Euler Hermes Economic Research

Weekly Export Risk Outlook

17 October 2013

In the headlines

FIGURE OF THE WEEK

USD110.9

Barrel price of benchmark Brent crude oil

US: The cavalry arrives just in time

Lawmakers passed a last-minute deal to raise the debt ceiling, to re-open the government on Thursday and to give back pay to workers on enforced leave of absence. However, the agreement only raises the debt ceiling until 7 February and only funds the government through to 15 January. To prevent more last minute deals, the agreement also established a bipartisan panel to negotiate a budget by December. Republicans, who had forced the shutdown by trying to defund Obamacare entirely, won only a minor concession for tighter income verification on applications for health insurance subsidies. On news of the agreement, treasury yields fell sharply and stock markets were up but the shutdown is estimated to have cut 0.3%-0.5% from Q3 GDP as consumer sentiment slipped, same-store sales growth fell to the lowest in the recovery, manufacturing eased in New York state, the Housing Index dropped and the Fed's Beige Book survey reported only modest growth, with four of the 12 Fed districts reporting deceleration.

France: Industrial output up in August

In August, industrial production increased by +0.2% m/m, below expectations (consensus at +0.6%), after contracting by -0.6% in July. Likewise, manufacturing output increased by +0.3% m/m after -0.8% the previous month. Increased output was mainly driven by a strong improvement in the automobile sector (+19.5% in August after -12.6% in July) and a moderate increase in agricultural products (+1.1% after +0.5%). However, output was down for machinery, electrical and electronic equipment (-3.3% after +0.2% in July) and coke and refined petroleum products (-5.3% after -6.1%). Industrial confidence improved in September, with the manufacturing PMI gaining 0.3pts to 49.5 but remaining below the 50 threshold that suggests overall expansion. Industrial output is now at a level below that recorded in the early 1990s. The share of the manufacturing sector in total added value declined from 13.5% in 1996 to 12% in 2013 and the share of manufacturing employment in total employment decreased from 19% to 13.5% over the same period.

Ireland: Challenging debt environment

Of the EUR85 billion total EU/IMF adjustment programme, EUR2.8 billion remains to be disbursed by December when the programme will end. Official sources suggest that the country does not plan to ask for a new credit line as the National Treasury has issued enough debt to cover expected financing needs until the end of 2014. Overall, the adjustment programme ends on a positive note, with a return to GDP growth, a current account surplus and stable employment. However, public debt is expected to reach 122% of GDP in 2014 and private debt is close to 300% of GDP (far above the EU limit of 160%). Significant debt repayments become due in the coming years, with reimbursements on the IMF loan scheduled for 2015 and on EU loans in 2019. Fiscal deficit targets have been slightly revised (i) downward to 7.3% of GDP for 2013 (excluding the banking bailout) from 7.5% announced in April (ii) upward to 4.8% and 2.9% for 2014 and 2015, respectively. Achievement of a primary balance surplus has been delayed by one year to 2014. Overall, debt sustainability as well as fiscal deficit reduction remain challenging and the official growth forecasts appear optimistic, with +0.2% in 2013 and +2% in 2014 whereas EH expects -0.3% and +1.4%, respectively.

North Africa: Political transitions remain fragile

In **Egypt**, uncertain security and stability remain detrimental to economic recovery. The GCC countries are providing financial support but the IMF is waiting for an elected government before providing full assistance. The outlook for key foreign currency earners (including tourism) is poor. In **Libya**, the recent short-lived detention by gunmen of PM Ali Zidan indicates that armed militia with little allegiance to the central government remain significant power centres and areas of the country seek autonomy. Meanwhile, oil output remains curtailed by security problems and by industrial disputes. In **Tunisia**, security issues are a concern, particularly away from the major urban centres, but political leaders appear more willing to negotiate and compromise. The Islamist al-Nahda (leader of a three-party ruling coalition) agreed to stand down and allow a caretaker government to oversee a period up to new elections. Moreover, the military is remaining out of political life and the IMF is providing support. Even so, expect all the political transitions in North Africa to remain challenging.

