Atradius
Managing risk, enabling trade

Economic Update

May 2018

Summary

Global

Real GDP growth forecasts

	2018	2019
World	3.2	3.0

Source: Oxford Economics

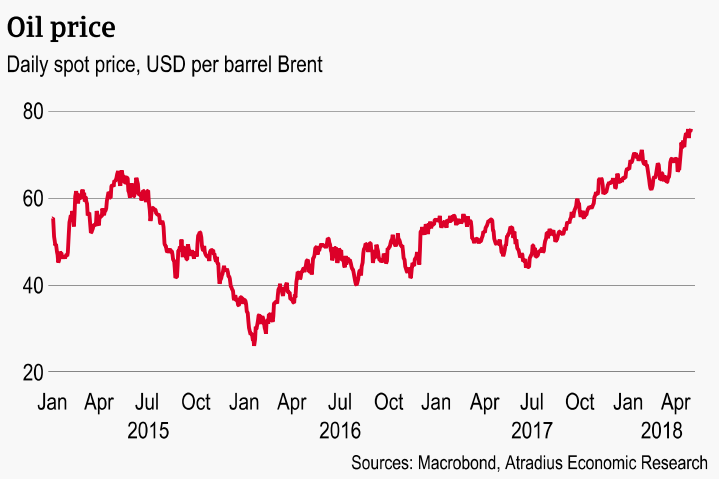
World economy is looking bright

Against the backdrop of a looming trade war, global GDP growth is still strengthening. 2017 marked a year of global economic growth acceleration of 0.6 percentage points, and 2018 promises to be another good year. GDP growth is expected to climb to 3.2% which would be the highest level since 2011. Demand is underpinned by favourable financing conditions, strong sentiment as well as US fiscal stimulus. A long-waited pick up of investment growth further pushes up trade growth.

Despite the strong cyclical momentum, there is an increasing amount of uncertainty that could negatively affect the forecast. The most prominent example is the protectionist stance taken by the US administration. Import tariffs have been announced on steel and aluminium. Even though the direct economic impact of the tariffs is likely to be limited, the uncertainty surrounding it could have a chilling effect on trade. Despite the rise in uncertainty, GDP growth is expected to decrease only slightly in 2019, to 3%.

The recovery of investment is accompanied by a strong pick-up in international trade flows. After a meagre 1.4% expansion in 2016, trade growth accelerated to 4.5% in 2017. The rebound was particularly strong in emerging economies, reflecting improved investment in formerly stressed commodities exporters. Advanced economies benefited from improvements in investment and domestic demand more generally. In its April 2018 World Economic Outlook update the IMF revised its trade growth forecasts for 2018 and 2019 up to 5.1% and 4.7% respectively.

Oil prices have increased above USD 70 per barrel, but are generally expected to stay within a range of USD 60 to USD 70. The lower boundary is set by an ongoing OPEC commitment to cap production and increasing tensions in the Middle East, while the upper boundary is set by increasing non-OPEC production, particularly US shale output. Oil prices are expected to stay in this range in 2018: the US Energy Information Administration expects oil to average USD 63.36 this year, up from USD 54.15.



Eurozone

Real GDP growth forecasts

	2018	2019
Austria	2.5	1.6
Belgium	1.6	1.7
France	2.1	1.9
Germany	2.3	1.8
Greece	1.6	2.7
Ireland	4.9	2.2
Italy	1.5	1.1
Netherlands	2.5	1.7
Portugal	2.2	1.9
Spain	2.9	2.4
Euro Area	2.2	1.8

