

Weekly Export Risk Outlook

23 July 2014

In the Headlines

FIGURE
OF THE WEEK

+0.1%

EH's revised
forecast for
Russia's GDP
growth in 2014



Russia: Further brake on growth

The combined force of U.S. and EU sanctions against Russia over its alleged support for separatists fighting in areas of eastern Europe has been strengthened. The U.S. targeted major banks (including Gazprombank and VEB), companies involved in work for the defence sector and energy companies (including Rosneft), which now face a ban on new medium- to long-term financing (longer than 90 days) from U.S. entities. If Russia is perceived as not co-operating with the west in regional matters, the EU intends to suspend new funding of projects in Russia through its investment banks (EIB and EBRD) and may announce bans on additional entities and individuals by end-July. Although new sanctions will have a more significant impact than previous measures, the details suggest that the U.S. and EU are still hesitant to target directly existing commercial relationships, including Russian energy supplies to the EU. Nonetheless, borrowing costs are likely to rise for Russian banks and companies as a whole, which should further undermine gross investment in Russia, which is now unlikely to recover from the weak performance it recorded in Q1 (down -14.6% y/y). EH reduced its real GDP growth forecast for 2014 to +0.1%.



Thailand: Business (almost) back to usual

Global demand continues to cushion the impact of political turmoil. Advanced indicators show a small rebound in exports (+0.5% y/y in May) and consumer and business confidence indices are improving. The business sentiment index in May was 48.6, compared with 44.3 in April, while the consumer confidence index reached 75.1 in June (67.8 in April). EH expects economic activity will recover gradually in H2, reflecting a pro-growth policy mix: (i) the regime announced at the beginning of July that it will help exporters by keeping the THB stable. After a sharp depreciation in H1, the THB appreciated moderately thereafter; (ii) responding to concerns stemming from a deceleration in domestic demand, a fiscal stimulus package was announced. The latter includes measures to boost lending to poorer households (credit to the private sector increased by +9.9% y/y in May, compared with an average of +18% in 2012-13) and the re-introduction of subsidies to rice farmers; and (iii) to "stabilize the political and business environment", the regime recently announced an interim constitution, with the intention of replacing it with a permanent constitution in July 2015, following which new elections will be held within a three-month period. EH expects GDP growth will be limited to +1.5% 2014, after +2.9% in 2013.



U.S.: Output growth but concerns about inflation and housing

Industrial production increased by a modest +0.2% m/m in June, but on an annualised basis it was +5.5% in Q2, compared with +3.9% in Q1, suggesting that Q2 GDP will be stronger, as expected. Industrial output from the manufacturing sector increased by a strong +6.7% in Q2, compared with +1.4% in Q1, driven by a marked improvement in auto production of +15.9%, compared with -2.4% in Q1. Meanwhile, gasoline prices increased by a sharp 3.3% m/m in June, driving up overall consumer price inflation by 0.3% m/m and 2.1% y/y, which is not unusually high but is around the Fed's 2% target rate for inflation. Fed Chair Yellen's recent apparent disappointment in the housing market was confirmed again this past month. While existing home sales gained +2.5% m/m in June, it still left the y/y rate at -2.9%. Housing starts and permits both fell for the second consecutive month, falling -9.3% m/m and -4.2%, respectively. On a more positive note, the housing market survey of homebuilders improved above the breakeven 50 level for the first time since January.



Sweden: Deflation becomes a public issue

In response to pervasive deflationary pressures, the central bank cut interest rates by 50bps (to 0.25%), above expectations. After a series of rate hikes between 2010 and 2011 (from 0.25% to 1.75%) reflecting rising household debt (above 170% of disposable income) and risks of overheating in the real estate market, deflationary conditions are now clearly endangering the private sector deleveraging process. The rate of inflation in June was only 0.2% y/y after five months in negative territory. In 2014, domestic demand will be the main driver of GDP growth (+2.2%), largely as a result of strong private consumption supported by improvements in the labour market and rising incomes. However, downside pressure on prices, with associated low nominal GDP growth, will put pressure on firms' margins and turnover. Net exports will contribute negatively to GDP growth, given the strength of imports and limited export growth because of SEK strength.



