Global Research & Analytics

CRISIL
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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.

Tariff war clouds darken

- Q2 growth in the United States (US) got a boost from the pick-up in exports as shipments were preponed to avoid tariffs
- Strong domestic demand and pick-up in capital spending propped up Japan's Q2 growth
- China's trade surplus narrowed in August on record high imports growth
- Brent crude oil prices eased cooled 2.4% on-month in August, following the deal between major oil exporting economies to increase crude oil output

Geopolitical headwinds battered the global economy, which stood firm in the face of tariff spats, currency fluctuations, and nervous investors. The second quarter (Q2) of 2018 reflected strong growth for most economies. Among the major advanced economies, the US and Japan posted solid Q2 growth, while euro zone recorded stable numbers. Among the emerging market economies, China continued with strong and steady growth, in line with its government's 6.5% growth target for 2018. Growth across these economies is largely supported by domestic demand.

However, threats lurk on the horizon, particularly with regard to global trade which has been sailing in choppy waters. The US-China trade war escalated in August, with the second round of the tit-for-tat tariff war kicking off on the 23rd despite trade negotiations between the nations. With this, $50 billion ($34 billion in the first round and $16 billion in the second) worth of each other's imports have been subjected to 25% tariff by both countries.

GDP Heat Map

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

	Q1-17	Q2-17	Q3-17	Q4-17	Q1-18	Q2-18
US	1.2	3.1	3.2	2.9	2.0	4.2
UK#	0.4	0.2	0.4	0.4	0.2	0.4
EA#	0.6	0.7	0.7	0.7	0.4	0.4
Japan	2.6	2.0	2.0	1.0	-0.6	3.0
China*	6.9	6.9	6.8	6.8	6.8	6.7

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

Improvement	Decline	Unchanged

US Economy

Unemployment rate remains steady

Euro Zone Economy

ECB maintains its main refinancing rate

US Economy

US economy to continue posting robust growth

The US GDP expanded at 4.1% on-quarter in Q2, up from the 2.2% growth[1] posted in Q1. This is the quickest growth since Q3 2018. Household spending and net exports pushed up US growth in Q2. Net exports contributed 100 bps because shipments of exports pulled forward to beat tariff imposition. The economy is expected to continue its solid growth momentum in Q3 as well, as per Atlanta Fed's real-time GDP tracker.

On the employment front, the US economy added 192,000 jobs, in line with the market consensus. The unemployment rate held steady at 3.9%. The annual average hourly earnings rate was up 2.9% on-year, finally breaking out of the 2.4%-2.8% range. Wage gains were steepest in the distribution sector (trucking) and other parts of the service industry with labour shortage.

The annual Consumer Price Index-linked (CPI) inflation was at 2.7% in July, stable compared with June, led by energy inflation, which rose 12.1% on-month. Private consumption expenditure deflator-based core inflation (excluding food and energy) was up 10 bps on-month, but at Fed's target range of 2% in July. Appetite for the greenback increased, causing the dollar index to gain 1.2% average on-month in August. This was on account of the anticipation of a steady Fed fund rate hike, especially after Fed Chair Jerome Powell's remark of following a gradual rate hike strategy at the Jackson Hole Economic Symposium, and the rising global uncertainties.

Consumer Price Inflation (y-o-y %)

	Feb-18	Mar-18	Apr-18	May-18	Jun-18	Jul-18
US	2.2	2.4	2.5	2.8	2.9	2.9
UK	2.7	2.5	2.4	2.4	2.4	2.5
EA	1.1	1.3	1.3	1.9	2.0	2.1
Japan	1.5	1.1	0.6	0.7	0.7	0.9
China	2.9	2.1	1.8	1.8	1.9	2.1

Source: Statistical bureau, respective countries

Policy Interest Rate (End of Month %)

	Mar-18	Apr-18	May-18	Jun-18	Jul-18	Aug-18
US	1.50-1.75	1.50-1.75	1.50-1.75	1.75-2.00	1.75-2.00	1.75-2.00
UK	0.50	0.50	0.50	0.50	0.50	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 banks, respective countries

Euro Zone Economy

Euro area posts stable growth in Q2

The euro area (EA) Q2 2018 GDP growth came in at 0.4% on-quarter (not annualized), stable compared with Q1, supported by acceleration in capital spending and private consumption, which was partly offset by negative contribution from net exports. Unemployment rate remained stable at 8.2% in July, the lowest recorded since November 2008. The annual harmonized indices of consumer prices came in at 2.1%, in July, up from 2% in June, led by a pick-up in energy. As per the Eurostat's flash estimate, inflation will likely ease back to 2% in August as energy prices cooled off a bit on-month. In its September meeting, the European Central Bank maintained its main refinancing rate at 0%. It confirmed the final round of the asset purchase program at a monthly pace of €15 billion would commence from October until December. The euro lost 1.2% average on-month in August against the dollar on concerns over the exposure of some European banks to Turkey's currency crisis.

