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An update of country and industry risks and opportunities

Portugal, Turkey, Russia, China, Mexico

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Portugal: A drama waiting in the wings?

Portugal's preliminary GDP estimate for H1 of 2011 showed 1.5% year-on-year contraction, due mainly to decreased fixed investment and household consumption, especially of durable goods. That said, exports grew strongly. Remarkably, the unemployment rate has not deteriorated and, seasonably unadjusted, actually improved 0.3% - although, at 12.1%, the level remains uncomfortably high. Insolvencies increased sharply between 2008 and 2010, and we expect business failures to increase further: by 10% year-on-year in 2011 and another 5% next year.

Atradius assessment:

There is no doubt that Portugal faces tough times ahead. The €78 billion EU/IMF bail out programme will dominate the scene from now till 2015. The programme aims at healthy government finance in combination with long-term growth, through a mix of strict fiscal consolidation and far-reaching structural reforms to address structural weaknesses, e.g. tax rises for both firms and consumers; cuts in the bill for public wages, public employment and pensions, lower subsidies and privatisation of state-owned enterprises. GDP should be given a boost by the downsizing of the government, expedited privatisation and labour market reforms. If it goes according to plan, the deficit will stand at 3% of GDP in 2013. GDP will however only gradually recover: shrinking over 2011-2013 with a return to weak growth in 2014.

But it is questionable whether this will work out. On the positive side, the coalition of the Social Democratic Party and Popular Party that won June's elections is expected to remain in power over the coming years, as the defeated Socialist party is weak. And, more importantly, the coalition has committed itself to executing the IMF programme - even striving for faster fiscal consolidation than that required. But, badly needed as this is, this zeal will not be enough. The execution of the austerity and reform programme has only just begun and will heavily burden a society already faced with a 12% unemployment rate. Moreover, exports will be under pressure if the recessionary tendency that is gradually manifesting itself in Portugal's main markets continues.

The near future looks bleak and it is up to the politicians to sell this to the electorate – in order to avoid an Iberian variant of the Greek drama currently being played out.

Russia: The Putin enigma

In a US-style congress of the United Russia party, prime minister Vladimir Putin accepted the 'invitation' from the current president Dmitry Medvedev to be the party's candidate in the March 2012 presidential elections. Meanwhile, Aleksei Kudrin, the long serving finance minister, announced that he would resign if Medvedev became the new prime minister - and was summarily dismissed by Medvedev.

Atradius' assessment

The announcement of the (almost certain) return of Putin to the presidency did not escape cynical comments, including those from oligarch Mikhail Prohkorov that Russia was becoming a 'farce and parody' of the Soviet Union. That may be an exaggeration: not least because the move is clearly politically stabilizing, and could speed up much needed reform of Russia's structurally weak economy, which thrives on oil and gas and is effectively run by state-owned monopolies or state-loyal companies operating in an opaque legal system. At present, the unreliable business climate is discouraging foreign investors and, even worse, Russia faces huge capital flows. The economic policy badly need an overhaul and it is not inconceivable that Mr Putin has concluded the current tandem is not suitable to this end. The manner of Kudrin's departure may bode ill for Medvedev. Kudrin is a personal friend of Putin and highly respected in financial circles, and would be missed if reform is to be taken seriously. After the elections, we may therefore hear little from Medvedev – and see the return of Kudrin.

Turkey: Beware of economic overheating and political overconfidence

The Turkish economy has recovered remarkably since 2009. Real GDP grew 9% last year, followed by 11% in Q1 and 8.8% in Q2 of 2011, driven by public sector spending ahead of the June general elections, and a liquidity boost from bank credit growth and foreign capital inflows. In fact, those inflows became so strong that the Central Bank had to lower the official interest rate, but the effect has been to fuel economic growth even more rather than to dampen domestic spending.

Atradius assessment

Despite a generally positive view on Turkey, we see two impending risks. One is that the parliamentary strength of Prime Minister Erdogan, confirmed in the June 2011 general elections allows, for a more assertive foreign policy, especially in the Middle East. Relations with Israel have deteriorated rapidly, and could even lead to an military conflict, while tensions on the Cyprus issue have increased. The second risk is that of further economic overheating, with imports increasing much faster than exports. The massive current account deficit (forecast to rise to 10% of GDP this year) and the recent depreciation of the Turkish lira could well lead to domestic economic growth going out of control. As much of the current account deficit is financed from volatile short-term investment, any shake-up of financial markets may trigger a massive withdrawal. Turkey is noted for 'boom and bust' so care must be taken in assessing business opportunities there.

China: Still has an ace up its sleeve

Inflation remains stubbornly high: 6.2% in August after 6.5% in July. Food prices are still the main source (+13.4%), with meat again a main contributor (+29.3%). Although inflation is expected to moderate in the coming months, it will exceed the 4% target rate: so the Central Bank is reluctant to ease monetary policy. However, interest rate increases are not yet expected, as economic growth slows and uncertainties over the global economy increase. In Q2 of 2011, economic growth was 9.5% year-on-year: marginally down on Q1. A further slowdown is expected, due to lower export demand and decreased investments due to recent monetary tightening.

Atradius assessment

In contrast to the public debt burdens in Europe and the US, China has an abundant cushion against external or internal shock. Its external finances are excellent, with large international reserves, and low public and external debt. During 2008/2009, China handled the crisis situation well, with a massive stimulus package. However, its property market and overinvestment may pose internal economic risks. The government also has contingent liabilities in the finances of local governments and the banking sector, and the plentiful lending of recent years may lead to deteriorating assets and higher non-performing loans. China can still cope with another crisis, but its future actions may aggravate its internal imbalances, reflected in low household consumption and a high savings rate.

Mexico: Better than its violent reputation

News about Mexico is often focused only on dreadful images of assassinations by drug gangs: 2010 was the bloodiest year ever and 2011 will probably be even worse. While, of course, such violence tarnishes Mexico's reputation as country to trade with or invest in, Mexico also presents many business opportunities.

Atradius assessment

After the 2009 recession, Mexican exports increased by 24% in 2010, contributing to a rebound of 5.5% in real GDP growth. This year, we expect some moderation in performance because of Mexico's ties with the struggling US economy. Nevertheless, inflation is under control, macroeconomic management is fine and the external financial position is strong.

Mexico's international payments position is excellent: foreign debt is low (less than 20% of GDP) and, even with short-term commitments, Mexico is able to honour its payment obligations. It has ample foreign reserves at its disposal and the IMF has granted a precautionary credit line of US$ 72 billion until April 2013, to be used in case of emergency and to stave off any capital flight out of the country.

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