

GLOBAL ECONOMIC OUTLOOK - DECEMBER

Monetary Department
External Economic Relations Division

2015

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Cut-off date for data

11 December 2015

CF survey date

7 December 2015

GEO publication date

18 December 2015

Notes to charts

ECB and Fed: midpoint of the range of forecasts.

The arrows in the GDP and inflation outlooks indicate the direction of revisions compared to the last GEO. If no arrow is shown, no new forecast is available. Asterisks indicate first published forecasts for given year.

Forecasts for EURIBOR and LIBOR rates are based on implied rates from interbank market yield curve (FRA rates are used from 4M to 15M and adjusted IRS rates for longer horizons). Forecasts for German and US government bond yields (10Y Bund and 10Y Treasury) are taken from CF.

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This year's final issue of Global Economic Outlook presents the regular monthly overview of recent and expected developments in selected territories, focusing on key economic variables: inflation, GDP growth, leading indicators, interest rates, exchange rates and commodity prices. In this issue, we also focus on the Chinese economy and its role in international trade. We investigate the causes of the sizeable fall in imports into China observed for almost a year now, and assess its potential impacts on international trade.

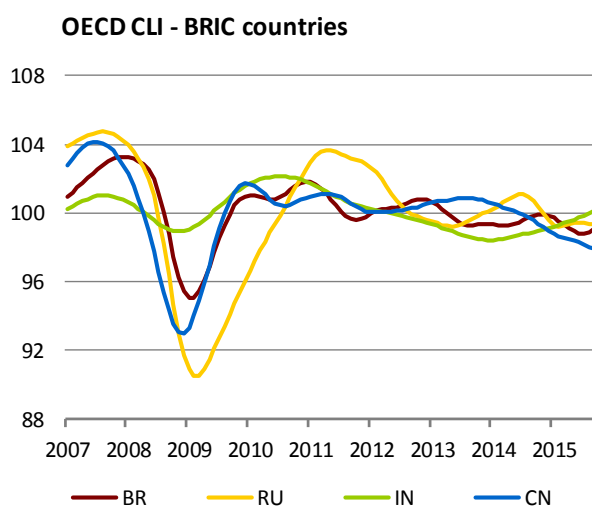
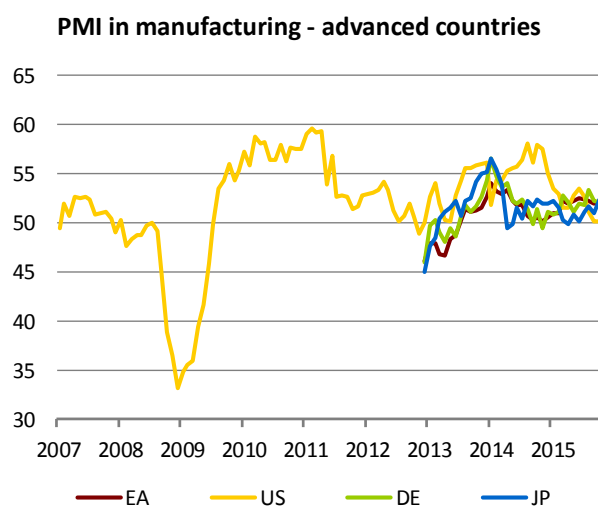
For the advanced economies, 2015 was a better year than 2014 as regards economic performance. What is more, this performance is highly likely to be sustained or very slightly exceeded in 2016. Whether this outlook materialises will depend, among other things, on how the current European migrant crisis is handled. The US economy was one of the engines of the global economic recovery again in 2015 (especially among advanced countries). After faltering briefly this year, Canada is also expected to contribute in 2016 to the solid growth outlooks of the G7 countries this year and the next; the UK should just about maintain its current rate of growth next year. The latest results for the Japanese economy indicate an improvement compared to last year, and a similar rate of improvement is expected in 2016. However, the assessment of 2015 is not purely positive from a macroeconomic point of view, since inflation in advanced countries has not yet been steered towards the 2% level generally regarded as price stability. Average inflation in Western European countries will probably be just 0.1%. This matches the average inflation rate in EU and euro area countries. The situation in the USA is no better. Despite being number one in terms of economic growth, the USA will record average consumer price inflation only 0.1 pp higher than the average in Europe. However, the outlooks for 2016 bring hope that consumer price inflation will at least exceed 1% in advanced economies, with the exception of Japan.

The GDP growth outlooks for the emerging BRIC countries remain very mixed. On the one hand, China and particularly India are showing strong economic growth. But while the Indian economy is gaining pace, the Chinese economy is slowing. This trend can be expected to continue into 2016, accompanied in China by a very slight increase in consumer price inflation to 2%; in India, inflation is expected to stabilise at around 5%, a level commensurate with India's buoyant economic growth. The two other BRIC economies, Russia and Brazil, are and will continue to be considerably worse off. Unlike India and China, Brazil and very probably also Russia will be in recession this year and the next. Moreover, the two countries will face high inflation (in relation to their economic growth), which is expected to reach double figures this year. Inflation is expected to drop to around 8% in Russia and 6% in Brazil next year.

The euro area interest rate remains negative at the one-year horizon for short maturities, partly in reaction to the expected monetary policy easing signalled by the ECB. The Fed is expected to raise its rates soon, most likely at its December meeting. According to CF, the US dollar is expected to appreciate with greater or lesser intensity against all the monitored currencies at the one-year horizon, the only exception being the Russian rouble, which is expected to be broadly stable.

The oil price outlook remains very slightly rising at the one-year horizon, but its path moved downwards again compared to the previous month. Oil prices are expected not to exceed USD 55 a barrel at the end of 2016. Natural gas prices based on long-term contracts normally lag behind oil prices and are therefore expected to continue falling in the next few months; a warm start to the winter and higher stocks are also now beginning to affect prices. The non-energy commodity price index also fell modestly compared to the previous month. The index is expected to increase only slightly at the one-year horizon owing to movements in both its sub-indices, i.e. food commodities and industrial metals.

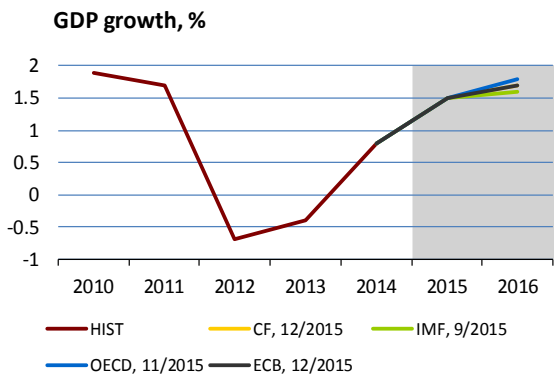
Leading indicators for countries monitored in the GEO



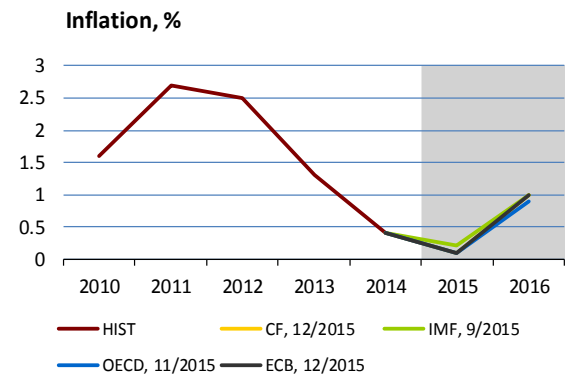
Zdroj: Bloomberg, Datastream

II.1 Eurozone

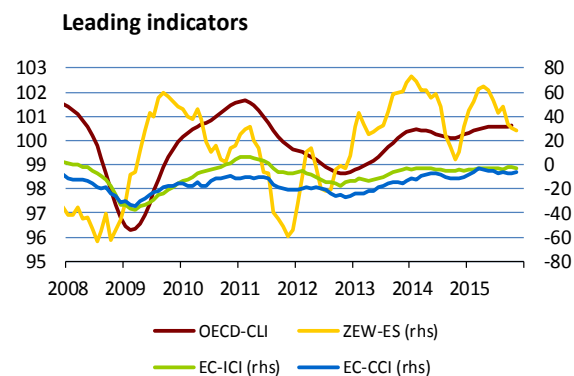
The euro area economy will probably grow by 1.5% this year. The growth is expected to accelerate slightly next year. In 2015 Q3, GDP increased by 1.6% year on year and 0.3% quarter on quarter. The growth was again fostered mainly by household consumption, but government investment and consumption also increased. Industrial production rose only moderately in Q3 in both year-on-year and quarter-on-quarter terms in Q3. However, the PMI in manufacturing increased moderately compared to the previous month to 52.8 points in November, indicating an improvement in the situation in the near future. Retail sales grew by 2.7% year on year and 0.6% quarter on quarter in Q3. This, combined with a continuing decline in the unemployment rate, create conditions for a further rise in household consumption. It is now evident that the average price level in the euro area has been virtually flat this year. Prices are expected to increase in 2016, but inflation will remain well below the ECB target. The ECB therefore eased monetary policy further at its meeting in December. This move had been expected by the markets, as the ECB had signalled it in advance. The ECB extended its current bond purchase programme until at least March 2017. However, it did not increase the total monthly size of the purchases. This, together with only a slight cut in its deposit rate to -0.3%, disappointed the markets. The ECB also announced that it would reinvest the proceeds of maturing bonds and start buying municipal bonds. Euro area HICP inflation was flat at 0.1% in November. The only slight annual rise in the price level overall was due mainly to higher food and services prices, while energy prices recorded a significant annual drop as in the previous month. Inflation excluding energy and food prices stood at 0.9% in November. The 3M Euribor continued to fall, breaking through the -0.1% level. Its outlook at the one-year horizon is even slightly lower. The outlook for the ten-year German government bond yield was unchanged at the one-year horizon.



