Euler Hermes Economic Research

Weekly Export Risk Outlook

10 April 2019

FIGURE OF THE WEEK

4.0%

March y/y inflation in Romania

In the Headlines

Eurozone: Higher loan demand from SMEs in Q1 2019

The ECB's dovish stance in terms of interest rate guidance and the extension of the TLTRO for another two years have pushed banks to favorably adjust credit standards for loans to corporates. Back in Q4, they were expecting credit conditions for loans to corporates to tighten but instead they remained broadly unchanged in Q1 2019 (-1%). However, large companies benefitted from an easing of credit conditions (-5%) while SMEs saw a small tightening (+1%). By country, credit standards eased for corporates in France and the Netherlands, remained unchanged in Spain and Italy, and tightened in Germany. In terms of demand, a stable trend was observed by banks in Q1 2019, instead of a rise which had been the norm since Q2 2015. Demand increased for loans to SMEs and remained unchanged for loans to large firms. We estimate that the SME bank financing gap could reach -3% of GDP in 2019 (or EUR400bn) should SMEs ask for the share of loans they consider as relevant for their future activity. By country, net demand for loans to enterprises increased in Germany and the Netherlands, while it declined in Spain and Italy given lower needs related to investments.

France: Another good export performance

The manufacturing production index unexpectedly recovered in February to a level that was not far from the peak reached in December 2017. Quite paradoxically, this growth appeared export-driven despite a context of overall trade uncertainty (car sector problems, Brexit fears). Chemicals (incl. pharmaceuticals) and transport equipment accounted for the bulk of the manufacturing production growth. It mirrored a strong start of French exports in 2019 (+EUR5.3bn y/y in the first two months). Transport equipment made +EUR1.6bn of export gains and chemicals benefited from +EUR1.5bn of additional exports. More than half of the overall export gains were realized in China (+EUR1.5bn, mainly aeronautics) and the U.S. (+EUR1.3bn, thereof +EUR0.8bn in aeronautics and +EUR0.2bn in pharmaceuticals). Export towards the UK increased by +EUR0.9bn in a visible race of inventory building by the UK before the Brexit deadline. Among the main disappointments, car suppliers suffered export losses of -EUR0.2bn, particularly towards Germany, a byproduct of German carmakers' current difficulties.

U.S.: Employment rebounds

The March employment report was reasonably solid and provided a sigh of relief after February's exceptionally weak report. The economy created +196k jobs, above expectations of around +170k, and much better than February's mere +33k. Both the unemployment rate and underemployment rate remained at very low levels of 3.8% and 7.3%, respectively, and job gains were mostly widespread. Despite these positive signs there were some nagging details. A rebound had been expected in manufacturing, but instead it lost -6k jobs, the worst performance in 32 months. Wage gains were weak and drove the y/y rate from +3.4% to +3.2%. February job creation was revised up from +20k to +33k, but that still left it at an exceptionally low level. Finally, the labor force shrank for the third consecutive month, driving the participation rate down from 63.2% to 63.0%. Despite these irritating details, the bottom line is that the headline numbers are strong, and the report gives some reassurance after last month's report and recent disappointments in retails sales, durable goods, and services ISM.

Emerging Markets: One size does not fit all yet

Manufacturing sectors in Emerging Markets (EM) are still in stagnation, as reflected by current PMI indicators. In March, the Chinese official manufacturing PMI improved visibly from 49.2 to 50.5 points (see our recent analysis) but activity data in other EM was still quite flat. Our aggregate EM excl. China PMI was at 50.2 in March, marking the fourth month in a row of a near stagnation index. Overall, the isolated Chinese recovery shows that its stimulus did not help other EM yet. The EM with the weakest manufacturing activity indicators are still those that are quite open and specialized on the following sectors: metals, cars and telecoms (three sectors which currently also show low global PMI indices, according to IHS Markit). South Korea, Taiwan, Mexico, Poland and Czechia are exposed to weak-nesses in one or several of these sectors. Moreover, the PMIs of Turkey and South Africa are still well below 50. These two large EM experienced a recession in the last quarters and there is evidence that the pressure on these two economies has remained strong.

