

FIGURE  
OF THE WEEK

23

June date of  
the UK's EU  
referendum

## In the Headlines



### UK: Eyes turn to the referendum on 23 June

PM David Cameron reached consensus with EU counterparts on the UK's reform requests ahead of a referendum on its EU membership. The deal includes: (i) an "emergency" brake usable for seven years to suspend in-work social benefits to EU workers for a four-year period and under special conditions; (ii) ability to abide by new specific provisions from the single rulebook on financial regulation; and (iii) acknowledgement that the UK is not committed to further EU political integration. The question at the 23 June referendum will be "Should the United Kingdom remain a member of the European Union or leave the European Union?". We continue to expect the UK will remain in the EU (even if by a narrow margin). However, the fears of a UK exit from the EU will affect sentiment and possibly delay investment decisions (see EH's [Economic Insight 30 November 2015](#)). We expect the negative impact will be highest in Q2 but it is already visible in declining portfolio investment (-GBP85bn since Q2 2015, with a potential Brexit explaining around 40% of the fall and the rest reflecting the general economic environment (including GDP slowdown, dovish monetary policy and external headwinds). We expect GDP growth will slow to +2% in 2016, from +2.2% in 2015, and to +1.9% in 2017.



### China: It's complicated

USD-denominated exports contracted further in January (-11.2% y/y from -1.4%) and producer prices contracted for the 47<sup>th</sup> consecutive month (-5.3% y/y). Total Social Financing, which is a measure of aggregate financing flows, increased to RMB3.4tn (from RMB1.8tn in December 2014). Banks issued RMB2.5tn of new loans. While this surge is partly due to seasonal factors (liquidity injection ahead of the Lunar New Year holidays) it also reflects a more accommodative PBoC monetary stance. In the short term, this could support firm domestic demand growth in Q1. In the longer term, a sustained increase of this magnitude, particularly if it is directed at companies, increases the need for deleveraging. Corporate debt is already around 160% of GDP, industrial profits were down -2.3 y/y in 2015 and growth in insolvencies in 2016 is forecast at +20%. We expect the authorities will step up fiscal support (deficit target of -3.5% of GDP, at least) with further tax cuts and more fiscal spending for infrastructure and social welfare. GDP growth may decelerate but is likely to remain around +6.5%.



### U.S.: A hint of inflation

A leading index of consumer confidence fell from 97.8 to 92.2 in February, driven by "turmoil in the financial markets". Existing home sales increased by +0.4% m/m in January, to the second highest level in nine years, and by +11% y/y. Median prices slipped -3.2% m/m (+4.8% y/y). Housing starts and permits fell by -3.8% m/m (+1.8% y/y) and -0.2% m/m (+13.5% y/y), respectively. The homebuilder sentiment index fell in February from 61 to a still strong 58, but it was the lowest since May 2015. Meanwhile, two regional Fed manufacturing surveys continued to signal contraction, but manufacturing industrial production gained +0.5% m/m in January (+1.2% y/y). The gain was driven by a sharp +2.8% m/m increase in motor vehicle production and by a very strong +6.2% y/y. Consumer prices were flat, but the core rate (excluding food and energy) gained +0.3% m/m. On a y/y rate, core CPI is now 2.2%, the highest since June 2012, and markedly above last January's 1.6%. Core producer prices gained +0.4%, but the y/y rate remained at a low +0.7%.



### Eurozone: Softer business confidence. Don't panic!

Preliminary estimates of February PMI signal a mild slowdown in overall activity, with the composite PMI at 52.7 (-0.9pps), the third consecutive month of deceleration since a four-year peak of 54.3 in December 2015. This stems mainly from weakness in the manufacturing sector, with the PMI down to 51.0 from 52.3 the previous month and 53.2 in December. The services sector showed stability, with the PMI at 53.0 (53.6 in January). While **France's** composite PMI registered contraction in February, at 49.8 from 50.2 in January – reflecting weaker services, 49.8 from 50.3 – the overall picture is one of recent relative stability. In contrast, **Germany** showed significant weakening in manufacturing, down to 50.2 from 52.3 in January and 53.2 in December. New orders in the manufacturing sector increased at the slowest pace since July 2015, while new export orders increased only marginally, pointing to difficulties for exporters with exposure to the emerging markets. We expect Eurozone GDP growth will be modest in 2016, probably slightly weaker than the current forecast of +1.7% (+1.5% in 2015).



EULER HERMES  
Our knowledge serving your success

# Countries in Focus

## Americas



### Argentina: Unblocking the path to international capital markets

President Mauricio Macri's negotiations to solve the conflict with debt 'holdouts' appear to have paid off. Thomas Griesa, the U.S. judge who first ruled that the country should not be allowed to pay off its restructured debt before it paid the "holdout" part - the 7% that had not been renegotiated in 2005 and 2010 - recently accepted a move to lift restrictions preventing the country from accessing capital markets. However, this comes with two conditions. First, the Argentinian Congress must repeal a law that was passed in the restructuring period that prevents the government from paying its holdout debt. Second, Argentina must reimburse the entire holdout debt to hedge funds before 29 February. Macri made an offer of USD6.5bn but the total sum involved is USD9bn. Two of the six biggest U.S. hedge fund creditors accepted this offer. Moreover, since the recent U.S. court ruling, those that rejected it have now lost some leverage power and may soon follow suit.

