Euler Hermes Economic Research

Weekly Export Risk Outlook

8 November 2017

FIGURE OF THE WEEK

+5.1%

Q3 2017 y/y GDP growth in Indonesia

In the Headlines

Germany: Solid growth outlook

The prospects for the German industrial sector remain favorable. In September, price-adjusted new orders in manufacturing increased a seasonally and working-day adjusted +1% on the previous month (August: +4.1%) while industrial production was down by -1.6%. A major driver behind the latter was the automotive sector, where production declined by -6.5% on the previous month (following a sharp jump of +11.1% in August). The strong fluctuation in monthly data was due to the fact that plant holidays in the automotive sector happened to be in July rather than in August this year, so the figures overstated the situation in August somewhat. In the third quarter as a whole industrial production increased by +1.1% on the previous quarter in seasonally-adjusted terms (Q1: +0.9%, Q2: +1.7%). Based on this we still feel comfortable with our real GDP call of +0.5% q/q for Q3. In light of overall very strong economic data (Ifo business climate, PMIs, new orders, labor market etc.) we will probably adjust our Q4 2017 and 2018 GDP growth forecasts based on the upcoming Q3 data release on 14 November. It looks like there is some upward potential.

Indonesia: Slowly picking up

Real GDP growth edged up to +5.1% y/y in Q3 (from +5% in Q2). While the increase in private consumption remained stable (+4.9% y/y), investment picked up speed (+7.1% y/y, after +5.3% in Q2). Exports surged by +17.3% y/y in Q3 but the impact on GDP growth was partially offset by an almost equally strong rise in imports (+15.1%). Looking ahead, strengthening investment growth indicates a gradual acceleration of economic expansion in the short run. Moreover, monetary policy is broadly accommodative: the Central Bank cut its policy rate by 0.25pp to 4.25% in September. Yet, domestic credit growth, at +7.9% y/y in September, has remained below the Central Bank's target of +10% y/y. Fiscal policy is cautiously accommodative with rising government expenditures targeting infrastructure development. Externally, the economy is benefiting from a rise in capital inflows (+12% y/y for FDI in Indonesia in Q3 2017). Against this backdrop, full-year real GDP growth is forecast to pick up gradually to +5.1% in 2017 (from +5% in 2016) and +5.2% in 2018.

Bahrain: Increased country risk

Last week, the smallest GCC member state reportedly asked Saudi Arabia and the UAE for financial support in order to replenish its FX reserves and avert a currency devaluation. Bahrain's fiscal and external vulnerabilities have steadily increased in the wake of continued low oil prices since 2014. Even though the annual fiscal deficit will decline from an average -18% of GDP in 2015-2016, it is expected to remain very large at around -12% in 2017 and -11% in 2018. Public debt has rapidly risen from 44% of GDP in 2014 to currently around 90%. The current account deficit widened to -4.7% of GDP in 2016 and is forecast to remain above -4% in 2017-2018. Financing the fiscal and external deficits has reduced the Central Bank's FX reserves to about USD1.4bn in August 2017 (import cover 0.7 months); and Bahrain's SWF is comparatively small, comprising about USD10bn at end-2016. The GCC neighbors are likely to provide the requested aid but on the condition of serious fiscal consolidation, which in turn will curb growth prospects in the short term. All in all, country risk in Bahrain has risen.

Emerging Markets: World, hold on

The manufacturing sector is still exhibiting growth in Emerging Markets (EM). Our proprietary EM aggregate Manufacturing PMI decreased to 51.3 points in October from 51.9 in September, but the bulk of this evolution was explained by two particular events. First, the Mexican PMI went down from 52.8 in September to 49.2 in October, the first below-50 print since September 2013. This was driven by the impact of the earthquake, already visible in Q3 growth figures (-0.2% q/q; see also WERO 2 November 2017), as it disrupted the supply chain as a result of raw material shortages. Second, the Chinese PMI index normalized to 51.6 points in October after a relatively high value in September (52.4). Elsewhere in other EM, the manufacturing activity stayed vibrant in October, particularly in open economies in Asia Pacific (e.g. 52.6 in Singapore, a new high since December 2009) and Eastern Europe (e.g. 58.5 in the Czech Republic, the highest figure since April 2011). It suggests that the overall growth momentum is still robust in the world economy, and that trade continues to accompany this growth cycle.

