Global Research
& Analytics

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GLOBAL ECONOMY

CRISIL Insights

November 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.

Slack after spurt

- The ongoing tariff war hit Q3 growth in the United States (US) and China as growth moderated on negative contributions from net exports
- Q3 growth weakened in the euro area (EA-19) to a four-year low, while it was the strongest in the past two years for the United Kingdom (UK)
- Crude prices averaged a four-year high of $81 per barrel in October

There's a wobble in global growth. Intensifying protectionism, the escalating trade war between the US and China, geopolitical tensions, uncertainty over Brexit, and tightening policy rates in the US are all taking a toll. And this list does not cover crude price dynamics. It's some way off from last year's talk of a synchronized global upswing.

Growth moderated in most global economies in Q3 of 2018, compared with Q2. The ongoing tariff war dented Q3 growth in both the US and China as net exports shaved off from overall gross domestic product (GDP) growth. The tariff war also squeezed growth in Japan, which was under pressure from a series of natural disasters. China posted its slowest growth since Q1 2009. Among other key advanced economies, while EA-19 clocked its weakest growth in Q3 since Q2 2014, the UK posted its strongest since Q4 2016.

Most major central banks held on to their policy rates. On the currency front, most currencies depreciated against the strengthening dollar. Concern surrounding Italy's fiscal deficit, a no-deal Brexit, and the slowing Chinese economy amid the US-China tariff war weighed on the euro, sterling pound and yuan, respectively. These factors also led to a pick-up in demand for high-yielding dollar-denominated safe-haven assets.

GDP Heat Map

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

	Q2-17	Q3-17	Q4-17	Q1-18	Q2-18	Q3-18
US	3.1	3.2	2.9	2.0	4.2	3.5
UK#	0.2	0.4	0.4	0.1	0.4	0.6
EA#	0.7	0.7	0.7	0.4	0.4	0.2
Japan	1.9	2.9	0.8	-1.1	3.0	-1.2
China*	6.9	6.8	6.8	6.8	6.7	6.5

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

Improvement | Decline | Unchanged

US Economy

Labor market was resilient in October with solid job gains

Euro Zone Economy

Unemployment rate continues to be stable

US Economy

Net exports and fixed investment drags down growth in US

The US real GDP growth[1] came in at 3.5% in Q3 2018, following 4.2% growth in Q2. Growth moderated due to negative contributions from exports and residential investment – the latter being a drag on growth through 2018. However, these were partially offset by positive contributions from consumer spending, business investment (inventories), and government outlays.

The labor market continued to be resilient in October, adding 250,000 non-farm jobs. Unemployment rate was steady at 3.7%.

CPI inflation had eased in September as energy prices fell during the month. The US Fed's preferred inflation metric – the private consumption expenditure deflator-based core inflation (excluding food and energy) – was at the Fed's target range of 2% for the fifth consecutive month.

In its November meeting, the Federal Open Market Committee kept its benchmark policy rates unchanged. The Fed also decided to continue rolling over the maturing Treasury securities and reinvest in agency mortgage-backed securities.

Consumer price inflation (y-o-y %)

	Apr-18	May-18	Jun-18	Jul-18	Aug-18	Sep-18
US	2.5	2.8	2.9	2.9	2.7	2.3
UK	2.4	2.4	2.4	2.5	2.7	2.4
EA	1.3	1.9	2.0	2.1	2.0	2.1
Japan	0.6	0.7	0.7	0.9	1.3	1.2
China	1.8	1.8	1.9	2.1	2.3	2.5

Source: Statistical bureau, respective countries

Policy interest rate (end of month %)

	May-18	Jun-18	Jul-18	Aug-18	Sep-18	Oct-18
US	1.50-1.75	1.75-2.00	1.75-2.00	1.75-2.00	2.00-2.25	2.00-2.25
UK	0.50	0.50	0.50	0.75	0.75	0.75
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 bank, respective countries

Euro Zone Economy

Growth momentum weakens in EA-19; strengthens in the UK

Q3 growth in EA-19 moderated to 0.2% on-quarter (not annualized), compared with 0.4% in Q2. The region's unemployment rate was stable on-month at 8.1% in September.

