Country Risk and the Global Outlook

December 2022

New Economic Realities Test Businesses

Commentary:

"PMI readings around the world indicate a global economic slowdown, and while central bankers are ramping down the pace of interest rate hikes, the policy playbook deployed in the two previous global recessions might not work this time. Mainland China's silent pivot on Covid containment puts a floor on the country's economic slide, but record-high cases mean that the benefits from reopening may only bear fruit slowly. Finally, collective labor activism around the world underscores the need for businesses to continuously monitor operational resilience and prepare for new challenges in the current macroeconomic environment. Even as India remains the fastest growing economy in the world, the intensity of the global spillover remains highly uncertain. If the contagion happens to be stronger than expected, the pace of recovery will be longer than the developed markets currently witnessing a slowdown." said Dr Arun Singh, Global Chief Economist, Dun & Bradstreet.

INTRODUCTION

Latest readings on the Purchasing Managers' Index (PMIs) around the world are broadly in the contractionary territory. It is hardly surprising and suggests an impending global economic slowdown. It is also worth noting that central banks have shifted to delivering smaller rate hikes now. It would be a mistake, however, to assume that central banks would reverse course at the first sign of economic trouble. What complicates the job of central bankers are unusually tight labor markets, which translate into high demand pressures, and the fact that evidence of inflation reduction globally is still quite weak.

There are two key points that businesses must consider. Firstly, the timing and intensity of this economic slowdown will differ across economies. For instance, the US is on a much better footing than the EU; and some developing markets in Asia, the Middle East and Latin America will outperform the US in coming months. Secondly, businesses cannot rely on the kind of policy support that was forthcoming in the last two global recessions (2008 and 2020). In terms of monetary policy, the lag between smaller rate hikes, pauses and then actual cuts may turn out to be long. The interim period would be fraught with uncertainty. On the other hand, with higher interest rates, government debt is now costlier. So fiscal support, too, will likely be limited or targeted. Businesses should take a hard look at when and how this slowdown will affect their operations (or viability), those of their subsidiaries, or their suppliers.

GLOBAL OUTLOOK: POLICY PIVOTS IN MAINLAND CHINA ARE WELCOME, BUT MAY NOT YIELD IMMEDIATE RESULTS

Within a matter of weeks, we have witnessed silent policy pivots on two key impediments to growth in Mainland China - the authorities have pushed for a more open financial support to the troubled property sector, and more importantly, there were first solid signs that covid containment measures will be more relaxed than they have been so far: home quarantines will be allowed and mandatory negative tests are no longer a requirement. It is a welcome change, and the fact that it is happening at a time when covid cases are hitting record levels in the country point to a rethink in government priorities. Arresting the economic slide is now firmly on top of the agenda. Key to note, however, is that the benefits of this policy loosening will be slow to materialize, as high case numbers will keep informal constraints on operations, with people remaining reluctant to leave their homes, and while the supply environment would improve in terms of reliability, a pickup in consumer confidence, which affects domestic demand, could be much slower.

Finally, while the US managed to stave off a nationwide strike of railroad workers, labor activism has hurt company operations around the world - strikes in the UK, South Korea, South Africa, Peru and even unrest in factories of Mainland China have made headlines in the past weeks. These frustrations stem from cost-of-living pressures, which are eating into workers' earnings, but are also a result of a tight labor market; employers are struggling to fill open positions, which is leading to significantly harder working conditions for those left to meet higher demand. Until cost pressures on essentials ease, labor activism may become more frequent, adding to the cost of inputs, operational and reputational risk for businesses.

Dun & Bradstreet Country Risk Analysis			
Country	**November 2022**	**December 2022**	**Change**
Country Risk Rating Upgrades (risk level has improved)			
Egypt	DB6a	DB5d	1 Quartile
Ethiopia	DB6b	DB6a	1 Quartile
Country Risk Rating Downgrades (risk level has deteriorated)			
Costa Rica	DB4c	DB4d	1 Quartile
South Africa	DB5a	DB5b	1 Quartile
Outlook Upgrades (from/to)			
Russian Federation	Deteriorating Rapidly	Deteriorating	
Outlook Downgrades (from/to)			

Norway	Improving	Stable
Singapore	Improving	Stable

REGIONAL SUMMARIES

North America

North America's regional outlook is retained as 'deteriorating'. Canada's Q3 GDP came in at 2.9% (annualized), but weak consumer spending indicates an impending economic slowdown. Inflation moved downward in October in the US but remained sticky for Canada; in both cases, it remains well above central bank targets, making the case for further rate hikes in the upcoming policy meetings. Despite news of mass layoffs especially among US firms, data indicates that the labor market in the region remains tight with firms struggling to fill job vacancies. The housing markets in both the US and Canada continued to show signs of cooling as mortgage rates climb to a multi-decade high.