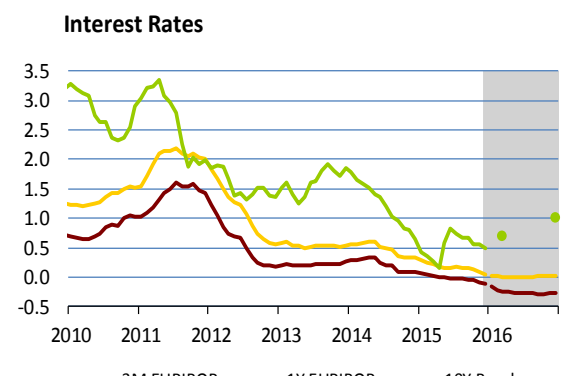
	CF	IMF	OECD	ECB
2015	1.5	1.5	1.5	1.5
2016	1.7	1.6	1.8	1.7



	CF	IMF	OECD	ECB
2015	0.1	0.2	0.1	0.1
2016	1.0	1.0	0.9	1.0



	OECD-CLI	EC-ICI	EC-CCI	ZEW-ES
9/15	100.6	-2.3	-7.0	33.3
10/15	100.6	-2.0	-7.5	30.1
11/15		-3.2	-5.9	28.3

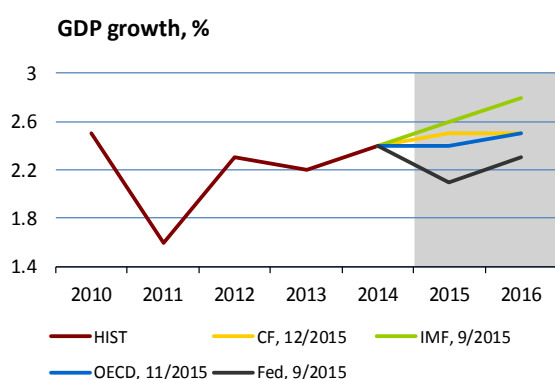


	11/15	12/15	03/16	12/16
3M EURIBOR	-0.09	-0.11	-0.26	-0.28
1Y EURIBOR	0.08	0.05	0.00	0.03
10Y Bund	0.55	0.50	0.70	1.00

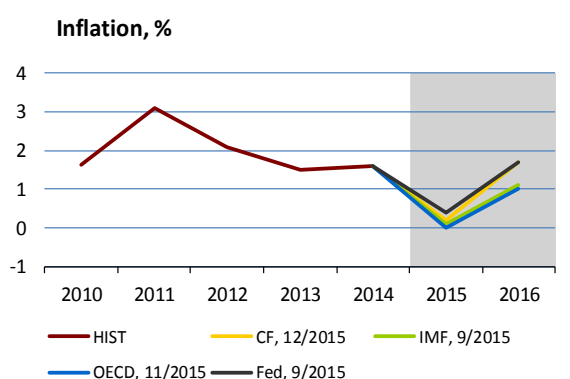
II.2 United States

The US economy expanded by a solid 2.1% in 2015 Q3 according to the second estimate (the first estimate had been 1.5%). Domestic demand maintained growth of 3% (in annualised quarter-on-quarter terms), while the decline in inventories was smaller than in the previous estimate. On the other hand, firms' profits decreased further due to the strong dollar and lower external demand. Industrial output also slackened considerably in year-on-year comparison in September and October, with energy producers in particular facing problems related to lower commodity prices. The PMI in manufacturing fell below 50 in November to its lowest level since June 2009 (48.6). The biggest drop was registered for new orders. The labour market, by contrast, recorded a considerable improvement. The number of new jobs in the non-agricultural sector rose by 211,000 in November (as compared to an estimate of 200,000), while the figures for the previous two months were revised up by 35,000. Unemployment was flat at 5.0% in September and October, while the participation rate edged up in November. Consumer confidence and retail sales fell further.

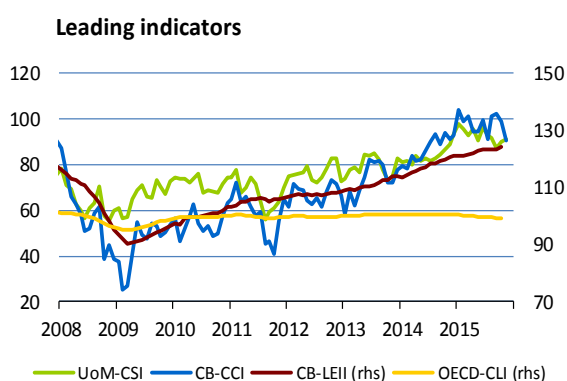
Annual consumer price inflation turned positive again in October (0.1%), while core inflation stayed at the September level (1.9%). The strongly positive labour market trends and solid GDP growth are fuelling speculation that the Fed will raise rates in December for the first time since 2004. A total of 87% of CF panellists believe that the Fed will take this step. The expected interest rate path also shifted upwards due to the new data. The December CF raised its GDP growth and inflation outlooks for 2015 by 0.1 pp. The inflation outlook for 2016 was unchanged, while the GDP growth outlook was lowered by 0.1 pp.



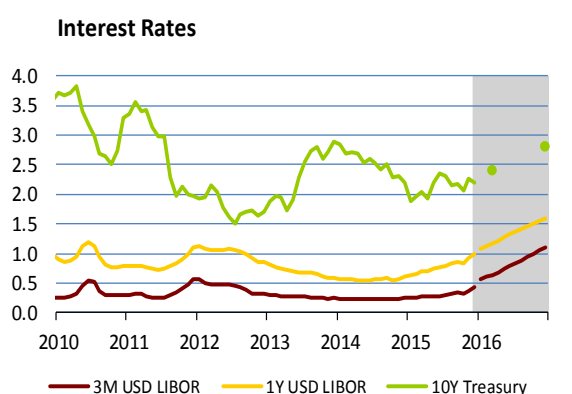
	CF	IMF	OECD	Fed
2015	2.5	2.6	2.4	2.1
2016	2.5	2.8	2.5	2.3



	CF	IMF	OECD	Fed
2015	0.2	0.1	0.0	0.4
2016	1.7	1.1	1.0	1.7



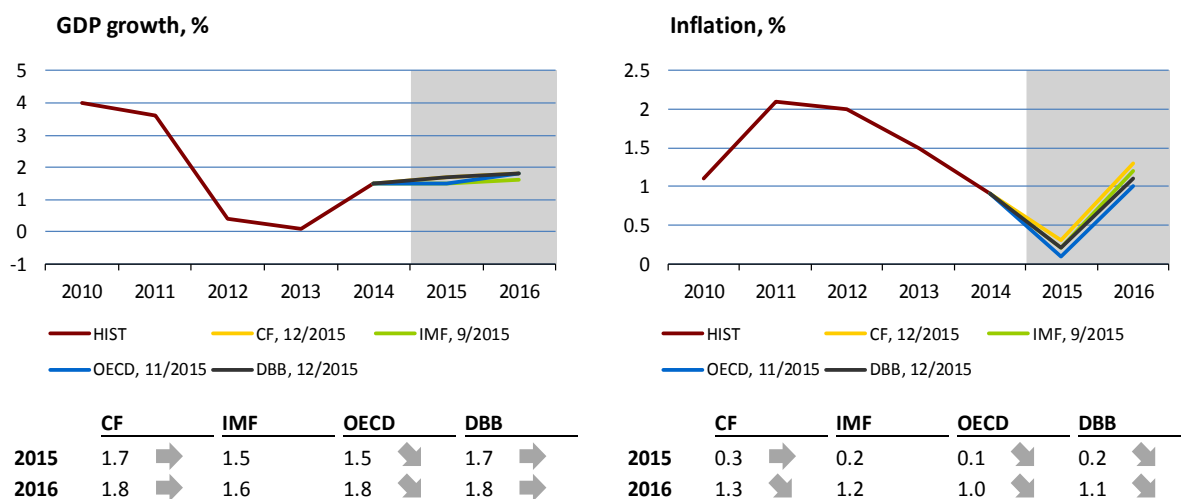
	CB-LEII	OECD-CLI	UoM-CSI	CB-CCI
9/15	123.3	99.3	87.2	102.6
10/15	124.1	99.2	90.0	99.1
11/15			91.3	90.4



	11/15	12/15	03/16	12/16
USD LIBOR 3M	0.37	0.42	0.62	1.10
USD LIBOR 1R	0.93	0.93	1.17	1.60
Treasury 10R	2.27	2.19	2.40	2.80

