Weekly Export Risk Outlook

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In the Headlines

FIGURE OF THE WEEK: EUR10BN>FINANCING PACKAGE FOR CYPRUS

Eurozone Debt Crisis: Cyprus bail-out

After an extremely tense period, during which banks in Cyprus were closed, a bail-out package with the Troika was agreed last weekend. Crucially, Laiki Bank (the country's second largest bank) will be split into a 'bad' and a 'good' bank. In the former, 40% of deposits above EUR100,000 will be converted to equity. The latter will be absorbed by Bank of Cyprus (BoC, the largest bank) in which deposits above EUR100,000 will also be subject to a debt swap (sufficient to reach a capital ratio of 9%, but probably at least 30%). The ECB will continue to provide liquidity support. Temporary controls will be placed on bank withdrawals. Another requirement is a reduction in the size of the banking sector to the EU average. Fiscal measures include a higher corporate tax rate and a privatisation programme. The Eurozone and IMF will provide up to EUR10 billion to cover the government's financing needs while maintaining debt sustainability. Following the agreement, the recession is likely to be deeper than expected and there is considerable uncertainty over its duration, particularly in the context of the wide modification of the economic structure as the banking sector contracts and public debt increases. Full implementation of the adjustment programme will also be challenging and will test government resolve, with debt sustainability finely balanced for some time. Banks re-open today, providing the first major test as the authorities try to shore up depositor confidence.

Eurozone: Difficult H1 2013

In March, business confidence (composite PMI) reached a four-month low (-1.7pps to 46.5, compared with a consensus expectation of 48.2) reflecting deteriorating prospects in both the manufacturing and services sectors. In Germany, the fall was more pronounced in services (-3.1pps to 51.6), while the manufacturing index fell below the 'no growth' threshold (-0.9pps to 49.8). The outlook is more worrying in France, with confidence in the services sector reaching a four-year low (41.9) and the index for manufacturing output remaining flat at a very low level (42.8). Overall, despite some recent improvement, current levels of business confidence suggest economic activity will remain weak in the coming months. Against this background and continuing political risk, EH expects a difficult H1 but with gradual signs of stabilisation emerging from early H2 2013.

Germany: Fewer start-ups

In 2012, the number of larger business start-ups—classified by the Federal Statistical Office as having a marked significance for the overall economy—totalled 134,200, down by -7% y/y. The number of new small business start-ups was also down in 2012, by a sharp -17% y/y, at 243,400. In the same period, the rate of establishment of new part-time businesses was stable, with around 241,000 start-ups. In terms of business de-registration, there were mixed results in 2012, with larger business closures up +2.4% y/y at 122,100, while closures of small businesses declined by -3.3% y/y, at 292,100. The number of de-registrations of part-time farms increased by +3.5% y/y at 157,600 in 2012.

BRICS: Summit

This week, leaders from Brazil, Russia, India, China and South Africa met in Durban and a key topic for debate at the BRICS summit was the establishment of a development bank, principally as a conduit for financing infrastructure projects. Details have still to be worked out, not least where the bank will be located, its structure and how (and to what extent) it will be capitalised. The countries also agreed to establish a pool of foreign exchange reserves (potentially USD100bn) to be used in support of a member in financial difficulties. Again, details are limited. Overall, the rather loose grouping is now showing some signs of deepening through mutual support and formal organisation. Expect further progress, but at a measured pace.

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Countries in Focus

Mediterranean, Africa & Middle East – *Oman: Update*

The country is strategically important as it is at the entrance to the Gulf and the international oil and gas waterborne trade routes (hydrocarbons provide 80% of Oman's export revenues). Despite some succession uncertainties, policy continuity has resulted from Sultan Qaboos' lengthy leadership. The business environment is generally sound and above average for the region. Fiscal and current accounts register strong surpluses, 11.4% and 7.7% of GDP in 2012, respectively, and FX reserves provide over five months of import cover. Foreign debt ratios are very low and repayment obligations are comfortable. Government spending, partly to limit potential contagion from the Arab Spring, is a key driver and overall GDP growth is forecast at +5% for 2013 and +4% in 2014.

Americas – *Colombia: Monetary policy and growth*

The central bank lowered the policy interest rate by 50bps last week, to 3.25% from 3.75%. The move reflects the slower pace of economic growth in recent quarters combined with inflation (1.8% y/y in February) below the mid-point of the 2-4% target range and below potential growth concerns, replacing fears of overheating. Although GDP growth has slowed, Q4 2012 data released last week showed a stronger performance than expected, as GDP increased by +3.1% y/y (+2.7% y/y in Q3) and +1.8% q/q (contraction in Q3). Q4 data took full year 2012 GDP growth to +4% (+6.6% in 2011). Expect growth of +3.8% in 2013 and +4% in 2014. If growth slackens there is scope to cut rates further, although credit expansion remains relatively strong, if more subdued than from mid-2011 to mid-2012.

Asia-Pacific – *Vietnam: Monetary policy*

Headline inflation fell by 0.2% mo/mo in March and eased to 6.6% y/y from an average 7% in January-February and an average 9.1% in 2012. The improvement in March—which was mainly driven by declining food prices and transport costs—gave the central bank confidence to lower its key policy interest rate (the refinancing rate) by 100bps, to 8% on 26 March. This was the first rate cut in 2013 following a cumulative 600bps reduction in 2012. Policymakers are eager to support the economy, which grew by +5% in 2012 (which was a 13-year low), but the scope for further interest rate cuts in 2013 is probably limited, perhaps to another 100bps, as inflationary pressures remain evident. Shocks to food prices and exchange rate volatility are key upside risks to inflation.

Europe – *Croatia: 2012 fourth year without growth*

Revised estimates from the Bureau of Statistics confirm that real GDP contracted by -2.3% y/y in Q4, marking the fifth consecutive quarter of decline. Full year 2012 GDP contracted by -2% and, after also declining in 2009-10 and stagnating in 2011, is now -11% down from the peak in 2008. Domestic demand was particularly weak in 2012, with private consumption decreasing by -3%, government consumption by -1.2% and fixed investment by -4.6%. Weak domestic demand also affected imports, which declined by -2.1% in 2012. Exports managed to grow, but only marginally at +0.4%, so that external demand mitigated the overall fall in GDP. EU economic weakness, tight monetary policy and fiscal austerity will continue to dent growth prospects. Expect 2013 to be another year without growth (stagnation at best).

Worth knowing

Other GDP

UK: -0.3% q/q and +0.2% y/y in Q4 2012 (third estimate) and +0.3% in 2012 overall. **France:** -0.3% q/q in Q4 2012 (second estimate). **Mozambique**: +8.3% y/y in Q4 2012 and +7.4% in 2012 overall.

Central African Republic

Rebels from the Séléka coalition (three distinct groups that unified in opposition to the regime) mounted a coup against the government of François Bozizé and took control of the capital, Bangui, on 24 March. Bozizé fled the country and a rebel leader, Michel Djotodia, declared himself president and suspended parliament and the constitution. While elections have been promised, the stability of the Séléka coalition is yet to be tested and national security remains tenuous.

Lebanon

The government of PM Najib Mikati resigned (22 March) but Mikati is willing to head a new government of national salvation.