Euler Hermes Economic Research

Weekly Export Risk Outlook

3 December 2015

In the Headlines

FIGURE OF THE WEEK

10.9%

Weighting of Chinese currency in the IMF's SDR from October 2016

Brazil: Deeper recession

Data released earlier this week by the statistical agency IBGE show a deeper recession than initially announced. Real GDP growth for Q1 and Q2 were revised downwards to -2.1% y/y (compared with -1.6% initially) and -3% y/y (-2.6%), respectively. In Q3, real GDP fell by a further -4.5% y/y, the deepest contraction since 1995. In q/q terms, GDP fell by -1.7% in Q3. Private consumption contracted by -1.5% q/q, reflecting weak household confidence because of high inflation (9.9% y/y in October), increasing unemployment (7.9% in October, compared with 4.7% a year ago) and contracting real payrolls (-2% y/y). Investment fell -4% q/q and inventories shaved -0.7pps from overall growth. Public consumption was the only demand component to show even meagre growth (+0.3% q/q). Despite a decline in exports (-1.8% q/q in Q3 after +3.1% in Q2), net exports again contributed positively to growth, given the marked fall in imports (-6.9% q/q after -8% in Q2). Given these latest data, the carry-over for 2015 stands at -3.5%. We now expect the economy will contract by -3.8% this year and it will remain in deep recession in 2016, with GDP contracting by at least -2%.

Eurozone: Just a bit more, but not enough

We were expecting the ECB to lower the deposit rate, to expand the QE duration and increase the monthly asset purchases from the current EUR60bn but only the first two of these were implemented on 3 December. The ECB announced that the range of assets that are purchased is wider (taking into account regional and local governments) and that the principal payments are reinvested before and post March 2017, which will allow liquidity to remain abundant up to 2018, at least. However, market reaction was muted, with the prospect of more action next year as economic growth remains weak; private consumption is supported by low inflation and low oil prices, but the main boost is behind us and further support of this kind now seems limited. We remain cautious about the strength of exports as the potential for a much lower EUR/USD seems low (expect 1.05 in 2016 from 1.1 in 2015) while global demand lacks momentum. ECB forecasts for GDP growth remain unchanged at +1.5% in 2015, +1.7% in 2016 and +1.9% in 2017, but inflation forecasts have been revised downwards (to +1% in 2016 and +1.6% in 2017). Forecasts for both indicators remain slightly above our expectations.

China: SDR inclusion, first step on long journey

The IMF announced that, effective from October 2016, the RMB will be included in its Special Drawing Rights (SDR) basket, with a weighting of 10.9%, compared with 41.7% for the USD and 30.9% for the EUR. The decision's symbolism is strong as it endorses the role of China as a key driver of the global economy and acknowledges positive improvements in the internationalisation of the RMB. In economic terms, the impact is yet to be assessed. In the short term, adjustments to the Central Bank balance sheet are likely to lead to an additional USD30bn RMB demand. This may increase significantly if the RMB becomes a full global reserve currency. To do so, China will have to open fully its capital account and loosen its grip on the currency. This is likely to be gradual and effectively communicated to avoid the type of currency and financial market volatility seen in August. The currency is still subject to strong downward pressures in response to weak economic news (such as manufacturing PMI) and the upcoming Fed hike. Greater clarity and more guidance on the RMB's internationalisation will be crucial.

Switzerland: Faltering investment dampens growth

Real GDP stagnated q/q in Q3 after increasing by +0.2% in Q2, as sharply declining gross investment offset improving consumption and external demand. Private consumption growth picked up to +0.4% q/q (+0.3% in Q2) and public spending surged by +1.8% q/q (-0.1%). Fixed investment fell by -0.2% q/q (+0.8% in Q2) as investments in construction dropped by -0.9% q/q while those in equipment were up by +0.2%. Inventories subtracted a heavy -2.2pps from Q3 q/q growth. Exports increased by +5.4% q/q (-4.1% in Q2) while imports increased by +3.3% q/q (-6.9%) so that net exports contributed +1.8pps to Q3 growth (+1.2pps in Q2). These high and volatile trade activity growth rates are explained by valuable items, which account for approximately 25% of Swiss external trade and that fluctuate strongly, rather uncorrelated with the business cycle. Excluding valuables, exports expanded by +0.6% q/q (+0.3% in Q2) and imports by +0.2% (-1.2%) – providing a better picture of the economy. Euler Hermes cut its full-year GDP growth forecast to +0.8% in 2015 and maintains +1.2% for 2016.

