Bank of Canada Urges You to Adapt: Slow Growth Is the “New Reality”

Description

The world is slowing–deal with it. At least that’s what Bank of Canada warned investors this week.

“We have to adapt to this new reality of lower potential growth. The faster we do this, the safer the financial system will be,” says Bank of Canada senior deputy governor Carolyn Wilkins. The central bank now believes that potential growth in global GDP has declined from a peak of 5% in 2005 to a sustainable rate of just 3%.

That’s resulted in trillions of dollars in lost wealth creation. “Natural by-products of slower potential growth are not only weaker corporate profits and dividends, but also a lower average rate of return on investments,” Wilkins added.

This month, **Deutsche Bank AG (USA)** (NYSE:DB) also released a report agreeing with the Bank of Canada’s findings. According to the report, the global economy is at an “inflection point,” potentially ending a long-term economic boom that started in the 1980s.

“We argue that we’re about to see a reshaping of the world order that has dictated economics, politics, policy and asset prices from around 1980 to the present day,” their report said.

They believe that the trends that have helped fuel world growth since the 1980s—namely globalization and demographics—are starting to deteriorate or even reverse. Wilkins agrees, saying that labour supply and productivity “are rising more slowly than in the past … contributing to the slowdown in global potential growth.”

“Extrapolation of the last 35 years will be one of the most dangerous things that policy makers and investors can do going forward,” Deutsche Bank’s report continues. “This will likely make the next 35 years very different from the last 35 years.”

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Policy makers and regulators will likely have their hands full managing a low-growth world.

“Slow growth worries me as a central banker, not only because it reduces our room to maneuver to achieve our inflation target. It also worries me because slower potential growth materially increases risks to financial stability,” Wilkins said.

She believes that investors typically link financial stability risks to unsustainably high growth, but “slower growth and lower returns can also add to vulnerabilities in the financial system.” She listed plenty of risks that have evolved due to the slow-growth environment, including sovereign debt crises, an oil-price shock, and the fallout from the Brexit.

“If there is one thing we have learned from the past decade, it is that imbalances can take a long timeto develop and even longer to resolve,” she added. Deutsche Bank was a bit more pessimistic. “A challenging few decades likely awaits us,” they wrote.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:DB (Deutsche Bank)

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