Euler Hermes Economic Research

Weekly Export Risk Outlook

7 March 2018

In the Headlines

FIGURE OF THE WEEK

25%

Planned U.S. import tariffs on steel

U.S.: Tariff threats overshadow other good news

Real personal consumption expenditures (PCE) fell -0.1% m/m in January, perhaps due to cold weather. More importantly, as a result of tax reform personal taxes fell -3.3% m/m, resulting in a steep +0.6% m/m gain in disposable personal income to +2.3% y/y; just six months ago it had been only +1.1% y/y. More income provides fuel for spending, and it pushed the savings rate up from 2.5% to 3.2%. The ISM manufacturing index rose +1.7 points to 60.8, the highest in almost 14 years. The report mirrored four strong Fed surveys. The ISM services index slipped -0.4 to a still strong 59.5. New Fed Chair Powell was slightly more hawkish in his first testimony to Congress, making three hikes this year a virtual certainty, and a fourth a possibility. President Trump announced import tariffs of 25% on steel and 10% on aluminum, sparking loud protests from business groups, and retaliatory threats from trading partners. If the tariffs are actually enforced, domestic producers of the metals will win, but manufacturers and consumers will lose due to price increases and retaliation from trading partners.

Greece: Economic recovery takes a breather

According to the Greek statistics office Elstat, the economy grew +0.1% q/q in the final quarter of 2017, marking the fourth consecutive quarter of positive economic growth. However, the growth reading failed to meet consensus expectations as private consumption disappointed with a decrease of -0.3% q/q and exports declined by -2.3% q/q despite the favorable European economic backdrop. Meanwhile, investment provided some positive news with a strong gain of +27.8% q/q. For 2017 as a whole, GDP growth now stands at +1.4%, in line with our expectations. In particular the strong increase in investment last year (+15.7%) is good news. However, given the relatively weak end to the year and the rather disappointing performance of private consumption over the course of 2017, our growth forecast of +2.5% for 2018 is now on the ambitious side. With Greece aiming to exit the third bailout program in August 2018, economic momentum will have to pick up again to ensure a smooth full return to international capital markets.

India: Let's grow

Real GDP rose by +7.2% y/y in Q4 2017 (up from +6.5% in the previous quarter) driven by a strong performance in manufacturing and construction. On the expenditures side, strong growth in investment (+12% y/y) offset weaker growth in private consumption (+5.6% y/y). Monthly indicators point to solid growth in 2018. Infrastructure output rose by +6.7% y/y in January (compared to +4.2% in December). The manufacturing PMI signaled expansion in both January (52.4) and February (52.1). Meanwhile, the authorities continue to pursue prudent economic policies. The central bank has maintained its cautious accommodative stance with a low policy rate but does not give any hint of further easing. On the fiscal side, the government has slowed the budget consolidation process: the deficit is expected at -3.5% of GDP in FY2017-18 (the fiscal year in India ends on 31 March) and -3.3% in FY2018-19, compared to the initial targets of -3.2% and -3%, respectively. Euler Hermes forecasts economic growth of +6.7% in FY2017-18, followed by +7.3% in FY2018-19.

Emerging Markets: Risk on

Growth conditions stabilized in Emerging Markets (EM) excluding China. Our aggregate manufacturing EM PMI eased from 52.0 points in January to 51.5 in February. The slowdown is fully explained by the evolution of China's official PMI from 51.3 to 50.3, but this data has to be taken with caution since the Chinese New Year may have had an impact on it. The other key deterioration was the drop in Russia's PMI to 50.2, the worst index since July 2016. Among the improvements, the main came from unbalanced economies (those with a large fiscal and/or external deficit: Brazil, Turkey, South Africa and Mexico) with an aggregate PMI of 53.0, the best in the last 7 years. It shows how these economies are benefiting from the dovish global economic environment. Asia Pacific economies excl. China (Singapore, Taiwan, Hong Kong, Korea and Indonesia) exhibited also an improvement to 52.1 on aggregate (best level since April 2011). It reflects that these markets, while highly exposed to China and at the same time very open to trade, are still in a good shape.

