



# Weekly Export Risk Outlook



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## In the Headlines

### FIGURE OF THE WEEK: EUR80BN > GERMANY'S FISCAL CONSOLIDATION

#### ▶ Germany: Austerity package

After two days of intense talks within the ruling centre-right coalition, German Chancellor Angela Merkel announced a large fiscal consolidation plan of more than EUR80 billion. Described as a 'unique effort', the austerity package largely relies on cuts in social welfare and unemployment benefits and reductions in various subsidies and public sector jobs (up to 15,000 losses), but also contains new taxes (e.g. on air travel, the nuclear power industry and the financial sector). The measures will be implemented from 2011 to 2014 with the aim of reducing the fiscal deficit from the 5.5% of GDP expected in 2010 (3.1% 2009) to 3% by 2013. However, further consolidation will probably be needed to meet the terms of the new constitutional law, which limits the budget deficit to 0.35% of GDP beyond 2015.

#### ▶ US: Disappointing employment data

The employment report (May non-farm payrolls) last Friday disappointed as the private sector created only 41,000 jobs, well below what had been expected. (Overall job-creation was 431,000, but this figure included 411,000 temporary jobs at the Census Bureau). However, the good news is that May was still the fifth consecutive month in which the report was positive. Moreover, Fed Chairman Bernanke commented that, while the unemployment rate will remain elevated, he thought the recovery in the US was gaining traction. The jobless rate fell slightly to 9.7% from 9.9% in May.

#### ▶ Hungary: Market turbulence

Comments by two senior party officials of the newly-elected Fidesz government claiming that Hungary faced a Greek-style crisis after the previous governments had allegedly falsified fiscal data sent markets tumbling last week. The forint fell by 4.7% against the euro within two days. The statements were probably aimed at lowering public expectations on election promises (tax cuts), but were ill-timed. Since the weekend, the government has begun damage-limitation with the economy minister affirming the commitment to the 3.8% of GDP fiscal deficit target agreed under the IMF Stand-By Arrangement currently in place. The forint has since recovered by 2.3%. While Hungary's fiscal/debt position, which is under strong scrutiny by the IMF and EU, is concerning, it is not as bad as that of Greece, but, nonetheless, expect markets to remain jittery for some time.

#### ▶ Brazil: Strong Q1 GDP growth

Q1 real GDP growth was a strong 2.7% qtr/qtr (seasonally adjusted), the fourth successive quarter of expansion and the most rapid to date. Driven by domestic demand, on the expenditure side, household spending continued to gain but the biggest increase was in gross fixed investment, while import growth surged outstripping that of exports. On the production side, industry led the way. Q1 growth of real GDP was also a very rapid 9% yr/yr, though from a low Q1 2009 base. The growth rate is likely to slow, but with consensus expectations of growth in calendar 2010 in excess of 6%, expect further interest rate increases (the central bank's monetary policy committee is meeting this week) to head off inflationary pressures.

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► **Mediterranean countries & Africa – *Madagascar: EU aid remains frozen***

Resolution of political differences—a coup in March 2009 was followed by attempts to forge a power-sharing system—remains elusive. This was illustrated in May when there was reportedly a failed armed mutiny by some factions of the police, perhaps reflecting uncertainty in relation to the rival power bases of former-president Marc Ravalomanana and the current leader of the interim government, Andry Rajoelina. The latter continues to govern unilaterally, with apparent disregard for power-sharing considerations. Accordingly, investor and donor communities remain hesitant, with the EU last week deciding to maintain suspension of development aid (approximately USD700mn) for another twelve months.



► **Americas – *Chile: Rebound after earthquake***

Latest data point to the economy bouncing back from the dislocation of the major earthquake in February. The monthly economic activity indicator (IMAECE) in April was up 8.2% mo/mo (seasonally adjusted) driven by increases in retail and wholesale trade output, along with utilities and communications. Manufacturing declined again, though at a more moderate pace. On a yr/yr basis, the indicator was up 4.6% after a 2.9% contraction in March. April's data suggest that the economy is still on course to grow by 4.5% in 2010, though much depends on copper prices, with the global recovery still fragile. Copper accounts for 14% of GDP and 53% of exports. However, the sound policy framework has been maintained by the new government and should continue to underpin overall stability.



► **Asia-Pacific – *Pakistan: Fiscal pledges, but uncertainty***

The federal budget for FY2010/11 (July-June) aims to cut the annual deficit by 1-2pp, to around 4.1% of GDP. This appears challenging, given that much of the reduction is projected to be achieved through increased revenues—rather expenditure savings—and military and other security spending will increase. In addition, increased revenues from the introduction of VAT as a replacement for the current sales tax will not be evident until after October, when the new tax is now scheduled to be introduced, following differences between the federal and provincial governments. Moreover, full implementation of VAT—exemptions have formed political negotiating counters—is not assured. Nevertheless, the current fiscal stance should satisfy the IMF for the time being, although significant political and economic risks could still derail the budget plans.



► **Europe – *Estonia: Euro entry***

This week, the finance ministers of the EU backed Estonia's Euro zone accession on 1 January 2011. As the country had already got the green light from the European Commission and the ECB in May, expect EU heads of state to follow these recommendations at the EU summit later this month. Despite the deep recession in 2009 (GDP shrank 14.1%), the authorities have managed to meet the Maastricht criteria, though the ECB retains concerns about the sustainability of inflation convergence. Inflation was for years the only obstacle to euro entry, but thanks to the recession-related deflation in 2009 the inflation criterion was finally met. Last month, the OECD also acknowledged Estonia's achievements by inviting it to become a full member of the Organisation.

Worth knowing

► **G-20**

The G-20 meeting of finance ministers and central bank heads in South Korea last week-end confirmed that fiscal deficit reduction to lower government debt-GDP ratios has moved to the forefront of the agenda in the wake of the Euro-zone crisis.

► **Philippines**

Q1 real GDP grew 7.3% yr/yr (2.1% Q4 2009) and 3.0% qtr/qtr (seasonally adjusted; 0.9% in Q4). May inflation was 4.3% yr/yr, which is also the average year-to-date. The central bank left its key policy interest rates unchanged last week.

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