Euler Hermes Economic Research

Weekly Export Risk Outlook

17 May 2017

FIGURE OF THE WEEK

+5.6%

Q1 2017 y/y GDP growth in Romania (flash estimate)

In the Headlines

U.S.: Manufacturing improving but consumer still dawdling

Manufacturing industrial production gained +1% m/m in April, the most in 39 months, while the y/y rate rose to +1.7%, the most in 28 months. Motor vehicles reversed recent weakness and gained +5% m/m, sending the y/y rate from +0.8% to +4%. Fifteen of 19 industries expanded in April. The report confirms anecdotal evidence and other data from the improving manufacturing sector. However, retail sales disappointed; after two weak months, expectations had been for an increase of +0.6% m/m, but the actual gain was only +0.4% m/m, pushing the y/y rate down from +4.8% to +4.5%. “Core” sales which feed into the GDP calculation rose only +0.2% m/m, as the y/y rate fell from +3.6% to +2.9%. Inflation data was mixed as producer prices rose +0.5% m/m, to +2.5% y/y, the highest in 63 months, while the core rate gained +0.4% m/m, to +1.9% y/y, the highest in three years. Conversely, despite small monthly gains, consumer prices on a y/y basis fell to +2.2% from +2.8% in February, and the core rate also fell -0.1pp to +1.9% y/y, the lowest in 21 months. While the news on manufacturing is strong, and housing and inflation data is mixed, the all-important consumer continues to dawdle.

UK: Possible rate hike in 2018?

The BoE kept its monetary policy stance unchanged last week: the key interest rate was held at +0.25% (7 to 1 majority), government bond purchases at GBP435bn and corporate bond purchases at up to GBP10bn (both with unanimous majority). The BoE assumes that Brexit will unfold smoothly but noted uncertainties around the process, notably with regard to households’ financial strength. Based on the assumption of an orderly EU exit after 2 years of negotiations with no transition arrangement (vs. a 2-year transition period expected by Euler Hermes), the BoE revised its GDP growth forecasts: down from +2% to +1.9% for 2017 but up by +0.1pp for each of the following two years, to +1.7% for 2018 and +1.8% for 2019. We expect +1.4% in 2017, +1% in 2018 and +0.9% in 2019. Further, the BoE’s inflation forecast was raised to +2.7% from +2.4% for 2017, followed by +2.6% for 2018 (from 2.8%) and +2.2% for 2019 (from 2.5%). These are broadly in line with our forecasts. The BoE signaled a possible interest rate increase as early as next year should the economy surprise on the upside. However, we continue to expect no rate hike throughout the whole Brexit process (until 2021).

Central and Eastern Europe: Gaining strong momentum

First estimates indicate that real GDP growth in the group of 11 EU members in the CEE region regained substantial momentum in Q1, accelerating to around +3.9% y/y (from +2.8% in Q4 2016). The key driver of this rebound was once again **Romania** which posted +5.6% y/y growth in Q1 (+5% in Q4), thanks to continued strong domestic demand that has been supported by fiscal stimulus. Headline inflation is still low (0.6% y/y in April) thanks to successive VAT cuts over the past 2 years; nonetheless risks of overheating should be monitored. Elsewhere, seasonally adjusted real GDP picked up to +4.1% y/y in both **Poland** and **Lithuania**, to +3.9% y/y in **Latvia** and to +3.7% y/y in **Hungary**, mainly driven by strengthening performances in both industry and services, as well as in construction in **Poland** and **Latvia**. Strong external demand, supported by consumer spending, led growth in the **Czech Republic** strengthen to +2.9% y/y. Q1 growth in both **Slovakia** (+3.1% y/y) and **Bulgaria** (+3.4% y/y) remained robust and nearly unchanged from the previous quarter. We expect average full-year growth of the 11 EU members in the CEE to pick up to +3.2% in 2017 (+2.9% in 2016).

China: Game of Trade Initiatives

Fears of a trade war eased over the past few days as China and the U.S. signed a 10-point agreement in which China agreed to open its market for specific U.S. corporates, especially beef and LNG exporters, credit card providers and rating agencies, while the U.S. made concessions on poultry imports from China and promised fair treatment of Chinese banks in the U.S. Moreover, China hosted the Belt and Road Forum, where it welcomed around 1500 delegates, including 29 heads of states and government leaders to discuss ways to boost international cooperation and connectivity. At this occasion, China committed to provide at least USD113bn in extra-funding for the One Belt One Road Initiative. Assuming that the project attracts further funding going forward, it could act positively on the global investment cycle through a boost in infrastructure investment as well as on trade, especially of capital goods and basic materials.

