marketmonitor

adapting to the challenging economic environment

October 2009

Still a mixed picture

You'll see from the reports in this edition of Market Monitor that, while there are tentative signs of economic stabilisation, these are tempered by indicators that still advise caution for future trade. Germany has recorded positive growth since the summer, but we still expect bank lending to continue to decline. Spain, in contrast, records negative growth forecasts for the short- and mid-term, but at least our indicators show that the high tide of payment defaults and insolvencies may finally have peaked. In the UK, however, a turnaround in the rising insolvency trend is still not in sight, and the troubled construction sector is forecast to continue to suffer into 2010. That said, the car scrappage scheme, which started later than in many other countries, will provide some cushion for the automotive sector in the coming six months.

Against this background, we continue to urge caution, not just when embarking on new trading ventures, but also in trade with established customers. Essentially, businesses need to tread more carefully in ALL their sales transactions – monitoring changes in the payment behaviour of current customers and taking extra care in assessing the financial strength of new prospects.

In this issue…

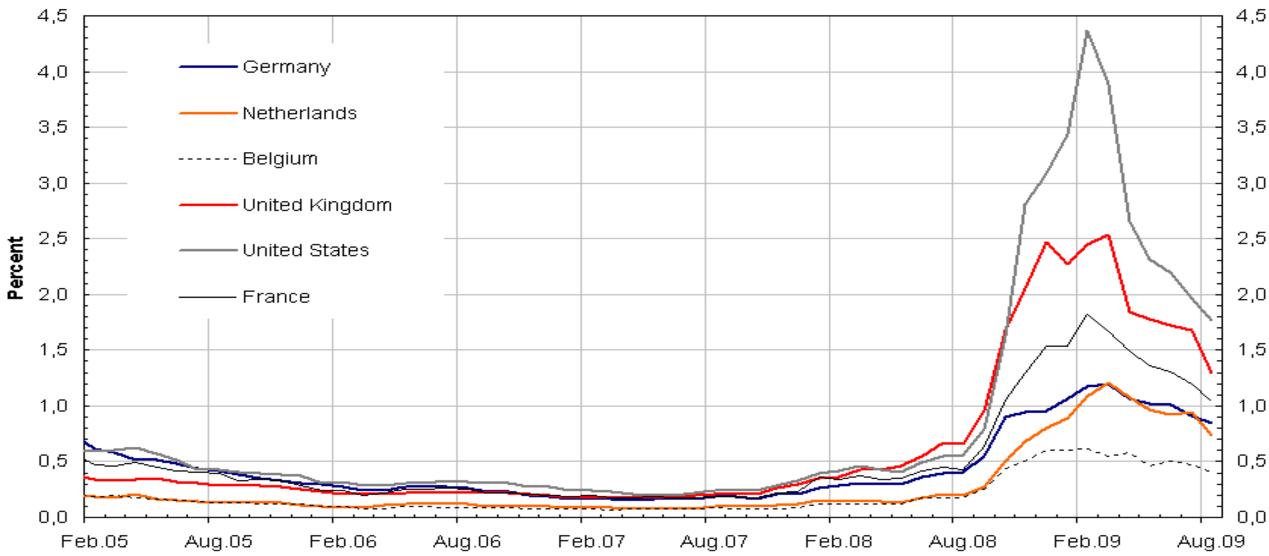
…we feature the following markets:

- **United Kingdom – with a spotlight on the construction and automotive sectors**
- **Mexico – with a spotlight on the retail and chemicals sectors**
- **Germany**
- **Spain**
- **Denmark**
- **Portugal**
- **Czech Republic**

Expected default in Western Europe and USA

One of the most important factors that any business needs to know is the trend of insolvencies in their markets. The following Expected Default Frequency (EDF) chart is based on listed companies in the markets referred to, and the likelihood of default across all sectors within the next year. In this context, default is defined as a failure to make a scheduled payment, or the initiation of bankruptcy proceedings. Probability of default is calculated from three factors: market value of a company's assets, its volatility and its current capital structure. As a guide, the probability of one firm in a hundred defaulting on payment is shown as 1%.

Median EDF evolution by country



Source: KMV Credit Monitor and Atradius Economic Research

The rebound in equity prices and a significant reduction of stock market volatility have translated into lower model-generated corporate default forecasts. EDFs have fallen back significantly in recent months, in both North America and Europe. In August 2009, the median EDF of all major Western economies dropped again compared to the previous month. While Belgium and Germany decreased slightly, France, The Netherlands, and the UK recorded the largest decrease since May. With a 19 basis points decrease the median corporate EDF in the US pool is now back below 180 basis points, after peaking at around 440 basis points in the first quarter of 2009. Despite this, it is worth bearing in mind that it is still well above its long term level. The same holds true for the recent EDF developments across European markets. While generally decreasing, the current EDF levels remain in line with readings from late 2008, indicating elevated default risk among listed companies.

On the following pages, we assess the impact of expected default in key markets

atradius
managing risk, enabling trade

Though the road is not smooth, recovery is on the horizon

In August 2009, the Expected Default Frequency (EDF) indicator for the UK recorded its largest decrease since May. EDF in the UK has been consistently declining since April 2009 however, the current EDF levels remain in line with readings from late 2008, indicating elevated default risk among listed companies (see chart page 2).

Recent re-adjusted figures show that the rate of economic contraction in Q2 of 2009 was 0.6%. This was lower than many had originally anticipated, with the construction and manufacturing industries showing slightly less deterioration than forecast. Construction actually declined by 0.8%, compared to the forecast 2.2% fall, and manufacturing fell by 0.1%, less than the forecast a 0.2% contraction. Exports of goods fell by 1.4% in Q2 and imports by 2.2%. While the weakness of Sterling should make UK sourced goods attractive, a general weakness in global demand means that many UK exporters are currently unable to make the most of this export opportunity.

