

FIGURE  
OF THE WEEK

+38,000

U.S. jobs  
created in May  
(+160,000  
expected)

## In the Headlines



### Eurozone: Consumption drives half of Q1 GDP growth

Q1 real GDP growth was revised upwards by +0.1pps to +0.6% q/q. Moreover, Q4 2015 growth was revised up to +0.4% q/q, from +0.3%. Exports had been the main growth driver through 2015, but consumption and corporate investment are now on a positive trend. Indeed, approximately half of the growth in Q1 GDP was driven by consumer spending, while company investment also increased at quite a strong pace for the second consecutive quarter (+0.9% q/q after +1.5% in Q4 2015). However, net exports acted as a drag on growth for the third consecutive quarter, as imports (+0.8% q/q) increased more rapidly than exports (+0.4% q/q). For the latter, growth was the weakest since Q1 2013, reflecting recent EUR appreciation and also weakness in external demand, notably in the emerging markets. In Q2, we expect a slightly softer growth momentum, with GDP likely to increase by +0.3% to +0.4% q/q as advanced indicators point to growth moderation. Overall, we expect GDP growth will fail to accelerate in 2016 and will increase at the same pace as in 2015 (+1.6%).



### U.S.: Widespread weakness, Fed on hold again

The May employment report was very disappointing, with only +38,000 jobs created, compared with expectations of around +160,000. May's job creation was the lowest since September 2010 and, in addition, the previous two months were revised down a total of -59,000. Job levels have contracted for three consecutive months, while the labour force has fallen by -820,000 in the past two months. Partially as a result, Fed Chair Janet Yellen gave a very dovish speech, suggesting there will not be a June interest rate hike and sharply lowering the odds on a July increase. Other negative news included: (i) manufacturing ISM increased in May but is still weak at 51.3 and the services ISM fell -2.8 to 52.9; (ii) the trade deficit widened in April, to -USD37.4bn, from -USD35.5bn; (iii) core factory orders fell -0.6% m/m and -4.4% y/y in April; (iv) construction spending, which had previously been strong, fell -1.8% m/m in April, the most since January 2011; and (v) productivity was down an annualised -0.6% q/q in Q1, the second consecutive fall, and +0.7% y/y, compared with a long-term average of +2.3%.



### South Africa: Status quo

The country retained its investment grade when S&P ratings agency this week did not move it to "junk" status, as had been widely reported as probable. The immediate market reaction to the "reprieve" was positive (but of uncertain duration); the ZAR strengthened by more than +3% and yields on government long bonds fell -14bps to 9.17%. However, attention now turns to Fitch, which may put South Africa on negative outlook (currently stable) after downgrading it in December 2015. In May, Moody's kept South Africa two levels above "junk" status, but with review for a downgrade. Moreover, S&P will review South Africa again in December, so the current reprieve from "junk" status and all that it entails (including negative investor outlook and higher borrowing costs) may not last long. It is difficult to see how the poor economic performance can be turned around in that time, although there is a window of opportunity for policymakers to make some encouraging moves. However, political tensions ahead of, and during, August's local elections may limit gains from positive policy announcements.



### Brazil: Recession eased in Q1

Real GDP contracted by -0.3% q/q in Q1 (-5.1% y/y), after -0.8% q/q in Q4 2015 (-5.9% y/y). Overall, real GDP has fallen -7% since its most recent peak in 2014 and is now back at its 2010 level. Contraction in private consumption deepened in Q1, to -1.7% q/q after -0.9% in Q4 2015. Consumers find themselves in a perfect storm, conditions that will continue in the coming months amid persistent inflationary pressures (9.3% y/y in April), rising unemployment (11.2% in April), slowing wage growth and tight financing conditions (interest rates reached 70% for non-earmarked credit for households). Investment continued to contract in Q1 (-2.7% q/q, after -4.8% in Q4 2015) and was down -25% from its latest peak in January 2014. Net exports contributed positively to overall growth in Q1 (+1.5pps) as exports rebounded strongly (+6.5% q/q) – perhaps driven up by the lifting of capital controls in Argentina in December 2015 – while imports continued to fall (-5.6% q/q). Overall, we expect the economy will contract by -3.5% in 2016.

