Atradius
Managing risk, enabling trade

Economic Update

April 2017

Summary

Global

GDP growth picking up, but could be threatened by political uncertainty

World economic growth is forecast to increase 2.8% in 2017, compared to 2.5% in 2016. Global growth is buoyed by a strong US economy, as well as improving outlooks for many emerging market economies. That said, substantial downside risks remain. After the March increase in the US policy rate, markets have priced in two more hikes this year, with the earliest one expected in June. US monetary policy normalisation could hurt some emerging markets with large external vulnerabilities. The likelihood has increased that the Trump administration may not be able to achieve many of its aims, including pro-growth measures such as infrastructure spending. This had led investors to pay more attention to the downside risks of the Trump presidency, notably those stemming from protectionism and aggressive foreign policy actions. There is a broad trend toward populism in western democracies. Political uncertainty has risen following the Brexit decision, the election of Donald Trump and the outcome of the Italian constitutional referendum. The next big test will be the presidential election in France. The net effect of further increasing uncertainty would be negative for global GDP growth, as business investment would be postponed and international trade could slow down further.

Protectionism and anti-trade policies are a major concern amidst this political uncertainty, threatening the outlook for international trade in 2017. In 2016, the volume of global trade slowed to only 1.3%, according to the Netherlands Bureau for Economic Policy Analysis, the slowest pace since the global financial crisis. This slowdown was primarily due to lower demand for goods, but finally there have been signs of a rebound since Q4 of 2016. With stronger global GDP growth prospects, Atradius forecasts world trade to pick up to 3% in 2017.

Backed by the OPEC supply deal, oil prices have stabilised in the USD 50-60 range per barrel of Brent. However, oil prices are too low to enable a significant revival. The US Energy Information Administration forecasts oil prices to level off in 2017, averaging USD 55 per barrel.

Oil price

Brent, USD per barrel

Source: IHS

Eurozone

Economic growth forecasts

	2017	2018
Austria	1.5	1.5
Belgium	1.4	1.6
Finland	1.3	1.4
France	1.3	1.4
Germany	1.4	1.6
Greece	1.5	2.1
Ireland	3.5	3.0
Italy	0.8	0.9
Netherlands	2.0	1.7
Portugal	1.6	1.4
Spain	2.5	2.2
Eurozone	1.6	1.5

Source: Consensus Forecasts (Mar 2017)

Eurozone: navigating through choppy waters

The eurozone economy is forecast to grow 1.6% in 2017 and 1.5% in 2018, supported by low oil prices, monetary easing and employment growth. This forecast is surrounded by high uncertainty. The triggering of Article 50, officially beginning the EU exit process, poses a significant downside risk to the UK and to a lesser extent to the overall European economy, as does the political uncertainty surrounding upcoming elections in large EU Member States.

Over the next two years, the Eurozone economy is likely to benefit from higher growth in emerging markets, as commodity prices recover. In advanced markets, the near term reflects mainly an expected fiscal stimulus in the US. At the same time an accelerated pace of monetary policy tightening in the US creates a growing divergence with the Eurozone, where current low policy rates are expected to last beyond the end of the asset purchase program. Markets expect tapering to be announced towards the end of this year. While foreign exchange markets are believed to have largely priced in the yield differentials between the US and Eurozone, a faster than expected US tightening cycle could lead to a further depreciation of the euro against the US dollar.

With moderate external tailwinds, Eurozone growth will largely have to come from private consumption and investment growth. Confidence indicators are pointing to accelerating economic activity. The European Sentiment Indicator (ESI) reached a value of 108 in February, the highest level in six years. Consumption growth is expected to remain robust in 2017. While the higher expected inflation rate may dampen consumption growth somewhat, employment and nominal wage growth are likely to remain supportive. ECB Bank Lending Survey data are pointing to robust demand for credit among businesses and households. We expect investment to grow at about the same rate this year as in 2016. However, investment growth is still considerably below pre-crisis levels, as it remains constrained by both crisis legacy issues and low productivity growth.