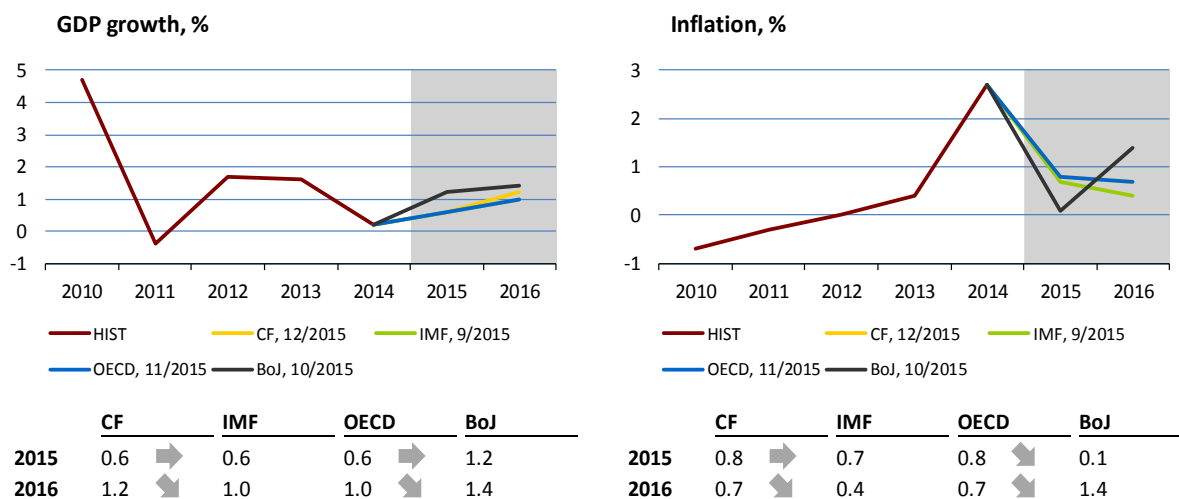
II.3 Germany

German economic growth slowed by 0.1 pp quarter on quarter to 0.3% in 2015 Q3, but in annual terms it accelerated by 0.1 pp to 1.7%. The outlook for the rest of this year has worsened somewhat in recent months. Industrial orders decreased and most leading indicators were roughly flat or increased only slightly. The December CF predicts GDP growth of 1.7% for this year as a whole. Similar outlooks were published by other institutions (the German government and the European Commission). However, the Bundesbank revised its forecast down to 1.5%. Next year, GDP growth is expected to reach 1.8%. German inflation rose by 0.1 pp to 0.4% in November. The growth was driven by oil prices, which started falling sharply in 2014 Q4, and this effect is now gradually unwinding. Average inflation is expected to be 0.3% in 2015 as a whole and accelerate to 1.4% in 2016.



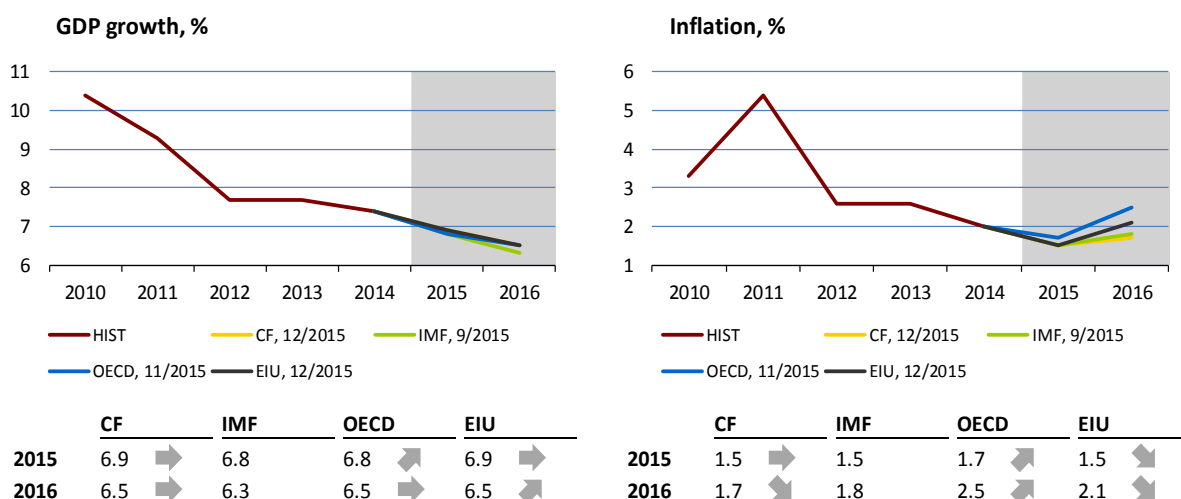
II.4 Japan

The Japanese economy avoided recession in Q3, with annualised quarterly GDP growth reaching 1%. This represented a significant shift compared to the initial November estimate (-0.8%). In particular, the figures on inventories, whose decline was smaller than originally expected, were revised. Capital expenditure also recorded an increase in Q3 (of 0.6%) instead of the originally announced decrease (-1.3%). The PMI leading indicator reached a 20-month high in November, indicating continued expansion in the industrial sector. However, consumer demand remains subdued despite record-low unemployment (3.1%). It is demand that will be targeted by Prime Minister Shinzo Abe's new stimulus plan. The new measures are aimed at supporting agricultural regions jeopardised by the TPP free trade agreement and at boosting demand among people with low incomes by making cash hand-outs. Annual headline inflation rose to 0.3% in October for the first time since March 2015, while core inflation excluding food prices was flat at -0.1% for the fourth consecutive month. According to the December CF, no increase in inflationary pressures can be expected next year either. The CF inflation outlook for 2016 even decreased compared to last month. The GDP growth outlook for 2016 was revised in the same way, while the inflation and economic growth outlooks for 2015 remained unchanged.



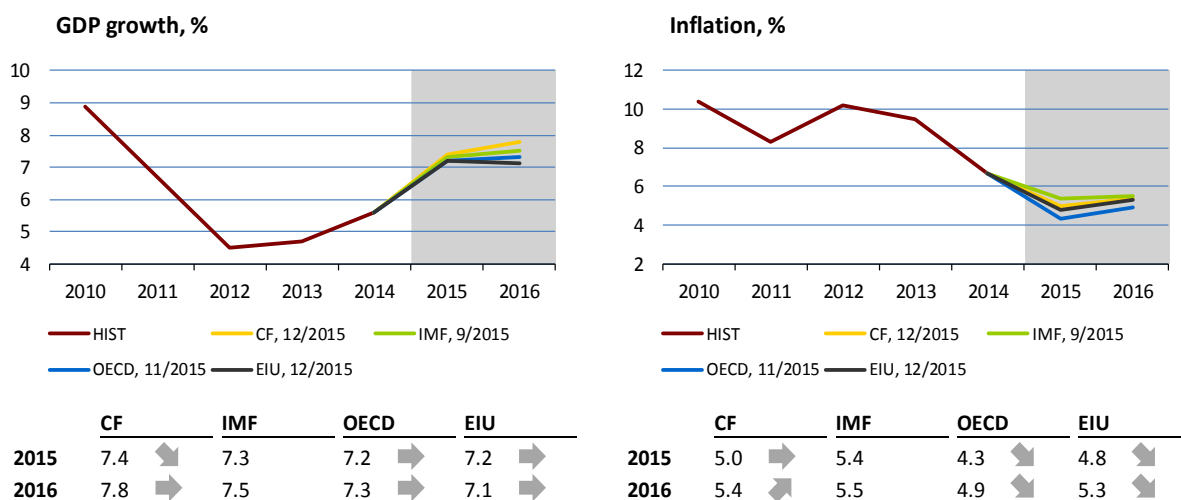
III.1 China

The short-term indicators recorded mixed trends in October and November. While industrial output growth slowed by 0.1 pp to 5.6% and the PMI for new orders in manufacturing fell below 50 points, the overall PMI in manufacturing increased slightly (to 48.6 points). New house prices started rising again year on year in October after 13 consecutive months of decline. As expected, the IMF added the renminbi to the SDR basket with effect from 1 October 2016. The renminbi will have the third-largest share in the basket (10.92%). The dollar remains in first place (41.73%), followed by the euro, whose share will be reduced significantly to just below 31% (for an analysis of the extent to which the renminbi complies with the conditions for inclusion in the SDR basket, see Focus in the August issue of GEO). The new GDP growth outlooks (CF, EIU, OECD) remained mostly unchanged. GDP growth will not exceed 6.9% this year and is expected to slow further to 6.5% next year. Inflation will accelerate slightly from the 1.5%–1.7% expected for this year to 1.7%–2.5% next year.



