Major Country Risk Developments
February 2020

By Byron Shoulton

Overview

The world confronts much uncertainty over the impact of the spreading coronavirus disease, which originated in **China** but has spread across the globe. Countries are now attempting to gauge the likely impact on economic growth, trade flows and travel. Companies and businesses have closed plants and offices in China, sent workers home and sometimes out of the country. Factories overseas are being closed as needed parts manufactured in China are not being shipped. The question of whether this will be a short-term distraction, or a longer-term global economic challenge is not fully known at this point. The World Health Organization (WHO) declared the disease a global public health emergency and will coordinate responses with Chinese agencies going forward. Chinese researchers are fully dedicated to finding a cure but there's no certainty how soon. At a minimum, this outbreak has altered perceptions about China as a reliable or safe destination for doing business and for travel at present. Disruptions and delays in the flow of goods into and out of China will be a fact of life - at least temporarily.

Meanwhile, Chinese citizens are showing anger over the government's response to the coronavirus (which at the time of this writing) had infected over 40,000 people in China, with a death toll of over 908 so far, and a further 2,700 reportedly in serious condition. China reportedly has another 30,300 suspected cases, while over 104,000 people have had close contact with infected persons according to China's national health commission.

The rapid spread of the virus has fueled discontent over the Chinese Communist Party's management of the outbreak...

The rapid spread of the virus has fueled discontent over the Chinese Communist Party's management of the outbreak, especially claims that local authorities in Wuhan city were prompted by the central government to conceal information about the disease during the early stages of the outbreak. The health emergency has brought normal life in China to a standstill, while supplies of face masks and other medical supplies have run low. State media, which usually is the mouthpiece for the government, exposed the apparent unpreparedness of local disease control and prevention officials who failed to adequately respond to basic questions about the extent of the outbreak. The revelations led to the removal of the heads of two agencies.

The world responded by suspending flights to and from China, screening travelers who recently visited China. More than 25,000 flights to and from China have been cancelled as more than 24 airlines suspend services to the country, an unprecedented shakeup in the world's second largest aviation market.

Despite the injection of $171 billion of additional liquidity into the country's financial system by the Chinese central bank [to help cushion a blow to confidence caused by the epidemic], Chinese stock markets tumbled upon returning from an extended lunar new- year holiday. China is also indicating that it may seek flexibility on its Phase-one trade deal with the U.S. that is supposed to take effect this month. Quarantines and travel lockdowns will hurt business activity and Chinese officials are evaluating cuts to the 2020 growth target as a result. Chinese ports are experiencing logistical constraints, holding up deliveries of agricultural goods including cargos of staples such as palm oil and soy. While Chinese authorities

are insisting that food safety can be ensured and that prices will remain stable, the port disruptions and closed air traffic highlight the country's current vulnerabilities. **Hong Kong** closed a majority of its checkpoints with the mainland after the first reported death from the disease occurred there. The commercial impact on Hong Kong will be huge, especially following seven months of civil unrest in the territory which resulted in that economy sliding into recession.

Chinese energy executives are projecting that the country's oil consumption will plunge by 25% in February as the coronavirus outbreak paralyses travel and shuts down industrial activity in the world's second-biggest economy. Executives at some of the country's largest refineries expect that nationwide demand will fall by a staggering 3.2 million barrels a day in February from last year — a drop equivalent to more than 3% of global consumption. Oil prices have already crashed on expectations of plunging demand as the Chinese authorities quarantined cities, restricted air and road travel, and extended factory closures. The projections of senior executives in China — the world's top oil importer — are likely to undermine market confidence further. Chinese oil demand in February 2019 was just under 13 million barrels a day, according to the International Energy Agency.

Saudi Arabia is pushing OPEC to make a major, short-term oil production cut of some 500,000 barrels per day as it seeks to respond to the impact of the coronavirus on demand for crude. The virus forced the authorities to put Wuhan, a key Chinese oil-and-gas hub, on lockdown and reduce movements inside China, the world's largest oil importer. Even as the deadly virus is eroding China's demand for crude, the 23-nation OPEC - plus alliance is split over whether the global health crisis now constitutes an oil-market emergency.

