Euler Hermes Economic Research

# Weekly Export Risk Outlook

20 February 2019

FIGURE OF THE WEEK

+0.02%

**Q4 2018 q/q GDP growth in Germany**

## In the Headlines

### U.S.: Retail results conflict, industrial production falls

Two of the largest U.S. retailers recently reported strong Q4 results. Sales at Amazon rose +8.2% y/y, and same-store sales at Walmart rose +4.2% y/y, but its online sales leapt +43% y/y. By contrast the government's December retail sales report was so bad that it lacked credibility, and may see a large revision. That report said that overall sales plunged -1.2% m/m, with losses in most major categories. Core retail sales, which strip out volatile items, were even worse at -1.8% m/m, the sharpest monthly decline in 19 years. The most unlikely detail of the report showed e-commerce falling -3.9% m/m, driving the y/y rate from a typical +11.1% to only +3.7%. The government report is an estimate based on a sample survey, but since Amazon and Walmart report actual results, they are more likely to be indicative of a healthy consumer. In other news, industrial production fell a sharp -0.6% m/m in January, the first decline in eight months. Manufacturing fell a steep -0.9% m/m, driving the y/y rate to +2.9% from September's high of +3.8%. Inflation reports continued to show little price pressures. Weekly jobless claims remain historically low but have risen +19.5% in the last four weeks.

### Germany: Economy moved sideways in second half of 2018

After the slight decline in economic output in the third quarter, real GDP increased only marginally by +0.02% q/q in seasonally adjusted terms in the final quarter of 2018. Domestic demand provided positive impetus. Investment rose strongly, private and public consumption also recorded an increase. By contrast, foreign trade did not provide any impetus. Exports and imports grew at a similar rate. The Federal Statistical Office also published revised figures for the previous quarters and for 2018 as a whole. According to these figures, the German economy did not grow by +1.5% in 2018 as previously published, but by +1.4% (working-day adjusted: +1.5%). We still do not expect the economy to slide into recession. However, especially in the first half of 2019, economic momentum is likely to be lower than we had previously assumed. More than usual, the economic outlook is currently subject to a high degree of uncertainty. Apart from political risks, we see the greatest forecast uncertainty in the following areas in particular: automotive industry, foreign trade and investment demand.

### Turkey: Recession deepens, rebalancing slows

Industrial production dropped for the fourth consecutive month in December, with the pace of contraction accelerating to -9.8% y/y (seasonally adjusted; -6.6% in November). This took annual growth of industrial output to just +1.8% for all of 2018, down from +8.9% in 2017. Likewise, retail sales dropped by -9.2% y/y in December, bringing the full-year 2018 expansion down to just +1.4%. Meanwhile, USD-denominated imports (goods and services) plunged by -27% y/y in December (-20% in November) while the previous rebound in exports (+7% in November) came to a halt in December (-2%). As a result, the monthly current account shifted back into deficit, after four months of surpluses. Still, the rolling 12-month external deficit is narrowing and should continue to do so, albeit at a slower pace. Amid these signs of a deepening recession, the Central Bank last week reduced reserve requirement ratios for banks in order to boost credit growth. However, the move may jeopardize the positive impact of the higher interest rates regime since September 2018 which led to a reduction of private sector credit growth to a healthy +15% y/y in December from an unsustainable peak of +39% in August 2018.

### South Africa: The trickiest is yet to come

In just two weeks, the South African growth rate for 2018 will be published. It will likely show a return to the low growth registered in 2016 (+0.6%) despite a sizeable fiscal deficit (-4.2% of GDP in 2018). However, the rising difficulties of key state-owned enterprises will likely imply some cost for public finances that will impact both the fiscal balance and public debt. Along with the structural current account deficit and its low coverage by stable (FDI) inflows, this suggests currency volatility and higher interest rate costs ahead. The Central Bank became hawkish last year, raising its policy interest rate (+25bps to 6.75% in November 2018) despite still low inflation (+4.3% y/y in January). Higher borrowing costs are particularly impactful since corporate debt has increased (debt service represents 87% of FX reserves). Ten-year government bond yields are still at 9.5%, a level far above South African nominal growth (which is at +5% currently), suggesting both higher inflation expectations and a significant currency risk premium.

