Global issues

**Slowing world trade dispels hopes for export-led recovery**

Growth of world trade has slowed significantly during the year as a consequence of stalling economic activity in developed countries, especially in Europe. After growing by 5 per cent in 2011, the world trade volume expanded by an annualized rate of only 1.2 percent in the second quarter of 2012.

Most European economies have entered into recession. While around 70 per cent of European trade is intra-European, the sharp reduction in import demand is also affecting other economies. The value of imports from extra-European trade partners has been declining steadily since March 2012 and dropped by more than 10 per cent year on year in July. Furthermore, Japan and the Republic of Korea as well as several emerging economies including Brazil, Singapore and Taiwan, recorded a decline in the value of their imports and exports in August from a year ago. China’s exports still showed a slight increase, but import demand fell. As grim perspectives for the global economy persist, the World Trade Organization (WTO) further downgraded its forecast for world trade growth to 2.5 per cent for the year 2012 as a whole, down from 3.7 per cent and less than half the long-term average.

**Wide variety of economic issues discussed in the UN General Debate**

At the sixty-seventh session of the United Nations General Assembly, a wide variety of economic issues were discussed in the speeches presented as part of the General Debate. While the continuing effects of the financial crisis did not dominate as in previous years, concerns about the lingering effects and the lack of coherent reform of the international financial system were presented by many countries. Brazil and Argentina expressed concerns about the effects of developed country policies on the economies of developing countries. Among developing countries, the Millennium Development Goals (MDGs) was a common subject, both in discussing important achievements made and in lamenting the remaining gaps. Calls for further cooperation to achieve the MDGs as well as working toward more sustainable development in general were expressed by a number of CIS, Eastern European, East and South Asian countries as well as South Africa and other countries in East Africa. Concerns about the impact of climate change—already felt, in particular, in countries relying on agriculture and in those exposed to natural hazards and rising seawater levels, such as small island nations—led to urgent calls to push ahead with the implementation of the sustainable development agenda articulated at the Rio+20 conference in June of this year.

**Figure 1: Merchandise exports and imports**

<table>
<thead>
<tr>
<th>Year-on-year percentage change in current dollar values</th>
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<tbody>
<tr>
<td>European Union (extra trade)</td>
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<td>China</td>
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<td>Japan</td>
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<td>Brazil</td>
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Sources: Japan: Ministry of Finance; China: General Administration of Customs; European Union: Eurostat; Brazil: Banco Central do Brazil; DESA.
Developed economies

United States: unemployment rate falls, but output growth remains subdued

The unemployment rate in the United States fell to 7.8 per cent in September, the lowest in five years, although still much higher than the pre-crisis level of 4.6 per cent. The number of workers in payroll employment increased by 114,000 during the month. The increase is too weak for a full recovery to pre-crisis employment levels any time soon, taking into account the growth of the labour force. Even so, consumer confidence improved slightly in September.

The United States Bureau of Economic Analysis revised its earlier second quarter estimate of GDP growth downward from 1.7 per cent to 1.3 per cent. Economic output data for more recent months indicate that growth has remained anaemic in the third quarter, further increasing the likelihood that the United States economy will expand by less than 2 per cent for the year 2012 as a whole.

Developed Asia and the Pacific: monetary policy actions under dire circumstances

On 19 September, the Bank of Japan announced its decision to expand the scale of its Asset Purchase Program from ¥70 trillion to ¥80 trillion. The increase will be used to purchase treasury discount bills and Japanese government bonds. The timeframe for implementation of the programme has been extended from mid-2013 to the end of 2013. The Bank of Japan expects the measure will help further push down long-term interest rates and risk premiums. The recent short-term economic survey of enterprise (Tankan) compiled by the Bank of Japan showed that the situation for the manufacturing industry was still dire during the third quarter and has only partially recovered from the impact of the natural disasters in 2011.

Though GDP growth in Australia remained solid during the first half of 2012, there are more and more signs that a slowdown is setting in. Employment declined by 27,000 between May and August; while recent data on retail sales, home loan commitments and business confidence all showed downward trends. Weakening export prices have caused a deterioration in the trade balance and could lead to further postponement of new investments in the natural resource sector. On 2 October, the Reserve Bank of Australia announced it would cut its policy rate (the cash rate) by 25 basis points to 3.25 per cent.

Western Europe: tensions building, yet again

With the announcement of its Outright Monetary Transactions (OMT) programme, the ECB has committed to purchase debt securities on the secondary market without time limits or quantity restrictions, but with the proviso that countries enter a rescue programme. Initially, financial market tensions eased notably in the first half of September following the announcement. However, as has been the case with all of the previous policy announcements, this has proved short-lived. The reluctance of countries to apply for rescue programs, increasing social pressures across the region, confusion about how to interpret the plan regarding bank bailouts and the speed at which a unified banking supervisory body is to be established, as well as continuing bad news on the economic front were all factors contributing to renewed financial market uncertainty.

