

FIGURE
OF THE WEEK

-20%

Spain's June y/y contraction in credit to non-financial corporates

In the headlines



UK: Positive surprise on growth

Growth accelerated in Q2, to +0.6% q/q, slightly above EH forecasts, after +0.3% in Q1. All the main industry sectors improved for the first time since Q2 2010, indicating that the UK's recovery is strengthening. The main contribution to the increase in GDP came from the services sector (+0.5pps), accounting for around 80% of the economy. Industrial production contributed +0.1pps to the increase, while the construction and agriculture sectors contributed +0.05pps and +0.01pps, respectively. The resilience of the labour market (stable unemployment at 7.8%) and strong retail sales (+0.9% q/q in Q2 after +0.5% in Q1) will have supported private sector consumption. Private investment growth is likely to have remained in positive territory, supported by recovering business confidence and improving credit conditions for the corporate sector. The GDP demand breakdown will be released on 23 August.



Spain: Slow progress?

The Bank of Spain yesterday released preliminary Q2 GDP growth estimates showing a contraction of -0.1% q/q, compared with -0.5% in Q1 and slightly above the forecast of EH. According to the National Statistical Institute, Q2 GDP data reflect a more negative contribution in domestic demand that was partially compensated by a positive contribution in net exports. Meanwhile, unemployment reached a record high of 26.9% in May, double the rate at end-2008 and retail sales decreased by -5% y/y in June, compared with -4.4% in May. Also, credit to NFC further deteriorated in June, declining by -20% y/y, the sharpest fall since November 2007. Against this background, EH expects a progressive stabilisation in growth in Q3/Q4, mainly triggered by further positive contributions from net exports and by improvements in business confidence. In June, for the first time since April 2011, the manufacturing PMI reached 50, indicating balance between expectations of growth and contraction. Overall, EH expects GDP to contract by -1.6% in 2013 and to recover only moderately in 2014, to +0.3%.



Eurozone: Weak corporate investment rate

In Q1, the business profit share (gross operating surplus divided by gross value added) remained stable at 37.7% on the back of a stabilisation in both gross value added and compensation to employees. The gross investment rate fell to 18.8%, reaching the lowest level in the past decade, reflecting contraction in investment (-3.4% q/q), while gross value added remained stable. Latest data for credit to NFC suggest that this trend is likely to continue in coming months as the amount of loans was down by -5% in June to the lowest level since early 2008. Further, investment surveys in Germany suggest that investment in France and Germany is more oriented towards equipment replacement and modernisation, rather than new production. Moreover, prevailing tight credit conditions and weak private demand remain a drag on investment. EH expects stabilisation in eurozone investment in Q3/Q4 if the trend in business confidence continues to improve. In this respect, the composite PMI, at 50.4 in July, was above the no-growth threshold for the first time since January 2012.



North Africa: Regional tremors

The political transitions in North Africa were always going to be difficult, given the revolutionary nature of the regime changes and expectations of the populations. In **Egypt**, the fall of the elected government in early July, detention of the president and ensuing demonstrations and violence delay the prospect of political and economic stability and therefore limit consumer and investor confidence. Without an elected government, IMF support is also on hold and the economy remains dependent on bilateral aid and grants, particularly from the GCC. In **Tunisia**, the political assassination of an opposition leader reflects deep divides between secular and Islamist groups and a similar killing earlier in the year brought down the government of the time. Consolidation of earlier political gains is proving difficult. Meanwhile, in **Libya**, tribal and regional divisions and heavily-armed militia are preventing the establishment of a centralised authority and improvements in security. Trading conditions are challenging throughout the region.



Countries in focus

America

US: Real data

Among generally weak recent data releases, the National Association of Realtors' Pending Home Sales Index, a gauge of future existing home sales, slipped -0.4% m/m in June on higher home prices and rising mortgage rates. The Case-Shiller Home Price Index increased by +1% m/m in May, but it was the smallest gain in four months and was below expectations. However, in y/y terms, growth is now +12.1% and prices in several cities are rising at over +20%. Meanwhile, the Dallas Fed's monthly regional manufacturing survey slipped from 6.5 to 4.4 in July as production and new orders fell. In addition, an index on consumer confidence fell from 82.1 to 80.3 in July as expectations for the next six months weakened, particularly regarding employment. An index reading in excess of 100 is normally associated with a strong economy.

Europe

Hungary: Monetary policy easing and fiscal concerns

The Monetary Council (MC) last week lowered the key policy interest rate by 25bps to a record low 4%. This was the 12th consecutive rate cut since August 2012, resulting in a cumulative reduction of 300bps. Inflation ticked up slightly from an all-time low of 1.7% y/y in April to 1.9% in June, but remained below the lower end of the 3%±1pps target range. The MC expects inflationary pressures to remain muted as a result of continued weak domestic demand and it intends to support the still faltering economy. Hungary did better than most of its peers during the recent market turmoil—the HUF/EUR exchange rate has remained broadly stable since end-April. However, concerns have returned on the fiscal front as the budget deficit reached -3.8% of GDP in Q1, putting Hungary at risk of being placed back under the EU's Excessive Deficit Procedure, which it exited in June.

Africa & Middle East

Mali: Elections and outlook

The first round of presidential elections was held on 28 July. An interim government has been in place following the outcome of a military coup in March 2012 and an insurgency in the north that led to the takeover of around 60% of the country by Islamic militants. In January 2013, French and AU troops intervened to protect the capital, Bamako, and disperse the militants. A successful poll will be followed by parliamentary elections later in the year and an elected government will allow the US to restore aid. However, underlying tensions have not been allayed, relations with Tuareg tribes in the north remain fragile, porous borders allow militants easy entry and exit routes and the economy contracted last year. As a result, after elections that were an effective two-person race between Ibrahim Boubacar Keïta and Soumaïla Cissé, expect the new president to have a challenging term in office.

Asia Pacific

South Korea: GDP growth accelerated in Q2

Q2 real GDP growth picked up to +1.1% q/q (advance estimate) from +0.8% in Q1, largely reflecting acceleration in consumption. Government spending expanded by +2.4% q/q in Q2 (+1.2% in Q1) and household spending shifted to an increase of +0.6% after falling by -0.4% in Q1. Fixed investment growth moderated to +1.9% q/q in Q2 (+3.8% in Q1). External trade activity also eased in Q2, with exports expanding by +1.5% q/q (+3% in Q1) and imports by +1% (+2.5% in Q1), but net exports still made a significant contribution to Q2 growth. In y/y terms, Q2 GDP growth picked up to +2.3% from +1.5% in Q1, with all major demand-side components showing an acceleration, notably fixed investment that, after four quarters of contraction, increased by +2.7% y/y, reflecting rapid expansion in construction investment (+7.1%). EH expects full year 2013 growth of around +2.5%.

What to watch

- August 1 – EU-27 July manufacturing PMI
- August 1 – Russia July manufacturing PMI
- August 1 – UK August BoE base rate decision
- August 2 – US July unemployment
- August 5 – Nigeria Q2 GDP
- August 6 – Italy Q2 GDP
- August 6 – Egypt July official reserves
- August 7 – UK BoE inflation report

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