Euler Hermes Economic Research

Weekly Export Risk Outlook

20 July 2016

In the Headlines

FIGURE OF THE WEEK

+6.7%

Q2 2016 y/y GDP growth in China

Turkey: Economic impact of failed coup likely to be limited

On 15 July, a small faction within the Turkish military attempted a coup which, however, failed within hours as there was neither public nor political backing, including from the opposition, for it. President Erdogan and the ruling AKP government are back in full control of the country. The immediate impact has been increased volatility on financial markets – as of today the TRY is down by about -6% against the USD and the ISE 100 is down by -8% as compared to pre-failed coup – which may continue in the next days or weeks. However, the Central Bank of Turkey (CBT) quickly announced it was ready to take any measures to ensure financial stability, if needed. And yesterday the CBT continued its gradual monetary easing cycle, lowering the overnight lending rate by 25bps to 8.75% while keeping the overnight borrowing rate at 7.25% and the key one-week repo rate at 7.5%, in line with expectations prior to the coup attempt. Euler Hermes does not expect a lasting, significant impact of the incident on the economy and maintains, for now, its forecast of full-year GDP growth of +3.6% in 2016. That said, country risk had already increased over the past three years and remains high, mainly reflecting (i) ongoing large current account deficits that are largely financed through short-term external debt which carries the risk of sudden reversal if investor sentiment changes; and (ii) increased political uncertainty and security risk as a result of spill-overs from the Syrian War and a series of terrorist attacks.

China: Faster, stronger, better? Not really…

Real GDP grew by +6.7% y/y in Q2 (unchanged from Q1) supported by a steady rise of tertiary sector activity (+7.5% y/y) and improved secondary sector production (+6.1%). In q/q terms, GDP growth accelerated to +1.8% in Q2 (from upwards revised +1.2% q/q in Q1) as a result of a strong stimulus. Monthly indicators were broadly positive except for investment. Real industrial production was up by +6.2% y/y in June (+6% in May). Nominal retail sales of consumer goods rose by +10.6% y/y. Growth of nominal urban fixed asset investment decelerated further (+9% y/y in Jan-Jun) with lower investment in the secondary sector and weaker private investment growth. Looking ahead, downside risks are still elevated. First, lower private investment and weaker business sentiment in manufacturing suggest lower activity growth in the short-run. Secondly, modest growth in global demand weighs on market opportunities. The weaker RMB helps ease the pain through improved competitiveness but weak export orders are still acting as a drag. For now, EH maintains its growth forecast of +6.5% for 2016.

Eurozone: Improving credit demand and supply

Banks reported looser credit conditions in Q2 for both corporates and households. Corporates in France, Italy and Germany were the main winners while for households, France, Italy and Spain were on top of the list. Banks expect broadly unchanged credit conditions on loans to corporates in Q3 while they expect a net loosening for loans to households. Increasing competition among banks is the main factor for the easing of credit conditions. In terms of demand, a positive trend has also been observed. For corporates, the overall low levels of interest rates are supportive for increasing credit demand, notably for financing M&A activities, inventories and working capital. For households, in addition to the low level of interest rates, improving housing market prospects and better consumer confidence are supportive for increasing credit demand. Banks have not yet reported any negative expectations for lending standards post Brexit. The Q3 survey to be published at end-October will be key to follow.

U.S.: Consumption strong, manufacturing and housing tepid

Consumption is on the rise as retail sales gained +0.6% m/m in June, the third consecutive increase. Ex-auto and gasoline sales rose +0.7% m/m to a strong +4.7% y/y. Although consumption was robust in Q2, we still maintain our 2016 GDP forecast at +1.9%, in part because manufacturing and housing are still weak. Manufacturing industrial production rose +0.4% m/m in June to a +0.4% y/y rate, well below the long-term average of +2.3%. Autos led the way with a +5.9% m/m surge. Ex-auto, manufacturing production fell by -1.2% y/y, an indicator that has been negative for 13 of the past 14 months. Housing starts rose +4.8% m/m and permits gained +1.5%. However, on a y/y basis, they are both falling at -2.0% and -13.6%, respectively. Inflation remains tame as consumer prices increased by 1.1% y/y in June, with core inflation (ex-food and energy) at 2.2% y/y. Producer price inflation was even weaker at 0.3% y/y with a core rate of 1.3% y/y.

