Global Research
& Analytics

CRISIL
An S&P Global Company

GLOBAL ECONOMY

CRISIL Insights

October 2017

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.

A round of sanguinity

- Rise in gasoline prices pushed up inflation in the United States (US) in August as hurricane Harvey forced temporary closure of refineries
- S&P Global Ratings cut China's sovereign credit rating from AA- to A+ as risks from prolonged period of strong credit growth increased
- Crude oil prices surged to two-year high in September as global inventories shrank

Synchronized pick-up or a short-lived surge? Structural growth or a fragile uptick? The debate about the state of the global economy persists even as growth gathers momentum. The International Monetary Fund (IMF) in its October edition of the World Economic Outlook has upgraded its global growth forecast by 10 basis points (bps) to 3.6% for 2017 and 3.7% in 2018, compared with 3.2% in 2016. The IMF has cited a broad-based cyclical upswing in Europe, China, Japan, the US, and emerging Asia for the revision. Even then, caution abounds, with the IMF flagging the rapid tightening of financial conditions, protectionism, and geopolitical strife as risks. The IMF also stated the recovery is incomplete as growth remains low, especially in Latin America, the Middle East and Sub-Saharan Africa. Moreover, weak productivity growth, low inflation, and an ageing population pose as a long-term threat to the recovery of many economies. Thus, the jury is still out on whether this latest acceleration in global growth will endure.

Gross Domestic Product (GDP) Heat Map

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

	Q1-16	Q2-16	Q3-16	Q4-16	Q1-17	Q2-17
United States	0.6	2.2	2.8	1.8	1.2	3.1
United Kingdom#	0.2	0.6	0.5	0.7	0.2	0.3
Euro Area#	0.5	0.3	0.5	0.6	0.5	0.6
Japan	2.1	2.0	0.9	1.6	1.2	2.5
China*	6.7	6.7	6.7	6.8	6.9	6.9

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

Improvement | Decline | Unchanged

US Economy

Core CPI continues its upward trend

Eurozone Economy

Employment rate lowest since February 2009

US Economy

Hurricanes cause high inflation and job loss in US

The US economy recovered in the second quarter (Q2), growing 3.1% on-quarter compared with 1.2% - the fastest pace of expansion since Q1 2015. However, given the present government's legislative struggle to push through pro-growth policies promised by President Trump during his election campaign, there seems little in the offing to spur growth further. S&P Global has, thus, revised its growth forecast for 2017 down to 2.1% (earlier 2.2%). Further, S&P Global expects the economy to grow at 2.3% in 2018 and remain ~2% annually through 2020.

Current account deficit widened to 2.6% of gross domestic product (GDP) in Q2 compared with 2.4% in Q1. In September, there was a sharp decline in employment with a non-farm payroll job loss of 33,000, reflecting the impact of hurricanes Irma and Harvey. The annual consumer price index (CPI) rose 1.9% in August, as against 1.7% in July, due to a sharp rise in gasoline prices as hurricane Harvey forced a temporary closure of refineries. The core CPI, which excludes food and energy prices, rose 1.7% in August for the fourth straight month.

The Federal Open Market Committee (FOMC) kept the target range of the federal funds rate unchanged at 1-1.25% in its September meeting, but suggested an additional hike by year-end, followed by three more in 2018. The FOMC also confirmed a gradual reduction in the size of central bank's balance sheet starting October. The dollar index weakened an average 1.2% on-month in September as trade deficit widened and tension between the US and North Korea continued to escalate.

Consumer Price Inflation (y-o-y%)

	Mar-17	Apr-17	May-17	Jun-17	Jul-17	Aug-17
United States	2.4	2.2	1.9	1.6	1.7	1.9
United Kingdom	2.3	2.6	2.7	2.6	2.6	2.7
Euro Area	1.5	1.9	1.4	1.3	1.3	1.5
Japan	0.2	0.4	0.4	0.4	0.4	0.7
China	0.9	1.2	1.5	1.5	1.4	1.8

Source: Statistical Bureau, Respective Countries

Policy Interest Rate (End of Month %)

	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17
United States	0.75-1.00	0.75-1.00	1.00-1.25	1.00-1.25	1.00-1.25	1.00-1.25
United Kingdom	0.25	0.25	0.25	0.25	0.25	0.25
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

Growth and inflation firm up in euro area

Euro area (EA) GDP grew 0.6% on-quarter (not annualized) in Q2, compared with 0.5% in Q1. The unemployment rate in August was 9.1% for the third consecutive month, the lowest level since February 2009. Annual CPI inflation was at 1.5% in August, up from 1.3% in July, mainly reflecting an increase in fuel prices. In its September meeting, the European Central Bank (ECB) kept interest rates and its asset purchase program unchanged. The main refinancing rate, marginal lending rate, and deposit rate stood pat at 0.00%, 0.25%, and -0.40%, respectively. The ECB expects the rates to remain unchanged and intends to continue with its asset purchase program at €60 billion until December 2017, or beyond, if necessary. S&P Global expects the ECB to announce a slowdown in asset purchases from €60 billion to €40 billion a month in the first half of 2018 and wind down the asset purchase program completely in early 2019.

Contrary to the EA, the United Kingdom posted a lackluster 0.3% on-quarter (not annualized) growth in Q2, compared with 0.2% in Q1. Inflation rose to 2.7% in August compared with 2.6% in July, above the Bank of England's (BoE) target inflation rate of 2% as the prices of clothing and motor fuel surged. Despite the rise, the BoE kept its policy rates unchanged at 0.25% in September to help stimulate growth. However, the BoE signaled that it may consider tightening the monetary policy over the coming months should the inflation continue to rise in line with its August projections.

