Euler Hermes Economic Research

Weekly Export Risk Outlook

9 September 2015

In the Headlines

FIGURE OF THE WEEK

-4.6%

Russia's Q2 y/y contraction in GDP

Eurozone: Let's twist again with the ECB!

The ECB revised GDP and inflation projections downwards - inflation in 2016 and 2017 is now expected at 1.1% (-0.4pps) and 1.7% (-0.1pps) - reflecting heightened downside risks, including lower oil prices and weakness among emerging markets. Meanwhile, the ECB is seeking to increase the issue share limit on purchases to 33% from 25%. For now, the amount of monthly purchases will remain unchanged at EUR60 bn but it appears that the 25% threshold is becoming a binding constraint on purchases of some non-sovereign bonds. An increase in the issue share limit signals that the Bank will employ its asset purchase programme flexibly. Consequently, we expect the ECB will extend its asset purchases beyond September 2016 and maintain its programme unchanged until at least mid-2017. This will allow the EUR to remain low and support exports. A policy change could be announced before the end of the year. As a final comment, an extension does not rule out an increase in the volume of monthly purchases and we see this as a likely scenario, given the weakness of nominal growth, low oil prices and subdued prospects for employment-restraining wage growth.

Russia: Sharp contraction in Q2, more to come

Second official estimates confirmed that the economy contracted by -4.6% y/y in Q2, after -2.2% y/y in Q1. Rosstat also published data that revealed a decrease in Q2 real GDP of -2% q/q (-1.6% in Q1), the fourth consecutive quarter of decline. On the production side, manufacturing contracted by -4.8% y/y in Q2, construction -6.9% y/y and mining -0.1% y/y. Retail trade plunged by -9.9% y/y, indicating that private consumption remained very weak. The real estate sector contracted by -5.7% y/y, transport and communication -4.1% y/y and financial services -5.2% y/y. Only agriculture (+2.1% y/y), utilities (+1% y/y) and public administration and defence (+1.2% y/y) increased modestly in Q2. Early indicators for Q3 signal continued weakness (see also WERO 19 August 2015). In August, the manufacturing PMI fell to 47.9 (48.3 in July) and the services PMI decreased to 49.1 (51.6 in July). As oil prices remain relatively low, EH expects Q3 to be at least as weak as Q2, although the recession may bottom out in Q4, and forecasts full-year GDP will contract by -4% in 2015, followed by -0.3% in 2016.

U.S.: In labour?

The August employment report was mixed, providing little clarity about whether the Fed will start increasing interest rates next week or sometime in the future. Elements of strength in the report include a -0.2pps fall in unemployment, to 5.1%, and an upward revision to the number of jobs created in the previous two months, by +44,000. However, unemployment was driven down by -41,000 people exiting the workforce, leaving the participation rate unchanged at 62.6%, the lowest since October 1977. Moreover, only +173,000 jobs were created in August, markedly below expectations of +225,000, and the manufacturing sector lost -17,000 jobs. Furthermore, while earnings increased +0.3% m/m, the y/y rate remained at +2.2%, only marginally above the rate of inflation. However, the ISM non-manufacturing report was more positive. Despite slipping -1.3 points, the index was 59 in August, decidedly above the 50 level signifying expansion, while new orders came in at a robust 63.4. EH expects that the economy will continue to grow at a modest pace, with overall growth of +2.5% in 2015.

Egypt: What a gas!

Announcement of the discovery of a "supergiant" offshore gas field, potentially the largest in the Mediterranean, could appreciably change the dynamics of both the Egyptian and regional economies. The deep water Zohr field could hold 30 tn cubic feet of natural gas and satisfy growing domestic energy needs and, perhaps, allow for future gas exports. Egypt is currently a net energy importer and supplies to some sectors (including cement and fertilisers) have periodically been rationed, curtailing output. In contrast to good news for Egypt, the discovery brings into question potential sales into the Egyptian market from the troubled Israeli Leviathan gas field. The Zohr field will be able to use existing infrastructure, so drilling can start in 2016 and output come onstream by 2017. Coming shortly after the inauguration of the Suez Canal improvements (see WERO 19 August 2015) there is a renewed vibrancy about the economy, but much will depend on maintenance of stability and security.

