Atradius
Managing risk, enabling trade

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Economic Outlook

A bright sky, for now

Editorial

A bright sky: that is what springs to mind when we consider the current state of the global economy. Data confirm that 2017 marked a year of acceleration in GDP growth, which grew 0.6 percentage points faster than the year before. 2018 promises to be another year of strong growth, with GDP growth pushing up to 3.2%. That would be the highest level since 2011. Trade growth is buoyant and investments are finally recovering. Energy and commodity prices rejoice in an upswing, supporting investments. Activity abounds. Growth, moreover, is broad-based and includes advanced as well as emerging economies. Even Latin America, notably Brazil, is dragging itself out of a long period of economic backlash. And while there is no shortage of political developments, they have thus far found no place in which to cast a shadow.

Not yet, at least. In our November Economic Outlook, we argued there was no time for complacency and that it was the right time for policy action. Now, six months on, we may cautiously conclude that policymakers – especially those in the US – have taken this advice perhaps a bit too literally.

The first policy is the USD 1.5 trillion tax cuts that were enacted in the US Tax Cuts and Jobs Act. That is believed to provide a growth stimulus of 0.5 percentage points over the next two years. It is obviously not this outcome, as such, that worries us. What does, is that such stimulus should not take place when the economy is already producing at full capacity. Unemployment is at a 17-year low. The tax stimulus may only create inflationary pressures that will be difficult to control. That is precisely what we do not need. It may trigger unguided rate hikes or unguided balance sheet reductions by the Fed, creating turmoil in the financial markets. This could lead to reduced household and business spending. The tax cuts, therefore, are a risk, it is an ill-timed economic experiment.

The second, and even less wanted, policy action has been the protectionist bend the US administration has taken since early this year. Emboldened by the political success of the Tax Cuts and Jobs Act the administration has targeted trade policy. In early March, tariffs on steel and aluminium imports were announced and implemented, albeit with wide exemptions. It triggered a muted retaliation from China, followed by the US announcement of a list of imported goods from China with a total value of USD 60 billion that would be subject to tariffs. China immediately responded. While neither the US nor the Chinese measures have been implemented yet, the picture of a trade war between the two largest economies on the planet has started to loom. Such a war may not happen, and – as we argue in this Outlook – it is not our main scenario. But if it does, there will be a large-scale impact on the global economy.

Since our November Outlook the global economy has further improved and we look forward to that continuing. However, at the same time, the chances of it improving for a longer period are deteriorating, especially due to the protectionist bend of the US administration. The sky is bright for now, so enjoy it while it lasts.

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Executive summary

The global economic upswing, underway since H2 of 2016, is continuing to strengthen. Recoveries are broadening into more emerging markets and global trade and investment activity have finally been picking up. At the same time, risks to the outlook have increased substantially since the November Economic Outlook. US policy uncertainty and a potential trade war could quickly darken the current bright skies.

Key points

- Global GDP growth is forecast to accelerate to 3.2% in 2018, the strongest annual expansion since 2011. Growth is expected to remain strong in 2019 but moderate slightly to 3.0%.
- The US economy is outpacing other advanced markets, with growth set to expand 2.8% this year before easing to 2.4% in 2019. After a very strong year, the eurozone economy is forecast to expand a solid 2.2% this year before easing further to 1.8% in 2019. Growth is also easing in Japan while it stays resilient in the UK.
- GDP growth across emerging market economies as a whole is picking up strongly. Latin America is set to see the strongest acceleration, to 2.0% in 2018 and 2.9% in 2019. Eastern Europe is expected to see some momentum easing from 3.0% this year to 2.5% next year. Emerging Asia will continue to enjoy the strongest growth, but a gradual slowdown in China is forecast to increasingly drag on regional growth, bringing it down to the still respectable 5.8% in 2018 and 5.5% in 2019.
- The global upswing has translated in further improvements in the insolvency environment. After a 4% decline in corporate failures across advanced markets in 2017, Atradius forecasts a further 3% decline this year. Insolvencies are also on a downward trend in key emerging markets.

The key trends underpinning the global economic upswing as well as the underlying risks are discussed in *Chapter 1* of this Economic Outlook. Global growth is increasingly broad-based, with recoveries in trade and investment underway, as well as oil and commodity prices. We highlight the significant increase in the risk of a trade war. However, there are also positive developments on trade that should not be ignored: at the global level, more policies are implemented to facilitate than to restrict trade and some countries are now accelerating trade liberalisation negotiations.

Naturally, US protectionism now tops our list of risks to the global economic outlook's bright sky. The second highest risk we identify also stems from the world's largest economy: misguided Fed policy. The remaining risks are (3) a hard landing in China, (4) a financial market correction, (5) heightened geopolitical risk, and (6) oil price volatility.

In *Chapter 2*, prospects and risks in developed economies are presented. The US outlook is revised up from the previous Outlook, as a loosened fiscal policy adds fuel to the economy that was already going strongly. The fiscal stimulus could increase the risk of misguided Fed policy and will reduce the policy tools to combat the next downturn in the US. Policymaking uncertainty, especially related to trade, may bring on that downturn more quickly than expected. The eurozone will continue to enjoy loose monetary policy and tightening labour markets but some momentum will ease as export growth slows. The UK is expected to remain resilient while Advanced Asia loses some momentum alongside slowing Chinese growth.

The outlook for emerging markets is discussed in *Chapter 3*. Special attention is paid to EMEs' vulnerability to global trade developments and initiatives undertaken to increase trade, in an effort to mitigate these risks. China's dominance in Asia and extensive investment activities across emerging markets, especially in Sub-Saharan Africa and Asia, are also causing more opposition and a possible threat to debt sustainability in some EMEs.

The bright sky foreseen for the global economy in 2018 is further reflected by the modestly positive insolvency outlook presented in *Chapter 4*. A 3% decline is forecast in aggregate corporate bankruptcies across advanced markets this year. The UK is the only real exception to the positive outlook. In Advanced Asia, Japan's insolvencies are expected to stabilise at historically low levels while corporate failures in other markets decrease strongly despite rising headwinds from China. Steady declines are also forecast for key emerging markets with available data – especially in Brazil as it bounces back from a deep recession.

1. The global macroeconomic environment

A bright GDP growth picture, for now

Against the backdrop of a looming trade war, global GDP growth is still strengthening. 2017 marked a year of global GDP growth acceleration of 0.6 percentage points and 2018 promises to be another good year. GDP growth is expected to climb even further to 3.2%. That would be the highest level since 2011. 2019 is expected to show some moderation with growth of 3%.

Table 1.1 Real GDP growth (%) - global regions

	2017	2018 f	2019 f
Eurozone	2.5	2.2	1.8
United States	2.3	2.8	2.4
Emerging Asia	6.0	5.8	5.5
Latin America	1.1	2.0	2.9
Eastern Europe	3.1	3.0	2.5
World	3.0	3.2	3.0

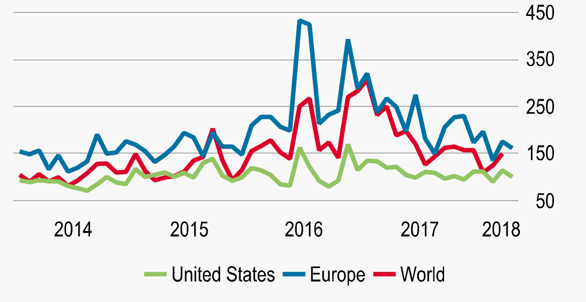
Sources: Macrobond, Oxford Economics

This picture is underpinned by continuation of the favourable financing conditions, strong sentiment as well as US fiscal stimulus. It is supported by a long awaited pick up of investment growth, which in turn further pushes up trade growth. This is expected to last during the forecast period. But, as we will elaborate in this Outlook, a new US trade policy with a more protectionist bend is taking shape. That implies our forecasts, that include the impact of the US tax cuts, are surrounded by an increasing amount of uncertainty.

Incoming 2017 data confirm the picture of our November Economic Outlook. With the exception of global-growth torchbearer Emerging Asia, all regions improved. Most notably, GDP growth in advanced economies gathered pace growing 2.3% (2016: 1.6%). The eurozone in particular improved, as private credit and employment exceeded expectations. US growth was buoyed by strengthened private investments and exports. Recovering Brazil dragged Latin America out of the 2016 recession. Both Russia, as it welcomed higher energy prices, and Turkey, banking on fiscal stimulus, strongly supported an Eastern European growth jump to 3.1%. Last but not least, Emerging Asia saw its GDP growth flat at 6%. China inched up somewhat while in India growth was depressed by temporary factors. Chinese and Indian GDP growth figures remain way above the emerging economies average of 4.4%.

1.1 Policy uncertainty still subdued

Economic policy uncertainty index, news-based

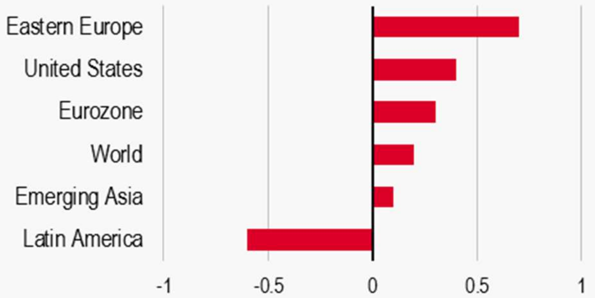


Sources: Macrobond; Baker, Bloom & Davis

Meanwhile the economic policy uncertainty (EPU) index signals calm, as opposed to late 2016 and early 2017 when it peaked. This is remarkable, especially now that the US administration has announced a break from its long-standing free trade policies. For Europe, the outcome of the Italian elections underlining the presence of a populist (and anti-EU) tendency in Europe has not created ripples either. Nor has the mini-crisis in the financial markets in early February. These events create uncertainty, but the mood is positive, also in this Outlook.

Positive the mood is indeed. Banking on the aforementioned factors continuing, our forecast for 2018 has been revised upward significantly compared to our November 2018 Outlook. The exception is Latin America where Q4 2017 data suggest growth momentum in the four largest economies to be less than initially anticipated.

1.2 2018 outlook has improved
Change in 2018 GDP growth forecasts from Nov 2017 to May 2018



Sources: Oxford Economics, Atradius

The emerging picture for 2018 is one of accelerating GDP growth, especially for the US and Latin America. Forecasts for the US reflect fiscal stimulus that will support further investment growth. Latin American growth is expected to accelerate, and markedly, to 2.1%. Other regions show marginal, if any, pressure on growth rates, whilst these remain high. In the eurozone, like in the US, investment growth is the main driver of the 2.3% GDP growth. It, however, has a different source, as there is no eurozone fiscal policy boost. It all comes from labour market strength, stepped-up bank lending and business sentiment indicators being on a high. In Emerging Asia, China is expected to decelerate to 6.4% due to some tightening in fiscal and monetary policy. GDP growth in India is forecast to pick up, helping to sustain the healthy 5.9% growth rate in the region. Eastern European GDP growth is lower, but healthy. Russian growth remains muted and Turkish growth carries on at a high rate.

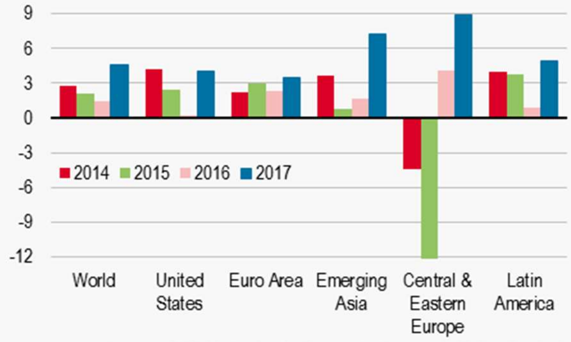
Growth acceleration, though, cannot last forever and 2019 shows a slight, but significant, compression of global growth. With the exception of Latin America where especially Brazil is getting in better shape, this is an across-the-regions phenomenon. The impact of stepped-up monetary policy normalisation, in the US and the eurozone, will be felt. Just like further slowing Chinese growth. Still, barring the manifestations of risks, the picture for 2019 remains bright, with 3% global growth expected.

Buoyant trade continues

In our November 2017 Economic Outlook we reported a strong rebound of global trade growth, based on data until August 2017. In this context, we revised our full year forecast upwards. Six months on it appears the final figure falls slightly short of the forecast. We can confirm the rebound has been strong indeed, at 4.5% compared to the meagre 1.4% in 2016.

Trade growth did very well in 2017, at least compared to 2016.[1] Similar to GDP growth figures, this is a broad-based rebound. US trade growth shot up to 4.1% from a dismal 0.2% as the eurozone climbed to 3.5% Emerging Asia found form at 7.3% and Latin America at 4.9% . Emerging Europe trade growth tops the list at almost 8.9%. These figures are all higher than what was forecast in November, confirming the acceleration in trade growth during 2017 that was signalled at the time.

1.3 Strong rebound in world trade in 2017
Volume of goods trade, % change y-o-y



Source: CPB Netherlands Bureau for Economic Policy Analysis

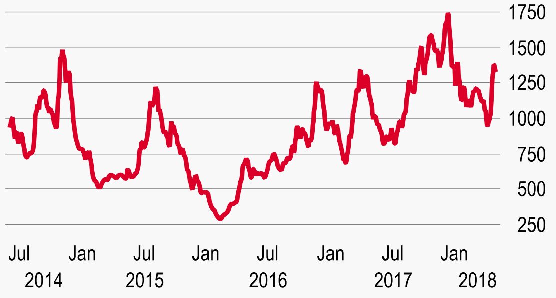
The 2017 figure contains a catch-up element as it comes from a (very) low base in 2016. Therefore, 2018 can be expected to show somewhat less buoyant trade growth. This is underpinned by the recent development of an indicator we regularly track for guidance on future trade growth, the global export orders index. This indicator stood at 51.8 in March, lower compared to the level upheld since the summer of 2017. Still, it signals firm expansion of global exports. Our forecast, of which the November one came very close to the actual 2017 figure, is also in line with this. We expect 3.7% global trade growth in 2018.

A bit less comforting is the development of the indicator that helped predict the mid-2017 trade growth revival, the Baltic Dry Index. This metric has come off from its four-year high of 1743 in December 2017 to hover around 1100 thus far in 2018. In April though, another sharp reversal occurred, driving up the BDI by over 40% at time of writing. While this offers relief, the fairly steep drop in

[1] The figure is still well below the 5.5% long-term average.

early 2018 is a clear reminder that current trade growth levels should not be taken for granted as US protectionist policies take shape. Protectionism would negatively affect commodity trade, which strongly correlates with freight costs, and that is anticipated in the Baltic Dry Index.[2]

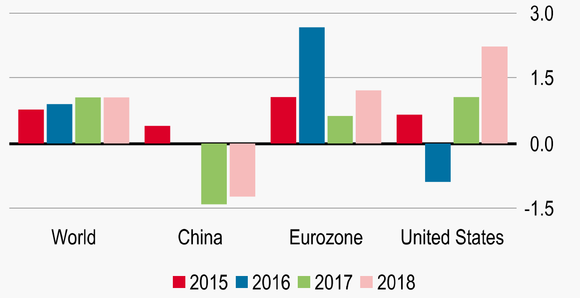
1.4 BDI needs to be kept a close eye on
Baltic Exchange, Shipping, Dry Index (BDI)



Source: Macrobond

What is underlying this still rather robust trade outlook? Let us (re)consider the contributing factors for trade growth we identified in our November Outlook. First, the fall of the policy uncertainty since early 2017, reflecting the reduced economic policy uncertainty at the time. Global as well as European policy uncertainty is now much lower, indicating calm as we highlighted above. This bodes well for global trade: a World Bank study has found a strong relationship between policy uncertainty and trade.[3] Second, the US economy has grown robustly in 2017 on the back of higher energy prices and less policy uncertainty. That has spurred investment growth, which is relatively trade intensive (compared to consumption growth). For 2018 and 2019 it looks even better with the upcoming US fiscal stimulus investment growth should remain strong. This will boost imports, and given that the US dollar is overvalued and expected to depreciate (see below), exports should increase as well. Third, China's import growth was very strong in 2017, at 7.3%, whereas exports also grew at 6.8%. This clearly helped global trade. Our November Outlook signalled that 30% of global trade acceleration could be attributed to Chinese demand, a figure that can even rise much higher if indirect channels such as intra-regional supply chains are included. Moreover, Chinese demand supported commodity price strengthening, which buttressed investment in commodity exporting countries. Chinese demand is expected to keep up in 2018 and later, but the impact of the switch towards less trade-intensive services (previously 43% of GDP, now 54%) will be felt. Chinese trade growth is forecast to remain high, but it is clearly decelerating in line with the GDP growth slowdown. This will weigh on trade growth. Fourth, support has come from large emerging economies recovering from recessions in 2017, like Brazil, Argentina and Russia. This has had a positive impact on Latin American and Eastern European trade growth. As these countries are forecast to grow further, with the exception of Turkey, their support for trade growth will remain. The upshot is then that the factors that have bolstered global trade growth in 2017, with a somewhat lower Chinese contribution, are there to stay in 2018-2019. Trade growth is perhaps slightly lower but remains robust.

1.5 Investment growth in Western markets offset by less growth in China
Fixed investment as a share of GDP, % change y-o-y



Sources: Macrobond, Oxford Economics

The question then is: what about the factors that hamper global trade growth? We have identified in previous Economic Outlooks the trade finance gap and protectionist measures. As to the global finance gap, this seems to have widened. As the WTO reports,[4] the financing gap has been constant at approximately USD 1.5 trillion since 2014. But this is a bit deceptive as the USD has fallen 16% over time and trade has not grown so much. The gap is concentrated in Asia, Latin America and Africa and the Middle East. Moreover, whilst at the high end of the market sufficient liquidity is available, trade finance is particularly difficult for SMEs, especially in the emerging economies. Bottlenecks present in smaller banks, which lack knowledge and face challenges to comply with the stepped-up regulatory requirements. This often prevents leverage from multilateral development banks as well.[5] Without clear initiatives by the WTO to address the issue, it seems the gap is there to stay, at least over the forecast period.

Meanwhile, the incoming data for 2017 (until October) provides a more optimistic picture of protectionist measures than we envisaged in November 2017. At that time, it appeared that net trade facilitation, the difference

[2] The index tracks the transport cost of commodities such as grain, iron ore and coal by ship.

[3] 75% of the global trade reduction between 2016 and 2015 is attributed to policy uncertainty. See Trade Developments in 2016: Policy Uncertainty Weighs on World Trade, World Bank February 2017.

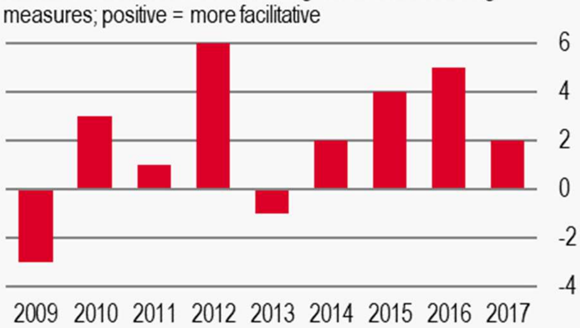
[4] See Overview of Developments in the International Trading Environment, November 2017.

[5] For example, the European Bank of Reconstruction and Development has rejection rates in the order of 50%.

between trade-facilitative and restrictive measures, was grinding to a halt, but late-2017 developments reversed that trend. Net trade facilitation was positive during 2017, in volume terms as well as value at USD 90 billion per annum. Moreover, the number of trade restrictive measures was at its lowest since 2009. The world seems to be on the right track. But such a conclusion may be premature since in early 2018 the US showed it would not only bark but also bite in trade matters.

1.6 Net trade facilitation remains positive

Difference between trade-facilitating and trade-restricting measures; positive = more facilitative



Source: WTO

Rising US protectionism spurs free trade agreements

Biting is what at least seemed to be the case when on March 2 the US administration announced 25% tariff on steel and 10% on aluminium imports. The tariffs were framed as a fight to preserve jobs for American steelworkers, a Trump campaign promise. Following the tariff announcements, the US chief economic advisor, Gary Cohn, resigned to be replaced by Larry Kudlow. Although the latter had been critical about the tariff levy, the view that protectionists had gained the upper hand in the White House prevailed. That boded ill for trade. These fears were further fed by the announcement later that month of a 25% tariff to be levied on USD 60 billion of Chinese imports, yet to be specified.[6] China's response (to the steel and aluminium tariffs) is on USD 3 billion imports from the US, a 15% levy on steel pipes and fresh fruits and a 25% levy on pork and aluminium.