Countries in Focus

Americas

U.S. & Canada: Fed nearing liftoff and Canada rebounds

In the **U.S.**, personal consumption expenditures (PCE) increased by only +0.1% m/m in October, below expectations of +0.3%. After inflation and taxes, income increased a strong +3.9% y/y, but consumption by only +2.7%, below the +3.3% long-term average. The Fed's favoured inflation gauge, core PCE, remained at +1.3% y/y, below the +2% target. Construction spending increased by +1% m/m in September to a strong +13% y/y but manufacturing data were mixed. November auto sales reached 18.2mn units annualised, a 12-year high, and durable goods orders gained +3% m/m in October (+0.5% y/y), the first positive in nine months, but the ISM index fell to 48.6, the lowest of the recovery. Fed Chair Yellen appears inclined to favour a December interest rate hike. **Canadian** GDP increased by +2.3% q/q annualised after contracting in Q1 and Q2. Growth was driven by a steep +9.4% gain in exports, boosted by a weak CAD. The Bank of Canada left interest rates unchanged.

Europe

Greece: Recession proves resilient

Q3 GDP contracted (-0.9% q/q) more than first estimated (-0.5%). The fall in GDP was much lower than initially expected, given strong import contraction (-17%) following capital controls. Net exports contributed +3.2pps to growth (exports declined by -7%). All domestic components were negative: private consumption (-0.8% q/q), total investment (-7%) and stocks (-2.7pps). However, following two quarters of positive growth, our forecast for 2015 is revised upwards (from -2% to -0.4%). We expect contraction will continue in 2016 as imports recover and exports and domestic demand remain weak, but growth will turn positive in H2. Capital controls are expected to be lifted by mid-2016 as banks will be fully recapitalised, some remaining measures are scheduled for a mid-December vote and the Troika review will follow shortly afterwards. If there is a positive outcome, new debt relief measures are expected in Q1 2016, although delays are likely. A Eurogroup progress meeting is scheduled for 7 December.

Africa & Middle East

Burkina Faso: Kab driver

Last Sunday's presidential election was won by Roch Marc Christian Kaboré, who received 53% of the vote. The election appears to have been conducted relatively fairly - the main opposition candidate (29.7%) conceded defeat - and potentially fills the political vacuum created by the forced resignation in October 2014 of former-president Blaise Compaoré whose plan to change the two-term presidential constitutional limit caused a civil uprising, as well as a brief military coup in September 2015. Initial reaction from the investor community is positive, with an expectation that policies under Kaboré will be more pro-business and that aspects of a new mining code will be altered to retain existing investments. Mining is the country's main source of foreign exchange. However, the social and political pressures that led to Compaoré's downfall provide a challenging environment and the government will be pressured to give priority to public-sector wage increases and social programmes.

Asia Pacific

India: Improving trend?

Q3 GDP growth accelerated to +7.4% y/y (from +7% in Q2). Domestic demand was the main driver; government consumption was up +5.2% (from +1.2%) and investment +6.8% (+4.9%). On the supply side, the improvement was led by a rebound in manufacturing (+9.3% y/y from +7.2%). Wholesale and retail sales were resilient (+10.6% y/y from +12.8%). Inflation accelerated for the third consecutive month in October, to 5% y/y. Against this background, the RBI kept its benchmark policy interest rate unchanged (repo rate of 6.75%) after a cumulative cut of 125bps since December 2014. High-frequency indicators signal gradual improvement. Domestic vehicle sales accelerated in October (+13.9% y/y from -0.5%) and bank loans are gaining traction. However, November's business surveys were disappointing; both manufacturing (50.3 from 50.7 in October) and services PMI (50.1 from 53.2) weakened. We see a moderate acceleration in GDP growth in FY2015-16, to +7.4% (+7.3% in FY2014-15).

What to watch

- December 04 – U.S. November employment report
- December 04 – U.S. November international trade
- December 04 – Canada November employment report
- December 04 – OPEC meeting
- December 04 – Germany October factory orders
- December 04 – Russia November CPI
- December 04 – Bulgaria & Croatia Q3 GDP (2nd est.)
- December 04 – Hungary & Romania Q3 GDP (2nd est.)
- December 04 – Eurozone November retail PMI
- December 07 – Germany Oct. industrial production
- December 07 – Eurozone Dec. investor confidence
- December 07 – Eurozone Eurogroup meeting
- December 07 – South Africa Q3 current account
- December 07 – Ukraine November CPI
- December 08 – Eurozone Q3 GDP (2nd estimate)
- December 08 – France Nov. business sentiment
- December 08 – EU Ecofin meeting
- December 08 – Japan Q3 GDP
- December 08 – China latest trade figures
- December 08 – Hungary November CPI
- December 09 – Czech Republic November CPI