ECONOMIC UPDATE

GLOBAL & INDIAN

July 2017

US second-quarter growth accelerates to 2.6%.

The pick-up was helped by consumer spending in the quarter expanding at a pace of 2.8%, and businesses stepping up spending on equipment. The growth rate for the first quarter was cut to 1.2%, compared with the previous estimate of 1.4%.Earlier this week, the IMF revised down its US growth forecast for this year from 2.3% to 2.1%.President Trump has pledged to pursue policies to boost the US economy, including cutting corporate and individual taxes, but has faced a Washington impasse. He has set an ambitious 3% growth target for 2017.

Consumer spending, which makes up more than two-thirds of the US economy, accelerated from the 1.9% growth figure from the first quarter. The resurgence in consumer spending accounted for most of the upturn in economic growth in the second quarter. Stuart Hoffman, PNC senior economic adviser, said that "real consumer spending once again did the heavy lifting" in terms of economic growth. But with wage growth remaining sluggish there are concerns spending may slow in the next quarter. A Labor Department report on Friday said its Employment Cost Index, which measures labour costs, increased 0.5% in the April to June period after growing 0.8% in the first quarter.

The latest growth figures suggest the Federal Reserve could still raise interest rates later this year, which would be the third increase in 2017. On Wednesday, the central bank left rates unchanged following its latest meeting. However, analysts said the data suggested Fed was under no pressure to act quickly."Although growth is solid, the lack of wage pressure buys the Fed plenty of time, and works with a very 'gradual' tightening cycle," said Alan Ruskin, of Deutsche Bank in New York.

Japan household spending jumps most since 2015 in sign of sustainable growth

Japanese household spending in June jumped the most since 2015 as job availability improved to a fresh 43-year high, in a sign the tightening labor market is helping push up wages and consumer spending — albeit gradually. Underscoring stubbornly low inflation despite the tightening job market, core consumer prices rose just 0.4 percent in June from a year earlier, unchanged from the previous month and still far below the Bank of Japan's ambitious 2 percent target. The batch of data points to a steady growth in the Japanese economy, the world's third largest, in the April-June quarter, supports the central bank's upbeat economic view.

The BOJ last week left monetary policy steady but once again pushed back the timing for hitting its price goal, highlighting the gap between steady growth and weak inflation and reinforcing the view that it will take some time to scale back its massive stimulus. Japan's economy expanded at an annualized 1.0 percent at the start of this year, posting a fifth straight quarter of growth on robust exports and a pick-up in private consumption. Domestic demand holds the key for a sustained expansion as net exports - or exports minus imports - likely trimmed gross domestic product growth in the April-June period, analysts say.

In an encouraging sign for private consumption, which comprises some 60 percent of the economy, household spending rose 2.3 percent in the year to June, up for the first time in 16 months and the biggest annual gain since August 2015.That compared with economists' median estimate of a 0.6 percent gain in a Reuters poll, data by the Ministry of Internal Affairs and Communications showed on Friday. Retail sales also grew 2.1 percent in the year to June, separate data showed.

Firmer consumption data indicates that the tightening job market is helping improve wages and household incomes, which in turn may stimulate consumer spending. The jobless rate unexpectedly fell to 2.8 percent in June, while the availability of jobs rose for the fourth straight month to hit the highest since February 1974, separate data showed.

Still, Japan's consumer prices are stubbornly weak because of companies' wariness about raising prices for fear of losing cost-sensitive customers, accentuating the challenge facing the BOJ in accelerating inflation towards its 2 percent target. The rise in the core consumer price index (CPI), which includes oil products but excludes fresh food prices, followed a 0.4 percent gain in May and matched a median market forecast.

IMF cuts 2017 growth forecasts for UK and US

The International Monetary Fund has cut its growth forecast for the UK economy this year after a weak performance in the first three months of 2017.In its first downgrade for the UK since the EU referendum in June last year, the IMF said it expected the British economy to expand by 1.7% this year, 0.3 points lower than when it last made predictions in April.

The Fund raised its forecasts for the UK after the Brexit vote as a result of the much stronger than envisaged activity in the second half of 2016. In October 2016, it pencilled in growth of 1.1% for 2017, raising this forecast to 1.5% in January this year and to 2% in April.

