Euler Hermes Economic Research

Weekly Export Risk Outlook

6 May 2015

FIGURE OF THE WEEK

-USD51.4 bn

U.S. trade deficit (goods & services) in March

In the Headlines

Eurozone: Keep (business) confident

The Composite PMI remained stable in April, in expansionary territory at 53.9 compared with 54 in March, and looks consistent with positive but still weak GDP growth in Q2 (similar to Q1 expectations of +0.3% to +0.4% q/q). Expansion was visible in both services and manufacturing sectors. In **Italy** the manufacturing index continued to expand, for the fourth consecutive month (at 53.8) with new export orders growing more strongly because of a lower EUR and therefore a downward adjustment in selling prices. However, the counterparty to this is that input prices continued to increase. **Spain** has also registered similar trends, with increasing demand leading to increased production from companies in the manufacturing sector. In contrast, in **Greece**, confidence deteriorated further and now stands at the lowest level since June 2013 (46.5), reflecting continued uncertainty and tight financing for companies (including lower credit availability and high cost of financing). We have revised downwards our GDP forecasts for **Greece**, to +0.2% (from +0.6%) in 2015, with prevailing high downside risks. For the **Eurozone** as a whole we expect GDP growth will reach +1.3% in 2015.

Spain: Highest GDP growth since 2007

The preliminary estimate of Q1 GDP growth indicates expansion of +0.9% q/q (after +0.7% in Q4 2014), the most rapid rate since 2007. The detailed breakdown will be published on 28 May but exports remained an important growth driver in the wake of competitiveness gains and EUR depreciation. However, short-term indicators give a mixed picture; consumer confidence continues to improve, reaching an eight-year high in March but retail sales, which took a downturn at the beginning of the year, are again declining. Moreover, industrial production is recovering, but is still around -30% below its pre-crisis peak. Additionally, unemployment is declining but remains high (23.8% in Q1) and deflationary pressures persist (CPI -0.6% y/y in April). Against this background, we expect the economy will continue to recover through this year, outperforming Germany, Italy and France. However, challenges still remain evident, with oil prices increasing gradually, EUR/USD volatility risks and uncertainty relating to general elections scheduled for December.

Turkey: Struggling

Inflation picked up for the third consecutive month, to 7.9% y/y in April, driven by surging food prices and currency depreciation. The TRY remains under pressure, falling -14% against the USD year-to-date (-6% against the EUR), because of concerns about loose monetary policy. The Central Bank lowered its key policy rate to 7.5% in early 2015 and appears reluctant to tighten now. The decline of the TRY has also largely countervailed any positive impact from lower oil prices. Leading economic indicators point to a weak start to 2015. Despite the weaker TRY, exports of goods fell -7.5% y/y in Q1, reflecting the sluggish recovery in Europe (-7% y/y for Q1 exports to the EU) and geo-political tensions in other important export markets including Iraq (-23% y/y) and Russia (-35% y/y). Industrial production decreased by -0.6% y/y in January-February and retail sales increased modestly (+2.6%). Business confidence indices improved moderately in April to 102.7 for manufacturing and 101.8 for retail sales but remain markedly below levels seen at end-2014. We revised 2015 real GDP growth to +3.2%.

Indonesia: A challenging year

Q1 GDP growth slowed to +4.7% y/y (+5% in Q4 2014). There was a deceleration in government consumption (+2.2% from +2.8%) but private consumption was resilient (stabilising at +5%). Investment increased moderately (+4.4% y/y from +4.3%) and net exports contributed positively as a result of a fall in imports (-2.2% y/y). At a sector level, there was a decrease in mining production, slowdown in construction and manufacturing was the main drag on growth. Advanced indicators give mixed signals. On the upside, the manufacturing PMI improved slightly to 46.7 in April (46.4 in March) and Central Bank business surveys improved. On the downside, consumer confidence decreased slightly. Credit conditions remain tight although the Central Bank reduced its key interest rate (-25bps in Q1) to 7.5% and we expect a -25bps cut in Q2 to support credit growth. Risks are on the downside, with twin deficits, weak external demand and difficulties implementing reforms. In the absence of further government action, GDP growth in 2015 will remain close to +5% (government target of +5.8%).

