Euler Hermes Economic Research

Weekly Export Risk Outlook

16 May 2018

In the Headlines

FIGURE OF THE WEEK

-0.2%

Q1 2018 q/q GDP decline in Japan (first estimate)

Japan: Q1 GDP – a disappointing reading

Real GDP contracted by -0.2% q/q in Q1 (after a downwards revised +0.1% q/q in Q4 2017) due to a decrease in domestic demand (-0.2% q/q) according to preliminary estimates. Both public and private consumption were flat. Investment contracted by -0.3% q/q in Q1, mainly because of a reduction in private residential investment (-2.1% q/q). Private non-residential investment declined by -0.1% q/q. Net exports contributed positively to growth (+0.1 pp), yet it is worth noting that both export (+0.6% q/q, after +2.2% in Q4) and import expansion (+0.3% q/q, after +3.1% in Q4) slowed markedly. Looking ahead, we cautiously believe that this contraction was temporary and we expect positive economic growth to return in Q2. Firstly, the Manufacturing PMI reading of 53.8 in April (up from 53.1 in March) suggests an uptick in manufacturing activity supported by a rise in new orders. Secondly, important indicators such as jobs and wages (+2.1% y/y in March) for consumption and capacity utilization (improvement from 98.6 in January to 102.4 in March) for investment suggest a rebound in private demand. Against that background, we expect economic growth of +1.2% in 2018 (after +1.7% in 2017).

Netherlands: Consumers are back

Q1 real GDP grew by +0.5% q/q, in line with expectations, after +0.7% in Q4 2017. Consumer spending grew by +1.7% q/q, the strongest pace since 2000. While part of the strength comes from unusually cold weather and consequently higher spending on heating, consumers also spent more on durable goods and services. Prospects look positive with consumer confidence at its highest level since 2007 and falling unemployment (4.9% in March, the lowest level since 2009). Visible tensions in the labor market could drive wages further up in the coming months. In addition, wealth effects from rising house prices (+7.7% y/y in March) coupled with an all-time high confidence in the sector are also positive. Investment in fixed assets increased by +2.3% q/q, as companies' margins stand at a relatively high level and turnover growth recovered strongly in 2017 (+8%). Capacity utilization rates in the industry sector are back to 2007 levels. Net exports contributed negatively to GDP growth (-0.9pp), for the first time in two years. However, this comes after five quarters of strong performance. Overall, we expect GDP growth to reach +2.6% in 2018 (after +3.3% in 2017) and +2.3% in 2019.

Germany: Economic momentum likely to reaccelerate

As expected, economic growth slowed significantly to +0.3% q/q in Q1 2018. A smaller seasonally and working day adjusted increase was last seen in Q1 2015. Nevertheless, we believe there is no reason to fear an end to the upswing. Special factors such as early Easter are likely to have played a role. We expect growth to reaccelerate in the course of this year. The chances that economic growth in 2018 will slightly exceed the +2% mark remain good. The fact that investment increased significantly in Q1 also points to an ongoing positive economic trend. The declines in exports and imports should not be overestimated, as fluctuations from quarter to quarter are not unusual. The moderate export development can under no circumstances already be attributed to the U.S. tariff threats. In our opinion, the global economic outlook remains positive, especially as demand from Europe is proving robust. Nevertheless, downside risks to the global economy have increased in view of the trade tensions. However, we remain convinced that negotiations will prevent a trade war.

France: Life in cartoon motion

The job market improved in Q1, despite relatively moderate GDP growth (+0.3% q/q). Private payrolls increased by +58k in Q1 compared to Q4 and by +270k over the last 12 months, despite a slight decrease in capacity utilization rates in the manufacturing sector during the quarter. This is the seventh consecutive quarter showing job creations above +200k (in 12-month sums terms). Non-farm private payrolls are now above 19mn jobs, so higher than the pre-crisis peak of 18.9mn in Q1 2008. The construction sector is still creating jobs (+7k in Q1), despite the deceleration in building permits in H2 2017. The manufacturing sector reduced jobs in Q1 as it had to decrease its output as a result of a high inventory build-up in Q4 2017. But the trend evolution is still favorable after the manufacturing sector had shown in Q4 2017 its first payrolls increase since Q1 2001. As a result, wage growth in the French economy recovered to +0.7% q/q and +1.4% y/y in Q1, the highest since 2014. We expect +1.6% in 2018 (on average), after three years at +1.2%.

