

Weekly Export Risk Outlook

3 September 2014

FIGURE
OF THE WEEK

-0.2%

Germany's
q/q Q2 GDP
contraction

In the Headlines



Germany: Losing momentum

Real GDP contracted by -0.2% q/q in Q2, after growing by +0.7% in Q1. The slightly weaker-than-expected result was largely due to a mild winter, which led to anticipatory effects in the construction sector in Q1, reflected in the drop in construction investment by -4.2% q/q in Q2 (+4.1% in Q1). As a result, gross fixed investment declined by -2.3% q/q in Q2 (+2.9% in Q1). Positive contributions to Q2 GDP were made by inventories (+0.4pps) as well as by private and public consumption, which both grew by +0.1% q/q, although this was down from +0.8% and +0.4% in Q1, respectively. Export growth picked up in Q2 but remained modest at +0.9% q/q (0% in Q1), outpaced by imports at +1.6% q/q (+0.5% in Q1) so that net exports contributed -0.2pps to Q2 growth. Reduced trade activity with Russia has affected external demand; nominal merchandise exports to Russia fell by -15.5% y/y in H1 (-19.7% y/y in June) while imports from Russia increased by +2.1%. In y/y terms, GDP growth decelerated to +1.2% in Q2 from +2.3% in Q1. Against a background of the lost momentum in Q2 and the ongoing heightened tensions relating to Russia and Ukraine, EH revised its full-year growth forecast to +1.5% in 2014 (from +1.9% previously). Meanwhile, a preliminary estimate has put CPI inflation at 0.8% y/y in August, unchanged from July.



China: Not too bad

Latest indicators point to a temporary slowdown in activity in July. Growth in industrial production and retail sales decelerated to +9% y/y (from +9.2% in June) and +12.2% y/y (+12.4%), respectively. Fixed asset investment growth in the first seven months of 2014 was +17% y/y, which is 0.3pps below the rate recorded during the January-June period. This deceleration was driven by a slowdown in investment in the property market and in key manufacturing sectors experiencing overcapacity. However, the lack of momentum should not lead to a hard landing in H2. Firstly, external trade should act as a cushion, as suggested by the strong increase in exports in July (+14.5% y/y from +7.2%). Secondly, domestic demand is expected to strengthen, especially in the services sector; the HSBC Services PMI increased to 54.1 in August from 50.0 in July. The outlook is also supported by a pro-growth policy mix (targeted monetary easing and a rise in infrastructure spending). Against this background, EH maintains its forecast of a gradual easing in GDP growth in 2014 and 2015 (+7.5% and +7.4%, respectively).



Brazil: Technical recession

Official data show that the economy is in technical recession as real GDP contracted by -0.6% q/q (-0.8% y/y) in Q2 while Q1 figures were revised down to -0.2% q/q (compared with +0.2% in initial data). As EH expected, the Football World Cup weighed against investment and growth, mainly as a result of fewer working days, while it fuelled inflationary pressures (+6.5% y/y in July). Investment contracted sharply in Q2 (-5.3% q/q), the fourth consecutive quarter of decline. A slight increase in private consumption (+0.1% q/q) only partially offset the decline in Q1 (-0.3% q/q). In line with this sluggish domestic demand, imports declined, while exports increased by +2.8% q/q, although barely compensating for the fall in Q1. External demand contributed positively overall to GDP growth (+0.7pps). Leading indicators show that a recovery in H2 will be gradual. EH expects GDP growth of +0.4% in 2014. Against this background, economic issues will be decisive in presidential elections scheduled for 5 October. If the elections go to a run-off, several polls show that the opposition candidate, Marina Silva (from the Brazilian Socialist Party) will come ahead of incumbent President Dilma Rousseff.



Eurozone: Fears of deflation are not over

Inflation in August was in line with consensus expectations at 0.3% y/y, down from 0.4% in July, mainly reflecting an intensification of the fall in energy prices (-2% y/y, from -1% in July) and continuation of the decline in food prices (-0.3% and negative for the third consecutive month). Downward pressures on headline inflation reflect the embargo imposed by Russia on food imports from the EU (around EUR12 billion per year of food imports) and the fall in oil prices. Core inflation (excluding food and energy prices) increased by 0.1pps to 0.9% y/y. EH does not exclude a repo or deposit rate cut at the ECB meeting tomorrow, although this is likely to have little effect on the real economy. Indeed, the ECB is likely to wait until the first tranche of TLTRO is given to banks (18 September) before announcing further measures. EH expects ABS purchases with public guarantees to start towards year-end, at the earliest. If recent EUR depreciation continues and credit conditions recover, the outlook for (and expectations of) inflation could improve, although only moderately. EH forecasts inflation at only 0.5% in 2014 and less than 1% in 2015, but with downside risks.



