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Country Risk and the Global Outlook

March 2023

Economic expectations sobering as businesses approach end of Q1.

Commentary:

"As we approach the end of Q1 2023, there is more caution in the global economic landscape. That the global economy held up well in 2022 instilled faith in markets as they entered 2023, though inflation data coming from the eurozone and the US may deflate the initial cheer. Businesses can expect tight credit conditions and weaker-than-forecast growth. The US Fed's March meeting may result in another 25 bps rate hike, while data coming from Asia indicates balanced dynamics that underpin our stable outlook for the region. In Mainland China, much of March will be spent analyzing the two sessions meeting. While Mainland China's re-opening will bode well for other Asian economies, weakness in exports markets of the EU, the UK, and the US may dampen the region's prospects. Domestic demand in India is still robust, GDP likely to grow by 6.2% in FY24. The capital expenditure budgeted at 3.3% of GDP in 2023-24 is expected to crowd-in private investment and strengthen job creation along with demand. The banking crisis in the US and Europe unlikely to cause a domino effect, may restrict capital flows and cause the rupee to weaken." said Dr. Arun Singh, Global Chief Economist, Dun & Bradstreet.

INTRODUCTION

Businesses are preparing to close the first quarter of 2023 with mixed feeling about the state of the global economy. The confusion is apparent when we look at the GDP and inflation data. GDP growth figures confirmed that the global economy held up well in 2022, but not as well as the markets had initially thought - Q4 2022 GDP estimates for both the US and Germany were revised downward. Data on inflation suggests that we are closer to the end of the current monetary tightening cycle, but, again, not as close as the markets had initially forecast (or hoped). Inflation in parts of the eurozone came in higher than expected and even higher than prior months, US headline inflation didn't come down as much as expected, and core inflation around the world is still rising. Businesses are likely to face tight credit conditions and anemic growth for a prolonged period.

In the US, a combination of a historically tight labor market, a weak housing market and expectations of higher-for-longer rates mean that financial market positions are being reversed from just a few weeks ago. The yield on the 10-year Treasury note climbed up again, the dollar regained strength, and hawkish chatter is back on the rise. We retain our call of a 25bps hike in the US Fed's March meeting, based on the rationale that in times of uncertainty, moving slowly can help the Fed avoid erring on the other side of over-tightening. Our call is contingent on no surprises in the inflation readings that will come in about a week prior to the Fed's March meeting. Any digressions from the expected quarter point hike may be jarring though.

On the other hand, data coming out of Asia consolidated our view on the region. In Mainland China, following the reopening, manufacturing is gathering steam, travel around the Lunar New Year picked up and inflation remains in control. Mainland China has just announced a 5% GDP growth target for 2023. This target is lower than the one set for 2022 and is modest enough to be met in the absence of a major shock. Much of March will be spent analyzing the details of the 'Two Sessions' meetings to get an insight into the current thinking of policymakers of the world's second-largest economy. China's reopening will help other Asian economies as well, but weakness in the exports markets of the EU, the UK, and the US, a cyclical downturn in the semiconductor market, external imbalances of several low- and middle-income countries, and geopolitics all work as dampeners on the region's prospects. We view this as a balanced dynamic, underpinning our stable outlook on the region, which is still an outlier to the deteriorating outlook globally.

GLOBAL OUTLOOK: MIDDLE EAST REGION'S OUTLOOK MAY BE CLOUDED BY SOFTENING OIL PRICES AND LACK OF PROGRESS ON IRAN'S NUCLEAR ENRICHMENT

The Middle East Region has had a sobering start to the year with earthquakes in Syria and Turkey. Early in February, oil prices increased in expectation of supply interruptions caused by the earthquakes. Exports from the Ceyhan terminal - a hub for oil exports from Iraq and Azerbaijan, and located on the Mediterranean coast - were halted. Investors remain jittery as China's demand is expected to climb again later this year, but there isn't much room for supply to grow. In the short term, we anticipate the oil price will be largely flat at its current level, with sporadic spikes. For oil-dependent GCC countries, on balance, prospects for 2023 look weaker than 2022.