In its October meeting, the ECB maintained its main refinancing rate at 0%. During the meeting, ECB President Mario Draghi also highlighted the risks to financial stability from Italy's proposed higher fiscal deficit and a no-deal Brexit.

Separately, the European Commission rejected Italy's 2019 budget proposal. This had proposed a fiscal deficit of 2.4% of GDP, edging closer to the 3% limit set forth by the European Union under the Stability and Growth Pact. The commission stated the proposal flouted Italy's commitment to lower the deficit and did not guarantee a reduction in the country's debt.

The UK in Q3 posted its strongest GDP growth since Q4 2016. The 0.6% on-quarter growth (not annualized), compared with 0.4% in Q2, was broad-based, indicating a revival in manufacturing and construction. On the demand-side, net exports were a significant contributor to growth. In September, the CPI inflation eased to 2.4%, compared with 2.7% in August, driven by rising energy and services prices. On the non-standard monetary policy front, the Bank of England decided to maintain the stock of UK government bonds at £435 billion and that of corporate bonds at £10 billion.

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

Japan Economy

Annual CPI inflation down on easing of food inflation

China Economy

Manufacturing PMI at a 27 month low in October

Japan's growth contracts as exports and consumption slump

Japan's Q3 GDP growth contracted 1.2% on-quarter, compared with 3% expansion in Q2, weighed down by negative contributions from exports and private consumption. A series of natural disasters which disrupted production, coupled with declining demand for exports amid US's protectionist trade policy, hurt Q3 growth.

Japan's unemployment rate (seasonally adjusted) was 2.3% in September down from 2.4% in August. The real average monthly household consumption expenditure slipped to 0.5% on-year in September, compared with 2.8% in August.

Annual CPI inflation was 1.2% in September, 10 basis points (bps) lower from August, as food inflation eased. CPI inflation excluding fresh food, the Bank of Japan's target inflation rate, was 10 bps higher on-month at 1% driven by energy prices.

Net exports weigh on China's Q3 GDP growth

China's GDP growth moderated to 6.5% on-year in Q3, compared with 6.7% in Q2. Negative contribution from net exports weighed on growth, which offset the positive contribution from final consumption and private investment. Steady deleveraging of the corporate sector and the intensifying trade war with the US is also weighing on growth.

In October, both the official manufacturing and non-manufacturing Purchasing Managers' Index (PMI) declined on-month, although it continued to be expansionary. However, the non-manufacturing sector continued to grow faster than the manufacturing sector. Non-manufacturing PMI stood at 53.9, down 100 bps on-month, while manufacturing PMI was 60 bps lower on-month at 50.2% – the lowest since July 2016.

In September, CPI inflation picked up for the fourth straight month to 2.5% compared with 2.3% in August, driven by rising food prices. In contrast, the producer price inflation eased to 3.6% from 4.1% in August amid weakening demand.

Energy prices soar to a four-year high in October

Most commodity prices rose in October. The energy index increased 1.3% on-month, with Brent crude averaging $81 per barrel in October – the highest since October 2014. Oil prices rose on concerns of US-Iran sanctions, a steep decline in production from Venezuela, and unrest in Libya and the Middle East. However, crude prices have started to ease since late October, hovering at $72-74 per barrel on expanding inventories. In 2018 so far, oil prices have risen ~41% on average on-year.

The non-energy index picked up 1.2%. Meanwhile, the agriculture index inched up 0.6%, led by a 4.4% surge in the beverage index and 0.5% increase in food index, which was partially offset by a 0.8% decline in the raw material index. The metal index gained 2.5%, led by a 7.3% rise in iron ore prices. Precious metals rose 1.6%.

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Argentina | China | Hong Kong | **India** | Poland | Singapore | UK | USA | UAE

CRISIL Limited: CRISIL House, Central Avenue, Hiranandani Business Park, Powai, Mumbai – 400076. India
Phone: + 91 22 3342 3000 | Fax: + 91 22 3342 3001 | www.crisil.com

/company/crisil @CRISILLimited /CRISILLimited /user/CRISILLimited Follow us on @lifeatcrisil

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