Euler Hermes Economic Research

Weekly Export Risk Outlook

22 April 2015

FIGURE OF THE WEEK

-0.6%

U.S. m/m contraction in industrial output in March

In the Headlines

China: New phase of the stimulus therapy

On 19 April, the People's Bank of China (PBoC) moved to reduce the reserve requirement ratio for banks (RRR) by a full 100bps (to 18.5%), marking the largest cut since the 2008 crisis. This was the country's second industry-wide cut in two months. The step-up in monetary easing is expected to free around RMB1.2 tn in additional liquidity, as the government attempts to boost bank lending and support economic growth. Targeted and specific RRR cuts were also announced, detailing an additional cut for the China Agricultural Development Bank (-200bps) as well as further cuts for rural financial institutions (-100bps) and banks that lend actively to SMEs (-50bps). Going forward, this move should be seen as a signal that the government is determined to reach its +7% GDP growth target. With advanced economic indicators pointing to a weak outlook in Q2 (MNI China Business Indicator down in April), we expect further easing in the short run in the form of an interest rate cut (-50bps) and, after stabilisation in Q2, GDP will accelerate slightly in H2, bringing full year growth to +7.1%.

U.S.: Anaemic manufacturing and housing

Industrial production contracted by -0.6% m/m in March, the third decline in four months, and although the manufacturing component gained +0.1%, over the past three months it has fallen at an annualised rate of -1.2%. Weakness in the oil sector pushed mining down -0.7% m/m while overcapacity and falling prices drove primary metals down -3.2%, the seventh loss in eight months. Housing data were also soft in March as starts were below expectations, gaining only +2% m/m (after declining -15.3% in the previous month) and falling by -2.5% y/y. Housing permits fell -5.7% m/m in March putting the y/y rate at a modest +2.9%. Meanwhile, inflation remains subdued, with the Consumer Price Index gaining only +0.2% m/m in March (0% y/y). The core inflation rate was also up +0.2% m/m to a +1.8% y/y rate. The Fed's Beige Book of anecdotal evidence was moderately upbeat, reporting increased retail sales in general and modest growth in 8 of 12 regions. EH expectations remain that the Fed will not increase interest rates before Q4.

Switzerland: Exports will decline by -CHF4 bn in 2015

The outlook for Swiss exporters has deteriorated after the removal of the CHF:EUR cap in January. After the initial knee-jerk 20% appreciation against the EUR in January, Euler Hermes expects the CHF will settle around CHF1.07 per EUR in H2, +14% stronger on average for the year. Exports to the Eurozone, Switzerland's main export destination with 46% of total exports, will thus feel the pinch of a stronger CHF and are estimated to decline by -CHF11 bn (-CHF4 bn to Germany). However, the moderate pick-up in world trade and the beneficial effects of USD strength – the CHF is forecast to be an average -11% weaker against the USD in 2015 – should offset much, but not all, of the negative FX effects in the Eurozone. Euler Hermes expects large export gains coming from the U.S. (+CHF5.3 bn) and China and Hong Kong (+CHF1.8 bn). Overall, Switzerland's exports are forecast to decrease by around -CHF4 bn in 2015 (for further details on the export outlook and export risks see our Economic Insight Switzerland April 2015).

Sub-Saharan Africa: Regional growth

In the IMF's recent World Economic Outlook (see also WERO 15 April 2015) the Fund lowered its forecast for GDP growth in 2015 in the Sub-Saharan Africa region by -1.25pps (relative to projections in October 2014) to +4.5% (after +5% in 2014). The reduced forecast reflects the impact of declining commodity prices and lingering weaknesses in key export markets but also the economic effects of the Ebola epidemic in west Africa. The decline in the oil price will have an adverse effect on the region's oil exporters, including the region's largest economy, Nigeria, and growth for the region's oil importers will remain broadly unchanged (from earlier projections) as benefits from lower oil import costs is balanced by negative effects associated with weaker non-oil commodities. Even so, the Fund remains relatively bullish overall on growth prospects and the region will record rates of expansion above those in advanced economies and in other emerging and developing economies (with the exception of Asia) in both 2015 and 2016. In the latter year, the IMF forecasts regional growth back over +5%. While downside risks persist, commercial prospects will therefore remain relatively good.