Countries in Focus

Americas

Brazil: Four full quarters of growth

Real GDP growth in Q4 2017 came in below our expectations, at just +0.1% q/q (after +0.2% in Q3), with a high contribution of investment growth (+0.3pp). That took full-year 2017 growth to +1%, with all four quarters posting positive increases. The recovery in private consumption and the change in inventories were the main drivers of the annual change. Investment subtracted -0.3pp from the annual growth performance despite growing in the last three quarters, mostly because of a strong negative carryover at the end of 2016. In 2018, we expect around +2.5% real GDP growth in Brazil on the back of (i) low inflation (+2.9% in January) which should support further real wage growth; (ii) easing lending conditions (lower lending rates at 26.3% in January, down from a high of 33.4% in October 2016); (iii) recovering credit; and (iv) recovering investment (after more than 3 years of decline). The adoption of further structural reforms will be key to lift the country's potential growth.

Europe

Turkey: Mixed data, as usual

Headline inflation edged down to 10.3% y/y in February (from 10.4% in January) and the TRY has remained fairly stable against the USD since the start of the year (though it is down -3% against the EUR). Hence the Central Bank of Turkey (CBT) kept its set of policy interest rates unchanged today, including the official policy one-week repo rate (8%) and the late liquidity window lending rate (12.75%). Since November 2017, the CBT has funded the market entirely through the latter, making it the effective policy rate. We expect the CBT to continue this unorthodox, relatively tight monetary policy stance in the next months. Should inflation fall markedly at some point, a subsequent cautious loosening is likely. Meanwhile, nominal exports of goods rose by +11% y/y in January but were outpaced by soaring imports at +38% y/y. As a result, the rolling 12-month trade deficit widened to –USD82bn in January 2018 from –USD57bn a year earlier. This poses upside risks to our current account deficit forecast of -4% of GDP in 2018, after an estimated -5.5% in 2017.

Africa & Middle East

South Africa: Honeymoon

South African growth data continued to improve in Q4 2017, coming in at +3.2% q/q annualized, after already two quarters of above trend growth (+2.9% in Q2 and +2.3% in Q3). The improvement of agricultural production (+23.5% in 2017) was a key trigger for the recovery. Agriculture is not a strong part of the economy, but the output normalization contributed to the observed disinflation. Low inflation was the main trigger for the overall growth acceleration. As a result, we lower our inflation forecast for 2018 to +4% on average. Considering this still benign inflation environment and the positive surprise on growth, we revise upward our 2018 growth forecast from +1.4% to +2%, the fastest rate since 2013 (+2.5%). This more favorable outlook should also make the fiscal balance adjustment easier, facilitating the implementation of reforms and driving fiscal revenues higher. As a result, we revise our fiscal balance 2018 forecast from -4.5% to -4% of GDP.

Asia Pacific

Hong Kong: Fading momentum?

GDP growth slowed to +3.4% y/y in Q4 2017 (from +3.7% y/y in Q3). Private consumption expanded by +6.3% y/y. Investment rebounded to an increase of +4.7% y/y in Q4 from a -1.3% y/y decline in Q3, largely thanks to stronger capital expenditures for machinery, equipment and intellectual products (+10.1% y/y). Export expansion remained robust (+3.4 % y/y for goods exports; +4% for services exports) driven by strong foreign demand for services. Looking ahead, we expect the economy to lose some momentum but to remain robust (+2.8% growth in 2018). Slower growth will be a result of weaker demand growth from China, tighter financing conditions, and property tightening measures. Yet, we expect domestic demand to remain relatively robust, supported by favorable fiscal policy. The budget proposals for FY2018-19 include tax relief for fragile agents and measures (for examples tax cuts) to support innovative corporates.

What to watch

- March 8 – Mexico February inflation
- March 9 – Brazil February inflation
- March 9 – U.S. February employment report
- March 9 – France January industrial production
- March 9 – Germany January industrial production
- March 11 – Colombia legislative elections
- March 12 – China February loan growth
- March 12 – Turkey January balance of payments
- March 13 – Argentina central bank meeting
- March 13 – U.S. February consumer prices
- March 14 – Argentina February inflation
- March 14 – Canada February Teranet housing prices
- March 14 – Spain January retail sales
- March 14 – U.S. February producer prices
- March 14 – U.S. February retail sales

Contact Euler Hermes
Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com