To revive flagging oil prices, Saudi Arabia has been advocating for a temporary round of cuts that would bring the alliance's total production curbs to around 1 million barrels a day. Brent crude, the global benchmark, has fallen 16% since January 7th, the day Chinese officials announced they had identified the new virus. Prices ticked higher on news of the Saudi plan.

Still, **Russian, Iranian and Nigerian** oil officials remain unconvinced that emergency action is needed. Despite the prodding of its de facto leader, Saudi Arabia, OPEC and 10 allied producers led by Russia stopped short of scheduling an emergency meeting of its full delegation. Instead, the group will soon hold a smaller technical meeting in Vienna to assess the virus's impact and make recommendations on possible collective action later. The group's next regularly scheduled meeting isn't due until early March.

Argentina's Buenos Aires province agreed to make a $250 million bond payment after failing to reach a deal with its creditors to accept a delay. The province will now seek to restructure its foreign debt obligations as it faces some $3 billion in payments due in 2020. The negotiations were closely watched by investors, as the outcome could affect talks to restructure more than $100 billion in sovereign Argentine debt. Many of the province's creditors also hold Argentine sovereign bonds.

USA

The U.S. ratified the USMCA, the revised NAFTA trade agreement among the U.S., Mexico and Canada. President Trump signed it into law in January. That leaves Canada as the only one of the three trade partners left to ratify the agreement. The Canadian parliament appears close to ratification. Not doing so would place Canada in the crosshairs of the Trump Administration as well as that of Mexico. Furthermore, like the other two countries, Canada needs the assurance of continuity in trade among the three partners which the revised agreement provides.

Separately, U.S. manufacturing rebounded in January, topping estimates and signaling growth in the beleaguered sector for the first time since last July. The

Institute of Supply Management's purchasing managers' index (PMI) increased to 50.9 in January, up from a four-year low of 47.8. While just above the 50 point level that signals expansion, the monthly advance was the largest since mid-2013. The figures, along with the strongest reading for the ISM's export index since September 2018 begs the question: is the worst over for American factories? The gain reflected sizable improvements in the orders and production components, while the employment gauge surged 9.5 points, also the largest gain in more than six years.

It is very likely that the reading reflects the positive impact of the recent Phase-one trade deal between the U.S. and China. In which case, the pick-up in manufacturing may be temporary as the halt in production by Boeing and uncertainties related to the coronavirus outbreak seem increasingly likely to stress global supply chains. The ISM reading shows the sector is barely expanding and remains in a precarious position. A quickly spreading coronavirus threatens to dampen activity abroad and adds to uncertainty about global prospects, while domestic demand has cooled, and Boeing's production halt of the 737 Max is weighing on producers.

Eight of 18 manufacturing industries reported growth in January, led by furniture, wood products, food and computers. Eight also reported that business shrank, including print, apparel, and electrical equipment sectors. Another report showed that companies are cutting back on capital expenditures.

Private construction spending on non-residential structures, including factories, hotels and office buildings, slumped 1.8% in December, the most since last April. However, U.S. housing construction activity picked up in recent months after declining at mid-year 2019. The consensus sentiment is that continued upward momentum in residential related construction during 1st half 2020 is likely, given continued strong employment, low interest rates, and a relatively stable pricing environment- which encourages demand. The recent strengthening of lumber prices underscores this trend.

The deficit in goods and services shrank 1.7% last year to $616.8 billion, the first decline since 2013, according to Commerce Department.

