Euler Hermes Economic Research

Weekly Export Risk Outlook

26 October 2016

FIGURE OF THE WEEK

14%

Brazil's Central Bank new reference interest rate

In the Headlines

Brazil: Fighting to keep debt under control

Brazil's fiscal deficit is expected to score -10% of GDP in 2016. Gross government debt has been escalating for 5 years. In order to prevent future increases, lawmakers in Brazil's Congress have tabled a proposal to limit the real increase of government spending to zero for up to 20 years. The proposal passed its first vote in the lower house, and is expected to be confirmed by the upper house. In what can be seen as a promising turning point, the Central Bank cut its target interest rate for the first time in 4 years from 14.25% to 14%. Markets were expecting an ease on monetary policy that could counter the current contractive economic cycle. Further loosening will rely on the easing of inflation and progress on reducing fiscal spending. Inflation in September scored the smallest increase since 1998, +0.08% m/m, a faster than expected decline. Our forecast for 2016 is +8.7% y/y. Inflation will continue to lose steam in 2017 towards the +4.5% y/y target rate (±2pp band). Meanwhile, GDP for 2016 is expected to be -3.5% y/y, a minor improvement over 2015.

Eurozone: Sustained growth in the private sector

IHS-Markit PMI surveys revealed that activity in the private sector expanded again in the month of October on the back of improved confidence thanks to more domestic demand. The Composite Index posted 53.3 against 52.6 in September, thanks to dynamic services (53.5 against 52.2). The manufacturing sector also performed better, with 54.4 against 53.8 in the previous month. The growth upturn in Germany is mostly what contributed to this acceleration. The German PMI composite stood at 55.1 against 52.8 in September on the back of renewed demand for German services (PMI at 54.1 against 50.9 last month). France, on the contrary, signaled a deceleration in activity for the whole of the private sector, with 52.2 in October against 52.7 last month. If manufacturers registered an acceleration in activity to a 31-month high, the services sector was less dynamic than in September, with the index at 52.1 against 53.3 before. Overall, these indicators show that the economic recovery is on a steady path. After +0.3% q/q in Q2 2016, we expect GDP to maintain its growth course in Q3 with the same rate of +0.3% q/q.

Russia: Current account surplus remains small

Initial estimates indicate that the current account surplus remained small at just USD1.9bn in Q3, after USD1.5bn in Q2 (revised down from an initial USD3.4bn in Q2) and USD12.2bn in Q1. Exports of goods increased by +4% q/q but were still down -10% y/y. As the average oil price remained stable in Q3 (USD47 per barrel of benchmark Brent) revenues from oil and oil products edged up slightly to USD32bn from USD30bn in Q2 but remained below the USD33bn shipped in Q4 2015, the weakest quarter last year. Imports of goods rose by +14% q/q and +5% y/y, with the latter marking the first annual increase since Q3 2013. Strengthening imports reflect the impact of a stabilized RUB (currently at 62 per USD), reduced inflation (6.4% y/y in September) and interest rates on domestic demand. For 2016 as a whole, Euler Hermes forecasts the current account surplus to narrow to about +1.7% of GDP from +5.3% in 2015. Meanwhile, net capital outflows by the private sector came in at –USD2.6bn in Q3, taking the cumulative net outflows to just –USD9.7bn year-to-date (–USD58bn in full-year 2015).

South Korea: Q3 GDP resilient yet fragilities remain

South Korean GDP decelerated to +0.7% q/q in Q3 from +0.8% in Q2 according to preliminary estimates. Private consumption slowed to +0.5% q/q. Government consumption accelerated to +1.4% q/q (from +0.1% q/q). Investment remained strong driven by construction activity (+3.9% q/q); other investment components weakened. Exports showed some signs of resilience with a recovery in services. On the supply side, the main drag was manufacturing activity which contracted by -1.0% q/q. Construction and services recorded firm growth. Looking ahead advanced indicators point to a resilient but fragile outlook. On the one hand, growth is driven by strong investment in construction and a rise in public expenditures. On the other hand, the export outlook is still weak: USD denominated exports decreased in September (-5.9% y/y). Last, downside risks are elevated with business surveys pointing to weaker growth in the short-run: manufacturing PMI is down to 47.6 in September. GDP growth is set to decelerated to +2.6% in 2017.

