

FIGURE
OF THE WEEK

112.9

Ifo Business
Climate Index
in April
for Germany

In the Headlines



France: When construction goes well, so does the economy

After the first round presidential election results, French bond spreads (OAT 10-year) tumbled and equities rallied. Fears of a shock right after the election have waned. On the ground, business confidence edged down to 104 points in April from 104.2 in March but remains well above the long-term average (100). Among the sub-indexes, manufacturing confidence showed the strongest evolution, improving to 108 in April, the highest since July 2011, rebounding from the short-term weakness in March (105, after 107 in February). But translation to real activity is lagging. Despite the sharp improvement of business confidence in December, manufacturing production has not accelerated yet and was still down -0.5% y/y in February (3-month average). This disconnect indicates that corporates have been ready to increase their output but are hesitating to do so since they still lack demand. But, a turning point may have been reached: the expected activity sub-index of the construction survey improved considerably to 10.3 (the best level since March 2008, and 15 points higher than 3 months ago). It means that sound order books (for about 7 months) are turning into effective production.



U.S.: Housing accelerating, confidence slips

The housing market is accelerating. Existing home sales in March reached the highest level of the recovery at 5.7mn units annualized. Prices grew by +5.3% y/y, and supply remains tight at 3.8 months vs. the average of 7 months. New home sales hit 621,000 units annualized and are the second highest of the recovery (after the 622,000 in July 2016). Prices are erratic but have grown +6.9% annually since the bottom of October 2010, and supply is tight at 5.2 months vs. the 5.9 month average. The market for new homes is only 10% of that for existing homes but provides a much higher boost to the economy per unit, since a new home requires much more materials and employees to construct. Consumer confidence slipped from 124.9 to 120.3, perhaps on concerns that policy changes seem stalled, but it is still the second highest in over 16 years. But while confidence is necessary for consumption, it is not enough. Consumers also need increasing income and wages, and until those emerge consumption is likely to continue to disappoint, and in fact may contribute to a very weak Q1 GDP reading.



Germany: Economic sentiment remains high

Confidence among German managers rose further in April. The Ifo Business Climate Index increased to 112.9 points, its highest level since mid-2011, from 112.4 in March. The assessment of the current business situation improved markedly, however, companies are slightly less optimistic regarding their six-month business outlook. This week's Ifo survey stands slightly in contrast to last Friday's flash PMI figures which showed a slight deterioration (but on a still high level). However, the broader Ifo survey should have a higher predictive power for the German economy than the PMI, signaling a further strengthening. The firming up of the world economy on the back of the economic stabilization in key emerging markets as well as an increasingly robust upward trend in the Eurozone are important factors behind the upswing in the German industry. However, the pickup in inflation to around 2% is eroding real income growth, suggesting that private consumption will provide less of a fillip than in the past two years. All told, we are penciling in an increase in real GDP of +1.7% in 2017.



Eurozone: Demand for bank lending is increasing

According to the ECB's latest Bank Lending Survey (BLS), demand for loans continued to increase in Q1 2017 and expectations for Q2 are positive. Easing lending conditions on the back of prevailing competition pressures have driven the rise in demand. In fact, credit standards eased for corporate loans, loans to households for house purchase and consumer credit. They should slightly tighten for companies and remain unchanged for households in Q2. Credit demand increased in Q1 for corporate loans, housing loans and consumer credit, mainly driven by the low level of interest rates, favorable housing market prospects and higher consumer confidence. By country, demand for corporate loans increased in Spain and Germany, stabilized in France, but fell in Italy and the Netherlands. In Q2, banks expect an overall increase in net demand of corporate loans, housing loans and consumer credit. Moreover, BLS banks reported a positive impact of the ECB's expanded asset purchase program on liquidity and financing conditions but a negative impact on net interest margins.

