Euler Hermes Economic Research

Weekly Export Risk Outlook

June 21, 2017

In the Headlines

FIGURE OF THE WEEK

€8.5 bn

3rd tranche of Greece's bailout program

France: Honeymoon avenue

President Macron got a new boost from the parliamentary elections and can pursue his ambitious reform agenda. First order of business is getting parliamentary approval for executive orders to fast-track labor market and cost-neutral tax reforms as early as this summer. Regarding economic evolutions, private sector confidence increased to fresh highs and shows the best alignment since August 2007. Consumers, the construction sector and the manufacturing sector are all exhibiting growth. Moreover, these surveys have passed through to hard data. Growth was +0.5% q/q in Q4 2016 and was revised up from +0.3% to +0.45% in Q1 2017. This offers a sound carry-over (+0.9%). Added to high business confidence, it strongly supports our +1.5% GDP growth forecast for full-year 2017. The labor market is also benefiting: job creation was +284,000 during the last 4 quarters and the construction sector added jobs in Q1 (+9,000k) for the first time since Q3 2008. As the economy is accelerating and fiscal incentives are acting, corporate investment is also recovering (+1.8% q/q in Q1), supported by evidence of improving cash positions in the French corporate sector.

Greece: The much-awaited tranche to be disbursed

On June 15, the Eurogroup meeting approved the much-awaited disbursement of the third tranche of the bailout program, worth EUR8.5bn. This will enable Greece to meet upcoming debt repayments, clear arrears and remove the risk of an imminent sovereign debt default. This follows the adoption by the Greek parliament of an ambitious fiscal package and other structural measures aiming at maintaining a primary surplus of +3.5% of GDP until 2022. However, the politically difficult discussion among creditors regarding the measures to be used to reduce the debt burden – proposals include extending the maturities of some loans and defer interest payments by up to 15 years – as well as the scope of the relief looks set to be postponed until the completion of the bailout in 2018. The IMF has eventually agreed to sign Greece's request for a 14-month credit line but will wait until the parameters for debt restructuring are clarified and long-term debt sustainability is ensured. We expect the economy to return to positive growth of +1% in 2017 and boost confidence, allowing a further relief of capital controls in H2.

Egypt: Wind of change, step 2

The government announced the unwinding of some of the capital controls introduced at the onset of the 2011 political uprising in order to limit capital outflows. The US$100,000 monthly limit on individual bank transactions was scrapped. This is not a complete unwinding of capital controls, since e.g. a US$50,000 monthly limit for importers of non-priority goods still prevails. But the announcement is welcome since barriers to foreign investment should decrease. This decision was made possible by the very positive impact of the exchange rate reform (see also our Country Report Egypt) on foreign reserves. Their import cover has sharply improved from 3 months last year to more than 7 months in May. GDP growth remained quite unaffected, at +4.3% y/y in Q1 2017, driven by the impact of the strong EGP depreciation (-50%) on external trade, boosting exports and weighing on imports. However, as inflation has accelerated since November 2016, to +29.7% y/y in May, the domestic economy appears to be cooling as indicated by slowing electricity consumption growth (+1% y/y in Q4 2016).

UK: One rate hike by year-end to support the sterling

The Monetary Policy Committee voted by a majority of 5-3 to maintain the key interest rate at +0.25%. Last month the balance was 7-1. The narrower majority signals that a +25bp rate hike could occur earlier than expected, possibly by year-end. The main reason behind this is the GBP depreciation, which is set to continue throughout the year due to the rise in political uncertainty while the start of the Brexit negotiations will also create volatility. Inflation should exceed 3% by autumn. In addition, economic growth slowed down to +0.2% q/q in Q1, real wage growth has been negative since February and house price increases have continuously slowed down since March 2016. These trends weigh on households' real purchasing power and jeopardize consumer spending while the saving rate has reached record lows in more than 50 years. We expect rate hikes to remain moderate, i.e. +25bp per year to +1.00% in 2019 when we expect a transition deal with the EU, before a Limited Free Trade Agreement may be reached in 2021, at the earliest.