Dun & Bradstreet Country Risk Analysis			
Country	**January 2023**	**February 2023**	**Change**
Country Risk Rating Upgrades (risk level has improved)			
Angola	DB6a	DB5d	1 Quartile
Ireland	DB3a	DB2d	1 Quartile
Country Risk Rating Downgrades (risk level has deteriorated)			
Colombia	DB4c	DB4d	1 Quartile
Turkey	DB6a	DB6b	1 Quartile
Outlook Upgrades (from/to)			
Italy	Deteriorating	Stable	
Malta	Deteriorating	Stable	

Outlook Downgrades (from/to)		
Turkey	Stable	Deteriorating
Oman	Improving	Stable

REGIONAL SUMMARIES

North America

North America's regional outlook is maintained as 'deteriorating'. A bumper US jobs report set the tone for higher-for-longer interest rates. Following this, incoming data showing insufficient progress on inflation containment cemented the view that the US central bank may have to retain its hawkish tilt for a little longer than markets were expecting at the start of 2023. In Canada, Q4 GDP numbers showed that the economy failed to expand in the final quarter of 2022. While inflation continues to trend lower, the Bank of Canada's call to pause rate hikes may be tested if the US Fed surprises markets with a higher-than-expected rate increment at its next meeting in March.

While labor market across the two major economies remains strong, weakness is becoming apparent elsewhere. Housing markets have weakened considerably, which will hit consumer spending down the road. Separately, D&B's Small Business Health Index for the US declined for a fourth straight month in December 2022, with the decline being broad-based across sectors.

Western & Central Europe

Western & Central Europe's regional outlook is 'deteriorating'. Defying the gloomiest predictions, both the eurozone and the UK avoided a recession in 2022, albeit by a whisker. However, headwinds remain. Growth is set to lose momentum in the first half of 2023, and with core inflation substantially above target, both the ECB and the BoE are likely to remain on a hiking policy trajectory in the coming months.

While credit risk increases significantly in a tighter financial environment, businesses should remain vigilant. Insolvencies in the EU rose 27% in the last quarter of 2022, relative to the third quarter; whereas, business liquidations in the UK are at a substantially higher level than in pre-pandemic years, consolidating a trend that started in 2021. While Europe has so far avoided the worst-case scenario of an energy-induced prolonged recession, inflation is not beaten yet. Pressure on business costs is likely to remain elevated and demand will likely contract as consumers continue to experience an erosion in their purchasing power.

The Nordics

Nordic economies have withstood the economic downturn prevalent in Europe so far. However, higher interest rates, weaking consumer confidence, high inflation, and a crack in housing prices seem to be taking a toll on the economic growth, with the majority of the region contracting in Q1 2023 and risking being in a downturn for most of 2023.

The Nordic economies are likely to slow considerably even by EU standards and will likely contract in 2023 at a sharper pace than the EU average. In nearly all Nordic countries, the short-term outlook for domestic demand remains challenging, household spending will be on the lower side, and core inflation will still be upwards and outpace wage rates. Despite risk to growth, the central banks are set to continue hiking rates and unlikely to reverse this before 2024.

The housing and construction sector across Nordics is under high pressure and this may affect prospects of economic recovery. Housing prices in Nordics are expected to fall 20-30% along with a lack of demand for housing

projects. The hike in interest rates add to the woes of buyers and housing companies alike. The tightening credit flow also appears to lead to lower credit demand in the household and business sectors.

The labor markets in Nordic countries were tight in 2022; however, these will likely 'correct' over 2023 and 2024. Moreover, real wages are projected to fall by up to 15% in 2023. This, along with the decline in real disposable income and downfall in retail sales, further accentuates the recessionary pressure in the region. We've also noted that the high level of current household savings was able to keep the consumption at relatively decent levels. As these savings reduce in 2023, there is a high chance of a steeper downturn in consumption.

Asia Pacific

The outlook for Asia Pacific region is retained at 'stable'. Incoming data on Mainland China's domestic activity has raised expectations of a rebound in regional economic activity. While more regional central banks paused their current hiking cycle, pressure is returning on regional currencies considering the renewed focus on the path and length of US Fed rates. We expect the baseline scenario of a 25-bps hike in US Fed funds rate in the upcoming March meeting, which seems priced in for now.

China's reopening is balanced by the weakness in some of other large regional economies such as Korea, Taiwan Region, and Australia, and a poor balance of payments situation in smaller countries such as Sri Lanka, Pakistan, and Bangladesh. The Bank of Japan (BOJ) has announced the successor to Governor Kuroda. While he has hit a reassuring tone of policy continuity for now, we remain wary about the current levels of inflation in Japan. The BoJ is now the only major central bank with negative policy rates, which makes Japanese financial assets a target for speculative trades on expectations of change in policy stance.

