Global issues

**BRICS anti-crisis facility**

During the G20 summit, the countries of the BRICS group (Brazil, the Russian Federation, India, China and South Africa) agreed to establish a contingent reserve arrangement by pooling resources in a $100 billion fund. China will contribute $41 billion, South Africa will contribute $5 billion, and the three other members will provide $18 billion each. This is a precautionary facility to help shield these emerging economies from stock market and exchange-rate volatility as the advanced economies withdraw their unconventional monetary stimulus.

**G20 concludes meeting in St. Petersburg**

The leaders of the G20 countries committed to pursuing policies to promote strong, sustainable and balanced growth and jobs. The G20 members agreed to a Medium Term Fiscal Action Plan, which aims to: ensure a clear and calibrated monetary stance going forward; pursue both supply and demand measures to promote jobs; introduce initiatives to promote long-term financing for investment; promote international cooperation to combat cross-border tax evasion and profit-shifting; and strengthen financial regulatory frameworks. The G20 Leaders’ Declaration, agreed at the St. Petersburg Summit on 5-6 September 2013, explicitly commits to support processes led by the United Nations for accelerating MDGs and Post-2015 endeavours to promote the sustainable development agenda, with emphasis on reaching agreements on concise and measurable goals that are universally applicable, and supporting it with the sustainable financing strategy. The Declaration further welcomes the Secretary-General’s initiative of a Summit on climate change in 2014 and plans to support the United Nations Framework Convention on Climate Change process and other initiatives in this area, and the Green Climate Fund. Additionally, the G20 will continue to emphasize improvements in food security, financial inclusion, infrastructure development, human resource development and domestic resource mobilization.

**Emerging markets increase debt sales**

Economic conditions in emerging markets continue to be unstable with continued capital flow and exchange-rate volatility (see Monthly Briefing No. 56, 9 July 2013, on volatility resulting from the United States Federal Reserve (Fed) announcement on tapering quantitative easing). In addition to recent measures to deal with these uncertain conditions, a number of emerging market economies and institutions issued debt recently in order to lock in low rates ahead of the scheduled meeting of the Fed in mid-September (see Monthly Briefing No. 57, 14 August 2013, on policy initiatives to deal with slowing growth in emerging economies). An expected announcement about the prospects for a tapering of the Fed’s quantitative easing program at that meeting was anticipated to drive borrowing costs higher. Despite the previous outflows, there was still considerable demand for a $7 billion offering by Russia and a $2 billion offering by South Africa, though both countries had to pay higher rates than they had in the past 12 months. Indonesia, Mozambique and the Korea Development Bank are also among those selling debt recently.

**Developed economies**

**The United States: still growing, but slowly**

The labour market in the United States continues its slow recovery. In August, payroll employment increased by 169,000, compared with an average monthly gain of 184,000 in the past 12 months, although the gains for the previous two months have been revised downward by a total of 74,000. The most recent report showed job growth in retail trade and health care, but employment in information technology declined. The unemployment rate declined to 7.3 per cent from 7.4 per cent in July, but this change was mainly caused by the 0.2 percentage point decline in the labour force participation rate, which is now at the lowest level since 1978. The decline in the participation ratio was a result of many factors, including the effect of an aging population and increased school enrollment. However,
there are also a large number of discouraged workers; this is seen in the declining participation rate for the prime age cohort of 25-54, which is down by 0.4 percentage points from a year ago.

The revised estimate for the real gross domestic product (GDP) of the United States shows an annualized growth of 2.5 per cent for the second quarter of 2013, much stronger than the advanced estimate, reflecting a rebound of private fixed capital formation, an increase in net exports, and a deceleration in the reduction of national defense expenditure. At the same time, the latest business surveys point to continued improvement in the economy. However, after the Fed decided to continue its quantitative easing program at the same rate, uncertainties still loom about the timing of an expected tapering of the program. In addition, Congress has yet to make a decision on the debt ceiling, which could provoke further market instability.

