COFACE ECONOMIC PUBLICATIONS

OCTOBER 2019

BAROMETER
COUNTRY AND SECTOR RISKS BAROMETER
Q3 2019

By the Coface Economic Research team

Global economy in 2020: general slowdown despite the action of central banks

As usual, many political events marked the summer: another episode of the Argentine exchange rate crisis, an unexpected change of government in Italy, major demonstrations in Hong Kong and Russia, an ever more challenging continuation of the "Brexit" process and an attack on oil installations in Saudi Arabia. The multiplication of areas of political uncertainty, combined with the risks mentioned at length in the first semester and still relevant today (decline of world trade in volume, high volatility in oil prices or even decline in automobile sales in Europe and China) continued to affect corporate morale. Now, in addition to Europeans and Asians firms, American companies are also openly concerned about President D. Trump's protectionist rhetoric. Should this pessimism, expressed by manufacturing companies, be seen as a temporary phenomenon without the risk of contagion to service activities, or on the contrary as a sign of a deep recession as in 2009? An intermediate scenario, similar to the one observed in 2001-2002 following the bursting of the "Internet bubble" now seems most likely: a gradual and partial transmission of the industrial recession to services and a notable slowdown of growth in 2020 in the main advanced economies. The only good news is that the central banks of the United States, the Eurozone and many emerging countries have taken measure of the situation by announcing monetary easing measures. In this context, there were two changes in country evaluations this quarter. They concern Hong Kong (downgraded from A2 to A3) and Mauritania (upgraded from D to C). As for the business sectors, after the series of downgrades concerning the automotive sector in June, the changes are less numerous this quarter but still indicate an increase in risks (13 downgrades but no upgrades). The automotive sector is still concerned (downgraded in three new countries) as well as the sectors that depend on it (chemicals in Germany for example). Corporate credit risks are also on the rise in the paper sector in North America. Finally, new victims of the rise of trade protectionism are to be reported (ICT sector in Korea notably).

International trade: the recession is confirmed

The fatigue of world trade was confirmed this summer. According to data from the Dutch CPB Institute, it contracted for the third consecutive quarter between April and June 2019. Over the year 2019 as a whole, Coface expects world trade to contract by 0.8% in volume[1] (**Chart 1**).

In 2020, the prospects will depend largely on the political environment: while the emergence of the first tangible effects of the Sino-American trade war plead, at first sight, for the search of a trade agreement between the two major global powers, the US President's actions in the context of a campaign for his re-election (and possibly a procedure of impeachment) remain difficult to predict. Even if almost all Chinese exports to the United States will be subject to customs duties at the end of 2019, there will still be room for maneuver for the US President to put pressure on China. As for tariff measures, it will still be possible for him to increase existing customs duties (he had stated during the 2016 presidential campaign that he would set customs duties on Chinese imports at 45%!). Above all, it will be possible for him to take non-tariff measures that could have very negative effects on trade. This is what he stated in one of his tweets on August 23: "American companies are asked to immediately start looking for alternatives to China". This announcement, which went almost unnoticed in mid-summer, could refer to a 1977 US International Emergency Economic Powers Act giving the US President the power to ban exports to China, Chinese imports from entering the country, as well as imports not directly from China but including content made in China. This is doable by considering China as an "unusual and extraordinary threat to national security, foreign policy or the American economy".

Even if this risk scenario does not materialize in 2020, the very fact that it exists should continue to encourage companies in postponing some of their investments in this climate of high uncertainty. This is confirmed by a recent NBER study[2]. A new political risk indicator for US companies listed on the stock market was created, based on the proportion of time dedicated to political risks during their quarterly financial results announcement meetings to investors. The authors conclude that political risks are increasing and are pushing US companies to devote more resources to lobbying and political party financing, at the expense of hiring and investment. These results are in line with Coface's previous work on the subject[3].

Growth: a two-speed Europe and a weaker than expected performance in 2020 in the United States and China...

These political uncertainties are not the only reasons for the recession of world trade and industry in advanced economies. Ongoing structural changes in the automotive sector, discussed at length last quarter[4], are still relevant: past and future anti-pollution standards in 2020 (especially in Europe) and changes in consumer behavior (especially in China). In this context, European economies are now moving at two speeds: on the one hand, those that are particularly dependent on world industry and trade (Germany) and/or penalized by internal political uncertainties (Italy, United Kingdom). In these three economies, GDP growth was zero or negative in the 2nd quarter of 2019. We therefore forecast positive but weak growth in 2020 (0.5% in Germany, 0.7% in Italy and 0.9% in the United Kingdom under the assumption that a "No deal" is avoided). On the other hand in France, Spain and the Netherlands[5], companies continue to invest and business failures remain in decline (**Chart 2**). Despite a slight slowdown, Coface still expects growth to remain above 1% in 2020 (1.2%, 1.9% and 1.5% respectively). Indeed, the service sectors of these economies remain resilient so far.

Growth also slowed in the United States in the 2nd quarter (to 2.0% on an annualized basis, after 3.2% in the first quarter). Business margins are eroding due to high labor costs and the effects of protectionist measures taken since the beginning of 2018. In this context, where the effects of past budgetary measures (notably the reduction in corporate taxes) will be less felt in 2020, Coface anticipates that growth will slow significantly (1.3% after 2.2% in 2019), i.e. at a level below the consensus (1.8% for 2020[6]). However, growth will not be negative for the year as a whole, which is a scenario quite similar to the one observed in 2001. Nevertheless, in Europe, the spreading effects of the signs of fatigue, from industry to services, are not very visible at this stage. In its recent history, industrial recessions have not always had significant contagion effects on service activities (**Chart 3**). They have therefore not always coincided with a recession for the economy as a whole - far from it - : over the last decade, the ISM index of business confidence in the manufacturing sector has fallen three times below the 50 limit indicating a reduction in output in the sector. Only once did this changeover correspond to a recession in GDP (in 2009). In the other two cases (late 2012 and late 2015), the latter slowed down without falling into negative territory.

1 The Coface forecast model for world trade includes oil prices (Brent), US manufacturing confidence (ISM), Korean exports and the cost index of maritime transport as explanatory variables (Baltic Index).
2 Tarek A. Hassan, Stephan Hollander, Laurence van Lent, Ahmed Tahoun (juin 2019): "Firm-Level Political Risk: Measurement and Effects, work document NBER 24029. https://www.nber.org/papers/w24029.pdf
3 Panorama Coface (octobre 2016) : "European Economies: Will political risk spoil the party in 2017?" https://www.coface.com/News-Publications/Publications/European-economies-Will-political-risk-spoil-the-party-in-2017
4 https://www.coface.com/News-Publications/Publications/Trade-tensions-return-to-the-forefront-of-the-global-economy-Country-and-Sectors-risks-Barometer
5 Focus Coface, septembre 2019 : "What is the secret of Dutch trade?". http://coface.com/News-Publications/News/Netherlands-What-is-the-secret-of-Dutch-tradeoir
6 Consensus Forecasts, septembre 2019.

In addition to the first one, the world's second economy is also slowing down sharply: Chinese industrial production grew by only 4.4% year-on-year in August, its lowest level since February 2002. There are many reasons for this slowdown: in addition to the still significant overcapacities in sectors such as construction and metallurgy, the automotive and ICT sectors are affected both by the effects of the trade war with the United States and the changes in the behavior of Chinese consumers, who are now more equipped with durable consumer goods. Here again, Coface anticipates that GDP growth will be below expectations in 2020 (5.8% "only").

