MID-YEAR GLOBAL OUTLOOK COUNTRY INSIGHT SERVICES

May 24, 2017

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PUBLIC

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# Mid-Year Global Economic Outlook

The Global Economy's Transition to the 'New Normal'

- COUNTRY INSIGHT SERVICES May 24 2017

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## **Country Insight Services**

Economic downturns, political upheaval, and natural disasters can all have an impact on global trade. Unrest can result in overnight barriers to imports, added taxes to exports, piracy activity in key shipping lanes, and other substantial obstacles to global business.

**D&B Country Insight** provides comprehensive analysis on over 130 individual countries that account for more than 95% of the global GDP, helping you understand:

- Political Risk: How stable is the country's government?
- Economic Risk: Is the economy expanding or contracting?
- External Risk: Is the currency stable or unstable?
- Commercial Risk: Will I get paid and how quickly?
- Trade Environment: Have import regulations changed?

#### **Contact the team**

#### **D&B** Country Insight Services

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Global Recovery Update – Our view

North America

Western Europe

Eastern Europe & Central Asia

Latin America

Asia-Pacific

Middle East & North Africa

Conclusion

Q&A

# Growth Prospects Outweigh Operational Risks

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Rising Nationalist Movement

Trade Uncertainty

**Foreign Policy** 

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Economic Volatility

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## Our Top Risks Facing the Global Economy

Region	Risk	Likelihood (%)	Probability (%)	Global Impact (1-5)
I	Pan-regional	The imposition of a border adjustment tax on US imports will lead to formal protests and probable retaliation from America's largest global trade partners.	50	3
2	Pan-regional	Rapidly growing cyber-dependence and connectivity lead to increasingly frequent and more damaging cyber incidents, with global ramifications.	70	2
3	Asia-Pacific	In China, contagion from bad debts in industry and local government triggers a hard landing for GDP and state rescues of mid-tier banks.	33	4
=4	Latin America	The widening investigation into the USD788m Odebrecht bribery scandal, which already includes II Latin American countries and several extra-regionally, leads to the cancellation of dozens of worldwide infrastructure projects resulting in substantial losses for foreign partners/contractors.	60	2
=4	Western Europe	Parliamentary elections in Italy end with the victory of anti-EU parties, triggering further pressure on the EU.	40	3
=6	Middle East & North Africa	Success of the authorities in combatting Islamic State in Iraq and Syria sees the group adopt high profile attacks in the Middle East and Europe disrupting the business environment.	50	2

The Dun & Bradstreet **Global Risk Matrix** ranks the biggest threats to business based on each risk scenario's potential impact on companies, assigning a score to each risk. The scores from the top ten risks are used to calculate an overall Global Business Impact score. Our latest Global Business Impact score highlights a significantly improved risk outlook for cross-border businesses.



## ...Drive Our Forecasts for Better but Mediocre Growth

#### Real GDP Growth (%)

	2015	2016e	2017	2018	2019	2020	2021
World	2.6	2.3	2.7	3.0	3.1	3.1	3.0
Advanced economies	2.2	1.7	1.9	2.2	2.1	2.1	2.1
US	2.4	1.6	2.2	2.6	2.3	2.2	2.0
Euroland	2.0	1.7	1.6	1.9	2.1	2.2	2.3
Japan	1.2	1.0	1.5	1.3	1.2	1.0	1.0
UK	2.2	1.8	1.8	1.6	1.6	1.7	1.8
Emerging economies	3.4	3.4	4.2	4.5	4.8	4.7	4.6
Brazil	-3.8	-3.6	0.2	1.5	2.0	2.1	2.3
Russia	-3.7	-0.2	1.3	1.7	1.7	1.7	1.8
India	7.9	7.1	7.5	8.0	8.0	8.0	7.2
China	6.9	6.7	6.3	5.8	6.0	5.5	5.1

## ....With Considerable Divergence Across Key Regions

#### Real GDP Growth (%)

	2015	2016e	2017	2018	2019	2020	2021
North America	2.3	1.6	2.2	2.6	2.3	2.2	2.0
Europe	2.1	1.8	1.7	2.0	2.1	2.2	2.3
Asia Pacific	4.5	4.4	4.5	4.4	4.6	4.4	4.2
Latin America & Caribbean	-0.6	-1.9	0.7	1.7	2.1	2.6	2.8
Eastern Europe & Central Asia	0.0	1.3	2.1	2.5	2.7	2.8	2.9
Middle East & North Africa	2.0	2.8	2.6	3.2	3.6	3.8	4.2
Sub-Saharan Africa	3.2	1.0	2.4	3.3	3.6	3.9	3.8
World	2.6	2.3	2.7	3.0	3.1	3.1	3.0