In August 2009, UK retail sales rose by 2.2% year-on-year. Between June and August, food sales continued to do better than non-food. Clothing and footwear sales weakened further. Home appliances and furniture fell back to the levels of a year ago after July's weather and clearance driven growth. With unemployment still rising and a natural move by the public to save rather than spend, there is likely to be continued pressure on retail spending, as consumers continue to conserve cash to safeguard their personal finances.

In Q2 of 2009 there were 5,055 compulsory liquidations and creditors' voluntary liquidations in England and Wales: an increase of 2.9% on the Q1 figure and an increase of 39.1% year-on-year. Current insolvency information from Experian shows that, in August, business insolvencies increased by 11.3% year-on-year, but dropped by 23% compared to July 2009 figures - the lowest number of monthly failures in 2009. Whilst this is clearly good news, it is unlikely to be the start of a positive trend. The tail end of the year brings its own challenges (retail stock building, construction slowdown, etc) so cash management will continue to be the major focus. The impact of the HM Revenue and Customs "Time to Pay" scheme is also likely to have had a positive impact on the insolvency levels over the last few months. However, payments will become due over the coming months, adding further stress to the cash flow of corporate UK. Therefore, we expect that business insolvencies will continue to rise over the next six months.

Growth will return in 2010

The last 5 quarters of contraction have now contributed to a cumulative reduction in GDP of 5.5%. Add to this the 2.5% growth anticipated for 2009 and it makes fairly grim reading. The National Institute of Economic Research (NIESR) figures show that GDP for Q3 is likely to show a further small contraction. The main negative contributor to this disappointing forecast is recent news that UK industrial output in August fell by 2.5% more than in July, and by 11.3% year-on-year.

Looking further forward, the British Chamber of Commerce (BCC) has re-forecast its GDP figure for 2009, saying that the UK will now contract by 4.3% before growing by 1.1% in 2010. The International Monetary Fund expects the UK economy to expand by 0.9% in 2010, so again there is an element of consistency between these forecasts.

History shows us that, even when the UK has come out of recession, insolvencies and unemployment continue to rise for another 6-12 months. With the number of unemployed in the UK currently standing at 2.47 million (the highest level for 14 years), the Confederation of British Industry (CBI) predicts that unemployment will not peak until Q2 2010, when it will reach around 3 million.

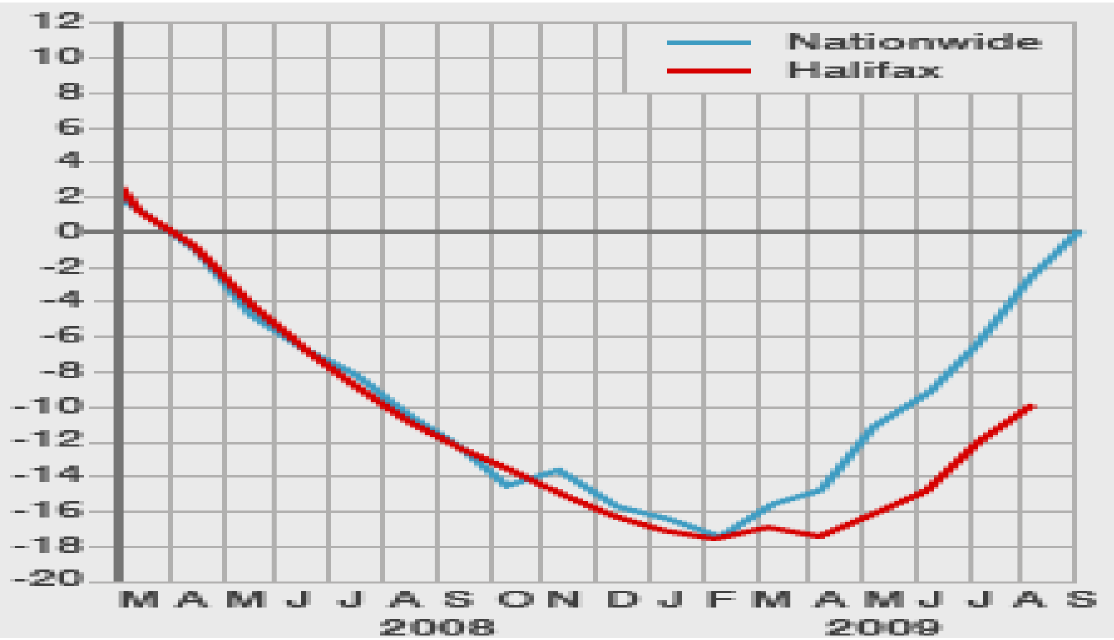
Construction

How has the global economic downturn impacted the British construction industry?

Housing: The UK construction sector has been in decline since the early part of 2008 – at first with the impact on private housing, brought about by the lack of liquidity in the market. Since then, different areas of construction have declined at a varying pace because of the lengthy timescales involved in the construction process. Despite this bleak picture, there is some evidence that recovery in the housing market has begun. House builders are now building again after a long period of destocking. House prices rose month-on-month for the third consecutive month in September. Year-on-year data is mixed. For instance, according to the Nationwide building society, house prices are now back where they were 12 months ago, while the Halifax says that they remain 7.4% lower (see chart below).

UK House Prices

Year change %



Source: Halifax & Nationwide

Mortgage approvals have been steadily improving month-on-month since the record low of November 2008. However, the August figures show a slight dip, suggesting that the market may have reached a plateau.

