Washington Week Spring Meetings: Macro Resilience; Geopolitical Fragility

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Economics In The Back Seat

My "Washington Week" involved alternating between events at the International Monetary Fund (IMF), the Institute of International Finance (IIF), and the World Economic Forum. This included both attending and presenting on panels covering macroeconomic developments, the future of the Bretton Woods institutions, geopolitics, longevity, and central banking. I also had the opportunity to network, catch up with some old friends and colleagues, and get a sense of what is moving the needle for both the macro forecast and research themes.

This year's IMF and World Bank Spring Meetings were held under the shadow of escalating geopolitical risks. Iran's recent attack on Israel added to the list of armed conflicts, while U.S.-China tensions and global realignment more generally continued to simmer. In contrast, the message on economics was generally positive, reflecting ongoing U.S. outperformance and the bottoming of activity in Europe. All told, economic developments are still taking a backseat to geopolitics.

Main takeaways

A geopolitical fragmentation overlay for everything. There was no escaping geopolitics at the Spring Meetings; it was literally everywhere. In most discussions, mainstream economics based on the primacy of markets driven by agents maximizing efficiency is now seen as insufficient. Any potential gains from (free) trade are now subjugated to security arguments. Industrial policy--once anathema--is now practiced by governments, including the U.S. through the Inflation Reduction Act (IRA). Self-sufficiency in key sectors is seen as a good thing. Textbook economics is just plain old naïve; the message is that we economists need to return to our roots and become more multidisciplinary.

U.S. economic outperformance on full display. On the macro front, the main topic was analyzing the continued surprising resilience of the U.S. economy. On my IIF panel, we agreed that the recent jump in productivity was a prime driver--as was fiscal policy via the IRA--but we were not convinced that this was a solid trend given the paucity of data points. I heard a growing number of U.S. economists saying that the Federal Reserve will be on hold for longer, maybe throughout 2024. Everyone seems to agree that financial conditions are not very tight, despite relatively high policy rates. Moreover, a few U.S. economists are now thinking that the next Fed rate move may be up, not down.

China overcapacity rears its head (again). Economists were underwhelmed by the higher-than-expected first-quarter GDP growth numbers for China, which came in above consensus at 5.3%. The major focus was on the increasing imbalance in the Chinese economy, with ongoing weak consumption and growing overcapacity in the production of electric vehicles and solar panels. Government stimulus is makings this worse. Despite their high quality, there are fears that China will "dump" these low cost (subsidized) products onto foreign markets, wiping out local industries. Some economists saw this as only a sectoral issue, while others saw it as more of a macro issue. To put this in context, China's current account surplus is around 2% of GDP, well below the 10% peak in the 2000s.

Global public institutions trying to find their way. With the aforementioned ongoing fragmentation and the Washington Consensus in the rearview mirror, the post-World War II institutions are reexamining their role. Discussion included a call for another round of reforms to increase alignment and relevance. Calls for cooperation to solve global problems go less heeded in the new fragmented world. As far as we can tell, plurilateralism is alive and well with shifting groups of countries forming coalitions on a transactional basis to achieve their national objectives.

Next Steps

The tension between geopolitics and economics looks unlikely to resolve any time soon. And as long as it persists, we economists will need to wear our multidisciplinary hats. Indeed, S&P Global Ratings economists, working with our research colleagues in our flagship Credit Conditions Committee exercise, continue to identify geopolitical risks as being more likely to affect our baseline than economic risks. This is underscored by our recent report, "Global Credit Conditions Update: Geopolitical Risks Rise On Iran-Israel Conflict Expansion Despite Immediate Reprieve."

In terms of macro, the recent outperformance of the U.S. provides further evidence of the end of lower for longer rates. The investment boom surrounding the energy transition, fueled in part by the IRA and large fiscal spending, as well as the uptick in productivity, all point to higher for longer rates. This constitutes a decisive break from the past two decades.