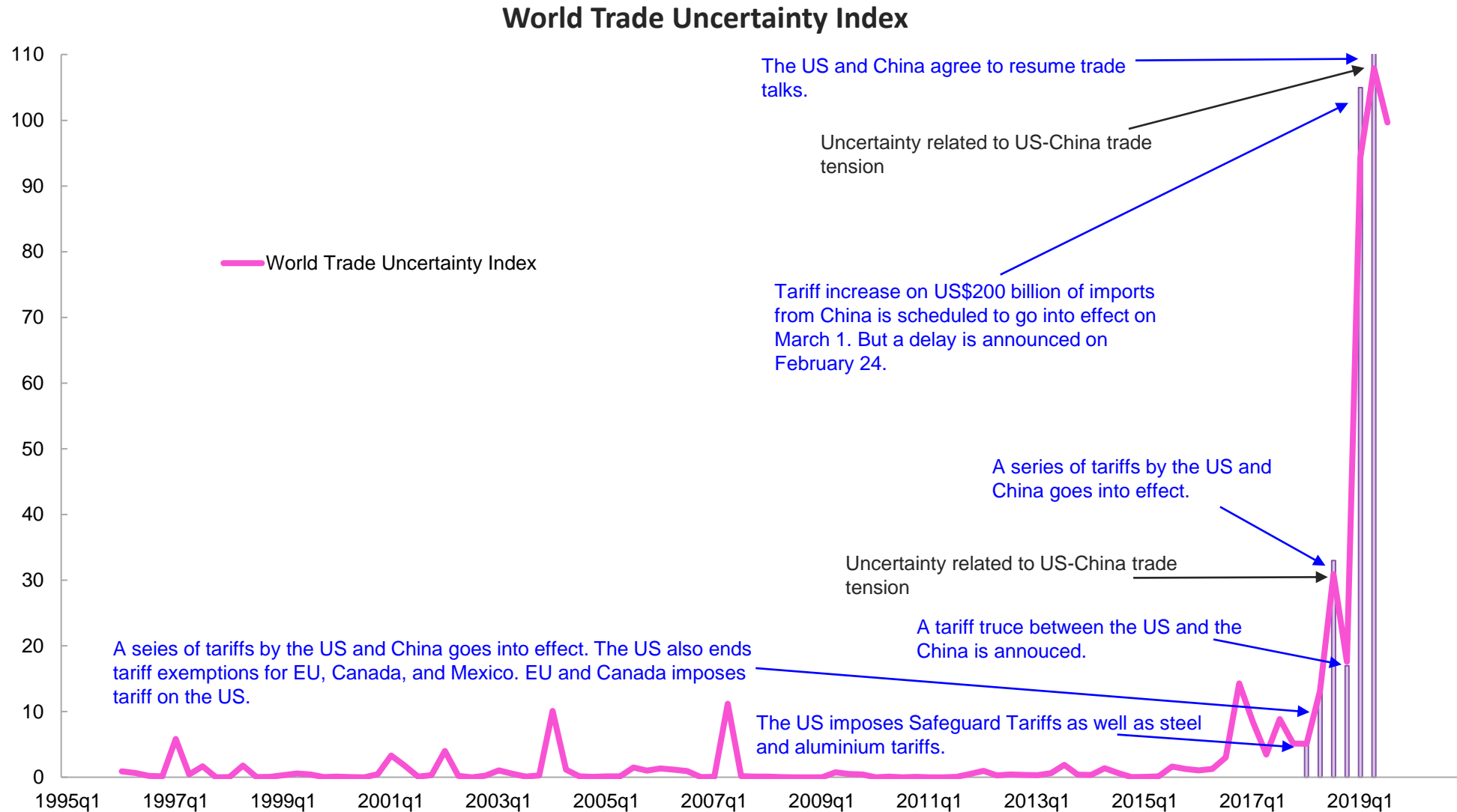


Monetary stimulus

Asset prices

Short-term effects

- **Trade tensions** are an important source of uncertainty in the global economy.



Source: Ahir, H, N Bloom, and D Furceri (2018), "World Uncertainty Index", Stanford mimeo.

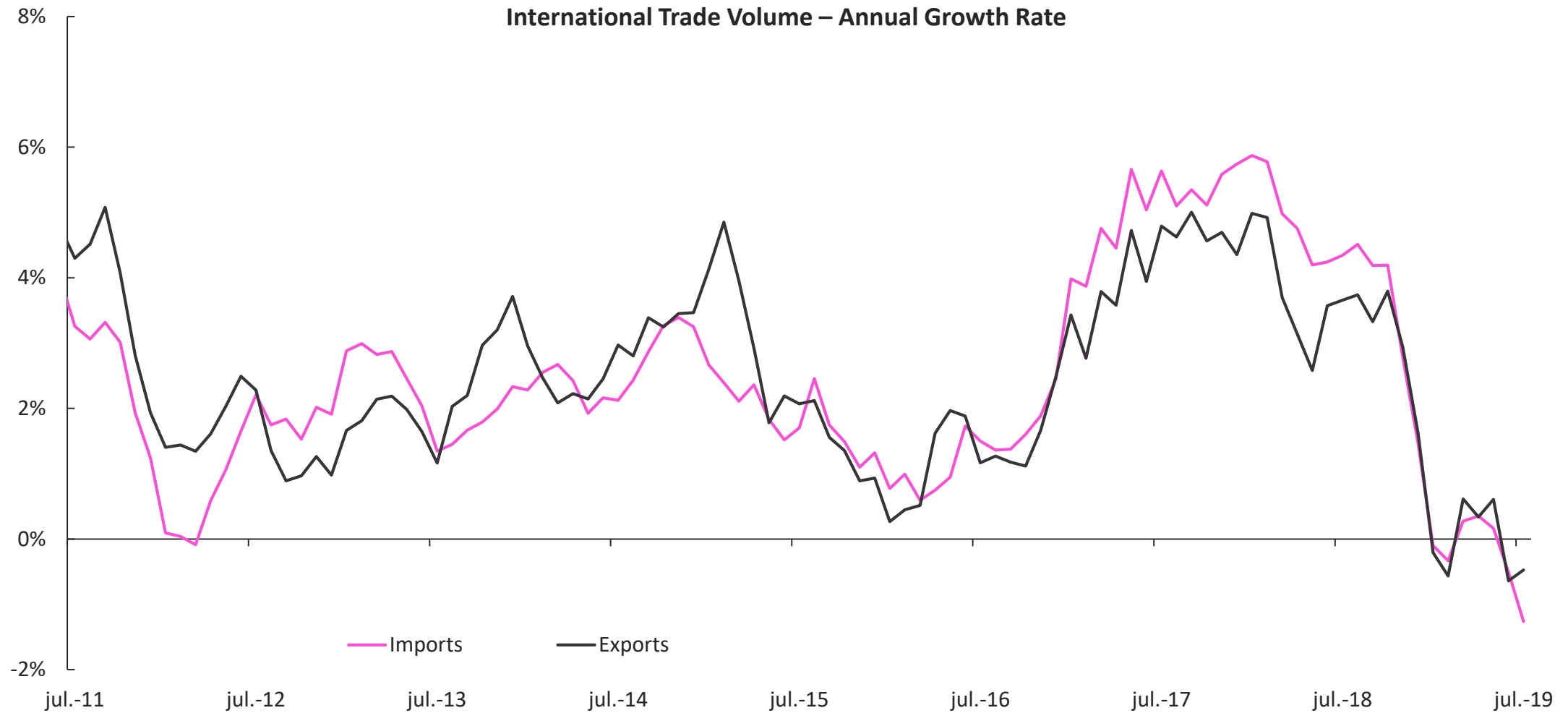
Escalation

Tariffs on exports, %



Source: Peterson Institute for International Economics

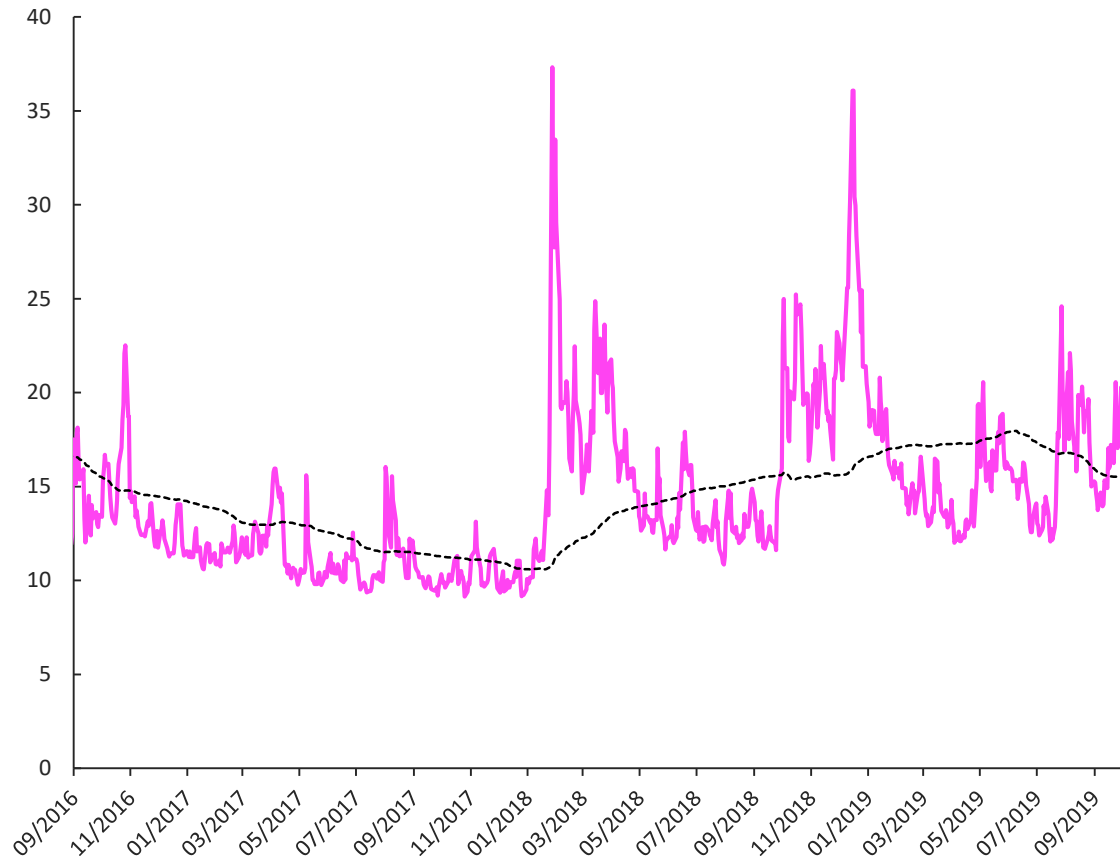
- **Trade tensions** are affecting international trade flows.



