REASONS TO BE CHEERFUL

THE GOOD TIMES ARE HERE – CAN THEY LAST?

Economies in the developed world seem to have finally recaptured some of their past vigour. After seven years of recovery, that had occasionally been punctured by the euro crisis, a hiccup in emerging markets, major gyrations in oil prices and political shocks on both sides of the Atlantic – think Trump and Brexit – households and companies are increasingly confident that the recovery will continue.

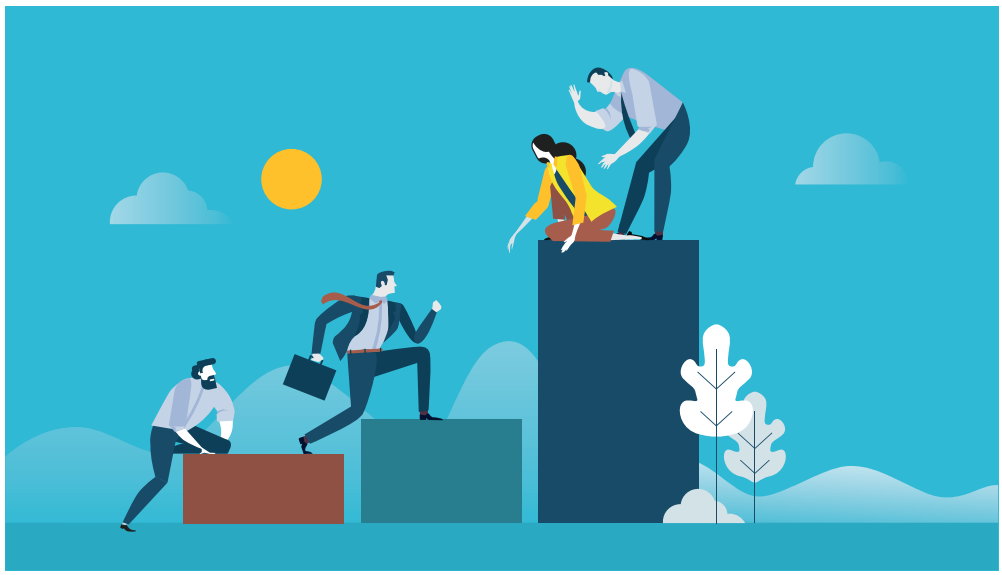
During 2016, growth in the advanced world accelerated to well above the averages of the previous years. Responding to healthy gains in private consumption and stronger export demand, businesses began to step up capital spending and hiring.

Slowly but surely, the post-Lehman age of caution is ebbing away, however, with 2017 probably marking the return to the more normal cyclical dynamics. With a strong end to the year for major advanced economies, the upswing looks set to sustain its healthy momentum in 2018.

One often reads that, after eight years of growth – around the normal business cycle length – a recession will *have* to come soon. While the economy often adheres to long-standing patterns and trends, which can be helpful guides, there are no hard and fast rules. Yes, a late-stage surge in demand is a little unusual. But then again, economic expansions do not simply die of old age.

The mere fact that we have not had a recession for a while is no reason to expect one imminently. If economies overinvest, raise too much inventory or run up too much debt, then a cleansing recession *is* needed to correct the excesses. But as households and companies, borrowers and investors still remain somewhat cautious, major economies are still far away from the excesses that could require a correction.

The most obvious sign of excess demand growth would be high levels of inflation. But this nasty beast is yet to rear its ugly head outside the Brexit-stricken UK. In the advanced world, firms are not yet overproducing or investing too much relative to demand. Meanwhile, credit growth remains modest relative to historical averages. For now, there are no major signs that we are heading for a bust. The good times can go on for a bit.



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As long as things don't get too hot, central banks will not spoil the party either. Because demand is likely to accelerate only gradually, firms should be able to lift supply quickly enough through investment, hiring and training, so that prices do not rise sharply. As the necessary balance-sheet repair from the pre-Lehman excesses is still incomplete, central banks will try to keep their economies off their leashes for as long as possible to avoid running the risk of choking off the upswing.

But, as always, there are some risks: first, that advanced economies are drawn into a major conflict either in the Middle East or East Asia; second, that China's growing debt troubles come to a head sooner rather than later; and third, that a misdirected and excessive US fiscal stimulus causes the US economy to overheat, bringing the global cycle to an early end. While we need to watch such risks carefully, we should attach only small probabilities to them for now.

Beginning in late 2016, financial markets started to rally as investors placed big bets that the global economy would gather momentum in the years ahead. They were right.

The key trends of 2017 look likely to carry into 2018. I wrote in this very column last year that, barring a major unexpected shock, the medium-term economic outlook was the most encouraging for a decade. The good news is that this statement is still true.

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