Don't mourn the passing of Ceefax and Minitel
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Opinion

Good news for 2012 – events won't shock us

Britain will suffer near recession and the eurozone will face break-up, but in a year's time we will be more cheerful

Anatole Kaletsky

Thank goodness it's over. Most people will remember 2011 as an intensely depressing and frustrating year. From the protesters now back in Tahrir Square to the deposed dictators of North Africa; from the Euro-federalists who thought that a single currency would blossom into friendship among the peoples of Europe, to the sceptics who counted the days to a euro break-up; from Nick Clegg, partaking of the bitter fruits of government, to Ed Miliband, who will never get to taste them, 2011 has been a year of disappointments.

Even the hedge-fund titans who boast of their ability to make fortunes whether markets are rising or falling have had a miserable year — with Wall Street, the dollar, the euro and the pound all ending the year almost exactly where they started.

After this catalogue of disappointments, it is hardly surprising that predictions of the year ahead are almost universally glum. Two thirds of Britons and Americans believe that their personal financial circumstances will decline. In Europe it is even worse.

The good news is that all the surveys and punditry round-ups that are traditional at this time of year have almost no predictive value. A year ago, economic forecasters were mostly optimistic, especially about the prospects for Britain.

None of the top geopolitical consultancies or intelligence agencies predicted the Arab Spring or the fall of Mubarak and Gaddafi or the replacement of the Greek and Italian prime ministers with the personal representatives of the German Chancellor.

Many did, on the other hand, predict an Israeli attack on Iran, another banking crisis in the US and Britain and a collapse of the US dollar, the Japanese bond market and British house prices, none of which occurred.

New year predictions are usually wrong not because pundits are stupid, but because politics and economics involve too many moving parts. The best we can do is analyse events as they unfold and draw some lessons from past forecasting failures.

What, then, might last year's errors tell us about the year ahead? A year ago, recovery was considered so well established in Britain that financial markets expected the Bank of England to start raising interest rates by May to rein in demand. Nobody, apart from Ed Balls, the Shadow Chancellor, seemed in the slightest bit worried about the impact of huge tax increases and public spending cuts on consumer spending and business investment.

The European Central Bank went one better, actually raising interest rates in February and April. On top of that, Germany demanded ever-larger fiscal contractions from the peripheral European nations.

> The US economy will continue to surprise us with its resilience

In China and most other emerging economies, interest rates were also raised aggressively from late 2010, but unlike Europe and Britain, these countries had good reasons for policy tightening since their economies were showing genuine signs of overheating. In America, by contrast, policymakers, investors and business leaders were much less confident about the outlook and totally unworried by the supposed inflationary pressures. The Federal Reserve Board continued to print large amounts of money until June, President Obama continued to plead with Congress for more stimulus and business lobbies continued to oppose proposals for higher taxes, regardless of the size of the budget deficit.

AP Photo/Kyodo News

The Japanese tsunami in March caused the world economy to slow down

In the event, conventional wisdom was wrong in its scepticism about America and its confidence in Britain and Europe. I challenged mainstream opinion when I pointed out that the British and US governments had set up a fascinating controlled experiment of a kind rarely possible in economics by imposing diametrically opposite budgetary policies on economies with virtually identical problems.

If Britain succeeded in slashing its deficits and recovering faster than America, where government borrowing remained unchecked, then George Osborne would have proved once and for all that Keynesian economics was bunk.

If, on the other hand, the US enjoyed decent growth in the years ahead, while Britain remained mired in recession, then what Keynes said in the 1930s would have been proved right: cutting public borrowing in the midst of a slump is counterproductive and incoherent, as every taxpayer and government employee is also a customer of private business.

Looking to 2012, this experiment provides one useful signpost amid the fog of uncertainties. It is now clear that the US economy is accelerating after the temporary slowdown caused by the oil shock that accompanied the Arab Spring and the Japanese tsunami; two genuinely unpredictable events of 2011.

Meanwhile, Britain's recovery has ground to a halt, while the eurozone is plunging into a deflationary black hole.

From this we can draw some conclusions for 2012. First, the US economy will continue to surprise by its resilience, that the US budget deficit will not be treated as a serious problem by investors and that President Obama will probably be re-elected, with the Democrats quite possibly regaining control of Congress.

Second, China, whose approach to macroeconomic management is much closer to the US than to the European model, will have another year of good growth and will not cause the shocks to the world economy that are widely feared in financial markets.

Third, Britain and the eurozone face another year of stagnation or outright recession. But there is a glimmer of good news. The outlook for Britain and the eurozone is probably no worse than investors and business leaders already recognise. Everyone now understands that Britain will suffer another recession or near recession, France will have its credit downgraded, Greece will default on its debts and the eurozone will either have to forge itself into a single nation or arrange an orderly break-up.

As events lose their capacity to surprise, their impact on business decisions also diminishes. If, as is fairly likely, Britain suffers nothing worse in 2012 than zero growth and the euro manages to avoid a chaotic break-up, probably by forcing the ECB to print piles of money, then the real surprises next year will come from the rest of the world, especially America and China, where conditions could turn out to be better than expected.

By this time next year, therefore, the world is likely to seem a rather more cheerful place. In short, the traditional wish for a prosperous new year might be less out of place than believed — unless, of course, something genuinely unexpected happens.