Atradius
Managing risk, enabling trade

Economic Update

July 2016

Summary

2 **Global** – World GDP is forecast to grow only 2.4% in 2016, weighed down by emerging market weakness and increasing uncertainty.

3 **Eurozone** – The modest eurozone recovery is expected to continue with 1.6% growth this year, but this will likely be revised down in coming months due to the effects of the EU membership referendum in the UK.

4 **Advanced Markets** – Momentum is decreasing in both the US and UK, driven by weaker external conditions and deteriorating economic sentiment. This is amplified in the UK by the uncertainty arising from the Brexit vote. 1.9% growth is forecast for both in 2016.

5 **Emerging Markets** – The effects of low oil prices, the slowdown in China and tighter financing conditions continue to weigh on prospects for many emerging markets this year.

6 **Credit and insolvencies** – Credit conditions are loosening further in most advanced economies while tightening in emerging economies. The insolvency outlook for 2016 has weakened for advanced markets while remaining poor for major emerging markets.

7 **Table: Macroeconomic indicators for key markets**

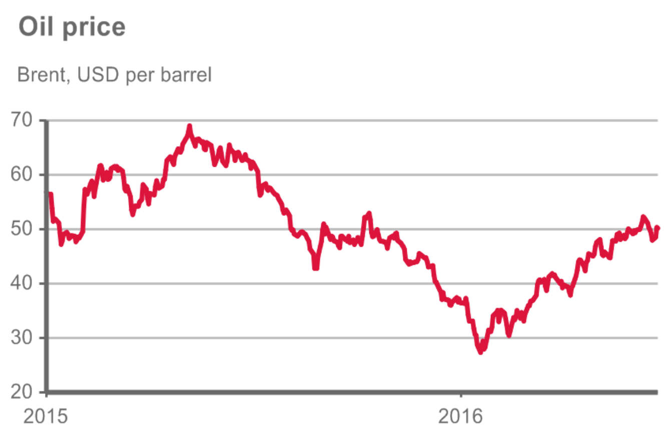
Global

Global growth weakening

The world economy is now forecast to expand only 2.4% this year, down from a moderate 2.6% seen in 2015. The protracted fall in commodity prices, slowdown of China's economy, and most importantly US monetary policy uncertainty have fuelled a recent bout of volatility in the international financial markets.

Oil prices have continued a gradual recovery through June, oscillating around USD 50 per barrel Brent. It appeared as though the global supply glut may finally be reducing: North American production is declining, supply from Iraq, Nigeria and Venezuela has been disrupted, and, Russia and Saudi Arabia had previously been rumoured to have agreed to freeze output. But it is unlikely that the rally will continue and we expect lower prices in the medium run. More US shale producers find it profitable to produce at these current prices and, as demonstrated in the most recent OPEC meeting in Doha, there is still significant risk of oversupply as major oil producers seek to retain market share.

World trade growth is expected to remain muted. The WTO has revised down its forecast for growth in the volume of trade in 2016 to 2.8%. Atradius forecasts a more modest 2.5% expansion. The main reason for this is our more bearish assessment of the impact of the transition of China from an industrial to a services-based economy.



Source: IHS

Eurozone

Economic growth forecasts

	2016	2017
Austria	1.4	1.5
Belgium	1.3	1.7
Finland	1.0	1.4
France	1.5	1.5
Germany	1.7	1.5
Greece	-0.9	1.2
Ireland	5.2	3.7
Italy	1.1	1.2
Netherlands	1.6	1.9
Portugal	1.2	1.6
Spain	2.8	2.3
Eurozone	1.6	1.6

