Euler Hermes Economic Research

Weekly Export Risk Outlook

03 June 2015

FIGURE OF THE WEEK

-3.8%

Switzerland Q1 2015 q/q Export growth

In the Headlines

Brazil: Recession has begun

Brazil's real GDP contracted by -0.2% q/q, after +0.3% q/q in Q4-2014, driven down by private consumption (-1.5% q/q) and investment (-1.3% q/q, the seventh quarter of continued fall). Net exports partially offset these negative figures. The volume of exports rebounded by +5.7% q/q, after a deep fall of -4.4% q/q in Q4-2014, combined with higher imports up +1.2% q/q. External demand contributed positively to GDP growth by +0.5pp q/q. The outlook remains gloomy for Brazil: short-term indicators (retail sales, industrial production, order books) continue to fall while business and consumer confidence are at record lows. Inflation reached +8.2% y/y in April, far above the Central Bank target (4.5% +/-2pp). In this context, the Central Bank is expected to pursue its monetary policy tightening over next months, after having raised the SELIC 225bps since September 2014 to 13.25%. Combined with drastic fiscal consolidation measures were adopted last week in order to meet the fiscal goal of a primary surplus of 1.2% of GDP in 2015, after a deficit of -0.6% in 2014. This restrictive cocktail of economic policies will weigh on an already weak economy. We expect Brazil to contract -1% this year.

U.S.: Q1 GDP -0.7% driven by trade deficit, weak consumption

First quarter annualized U.S. GDP growth was revised down sharply from +0.2% to -0.7%, driven by a surge in the trade deficit. The deficit rose due to the clearance of the import backlog at the West Coast ports and the stronger U.S. dollar. However even outside of the trade deficit, the report was weak as consumption grew only by +1.8% in Q1. And going into April personal consumption expenditures (PCE) actually shrank -0.05%, putting the 3 month average at an annualized rate of only +1.2%, even though disposable income gained +3.6%. The core PCE inflation rate was +1.2% y/y. April factory orders fell -0.4%, with durable goods orders dropping -1.0%, and an indicator of new orders for business spending fell for the third time in four months, losing -0.3%. One piece of good news was the ISM manufacturing survey which gained +1.3 points to a tepid 52.8, while the new orders component rose +2.3 points to a solid 55.8. The Fed can explain away the trade deficit but weak inflation and negative consumption are likely to put the first rate hike in Q4.

Switzerland: Q1 GDP falls modestly as expected

Q1 real GDP contracted by -0.2% q/q as the CHF appreciation after the removal of the CHF:EUR cap in January hit exports as expected. Exports of goods and services declined by -3.8% q/q while imports increased by +3.2% q/q. Domestic demand held up well, with private consumption growth accelerating to +0.5% q/q (+0.3% in Q4), in part benefitting from cheaper imports. Government consumption was up by +0.1% q/q (+2% in Q4). Fixed investment growth improved to +0.4% q/q in Q1 (flat in Q4) thanks to a large rebound in construction investment (+0.3% q/q, up from -1.5% in Q4) which more than offset a concurrent weakening of investment in equipment (+0.5% q/q, after +0.9% in Q4). In y/y terms, Q1 real GDP growth slowed to +1.1% from +1.9% in Q4. In May leading indicators such as the KOF business cycle index (up to 93.1 from 89.8 in April) and the PMI for the manufacturing sector (up to 49.4 from 47.9) suggest that Swiss firms have partially recovered from the initial CHF appreciation shock already. Euler Hermes maintains its forecasts for full-year GDP growth of +1% in 2015 and +1.2% in 2016.

Belgium: On track for a moderate economic recovery

GDP growth in Q1 (+0.3% q/q) has been mainly driven by household consumption (+0.7% q/q). Private investment contracted for the second consecutive quarter (-0.8% q/q) on the back of decreasing investment in construction and in equipment. Net exports contributed positively to growth (+0.2pp) with exports increasing by +0.5% q/q. After reaching a record high of 11 740 cases in 2014, business insolvencies are expected to remain on a downward trend in 2015 and 2016. However, an upside trend is visible in the Brussels region and overall, business insolvencies remain 40% above the 2007 level. The lower cost of financing (2.5% for bank loan rates) and an upturn in loans to non-financial corporations thanks to the ECB QE program should support investment going forward. In addition, firms' profitability should benefit from the lower cost of financing and the lower oil prices. However, turnover growth remains weak (+0.5% in 2015 and +2% in 2016) and the labor market recovery very slow. The suspension of wage indexation rule as well as, by 2019, the decrease in employers' SSC to 25% of the labor cost will give a temporary boost to companies' competitiveness. GDP growth should reach +1.3% in 2015 and +1.5% in 2016.

