Political Risk Maps

Quarterly Newsletter: June 2023

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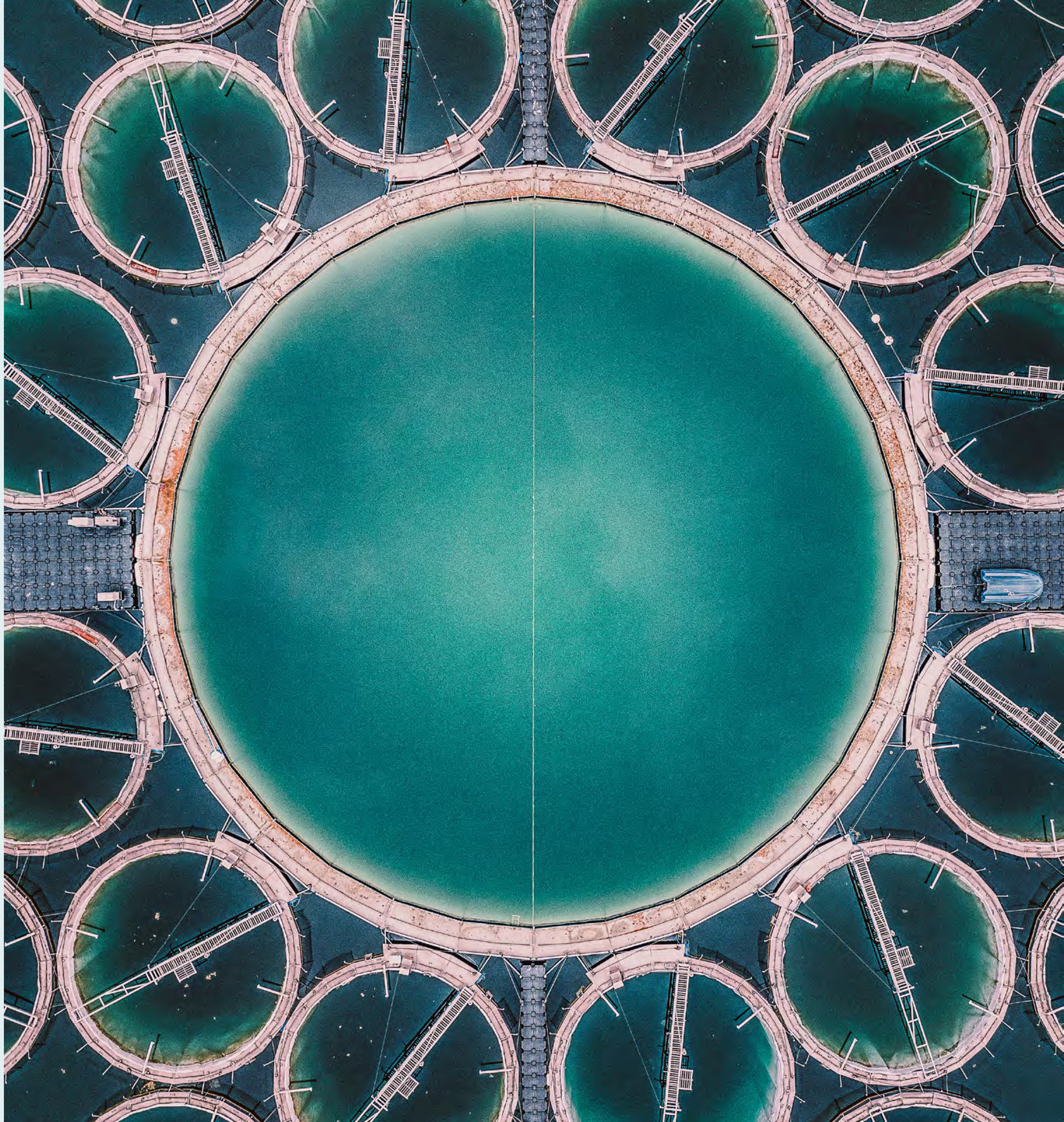

Summary

In this quarter's edition of Aon's Political Risk newsletter, we take a deep dive into the implications of EU-US tensions linked to recent green policies and what this means for emerging markets, as well as our regular look at major political developments worldwide.

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U.S./EU Green Tensions and EM Implications

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Tensions between the U.S. and the EU over the U.S. Inflation Reduction Act (IRA) are unlikely to end in a protectionist spiral. Rather, it reflects U.S. catch-up and competition that the EU has not experienced recently, though tensions do not need to be de-escalated at some stage this year.

With China setting its own course on climate change, increased competition should improve EM countries' access to technologies and at a more affordable price. However, the starting point in finances will have an influence in adoption, which favors big EM countries as low income EM countries are struggling with foreign currency debt.

Meanwhile, a major leap forward at COP28 in Abu Dhabi November 2023 remains unlikely, as strategic competition between the U.S. and China argues against agreement with the two key players.

U.S. Leap Forward, But EU Are More Sustainable

The U.S. IRA act has provided a leap forward for renewables in the U.S., with private sector investors scrambling to look at investments that have been made more attractive by the tax breaks for renewable electricity production in the act. Meanwhile, tax breaks for manufacturing, plus subsidies for electric vehicles with U.S. origins, are prompting major multinationals to consider North America rather than Europe e.g., VW's new car factory in the U.S. and battery factories in Canada rather than Europe.

European politicians are accusing the U.S. of not having a level playing field in contrast to the EU, which is causing tensions with the Biden administration. The EU Commission is suggesting that the EU should have its own minimum input of 40 percent in its new proposal for a net zero industry act (NZIA). Meanwhile, the EU also wants to impose a tax on goods from outside the EU (CBAM certificates) in carbon-intensive industries and avoid EU companies being at a disadvantage due to EU carbon taxes (EU ETS emission scheme).

However, this carbon border adjustment mechanism (CBAM) is due to start in 2026 on a free basis with the taxes kicking in between 2030-34. Finally, the EU wants to champion a critical rare earth materials act (heavily used in renewable products) to diversify supplies away from China.

Figure 1: U.S. and EU Electricity Production by Source

(% of total)

	Oil	Natural Gas	Coal	Nuclear Energy	Hydro Electric	Renewables
U.S.	0.5%	38.4%	22.2%	18.6%	5.8%	14.2%
European Union	1.5%	18.9%	15.2%	25.3%	11.9%	25.2%

Source: BP 2021

China is also accelerating renewables (mainly solar) in electricity production, both for domestic energy security reasons and to avoid adverse effects from any future price spikes in gas and oil prices. China wants to sustain leadership in production in the renewables fields (e.g., solar panels) to sustain exports and knowledge leadership, but does want to be selective in sourcing renewable goods abroad to protect domestic industries.

Climate change tensions are thus growing between the EU and U.S., as well as between the West and China. Could we see an outbreak of more green protectionism on one of the key growth drivers for the 2020's? Some context is worthwhile. The EU has felt that it has leadership in the renewables field and now finds the U.S. is trying to make a leap forward. However, the U.S. has lagged behind with cheap gas, meaning the percentage of renewables electricity production is less than the EU (Figure 1). Meanwhile, big oil and autos have slowed the rollout of electric vehicles and the associated charging structure with sales of U.S. electric vehicles being 5 percent in 2021 versus 16 percent and 17 percent for the EU and China respectively.