Countries in Focus

Americas

U.S.: Gasoline prices becoming a headwind

Inflation was mostly benign in April. Producer prices fell from +3.0% y/y to +2.6% while the core rate, which strips out volatile food and energy prices, fell from +2.7% y/y to +2.3%. On the consumer side, core prices rose +0.1% m/m, the 13th consecutive increase, and remained at a +2.1% y/y rate. But gasoline prices rose +3.0% m/m to a +13.4% y/y rate, driving overall consumer prices to +2.5% y/y, the fastest pace in 15 months. That rise in prices in turn drove gasoline retail sales up +0.8% m/m to a steep +11.7% y/y rate, perhaps cannibalizing overall retail sales. They fell from +4.9% y/y to +4.7%. And gasoline prices, driven by political uncertainty and strong demand, remain on the march as the summer driving season approaches. The expected benefits of the tax cuts and income increases may now be offset by the headwinds of gasoline prices.

Europe

Turkey: Keep on sliding

President Erdogan yesterday remarked that he would take greater influence on monetary policy if he wins the presidential election next month. He also repeated his unconventional view that lower interest rates are needed to reduce inflation. This sparked a renewed sell-off of the TRY which fell to a new all-time low of 4.50 against the USD at one point this morning (around -15% YTD), before recovering some of the losses. Apart from concerns about the erosion of the Central Bank's independence, the current TRY slide is also driven by high and rising inflation (see also WERO 9 May 2018) and a continuously widening current account balance. The latter came in at –USD4.8bn in March, taking the 12-month rolling shortfall to –USD55bn (up from –USD47bn in December and –USD33bn in March 2017). Only 13% of that were covered by net FDI inflows. As investor confidence is rapidly waning, an emergency interest rate hike before the next scheduled monetary policy meeting on 7 June is on the cards, despite all the rhetoric against raising rates. Otherwise the TRY may end up in a free fall.

Africa & Middle East

Africa: Carrot and Stick for indebted oil exporters

The rise in the oil price (the benchmark Brent hit an intraday high of 79 USD/bbl on 15 May) will fuel growth in African oil exporters. This is welcomed since many of them have sizeable twin deficits (public and external). Their debt levels increased and some payments were delayed, particularly intercompany debt in sensitive sectors (e.g. the oil sector) as well as wages or pensions in some economies (e.g. Congo Republic). The recent rescheduling of Mozambique's sovereign debt to its bilateral creditors has already led to expectations that this mechanism could also work for other countries with high bilateral debt loads (e.g. Congo Rep., Angola and Zambia). Despite the rise in long-term interest rates in the U.S. and the USD strength, current commodity prices and credit conditions are supportive for frontier markets and have allowed African economies to issue USD20bn in Eurobonds YTD. However, caution is warranted. The oil price faces medium-term downside risks (supply should increase, driven by higher prices) and banking on it to issue more debt may prove a blind run sooner or later.

Asia Pacific

China: Landing softly

April figures suggest slower (but still solid) activity expansion. Both retail sales (+9.4% y/y, down from +10.1% in March) and investment growth (+7% y/y YTD, down from +7.5% y/y in January-March) weakened. Good news came from industrial production which accelerated to +7% y/y (from +6% in March) driven by a rise in automobile and steel production. In fact, the latter benefited from the easing of pollution controls which were imposed over the winter. On trade, USD-denominated exports rose by +12.9% y/y in April after a contraction in March (-2.7%), yet the pace was slower than the overall Q1 performance (+14.1% y/y). Looking at advanced indicators, the official Manufacturing PMI edged down to 51.4 points (from 51.5 in March) due to weaker new orders; the Non-manufacturing PMI remained at a high level of 54.8 in April. Against this background, we expect economic growth to remain firm at +6.5% in 2018 but slower than last year (+6.9% in 2017).

What to watch

- May 17 – Egypt monetary policy decision
- May 17 – France Q1 ILO unemployment rate
- May 18 – IMF Board meeting on Argentina
- May 18 – Japan April consumer prices
- May 21 – Japan April trade balance
- May 21 – Poland April industrial production
- May 21 – Thailand Q1 GDP growth
- May 22 – Eurogroup meeting
- May 22 – Hungary Central Bank meeting
- May 23 – Eurozone May PMIs
- May 23 – South Africa April inflation rate
- May 23 – Turkey May consumer confidence
- May 23 – UK April consumer prices
- May 23 – U.S. April new home sales
- May 23 – U.S. FOMC minutes