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Emerging Markets Monitor

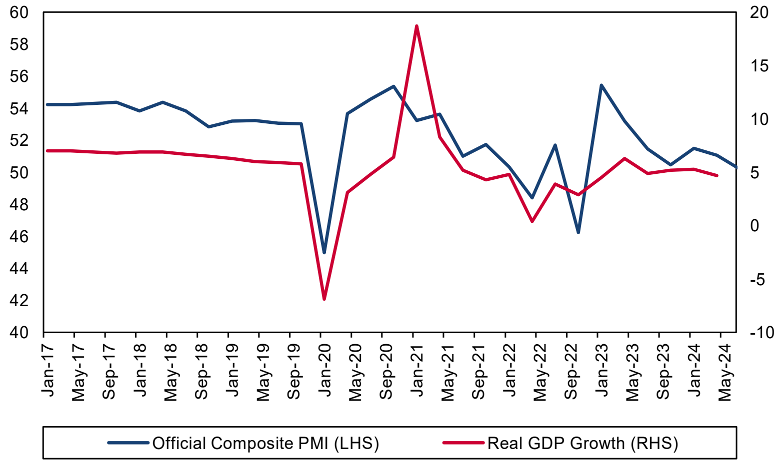
Mainland China: PMIs Point To Weak Q3 Start

Key View

- The official composite PMI for July suggests a further slowdown in Mainland China's economic momentum, after the second quarter's growth missed nearly all analyst forecasts.
- July PMI readings for all key sectors – manufacturing, construction and services – were lower than in June.
- Aggregate industrial profits continued to recover from a low base a year ago, with private firms performing better than state-owned enterprises.

Growth Momentum Likely Slowed Further

China (Mainland) – Official Composite PMI, quarterly ave & Real GDP, y-o-y % chg



Source: Haver, BMI

continued on page 2

Czech Republic: Weaker 2024 Growth

Czech GDP growth accelerated from 0.2% q-o-q in Q1 2024 to 0.3% in Q2 2024, according to flash estimates meeting our expectations but below consensus estimates for 0.4%.

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Saudi Arabia: Growth Will Turn Positive In 2024

Growth in Saudi Arabia will move from a contraction of 1.3% y-o-y in H1 2024 to positive growth of 2.7% y-o-y in H2 2024, driven by a rebound in the oil sector and despite a slowdown in the non-oil economy.

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Ethiopia: New IMF Programme

We expect that Ethiopia's new IMF programme, a four-year Extended Credit Facility arrangement agreed on July 29 and totalling USD3.4bn, will support macroeconomic stability.

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Mainland China's latest purchasing managers' index (PMI) data released on July 31 suggest that the economy has had a weak start to Q3 2024, after real GDP growth in Q2 missed nearly all analyst forecasts. The official composite PMI was 50.2 in July (June: 50.5), the lowest reading since December 2022 although it remained above the neutral mark of 50. This suggests a further slowdown in economic momentum. The PMI releases followed a Politburo meeting a day earlier, during which China's leaders stressed the importance of boosting consumption and expanding domestic demand. Efforts to lift spending have largely focused on incentives for households to trade-in their old appliances and cars for new ones. Despite that, growth in retail sales has remained lacklustre, with auto sales registering five consecutive months of y-o-y declines as of June.

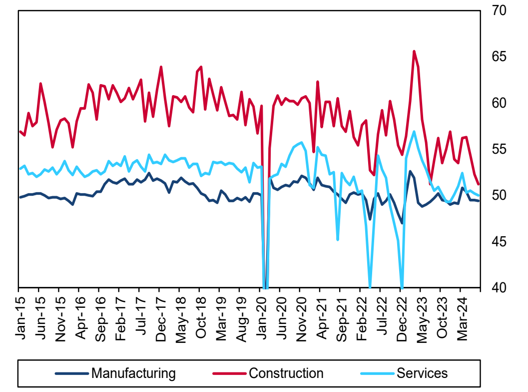
PMIs: The official manufacturing PMI was in contractionary territory for the third consecutive month in July with a reading of 49.4 (June: 49.5). The new orders sub-index also recorded its third consecutive contractionary reading of 49.3 for July (June: 49.5). The manufacturing output sub-index fell to 50.1 (June: 50.6), remaining just above the 50-point neutral mark. This paints a challenging outlook for industrial production, which was a key growth driver for China in H1. The official non-manufacturing PMI remained mildly expansionary with a reading of 50.2 for July (June: 50.5). Construction PMI was 51.2 (June: 52.3), the lowest reading since July 2023. Meanwhile, services PMI was neutral at 50.0 (June: 50.2), suggesting that retail sales growth is likely to remain subdued in the near term.

Industrial Profits: Aggregate industrial profits rose by 3.5% y-o-y over January-June 2024, remaining stable from 3.4% over January-May. Profits at state-owned firms inched up 0.3%, while private companies recorded a 6.8% increase. Industrial profits are recovering from a low base of comparison, following declines over 2022 and 2023. We expect profit growth to remain lacklustre in the coming months, as producer prices, which measure the price level when manufactured goods are sold for the first time, are likely to remain under pressure

Monetary Policy: The People's Bank of China (PBoC) made a surprise off-schedule move on July 25 to cut the one-year medium-term lending facility (MLF) rate by 20 basis points (bps) to 2.30%, just days after it lowered the seven-day reverse repurchase rate by 10bps to 1.70%. The back-to-back interest rate cuts suggest that authorities are intensifying efforts to support the economy. The MLF has become a less important liquidity management tool as the rate remains higher than interbank rates. As such, we expect the MLF rate to remain unchanged for the rest of 2024.

Lower PMI Readings For All Key Sectors

China (Mainland) – PMIs



Source: Haver, BMI

Latest Developments

On July 30, Bloomberg reported that electric vehicle (EV) brands from China captured a record 11.0% in market share in Europe in June 2024. China-based EV companies had been rushing to register their cars before July 5 to avoid additional tariffs by the EU. On July 29, Reuters reported that Italian Prime Minister Giorgia Meloni met China's President Xi Jinping in Beijing. The two leaders discussed the war in Ukraine, the crisis in the Middle East and growing tensions in the Indo-Pacific. On July 29, Global Times reported that 10 commercial banks in China simultaneously cut deposit rates. One of them, China CITIC Bank, announced a 5bps cut to its demand deposit rate to 0.15%, and a 10bps cut to the one-year deposit rate to 1.2%.

On July 25, CNBC reported that China will allocate CNY300.0bn in ultra-long special government bonds to expand an existing equipment trade-in and upgrade programme. The programme, which covers household appliances and cars to farm equipment and apartment elevators, aims to boost spending and investment amid weak confidence.

Israel: Wartime Conditions Pressure Public Finances In The Short Term

Key View

- We expect Israel's budget deficit to widen to 7.2% of GDP in 2024 and fall back to 4.6% in 2025.
- A rising bond yield differential with the US suggests that markets have some concerns regarding the public finance position but generally Israel has plenty of fiscal space.
- The debt ratio will remain elevated in the medium term compared to pre-Covid rates, peaking close to 70% of GDP but is not expected to pose too many market concerns.

The 2024 Fiscal Position: Multi-Decade Wide Deficit

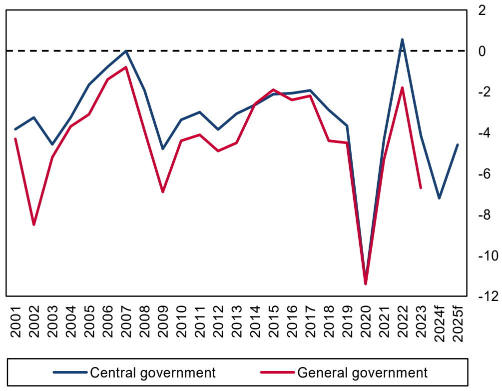
Our forecast suggests that **Israel will record a fiscal deficit of 7.2% of GDP in 2024,** which is marginally narrower than the previous estimate of 7.5%, partly because we now expect slightly stronger GDP growth. Nonetheless, the military outlays associated with the war in Gaza and the fighting on the northern front are putting a considerable strain on the public purse and official estimates suggest that over the 12 months to May 2024 the deficit amounted to 7.2% of GDP. On the assumption that military outlays are wound down in the second half of the year and as base year effects diminish, so the deficit-to-GDP ratio should not noticeably deteriorate. Nonetheless, excluding the Covid-induced deficit of 11.2% of GDP in 2020, the 2024 central government deficit ratio (which we forecast) will be the largest on record while the general government balance will rival that of 2002.

Looking more closely at the data for the first five months of 2024, although central government revenues were 2.0% higher than in the corresponding period of 2023, outlays were 35.0% higher. Expenditure on civilian projects was up 19.2% y-o-y, as a result of efforts to provide support for those impacted by the conflict. Higher military spending accounted for the bulk of the increase, rising by 120.8% y-o-y in the period January to May 2024. **When assessed relative to the revised 2024 budget plan, agreed in March, the figures do appear less worrying**. On a linear basis, revenues are slightly above target (year-to-date revenues are already at 44.5% of the annual target). Meanwhile, outlays are slightly below target at 42.8% of the annual figure, although military expenditure is currently on track to exceed budget but there is a presumption that this item will be scaled back in H2.

Our forecast suggests that the deficit may overshoot slightly, reaching ILS138bn in 2024 compared to a deficit of ILS129.2bn in the budget. This is largely because we assume that military outlays will not slow quite as rapidly as the government anticipates. However, this is a modest overshoot and the current spending and revenue trajectories suggest that risks to our 2024 deficit projection may be tilted towards a narrow deficit.

2024 Will Be A Bad Year For Government Finances

Israel – Government Balances As % of GDP



f = BMI forecast. Source: Haver, BMI

Debt On An Upward Trajectory

The expansion of government spending to finance the war will result in a significant increase in the debt-to-GDP ratio. On our forecast, the debt ratio will rise from 60.3% at the end of 2023 to 67.1% at end-2024 and will go slightly higher over the medium term. However, it remains well below rates recorded in the early-2000s when the debt ratio peaked at 85.1% in 2003 and is an indication of the extent to which Israel still has a considerable amount of fiscal space.

Rising Yields To Increase The Pressure

Over the course of 2024, **the yield differential between Israeli and US 10-year bonds has widened, which is a measure of the extent to which market concerns regarding Israel's financial position have intensified.** The yield differential has widened to over 70 basis points which is the widest since May 2014 and compares to virtually zero at the start of 2024, with 10-year Israeli bonds now yielding 5.00%. This will play on government finances and we expect that debt servicing costs will rise from 1.9% of GDP in 2023 to around 2.2% of GDP in 2024. Risks are tilted to the upside here, for any further widening of the risk premium will add to the fiscal pressures, although we believe that market concerns are somewhat overblown.

2025 And Beyond

On the assumption that the wartime pressures on public finances begin to abate, **we expect the deficit to narrow in 2025, to around 4.6% of GDP, and to continue narrowing in the medium term as an economic recovery gives a boost to revenues.** Nonetheless, the debt ratio will continue to rise and is predicted to rise towards 70% of GDP by 2028. In an effort to plug some of the fiscal gaps, the budget programme announced in March 2024 indicated that VAT would be raised from 17.0% to 18.0%, effective from January 2025, which is officially expected to raise additional revenue equivalent to 0.4% of GDP. A temporary additional tax on bank profits will also be in place until end-2025.

Even before the outbreak of war in 2023, the IMF suggested that there was scope for some increases in taxes via increases in low-bracket tax rates; reductions in tax incentives and curbs on certain tax exemptions, particularly for VAT. Given the more difficult fiscal circumstances in which Israel now finds itself, such measures may come back onto the policy agenda as the government seeks additional revenue to finance elevated military outlays compared to pre-October 2023 levels, especially as we expect higher-for-longer geopolitical risks in the region.

Risks To The Forecast

Fiscal forecasts are generally fraught with uncertainty but would appear to be balanced in the near term. As noted above, the current trajectory of revenue and spending, if continued, could result in a 2024 deficit which undershoots our forecast of 7.2% of GDP. However, it would not take much to knock it off course if, for example, interest rates rise by more than we expect or there are unanticipated military outlays. Medium-term risks are also generally balanced although should growth fail to recover to its pre-war path, Israel may struggle to generate the revenues required to reduce the deficit below 3% of GDP.

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BMI COCOA PRICE FORECAST (USD PER TONNE)	2023 Avg	Latest	2024 YTD	2024f	2025f	2026f	2027f	2028f
BMI Price Forecast	3,296	6,785	7,406	7,000	5,600	5,200	5,000	4,800
Bloomberg Consensus	-	-	-	7,225	6,000	5,500	5,200	5,100

f = BMI forecast. Note: ICE-listed second-month futures contracts; data correct as of July 19, 2024. Source: Bloomberg, BMI

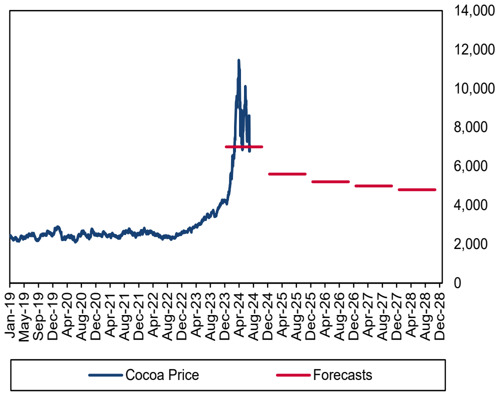
Cocoa: Outlook Raised As Supply-Side Concerns Exert Upward Pressure

Key View

- We are raising our 2024 average price forecast for ICE-listed second-month cocoa futures contracts from USD6,500 per tonne to USD7,000 per tonne.
- We forecast that 2023/24 will be the third consecutive season of deficit for the cocoa market, with consumption outpacing production by 0.40mn tonnes. We expect global production in 2023/24 to be 4.39mn tonnes, equivalent to a 12.1% y-o-y decrease, largely driven by unfavourable weather conditions in West Africa.
- With regards to consumption, we expect this to decrease by 4.5% y-o-y, down to 4.8mn tonnes in 2023/24 from 5.0mn tonnes in 2022/23. We believe that elevated prices will ultimately result in decreased demand, although we flag that this has remained relatively resilient to date.