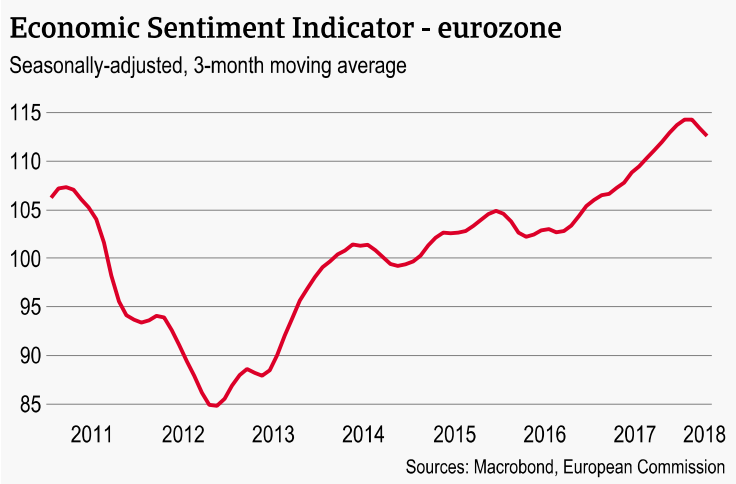
Source: Oxford Economics

Eurozone growth cycle reaching an inflexion point

With a 2.5% expansion in 2017, the eurozone economy experienced its strongest year since 2007. While robust performance is expected to continue in 2018, recent developments in sentiment indicators and slower economic growth in Q1 of 2018 suggest that the growth cycle is nearing its peak. Quarterly economic growth slowed to 0.4% in Q1 of 2018, down from 0.7% in Q4 of 2017. However, Eurozone growth is forecast to decrease only slightly this year, to 2.2%. Employment and nominal wage growth are expected to remain supportive of economic expansion. Investment is expected to accelerate this year to its highest growth rate since 2007, supported by increasing utilization rates and benign monetary conditions. Exports are forecast to expand by 5% this year, sustaining the momentum of last year. Exports benefit from a cyclical recovery in global trade, while the appreciation of the euro is slowly turning into a headwind.

There remain important risks that could throw sand in the wheels of growth. Political risk remains an issue in Italy, with no clear expectation which parties will form a government. The return of protectionism is another risk, recently exemplified by the US announcement to impose tariffs on steel and aluminium imports. It remains to be seen if the EU will gain a permanent exemption, but even if it would fall subject to the steel and aluminium tariffs, the immediate economic impact is likely to be limited. Nevertheless, the uncertainty created by the return to protectionism could have a chilling effect on trade.

ECB president Draghi stated that he is more confident that inflation in the eurozone is on the right track. Nevertheless, inflation and core inflation (excluding food and energy) fail to come close to the ECB's target of 2%. In March inflation was 1.3%, while core inflation stood at 1%, and inflation is likely to remain below 2% for the forecast period. Therefore, the ECB is committed to give ample degree of monetary stimulus, meaning that financing conditions for businesses are likely to remain benign.



Advanced Markets

Real GDP growth forecasts

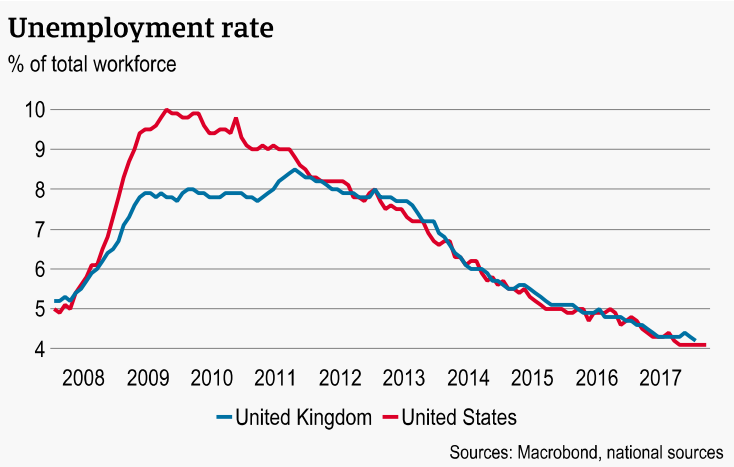
	2018	2019
United Kingdom	1.7	1.7
United States	2.8	2.4

