Managing risk, enabling trade

Economic Update

February 2018

Summary

Global

Real GDP growth forecasts

	2018	2019
World	3.2	2.9

Source: Oxford Economics

Global economic sweet spot

Global economic momentum is continuing to gather steam. After a 3.0% expansion in worldwide output in 2017, GDP is forecast to grow 3.2% in 2018. The global economy finds itself in a sweet spot of broad-based growth, improving labour markets, and still-loose financing conditions. Stronger external demand has led to upward revisions in GDP forecasts for a number of countries, including China. Furthermore, tax reform in the US will also stimulate higher economic activity there. The global economic upswing is forecast to continue into 2019.

Robust GDP growth is accompanied by a strong pickup in international trade flows. After a meagre 1.5% expansion in 2016, most recent figures show 4.3% trade growth in November 2017 (annual change in 12-month rolling average). Trade growth is additionally supported by an investment recovery in advanced economies and manufacturing output increases in Asia. In its January 2018 World Economic Outlook update the IMF revised its trade forecasts for 2018 and 2019 up to 4.6% and 4.4% respectively.

The price of oil has continued its upward trend which began in summer 2017, further supporting economic stabilisation and recoveries in many emerging markets. A barrel of Brent oil now fetches about USD 70, a level unseen since late 2014. Inventories have declined faster than expected due to surprisingly strong global oil demand growth. On the supply side the extension of OPEC's production cut deal until the end of 2018 and weather-related production disruptions created upward price pressure. Nevertheless, the resilience of US shale production is expected to keep prices moderate in 2018 and 2019, while geopolitical risks could cause upward shocks. The US Energy Information Administration forecasts further rising oil prices: from an average of USD 54.15 last year to USD 59.74 and USD 61.43 in 2017 and 2018 respectively.

Oil price

Daily spot price, USD per barrel Brent

Sources: Macrobond, Atradius Economic Research

Eurozone

Real GDP growth forecasts

	2018	2019
Austria	2.4	1.6
Belgium	1.6	1.5
France	2.1	1.7
Germany	2.4	1.8
Greece	2.5	2.2
Ireland	2.4	2.4
Italy	1.4	1.1
Netherlands	2.2	1.7
Portugal	2.2	1.9
Spain	2.9	2.4
Euro Area	2.2	1.8

Source: Oxford Economics

Eurozone growth reaches highest level in a decade

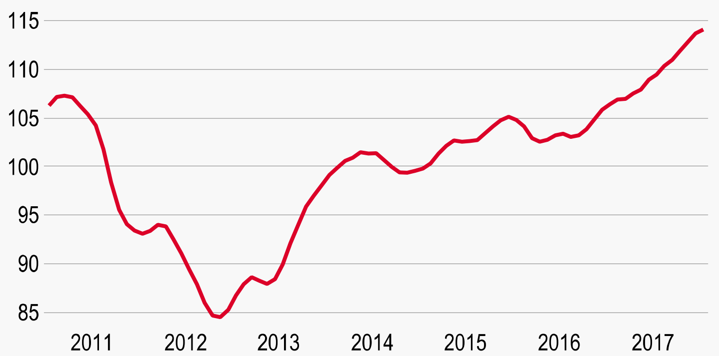
The cyclical upswing in the eurozone is hardly showing signs of abating. In Q4 of 2017 eurozone output expanded by 0.6% compared to Q3. This lifts the annual growth rate in 2017 to 2.5% - the highest since 2007. Going forward we expect GDP growth in the eurozone to remain strong. The European Sentiment Indicator (ESI) declined slightly in January 2018, but remains at a very high level of 114.7. Employment and nominal wage growth are expected to remain supportive for GDP growth, while inflation remains subdued. Investment should continue to grow at a moderate pace, although it remains somehow constrained, mainly due to legacy issues from the 2008 credit crisis and low productivity growth. However, export growth is expected to slow down in 2018, due to a strengthening of the euro. GDP growth in the eurozone is therefore likely to cool to 2.2% in 2018.

The stronger domestic situation reduces the vulnerability to external shocks. Political risk has receded since the landslide victory of Emmanuel Macron in France, but political issues remain a downside risk for 2018. Italy will hold parliamentary elections on March 4, and polls show a weakening popularity among the pro-European ruling socialist party versus more nationalistic parties, suggesting that political risk may increase ahead of the 2018 general election. Our baseline scenario remains that a centrist government will emerge, potentially a minority coalition, but the road up to such a coalition could be difficult.

At the end of January 2018 the euro broke the USD 1.25 mark for the first time in more than three years, after ECB president Draghi said he had grown more confident that inflation in the eurozone will approach its target. Nevertheless, given that the inflation is likely to remain below the ECB's 2% target for the forecast period, monetary policy will remain extremely loose for the foreseeable future.

