Euler Hermes Economic Research

Weekly Export Risk Outlook

31 March 2016

In the Headlines

FIGURE OF THE WEEK

+2.4%

U.S. GDP growth in 2015 (same as 2014)

Turkey: Public spending secured robust growth in 2015

Seasonally- and calendar-adjusted Q4 2015 real GDP growth moderated to +4.1% y/y (+5.3% in Q3) and +0.7% q/q (+1.2% in Q3), taking full-year 2015 growth to a nevertheless surprisingly strong +4% (up from +3% in 2014). Surging public sector consumption (+5.4% y/y) and investment (+9.9% y/y) remained the key growth drivers in Q4, bringing the full-year rises to +6.7% and +7.6%, respectively. Private sector investment growth remained weak at +1.7% y/y in Q4 and +2.7% in 2015 as a whole. Consumer spending grew by a robust +4.5% in 2015 but continued to slow in Q4, to +3.8% y/y, affected by ongoing currency weakness and rising unemployment (10.5% in Q3). External trade activity remained weak and net exports subtracted -0.3pps from full-year GDP growth as real exports declined by -0.8% while imports edged up by +0.3%. In 2016, the economy will benefit from ongoing government support and low oil prices but downside risks have increased, namely mounting geo-political threats and tensions with Russia. Early 2016 data, point to a slowdown in activity (see WERO 16 March 2016). Euler Hermes expects annual real GDP growth will moderate to +3.3% in 2016.

China: Uneven recovery in industrial profits

Industrial profits of large companies increased in the first two months of 2016 (+4.8% y/y compared with -2.3% in the same period of 2015). The increase was led by the private sector (+7.5%) but state-owned companies continued to register a decline in profits (-14.5%). Sectors related to domestic demand (agro-food) or that are government targets (high-end electronics and automotives) improved profitability but for primary industries there was further contraction in profits (-12.1% in mining and quarrying). This divergence is likely to continue. Private demand has lost momentum because of weaker confidence and negative wealth effects from financial markets and external demand remains on a downward trend. Supportive measures (including tax cuts, public investment and targeted monetary easing) will probably focus more on sectors related to the new economic model (private consumption and high value added). Unproductive state-owned companies and sectors with overcapacity (metals and machinery) are likely to continue to struggle with deflationary pressures and a high debt burden.

Eurozone: More credit to the private sector

Credit to non-financial corporations (NFC) increased by +0.6% y/y in February. **France** and **Germany** registered credit growth of +0.2% m/m and +0.7%, respectively. There are also encouraging signs in **Italy** and **Spain**, where the credit crunch was a significant economic drag in recent years, with credit to NFC up by +0.1% m/m and +0.2%, respectively, after three months of contraction. The increasingly accommodative stance of the ECB, in the form of several cuts in the deposit rate as well as unconventional measures (including the TLTRO and asset purchases of sovereign and corporate bonds) may affect the private sector through additional bank credit supply, but also rising demand. This stance exerts downward pressure on bank interest rates, especially for loans to the SMEs. The Eurozone average is 2.7%, an unprecedented low, with **France**, **Spain** and **Germany** close to this average but **Italy** remains above, at 3.7%, as the banking system is reforming. The pick-up in credit confirms the recovery in Eurozone demand and that companies are increasingly likely to boost investment through bank financing and less through their cash flows.

Sub-Saharan Africa: Mixed bag

Presidential elections in **Niger** (run-off) and the **Republic of Congo** are expected to return to office incumbents Muhamadou Issoufou (second term) and Denis Sassou Nguesso (in power through most of the period since 1979 and allowed to run again because of constitutional changes to term and age limits), despite perceptions of electoral irregularities. Presidential elections in Zanzibar, a semi-autonomous group of islands and part of **Tanzania**, resulted in withdrawal of assistance from an aid agency because of perceptions of suppression of democratic rights. In contrast, a presidential run-off in **Benin** was “a model for Africa”, with President Thomas Boni Yayi standing down after serving two terms and in **Cape Verde** the opposition gained an absolute majority and unseated the ruling party. Meanwhile, **Senegal** held a referendum on cutting presidential mandates to five from seven years and barring presidents from running for more than two consecutive terms. This mixed outlook for political evolution in Africa again underlines the importance of selectivity in relation to market prospects.