Despite increasingly expansionary monetary policies

Many central banks have taken note of this marked slowdown in growth and announced monetary easing measures (**Chart 4**). In the United States, the Federal Reserve lowered its key policy rate for the second time in two months in September 2019 (target 1.75%-2%). Moreover, for the first time in ten years, it injected liquidity into the day-to-day money market on September 17 2019. The lack of liquidity in the banking sector illustrated by this action underlines the fact that the Fed will probably have to start buying assets again and thus increase the size of its balance sheet again in the coming quarters. For its part, the European Central Bank relaunched its bond purchase program on 12 September 2019 and lowered the rate on deposits taxing banks' excess liquidity (from -0.40 to -0.50%).

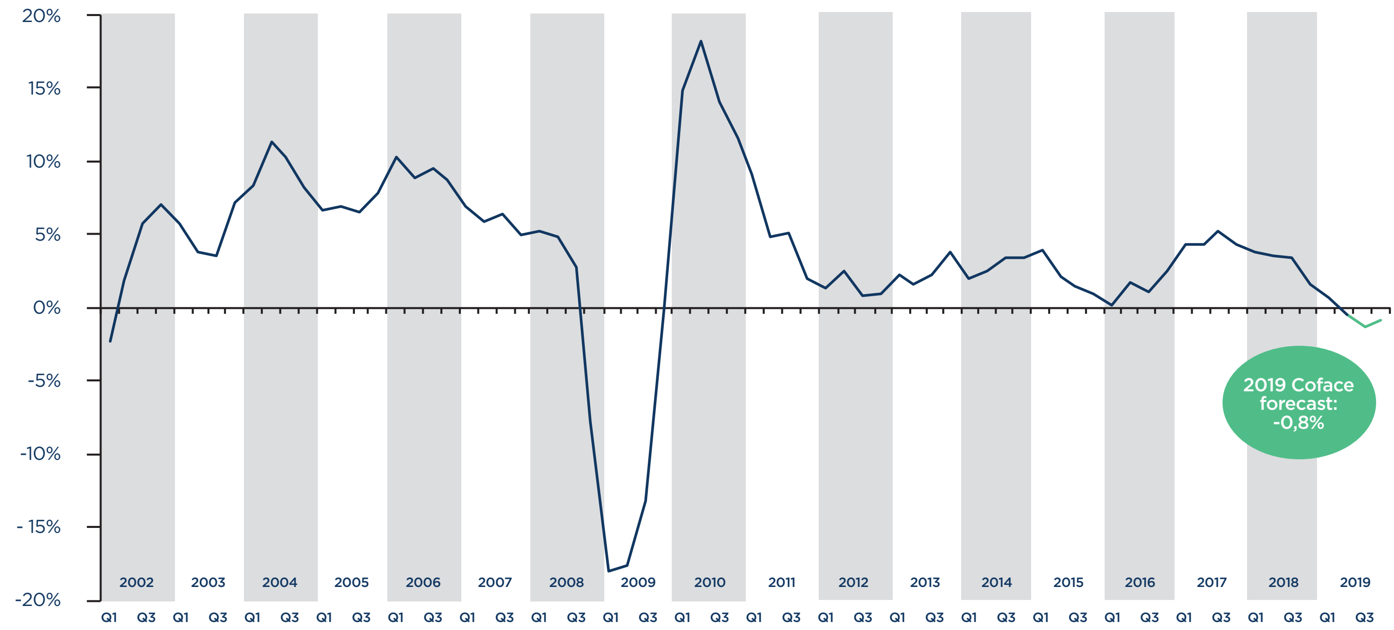
The effects of these monetary policies that set negative nominal interest rates are uncertain. Of course, negative policy rates can stimulate the economy by lowering commercial bank lending rates to households and businesses. Nevertheless, they can also erode banks' profitability by reducing spreads with deposit rates (if the "floor" rate of the latter is zero). However, these lower profits are likely to encourage banks to increase interest rates on loans granted. In theory, the positive effect on activity prevails. At any rate, this is the conclusion of a recent study by the San Francisco Federal Reserve[7] : the effect of a decrease in interest rates in negative territory is between 60 and 90% of an action of the same magnitude in positive territory. The expected impact of recent monetary easing measures in the Eurozone in particular would therefore be real. In practice, the few recent experiences with negative nominal interest rate policies do not provide much clarity. The central banks of the Eurozone, Switzerland, Denmark, Japan and Sweden adopted monetary policies with negative nominal interest rates between 2014 and 2018. At first glance, the results of these policies seem mixed. These ultra-expansionist monetary policies have not allowed inflation to move closer to its target in the first four cases: it has remained at a level very close or even below the one observed before the implementation of negative rates. Sweden seems to be the exception: the adoption of negative nominal key interest rates coincided with a significant rebound in consumer inflation.

In addition to the Eurozone, the United States and China, monetary policy has been eased in many other economies, particularly emerging ones: Mexico, Brazil, India, Indonesia, the Philippines, Malaysia, Korea, Russia, Peru, Egypt, South Africa, Nigeria and Saudi Arabia all have in common that they have a central bank that has cut their main key interest rate at least once since the beginning of the year. This trend accelerated during the summer. Even in Turkey, where the effects of the 2019 crisis are still visible, the central bank did not hesitate to do the same. Among the few exceptions is Argentina, unable to emerge from its exchange rate crisis (**Chart 5**), which deepened in mid-summer following the primary elections that revealed the high probability of defeat of the outgoing President Macri in the presidential election, the first round of which is scheduled on 27 October 2019. In order to limit downward pressure on the peso, the central bank was even forced to introduce capital controls, which had been lifted when President Macri took office in November 2015.

Again, the effects of these more expansionary monetary policies in emerging economies are uncertain. Indeed, in emerging economies, the transmission of the monetary policy via the exchange rate is usually more important than through bank credit compared to advanced economies (the former being less banked). However, this should be put into perspective in the current context: all other things being equal, a fall in the interest rate encourages investors to leave the country's capital in favor of investments abroad of which the return will be seen as more attractive. These capital outflows favor a depreciation of the local currency making exports (imports) more (less) competitive. However, this transmission is less likely to work when other central banks do the same thing: the yield gap between an investment in the local market and an investment abroad does not change, so that the exchange rate and the trade balance are not affected (**Chart 6**).

