

Growing Beyond

Rapid-growth markets

EY Rapid-Growth Markets Forecast

October 2013



EY

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“Our rapid-growth markets may be feeling buffeted by a global storm that has long been affecting their mature market counterparts. But with the right policy responses to the immediate challenges they face, and a determination to continue reforming their economies, they can continue to build a future based on sustainable growth.”

Rajiv Memani,
Chairman of the Global Emerging
Markets Committee

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Many emerging markets such as Brazil, India, Indonesia and Turkey have been forced to tighten monetary policy as a result of external pressures and we now expect growth next year in RGMs to be 4.7%.

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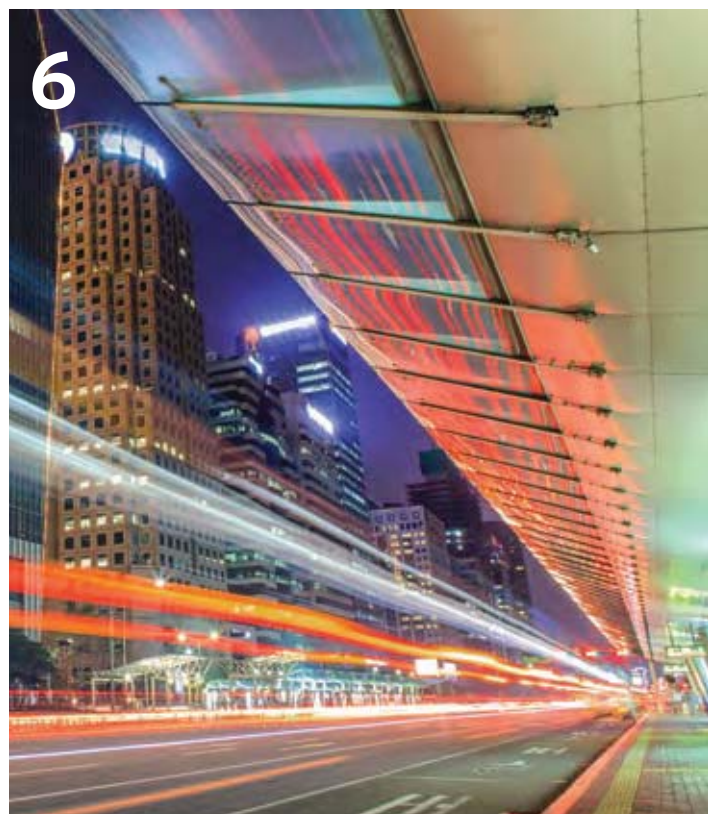
**OXFORD
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October 2013 Forecast

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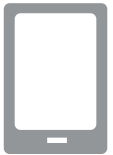
Welcome



A handwritten signature in white ink on a dark background, appearing to read 'Rajiv Memani'.

Rajiv Memani
Chairman of the Global Emerging
Markets Committee

The narrative of the global economy appears to have taken a turn. Since the start of the world's financial crisis, the mature economies have struggled with recession, budget cuts and then slow growth. Meanwhile, the emerging markets have been much more stable, withstanding the global storm and posting impressive GDP growth rates.



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However, 2013 has so far told a different story. Despite persistent political uncertainty over the federal debt ceiling, the US economy has stabilized and strengthened. And recession has ended at last in the Eurozone. Europe has enjoyed a period of relative financial stability, and a recovery – albeit a slow and painful one – is under way.

But while things are looking up in mature markets, the emerging economies are looking less resilient.

With the notable exception of China, GDP growth in the second quarter of the year is showing a declining trend across our rapid-growth markets (RGMs). So, what is causing this shift in events?

Uncertainty in global financial markets has been heightened: first, by indications that the US would start to unwind its program of quantitative easing, and then by the political dispute over the US debt ceiling. With signs of revival in the Eurozone, and US exuberance over shale gas discoveries, both these regions are looking more stable than before.

Earlier this year, most emerging markets, confident of healthy GDP growth over a sustained period and steady capital flows from developed markets, were spending freely on consumer and capital goods. The rising imports and high commodity prices resulted in increased current account deficits and rising inflation. With the economic recovery in the developed markets and announcements regarding quantitative easing, the tide of capital flows reversed suddenly. The result has been a marked fall in many RGM currencies, sharp rises in bond yields and underperformance in equities. In response to these external pressures, a number of RGMs have been forced to tighten monetary policy. The rise in bond yields and policy rates have led to much higher borrowing costs for governments, businesses and households. These rising costs will translate into lower investment and consumption, all of which weighs on their immediate growth prospects. We now expect growth next year in RGMs to be 4.7%. This is considerably weaker than the 5.7% forecast in our July edition.

However, given that tapering of quantitative easing in the US is likely to be delayed to next year, and the economic recovery in several developed markets, we are beginning to see capital flows toward the emerging markets. This gives governments in emerging markets the opportunity to move

forward with structural reforms and ease regulatory restrictions. This will restore investor confidence and help to inject greater doses of capital. In some of the larger RGMs, upcoming elections could be defining moments for change. Those that fail to reform are likely to suffer for a longer period. It is critical that RGMs deregulate where required and make fundamental changes to make export oriented sectors more successful by taking full advantage of the depreciation in their currencies.

We are also seeing the emergence of the next tier of emerging markets, in addition to the BRICS. Investors are attracted to the relative ease of doing business and reduced complexities in these new emergers.

Inside, we explore what these developments mean for businesses and how they can respond. Advice ranges from ensuring that big currency risks are hedged, to reviewing the comparative cost of corporate locations in the light of currency shifts. In the longer run, businesses need to adapt to changing consumption patterns among indebted consumers, and work out how to succeed in a world where money is more expensive.

This edition of the *Rapid-Growth Markets Forecast* includes an important innovation. While differences in growth between RGMs are important, it is also helpful for investors and businesses to compare the outlook in different sectors. So, for this and future reports, we are providing a forecast for growth in RGMs across sectors. Strong manufacturing growth in emerging markets means that, by 2020, they will be producing more trucks than developed markets. And these trucks will, of course, need parts, assembly, marketing and many other elements. Understanding sector trends will make it easier to spot such opportunities.

Our rapid-growth markets may be feeling buffeted by a global storm that has long been affecting their mature market counterparts. But they still have the power to write the next chapter of their story. With the right policy responses to the immediate challenges they face, and a determination to continue reforming their economies, they can continue to build a future based on sustainable growth.

To learn more about rapid-growth markets, their business environments and local contacts, please visit ey.com/rapidgrowth.

Highlights

Weak growth and sharp currency falls have added to the challenges in rapid-growth markets

- ▶ With the notable exception of China, GDP growth in Q2 2013 and the outlook in Q3 is showing a declining trend across most of the rapid-growth markets (RGMs). In contrast, the advanced economies have surprised us with their resilience.
- ▶ RGMs have been buffeted by instability across financial markets. This has added to the challenges they face. A flight from risk has driven sharp falls in RGM currencies, steep rises in bond yields and an underperformance of equities. The political dispute over the US government shutdown and debt ceiling has increased uncertainty in financial markets – and about growth prospects in the US and beyond.

High inflation and borrowing costs will weigh on investment and consumption

- ▶ Many emerging markets, such as Brazil, India, Indonesia and Turkey, have been forced to tighten monetary policy as a result of external pressures.
- ▶ The rises in bond yields and policy rates have led to much higher borrowing costs for governments, businesses and households. These higher costs will translate into lower investment and consumption.

- ▶ We now expect growth next year in RGMs to be 4.7%. This is considerably weaker than the 5.7% forecast in our July edition. The move is driven by downward revisions to Latin America, Russia and Asia.

Many RGMs are still vulnerable to external pressures

- ▶ We are likely to see further financial market volatility over the coming months. Our heatmap of risk shows that a number of RGMs remain vulnerable to pressures from capital outflows.
- ▶ Turkey, Argentina, Egypt and India all rank as vulnerable according to our risk index. Risk in these countries is driven by relatively high current account deficits, high levels of government debt, fast-growing credit markets, and inflation.

Tackling medium-term challenges in RGMs will require a political consensus for reform

- ▶ Many responses to the financial market volatility have been too focused on trying to slow the currency falls. Not enough emphasis has been put on policies to boost medium-term growth.

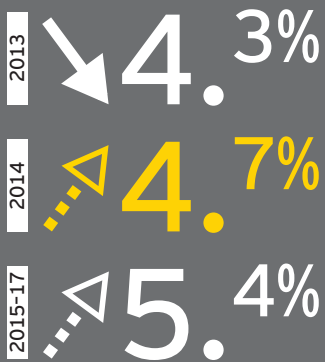
- ▶ With some of the major RGMs facing elections over the next year, it has been harder to build a political consensus for economic reforms. We will see more divergences in growth prospects between those RGMs that are willing and able to implement economic reforms to facilitate growth, and those with weaker institutions.

- ▶ India needs to take bold steps to improve its business environment, and Brazil's consumers are saddled with high levels of debt. In contrast, Indonesia has cut fuel subsidies to improve its fiscal sustainability, while Mexico plans to open its oil sector to more foreign investment.

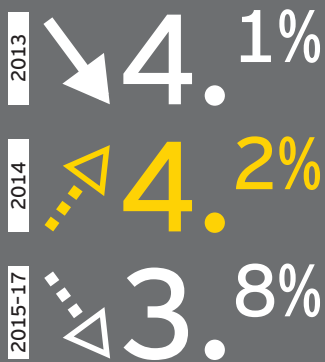
- ▶ The lower rate of growth in China is part of a deliberate effort by the Government and central bank to curb the rapid growth in credit and set the economy on a more sustainable path. But maintaining growth while China rebalances will be tricky. Financial sector reform and the development of the recently opened Shanghai free-trade zone are keys to spurring trade and innovation in China.

- ▶ Despite the near-term challenges, manufacturing and utilities – which represents nearly a third of output in RGMs – is expected to grow by more than 6% in 2015-17. As the numbers of middle-class households expand rapidly in RGMs, demand for financial and business services will also grow strongly in coming years, rising almost 6% by 2017.

GDP growth



CPI inflation



RGM new cars registration

2010 **25.2m**

In 2010, for the first time ever, the RGMs registered more new cars than the advanced economies. Over the next 10 years, the number of new cars registered will:

- ▶ Stay roughly constant in Japan
- ▶ Nearly double in Brazil, Russia, South Africa and Turkey
- ▶ More than double in China, India, Indonesia and Thailand.

Top five potential risks from heatmap

| | Overall score |
|-----------|---------------|
| Turkey | 20 |
| Argentina | 18 |
| India | 18 |
| Egypt | 17 |
| Vietnam | 17 |

RGM forecast by sector

| | 2013 | 2014 |
|---------------------------------|------|------|
| Manufacturing and utilities | 4.5 | 5.5 |
| Primary sector | 1.9 | 2.2 |
| Construction | 4.8 | 5.6 |
| Distribution | 4.4 | 5.1 |
| Financial and business services | 4.2 | 5 |
| Non-market services | 4.9 | 5.1 |





Implications for businesses:

Unstable environment requires agility

Unstable environment requires agility

Brighter growth prospects for developed economies have dimmed those of many RGMs. The prospect of less accommodative monetary policy in the US has sucked money from many fast-growth economies, causing their currencies to fall, interest rates to rise and growth to slow.

Few companies will, as a result of slower growth in RGMs, come to see emerging markets as less attractive compared with developed ones. But, as the world begins to adjust to the end of cheap money, many firms will want to review their fast-growth investments and operations in light of changed currency values and demand prospects.

An uncertain outlook

The broad geopolitical outlook remains unstable. The failure of the US Congress to agree a new budget was greeted by a slide in the dollar but a rise in US equity markets. Political and economic uncertainty is widespread, from Europe, through parts of the Middle East to rising Asia. China's rebalancing, free of currency instability, progresses soundly. But risk has increased sharply in some rapidly growing markets, notably India, Turkey, Egypt and Argentina. To cope with this changing backdrop, corporate leaders need to be alert. They must ensure that their decision-making is responsive and their companies are agile.

Focus on the business while waiting for the pickup

As a result of developments over the past quarter, our 2013 GDP growth forecast for the 25 RGMs has been cut to 4.3%, down from the 4.6% we anticipated in our July edition. More importantly, the pickup we expected next year will now be delayed until 2015. Responding to slowing growth in Asia and Latin America, we have reduced our 2014 forecast for overall growth in RGMs from 5.7% to 4.7%. However, we expect a resurgence to 5.3% in 2015.

Businesses must focus on four main factors: currency valuations, demand prospects, the investment outlook and structural adjustment.

Responding to weakening currencies

The value of many RGM currencies has fallen. Notably, this is the case in countries that could benefit from structural market reform, such as Brazil, Russia, India, Indonesia, South Africa and Turkey.

As a result, growth in reported revenues and profits of European and US groups with big sales in these markets will slow. The slowdown will be pronounced in the automotive, and consumer and luxury goods sectors. Volumes sold in these markets could also fall, or grow more slowly. This is because imported goods will cost more, while the cost of imported raw materials for locally manufactured goods will rise. If price rises are passed on to consumers, they will probably buy less. If not, margins will be squeezed. Where the financial flows involved are significant, companies should seek to protect their margins by hedging currencies – and market data shows that more are doing so.

Look for the best location

If lower valuations continue, however, companies can adapt their operations to changes in the relative competitiveness of locations. Sites serving national markets may try to bolster local sourcing, or procurement from other countries or regions where currencies tend to move in step.

Multinationals may want to rebalance production for global markets in favor of sites that are benefiting from currency devaluation. Some service industries could also benefit from the enhanced competitiveness that arises from cheaper currencies. These include software, consulting and tourism. However, companies should note that rising costs in RGMs are likely to spur inflation. Indeed, wages are gradually increasing.

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Sales of new cars in emerging markets now exceed those in developed countries. And their share is growing. Although US vehicle registrations are experiencing a post-recession recovery, the underlying trend for light vehicle sales in developed markets is flat. Yet global car sales are set to rise from 81 million last year to 116 million in the next decade. Most of that growth will be in emerging markets, with the BRIC countries acting as the primary drivers until 2020.

Given the low density of cars per 1,000 people, a growing middle class and, in some cases, strong population growth, emerging markets are vital to automotive companies – and they must invest in them. More cars are now sold in China than in the US.

But each market is unique, and volatility is a growing challenge. Many markets face poor infrastructure and urban traffic management, complicated regulatory framework and insufficient technological expertise, particularly in the supplier space. Though economic growth has slowed, the Brazilian car market still looks promising. In India, the introduction in March of a higher tax rate on popular sports utility vehicles (SUVs) caused annual growth in SUV sales to slump abruptly from 52% to single digits. And in China, the Government is restricting vehicle registrations in congested areas.

In most markets, the US, European and Japanese vehicle manufacturers dominate. The Chinese Government is promoting its own brands, but they continue to struggle in the marketplace. Incentives for local manufacturers are also significant in

Russia and India. In time, they will become big players. But that is not a near-term concern for established rivals.

To stay competitive, manufacturers need to identify the best vehicles for each market. There is a huge uptick across most markets in the sales of smaller, more fuel-efficient SUVs, and manufacturers can make good profits on them.

To reduce the manufacturing complexity, increase flexibility and save costs, companies are reducing the number of vehicle platforms and leveraging them across markets. They are laying thrust on global platforms, using the same base globally to produce multiple vehicles on the same line.

Improving the fuel efficiency of vehicles is also important for automotive companies, and light-weighting is just one way of doing so. Looking ahead, diverse powertrains, including diesel, electric, hybrid, fuel cells and compressed natural gas, will all win a place in the market. No company alone can afford to pay the cost of being at the cutting edge of every technology. So they will have to collaborate to ensure that they aren't shut out of some markets.

With the number of megacities growing, companies need to create sustainable integrated transport networks – involving the use of cars, trains, buses and bicycles – to address the future urban mobility market. To succeed in this emerging ecosystem, companies need to develop their value propositions and identify ways in which they can work together to enhance their competitive positions.

Adapting to more discriminating consumers

But what about the long-term impact on consumer demand? As expansion slows in emerging markets, will developed economies broaden their appeal? Probably not. Setting aside exceptions such as Brazil, growth in many RGMs, from China and Nigeria to Kazakhstan and much of the Middle East, still far outpaces growth in the US, Japan and, especially, Europe.

For many products and services, developed markets are replacement markets. But in RGMs, newly minted middle-class consumers are buying their first cars, life insurance contracts or designer dresses. Services already account for almost half of gross value-added among our 25 RGMs, and that share will grow.

The scope for sales growth in business, financial and consumer services – from hotel nights to coffee shops – is much greater. Western business models will not necessarily be replicated, but leapfrogged by technology and more collaborative consumption. To understand demand and profit, companies must embrace these consumers.

Unstable environment requires agility

Shrewd investment

Consumer debt in many RGMs rose rapidly when money was cheap. Now, capital outflows and rising bond yields have pushed up the cost of borrowing for households, businesses and governments. As a result, investment becomes less attractive. Companies that cater to consumers in RGMs should prepare for a more somber mood and slower spending growth. They should also review financing costs within their own operations, and hedge against interest rate rises where possible. It pays to treat foreign currency borrowing with care. Higher rates may challenge the economics of investment plans: because the returns are less certain, they must now be monitored carefully.

Profiting from reforms

During the years of rapid growth, the pressure to make difficult policy choices eased. Now, for example, countries such as Indonesia are curtailing fuel subsidies to invest more in education and infrastructure. To rekindle growth, countries will be more motivated to reform labor laws, open markets and simplify business administration. Business leaders should step up monitoring to spot new opportunities. In particular, cash-strapped governments may be more open to public-private partnerships to address issues such as inadequate transport infrastructure. But would-be partners, whether foreign or domestic, should read the small print with care. The balance of power is shifting. Quantitative easing, a temporary policy designed to spur recovery in developed economies, also buoyed up RGMs. As the tide of money ebbs and some RGMs become more exposed, companies with cash piles have more choices. Competition between RGMs for the favor of footloose capital and business is intensifying again. Business leaders should prepare for a world of more balanced growth, where money has more value.

▶ Responding to instability

Today

- ▶ Ensure that big currency risks, such as energy priced in US dollars, are hedged where possible.
- ▶ Revise sales and financial forecasts.
- ▶ Accentuate the focus on efficiency and productivity – but avoid knee-jerk cost-cutting.
- ▶ Be wary of foreign currency borrowing, monitor the implications of rising interest rates and hedge where necessary.
- ▶ Where necessary, inform stakeholders, including shareholders, of consequences.
- ▶ Review the comparative cost of corporate locations in the light of currency shifts.

Tomorrow

- ▶ Take a fresh look at supply chain economics. Have new suppliers become competitive?
- ▶ Look out for upward pressure on costs: keep wages under review.
- ▶ Accentuate customer focus: scan for and adapt to changing consumption patterns among indebted, squeezed consumers.
- ▶ Closely monitor instability in high-risk markets, especially of currencies, interest rates and inflation.
- ▶ Watch for widening divergences in growth prospects. Be alert to opportunities arising from any renewed focus on market reforms.
- ▶ Ensure that the business is adapted to a world in which money is more expensive.





New challenges deepen need for reform

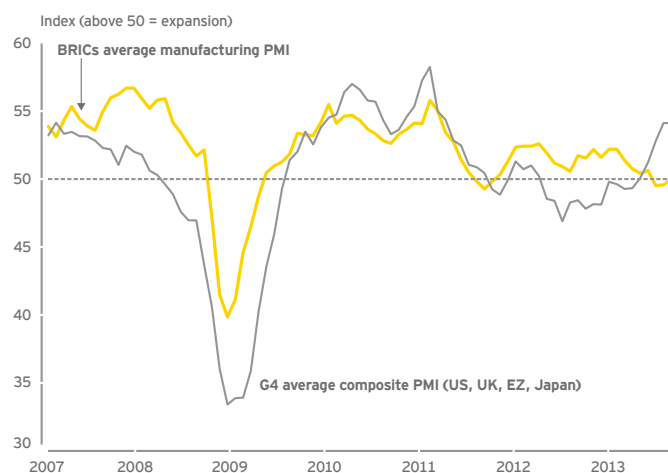
New challenges deepen need for reform

Declining growth trend in H1 2013

GDP growth slowed across most of the rapid-growth economies in H1 2013. India reported its weakest annual growth for more than four years in Q2 and Russia fell into a technical recession. While China's economy shows signs of improvement in Q3, for most other rapid-growth markets, Purchasing Managers' Index (PMI) surveys suggest that this weakness has continued into Q3.

Figure 1

World: purchasing managers' indices



Source: Oxford Economics; Markit.

In contrast, recent months have seen GDP growth exceed expectations in Japan and the Eurozone, with a range of positive indicators across the advanced economies. The US non-manufacturing PMI reached an eight-year high in August, while the UK composite index recorded its highest ever reading in the same month.

The longest recession in Eurozone history came to an end in Q2 2013, and a slow recovery is now in prospect. GDP is forecast to fall by 0.5% in 2013, but a substantial easing in the pace of fiscal austerity will help lift growth to 0.9% in 2014 and 1.5% a year in 2015-17.

The recovery in the US appears well established, with growth close to 3% expected next year. However, the US faces potential further headwinds as a result of the political dispute over the US government shut-down and debt ceiling. If US growth prospects were hit significantly, exports would fall and global risk aversion would rise, adding to the financial market pressures on RGMs.

Financial turmoil adds to challenges ...

Alongside the lower-than-expected economic data, RGMs have been buffeted by considerable instability in financial markets. This was partly caused by expectations that the US Federal Reserve would start to taper quantitative easing and that there would be a rise in US bond yields. But instability also reflects heightened unrest in the Middle East and concerns over structural weaknesses across a number of RGMs. Turmoil in the financial markets has added to the challenges that rapidly growing economies face, and a number of them look vulnerable to further pressures in the short term. These factors have brought about a flight from riskier assets. The effect of this has been:



► **Sharp drops in RGM currencies.** The Indian rupee depreciated by 20% in the space of three months to reach a record low against the dollar in late August. The currencies of Indonesia, Turkey and Brazil have also endured substantial depreciations. The currencies hit hardest have been those with particularly wide or deteriorating current account deficits, such as South Africa, Turkey, Indonesia and India. While some currencies are now recovering, there will be an impact on inflation this year. And some markets are still vulnerable to pressures on their current accounts.

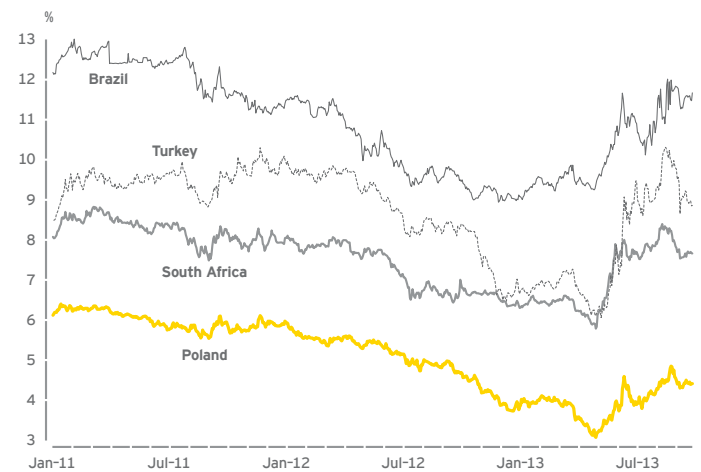
► **A sharp rise in bond yields.** Government bond yields in many RGMs have risen sharply. Brazilian and Turkish yields rose by around 200 basis points (bps) and 300bps respectively from May to September. They have fallen a little recently, but they remain much higher than in April. The rises in bond yields preceded any moves in policy rates. In addition, many rapidly growing economies have been forced to tighten monetary policy despite the weak growth as a result of external pressures. They include Brazil, India, Indonesia and Turkey.

