EMMANUEL MACRON IS MY HERO

After the IMF's latest lessons in political economy.

By Bart Le Blanc

- *What a change: from euphoric reading one year ago with 75% of the world-economy looking forward to growth, to today's IMF prediction of most of the world facing an economic slowdown and darker clouds ahead!*
- *The new IMF Chief Economist Gita Gopinath is uncommonly straightforward in her commentary directed at the world's policy makers: address in a cooperative way the big issues such as climate change, international trade and fiscal imbalances or else fear far worse.*
- *She also calls for more multi-lateral cooperation on these big topics, however many of today's political players do not look to be very attracted by the calls for multilateralism.*
- *Emmanuel Macron's "Grand Débat National" seems to have inspired IMF's call for a "social dialogue on inequality and social discord".*
- *It is a courageous initiative and Macron is my hero!*
- *Much of the Brexit chaos in the UK could have been avoided if some form of grand debate would have been undertaken instead of the current narrow party-political bias.*
- *However major economic and political events do not always have the predicted impact on financial markets, particularly not in times of "easy money".*
- *As long as monetary policies across the developed world remain accommodating (as is currently expected, in contrast to some months ago), risk assets may continue to flourish.*
- *But after a good start of the year, investors could still head for the hills of May (and come back in September?).*

1. "Growth Slowdown, Precarious Recovery"

The Editor of IMF's World Economic Outlook is probably a clever, but prosaic person of few words. The choice for this quarter's report title (see above) is a style example of verbal moderation.

The report starts by observing that much can happen in a year's time. Only one year ago, the IMF shared with us that three-quarters of the world economy was looking forward to a brighter future with higher levels of economic growth.
Today they see the economy slowing down for the larger part of the global economy and further dark stormy clouds ahead!

Overall world GDP growth is predicted to be just above 3% for the year but major uncertainties are threatening and a further drop could be hitting some countries more than others.

Table 1.1. Overview of the *World Economic Outlook* Projections
(Percent change, unless noted otherwise)

		Projections		Difference from January 2019 *WEO Update*[1]		Difference from October 2018 WEO[1]	
	2018	2019	2020	2019	2020	2019	2020
World Output	**3.6**	**3.3**	**3.6**	**–0.2**	**0.0**	**–0.4**	**–0.1**
Advanced Economies	**2.2**	**1.8**	**1.7**	**–0.2**	**0.0**	**–0.3**	**0.0**
United States	2.9	2.3	1.9	–0.2	0.1	–0.2	0.1
Euro Area	1.8	1.3	1.5	–0.3	–0.2	–0.6	–0.2
Germany	1.5	0.8	1.4	–0.5	–0.2	–1.1	–0.2
France	1.5	1.3	1.4	–0.2	–0.2	–0.3	–0.2
Italy	0.9	0.1	0.9	–0.5	0.0	–0.9	0.0
Spain	2.5	2.1	1.9	–0.1	0.0	–0.1	0.0
Japan	0.8	1.0	0.5	–0.1	0.0	0.1	0.2
United Kingdom	1.4	1.2	1.4	–0.3	–0.2	–0.3	–0.1
Canada	1.8	1.5	1.9	–0.4	0.0	–0.5	0.1
Other Advanced Economies[2]	2.6	2.2	2.5	–0.3	0.0	–0.3	0.0
Emerging Market and Developing Economies	**4.5**	**4.4**	**4.8**	**–0.1**	**–0.1**	**–0.3**	**–0.1**
Commonwealth of Independent States	2.8	2.2	2.3	0.0	0.0	–0.2	–0.1
Russia	2.3	1.6	1.7	0.0	0.0	–0.2	–0.1
Excluding Russia	3.9	3.5	3.7	–0.2	0.0	–0.1	0.0
Emerging and Developing Asia	6.4	6.3	6.3	0.0	–0.1	0.0	–0.1
China	6.6	6.3	6.1	0.1	–0.1	0.1	–0.1
India[3]	7.1	7.3	7.5	–0.2	–0.2	–0.1	–0.2
ASEAN-5[4]	5.2	5.1	5.2	0.0	0.0	–0.1	0.0
Emerging and Developing Europe	3.6	0.8	2.8	0.1	0.4	–1.2	0.0
Latin America and the Caribbean	1.0	1.4	2.4	–0.6	–0.1	–0.8	–0.3
Brazil	1.1	2.1	2.5	–0.4	0.3	–0.3	0.2
Mexico	2.0	1.6	1.9	–0.5	–0.3	–0.9	–0.8
Middle East, North Africa, Afghanistan, and Pakistan	1.8	1.5	3.2	–0.9	0.2	–1.2	0.2
Saudi Arabia	2.2	1.8	2.1	0.0	0.0	–0.6	0.2
Sub-Saharan Africa	3.0	3.5	3.7	0.0	0.1	–0.3	–0.2
Nigeria	1.9	2.1	2.5	0.1	0.3	–0.2	0.0
South Africa	0.8	1.2	1.5	–0.2	–0.2	–0.2	–0.2
Memorandum							
European Union	2.1	1.6	1.7	–0.3	–0.1	–0.4	–0.1
Low-Income Developing Countries	4.6	5.0	5.1	–0.1	0.0	–0.2	–0.2
Middle East and North Africa	1.4	1.3	3.2	–0.9	0.3	–1.2	0.3
World Growth Based on Market Exchange Rates	3.1	2.7	2.9	–0.3	0.0	–0.4	0.0
World Trade Volume (goods and services)	**3.8**	**3.4**	**3.9**	**–0.6**	**–0.1**	**–0.6**	**–0.2**
Imports							
Advanced Economies	3.3	3.0	3.2	–1.1	–0.1	–1.0	–0.3
Emerging Market and Developing Economies	5.6	4.6	5.3	–0.5	–0.3	–0.2	–0.2
Exports							
Advanced Economies	3.1	2.7	3.1	–0.2	–0.3	–0.4	–0.3
Emerging Market and Developing Economies	4.3	4.0	4.8	–0.5	0.0	–0.8	0.0
Commodity Prices (US dollars)							
Oil[5]	29.4	–13.4	–0.2	0.7	0.2	–12.5	4.2
Nonfuel (average based on world commodity export weights)[6]	1.6	–0.2	1.1	2.5	–0.1	0.5	0.8
Consumer Prices							
Advanced Economies	2.0	1.6	2.1	–0.1	0.1	–0.3	0.1
Emerging Market and Developing Economies[7]	4.8	4.9	4.7	–0.2	0.1	–0.3	0.1