The U.S. trade deficit narrowed in 2019 for the first time in six years, as Americans imported less from overseas and exports fell amid trade tariffs and slower global growth. The deficit in goods and services shrank 1.7% last year to $616.8 billion, the first decline since 2013, according to Commerce Department. Demand for American-made products waned last year amid U.S. trade disputes with trading partners such as China and a weak global economy. Exports declined last year for the first time since 2016, dropping by 0.1%, but imports fell by a greater amount, 0.4%, leading to the drop in the deficit. Trade has been volatile in recent months, partly due to companies stockpiling imports to get ahead of anticipated tariff increases.

The trade numbers apparently were most evident in the fourth quarter when tariffs on clothing and other imports from China went into effect, leading to volatility in imports. The U.S. and China in January signed an agreement that amounts to a cease-fire in their two-year trade war, though it leaves in place tariffs on $370 billion of Chinese goods. The data also predates the coronavirus outbreak that has disrupted travel and global supply chains. U.S. total trade in goods with China—imports plus exports—fell 15.3% in 2019 from the year before. It was the biggest drop among the nation's top 20 trading partners.

The U.S. deficit in goods with China decreased 17.6% in 2019, falling to its lowest level since 2014. Last year, China slipped to third place in total trade in goods with the U.S., falling behind Canada in second place and Mexico in first. The U.S. economy has run trade deficits for decades, during both economic expansions and recessions, which reflects the fact that Americans consume more than they produce relative

to the rest of the world. To turn a trade deficit into a surplus, the U.S. would need to import less and export more of its products and services, which include foreign tourists coming to the U.S. Other factors such as last year's grounding of Boeing Co.'s 737 MAX jetliner have scrambled U.S. export data. Exports of civilian aircraft declined by 22.2% last year, while exports of industrial supplies and capital goods also decreased overall.

Nigeria

Nigeria declined to re-open its borders with neighbors in early February, despite setting a deadline to do so in November 2019. Last August Nigeria's president, Muhammadu Buhari, ordered a partial shutdown of trade across the frontier with Benin and in September he expanded the measure, imposing a total ban on trade in goods across all of Nigeria's land borders. In early November the closure was given an expiry date of January 31, 2020, but this has passed without the closure being lifted. Nigeria has been repeatedly pressed by fellow members of the Economic Community of West African States (ECOWAS) to re-open its borders but, although people have been allowed to cross, the border remains closed to goods from either side.

The closure is partly motivated by a desire to help Nigerian farmers by blocking the inflow of highly popular Asian rice—often smuggled in via Benin—forcing Nigerian consumers to buy costlier, home-grown rice. It also aims to curb the smuggling of subsidized Nigerian fuel into Benin and Togo by illicit marketers hoping to exploit arbitrage opportunities. The border closure embodies a generally protectionist mindset under the Buhari administration. Mr. Buhari has said that a decision on whether or not to reopen the borders to freight would only come after the government had considered the recommendations of a committee formed to review the issue, which is still considering its conclusions. The date when the border will open is uncertain but some expect it to coincide with the official start of the African Continental Free Trade Agreement (AfCFTA) on July 1, 2020. To openly ignore the advent of the trade deal so flagrantly would be diplomatically uncomfortable as Nigeria is a formal signatory to it. Also, inflation is ticking upwards (12%-14%) in Nigeria, reaching a level that the central bank calculates will harm output growth, potentially requiring a hike in interest rates. Higher food prices as a result of the ban on imports are also a recipe for public unrest in a country where poverty is rising. Steadily rising inflation places pressure on the government to rethink its border policy. The closures were conceived as a means to reduce smuggling, and the measure has support from agricultural lobbyists wanting to prevent the inflow of cheap imports. Whether this consideration outweighs the wider inflationary impact is an issue that requires swift resolution. President Buhari has long been a defender of consumer subsidies and interventions to shield Nigerians from high prices. The expectation is that the AfCTFA will be implemented in mid-2020, despite widespread delays. However, ECOWAS members outside of Nigeria will continue to lose valuable export earnings (particularly from agricultural exports) while the Nigerian import ban remains in place, until the AfCFTA comes into effect.

The country's public indebtedness more than doubled since President Buhari came to power in May 2015.