Economic Sentiment Indicator - eurozone

Seasonally-adjusted, 3-month moving average



Sources: Macrobond, European Commission

Advanced Markets

Real GDP growth forecasts

	2018	2019
United Kingdom	1.5	1.6
United States	2.8	2.0

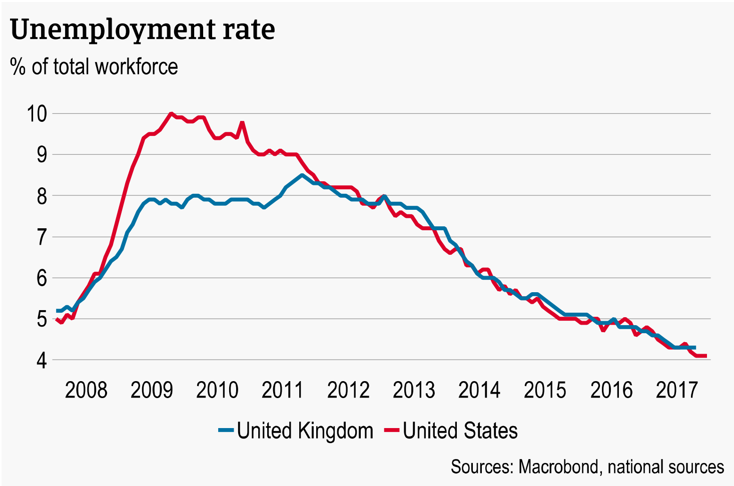
Source: Oxford Economics

US and UK outlook diverging

The US economy is estimated to have grown 2.3% in 2017, driven by consumer spending and business investment. This points to solid momentum going into 2018, supporting a 2.8% annual growth forecast. Unemployment is at a 16-year low, at 4.1%. The new tax plan is additionally contributing to the robust outlook and may push growth up even higher in 2018 to 2019. However, the sustainability of this strong growth is unexpected to last in the medium term due to the temporary nature of some of the stimulus measures, ongoing weakness in productivity and expected interest rate hikes.

In real effective terms, the US dollar has depreciated 6.8% year-on-year over 2017. This, combined with stronger economic growth and higher commodity prices is putting upward pressure on inflation, which stood at 2.1% year-on-year in December 2017. Inflation should pick up further in 2018 as base effects from unlimited cell phone data plans drop out. In this environment, the Federal Reserve has expressed a clear desire to raise interest rates at least three times in 2018.

The UK economy on the other hand is slowing down slightly – after a modest 1.8% expansion in 2017, growth is expected to ease to 1.5% this year. While unemployment is still at only 4.3%, inflation has increased to 3% and is expected to stay elevated in 2018, weighing on consumer purchasing power. The outlook remains stable but risks lean to the downside as uncertainty increases in the run-up to the UK's official departure from the EU in March 2019.



Emerging Markets

Real GDP growth forecasts

	2018	2019
Emerging Asia	5.8	5.5
Eastern Europe	2.8	2.4
Latin America	2.4	3.0
Emerging Markets	4.7	4.6

Source: Oxford Economics

Strengthening economic momentum for emerging markets

The economic momentum for emerging markets is strengthening, supported by higher trade growth and a surge in commodity prices, easier access to finance and better domestic policymaking in some major markets. Some of the largest markets (Russia, Brazil and Argentina) are emerging from recession, while many others benefit from the rebound in commodity prices. However, some risks remain. Financial markets have become more complacent for the time being, but a future tightening of global financial conditions could be adversely affect countries with high external liabilities (such as Turkey, South Africa, and Argentina).

Emerging Asia is expected to maintain its high growth rate in 2018, driven by steady growth in China as well as high growth in India. GDP growth in China has positively surprised in 2017, contributing to the stronger world economic outlook. Domestic demand, supported by policy easing and supply-side reforms alongside stronger external demand have pushed Chinese GDP growth to a predicted 6.8% in 2017. In 2018 growth is forecast to slow to 6.4% as authorities will take steps to rein in credit growth. India's GDP growth is likely to return to 7.5%, after growth was suppressed in 2017 due to economic reforms – the authorities' currency exchange initiative and the introduction of the country-wide Goods and Services Tax.

In Eastern Europe, the outlook for Russia has improved in line with the modest recovery in oil prices. In 2018 Russian GDP is expected to increase by 1.8%. However, structural weaknesses and the negative impact of sanctions on productivity and investment will continue to weigh on growth. While growth in the Central Eastern European markets remains underpinned by robust domestic performances in 2018, it is forecast to ease slightly without the catch-up in investment inflows that boosted the expansion last year.

