Euler Hermes Economic Research

Weekly Export Risk Outlook

21 November 2018

FIGURE OF THE WEEK

-4.6%

Sept. 2018 m/m decline in retail sales in Turkey

In the Headlines

U.S.: Consumers poised for the holidays

The latest data goes from good, to OK, to bad. Most importantly, the consumer seems poised to give a solid boost to holiday sales and the overall economy. Retail sales gained a strong +0.8% m/m to a +4.6% y/y rate in October. However, the headline was driven by a +3.5% m/m surge in gasoline sales and a +1% m/m gain in auto sales. After stripping out volatile components, core sales gained only +0.3% m/m but remained at a strong +4.5% y/y rate. Gains were widespread with a timely +1.3% m/m jump in department stores. Separately, industrial production was a bit more modest at +0.1% m/m, with the critical manufacturing component rising a stiffer +0.3% to +2.7% y/y. Thirteen of 19 sub-sectors are expanding, the most in over seven years. Housing, however, may now be the weakest link in the economy, buffeted by rising mortgage rates, high prices, and low supply. The housing market index fell a sharp -8 points to 60, the lowest in over two years. The future sales component fell -10 points, the most in 31 years. Housing starts and permits both fell into negative y/y rates at -2.9% and -6%, respectively.

Russia: Q3 growth disappointed but Q4 set to be better

First estimates indicate that real GDP growth decelerated to +1.3% y/y in Q3, down from +1.9% in Q2. The outcome in Q3 was disappointing as increased oil production and higher oil prices as well as the FIFA World Cup had led to expectations of stronger growth. But monthly activity data painted a mixed picture. Real retail sales growth edged down to +2.9% y/y in Q3 from +3.1% in Q2, indicating that private consumption remained the key albeit slowing growth driver in Q3. The increase in calendar-adjusted industrial production picked up to +2.8% y/y in Q3 from +2.6% in Q2. However, agriculture dropped by -6.1% y/y and construction output fell by -0.4%. Uncertainty regarding new U.S. sanctions have possibly curtailed corporate investment in Q3. Looking ahead, early indicators point to a rebound in Q4. Industrial production growth accelerated to +3.7% y/y in October. And the Manufacturing PMI improved to a six-month high of 51.3 points in October, up from an average 49.0 in Q3 and back into growth territory. Moreover, the Services PMI jumped to an 11-month high of 56.9. Overall, we maintain our real GDP growth forecasts of +1.6% in 2018 and +1.5% in 2019.

Turkey: Currency crisis is taking its toll on real economy

Latest activity indicators show that the currency crisis has begun to impact the real economy in Q3, as expected (see also our Insight Turkey). In September, industrial production contracted by -2.7% m/m (after -1.3% in August) and also by -2.7% y/y, bringing the expansion in Q3 down to +1.6% y/y (from an average +7.6% y/y in H1). Moreover, real retail sales dropped by -4.6% m/m and -3.4% y/y, taking the performance in Q3 to just +0.4% y/y (which compares to an average +7.4% y/y in H1). The data suggests that investment and consumer spending are likely to decrease in H2 and perhaps also in 2019. We expect two to three quarters of real GDP contraction until mid-2019 and growth of just +0.4% in 2019 as a whole. Meanwhile, following the decisive 625bp interest rate hike in September, the TRY has recovered to around 5.35 against the USD from lows around 7.00 in mid-August, but its value is still -30% down YTD. As a result, the tradable sector has begun to rebalance as the markedly weaker currency has already caused a strong rise in import costs and a sharp contraction of imports (-17% y/y in September). In contrast, exports benefit from the more competitive currency and surged by +20% y/y. We expect the trade deficit will nearly half to –USD23bn in 2019 from around -USD43bn in 2018.

Hungary: Monetary policy stance remains ultra-loose

The Monetary Council (MC) of Hungary kept its key policy interest rate (3-month deposit rate; +0.9% since May 2016) and the overnight deposit rate (-0.15%) again unchanged this week, even though consumer price inflation had risen to a near-six-year high of 3.8% in October. The MC argued that volatile items such as fuel and food prices drove up headline inflation while core inflation remained more moderate at 2.6%. It expects the headline rate to ease somewhat and remain within its 3% ± 1pp target range in the next months. Euler Hermes projects average annual inflation of 3.3% in 2019, but a still overheating labor market poses some upside risk to this forecast. As the unemployment rate came in at 3.8% in Q3 2018 (+0.2pp q/q; -0.2pp y/y), nominal wages rose by a still high average +11.2% y/y in July-August, after +11.3% in Q2 2018, though this is down from a peak of +14% in Q2 2017. The MC reiterated that it was prepared for a future normalization of its monetary policy and we expect it to tighten when needed.

