Euler Hermes Economic Research

Weekly Export Risk Outlook

10 March 2016

In the Headlines

FIGURE OF THE WEEK

-13.8%

Decline (y/y) in Chinese USD-denominated imports in February

Eurozone: Further and better quality monetary easing

The ECB has reinforced its monetary policy. As expected, it cut its key interest rates: -5bps to 0% for the refi rate and -10bps to -0.4% for the deposit rate and it expanded its quantitative easing (QE) programme to EUR80bn each month from EUR60bn. Positive news came from the change in the type of assets purchased to investment-grade, non-financial corporation bonds, while expanding the limit of sovereign bond purchases (to 50% per issuer from 33%). Buying corporate debt will ease financing costs for corporates and improve their profitability. In addition, the ECB decided to launch another series of four-year, targeted and longer-term refinancing operations (TLTRO II) starting in June, with the last operation set to mature in 2021. This should offer attractive financing conditions for banks (today at 0%) and, in turn, further ease private sector financing conditions as banks will have access to even cheaper liquidity if they increase their loan portfolio. ECB President Mario Draghi said that measures on interest rates would progressively give way to non-conventional measures, said to be more efficient. We believe the ECB will act again at the end of 2016 to support inflation recovery. The ECB expects inflation at +0.1% in 2016, +1.3% in 2017 and +1.6% in 2018.

U.S.: Strong job growth, but the Fed to stay on hold

The economy gained a strong +242,000 jobs in February and the previous two months were revised up +30,000. However, hourly wages declined -0.1% m/m, only the second fall in over three years, sending the y/y rate to +2.2% from +2.6% just two months ago. We see virtually no likelihood of a Fed hike next week and perhaps two, at the most, in 2016. The ISM non-manufacturing index in February slipped to 53.4 (53.5 in January) but still signals expansion. The details are positive as eight of ten components are above 50, with new orders a strong 55.5 despite slipping -1pts, and export orders rebounded to 53.5 from 45.5. Core factory orders increased +3.4% m/m but are still down -3.2% y/y. The trade deficit deteriorated more than expected in January, to -USD45.7bn from -USD44.7bn, as exports, negatively affected by the stronger USD, fell -2.1% m/m and imports slowed -1.3% on weak demand. The Fed's Beige Book of anecdotal evidence paints a mixed picture as consumption increased overall but several Fed districts reported a downturn. Productivity in Q4 2015 fell -2.2% q/q annualised.

Italy: Not bad, but still weak

A breakdown of Q4 2015 GDP data gives a more positive picture than the superficially meagre overall growth of +0.1% q/q suggests. Excluding stocks, GDP increased by +0.5% q/q, mainly resulting from consumer spending growing slightly (+0.3% q/q), higher public spending (+0.6% q/q) and an acceleration in investment (+0.8% q/q). The rebound in exports by +1.3% q/q, although somewhat offset by more dynamic import growth of +1% q/q, also contributed to overall growth. GDP in full-year 2015 increased at a relatively slow pace (+0.6%), with exports the main contributor (+1.2pps). Indeed, exports grew at the highest pace since 2011 (+4.1%), reflecting the positive impact of a weaker EUR. Consumption picked up by +0.9% in 2015, helped by lower oil prices. Meanwhile, the increase in demand and improving financing conditions are likely to continue to support investment, which increased by +0.6% in 2015 after seven consecutive years of contraction. These positive indicators suggest a moderate acceleration in 2016 and we forecast GDP growth of +1.1%.

Egypt: Sphinx-like riddles

Business challenges are compounded by global headwinds, including weak oil prices that reduce earning capacity from the Suez Canal and Sumed pipeline and a weak recovery in Europe that slows inward investment and tourism flows. Policy responses have caused further uncertainties at the corporate level. Monetary policy will remain restrictive, given the CBE's mandate to guard against inflationary pressures (double digit growth) and the EGP will be gradually weakened. Of particular current concern are recent restrictions on access to foreign exchange. These regulations require careful interpretation because of exemptions and exclusions but they include an increase in the required monthly foreign currency deposits at the CBE for some importing companies. This week, the CBE issued further changes aimed at easing restrictions on foreign exchange for companies that import "basic commodities". The regulatory confusion increases payment delays (non-payment risks are also higher) and complicates commercial transactions.

