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.

The helicopter's set to land

- Despite the disruptions caused by hurricanes Irma and Harvey, the United States (US) economy posted a solid 3% expansion in the third quarter (Q3) of 2017
- The Bank of England (BoE) hiked its policy rate by 25 basis points (bps) for the first time since 2007
- Slowdown in real estate and construction activity softened China's growth in Q3 2017 to 6.8% on-year
- Energy prices soared for fourth consecutive month in October, led by a rise in crude oil prices

Underwritten by the monetary stimulus of central banks and buttressed by government policies across the world, the global economy has quietly turned around. Q3 augured well for major economies, giving credence to the widespread conviction of an ongoing and sustainable global recovery. While growth moderated in the US, Euro area (EA), Japan and China to 3% on-quarter, 0.6% on-quarter, 1.4% on-quarter and 6.8% on-year, respectively, the United Kingdom (UK) posted a decent 0.4% on-quarter growth in Q3 2017. Potential pain points, real and imagined, remain, but central banks are moving towards unwinding of the quantitative and qualitative easing (QQE) program initiated post the global financial crisis. This may be the critical point in the growth story. Even as the US Fed has initiated its balance sheet normalization program and penciled another rate hike in December and three more in 2018, the BoE hiked its policy rate in November for the first time since 2007. The European Central Bank (ECB) has taken a softer stance by reducing the pace of its asset purchase program (starting January 2018), although extending the duration till September 2018. The Bank of Japan (BoJ), however, kept policy rates unchanged and continued with its QQE program, keeping the 10-year government bond yield at 0%.

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	3.0
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	2.0	0.9	1.6	1.0	2.6	1.4
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

US Economy

FOMC moves towards a tighter monetary policy

Eurozone Economy

ECB maintains accommodative stance

US Economy

US economy braves stormy weather

Despite battling the headwinds of Hurricanes Irma and Harvey, the US economy posted a solid 3% growth in Q3 2017. The economy weathered negative contributions from residential fixed investment and state and local government spending, which were offset by positive contributions from personal consumption expenditure, private inventory investment, federal government spending and net exports.

The economy witnessed 261,000 job gains (non-farm payroll) in October as employment in food services and drinking places, professional and business services, manufacturing, and healthcare increased. In addition, the Bureau of Labor Statistics corrected its September jobs gains to 18,000 from the previously reported job loss of 33,000.

Trade deficit widened in September to $43.5 billion compared with $38.5 billion a year ago as imports grew faster (6.1%) than exports (4.6%). Annual consumer price index (CPI)-linked inflation rose 2.2% in September, up from 1.9% in August. The pickup reflected a surge in gasoline prices after Hurricane Harvey disrupted production in several major refineries. However, core inflation (CPI excluding food and energy) stayed at 1.7% for the fourth consecutive month.

The Federal Open Market Committee (FOMC) kept the target range of the federal funds rate unchanged at 1-1.25% in its November meeting. S&P Global expects the FOMC to raise policy rates by 25 bps in December, given the solid gross domestic product (GDP) growth and favorable financial conditions, which outweigh concerns of soft inflation. In addition, S&P anticipates three more rate hikes of 25 bps each in 2018.

Consumer Price Inflation (y-o-y%)

	Apr-17	May-17	Jun-17	Jul-17	Aug-17	Sep-17
United States	2.2	1.9	1.6	1.7	1.9	2.2
United Kingdom	2.6	2.7	2.6	2.6	2.7	2.8
Euro Area	1.9	1.4	1.3	1.3	1.5	1.5
Japan	0.4	0.4	0.4	0.4	0.7	0.7
China	1.2	1.5	1.5	1.4	1.8	1.6

Source: Statistical Bureau, Respective Countries

Policy Interest Rate (End of Month %)

	May-17	Jun-17	Jul-17	Aug-17	Sep-17	Oct-17
United States	0.75-1.00	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	0.25
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

ECB slows QQE pace, BoE hikes policy rates

EA GDP posted a healthy 0.6% on-quarter growth in Q3 2017, slightly below 0.7% in Q2. Unemployment rate fell to 8.9% in September, the lowest unemployment rate since January 2009.