Figure 2
Emerging markets: exchange rates vs. US\$



Source: Haver Analytics.

Figure 3
Emerging markets: 10-year government bond yields



Source: Haver Analytics.

New challenges deepen need for reform

► Consumers in Brazil still buffeted by inflation and high interest rates

The Brazilian real (BRL) has fallen more than 9% since the start of the year. Although the economy is significantly less vulnerable to exchange rate risks than it was in the late 1990s, the current account deficit is still growing. Although Brazil has more than US\$300b in foreign reserves and is a net foreign creditor, this deficit could become a problem in the medium-to-long term. The depreciating currency may generate some inflationary pressure and fuel the need for higher interest rates. Although this may have an impact on growth, it must be taken into consideration that, in the past 10 years, Brazil grew significantly despite high interest rates. One of the reasons why growth can be maintained in these conditions is that financing for investments is widely available at subsidized interest rates at the Brazilian Development Bank (BNDES).

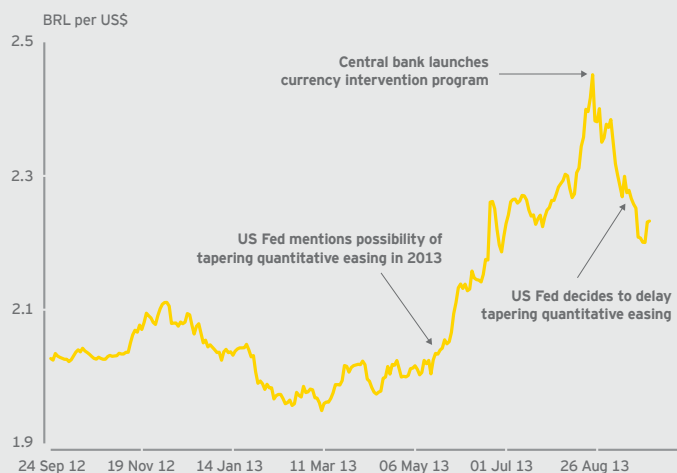
However, some business investments could be affected because the price of imported capital goods may increase. On the positive side, a weaker exchange rate should start to make Brazilian firms more competitive. This may counteract the slowdown in consumption, but a significant boost to trade should not be expected. A number of structural problems also need to be addressed. But with elections due by next October, the Government's focus is likely to remain on the short term.

The Brazilian real has weakened significantly ...

In the past three months, the BRL has been badly affected by uncertainty over US monetary policy. Between 22 May and 21 August, the real fell almost 20% to 2.42 against the US dollar, before rebounding to 2.20 in the aftermath of the US Federal Reserve's decision to postpone tapering its program of asset purchases. The real has since regained some ground, but remains weaker than it was at the start of the year.

Figure 4

Brazil: exchange rate

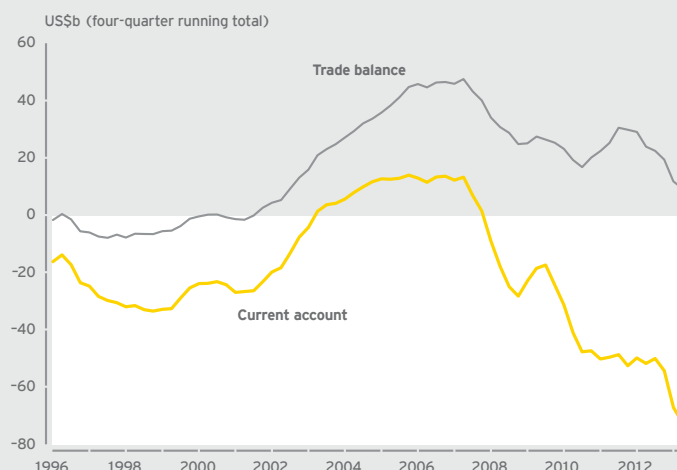


Source: Haver Analytics.

Although Brazil looks substantially less vulnerable to exchange rate movements than it has been in the past, a growing current account deficit is still a cause for concern. The deficit reached US\$72b (3.2% of GDP) in the year to June. Large current account deficits have to be funded from foreign borrowing, which makes countries more vulnerable to sudden withdrawals. Nevertheless, we expect the current account deficit to reduce somewhat in the medium term, as world demand picks up and the effects of the depreciation make Brazilian exports cheaper.

Figure 5

Brazil: external balances



Source: Central Bank of Brazil.

We expect the real to trade between 2.20 and 2.40 to the US dollar in the final months of 2013, and at around 2.40 next year, in the run-up to the October presidential elections. The weaker currency will increase the price of imports and raise inflation. We expect CPI inflation to average 6.1% in 2014, well above the central bank's official target of 4.5%.

Central bank set to tighten policy and intervene in currency markets

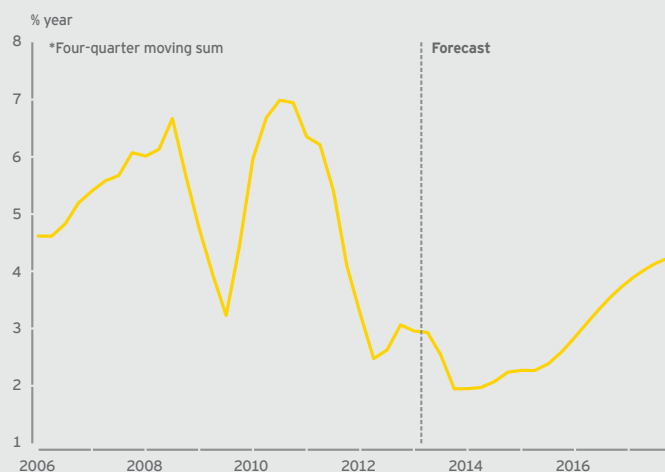
The combination of a weaker exchange rate and the prospect of higher inflation have prompted the monetary authorities to adopt a more aggressive response. Last month, the central bank announced a currency intervention program worth more than US\$60b. The program, which will last until December, will inject liquidity into the currency markets to reduce volatility. The authorities also raised the Selic policy rate to 9.5% in October, and we expect rates to reach 9.75% by the end of the year.



Adjustments may allow the economy to grow in excess of 3% in 2014

Nevertheless, this intervention will not be enough to bring inflation down to the target of 4.5%. Households in Brazil currently spend around a fifth of their disposable income on servicing debt, so some degree of deleveraging is required. Indeed, our heatmap of vulnerability for RGMs shows that, over the last three years, only in Turkey has credit as a share of GDP grown faster. But now credit markets are more mature, credit growth should moderate, easing the risks associated with rapid credit growth. Household indebtedness reached a peak in 2011-12. These consumers are now in the process of paying off debts. Because interest rates were high, Brazilians of all socioeconomic classes developed a culture of taking on short-term debt. Despite inflation, to which wages are indexed, the reduction of debt should soon enable consumption growth to pick up more than 3% by 2016.

Figure 6
Brazil: private consumption



Source: Oxford Economics.

Structural problems need to be addressed ...

Labor productivity in Brazil (GDP per worker) has grown by an average of only 1% a year for the past 15 years, compared with 1.6% in the US.

Yet despite the subdued pace of economic activity in the last two years, the jobless rate has remained close to all-time lows. In part, this is because Brazilian labor laws make it expensive to fire workers. Reforms to enhance productivity would therefore be more likely to promote an upturn in growth.

As well as the labor laws, businesses face obstacles such as high and complex taxes, poor infrastructure and excessive bureaucracy. These difficulties are so longstanding that they have their own name – the *custo Brasil* – or “Brazil cost”. We believe that these structural factors are a key reason why manufacturing investment was so weak in 2012, despite record-low real interest rates.

... but the pace of reform remains slow

Consumer spending has benefited from helpful labor market conditions and better access to credit. But a prolonged period of an uncompetitive exchange rate and industrial inflexibility pushed much of this demand into imports, while local manufacturing stagnated. It will take some time for a more competitive BRL to reverse this.

The economic environment could be improved if the authorities were to implement reforms. Some changes have been made, but the Government’s current focus is on short-term adjustments to boost demand.

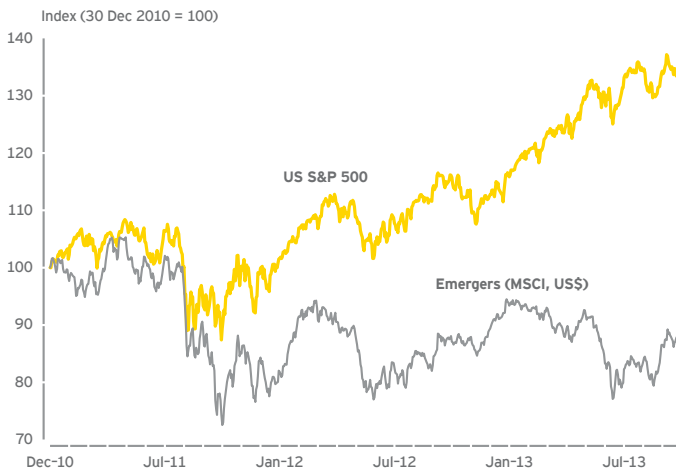
Medium-term outlook constrained

The outlook for Brazil is for relatively sluggish expansion. Annual GDP growth is forecast at just 3.2% for the next four years. This represents a considerable slowdown compared with the 4.6% seen from 2004-08. However, if Brazil were able to improve its business environment significantly and boost investment in infrastructure, growth could exceed expectations, rising above 4% over the medium term.

New challenges deepen need for reform

► **A significant underperformance of equity markets.** RGM equity markets have fallen by around 5% since the start of 2013. In contrast, the US Standard & Poor's index has risen by more than 15% over the same period.

Figure 7
Emerging markets: equity markets



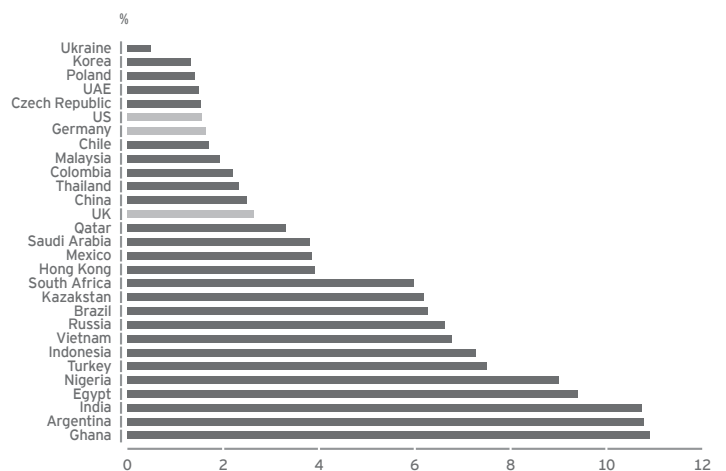
Source: Haver Analytics.

... and lowers growth prospects

While some RGM currency and equity markets have started to recover, the impact of falls in the financial markets will be felt for some time. The fall in currencies and rise in risk premiums in rapidly growing economies have added to the challenges for RGMs, especially as weaker currencies add to inflationary pressures. Higher inflation is a particular issue for Argentina and Ghana, where we expect consumer price index (CPI) inflation above 10% for this year as a whole.

The increases in bond yields and policy rates have led to much higher borrowing costs (in domestic and foreign currencies) – for RGM governments, businesses and households. The higher cost of borrowing will translate into lower investment. Consumption will be hit by falls in financial wealth, the greater cost of consumer credit and higher prices for imported goods, particularly commodities. The weaker outlook for domestic demand in RGMs, and subsequent weaker trade flows, has led us to revise down our forecast for growth in RGMs next year to 4.7%. This is substantially lower than the 5.7% we expected in July. The downgrade is driven in particular by lower forecasts for Asia and Latin America.

Figure 8
RGMF: CPI inflation, 2013 forecast



Source: Oxford Economics; Haver Analytics.



Some RGMs vulnerable to further pressures

Volatility in the financial markets is set to continue over the coming months. The recent capital outflows have provided a prescient reminder of how quickly countries can become embroiled in currency, or other, financial crises. Government debt is relatively low across many of the RGMs and central banks are better equipped to fight inflation than in previous decades. However, in some cases, the growth of the financial sector and globalization has added to potential vulnerabilities. Which RGMs are best placed to weather further financial storms, particularly as monetary policy is gradually tightened in the advanced economies?

Heatmap for RGMs

We have prepared a heatmap of vulnerability for the RGMs, drawing on previously published research into currency and banking crises, ranking each country under seven indicators of risks.¹ The purpose of our heatmap is to offer a risk assessment tool when evaluating different markets.

We ranked the 25 rapid-growth markets from 1 to 25 according to 7 components:

- ▶ The strength of the current account balance in 2012
- ▶ The level of external debt over GDP in 2012
- ▶ The level of government debt over GDP in 2012
- ▶ Average inflation in 2013
- ▶ The average growth of credit markets as a share of GDP from 2010 to 2012
- ▶ The ratio of foreign exchange reserves to imports in 2012
- ▶ The change in the currency against the US dollar over the 12 months to the end of September 2012

When giving the overall score (first column in the table) we have added all seven ranking figures; however, we have normalized the total ranking figures between 1 and 20. The highest figure indicates the highest risk.

For each indicator, the top eight countries are colored green, the middle nine colored orange and the riskiest eight colored red.

The heatmap shows:

- ▶ Large current account deficits need to be financed from foreign funding, leaving countries vulnerable to capital outflows.
- ▶ High levels of both external debt and government debt can lead to a country being unable to meet its debt payments, particularly following a sharp fall in its exchange rate.
- ▶ When a country's foreign exchange reserves are low compared with its imports, its import cover is low and it has less scope to protect itself against currency volatility.
- ▶ Sharp falls in currencies over the past year can be an indication of falling investor confidence in a country's ability to manage its external position.
- ▶ High credit growth and inflation can lead to asset price bubbles and other distortions within an economy. They can also limit the policy options available when a crisis occurs. For instance, reducing interest rates can help to boost growth, but it can also fuel inflation.

To give a few examples, in South Africa, credit markets are already relatively well developed, so credit markets are now growing slower than other RGMs and, as a result, are less of a concern (green). But low foreign reserves relative to imports, and a substantial current account deficit are flagged as higher risks (red).

In Indonesia, Turkey and Vietnam fast growing credit markets must be monitored carefully (red).

¹ Luc Laeven and Fabian Valencia, *Systemic Banking Crises: A New Database*, International Monetary Fund, 2008.

New challenges deepen need for reform

Heatmap

| | Overall score | Current account | External debt | Gov. debt | Inflation | Growth in credit-GDP | Import cover | Currency change over year |
|----------------|---------------|-----------------|---------------|-----------|-----------|----------------------|--------------|---------------------------|
| Turkey | 20 | 22 | 21 | 15 | 20 | 25 | 18 | 20 |
| Argentina | 18 | 12 | 13 | 16 | 24 | 23 | 12 | 25 |
| India | 18 | 21 | 8 | 21 | 23 | 16 | 13 | 22 |
| Egypt | 17 | 17 | 7 | 25 | 22 | 5 | 24 | 21 |
| Vietnam | 17 | 5 | 19 | 20 | 18 | 22 | 25 | 11 |
| Ghana | 17 | 25 | 17 | 22 | 25 | 8 | 21 | 1 |
| Indonesia | 16 | 16 | 11 | 9 | 19 | 20 | 11 | 24 |
| South Africa | 15 | 23 | 14 | 13 | 14 | 1 | 19 | 23 |
| Poland | 15 | 20 | 24 | 23 | 3 | 15 | 15 | 7 |
| Brazil | 15 | 14 | 6 | 24 | 16 | 24 | 3 | 19 |
| Czech Republic | 15 | 15 | 22 | 17 | 5 | 17 | 20 | 8 |
| Colombia | 13 | 18 | 9 | 11 | 8 | 19 | 10 | 18 |
| Chile | 13 | 19 | 20 | 4 | 6 | 12 | 14 | 17 |
| Mexico | 13 | 13 | 10 | 12 | 13 | 18 | 16 | 10 |
| Ukraine | 13 | 24 | 25 | 14 | 1 | 3 | 22 | 1 |
| Kazakhstan | 12 | 7 | 23 | 6 | 15 | 4 | 17 | 14 |
| Malaysia | 12 | 6 | 16 | 19 | 7 | 14 | 7 | 16 |
| Thailand | 12 | 11 | 15 | 10 | 9 | 21 | 5 | 12 |
| Russia | 10 | 9 | 12 | 5 | 17 | 11 | 4 | 15 |
| Korea | 9 | 8 | 18 | 18 | 2 | 6 | 9 | 5 |
| Nigeria | 9 | 4 | 4 | 8 | 21 | 2 | 8 | 13 |
| China | 8 | 10 | 5 | 7 | 10 | 13 | 2 | 6 |
| UAE | 6 | 3 | 1 | 1 | 4 | 7 | 23 | 1 |
| Saudi Arabia | 5 | 2 | 1 | 1 | 12 | 10 | 1 | 9 |
| Qatar | 4 | 1 | 1 | 1 | 11 | 9 | 6 | 1 |

What is displayed in each column:

1. **Overall scores** are based on the addition of the seven rankings. We have then normalized the total rankings from 1 to 20. The highest figure indicates the highest risk.
2. **Current account** balance shows the strength of the current account balance in 2012.
3. **External debt** shows the level of external debt over GDP in 2012.
4. **Government debt** shows the level of government debt over GDP in 2012.
5. **Inflation** shows average inflation in 2013.
6. **Growth in credit market** shows the average growth of credit markets as a share of GDP from 2010 to 2012.

7. **Import cover** shows the ratio of foreign exchange reserves to imports in 2012.
8. **Currency change over year** shows the change in the currency against the US dollar over the 12 months to the end of September 2012.

Legend of colors used in first column (Overall score):

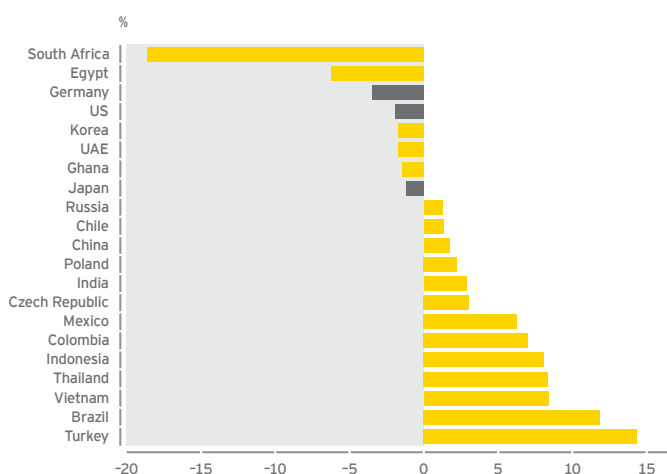
For each indicator, we have marked:

- ▶ In red: eight countries with highest risk
- ▶ In orange: nine countries with medium risk
- ▶ In green: eight countries with the lowest risk



Turkey, Brazil, Indonesia and Thailand have all seen rapid growth in credit over the past three years. Some of this reflects the deepening of financial markets in these countries, as the middle class expands and the demand for financial services rises. But a credit boom can lead to high levels of consumer debt, which can trigger a slowdown in consumption when interest rates rise. So rising credit can indicate that an economy is vulnerable to interest rate rises.

Figure 9
Average growth in credit over GDP over the last three years

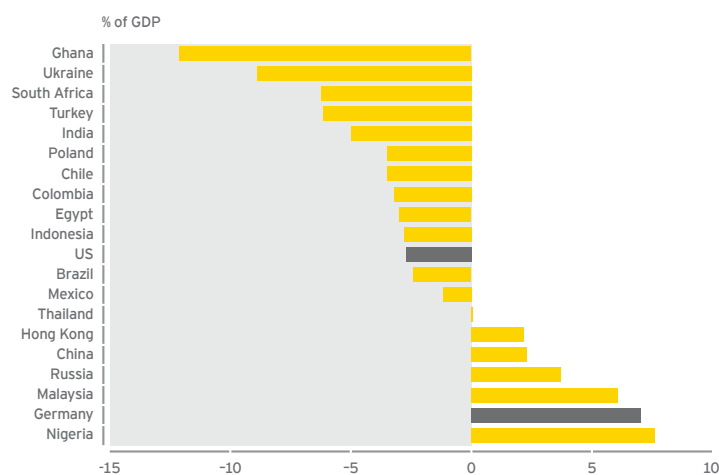


Source: Oxford Economics; Haver Analytics.

Looking at all of our selected risk indicators, we find that Turkey, Argentina, Egypt and India all show elements of vulnerability to currency and other financial crises. This vulnerability is caused by relatively high current account deficits, levels of government debt and inflation.

In contrast, countries in the Middle East, such as Saudi Arabia, Qatar and the UAE, appear robust, with low levels of government and external debt. The heatmap also suggests that the sharp falls in Columbia's currency may not be justified on the basis of fundamentals. It has low inflation and relatively moderate levels of government and external debt.

Figure 10
RGMs: current account 2012



Source: Oxford Economics; Haver Analytics.

Medium-term challenges are moving into view

Substantial medium-term challenges across a number of leading RGMs are becoming increasingly clear. But many responses have been too focused on trying to slow the currency falls. Not enough emphasis has been put on policies to boost medium-term growth. In addition, with some of the major RGMs facing elections over the next year – and major public protests over public spending in countries like Brazil and Turkey – it has been harder to build a political consensus for economic reforms. As a result, we now expect growth to be lower across RGMs in 2015, with an expansion of 5.3%, compared with the 5.9% forecast in the July report.

Brazil remains trapped into a low growth and high inflation dynamic, with inflation expected to be above 6% this year and growth well below 3%. Interest rates rose to 9.5% in September and are expected to increase a further 25bps. This will hamper the investment growth that is crucial to Brazil's future. The central bank's commitment to boost the exchange rate by providing more liquidity to the market may prove ineffective and hinder efforts to improve Brazil's competitiveness.

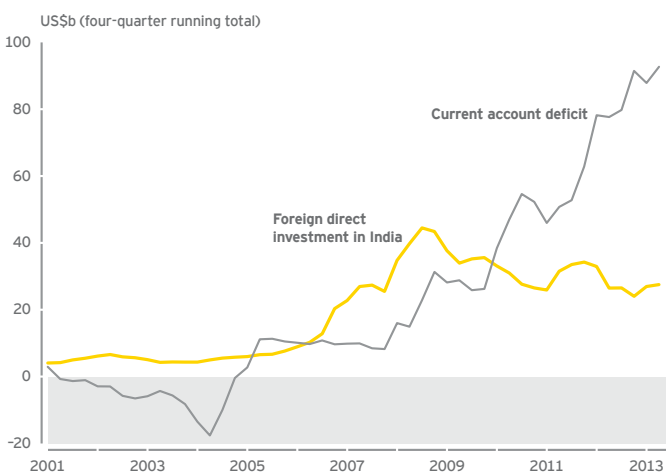
We are likely to see a continued slowdown of Brazil's consumer spending in the medium term, as households seek to reduce their high levels of debt. Government policies need to be more focused on developing infrastructure to boost Brazil's manufacturing competitiveness, and education to ensure the right skills for the next generation, rather than short-term initiatives.

New challenges deepen need for reform

Compared to its “golden era” of 2005-10, when the economy expanded at an average of almost 9% a year, GDP growth in India dropped to just 5% in 2012, and to 4.4% in Q2 2013. The current account deficit has more than doubled to 5% of GDP and, even in the face of slowing demand, inflation has remained stubbornly high.

Figure 11

India: FDI inflows and the current account



Source: Reserve Bank of India.

The Government has attempted to reduce the current account deficit by raising the import duty on gold and encouraging external financing by the proposed issue of “quasi-sovereign” bonds – whereby the Indian Government provides a guarantee to the bondholders against the default of organizations that raise finance for large infrastructure projects. But the announcements failed to reassure investors that a concerted medium-term plan to improve India’s growth prospects was in place.