Countries in Focus

Americas

Latin America: Currency risk remains strong

The main currencies of the region have appreciated since the beginning of March, reflecting a recovery in commodity prices. The Brent oil price is up +12.7% since the beginning of the month and copper prices +4.6%. As a result, in the past 10 days, the **Brazilian** real (BRL) gained +5% against the USD, the **Mexican** peso (MXN) +1%, the **Colombian** peso (CBP) +6% and the **Peruvian** Nuevo sol (PEN) and the **Chilean** peso (CLP) +2%. This does not compensate for the currency falls over the past 18 months: the BRL lost -55% from its peak in June 2014, the CBP -52%, the MXN -31%, the PEN and the CLP -20%. Moreover, this recovery could be short-lived, given longer-term downward pressures on commodity prices, weak global trade, the slowdown in China and reticence of major oil producers to cut output. Additionally, financial markets will continue to encounter uncertainty and high volatility. As a result, currency risk will remain one of the major hazards when trading with the region.

Europe

Croatia: Finally out of recession

After six consecutive years of annual GDP contraction, the economy returned to growth, with +1.6% expansion in 2015 reflecting a moderate recovery in domestic demand. Private consumption increased by +1.2%, government consumption by +0.6% and fixed investment by +1.6%. Exports expanded by +9.2%, outpacing imports at +8.6%, so that net exports made a positive contribution of +0.5pps to growth in 2015. Euler Hermes expects the recovery will gradually gain momentum, resulting in growth of around +1.8% in 2016 and +2% in 2017. However, the level of annual GDP will remain approximately -10% below the peak reached in 2008. Country risk is also gradually improving. The current account has been in surplus since 2013, surging to around +4.5% of GDP in 2015, and is likely to remain so in 2016-17. However, total external debt remains very high (108% of GDP in 2015), a legacy of large current account deficits in the past. And public debt increased to 90% of GDP in 2015 (34% in 2007).

Africa & Middle East

United Arab Emirates: Private means

As with all oil exporters, the economy is adjusting to a period of low international prices. Export revenues have weakened, GDP growth is slowing – the IMF recently stressed that it is a slowdown and not a contraction – and January's PMI was down to 52.7 (53.3 in December 2015). While still signposting expansion, the PMI indicates that business conditions for the non-oil private sector, in particular, are more challenging. New orders are increasing at the slowest pace since the end of 2010, new export business appears to be stagnating and credit availability is tightening. For the economy overall, FX reserves currently provide an import cover of around three months but the UAE controls SWFs of over USD1,200bn (USD770bn in ADIA) and the state's financial cushion is therefore extensive and underpins its reform strategy. EH expects GDP growth of around +2% in 2016 and +3% in 2017, although expansion could be higher if sanctions relief in Iran engenders greater regional trade growth.

Asia Pacific

China: Preparing the ground

Recent economic releases are disappointing. USD-denominated exports contracted by -25.4% y/y in February, imports fell by -13.8% and producer prices declined for the 48th consecutive month (-4.9% y/y). Meanwhile, the government unveiled its economic targets for this year. As we expected, growth targeting was relaxed, with a 2016 GDP growth range between +6.5% and +7% and expectations are now lower than last year (+7% in 2015). Moreover, the authorities did not provide a detailed outlook for external trade, reflecting: (i) last year's target of +6% expansion in trade was completely missed; (ii) the current external environment is very challenging. The government expects domestic demand will remain the main growth driver, supported by further fiscal stimulus (the deficit target is now -3% of GDP, from -2.3%) and a more accommodative monetary policy. Quickening the pace of reforms (including SOE restructuring and overcapacity reduction) will be at the centre of the policy agenda.

What to watch

- March 11 – Canada February unemployment
- March 11 – Germany February CPI
- March 11 – Poland interest rate decision
- March 15 – U.S. February producer prices
- March 15 – U.S. February retail sales
- March 15 – Poland February CPI
- March 15 – Venezuela January CPI
- March 15 – Brazil December unemployment
- March 15 – Italy January general government debt
- March 16 – U.S. February consumer prices
- March 16 – U.S. February housing starts and permits
- March 16 – U.S. February industrial production
- March 16 – U.S. Fed policy statement and forecasts
- March 16 – UK February unemployment
- March 16 – Russia February industrial production
- March 17 – UK BoE bank rate decision
- March 17 – South Africa interest rate decision
- March 17 – EU summit

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