

Weekly Export Risk Outlook

2 October 2013

FIGURE
OF THE WEEK

26.6%

Spain's official
forecast for
unemployment
in 2013

In the headlines



US: Shut down, with a debt ceiling approaching

Republicans tried to defund Obamacare, Democrats refused, and a partial government shutdown resulted, effective from 1 October. There have been 17 shutdowns since 1977 lasting from a few days to a few weeks, but it is unclear how long this one will last. Approximately 30% of government workers or 800,000 people will not be at work. Essential services such as Medicare, Social Security, defence, mail and air traffic control will continue to operate, while parks, museums and other non-essential agencies (including economic statistics) will be closed. The Fed's anticipation of fiscal delay was apparently good reason for not tapering in September. Economists estimate the shutdown will cut 0.2%-0.5% per week from GDP growth. More worrisome, the debt ceiling will be hit around 17 October. If the two parties remain intransigent, it is possible that the government could default on its debt, although it is unlikely. Expect consumer and business confidence to fall amid the uncertainty.



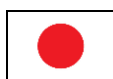
Eurozone: The ECB is likely to come to the rescue...but not yet

The ECB left its key interest rate unchanged at 0.5% while maintaining a dovish stance. Mario Draghi highlighted the prevailing tight credit conditions and remained cautious on the overall recovery, which he views as 'weak, fragile and uneven'. The ECB reiterated its commitment to 'use all available instruments' to ensure that money markets conditions do not hamper the economy. Although there is no immediate need to announce a new LTRO, its implementation seems a necessity to counter the bank deleveraging process that weighs on bank lending to the private sector and that continues as a drag on investment. EH expects a new LTRO at the beginning of 2014 (or end-2013, at the earliest), when the existing three-year LTRO maturity drops below 1-year and when the ECB will publish the eurozone banks' balance sheet assessments (Asset Quality Review) and the EBA the liquidity stress tests. Also, towards year-end, the ECB and the EIB are expected to provide further ideas on how to support lending to SMEs. A rate cut by year-end is not excluded if the economic outlook shows further signs of weakness, but EH expects the effectiveness of such a move to be limited, given the zone's financial fragmentation.



Spain: Reduction in the pace of austerity

The 2014 budget plan maintains fiscal austerity, but with only moderate expected impact on economic growth. Fiscal targets have been revised, with a budget deficit in 2013 of -6.5% of GDP (-6.3% in April) and -5.8% is projected for 2014. Most adjustments are expected to come from the autonomous regions, previously responsible for most of the fiscal slippage. Contrary to 2012/13, there are no projected tax increases but previous fiscal adjustments will continue to weigh on growth in 2014 and austerity will be maintained, with no civil service wage increases for the fourth consecutive year. The interest debt burden is set to decrease further, from EUR38.6 billion in 2013 to EUR36.6 billion in 2014, reflecting an improved sovereign market. However, in the absence of a transfer from the banking system bailout (EUR40 billion or 4% of GDP) to the ESM (not likely before H2 2014), interest expenditures will remain high. Official forecasts for 2014 are GDP growth of +0.7% (previously +0.5%) and unemployment falling to 25.9% from 26.6% in 2013. EH is less optimistic about 2014 and expects GDP growth of +0.4%, a fiscal deficit of -6% of GDP and public debt of 98% of GDP (from 91.3% in 2013), a new record level.



Japan: Sales tax to increase to 8% next April

This week and as expected, PM Abe announced an increase in the sales tax from 5% to 8%, effective from April 2014. As a result, around YEN8000 billion (USD82 billion) will be raised in public revenue. It will be the first increase in the sales tax for over 15 years. In 1997, the tax rate increased by 2pps to 5% and private consumption growth decelerated to +0.9% (from +2.3% in 1996). To avoid this kind of scenario and to cushion the effect of the increase, Abe also announced a set of measures to provide a stimulus equivalent to at least YEN5 trillion. This includes cash handouts for low-income families but also tax breaks for companies, with a cut in corporate tax (currently 38% and among the highest in the advanced economies) to encourage corporates to increase wages and boost capital investment. Against this background, EH expects GDP growth to slow by -0.5pps to +1.5% in 2014, which would represent a lower negative impact than in 1997 (-1.1pps), with the tax effect partially offset by the stimulus.