Fuente: Bureau for Economic Policy Analysis. Annual growth rate for imports and exports volume.

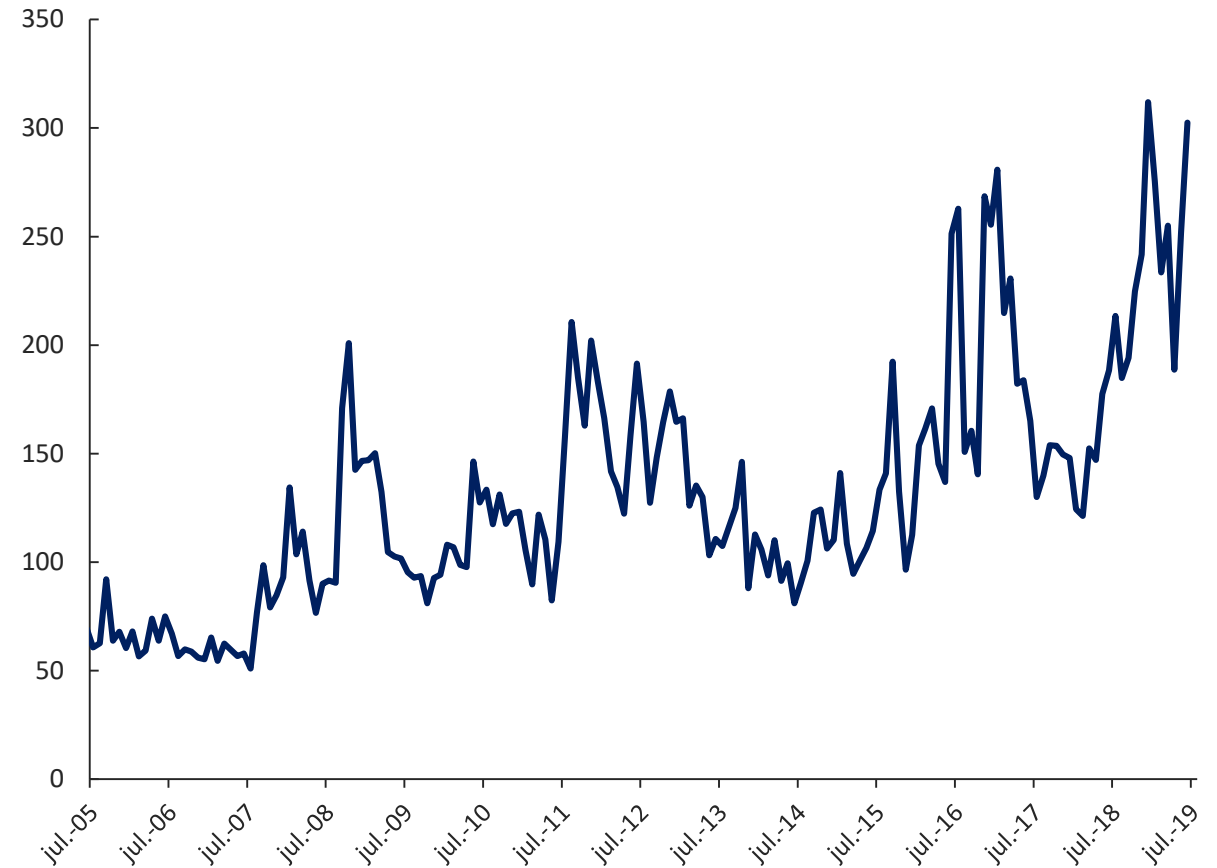
- Furthermore, brexit and geopolitical developments add to the current uncertain environment.

VIX Index



Source: Bloomberg

Global Economic Policy Uncertainty Index*



Source: Davis, Steven J., 2016. "An Index of Global Economic Policy Uncertainty," *Macroeconomic Review* * The GEPU index is a GDP-weighted average of national EPU indices for 16 countries that account for two-thirds of global output. Each national EPU index reflects the relative frequency of own-country newspaper articles that contain a trio of terms pertaining to the economy, uncertainty and policy-related matters.

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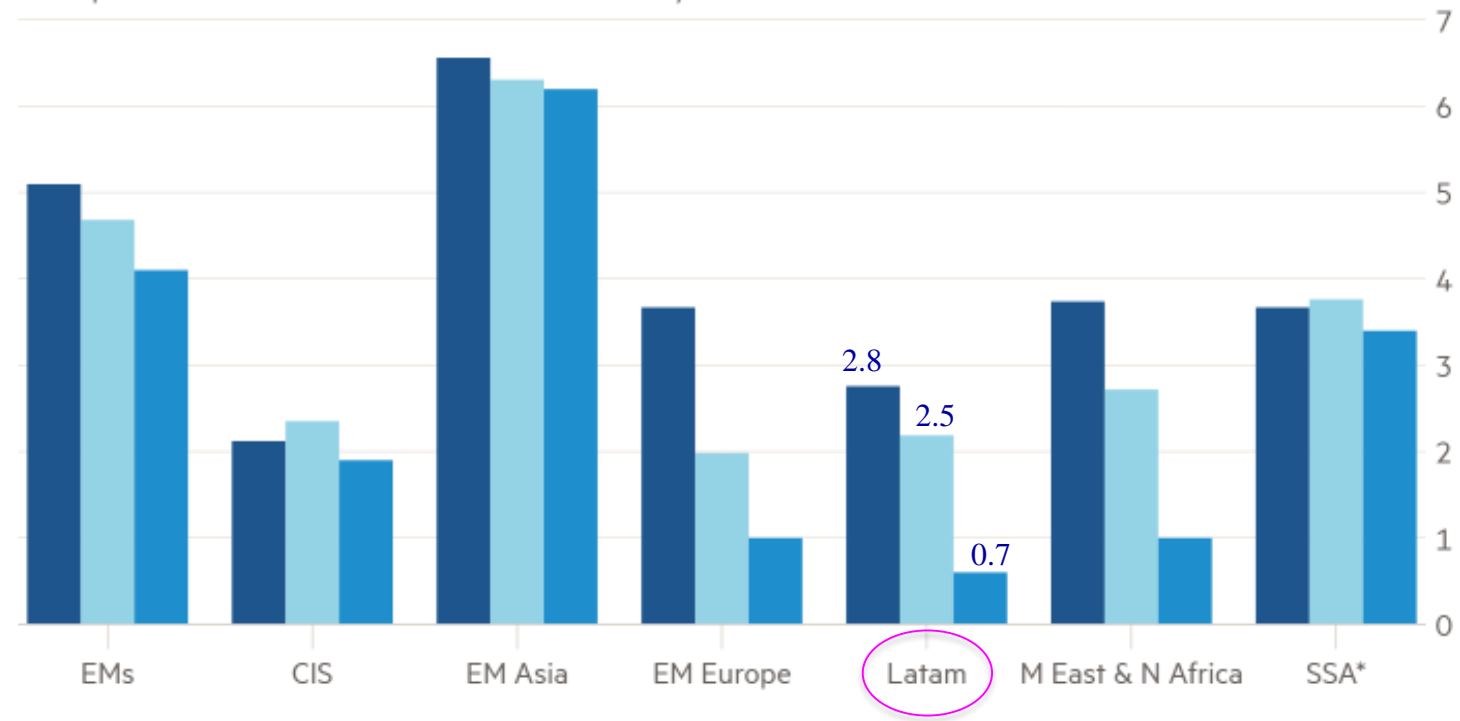
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Deepening gloom

