Financial System Stabilized for Now, Yet an Environment of Unease Looms Large

Commentary:

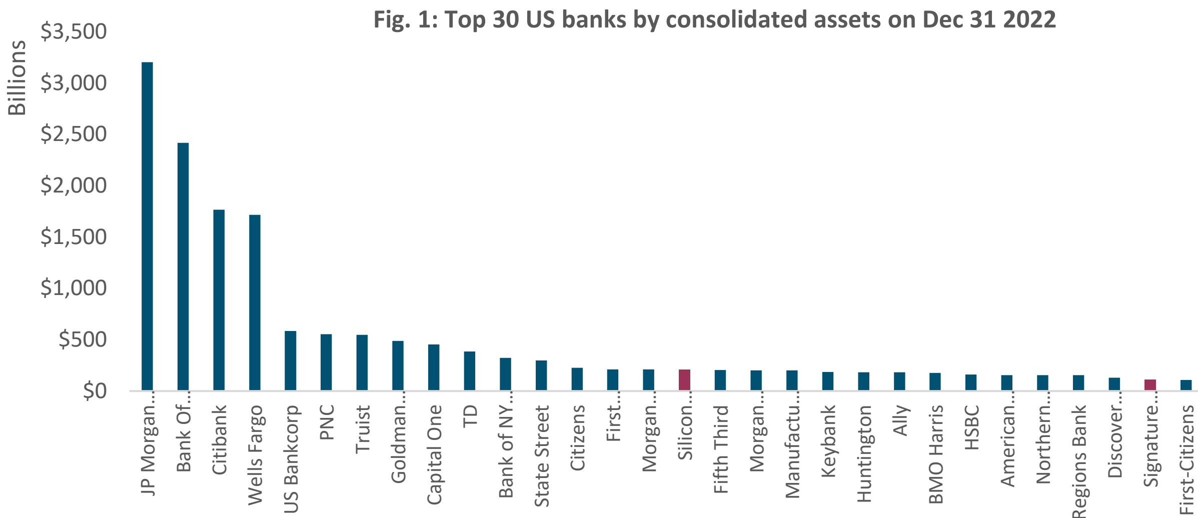
"Considering how connected the global financial and economic landscape is, failure of any financial institution will create ripples, and so the chain of events surrounding the case of SVB, Signature and Credit Suisse was not surprising. However, the comprehensive, decisive, and timely intervention of authorities averted a financial contagion and was a major boost toward restoring investor confidence. The focus in the medium term would be on regulatory scrutiny that banks, specifically small and mid-sized ones, will undergo; not to forget that tighter credit conditions will prevail across the global economy. It would be fair to add that events of the past weeks may have brought us closer to the end of the current rate hiking cycle, at least in the US, potentially leaving room for one final 25 bps hike in this quarter before a long pause. This likely factored in the RBI's recent decision to pause its rate hiking cycle as well. Although growth expectation have come down marginally, India appears to be a relative bright spot, especially in the medium term. Domestic demand is expected to remain resilient despite external headwinds and greater thrust on government capital expenditure could crowd-in private investment and bolster job creation." said Dr. Arun Singh, Global Chief Economist, Dun & Bradstreet.

Introduction

The failure of two mid-sized US banks – Silicon Valley Bank and Signature – and an arranged merger of the globally systemic Credit Suisse with rival UBS in quick succession made the global financial system very nervous. And that all this happened around the 'Ides of March', made for an interesting coincidence.

The extent and speed with which the US authorities acted was comprehensive and decisive, with the aim of restoring faith in the US banking system. Granted that the two regional lenders were not pre-designated as systemic, but from an asset-size standpoint, they were consequential (Fig. 1).

SVB and Signature were mid-sized banks, making them the second and third largest bank failures in US history.



Source: US Fed

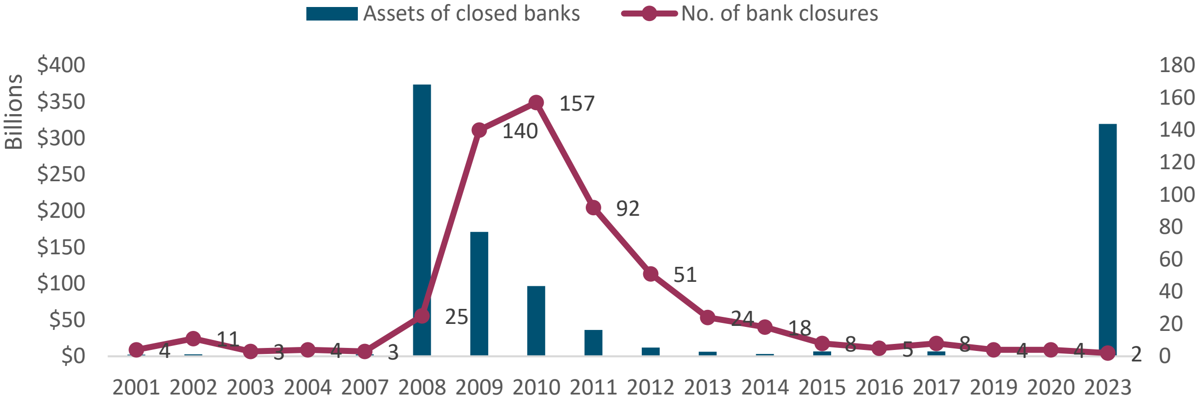
Despite those decisive actions, investor and depositor unease remained high, with peers such as First Republic Bank, PacWest, and Western Alliance coming under severe pressure. The hunt for weak links in the financial system spread across the Atlantic, leading to the eventual fall of Credit Suisse. Now that the storm seems to have settled, there are a few key takeaways.

What does it mean for other banks?

Since the first announcement of Silicon Valley Bank's takeover by the US Federal Deposit Insurance Corporation (FDIC), efforts to limit the contagion have only been ramped up. Apart from systemic treatments, full guarantee on deposits of the failed banks, and the deployment of a new emergency lending facility, which allows banks to borrow money from the Fed against securities at their face value (without haircuts), we have seen large private banks shoring up the deposits of smaller ones, central banks announcing a coordinated action plan to maintain dollar liquidity through the global financial system, and swift (and sweet) deals on failed banks. Most actions were geared toward protecting depositors. And yet, it is hard to say that the crisis of confidence is over.

Depositors are likely to continue to de-risk and move to the safety of large lenders. Banks with a narrow depositor base or with a high proportion of deposits above insurance thresholds or those whose management is perceived as weak, may continue to face a drain on their deposits. It is worth highlighting that more banks folded up in 2009 and 2010 – two years after the fall of Washington Mutual and Lehman Brothers – than in 2008 at the peak of the Global Financial Crisis (Fig. 2).

Bank failures in the US peaked two years after the fall of Washington Mutual and Lehman Brothers at the height of the 2008 Global Financial Crisis.



