

HSBC Emerging Markets Index Q3 2011

Emerging market growth begins to stall as manufacturing succumbs to lost momentum in world trade

Key points

- HSBC Emerging Markets Index dips to 51.9 in Q3 2011 in troubled global economy
- Output growth at slowest in nine quarters, manufacturing output growth turns negative
- Manufacturing slowdown most acute in South Africa, Taiwan and Brazil; only Turkey and Israel record faster growth
- Service sector records modest growth but business optimism slides to lowest level this year
- Input cost inflation eases further amid persistent policy tightening across the emerging world

Summary

Emerging market growth slowed to its weakest level in nine quarters in the third quarter of 2011, reflecting the continued decline in world trade volumes, the HSBC Emerging Markets Index (EMI) shows.

The EMI slid to 51.9, down from 54.2 in the second quarter, the fourth-lowest reading in the series history.

Sluggish developed market demand led to reduced output from almost all emerging markets surveyed. Producers reduced their work backlog to sustain activity levels but the resulting spare capacity suggests that imminent job losses are inevitable.

Emerging market manufacturing output fell in Q3, bringing to a close nine successive quarters of growth. In contrast, service providers saw business activity increase over the quarter, but at the slowest pace of expansion since Q2 2009.

Stephen King, HSBC's Chief Economist, said: "It is now apparent that world trade growth peaked in the first quarter. Companies in the emerging world have reacted by clearing their order backlogs at a faster rate than before, helping to support activity near-term. But in the absence of any quick rebound in trade momentum, the weakness revealed in this latest EMI is likely to show up in future employment losses. Already, jobs growth in the emerging world appears to have stagnated.

"While emerging nations do not face the same deleveraging imperative as the developed world, they nevertheless suffer their fair share of contagion in an increasingly "risk-off" environment. While, over the long-term, there is clear evidence of economic de-coupling, there is not much evidence of financial market de-coupling on a day-to-day basis.

"Abating inflationary pressures creates a little more room for policy flexibility but it would be wrong to conclude that emerging nations are about to launch stimulus on a scale similar to that seen in 2008/09. It therefore seems increasingly likely that emerging nations will not be able fully to offset the endemic weakness in the developed world, implying that the pace of global economic growth will remain well below 3% in both 2011 and 2012, a disappointing performance relative to past history, notwithstanding the sound underlying economic fundamentals on offer in many parts of the emerging world."

Manufacturing production decreased in Brazil, China, Singapore, South Africa, South Korea and Taiwan. South African and Taiwanese manufacturers recorded particularly marked rates of decline in output, followed by Brazil, where production fell at the fastest rate since Q1 2009. Meanwhile, China and Singapore recorded marginal and modest rates of reduction respectively.

Fred Neumann, HSBC's co-head of Asian Economics, said: "While Asia continues to grow faster than the developed world, the region has not been immune to weakening global trade and rising uncertainty in the US and Eurozone. While fragile, employment and consumption will continue to offset sluggish export demand. Inflationary risks continue to loom but the emerging world is better placed to employ monetary tools to tame price pressures.

"HSBC's EMI points to the potential of Asia's services sector to keep emerging markets growth steady, even if activity and sentiment in this sector eased in 3Q11. Asian businesses engaged in services have the opportunity to leverage resilient domestic demand. Asian investors will continue to hunt for 'safety' amidst increasingly turbulent financial markets and may continue to look to emerging markets assets for protection and growth."

Eastern European manufacturers generally fared better than emerging Asia firms during Q3, but all saw production growth moderate over the quarter. Russia recorded only a marginal increase in factory output, while rates of expansion slowed to recent lows in the Czech Republic and Poland. Meanwhile, growth in Indian manufacturing slowed to a two-and-a-half year low. Conversely, Turkey and Israel were the only emerging market manufacturing sectors to record a faster increase in output levels.

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Against a backdrop of muted global demand, emerging market manufacturers reported lower volumes of new export business for the first time in nine quarters. Foreign order levels fell across the majority of markets, with the Czech Republic, Saudi Arabia and UAE the only exceptions. Of the big-four emerging markets, Brazil and India recorded the fastest rates of decline in new export orders, while China registered only a marginal reduction.

Service sector activity growth eased to a nine-quarter low in Q3 2011, with rates of expansion slowing across all of the big-four emerging markets. When questioned about the prospects for activity over the next year, emerging market service providers expressed the third-lowest degree of optimism since data were first compiled in Q4 2005. Business confidence dipped to a series-record low in China, while Russian service sector firms were the least optimistic in ten quarters.

