GLOBAL ECONOMY

CRISIL Insights

January 2018

The CRISIL Insights Global Economy series represents our outlook on the financial scenario across the world and provides a perspective into how it will shape up in the near future.

Tailwinds to fan stronger global recovery in 2018

- The United States (US) Fed raised its target range for policy rates by 25 basis points (bps) in December from 1.25% to 1.50%
- The People's Bank of China raised its repo rate by 5 bps to 2.5% for 7 days' and 2.8% for 28 days' agreements
- Global energy indices rose owing to higher crude oil and coal prices, while non-energy indices shed some heat with a fall in agriculture and fertilizer indices in December

In its January edition of the Global Economic Prospects report, the World Bank estimates the global economy to grow 3.1% in 2018, a tad higher than 3% (estimate) in 2017. Recovery in investment, manufacturing, and trade is seen as the major stimulant to growth this year. Growth in advanced economies is expected to moderate slightly to 2.2% from 2.3% (estimate), as central banks gradually tighten the easy monetary policy pursued following the global financial crisis. On the other hand, emerging markets and developing economies as a whole are projected to strengthen to 4.5% from 4.3% (estimate), as commodity exporting economies benefit from firming commodity prices.

Gross Domestic Product (GDP) Heat Map

GDP Growth (Q-o-Q SA annualised %)

	Q2-16	Q3-16	Q4-16	Q1-17	Q2-17	Q3-17
United States	2.2	2.8	1.8	1.2	3.1	3.2
United Kingdom#	0.5	0.5	0.7	0.3	0.3	0.4
Euro Area#	0.3	0.4	0.6	0.6	0.7	0.6
Japan	1.6	0.9	1.4	1.5	2.9	2.5
China*	6.7	6.7	6.8	6.9	6.9	6.8

Note: * y-o-y % #q-o-q, not annualized
Source: Statistical Bureau, Respective Countries

Improvement | Decline | Unchanged

US Economy

GDP growth estimate revised down for Q3

Eurozone Economy

EU and UK reach a deal on Brexit divorce terms

US Economy

Tax cuts boost US growth prospects

The US Bureau of Economic Analysis revised down gross domestic product (GDP) growth estimate for the third quarter (Q3) to 3.2% (earlier 3.3%). The downward revision was on account of a lower than estimated growth in personal consumption expenditure, partly offset by an upward revision in state and local government spending. Meanwhile, the US Congress passed the proposal to announce tax cuts worth ~$1.5 trillion spread over the next 10 years.

Current account deficit narrowed to $100.6 billion in Q3 from $110.3 billion a year ago, on account of an improvement in primary and secondary income receipts. Trade deficit, however, widened by $13.5 billion on-year to $134.4 billion in Q3. In November, the trade deficit widened to $50.5 billion compared with $46.4 billion a year ago, as imports (8.4%) grew slightly faster than exports (8.3%).

Annual Consumer Price Index (CPI)-linked inflation rose 2.2% in November, compared with 2% in October. Inflation was fueled by rising energy prices, with gasoline prices surging 16.5% on-year. However, core inflation (CPI excluding food and energy) moderated to 1.7% after a 1.8% increase in the preceding month.

Consumer Price Inflation (y-o-y%)

	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17
United States	1.6	1.7	1.9	2.2	2.0	2.2
United Kingdom	2.6	2.6	2.7	2.8	2.8	2.8
Euro Area	1.3	1.3	1.5	1.5	1.4	1.5
Japan	0.4	0.4	0.7	0.7	0.2	0.6
China	1.5	1.4	1.8	1.6	1.9	1.7

Source: Statistical Bureau, Respective Countries

Policy Interest Rate (End of Month %)

	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17	Dec-17
United States	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25	1.25-1.50
United Kingdom	0.25	0.25	0.25	0.25	0.50	0.50
Euro Area	0.0	0.0	0.0	0.0	0.0	0.0
Japan	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
China	4.35	4.35	4.35	4.35	4.35	4.35

Source: Central Banks, Respective Countries

Eurozone Economy

Unemployment rate falls to new low in EA

The euro area (EA) GDP grew 0.6% on-quarter in Q3, slightly below 0.7% for Q2. This was because the recovery in net exports was offset by slower growth in investment and household consumption expenditure. Goods trade surplus narrowed to €18.9 billion in October, compared with €19.2 billion a year ago, as imports rose faster (10.1%) than exports (8.8%). Annual CPI inflation was 1.5% in November, compared with 1.4% in October. The pick-up was led by a rise in fuel and food (dairy and eggs) prices. Core inflation (excluding energy, food, alcohol and tobacco) was 0.9%, unchanged from October. As per the preliminary estimate for December, inflation eased by 10 bps on-month to 1.4%, led by energy and food prices. The unemployment rate fell to 8.7% in November, down from 8.8% in October. This is the lowest unemployment rate recorded in EA since January 2009.