Countries in Focus

Americas

US: Tepid data, but more concern over the consumer

The housing market continues to demonstrate its usual volatile movements with a long-term upward drift. Housing permits rose 6.3% m/m in September, the fifth increase in six months. A sharp -9.0% m/m fall in starts was not as bad as it looked since it was driven by the volatile multi-family component. Unit sales of existing homes rose +3.2% m/m after having fallen in the previous two months, putting the y/y rate at a mere +0.6%, but prices fell -2.4% in September, the third straight loss. Consumer confidence slipped 4.9 points to 98.6 as respondents' assessments of both present and future conditions fell -7.3 and -3.3 respectively. The Fed's Beige Book indicated that "Outlooks were mostly positive, with growth expected to continue at a slight to moderate pace ..." and mild inflation. But the report described both consumption and manufacturing as mixed at best. The recent data is best described as tepid, but concerns over the consumer suggest weaker growth than previously expected.

Europe

Germany: Economic sentiment on a high

The Ifo Business Climate Index climbed to a 30-month high of 110.5 in October, extending the September rebound (109.5) with both the current (to 115.0 from 114.7) and expectation component (to 106.1 from 104.5) rising. This is in line with the increases of the headline ZEW Economic Sentiment Expectations Index to 6.2 (from 0.5) and the ZEW Present Sentiment Index to 59.5 (from 55.1). Moreover, the October flash PMI Composite Output Index rose to 55.1 (from 52.8) as a result of a strong rebound in the Services Activity Index (to 54.1 from 50.9) and a further increase in the Manufacturing Output Index (to 56.9 from 56.4). Meanwhile, the GfK Consumer Climate Indicator edged down to 10.0 in October (from 10.2) and is forecast at 9.7 in November. However, it remains well above the long-term average (5.6 since 2001) and the Economic Expectations component continued to increase. Euler Hermes maintains its GDP growth forecasts of +1.8% in 2016 and +1.7% in 2017.

Africa & Middle East

Nigeria: Once upon a time a credit crunch

Evidence of liquidity shortages are mounting in Nigeria. Access to dollar liquidity on the interbank market was tightened in August. More recently, Naira's notes were made scarcer in order to balance with already scarce dollars and stabilize the exchange rate. The official rate is about 315 NGN/USD since end-august, but the unofficial one depreciated a bit more and the black market premium is nearing 40% and the inflation rate was +18% y/y in September. As a result of these limitations, an increasing number of businesses fall short of liquidity in order to run their current operations and pay their imports. Since 75% of operations are paid in cash, access to cash is a key precondition to run a business. In conclusion, the import cover of foreign exchange reserves remains quite good (6.5 months of imports), as reserves hold on but imports plummet, crowding out private sector business conditions. We forecast -2.3% GDP growth in 2016.

Asia Pacific

Japan: Towards gradual improvement ?

Last indicators show mixed signals. Deflationary pressures increased further in September with producer prices declining by -3.2% y/y. On activity, exports are still a matter of concern (down -6.9% y/y in September) hindered by lower demand from ASEAN markets and the US. By contrast, some advanced indicators show signs of improvement. Bank lending accelerated slightly in September (+2.2% y/y from +2%). Business sentiment gained some traction: manufacturing PMI rose to 51.7 in October (from 50.4 in September) thanks to a rise in output and new orders. Looking ahead, GDP growth is set to pick up speed gradually. Both monetary and fiscal stimulus should start to bear fruit in Q4, leading to a gradual rise in activity. Yet, downside risks are still significant and stem from low demand growth from overseas.

What to watch

- October 27 – US September durable goods order
- October 27 – UK Q3 GDP
- October 28 – France Q3 GDP
- October 28 – Spain Q3 GDP
- October 28 – US Q3 GDP
- October 31 – Mexico Q3 GDP
- October 31 – Germany September retail sales
- October 31 – Eurozone Q3 GDP
- October 31 – US September personal income
- November 1 – US September ISM manufacturing index
- November 1 – Nigeria Manufacturing PMI
- November 2 – EU October Manufacturing PMI
- November 2 – US Fed policy announcement
- November 3 – UK monetary policy decision
- November 3 – Brazil October Manufacturing PMI

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