Euler Hermes Economic Research

Weekly Export Risk Outlook

14 October 2015

In the Headlines

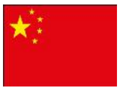
FIGURE OF THE WEEK

USD50

Barrel price of benchmark Brent crude oil (-44% y/y)

Turkey: Lira – how low can it go?

The deadliest terrorist attack in recent history on 10 October in Ankara, with around 100 fatalities, is adding to the already highly-uncertain political environment. Security concerns will rise further and the military campaign against both IS and PKK, which are under suspicion for this and a recent series of smaller attacks, will intensify. The lira has fallen from USD1:TRY2.90 before the latest attack to USD1:TRY2.94 today but beforehand it had recovered from an all-time low of USD1:TRY3.06 in mid-September as a result of some improving economic trends; in August, industrial output increased by +7.2% y/y and the current account deficit narrowed to just -USD163mn (although largely reflecting a fall in imports of -17% y/y). The external deficit remains Turkey's *Achilles' heel*, amounting to –USD26bn in January-August and on track to exceed -5% of GDP in 2015 as a whole. Combined with the upcoming U.S. Fed interest rate hike, this is exerting continued downward pressure on the TRY. Quick formation of a new government after the re-run on 1 November of June's inconclusive parliamentary elections will be a positive and mitigate these pressures to some extent. However, this is far from certain.



China: Struggling?

In September, the trade surplus remained large at +USD60.3bn (+USD60.2bn in August) despite a large contraction in imports (-20.4% y/y, -13.8% in August). A regional breakdown shows import declines from most large trade partners, particularly ASEAN (-26.6% y/y) and Japan (-19.3%). On the export side, data were slightly positive; total export growth was still negative (-3.7% y/y) but a regional breakdown reveals some improvement, with exports to the U.S. and ASEAN up by +6.7% y/y and +6%, respectively. Meanwhile, deflationary pressures persisted in September; producer prices declined for the 43rd month (-5.9% y/y) and consumer price growth weakened to 1.6% y/y from 2%. Overall, high-frequency indicators suggest growth in Q3 will slip below the +7% government target. The outlook is clouded by weak export orders, price pressures and relatively weak growth in domestic demand; private consumption is showing resilience but lower investment growth is acting as a drag. We expect further easing measures and GDP growth will increase by +6.8% this year and by +6.5% in 2016.

UK: Is no inflation good news?

Inflation fell back into negative territory, at -0.1% y/y in September – it was also negative for a period in April and June – reflecting renewed weakness in oil prices and falling food and transport prices of -2.2% y/y and -2.7%, respectively. Prices of goods fell -2.4% y/y while prices of services increased steadily (+2.5%). Core inflation (excluding food and energy prices) remained stable at 1% y/y. The fall in headline inflation is in line with expectations and is likely to continue for a further 2-3 months. Overall, inflation is likely to be 0.1%, at best, on average in 2015 and then increase to almost 1% in 2016 (still very weak). Indeed, the drop in the pound on the back of increasing dovish market expectations related to the first BoE rate hike (our expectation is for Q2 2016, at the earliest) bodes well for positive inflation going forward. Moreover, still solid wage growth (around +3% y/y) and declining unemployment (5.4%, the lowest level since 2008) are also supportive. Although low inflation supports household real purchasing power it is a drag on company turnover, which has been on a downtrend since Q2 2014.

Canada: Healthy jobs and housing markets

The latest jobs report was mostly positive with +12,100 jobs created in September, the third consecutive month of gains and the sixth this year. Wage growth was +2.2% y/y in September, the fifth consecutive month above inflation. The labour force increased by +31,000 after +52,000 in August, sending the participation rate up +0.2pps to 65.9% while simultaneously driving unemployment up to 7.1% from 6.8% in July. However, other details clouded the report. Education lost an unlikely -51,000 jobs, which has been attributed to problems with seasonal adjustments. Full time jobs fell -62,000, part-time jobs gained +74,000 and hours worked fell -0.8% m/m. Meanwhile, the housing market is continuing to rebound with a sharp gain in starts of +230,700 annualised units in September after +214,300 in August. It was the largest gain in three years. Multiple unit starts increased +157,900, the second highest in 25 years, representing a +10.5% y/y increase. Both the jobs and housing data support EH's outlook for encouraging GDP growth going forward.

Countries in Focus

Americas

Mexico: Consumer durable?

