



## AFRICA

### Mozambique: election results confirm clear victory for FRELIMO and President Guebuza

- > **Event:** The ruling Front for the Liberation of Mozambique (FRELIMO) has strengthened its position and now has 191 of 250 parliamentary seats. FRELIMO member Armando Guebuza secured 75% of the votes in the first round of the presidential elections and can thus start his second presidential term. The landslide victory is, however, less convincing than it appears at first sight, with a persisting democratic deficit and voter turnout under 50%.
- > **Impact on country risk:** Foreign exchange revenue from aluminium exports declined sharply in 2009 but overall the country proved fairly resilient during the global economic crisis. The authorities have signed an IMF agreement to improve external liquidity, and political stability along with the policy mix have helped to maintain the country's political risk ratings (**analyst:** Inge Lambrechts, i.lambrechts@ondd.be).

## ASIA

### Philippines: state of emergency declared in the South after extraordinary carnage

- > **Event:** On 23 November, 57 people, among them many elected politicians and a dozen of journalists, were killed by armed gunmen in the Maguindanao province on the island of Mindanao. The national police has arrested the main suspect, Andal Ampatuan Jr, a mayor in the named province, member of Arroyo's party and son of the powerful province governor. While rejecting any suspicion, he is accused of having organised the massacre through his private militia to prevent a representative of a rival clan from running during the next provincial elections. Faced with high pressure, President Gloria Arroyo has sent additional troops to the island to capture all perpetrators of the killings and restore order.
- > **Impact on country risk:** The politically motivated carnage comes at a bad time for the incumbent President, who had just resigned as head of the ruling Lakas-Kampi-CMD coalition. Coalition candidate Gilbert Teodoro can now start campaigning for the upcoming presidential elections in May 2010. His first task will be restoring the ruling coalition's popularity, which has been seriously tarnished over the last few years given Arroyo's weak legitimacy after several accusations of corruption and electoral fraud. The latest outburst of political violence clearly highlights the risk of further political instability until May. (**analyst:** Raphaël Cecchi, r.cecchi@ondd.be)

### Vietnam: slight devaluation of the dong and monetary tightening by the Central bank

- > **Event:** The State Bank, Vietnam's central bank, has made a double move. For the first time since last December, it devalued the dong by 5.2% against the USD to mitigate the widening trade deficit and tightened the dong's daily trading band from 5 to 3% to limit future decline. Secondly, the State Bank has decided to raise its benchmark interest rate from 7 to 8% to reign in accelerating inflation.
- > **Impact on country risk:** Devaluation could improve the competitiveness of Vietnam's falling exports hit by flat US demand, and could drive back the country's swelling trade deficit. However, the move could put the dong under increased pressure in the upcoming months and could further

undermine already weak confidence in the local currency, as was shown by the significant drop in domestic stock markets following the announcement. The authorities' ability to defend the dong is after all constrained by foreign exchange reserves still decreasing due to significantly lower capital inflows and remittances. A weakening dong, together with a continued loose credit supply and possible quantitative easing to finance the heavy fiscal deficit would fuel re-emerging inflation pressure (4.35% y-o-y in November). The raise in interest rates, which will probably be repeated soon, points out the threat. Therefore, the authorities are likely to take other measures in the short term to deal with the array of problems. (**analyst:** Raphaël Cecchi, r.cecchi@ondd.be)

## EURASIA

### Kazakhstan: lingering banking issues raise fears of Argentine scenario

- > **Event:** Kazakhstan's troubled banking sector constitutes the main downside risk to Kazakhstan's economic outlook. Though other defaulting banks have reached rescheduling agreements with their creditors, negotiations with BTA Bank are dragging on. BTA defaulted on its foreign debts late April and has tried to restructure its sizeable foreign debts since then. BTA has the largest liabilities in the Kazakh banking sector as it attracted foreign funding to finance its (overly) ambitious expansion plans in recent years.
- > **Impact on country risk:** The official deadline for the complex rescheduling process with BTA is set at 7 December by the Kazakh supervisory authorities. With progress said to be limited so far, tension will mount as 7 December is inching closer and the risk increases of an outright liquidation of Kazakhstan's largest bank. Without a satisfactory arrangement for BTA, Kazakhstan could face an Argentine scenario and be shut out of international capital markets for years. Still, Kazakhstan has managed to attract considerable investments lately from countries China and South Korea. (**analyst:** Ben Deboeck, b.deboeck@ondd.be)

