Trading Globally: Opportunities & Risks

Global Trade Flows (Exports and Imports)—Insights

• Global trade volumes are estimated to have grown by 5.0% in 2011, with the robust expansion in Q1 undermined by a number of shocks later in the year.

• Asia and the US took the lead in export growth while Europe and Africa were respectively affected by the sovereign debt crisis and the interruption of oil supply from Libya (which led to an 8% contraction in African exports).

• The economic slowdown in H1 2012, geopolitical factors and recent natural disasters are liable to soften global export and import growth in coming quarters.

• Exporters need to monitor country-specific political, economic and commercial risks.

• High trade opportunities, low macroeconomic volatility: Canada, China, India, UAE, UK.

• Low trade opportunities, high macroeconomic volatility: Afghanistan, Ecuador, Hungary, Syria, Yemen.

Recent Developments: Global Trade Slowed in 2011

Preliminary data for global exports and imports suggest that world trade volumes grew by 5.0% year on year (y/y) in 2011, significantly below the exceptional 13.8% recorded in 2010 as the global economy rebounded from 2008/09 contraction. The 5.0% growth seen in 2012 is also lower than the long-term average of 6.0% for 1990-2008. Trade's healthy growth in Q1 2011 ground to a halt after a number of negative shocks hit the global economy, slowing it down. First, the ongoing sovereign debt crisis in the euro area (which in 2011 accounted for more than 21% of world imports) significantly curtailed import demand in the region. Second, the earthquake and tsunami in Japan, as well as the floods in Thailand, disrupted supply chains, curtailing exports from east Asia in particular. Third, the conflict in Libya caused the interruption of oil and gas supplies from the country, leading to an 8% contraction in African exports.

Emerging markets (and Asia-Pacific economies in particular) were the main drivers of global trade growth in 2011, mainly due to relatively robust economic growth and weaker currencies. In nominal terms, average imports in Asia-Pacific economies grew by 23% in 2011, compared with only 18% in the advanced economies. In terms of the share of global imports, Europe heads the list with 38.1% of the total, followed by Asia-Pacific economies (30.9%) and North America (17.2%).
Outlook: Global Trade Growth to Moderate Further in 2012

Although global trade seems to have regained momentum in Q1 2012, led by developing countries, but with high-income countries still lagging, the risk of a slowdown in economic growth over the year is liable to slow the growth (in volume terms) of global exports and imports. The economic slowdown will be exacerbated by the overhang from recent geopolitical factors (mainly the political turmoil of the ‘Arab Spring’ and the conflict in Libya) and natural disasters (the tsunami in Japan and flooding in Thailand).

However, downside risks remain elevated. We are primarily concerned about the emerging economies, which drove the recovery of the global economy after the 2008–09 contraction. China’s property market is deflating and steel makers suffered financial losses in Q1 2012; imports to China grew by just 7.1% y/y in Q1. Meanwhile, Brazil’s real GDP growth in Q1 slowed to 1.4% y/y as the stronger Real drew in imports and reduced the competitiveness of exports. Brazil’s cumulative 1.5-percentage point policy rate cut since March, and China’s widening of its daily exchange rate band against the US dollar to 1% in April, indicate policy makers are fearful of a sharper slowdown despite continuing inflationary pressures. Meanwhile, poor fiscal governance and inadequate reforms will hold growth in India below 7%.

The other major issue is the failure to resolve the sovereign debt crisis in Europe. In particular, the euro debt crisis threatens to lead to a Europe-wide financial crisis that could derail the economic recovery and trigger a devastating contagion to EU banks, with knock-on effects on trade finance availability and growth prospects. In this context we are wary that an economic slowdown or a negative shock could threaten the rebound in global trading in the coming quarters.
Global Trade Flows, 2001 to 2011

Imports
In 2011, euro-area countries and the US continued to be the main importers by size (in US dollar terms), despite fast growth rates recorded in China, India and other emerging markets over the past ten years. The euro area was the largest importer in the world in the last decade (with more than USD4.5trn of total imports), followed by the US with USD2.3trn. Another mature economy, Japan, which was the third-biggest importer in 2000, fell to fourth position in 2011. China, with imports worth USD1.7trn, has overtaken both Japan and Canada (in 2011, Canada fell to seventh position, behind South Korea and Hong Kong with USD521bn and USD501bn, respectively).

