Euler Hermes Economic Research

Weekly Export Risk Outlook

8 April 2015

In the Headlines

FIGURE OF THE WEEK

126,000

Number of US nonfarm payroll jobs added in March, Lowest since Dec 2013

Italy and Spain: QE pass-through to companies starts to be visible

Nascent evidence of QE's positive impact began to be visible in Italy and Spain as business confidence shows signs of improvement. In Italy, the Manufacturing PMI increased to 53.3 in March, up from 51.9 in February while it maintained momentum by edging up to 54.3 in Spain, after 54.2 in February. In Q1, the index average is the highest since Q2 2014 for Italy and since 2008 in Spain. Importantly this suggests 0.1-0.2% q/q GDP growth for Italy, the first positive quarter since Q3 2013, and around 0.5% q/q GDP growth for Spain. Output and new orders increased sharply in both countries, driven by strengthening external demand supported by the weaker euro. The employment component increased at the strongest pace in 4 years in Italy, and 8 years in Spain, showing rising optimism and momentum in the manufacturing sector. The Services PMI also increased from the no-change level of 50.0 in February to 51.6 in March in Italy and from 56.2 to 57.3 in Spain, suggesting a pick-up in activity and rising employment. We expect Italian GDP growth at +0.4% in 2015, after 3 consecutive years of recession, while Spanish GDP should expand by 2%, among the fastest pace in the Eurozone.

U.S.: Jobs and manufacturing weak

The March employment report disappointed, showing job growth of only +126,000, the lowest since December 2013, and about half of expectations. The previous two months were also revised down a total of -69,000. Manufacturing and construction both lost -1,000 jobs, the first losses in 15 and 20 months respectively. Real average weekly earnings are up only +0.4% y/y against +1.2% in January. The ISM manufacturing index and the critical new orders component both fell for the fifth straight month to an uncomfortably low 51.5 and 51.8 respectively; eight of ten components fell and four are now below 50. Durable goods orders crept up +0.2%, the first increase in five months, but the critical non-defense capital goods ex-aircraft category fell for the sixth straight month. The trade deficit narrow from -USD42.7 bn to -USD35.4 bn but largely because imports dropped a steep -4.4%, suggesting anemic consumer demand. The lone bright spot was the ISM non-manufacturing which slipped "only" -0.4 to a still firm 56.5.

Iran: Are we there yet?

The framework deal worked out by the P5+1, the EU and Iran is just that – a framework. It provides the outline for an agreement timetabled for end-June and which, if completed, will detail the negotiated terms of some sanctions relief in exchange for capping Tehran's nuclear capabilities. The short-term market reaction to the agreed framework was to send oil prices lower, although significant additional Iranian oil is unlikely to reach global markets for some time. The timing of sanctions relief is unclear and only nuclear-related sanctions are under review. Much can still go wrong before the end of June, interpretations of the framework deal are already at variance and expectations everywhere now have to be managed. However, the positives (face-to-face discussions are to be welcomed in themselves) and the potential should not be overlooked. The potential arises from Iran's market of 79 mn people, possession of the world's fourth largest oil reserves and the largest gas reserves and an economy of around USD350 bn. Additional commercial opportunities, however, may be slow in emerging.

Cyprus: The end of all capital controls, but not yet out of the woods

On April 6th Cyprus lifted all capital controls introduced in 2013 in response to strong deposit outflows. However, the Cypriot economy continues to face strong issues: deflationary pressures remain high with negative inflation rate since April 2013 (-1.9% y/y in March) and unemployment rate on the rise (16.3% in February). Non-performing loans (NPLs) exceed 50% of all loans and are preventing banks from extending new credit to the private sector. Further, interest rates remain very elevated, at above 5% for loans to SMEs, and at almost 6% for consumer rates, and even higher in real terms given the negative inflation rate. Against this background, we expect GDP to fall by -0.5% this year, declining for the fourth consecutive year, and returning to slightly positive growth in 2016 (+0.6%). The EU/IMF programme is scheduled to end in 2016.