Now, is this really biting? With regard to steel and aluminium that is highly questionable. Pending the NAFTA negotiations, Mexico and Canada earned an immediate exemption. Australia followed suit due to the existence of a 'security arrangement' with the US. Later exemptions were granted for the EU, Brazil and South Korea, implying that 67% of steel imports and 55% of aluminium imports are exempted, at least for the time being. With such large chunks of imports being exempt, the benefit for US steel and aluminium firms are significantly diluted, just like the impact for the rest of the world. Barring exemptions, the US metals industry would indeed be supported with a price increase. Such would however come at the expense of those firms that use metals as input, with the latter negative effect outweighing the positives for metal firms. Outside the US, firms would face price pressure of up to 3% for steel and 2% for aluminium.[7] While the current economic impact may be limited, even very limited, the US administration has created a stronger negotiating position: the threat of withdrawal of exemptions can be used to put pressure on countries in trade issues. The US has created a position to bite.

As to the levies on USD 60 billion worth of imports from China, matters seem to be a bit different. Doubts about China playing by the rules of the (WTO) book of trade have a long history in the US and are shared by the EU and Japan. Specifically, the Chinese practice of demanding that US firms operating in China share intellectual property is a thorny issue, as part of a broader claim of unfair Chinese trade practices. The announced tariff levies are part of a two-pronged approach to address the issue, with the other one being a WTO complaint. The approach is well planned as well, with the US trade department having penned a 200-page report, contrasting with the steel and aluminium levies just being underpinned by a presidential campaign promise. The US seems ready to bite.

US trade policy has taken a protectionist bend. That is clear. But, the steel and aluminium levies resulted from what is considered a chaotic process and have so far predominantly helped put the US in a better negotiating position. The approach towards China is better thought through and addresses longstanding and broad based concerns.[8]

Moreover, the protectionist rhetoric has triggered the EU accelerating its trade negotiations with Japan, Mercosur and Mexico.[9] South American countries continue on their path to foster trade integration (see box 3). The Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP: the former TPP) from which the US withdrew immediately after the installation of the Trump administration, was signed in early March after an accelerated process. As the US policy takes a protectionist bend, and prepares for a looming trade war, the rest of the world reinforces trade ties.

[6] There were rumours that the US administration was to target Chinese technological exports to the US, in an attempt to halt China challenging US supremacy in that field. See 'Dominance of future industries at stake', Financial Times, March 24th 2018.

[7] We have detailed the analysis in 'Trump tariffs threaten trade', Atradius Economic Research, March 2018.

[8] See for example Faction and friction, The Economist March 17th, 2018.

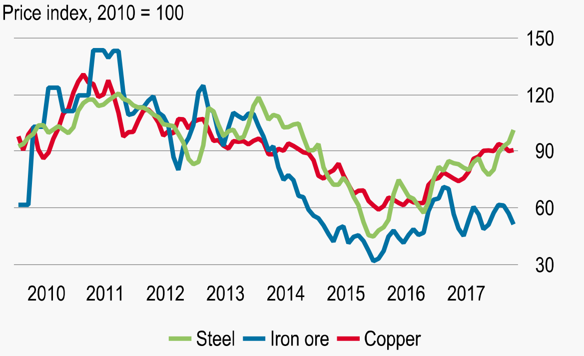
[9] For more details, see 'EU to speed up completion of free trade agreements', Atradius Economic Research, March 2018.

Tariffs pose threat to commodity prices

Commodity prices have raised since our latest Outlook, with the metals prices moving up approximately 10% since.[10] At least, that was the picture until February, before the Trump tariff furore on steel and aluminium broke. The latter though is not expected to disrupt the underlying positive trends, at least not at this stage, other than adding uncertainty to an already volatile market picture. As we have argued, with the US steel measures being so wide and exemptions ample, their direct impact is limited. Rather, fears for a trade war have further fed uncertainty, volatility, and put pressure on the upward trend. Considering the major metals, the iron ore price has benefitted from the relatively favourable developments in the steel sector.[11]

1.7 Commodity prices gain some ground

Price index, 2010 = 100



Sources: Macrobond, Atradius

Whereas we have previously expressed some scepticism of the willingness of China to reduce production capacity, incoming data challenge that view. Incoming data from the Chinese authorities, at least, show the country is on track to meet a steel capacity reduction of 150 million tonnes by 2020.[12] There is also the incentive from the Chinese plan to reduce air pollution by limiting production.[13] Capacity reduction, as well as the strong demand resulting from the global economy and construction in particular, has been a clear support for steel prices. On the back of that, iron ore prices have edged up as well. Copper prices have risen even more prominently, by around 30% y-o-y in 2017. Copper supply was constrained, due to for example a 44-day strike in a large Chilean mine. Output was even somewhat depressed compared to 2016. Higher demand came from the steady growth in the global construction sector and the growth in the electric car market, where heavy copper using batteries are used for recharging. The result was a shrinking supply surplus in the copper market and price support. Aluminium prices have been bolstered by the global economic recovery, increasing almost 20% in 2017.

Market fundamentals are favourable. In 2018, demand is expected to exceed supply. This is because the combination of continued supply constraints and demand growth as the global economy remains in good shape, which will rebalance the markets - away from the current supply surpluses. That will provide support for metals prices. In that sense not much has changed compared to our November Outlook.

What have changed are the Trump tariffs and, even worse, the likelihood of a trade war. To see why this is a risk for commodity prices, reconsider the impact of the 25% levy on steel in more detail. If we leave out the exemptions, US producers will increase prices, potentially to the tune of 21%.[14] That will provide a boost to US production. Steel producers in other countries, however, especially those exporting to the US, will bear the brunt. Their exports to the US are substituted by US producers. Logic suggests that they will first attempt to sell to other markets, putting pressure on prices outside the US, perhaps to the tune of 3%. Those lower prices will subsequently reduce output outside the US. The upshot is two steel prices instead of one, higher than before in the US and lower in the rest of the world. The latter will clearly compress the current upward price trend. The picture worsens further if the EU, faced with additional flows from steel exporters, raises tariffs on steel as well. Then the mechanism just described for the US will apply to the EU as well, and the rest of the world will bear the brunt, facing further pressure on steel prices. It may be clear a tariff on aluminium, or any other commodity, has similar effects.

Though current exemptions prevail, they are temporary. What the market fears is a trade war, with clear negative effects on prices. In that latter context, it should be considered that whereas the US (or the EU for that matter in the example) extends production, the lower production elsewhere does not immediately lead to capacity reduction. Thus, the global picture for the steel industry is then one prone to capacity expansion, where reduction is badly needed. It may be clear that such a foreboding picture spooks the markets. This feeds into prices.

[10] The index includes iron ore, copper, aluminium, tin, zinc, lead and uranium.

[11] Iron ore is a key input component for steel production.

[12] In 2017 Chinese steel production was 834 million ton.

[13] More precisely, it is coming from the Energy Production and Consumption Revolution Strategy (2016-2030).

[14] See Trump tariffs threaten trade, Atradius Economic Research March 2018.

Oil price corridor shifts upward

In November last year, we reported about the oil market being on a slightly upward trajectory, pushing over the imaginary USD 60 per barrel Brent boundary. That hinted the period of relatively calm movement within the USD 50-60 corridor might be over, volatility was back. Now, what we have seen since is indeed more volatility. More importantly, the price corridor seems to have shifted upwards to the USD 60-70 range.

That is somewhat unexpected. The USD 50-60 corridor was a result of the OPEC agreement to curb production and the US shale production flexibility. OPEC production restraint would keep the oil price above USD 50 per barrel; prices above USD 60 would be prevented by acceleration of US shale production. The current truth of the market is that prices do not go below USD 60, whilst there are regular flirts with the USD 70 per barrel price level.

What is going on? Prices were already on the rise when we wrote our November Outlook. That rise followed a USD 44 per barrel trough in June when, despite an OPEC agreement, US production quickly accelerated in response to higher prices. In addition, Libya and Nigeria, exempted from the OPEC agreement, pushed up output. But then US production eased somewhat and, with the global economy shifting to a higher gear, oil stocks began declining. Moreover, on November 30th OPEC plus, crucially, Russia (therefore OPEC+), announced an extension of their production cuts to the end of 2018. This confirmation of the agreement was accompanied by the announcement of an aggregate rate of compliance of 128%.[15] That shored up doubts about the credibility of OPEC+ production restraint and provided strong support for prices as well as US shale production. Indeed, US shale production ultimately rose strongly in 2017, by 670 mb/d, beating all expectations. But that level was simply not high enough to compensate for the impact of the demand surge for oil resulting from the global economic upswing and OPEC+ production curbs. The result was a higher oil price. Volatility moreover is higher due to uncertainty in the geopolitical (namely US and North Korea, Saudi Arabia and Iran, Syria) and trade environment having geared up as well.

The upshot of these developments, particularly the strong demand, is that we now carefully revise our view on the oil price, upwards to the USD 60 – USD 70 range for the forecast period. Given the global GDP forecast, oil demand is expected to steadily grow in 2018, surpassing the 100 mb/d level by the end of the year. It is then expected to level off somewhat in 2019 as economic growth slows. Growth will be particularly strong in Asia, most prominently in India and China, despite the latter country moving its focus away from fossil fuel and towards substitutes. On the supply side, as OPEC+ is expected to continue to show production restraint, the surge in global demand for oil will be met by further US shale production. Still, with uncertainty, especially in geopolitical and trade matters, on the rise, swings in price levels along the way are almost a certainty. These swings, moreover, will be aggravated if investment levels in the oil sector do not take off. In 2017, there has only been a minor increase versus 2016, which marked a second year of 25% investment compression. For 2018, only a modest rise is foreseen. Once it becomes clear that the accumulated investment needs will not be met, large swings in prices, with an upward inclination, can be expected.

In this context, it is important to note that we consider ourselves to be part of a world where, since the Paris Agreement, environmental concerns have taken centre stage. Still, the underlying scenario we adhere to is that the world will not be fossil fuels free. Indeed, as compliance to the Paris Agreement is expected to be only partial, oil demand continues to rise. That will not be true in an alternative scenario developed by the IEA.[16] Such a scenario envisages surpassing the Paris Agreement objectives, but even then, oil demand will still be 75% of its current levels.

1.8 Oil price corridor shifts upward
Daily spot price, USD per barrel Brent

Source: Macrobond

[15] Indeed, this means that OPEC+ production was even 28% lower than agreed.

[16] See the Sustainable Development Scenario in IEA World Energy Outlook 2017.

Monetary policy tightening: Fed gently gears up

In our November Outlook, we concluded that more robust US inflation could be expected. The US labour market stance simply warrants wages to leap up, while the impact of the inflation depressing 'Amazon effect'[17] could not be expected to last forever. The gradual climb of the oil price, moreover, would also provide upward pressure. As in the eurozone unemployment, albeit declining, is still high, wage pressures are far less prominent here. Inflationary pressures are low in the eurozone as well.

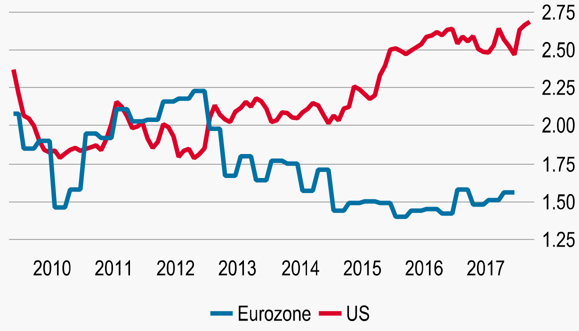
So far, we have seen only some of the expected upward movements in inflation in the US. US unemployment has remained low and effectively unchanged at 4.1%, with the participation rate dipping slightly from its six-month high of 63% to 62.9%. But wage growth continues to hover slightly below 3%, signalling an amount of slack in the labour market. Inflation reached 2.4% in March but some stabilising is evident. Eurozone inflation behaved more in line with what we expected. Unemployment improved to 8.5%, a nine-year low, but at this level, one will not worry about labour market tightness. There is an abundance of slack in the eurozone labour market. Significant wage growth has not been visible nor is it expected over the forecast horizon.[18] Inflation remained low at 1.3% in March, marking roughly a 1.1 percentage point difference with the US.

With these figures in mind, one can question whether the expectation of robust inflation in the US, is still justified. We think it is, and that it has firmed since November last year. This is due to the fiscal policy stimulus that is provided by the US Tax Cuts and Jobs Act legislated in late 2017. It will provide additional US growth through US 1.5 trillion in tax cuts: about 0.5% in 2018 and 2019. This could drive up inflation, as flagged in chapter 2, and that the already higher inflation forecast of 2.5% even contains an upward risk.

The Fed under the new chair Jerome Powell seems clearly aware of this. Still, the call for accelerated tightening of monetary policy is treated with caution. Fed policy is predominantly data-based. Besides inflation, economic activity, especially as reflected in the labour market situation, is closely watched. As the inflationary pressures are perhaps clear, labour market dynamics perhaps less so, with wage growth being rather subdued. Indeed, so far, the monetary stance remains accommodative. We have observed two more 0.25 percentage point rate hikes since November in conjunction with ongoing balance sheet reduction. The latter is crafted by only partially reinvesting the redemptions of the bonds and mortgage-backed securities purchased under the quantitative easing (QE) program. Only amounts received in excess of USD 10 billion on a monthly basis are reinvested, a figure that is to increase gradually to USD 50 billion per month.[19] The result is that the Fed balance sheet has started to shrink since mid-2017 and this will continue. Further rate hiking can also be expected, perhaps three more this year.

1.9 Wage pressures stronger in the US

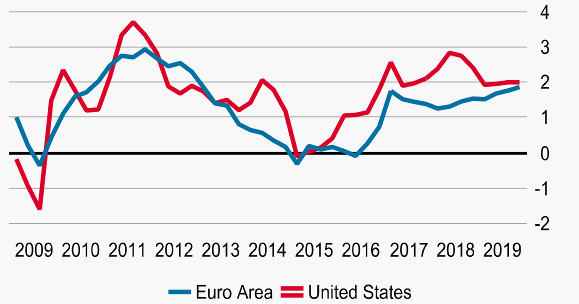
Wage growth, % change y-o-y



Sources: Macrobond, ECB, BLS

1.10 Inflation approaching targets

Headline inflation indices, y-o-y % growth



Sources: Macrobond, Oxford Economics

Meanwhile, in the eurozone the ECB has taken a next, though extremely careful, step towards monetary policy normalisation. The first was made already in late 2017 when an announcement of tapering the asset sales to EUR 30 billion per month was made. It was accompanied with the note that its QE programme would run until September 2018 and the pledge that it would extend or even expand the program if needed. Precisely that latter pledge was removed in the March communication, a clear forward guidance that the programme may be terminated later this year. That is all there is for now, implying an ongoing expansion of the ECB balance sheet, whilst

[17] This effect comes from firms moving to on line sales, lowering costs and generating more competition.

[18] Some wage pressure in the German labour market, such as the 6% wage increase demand from public sector workers, is insufficient to translate into a eurozone-wide effect.

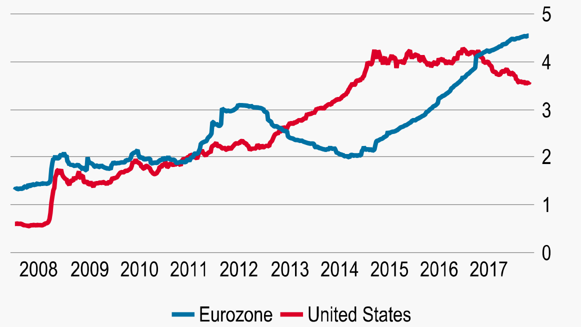
[19] See Federal Reserve Bank, Monetary Policy report, February 2018.

official rates remain at or even below zero. In the course of 2018 the ECB is expected to further clarify its stance, whereby the question is if, and not when, monetary policy normalisation starts. The first step is to stop buying assets, and then to hike rates, starting in 2019. This may be accompanied by some form of balance sheet reduction, comparable to the US.

As bond yields are rising and the equity market rally has come to a halt, financial market conditions as such remain relatively benign. Firms are still relatively easily funded. This is what central banks care about as well. Because if the financial environment changes, especially if it does so rapidly, investments may falter.

1.11 ECB and Federal Reserve balance sheets

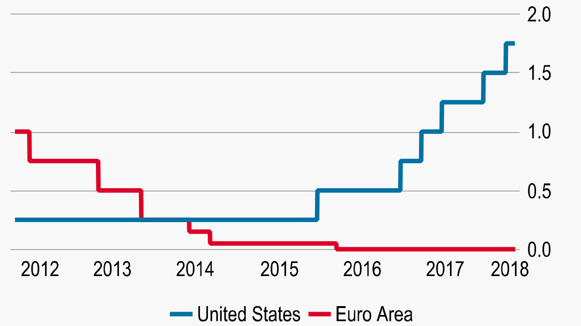
Total assets, trillions of euros



Sources: Macrobond, Federal Reserve, ECB

1.12 ECB vs Fed policy rates

Percent per annum



Source: Macrobond

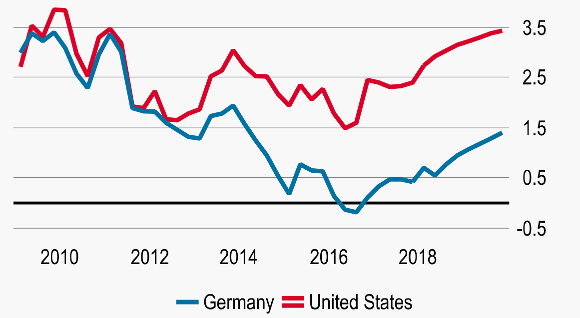
Bond yields up as dollar weakness surprises

Monetary policy stance is one thing, steering financial markets, which is what really matters for finance of economic activity, is another. Given the picture of monetary policy in the US and eurozone sketched above, one would expect that short-term rates diverge. US bond yields are expected to be up, with the eurozone ones, as represented by the German ones, more or less flat. That is indeed what we see, marking the effectiveness of forward guidance.

For long-term bond yields, official rates as well as inflation expectation differentials come into play. We have seen the latter diverging, with the US inflation moving up as a result of, amongst others, US fiscal stimulus. That suggests increasing divergence in the long-term bond market as well. This, however, is not what we observe. Beside the US 10-year Treasury yield, the German 10-year bund yield has gone up as well. The missing link here is hidden in the analysis in the previous section: ECB forward guidance. It alerted the market to future higher interest rates, driving up yields.

1.13 Yields expected to continue increasing

10-year government bond yields



Sources: Macrobond, Oxford Economics

Short-term yields, on the other hand, are indeed diverging which should put upward pressure on the US dollar. But this is not happening: the dollar has continued to slide – losing more than 7% of its value since January 2017, in real effective terms. For this somewhat surprising phenomenon, explanations can be found. First, the US dollar is still at historical highs and is considered overvalued as such. At the same time, economic growth in the rest of the world growth is accelerating compared to the US.[20] The dollar pressure continues as long as the overvaluation and catch-up demand from the rest of the world are being corrected. Second, there is ongoing dollar lending by firms and governments across the globe. The dollars borrowed may partly find their way to the exchange markets, depressing the dollar. Third, monetary policy expectations are shifting.[21] Market expectations have shifted towards a more hawkish ECB approach, implying a call for euros and thus downward pressure on the dollar.

The first two reasons create an effect that lasts as long as the underlying causes, GDP growth catch-up and US dollar lending, persist. The third reason creates a one-off effect. Banking on these former two effects to persist for a while, and boosted by the monetary policy expectation shift, the dollar is overvalued. This is notwithstanding the

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[20] Dollar weakness: pumping the late cycle. Oxford Economics, February 19, 2018.