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Chile: Rate cut to offset economic slowdown

In line with expectations, the central bank cut the key monetary policy rate by 25 bps, to 3.75% (5% in the same period of 2013). After abstaining from cuts in the past three months, the authorities took action because the local economy continued to slow, particularly in relation to investment and private demand. Recently-elected President Michelle Bachelet's new tax system is dampening investor confidence, particularly through the abolition of the FUT (Fondo Utilidad Tributario), a major source of investment for large companies. As the world's largest copper exporter, Chile is sensitive to weak copper prices, which, coupled with increased energy costs in the mining sector, have also been a drag on economic growth. Furthermore, inflation is still high at 4.3% y/y in June (4.7% y/y in May but 2.8% y/y in January), above the central bank's target of 3% +/- 1pps. EH expects the economy will grow by +3.3% in 2014, below the +5.3% annual average in the previous four years.

Europe



Cyprus: Still a long way to go

The completion of the 5th Troika review of Cyprus, expected by end-July, should pave the way for a further disbursement of the EU/IMF adjustment programme agreed in spring 2013. Out of the EUR10 billion in financial assistance around 50% has been released. The programme appears to be on track, but downside risks remain. These mainly relate to: (i) the prolonged period of tight credit supply and delays in the restructuring of the large and increasing stock of NPLs in the domestic banking system (that reached 50% of total loans); (ii) the unresolved deficit on the primary balance (at -2% of GDP in 2013); (iii) negative spillovers emerging from the weakness in the Russian economy; and (iv) insufficient implementation of structural reforms. The programme is expected to end in December 2016 but exit is likely to prove challenging. EH expects Cyprus will register its fourth consecutive year of recession in 2015 (-1%, after -4.5% in 2014).

Africa & Middle East



Saudi Arabia: Open plan?

The largest stock exchange in the Middle East (market capitalisation of around USD530 billion and with its leading index up over 14.9% since the start of the year) will be opened partially to international investors outside the GCC. The Capital Market Authority will announce rules for the participation in the stock market of qualified foreign financial institutions, although an implementation timetable is yet to be made available. This opening may herald a period of relative economic liberalisation as the kingdom seeks to diversify away from dependence on oil and gas. However, EH expects that Saudi conservatism will prevail and changes will be implemented only slowly. Even so, it is likely that there will be significant investor interest in the kingdom, which has a Sovereign Wealth Fund currently commanding assets of over USD735 billion and the world's second largest crude oil reserves. EH expects GDP growth of +4.5% in 2014 and around +5% in 2015, with upside potential.

Asia Pacific



China: Improving financing conditions

Total social financing, which is a broad measure of total credit, increased by 4% over the past six months and bank loans increased by 9.6% y/y over the same period. Moreover, alternative credit (a proxy for shadow banking) continued to decrease (-3%). These improvements in the quality of financing result, in particular, from various policy measures adopted since the beginning of the year. These include stricter regulation to limit shadow banking (including constraints on trust and bank balance sheets) and more targeted liquidity measures to support domestic demand (including lower reserve requirement ratios). Meanwhile, RMB internationalisation is gaining traction. On 21 July, China signed a three year bilateral swap agreement with the Swiss Central Bank for a total of RMB150 billion (USD24.17 billion). This will support the use of the RMB as an international currency for trade, investment (as a medium of exchange) and savings (as a reserve currency).

What to watch

- July 24 – Brazil June unemployment
- July 24 – Eurozone July PMI (manufacturing & services)
- July 24 – UK June retail sales
- July 24 – U.S. June new home sales
- July 24 – Spain Q2 unemployment
- July 25 – Brazil June current account
- July 25 – U.S. June durable goods orders
- July 25 – Germany July IFO business climate
- July 25 – UK Q2 GDP (preliminary)
- July 25 – Germany August consumer confidence
- July 26 – Germany June retail sales
- July 29 – South Africa Q2 unemployment
- July 29 – Spain June retail sales
- July 29 – U.S. May Case-Shiller home price index
- July 30 – U.S. Q2 GDP
- July 30 – U.S. Fed meeting
- July 30 – Spain Q2 GDP (first estimate)
- July 30 – Belgium Q2 GDP (preliminary estimate)

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