Euler Hermes Economic Research

Weekly Export Risk Outlook

21 December 2016

FIGURE OF THE WEEK

+50bps

Banxico interest rate hike

In the Headlines

France: A Winter's Tale

A recovery is ongoing as growth is accelerating overall as well as in several key sectors. Manufacturing confidence is up from 102 in November to 106 in December (best level since July 2011). Consumer spending accelerated in October and November (see also WERO 30 November 2016) after about six months of stagnation and, as a result, industrial output should start to pick up as well. Services confidence improved likewise from 102 to 106 and retail trade confidence boomed from 104 to 107. Construction was the only laggard, consolidating to 98, from 99 in November, though the latter was up by +3 points. As a result, Euler Hermes maintains its above consensus GDP growth forecasts of +0.5% q/q in Q4 2016 and +1.4% in full-year 2017 (after +1.3% in 2016). Moreover, this slight growth acceleration is expected to boost nominal GDP growth to +2.3% in 2017 (would be first year above +2% since 2011) and turnover growth to +1.4% in 2017 (strongly up from +0.3% in 2016).

Mexico: Increasingly hawkish

Banxico raised its key interest rate by 50bps to 5.75% last week, slightly on the upper side of market expectations. It is the third 50bps increase in a row, each one of them after a shorter period of time, since the central bank began tightening last December. The move is a response to the increase in inflation expectations after the 0.3% m/m release for November which took the y/y rate to 3.3% from 2.5% y/y in June, though it was still below the 4% upper bound of Banxico's inflation target range. But the significant depreciation of the MXN since the outcome of the U.S. elections has further raised the monetary authority's concerns about inflation. Banxico's move is also to accommodate for the Fed's 25bps rate rise last week. Markets expect future hikes by a cumulative 75bps in Mexico in 2017. Euler Hermes forecasts average inflation of 3.4% in 2017, after 2.8% in 2016. Industrial production fell -0.6% y/y in October although not as much as the -1.3% registered in September, and manufacturing production accelerated to +0.9% y/y in October compared to +0.6% y/y in September.

Turkey, Russia and Hungary: Monetary policy on hold

The Monetary Policy Committee (MPC) of **Turkey** kept its policy interest rates unchanged yesterday, after it had hiked rates last month for the first time in almost three years. The MPC indicated that it is currently more concerned about the slowdown in economic activity (see also WERO 15 December 2016) than about inflationary risks in the wake of recent TRY depreciation (-11% since the U.S. elections). The Central Bank of **Russia** (CBR) left its key rate at 10% last week, unchanged since September, even though inflation risks have subsided somewhat (5.8% y/y in November) while economic activity remains weak. The CBR targets 4% inflation at end-2017. The Monetary Council of **Hungary** also maintained its key policy interest rate yesterday, unchanged at 0.9% since May. Inflation has left negative territory and rose to a still modest 1.1% y/y in November. However, GDP growth weakened to +2.2% y/y in Q3 (from +2.8% in Q2). In 2017, Euler Hermes expects monetary tightening in **Turkey** and perhaps in **Hungary** (if inflation and growth pick up) while **Russia** is likely to cut interest rates.

Eurozone: Better Q4 should bring 2016 GDP growth to +1.7%

The Eurozone PMI Composite Output Index remained unchanged at 53.9 in December. While the Services Index dropped slightly (-0.7pt to 53.1), the Manufacturing Index accelerated to a 32-month high (+2pts to 56.1) led by Germany, but also France. Confidence in the manufacturing sector registered its highest quarterly performance of the year thanks to (i) the lower EUR during the quarter (real effective exchange rate down -1%) which gave a boost to new orders, (ii) recovering employment, and (iii) firms' expectations of rising output prices in 2017. However, the EUR depreciation and the rise in oil prices have led to accelerating factory costs which showed the biggest jump in five years. Overall, EH expects an acceleration of GDP growth to +0.4% to +0.5% q/q in Q4 2016 from +0.3% q/q in the previous two quarters. This should bring full-year GDP growth to +1.7% in 2016 after +1.9% in 2015.

Note: WERO is taking a break. The next issue will be 11 January 2017.

