Press release

Euler Hermes 2017 Economic Outlook:
Superheroes, sidekicks, and villains: the Guardians of the economy

PARIS – 18 JANUARY 2017 – Despite economic and political hurdles from China's readjustment, Brexit, and the unexpected U.S, election results, global GDP growth should reach a resilient +2.5% by year-end 2016, according to Euler Hermes, the worldwide leader in trade credit insurance. In 2017, growth should pick up to +2.8%, remaining below +3% for the seventh consecutive year -- a glass ceiling that has become harder to break each year.

"A series of unexpected events jeopardized global growth in 2016, defying all forecasts. In parallel with the rise in populist and protectionist votes, global trade volume growth only reached +1.9%, its lowest level since 2009," said Ludovic Subran, chief economist at Euler Hermes.

However, various forms of global and local resilience came to the fore to offset the tremors and turbulences. With Chinese GDP growth at +6.7%, UK growth at +2%, oil prices ending the year above 50 USD/bbl, and stock markets reaching record highs after Trump's election, things were not all bleak.

The slight expected pick-up in 2017 is due to a large extent to the U.S., an exit from recession in Russia and Brazil, and resilience in Europe and Asia. Wider divergence between regions can be expected:

- The U.S., or Captain America, would benefit from a fiscal boost pushing growth to +2.4% in 2017. After a year of uncertainty and economic pause, the aftermath of the election is already restoring confidence. Euler Hermes' baseline scenario foresees a partial implementation of the electoral pledges, including the launch of a fiscal stimulus package for 2017.The active policy-making should spur private investment if political noise, faster Fed tightening and renewed protectionism are contained.

- Spider-Man, or the Eurozone, should grow +1.6% in 2017, wearing its web-shooters. It will continue to face its set of troubles, from Brexit to the Italian banks situation, but strong institutional stopgaps (accommodative monetary policy, fiscal stimuli, and European programs) will help contain risks. The regime switch in multilateralism could also mean that Europe flexes its policy muscles on industry, innovation and trade to dodge the balls coming from the U.S. and China. The busy election calendar could postpone decisive action to 2018, but major ideas could be put forward this year to generate traction from the Member States.

- The Chinese Iron Man will address its fragilities, such as credit risk and excess capacities, to avoid further volatility. Strong public support and cautiously accommodative monetary policy should help reach +6% growth this year. The failed attempt to achieve Market Economy Status and expected protectionist measures from the U.S. could mean retaliation and heightened political tensions between the world's two biggest economies. The EU and Japan are expected to make concessions to preserve trade relations with China. As a consequence, China would accelerate its outside influence agenda: One Belt One Road, the Regional Comprehensive Economic Partnership and RMB internationalization.

- In emerging markets, the absence of a broad-based acceleration will increase selectivity and the emerging Fantastic Four will need superpowers to attract investors. Some will capitalize on buffers (South Korea); private sector spending will be pivotal in others (e.g. Russia and India); elsewhere, the business cycle may be limited by ongoing adjustments (Brazil and South Africa); while another group of countries may even face growing imbalances (Mexico, Turkey).

	2015	2016	2017	2018
Global GDP growth	**2.7**	**2.5**	**2.8**	**2.8**
United States	2.6	1.6	2.4	2.2
Brazil	-3.8	-3.5	0.6	1.8
Mexico	2.5	2.0	2.2	2.4
United Kingdom	2.2	2.0	0.9	0.6
Eurozone	***0.0***	***1.7***	***1.6***	***1.5***
Germany	1.5	1.8	1.7	1.7
France	1.2	1.3	1.4	1.3
Italy	0.6	0.9	0.6	0.8
Spain	3.2	3.3	2.3	2.0
Central and Eastern Europe	**0.2**	**1.2**	**1.7**	**2.0**
Russia	-3.7	-0.6	1.0	1.2
Turkey	6.1	1.3	1.0	2.0
Asia	**4.9**	**4.8**	**4.7**	**4.5**
China	6.9	6.7	6.2	5.8
Japan	0.6	0.8	1.0	0.9
South Korea	2.6	2.7	2.5	2.7
India	7.6	7.2	7.5	7.5
Middle East	**2.1**	**2.1**	**2.2**	**2.6**
Saudi Arabia	3.4	1.2	2.0	2.5
Africa	**3.1**	**1.6**	**2.6**	**3.3**
South Africa	1.3	0.5	1.5	1.5

