ASIA

Cambodia : Opposition party ban will secure the PM re-election in 2018

Event

The Supreme Court has dissolved the main opposition CNRP party (Cambodia National Rescue Party) and banned 118 of its officials from political activities for the next five years. Its parliamentary and local seats are to be redistributed among the other parties, primarily benefiting the ruling CPP party (Cambodian People's Party). Meanwhile, CNRP leader Sam Rainsy remains in exile whereas his successor Kem Sokha was arrested last September for alleged participation in an international conspiracy against the government. Most CNRP members have resigned or left the country. No appeal is allowed.

Impact on country risk

This decision by a court led by a CPP figure and finalizing a CPP lawsuit, concludes the CPP's continued crackdown against media, civil society and the opposition since CPP's relatively disappointing outcome at local elections last July. With merely a small opposition remaining, the CPP victory at next year's parliamentary elections seems secured and will avoid a repeat of the 2013 polls which the CPP won by its closest margin ever. Therefore, Prime Minister Hun Sen is expected to add five more years to his long-standing rule. What is seen as a democratic setback has been followed by western condemnation and might pave the way to EU and US sanctions. They both have the capacity to put pressure on Cambodia as they are the two largest export markets for its key garment sector, and might in theory contemplate a suspension of their preferential bilateral trade regime. The US has already stopped aid. However, in the coming months, the US and EU attention will be focused on more urgent domestic issues. Thus, it remains to be seen whether any sanction threats, particularly hitting Cambodian exports, will materialize in the absence of fair elections in 2018. What is sure though is Cambodia's continued and increasing reliance on its Chinese ally. Solid financial and political support from a stronger China makes indeed Hun Sen look more confident in rebuffing any criticism and potential western sanction threats. Moreover, a dissolved opposition and a tougher security policy should fuel political continuity and domestic stability, thereby contributing to keeping a stable investment climate and a strong growth trajectory. As a result and unless EU/US sanctions on exports are taken, political risk might in fact not deteriorate from those latest developments.

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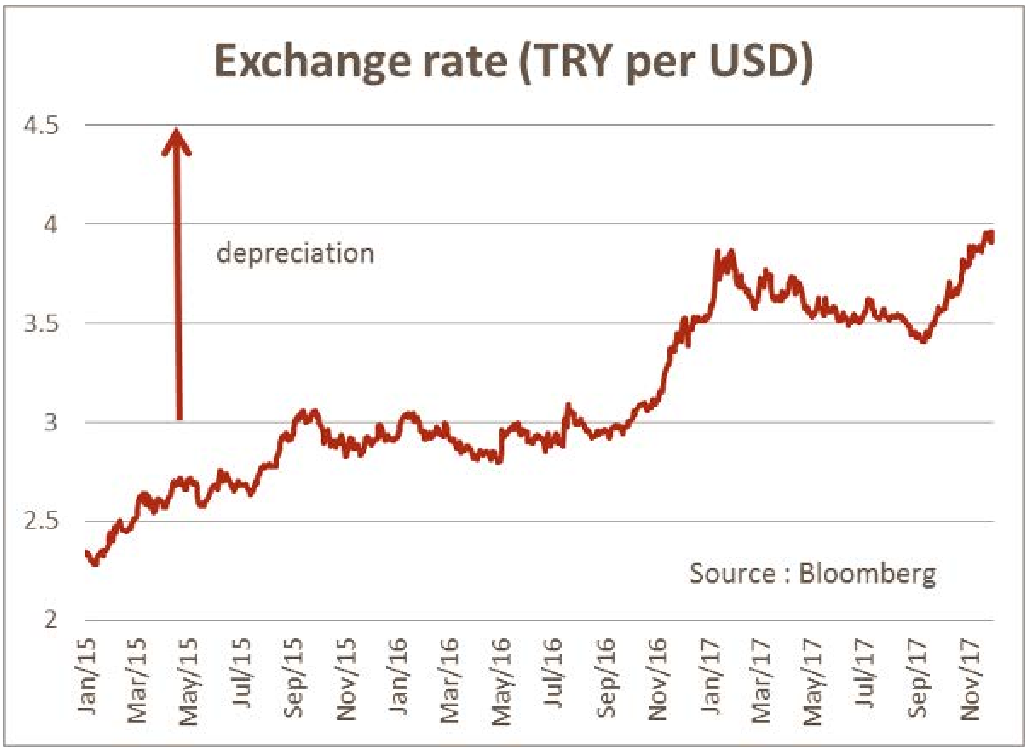
EUROPE