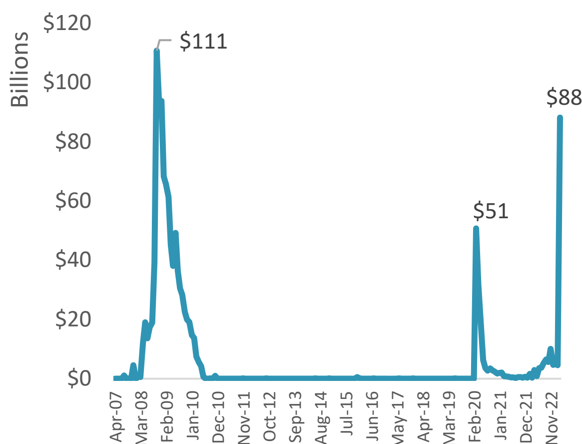
Source: FDIC

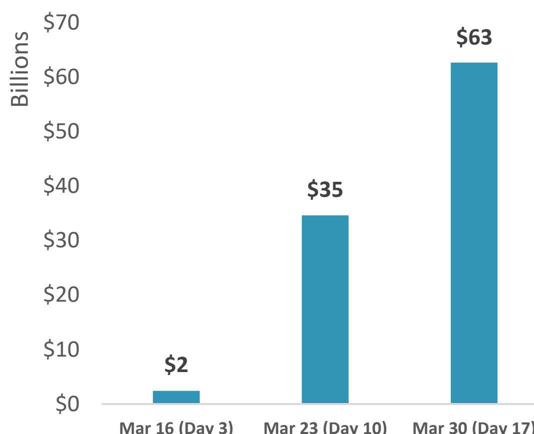
Also, it will be costlier and more difficult for banks to access non-deposit funding. At the end of March 2023, use of the US Fed's Primary Credit Facility was the highest since 2008 (Fig. 3) and even the use of the newly launched emergency facility, the Bank Term Funding Program, has been ramped up significantly (Fig. 4) since its launch on March 12, 2023. Meanwhile, investors are closely following the resolution process at these banks to assess their risk. Specifically, the treatment of AT1 bond holders in the settlement of Credit Suisse has sparked concerns among holders of similar bonds elsewhere in Europe, leading to a near halt on fresh issuances. When market activity picks up again, the asset class is likely to be repriced.

While the immediate focus of authorities has been to contain panic and douse fires, in the medium term, banks – particularly small and mid-sized banks – are likely to face far more stringent regulatory scrutiny. This will squeeze their operating margins and limit risk-taking.

The upshot of all this is that we may see more bank failures in the months to come, even if they do not make headlines.

Use of the Fed's special lending facilities has increased considerably, indicating stress on liquidity positions and cost of funding for banks.





Source: US Fed

What does it mean for the economy?

As a first step, these bank failures are likely to force all lenders and financial institutions to review their books closely to find parallels with the issues that plagued the failed institutions. This will create tighter credit conditions throughout the economy. Sectors such as commercial real estate that are reliant on funding from mid-sized lenders in the US will face the pinch a bit more strongly than the rest.

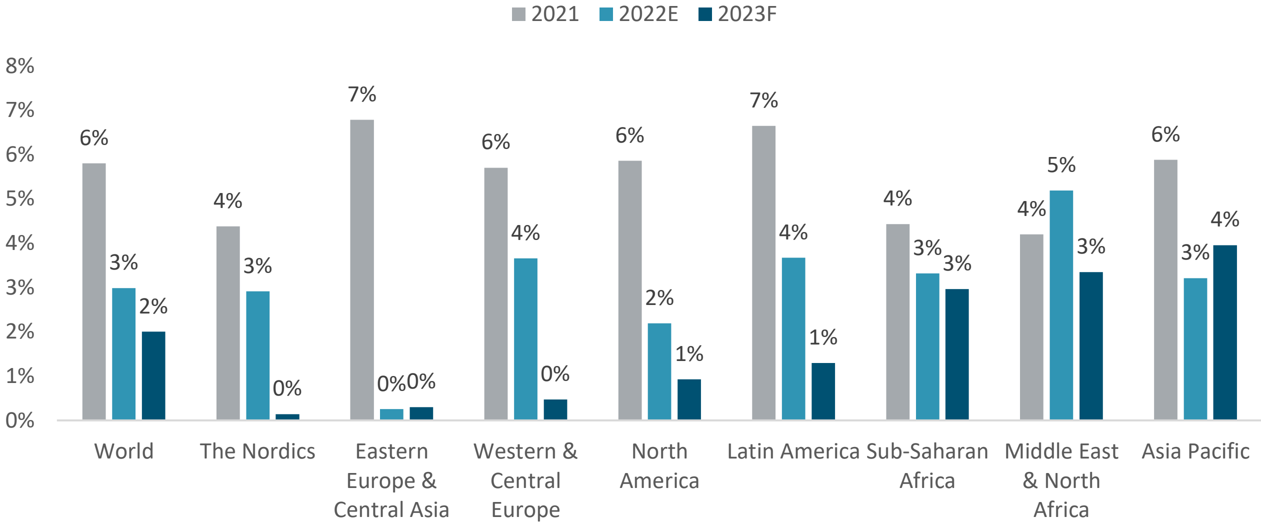
It is also worth placing these bank failures against the broader economic backdrop. For months, watchers of economic cycles were busy predicting a recession in the US economy. From that perspective alone, these bank failures have increased the downside risks to the economy.

The silver lining here is that these bank failures have implicitly tightened monetary conditions further (akin to the ongoing rate increments by the Fed), aiding the central bank's fight against persistently high inflation. The Fed proceeded with a 25-bps rate hike in its March meeting, in line with our expectations, sticking to its script of prioritizing inflation control. It has, however, balanced it out with a more dovish commentary that accompanied the rate hike. We believe that events of the past few weeks in the banking sector have brought us closer to the end of the current rate hiking cycle, at least in the US, potentially leaving room for one final 25-bps hike in this quarter before a long pause. For businesses, the bottom line remains that access to financing is more difficult and costlier than last year.

Commercial in Confidence

Regional Summaries

Global growth is expected to slowdown in 2023, with some growth opportunities in the Asia Pacific region.



Source: Haver Analytics; Dun & Bradstreet forecasts for 2023

North America

North America's regional outlook is maintained as 'deteriorating'. The economic picture in the region continues to give mixed signals. In Canada, the housing market and oil production continue to soften, whereas manufacturing and retail sales have managed to hold up well. In the US, private consumption remains an area of strength, whereas manufacturing continues to show sustained signs of weakness. In both the economies, labor markets are driving a large part of the economic resilience and making it harder to call which way the fight against inflation is going for now.

The Canadian government announced spending plans in its 2023/24 Budget. Titled 'Made-in-Canada Plan', most proposals were designed to incentivize investment in clean energy technology and address the realignment of global trading patterns. The Canadian economy rebounded sharply in January, with 0.5% m/m growth, but is set to cool in mid-2023 as consumers start feeling the impact of tight monetary policy.

