Economic Update Emerging Markets

5 February 2013

Emerging Markets – A mild recovery at best

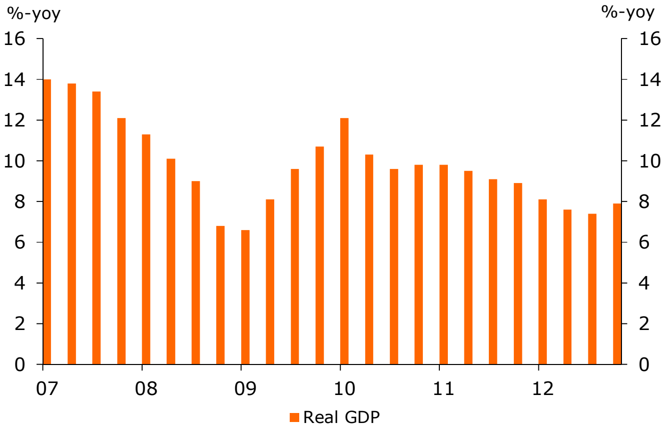
Real GDP growth

	'11	'12	'13
World	3.9	3.2	3.5
US	1.8	2.3	2.0
Euro area	1.4	-0.4	-0.2
CEE	5.3	1.8	2.4
CIS	4.9	3.6	3.8
Developing Asia	8.0	6.6	7.1
China	9.3	7.8	8.2
Latin America	4.5	3.0	3.6
MENA	3.5	5.2	3.4
SSA	5.3	4.8	5.8

Source: IMF WEO update

In some emerging markets, economic growth has started to pick up in the fourth quarter of last year. January's purchasing managers indices suggest that many others are following suit in January. However, this is not the case for all emerging markets. Especially those that heavily depend on demand from the eurozone continue to struggle. In all emerging markets, however, even in those that have started to recover, economic policies remain mainly focused on supporting growth. Understandable, as a recovery this year will be mild at best. Thus, although 2013 should be a better year than 2012, growth will remain relatively weak and below the long-term trend.

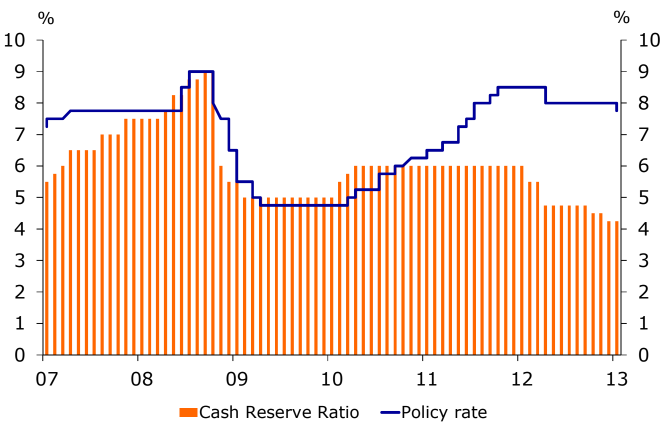
China – Growth recovering, but relatively weak



Source: Reuters EcoWin

In the last quarter of 2012, the Chinese economy grew by 7.9% yoy, up from 7.4% in the third quarter. It is the first time since 1Q11 that growth accelerated. Economic stimulus from the government and a slightly improved external environment helped to push up growth in the final months of the year. Helped by a relatively strong fourth quarter, full year growth came in at 7.8% in 2012. On the one hand, China has thus successfully circumnavigated a hard landing in 2012. However, last year's growth rate is also the slowest since 1999. At around 8%, next year's growth outlook is only slightly better. Moreover, risks are skewed to the downside while upside potential is limited.

India – Monetary boost



Source: Bloomberg, Reuters EcoWin

On 29 January, the Reserve Bank of India (RBI) cut its policy rate and the cash reserve ratio by 25bps to 7.75% and 4.0%, respectively. The RBI cited receding inflationary pressures, weaker economic growth and tight liquidity conditions as reasons. Also, the government's decision to phase out retail diesel price regulation helped. Although this will raise inflationary pressures in the short-term, the resulting reduced fiscal spending will lower inflationary pressures in the long-run. RBI's growth projections were lowered to 5.5% for the current fiscal year, which is substantially lower than the 6.5% expected in July 2012. While the pass-through mechanisms are far from perfect in India, the economy can use the monetary boost.