Cocoa Prices To Remain Above Historical Averages

Global – ICE-Listed Second-Month Cocoa Futures, USD per tonne



Note: dashed red lines = BMI forecast. Source: Haver, BMI

We are raising our 2024 average price forecast for ICE-listed second-month cocoa futures contracts from USD6,500 per tonne to USD7,000 per tonne. We flag that there has been significant price movement in the cocoa futures market over the first half of 2024, with a sharp rally in prices up to mid-April followed by significant swings and market volatility. On July 19 2024, cocoa futures closed the session at USD6,785 per tonne, a 4.1% decrease from the day prior and equivalent to a 27.7% m-o-m decrease. At the same time, the closing price represents a 98.5% y-o-y increase and, on a year-to-date basis, prices have risen by 124.8% up to July 19. The latest closing price is also 40.8% lower than the all-time high reached of USD11,461 per tonne, reached on April 19 2024. After average monthly contract price increases for 17 consecutive months between November 2022 and April 2024, the average monthly price for cocoa futures dropped to USD7,860 per tonne in May from USD10,039 per tonne in April 2024. The average monthly price then increased once more in June to USD8,849 per tonne and in July-up-to July 19 was of USD7,749 per tonne.

As we had noted in our last price forecast, the cocoa futures market has been characterised by low liquidity and heightened uncertainty and instability, largely due to the elevated prices throughout H1 2024. In the year-to-date up to July 19, the average intra-day price volatility has been of 6.4%, significantly higher than the 1.8% in 2023. From the monthly average peak reached in May of 9.8%, this has since decreased to 7.9% in June and 7.3% in July, suggesting a possible transition away from a period of significant instability. According to the US CFTC's latest Commitment of Trader Reports, the net long position in cocoa futures and options was 23,351 on July 16 2024. Although this is a contraction from the trough reached on April 30 2024, it is still significantly lower than the first net long position of 2024 which was 62,942. Historically high prices have also deterred traders from purchasing beans, reflected in the open interest on July 18 being 58.7% lower than the 2024 high reached on February 12. This ultimately means that small volumes of trade can have a significant impact on prices, the reason behind the fluctuations over recent months. In the short term, we expect upward price momentum to diminish and prices to remain below the all-time highs reached in April 2024, we believe that supply-side concerns will maintain prices above historical averages.

We forecast that 2023/24 will be the third consecutive season of deficit for the cocoa market, with consumption outpacing production by 0.40mn tonnes. We expect global production in 2023/24 to be 4.39mn tonnes, equivalent to a 12.1% y-o-y decrease, largely driven by unfavourable weather conditions in West Africa. The now terminated El Niño event coupled with intense seasonal Harmattan winds weighed heavily on productivity in the region. Output in the two largest cocoa producers, Côte d'Ivoire and Ghana, will decrease significantly in 2023/24, by 20.6% y-o-y in the former and by 25.1% y-o-y in the latter. Decreased production has been the main factor driving cocoa prices throughout H1 2024 and we expect this to continue throughout H2 2024. For example, in mid-July, Bloomberg reported that the Ghanaian cocoa board is aiming to limit cocoa purchases for the 2024/25 seasons. Cocoa inventory data also points to supply-side pressures. As of July 19 2024, ICE-certified cocoa inventories in New York were down 9.5% m-o-m, 38.1% compared to six months prior and 43.6% y-o-y. The decreases were more significant for ICE-certified EU cocoa stockpiles which, as of July 18, 2024, were down 10.2% m-o-m, 40.6% compared to six months prior and 63.3% y-o-y. Cocoa inventories in Europe have been more significantly affected because most cocoa produced in West Africa is destined for the region, meaning that the supply concerns in Ghana and Côte d'Ivoire have had larger impact there.

In July 2024, reports of more favourable weather conditions in Ghana and Côte d'Ivoire resulted in optimism from cocoa farmers and contributed to prices decreasing. Although both the Ghanaian and Ivorian cocoa boards have expressed confidence in rebounding production in 2024/25, we remain cautious about the likelihood of this happening. The US Climate Prediction Center now forecasts that the transition to a La Niña weather pattern will occur between August and October 2024. We identify this as a risk to our production forecast as the pattern is tends to bring above-average precipitation to West Africa. This could be beneficial for cocoa production, but if the pattern were to be particularly intense it could result in flooding and increased spread of plant disease as happened in H1 2023. Therefore, we flag the development and relative strength of La Niña as a leading factor to monitor with regards to the 2024/25 cocoa season. Beyond this, we believe that the widespread incidence of the cocoa swollen shoot virus is also a concern for 2024/25.

With regards to consumption, we expect this to decrease by 4.5% y-o-y, down to 4.8mn tonnes in 2023/24 from 5.0mn tonnes in 2022/23. We believe that elevated prices will ultimately result in decreased demand, although we flag that this has remained relatively resilient to date. The latest data on global grindings from Q2 2024 indicates that these have increased by 2.0% from Q2 2023, while they had decreased 0.7% y-o-y in Q1 2024. While markets were forecasting decreases in demand as a result of upward pressure on cocoa prices throughout H1 2024, it appears that concerns about future shortages and the utilisation of last season's beans explains the continued demand. The resilience in processor demand has also been a factor keeping prices above historical averages. We continue to expect a slow-down in cocoa grindings, in line with forecasts by the International Cocoa Organisation and we will be monitoring the next data release for Q3 2024 for signs of market momentum dissipating. With regards to demand, we also note the bullish impact of the EU's Deforestation Regulation (EUDR), which came into force in June 2023 and will be applicable from January 2025. The law will prohibit the sale in the EU of covered commodities that are not deforestation-free. In 2023, 49.5% of total cocoa imports were destined to the EU, highlighting the relevance of this regulation for consumption patterns of the commodity.

As we have noted in a previous piece looking in detail at the potential effects of the EU's legislation, we expect the EUDR to create obstacles for cocoa exports. As the largest market for cocoa globally, we anticipate the regulation will have significant effects on production practices for cocoa. Concretely, the regulation requires due diligence statements to be provided and environmental credentials to be demonstrated to enter the EU market. The due diligence process will also relate to human rights and the rights of indigenous communities' and non-compliance with the regulation will be met with penalties including fines up to 4% of a company's annual turnover in the EU. Industry players and commodity-exporting countries have argued that the EUDR will create financial and technological burdens that will weigh most heavily on smallholder producers. Most cocoa is produced by smallholder farmers in West Africa so this is a particular concern in the region. Heightened administrative costs and worries that many producers will simply be unable to comply with the regulation represent downside risks to consumption. In 2023, 59.0% of West African cocoa was destined for the EU and cocoa from the region represented 58.2% of the EU's total imported cocoa. This is evidence of the potential for this regulation to significantly impact cocoa consumption globally.

Long-Term Outlook

Beyond 2023/24, we forecast that the global cocoa market will post a narrower deficit in 2024/25 before returning to a surplus thereafter, contingent on normal weather conditions. We expect cocoa prices to trend downwards through the medium term. We forecast that the average annual price of ICE-listed second-month cocoa futures will decline to USD5,600 per tonne in 2025 and will thereafter continue to ease through to 2028. We forecast that prices will remain above recent historical averages, in part due to the three consecutive years of deficit which will weigh on stocks. We also expect several long-term factors to weigh on structural production growth.

We have identified a number of structural issues negatively affecting cocoa productivity in West Africa. Cocoa production growth in the region has been largely driven by growth in area harvested rather than yields, resulting in the destruction of forests and protected areas. Not only is this unsustainable, as suitable land is a finite resource, but it is also at odds with the EUDR discussed above and initiatives by local governments such as Côte d'Ivoire's target to reach 20% of forest cover by 2030, up from 9% in 2022.

The predominance of smallholder farmers in cocoa cultivation is also a matter of concern, given that cocoa producers earn very little added value in the cocoa supply chain. This has resulted in decades of underinvestment in the sector, leading to ageing trees with lower yields and heightened vulnerability to weather fluctuations. Furthermore, the reliance of smallholder farmers on monocultures has decreased soil fertility and worsened both soil and tree health.

Another long-term production risk is the increasingly widespread presence of cocoa swollen shoot virus disease in West Africa. According to the Ghana Cocoa Board, disease coverage in the country has increased by 88% from 2017 to 2023 and accounts for 17% of loss in cocoa production annually. As there is no treatment to the disease other than cutting down trees, we flag this as having the potential to significantly weigh on production in the long term. Given current price strength, the implicit opportunity cost of cutting infected trees is high, which could see the disease spread further.

In addition, a desire to realise high prices could see the replacement of aged trees postponed insofar as cocoa trees require several years to progress from their initial planting to full capacity production. Finally, illegal mining is a particular concern in Ghana, threatening cocoa production as farmers venture into illegal gold mining because they expect greater returns. This decreases area harvested, damages soil and pollutes waterways, resulting in lower yields.

BMI VIETNAM CURRENCY FORECAST	2023	Spot	2024	2025
VND per USD, eop	23,866	25,295	25,000	23,500
VND per EUR, eop	25,732	27,481	27,175	26,085
Policy rate, %	4.50	4.50	4.50	4.50

Source: Bloomberg, BMI. Last updated: July 29 2024

VND: Unit To Gradually Appreciate Yet Risks Persist

Key View

- We maintain our view that the Vietnamese dong will trade sideways and start to slightly strengthen when the Fed begins to cut rates.
- Risks are balanced: there are depreciation risks from US rates staying higher for longer and potential policy instability in Vietnam, and the prospect of appreciation if a sharp US slowdown will result in more aggressive rate cuts.

Short-Term Outlook (three-to-six months)

We maintain our view that the Vietnamese dong will trade sideways and start to slightly strengthen when the US Federal Reserve (Fed) begins to cut rates, which we expect will occur in September 2024. We expect a rate of VND25,000/USD at the end of 2024, indicating a modest 1.7% appreciation from the current spot rate of VND25,428/USD.

Since our last forecast, we have made major changes to our outlook. On the one hand we have changed our US and Vietnamese monetary policy forecasts and on the other we forecast a wider current account surplus than previously expected. These factors together have allowed us to maintain our forecast.

Interest Differentials (Depreciation Pressure): Since our last forecast, we have revised our expectations for Fed rate cuts in 2024 from 100 basis points (bps) to 50bps, while also revising our expectation for the State Bank of Vietnam (SBV) to hold rates steady instead of cutting them by 25bps.

This results in a slight increase in the interest differential, which is likely to exert additional depreciation pressure on the Vietnamese dong.

Current Account (Appreciation Pressure): We recently revised up our GDP forecast for Vietnam, largely due to the recent increase in electronics exports amid the global silicon cycle recovery.

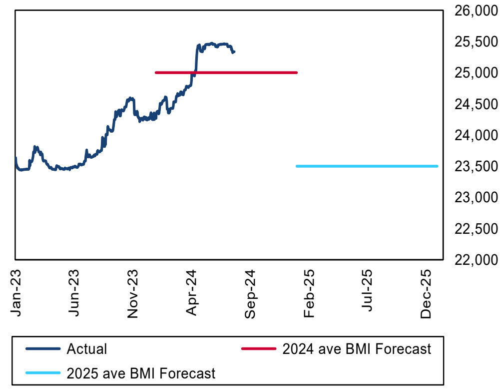
We expect this, along with growing inbound tourism and remittances, will further widen the current account surplus, causing appreciation pressure on the dong.

Long-Term Outlook (six-to-24 months)

We maintain our longer-term view that the Vietnamese dong will strengthen further as the Fed continues to ease monetary policy, while the SBV keeps its rate steady. Toward the end of 2025, we expect the exchange rate to appreciate by 6%, reaching VND23,500/USD by the end of 2025. This level matches early 2023, when Vietnamese interest rates were 40bps below those in the US, a differential we expect to see again by the end of 2025. As for the impact of a potential Trump presidency on the dong exchange rate, given its past pattern, we are tak-

Dong To Gradually Strengthen

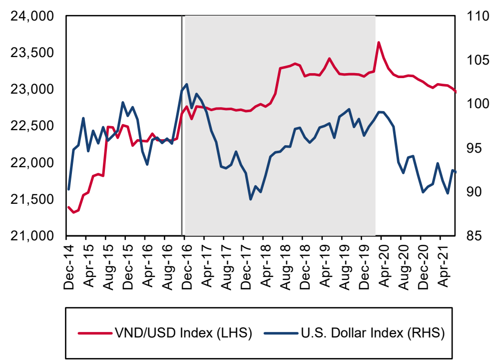
Exchange Rate, VND per USD



Source: Bloomberg, BMI

Dong Depreciated During Trump's First Term, Unlike Its Asian Peers

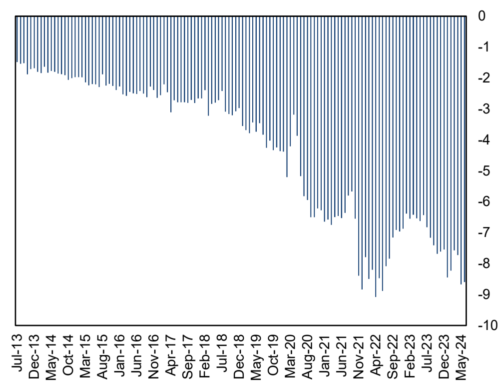
Exchange Rate, VND per USD Index & US Dollar Index



Note: Event line is when Trump was elected as president and shaded area is Trump's first term.
Source: Bloomberg, BMI

Vietnam's Increasing Influence In US Trade Deficit

US – Trade Deficit To Vietnam, USDmn



Source: United States Census Bureau, BMI ing a neutral stance for our forecast. During the last Trump presidency, the Vietnamese dong depreciated which was in contrast to regional peers whose currencies strengthened, due to actions by the SBV and factors unique to Vietnam.

One possible explanation is that while Asian currencies generally strengthened (against a weaker dollar) due to concerns about the expanding US fiscal deficit, Vietnam also felt this impact. However, accusations of an artificially weak dong offset the effect.

This scenario could happen again, with the dong still on the US Congressional 'monitoring list' due to Vietnam's significant trade surplus and Donald Trump's hardline stance on Vietnam's current account surplus.

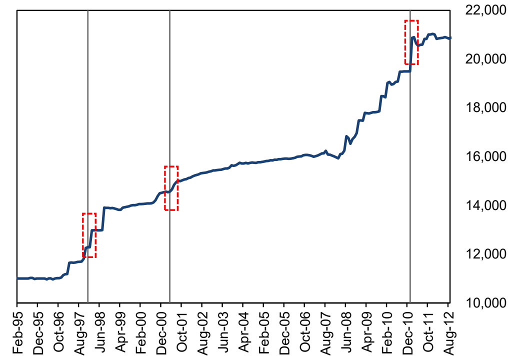
If Trump were to impose tariffs on Vietnamese imports, accusing Vietnam of keeping the dong weak, we believe the surplus could shrink, which could potentially weaken the dong further, creating a feedback effect and achieving the opposite of what was intended.