[21] Davies, G. Dollar weakness driven by monetary policy after all, Financial Times February 28, 2018.

growing interest rate differential at least for short-term yields. Oxford Economics expects the USD to depreciate almost 12% in 2018 and a further 2% in 2019.[22]

Equity market rally halts, volatility returns

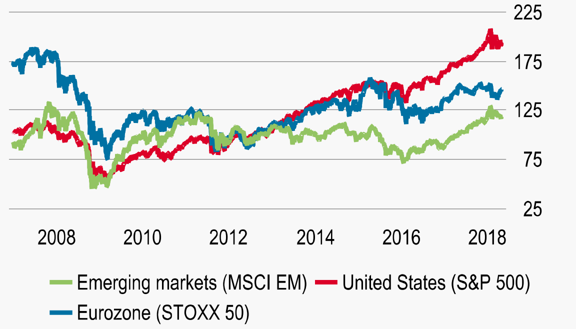
In our November Outlook we mentioned the possibility of a correction on financial markets. This was based on the equity rally that had been going on since mid-2016. Of course the US tax reform of late-2017 provided another boost to the ongoing optimism in the market. Although we never believed it, the sky seemed to be the limit to some. There were no signs of something brewing either. The VIX index, which is indicative of uncertainty in the financial market, was extremely low. That the SKEW index was still elevated and even leaping up. But this was less of a worry for most investors. The SKEW index just measures the size of the risk given a tail event, not that such a tail event would happen.

That has changed now. The defining moment was the end of January, when a favourable US labour market report was released, suggesting a large annual increase in hourly earnings? That triggered inflation fears and thus fear for - unanticipated – accelerated Fed hikes. Global equities took a hit, with all major indices lower in a week's time: the Dow Jones Industrial Average 4.6%, the FTSE 100 8.2% and the MSCI Emerging Markets 7.5%. Though substantial, these drops should be evaluated in context; the October 1987 Dow Jones fall was 23%. The January drop was turmoil, not a crisis. Moreover, the markets have recovered somewhat since, although the rally has now clearly halted. There is a limit below the sky.[23]

The late January turmoil coincided with a spike in US stock market implied volatility to levels of 2015, when the Chinese stock market rumbled. BIS research suggests the spike was accentuated by traders that had taken a bet on persistently low volatility and had to unwind their positions to limit losses. Implied volatility is now at a higher level, which the BIS considers 'healthy' as too low levels suggest an illusion of calm.[24] We think volatility has returned to levels that are more normal. Meanwhile, the SKEW index of the S&P 500 suggests that the probability of a large equity market correction, given such a correction, remains elevated. It has not markedly increased since November, though.

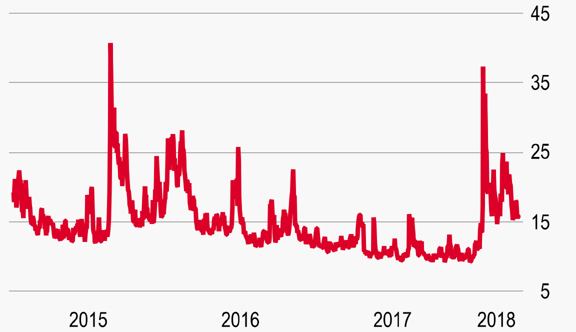
As bond yields are rising and the equity market rally has come to a halt, financial market conditions as such remain relatively benign. Firms are still relatively easily-funded. This is what central banks care about as well. Because if the financial environment changes, especially if it does so rapidly, investments may falter.

1.14 Stock rally stabilises
Index, 2012 = 100



Source: Macrobond

1.15 Volatility spikes
S&P 500 volatility index (VIX)



Source: Macrobond

Elevated political risk

In the first section, we have discussed economic policy risk and concluded that the relevant policy indicator, the Economic Policy Uncertainty Index, was relatively low. Here we want to turn to an element of risk that we have long disregarded in previous Outlooks, geopolitical risk. That is the risk of wars, terrorist acts and tensions that affect the normal and peaceful course of international relations. Such events clearly have an impact on the economy as such. But it is not that element, the materialisation of a risk, which has a protracted impact. What does is the threat of these events. That negatively affects decisions of households and firms to spend, and thus lowers economic activity and stock returns, and

[22] The figure of 12% is in accordance with an estimate of the overvaluation of the USD of 10% that the IIF has made. See How Big is the US Trade Imbalance? IIF, January 22, 2018.

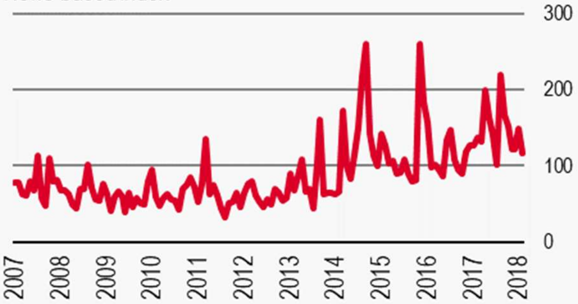
[23] Some broader reasons for the correction are (i) that investors had become a bit complacent, as signalled by their high exposure to equities and unwillingness to pay insurance; (ii) a rethink of the global economic and financial outlook; and (iii) the increasing bond yields, which suggest at least some portfolio substitution. See Boo!, The Economist, February 10th 2018.

[24] BIS Quarterly Review, Media Briefing, Remarks by Claudio Borio, March 2018.

leads to capital flow to safe havens over a longer period of time.[25]

1.16 Geopolitical threat at elevated level

News-based index



Source: Caldara & Iacoviello

Both elements, the risk of an event and the event as such, are captured by the Geopolitical risk index (GPR Index), a news-based index. The current level of this index is elevated: during the years 2007-2014 its level was around 75, since then it hovers around 130-135. Recent spikes relate to the Russian annexation of the Crimea (2014), ISIS escalation (2014), Paris attacks (2016) and North Korean nuclear threat (2017).

For the forecast period, we clearly have no shortage of threats, especially now that the US is taking a more assertive, self-centred attitude towards foreign policy.[26] The conflict in Syria regularly threatens to create a military confrontation between rebel backing US, UK and France on the one side, and Syrian regime backing Russia on the other side. The carefully drafted multiparty nuclear deal with Iran is under severe scrutiny in the US, with the US president having classified the deal 'the worst ever'. Containment of Iran's nuclear ambitions is under pressure as well. On North Korea there have been exchanges of unpleasant language between the US president and his North Korean counterpart. North Korea is rapidly developing into a nuclear power. In Yemen, archenemies Iran and Saudi Arabia are fighting a proxy war that may escalate into a wider Middle East conflict. Resolving these, or at least bringing some of these back to lower levels of conflict will clearly help bolster the current upswing in the global economy, or at least prevent that it is threatened by it. The GPR Index should be brought down, but we have no signals that this will occur.

[25] See Caldara, D. and Iacoviello, M. Measuring Geopolitical Risk, Board of Governors of the Federal Reserve System, February 2018.

[26] The most recent underscoring hereof is the nomination of John Bolton, a well-established foreign policy hawk, as US National Security advisor to the President.

Risks to the Outlook

In our November Outlook we have already mentioned US protectionism as a potential, albeit lower, risk to the Outlook. At that time, we (and a lot of others) were not convinced the US would really follow a protectionism agenda. That has now changed, for reasons we have discussed in this Outlook. The risk of a trade war based on US protectionism is clearly the top risk to the outlook. Fed policy being misguided remains a risk, but is simply being overtaken by US protectionism. A not carefully managed China slowdown, or hard landing, also remains on the list, but it has been moved down as well for similar reasons. Finally, we have changed the sequence of the remaining risk factors as well, now that we are less comfortable with the financial market situation and the geopolitical situation has clearly worsened. Oil price volatility is less of a worry, though not completely absent.

US protectionism turns into trade war. What we have seen so far is limited protectionist measures from the US, on steel and aluminium and on Chinese imports in general. The latter has not yet been implemented, and neither have Chinese retaliation tariffs (with some exceptions). Even if implemented this is not yet the picture of a trade war, simply because it regards only a limited part of bilateral trade. At this stage though, it is no longer realistic to disregard much further steps by the US. One can then imagine tariffs on all Chinese imports, and other Asian countries. In addition, NAFTA may break-up as the US may no longer participate. In such a scenario, or another where for example the EU is involved, we face a trade war. This would have severe consequences, with global GDP growth falling by 0.5 percentage point, with – in this example - Asian countries and Mexico being in the middle of the trade war and bearing the brunt, just like the US itself. Trade growth would plummet.

Fed policy. Our baseline scenario is a well-guided and well-targeted tightening policy by the Fed essentially following the current approach. The new chair, Jerome Powell, has started well in this respect and is expected to continue the line of Janet Yellen. Powell is not a trained economist, but the recent appointment to the chair of the New York Fed of John Williams, who is a well-respected economist, provides confidence. Still, even a careful, data driven approach that is pursued has a risk, particularly now that the US administration uses fiscal policy tools to stimulate the economy in an upswing. This is unorthodox economic policy and the Fed may be forced to react by accelerating hikes. If this is not well-guided, the higher US rates could trigger capital flows away from the emerging economies, hampering finance and growth opportunities. In such a scenario, firms, households and governments across the globe will face higher finance costs. That will restrain global growth.

Table 1.2 Risks to the global economic outlook

	Risk	Symptoms	Effects	Probability	Impact
1	US protectionism	Trade barriers such as tariffs or targeted restrictions introduced	Severe constraints on trade with US	moderate	high
2	Misguided Fed policy	Financial market turbulence, flows to emerging economies plummet	Tighter credit for firms in emerging economies; debt service issues	moderate/low	high
3	China hard landing	Unstable banking sector, credit constraints, acceleration capital outflows, pressure on currency	Financial market volatility, spill-over into dependent (REM) economies	low	moderate
4	Financial market correction	Strong, rapid and sustained correction on overvalued equity markets, not triggered by risk 1-3 or 5-6.	Fall in confidence affecting spending. Negative wealth effects households affecting consumption	low	moderate
5	Geopolitical risk	Increasing tensions in Middle East, especially between Saudi Arabia and Iran, and/or Korean peninsula	Middle East: Lower oil production and GDP, oil price volatility, fall in confidence. Korean peninsula:confidence declines, predominantly regionally	low	moderate
6	Oil price volatility	Lagging oil industry investments with strong demand. Pressure on oil price stocks.	Uncertainty affects confidence, especially firms. Unexpected swings in inflation. Lower investment.	low	moderate

Source: Atradius Economic Research

China hard landing. The Chinese authorities have proven consistently able and willing to uphold the GDP growth targets that were set for the economy. They have used fiscal and monetary space to this end. Therefore, from this one can be confident that a sudden drop in economic growth or a hard landing (which has never been the Atradius main scenario) has moved further away – again since the November Outlook. Moreover, plans to reign in credit growth exist and are being implemented. Nevertheless, the financial vulnerabilities in the economy, such as debt levels, have continued to grow. Chinese authorities may be forced or feel compelled to pursue a more aggressive course on restraining credit growth. That would bring in the possibility of a hard landing again. For that reason, we cannot discard it.

Financial market correction. The surge in equity prices that we have seen in the aftermath of the Trump election has halted and volatility is back. There has been only a limited correction and one can consider more volatility a healthier reflection of investor attitude. Still, there is a risk that in a world still awash with money, equity prices, and more broadly, asset prices, are too high. The VIX index movements and the level of the SKEW suggest that, if a correction occurs it could be large. And that the probability that a correction occurs has gone up. The impact of such a correction would be exacerbated if Fed policy is misguided or poorly targeted. Damage will be done because firms as well as households may react by restraining spending. That will curb growth.

Geopolitical risk. The geopolitical risk indicator signals elevated levels of geopolitical risk. That hampers growth, especially via lower confidence of households and firms. Tensions in the Middle East and the North Korean nuclear assertiveness were suspects already identified in our previous outlook. Since then, the US administration has stepped up its assertiveness with a more self-centred approach. The multiparty Iran nuclear deal for example has been at risk since the beginning of the Trump presidency. With a new Security advisor appointed who is reputedly a foreign policy hawk matters have not improved, and neither have risks.

Oil price volatility. Our baseline scenario is that the oil price gradually increases within the USD 60-70 per barrel range over the forecast period. This is based on an investment level that accommodates oil demand over the medium term and causes no shocks in demand development. If such investment levels turn out insufficient, the oil price can go up swiftly and become very volatile in the short term. This is just because the market is no longer confident about a gradual development. Then, the global economy will face higher and more volatile oil prices, hampering growth in oil importers such as the Eurozone. The volatility will also hamper investments in the industry and limit the ability to reset macroeconomic policy in the oil exporting countries. Global growth will be negatively affected in such scenario.

2. Advanced economies – Prospects and risks

End to the good times coming closer in sight

Economic strength across advanced markets has been one of the key drivers of the broad-based global upswing since 2017. The outlook for 2018 is similarly strong before some momentum begins to ease in 2019. The US is the only economy whose growth is expected to accelerate significantly in 2018 due to fiscal stimulus on top of its solid economic fundamentals. But this unorthodox policymaking is increasingly a downside risk for the US, and in turn world, economy. The eurozone outlook remains firm but some euro strengthening will drag on its exports, increasingly weighing on GDP growth in 2018 to 2019. The UK also remains resilient and is benefitting from higher external demand but uncertainty related to Brexit remains a downside risk. A more uncertain trade picture, both due to US policy uncertainty and, more importantly, the slowdown in China, is weighing on the steady outlooks for Advanced Asian countries.

Table 2.1 Real GDP growth (%) - major markets

	2017	2018 f	2019 f
Eurozone	2.5	2.2	1.8
United States	2.3	2.8	2.4
United Kingdom	1.8	1.7	1.7
Japan	1.7	1.5	0.9

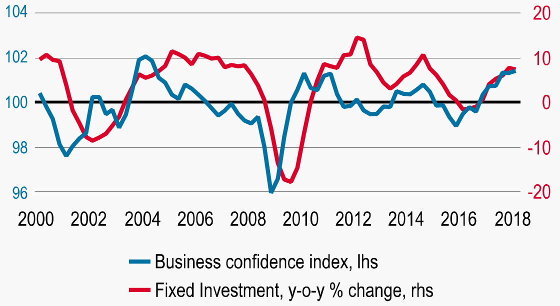
Sources: Macrobond, Oxford Economics

US economy firing up at the future's expense

After a solid performance in 2017, the US economy entered 2018 with strong momentum. The announcement of tax reform in December 2017 will bring the rate of growth up even further – motivating a 0.2 percentage point revision up for our 2018 forecast to 2.8%. Strong growth is expected to last into 2019 but the short-term nature of fiscal stimulus means the positive effects are likely to ease slightly in the year. While the US outlook for 2018 and 2019 is characterised by good news, more aggressive monetary tightening and trade tensions may translate into slower economic growth in the latter-part of our forecast period.

The pickup in economic growth in 2017 was exclusively driven by strong business investment. This is a very positive development for the long US economic recovery, which to this point has relied too heavily on consumers. Business investment reached 7.7% annual growth in Q4 of 2017 and is expected to continue this trend in 2018, in line with increasing business confidence which has now reached 2004 levels (see figure 2.1). A large part of the investment recovery was a rebound in investment in the oil and gas industry in response to higher energy prices. However, as the unsustainable rate of drilling expansion has reversed, investment continues to pick up and investment intentions across sectors are buoyed by tax reform.

2.1 Business investment boom supported by high confidence

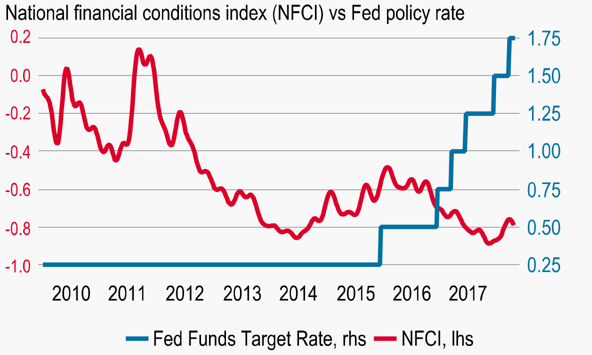


Sources: OECD, BEA

Private consumption has remained strong in the US through recent years, underpinned by declining unemployment, real wage growth, and continued loose credit conditions. The unemployment rate is steady at 4.1%, a 17-year low, wage growth is steady at 2.7% and labour force participation has ticked up to only 62.9%, from 62.7% in November. Despite acceleration in Fed tightening, credit conditions remain easy, as evidenced by the national financial condition index, supporting household spending in 2018. Some strain may be in the cards though for 2019. By this time, higher interest rates are expected to weigh on consumer spending and the very tight labour market is expected to push inflation higher than targeted, further reducing spending power. Price pressures have already been intensifying due to the weaker dollar, tightening labour market, and strong housing market. Protectionist measures could also put further upward pressure on prices. Inconsistent wage growth and the low participation rate indicate that the economy is still not at full employment suggesting there is still room to push prices further. Thus inflation is expected to continue ticking up as unemployment falls further to a projected 3.6% by end-2018.

2.2 US financial conditions remain easy

National financial conditions index (NFCI) vs Fed policy rate



Sources: Macrobond, Federal Reserve Bank of Chicago

Net exports exerted a slight drag on economic growth in 2017 as stronger domestic activity caused the pace of import growth to exceed that of export growth. Despite lower energy import demand thanks to greater energy self-sufficiency, the robust economic outlook for domestic consumption and investment indicate that net exports will continue to drag on growth this year and next. The negative trend here is also in spite of the weaker US dollar, discussed in Chapter 1. The weaker dollar, while not reversing the negative contribution of net exports to growth, should contain the negative effect, by making imports more expensive and exports more competitive.

Fiscal stimulus to boost growth but increases risk of overheating

In December 2017, Congress passed the Tax Cuts and Jobs Act (TCJA), the most sweeping overhaul of the tax code in decades and the most important legislative victory of the first year of the Trump presidency. The main tenants are a reduction in the corporate tax rate to 21% from 35% and related measures to facilitate business investment. The Tax Policy Center estimates that the TCJA should increase the average American household income in 2018 by USD 1,200. While this should provide some boost to private consumption, the extent is highly uncertain since most benefits will go to more wealthy households.

The TCJA is accompanied by the Bipartisan Budget Act of 2018 (BBA). The new budget resolution increased domestic and military spending caps, bringing expenditures in 2018 and 2019 about USD 150 billion higher. Higher government consumption alongside the jolt to business confidence and investment prospects however ensure higher GDP growth than previously expected. While this significant fiscal stimulus will boost GDP growth in 2018 and 2019, it runs the risk of bringing the next downturn sooner. This is because it is pro-cyclical – coming at a time when US economic growth is accelerating, a decade into the current economic expansion. It could drive inflation pressures more quickly than currently expected, forcing the Federal Reserve to hike rates more quickly to avoid overheating.

The impact on government finances is also negative and could also contribute to the next downturn. Despite rising GDP growth, the lower revenue and higher spending that the US government will pursue will raise public debt as a share of GDP: the Congressional Budget Office (CBO) estimates public debt will reach 96% of GDP in 2020. Should growth not prove as strong as expected, the federal deficit and debt levels would widen quicker. Higher debt levels and higher future interest rates will limit the tools at the government's disposal to support the economy in case of a recession, producing a deeper downturn than otherwise.

Box 1 America's trade deficit will stay in 2018 and 2019

The Trump administration has shifted US policy away from free trade to protectionism, motivated in part by the trade deficit or the fact that the US imports more than it exports. However, the trade deficit is neither bad for the economy nor is it likely to be effectively addressed by protectionist measures.

The balance of trade does not exist in a bubble – it is a part of a country's national accounts and as such is affected by much more than imports and exports. The trade balance is the largest component of the current account, which also includes income balance and transfers. A current account deficit is balanced by a corresponding surplus in the capital and financial accounts, meaning more foreign money and investment flows into the US than the other way around. Essentially, American households, companies, and government are using world savings to meet their current investment and consumption demands. This is neither good nor bad and offers little indication of the direction of the US economy. To some extent, one can argue that it shows the relative strength of the US to the rest of the world, as it demonstrates higher demand, confidence and investment. The safe haven status of the US dollar and assets ensure that foreign investment will continue to flow in and finance the trade deficit.

The trade deficit cannot be reduced as simply as restricting imports through tariffs. The structural shift in trade to lower-cost manufacturing abroad and the historically strong US dollar increase demand for foreign products in the US. At the same time, the US has developed to a services-driven economy (80% GDP) and has a services trade surplus with the rest of the world. On top of the structural shift in the US and global economy, bilateral import tariffs are also likely to be ineffective in narrowing the trade deficit. In the absence of significant and rapid behavioural shifts of US consumers to save more, targeting individual countries like China, with which the US has a large trade deficit, would simply lead to either import substitution to other countries – reducing the bilateral deficit with one country and increasing it with others – and/or higher costs for businesses and consumers.

