Euler Hermes Economic Research

Weekly Export Risk Outlook

14 September 2016

FIGURE OF THE WEEK

+3.1%

Q2 2016 y/y GDP growth in Turkey

In the Headlines

Turkey: Q2 GDP growth slowed more than expected

Real GDP growth decelerated to +0.3% q/q and +3.1% y/y in Q2 2016, from +0.7% q/q and +4.7% y/y in Q1. The breakdown of the y/y figures reveals that Q2 growth was again entirely driven by strong consumer spending (+5.2% y/y in Q2, albeit down from +7.1% in Q1) and very strong public spending (+15.9% y/y, after +10.9% in Q1). Although the election year 2015 is over, the government continues with strong fiscal stimulus. However, annual fixed investment growth weakened further into contraction territory (-0.6% y/y, after 0% in Q1) and inventories subtracted -0.6pps from Q2 growth (-0.3pps in Q1). Moreover, real export expansion came to a near-standstill at +0.2% y/y in Q2 (+2.4% in Q1) while real imports remained strong (+7.7% y/y, up from +7.3% in Q1) so that the negative contribution of net exports to growth rose to -2.3pps in Q2 (-1.6pps in Q1). Early indicators suggest a further deterioration of business confidence (manufacturing PMI) and economic activity (industrial production, and retail sales contracted in July) in Q3. EH expects that the economic slowdown will continue in H2, resulting in full-year real GDP growth of about +3% in 2016 (after +4% in 2015). The forecast for 2017 is +3.2%.

Eurozone: Trying to achieve the initial easing targets

The ECB did not announce any new measures at its meeting last week and kept its economic forecasts broadly unchanged. Eurozone real GDP is expected to grow at a moderate but steady rate (+1.7% in 2016; +1.6% in both 2017 and 2018) and inflation to pick up gradually (+0.2% in 2016; +1.2% in 2017 and +1.6% in 2018). EH does not expect the ECB to increase the pace of its monthly asset purchases but rather to extend it beyond March 2017 and to ensure better implementation. So far, the ECB has reached its target of asset purchases (EUR60bn per month initially and EUR80bn since March 2016) only three times. Indeed, the bond market rally makes the QE conditions hard to achieve as around 60% of the Eurozone bond market is trading at negative yields. Special Committees have been appointed to help redesign the QE program. The main options are: (i) raise the limit per bond issue above 33%; (ii) buy bonds with yields below the -0.4% deposit rate rule; (iii) target bonds with shorter maturities (less than 2 years); and (iv) extend the purchases to other classes of assets.

Venezuela: New elections and default ahead?

Major demonstrations demanding for a recall referendum against President Maduro have mounted since the beginning of September. The referendum needs to be held this year in order to trigger new elections. Popular outrage is growing over food and basic goods shortages, skyrocketing inflation (800% expected in 2016) and the deepening economic recession (forecast at -10% in 2016). International support for Maduro has also weakened. Yesterday, the fellow Mercosur member states set Venezuela a time limit until 1 December to align with the membership requirements to avoid being suspended from the trade bloc. Moreover, the lack of financing persists amid long-lasting low oil prices (95% of exports), a rapid depletion of foreign exchange reserves, no access to capital markets and China rethinking its financial support to the country. PDVSA, the national oil company, proposed on Tuesday a bond swap on USD7bn in outstanding debt due in 2016 and 2017 for new bonds maturing in 2020. However, investor appetite is weak. A default on the public debt cannot be ruled out.

China: Growth stabilizes, policy fine tuning to continue

Economic activity showed signs of stabilization in August. Growth of both industrial production (+6.3% y/y, from +6% in July) and retail sales (+10.6% y/y, from +10.2%) strengthened and investment growth stabilized (+8.1% y/y YTD). Exports (in USD) continued to decrease but at a slower pace (-2.8% y/y, after -4.4% in July) and imports recovered (+1.5% y/y) after the drop in July (-12.5%). The business sentiment was broadly positive with both PMIs (official and private-sector) reading above 50 in August. This suggests that Q3 GDP growth should remain in the comfort zone of the authorities (+6.5% to +7%). In that context, policymakers will maintain a “cautious easing stance”. In particular, the Central Bank will keep interest rates at a low level and continue to provide adequate liquidity to the banking sector. However, credit supply will likely be more targeted and authorities will probably tighten regulation to contain financial risks especially from the housing market. On the fiscal side, the support will remain strong to sustain economic growth. Euler Hermes expects real GDP to grow by +6.5% in 2016.