Countries in Focus

Americas

Brazil: Selic up again

On 9 October, the central bank increased its key policy interest rate (Selic) by 50bps to 9.5%, as part of its continuing attempt to curb inflationary pressures. The Selic was left unchanged between October 2012 and April 2013, at 7.25%, but since then the bank has tightened monetary policy in a gradual process. The rate of inflation has been increasing since H2 2012, from around 5% to 7.2% in March this year, a one-and-a-half year high, reflecting dynamic domestic demand and H1 growth. Additional inflationary pressures stem from BRL depreciation between May and August, high labour costs and increases in import taxes. The central bank's target range for inflation for 2013 is 4.5% +/- 2pps but the rate is among the highest in Latin America (5.7% in September), behind double-digit rates in Venezuela and Argentina. EH expects average inflation rates of 6.6% in 2013 and 5.7% in 2014 and GDP growth to decelerate slightly in 2014 to +2% from +2.2% this year.

Europe

Serbia: Recovery comes to near-standstill in Q2

Revised estimates from the Statistical Office show that real GDP increased by just +0.2% y/y in Q2, down from the flash estimate of +0.7% as well as from +2.7% inQ1. Domestic demand weakened further as a result of continued tight monetary policy and reinforced fiscal austerity. Private consumption declined by -1.2% y/y in Q2, government consumption by -6.6% and fixed investment dropped by -18.5% . Weak domestic demand also eroded import demand which was down by -0.5% y/y in Q2. Exports expanded by +9.1% y/y so that net exports prevented the economy from slipping back to y/y contraction in Q2. Nonetheless, Serbia is on the brink of returning to recession as Q2 real GDP shrank by -0.3% in q/q terms, after +2.5% growth in Q1. On the supply side, strong expansion of agriculture (+20.5% y/y) and information & communications (+9.6% y/y) was offset by sharp declines of construction (-42.5% y/y) and trade (-4.7% y/y). EH expects full year growth of about +1% in 2013.

Africa & Middle East

Uganda: Primary sector boosts growth

GDP increased by +5.7% y/y in Q2, up moderately on +5.5% in Q1 but suggesting that the economy is resilient to headwinds elsewhere in the emerging world. However, one of the main growth drivers in H1 was the cash crop sector (mainly coffee), which is highly cyclical, so the rate of growth may ease somewhat in H2. Even so, EH increased its GDP growth forecasts and now expects +5% in 2013 and +6.5% in 2014, led by investments in infrastructure and in energy projects (hydro-power and oil). Meanwhile, although President Yoweri Museveni remains broadly popular, there are perceptions that the leadership is becoming increasingly autocratic and that, although the country is a multi-party democracy, political and some civil liberties are artificially limited and that economic benefits do not filter down to the wider population. A two-term limitation on the presidency has already been dropped. Expect a constitutional upper age limit on the position to be amended soon.

Asia Pacific

Asia: Mixed signals

Industrial output in **Japan** contracted by -0.9% m/m in August, after increasing by +3.3% in July and capacity utilisation fell by -2.1% m/m from an increase of +3.7%. However, the short-term outlook remains positive as demand indicators show that the economy is still on track for GDP growth of +2% in 2013. In particular, consumer confidence increased strongly in September (45.5 from 43 in August), although this may be explained partly by consumption ahead of next year's tax increases. In **China**, the latest data provide mixed signals, with external trade continuing to be positive but at a lower level (trade surplus USD152 billion in September from USD285 billion in August), with less support from the export side (contraction of -2.6% m/m in September). In the meantime, loans increased by CNY787 billion in September from CNY675 billion in August but should be contained in the short term as inflation (3.1% in September) is approaching the government's 3.5% target for 2013.

What to watch

- October 17 – Eurozone August current account
- October 17 – Portugal 2014 budget
- October 17 – UK September retail sales
- October 17 – US September CPI
- October 18 – Canada September CPI
- October 18 – China Q3 GDP
- October 18 – US September industrial production
- October 23 – UK BoE October meeting minutes
- October 23 – Eurozone October consumer confidence
- October 24 – Eurozone October flash PMIs

Note: many US data releases are waiting for the re-opening of full government services.

Contact Euler Hermes Economic Research Team
research@eulerhermes.com

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