Euler Hermes Economic Research

Weekly Export Risk Outlook

4 December 2013

FIGURE OF THE WEEK

6.64bn

Portugal's EUR bond exchange

In the headlines

Ukraine: Mass protests, country risk already very high

Anti-government protests that were triggered by a government decision on 21 November not to sign an EU Association Agreement strengthened over the past week, supported by the main opposition parties. The protests are likely to continue for some time but the government of President Yanukovych is unlikely to fall. This week it easily survived a no-confidence motion in parliament tabled by the opposition. However, the decision against the partnership deal with the EU closed an opportunity to improve Ukraine's persisting precarious economic situation. The country has been in recession since mid-2012. EH forecasts that real GDP will contract by -1.5% in 2013 and by -2% in 2014. External liquidity risks have been rising since an IMF stand-by programme went off track in April 2011. Continued central bank intervention to defend the quasi-fixed exchange rate, which has faced considerable downward pressure over the past two years, reduced FX reserves to USD19 billion in October, down 49% from an all-time high in April 2011. FX now covers only two months of imports. As around USD10 billion in external debt is maturing in 2014, Ukraine now needs to forge an agreement on financial support from Russia, otherwise a renewed sharp exchange rate correction and balance of payments crisis cannot be ruled out in 2014.

Portugal: Successful bond exchanges

On 4 December, Portugal exchanged EUR6.64 billion in bonds maturing in June and October 2014 and October 2015 for bonds maturing in October 2017 and June 2018. The amount exceeded expectations and is seen in positive terms by the markets, particularly as Portugal will need to finance its funding needs partially on the bond markets starting in 2014, before full market access scheduled for 2015. The main purpose of the operation is to ease the debt burden in the coming years as it reduces Portugal's funding needs by around EUR2.5 billion in 2014 and by EUR4.1 billion in 2015. In Q2, the Treasury started to pre-fund 2014 borrowing needs (estimated at EUR35 billion) while the privatisation plan is ongoing. However, the government will need to conduct further bond issuance next year as the IMF/EU financial assistance programme is scheduled to end in May-June 2014. Around EUR8 billion of the aid package still needs to be disbursed next year.

US: A grey Black Friday?

Initial reports relating to holiday sales were disappointing. The National Retail Federation (NRF) had forecast sales growth of 3.9% y/y for the entire holiday season but, for the critical Black Friday weekend, sales actually fell 2.7%, the first decrease in seven years. A separate report from ShopperTrak showed an increase of only 1% compared with expectations of 2.4%, the lowest since 2009. Similarly, Consumer Confidence fell 2 points in November; the Expectations component plummeted to 69.3 from 91.1 in June. Meanwhile, recent housing data have been mixed. Pending home sales fell for the fifth consecutive month and existing home sales fell for the fourth time in five months and are now up only 5.2% y/y. However, prices of existing homes moved up marginally and are now +13% over last year and permits increased for the second consecutive month and are now up 14% y/y. On a final bright note, the ISM manufacturing index increased for the sixth consecutive month, led by new orders. The data are mixed, with the disappointing holiday sales perhaps the critical indicator.

Denmark & Sweden: Recovering domestic demand

After contracting in Q2 (-0.1% q/q), **Sweden's** GDP turned positive in Q3 (+0.1%), driven by external trade that contributed +0.1% to overall growth, while domestic demand remained stable. However, the trade data reveal that both exports and imports contracted. Domestic demand excluding inventories was quite strong (+0.7%) reflecting a significant increase in investment (+2.5%), improving private consumption (+0.3%, similar to Q2) and expanding public spending (+0.1% after +0.3% in Q2). EH expects GDP growth of +0.9% in 2013 and +2.3% in 2014 reflecting more favourable terms of trade, a rebound in private investment and growth in private consumption. In **Denmark**, GDP growth slowed to +0.4% in Q3, after +0.6% in Q2, with a large negative contribution from external trade (-1.1%) as imports were strong (+3% q/q) and exports lost competitiveness. Domestic demand growth gained momentum (+1.5%, +0.8% excluding inventories) but ongoing household deleveraging continues to dampen private consumption. Investment increased by +3% after +1% in Q2. Overall, EH expects GDP growth to remain weak in 2013 (+0.4%) and to accelerate moderately in 2014 (+1.4%) driven by domestic demand.

