Euler Hermes Economic Research

Weekly Export Risk Outlook

10 September 2014

FIGURE OF THE WEEK

USD99

Barrel price of benchmark Brent crude oil

In the Headlines

Turkey: Slowdown

Q2 real GDP increased by +2.1% y/y (down from an upwardly revised +4.7% in Q1) and contracted by -0.5% q/q (+1.8% in Q1). The sharp slowdown is largely a result of weakening domestic demand, despite monetary policy easing, with private consumption expanding by just +0.4% y/y (+3.2% in Q1), government consumption by +2.4% (+9.2% in Q1) and fixed investment declining by -3.5% (-0.2% in Q1). In addition, external trade moderated, with export growth slowing to +5.5% y/y (+11.1% in Q1), partly reflecting the conflict in Iraq (a key trading partner) and the modest EU recovery, but also because Q1 exports were boosted by one-off gold exports to Switzerland. Imports contracted by -4.6% y/y in Q2 (+0.7% in Q1) so that net exports remained a stable and positive contributor to growth. Monthly data for industrial production, retail trade and the Real Sector Confidence Index suggest that output may remain weak in Q3. EH expects further monetary easing, even though annual inflation has been above 9% since April (9.5% in August), and full-year GDP growth of +3.1% in 2014 and +3.8% in 2015.

Russia: Sanctions begin to take effect

A second estimate of RosStat confirmed that Q2 real GDP increased by +0.8% y/y, after +0.9% in Q1, and added that it increased by +0.2% in seasonally-adjusted q/q terms, slightly up from +0.1% q/q in Q1 (which was revised up from -0.3% q/q previously). RosStat also published production side details, showing a sharp -4.3% q/q drop of the financial sector in Q2 (+4.5% in Q1) as well as continued contraction in real estate (-1.4% q/q) and manufacturing (-0.2% q/q). Construction and trade returned to modest q/q growth in Q2 but continued to decline in y/y terms. Overall, the details suggest that the geo-political tensions over Ukraine have already affected consumer and investor confidence and ultimately the economy in H1. As the West deepened sanctions against Russia in Q3 and the tensions are not expected to subside in the near term, EH forecasts Russia will slide into recession in H2, resulting in a contraction of full-year 2014 GDP of -0.6%. On 8 September, the EU adopted new sanctions that basically extend existing measures – including restricted access to EU capital markets for large Russian state-owned oil companies such as Rosneft, Transneft and Gazpromneft – but said their entry into force will be delayed to leave time to assess whether a ceasefire in Ukraine, agreed on 5 September, is holding.

Eurozone: Positive steps, but no euphoria

In line with EH expectations, the ECB lowered key interest rates by 10bps (refi rate 0.05%, marginal lending facility rate 0.3% and deposit facility rate –0.2%). The ECB surprised positively by announcing an ABS/RMBS and covered bonds purchase programme starting in October, earlier than expectations of year-end. This should boost credit to the private sector and ease financing conditions, especially for SMEs. The programme is likely to benefit most Italy and Spain, given the size of their ABS/RMBS markets. Further measures were not indicated but the intention is to return the ECB balance sheet to its early 2012 size of EUR3 trillion (EUR1 trillion larger than currently). This suggests that monetary policy could become even more accommodative in coming months, with extended/new measures in early 2015 after the results from the ECB AQR and stress tests are published (November) and the tranches of TLTRO are given to banks (approximately EUR400 billion on 18 September and 11 December). The recent depreciation of the EUR is likely to continue, given the rate cuts and ECB balance sheet expansion. In turn, this could improve the inflation outlook and expectations, albeit moderately. EH forecasts inflation at 0.5% in 2014 and less than 1% in 2015, with downside risks, and subdued GDP growth of +0.8% in 2014 and +1.3% in 2015.

U.S.: Labour market weakness continues

The August employment report showed job gains of only 142,000, markedly below expectations of 230,000, the average rate of increase to date in 2014. Data for the preceding two months were revised down 28,000, and the labour force participation rate deteriorated to 62.8% matching recent lows not seen since 1978. The y/y growth rate of average weekly earnings after inflation was 0%. Meanwhile, July factory orders increased by +10.5% m/m but were skewed by aircraft sales; ex-transportation orders were actually down -0.8%. In contrast, the trade deficit fell slightly in July from USD41.5 billion to USD40.8 billion, and the ISM Non-Manufacturing Index improved from 58.7 to 59.6 in August, markedly above the 50 level indicating expansion. The critical new orders component fell slightly but was still very strong at 63.8. Low wage pressure, geo-political uncertainty and a narrowing supply of Treasury securities unexpectedly lowered the yield on the 10-year Treasury note by -60bps since the beginning of the year, to 2.4%, thereby easing pressure on the Fed to start increasing interest rates.