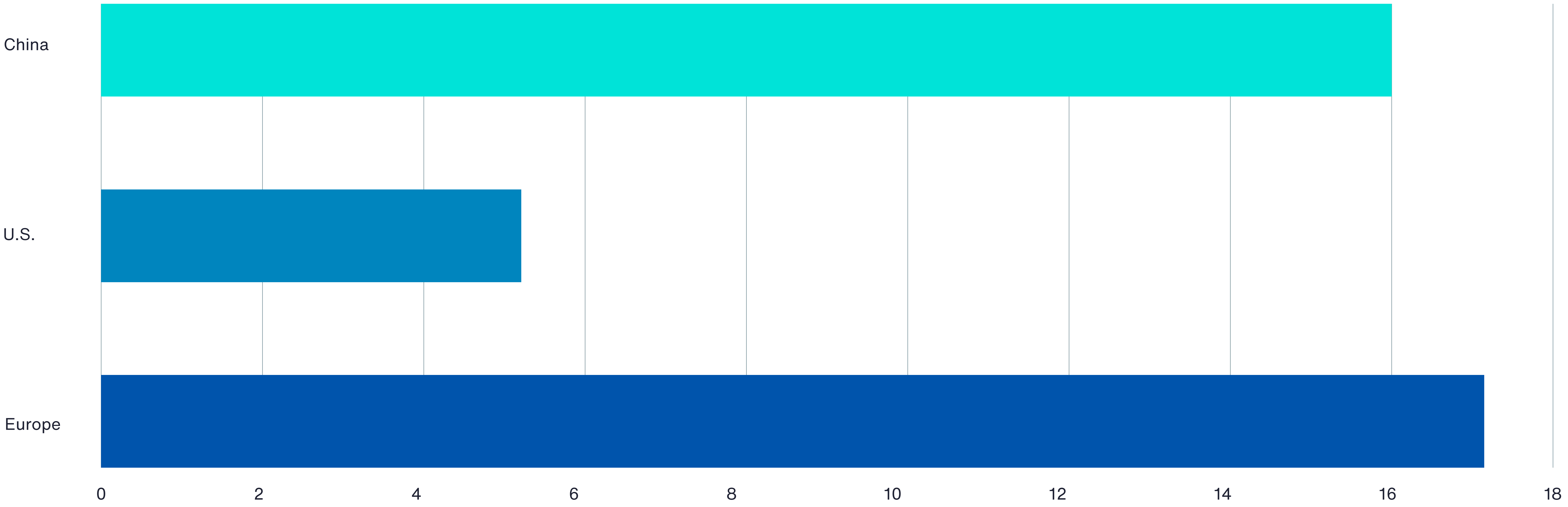
EU tensions with the U.S. thus reflect concerns about the EU losing its advantage. Europe does have its own set of green loans and grants that were a key part of the Next Gen Recovery and Resilience Facility (RRF) funds out of the 2020 COVID crisis. It is estimated that these total EUR 223 billion over the next 10 years, which contrasts with the estimated $369 billion (the tax credits are uncapped) from the U.S. IRA act. The critique is that the U.S. IRA will likely be more powerful in drawing in private funding due to tax breaks compared to the EU politically-targeted grants and loans (e.g., EUR 24 billion for high speed trains in Italy).

Even so, EU27 grants and loans are complemented by a huge financial commitment from individual EU government to subsidize and drive renewables energy production (around EUR 800-900 billion over the next 10 years). Overall, more competition in renewable and electric vehicles technologies is healthy for the global economy.

One other important issue does exist, however. The U.S. wants to see the EU taking a more proactive stance in restraining China's rise and on Taiwan, but Europe is split on this. Ideally, U.S./EU/China should try to align to speed up climate change commitments before the key G20 Summit in India September 9-10 and COP 28 in Abu Dhabi starting November 30 (where the key five-year stock take is due to take place). The problem is that U.S. and China relationship remains strained over the Ukraine war/Taiwan and EU countries are suspicious of China peace objectives.

Figure 2: U.S./China and Europe Share of Electric Cars Sold

Total %



Source: IEA 2021

All of this has some key impacts on EM countries and a number of points are worth making.

With all three major economic powers driving green technologies forward, this should make renewables and climate change solutions (e.g., electric vehicles/green hydrogen) more accessible and cheaper for EM countries to adopt.

A lot of countries are focused on energy security after the Ukraine war and this drives domestic renewables investment.

Brazil's existing large hydroelectricity production means it has an advantage domestically and in the region, as the Lula administration wants to champion Brazil's green industry. India remains focused on a rapid scale-up of solar power to replace imported fossil fuels and sustain strong growth with reasonable costed electricity production.

China itself is also rapidly scaling up solar power electricity production, which should start to restrain coal and gas imports in the coming years. Russia's initiatives on green adoption remains lacking, however, given the dominance of fossil fuel industries and the current domestic siege mentality with the Ukraine war. Finally, South Africa's solar potential is being ramped up too slowly to ensure a stable electricity supply given the current crisis in coal-fired power stations. This is set to be a big drag on South Africa's GDP growth in 2023-24, especially as the 2024 election will likely see a weak ANC and Democratic Alliance coalition.

While a lot of focus is on renewable electricity production in the 2020s, the other big wave is to reduce oil demand for transportation via electric vehicles and green hydrogen (produced by renewable electricity) for ships/trucks and potentially airplanes. This requires a country to have spare renewable electricity production, but also a coordinated domestic plan to support infrastructure build-out.

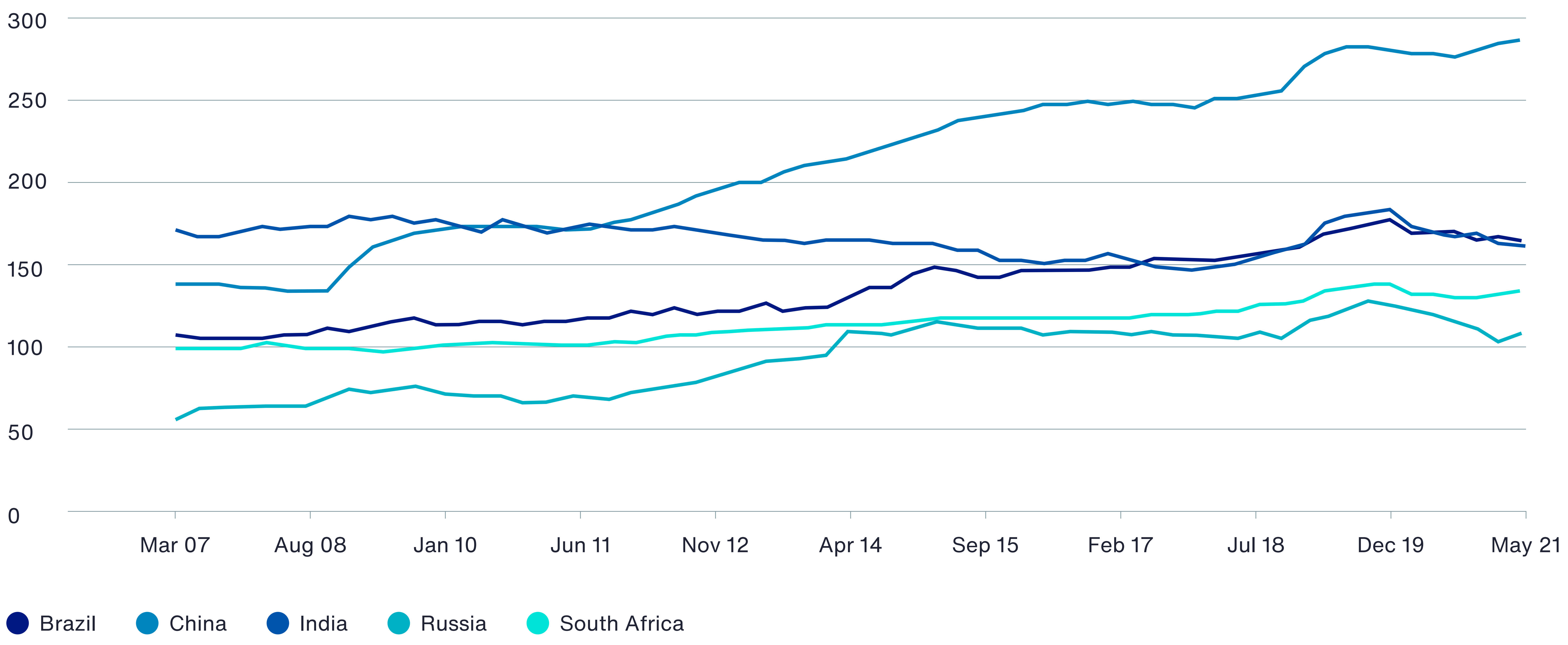
Saudi Arabia green hydrogen ambitions should be watched closely in the coming years, as they want to take leadership in this area. Brazil/China and India have lots of ambition to swing behind the greening of transport, but it is also a question of EM countries' finances to support government initiatives and aspirations.