Source: Oxford Economics

US outlook strong while UK economy falters

The US economy is now, as of May, in its second-longest economic expansion on record: eight years and ten months. The expansion has generally been steady but unspectacular so far, but is set to pick up in 2018. The Q1 of 2018 GDP growth figure, while slowing to 2.3% y-o-y from 2.9% y-o-y in Q4 of 2017, was above consensus expectations, and is expected to even be revised up. This is due to the fact that the effects of the tax cuts were only beginning to be felt in March, which is not yet well accounted for in the first quarterly estimates. The announcement of tax reform and higher government spending has been accompanied by higher business confidence and strong growth in non-residential fixed investment. Momentum is expected to continue gathering in the remaining quarters, pushing annual GDP growth up to 2.8%. At this point the late-stage stimulus does not seem to overheat the economy. The labor market is tight, but there is still room for further tightening: with unemployment steady for the past five months at 4.1%, the participation rate has dipped slightly to 62.9%, and wage growth continues to accelerate only modestly (up 2.7%). Personal Consumption Expenditure (PCE) inflation, excluding food and energy, picked up to 1.9% in March from 1.6% in February, bringing inflation closer to the Fed's target. Inflation is expected to reach 2.1% in Q4 of 2018, and this stronger, but not overheating, inflation outlook supports the Fed's current tightening path – with three additional 25 basis points rate hikes expected this year.

After a surge in manufacturing output in Q4 of 2017, the UK economy recorded a robust GDP growth of 1.8% in 2017. However, this momentum did not continue into Q1 of 2018: preliminary estimates show a mere 0.1% q-o-q growth rate, the weakest quarterly expansion since early 2012. Adverse weather conditions and a sharp contraction in construction output were behind the slowdown, but other data points to potentially more structural issues. Consumer borrowing slowed to its lowest pace in more than five years and the latest manufacturing PMI dipped to a 17-month low. This could cause a downward revision in the steady 1.7% GDP growth forecast for 2018.



Emerging Markets

Real GDP growth forecasts

	2018	2019
Emerging Asia	5.8	5.5
Eastern Europe	3.0	2.5
Latin America	2.0	2.9
Emerging Markets	4.6	4.6

Source: Oxford Economics

Emerging market outlook remains robust

Emerging market economies (EME) as a whole are forecast to grow 4.6% in 2018, a mild acceleration from the 4.5% expansion recorded in 2017. Growth is supported by the global economic upswing, boosting external demand, easing financial conditions, improving domestic policymaking in some markets, and higher commodity prices. However, at the same time risks to the outlook have substantially increased. On top of tightening US monetary policy, a potential Sino-American trade war could have severe negative effects for those with high export dependence on either market. The ongoing slowdown in China (to 6.4% growth this year from 6.9% last year) is also problematic, especially for smaller Asian markets dependent on exports to China. China's rising influence through investments in EMEs, especially in Emerging Asia and Sub-Saharan Africa contributes to increasing debt levels and opposition in some countries.

Growth will be highest again in Emerging Asia with 5.8%, marking a mild slowdown from a 6.0% increase in 2017. As Chinese authorities take measures to rein in credit growth, bringing down annual GDP slightly, India will become Asia-Pacific's fastest growing economy, with a 7.3% expansion expected in 2018. Strong domestic demand and supportive macroeconomic policies are boosting growth as well as capital inflows.

Latin America is forecast to see a strong increase in annual GDP growth to 2.0%, from 1.1% last year. The recovery is underpinned by strengthening domestic demand and a supportive external environment. Brazil, the region's largest economy, is steadily emerging from recession with 2.4% growth forecast in 2018. The region is generally well-positioned to deal with external shocks coming from global trade disruption and/or faster US monetary tightening.

Eastern Europe is enjoying stable economic growth of 3%, but individual country growth rates are very diverse. Russia is only slowly recovering from recession, with growth set to pick up to 1.8% from 1.6% last year. Higher geopolitical risk could weigh on the recovery as tensions with the West have increased, mainly due to the conflict in Syria. Growth in export-oriented EU member states will stay strong, supported by external demand and high investment. After a credit-fuelled surge in Turkish GDP growth to 7.4% in 2017, growth is cooling down to a still strong 4.2%. Underlying vulnerabilities are dragging on economic expansion, especially exchange rate volatility, high corporate debt, and geopolitical risk.