One way to tackle the current account deficit would be to cut fuel subsidies. This would reduce the government deficit and oil imports. But with elections next year, it has been difficult to achieve a political consensus for this reform. Nevertheless, India’s finance minister has announced some encouraging measures to improve efficiency. They include liberalizing foreign direct investment (FDI) in key sectors such as retail and insurance, though implementation

will require legislation at the state level. In addition, to further improve India’s business environment, greater infrastructure investment is needed, particularly in the power sector. We now expect GDP to expand by 4.5% in 2014, down markedly from the 6.4% estimated in our July edition. Growth is then expected to remain below 7% in 2015-17.

The preliminary estimate indicates that Russia slumped into a technical recession in Q2, following successive quarterly contractions in H1.² Such an outcome is extremely disappointing, particularly in the light of oil prices that have averaged over US\$100 per barrel. As a result, our forecast for real GDP growth this year has been downgraded to 1.5%, compared with the 2.7% envisaged in July. In the medium term, the economy’s poor demographic profile, together with a fairly limited pace of policy reform, will constrain real GDP growth to less than 4%. We think that risks are skewed to the downside, with the recent slowdown having highlighted the existence of structural deficiencies.

Some RGMs are better placed to implement reforms

Certain RGMs have made significant progress in addressing their medium-term sustainability. In June, Indonesia improved its fiscal position by reducing fuel subsidies. The Government has said that three-quarters of the estimated IDR18.4t (US\$1.8b) of savings that result will be spent on infrastructure under the 2014 budget. In addition, the reduced burden of fuel subsidies should make for a more stable macro environment and enhance Indonesia’s attractiveness as a destination for investors. Nonetheless, the rupiah is one of the few RGM currencies that did not gain much ground against the dollar in September. It could be that investors are underweighting some of the progress that Indonesia has made.

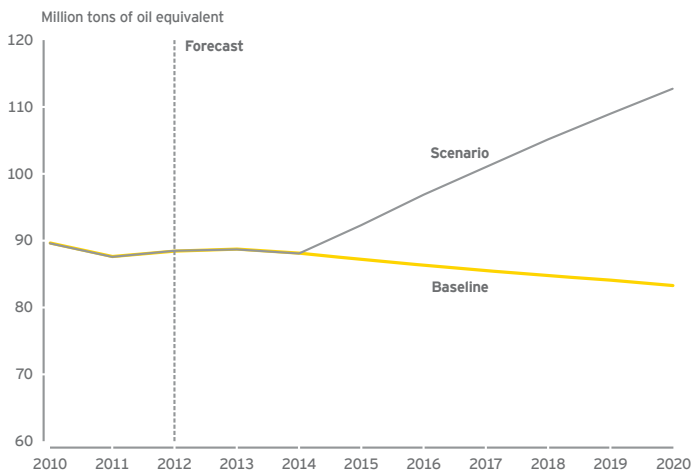
Mexico was hit by an unexpectedly sharp 0.7% fall in GDP in Q2. However, we do not expect the weakness of the Mexican economy in H1 to be repeated in H2, because its fundamentals remain fairly sound. Inflation is relatively low, macro policy is supportive – indeed the Mexican central bank cut its target rate by 25bps in September – and the country’s exporters should benefit from rising demand in the US. In addition, the Mexican Government is pressing ahead with structural reforms, and is now focusing on the oil sector. If progress is made here and the economy picks up, currency weakness in Mexico may be more short-lived than in other RGMs.

² A technical recession is defined as two consecutive quarters of negative economic growth as measured by a country’s GDP.



Figure 12

Mexico: oil exports



Source: Oxford Economics; International Energy Agency.

Substantial reforms to the oil sector have been announced, against the backdrop of falling oil production levels. Foreign participation in the market will be allowed for the first time since 1938. The Government's aim is to exploit untapped reserves by attracting the technical knowledge and capital of foreign producers. If the Government reaches a deal that is acceptable to the multinational oil companies, the economic benefits could be substantial. The authorities hope to secure an additional US\$10b of investment in the sector every year until 2025. They estimate that this would increase production by around one million barrels per day. If this were achieved, we estimate that an additional 330,000 jobs would be created by 2020, and that oil exports would rise by a third to around 110 million tons of oil equivalent.

Brighter news in China

In China, better economic news has put the recovery on a more established footing. Manufacturing output and new orders have improved, while growth in retail sales has been steady over the course of the year. As a result, we now expect growth this year close to the Government's target of 7.5%. But next year, as bank lending slows – particularly to state-owned enterprises – investment will moderate and overall GDP growth will slow to around 7%.

The slowing of China's growth from rates over 10% in 2010, to closer to 7% now, reflects the weakness in world trade. But it is also the effect of deliberate policies aimed at reducing dependency on credit-fuelled investment and rebalancing the economy by encouraging higher consumption.

Maintaining growth while credit is reined in will be tricky. China needs to boost its productivity and improve its urban environment. Financial sector reform and the development of the recently opened Shanghai free-trade zone are keys to spurring trade and innovation.

We are likely to see more of a divergence in growth between those RGMs that are able to manage their economic reform effectively and those with weaker institutions that face more challenges in implementing reforms.

Conclusions

- ▶ Growth has been slowing across most RGMs in the last six months, with the notable exception of China. In contrast, the advanced economies have surprised us with their resilience.
- ▶ RGMs have been buffeted by instability across financial markets. This has added to the challenges they face. A flight from risk has driven steep falls in RGM currencies, sharp rises in bond yields and an underperformance of equities. Some RGMs remain vulnerable to capital outflows.
- ▶ Higher borrowing costs will weigh on investment and consumption. We now expect RGM growth next year to be 4.7%, considerably weaker than our July projection of 5.7%. This move is driven by downward revisions to Latin America, Russia and Asia.
- ▶ To achieve growth of 5.5% by 2016, RGMs will need to achieve a political consensus on economic reform. Over the next three years, we will see more divergences in growth prospects between those RGMs that are willing and able to implement growth-boosting economic reforms and those that are not.

New challenges deepen need for reform

► Manufacturing, a key sector

Outlook for different sectors across RGMs

While differences in growth between RGMs are important, it is also helpful for investors and businesses to look at the outlook for different sectors across RGMs.

Forecast of rapid-growth markets by sector (annual percentage changes in gross added value)

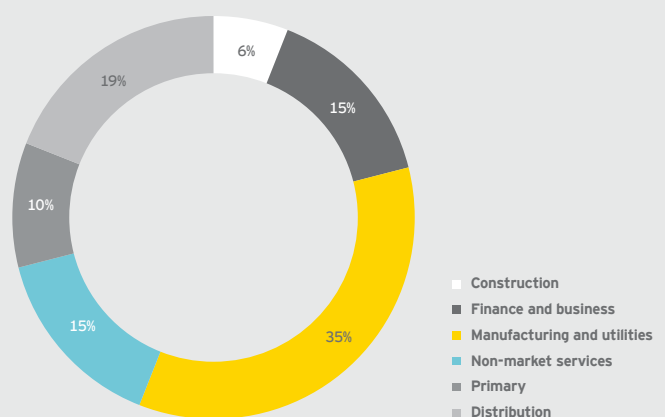
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|---------------------------------|------|------|------|------|------|------|
| Manufacturing and utilities | 5.1 | 4.5 | 5.5 | 6.3 | 6.5 | 6.3 |
| Primary sector | 1.7 | 1.9 | 2.2 | 2.6 | 2.6 | 2.6 |
| Construction | 5.0 | 4.8 | 5.6 | 6.0 | 6.1 | 6.1 |
| Distribution | 5.6 | 4.4 | 5.1 | 5.5 | 5.8 | 5.8 |
| Financial and business services | 4.2 | 4.2 | 5.0 | 5.6 | 5.9 | 5.9 |
| Non-market services | 4.4 | 4.9 | 5.1 | 5.4 | 5.5 | 5.4 |

Source: Oxford Economics.

Last year, more than a third of gross value added (GVA) in the rapid-growth economies came from manufacturing and utilities. The largest manufacturing sectors are food, beverages and tobacco; electronics and electrical engineering; and machinery and transport equipment. While weaker global demand has slowed growth of the manufacturing and utilities sector to less than 5% this year, we expect it to recover strongly, growing in excess of 6% in 2015-17.

The primary sector, which includes agriculture and mining, remains vital. But its share of total output across the RGMs has declined, as these markets have diversified into higher-value sectors.

Figure 13
RGMs: gross value added by sector, 2012



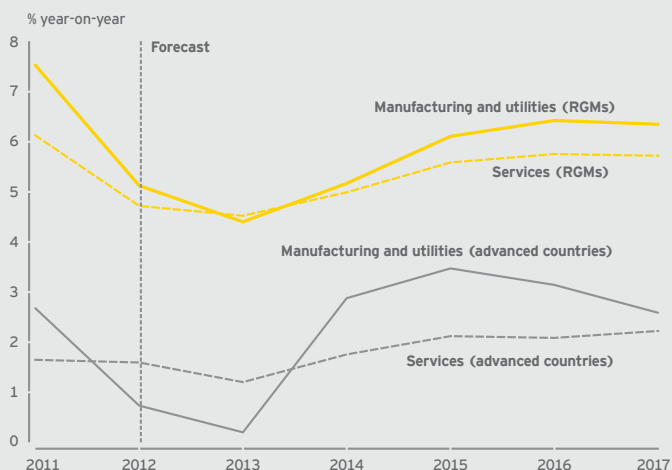
Source: Oxford Economics.



The services sector already contributes almost half of the GVA in our rapid-growth markets. As figure 13 shows, this is split fairly evenly between finance and business services, distribution (which includes wholesale and retail trade; hotels and catering; and transport and communications) and non-market services. Non-market services include public administration, education, health and other public services (including arts, entertainment and recreation).

Over the next five years, consumer spending is expected to grow much faster in the RGMs than in the advanced economies, as the number of middle-class households expands rapidly throughout the emerging world. As a result, demand for services will grow very strongly in coming years.

Figure 14
RGMs: sectoral growth



Source: Oxford Economics.

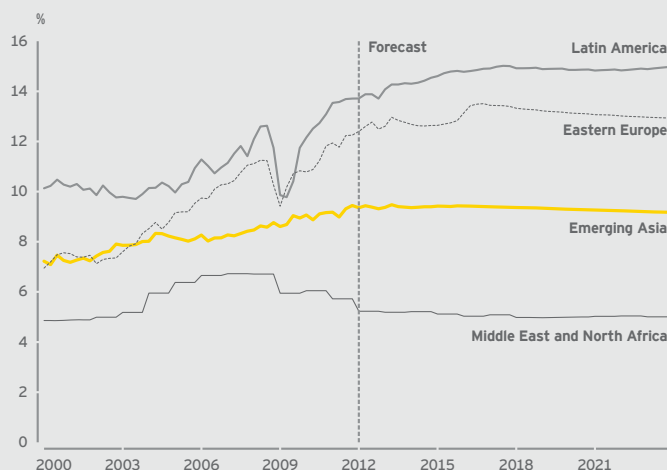
Perhaps due to the bulkiness of the components in heavy goods manufacturing and the associated high transport costs, trade flows in this sector tend to be quite localized. Last year, more than 85% of Brazil's road transport equipment exports went to neighboring countries in Latin America, and almost two thirds of Indonesia's went to the rest of Asia. As a result, currency volatility will have a limited impact on this sector.

But in manufacturing sectors where transportation is easier, trade flows tend to be more globalized. For example, around two thirds of Indonesia's exports of clothing, footwear and bags go outside of emerging Asia. This reflects strong demand from the US and Europe for these easily-packaged goods.

Food and beverages is another portable sector. Around 10% of Brazil's meat exports go to the rest of Latin America, the US or Canada. Nearly a third goes to the Middle East and North Africa, and over a quarter to Asia.

Transport equipment is one of the largest manufacturing sectors. It contributes nearly 15% of manufacturing in Latin America, more than 10% in Eastern Europe and almost 10% in emerging Asia.

Figure 15
Road transport as a proportion of the manufacturing sector



Source: Oxford Economics.

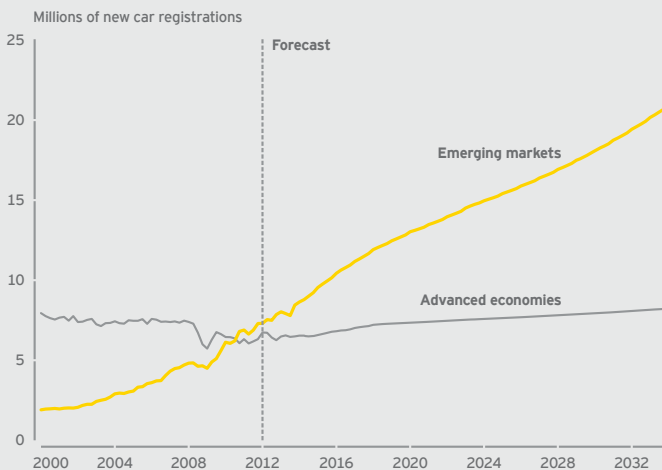
New challenges deepen need for reform

► Manufacturing, a key sector (continued)

Transport, a key sector for RGMs as consumers ...

Indeed, the chart below illustrates the growing importance of the transport sector for RGMs, as incomes rise and households begin to demand more consumer products. In 2010, for the first time ever, there were more registrations of new cars in the emerging markets than there were in the advanced economies. While the number of registrations will stay roughly constant in Japan over the next 10 years, it will more than double in China, India, Indonesia and Thailand. It will nearly double in Brazil, Russia, South Africa and Turkey. And by 2020, emerging markets will be producing more trucks than developed markets, reflecting the former's strong manufacturing growth.

Figure 16
Emerging markets: registrations of new cars

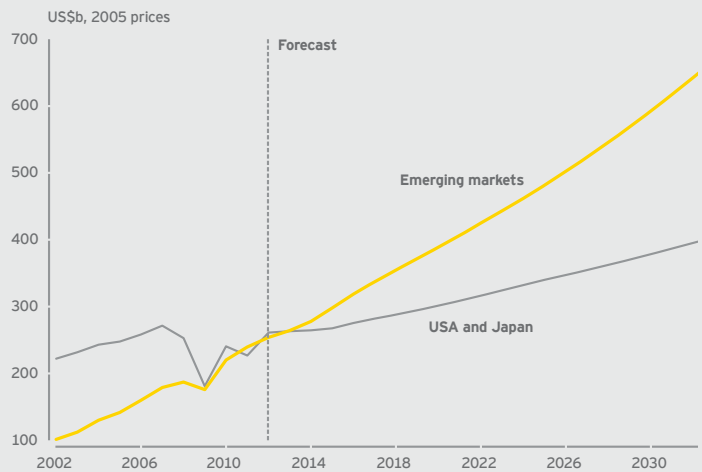


Source: Oxford Economics.

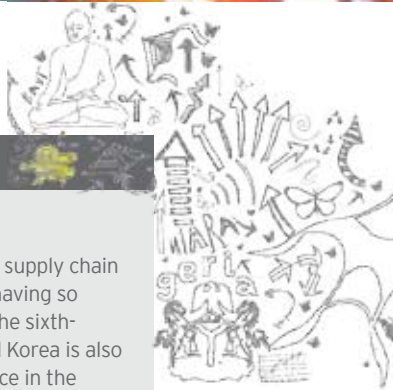
... and as fast-growing producers

In addition to being an increasingly important source of demand, many of the RGMs are also key producers. Last year, in another first, car production in the emerging markets outstripped production in Japan and the US combined. Seven of the RGMs were ranked among the top 10 producers of motor vehicles last year, namely China, Turkey, Mexico, Thailand, Korea, Indonesia and Brazil. Within 10 years, India and South Africa will join the top 10.

Figure 17
Motor vehicles and parts, value added output



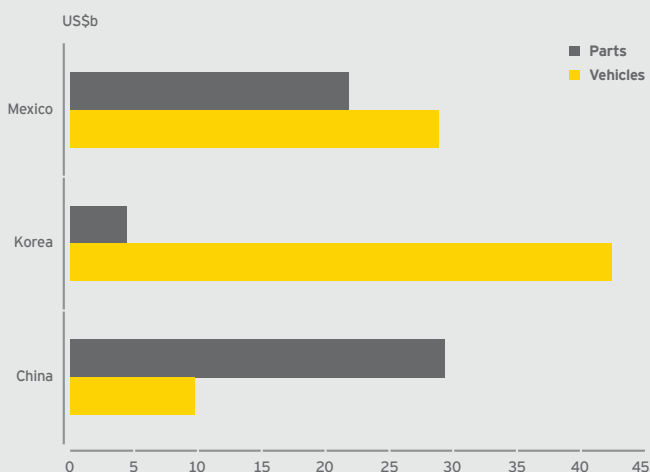
Source: Oxford Economics.



Asia benefits from specialization

In emerging Asia, countries play different roles in the global supply chain for road transport. This enables the region to benefit from having so many rapidly growing countries close together. Thailand is the sixth-largest producer of motor vehicles in the world by value and Korea is also a key producer. But both have a much smaller global presence in the market for vehicle parts and bodies. In contrast, China and India produce around twice as many parts for vehicles as they do final vehicles. Figure 18 illustrates this trend. For Mexico, and other large automobile producers, such as Turkey and Poland, the ratio of parts to final vehicles is more balanced than in Asia.

Figure 18
Exports of road transport equipment, 2012



Source: Oxford Economics.



Growth in the paper industry

What opportunities does the shift in the global economy present for the forest products, paper and packaging industry? Where can the greatest business opportunities be found? Should the industry focus on countries like Mexico, Colombia, South Africa, Turkey, Thailand, Vietnam and Indonesia?

Our answer to the last question is yes. And in our latest report, *Reaching out – opportunities in the new rapid-growth markets*, we offer companies that operate globally and locally insight on the macro-economic development and investment attractiveness of these seven rising stars.

Download the report at ey.com/FI/fi/Industries/Other-industry-sectors/Forest-Products--Paper-and-Packaging

Forecast for rapid-growth markets


25 rapid-growth markets

We define rapid-growth markets on the basis of three key criteria:

- ▶ Proven strong growth and future potential
- ▶ Size of the economy and population
- ▶ Strategic importance for business

Figure 19 shows the GDP growth of our 25 rapid-growth markets over the last 10 years, comparing these with the leading advanced economies. Together, they represent a significant proportion of the world economy (Figure 20).

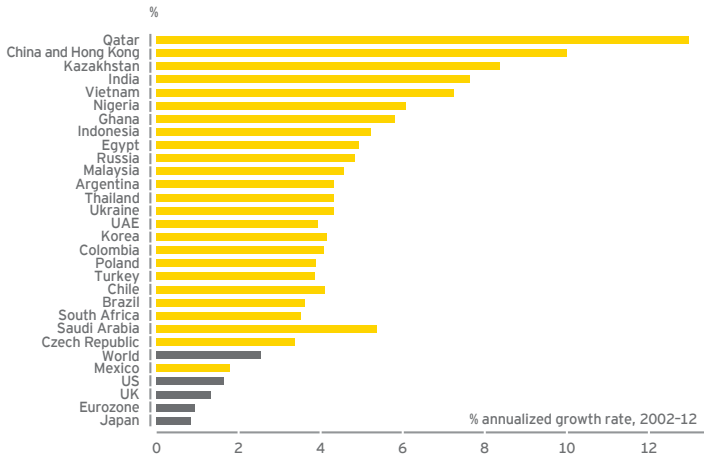
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Mainland China and Hong Kong
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Colombia
Czech Republic
Egypt
Ghana
India
Indonesia
Kazakhstan
Korea
Malaysia
Mexico
Nigeria
Poland
Qatar
Russia
Saudi Arabia
South Africa
Thailand
Turkey
Ukraine
United Arab Emirates
Vietnam

Figure 19

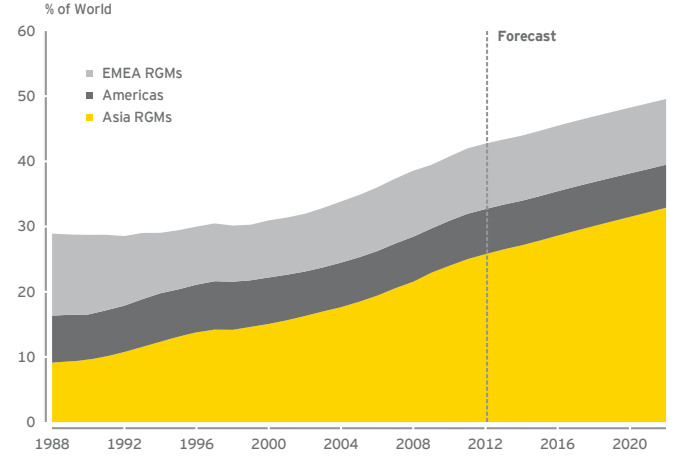
Real GDP growth 2002-12



Source: Oxford Economics.

Figure 20

Share of world GDP in PPP terms



Source: Oxford Economics.



Argentina



GDP growth

2014 1.4%

Agriculture prompts growth spurt, before retrenchment in 2014

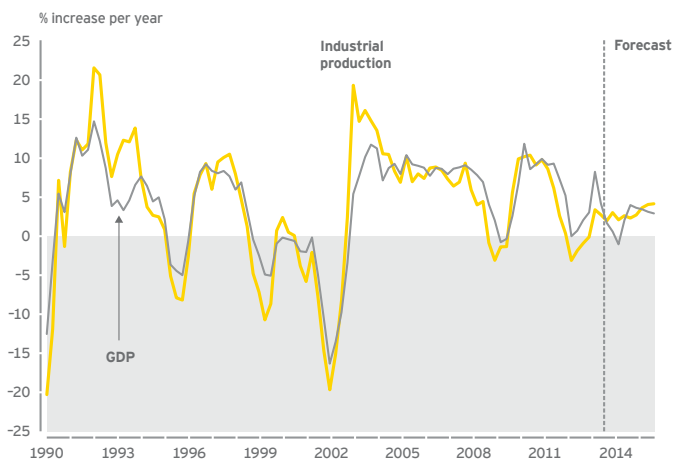
Our GDP growth forecast has jumped to 4.3% this year, compared with the 2.7% anticipated in our previous edition. Activity accelerated in H1 2013, as the economy benefited from a good soya harvest. This helped to boost both domestic demand and investment. However, preliminary industrial production data for August indicates that the economy will slow in the second half of the year. High inflation is reducing the country's international competitiveness, and we expect to see some weakening of

demand in Argentina's export markets in the coming months. Next year, therefore, growth is forecast to slip back to 1.4%, lower than the 1.9% recorded in 2012.

Argentina faces several structural challenges that must be overcome if it is to achieve its full growth potential. In the medium term, domestic activity will be held back by rising inflation and the impact of numerous policy-induced economic distortions. Some progress is being made.

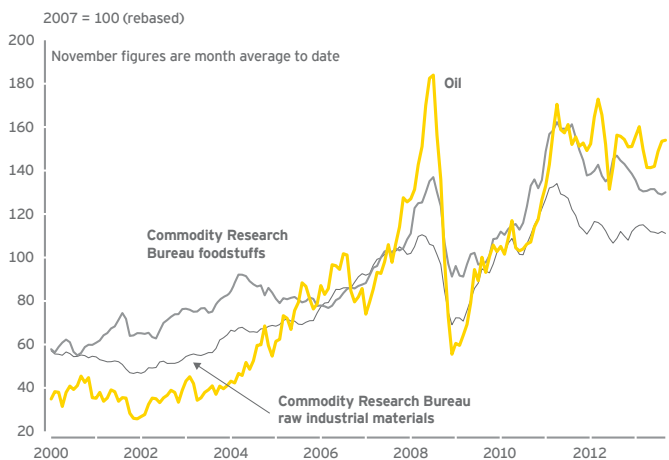
For example, in the oil sector, the Government is legislating to make conditions more flexible for companies wishing to repatriate earnings. But while inflationary pressures and policy distortions remain, annual growth is unlikely to exceed 3.5%. However, reform could raise potential growth above 4%, as the country is rich in natural resources and has a well-educated workforce.