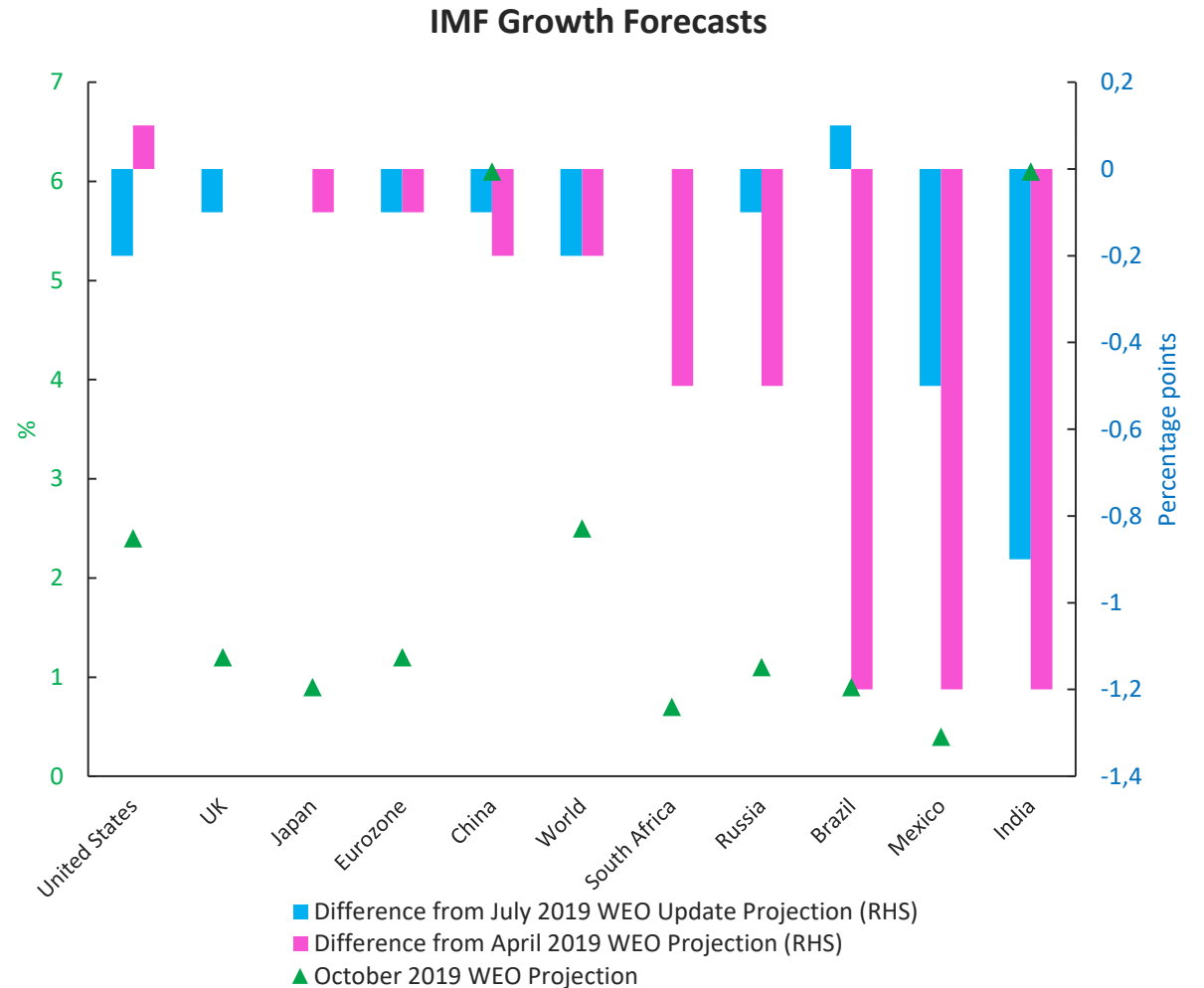
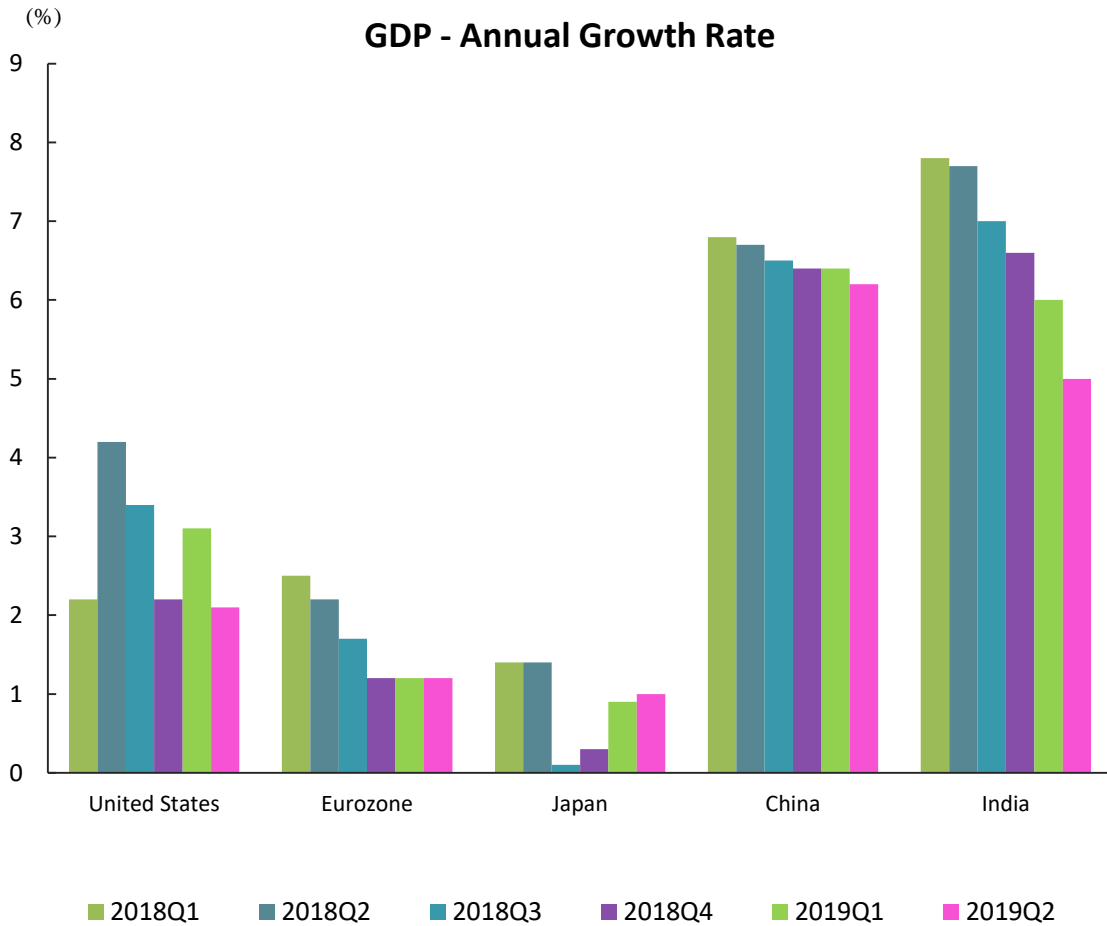
GDP growth forecasts for 2019 (%), by date made

■ April 2018 ■ October 2018 ■ July 2019

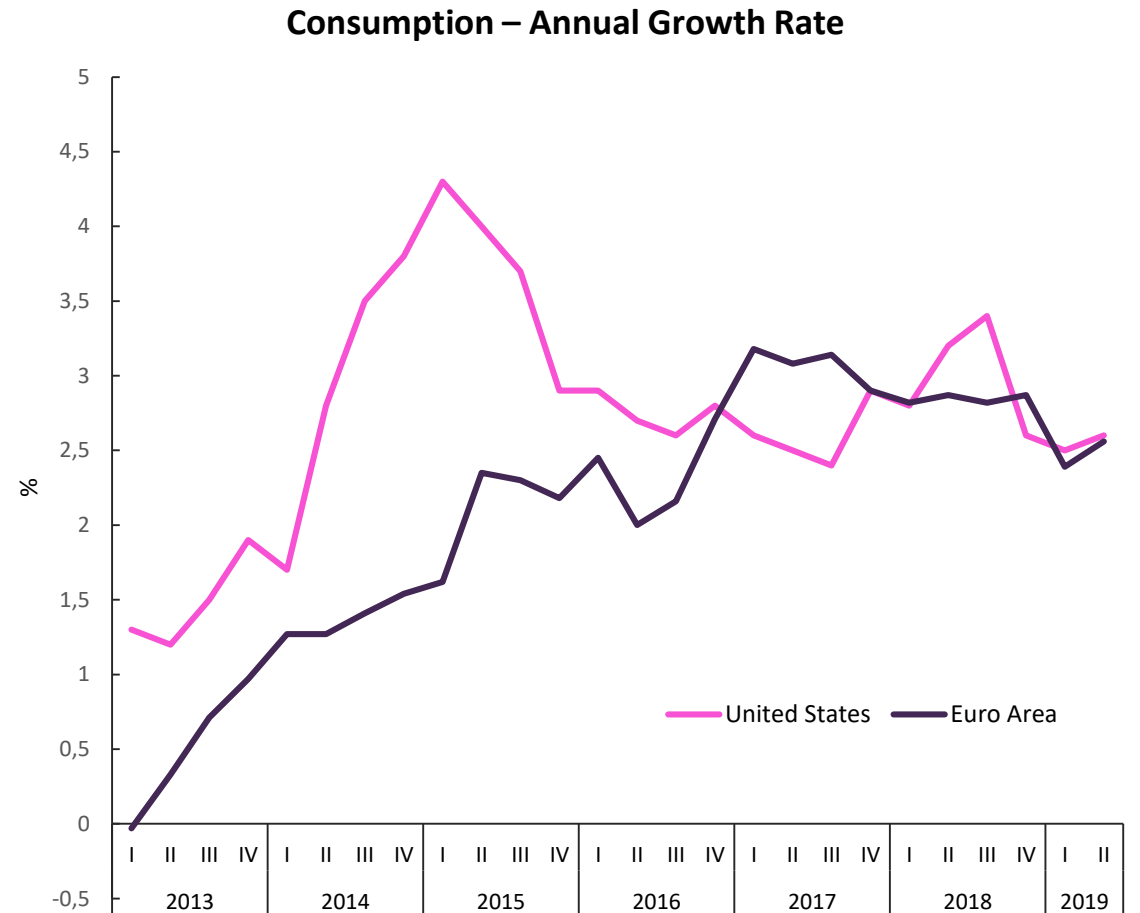
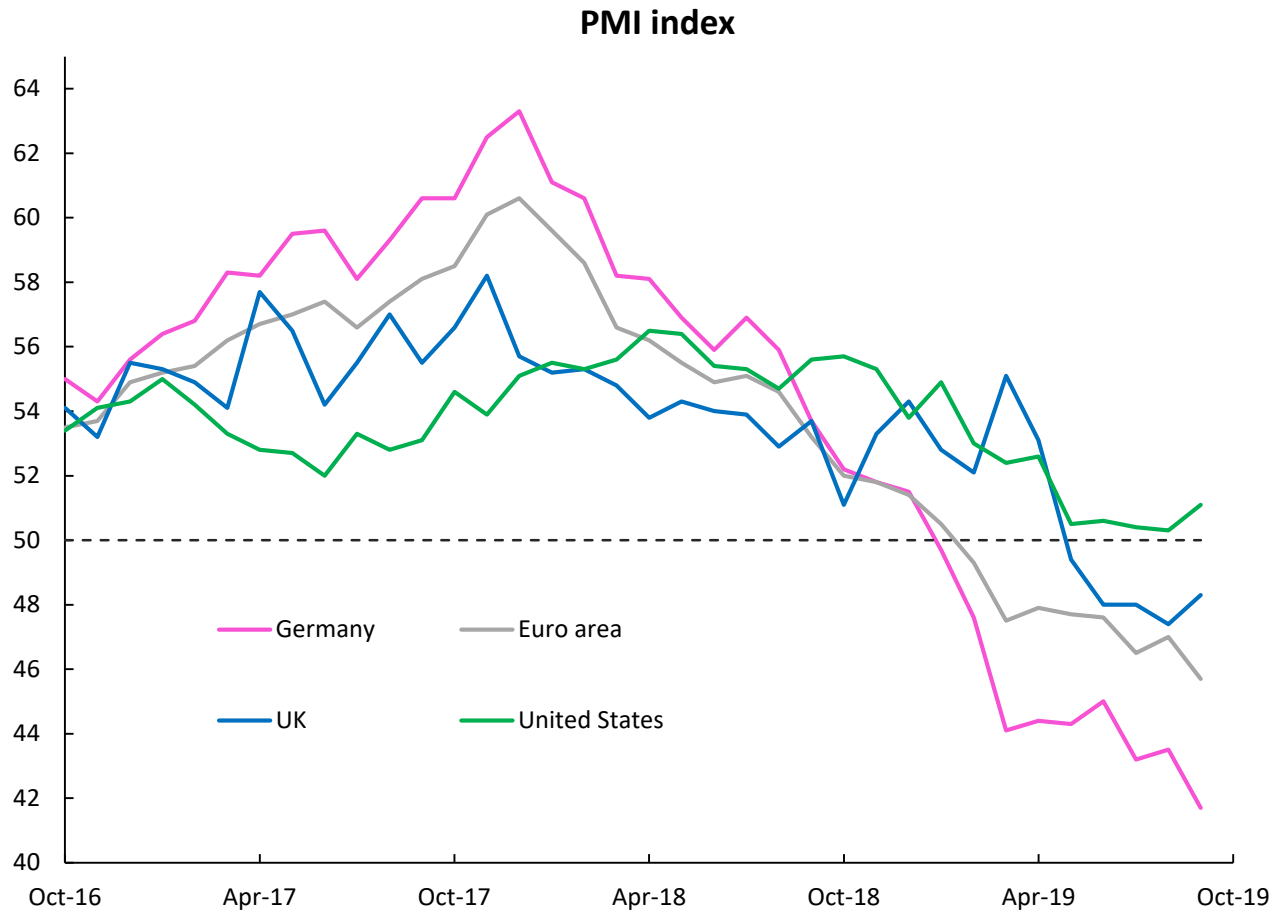