Countries in Focus

Americas

Canada: Q1 GDP -0.6% from low oil prices, weak U.S.

As expected Canadian GDP suffered in the first quarter, dropping -0.6% on an annualized basis. The Canadian economy was hit with a combination of severe winter weather, collapsing oil prices, and a wobbly U.S. economy; exports to the U.S. account for almost 20% of Canadian GDP. The weak Canadian dollar may draw a tourism boost this summer, but the effect of low oil prices is likely to be more persistent. The energy sector shrank -6.5% in Q1 to a -3.6% y/y rate while support activities for the oilfields fell a dramatic -76% in Q1 to -49% y/y. In its most recent statement, the Bank of Canada (BoC) struck an optimistic tone, but the sharp contraction in the oil patch, and the BoC's implicit reliance on the U.S. economy will keep the Bank on hold at best, and it may actually cut rates as the year progresses.

Europe

Poland: Robust Q1 GDP growth

Q1 real GDP growth picked up to +1% q/q (+0.8% in Q4 2014) and +3.6% y/y (+3.3% in Q4). Details show a recovery of net exports in Q1 which added +1.1pps to y/y growth, the first positive contribution since end-2013, because the sound increase in exports (+8% y/y) outpaced imports (+6% y/y). Domestic demand was negatively affected by a sharp drop in inventories (-1.5pps), which pulled down gross capital formation by -0.5% y/y, despite a surge in fixed investment (+11.4% y/y). Private consumption continued to rise by a robust +3.1% y/y in Q1 (+3% in Q4) while government consumption growth moderated to +3.3% y/y (+6.4% in Q4). EH expects the momentum to continue and forecasts full-year growth of +3.3% in 2015 and +3.4% in 2016. Against the backdrop of robust output growth and gradually easing deflation (-1.1% y/y in April, up from the record low of -1.6% y/y in February), the Monetary Policy Council decided today to keep its key policy interest rate unchanged at 1.5%.

Africa & Middle East

Ethiopia: Growing market

Preliminary results show that the ruling EPRDF party and its allies won an overwhelming majority in legislative polls that African Union observers declared as "generally consistent with the AU guidelines on the conduct of elections". The final result is not yet available but the EPRDF was widely expected to dominate the new parliament, given the fractured nature of the opposition and recent economic successes. Policies are expected to remain relatively unchanged under PM Hailemariam Desalegn. Inward foreign investment remains strong, spurred by relatively low wages, cheap power supplies and duty-free access to U.S. markets through the African Growth and Opportunity Act (AGOA). Average annual GDP growth in the ten-year period to end-2014 was +10.5% and Euler Hermes expects expansion of +8% in 2015 and +9% in 2016. Commercial opportunities will remain good in business related to infrastructure projects and the government plans to expand the manufacturing base.

Asia Pacific

India: GDP Picking up

GDP grew by +7.5% y/y in Q1 2015 (from +6.6% y/y in Q4 2014) bringing growth to +7.3% in FY2014-15. Looking at the breakdown private consumption (respectively +7.9% y/y from +4.2% y/y) and investment (+4.1% y/y from +2.4% y/y) rebounded in Q1, exports decreased (-8.2% y/y). In April CPI inflation decelerated to a four-month low (+4.87% y/y) remaining within RBI target (below 6% by January 2016). Against this background, the RBI cut its policy rates by 25 bp for the third time this year on Tuesday. The benchmark repo rate was decreased to 7.25 % (from 7.50%) with immediate effect and the reverse repo rate was lowered to 6.25 percent (from 6.50%). The Central Bank argued that the recovery is still fragile with low domestic capacity utilization, ongoing deinflationary pressures, and limited growth in credit. Going forward, we expect another rate cut of -25bp by end of Q3 to strengthen credit growth. Investment is set to accelerate and GDP will likely increase by +7.7% in FY2015-16.

What to watch

- June 04 – Finland Q1 GDP
- June 04 – UK Bank of England Bank Rate
- June 04 – Russia May CPI
- June 05 – France April Trade Balance
- June 05 – Hungary Q1 GDP
- June 05 – Eurozone Q1 GDP
- June 05 – Mexico May Consumer Confidence
- June 08 – China May Trade Balance
- June 08 – Germany April Industrial Production
- June 08 – France May Business Confidence
- June 09 – Peru April Trade Balance
- June 10 – France, Italy & UK April Industrial Production
- June 10 – India May Trade Balance
- June 10 – Turkey Q1 GDP
- June 10 – Brazil May IBGE Inflation

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Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com