Euler Hermes Economic Research

Weekly Export Risk Outlook

31 October 2018

In the Headlines

FIGURE OF THE WEEK

+0.2%

Q3 2018 GDP growth in the Eurozone (q/q, flash estimate)

U.S.: Strong GDP headline, weak details

Q3 GDP grew at an annualized rate of +3.5% q/q, in line with expectations. The y/y rate is now +3.0%, the fastest in four years, and the consumer posted a second strong quarter at +4.0%, after +3.8% in Q2. But there were some downsides as well: +2.0% of the +3.5% headline gain came from the largest increase in inventories in seven years; net exports knocked -1.8% off the headline, the most in 33 years as imports surged +9.1% while exports shrank -3.5%; business investment grew only +0.8% after six quarters averaging +7.6%, and residential investment fell -4.0%, the third straight loss. Turning to September data, PCE core inflation remains at the Fed's +2% y/y target. Real personal disposable income slipped from +3.0% y/y to +2.9%, and real consumption fell from +3.2% to +3.0%. But consumer confidence rose for the fourth straight month, gaining +2.6 points to 137.9, the highest in 18 years. Both the present situation and expectations components rose to near 18-year highs as well. Overall, the economy still appears solid despite some disappointing data.

France: Alto ma non troppo

GDP growth picked up to +0.4% q/q in Q3 from +0.2% in Q2. Private consumption was the main explanatory factor (+0.5%), driven by unusual seasonality (recovery in transportation after Q2 strikes, and skyrocketing car output before implementation of new norms). But it showed no catch-up effect from subpar growth in Q4 2017 to Q2 2018. Export growth recovered also (+0.7%) and contributed to the growth acceleration in Q3, after broadly stagnating in H1. Meanwhile, investment patterns remained relatively unchanged. Corporate investment continued to increase (+1.4%), driven by digitalization (half of the growth) and capacity building (the capacity utilization rate is 85.3%). Household investment decreased by -0.2%, after being flat in H1 (and posting +5.6% in 2017). Overall, household spending growth in 2018 is expected to be the lowest (+1%) since 2013 (reflecting purchasing power issues in H1 and increasing savings in H2). We expect +0.3% q/q GDP growth in Q4 (as subdued demand weighs on manufacturing confidence which fell -3 points in October) and +1.5% in full-year 2018. A slight recovery to +1.8% is forecast for 2019, driven by an improving outlook for purchasing power.

Germany: Trade dispute weighs on the economy

Sentiment among German companies weakened further in October. The ifo business climate index fell to 102.8 points from 103.7 points in September. Companies were less satisfied with their current business situation and less optimistic about the months ahead. Without doubt, the trade dispute with the U.S. is increasingly weighing on the German economy. While the business climate deteriorated in manufacturing, trade and services, the respective index for the construction sector hit another record high. Labor market trends remained clearly positive in October. Compared to the previous month, the number of unemployed fell by 12 000 in seasonally-adjusted terms. Employment continues to grow strongly. In September, the number of people employed was up by +1.3% on the previous year. The rise in employment continues to be solely due to the increase in jobs liable to social insurance. It recorded an increase of +2.2% in August. On the back of a somewhat clouded growth outlook for the German economy, we expect the positive labor market trend to continue, albeit at a slower pace.

Italy: GDP stagnation in Q3 bodes ill for 2019 fiscal plans

In the third quarter of 2018, the Italian economy recorded no economic growth compared to the previous quarter. This is the weakest rate of GDP expansion recorded in almost four years. While no detailed breakdown of the main GDP components is available yet, in our view the disappointing Q3 growth reading is a result of the elevated level of policy uncertainty observed in Italy over the past few months. This has likely weighed on investment and consumption decisions. In addition, global trade growth has weakened this year, as a result of which tailwinds to the Italian economy from the external sector have likely moderated. No imminent pick up in Italian economic momentum is in sight, as uncertainty around the government's fiscal policy continues to linger. The Italian economy is unlikely to grow more than +1% this year, down from +1.5% last year.