Risk To Outlook

Risks are balanced: depreciation risks arise from the case where US rates stay higher for longer and potential policy instability in Vietnam. In contrast, appreciation risks may arise due to significant weakening of the US economy which results in more rate cuts. Historically, leadership changes in Vietnam have led to a weakening of the dong for a period of a few months.

Paramount Leader Change In Vietnam Caused Depreciation In The Past

Exchange Rate, VND per USD



Note: Event lines show the change in the General Secretary. Source: Bloomberg, BMI

Following the recent passing of Nguyen Phu Trong, the initial reaction did not result in a weaker dong, but further instability could cause depreciation, as it did in the past.

Mainland China: Market Will Miss 2024 Growth Target

Key View

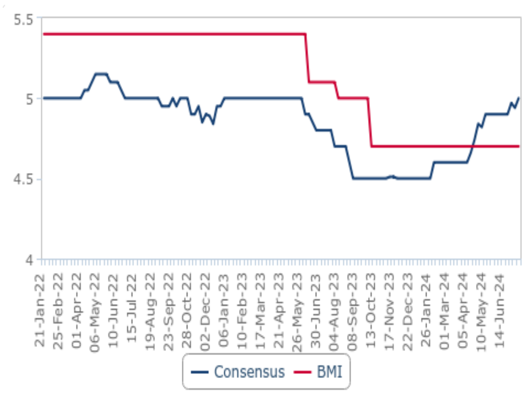
- Real GDP growth slowed to 4.7% in Q2 2024, vindicating our below-consensus 2024 growth forecast of 4.7%.
- We think the economy will slow further in the second half of the year, as the property downturn, pay cuts and tariffs imposed by the EU and US bite.
- These headwinds are set to persist in 2025 and we expect growth to slow further to 4.4%.

Real GDP growth fell visibly to 4.7% y-o-y in Q2 2024, from 5.3% the previous quarter, underperforming nearly all analyst forecasts (BMI: 5.0%, Bloomberg consensus: 5.3%). The lacklustre data vindicate our previous assessment that the outperformance in Q1 2024 was largely due to a favourable base in Q1 2023 rather than any real positive momentum in the economy. We have long held the view that the Mainland Chinese economy would slow to 4.7% growth in 2024. Our forecast now implies that growth will slow to around 4.5% in H2 2024. Between the ongoing downturn in the property sector and pay cuts affecting the most productive sectors of the economy, we think a further slowdown is very likely. **As such, we still expect the economy to miss the government's 'around 5.0%' growth target and maintain our 2024 growth forecast at 4.7% (Bloomberg consensus: 5.3%).**

The slowdown in Q2 was driven largely by the tertiary sector (roughly equivalent to the services sector), which decelerated to just 4.2% growth, from 5.0% in Q1, indicating continued weakness in private consumption. The secondary sector, which mostly has to do with manufacturing, slowed as well from 6.0% to 5.6%. The ongoing property downturn still shows little sign of reversing. Residential property transactions have fallen by 21.9% in the first six months of 2024. As a result, residential property prices have continued to fall. **As we have been arguing, the resulting negative wealth effects are likely to suppress household spending in 2024 and beyond.**

BMI Still Expects Mainland China To Miss Growth Target

China (Mainland) – 2024 Real GDP Forecasts, % chg



Source: Bloomberg, BMI

Consumers face another stiff headwind in the form of pay cuts. The aggressive pay cuts in the financial,tech and public sectors have persisted according to reports from Caixin. Part of that is due to the slowing economy. But much of it also has to do with President Xi Jinping's push for 'common prosperity' under which pay in the financial sector has been singled out as being 'excessive'. With the government mulling a pay cap for state-owned finance firms at CNY3.0mn per year, it appears that there are still more cuts to come. Retail sales volumes growth fell to just 1.8% y-o-y in June, the slowest since January 2024. **Besides the**

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direct impact on household spending capacity, the pay cuts mean they are more likely to fall behind on mortgage payments, which means an even deeper downturn in the property market and a further hit to consumer confidence, and so on.

With developers likely to hold back on real estate investment as a result, we think investment growth will at best remain at current weak levels – fixed asset investment growth has been sluggish at around 4% y-o-y, weighed down by private sector, and in particular the real estate sector.

While export growth rebounded from the 7.5% y-o-y contraction in Q1 2024 to expand by an average of 5.9% in Q2, we expect a slowdown ahead. We believe that the EU's additional tariffs on China-produced electric vehicles and US President Joe Biden's broader tariffs against China's green technology are one impediment. More importantly, we expect the US economy will slow over H2 2024. **Caught between sluggish domestic demand and challenging external demand, we think industrial output growth will slow further from 5.3% y-o-y in June, which already marked a material drop from January's peak of 7.0%.**

That said, government support should prevent a deeper slowdown – Beijing would not want to miss its 'around 5.0%' growth target by much, if at all.

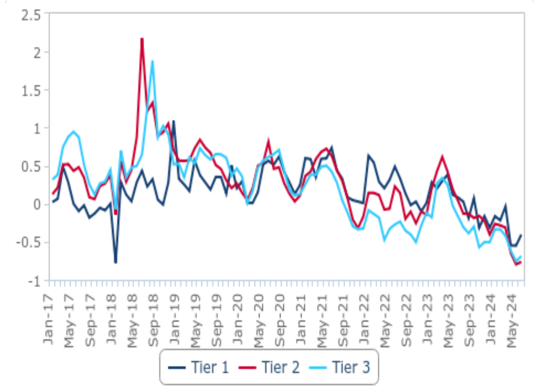
Ultimately, it has little room to manoeuvre and we do not expect 'flood-like' stimulus from Beijing to push growth back above 5.0%. Local authorities are struggling to raise revenue as land sales, which account for about 30% of their revenue have slumped. Fiscal revenue shrank by 4.1% y-o-y in January-May, the fastest rate of decline in more than a year.

There is room for the central government to issue more bonds to try and make up the shortfall, but we think it will be sparing in that regard after already committing to issue CNY-1trn in ultra long-term bonds in March 2024. Meanwhile, falling banking sector profitability means the People's Bank of China will be hard pressed to lower the medium-term lending facility rate much further.

As for 2025, we forecast a further slowdown to 4.4% real GDP growth. The property downturn has scope to worsen in the absence of additional stimulus measures. Coupled with a weak employment and wage outlook, it is hard to see how consumption will rebound significantly in 2025. Externally, we expect protectionism against China to pick up regardless of who wins the US presidential election in November 2024.

Property Downturn Still Under Way

China (Mainland) – House Prices, % m-o-m



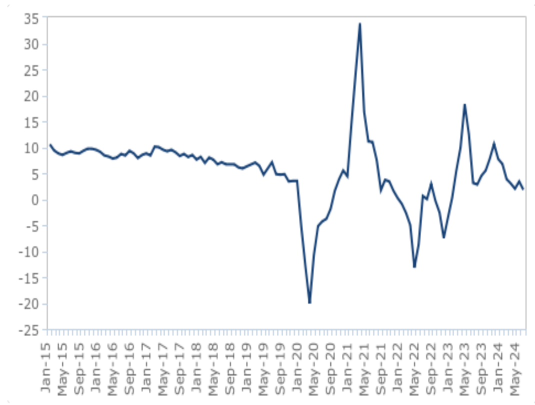
Source: Haver, BMI

Risks To Outlook

We see balanced risks to our forecasts given that we are already below consensus on our views, but we note that much will depend on the government's willingness to support the economy.

Consumer Spending Slump Has Further To Run

China (Mainland) – Y-O-Y Retail Sales Growth Less Inflation



Source: Haver, BMI

Additional stimulus could achieve the 5.0% growth target, but it will be challenging. EU tariffs might be reduced in November, but a second Trump term could lead to more aggressive tariff hikes.

2024-2025 GROWTH OUTLOOK

	2024f	2025f	Notes
Real GDP growth, %	4.7	4.4	Our 2024 forecast is below the consensus estimate of 5.3%.
Private consumption, pp contribution	1.5	1.6	The housing market downturn is likely to persist and weigh on private consumption through negative wealth effects. Aggressive pay cuts to lower 'excessive' pay in the financial and tech sectors will also weigh on household spending.
Government consumption, pp contribution	1.0	1.0	We expect relatively muted government support as policy constraints bind.
Fixed capital formation, pp contribution	1.2	1.5	The housing market downturn should also weigh on real estate investment. An expected increase in infrastructure investment is unlikely to prevent a further investment slowdown in 2024 and 2025.
Net exports, pp contribution	0.2	0.1	The exports recovery has probably played out fully. Slower global growth and tariff hikes will weigh on exports growth over the coming quarters. The silver lining is that the poor consumption outlook means slower imports growth as well, supporting the trade balance.

f = forecast. Source: BMI

Philippines: Credit Growth To Slow, But Banking Sector Stable

Key View

- We have revised our end-2024 credit growth forecast from 10.0% to 9.0% y-o-y on account of later and fewer cuts by the Bangko Sentral ng Pilipinas.
- Against the backdrop of high interest rates, asset quality will remain under pressure.
- However, financial risks remain well-contained as the banking system boasts robust capital buffers and loan provisions.

With the likelihood of fewer rate cuts in 2024, we have revised our end-2024 loan growth projection downwards from 10.0% to 9.0% y-o-y. While this is by no means a strong performance – well below the 2015-2019 average of 14.3% – it marks a slight improvement from 2023. What is notable is the deterioration in asset quality against the backdrop of restrictive financial conditions. Still, financial stability risks remain manageable, underpinned by robust capital buffers.

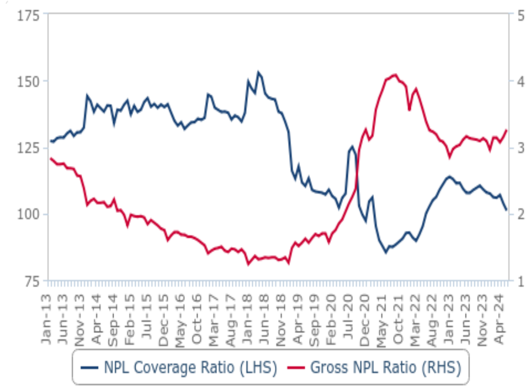
The impact of monetary tightening has been apparent in data for some time now. Credit growth typically averages double digits in the Philippines, which has hardly materialised in over a year. Admittedly, it reached 10.4% y-o-y in April, but a slowdown to 9.7% in May quickly ensued. Given that rate cuts are only likely in Q4, we think that this underperformance will persist for a while longer. We have recently adjusted our interest rate forecast following our change in view for the US Federal Reserve (Fed). We are now expecting the Bangko Sentral ng Pilipinas (BSP) to cut by 50 basis points, starting from October. A delay in monetary loosening means that any material gains in credit growth will likely only be felt in 2025.

For now, tight financial conditions will continue to weigh on asset quality. Non-performing loans (NPLs) have remained on a broad uptrend as high interest rates curtailed borrowers' repayment ability. NPLs rose from 2.85% in December 2022 to 3.26% in May 2024, coinciding with interest rates being at their highest in over a decade. Similarly, NPL coverage has taken a hit, dipping from 113.8% to 101.1% in the same period. Banks have probably drawn down on their provisions to make up for the losses in NPLs. If they had not done so, the figures for NPLs reported would have been much higher. The upside is that the current high interest rate environment will enable banks to strengthen their financial buffers. Net interest margins (NIM) have expanded to their highest levels in a decade, driven by the BSP's tightening measures. Consequently, banks' profitability metrics have significantly improved. Return on Equity (RoE) increased from 9.7% in Q2 2022 to 12.4% in Q1 2024 and Return on Assets (RoA) rose from 1.2% to 1.5% over the same period. Wider NIMs have so far offset the slowdown in credit growth. Enhanced profitability will allow banks to allocate more resources to buffers, safeguarding them from any potential negative shocks. Nevertheless, we believe financial stability risks remain manageable. The banking system is supported by robust capital buffers, with the capital adequacy ratio standing at a healthy 16.6% in Q1 2024, way above the 10.0% regulatory minimum.

The government's push for digitalisation will significantly enhance the operating environment for banks. Currently, the market is underbanked, with a credit-to-GDP ratio of approximately 48.3% in 2023, compared to the global average of around 144.8%, as reported by the World Bank. According to a 2021 financial inclusion survey by the central bank, an estimated 40% of Filipino adults are unbanked. To address this, the BSP has implemented several reforms aimed at increasing competition within traditional banking and fostering the growth of fintech alternatives.

NPLs On The Rise Despite Provisions Falling

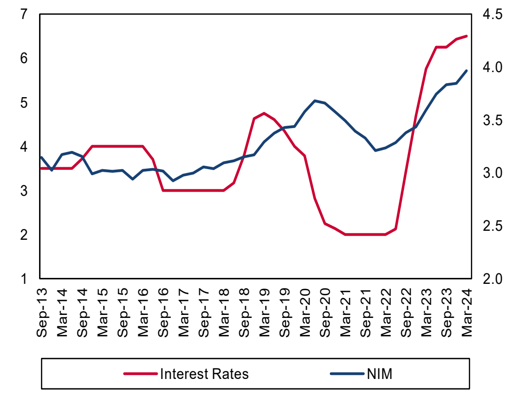
Philippines – NPL Coverage Ratio & Gross NPLs Ratio, %



Source: BSP, BMI

Widening NIMs In The Philippines...

Philippines – Interest Rates (LHS) & NIM (RHS), %

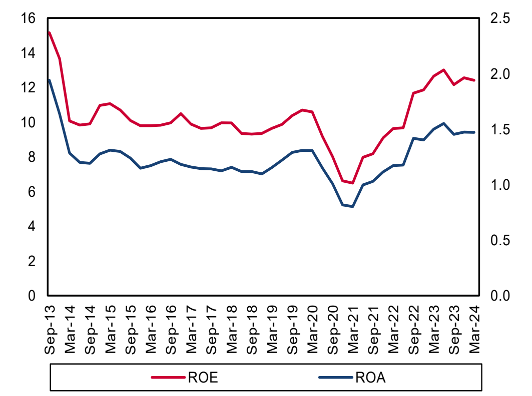


Source: BSP, BMI

Furthermore, the BSP has set an ambitious target to achieve 70% banking penetration in the Philippines by 2030. Greater financial inclusivity is expected to drive the development of the banking sector in the medium term.

