

THE BIG SWITCH

Georges Dib

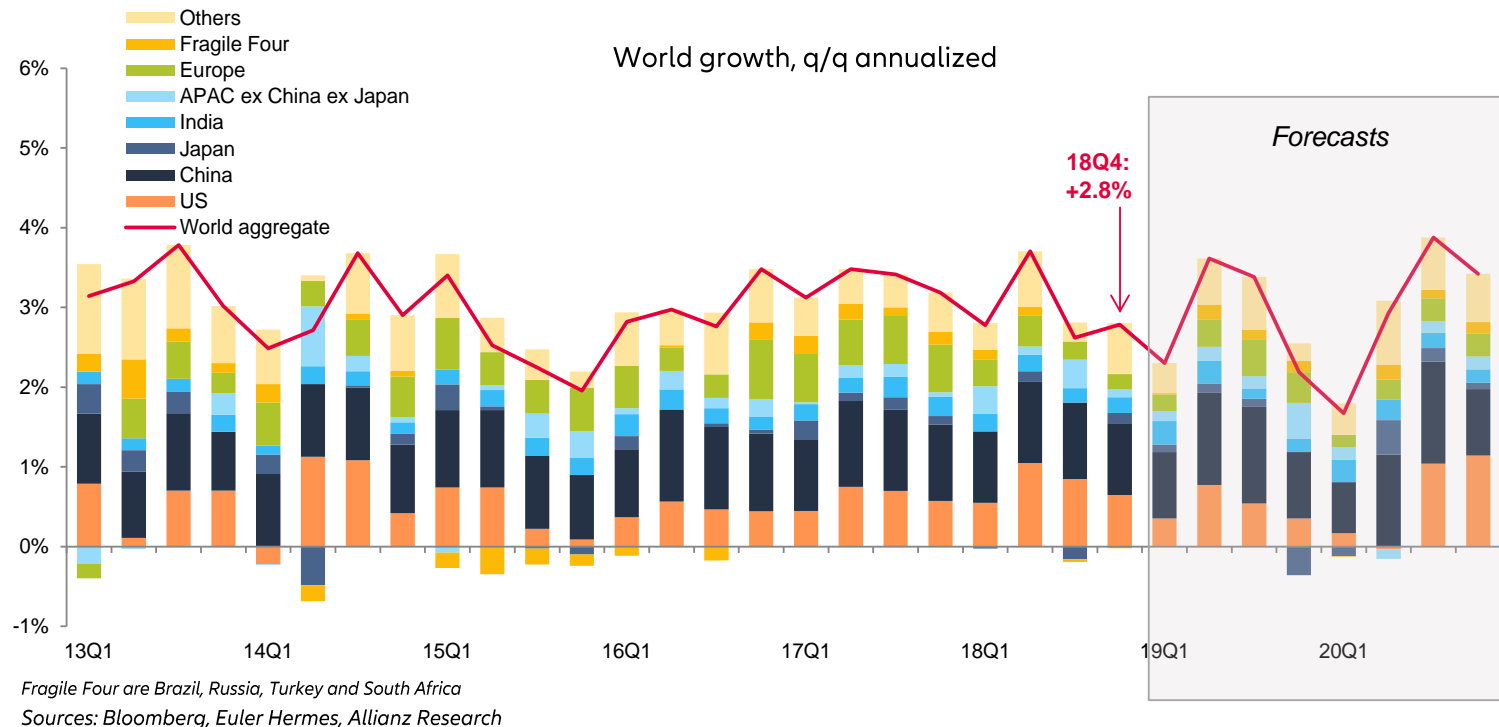
Economist

COSEC 50th anniversary

Porto, 6 May 2019



GLOBAL GROWTH: BUMPY ROAD AHEAD

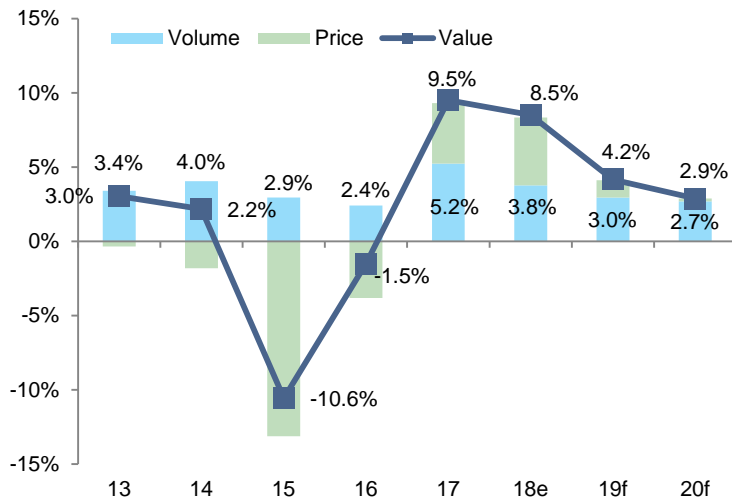


China's and the US fiscal stimulus will allow escaping the soft patch of Q3 18 – Q1 19. The recovery should be short-lived because of a negative shock occurring in the US with a maximum impact to be felt in Q1 20. The recovery of H2 20 will embody a normalization of growth in the US, the succession of stop and go maintaining developed economies below potential