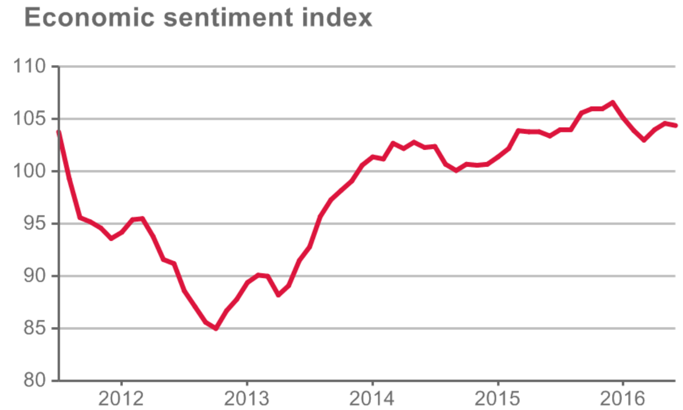
Source: Consensus Forecasts (Jun 2016)

The eurozone economy increasingly fragile

2016 has proven how fragile the eurozone recovery remains. GDP growth for the region rose 1.5% last year, thanks to the improving labour market, low oil prices, and ultra-loose monetary policy, all contributing to rising business investment and domestic demand. The soft euro also helped boost foreign demand. But global risks – as well as domestic risks stemming from the UK's vote to leave the EU and increasing security concerns related to Middle East tensions – have risen. The EUR/USD exchange rate has depreciated 3% since the referendum vote. Economic growth was expected to stay relatively flat at 1.6% in 2016 but post-Brexit revisions are expected to be more restrained.

In order to address the waning economic outlook and avert deflation, the European Central Bank (ECB) cut interest rates to zero and expanded its expansionary monetary policy in March. Markets predict a further rate cut in Q4. Inflation fell to -0.1% year-on-year in May 2016. The ECB has indicated that further stimulus is a possibility to tame the current bout of volatility.

Expectations, however, are broadly stable. The European Commission's economic sentiment index decreased only 0.2 percentage points in June to 104.4, with consumers and business managers showing optimism regarding the robustness of eurozone growth.



Source: IHS, European Commission

Advanced Markets

Economic growth forecasts

	2016	2017
United Kingdom	1.9	2.1
United States	1.9	2.3

Source: Consensus Forecasts (Jun 2016)

US and UK outlooks clouded by uncertainty

The 2016 forecast of UK GDP growth has been regularly revised downward, from 2.5% forecast in September 2015 to 1.9% in June 2016. We expect this trend to continue in July revisions when the vote to leave the EU is accounted for. Preliminary survey results as of June 28th from Consensus Economics show an average prediction of only 1.4% growth. The loss of confidence has caused the pound to experience a historic depreciation of over 11% since the outcome of the EU membership referendum was announced. The Bank of England also alluded to further stimulus measures this summer to counter the slowing in economic growth and heightened uncertainty. However, the loss in consumer and business confidence will be partially offset by an increase in exports.

The buoyant, consumer-driven recovery in the United States has disappointed in 2016. Uncertainty surrounding the impact of financial turbulence and slowing emerging market growth has increasingly clouded the 2016 outlook. The volume of exports fell 5% in April 2016 compared to April 2015 due to the relatively strong US dollar and waning external demand. This trend is likely to continue with further dollar appreciation expected as a result of the Brexit. This new economic landscape is likely to temper the Fed's appetite for a rate hike. Current estimates suggest that they will delay any further tightening until Q4 at the earliest. Despite the general gloom, the labour market is increasingly strong; unemployment is low at 4.7% and the participation rate and wage growth are finally picking up. Similarly, inflation is up to 1.1% y-o-y in May.

Source: IHS

Emerging Markets

Economic growth forecasts

	2016	2017
Asia (excl. Japan)	5.7	5.6
Latin America	-0.5	2.0
Eastern Europe	1.3	2.4

Source: Consensus Forecasts (Jun 2016)

Another difficult year for emerging markets

Aggregate growth across emerging market economies (EMEs) is forecast to rise 4% in 2016, the slowest pace since the onset of the global crisis. Headwinds that have been growing through 2015 will persist this year. Growth continues to be weighed down by low commodity prices, uncertainty regarding the pace of US monetary policy normalisation, rising (geo-)political risk, and concerns about domestic policy measures.