Figure 21
GDP and industrial production



Source: Oxford Economics.

Figure 22
World: commodity prices



Source: Commodity Research Bureau; Haver Analytics.

| Argentina | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 1.9 | 4.3 | 1.4 | 3.3 | 3.3 | 3.1 |
| CPI inflation (% per year) | 10.0 | 10.7 | 11.0 | 9.8 | 9.5 | 9.0 |
| Current account balance (% of GDP) | -0.1 | -0.4 | -0.3 | -0.2 | -0.2 | -0.2 |
| External debt total (% of GDP) | 30.0 | 30.4 | 33.2 | 33.9 | 33.7 | 33.1 |
| Short-term interest rate (%) | 12.0 | 14.4 | 12.8 | 9.5 | 8.4 | 7.9 |
| Exchange per US\$ (year average) | 4.6 | 5.4 | 6.4 | 6.9 | 7.4 | 8.0 |
| Government balance (% of GDP) | -2.5 | -1.9 | -1.6 | -1.2 | -0.9 | -0.7 |
| Population (millions) | 41.1 | 41.5 | 41.8 | 42.2 | 42.5 | 42.9 |
| Nominal GDP (US\$b) | 475.1 | 476.5 | 456.3 | 476.5 | 500.9 | 526.5 |
| GDP per capita (US\$ current prices) | 11,549.7 | 11,483.0 | 10,904.6 | 11,291.6 | 11,775.4 | 12,279.3 |

Source: Oxford Economics.

Brazil



GDP growth

2014 **1.9%**

Less impetus from household spending

After growing by just 0.9% in 2012, Brazil's economy exceeded expectations by rising 1.5% on the quarter in Q2, following a 0.6% increase in Q1. This has prompted us to raise our forecast for 2013 GDP growth to 2.6%, up from the 2.4% envisaged three months ago. However, the pickup in Q2 could be short-lived as tighter policy will constrain activity.

Brazil remains hobbled by low growth and volatile inflation. Despite the Government's attempts to keep controlled prices at bay,

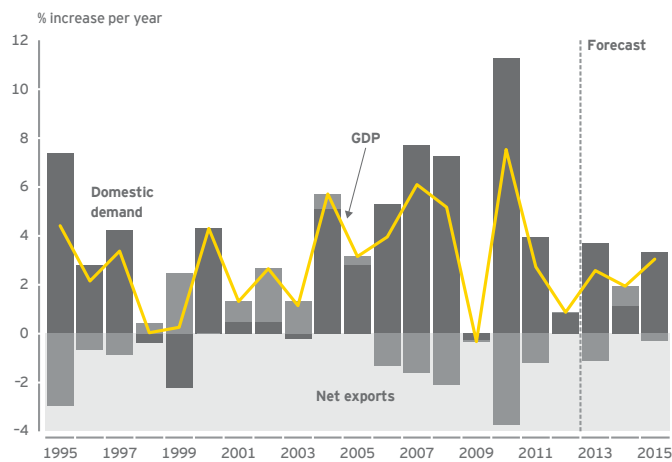
overall inflation is still close to the ceiling of the central bank's 4.5% +/-2% target. The central bank is expected to raise the Selic rate to 9.75% by the end of 2013.

We have observed a slowdown in consumer spending. This is mainly because, while real incomes grew significantly between 2000 and 2007, private credit surged and these consumers are now in the process of paying off debts. But in the longer term, reducing debt levels should enable a new cycle of stronger consumption growth.

The social unrest seen earlier this year has now calmed down. It is now seen as more of a reaction to corruption and misspending by the Government than a protest over economic issues. All of next year's presidential candidates have an incentive to promote reform, which could lead Brazil back toward 3.5% growth. If the country is able to improve its business environment and invest more in infrastructure, annual growth could hit 4%.

Figure 23

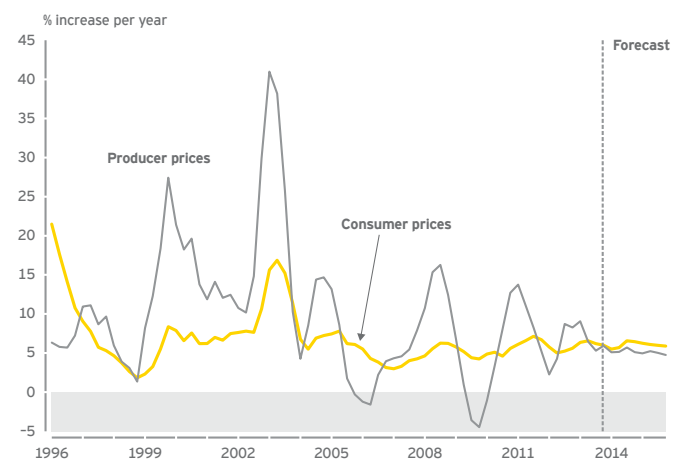
Contributions to GDP growth



Source: Oxford Economics.

Figure 24

Prices and earnings



Source: Oxford Economics.

Brazil

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 0.9 | 2.6 | 1.9 | 3.0 | 3.3 | 3.3 |
| CPI inflation (% per year) | 5.4 | 6.3 | 6.1 | 6.0 | 5.5 | 4.9 |
| Current account balance (% of GDP) | -2.4 | -3.6 | -2.8 | -2.3 | -2.2 | -2.2 |
| External debt total (% of GDP) | 13.6 | 13.8 | 13.8 | 14.0 | 14.1 | 14.2 |
| Short-term interest rate (%) | 8.5 | 8.2 | 9.7 | 9.7 | 8.9 | 7.9 |
| Exchange per US\$ (year average) | 2.0 | 2.2 | 2.4 | 2.5 | 2.5 | 2.6 |
| Government balance (% of GDP) | -2.5 | -3.1 | -3.7 | -3.3 | -3.2 | -3.5 |
| Population (millions) | 198.9 | 200.6 | 202.2 | 203.9 | 205.4 | 206.9 |
| Nominal GDP (US\$b) | 2,255.0 | 2,215.3 | 2,133.7 | 2,305.9 | 2,440.5 | 2,531.8 |
| GDP per capita (US\$ current prices) | 11,337.8 | 11,043.8 | 10,549.9 | 11,311.5 | 11,880.4 | 12,234.3 |

Source: Oxford Economics.

Chile



GDP growth

2014  4.9%

Growth set to slow to 4.6% this year ahead of steady recovery

The economy expanded by just 0.5% in Q2 2013, weighed down by contraction in the mining sector. We now expect GDP growth of 4.6% in 2013 as a whole. Strong private consumption, underpinned by rises in employment and real wages, helped to drive growth through H1 2013. However, we expect this to slow in the coming months, as real household income growth begins to moderate. Meanwhile, investment is dampened by weaker business confidence, deteriorating corporate lending conditions

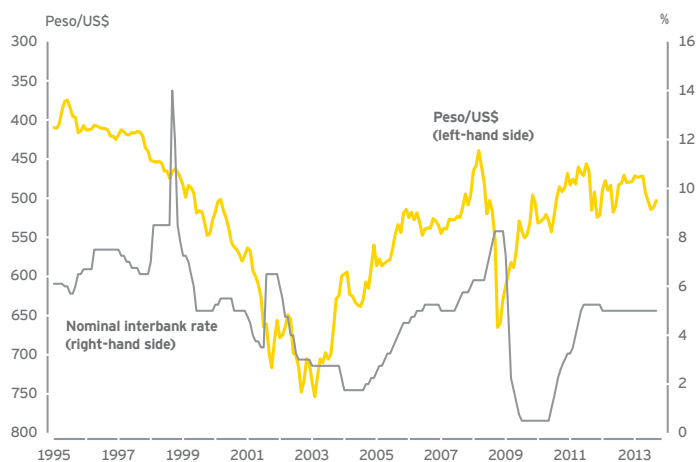
and sliding equity and copper prices. As a result, domestic spending is unlikely to be as robust in the coming quarters as it has been in recent years.

With inflation still well below the 3% target, the central bank has the scope to bolster the economy in the face of a subdued external outlook and the risk of a marked slowdown in domestic demand. We expect Chile's main policy rate to be cut to 4.75% in

Q4, which should help boost confidence and ease credit conditions.

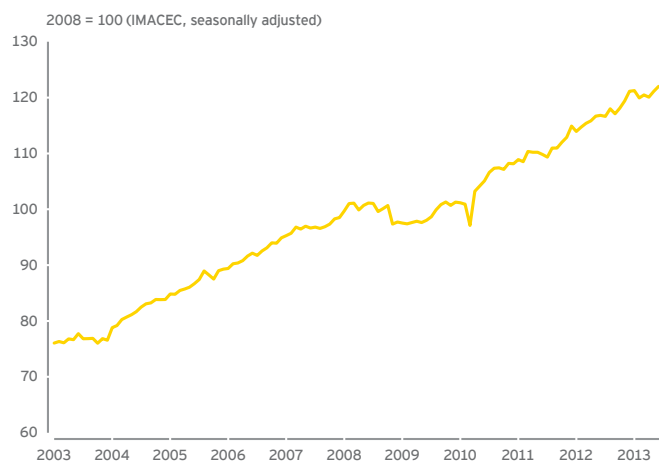
Macroeconomic and financial stability should help to promote investment, boost capacity and raise living standards over the long term. We expect the economy to grow by almost 5% in the medium term. However, our long-term growth target is subject to Chile overcoming a number of energy infrastructure constraints.

Figure 25
Exchange and interest rates



Source: Banco Central de Chile; Haver Analytics.

Figure 26
Monthly indicator of economic activity



Source: Haver Analytics.

| Chile | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 5.6 | 4.6 | 4.9 | 5.1 | 5.0 | 4.9 |
| CPI inflation (% per year) | 3.0 | 1.6 | 2.6 | 2.8 | 3.0 | 3.0 |
| Current account balance (% of GDP) | -3.5 | -2.9 | -2.7 | -2.1 | -1.4 | -0.8 |
| External debt total (% of GDP) | 37.5 | 37.8 | 37.2 | 36.1 | 35.0 | 33.5 |
| Short-term interest rate (%) | 5.0 | 4.9 | 4.6 | 5.6 | 5.8 | 5.8 |
| Exchange per US\$ (year average) | 486.5 | 492.2 | 502.7 | 508.6 | 514.0 | 516.4 |
| Government balance (% of GDP) | 0.6 | -0.6 | -0.4 | 0.1 | 0.4 | 0.2 |
| Population (millions) | 17.5 | 17.6 | 17.8 | 17.9 | 18.1 | 18.2 |
| Nominal GDP (US\$b) | 268.3 | 282.7 | 300.3 | 322.7 | 346.4 | 372.8 |
| GDP per capita (US\$ current prices) | 15,342.2 | 16,024.6 | 16,876.0 | 17,983.5 | 19,146.0 | 20,442.2 |

Source: Oxford Economics.

Mainland China and Hong Kong special administrative region (SAR)



GDP growth

2014



7.1%

China regains momentum

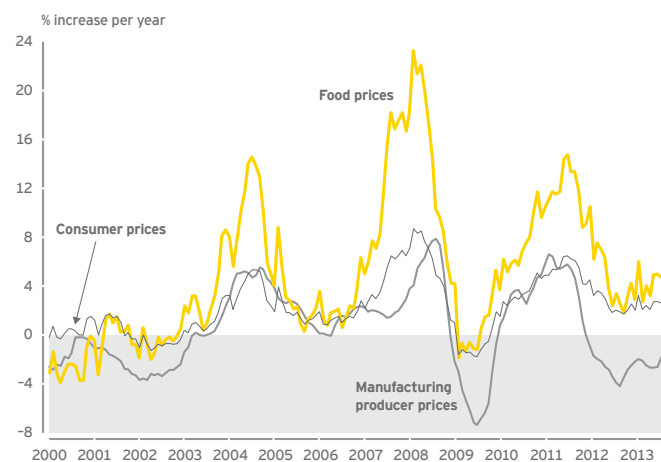
China's economy has picked up steam in Q3. In August, industrial production rose by 10.4% on the year, the fastest annual rate since March 2012. The official manufacturing PMI suggests that this strength continued in September with domestic new orders rising to 52.8, the highest since April last year. Retail sales have grown steadily. As a result, we now expect growth of 7.4% in 2013, close to the Government's target of 7.5%.

Some of the pickup reflects the strong growth in credit at the beginning of this year, as well as some of the fiscal measures taken to support small businesses, such as tax cuts. Actual credit growth has now slowed significantly and this will have more of an impact on investment. So investment and GDP growth are both set to slow, and we expect growth closer to 7% next year.

Hong Kong's exports have gained strength but Hong Kong remains very exposed to

financial markets. The Hang Seng fell sharply in May and June but it has rallied recently. In addition, property prices have moderated in response to government measures to cool the market. The Shanghai Free Trade Zone is now open. And as China's economy matures, increasing demand for financial services could help to drive growth in Hong Kong and the Mainland close to 7% over the medium term.

Figure 27
Inflation



Source: China Bureau of Statistics; Haver Analytics.

Figure 28
Hong Kong: stock market



Source: Hang Seng Index Services Limited; Haver Analytics.

| Mainland China | | | | | | |
|--------------------------------------|---------|---------|----------|----------|----------|----------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Real GDP growth (% per year) | 7.7 | 7.4 | 7.1 | 7.3 | 7.5 | 7.4 |
| CPI inflation (% per year) | 2.6 | 2.5 | 2.9 | 2.9 | 3.0 | 3.0 |
| Current account balance (% of GDP) | 2.3 | 3.3 | 3.1 | 3.0 | 2.8 | 2.7 |
| External debt total (% of GDP) | 9.2 | 9.3 | 9.1 | 8.9 | 8.7 | 8.5 |
| Short-term interest rate (%) | 4.6 | 4.7 | 4.5 | 4.5 | 4.8 | 5.0 |
| Exchange per US\$ (year average) | 6.3 | 6.2 | 6.0 | 5.8 | 5.7 | 5.5 |
| Government balance (% of GDP) | -0.8 | -1.1 | -1.6 | -2.0 | -1.9 | -1.8 |
| Population (millions) | 1,372.3 | 1,380.8 | 1,389.1 | 1,397.0 | 1,404.6 | 1,412.1 |
| Nominal GDP (US\$b) | 8,233.4 | 9,082.9 | 10,273.5 | 11,692.2 | 13,282.4 | 15,088.4 |
| GDP per capita (US\$ current prices) | 5,999.8 | 6,578.0 | 7,396.0 | 8,369.7 | 9,456.2 | 10,685.2 |

Source: Oxford Economics.

Colombia



GDP growth

2014



4.0%

Mining to drive long-term growth, helped by FDI and public spending

We expect Colombia's economy to grow 3.7% this year. This rate is ahead of the regional average, but slightly slower than in 2012. Activity continues to be supported by expansionary fiscal and monetary policy.

The central bank cut its key policy rate by 100bp in Q1, to 3.25%. The aim was to help boost the economy in the face of sluggish world growth. Inflation remains low, recording just 2.3% in September – well within the 2%-4% target range. Monetary

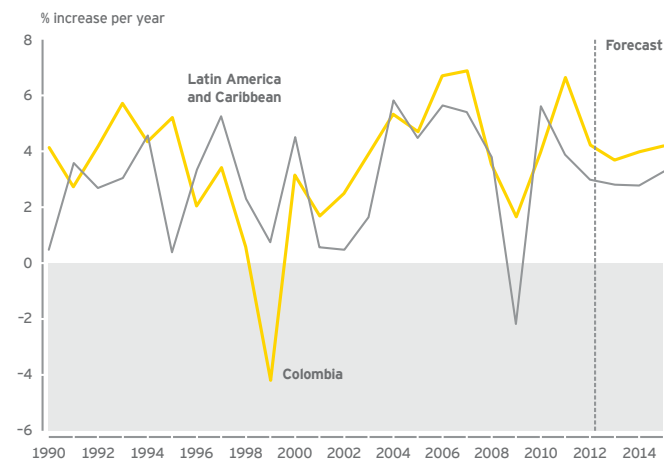
policy is likely to remain loose, even if currency falls put upward pressure on prices. The exchange rate depreciated by 5%-10% against the US dollar from the start of the year to the end of September.

Next year, pre-election spending will continue to support activity, helping to secure growth of 4%. The Government has already announced a 5.8% rise in budgeted spending, with infrastructure likely to see a major boost.

Foreign investment in oil, coal and mineral extraction is rising. This will fund exploration and development. These activities account for two-thirds of exports, so should help bolster the economy – especially as world trade begins to pick up again later this year. And a successful outcome to peace negotiations between the Government and the FARC guerrilla group would boost confidence and output.

Figure 29

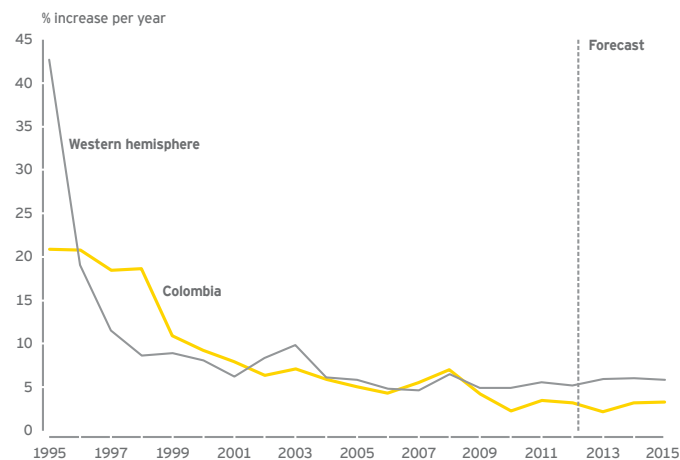
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 30

Inflation



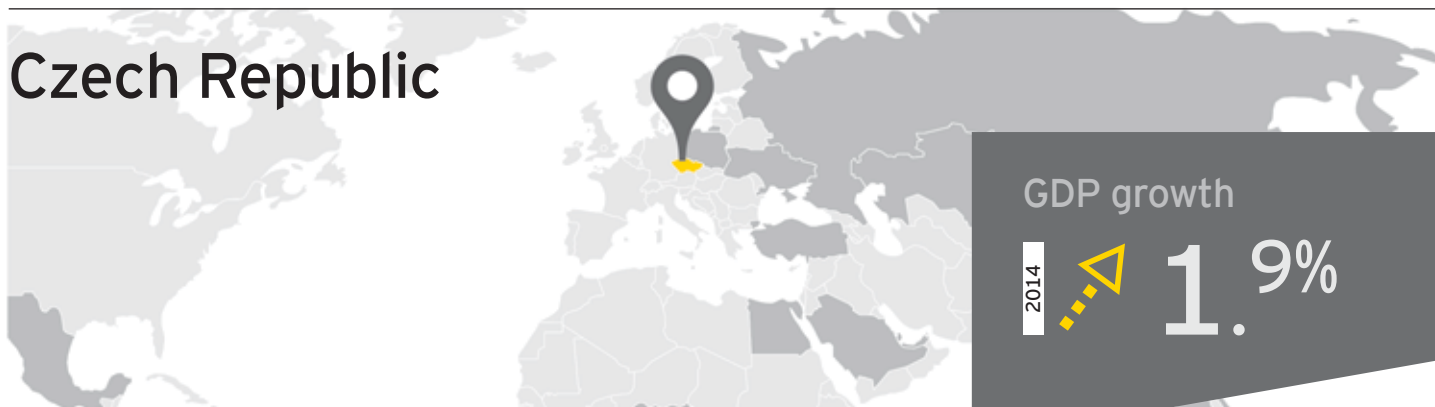
Source: Oxford Economics; Haver Analytics.

Colombia

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 4.2 | 3.7 | 4.0 | 4.2 | 4.0 | 4.0 |
| CPI inflation (% per year) | 3.2 | 2.2 | 3.2 | 3.3 | 3.3 | 3.3 |
| Current account balance (% of GDP) | -3.2 | -3.6 | -3.9 | -4.1 | -4.2 | -4.2 |
| External debt total (% of GDP) | 21.6 | 24.1 | 27.1 | 29.8 | 32.3 | 34.2 |
| Short-term interest rate (%) | 5.0 | 3.4 | 4.3 | 5.5 | 6.5 | 6.9 |
| Exchange per US\$ (year average) | 1,796.9 | 1,870.2 | 2,000.0 | 2,109.6 | 2,195.0 | 2,258.1 |
| Government balance (% of GDP) | -1.9 | -2.8 | -2.6 | -2.5 | -2.2 | -2.0 |
| Population (millions) | 47.5 | 48.1 | 48.8 | 49.4 | 49.9 | 50.5 |
| Nominal GDP (US\$b) | 369.8 | 377.3 | 378.7 | 386.4 | 399.0 | 416.7 |
| GDP per capita (US\$ current prices) | 7,781.6 | 7,838.6 | 7,767.7 | 7,828.0 | 7,991.4 | 8,252.1 |

Source: Oxford Economics.

Czech Republic



GDP growth

2014



1.9%

Recession over, but acceleration must wait till 2014

Our GDP forecast remains unchanged at a 1% decline in 2013. A stronger-than-expected GDP pickup in Q2 dragged the economy from a recession that started in 2011. However, net trade was the only positive component. This suggests that the remainder of 2013 is likely to be weak, constrained by high unemployment and fiscal austerity.

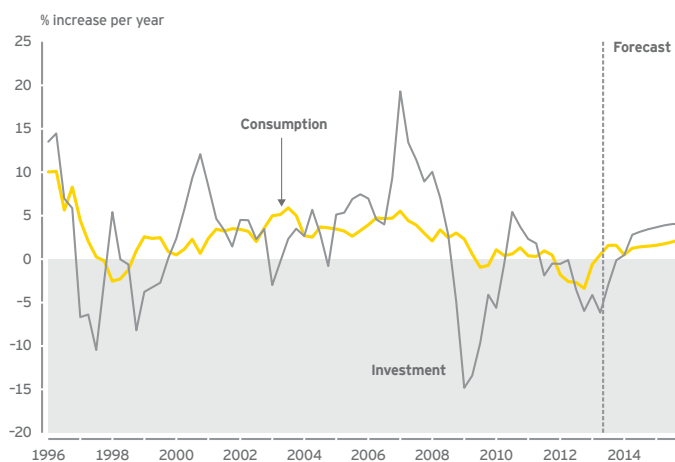
foreign demand improves. An upside risk to our forecast comes from a possible increase in public spending on infrastructure and housing. EU funds could help with this, as could an easing of austerity measures after October's elections. This impetus is especially welcome because the key policy rate is already 0.05% and cannot be cut further to stimulate activity.

almost 87% of GDP in 2012. We expect exports to pick up over the medium term as demand from the Eurozone improves, albeit at a moderate pace. Capacity constraints and slower labor productivity growth mean that, over the medium term, exports are unlikely to repeat gains in market share. As a result, GDP is set to grow by just over 2.5% on average in 2015-17, below pre-crisis levels.

