Euler Hermes Economic Research

Weekly Export Risk Outlook

28 March 2018

FIGURE OF THE WEEK

USD67

Average barrel price of benchmark Brent crude oil in Q1 2018

In the Headlines

China: Escalation in trade relations with the U.S.

The United States announced a certain number of protectionist measures over the past three weeks. One is an import tariff of 25% on steel and 10% on aluminum. Some major trading partners (Canada, Mexico, EU) have been exempted for now, with the notable exception of China. Two is a 25% tariff on USD60bn worth of Chinese exports. The list of sectors concerned should be revealed shortly. We estimated that these moves could cost China USD15bn in export losses. China retaliated with a 25% tariff on USD3bn worth of U.S. exports including wine, pork and steel. U.S. exporters could lose USD700mn. Going forward, the U.S. could target the Chinese electronic, electrical and textile sectors as these are the largest contributors of its deficit with China. China could focus on agrifood where it has its largest deficit with the U.S. Moreover, we may see Chinese measures on financial services and investment flows. For now, the overall impact on economic growth in China would be relatively moderate. We expect real GDP to grow by +6.5% in 2018 (after +6.9% in 2017).

France: The ties that bind

In France, some ties are progressively darkening the good economic momentum, weighing on private sector confidence. First, the difficulties to hire people when the economy is booming have created bottlenecks in the corporate sector. For example, the construction sector has order books above seven months, but 63% of the businesses face difficulties to hire. Second, households have lost some faith since they have felt their financial situation deteriorating. Household confidence landed and the savings rate was still high in 2017 (14.2%, after 14% in 2016) despite a visible decline in unemployment. One cause is higher inflation. It weighed on overall household purchasing power during Q4 2017 (+0.2% q/q, after +0.5% q/q in Q3). Moreover, tax increases in Q1 worsened their perception (higher tax on gasoline, increase of social contribution – CSG – on pensions). Third, corporates margins have been stable at below pre-crisis levels since mid-2015. In 2017, they stood at an average 31.7% (33.5% in Q1 2008). Services sectors are particularly feeling the pressure (26.5% for retail and 27.1% for business services). A lower tax burden would certainly help.

South Africa: Implementation time

The honeymoon period is still benefiting the new government. The willingness to reduce the fiscal deficit and stabilize the debt levels has convinced international rating agencies. Moody's recently moved the outlook of its sovereign rating for South Africa from negative to stable, with important positive consequences for corporate ratings. Inflation has again surprised on the downside at +4% y/y in February, and should continue to ease as a result of the ZAR appreciation. We forecast the ZAR to end 2018 at 11.5 per USD (on average, +11% higher than its 2017 average). This will give a welcomed leeway to the Central Bank to reignite its easing cycle. We expect the policy rate to be cut by -100bp this year, sending it to 5.75% by year-end. However, in the long run the more difficult task will be to reform public finances and in particular SOEs. The deteriorating situation of public corporates took already its toll on the overall corporate sector situation in 2017. After experiencing their trough in September 2017, insolvencies have begun to increase (+5% from September to January 2018).

Belgium: Another year of above potential growth

Real GDP rose by +1.7% in 2017, the highest since 2011. We expect growth to edge up to +1.8% in 2018. Private consumption should exit the soft mood (+1.4% in 2018, after +1.1% in 2017) as the one-off negative effects from the rise in taxes and the subsequent increase in inflation (+2.1% in 2017) will wane. Household real purchasing power in 2018 should be supported by higher wage growth (slightly above +2%) and lower inflation (+1.6%). Export gains reached EUR21bn in 2017, the highest since 2011. We expect export gains to rise further to EUR25bn in 2018 as strong global export growth will support higher volumes and companies' pricing power should continue to improve. After four consecutive years of contraction, manufacturing turnover growth registered a strong +9.9% in 2017, partly driven by the rise in oil prices. NFC' margins continued to strengthen in 2017 to 43.4% of the value added at end-2017, 2pp above the Eurozone average and the highest level since 2000. This coupled with the positive demand perspectives and low corporate debt should continue to support business investment growth in 2018 (forecast at +2.1%).