# Countries in Focus

## Americas



### Peru: Surprising (and still uncertain) election result

Pre-election opinion polls had showed that Keiko Fujimori was favourite to win the second round of presidential elections. However, with 98.7% of the votes counted, Pedro Kuczynski (50.17% of the votes, compared with Fujimori's 49.83%) appears as the likely winner. Final results should be available on Thursday. Both candidates are from conservative parties and have campaigned on security issues as violence is one of the main concerns of the population. Both have also promised to invest in infrastructure. Fujimori is a somewhat controversial candidate as she is the daughter of former-president Alberto Fujimori (1990-2000), currently imprisoned for alleged crimes against humanity. Kuczynski, an ex-finance minister, is perceived as more pro-business and likely to pursue the reform agenda launched by the incumbent President Ollanta Humala. Annual average GDP growth over the past five years (+5.4%) was markedly above that of the region (+1.7%).

## Europe



### Eurozone: ECB back to wait-and-see

The ECB left all its policies unchanged - interest rates, QE programme and liquidity measures. The Corporate Sector Purchase Programme (CSPP) and the TLTRO II (designed to boost lending to the real economy) will be implemented on 8 June and 22 June, respectively, and the ECB is expecting further stimulus from these measures. With inflation likely to remain below target (2%) through to 2018, the ECB is prepared to expand the size of these programmes, particularly the CSPP, and their duration. We expect the CSPP will represent 12% of total QE, which now stands at EUR80bn/month. Recent credit conditions and economic data show some improvement but the outlook is uncertain: inflation is expected to average +0.2% in 2016 (low oil prices), low employment recovery and associated muted wage pressures. We expect GDP will grow at the same pace as in 2015 (+1.6%) and that the ECB will announce new easing measures by year-end, probably towards late autumn.

## Africa & Middle East



### Saudi Arabia: Transformational leadership

The National Transformation Program (NTP) was formally unveiled this week. It is a five-year plan (2016-2020) that provides some detail to the outline Vision 2030 plan announced earlier (see [WERO 11 May 2016](#) and [WERO 27 April 2016](#)). Unlike previous development plans, the NTP gives specific objectives and measures of success (key performance indicators, KPIs) for the agencies responsible for implementation and delivery. Key objectives to be reached by 2020 include: increasing government non-oil revenues by +USD98.4bn, creation of an additional +450,000 jobs, increasing non-oil exports by +USD39bn, reduction of -SAR200bn in water and electricity subsidies and improvement in the country's World Bank ranking in relation to contract enforcement, to 50 from the current 85. The NTP also specifies the potential introduction of income tax (including residents) and of registration fees for real estate properties and real estate profits. A challenging outlook, but the plan is taking shape.

## Asia Pacific



### China: More tightrope walking

Latest data suggest a difficult transition and moderation in the pace of growth; industrial recovery appears to have halted in April-May, reflecting a more moderate credit expansion and weak external demand. Indeed, USD-denominated exports contracted further in May (-4.1% y/y from -1.8% y/y in April) with decreases in demand in the U.S. (-12% y/y) and EU (-2.1%). This subdued performance is likely to persist in the short term as manufacturing surveys continue to signal sluggish export orders and some countries are implementing anti-dumping measures against Chinese steel makers. China will again have to rely on its domestic market to spur growth. For now, fundamentals remain encouraging. Household incomes are increasing and consumer confidence is recovering. Business surveys indicate that the services sector is still in expansion (Caixin Services PMI at 51.2). The relaxed fiscal stance will also provide some momentum in Q2. EH expects GDP growth will slow to +6.5% in 2016.



## What to watch

- June 08-15 – Eurozone May inflation
- June 09 – South Africa April mining output
- June 09 – Germany April trade balance
- June 09 – UK April trade balance
- June 09 – Venezuela Q1 GDP
- June 10 – Canada May employment report
- June 10 – France April IP & manufacturing production
- June 10 – Italy April industrial production
- June 10 – Mexico April IP & manufacturing production
- June 12 – China May IP, retail sales & fixed asset invest.
- June 14 – U.S. May retail sales
- June 14 – Eurozone April industrial production
- June 14 – Brazil April retail sales
- June 14 – Brazil June industrial confidence
- June 15 – U.S. May industrial production
- June 15 – U.S. Federal Reserve policy statement
- June 15 – Ireland Q1 GDP (first estimate)
- June 15 – Brazil April economic activity

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