Despite most indicators moving in the right direction, we shouldn't become complacent. The number of housing starts in 2009 will be around 70,000, down from 170,000 a year at its peak, and the lowest since 1924. Moreover, most house builders were generating cash during their destocking phase, with no building costs, and were therefore able to service/repay debt. They will now once more be incurring building costs which have to be funded. Banks remain more reluctant to lend, and we have already seen a number of the larger players turning to shareholders with placements and rights issues to fund land purchases.

Commercial/industrial construction: The commercial market is a buyer's market and heavily reliant on the retail/services industry. But the difficulties faced by retailers have often led to insolvency, which in turn means a significant decrease in occupancy rates and less demand for additional capacity. Construction output in the commercial arena is expected to decline by 53% during 2009, while factory construction is expected to fall by 28%.

Public construction: There is some positive news on public spending in the short term, with large government investments being made in rail, health and education, and a strong pipeline of projects for the remainder of 2009 and 2010. This is tempered somewhat by the fact that social house building is expected to be down about 20% in 2009, as it often depends on accompanying private house building, typically on a shared site. Many construction companies are 'hybrid', with activities over a broad range of construction subsectors, and are thus exposed to many different areas of construction. So, as private house building has traditionally provided much higher margins than most other construction areas, a downturn in private housing has hit a number of these companies very hard.

What is the current trend in payment delays, payment defaults and insolvencies and why?
Real estate and construction companies account for 25% of all insolvencies in the UK. In Q2 of 2009 1,573 companies in this sector became insolvent: twice that seen in Q3 of 2007, before the credit crunch.

What should companies selling products into the construction industry pay particular attention to?
The construction sector, by its very nature, is highly geared, with debt facilities historically provided by financial institutions based on strong cash flows and good levels of security. Now, covenant breaches on bank facilities have become the norm because of cash flow problems. Because of this, suppliers into the construction industry should pay particular attention to a buyer's debt profile, their ability to service the debt, and the amount of their available bank facilities.

What is Atradius' short term outlook for the construction industry?
Insolvencies continue to rise. There is very little prospect of any meaningful growth in construction output for a number of years. Unemployment in the sector is growing at an alarming rate. The Atradius outlook on the construction sector in the short and medium-term is therefore negative.

Automotive

How has the global economic downturn impacted the British automotive industry?

The major Original Equipment Manufacturers (O.E.M.s) reacted too slowly to the economic downturn and only started cutting production in the UK around the Christmas period, which meant there was a severe oversupply of vehicles in the marketplace. The year to date has seen a period of mass de-stocking, with the industry buoyed by the success of the scrappage scheme. In September 2009 new car sales rose by 11.4% compared with the same month last year. This was also the first time in 5 years that sales of new cars had been higher than in March, when the year's other new registration number is released. The aftermarket has fared better during the downturn, as owners of larger family cars have chosen to maintain their existing vehicle instead of upgrading or buying a new one.

What is the current trend in payment delays, payment defaults and insolvencies?

With the oversupply of vehicles, extended terms will be sought as manufacturers seek to reduce stocks. The biggest dealerships are currently cutting costs to cope with the downturn. However, a number of smaller dealers have already fallen by the wayside. The scrappage scheme has ensured that the industry in general has avoided major insolvencies, although the recent announcement of the closure of a Jaguar plant reminds us that major manufacturers continue to strive to increase their efficiency and competitiveness in this sector.

What should companies selling products into the automotive sector pay particular attention to?

Identifying the part that a company plays in the supply chain is key. We have seen that the aftermarket has held up reasonably well, and the scrappage scheme has boosted the sale of new cars. UK design engineering, which generates a turnover of some £ 650 million, with around 65% exported, has been able to benefit from the success of the scrappage schemes throughout Europe. However, it is also clear that the scheme has benefited almost exclusively smaller more efficient cars bought by consumers while, outside of the city car and supermini sectors, sales remain poor, and corporate sales - which previously accounted for half of the new car market - have not benefited at all.

What is Atradius' short term (6 month) outlook for the automotive industry?

The industry recently welcomed the Government's announcement that it would be extending the funding available under the scrappage scheme to £400 million from £300 million to run to February 2010. However, despite this, we believe the marketplace will remain difficult in 2010 as new car sales will come under pressure, as many consumers will already have bought their new vehicles earlier than planned because of the incentive of the scrappage scheme in 2009, and because that scheme will eventually be wound up. Moreover, the VAT rate returns to 17.5% on January 1st.

A more positive outlook for the second part of the year

In the second quarter, Mexico suffered one of its worst GDP contractions ever (-10.3% year-on-year). Between January and August, Mexican exports fell by 25% due to deteriorating US demand (exports to the US constitute a fifth of Mexico's GDP). The unemployment rate rose to 6.2% in August: the highest for 13 years.

Remittances (the funds that expatriate workers send back to Mexico and which feed into the economy) decreased by 11.9% in the first half of the year, compared to an annual average growth of 16% over the last 10 years. Bank consumer credit growth is also shrinking after an average 35% annual growth on since 2001. Both of these factors have taken considerable liquidity out of the economy.

All this has an immediate impact on companies' payment behaviour, reflected in the steady increase in the Expected Default Frequency score since September 2008, to levels not seen since 2005. This indicator peaked at the end of Q1 of 2009 and subsequently showed a slight improvement, but remains high in August 2009.

Meanwhile, due to a more positive outlook for the second part of 2009 and, in common with trends in many other capital markets, Mexican share prices have picked up in recent months. Indicators of consumer and business confidence showed a slight recovery in September, but it is still unclear if this improvement will last for the rest of the year.