# Countries in Focus

Americas

## Brazil: Don't count your chickens before they are hatched

Today, the government will present the pension reform to Congress, starting a lengthy, politically tense process. It comes after President Bolsonaro's first political crisis (the Secretary General was fired on the back of corruption allegations). The constitutional bill needs to gather a 60% majority in both houses of Parliament. Given Congress' fragmentation, Bolsonaro's lack of a stable coalition and confusing communication we do not expect the reform to be passed before H2 2019. Besides, the final reform is likely to be a watered-down version of the initial one; as of now it aims at saving some USD270bn in ten years in public funds by raising the minimum retirement age to 65 (men) and 62 (women) and shifting to a capitalization model (each individual contributes for their own retirement). At the same time, market and consumer optimism is at record highs, decoupling from hard data. Political gridlock or a disappointing reform could bring back market volatility and higher borrowing costs, as we warned last fall.

Europe

## Central & Eastern Europe: Growth is slowing but remains robust

First estimates indicate that real GDP growth in the group of 11 EU members in the CEE region came in at +4.2% y/y in Q4 (unchanged from Q3), taking full-year 2018 growth to an estimated +4.3%. The latter is slightly down from +4.7% in 2017 but well above the 10-year average of +2.3%. **Poland** outperformed the region last year with growth of +5.1% (for details see WERO 6 February 2019). In **Hungary**, annual GDP growth rose markedly to +4.8% (from +4.1%) amid ongoing overheating concerns stemming from rapid wage growth while monetary policy remains very loose. Growth accelerated also in **Slovakia** (to +4.1% from +3.4%) and **Latvia** (to +4.8% from +4.5%) while it moderated in **Czechia** (to +3% from +4.3%), **Bulgaria** (to +3.1% from +3.6%) and **Lithuania** (to +3.5% from +4.1%). **Romania** saw the steepest slowdown (to +4.1% from +7%) as the economy is rebalancing from overheating in 2017. Against the backdrop of an easing investment boom at home and a growth slowdown in Western Europe, we expect regional growth of the 11 EU members in CEE to moderate to around +3.3% in 2019.

Africa & Middle East

## Senegal: Economy stuttering, but no slump ahead

Senegal's GDP per capita grew by +17% between 2013 and 2018. The stability of growth was exceptional from 2014 to 2017, with the highest and the most stable expansion period of the last four decades, based on the implementation of the Emerging Senegal Plan. However, growth decreased markedly in 2018 against the backdrop of rising oil prices. As a result, GDP growth in 2018 (+4.5%) was the weakest compared to the previous three years. The manufacturing sector was particularly hit, with a -0.8% y/y performance in Q3 2018. Among other achievements, youth unemployment steadily decreased during the last years to just 5% of the population. However, the model is still vulnerable to a shift in general conditions since the current account deficit amounts to -8% of GDP. Despite the progress made, Senegal is still a low income economy. Its GDP per capita accounts for just 7% of the corresponding figure in an advanced economy. Hence, income shocks such as in 2018 have significant consequences on consumer confidence. In 2019, we expect GDP growth to re-accelerate to +6%.

Asia Pacific

## China: A temporary or a durable boost?

USD-denominated exports rose by +9.1% y/y in January (after a -4.4% decline in December) mainly driven by demand from the EU (+15.3%) and ASEAN (+12.5%). USD-denominated imports continued to contract but at a slower pace (-1.5% y/y after -7.6% in December) as imports from the EU recovered (+8.2% y/y) and demand for ASEAN goods decreased more moderately. Meanwhile, credit figures surprised on the upside, with strong growth of aggregate credit flows in January (+RMB4.6tn, after +RMB1.6tn in December). In other news, price figures revealed disappointing producer prices (+0.1% y/y in January) raising deflation fears. Looking ahead, we believe that these data should be interpreted with caution as they have been probably distorted by the Chinese New Year holidays. We cautiously maintain our GDP growth forecast for this year at +6.3% (after +6.6% in 2018).


# What to watch

- February 21 – France February business confidence
- February 21 – Eurozone Febr. PMI (flash estimate)
- February 21 – Poland February business confidence
- February 21 – U.S. January existing home sales
- February 22 – Canada December retail sales
- February 22 – Germany Q4 2018 GDP (with details)
- February 22 – Germany ifo business climate index
- February 22 – Turkey February business confidence
- February 22 – U.S.: four Fed members speak
- February 25 – Mexico Q4 2018 GDP (with details)
- February 26 – Hungary Central Bank meeting
- February 26 – U.S. February consumer confidence
- February 26 – U.S.: Fed Chair Powell speaks
- February 27 – China January industrial profits
- February 27 – Argentina Dec. economic activity index




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**Contact Euler Hermes Economic Research Team**
research@eulerhermes.com

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