GLOBAL TRADE: A VALUE ADJUSTMENT

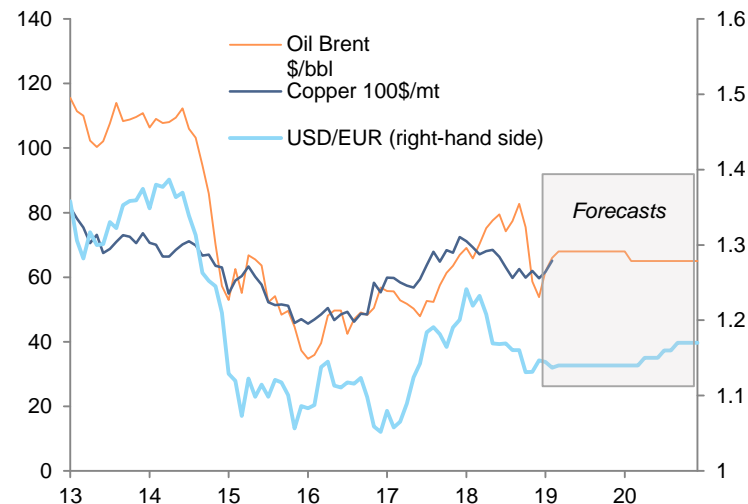


Global Trade of goods and services



Sources: Euler Hermes, Allianz Research

Commodity prices and USD/EUR exchange rate

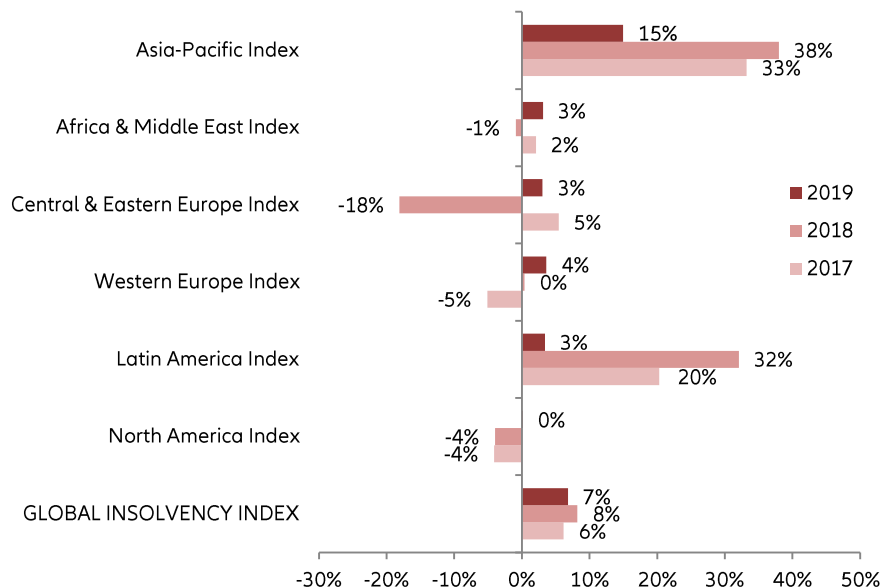


Sources: IHS, Euler Hermes Estimates

Global trade is expected to pick up in H2 19 as trade tensions should diminish while, China's economic stimulus, coupled with the residual impact of the US stimulus, is expected to start producing positive effects. The recovery of commodity prices and global activity should not be strong and rapid enough to avoid a global trade deceleration at +3.0% in 2019 compared with 3.8% in 2018. Indeed, a rapid deceleration of economic activity in the US as early as Q4 19 is expected to pursue the decelerating trend of global trade in 2020 being expected at 2.7% y/y.

GLOBAL INSOLVENCIES: ON THE UPSIDE, AS EXPECTED

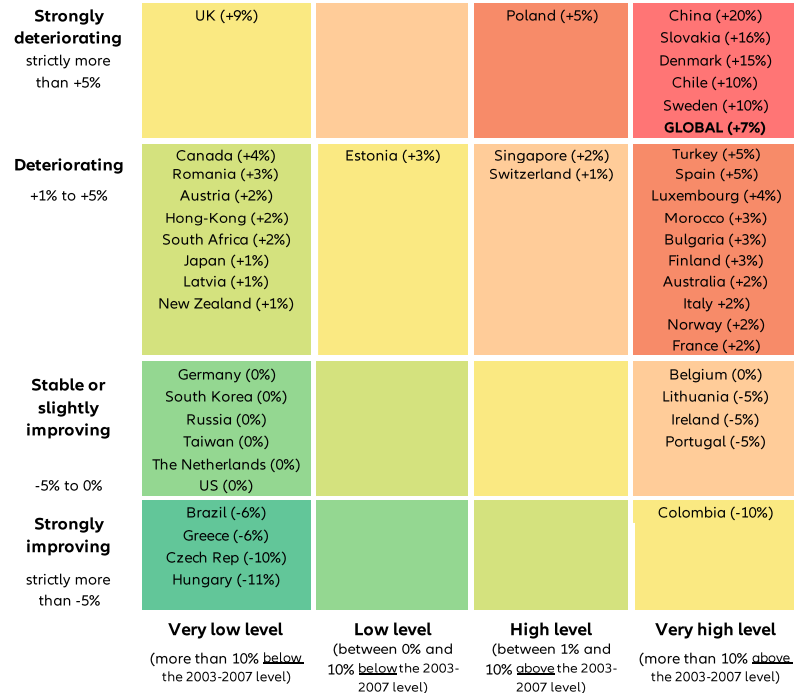
EH Global and Regional Insolvency Indices (yearly changes in %)



Sources: National statistics, Euler Hermes, Allianz Research

We expect our Global Insolvency Index to keep on increasing in 2019 (+7% after +8% in 2018), with a deceleration in Asia, a stabilization in the US and a rebound in Europe. We expect 2 out of 3 countries to post an increase in insolvencies, and 1 out of 2 countries to register in 2019 more insolvencies than over the 2003-2007 period