Growth will pick up again in 2010

Although the Peso / US-$ exchange rate is less volatile than in previous periods, insolvencies continue to be high. We still do not see a real recovery of the construction sector, even though the government has announced large-scale projects to assist the industry. Construction still suffers from significant defaults, as projects are frozen and / or budgetary allocation not made available. The Mexican automotive sector has proved to be a cost-effective producer of parts and components, but its place in the world's top ten automotive producers is threatened by the BRIC economies. For the next year, production levels in Mexico will depend on US demand for new vehicles. The food sector remains classified as a positive sector but is affected by the volatility of international basic grain prices. Tourism has suffered from the swine flue outbreak and media coverage of gang related drug violence in parts of the country, as the government seeks to crack down on the narcotics trade.

The International Monetary Fund (IMF) forecasts a GDP contraction of 7.3% this year. This is the sharpest fall since the 1995 Tequila Crisis and the worst in Latin America this year. That said, a recovery to 3.3% output growth is forecast for next year.

Retail

How has the global economic downturn impacted the retail industry?

The high unemployment rate, mainly affecting the northern part of Mexico, and the fear of losing jobs, have made consumers reluctant to spend over recent months. In addition, the massive decrease of remittances has played a major role in reducing consumer demand. In August 2009, consumer credit contracted by 21.3% year-on-year and will remain constrained, because of the increased bad debt ratios of Mexico's main banks.

Supermarket chains are expected to weather the financial downturn better than department and speciality stores, as customers delay discretionary spending on products like clothing or electronics. The typical Mexican consumer is considered to be in a “Stay at home” mode, as consumer trends shift towards eating at home rather than going out, and watching TV instead of going to the cinema. This is changing discretionary spending habits and explains why grocery sales show a positive trend in the middle of a recession.

What is the current trend in payment delays, payment defaults and insolvencies?

In 2009 there has been a steep increase in payment delays, caused by slower receivables turnover and the increase in bad debt. Since June 2009, the banking sector (including bank/retailer credit operations) displayed a bad debt ratio of 9.2%. The Mexican Central Bank expects to see higher bad debt levels in the future. The recent tightening of credit policies for some retail stores has resulted in lower sales volumes.

What should companies selling products into the retail sector pay particular attention to?

Analyse the credit cycle fully, and pay special attention to receivables and inventory turnover. Look carefully at profitability, as many retailers are selling at discount rates in order to move inventory. The retailers' geographic location should also be taken into account, as some rural areas are experiencing greater economic hardships than others. A retailer's product mix is very important in determining the extent of its reliance on merchandise that has been impacted by the economic crisis. And assess the retailer's consumer credit programmes and the impact that this may have on the overall operation.

What is Atradius' short term (6 month) outlook for the retail industry?

As unemployment has increased and a rebound in both credit markets and remittances from the US is not expected in the short term, we see no real improvement in the coming months.

Chemicals

How has the global economic downturn impacted the chemical industry?

Many of the key players in the Mexican chemical sector reported lower sales volumes in the first half of 2009, as a result of the downturn, customer destocking, and the drop in average chemical prices. According to the latest 2009 figures from the Mexican Chemical Industry Association (ANIQ), chemical sector output and domestic sales are showing negative trends. Inorganic chemicals (chlorine and soda sub-sectors mostly), synthetics, artificial fibres and industrial gas sub-sectors are the worst affected.

Most of the chemical groups increased their debt levels in the last quarter of 2008, as they required extra funding for operations, acquisitions in Mexico and South America, and to cover losses from low margins and exchange rate fluctuations at the end of the year. But, as funding from banks has tightened and the capital expenditures of those companies has in many cases shrunk, 2009 has been a year dedicated to paying off and/or restructuring debts.

What is the current trend in payment delays, payment defaults and insolvencies and why?

In 2009, the chemical sector has experienced some defaults and bankruptcies as well as a significant increase in payment delays, as many highly leveraged firms have suddenly found their bank/supplier credit lines reduced or cancelled. Distributors (many of them in the fertilizer sector), have reported high levels of expensive inventory that need to be sold at a loss, because of the drop in raw material prices in 2009 and the Peso devaluation.

What should companies selling products into the chemical sector pay particular attention to?

Highly geared companies with risky capital structures are more likely to default as the Mexican financial system has tightened its credit policies. Companies that import or borrow in hard currencies should be subject to closer scrutiny in view of the volatility of the Peso. Additionally, suppliers should confirm the status of bank lines and compliance with bank covenants.

An awareness of the sub-sector and the end market of chemical firms is also important. Although most of the sub-sectors reported negative trends (see above), the chemical firms that reported better results in 2009 were those whose end market was the food and beverage sector. Lubricant manufacturers have actually recorded positive export trends. Some sectors such as agrochemicals are usually heavily undercapitalised and so a closer analysis of their inventory trends is required.

