Euler Hermes Economic Research

Weekly Export Risk Outlook

12 December 2018

FIGURE OF THE WEEK

-1.1%

Q3 2018 q/q GDP decline in Turkey

In the Headlines

Turkey: Recession and rebalancing on their way

The economy is on course of slipping into a technical recession (defined as two consecutive quarters of negative q/q growth), as expected, as real GDP contracted by -1.1% q/q in Q3. The currency crisis has taken its toll on domestic demand. Consumer spending decreased by -3.9% q/q and fixed investment by -3.6% in Q3. Even public spending shrank by -2.9% q/q. The strong TRY depreciation also triggered a sharp rise in import costs and caused real imports to decline by -6.3% q/q. However, real exports benefited from the weaker TRY and grew by +4.1% q/q in Q3, so that net exports mitigated the overall decline in GDP. In y/y terms, real GDP still grew by +1.6% in Q3, but this was markedly down from an average +6.3% in H1. We expect the recession to continue and forecast full-year growth of just +0.4% in 2019. Meanwhile, the rebalancing of the external sector has continued. In October, the first monthly trade surplus in almost ten years was posted while the current account recorded its third consecutive monthly surplus, at +USD2.8bn, reducing the 12-month rolling deficit to -USD39.4bn. We forecast the annual current account deficit to narrow from -5.5% in 2017 to -3.4% in 2018 and -1.5% in 2019.

France: It's getting worse, before it gets better

The yellow vest movement already took its toll on consumer spending which is now likely to decrease by -0.2% q/q in Q4 (as in Q2, after some previous strikes). As a result, GDP is expected to stagnate in Q4, resulting in +1.5% growth in 2018 overall. Moreover, the movement should have an impact on insolvencies. There were +700 additional business insolvencies in Q3 2018 as compared to the same quarter a year ago. We forecast +1000 additional insolvencies in Q4, taking the full-year number in 2018 to the same level as in 2017. The policy measures announced to end the strikes will have two key impacts. The cancellation of the fuel tax rise will add to the recent slowdown of the oil price and send consumer prices down to +1% y/y by May 2019 (from +2.2% in October). More fiscal measures (about 0.5% of GDP designed to increase the minimum wage and decrease social contributions for low incomes) were also announced. They should trigger a comeback to higher growth (+1.7% in 2019, with +0.5% q/q in Q1) but also threaten to post a fiscal deficit above the -3% of GDP threshold.

U.S.: A softer tone

Recent economic data has become softer. The economy added 155k jobs in November, which was a decent increase but was short of expectations of 190k, and the previous two months were revised down. While the unemployment rate stayed at 3.7%, the lowest since 1949, the broader U-6 rose +0.2pp to 7.6%. Hourly wages growth was unchanged at +3.1% y/y but a shorter workweek resulted in weekly wages falling from +3.4% y/y to +2.8%. Separately, the ISM services and manufacturing reports were both strong, but another manufacturing report was mixed. New orders for core durable goods fell for the third consecutive month, while shipments of those goods rose. The Fed's Beige Book showed slowing growth in some districts, cost increases from tariffs, and "somewhat weaker" non-auto sales. Various reports indicate that Fed officials are becoming substantially more dovish and may sharply reduce the pace of rate increases after next week's almost certain hike. The NFIB's small business optimism index fell to the lowest in seven months.

China: A difficult end of year

Trade figures were disappointing in November. USD-denominated exports growth slowed to +5.4% y/y (from +15.6% in October) and imports growth slowed to +3% (after +21.4% in October). The slowdown reflects a correction after a higher than expected performance in Q3 as corporates frontloaded new orders before a potential rise of tariffs (previously scheduled for January). We expect trade figures to remain week in December before recovering slightly in the first half of next year as U.S.-China relations normalize. Meanwhile, headline inflation slowed to 2.2% y/y (after 2.5% in October) and producer prices rose a modest 2.7% (down from 3.3%), with the latter signaling some risk of deflation. We believe that the slower price growth is related to a combination of factors that include weaker oil prices, a wave of tariff cuts implemented by China and softer growth in domestic demand. Looking ahead, we expect consumer price inflation to remain relatively low in 2019 at 2.5% on average on the back of modest oil prices (we forecast USD69 per barrel) and slower economic growth (+6.3%).

