Euler Hermes Economic Research

Weekly Export Risk Outlook

3 November 2016

In the Headlines

FIGURE OF THE WEEK

+0.3%

Q3 GDP growth for the Eurozone (q/q, first estimate)

U.S.: Consumption still tepid, but Fed hike likely in December

Q3 GDP grew at an annualized rate of +2.9% q/q, the fastest in two years. Investment grew for the first time in four quarters, gaining +3.2%. Net exports contributed +0.8pp, the most in four years. There were two weak spots in the report, however. Residential investment fell -6.3%, the second straight loss, and personal consumption (PCE) grew only +2.1%, after +4.3% in Q2. The real disposable personal income (DPI) needed to fuel PCE rose only +0.1% m/m in September to an anemic +2.1% y/y rate. Decelerating DPI and falling consumer expectations suggest weak consumption going forward. Therefore Euler Hermes will reduce its 2016 GDP forecast from +1.7% to +1.5% and its 2017 forecast from +2.2% to +2.1%. Separately, the ISM manufacturing index crept up from 51.5 to 51.9, just into expansionary territory, but the critical new orders component fell -3.0 to 52.1. The Fed left interest rates unchanged, but the accompanying statement was more hawkish, making three separate references to higher inflation and saying that the case for a hike "continued to strengthen." We expect the Fed will hike in December unless financial markets fall significantly as a result of election uncertainty.

France: Cold summer

Initial estimates put real GDP growth at +0.2% q/q in Q3, making it the second consecutive quarter of subpar growth. As a result, EH has lowered its full-year growth forecast for 2016 from +1.5% to +1.3%. The main driver of the Q3 weakness was subdued demand. Private consumption stalled for the second consecutive quarter. Consumer confidence suffered from hurdles during the summer (effects of Nice attack on tourism and unemployment in August). Moreover, a noisy environment (Brexit, lackluster demand, forthcoming elections) prevented corporates to invest more (-0.2% q/q) despite evident investment lags. The only positive surprise was household investment (+0.8% q/q) explained by low building materials' prices, low interest rates and strong financing capacity of households (3.5% of GDP per year). Q4 should post stronger growth since unemployment decreased markedly in September and consumer confidence recovered to post-2008 crisis highs in October. For 2017, EH forecasts growth of both real GDP (+1.4%) and nominal GDP (+2.3%, after +2% in 2016) to pick up.

UK: Resilience of post-Brexit GDP only temporary

Q3 GDP growth slowed down less than expected, to +0.5% q/q from +0.7% in Q2. However, production in the construction sector continued to contract (-0.1pp contribution to GDP growth, the most negative since Q3 2012) as demand is weaker and uncertainty higher. Despite the GBP depreciation, production in the manufacturing sector contracted as well (-0.05pp). There are already signs of rising upside pressure on output prices as a result of the sterling depreciation. Value added in the services sector was the only positive contributor to Q3 GDP growth (+0.64pp) mainly driven by growth in the transport, storage and communication industries, notably by the motion picture, video and TV program production, sound recording and music publishing activities, and computer programming industries. Going forward, economic prospects should deteriorate as the EU exit procedure activation is nearing (by March 2017). EH expects GDP growth to slow down to +0.7% in 2017, on the back of falling corporate investment and lower consumer spending as inflation should reach +2.5% on average in 2017 which will also limit the BoE's leeway to lower interest rates further.

China: On steroids?

Industrial profits increased by +8.4% y/y in the first nine months of 2016. "New growth model" related industries (automotive, chemicals and electronics, e.g.) continue to post strong growth, while basic materials producers are still struggling. From a corporate perspective, state companies underperformed (+2.6% y/y YTD) while private sector companies have shown resilience. Going forward, the latest business sentiment surveys are encouraging. The official manufacturing PMI increased to 51.2 in October (from 50.4 in September) driven by a rise in production and new orders as well as improved SME performance. The official non-manufacturing PMI improved as well, to 54.0 in October from 53.7 in September. The economy is still benefitting from the authorities' support and GDP growth is set to remain in the government's comfort zone this year (between +6.5% and +7%). In the medium-term, economic growth is forecast to decelerate slightly (+6.4% in 2017) as the authorities lower credit supply growth to reduce financial risks.