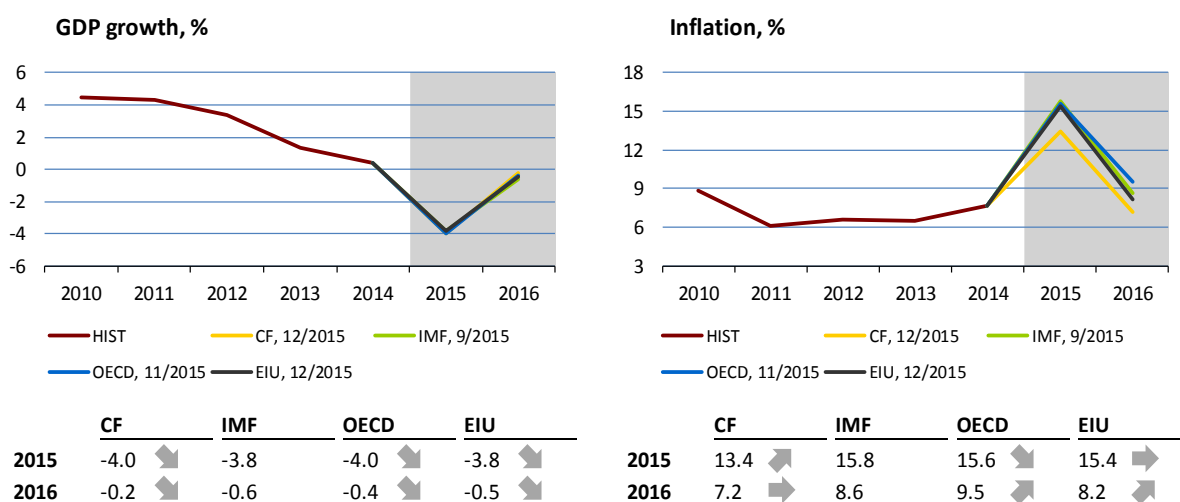
III.2 India

India is the world's fastest growing economy. Its growth is due mostly to domestic demand, which will remain the driver in the period ahead. Consumer confidence is also rising on growing optimism about the country's economic outlook. After a fall in September, industrial output rose again in October at a much faster-than-expected rate of 9.8%, thanks mainly to mining and electricity generation. However, the PMI in manufacturing fell for the fourth consecutive month. Its November value of 50.3 points is close to the contraction band. The EIU left its GDP growth outlook unchanged. CF lowered its outlook by 0.1 pp. As expected, inflation was 5.4% in November, still affected by rising food prices. India's central bank set an inflation target for March 2017, when inflation should be under 5%. The EIU cut its inflation outlooks for the two periods by 0.8 and 0.6 pp respectively, while CF raised its forecast for the next period by 0.1 pp.



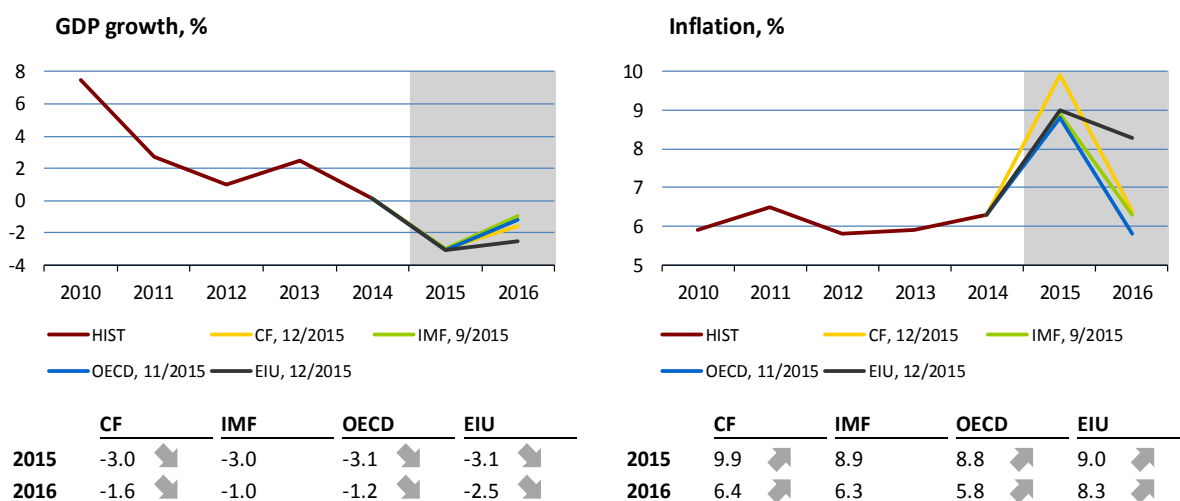
III.3 Russia

The Russian GDP contraction slowed in Q3 compared to the previous quarter, to “only” 4.1%. However, two pieces of bad news for the country’s future economic development appeared right at the start of December. Russia is imposing a range of sanctions on Turkey in response to the shooting down of a Russian warplane by the Turkish military. The sanctions include an embargo on certain foods (Turkey is an important trading partner for Russia) and restrictions on tourism and air transport. Russia is also considering the suspension of Russian-Turkish investment projects. The other piece of bad news was a drop in the Brent crude oil price below USD 40 a barrel. The rouble weakened in response to this fall and only slightly reversed the loss after the CBR left its key rate unchanged. The new outlooks for Russian economic growth for both this year and the next were lowered further. CF, the EIU and the OECD predict a GDP contraction of 3.8%–4.0% for this year. Next year, GDP should fall only slightly. The new inflation forecasts range between 13.4% and 15.4% for 2015 and between 7.2% and 8.2% for 2016.



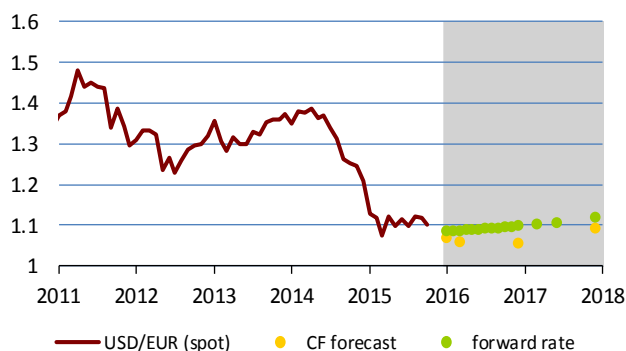
III.4 Brazil

Brazil is in its worst recession in decades. The Brazilian economy contracted by 4.5% in Q3. Due to the continuing economic and political crisis, Moody’s is reviewing the country’s rating and may downgrade it to speculative. Contrary to expectations, industrial output decreased in October. Unemployment rose to 7.9% in October after two months of stagnation. The PMI in manufacturing fell again in November, remaining in the contraction band for the tenth consecutive month. The EIU revised its GDP growth outlooks downwards by 0.3 pp for this year and by a considerably larger 1.8 pp for the next. CF also lowered its outlooks by 0.2 pp and 0.6 pp respectively. Inflation went up by 0.6 pp compared to the previous month to 10.5% in November, with fuel, food and housing prices recording the fastest growth. Despite the rise in inflation, the central bank left its main policy rate unchanged again so as not to further harm the already weak economy. CF and the EIU both increased their inflation outlooks for 2015 by 0.2 pp. CF raised its prediction for 2016 by 0.3 pp and the EIU increased its by 1.7 pp.



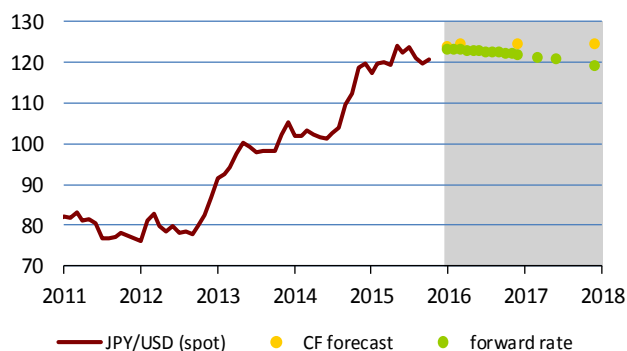
IV. Outlook of exchange rates vis-à-vis the US dollar

The euro



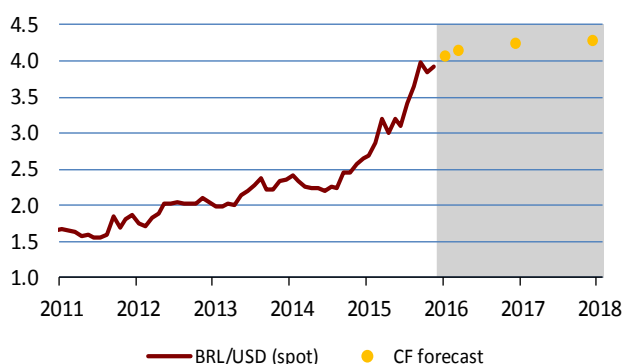
	7/12/15	01/16	03/16	12/16	12/17
spot rate	1.085				
CF forecast		1.067	1.059	1.053	1.090
forward rate		1.085	1.086	1.097	1.118

The Japanese yen



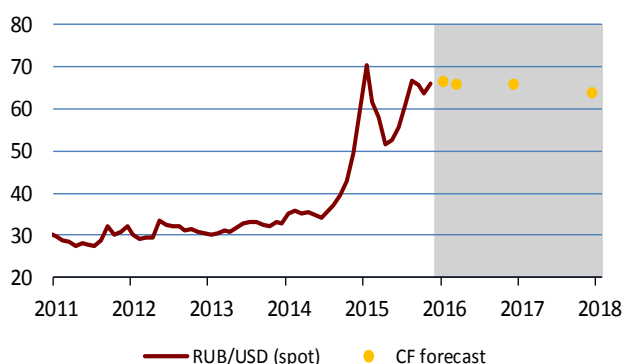
	7/12/15	01/16	03/16	12/16	12/17
spot rate	123.3				
CF forecast		123.7	124.5	124.4	124.6
forward rate		123.2	123.1	121.8	119.2