Mr Trump's policy prescription is also self-defeating for the trade balance and potentially good for moderating economic growth. The US economy has been outperforming peers through the recovery from the 2008-9 financial crisis, creating higher demand for imports compared to foreign demand for US goods and services. Higher import growth compared to export growth implies a drag on GDP growth. Now with late-in-the-cycle fiscal stimulus, import demand is expected to pick up further, which could help in preventing the US economy from overheating. As it exerts a drag on GDP growth, the ability to increase imports helps keep a lid on inflation and thus interest rates.

Monetary and trade policy could put sand in the wheels of the US expansion

While economic fundamentals are strong, buoyed by strong private consumption and business investment, and further supported by fiscal stimulus, downside risks in the form of tighter monetary policy and trade tensions may materialise in the latter part of our forecast period.

Thus far, the economy has responded well to rate hikes, offering confidence to potentially accelerate the pace of monetary tightening. After four hikes in 2017, the Fed raised its policy rate another quarter-point in March 2018 to the still very low range of 1.5% to 1.75%. This was the first major policy decision under the new chairman, Jerome Powell, and was smooth and in line with expectations. The Fed raised its economic forecast significantly from the previous quarter, taking into account the tax reform and lifting of government spending caps. They also now have begun hinting at a more aggressive tightening pace. Market expectations point to two more 25 basis point hikes to 2.25% in 2018, while the Fed expects three more to 2.5%. Market and Fed expectations were both raised for 2019 to 2020 though, expecting at least one more hike than previously expected. Now, the median FOMC expectation for end-2020 is 3.4%, 50 basis points higher than the long run estimate – in other words higher than the underlying strength of the economy should suggest. This more aggressive stance and commitment to act in the face of rising inflation may mean interest rate hikes more quickly than market expectations, causing households and businesses to rein in spending, and bringing on the next recession sooner.

Trade policy missteps could also have significantly negative ramifications for the US economy. At this time last year, we were relieved to see that President Trump's campaign-trail trade rhetoric was 'all bark, no bite', but now we are seeing some action beyond symbolic steps. Further protectionist measures, on top of those already announced, would hurt the US economy by curtailing growth and employment and leading to higher domestic inflation. It would create a double whammy through a loss of competitiveness of US firms and an acceleration of the Fed's monetary tightening path. It would also disproportionately hurt key industries that may be targeted by trade partners, such as the agricultural sector. Oxford Economics scenario testing estimates a 0.9% negative impact on average annual impact on GDP growth over the next five years in this case.

Eurozone: enjoying the boom while it lasts

The eurozone finds itself in a sweet spot, characterised by robust GDP growth, declining unemployment, strong business and consumer confidence and loose financing conditions. The broad-based economic expansion is forecast to continue in 2018, when we expect eurozone GDP to expand by 2.2%. This is slightly higher than expected during the November Economic Outlook.

While eurozone growth figures point to robust performance, recent developments in sentiment indicators suggest that the growth cycle is nearing its peak. After reaching record levels towards the end of 2017, the European Sentiment Indicator (ESI) and the composite PMI declined somewhat at the start of the year and held steady in April. This indicates that the growth cycle could be reaching an inflexion point. Moreover, there are a number of risks that could threaten medium-term growth in the eurozone, including Brexit and rising protectionism.

Table 2.2 Real GDP growth (%) - eurozone

	2017	2018 f	2019 f
Austria	3.1	2.5	1.6
Belgium	1.7	1.6	1.7
France	2.0	2.1	1.9
Germany	2.5	2.3	1.8
Greece	1.3	1.6	2.7
Ireland	7.8	4.9	2.2
Italy	1.5	1.5	1.1
Netherlands	3.3	2.5	1.7
Portugal	2.7	2.2	1.9
Spain	3.0	2.9	2.4
Euro Area	2.5	2.2	1.8

Sources: Macrobond, Oxford Economics

Domestic demand remains the main pillar of GDP growth in 2018. Consumption growth is likely to remain robust, while investment is expected to increase at a higher rate in 2018 compared to last year as sentiment remains strong and capacity utilisation rates are increasing. On the other hand, the appreciation of the euro is slowly turning into a headwind for export growth.

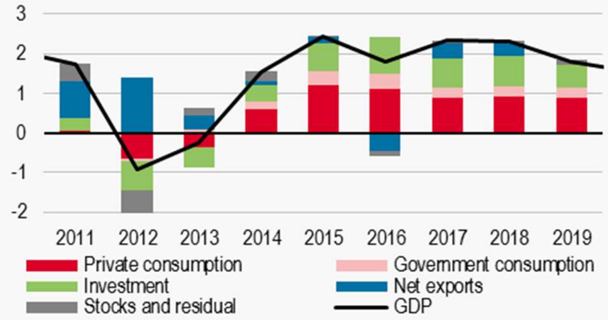
Domestic demand accelerating

Domestic demand remains the main growth engine contributing 2 percentage points to 2018 GDP growth. Private consumption growth continues to benefit from an improving labour market, moderate inflation, accommodative monetary conditions, and strong consumer sentiment. Private consumption is expected to grow by 1.6% in 2018, in line with last year.

Employment momentum strengthened in H2 of 2017. The unemployment rate remained at 8.5% in March 2018, the

2.3 Eurozone growth to cool slightly

Eurozone GDP and components, y-o-y %



Sources: Macrobond, Eurostat, Oxford Economics

lowest since 2008. The rate of job growth is likely to remain robust this year. We forecast an unemployment rate of 8.2% in 2018. The neutral rate of unemployment is estimated to be around 7%.[27] This implies there is still considerable slack in the labour market.

Wage growth is showing some signs of improvement but remains subdued. Over the past four months, the inflation rate declined due to lower contributions from food and energy. Non-energy and services contributions, which are better measures of underlying inflationary pressures, remained more or less constant. In 2018, the inflation rate is expected to moderate to 1.4%, slightly down from last year's 1.5%. This will provide support to real disposable income growth. However, the below-target inflation forecasts are expected to keep the ECB in stimulus mode (see Chapter 1).

Despite improvement of the eurozone labour market, wage growth remains subdued and is unlikely to generate strong inflation pressure in the short-term. This is leading to fears that the traditional negative relationship between unemployment and wage growth has been broken.[28] Figure 2.3 shows that lower unemployment was clearly associated with wage acceleration in the period 1998-2000. This relationship was less clear between 2011 and 2017. A number of factors could explain the 'broken' relationship: reduced bargaining power of workers, driven by lower unionisation rates, increased migration, and technology which have given employers more leverage over workers. There is also a branch of economists that claim inflation is behaving differently than in the past: weak productivity growth may be causing low inflation and inflation expectations may be anchored at lower

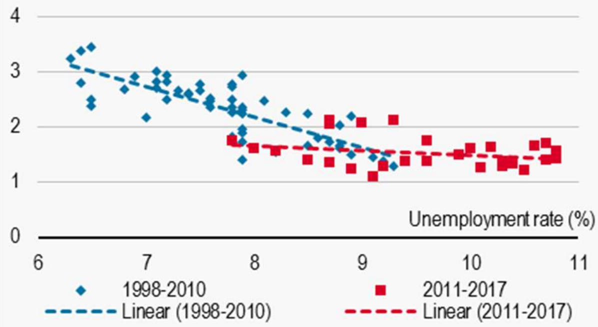
[27] Technically this is called NAIRU, or non-accelerating inflation rate of unemployment: the level of unemployment at which inflation is constant.

[28] The inverse relationship between unemployment and wage growth is known as the Phillips curve, named after New Zealand economist William Phillips.

levels (so that there is no need for workers to demand higher wages)[29].

2.4 Phillips curve has flattened

Compensation per employee, y-o-y % growth



Sources: Macrobond, ECB, OECD

However, the claim that the link between unemployment and wage growth is broken, may prove to be premature. With unemployment declining, labour market slack is gradually disappearing. The decline in unemployment will eventually feed into higher wage demands and higher inflation. There are cautious signs of this happening in relatively tight labour markets, particularly in Germany.

Investment growth is expected to accelerate to 3.4% in 2018, from 3.1% in 2017. Investment is supported by strong business sentiment, tight capacity and the continued strength of bank lending to firms. The rate of capacity utilisation in the manufacturing sector is showing steady improvement and in December 2018, the Business Climate Indicator reached the highest level recorded since 1985. Despite edging slightly lower at the start of this year, it remains high.

The eurozone banking sector is gradually growing in better shape. Bank lending to non-financial corporations and households continued to expand over the second half of 2017. Leverage remains high, but nonperforming loans (NPLs) have been showing improvement. Italian banks are still a weak spot, with NPLs standing at 16%. The nascent economic recovery and the pressure to deleverage are likely to keep lending growth constrained.

External environment

Momentum in the global economy remains strong, as the broad-based cyclical upswing continues, buoyed by the rebound in investment and trade, still favourable financial conditions and a supportive policy mix. While eurozone exports benefit from the cyclical recovery in global trade, the appreciation of the euro is acting as a counterweight. On balance, the real effective exchange rate has appreciated by 1.3% since November last year. In bilateral terms, it has been gaining value against the US dollar (3.2%), driven by lower political uncertainty and expectations of a faster pace of monetary policy normalisation in the eurozone. Despite the expected further appreciation of the euro, export growth is forecast to remain robust in 2018. Extra-eurozone exports are expected to expand by 5% in 2018, in line with the historical average.

2.2 Euro appreciates against USD

November 2017=100

Source: Macrobond

Risks are balanced in the near term, but important risks remain for the medium term. In the short term, the political situation in Italy remains a risk for eurozone stability. The Italian elections proved a major victory for populist parties and loss for Renzi's Democratic Party. The coalition talks are likely to become lengthy and potentially messy. The most likely result is a hung parliament, but there is no clear expectation as to which parties are willing to join the government. A second election cannot be ruled out.

In the medium term, the return of protectionism and Brexit could throw sand in the wheels of eurozone recovery. The recently announced transition agreement should ensure limited Brexit-related impact in our forecast period, but any subsequent barriers to trade and investment will have a negative impact on countries exposed to trade with the UK. Regarding protectionism, the European Union is on track to get exempted from the steel and aluminium tariffs announced by US president Donald Trump (see Chapter 1). In 2017, the US imported USD 6.6 billion of steel from the EU (23% of total US steel imports). If, contrary to our expectations, EU metals exports to the US would become subject to a tariff, the direct economic impact will be limited. However, an escalation of the trade war could jeopardise other sectors, such as the European car industry (Box 2).

While protectionism is currently grabbing headlines, there is also positive news on EU trade. European policymakers are taking steps to reduce vulnerabilities to negative external developments by accelerating free trade

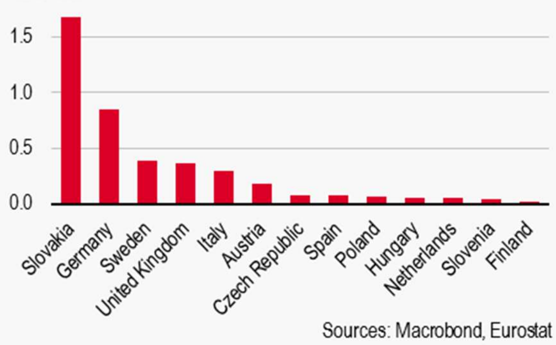
[29] Broken Phillips Curve a Symptom of Lower U.S. Inflation Expectations, Pimco, May 2017.

agreement negotiations with major trading partners like Japan and Mercosur[30]. This should help mitigate the impact from the manifestation of protectionism risks and could even be considered an upside risk.

Box 2 Cars: Europe's Achilles heel?

One driving force behind the protectionist bend of the US administration seems to be frustration over the trade deficit with various countries.[31] The eurozone as a whole runs a trade surplus of USD 133 billion with the US. In the event of a trade war, Trump is likely to slap an import tariff on European cars. In that case, he would hit Europe where it hurts most. In 2016, the EU exported USD 38 billion worth of cars to the US. The European countries most exposed to the US market in terms of road vehicle exports as a percentage of GDP are Slovakia, Germany, Sweden and the United Kingdom. The economic damage from an import tariff on cars is expected to be much greater than one on steel and aluminium. A 35% tariff on European cars, for instance, could cost Europe USD 17 billion each year in export revenues.[32]

Road vehicle exports to the US



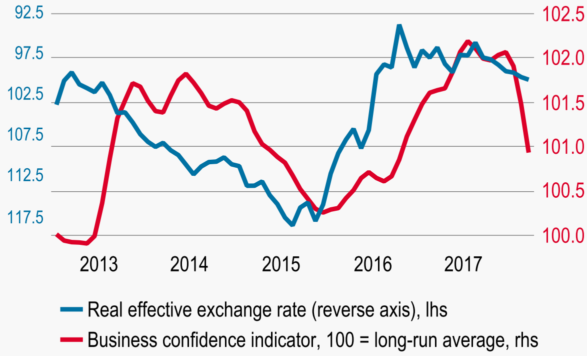
Sources: Macrobond, Eurostat

UK prospects are steady but fragile

The story of the UK economy post-Brexit referendum is one of resilience. In 2017, growth held up at 1.8% (as opposed to the 1.5% projected in our November Outlook) following an unexpectedly strong Q4. Manufacturing output has surged and industrial production, at 2.1%, reached its highest level in seven years in 2017. Despite this strong momentum entering 2018, Q1 growth disappointed with only 0.1% growth q-o-q, the slowest pace since 2012. Some of the slowdown is due to the one-off effect of bad weather but also a slowdown in the construction sector and weakening consumption. Despite the rough start to the year, we still forecast a 1.7% growth rate this year and next, but with higher downside risk.

Uncertainty surrounding Brexit does continue to cloud the outlook. Business investment slowed to 0.9% in 2016 and 2017, following a nearly 5% per year average from 2010 to 2015. The outlook for 2018 and 2019 is slightly better with 1.7% and 2.7% forecast respectively, but remains below average and confidence is beginning to weaken, but remains positive. The modest 0.3 percentage point boost to GDP that net exports brought in 2017 thanks to the sharp depreciation of the pound is expected to ease slightly as the pound strengthens and UK exports lose competitiveness.

2.6 UK confidence rally reversing



Sources: Macrobond, BIS, OECD

Consumer spending has been supported by employment gains, high borrowing, and a drawdown on savings, but is increasingly dragging on GDP. January 2018 marked the 12th consecutive month of decline in real wages, restraining Britons' spending power. Lower spending power for consumers is behind the mere 0.3% expansion of the services sector in Q1, which accounts for 80% of the UK economy. This squeeze should be nearing an end though, as the pace of nominal wage growth has been accelerating, up 2.8% y-o-y in the three months leading to January, its highest rate since September 2015, and inflation has eased slightly to 2.5%, still far above target, but down from its peak of 3.2% in November 2017. Inflation is expected to stay elevated but to ease to below 2% by late 2018 as the base effect of sterling weakening falls out and oil price expectations stabilise. Private consumption growth, however, will be slightly strained in 2018 and 2019 by the government's fiscal tightening and higher interest rates.

The brighter outlook for real wage growth arrived at the same time as other good news. In the March EU summit, it was announced that a transition period following Brexit in March 2019 to December 2020 was agreed. This effectively removes the risk of a cliff-edge Brexit next year, offering relief to many firms with brighter prospects for a smooth Brexit. Combined, these developments

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[30] 'EU to speed up free-trade agreements', Atradius, March 2018

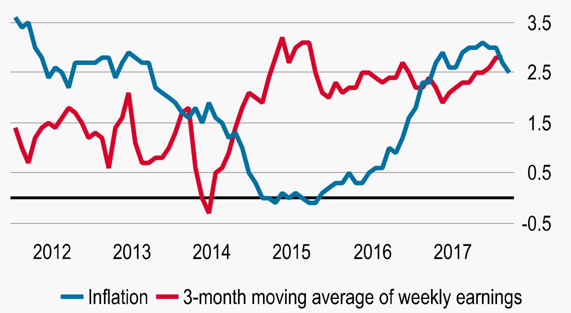
[31] Trump reportedly calls Germans 'very bad,' threatens to end German car sales, https://www.cnbc.com/2017/05/26/trump-calls-germans-very-bad-threatens-to-end-german-car-sales-reports.html (26 May 2017)

[32] Still on the road? Assessing Trump's threat to European cars, Bruegel, March 2018

should support a steady year of 1.7% growth in 2018. This was previously expected to give the Bank of England the leeway to hike rates again to 0.75% in its May meeting, the weak Q1 GDP readings effectively eliminated the chances of this. The prospect for a hike later in 2018 is also lower as the BoE slips back into wait-and-see mode. While the extension of the transition agreement eases some pressure for Brexit negotiations, it is still an extremely tight timeline to establish the future relationship of the UK and EU.

2.7 Real income squeeze easing in UK

% change y-o-y



Sources: Macrobond, ONS

Advanced Asia: China slowdown has more impact than US trade policy

Following a strong 2017, economic growth in Advanced Asia is easing in 2018 and 2019. Higher-than-expected external demand supported growth in 2017, but this stimulus is expected to fade over the forecast period, as the trade environment worsens.

Table 2.3 Real GDP growth (%) - Advanced Asia

	2017	2018 f	2019 f
Japan	1.7	1.5	0.9
Hong Kong	3.8	3.0	2.5
Singapore	3.6	3.1	2.4
South Korea	3.1	2.8	2.6
Taiwan	2.8	2.6	2.5

Sources: Macrobond, Oxford Economics

In Japan, fiscal stimulus combined with the stronger external demand brought GDP growth up to 1.7% in 2017 from 1.0% in 2016. Export growth is expected to ease though in 2018 and 2019 as Chinese import demand moderates. US protectionism is also a downside risk for Japan's export outlook, but the overall impact for Japan should be limited as the country pursues more trade, especially with Asia (see Japan's leadership in CPTPP discussed on page 22). GDP growth is forecast to ease slightly to 1.6% in 2018 and further to 0.9% in 2019.

As Chinese demand weakens, growth will depend more on domestic drivers. Investment and consumption have been strong but momentum here is also beginning to wane. Japan's PMI slipped to 51.3, a 17-month low, in March reflecting a loss of steam in its economic recovery. Despite labour shortages, wage growth is expected to stay stubbornly low at 0.9% this year, continuing to put little pressure on private consumption or prices. A planned consumption tax hike in 2019 should further reduce consumption.

Like in Japan, external demand was an important contributor to solid GDP growth in the smaller, but still sizeable, developed economies in Asia last year. Exports also made a strong start this year in Taiwan and Singapore, and even accelerated in South Korea and Hong Kong, providing a sound footing for overall growth in 2018. In the course of this and next year, however, the trade environment will likely worsen, with China's growth slowdown having more impact than US trade policies.

South Korea's large trade surplus with the US leaves the economy exposed to targeted protectionist measures from the US, like recent tariffs on solar panels and washing machines. But the steel and aluminium tariffs imposed on a larger group of countries are hurting South Korea only modestly, since steel exports account for just 6% of exports. Export growth in Taiwan is expected to slow from the strong rate (7.4%) in 2017, because of falling demand from China. Still, it can stay at a strong level if the international trade climate does not deteriorate. In a worst case scenario, if the dispute between the US and China leads to a partial shift of Chinese semiconductor purchases away from Taiwan to the US as the Chinese have suggested, the repercussions for the Taiwanese economy would be more severe. Singapore also may see slowing exports growth, but is the least vulnerable for China's growth slowdown with a more diversified mix of export destinations. For Hong Kong unfavourable US trade policies towards China would have a strong impact on growth, due to its dependence on external trade and because its financial sector is vulnerable to global uncertainty. More than that, the Hong Kong economy will feel the consequences from the growth slowdown in mainland China. A downward risk for Hong Kong is the very high level of private debt, which may force households to reduce spending in a later stage.

Domestic developments are more varied. Both South Korea and Taiwan benefit from a strong labour market stimulating private consumption. In South Korea expansionary government expenditures and low inflation are helpful as well. In Taiwan bullish business sentiment suggests investments will recover from last year's dip. Both economies are expected to show a mild slowdown in growth, which should also be the case for Hong Kong and Singapore, despite fiscal stimulus in Hong Kong and a strong services sector in Singapore.