After emerging from their recessions last year, 2018 growth is expected to increase further in Brazil and Argentina, forecast 2.5% and 3.6% respectively. This is pushing growth in Latin America to 2.4% this year. The slow recovery in Brazil reflects the ongoing weakness in domestic demand and increased political uncertainty due to corruption allegations involving major politicians. Mexico's economic outlook for 2018 has improved over the past couple of months, due to fading uncertainty over the potential fallout from US policy volatility and a resilient domestic performance.

Credit and insolvencies

Insolvency outlook remains benign for the time being

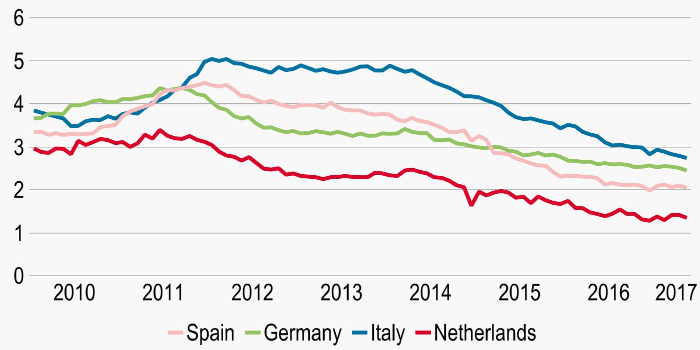
Following an estimated decrease of 3% in 2017, business insolvencies in advanced markets are forecast to decline 2% in 2018. The steady outlook is primarily supported by the surprising strength of the eurozone recovery. According to the ECB's Q4 bank lending survey, household and corporate lending has reach post-crisis heights. Banks in the euro area banks expect demand for loans of all types to grow in Q1 of 2018 and credit standard to continue easing. Lending growth is expected to hold up in 2018, supported by very low interest rates set by the ECB, but prospects that the ECB will withdraw stimulus are increasing. Across the eurozone insolvencies are forecast to decrease by almost 6% in 2018, led by the Netherlands (-4%), Portugal (-11%), and Italy (-5%).

In line with our forecasts, corporate insolvencies in the US fell 4% in 2017, supported by stronger domestic demand and high business confidence. This trend is expected to continue into 2018, but with historically low levels insolvencies are forecast to decline only 2% in 2018. There are some upside risks to this outlook, particularly the tax reform, as well as downside risks - mainly in form of a too hawkish monetary tightening. In the UK, corporate insolvencies are on an upward trend despite the economic resilience and high business confidence. Insolvencies rose 4% in 2017 and we expect them to increase another 4% in 2018, as GDP growth eases and inflation further squeezes household finances.

In emerging markets credit conditions are finally improving, in line with the stronger global economic recovery. According to the Institute of International Finance's EM bank lending survey, conditions went into easing territory for the first time since Q1 of 2013. The composite index increased by 1.5 points to 50.8 in Q3 of 2017 (50 is neutral). The index is also at its highest level since Q2 of 2011. Looking forward, conditions are expected to ease further, supporting a more benign insolvency outlook for emerging markets in 2018.