Countries in Focus

Americas

Latin America: Exports are (finally) back

After two years of tough headwinds, an upturn on export revenues has been visible since the beginning of the year. We estimate merchandise exports in Q1 rose by +EUR8.2bn in Mexico (50% thereof to the U.S.), by +USD6.2bn in Brazil, by +USD4.9bn in Peru and by close to +USD1bn in Argentina, Ecuador and Colombia. These positive developments are expected to strengthen over the next months on the back of: (i) good crop forecasts, notably soy and corn harvests in Brazil and Argentina; (ii) increasing commodity prices that are benefiting both agriculture (Brazil, Argentina, Peru) and energy exporters (Colombia, Peru, Ecuador, Mexico); (iii) the gradual recovery of global trade which we expect to rise this year by +3.3% in volume and +3.6% in value. As a consequence, currencies have appreciated since the beginning of the year, with Mexico being on top. The appreciation is expected to continue throughout 2017, erasing at least the losses suffered in 2016.

Europe

Netherlands: Strong investment drives growth

Real GDP increased by +0.4% q/q in Q1, down from an average +0.7% q/q in 2016. However, excluding stocks, growth reached a strong +0.8% q/q. Investment posted the highest rise, with +1.9% q/q for construction and +15% q/q for machinery investment. Residential building registered strong growth thanks to the recovery in consumer confidence (to the highest level since 2007), rising employment and low real interest rates which all continued to boost housing permits (+36% y/y in Q1) and prices (+5.7% y/y in Q1). The manufacturing industry also increased at its fastest pace since the start of 2011, especially machinery, transport equipment and chemicals, thanks to an acceleration in demand from abroad. Consumer spending fell slightly (-0.1% q/q) mainly due to lower spending on food and natural gas while spending on services (notably hotels and restaurants) accelerated. Overall we expect GDP to grow by +2% in 2017.

Africa & Middle East

Nigeria: Recovering gradually

The Parliament just approved an increase in spending by +21%. This should help the economy to recover from a recession (GDP contracted by -1.5% in 2016) but the stimulus is not as strong as expected, compared to the forecast nominal GDP growth rate of +16% in 2017. Moreover, fiscal spending implementation is generally relatively weak and slow. In 2016, for example, flaws in public finance added to the credit crunch in the overall economy. However, the outlook is slightly more positive this time. Overall risk appetite in the world economy as well as financial flows to Emerging and Frontier Markets are recovering. Moreover, the easing of capital controls in Nigeria has somewhat reduced dollar scarcity in the economy. As a result, GDP growth is forecast to recover to +1% in 2017. But since oil prices are not recovering strongly, the fiscal deficit should worsen to -6% of GDP or so (-5.5% in 2016). However, there is no solvency issue since public debt is still quite low at about 16% of GDP.

Asia Pacific

Hong Kong: An export-led acceleration of GDP growth in Q1

Economic growth accelerated significantly to +4.3% y/y in Q1. Exports of goods surged by +9.2% y/y, supported by strong demand from Mainland China. Domestic demand continued to record solid growth. Private consumption expanded firmly at +3.7% y/y. Investment gained some traction, rising by +6.4% y/y in Q1 (up from +5.6% in Q4 2016) reflecting rising activity in construction. Going forward, real GDP growth is set to remain solid but will lose some momentum in H2, resulting in full-year 2017 growth in the range of +2.5% to +3%. Export growth is set to decelerate to a more sustainable pace as China's economic performance is expected to moderate owing to less supportive credit conditions. Domestic demand in Hong Kong should remain resilient thanks to a strong labor market and positive income growth supporting private consumption.

What to watch

- May 18 – Japan Q1 GDP
- May 18 – Philippines Q1 GDP
- May 19 – Canada March retail sales
- May 19 – Iran presidential election
- May 19 – Italy March current account balance
- May 19 – Malaysia Q1 GDP
- May 19 – Poland April industrial production
- May 19 – Russia April industrial production
- May 23 – France May business confidence
- May 23 – Germany Q1 GDP (with details)
- May 23 – Germany May IFO business climate
- May 23 – Hungary Central Bank meeting
- May 23 – U.S. April new home sales
- May 24 – Bank of Canada policy statement
- May 24 – Croatia Q1 GDP (flash estimate)
- May 24 – U.S. April existing home sales

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