Latin America & Caribbean

Inflation is turning out to be persistent and sticky across major markets, including Argentina, Chile, Colombia, Mexico, and Peru. While the increase in core inflation has been dominating the inflation narrative for Brazil and Mexico, we see a bigger risk to inflation emanating from an increase in wages, which is outpacing the increase in productivity levels. Central banks will continue to hike rates, albeit at a slower pace. The monetary tightening cycle would likely draw to a close in Mexico and Colombia by March 2023. Reflecting the upward shift in interest rate expectations, yields have climbed on sovereign bonds. This trend will likely continue in the near future.

China's abandonment of its 'zero-Covid' policy bodes well for commodity-exporting nations. Chile and Brazil will be among the main beneficiaries of China's demand recovery as soybeans and copper prices will climb. 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. Nevertheless, elevated inflation, tight monetary conditions, and the continuing possibility of civil unrest have the potential to erode business and consumer confidence and weigh on economic activity in the region.

Eastern Europe & Central Asia

For the EECA region, 2023 would be a year of weaker growth with delayed economic recovery. The combined effects of weaker Euro area economy, high inflation, lower business confidence, and the war in Ukraine will depress private spending, the industrial sector, and export markets, as well as lower domestic demand due to high interest rates.

The drop in energy prices acts as a temporary support to EECA economies, although core inflation is still high. Central banks in the region were among the first to raise interest rates and the first ones to go for rate hike pause.

With the natural gas price coming back to levels seen before the outbreak of Russia-Ukraine war, along with historically high gas storage across Europe usually seen around this time of the year, the impending energy crisis is largely thwarted. Countries in Eastern Europe have also enhanced their coal capacities to partially substitute the requirement of Russian gas.

For Central Asian economies, 2023 is expected to be a year of slowdown and possible a late recovery. Since Russia is the region's the key trading partner, continued disruption to trade with Russia is affecting these economies adversely. However, the surge in commodity prices and Europe's quest for an alternative energy source to Russia will benefit Central Asian economies in the near to medium term.

Middle East & North Africa

The outlook for the MENA region is at 'stable', though growth prospects for oil rich GCC economies have deteriorated slightly because of lower oil production and cooling energy prices. The abolition of Covid restrictions in China will support demand for oil, as well as tourism in the region. A series of deadly earthquakes in Syria in February has disrupted economic activity in the country's northern governorates until Q2 2023, with repairs to damaged energy infrastructure likely to continue into 2024. The ongoing civil war in the country will also disrupt attempts to deliver aid to both rebel- and regime-held areas. Damages to major air and sea terminals in Turkey, a significant trading partner and trade hub, will lead to delays to goods flow into the region.

In Israel, the government announced that it wants to push through legislation aimed at reforming the judicial system. This has led to widespread popular protests as critics claim the Supreme Court's ability to overturn laws would be severely curtailed while also giving the government more power over the appointment of judges. Israel might also be looking to step up its operations after reports emerged that Iran has successfully enriched uranium to 84%, which has the potential to destabilize the region.

Sub-Saharan Africa

The outlook for Sub-Saharan Africa has been maintained at 'deteriorating' amid East Africa's drought challenges and South Africa's continued and severe power outage. A global slowdown will add to the difficulties for Africa's key commodities exporters. There are some silver linings though - the terms of trade remain favorable and Europe has been increasingly looking more toward Africa as a substitute for Russian natural gas and oil. Below-normal rainfall is expected during the rainy season over the next three months in the Horn of Africa, which is heading into its sixth consecutive failed monsoon, with Ethiopia, Somalia and Kenya being the worst affected countries. The drought also exacerbates the challenges of food security and threatens social stability. Even for countries that are agro-based, high cost of fertilizers is proving to be a huge challenge.

The candidate from the incumbent APC party, Bola Tinubu, won the 2023 presidential election in Nigeria, which was fraught with technological failures, leading the opposition to question the accuracy of the result. The incoming president will take office in a shaky economic environment where high debt payment costs are restricting spending on public goods such as infrastructure investment and education spending and limiting the government's capacity to spur growth. The country is also facing an acute shortage of cash after the central bank decided to replace its banknotes with a re-designed currency. The most industrialized economy in the region, South Africa, has been experiencing severe power cuts, to the point where President Ramaphosa declared a "state of disaster" and enabled the government with additional powers to sign emergency procurement procedures faster and with less oversight.

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 the lowest risk, DB7 is the 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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