Euler Hermes Economic Research

Weekly Export Risk Outlook

22 July 2015

FIGURE OF THE WEEK

USD1,113

Gold price per ounce (-16% y/y, -41% from Sept 2011 high)

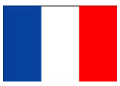
In the Headlines

Iran: Regional impact of the negotiated deal

The agreement reached to limit Iran's nuclear programme in exchange for an easing of sanctions (see WERO 16 July 2015), which has now been unanimously endorsed by the UNSC, will have regional repercussions, some of which will take time to come to fruition. There are also uncertainties as to whether the deal will hold (possible re-imposition of sanctions is built into the agreement) and, if it does, when actions on both sides will be implemented. Israel and some within the GCC countries see the deal as a strong negative for regional security, perhaps leading to enhanced Iranian support for groups including Hezbollah and Hamas and promotion of a localised race for nuclear defences. Iran will also be competing with other OPEC members for market share for oil exports (within or outside output agreements). On the plus side, larger trade and investment flows with Iran are likely to boost non-Iranian ports, financial centres and trading hubs in the region, including Dubai in the UAE. As global commercial entities seek to gain access advantages ahead of the anticipated lifting of sanctions on Iran in early 2016, trans-shipment ports in the region are likely to see a boost to trade beginning in H2 2015.

Brazil: Recession deepens

Industrial production fell by -6.9% y/y in May, completing 15 consecutive months of y/y contraction, and business confidence is at record lows. Retail sales have contracted by -5.6% from a recent peak in November 2014, reflecting weakness in private consumption. In addition, unemployment reached 6.9% in June (almost 2pts above the rate 12 months previously), inflationary pressures persist (8.9% y/y in June, markedly above the target of 4.5%) and economic policies continue to tighten. Indeed, since October 2014, the Central Bank has increased the key interest rate (SELIC) by a cumulative 275bps, to 13.75% in June, and further increases are expected, given the hawkish messages in the recent COPOM minutes. Moreover, additional cuts in public spending are likely as the government appears committed to reach its fiscal target for 2015 (primary surplus of +1.2% of GDP) despite a fall in fiscal revenues because of the weak economy. Against this background, we expect economic recession this year, with overall GDP contracting by -1.5%, among the worst in the region. Risks are on the downside.



France: The summer is magic

Signs of a (slow) broad-based recovery continue to be evident, as shown by the July INSEE business climate surveys. The industrial business climate improved by 2pts to 102 and is back above its long-term average. Global and export order books have improved and the corresponding balances are higher than their long-term average. The business climate in wholesale trade improved to 103 (+1pt) but more wholesalers expect a fall in prices. In services, the indicator improved by 2pts and, at 97, is at its highest level since October 2011, reflecting higher expected activity and demand. Additionally, more business leaders consider that employment has increased, particularly in temporary work agencies. The business climate in the retail sector remains stable at 106 and it has been above its long-term average since the beginning of the year, buoyed by the rebound in consumption. The business climate in the building construction industry, however, remains weak, at 90. Overall, after a sluggish Q2, Q3 started on a brighter note and the economy is on track for +1.2% real GDP growth this year.

U.S.: A hot summer housing market

Housing may finally be turning the corner, supporting Euler Hermes' forecast of +2.5% GDP growth for 2015. Starts increased by +9.8% m/m and +26.6% y/y in June, with growth concentrated in the multi-family component, which gained +29.4% m/m and +48.2% y/y, reflecting strong demand for rentals. Housing permits increased by +7.4% m/m, the third consecutive increase, registering a y/y increase of +30%. Again the main growth driver was multi-family dwellings, which gained +15.3% m/m and +70.4% y/y. The housing market index was unchanged at the 60 level but this represents a marked recovery from a recent low of 52 in March. The present sales index gained +1pt to 66 and is up +8pts since May. Expectations for future sales gained +2pts to a strong 71, also up +8pts since May. Only foot traffic lagged at 43 but this is up +4 points in two months. Meanwhile, consumer price inflation increased by 0.3% m/m and 0.2% y/y in June, while the core rate increased by only 0.2% to 1.8% y/y, still hovering just below the Fed's 2% target.