Nigeria's public debt stood at $85.38 billion at end-September 2019, up from $82 billion a year earlier according to Nigeria's Debt Management Office (DMO). The increase stemmed from growth in both domestic and foreign borrowing, as federal and state governments sought to plug budgetary gaps. The country's public indebtedness more than doubled since President Buhari came to power in May 2015. Critics of the Buhari administration's expansionary fiscal policy `worry that the debt accumulations put the country's fragile economy at risk of sliding into

another crisis, reminiscent of the problems that led to the 2005 debt-relief deal with the Paris Club. Addressing those concerns, the head of DMO recently revealed that Nigeria's debt-to-GDP ratio was 19%, which is below its sustainability limit of 25% and well under typical levels in developed countries. However, it was acknowledged that low government revenue means the debt service cost relative to revenue in Nigeria is high. About half of the federal government's income goes toward debt servicing.

Nigeria's public debt obligations are set to continue to rise in the medium term as improvements in revenue generation fall short of the income needed to finance a near-doubling of the minimum wage. Officials are hoping to source most of the foreign credit from concessionary financiers to minimize further exposure to higher-charging lenders who, as of last September, were owed $11.2 billion (41.5% of the country's external debt) up from $1.5 billion (14.1% of foreign debt) in September 2015. As a lower-middle-income country with access to international capital markets, it is unlikely that Nigeria will be able to meet all its financing needs through soft loans, requiring the issue of Eurobonds (which makes sense as a strategy, given currently loose global monetary conditions).

Bucking a global trend of declining poverty, Nigeria entered 2020 with an estimated 95 million people (47.7% of its population) living on less than $1.90 per day, according to estimates published by the World Poverty Clock, a monitoring service. As President Buhari has twice won an election promising to reduce poverty, the issue is a sore reminder of shortcomings of the sitting administration. According to the report all parts of Nigeria are affected by poverty in different ways, but with scarce resources there is not a lot that the government can do.

The country struggles to attract needed foreign direct investments. FDI inflows fell from $8.9 billion in 2011 to $2 billion in 2018. The reason for the continued lack of interest in Africa's largest economy among long-term investors are complex and include sluggish economic growth (about 2%), insecurity, uncertainty over the foreign-exchange regime, and stifling regulations. On top of this, there are regular disputes between the government and international government and international companies, (including a tax dispute with the South African telecommunications firm MTN) which help define Nigeria as an extra-risky place to do business. It is ranked 146th out of 180 countries covered in the Corruption Perception Index. That report's low appraisal of Nigeria has displeased the Buhari administration which came to power promising to root out endemic corruption. The sitting attorney general complains that the report is unfair and does not reflect recent achievements. Nigeria's official anti-corruption agency also rejected the evaluation as being baseless, noting that the ranking of the country as the fourth most corrupt country in West Africa is without empirical foundation.

National Bureau of Statistics, a government agency, found that 30.2% of Nigerian citizens who have made contact with a public official in the 12 months before the survey, had paid a bribe or were asked by a public official to pay a bribe.

The government has taken some steps to address corruption, including pursuing certain high-profile business and political figures suspected of double dealing. However, such attempts have had little effect on dispelling the culture of corruption that pervades many levels of the Nigerian state. The Corruption in Nigeria report published in December 2019 by the National Bureau of Statistics, a government agency, found that 30.2% of Nigerian citizens who have made contact with a public official in the 12 months before the survey, had paid a bribe or were asked by a public official to pay a bribe. This was an improvement on the 32.3% in the previous survey conducted in 2016. But the report noted that although the prevalence of

bribery might have decreased a bit, the frequency of bribe-paying had changed little since 2016. Hence, the challenge remains a major obstacle to prospective investors and or creditors. Progress on market-oriented reforms remains slow, given various vested interests and inefficiencies. The upstream oil sector remains characterized by joint-ventures between the state oil company and multinationals. This year, the government aims to squeeze revenue from oil companies to address fiscal imbalances. New royalty rates in the offshore subsector are said to have the potential to further harm direct investment inflows from foreign oil majors.