Despite lacklustre overall GDP growth (+0.5% q/q and +2.2% y/y in Q2) and state fiscal retrenchment as oil revenues have declined, consumer spending is buoyant. Sales of consumer goods were up +1.9% m/m and +3.6% y/y in July, car sales increased +25% y/y in September and the country's largest retailer announced sales growth of +12.5% y/y in September. Consumption is spurred by: (i) jobs and real wage growth, particularly in the manufacturing sector (ii) relative price stability; consumer price inflation in September was 0.37% m/m and 2.52% y/y, the lowest since the survey was launched in 1970 and (iii) monthly workers' remittances are back above USD2bn; Mexico is the largest contributor to the U.S. foreign workforce. With inflation below the midpoint of the official target rate of 3% +/- 1%, monetary policy can take a lower profile than fiscal adjustments and it is the latter (and weaker investment in the energy sector) that will constrain GDP growth below +3% this year and in 2016.

Europe

Russia: Current account surplus narrows as exports plunge

Initial official estimates indicate that the current account surplus in Q3 was +USD5.4bn, down from +USD15.8bn in Q2. Exports of merchandise goods contracted by -14% q/q and -38% y/y reflecting the renewed fall in global oil prices in Q3. Imports were also down, by -38% y/y, but edged up slightly by +4% q/q. As a result, the trade surplus narrowed to +USD28bn in Q3, down from +USD43bn in Q2 and +USD45bn in Q3 2014. Meanwhile, Q3 saw net capital inflows by the private sector of +USD5.3bn, marking the first quarter of net inflows since Q2 2010. Nonetheless, the cumulative net capital outflows since the start of 2014, nearly -USD200bn, will continue to affect adversely investment activity over the next year. Corporates continue to deleverage as is reflected in the ongoing decline in total external debt to USD522bn in Q3 (-6% q/q, -23% y/y). Overall, fundamentals remain weak and Euler Hermes continues to forecast full-year GDP will decline by -4% in 2015 and -0.3% in 2016.

Africa & Middle East

United Arab Emirates: Down but certainly not out

The PMI was down to 56.0 in September (57.1 in August) but still indicating overall expansion boosted by higher output and new orders. This supports an official forecast of GDP growth of more than +3.5% this year (we expect +3.5% in 2015 and +4.5% in 2016). However, the sharp fall in oil prices (benchmark Brent at USD50/barrel is currently down -43.6% y/y) is weakening fiscal and current account balances and increasing financial vulnerability. In the short term, this does not represent a major problem, particularly as the UAE possesses Sovereign Wealth Funds estimated at USD1,215bn. Even so, the official response to weaker oil revenues is fiscal consolidation, including reductions in energy subsidies and cuts in spending on non-priority projects. We expect the fiscal balance will move into deficit this year (-3.8% of GDP, +6% in 2014), the current account surplus will be more than halved to a still comfortable +6% of GDP and the exchange rate regime (a policy anchor) will remain unaltered.

Asia Pacific

Singapore: Monetary easing, Act 2

The economy avoided a technical recession in Q3, with growth of +0.1% q/q saar (-2.5% in Q2). Manufacturing contracted for the second consecutive quarter (-3.6% q/q saar from -17.4%) with weak performances in electronics, precision engineering and transport but services was a growth driver, accelerating to +0.8% q/q saar (from +0.2%). Advanced indicators point to resilience in domestic demand amid weaker export growth. However, going forward, risks are tilted to the downside. The trade outlook is weak. Major high-income economies (including the U.S. and Eurozone) are set to accelerate, but at a moderate pace, and China's GDP growth will decelerate as a result of lower investment and export growth. Downward price pressures are still evident, with core inflation at 0.3% y/y in Q3 and the CPI declining by -0.6%. The Central Bank "eased" monetary policy for the second time this year reducing the rate of appreciation of the SGD NEER policy band; the width and level of the band were unchanged.

What to watch

- October 15 – U.S. September CPI
- October 15 – Poland September CPI
- October 15 – EU leaders two-day summit, Brussels
- October 15 – Israel September CPI
- October 16 – U.S. September industrial production
- October 16 – Canada August manufacturing shipments
- October 16 – Austria September CPI
- October 19 – EC August construction
- October 19 – Ukraine Sept. industrial production
- October 20 – Hungary interest rate decision
- October 20 – Germany September PPI
- October 20 – U.S. Sept. housing starts & permits
- October 21 – South Africa September CPI
- October 21 – Canada BoC policy statement
- October 21 – Turkey interest rate decision

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