Euler Hermes Economic Research

Weekly Export Risk Outlook

29 June 2016

FIGURE OF THE WEEK

USD1,324

Gold price per ounce (+12.6% y/y)

In the Headlines

UK: What next?

At a European Council meeting yesterday, with the UK present for the last time, EU leaders asked for the UK's EU exit process to be "orderly". This should allow a more rapid change of leadership in the UK, with the new Prime Minister likely to be elected at the Conservative Party convention at the start of September. Incumbent PM David Cameron reiterated his plan to leave it for his successor to trigger Article 50 of the EU Treaty, which allows for the start of negotiations about an exit. The second day of the European Council, taking place with only 27 Heads of State, should help forge a common negotiation stance. Despite financial market pressure easing somewhat, with FTSE losses since the Brexit vote -3% (28 June), some sectors, including financials, automotive, construction and retail, are recording strong losses. Volatility is expected to remain high, given the prolonged period of uncertainty. Recession risk in H2 in the UK is high. Indeed, GBP depreciation will impact purchasing power, while investment is expected to take a hit. Import prices in the UK are expected to increase and volumes to adjust lower, moderately impacting Eurozone countries in 2017, with a fall of -0.1pps of GDP growth.

Spain: Political deadlock may not be resolved

After the failure to produce a government following elections in December 2015, new general polls were held last Sunday. The People's Party (PP) was confirmed as the political organisation with most parliamentary seats (137 out of a total 350), obtaining an additional +14 seats compared with December. Although it remains the second largest political force with 85 seats, the socialist party (PSOE) disappointed, losing -5 seats from December's elections. The centre-right Ciudadanos, which surprised in the previous elections with 40 seats, also lost support and obtained only 32 seats. Moreover, the hard-left did not gain strength as the Podemos Unidos coalition obtained 71 Congressional seats, the same number as in December. Despite these results and changed distribution of seats, the political deadlock may not be entirely resolved as no single party obtained an absolute majority in Congress. We estimate that political uncertainty will reduce real GDP growth by -0.3pps in 2016 and the economy will expand by +2.6% overall, after +3.2% in 2015.

Ghana: Too early to suggest return of a success story?

Provisional data show GDP growth in Q1 was +4.9% y/y (+4.1% in Q4 2015), driven by services (+8.8%, boosted by the power, water and communications sub-sectors) and agriculture (+2.8%, crops and cocoa), which offset contraction in industry (-1.1%, gold output declined and oil output from the Jubilee field was below target). The services sector accounts for around 60% of overall GDP and industry over 27%. We forecast overall GDP growth of +5% in 2016, compared with a government target of +5.4%, representing a bounce back from around +4% in 2014 and 2015. Ghana currently has an IMF three-year Extended Fund Facility through to April 2018 that supports an economic reform agenda but there are some concerns that policy drift could become evident ahead of the November elections. Indeed, President John Mahama announced plans to lower electricity prices following public demonstrations relating to sharply higher tariffs. If stability is maintained around election time, EH expects GDP growth will increase to +7.5% in 2017, with associated commercial opportunities.

Jordan: Supporting act

The IMF and local authorities reached a staff-level agreement for a three-year Extended Fund Facility. If, as seems likely, this receives approval from the Fund's board in July it will also unlock the way for wider donor loans and grants aimed at supporting the economy at a time when it is challenged by large-scale refugee inflows. The IMF facility will also support Vision 2025, Jordan's 10-year economic planning framework, one pillar of which is to reduce public debt from around 94% of GDP currently to approximately 77% by 2021. The Fund recently noted that Jordan's currency peg "has served the economy well" and we do not envisage a change in the exchange rate system in the short term. This week's car bombing on the northern border with Syria was a reminder of the country's regional risk perspective and some trade disruptions have been reported, although the business environment remains relatively supportive. We forecast GDP growth of around +2.5% in 2016 and +3% in 2017.