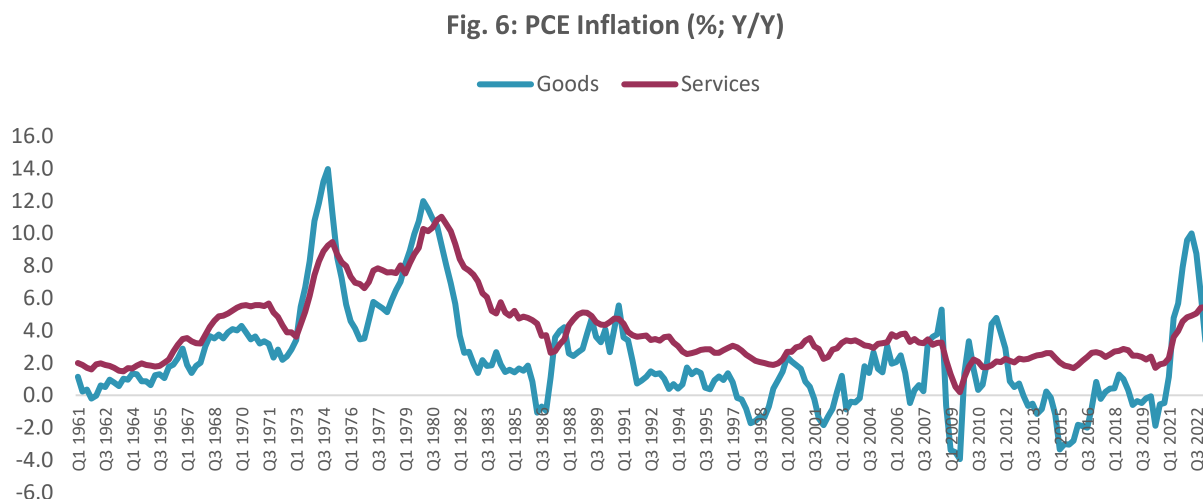
The biggest news though was that of two US bank failures, which disrupted financial markets and had spillovers into the European banking system as well. Following the collapse of SVB and Signature bank within two days of each other, the Federal Deposit Insurance Corporation and the US Fed stepped in with decisive moves to limit the panic from spreading. Regardless, a depositor rush to safety took a toll on the bank's peer group. While the economic fallout seems to have been contained for now, the risk of a systemic banking crisis is likely to dominate at least the first month of Q2. The US Fed persisted with a 25-bps rate hike in March (despite calls for a pause), but we believe that Q2 2023 is likely to see the last of rate increments in the current cycle. The Bank of Canada stayed its course, keeping interest rates steady for a second consecutive meeting on April 12.

Bank failures will further squeeze credit flow in the economy, and the risk to financial market stability has given the US Fed reason to pause rate increments sooner than what inflation dynamics would probably warrant. As credit conditions tighten further, we are likely to see downside risks to the economy becoming

more prominent in the coming quarter, although an outright recession is still not our base case scenario. Apart from the banking system, the performance of the housing market in the coming quarter would be worth monitoring, when activity in the market usually peaks seasonally. Also, the performance of household consumption, particularly on services, as the excess savings of households have been considerably run down and services inflation remains a key driver of current inflation in the region.

Services demand is still exerting upward pressures on inflation

Fig. 6: PCE Inflation (%; Y/Y)



Source: Haver Analytics

In the later weeks of the quarter, we expect market attention in the US to shift to a potential political quarrel over the raising of debt ceiling, as incoming data would bring clarity to a more accurate assessment on the ‘X-date’ – the date when the US Government will no longer be able to meet its obligations, barring an agreement on raising the debt ceiling. This is likely to add to the political frenzy that has kicked off in Q2 with the indictment of former President Donald Trump in one of the ongoing investigations.

Western & Central Europe

Western & Central Europe’s regional outlook remains at ‘deteriorating’. With the Eurozone and the UK narrowly avoiding recession in 2022, businesses had started to look to 2023 more optimistically. However, the failure of Silicon Valley Bank and the acquisition of Credit Suisse by UBS in March triggered financial volatility and spread fears of contagion across Europe and globally, abruptly cooling down much of the cheerful mood at the beginning of the year.

While contagion has so far been limited, and despite the European banking being significantly more capitalized than at the outset of the Global Financial Crisis, the risk of further confidence-driven turmoil remains. At the same time, though peaking in most European countries, inflation is only moderating slowly and continues to be elevated across Europe. UK inflation had been declining since October, when it reached its peak at 11% y/y (Fig. 7).

Fig. 7: Inflation

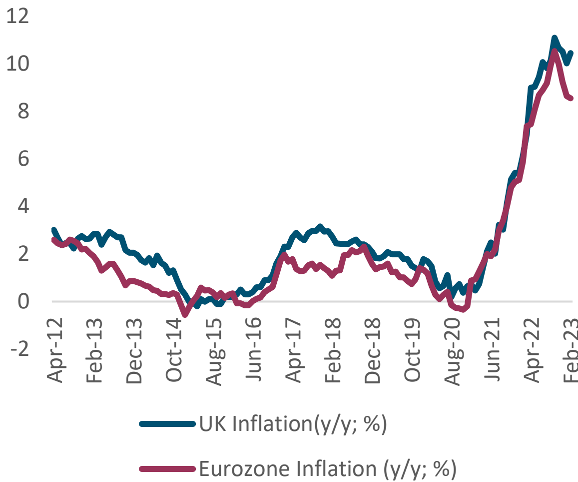
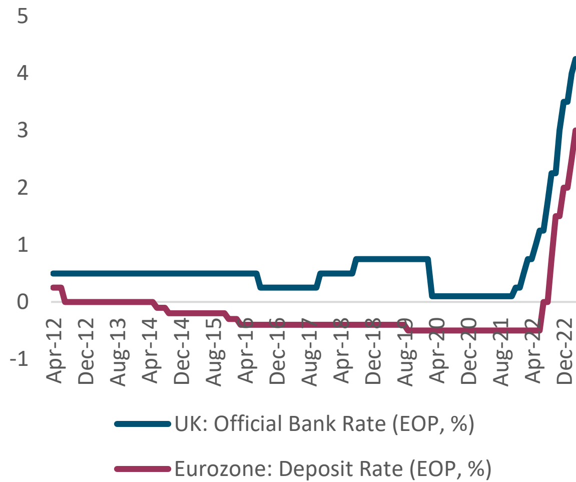
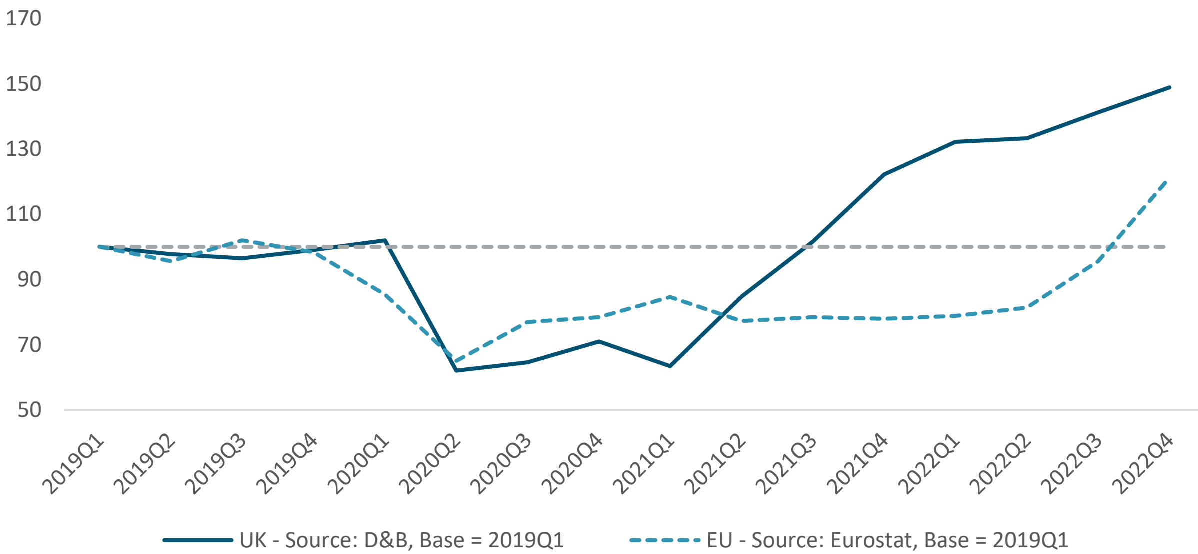