Guyana

The beginning of crude production and surging investment will boost GDP growth in Guyana over the coming year or two. Oil revenues should help support public spending growth as well as infrastructure investments, particularly as the Guyanese government looks to add regulatory capacity, improve social services and develop the country's transport network.

Growth projections have been revised for 2020-21 to 20% from 5.1% previously and to 17% from 5.4% previously. Still, there are significant uncertainties surrounding those forecasts given Guyana's limited data and the likelihood of volatile energy production in the short-to-medium term. The economic impact that oil and gas production would have on Guyana are significant, given the size of its offshore energy deposits and its limited economic development to date.

In December ExxonMobil, the primary operator in Guyana's offshore Stabroek bloc, produced its first barrels of oil, ahead of the previous expectation of first oil in early 2020. Forecasts are that Guyana will produce 55,000 barrels per day (b/d) in 2020, which will ramp up to 337,500 b/d by 2024, significantly boosting exports and offering tailwinds to domestic consumption. Forecasters note that sustained exploration in the Stabroek and other offshore blocks could boost Guyana's proven reserves and bolster the long-term production outlook.

The oil and gas and construction sectors will continue to attract foreign investment. In addition to ExxonMobil, European energy companies Total and Tullow oil will continue to increase investment in exploration and production capabilities. The Guyanese government has worked with foreign companies to develop technical training programs to hire more Guyanese nationals to help lower unemployment. The influx of oil revenues will also support public sector hiring and infrastructure investment as the country adds regulatory capacity, expands social services and modernizes its transport network. Guyana scores a 23.8 out of 100, the third -lowest score in the Caribbean, in the "Transport Network" subcomponent of Fitch's Operational Risk Index, underpinning the country's needs.

In addition to ExxonMobil, European energy companies Total and Tullow oil will continue to increase investment in exploration and production capabilities.

Separately, growth in other industries will likely be more uneven. Agriculture and mining have been historical drivers of Guyana's economic growth. However, they are likely to be eclipsed by the rising energy sector. Subsidy cuts to the state-owned Guyana Sugar and more limited access to the EU have drastically cut sugar production, and there is no expectation of any meaningful improvement in the foreseeable future. Modest growth in mining output is expected, as investments to expand gold production will likely be offset by a structural slowdown in bauxite production. As oil production ramps up and the Guyanese government expands public sector employment, the expectation is that many Guyanese workers will transition into jobs in the energy, construction and service

industries. There remain levels of uncertainty surrounding the economic and political outlook for Guyana. The still-ongoing oil discoveries, and Guyana's limited political and regulatory institutional capacities underscore a wide range of outcomes for real GDP growth and fiscal forecasts. Complicating accurate forecasting, the Bank of Guyana (the central bank) and the Bureau of Statistics do not regularly release GDP by expenditure data. While there are no published official or consensus estimates for Guyanese growth, the IMF forecasts real GDP growth of 85.6% y-o-y in 2020, which likely reflects more optimistic assumptions about how much oil production will come online in 2020 than some observers believe is probable.

A highly competitive March 2020 election may result in a change of government or produce political unrest. Following a contentious no confidence vote in December 2018, both the ruling A Partnership for National Unity (APNU) coalition and the opposition Peoples' Progressive Party/Civic (PPP) have engaged in heated partisan rhetoric, and there have been reported incidence of violence against PPP party activists.

APNU currently holds a single-vote majority in the National Assembly, and current polling shows an uncertain race. This suggests the possibility of social instability, especially given that the next government will control the disbursement of oil revenues. A shift to a PPP administration may result in negotiations to push for higher royalty rates from international energy companies or greater scrutiny of the extractive industries.

Brazil

Growth in economic activity is expected to be modest over the coming quarters. Private consumption and investment are forecast as the main drivers of this growth, underpinned by historically low interest rates and strengthening sentiment among consumers and businesses. The 2020 GDP growth forecast was revised to 2.3% from 2% previously.

