

FIGURE
OF THE WEEK

+EUR 9 bn

France's y/y
export gains
in January-
April 2019

In the Headlines



Germany: Very weak start to Q2

The German economy's start to the second quarter proved very disappointing. German exports and industrial production recorded their sharpest declines since August 2015, exposing the continued vulnerability of Europe's largest economy to political uncertainties related to global trade as well as Brexit. Exports fell -3.7% while industrial output dropped -1.9% compared to the previous month, driven by a marked decline in the production of investment and intermediate goods. New orders in the manufacturing sector provided a welcome ray of light with a seasonally adjusted gain of +0.3% in April compared to the previous month, while the value for the month of March was slightly corrected upwards (+0.8%). Excluding bulk orders, the increase was even significantly stronger (+2.1%). However, the most recent order figures are hardly a reason to sound the all-clear: The tentative trend reversal in foreign demand observed in early 2019 could quickly vanish into thin air again in view of the recent intensification in the U.S.-China trade dispute, and there are initial signs that the weakness in industry is also increasingly weighing on German domestic demand. Expect German economic momentum to remain subdued for the coming quarters with risks tilted to the downside.



UK: Contingency stockpiling will accelerate in Q3 again

Stocks have increased continuously since Q1 2018 – and accelerated markedly in Q1 2019. An adjustment is ongoing, indicated by figures for monthly GDP which was down -0.1% m/m in March and -0.4% in April. Manufacturing output even fell -3.9% m/m in April. Services showed signs of weakness as well (flat m/m in April) after being artificially driven by wholesale & retail as well as information & communication previously, most probably linked to Brexit preparations. Hence, we expect stocks to subtract -0.4pp from Q2 GDP growth after adding +0.8pp in Q1. The race for the next PM in the UK looks tight and increases the uncertainty. The expected appointment by 22 July would not allow enough time for renegotiating the Irish backstop which most of the candidates want. A new extension of Article 50 is likely (until mid or end-2020) possibly accompanied by a referendum. Yet, given the hard stance on both sides (UK and EU), overall uncertainty as well the no deal probability (from 25% to 40%) are likely to increase. Hence, UK companies will accelerate stockpiling again in Q3. We expect GDP growth of +1.2% in 2019 and +1% in 2020.



France: The worse, the better?

Exports made their best start since 2011, with gains of +EUR9bn in the first four months of 2019. Grain and luxury were the most unexpected overperformers. Africa made +EUR850mn of export gains, the first increase since 2015 mainly explained by rising grain exports in a region affected by poor rains. Overall, luxury is the strongest overperformer with +EUR2bn of additional exports, perhaps reflecting a flight to quality in a world economy surrounded by multiple economic uncertainties. Aeronautics (+EUR2.8bn) and chemicals (+EUR1.7bn) were the other two strong (usual) performers. Otherwise, concerns remain in the car value chain, since French car suppliers' export losses widened to -EUR0.4 bn. In the EU, the UK (+EUR1.8bn, in precautionary stockpiling nurtured by the first Brexit deadline) and Italy (+EUR0.7bn despite poor GDP growth prospects of +0.2% in 2019) accounted for the largest export gains. Outside of the EU, China (+EUR1.3bn) and the U.S. (+EUR1.1bn) took these roles. Overall, we expect lower export growth in H2 and French export gains to reach +EUR14bn in 2019.



Poland: Economy slows gradually, corporate risks rise

Second estimates show that Q1 GDP growth eased to +4.7% y/y from +4.9% in Q4 2018. Consumer spending growth moderated to +3.9% y/y, but public spending rose by +6.4% thanks to fiscal stimulus ahead of the elections in fall and fixed investment surged by +12.6% in Q1 on the back of a continued strong utilization of EU funding for eligible projects. However, inventories subtracted -1.6pp from Q1 growth. External trade activity eased in Q1 as demand from the Eurozone cooled, with exports expanding by +5.9% y/y and imports by +5%, so that net exports contributed +0.7pp to growth in Q1. Meanwhile, [Poland's corporates continue to face headwinds](#). Despite the economic boom over the past few years, non-payment risk has risen since 2016, reflected in an average annual increase of +10% in corporate insolvencies in 2016-2018. We expect insolvencies to increase by another +10% in 2019, posing particular risks to large-scale suppliers of Polish companies.

