EXPORT INSIGHT

JULY - AUGUST

Your Guide to Last Month's Key Events, Shaping and Shaking the Local and Global Economy and Business, with a Forward-Looking Punch

Dear Members and Friends,

The summer's raging – along with the easing of the work tempo in the offices and beyond – but global affairs; business and otherwise are as lively as ever. Welcome to the latest July-August issue of Export Insight, in which we zoom onto the monetary policy developments and outlook in the region of Central and Eastern Europe (CEE). The region was among the world's first to start hiking interest rates and tightening monetary policy, and now is due to revert course. The catch? Worry that inflation is entrenched and can still spiral, against the backdrop of an all-over subdued growth. Outside the remit of the region, we focus on China, which is all the frenzy, as Germany publishes its long-awaited China strategy. The spoiler: it has moved from 'decoupling' towards 'de-risking', softening its rhetoric as economic headwinds intensify, and minding its export-oriented businesses' interests. China has taken the front and center also in the context of the long-anticipated Anthony Blinken's late visit. The NATO Vilnius Summit and G20 finance ministers India meetings were also noteworthy events in recent weeks. Amid all the soaring heat across Europe we here at the The Council of Slovak Exporters' wish you a cool summer!

Foreword by the Chairman

Lukáš Parízek

2023 MONETARY POLICY OUTLOOK IN CENTRAL AND EASTERN EUROPE (CEE)

Central and Eastern Europe's (CEE) monetary policy is prepared to move towards a loosening stance, as core inflation has stabilized or declined in some cases and the region has seen a slowdown of growth, but the scope remains limited. CEE has been fighting double-digit inflation since the start of Russia’s war in Ukraine in February 2022 (Fig. 1), compelling local central bank for an aggressive tightening action. But headline inflation has bottomed out and core inflation has broadly stabilized across the region. In May, headline inflation in Romania and Bulgaria has declined below the double-digit threshold, while in Czechia, Poland and Slovakia it fell to the 12 per cent mark. It remains highest in Hungary, above 20 per cent. The underlying inflation pressures (core inflation) have bottom out in most region’s economies.

