Euler Hermes Economic Research

Weekly Export Risk Outlook

30 April 2015

In the Headlines

FIGURE OF THE WEEK

+0.2%

U.S. Q1 GDP growth q/q annualised

U.S.: Fed unlikely to move before Q4-2015

The Fed left the overnight funds rate unchanged, but did make several amendments to its policy statement, removing all calendar references and returning to data dependence as a key to decision making. The statement said “economic activity will expand at a moderate pace” and went into some detail about the results of some “transitory factors” that put a drag on the economy; “economic growth slowed…job gains moderated…growth in household spending declined…investment softened… housing sector remained slow, and exports declined”. EH expects that the Fed raise interest rates in Q4-2015. First quarter GDP supported the Fed’s assessment, showing very weak growth of +0.2% q/q annualized, compared with expectations of +1%. Consumption growth declined to only +1.9%, from +4.4% in the previous quarter, net exports subtracted -1.3% and, after stripping out inventories, the economy actually contracted by -0.5%. EH expects the remainder of the year to show much stronger growth, with data in the coming months particularly important. Evidence of pent up demand and a shaking off of the dire winter will be vital in the coming weeks. Among other signs of weakness, consumer confidence in March fell -6.2 points (95.2), driven by expectations of labor market weakness.

UK: Companies don’t like election uncertainty

GDP growth slowed more than expected in Q1, to +0.3% q/q compared with consensus expectations of +0.4%. The main positive contribution came from services, particularly retail trade, even though growth slowed to +0.5% q/q, after +0.9% on average since Q1 2014. In contrast, construction activity fell by -1.6% q/q, for the second consecutive quarter, while production industries also showed weakness, with manufacturing production down by -0.1% q/q. Going forward, we expect GDP growth will remain at +0.5% q/q on average, with Q2 GDP negatively affected by lower investment because of uncertainties relating to the elections. On a yearly basis, this will result in a lower than expected GDP growth (+2.2% in 2015), also reflecting a negative contribution from net exports. As a result, we expect the BoE will not tighten policy until Q2 2016, particularly as we expect inflation will remain markedly below the BoE 2% target for the next two years. In 2016, we expect GDP growth will slow to +2% and insolvencies will increase by +4%, reflecting monetary policy tightening and strong business creation since 2013.

Germany: Economic sentiment stabilises

The Ifo Business Climate Index climbed for the sixth consecutive month in April, to 108.6 (from 107.9 in March). However, while the current situation component again increased (to 113.9 from 112.1) the expectation component eased slightly (to 103.5 from 103.9). This is consistent with April’s moderate decline in the headline ZEW Economic Sentiment Expectations Index to 53.3 (from 54.8 in March), while the ZEW Present Sentiment Index surged to 70.2 (from 55.1). Moreover, the overall GfK Consumer Climate Indicator increased to 10.0 in April (from 9.7) and is forecast at 10.1 in May, but the Economic Expectations component eased slightly. Meanwhile, the five-month uptrend in the PMI took a break in April, with the Composite Output PMI down to 54.2 (55.3 in March) as a result of decreases in the Manufacturing Output Index (to 51.9 from 52.8) and the Services Activity Index (to 54.4 from 55.4). All in all, these surveys indicate stabilization after the rebound from the low in economic sentiment in autumn 2014 and support Euler Hermes' forecast of +1.7% real GDP growth in 2015.

Nepal: GDP likely to contract by -2% in FY2014/15

We expect the tragic earthquake in Nepal is likely to see GDP fall by -2% in the fiscal year ending in July 2015, reflecting a fall in private consumption (80% of GDP) and investment (23%). Gradual recovery is expected (+0.5% in FY2015/16) as a result of external financing and rebuilding after the earthquake. Official estimates put rebuilding costs above USD10 bn (equivalent to half of GDP) and the reconstruction process will take several years. Domestic savings represent only 10% of GDP so financing the recovery requires external assistance. Inward transfers (30% of GDP in 2014), the major economic buffer, are expected to increase but at a moderate pace (+8%, compared with an annual +15% over the past five years) reflecting weaker outlooks in host countries, particularly the GCC. The ADB pledged financial support of USD3 mn and the IMF announced its willingness to provide balance of payments support to preserve economic and financial stability. Moreover, we expect China (the principal investor) and India (premier trade partner) will also provide economic support.

