Weekly Export Risk Outlook

EULER HERMES

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In the Headlines

FIGURE OF THE WEEK: 1.2% > BRAZIL'S Q2 REAL GDP QTR/QTR GROWTH

Brazil: Q2 GDP better than expected

Q2 growth of GDP slowed, but nonetheless at 1.2% qtr/qtr sa and 8.9% yr/yr surprised on the upside. Fixed investment continued to grow rapidly, up 2.4% qtr/qtr and a record 26.5% yr/yr. Household consumption growth was solid at 0.8% qtr/qtr and 6.7% yr/yr, as real salaries increased, and government consumption was also up strongly. The net export contribution, however, was negative. While a slower pace of overall growth is likely to continue in H2 and 2011, influenced by tighter monetary policy, fading fiscal stimulus and slower export growth, continued real income growth should support consumption and investment confidence, contributing to domestic demand momentum. Expect GDP growth of 7.5% in 2010 and 4% in 2011.

Romania: IMF agreement

The IMF and the European Commission (EC) reached staff level agreement in August on the fifth review under a 24-month international financial support package, noting they are now satisfied with the government's fiscal reform measures. IMF approval of the previous review had been delayed until July owing to insufficient reform progress. However, the EC's unconnected annual report on Romania criticised lack of progress on judicial reform and corruption, which could result in below-potential EU funding. Meanwhile, the mid-year VAT hike from 19% to 24% pushed July inflation to 7.1% yr/yr (4.4% June). The economy technically left recession in Q2 as real GDP grew 0.3% qtr/qtr sa. On a yr/yr basis, however, GDP continued to contract—by 0.5% after 2.6% in Q1. Expect calendar 2010 GDP to shrink by around 1% with end-year inflation of 7-8%.

Pakistan: IMF provides further support

The IMF's commitment of an emergency USD450mn loan under its Emergency Natural Disaster Assistance (ENDA) facility—additional to an existing programme of around USD11bn—has a significance that exceeds the amount. Firstly, it is quick disbursing and non-conditional, with the amount allocated to Pakistan's budget to support the emergency response. This reflects the scale and seriousness of the floods and associated damage. Secondly, the Fund is reviewing the Stand-By Arrangement, which was first approved in November 2008 and later augmented, with a likelihood of extending it or easing some conditionality—a fifth review is due shortly, with a potential USD1.7bn disbursement. This suggests that the IMF remains committed to Pakistan in the medium- to long-term and also reflects the strategic importance of the country.

Commodities: Inflationary and political risks

Following riots that claimed several lives, Mozambique reversed its decision to increase bread prices by 30%. In turn, this had reflected soaring wheat prices as Russia (formally) and Ukraine and Kazakhstan (informally) imposed restrictions on grain exports following a severe drought. Expect countries, including Egypt, that provide government subsidies on bread to experience strained budgets. Additionally, red meat prices have increased by as much as 33% over the last few months, partly reflecting reduced sheep flocks in Australasia, and this has aggravated inflationary pressures in Muslim countries during Ramadan.

Countries in Focus

Mediterranean countries & Africa – *Zambia: Growth potential*

China is an increasingly important source of loans and investment, partly reflecting Zambia's abundance of natural resources (potential hydro-electricity generation, rich arable land, limestone, gold and cobalt, as well as copper). Annual average real GDP growth was over 5% in 2003-09, boosted by recovery in mining output and as a result of strong FDI flows. Economic indicators in H1 2010 suggest continuing robustness, with mining (10% of GDP), construction and agriculture (maize output at a twenty-year high) as key drivers. Copper prices are expected to remain firm. The business environment is improving, although trading conditions remain hampered by weak infrastructure and power outages that disrupt industrial and commercial output. Expect GDP growth of around 7.5% this year and 6.5% in 2011.

Americas – *Guyana: Commodity based growth*

The commodity based economy—principally gold, sugar and bauxite—has seen growth of real GDP per capita in the past ten years of an annual average 2.4%. Real GDP increased by an estimated 3.3% in 2009 as agricultural output recovered in H2 and gold production remained strong. The fiscal deficit has been halved relative to GDP since 2006, while inflation (annual average) should remain below 4% in 2010. The large current account deficit (11-12% of GDP) is 75-80% covered by net FDI inflows and FX reserves, which have increased steadily, provide 4 months import cover and more than cover external debt payments due. Politics have become less unstable, with the 2006 elections passing off relatively peacefully. The next election is due by August 2011.

Asia-Pacific – *Philippines: Strong performance*

Q2 real GDP grew by a markedly strong 7.9% yr/yr, after an upwardly-revised 7.8% in Q1. On the supply side, industry was the main driver, expanding by almost 16% yr/yr, reflecting rapid construction growth and strong external demand, particularly for electronic and electrical products. Services grew by 6.4%, while agricultural output shrank by 3% owing to drought. On the demand side, growth was relatively broad-based with private consumption up 4.9% yr/yr, government consumption 5.6%, investment 11% and exports 27.4%. Imports increased by 23.9%. Expect domestic demand to remain robust in H2, though external demand is likely to ease, resulting in growth of 6%+ in 2010 overall. Meanwhile, inflation edged up to 4% yr/yr in August from 3.9% in July.

Europe – *Russia: Easing of recovery?*

Q2 real GDP expanded by 5.2% yr/yr, up from 2.9% in Q1, driven by private and government consumption and exports. Industrial production growth accelerated to 10.9% yr/yr in Q2 from 9.5% in Q1, though on a monthly basis it weakened from 12.6% yr/yr in May to 5.9% in July. The decline almost certainly continued in August when a heat wave forced several companies to shut down production. Expect H2 growth overall to weaken as base effects fade, external demand eases and a ban on grain exports remains in place. Despite the export ban, food prices have still risen, pushing inflation to 6.1% yr/yr in August from a record low 5.5% in July. Expect full year GDP growth of around 3.3% in 2010 and end-year inflation of around 8%.

Worth knowing

Ethiopia
The birr was devalued by almost 17% against the USD on 1 September (ETB16.44=USD1 on 3 September).

Iran
Japan followed the US and EU and strengthened unilateral sanctions against Iran, one of its key oil suppliers.

Australia
The Labor Party under PM Julia Gillard gained the partial support of the last two independent MPs, thereby securing a narrow 76-74 parliamentary majority. Expect the legislative process to be challenging.

World Trade
The WTO reported that the value of world merchandise trade increased by 25% yr/yr in H1 2010.