The Brazilian real



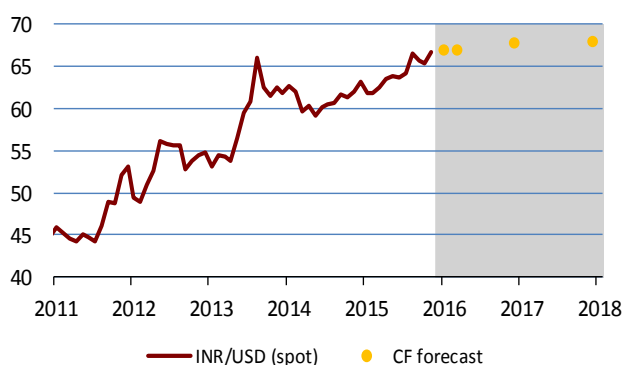
	7/12/15	01/16	03/16	12/16	12/17
spot rate	3.773				
CF forecast		4.067	4.132	4.241	4.271

The Russian rouble



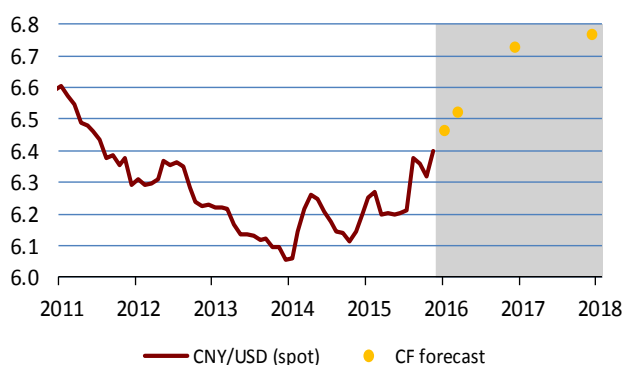
	7/12/15	01/16	03/16	12/16	12/17
spot rate	68.92				
CF forecast		66.26	65.69	65.83	63.58

The Indian rupee



	7/12/15	01/16	03/16	12/16	12/17
spot rate	66.73				
CF forecast		66.85	66.89	67.79	67.94

The Chinese renminbi



	7/12/15	01/16	03/16	12/16	12/17
spot rate	6.408				
CF forecast		6.462	6.520	6.724	6.767

Exchange rates as of last day of month. Forward rate does not represent outlook; it is based on covered interest parity, i.e. currency of country with higher interest rate is depreciating. Forward rate represents current (as of cut-off date) possibility of hedging future exchange rate.

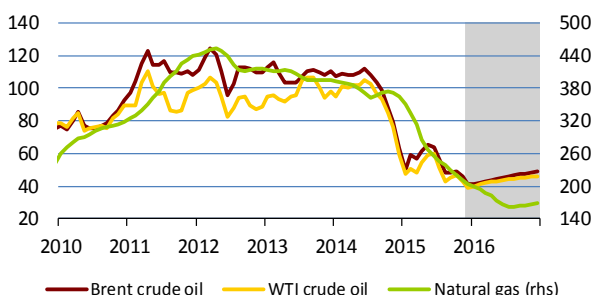
V.1 Oil and natural gas

The Brent crude oil price dropped by more than 8% in the second week of November and, with just a few exceptions, stayed below USD 45 a barrel (bbl) for the rest of the month as concerns about excess supply started to prevail on the market again following news of continued growth in oil stocks and amid expectations of further growth in stocks of oil products. The downward pressure on oil prices (and other commodities) was also fostered by strong appreciation of the US dollar as from mid-October. A further price drop (as far as USD 40/bbl) was recorded in the second week of December after the OPEC meeting. OPEC showed no willingness to support oil prices and, for the first time in decades, set no production quotas.

The market oil price forecast based on the 7 December futures curve shifted downwards again and continues to predict only a gradual rise in the Brent oil price to around USD 49/bbl and USD 54/bbl at the end of 2016 and 2017 respectively. The December EIA forecast of an average price of USD 56/bbl for 2016 is markedly higher (by more than USD 10/bbl), as is the November CF forecast. There are risks to the forecast on both sides. The oil price might see a further marked fall if the massive growth in stocks of oil and oil products continues and their volume nears the limits of the available storage capacity. However, most estimates agree that the oil market should approach equilibrium at the end of 2016 or in 2017 thanks to a steady but slower rise in demand and a slowdown, or even a temporary drop, in the supply of oil.

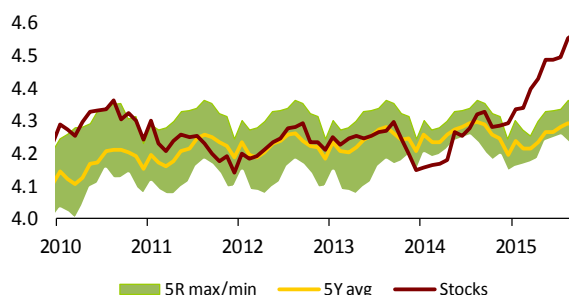
Natural gas prices fell in Europe and especially in the USA in November owing to high stocks and unusually warm weather.

Outlook for prices of oil (USD/barrel) and natural gas (USD / 1000 m³)

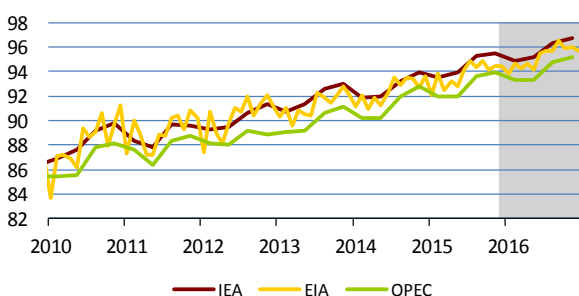


	Brent	WTI	Natural gas
2015	53.83 ↗	48.91 ↗	263.08 ↗
2016	45.33 ↘	43.50 ↘	174.10 ↘

Total stocks of oil and oil products in OECD (bil. barrel)

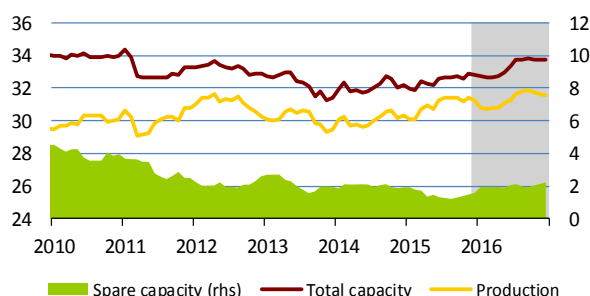


Global consumption of oil and oil products (mil. barrel / day)



	IEA	EIA	OPEC
2015	94.57 ↗	93.82 ↗	92.88 ↗
2016	95.78 ↗	95.22 ↗	

Production, total and spare capacity in OPEC countries (mil. barrel / day)



	Production	Total capacity	Spare capacity
2015	30.98 ↗	32.46 ↗	1.48 ↘
2016	31.29 ↗	33.30 ↗	2.01 ↗

Note: Oil price in USD/barrel, price of Russian natural gas at German border in USD/1,000 m³ (IMF data, smoothed by the HP filter). Future oil prices (grey area) are derived from futures and future gas prices are derived from oil prices using model. Total oil stocks (commercial and strategic) in OECD countries including average, maximum and minimum in past five years in billions of barrels. Global consumption of oil and oil products in millions of barrels a day. Production and extraction capacity of OPEC in million barrels a day (EIA estimate).
 Source: Bloomberg, IEA, EIA, OPEC, CNB calculation

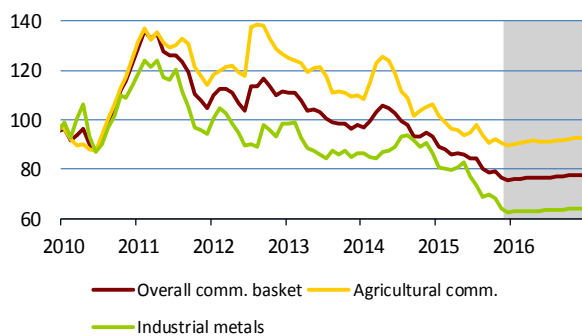
V.2 Other commodities

After a slight rise in October, the average monthly non-energy commodity price index resumed a downward path in November and continued falling at the start of December. The food commodity and the industrial metals sub-indices showed similar patterns. The latter recorded a temporary rise in September. The outlooks for all three indices are moderately rising, although the predicted growth for metals is negligible.

Prices in the industrial metals category fell virtually across the board owing to a still weak outlook for Chinese industry (the PMI in manufacturing rose only slightly in November, from 48.3 to 48.6). Moreover, the outlook for US industry worsened (at 48.6 in November, the PMI was below 50 for the first time in three years) and prices were also under pressure from the strengthening dollar. Aluminium record the smallest drop in price, as Alcoa announced production cuts. In contrast, the iron ore price declined further as large producers continued to raise production, while steel output is falling in China and globally. Copper and nickel prices also fell sharply.