The economy added 532,472 formal jobs in 2019, bringing the unemployment rate down to 11.2%, the lowest since May 2016.

A pick-up in momentum in December -January has influenced the conclusion that consumption will be the most significant driver of the rebound. Although private consumption growth plateaued over recent months, a steady strengthening labor market and low interest rates are feeding through to higher consumer confidence and spending.

The economy added 532,472 formal jobs in 2019, bringing the unemployment rate down to 11.2%, the lowest since May 2016. Consumer confidence, while below a spike following the inauguration of President Bolsonaro in January 2019, has ticked up heading into 2020, and retail sales rose at the start of the 4th quarter 2019.

The central bank cut its benchmark Selic target rate to a new historic low of 4.5% in December, where it is expected to remain in 2020. The expectation is that the rate cuts will continue to filter through the Brazilian financial system over the coming quarters, bringing interest rates on credit to new lows. As of November 2019, the average interest rate on new credit operations, at 23.9% annually, was the lowest since 2014.

With pension reform now complete, investment is picking up. That is in large part because pension reform reduces concerns over the government's long-term fiscal sustainability and allowed the central bank to cut rates. During the recent quarter the construction sector was among the strongest performers, expanding 4.4%, the second quarter of growth since mid-2014.

Beyond lower interest rates from bank financing, Brazil's largest corporates will also benefit from relatively strong domestic financial markets. Nevertheless, there are signs of slack in the economy, particularly in the industrial sector.

In its first year the Bolsonaro administration oversaw the enactment of contentious pension reforms. That success has bolstered business and investor confidence in the economic policy direction of the government. The stage now needs to be prepared to accomplish privatization of state-owned assets and enacting needed tax reforms. Much skill will be needed to push through these additional reforms in 2020-21. Success will hinge on forging the right alliances with congressional leaders. There are concerns that President Bolsonaro may not have built enough support in Congress to be able to prevail on these difficult and long debated reforms. Still, sentiments among businesses and some consumers have improved, with an increasing tilt toward optimism that the worst may now be over. Brazil appears to be gradually inching its way back to modest but sustained growth over the next few years, supported by essential policy reforms that would ease the burden on over-stretched state finances, with the rare possibility of eventually cutting taxes on businesses and households. Together, these trends would represent a sea change in Brazilian politics and economic management.

By Byron Shoulton, FCIA's International Economist
For questions / comments please contact Byron at
bshoulton@fcia.com

FCIA's Deals Of the Month

Trade Finance Policy: $10,000,000 limit of liability supporting a 2 year bullet payment in the financial sector, Central America.

Bank's Accounts Receivable Purchase Policy: Non-cancelable* Limits Policy with limit of liability of $50,000,000 insuring nonpayment risk on purchased receivables of US companies in the petrochemical sector.

What is Trade Credit Insurance?

If you are a company selling products or services on credit terms, or a financial institution financing those sales, you are providing trade credit. When you provide trade credit, non-payment by your buyer or borrower is always a possibility. FCIA's Trade Credit Insurance products protect you against loss resulting from that non-payment.

* ***Non-Cancelable Limits:*** *Subject to policy terms and conditions, after issuing the policy, the insurer may not unilaterally reduce any country or buyer limits.*

Although FCIA has made every effort to insure the accuracy of this publication we do not accept any responsibility whatsoever for - including but not limited to - errors, omissions, opinions or advice given. This publication is not a substitute for professional advice and all information is for guidance only. Coverage descriptions in this brochure are summarized. Consult the policy declarations and policy form for a full description of the applicable terms, conditions, limits and exclusions. Policies are underwritten by Great American Insurance Company, which is an authorized insurer in 50 states and the District of Columbia © Copyright 2020 by FCIA Management Company, Inc. FCIA logo (letters and design) are registered service marks of Great American Insurance Company. All rights reserved.