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Countries in Focus

Americas

U.S.: Robust outlook remains intact

Recent data remains solid. Durable goods orders rose +3.1% m/m to +8.9% y/y. Primary metals, perhaps driven by recent tariff threats, led the way, up +2.7% m/m to +12% y/y. More importantly, orders for core capital goods turned positive for the first time in three months, gaining +1.8% m/m to +8% y/y. All the y/y rates are well above historical averages. Volatile new home sales slipped -0.6% m/m, to a +0.5% y/y rate. Prices, however, rose +9.7% y/y, and supply is up from a scarce 4.8 months in November to a balanced 5.9 months in February, and combined with improving weather, sales may rebound in the spring. Consumer confidence slipped -2.3 points, perhaps on fears of a trade war (now falling), but remained near a 17-year high. Importantly, the percentage of respondents saying jobs were plentiful was at a 17-year high, and those saying jobs were hard to get were at a 17-year low.

Europe

Hungary: Ultra-loose for too long?

The Monetary Council (MC) of Hungary kept its key policy interest rate (3-month deposit rate; +0.9%) and the overnight deposit rate (-0.15%) again unchanged this week. Moreover, it announced that it will continue mortgage bond purchases and monetary policy interest rate swaps – additional easing measures introduced earlier this year – for an extended period. We do not believe that this ultra-loose policy stance is still necessary as growth is strong (+4.4% y/y in Q4; +4% in full-year 2017). Admittedly, inflation is still below the MC's 3% target and has declined to +1.9% y/y in February from 2.6% in August 2017. However, this has been helped by a number of one-off effects, including (i) VAT rate cuts, (ii) lower fuel inflation, (iii) reductions in the corporate tax rate in 2017 and employers' social contributions in 2018 that have offset rapid wage growth so far. We expect these effects to unwind over the course of the year, inflation to rise as a result to 3.3% by end-2018, and the MC to shift towards moderate tightening in H2. Should the latter not happen, then there is a risk of economic overheating.

Africa & Middle East

Tunisia: As time goes by

The IMF announced that about USD250mn will be disbursed to Tunisia. This is rather symbolic as it will add only about 5% to foreign exchange reserves (USD4.8bn) thus not really alleviating the liquidity issue reflected in their current level of import cover of 2.5 months. As economic growth is forecast to recover to +2.5% in 2018, imports should rise by +11% in 2018, putting even more pressure on the import cover ratio. As a result of the low liquidity, the Central Bank let the dinar depreciate; and inflation increased to +7.1% y/y in February. The government's willingness to reduce the fiscal deficit (-6.1% of GDP in 2017) was reaffirmed but little progress was seen in the past, since public spending is a sensitive topic in the country. Hence, the Central Bank started to tighten monetary policy, hiking the key policy rate to 5.75% (+75bp). However, the real interest rate is still negative. The extent of the current account deficit (-9% of GDP of 2018) shows that some rebalancing is needed.

Asia Pacific

Singapore: After the peak

Latest data point to slower economic activity in February. SGD-denominated non-oil domestic exports (NODX) contracted by -5.9% y/y (after +12.9% in January) on the back of lower electronic exports and lower exports to China and the EU. Industrial production growth decelerated to +8.9% y/y (after +16.9% in January) driven by a slower performance in electronics and chemicals. Core inflation edged up to 1.7% (from 1.4% in January). Going forward, we believe that the trade slump in February was temporary and partially driven by seasonal effects (Chinese New Year). Yet, it is unlikely that the export-driven economy will experience growth similar to last year (+8.8% for NODX; +3.6% for real GDP) in 2018. First, demand from China should continue to grow but a slower pace than last year (China's GDP growth is forecast at +6.5% in 2018, down from +6.9% in 2017). Second, rising protectionist measures from the U.S. could hamper global trade growth. Against this background, we pencil in economic growth of +2.9% in 2018 in Singapore.

What to watch

- March 29 – Canada January GDP
- March 29 – Czech Republic Central Bank meeting
- March 29 – Egypt monetary policy meeting
- March 29 – Germany February labor market statistics
- March 29 – Germany March inflation (flash estimate)
- March 29 – Turkey Q4 and 2017 GDP
- March 29 – U.S. February personal income and outlays
- March 30 – France March CPI inflation
- March 30 – Russia Q4 GDP
- March 30 – Russia February industrial production
- March 31 – China March official PMIs
- April 2 – U.S. March ISM manufacturing index
- April 3 – Germany February retail sales
- April 3 – Turkey March CPI and PPI inflation
- April 4 – U.S. March ISM non-manufacturing index

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