The good news for big EM excluding China is that their total non-financial sector debt (government/households and corporates) are not excessive (Figure 3) provided that they get inflation back towards targets. Monetary policy tightening in Brazil/India and South Africa should bring down real and nominal interest rates in the remainder of 2023 and 2024/25. In turn, this should control debt servicing and allow some government structural support for the electricity and transport revolutions required by climate change objectives. China's total non-financial sector debt, however, is now higher than the U.S. or the Eurozone and has built up rapidly since 2007.

China's authorities can influence domestic creditors to roll over China's Yuan debt to avoid a major financial crisis, but new large increases in debt finance are unlikely. This will be a constraint in the latter part of this decade in terms of financing China's domestic green initiatives. However, low-income EM countries have a difficult financial position to allow them to accelerate electricity and transport transformations.

Figure 3: Total Non-Financial Sector Debt/GDP Since Q1 2007

Total %



Source: Source: Bank of International Settlements

The real difference in EM is between the big EM countries that largely borrow in their own currencies and low-income EM countries that have borrowed in foreign currencies since 2007. The IMF has estimated that 37 out of 69 low-income countries are in debt distress or at risk of debt distress and eight countries are currently in default. One of the critical issues is how debt restructuring occurs for the eight countries in default and others that have not defaulted but are in distress (e.g., Ethiopia).

This has become more complex as debt is no longer dominated by Western governments and banks, but includes private sector creditors and China. In the remainder of 2023, the Sri Lanka debt restructuring should be worth watching closely and the Ethiopia discussion on preemptive debt restructuring (with the IMF discussing a loan program and debt restructuring in tandem). The prospect is that the electricity and transport revolution will occur more slowly in low-income EM countries than big EM countries over the next one to two decades.

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Regional Overview of Political Risks

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Regional Overview of Political Risks

Asia

As several countries in Asia gear up for elections, the political landscape in the region remains tumultuous. While some Asian governments aim to secure a re-election via the introduction of populist measures, others are battling high inflation and dimming growth prospects. The political risk picture in Asia is therefore mixed. Although 2022 was a good year for growth across Asia, with economies slowing down in 2023, governments will have to prop up domestic demand and shield the public from high inflation and the fallout from excessive monetary tightening. This could spark some frustration among the public in these countries. Additionally, a risk of conflict in the South-China Sea cannot be completely ruled out. However, in our view, an open conflict remains unlikely for now, as the dominant countries choose to exercise restraint. Geopolitical risks pertaining to open or latent conflicts such as the South China Sea or the one between India and Pakistan could stoke instability intermittently.

One significant development in Asia is Sri Lanka's latest bailout package from the IMF. The government received an approval for an Extended Fund Facility worth $2.9 billion, with its first loan tranche already disbursed in early April. The approval comes after substantial negotiations between the Sri Lankan government and its bilateral creditors, mainly China, India and Japan. China held out the longest before providing assurances on the debt restructuring front. The package comes along with specific conditions pertaining to economic and social sector reforms, which the IMF will closely monitor the progress of. Sri Lanka is expected to provide a framework of debt restructuring for both domestic and external debt in the second quarter to the IMF. The government will also turn its focus towards implementing the Fund's policy recommendations. Unpopular policies though will likely trigger some pushback from the opposition parties and increases the risk of public protests. Restructuring of state-owned enterprises and measures towards fiscal consolidation could result in job losses and increased taxes, which could stoke public frustration. Therefore, political instability in Sri Lanka will be heightened in the near term, and will be compounded by the government's narrow parliamentary majority. Should the opposition mount challenges, it could potentially lead to the government's collapse and impede efforts to address the economic crisis.

Yet another politically sensitive nation in Asia, for now, is Myanmar. The country will remain in turmoil over the near term, as the 2021 coup and the repeated violent crackdown on the public will continue to fuel domestic unrest and the security situation in the country, including in urban areas remains dire. The junta's recent actions have caused a significant portion of the population, including ethnic Burmese - who previously supported the fight against the country's numerous ethnic armed groups and the repression of the Rohingya ethnic group - to turn against it.

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In a similar vein, it appears that the military will sustain its dominance in Thai politics. Despite all government efforts, it appears that the opposition party, Puea Thai Party (PTP) will win the most seats in Thailand's upcoming May 14th 2023 general election, as the public votes for a pro-democracy government. However, they will not secure a majority and a coalition government. This will likely mean an accommodative stance towards the military/royal family is likely, given the institutional set-up and therefore, pro-democracy protests may persist. Further, recent small-scale attacks in the Muslim-dominated southern provinces will continue. The recent visit by the Malaysian Prime Minister, Anwar Ibrahim, may lead to new peace talks between the Thai government and separatists in late 2023.

Elsewhere in Asia, on January 5th, Vietnam's National Assembly appointed Tran Hong Ha and Tran Luu Quang as deputy prime ministers, replacing Pham Binh Minh and Vu Duc Dam. The eviction of senior officials is a rarity in Vietnam, and is linked to corruption scandals in this case. Corruption remains rampant in Vietnamese politics and therefore any significant improvements on this front are unlikely. More recently, the national assembly on 2nd March elected Vo Van Thuong as Vietnam's new president for the 2021-2026 term. He secured a landslide victory, securing 487 out of 488 members' vote. The voting, however, was largely a procedural affair as the ruling Communist Party a day earlier had already picked him as new head of state.