The latest round of economic indicators for the region continue to point to a decline in output in the third quarter of 2012, which would mark two consecutive quarters of negative growth and thus a recession, and show no evidence of better prospects in the fourth quarter. The European Commission’s Economic Sentiment Indicator continued its downward trend since February. The Markit Eurozone Composite Output Index, while dropping only marginally, remained well below the neutral mark of 50.0 (indicating a decline in activity) for the eighth successive month, and registered a particularly sharp drop in France.

Unemployment for the euro area remained stable for the third month in a row, but at 11.4 per cent, a record level for the region and up 1.2 percentage points relative to a year ago. Unemployment rates remain very high and are still increasing in the crisis countries. Unemployment affected 25.1 per cent in Spain in August 2012 (up from 22 per cent a year ago), 15 per cent in Ireland (from 14.7 per cent), 15.9 per cent in Portugal (from 12.7 per cent), and in Greece was 24.4 per cent in June (up from 17.2 per cent a year ago). A particular concern is that youth unemployment is much higher than the average.

New EU members: attempts to utilize monetary policy despite inflation

Further weakening in external and domestic demand is acting as a drag on economic recovery in Central Europe. In Poland, industrial production remained virtually flat in August, growing by 0.5 per cent year on year. Slowing output will make it harder to meet budget deficit targets. In early October, Poland sold $2.26 billion worth of 12-year bonds to help to finance the deficit, benefiting from low yields. Although headline inflation in the country remains above the central bank’s target range, core inflation is falling. In the Czech Republic, manufacturing output declined sharply and consumer confidence hit its lowest point in 12 years in September. Performance of the automotive industry was weaker than anticipated in the first eight months of 2012. In Hungary, by contrast, export-oriented manufacturing activity improved during September.
Although in the Czech Republic headline inflation exceeded the central bank’s target range in August, the Czech National Bank in September reduced its already low benchmark rate to 0.25 per cent, which 0.5 points below the ECB’s rate. In a similar move, the Hungarian National Bank cut its policy rate by another 25 basis points in late September, even though consumer prices increased by an annualized rate of 6 per cent in August.

Meanwhile, Romania’s economy exited recession in the second quarter, when seasonally adjusted GDP grew by 0.5 per cent quarter on quarter.

**Economies in Transition**

**CIS and Georgia: Russian Federation tightens monetary policy amid inflation concerns**

In August, there were signs of weakening domestic demand in the Russian Federation. Higher food prices affected food sales, and industrial output grew by only 2.1 per cent year on year while construction stagnated. As corporate profitability declined due to rising costs, investment grew by only 2.3 per cent in August. However, manufacturing sentiment apparently improved in September, with stronger PMI indices for output and new orders. Price pressures also intensified in September, with inflation above 6 per cent. In response, the central bank raised its key interest rates by 25 basis points in September, despite strong objections from the corporate sector. In Ukraine, industrial output declined by 4.7 per cent year on year in August, and export-oriented industries suffered serious setbacks in sales. Drought continues to affect agricultural output in the CIS. In Kazakhstan, by mid-September only 8.7 million tonnes of grain had been harvested, leading the Government to project a total harvest of about 13 million tonnes for 2012, which is less than half the 26.9 million tonnes harvested in 2011.

**South-Eastern Europe: Bosnia and Herzegovina receives new funding from the IMF**

In Croatia, industrial production grew by 2.1 per cent in August year on year. Output of consumer and capital goods increased, perhaps owing to a successful tourist season. However, mining and quarrying fell by 21 per cent as the sector’s demand was undermined by stagnating construction. Stronger tourism receipts helped to narrow the current account deficit. Between January and August, tourist arrivals in Montenegro were up by 4.1 per cent compared with the same period a year ago. In the former Yugoslav Republic of Macedonia industrial production plunged by 8.1 per cent year on year in August. The contraction was across the board. The country’s second quarter GDP shrunk by 0.9 per cent year on year.

The earlier estimate for Serbia’s second quarter GDP was revised downward. GDP declined by 0.8 per cent year on year, as manufacturing experienced a serious drop and the trade balance deteriorated. The Government announced additional measures to reduce the budget deficit, including increases in the VAT rate, excise duties, and taxes on dividends and interest income from October.

In September, the Executive Board of the IMF approved a new stand-by loan for Bosnia and Herzegovina worth $520.6 million. The previous IMF program for the country was suspended.

**Developing economies**

**Africa: Zambia successfully issues a Eurobond loan**

South Africa’s current account deficit reached 6.4 per cent of GDP in the second quarter, up from 4.9 per cent in the first quarter and the highest level in four years. While weaker exports in light of slowing global demand were the main driver in this respect, the recent labour conflict in the mining sector may further hurt export performance and push the external balance further into deficit in the third quarter.

Zambia issued a $750 million, 10-year Eurobond loan at a yield of 5.625 per cent, which is less than the current yield for comparative bonds of some of the economies in the euro zone. The bond was almost 16 times oversubscribed, making it the most successful bond launch in sub-Saharan Africa. The underlying factors include Zambia’s role as Africa’s biggest copper producer and ample liquidity in developed economies.

