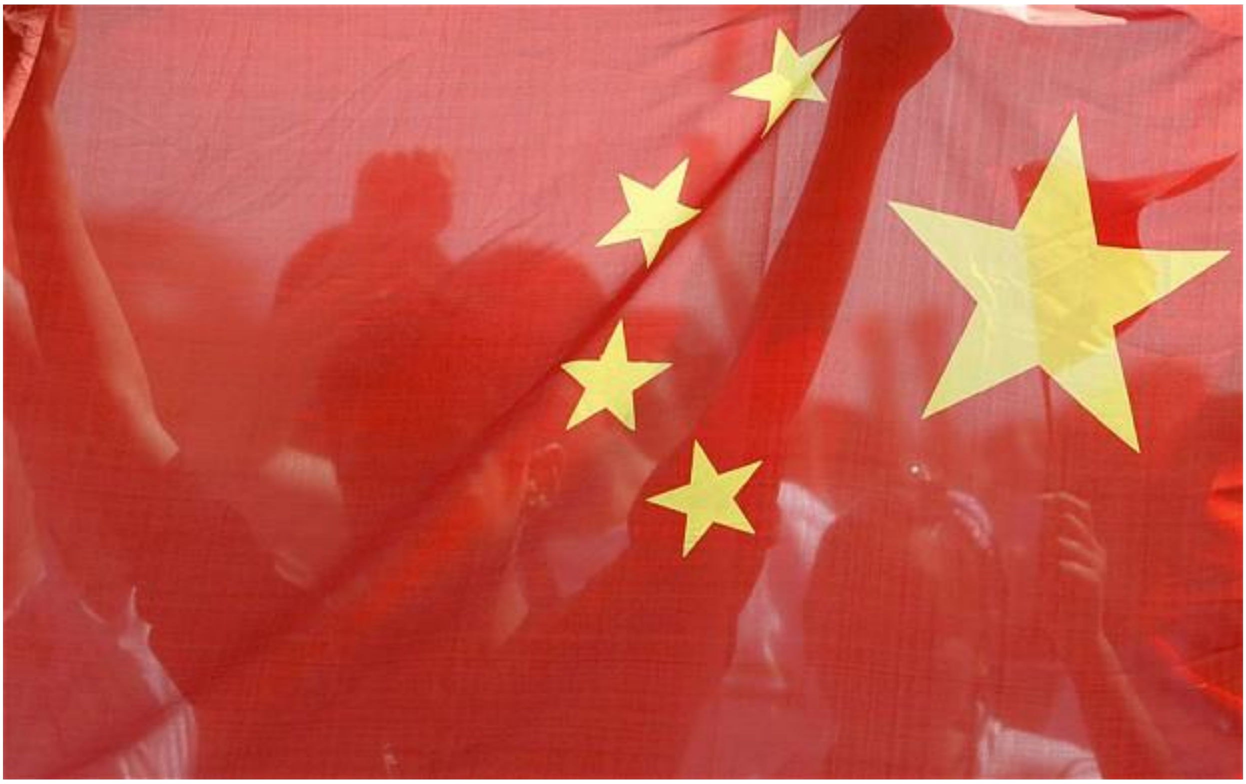
The Telegraph

Weak China and cheap oil do not a happy forecaster make

2016 was a year of surprises, with some particularly unexpected twists for the UK, says Roger Bootle



The Chinese are opening their first overseas military base in Djibouti Photo: Reuters

By Roger Bootle
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It's nearly that time of year again: the time to reflect and take stock of the year just passed. My excuse for getting in early is twofold: first, an impending holiday; second, the likelihood that nothing much will happen between now and December 31 to change the economic landscape.

This year has had its fair share of surprises, perhaps most importantly, the further falls in oil prices and continued softness of **other commodities**. Of course, the weakness of oil prices had begun before the start of the year, but the sheer extent of the fall since mid-2014 has caught almost all observers by surprise.

Even more surprising has been the apparently negative effect on the world economy. If you had told us two years ago, or even one year ago, that oil would fall below $40 a barrel, most economists would have said that this would be extremely bullish for the world economy. As it is, each new phase of oil and commodity price weakness seems to have led to stock market losses and renewed bearishness about the world economy.