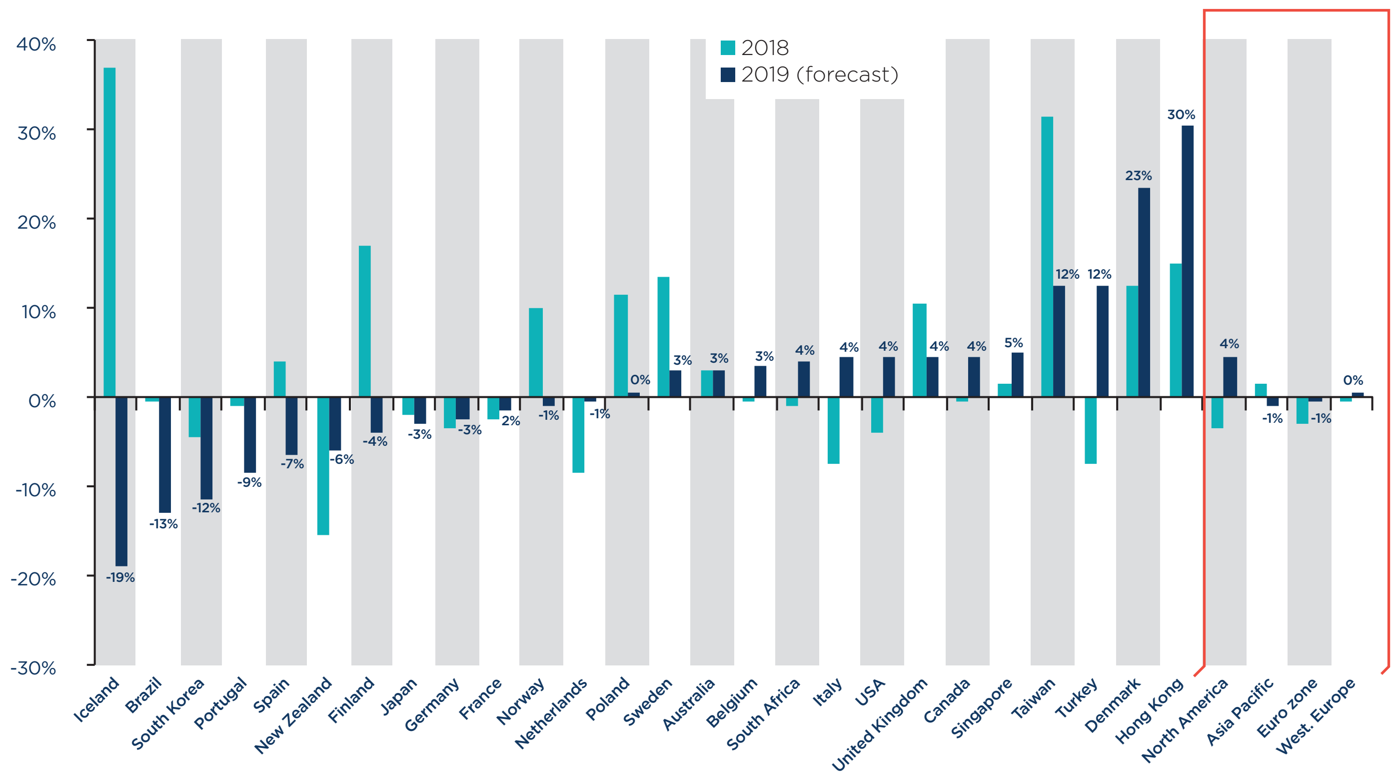
7 Ulate, Mauricio (Septembre 2019): "Going Negative at the Zero Lower Bound: The Effects of Negative Nominal Interest Rates," Document de travail 2019-21 de la Réserve Fédérale de San Francisco. https://doi.org/10.24148/wp2019-21

Chart 1:
Global trade
(yearly % change in volume)



Sources: CPB, Coface

Chart 2:
Annual evolution of corporate insolvencies per country
(in %)



Source: Coface, domestic sources

Chart 3:
Business confidence in the US
(PMI index)

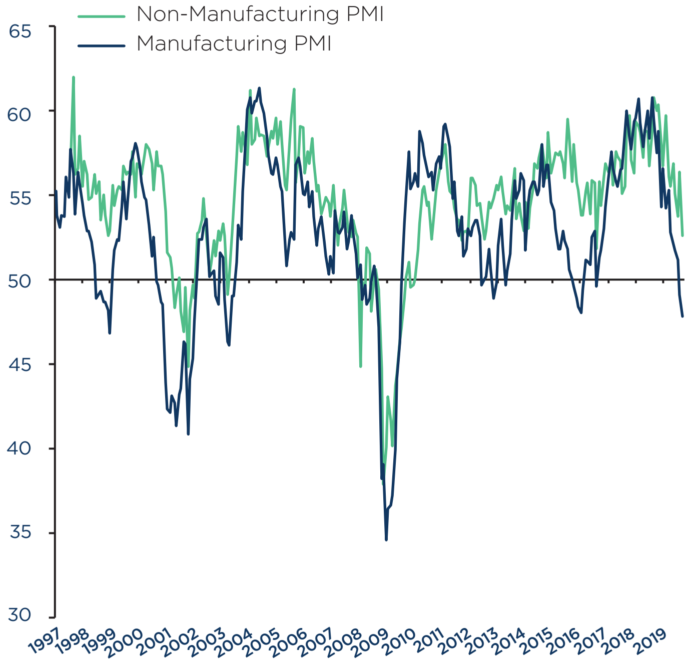


Chart 4:
World: Inflation and Central Bank Policy rates
(%, nominal GDP weights, 34 countries)

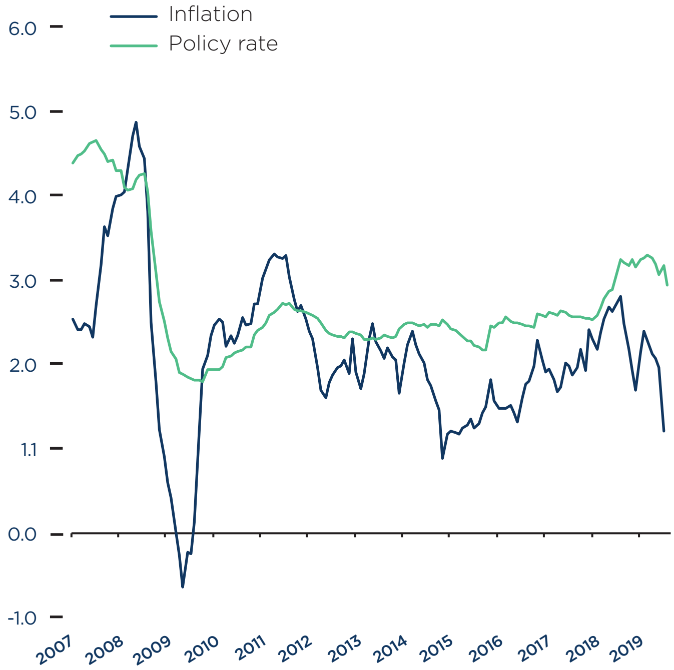


Chart 5:
Variation of the exchange rate vs US dollar
(in % between 1st January and 11th October 2019, increase=appreciation)

