

GLOBAL ECONOMY

CRISIL Insights

December 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.

Growth's on the up, mostly

- United States (US) growth for third quarter (Q3) of 2017 revised up by 30 basis points (bps) to 3.3% on-quarter
- Revised growth numbers put Japan on a solid growth track with 2.9% on-quarter growth in Q2 and 2.5% in Q3 2017
- Service and construction activity picks up in China as indicated by the official non-manufacturing Purchasing Manager's Index (PMI), which grew 54.8% in November
- Brent crude prices rise to \$62.7 per barrel (bbl) on average in November, gaining 9.1% on-month

Good times seem to have finally returned, notwithstanding lingering risks to the world economy. According to the World Bank, global growth continued to be solid and broad-based in Q3 2017 at 3.4% on-quarter, despite the slight moderation from the previous quarter's particularly strong performance (3.6% on-quarter). Among the major economies, growth accelerated in the US and United Kingdom (UK) and moderated in the euro area (EA), China and Japan. Even more positive is that the World Bank expects the synchronized global recovery to continue in Q4.

Gross Domestic Product (GDP) Heat Map

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

	Q2-16	Q3-16	Q4-16	Q1-17	Q2-17	Q3-17
United States	2.2	2.8	1.8	1.2	3.1	3.3
United Kingdom#	0.5	0.4	0.6	0.3	0.3	0.4
Euro Area#	0.3	0.4	0.6	0.6	0.7	0.6
Japan	1.6	0.9	1.4	1.5	2.9	2.5
China*	6.7	6.7	6.8	6.9	6.9	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

FOMC maintains accommodative stance

Eurozone Economy

Inflation increases led by energy prices

Solid growth and employment data turns the spotlight back on US

The economy posted a three-year high of 3.3% on-quarter (earlier 3%) in Q3 2017, driven by personal consumption expenditure, private inventory investment, non-residential fixed investment, and net exports. While growth and employment remained solid, trade deficit widened in October to \$48.7 billion compared with \$43.1 billion a year ago as imports grew faster (7%) than exports (5.6%). Annual consumer price index (CPI)-linked inflation rose 2% in October, compared with 2.2% in September. Core inflation (CPI excluding food and energy) rose 1.8% after recording 1.7% increase in the preceding five months.

The Federal Open Market Committee (FOMC) in its December meeting raised the target range for federal funds rate by 25 bps to 1.25%-1.50%. The FOMC maintained its accommodative stance in order to support the strengthening labor market conditions and enable a sustained return to the target 2% inflation in the medium term. S&P Global expects the FOMC to raise the federal funds rate thrice in 2018 by 25 bps. Dollar index gained 0.2% on-month on average in November as investors cheered improving growth and employment. Appointment of Federal Reserve Governor Jerome Powell as the new chairperson of the US Fed and the unveiling of tax reforms by House Republicans in Washington also helped the greenback.

Consumer Price Inflation (y-o-y%)

	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17
United States	1.9	1.6	1.7	1.9	2.2	2.0
United Kingdom	2.7	2.6	2.6	2.7	2.8	2.8
Euro Area	1.4	1.3	1.3	1.5	1.5	1.4
Japan	0.4	0.4	0.4	0.7	0.7	0.2
China	1.5	1.5	1.4	1.8	1.6	1.9

Source: Statistical Bureau, Respective Countries

Policy Interest Rate (End of Month %)

	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17	Nov-17
United States	1.00-1.25	1.00-1.25	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	0.50
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

Growth moderates in EA, while UK growth shows resilience

EA gross domestic product (GDP) growth in Q3 was 0.6% on-quarter, slightly below 0.7% recorded in Q2. Trade surplus widened to €26.4 billion in September, compared with €24.3 billion a year ago, as exports rose faster (5.6%) than imports (5.1%). Annual CPI inflation was 1.4% in October, led by fuel and housing prices. Core inflation was 0.9%, slightly down from September's 1.1%, partly due to decline in services cost. As per the preliminary estimate for November, inflation increased by 10 bps on-month to 1.5%, reflecting rise in energy prices. In its December meeting, the European Central Bank (ECB) kept its main refinancing rate and interest rates on marginal lending and deposit facilities, unchanged at 0%, 0.25% and -0.4%, respectively. In addition, the ECB reiterated its intent to reduce the bond purchases from the current pace of €60 billion per month to €30 billion starting January 2018, and they would be extended until at least the end of September 2018. Euro depreciated 0.1% on-month on average in November, owing to stronger dollar and the failure of German Chancellor Angela Merkel to form a three-way coalition with the Free Democrats. Merkel's Christian Democrats currently is in coalition with the Christian Social Union party.