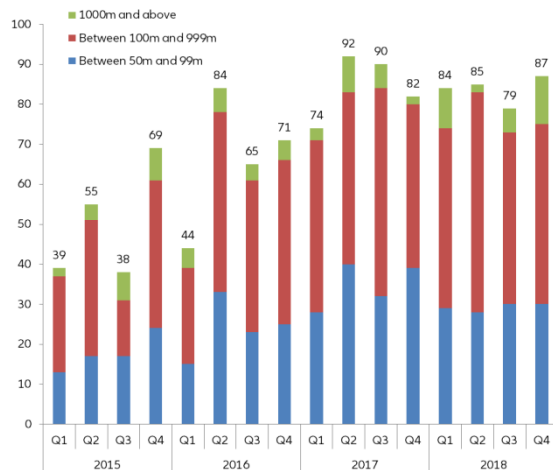
Insolvency Heat Map 2019



MAJOR INSOLVENCIES: HIGHER FREQUENCY, WORSE SEVERITY



Number of major insolvencies*
(by size of turnover in million of EUR)



(*) Companies with a turnover exceeding EUR50m
Source: Euler Hermes

Major insolvencies* by sector and by region (number of insolvencies)

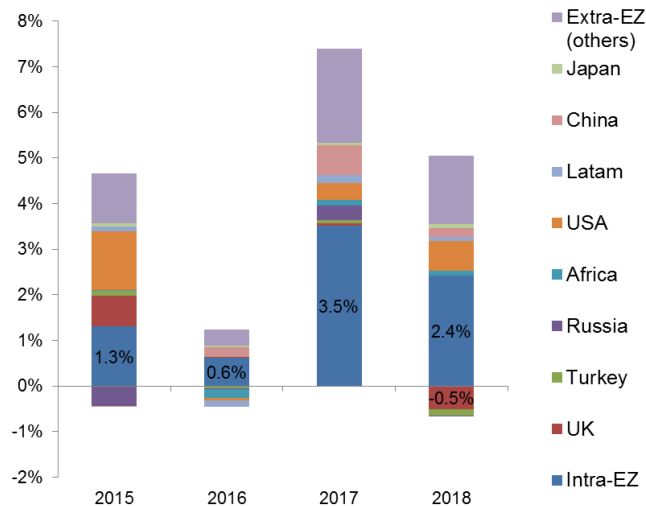
	Africa/Middle East and Latin America	North America	Central & Eastern Europe	Asia Pacific	Western Europe	TOTAL
Pharmaceuticals	-	-	-	-	1	1
Transport equipment	-	-	-	-	3	3
Electronics	-	-	-	2	3	5
Paper	-	-	-	1	4	5
Commodities	-	-	1	3	3	7
Chemicals	-	1	1	4	2	8
Computers & Telecom	1	-	-	6	1	8
Textile	1	1	1	3	3	9
Automotive	-	-	4	1	7	12
Household equipment	-	3	2	3	9	17
Transportation	-	3	4	1	9	17
Machinery/Equipment	-	-	6	4	11	21
Metals	-	1	-	10	10	21
Energy	-	8	7	7	2	24
Services	-	3	5	6	18	32
Agrifood	-	-	7	12	15	34
Retail	3	15	4	5	24	51
Construction	-	3	17	23	17	60
Total	5	38	59	91	142	335

(*) Companies with a turnover exceeding EUR50m
Source: Euler Hermes

2018 posted 335 major insolvencies (-3 cases), with a cumulative turnover of EUR158bn (+40%). Rise in severity comes from the biggest top failures with a turnover exceeding EUR100m : +10 cases in number (30) , with a cumulative turnover increasing by 87% to EUR100bn). **Hot spots** continued to be **Construction** (60 major insolvencies) , notably in Asia (+11 cases to 23), and **Retail** (51 cases), notably in Western Europe (24) – which remains the region with the highest number of major insolvencies. **Asia** is in second place with a noticeable rebound in Agrifood (+7 cases) as well as in Energy and Computer/Telecom (both +6). Retail in the US registered 15 new major insolvencies despite the already impressive list of 34 cases over 2015-2017.

EUROZONE: TRADE BETWEEN A ROCK AND A HARD PLACE

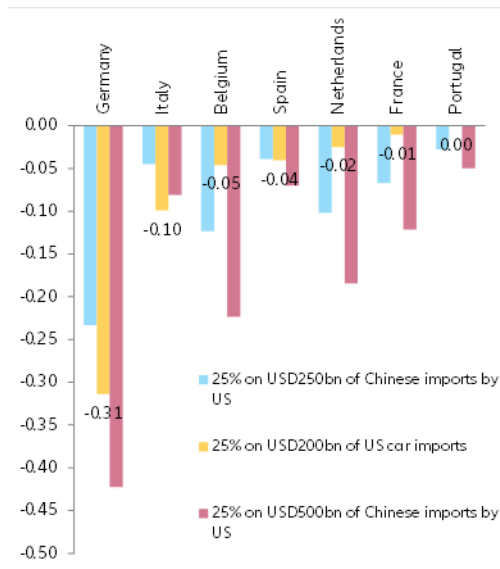
EZ exports by destination, annual growth and contributions



