Euler Hermes Economic Research

# Weekly Export Risk Outlook

12 February 2014

FIGURE OF THE WEEK

113,000

New jobs created in the US in January

# In the Headlines

## Emerging Markets: Turbulence but no crash

The tapering (monetary tightening) by the US Fed, a slowdown in demand in China and a busy election timetable around the world this year have caused (in that order) new concerns about emerging markets (EM). Despite recent adverse effects on EM stock markets and currencies, with associated increases in domestic interest rates, EH does not expect a systemic crash. While EH expects the situation will stabilise it also anticipates selected second-round effects, notably some heightened financing and non-payment risks for businesses. Vulnerability related to capital outflows is common for EM but adoption of the right policy toolkit can protect growth and the private sector. EH identifies a watchlist of vulnerable countries: a Fragile 10 of **Argentina, Indonesia, Turkey, Brazil, South Africa, India, Chile, Colombia, Philippines** and **Mexico** (affected partly because of the size of their financial markets and partly by their external and/or domestic vulnerabilities) and a Weak 4 of **Thailand, Russia, Ukraine** and **Venezuela** in which recent deterioration is largely linked to political risk events and/or other domestic issues. [For a detailed analysis see EH's Economic Insight published on 6 February, click here]

## Ukraine: Devaluation and capital controls

Last week, the central bank devalued the official exchange rate of the UAH by 9% from 8.0 to 8.7 against the USD and also imposed capital controls on foreign currency purchases. The move came after weeks of FX intervention to maintain the pegged exchange rate regime – apparently abandoned now – that reduced FX reserves substantially but failed to prevent a 10% slide in the UAH on cash markets. A protracted economic crisis and downward pressure on the UAH have been exacerbated by the ongoing political crisis as well as Russia's suspension of a USD15 billion bail-out in response to the government's resignation at end-January. Without resumption in foreign aid in the near term, the risks of further UAH depreciation and sovereign default will continue to rise. Meanwhile, anti-government protests have continued but have been largely non-violent over the past two weeks as the opposition and the president have been negotiating constitutional changes to resolve the political crisis. However, prospects of a near-term resolution of the conflict appear slim.

## US: Weak job growth

The January employment report showed only 113,000 jobs created, markedly below expectations of around 180,000 and the second consecutive poor data release as only 75,000 new jobs were generated in December 2013. Cold weather and heavy snow probably affected December job creation but cannot be accountable in total for the economy's weakness in January. There are some positives in the data, including a 0.1pps dip in unemployment to 6.6% and slight improvements in participation rates and duration of unemployment. Construction jobs rebounded from December 2013 and manufacturing added 21,000 jobs, the sixth consecutive gain (although modest). Meanwhile, the new Fed Chair Janet Yellen gave her first public testimony to Congress and appears likely to continue the current policy of tapering throughout 2014, the ISM non-manufacturing survey for January was 54, firmly above the 50 level showing expansion, and the House voted to suspend the debt ceiling limit until March 2015 and the Senate will likely do the same, averting for another year a battle over spending.

## Norway: Moderate overall growth in 2013

In Q4 2013, GDP decreased by -0.2% q/q, reflecting strong falls in investment (-1.1%) and exports (-3.2%). Total consumption was more resilient but remained subdued, with household spending increasing by +0.4% and government expenditure by +0.5%. Overall, economic activity remained weak in 2013 (+0.8%) as external trade provided a drag on GDP growth (a negative contribution of -2.3pps) because of low external demand, despite NOK depreciation. A weak performance in energy-related activities is also an explanation. Mainland GDP performed better, with growth of +2% in 2013, but remaining below long-term average annual expansion. In 2014, economic activity should strengthen, with a less negative impact from net exports and resilient domestic demand, especially as the government decided to spend a larger portion of oil revenues this year. However, the housing market is likely to enter a cycle of lower prices while households remain overly indebted. EH expects GDP growth of +2.3% in 2014 and to reach the long-term growth rate only in 2015 (+2.7%).

