Euler Hermes Economic Research

Weekly Export Risk Outlook

23 March 2017

In the Headlines

FIGURE OF THE WEEK

-2.3%

Argentina's 2016 GDP contraction

Argentina: The skies clear up

Real GDP grew by +0.5% q/q in Q4 2016 and the figure for the previous quarter was revised upwards from -0.2% q/q to +0.1% q/q. With regard to full-year GDP, exports and public consumption increased by +3.7% and +0.3%, respectively. However, private consumption and investment shrank by -1.4% and -5.5%, respectively. As a result, annual GDP contracted by -2.3% in 2016, compared to the average +3.3% recorded in the previous decade. Euler Hermes predicts full-year real GDP growth to accelerate to +3.2% in 2017, with investment being the main driver of the recovery. Companies, in particular SMEs, will benefit from lower interest rates on loans from the banking sector as inflation is expected to continue its descending path in the near term. However, in contrast to the downward trend initiated early last year, consumer prices remained sticky during H2 2016 and led to a prudent revision of market expectations of future key policy interest rate cuts in the last three months. Headwinds could come from potential second-round effects of changes in regulated prices, such as the reduction of energy subsidies and the increase in tariffs, and from demands for stronger wage raises.

UK: The final countdown to Article 50

On 29 March, PM Theresa May should trigger Article 50 of the Treaty of Lisbon, kicking off Brexit talks which are expected to last around 18 months, until autumn 2018. Then, until spring 2019, the European Council and the UK, EU member states and the European Parliament will have to ratify the agreement. Talks will first start with the EU-27 discussing common guidelines ahead of a Brexit Summit on 29 April 2017. They should then issue directives that give mandate to the EU Commission to negotiate on their behalf. The EU and the UK will need to negotiate more or less at the same time the EU exit, the new trade deal and the UK stand-alone WTO schedule of commitments. If no Brexit deal is reached and ratified within the two-year timeframe, the European Council and the UK could unanimously decide to extend the deadline. Otherwise, the UK could drop out of the EU without a legally binding exit agreement and the WTO tariffs (above 5% on average) would apply to trade in goods and services. We expect a timely EU exit agreement, accompanied by a transition deal until 2021 when a final trade deal with the EU should be effective (a Limited FTA comprising average weighted tariffs below 5%).

Ukraine: Out of recession, but recovery remains fragile

Second official estimates have put Q4 real GDP growth at +4.8% y/y (up from a preliminary estimate of +4.7%). The growth rates of Q3 and Q2 were also revised up to +2.3% y/y and +1.5% y/y. This takes full-year 2016 GDP growth to +2.3%, a better than expected recovery from the sharp -9.8% recession in 2015, although base effects played a role. The recovery was driven by a strong rebound in fixed investment which surged by +20.1% in 2016, though they remain well below the pre-recession level after having dropped by -9.2% in 2015, -24% in 2014 and -8.4% in 2013. Moreover, inventories added +3.5pp to 2016 GDP growth. Private consumption rebounded as well but only to a modest increase by +1.8% (-20.4% in 2015). Government spending was flat in 2016. Meanwhile, net exports subtracted -5.5pp from 2016 growth (+2.8pp in 2015) as imports recovered to an increase by +8.4% (-17.9% in 2015) while exports continued to contract by -1.6% (-13.2% in 2015). Euler Hermes expects annual GDP growth to fall back to +2% in 2017 as the investment surge will ease and the currently ongoing blockade of coal trade and cargo traffic with the breakaway regions will hit industrial output.

Japan: An export- led acceleration

Growth of JPY-denominated exports accelerated rapidly to +11.3% y/y in February from +1.3% in January. The figure drew the attention for three reasons. Firstly, it signaled a relatively strong start of the year for the Japanese economy. Secondly, a closer look at the export growth drivers provides evidence of a strong demand improvement in Asia as Japanese exports to China and ASEAN rose by +28.2% y/y and +10.5% y/y, respectively. Thirdly, a rise of net exports to the U.S. (+1.5% y/y) raises concerns over an increase in tensions with the Trump administration. Looking ahead, we expect trade to shape the outlook. In the short run, GDP growth is set to enjoy an export-led acceleration driven by higher demand in Asia and the U.S. In the longer term, a sustained expansion will depend on the U.S. trade policy direction. Euler Hermes cautiously forecasts the Japanese economy to rise by +1.2% in 2017 (after +1% in 2016).