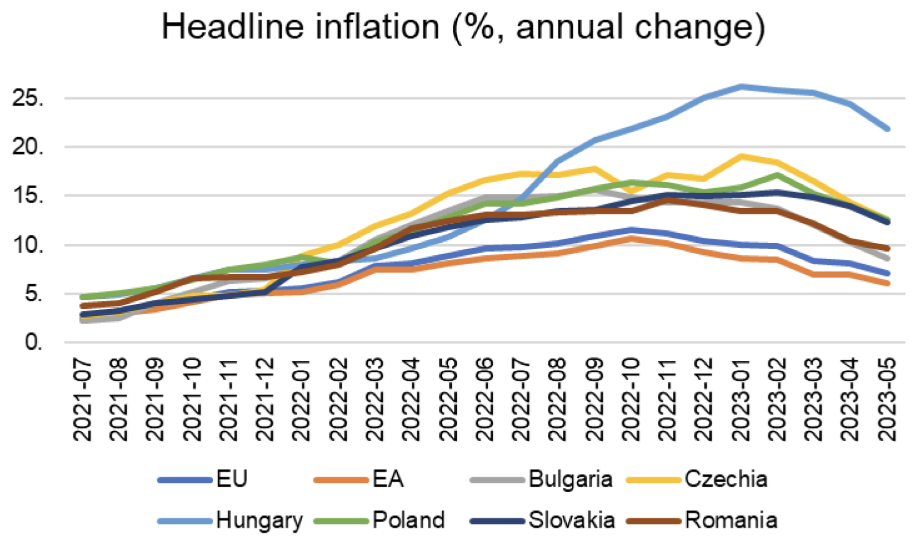

Fig 1.a

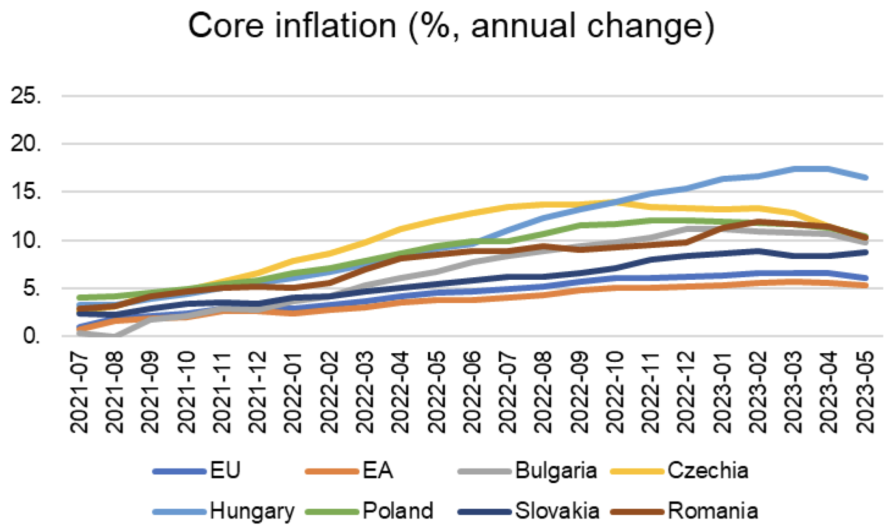

Fig 1.b

Source: Eurostat. Last observation refers to May 2023.

In addition to disinflation, the region has seen a marked slowdown in growth, with some additional headwinds expected to the open and manufacturing export-oriented economies in the region emanating from weak external demand, and stagnating growth in the eurozone and particularly, Germany. Growth has decelerated markedly, with the Hungarian economy shrinking for the third consecutive quarter in the first quarter of 2023 and the Czech growth barely positive. The continued disinflation coupled with fragile growth prospects make monetary easing compelling but economic stagnation of CEE's main trading partners, subdued manufacturing activity, and fragile consumer spending as well as lingering high inflation limit the scope for easing.

Core inflation remaining in the double digits territory in most region's economies is a particular source of concern. This is why in Poland and Czechia, Monetary policy boards remain divided over inflation becoming entrenched, and some members even advocating for rate hikes. Persistent unease over the risk of a potential wage-price spiral is amplified by political pressure to keep fiscal policies relaxed, particularly in Poland and to a lesser extent in Slovakia, in the run-up to the parliamentary election this fall.

Headline inflation in the eurozone softened to 6.1% in May from 7% in April, but underlying nominal pressures endured. The European Central Bank (ECB) raised its policy rates by 25 bp at its most recent June monetary policy meeting (Fig.2), on the expectation of eurozone inflation lingering above its 2% target until 2025. Following sustained tightening since last summer, another 25 bp rise in July, with the deposit rate at 3.75% and the main refinancing rate at 4.25% is expected. If core inflation in the summer months proves to be more persistent than anticipated, the likelihood of the ECB needing to continue tightening its monetary policy remains considerable.

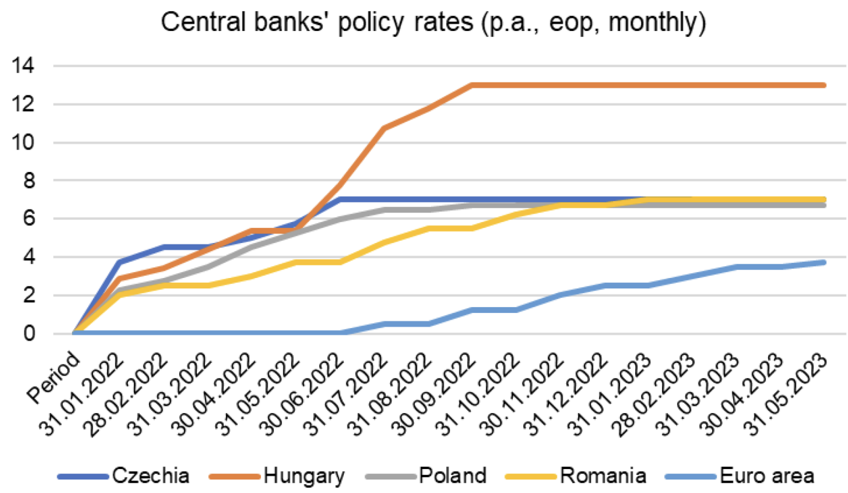

Fig 2.

