



Weekly Export Risk Outlook



EULER HERMES

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In the Headlines

FIGURE OF THE WEEK: **+9%** > S&P 500 IN JULY

▶ Euro-zone: Private sector credit growth

According to ECB preliminary estimates, credit to the private sector posted a third consecutive month of yr/yr increase in June, albeit at a very low level (+0.3% in June and an average +0.2% for Q2), confirming the trend reversal started in April after seven consecutive months of yr/yr decline and fears of a credit crunch. Loans to households again accelerated (to +2.8% yr/yr), but this resulted largely from lending for house purchase (+3.4%)—72% of the total for households—while consumer credit remained negative for the 15th consecutive month (-1.6% yr/yr in June). Loans to non-financial corporations decreased slightly less markedly (to -1.9% yr/yr), but with opposing trends evident in long-term credit (+3.3% yr/yr for over five-year loans) and short-term credit (-10.1% yr/yr for up to one-year credit), with the latter back to Q1 2007 levels.

▶ South Korea: Q2 real GDP growth

Real GDP growth eased slightly to 7.2% yr/yr in Q2 (advance estimate) from 8.1% in Q1, partly as a result of waning base effects. On a qtr/qtr basis, growth moderated to 1.5% in Q2 from 2.1% in Q1. Government spending growth dropped to 0.1% qtr/qtr (down from 5.8% in Q1) as fiscal stimulus has been cut back. Investment increased by just 0.5% (1.5% in Q1) as weakness in house building dragged down construction spending by 3.4%. Growth was mainly driven by private consumption, which expanded by 0.8% (0.7% in Q1) and exports, which grew by 7% (2.9% in Q1). Imports also grew by 7.1% (4.4% in Q1) but the higher level of exports meant that net trade contributed 0.4pps to growth. Overall, growth is likely to slow in H2 as global demand is set to decline—expect about 5.5% in 2010 as a whole.

▶ India: Interest rates and stress testing

The RBI yesterday released its First Quarter Review of Monetary Policy FY2010-11 and increased its two key policy rates—the repo by 25bps to 5.75% and the reverse repo by 50bps to 4.5%, thereby narrowing the differential and indicating a desire to soak up excess liquidity. In a separate statement, the RBI announced that it will conduct twice-yearly stress tests on banks. This is largely a prudential move aimed to instil even more confidence in the financial system, which has proved resilient during the recent heightened global uncertainties. The dominant concern now is inflation, with growth in wholesale prices in double digits since February. Indeed, containing inflation and anchoring inflationary expectations is now the key policy stance. This is understandable, given strong industrial output and overall GDP growth. The RBI is now forecasting GDP expansion of 8.5% in 2010-11, up from its April projection of 8%, and there is an upside bias. Expect further monetary tightening.

▶ US: Financial markets

The S&P 500 gained almost 9% in July, boosted by a combination of good earnings and falling interest rates. Strong earnings have been posted by Fedex, Microsoft, AT&T, DuPont, McDonalds, Ford, Caterpillar and many more. Earnings are expected to be 30+% over last year. Despite this growth, interest rates continue to fall. The yield on the 10-year Treasury note has fallen from 4% in April to 3% currently as the bond market focuses on weak economic news and a Fed tightening, which seems to drift further away every day. Futures markets show only a small chance of the Fed tightening by the end of this year. In the meantime, falling interest rates, plus good earnings, are positive for the stock market.

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► Mediterranean countries & Africa – *Tunisia: Planning*

President Zine al-Abidine Ben Ali last week promulgated into law the country's 12th Five-Year Development Plan (2010-14). Average annual GDP growth of 5.5% is projected over the period—with emphasis on high-knowledge activities within the services sector—even though there are significant uncertainties in key EU export markets. Challenging aspects of the plan include creation of an additional 415,000 jobs by 2014, cutting unemployment to 11.6% from 14.7% and keeping the budget deficit to below 2.7% of GDP. Nevertheless, the IMF recently provided a relatively positive endorsement of economic management, which is expected to remain prudent. Expect comfortable GDP growth of around 4% in 2010 and 2011, but a relatively subdued EU recovery may make the Plan's overall targets challenging.



► Americas – *Peru: Sound recovery*

Real GDP growth is likely to have exceeded 9% yr/yr in Q2 2010, after just 0.9% in 2009 (9.8% 2008). This continues the strong recovery begun in H2 2009, supported by expansionary fiscal and monetary policies—facilitated by previously prudent policies that left debt ratios low—and higher commodity prices. Growth should ease as monetary policy has started to tighten and as the fiscal stimulus fades, but expect 6.7% in 2010 as a whole and 5% in 2011. Inflation is within the 1-3% target range, where it should remain through 2011. The current account balance will be in small deficit in 2010-11 but should be more than covered by FDI inflows. FX reserves cover 13 months of imports and more than 400% of external debt repayments. Presidential elections are due in 2011.



► Asia-Pacific – *Malaysia: Favourable outlook*

Inflation continues to increase gradually, to 1.7% yr/yr in June, up from 1.6% in May and 1.1% at end-2009, although price pressures are likely to remain contained. Nonetheless, the central bank raised its key policy interest rate by 25bps to 2.75% in July, citing continued robust economic activity. The move is also seen as an attempt to bring the policy rate to a neutral range of 3-4%. In May, industry grew 3.3% mo/mo (after a fall in April) and 12.6% yr/yr. In April-May, average monthly industrial output increased by 11.6% yr/yr, slightly up from 11% in Q1, and average monthly merchandise export growth remained strong at 37%, marginally down from 40.5% in Q1. However, as base effects wane and global trade weakens in H2, expect full-year growth to ease to 6-7% from 10.1% yr/yr in Q1.



► Europe – *Poland: Solid growth*

In Q1, real GDP growth slowed to 0.5% qtr/qtr (1.1% in Q4 2009) and 3% yr/yr (3.3% in Q4). A surprising 12.4% yr/yr drop in investment was balanced by accelerating private consumption expansion (2.2%) and strong inventory re-stocking, which contributed 2.1pps to growth. Exports increased by 9.8% while imports shifted back to growth of 7.9% after five quarters of yr/yr decline, resulting in net trade contributing 0.7pps to overall growth. The expansion of industrial output accelerated to 11.7% yr/yr in Q2 from 9.5% in Q1, suggesting that Q2 GDP growth may be somewhat stronger than Q1. Economic activity should lose some momentum in H2 as a result of weakening export demand and subdued overall final domestic demand. Expect around 3% growth in calendar 2010 after 1.8% in 2009.

Worth knowing

► Elections

São Tomé & Príncipe: parliamentary 1 August. **Solomon Islands:** parliamentary 4 August. **Kenya:** referendum on draft constitution 4 August.

► Israel

The Bank of Israel increased its key interest rate by 25bps to 1.75% (26 July, effective 1 August). This reflects concerns relating to inflationary expectations, which are currently at the upper edge of the official 1-3% target range.

► UK

Q2 growth of real GDP was an unexpectedly strong 1.1% qtr/qtr, led by the construction sector.

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