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U.S.: Consumption limits the pace of recovery

Q2 GDP growth was revised up to +4.2% q/q annualised (from +4%), but consumption increased only by +2.5%, compared with a long-term average of +3.3%. Moreover, consumption contracted by -0.2% in July, dragged down by weakness in after-tax income, which increased by a mere +0.05%. However, most other recent data continue to show improvement. After-tax corporate profits staged a major rebound in Q2, gaining +8.3% q/q, after the expiration of a depreciation tax break drove Q1 profits down -16.3%. The August ISM manufacturing index was very strong, up to 59 from 57.1, markedly above the 50 level indicating expansion. New orders were particularly strong at 66.7 (from 63.4). Construction spending in July rebounded +1.8% m/m, compared with a fall of -0.9% in June. The pending home sales index, which leads existing home sales, increased to a strong 105.9 in July (+3.3% m/m). The economy is improving, but is held back by weak consumption and job growth.

Europe



Italy: Signs of stagnation, rather than recovery

The Q2 GDP breakdown shows that the -0.2% q/q contraction resulted largely from net exports (-0.2pps) as there was a strong rebound in imports (+1% q/q) and near stagnation in exports (+0.1%). Domestic demand stabilised after two consecutive quarters of contraction. Private consumption increased by +0.1% q/q, the third consecutive quarter of positive growth. Inventories had a positive contribution on growth (+0.2pps) indicating that companies anticipate a slight pick-up in private consumption in coming quarters. Private investment continued to contract, at -0.9% q/q, while public consumption fell by -0.1%. Private consumption is expected to continue to grow slowly, while the contraction in investment should moderate. Exports are expected to remain soft as a consequence of sanctions imposed on Russia since July. EH revised downwards its GDP forecasts to 0% in 2014 and to +0.9% in 2015.

Africa & Middle East

Lesotho: Coup attempt?

An alleged coup attempt last weekend was symptomatic of a deep political rift in the country. Parliament has been suspended since June and the coalition government is ineffective. When the military surrounded the premier's official residence and some police stations, PM Thomas Thabane fled to neighbouring South Africa. The military reportedly supports Mothetjoa Metsing, Thabane's deputy and political rival. Lesotho is encircled by South Africa and is economically dependent on that country (82% of imports). In turn, South Africa provides an overall stabilising influence on the small kingdom (troops were sent in 1998 after rioting) and will now attempt to diffuse the political tensions. The latter are unlikely to have a serious impact on the textile and clothing sector, which accounts for over 50% of exports and, given South Africa's economic and security dominance and its interests in Lesotho's water and hydroelectric output, the region is unlikely to be destabilised.

Asia Pacific



Australia: Underperforming

GDP increased by +0.5% q/q in Q2 after a strong Q1 (+1.1% q/q). This slowdown was mainly the result of a negative contribution from net exports (-0.9pps q/q). Final consumption expenditure and investment increased by +0.5% q/q and +0.3%, respectively. On the supply side, the breakdown reveals that mining was the main drag on growth (-1.4% q/q). This sector, which accounts for over 50% of exports, continues to be adversely affected by lower global demand, particularly from China. In the short term, the outlook is likely to remain fragile and growth is expected to be moderate (+0.5% q/q on average in H2). Indeed, while monetary policy is favourable, fiscal tightening and advanced indicators continue to point to weak activity levels; manufacturing PMI re-entered contraction territory in August (47.3 after 50.7 in July). Against this background, EH expects GDP will grow by +3% in 2014 after +2.4% in 2013.

What to watch

- September 4 – Eurozone ECB press conference
- September 4 – UK BoE meeting
- September 4 – U.S. July trade balance
- September 4 – U.S. Aug. ISM non-manufacturing index
- September 4 – Saudi Arabia Q2 GDP
- September 5 – Canada August unemployment
- September 5 – Eurozone Q2 GDP (2nd estimate)
- September 5 – Germany July industrial production
- September 5 – U.S. August employment report
- September 5 – Finland Q2 GDP (2nd estimate)
- September 7 – Egypt August international reserves
- September 8 – China August trade balance
- September 8 – Czech Republic August inflation
- September 10 – Croatia Q2 GDP (details)
- September 10 – China August aggregate RMB financing

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