... Will Provide A Boost To Profitability

Philippines – ROA (LHS) & ROE (RHS), %



Source: BSP, BMI

Venezuela: Uncertainty In Elections; Maduro Likely To Remain In Power

Key View

- We maintain our view that Venezuelan President Nicolás Maduro will remain in power following the contested July 28 2024 presidential election and the subsequent widespread accusations of voter fraud.
- We expect additional statements from international observers that will deem the elections undemocratic and unfair in response to the Maduro government's contention that he won 51.2% of the vote, while the opposition coalition found that Edmundo González won 67.0% of the vote.
- The US will likely reimpose sanctions following an official declaration on the outcome of the Venezuelan election, but it will wait to do so until it has additional proof.

We maintain our view that Venezuelan President Nicolás Maduro will remain in power following the contested presidential election that was held on July 28 2024 and was marred by widespread accusations of voter fraud. Maduro appears to have maintained enough internal, institutional support, namely from the military, as well as the judicial and legislative branches. Furthermore, Maduro has given no indication that he is willing to leave power voluntarily (via a 'golden bridge' offramp), despite the mounting pressure from civil society and foreign governments.

Since the electoral commission (CNE) released its results, key domestic developments include the following:

- The CNE certified the election results, indicating Maduro won with 51.2% of the vote, over 44.2% for González.
- The opposition coalition (PUD) leader, María Corina Machado, stated that Edmundo González, the candidate for the PUD, won 67% of the vote, while Maduro won 30% and that her party holds 81.2% of the voter tally sheets.
- Attorney General Tarek Saab stated that the delayed results were due to the CNE's system being impacted by a cyberattack from hackers in North Macedonia. Saab has announced a criminal investigation into Machado and other PUD leaders for this alleged hack.
- On July 29 2024, the Carter Center (one of the international observers) called on the CNE to publish the results. On July 30 2024, the Carter Center stated that it 'cannot verify or corroborate the results of the election declared by the [CNE]' and that the election 'cannot be considered democratic'.
- Thousands of Venezuelans have begun protesting in the streets. Reports indicate that 16 have been killed since protests began. There are reports of mass civilian detentions by state security forces with the attorney general having announced 749 arrests (including a leading member of the opposition, Freddy Superlano).

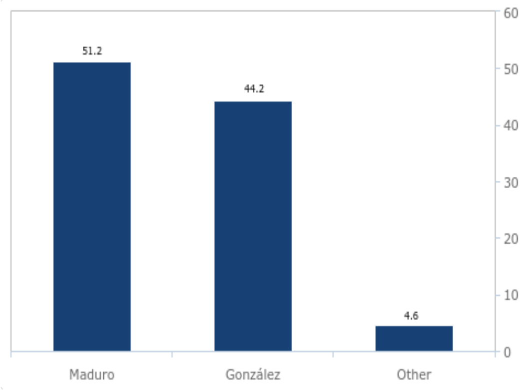
International Response

With the Maduro government having seemingly reneged on the terms of the Barbados Agreement so outrightly, we expect that additional sanctions will be implemented. However, this decision is likely to be delayed until additional electoral observers present their findings on the validity of the election results.

At the time of writing on July 31 2024, only a handful of countries have rejected the electoral outcome, while a majority of Western governments have instead voiced their concerns about the electoral process and called on the Maduro government to release full and transparent election results. Foreign allies of Venezuela (that share similar ideologies) have recognised the result.

Maduro-Controlled CNE Reports Maduro Won

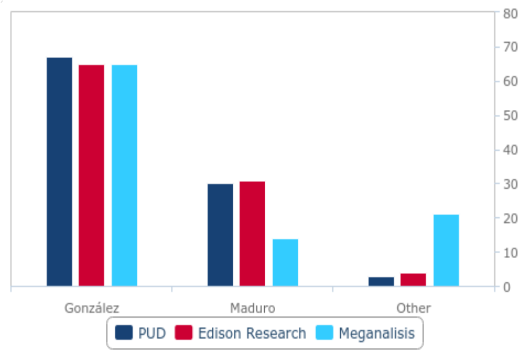
Venezuela – Electoral Results From CNE, %



Note: The CNE disclosed these results around 12:00am on July 29 2024 and reports an 80% turnout. Source: CNE, BMI

Non-Government-Affiliated Sources Match Opposition Tally

Venezuela – Election Polling & Opposition-Supplied Outcome

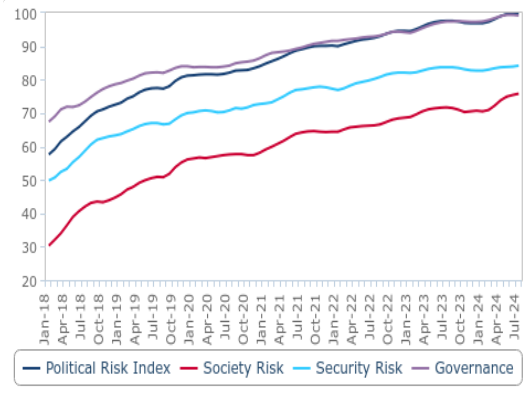


Note: PUD data from its website based on polling data it claims to have collected. Source: resultadosconvzla.com, Edison Research, Meganalisis

We expect that the future sanctions regime – once implemented – will be more punitive than the

High Risk Environment To Prevail

Venezuela – Political Risk Index



Note: Scores out of 100; 0 = lowest risk; 100 = highest risk. Source: BMI

current status quo given how openly fraudulent the election process has appeared. This will result in a worse economic situation than we had previously forecast, though it is very difficult to ascertain how substantial the impact will be without more details on a future sanctions regime.

At minimum, it seems as though licences granted to a handful of energy companies to resume operations in Venezuela may be revoked, depriving the government of much needed FX and increasing already substantial fiscal pressures. History suggests that Maduro will respond to this by using the central bank to finance the deficit, which will see inflationary pressures pick back up (from 51.4% y-o-y as of June 2024) and push the economy back into a painful recession. Against this backdrop, outward migration will likely pick up, deepening the downturn and creating problems for Venezuela's neighbours.

While the outlook is downbeat, we note that the smaller size of the economy relative to when sanctions were first introduced in the 2010s and the administration's experience with managing the economy with these constraints will act to somewhat reduce the overall impact.

Cuba: Economic Crisis Is Deepening

Key View

- We forecast that the Cuban economy will contract by 2.0% in 2024 and 1.5% in 2025; however, these forecasts are highly tentative given the lack of available data.
- The mass exodus from the island and what data is available suggest that the economy is drifting towards a major crisis.
- Our forecast has a large degree of uncertainty due to the lack of reliable data for the last 18 months.

Based on on-the-ground reporting from the last few months, Cuba is facing the worst economic crisis in decades, with the economy likely to contract by a minimum of 2.0% in 2024 and 1.5% in 2025, per government estimates. Earlier in 2024, Cuba had to request assistance from the UN World Food Programme to help with providing milk to children under seven, something that did not happen in the 1990s when Cuba experienced its worst economic contractions ever. Following the collapse of the Soviet Union and the end of Soviet economic support, Cuba saw three years of double-digit contraction (-10.7% in 1991, -11.5% in 1992 and -14.9% in 1993). This was later followed by economic liberalisation measures and a lukewarm recovery.

This current crisis is in some ways similar, as in the last few years, Cuba was severly impacted by the Covid-19 pandemic, the inability of Venezuela to offer assistance and the imposition of more severe sanctions by the former Trump administration. These sanctions have not been substantially eased by the Biden administration.

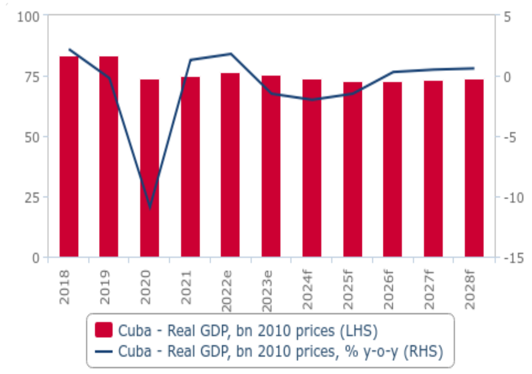
Cuba's long-standing structural issues linked to scarce forex reserves and state mismanagement have led to persistent electricity, fuel and food shortages. This has led to the largest exodus of migrants in decades. Currently, we are sceptical that Cuba's trajectory (without structural reforms) is sustainable in the absence of outside aid.

According to economist Carmelo Mesa-Lago, one of **Cuba's major issues through the years has been an inability to pay for its imports without outside aid either from the Soviet Union or Venezuela.** Cuba saw very slow economic growth throughout the late 2010s, when assistance from Venezuela was already slowing down; however, the crisis deepened as Cuba was not able to recover from the 10.9% Covid-related contraction that it saw in 2020.

As sanctions curbed activity in the tourism sector, we also saw a fall in net goods export. In 2021 and 2022, Cuba's GDP growth printed at just 1.3% and 1.8% respectively, with the economy

Deeper Forecast Revision As Cuba Continues To Face Multiple Headwinds

Cuba – Real GDP (2018-2028)



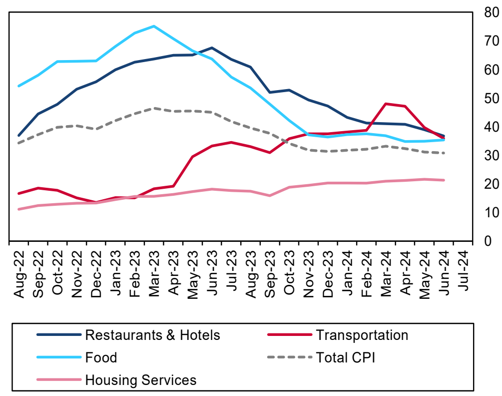
e/f = BMI estimate/forecast. Oficina Nacional de Estadísticas e Información, BMI

subsequently contracting by 1.0-2.0% in 2023, according to the government's press releases.

We have doubts about the accuracy of these numbers; however, the estimated 1.5% contraction in 2023 means that we believe that the official data will show a further 2.0% decline in 2025.

Government CPI Data Do Not Reflect Depth Of Crisis

Cuba – Consumer Price Index By Selected Categories, % y-o-y (2022-2024)



Source: Nacional de Estadísticas e Información, BMI

We also note that though the GDP growth contractions are smaller than what we saw in the early 1990s, Cuba also entered the Covid-19 pandemic at a much lower

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baseline in terms of standards of living compared with the relative prosperity that it saw in the late 1980s.

One of the reasons that we are sceptical about the official statistics relates to migration data that points to a mass exodus from the country. Government data show that outward migration out of Cuba has been steady since 2016; however, it significantly increased in 2021 and 2022, with the population shrinking in those years by 6.1% and 2.1% respectively. Although we do not have clear 2023 data, numbers from the US Custom and Border Patrol as well as independent reporting indicate that between 10.0% and 17.0% of the population likely left the island over the last two to three years.

The impact from these trends on private consumption was likely exacerbated in 2023 by the government's decision to lift subsidies covering gasoline amid a ballooning fiscal deficit (some news outlets put it at around 18% of GDP earlier in 2024). The government has instead increased enforcement of price controls and clamped down on private businesses (government restrictions on operating private enterprises were lifted in 2021). **These government measures will only lead to more shortages and higher prices on the parallel market, which will cause a further collapse in private consumption.**

Reflecting loose compliance with price controls, the government's inflation data does not capture how much purchasing power has weakened. Cuba's parallel exchange rate (as tracked by the outlet El Toque) hovered around CUP330/USD in July 2024, compared with CUP190/USD in May 2023, which indicates purchasing power of citizens fell by more than the 30.0% headline consumer price inflation growth reported by the government.

According to our estimates, net exports in Cuba are down significantly. Prior to the Covid-19 pandemic, one of the sources of hard currency in addition to remittances was the tourism industry, which, according to media sources, accounted for as much as 10% of GDP prior to the pandemic. The tourism sector has not yet recovered, and has instead come under further pressure since late 2023, which has exacerbated forex shortage issues.

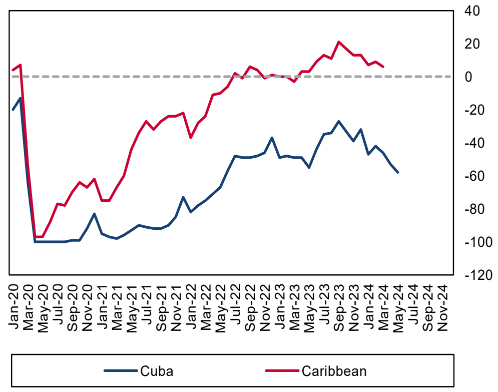
Goods imports fell by nearly 60% y-o-y in 2023, according to Trade Map data. This is not surprising considering the hard currency shortages mentioned previously. Exports were likewise down, as Cuba's output and production of manufactured goods continue to be negatively impacted by power outages as well as other interruptions.

All indications suggest that this downward trend will continue this year and through to 2025. While imports fell across categories, exports decreased in specific categories, notably nickel, zinc and lead exports, chemical products and mineral fuels.

Although there are risks to our forecast due to data integrity issues, the economy is clearly in a very challenging position. With the government reluctant to make substantial structural reforms, avoiding a liberalisation of the economy and clamping down on private enterprises, we expect the economic crisis to only worsen in the absence of outside aid from old allies such as Russia and Venezuela.

Tourism Industry Never Recovered

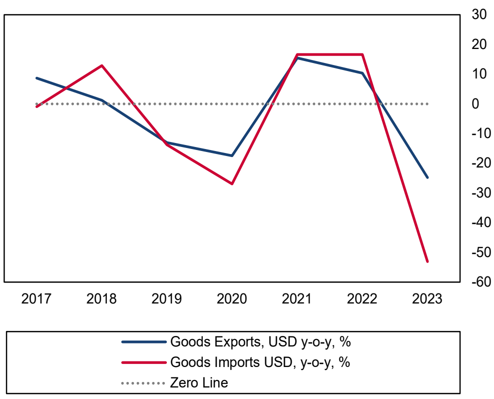
Caribbean – Regional Average Arrivals Compared With Cuba (2020-2024)



Note: Arrivals are compared with a baseline percentage in 2019. Source: UNWTO, BMI

Both Goods Exports And Imports Collapsed In 2023

Cuba – Goods Exports & Imports, % chg y-o-y (2017-2023)



Source: Trade Map, BMI

In the short term, this means more economic pain. If the crisis deepens over the next couple of quarters, we may see the emergence of major protests, which will force the government to take action.