What cannot be ignored is the cumulative, negative impact of serious restrictions and uncertainties from US driven trade tensions, tensions within Europe e.g. Brexit, Europe's North-South divide, the impact of new car emission limits in Germany, economic crises in Argentina and Turkey, volatile commodity markets and so on.
However the IMF expects the slowdown to be not more than a dip with a recovery in the second half of the year, followed by resumed growth in 2020 as earlier foreseen (see summary table above).

The 2019 dip is expected to be most prominent in some European countries each for very different reasons: Germany -0.5% resulting from lower business confidence and the impact of new car emission limits on the automotive industry, Italy – 0.5% following the lack of structural reform in the populist government policies and the UK as its outlook continues to suffer under Brexit uncertainty.

Since late 2018, slowing trade levels and lower industrial production have left their marks. Inflation expectations have fallen, as have interest rates in their wake. But following a severe market correction at the end of 2018, the asset bubble has now fully reflated and is as gaseous as before. As former Euromoney Editor Hamish McRae recently concluded: "*Thanks to a decade of a world awash with cash, asset prices have soared…. High asset prices pass on more wealth to those who already have it. The result is that … in most developed countries wealth inequality has risen"* (The Times 16 April 2019 see also my previous commentary "*The BIG Question*" of January 2019).

This first World Economic Outlook under IMF's new Chief Economist Gita Gopinath takes an impressively refreshing firm stance on the many non-economic threats to the world economy. Her lessons on political economy for national and international policy makers are well chosen.
In the Outlook the IMF addresses policy makers around the world directly by asking them to urgently tackle in a "*constructive and cooperative way"* issues such as the following:

- Climate change
- International trade
- Brexit
- Financial imbalances in public finance and banking particularly in countries such as Italy
- Social dialogue on "inequality and social discontent"
- International tax effectiveness.

Mrs. Gopinath writes in her Foreword "*There is a need for greater multilateral cooperation to resolve trade conflicts, to address climate change and risks from cyber security, and to improve the effectiveness of international taxation.*"

2. Bretton Woods' 75th anniversary present: today's political leaders' views on multi-lateral cooperation

A call for international cooperation might not be what is foremost in the mind of some of today's big political power players such as president Trump, chairman Xi and president Putin, president Jair Bolsonaro in Brazil, and populist politicians in Europe such as Matteo Salvini and Luigi Di Maio in Italy or Viktor Orban in Hungary and Jaroslaw Kaczynski in Poland.
Even in traditionally open, liberal and democratic countries in Europe, the political rally cry of a growing group of nationalist and/or populist movements follows the "MAKE **MY** COUNTRY GREAT AGAIN" slogan.

Not the best environment to ask for more international cooperation. It seems that policymakers' inclination to cooperate has never been so low since the Bretton Woods Agreement 75 years ago.