Countries in Focus

Americas

Guatemala: General elections amid political crisis

Following a corruption scandal that triggered large-scale demonstrations, Congress lifted presidential immunity for the first time and Otto Molina Pérez resigned and was ordered to jail. Vice-president Alejandro Maldonado was sworn in as president last Thursday. Amid this political crisis, the first round of general elections was held on Sunday. None of the 14 presidential candidates gathered more than 50% of the votes, so a runoff is scheduled for 25 October. It will be contested by Jimmy Morales of the FNC (National Front for Convergence), who received most votes (24%) and whoever is officially declared second; the vote count so far puts Sandra Torres from the left-wing UNE (Unidad Nacional de la Esperanza) slightly ahead of Manuel Baldizón, of the Renewed Democratic Freedom party. Despite the political crisis, the impact on the economy is likely to be muted as a change of political leadership was expected. EH believes activity will remain dynamic, with GDP expanding by around +4% this year.

Europe

UK: Export prospects hurt by GBP appreciation

The trade balance in goods deteriorated in July (-EUR11.1 bn), the largest deterioration since July 2013, reflecting a fall in exports (mainly chemicals and cars) but a pick-up in imports (machinery and transport equipment). Most of the overall deterioration derives from trade with non-EU countries, notably the U.S., Switzerland and China. On a yearly basis, the deficit in goods reached -EUR120 bn, compared with a surplus of +EUR91 bn for services. The relatively poor performance of exports of goods results from a continued loss in competitiveness and weak productivity growth, despite attempts to boost re-industrialisation. The real effective exchange rate is up +5% y/y since January and this trend is expected to accelerate, given currency depreciation in most trade partners (except the U.S.) and the anticipated hike in interest rates by the BoE in H1 2016. Prospects for export orders are on the downside as we expect GBP to remain strong. Overall, GDP growth will slow to +2.5% in 2015 (+3% in 2014).

Africa & Middle East

Ghana: Steady ahead

Weakness in commodity prices for oil, gold and cocoa and earlier fiscal over-spending resulted in a request for IMF financial assistance. In April, the Fund approved a three-year Extended Credit Facility (ECF) of USD918 mn that aims to restore debt sustainability and macro-economic stability and return the economy to high growth and job creation. In a recent review of progress, the Fund reports that, despite the unfavourable international backdrop, implementation of the reform process that underpins the ECF is broadly satisfactory. In particular, the government's fiscal consolidation measures are on track, including action on eliminating fuel subsidies. FX reserves declined to USD3.2 bn at end-June and currently provide import cover of just over two months, so the authorities are likely to continue the reform process to maintain continuing support under the ECF. EH expects GDP growth of only +3% in 2015 (over +8% in 2012) but a bounce back to around +6% in 2016.

Asia Pacific

China: Trade weak in August and, maybe, September

Exports in USD terms contracted in August but the pace (-5.5% y/y) was slower than in July (-8.3%). A breakdown reveals a decrease in demand from all main partners, with exports to the EU (15.5% of total exports) and Hong Kong (14.8%) down by -7.5% y/y and -3.8%, respectively. Import data are more disappointing (-13.8% y/y in August from -8.1%) with a broad fall in Chinese demand. September data are likely to continue this pattern as new export orders are still on the downside and domestic private demand is growing slowly. However, we expect a gradual change in Q4, with positive export growth supported by firmer demand in advanced economies, although the recovery path for imports will probably take longer reflecting negative price effects of primary commodities and still adjusting domestic demand. Investment is set to slow further reflecting weak sentiment and reduction in overcapacity but domestic consumption will remain resilient as a result of a high state contribution.

What to watch

- September 10 – China August CPI
- September 10 – France July industrial production
- September 10 – Japan August PPI
- September 10 – UK MPC base rate
- September 10 – South Africa July mining output
- September 11 – Germany August CPI
- September 11 – India July industrial production
- September 11 – U.S. August PPI
- September 14 – Kenya Q2 GDP
- September 15 – U.S. August retail sales
- September 15 – U.S. August industrial production
- September 15 – South Africa Q2 current account
- September 16 – U.S. August CPI
- September 17 – U.S. August housing starts
- September 17 – U.S. Fed policy statement

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