Countries in Focus

Americas

U.S.: Trade suffers, but outlook for Q2-Q4 brightens

The trade deficit in March increased to -USD51.4 bn from -USD35.9 bn in February, possibly enough to send Q1 GDP into negative territory. Imports increased strongly, by +7.7% m/m, driven by a stronger USD and sharp +36% increase in ship unloadings after resolution of the West Coast port strike. Meanwhile, real personal consumption increased at a +1.9% q/q annualised rate in Q4 2014 but disposable income was up a sharp +6.2%. Consumer sentiment increased to 95.9, the highest level since 2007 and, combined with the rapid increase in income and the waning effects of the port strike, EH expects consumption will drive a rebound in GDP for the remainder of 2015. The non-manufacturing ISM index also painted a positive picture, gaining +1.3 to 57.8 (new orders rising +1.4 to 59.2). The manufacturing sector still lagged, however, as the ISM index in April remained unchanged at an anaemic 51.5 and factory orders increased +2.1% - but it was the first gain in 10 months.

Europe

Russia: Further monetary easing…but will it work?

The Central Bank of Russia lowered its key policy interest rate by -150bps to 12.5% last week, despite inflation remaining above 16%. The third rate cut after the sharp hike to 17% in December 2014 is intended to support the declining economy and was justified with the recent firming of the RUB and a perceived stabilisation of annual inflation, which was estimated at a preliminary 16.5% in April after 16.9% in March. At currently around 1:50 against the USD, the RUB has indeed regained +27% since the low at end-January. However, its value remains around -30% below the average of 2014 (1:38.6). Russian companies will continue to face difficulties in repaying external debt maturing this year, still estimated at around USD100 bn. Meanwhile, the PMI manufacturing index of 48.9 in April (slightly up from 48.1 in March) continues to signal contraction. Worrisome, the flow of new orders declined at the sharpest rate in almost six years. Euler Hermes forecasts GDP will contract by -5.5% in 2015.

Africa & Middle East

Chad: What a relief!

The IMF and the World Bank announced debt relief of around USD1.1 bn, of which USD1 bn represents relief from current obligations to multilateral agencies (through the HIPC Initiative and the MDRI programme) and the remainder to bilateral and commercial creditors. Chad becomes the 36th country to receive relief under HIPC - the first since 2012. Completion point under the HIPC reflects recent improvement in economic management and macro-economic stability, partly under a three-year Fund ECF-supported programme, and will reduce the country's debt burden significantly. The external debt/exports ratio will fall from 55.1% at end-2013 to 31.3% at end-2015 and to 12.5% at end-2019. However, these indicators depend on external developments including oil prices (crude oil accounts for over 90% of exports) and the country's ability to raise new financing, as well as government policy. The Sahel is a challenging environment and commercial opportunities are likely to be limited.

Asia Pacific

Australia: A second cut this year

The Central Bank (RBA) cut its policy interest rate for the second time this year, lowering it by -25bps to a record low 2%. The economy is currently facing tough headwinds, with the end of the commodity boom translating into weaker domestic investment and the Chinese slowdown (and generally weak commodity prices) weighing on exports. In Q2, we expect the economy will remain weak. The labour market is showing positive signals, with a modest decrease in unemployment (6.12% in March from 6.15% in February) but April business surveys indicate a sluggish outlook, with a slight deterioration in service activities (PMI 49.7 from 50.2 in March), a moderate improvement in the outlook for manufacturing and expansion in construction. Against this background, and with continued disinflationary pressures, we expect the RBA will instigate a further -25bps rate cut in Q2. This should boost credit growth, support investment in H2 and bring full year growth in 2015 to +2.6%.

What to watch

- May 07 – France March industrial production
- May 07 – South Africa March electricity production
- May 07 – Egypt April international reserves
- May 08 – Canada April unemployment
- May 08 – China April trade balance
- May 08 – Germany March current account
- May 08 – Germany March industrial production
- May 08 – UK March trade balance
- May 08 – U.S. April employment situation
- May 08 – Turkey March industrial production
- May 08 – Hungary April CPI
- May 12 – Estonia Q1 GDP flash estimate
- May 13 – U.S. April retail sales
- May 13 – Bulgaria, Hungary, Romania & Slovakia Q1 GDP flash estimates

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