Sources: Eurostat, Allianz Research

The UK should not be a negative contributor to Eurozone exports in 2019

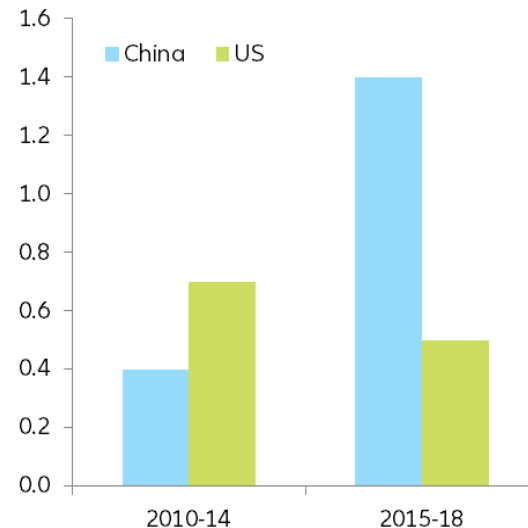
Export losses from US-China trade dispute (secondary and tertiary round effects), pp



Sources: Chelem, National sources, Allianz Research

Higher domestic difficulties in the US should divert President Trump's administration away from renewed protectionism

Elasticity between China and US real GDP growth (y/y) and the Eurozone

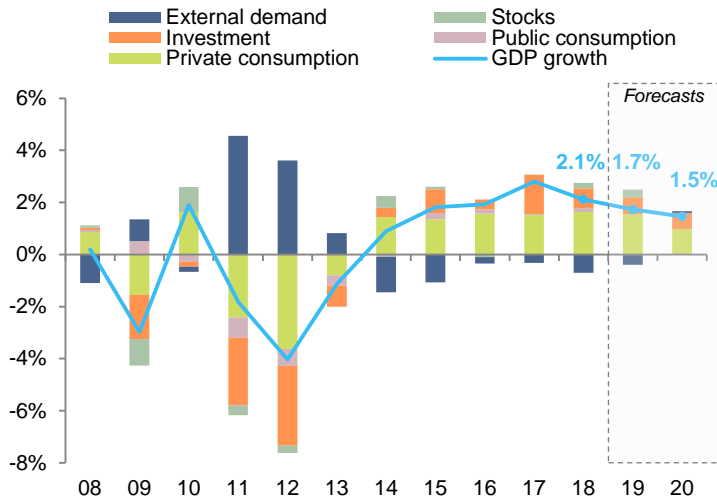


Sources: Allianz Research

China's stimulus should provide tailwind to Eurozone export growth in H2 2019

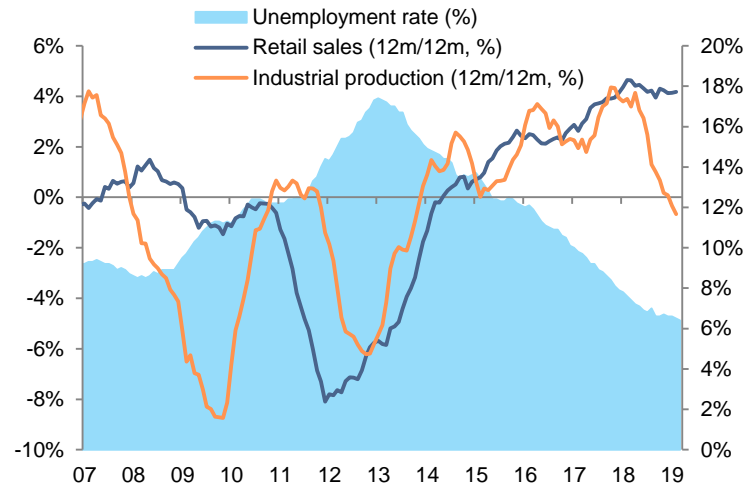
PORTUGAL FROM REMONTADA/RETORNO TO MODERATION

Bond yields and stock market index



Sources: IHS, Euler Hermes, Allianz Research

Unemployment and retail sales

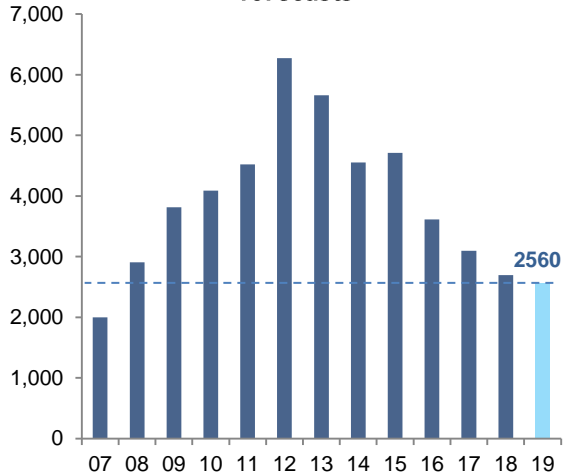


Sources: IHS, Euler Hermes, Allianz Research

Portugal reconciled with higher growth levels outpacing the Eurozone average, and should gradually slow in 2019 (+1.7%) and 2020 (+1.5%). Since 2014, Euler Hermes upgraded Portugal's country risk rating from B3 to B2 (Q3 2014), from B2 to BB2 (Q3 2016) and more recently from BB2 to BB1 in Q2 2018. After subtracting on average -2pps to growth between 2009 and 2013, private consumption has positively contributed to growth by an average of +2.3pps since then and should continue growing in 2019 and slow down in 2020. It has been lifted by rising income, thanks to the impressive decline in unemployment.