Economic activity will pick up only from 2014, when austerity pressures ease and

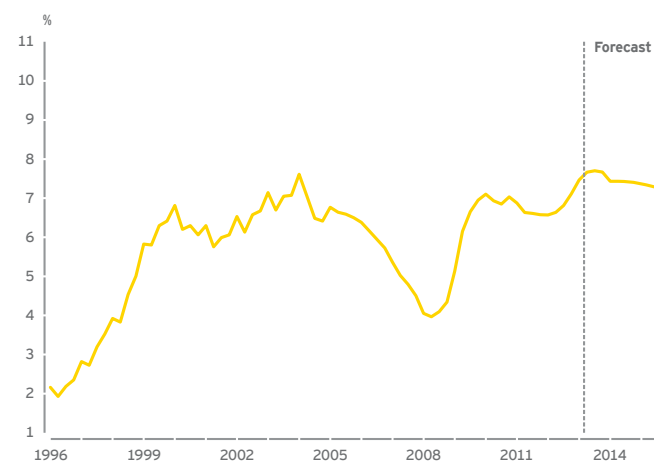
The Czech economy remains very dependent on exports. They accounted for

Figure 31
Consumption and investment



Source: Oxford Economics.

Figure 32
Unemployment



Source: Oxford Economics.

Czech Republic

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | -0.9 | -1.0 | 1.9 | 2.6 | 3.0 | 3.0 |
| CPI inflation (% per year) | 3.3 | 1.5 | 1.7 | 2.0 | 2.1 | 2.1 |
| Current account balance (% of GDP) | -2.4 | -1.4 | -3.1 | -3.4 | -3.3 | -2.8 |
| External debt total (% of GDP) | 50.6 | 51.6 | 53.9 | 55.3 | 55.3 | 54.7 |
| Short-term interest rate (%) | 1.0 | 0.5 | 0.5 | 0.7 | 1.2 | 1.7 |
| Exchange per US\$ (year average) | 19.6 | 19.5 | 20.3 | 21.6 | 21.9 | 21.9 |
| Government balance (% of GDP) | -2.6 | -2.9 | -2.9 | -2.8 | -2.6 | -2.3 |
| Population (millions) | 10.5 | 10.5 | 10.5 | 10.5 | 10.5 | 10.5 |
| Nominal GDP (US\$b) | 196.5 | 198.2 | 197.4 | 195.2 | 202.5 | 212.8 |
| GDP per capita (US\$ current prices) | 18,705.0 | 18,862.3 | 18,781.1 | 18,579.2 | 19,300.2 | 20,299.2 |

Source: Oxford Economics.

Egypt



GDP growth

2014 **2.4%**

Activity improving despite political turmoil

Hopes of a political compromise between the military-backed government and the Muslim Brotherhood (MB) have been dashed, with the army violently suppressing the Brotherhood. A new 50-member panel has been charged with drafting final amendments to a new constitution containing only two (and non-MB) Islamists.

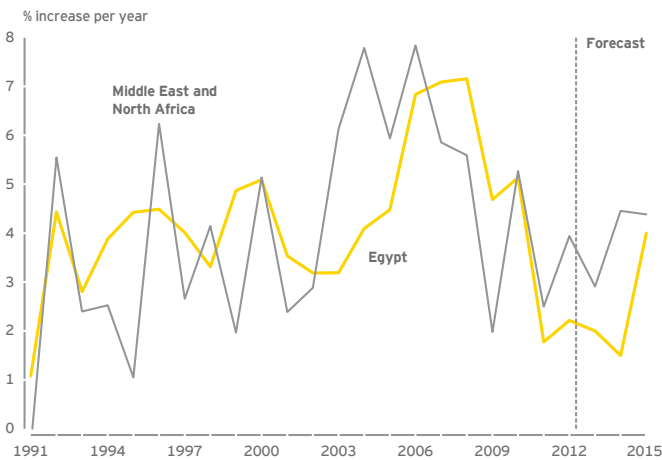
Nevertheless, the economy appears to have been largely resilient, as business sees the prospect of improved political and economic

stability. Notably, aid from the Gulf Cooperation Council helped reserves to hit a 21-month high of US\$18.9b at the end of August. This helped to stabilize the Egyptian pound and bring at least a temporary end to fuel shortages. However, since the uprising in early 2011, reserves have fallen by more than US\$20b. Along with delayed payments to oil companies, Egypt may also have to pay back some US\$2b to Qatar, with whom relations have deteriorated since the military intervention.

Against the backdrop of slow growth, weak policy implementation and high government spending, the budget deficit continues to widen. This crowds out funds for private sector investment. However, the emergency US\$3.2b economic stimulus plan, which focuses on investment projects, should support GDP growth of 2.4% in 2013-14. This compares with the 1.7% forecast in the previous edition.

Figure 33

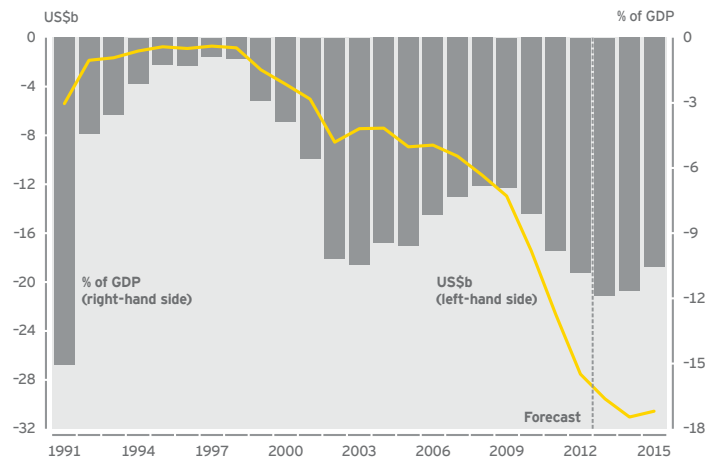
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 34

Government budget balance



Source: Oxford Economics.

Egypt

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 2.2 | 2.4 | 2.4 | 4.0 | 5.9 | 5.6 |
| CPI inflation (% per year) | 7.1 | 9.2 | 10.1 | 8.5 | 6.0 | 6.0 |
| Current account balance (% of GDP) | -3.6 | -1.7 | -2.5 | -2.8 | -2.6 | -2.7 |
| External debt total (% of GDP) | 15.0 | 16.4 | 16.3 | 15.6 | 15.0 | 14.3 |
| Short-term interest rate (%) | 13.0 | 12.3 | 11.5 | 10.0 | 9.0 | 8.0 |
| Exchange per US\$ (year average) | 6.1 | 6.9 | 7.3 | 7.5 | 7.7 | 7.9 |
| Government balance (% of GDP) | -10.8 | -13.8 | -11.6 | -10.5 | -9.7 | -9.2 |
| Population (millions) | 83.9 | 85.4 | 86.8 | 88.2 | 89.5 | 90.8 |
| Nominal GDP (US\$b) | 254.7 | 251.0 | 268.0 | 291.8 | 319.1 | 348.1 |
| GDP per capita (US\$ current prices) | 3,033.8 | 2,941.0 | 3,088.6 | 3,309.0 | 3,565.0 | 3,831.8 |

Source: Oxford Economics.

Ghana



GDP growth

2014 **6.1%**

Growth moves from spectacular to solid as oil boost fades

GDP growth slowed to 6.7% in Q1 2013 from 7.9% in 2012 and 15% in 2011, as the big boost from the start of oil production faded. Services are still growing strongly and agriculture is picking up, but the rise in oil output is leveling out and world gold prices are lower. We forecast solid GDP growth of about 6.5% in 2013 and then 5.5%-6% a year in 2014-17.

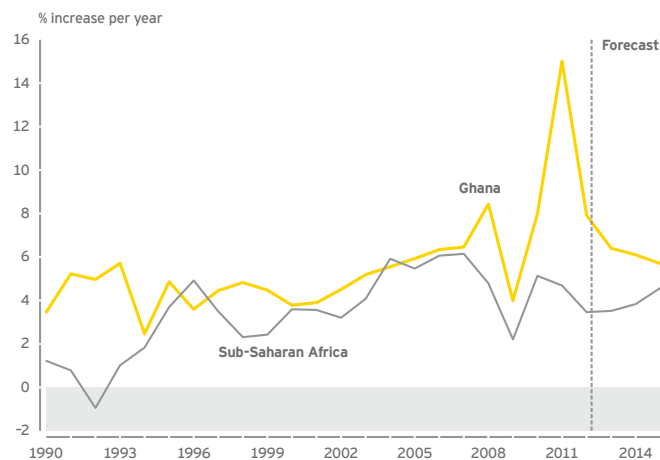
After falling into single digits in 2011 and 2012, inflation has risen, pushed up by high

world oil prices, cuts in fuel subsidies and heavy state spending ahead of the 2012 elections. In September 2013, the inflation rate was 11.9%. With price pressures persisting, the budget deficit rising and surging imports putting the Ghanaian cedi under downward pressure, the Bank of Ghana raised its key interest rate by 100bp to 16% in May 2013. It remains concerned about inflationary pressures following recent fuel and transport price rises.

The current account deficit rose to almost US\$5b (over 12% of GDP) in 2012. Despite a small decline in H1 2013, it will remain at around this level as world prices for oil and gold ease. Foreign exchange reserves remained modest at US\$5.8b in August, equal to a little over three months of imports. But with oil revenues set to climb over the medium term, we expect the current account deficit to fall to about 3.0% of GDP in 2017.

Figure 35

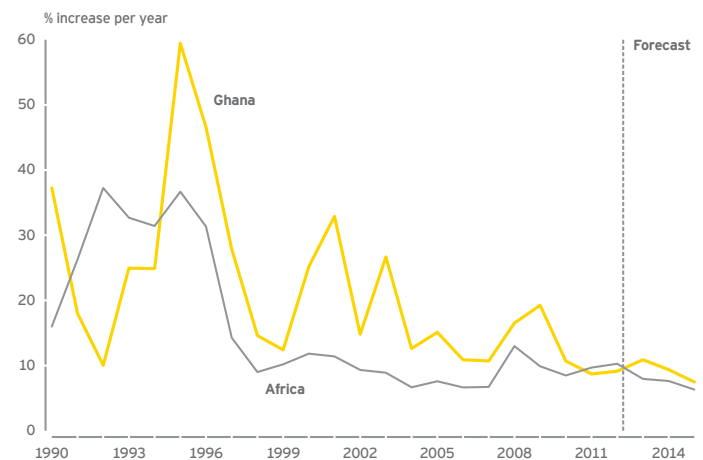
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 36

Inflation



Source: Oxford Economics; Haver Analytics.

| Ghana | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 7.9 | 6.4 | 6.1 | 5.7 | 5.4 | 5.0 |
| CPI inflation (% per year) | 9.2 | 10.9 | 9.4 | 7.5 | 6.0 | 5.2 |
| Current account balance (% of GDP) | -12.1 | -11.7 | -9.5 | -6.0 | -4.2 | -3.0 |
| External debt total (% of GDP) | 35.1 | 40.1 | 43.0 | 43.6 | 43.4 | 42.4 |
| Short-term interest rate (%) | - | - | - | - | - | - |
| Exchange per US\$ (year average) | 1.8 | 1.9 | 2.0 | 2.1 | 2.1 | 2.2 |
| Government balance (% of GDP) | -4.7 | -6.2 | -5.6 | -5.1 | -4.6 | -4.2 |
| Population (millions) | 25.6 | 26.1 | 26.7 | 27.3 | 27.9 | 28.5 |
| Nominal GDP (US\$b) | 40.7 | 44.5 | 49.6 | 54.7 | 59.7 | 64.7 |
| GDP per capita (US\$ current prices) | 1,592.5 | 1,700.6 | 1,856.5 | 2,004.2 | 2,137.5 | 2,270.3 |

Source: Oxford Economics.

India



Medium-term outlook weakens

India's GDP rose 4.4% year-on-year in Q2 2013, which was weaker than expected and the lowest rate of growth since Q1 2009. And with disappointing developments both at home and abroad, we have lowered our growth forecast significantly. We now expect GDP to expand 4.1% in 2013 and 4.5% in 2014. These projections compare with our previous estimates of 5.1% and 6.4% respectively. Growth is then expected to remain below 7% in 2015-17.

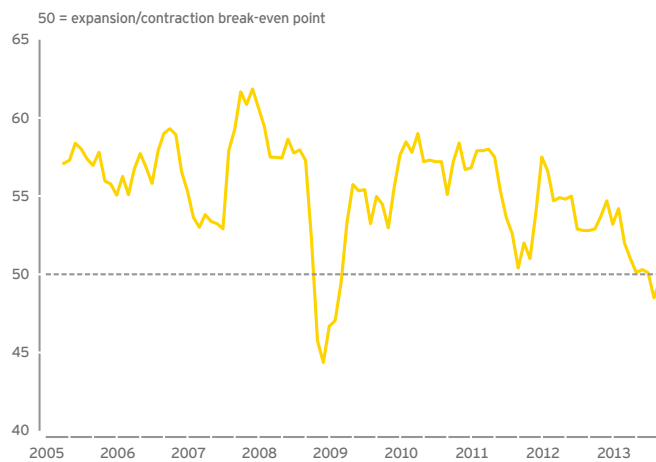
Large outflows of capital and a sharp depreciation in the currency – triggered by the US Federal Reserve's remarks in May about potentially scaling back its quantitative easing program – will continue to drag on the economy in the medium term. As a consequence, monetary policy will remain relatively tight. However, to support the rupee, the central bank has announced a window in which foreign currency non-resident US dollar fund swaps

will be allowed, enabling banks to convert US dollar deposits by Indians abroad.

India urgently needs to push through structural reforms if it is to achieve its long-term growth target of 8% per year. And decisive economic action is required on issues such as subsidy cuts and the liberalization of FDI.

Figure 37

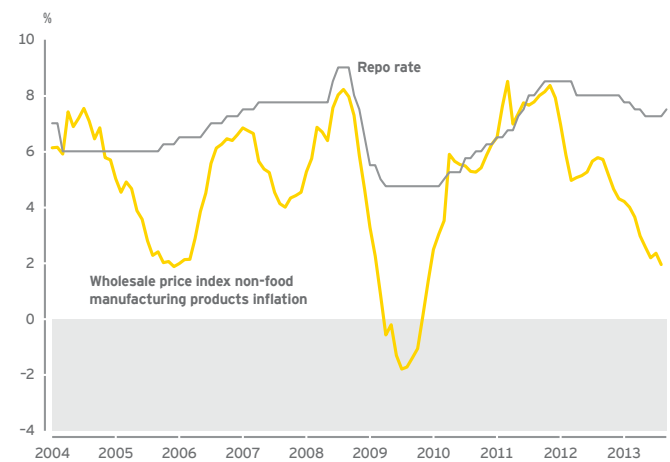
HSBC manufacturing purchasing managers' index (PMI)



Source: Markit.

Figure 38

Interest rate and wholesale price index inflation



Source: Oxford Economics.

| India | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 5.1 | 4.1 | 4.5 | 5.9 | 6.3 | 6.6 |
| CPI inflation (% per year) | 7.5 | 6.0 | 5.3 | 4.6 | 4.1 | 4.0 |
| Current account balance (% of GDP) | -5.0 | -3.9 | -4.9 | -4.7 | -3.5 | -2.6 |
| External debt total (% of GDP) | 19.4 | 19.8 | 19.4 | 17.5 | 15.6 | 14.2 |
| Short-term interest rate (%) | 9.5 | 9.4 | 7.7 | 7.7 | 7.8 | 7.7 |
| Exchange per US\$ (year average) | 53.5 | 58.7 | 64.0 | 64.8 | 64.6 | 65.7 |
| Government balance (% of GDP) | -5.6 | -5.5 | -4.1 | -3.2 | -2.6 | -2.2 |
| Population (millions) | 1,249.0 | 1,265.0 | 1,280.7 | 1,296.1 | 1,311.2 | 1,326.2 |
| Nominal GDP (US\$b) | 1,827.2 | 1,863.5 | 1,942.2 | 2,193.5 | 2,512.4 | 2,808.2 |
| GDP per capita (US\$ current prices) | 1,463.0 | 1,473.2 | 1,516.5 | 1,692.4 | 1,916.1 | 2,117.6 |

Source: Oxford Economics.

Indonesia



GDP growth

2014  5.4%

Domestic activity holds up as elections bear on reform agenda

Indonesia is facing slowing growth, sharply rising inflation, a falling exchange rate for the Indonesian rupiah (IDR) and a widening current account deficit. With elections due next year, the first priority for the authorities is to curb inflation, which has squeezed real incomes. Since June, interest rates have risen by a combined 150bp to 7.25%.

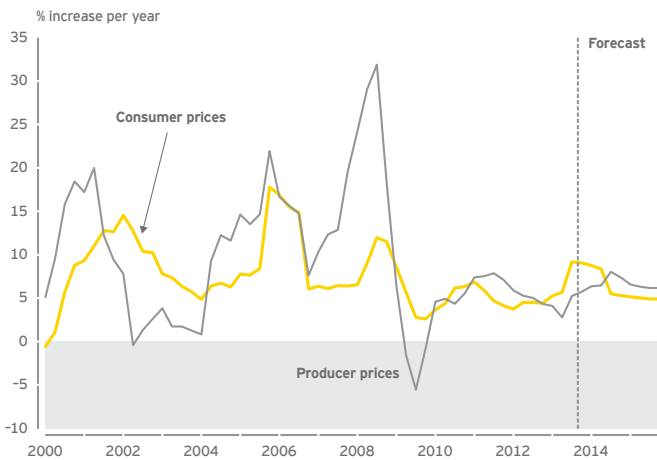
But the IDR has continued to depreciate. We expect the currency to settle in Q4 2013 as stronger global demand should help to stabilize the external deficit. However, a sharper fall in the IDR would increase inflationary pressures and slow growth.

To help maintain reasonable momentum in domestic activity, the Government will introduce more fiscal stimulus in the coming months. The Government has said that the

IDR18.4t of savings it expects to make from the fuel subsidy cut will go toward the 2014 budget. But there is a risk that reform efforts could be delayed by next year's elections.

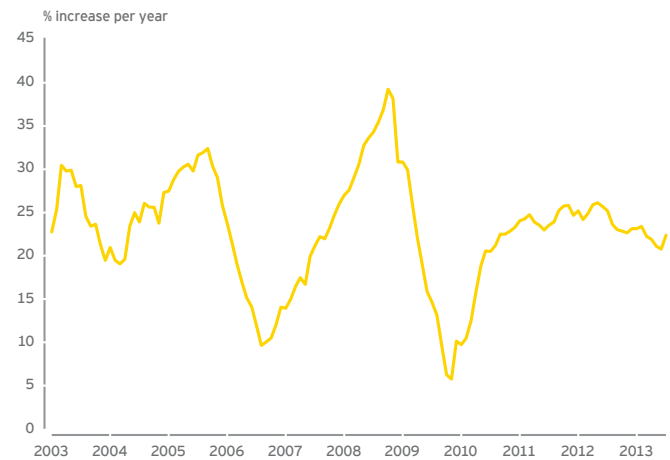
We have lowered our GDP growth forecasts slightly, from 6.1% to 5.6% for 2013 and from 6.0% to 5.4% for 2014. Strong domestic fundamentals should support medium-term growth above 5.5%.

Figure 39
Inflation



Source: Oxford Economics.

Figure 40
Bank lending growth



Source: Bank Indonesia; Haver Analytics.

| Indonesia | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 6.2 | 5.6 | 5.4 | 5.9 | 5.6 | 5.4 |
| CPI inflation (% per year) | 4.3 | 7.0 | 6.7 | 5.0 | 4.7 | 4.5 |
| Current account balance (% of GDP) | -2.8 | -3.7 | -2.9 | -2.6 | -2.8 | -2.5 |
| External debt total (% of GDP) | 27.5 | 28.6 | 25.5 | 22.8 | 20.9 | 19.4 |
| Short-term interest rate (%) | 4.7 | 5.8 | 7.3 | 7.8 | 7.8 | 7.8 |
| Exchange per US\$ (year average) | 9,403.2 | 10,336.1 | 10,445.1 | 10,338.1 | 10,443.0 | 10,592.3 |
| Government balance (% of GDP) | -1.8 | -1.4 | -0.8 | -0.6 | -0.6 | -0.5 |
| Population (millions) | 237.7 | 240.0 | 242.3 | 244.5 | 246.6 | 248.6 |
| Nominal GDP (US\$b) | 876.4 | 888.2 | 988.3 | 1,108.8 | 1,213.9 | 1,319.0 |
| GDP per capita (US\$ current prices) | 3,687.5 | 3,700.8 | 4,079.5 | 4,535.7 | 4,923.2 | 5,305.4 |

Source: Oxford Economics.

Kazakhstan



GDP growth

2014 **6.5%**

Oil and global demand boost growth prospects

Near-term growth prospects have been improved by the news that oil has been produced from the Kashagan field. The first export sales could come in October, although it is not clear how quickly output will ramp up to its phase 1 level of 180,000 barrels per day (b/d). Under phase 2, output would rise to 370,000 b/d, giving a substantial boost to current national output of 1.6m b/d.

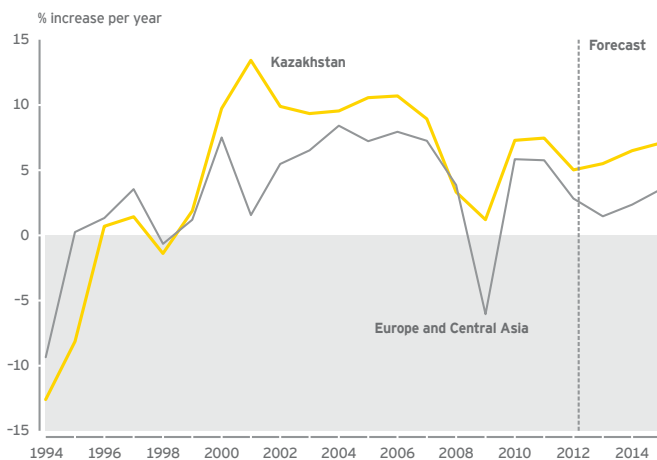
This news, plus the announcement that Kazakhstan and China have signed 22 agreements worth a total of US\$30b, notably relating to oil and gas, reinforces our belief that GDP growth will accelerate from 5.0% in 2012 to 5.5% this year and 6.5% in 2014. Industrial and construction growth are rising, albeit from a low base, while the service sector continues to expand robustly. We expect the economy to grow by 7% during 2015-17. In the longer

term, growth will settle to around 6% as infrastructure spending slows.

Kazakhstan has joined Russia in pegging its currency to a basket of currencies instead of a managed float with the US dollar. The aim is to deter speculators and better reflect trading patterns. This move could be an intermediate step toward a more flexible floating corridor arrangement.

Figure 41

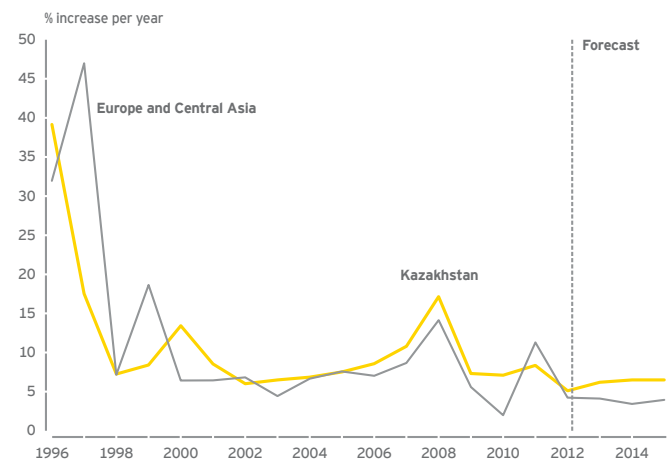
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 42

Inflation



Source: Oxford Economics; World Bank.