Source: BIS. End of period, last observation refers to May 2023.

INTERNATIONAL SPOTLIGHT

Western leaders met with top Ukrainian officials at a pivotal NATO summit last month.

NATO's Vilnius Summit will be remembered both for the fireworks over Ukraine and historic outcomes on Sweden, along with the most detailed defense plans since the Cold War and unprecedented G7 commitments to Kyiv. While it did not yield a clear path to Ukraine's NATO membership, as the country fends off Russian forces, the Vilnius summit communiqué asserted that "We will be in a position to extend an invitation to Ukraine to join the alliance when allies agree and conditions are met." Moreover, the Summit is consequential for the security of the CEE region, as the alliance pledged to fortify its eastern defenses and security, including following the Prighozhin's mutiny and the relocation of the mercenaries to Belarus (Foreign Policy, Atlantic Council)

The war in Ukraine is reshaping world trade and investment,

across regions and industries, according to a July World Bank analysis. A new study shows that world trade will drop by one percent, lowering global GDP by just under one percent. Manufacturing exporters such as Vietnam, Thailand, and Mexico see a sharp decline, especially in energy intensive sectors. Net exporters of crops, including Turkey, Brazil, and

India, and of fossil fuels, such as Nigeria and countries in the Middle East, see a surge in their exports, attenuating the negative effects of the war. The economic shock waves are moving through five channels: commodity markets, logistics networks, supply chains, foreign direct investment (FDI), and sectors such as tourism. (World Bank)

The trade-oriented powerhouse, Germany, has published its newest 'China strategy' in July (available here).

A compromise between the three ruling coalition parties, it is mindful of German businesses' needs for the country's largest trading partner amid economic pain, with little room for an open challenge of Beijing's geopolitical advances. Europe's economic powerhouse Germany slid into a recession when it posted -0.5% and -0.3% on-quarter in the last three months of 2022 and the first quarter of 2023, respectively. (Euronews)

July third G20 Finance Ministers and Central Bank Governors Meeting in India had G20 finance

chiefs discussing pervasive global challenges, such as climate change, pandemics, rising debt in low-income countries. Sri Lanka and Ghana defaulted on their international debts in 2022, roughly two years after Zambia defaulted. And more than half of all low-income countries face debt distress, which hurts their long-term ability to function and develop. U.S.' Janet Yellen Yellen added that it was vital to "press for more ambition and specific reforms" with respect to global development banks. Full communique is available here. (AP)

Renault boss warns the war of the future will be over critical raw materials.

Originally, his trip was abruptly canceled when the balloon, claimed by China to be monitoring weather, drifted across the continental US and was destroyed by American military aircraft. During his visit, Mr. Blinken will have meetings with China's top foreign policy officials, re-opening diplomatic channels and moving forward on the global priorities, easing trade tensions, and potential conflict over the Taiwan strait. (BBC)

Saudi Arabia's Ma'aden to acquire 10% of Brazil base metals firm

Saudi Arabian Mining Company (1211.SE), known as Ma'aden, has agreed to acquire a 10% stake in Brazil's base metals company Vale, it said in a bourse statement, as part of a strategy to invest in global mining assets. Ma'aden, through Manara, its joint venture established with the Public Investment Fund, signed a binding agreement to acquire the 10% stake in Vale Base Metals, based on an enterprise value of $26 billion. (Reuters)

V4 REGION

SLOVAKIA

WHAT'S UP

Thanks to the optimal spring weather, Slovak farmers can look forward to a significantly better harvest than last year. The harvest of wheat, barley and rapeseed will be roughly one-tenth higher than a year ago, according to the Slovak statistical office.

