Euler Hermes Economic Research

Weekly Export Risk Outlook

11 September 2013

FIGURE OF THE WEEK

+10.4%

China's August y/y increase in industrial output

In the headlines

Eurozone: Southern Europe, partly cloudy but partly sunny

In **Italy**, Q2 GDP contracted by -0.3% q/q, slightly worse than a preliminary estimate of -0.2%. Domestic demand continued to contribute negatively, with consumer spending down by -0.5% q/q and investment down by -0.3%. However, the pace of contraction in the latter moderated quite significantly as a result of a pick-up in fixed investment (+0.5%, the first growth since Q2 2011). Net trade contributed positively, reflecting export growth of +1.2% q/q and import contraction of -0.3%. Going forward, domestic demand is likely to limit growth as unemployment reached a new record high of 12.1% in Q2 and credit conditions remain tight. EH left its GDP forecasts unchanged at -1.8% in 2013 and +0.3% in 2014 partly reflecting delayed implementation of structural reforms and lack of competitiveness. In **Portugal**, growth surprised on the upside in Q2 (+1.1% q/q, the highest since early 2010), mainly a result of strong exports (+5.2% q/q). Domestic demand stabilised as a result of growth in consumer spending (+0.4% q/q) and lower contraction in investment (-0.1% q/q). Unemployment moderated to 16.9% in Q2 (17.6% in Q1), the first time since mid-2008. However, risks remain skewed on the downside, reflecting the political environment (the government needs to implement EUR5 billion more in austerity measures but the Constitutional Court rejected several similar actions in April). The Troika will assess the progress made by the country in mid-September, by which time a partial return to the bond markets is scheduled. EH revised upwards its GDP forecasts to -1.9% in 2013 and +0.4% in 2014.

Russia: Q2 GDP growth disappoints

Second estimates of RosStat confirmed that Q2 real GDP increased by +1.2% y/y, while Q1 growth was revised upwards to +1.9% y/y from +1.6%. According to q/q seasonally adjusted data, real GDP contracted by -0.3% in Q2 after -0.2% in Q1, indicating that the economy was technically in recession in H1. Agriculture was almost flat in Q2, at -0.1% y/y and +0.1% q/q, but significant y/y increases are expected in H2 reflecting early reports of a good harvest this year after a weak one in 2012. Both manufacturing and construction declined in y/y as well as q/q terms, at -0.5% y/y (-1.2 q/q) and -3.2% y/y (-1.4 q/q), respectively. Most service sectors continued to expand in Q2, except for financial services, which contracted by -1.7% q/q, although it maintained strong growth of +12.5% in y/y terms. The slowdown in retail sales growth suggests that private consumption may have lost momentum (demand-side data are not yet available). The manufacturing PMI was in contraction territory in July and August, while the service-sector PMI returned to growth in August. EH forecasts full year growth of around +2% in 2013.

China: Strong August data

In August, industrial production increased by +10.4% y/y (the most rapid rate in 17 months), up from +9.7% in July. The largest increases were in car manufacturing (+13.9%), ferrous metals (+13.6%) and electric equipment (+12.8%). This is in line with the recent upturn in manufacturing PMI, which gained 2.4 points to 50.1 in August, after four months of decline. Data were also positive on the demand side, as retail sales increased by 13.4% y/y in August, up from 13.2% in July. These positive data suggest that recent measures of the government to boost economic growth (including tax concessions and support for SMEs) are starting to be effective. EH expects further moderate deceleration in H2, with +7.4% GDP growth overall in 2013 and expansion in 2014 to be slightly higher.

Germany: Mixed performance

The Ifo Business Climate Index continued to rise in August, by +1.2% m/m, following +0.3% in July. Despite this improvement, new orders received by industry fell by -2.7% in July m/m, following +5% in June. Foreign demand declined at a more rapid pace (-4.5%) than domestic demand (-0.3%) in July, with a marked fall in demand from the eurozone (-7.5%, after +8.8% in June), compared with a slower decline from countries outside the zone (-2.6%, after +4.5%). Moreover, industrial production was down by -2.1% in July after +1.9% in June, including lower output in the pharmaceutical industry (-6.1%), computers and electronics (-5.3%) and machinery and equipment (-4.6%), while other sectors, including clothing (+4.9%), chemicals (+3%) and the printing industry (+2.2%), recorded higher output. Construction was up by +2.7% in July after +1.1% in June.