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Countries in Focus

Americas

Colombia: 4G infrastructure program

The Fourth Generation Roads Concession (4G) has been established by the government as the backbone of its 2014-2018 National Infrastructure Development Plan. With a total amount of COP47bn, the project is an enthusiastic near ten-year investment program with a number of different public and private partnerships and intends to create an efficient and optimized road grid, reducing both transportation costs and travel time by 20% and 30%, respectively. Underlying consequences would be better benefits from improved trade and business growth. Expected short- to mid-terms effects include the creation of 180,000 jobs and raising GDP growth by +1.5pps during the works. In the longer run, potential average output growth should rise to +5.3% from +4.6%. The unemployment rate is expected to fall by a solid -1pp, contributing to the steady improvement of the job market that has been witnessed for the last couple of years already.

Europe

Poland: Slowdown

Q3 real GDP growth decelerated to +2.5% y/y from +3.1% in Q2, taking the average of the first three quarters to +2.9% y/y. The demand-side breakdown reveals a shift from broad-based, balanced growth in 2015 to growth that is entirely driven by domestic spending and inventories in 2016. The latter added +1.1pps to Q3 growth while fixed investment dropped by a hefty -7.7% y/y (-5% in Q2). Private consumption rose by +3.9% y/y in Q3 (+3.3% in Q2) and public spending by +4.9% y/y (+3.9% in Q2). External trade activity moderated but was still robust, with exports rising by +6.8% y/y (+11.4% in Q2) and imports by +7.8% (+10% in Q2) so that net exports subtracted -0.3pps from Q3 growth (+1pp in Q2). The decline in investment is in part related to a slowdown in the use of EU funds for investment (which is expected to recover in 2017) but in part also to weakened investor confidence. Euler Hermes forecast full-year GDP of +2.8% in 2016 and +2.9% in 2017.

Africa & Middle East

Congo, DR: History repeating

19 December marked the end of President Kabila's second term. The constitution prohibits Kabila to seek an additional mandate, but elections were postponed to 2018 and a political crisis is ongoing in a country which has not yet had a peaceful transfer of power. This puts a downside risk to Congo DR's prospects. Riding on high mineral prices, Congo had averaged growth of +8% in 2010-2015, but growth has since slowed to +4% in 2016 (and is forecast at +3% in 2017) since the government reduced fiscal expenditure from USD8bn in 2015 to USD4.5bn in 2016, in order to cope with shrinking revenues and to keep public debt relatively steady (20% of GDP in 2016). The main economic risk could be related to liquidity issues. The Congolese Franc depreciated by -17% in the last few weeks, and the premium on the black market is widening. Moreover, the import cover of foreign exchange reserves fell to 3.5 months and may decrease further in the wake of the political crisis.

Asia Pacific

Japan: Changing mood

The Bank of Japan (BoJ; the central bank) left its monetary policy unchanged on 20 December (key policy interest rate at -0.1%). The institution revised upwards its assessment of the economy, citing a gradual recovery in both domestic and external demand. The outlook for exports and inflation has improved slightly thanks to a weaker yen which has relieved somewhat the pressure on the BoJ to ease further. The business sentiment edged up. The Tankan survey improved for large manufacturers in Q4 while the flash Manufacturing PMI increased to 51.9 points in December (from 51.3 in November) on the back of higher output and new orders. Looking ahead, risks to the outlook are elevated and stem mainly from external factors, especially a potentially more protectionist U.S. as well as lower economic growth in both China and Europe. Euler Hermes expects real GDP growth to accelerate slightly to +1.1% in 2017 from +1% in 2016.

What to watch

- December 22 – Argentina Q3 GDP
- December 22 – Czech Republic interest rate decision
- December 22 – UK December consumer confidence
- December 23 – France November consumer spending
- December 24 – Poland November retail sales
- December 26 – Turkey December business confidence
- December 26 – Ukraine November industrial production
- December 27 – China November industrial profits
- December 27 – Germany November retail sales
- December 28 – Italy December consumer confidence
- December 28 – UK December house prices
- December 30 – Egypt Q3 GDP
- January 3 – France, Germany December CPI
- January 4 – Eurozone December CPI
- January 5 – Brazil November industrial production
- January 5 – Turkey December CPI
- January 11 – UK November industrial production

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Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com