Fig. 8: Interest Rates



Source: Haver Analytics

However, it rose to 10.4% y/y in February, from 10% in January, mostly driven by increased food prices. Importantly, more than 80% of the items in the basket considered by ONS showed price increases, indicating that inflation continues to spread across the different sectors of the economy. Eurozone inflation has also been decreasing from the October peak of 10.5% y/y, reaching 8.5% in January. However, Eurostat flash estimates show that consumer prices have likely grown at 8.5% y/y in February too, an indication that inflationary pressures in the Eurozone are still strong. With core inflation rising above 6% y/y in both in the Eurozone and the UK, the ECB and the BoE could soon be caught between a rock and hard place, with price stability and financial stability encroaching on one another. Over the last year, interest rates have risen dramatically in both the UK and the Eurozone (Fig. 8). However, all else equal, and with inflationary pressures still strong, interest rates are likely to increase further before possibly stabilizing. Rate cuts are unlikely in the short term.



Source: Eurostat

With higher interest rates feeding through European economies, credit risk increases significantly, and businesses should remain vigilant. Insolvencies in the EU rose 27% in Q4 2022, relative to Q3; whereas business liquidations in the UK continue to fare at substantially higher level than in pre-Covid 19 pandemic years, consolidating a trend that started in 2021 (Fig. 9). While Europe has so far avoided the worst-case scenario of an energy-induced recession, inflation is yet to be countered and financial stability risks have emerged strongly. Pressure on business costs is likely to remain elevated and demand may contract as consumers continue to see their purchasing power eroded.

The Nordics

The Nordic regional outlook remains at 'deteriorating'. On average, the Nordic economies weathered the energy crisis relatively well in 2022. However, toward the end of the year, GDP growth turned negative in both Finland (-0.2%) and Sweden (-0.6%). Moreover, the March financial turmoil related to the failure of Silicon Valley Bank and the forced acquisition of Credit Suisse by UBS represents an important risk for regional economies, which are characterized by relatively overheated and highly concentrated property markets. While central banks should have the financial resources to intervene if necessary and banks are well capitalized, risks in the housing sector, in countries such as Sweden, are particularly high, with house prices expected to fall by up to 15-20% by the end of 2023 (peak to trough).

Fig. 10: Inflation Likely to Have Peaked but Moderates Slowly

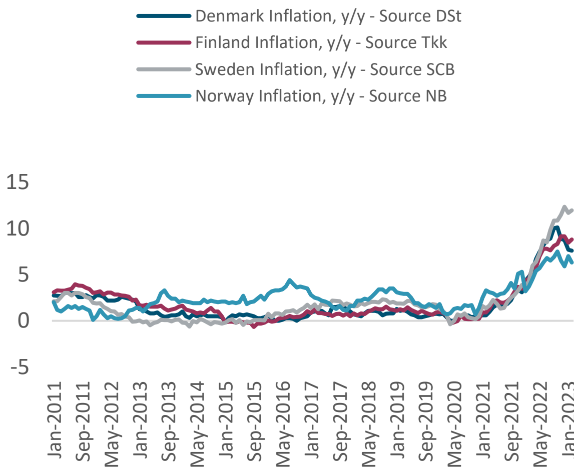
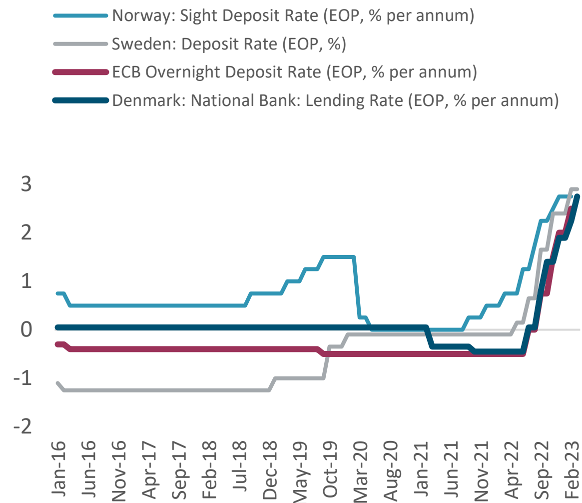


Fig. 11: Tighter financial conditions



Source: Haver Analytics; Eurostat

Inflation in the region seems to have peaked but remains elevated and in the double-digit territory in the case of Sweden (Fig. 10). Consequently, interest rates, which have increased dramatically in 2022, will have to continue to rise in the short term, before possibly stabilizing. When it comes to economic growth, a multi-speed dynamic is likely to play out the region in 2023, with negative annual growth in Finland and Sweden and positive annual growth in Norway and Denmark.

With higher interest rates feeding through Nordic economies, credit risk will increase significantly and businesses should remain vigilant. The region has so far avoided the worst-case scenario of an energy-induced recession, but growth rates were negative in Finland and Sweden toward the end of 2022. Moreover, inflation remains elevated, with pressure on business costs likely to remain strong and demand to contract as consumers continue to see their purchasing power eroded. At the same time, financial contagion unfolding from international financial markets could severely impact already vulnerable housing markets.

