A HAPPY NEW YEAR

If 2013 was remarkable for what did not happen rather than what did, should we expect shock waves of crisis in 2014? Rob Wood investigates

No crisis lasts for ever. After five years of hard slog following the financial car crash, results are now becoming visible. The fear factor is fading and monetary policy is working. This year could bring more welcome news on the world economy.

The backdrop to this rosy New Year message was a remarkable 2013. It was remarkable mostly because of things that did not happen rather than things that did.

Despite doom-mongers forecasting a eurozone break-up, it did not happen. The European Central Bank's (ECB's) promise to behave like a normal central bank – in other words, to act as a lender of last resort – continued to calm markets. A badly botched Cypriot bail-out did not rattle markets much. The eurozone has now returned to growth.

There was also little turmoil over the US Federal Reserve tapering its quantitative easing programme. The emerging market wobbles over the summer did not turn into a rout. In fact, they seem to have prepared markets for the actual Fed decision to taper.

The third mishap missing in action was a fiscal accident in the US. There was a lot of noise, hand-wringing and mud-slinging, but in October, the US agreed a budget and did not default on its debt. There was probably too much, and too indiscriminate, fiscal tightening, but the economy coped.

The one thing that did happen was that monetary policy got traction. Back in 2012, central banks were like cars stuck in the snow. Pressing the accelerator just left the wheels spinning and the car sliding backwards. The easing fear factor was like the snow melting. Policy got a grip.

The UK is a prime example of what can happen once paralysing uncertainty eases and the crippling credit crunch abates. The UK went from teetering on the edge of a triple-dip recession to expanding rapidly. Some 92% of large UK companies surveyed in a regular Deloitte report described uncertainty as above normal, high or very high in Q4 2012. That fell to 60% in Q4 2013.

The eurozone periphery is benefiting, too. In December, Spain posted a purchasing managers index figure of 54.2 for its services sector, stronger than in Germany. Meanwhile, Spanish unemployment fell by 108,000 in December, one of the biggest monthly declines on record. The reforms and hard slog of cutting labour costs are bearing fruit.

Growth is likely to take further hold in 2014 across Europe and the US. A lack of inflationary pressure will allow central banks to keep interest rates on hold until the spring of 2015. Fiscal drag will ease in the US and the eurozone.

The US and the UK will lead the eurozone. The damage that the severe recession inflicted on bank balance sheets, together with the uncertainty ahead of a new round of ECB stress tests in 2014, has caused a continuous credit crunch for SMEs in the periphery. But growth should gradually return to trend rates throughout this year.

There will be some emerging-market upsets in 2014, but a shock wave of crisis looks unlikely. China, the biggest emerging market, is not reliant on fickle hot money flows. In any case, why expect a crisis now if it did not happen in response to surging bond yields last year?

The main concern will now move from whether central banks can engineer growth to whether the costs are too high. Will they need to rein in the largesse before the real economy is back to health because of worrying asset bubbles? That is most obvious in the UK with the booming housing market.

For now, concern over costs is not a worry that will derail growth. Indeed, 2014 could be the sweet spot of the cycle where we benefit from low inflation, improving growth and central banks determined not to spoil the party.

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