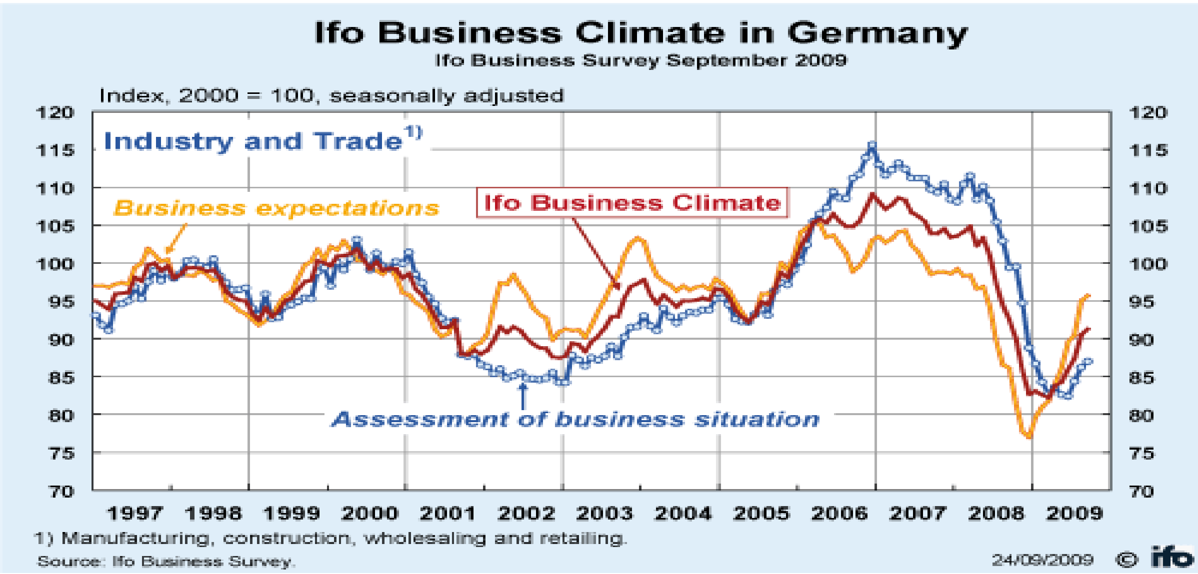
What is Atradius' short term (6 month) outlook for the Chemical industry?

Our outlook on this sector remains conservative as the credit market continues to be tight. We do not foresee a significant recovery in short term demand from industrial consumers – the main recipients of chemical production.

Rising business climate in Germany

In August 2009, the Expected Default Frequency (EDF) indicator for Germany dropped again compared to the previous month (see chart page 2). While generally decreasing, the current German EDF levels remain in line with readings from late 2008, indicating elevated default risk among listed companies.

After growth of 0.3% in Q2 of 2009, it is expected that the German economy will continue to recover, with 0.7% growth in Q3 compared to Q2. Many institutions have revised their economic forecast upwards since six months ago. The Ifo business climate for industry and trade continued to rise in September. Both the current business situation and outlook indicators again increased compared to previous months. That said, most firms still assess the business situation to be poor, while there is a more optimistic view of the next six months' outlook (see chart below).



During the last three months we have seen a stabilisation, albeit on a very low level, in the performance of severely affected trade sectors such as machinery, steel, transport and automotive. With the end of the car scrapping scheme in early September, the small car segment will now face more difficulties, as will suppliers. Pressure will continue on discounts and in the leasing sector. However, we expect a stabilisation of the automotive sector in the mid-term. In the machinery sector, the historically high orders on hand have been depleted. In September, new orders declined by 40% year-on-year and additional capacity adjustments seem inevitable. In comparison, less affected industries, like agriculture or pharmaceuticals, will continue to show a high degree of resilience in the mid-term future. With some qualifications, so will consumer goods such as food, which have so far profited from robust private consumption. There is, however, still the downside risk of deteriorating private consumption due to the expected expiry of short-working schemes and a rise in unemployment next year.

According to a Dun and Bradstreet study, payment morale deteriorated in Q2 of 2009. 78.4% of all German companies paid their invoices within the agreed payment term, a decrease of 1.13% over the previous quarter. The average delay was 9.7 days (9.1 days in Q1 of 2009). The transport and logistics sector registered the largest decline, with only 68.4% of companies paying on time. While that sector recorded the worst figures of any industry, in contrast the pharmaceuticals industry ranks best with 92.8% of companies paying without delays. These results are borne out by Atradius' own experience.

From January to July 2009, the number of corporate insolvencies increased by 15.3% year-on-year: to 19,188. In the first half of the year, the value of outstanding receivables rose from €14.7 billion to €24.4 billion – an extremely worrying tendency. Despite the German economy's modest recovery, we expect a continuing and significant increase in corporate failures for the rest of the year. This trend will persist in 2010, albeit at a lower level of around 10%.

Will banks tighten their credit policies further?