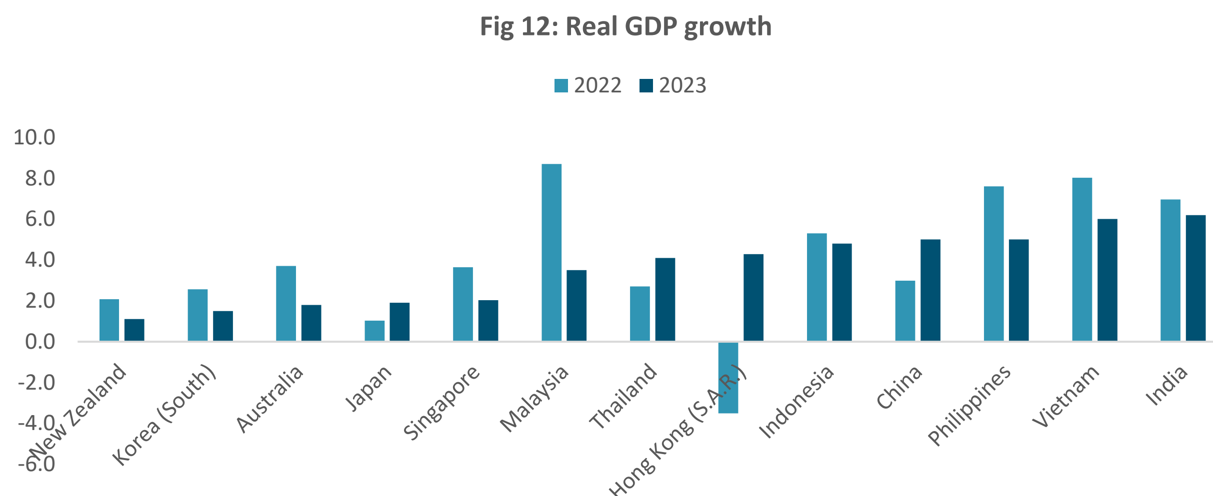
Asia Pacific

The outlook for Asia Pacific region is retained as 'stable'. Growth in 2023 is set to be slower than 2022, with the notable exceptions of Mainland China, Hong Kong SAR, and Thailand. China is consolidating its gains from reopening and is likely to achieve its growth target of around 5% for 2023. After contracting in 2022, Hong Kong SAR is preparing to turn a corner on its recent poor run on the economy, marked by negative growth in three out of the last four years. Thailand will be a key beneficiary of the return of Chinese tourists.

China's reopening and the clouded economic environment in US and Europe will set the tone for growth divergence in the region. In the near term, economies closely levered to the Chinese economy will gain from the reopening boost, while those exporting heavily to European and US markets would see a drag on external demand. It is worth highlighting though that beyond that, China's growth dividends will be limited for the rest of the world, as there is a greater emphasis on reviving consumption and ensuring macroeconomic stability. This has also led the Chinese Government to deploy policy support judiciously.

From a medium-term perspective, Indonesia and India remain bright growth spots; Vietnam also offers good growth and investment opportunities, but it may take some time to recover from the shadow of a

recent political shuffle at the top. The political reshuffle, in turn, stemmed from an ongoing anti-corruption campaign, which could strengthen the country institutionally in the long term, but for now, it has slowed economic activity.



Source: Haver Analytics and Dun & Bradstreet forecasts for 2023

Banking sector in the region has, thus far, proved resilient to the financial market turmoil witnessed in the US and Europe following bank failures; however, given considerable global linkages in the financial system, a contagion in case of further distress cannot be ruled out. Separately, financial institutions exposed to carry trades on bonds (e.g., Japanese financial institutions) will remain under the spotlight for balance sheet implications like those experienced by the Silicon Valley Bank in the US, especially if Japan finally embraces a change in its monetary policy stance. Other countries such as Vietnam – where the financial system has been under some sort of recent stress due to problems in the real estate sector and which has a history of a banking crisis – may attract attention and scrutiny if the contagion were to spread. China's central bank (PBoC) has preemptively cut its reserve requirement ratio to provide liquidity support in the aftermath of the failures at SVB and Credit Suisse. With inflation in control and the US Fed also nearing the end of its tightening cycle, other central banks in the region are also likely to cut rates swiftly in case the financial contagion spreads.

South Korea and Japan's move to resolve their long-standing dispute over the colonial-era-forced labor compensation will finally pave the way for resolution of trade disagreements. It would also lead to a deeper cooperation over security issues in the region. While inflationary pressures in the region remain contained, the propensity of countries to use export controls is not seemingly fading away. Australia became the latest country to propose legislations on energy export caps, which may become a source of the next round of disruption in energy supply chains and is a key thing to monitor for the coming quarter.

Finally, China's agreement to participate in the debt restructuring of Sri Lanka by offering relief in repayments has removed a key hurdle to unlocking IMF's funding for the island nation. This could lead to some meaningful progress on resolving Sri Lanka's debt crisis in the coming months. Meanwhile, Pakistan's slide toward default remains one to watch despite the note of confidence sounded by the country's leadership.

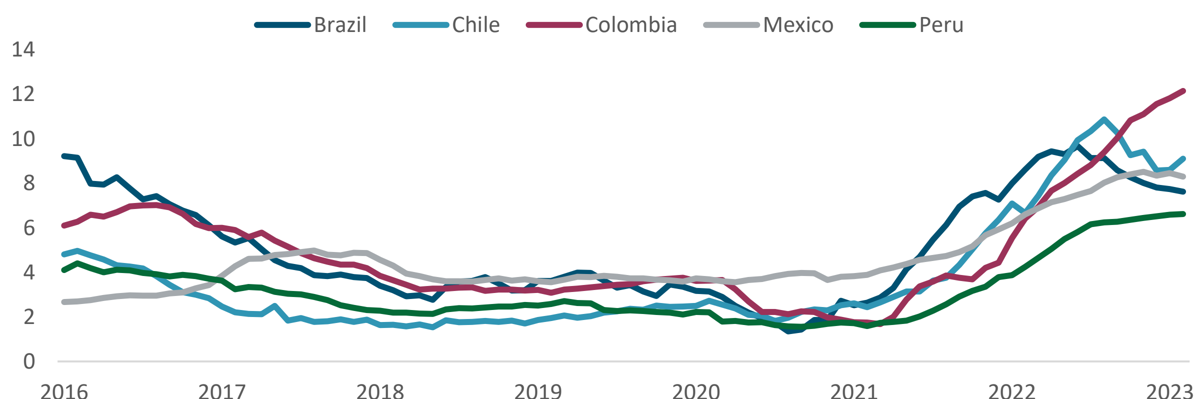
Latin America & Caribbean

We have maintained the outlook for Latin America at 'deteriorating'. The economy grew about 3.5% in 2022, employment increased significantly, and the service sector recovered from the effects of the Covid 19 pandemic. Economic growth will be tepid in 2023 amid a slowdown in the global economy in addition to high inflation and high interest rates that will weigh on consumer demand and business spending. Our projected growth for the region is at 1.3% in 2023, before it picks up slightly to 2.1% in 2024.

