Euler Hermes Economic Research

Weekly Export Risk Outlook

7 February 2018

In the Headlines

FIGURE OF THE WEEK

+1.5%

Russia's GDP growth in 2017 (flash estimate)

Emerging Markets: Boom, boom, boom, boom

Overall conditions in Emerging Markets' (EM) manufacturing sectors eased marginally in January but stayed very supportive as indicated by the EH EM Manufacturing PMI at 52.0 points (52.2 in December). Some large EM such as China and India showed a loss of momentum but overall there were more improvements (10) than deteriorations (5) in our sample of 15 EM. Moreover, open EM still exhibited a steady increase: their aggregate PMI reached 53.7 in January (53.0 in December), the best figure since March 2011. This reflects that the favorable trade momentum during the last quarters triggered an acceleration of domestic demand. Capacity utilization rates have increased and reached highs in many economies, which has two possible consequences. First, it has fueled a positive momentum (and outlook) for private investment. Second, it may hamper near-term growth as a result of labor scarcities, an overheating syndrome and related inflationary pressures. As a result, the monetary policy stance is likely to become more hawkish, mainly in Asia-Pacific, but also in Eastern European EU countries. Both the Czech Republic and Romania hiked their key policy rates by +25bp over the past week.

Germany: Production continues to rise

Output in industry, including energy and construction, fell by -0.6% m/m on a seasonally and working day-adjusted basis in December 2017. In Q4 2017 as a whole, overall output increased by +0.7% q/q. And production in December exceeded the previous year's level by a robust +6.7%. In view of the very pronounced increase in industrial new orders in the third and fourth quarters of 2017, the upward trend in production is likely to continue throughout early 2018. Overall, the economic indicators continue to show a positive picture. The sustained strong employment growth, the significant decline in unemployment, the rising order intake and high export growth are the positive factors. However, not too much impetus came from the retail sector in the fourth quarter as real sales remained at roughly the same level as in the third quarter. Real GDP in the fourth quarter of 2017 is estimated to have increased by +0.5% compared with the previous quarter, slightly less than in the first three quarters of last year.

UK: A soft start of the year on the corporate side

Business confidence softened more than expected in all sectors in January. The Construction PMI registered the biggest drop (-2 points to 50.2), followed by the Services PMI (-1.2 points to 53.0) and the Manufacturing PMI (-1 point to 55.3). While the Construction PMI suggests almost stagnating activity in a context of contracting production since three consecutive quarters, a level well above 50.0 in the Services and Manufacturing PMIs indicate further acceleration, albeit at a slower pace. We are still at an early stage of Q1, but the confidence levels in those two key sectors of the economy suggest GDP growth of +0.3% q/q in Q1. The global outlook should continue to provide positive support to UK companies against the backdrop of slower domestic demand. However, price pressures remain strong and companies face a 'lower profitability and high indebtedness' issue. Overall, business insolvencies increased by +9.9% y/y in Q4. Bankruptcy data per sector are available only for Q3 as yet, showing that accommodation and restaurants, transportation and storage, information and communication, manufacturing, construction and trade were the most impacted sectors.

Russia: Moderate recovery in 2017 set to continue in 2018

According to preliminary estimates, real GDP expanded by +1.5% in 2017, a moderate recovery from two years of annual contraction (2016: -0.2%; 2015: -2.8%). The breakdown of GDP indicates that consumer spending grew by +3.4% and fixed investment by +3.6%, supported by low inflation and a strengthened currency (the RUB gained an average +13% against the USD in 2017). Moreover, stocks added +1pp to 2017 growth. However, government consumption continued to decline by -0.9%. Real export growth gained momentum last year, thanks to higher commodity prices and the improved global environment, increasing by +5.4%. However, the recovery of domestic demand boosted real import growth to +17% so that net exports subtracted -1.9pp from overall growth in 2017. Looking ahead, we expect the gradual recovery to continue in 2018, benefiting from monetary policy easing, robust consumer spending and higher oil prices. However, the output cut deal with OPEC will restrain oil production and exports to some extent. We forecast real GDP growth of +1.9% this year, but potential new sanctions pose some downside risk to this outlook.