## Europe



### Germany: Strengthening domestic vs. weakening external demand

Q4 2015 real GDP increased by +0.3% q/q, matching the pace in Q3 and slightly below the +0.4% average during H1. Growth was driven by domestic demand, notably government spending, which was up by +1% q/q while private consumption eased to +0.3% q/q. Fixed investment beat expectations at +1.5% q/q, supported by strong public investment. Net exports subtracted -0.5pps from Q4 2015 q/q growth as exports declined by -0.6% q/q while imports increased by +0.5% q/q. Meanwhile, the Ifo Business Climate Index fell to 105.7 (from 107.3 in January) marking the third consecutive month of decline and a 14-month low. The sharp fall reflects a drop in the expectation component to 98.8 (from 102.3) that offset a slight improvement in the current situation component to 112.9 (from 112.5). Euler Hermes expects the opposing forces – strengthening domestic demand and weakening external demand – will continue in H1 and forecasts full-year GDP growth of around +1.8% in 2016.

## Africa & Middle East



### South Africa: Will safe fiscal hands protect investment status?

Today's state budget showed a certain amount of resolve to tighten the fiscal environment and thereby ease some of the pressures building for a downgrade by credit rating agencies (see also [WERO 3 February 2016](#)). Cabinet reshuffles at the end of last year signposted that fiscal policy was likely to be sound and relatively independent (see also [WERO 17 December 2015](#)). FM Pravin Gordhan did not opt for dramatic policy changes but announced tax increases projected to add ZAR18bn to revenues and a cut of ZAR10bn in the overall annual spending ceiling, although with increased expenditure on education, infrastructure and social protection. Official projections now indicate that the budget deficit will fall to -2.4% of GDP in FY2018/19 from -3.2% in FY2016/17 and the Treasury's revised GDP growth forecast for 2016 is +0.9%, compared with +1.3% in 2015. Whether these targets are reached may depend on the rating agencies' reactions, which are not clear cut. Challenging times.

## Asia Pacific



### Hong Kong & Singapore: Trade hubs under pressure

GDP growth in **Singapore** was revised slightly down to +2% in 2015 (+2.1% in the previous estimate). Manufacturing contracted by -5.2%, in line with lower exports (-7.2% for merchandise goods) and services expanded by +3.4%. Meanwhile, preliminary estimates indicate that lower growth in **Hong Kong** in Q4 2015 (+1.9% y/y, +2.2% in Q3) resulted in a full-year average of +2.4% (+2.6% in 2014). Downside risks have increased for both countries, with insolvencies in 2016 set to increase by +15% for both. GDP growth is likely to remain modest (around +2%), significantly below long-term averages (+6% for **Singapore**, +4% for **Hong Kong**). Export opportunities are limited, reflecting China's slowdown and only moderate improvement in demand growth in high-income economies. Export growth of financial services will be challenging and the two markets will rely on domestic demand to spur growth. Expect further public support to maintain private sector demand.



## What to watch

- February 25 – Germany Feb. GfK cons. confidence
- February 25 – Brazil January unemployment
- February 25 – U.S. January durable goods orders
- February 25 – Italy bus. & consumer confidence
- February 25 – UK Q4 GDP components
- February 26 – France Q4 GDP & February CPI
- February 26 – Croatia & Slovenia Q4 GDP growth
- February 26 – U.S. Q4 GDP & Jan. income/spending
- February 26 – Iran elections (including parliamentary)
- February 26 – Germany & Spain February CPI
- February 26 – Mexico January unemployment
- February 26 – Ireland general elections
- February 29 – Poland & Sweden Q4 GDP
- February 29 – Germany January retail sales
- March 01 – Russia & Turkey Feb. PMI manufg.
- March 01 – Canada Q4 GDP
- March 01 – U.S. February ISM manufacturing
- March 02 – Spain February unemployment
- March 03 – Brazil Q4 GDP
- March 03 – France Q4 unemployment

## DISCLAIMER

These assessments are, as always, subject to the disclaimer provided below.

This material is published by Euler Hermes SA, a Company of Allianz, for information purposes only and should not be regarded as providing any specific advice. Recipients should make their own independent evaluation of this information and no action should be taken, solely relying on it. This material should not be reproduced or disclosed without our consent. It is not intended for distribution in any jurisdiction in which this would be prohibited. Whilst this information is believed to be reliable, it has not been independently verified by Euler Hermes and Euler Hermes makes no representation or warranty (express or implied) of any kind, as regards the accuracy or completeness of this information, nor does it accept any responsibility or liability for any loss or damage arising in any way from any use made of or reliance placed on, this information. Unless otherwise stated, any views, forecasts, or estimates are solely those of the Euler Hermes Economics Department, as of this date and are subject to change without notice. Euler Hermes SA is authorised and regulated by the Financial Markets Authority of France.

© Copyright 2016 Euler Hermes. All rights reserved.