The growing list of visible power play by politicians around the world illustrates an increasingly nationalistic streak; actions that are deemed good for "our own people".

This list of topics is also frightening.
On international trade and economic and political cooperation:

- US Trade policy tensions with neighbouring countries Canada and Mexico, with China and with the EU.
- US withdrawal from the Climate Change Paris Treaty.
- Brexit
- Plans to build a wall on US-Mexican border
- China financial "imperialism" through initiatives such as the Silk Route/Belt and Road Project
- Attacks on the FED's independence as central bank
- Anti-migration actions in many developed economies assumed to protect "Jobs for our own people"

Political upheaval in Europe:

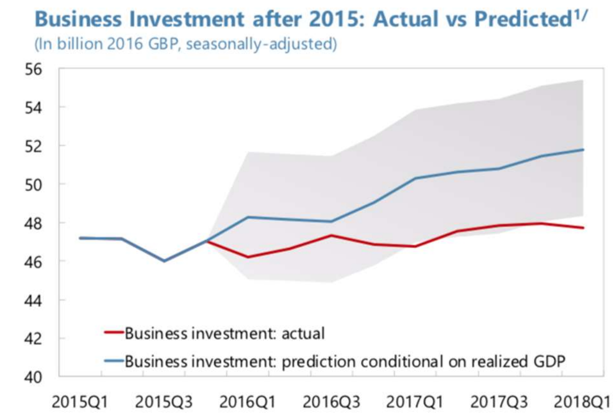
- "Yellow Vests" grass roots protests against government reforms and "green" taxes in France
- Italian populist coalition government (right wing Euro-sceptic LegaNord/Salvini - Left wing Five Star Movement/Di Maio) aimed at redressing government cuts and introducing a minimum income for all
- New "illiberal democracies" in Hungary and Poland reforming migration policies and control over the judicial system
- Growing right wing mostly Euro-sceptic movements in many northern European countries such as Sweden, Denmark, Germany and the Netherlands resulting in political fragmentation

On security issues:

- Cyber-crime as a new warfare instrument
- China's approach to IP, intelligence, etc.
- Growth of right wing/fascist terror as seen in New Zealand threat
- US withdrawal from the Iran nuclear treaty and threatening other Treaty partners with reprisals
- US pressure on other NATO members re NATO contribution levels
- Ongoing Israel-Palestine conflict incl. land grab of disputed territory and other Middle East tensions

And the list is far from exhaustive. In normal times, economic development would suffer under so much conflict, tension and uncertainty. Particularly companies would wait and see before investing.

Take the United Kingdom as an example. A recent IMF study "*Brexit Referendum and Business Investment in the UK*" by Lucyna Górnicka (October 2018) points at a growing gap between predicted levels of business investment and actuals after the UK referendum (see graph below).



Sources: Haver Analytics, author's calculations.
1/ Grey area: 90 percent prediction bands.

One can only wait to see the devastating impact that such development may have on employment and income.

At the same time it seems surprising that the world is relatively peaceful although social media might sometimes give you another idea. Economic growth may be at a slower pace but people seem to go about their usual business.
Increased consumption in the UK compensates partly for lower investment and things seem for many not that bad.
And the introduction of a basic income in Italy is likely to result in higher public debt, which is already the highest in Europe after Greece.
So is the "*no worries"* approach the right attitude for the short term?

3. Yellow Vests in France

There is no escaping the structural reform message of the IMF for a sustainable economic outlook whichever country focus one takes. As Gita Gopinath advocates, countries need to address the multiple threats in a constructive and cooperative way.
France seems to have been the intriguing inspiration for her call for a *"Social dialogue on inequality and social discontent".*

Following the first Yellow Vests protest in France at the end of 2018, it became quickly clear that this was not just a flash-in-the-pan type of grass roots protest.
It was also not a repeat of 1968.
And not just another urban protest movement driven by ideas of anti-US and its Vietnam war, by a different vision on democracy, on capitalism, against consumerism. A movement initiated by students and followed by workers' rights activists.
No, the 2018/2019 Yellow Vests initiative comes from rural origins as a protest against impact on lower and middle income families from cumulative government actions on labour market reforms, public spending cuts, welfare reforms, changes in the pension system.

The protest movement flared up when the same rural people were also confronted by a series of ecological measures such as a lower speed limit on rural roads and the extra charges on diesel fuel for their cars. The fact that these measured were passed through the political system in for France uncustomary speed, made people feel "jumped on".
As many of the measures were part of a broader economic reform package in which reduction of corporate and wealth tax were introduced, made it easy to demagogically fight for these reverse Robin Hood politics ("Rob the poor to give it to the rich").