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Countries in Focus

Americas

Chile: Slower but still solid Q3 growth

Q3 GDP growth registered a stronger slowdown than expected as it came in at +0.3% q/q, after +0.7% in Q2 and +1.2% in Q1. Compared to the same quarter last year, growth decelerated to +2.8% (y/y) from +5.1% in Q2. This slowdown should not be overestimated as Q1 and Q2 2017 were weak, leading to a strong rebound in Q3 2017. Activity in Q3 2018 was mainly driven by net exports (+1pp), private consumption (+0.4pp) and investment (+0.3pp). Then where's the catch? The significant drag came from a change in inventories which subtracted -1.4pp from the q/q figure. Previous inventory building resulted from (too) high business optimism (the more companies expect activity to sustain or accelerate, the higher the inventory increase). In Q3, companies hence moderated their enthusiasm and cut inventories as external conditions have toughened, the central bank has begun monetary policy tightening (+10pp policy rate hike to 2.60% in October), copper prices have eased and consumption has shown signs of slowing.

Europe

Bulgaria: Gradual slowdown ahead

Flash estimates indicate that seasonally adjusted real GDP growth eased to +3% y/y in Q3 from +3.4% in Q2, taking the average of Q1-Q3 2018 to +3.3% y/y. The GDP breakdown reveals that strong domestic demand was again the sole growth driver in Q3, with final consumption rising by +6.9% y/y (unchanged from Q2) and fixed investment by +6.2% (+6.6% in Q2). Moreover, inventories added +1.9pp to Q3 growth (+1.3pp in Q2). The firm expansion in investment signals that Bulgaria is catching up with other Central European countries with regard to better absorption of EU funds. Meanwhile, external demand has continued to be a drag on growth in Q3. Exports contracted by -3.2% y/y (after -1.9% in Q2) while imports increased by a solid +5.1% y/y (+5% in Q2) so that net exports subtracted a hefty -5.4pp from Q3 growth (-4.5pp in Q2). Overall, we forecast full-year growth to moderate from +3.6% in 2017 to +3.2% in 2018 and +3% in 2019.

Africa & Middle East

South Africa: It's the same old story

Has South Africa experienced negative growth for a third quarter in a row in Q3? The answer will come on 4 December. Obviously, this is a risk since the Manufacturing PMI is still significantly below 50 (42.4 in October). Mining production posted another decrease in Q3 (by about -4% y/y). The palladium output was among the deteriorations, a disappointment as the demand for that commodity increased particularly in China as a result of the effort to curb emissions. The evidence of new power shortages was another bottleneck for the South African economy, showing that there has been no progress on SOE reform. Moreover, the World Bank's latest *Doing Business* survey suggests that some African countries with far lower income levels made good progress, with Kenya ranking 60th and Morocco 61st out of 190 economies. South Africa is still 82nd, with one of the worst assessments regarding trading across borders (rank 143). Overall, there is a clear downside risk to our growth forecasts (+0.7% in 2018 and +1.3% in 2019).

Asia Pacific

Thailand: Domestic demand-driven GDP growth in Q3

Real GDP growth slowed to +3.3% y/y in Q3 2018 from +4.6% y/y in Q2. Exports contracted by -0.1% y/y due to less shipments of agricultural commodities, a deceleration of demand growth for manufacturing products and weaker tourism. Private consumption accelerated to +5% y/y from +4.5% in Q2 and investment gained traction to +3.9% y/y (+3.2% y/y in Q2). The Manufacturing PMI declined to 48.9 points in October (from 50.0 in September) with lower new export orders, reflecting slower growth in global demand and still heightened trade tensions between China and the U.S. Looking ahead, domestic demand will likely be the main driver in the short run, driven by continued public investment in strategic infrastructure (Eastern Economic Corridor Plan, e.g.) and ongoing accommodative monetary policy. Economic growth is expected to moderate to +3.6% in 2019 (from +4.2% in 2018).

What to watch

- November 22 – France Nov. business confidence
- November 22 – South Africa monetary policy meeting
- November 22 – Turkey Nov. consumer confidence
- November 23 – Canada September retail sales
- November 23 – Germany Q3 GDP (with details)
- November 23 – Poland October retail sales
- November 23 – Poland Nov. business confidence
- November 24 – Nigeria Q3 GDP
- November 26 – Czechia Nov. economic sentiment
- November 26 – Germany Nov. ifo business climate
- November 26 – Turkey Nov. business confidence
- November 27 – China October industrial profit
- November 27 – France November consumer confidence
- November 27 – U.S. November consumer confidence
- November 26-30 – U.S.: eight Fed speeches

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