**Japan: recovery may slow down**

The second estimate for the real GDP of Japan shows an annualized growth rate of 3.8 per cent in the second quarter of 2013, a jump from the 2.6 per cent reported in the first estimate. The upward revision was mainly attributed to faster growth in private and public investment, and slower de-stocking of inventory. The growth rates for both private and public consumption were slightly lower than in the original estimate. The GDP growth rate for the first quarter was also revised up from 3.8 per cent to 4.1 per cent.

On the other hand, the available statistics for the third quarter point to a reduced pace of expansion. While industrial production recovered from the drop in June and resumed the level it had reached in May, the tertiary sector index fell 0.4 per cent in July. Export volume dropped significantly, by almost 5 per cent from June to July, leaving it at about 4 per cent lower than one year ago. Progress in the labour market is also not solid. Although the unemployment rate declined from 3.9 per cent in June to 3.8 per cent in July, the main cause was the reduced labour supply. The employment level actually has not increased in the last three months. In July, the regular wage rate maintained the declining trend of the past two years.

**Western Europe: Western Europe exits recession**

After six consecutive quarters of declining GDP, the euro area finally exited recession in the second quarter of 2013, with GDP growing by 0.3 per cent quarter over quarter. There were particularly sharp rebounds in Germany (0.7 per cent), France (0.5 per cent) and the United Kingdom of Great Britain and Northern Ireland (0.6 per cent). Italy, the Netherlands and Spain continued to contract but at a diminishing pace, with rates of growth of -0.2, -0.2, and -0.1 per cent, respectively. Growth was led by net exports, contributing 0.2 per cent, with private and public consumption contributing 0.1 per cent, while inventories detracted 0.1 per cent. Investment made no contribution.

Survey data continued to improve, consistent with positive but subdued growth going forward. In August, the European Commission’s Economic Sentiment Indicator (ESI) increased sharply in both the European Union and the euro area for the fourth successive month in both regions, and now lie close to their long-term averages. The Markit Eurozone Composite Output Index continued to increase, with the second consecutive month above 50—the point that demarks expansion from contraction. Manufacturing has been leading the upturn, but the service sector has now also turned the corner.

Unemployment remained stable at 12.1 per cent in the euro area where it has been since April. In Ireland, Italy, Portugal and Spain, unemployment rates have either stabilized or have begun to come down, albeit from highly elevated levels.

**New EU members: green shoots tentatively emerge in Central Europe**

Following mixed second quarter performance of the economies of the new European Union (EU) member States, the forward-looking indicators for July and August (such as purchasing manager’s indices based on the new industrial orders) hint at a slightly improved outlook for the second half of the year, especially in the Czech Republic, Hungary and Poland. Growth of GDP in Poland in the second quarter was stronger than anticipated, at 1.1 per cent year on year, and the economy appears to have retained the momentum. Although the expansion in the second quarter was mainly due to net exports, indicators such as strong retail sales in July point to recovering domestic demand, with nominal wage growth outpacing inflation. Consequently, the National Bank of Poland is likely to abandon its easing cycle. By contrast, the Hungarian National Bank and the National Bank of Romania cut their main policy rates in August by 20 and 50 basis points, respectively.

Some countries in the region saw positive trends in their labour markets during the summer months, which may reflect seasonal factors, such as a pick-up in construction and tourism. In Poland, the unemployment rate fell to 13.1 per cent in July from 13.2 per cent in June. However, in the Baltic States, and especially in Lithuania, the declining unemployment rate is partially explained by contraction in the labour force due to negative net migration.
Economies in transition

**CIS: Kazakhstan adopts new currency peg structure**

The economy of the Russian Federation, following its weak performance in the second quarter (growth was revised downward to 1.2 per cent year on year from the 1.9 per cent announced earlier), remains sluggish. However, domestic demand apparently strengthened in August. Inflation in August remained at the same level of 6.5 per cent registered in July. Elsewhere in the CIS, inflation remained high in Armenia in August, at 9.3 per cent, reflecting the effect of the earlier increase in the price of Russian natural gas. In response, the Central Bank of Armenia increased its policy rate in August by 50 basis points. In neighbouring Georgia, by contrast, consumer prices declined in August by 0.4 per cent year on year.