CRISIL
An S&P Global Company

Japan Economy

Core inflation rises

China Economy

S&P Global Ratings cuts China's credit rating

Japanese growth remains robust despite downward revision

Japan's GDP growth in Q2 was revised sharply downward to 2.5% on-quarter (previously estimated as 4%). Despite the downward revision, the growth, supported by strengthening private consumption and robust private and public investment, remains healthy, balanced, and above trend. Core inflation rose 0.2% with increases in the prices of education (0.4%) and clothes.

In addition, real average monthly household consumption expenditure increased 0.6% on-year in August as expenditure on transport and communication, and housing increased. In August, annual inflation was at 0.7%, compared with 0.4% in July, as energy prices shot up. Inflation has remained positive since October 2016. Core inflation rose 0.2% with increases in the prices of education (0.4%) and clothes.

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% in September, citing weakness in core inflation.

Ballooning credit growth threatens China's sovereign rating

China's GDP grew 6.9% in Q2, unchanged from Q1, mainly driven by robust consumption growth. As per the official Purchasing Managers' Index (PMI), the non-manufacturing sector (led by services) grew faster than the manufacturing sector in August. The manufacturing PMI was 52.4% in September, up 70 bps on-month and, while non-manufacturing PMI was 55.4%, up 200 bps. As a result, S&P Global revised up its growth forecast by 10 bps to 6.8% in 2017 and 6.4% in 2018. However, the excess credit growth, which could result in an abrupt growth slowdown, remains a risk. Despite monetary and regulatory tightening, credit growth continues to outpace nominal GDP growth. The total stock of non-financial sector debt, estimated at around 260% of GDP in the fourth quarter of 2016, is still expanding. Citing increased risks on account of prolonged period of strong credit growth, S&P Global Ratings has cut China's sovereign credit rating in September from AA- to A+.

The People's Bank of China (PBoC) kept its benchmark lending rate unchanged at 4.35%. However, the PBoC hinted it would reduce its reserve ratio requirement by 50 bps to 1.50% for banks that meet its requirements for lending to small business and the agricultural sector.

Commodity prices rise in September

As per the World Bank's pink sheet, prices of all commodities, except beverages, rose in September. While energy prices increased 5.4% on-month, non-energy prices rose 1.5%. Energy commodity shot up as oil prices surged. Brent crude prices averaged to a two-year high of $56.2/bbl in September (crude prices averaged to $56.6/bbl in July 2015). Hurricane Harvey impacted up to one-third of the US refinery capacity, resulting in a temporary spike in US gasoline prices. This, coupled with falling production in Libya and the Organization of Petroleum Exporting Countries (OPEC) and non-OPEC countries' decision to restrict their output to ~1.8 million bbl/day until March 2018, pushed up crude prices. CRISIL Research believes Brent will range at $50-$55/bbl in fiscal 2018, compared with $48.5 in fiscal 2017.

Non-energy commodity prices rose modestly. Agricultural prices climbed up to 1.4% led by strong upturns in most edible oils and wheat prices. The outlier to the trend of increases, beverage prices, fell 1% due to weakness in coffee prices. Fertilizer prices surged over 6.1%, led by a sharp rise in urea prices. Metals and minerals prices advanced 1.4%, led by an escalation in zinc prices. Prices of precious metals rose 2.4%.

Source: CRISIL Research

About CRISIL Limited

CRISIL is an agile and innovative, global analytics company driven by its mission of making markets function better. We are India's foremost provider of ratings, data, research, analytics and solutions. A strong track record of growth, culture of innovation and global footprint sets us apart. We have delivered independent opinions, actionable insights, and efficient solutions to over 100,000 customers.

We are majority owned by S&P Global Inc., a leading provider of transparent and independent ratings, benchmarks, analytics and data to the capital and commodity markets worldwide.

About CRISIL Global Research & Analytics (GR&A)

CRISIL Global Research & Analytics (GR&A) is the world's largest and top-ranked provider of high-end research, risk and analytics services. We are the world's largest provider of equity and fixed-income research support to banks and buy-side firms. We are also the foremost provider of end-to-end risk and analytics services that include quantitative support, front and middle office support, and regulatory and business process change management support to trading, risk management, regulatory and CFO functions at world's leading financial institutions. We also provide extensive support to banks in financial crime and compliance analytics. We are leaders in research support, and risk and analytics support, providing it to more than 75 global banks, 50 buy-side firms covering hedge funds, private equity, and asset management firms. Our research support enables coverage of over 3,300 stocks and 3,400 corporates and financial institutions globally. We support more than 15 bank holding companies in their regulatory requirements and submissions. We operate from 7 research centers in Argentina, China, India, and Poland, and across several time zones and languages.

CRISIL Privacy Notice

CRISIL respects your privacy. We use your contact information, such as your name, address, and email id, to fulfil your request and service your account and to provide you with additional information from CRISIL and other parts of S&P Global Inc. and its subsidiaries (collectively, the "Company") you may find of interest.
For further information, or to let us know your preferences with respect to receiving marketing materials, please visit http://www.crisil.com/privacy. You can view the Company's Customer Privacy at https://www.spglobal.com/privacy.

Last updated: April 2016

Disclaimer

CRISIL has taken due care and caution in preparing this report. Information has been obtained by CRISIL from sources which it considers reliable. However, CRISIL does not guarantee the accuracy, adequacy or completeness of any information, and is not responsible for any errors in transmission; and especially states that it has no financial liability whatsoever to the subscribers / users/ transmitters/ distributors of this report.