Emerging Asia will remain the fastest growing world region by far with 5.7% growth forecast. India's economy is forecast to grow 7.6% leading this figure. But headline Asian growth is 0.1 percentage points lower than in 2015 due to China's economic slowdown amidst a rebalancing toward services and consumption-led growth. The performance of China has a large impact on many other countries. Lower import demand in China, in combination with declining commodity prices, affects many economies in the region and commodity-exporting countries around the world. The situation is increasingly dire in emerging economies in Europe and Central Asia (Russia, Kazakhstan, Azerbaijan), the Middle East (Saudi Arabia, Oman) and Latin America (Brazil, Venezuela).

Latin America is forecast to experience another GDP contraction in 2016 of -0.5%, suffering from low commodity prices as well as political scandals. The overall figure is weighed down by Venezuela (-8.7%) and Brazil (-3.4%). Recessions are also expected to continue in Argentina and Ecuador.

On the other hand, the situation in Eastern Europe is expected to improve. After a meagre 0.2% expansion in 2015, regional GDP is forecast to rise 1.3% in 2016. The recession in Russia will continue (be it at a slower pace: -0.9%) but Ukraine's economy is forecast to grow 1.1% as the economy stabilises from a very low starting point.

Credit and insolvencies

Business environment worsening

It appears that ECB policy is having some of its intended impact on credit conditions in the eurozone. Interest rates charged by banks on company loans have continued their downward trend since 2012. The 2016 Q1 ECB Bank Lending Survey shows that negative deposit rates are effectively boosting lending (though they are further hurting bank profitability).

Despite improving credit conditions, the insolvency outlook has deteriorated amid rising global uncertainty. Low commodity prices are a major factor in rising insolvencies in Australia (+6%), Canada (+4%) and to a lesser extent the United States (+2%). Lower external demand for exports is another issue weighing on the business environment in the US as well as in many advanced countries including the UK (+2%), New Zealand (+2%) and Japan (-1%). The UK's forecast will worsen further due to Brexit related market volatility. Countries with significant trade and investment ties to the British market will also experience negative revisions. The Netherlands (-10%), Belgium (-5%) and Ireland (-2%) are particularly vulnerable.[1]

In emerging markets, credit conditions are still tightening, largely in response to increased global financial market uncertainty. Many emerging markets, particularly commodity-exporters and those dependent on China, are forecast to see a rise in insolvencies. The economic slowdown in China is expected to lead to a sharp increase in insolvencies there while recessions in Brazil and Russia will also lead to rising bankruptcies.

Source: IHS

[1] A closer look at the implications of the Brexit decision can be found at: https://group.atradius.com/publications/economic-research-brexit-update.html.

