Euler Hermes Economic Research

Weekly Export Risk Outlook

15 April 2015

In the Headlines

FIGURE OF THE WEEK

USD60

Barrel price of benchmark Brent crude oil (-45% y/y)

World Economy: Bounce back or limp forward?

The latest IMF biannual World Economic Outlook indicates a moderately positive – but uneven – global growth assessment in the short term but provides medium-term concerns because of complex underlying factors. Growth in advanced economies is projected to strengthen in 2015 but in emerging market and developing economies it is expected to be weaker. Overall, the IMF forecasts global growth, using market exchange rates, of +2.8% in 2015 and +3.2% in 2016. EH is marginally less optimistic, with +2.7% in 2015 and +3.1% in 2016.

The IMF forecasts growth in **advanced economies** – supported by weaker oil prices – at +2.4% in 2015 (+1.8% in 2014). Growth in the **U.S.** is projected at around +3% in 2015 and 2016, with domestic demand promoted by lower oil prices, more moderate fiscal adjustment and continued support from an accommodative monetary policy, despite anticipated higher interest rates and some drag on net exports from recent USD appreciation. The **Eurozone** is now showing positive momentum, supported by lower oil prices, low interest rates and a weaker EUR. In **Japan,** after a disappointing 2014, a weaker JPY and lower oil prices are expected to boost growth. For most **emerging and developing economies** (with a marked exception in **India**) growth prospects in 2015 are slightly worse. Growth is projected to slow to +4.3% in 2015 from +4.6% in 2014, reflecting further slowdown in **China**, weakness in **Latin America**, the impact of oil price declines on **oil exporters** and some structural restraints and geo-political tensions. However, growth in **low-income countries,** as a group, is expected to slow only moderately and still register GDP expansion of +5.5% in 2015 (+6% in 2014) before a rebound in 2016, partly reflecting increased external demand from advanced economies.

The Fund's medium-term concerns include legacies from the financial crisis and Eurozone problems, including bank sector weakness and high levels of public, corporate and household debt. These weigh on spending patterns and growth in some countries and low growth slows the deleveraging process. Moreover, ageing populations, investment inertia and relatively low productivity growth suggest that lower potential growth may now be the norm for both advanced and emerging market economies.

China: Keep calm, after all it is +7% growth

GDP growth slowed to +7% y/y in Q1 (from +7.3% in Q4 2014). Economic activity continues to show signs of weakness, with further slowdown in both industrial production (+6.4% y/y in Jan-Mar from +6.8% in Jan-Feb) and retail sales (+10.6% y/y from +10.7%). Fixed asset investment remains on a downward trend (+13.5% y/y) and industrial profits are still decreasing (-4.2% y/y in Jan-Feb). Negative price pressures remain evident in the manufacturing sector, with PPI decreasing in March (-4.6%) for the 37th month. Even so, there is some good news. Firstly, per capita disposable income growth remains strong (+9.4% y/y in Jan-Mar) and consumer confidence is up. Secondly, key sectors targeted in the 12th Five-Year Plan are showing positive developments: high-tech sector profitability was up by +48.4% y/y in Jan-Feb, online retail sales increased +41.3% in Jan-Mar and services remain resilient. Thirdly, the policy mix is supportive. In Q1, the PBoC cut its lending rate and the Reserve Requirement Ratio. Another cut is expected in Q2 (- 25bps for the lending rate). This, coupled with additional fiscal stimulus, will enable GDP to increase by +7.1% in 2015.

Eurozone: More credit to come

In the Q1 ECB Bank Lending Survey we note visible improvements as a result of the ECB QE programme. There was a net easing of credit standards on loans to corporates across the region, especially in Italy. Credit demand continued to improve, although fixed investment continued to remain a drag. The survey shows that over the past six months, banks benefitted from an increase in liquidity as a result of the ECB ABS and covered bonds purchases that they used, and will continue to use, to grant new credits to the private sector. Looking at the real data, credit to the private sector seems to have reached a trough of -0.1% y/y in February. More specifically, credit to non-financial corporations increased by EUR8 bn in February but remained in contraction on a y/y basis (-0.7%, compared with -1.2% in January). Real interest rates on loans to SME in Italy and Spain fell by -50bps in February, although remaining elevated (4.7% in Spain and 4.5% in Italy, compared with <3% in France and Germany). We expect financing will become less constraining for companies in the months ahead.