Countries in Focus

Americas

U.S.: Q1 outcome not looking good

Q4 2015 GDP increased by an annualised +1.4% q/q, with full year 2015 growth at +2.4%. Investment fell -1% q/q, the second consecutive contraction, and net exports cut -0.3pps off the headline rate, but consumption was up +2.4%. However, another measure showed consumption of +0.2% m/m in February and 0% in January, suggesting that Q1 consumption will be under +2% annualised, pressuring GDP. Wages and salaries fell -0.1% m/m, only the second decline in 31 months. February's trade deficit widened to –USD62.9bn from -USD62.4bn, also pressuring Q1 GDP as does a fall in corporate profits (-7.8% q/q in Q4 2015, the second consecutive fall and the fourth in five quarters). Full-year profits fell -3.1%. Fed Chair Janet Yellen gave a very dovish speech, citing a litany of downside risks, reiterating a gradual approach and setting market (and EH) expectations of one rate hike, at most, in 2016. Despite weak activity, consumer confidence improved in March to 96.2, from 94.0.

Europe

UK: Fears of a Brexit impact investor confidence

The BoE announced an increase in its countercyclical capital buffer rate to 0.5% of risk-weighted assets from zero, thus imposing further capital restrictions on banks operating in the UK. The Governing Council assessed that an increasing financial cushion is needed to insure the resilience of the banking system in case of higher financial stress. The new rate will come into effect a year from now and the BoE intends a gradual increase to 1%. Uncertainty around the referendum on the UK's EU membership, scheduled for 23 June 2016, is visible; the GBP has lost -8% against the USD since mid-2015 and reached its lowest level since April 2009. In addition, Brexit fears partly explain the decline in inward portfolio investment (-GBP85bn) and have reduced the opportunities of attracting more FDI. Indeed, the stock of FDI may have increased by an additional +GBP300bn since 2014 in a "no Brexit risk" environment. Overall, we expect GDP growth will slow to +1.9% in 2016 from +2.3% in 2015.

Africa & Middle East

Bahrain: Rain check

Q4 2015 GDP growth was +2.8% y/y and for the full year the economy expanded by +2.9%, compared with +4.5% in 2014. Despite low oil prices and regional and international headwinds the economy, which is relatively diversified compared with other GCC countries, remains relatively resilient. Even so, we expect GDP growth will slow further this year and next, to around +2% and +2.5%, respectively. A less expansionary fiscal environment and enduring socio-political discontent will limit growth in domestic demand and the financial sector will be further negatively influenced by global market volatility, concerns relating to China and uncertainty over the path of monetary policies around the world. Austerity measures have included subsidy reductions and increases in prices of utilities and fuel (40-60%). Further state spending cuts are expected and the knock-on effect will make the private sector commercial environment more challenging.

Asia Pacific

South Korea: Bouncing back?

Industrial production was up +2.4% y/y in February (-2.2% in January) and retail sales growth remained in positive territory (+3.1% y/y) although with some weakness (-1.8% m/m). Consumer confidence edged up slightly in March (100 from 98 in February) and business confidence improved with the Business Survey Index for manufacturing up to 68 in March (63 in February). However, this momentum is fragile; export growth and new orders are weak and scope for a strong improvement is limited by unemployment (4.1% in February, up from 3.5% in January) and large household debt. Additionally, significant deflationary pressures persist (producer prices -3.4% y/y in February). Expect the government to provide further fiscal support this year and the monetary authorities are likely to ease policy further (-25bps in Q2). This will help curb deflationary pressures and support demand growth. EH expects GDP will increase by a modest +2.5% in 2016.

What to watch

- April 01 – Spain, Italy, Greece & UK March PMI
- April 01 – Brazil March manufacturing PMI
- April 01 – U.S. March employment report
- April 01 – U.S. March ISM manufacturing index
- April 01 – China official PMI (NBS) & Caixin manuf. PMI
- April 03 – Egypt March international reserves
- April 04 – Germany February unemployment
- April 04 – U.S. February factory orders
- April 05 – U.S. February international trade
- April 05 – U.S. March ISM non-manufacturing index
- April 05 – Canada February trade balance
- April 05 – Saudi Arabia & UAE March PMI

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