Countries in Focus

Americas



Venezuela: When pain turns into rage

Venezuela has been riven by anti-government street protests over the past weeks, which left over 20 people dead. Opposition supporters ask for an electoral calendar and accuse President Maduro of eroding democracy. This renewed crisis began on 29 March when the Supreme Court tried to take over the powers of the opposition-controlled National Assembly and peaked on 7 April with the announcement of a 15-year ban from public office for opposition leader Henrique Capriles. The uprising is also a response to the alarming economic situation in the country. The oil-dependent economy collapsed when oil prices plummeted in 2015. The ensuing removal of social welfare and rampant inflation aggravated unemployment and poverty. GDP shrunk by almost -10% in 2016, completing four consecutive years of recession and falling back to its 2005 level. We expect the downturn to continue in 2017 while hyperinflation will keep on threatening the economy.

Europe



Poland: Strengthening momentum in Q1

Industrial production surged by +11.1% y/y in March, after a weak +1.1% y/y in February, taking growth in Q1 to +7.3% y/y, up from just +1.5% in Q4 2016. The strong industrial performance was driven by manufacturing output which rose +12.7% y/y in March and +8.1% y/y in Q1. Further, it was matched by a recovery of construction activity which soared by +17.2% y/y in March, after declining throughout 2016 and again in February (-5.3% y/y), bringing the Q1 output increase to +3.9% y/y. Moreover, real retail sales rose by +7.9% y/y in March and by +7.1% y/y in Q1, continuing a quarterly uptrend throughout 2016 with +6.5% y/y in Q4. These data point to an acceleration of real GDP growth in Q1 from the +2.5% y/y recorded in Q4 2016. Looking ahead, the leading consumer confidence indicator as well as the business tendency surveys in industry, construction, trade and services all show m/m improvements in April. We forecast GDP growth of +2.9% in 2017 (+2.7% in 2016).

Africa & Middle East



Tunisia: The Dinar fell and should depreciate further

The TND lost -6% within days after the Finance Minister's announcement on 18 April that the Central Bank will let the currency depreciate gradually. That announcement came shortly after an IMF statement on the expected completion of its review of Tunisian policies (USD300mn should be made available). Exchange rate depreciation followed a further deterioration of Tunisia's external balances. The trade deficit increased by +57% during the first quarter (mainly oil price effect on imports) and the import cover of foreign reserves fell to 3.3 months. The natural dollar outflows implied by the trade deficit and the need to attract fresh capital inflows to balance this outflow and ensure public financing led to the decision to reduce exchange rate interventions and let the dinar depreciate gradually. We expect the fiscal deficit at around -5.6% and the current account deficit at -7.5% of GDP in 2017; hence the government will probably (need to) implement more reforms to rebalance its economy.

Asia Pacific



Japan: Are stars aligning?

Japanese exports continued to rise in March (+12% y/y) supported by growing demand from China, the U.S. and Western Europe. With regard to sectors, export growth drivers were broadly based, with strong performances in key industries such as vehicles, electrical machinery and chemicals. Meanwhile, imports surged as well in March (+16% y/y) suggesting that domestic demand growth strengthened in Q1. Positive signals came also from encouraging bank lending figures (up +3% y/y in March from +2.8% in February) and rising machine tool orders (+22.6% y/y). Looking ahead, business sentiment suggests a continued momentum in Q2. The Nikkei flash Manufacturing PMI rose to 52.8 points in April (from 52.4 in March) on the back of higher new orders, output and stronger job creation. Against this background, Euler Hermes expects real GDP growth to accelerate to +1.2% in 2017 (from +1% in 2016).

What to watch

- April 27 – Germany April inflation (preliminary)
- April 27 – South Korea Q1 GDP
- April 27 – U.S. March durable goods orders
- April 27 – U.S. March foreign trade
- April 28 – Belgium Q1 GDP
- April 28 – Canada February GDP
- April 28 – France Q1 GDP
- April 28 – Russia Central Bank meeting
- April 28 – UK Q1 GDP
- April 28 – U.S. Q1 GDP
- May 1 – U.S. March construction spending
- May 1 – U.S. March personal income and consumption
- May 1 – U.S. April ISM manufacturing index
- May 3 – Eurozone Q1 GDP
- May 3 – Turkey April CPI
- May 3 – U.S. Fed policy announcement

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