The collapse of Silicon Valley Bank and the turmoil around Credit Suisse are not likely to pose direct threats to Latin America's financial system, but the fallout of recent events would likely be felt through its impact on market confidence and knock-on effect on monetary policy and interest rates from the US Fed and other major central banks.

On a positive note, inflationary pressures are easing in many nations as a result of central banks' proactive and deliberate actions, as well as reduced food and energy prices globally. However, core inflation – which excludes food and energy – is still high and hovering at around 8% in Brazil, Mexico, and Chile. We believe that a rise in wages that is surpassing productivity growth poses a greater threat to inflation.

Fig. 13: Core inflation (% y/y)



Source: National Central Banks

China's abandonment of its 'zero-Covid' policy augurs well for commodity-exporting nations. Chile and Brazil will be among the main beneficiaries of China's demand recovery, as soybeans and copper prices climb up. Elsewhere in the region, countries would benefit from the tighter-than-expected labor market conditions in the US, as remittances strengthen. This is expected to mitigate some of the transfer and forex risks.

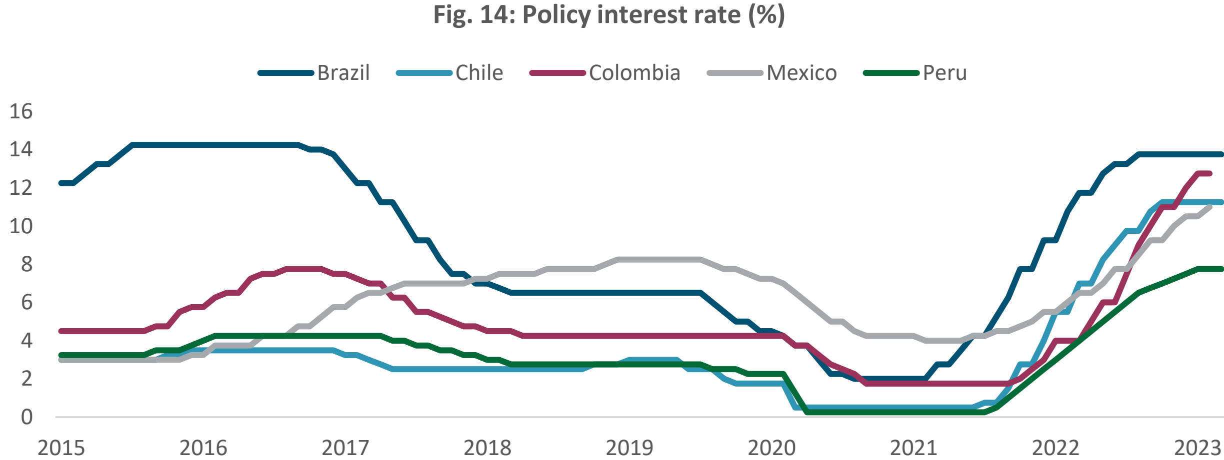
Social discontent and decreased trust in public institutions have been long-standing issues in Latin America. In 2023, Latin American politics is likely to see high levels of uncertainty, and in the worst case, governance crises across several countries in the region. General elections are due to be held in Paraguay and Guatemala in this quarter, and in Argentina, later in the year. Other significant elections and referendums will also be held throughout the region, including state elections in Mexico, local elections in Ecuador, and constitutional assembly elections in Chile. The ongoing social pressure in Peru could lead to earlier-than-planned general elections, while the status of presidential elections in Haiti remains uncertain.

The most significant of the elections is perhaps in Argentina, which is on the brink of an economic crisis. The worst drought in 60 years across the Pampas region is heightening fears of farmers' default and putting at risk targets agreed with the IMF. Negotiations are ongoing and recently the IMF announced it had reached a 'staff-level agreement' to ease the country's economic targets under a new debt plan, citing 'the challenges of an increasingly severe drought'. The headline inflation rate crossed 100% y/y in February for the first time since 1991, while the black-market rate for the peso has climbed to almost double of the official exchange rate.

After Lula da Silva assumed office in January as the President in Brazil, the governor of Banco Central do Brasil has come under criticism from the government for the 'excessive' increase in interest rates, which have been an impediment to growth. GDP contracted 0.2% q/q over the first three months of 2023, driven by weaker industrial output and services sector activity, interrupting five consecutive quarters of growth. We expect monetary policy to turn dovish; the BCB kept the SELIC rate unchanged at 13.75% in March, and we expect it to hold until mid-2023 before gradually bringing the rate down.

More central banks in Latin America will consider rate cuts as economic activity declines, inflation eases, and inflation expectations return to the target range, regardless of concern over the direction of the global economy. For instance, Costa Rica made headlines in mid-March by moving forward with a cut to its policy rate, becoming the first Latin American economy to enter a monetary easing cycle after sharply raising rates in 2021–2022. This was despite the banking sector stress in the US and Europe, which caused currency jitters worldwide.

Fig. 14: Policy interest rate (%)



Source: National Central Banks

Eastern Europe & Central Asia

The outlook for Eastern Europe & Central Asia is 'deteriorating'. Output in Eastern Europe, although expected to slow down sharply in 2023, would still be higher than Europe's average growth rate. It is feared that further disruptions to gas supply and impact of slowdown in the EU would also affect Eastern European economies.

A few economies in Eastern Europe appear to have higher fiscal vulnerabilities toward slowdown concerns in the EU region. Output in Eastern Europe was expected to expand around 5% in 2022 and will likely grow

around 3% in 2023. Smaller countries in the region are particularly fragile due to heavy reliance on external trade, poor diversification, and rising debts.

Although the Russian economy contracted around 3% in 2022, it has shown remarkable resilience and is expected to bounce back to growth in 2023. Similarly, Ukraine is likely to post growth in 2023 backed by Europe's Marshall plan and uptick in economic activities. Poland posted robust GDP expansion in 2022 but will likely witness muted growth in 2023. Turkey is expected to grow in the range of 3-4% backed by government spending ahead of planned elections and better-than-expected net exports, in part attributable to increased exports to Russia.

The near-term economic risks for the region are anemic industrial sector, high inflation, tightening financial conditions, a prolonged war, and high geopolitical uncertainty. High inflation is biting into real household incomes within the region.

Output in Central Asia is expected to grow around 5% in 2023, much like 2022. There has been a rise in consumption, driven by public sector wage hikes, high remittance flows and a sharp increase in shadow trade with Russia, as well as gains in commodity exporters. At the same time, Central Asian economies are facing heightened economic vulnerabilities due to the Russia-Ukraine war, high inflation, unsustainably high external debt, slowdown in consumption, and weakened export sector. Except Kazakhstan, which is expected to grow 3.5% in 2023, all other economies are likely to witness lower growth in 2023 than 2022. Kyrgyzstan's GDP grew 5.5% in 2022 compared to 3.6% in 2021 and a contraction of 8.4% in 2020. Tajikistan is expected to grow around 5% in 2023. Uzbekistan is expected to grow 4.9% in 2023. Surge in capital inflow, migrants from Russia, and a possible rerouting of some trade and financial flows could support these economies in 2023 and 2024.