The UK economy grew at 0.4% on-quarter in Q3 2017, 10 bps higher than the previous two quarters. In October, the annual CPI inflation was at 2.8%, unchanged from September, led by increase in food and housing prices. The Bank of England (BoE) kept its key policy rate unchanged at 0.5% in its December meeting. It also stated that any future increases in the policy rate are expected to be at a gradual pace and to a limited extent. Earlier in November, the BoE had raised interest rates for the first time in a decade by 25 bps citing inflationary risk. In November, the sterling gained 0.2% against the US dollar on average as investors cheered the economy's resilience as seen in Q3 growth data.

Japan Economy

Unemployment rate stable

China Economy

Trade surplus narrows

Private investment supports solid growth for Japan

Japan's Q3 GDP growth data was revised up to 2.5% on-quarter (earlier 1.4%), 40 bps lower than the revised 2.9% (earlier 2.6%) growth posted in Q2. While private consumption and government investment declined, increase in private non-residential investment and net exports supported growth. S&P Global expects the economy to expand 1.6% in 2017 and 1.2% in 2018. S&P Global expects the economy to expand 1.6% in 2017 and 1.2% in 2018.

Trade surplus narrowed to ¥284.6 billion in October, down from ¥481.2 billion a year earlier as imports rose faster (18.9% on-year) than exports (14%). Unemployment rate was at 2.8%, stable since June 2017. Annual CPI inflation was at 0.2%, compared with 0.7% in September. Increase in energy prices were offset by a decline in food prices during the month. Core inflation (excluding food and energy) was also at 0.2%, same as a month ago. Core inflation was led by rising medical care prices. Since the Bank of Japan did not hold any monetary policy meeting in November, the key policy rate stayed unchanged at -0.1%, and the target yield on 10-year Japanese government bonds at ~0%. Yen appreciated 0.2% as investors piled in on expectations of strong earnings from Japan Inc.

PMI signals pick-up in service and construction activity in China

China's economy grew at 6.8% on-year in Q3 2017, 10 bps lower than the previous two quarters, reflecting a slowdown in real estate and construction activity. S&P Global expects the economy to grow 6.8% in 2017 and 6.5% in 2018, with the excess credit growth posing as a downside risk. In November, China's official non-manufacturing PMI continued to grow faster than manufacturing PMI, signaling an improvement in services and construction activity. While the manufacturing PMI was 51.8% in November, up 20 bps on-month, the non-manufacturing PMI was 54.8%, up 50 bps.

October trade surplus narrowed \$38.2 billion, down from a year-ago \$48.8 billion, as imports rose sharply (18.6%) as compared with exports (8.1%). Annual CPI inflation fell 1.7% in November compared with 1.9% in October, as a sharp rise in prices of fuel and healthcare was partially offset by a decline in food prices. Producer price indexed (PPI)-linked inflation was 5.8%, compared with 6.9%. Prices for mining and quarrying industry, and raw materials industry led the PPI inflation. The People's Bank of China kept its benchmark lending rate unchanged at 4.35%. Yuan gained an average 0.1% against the dollar on-month in November as the central bank intervened to increase the midpoint value of the fixed currency.

Energy prices crossed \$60/bbl in November

As per the World Bank's pink sheet, energy prices gained for a fifth consecutive month in November surging 7.7% on-month, led by strengthening oil prices. Brent crude rose to \$62.7/bbl on average, gaining 9.1% on-month due to the high level of compliance on production cuts by most oil producing countries. The anti-corruption purge by Saudi Arabia's crown prince through a series of high profile arrests has also caused a surge in oil prices. Going forward, most oil producing countries have agreed to extend their production cut until the end of 2018. Hence, CRISIL Research has revised up its Brent forecast to \$55-60/bbl (earlier \$50-55/bbl) in fiscal 2018, compared with \$48.5/bbl in fiscal 2017.

Non-energy prices grew marginally at 0.2%. Agriculture prices rose 0.4% as increase in food prices (0.8%) was offset by decline in beverages price (1%). Fertilizer prices declined 3%, led by a 6.5% drop in urea prices. Metal and mineral prices inched up at 0.1% as gains in nickel (5.6%) and iron ore (4.2%) prices were balanced by decline in lead (1.5%) and aluminum (1.6%) prices. Precious metals rose slightly by 0.2%.

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