While all appears quiet in Vietnam, South Korea is facing heat from its neighbor in the North. According to local media reports from South Korea, North Korea is believed to have conducted a test of a new type of solid-fuel intermediate to long-range ballistic missile on 13th April. South Korea's military concluded this after analyzing the missile's trajectory, which was different from the liquid fuel ballistic missiles that North Korea has used in the past. The missile traveled approximately 1,000 kilometers at an altitude of below 3,000 km before falling into the East Sea. Japan too issued an evacuation order for the island of Hokkaido, but retracted it later, given the lower range of the missile. Tensions between North and South Korea are expected to continue building up as South Korea responds to North Korea's threats with military build-up as well. The recent missile test follows North Korea's decision to stop taking inter-Korean military calls from South Korea without explanation.

Another geopolitical hotspot in the South China Sea is Taiwan. China-Taiwan relations appear to be at the lowest in 20-years. China has been carrying out regular military exercises around Taiwan in recent months. However, the likelihood of the U.S. getting involved in a cross-Strait conflict continues to deter China from a deliberate invasion. China's Navy is currently not strong enough to face the U.S. Navy in the scenario of a war and China's military buildup will take into the 2030s before it has enough aircraft carriers. The U.S. has sustained its support for Taiwan, and continues to provide national security. This is only likely to further fuel cross-Strait tensions. The risk of an open conflict will rise each time China engages in major military exercises over Taiwan. There is also a chance that China may threaten Taiwan's Pratas Islands, which could impact critical supply chains.

Meanwhile, on the Indian subcontinent, the political landscape is evolving rapidly. Bangladesh experienced a series of public protests in 2022, and the chance of these recurring in 2023 is high, as the government continues to bring out IMF-backed reforms which attract further public ire. The country is also gearing up for elections in January 2024, and political instability will remain elevated until then. The government led by the Awami League, under the leadership of incumbent Prime Minister, Sheikh Hasina Wajed will secure another victory, given the lack of formidable opposition and the party's deeply entrenched patronage network. There is a chance that the leading opposition party may stage protests and resort to violence in the run-up to the elections, elevating security concerns. In Afghanistan, the security situation remains bleak, as the Taliban continues to dominate the political sphere and rule with a tight fist. The Taliban's hardline interpretation of the sharia law, and its implementation of policies in line with it, could stoke low-level protests. The latest in a series of attacks was carried out by a suicide bomber outside the Ministry of Foreign Affairs in Kabul in March. This was the second such attack this year.

In neighboring Pakistan too, the political environment remains turbulent. The country is scheduled to have its national elections in H2-2023, and security and political instability will remain heightened in the run-up. The current coalition government has a razor-thin majority in parliament and enjoys little public support given its recently implemented austere measures to address the economic concerns Pakistan is facing. Pakistan is currently facing a balance of payments crisis, alongside elevated inflation and increasing terrorism. As a consequence, it is likely that the leader of the opposition, Imran Khan will be voted into power in the elections. However, he does not enjoy military support and therefore any improvement in the security or economic situation is unlikely even under him. Earlier in January, a suicide bomber killed close to 90 people in Peshawar, while over 20 other small blasts or attacks have been reported since the start of the year. It is noteworthy that Pakistan has reportedly overtaken Afghanistan as the most terror-hit country, according to a recent report by the Institute for Economics and Peace, Australia.

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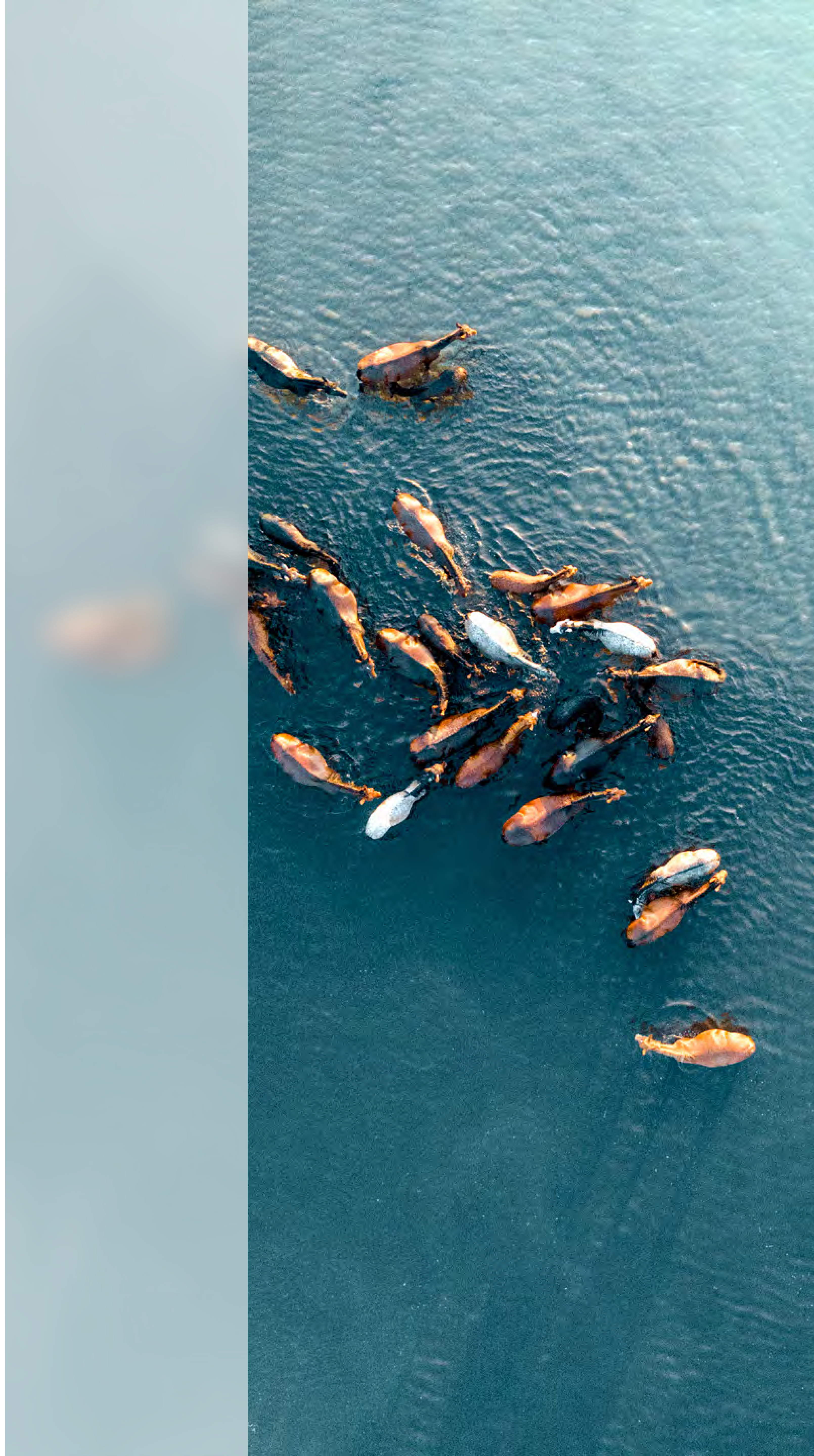
Across the border though, India continues to shine bright. With the Modi-led Bhartiya Junta Party enjoying a strong majority in parliament and ruling in several Indian states, the passing of legislation and policy implementation has been fairly easy. India's economic performance in 2022 has been robust, which continues to garner support for Mr Modi and his policy making. While there is little formidable opposition from any single party to the BJP, there is a high chance of several parties aligning to keep the BJP out of power in the May 2024 national elections. The chance of defeating the BJP with a majority remains minimal though. However, it is worth noting that while the BJP is enjoying support at the national level, it appears to be losing ground in state elections. Regional elections therefore will stoke friction in the run-up to May 2024. The latest improvements on the economic front, with inflation trending downward and business sentiment remaining robust, are also supportive of the government's public image. Mr Modi's popularity has not waned despite the recent Adani group crisis being linked to the BJP. There is however, a small chance of some communal violence across India in specific states such as West Bengal, Uttar Pradesh and Kerela. This is more on account of stoking public sentiment ahead of elections. Further, for India, a growing concern is the risk of a latent conflict with China turning into an open one. China from time to time is involved in skirmishes along the border and is known to incite some retaliation from the Indian military. Tensions have increased recently when China attempted to rename 11 Indian villages along the border. India responded by bolstering its military presence in the area.



