24 April 2013

In the Headlines

FIGURE OF THE WEEK: USD100.3 >BARREL PRICE OF BRENT OIL (-15.5% Y/Y)

Eurozone: Surprising fall in German business confidence

Business confidence remained stable in April, with the PMI Composite Index at 46.5, a level still suggesting contraction in the manufacturing and services sectors, evident since August 2011 and February 2012, respectively. The German manufacturing PMI came in below expectations at 49.7, ending a four-month period of expansion, and confidence in the services sector also disappointed, falling below 50 for the first time in five months (49.2, against consensus expectations of 51). In contrast, in France, the rates of decline in both the services and manufacturing sectors continued to ease. Indeed, both the manufacturing and the services PMIs came in above expectations, at 44.4 and 44.1, respectively, although they remain at very weak levels. Overall, the surveys continue to suggest falling output across the zone (albeit at a slower pace), partly reflecting weak domestic and export orders. EH revised downwards its eurozone GDP growth forecast for 2013, by -0.2pps to -0.3%, as the current expectation is that stabilisation in economic activity will not be apparent until towards the end of the year.

US: Strong housing market

The housing market remained the brightest spot in the economy in March, with starts increasing by +46.7% y/y and permits by +17.3%. Sales of existing single-family homes were up +9.1% y/y and new home sales were up a strong +18.5%. Prices for existing homes were up by a robust +12.1% y/y, while growth in prices in the much smaller new-home market slipped to +3% from +18.2% in December 2012. Supply for both existing and new houses is very tight, at 4.7 and 4.4 months, respectively. Such a strong performance in the housing sector is a current positive, although it raises concerns that the market may be artificially inflated by professional investment groups and others that are taking advantage of the Fed's easy money policy.

Brazil: Interest rates increased

With March y/y inflation moving beyond the upper bound of the target range (6.6% against 4.5% +/-2%) and expectations for the end of 2013 still at the upper end, the central bank last week raised the policy interest rate by 25bps, to 7.25%. This shifts the focus firmly away from growth, although GDP is unlikely to increase by more than +3% this year and indicators in the early months have not been strong. A short tightening cycle now seems likely, although rates should remain historically low. Meanwhile, the government is seeking to create more fiscal leeway by committing itself to the same overall primary fiscal surplus target this year (+3.1% of GDP) but without obligation of the central government (target +2.2%) to offset any shortfall in the non-central government surplus.

Tunisia: IMF support

On 19 April, the Fund reached a staff-level agreement with the country for a Stand-By Agreement (SBA) of USD1.75 billion. If approved by the IMF board, which seems likely, the facility will be in place for a period of 24 months, with disbursements made over the same period. An IMF facility will provide timely support during this stage of the political transition and it acts as a bellwether for the donor and investor communities at large. Even so, the challenges remain significant, with stability and security still not assured. As recently as February, a political assassination introduced further uncertainty and led to a reconstituted moderate Islamist-led government. Moreover, political and social uncertainties—the constitution is being redrafted and elections are expected in October-November—come at a time when the economy remains affected by weak external markets (Europe accounts for over 70% of exports and over 50% of imports and is a major source of tourism). EH forecasts GDP growth of +3% in 2013 and +4% in 2014, still below the recent long-term annual average of +4.4% (2000-10).

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Countries in Focus

Mediterranean, Africa & Middle East – *Nigeria: Security*

Intense fighting in the north between the armed forces and militant Islamists—including use of rocket-propelled grenades—with associated heavy loss of civilian life suggest an escalation in the conflict with rebel groups, including Boko Haram, which seeks an Islamic state in northern Nigeria. The timing of this event, immediately prior to the inauguration of a committee to discuss an amnesty deal for Boko Haram, raises questions over the federal government's ability to control the northern part of the country and, perhaps, parts of the military. In addition, tensions persist in the oil-rich Niger delta region where substantial crude oil output continues to be lost to criminal activity. Even so, annual GDP growth has not fallen below +6% since 2005 and EH forecasts +7% in 2013 and +6.5% in 2014.

Americas – *Paraguay: Election result*

Colorado Party (CP) candidate Horacio Cartes comfortably won the presidential elections held last Sunday, with 45.8% of the vote against 36.9% for his nearest rival, Efrain Alegre of the ruling Authentic Liberal Party (PLRA). Cartes' election is likely to herald Paraguay's return to Mercosur and other regional and international bodies from which it was suspended following the ousting of former president Fernando Lugo. Cartes, a political newcomer, is likely to be pro-business and relatively orthodox in terms of economic policies, but how reformist remains to be seen. Preliminary results suggest that the CP (19 of 45 seats) will not have a majority in the Senate, although it will in the lower house. The president-elect should benefit from a strong economic rebound this year, after GDP contracted in 2012.

Asia-Pacific – *Thailand: Monetary policy & update*

The Monetary Policy Committee (MPC) left the key policy interest rate unchanged at 2.75% in April. Headline inflation fell to 2.7% y/y in March from 3.3% in February and core inflation eased to 1.2% in March from 1.6% a month earlier, comfortably within the monetary policy target range of 0.5-3.0%. The MPC expects inflation to remain contained in the near future and the economy to moderate to a normal trend, following the post-flood recovery that boosted real GDP growth to +6.4% in 2012. However, the weak state of the global economy poses some downside risk to growth. In February, manufacturing output fell by -1.2% y/y (+10.1% in January) and nominal exports declined by -4.6% y/y (+15.6% in January). Expect some monetary easing if growth decelerates more than projected.

Europe – *Slovak Republic: Outlook*

Real GDP increased by +2% in 2012, making the Slovak Republic the second-fastest growth economy in the eurozone (after Estonia). Domestic demand was weak, however, and net exports were the sole growth driver as exports were up +8.6% while imports increased by just +2.8%. The current account posted the first annual surplus (2.3% of GDP) since 1995. New capacity in the automotive sector supported industrial production and exports in 2012, mitigating the impact of weakening eurozone demand, although this effect will wane because of the growth slowdown (+0.7% y/y in Q4 2012). Moreover, in January-February 2013, turnover contracted in major sectors, including industry (-2% y/y), construction (-5.1%) and retail trade (-1.6%). Expect GDP growth to ease to around +1.2% in 2013.

Worth knowing

China

The April flash manufacturing PMI (HSBC/Markit) was 50.5, still in positive territory, but down from 51.6 in March.

European Central Bank

The Q1 2013 Lending Survey suggests that credit standards for NFC loans improved slightly (and are expected to remain stable in Q2) because of improving financing conditions for eurozone banks and lower risk perceptions related to economic activity and industry specific risks. Banks reported unchanged net declines in the demand for loans to NFC reflecting the negative impact of fixed investment on firms' financing needs, but expectations point to a less negative decline in demand for loans to NFC.

Kuwait

The surplus in the external merchandise trade account increased by +20.7% in 2012, to a record USD92.6 billion, equivalent to around 54% of GDP, another record. Exports of goods totalled USD118.5 billion in 2012 (oil accounted for 95% of the total).

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