The United Kingdom's (UK) Q2 GDP growth came in at a modest 0.4% on-quarter (not annualized), following weak Q1 growth of 0.2%. In July, the CPI inflation came in at 2.5%, up 10 bps on-month, driven by rising energy prices. The sterling pound fell 2.3% on average on-month, respectively, on growing concerns over a no-deal Brexit, i.e., the UK leaving the European Union on March 29, 2019, without a pact on their future relationship.

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

Japan Economy

Q2 growth supported by strong domestic demand

China Economy

PBoC revives counter-cyclical factor

Solid Q2 growth recovery for Japan

Japan's Q2 GDP growth was revised up to 3% on-quarter (earlier 1.9%), after contracting 0.6% in Q1, supported by strong domestic (private) demand and pick-up in capital spending.

Japan's unemployment rate (seasonally adjusted) was 2.5% in July, up from 2.4% in June. The real average monthly household consumption expenditure was up 0.4% on-year in July, after declining 1.2% in June, breaking a five-month contraction trajectory. Annual CPI inflation was at 0.9% in July, up 20 bps on-month, led by food and fuel inflation. CPI inflation excluding fresh food, the Bank of Japan's (BoJ) target inflation rate, was stable at 0.8%.

On the currency front, the yen appreciated 0.5% on average on-month in August against the dollar. This was as investors withdrew from risky emerging market currencies and scurried for safe haven assets amid the on-going US-China trade war and the Turkish crisis.

China's trade surplus continues to narrow in August

China's Q2 GDP growth was marginally lower at 6.7% on-year, compared with 6.8% in Q1, although in line with the government's 6.5% growth target for 2018. GDP growth remains strong despite evidence of steady deleveraging of the corporate sector and the intensifying trade war with the US. In August, China's non-manufacturing sector continued to advance at an improved pace while the manufacturing sector expanded at a slower pace on-month. The official non-manufacturing Purchasing Managers' Index (PMI) was at 54.2%, up 20 bps on-month, while the manufacturing PMI was 10 bps lower on-month at 51.3%. CPI inflation was at 2.1% in July compared with 1.9% in June, largely due to an uptick in fuel and healthcare inflation. China's trade surplus narrowed to $28.1 billion in July primarily due to a sharp rise in the import bill. Export growth remained strong amid a slowdown in shipments to the US and EU. Meanwhile, imports grew faster, largely due to a lower base. In August, the trade surplus narrowed further to $27.9 billion compared with $40.05 billion a year ago, below the market consensus. Imports jumped 20% on-year to a record high while exports rose at a softer 9.8%.CPI inflation picked up further to 2.3%, driven by surge in fuel and services inflation. Contrarily, the producer price inflation eased to 4.1% from 4.6% in July due to the lowering of mining and quarrying and raw material prices.

The Chinese yuan depreciated 1.9% on-month on concerns of the ongoing Sino-US tariff war and emerging market sell-off triggered by the Turkish crisis. To stem the sharp depreciation of the yuan and stabilize the currency market, the People's Bank of China (PBoC) revived a 'counter-cyclical factor' in its methodology for daily fixing of the yuan's midpoint. The PBoC maintained its benchmark lending rate at 4.35%.

Commodity prices mostly declined in August

According to the World Bank's pink sheet, prices of most commodities declined in August. Both energy and non-energy commodities fell 1.7% on-month.

Energy indices fell as crude prices eased in August, averaging $72.4 per barrel compared with $74.3 in July. Prices declined during the initial part of the month following the deal between the Organization of Petroleum-Exporting Countries (OPEC) and Russia. The deal was an agreement to increase crude output from July in an attempt to balance the impact of falling output from Venezuela, Libya and Iran. However, prices began to pick up and hover at ~$75 per barrel towards the end of the month on supply cuts from Saudi Arabia and rising US-Iran tension. CRISIL Research expects crude at $68-73 per barrel in fiscal 2019, compared with $57.4 last fiscal.

Non-energy indices were dragged down by agriculture and metals and minerals indices, which fell 1.8% and 2.1%, respectively. Precious metals weakened 3.2%.

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