While the country is operating a managed float regime, in September the National Bank of Kazakhstan announced its decision to peg the currency to a basket of foreign currencies, replacing the earlier peg to the dollar (although the dollar will still form 70 per cent of the peg), in order to reduce exchange-rate volatility.

In Ukraine, agricultural output was strong in June and July, and industrial production may have bottomed out. Private consumption remained strong with retail sales growing by 11 per cent in the second quarter. The National Bank of Ukraine cut its policy rate in August.

In September, Armenia expressed its intention to join the Customs Union of the Russian Federation, Belarus and Kazakhstan and to participate later in the formation of the Eurasian Economic Union. Consequently, the country is unlikely to conclude the free trade agreement it had envisaged and negotiated earlier with the EU, owing to the different tariff structure between the two blocks.

**South-Eastern Europe: Serbia’s growth continues to be driven by exports**

In Serbia, real GDP increased by 0.7 per cent year on year in the second quarter, bringing the total growth for the first half of the year to 1.4 per cent. Growth was mostly driven by net exports, especially from the automotive industry, while domestic demand remains subdued. In the former Yugoslav Republic of Macedonia, meanwhile, industrial output strengthened in summer, growing by 3.9 per cent year on year in July. In Bosnia and Herzegovina, industrial output trends in summer diverged between the different parts of the Federation.

**Developing economies**

**Africa: Libyan oil output continues to fall**

Oil production and exports have continued to decline in Libya as a result of ongoing protests (see World Economic Situation and Prospects Weekly Highlight, 21 August). Output at the beginning of September was down to a low of around 150,000 barrels per day (bpd) compared to an estimated capacity of 1.6 million bpd and there were only 80,000 bpd in exports. The cost has been estimated at $130 million per day in lost revenue.

GDP growth was up slightly in South Africa to 2.0 per cent year on year for the second quarter, driven higher by growth in the manufacturing sector, but held back by contraction in the economically significant mining sector. The current-account deficit was down slightly from 6.7 per cent in the first quarter to 6.5 per cent in the second quarter. Exports increased by 10.8 per cent compared to the previous quarter, also driven by the depreciation of the rand, while imports were up by 6.3 per cent. In Mozambique, interest rates were cut by 25 basis points to 8.75 per cent in light of easing inflation. Similarly, the Bank of Botswana reduced its policy interest rate by 50 basis points to 8 per cent, also underpinned by lower inflation as well as slowing growth.

The Liberian Senate passed a new minimum wage law that establishes a threshold of US $6 per day as a minimum for an unskilled worker.

**East Asia: regional growth slows; capital outflows exert downward pressure on currencies**

Macroeconomic conditions in East Asia have become more challenging amid slowing regional growth and continuing capital outflows. Several regional currencies depreciated considerably against the dollar in August as fears of an upcoming tapering of the Fed’s bond-buying program prompted investors to pull out of emerging market debt and equity funds. The Indonesian Rupiah weakened by more than 8.0 per cent against the dollar amid concerns over slower domestic growth, rising inflation and a widening current account deficit to 4.4 per cent of GDP in the second quarter of 2013. In response, the Government and central bank announced a set of measures aimed at relieving pressure on the current account and the rupiah. This includes tax incentives for exporting firms, removal of export quotas on certain goods and initiatives to increase the supply of foreign currency.
Thailand’s economy entered into a technical recession in the second quarter of 2013 owing to weakness in household consumption, private investment and exports. Seasonally adjusted output contracted by 0.3 per cent from the previous three months, following a decline by 1.7 per cent in the first quarter. On a year-on-year basis, growth slowed to 2.8 per cent. In Malaysia, GDP expanded by 4.3 per cent year on year in the second quarter, slightly slower than expected. Domestic demand continued to be buoyant, partially offsetting the continuing weakness in exports.