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Eastern Europe and CIS

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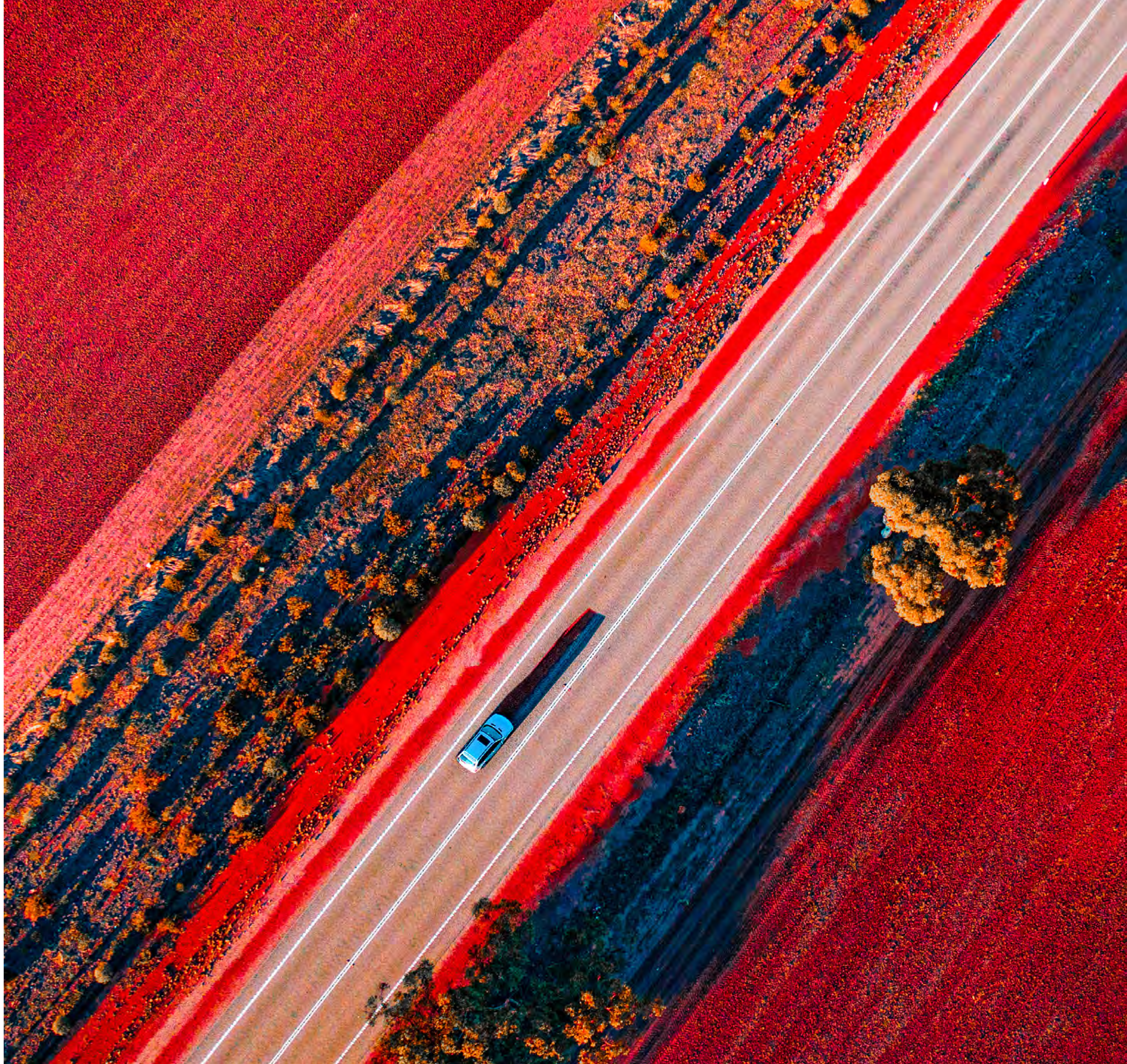
Russia's war in Ukraine is shifting towards a stalemate, with Russia's and Ukraine's spring offensives having failed to gain ground in eastern Ukraine. This active phase of the war can drag on, but prospects of a credible peace deal are slim. Hopes could rise of a ceasefire later in 2023, as China/India and others try to encourage an end to hostilities. However, the pre-conditions for peace are high, with Russia wanting an end to Western arms supplies to Ukraine, and Ukraine wanting Russian withdrawal from occupied territories. These remain formidable hurdles to a peace deal. For commodity markets, the grain deal means that raw material food prices have fallen back since spring/summer 2022, while European gas prices are now back to just around prewar levels. These commodity prices will likely still be sustained, as Russian sanctions will not be eased until a credible peace deal has been agreed.



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In Kazakhstan, the March elections saw power being retained by the ruling party (Amanat), which will boost President Tokayev. The elections themselves were part of the long road from a super strong president towards more of a balance between the president and parliament. Some criticism of the election process has been voiced with concern over vote manipulation. However, the result has largely been accepted locally and should not be a source of prolonged instability. Meanwhile, Tokayev continues to be lukewarm about the war in Ukraine and wants to ensure some perceived distance from Russia and President Putin's stance – though this will likely remain subtle rather than a hardline stance that could cause problems with Russia.

Elsewhere, no countries in the region saw a rating change, but the spillover of the Ukraine war remains evident. Moldova formed a new government in February, with the key priority being security rather than long-term economic developments. Concerns have grown about Russian inference in Moldova, with President Maia Sandu saying Russia has been plotting an overthrow of the government by foreign-based saboteurs. Tensions will remain, but with Russian forces tied up in Ukraine, the risks largely surround intermittent incidents. Elsewhere, Georgia's government withdrawal of the foreign agent's law in March has not healed domestic tensions, as the government has paused the swing towards the West and its values and still wanting to avoid upsetting Russia. This is in contrast to popular support for the EU in Georgia. Meanwhile, concerns over Russian interference in the North Kosovo/Serbia dispute have caused the EU to redouble efforts to ensure dialogue and de-escalation by both sides. However, the EU has not made any new promises on accession for either country into the EU, which remains a long-term goal and a potential fix for tensions. Finally, though Uzbekistan is holding a referendum next April 30th on a constitutional reform, uncertainties remain about the pace of economic reform in the country and the tilt towards more international openness. Moreover, despite the drift away from Russia, Uzbekistan and Kazakhstan are in talks with Russia about increased energy ties between the three countries and for exports to China.