*sub-Saharan Africa
Source: IMF World Economic Outlook
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- The global economy is decelerating, and growth forecasts are lower.
- Trade tensions and uncertainty might be the reason behind lower growth.



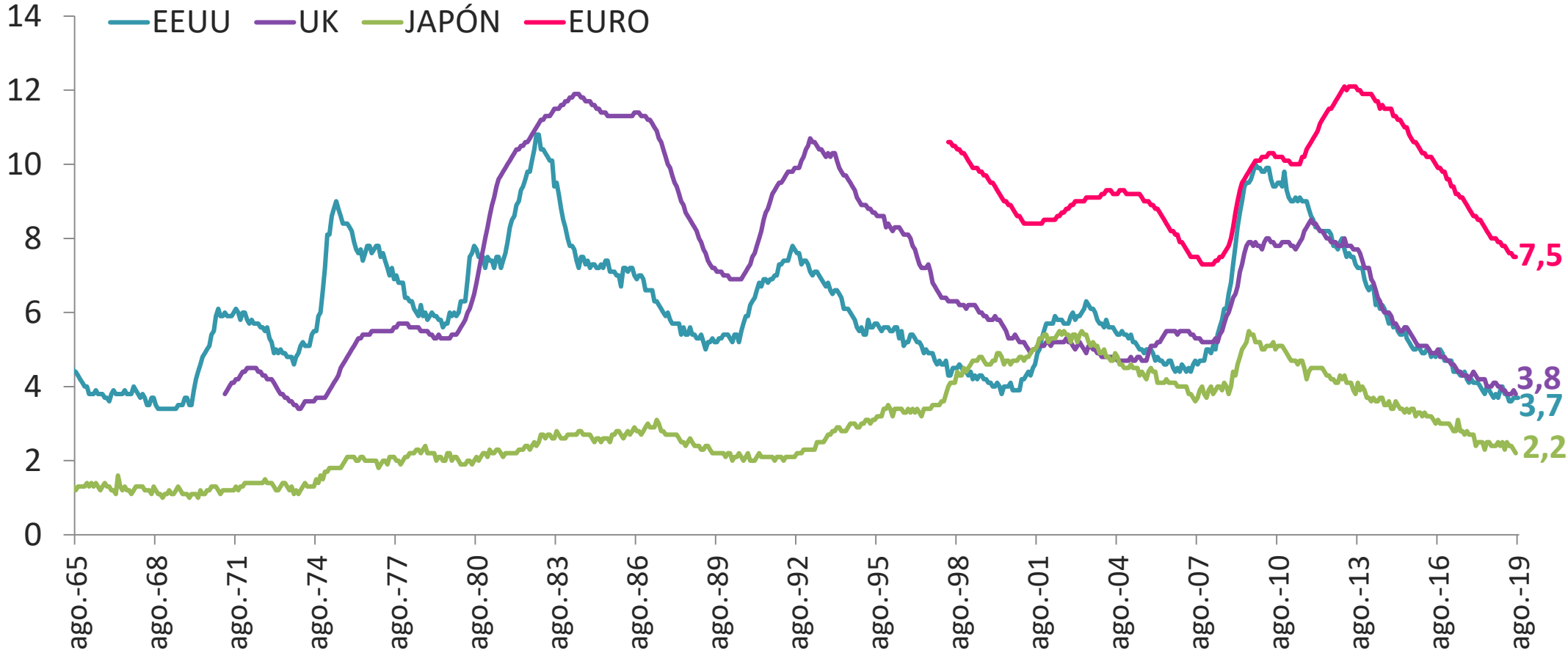
- The signs of global deceleration are clear in the manufacturing sector. On the other hand, consumption remains strong.



Fuente: Bloomberg, St. Louis Fed and ECB. For the United States, growth of the Personal Consumption Expenditure (PCE).

And unemployment very low

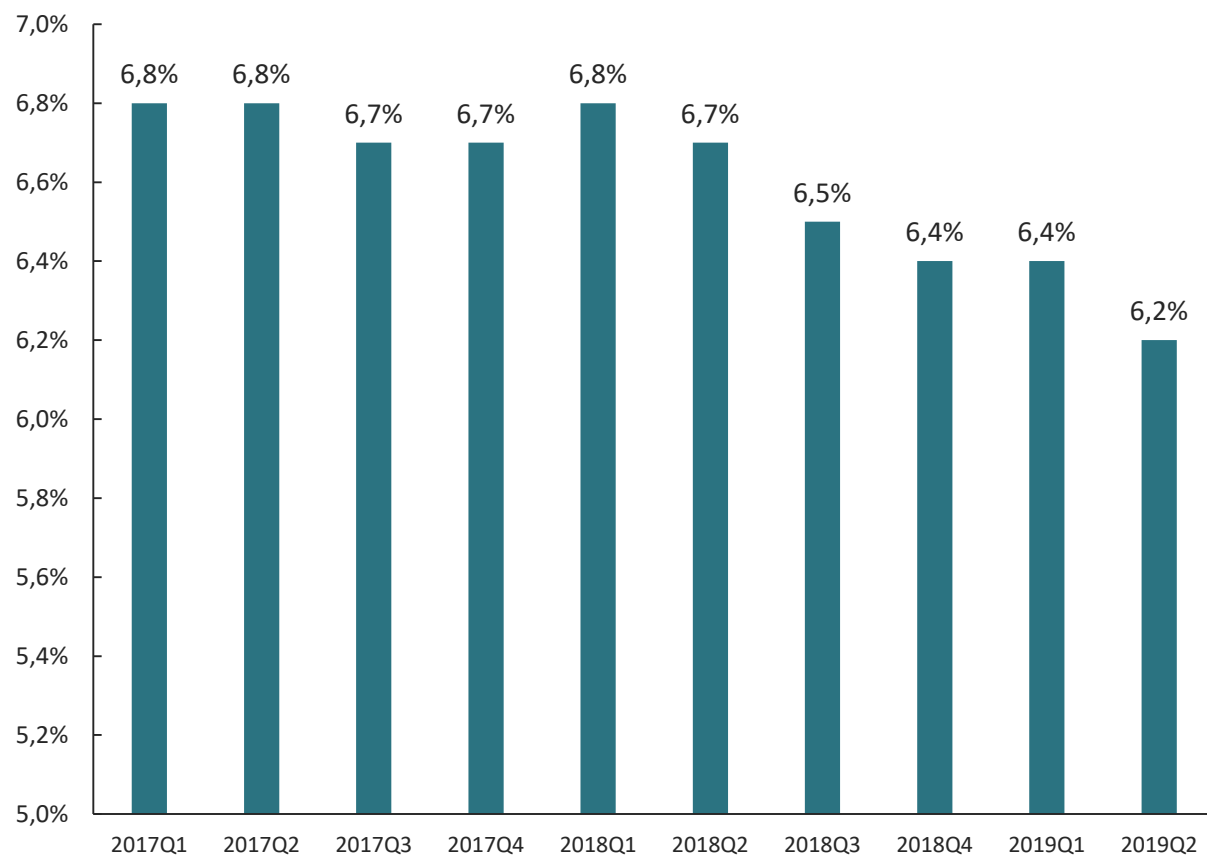
(%)



Source: Bloomberg.