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Countries in Focus

Americas

Brazil: Preliminary signs of the reality check

The expected reality check for 2019 has started to materialize. Retail sales stalled in February, confidence fell to pre-Bolsonaro election levels as his approval ratings dropped, and the unemployment rate is back above 12%. As for companies, although industrial production rebounded in February (+0.7% m/m), it contracted in y/y terms for the sixth straight month, and business confidence weakened. Political confusion (corruption allegations in Bolsonaro's entourage, firing of a minister, disagreements with the House Speaker) and the first difficulties in the pension reform legislative process have also caused the Brazilian real (BRL) to follow a depreciating trend since the end of January, erasing almost all the gains made in the first month. The stock market rally is moderating after breaking the 100,000 points threshold (now around 96,000). As a result, we still forecast a sluggish recovery (+2% GDP growth this year) and painful and lingering pension negotiations which could raise borrowing costs again.

Europe

Romania: Inflation up but interest rates on hold

Last week, the National Bank of Romania (NBR) held its policy rate unchanged at 2.5%, even though CPI inflation had risen to 3.8% y/y in February and thus climbed above the upper bound of the NBR's 2.5% ± 1pp target range. Today it was published that inflation rose further to 4% y/y in March. The rate decision by the NBR Board was unanimous, but some Board members raised concerns about a number of upside risks to future inflation. These include that core inflation rose to 2.7% y/y in February from 2.4% at end-2018 and the further tightening of the labor market. The unemployment rate (national definition) remained at the historical low of 3.3% in January while the growth of wages (net average nominal earnings) re-accelerated to +18% y/y in the first two months of 2019 from +13% in Q4 2018. Moreover, the RON, which was remarkably stable in 2018, has weakened this year (-2% vs. the EUR YTD). We expect the NBR to continue to try to curtail macroeconomic imbalances by upholding firm control over money market liquidity, but this is likely to be accompanied by an interest rate hike later this year.

Africa & Middle East

Israel: Voters opt for continuity

Early parliamentary elections held yesterday are likely to result in a fifth term in office of incumbent PM Netanyahu. With almost all votes counted, his conservative Likud party is leading neck-and-neck with the centrist Blue and White alliance (both around 29%) of his main contender, ex-military chief Benny Gantz. But Likud and its right-wing allies are likely to be the largest bloc with around 65 seats in the 120-seat Knesset (the parliament). The political impact of the outcome could be continued and perhaps increased tensions between Israel and its foes in the region. Netanyahu, who is currently facing corruption allegations, made a crucial announcement during his campaign, suggesting a new government may annex parts of the occupied West Bank (those with Jewish settlements). The economic track record under Netanyahu is good. Real GDP grew by an average annual +3.6% over the past decade. We forecast growth of +3.1% in 2019 and +3.6% in 2020.

Asia Pacific

Japan: Fragility

The latest figures signal that the economy entered 2019 on a soft footing. Household spending growth slowed down to +1.7% y/y in February (from +2% y/y in January). Retail sales growth eased to +0.4% y/y (after +0.6% in January) and industrial production contracted (-1% y/y). March's business surveys provide a mixed outlook. The manufacturing PMI recovered slightly to 49.2 points (from 48.9 in February) but continues to indicate a contraction of activity (PMI below 50.0). The services PMI decreased to 52.0 (from 52.3 in February) but continues to signal expansion. In that context, the Central Bank will likely maintain its extra-loose monetary policy stance in 2019-2020. On the fiscal side, the authorities have enacted stimulus measures of +JPY2.03tn to offset the impact of the rise in the sales tax (to 10% from 8%) scheduled for October. If economic activity growth were to slow further, it is likely that that tax hike would be delayed.

What to watch

- April 11 – Germany March inflation (final)
- April 11 – Turkey February balance of payments
- April 11 – U.S. March producer prices
- April 12 – Canada March home prices
- April 12 – Hungary February industrial production
- April 12 – Romania February industrial production
- April 15 – Brazil February economic activity index
- April 15 – Bulgaria March consumer prices
- April 15 – China March total social financing
- April 15 – Poland March consumer prices
- April 15 – Slovakia March consumer prices
- April 16 – Argentina March inflation
- April 16 – Croatia March consumer prices
- April 16 – Turkey February industrial production
- April 16 – U.S. March industrial production

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Contact Euler Hermes Economic Research Team
research@eulerhermes.com

Publication Director
Ludovic Subran, Chief Economist
ludovic.subran@eulerhermes.com