Countries in Focus

Americas

US: Labour market report below expectations

The August employment report came in below expectations, with only 169,000 jobs created, downward revisions of 74,000 jobs in the preceding two months and an increase in the duration of unemployment. The latter fell to 7.3% but it was because 312,000 people became discouraged and left the labour force, driving the participation rate to a 35-year low. Hourly earnings and weekly hours both increased but real wages were up only +0.9% y/y. On a positive note, the ISM services index increased to 58.6 (>50 indicates expansion), the highest since December 2005, with strength in the critical new orders component at 60.5. Auto sales in August increased to a 16.1 million annual rate, the highest since November 2007. The combination of weak employment but strength in some sectors suggests that employers are improving existing labour utilisation rather than hiring additional workers. Indeed, productivity increased at an annualised rate of +2.3% in Q2, holding unit labour costs flat.

Europe

Turkey: Q2 GDP growth picks up, subdued H2 outlook

Q2 real GDP growth accelerated to +2.1% q/q (+1.5% in Q1) and +4.4% y/y (+2.9% in Q1) as a result of strong gains in domestic demand. Private consumption expanded by +6.4% y/y, public consumption +7.4% and investment +3.7% (reflecting a +36.7% surge in public sector investment). Export growth decelerated to just +1.2% y/y, while imports increased by +11.7%, so that net exports made a large negative contribution to Q2 growth. Going forward, mounting headwinds since mid-2013 are likely to limit GDP growth in Q3, which may be followed by a modest recovery in Q4. In the wake of news in May that the US Fed would taper its QE, growth prospects have been hit by capital outflows, currency depreciation (the TRY lost around -13% against a 0.5USD+0.5EUR basket during May-August) and monetary tightening (to stabilise the TRY). Political turbulence has added to the concerns. EH has reduced its full year growth forecast to +3.3% in 2013.

Africa & Middle East

Gulf Co-Operation Council: GDP data

In Q2, **Saudi Arabia's** GDP increased by +2.7% y/y, up from +2.1% in Q1 but compared with +5.6% in the same quarter a year earlier. Growth in the non-oil sector was +4.3%, driven by strong output in manufacturing, construction, trade and government services. However, oil output (42% of GDP) acted as a drag on growth, with production of crude oil and NGLs down -3.5% y/y. Recently, oil output increased (to 9.5 mbpd in July) to satisfy global demand following supply disruptions (including Libya and Syria). Overall, EH expects GDP growth of +4% in 2013 and +4.5% in 2014. Meanwhile, in **Kuwait**, official data show GDP in 2012 increased to USD171 billion, a nominal increase of +15.7% in the course of the year and led by increased oil output (2.7 mbpd) but also high government spending and a positive contribution from the finance sector. EH expects oil output gains going forward will be limited and projects GDP growth of +4% in 2013 and +3% in 2014.

Asia Pacific

Indonesia: Monetary policy tightened to bolster the currency

In response to sharp falls in the IDR, Bank Indonesia (BI, the central bank) raised its key policy interest rate by 50bps to 7% at an emergency meeting at end-August, after it had opted for no change just two weeks earlier. In the wake of the recent emerging market (EM) sell-off, the IDR fell by -5.6% against the USD during May-July. This was less than for several other EM currencies as a result of large-scale intervention by BI. However, this caused a -13.8% (USD14.3 billion) decline in foreign exchange (FX) reserves. During August, depreciation accelerated to -10% but the IDR has stabilised in September, to date. EH does not expect a full-blown currency crisis as FX reserves are still sufficient to cover five months of imports or all external debt payments falling due within 12 months. However, recent monetary tightening will weigh on the economy and we have revised our GDP growth forecast to +5.8% in 2013 from +6%. Additionally, expect corporate insolvencies to rise.

What to watch

- September 11 – UK July unemployment rate
- September 12 – Eurozone July IP
- September 12 – India July IP
- September 13 – Japan July IP
- September 13-14 – Eurozone/EU27 Fin Min meeting
- September 15 – Israel August CPI
- September 15 – Macau parliamentary elections
- September 16 – Portugal - Troika review
- September 16 – Eurozone Q2 labour costs
- September 16 – Eurozone August CPI
- September 16 – Rwanda parliamentary elections
- September 16 – Israel Q2 GDP
- September 17 – Eurozone July trade balance
- September 18 – BoE minutes
- September 18 – Fed rate decision

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