Lasting crisis casts doubts on muted-recovery scenario for 2012

Analysis by credit insurer Euler Hermes

- **Euler Hermes lowers its forecasts for world growth to 3% in 2011 and 3.2% in 2012.**
- **The large emerging economies will continue to shore up world growth.**
- **In Europe, the banking crisis linked to the sovereign debt situation erodes growth prospects.**
- **The slow down in corporate insolvencies is likely to come to a halt in 2012.**

Paris, October 20, 2011 – In a turbulent economic environment, Euler Hermes is forecasting a slowdown in world growth over the next 18 months. The credit insurer has revised downwards its June forecast. It is now forecasting growth of 3% in 2011 (0.3% lower than its June forecast) and of 3.2% in 2012, down by 0.4%), following growth of 4.3% in 2010. Growth in world trade will drop back to around 7% in 2011 and 2012 compared with 14% during the 2010 recovery.

The recovery is running out of steam in the euro zone and the United States. GDP[1] growth is expected to stand at 1.6% in 2011 both in the euro zone and the United States. In 2012, growth is forecast at 1.3% for the euro zone and 2.0% for the United States. The emerging economies will enjoy stronger growth in 2012, with 4% in Latin America, 3.5% in Central Europe and 7.1% in Asia excluding Japan.

Among the countries ‘driving’ world growth, India and China stand out in particular with growth forecast at 8.5% in 2012. Growth in Brazil is expected to reach 3.5% in 2011 and 3.7% in 2012. However, for the emerging countries as a whole, which currently account for 38% of world GDP, growth is slowing (under 6% in 2011 versus 7% in 2010).

In Europe, however, some advance indicators seem vulnerable to hesitation on the decisions that should be taken to deal with a double crisis, that of the banks and of sovereign debt. This increases the likelihood of a worse scenario for 2012

Change in trend in corporate insolvencies

“Prospects of a slowdown in world GDP growth will have a negative impact on several growth drivers. Households may reduce their consumption of durable goods, while companies may cut back on investment and trim their budgets,” explains **Wilfried Verstraete**, Chairman of Euler Hermes’ Group Management Board. “In the present highly uncertain business climate, we can also expect to see a less positive trend in corporate insolvencies. Although these were still declining until very recently, the downward trend has now come to a halt,” he added. In 2010, the number of corporate insolvencies dropped by 5% worldwide, particularly in Asia and North America. Even though most of the major economies are resisting well, this positive tendency is slowing in Europe and insolvencies continue to increase in the more vulnerable European countries (Greece, Ireland, Italy, Portugal and Spain).

Structural differences and different economic conditions from one region to another

There are still fears of a double-dip in the **United States**. Despite some reassuring news, such as robust corporate earnings, the downward trend in corporate insolvencies and growth in bank lending, GDP growth remained low, at 1.3%, in the second quarter, with consumption remaining virtually flat at 0.1%. Other indicators such as the housing market, manufacturing output and employment also point to a fragile situation. “Media hype abounds: Stimulus plans? Austerity plans? But what is urgent now is to decide measures to protect growth and employment over the short term”, says Euler Hermes Chief Economist, **Ludovic Subran**.

Recovery has slowed dangerously in the **euro zone,** with domestic demand contracting for the first time since 2009. “The overall momentum is disappointing to the say the least. Even the major euro

[1] GDP: Gross Domestic Product

zone countries have recorded a sharp slowdown with a sudden halt in Germany and France and very weak growth in Italy and Spain," says Ludovic Subran. The slowdown in activity is likely to be confirmed in the second half, with growth of only 0.1% compared with 1.0% in the first half. According to Ludovic Subran, "the real risk is that of an even greater deterioration if solutions to provide support to the countries and financial institutions currently in difficulty are not decided immediately. It is essential to prevent any risk of contagion to the entire euro zone, and possibly beyond it."