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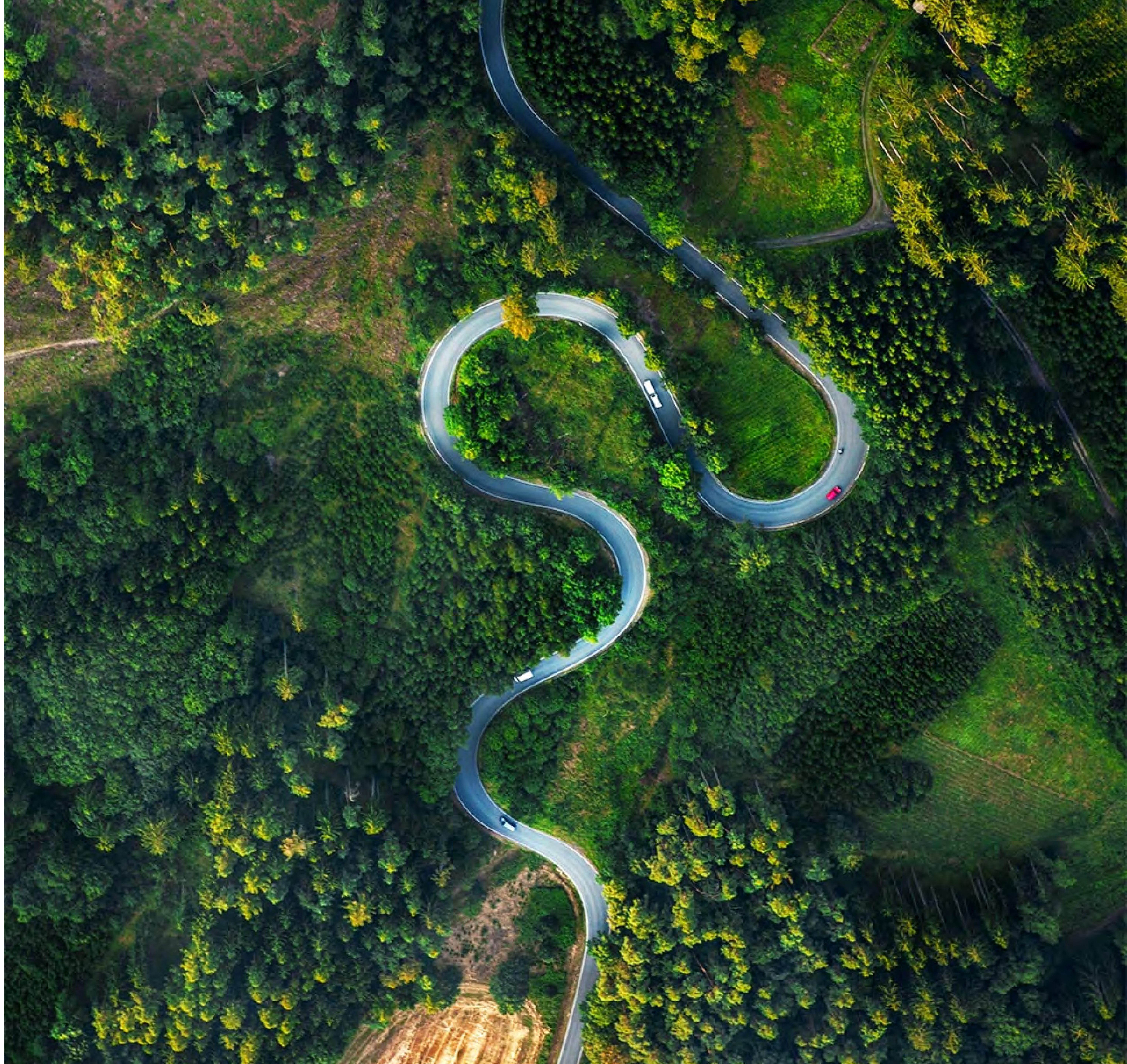
Latin America

Latin America

Latin America political risks has been kept mostly unchanged over the last few months, though some countries registered important events. In Brazil, after pro-Bolsonaro supporters invaded several government buildings on January 8th, opposition leaders have lost some ground as hundreds of protesters were arrested and face criminal charges against their actions. No new anti-government protests have been registered since then and Lula da Silva government has been able to put forward its agenda smoothly. Still, Lula faces a hostile Congress where opposition is relatively strong and some consensus is needed to pass legislation. The biggest test he faces is to pass the new fiscal framework, which we believe part of the opposition will support and that framework should be approved by both houses of Congress.



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There have been some clashes with the Brazilian Central Bank (BCB) President Roberto Campos Neto by several government members including Lula himself stating that interest rates are too high and the person to blame is the BCB President. However, due to the BCB independence bill, Campos Neto will stay in charge until December 2024. We see these clashes as a way of Lula's government putting the blame of low growth in 2023 on someone else.

Moving on to Mexico, the biggest news is that the Supreme Court has suspended the so-called "Plan B" of the electoral reform. The reform was an alternative of the "Plan A", which could not get the 2/3 needed to make constitutional amendments. Plan B was passed with a simple majority and was softer as it only changed ordinary laws. Still, the reform weakens the electoral organization by ending several state careers and making appointments on key posts of the electoral organization more political than technical. The Supreme Court will suspend the reform until the judges decide whether this reform is constitutional or not. The decision could take months to materialize but a final answer is likely to be decided this year as Mexico faces a general election in 2024, in which incumbent President Andres Manuel Lopez-Obrador will not participate as re-election of a sitting president is vetoed by the Constitution.

In Argentina, all eyes are on the general election in October. The major problem is that neither the opposition nor the ruling coalition has appointed their candidates. There is some consensus that incumbent President Alberto Fernandez has a low probability of winning and thus several names on the ruling coalition

are promoting themselves as the ideal candidate. In the opposition, former President Mauricio Macri has already stated that he will not participate in the election and there is still an open road for several candidates. The most likely scenario is that the two forces will wait until the Open Primary (PASO) in July to define their candidates. Due to the unstable macroeconomic environment, it is very likely that the opposition wins the election for President with whoever candidate they appoint and gains the majority in Congress.

Moving to the Andean region, after seeing strong protests in the aftermath of the imprisonment of Pedro Castillo, Peru has registered over 60 deaths in violent protests across the country. Protesters were demanding the immediate release of the President, who tried a state coup by closing the Congress and announcing an exception regime (similar to martial law) on television. In the recent weeks, the protests have cooled down and interim President Dina Boluarte is likely to stay in power until new elections are called. However, the situation is fluid and could change anytime. Congress has the power to quickly impeach the President and it is a scenario we could not discard in the short term.