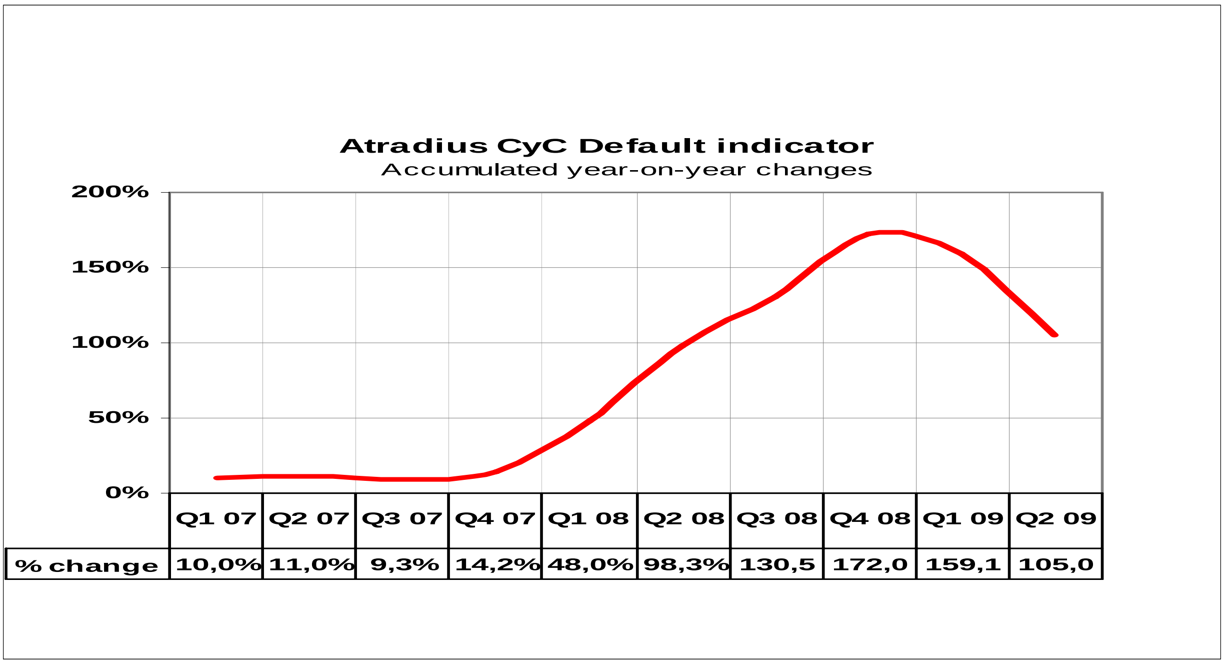
Although the Deutsche Bundesbank registered a slight growth in loan portfolios in Q2 of 2009 compared to the first quarter of 2009, bank lending overall has not increased over the same period. One reason is decreasing investments, with companies consequently having lower financing requirements. Another is the banks' cautious lending policy, reflecting their assessment of current and expected deterioration in companies´ creditworthiness. Beside the more cautious loan policy, it is worth noting that banks are not passing on the currently extremely low base rate to borrowers by lowering firm borrowing rates.

We expect that bank lending will continue to decline after companies have disclosed their 2009 annual accounts, as in many cases this will trigger a rapid deterioration of borrowers' ratings. Those businesses mainly affected will be in the machinery, steel and automotive sectors. Additionally, we expect that companies currently in the process of restructuring will be closely scrutinised by their banks at the end of 2009 and beginning of 2010, and that less promising or more cumbersome restructuring processes will not be supported with additional liquidity.

Payment defaults and insolvencies are decreasing

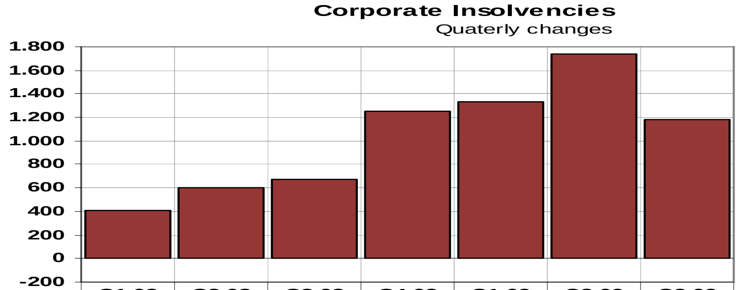
The recession in Spain is slowing down, with a contraction in GDP of 1.1% quarter-to-quarter in Q2 of 2009 compared to 1.6 in Q1. Domestic demand continues to fall (down 1.2% in Q2 compared to the previous quarter), due to a decrease in private consumption and fixed capital investments. Gross fixed capital formation – a measure of net new investment in fixed capital assets - deteriorated by 17%. However, in contrast, foreign demand made a positive contribution to aggregate growth (3.1%).

The business environment remains difficult. Payment delays have trebled and insolvencies have quadrupled since 2007. That said, since our last analysis in July, we have seen further indications of a changing pattern of company payment delays. While, in the second quarter of 2009, the median of payment default increased by 105% year-on-year, according to the Atradius Crédito y Caución Default Indicator, there is a decreasing trend in such defaults since their peak in Q4 of 2008 (see chart below).



Source: Atradius

There are also signs of improvement in insolvencies. According to our preliminary data, based on figures published by Official State Gazette (Boletín Official del Estado), we expect 1,180 business failures to be registered in Q3 of 2009, a 32% improvement on the previous quarter (see chart next page). After the peak of more than 1,700 cases in the second quarter this will be the first decrease in insolvencies following two years of steady increase.



	Q1 08	Q2 08	Q3 08	Q4 08	Q1 09	Q2 09	Q3 09
Total	406	604	678	1.249	1.335	1.741	1.180
% change	22,3%	48,8%	12,3%	84,2%	6,9%	30,4%	-32,2%