# Even Without Policy Uncertainty, Global Trade Will Expand Only Modestly



Sources: WTO, Dun & Bradstreet

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## The New Normal for US Interest Rates Has Global Implications



Sources: Federal Reserve, Dun & Bradstreet

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# North America

## US Economy's Fundamentals Solid, But Fiscal Policy Boost Not Likely to Add to Growth Until 2018 ...

	2015	2016	2017F	2018F	2019F	2020F	2021F
Real GDP, % SAAR	2.6	1.6	2.2	2.6	2.3	2.2	2.0

- The fundamentals of the economy are solid, we are now in the 3<sup>rd</sup> longest expansion in history
- Consumers are the main driver of GDP, and will bounce back after a breather
- The labor market is near **full-employment**, which bodes well for wage growth and sustained consumer spending, despite Q1 doldrums
- Business spending might also be picking up, thanks to **optimism** (sustainability?)
- Stimulus effects of the President's proposed measures are likely to take some time (implementation risks?)
- As of March 2017, we expect the "Trump bump" to growth to materialize in 2018, rather than 2017
- As of now, we expect fiscal measures to add to growth, but **not by a large amount** as the economy will be at full-employment by then

## ... Implementation Risks Cloud Eventual Impact



Sources: Bloomberg, Dun & Bradstreet

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## Canada: Gradually Improving, but Unspectacular Growth



While Canadian mortgage rates have trended down over time, a sudden rise in U.S. Treasury rates will likely lead to higher Canadian borrowing rates likely immediately slowing the market or even worse disrupting it.

Historical Correlation Matrix {Yields on 10-year government notes}	U.SCanada	U.SAustralia	U.S France	U.SGermany	U.SItaly	U.SSpain	U.SUK
	0.96	0.88	0.88	0.85	0.56	0.5	0.94

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# Western Europe

## **Economic Baseline Figures**



- The region's outlook is largely positive: the euro zone grew by 1.7% in 2016, down from the 1.9% seen in 2015 but still the second-highest growth rate since 2010.
- Looking ahead, we expects a further recovery in 2017, as implied by encouraging figures for several forward-looking indicators.
- Labour market conditions are also improving, but country-level differences remain substantial.

## Problem: significant country level differences remain

Country	Average Share of Prompt Payments
Denmark	86.5%
Germany	81.7%
Hungary	55.4%
European Average	39.1%
Bulgaria	23.7%
Portugal	19.5%
Romania	17.6%

## Problem: significant country level differences remain

Country	Average Share of 90+ Days Late Payments				
Romania	20.4%				
Poland	15.0%				
Portugal	9.6%				
European Average	3.7%				
Czech Republic	0.7%				
Germany	0.2%				
Denmark	0.1%				

## Political Risk is falling but still elevated

- French presidential elections reduced risks
- But: Macron needs parliamentary majority (11/18 June)
- German elections: unimportant from a country risk perspective
- First key risk: Parliamentary elections Italy (early 2018)
- Second key risk: Brexit negotiations (until late 2018)

# Eastern Europe & Central Asia

## Growth to remain at historically weak levels...

**Regional GDP Growth** 



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Source: Dun & Bradstreet & Haver Analytics

## Monetary Policy Normalisation: rates coming down...

#### **Central Bank Interest Rate**



Source: Dun & Bradstreet & Haver Analytics

### ...as exchange rates stabilise and inflation moderates



#### Source: Dun & Bradstreet & Haver Analytics

## **Risks & Opportunities**

#### Risks

- -Financial: While banking sector risks have moderated recently, the potential for a systemic crisis cannot be discounted
- -Economic: Failure to diversify away from an oil-centric economic model, resulting in lower-for-longer regional economic growth
- -Political: Persistent economic hardship and growing frustration with government policies and corruption lead to increasing social unrest, threatening the stability of the region's political regimes

#### **Opportunities**

**Financial:** Strengthening currencies (e.g. Russian rouble) are offering some of the largest returns in emerging markets

**Economic:** Agricultural sector revival in a number of countries – including Russia, Ukraine and Kazakhstan – is opening up new opportunities in the region

**Political:** As a number of governments push ahead with ambitious privatisation drives, there is the potential for the development of a more investor-friendly political climate

# Latin America

## Lethargic return to growth



2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016e 2017f 2018f 2019f 2020f 2021f

Source: Dun & Bradstreet & Haver Analytics

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## Inflationary pressures ease (for some) ....