Kazakhstan

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 5.0 | 5.5 | 6.5 | 7.1 | 6.7 | 6.3 |
| CPI inflation (% per year) | 5.1 | 6.2 | 6.5 | 6.5 | 6.2 | 6.0 |
| Current account balance (% of GDP) | 3.8 | 1.2 | 1.4 | 1.8 | 2.3 | 2.8 |
| External debt total (% of GDP) | 68.3 | 60.3 | 52.5 | 45.2 | 39.3 | 34.4 |
| Short-term interest rate (%) | 2.4 | 3.5 | 4.7 | 5.7 | 6.5 | 7.0 |
| Exchange per US\$ (year average) | 149.1 | 152.2 | 158.0 | 162.7 | 167.6 | 172.7 |
| Government balance (% of GDP) | -3.0 | -2.6 | -2.5 | -2.5 | -2.6 | -2.7 |
| Population (millions) | 16.4 | 16.5 | 16.7 | 16.9 | 17.0 | 17.2 |
| Nominal GDP (US\$b) | 200.5 | 215.7 | 235.6 | 260.9 | 287.2 | 314.2 |
| GDP per capita (US\$ current prices) | 12,246.9 | 13,037.3 | 14,097.9 | 15,452.8 | 16,850.0 | 18,263.1 |

Source: Oxford Economics.

Korea



GDP growth

2014



2.9%

Fiscal stimulus gives short-term glow, but prospects for 2014 darken

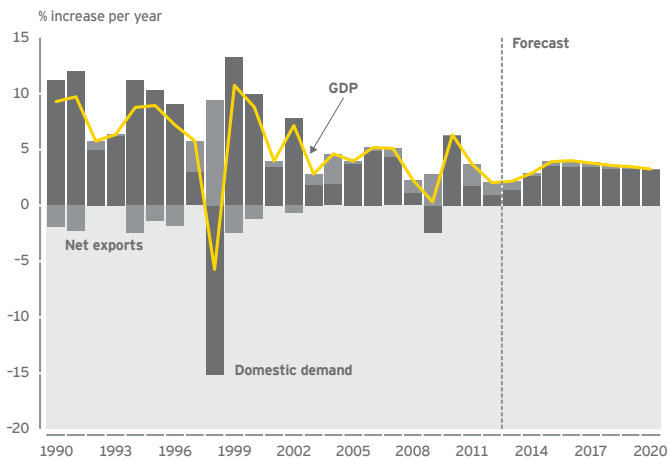
Although quarterly GDP growth in Korea was surprisingly strong in both Q1 and Q2, it was the result of a sharp fiscal stimulus rather than a pickup in the underlying economic drivers. Private investment and consumption were sluggish in H1, while export volumes rose modestly. As firms become more confident about prospects for the world economy, these areas of spending will gain momentum. However, the improvement will be gradual.

Indeed, the latest monthly data has been patchy. Although estimated seasonally adjusted exports rose strongly in August and employment has continued to rise, the manufacturing PMI fell in August and September, and the inventories-to-shipments ratio jumped up in July. In addition, the Korean won (KRW) has been one of the stronger Asian currencies this year. Sales to Japan have clearly been affected by the KRW's sharp appreciation against the Japanese yen.

Given this mixed picture, we expect the pace of growth to be modest in H2, resulting in GDP growth of 2.2% in 2013 as a whole. Growth should speed up in 2014 as consumers and firms feel more inclined to spend. But the acceleration will be significantly less rapid than we expected in July given our more cautious forecasts on the Chinese economy and the strength of world trade.

Figure 43

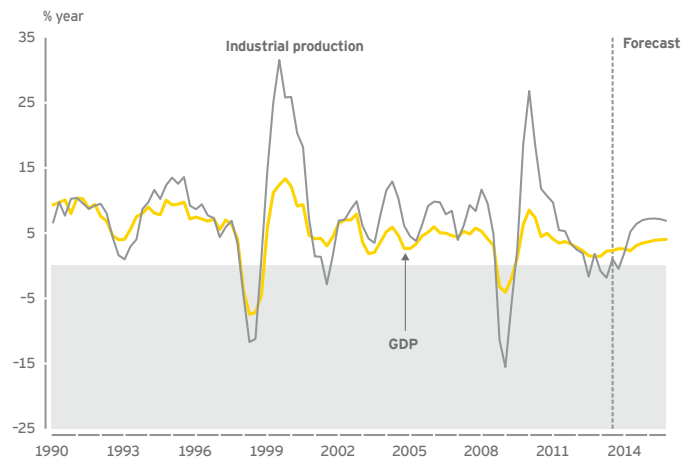
Contributions to GDP growth



Source: Oxford Economics.

Figure 44

GDP and industrial production

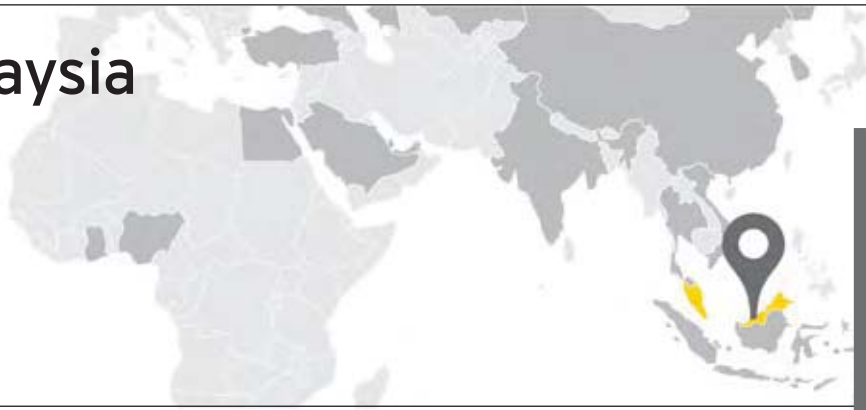


Source: Oxford Economics.

| Korea | | | | | | |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Real GDP growth (% per year) | 2.0 | 2.2 | 2.9 | 3.9 | 4.0 | 3.7 |
| CPI inflation (% per year) | 2.2 | 1.3 | 2.5 | 2.8 | 2.6 | 2.5 |
| Current account balance (% of GDP) | 3.8 | 5.5 | 4.3 | 2.7 | 1.8 | 1.2 |
| External debt total (% of GDP) | 36.8 | 34.5 | 32.9 | 30.8 | 28.9 | 27.1 |
| Short-term interest rate (%) | 3.3 | 2.7 | 2.7 | 3.5 | 4.5 | 4.7 |
| Exchange per US\$ (year average) | 1,126.8 | 1,102.3 | 1,095.4 | 1,088.0 | 1,080.2 | 1,073.3 |
| Government balance (% of GDP) | 1.4 | -1.3 | -0.9 | -0.5 | -0.3 | -0.2 |
| Population (millions) | 48.8 | 48.9 | 49.1 | 49.2 | 49.3 | 49.3 |
| Nominal GDP (US\$b) | 1,129.8 | 1,192.2 | 1,251.9 | 1,335.5 | 1,426.6 | 1,520.2 |
| GDP per capita (US\$ current prices) | 23,144.8 | 24,357.1 | 25,516.0 | 27,163.9 | 28,964.3 | 30,817.7 |

Source: Oxford Economics.

Malaysia



GDP growth

2014



4.8%

Growth prospects limited by weak domestic demand

GDP grew by 4.3% year-on-year in Q2, up slightly from the 4.1% posted in Q1. Strong growth in government and household spending offset a sharp deceleration in investment and continued weakness in exports.

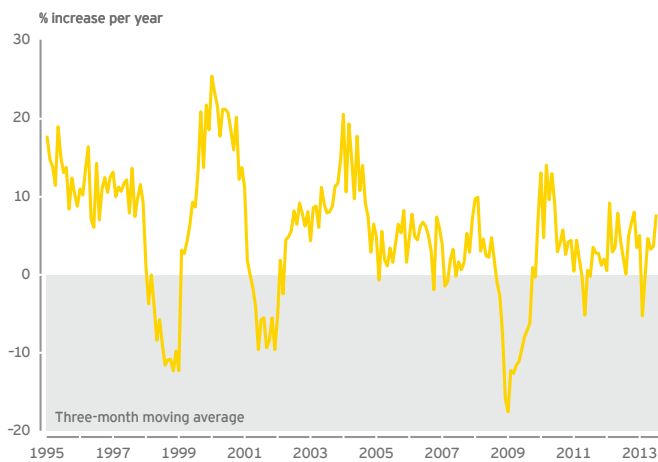
Early indications suggest that growth in Q3 will pick up from the lackluster pace in H1. In July, estimated seasonally adjusted exports recorded their strongest monthly

rise in 10 months, supporting a substantial 2.2% monthly rise in industrial production (up 7.5% on the year).

Concern over the size of the budget deficit, a falling trade surplus and the prospect of less accommodative US monetary policy have led to pressure on the Malaysian ringgit (MYR). As a result, we do not expect the central bank to raise its key interest rate.

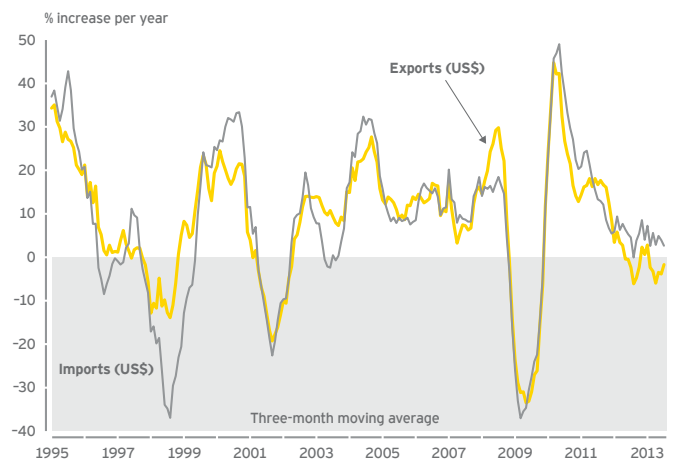
While a modest recovery in exports is expected, the outlook for domestic demand is softer. As the Government attempts to trim the budget deficit, we expect a consumption tax to be introduced next year and a number of public investment projects to be postponed. Consequently, while our forecast for growth this year is little changed, our 2014 forecast has been lowered to 4.8% from 5.7% in the previous edition.

Figure 45
Industrial production



Source: Department of Statistics.

Figure 46
Exports and imports



Source: Department of Statistics.

| Malaysia | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 5.6 | 4.4 | 4.8 | 4.4 | 4.5 | 4.3 |
| CPI inflation (% per year) | 1.7 | 1.9 | 3.0 | 3.2 | 3.0 | 3.0 |
| Current account balance (% of GDP) | 6.1 | 3.7 | 4.1 | 3.9 | 4.1 | 4.2 |
| External debt total (% of GDP) | 34.4 | 37.8 | 38.5 | 37.6 | 37.8 | 38.0 |
| Short-term interest rate (%) | 3.0 | 3.1 | 3.2 | 3.7 | 3.6 | 3.6 |
| Exchange per US\$ (year average) | 3.1 | 3.2 | 3.2 | 3.1 | 3.1 | 3.1 |
| Government balance (% of GDP) | -4.4 | -4.7 | -3.5 | -3.4 | -3.8 | -3.8 |
| Population (millions) | 28.8 | 29.3 | 29.7 | 30.1 | 30.5 | 30.9 |
| Nominal GDP (US\$b) | 305.1 | 310.2 | 332.7 | 370.0 | 399.0 | 427.9 |
| GDP per capita (US\$ current prices) | 10,579.0 | 10,600.1 | 11,210.7 | 12,296.8 | 13,082.7 | 13,845.6 |

Source: Oxford Economics.

Mexico



Sharp slowdown hits growth outlook

Mexico's economy slowed sharply in the first half of 2013, with GDP contracting 0.7% in Q2 after stagnating in Q1. Weak domestic demand was the main reason for the contraction in Q2, with consumption falling 0.8% and investment down 1.9%. As a result, we have downgraded our forecast for GDP growth substantially, and now expect the economy to expand 1.2% this year.

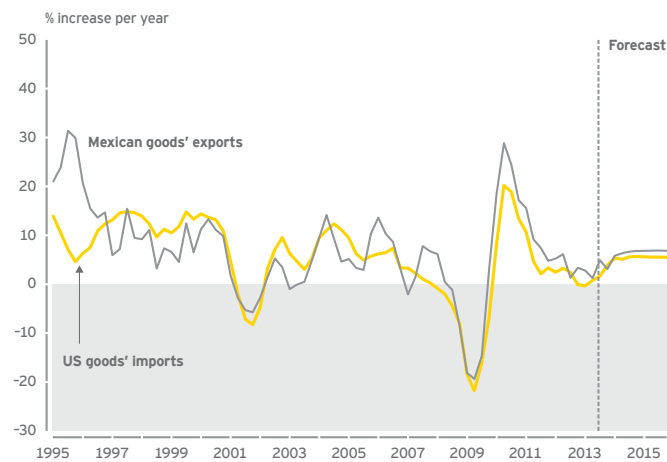
But looking ahead, conditions are expected to improve. Stronger external demand is feeding through to exports, which grew by 1.2% on the quarter in Q2. And with inflation still falling (to 3.4% in August), policy is becoming more supportive. In September, the central bank reduced its target rate to 3.75%.

Reforms to education, the labor market and telecoms have been announced this year.

The petroleum sector has also been opened up to foreign participation. But despite the three main political parties signing up to a broad reform program – the Pact for Mexico – consensus is not without limits. Therefore, these reforms may prove difficult to implement. If they are passed, the gains will be significant, and could allow the economy to grow annually by 4.5% over the medium term.

Figure 47

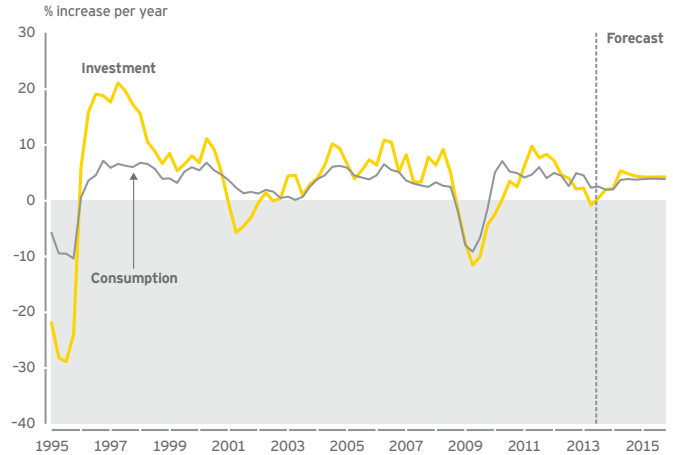
Merchandise trade: US vs. Mexican growth



Source: Oxford Economics.

Figure 48

Consumption and investment



Source: Oxford Economics.

| Mexico | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 3.6 | 1.2 | 3.9 | 4.1 | 4.2 | 4.1 |
| CPI inflation (% per year) | 4.1 | 3.7 | 3.4 | 3.3 | 3.2 | 3.1 |
| Current account balance (% of GDP) | -1.2 | -1.9 | -1.1 | -1.0 | -1.3 | -1.3 |
| External debt total (% of GDP) | 25.1 | 24.6 | 24.0 | 23.4 | 23.1 | 22.8 |
| Short-term interest rate (%) | 4.4 | 3.8 | 3.9 | 4.9 | 5.3 | 5.7 |
| Exchange per US\$ (year average) | 13.2 | 12.7 | 12.8 | 12.9 | 13.2 | 13.4 |
| Government balance (% of GDP) | -2.2 | -1.9 | -2.5 | -2.6 | -2.7 | -2.8 |
| Population (millions) | 121.0 | 122.5 | 124.0 | 125.4 | 126.8 | 128.2 |
| Nominal GDP (US\$b) | 1,179.2 | 1,251.8 | 1,335.7 | 1,424.5 | 1,500.2 | 1,585.9 |
| GDP per capita (US\$ current prices) | 9,743.4 | 10,217.1 | 10,773.6 | 11,358.6 | 11,831.5 | 12,374.0 |

Source: Oxford Economics.

Nigeria



Non-oil sector picks up the slack but growth still poised to slow

GDP grew 6.2% on the year in Q2 2013, down slightly from Q1. Growth in H1 was a little below the 2012 rate of 6.5%. The non-oil sector remains the main driver of growth, rising 7.4% on the year in Q2. While services, agriculture, and wholesale and retail trade are engines of growth, the oil sector has stalled, posting a fall of about 1%. We still forecast GDP growth of some 6.5% in 2013. However, we expect it to slow to 5%-6% a year in 2014-17 as the Government struggles to implement policy

reforms ahead of elections in 2015 and the oil sector continues to weigh on activity.

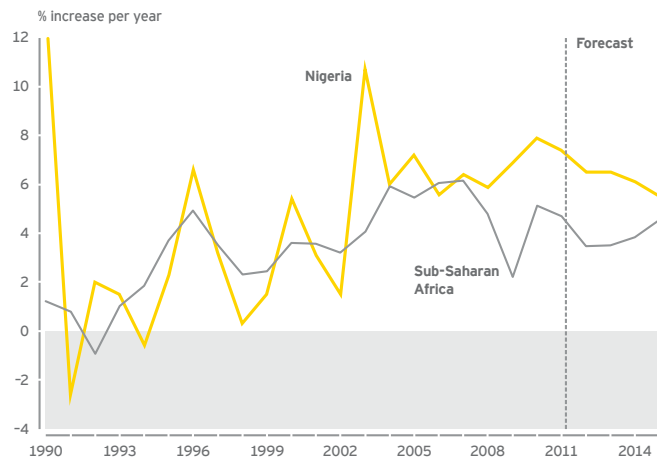
Inflation was 12.2% in 2012, but it has since eased to just over 8%. Lower inflation enabled the Central Bank of Nigeria (CBN) to cut interest rates in May to try to support activity. Rates have remained unchanged since then. The CBN remains concerned about the impact of spending by the states on the budget deficit. High public

expenditure is expected to lift the budget deficit to about 4% of GDP in 2013.

Strong oil exports raised the current account surplus to around 7.5% of GDP in 2012. But with lower world oil prices expected over the next few years, this surplus is set to fall. However, the overall balance of payments remains reasonably solid. Foreign reserves are close to US\$45b, providing around 10 months' import cover.

Figure 49

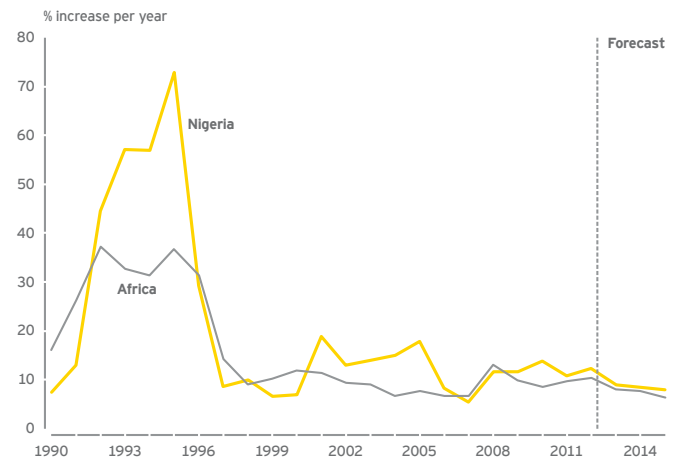
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 50

Inflation



Source: Oxford Economics; Haver Analytics.

| Nigeria | | | | | | |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Real GDP growth (% per year) | 6.5 | 6.3 | 6.1 | 5.5 | 5.3 | 5.1 |
| CPI inflation (% per year) | 12.2 | 8.5 | 8.0 | 8.0 | 8.0 | 8.0 |
| Current account balance (% of GDP) | 7.6 | 3.3 | 1.0 | 0.6 | 0.4 | 0.3 |
| External debt total (% of GDP) | 5.0 | 4.7 | 4.4 | 4.1 | 3.9 | 3.8 |
| Short-term interest rate (%) | 14.2 | 11.5 | 9.5 | 8.0 | 7.0 | 7.0 |
| Exchange per US\$ (year average) | 156.8 | 159.8 | 163.1 | 166.2 | 170.5 | 175.8 |
| Government balance (% of GDP) | -3.1 | -4.1 | -4.1 | -3.0 | -1.9 | -0.9 |
| Population (millions) | 167.0 | 171.2 | 175.5 | 179.8 | 184.6 | 189.4 |
| Nominal GDP (US\$b) | 267.6 | 302.8 | 340.2 | 380.4 | 421.5 | 464.1 |
| GDP per capita (US\$ current prices) | 1,602.9 | 1,768.4 | 1,938.1 | 2,115.5 | 2,283.3 | 2,450.0 |

Source: Oxford Economics.

Poland



GDP growth

2014 2.4%

Outlook brightens as economy emerges from slowdown

Real GDP rose by 0.4% on the quarter in Q1 2013 on a seasonally and working-day adjusted basis, in line with our forecast. Growth was again driven by net trade. This is a symptom of the current weakness of domestic demand, particularly investment.

Since the previous edition, we have upgraded our 2013 GDP growth forecast for Poland from 0.9% to 1.1%. The move partly reflects revisions to the historical path of real GDP, which have created

stronger base effects, and a slight improvement in the prospects of the Eurozone.

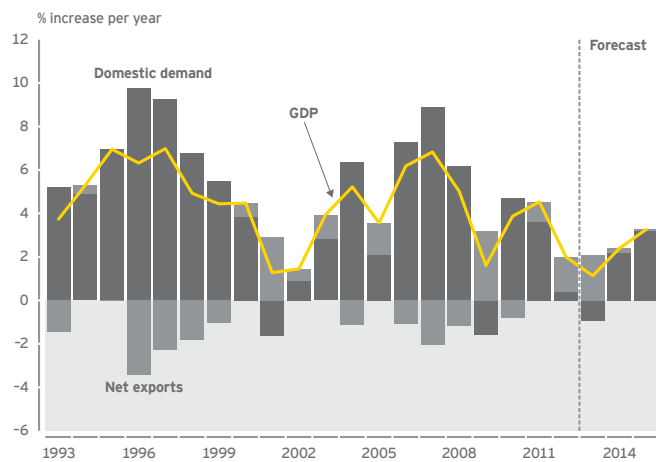
Recent data releases appear to confirm that the slowdown has bottomed out, with industrial production having picked up. Construction improved notably in July after a torrid 12 months. However, it dipped again in August, indicating that the recovery will be fragile. Activity should pick up in H2, as the economy starts to benefit

from the extensive monetary easing implemented over the past year. In H1 2013, GDP growth was driven by net trade. But more recent data suggests that domestic demand is beginning to pick up.

In the medium term, we expect growth to rise gradually to just over 3.5%. This reflects a combination of sound fundamentals and the existence of spare capacity following the prolonged slowdown.

Figure 51

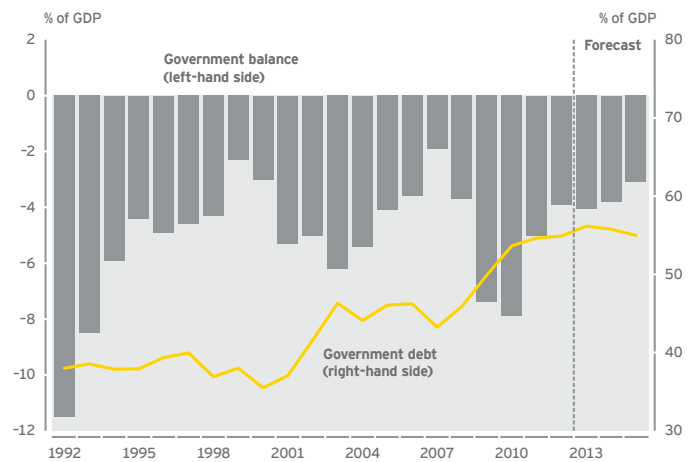
Contributions to GDP growth



Source: Oxford Economics.