3. Emerging economies – prospects and risks

Moving further on the way to free trade

Economic growth is accelerating in emerging markets, especially in Latin America, with Brazil moving out of recession. One important risk to the strengthening outlook is still faster-than-expected US monetary tightening, which could hurt highly indebted countries. The threat of a trade war is another risk, especially if it hurts China. However, some of the larger emerging markets are rather closed, particularly those in Latin America, mitigating their vulnerability to these external developments. More importantly, rising US protectionism seems to have spurred free trade initiatives around the world. All emerging regions, except for the Middle East, have moved on with trade liberalisation. Still, an escalation of the actual trade skirmishes towards a trade war would have a negative impact.

Table 3.1 Real GDP growth (%) - emerging markets

	2017	2018 f	2019 f
Sub-Saharan Africa	2.4	3.4	3.7
Emerging Asia	6.0	5.8	5.5
Eastern Europe	3.1	3.0	2.5
Latin America	1.1	2.0	2.9
MENA	1.9	3.1	3.6
Emerging Markets	4.5	4.6	4.6

Sources: Macrobond, Oxford Economics

Worries about the trade environment are also related to China. President Xi Jinping is trying to position his country as a defender of global trade and economic openness. But criticism of China's role in the global economy is growing. Regarding free trade and capital movements, China is being accused of not offering a level playing field to other countries. Chinese companies are also being accused of theft of intellectual property, violating patents and counterfeiting brand names. Furthermore, Chinese import tariffs on a trade-weighted basis are higher than those implemented by the US and the EU[33] and China is less open for foreign investments than western countries.

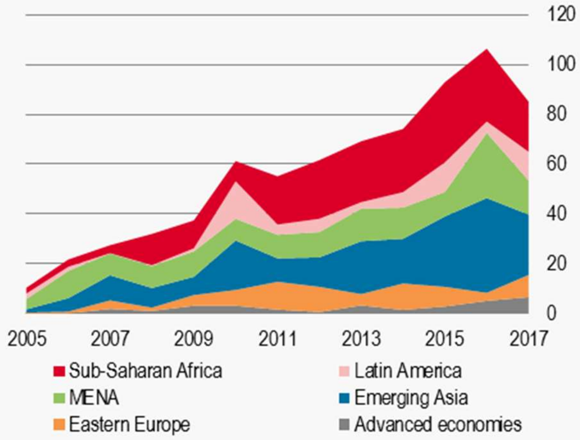
Also worrying are China's extensive investment and lending activities in Africa and Asia, as part of its Belt and Road Initiative. On the positive side, these help countries to develop the raw materials sector and improve infrastructure. But the financing of these building projects often becomes a problem, with many of these countries seeing rapidly worsening debt positions. While there is not always a direct link between the projects and external debt, half of the top-10 countries in terms of size of Chinese projects relative to GDP in the period 2005-2017 are in debt distress and another four are at high risk[34].

[33] Leering, Raoul and Timme Spakman (2018) – Unfair Trade: Does President Trump have a point

[34] Atradius (2018) – Internal note 'Vulnerability emerging economies to capital flows China, February 2018; American Enterprise Institute and Heritage Foundation - China Global Investment Tracker 2017; and IMF - List of LIC DSAs for PRGT-Eligible Countries, March 2018.

3.1 Chinese investment abroad concentrated in EMEs

Chinese projects, USD billion, 2005-2017



Sources: Atradius, American Enterprise Institute and Heritage Foundation

Emerging Asia: modifying the impact of global trade skirmishes

Rather than being a victim of the new, more protectionist global trade environment, many Asian countries show they want to benefit from free trade by concluding new agreements or deepening existing ones, and putting reforms at the core of their economic policies. If a real trade war occurs, Asia will feel pain, especially China. But both strong domestic economic developments and further liberalisation of international trade will modify the impact of the trade skirmishes.

Table 3.2 Real GDP growth (%) - Emerging Asia

	2017	2018 f	2019 f
China	6.9	6.4	6.0
India	6.3	7.3	7.0
Indonesia	5.1	5.2	5.2
Emerging Asia	6.0	5.8	5.5

Sources: Macrobond, Oxford Economics

Free trade initiatives by India and ASEAN countries

With a relatively closed economy, India is not very vulnerable to trade restrictions in general. Whereas India probably will not be exempt from the American tariffs on aluminium and steel, these are unlikely to dent the Indian metals sector. Just 4% of Indian steel exports and 2% of aluminium exports are headed to the US. Only if tariffs would be imposed on other products than metals, will the impact be felt. More import for Indian foreign trade than the US tariffs are the steps the government is taking. India is trying to formalise a free trade agreement with the EU. Talks for an India-EU FTA were put on hold in 2013, but after the India-EU Summit in Delhi last year, negotiations have resumed. In another step forward, Prime Minister Narendra Modi early this year announced his government will ease restrictions on foreign direct investments (FDI) in various sectors, which is another effort – after the GST unification and the demonetisation scheme – to improve the ease of doing business in his country. Increased economic liberalisation is contributing to India's long-term real GDP growth, which is expected to average 6.5% over the next decade. India will continue to be one of the fastest growing emerging market economies.

The ASEAN countries are also willing to improve their business environment and reduce trade and investment barriers within and outside of the bloc in coming years. The ASEAN Economic Community (AEC), which the ten member-states[35] established three years ago to give a boost to regional economic integration, helps to roll back non-tariff barriers and harmonise regulatory procedures. The wider, but less far-reaching Regional Comprehensive Economic Partnership (RCEP, consisting of ASEAN and the six countries with which the association has concluded free-trade agreements[36]) will help streamline existing free-trade agreements.

Another example of Asia's choice not to join the protectionist wave is the Trans-Pacific Partnership (TPP), which died before its birth because US president Trump decided not to join. However, it was resurrected as the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), with all other original TPP signatories[37]. China, which is not participating, has always viewed TPP with suspicion, considering it an attempt to contain growing Chinese influence in the region. Another objection of China to the TPP was the Western concepts of commercial fairness in the treaty, like the inclusion of protections on intellectual property. It is therefore that China has been promoting the RCEP and hoped it would be an alternative for several Asian countries when the TPP seemed to be stranded.

Growing opposition to China's dominance in the region

The CPTPP can be seen as a reaction of Asian and other countries to the change in US trade policy. It is also a sign that there is growing opposition to China's wish to dominate Asia with its trade and investment activities.

[35] The ten member states of the ASEAN are Indonesia, Thailand, Philippines, Malaysia, Singapore, Vietnam, Myanmar, Cambodia, Laos and Brunei.

[36] The six countries in the RCEP next to ASEAN are China, Japan, India, South Korea, Australia and New Zealand.

[37] The eleven countries participating in the CPTPP are Japan, Canada, Australia, Mexico, Malaysia, Singapore, Chile, Vietnam, Peru, New Zealand and Brunei.

Japan played a strong role in ensuring that CPTPP came through, because it wanted to secure the high standards of the agreement in areas such as tariff reductions, state-owned enterprises, labour protection, e-commerce, human rights and the environment. But CPTPP also may strengthen Japan's position in negotiations about RCEP, to make it a high-quality trade agreement, whereas China is in favour of lower standards.

Besides Japan, also smaller countries in the region have problems with China's role in the region, especially the ones taking part in China's Belt and Road Initiative (BRI). The initiative involves China underwriting billions of dollars of infrastructure investment in countries along the old Silk Road linking it with Europe. The ports, roads and railways built by the Chinese however do not always bring the benefits the receiving countries hope for.

For example, China will gain substantially from a railway linking it to mainland Southeast Asia through Laos, delivering access to major trading partners and fast-growing tourism markets. But for Laos, with few exports save hydroelectricity, the benefits are less clear and the financial burden is large, whereas both public and external finances are weak. Because China is the main creditor of Laotian debt, Laos' dependence on China is large and growing. In reaction to this, the current leadership in Laos is trying to diversify the country's relationships beyond China, especially to the ASEAN countries.

China is also an important trading partner and a welcome source of investments for Pakistan, Sri Lanka, the Philippines, Indonesia, Myanmar and Cambodia. But an increasing number of countries are seeking alternative alliances amid unease over China's rising influence and unpredictable US foreign policy as well. The US and China have long been the dominant powers in Southeast Asia, but the region is increasingly turning to India and Australia for both political and economic cooperation. They are also trying to deepen the ties with each other, for example in the ASEAN, or by joining the CPTPP, like Taiwan, South Korea, Thailand, Indonesia and the Philippines have done.

China resumes path of gradual growth slowdown

The threat of a trade war is not visible in China's economy yet. Exports in the first quarter were strong, with volume growth of 8.8% year-on-year, after 6% in the fourth quarter of 2017. Given our healthy outlook for global growth, the prospects are positive as well. Domestic demand is likely to cool on tighter financial policy. Regulatory tightening and further rate hikes in the US should maintain the upward pressure on Chinese interbank interest rates. Together with the impact of the gradual transition from export- and investment-led growth towards consumption-driven growth, this is expected to slow growth in investment to 5.1% this year and 4.7% in 2019. A negative impact on economic growth also will come from less buoyant fiscal spending. Infrastructure spending will probably stay high, but will slow on the tightening up of local government financing. Assuming the US trade restrictions will not lead to a full-fledged trade war, we expect GDP growth will slow to 6.4% this year and 6.0% in 2019, from last year's 6.9%.

Apart from the trade-war risk, chances of a hard landing scenario, in which a more severe growth slowdown is accompanied by a dramatic unemployment increase and social instability, have diminished. The People's Bank of China (PBOC) tries to reduce the risks from excessive debt and speculative investments by targeted tightening measures and financial sector regulators have been toughening rules. Tighter monetary policy will be accompanied by the recapitalisation of low- and mid-tier banks and corporate debt-restructuring programs. The stock of domestic credit, however, will remain at very high levels in the coming years. Especially rapidly rising household debt is worrying now, though not yet at very high levels. For the financial sector, it helps that the Chinese government will continue with its financial liberalisation efforts over the coming years, allowing market forces to play a greater role in the economy.

The current account surplus is falling to 1.2% GDP this year, but may stay at that level in the coming years. The authorities will probably maintain the capital restrictions imposed last year because of the threat of potential large capital outflows. The tighter controls have helped to stabilise the exchange rate, but further monetary tightening in the US will probably put downward pressure on the Chinese currency. Reserves are large enough to limit a depreciation and/or smooth volatility.

Macro policies support India's economy

Strong domestic demand and supportive macro policy are the main contributors to the acceleration of growth in India's economy. Private consumption has picked up in the first part of 2018 – partly due to a recovery from the temporary impact of the demonetisation scheme and the GST introduction last year – and may result in a 7.8% increase year-on-year for 2018 as a whole. Public spending ahead of the parliamentary and state elections and rising infrastructure spending are pushing government consumption up by a strong 9%. Net exports are expected to be a drag on GDP growth again this year. The current account deficit probably will remain within 2-3% of GDP, but a further increase in oil prices could raise the deficit to a more worrying level, and can bring downward pressure on the currency. Also monetary tightening in the US and a still-elevated government budget deficit are negatives for the exchange rate, but high levels of foreign-exchange reserves may prevent the rupee from depreciating rapidly. A positive impact on capital inflows, and therefore on the exchange rate, should come from the supportive economic policies mentioned earlier. Prime Minister Modi, who is in a strong position, is still going ahead, though gradually, with economic reforms. The biggest hurdles to make the Indian economy more efficient are in the banking sector, where problems concerning fraud and non-performing loans have to be addressed by the authorities.

Export growth losing momentum in Southeast Asia

Like China and India, countries in Southeast Asia still show strong external trade figures. Momentum, however, is slowing, with a significant decline in the rate of growth in exports in several countries because of cooling demand from China. The countries with the highest export growth rates in 2017, the Philippines and Vietnam, are expected to show the biggest reductions in growth rates, but exports still may increase about 9% year-on-year in both 2018 and 2019. In Indonesia, Thailand and Malaysia the decline in the pace of growth is not expected to be as dramatic, with export growth forecasts of 4-5% this year, and a bit slower in 2019.

On the domestic side, the picture is divergent. In Indonesia, both government expenditures and private consumption are strengthening, so that GDP growth will reach 5.3% annually this and next year, after last year's 5.1%. Given the solid fundamentals of the economy, we expect capital inflows to continue, supporting the currency. But with foreign investors holding nearly 40% of Indonesian government debt, the rupiah could weaken should US monetary policy be tightened more than expected.

In Malaysia and Thailand upcoming elections have an opposite impact. Whereas fiscal spending is the main driver of economic growth ahead of the upcoming general elections in Malaysia, the continued delay to elections in Thailand prevents economic momentum from building. Still, with the ruling government in Malaysia expected to stay in power, fiscal consolidation in the second half of the year, together with slowing external demand, will likely slow GDP growth to 5.2% this year and 4.6% in 2019, from a strong 5.9% last year. Thailand is also expected to see some lower GDP growth this year, but supportive monetary policy, rising tourism and increasing infrastructure spending by the government keep the growth slowdown contained. After growing 3.9% last year, GDP may grow 3.2% and 3.0% in 2018 and 2019 respectively.

The Philippines and Vietnam are showing the highest growth rates among the five largest Southeast Asian economies. Besides the above-mentioned relatively high export growth rates, the Vietnamese economy is helped by strong FDI inflows and expansionary monetary conditions. Rapid credit growth, leading to increasing non-performing loans in the banking sector, however, is a downside risk for the economy. In the Philippines, growth is being supported by strong government expenditures for infrastructure. In both countries GDP growth is expected to stay above 6% this and next year.

Latin America: recovery firming, but politics remain challenging

A gradual economic recovery is underway in Latin America, underpinned by strengthening domestic demand and a supportive external environment. However, upcoming elections in Brazil and Mexico and policy miscommunication in Argentina have raised uncertainty about policy direction and are weighing on the outlook. That said, the region is generally well-positioned to deal with external shocks coming from global trade disruption and a faster increase in US interest rates than currently expected by the market. Various trade initiatives (see Box 3) will somewhat cushion the impact from US protectionism and a potential trade war between the US and China. The region is an important supplier of aluminium and steel to the US, accounting for 10% and 20% respectively of US imports. Argentina, Brazil and Mexico account for most of this. So far, these countries have been exempted from the tariffs. But even if these exemptions would be lifted, the impact on their exports would be limited, ranging from 0.9% (Mexico) to 1.4% (Argentina) of total exports. Moreover, macroeconomic fundamentals in most countries are sound, with low inflation, modest external imbalances and strengthening economic growth. Strong policy frameworks, flexible exchange rates, and sufficient buffers underpin shock resilience. Argentina remains the most vulnerable.

Table 3.3 Real GDP growth (%) - Latin America

	2017	2018 f	2019 f
Argentina	2.8	2.8	3.3
Brazil	1.0	2.4	3.2
Chile	1.6	3.8	3.0
Colombia	1.8	2.4	3.3
Mexico	2.3	2.2	2.4
Peru	2.5	3.5	3.8
Venezuela	-9.2	-6.8	-0.7
Latin America	1.1	2.0	2.9

Sources: Macrobond, Oxford Economics

Box 3 Update of trade initiatives in Latin America

Growing protectionism is definitely not the norm on the American continent. Latin American countries have taken various initiatives to strengthen regional integration and move forward with Free Trade Agreements (FTA). Three of the four Pacific Alliance countries, **Chile**, **Mexico** and **Peru**, were among the signatories of the **Comprehensive and Progressive Agreement for Trans-Pacific Partnership** (CPTPP) in Chile last March. This is an alternative to the Trans-Pacific Partnership from which the US withdrew last year. Meanwhile, negotiations between **Mexico and the EU** on an extension and modernisation of the FTA in place since 2000 have been concluded in April. Additionally, **Chile and the EU** started negotiations to modernise the trade part of their association agreement in November 2017. Negotiations between the **EU and the Mercosur trade bloc** (Argentina, Brazil, Paraguay and Uruguay) on a FTA are nearing completion. These talks have been on-and-off since 1999, but were accelerated in 2017 under the leadership of Argentine president Macri. The intention of both sides is to reach a deal before summer 2018. Additionally, the **Mercosur** countries began to consider initiating talks on a separate FTA with **Canada** last March. Talks on a potential 'convergence' between **Mercosur** and the much more open countries of the **Pacific Alliance** (Chile, Colombia, Mexico and Peru) are ongoing, but a deal is some way off. Finally, trade is also being liberalised in **Central America**. In June 2017 a **landmark customs union** between Guatemala and Honduras entered into force, making it the first joint customs territory in the Americas. Talks about inclusion of El Salvador started in July 2017. And last February, five Central American countries – Costa Rica, El Salvador, Honduras, Nicaragua and Panama – signed an **FTA with South Korea**.

Argentina: Increasingly challenging policy environment

After winning a decisive victory in mid-term elections last October, the government of President Macri has continued reforms. In November, the fiscal framework was further improved, and in December, some pension and tax reforms were enacted. However, popular resistance to reforms is growing, weighing negatively on consumer sentiment and slowing the reform process.

Argentina's economy grew 2.9% in 2017, up from a contraction of 2.2% in 2016, driven by improved investment and private consumption. Growth became more broad-based as the manufacturing sector steadily recovered. However, the economic outlook has worsened compared to the previous Economic Outlook. Growth is now expected to more or less stabilise at last year's level, due to the worst drought in 30 years, stubbornly high inflation and miscommunicated monetary policies. Last December, authorities raised the – too ambitious – inflation target for 2018 (to 15% from 10%) and 2019 (to 10% from 5%) and subsequently cut interest rates. This has rattled financial markets, which assessed the cut in interest rates to be too soon, resulting in peso depreciation and rising inflation expectations. The peso has weakened by some 15% since mid-December and is one of the weakest currencies this year. The interest rate cut has thus backfired as peso weakness will hamper the disinflation process and will weigh negatively on economic growth going forward. Meanwhile, the central bank's ability to control inflation is hampered by ongoing, albeit declining, financing of the fiscal budget.

On the fiscal side, President Macri succeeded in reducing expenditures on subsidies and social security. But the fiscal deficit remained mostly unchanged at 6% of GDP due to higher interest payments. Fiscal consolidation is needed to achieve a more balanced policy mix, which would help to lift confidence, unleash FDI, and reduce inflation and the current account deficit. The latter widened to 5.1% of GDP in 2017 from 2.7% in 2016 and its highest level in 20 years. This was due to a shift in the trade balance from a surplus to a deficit on the back of trade liberalisation and rising domestic demand. Most of the deficit is financed by portfolio inflows, leaving the country exposed to normalisation of US interest rates and shifts in investor sentiment. Although official reserves have risen, they are insufficient to cover the high gross external financing need. On a positive note, access to capital markets remains good, but this might change when interest rates in the US rise further or when the government does not succeed in improving its policy mix.

Brazil: Rising political uncertainty, accelerating recovery

Brazil's political scene is dominated by presidential elections in October. The field is much more open than usual, as the Lavo Jato corruption scandal has damaged the reputation of established political parties and their representatives. Campaigning officially starts in August, but politicking is already under way. This will make it highly unlikely that president Temer will make further progress with his structural reform agenda. Earlier this year, Temer had to call off the crucial pension reform vote as it became increasingly evident that the unpopular measures would lack sufficient votes so close to the elections.

Meanwhile, despite the uncertain political environment the economic recovery is gaining momentum and business and consumer confidence remain buoyant. Brazil's economy grew by 1.0% in 2017 from -3.5% in 2016. This was its first expansion in three years. It is boosted by a jump in exports and household spending. Household incomes are profiting from rising employment and real wages, and interest rate cuts to a record low of 6.5%. The latter was possible as inflation, at 2.7%, remains at historically low levels and below the target band of 3% to 6%. Even private investments are growing since Q4 of 2017 for the first time in almost four years. High frequency indicators show that the strengthening of the economic expansion continued this year amid still favourable conditions. The PMI rose to 52.6 on average in Q1 of 2018, the strongest quarterly gain in seven years. This underpins our expectation that economic growth will strengthen further over the outlook period.