Turkey: Turkish Lira again under pressure

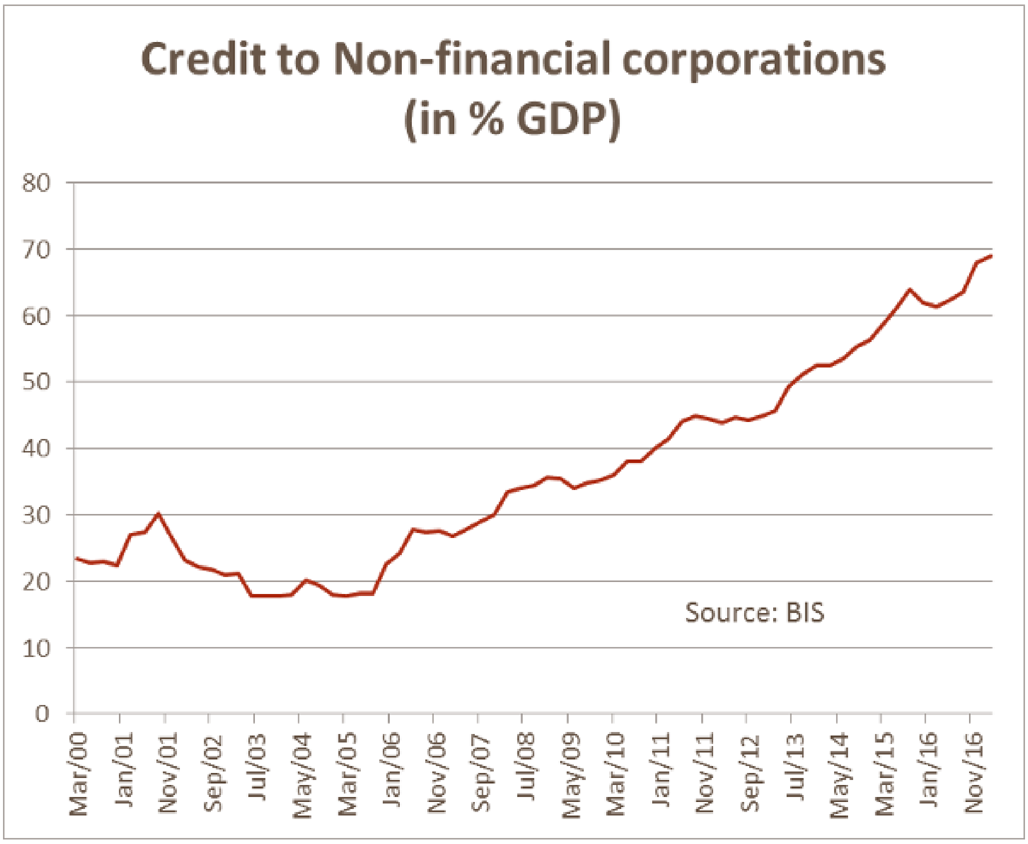
Event

Since September 2017, the Turkish Lira is again under pressure (cf. graph). End November, lira deprecation was driven by confirmation that a gold trader agreed to testify in a US sanctions trial. In October, the Turkish lira slumped amid emergence of diplomatic tension with the US.



Impact on country risk

Turkish Lira deprecation is a source of concern not only as it fuels inflation (11.9% in October according to the Central Bank) but also as corporate debt is relatively high and often denominated in foreign currency which means that any depreciation of the lira increased the cost of reimbursing the debt. Over the past few years, corporate debt has increased sharply (cf. graph). As this increase was mainly financed by domestic banks, this could put pressure on the banking sector which is exposed to foreign investor confidence. After all, its negative net foreign asset position deteriorated sharply between 2009 and 2014 (to almost 20% of GDP). Since then, it has improved in relative terms but remains above 15% of GDP mid-2017, a high level. In order to finance its widening current account deficit (expected to reach 4.6% of GDP in 2017 according to IMF World Economic Outlook October 2017 from 3.8% in 2016), Turkey relies heavily on short-term capital flows and is thus vulnerable to a change in foreign investor confidence. This means that the Turkish lira remains volatile and highly vulnerable to a change in risk aversion among investors as highlighted by the recent episode of lira depreciation. If the central bank decides to intervene in the exchange market rather than to increase interest rates to stem lira depreciation, this could lead to a further drop in foreign exchange reserves. This would incline Credendo to downgrade its short term political risk (currently in category 3). Growth is likely to slow down in 2018 after impressive recovery this year driven by various pro-growth measures adopted by the authorities (such as temporary tax cuts and credit guarantee fund). In this context, commercial risk remains high (in category C on a scale from A to C).