Countries in Focus

Americas

Argentina: Waiting for the elections

Industrial production is constrained by import and currency controls, private consumption is hampered by persistent inflationary pressures and access to international capital markets remains blocked (there is still no agreement with the “vulture” funds). We do not expect significant economic improvement before the general elections, which are scheduled for October, as international investors are in “waiting mode” until they can gauge whether the new president will be more business friendly. Meanwhile, social unrest and currency depreciation will be the main challenges. Financial support from China and high export revenues have prevented further erosion of international reserves and limited the pace of currency depreciation (-1% per month against the USD since March 2014). However, a collapse of the ARS cannot be ruled out if the Central Bank loses the ability to defend the currency. FX reserves currently provide an import cover of below four months.

Europe

Russia: Devil in the detail

Initial official estimates indicate that the current account surplus in Q1 was +USD23.5 bn, a decrease of only USD2.4 bn from Q1 2014, despite weak oil prices, imposition of sanctions and an associated decline in goods exports of USD36.4 bn over the same time period. In Q1, exports of merchandise goods were down -29.6% y/y but imports declined by a marked -36.3% y/y. The cut back in imports partly reflects the impact of a weaker RUB and heightened inflationary pressures on the purchasing power of the private sector. In addition, sanctions make it more difficult for Russian borrowers to roll over external loans and this decreases net interest outflows. Relatively positive aggregated data on the current account therefore disguise weak fundamentals rather than a position of strength and re-affirm our view that the recession will be protracted. EH forecasts a contraction in GDP of -5.5% in 2015 (after +0.6% in 2014) and our tentative forecast for 2016 is -4%.

Africa & Middle East

Morocco: Far from being a basket case

The Central Bank revised the weighting in the country’s dirham (MAD) currency basket. The MAD's value will now be based on weightings of 60% for the EUR and 40% for the USD (previously an 80/20 split). The change reflects: recent EUR weakness (increasing import costs), adjustments in structural trade patterns and other transactions and a stepped move towards a more-flexible exchange rate system that will improve competitiveness. Although the bulk of international transactions are still denominated in EUR (France and Spain account for around 36% of exports and 25% of imports), trade with and investment from the GCC (currencies linked to the USD) are increasing. Approximately one-third of FDI inflows and 15% of remittances involve the GCC. Overall, the currency change reflects the country’s broadening trading environment. We expect the MAD will depreciate moderately against the EUR in the medium term and assist export industries focused on Eurozone markets.

Asia Pacific

India: Lower inflation suggests further policy action

Inflationary pressures receded in March, with CPI growth (5.2% y/y) lower than in February (5.4%) and wholesale prices remaining in negative territory (-2.3%), reflecting weak food inflation and low energy prices. With CPI inflation remaining below the RBI target (maximum 6%), room for further monetary easing has increased. However the Central Bank decided to pause its easing cycle (two rate cuts of -25bps in Q1). Activity data have shown some improvement with production (+5% y/y in February and +2.8% y/y in January) and confidence in industry (HSBC Markit Manufacturing 52.1 in March from 51.2 in February) advancing. Domestic demand is set to pick up gradually from Q2 onwards, reflecting improved credit conditions. Inflation is likely to increase only moderately in the short term (5.3% y/y in Q2) because of low energy prices. Against this background, the RBI will probably lower its key rate (by 25 bps). GDP growth will be +7.7% in FY2015/16 (from +7.5% in FY2014/15).

What to watch

- April 16 – U.S. March housing starts
- April 17 – Japan March consumer confidence
- April 17 – U.S. March CPI
- April 17 – Russia March real disposable income
- April 17 – Russia March unemployment
- April 17 – Argentina March national urban CPI
- April 20 – Argentina March budget balance
- April 20 – Brazil weekly trade balance
- April 21 – South Africa February leading indicator
- April 21 – South Africa March CPI
- April 21 – Argentina March trade balance
- April 22 – Brazil March current account

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Contact Euler Hermes Economic Research Team
research@eulerhermes.com

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