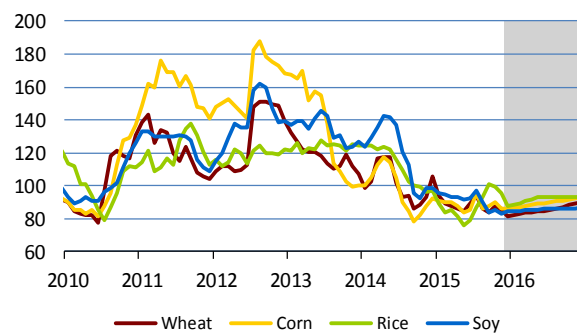
Agricultural commodity prices also came under pressure from the firming dollar, but showed mixed trends. The USDA raised its estimate of global corn stocks in November after this year's harvest (thanks mainly to higher stocks in China and the USA). This, combined with falling fuel prices, pushed corn prices down. Wheat and rice prices also fell. Estimated soy stocks also rose due to record crops in the USA. As a result, the soy price stagnated near an eight-year low. In contrast, the sugar price kept rising, with production in Brazil falling in year-on-year terms due to a higher proportion of sugar cane being used to produce bioethanol. Rubber prices rose from a long-term low for the first time in several months.

Non-energy commodities price indices



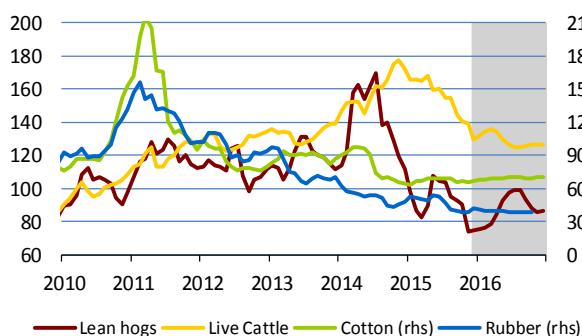
	Overall	Agricultural	Industrial
2015	82.8 ↗	94.7 ↗	73.9 ↗
2016	76.9 ↘	91.6 ↗	63.4 ↘

Food commodities



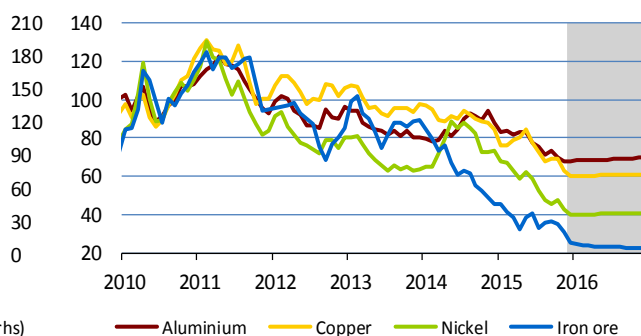
	Wheat	Corn	Rice	Soy
2015	87.3 ↗	88.1 ↗	88.2 ↗	90.3 ↗
2016	85.6 ↘	89.6 ↘	92.0 ↗	85.6 ↗

Meat, non-food agricultural commodities



	Lean hogs	Live Cattle	Cotton	Rubber
2015	91.7 ↗	154.1 ↗	67.5 ↗	46.6 ↗
2016	87.9 ↗	129.1 ↘	69.5 ↗	

Basic metals and iron ore



	Aluminium	Copper	Nickel	Iron ore
2015	76.6 ↘	72.9 ↘	54.4 ↘	36.0 ↘
2016	68.9 ↘	60.6 ↘	40.4 ↘	23.2 ↘

Note: Structure of non-energy commodity price indices corresponds to composition of The Economist commodity indices. All prices are given as indices, 2010 = 100 (charts) and percentage changes (tables).

Source: Bloomberg, CNB calculations.

The role of China in the slowdown in international trade¹

China's economic importance has risen sharply over the last 20 years. Changes in its economy are therefore increasingly affecting the global economy. This article investigates the causes of the sizeable fall in imports into China observed for almost a year now and analyses its impacts on international trade. The analysis shows that the fall can be explained not only by global commodity market developments and the global slowdown, but also by the transformation of the Chinese economy, especially growth in the share of higher-value-added products and a related decline in the import intensity of exports. A slowdown in the residential property sector is also playing an important role. International trade can be expected to pick up again, but the growth will be much slower than before the crisis.

1 China's trade integration

International trade is a major channel of transmission of external shocks. The volume of exports is determined mostly by external demand, while the volume of imports is governed by domestic demand, i.e. consumption demand of households, investment demand of firms and government demand. In addition, both exports and imports are affected by domestic and foreign inflation, the exchange rate, the choice of invoicing currency and transaction currency, and even by the country's degree of financial integration.² A drop in external demand or a fall in production for export has a negative effect on GDP growth and inflation in the domestic economy. The more open an economy is, the more exposed it is to external shocks. This also applies to goods re-exports (imports of components for production of a final product and the subsequent export of that product), where an external shock to imports has a knock-on effect on exports.

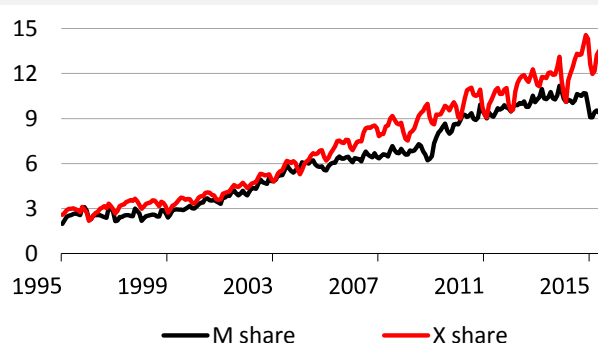


Chart 1: China's share in global exports and imports, in %

Note: X share is China's share in global exports and M share is China's share in global imports of goods at current prices, CIF, three-month moving average. Most recent observation: September 2015.

Source: IMF-DOTS (DataStream), author's calculation

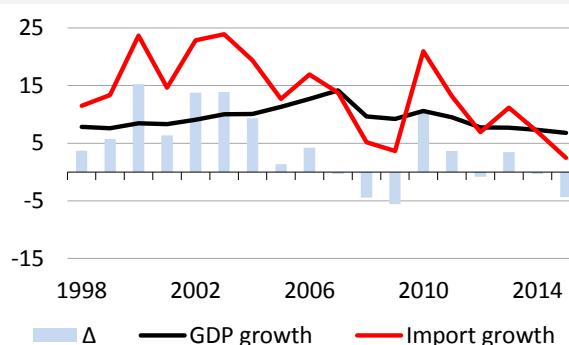


Chart 2: Growth in Chinese imports and GDP, y-o-y in %

Note: GDP growth is the annual growth rate of Chinese GDP in %; import growth is the annual growth rate of total imports into China in % at constant prices. The bar chart (Δ) depicts the difference between import growth and GDP growth in pp. Annual data; 2015 data are based on the October IMF-WEO estimate.

Source: Oct 2015 IMF-WEO, author's calculation

China's importance in international trade has risen sharply over the last 20 years. In the mid-1990s, the country accounted for just 2.5% of global imports of goods and commodities. Its share of exports was only slightly higher (see Chart 1). In 2014, China's imports exceeded 10% of global imports, four times the level of 20 years earlier. Its share of exports increased even more rapidly in the same period (to almost 13%). In absolute terms, China's total international trade turnover reached USD 4.3 trillion,³ making it number one in the world in this respect.⁴

¹ Author: Oxana Babecká Kucharčuková (Oxana.Babecka-Kucharcukova@cnb.cz). The views expressed in this article are those of the author and do not necessarily reflect the official position of the Czech National Bank.

² For the role of the Chinese currency in international transactions, see Benecká (2013). Komárek (2010) examines the overvaluation/undervaluation ("misalignment") of the renminbi vis-à-vis the three global reserve currencies: USD, JPY and EUR. The international integration of the Chinese stock market is discussed by Babecký et al. (2011).

³ HKTDC Research (2015).

⁴ For example, China's share in global exports is 56% for computers and 65% for plastic toys. Moreover, it accounts for at least 10% of global exports in one-third of all the categories monitored in the UN Comtrade

However, Chinese export growth has been slowing for several years, partly because of the global slowdown, which is weakening external demand for Chinese goods.⁵ Exports even started falling in 2015. However, the biggest change can be seen for Chinese imports. In the first ten months of this year, imports of goods into China in nominal USD terms dropped by 15.5% year on year. Import growth had been declining irregularly since March 2014, but since November 2014 imports have been falling continuously. The downward trend is accelerating, and this, in turn, is affecting the macroeconomic situation in China's main trading partner countries, not only via falling real exports growth, but also via prices.

2 Imports and structural changes in the Chinese economy

Energy commodities and industrial metals are major Chinese import items. Consumption of metals and energy in China tripled in 2000–2014.⁶ The decrease in nominal imports thus largely reflects (but simultaneously influences – see below) price movements on commodity markets, especially the decline in global oil prices. Crude oil was the largest Chinese import item in terms of value in 2014. China's demand is meanwhile monitored as a factor influencing global oil prices. Given that consumption in China accounts for 11% of global oil consumption, its share in global demand is far from dominant. Nevertheless, consumption growth in China still accounts for the largest share of global oil consumption growth, and this amplifies its influence on oil prices. Owing to growth in strategic reserves, which is accelerating at a time of falling oil prices, China is additionally contributing to reducing the oil market disequilibrium. The industrial metals and coal market, however, is much more sensitive to developments in the Chinese economy. China's consumption of these commodities currently accounts for 50% of global consumption,⁷ and this has a sizeable effect on their prices. Not surprisingly, then, the drop in Chinese demand for iron ore imports has led to a marked decline in the price of iron ore on world markets.