Countries in Focus

Americas

Peru: Supportive economic policies

After +5.8% in 2013, the Peruvian GDP grew only +2.4% in 2014, a five-year low. Public and private consumption decelerated slightly. The end of the mining investment cycle, tighter external financing conditions, the fall in commodity prices and lower external demand, notably from China, weighed on investment and exports, which contracted by -2% and -0.3% respectively in 2014. A larger fall of imports (-1.4%) saw a positive contribution of net exports to real growth. In this context, the government announced a series of fiscal stimulus packages, including tax cuts, increases in fiscal spending and several measures to support investment. Also January saw the central bank cut the key rate by 25bps (the third cut since July) to a six-year low, coupled with a drop in local currency reserve requirements from 8.5% to 8.0% in March. Further loosening of the monetary policy is likely in coming months if the activity remains weak, as inflationary pressures are under control (+3% y/y in March).

Europe

Romania: Monetary policy remains accomodating

Last week the National Bank of Romania (NBR; the central bank) lowered its key policy interest rate by 25bps to 2% and also lowered its lending facility rate by 50bps to 3.75% aimed at pursuing adequate liquidity management. Headline inflation has been below the NBR's 2.5%±1pp target range since early 2014, mainly due to declining food and energy prices, and stabilized at 0.4% y/y in the first two months of 2015. Looking ahead, the NBR expects only a slight uptrend in inflation. Real GDP growth slowed to +2.8% in 2014 (after a strong +3.4% in 2013), driven by rapid expansion of private (+4.5%) and especially government consumption (+5.9%). Fixed investment continued to decline by -3.5%, retarded by subdued bank lending to the private sector which has contracted since March 2013 (-3.7% y/y in February 2015). The contribution of net exports to 2014 growth was flat. Euler Hermes expects a +2.7% growth in 2015, with a similar GDP breakdown as last year.

Africa & Middle East

Nigeria: Breaking with the past?

It was a significant development for Nigeria and, perhaps, for Sub-Saharan Africa that an incumbent head of state and the ruling party were both voted out of office and that the election result was accepted by the defeated parties. That does not make the challenges ahead any easier but a government with a popular mandate within a political landscape where democracy is perceived as further embedded should ease the path. Those challenges for President-elect Muhammadu Buhari – his term in office begins in May – include containing the Boko Haram insurgency and rebalancing the economy, which is currently buffeted by lower oil prices. The new regime is expected to impose some austerity measures but will also attempt to engender a system of accountability and transparency in management of the country's oil and gas receipts. We expect GDP growth will be supported by robust non-oil developments and GDP growth will be +4.5% in 2015 and +6% in 2016 (long-term trend +6.2%).

Asia Pacific

South Korea: Weak demand figures suggest further policy action

Nominal exports decreased in Q1 (-2.8% y/y from +0.9% in Q4 2014) as a result of weaker demand from China and Japanese Yen depreciation. Imports fell sharply (-15.2% y/y after -2.8%) in line with slowing domestic demand. Advanced indicators are pointing to limited improvement in Q2. HSBC Markit Manufacturing PMI decreased below the 50 threshold in March (49.2 from 51.1 in February) reflecting a decline in manufacturing production and decreasing new orders. On the demand side, lower consumer confidence (101 in March from 103 in February) and worsening labor market suggest a slowdown in private consumption. In that context, the policy mix is set to be more supportive. The Central Bank has already cut its policy rate in March (-25 bp to 1.75%) and the government announced a KRW10 bn stimulus package. With inflation slowing down to +0.4% y/y in March (from +0.8% in December), an additional rate cut (-25bp) is likely. This will help the economy grow by +2.9% in 2015.

What to watch

- April 09 – United Kingdom February Trade Balance
- April 09 – Brazil February Unemployment Rate
- April 09 – Mexico March CPI
- April 10 – China March CPI
- April 10 – France & Spain & UK February IP
- April 13 – China March Trade Balance
- April 13 – Italy February IP
- April 14 – U.S. March retail sales
- April 14 – Spain & UK March CPI
- April 15 – Brazil February Economic Activity
- April 15 – U.S. March industrial production
- April 15 – Poland monetary policy meeting
- April 15 – France & Germany March CPI
- April 15 – ECB meeting

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