

Research

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EM: Countries at risk amid the global credit crunch

The credit crisis is spreading and after the economic and financial collapse in Iceland, the markets are asking the question - which country will be the next to fall? The markets seem to have decided that Hungary will be the next 'Iceland' and the Hungarian forint has plummeted in recent days. However, there are other countries that share some unpleasant similarities with Iceland.

In this note we list 15 countries that we think are in the 'danger zone' in the present environment. That is not to say that these countries will undergo the same fate as Iceland, but they are all at risk of a significant slowdown in the economy and of increased financial distress - as we have seen in Iceland and Hungary recently.

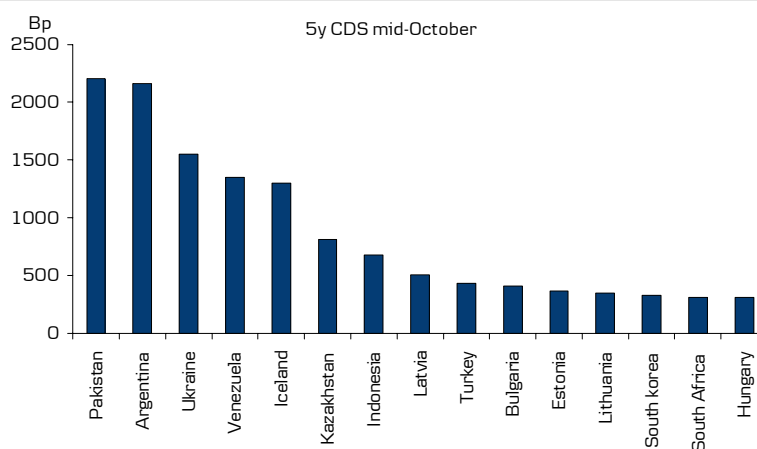
We focus on three factors when deciding which countries should be included in the 'danger zone':

- Large current account deficit, high credit growth in recent years, asset market bubbles, large reliance on foreign currency funding
- Increased political risks - both domestic and geo-political
- Commodity exporters that failed to used to the 'good years' to save for the bad years


Once again, it is not a given that these countries will undergo a similar collapse as Iceland, but we think market participants should be very careful in these markets.

Below we list the countries with a few key facts on each. There is no ranking of the countries and it is not an 'Iceland look-alike contest', but rather a general list of countries with heightened risks in the present deleveraging environment.


For more information on the countries, please refer to our *Emerging Markets Briefer - IMF's busy travel itinerary* published yesterday.