Countries in Focus

Americas

Canada: Labor market gains in August

The economy created +26.2k jobs in August, reversing two months of losses. The largest gains were in Ontario (+10.5K) and Quebec (+21.9k), while Alberta created +2.7k jobs, the first gain in five months, and BC lost -6.7k jobs, only the second loss in eight months. The goods and service sectors both rose for only the third time in 15 months while full time jobs rose +52.2k and part time jobs fell -26k. Over the past year the labor market is showing some stress as job creation has slowed to only +0.4% y/y compared to +1.1% last August; the job gains have all been in Ontario, Quebec, and BC (+37.2k, +33.6k, and +72.6k); Alberta continues to suffer losing -53.4k jobs, and; full time jobs shrank -35.7k while part time jobs rose +113.1k. But with the unemployment rate at 7.0% (compared to the long-term average of 7.7%), the slowing growth may be more a sign of a tighter labor market than a weaker economy. Euler Hermes forecasts GDP growth of +1.3% for 2016 and +2.2% for 2017.

Europe

UK: Construction sector in the Brexit forefront

Last week a series of indicators confirmed the softness of the construction sector. Mounting uncertainty constrains consumer confidence and willingness to engage in major transactions, as indicated by: (i) house prices falling by -0.2% m/m in August after -1.1% m/m in July; (ii) July home sales declining by -1% m/m; (iii) July mortgage approvals being down for the second month in a row, to 60,912, the lowest since January 2015; and (iv) July construction output remaining flat (an increase in public construction works compensated for the fall in private construction output). Meanwhile, the GBP depreciation (the real effective exchange rate fell by -7% in July alone, after a cumulative -5% in H1) and the high proportion of imported inputs for a range of products are expected to drive inflation to an average +2.5% in 2017. This should erode households' real income growth further as wages have started to decelerate (+2.1% y/y in the three months to July, down from +2.3% y/y in June).

Africa & Middle East

Gabon: Political uncertainty to test economic resilience

GDP growth has remained resilient and is forecast at +4% in 2016, after +4.5% in 2015. As an oil exporter, Gabon has suffered from low oil prices, but expansionary fiscal policy has helped to cope with the shock. More generally, fiscal policy in the last years was designed to support the diversification of the economy. This goal was achieved as the contribution of the oil sector to GDP decreased from 45% in 2010 to 23% in 2015. However, this diversification was financed with fiscal resources directly coming from oil revenues. As these revenues decreased and the government decided to keep financing the economy, public debt rose from almost 30% of GDP in 2013 to an estimated 50% in 2016. Accordingly, this strategy is not sustainable in the long run. With a running current account deficit, the country needs to attract foreign investment. However, the recent political turbulences in the wake of disputed presidential elections are not exactly what investors are looking for.

Asia Pacific

Japan: In the slow growth trap?

Latest activity indicators suggest weak economic growth prospects. Industrial production fell in July (-4.2% y/y, after -1.5% y/y in June). Both the Nikkei Manufacturing (49.5) and the Services PMIs (49.6) were below 50 in August, signaling activity contraction. Bank lending growth was low in August (+2% y/y). Deflationary pressures persist for producers with the PPI declining in August (-3.6 % y/y). An improvement was recorded in machinery orders (+5.2% y/y in August, after -0.9% in July) but it is too early to conclude that the sector has turned the corner. The short-term outlook remains challenging. While private consumption is set to prove resilient benefitting from both higher wages and lower inflation, stronger growth will also depend on favorable investment and export conditions. Currently, the latter are hampered by the strong yen and declining profits. Fiscal policies support growth, but further support from the Central Bank is also needed. EH expects GDP to grow by +0.7% in 2016.

What to watch

- September 15 – Eurozone August consumer prices
- September 15 – Russia August industrial production
- September 15 – UK August retail sales
- September 15 – UK BoE Bank Rate
- September 15 – Ukraine interest rate decision
- September 15 – U.S. August industrial production
- September 15 – U.S. August producer prices
- September 15 – U.S. August retail sales
- September 16 – Russia interest rate decision
- September 16 – U.S. August consumer prices
- September 19 – Eurozone July current account
- September 19 – Poland and Russia August retail sales
- September 20 – Hungary interest rate decision
- September 20 – Ukraine August retail sales
- September 20 – U.S. August housing starts
- September 21 – Ukraine August industrial production
- September 21 – U.S. Federal Reserve policy statement

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