Macroeconomic indicators for key markets

	GDP growth (% of GDP)			Budget balance (% of GDP)			Current account balance (% of GDP)			Export growth (%)			Political risk Rating[1]	
	2015	2016	2017	2015	2016	2017	2015	2016	2017	2015	2016	2017		
Western markets														
Austria	0.9	1.4	1.5	-1.2	-1.6	-1.2	2.4	2.3	2.7	3.3	5.0	4.8	2	POSITIVE
Belgium	1.4	1.3	1.7	-2.6	-2.0	-1.8	0.7	1.5	1.1	1.7	4.2	6.0	1	STABLE
Finland	0.5	1.0	1.4	-2.8	-2.2	-2.0	-0.6	0.4	0.3	-2.5	4.8	3.4	2	POSITIVE
France	1.2	1.5	1.5	-3.8	-2.8	-2.3	0.1	-1.1	-0.9	6.2	3.2	4.8	2	STABLE
Germany	1.7	1.7	1.5	0.7	0.4	0.3	8.5	8.3	7.9	6.1	3.3	4.5	1	
Greece	-0.2	-0.9	1.2	-7.2	-2.9	-2.7	-0.1	1.6	1.4	-6.9	-4.2	5.2	7	POSITIVE
Ireland	7.8	5.2	3.7	-2.3	-1.0	-0.4	4.5	2.3	4.6	18.3	5.4	6.0	3	NEGATIVE
Italy	0.8	1.1	1.2	-2.6	-2.6	-2.2	2.5	1.5	0.8	3.5	2.8	4.0	4	POSITIVE
Netherlands	2.0	1.6	1.9	-1.8	-2.2	-1.9	9.2	9.7	9.6	1.7	4.0	6.5	1	
Portugal	1.5	1.2	1.6	-3.0	-2.8	-2.2	0.5	0.3	0.4	4.0	1.7	4.9	5	POSITIVE
Spain	3.2	2.8	2.3	-5.1	-4.3	-3.7	1.4	0.2	-0.2	5.8	5.6	5.9	4	POSITIVE
Eurozone	1.6	1.6	1.6	-2.1	-1.8	-1.5	4.0	3.5	3.2	5.2	3.3	3.7		
Australia	2.5	2.9	2.9	-1.7	-2.0	-2.3	-4.8	-4.3	-4.2	-2.2	3.5	5.1	1	
Canada	1.1	1.4	2.2	-1.3	-1.4	-1.0	-3.2	-2.2	-0.8	-0.3	1.5	2.2	1	
Denmark	1.2	1.3	1.8	-1.6	-1.4	-1.1	7.0	9.5	10.3	2.3	4.3	5.6	1	
Norway	1.0	0.9	1.8	5.2	3.7	4.2	8.0	5.6	6.8	-4.0	-4.0	5.8	1	
Sweden	4.2	3.6	2.6	0.0	-0.7	-0.4	6.0	6.8	5.9	7.8	6.5	4.9	1	
Switzerland	0.9	1.1	1.5	-0.2	-0.3	-0.2	11.4	9.3	8.5	-3.2	3.4	4.4	1	
United Kingdom	2.3	1.9	2.1	-4.3	-3.1	-2.4	-5.2	-5.0	-4.1	-0.4	1.8	6.9	2	STABLE
USA	2.4	1.9	2.3	-3.4	-3.5	-3.2	-2.7	-2.8	-2.7	-3.8	-0.2	6.8	1	
Central and Eastern Europe														
Czech Republic	4.3	2.4	2.7	-0.4	-0.6	-0.9	0.9	0.8	-0.2	5.8	5.3	6.0	3	STABLE
Hungary	2.9	2.3	2.7	-1.9	-2.6	-2.7	4.4	4.5	3.9	8.1	7.3	8.6	5	POSITIVE
Poland	3.6	3.5	3.4	-2.6	-3.2	-3.3	-0.2	-1.0	-1.3	9.2	5.5	5.3	3	NEGATIVE
Russia	-3.7	-1.2	1.0	-3.9	-3.8	-3.4	5.2	1.3	0.2	16.7	16.5	3.4	5	POSITIVE
Slovakia	3.6	3.2	3.3	-3.0	-1.9	-1.5	-1.3	-0.4	0.1	6.2	5.3	6.1	3	POSITIVE
Turkey	3.6	3.4	3.5	-1.8	-2.7	-2.2	-4.5	-5.0	-5.2	11.0	8.0	10.7	5	STABLE
Asia														
China	6.9	6.6	6.3	-3.5	-4.2	-4.2	3.1	3.4	4.0	1.7	8.4	8.2	3	STABLE
India	7.5	7.6	7.7	-7.4	-5.8	-4.5	-1.1	-1.2	-1.7	-6.2	10.8	10.9	4	NEGATIVE
Japan	0.6	0.5	0.9	-5.3	-6.8	-6.9	3.3	3.1	2.9	3.4	-4.2	8.1	3	POSITIVE
Latin America														
Brazil	-3.8	-3.7	0.7	-10.3	-10.1	-8.9	-3.4	-1.0	-1.4	19.4	12.3	5.6	5	POSITIVE
Mexico	2.5	2.4	2.8	-3.5	-2.9	-2.8	-2.8	-2.2	-2.4	9.3	6.1	5.9	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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David Ricardostraat 1– 1066 JS Amsterdam
Postbus 8982 – 1006 JD Amsterdam
The Netherlands
Tel. 020 553 9111
info@atradius.com
www.atradius.com