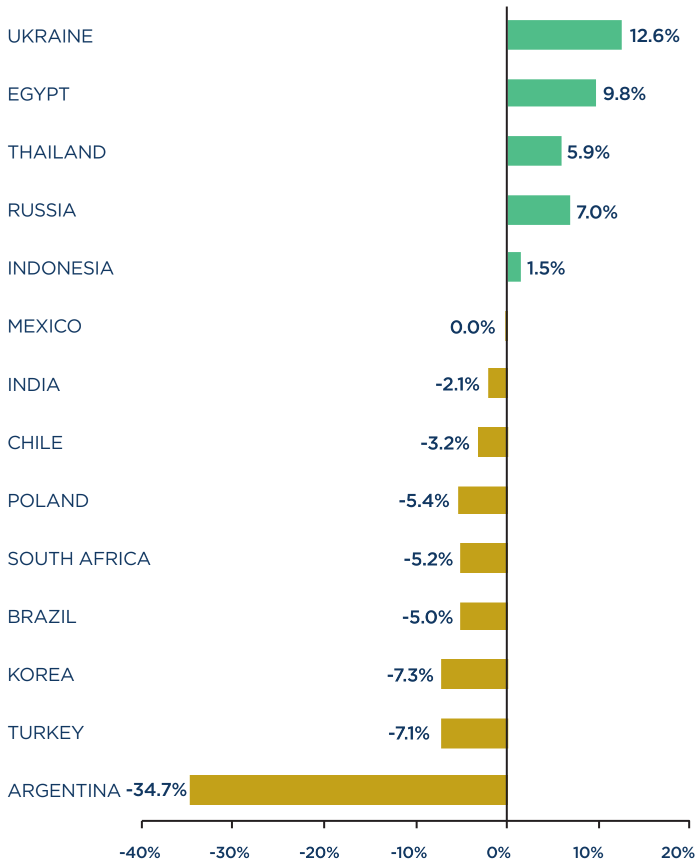
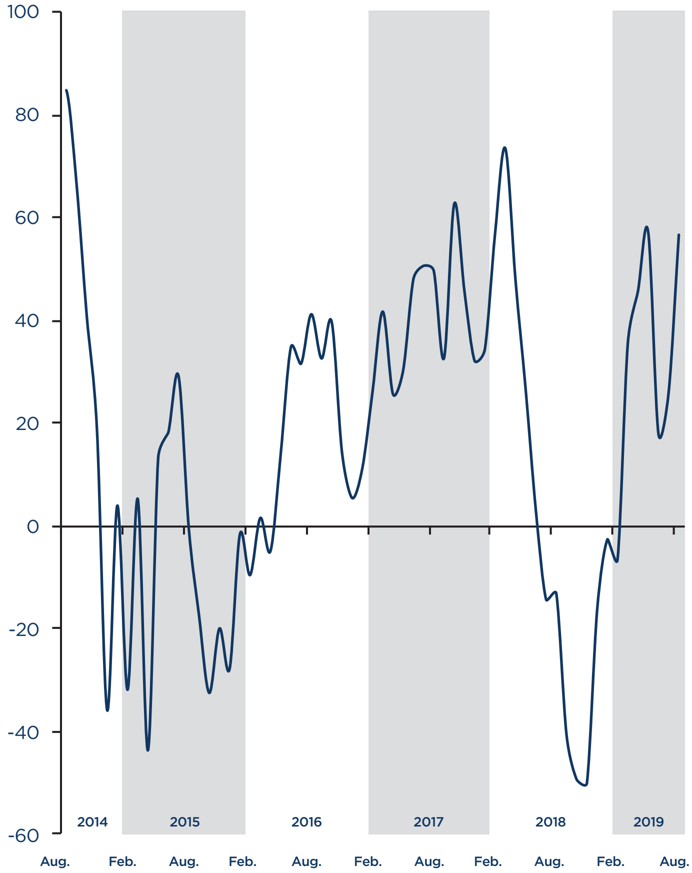


Chart 6:
Capital flows towards 23 emerging countries
(excl. China, in billion USD)



Sources: IIF, Coface

Country Risk Assessment Changes

COUNTRY	Previous Assessment		Current Assessment
MAURITANIA	D	↗	C
HONG KONG	A2	↘	A3

Hong Kong ↘
(Downgrade from A2 to A3)

- The US-China Trade War has had a huge impact on exports. While Hong Kong domestic exports account for only a small proportion of GDP, Chinese re-exports are more significant at 150% of GDP. These have contracted by -4 % YOY on average in the first six months of 2019, and this headwind is expected to last well into 2020.
- Weaker export related income and sentiment has impacted domestic demand, both on the consumption and investment front. Together with pressures on the external front, this contributed to a very weak growth rate of 0.6% YOY in Q1 and Q2. GDP contracted in sequential terms to -0.3% QOQ in Q3.
- Some sectors, including retail, services and transportation are expected to be hit as a result of protests, which started in June 2019 and don't seem to be abating. The impact is two-fold: on the one hand, shopping malls have been forced to close as protestors flooded main streets; but also, tourism numbers declined very significantly in July and August. Weaker demand will further drag growth down in Q3, which will very likely result in a technical recession, before fiscal measures kick in. Fiscal stimulus accounts for 1% of GDP so it won't be enough to move the needle significantly.

Mauritania ↗
(Upgrade from D to C)

- Growth is expected to reach its highest level since 2014 (5.2%) in 2019, specifically due to improved terms of trade and strong performance in non-extractive sectors (agriculture, construction, services).
- The country's fiscal position has improved significantly, and the country now has a primary fiscal surplus.
- In 2018, for the first time since 2011, Mauritania's external debt declined as a percentage of GDP.
- Foreign exchange reserves are on an upward trajectory and the exchange rate has been relatively stable for several months.
- Although contested by the opposition, the transition between Mohamed Ould Abdel Aziz, who has been at the head of the country for 11 years, and Mohamed Ould Ghazouani, who was Minister of Defense between 2018 and 2019, has been relatively smooth in a country regularly marked by political crises throughout its history.

BUSINESS DEFAULT RISK

- A1 Very Low
- A2 Low
- A3 Satisfactory
- A4 Reasonable
- B Fairly High
- C High
- D Very High
- E Extreme
- ↗ Upgrade
- ↘ Downgrade

Sector Risk Assessment Changes

REGIONAL SECTOR RISK ASSESSMENTS

	Asia-Pacific	Central & Eastern Europe	Latin America	Middle East & Turkey	North America	Western Europe
Agri-food	Medium Risk	Medium Risk	High Risk	Medium Risk	High Risk	Medium Risk
Automotive	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk
Chemical	Medium Risk	Medium Risk	High Risk	Medium Risk	Medium Risk	Medium Risk ↘ High Risk
Construction	Very High Risk	High Risk	High Risk	Very High Risk	High Risk	Medium Risk
Energy	High Risk	Medium Risk	High Risk	High Risk	Medium Risk	Medium Risk
ICT*	High Risk	Medium Risk	High Risk	High Risk	Medium Risk	Medium Risk
Metals	High Risk	Medium Risk	High Risk	Very High Risk	Medium Risk	High Risk
Paper	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk ↘ High Risk	High Risk
Pharmaceuticals	Low Risk	Low Risk	Medium Risk	Medium Risk	Low Risk	Medium Risk
Retail	Medium Risk	Medium Risk	Medium Risk	High Risk	High Risk	Medium Risk
Textile-Clothing	High Risk	Medium Risk	High Risk	High Risk	Very High Risk	High Risk
Transport	Medium Risk	High Risk	High Risk	Medium Risk	Medium Risk	Medium Risk
Wood	High Risk	Medium Risk	Medium Risk ↘ High Risk	Medium Risk ↘ High Risk	Medium Risk	Medium Risk ↘ High Risk

* Information and Communication Technologies
Source: Coface

ASIA-PACIFIC

	Asia-Pacific	Australia	China	India	Japan	South Korea
Agri-food	Medium Risk	High Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Automotive	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk
Chemical	Medium Risk	Low Risk	Medium Risk	Medium Risk	Medium Risk	Low Risk
Construction	Very High Risk	Medium Risk	Very High Risk	High Risk	Medium Risk	Very High Risk
Energy	High Risk	Medium Risk	High Risk	High Risk	High Risk	High Risk
ICT*	High Risk	Medium Risk	High Risk	Very High Risk	Medium Risk	Medium Risk ↘ High Risk
Metals	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk
Paper	Medium Risk	High Risk	Medium Risk	Medium Risk	High Risk	Medium Risk
Pharmaceuticals	Low Risk	Low Risk	Low Risk	Low Risk	Low Risk	Low Risk
Retail	Medium Risk	High Risk	Medium Risk	High Risk	Medium Risk	Medium Risk
Textile-Clothing	High Risk	High Risk	High Risk	High Risk	High Risk	Medium Risk
Transport	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	High Risk
Wood	High Risk	High Risk	High Risk	Medium Risk	Medium Risk	Medium Risk

* Information and Communication Technologies
Source: Coface

SOUTH KOREA

ICT ↘
(Medium Risk to High Risk)

- Trade war between Japan and South Korea will hurt ICT manufacturers, who depend on Japanese supply of key inputs.
- South Korean ICT manufacturers have been experiencing pressures on profits, stemming from subdued semiconductor prices. Weaker demand has dampened the outlook for the product.
- The South Korean ICT sector remains exposed to risks surrounding the US-China trade war. South Korea is exposed as an upstream supplier of components. As such, it is exposed to supply chain shifts but more importantly, weaker demand from China as the country pushes towards self-sufficiency goals in the ICT sector.