Figure 52

Government budget balance and debt



Source: Oxford Economics.

| Poland | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 2.0 | 1.1 | 2.4 | 3.3 | 3.6 | 3.7 |
| CPI inflation (% per year) | 3.7 | 1.4 | 2.3 | 2.4 | 2.5 | 2.5 |
| Current account balance (% of GDP) | -3.7 | -1.3 | -1.4 | -1.9 | -2.3 | -3.0 |
| External debt total (% of GDP) | 71.6 | 73.1 | 78.5 | 83.4 | 83.0 | 82.0 |
| Short-term interest rate (%) | 4.7 | 2.8 | 2.7 | 3.7 | 4.2 | 4.2 |
| Exchange per US\$ (year average) | 3.3 | 3.2 | 3.2 | 3.3 | 3.3 | 3.2 |
| Government balance (% of GDP) | -3.9 | -4.1 | -3.3 | -2.5 | -2.1 | -1.9 |
| Population (millions) | 38.6 | 38.6 | 38.6 | 38.6 | 38.6 | 38.6 |
| Nominal GDP (US\$b) | 489.9 | 510.9 | 535.9 | 554.3 | 591.9 | 632.6 |
| GDP per capita (US\$ current prices) | 12,706.3 | 13,242.4 | 13,881.2 | 14,358.6 | 15,337.5 | 16,398.9 |

Source: Oxford Economics.

Qatar

GDP growth

2014  **6.0%**

Increased public spending to drive stronger growth next year

We expect a further slowdown in GDP growth to 5.8% this year. This compares with growth of 6.2% in 2012. Non-oil GDP growth is expected to slow from 14% last year to 12.2% this year. Given Qatar's self-imposed moratorium on increasing gas capacity, we do not expect much change in liquefied natural gas output until at least 2015.

With respect to oil, spare capacity is negligible. Both offshore and onshore fields are ageing and their yields should decline

over time. Capacity could rise a little over the next five years, aided by current projects at the onshore Dukhan field and Bul Hanine field, but this is not guaranteed. The challenging offshore Al-Shaheen field could also see new investment. Against this background, it is clear that the impetus for growth will need to come from the non-oil sector.

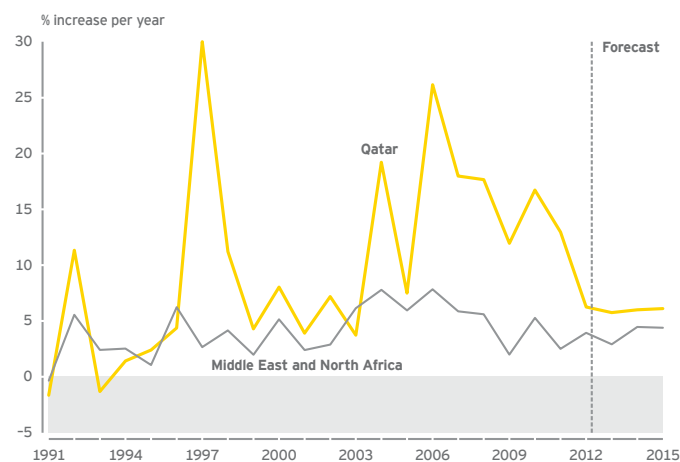
In 2012-13, planned substantial public spending increases failed to materialize,

with a rise of just 2.2%. This was dampened by a 9% decline in capital spending. As revenues increased by almost 25%, the government surplus more than doubled to QAR99b or just over 14% of GDP. However, we expect spending to increase by some 20% in 2013-14, leading to a lower surplus.

We expect the economy to grow by 6.0% between 2014 and 2017, helped by stronger global demand.

Figure 53

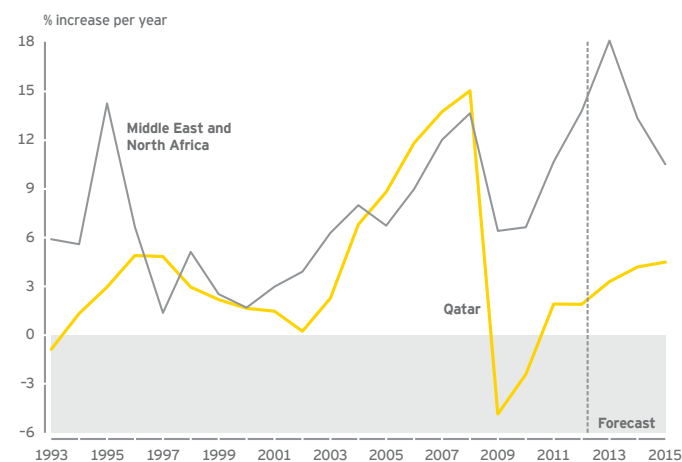
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 54

Inflation



Source: Oxford Economics; World Bank.

| Qatar | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|-----------|-----------|-----------|-----------|-----------|-----------|
| Real GDP growth (% per year) | 6.2 | 5.8 | 6.0 | 6.1 | 6.0 | 6.0 |
| CPI inflation (% per year) | 1.9 | 3.3 | 4.2 | 4.5 | 4.5 | 4.5 |
| Current account balance (% of GDP) | 32.0 | 27.7 | 24.0 | 21.9 | 20.1 | 19.0 |
| External debt total (% of GDP) | 44.1 | 38.3 | 35.6 | 32.8 | 30.1 | 27.5 |
| Short-term interest rate (%) | - | - | - | - | - | - |
| Exchange per US\$ (year average) | 3.6 | 3.6 | 3.6 | 3.6 | 3.6 | 3.6 |
| Government balance (% of GDP) | 14.2 | 10.6 | 9.4 | 9.9 | 9.6 | 9.5 |
| Population (millions) | 1.9 | 1.9 | 2.0 | 2.0 | 2.1 | 2.1 |
| Nominal GDP (US\$b) | 192.4 | 221.6 | 233.6 | 248.7 | 265.4 | 285.1 |
| GDP per capita (US\$ current prices) | 102,966.1 | 115,190.2 | 118,072.9 | 122,327.0 | 128,451.7 | 135,818.7 |

Source: Oxford Economics.

Russia



GDP growth

2014



2.8%

H1 recession prompts sharp downgrade to 2013 forecast

Preliminary estimates indicate that the economy slumped into a technical recession¹ in H1, following successive quarterly contractions. Such an outcome is extremely disappointing, particularly in the light of strong oil prices, which have averaged over US\$100 per barrel. As a

result, our forecast for real GDP growth this year has been downgraded to 1.5%, from 2.7% in our previous edition.

We expect a very modest rebound in activity during H2, spurred initially by the strength of this year's harvest. Inflation should also fall back in the near term, following the Government's decision to freeze certain state-regulated service tariffs next year. This should trigger a concerted

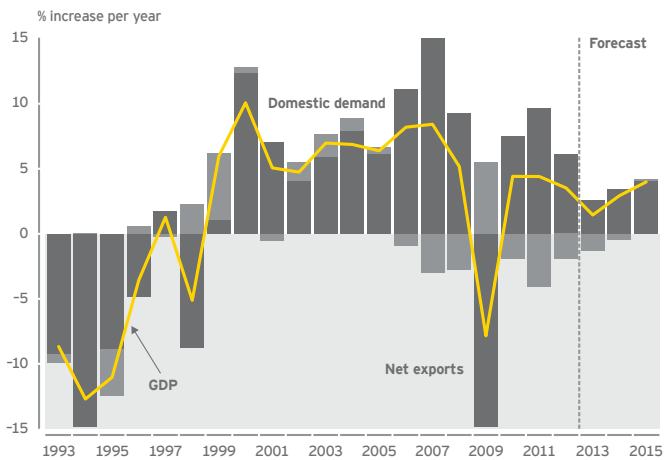
monetary easing cycle, boosting real GDP growth to nearly 3% by 2014.

In the medium term, the economy's poor demographic profile and slow pace of reform will constrain real GDP growth to less than 4%. We think that risks are skewed to the downside, with the recent slowdown highlighting the existence of serious structural deficiencies.

¹ A technical recession is defined by two consecutive quarters of negative economic growth as measured by a country's GDP.

Figure 55

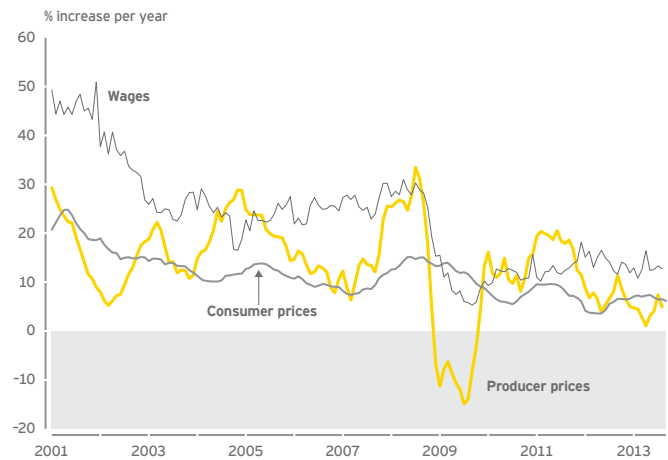
Contributions to GDP



Source: Oxford Economics.

Figure 56

Inflation



Source: Federal State Statistics Service; Haver Analytics.

| Russia | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 3.4 | 1.5 | 2.8 | 3.3 | 3.1 | 3.2 |
| CPI inflation (% per year) | 5.1 | 6.6 | 4.9 | 5.1 | 5.0 | 4.8 |
| Current account balance (% of GDP) | 3.7 | 1.5 | 1.3 | 0.8 | 0.2 | -0.3 |
| External debt total (% of GDP) | 29.4 | 33.9 | 35.4 | 35.9 | 36.4 | 36.8 |
| Short-term interest rate (%) | 7.2 | 7.5 | 7.2 | 7.1 | 7.0 | 6.8 |
| Exchange per US\$ (year average) | 31.1 | 31.8 | 32.6 | 32.8 | 33.1 | 33.6 |
| Government balance (% of GDP) | 0.8 | -0.7 | -1.4 | -1.8 | -2.3 | -2.3 |
| Population (millions) | 143.1 | 142.8 | 142.4 | 142.1 | 141.7 | 141.3 |
| Nominal GDP (US\$b) | 2,012.2 | 2,122.3 | 2,238.9 | 2,412.1 | 2,581.8 | 2,750.2 |
| GDP per capita (US\$ current prices) | 14,063.1 | 14,866.2 | 15,721.5 | 16,979.9 | 18,222.1 | 19,463.8 |

Source: Oxford Economics.

Saudi Arabia



GDP growth

2014 4.3%

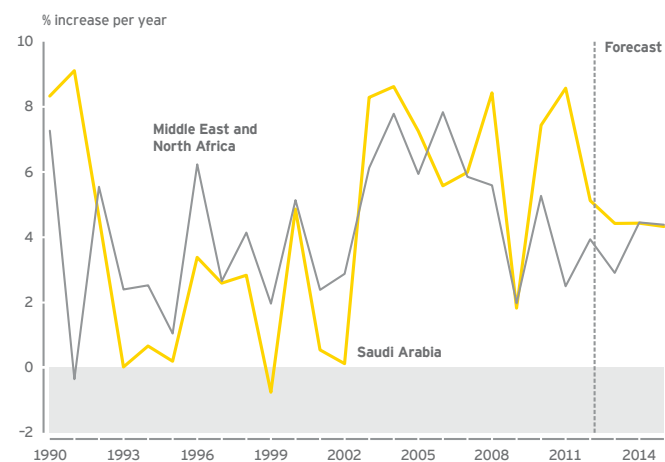
Oil output dips but domestic consumption remains robust

We expect the Saudi economy to grow by just over 4.0% this year and next. This is down from the 5.1% growth achieved in 2012. This slowdown largely reflects lower oil production, which we anticipate being down 2.3% on the year in 2013 and then up by a modest 2.1% in 2014. Nevertheless, our growth forecast for 2013 has been downgraded since the last edition, due to lower-than-expected oil production in Q2.

In contrast, non-oil growth will remain robust over the next few years, with consumption supported by very strong credit growth and accommodative fiscal and monetary policy. The strongest performing sectors will be those that are driven by domestic consumption and that stand to benefit from recent government investment. Transport, construction and utilities are likely to be among the top performers.

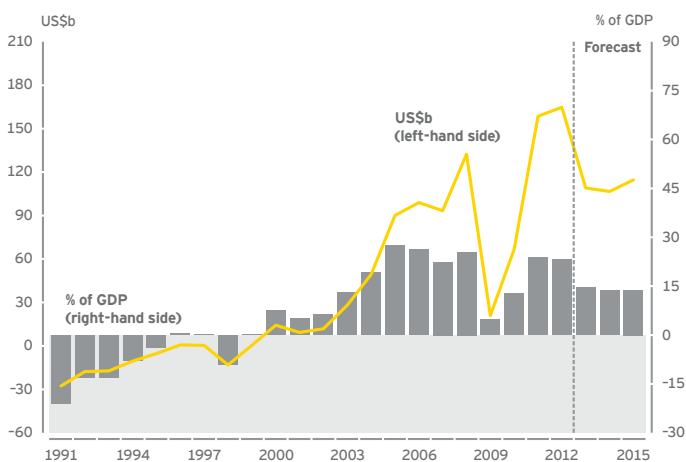
We expect annual growth to average almost 4.5% in the years to 2017, supported by strong fundamentals. However, the development of shale oil and gas in North America and rising oil supplies elsewhere presents a downside risk to the forecast. Besides limiting growth in Saudi's real oil output, this would also put downward pressure on oil prices, weakening government finances and constraining the scope for the expansionary fiscal policy of recent years.

Figure 57
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 58
Current account balance



Source: Oxford Economics.

| Saudi Arabia | | | | | | |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Real GDP growth (% per year) | 5.1 | 4.0 | 4.3 | 4.3 | 4.0 | 3.9 |
| CPI inflation (% per year) | 2.9 | 3.7 | 4.0 | 3.8 | 3.8 | 3.5 |
| Current account balance (% of GDP) | 23.2 | 15.1 | 13.9 | 13.9 | 13.0 | 12.7 |
| External debt total (% of GDP) | 11.7 | 11.1 | 10.7 | 9.8 | 9.0 | 8.2 |
| Short-term interest rate (%) | 0.9 | 1.0 | 1.0 | 1.0 | 1.5 | 2.0 |
| Exchange per US\$ (year average) | 3.8 | 3.8 | 3.8 | 3.8 | 3.8 | 3.8 |
| Government balance (% of GDP) | 14.0 | 8.4 | 5.5 | 2.8 | 1.1 | 1.2 |
| Population (millions) | 28.7 | 29.3 | 29.9 | 30.5 | 31.1 | 31.7 |
| Nominal GDP (US\$b) | 711.0 | 746.3 | 771.7 | 826.0 | 881.3 | 940.9 |
| GDP per capita (US\$ current prices) | 24,789.1 | 25,469.7 | 25,791.2 | 27,048.0 | 28,302.9 | 29,647.7 |

Source: Oxford Economics.

South Africa



GDP growth

2014 **3.2%**

Growth still driven by domestic demand, even as inflation undermines consumption

GDP growth of 0.8% in Q2 was stronger than forecast, driven partly by a bounce back from a poor Q1. Although weaker than last year, domestic demand is expected to remain the primary source of growth, and GDP is expected to increase by 2% in 2013 and 3.2% in 2014.

Consumer spending is softening relative to last year as stubbornly high inflation erodes real incomes. Inflation hit 6.4% in August, breaching the 6% target ceiling. It is

expected to fall back only gradually, due to the ongoing softness of the South African rand. This inflation undermines the purchasing power of consumers, particularly the poor. Consumption growth is forecast to be 2.4% for 2013 and 2014, compared with 3.5% last year.

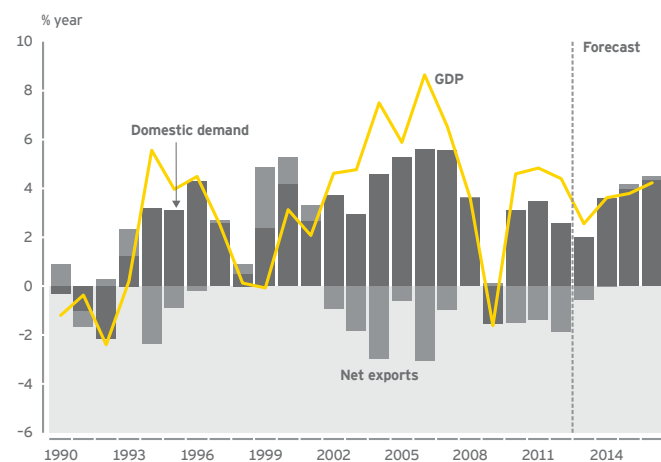
Investor confidence is being hit by both foreign and domestic challenges. These include labor unrest in the mining and auto industries, high wage growth in key sectors,

currency volatility, structural rigidities and weak external demand. Given these factors, investment growth is forecast to be a modest 3.4% in 2013 and 3.5% in 2014.

Growth should improve over the medium term. However, risks come from a weaker than expected recovery in key trading partners, which would result in an even higher external deficit than in the baseline. A failure to improve labor relations would also limit growth.

Figure 59

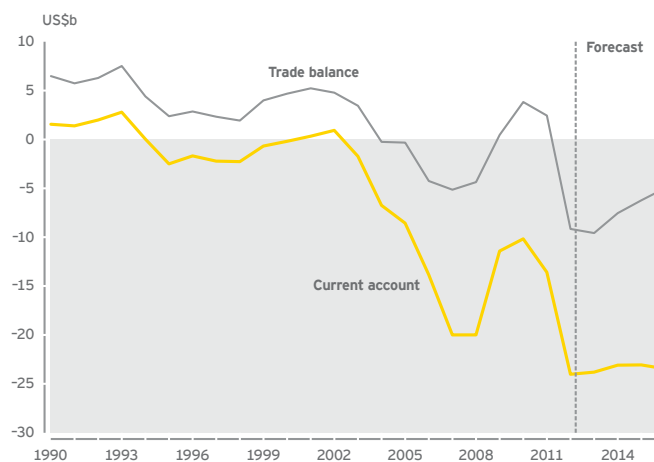
Contributions to GDP



Source: Oxford Economics.

Figure 60

Current balance



Source: Oxford Economics.

South Africa

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 2.5 | 2.0 | 3.2 | 3.5 | 3.8 | 3.9 |
| CPI inflation (% per year) | 5.7 | 6.0 | 5.8 | 5.0 | 4.8 | 4.8 |
| Current account balance (% of GDP) | -6.3 | -6.0 | -5.7 | -5.6 | -5.2 | -5.1 |
| External debt total (% of GDP) | 33.2 | 39.2 | 40.2 | 39.5 | 38.4 | 38.0 |
| Short-term interest rate (%) | 5.4 | 5.1 | 5.3 | 6.3 | 7.2 | 7.5 |
| Exchange per US\$ (year average) | 8.2 | 9.6 | 9.7 | 9.5 | 9.2 | 9.3 |
| Government balance (% of GDP) | -4.7 | -4.4 | -4.1 | -3.7 | -3.5 | -2.9 |
| Population (millions) | 52.4 | 52.8 | 53.2 | 53.5 | 53.9 | 54.2 |
| Nominal GDP (US\$b) | 384.9 | 354.7 | 379.7 | 423.5 | 471.7 | 511.4 |
| GDP per capita (US\$ current prices) | 7,342.7 | 6,716.6 | 7,140.4 | 7,911.2 | 8,754.0 | 9,432.3 |

Source: Oxford Economics.

Thailand



GDP growth

2014  4.4%

Buoyant tourism helps to end recession

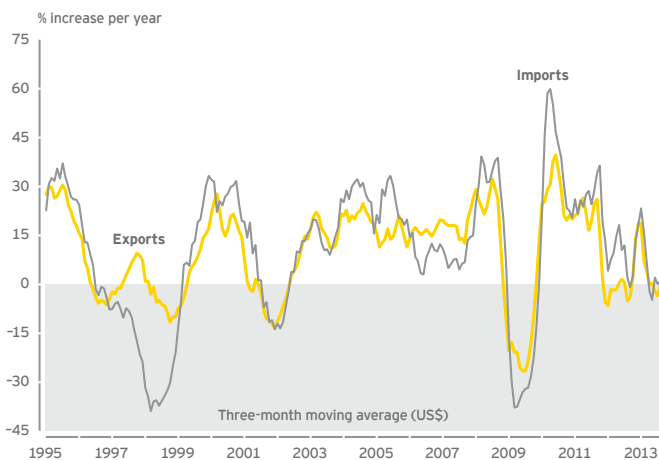
We expect the Thai economy to grow modestly in Q3, having fallen into recession in H1. Estimated seasonally adjusted export values rose on the month in July for the first time since April. And August saw the current account return to surplus for the first time in four months. Modest improvements in the US and Eurozone, and a gradual pickup in intra-Asian trade, should lead to a gentle increase in global trade flows.

Domestic data for activity in July and August showed little sign of improvement. Seasonally adjusted manufacturing output, consumer spending and investment all remained subdued in July and August. But annual growth in visitor arrivals has been strong, registering 28% on the year in August after a gain in excess of 20% during H1 2013.

Despite broadly supportive macro policy, the weak Q2 result has prompted us to lower our forecast for this year. We now anticipate GDP growth of 3.0% in 2013, down from the 4.2% expected in the previous edition. Tax incentives for buying cars expired on 31 December 2012, hitting spending as consumers brought forward purchases to the end of 2012. But spending should start to pick up, supporting growth of 4.4% in 2014 and 5.2% in 2015.

Figure 61

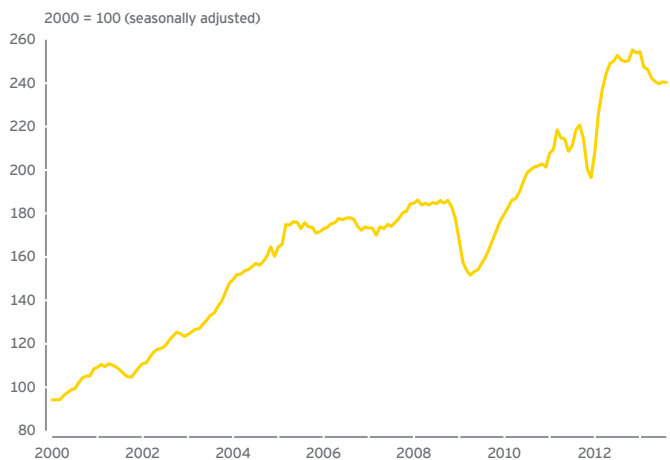
Exports and imports



Source: Customs Department; Haver Analytics.

Figure 62

Private investment indicator



Source: Bank of Thailand; Haver Analytics.

| Thailand | | | | | | |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Real GDP growth (% per year) | 6.5 | 3.0 | 4.4 | 5.2 | 5.4 | 4.9 |
| CPI inflation (% per year) | 3.0 | 2.2 | 2.6 | 2.4 | 2.5 | 2.7 |
| Current account balance (% of GDP) | -0.4 | -0.8 | 0.1 | 0.9 | 1.4 | 1.2 |
| External debt total (% of GDP) | 33.1 | 36.6 | 36.7 | 36.7 | 36.9 | 37.2 |
| Short-term interest rate (%) | 3.1 | 2.6 | 2.6 | 3.4 | 4.7 | 5.6 |
| Exchange per US\$ (year average) | 31.1 | 30.6 | 31.3 | 32.5 | 33.4 | 34.2 |
| Government balance (% of GDP) | -4.5 | -2.1 | -2.7 | -2.9 | -2.8 | -2.8 |
| Population (millions) | 68.9 | 69.3 | 69.6 | 70.0 | 70.3 | 70.6 |
| Nominal GDP (US\$b) | 366.4 | 390.9 | 408.2 | 423.9 | 445.6 | 469.5 |
| GDP per capita (US\$ current prices) | 5,314.9 | 5,640.3 | 5,861.6 | 6,057.6 | 6,338.7 | 6,648.2 |

Source: Oxford Economics.