Corporate interest rates

Interest rates on short-term corporate loans, %



Sources: Macrobond, IMF

Macroeconomic indicators for key markets

	GDP growth (% of GDP)			Budget balance (% GDP)			Current account balance (% GDP)			Export growth (%)			Political risk Rating[1]
	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	
Western markets													
Austria	3.1	2.4	1.6	-1.2	-1.0	-0.9	2.2	1.0	1.0	5.8	3.8	3.1	2 POSITIVE
Belgium	1.7	1.6	1.5	-1.3	-1.5	-1.3	-0.5	-0.2	-0.2	4.9	4.1	3.3	2 STABLE
Finland	3.0	2.4	1.8	-1.1	-0.8	-0.4	-0.1	0.0	0.0	8.1	1.6	2.5	2 POSITIVE
France	1.9	2.1	1.7	-2.9	-2.8	-3.0	-1.0	-1.5	-1.5	2.8	4.0	3.4	2 STABLE
Germany	2.5	2.4	1.8	1.4	1.0	0.3	7.9	8.4	8.0	4.9	5.4	4.1	1
Greece	1.4	2.5	2.2	-0.3	0.4	0.8	-1.0	0.3	0.4	8.4	8.7	5.5	7 POSITIVE
Ireland	5.8	2.4	2.4	0.5	0.7	0.6	9.1	3.5	4.2	4.1	0.3	2.5	3 NEGATIVE
Italy	1.6	1.4	1.1	-2.1	-1.8	-1.4	2.6	2.1	1.8	5.2	4.1	3.5	4 STABLE
Netherlands	3.3	2.2	1.7	0.6	0.5	0.8	10.4	9.7	9.5	5.9	4.0	2.8	1
Portugal	2.7	2.2	1.9	-1.0	-1.2	-1.2	0.3	0.4	0.1	7.4	5.7	4.5	5 POSITIVE
Spain	3.1	2.9	2.4	-3.1	-2.3	-2.1	1.7	1.6	1.1	5.3	4.7	4.2	4 POSITIVE
Eurozone	2.4	2.2	1.8	-1.0	-0.8	-0.9	3.2	3.0	2.8	4.8	4.3	3.6	-
Australia	2.2	2.4	2.4	-1.6	-1.4	-1.4	-1.8	-1.6	-1.7	4.8	5.7	5.2	1
Canada	2.9	2.0	1.9	0.3	-0.6	-0.9	-3.1	-2.9	-2.5	1.0	2.7	4.1	1
Denmark	2.1	1.9	1.8	-0.4	0.0	0.0	8.0	7.0	6.5	3.8	2.4	1.6	1
Norway	2.3	2.5	2.1	2.4	1.1	0.7	6.3	6.6	5.7	2.6	4.3	2.8	1
Sweden	2.7	2.6	2.0	1.2	0.9	0.5	3.8	3.6	3.1	3.7	3.9	3.4	1
Switzerland	1.0	2.4	1.7	0.3	0.5	0.4	7.9	10.0	10.5	3.2	5.0	3.0	1
United Kingdom	1.8	1.5	1.6	-2.3	-1.9	-1.3	-4.5	-3.4	-2.6	6.3	3.7	3.3	2 STABLE
United States	2.3	2.8	2.0	-4.4	-4.9	-4.8	-2.4	-2.8	-3.0	3.3	3.7	3.0	1
Central and Eastern Europe													
Czech Republic	4.5	3.6	2.6	-0.1	0.0	-0.4	1.0	0.3	0.2	6.9	7.1	5.8	3 POSITIVE
Hungary	4.0	3.6	2.6	-2.0	-1.8	-1.8	3.8	3.2	2.6	7.1	6.1	3.8	4 NEGATIVE
Poland	4.4	3.8	3.3	-1.9	-1.7	-1.9	0.3	-0.2	-0.7	6.7	5.2	4.5	3 NEGATIVE
Russia	1.6	1.8	1.4	-1.8	-2.0	-1.5	2.6	4.5	4.2	5.0	4.5	2.5	5 NEGATIVE
Slovakia	3.4	3.2	2.8	-1.4	-1.3	-1.3	-1.6	-1.6	-1.7	3.2	4.5	4.5	3 POSITIVE
Turkey	6.9	3.9	3.1	-2.0	-2.2	-2.1	-5.1	-4.9	-4.3	11.3	3.4	1.6	5 STABLE
Asia													
China	6.8	6.4	6.0	-3.2	-3.0	-3.0	1.2	0.9	1.1	6.7	5.0	5.0	3 STABLE
India	6.2	7.5	7.0	-3.8	-3.1	-3.4	-1.5	-1.5	-1.0	3.7	4.8	6.6	4 NEGATIVE
Japan	1.8	1.7	0.9	-5.0	-5.5	-4.9	4.1	4.0	3.8	6.3	5.0	3.0	3 POSITIVE
Latin America													
Brazil	1.1	2.5	3.3	-8.6	-7.7	-6.3	-0.5	-1.1	-1.4	6.5	5.1	3.7	5 POSITIVE
Mexico	2.2	2.2	2.4	-1.5	-2.0	-2.0	-1.8	-1.9	-1.9	3.3	4.4	4.4	4 POSITIVE

[1] Note: STAR is Atradius' in-house political risk rating. The STAR rating runs on a scale from 1 to 10, where 1 represents the lowest risk and 10 the highest risk. In addition to the 10-point scale there are rating modifiers associated with each scale step: 'Positive', 'Stable', and 'Negative'. These rating modifiers allow further granularity and differentiate more finely between countries in terms of risk.

Sources: Oxford Economics, Atradius Economic Research

If you've found this economic update useful, why not visit our website www.atradius.com where you'll find many more Atradius publications focusing on the global economy, including country reports, industry analysis, advice on credit management and essays on current business issues.

Connect with Atradius on social media

Atradius
David Ricardostraat 1– 1066 JS Amsterdam
Postbus 8982 – 1006 JD Amsterdam
The Netherlands
Tel. 020 553 9111
info@atradius.com
www.atradius.com