European Sentiment Index

Sources: IHS, Eurostat

Advanced Markets

Economic growth forecasts

	2017	2018
United Kingdom	1.7	1.3
United States	2.2	2.4

Source: Consensus Forecasts (Mar 2017)

US enjoying strong growth in 2017 while UK proves resilient

The US economy is forecast to expand at a solid pace of 2.2% in 2017, supported by solid job growth and increasing wages, which sustain private consumption. The forecast has been revised down by 0.1 percentage points since last month though as the chances that President Trump can push forward his campaign promises of higher public spending becomes more unlikely. A sharper monetary tightening pace will also restrain economic growth slightly. In its meeting on March 14-15, the Federal Reserve raised its main policy interest rate by 25 basis points to a range of 0.75 to 1 percent. The Fed's preferred inflation measure, personal consumption expenditures, rose to 1.9% in January and the labour market has continued its healthy performance. While wage growth remains low indicating some slack still in the labour market, the Fed will likely hike rates another two times this year.

Protectionist rhetoric is a downside risk to US economic growth, but actual policy implications remain uncertain. The current US economic recovery is one of the longest in the post-war period, which increases the statistical probability of a business cycle recession. For the time being growth is forecast to stay robust at 2.4% in 2018, supported by the strong labour market, but could be hampered by populist policies in the medium term.

On March 29, the UK government invoked Article 50, formally beginning the exit negotiation process with the EU. In the aftermath of the Brexit vote, the UK economy has remained resilient, recording 2% growth in 2016, which is only a slight slowdown from the 2.2% expansion seen in 2015. Consumer spending has been the engine of economic expansion, supported by relatively high employment. The momentum remains strong thus far in 2017, but higher inflation due to the weak pound and increasing uncertainty surrounding negotiations with the EU will likely weigh on growth in the course of 2017. Full year growth is forecast to ease to 1.7%.

Source: IHS

Emerging Markets

Economic growth forecasts

	2017	2018
Asia (excl. Japan)	5.6	5.5
Latin America	1.6	2.5
Eastern Europe	2.2	2.6

Source: Consensus Forecasts (Mar 2017)

Emerging markets to see modest recovery in 2017

Emerging markets face a reasonable growth outlook for 2017. Growth is returning in a number of key markets that experienced macroeconomic strain last year (Russia, Brazil, and Argentina). Overall, emerging markets will benefit from the rise in commodity prices.

Emerging Asia is expected to uphold its growth rate, fuelled by high growth in India in particular, despite slowdowns in other markets. China's economy is expected to increase by 6.5% this year, down from 6.7% last year. However, China continues to rely on policy stimulus measures, with rapid expansion of credit. While Chinese authorities are aware of the risks, progress is slow, especially in restructuring highly indebted and inefficient state-owned enterprises. Chinese GDP is expected to slow further in the medium-term as the economy transitions from credit-driven investment growth to more domestic consumption driven growth. While we do not expect a hard landing of the Chinese economy in the short-term, the risks are considerable.

In Latin America, Brazil and Argentina will exit recession (0.7% and 3% GDP growth respectively) thanks to a return to orthodox and market-friendly policies. The presidency of Mr Trump in the US has led to a downward revision of Mexico's GDP forecast.

In Eastern Europe, the outlook for Russia has improved due to a recovery in oil prices. GDP growth is expected to reach 1.3% in 2017 and to rise slightly to 1.6% in 2018. However, in the medium-term structural weaknesses and the negative impact of sanctions on productivity and investment will continue to weigh on growth.

The Trump presidency comes with both upside and downside risks for emerging markets. Mr Trump's plans to boost infrastructure spending could be beneficial for countries exporting commodities, especially construction inputs like iron and steel. However, there are also considerable downside risks stemming from protectionist trade policies and controls of migration (this is especially relevant for Latin America). In addition, a monetary policy tightening cycle in the US could hurt emerging markets, particularly those countries with high external vulnerabilities.