# Countries in Focus

Americas

## Latin America: Inflationary pressures broadly contained

Inflationary pressures remain subdued in **Chile** and **Colombia**, with consumer prices increasing in January by 2.8% y/y and 2.1%, respectively, below the central bank inflation targets of 3% in both countries. Inflation in **Peru** was 3.2% in January, slightly above the upper limit of the inflation target range (2% ±1%), mainly because of increased food and energy prices. In **Mexico**, prices accelerated in January to 4.5% y/y (after 4% in December 2013), largely reflecting temporary factors including new taxes on some food, drink and fuels. In **Brazil**, inflationary pressures continue to ease, with 5.6% y/y in January (after peaking at 6.7% in June 2013) mainly resulting from a tightening in monetary policy (+325bps to 10.5% since April 2013) as a response to a currency slide and inflationary pressures. However, inflation remains at the high end of the target range (4.5% ±2%). **Argentina** and **Venezuela** remain outliers, with January CPI data expected to remain significant concerns for both.

Europe

## The Baltics: Flash estimates of GDP growth

In 2013, **Latvia** was again one of the fastest growing economies in CEE, even though Q4 real GDP growth eased to +3.5% y/y and +0.7% q/q, taking full-year growth to an estimated +4% (+5% in 2012). Services (+6.7%), retail trade (+3.9%) and manufacturing (+2.6%) were the key growth drivers in 2013. In **Lithuania,** Q4 2013 GDP growth accelerated to +3.5% y/y and +1.2% q/q, resulting in full-year growth of +3.2% (+3.7% in 2012) which was mainly driven by a rebound in the construction sector and by manufacturing. **Estonia**'s Q4 2013 GDP growth came to a halt in y/y terms and decreased by -0.1% q/q, taking full-year growth to just +0.7% (+3.9% in 2012). On the expenditure side, robust domestic demand was the key growth driver in all three countries in 2013, while moderating external demand (declining in Estonia) caused the overall slowdown. EH expects 2014 growth in Latvia and Lithuania to be similar to 2013, while Estonia should pick up to around +2%.

Africa & Middle East

## Ghana: Policy action aimed at limiting currency weakness

Frontier, as well as emerging, markets are subject to the recent asset class sell-off and period of rapid currency weakening. The GHS depreciated by 7.8% against the USD in January and the central bank last week increased its key policy interest rate by 200bps to 18% and introduced new regulations that strictly limit FX and foreign-currency account operations. However, GHS weakening also reflects domestic structural rigidities, including large fiscal and current account deficits. State spending before the December 2012 elections pushed the budget deficit up to -12% of GDP last year and increased inflation (13.5% in December 2013, compared with a target range of 9% ±2%). Deterioration in the fiscal accounts, in particular, led to downgrades from the international rating agencies and prompted the IMF to raise concerns about economic stability. EH revised downwards its GDP growth forecast for 2014 (+6%), partly reflecting weak gold prices, as well as last week's actions.

Asia Pacific

## Australia: Towards moderate growth

Last week, the central bank kept its key policy interest rate unchanged for the sixth consecutive month, at a record low 2.5%. The dovish stance is likely to be maintained until the economy returns to solid growth. Recent indicators continue to give mixed signals. In January, the manufacturing PMI indicated contraction for a third consecutive month, at 46.7 from 47.6 in December 2013. Meanwhile, the National Australian Bank survey points to an improved outlook, with the business confidence index up 2 points to 8. The fundamentals continue to reveal a weak short-term outlook. Unemployment in H1 is likely to register its highest level (5.9%) since 2004. Moreover, household purchasing power will probably remain eroded by inflationary pressures (+2.7% y/y in Q4 2013 from +2.2% in Q3) and exports are projected to be less buoyant, reflecting an anticipated slowdown in Chinese demand. Overall, EH expects GDP growth will increase at a moderate pace in 2014 (+2.7%).


# What to watch

- February 13 – Germany January CPI
- February 13 – US January retail sales
- February 14 – China January PPI
- February 14 – Bulgaria & Hungary January CPI
- February 14 – EU-28 Q4 2013 GDP (first estimate)
- February 14 – India January WPI
- February 14 – US January industrial production
- February 16 – Israel Q4 2013 GDP
- February 17-18 – Eurogroup/Ecofin meetings
- February 18 – Iran nuclear talks with world powers
- February 19 – US January Fed minutes released





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