## As exchange rates regain ground ...



Exchange Rate (per USD)

## ... leading to divergent monetary policy



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### Recommendations

- ✓ With the exposure of new corruption scandals such as the USD788m Odebrecht bribery case, ensure compliance with anti-corruption laws to minimize reputational risk.
- ✓ Develop contingency plans for the elevated risk of expropriation in Venezuela as political turmoil escalates.
- ✓ Expect ongoing challenges with bureaucracy and inadequate infrastructure.
- ✓ Despite some apparent softening in the original ultra-protectionist stance of the US administration, carefully monitor moves to re-negotiate NAFTA, and watch for changes to US trade and immigration policies. These could impact agriculture exports (South America) and manufactured goods (Mexico) as well as remittance inflows (Mexico, Central America).
- ✓ As the UK negotiates its divorce from the EU in the next two years, follow Brexit talks particularly regarding the impact on investment and trade. Post-2019 watch for new bilateral UK trade deals in the wake of Brexit but expect delays in finalization of agreements.

# Asia-Pacific

## China: Regulatory arbitrage has driven rapid credit creation



# China: example of regulatory arbitrage driving rapid credit creation using onshore and offshore institutions



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# Off-balance sheet wealth management products present contagion risks and have grown rapidly



Source: China Banking Wealth Management Registration System

# Small financial institutions are exposed to interest rate shocks as regulators close up funding channels

#### China 3-month interbank cash rate Bank financing from central bank, % deposits 8.0 16 7.0 14 6.0 12 5.0 10 4.0 8 3.0 2.0 4 1.0 2 0.0 0 o-un[ Apr-10 Dec-16 Oct-12 Feb-II Aug-13 Jun-14 Feb-16 Dec-II Apr-15

- Smaller banks have already exceeded their wholesale finance caps once Certificates of Deposit are included
- Even large city banks with international investors will be affected by new macroprudential assessment framework
- Regulators are determined to close loopholes and this will increase the cost of wholesale finance

Sources: Tullett Prebon, IMF, People's Bank of China, Haver Analytics

- New bank regulator chief since Q1 investigating "various phenomena of disorder"
- Insurance and securities sectors also under investigation
- A 1% increase in non-equity debt servicing costs = 20% of 2016 industrial firm profits



#### China

## Japan's financial crisis: lessons for China?

Deregulation of financial sector rapid credit growth hunt for yield (declining returns made banks less demanding about borrower's creditworthiness and rely increasingly on real estate as collateral) asset price bubbles.

Lax monetary policy for too long followed by policy tightening precipitated the unwinding of unsustainable balance sheets.



Japan: monetary policy and asset prices 1980-2003

Sources: Japan Real Estate Research Institute, Bank of Japan, Nihon Keizai Shimbun, Haver Analytics

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# **Bottom Line**

Even if China can avoid a financial crisis due to careful policy calibration, we expect a period of slower growth, and more frequent business failures. And even if China avoids a hard landing, thanks to its services sector and wealthy, economically diversified urban conurbations, capital controls will continue and softer physical commodity demand will have impacts on global supply and demand.

# Middle East & North Africa

## Average Annual Oil Prices (USD/b)



Source Dun & Bradstreet

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## Factors Affecting Oil Prices

- OPEC production quotas
- Rising US supply
- Slow demand growth
- Inventories
- US dollar strength

## The Depressing Political Environment Outlook



#### Legend:

- Green is best risk, amber middling risk and red worst risk
- Arrows range from improving ( $\nearrow$ ), through stable ( $\rightarrow$ ) and deteriorating ( $\searrow$ ) to rapidly deteriorating ( $\downarrow$ ).

## Areas of Concern

- Iran-Saudi Islamic Cold War
- Civil wars in Libya, Syria, Iraq and Yemen
- States of Emergency in Bahrain, Egypt and Turkey
- Roll back of Islamic State but resurgent al-Qaeda
- Israel-Palestine



# Thank You!

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