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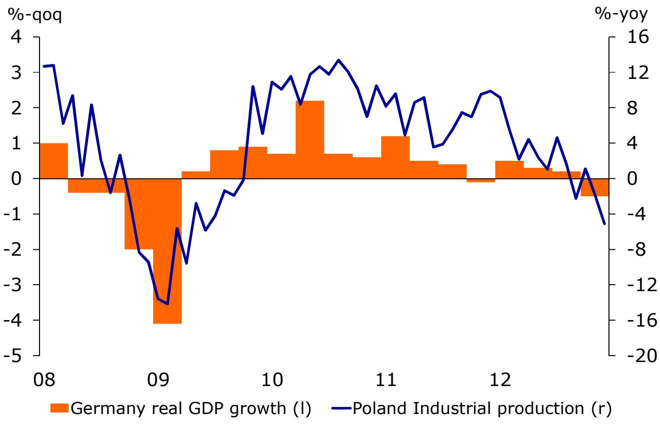
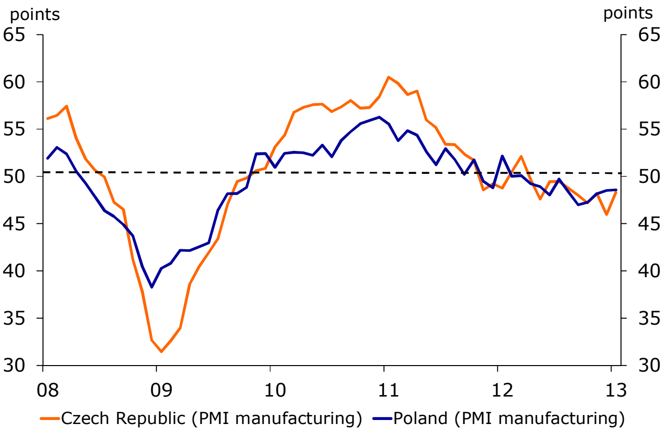
Poland – Heading for a recession?



Source: Reuters EcoWin, Eurostat

Concerns are rising that Poland might be heading for its first recession in two decades, as December 2012's industrial production (IP) figures came in far weaker than expected. Adjusted for seasonal effects, IP fell by 5.1% yoy, following a 1.8% yoy contraction in November. The strong decline seems to reflect both weak domestic demand and Germany's Q4 GDP contraction. The production of cars, electronics and furniture, usually major export drivers, fell strongly, as did construction output. As unemployment rose accordingly, growth in Q4 was likely very weak at best. While this should increase the likelihood of additional interest rate cuts, a recession may not be averted.

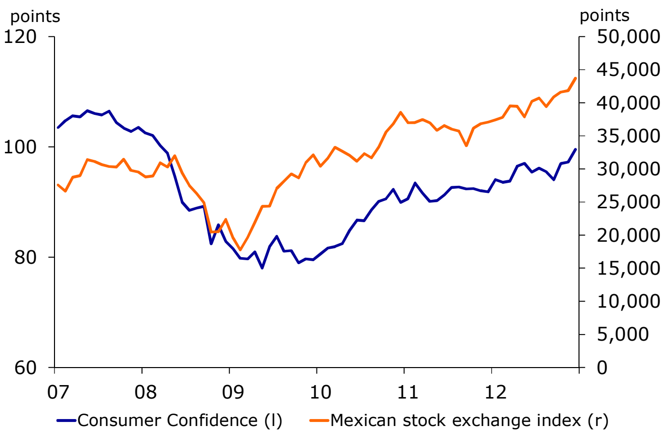
Emerging Europe – Little reason for optimism



Source: Reuters EcoWin

The newly released PMI's for Emerging Europe signal that Santa did not bring the hoped recovery. For most countries in the region, the PMI's stayed below the level of 50 points, which indicates falling production. Even though the Czech Republic's PMI increased from 46 to 48 points, Poland's PMI stagnated at 48 points. Unfortunately, the news was not much better for the rest of Emerging Europe. Underlying these numbers is a familiar story: the region's openness to and dependence on the eurozone makes it vulnerable to the zone's debt crisis. The only exception is Turkey, where the PMI reached its highest point in 14 months. Still, overall, there is little reason for optimism.

Mexico – A good start of the year



Source: Bloomberg, Reuters EcoWin

Mexico started the new year on a rather positive note, as consumer confidence climbed to a 5-year high, while the purchasing manager's index (PMI) and the stock market index even reached all-time-highs. Following the passage of labor and education reforms by the new President Enrique Peña Nieto, consumer confidence increased to 99 points in December. Reflecting the strongest increase in new orders since the index began, the PMI rose from 55.6 to 57.1 points last month, indicating strong expansion of production. While the avoidance of the US fiscal cliff should help to maintain the positive momentum, ongoing commitment to structural reforms is needed to prolong this trend.

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