

Euler Hermes Economic Research

Weekly Export Risk Outlook

23 October 2014

FIGURE OF THE WEEK

+7.3%

China's Q3 y/y GDP growth

In the Headlines

China: Resilience in Q3 reflects export boost

GDP increased by +7.3% y/y (+1.9% q/q) in Q3 following +7.5% y/y (+2% q/q) in Q2. The supply side breakdown reveals that the slowdown stemmed from weaker growth in construction (+9% y/y from +9.2% in Q2) and services (+7.9% y/y from +8%), particularly those related to real estate and finance. Growth in the primary sector strengthened in Q3 (+4.2% y/y from +3.9%) as a result of improved financing conditions for rural companies, following successive accommodative measures between April and June. On the demand side, investment remained the main drag on growth, reflecting the weak performance of the property market. Overall, the main growth driver in Q3 was external trade, with exports up +13% y/y (+5% in Q2). Against this background, we expect GDP growth will accelerate moderately in the coming quarters as further targeted macro-measures will help offset the negative effects feeding through from further local government fiscal consolidation and from continuing weakness in the property sector. We expect GDP growth of +7.4% in 2014 and +7.3% in 2015.

France: No light yet at the end of the corporate tunnel

The business climate index in October was unchanged at 91 (compared with 94 in June), still below its long-run average of 100. The turning-point indicator remained at a very unfavourable level of -1 for the third consecutive month. Manufacturing went back up to its July level (97) but Building Construction continued its rapid fall and reached its lowest level since December 1996 (88). The deterioration in Retail Trade was halted at 90, but the index is markedly below July's figure (99) and back to August 2013 levels. The outlook for Services is relatively better, with business confidence in October up +1 point to 93. All in all, these figures confirm our subdued outlook for the rest of the year…which may be even more restrained that initially expected. This also means that company turnover, which is falling by -0.5% to -1% on average, will not rebound before 2015. Given our forecast of around +1.8% nominal growth in 2015, we expect a moderate +1% (at best) increase in turnovers next year.

U.S.: Cloudy growth picture, but low inflationary pressures

Recent economic data continue to provide mixed signals, with strong industrial output, weak retail sales and an erratic housing market. Industrial production increased by +1% m/m in September, driven by a sharp jump in utilities, and manufacturing was up +0.5% m/m, putting it at a robust 3.7% y/y. Retail sales fell -0.2% m/m in September, the first decline in nine months, and the weakness was widespread with the only positive note coming from electronics (+3.4%), driven by sales of iPhones. Existing home sales gained +2.4% m/m in September but were -1.7% y/y and prices fell for the third consecutive month (-4% m/m). Supply remains tight at 5.3 months (long-term average of 6.3). The Housing Market Index fell sharply in October from 59 to 54, driven by a lack of prospective buyers. September housing starts increased by +6.3% m/m and permits gained +1.5% m/m (both fell in August). Meanwhile, inflation remains subdued, with PPI down -0.1% m/m (+1.6% y/y) in September and the CPI up just +0.1% m/m (+1.7% y/y) in the same month.

Eurozone: Looking for positives? Maybe Q1 2015

The Composite PMI edged up slightly to 52.2 in October (up from 52.0 in September) but remained below the average recorded in Q3. The uptick in October was boosted by an increase in the Manufacturing PMI Output (51.9 from 51.0 in September, to a three-month high) while the Services PMI remained stable at 52.4. Caution should remain as the rates of expansion in the business confidence indicators remain very low and new orders are on the decline. In Germany, the Composite PMI increased to 54.3 as a result of an improvement in the Manufacturing Output index after two months of decline (to 53.3 from 51.0 in September) while the Services PMI edged down to a four-month low of 54.8 (from 55.7). The Composite PMI for France fell further, to 48.0, an eight-month low, reflecting contraction in both the manufacturing and services sectors. In the rest of the zone, new business growth remains very weak. Overall, at the start of Q4, economic prospects remain weak and suggest sluggish GDP growth (around 0.1-0.2% q/q) against a background of continuing high deflationary pressures. The ECB is expected to start its ABS/RMBS purchase programme in Q4 and positive surprises may extend from further measures implemented in Q1 2015 (including corporate/sovereign bond purchases). We expect GDP growth in the Eurozone of +0.7% in 2014.