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Countries in Focus

Americas

Canada: Record setting jobs report

The November employment report literally set records. The economy created 94,100 jobs, the most in any single month since records began in 1976. The unemployment rate dropped to yet another record low of 5.6%. The participation rate rose +0.2%, and the workweek gained a sharp +0.9%. Overall it was a vibrant and energetic report. Fortunately for the Bank of Canada (BoC) there was one soft spot, which was that the +0.1 m/m increase in wages wasn't enough to offset recent weakness, so the y/y rate fell to +1.7%. Earlier in the week the BoC had left the policy rate unchanged but had issued a substantially more dovish statement, and the slower wage growth supports its case. The BoC cited weakness in the energy sector, global trade issues suppressing demand, and "less momentum going into the fourth quarter." Nonetheless it is most likely that the BoC will hike rates at least once in 2019. We forecast GDP growth of +2% in 2019 and +1.8% in 2020.

Europe

Poland: Strong growth in Q3, slowdown expected in 2019

Real GDP growth maintained a strong pace of +5.1% y/y in Q3 (unchanged from Q2). However, the demand-side breakdown revealed that Q3 growth was mainly driven by domestic demand, in contrast to Q2 when it was broad-based. Private consumption rose by +4.5% y/y and government consumption by +3.6% in Q3. Capital formation rebounded strongly in Q3 after the temporary moderation in Q2, with fixed investment up by +9.9% y/y and inventories contributing +1pp to y/y growth. Meanwhile, external trade activity lost momentum in Q3, with exports up +4.9% y/y (+7.6% in Q2) and imports up by +6.9% (+6.5% in Q2) so that net exports subtracted -0.9pp from Q3 growth (+0.9pp in Q2). Looking ahead, real retail sales growth moderated to +4.4% y/y in October from an average +5.5% in Q3 and industrial output growth to +5% y/y from an average +5.9% in Q3. Moreover, the Manufacturing PMI dropped to a four-year low of 49.5 points in November. We expect the economy to cool in the coming quarters and forecast full-year GDP growth of +3.5% in 2019, after +4.9% in 2018.

Africa & Middle East

Nigeria: It's (oh) so quiet

In Nigeria, GDP growth was quite stable in Q3, at +1.8% y/y. This figure is quite deceptive, since the implementation of delayed fiscal spending from H1 should have supported growth in Q3. It also implies that full-year growth will likely miss our former expectation. As a result, we revise our forecasts to +1.8% in 2018 (instead of +2%) and +2.2% in 2019 (down from +2.5%). Growth is still far from recovering to the levels observed before the oil price collapse (+6.3% in 2014). Nigeria is benefiting from more favorable financing conditions (a new USD2.9bn Eurobond issuance was made in November and the import cover of foreign exchange reserves has reached eight months) but investment in infrastructure remains quite low and pro-business reforms are still lagging. Nigeria's ranking in the World Bank's *Doing Business 2019* survey has made no progress overall (146th) and is particularly low on some key items (171st on getting electricity, 184th on registering property, 149th on resolving insolvency), explaining why the growth potential remains so low.

Asia Pacific

Australia: Under pressure

Economic growth slowed to +0.3% q/q in Q3 after a strong +0.9% in Q2. The main culprits were private investment (-0.8% q/q), households consumption (+0.3% q/q) and exports (+0.1% q/q). Government expenditures remain the major growth driver, mainly in the form of public investment (+3.4% q/q). Looking ahead, weaker business sentiment in the manufacturing sector (the Manufacturing PMI dropped to 51.3 points in November from 58.3 in October) associated with a slowdown in gross operating profits growth in Q3 point to a continued weakness in private investment. Moreover, a weaker housing market and a modest growth of income will act as a drag on consumption. In that context, we expect economic growth to decelerate to +2.5% in 2019 (from an estimated +3% in 2018).

What to watch

- December 13 – Eurozone ECB meeting
- December 13 – Turkey monetary policy meeting
- December 13 – Ukraine monetary policy meeting
- December 13-14 – EU summit
- December 14 – Russia monetary policy meeting
- December 14 – U.S. November industrial production
- December 14 – U.S. November retail sales
- December 15 – Mexico 2019 budget proposal
- December 17 – Turkey October industrial production
- December 18 – Argentina Q3 GDP
- December 18 – Germany ifo business climate index
- December 18 – Eurozone November inflation
- December 18 – Hungary monetary policy meeting
- December 19 – Poland November industrial production
- December 19 – Japan November trade figures

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