Fuel costs are weighing on a number of countries. Both Tunisia and Egypt are implementing plans to cut fuel subsidies and reform the subsidy system in order to lower budget deficits. Government deficits of the two countries currently stand at 6.6 per cent and 11 per cent of GDP, respectively. Regulators in Kenya raised the prices of diesel, petrol and kerosene. In the first half of 2012, Tanzania’s current account deficit widened by 7.3 per cent of GDP caused by a rising oil import bill.

Rwanda’s economy grew by 9.4 per cent in the year through June. Industrial production was up 12 per cent, the services sector expanded by 12 per cent, and the farming sector grew by 6 per cent.
East Asia: manufacturing and trade data indicate ongoing weakness

East Asia’s economies continue to face headwinds from weak demand in Europe and slower growth in China. The latest figures on manufacturing activity and trade indicate ongoing weakness in the region, especially in the strongly export-oriented economies. In the Republic of Korea, industrial production contracted by 1.7 per cent month on month in August. This decline reflects sluggish exports and a sharp drop in automobile production caused by a prolonged labour strike at Hyundai-Kia, the country’s biggest auto group. In Thailand, industrial production declined by 2.6 per cent in August month on month and by 11.3 per cent from a year ago, mainly owing to a slump in the electronics sector. Thailand’s merchandise exports to the EU dropped by 22.8 per cent year on year in August and exports to China declined by 12.9 per cent. In China, the Purchasing Manager’s Index improved slightly in September, but continued to signal a contraction of manufacturing activity.

Economic growth in Viet Nam picked up from 4.7 per cent in the second quarter to 5.4 per cent in the third, following five interest rate cuts in the first half of 2012. However, after falling to a multi-year low of 5 per cent in August, year-on-year inflation accelerated to 6.5 per cent in September, sparking renewed fears over the country’s outlook.

South Asia: India's Government enacts significant reforms

India’s Government announced a series of significant economic reforms aimed at reducing the fiscal deficit and promoting economic growth. The authorities increased the heavily subsidized diesel price by about 12 per cent and restricted purchases of subsidized cooking gas cylinders. In addition, the Government decided to open up the country’s retail and aviation sectors by allowing 51 per cent foreign investment in multi-brand supermarkets and department stores and 49 per cent foreign investment in Indian local airlines. The measures have triggered massive protests from opposition parties and trade unions, which organized a day-long nationwide strike against the reforms.

The sanctions by the EU and the United States have triggered a severe currency crisis in the Islamic Republic of Iran. On the black market, the rial lost more than 40 per cent against the dollar between September 24 and October 2. The end of EU purchases of Iranian oil in July has led to a marked decline in export revenues; moreover, the US sanctions against financial institutions that deal with the Central Bank of the Islamic Republic of Iran has cut the country off from foreign exchange. With the central bank unable to support the value of the rial and inflation accelerating to 23.5 per cent in August, demand for foreign exchange is rising rapidly, pushing down the rial.

In Sri Lanka, GDP growth decelerated to 6.4 per cent year on year in the second quarter of 2012, the lowest pace since late 2009. The slowdown reflects weak exports and less buoyant domestic demand following monetary policy tightening.

Western Asia: weakening exports, except for oil and gold

Despite Saudi Arabia’s decision to provide world markets with extra oil supplies, oil prices remain elevated, with Brent averaging $113 per barrel in September. In Kuwait, oil exports representing more than 90 per cent of government revenues contributed to the highest budget surplus on record, allowing the Government to increase the share of state revenues allocated to future generations from 10 to 25 per cent.

High oil prices and weakening global import demand are exerting pressure on current account balances of oil-importing countries. In Israel, the trade deficit widened in August on the back of declining exports of low-, medium- and high-tech goods. Turkey’s apparently robust export performance continued unabated, with goods exports between January and August rising by 12.8 per cent year on year. This trend is being supported by an increase in gold exports, which accounted for 18 per cent of total exports in August, most of it going to embargo-hit Iran. Excluding gold, however, exports only rose by 3 per cent during that period, and declined by 4 per cent year on year during the month of August. Facing weakening domestic and external demand, the Turkish central bank lowered the upper limit of its overnight lending rate from 11.5 per cent to 10 per cent.

Latin America and the Caribbean: weakening growth perspectives but inflation and unemployment remain low

The global economic situation is affecting Latin America’s growth mainly through the export channel, particularly in the Southern cone. Brazil’s exports fell by 14 per cent in August year on year. During the January-August period, exports had fallen 4 per cent compared with the same period in the previous year. In Argentina, the export volume recorded in August 2012 was down by 6 per cent from a year ago. Exports during January-August had declined by 1 per cent compared with the same period in 2011. Exports to the EU suffered most. The export decline has become reason for increasing concern, the more so because policymakers fear that the additional quantitative easing measures in developed countries could lead to appreciation of their exchange rates.

Inflation and unemployment rates remained low in August. In Bolivia, consumer prices increased by 0.4 per cent (4.4 per cent year on year); in Chile by 0.2 per cent (2.6 per cent year on year); and in Mexico by 0.3 per cent (4.6 per cent year on year). Brazil’s unemployment rate dropped to 5.3 per cent in August, down by 0.7 percentage points from a year ago. In Mexico, the unemployment rate also declined to 5.3 per cent from 5.8 per cent a year ago.