PORTUGAL: CORPORATES NOT FULLY HOME AND DRY YET

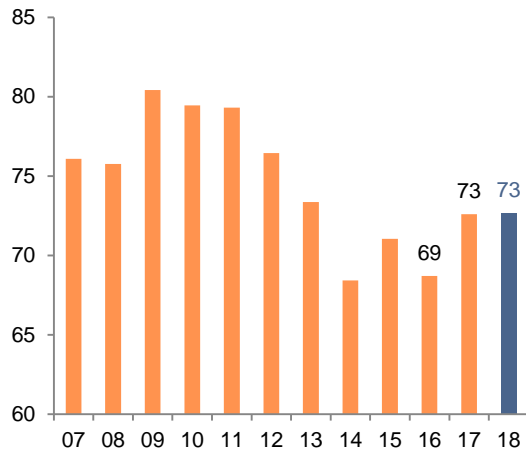
Number of corporate insolvencies and forecasts



Sources: Euler Hermes, Allianz Research

Number of corporate insolvencies has decreased along with economic recovery. Yet in 2019 total number of insolvencies will still be 28% above 2007 levels!

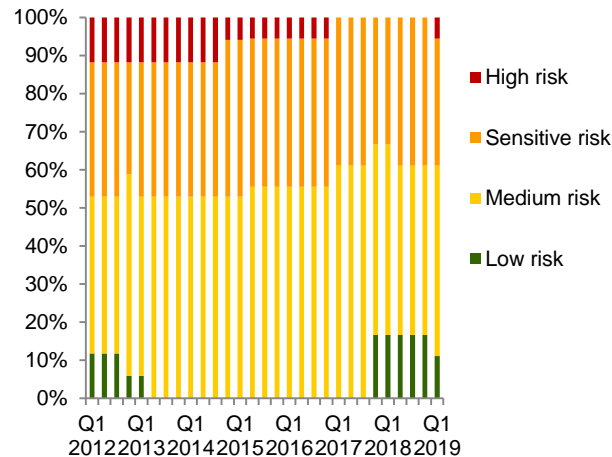
Days Sales Outstanding (DSO, in number of days)



Sources: Bloomberg, Euler Hermes, Allianz Research

As growth accelerated, companies extended their trust to their clients through longer payment delays. Portugal's DSO increased by +4 days to 73 days in 2017. In 2018, it stabilized as the slowdown called for more caution.

Sector risk ratings in Portugal

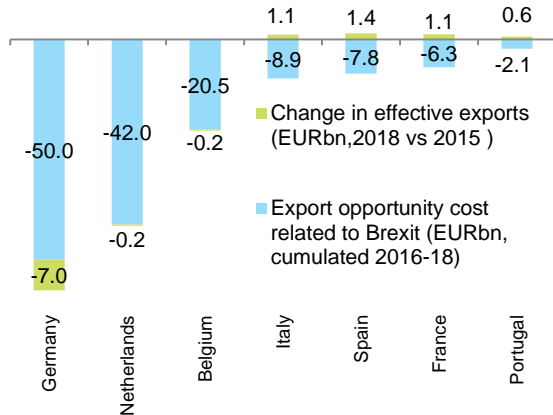


Sources: Euler Hermes, Allianz Research

Despite the impressive recovery of Portugal, business conditions have not strongly improved in all sectors. A majority of them are assessed at 'Medium' level of risk, but several others are at 'Sensitive' level of risk for profitability or liquidity issues (Construction, ICT sub sectors).

PORTUGAL: MODERATE RISKS ON TRADE, BUT SLOWDOWN AHEAD

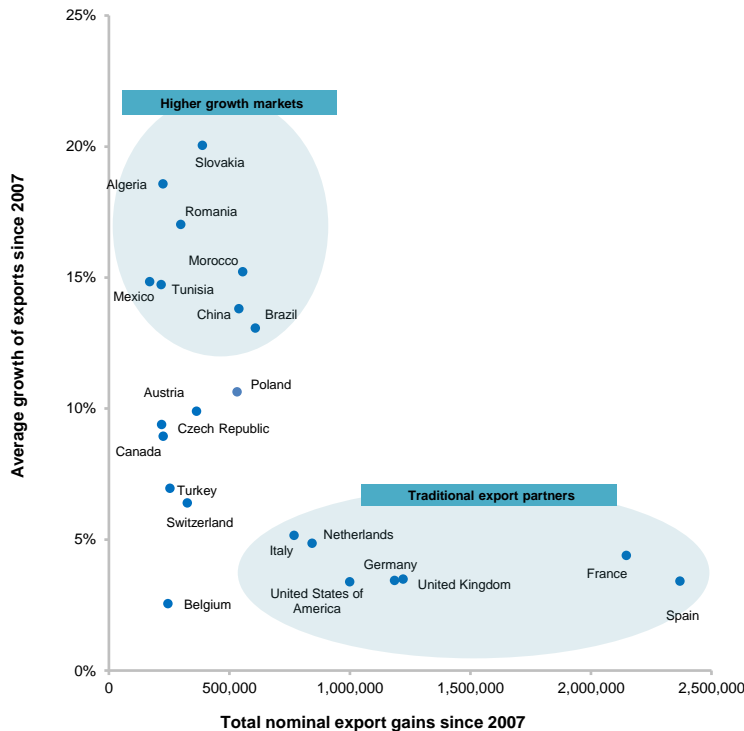
Lost export opportunities since the Brexit vote



Sources: Euler Hermes, Allianz Research

Brexit has already led to EUR2bn of lost export opportunities for Portuguese exporters since 2016. In France, -EUR6.3bn and in German, -EUR50bn. In case of a no-deal Brexit, export losses of EUR270mn (only 0.4% of total Portuguese exports).

