Euler Hermes Economic Research

Weekly Export Risk Outlook

18 April 2018

FIGURE OF THE WEEK

+6.8%

Q1 2018 y/y GDP growth in China

In the Headlines

China: Behind the (solid) growth numbers

Real GDP rose by +6.8% y/y in Q1 2018 (similar pace to Q4 2017). Yet, the quarterly growth rate indicates a continued deceleration (+1.4% q/q in Q1, compared to +1.6% in Q4). Looking at the growth breakdown by components (only available on y/y basis), the tertiary sector recorded a slowdown but remained the main growth driver (+7.5% y/y in Q1, after +8.3% in Q4) while the industry gained some momentum (+6.3% y/y, up from +5.7%). Monthly figures suggest that economic expansion may decelerate further in the near term. Apart from retail sales (+10.1% y/y in March), all key indicators slowed down in March, for example industrial production (+6% y/y after +7.2% y/y in Jan-Feb) and investment (7.5% y/y in Q1 after +7.9% y/y in Jan-Feb). Moreover, USD-denominated export growth contracted by -2.7% y/y in March after a +24% y/y surge in January-February. Looking ahead, we expect economic growth to lose further traction as (i) trade frictions with the U.S. should dent the export performance, and (ii) deleveraging policies (e.g. tightened regulation) will hamper debt-intensive sectors (e.g. heavy industries). Euler Hermes forecasts full-year GDP growth of +6.5% in 2018.

Russia: Reprieve, for now

Last week, Russian financial markets suffered a blow after the U.S. Department of Treasury had imposed new sanctions on 6 April, targeting not only government officials but also seven businessmen and 12 companies they control. By mid of last week, the RUB lost around -11% to the USD, yields on 10-year government bonds rose by +8% and the MOEX stock market index fell by -8%. Markets remained volatile until Monday as many analysts had expected the U.S. to announce further new sanctions owing to Russia's role in Syria. However, as President Trump drew back from new sanctions yesterday, markets have recovered some ground, improving some 4% against last week's lows or peaks, respectively. The sanctions will certainly affect the targeted companies, but Russian authorities have pledged to help if needed. For now, we do not expect a significant macroeconomic impact and retain our forecast of +1.9% GDP growth in 2018. Meanwhile, higher oil prices will ensure that Russia continues to run current account surpluses. A first estimate indicates an external surplus of +USD29bn in Q1 2018, up from +USD22bn in Q1 2017 and +USD35bn in 2017 as a whole.

Turkey: Snap elections will not resolve economic risks

President Erdogan today announced early elections to be held on 24 June, bringing presidential and legislative polls forward by more than a year. Local financial markets have rallied upon the news, perhaps reflecting hopes that this will reduce political uncertainty. Over the past month, the Turkish lira (TRY) was under significant pressure; and on 12 April, it fell to new lows against the USD (1:4.15) and the EUR (1:5.14). Despite today's rally, the TRY remains one of the worst performing Emerging Markets currencies this year, down -6% vs. the USD and -10% vs. the EUR in 2018 YTD at the time of writing. However, as early elections raise the risk of too loose monetary policy ahead of the vote, they will rather exacerbate than mitigate the large and rising external vulnerabilities and mounting overheating concerns that Turkey currently faces (see also WERO 4 April 2018 and WERO 22 March 2018). Hence we expect the TRY to come under renewed pressure in the next weeks.

UK: Lower pressures on margins in 2018

The appreciation of the GBP since late 2017 (+5.7% vs. the USD and +1.4% vs. the EUR) has helped inflation to moderate to +2.5% y/y in March 2018, the lowest level since March 2017. Core inflation stood at +2.3% y/y. However, the recent rise in oil prices has driven up input price growth to +4.2% y/y in March from +3.8% in February, though it remained well below the 2017 average of +11%. Hence, pressures on firms' margins have significantly moderated compared to last year. However, the acceleration in wages (+2.8% y/y in February compared to +2.1% on average in 2017) – while bringing real purchasing power slightly into positive territory – should put upside pressure on core inflation going forward. We expect a peak in wage growth at +3% y/y in the coming months. Lower shortages on the labor market should moderate wage pressures thereafter; unfilled job vacancies fell in January (-8,000) for the first time since June 2017. Hence, we expect inflation to reach +2.4% on average in 2018 (down from +2.6% in 2017) and +2.2% in 2019. The Bank of England is likely to increase its key policy interest rate by +25bp to +0.75% on 10 May.