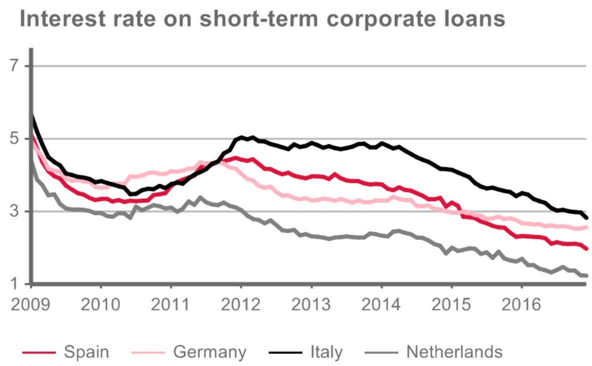
Credit and insolvencies

Insolvency outlook stable but downside risks on horizon

Credit standards for corporate loans in the eurozone tightened slightly in Q4 of 2016, the first tightening since Q4 of 2013. Banks have turned more risk-wary, especially as very low interest rates eat into bank profits. However, in Q1 of 2017 another net easing in credit standards is expected, supported by strengthening capital positions of most banks. Demand for loans continues to grow, supported by lower interest rates. Therefore, credit conditions should support the European business environment in 2017.

The 2017 outlook for insolvencies in the eurozone is relatively positive, but subject to exceptional downside risks. We forecast a 3% decrease in corporate bankruptcies. Insolvencies are expected to be flat in Germany, Austria and Italy. The Netherlands is forecast to see only a 3% drop in business failures after several years of double-digit declines. As more business-friendly policies in France have supported businesses there, we predict a 3% decline. However, due to the eventful political calendar for the eurozone in 2017, those forecasts may be subject to downward revisions. Depending on the outcome of the upcoming elections in France, Germany and potentially Italy, policymaking directions may change to a more business-unfriendly manner, weighing on investment and employment. In this respect, a slowdown in one market could lead to a spillover into others due to close trade and investment ties.

A positive outlook for commodity prices is improving the insolvency outlook for many economies with large natural resource sectors. Across developed markets, this will aid businesses in the US, Norway, and Canada. This is also a positive development for many emerging markets, which depend more strongly on commodity prices. However, rising US interest rates will make financing conditions tighter for businesses across North America as well as in emerging markets.