Source: Atradius

No "Japanisation" of Spain

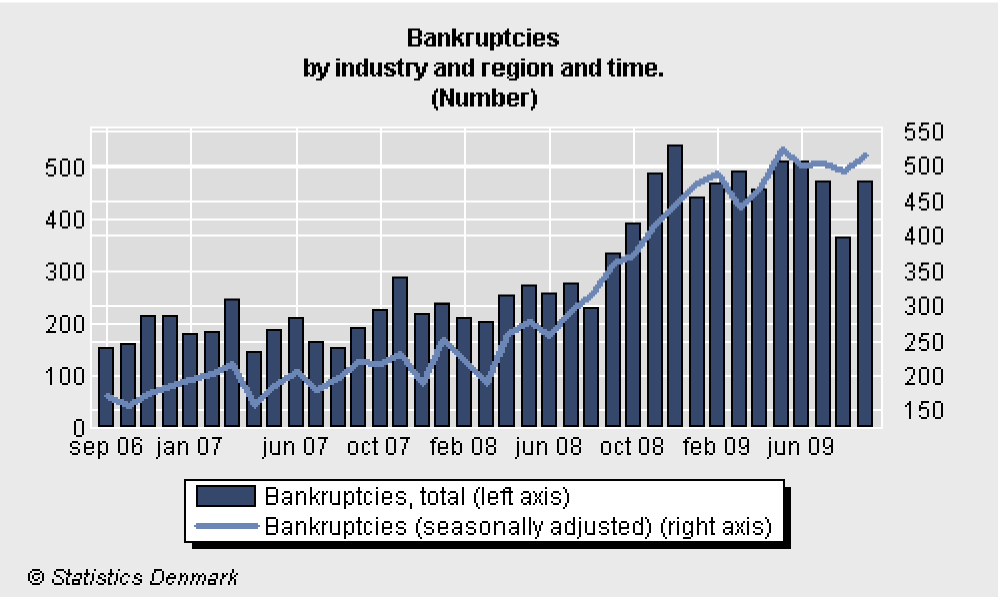
We forecast that 2009 will mark the bottom of the recession for Spain and that the economy will stabilise in 2010, with a recovery gaining momentum towards 2012. The IMF has revised it forecast for Spain's GDP growth upwards: to a decline of 3.8% in 2009 and 0.7% in 2010. For the time being, the economy will continue to be characterised by flat domestic demand and a high unemployment rate. In Q2 of 2009 unemployment stood at 18.5%, with increases across all business sectors. All forecasts are of a further deterioration in 2010, peaking at more than 20%. But those predicting a "Japanisation" of the economy, with deflationary pressures triggering a long-lasting downward spiral, will be proved wrong.

Construction will remain a major economic force, but its share of GDP will decline in the long-term, and it is not clear yet which sector will take over construction's leading role in the Spanish economy. We expect that, across all industries, some companies will emerge from the recession stronger. In the main, these will be SMEs who have reinvested sufficient profits into R&D projects to enable them to develop high tech solutions, diversify and enter new markets, and thus become less reliant on the domestic market. We expect the environmental industry to further extend its leading position in R&D investments.

Improvement in some leading indicators but still a long way to go

Denmark is still in a recession, and the 2nd quarter figures showed no sign of recovery yet. According to Statistics Denmark, GDP fell by 2.6% in Q2 of 2009 compared to the previous quarter and by 7.2% year-on-year. This was due to a sharp decrease in exports (13.6% year-on-year), imports (16.4%) and private consumption (7.2%). Business investments fell by 16.3% and car sales deteriorated by 38.5% over the same period. Only public consumption expenditure increased by 2.5%.

The number of corporate insolvencies rose sharply in the second half of 2008 and peaked with 524 insolvencies in December, leading to an annual increase of 62%. Since December 2008, the monthly figures have stabilised at 450 – 500 (see chart below). If the number of insolvencies remains at this level for the rest of 2009, the annual number of insolvencies will increase by another 43%.



Construction

The Danish construction industry was overheated in 2006 and 2007. At the end of 2007 the price bubble started to burst. Since then, the average price for a typical Danish family house has dropped by 15%, and, in the Copenhagen area, by as much as 30%. Some analysts expect average house prices to decrease further in the coming months before stabilising. This has led to many bankruptcies in the construction industry: mainly SMEs focused on house building. In contrast, larger and more diversified construction companies are still doing well.

Construction materials

In 2006 and 2007, many companies expanded their capacity but now there is a need to de-stock and downsize. So far, we have seen only quite small companies become bankrupt, but many of the large players have also been severely hit.

Transport

Denmark's large international marine sector has already fallen victim to massive cut-backs and some insolvencies. There is also severe overcapacity in land transport, which has to be reduced. Since September last year, turnover in Danish land transport has fallen by 25%.

Retail

With house prices falling, the value of pension savings declining and unemployment rising, consumers have responded by increasing their savings. Consequently, demand for cars, furniture, clothing and other consumer durables is weakening. This has already caused many bankruptcies in the retail sector and we expect many more to come, especially in those sectors mentioned.

Some signs of stabilisation

That said, we expect stabilisation of the Danish economy in the third quarter. The stock market started to pick up again in March 2009, following the international trend. The OMX20 index, comprising the 20 most traded Danish shares, has since March increased by some 50%. Interim accounts for those 20 companies have shown a mixed picture, but most performed better than expected. The banking sector has also stabilised, strongly supported by two government-backed packages: the first offering an unlimited guarantee for deposits in Danish banks, and the second giving banks the opportunity to raise subordinated loan capital from the Danish state for a period of 2-3 years. A few small banks and two regional banks have filed for bankruptcy, and have been taken over by the Danish state to manage their dissolution.

Interest rates are currently at a record low. This will probably not in itself lead to any increase in business investments, given the current overcapacity in the production sector, but private consumption may benefit from the lower cost of short-term loans in the housing sector.

Besides the general economic crisis, Denmark has also to deal with the negative outcome of an overheated economy in 2007 and first half-year 2008 - which caused relatively high wage increases and overstaffing - and the currency depreciation in some of its main export markets. This will take time and no strong rebound can be expected in the short-term. That said, at least some important lead indicators have bottomed out. The industry confidence indicator has risen from -34 in April 2009 to -8 in August and the consumer confidence indicator has increased from -11.7 in March 2009 to -1.1 in September. The index for annual wage increases in the production sector has fallen to 3.0% in the second quarter. Therefore, some of the most competitive industry sectors may see some small improvements in Q4 of 2009.