BUSINESS DEFAULT RISK

- Low Risk
- Medium Risk
- High Risk
- Very High Risk
- ↗ Upgrade
- ↘ Downgrade

CENTRAL & EASTERN EUROPE

	Central & Eastern Europe	Czechia	Poland	Romania
Agri-food	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Automotive	High Risk	High Risk	High Risk	Medium Risk
Chemical	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Construction	High Risk	Medium Risk	High Risk	High Risk
Energy	Medium Risk	Medium Risk	Medium Risk	High Risk
ICT*	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Metals	Medium Risk	High Risk	Medium Risk	High Risk
Paper	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Pharmaceuticals	Low Risk	Low Risk	Low Risk	Low Risk
Retail	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Textile-Clothing	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Transport	High Risk	Medium Risk	High Risk	Medium Risk
Wood	Medium Risk	Medium Risk	Medium Risk	Medium Risk

** Information and Communication Technologies*
Source: Coface

BUSINESS DEFAULT RISK

Low Risk

Medium Risk

High Risk

Very High Risk

Upgrade

Downgrade

Decoding the WORLD ECONOMY
3rd quarter 2019

coface FOR TRADE

coface
FOR TRADE

COUNTRY RI

161 COUNTRIES UNDER THE MAGNIFYING GLASS

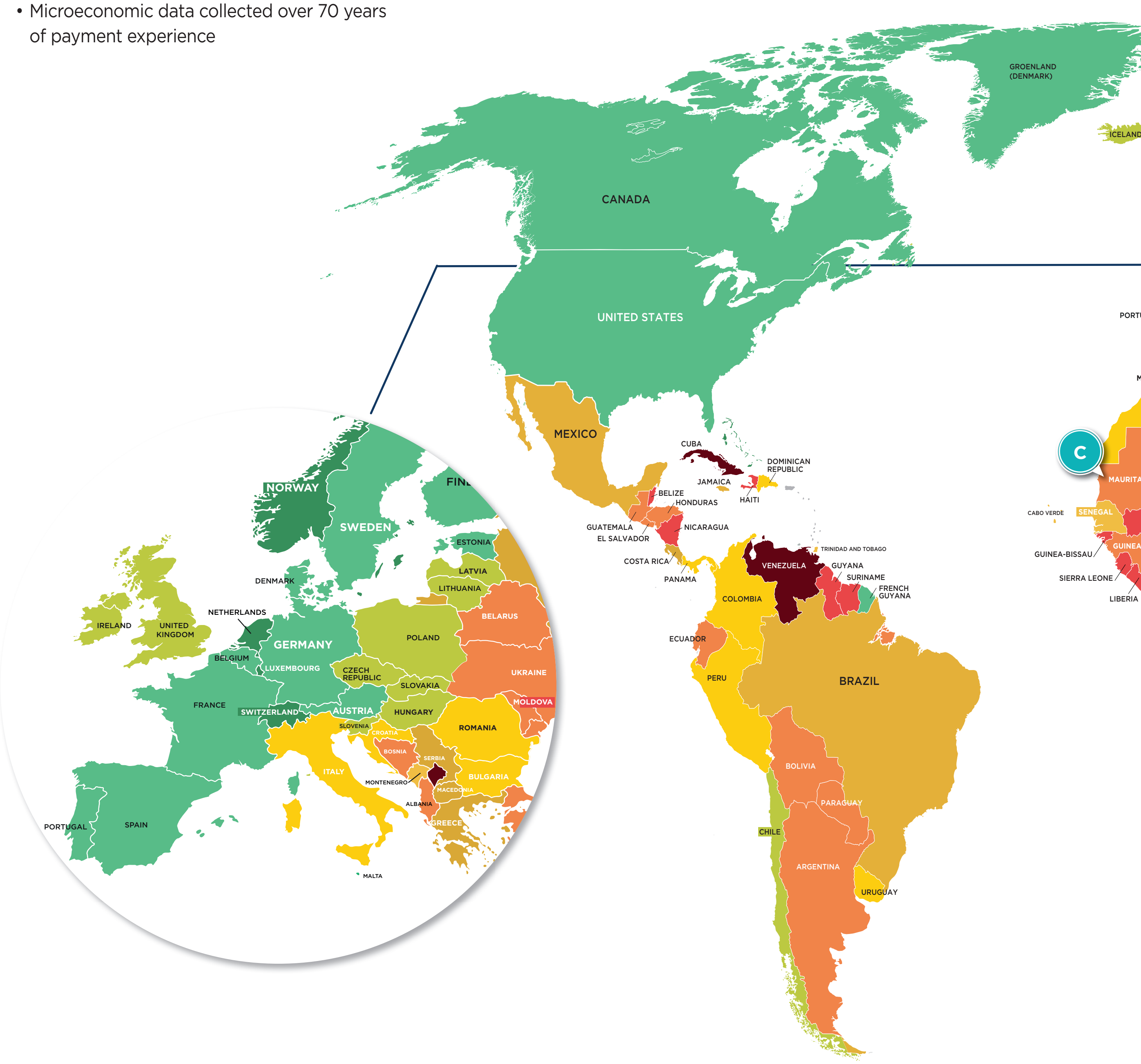
A UNIQUE METHODOLOGY

- Macroeconomic expertise in assessing country risk
- Comprehension of the business environment
- Microeconomic data collected over 70 years of payment experience