Countries in Focus

Americas

Cuba: The détente was short-lived

On June 16, U.S. President Trump announced a partial reversal of the two-year warming of relations between the U.S. and Cuba. Tourism in Cuba benefited from this rapprochement as the number of tourist arrivals increased by +12% y/y in H1 2016, after +16% y/y in H1 2015. U.S. exports to Cuba surged for the fifth consecutive month in February 2017 (+31.7% 12m/12m), reaching USD240bn. According to the Trump administration, exceptions will be made for U.S. travel routes, diplomacy and for telecommunication services partnerships. Instead, the U.S. will prohibit dealings with military-run companies. In doing so, it aims the GAESA, a conglomerate owned by the Cuban armed forces which is deemed to account for half of the country's economic activity. The economy is also being strongly hit by the crisis in Venezuela, a key trade partner, after it slashed its oil supply to Cuba, generating energy shortages and restrictions on the island.

Europe

Russia: Monetary easing while growth faces new downside risks

The Central Bank of Russia (CBR) lowered its key policy interest rate by 25bp to 9.00% last week, continuing the monetary easing cycle that began in March. The move reflects that inflation, at 4.1% y/y in April and May, remains well on track to meet the CBR's end-2017 target of 4%, while the economic recovery remains subdued. Second estimates confirmed that Q1 GDP grew by +0.5% y/y. Also last week, news of potentially new, tougher U.S. sanctions against Russia – approved by the U.S. Senate but still subject to endorsement by the House of Representatives and President Trump – was unwelcome for Russian financial markets. The Senate move signaled that earlier expectations of swift sanctions relief after Trump's election were premature and have increased uncertainty over the length of the sanctions. New sanctions would mainly target Russian energy, infrastructure and defense sectors and pose a downside risk to medium-term growth. The short-term impact should be small as foreign investor interest is currently still muted. We maintain our growth forecast of +1.3% for 2017 as a whole.

Africa & Middle East

Nigeria: I feel it coming

Growth is on the way back. Q1 real GDP was still down by -0.6% y/y but the trough is now well behind (-2.4% y/y in Q3 2016) and the drivers triggering last year's recession (-1.5% in full-year 2016) are progressively normalizing. The credit crunch caused by strict capital controls is now less striking. The unwinding of these controls has led to an improvement in the provision of foreign currency to the financial and corporate sectors. As a consequence, the gap between the official and the black market exchange rates decreased from +40% in March to +10% currently. However, the bottlenecks created last year by capital controls and exchange rate turbulences had an impact on prices and, now, second-round effects imply inflation persistence, i.e. the balance of risks to our +15% forecast for 2017 is now more on the upside. The net effect on growth is expected to be positive (+1% in 2017) as better access to USD will support the external sector, though high inflation will keep weighing on domestic demand.

Asia Pacific

New Zealand: Holding firm

GDP rose by +0.5% q/q in Q1 2017, up from +0.4% in Q4 2016. Agriculture grew +4.3% q/q thanks to intense dairy production. Retail trade and accommodation rose by +1.8% q/q, reflecting a strong performance in automotive sales. The manufacturing sector expanded by +1% q/q, driven by transport equipment and machinery. Construction put a drag on the economy, contracting by -2.1% q/q. The expenditure measure of GDP reported a more subdued performance at +0.2% q/q. While domestic demand proved relatively resilient, net exports contributed negatively to growth with strong import growth (+1.3% q/q) and declining exports (-0.4% q/q). Going forward, we expect the economy to pick up speed. Macro policies should remain supportive, with the policy interest rate kept at a low level. Expenditure on GDP growth is set to prove firm at +2.5% in 2017, after +3.6% in 2016.

What to watch

- June 22 – Eurozone June Consumer Confidence
- June 22 – European Council Meeting
- June 22 – France June Business Confidence
- June 22 – Turkey June Consumer Confidence
- June 23 – Brazil June Inflation
- June 23 – Eurozone June PMIs (preliminary)
- June 23 – Germany June Ifo Business Climate
- June 23 – Turkey June Business Confidence
- June 25 – Italian municipal elections (second round)
- June 26 – Czech Republic June Economic Sentiment
- June 26 – Poland May Retail Sales
- June 26 – Poland June Business Confidence
- June 27 – Brazil May Current Account Balance
- June 27 – Ukraine May Industrial Production
- June 28 – Argentina Q1 Current Account Balance
- June 28 – France June Consumer Confidence