Countries in Focus

Americas

Colombia: A challenging year ahead

As real GDP growth decelerated through the course of last year (+3.5% y/y in Q4, compared with +6.4% in Q1), growth for 2014 as a whole was +4.6%, after +4.9% in 2013. The pick-up in investment (+10.9%) was not sufficient to offset the substantial deterioration in net exports; import growth accelerated by +9.2% and exports contracted by -1.7%. The external sector was affected adversely by the oil price shock as crude oil is the country's largest export category, accounting for almost 50% of total exports by value. At this juncture, short-term indicators suggest that economic activity continued to soften in Q1. Retail sales, although up from last year, appear to have weakened since the beginning of the year and industrial production contracted by -2.5% y/y and -1.3% in January and February, respectively. Against this background, Euler Hermes expects real GDP growth will fall below +4% in 2015.

Europe

Hungary & Poland: Further monetary easing to come

The Monetary Council of **Hungary** lowered its key policy interest rate by another 15bps to 1.8% this week, the 26th consecutive cut since August 2012, citing the continued deflationary environment and below potential output growth. Consumer prices continued to fall but the rate of decline slowed to -0.6% y/y in March from the all-time low of -1.4% y/y in January. Industrial production increased by +5.8% y/y in February but fell by -0.3% m/m. Last week, the Monetary Policy Council (MPC) of **Poland** kept its key policy interest rate unchanged at 1.5%, following the 50bps cut in March. Deflation eased only slightly to -1.5% y/y in March from the record low of -1.6% y/y in February and the MPC expects it to continue because of the fall in global commodity prices, moderate wage growth and the lack of demand pressures. Euler Hermes expects one or two more interest rate cuts in both countries before a return to moderate inflation, possibly in H2, will end the monetary easing cycles.

Africa & Middle East

South Africa: Outbreak of violence

Recent protests and violence raised diplomatic concerns about the safety of foreign nationals in the country. The targets of the violence are mainly immigrants from other African countries (and some Asians) and recent actions stem from long-standing structural weaknesses in the economy, particularly lack of jobs (unemployment is officially around 25% of the workforce) and housing. Indeed, periodic outbreaks of forceful xenophobia have been evident for several years, but usually dissipate quickly. The government has deployed the army to support the police force in maintaining law and order. While these recent events may partially dent the country's image, South Africa remains one of Sub-Saharan Africa's more stable countries and easiest places to do business. World Bank governance indicators are relatively good and in the Bank's 2015 Doing Business survey only Mauritius in the region is graded higher than South Africa, which ranks 43rd out of 189 economies assessed overall.

Asia Pacific

Japan: First trade surplus since 2011

The trade balance in March was surprisingly positive, with a surplus of +JPY3.3 bn, compared with a deficit of -JPY573 bn in February, and the first merchandise trade surplus since February 2011. This was driven by stronger external demand in Europe and the U.S., with real exports increasing to those markets by +13.7% y/y and +5.9% y/y, respectively. In terms of sectors, the surplus derived from a good export performance of autos and general machinery. The -10.3% y/y decline in imports is partly linked to lower oil prices, with mineral fuel imports declining by -36.5% y/y, but it is also as a result of base year effects from the April 2014 consumption tax hike. Imports increased strongly prior to the tax increase but correspondingly weakened after the hike. We do not expect this surplus to last over the year as imports are likely to recover with improving domestic demand. However, with lower energy prices, the trade deficit is set to narrow to -1.4% GDP in 2015 (from -2% in 2014).

What to watch

- April 23 – China April PMI manufacturing
- April 23 – Eurozone April PMI
- April 23 – UK March retail sales
- April 23 – France April business confidence
- April 23 – Spain Q1 unemployment
- April 23 – U.S. March new home sales
- April 24 – U.S. March durable goods orders
- April 24 – Germany April IFO business climate
- April 27 – Germany March retail sales
- April 27 – France March total jobseekers
- April 28 – U.S. April consumer confidence
- April 28 – France April consumer confidence
- April 28 – UK Q1 GDP
- April 29 – U.S. Q1 GDP
- April 29 – U.S. Fed policy announcement
- April 29 – Germany May GfK consumer confidence
- April 29 – Ukraine Q1 GDP flash estimate

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