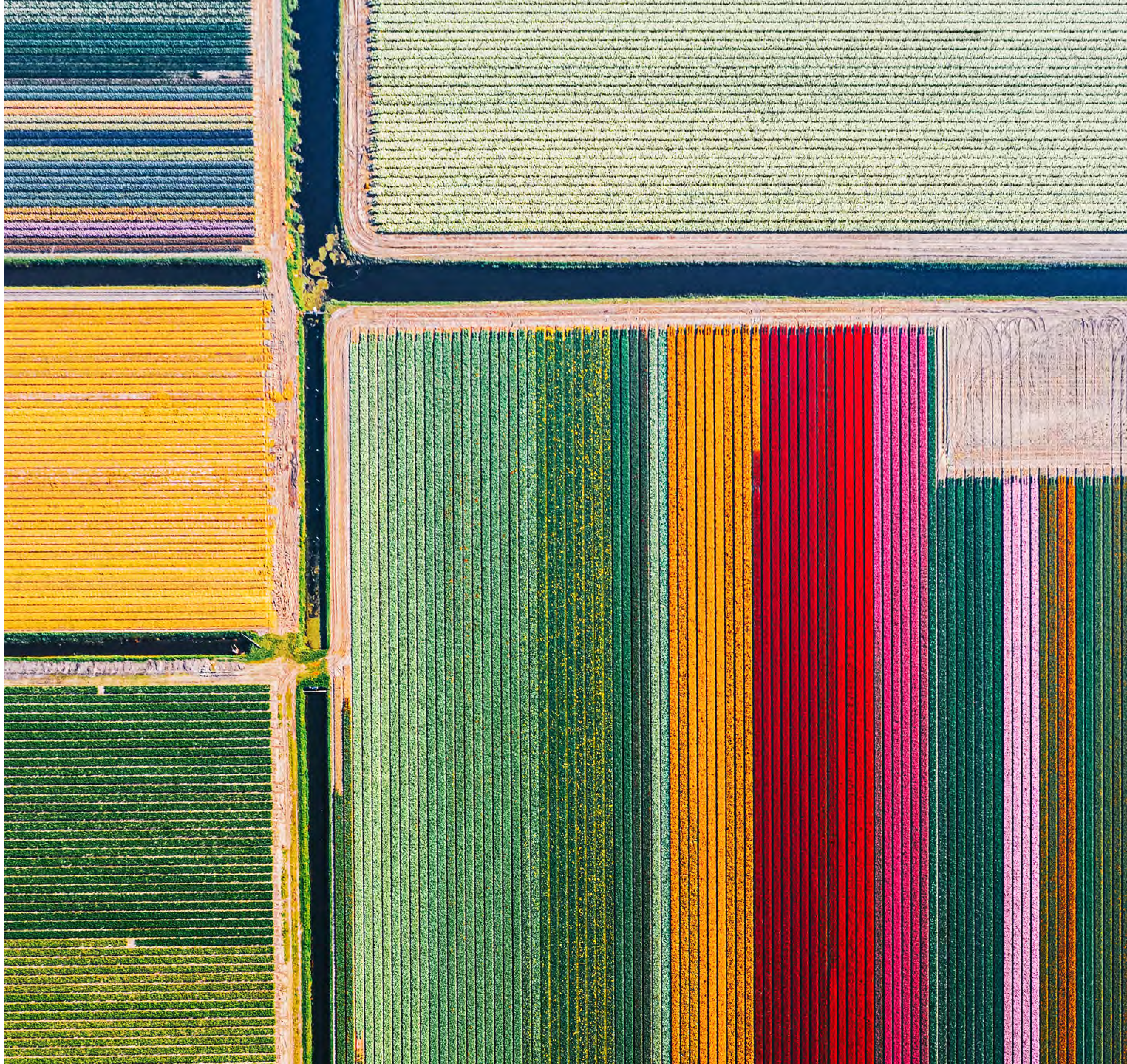
In Ecuador, the increasing wave of violence perpetuated by narco organizations has led President Guillermo Lasso to decree an exception regime in some cities in which the violence has escalated. In parallel, Guillermo Lasso is facing the second impeachment procedure of his government. The President is accused of corruption in the state oil company. Hearings in the Congress are scheduled to occur in the next few months and it is yet unclear whether Lasso will stay in charge of Ecuador after the procedures end in Congress.

In Colombia, President Gustavo Petro has faced his first drop in popularity, as the fiscal authority are investigating his son Nicolas Petro over alleged corruption cases. Petro has been able to approve an ambitious tax reform in Congress. However, due to his lack of popularity, and in the face of regional elections in October, it is very unlikely that Petro will be able to pass his ambitious Health Reform (universal access of health services for all Colombians).

Finally, in El Salvador, the exception regime (similar to martial law) approved by the legislative chamber has completed one year. The measure that suspends several individual rights was aimed at reducing the violence produced by the criminal organizations “Los Pandilleros”. Since its implementation, the official number of homicides has fallen, but human rights organizations have stated that around 60 persons were killed in the custody of the army and the police and the capacity of state organizations to investigate those deaths was reduced. President Nayib Bukele holds strong popularity in El Salvador and controls the legislative house. The exception regime is set to continue indefinitely.

3 The Middle East and North Africa (MENA)

The major development in the region: China brokered a deal for Iran and Saudi Arabia to re-establish relations, which has implications beyond the two countries. Foreign ministers have already met in Beijing in early April and Iran's President Raisi is planning a trip to Saudi Arabia. Saudi Arabia's motivation is to promote regional peace, which in turn will help foreign funding to the Vision 2030 mega projects. Additionally, Saudi Arabia is also motivated by not allowing a Russia-Iran-China axis to form. From Iran's standpoint, the agreement allows a greater focus on domestic issues, while also potentially mitigating the economic crisis by improving relations with Middle East countries and China.



Although no preconditions were made on Yemen, the hope is that the dramatically reduced level of fighting in the last year can be sustained and Iran's involvement could wane. Whether this will lead to peace talks remains uncertain, however. Iran has also appointed the first ambassador to the UAE for seven years, this points to a wider improvement in regional relations. Elsewhere, in March, Iran and Iraq also reached a security agreement that is ambiguous, but allows both sides to protect the common border. For Iran, this reduces the risk of Iraqi Kurds being involved in Iran affairs. Finally, Saudi Arabia and others are moving towards Iran's desires that Syria should be readmitted to the Arab League.

The obvious losers are the U.S. and West, that are less interested in the region and currently, much more focused on the Ukraine war. Given that the Ukraine war will likely continue, the U.S. and West could continue to play less of a role in the region. The U.S. did attack eastern Syria in retaliation for the death of a U.S. contractor, but this was an isolated development. The U.S. will also become domestically focused as the run-up to the 2024 presidential election gets underway. Russia will intermittently work with certain countries to extend its multi-year increase in geopolitical influence as well as cooperation with OPEC+, but the biggest opportunity is for China. Russia is overextended with the Ukraine war and cannot provide support for forward-looking Gulf countries aiming for an economic transformation over the next decade to ensure less dependence on fossil fuel exports. China's willingness to broker an Iran-Saudi agreement is largely for economic reasons, as China does not want a major military footprint in the region. China sees advantages in working with the region for energy security and export potential, as well as the soft power of geopolitical influence. How this develops with Middle East countries in the coming years will be tricky, as Chinese companies' experience in Africa shows that China wants control of projects and companies and this may not be acceptable in a number of countries. Meanwhile, the economic focus for China suggests they will not become involved in every conflict in the region but rather involvement will be tactical and driven by economic opportunity.