Countries in Focus

Americas

Brazil: GDP contracted in Q3

GDP contracted by -0.5% q/q in Q3, after strong expansion in Q2 (+1.8%). This decline was driven by a fall in investment (-2.2% q/q after +3.6% in Q2) and in exports (-1.4% after +6.8%). As imports contracted only moderately (-0.1%), external trade contributed negatively to overall economic growth. Private consumption gained momentum (+1% after +0.3% in Q2), as did government spending (+1.2% after +0.5%). On the supply side, contraction was driven by a sharp drop in agriculture (-13.2% after +18%) and a slowdown in industry (+0.4% after +9.1%) and in services (+0.4% after +3.1%). Advanced indicators show some positive signs for the end of the year: industrial production accelerated in October (+0.6% m/m after +0.5%) and consumer confidence improved in November (112.8 from 111.7), although business confidence decreased to 49.7 in November, below the expansion threshold. EH expects GDP growth of +2.2% in 2013 (+1% in 2012) but does not expect a significant improvement in 2014, with GDP growth remaining relatively subdued.

Europe

Switzerland: GDP growth remained robust in Q3

Detailed data from the State Secretariat for Economic Affairs show that Q3 real GDP growth decelerated to +1.9% y/y from +2.5% y/y in Q2 but remained steady at +0.5% in q/q seasonally adjusted terms. The expansion of private consumption slowed markedly to +0.2% q/q (+0.6% in Q2) while government consumption picked up to +1.1% q/q (+0.2% in Q2). Investment in equipment contracted by -0.1% q/q in Q3 (+3.5% in Q2) while a recovery in construction investment growth to +1% q/q (flat in Q2) kept overall fixed investment growing by +0.4% q/q (albeit down from +1.9% in Q2). External trade activity moderated sharply in Q3, with exports up by just +0.1% q/q (+0.9% in Q2) and imports declining by -0.4% q/q (+0.9% in Q2), so that that net exports contributed around +0.2pps to Q3 growth. Leading indicators, including the PMI and the KOF economic barometer, point to continued robust growth. EH forecasts full year growth of around +2% in both 2013 and 2014.

Africa & Middle East

Morocco: Financing to cover potential shortfalls

The country may issue a EUR1 billion eurobond, perhaps in early 2014. Morocco is rated BBB- by S&P and Fitch and Ba1 by Moody's and has two outstanding EUR issues due in 2017 (EUR500 million) and 2020 (EUR1 billion), as well as two USD bonds (USD1.5 billion due in 2022 and USD750 million due in 2042). The new bond is expected to be a 10-year instrument and with it Morocco will become the second largest sovereign eurobond issuer in Africa, after South Africa. The issuance reflects the government's needs for budget financing (EH expects a fiscal deficit above-6% of GDP in 2013, after -7.6% in 2012) at a time when fiscal consolidation, partly through subsidy reduction, is challenging. Nevertheless, the economy is relatively diversified, with higher value-added sectors, including automotive, electronics and aeronautical industries and EH expects GDP growth of +4.5% in 2013 and in 2014. Moreover, an IMF Precautionary Liquidity Line provides support, in need.

Asia Pacific

India: Indicators moving in concert

GDP accelerated in Q3, to +4.8% y/y from +4.4% in Q2. Most key drivers showed an improvement, with a marked contribution from the important agricultural sector (+4.6% y/y) after rising production of cereals and oil seeds. Manufacturing increased by +1% y/y after a contraction in Q2 (-1.2%). The strongest performances in Q3 were recorded in the services sector, with "Financing, Insurance and Business" and "Trade, Hotel, Transport and Communication" sub-sectors increasing by +10% y/y and +27%, respectively. Meanwhile, the current account balance improved from a deficit of -5% of GDP (USD21.8 billion) to -1.2% (USD5.2 billion) as a result of a good export performance. Moreover, the latest surveys point to further improvements in the short term. In particular, the HSBC Manufacturing PMI increased above 50 for the first time in four months, to 51.3 in November (from 49.6 in the previous month) reflecting increases in new orders and output.

What to watch

- December 4 – OPEC meeting
- December 5 – Eurozone GDP Q3 (second estimate)
- December 5 – ECB December interest rate
- December 5 – UK October trade balance
- December 6 – Canada November unemployment
- December 6 – Germany October industrial production
- December 6 – UK October industrial production
- December 6 – US November employment report
- December 6 – France October trade balance
- December 6 – US November non-farm payrolls
- December 9 – China new Yuan loans

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