WHAT'S NEXT

Slovakia is not threatened by a shortage of grain, which will contribute to the stabilization of food prices, says the head of the Chamber of Agriculture and Food Industry. On the other hand, costs, including fertilizer, remains high, which will eat into farmers' profits. Overall, the picture is slowly but surely looking up for Slovak farmers, after a tough patch over the last few summers.

CZECHIA

WHAT'S UP

In May, industrial production unexpectedly rose by 1.6% on a monthly basis, at odds with expectations. However, on an annual basis, industrial production was higher by 1.4%. This figure was partly affected by base effects and a high backlog of orders in the automotive sector. The automotive sector still contributes significantly to the growth of industrial production.

WHAT'S NEXT

Last year's problems with imports of semiconductors and cables implied a high production growth in the first six months of 2023 (correction effect). Secondly, these problems also resulted in a high volume of unfinished orders, which increases this year's production. But these culprits are expected to gradually fade away.

HUNGARY

WHAT'S UP

WHAT'S NEXT

The volume of industrial production in Hungary dropped by 4.6% on an annual basis in May but increased by 1.6% on a monthly basis, surprising to the upside, given the purchasing manager sentiment across Europe. The manufacturing of electrical equipment grew at the highest rate, but transport equipment increased, too.

The short-term outlook for industrial production is still hazy. On the one hand, the slowdown in the global economy poses a drag on the Hungarian economy, as the economic performance of Hungary's main export markets continues to be subdued. On the other hand, a substantial battery capacity is set to start operating soon, having completed its testing period in June.

POLAND

WHAT'S UP

In May industrial output declined by -3.2% annually, while real retail sales dropped by -6.8%, and construction and assembly output was also down in May 2023 compared to the previous year. The weak performance of these sectors is also visible based on quarterly averages. The deceleration in global economic activity has affected Poland, with these sectors being dragged down by weak external demand.

WHAT'S NEXT

In the next weeks, Poland will see the complete set of data for the second quarter. Industry is expected to grow monthly, but be lower than last year, while retail sales growth should remain negative, reflecting the weakness of private consumption.

COUNTRY IN FOCUS

RETHINKING CEE COOPERATION WITH CHINA

Sino-European relations

China and the European Union have an extensive and growing economic relationship. The relationship has at times been complicated due to the distortions caused by China's state capitalist system and the diversity of interests within the EU's incomplete federation. More can be done to capture the untapped trade and investment opportunities that exist between the parties. China's size and dynamism, and its recent shift from an export-led to a domestic demand-led growth model, mean that these opportunities are likely to grow, and most likely, rapidly. As the Chinese economy matures, it is likely to evolve into a stabilized economy in world markets as opposed to the disruptive force it was during its extraordinary breakout period.

The region of Central and Eastern Europe (CEE), in particular, has been viewed as a promising region

for an expanded and pragmatic Sino-CEE cooperation, and also hoped to be China's economic gateway to Europe. This is exemplified by several economic and diplomatic formations, notably, the massive, infrastructure-focused Belt and Road Initiative and the '17+1' format bound to increasing Chinese investment in the region. Many region's political leaders also favored close ties to China.

Among CEE countries, Hungary especially has remained keen on keeping Beijing close,

as evidenced by last August announcement of Chinese Contemporary Amperex Technology Co., Limited to open its second European battery plant in Hungary, with an investment of EUR7.3 billion, more than three times the previous one. Apart from Hungary, the '17+1' format has engendered the Port of Piraeus in Greece, where the Chinese shipping company Cosco has been the majority stakeholder since 2016.

But there is more potential to diversify mostly westbound trade and investment flows in the region, including from China,

in the spirit of pragmatic economic cooperation, and outside the scope of strategically important (national security-relevant) domains, like in energy or 5G. In 2021, Chinese FDI in Europe was on the rise, according to the Mercator Institute for China Studies (MERICS) analytics. But it was Western Europe – notably, Germany, France, the Netherlands and the UK (Fig.3) – that was the biggest FDI beneficiary.