However, uncertainty over policy direction after the elections could pose headwinds for investments and growth going forward. It could also result in more currency volatility. So far, investors have responded remarkably sanguinely to the delay in pension reforms and rising political uncertainty, unlike the rating agencies, that further downgraded their sovereign ratings for Brazil. Equities, bonds, and credit default swaps have been largely unaffected, reflecting the expectation that elections will be won by a centre, reform supportive candidate, who will carry on Temer's reform agenda. But this sentiment might be turning: the currency depreciated following the imprisonment of former President Lula da Silva, making it highly unlikely that he will be able to run for the presidency. Previously markets rallied on developments that undermined his candidacy, given his anti-reform stance, but with other anti-reform candidates leading the polls, uncertainty is growing. The currency has depreciated by 3.4% YTD vis-à-vis the US dollar .

Pension reforms remain the most urgent. Without measures to contain the growth in pension expenditure, which already constitutes a third of total government spending, it will be difficult to comply with the 'spending cap rule' in the medium term, and to put the debt-to-GDP ratio on a sustainable trajectory. Thanks to this rule and a faster than expected economic recovery, the primary deficit was at 1.7% of GDP below the targeted 2.3% of GDP. This, and current low interest rates, have helped to bring the fiscal deficit down from 9% of GDP in 2016 to 7.3% of GDP last February. But deficits remain high pushing the government-debt-to-GDP ratio further up from 70% in 2016 to 75% of GDP last February. Positively, nearly all of this debt is financed in local currency, on the domestic market, and the sovereign remains a strong net-external creditor. This mitigates sovereign risks. Also, the shock absorbing capacity of the Brazilian economy remains strong, underpinned by a flexible exchange rate, a sound banking sector, and very high official reserves.

Mexico: Economy resilient, politics cloud outlook

Mexico's political scene is also dominated by general elections, which are scheduled for July 1st. The anti-establishment, leftist candidate, Andrés Manuel López Obrador is leading the polls. He is running for president for the third time and chances are growing that this time he will win, as he will benefit from a highly fragmented political environment and growing discontent with traditional political parties. Moreover, there is no second round, implying that a candidate can win with relatively limited public support. Obrador's past rhetoric has raised concerns over the durability of orthodox macroeconomic policies and the future of the structural reforms initiated by current president Peña Nieto. However, a radical policy shift is highly unlikely given a solid institutional framework, including congressional budget limits, and the need for constitutional changes to undo past reforms. That said, a potential Obrador administration would slow the pace of reforms, which will negatively weigh on economic growth going forward.

Already, uncertainty surrounding the upcoming elections and NAFTA renegotiations (see Box 4), together with policy tightening have weakened investment. Real GDP growth slowed as a result to 2% in 2017, from 2.9% in 2016. Private consumption and exports were the main drivers. Going forward, economic growth is expected to more or less stabilise over the forecast period, as rising exports will most likely be offset by falling domestic demand. Authorities continued to tighten policies to adjust government finances to an environment of lower oil prices and to curb inflationary pressures. These policies are paying off: a primary surplus was achieved for the first time since 2008, helping to reduce the budget deficit to 1.1% of GDP in 2017 (from 2.8% in 2016) and the debt-to-GDP ratio to 46 (from almost 49 in 2016). This was the first decline since 2007. Also, inflation has eased to 5% last March from a peak of 6.8% end-2017. Moreover, these policies helped to stabilise financial markets and to maintain investor confidence. The peso is on an appreciating trend since end-2017 and one of the strongest currencies so far this year (see figure 2.3). Peso strength also reflects the signing of the CPTPP, which will help to diversify Mexico's trade away from the US, the US

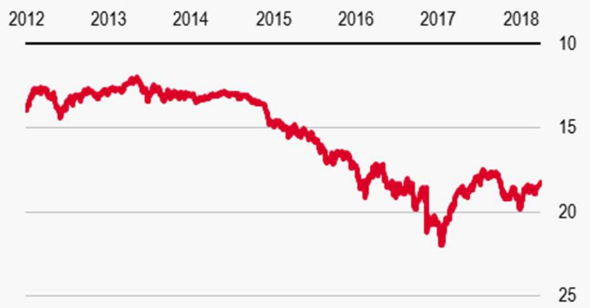
Box 4 Renegotiation of NAFTA: agreement in sight

After seven rounds of negotiations, talks on renegotiation of NAFTA accelerated in April. The urgency of a deal has increased due to the ending of the reprieve given to Canada and Mexico on steel and aluminium tariffs, and upcoming elections in Canada (June; local), Mexico (July; general) and the US (November; midterm). A softening of the US stance on some issues also helped to speed up the process. This reflected increased pressure from the US business community to reach a deal and the tax reform approval in the US, which reduced the urgency for the Trump administration to deliver on other campaign promises. However, wide differences remain on the most contentious issues: higher rules-of-origin requirements for the car industry, revisions to the dispute settlement clauses in the agreement and a possible sunset clause that would require the partners to recommit to NAFTA every five years. Still, chances have increased that some kind of agreement will be reached in May. Failure to do so increases the risks of a more protracted negotiation process, as a possible change in the political landscape in Canada and particularly Mexico could further complicate negotiations. Also, the he later a deal is agreed, the less time members of the current US Congress has to ratify it.

government's announcement that it would exempt Mexico from possible tariffs on steel and aluminium, and indications that the US wants a deal in principle on NAFTA before the elections. Going forward, rising volatility associated with the elections and increasing US interest rates is to be expected. But Mexico remains in a good position to deal with shocks given moderate external imbalances, robust policymaking, a flexible exchange rate and sizable reserves which are underpinned by an IMF Flexible Credit Line (FCL).

3.2 Mexican peso keeping strong

Peso per USD, reverse axis



Source: Macrobond

Other Pacific Alliance; leadership change, economy gaining speed

The remaining Pacific Alliance countries are also undergoing leadership changes. In Chile, Sebastián Piñera of the centre-right Chile Vamos coalition took office in March. In Peru, political stability has returned following the resignation of President Pedro Pablo Kuczynski the same month after mounting allegations of corruption and the threat of impeachment. Here Vice President Martín Vizcarra took over the presidency and appointed an entirely new cabinet. Legislative elections in Colombia marked a shift to the right. Presidential elections are scheduled for the end of May, with a runoff likely in June. Continuity of sound macroeconomic policies in all three countries is assured, despite the change in leadership.

Economic growth in all three countries is rebounding on the back of a supportive external environment and strengthening domestic demand. The latter will be positively impacted by improved confidence in Chile under the new leadership and the lagged effect of interest rate cuts in Colombia and Peru. In the latter country, a recent law was passed that reduces financial risks for new investors in the country's infrastructure and construction projects, which will also facilitate growth going forward. Additionally both Peru and Chile will profit from the CPTPP deal. All three countries remain well-placed to deal with the normalisation of US monetary policy, due to sound policy frameworks, flexible exchange rates and healthy buffers, which for Colombia are underpinned by a flexible credit line from the IMF.

Central & Eastern Europe: losing momentum

Central & Eastern Europe (CEE) is forecast to grow a steady 3.0%, almost in line with the 3.1% recorded in 2017 before losing some momentum in 2019. The regional headline figure though hides some large regional discrepancies. Russia, the region's largest economy, only slowly crawled out of its recession in 2017 and its growth is expected to remain subdued in the forecast period, constrained by sanctions. The export-oriented economies of Central Europe, on the other hand, saw a spike in growth in 2017 as external demand strengthened but as the eurozone upswing cools off, momentum in those countries is expected to ease. Turkey was the biggest surprise to the upside, in 2017 growing 7.3% due to government stimulus, but this is expected to quickly fade.

Table 3.4 Real GDP growth (%) - Eastern Europe

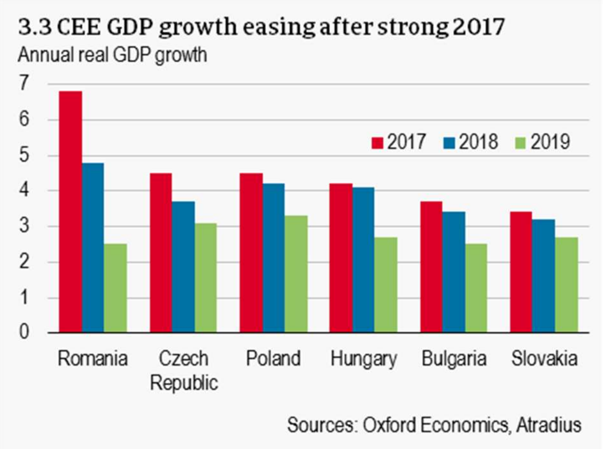
	2017	2018 f	2019 f
Bulgaria	3.7	3.4	2.6
Czech Republic	4.5	3.7	3.1
Hungary	4.2	4.1	2.7
Poland	4.5	4.2	3.5
Romania	6.8	4.9	2.5
Russia	1.6	1.8	1.4
Turkey	7.3	4.4	3.1
Ukraine	2.3	3.2	3.0
CIS	2.1	2.3	2.0
Eastern Europe	3.1	3.0	2.5

Sources: Macrobond, Oxford Economics

Central Europe: losing pace as trade boost gives way to domestic weaknesses

GDP growth in Central Europe is slowing down but remains strong. These markets are generally characterised by high trade openness, as measured by exports as a percent of GDP, and are closely ingrained in European supply chains. As such, they benefitted strongly last year from the pickup in demand in the eurozone. Growth in 2017 was also underpinned by tightening labour markets, easy monetary conditions and expansionary fiscal policy. But this momentum is not expected to last in 2018 and 2019 as some eurozone demand cools, underlying structural issues weighing on growth, and political risks increasing.

Overall, the growth outlook for Eastern European member-states is still strong, driven by domestic demand as the stimulus from trade fades. But the region is increasingly grappling with labour shortages and low productivity that threaten the medium term outlook. Unemployment rates are at a decade low or even all-time lows in some countries and below the EU average in all but Slovakia. Wage growth is picking up, due to increased worker bargaining power and public policy, and inflation remains low, supporting a strong expansion in household consumption. But labour shortages are increasingly a problem due to underlying demographic trends (emigration and low birth rates) with many firms finding it difficult to fill vacancies, especially in Hungary and the Czech Republic. These trends exacerbate the ongoing problems with productivity gains which are being outpaced by wage growth. The comparative advantage with Western Europe will persist through the outlook period, but the current boon for private consumption will ease, losing some momentum for growth in 2019 and beyond.



Politics in the region is increasingly a risk for the economic outlook. Momentum will further ease as the stimulus from pro-cyclical fiscal policies fades out. Corruption remains an issue in the region, especially for Hungary, Romania, and Bulgaria. Right-leaning parties with broad public support in Hungary and Poland, have made changes to their judiciary systems among other controversial policies, increasing the chances for EU retaliation. The announced EU budget for 2021-2027 is expanding the criteria for cohesion policy funds beyond simply GDP per capita, which favoured Portugal and the newer member states of CEE, to more values-based criteria including the environment for migration and innovation. This is expected to greatly reduce the funding available to the region, especially Poland, Hungary and Czech Republic. On top of this, without the UK's budget contribution, total funds available will also simply be less. Lower EU inflows would not choke off growth in the region but could severely impact some sectors, especially construction which depends on EU financing.

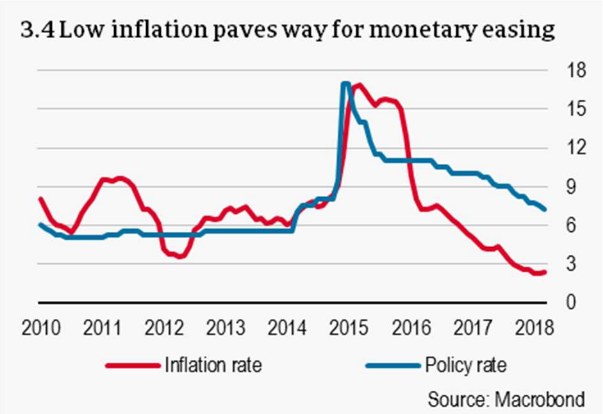
Russia: rising tensions with the West

Vladimir Putin has won a fourth term as president of Russia, receiving 77% of the vote. With the current leadership remaining in place, the economy is also expected to remain broadly on the same path over the coming years. GDP is forecast to expand by 1.8% in 2018, underpinned by a low inflation rate and a reasonably stable exchange rate. A number of events could threaten the growth forecast, including geopolitical tensions, a further tightening of international sanctions and renewed oil price volatility.

The Russian economy continues to struggle with US and EU sanctions. Tensions have increased following the alleged attack by Russia on a former Russian spy living in the UK. The crisis has led to the expulsion of Russian diplomats from more than 20 counties. New US sanctions against Russia were announced on April 6 to punish Moscow for its alleged meddling in 2016 US elections. Recent developments in the Syrian conflict have heightened the risk of a further escalation of tensions between Russia and the West.

GDP grew 1.6% in 2017 compared to a contraction of 0.2% in 2016. Stronger growth, higher oil prices and a relatively tight monetary policy have contributed to rouble appreciation in 2017. In 2018, the rouble is expected to appreciate another 4%. While this may create some headwinds for export growth, exports are still expected to grow 4.5%. As the rouble is correlated with oil prices, any rapid fall in oil prices could lead to renewed volatility.

Private consumption is expected to grow by 3.0% in 2018, down from 4.4% last year. Consumption growth is likely to remain robust, driven by an upward trend in consumer confidence and a low inflation rate boosting real disposable income. Russia has seen steady decline in consumer price inflation since late 2015, with inflation hitting a record low of 2.2% in February 2018, well below the central bank's 4% inflation target (figure 3.5). The low inflation rate allowed the central bank to cut its main policy rate by 25 basis points in February to 7.5%, following a 50 basis point cut in December 2017. The central bank is expected to continue cutting its policy rate in 2018 as inflation remains below target and growth disappoints.



The Russian banking sector is undergoing nascent recovery, with credit growth expected to pick up this year due to stronger economic activity and easing monetary conditions. The central bank's interventions to bail out Otkritie and B&N bank have prevented a systemic crisis. However, the launch of new US sanctions against Russian oligarchs and their companies threatens to derail the recovery, through uncertainty and lower investment. In 2018, fixed investment is expected to grow by 1.8%, down from 4.4% last year. The high level of perceived risk, corruption and a weak institutional backdrop are likely to keep investment growth subdued.

The government is still faced with a tight budget constraint as a result of low commodity prices. After narrowing sharply in 2017 on the back of higher oil prices, the fiscal deficit is expected to widen again in 2018 to 2.2% of GDP. The adjustment to government expenditure is likely to be less radical than planned given promises Putin has made to increase social spending.

The government has adopted a fiscal rule based on a conservative oil price baseline of USD 40. It will continue to use above-budgeted oil revenues to intervene in the currency market to stem the rise of the rouble and to build foreign exchange reserves. This build-up of foreign reserves is allowing Russia to avoid reliance on borrowing and to pursue a more independent economic policy.

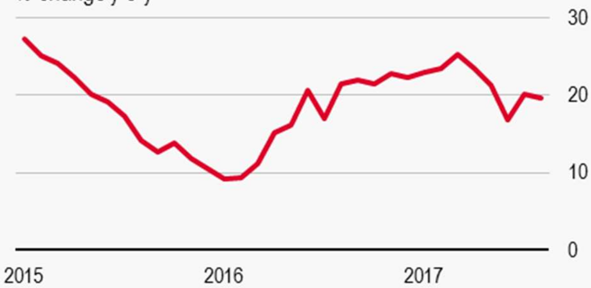
Turkey's stop-go policy

With President Erdogan in the driver's seat, Turkey's economic growth skyrocketed to 7.4% in 2017. All stops were pulled out to prop-up growth after the failed coup attempt in 2016. Measures included various tax and employment incentives and a credit support scheme. But now signs of overheating have become apparent and economic imbalances are growing. The output gap turned positive, inflation is stubbornly high, and the already sizeable current account deficit is widening. Although industrial production was still close to its record high in February, which suggests a continuation of momentum in the first quarter of 2018, a moderation of real GDP growth to 4.2% is expected for 2018 and 3.1% for 2019, as various government stimulus measures have expired and a series of tax hikes is planned for 2018-2020.

Some cooling of the credit-driven economy is welcome, but there is a risk that this stop-go policy leads to a more severe slowdown, because it will expose Turkey's weak economic fundamentals. The increase in the corporate tax rate from 20% to 22% could for example contribute to a further deterioration in the business environment that is already full of political uncertainties. It may even stop the nascent recovery of business investment in productivity-enhancing capital goods in its tracks. While until recently credit has been mainly fuelling a construction boom, the fading of the credit impulse is already reflected in a slowdown of the real estate market. Telling in this regard is the deceleration of loan growth (see figure). Not only is there less support from the government's credit guarantee fund, banks may also become more cautious to extend loans as corporate sector indebtedness has increased to 68% of GDP. Freshly announced stimulus measures including extension of employment incentives and a USD 34 billion corporate investment incentive scheme could ameliorate these concerns, but the fact remains that a patchwork of temporary policy measures instead of structural reforms will not optimally contribute to a sustainable economic recovery. This new round of fiscal stimulus measures is probably intended to bolster popular sentiment in the run-up to the presidential and parliamentary elections which have been moved forward by 1.5 years to June 2018. Snap elections are called to limit uncertainty and speed up the controversial transformation of the political system that gives unparalleled power to the president.

3.5 Non-financial sector credit growth in Turkey is decelerating

% change y-o-y



Source: TCMB

Monetary policy is sending similarly ambiguous signals. Hesitant monetary policy actions make investors nervous and increase the risk of a hard landing and/or a sudden stop of capital inflows. Inflation has receded somewhat from their highs in 2017 due to favourable base effects, but at 10.2% in March remains far off from the central bank target of 5%. The stickiness of inflation is also illustrated by even higher core inflation and elevated (longer-term) inflation expectations. The central bank seems to be falling behind the curve. In its first two meetings this year it kept interest rates unchanged. Increased political pressure from President Erdogan, who holds the unorthodox view that high inflation is caused by high interest rates, may have been partly to blame. At the end of April, the central bank finally raised the rate on its Late Liquidity Window by 75 basis points, to stave off growing depreciation pressure. Turkey is vulnerable to exchange rate shocks given its large foreign exchange (FX) share of corporate debt. The lira-dollar exchange rate is volatile and has reached an historically weak level in early 2018. Lira depreciation adds to the corporate debt service burden leaving less room for capital expenditure. This exchange rate risk has been recognised by the central bank that enhanced measures to curb FX lending. The Turkish economy is very vulnerable to capital outflows, because a large part of the current account deficit is financed by short-term financing. Portfolio inflows have recently softened, while FDI remains notoriously low. Despite strong export growth, domestic overheating has aggravated the current account deficit via increased import demand. Rising oil prices are also a threat in this regard. International reserves have gradually declined over the past years and are not sufficient to cover external gross financing needs.

The weakness of the lira is also caused by increased geopolitical risk. Turkey's latest military operations against the Syrian Kurds further eroded international goodwill. This act could also evolve into a wider conflict with the Kurdistan Workers' Party (PKK) at home or with other international actors in the Syrian war zone. Tensions between Turkey and its Western allies such as Germany and the US have not abated and negotiations to modernise the customs union between Turkey and the EU seem to be stuck. Trump's trade tariffs also hit Turkey's steel exports to the US (albeit steel exports comprise less than 1% of total exports). If Turkey fails to qualify for tariff exemption like the EU this could further contribute to the rift. Instead, Turkey is more leaning toward the East for example by buying military equipment from Russia instead of from fellow NATO members. On collision course or not, overheating is not likely to be appropriately addressed with monetary policy falling behind the curve and stop-go fiscal policies. On the other hand, hopes are that necessary structural reforms will no longer be postponed if the president succeeds in consolidating his grip on power in the snap elections.

MENA: no regional counterforce to trade tariffs

Economic growth in the MENA region is forecast to gradually pick up from the oil-driven economic downturn to 3.1% in 2018 and 3.6% in 2019. The trough was reached at 1.9% growth in 2017 when OPEC+ imposed production cuts. Saudi Arabia and Kuwait will emerge from recession this year. Although the extension of OPEC+ restrictions until end-2018 somewhat dimmed the outlook for 2018, the expected flat oil production is clearly better than the contraction we have seen in 2017. The higher oil price is helping the recovery and various governments, including Saudi Arabia, UAE and Oman, are seizing the opportunity to ease their fiscal consolidation policies and re-focus on boosting economic growth. This will be reflected in capital expenditures to spur ahead the national economic diversification programmes and in social transfers to vulnerable households to quell lingering social unrest. Unemployment rates have remained high since the Arab uprisings due to the subsequent oil price crash and demographic challenges. Early this year small scale protests have for example erupted in Oman, but also in Iran where the benefits of the oil production catch-up after sanction relief were not directly felt by the wider population. Besides diversification programmes, the preparations of the World Expo in Dubai in 2020 and the FIFA World Cup in Qatar in 2022 continue to attract large infrastructure investments to the region and drive medium-term growth.