Elsewhere, the overall risk level remains very high in Iraq, Yemen, Syria and Libya. In Iraq, Prime Minister al Sudani is at the head of a weak government, with no signs of any momentum towards building out the non-oil sector or cracking down on corruption. Despite the weakness and last year's expectations that this government was a one-year stopgap, al Sudani and the coordination framework (CF) want to serve a four-year team and this could risk clashes with the opposition later this year and into 2024. In Libya, the tense political environment remains. Though the two opposing governments (the High Council of State (HSC) in Tripoli and the House of Representatives (HoR), based in the east) are undertaking talks, this is unlikely to lead to a unified election. Instead, the best that can be achieved is another attempt at a transitional executive authority, with representatives from both parliaments. At least, while talks are occurring, it does mean that the uneasy calm in Libya can continue, but this is not yet a road to long-term stability.

Meanwhile, in North Africa it is worth highlighting Tunisia. The arrest in February of Jaouhar Ben M'barek, a prominent opposition figure, shows that the crackdown from President Saied continues as he extends his political control. With still high debt levels, plus the global slowdown, this leaves Tunisia in a difficult economic position as foreign funds are apprehensive. Elsewhere, tension remains between Algeria and Morocco over the routing of the Nigeria-Europe gas pipeline through Morocco. Egypt has seen less dramatic developments than those of 2022. Then, when Egypt's financial difficulties were exposed by the spillover of the Ukraine war, an IMG package was followed by deposits from Saudi Arabia and Gulf deposits into Egypt's central bank, as well as pledges of major new investments. Saudi Arabia has signaled that future financial support will be conditional on reform, which in the current situation, Egypt would have to accept.

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Sub-Saharan Africa

Sub-Saharan Africa

In sub-Saharan Africa, politics is a crucial issue at the moment. In Nigeria, Bola Tinubu has been elected president, complementing the existing government led by the All Progressives Congress. Though the opposition has contested the result, we see the central scenario as being one of pressures ebbing rather than widespread civil unrest. Nevertheless, Mr. Tinubu has economic and domestic security challenges that will take time to address. The promise to curtail the fiscal deficit in the period up to 2027 needs to be contrasted with election promises for more expenditure. Higher taxes in the medium term are the way to achieve the long-term objective, but this will be politically unpopular. It will likely be more difficult to address domestic security issues, given longstanding divisions on ethnic and religious grounds. The low turnout in the presidential election shows that the government does not yet have widespread support.

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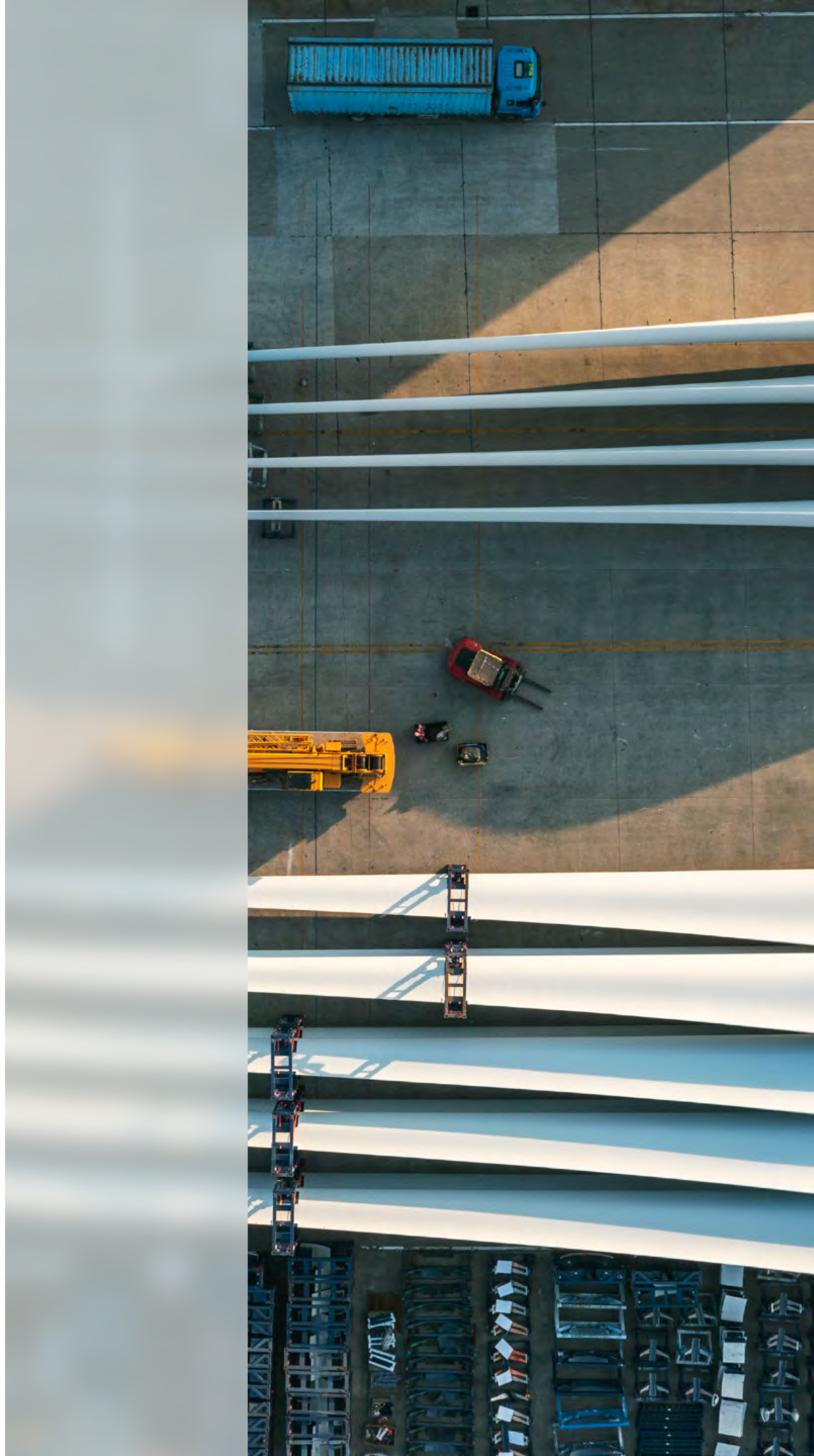
In Kenya, March has seen protests and arrests against President Ruto after the close 2022 presidential elections, which some contested (though they were not as bad as the protests after the 2007 and 2017 elections). However, the protests also reflect anger about high inflation and unemployment, which the new government has not done enough to address. While Kenya has a population dividend that will fuel healthy growth in the next few years, the government needs to act more on people concerns to avoid protests being repeated and slow economic development.

In Ethiopia, the cessation of hostilities in Tigray in November still leaves internal tensions in the country, with the U.S. secretary of state in March pressuring the government to undertake a transitional justice process after the war. However, the peace is holding and the U.S. and international agencies remain supportive of a shift towards reconstruction and resumption of good growth. Stability is also required to help get an IMF support package in place and an associated restructuring of foreign debt (mainly to China) under the G20 common framework (Paris Club/China and other creditors). Supplementary bilateral aid from the U.S. could be delayed however, as the U.S. is very keen on a transitional justice process.

Elsewhere, Ghana and Zambia remain in focus due to external debt problems. What happens in Ethiopia will likely have an impact on these countries. One question is whether Ethiopia will get better treatment that Chad did in November. This unlocked a modest IMF loan, which involved debt restructuring, but no cancellation of debt and thus delayed rather than reduced debt repayments.



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