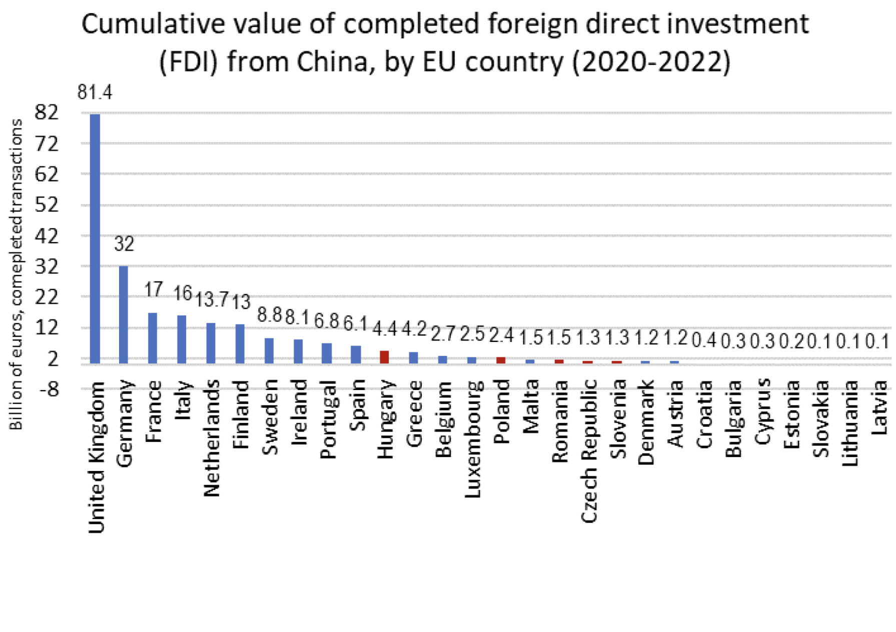

Fig 3.

Major greenfield investments by China could extend

beyond just the UK, France, Germany, and Hungary, to the CEE-region by-and-large. The automotive industry, following the ban on the sale of petrol and diesel-powered combustion engine cars from 2035 and the transition towards electric vehicles (EVs), offers a natural opportunity for a mutually advantageous cooperation, at least over the short run, until a broader trading partners diversification can be achieved in Europe, in the efforts to safeguard the continent's long-term economic interests. Such cooperation may help the EU retain its automotive market shares, as well as to leap forward on its climate ambitions, including in the arenas of renewable energy sources, and green mobility. For China, Europe has already become a key market in its global EV expansion strategy. Brussels may, meanwhile, screen the investments to comply with the rules and stipulations concerning legal and practical hurdles around potential acquisitions of strategic assets. As Europe is in the middle of reformulating its China strategy, such pragmatic cooperation may render the Sino-European relations more balanced.

Events of Note
June-July 2023

03/07/23
CSE in Prague

The Council *of* Slovak Exporters were in Prague as guests of the Ministry of Foreign Affairs of the Czech Republic for the annual convergence of their Economic Diplomats at the picturesque Czernin Palace- view photos

04/07/23
Argentex

The Council *of* Slovak Exporters signed a landmark agreement with Argentex PLC, in the UK to provide currency solutions to its members- view photos

10/07/23
CSE in Uzbekistan

The Council *of* Slovak Exporters was on the road with Chairman Lukas Parizek in Uzbekistan as a special guest of the government see more of what he said and who he visited 2023 - watch video or view photos

12/07/23
FMCG Open Day

Council *of* Slovak Exporters had a first of its kind FMCG Open Day inviting our partners from the UAE; TACCT Global to sample some of Slovakia's finest food and beverages from our member pool and beyond- view photos

For **more information** on these or any other events please email us at **info@exporteri.sk**

Realizované s finančnou podporou

Nadácie Ministerstva hospodárstva SR na rok 2023