Countries in Focus

Americas

U.S.: Recent data strong, but trade concerns drag

Recent data depict a robust economy. The consumer finally returned as retail sales rose for the first time in four months, gaining +0.6% m/m to a +4.5% y/y rate. Auto sales rose +2% m/m after four straight months of declines which were caused by hurricane replacement sales in the fall. Core retail sales rose +0.4% m/m, the first increase in four months to a firm +3.8% y/y. Housing starts and permits both rose to y/y rates of +10.9% and +7.5%, certainly a positive, but the data is volatile. Industrial production rose +0.5% m/m to 4.3% y/y, twice the long-term average, and down only -0.1% from February's seven-year high. Manufacturing gained +0.1% m/m to a six-year high of +3% y/y. The Fed's Empire State Survey also showed strength in manufacturing production, but the six-month expectations component plunged from 44.1 to only 18.3, only half the long term average and the lowest in two years. The culprit was metals tariffs and fears of a trade war.

Europe

Ukraine: Monetary policy on hold but to remain tight

The National Bank of Ukraine (NBU) kept its key policy interest rate at 17.0% last week, following four hikes by a cumulative 450bp between October 2017 and March 2018. Headline inflation eased to 13.2% y/y in March (from 14% in February) but remained well above the NBU's end-2018 inflation target range of 6% ± 2pp. March inflation was mainly driven by surging prices for food, transport and some services. Core inflation remained also elevated at 9.4% y/y in March. Nonetheless, the NBU considered the current monetary conditions sufficiently tight to bring inflation back to its medium-term target (5% ± 1pp in 2019 and thereafter). In contrast, Euler Hermes expects headline inflation to remain above the targets in 2018-2019. Meanwhile, upwards revised data by the State Statistics Service show that real GDP grew by +2.2% y/y in Q4 2017 (gradually slowing down from +2.8% in Q1) and by +2.5% in full-year 2017. We expect higher interest rates to cause a growth deceleration to +2.2% in 2018.

Africa & Middle East

Nigeria: Financial conditions are improving

In Nigeria, some basic drivers of growth acceleration are currently materializing. The price signal is improving in two ways. First, crude oil prices are currently up to above USD70/bbl, a level where the country runs current account surpluses (+2.5% of GDP is expected in 2018). Second, inflation recorded the slowest pace in two years in March (+13.3% y/y). It should continue to surprise on the downside and reach 10% by year end, with a positive impact on household purchasing power. Exchange rate stabilization is the main explanation behind gradual disinflation since the official and black market exchange rates have been fairly aligned since August 2017. The credit signal is also normalizing. Money supply growth accelerated (+8.1% y/y in February) and capital inflows are back. Foreign currency liquidity is no longer scarce, as foreign exchange reserves are increasing fast and reached USD47bn in March 2018, or nine months of import cover (up from six months one year ago). It should help growth to accelerate from +0.8% in 2017 to +2.5% in 2018.

Asia Pacific

Singapore: Robust growth in Q1

First estimates indicate that Q1 real GDP rose by +4.3% y/y (up from +3.6% in Q4 2017) and +1.4% on a q/q annualized basis (+2.1% in Q4). Growth was driven by a strong performance of the manufacturing sector (+10.1% y/y) with all clusters in the sector increasing, notably the electronics and precision engineering clusters. Services posted robust growth of +3.8% y/y in Q1 (+3.5% in Q4), mainly thanks to solid momentum in the financial and wholesale and retail trade sectors. Meanwhile, construction output continued to contract for the seventh consecutive quarter, by -4.4% y/y in Q1, as both private and public sector building activities fell. Euler Hermes forecasts full-year growth to ease to +2.9% in 2018 (from +3.6% in 2017). In February, CPI and core inflation picked up to 0.5% and 1.7% y/y (from 0% and 1.4%), respectively. As the Monetary Authority expects upward price pressures to persist this year, it tightened monetary policy last week.

What to watch

- April 19 – Poland March industrial production
- April 20 – Canada February retail sales
- April 20 – Canada March consumer prices
- April 20 – Poland March retail sales
- April 20 – Turkey April consumer confidence
- April 23 – Japan April Manufacturing PMI (flash est.)
- April 23 – U.S. March existing home sales
- April 24 – Germany April Ifo business climate index
- April 24 – Hungary Central Bank meeting
- April 24 – France April business confidence
- April 24 – Turkey April business confidence
- April 24 – U.S. March new home sales
- April 24 – U.S. April consumer confidence
- April 25 – France April household confidence
- April 25 – Turkey Central Bank meeting

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