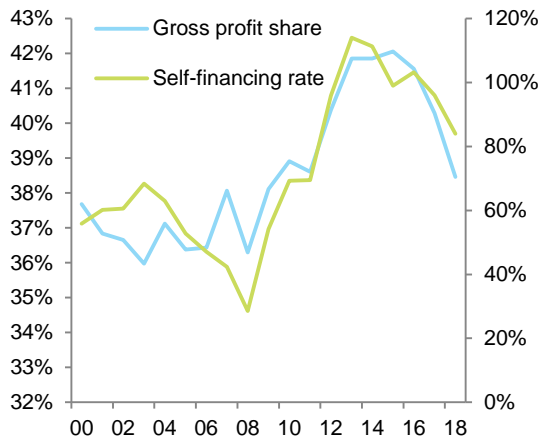
Export Partners



While the initial driver of the recovery was export growth (+60% real growth between 2009 and 2017 vs. 20% between 2001 and 2009), it should face headwinds as Portugal's major trading partners' activity slows. Export growth helped the share of exports in Portugal's GDP rise from around 30% to 44%. Now, companies need to look for the next growing country.

PORTUGAL: SECURING FINANCING STILL A CHALLENGE

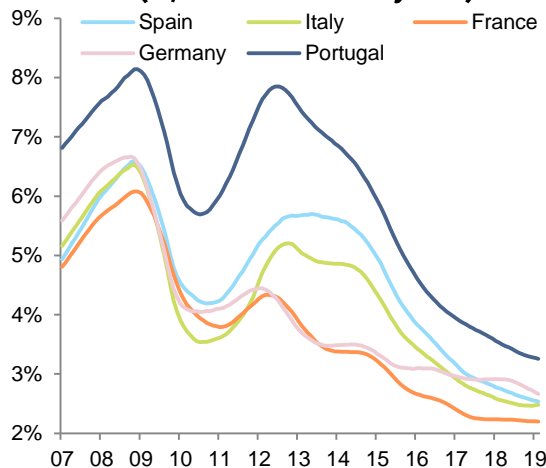
Profit share and self-financing rate of companies



Sources: IHS, Euler Hermes, Allianz Research

Margins are now lower than the Eurozone average at 38.5% vs. 41%. The self-financing rate of companies has dropped with margins. As it is < 1 , it means companies are in need of external sources to fund their investments.

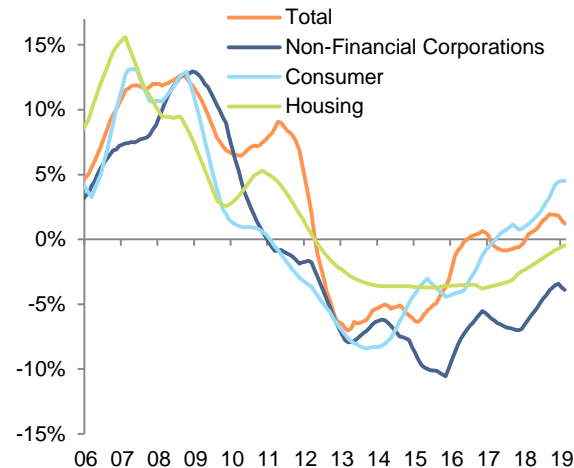
Interest rates on loans for SMEs (% for loans over 5 years)



Sources: Bloomberg, Euler Hermes, Allianz Research

Lower sovereign yields drove corporate spreads down to 2.7% end 2018 down from 7.6% in 2008. Yet interest rate on loans for SME remain higher than in peer countries

Sector risk ratings in Portugal

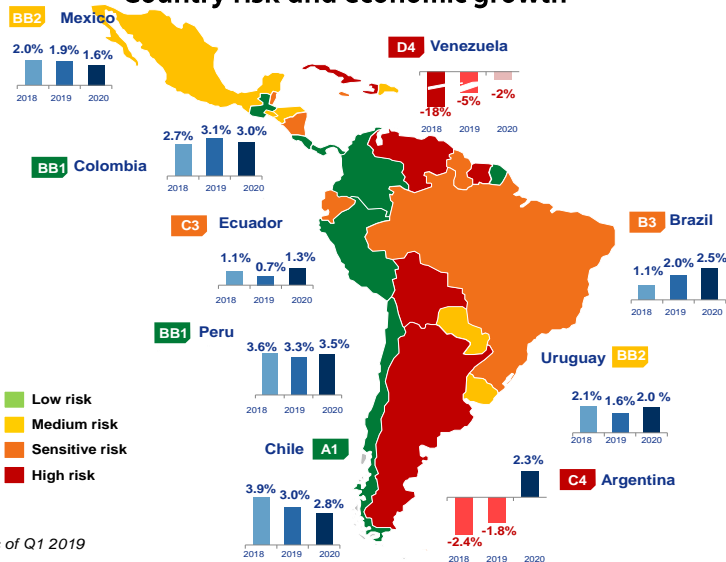


Sources: Euler Hermes, Allianz Research

Corporate credit is still contracting in the country. The national strategy for entrepreneurship ('Start-up Portugal') was set up to provide alternatives to bank loans such as equity finance, crowdfunding, peer-to-peer lending and co-investment.

LATAM: MONETARY RELIEF, BUT REALITY CHECK

Country risk and economic growth



Data as of Q1 2019

Sources: IHS, IMF, Euler Hermes, Auzanz Research

Growth will slightly accelerate (+1.4% in 2018, +1.9% in 2019, +2.4 in 2020). In Argentina, a reelection of Macri is still the baseline, but not a done deal. The rebalancing is not over and will continue to be painful for the real economy.