Table 3.5 Real GDP growth (%) - MENA

	2017	2018 f	2019 f
Egypt	4.2	4.7	4.9
Morocco	4.1	3.2	3.9
Qatar	1.3	3.1	3.4
Saudi Arabia	-0.7	2.0	2.8
Tunisia	2.0	2.1	2.3
United Arab Emirates	1.7	2.7	3.8
MENA	1.9	3.1	3.6

Sources: Macrobond, Oxford Economics

Fiscal consolidation will still continue, but at a more gradual pace and with a focus on non-oil revenue raising measures. The introduction of 5% VAT in the Gulf Cooperation Council (GCC) countries is the most eye-catching one, but the impact is less impressive than it looks. So far only Saudi Arabia and the UAE have managed to implement it as scheduled per 1st of January 2018. Bahrain may follow later this year and Qatar, Oman and Kuwait will be pressed by the final deadline of 2019. Quite some products are exempted and in Saudi Arabia cash handouts are used to cushion the impact on purchasing power of vulnerable households. The positive side of this is that private consumption growth is not likely to experience a major backlash. Nevertheless, measures to further shore up internal but also external finances remain necessary. This especially holds for countries such as Bahrain and Oman, and to a lesser extent Saudi Arabia and Algeria that have fiscal break-even oil prices that are well above the current oil price.

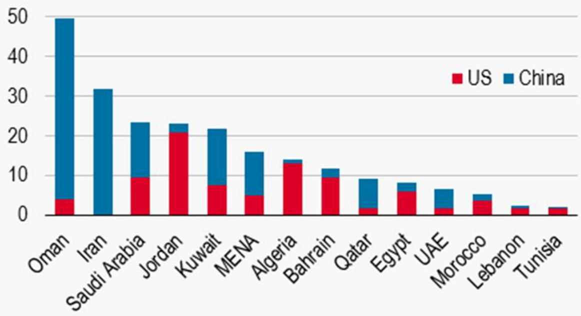
Not only the recent oil price recovery but also the availability of easy money on the international capital market to finance shortfalls seems to have reduced the sense of urgency for fiscal adjustment. Risks of deterioration in financing conditions have led MENA countries to front-load their international bond issuance, which surged further from less than USD 70 billion in 2016 to almost USD 95 billion in 2017. Aside from misguided Fed policy that would negatively affect global financing conditions, regional instability and the increased public and external debt burden could also translate into higher risk premiums for MENA countries. At the same time, domestic interest rates are rising in line with Fed hikes in the countries that have pegged their currency to the US dollar. While this helps to bolster deposits after the oil crash-related liquidity squeeze, it will also continue to constrain domestic credit growth that is still subdued.

Economic growth in oil-importing countries in the region benefits from structural reforms. Egypt, Jordan, Tunisia and Iraq are under guidance of IMF programmes. Morocco's precautionary liquidity line with the IMF on which it has not drawn has expired, but fiscal reforms are expected to continue and growth will keep up despite some weather related swings. Tunisia and Jordan are struggling to meet the fiscal targets of their IMF programmes, while Lebanon is facing political instability.

In general, the direct impact of a potential trade war between the US and China will be limited for MENA, especially for the oil-exporting countries, because hydrocarbons are not (yet) targeted by tariffs. Although UAE and Bahrain, and to a lesser extent Qatar, are large aluminium suppliers to the US, the aluminium and steel tariffs are not likely to hit their total exports too hard, regardless of whether they qualify for exemptions or not. Aluminium and steel exports to the US are less than 1% of total goods exports for UAE and Qatar and less than 5% for Bahrain. However, Bahrain is investing heavily in a major expansion of its aluminium industry. Some countries in the Middle East could be caught in the middle though, when a trade war results in a slowdown of external demand from the US and China. More than 20% of the goods exports of Oman, Iran, Saudi Arabia, Jordan and Kuwait are to those two economic powers combined. Enhanced trade integration in the GCC is not expected to be a likely counterforce. Intra-regional trade is low and disunity within the customs union is growing. There is not much progress in resolving the boycott of Qatar, while the UAE and Saudi Arabia are strengthening economic and military ties, apparently outside the GCC. Also the threat of new sanctions for Iran creates more uncertainty about the stability of the region. US President Trump is pressuring the EU to go along with his efforts to 'fix' the nuclear deal. Although the EU and the other signatories (besides the US) seem still committed to the nuclear deal, some new sanctions for example to curb Iranian ballistic missile development may receive some support.

3.6 Exports to US and China are substantial for some MENA countries

Exports to US/China as % total exports



Source: UNCTAD

Sub-Saharan Africa: investments support economy, but increase vulnerabilities

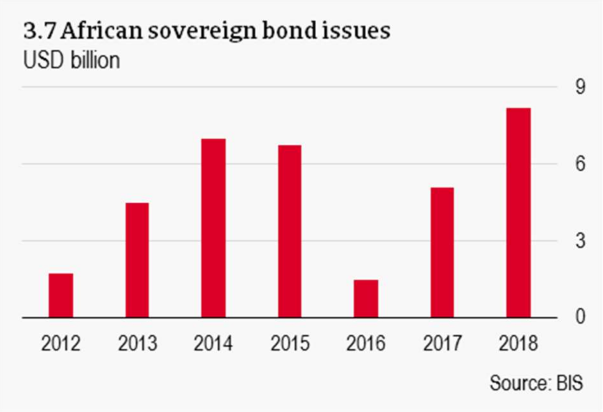
Economic growth in the Sub-Saharan African countries is expected to accelerate to 3.4% this year from 2.4% in 2017, and further to 3.7% in 2019. Across the region there is much heterogeneity. The region's three largest economies – Angola, Nigeria, and South Africa – are all rebounding, but economic growth remains relatively low. Both Angola and Nigeria are still adjusting to the lower oil price environment and South Africa is still facing negative effects from the policy uncertainty of previous years. Excluding these larger economies, economic growth in Sub-Saharan Africa would be much higher. The non-resource rich countries show solid economic growth figures, driven for a large part by high public investments (Senegal, Cote d'Ivoire, Ethiopia and Kenya). All commodity-exporting countries are benefitting from the increasing commodity prices, but there are some differences between them. In general oil-exporting countries (Gabon, Angola, and Nigeria) are adjusting slowly to the low oil prices after being hit hard by the oil-price collapse. This is in contrast to metal-exporting countries like Zambia (copper) which did not enter a recession and have rebounded more quickly.

Table 3.6 Real GDP growth (%) - Sub-Saharan Africa

	2017	2018 f	2019 f
Ghana	8.3	7.2	6.1
Kenya	4.6	5.7	6.3
Nigeria	0.8	2.6	3.2
South Africa	1.3	2.0	2.0
Sub-Saharan Africa	2.4	3.4	3.7

Sources: Macrobond, Oxford Economics

Over the past years, many African countries have increased their investments in infrastructure. These investments have been financed by borrowing, leading to a rapid increase in their debt levels. According to the IMF the median of Sub-Saharan African total public debt was 48% of GDP in 2016, compared to 29% in 2012. Some countries have already run into problems (Mozambique, Congo Brazzaville and Chad) and others are challenged not too. Especially vulnerable are those countries that have benefitted from the favourable global financing conditions and turned to the international capital market. With interest rate increases on the horizon, African countries are increasingly motivated to seize the opportunity and issue bonds against favourable rates. In only the first four months of this year, a record amount of African sovereign bond issues, excluding South Africa, took place. A faster tightening of the US monetary policy will definitely have an impact on the African region. Increasing interest rates will increase the debt service costs, which for some are already quite high.



A new free trade deal

Africa's main export products are commodities, much of which are exported to China, making it vulnerable to a Chinese economic slowdown. If increasing US protectionism leads to a trade war and the Chinese economy is negatively impacted, Africa will suffer. Extra-Africa exports are mainly commodities, but intra-trade is more diversified and manufacturing based. However, currently Africa is one of the regions where intra-trading is least developed. It accounts for only 15% of all trade on the continent. To increase the economic potential of the region African countries recently signed a deal to create a free trade zone. In March this year, 44 African countries signed a framework to establish an African Continental Free Trade Area agreement (AfCFTA). Before the agreement comes in full force there are some obstacles to overcome. Ten countries, including Nigeria and South Africa, have yet to sign the agreement and for it to come into force 22 countries have to ratify it. Getting Africa's largest economy, Nigeria, on board is a huge challenge. The goal is to create a single market for goods and services and free movement of business persons and investments. According to the UN Economic Commission for Africa it could increase intra-African trade by 52% by the year 2022, remove tariffs on 90% of goods, liberalise services and tackle other barriers to intra-African trade, for example the long delays at border posts. Once AfCFTA is in force it could become the world's largest free trade area and deliver huge benefits for the African continent.

South Africa: investor confidence improved

With the removal of Zuma as president, sentiment has improved toward South Africa. This was clearly visible in the improvement of confidence indicators, both business and consumer, and an appreciating rand. Cyril Ramaphosa took over presidency in February and is expected to reverse the gradual erosion of the institutional strength of South Africa under the previous leadership. There are already some visible changes such as changes in leadership in key government institutions. There is also the clear strategy in the 2018 budget, in which fiscal adjustments have been announced to reduce the deficits and keep the debt burden sustainable. A bold step has been taken on April 1 with the implementation of the first VAT increase since 1993, to 15% from 14%.

Despite the positive changes, challenges remain for South Africa. The ANC is highly divided ideologically and parliamentary elections are on the agenda in 2019, which could slow the process of implementing structural reforms. Thereby populist measures, such as free higher education and land expropriation without compensation, are a threat to fiscal sustainability and investment sentiment. For the short term the economic recovery will continue, helped by higher commodity prices and improving external demand. GDP growth is expected to increase 2% annually in both 2018 and 2019. However, structural constraints like high unemployment and shortages of skills will keep economic growth subdued.

Nigeria: recovery helped by higher oil prices

Higher oil prices and oil production are supporting the Nigerian economy, resulting in economic growth of 2.6% in 2018 and 3.2% in 2019. Increasing activity in the agriculture sector and an expected increase in public investments in infrastructure will also provide support. Due to higher oil prices and subdued import demand there are surpluses on the current account. This in combination with an increase of capital inflows resulted in an increase of foreign exchange reserves to USD 47 billion. FX shortages have been addressed somewhat, but prioritising favoured sectors remains and multiple exchange rates are still intact. The recovery is rather fragile and economic growth remains moderate. Although inflation is declining, it remains high at 16% this year, which will keep interest rates high and constrain domestic demand.

4. Implications for the insolvency environment

Insolvency environment continues to improve

As discussed in the preceding chapters, global growth is strengthening. With improved GDP growth in 2017, 2018 is expected to show an even further improvement of 3.2%. With GDP growth the main driver of insolvency developments, our insolvency forecast shows comparable improvement, with insolvencies expected to decrease 4.1% globally. The main risks to the outlook are US protectionism, including the threat of a trade war, a China hard landing, with high debt levels forcing China to restrain credit growth, and a financial market correction due to a misguided Fed policy, with restrained spending by both firms and households.

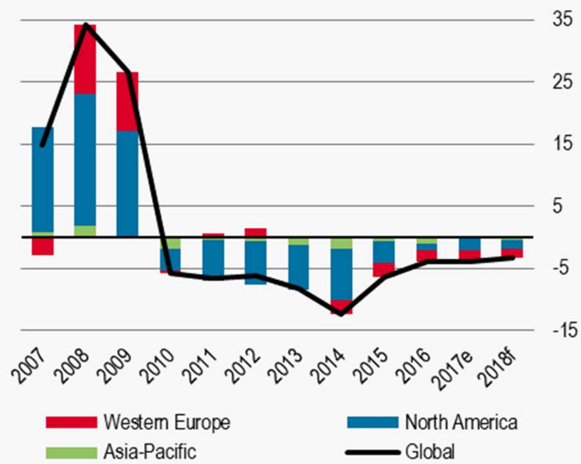
Europe – robust performance

Economic strength across advanced markets has been one of the key drivers of the broad-based global upswing since 2017. The outlook for 2018 remains strong however we expect momentum to begin to ease in 2019. The outlook is characterised by robust GDP growth, declining unemployment, and strong business and consumer confidence, key positive drivers for the insolvency rate. The outlook for almost all western European countries is positive. However protectionism is a potential threat to the current growth.

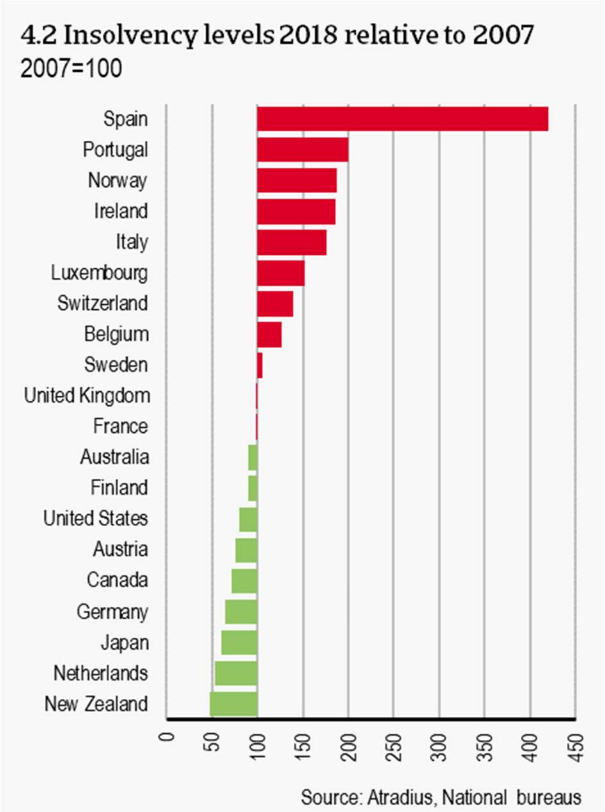
GDP growth in the **Netherlands** is expected to remain robust in 2018. Private consumption growth is benefiting from positive wealth effects, employment creation and wage growth. Investment growth is likely to wane somewhat compared to 2017, due to lower residential investment growth. We expect a slight easing in the pace of decline in insolvencies to -8% as the annual volume of insolvencies is only at 60% of its 2007 level.

4.1 Global insolvency developments

Global insolvency growth, regional contributions



Source: Atradius



Germany's outlook is characteristically strong supported by exports. GDP growth is forecast to remain robust in 2018. Domestic dynamics remain strong. Private consumption continues to expand, but at a lower rate than in 2017. Investment growth remains robust. The insolvency forecast for 2018 is a decrease of 6%.

Growth is picking up in **Finland**, driven by private consumption from pent-up demand this year, declining unemployment, still low inflation, and very low interest rates. Momentum should continue into H1 of 2018 but ease in H2 bringing annual insolvencies down only 6% following last year's 10% decline.

GDP in **France** is forecast to expand 2% this year. With industrial production expected to grow significantly and unemployment decreasing, we expect a 7 % decline in the total number of insolvencies this year, bringing the country's annual count close to pre-crisis levels.

Italy showed improved GDP growth, somewhat lower unemployment and much higher industrial production growth. This all supports the picture of a strengthening recovery, one reflected in a 10.8% decline in insolvencies in 2017. The picture is expected to carry over to 2018. This, as well as the still high number of insolvencies, warrants a decline in insolvencies in line with our model forecast of 10%. With the results of the March elections showing Populist Party majority, uncertainty over badly-needed future reforms have markedly grown. The forecasts are therefore subject to downward risk.

Spain is still recovering from the 2013 crisis, but is now entering its fifth year of growth, with unemployment falling and industrial production growing. These indicators are all expected to remain solid. We forecast a decrease in insolvencies of 6%, which may still be conservative.

The **Portuguese** economy is doing rather well and continued GDP growth is expected, as well as an improvement in unemployment. Industrial production growth should decline slightly but remains high. With the number of insolvencies still very high we expect a decrease in insolvencies of 14%.

UK insolvencies have ticked up over the past year. Cost pressures in the form of negative real wage growth have been straining consumer spending and while this should ease in 2018, Brexit uncertainty could cause more saving by consumers. The stimulus of the weak pound will fade as well, reducing the stimulus to UK manufacturers and exporters. The bankruptcy of Carillion, a construction giant, will also have significant consequences for many smaller construction companies, at the same time that the housing market is cooling off which we predict will drive a 4% overall increase in insolvencies.

North America – strong consumer spending, slight decrease in insolvencies

The **US** economic outlook is robust, at least for 2018. Overall economic growth is accelerating, supported by fiscal stimulus and strong consumer spending, low and falling unemployment, real wage growth, and access to cheap credit. Tax reform should also provide stimulus to US firms and support higher business investment, higher wage growth and inflation.

There are increasing downside risks in the form of more aggressive monetary tightening making finance more expensive, and also a slight USD recovery which will weigh on export competitiveness. However, the positives for 2018 clearly outweigh the negatives and with business confidence is at a decade high, we expect a 3% decrease in insolvencies.

Canadian economic growth has been catching up in 2017 (3%), driven primarily by stronger-than-expected private consumption growth. This year growth is expected to ease back slightly to 2%. Private consumption will likely ease as stronger growth will increase inflationary pressures and raise interest rates. Thus we expect a slight decrease in insolvencies in 2018 (-2%).

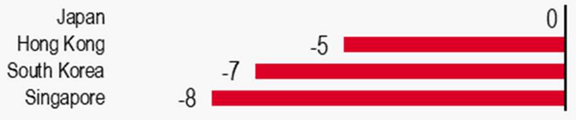
Developed Asia – strong performance, momentum slowing

Economic growth is expected to slightly weaken in **Japan** this year. Yen depreciation and stronger external demand have been driving up exports. Private consumption and capital spending are also boosting growth. But the ongoing slowdown in China could drive up yen value. Insolvencies were flat in 2017 at historically low levels. Again, since levels are already 60% of the pre-crisis level (2007), our forecast for 2018 is no change.

In **Singapore**, economic growth is expected to slow in 2018 from the strong pace last year, due to weaker growth in China, Singapore's most important export market. Still, the economy remains robust and inflation is subdued. Interest rates are expected to rise a bit, but remain low. In this environment insolvencies can fall further by 8% to the levels seen in 2011 and 2012.

4.4 Insolvency outlook 2018

% change y-o-y



Source: Atradius

BRICS markets – BRIS on the rise, C slowing down

This year, strong domestic demand and supportive macro policy are the main contributors to acceleration of growth in **India's** economy. With private consumption picking up this year, we expect a 10% decrease in insolvencies in 2018. Risks to the outlook are problems concerning banking frauds and non-performing loans, which call for restructuring of public sector banks.

With **China's** economy slowing down, we expect the number of insolvencies to increase in 2018. The excessive debt and speculative investments are meant to be reduced by targeted tightening measures and tougher rules in the financial sector. At the same time the Chinese government continues its financial liberation efforts to establish an increase in market forces.

In **Russia**, GDP growth is forecast at 1.8% in 2018, slightly higher than last year. Consumption remains the most important growth driver in 2018. Investment growth remains constrained by sanctions however, limiting investment opportunities and deleveraging. Insolvencies are expected to decrease 6% this year.

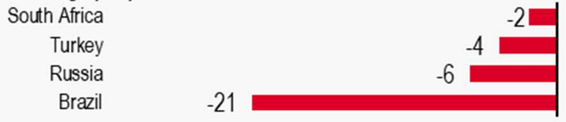
Turkey's economic performance was extraordinarily strong in 2017 and is expected to remain strong in 2018 with growth forecast at 4.4%. We expect insolvencies to decrease 4% as well. However, the increase in the corporate debt level during the economic boom could prove to be a burden for companies going forward, since credit support measures are being phased out in 2018 and interest rates are increasing. Moreover, exchange rate risk is high given the large share of foreign currency denominated corporate debt and the renewed weakness of the Turkish lira.