Fig. 15: Real GDP growth (%)

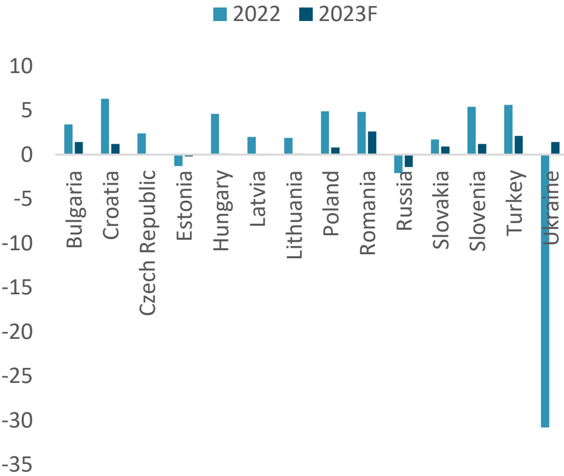
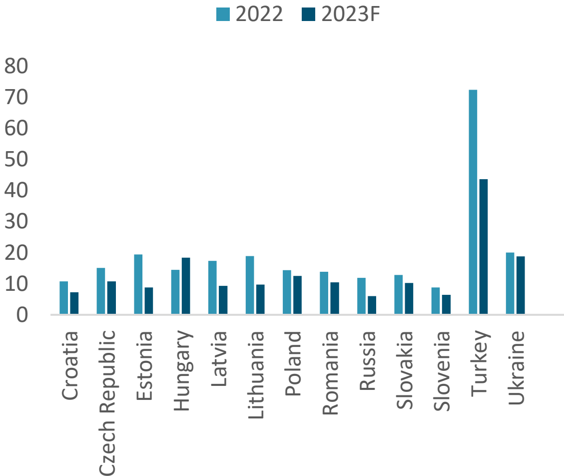


Fig. 16: Inflation (%)

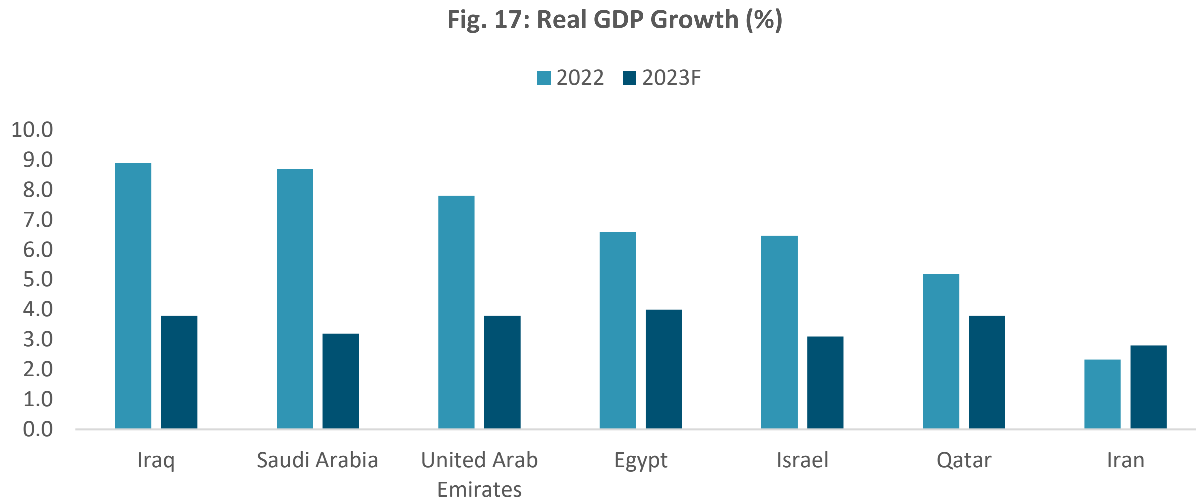


Source: Consensus Economics

Middle East & North Africa

The outlook for the MENA region is at 'stable' even as the economies of oil-rich Gulf Cooperation Council (GCC) countries have slightly lower GDP forecasts due to decrease in oil production and falling energy prices. We perceive the recent gyrations in the oil market in response to the financial sector volatility to be short-lived, hence having no substantial impact on growth prospects for the region. We believe fundamental macro factors will influence monetary policy in developed nations, expected to

remain contractionary, which pose more of a headwind for oil prices. The removal of covid restrictions in China will increase the demand for oil and boost tourism in the area.



Source: Haver Analytics and Dun & Bradstreet forecasts for 2023

On the geopolitical front, Saudi Arabia and Iran restored bilateral relations in March in a historic deal after years of hostility and a formal severance of connections in 2016. This reconciliation, brokered by China, can potentially bring some stability to the region. Close on the heels of this announcement, Saudi Arabia and Syria also agreed to reopen their embassies after an 11-year freeze in diplomatic relations, a major step forward in the gradual process of reintegrating Syria into the regional fold.

The Saudi-Iran deal implies improved security environment for Saudi Arabia. Saudi Arabia has been pursuing an assertive foreign policy seeking to balance the Kingdom's ties to Washington with its growing relationships with China and other Asian powers. From Iran's standpoint, this is a welcome development after years of isolation at a regional and international level. It follows a recent normalization of relations with the UAE and helps it fend off Western sanctions pressure, fitting into its 'Look to the East' policy. A testament to Iran's view is the prominence of Russian foreign investment into Iran, signaling increased cooperation between the two since the breaking out of the conflict between Russia and Ukraine.

The diplomatic breakthrough also shows China's prospective willingness to take on a bigger geopolitical role, mediating peace agreements and influencing the security architecture in the region as the US formerly did.

While the agreement is well-received throughout the Middle East, a Saudi Arabia-Iran détente could mean that the Abraham Accords could lose prominence, which will be a cause of concern for Israel. Israel has a strong stance against Iran's nuclear development and its efforts to form an Arab alliance to oppose Iran's nuclear ambitions could suffer a setback as both the UAE and Saudi Arabia have now re-established ties with Iran.

Israel has been facing difficulties on the domestic front as well. The government recently backtracked on its intention to push through a legislation aimed at reforming the judicial system. There had been some discord among the ruling coalition itself, with the minister of defense, Yoav Gallant, dismissed after he criticized the plans. There were widespread public protests – largest in more than a decade – which resulted, as critics claimed, that the legislation would drastically limit the Supreme Court's capacity to reject laws while also giving the government more control over the appointment of judges.