Latin America vulnerability scorecard

2019 forecasts		Argentina	Brazil	Mexico	Colombia	Chile
External vulnerabilities and debt rollover risk	Current account balance	-1.27%	-0.8%	-1.7%	-3.4%	-1.9%
	External debt (% GDP)	42%	17%	38%	32%	44%
	% of foreign-denominated debt (2017)	51%	18%	25%	27%	40%
	Reserve adequacy (Aug 18)	Adequate	High	Adequate	Adequate	Low
Cycle management	Real interest rate (Aug 18, policy rate - CPI inflation)	8.6%	2.4%	3.1%	1.0%	0.1%
	Real GDP growth	-1.8%	2.0%	1.9%	3.1%	3.0%
Fiscal risk	Fiscal deficit	-2.7%	-6.7%	-2.5%	-2.6%	-0.9%
	Public debt	86%	90%	54%	50%	26%
Policy uncertainty risk	Probability of policy mistakes	High	High	High	Low	Low

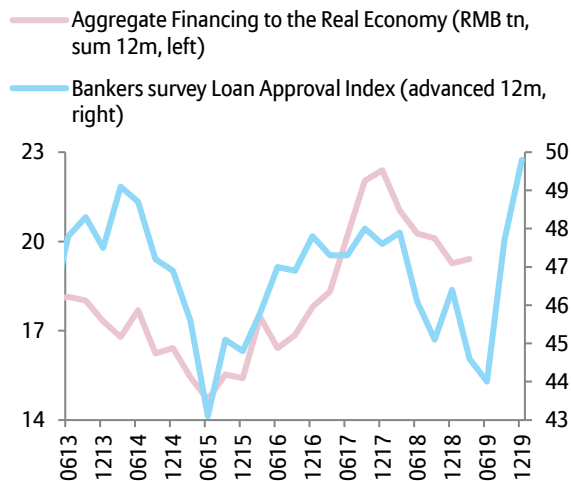
Sources: IHS, IMF, Euler Hermes, Allianz Research

Policy commitments and the Fed's big switch have favored optimism by providing a monetary relief: better sentiment, neutral investor opinion, lower yields, stronger currencies. Central banks could pause or postpone tightening.

Mind the reality checks: In Brazil we see better internal demand, but the pension reform is likely to disappoint, putting pressure on borrowing costs. Mexico's growth should be capped despite a better consumer outlook, as investors are wary of nationalistic policies.

CHINA: TANGIBLE EFFECTS OF THE STIMULUS ARE BUILDING UP

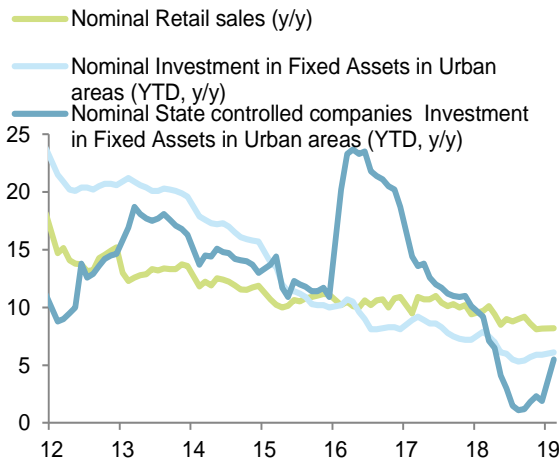
Financing conditions



Sources: IHS, Allianz Research

Credit conditions: bankers survey suggest a pick up of credit in the coming months.

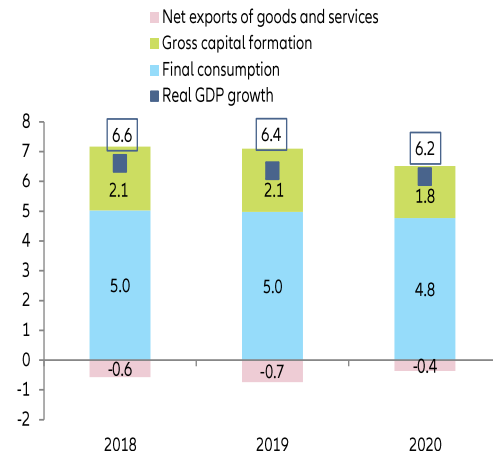
Demand indicators



Sources: IHS, Allianz Research

Demand: investment picks up speed as SOEs investment recovers and credit conditions improve. Consumer demand growth stabilizes on the back of tax cuts

GDP growth and sub-components

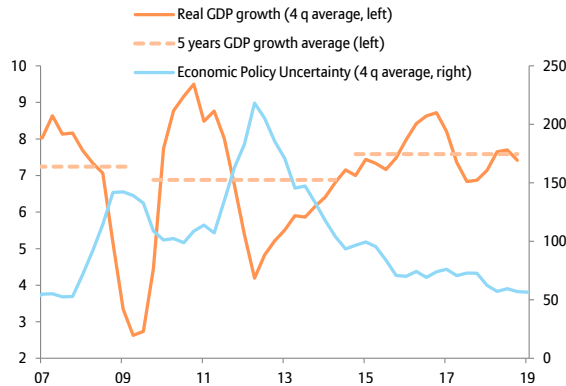


Sources: IHS, Allianz Research

We revised our forecasts by +0.1pp for both 2019 and 2020. We expect a modest acceleration from Q2 onwards. Domestic demand will be main driver