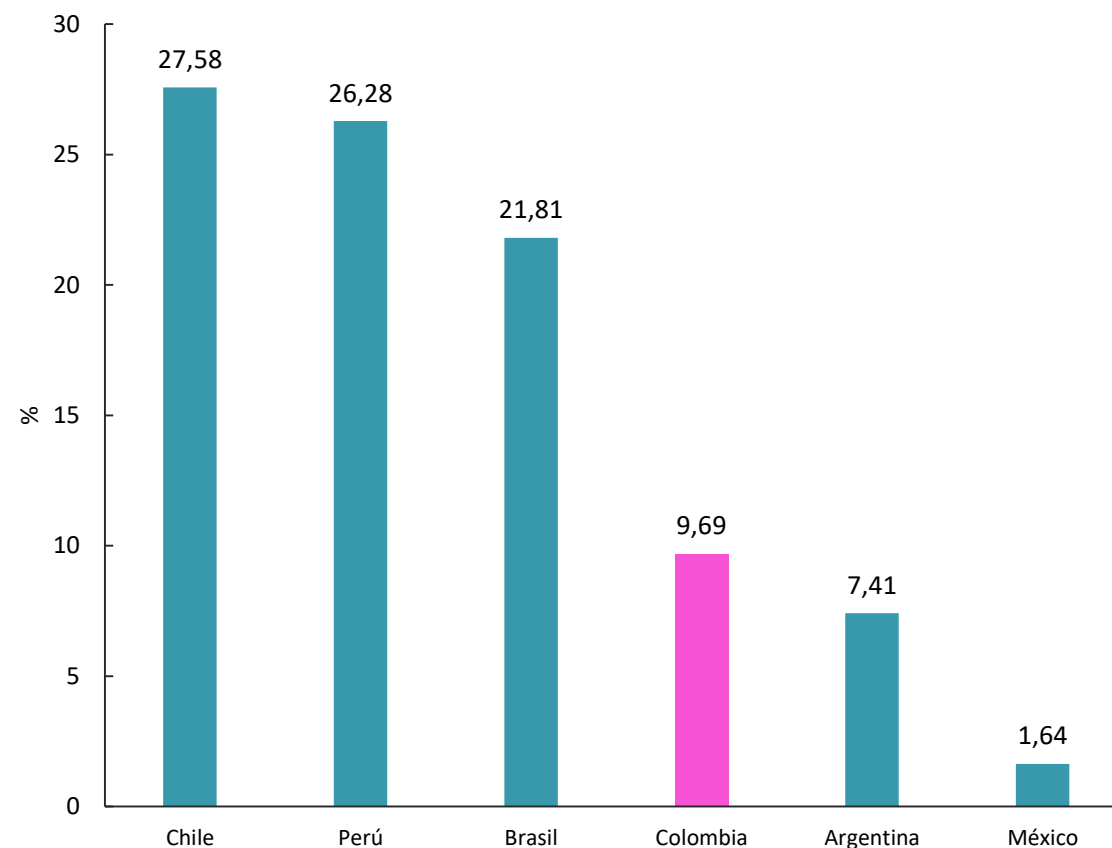
- The lower growth rate in China is of particular concern. A profound deceleration could have consequences on the region through the trade and investment channels.

China - GDP Annual Growth rate



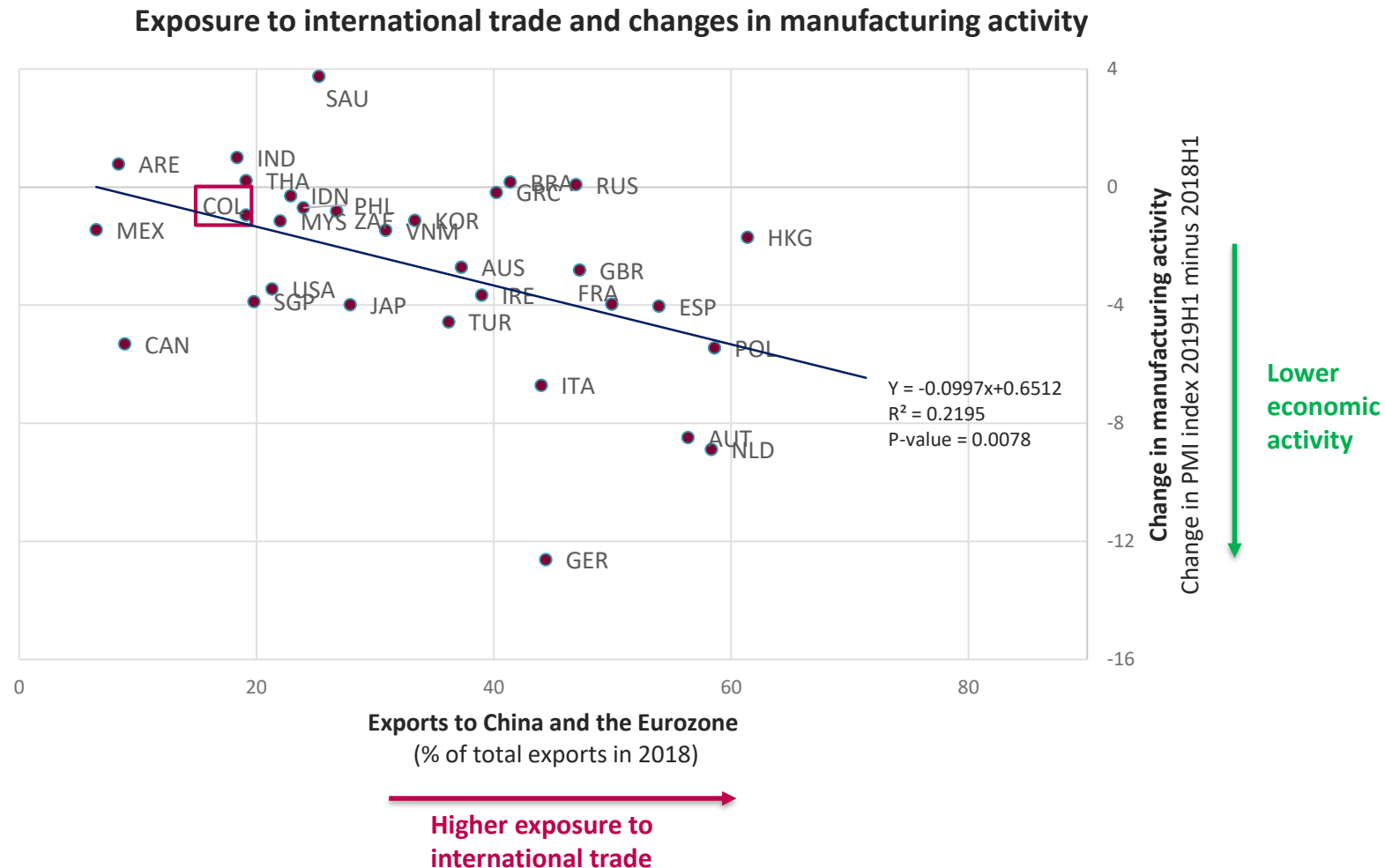
Fuente: FMI

Exports to China as a percentage of total exports



Fuente: UNCOMTRADE y DANE

- Trade tensions could be behind lower growth. Countries more exposed to international trade, and to the regions involved in trade tensions, have seen a larger deceleration in manufacturing activity.



Source: Banrep, IMF – *Direction of Trade Statistics* and Bloomberg. Based on a graph for the BIS June meeting of Governors.

- Besides affecting growth levels, the highly uncertain environment could cause higher volatility in Latam currencies through more volatile commodity prices.