The European Union (EU) and the United Kingdom (UK) reached a deal on Brexit divorce terms, subject to legislative approval, which included a potential $54-60 billion payment from the UK to the EU. The UK economy grew at 0.4% on-quarter in Q3 2017, 10 bps higher each than the past two quarters. Services was the major contributor to GDP growth, while construction growth declined. Positive contribution from household spending also aided growth.

Japan Economy

Trade surplus narrows

China Economy

Annual CPI inflation increases with energy prices

Japan's employment and wages look up

Japan's Q3 GDP grew 2.5% on-quarter, 40 bps lower than the revised Q2 growth of 2.9%. While private consumption and government investment declined, an increase in private non-residential investment supported growth. S&P Global expects the economy to expand 1.6% in 2017 and 1.2% in 2018 and 2019 each.

Trade surplus narrowed to ¥112.2 billion in November, down from ¥146.5 billion a year ago, as imports rose faster (17.2% on-year) than exports (16.2%). Japan's employment and real monthly wages improved in November, raising expectation of a pick-up in private consumption. Unemployment rate was at 2.7% in November, compared with 2.8% in October. Annual CPI inflation was at 0.6% in November compared with 0.2% a month ago, led by an increase in energy prices. While CPI excluding fresh food stood at 0.9%, 30 bps higher than in October, core inflation (excluding food and energy) was 10 bps higher at 0.3%, led by rising medical care prices.

In its December meeting, the Bank of Japan kept its policy rate unchanged at minus 0.1%, and the target yield on 10-year Japanese government bonds at ~0%. It also stated that it would continue with its quantitative and qualitative monetary easing policy until CPI excluding fresh foods exceeded its 2% target.

People's Bank of China raises repo rate by 5 bps

China's GDP grew 6.8% on-year in Q3, 10 bps lower than the previous two quarters, reflecting a slowdown in real estate and construction activity. S&P Global expects the economy to grow 6.8% in 2017 and 6.5% in 2018, with excess credit growth posing as a downside risk. In December, China's official non-manufacturing Purchasing Managers' Index (PMI) continued to grow faster than manufacturing PMI, signaling a pick-up in construction activity. While the manufacturing PMI was 51.6% in December, down 20 bps on-month, the non-manufacturing PMI was 55%, up 20 bps.

November trade surplus narrowed to $40.2 billion, from $44.2 billion a year ago, as imports grew faster (17.7%) than exports (12.3%). Annual CPI inflation in December inched up to 1.8% from 1.7% in November led by a spike in fuel, healthcare, and housing prices. Producer Price Index (PPI)-linked inflation was 4.9% in December, compared with 5.8% in November, led by the prices for mining and quarrying industry, and raw materials industry.

While the People's Bank of China kept its benchmark lending rate unchanged at 4.35%, it raised its repo rate by 5 bps to 2.5% for 7 days' and 2.8% for 28 days' agreements, following the December Fed rate hike. It also raised interest rate for its one-year medium-term lending facility by 5 bps to 3.25%.

Energy prices gain, non-energy prices decline in December

As per the World Bank's pink sheet, energy prices gained for a sixth consecutive month in December rising 2.1% on-month, led by strengthening crude oil and coal prices. Brent crude rose to $64.4 per barrel (bbl) on average during the month, owing to the high level of compliance on production cuts by oil producing countries, which have agreed to continue cuts till end 2018. CRISIL Research expects crude prices to range $55-60/bbl in fiscal 2018, compared with $48.5/bbl in fiscal 2017.

Non-energy indices fell 0.4% led by a fall in agricultural and fertilizer indices. Agricultural index declined 0.7%, as the fall in beverages (-5.2%) and food indices (-0.9%) offset the rise in raw material prices (2%). Fertilizer index declined 5%, led by 11% drop in urea prices. Metals and minerals index gained 0.8%, led by 12.5% rise in iron ore prices. Precious metals index declined 1.9%, owing to a decline in gold prices (-1.4%).

Source: CRISIL Research

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Last updated: April 2016

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