Countries in Focus

Americas

Costa Rica: Cost(a) effective

The export sector remains weak (-6.81% q/q and -16.15% y/y in Q1), largely reflecting the impact of the closure last year of a microprocessor assembly and manufacturing plant. Against this background, Q1 GDP did relatively well, increasing by +0.44% q/q and +2.6% y/y. A positive boost came through increased consumer spending – growth on a q/q basis was the highest since Q4 2011 – resulting from an income effect from lower oil prices. Meanwhile, a low inflationary background allowed the Central Bank to reduce the key policy interest rate for five consecutive months, to a current 3.5%, which is the lowest since the data series was activated in 2006. We expect these twin effects (weak exports and relatively strong consumption) will continue but their relative impact will diminish. The export sector is likely to get a boost from output growth from the manufacture of medical equipment. Overall, we expect GDP growth of +3.7% in 2015.

Europe

Russia: Downturn deepened in Q2

Q2 industrial output contracted by -4.9% y/y, sharply down from -0.4% y/y in Q1. Looking at the breakdown, manufacturing performed particularly weakly, down by -7.4% y/y in Q2 (-1.6% in Q1), with the downturn more focused on investment and intermediate goods such as transport equipment, machinery, metals and textiles. Fixed investment declined by -6.5% y/y in Q2. Moreover, mining production also moved into contraction in Q2, down by -0.9% y/y (+0.7% in Q1), as the boost from a government-backed oil refinery upgrade is starting to unwind. Agricultural production is still increasing following the import ban on EU products from August 2014 but it has steadily slowed from +4.2% y/y in March to +1.6% y/y in June. Meanwhile, the fall in retail sales deepened further to -9.4% y/y in Q2 (-7% in Q1), choking hopes of an early consumption recovery. Altogether, this points to a sharply deepening recession in Q2 and Euler Hermes continues to forecast full-year 2015 GDP will fall by -4%.

Africa & Middle East

West Africa: Another cause for concern

There is mounting alarm that the region, with a recent Ebola outbreak still not eradicated, may now be subject to an attack of a highly virulent avian flu virus, H5N1. The latter can be transmitted to people and is considered highly lethal. As a result, the FAO has already called for USD20 mn as a minimum medical response to stem the outbreak and limit its potential contagion. To date, the virus has been detected in poultry farms and markets in Burkina Faso and Niger but also in large regional economies including Nigeria, Ghana and Côte d'Ivoire. Poultry production in the region increased in the past 10 years, with output in Côte d'Ivoire up +60% since 2006, providing a nutritious and inexpensive source of food. The economic impact of an outbreak of H5N1 is difficult to quantify at this stage but the World Bank estimates that Ebola led to foregone economic expansion in the three worst hit countries (Sierra Leone, Guinea and Liberia) of at least USD1.6 bn. Expect commercial disruptions.

Asia Pacific

Vietnam: Q2 GDP growth gains momentum

First estimates show that Q2 real GDP expanded by +6.4% y/y, up from +6.1% y/y in Q1, taking H1 growth to +6.3% y/y. On the production side, industry (+9.1% y/y) was the main growth driver in H1, with manufacturing rising by +10%, mining +8.2% and construction +6.6%. The services sector increased by +5.9% y/y in H1 while agriculture grew more modestly, by +2.4% y/y. Demand-side details are limited but it is reported that total consumption increased by +8.7% y/y in H1 and gross capital formation by +6.9% y/y while net exports made a negative contribution of -3.7pps to H1 growth. Meanwhile, inflation remained low at 1% y/y in June, the same as in the previous two months, largely as a result of low oil prices. Nonetheless, the central bank has so far refrained from lowering its key policy interest rate (currently 6.5%). Euler Hermes expects some form of monetary easing in H2 2015 and forecasts full-year GDP growth will pick up moderately from the +6% achieved in 2014.

What to watch

- July 23 – Brazil June unemployment
- July 23 – Canada May retail sales
- July 23 – UK June retail sales
- July 23 – Turkey monetary policy meeting
- July 23 – South Africa interest rate decision
- July 24 – China July flash manufacturing PMI
- July 24 – EU July flash PMI
- July 24 – U.S. June new home sales
- July 23 – Nigeria interest rate decision
- July 27 – Israel interest rate decision
- July 27 – Germany June retail sales
- July 27 – U.S. June durable goods orders
- July 28 – South Africa Q2 unemployment
- July 27 – Germany July Ifo business climate
- July 28 – U.S. July consumer confidence
- July 28 – Ukraine Q2 current account
- July 29 – Germany July GfK consumer confidence
- July 29 – U.S. Fed meeting

View all Euler Hermes Economic Research online
http://www.eulerhermes.com/economic-research

Contact Euler Hermes Economic Research Team
research@eulerhermes.com

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