Countries in Focus

Americas

U.S.: Manufacturing showing strength

The manufacturing sector is showing signs of significant strength. Manufacturing industrial production rose +0.5% m/m in February to a +1.2% y/y rate, the highest in two years. Machinery and computer/electronics are leading the way at +5.1% m/m and +5% y/y, while appliances and apparel are lagging at -4.1% and -4%, respectively. Perhaps more importantly, only 7 out of 19 sectors are in contraction; just four months ago 12 were. Regional Fed manufacturing surveys are also very strong. While the Philly Fed survey slipped, it is at the highest since November of 2014, and the new orders component rose to a 29-year high. New orders in the NY Fed survey rose to the highest in almost 13 years. Consumer sentiment was also strong, with the present situation component hitting a 17-year high. February housing data was mixed although starts, permits, and existing home sales all remained positive in terms of y/y growth.

Europe

Czech Republic: Growth curtailed by weak investment activity

Second estimates by the Central Statistical Office show that Q4 real GDP grew by +1.9% y/y, up from +1.5% in Q3 but well below the average +3.2% posted in H1. Q4 growth took the expansion of real GDP in 2016 as a whole to +2.4%, considerably down from the exceptional eight-year high of +4.5% in 2015. The deceleration of full-year growth is largely explained by a sharp fall in EU co-financed investment activity at the beginning of the new programming period which caused fixed investment to contract by -3.5% in 2016, after a strong +9% increase in 2015. Consumer spending was the main growth driver in 2016, up by +2.9% (+3.1% in 2015) while public spending moderated to +1.5% (+2% in 2015). External trade activity slowed down as well, but since export expansion (+4.3%) outpaced imports (+3.2%), net exports added +1.1pp from 2016 growth (+0.1pp in 2015). Euler Hermes forecasts annual growth to pick up to +2.8% in 2017 as investment activity should recover.

Africa & Middle East

Morocco: All about that crop

In 2016, the economy registered some disappointing developments. After +4.5% in 2015, GDP growth tumbled to +1.1% (EH expectation was +1.5%). The main laggard was agricultural output (-10.1%) due to severe drought conditions. This combined with subdued demand in the main trading partners (Spain and France) reduced export growth to just +2.5% in 2016. Since imports (+9.5% in 2016) were driven up by capital goods (implementation of past investment plans), the current account deficit worsened unexpectedly to -4.2% of GDP in 2016 (from -2.2% in 2015). Last, but not least, the fiscal deficit rose to -4.2% of GDP, markedly larger than initially planned (-3%). In 2017, conditions should normalize. Better weather conditions are already in place to sustain a growth acceleration to +4.5%. Regarding foreign demand, 2017 should improve as well. Export gains are forecast at EUR1.8bn, more than three times of what was achieved in 2016, and the current account deficit should narrow to -2.7% of GDP.

Asia Pacific

New Zealand: Hit by a bad weather effect

Expenditures on GDP rose by a timid +0.2% q/q in Q4, following a strong +0.9% in Q3 (note that in New Zealand's statistics GDP on the expenditure side usually differs slightly from GDP on the production side). Exports of goods and services decreased significantly by -3.8% q/q as bad weather took a toll on dairy production. Domestic demand softened with lower growth of both private consumption (+0.4% q/q) and investment (+0.7% q/q). Going forward, high frequency indicators suggest an improvement in the short run. Both manufacturing (55.2) and services (58.8) PMIs were clearly above the 50-threshold in February, signaling expansion. Monetary policy is set to remain accommodative in the wake of looming uncertainties over global economic activity and manageable inflation (+1.3% y/y in Q4 2016). Despite the weak Q4, expenditures on GDP grew by +4% in 2016. Euler Hermes expects a softening to around +3% in 2017.

What to watch

- March 24 – U.S. February durable goods orders
- March 24 – Russia Central Bank meeting
- March 24 – Eurozone March PMI (flash)
- March 24 – France March PMI (flash)
- March 24 – Germany March PMI (flash)
- March 27 – Germany March IFO business climate
- March 27 – Germany February retail sales
- March 27 – Italy March consumer confidence
- March 27 – Italy March manufacturing confidence
- March 27 – Turkey March business confidence
- March 28 – Hungary Central Bank meeting
- March 28 – Ukraine February industrial production
- March 28 – U.S. February international trade
- March 29 – Argentina Q4 current account balance
- March 29 – France March consumer confidence
- March 29 – Japan February retail sales

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