BUSINESS DEFAULTING RISK

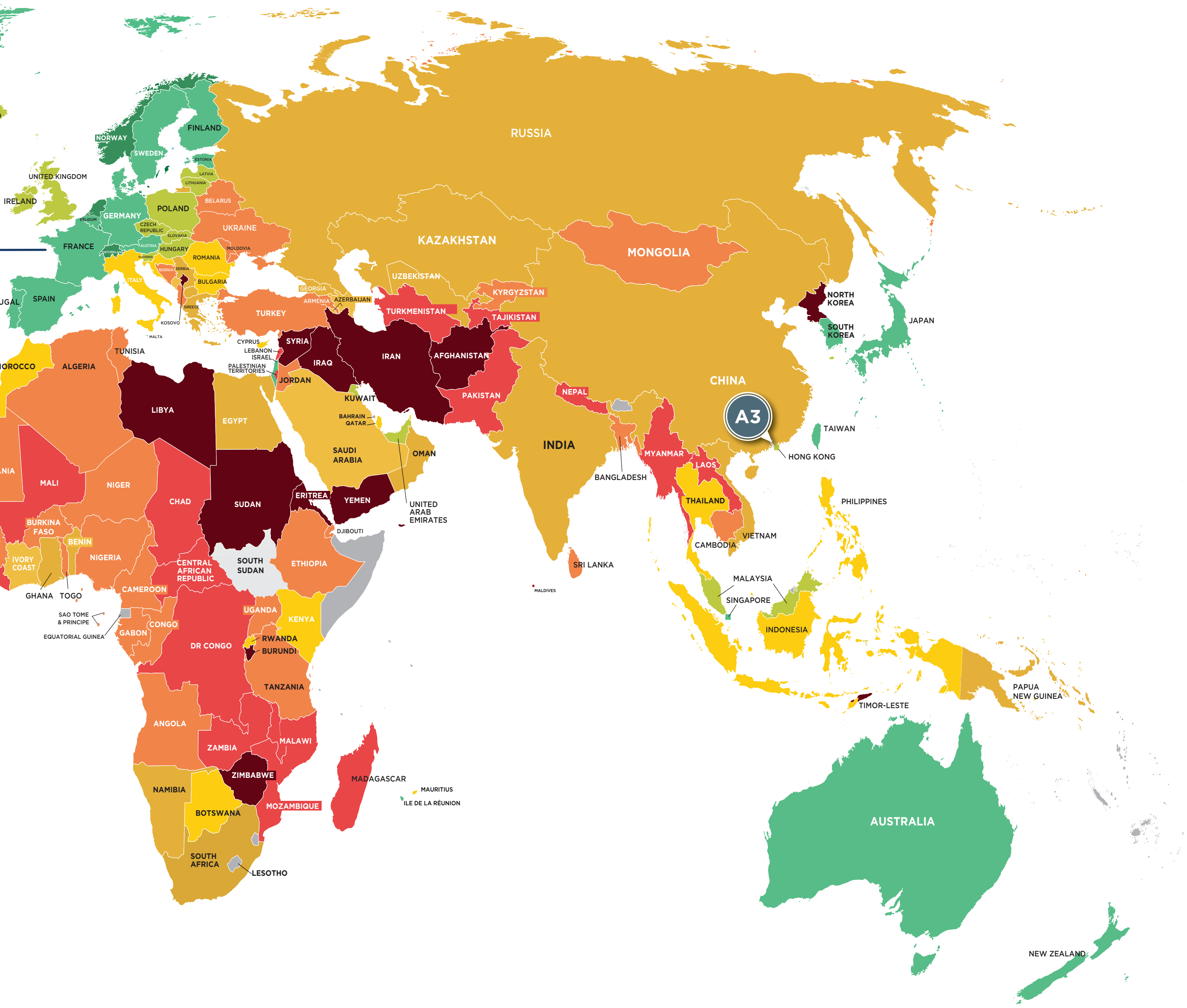
UPGRADES

DOWNGRADES



SK ASSESSMENT MAP

A1	A2	A3	A4	B	C	D	E
VERY LOW	LOW	SATISFACTORY	REASONABLE	FAIRLY HIGH	HIGH	VERY HIGH	EXTREME



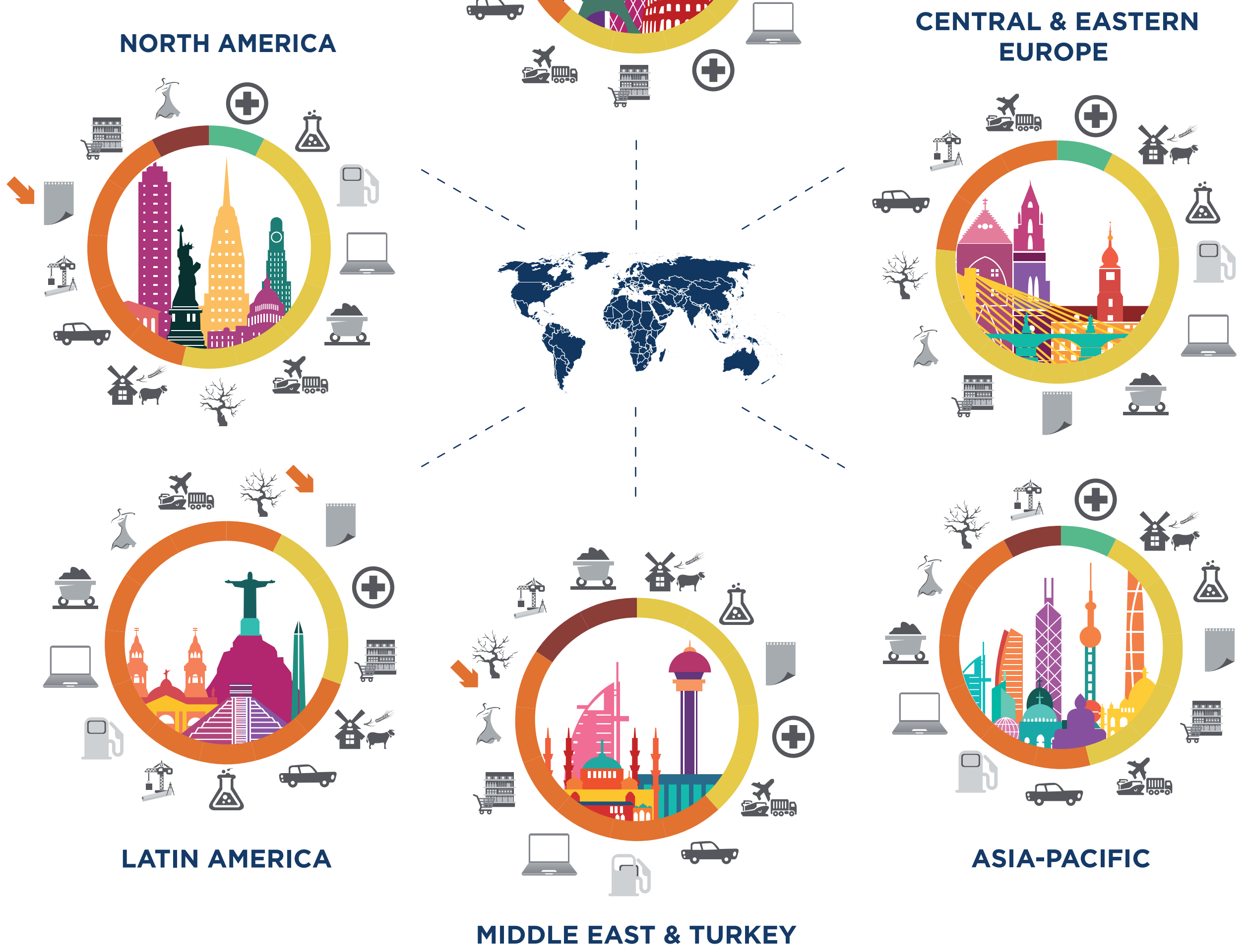
SECTOR RISK ASSESSMENTS
3rd quarter 2019

13 MAJOR SECTORS ASSESSED WORLDWIDE

Coface assessments are based on 70 years of Coface expertise

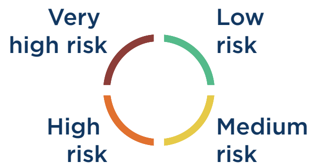
Financial data published by listed companies from 6 geographical regions

5 financial indicators taken into account: turnover, profitability, the net debt ratio, cashflow, and claims observed by our risk managers



agri-food	ICT*	textile-clothing	Upgrade
automotive	metals	transport	Downgrade
chemical	paper	wood	
construction	pharmaceuticals		
energy	retail		

* Information and Communication Technologies



LATIN AMERICA

	Latin America	Argentina	Brazil	Chile	Mexico
Agri-food	High Risk	High Risk	High Risk	High Risk	High Risk
Automotive	High Risk	Very High Risk	Medium Risk	Low Risk ↘ Medium Risk	High Risk
Chemical	High Risk	High Risk	High Risk	High Risk	High Risk
Construction	High Risk	High Risk ↘ Very High Risk	High Risk	High Risk	Very High Risk
Energy	Medium Risk	Medium Risk	Medium Risk	Low Risk	Very High Risk
ICT*	High Risk	Very High Risk	Medium Risk	Medium Risk	High Risk
Metals	High Risk	High Risk	High Risk	Medium Risk	High Risk
Paper	Medium Risk	High Risk	Medium Risk	Medium Risk	Medium Risk
Pharmaceuticals	Medium Risk	Medium Risk	Medium Risk	Low Risk	Medium Risk
Retail	Medium Risk	Very High Risk	Medium Risk	Medium Risk	Medium Risk
Textile-Clothing	High Risk	Very High Risk	High Risk	Medium Risk ↘ High Risk	High Risk
Transport	High Risk	High Risk	High Risk	Medium Risk	Medium Risk
Wood	Medium Risk ↘ High Risk	High Risk	High Risk	Medium Risk	Medium Risk ↘ High Risk