Countries in Focus

Americas

Venezuela: Political crisis and economic collapse

With shortages of food and basic goods increasing, the country is on the brink of economic and social collapse. The outlook is extremely negative: GDP will contract by around -10% in 2016; inflationary pressures are not abating (above 1,000% this year); and social discontent continues to mount. The political opposition accuses Maduro's government of responsibility for the country's slump and has launched a petition that could lead to a referendum to remove the president. A first petition was declared invalid by the National Electoral Council (CNE) on 10 June and a new one was launched. Petitioner identity will be checked by the authorities to avoid fraud. The CNE will have until 26 July to decide whether the new petition is valid. If it does, the referendum could be held as soon as early 2017. To remove the president, an equal or greater number of votes than Maduro received in the 2013 elections (7.5mn) need to be in favour of his recall. In this case, new elections will take place.

Europe

Germany: Sentiment improved ahead of Brexit

The Ifo Business Climate Index climbed to a seven-month high in June, to 108.7 (107.8 in May) with both the current (114.5 from 114.2) and expectations component (103.1 from 101.7) rising. This is in line with increases in the headline ZEW Economic Sentiment Expectations Index to 19.2 (from 6.4 in May) and the ZEW Present Sentiment Index to 54.5 (from 53.1). Moreover, the GfK Consumer Climate Indicator increased to 9.8 in June (from 9.7) and is forecast at an 11-month high of 10.2 in July. Meanwhile, the June flash PMIs remained markedly above the 50.0-threshold indicating expansion, with the Composite Output Index slightly down to 54.1 (from 55.1) as a result of a decrease in the Services Activity Index (53.2 from 55.2) while the Manufacturing Output Index improved to a 26-month high of 55.7 (53.3). EH expects sentiment indicators to fall and perhaps overreact next month in response to the Brexit decision but maintains, for now, its forecast of +1.7% real GDP growth in 2016.

Africa & Middle East

Bahrain: Rain check?

Last week, a prominent Shia cleric, Sheikh Isa Qassim, was stripped of his citizenship for allegedly serving foreign interests. Earlier in June, the government suspended and confiscated the assets of al-Wefaq, a Shia opposition organisation, which the authorities accuse of perpetrating "terrorism, extremism and violence". Given the country's religious character (Shia majority governed by a Sunni minority) and recent history (Saudi Arabia sent troops to prevent an Arab Spring uprising in 2011) this appears to be an escalation of the wider regional power rivalry between Shia and Sunni forces. It is potentially a high risk development as sectarian divides appear likely to intensify. There are other factors in this potent mix; Bahrain hosts the U.S. Fifth Fleet, the UK is expanding its naval base and the economy depends on sectors including finance, which is subject to volatile flows. Prevailing headwinds from low oil prices and heightened stability concerns may limit commercial opportunities.

Asia Pacific

South Korea: Stimulating growth

The government launched a KRW20trn budgetary plan (equivalent to 1.2% of GDP) to spur anaemic growth and stabilise financial markets. The objective is to improve job creation and support regional economies hindered by corporate restructuring. External uncertainties are expected to grow with the UK's decision to leave the EU. The budget plan follows a policy interest rate cut of -25bps in mid-June. These stimulus measures are deemed necessary because GDP growth slowed to +2.8% y/y in Q1 (from +3.1%), deflationary pressures are still elevated (producer prices -3.1% y/y in May) and consumer price inflation is low. Indicators point to fragile growth in the short term, with low confidence (Nikkei Manufacturing PMI 50.1 in May). Modest demand pick-up in high income countries and China suggest a weak outlook for exports. Further fiscal and monetary support measures are likely to foster domestic demand. Euler Hermes expects growth will slow to +2.5% in 2016 (+2.6% in 2015).

What to watch

- June 30 – Eurozone & Poland June CPI
- June 30 – France May consumer spending
- June 30 – Germany May retail sales
- June 30 – UK Q1 GDP (third estimate)
- June 30 – Romania interest rate decision
- July 01 – Eurozone June manufacturing PMI
- July 01 – Eurozone May unemployment
- July 01 – Japan May unemployment
- July 01 – Spain June manufacturing PMI
- July 01 – Peru June CPI
- July 01 – Brazil June manufacturing PMI
- July 04 – Eurozone July Sentix investor confidence
- July 04 – Turkey June inflation
- July 05 – Eurozone June service & composite PMI
- July 05 – Russia June inflation
- July 06 – Poland interest rate decision
- July 06 – Germany May factory orders

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