14 November 2012

In the Headlines

FIGURE OF THE WEEK: +2.9% > RUSSIA'S YR/YR Q3 GDP GROWTH

China: Export growth acceleration

October trade data surprised on the upside as export growth accelerated to +11.6% yr/yr, the largest increase in five months and the third consecutive period in which the pace picked up (+9.9% in September). Exports have been helped by demand from emerging economies and from the US, but Europe and Japan are still weak. Import growth remained relatively weak in October, however, at +2.4%, unchanged on the previous month. As a result, the trade surplus increased. The export data support earlier releases on industrial output, retail sales and fixed investment, all of which showed an acceleration for the second successive month. Bank lending was relatively subdued in October and less than expected, but the broader social financing measure continued to accelerate. These signs of improvement lend support to the authorities in their cautious stance towards policy loosening.

Eurozone: Industrial production declines

EZ industrial production (IP) declined by -2.5% mo/mo in September, the largest monthly fall since November 2008, offsetting a large part of the rebound earlier in the quarter. Nonetheless, overall, IP in Q3 ended up with a +0.3% qtr/qtr increase, better than the -0.5% decline in Q2. This implies a possibly less unfavourable Q3 GDP than had been expected, but also suggests, along with business surveys, that a significant contraction in Q4 will be hard to avoid. Meanwhile, the Greek parliament approved the 2013 budget, with the required cuts, but the EZ and IMF are still considering the outstanding disbursement of financial support, although EZ finance ministers seem to agree on a longer-time horizon in which Greece must make necessary fiscal adjustments. To maintain payments Greece is issuing short-dated debt domestically.

Germany: Mostly weak data

In September, new orders received by industry were down significantly, by -3.3% mo/mo after -0.8% in August, with foreign demand particularly weak at -4.5%. These data provide evidence of very weak demand from within the EZ (-9.6%), while orders from outside the zone were also down, but more moderately, at -1.5%. Additionally, industrial production in September decreased sharply, by -2.3% mo/mo after -0.4% in August, with marked falls in textiles (-6.1%), chemicals (-3.6%), computers and electronics (-7.3%) and the car industry (-10.7%). Construction output remained positive, however, with an increase of +2.7%, following a contraction of -2.6% in the previous month. The latest Ifo Business Climate Index reinforced the generally weak tone of recent data, as it declined again in October—for the sixth consecutive month (-1.4% mo/mo).

Russia: Q3 GDP growth and inflation

As expected, real GDP growth slowed further in Q3, to +2.9% yr/yr (flash estimate) from +4% in Q2 and +4.9% in Q1. Drought and wildfires affected the harvest in Q3, while industrial output growth remained weak at +2.5% (+2.3% in Q2). Nominal merchandise exports continued to contract, by -2.1% yr/yr in Q3 (-1.3% in Q2), reflecting the global slowdown, while imports shifted back to moderate growth of +1.4% (-1.4% in Q2). Domestic demand also weakened in Q3 as private consumption was dampened by a rise in regulated prices for utilities and by sharply higher food prices, the latter a result of the poor harvest. Headline inflation accelerated to 6.6% yr/yr in September from an all-time-low of 3.6% in May. Expect full-year growth of around +3.8% in 2012 and +4% in 2013 and annual inflation to stabilise at around 6% in the next few months.

Countries in Focus

Mediterranean, Africa & Middle East – *Mali: Security issues*

At a summit meeting of ECOWAS, regional leaders agreed to deploy 3,300 soldiers to assist the local army retake the north of the country, which is currently under the control of Islamic extremists, including an al-Qaida offshoot. This follows a UN resolution in October that provided a 45-day window for the regional body to devise such a strategy. The UNSC is now likely to approve the plan but armed forces are unlikely to be deployed—if needed—until December or the new year. The militant forces in the north are well armed and entrenched, so expect significant opposition to attempts to unify the country, particularly as some regional states, including Algeria and Mauritania, appear unsupportive of the UN/ECOWAS initiative. Heightened tensions make the business and trading environment even more challenging.

Americas – *Chile: Interest rates and update*

At its latest policy meeting, the central bank again left the key interest rate unchanged at 5%. Headline inflation remains just below the 3% mid-point of the bank's target range (2.9% yr/yr in October). On the real-side of the economy, the monthly indicator of economic activity (a proxy for GDP) was up +1% mo/mo in September, compared with +0.3% in August, the biggest monthly increase this year, which suggests that Q3 real GDP data to be released later this week should show another quarter of solid growth. This inflation/growth nexus points to little immediate pressure to adjust interest rates. Expect growth in 2012 to be around +5%, after a resilient performance in the first nine months, despite lower copper prices, but to slow to +4.3% in 2013.

Asia-Pacific – *Sri Lanka: Budget plan*

The FY2013 budget focuses on economic and fiscal consolidation, investment in infrastructure, liberalisation of the business environment (tax exemptions and increased thresholds) and promotion of the country as a trans-shipment hub. The deficit is projected to be cut to -5.8% of GDP (estimated -6.2% in FY2012) and around 80% of it will be financed through domestic borrowing. Given global uncertainties, Sri Lanka's open economy (imports equivalent to 38% of GDP) and a budget that assumes GDP growth of +7.5%, the deficit appears ambitious. EH expects growth of around 5.5% in calendar 2012 and 2013 and that the central bank will keep interest rates on hold this Friday, as they have been since April after a period of tightening in monetary policy in Q1.

Europe – *Baltics: Surprisingly strong Q3 GDP growth*

In **Estonia**, Q3 real GDP growth accelerated to +3.4% yr/yr (+2.2% in Q2) and +1.7% qtr/qtr sa (+0.5% Q2), mainly driven by domestic demand. Construction, retail trade and other services contributed notably to growth, while the largely export-dependent manufacturing sector declined by -2.4% yr/yr. **Latvia** remains one of the fastest growing economies in the region, with Q3 GDP surging by +5.3% yr/yr (+5.0% in Q2) and +1.7% qtr/qtr sa (+1% in Q2). Strong increases in trade (+7% yr/yr), construction (+8%) and industry (+7%) reflect robust domestic and external demand. In **Lithuania**, strong Q3 GDP growth of +4.4% yr/yr (+2.1% in Q2) and +1.3% qtr/qtr sa (+0.6% in Q2) was also fairly broad-based. Expect full-year 2012 growth of around +3% in Estonia and Lithuania and +5% in Latvia.

Worth knowing

Japan

Q3 GDP contracted by an annualised -3.5% qtr/qtr sa, reflecting a weak domestic economy but also fragile global markets (particularly in Europe and elsewhere in Asia, which are key export destinations) and regional tensions.

Poland

The central bank lowered its key policy interest rate by 25bps to 4.5% last week, as inflation is easing while growth is stuttering. CPI inflation fell to 3.4% yr/yr in October from 3.8% in September and is now within the central bank's 2.5%±1pp target for 2012.

Saudi Arabia

As from 15 November, companies in the private sector that have a labour force with a foreign (non-GCC) majority may be liable to a fine of SAR2,400 (USD640) each year for every "excess" worker. Last year, a quota system was introduced to try and improve employment prospects for Saudi nationals, with variable impact. The new policy, if applied strictly, could affect many companies in a country where an estimated nine out of 10 private sector employees are foreigners.