In contrast, growth in the Philippines remained very robust, with GDP expanding by 7.5 per cent year on year in the second quarter. Higher public and household spending helped the economy defy the regional slowdown.

**South Asia: growth slows in India**

India’s economic difficulties worsened in August, with the rupee falling sharply to a record low against the dollar. Expectations of an upcoming tapering of the Fed’s bond-buying program, combined with concerns over India’s sluggish growth, high inflation and large current-account deficit, triggered further significant capital outflows. As a result, the rupee lost more than 10 per cent against the dollar in August alone. A combination of inflationary and liquidity problems resulted in the Reserve Bank of India (RBI) resorting to a rise in the policy rate (the rate at which it lends to commercial banks) by 25 basis points (bps) to 7.5 per cent while also reducing the rate for the marginal standing facility (a window for banks to borrow from the RBI in an emergency situation) by 75 bps to 9.5 per cent. A continued focus on lowering inflation to support economic growth and on stabilizing the currency may demand a second round of adjustments on these fronts.

Recently released macroeconomic data signal ongoing weaknesses. Growth slowed to a 4-year low from 4.8 per cent in the first quarter of 2013 to 4.4 per cent in the second quarter as investment activity remained sluggish. Consumer price inflation continued to be close to 10 per cent in July 2013. Some rays of hope appeared in recent trends in trade as the Government’s measures to curb gold imports seemed to yield results. Gold imports were down sharply in June/July, compared to the previous two months. In July, total merchandise imports were 6.2 per cent lower than a year ago, while exports grew by 11.6 per cent.

**Western Asia: Turkey’s unorthodox policy approach to currency depreciation**

Turkey is facing a confluence of headwinds as the Turkish lira has depreciated by 17 per cent against the dollar since May 2013, the benchmark Istanbul stock index has declined by about 30 per cent from its record high, and domestic bond yields have surged. All this occurred amid a new wave of financial turbulence in emerging market economies as the announcement by the Fed about the possibility of tapering its quantitative easing program triggered a reversal of foreign capital inflows to these economies. The Turkish economy had robust growth for the past decade and weathered the global financial crisis of 2008. However, its current account has registered a large deficit, partly financed by short-term foreign debt, with the ratio of short-term foreign debt to GDP the highest among the large emerging market economies, making Turkey more vulnerable than others to the reversal of capital inflows.

More interestingly, unlike other emerging market economies, such as Brazil and India, which have followed the orthodox policy of raising interest rates to fight against currency depreciation, the Central Bank of Turkey has adopted an unorthodox policy scheme by creating an interest rate corridor between 6.75 per cent and 7.75 per cent without increasing the policy interest rate. Comparing these two different policies, the former runs a risk of choking the real economy by raising interest rates while the latter carries a risk of higher inflation driven by currency depreciation.

**Latin America and the Caribbean: increasing risks despite recent positive economic figures**

The Brazilian economy posted surprisingly faster GDP growth in the second quarter of 2013 (3.3 per cent, year on year) supported by higher investment and a robust agricultural sector. Similarly, Venezuela registered higher GDP growth for the second quarter (2.6 per cent year on year) following positive trends in the manufacturing and oil sectors. Conversely, recent data for Mexico shows that economic growth slowed in the second quarter of 2013, contracting 0.7 per cent quarter on quarter. In Chile, exports have picked up in July by 9.2 per cent year on year. Despite positive signs in some of these economies, the environment for capital flows continues to deteriorate and uncertainties regarding the second half of the year are mounting. Stock markets in the region are underperforming as other emerging markets and local currencies continue to depreciate against the dollar. The Brazilian real for instance has lost close to 11 per cent of its value against the dollar over the past three months. This depreciation has prompted the Brazilian Government to cut import tariffs on many products in order to avoid inflationary pressures and minimize a potential economic slowdown in the short term, although it could ease also competitiveness pressures in the medium term.