Results of a IGARCH (1,1) model

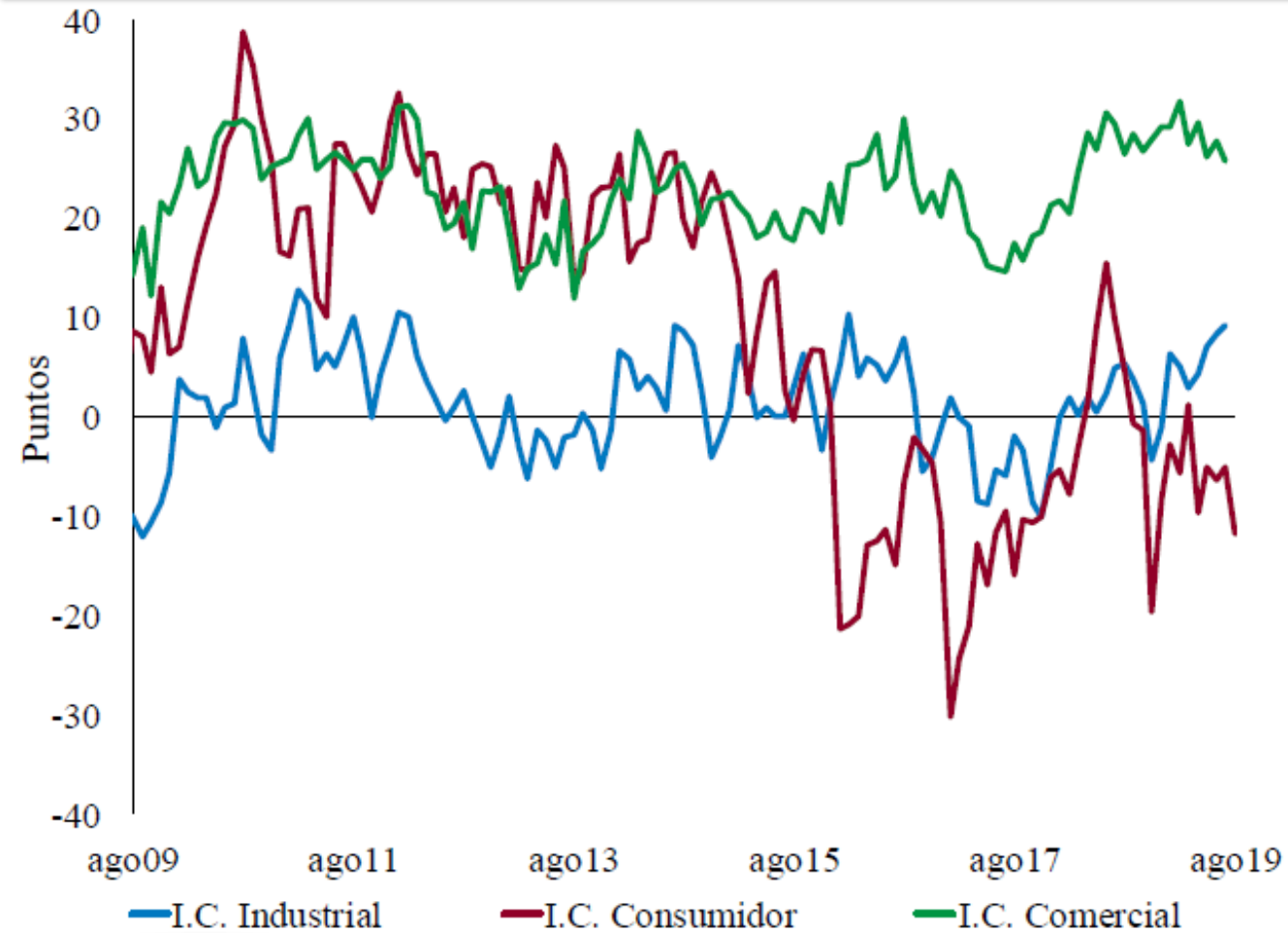
	COP volatility	BRL volatility	CLP volatility	MXN volatility	PEN volatility
Trade Uncertainty	0.000022** (0.000011)	0.0059*** (0.0030)	0.0027*** (0.0010)	0.000012 (0.000013)	0.0017*** (0.0003)
Interest rate differential volatility	-0.0221** (0.0106)	0.0478* (0.0258)	0.0630*** (0.0204)	-0.0064 (0.0061)	0.0072*** (0.0026)
Oil volatility	0.0019** (0.0080)			0.0042** (0.0020)	
Soy volatility		0.0055*** (0.0021)			
Copper volatility			0.0024** (0.0011)		0.0000 (0.0000)

Source: Banco de la República. Coefficients are obtained from the following IGARCH(1,1)-M model with a sample from Jan 2003 to Sep 2019:

$$Returns = \beta_0 + \beta_1 Returns_{t-1} + \beta_2 \Delta Interest\ Rate\ Differential_t + \beta_3 \Delta CDS + \beta_4 Commodities\ Returns + \beta_5 \sqrt{\sigma_t^2} + \varepsilon_t$$

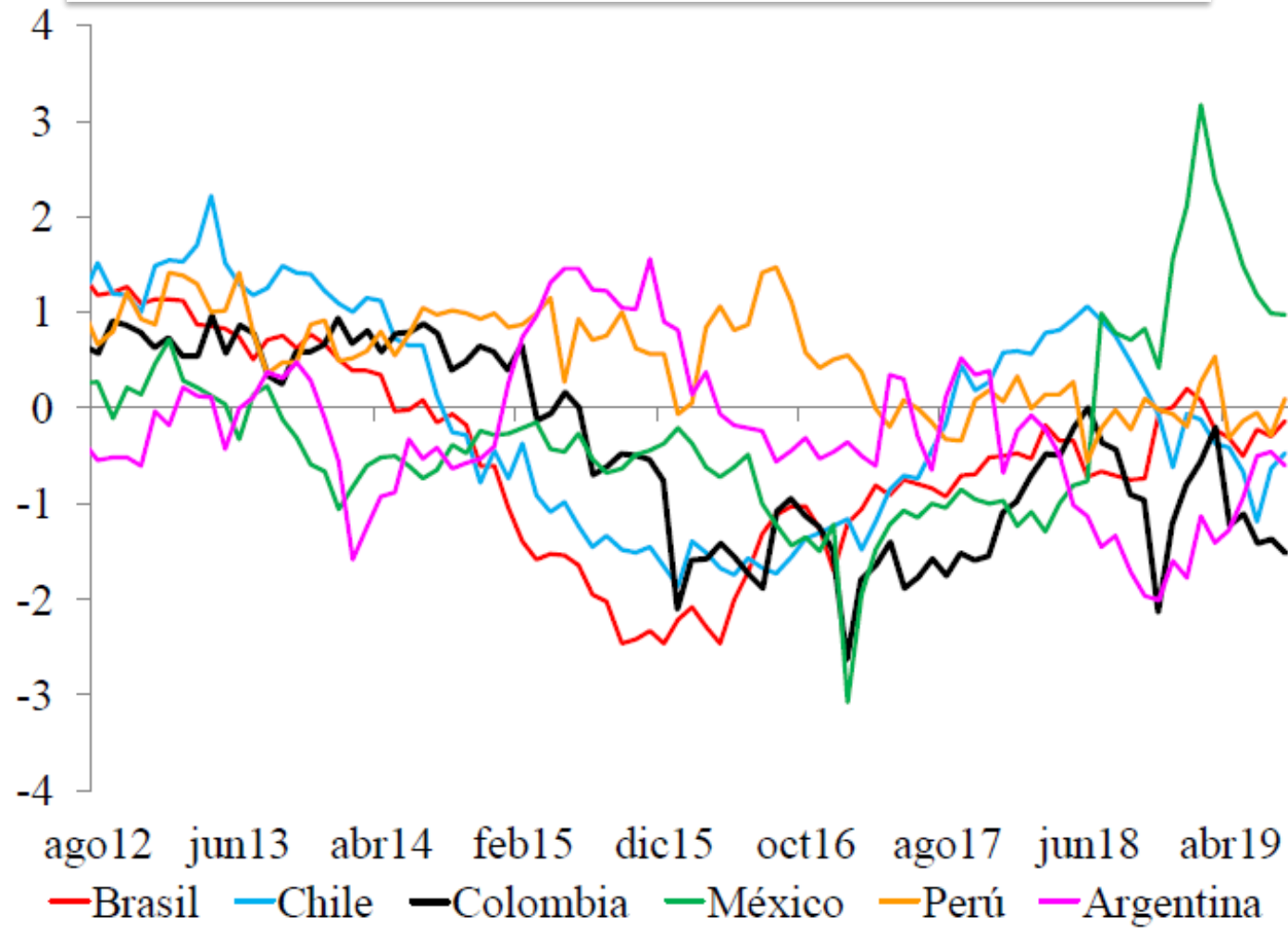
$$\sigma_t^2 = \alpha_1 \varepsilon_{t-1}^2 + \alpha_2 \sigma_{t-1}^2 + \alpha_3 Trade\ Uncertainty + \alpha_4 Vol\ Commodities\ Returns + \alpha_5 Volatility\ of\ Interest\ Rate\ Differential, \quad where \alpha_1 + \alpha_2 = 1$$