Countries in Focus

Americas

U.S.: Employment slowing, odds of Fed cuts rising

The May employment report was a major disappointment, showing job gains of only +75k vs. expectations of +180k, and downward revisions of -75k from the previous two months. Job growth has been slowing over the past three, six, and 12 months. Weakness was widespread across most industries. Wages disappointed too as the y/y rate fell to +3.1% from +3.4% three months ago. The unemployment rate remained unchanged at 3.6%, and the participation rate was also unchanged at 62.8%. The report adds to a growing body of evidence that the economy is slowing and the odds of a recession are rising. In addition, the Fed Funds futures market shifted dramatically last week and is now pricing in at least two full cuts this year, with the first one coming in July. A separate report showed weak inflation, as the increase in headline producer prices fell from +2.2% to +1.8%, the lowest in over two years. The less volatile core inflation rate slipped from +2.4% to +2.3%.

Ukraine: Political uncertainty and economic slowdown

Last week, Ukraine's new President Volodymyr Zelensky made his first foreign trip since his inauguration on 20 May, visiting officials of the EU and NATO in Brussels. He reconfirmed Ukraine's commitment to aim for accession to both institutions. However, this move is likely to complicate the restart of peace talks with Russia and end the war with Russia-backed separatists in east Ukraine, a goal that Zelensky has declared as his top priority. On the economic front, Q1 real GDP growth decelerated markedly to +0.2% q/q (from +1.1% in Q4) and +2.2% y/y (from +3.5% in Q4). Details have not been released as yet but monthly indicators suggest that the industrial sector was a key drag on Q1 growth. Industrial production contracted by -0.8% y/y in Q1 2019, compared to -0.4% in Q4 2018 and +2.9% y/y growth in Q1 2018. However, the sector rebounded to +5.3% y/y growth in April 2019. Overall, we forecast full-year GDP to expand by +2.4% in 2019 (after +3.3% in 2018) and +2.5% in 2020.

Africa: When it does not rain, it still pours

Africa's growth in 2019 is set to be cut widely from +2.8% in previous estimates to just +2% due to abnormally low rains in various parts of the continent, especially in the east, south and north. This has two consequences:

(i) Agricultural output and exports will be hit hard and, in some cases, these countries will even need to import (particularly grain). (ii) Low water resources will constrain power generation, acknowledging the fact that hydro-power generation in Africa is above the world average. As a consequence, countries with energy-intensive sectors (e.g. mining) will feel the pain. It can also contribute to a risk of social discontent and/or to fiscal sustainability in highly subsidized countries, which is already the case in Sudan, Algeria or Zimbabwe (see [WERO 17 April 2019](#)). More generally, it also shows how deep the gap between growth plans and current water resources capabilities can be (see [WERO 21 March 2019](#)). Among others, rains below normal are fundamental drivers triggering growth revisions in 2019 for [South Africa](#), [Morocco](#) and [Zambia](#) (to 0%, +2%, and +1.5%, respectively).

Thailand: Losing momentum

Q1 real GDP growth decelerated to +2.8% y/y (+3.6% in Q4) as sluggish external demand hit exports (-4.9% y/y). Consumer spending (+4.6%) and fixed investment (+3.2%) slowed down in Q1; only public spending (+3.3%) gained momentum while inventories added a strong +2.8pp to Q1 growth. Going forward, we expect Thailand to remain affected by the global slowdown in trade and the uncertainty surrounding the U.S.-China trade feud. While fiscal stimulus and accommodating monetary policy should partially offset the effects of the deteriorating external environment, ongoing policy uncertainty might undermine business and consumer confidence to some extent, and could limit the growth momentum in the near term. After the general elections in spring 2019, no party had a majority of seats in the House of Representatives. But it looks now as if a pro-military coalition has been formed that will support the continuation of a military-led civilian government. As a result, policy delays are likely to continue as well. Overall, we expect full-year growth to slow to a still solid +3.4% or so in 2019 (after +4.1% in 2018).

What to watch

- June 13 – Eurogroup meeting
- June 14 – Poland May inflation
- June 14 – Russia Central Bank meeting
- June 14 – Turkey April balance of payments
- June 14 – U.S. May industrial production
- June 14 – U.S. May retail sales
- June 18 – Eurozone April trade
- June 18 – Eurozone May inflation
- June 18 – Turkey April industrial production
- June 18 – U.S. May housing starts
- June 19 – Eurozone April construction output
- June 19 – UK April house prices
- June 19 – UK May inflation
- June 19 – U.S. Federal Reserve policy announcement
- June 20 – UK Bank of England monetary policy meeting

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