US Congress narrowly averted a massive railroad strike, but it was symptomatic of new risks to the supply environment, already battered by weather events and natural disasters from earlier this year. Goods manufacturers should note that the demand for their goods continues to weaken. In the services sector, labor shortages and rising wages are putting pressure on profit margins of businesses.

Western & Central Europe

Western Europe's regional outlook is retained as 'deteriorating rapidly'. As euro zone inflation shows mild signs of deceleration, core and headline inflation remain considerably above target across many economies in the continent, even though significant differences across countries persist. As the effects of inflationary pressures and tighter monetary transmit in the economy, businesses should expect interest rates to further increase, input costs to remain elevated and demand to weaken.

In the UK, the new prime minister Rishi Sunak continues the inversion of Liz Truss' policies, opening the way to a period of fiscal consolidation that, while reducing pressure on Sterling and Gilts in the short term, is likely to pose medium-term challenges to firms, including SMEs, and the economy at large, via higher costs for investors, workers, and savers. After the Autumn budget, businesses should re-assess fiscal burden: the amount of taxes due in 2022 and especially in 2023 has likely changed.

The Nordics

Nordic nations are reeling under high inflation, economic uncertainty, and growth slowdown. High interest rates are hurting industrialized nations while property markets also look vulnerable. The region's energy infrastructure also faces threat of potential sabotage, like Nord-stream2 pipeline recently.

Inflation-related developments worsened the risk of recession in the region as consumer price growth in Norway and Denmark hit levels not seen in decades. Consumer prices in the Nordic region have reached levels unprecedented in decades, with Norway (7.5%), Denmark (10.1%), Sweden (10.9%) and Finland (8.3%) registering a 40-year high.

There are signs of contraction in 2022-23, with high household indebtedness, falling consumer spend and high borrowing costs causing economic distress. The factors causing inflation are high energy, food and commodity prices, along with capacity constraints, supply chain bottlenecks and overheating housing markets.

Asia Pacific

The outlook for the Asia-Pacific region is retained as 'deteriorating' as the region faces the brunt of cooling global economic growth and geopolitical tensions. Trade data from the region continues to show signs of weakness, and while some currencies pared back losses against the USD, they generally maintain a depreciation bias. While inflation in the region is more benign compared to other parts of the world, upward pressure is apparent, forcing further monetary tightening in the region. The recently concluded G-20 summit in Bali raised expectations that international coordination was possible.

Businesses should note the change in Mainland China's approach to virus management and a clear call from the governing leadership to stabilize the property sector and, in turn, the economy. It is a positive development for the regional economy but there is limited expectation of a swift turnaround. North Korea's aggressive missile tests, US's national security strategy document, shuffling of military resources in the Indo-Pacific and greater focus on security in Taiwan Region, Japan and South Korea, all points to heightened focus on security issues in the region. Businesses should review supply chains and prepare for higher financing and compliance costs. Portfolio investors should also note risks to domestic political stability in countries such as Pakistan and Malaysia.

Latin America & Caribbean

The United States granted Chevron Corporation a limited license to extract oil in Venezuela. However, this will not have a material impact on the Venezuelan economy since transfer of dividends to Petróleos de Venezuela (PDSA) or royalties and taxes to the government are prohibited. Given the minimal volumes of extraction, this will also have almost no impact on global crude oil prices in the short term. Concerns around corruption, economic mismanagement, and environmental concerns will continue to deter investments.

Brazil and Colombia could potentially loosen their fiscal policy over lower growth concerns, triggering volatility in the financial markets. Frictions surrounding the United States–Mexico–Canada Agreement continue to dampen investor appetite in Mexico. Developments on the next round of talks on trade disputes needs to be closely monitored. Political risks continue to remain elevated in Peru as the president faces a third impeachment attempt, resulting in a policy paralysis.

Eastern Europe & Central Asia

The outlook for EECA is retained at 'rapidly deteriorating' with Russia-Ukraine war in its 11th month with no sign of resolution. The regional economies are facing economic distress especially ones closely linked with Russia, Ukraine, or the EU. A few of the central Asian economies are gaining some support from high commodity and energy prices; however, higher inflation and central banks pushing rates higher are causing distress among both consumers and businesses.

The growth in the region is set to plummet sharply in 2023 with lower government revenues and worsening fiscal position coupled with high energy & commodity prices. The World Bank forecasts European and Central Asian economies to contract 0.2% in 2022, reflecting negative spillovers from the Russian invasion of Ukraine. Regional

inflation in Bulgaria, the Czech Republic, Romania and the Baltic countries is lower than other regions and economies, while it is high in Croatia, Hungary, Russia, Ukraine, Turkey and Poland. As per IMF forecasts, for many eastern European nations, higher energy subsidies and refugee support programs are expected to add 0.8-1% of GDP to the 2022 fiscal deficits compared to pre-war projections.