Credit and insolvencies

Insolvency outlook remains benign for the time being

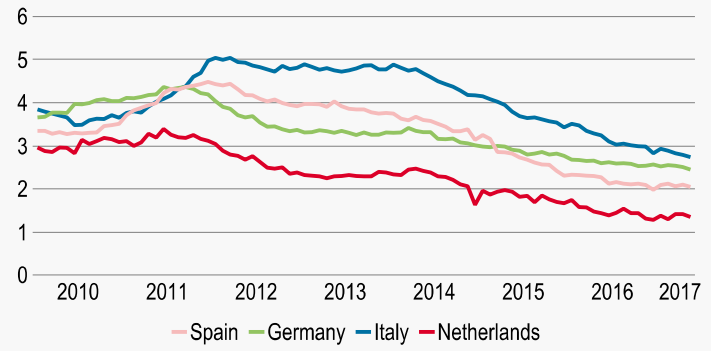
The insolvency outlook has improved in Q1 of 2018, in line with the strong economic outlook, underpinning another 4% projected decline in global insolvencies. Business conditions in the eurozone remain favourable. Credit conditions for enterprises have continued to ease in Q1 of 2018 and demand for loans is increasing, according to the ECB's most recent bank lending survey. Banks expect this trend to continue in Q2. Accommodative financing conditions next to the broad-based economic growth in the eurozone should support firms this year, but some may suffer from a stronger euro. Portugal (-14%), Greece (-10%), and Italy (-10%) are expected to see the strongest year-on-year insolvency improvements. The Netherlands is forecast to see an 8% decline and Spain a 6% decrease.

The insolvency outlook for the US is revised slightly lower to a 3% decrease despite the fiscal stimulus. Easy financing conditions, high domestic demand, increasing business confidence and investment are all supporting the bankruptcy outlook. With insolvencies at 80% of their 2007 level and the economy getting very late in its business cycle, we expect the downward trend in insolvencies to begin easing this year. However, high corporate debt is a major downside risk as the Fed accelerates its tightening cycle over the year and beyond. The UK is forecast to see a 4% increase in insolvencies, in line with 2017, as economic growth eases and Brexit-related uncertainty impedes investment. Bankruptcies will be concentrated in the construction sector and consumer-related industries.

In emerging markets, the corporate outlook is also relatively positive. Q4 of 2017 marked the second consecutive quarter of easing bank lending conditions according to the IIF. Conditions are expected to continue easing in 2018, but political risk is an increasing downside risk. The stronger global economy and easier financing conditions should support decreases in insolvencies, while the recoveries in Brazil and Russia should continue to drive insolvency declines in those markets. Business failures in Turkey are also expected to decrease slightly in 2018 following a strong boom in 2017, but credit risks are quickly rising.