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LATIN AMERICA

Brazil: Resignation of minister can prove an opportunity to push through the vital pension reform

Event

Bruno Araújo resigned from his post as minister of Cities. Araújo was one of four ministers representing the centrist PSDB (Brazilian Social Democracy Party). The resignation is a sign of a rift between the embattled president Temer and one of his most powerful coalition partners. A reason for the conflict could be that the PSDB is likely to stand its own candidate for the presidential election in October 2018. Hence, many of the PSDB want to distance themselves from the deeply unpopular Temer government to better their chances at the polls. Temer chose Alexandre Baldy, from the Progressive Party, to be the new minister of Cities.

Impact on country risk

After the departure of Araújo, Temer is seeking to secure political backing for the pension bill. The decision to swear Alexandre Baldy in is likely a move designed to please the Progressive Party which has 40 seats in the chamber. The cap on pension spending is a flagship proposal of Temer to rein in fiscal expenditure. Indeed, despite some fiscal reforms, the fiscal deficits remains relatively elevated (at an expected 9.2% of GDP in 2017), swelling the relatively high public debt (expected at 83.4% of GDP in 2017). Also in the future, relatively large fiscal deficits are expected, likely pushing the public debt to close to 100% of GDP in 5 years' time. The pension reform was first presented to Congress a year ago and has since then already been watered down several times. The stakes are quiet high for Brazil. The failure to approve even a watered down pension bill could have an important impact on the economy. Next to aggravating the fiscal situation and trigger sovereign downgrades by rating agencies, it could put pressure on the currency, spur inflation, tighten the monetary policy and decrease the positive growth prospects (expected at 1.5% in 2018).

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Venezuela: Debt default was long time due

Event

This month, Venezuela and its state oil company were declared officially in default by rating agencies. The ratings agencies' declarations are symbolically important but do not imply that creditors will take immediate action. Indeed, as a result of the default, creditors can seize the country´s vital oil shipments and seize assets overseas (such as PDVSA-owned Citgo in the US). However, for the moment, creditors are not banding together to take legal action against Venezuela's external assets.

Impact on country risk

Given the poor liquidity and severe economic challenges, the debt default was long time due. The country has been hit hard by unorthodox policies (first exchange restrictions were imposed in 2003), lack of investment in productive capacity and especially low oil prices since 2014. Indeed, the economy, underpinned by the world's largest oil reserves, relies heavily on oil revenues. As a consequence, the economy has been contracting with a cumulative 39% in 4 years. Moreover, fiscal deficit is expected to reach a high level of 18.5% of GDP in 2017, and inflation to skyrocket to about 1.100%.

Furthermore, foreign exchange reserves are at a 20 year low, covering only 1 month of import. In addition, the black market exchange rate has soared to 7,000 times the official rate. The current account deficit has been relative modest, mostly due to heavy import compression which has led to a lack of medicines and other basic goods in Venezuela. Therefore, the fact that Venezuela has continued its debt payments in the past years is a bigger surprise than its recent default. A debt restructuring is likely to be very complex. Venezuela's debts have been issued by various entities, with varied legal clauses, to multiple parties. Venezuela also owes money to China, Russia, Brazil and multilateral lenders, increasing the geopolitical complexity. On top of that, US sanctions block US-regulated institutions and investors from buying new Venezuelan bonds, as would be issued in a typical debt restructuring. The EU has extensive sanctions on the country as well. Hence, the likely outcome is a protracted period of financial limbo with various lawsuits, likely granting president Maduro further time in office. Due to the current economic situation, Credendo country risk ratings are likely to remain in the worse category in the coming year.

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MENA

Saudi Arabia: Crown prince in the spotlight

Event

In November, Saudi Arabia's crown prince, Mohammed bin Salman, has put himself and Saudi Arabia firmly into the spotlight with its high profile anti-corruption purge. Around 200 individuals, including members of the royal family and the son of the former King, have been arrested. This comes at a time that the crown prince is pushing for a more aggressive foreign policy as has already been visible with the intervention in Yemen, the blockade on Qatar, the increased tensions with Iran and now recently with the resignation announcement of the Lebanese prime minister.