CUBA GDP GROWTH FORECAST

	2022e	2023e	2024f	2025f
Real GDP, % chg	1.8	-1.5	-2	-1.5
Private consumption, pp	1.2	-1.6	-1.1	-1.2
Government consumption, pp	0.6	-0.8	-0.4	-0.4
Gross fixed capital formation, pp	-0.6	-0.4	-0.5	-0.3
Net exports, pp	0.8	-4.2	-0.1	0.4

e/f = BMI estimate/forecast. Source: Oficina Nacional de Estadísticas e Información, BMI

Czech Republic: Weaker 2024 Growth Following Historical Data Revision

Key View

- Czech GDP growth accelerated from 0.2% q-o-q in Q1 2024 to 0.3% in Q2 2024, according to flash estimates meeting our expectations but below consensus estimates for 0.4%.
- We are, nonetheless, revising our full-year growth forecasts for 2024 from 1.6% to 1.1% and for 2025 from 2.5% to 2.9% following sweeping revisions to historical annual data.
- We continue to foresee a modest upswing in household consumption as the main driver of growth in 2024, though headwinds from a weak external backdrop remain the main limitation on growth.

Czech GDP growth accelerated from 0.2% q-o-q in Q1 2024 to 0.3% in Q2 2024, according to flash estimates meeting our expectations but below consensus estimates for 0.4%. We are, nonetheless, revising our full-year growth forecasts for 2024 from 1.6% to 1.1% and for 2025 from 2.5% to 2.9% following sweeping revisions to historical annual data.

Revisions made to domestic economic activity through to 1995 have put the Czech economy on a slightly stronger footing than was previously understood, with the economy now shown to have been 2.2% larger in 2023 than previously.

Importantly, the Czech economy is now 1.2% larger in real terms than its pre-Covid level in 2019, compared to earlier estimates suggesting that the economy was 0.1% smaller. In this context, revisions to our forecasts have been largely mechanical, as our trajectory for near-term economic growth remains largely unchanged.

Flash estimates for Q2 2024 largely confirmed our expectations for a nascent recovery in household spending. Though missing a detailed component breakdown, the Czech Statistical Office (CZSO) confirmed that increasing domestic demand with private consumption in particular driving an increase in quarterly GDP. This offset negative contributions from net trade – likely a result of weakness in the Czech Republic's key trade partners including Germany where GDP contracted 0.1% in the same quarter.

Private consumption will be among the most important drivers adding 0.9pp to growth in 2024 and 1.0pp in 2025. The recovery in consumption follows the sharp 2.8% contraction experienced in 2023, which subtracted 1.3pp from growth. A sharp recovery in real incomes in 2024 has driven an improvement in Czech consumer confidence, which reached a low of -29.6 in November 2023 and has since recovered to -10 in June 2024.

This has precipitated the recovery in spending as implied by retail sales volumes, where growth has improved since the start of the year. Real incomes will benefit in particular from the slowdown in inflation, which has fallen to 2.0% y-o-y in June from its end-2023 rate of 6.9%, while nominal wage growth remains upbeat.

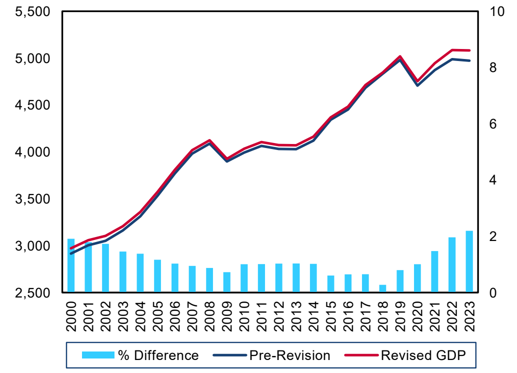
While the gradual recovery in domestic demand should weigh on net trade, a low base following the 0.9% contraction in imports in 2023 will keep the contribution from net trade positive.

Despite a weak external backdrop, we thus expect net trade to add 1.3pp to growth in 2024. This is less than the 3.0pp in 2023 as concerns about a lack of demand from the Czech Republic's most important trading partners in the eurozone, such as Germany, which accounts for 32.8% of total merchandise exports, will limit the export boost to growth.

We note that the relatively higher share of final manufacturing production will insulate the economy more than its peers in the CEE (such as Poland and Hungary) that rely more on intermediate goods production.

Revisions Imply Stronger Than Expected Footing For Czech Economy

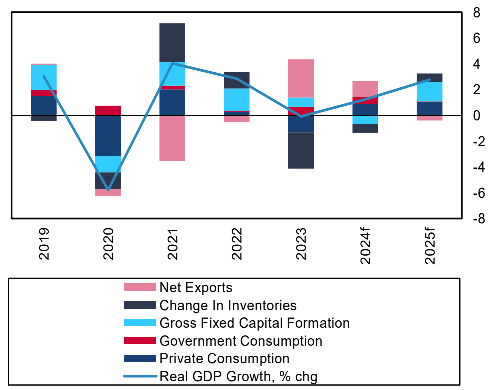
Czech Republic – Real GDP, CZKbn



Source: Eurostat, BMI

Private Consumption Remains...

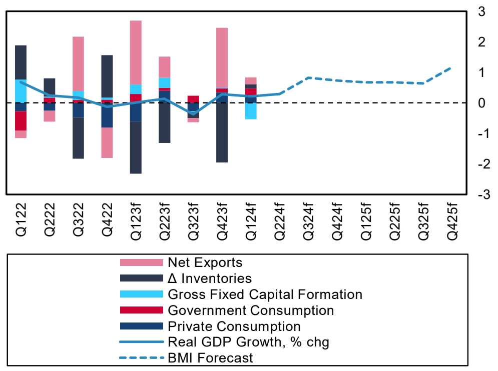
Czech Republic – Real GDP Growth, % chg, & Component Contributions, pp



f = BMI forecast. Source: Haver, BMI

... Key Driver Of Growth Recovery

Czech Republic – Quarterly Real GDP Growth, % chg q-o-q, & Component Contributions, pp



f = BMI forecast. Source: Haver, BMI

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Export growth will remain below its 2015-2019 pre-Covid average of 4.4% in 2024 as we forecast growth of 3.3%. On a quarter-on-quarter basis we expect export growth to accelerate from H2 2024 onwards.

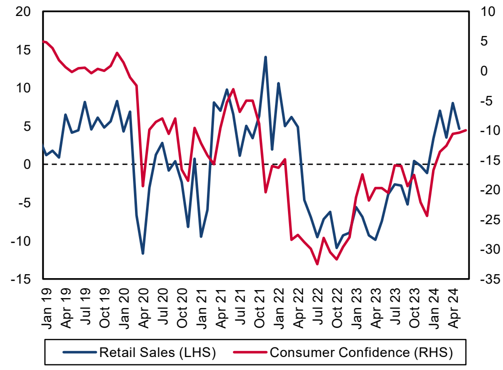
The investment outlook, meanwhile, remains significantly more constrained. Tighter lending conditions, as well as a pullback in government support as part of its 2023 austerity package, is likely to continue act as a headwind to investment growth. In 2023, the government removed around CZK55bn in subsidies for business and commerce, reducing incentives to invest. Meanwhile, we do not expect the Czech National Bank's current easing cycle to stimulate demand in capital expenditures until later in 2024 and in 2025, given the large lags in monetary policy transmission to the real economy. Manufacturers have also been hesitant to rebuild inventories as a result of the uncertain domestic and continental outlook, which has led to an unwinding in recent quarters. This has been reflected by weakness in industry, where output has remained weak over the last 12 months, while the manufacturing PMI extended its 11-month streak of contractionary (sub-50) readings in June.

Risks To Outlook

Risks to our forecasts are tilted to the downside. We remain highly concerned about the external backdrop, particularly

Recovery In Real Incomes To Boost Consumption

Czech Republic – Retail Volumes Growth, % chg y-o-y, & Consumer Confidence, balance of responses



Source: Haver, BMI

following the unexpected 0.1% q-o-q contraction in German GDP growth in Q2 2024.

An acceleration in exports growth in H2 2024 remains core to our view for a gradual improvement in Czech Republic's growth. However, a decline in sentiment indicators in Germany does not bode well for German activity, with the possibility of further underwhelming growth rising.

Serbia: EU Deal To Provide Opportunities For Both Sides

Please Note: *BMI is enhancing its risk analysis with a new scoring system following its acquisition of GeoQuant, a market-leading provider of political risk data. From March 27 2024, risk scores are inverted: zero now represents the lowest risk and 100 represents the highest risk. This allows for clearer, industry-standard assessments. For further details, please refer to our updated methodology document.*

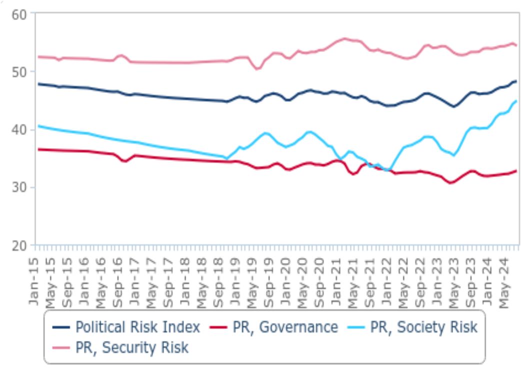
Key View

- We believe that a new agreement between Serbia and the EU marks a renewal of the economic relations between the parties at a time when geopolitical tensions are acute. That said, we do not believe that the agreement will make a significant difference to Serbia's political trajectory.
- We believe that the agreement will – in time – create new opportunities for development by boosting Serbia's foreign investment and its export market, particularly in its minerals industry.
- For the EU, the agreement marks a step forward in its attempt to diversify its resource supply chains.

On July 19, the EU and Serbia signed a Memorandum of Understanding (MoU) to launch a Strategic Partnership on sustainable raw material production, battery value chains, and electric vehicles. **Although the political deal will unlock new areas of cooperation between Serbia and the EU, it will not have a transformative effect on Serbian foreign policy.** The agreement is the precursor to a more comprehensive roadmap to put the partnership into practice. Cooperation will be focused on five areas. Particularly important are a series of related agreements also signed on July 19 that will grant the EU

Security Risks Drive Political Risk Up As Serbia Sits Between Russia And The West

Serbia – Political Risk & Components



Note: 100 = highest risk, 0 = lowest risk. Source: BMI

and European car makers exclusive access to Serbian lithium as well as paving the way for the construction of one of the largest lithium mines in Europe.

We believe that this agreement marks a renewal of Serbia's economic relations with the EU at a time when geopolitical tensions between the two parties are heightened. The EU has been critical of Serbia's pro-Russian foreign policy stance. For instance, the EU's 2023 enlargement criticised Serbia for not aligning with European foreign policy, including sanctions against Russia.

Until recently, EU member states have been supporting Kosovo's application for Council of Europe (an extra-EU human rights body) membership, which is also a source of tension between Serbia and the bloc. Therefore, the cooperation agreement, which builds on the existing Stabilisation and Association Agreement between Serbia and the EU as well as being a part of the bloc's Western Balkan Strategy shows a renewed commitment by both parties to work together on strategic investments.

That said, we do not believe that the agreement will make a significant difference to Serbia's political trajectory. Serbia has long pursued a multi-vector foreign policy that seeks the country's economic future with the EU but views Russia as the guarantor of its security. This reliance on Russia is largely tied to painful memories of NATO's intervention in the Kosovo War in 1999.

We view the agreement as firmly in the economic pillar of Serbia's foreign policy, having no regard to security policy. The agreement is focussed on generating supply chain opportunities and economic development possibilities for the EU and Serbia respectively. With Serbian President Aleksandar Vučić's grip on power remaining firm, we ultimately do not think that the agreement will do much to bring Serbia's security policy into the Western fold.

Additionally, the deal is highly controversial and sparked significant protests in 2021 and 2022. In particular, the construction of the lithium mine has caused public outrage.

The project was initially cancelled in January 2022 and opponents continue to raise concerns about the environmental impact of large-scale mining in Serbia.

Activists highlight weaknesses in Serbia's legislative and regulatory framework, which could indeed lead to unsustainable mining practices.

Serbians also point out that most of the benefits will flow to EU citizens. Serbia's own prospect of joining the EU remains scant and the country will be faced with most of the pollution problems associated with resource extraction.

Despite these concerns the political establishment of Serbia forged ahead with its plans after securing a further legislative mandate in December 2023. We suspect that this will see social risks rising in Serbia over the medium term, especially if environmentalists' fears come true.

On the economic front, we believe that the agreement will – in time – create new opportunities for development by boosting foreign investment and Serbia's export market, particularly in its minerals industry. Mined by Rio Tinto, a British-Australian firm, the exceptionally pure 'Jadarite' lithium (named after its origin in the Jadar region) will likely bring around EUR6bn in new investments (according to German Chancellor Olaf Scholz) and allow Serbia to play a key role in Europe's green transition. This will likely enhance the Serbian minerals markets as a source of resources for Europe. However, we do note that significant potential for misuse of investment funding could blunt the positive economic impact of the project. This is particularly true because, under the EU agreement, President Vučić will personally oversee development of the mine.

For the EU, the agreement marks a step forward in its attempt to diversify its resource supply chains. It is part of a wider drive by the EU to tap more markets to satisfy its resource demand.

The Critical Raw Materials Act, concluded in April 2024, seeks to lower the risk to EU supply chains by limiting the share of EU imports provided by any one country. According to the EU Commission, 97% of lithium used in the EU currently comes from Mainland China and it has been seeking alternative sources for the critical material in the Green Transition.

Therefore, EU is looking past some of the geopolitical questions around a collaboration with Serbia to secure its supply of lithium and place its green transition on a more diversified, less China-dependent footing. Our Metals & Mining team has covered the European Lithium Outlook in great detail and notes significant headwinds to Europe's lithium capacity.