Overall, insolvencies move very cyclically in **Brazil** and are generally modest. However, a sharp decline in insolvencies is to be expected this year, considering the rebound of the economy following its deepest recession ever. Economic growth is forecast to be more than 2% this year, supported by record low inflation and interest rates, and improving labour market conditions. Moreover, in their 2017Q4 Bank Lending Survey, the Institute of International Finance reports easing bank lending conditions and forward-looking indicators suggest further improvements this year. Year-to-date insolvencies have declined 25% compared to the same period last year. For the year as a whole, we predict insolvencies will fall 21%, which is the model outcome. Rising political uncertainty ahead of the October elections could be a downside risk going forward though.

Finally, **South Africa** has been emerging from a technical recession with economic growth increasing to 2% this year, supported by improving confidence due to the installation of Ramaphosa as president. A stronger rand and lower inflation could result in an interest rate cut, supporting investments and private consumption.

4.5 Insolvency outlook 2018

% change y-o-y



Source: Atradius

Appendix: forecast tables

Table A1: Macroeconomic headline figures - developed markets

	GDP growth (% change p.a.)			Inflation (% change p.a.)			Budget balance (% of GDP)			Current account (% of GDP)			Export growth (% change p.a.)			Private cons. (% change p.a.)			Fixed investment (% change p.a.)			Government consumption (% change p.a.)			Retail sales (% change p.a.)			Industrial prod. (% change p.a.)		
	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019
Australia	2.3	2.7	2.6	1.9	2.4	2.4	-1.7	-1.3	-1.3	-2.3	-2.0	-2.3	3.8	4.5	6.6	2.7	2.5	2.1	3.1	2.3	-0.2	3.6	2.7	2.7	2.2	2.3	1.6	1.1	3.2	5.1
Austria	3.1	2.5	1.6	2.1	1.8	1.8	-1.2	-1.0	-0.9	1.9	1.0	1.0	6.2	4.1	3.0	1.5	1.9	2.0	4.9	3.8	2.1	1.2	1.6	1.4	1.1	0.4	2.2	3.9	3.8	3.3
Belgium	1.7	1.6	1.7	2.1	1.7	1.5	-1.3	-1.4	-1.2	-0.2	-0.5	-0.3	4.5	4.4	3.7	1.1	1.7	1.7	1.0	3.8	2.8	1.1	1.1	1.0	-0.1	1.6	1.7	3.0	3.0	1.8
Canada	3.0	1.8	2.1	1.6	2.2	2.0	0.3	-0.6	-0.9	-3.0	-3.4	-2.8	1.0	2.3	4.2	3.4	2.4	1.9	2.8	3.0	1.5	2.2	1.8	1.2	5.4	2.6	1.8	5.1	2.0	1.9
Denmark	2.2	1.9	1.9	1.1	1.0	1.8	-1.3	0.0	0.0	7.7	5.4	4.6	4.4	2.2	1.8	1.5	2.6	2.8	3.7	3.6	2.3	1.1	1.6	2.1	1.1	1.5	2.3	0.6	2.2	2.1
Finland	2.6	2.8	1.8	0.8	1.1	1.5	-0.4	-1.0	-0.6	0.7	0.0	0.0	7.8	3.9	2.8	1.6	2.0	1.7	6.3	3.6	2.7	1.3	0.4	0.6	3.1	3.7	1.6	3.5	1.0	2.0
France	2.0	2.1	1.9	1.0	1.4	1.5	-2.9	-2.8	-2.8	-1.2	-1.0	-0.9	3.3	5.0	3.4	1.3	1.5	1.7	3.8	3.6	2.8	1.6	1.4	1.2	3.7	2.8	2.3	2.4	2.6	1.5
Germany	2.5	2.3	1.8	1.7	1.6	2.1	1.1	0.9	0.3	7.9	8.1	7.8	5.3	6.0	4.1	2.1	1.5	1.7	3.9	3.5	3.4	1.6	1.7	1.6	3.0	1.6	1.5	3.3	3.2	2.3
Greece	1.3	1.6	2.7	1.1	0.8	0.7	0.9	0.4	0.7	-1.1	1.2	1.4	6.9	8.7	5.6	0.1	0.4	2.0	9.7	1.8	4.1	-1.2	2.3	1.9	1.3	1.3	2.2	4.5	1.1	3.0
Hong Kong	3.8	3.0	2.5	1.5	2.3	1.9	1.5	1.0	0.6	4.2	2.6	2.8	5.5	3.4	3.6	5.4	3.6	2.2	4.2	3.3	2.5	3.4	3.1	2.7	1.9	5.8	2.2	0.5	0.6	0.5
Ireland	7.8	4.9	2.2	0.3	1.4	1.5	0.5	0.6	0.5	12.4	3.3	4.0	6.8	2.2	2.1	2.1	3.0	2.6	-21.8	-4.7	3.0	1.8	3.2	2.7	4.1	12.2	7.7	-2.2	3.6	1.7
Italy	1.5	1.5	1.1	1.2	1.0	1.6	-1.9	-1.8	-1.3	2.7	2.9	2.4	6.0	4.8	3.5	1.3	1.0	0.8	3.9	4.4	1.3	0.1	0.4	0.4	-0.2	0.2	1.0	3.7	2.8	0.8
Japan	1.7	1.5	0.9	0.5	1.0	1.1	-5.0	-5.5	-4.9	4.0	3.9	3.6	6.8	5.1	2.7	1.0	1.0	1.0	2.6	2.6	0.7	0.1	0.6	0.7	1.9	0.5	0.9	4.7	1.6	1.8
Luxembourg	3.3	3.6	3.5	2.1	1.6	1.8	0.7	0.3	0.5	4.9	4.6	4.5	4.5	4.6	4.2	2.5	2.5	2.3	5.0	4.1	4.6	1.4	2.5	3.3	-24.0	2.4	3.2	-0.6	4.2	3.4
Netherlands	3.3	2.5	1.7	1.4	1.5	1.7	1.1	1.0	1.1	10.2	10.2	9.9	6.4	4.8	2.9	1.9	1.7	1.7	5.7	4.0	3.0	1.2	1.3	1.2	2.8	1.7	1.1	1.6	3.8	1.3
New Zealand	3.1	2.7	2.0	1.9	1.8	2.1	1.2	0.9	0.7	-2.7	-1.3	-1.5	2.6	4.6	2.3	4.5	3.4	2.3	3.3	6.0	2.9	4.7	1.8	0.9	5.6	4.5	2.3	2.0	2.5	2.5
Norway	1.9	2.2	2.0	1.9	1.8	1.8	5.2	4.9	4.4	5.1	4.3	3.8	1.0	2.0	3.1	2.5	2.7	1.8	3.7	3.9	2.9	2.0	2.1	1.6	2.1	1.4	1.8	2.2	0.6	0.1
Portugal	2.7	2.2	1.9	1.4	1.2	1.9	-1.0	-1.2	-1.2	0.6	0.4	0.1	7.8	5.2	4.5	2.3	2.1	1.5	9.1	3.9	3.9	-0.2	0.8	0.7	4.0	3.0	1.4	3.9	1.6	1.6
Singapore	3.6	3.1	2.4	0.6	0.8	1.8	-0.3	-1.6	-1.1	18.9	19.4	18.6	4.1	3.3	2.7	3.1	4.2	2.9	-1.8	3.7	4.7	4.1	1.1	2.9	1.4	4.2	2.9	10.6	5.7	3.7
Spain	3.0	2.9	2.4	2.0	1.5	1.7	-3.1	-2.3	-1.9	1.9	1.5	1.2	5.0	4.5	4.3	2.4	2.4	1.9	5.0	4.2	3.2	1.6	1.3	1.2	0.9	1.5	1.6	3.2	2.8	2.2
South Korea	3.1	2.8	2.6	1.9	1.6	2.0	1.2	0.5	0.4	5.1	4.3	4.8	1.9	4.8	4.2	2.6	2.6	2.3	8.6	3.0	2.4	3.4	5.4	4.3	2.0	2.7	2.3	2.5	0.9	3.8
Sweden	2.7	2.8	2.1	1.8	1.8	2.5	1.1	0.7	0.3	3.2	3.2	3.2	4.0	4.9	3.5	2.4	2.3	2.0	6.5	4.9	4.1	0.8	1.3	1.4	2.3	2.4	2.7	4.7	4.4	1.4
Switzerland	1.0	2.4	1.7	0.5	0.7	0.8	1.2	1.0	0.4	7.1	8.2	9.1	2.7	4.8	3.4	1.2	1.6	1.7	3.0	3.2	2.3	0.9	1.2	1.1	-1.1	0.6	1.4	5.8	5.8	3.8
United Kingdom	1.8	1.7	1.7	2.7	2.3	1.6	-2.2	-2.1	-1.6	-4.1	-3.1	-2.3	5.7	4.6	3.4	1.7	1.0	1.1	4.0	2.1	3.0	0.1	1.3	0.9	2.1	0.9	2.1	1.9	3.5	1.3
United States	2.3	2.8	2.4	2.1	2.6	2.0	-4.8	-5.0	-4.8	-2.4	-3.0	-3.2	3.4	4.1	2.8	2.8	2.6	2.1	3.4	5.0	4.0	0.1	1.5	2.2	3.9	2.5	2.7	1.6	4.1	3.7
Eurozone	2.5	2.2	1.8	1.5	1.4	1.7	-0.9	-0.8	-0.8	3.5	3.3	3.2	5.3	4.9	3.6	1.7	1.6	1.6	3.1	3.4	2.8	1.2	1.3	1.2	2.3	1.9	1.6	2.9	3.4	2.0

Source: Oxford Economics

Table A2: Macroeconomic headline figures - emerging markets

	GDP growth (% change p.a.)			Inflation (% change p.a.)			Current account (% of GDP)			Private cons. (% change p.a.)			Export growth (% change p.a.)		
	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019	2017	2018	2019
China	6.9	6.4	6.0	1.5	2.4	2.6	1.3	1.3	1.3	7.8	7.4	6.9	6.6	5.7	4.5
India	6.3	7.3	7.0	3.3	5.3	5.5	-1.5	-2.1	-2.1	5.7	8.9	7.7	5.5	5.6	6.0
Indonesia	5.1	5.2	5.2	3.8	3.4	4.0	-1.7	-2.0	-1.5	5.0	5.0	5.2	9.1	5.9	5.5
Malaysia	5.9	5.2	4.4	3.8	2.9	3.2	3.0	4.1	2.8	7.0	6.0	4.8	9.6	4.5	3.0
Thailand	3.9	3.2	3.0	0.7	1.2	1.3	10.8	9.9	10.5	3.2	3.2	3.5	5.5	4.9	3.4
Emerging Asia	**6.0**	**5.8**	**5.5**	**2.4**	**3.2**	**3.6**	-	-	-	-	-	-	-	-	-
Argentina	2.8	2.8	3.3	24.6	22.9	15.5	-4.8	-5.8	-5.5	3.6	2.8	4.1	0.4	3.3	6.9
Brazil	1.0	2.4	3.2	3.4	3.1	3.6	-0.5	-1.2	-1.6	0.9	2.5	3.2	5.7	6.2	4.5
Chile	1.6	3.8	3.0	2.2	2.4	3.0	-1.5	-1.8	-2.1	2.5	3.1	2.8	-1.0	4.2	2.1
Colombia	1.8	2.4	3.3	4.3	3.4	3.2	-3.4	-3.0	-2.8	1.7	2.4	3.3	-0.9	2.3	3.2
Mexico	2.3	2.2	2.4	6.0	4.5	3.5	-1.7	-1.8	-1.7	3.3	2.3	2.3	3.9	3.7	4.4
Peru	2.5	3.5	3.8	3.0	1.6	2.2	-1.7	-1.8	-1.5	2.4	3.4	3.5	7.3	4.1	5.7
Venezuela	6.8	6.6	6.4	3.5	3.9	4.1	4.5	1.0	1.8	9.2	6.9	6.6	14.3	13.1	11.0
Latin America	**1.1**	**2.0**	**2.9**	**6.3**	**5.8**	**5.0**	-	-	-	**1.6**	**2.5**	**3.3**	-	-	-
Bulgaria	3.7	3.4	2.6	2.1	2.5	2.5	4.5	4.0	4.0	4.5	3.5	2.4	3.8	5.4	3.1
CIS	2.1	2.3	2.0	5.5	5.3	5.5	-	-	-	-	-	-	-	-	-
Czech Republic	4.5	3.7	3.1	2.4	2.3	2.0	1.1	0.2	0.1	4.0	3.5	2.7	6.9	7.1	5.8
Hungary	4.2	4.1	2.7	2.3	2.7	3.2	3.0	3.1	3.0	4.7	4.9	3.0	7.1	6.2	4.3
Poland	4.5	4.2	3.5	2.0	1.7	2.1	0.1	-0.4	-0.6	4.8	4.2	3.5	6.8	5.1	4.5
Romania	6.8	4.9	2.5	1.3	4.5	2.7	-3.5	-2.1	-1.6	9.9	5.5	2.0	9.0	2.9	1.9
Russia	1.6	1.8	1.4	3.7	3.2	4.0	2.6	5.1	4.3	4.4	3.0	2.8	5.0	4.5	2.5
Turkey	7.3	4.4	3.1	11.1	9.9	9.0	-5.5	-6.1	-5.1	6.1	4.0	3.2	12.0	5.6	2.8
Ukraine	2.3	3.2	3.0	13.7	13.0	10.0	-3.3	-3.1	-2.9	3.6	3.5	3.5	1.6	4.5	4.5
Central & Eastern Europe	**3.1**	**3.0**	**2.5**	**3.6**	**3.5**	**3.7**	-	-	-	-	-	-	-	-	-
Egypt	4.2	4.7	4.9	29.5	13.4	12.5	-5.2	-4.1	-3.7	4.2	2.8	3.3	86.0	32.2	8.4
Morocco	4.1	3.2	3.9	0.8	2.2	2.3	-5.1	-5.0	-4.3	4.3	3.2	3.9	8.8	7.2	6.2
Qatar	1.3	3.1	3.4	0.4	2.6	3.4	2.6	5.2	7.0	17.7	10.3	6.2	6.7	3.3	2.7
Saudi Arabia	-0.7	2.0	2.8	-0.9	3.2	3.0	0.6	3.3	4.0	2.0	3.0	2.5	-3.2	1.1	3.1
Tunisia	2.0	2.1	2.3	5.3	6.5	6.1	-10.4	-9.9	-9.4	1.1	1.3	1.7	2.5	4.4	3.7
United Arab Emirates	1.7	2.7	3.8	2.0	4.4	4.0	7.4	4.9	3.9	1.5	2.0	2.0	3.1	4.2	5.2
MENA	**1.9**	**3.1**	**3.6**	**12.4**	**12.1**	**10.5**	-	-	-	-	-	-	-	-	-
Ghana	8.3	7.2	6.1	12.4	10.0	9.6	-4.5	-3.6	-3.9	3.3	6.6	6.5	15.0	7.4	7.4
Kenya	4.6	5.7	6.3	8.0	5.5	5.7	-7.1	-7.5	-7.3	4.6	5.5	6.0	3.1	4.9	6.4
Nigeria	0.8	2.6	3.2	16.5	13.4	11.9	1.7	2.4	2.0	-0.6	1.1	3.1	5.1	7.4	4.3
South Africa	1.3	2.0	2.0	5.3	5.0	5.3	-2.5	-2.8	-3.1	2.2	2.6	3.1	-0.1	3.1	1.8
Sub-Saharan Africa	**2.4**	**3.4**	**3.7**	**12.3**	**11.0**	**9.7**	-	-	-	-	-	-	-	-	-

Source: Oxford Economics

Table A3 Total insolvencies - annual percentage change

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018f
Australia	-4	18	3	-1	5	1	4	-22	10	-12	-7	-4
Austria	-6	0	9	-8	-8	3	-10	-1	-5	1	-3	-6
Belgium	1	10	11	2	7	4	11	-9	-9	-6	9	-2
Brazil	-35	-18	6	-18	-10	11	-9	-6	7	4	-8	-21
Canada	-10	-7	-2	-11	-9	-4	0	-1	3	3	-3	-2
Denmark	-	-	-	-3	-22	4	-15	-21	15	18	-4	2
Finland	-1	16	25	-13	3	0	6	-5	-14	-6	-10	-6
France	7	7	14	-5	-1	3	3	0	0	-8	-5	-7
Germany	-15	0	12	-2	-6	-6	-8	-7	-4	-7	-7	-6
Greece	-3	-35	68	-35	-4	19	-10	-36	-20	-49	8	-10
Hong Kong	7	-3	50	-43	-13	2	15	3	1	-9	-14	-5
Ireland	19	100	50	10	7	3	-19	-15	-10	-2	-15	-2
Italy	-41	22	25	20	8	3	13	11	-6	-9	-11	-10
Japan	6	11	-1	-14	-4	-5	-10	-10	-8	-6	0	0
Luxembourg	-	19	17	32	8	8	1	-19	3	13	-19	-8
Netherlands	-13	-14	53	-9	0	19	10	-22	-24	-19	-22	-8
New Zealand	-5	-35	45	-5	-12	-7	-13	-7	4	1	-20	-3
Norway	-6	41	47	-17	0	-13	18	6	-3	-1	4	0
Portugal	-	39	28	21	-5	46	1	-13	12	-6	-16	-14
Russia	-	14	80	8	-18	-6	9	18	1	-3	9	-6
Singapore	-7	-16	-12	-25	-1	14	14	-12	1	1	-9	-8
South Africa	4	5	25	-3	-11	-24	-13	-13	-5	-1	-3	-2
South Korea	-9	19	-27	-21	-13	-10	-18	-16	-14	-23	-11	-7
Spain	18	188	88	-4	15	32	10	-27	-21	-9	-2	-6
Sweden	-5	7	20	-4	-4	7	4	-6	-11	-5	6	-3
Switzerland	-	-7	24	20	-22	41	-5	-10	4	7	3	-6
Turkey	-	-	-	-	12	7	8	-9	-13	-10	19	-4
United Kingdom	-10	35	14	-18	4	-4	-9	-8	-10	0	4	4
United States	42	52	41	-7	-15	-16	-17	-19	-8	-2	-4	-3

Sources: Atradius, Macrobond, national sources

Table A4 Total insolvencies - index, 2007 = 100

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018f
Australia	100	118	121	120	126	127	133	104	115	101	94	91
Austria	100	100	110	101	93	96	87	86	82	83	81	76
Belgium	100	110	123	125	133	138	153	140	127	119	130	127
Brazil	100	82	87	71	64	71	65	61	66	68	63	50
Canada	100	93	91	81	74	71	71	71	73	75	73	71
Denmark (2009 = 100)	-	-	100	97	76	78	67	53	60	71	68	69
Finland	100	116	145	127	131	131	139	132	114	107	96	90
France	100	107	123	117	115	118	122	121	122	112	106	99
Germany	100	100	112	110	103	97	89	83	79	74	69	65
Greece	100	65	109	71	68	81	73	47	37	19	21	19
Hong Kong	100	97	146	83	72	74	85	87	88	81	69	65
Ireland	100	200	300	330	354	364	295	252	227	223	189	185
Italy	100	122	152	182	197	203	229	254	239	219	195	175
Japan	100	111	110	95	90	86	77	69	64	60	60	60
Luxembourg	100	119	139	183	197	213	215	175	180	204	165	152
Netherlands	100	86	132	119	120	143	157	122	92	75	58	53
New Zealand	100	65	94	89	78	73	63	59	61	62	49	48
Norway	100	141	207	171	172	150	176	186	180	179	187	187
Portugal	100	139	179	216	205	300	303	262	294	277	233	201
Russia	100	114	205	222	183	173	188	222	223	216	236	222
Singapore	100	84	74	56	55	63	72	64	64	65	59	54
South Africa	100	105	131	127	113	86	75	66	62	61	59	58
South Korea	100	119	87	68	59	54	44	37	31	24	22	20
Spain	100	288	540	520	598	791	866	635	501	458	447	421
Sweden	100	107	128	123	118	126	130	122	108	103	109	106
Switzerland	100	93	115	138	107	151	143	130	135	144	148	139
Turkey (2010=100)	-	-	-	100	112	119	129	118	102	92	109	105
United Kingdom	100	135	153	125	130	124	113	104	93	93	97	101
United States	100	152	215	199	169	142	118	95	88	85	82	80

Sources: Atradius, Macrobond, national sources