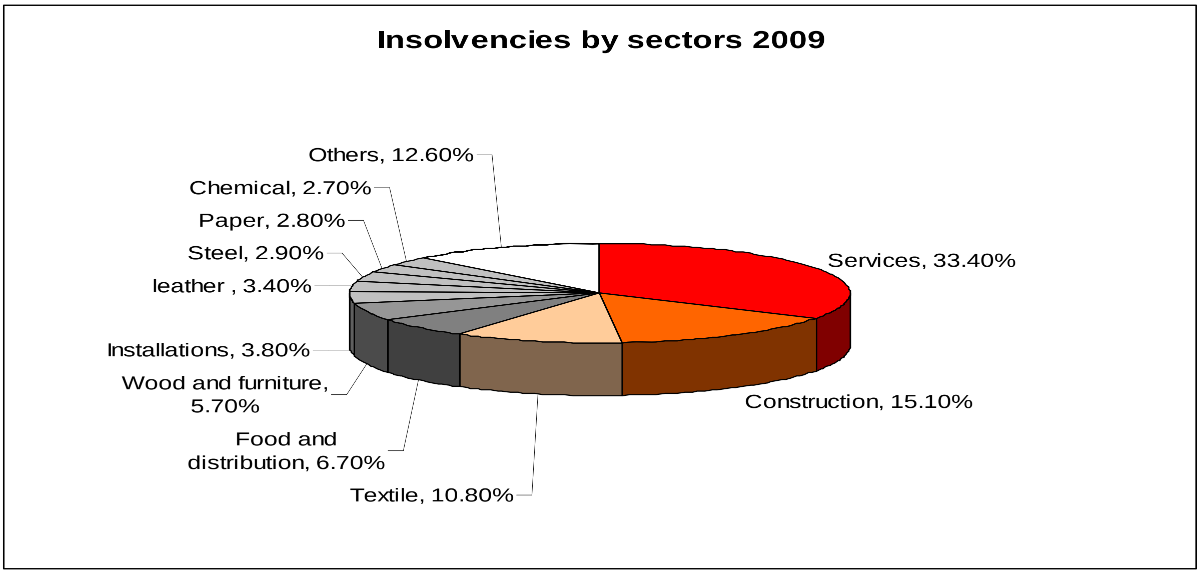
Increasing payment defaults

Portuguese GDP continued to decrease in the second quarter of 2009 (-3.7%). The current crisis has spread rapidly into all industrial and commercial sectors. Payment conditions deteriorated in the early months of the year, increasing the risks for vendors. About 90% of Portuguese companies experienced payment delays, severely damaging their competitiveness. Portuguese payment times are, on average, 92 days and in case of public sector buyers, up to 130 days. Along with Greece, Spain, and Italy, Portugal has the slowest payers in Europe.

Payment default increased in the first 9 months of 2009: by 42% year-on-year. Corporate insolvencies have increased sharply since the second quarter (see chart below) with 3626 cases registered in September, compared to 2558 cases in September 2008.

	QI	QII	QIII	QIV
Number of insolvencies 2008	968	1824	2558	3113
Number of insolvencies 2009	1026	2360	3626	
Variation %	6%	29%	37%	

Source: Atradius



Source: Atradius

The service industry (retail, tourism, transport, travel agencies) has been directly affected by falling private consumption. Decreasing incomes from tourism and increasingly restrictive consumer credit by banks have additionally contributed to the service sector's problems.

Construction has been in crisis since the beginning of 2001 and in that sense is not impacted by the global economic downturn as it is in other European countries. The outlook for the whole industry remains negative, especially for activities related to home building.

The textile sector has been in a deep crisis for two years due to deteriorating competitiveness, and depends largely on subsidies provided by the Portuguese government and the EU.

Structural problems loom large

Economic conditions are still extremely weak: how and when the Portuguese economy will return to more sustainable growth remains highly uncertain. Structural problems, such as low skills and wage competitiveness, weak productivity, rising unemployment and lower foreign and domestic orders, have suppressed economic activity and will continue to do so. Exports of automotive components and textiles have struggled in recent years because of fierce low cost competition from the Far East and Eastern Europe.

Overall, business risks - falling profitability, payment delays, rising corporate insolvency levels - will remain a source of concern.

Growth picked up again in the second quarter

According to the Czech Statistical Office, GDP decreased by 5% in the first half of the year compared to the corresponding period in 2008. However, output increased by 0.1% in Q2 compared to the previous quarter. The economy continues to suffer from weak exports, which declined by 18% between January and August 2009. In line with our last analysis in May, we still assess heavily export-oriented companies in the automotive, machines, chemicals, transport, and textile and furniture sectors to be experiencing the greatest problems.

Industrial production has deteriorated by almost 20% since January 2009, mainly caused by a decrease in sales and new orders in the manufacturing industry. Sales and repairs of vehicles have fallen rapidly, as has the demand for services. In contrast, the construction sector has shown some resilience: while building construction decreased in recent months, civil engineering continued to grow.

The trend in producers´ prices varied considerably. In the agricultural sector, prices fell steeply and, in the industrial sector, prices fell only slightly. Prices in the construction sector increased, except for construction materials. The price level of services rose, except of transport. Consumer prices increased by 1.8% in the first half of the year.

The economic decline has led to an increase in unemployment. The IMF forecasts a rise in the unemployment rate to 7.9% this year. As in the last Market Monitor, we are still seeing a tightening of credit conditions by banks. As a result, it remains extremely difficult for Czech companies to obtain new finance and many are now facing a credit shortage and/or stricter credit terms. We have also seen tightening liquidity in factoring companies.

Opportunities in the construction sector

We still expect insolvencies in the Czech Republic to increase by 15%-20%: to approximately 1700. Those most affected will be transport, construction, textiles and steel traders, as well as companies linked to the automotive industry.

However, there are still some opportunities in the current environment, mainly in the construction sector. EU funds are earmarked for infrastructure improvements, providing good prospects for the infrastructure construction sub-sector. There are also programmes for insulating flats and adapting heating systems to better ecological standards.