The 'Arab Spring' has brought about major changes in the **Middle East and North Africa**, and its impact on the growth outlook will continue to be felt throughout 2012. Euler Hermes is forecasting growth of 2.9% in 2011 and 3.9% in 2012, with significant downside risk. The political transition is still fragile in Egypt and Tunisia, and the Libyan, Syrian and Yemenite economies are expected to contract this year.

GDP growth slowed in **Central and Eastern Europe and Russia** in the second quarter – down to 4.4% versus 5.4% in the first quarter - due to a dip in its main growth drivers: external demand and investment. Growth is expected to come in at 4% in 2011 and 3.5% in 2012. Turkey again recorded the strongest growth in the region in the second quarter, adding to the fears of overheating.

Growth is also forecast to slow in **Latin America**, dropping to 4% in 2011 and 3.7% in 2012, compared with 6.1% in 2010. Brazil, Mexico, Chile, Columbia and Peru are the countries in the best position to cope with the uncertainties linked to a global economic downturn, even though they are not completely safe from a negative growth shock, linked in particular to second round effects of the expected fall in commodities prices.

In **Sub-Saharan Africa,** GDP is expected to grow by 5.2% in 2011 and 4.9% in 2012. This is a significant improvement on the low point reached in 2009. However, there is still possible downside if world demand, particularly for commodities, declines.

Overall, **South, Central and East Asian** economies remain well equipped to cope with the uncertain global outlook**.** Growth is forecast to slow to 7.3% in 2011 and 7% in 2012. Growth decelerated in most ASEAN[2] countries in the second quarter, due to supply chain problems linked to the events that occurred in Japan in March. In contrast, the slight slowdown in the Chinese economy is due to monetary tightening. Nonetheless, together with India, where consumption remains strong, China continues to be one of the main drivers of world growth.

Country risk[3] increased in six countries and declined in three other countries between June and September

According to Euler Hermes' calculations, country risk increased in four countries due to greater exposure to economic risk: Turkey (up from 'sensitive' in June 2011 to 'high' in September 2011), Cyprus went from 'low' to 'sensitive' over the same period while risk rose from 'low' to 'medium' for Costa Rica and Trinidad and Tobago. Risk increased in two other countries due to their dependence on external financing, particularly Italy with an increase from 'low' to 'sensitive' and Croatia, up from 'medium' to 'sensitive'.

In contrast, risk decreased for three other countries. In Japan (down from 'sensitive' to 'low') and Slovenia ('medium' to 'low'), economic conditions improved for the short term, whereas Azerbaijan benefited from an improving structural situation (down from 'high' to 'sensitive').

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[2] ASEAN: Association of South East Asian Nations
[3] Euler Hermes distinguishes four levels of country risk: low, medium, sensitive, high.

Appendix: Euler Hermes Growth Forecast

GDP Evolution	2011	2012
World	3.0%	3.2%
Regions		
Euro Zone	1.6%	1.3%
Central and Eastern Europe	4.0%	3.5%
North America	1.6%	2.0%
Middle East & Africa	3.6%	4.5%
Asia (excluding Japan)	7.3%	7.1%
OECD	1.3%	1.8%
non OECD	5.8%	5.6%
Countries		
Austria	3.2%	1.8%
Belgium	2.6%	1.7%
Brazil	3.5%	3.7%
Canada	2.2%	2.3%
China	9.0%	8.5%
Denmark	1.2%	1.4%
Finland	3.4%	1.7%
France	1.6%	1.3%
Germany	2.9%	1.6%
Greece	-4.7%	-0.8%
India	8.0%	8.5%
Ireland	1.5%	1.7%
Italy	0.7%	0.6%
Japan	-0.8%	2.5%
Netherlands	1.8%	1.3%
Norway	1.2%	1.9%
Portugal	2.0%	-1.4%
Russia	3.7%	3.6%
Spain	0.7%	1.0%
Sweden	4.3%	1.8%
Switzerland	2.0%	1.5%
United Kingdom	1.0%	1.4%
United States	1.6%	2.0%

Sources : IHS Global Insight, Euler Hermes forecasts

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