EU-SERBIA AGREEMENT: AREAS OF COOPERATION

Area of Cooperation	Notes
Development of value chains for raw materials, batteries, and electric vehicles	Promotion of cooperation between EU and Serbian industrial actors as well as other stakeholders. Establishing a project pipeline with special focus on electric vehicles.
Research and innovation (R&I)	In conjunction with the existing cooperation under the EU Horizon Europe R&I programme and other schemes. Sharing of knowledge and technologies related to sustainable exploration, extraction, processing, and recycling of secondary raw materials.
Application of high environmental, social, and governance standards	Mutual consultation and exchange of information on relevant policies and initiatives along the entire value chains, including through the application of increased due diligence and traceability for the battery value chain.
Mobilisation of financial and investment instruments	In support of partnership projects through Invest EU, the Western Balkans Investment Framework and a Single Project Pipeline in Serbia as well as under the European Raw Materials Alliance and European Battery Alliance.
Skills development for high-quality jobs in raw materials and battery sectors	Includes participation of Serbian organisations in European Battery and upcoming Raw Materials Academies, including possible Serbian contribution with dedicated programmes and internships.

Source: European Commission, BMI

Lithuania: Growth Outlook Continues To Improve

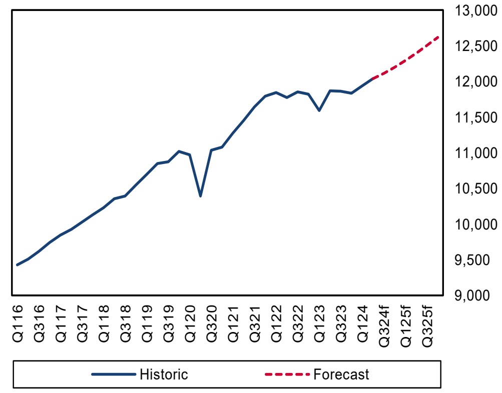
Key View

- We have revised up our real GDP growth forecast for Lithuania in 2024 to 2.4% and to 3.2% in 2025, from 2.0% and 3.1% respectively.
- The revision was driven by a better-than-expected growth turnout in H1 2024, with Q2 2024 surprising to the upside as real GDP grew by 0.9% q-o-q, stronger than our forecast of 0.5% q-o-q.
- Lithuanian growth will primarily be driven by consumption and investment, while external demand is taking longer to recover amid a still soft global backdrop.

Growth in Q2 2024 surprised to the upside. Flash estimates from the State Data Agency of Lithuania show that the economy grew by 0.9% q-o-q in Q2 2024 unchanged from upwardly revised figures in Q1 2024, but stronger our forecast of 0.5%. The expenditure release of the growth print is not yet available, but the press release of the State Data Agency highlights that the largest positive influence on the change in GDP was made by construction and manufacturing activities, with year-on-year activity rates expanding by 1.4%, decelerating from 3.0% in Q1 2024. Taken together, Lithuania's real GDP in H1 2024 increased by 2.2% y-o-y, and since we expect the economy to pick-up further momentum in the second half of the year, we have revised up our full-year growth forecast from 2.0% to 2.4%. Our forecast for 2025 now sits at 3.2%, up slightly from 3.1% before.

Economic Recovery...

Lithuania – Real GDP, EURmn



f = BMI forecast. Source: Eurostat, BMI

Domestic Demand To Power Recovery

Lithuania's economic recovery through H2 2024 will remain driven by domestic demand. In Q1 2024, household consumption surpassed its peak before the surge in inflation and robust retail sales growth (3.5% y-o-y in Q2 2024) and tame inflation (0.8% y-o-y in Q2 2024) suggests that consumer spending remained lively in Q2 2024. Looking ahead, additional monetary easing by the European Central Bank (ECB) – with another 50 basis points (bps) worth of cuts in H2 2024 to complement the 25bps reduction in June – will ease household debt servicing costs and support purchasing power. The brightening outlook for the Lithuanian consumer is reflected in confidence survey's, which tough easing somewhat from a multi-year high in June, remain elevated and crucially optimistic about the next 12 months.

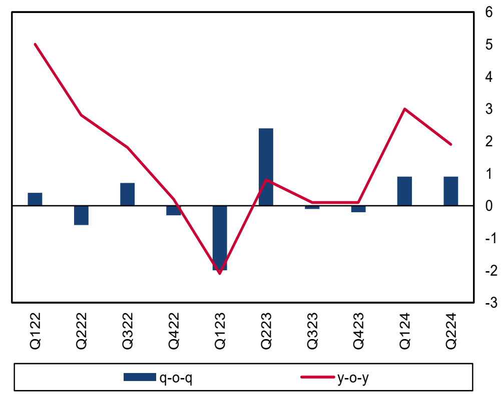
Domestic demand will also receive significant tailwinds from buoyant investment activity. Tough dipping somewhat in Q1 2024, Lithuania's investment-to-GDP ratio in Q4 2023 reached its highest level since the global financial crisis. This is indeed a positive development, especially as capacity utilisation in Q1 2024 stood well below its all-time high (70.7% to 78.8%), which suggests to us that Lithuanian business continue to invest despite a challenging economic backdrop.

Much of the investment increase going forward (we forecast an average of 4.3% in 2024, from 3.3% in Q1 2024) will be fuelled by an increase in EU funds, in particular from the Recovery and Resilience Facility (RRF), from which Lithuania can draw a maximum of EUR3.9bn (7.9% of GDP in 2019). With 35.2% of that amount paid out thus far, the largest amount of inflows are planned for this and next year – a major tailwind for fixed investment in the quarters ahead.

External conditions are turning more supportive, but demand will only pick-up more substantially in 2025. Though he eurozone's composite Purchasing Managers' Index (PMI) remained in expansion in Q2 2024, prior to positing negative readings through the majority of Q1 2024, the first month of Q3 2024 got off to a weak start, easing to 50.1 in July, from 50.9 in June. With the EU economies receiving around 60% of Lithuania's exports, it comes as little surprise that export order book levels remain well below their 10-year average and that export expectations have deteriorated from April to July. Therefore, we only expect external demand to pick-up more significantly through 2025 by when global monetary conditions will have eased further.

... Running Its Course

Lithuania – Real GDP Growth, %



Source: Eurostat, BMI

Risks To Outlook

Risks to Lithuania's growth outlook remain balanced. On the upside, domestic demand, propelled by household consumption and fixed investment may well grow at an even stronger clip than we currently anticipate, especially in light of pent-up demand built up over the past few years. On the downside, external demand could take longer to recover, bearing in mind the ongoing weakness of Germany's manufacturing economy. Less-than-expected policy rate cuts could also act as a headwind, keeping monetary and financing conditions tighter for longer.

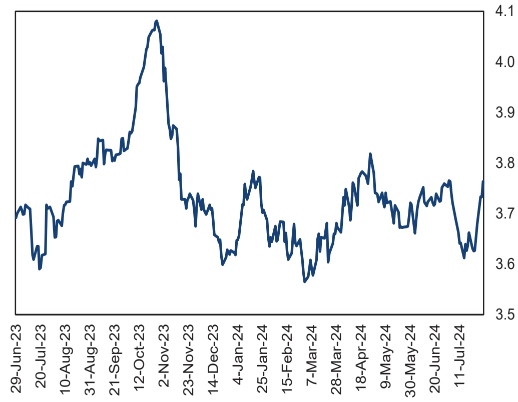
MENA: Political Update – Triple Attacks Increase Risk Of Regional War

Key View

- We believe that Israel's targeting of Hezbollah's second in command in Beirut suburbs and the killing of Hamas's political leader Ismail Haniyeh in Tehran increase the risk of a full-scale/wider war in the Middle East.
- This is because the two events will trigger a coordinated or individual retaliation from Iran, Hezbollah and other groups in the 'Axis of Resistance' that could equally either signal a de-escalation in the tensions or lead to a broader war.
- We believe that the killing of Haniyeh will complicate the ceasefire negotiations as Hamas will become more averse to reach an agreement with Israel.

Geopolitical Risks Weighing On Shekel And Rial

Israel – ILS per USD



Source: Haver, Bonbast, BMI

On the night of July 30/31 2024, three main events happened in the Middle East and North Africa:

1. Israel retaliated against the Majdal Shams attack, targeting Fouad Shukr, reportedly Hezbollah's second in command, in an attack on a Beirut suburb that killed another four civilians and injured more than 70.
2. The US targeted the Popular Mobilisation Forces (PMF) in Jurf al Sakhar in Iraq's Babil province, killing more than four PMF members. This is likely to deter the PMF's attacks on US assets, which have resumed over the past week after a long pause since February 2024.
3. A missile targeted and killed Hamas's political leader Ismail Haniyeh in Tehran. While no one has yet to claim the attack, it is widely attributed to Israel.

We believe that the three events significantly increase geopolitical risks in MENA, especially given that Iran and the 'Axis of Resistance' will most likely retaliate against Israel. Israel's retaliation against Hezbollah was more forceful than we had expected, and we believe that it crosses Hezbollah's presumed 'red line', as it targeted Beirut and resulted in civilian casualties.

Haniyeh's death was on Iranian soil, and the Supreme Leader Ali Khamenei sent a similar threat of retaliation when Israel targeted the Iranian diplomatic complex in Syria on April 1 2024, which resulted in Iran launching its first direct attack on Israel. Haniyeh's death not only serves to neutralise Hamas leadership, but also to send a strong message to Iran's new president on his inauguration day. We think that Iran and its 'Axis of Resistance' will retaliate to re-establish deterrence, which was compromised following the dual assassinations.

We are of the opinion that the risk of a full-scale war between Israel and Hezbollah/Iran has increased to 50.0% from 20.0% previously. An all-out war will imply the involvement of all 'Axis of Resistance' members and Iran, cause significant loss of life and bring about immense destruction to both Israel and Lebanon.

Iran and the 'Axis of Resistance' can choose to conduct separate or coordinated retaliatory measures. Under coordinated measures, Iran, Hezbollah, Iran-backed groups in Syria and Iraq, and the Houthis in Yemen would join forces to launch an attack against Israel and possibly US assets in the region. A coordinated response would further stretch Israel's military capabilities, especially considering that when Iran launched a direct attack on Israel in April 2024, the latter required the assistance of the US, UK, France and other forces to intercept it.

Meanwhile, a separate attack would involve a direct attack by Iran and individual members of the 'Axis of Resistance' against Israel, but not necessarily at the same time. We think that Iran's response will be more forceful and assertive than in April (ie, we do not think that it will be telegraphed).

Similarly, we think that Hezbollah will likely launch attacks on sensitive targets that it previously identified in the hudhud videos (Kiryah in Tel Aviv or the Ramat David Air Base).

In either case, the outcome is binary: either signalling a de-escalation or an escalation towards a regional war. We continue to believe that there is scope for diplomacy to avert an outright war in the Midde East and North Africa region at this stage.

However, in an escalatory tit-for-tat exchange, the situation can quickly spiral out of control. The situation in the region is still evolving, and we are closely monitoring it, especially as Hezbollah has yet to release a statement to confirm Fouad Shukr's death.

We suspect that Israel and the US may have coordinated the attacks on the night of July 30/31 2024. The US could have potentially supported Israel's retaliation against Hezbollah, given the profile of the target (he was involved in the killing of US Marine Corps in Lebanon in 1983 and had a USD5.0mn bounty by the US government). It appears that the US timed its attacks on Iran-backed armed groups in Iraq for the same night, possibly to deter the group from planning a coordinated response against the US/Israel.

The triple attacks will likely undermine the US-Iran indirect communication and efforts to contain regional tensions since October 7 2023. The US is reportedly moving ships closer to the Mediterranean coast to establish deterrence, and in the worst-case scenario plan the evacuation of US citizens from the region. In case of a wider war, we believe that the US would provide all necessary support to Israel and play a defensive role in intercepting missiles and drones.

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In terms of ongoing negotiations over a ceasefire in Gaza, we think that the prospect of an agreement has become extremely low. Haniyeh was leading the negotiations on Hamas's side, and his death will make Hamas more averse to offer concessions, especially as he was more flexible than the military commanders in Gaza.

This contrasts with Israel, which might be now more willing to offer compromises to reach a ceasefire after securing two important wins: eliminating Hamas' top political leader and Hezbollah's second in command.

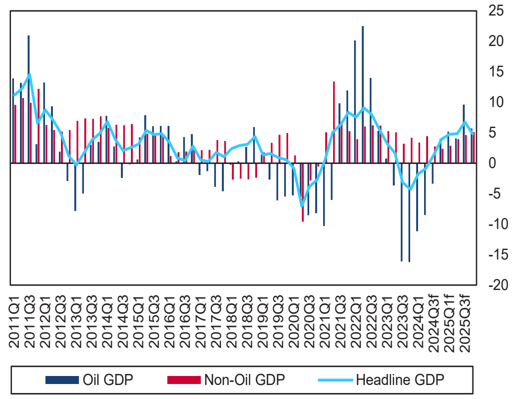
We believe that further delays in the ceasefire and the return of remaining hostages will increase domestic tensions in Israel and deepen polarisation.

Reflecting the increased risk in both Iran and Israel, their respective currencies have weakened. The Israeli shekel has lost 2.2% since July 29 2024, of which 1.0% was on July 31, and is currently trading at ILS3.76/USD.

The Iranian rial on the parallel market lost 2.9% since July 29 2024, of which 1.2% was on July 31, and has reached IRR602,500/USD at the time of writing.

Headline Growth Back To Positive Territory In H2 2024

Saudi Arabia – Quarterly GDP, % y-o-y



f = BMI forecast. Source: Gastat, BMI

Furthermore, we note that Brent crude oil price is up more than 2.0% on July 31 2024, and has exceeded USD80.0 per barrel at the time of writing, reflecting higher geopolitical risk.

Saudi Arabia: Growth Will Turn Positive In 2024 And Accelerate In 2025

Key View

- Growth in Saudi Arabia will move from a contraction of 1.3% y-o-y in H1 2024 to positive growth of 2.7% y-o-y in H2 2024, driven by a rebound in the oil sector and despite a slowdown in the non-oil economy.
- The oil sector will return to positive growth in Q4 2024 following the expiration of OPEC+ cuts, while the non-oil economy will face headwinds due to tight financial conditions in H2 2024.
- In 2025, growth will sharply accelerate to 5.3% due to a recovery in oil production and significant interest rate cuts, supporting both the oil and non-oil sectors.

We forecast Saudi Arabia's growth will flip to positive territory in H2 2024 and come in at 2.7% y-o-y after a contraction in H1 2024 of 1.3% y-o-y. On July 31 2024, Saudi Arabia's General Authority for Statistics Gastat released the kingdom's Q2 2024 GDP print, which showed a contraction of 0.4% y-o-y (slightly sharper than our expectation of 0.3% y-o-y).