* Information and Communication Technologies
Source: Coface

ARGENTINA

Construction ↘
(High Risk to Very High Risk)

- Sector strongly hit by the economic recession. The poor fiscal position has hit public investments hard. The same happened with private investments, in the absence of a perspective of economic resumption and driven by the uncertain political scenario (with high chances of a change of government coming from the presidential elections of October 2019).
- Activity levels in Argentina's construction sector dropped 1.7% YoY in July 2019, marking the eleventh month of declining values, according to INDEC. It dropped 8.3% in the first seven months of 2019 YoY.
- The strong depreciation of the exchange rate (33% year-to-date until September 6) increases the costs of importing capital goods. Finally, policy rate stands at prohibitive levels, undermining the credit market (currently at roughly 85%).

CHILE

Automotive ↘
(Low Risk to Medium Risk)

- Automotive retail sales have decelerated in recent months. According to the National Automobile Association of Chile (ANAC), new cars sales rose by 0.6% YOY, after five months of downward trend. As for the January-July period, 218,494 units were sold, marking a drop of 6.4% compared to the same period in 2018.
- The industry predicts that 380,000-390,000 units will be sold in 2019 compared to 417,038 in 2018. The relatively weaker performance can be partially explained by the year-to-date lower economic momentum.
- The latter, in counterpart, is a side effect of lower international copper prices and the negative impact of the worst drought in 60 years on mining and agro activities.

Textile-Clothing ↘
(Medium Risk to High Risk)

- Low competitiveness and high vulnerability to Asian imports (mostly coming from China).
- According to GDP figures for Q2 2019, production of textiles, clothing, leather and footwear dropped by 10.4% YoY (-9 % YoY in Q1 2019).
- According to national statistical institute INE, wholesale of textile products, clothing and footwear dropped by 4.6% in the first seven months of the year YoY. Finally, retail sales of clothing, footwear and accessories dropped by 1.3% in the same comparison basis.

MEXICO

Wood ↘
(Medium Risk to High Risk)

- According to the national statistical institute Inegi, wood production shrunk by 0.3% YoY in the first seven months of 2019. Manufacture of furniture, mattresses and blinds dropped by 4.9% in the same comparison basis.
- Due to the increase of fires this year and the growing imports - of 83% of the total used in the country - the timber and furniture industry expects a 4.5% decline in 2019. According to the National Chamber of the Wood Industry (Canainma), the fires were fought on time, but they were left adrift as a result of the lack of resources for their control. This is a consequence of the National Forestry Commission (Conafor) getting 50% of its budget cut for this year.
- Last but not least, domestic demand should remain undermined by decelerating economic activity.

BUSINESS DEFAULT RISK

Low Risk
Medium Risk
High Risk
Very High Risk
Upgrade
Downgrade

MIDDLE EAST & TURKEY

	M. East & Turkey	Israel	Saudi Arabia	Turkey	UAE
Agri-food	Medium Risk	Medium Risk	Medium Risk	High Risk	Medium Risk
Automotive	High Risk	Low Risk ↘ Medium Risk	High Risk	Very High Risk	Medium Risk
Chemical	Medium Risk	Low Risk	Medium Risk	High Risk	Medium Risk
Construction	Very High Risk	High Risk	Very High Risk	Very High Risk	High Risk
Energy	High Risk	Medium Risk	Medium Risk	Very High Risk	Medium Risk
ICT*	High Risk	Medium Risk	High Risk	Very High Risk	High Risk
Metals	Very High Risk	Medium Risk	Very High Risk	Very High Risk	High Risk
Paper	Medium Risk	Medium Risk	Medium Risk	High Risk	Medium Risk
Pharmaceuticals	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Retail	High Risk	High Risk	Medium Risk	Very High Risk	Medium Risk
Textile-Clothing	High Risk	High Risk	Medium Risk	High Risk	Medium Risk
Transport	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Wood	Medium Risk ↘ High Risk	Medium Risk ↘ High Risk	Medium Risk	High Risk	Medium Risk

* Information and Communication Technologies
Source: Coface

ISRAEL

Automotive ↘
(Low Risk to Medium Risk)

- Sales are very vulnerable to trade and environmental risks. The change in green tax regulations moved car demand upfront so Q2 was a slowdown period for car sales. This exposure to the regulation changes creates an uncertainty for car dealers by increasing demand volatility. For companies having a high debt level, changes in demand would weigh on turnover and deteriorate cash flow management. Yet risks remain quite balanced with a low level of inflation, low interest rates and full employment.

Wood ↘
(Medium Risk to High Risk)

- In the wood sector, there are small manufacturers, but a lot of them have gone bankrupt. The carpentry business is risky and most of the wood (furniture etc.) is imported, which represents competition for local producers. The very small size of wood producers represents higher risk of bankruptcy.

BUSINESS DEFAULT RISK

Low Risk
Medium Risk
High Risk
Very High Risk
↗ Upgrade
↘ Downgrade

NORTH AMERICA

	North America	Canada	United States
Agri-food	High Risk	Medium Risk	High Risk
Automotive	High Risk	Medium Risk ↘ High Risk	High Risk
Chemical	Medium Risk	Medium Risk	Medium Risk
Construction	High Risk	High Risk	High Risk
Energy	Medium Risk	High Risk	Medium Risk
ICT*	Medium Risk	Medium Risk	Medium Risk
Metals	Medium Risk	High Risk	Medium Risk
Paper	Medium Risk ↘ High Risk	Medium Risk ↘ High Risk	Medium Risk ↘ High Risk
Pharmaceuticals	Low Risk	Low Risk	Low Risk
Retail	High Risk	High Risk	High Risk
Textile-Clothing	Very High Risk	High Risk	Very High Risk
Transport	Medium Risk	Low Risk	Medium Risk
Wood	Medium Risk	High Risk	Medium Risk

** Information and Communication Technologies - Source: Coface*

CANADA

Automotive ↘
(Medium Risk to High Risk)

- Automotive products and auto parts output continued to fall in Q2 2019 (-2.6% YOY after -3.8% in Q1 and -0.6% in 2018), driven by motor vehicles production (-1.7% YOY in Q2 after -3.8% in Q1). In addition, the outlook is also negative on the demand side: while car sales fell further (-15% YOY in July after -13.6% in Q2), truck sales (74% of total registrations) continued to decrease slightly (-0.2% YOY after -0.1%). As a result, total vehicles sales contracted further: -4.6% YOY in July after -4.7% in Q2. The sector is affected by the increasing cost of lending, due to the higher interest rate.

Paper ↘
(Medium Risk to High Risk)

- Wood production fell by 6.9% YOY in Q2 2019 (after already -7.2% in Q1). The wood industry is affected by US tariffs on lumber (21%) and by the construction sector slowdown. Moreover, paper production also continued to decrease sharply (-9.9% YOY in Q2 2019 after -5.5% YOY in Q1). Paper output is around 30% below its pre-crisis level. The situation is worsening for the paper industry: wood pulp prices have been declining since the beginning of the year - due to the economic slowdown in China (that buys 35% of wood pulp globally) - and are expected to follow this trend.