These developments were the result of China’s exceptional economic performance: between 2001 and 2011 China’s imports grew by 59% per year on average, compared with more modest rates of 14% in both the euro zone and Japan, 9% in the US and 14% in Canada. Likewise, in the same period other emerging markets also recorded extremely high import growth rates: India’s imports rose by an average of 77% per year, South Korea’s by 26% and Singapore’s by 21%, thus expanding their import markets considerably.
Exports

Looking at exports by size (in US dollar terms) also shows the growing role played by emerging economies in this respect. According to D&B estimates, up until Q4 2011 the euro area was still the biggest exporter in the world, with USD4.5tn, followed by China with USD1.9tn and the US in third position with USD1.5tn; this is a significant change from 2001, when the US was still the second-biggest exporter in the world and China was only fourth, behind Japan but ahead of Canada (which are now fourth and seventh, with USD819bn and USD452bn, respectively).

Indeed, from 2001 to Q4 2011 China’s exports grew at a much higher pace (62% annual average) than the euro zone’s (13%), the US’ (10%), Japan’s (10%) and Canada’s (7%). A similar performance was also recorded in other emerging economies, such as South Korea, Russia (which is now the sixth-largest major exporter in the world, owing mostly to its considerable hydrocarbon exports) and Mexico.
Trading Globally: Opportunities and Risks

Over the next two years the continued expansion in global trade flows will offer increasing opportunities to exporters, particularly in emerging markets. That said, country-specific political, economic and commercial risks will continue to warrant caution and careful monitoring. A group of eight countries (in the top-left cell of the matrix below) will guarantee the best import opportunities (in US dollar terms) and the lowest degree of macroeconomic volatility for foreign companies. These countries include: major developed countries (such as Canada and the UK) that have benefited from relatively high growth rates and low exchange rate volatility in the past and are likely to post positive (albeit modest) growth in the next two years; fast-growing emerging markets such as China, India and Indonesia, with high import potential and a comparatively solid macroeconomic environment; and smaller (but stable and expanding) economies such as the UAE and Saudi Arabia.

A second set of seven countries consists of economies featuring medium trade opportunities and low macroeconomic volatility (the centre-left cell). These countries comprise: small, mature economies (such as Denmark and Norway) that enjoy solid macroeconomic and commercial fundamentals; and minor and relatively economically stable developing countries, such as Kuwait. Compared with these economies, Brazil, Japan, the US and Taiwan will offer better trade opportunities to foreign exporters, but also a higher degree of macroeconomic volatility; these markets belong to a group of 12 countries (top-centre cell in the matrix), mostly large, fast-growing markets from the Asia-Pacific region, with the mature US and Japanese markets as outliers.

In sharp contrast with these groups, a set of 18 high-risk and low-opportunity countries (at the bottom-right of the matrix) consists of mostly frontier markets and EU economies hard-hit by the latest global downturn. These include small, politically unstable countries (e.g. Afghanistan, Yemen and Zimbabwe) and European economies still reeling from the effects of the 2008-09 financial crisis (such as Hungary, and Estonia). A small group of five equally risky but higher-growth countries (centre-right cell) includes politically unstable and economically volatile countries, such as Belarus, whereas a bigger cluster of 52 economies (bottom-centre cell) offers a medium macro-economic volatile environment with low import opportunities; this latter group contains a wide range of small emerging markets, mostly from the Africa, Latin America and Asia-Pacific regions but also mature European markets such as Austria, Germany and Italy.
The D&B Import Opportunities and Economic Volatility Index shows trade opportunities (vertical axis) and the degree of macroeconomic volatility (horizontal axis) for foreign companies in 132 countries. Import Opportunities are measured by the forecast size of imports (in US dollar terms) for each country over the next two years; and Macroeconomic Volatility is an indicator derived from past exchange rates (40% of the indicator’s weighting), real GDP growth volatility (40%) and D&B’s country risk ratings (20%).
**United States**

**Opportunities:**
- While still fragile, the economy has gathered pace since late 2011, helping to lift demand for imports.
- By March 2012, the manufacturing sector had grown for 32 consecutive months and order books implied continued expansion.
- According to the World Bank’s latest Doing Business report, it takes substantially less time to trade with the US than with the OECD on average, although costs and documentation requirements are similar.