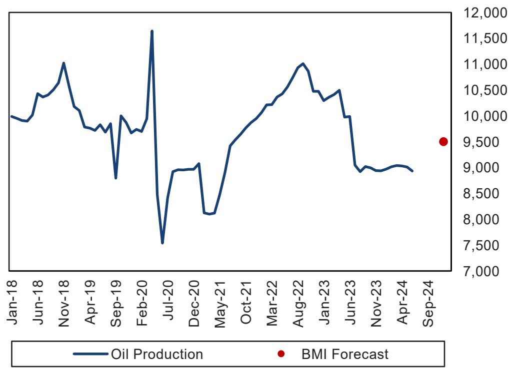
This was largely due to a sharp contraction of 8.5% y-o-y in the oil sector, but contrasted with an acceleration in growth in the non-oil economy from 3.4% y-o-y in Q1 2024 to 4.4% y-o-y in Q2 2024.

While our expectations for headline growth to turn positive in H2 2024 hinge on a rebound in growth in the Oil & Gas sector due to a normalisation of production and favourable base effects, this will be partially offset by a slowdown in non-oil activity as financial conditions remain tight. We expect that growth in the non-oil economy will slow from 3.9% y-o-y in H1 2024 to 2.6% y-o-y in H2 2024. This will nonetheless still exceed the 2015-2019 pre-Covid-19 average non-oil growth rate of 2.1%.

A gradual return of oil production in Q4 2024 will support the Oil & Gas sector. Our Oil & Gas team expects that oil production in Saudi Arabia will start rising gradually in Q4 2024 as the extension of the existing OPEC+ cuts to Q3 2024 expires.

Rebound In Oil Production Will Support Oil Sector

Saudi Arabia – Oil Production, thousand b/d



Source: OPEC, BMI

This will see growth in the oil sector, which accounted for around 29% of GDP in Q2, return to positive territory, which will support headline growth. Overall, we expect that the Oil & Gas sector will grow by 0.3% y-o-y in H2 2024, compared to a significant contraction of 9.8% y-o-y in H1 2024.

Despite an acceleration in growth in Q2 2024, we expect that the non-oil economy will face headwinds in H2 2024, which will mainly be due to tight financial conditions.

Despite the strong print, however, the non-oil economy is starting to experience further pressure on domestic consumption.

Point of sale transactions in June 2024 slowed to 1.8% y-o-y, which is the softest growth print since May 2020, when point of sales transactions contracted. After accounting for inflation, which came in at 1.5% y-o-y in June 2024, we believe that the print would represent only 0.3% y-o-y growth.

While consumer lending turned positive after contracting in Q4 2023, growth remains slow at 1.9% y-o-y in Q2 2024. This is largely due to tight financial conditions which have significantly increased the cost of credit. We expect that financial conditions will remain tight in H2 2024, with only 50 basis points (bps) worth of policy rate cuts in Q4 2024.

While we expect that momentum will remain relatively resilient due to elevated oil prices, we still expect some deceleration as financial conditions remain tight.

We think that elevated oil prices will provide some financing for Government Related Entities (GREs) to continue funding diversification efforts in line with Vision 2030, which will also have some positive spillovers on the private sector. However, rate sensitive sectors like construction will still face headwinds due to elevated interest rates.

Cement deliveries, which is indicative of construction activity, have remained subdued since the start of the tightening cycle in Saudi Arabia. This is despite a strong government-led investment drive.

In 2025, we expect that growth will accelerate sharply to 5.3%. This is largely because of a recovery in oil production, which our Oil & Gas team expects will grow by 6.2% compared to a 4.9% contraction in 2024. Similarly, interest rate cuts will provide a significant tailwind to the non-oil economy, especially as energy prices remain elevated, which would support diversification efforts.

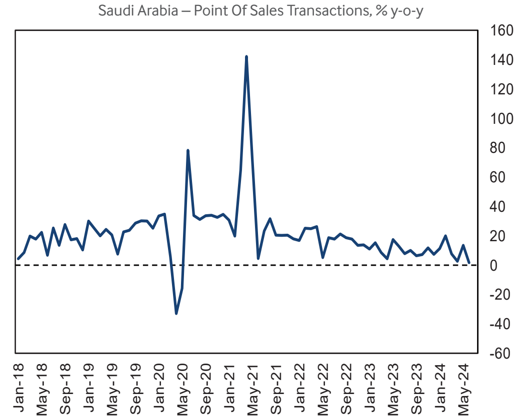
We expect that Saudi Arabia's Central Bank will follow the US Fed and cut its policy rate by 200 bps in 2025. While our Oil & Gas team expects that the average price of Brent oil will dip to USD82.0 per barrel (/bbl) in 2025 from USD85.0/bbl in 2024, it will remain elevated relative to historical averages and provide financing for GREs to continue investing in diversification efforts in line with Vision 2030.

We also think that this investment drive will intensify in 2025 as the authorities seek to meet some of the mid-term Vision Realisation Program deadlines which are set for the year.

Risks to our forecast are mixed. On the upside, a significant escalation of tensions in the region in relation to the Israel-Hamas war could lead to a significant spike in energy prices, which would possibly see OPEC+ members, including Saudi Arabia, be more willing to increase oil production and provide more financing for GREs to invest in the kingdom. However, it is important to note that such escalation would delay Vision 2030 goals, especially in relation to the development of Saudi Arabia's tourism sector.

Point Of Sale Transactions Growth Is Slowing

Saudi Arabia – Point Of Sales Transactions, % y-o-y



Source: SCB, BMI

On the downside, we believe that a more significant slump in energy prices, possibly due to a sharper-than-expected global economic slowdown, could delay a rebound in oil production and dampen headline growth for Saudi Arabia in Q4 2024 and 2025. This would also reduce financing available for GREs and dampen investment in the kingdom.

This will see growth in the Oil & Gas sector, which will support headline growth. The Oil & Gas sector's recovery will likely have a significant impact on the overall economic stability of the region. Continuous monitoring of geopolitical developments will be crucial for adjusting forecasts accordingly.

GROWTH OUTLOOK FOR 2024

Forecast	2023	2024f	Notes
Real GDP growth, %	-0.8	0.7	A recovery in oil production in Q4 2024 will push headline growth into positive territory despite some softening in non-oil economic activity in H2 2024.
Private consumption	2.1	1.3	Household consumption growth will ease on a year-on-year basis, as tighter monetary policy will kick in on consumer spending. However, robust consumer sentiment and easing inflationary pressures will see spending growth remain relatively resilient.
Government consumption	1.4	0.9	Government spending growth will likely continue to moderate as the government adopts a more prudent spending approach.
Fixed capital formation	1.3	1.1	Investment activity will remain above trend, as elevated oil prices will support the liquidity of government-related funds, feeding through robust investment. However, tight financial conditions will remain a drag and slow investment momentum.
Net exports	-4.7	-2.7	Hydrocarbon production growth will contract significantly as a result of OPEC+ production cuts. Meanwhile, import growth will remain robust, driven by steady demand for capital inputs and raw materials as construction work picks up and industrial firms expand.

f = BMI forecast. Source: Bloomberg, BMI

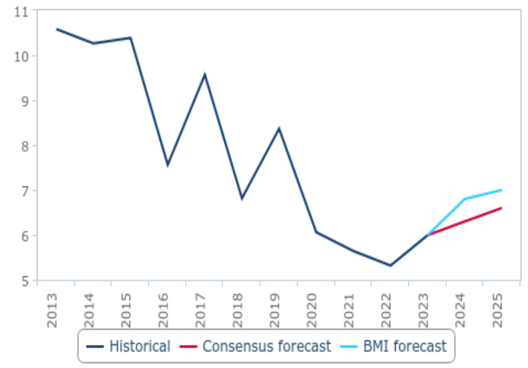
Ethiopia: New IMF Programme Will Support Macroeconomic Stability

Key View

- We expect that Ethiopia's new IMF programme, a four-year Extended Credit Facility arrangement agreed on July 29 and totalling USD3.4bn, will support macroeconomic stability.
- This development was in line with our long-held view and, as such, we have maintained our real GDP growth forecasts at 6.8% for 2024 and 7.0% for 2025.
- The liberalisation of the exchange rate, undertaken to secure the programme, will catalyse foreign investment, and inflationary risks should be relatively limited due to the implementation of subsidies and other social support programmes.
- However, risks to our views are numerous, given that inflation could surge as a result of the birr's devaluation, weighing on growth and social stability and, by extension, posing risks to investor sentiment and the broader debt restructuring process.

IMF Deal Underscores Our Optimistic Ethiopian Growth Outlook

Ethiopia – Real GDP Growth, % (2013-2025)



Source: FocusEconomics, UN, BMI

We expect that Ethiopia's new IMF programme, agreed on July 29, will support macroeconomic stability and the wider debt restructuring process. This was in line with our long-held view that Ethiopia would eventually secure a financing deal with the fund, forming a key part of its debt restructuring process after the country missed a coupon payment on its sole eurobond in December 2023.The programme – a four-year Extended Credit Facility arrangement totalling USD3.4bn – points to significant optimism surrounding Ethiopia's recent economic reforms. IMF Managing Director Kristalina Georgieva said that 'the approval of the ECF is a testament to Ethiopia's strong commitment to transformative reforms. The IMF looks forward to supporting these efforts to help make the economy more vibrant, stable, and inclusive for all Ethiopians.'

IMF Deal Supports Growth Outlook, As Expected

Given that the IMF deal was in line with our view, we have not made any adjustments to our core macroeconomic projections. We remain optimistic on Ethiopia's near-term growth, expecting 6.8% in 2024 and 7.0% in 2025, higher than the consensus forecasts of 6.3% and 6.6% respectively. This is largely because our outlook was premised on Ethiopia getting an IMF deal before end-2024 and subsequently would have significantly higher inflows of dollars and foreign direct investment.

We expect that the deal will support investor sentiment as it represents a concrete marker of progress on Ethiopia's debt restructuring process under the G20 Common Framework. Ethiopian officials have said that 'debt restructuring should be finalised before the next IMF programme review.' The deal also indicates that recent economic reforms are progressing well.

Currency Reform Bodes Well

As we have repeatedly outlined, securing an IMF deal was contingent on the authorities' commitment to economic reforms, including the liberalisation of the

ETHIOPIA – FOREIGN EXCHANGE REFORMS ENACTED ON JULY 29

Key Element	Description	Impact
Market-based exchange rates	Banks are allowed to buy and sell foreign currencies at freely negotiated rates, with limited NBE intervention.	Addresses FX shortages and aligns rates with market dynamics, improving economic stability.
End of surrender requirements	Exporters and commercial banks can retain foreign exchange, boosting private sector FX supplies.	Increases FX availability in the private sector, enhancing liquidity.
Removal of import restrictions	Previous prohibitions on 38 product categories have been lifted, liberalising the FX market for imports.	Facilitates the import of goods, lowering costs and increasing product availability.
Retention rules improvement	Exporters can retain 50% of their foreign exchange proceeds, up from 40%.	Provides exporters more capital to reinvest, promoting growth and competitiveness.
Non-bank FX bureaus	Non-bank entities can now engage in buying and selling foreign currency cash notes at market rates.	Increases competition and enhances price discovery, potentially leading to better rates and services for consumers and businesses.
Special economic zones	Companies in these zones can retain 100% of their foreign exchange earnings.	Encourages investment in these zones, promoting industrial and economic development.
Temporary subsidies	Subsidies on essential imports like fuel, fertilizers, medicine, and edible oil to minimize price impacts.	Helps manage the cost of living by keeping essential goods affordable during the transition.
Opening securities market	Ethiopia's securities market is now open to foreign investors, with terms and conditions to be specified.	Attracts foreign investment, increasing capital inflows and supporting financial market development.

Source: National Bank of Ethiopia, BMI exchange rate. Since March 2022, the birr had been tightly managed against the US dollar, resembling a crawling peg arrangement. However, on July 29 2024 (hours before the IMF deal was announced), the National Bank of Ethiopia announced a shift to a market-based exchange rate regime, allowing banks to buy and sell foreign currencies from and to their clients and between themselves at freely negotiated rates, alongside other FX liberalisation measures. Over time, we expect that these reforms will support investor positioning towards Ethiopia, forming a key part of the country's efforts to attract more foreign investment.

Already reflecting stronger investor positioning towards Ethiopia, following the confirmation of a deal the country's eurobond yield fell to 77.4%, from 88.1% prior, though we do note that it remains very high following the December 2023 default and as the IMF deal is only the first of many steps that Ethiopia must take to restructure its debt burden.

As we had expected the birr to be devalued this year, we retain our end-2024 forecast of ETB80.0/USD. Following the announcement, the Commercial Bank of Ethiopia – the country's main bank – initially quoted the middle rate at ETB75.4/USD, 23.1% weaker than the July 26 rate of ETB58.1/USD, and maintained this rate for July 30. Thus far, the devaluation process is following the framework that we have outlined previously, with an initial good-faith sharp adjustment (to secure the IMF deal) followed by a period of more managed depreciation, to avoid unnecessary macroeconomic instability.

We anticipate that two short-term factors will limit the pace of depreciation. First, the IMF has front-loaded its support, allowing for the immediate disbursement of USD1.0bn. This will bolster short-term dollar supply and will allow the authorities to manage the pace that the birr is devalued at, which is crucial given that the parallel market rate reportedly stood at around ETB120.0/USD as of July 30 (37.2% weaker than the current spot of ETB75.4/USD).

Second, we also expect that the IMF deal will prompt an increase in other capital inflows, supporting dollar supply over the medium-term. The USD3.4bn from the IMF is only part of the USD10.7bn that the authorities expect in total, from loans, grants, and debt re-profiling.

The IMF stated that the programme will 'catalyse additional external financing from development partners and provide a framework for the successful completion of the ongoing debt restructuring'. This rapid increase in FX inflows should see the birr's official and parallel rates converge towards our end-2024 forecast, limiting the likelihood of a sharper depreciation.