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Countries in Focus

Americas

Brazil: Corporates are not home and dry yet

As expected, far-right candidate Jair Bolsonaro won the runoff of the Brazilian presidential election last Sunday with more than 55% of the votes, beating opponent Fernando Haddad (workers' party of PT) by 10 million votes. Our new report shows that his pro-business policy platform is the "least worst" choice for corporates, triggering a small confidence boost while potentially leading to the creation of 90 000 additional companies in 2019 compared to 2018. Yet Bolsonaro's economic program lacks details, some proposals are unrealistic (severe austerity could cut -1.2pp of GDP growth in 2019) while governability issues will remain. Lastly, the president's economically liberal policy platform could be unstable. Hence, in the context of an underwhelming outlook for economic growth in Brazil and shrinking global liquidity, corporates are not home and dry yet, as borrowing costs could increase in the medium term. Mind sectors whose debt is at risk: retail, auto suppliers, textiles, food and energy.

Europe

Turkey: Monetary policy on hold

The Monetary Policy Committee of Turkey kept its set of policy interest rates unchanged on 25 October (including the one-week repo rate at 24%), even though inflation had surged to 24.5% y/y in September. Markets have reacted calmly so far, with the TRY slightly up and long-term interest rates slightly down since the move. However, the ISE 100 stock market index has continued its downtrend since 18 October, reflecting the weakening real economy. Business confidence deteriorated further in October. The Services Sector Confidence Index fell to 75.7 points, the lowest level since records began in 2011 (after it had dropped to 79.4 in September from 88.0 in August). Retail Trade Confidence declined to a new low of 87.0 in October. Construction Sector Confidence edged up to 58.7 in October (from 57.3 in September) but this is still the second lowest score since 2011. We expect a hard landing of the economy with just +0.4% growth in 2019 (after +3.3% in 2018).

Africa & Middle East

Qatar: Growth is gathering momentum

Real GDP growth picked up to +2.5% y/y in Q2 from +2% in Q1 (the latter was revised upwards from a previous estimate of +1.4% y/y). The acceleration in Q2 was mainly due to a narrowing of the contraction in the hydro-carbon sector to -1.1% (from -2.1% in Q1) while growth in the non-hydrocarbon sector rose slightly to +6.1% (from +5.8% in Q1). Notably, the manufacturing (+14.1%) and construction (+15.3%) sectors continued to expand strongly. We expect the hydrocarbon sector to recover further in H2 thanks to the revised OPEC agreement from end-June which should result in an increase in Qatari oil output. Hence we project GDP growth to accelerate further in H2 and reach +2.6% in 2018 as a whole. Meanwhile, consumer prices contracted by -0.4% y/y in September, after a +0.6% increase in August, driven by declines in prices for communication (-11.9%), recreation and culture (-4.6%), utilities (-2.9%) and foodstuff (-2.5%). We expect average inflation of +0.4% in 2018.

Asia Pacific

South Korea: Time for action

Economic activity rose by +0.6% q/q in Q3 of 2018 (a pace similar to Q2). Consumption was the main driver, with a solid growth (+0.8% q/q) driven by an acceleration of both government and private consumption. Investment contracted sharply (-4.5% q/q). External trade contribution to growth was positive, with a solid export performance (+3.9% q/q). A fiscal stimulus package consisting of social welfare measures and the creation of public sector jobs helped to keep consumption in-check. Private investment is being hindered by measures to curb housing prices, rising uncertainties around trade and an increase in minimum wages. In that context, it is likely that the central bank will put the tightening cycle on hold, and fiscal support would increase. The government has already announced a +9.7% increase in expenditure in 2019. Economic growth is set to rise by +2.8% in 2018 and +2.7% in 2019.

What to watch

- November 1 – US Q3 productivity
- November 1 – Turkey October Manufacturing PMI
- November 1 – US October ISM manufacturing index
- November 1 – Russia October Manufacturing PMI
- November 2 – US October employment situation
- November 2 – Poland October Manufacturing PMI
- November 2 – US September international trade
- November 2 – Eurozone, France, Germany October Manufacturing PMI
- November 5 – Indonesia GDP for Q3
- November 5 – Spain October unemployment rate
- November 5 – Turkey October CPI and PPI
- November 6 – Germany September factory orders
- November 6 – Russia October Services PMI
- November 7 – Germany September industrial production

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