

GLOBAL ECONOMY

CRISIL Insights

May 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.

Protectionism cloud over global growth

- Trade tensions between the United States (US) and China remained high in March-April. S&P Global estimates that the tariff spat would shave off 10 basis points from the US gross domestic product (GDP) in 2018 and 2019
- For the first time in 13 months, China posted a trade deficit in March of \$5 billion as exports fell while imports posted double-digit growth, reflecting strong domestic demand
- Shrinking inventories coupled with geopolitical uncertainties in oil-producing nations took crude prices beyond the psychological threshold of \$70 per barrel in April

The International Monetary Fund's (IMF) April update of the World Economic Outlook underlines the broad transnational revival in growth and expects the expansion to continue. What's notable is the IMF expects global growth to tick up to 3.9% in 2018 and 2019, supported by strong growth momentum in both, advanced economies and emerging market and developing economies (EMDEs). Advanced economies will likely continue expanding above their potential growth rate in the two years. Growth in EMDEs would firm up further with continued strong performance in emerging Asia and Europe and a modest upswing in commodity exports after three years of weak performance. However, the IMF flagged several downside risks to its forecast, which include protectionist sentiments that harm international trade, geopolitical tensions, and sharp tightening of global financial conditions.

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	2.3
UK [#]	0.7	0.3	0.2	0.5	0.4	0.1
EA [#]	0.6	0.6	0.7	0.7	0.7	0.4
Japan	1.1	1.9	2.4	2.4	1.6	N/A
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
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US Economy

Real GDP growth slows down

Eurozone Economy

Lowest unemployment rate recorded since Dec 2008

Trade tensions jeopardize US growth

The US real GDP growth for Q1 2018 was a slower 2.3% on-quarter, compared with 2.9% in Q4 2017. This was due to a slowdown in personal consumption expenditure, fixed investment and government spending, which were partially offset by an upturn in private inventory investment and net exports. Trade tensions between the US and China remained high during the month, especially with the two economies engaging in a tariff war and the Trump administration reportedly asking China to cut its trade deficit with the US by \$200 billion by the end of 2020.

The annual consumer price index-linked (CPI) inflation was 2.4% in March 2018, the highest level seen March 2017, led by a sharp spike in energy (7%) and shelter (3.3%) indices. Although acknowledging the pick-up in inflation and the slowdown in Q1 growth, the Fed kept interest rates unchanged at 1.50% to 1.75% in its May meeting, in line with market expectations. The dollar index gained a marginal 0.1% on-month on average in April as the 10-year US Treasury yields briefly touched the psychologically important 3%-mark for the first time in four years.

Consumer Price Inflation (y-o-y%)

	Oct-17	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18
US	2.0	2.2	2.1	2.1	2.2	2.4
UK	3.0	3.0	3.1	3.0	2.7	2.5
EA	1.4	1.5	1.4	1.3	1.1	1.3
Japan	0.2	0.6	1.0	1.4	1.5	1.1
China	1.9	1.7	1.8	1.5	2.9	2.1

Source: Statistical Bureau, Respective Countries

Policy Interest Rate (End of Month %)

	Nov-17	Dec-17	Jan-18	Feb-18	Mar-18	Apr-18
US	1.00-1.25	1.25-1.50	1.25-1.50	1.25-1.50	1.50-1.75	1.50-1.75
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

Growth moderates in Eurozone

The Eurozone or euro area (EA-19) GDP moderated to 0.4% on-quarter (not annualized) in Q1 2018, from 0.7% in Q4 2017. The seasonally adjusted unemployment rate was stable at 8.5% in March. This remains the lowest rate recorded in the EA-19 since December 2008. The annual harmonised indices of consumer prices (HICP) came in at 1.3% in March, up from 1.2% in February, led by an increase in services, food and energy indices. Given the recent pick-up in crude oil prices, the European Central Bank (ECB) expects the inflation to hover ~1.5% for the rest of the year. During its April meeting, the ECB maintained its main refinancing rate at 0% and signaled holding the rate steady for an extended period. The euro lost 0.5% on-month in April against the dollar on average as investors frowned upon the ECB's dovish stance. Divergent monetary policies of the ECB and the US Fed, coupled with uncertainties regarding the US fiscal deficit, have led to uncertainties around the path of the euro-dollar exchange rate.