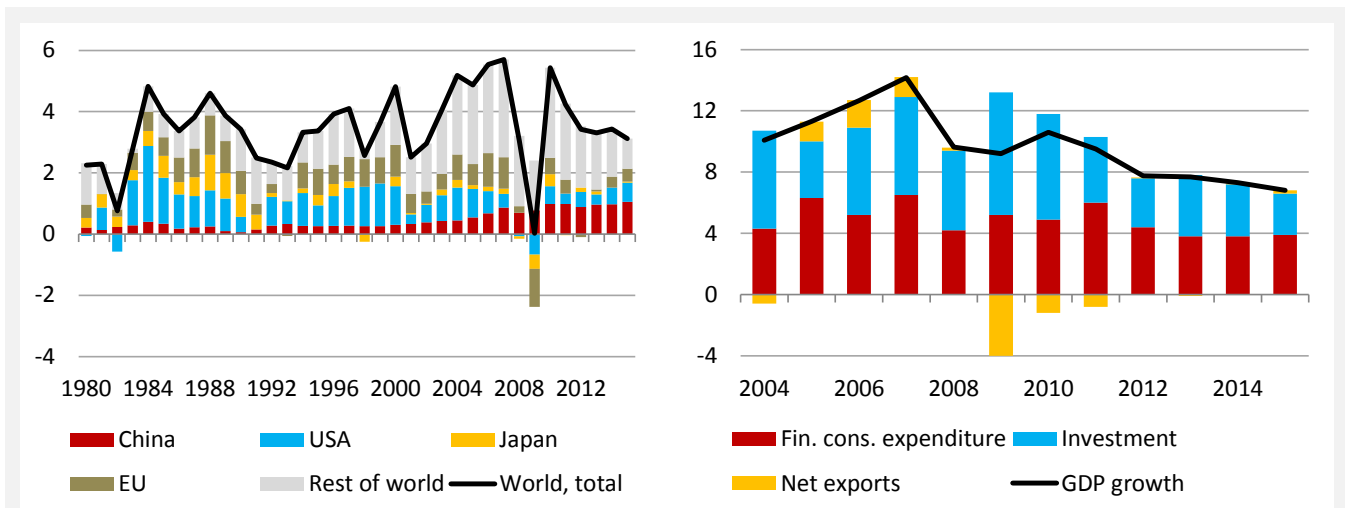


Chart 3: China's contribution to global GDP growth, year-on-year change in %, contributions in pp

Source: IMF (2015)

Chart 4: Decomposition of China's GDP growth, year-on-year change in %, contributions in pp

Source: IMF (2015)

Growth in Chinese imports has also slowed sharply in real terms, but remains positive. According to an estimate in the IMF's October World Economic Outlook (WEO) it has been fluctuating around 2% this year. For comparison, import growth has repeatedly exceeded 20% in the past, most recently in 2010. A comparison of annual GDP growth and import growth reveals that their dynamics are completely different (a correlation of just 0.34). This implies that the elasticity of imports to GDP is changing over time. It is also interesting that since 1998 there have been only two periods in which import growth was significantly lower than overall economic growth, namely 2008–2009, when the escalating global financial and economic crisis had the biggest impact on international trade, and again this year (see Chart 2). This year's marked slowdown in imports compared to overall economic growth points not only to an effect of lower domestic

database (source: IMF – People's Republic of China: Staff Report for the 2015 Article IV Consultation, July 2015.).

⁵ Although the global slowdown is also due partly to the slowdown in China.

⁶ European Commission (2015).

⁷ European Commission (2015).

demand stemming from the global slowdown,⁸ but also to the structural changes going on in the Chinese economy, with an emphasis on a higher share of services.⁹

The residential property sector is a key factor for economic growth and trade in China. Over the last ten years it has been the driver of the rapid growth of the Chinese economy¹⁰ and has been supported by a sharp rise in investment (from 4% of GDP in 1997 to 15% in 2014). Bank loans in the property sector currently account for 20% of total loans provided. Residential investment growth peaked in 2013 at 10.4% of GDP (for comparison, residential investment in Spain peaked at 12.5% of GDP in 2006). The property sector is closely linked to many other sectors. When it started slowing in 2014 (owing to the mismatch between excessive supply and limited demand), this had a negative impact on Chinese imports of goods and commodities for use in construction (such as the above-mentioned decline in iron ore imports). In cases like this, foreign commodity exporters face a double shock (a drop in demand and a drop in prices). However, such a shock is positive for commodity-importing countries.

Although China's current economic growth rate is less than half that recorded in the final pre-crisis year, it remains the biggest contributor to global growth (see Chart 3). Since 2010, economic growth in China has been on a downward trend and the GDP structure has undergone visible changes. Among other things, the share of services in total value added has risen. The saving rate has fallen, while investment growth remains high despite having slowed. The contributions of investment and final consumption to GDP growth have been broadly comparable in recent years (see Chart 4). A slight decrease in the share of investment (especially in the property sector) in total GDP growth is expected this year. Net exports were an important source of China's economic growth in 2005–2007, but their contribution was negative in 2009–2011 and has been insignificant since then. Although net exports at constant prices can be expected to have a rather larger impact on GDP growth this year, their positive contribution is mostly a result of import growth deteriorating faster than export growth. Nominal imports have been falling much faster as a result of almost a year of declining goods imports, while imports of services (mainly travel) are developing favourably. However, the share of services in total foreign trade remains low compared with advanced countries, despite having risen significantly.

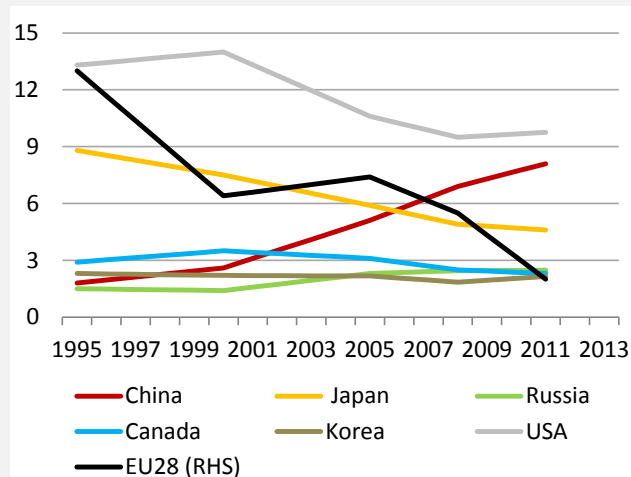


Chart 5: Share of value added in selected countries in global value added, in %

Source: IMF (2015)

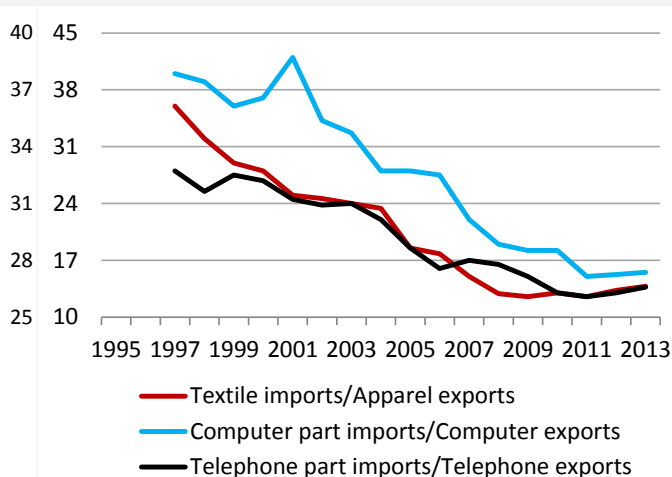


Chart 6: Import intensity of exports for selected goods categories, in %

Source: IMF (2015)

The individual components of GDP have different import intensities. It can be assumed, for example, that exports and investment are more import-intensive than household and government consumption. The elasticity between imports and GDP is changing as a result of movements in the shares of the individual GDP components (for example, a slowdown in investment and export growth relative to household

⁸ Domestic demand has been slowing gradually since 2010. According to an EIU estimate, domestic demand growth fell to 7.2% in 2014 and will bottom out at 4.2% this year. It is expected to accelerate slightly in the years ahead.

⁹ The share of services in value added (excluding construction) has almost doubled over the last 40 years and overtook that of manufacturing in 2013. However, the Chinese services sector remains small relative to the OECD average (OECD, 2015).

¹⁰ Chivakul et al. (2015).

consumption growth). Import-intensive GDP components fall sharply in periods of recession or crisis, leading to a much sharper drop in international trade than in GDP itself.¹¹

Over the last ten years, Chinese exports have changed not only in terms of quantity, but also in terms of quality – towards higher-value-added and less labour-intensive products. Value added in China has risen sharply. Its share in global value added is now close to 10% (see Chart 5). The higher quality and growth in value added has enabled China to produce a greater proportion of its output itself, which has lowered the import intensity of exports. Processed exports with a high share of imports have gone down from 56% in 2005 to around 35% today. Although China is worse off in terms of price competitiveness, from the point of view of international trade this has given Asian and African countries greater room to succeed on the market thanks to lower labour costs, albeit with lower-quality products.