Countries in Focus

Americas

Colombia: Among Latin America's bright spots

Consumer prices continued to accelerate in August, increasing by 3% y/y (compared with 2% in January), mainly driven by food prices, which increased by 3.6% y/y, a high in the past 21 months. After easing in June and July, core inflation picked up again in August, to 3% y/y. EH expects it will moderate progressively in forthcoming months as recent monetary policy tightening begins to take effect. The key policy interest rate was increased to 4.5% in August and is now up by 100bps since April. EH expects average inflation will reach 2.9% in 2014 and 3.3% in 2015, within the official target range of 3% +/-1pps. EH expects strong growth in the real economy, with GDP increasing by +4.9% in 2014 and +4.7% in 2015. These rates compare favourably with the regional average of below +2% in 2014. With steady economic growth and inflationary pressures under control, Colombia remains among the Latin American countries with good prospects for 2014 and 2015.

Europe

The Netherlands: Recovering from economic malaise

GDP growth rebounded by +0.5% q/q in Q2 (after -0.4% in Q1). Net exports were particularly strong (+1.2pps) while domestic demand continued to contract (-0.7pps) reflecting a strong decline in investment (-3.1% q/q). Household consumption picked up slightly (+0.2% q/q). Growth, albeit weak, is expected to recover in 2014 (+0.6%). Net exports will remain the largest contributor to GDP growth in 2014 (+1pps). Increasing capacity utilisation rates of industrial plant and machinery suggest a positive momentum to investment growth. The deterioration in the housing market appears to have come to an end as house prices have been stable in recent quarters and the number of transactions is increasing progressively. In 2015, EH expects GDP growth of +1.2% but it will remain low compared to pre-crisis levels, making it difficult for businesses to grow their topline, given weak price pressures (inflation 0.8% in 2015, after 0.5% in 2014).

Africa & Middle East

Iraq: New government, old problems

A new government is in place, offering hope that some of the country's problems can now be addressed. The government of PM Haider al-Abadi includes representatives of the majority Shia and the minority Sunni and Kurd communities. In that respect, the government may be more conciliatory to minorities than its predecessor under Nouri al-Maliki. However, there are concerns that the government may have been formed partly under international duress and its durability is uncertain; the Kurds, seeking greater autonomy and control over oil shipments, have openly made their participation conditional on their demands being met within a three-month deadline. Meanwhile, Sunni support to help counter the threat of the militant Islamic State (IS) is also uncertain. Do not expect IS to relinquish Iraqi (or Syrian) territory easily, with or without international military intervention, and problems for Iraq and the wider region are unlikely to be resolved in the near term.

Asia Pacific

China: Trade surplus at a record high in August

Trade figures for August released by a local authority (the General Administration of Customs) continue to give positive signals. The trade balance reached a record high for the second consecutive month (USD49.8 billion after USD47.3 billion in July) supported by a strong rise in exports (by +9.4% y/y) and a fall in imports (-2.4% y/y following -1.5% in July). Indeed, exports to the country's main trade partners continued to grow strongly: to the U.S. by +12.5% y/y, the EU by +11.4% and to ASEAN by +13%. Imports from the U.S. declined by -3.1% y/y. The increase in external trade activity is likely to act as a cushion in Q3, as domestic indicators (including construction and industrial production) are showing signs of weakness. External trade will remain a key driver of growth as a result of a supportive monetary policy, particularly exchange rate intervention to maintain RMB at adequate levels, and financing measures for exporters. EH expects GDP growth of +7.5% in 2014.

What to watch

- September 11 – Brazil July retail sales
- September 11 – Mexico July industrial production
- September 12 – Spain August CPI
- September 12 – Eurozone July industrial production
- September 12 – Eurogroup meeting
- September 12 – Japan July industrial production (final)
- September 12 – U.S. August retail sales
- September 14 – China August FDI
- September 15 – U.S. August industrial production
- September 15 – Colombia July industrial production
- September 15 – Colombia July retail sales
- September 16 – U.S. August PPI
- September 16 – Israel Q2 GDP
- September 16 – UK August CPI
- September 17 – UK BoE minutes
- September 17 – Eurozone August CPI
- September 18 – UK : Scotland independence referendum

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