Countries in Focus

Americas

U.S.: A solid picture

The economy is strong and we are upgrading our 2017 GDP growth forecast from +2% to +2.2%, despite a slightly disappointing jobs report. In October, +261,000 jobs were created, rebounding from the hurricanes, but below expectations of +325,000. Still the average of the past two hurricane-affected months is +140,000, not far from the average over the last year of +175,000. The unemployment rate fell from 4.2% to 4.1% in October, but it was because the labor force shrank. Wages were flat, putting the y/y rise to +2.4%, the lowest in 21 months. The GOP released its tax plan which will add USD1.5trn to public debt over 10 years. It is likely to pass the House but will face opposition in the Senate. President Trump appointed Jerome Powell as the new Fed chair, who will likely continue Yellen's path since he has not dissented from a Fed decision since 2012. Several other reports indicated strength in the economy, including the ISM non-manufacturing index, productivity, and factory orders (+8.3% y/y).

Europe

Latvia, Lithuania & Serbia: Diverging growth trends

In **Latvia**, Q3 real GDP growth accelerated to +1.5% q/q and +5.8% y/y (from +1.4% q/q and +4% y/y in Q2). On the production side, Q3 growth was driven by a surge in construction (+23% y/y) and strong increases in industrial output (+8% y/y) and services (+4% y/y), of which retail sales were up by +5% y/y. We have revised upwards our full-year growth forecasts to +4.4% in 2017 and +3.9% in 2018. **Lithuania**'s Q3 GDP growth eased to +0.1% q/q and +3.1% y/y (from +0.6% q/q and +4.1% y/y in Q2). Details are not available as yet, but the statistical office indicated that services were the main growth driver in Q3, including wholesale and retail trade, transportation and storage, accommodation and food service. We now project full-year growth +3.5% in 2017 and +3.2% in 2018. In **Serbia**, real GDP expanded by +2.1% y/y in Q3 (up from +1.3% in Q2). We have slightly revised our full-year growth forecasts to +1.6% in 2017 and +2.5% in 2018.

Africa & Middle East

Morocco: Growth is plateauing

Growth was back in Morocco at the beginning of 2017, as a result of better crops. The comeback of agricultural production above 2015 highs is a key contributor to overall growth. Again, the agricultural output went up by +14.7% y/y in Q3 and was a key driver of overall real GDP growth of +3.8% y/y. However, the latter was below the Q2 performance (+4.2% y/y), mainly because growth of non-agricultural GDP (85% of the economy) edged down to +2.6% in Q3 (from +2.8% in Q2). This somewhat deceptive performance is putting a downside risk to our overall scenario for 2017 and 2018 (EH expects +4.5% growth in both years). The downside risk is stronger for 2018 since positive base effects seen in 2017 in the agricultural sector were a one-off. Growth in the non-agricultural sector is not accelerating as previously expected. It reveals a somewhat poor efficiency of investment: typically Morocco needs 10 points of investment (in % of GDP) to nurture 1pp of GDP growth.

Asia Pacific

China: A gradual moderation

China's official PMIs suggest a moderation of economic activity growth in October. The manufacturing index decreased to 51.6 points (from 52.4 in September) reflecting lower growth in new orders, new exports orders and output especially. The non-manufacturing index declined to 54.3 (from 55.4 in September) showing a contraction in employment and lower growth in new orders. Hard data for October also indicate a moderate slowdown of activity: USD-denominated exports growth eased to +6.9% y/y from +8.1% in September while USD-denominated imports expansion edged down to +17.2% y/y (from +18.7% in September). Going forward, economic growth is expected to decelerate further as a result of tighter monetary policy and more stringent financial regulation. We forecast real GDP to increase by +6.7% in 2017 and +6.3% in 2018.

What to watch

- November 9 – Germany September foreign trade
- November 9 – Mexico October inflation
- November 10 – France Sept. industrial production
- November 13 – Russia Q3 GDP (preliminary)
- November 13 – Turkey September BOP
- November 14 – Brazil September retail sales
- November 14 – China October industrial production
- November 14 – China October retail sales
- November 14 – Eurozone & EU Q3 GDP (preliminary)
- November 14 – Germany Q3 GDP (preliminary)
- November 14 – Italy Q3 GDP (preliminary)
- November 14 – U.S. October consumer prices
- November 14 – U.S. October producer prices
- November 14 – U.S. October retail sales
- November 15 – Canada Oct. Teranet home price index
- November 15 – Colombia Q3 GDP (preliminary)

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