EA trade surplus narrowed €16.1 billion in August, compared with €17.5 billion a year ago. Exports grew 6.8% on-year, while imports rose 8.6%. Annual CPI inflation was 1.5% in September, the same as in August, led by rising prices of fuel. Core inflation was 1.1%, slightly down from 1.2% in August. As per the preliminary estimate for October, inflation slipped by 10 bps on-month to 1.4%, as a slowdown in energy costs offset a rise in food prices.

In its October meeting, the ECB kept its main refinancing rate and interest rates on marginal lending and deposit facilities, unchanged at 0%, 0.25% and -0.4%, respectively. It announced bond purchases will be reduced from the current pace of €60 billion per month to €30 billion starting January 2018, which would be extended until at least the end of September 2018.

In the UK, the BoE raised interest rates for the first time in a decade. At its November meeting, the BoE raised its benchmark interest rate by 25 bps to 0.5%. The move was aimed at restraining headline inflation, which rose above the BoE's 2% target. The economy grew at 0.4% on-quarter in Q3 2017, 10 bps higher than the last two quarters. While services continued to be the major largest contributor to GDP growth, it was a modest pick-up in manufacturing that helped growth compared with the past two quarters.

Japan Economy	China Economy
Q3 growth declines	Trade surplus down on sharp rise in imports

Japan continues easy monetary policy

Japan posted 1.4% growth in Q3, lower than 2.6% clocked in Q2. The decline in private consumption and government consumption weighed heavy on Q3 growth. However, these were offset by the positive contribution from private non-residential investment and net exports.

Trade surplus rose to ¥667.7 billion in September, up from ¥486.6 billion a year earlier. Exports increased 14.1% on-year, while imports rose 12.1%. In September, annual CPI inflation was at 0.7%, same as in August, led by increase in energy prices. Core inflation, however, continued to stay low at 0.2% as prices of housing and clothes and footwear fell. The BoJ kept its policy rate unchanged at minus 0.1%, and the target yield on 10-year Japanese government bonds at ~0% in its October meeting. It also announced it would continue its bond purchase program around the current pace of ¥80 trillion per annum to ensure the 10-year Japanese government bonds' yield remains at ~0%.

Growth softens 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. China's official Purchasing Managers' Index (PMI) indicated the non-manufacturing sector continued to grow faster than manufacturing sector in October. While the manufacturing PMI was 51.6% in October, down 80 bps on-month, the non-manufacturing PMI was 54.3%, down 110 bps.

The September trade surplus was $28.5 billion, down from $42 billion a year ago, as imports rose sharply (19.1%) compared with exports (7.5%). Annual CPI inflation rose 1.9% in October compared with 1.6% in September, owing to a sharp rise in prices of healthcare and housing. The People's Bank of China (PBoC) kept its benchmark lending rate unchanged at 4.35%. However, the PBoC hinted at reducing 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.

Energy prices pick up for fourth consecutive month

Energy prices increased for the fourth consecutive month in October by 3.3% on-month, led by strengthening oil prices. Brent crude prices rose to $57.5 per barrel on average, due to geopolitical tensions in Iran and Iraq coupled with high level of compliance on production cuts by members of the Organisation of Petroleum Exporting Countries. Agriculture prices edged lower during the month, due to a fall in food (0.1%) and raw material (2.5%) prices. Fertilizer prices climbed 4.9%, aided by a 12% jump in urea prices. Metals and mineral prices advanced a modest 0.9%, led by an uptick in lead (5.2%) and copper (3.5%) prices, offsetting a 13.8% plunge in iron ore prices. Precious metals prices dropped 2.7% as prices of gold (2.6%) and silver (2.8%) fell.

In Commodity Markets Outlook, October 2017, the World Bank forecasts energy prices to climb 4% in 2018 after a projected 23.7% leap in 2017. Non-energy prices are expected to gain marginally (0.6%) as a marginal pick-up in agricultural commodities would be offset by fall in prices of fertilizers and metals. Agricultural commodity prices are forecast to recede modestly (0.6%) in 2017 but largely stabilize (1.2%) in 2018. Metals prices are projected to ease slightly (0.7%) in 2018 following a 22.4% increase in 2017, partly due to a decline of iron ore prices. Precious metals prices are forecast to slip 0.2% in 2017, and further by 0.8% in 2018, as anticipated hikes in US federal funds rates materialize, bringing down prices of gold and silver.

Source: CRISIL Research

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