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Countries in Focus

Americas



Canada: Key policy interest rate kept at 1%

The Bank of Canada (BoC) kept its overnight interest rate unchanged at 1% for the 50th consecutive month. However, the BoC's statement took on a somewhat more hawkish tone, stating that "core inflation rose more rapidly than was expected in July." Indeed, the September CPI report showed the y/y core inflation rate at 2.1%, just above the BoC's 2% target and substantially higher than the 0.9% recorded last November, when deflation fears arose. Even so, the BoC's long-term forecast of headline inflation as low as 1.4% in Q2 2015 is likely to hold the overnight rate at 1% for some time. That stance is supported by data on retail sales, which fell by -0.3% m/m in August, the second straight monthly decline. Over the past year, retail sales were driven by auto sales, which increased by +8.1%, leaving sales ex-auto at a reasonable but less robust +3.3%. Euler Hermes expects GDP will increase by +2.3% in 2014 and by +2.6% in 2015.

Europe



Greece: A new form of financial assistance increasingly likely

The possibility of an end-year exit from the bailout programme without further financial assistance triggered a strong spike in yields (+281bps in one-week, to 8.64% for the 10-year yield, the highest since mid-2013) suggesting a lack of investor confidence. The funding needs (fiscal deficit and debt maturing) are estimated at EUR21 bn in 2015 and EUR9 bn in 2016. We see a high likelihood of new financial assistance after end-2014, perhaps a combination of an Enhanced Conditions Credit Line (ECCL) from the ESM and further debt relief from the EU (longer loan maturity and/or lower interest rates). Greece will need to be under an EU programme to benefit from ABS/RMBS purchases expected to start in Q4 (EUR25 bn of potential market). Meanwhile, parliament will elect a President of the Republic in February 2015 and the governing coalition, to be effective, needs a two-thirds Chamber majority (currently only 50%). As a result, there is a risk of early elections in 2015.

Africa & Middle East



Mozambique: Africa still rising here

Preliminary results indicate that the ruling FRELIMO party won most votes in last week's parliamentary and presidential elections and that its candidate, Filipe Nyusi will become head of state (incumbent president Armando Guebuza stands down after two terms). However, RENAMO, the largest opposition party, rejected the results and there is a risk that violence will ensue. If relative domestic stability is preserved then confidence will increase that existing policies will continue and that the growth trajectory will not be halted; annual average GDP growth over the ten years to end-2013 was +7.4%. The key growth driver comes from substantial oil and natural gas investments and discoveries. Debt raised on the back of future energy flows may result in problems going forward but, for now, commercial prospects relating to ancillary industries to the oil and gas sector, to infrastructure projects and construction appear good. EH expects GDP growth of +8% in 2014 and +7.5% in 2015.

Asia Pacific



Indonesia: New president, great expectations

Joko Widodo, former governor of Djakarta, was sworn in as president at a momentous time for the country. On the economic front, signals are broadly positive but with a fragile outlook. Domestic demand is proving resilient and continuing increases in capacity utilisation rates (78.2 in Q3 from 77.0 in Q2) suggest that the investment cycle strengthened in Q3. However, external trade figures continue to disappoint (a deficit of -USD318 bn in August after a surplus of +USD42.4 bn in July) and this is likely to continue reflecting (i) weak commodity prices and (ii) a slowdown in Chinese demand. Trade data confirm our view that improvements in the current account deficit will be gradual. On the political front, implementation of structural reforms to improve management of public finances will be challenging, particularly given the lack of a parliamentary majority. Against this background, we expect GDP growth will recover gradually from +5.2% in 2014 to +5.8% in 2015.



What to watch

- October 24 – UK Q3 GDP (first estimates)
- October 24 – U.S. September new home sales
- October 24 – South Korea Q3 GDP
- October 26 – Brazil presidential election (second round)
- October 26 – Eurozone ECB results AQR & stress tests
- October 27 – U.S. September pending home sales index
- October 27 – Vietnam October trade balance
- October 27 – Germany October IFO business confidence
- October 28 – European Commission forecasts
- October 28 – U.S. September durable goods orders
- October 28 – U.S. October consumer confidence
- October 28 – U.S. August Case-Shiller home price index
- October 28 – Japan September retail sales
- October 29 – U.S. Fed FOMC policy decision
- October 29 – Japan September industrial production
- October 29 – Belgium Q3 GDP (preliminary)

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