**Risks:**
- Demand for consumer goods will remain under pressure, with the labour market still fragile and household incomes eroded by inflation; this will weigh on key sectors such as automotive, manufacturing, transportation and retail.
- The ongoing slump in the housing market reduces demand from the construction sector.
- Delinquency rates and bankruptcy filings will remain elevated compared to the mid-2000s.
- Partisan politicking and political uncertainty ahead of the 2012 elections is likely to undermine business and consumer confidence, muting import demand.

**United Kingdom**

**Opportunities:**
- The UK’s ranking in the category ‘trading across borders’ in the World Bank’s Doing Business report for 2012 improved to 13 (from 15 in the 2011 report), with documentation requirements, time involved and costs below the OECD average.
- The government’s policy aimed at decreasing corporate taxation (from 26% to 25% starting from April 2012, with the intention of lowering it to 23% by 2014/15) encourages private sector investment.
- Some prospects exist in export-led companies, especially whose trading with developing countries that are experiencing growth.

**Risks:**
- Current UK fiscal policy aims to boost exports and investment rather than consumer and public demand, thus decreasing import demand from the public and consumer sectors.
- The labour market outlook is bleak given looming cuts in public sector jobs: high unemployment will continue to suppress consumer demand.
- The weak pound sterling and high input prices (e.g. energy) raise costs for UK importers and threaten to undermine demand for imports.
Russia

Opportunities:
• Russia’s ranking in the category ‘trading across borders’ in the World Bank’s 2012 Doing Business report improved to 160 (from 166 in the 2011 report).
• The strong real appreciation of the rouble over 2011 and into 2012 will support import demand.
• The growing middle class in Russia perceives foreign brands as higher quality and increasingly prefer shopping and travelling abroad.
• WTO accession (expected in mid-2012) will provide opportunities for importers due to lower tariffs and reduced entry barriers for the Russian market, especially in manufactures, machinery and transport equipment, and automotive products.

Risks:
• Despite ongoing fiscal stimulus measures and the windfall from high oil prices, modest growth is expected in 2012, indicating suppressed domestic demand and thus weaker import demand.
• High inflation, which softened before presidential elections in March 2012, is likely to pick up and put pressure on domestic demand and jeopardise returns on trade and investment.
• In spite of improvements in the World Bank’s Doing Business report for 2012 Russia still suffers from poor logistics (in particular within customs operations), inefficient public institutions and corruption.

China

Opportunities:
• China’s inland provinces continue to undergo rapid urbanisation, led by resource-intensive investment.
• Middle-class segments of the population are growing, creating new sources of disposable income and bringing novel, expanded consumption patterns.
• The working age population is due to reach an historic maximum in the mid-2010s.
• Government revenues have grown rapidly and fiscal pressures are largely absent.

Risks:
• A number of sectors slowed markedly in late 2011, including construction, real estate sales, some manufacturing, automobile sales and steelmaking.
• The financial sector has substantial opacity, with the shadow banking sector of informal lenders having contracted sharply in 2011, reducing firms’ liquidity.
• Local government debt spiked in 2009–10; while not large enough to cause systemic financial woes, it would add to problems in the event of a ‘hard landing’.
• Inflation and an overextended luxury real estate sector limit options for policy loosening.
• Water stress is a negative factor: the south-to-north water transfer megaproject is much needed.
South Korea

Opportunities:
• Exports to the US rose a rapid 27.9% year on year (y/y) in March after the implementation of the US-Korea free-trade agreement.
• According to a survey by the Korea Chamber of Commerce and Industry, the manufacturers’ Business Sentiment Index rose to 99 for Q2 (from 77 in Q1).
• South Korean manufacturers continue to be highly competitive in China, and in global markets requiring competitive R&D, such as mobile phone handsets.
• Employment in March rose for the first time since November, and new domestic and international orders rose.

Risks:
• Shipments to the EU fell by 20.3% y/y in March, and as South Korea exports close to one-tenth of exports to the EU this will tell on its own growth if sustained.
• Delinquent corporate loans rose in February, with the construction, real estate, and housing and shipping sectors registering the largest increases.
• The leadership succession in North Korea to Kim Jong-un has not yet posed overt risks to business confidence but relations with the North could still do so in the 2010s.