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	2.5	1.6	-1.2	-1.0	-0.9	1.9	1.0	1.0	6.2	4.1	3.0	2 POSITIVE
Belgium	1.7	1.6	1.7	-1.3	-1.4	-1.2	-0.2	-0.5	-0.3	4.5	4.4	3.7	2 STABLE
Finland	2.6	2.8	1.8	-0.4	-1.0	-0.6	0.7	0.0	0.0	7.8	3.9	2.8	2 POSITIVE
France	2.0	2.1	1.9	-2.9	-2.8	-2.8	-1.2	-1.0	-0.9	3.3	5.0	3.4	2 STABLE
Germany	2.5	2.3	1.8	1.1	0.9	0.3	7.9	8.1	7.8	5.3	6.0	4.1	1
Greece	1.3	1.6	2.7	0.9	0.4	0.7	-1.1	1.2	1.4	6.9	8.7	5.6	7 POSITIVE
Ireland	7.8	4.9	2.2	0.5	0.6	0.5	12.4	3.3	4.0	6.8	2.2	2.1	3 NEGATIVE
Italy	1.5	1.5	1.1	-1.9	-1.8	-1.3	2.7	2.9	2.4	6.0	4.8	3.5	4 STABLE
Netherlands	3.3	2.5	1.7	1.1	1.0	1.1	10.2	10.2	9.9	6.4	4.8	2.9	1
Portugal	2.7	2.2	1.9	-1.0	-1.2	-1.2	0.6	0.4	0.1	7.8	5.2	4.5	5 POSITIVE
Spain	3.0	2.9	2.4	-3.1	-2.3	-1.9	1.9	1.5	1.2	5.0	4.5	4.3	4 POSITIVE
Eurozone	2.5	2.2	1.8	-0.9	-0.8	-0.8	3.5	3.3	3.2	5.3	4.9	3.6	-
Australia	2.3	2.7	2.6	-1.7	-1.3	-1.3	-2.3	-2.0	-2.3	3.8	4.5	6.6	1
Canada	3.0	1.8	2.1	0.3	-0.6	-0.9	-3.0	-3.4	-2.8	1.0	2.3	4.2	1
Denmark	2.2	1.9	1.9	-1.3	0.0	0.0	7.7	5.4	4.6	4.4	2.2	1.8	1
Norway	1.9	2.2	2.0	5.2	4.9	4.4	5.1	4.3	3.8	1.0	2.0	3.1	1
Sweden	2.7	2.8	2.1	1.1	0.7	0.3	3.2	3.2	3.2	4.0	4.9	3.5	1
Switzerland	1.0	2.4	1.7	1.2	1.0	0.4	7.1	8.2	9.1	2.7	4.8	3.4	1
United Kingdom	1.8	1.7	1.7	-2.2	-2.1	-1.6	-4.1	-3.1	-2.3	5.7	4.6	3.4	2 STABLE
United States	2.3	2.8	2.4	-4.8	-5.0	-4.8	-2.4	-3.0	-3.2	3.4	4.1	2.8	1
Central and Eastern Europe													
Czech Republic	4.5	3.7	3.1	-0.1	-0.4	-0.4	1.1	0.2	0.1	6.9	7.1	5.8	3 POSITIVE
Hungary	4.2	4.1	2.7	-1.9	-1.8	-1.8	3.0	3.1	3.0	7.1	6.2	4.3	4 NEGATIVE
Poland	4.5	4.2	3.5	-1.1	-1.3	-1.5	0.1	-0.4	-0.6	6.8	5.1	4.5	3 NEGATIVE
Russia	1.6	1.8	1.4	-1.2	-2.0	-1.5	2.6	5.1	4.3	5.0	4.5	2.5	5 NEGATIVE
Slovakia	3.4	3.3	2.7	-1.4	-1.0	-1.1	-1.8	-1.6	-1.7	4.3	4.7	4.5	3 POSITIVE
Turkey	7.3	4.4	3.1	-1.6	-1.9	-1.9	-5.5	-6.1	-5.1	12.0	5.6	2.8	5 STABLE
Asia													
China	6.9	6.4	6.0	-3.6	-3.4	-3.3	1.3	1.3	1.3	6.6	5.7	4.5	3 STABLE
India	6.3	7.3	7.0	-4.1	-3.5	-3.4	-1.5	-2.1	-2.1	5.5	5.6	6.0	4 NEGATIVE
Japan	1.7	1.5	0.9	-5.0	-5.5	-4.9	4.0	3.9	3.6	6.8	5.1	2.7	3 POSITIVE
Latin America													
Brazil	1.0	2.4	3.2	-7.8	-7.3	-6.6	-0.5	-1.2	-1.6	5.7	6.2	4.5	5 POSITIVE
Mexico	2.3	2.2	2.4	-1.0	-1.5	-2.3	-1.7	-1.8	-1.7	3.9	3.7	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