## EUROPE

### Russia : massive monetary easing does not result in swift economic resurgence

- > **Event:** Despite repeated reductions of the refinancing rate by the Central Bank, monetary easing has failed so far to kick-start lending by Russian banks. Even though liquidity is no longer an issue for the Russian banking sector, banks are little responsive to monetary policy as they brace themselves for further asset deterioration.
- > **Impact on country risk:** Current (still weak) signs of economic improvement can all be explained by an oil price surge. Despite recovering oil and gas exports, growth remains sluggish as domestic demand is very weak due to low credit facilities, among others. The prompt responsiveness of fundamentals to the slightest relapse of energy prices highlights their strong correlation. The larger part of capital inflows having returned to Russia lately consists of speculative short-term money, subject to volatile investors moods and of little use in terms of stable long-term growth, as was shown over the past year. (**analyst:** Ben Deboeck, b.deboeck@ondd.be)

## LATIN AMERICA

### Uruguay: Mujica wins the presidential election, paving the way for continuity

- > **Event:** Mujica has won the second run of the presidential elections, securing a second term for the ruling centre-left Frente Amplio coalition that controls both houses of congress. He campaigned on pledges to improve education, reduce poverty and fight crime. The economic team of the former government will remain in place. Since the Argentine crisis that struck Uruguay's economy with a vengeance, macroeconomic policies have focused on reducing vulnerabilities by skilful public debt management, a better-regulated banking system and a more flexible exchange rate regime. Thanks also to the appropriate response in terms of fiscal and monetary policies, the economy held out relatively well during the crisis, with growth rebounding in the second quarter of 2009.
- > **Impact on country risk:** Uruguay is well-positioned to benefit from the global recovery while the Mujica's victory has paved the way for the continuity of economic policy. FDI inflows have

improved productivity for the tradable sector, including agriculture and agribusiness. Nevertheless, the country remains dependent on regional development while still faced with high public debt and with the recent increase in fiscal deficit that needs to be tackled soon. (**analyst:** Pascaline della Faille, p.dellafaille@ondd.be)

#### Venezuela: two banks closed and two other seized add pressure to banking sector

- > **Event:** In mid-November, the government took control of four banks (Confederado, Banpro, Canarias and Bolivar) for allegedly failing to meet lending targets, making unauthorized share transactions and diverting deposits. Later on, the government decided to close two of them (Banpro and Canarias). Depositors will get their funds back. The two other banks will be administrated by the government. Clients will not have access to their deposits at those banks. Assets of these banks account for 8.4% of financial sector assets. The state now controls about 20% of the banking system. Contrary to past experience, the government made no mention of compensation payments to shareholders. Chavez has also said that he has “no problem” nationalizing the entire banking sector.
- > **Impact on country risk:** The economy is now officially in recession for the first time since 2003. Pressures on the banking system are likely to grow as the government claims that the lack of credit to the productive and strategic sector is one of the drivers of the current slump. (**analyst:** Pascaline della Faille, p.dellafaille@ondd.be)

### MIDDLE EAST

#### Lebanon: newly formed unity government but major economic reforms could still be put off

- > **Event:** Five months after the general elections, Saad Hariri presented his Unity Cabinet, including two Hezbollah ministers. The power sharing agreement is a first step towards restoring the country's stability but much-needed fiscal and economic reforms could still be stalled due to ideological divisions among cabinet members. Representatives of Saad Hariri's pro-Western Future bloc and other government fractions have different views on telecommunications and energy reforms.
- > **Impact on country risk:** After the 2006 conflict between Hezbollah and Israel, any new tensions between Hezbollah and Israel could pose serious challenges for the new government. In addition, the government has significant debt service obligations due to its huge public debt, which represents about 150% of its 2009 GDP. If disbursed, funds that were pledged at the Paris III donor conference could offer some relief and the relatively strong economic activity has also helped to raise fiscal revenue. If the new cabinet can enhance political stability and stimulate infrastructure investment, the country risk could gradually improve. However, it remains to be seen how effective the government will be. (**analyst:** Inge Lambrechts, i.lambrechts@ondd.be)

#### United Arab Emirates (UAE): Dubai World needs to extend maturities

- > **Event:** Dubai World has stated it seeks a debt standstill until May 2010 and has appointed a global accountancy group to negotiate a debt restructuring deal. The announcement came unexpectedly and has once again harmed investors' confidence. However, it was clear that Dubai World, which owns the troubled real estate developer Nakheel, faced important financing needs and that the central government of Dubai would not necessarily step in to meet all debt-servicing needs of all ailing government related entities. After all, in last month's edition of ONDD's Risk Monthly it was mentioned “(...) that there is also growing uncertainty whether there will be sufficient funds available to bail out all public companies in Dubai.” According to another public statement, DP World, Dubai World's port operator, would not be included in the debt restructuring.
- > **Impact on country risk:** Despite the damage to investor confidence and reduced creditworthiness for a number of Dubai's high-profile government-related entities, the political risks are mitigated at country level since the transfer risk is the responsibility of the UAE's Central Bank. Besides, Abu Dhabi still has a strong net foreign asset position. However, the lack of a clear bail-out strategy for public companies and individual emirates in financial distress is a cause for concern. (**analyst:** Inge Lambrechts, i.lambrechts@ondd.be)