UNITED STATES

Paper ↘
(Medium Risk to High Risk)

- Both paper and wood production contracted in the three months to August (respectively -4.9% YOY and -1%). The situation is worsening for the paper industry: China is planning to tax paper products imports from the United States from 15th December onward. As more than 30% of wood, paper and wood pulp exports go to China, the sector is likely to be affected. Wood pulp prices have been declining since the beginning of the year - due to the economic slowdown in China (that buys 35% of wood pulp globally) - and are expected to follow this trend.

BUSINESS DEFAULT RISK

- Low Risk
- Medium Risk
- High Risk
- Very High Risk
- ↗ Upgrade
- ↘ Downgrade

WESTERN EUROPE

	Western Europe	Austria	France	Germany	Italy	Netherlands (the)	Spain	Switzerland	United Kingdom
Agri-food	Medium Risk	Low Risk	Medium Risk	Medium Risk	High Risk	Medium Risk	Medium Risk	Medium Risk	High Risk
Automotive	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk	Low Risk ↘ Medium Risk	Very High Risk
Chemical	Medium Risk ↘ High Risk	Low Risk	High Risk	Medium Risk ↘ High Risk	High Risk	Medium Risk	Medium Risk	Low Risk	High Risk
Construction	Medium Risk	Medium Risk	Medium Risk	Low Risk	Very High Risk	Medium Risk	Medium Risk	High Risk	Very High Risk
Energy	Medium Risk	Medium Risk	Medium Risk	Medium Risk	High Risk	Medium Risk	High Risk	Medium Risk	High Risk
ICT*	Medium Risk	Medium Risk	Low Risk	Medium Risk	High Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk
Metals	High Risk	Medium Risk	High Risk	High Risk	High Risk	Medium Risk	Medium Risk	High Risk	Very High Risk
Paper	High Risk	Medium Risk	High Risk	High Risk	High Risk	High Risk	Medium Risk	High Risk	High Risk
Pharmaceuticals	Medium Risk	Low Risk	Low Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Low Risk	Medium Risk
Retail	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	High Risk
Textile-Clothing	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk	High Risk	Medium Risk	High Risk
Transport	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Medium Risk	Low Risk	Medium Risk	Medium Risk
Wood	Medium Risk ↘ High Risk	Medium Risk	Medium Risk	Medium Risk ↘ High Risk	High Risk	Medium Risk	Medium Risk	Medium Risk	High Risk

* Information and Communication Technologies
Source: Coface

BUSINESS DEFAULT RISK

- Low Risk
- Medium Risk
- High Risk
- Very High Risk
- ↗ Upgrade
- ↘ Downgrade

GERMANY

Chemical ↘

(Medium Risk to High Risk)

- The sentiment in the German chemical sector deteriorated. The Ifo business climate for chemical products went down from around 9 points in the first quarter of 2019 to -10.8 points in August 2019. The sub-indicators for business expectations, employment and production fell (double-digit) into the negative territory. This sobering mood is reflected in the ZEW-sentiment indicator for this sector, too.
- In the yearly comparison, new orders and production have negative growth rates since October 2018. In June/July 2019 the new orders and production rates were negative (double-digit). The exports growth rate went negative, coming from 14% in February 2019, and the imports are declining as well.
- As we are downgrading our GDP forecasts from 0.8% to 0.5% YOY this year and from 1.2% to 0.5% for next year, the domestic demand for chemical products will be low. The German chemical sector is highly related to the automotive sector (on the petro-chemical side but also as in an input good for plastics and other components of automobiles). As we do not see signs for a recovery of the automotive sector, the outlook for the chemical sector is been dragged down as well. The demand from abroad is weak as well. The decrease of the growth rate of global trade is weighing on the sector globally.
- Additionally, the input costs of the chemical sector are increasing. On top of the already very high electricity prices in Germany, the oil prices shot up following the attack of the world's largest oil processing plant in Saudi-Arabia. The attack cut the production of global crude oil output by 6% and led to an oil price increase of around 20%. Big German chemical companies like BASF and Bayer have already downgraded their profit outlook. Special chemical producers like Evonik have the same problems.

Wood ↘

(Medium Risk to High Risk)

- The business climate for wood products is hovering over the negative territory (2.2 points in August) for the first time in five years. Specifically business expectations are down (deep in the negative area) and the sub-indicator for production fell in the negative territory, too.
- The production of wood products is negative in the yearly comparison (-2.1% in June 2019 after -4% in May), but can be volatile. The capacity utilization in the third quarter of 2019 (not-seasonally adjusted) is the lowest one (in yearly comparison) since 2015. Insolvencies increased compared to last year.
- The last summer worsened the situation in the German forests, which is called "Waldsterben" ("forest die-back"). Climate change has severe effects on German forests. The climate is too hot and too dry to sustain the health of the trees. The forests have not regenerated from the hot and dry summer of last year and this summer Germany hit new high-temperature records in several places (and not only one place as previously). There are bigger forest fires than in the past.
- Additionally, the bark beetle is destroying big forests of spruces. In total, around 110 000 hectare of forests were destroyed because of heat, fire and pests.

SWITZERLAND

Automotive ↘

(Low Risk to Medium Risk)

- Passenger car registrations decreased by 9.5% in August from the same month last year, after having remained flat in July and already decreased by 9.8% in June.
- Auto parts exports could be affected by global woes in the sector.

OTHER COUNTRIES

	Russia	South Africa
Agri-food	Low Risk	High Risk
Automotive	Medium Risk	High Risk
Chemical	Low Risk	Medium Risk
Construction	High Risk	Very High Risk
Energy	Medium Risk	High Risk
ICT*	Medium Risk	Medium Risk
Metals	High Risk	High Risk
Paper	Medium Risk	Medium Risk
Pharmaceuticals	High Risk	Medium Risk
Retail	Medium Risk	High Risk
Textile-Clothing	High Risk	High Risk
Transport	High Risk	High Risk
Wood	Medium Risk	High Risk

* Information and Communication Technologies
Source: Coface

BUSINESS DEFAULT RISK

- Low Risk
- Medium Risk
- High Risk
- Very High Risk
- Upgrade
- Downgrade

COFACE GROUP ECONOMISTS

Julien Marcilly
Chief Economist
Paris, France

Sarah N'Sondé
Head of Sector Analysis
Paris, France

Bruno De Moura Fernandes
Economist, North America, France, and the United Kingdom
Paris, France

Carlos Casanova
Economist, Asia-Pacific
Hong Kong

Christiane von Berg
Economist, Northern Europe
Mainz, Germany

Dominique Fruchter
Economist for Caucasus, the CIS, the Balkans, Switzerland & Ukraine
Paris, France

Erwan Madelénat
Sector Economist and Data Scientist
Paris, France

Grzegorz Sielewicz
Economist, Central & Eastern Europe
Warsaw, Poland

Khalid Aït-Yahia
Sector Economist and Statistician
Paris, France

Patricia Krause
Economist, Latin America
São Paulo, Brazil

Ruben Nizard
Economist, Africa
Paris, France

Seltem Iyigun
Economist, Middle East & Turkey
Istanbul, Turkey

With the help of **Aroni Chaudhuri**
Coordinator
Paris, France

DISCLAIMER

October 2019 — Layout: increa ✱ — Photo: AdobeStock

COFACE SA
1, place Costes et Bellonte
92270 Bois-Colombes
France

www.coface.com

coface
FOR TRADE