Countries in Focus

Americas



Brazil: Downward revision in official growth forecast

The central bank revised downwards its GDP growth forecast for 2013, to +2.5% from +2.7% previously. Advanced indicators suggest a slowdown in economic activity in Q3, with a moderate rebound at the end of the year. Domestic demand will be the only driver of growth in 2013 (+2.5pps) as net exports will contribute negatively (-1pps). On the demand side, the main contributor to growth will be investment (+6.5%, from -4% in 2012) whereas both household and government consumption will slow (+1.9% and +1.8%, from +3.1% and +3.2% in 2012, respectively). On the supply side, 2013 growth will be driven mainly by agriculture and livestock (+10.5%) while industry and services will grow only moderately (+1.1% and +2.3%, respectively). EH expects GDP growth to accelerate in 2013 to +2.2% from +0.9% in 2012 but then to slow to around +2% in 2014, reflecting tight monetary conditions, high inflation, exchange rate volatility and structural weaknesses.

Europe



Czech Republic: Gradually emerging from recession

Revised data show that seasonally-adjusted real GDP increased by +0.6% q/q in Q2, following six consecutive quarters of contraction. Domestic demand remained weak, with private consumption declining by -0.1% q/q, government consumption by -0.7% and fixed investment by -0.6%. Net exports were the growth driver as exports increased by +2.4% q/q while imports were nearly flat at +0.1%. As a result of a large fall in inventories, Q2 real GDP continued to contract in unadjusted y/y terms, by -1.3%, although this was an improvement from -2.9% in Q1. Last week, the central bank kept its key policy interest rate at 0.05% and announced retention of this historic low rate until inflationary pressures increase markedly. EH expects the economy to continue to recover in H2, resulting in a full year decline of GDP of -1% in 2013. On the political front, early parliamentary elections will take place on 25-26 October, following the dissolution of the Lower House in August.

Africa & Middle East



Middle East: Small but potentially significant steps

Recent events have given hope for resolution of some key areas of existing and potential conflict. A UN resolution on **Syria** has already led to progress in cataloguing the country's stock of chemical weaponry, prior to its planned elimination. At the UN, the US and **Iran** found scope for an unexpected level of rapprochement, ending with presidential dialogue. If progress is maintained, there is a considerable upside for the region, including **Lebanon**, **Jordan** and, perhaps, **Iraq**. However, there are significant challenges (the civil war in **Syria** continues, with potential for state disintegration) and obstacles (the US and Iranian presidents have to get domestic political support for improved relations and there remains considerable mutual distrust). Moreover, regional balances may be upset further as **Israel** and **Saudi Arabia** will be wary of the possibility of closer ties between Tehran and Washington. EH does not expect commercial opportunities to improve markedly in the short term.

Asia Pacific



Asia: Mixed industrial production data

Industrial production in **South Korea** continued to recover in August, increasing by +3.3% y/y, after +0.9% in July, led by strong automobile and consumer electronics output. This improvement is consistent with recent manufacturing PMI data, which gained 2.2 points (to 49.7) in September, although remaining below the threshold for expansion. In **Japan**, industrial production decreased by -0.2% y/y in August, after +1.8% in July. However, other data suggest an improvement in both internal and external demand as retail sales increased by +12.4% y/y in September (after -6.4% in August) and exports increased by +14.7% y/y in August (after +12.2%). Industrial production was weaker in **Taiwan** in August (-0.7% y/y after +2.1% in July) but advanced indicators show some improvement in industrial confidence (manufacturing PMI was 52 in September). Overall, data suggest a gradual improvement in Asia in Q4, reflecting a rise in business confidence. After a slowdown in 2013 (+4.7%), regional GDP growth should accelerate to +4.9% in 2014.

What to watch



- October 3 – Eurozone September composite PMI
- October 3 – Eurozone August retail sales
- October 4 – Eurozone August PPI
- October 4 – Russia September CPI
- October 4 – US September unemployment
- October 4 – Ireland constitutional referendum
- October 7 – Eurozone Oct. Sentix investor confidence
- October 8 – Germany August trade balance
- October 8 – France August trade balance
- October 8 – Ethiopian presidential elections
- October 8 – Azerbaijan presidential elections
- October 9 – UK August industrial production
- October 9 – US minutes Fed's September meeting

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