3 Impact on trading partner countries

The five largest exporters to China (South Korea, Japan, the USA, Germany and Australia) had shares of between 5% and 10% of total Chinese imports in 2014 (see Chart 7a). The decline in nominal imports in China deepened in 2015. For many countries, the fall in their exports to China was larger than the fall in their total exports (see Chart 7b). In January–September 2015, imports to China from the USA recorded the smallest decline (7%) while those from Australia saw the largest decrease (26%) as a result of a fall in iron ore imports. The slowdown in Chinese imports is expected to continue to affect commodity exporters most of all. Germany is China's largest EU trading partner. From the perspective of international trade, China is Germany's fourth largest trading partner. Exports to China account for 6.5% of total German exports. Chinese imports from Germany fell by 15% in January–September (mainly because of lower car imports). The impact on the German economy should therefore also be sizeable.

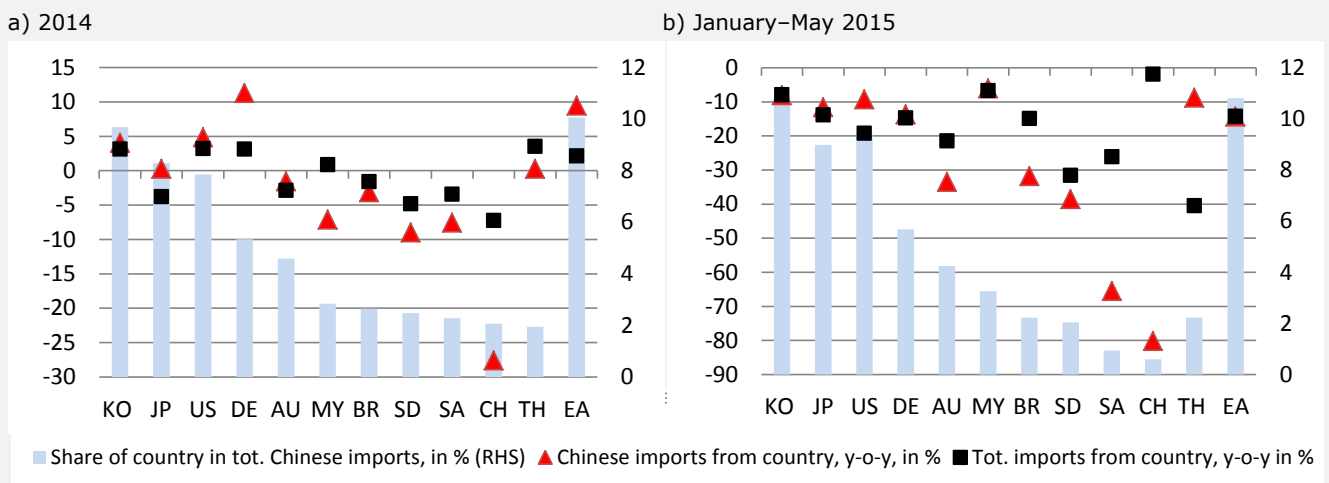


Chart 7: Dynamics and geographical structure of Chinese imports by main trading partner country

Note: Where the red points are below the black ones, the fall in the country's exports to China is larger than the fall in its total exports. KO – Korea, JP – Japan, US – USA, DE – Germany, AU – Australia, MY – Malaysia, BR – Brazil, SD – Saudi Arabia, SA – South Africa, CH – Switzerland, TH – Thailand, EA – euro area.

Source: IMF-DOTS, author's calculation

To sum up, Chinese imports have fallen sharply in nominal terms and imports at constant prices have slowed considerably in 2015. China's trade dynamics have been affected not only by the global slowdown, but also by structural changes in its economy. The fall in Chinese demand for commodities has been reflected not only in a decline in the volumes of commodities imported; in some cases it has also contributed to a decline in their prices. Commodity exporters are being – and will continue to be – hit much harder by the negative shock of the Chinese trade deterioration than commodity importers (e.g. most EU countries). However, the direct impact on the EU economy should be less significant.

Assuming continued structural changes supporting economic growth and convergence of China towards advanced economies, Chinese foreign trade can be expected to accelerate slightly in the long run, albeit to significantly lower levels than before the crisis. According to the EIU outlook, for example, export growth will be in the range of 3.9%–4.9% and import growth 3.3%–4.5% in 2017–2020. At the same time, the current account surplus will narrow substantially as a result of a marked widening of the services deficit and a reduction in the goods surplus. The EIU continues to expect the Chinese economy to slow. GDP growth will fall to 4.7% in 2020 from the 6.9% expected this year. Conversely, the October IMF outlook predicts stabilisation of growth at 6.3%. If this scenario materialises, higher growth rates of Chinese foreign trade

¹¹ Bussière et al. (2013). The authors use input-output tables for 18 OECD countries to analyse the elasticity of international trade in terms of demand composition.

can also be expected. However, the greater uncertainty associated with long-term outlooks compared to short-term ones should be borne in mind.

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A1. Change in GDP predictions for 2015

	CF		IMF		OECD		CB / EIU	
EA	0	2015/12	0	2015/9	-0.1	2015/11	+0.1	2015/12
		2015/11		2015/7		2015/9		2015/9
US	+0.1	2015/12	+0.1	2015/9	0	2015/11	+0.2	2015/9
		2015/11		2015/7		2015/9		2015/6
DE	0	2015/12	-0.1	2015/9	-0.1	2015/11	0	2015/12
		2015/11		2015/7		2015/9		2015/6
JP	0	2015/12	-0.2	2015/9	0	2015/11	-0.5	2015/10
		2015/11		2015/7		2015/9		2015/7
BR	-0.2	2015/12	-1.5	2015/9	-0.3	2015/11	-0.3	2015/12
		2015/11		2015/7		2015/9		2015/11
RU	-0.1	2015/12	-0.4	2015/9	-0.9	2015/11	-0.2	2015/12
		2015/11		2015/7		2015/6		2015/11
IN	-0.1	2015/12	-0.2	2015/9	0	2015/11	0	2015/12
		2015/11		2015/7		2015/9		2015/11
CN	0	2015/12	0	2015/9	+0.1	2015/11	0	2015/12
		2015/11		2015/7		2015/9		2015/11

A2. Change in inflation predictions for 2015

	CF		IMF		OECD		CB/EIU	
EA	0	2015/12	+0.1	2015/9	-0.5	2015/11	0	2015/12
		2015/11		2015/4		2015/6		2015/9
US	+0.1	2015/12	-0.0	2015/9	-0.0	2015/11	-0.3	2015/9
		2015/11		2015/4		2015/6		2015/6
DE	0	2015/12	-0.0	2015/9	-1.1	2015/11	-0.3	2015/12
		2015/11		2015/4		2015/6		2015/6
JP	0	2015/12	-0.3	2015/9	-1.0	2015/11	-0.6	2015/10
		2015/11		2015/4		2015/6		2015/7
BR	+0.2	2015/12	+1.1	2015/9	+0.5	2015/11	+0.2	2015/12
		2015/11		2015/4		2015/6		2015/11
RU	+0.3	2015/12	-2.1	2015/9	-0.7	2015/11	0	2015/12
		2015/11		2015/4		2015/6		2015/11
IN	0	2015/12	-0.7	2015/9	-1.4	2015/11	-0.8	2015/12
		2015/11		2015/4		2015/6		2015/11
CN	0	2015/12	+0.3	2015/9	+0.1	2015/11	-0.1	2015/12
		2015/11		2015/4		2015/6		2015/11

A3. List of abbreviations

ABS	asset-backed securities	GDP	gross domestic product
bbl	barrel	HICP	harmonised index of consumer prices
BoJ	Bank of Japan	CHF	Swiss franc
BR	Brazil	ICE	Intercontinental Exchange
BRIC	countries of Brazil, Russia, India and China	IFO	Institute for Economic Research
BRL	Brazilian real	IFO-BE	IFO Business Expectations
CB-CCI	Conference Board Consumer Confidence Index	IMF	International Monetary Fund
CB-LEII	Conference Board Leading Economic Indicator Index	IN	India
CBOT	Chicago Board of Trade	INR	Indian rupee
CBR	Central Bank of Russia	IRS	Interest Rate swap
CF	Consensus Forecasts	JP	Japan
CN	China	JPY	Japanese yen
CNB	Czech National Bank	LI	leading indicators
CNY	Chinese renminbi	LIBOR	London Interbank Offered Rate
DBB	Deutsche Bundesbank	MER	Ministry of Economic Development (of Russia)
DE	Germany	MMBtu	million of British Thermal Units
EA	euro area	OECD	Organisation for Economic Co-operation and Development
EBRD	European Bank for Reconstruction and Development	OECD-CLI	OECD Composite Leading Indicator
EC	European Commission	PMI	Purchasing Managers' Index
ECB	European Central Bank	PPI	producer price index
EC-CCI	European Commission Consumer Confidence Indicator	RU	Russia
EC-ICI	European Commission Industrial Confidence Indicator	RUB	Russian rouble
EIA	Energy Information Administration	TLTRO	targeted longer-term refinancing operations
EIU	Economist Intelligence Unit	UoM	University of Michigan
EU	European Union	UoM-CSI	University of Michigan Consumer Sentiment Index
EUR	euro	US	United States
EURIBOR	Euro Interbank Offered Rate	USD	US dollar
Fed	Federal Reserve System (the US central bank)	USDA	United States Department of Agriculture
FOMC	Federal Open Market Committee	WEO	World Economic Outlook
FRA	forward rate agreement	WTI	West Texas Intermediate (crude oil used as a benchmark in oil pricing)
GBP	pound sterling		

A4. List of thematic articles published in the GEO

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