Surveys in Colombia: manufacturing, trade and consumption



Source: Fedesarrollo

Consumption surveys in Latin America



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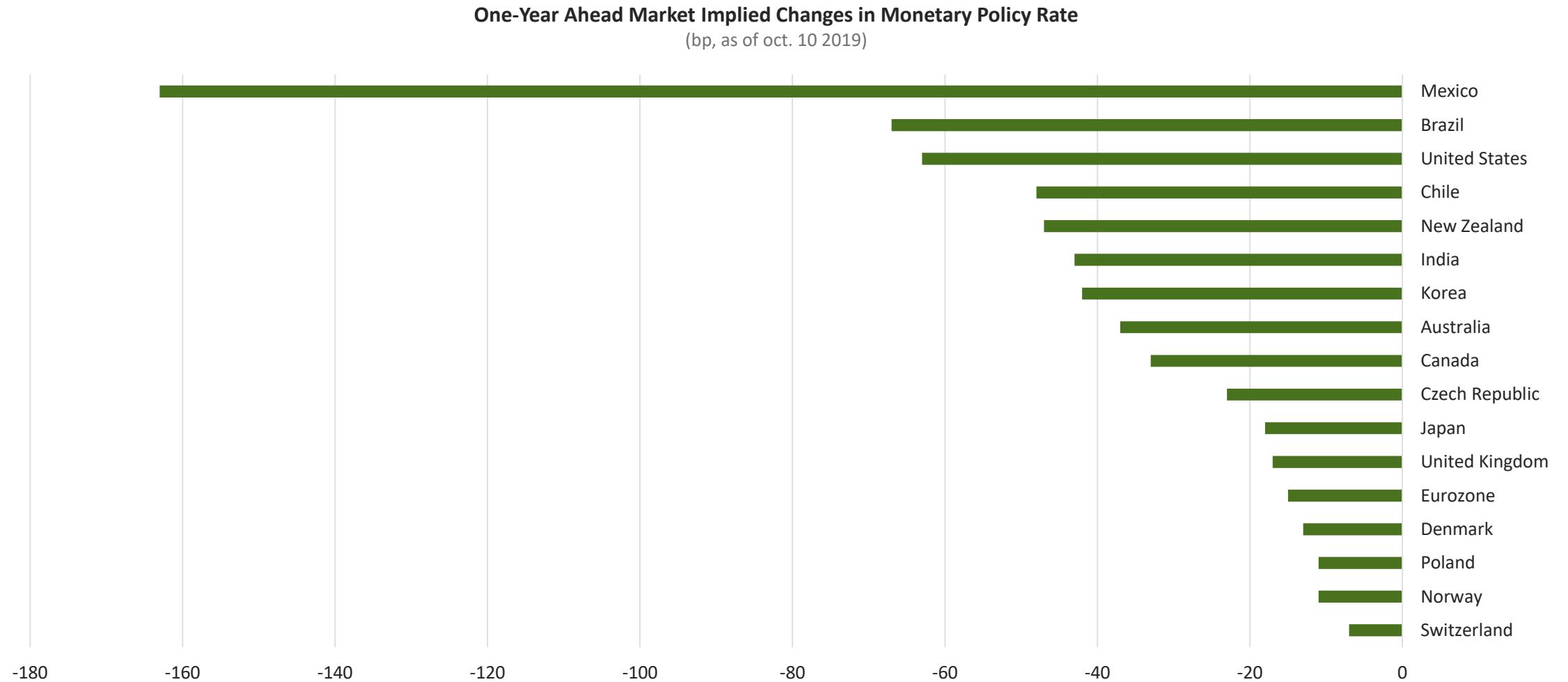


Monetary stimulus

Asset prices

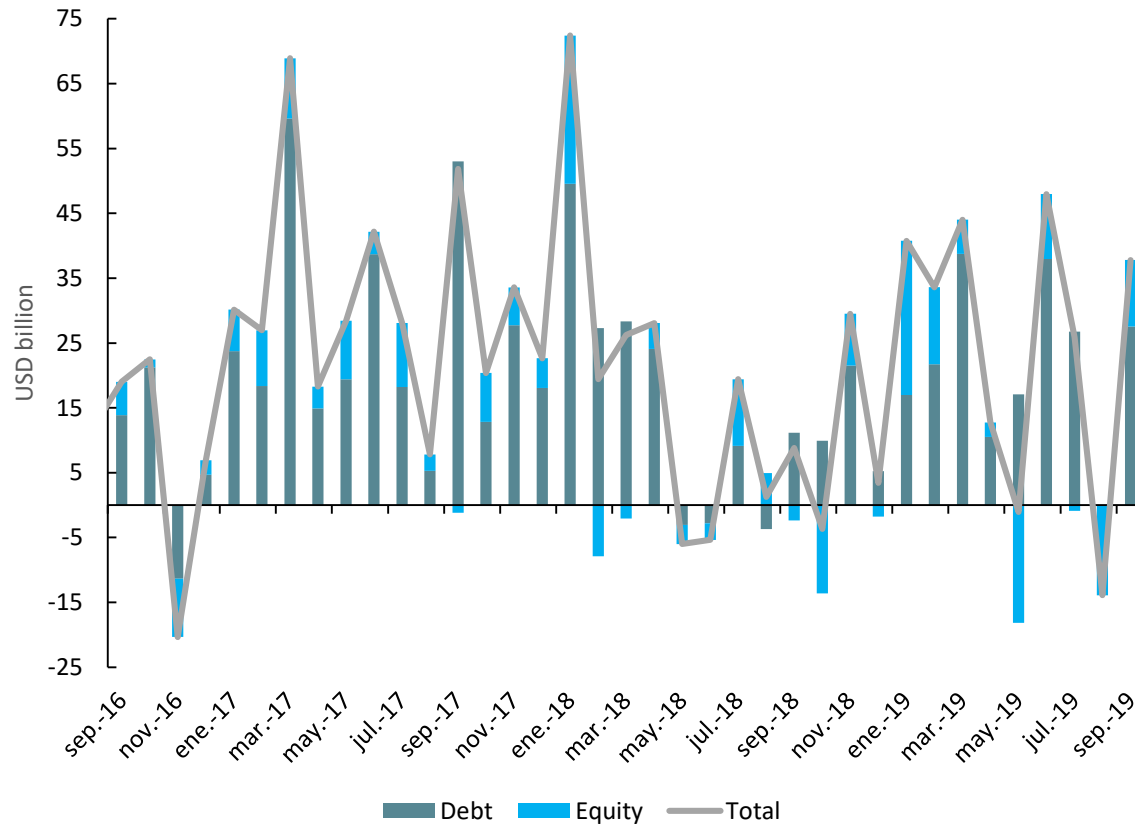
Short-term effects

- Global liquidity continues to be strong, and given the lower growth and higher uncertainty, markets expect monetary policy easing in the future.

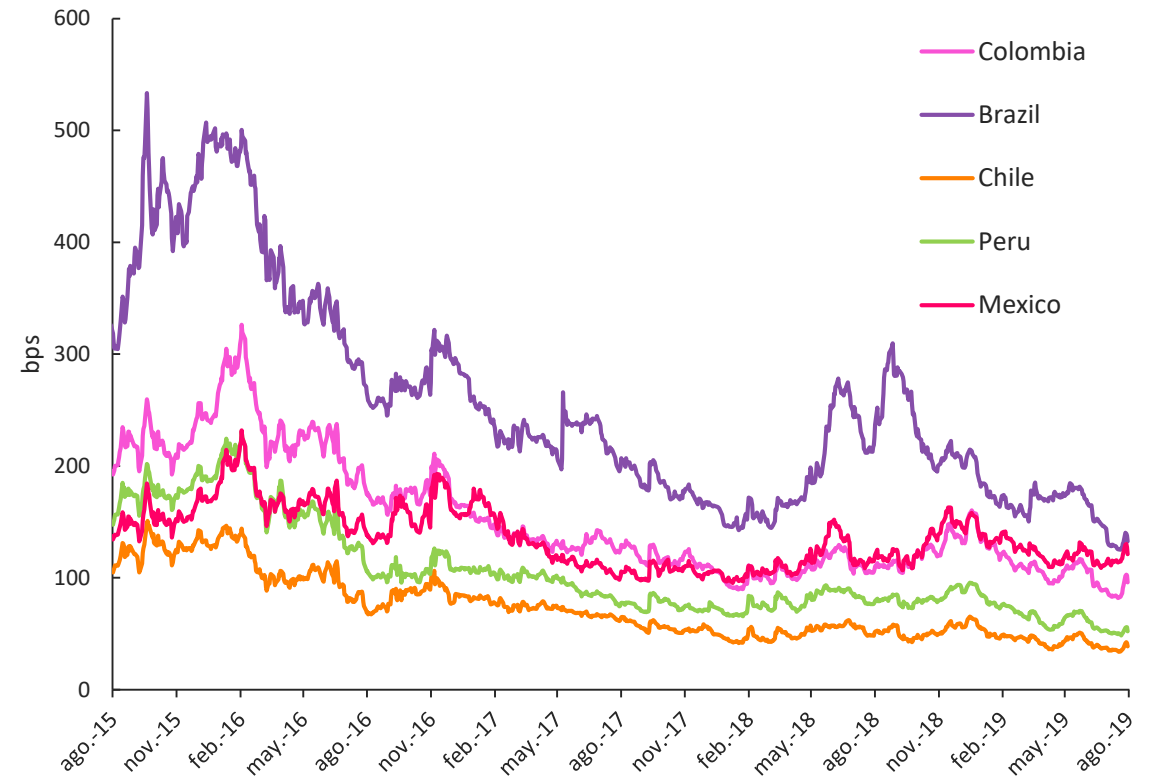


- Emerging markets could benefit from monetary easing through higher capital flows. However, an increase in international uncertainty could alter the financing conditions for these economies.

Portfolio Flows to Emerging Markets



5-Year CDS



Source: Bloomberg and IIF.