The United Kingdom's (UK) GDP came in flat at 0.1% on-quarter (not annualized) in Q1 2018, the slowest growth since Q4 2012. The UK was dragged down by a decline in construction activity (fell 3.3%) and a slowdown in manufacturing (0.2% growth). The pound continued to strengthen in April, gaining 0.7% over the dollar. The CPI inflation, which is the target inflation rate of the Bank of England (BoE), also eased to 2.5% in March, down from 2.7% in February. In its May meeting, the BoE left policy rates unchanged at 0.5%.

Japan Economy

Policy rate unchanged in April

China Economy

CPI inflation eases

Japan's inflation dips in March, reversing a four-month uptrend

Japan finished 2017 stronger, with 1.7% GDP growth compared with 0.9% in 2016, driven by domestic demand.

Annual CPI inflation eased to 1.1% in March compared with 1.5% in February, breaking the four-month trend of a steady pick-up due to a decline in food inflation. CPI inflation excluding fresh food, the Bank of Japan's target inflation rate, also eased 10 bps on-month to 0.9%. Japan's central bank left its policy rate unchanged in April at -0.1%. It declared it would continue its quantitative and qualitative monetary easing with yield curve control until inflation reaches its 2% target, dousing market speculation on a rate hike.

The yen weakened 1.4% on average on-month against the dollar in April, as investors sentiment slumped after inflation declined in March. The inflation numbers erased the possibility of an unwinding of quantitative and qualitative monetary easing policy in the near future.

China continues on a strong growth trajectory

China's GDP grew 6.8% on-year in Q1 2018, unchanged from the previous quarter, as per the preliminary estimate. The strong growth was supported by both the manufacturing and services sector. According to China's official Purchasing Manager's Index (PMI), the manufacturing sector slowed on-month compared with the non-manufacturing sector in April. The manufacturing PMI was 51.4%, 10 bps lower on-month, while the non-manufacturing PMI was 54.8%, increasing 20 bps on-month.

Exports growth recovered (12.9%) in April, with trade surplus beating market expectations, after China has posted trade deficit in March for the first time since February 2017. Trade surplus narrowed to \$28.8 billion in April, compared with \$37.4 billion a year ago, as imports continued to grow at a solid 21.5%. CPI inflation eased to 2.1% in March compared with 2.9% in February as rising demand due to the Lunar New Year retreated. The People's Bank of China maintained its benchmark lending rate at 4.35%. The yuan gained 0.4% on-month on average in April against the dollar.

Crude oil prices cross \$70/bbl threshold in April

Both the energy and non-energy indices advanced in April, as per the World Bank's pink sheet.

The energy index gained 8.2% on-month in April, led by a 40% increase in US natural gas price. Crude oil prices also added pressure to the index, with the Brent crude oil price crossing the psychological threshold of \$70 per barrel (bbl) during the month. Brent crude prices averaged \$72.1/bbl in April, up from \$66/bbl a month ago, due to rising geopolitical concerns regarding US sanctions against Iran, and tensions between Iran and Saudi Arabia in Yemen. Another factor contributing to the price hike was strong oil demand and greater-than-expected compliance by the 22 oil-producing countries to their agreed production cuts which helped draw inventories down. CRISIL Research expects crude at \$68-\$73/bbl in fiscal 2019, compared with \$57.4/bbl in fiscal 2018.

The non-energy index gained 1.8% in April led by an increase in agriculture and metal indices. While agriculture index increased 1.7%, fertilizer fell 0.7%. The metal index gained 2.3%, led by an increase in aluminum and nickel prices. Precious metals indices were up 0.7% due to gains in gold prices.

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