Countries in Focus

Americas

US: Strong economic fundamentals remain intact

The economy continues to exhibit strength as 200,000 jobs were created in January, exceeding expectations of 180,000, while December was revised up from 148,000 to 160,000. Gains were widespread, the unemployment rate remained unchanged at 4.1%, and the labor force surged by a massive +518,000, the most in over two years. But most importantly wages grew a solid +0.3% m/m to +2.9% y/y, finally returning to pre-recession rates after almost nine years. The increase in wages led to fears in the stock market over higher inflation and interest rates, possibly sparking a two-day stampede for the exits which was partially reversed on Tuesday. The stock market often separates from economic fundamentals and is a poor indicator of the future. Most recently for example, the ISM manufacturing and non-manufacturing indexes were 59.1 and 59.9 points, respectively, both led by new orders well into the 60s. Our forecast of +2.6% GDP growth and 3-4 Fed rate hikes this year remains intact.

Europe

Poland: Strong growth in 2017, set to continue in H1 2018

Preliminary estimates show that real GDP growth accelerated markedly to +4.6% in 2017 from +2.9% in 2016. Demand-side details are only partly available as yet but indicate that growth was almost entirely driven by domestic uses (+4.5pp) while net exports made only a tiny positive contribution (+0.1pp). Private consumption grew by +4.8%, up from +3.9% in 2015. Thanks to an increased utilization of EU funding for eligible projects, fixed investment rebounded to a rise of +5.4% in 2017, after it had dropped by -7.9% in 2016. Data for Q4 are not provided as yet but the full-year figure suggests that Q4 growth surged to above +5% y/y. Moreover, industrial production rose by +8% y/y in Q4, up from an average +6% y/y in Q1-Q3. The manufacturing PMI eased to a still sound 54.6 points in January (55.0 in December), held back by capacity constraints but new orders and export orders accelerated. All this bodes well for the start of 2018 and we forecast +4% growth for this year as a whole.

Africa & Middle East

Africa: Trade is trendy

The Africa Union is set to launch a Continental Free Trade Area (CFTA) on 21 March. It will follow other announcements such as Morocco's ongoing adhesion the Economic Community of West African States (ECOWAS). Trade integration in Africa has been quite low so far – only 25% of African exports go to other African economies – indicating that more intra-continental trade is likely to boost growth. Regional integration has been the DNA of export-driven strategies elsewhere. Regional trade accounted for 70% of exports in Europe and 60% in Asia in 2017. Trade barriers are still high among African economies which see each other often as trade competitors. For example, the West African neighbors Côte d'Ivoire and Ghana maximized their cocoa beans output in 2017 despite existing agreements supposed to cap the output when prices are low. In contrast, the East African Community showed a better performance of regional trade integration, with interesting results. It was the only region to smooth completely the growth impact of low commodity prices, growing by +6.5% on average in 2015-17.

Asia Pacific

Indonesia: Moving up

Real GDP growth accelerated to +5.2% y/y in Q4 2017, up from +5.1% in Q3. Investment picked up speed (+7.3% y/y, up from +7.1%), private consumption increased by +5% y/y (from +4.9%) and exports rose by +8.5% y/y. Full-year 2017 growth edged up to +5.1% from +5% in 2016. Going forward, there is room for cautious optimism. Export growth will remain robust thanks to rising commodity prices and solid external demand. The positive investment cycle is set to continue on the back of higher public spending on infrastructure, a rise of foreign direct investment inflows and stronger credit growth. Loan growth picked up to +8.4% y/y in December from +7.5 in the previous month. The degree of the expected growth acceleration will largely depend on consumer spending expansion which is projected to edge up from +4.9% in 2017, albeit at a slow pace, retarded by rising inflation. Against this background, we forecast a modest acceleration of GDP growth to +5.3% in 2018.

What to watch

- February 8 – UK BoE monetary policy meeting
- February 9 – Canada January employment report
- February 9 – China January PPI and CPI
- February 9 – France December industrial production
- February 9 – Norway Q4 2017 GDP
- February 9 – Russia monetary policy meeting
- February 9 – UK December construction output
- February 9 – UK December industrial production
- February 9 – UK December trade balance
- February 13 – UK January CPI
- February 14 – EU and Eurozone Q4 2017 GDP
- February 14 – Italy Q4 2017 GDP
- February 14 – Japan Q4 2017 GDP
- February 14 – U.S. January consumer prices
- February 14 – U.S. January retail sales

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