Countries in Focus

Americas

Canada: Strong Q3 GDP, but likely cooler the rest of the year

GDP rose for the third consecutive month, gaining +0.2% m/m in August. The goods sector accounted for all the gains, growing +0.7% m/m, while services were flat. The energy sector notched its third consecutive gain, climbing +1.2% m/m, bringing the y/y rate to +0.6%, the first positive read in four months. Construction gained +0.4% m/m, the first increase in five months. The overall strong performance over the past three months implies that even if growth is flat in September, Q3 annualized growth would be a robust +3.2% q/q. But some off that increase is simply a rebound from Q2's -1.6%. And some August details suggest gains may be unsustainable, such as a +14% m/m rise in potash production and an energy sector which has gained +14.7% annualized over the past three months. Therefore growth is likely to cool the rest of the year, which leads EH to revise its 2016 forecast down -0.1pp to +1.2% while the 2017 forecast falls -0.2pp to +2.0%.

Europe

Eurozone: It seems tough to accelerate despite better policy-mix

Preliminary estimates indicate that Q3 real GDP grew by +0.3% q/q, in line with our expectations, unchanged from Q2 and close to the average quarterly growth since Q2 2013 (+0.4% q/q) when the region returned to positive growth. The improved policy-mix has failed to boost growth as yet. The ECB's QE program is certainly Europe's biggest safety belt and redistributor, but the ambitious program struggles to meet targets. Meanwhile it is planned to double the size of the Juncker Investment Plan to EUR630bn by 2022, however, only EUR116bn have been disbursed to date, concentrated in four EU countries (UK, Italy, France, Spain). The region as a whole should remain resilient but a busy political calendar may cause some turbulences. The Italian referendum on 4 December and upcoming elections in the Netherlands (March 2017), France (April) and Germany (September) could be a drag on firms' willingness to invest more. Overall, EH expects GDP to grow by +1.6% in both 2016 and 2017.

Africa & Middle East

Jordan: Growth is slowing

Recently published data by the Department of Statistics put Q2 2016 real GDP growth at +1.9% y/y, following +2.3% y/y in Q1. It was the lowest increase since Q2 2010. Output in mining and quarrying dropped by -26.8% y/y in Q2 (after -8.5% in Q1), while Q2 growth moderated in manufacturing (+0.8% y/y from +0.9% in Q1), trade, hotels and restaurants (+0.8% y/y from +1.6% in Q1), construction (+1.1% y/y from +2.6% in Q1) and utilities which, however, remained the strongest growing sector with +12.5% y/y (albeit down from +16.5% in Q1). Q2 growth picked up in transport and communication (+3.5% y/y from +3% in Q1) and financial and business services (+3.8% y/y from +3.6% in Q1). The agricultural sector expanded by +6.9% y/y in Q2. Euler Hermes expects full-year real GDP growth of +2.2% in 2016, down from +2.4% in 2015 and compared to an average annual +4.5% over the past 10 years. A moderate pickup to +2.5% is forecast in 2017.

Asia Pacific

Taiwan: Strong Q3 GDP – temporary boost or durable trend?

Real GDP growth accelerated to +2.1% y/y in Q3 from +0.7% in Q2, according to preliminary estimates. Exports picked up speed (+3.6% y/y from +0.6%). Investment (+3.2% y/y) recovered from contraction and private consumption (+2.4% y/y) strengthened. Three reasons can explain these improvements. First, the manufacturing industry has seen a marked rise in new orders as a result of the launch of a particular new tech product. Second, the central bank has aggressively embarked on accommodative monetary policy in order to boost domestic activity; it has decreased it key policy interest rate in four steps from 1.875% in August 2015 to 1.375% currently. Third, fiscal support is accelerating, reflected in higher government consumption. Looking ahead, there is still room for caution: the technology industry is subject to cyclical swings and the export outlook is weak owing to low growth in demand from overseas.

What to watch

- November 4 – Canada October employment report
- November 4 – Colombia October CPI
- November 4 – Japan October PMI services
- November 4 – Romania interest rate decision
- November 4 – U.S. October employment report
- November 7 – Indonesia Q3 GDP growth
- November 7 – Germany September factory orders
- November 7 – Spain September industrial production
- November 7 – UK October house prices
- November 8 – Germany September industrial production
- November 8 – Turkey September industrial production
- November 8 – UK September industrial production
- November 8 – U.S. presidential and congressional elections
- November 9 – Brazil October CPI
- November 9 – France October business sentiment
- November 9 – Poland interest rate decision

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