In a continuation of a trend observed over recent EMIs, the latest survey provides further evidence to suggest that persistent policy tightening across the emerging world has contributed to weakening inflation pressures. The rate of input cost inflation eased to a four-quarter low across EMI markets. Of the largest emerging markets, Brazil (two-year low), China (slowest in four quarters) and Russia (weakest in one-and-a-half years) all recorded slower increases in average costs. With input price inflation weaker, emerging market companies raised their output charges at the least marked pace for a year, with rates of increase easing across both services and manufacturing.

With inflows of new business increasing at a reduced rate, companies ate into their backlogs of work to help sustain activity levels, suggesting an element of spare capacity across the emerging world. Consequently, employment growth as measured across manufacturing and services eased to the slowest for nine quarters, reflecting a weaker rate of job creation in services and a stagnation of manufacturing employment. India recorded a decrease in headcounts for the first time since Q1 2009, while Brazil, China and Russia all recorded weaker rates of employment growth.

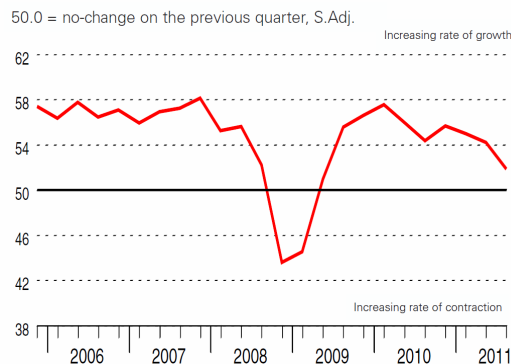
The HSBC EMI is calculated using the long-established PMI data produced by global financial information services company Markit. HSBC announced a partnership in 2009 with Markit to sponsor and produce a number of emerging market PMIs.

The HSBC EMI is released quarterly and is available via:

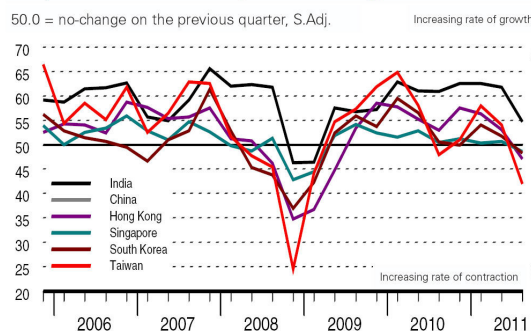
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The next HSBC EMI will be released on 9 January 2012.

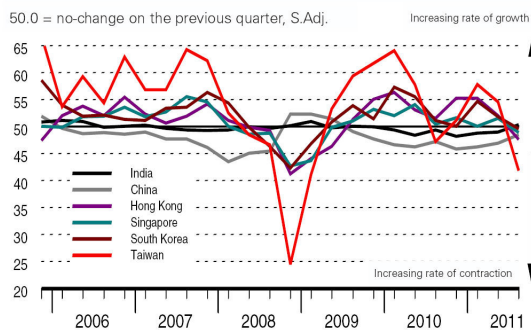
EMI (all-sector output)



Output in Asia countries (manufacturing)



New export orders in Asia countries (manufacturing)



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Notes to Editors:

The HSBC Emerging Markets Index (EMI) is a weighted composite indicator derived from national *Purchasing Managers' Index*TM (*PMI*TM) surveys in the emerging markets of Czech Republic, Hong Kong, Israel, Mexico, Poland, Singapore, South Africa, South Korea, Taiwan, Turkey, UAE, Saudi Arabia and the increasingly important BRIC economies of Brazil, Russia, India and China. These surveys collectively track business conditions in over 5,800 reporting companies.

The *Purchasing Managers' Index*TM (*PMI*TM) surveys on which the EMI is based have become the most closely-watched business surveys in the world, with an unmatched reputation for accurately anticipating official data. The survey data are collected using identical methods in all countries, with survey panels stratified geographically and by International Standard Industrial Classification (ISIC) group, based on contributions to GDP.

Survey responses reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators, a 'diffusion' index is produced, which reflects the percentage of positive responses plus a half of those responding 'the same'. Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50 indicates an overall increase in that variable, below 50 an overall decrease. All data are seasonally adjusted.

Data collected at the national level for manufacturing and services are then weighted together according to relative contributions to national or regional GDP to produce indicators at the national whole economy or aggregate emerging market level.

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Markit:

Markit is a leading, global financial information services company with over 2,200 employees. The company provides independent data, valuations and trade processing across all asset classes in order to enhance transparency, reduce risk and improve operational efficiency. Its client base includes the most significant institutional participants in the financial market place. For more information please see www.markit.com

Markit Economics:

Markit Economics is a specialist compiler of business surveys and economic indices, including the *Purchasing Managers' Index*TM (*PMI*TM) series, which is now available for 32 countries and also for key regions including the Eurozone. The *PMIs* have become the most closely watched business surveys in the world, favoured by central banks, financial markets and business decision makers for their ability to provide up-to-date, accurate and often unique monthly indicators of economic trends.

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