Global Research
& Analytics

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GLOBAL ECONOMY

CRISIL Insights

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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.

Braving protectionist headwinds

- The real-time gross domestic product (GDP) tracker of the Atlanta Federal Reserve has signaled stronger-than-expected economic activity in the United States, and projected 4.8% growth for Q2
- In its June meeting, the European Central Bank (ECB) announced tapering of its asset purchase program with the last round to be undertaken from October to December
- China's trade surplus narrowed, as imports growth outpaced exports, posing a downside risk to growth
- Brent crude prices cooled on-month after the decision to increase output from July, averaging $74.4 per barrel

The escalation of trade tensions between the US and its major trading partners is running synchronous with the global financial tightening triggered by the unwinding of accommodative monetary policy by the central banks of some major advanced economies. These could have broader ramifications and sow the seeds of a noteworthy global growth slowdown. Even as the global trade is battered by protectionist sentiment and tariff wars, short-term indicators are signaling a revival in Q2 after growth slowed in Q1 in most advanced economies. Central banks of key advanced economies signaled the end of their accommodative monetary policy in the near future. While the US Fed raised its federal funds rate in June, the ECB announced tapering of its asset purchase program. Contrarily, the Bank of Japan is continuing with its monetary policy easing.

Gross Domestic Product (GDP) Heat Map

GDP growth (q-o-q SA annualized %)

	Q4-16	Q1-17	Q2-17	Q3-17	Q4-17	Q1-18
US	1.8	1.2	3.1	3.2	2.9	2.0
UK#	0.7	0.3	0.2	0.5	0.4	0.2
EA#	0.6	0.6	0.7	0.7	0.7	0.4
Japan	0.9	2.6	2.0	2.0	1.0	-0.6
China*	6.8	6.9	6.9	6.8	6.8	6.8

Note: * y-o-y %, #q-o-q, not annualized
Source: Statistical bureau, respective countries

Improvement | Decline | Unchanged

US Economy	Eurozone Economy
Labor market remains robust	Lowest employment rate recorded since Dec 2008

US Economy

US expected to post robust growth in Q2

The US is expected to post robust GDP growth[1] in Q2. The Atlanta Fed's real-time GDP tracker has projected Q2 growth at a solid 4.8%. This comes as a relief after Q1 growth moderated to 2% on-quarter (revised down from 2.2%) compared with 2.9% in Q4 2017, largely due to a slowdown in consumer and government spending.

The labor market continued to be robust, with the economy adding 213,000 non-farm jobs in June. However, the wage story remains unimpressive, with annual wage growth not being able to break out of the 2.5%-2.8% shackle. The wage growth is barely keeping up with Consumer Price Index (CPI)-based inflation, which has been consistently rising, reaching 2.8% in May, depicting the stress on real wage growth. The May CPI inflation was up 30 bps compared with April, led by a surge in energy prices. Core CPI inflation (CPI excluding food and energy) rose 10 bps to 2.2%, led by services inflation.

The dollar index gained for the six month in a row, appreciating 1.6% on-month on average in June. This was as investors rushed to invest in safe-haven dollar assets following the geopolitical uncertainties triggered by the Sino-US tariff war.

Consumer Price Inflation (y-o-y %)

	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18	May-18
US	2.1	2.1	2.2	2.4	2.5	2.8
UK	3.1	3.0	2.7	2.5	2.4	2.4
EA	1.4	1.3	1.1	1.3	1.3	1.9
Japan	1.0	1.4	1.5	1.1	0.6	0.7
China	1.8	1.5	2.9	2.1	1.8	1.8

Source: Statistical bureau, respective countries

Policy Interest Rate (End of Month %)

	Jan-18	Feb-18	Mar-18	Apr-18	May-18	Jun-18
US	1.25-1.50	1.25-1.50	1.50-1.75	1.50-1.75	1.50-1.75	1.75-2.00
UK	0.50	0.50	0.50	0.50	0.50	0.50
EA	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

Output gap is closing in the euro area

The euro area (EA) economic activity is slowing, suggesting the output gap is almost closed and economic expansion will meander going forward. In Q1, the GDP moderated to 0.4% on-quarter (not annualized), from 0.7% in Q4 2017. This was mainly due to a fall in exports coupled with flat government spending. The labor market remained robust in the region with the seasonally adjusted unemployment rate printing at 8.4% in May, the lowest rate recorded since December 2008.