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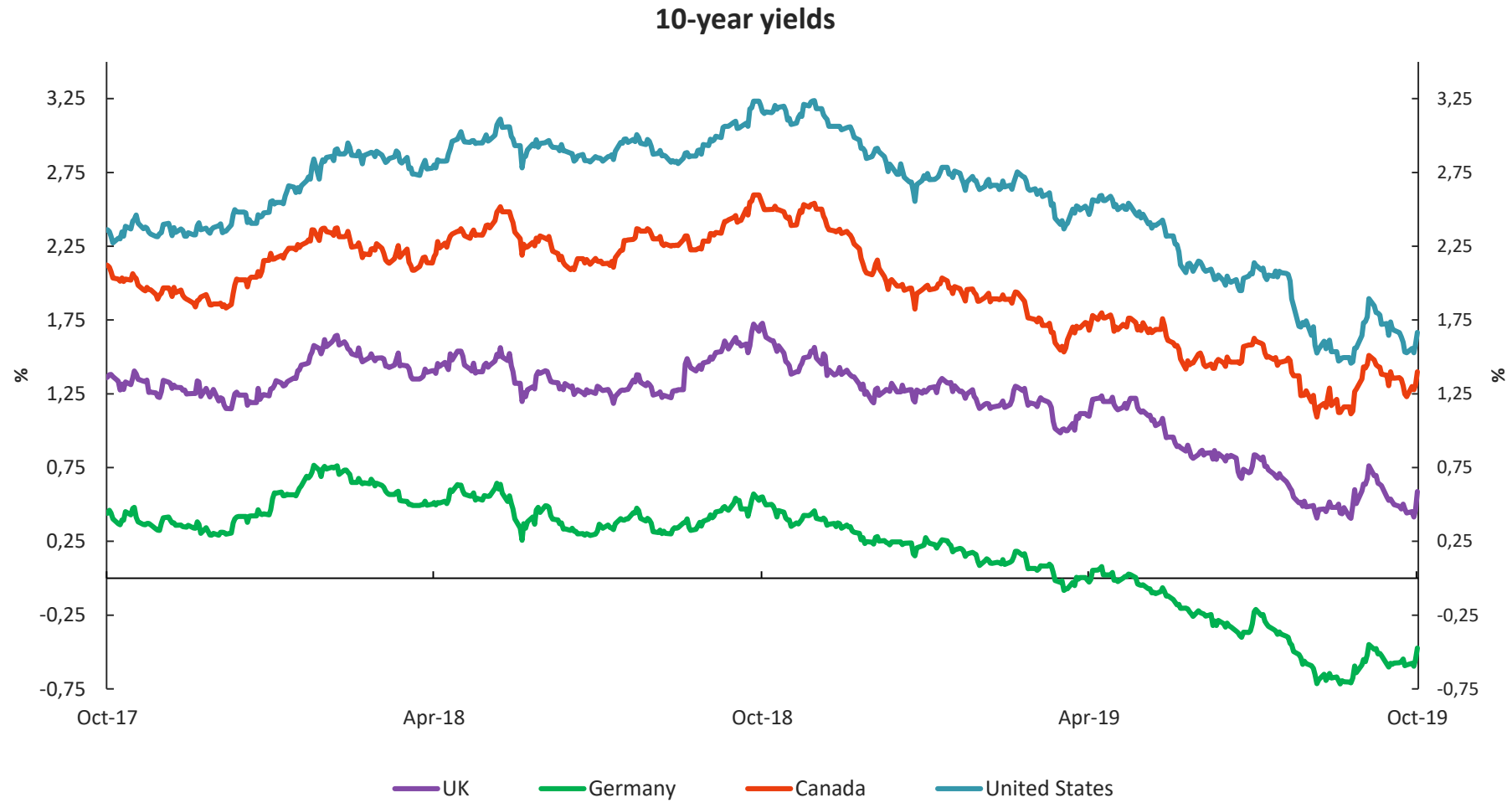


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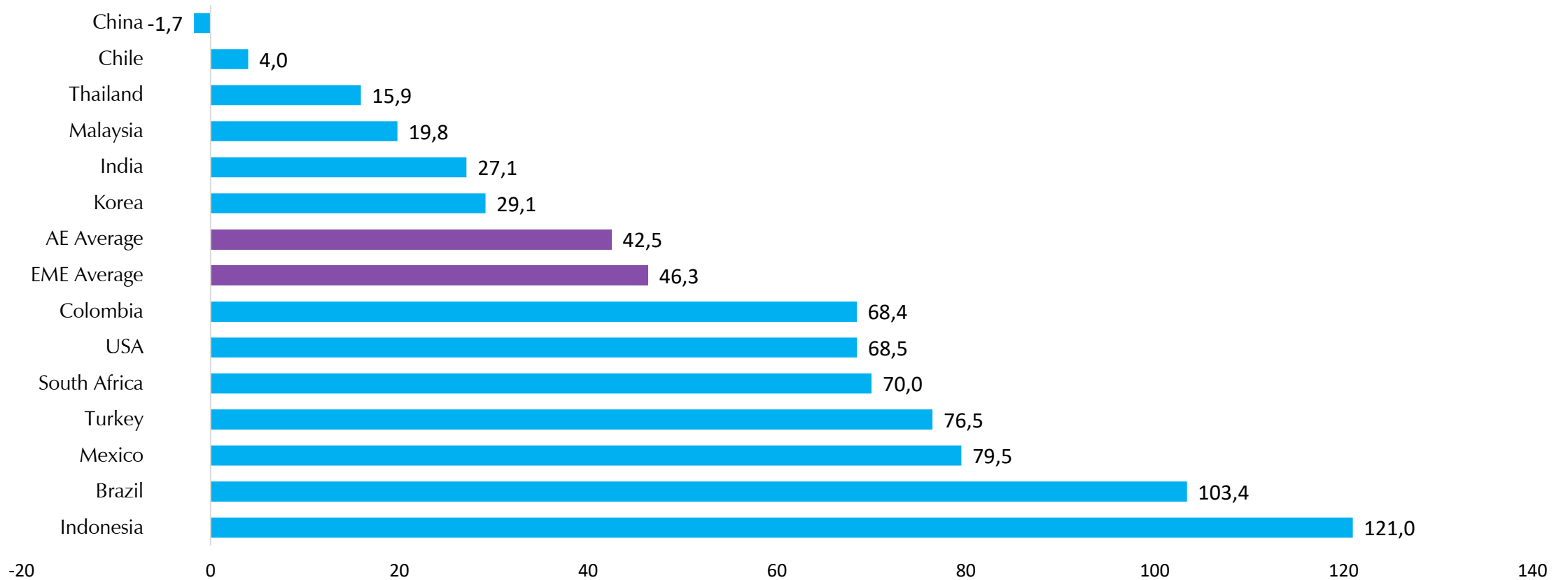
Short-term effects

- Changes in monetary policy expectations, lower growth, and higher international uncertainty have influenced long-term yields in advanced economies.



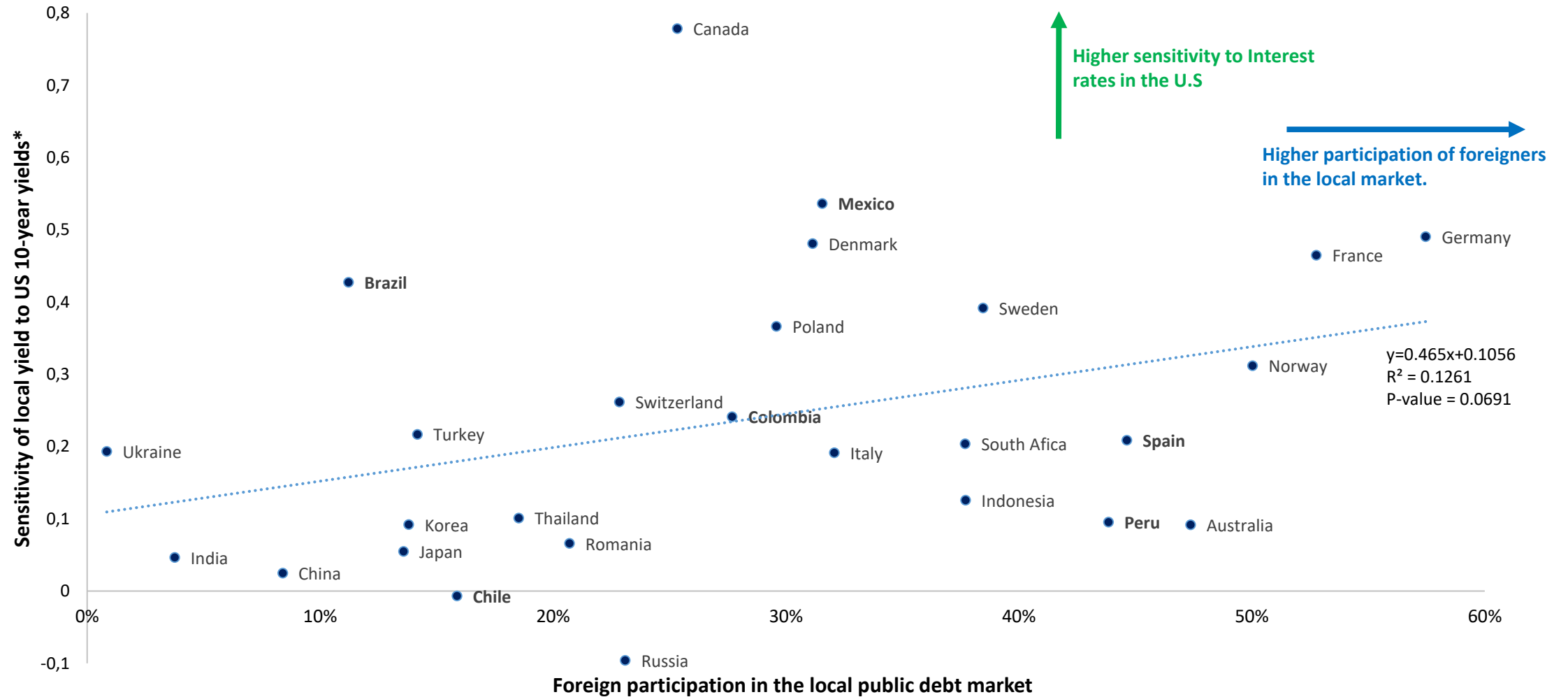
This change could have consequences on local yields and financial conditions.

Change in 10-year Local Currency Sovereign Yields after a 100 bp Monetary Policy Surprise* in the United States
(bp)



Source: Hoek, Jasper, Steven B. Kamin, and Emre Yoldas, 2019. "When Is Good News Bad News? U.S. Monetary Policy, Macro Surprises, and Financial Conditions in Emerging Markets," Federal Reserve Board, unpublished manuscript. The sample spans Jan. 2010 – Aug. 2018 (69 FOMC meetings). *The monetary policy surprise measure is the change in 8-quarter ahead yield implied by Eurodollar futures contract in 1-hour window around FOMC statements. Standard deviation of this surprise measure is about 7 bps. All EME asset prices are measured from day before to day after FOMC statements.

- Some countries might be more sensitive to this spillover given the participation of foreign investors in their financial markets.



- Some currencies in the region are experiencing a decoupling from their traditional fundamental factors.

Colombian Peso and Oil prices



Mexican peso and Oil prices



Source: Bloomberg



Thank you