Maurice Obstfeld, the IMF's economic counsellor, pointed to a marked change in early 2017. He said the UK's growth forecast had been lowered based on its "tepid performance" so far this year, adding: "The ultimate impact of Brexit on the United Kingdom remains unclear."

The IMF left its growth forecast for the UK in 2018 unchanged at 1.5% but said one key risk facing the global economy was that the Brexit talks would end in failure. It contrasted its gloomier outlook for the UK with a rosier forecast for the rest of the EU, with 2017 growth upgrades for the four biggest Euro zone countries – Germany, France, Italy and Spain. Germany has been revised up by 0.2 points to 1.8%, France by 0.1 points to 1.5%, while Italy and Spain have both been revised up by 0.5 points to 1.3% and 3.1% respectively.

The Fund produces a world economic outlook in April and October to coincide with its spring and annual meetings, but provides updates in January and July. Launching the report in Kuala Lumpur, Obstfeld said the IMF had left its global growth forecasts unchanged at 3.5% in 2017 and 3.6% for next year, noting that the stronger performance by the Euro zone, China and Japan had been offset by weaker performances elsewhere."The recovery in global growth that we projected in April is on a firmer footing; there is now no question mark over the world economy's gain in momentum," Obstfeld said.

He added that Donald Trump's failure so far to push through his promised package of tax cuts had dampened US growth prospects."From a global growth perspective, the most important downgrade is the United States," he said. "Over the next two years, US growth should remain above its longer-run potential growth rate. But we have reduced our forecasts for both 2017 and 2018 to 2.1% because near-term US fiscal policy looks less likely to be expansionary than we believed in April."

Three months ago, the IMF said it expected growth in the world's biggest economy to be 2.3% this year and 2.5% next. The Fund said that while the risk of a repeat of the electoral shocks of 2016 – Brexit and Trump's presidential victory – had declined; policy uncertainty remained at a high level and could rise further. It singled out "difficult-to-predict US regulatory and fiscal policies, negotiations of post-Brexit arrangements, or geopolitical risks", all of which it said could harm confidence, deter private investment, and weaken growth.

China willing to give up growth in short-term

A senior Chinese economic official indicated that policymakers would be willing to sacrifice some short-term economic growth in order to deal with systemic risks. China is trying to contain rising debt and defuse property bubbles amid fears such risks could derail the world's second-largest economy if not handled well, but policymakers will be treading warily ahead of a key party meeting later this year.

"(China can't let smaller risks) eventually lead to large systemic risks that would cause serious harm to China's economy," Yang Weimin, vice minister of the Office of the Central Leading Group on Financial and Economic Affairs, said."We would rather sacrifice in some other areas, but also deal with the relationship between stable growth and risk prevention", Yang said.

But Yang also said China could achieve both goals of maintaining steady growth while containing debt levels. China's total private and public debt has exceeded 250 percent of GDP, up from 150 percent before the global financial crisis, according to the Organisation for Economic Co-operation and Development. Chinese regulators have already launched a crackdown on riskier types of financing, but the drive has pushed up short-term borrowing costs.

The government's efforts to lower debt levels in the economy will be a long-term process and the key is to push state-owned firms to deleverage, Yang said."We cannot allow the leverage ratio to continue to rise in order to safeguard economic growth," he said.

China's economy grew a faster-than-expected 6.9 percent in the second quarter, matching the first quarter's pace, supported by solid exports, industrial production and consumption. But analysts expect growth to slow in the second half as the property sector cools and borrowing costs for firms climb. Chinese leaders have pledged to keep the economy steady as they prepare for a five-yearly transition later this year. Government officials have said steady growth in the first half could help hit the full-year target of around 6.5 percent and achieve even better results. Yang also said that China's economic outlook is bright and the country will not fall into the middle-income trap.

China will fine-tune monetary policy to offset the impact of changes in market interest rates, said Wang Zhijun, another party official. Higher market interest rates have started to trickle down to the real economy. The weighted average lending rate of China's non-financial firms rose by 26 basis points in the first quarter to 5.53 percent, according to data from the central bank. Data for the second quarter is due in early August.

HSBC reports 5% rise in H1 profit, announces up to $2 billion share buyback Once 'fragile' India gets thumbs up even as rates set to fall China's economy grew 6.9 percent in the second quarter from a year earlier, faster than expected and in line with the first quarter's growth. Analysts polled by Reuters had expected the economy to expand 6.8 percent in the April-June quarter, slightly slower than the previous quarter's robust 6.9 percent pace. The government is aiming for growth of around 6.5 percent in 2017, slightly lower than last year's actual 6.7 percent, which was the weakest pace in 26 years.