Turkey



Growth weakens amid market turbulence

Turkey's financial markets have been under pressure since mid-May, with market interest rates up 200bp-300bp and the Turkish lira (TRY) falling more than 10% against the euro. The central bank raised the overnight lending rate (but not the repo rate) in July and August. With the bank still determined to bring down CPI inflation to 5% in the long run, further action is likely.

The TRY's recent weakness, together with higher oil prices and rising core inflation,

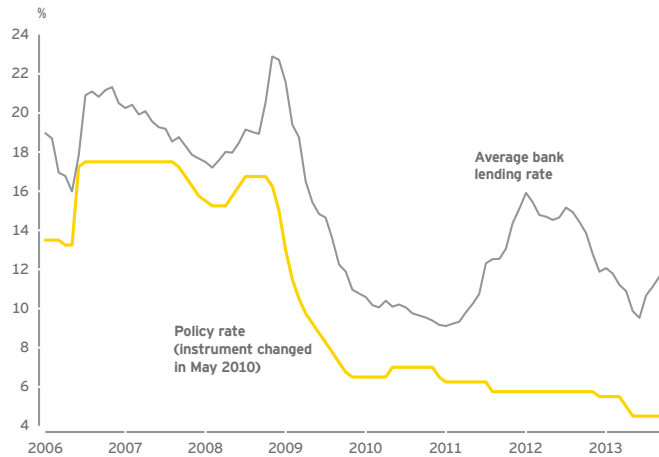
means that headline CPI inflation should average 6.8% in 2014 rather than the 5.4% we forecast in July. This will squeeze consumers' purchasing power, while the demand for loans among households and firms will be affected by the rise in bank lending rates.

Global financial turbulence is affecting an economy that was growing rapidly. It was up 2.1% on the quarter in Q2. As a result, we expect growth to be slightly less strong in

H2 2013 and early 2014. But more moderate activity should help stabilize the external deficit. Looking further ahead, if market interest rates stabilize and global trade picks up in response to the improving US and EU economies, Turkish GDP growth should accelerate through 2014. We now forecast that GDP will grow by 3.9% this year and 3.5% in 2014, before rising to a little over 5% in 2015.

Figure 63

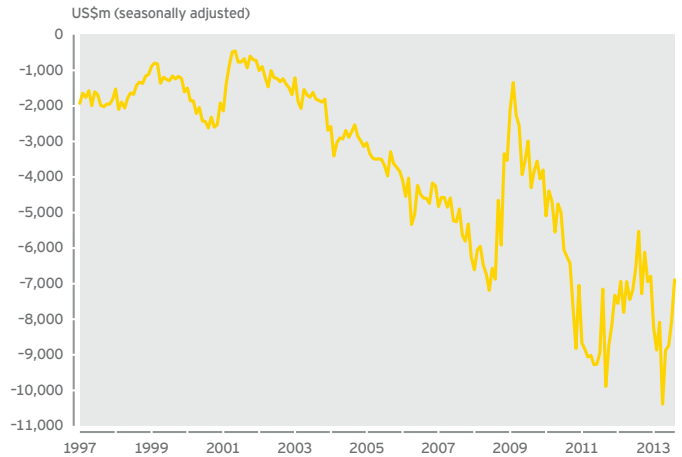
Interest rates



Source: Oxford Economics; Central Bank of Turkey; Haver Analytics.

Figure 64

Monthly trade balance



Source: Turkish Statistical Institute; Haver Analytics.

| Turkey | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 2.2 | 3.9 | 3.5 | 5.2 | 5.2 | 5.0 |
| CPI inflation (% per year) | 8.9 | 7.6 | 6.8 | 5.4 | 4.7 | 4.3 |
| Current account balance (% of GDP) | -6.2 | -7.1 | -6.4 | -6.7 | -7.0 | -6.8 |
| External debt total (% of GDP) | 41.6 | 44.7 | 45.9 | 43.8 | 41.5 | 39.1 |
| Short-term interest rate (%) | 8.7 | 6.7 | 7.6 | 9.0 | 9.5 | 9.5 |
| Exchange per US\$ (year average) | 1.8 | 1.9 | 2.1 | 2.1 | 2.2 | 2.2 |
| Government balance (% of GDP) | -2.1 | -1.8 | -2.1 | -1.5 | -1.3 | -1.3 |
| Population (millions) | 74.1 | 75.0 | 75.9 | 76.8 | 77.6 | 78.3 |
| Nominal GDP (US\$b) | 789.9 | 819.9 | 831.1 | 897.4 | 976.3 | 1,067.9 |
| GDP per capita (US\$ current prices) | 10,658.8 | 10,925.6 | 10,943.8 | 11,685.8 | 12,586.1 | 13,638.0 |

Source: Oxford Economics.

Ukraine



GDP growth

2014 2.5%

Exports set to kick-start growth as weakness at home continues

Weak industrial output and exports continue to delay any recovery. While growth will be little better than zero this year, a gradual recovery in the EU and Russia will enable an export-led return to growth in 2014-16. However, the upturn will also require renewed bilateral or multilateral loans to finance the large budget and external deficits. We forecast GDP growth of 2.5% in 2014 and then a pickup to almost 5% in 2016. However, uncertainty ahead of presidential elections in early 2015 may dampen prospects.

Having fallen sharply over the past year, inflation will accelerate to some 5%-6% in 2014-17 as the large fiscal deficit (close to 6% of GDP in 2013) forces subsidies on energy and consumer goods to be withdrawn. This may help investment by deepening the fall in real interest rates. However, it will delay monetary easing and may put pressure on the Ukrainian hryvnia. The currency is already at risk from the large external deficit and lower reserves that have been whittled away by debt repayments.

Lower imports are helping to contain the large current account deficit, which is set to fall to 7.4% of GDP in 2013. But heavy debt service costs and lower reserves mean that a new IMF standby or fresh bilateral loans are needed soon. Prospects for greater capital inflows would be enhanced by an association agreement with the EU, although this could exacerbate tensions with Russia.

Figure 65

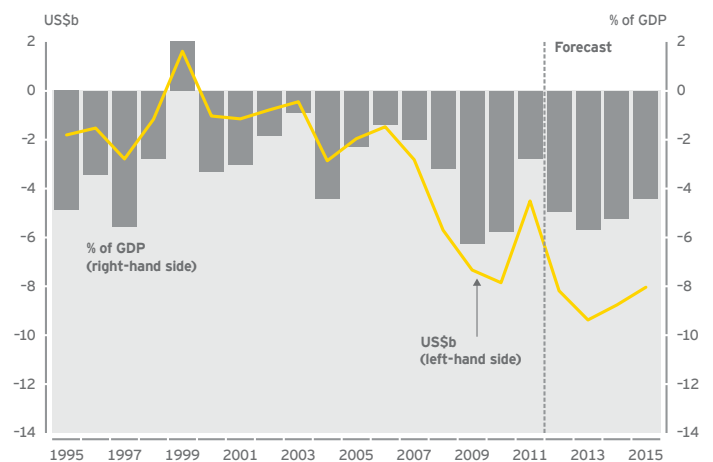
Inflation



Source: Oxford Economics; World Bank.

Figure 66

Government budget balance



Source: Oxford Economics.

Ukraine

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|---------|---------|---------|---------|---------|---------|
| Real GDP growth (% per year) | 0.1 | 0.1 | 2.5 | 4.5 | 4.8 | 4.6 |
| CPI inflation (% per year) | 1.7 | 0.5 | 6.0 | 5.5 | 5.5 | 5.5 |
| Current account balance (% of GDP) | -8.9 | -7.4 | -6.8 | -6.2 | -5.5 | -4.9 |
| External debt total (% of GDP) | 88.2 | 94.2 | 98.2 | 95.4 | 91.4 | 87.2 |
| Short-term interest rate (%) | 7.5 | 7.0 | 7.1 | 7.1 | 7.0 | 7.1 |
| Exchange per US\$ (year average) | 8.0 | 8.1 | 8.6 | 8.7 | 8.8 | 8.9 |
| Government balance (% of GDP) | -4.9 | -5.7 | -5.2 | -4.4 | -3.4 | -2.4 |
| Population (millions) | 45.0 | 44.7 | 44.5 | 44.2 | 44.0 | 43.8 |
| Nominal GDP (US\$b) | 165.8 | 165.6 | 168.2 | 182.6 | 200.3 | 219.9 |
| GDP per capita (US\$ current prices) | 3,688.4 | 3,703.6 | 3,783.5 | 4,128.8 | 4,552.9 | 5,026.1 |

Source: Oxford Economics.

United Arab Emirates



GDP growth

2014 **3.9%**

Diversification drive pays off as non-oil sector strengthens

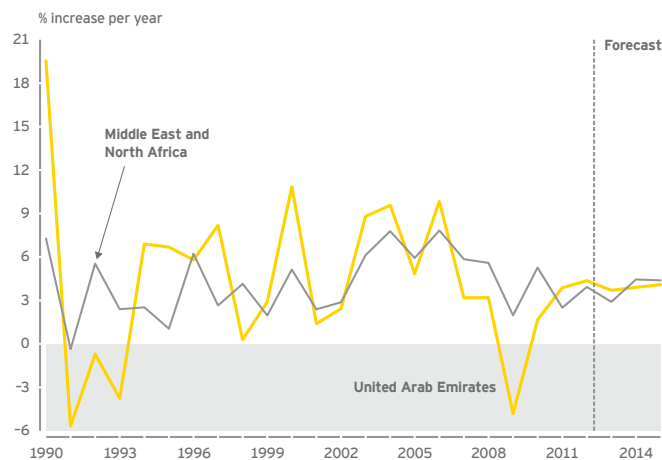
We expect GDP growth of around 4% in both 2013 and 2014, down slightly from 4.4% in 2012. The slowdown is due to a smaller increase in oil output, although the non-oil economy is expected to gather momentum over the next two years. The construction and real estate sectors, which have seen prolonged weakness since 2009, are expected to pick up, while trade and tourism should remain buoyant.

The medium-term outlook for the UAE is bright despite limited potential for significant oil-driven growth. Non-oil output now accounts for over 70% of GDP, compared with less than 60% just a decade ago. Having benefited from heavy government investment, Dubai is firmly established as a regional hub for trade, logistics and information services. Abu Dhabi has targeted knowledge-intensive sectors, such as aviation, petrochemicals, renewable energy and health care.

We expect non-oil growth to average a robust 4.5% in the years to 2017, with upside risks if reforms progress in areas like foreign ownership and bankruptcy laws and policy becomes more transparent.

Figure 67

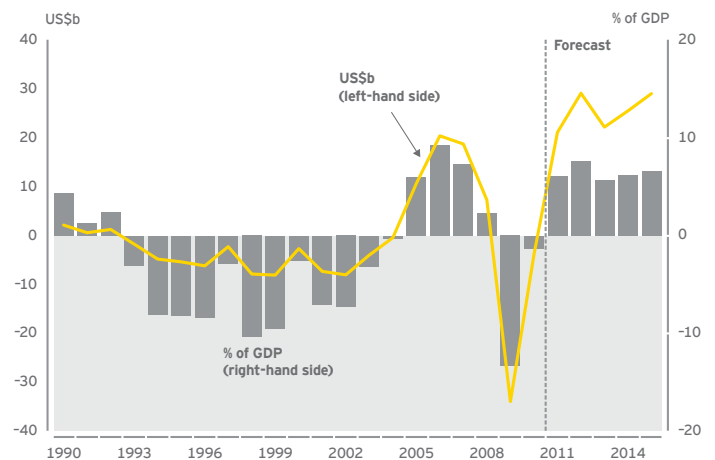
Real GDP growth



Source: Oxford Economics.

Figure 68

Government budget balance



Source: Oxford Economics.

United Arab Emirates

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 4.4 | 4.1 | 3.9 | 4.1 | 3.8 | 3.6 |
| CPI inflation (% per year) | 0.7 | 1.1 | 2.4 | 3.0 | 3.0 | 3.0 |
| Current account balance (% of GDP) | 17.3 | 13.0 | 11.6 | 9.8 | 9.0 | 8.9 |
| External debt total (% of GDP) | 28.7 | 25.3 | 21.6 | 19.3 | 16.8 | 14.5 |
| Short-term interest rate (%) | 1.4 | 1.4 | 1.4 | 1.5 | 2.0 | 3.5 |
| Exchange per US\$ (year average) | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 | 3.7 |
| Government balance (% of GDP) | 7.6 | 5.6 | 6.1 | 6.6 | 6.5 | 6.1 |
| Population (millions) | 7.9 | 8.0 | 8.2 | 8.4 | 8.5 | 8.7 |
| Nominal GDP (US\$b) | 383.8 | 394.8 | 416.4 | 440.9 | 475.7 | 518.5 |
| GDP per capita (US\$ current prices) | 48,849.3 | 49,167.6 | 50,776.6 | 52,647.6 | 55,746.4 | 59,640.1 |

Source: Oxford Economics.

Vietnam



GDP growth

2014



5.2%

Strong investment puts growth on upward trajectory

Subdued export markets and persistent high real interest rates have kept 2013 GDP growth close to last year's 5.0%. But a sustained pickup is in prospect from 2014, as the past year's strong inward investment rise starts to boost exports to faster-recovering markets. Despite an inflation rebound in the second half of the year, policy interest rate cuts are set to resume in 2014. This should precipitate a deeper fall in private sector borrowing costs as the banks continue to return to health.

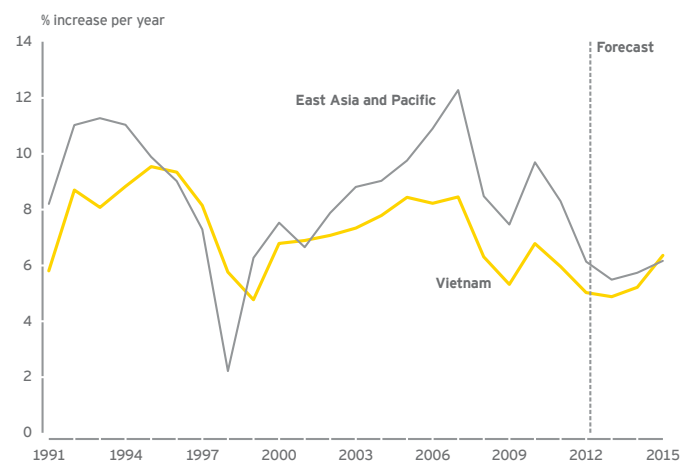
Although the trade deficit will widen again from 2015, a generally balanced current account and rising FDI should ensure that the Vietnamese dong will depreciate only in line with inflation. This will widen the scope for monetary easing and continued loan growth.

Better trade access, rising remittances and receding energy constraints will also support medium-term growth and contain inflation. But linkages between the foreign-

invested sector and smaller private firms are weak, and state-owned firms are set to maintain preferential credit access. This could prolong inefficiency and over-expansion. Rising exports and FDI, and the fast-expanding domestic market, will underpin growth in excess of 6% in 2015 and 7.0% in 2016-17.

Figure 69

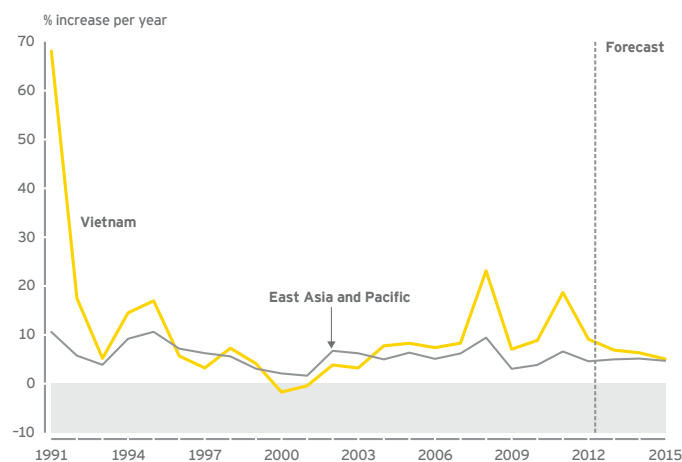
Real GDP growth



Source: Oxford Economics; World Bank.

Figure 70

Inflation



Source: Oxford Economics; World Bank.

Vietnam

| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
|--------------------------------------|----------|----------|----------|----------|----------|----------|
| Real GDP growth (% per year) | 5.0 | 4.9 | 5.2 | 6.4 | 7.0 | 6.8 |
| CPI inflation (% per year) | 9.1 | 6.9 | 6.3 | 5.1 | 4.5 | 4.5 |
| Current account balance (% of GDP) | 6.5 | 2.9 | 0.3 | -1.4 | -2.5 | -2.6 |
| External debt total (% of GDP) | 36.3 | 30.3 | 27.4 | 26.2 | 25.9 | 25.6 |
| Short-term interest rate (%) | 9.0 | 8.3 | 7.0 | 6.0 | 6.0 | 6.0 |
| Exchange per US\$ (year average) | 20,828.0 | 20,988.4 | 21,408.2 | 21,897.3 | 22,289.3 | 22,698.8 |
| Government balance (% of GDP) | -3.5 | -4.1 | -3.6 | -3.3 | -3.0 | -2.8 |
| Population (millions) | 89.7 | 90.6 | 91.5 | 92.4 | 93.2 | 94.0 |
| Nominal GDP (US\$b) | 139.5 | 155.1 | 170.1 | 185.8 | 204.1 | 223.7 |
| GDP per capita (US\$ current prices) | 1,554.9 | 1,712.0 | 1,858.9 | 2,010.4 | 2,188.8 | 2,379.7 |

Source: Oxford Economics.



Cross-country tables



Cross-country tables

| Real GDP growth | | | | | | |
|----------------------|------------|------------|------------|------------|------------|------------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Americas | 2.5 | 2.4 | 2.9 | 3.6 | 3.8 | 3.7 |
| Argentina | 1.9 | 4.3 | 1.4 | 3.3 | 3.3 | 3.1 |
| Brazil | 0.9 | 2.6 | 1.9 | 3.0 | 3.3 | 3.3 |
| Chile | 5.6 | 4.6 | 4.9 | 5.1 | 5.0 | 4.9 |
| Colombia | 4.2 | 3.7 | 4.0 | 4.2 | 4.0 | 4.0 |
| Mexico | 3.6 | 1.2 | 3.9 | 4.1 | 4.2 | 4.1 |
| EMEIA | 3.7 | 3.1 | 3.8 | 4.6 | 4.8 | 4.8 |
| Czech Republic | -0.9 | -1.0 | 1.9 | 2.6 | 3.0 | 3.0 |
| Egypt | 2.2 | 2.4 | 2.4 | 4.0 | 5.9 | 5.6 |
| Ghana | 7.9 | 6.4 | 6.1 | 5.7 | 5.4 | 5.0 |
| India | 5.1 | 4.1 | 4.5 | 5.9 | 6.3 | 6.6 |
| Kazakhstan | 5.0 | 5.5 | 6.5 | 7.1 | 6.7 | 6.3 |
| Nigeria | 6.5 | 6.3 | 6.1 | 5.5 | 5.3 | 5.1 |
| Poland | 2.0 | 1.1 | 2.4 | 3.3 | 3.6 | 3.7 |
| Qatar | 6.2 | 5.8 | 6.0 | 6.1 | 6.0 | 6.0 |
| Russia | 3.4 | 1.5 | 2.8 | 3.3 | 3.1 | 3.2 |
| Saudi Arabia | 5.1 | 4.0 | 4.3 | 4.3 | 4.0 | 3.9 |
| South Africa | 2.5 | 2.0 | 3.2 | 3.5 | 3.8 | 3.9 |
| Turkey | 2.2 | 3.9 | 3.5 | 5.2 | 5.2 | 5.0 |
| Ukraine | 0.1 | 0.1 | 2.5 | 4.5 | 4.8 | 4.6 |
| United Arab Emirates | 4.4 | 4.1 | 3.9 | 4.1 | 3.8 | 3.6 |
| Asia | 6.3 | 6.1 | 6.0 | 6.4 | 6.6 | 6.5 |
| China and Hong Kong | 7.3 | 7.2 | 6.9 | 7.1 | 7.3 | 7.3 |
| Indonesia | 6.2 | 5.6 | 5.4 | 5.9 | 5.6 | 5.4 |
| Korea | 2.0 | 2.2 | 2.9 | 3.9 | 4.0 | 3.7 |
| Malaysia | 5.6 | 4.4 | 4.8 | 4.4 | 4.5 | 4.3 |
| Thailand | 6.5 | 3.0 | 4.4 | 5.2 | 5.4 | 4.9 |
| Vietnam | 5.0 | 4.9 | 5.2 | 6.4 | 7.0 | 6.8 |
| Total | 4.6 | 4.3 | 4.7 | 5.3 | 5.5 | 5.4 |

Cross-country tables

| CPI inflation | | | | | | |
|----------------------|------------|------------|------------|------------|------------|------------|
| | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 |
| Americas | 5.1 | 5.2 | 5.2 | 5.0 | 4.7 | 4.4 |
| Argentina | 10.0 | 10.7 | 11.0 | 9.8 | 9.5 | 9.0 |
| Brazil | 5.4 | 6.3 | 6.1 | 6.0 | 5.5 | 4.9 |
| Chile | 3.0 | 1.6 | 2.6 | 2.8 | 3.0 | 3.0 |
| Colombia | 3.2 | 2.2 | 3.2 | 3.3 | 3.3 | 3.3 |
| Mexico | 4.1 | 3.7 | 3.4 | 3.3 | 3.2 | 3.1 |
| EMEIA | 5.9 | 5.4 | 5.1 | 4.7 | 4.4 | 4.3 |
| Czech Republic | 3.3 | 1.5 | 1.7 | 2.0 | 2.1 | 2.1 |
| Egypt | 7.1 | 9.2 | 10.1 | 8.5 | 6.0 | 6.0 |
| Ghana | 9.2 | 10.9 | 9.4 | 7.5 | 6.0 | 5.2 |
| India | 7.5 | 6.0 | 5.3 | 4.6 | 4.1 | 4.0 |
| Kazakhstan | 5.1 | 6.2 | 6.5 | 6.5 | 6.2 | 6.0 |
| Nigeria | 12.2 | 8.5 | 8.0 | 8.0 | 8.0 | 8.0 |
| Poland | 3.7 | 1.4 | 2.3 | 2.4 | 2.5 | 2.5 |
| Qatar | 1.9 | 3.3 | 4.2 | 4.5 | 4.5 | 4.5 |
| Russia | 5.1 | 6.6 | 4.9 | 5.1 | 5.0 | 4.8 |
| Saudi Arabia | 2.9 | 3.7 | 4.0 | 3.8 | 3.8 | 3.5 |
| South Africa | 5.7 | 6.0 | 5.8 | 5.0 | 4.8 | 4.8 |
| Turkey | 8.9 | 7.6 | 6.8 | 5.4 | 4.7 | 4.3 |
| Ukraine | 1.7 | 0.5 | 6.0 | 5.5 | 5.5 | 5.5 |
| United Arab Emirates | 0.7 | 1.1 | 2.4 | 3.0 | 3.0 | 3.0 |
| Asia | 2.8 | 2.7 | 3.1 | 3.0 | 3.0 | 3.0 |
| China and Hong Kong | 2.7 | 2.6 | 2.9 | 2.9 | 2.9 | 2.9 |
| Indonesia | 4.3 | 7.0 | 6.7 | 5.0 | 4.7 | 4.5 |
| Korea | 2.2 | 1.3 | 2.5 | 2.8 | 2.6 | 2.5 |
| Malaysia | 1.7 | 1.9 | 3.0 | 3.2 | 3.0 | 3.0 |
| Thailand | 3.0 | 2.2 | 2.6 | 2.4 | 2.5 | 2.7 |
| Vietnam | 9.1 | 6.9 | 6.3 | 5.1 | 4.5 | 4.5 |
| Total | 4.3 | 4.1 | 4.2 | 4.0 | 3.8 | 3.7 |

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