Countries in Focus

Americas

Mexico: Losing traction

A relatively depressed manufacturing sector is dragging down the Mexican economy. Industrial production has fallen by -1.2% y/y since the beginning of the year, while business confidence has deteriorated strongly since April. Industrial corporates are suffering from slower industrial output in the United States (which accounts for 80% of Mexican industrial exports) and from tighter financing conditions. The Central Bank raised its key policy interest rate in late June by +50bps (+125bps since December 2015) to 4.25%, in an attempt to contain the negative impact of the Brexit vote on the Mexican peso. Although private consumption remains solid (retail sales expanded by +8.6% y/y in May) thanks to low inflation and increasing employment, wages and remittances, we expect economic growth to decelerate to +0.5% q/q in Q2, after +0.8% in Q1. Overall, real GDP should expand by +2.5% in full-year 2016, the same pace as in 2015.

Europe

France: Growth has strong foundations, but should be bumpy

The attacks in Nice are likely to have an impact on the private sector, however, not a long-lasting one. The expected impact should be on consumer confidence and as a result on private consumption. Last year's attacks affected consumption growth during Q4 (down to a mere +0.1%). As a result, corporates accumulated strong inventories in Q4 and industrial production was affected during the following months. But consumption recovered very strongly in Q1 (+1.1%). A similar bumpy growth profile is possible now, but Euler Hermes is confident on trend growth prospects (forecast at +1.5% this year and next). Growth foundations are strong. Households are wealthy (their financing capacity is about 3.5% of GDP each year), the worst is behind for the labour market, corporate margins are recovering quickly (from 29.8% in Q4 2013 to 32.1% in Q1 2016) and cheap credit conditions and building materials are bright spots for the construction sector.

Africa & Middle East

Israel: Upwards (revisions) and outwards (outlook)

Consumer prices on an annual basis have remained in a deflationary trend since September 2014, despite near-zero interest rates (the benchmark policy rate has been 0.1% since February 2015). Consumer price inflation in June increased for the third consecutive month (0.3% m/m) after five months in decline but this was still -0.8% y/y, compared with an official target range of 1% to 3%. Expect monetary policy to remain accommodative. Meanwhile, Q1 GDP growth was again revised upwards, to an annualised +1.7% q/q from +1.3% in the previous estimate and +0.8% in the original data. Part of the revision reflects an improvement in export data, with shipments declining by -5.3% in Q1 rather than -8% in the earlier estimate. EH expects GDP growth of around +3% in 2016. With regional tensions (Syria and Lebanon) now compounded by uncertainties relating to Turkey, key trading links will remain with the U.S. (27% of exports and 12% of imports), Europe and Greater China.

Asia Pacific

Singapore: Good or bad news?

Based on advance estimates, real GDP grew by +2.2% y/y in Q2 (after +2.1% in Q1) benefitting from strong base effects. On a q/q seasonally adjusted annual rate (saar) basis, GDP growth accelerated to +0.8% (up from +0.2% in Q1) due to a recovery in services (+0.5% q/q saar). Activity in manufacturing (+0.3% q/q saar, down from +18.4% in Q1) and construction (+0.6%, down from +3.5%) continued to expand but the strong growth deceleration indicates that economic performance is not stable yet. Going forward, we see limited scope for improvement. Business surveys still point to a weak outlook, signalling declining production and new export orders. In order to combat this economic downturn, the government has enacted an expansionary budget for 2016 with measures to support business (tax rebates, favourable lending conditions) elderly and needy households. This should help to boost domestic demand. Euler Hermes expects full-year GDP growth of +1.6% in 2016.

What to watch

- July 21 – Eurozone ECB monetary policy meeting
- July 21 – U.S. June existing home sales
- July 21 – South Africa SARB interest rate decision
- July 21 – Brazil July IBGE Inflation IPCA-15
- July 21 – Ukraine June industrial production
- July 22 – Eurozone July PMIs (flash estimates)
- July 25 – Austria May industrial production
- July 25 – Brazil July Consumer Confidence
- July 25 – Germany July Ifo business climate
- July 26 – U.S. June new home sales
- July 26 – U.S. July consumer confidence
- July 26 – Hungary interest rate decision
- July 27 – Germany July GfK consumer confidence
- July 27 – Germany June retail sales
- July 27 – U.S. June durable goods orders
- July 27 – U.S. Federal Reserve policy statement
- July 27 – UK Q2 GDP (preliminary estimate)

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Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com