Japan

Opportunities:
• Japan’s energy imports have risen substantially since the Great East Japan Earthquake of March 2011, with only one of 54 nuclear reactors operating as of April 2012.
• The desire of firms to diversify suppliers outside Japan to prevent any repeat of the post-quake supply chain problems of 2011 has also encouraged imports.
• Reconstruction is due to boost 2012 real GDP growth to almost 2%.
• The strong yen has also encouraged imports, up 11% in yen terms in March 2012.

Risks:
• A weaker yen would be welcome to manufacturing exporters, but increased energy imports have created a trade deficit in some recent months, potentially eroding the safe haven status of the yen.
• The near-shutdown of Japan’s entire stock of nuclear reactors over safety fears and the political difficulty of restarting them in localities exposes its firms more directly to global energy price volatility.
• The political consensus needed to raise sales taxes, bearable given low inflation, is absent, delaying the task of controlling public debt (more than twice GDP).
• The March 2011 disaster has permanently lowered the economic potential of the northeast region.
**Indonesia**

**Opportunities:**
- D&B forecasts above-5% real GDP growth in 2012, and over 6.5% average real GDP growth in 2013-16.
- By late 2011 the wholesale, retail and hospitality, and transportation and communications sectors were growing at or close to double-digit rates.
- Despite concerns in the 2000s of permanent overshadowing by China, the manufacturing sector is double its size at the start of the previous decade.
- Indonesia's congested and fragmented infrastructure mean that new network capacity can still have large returns for the economy as a whole.

**Risks:**
- Excess bureaucracy, corruption and protectionism is still deterring potential FDI.
- The mining, plantation and forestry sectors face uncertainty in the development and implementation of key legislation at local and national levels.
- Indonesia’s medium-sized economy is still exposed to the risk of capital flight and energy price volatility, the latter affecting public finances via subsidies.
- Inadequate road and power generation/transmission infrastructure throughout the archipelago increases costs and hampers business development.

**Brazil**

**Opportunities:**
- Brazil's economy has benefitted from strong demand for its commodity exports and rising levels of foreign capital inflows since 2009.
- Continued infrastructure development and the expansion of the offshore oil sector in particular will ensure demand for capital goods imports.
- The country’s growing middle class will provide a stable source of demand for consumer goods.

**Risks:**
- The global slowdown (particularly in China) will dampen demand for Brazilian commodities throughout 2012–13.
- The economy has already slowed significantly (from a mini-boom in 2010) as a result of tighter fiscal and monetary policy combined with weaker external demand.
- Many exporters to Brazil are likely to see falling sales in 2012–13 thanks to tighter import controls and higher import tariffs. Car makers are likely to be hit especially hard.
- Currency depreciation in 2012 will help to dent import demand, and currency volatility will be an ongoing concern.
Canada

Opportunities:
• Canada’s natural resource sector (which accounts for nearly 50% of exports) is still benefitting from elevated global commodity prices.
• Large-scale investment commitments continue to flow into the country’s metal and oil and gas sectors, reflecting their favourable export prospects.
• The strong currency has increased Canadians’ purchasing power; many consumers now purchase products more cheaply directly from foreign retailers.
• The strength of the currency is also encouraging (or forcing) many firms to boost imports of productivity-enhancing technologies.

Risks:
• With the economy slowing, consumer demand is a source of concern, with household debt levels close to all-time highs.
• The housing market is overvalued; and a sharp correction would have significant impacts on multiple sectors.
• As it is, some sectors are already seeing rising business failures (manufacturing, construction, and accommodation and food services).
• The strong currency remains a challenge for the country’s struggling manufacturing sector.

India

Opportunities:
• While clearly undergoing a slowdown, India is still expected to post real GDP growth of more than 6% in both 2012 and 2013, while keeping average inflation in single digits.
• India’s rapidly growing middle class retains a pent-up demand for basic consumer goods, while India’s more affluent have shown strong demand for high-end luxury items.
• With inflation trending downward and monetary policy loosening, corporate profits are set to rise after contracting through H2 2011.

Risks:
• Industrial and infrastructure investment remains hampered by policy uncertainty, administrative delays and high interest rates.
• The government’s decision to raise excise and service taxes will raise the cost of production.
• Planned caps on government subsidies (e.g. petroleum products) will dampen import demand but help to improve its own finances.
• The minority coalition government lacks legislative authority and frequently backtracks on promised policies.

For more information about trade terms, please contact D&B Country Risk Services.
D&B Country Risk Services
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Additional Resources
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