Middle East & North Africa

The overall outlook for the MENA region, especially for GCC countries, has weakened because of lower oil production and energy prices, which means a deceleration in growth in 2023. Real GDP growth in Saudi Arabia is predicted to slow to 3.8% in 2023 from an expected 9.1% in 2022, as external demand for oil weakens. Clients should factor in a moderate decline in economy-wide payments performance next year. In their latest meeting, OPEC+ decided to maintain the production cut at 2 million bbd, which amounts to ~2% of global oil demand.

Saudi Arabia's hosting of the Chinese President Xi Jinping for the first China-Arab States Summit and the China-Gulf Cooperation Council Summit in Riyadh is likely to further strain the ties between Washington and Riyadh. Riyadh sees a geopolitical order that is largely in flux, with an opportunity to enhance its leverage in the international system and is trying to project itself as a regional leader by broadening its interest in establishing ties with Europe, Russia on the energy front, and many Asian countries on the economic front.

Sub-Saharan Africa

As the rains fail for the fifth year in a row, a famine in East Africa is becoming more likely, the most severely affected countries being Ethiopia, Somalia and Kenya. Efforts to aid the needy populations are being undermined by violent conflicts in the Horn of Africa. The exceptional drought underlines the vulnerability of the region to climate-related risks, which are expected to intensify because of climate change. Along with delayed aid, Russia's invasion of Ukraine caused a spike in global food and fuel prices, making aid delivery more expensive.

Zimbabwe has long battled with power outages, but the problem has sharply worsened since its main generator, a hydro plant at the giant Kariba Dam, began to struggle with low water levels caused by the recurring droughts leading to power cuts of up to 19 hours every day. Zimbabwe imports some electricity from South Africa, but the most industrialized nation in Africa has also been experiencing heavy power cuts spanning six hours a day. The state-owned Eskom, which gets most of its electricity from ageing coal-fired power plants prone to breakdowns, plans to cut about 6,000 megawatts (MW) of power in a staggered manner to prevent a catastrophic collapse of the national electricity grid. South Africa also exports electricity to Mozambique, Lesotho, Swaziland, Namibia, and Botswana. The situation jeopardizes the availability of electricity in the region, and some countries are moving to secure supply - for example, Botswana is looking to purchase more power from Zambia.

DUN & BRADSTREET RISK INDICATOR

Dun & Bradstreet's Country Risk Indicator provides a comparative, cross-border assessment of the risk of doing business in a country. The risk indicator is divided into seven bands, ranging from DB1 to DB7 – DB1 is lowest risk, DB7 is highest risk. Each band is subdivided into quartiles (a-d), with 'a' representing slightly less risk than 'b' (and so on). Only the DB7 indicator is not divided into quartiles.

The individual DB risk indicators denote the following degrees of risk:

DB1	Lowest Risk	Lowest degree of uncertainty associated with expected returns, such as export payments and foreign debt servicing.
DB2	Low Risk	Lowest degree of uncertainty associated with expected returns. However, country-wide factors may result in higher volatility of returns at a future date.
DB3	Slight risk	Enough uncertainty over expected returns to warrant close monitoring of country risk. Customers should actively manage their risk exposures.
DB4	Moderate Risk	Significant uncertainty over expected returns. Risk-averse customers are advised to protect against potential losses.
DB5	High Risk	Considerable uncertainty associated with expected returns. Businesses are advised to limit their exposure and/or select high-return transactions only.
DB6	Very High Risk	Expected returns subject to large degree of volatility. A very high expected return is required to compensate for the additional risk or the cost of hedging such risk.
DB7	Highest Risk	Returns are almost impossible to predict with any accuracy. Business infrastructure has, in effect, broken down.

Rating and Outlook Changes:

Rating changes: Changes in rating are made when we judge that there has been a significant alteration in a country's overall circumstances – this could stem from a one-off event (e.g., a major natural disaster) or from a change in something structural/cyclical (e.g., an important shift in growth prospects). An upgrade indicates a significant change for the better, a downgrade a significant change for the worse. The number of quartiles of change indicates the extent of the improvement/deterioration in circumstances.

Outlook changes: The outlook trend indicates whether we think a country's next rating change is likely to be a downgrade ('Deteriorating' trend) or an upgrade ('Improving' trend). A 'Stable' outlook trend indicates that we do not currently anticipate a rating change in the near future.

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