The Yellow Vests movements is not a political movement but seem to consist more of groups of local disaffected people who protest on a regular basis i.e. Saturday every week, by blocking traffic on roundabouts throughout France, and demonstrate in the big cities and particularly in Paris.
After its relatively peaceful start in November 2018 more hard-core protesters and vandalism elements have joined (and taken over?) the movement as a result of which they have become more violent and particularly in Paris even criminal through aggressing people and police and even looting.
The Saturday marches and protest actions continue till today although at a much diminished scale.

4. Le Grand Débat National

President Emmanuel Macron's initial reaction was fierce with much police presence and police action against sometimes violent protest and, in some cities, criminal behaviour such as looting of shops.
But after months of persistent protests and actions in many parts of France, the government acknowledged that there was more to these Yellow Vests demonstrations then just disagreement on certain cumulative government action and measures.

From the last weeks of 2018 the government took a more responsive attitude and launched a series of initial measures to soften some of the contested policies for example by cancelling the increase of the duty on diesel and increasing the legal minimum wage.
It became however quickly clear that the level of dissatisfaction was beyond repair by simple measures.

President Macron then took a courageous initiative by launching "Le Grand Débat National".
In an open letter to all compatriots of 15 January 2019 (see copy of the header below), he announced this big national debate organised on a local level, to address issues affecting the country and peoples' daily lives.

In clear language, he acknowledges the deep felt dissatisfaction and anger with the current state of play: for some groups taxes are too high, public services too distant, wages too low for a dignified living in a country which does not offer the same chances for everyone.


LE PRÉSIDENT DE LA RÉPUBLIQUE FRANÇAISE

Chères Françaises, Chers Français,
Mes chers compatriotes,

The agenda was set by the French government and turned around four big themes:

- Taxes, our public spending and public service
- Organisation of the State and public institutions
- Ecological transition
- Democracy and citizenship.

This Big National Debate has taken place in the first months of 2019 and has recently been concluded.
More than 10,000 meetings have been held throughout France. The President himself was actively involved in many local debates.

More than 1.5 million people have participated in the discussions throughout France and 1.9 million digital comments and contributions have been received!
It was foreseen that President Macron would present the conclusions the government has drawn on the 15th of April, the day that fire almost destroyed another French national symbol: the Notre Dame in Paris.

At the time of writing this commentary no new date has been set for Emmanuel Macron's Le Grand Débat National restitution. However some elements have been shared or leaked.
Prime Minster Édouard Philippe has already indicated that tax reform could be envisaged with a reduction of tax rates at the lower and middle-income levels. The indexation of state pensions is expected to be restored to the pre-reform system.
On political reform it seems that some form of direct democracy through referendum is foreseen but on local or regional issues and not on major national or international topics.

One cannot assume that the debate will be wrapped up and closed soon without further fierce political fights.
It would however be significant if the next stage is in Parliament and not on the streets of France. And then Emmanuel Macron will be everybody's hero!

What a difference would it have made if Theresa May's government would have taken a Macron-type approach on the Brexit debate instead of being stuck in a party political deadlock.

5. Do financial markets follow or anticipate or.... ?

Experience has shown that the relationship between the world economy and geo-political events and their effect on financial markets are far from straightforward.

The following chart developed by US asset manager Fisher Investments shows that global stock markets have seen a generally upward trend since 2009, regardless the many moments when major economic and financial events were expected to de-rail financial markets.

Exhibit 1: Global Stocks Rise Despite Slow Growth Worries

Source: Fisher Investments, 10 years of slow growth fears April 2019

It seems that relative pricing of assets was an important determinant in this development: monetary expansion kept interest rates extremely low and thus increased the attraction of risk assets such as equity and property to the levels we usually call inflationary "bubbles".
So as long as the major central banks continue to follow easy money policies (as also the Fed is now expected to do for the foreseeable future), the appetite for risk assets will continue.

There may be hic-ups on the way, for example around Brexit.
The chance of a cross party agreement is fading by the day and the likelihood of elections for the European Parliament in the UK growing.
Such elections may have grave effects on the major political parties but particularly for the currently governing Conservative Party. According to current opinion polls they could emerge from those elections with significantly reduced voters' support.
Such outcome may not be without impact on the national government level. The resulting political crisis may cause further major political chaos in the UK, threaten the governability of the country and have a shock effect on financial markets particularly in Europe.

If such events would be followed by the forecasted slowdown turning into even the mildest of a recession as Guggenheim recently predicted (see "*Forecasting the Next Recession*" of April 2019), the impact on financial markets could be severe, particularly in those assets classes where valuations are already very high.

With a generally good run in the first few months of 2019, investors may reduce their risks exposures faster than predicted and head for the hills of May (and come back in September…).

April 2019