Countries in Focus

Americas

Brazil: SELIC hike

For the fourth consecutive month, the Central Bank raised the key interest rate (SELIC) by 50bps, to 13.25%, the highest level since late-2008. Limiting inflationary pressures is therefore confirmed as the priority of the national monetary authorities, at the expense of weakening activity, with industrial production and retail sales contracting. Consumer prices increased by 8.1% y/y in March, markedly above the target inflation range of 4.5% +/-2pps, and are expected to continue strengthening. Industrial and consumer confidence continue to fall, both recording new record lows in March. Finance Minister Joaquim Levy asserted that to recover investor confidence fiscal consolidation is a key target for 2015 and several austerity measures have been announced, including tax increases and spending cuts. However, many of these need Congress approval to be fully implemented. After stagnating in 2014, we expect the economy will fall into recession this year (GDP contracting by -0.7%, at least).

Europe

Finland: Out with the old, in with the new

The Centre Party emerged as the political organisation with most seats in parliament, following this month's legislative elections, securing 49 of the 200 seats available and with 21.1% of the vote. Talks will now begin to form a ruling coalition but, with only narrow margins separating the three other main parties, there is no clear candidate to form an alliance with the Centre Party: The populist Eurosceptic Finns won 38 of the available seats, the incumbent National Coalition Party 37 seats and the Social Democrats won 34 seats. The new government may take weeks to form and will be tasked with addressing the country's most persistent economic crisis in recent history. In 2014, GDP contracted for the third consecutive year (-0.1%), a trend we expect to continue in 2015 (-0.4%) reflecting the Russian crisis (through the export channel) and weakness in domestic demand. EH expects the recession will end in 2016 (+0.6%).

Africa & Middle East

Saudi Arabia: It's a generation thing

Yesterday, HRH King Salman bin Abdulaziz Al Saud announced far-reaching changes in the country's leadership. The king's half-brother, Muqrin bin Abdulaziz, was replaced as Crown Prince (and heir apparent) by Interior Minister Mohammed bin Nayef Al Saud, who is King Salman's nephew. This is the first time a grandson of the kingdom's founder, rather than a son, has been appointed as Crown Prince. Long-serving (since 1975) Foreign Minister Prince Saud bin Faisal Al Saud was replaced and the king strengthened his own bloodline by appointing his son and Defence Minister, Mohammed bin Salman, as deputy crown prince. These changes usher in further evidence of the long-anticipated empowerment of a new generation of leaders and clarity of the succession process (for now) is market and rating agency positive. In terms of foreign policy, do not expect fundamental differences. Moreover, we do not expect Saudi Arabia will change its current stance on OPEC production quotas.

Asia Pacific

Thailand: Surprising rate cut will boost economic growth

The Central Bank unexpectedly cut its benchmark interest rate yesterday, from 1.75% to 1.50% (close to its historic low of 1.25%), after a five-to-two vote in favour of this decision. The Central Bank had already surprised the economic forecasters by cutting its benchmark rate from 2.00% to 1.75% in March. This latest cut comes against a background of tepid economic activity, with GDP increasing in 2014 (+0.7%) at its slowest pace since 2011, exports decreasing for a third consecutive month (y/y basis) and consumer confidence on a decreasing trend. Moreover, the Central Bank now sees a lower-than-predicted inflation dynamic (as core CPI slowed to 1.31% y/y in March from 1.45% in February) as well as downside pressures on exports from a strong THB that will not be offset by the observed rebound in tourist activity. Euler Hermes expects this rate cut will contribute positively to GDP growth of +3% in 2015 and +3.5% in 2016.

What to watch

- May 01 – China & Japan April manufacturing PMI
- May 01 – Japan March unemployment
- May 01 – U.S. April manufacturing ISM
- May 01 – Eurozone March unemployment
- May 01 – Mexico March budget balance
- May 01 – Peru April CPI
- May 01 – UK April manufacturing PMI
- May 04 – U.S. March factory orders
- May 04 – Eurozone April manufacturing PMI
- May 04 – Turkey April CPI
- May 04 – Brazil & Mexico April manufacturing PMI
- May 04 – Brazil April trade balance
- May 04 – U.S. April non-manufacturing ISM
- May 05 – Brazil March PPI
- May 05 – Indonesia Q1 GDP
- May 06 – Eurozone March retail sales
- May 06 – Poland monetary policy meeting
- May 06 – Romania monetary policy meeting
- May 06 – Brazil March industrial production
- May 06 – Russia & Ukraine April CPI

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