In **various columns over the past year** I have tried to set out the reasons for this apparent paradox: the losses from lower oil prices were more concentrated than the gains, which are spread thinly throughout the world economy, and hence the immediate response of the losers has been stronger. Accordingly, the overall result across the world was a hit to both consumption and investment.

"Plenty of readers will surely say that the year's biggest surprise was closer to home, namely the election result"

But there is another reason that links up with this year's other big surprise – the **apparent weakness of the Chinese economy**. Each downward lurch of commodity prices was seen as confirming people's worst fears about China, and heralding weakness for the world economy as a whole.

This may be the first year in modern times that the rest of the world has been dominated by **events in China**. What was surprising about this was not the idea that the Chinese economy was slowing down, nor the revelation that China is now extremely important for the world economy, but rather the way that both commentators and investors latched on to the problems that had been obvious for some time and then worked themselves into a lather over August's weakness in the Chinese stock market. Yes, Chinese stock prices fell a long way; but in the preceding year they had risen a long way. Even after the big drops in prices, the stock market remains almost 20pc up over the previous year. So this was hardly a 1929-style crash.

I suppose financial markets need to have something big to worry about. This year saw the reappearance – and then temporary eclipse – of another subject thought likely to bring a crisis, namely the threat of a **Greek exit from the euro**. This appeared centre-stage briefly in June but then rushed off stage left, not to appear again. So, denied a real Greek crisis, the perma-bears latched on to the China threat.

In fact, they had more than China to get their teeth into. One major theme of 2015 was the comparative weakness of **emerging markets**. Apart from India, the Brics were a disaster zone, each for rather different reasons; other emerging markets also did relatively poorly. Africa experienced huge falls in growth and most of Latin America was very weak. By contrast, the developed economies held up well.

Although it was certainly not expanding at a breakneck pace, the US economy posted solid growth and strong job creation. US economic strength was not unexpected, but the long delay in the consequent rise in US interest rates was rather surprising. The reason was partly continued low inflation, due to the forces described above, but also a jitteriness about the world economy – especially China – and anxiety about the fragility of financial markets.

The year was also striking for the contrast between the US Fed moving to tighten monetary policy and the **European Central Bank** (ECB) loosening it. Accordingly, the year saw a surge in the dollar and an accompanying drop in the euro. Interestingly, the eurozone did not have a bad year. Indeed, as I had predicted, helped by low oil prices, it enjoyed one of its best years for ages. Mind you, this boost was not exactly home-grown. Europe gained from low oil prices and, thanks partly to the weak euro, the eurozone current account surplus continued to grow, representing the export elsewhere of unemployment and deflation.


David Cameron's election victory provides the perfect opportunity for the Conservatives to seize the political agenda and boost the case for capitalism Photo: Getty Images

Plenty of readers will surely say that the year's biggest surprise was closer to home, namely the **election of a Conservative government** with a clear majority. With some justification – although at least one commentator can claim to have foreseen this. (Modesty forbids me from being precise.) More importantly, so far at least, surprising or not, this election result does not appear to have had much economic effect. Admittedly, without it we would not be having a referendum on our EU membership, and this referendum, when it comes, could bring a result of overwhelming importance. This aside, we will have to wait for a few years yet before the economic data reflect any effects from the Conservative victory.

On the data we already have, the UK has been doing pretty well. I thought inflation would fall to very low levels but I suggested something like 0.5pc.

In the event, the rate dipped into negative territory and inflation will finish the year not far from zero. These low rates strengthened something that had seemed likely to me from some way off, namely the return to real earnings growth. This helped the UK to be the **fastest-growing country in the G7**. That is not exactly surprising; nor is it quite as good as it looks. Our external trade still performs badly. Although I suggested a year ago that the pound was overvalued and needed to fall, it is not exactly surprising that this hasn't yet happened.

Whether this prospect has receded or still lies in wait to surprise us in 2016 is a subject I will return to, but the soon not-to-be-kept resolutions are still burning bright.

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