Many analysts expect the world's second-largest economy to lose steam later in the year as policy measures to rein in red-hot housing prices and a rapid build-up in debt take a greater toll on growth. Gross domestic product (GDP) in April-June grew 1.7 percent quarter-on-quarter, compared with growth of 1.3 percent in January-March, the National Bureau of Statistics said on Monday.Analysts had expected quarterly growth would quicken to 1.7 percent.

No 10 says free movement ends when UK leaves EU

On Friday, Chancellor Philip Hammond warned full controls could take "some time", prompting speculation free movement may continue in all but name after the UK leaves in March 2019.But amid claims of splits in cabinet, No 10 has moved to make clear free movement will end when the UK leaves. It said: "It would be wrong to suggest it... will continue as it is now."Downing Street's move followed days of uncertainty over future immigration policy during any transitional phase after Brexit.

The PM's spokesman said plans for a registration system for migrants arriving after March 2019 had been set out last week, and Prime Minister Theresa May had raised, as long ago as January, the prospect of a transition period before the post-Brexit system was implemented. At the moment, citizens from the other 27 EU member states have the right to come and work and live in the UK. Ministers have said Brexit will enable the UK to control who comes to the country and in what numbers but there has been debate within government about how quickly this will happen and what its impact will be.

Mr Hammond has said the cabinet is united behind the need for a transitional period of up to three years after Brexit, a period of time in which he said many arrangements would "remain very similar to how they were the day before we exited the European Union".

The chancellor has suggested that many things will remain the same after Brexit. He has said his goal is to minimise the level of disruption to British business and consumers, by retaining access to European markets both for goods and workers. But International Trade Secretary Liam Fox has warned that allowing unregulated EU immigration to continue would be a betrayal of last year's referendum result, while a former Brexit minister, David Jones, suggested some ministers were being "kept out of the loop" by No 10 and the Treasury. No 10 said the shape of post-Brexit immigration controls would become clearer in due course, with legislation due to be presented to Parliament later this year.

"It would be wrong to speculate on what these might look like or to suggest that freedom of movement will continue," the spokesman said."Free movement will end in March 2019. We've published proposals on citizen's rights. Last week the home secretary set out a registration system for EU nationals arriving post March 2019.

China's international trade grows less than expected, surplus with US dips

China reported July exports were up 7.2 percent in dollar terms, while imports were up 11.0 percent in dollar terms. Analysts polled by Reuters expected a 10.9 percent rise in exports and a 16.6 percent increase in imports in dollar terms. China on Tuesday reported July exports were up 7.2 percent in dollar terms, while imports were up 11.0 percent in dollar terms. Both were lower than expected. In June, China reported a 17.2 percent increase in imports and an11.3 percent on-year rise in exports in dollar terms. The declines can be partly explained, according to Capital Economics China economist Julian Evans-Pritchard, by negative price effects due to cooling producer price inflation. Despite the slowdown in trade growth momentum, China's exports and imports were still registering strong expansion on a year-on-year basis, said Rajiv Biswas, IHS Markit's chief economist for Asia Pacific.

China's July trade balance was $46.74 billion while the country's surplus with the U.S. was $25.2 billion. The two countries' trade is closely-watched amid current tensions between the economic giants about trade practices. A month earlier, Chinese customs data has shown China ran a $25.4 billion surplus with the U.S.IHS' Biswas said trade tensions between the U.S. and China have eased after the Chinese cooperated on tougher sanctions on North Korea. In Yuan terms, July exports were up 11.2 percent in Yuan terms while imports were up 14.7 percent in Yuan terms from a year ago."Despite the uptick at the end of [the second quarter], trade growth now appears to be on a downward trend," Evans-Pritchard said.

The sharp decline in import growth since the beginning of the year suggests domestic decline is softening, he added. "With the headwinds to domestic demand from policy tightening increasing, we think the slowdown in import growth has further to run," he said. Further downside to export growth however should be limited due to the positive outlook for China's main trading partners, said Evans-Pritchard. Market watchers keep their eyes on the world's second-largest economy ahead of a key Communist Party meeting in the fall.