Source: IHS

Macroeconomic indicators for key markets

	GDP growth (% of GDP)			Budget balance (% of GDP)			Current account balance (% of GDP)			Export growth (%)			Political risk Rating[1]	
	2016	2017	2018	2016	2017	2018	2016	2017	2018	2016	2017	2018		
Western markets														
Austria	1.5	1.5	1.5	-0.8	-1.0	-0.6	2.7	2.6	3.1	2.0	4.1	4.5	2	POSITIVE
Belgium	1.2	1.4	1.6	-2.7	-2.6	-2.4	0.9	1.0	0.6	1.5	2.8	4.2	2	STABLE
Finland	1.6	1.3	1.4	-2.0	-2.2	-2.5	-0.9	0.0	-0.1	1.4	4.6	3.1	2	POSITIVE
France	1.3	1.3	1.4	-3.4	-3.0	-2.9	-1.1	-1.2	-1.3	-0.5	2.7	3.6	2	STABLE
Germany	1.4	1.4	1.6	0.2	0.1	0.0	8.9	8.1	8.1	1.0	3.0	3.8	1	
Greece	0.0	1.5	2.1	-2.4	-1.9	-1.0	-1.0	-1.4	-1.4	-3.6	4.6	3.7	7	POSITIVE
Ireland	5.2	3.5	3.0	-1.5	-0.7	0.2	11.1	10.2	8.3	0.2	12.2	5.6	3	NEGATIVE
Italy	0.8	0.8	0.9	-2.4	-3.8	-2.9	2.3	1.4	1.5	0.1	2.7	3.2	4	STABLE
Netherlands	2.0	2.0	1.7	-0.3	-0.9	-0.9	8.1	11.5	15.7	-0.3	10.2	8.9	1	
Portugal	1.4	1.6	1.4	-2.5	-1.2	-1.4	0.1	-0.8	-1.0	1.1	2.6	3.1	5	POSITIVE
Spain	2.5	2.5	2.2	-4.5	-3.5	-3.0	1.8	1.0	0.9	2.3	4.5	5.3	4	POSITIVE
Eurozone	1.7	1.6	1.5	-1.8	-1.9	-1.7	3.9	3.5	3.8	2.7	3.2	3.0		
Australia	0.0	0.0	0.0	-1.6	-1.1	-0.6	-2.8	-2.3	-3.3	1.3	8.3	2.2	1	
Canada	2.1	2.1	2.0	-1.9	-2.0	-1.6	-3.3	-2.3	-2.7	-0.4	6.5	3.0	1	
Denmark	1.1	1.5	1.7	-1.5	0.1	-0.1	7.9	7.3	6.7	-1.0	7.5	7.2	1	
Norway	1.6	1.6	1.9	2.7	4.5	5.8	3.7	2.5	1.4	4.7	5.6	4.5	1	
Sweden	2.5	2.5	2.2	0.2	-0.4	-0.2	4.5	5.7	5.2	-0.8	3.1	4.2	1	
Switzerland	1.5	1.5	1.7	0.9	0.8	0.8	9.7	7.9	7.0	3.4	3.3	4.2	1	
United Kingdom	1.7	1.7	1.3	-3.4	-2.7	-2.5	-4.9	-3.7	-3.7	4.4	7.0	6.3	2	STABLE
USA	2.2	2.2	2.4	-4.2	-3.5	-3.7	-2.6	-2.3	-2.2	-1.5	4.2	4.8	1	
Central and Eastern Europe														
Czech Republic	2.8	2.8	2.6	0.0	-0.7	-0.4	1.6	0.5	-0.7	-0.6	6.7	4.8	3	POSITIVE
Hungary	1.2	2.2	2.8	-1.8	-2.5	-2.7	4.4	3.6	3.0	4.3	6.8	8.7	5	POSITIVE
Poland	2.2	2.8	2.9	-2.6	-3.4	-3.1	-0.5	-1.3	-1.4	5.8	4.5	6.1	3	NEGATIVE
Russia	4.8	3.6	3.2	-3.8	-3.1	-1.4	1.9	4.3	2.4	-9.6	22.3	-3.4	5	POSITIVE
Slovakia	-0.5	1.3	1.6	-2.3	-1.7	-1.3	-0.6	0.2	1.2	3.3	4.7	6.7	3	POSITIVE
Turkey	2.5	2.5	2.4	-2.1	-2.4	-2.3	-3.6	-4.8	-5.2	5.5	14.0	9.5	5	STABLE
Asia														
China	2.5	2.6	2.8	-4.2	-4.2	-4.0	1.9	3.0	2.9	6.5	8.6	8.1	3	STABLE
India	1.9	2.0	2.1	-6.7	-4.9	-4.9	-0.6	-1.2	-2.0	10.3	7.8	19.8	4	NEGATIVE
Japan	1.2	1.2	1.0	-3.7	-3.3	-3.5	3.8	3.9	3.7	-8.0	4.9	8.3	3	POSITIVE
Latin America														
Brazil	3.7	3.7	3.8	-9.0	-7.6	-5.7	-1.3	-1.6	-1.7	5.0	6.5	9.7	5	POSITIVE
Mexico	3.6	3.6	3.6	-3.3	-2.2	-1.8	-2.7	-2.9	-1.9	10.1	1.7	1.4	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: Consensus Economics, IHS, National accounts, Atradius Economic Research

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