Impact on country risk

The flamboyant crown prince is moving Saudi Arabia away from the low profile and consensus based politics that has governed the country in the past to a more centralised way of governing the country where he has been the driving factor behind some bold policy measures such as the current anti-corruption purge. The purge seems to serve three aims. First of all, it aims at ending the system of patronage in the country. In Saudi Arabia, state contracts and resources were often funnelled to members of the royal family and the business elite. This has resulted in a significant drain on government resources. Secondly, it helps to consolidate his power. By jailing for example the head of the National Guard and son of the former king he removed a potential rival. Lastly, the current corruption purge makes the fiscal consolidation that is currently implemented more easily to swallow for the Saudi population. People indeed had the feeling that the elite was always above the law, while they had to bear the consequences of the current fiscal consolidation. At the same time the crown prince continues pushing forward the economic reform programme he has ignited in Saudi Arabia. The Vision 2030 programme remains largely on schedule, but the results of the programme are expected to only show themselves in the country's macroeconomic data over the coming years. Nevertheless, significant fiscal consolidation has already been introduced, and this is expected to lead to a reduction of the fiscal deficit from 17.2% of GDP in 2016 to 9.3% of GDP in 2017. While the reforms will have a positive impact on the Saudi's economy in the long term, they are currently still having a negative short term effect on the economy. Economic growth is projected to be only 0.1% in 2017 and only 1.1% in 2018. Prince bin Salman's foreign policy currently poses the largest risk for Lebanon. Riyadh is increasing the pressure on Lebanon for the presence of Hezbollah in the country. This can have strong implications for Lebanon depending on how far Saudi Arabia is willing to push it. For example because the Lebanese financial sector is strongly dependant on non-resident deposits from abroad and on remittance inflows into the country, the Lebanese banks then borrow these sums to the central bank were they consist of a large part of the Central Bank reserves. If the remittance flows (which mainly originate from the Gulf countries) would stop and the non-resident deposits are being withdrawn, this would have large consequences for the banking sector in Lebanon and the central bank's reserves. However, it is far from certain that this will be the case and the Saudi measures could be limited to further diplomatic pressure.

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AFRICA

Zimbabwe: Will things get better in the post-Mugabe era?

Event

On 21 November, 93-year old President Mugabe inelegantly left office after 37 years of authoritarian rule, greeted by mass public celebrations. His forced yet non-violent departure followed the sacking of Vice President Emmerson Mnangagwa earlier this month, aimed at Grace Mugabe's ordinary take-over of the presidency from her 41 years older husband. Obviously, she overplayed her hand, not taking into consideration how despised she is within the ruling Zanu-PF party and the army. The military intervened and armoured troops rolled into Harare on 14 November to reinstate Mnangagwa, ending the era of one of Africa's most notorious 'presidents-for-life'. The 75-year-old Mnangagwa, who served under Mugabe as minister of state security and of justice, is also known as 'the crocodile' dreaded for his record of fearsome repression and persecution of the opposition. He was sworn in on 24 November as Zimbabwe's interim president and declared to tackle corruption, protect foreign investments and rebuild the economy. It remains to be seen whether these promises will be left hanging or will be actually fulfilled.

Impact on country risk

Mugabe's incompetence and ruinous policies caused the economy to collapse and impoverished the people of what was once one of Africa's most prosperous countries. After corruption scandals in the 1990's blew large holes in the budget, the IMF decided to withdraw all support. At the turn of the century, Mugabe set off a reckless campaign of land grabs ('indigenisation law') and started confiscating land without compensation from white farm owners at a raging pace. As a result, Zimbabwe's GDP started tumbling down while government and export revenues collapsed and failed to recover ever since. At the same time, violent oppression and poverty drove a large part of the population into exile. As the government ran out of money, it simply started printing it, leading to a period of hyperinflation which lasted until 2009, when the US dollar became legal tender. Today, Zimbabwe is bankrupt while acute cash shortages – partly resulting of low trade returns – paralyse the dollar-based economy. The country needs the IMF, World Bank and creditors to restructure debts and supply new loans. However, aid of multilaterals will be strictly conditional on political and policy reforms and properly supervised elections, something Mugabe never agreed with. Henceforth, organising credible elections in 2018 will be the foremost priority for the new government. For the time being, Zanu-PF is expected to consolidate its power as the opposition is weak and fragmented. Credendo classifies Zimbabwe on the worst category for more than 15 years and the challenges confronting the country remain rife. Hence, the outlook can only improve when for starters proper elections are organised, the huge outstanding unpaid debts (around USD 9 billion) are treated and investors are reassured by repealing the harmful 'indigenisation law'.

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