Despite the liberalisation of the exchange rate, we do not expect a resurgence in price growth. Alongside exchange rate reforms, the authorities implemented a raft of other measures, including the removal of import restrictions, the introduction of temporary subsidies, and substantial social support measures. Subsidies will limit upside inflationary risks, while social support measures will lessen the impact on household incomes

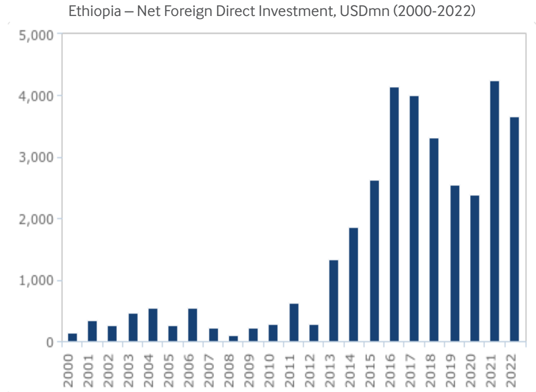
Due to dollar shortages and strict restrictions on access to foreign exchange, we believe that the parallel rate was more widely used in the real economy, limiting the impact of the official rate's depreciation on consumer prices. We still expect that price growth will end 2024 at 13.3%, down from 19.9% in June 2024. Overall, price growth will average 20.3% in 2024, the lowest level since 2019.

Risks To Outlook

Risks to our outloook remain high. Our growth forecasts are premised on continued disinflation despite the birr's devaluation.

Capital Inflows Will Pick Up As Investor Sentiment Improves

Ethiopia – Net Foreign Direct Investment, USDmn (2000-2022)

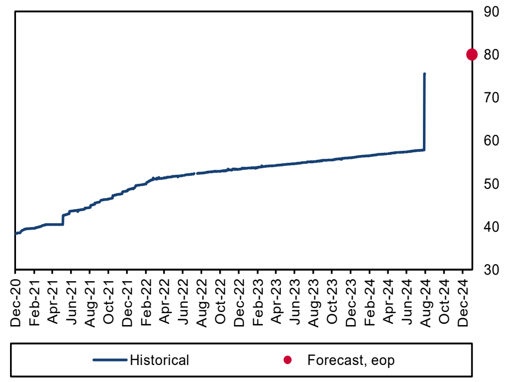


Source: UNCTAD, BMI

However, should the pass-through from the official rate to inflation be stronger than we anticipate, or indeed if the authorities fail to successfully manage the rate of depreciation, inflation will almost certainly pick up again.

Birr Will Remain Weak Following Devaluation

Exchange Rate, ETB per USD

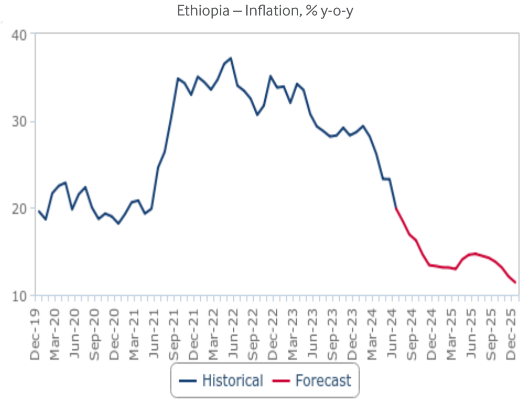


Note: BMI forecast. Source: Haver, National Bank of Ethiopia, BMI

This increases the risk of protests (as we have seen in Kenya in July 2024) against both the government and IMF, which could disrupt commercial activity and sour investor sentiment.

Disinflation Will Continue Despite Birr Devaluation

Ethiopia – Inflation, % y-o-y



Note: BMI forecast. Source: Haver, Ethiopian Statistical Service, BMI

Congo-Brazzaville: Risks To Political Stability Will Remain

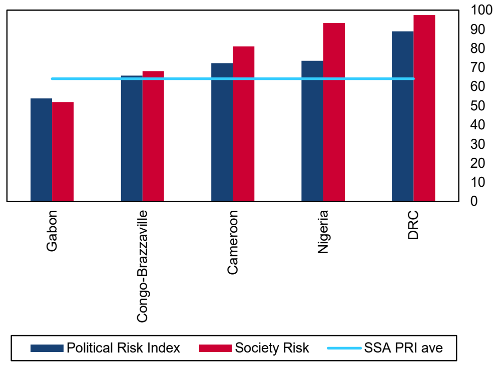
Please Note: *BMI is enhancing its risk analysis with a new scoring system following its acquisition of GeoQuant, a market-leading provider of political risk data. From March 27 2024, risk scores are inverted: zero now represents the lowest risk and 100 represents the highest risk. This allows for clearer, industry-standard assessments. For further details, please refer to our updated methodology document.*

Key View

- We expect that political stability and policy continuity will continue in Congo-Brazzaville for the remainder of 2024.
- That said, limited improvements in socio-economic conditions will raise political risks in the medium term, especially in the run-up to the 2026 elections.
- Congo-Brazzaville's business environment will continue to be undermined by regulatory and political hurdles, including perceptions of widespread corruption.

Congo-Brazzaville's Political Risk Remains Above SSA Average

Congo-Brazzaville – Political Risk Index & Society Component



Note: Scores out of 100; 0 = lowest risk; 100 = highest risk. Source: BMI

We expect that political stability and policy continuity will continue in Congo-Brazzaville for the remainder of 2024. Our view is primarily informed by the ruling party Parti Congolais du Travail dominating both the Senate and the National Assembly, as well as the longstanding rule of President Denis Sassou-Nguesso, who has ruled the Republic of Congo for a cumulative 40 years. He has maintained power by amending the Constitution to remove age limits and extend term limits in 2015, which was met with widespread protests and claims of fraud. Despite the lack of obvious challenges to his authority, Nguesso's administration is associated with increasing perceptions of corruption and suppression of civil liberties.

While political risks are muted in the short term, we believe that limited improvements in socio-economic conditions will raise stability risks in the medium term. According to 2023 Afrobarometer survey data, 48.3% of the respondents believed that the country's economic conditions were 'worse' or 'much worse' than 12 months before, while 56.9 responded that the government had managed the economy 'very badly'.

Widespread poverty, evidenced by a by 35.2% contraction in GDP per capita between 2014 and 2023, combined with a high unemployment rate of 41.2% in 2023 and inadequate public services, will likely increase public dissatisfaction with the government. Despite Congo-Brazzaville's recent progress in structural reforms, which unlocked USD43mn through the country's Extended Credit Facility with the IMF, fiscal consolidation and the phasing out of subsidies will put pressure on household finances and add to the existing living standard woes caused by high inflation and flood-related infrastructure damage in early 2024.

Consequently, we expect President Nguesso's administration to face increasing pressure in the lead-up to the 2026 elections. Signs of this pressure are already evident with the formation of the opposition platform 'Alliance for Democratic Change in 2026,' which includes three political parties aiming to challenge Nguesso's long-standing rule, despite none of them currently holding seats in parliament. However, any public dissatisfaction will likely be restricted by security forces which have historically limited protest activities

Congo-Brazzaville's business environment will continue to be undermined by regulatory and political hurdles. Persistent power cuts, due to the inefficiencies of the state-owned Énergie Électrique du Congo, have prompted the government to seek a private operator for electricity distribution under a leasing contract.

While privatising electricity provision may offer some improvements, substantial reforms are needed to address the fundamental challenges within the country's operating environment.

Perceived corruption remains widespread, with the president's family and advisers having been accused of exploiting the National Petroleum Company of Congo for personal gain. French authorities have been investigating Orion Oil since 2012, allegedly used by Nguesso for misappropriating oil revenue.

Meanwhile, the government's involvement in key industries like oil, minerals and aviation further complicates the business landscape, with business rights often being undermined by bureaucracy and weak judicial safeguards. The revocation of mining licenses from companies like Sundance Resources and Avima Iron Ore in December 2020 has discouraged non-Chinese mining investment, with disputes over these licenses lasting until July 2024.

Climate change compounds Congo-Brazzaville's socio-economic challenges, posing a significant risk to social stability. The country faces rising temperatures, erratic rainfall and increased storms and severe flooding, with recent floods in late 2023 and early 2024 affecting over 1.8mn people. Currently, 36% of the population is food insecure and crop yields could drop by 5-15% by 2050 according to the World Bank.

As such, the impacts of climate change threaten infrastructure, labour productivity and agricultural output. If the country's climate preparedness is not improved, these issues will exacerbate social instability, as reduced agricultural productivity, impaired health and higher flooding risks will exacerbate social grievances. Efforts are underway to integrate climate aspects into policy and enhance structural reforms, such as seeking funding from the Resilience and Sustainability Facility. However, delays in funding and mitigation measures could lead to more frequent humanitarian crises related to adverse weather events.

BMI EMERGING EUROPE FX FORECASTS, AVE

	2022	2023	Current	2025	2026
Czech Republic, CZK per EUR	24.56	24.00	23.51	25.00	24.38
Hungary, HUF per EUR	391.83	381.84	365.64	417.50	430.00
Poland, PLN per EUR	4.69	4.55	3.97	4.28	4.23
Romania, RON per EUR	4.93	4.95	4.60	5.01	5.05
Russia, RUB per USD	68.48	85.16	86.33	97.25	97.00
Turkiye, TRY per USD	16.55	23.74	33.06	41.25	47.25
Ukraine, UAH per USD	32.34	36.57	41.03	43.00	45.50

Source: Haver, BMI. Last updated: July 31 2024

BMI LATIN AMERICA FX FORECASTS, AVE

	2022	2023	Current	2025	2026
Argentina, ARS per USD	130.62	296.26	932.00	1,300.00	1,500.00
Brazil, BRL per USD	5.16	4.99	5.66	5.40	5.05
Chile, CLP per USD	873.31	840.07	956.58	900.00	859.08
Colombia, COP per USD	4,256.19	4,325.96	4,089.05	4,300.00	4,263.68
Mexico, MXN per USD	20.13	17.76	18.60	19.50	18.75
Peru, PEN per USD	3.84	3.74	3.73	3.60	3.60

Source: Haver, BMI. Last updated: July 31 2024

BMI SUB-SAHARAN AFRICA FX FORECASTS, AVE

	2022	2023	Current	2025	2026
Ghana, GHS per USD	8.27	11.02	14.90	14.09	15.27
Kenya, KES per USD	117.87	139.85	129.92	135.50	138.37
Nigeria, NGN per USD	425.98	636.13	1,611.21	1,359.75	1,377.22
South Africa, ZAR per USD	16.36	18.45	18.27	19.19	19.57
Uganda, UGX per USD	3,689.82	3,726.14	3,721.36	3,870.54	3,878.16
Zambia, ZMW per USD	16.94	20.21	26.17	24.20	24.80

Source: Haver, BMI. Last updated: July 31 2024

BMI MIDDLE EAST AND NORTH AFRICA FX FORECASTS, AVE

	2022	2023	Current	2025	2026
Egypt, EGP per USD	19.16	30.63	48.57	47.98	48.93
Morocco, MAD per EUR	10.69	10.96	9.91	10.72	10.86

Source: Haver, BMI. Last updated: July 31 2024

BMI EMERGING ASIA FX FORECASTS, AVE

	2022	2023	Current	2025	2026
China (Mainland), CNY per USD	6.74	7.08	7.22	7.15	7.13
India, INR per USD	78.60	82.60	83.70	81.50	83.54
Indonesia, IDR per USD	14,849.85	15,236.88	16,294.00	15,616.25	15,850.49
Malaysia, MYR per USD	4.40	4.56	4.61	4.48	4.51
Philippines, PHP per USD	54.48	55.63	58.65	55.75	56.20
Taiwan, China, TWD per USD	29.81	31.16	32.84	30.80	28.30
Thailand, THB per USD	35.06	34.80	35.76	35.75	36.75

Note: May include territories, special administrative regions, provinces and autonomous regions. Source: Haver, BMI. Last updated: July 31 2024

BMI EMERGING EUROPE CENTRAL BANK POLICY RATE FORECASTS, % EOP

	2022	2023	Current	2025	2026
Czech Republic	7.00	6.75	4.75	3.00	3.00
Hungary	13.00	10.75	6.75	5.00	4.00
Poland	6.75	5.75	5.75	4.50	4.00
Romania	6.75	7.00	6.75	4.50	4.00
Russia	7.50	16.00	18.00	16.00	14.00
Turkiye	9.00	42.50	50.00	30.00	15.00
Ukraine	25.00	15.00	13.00	10.50	8.00

Source: Haver, BMI. Last updated: July 31 2024

BMI LATIN AMERICA CENTRAL BANK POLICY RATE FORECASTS, % EOP

	2022	2023	Current	2025	2026
Argentina	75.00	100.00	40.00	20.00	10.00
Brazil	13.75	11.75	10.50	8.50	8.00
Chile	11.25	8.25	5.75	4.00	3.75
Colombia	12.00	13.00	10.75	5.25	4.50
Mexico	10.50	11.25	11.00	8.50	8.00
Peru	7.50	6.75	5.75	3.75	3.00

Source: Haver, BMI. Last updated: July 31 2024

BMI SUB-SAHARAN AFRICA CENTRAL BANK POLICY RATE FORECASTS, % EOP

	2022	2023	Current	2025	2026
Ghana	27.00	30.00	29.00	20.00	16.00
Kenya	8.75	12.50	13.00	8.00	8.00
Nigeria	16.50	18.75	26.75	22.00	18.00
South Africa	7.00	8.25	8.25	7.00	6.75
Uganda	10.00	9.50	10.25	9.00	8.00
Zambia	9.00	11.00	13.50	11.50	10.00

Source: Haver, BMI. Last updated: July 31 2024

BMI MIDDLE EAST AND NORTH AFRICA CENTRAL BANK POLICY RATE FORECASTS, % EOP

	2022	2023	Current	2025	2026
Egypt	17.25	20.25	27.25	16.25	8.25
Morocco	2.50	3.00	2.75	2.00	2.00

Source: Haver, BMI. Last updated: July 31 2024

BMI ASIA CENTRAL BANK POLICY RATE FORECASTS, % EOP

	2022	2023	Current	2025	2026
China (Mainland)	2.75	2.50	2.30	2.20	2.10
India	6.50	6.50	6.50	5.50	5.00
Indonesia	5.50	6.00	6.25	5.00	5.00
Malaysia	2.75	3.00	3.00	3.25	3.25
Philippines	5.50	6.50	6.50	4.50	3.50
Taiwan, China	1.75	1.88	2.00	1.88	1.75
Thailand	1.25	2.50	2.50	2.00	1.50

Note: May include territories, special administrative regions, provinces and autonomous regions. Source: Haver, BMI. Last updated: July 31 2024