Sub-Saharan Africa

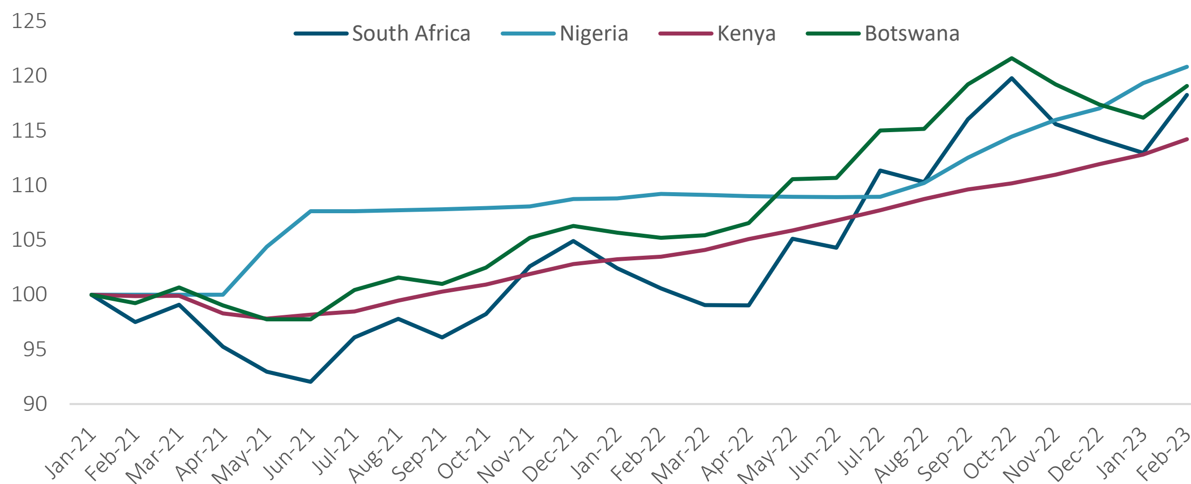
We have kept the outlook for Sub-Saharan Africa at 'deteriorating'. Regional growth is likely to have decelerated in Q1 this year, led by a slowdown in the global economy, volatile commodity prices and tightening financial conditions. Rising energy, fertilizer and food costs are also continuing to weigh on the region. Unrelenting drought in the Horn of Africa into Q2 means millions continue to face acute hunger and internal displacement. Somalia and Ethiopia are among the affected countries, where the effects of natural disasters are being accentuated by conflict and instability. But the outlook is not entirely gloomy as competition for the region's natural resources remains high and growth prospects vary by country.

Weaker external demand and a sharp uptick in global inflation have been compounded by weakness of domestic currencies, which is set to continue into Q2 2023. Monetary policy normalization in the developed world, weak investment flows, and risk aversion have caused capital outflow from the region. Currency weakness is especially acute in commodity-exporting countries such as Nigeria, South Africa, and Botswana where expectations of weaker demand are weighing on prices. The unfolding banking crisis is likely to tighten further global financial conditions, drive flight to safer assets and weigh on regional currencies. Policy space to address these challenges is thin since fiscal positions have deteriorated during the covid crisis and monetary policy kept shape with global central banks.

Within broader political instability, higher food and fuel costs continue to increase the likelihood of civil strife escalation. Bola Tinubu was declared Nigerian president-elect on March 1, following the 2023 presidential election, winning a third of votes. However, violent attacks broke out amid claims from opposition parties that the presidential vote was rigged, and over technical failures and alleged discrimination related to identity and party affiliation, ultimately leading to state governor elections being postponed. The security crises enveloping the elections are emblematic of the challenges facing the country. Slowing growth, elevated inflation, fuel insecurity, and heightened risks of social unrest have increased the demand for and cost of insurance for businesses operating and investing in Nigeria.

Economic performance this year across the Sub-Saharan region is, however, divergent; whereas Nigeria should still see just under 3.0% GDP growth and Kenya topping out around 4.0%, we expect only around 1.5% growth in South Africa. The most industrialized economy in the region has been experiencing severe power cuts for years since the state utility Eskom has been unable to reliably meet demand. But power shortages have escalated in recent months. South African President Ramaphosa appointed a minister for electricity with additional powers granted to government to sign emergency procurement procedures faster and with less oversight. Nonetheless, industries in the country will suffer until sustainable solutions create a meaningful impact, and we have recently made downgrades across our range of business indicators, as well as to the overall Country Risk Rating.

We expect international competition to secure Sub-Saharan Africa's minerals and energy products to intensify as risk appetite increases. A proposal in March by the European Commission has sought to coordinate the secure supply of essential raw materials and simultaneously reduce dependence on single large suppliers such as China. Currently South Africa, the Democratic Republic of Congo and Guinea are among the largest suppliers in the region to the EU of critical raw minerals, so this proposed legislation bodes well for established producers. In a similar vein and in the same month, the EU announced an initial investment of €50mn in the DRC's critical minerals sector and infrastructure. Formally part of the EU's Global Gateway Initiative to rival China's Belt and Roads Initiative, the investment will be used to improve geological mapping.



Source: Haver Analytics and Dun & Bradstreet forecasts for 2023

Key Commodity Outlook: Oil

In a surprise move, OPEC+ announced a cut in oil output until the end of 2023, starting with a 1.1 million barrels per day cut, which will increase to a 1.6 million barrels per day cut by July. Even assuming OPEC+ members' current lower-than-stipulated outputs, the net impact on supply will be an effective reduction of 0.8-1 million barrels per day for the remainder of 2023. Meanwhile, the US Strategic Petroleum Reserves (SPR) are running at a multi-decade low of 372 million barrels per day. In 2022, the Biden administration sold 180 million barrels from the SPR at $96 per barrel with a commitment to buy it back at around $70 per barrel, but the buyback never happened, even when oil prices fell to $70-80 range following the financial turmoil.

Following the OPEC+ announcement, the US will neither be able to supply any more oil from the SPR because its reserves are already very low, nor will it be able to buy more because prices will now stabilize at higher levels. As a result, the move by OPEC+ has reduced the US to a non-player status on global crude pricing power. In addition, global oil demand is set to accelerate sharply over the course of 2023, while global oil supply is expected to fall short in the second half of the year, leading to a deficit. OPEC+ may be ensuring this demand-supply dynamic returns to a deficit in the first half of the year by cutting output in advance.

Earlier, both the Federal Reserve and the European Central Bank stayed their course with hikes in interest rates in March. Inflationary pressures took precedence over recent financial market tensions while formulating monetary policy, signaling that fundamental macro considerations will be the ones impacting interest rate path. The reopening of China happened during a period of weak industrial activity, around the seasonally quiet Lunar New Year holiday period. However, road traffic and air travel in China were stronger than anticipated during the holiday period. Signs of improvement have also emerged in Europe, with several major European economies avoiding recession at the end of 2022. In the backdrop of this anticipated surge in demand, OPEC+'s move may result in sustained higher fuel inflation globally and a tougher path for central banks to tame inflation.