INDIA: POLICIES TO BOOST BUSINESS

Real GDP growth and economic policy uncertainty



Sources: Euler Hermes, Allianz Research

Interest coverage ratio for listed Non-Government Non-Financial Companies

	EBIT/Interest Payment
2018	
Agriculture and Related Activities	5.2
Mining and Quarrying	2.1
Manufacturing	4.7
Chemicals and Chemical Products	9.4
Pharmaceuticals and Medicines	8.1
Computer and Electronic Equipments	4.0
Electrical Machinery and apparatus	3.5
Machinery and Machine Tools	8.1
Motor Vehicles and Other Transport Equipments	10.8
Jewellery and Related Articles	3.0
Medical Precision and Other Scientific Equipments	7.8
Electricity and Gas Supply	1.4
Construction	1.3
Services (Other than IT)	1.1
Wholesale and Retail Trade	2.5
Transport and Storage Services	2.3
Hotel and Restaurant	2.4
Real Estate	1.8
Business Support Services	4.3
Hospital Services	2.8
Video and Television Programming and Broadcasting	14.0
IT, Computer software and related services	72.9
All Companies	3.8
Above all companies average	

Sources: Bloomberg, Euler Hermes, Allianz Research

India infrastructure needs

Figure 4: Infrastructure needs per year until 2022

	Effort per year (USD bn)	Effort per year (% FY2017-18 GDP)
Total	203	7%
Energy	108	4%
Transport	48	2%
Telecom	31	1%
Water	16	1%

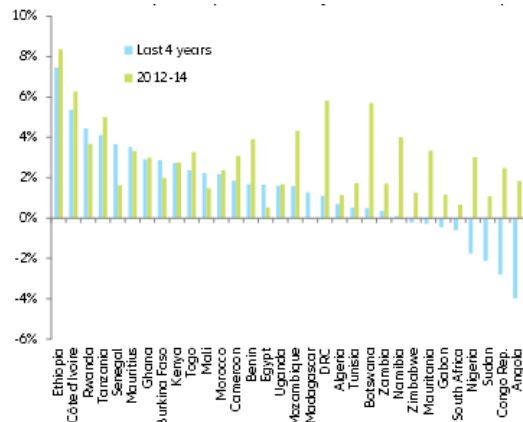
Sources: Euler Hermes, Allianz Research

India = fastest-growing economy among G20 countries in 2018 with +7.4% GDP growth. Active and decisive policy-making has contributed as much as +0.7pp to growth p.a. on average in the last 5 years. But our Now India Index (NII) suggests that growth momentum slowed to +6.2% in Q1 from +6.6% in Q4 2018. There are three things India's next government needs to do to boost business: (1) (Even) more openness to attract capital and support trade - this will help private banks and investors, manufacturing (pharma, motor vehicles) and IT services. (2) Second, a new infrastructure and industrial strategy could help bridge the estimated USD203bn infrastructure gap. (3) Last, social spending and redistribution policies will have to become more cost-effective to address growing inequalities.

AFRICA: CLIFF-HANGERS



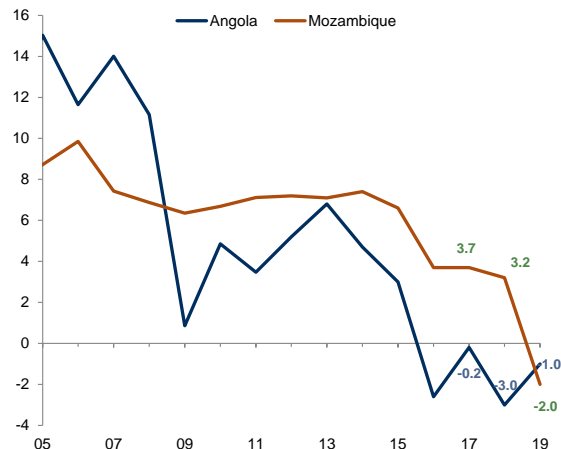
Africa: Growth per capita, last 4 years vs. 2012-14



Sources: IHS Global Insight, Allianz Research

Growth asymmetries observed in the last 4 years should prevail in the next 2 years. From Ethiopia to Morocco, growth has not changed much. Growth accelerations (e.g. Mali and Madagascar) improved the country risk. Income pressures have been deteriorating it (from Cameroon to Angola).

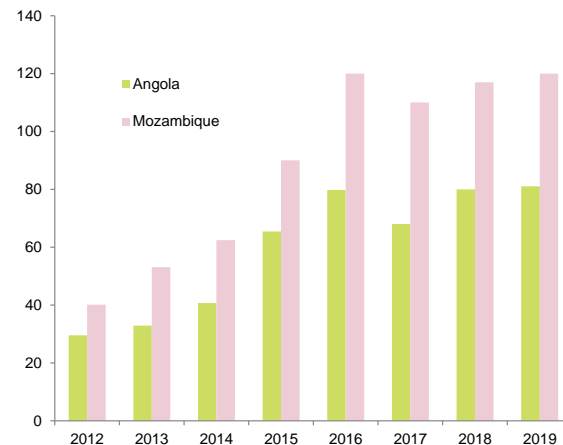
Real GDP growth profiles in %



Sources: IHS Global Insight, Allianz Research

The two countries were hit by the commodity price slump from 2015. The impact was deeper in Angola, since the country should enter into its 4th straight year of recession in 2019. Mozambique to be hit hard by the Cyclone Idai and Kenneth.

Public Debt dynamics in % of GDP



Sources: IHS Global Insight, Allianz Research

Mozambique debt was revised on the upside from 2015, as a result of hidden debt loads that now need to be restructured. Angola also suffered from a steady increase, based on SOEs debt which turned partially into NPLs.

THANK YOU!

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Economist

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