## COUNTRY IN THE SPOTLIGHT: SAUDI ARABIA

The majority of Saudi Arabia's 24.2 million inhabitants are Sunni Muslims. The country has maintained good relations with Western powers and has supported the international fight against terrorism. The country also faces an internal terror threat and has stepped up actions against al-Qaida cells. Now, some al-Qaida members have moved to neighbouring Yemen. The security situation in Yemen has recently deteriorated and has spread to the border with Saudi-Arabia. The Yemeni government has been unable to control the fighting by Houthi rebels, who state that the Yemen Sunni government has marginalized Shia Muslims. The Yemeni government has to rely on Saudi actions to resolve the conflict. Saudi Arabian involvement is rather controversial as some analysts fear it may fan the grievances of the Houthi rebels. Iran, a Shia Muslim country, has condemned Saudi Arabia's intervention but denies it has provided military or financial support to the Houthi movement. The conflict in Yemen has thus fuelled discussion among two important regional powers backing different ideological parties in Lebanon. The geopolitical relations in the Gulf region are complex and remain a downside risk for Saudi Arabia.

### Strong reliance on oil sector influences economic outlook

The unprecedented volatility of the oil price, ranging from more than 145 USD a barrel in July 2008 to under 35 USD a barrel in February 2009, and to a more sustainable level of about 75 USD a barrel today, is intertwined with Saudi Arabia's economic situation. Indeed, Saudi Arabia is a swing producer and changes in its oil output have an impact on the national economy as well as on the international oil market. The OPEC decision to reduce production quotas as oil prices plummeted therefore implied a substantial cut in Saudi Arabia's oil production. In July 2008, the country pumped up 9.5 mn barrels of oil per day (b/d) against some 8.2 mn b/d today, creating an overcapacity of 4.3 mn b/d. As a result, the fall in the GDP growth rate from 4.4% in 2008 to -0,9% in 2009 is not surprising. Thanks to the government's economic support program, the non-oil sector has grown by 3.3% this year. The government has also set up an education plan to push back the unemployment rate. As the global economic crisis appears to be bottoming out and the oil market is expected to recover, the 2010 GDP growth forecast is more optimistic and in line with Saudi Arabia's average long-term economic growth, i.e. 4.1% during 2000-07.

### Credit risks prevail despite fairly limited transfer risk

To finance the public programs, the authorities can draw on national wealth accumulated during the commodity price boom. Indeed, the fiscal balance has shown a positive balance from 2003 onwards and public debt has declined to less than 14% of GDP in 2008. The foreign exchange reserves are managed by the Saudi Arabian Monetary Authority (SAMA) and exceeded 438 bn USD at the end of 2008. SAMA applied a conservative investment strategy and managed to avoid large financial losses. So, external liquidity is still excellent and foreign exchange reserves cover more than one year of all import costs. The SAMA's policies also helped to protect local banks during the global financial turmoil. Commercial banks' loan-to-deposit ratio is relatively low and official support also prevented a systemic banking crisis. Nonetheless, several local banks have exposure on two large Saudi conglomerates, Saad Group headed by Maan al Sanea and Ahmad Hamad Algosaihi and Brothers (AHAB), which have defaulted on their debts and are involved in a legal dispute over fraud. The total debt of the two companies to both local and international banks probably exceeds 20 bn USD. SAMA has indicated it is not willing to buy up the debts but announced a deal for local banks. Saad recently denied the existence of such a debt agreement. These developments have raised concerns among international creditors and have demonstrated that transparency issues continue to weigh on the business environment.

There is little risk of debt distress at the country level as the external debt ratio is expected to vary around 20% of GDP in 2010 and to represent less than 40% of current account receipts. This year's current account surplus will be modest as import needs and costs are traditionally high for narrowly-based economies but a higher current account surplus is forecast for 2010 as the current account receipts, which predominantly come from oil exports, are likely to increase again. Although the current account surplus will probably fail to reach the historically high level of 2008 (134.2 bn USD) during the next couple of years, the external position is expected to be benign during the forecast period. In all, the political risk outlook is favourable but complacency is out of place as Saudi Arabia is not immune to the problems of the global economy and commercial risks cannot be neglected.