The annual harmonized indices of consumer prices (HICP) came in at 1.9% in May, up from 1.3% in April, led by energy and services inflation. As per the Eurostat's flash estimate, inflation is expected to quicken to 2% in June and is expected to remain elevated as a result of soaring energy prices.

The United Kingdom's (UK) GDP was revised up to 0.2% (earlier 0.1%) on-quarter (not annualized) in Q1 2018, mainly due to a change in the methodology for measuring GDP. In May, the CPI inflation came in at 2.4%, stable compared with April, driven by rising energy prices. The pound weakened 1.4% on-month on average in June over a stronger dollar and due to a lack of substantial progress in the Brexit negotiations at the June 28-29 EU council.

[1] All growth numbers are seasonally adjusted and annualized, unless stated otherwise

Japan Economy

Household consumption expenditure contracts for the fourth straight month

China Economy

CPI inflation stable

Persisting weakness in consumer spending looms over Japan's growth prospects

Sluggish domestic demand and weak investment dragged down Japan's GDP growth to -0.6% on-quarter in Q1. The contraction follows eight consecutive quarters of expansion. Weakness in consumer spending has persisted in Q2 as well.

Japan's unemployment rate (seasonally adjusted) came in at 2.2% in May, lower compared with 2.5% in April. The real average monthly household consumption expenditure contracted 1.4% on-year in May, compared with a 1.3% fall in April. This marks the fourth month consecutive month of contraction. Annual CPI inflation eased to 0.7% in May, inching up from 0.6% in April, led by food inflation. CPI inflation excluding fresh food, the Bank of Japan's target inflation rate, was stable at 0.7% in May.

The Bank of Japan left its policy rate unchanged in June at -0.1%. It declared it would continue its quantitative and qualitative monetary easing with yield curve control until inflation reaches its 2% target. The yen weakened 0.4% on average on-month against the strengthening dollar in June.

China's trade surplus narrows

Q1 GDP growth for China printed a solid 6.8% on-year, unchanged from Q4 2017. The strong growth was supported by both the manufacturing and services sectors.

In June, although China's manufacturing sector Purchasing Managers' Index (PMI) remained above 50% (indicating economic expansion) in June, it slowed 40 bps on-month. Non-manufacturing PMI continued to rise for the fourth month in a row, up 10 bps on-month.

CPI inflation was stable at 1.8% in May largely due to a drop in food inflation. Meanwhile, producer price inflation edged up for second straight month to 4.1% in May from to 3.4% in April, lifted by a sharp rise in raw material and manufactured goods prices.

On the monetary policy front, the People's Bank of China maintained its benchmark lending rate at 4.35% even after the US Fed hiked its policy rates in June. The yuan weakened 1.5% on-month on average in May against a strong dollar.

Crude oil prices ease on-month in June

Energy prices eased in June, averaging $74.4 per barrel compared with $77 per barrel in May. Prices declined following the deal between the Organization of Petroleum-Exporting Countries and Russia to increase crude output from July in an attempt to balance the impact of falling production from Venezuela, Libya and Iran coupled with the continuous rise in US oil production.

However, strong demand in the US owing to the summer driving season taken with the output disruption in Venezuela, Nigeria and Libya, prevented prices from falling further. Also, the US asking all countries to stop oil imports from Iran by November supported prices from declining further. CRISIL Research expects crude at $68-73 per barrel in fiscal 2019, compared with $57.4 last fiscal.

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