** Weights in global GDP at market price, 2016*

"The low growth environment has yielded to key changes in the world economy. As in X-Men comic books, there are positive heroes and toxic characters. Reflation, isolationism of trade and financial flows, and policy nudges will shape most of the 2017-18 risks and opportunities for businesses around the world", warned Ludovic Subran.

Several 2017 factors favor a contained price recovery, reflating the world economy

Low growth drove the balance sheet adjustments of indebted countries and sectors in 2016. Lower demand growth meant commodity prices and the general price level took a hit, causing sluggish turnover growth and fewer investment incentives.

Several factors trigger a better price outlook. First, oil prices will benefit from a positive base effect and are expected to plateau at USD54 per barrel in 2017. Second, in the U.S., active policy-making will cause prices to increase faster as the economy is nearly full. Third, supportive policies are finally boosting demand growth. In China, the construction sector made a noticeable comeback, supporting worldwide metal prices. The result is the end of deflation for Chinese producer prices and a timid recovery of the manufacturing sector globally. Accommodative monetary policy has been also helping: low credit costs have paved the way to a recovery in residential investment worldwide, and market inflation expectations are now above +2% in the U.S. In addition, new pledges to boost infrastructure spending are driving prices up.

(De)globalization: The end of the Magneto effect for trade and financial flows?

Global trade growth could recover by +3.5% in 2017 in value terms, as imports from the U.S., Europe, and the emerging world are on the rise. Volume growth is forecast at +2.9% in 2017. Regime switch in demand (China's rebalancing; energy autonomy in the U.S.; adjustments in the emerging world), rising direct and indirect protectionism, and servitization/digitalization explain this trend. Going forward, political escalation on location choices for visible industries (e.g. automotive), the shortening of supply chains, and greater retention of value-added activities will be the norm as the U.S. and China have moved in that direction.

Another trend is also vivid: financial balkanization, or financial de-globalization, which will accelerate isolationism if not addressed. Indeed, financial flows within and between countries continue to disappoint: (i) capital is not going into the real economy and credit conditions are still too conservative in Asia Pacific and Latin America; (ii) savings are staying in high-income markets, even if not yielding much. Total domestic financing grew at a compound annual growth rate of +5% between 2011 and 2015, compared to only +0.5% for cross-border bank credits.

More policy nudges expected everywhere, could look like a perfect storm

2017 will be another year of heavy politics weighing on economic performance. The U.S. is under scrutiny, as policy decisiveness is expected to be a trait of the Trump administration. The risk of retaliation is high. Contagion risks are also high as the U.S. is the world's largest economy, the most interdependent (largest current account deficit, hegemony of the dollar), and the market place for many global goods and services.

Europe will have to deal with a heavy political calendar: The Netherlands election in March, France in April and Germany in September. Mainstream parties face strong challengers. Yet Europe is showing policy resilience and should weather surprises.

In China, pressures are mounting to deliver promises and restore the confidence needed to finance growth with savings from the Chinese people. Still, the country is likely to become more reform-oriented and less supportive after the Congress meeting in October 2017. In other emerging markets, stormy weather will cloud the outlook where numerous elections are scheduled (Iran, South Africa, Mexico, Brazil).

"The adequacy of policy responses by established political forces, and the resilience of the private sector, will largely determine who will weather political uncertainty and a decrease in global liquidity," concluded Subran. "Beggar-thy-neighbor policies are a clear risk and businesses around the world have to rediscover economic, political and country risk intelligence, scenario and contingency planning, as well as existing hedging instruments."

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