Source: Bloomberg


<p>Iceland</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB (negative) • Moody's: A1 (downgrade review) • Fitch: BBB- (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -20% of GDP • Inflation: 12.1% y/y • GDP/capita: 60122 USD <p>5y CDS: 1304.1</p>	<ul style="list-style-type: none"> • In recent years Iceland has become the most indebted country in the world and credit growth has been very strong. • The Icelandic boom has now come to an end with the total collapse of the Icelandic financial sector and GDP is likely to drop sharply. • Iceland is in negotiations with Russia about a possible loan to get out of the crisis. However, we expect the IMF to step in sooner or later with a rescue package.
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<p>Bulgaria</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB+ (stable) • Moody's: Baa3 (stable) • Fitch: BBB (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -25% of GDP • Inflation: 12.2% y/y • GDP/capita: 6849 USD <p>5y CDS: 409.2</p>	<ul style="list-style-type: none"> • Widening of current account deficit is key risk – strong credit growth due to buoyant consumer spending may fuel inflationary pressures further. A hard landing is increasingly likely. • This regime has been stable for a long time, but large and increasing imbalances and the risk of a hard landing are raising doubts about the sustainability of the currency board regime.
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<p>Estonia</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: A (negative) • Moody's: A1 (stable) • Fitch: A- (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -13% of GDP • Inflation: 10.2% y/y • GDP/capita: 18809 USD <p>5y CDS: 370.0</p>	<ul style="list-style-type: none"> • High probability of negative growth for 2008. Recovery is expected in 2010-11. • Inflation is not expected to slow until 2009. • The property market bubble has burst and prices have dropped sharply and could continue to fall for some time.
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<p>Hungary</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB+ (negative watch) • Moody's: A2 (stable) • Fitch: BBB+ (stable) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -5.5% of GDP • Inflation: 6.3% y/y • GDP/capita: 16343 USD <p>5y CDS: 313.3</p>	<ul style="list-style-type: none"> • Despite the fact that Hungary has seen a significant improvement in both the current account situation and public finances over the past year, the markets seem to have 'decided' that Hungary is the next Iceland. • The IMF has already offered Hungary 'financial and technical' support. The ECB is providing the Hungarian central bank with a EUR3bn liquidity facility.
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<p>Kazakhstan</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB- (negative) • Moody's: Baa2 (stable) • Fitch: BBB (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: 4.3% of GDP • Inflation: 17.6% y/y • GDP/capita: 9076 USD <p>5y CDS: 812.5</p>	<ul style="list-style-type: none"> • The Kazakh financial sector has been heavily addicted to foreign currency funding in recent years. Rich liquidity supported construction and property market sectors. • However, the construction boom is over, and the Kazakh economy faces headwinds from lower oil prices.
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<p>Latvia</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB+ (negative) • Moody's: A2 (stable) • Fitch: BBB (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -15.1% of GDP • Inflation: 15.9% y/y • GDP/capita: 14930 USD <p>5y CDS: 508.3</p>	<ul style="list-style-type: none"> • GDP growth is likely to be negative in 2008 and may not resume until 2012-13. Large imbalances like high C/A deficit will make recovery process painful. • High inflation will remain high next year due to hike in energy prices. • House prices have fallen significantly and could fall further due to tight credit conditions.
<p>Lithuania</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: A- (negative) • Moody's: A2 (stable) • Fitch: A- (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -14.9% of GDP • Inflation: 11.3% y/y • GDP/capita: 14456 USD <p>5y CDS: 350.0</p>	<ul style="list-style-type: none"> • Growth will slow; however, the slowdown will not be as strong as in the other Baltic States. • There is a risk that the housing market will stagnate and house prices will fall as in the other Baltic countries.
<p>South Africa</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BBB+ (stable) • Moody's: Baa1 (positive) • Fitch: BBB+ (stable) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -8.0% of GDP • Inflation: 11.8% y/y • GDP/capita: 6170 USD <p>5y CDS: 313.8</p>	<ul style="list-style-type: none"> • Inflation has risen sharply recently, and the central bank is way behind the curve with its monetary policies. • Imbalances are very large and the economy is stalling as domestic demand is very weak. • With the resignation of the president, political risks have risen significantly.
<p>Turkey</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BB- (stable) • Moody's: Ba3 (stable) • Fitch: BB- (stable) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -6.5% of GDP • Inflation: 10.5% y/y • GDP/capita: 11463 USD <p>5y CDS: 432.7</p>	<ul style="list-style-type: none"> • The Turkish current account deficit has increased sharply in recent years and Turkish foreign debt remains high. This makes Turkey very sensitive to the global credit crisis. • Political risk has increased in Turkey over the past year with tensions between the Turkish Islamist-oriented government and Turkish secular elite rising.
<p>Ukraine</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: B+ (stable) • Moody's: B1 • Fitch: BB- (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -10% of GDP • Inflation: 25.3% y/y • GDP/capita: 4319 USD <p>5y CDS: 1550</p>	<ul style="list-style-type: none"> • Inconsistent policies and increased political uncertainty ahead of snap parliamentary elections represent a dangerous combination given tensions in global liquidity markets and large imbalances in the Ukrainian economy. • Ukraine has asked the IMF for help to limit liquidity strains.


LATAM


<p>Argentina</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: B (stable) • Moody's: B3 (stable) • Fitch: RD <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: 0.8% of GDP • Inflation: 9.1% y/y • GDP/capita: 8522 USD <p>5y CDS: 2160.0</p>	<ul style="list-style-type: none"> • Argentina failed to address structural issues over the past couple of years, where growth has been high. • The economy has become highly distorted - including heavy subsidisation and taxation. Public spending has been excessive and monetary conditions far too easy.
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<p>Venezuela</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BB- (stable) • Moody's: B2 (upgrade review) • Fitch: BB- (negative) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: 8.5% of GDP • Inflation: 27.2% y/y • GDP/capita: 11828 USD <p>5y CDS: 1350.0</p>	<ul style="list-style-type: none"> • It is easy to hide structural issues, when oil prices are rising and the global environment is benign. • However, as the global credit escalates, structural issues become very visible very fast. • The boom is over and the economy is heading for a sharp slowdown.
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Emerging Asia

<p>Indonesia</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: BB- (stable) • Moody's: Ba3 (stable) • Fitch: BB (stable) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: 0.1% of GDP • Inflation: 9.8% y/y • GDP/capita: 2181 USD <p>5y CDS: 676.7</p>	<ul style="list-style-type: none"> • The current account has turned into small deficit because of resilient domestic demand and higher crude oil prices. • Sensitive to foreign portfolio flows with considerable foreign exposure in domestic bond market. • However, current account to improve on lower oil prices and very strong FX reserve position.
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<p>Pakistan</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: CCC+ (negative) • Moody's: B2 (negative) • Fitch: N/A <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -8.7% of GDP • Inflation: 12.0% y/y • GDP/capita: 1000 USD <p>5y CDS: 2204.1</p>	<ul style="list-style-type: none"> • FX reserves are running dangerously low in light of a major current account deficit and the continued need to service foreign debt. • Weak government has prevented necessary adjustment in economic policy. • Either IMF or Middle Eastern bail-out needed.
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<p>South Korea</p> 	<p>Credit rating:</p> <ul style="list-style-type: none"> • S&P: A (stable) • Moody's: A2 (stable) • Fitch: AA (stable) <p>Avg. 2008 estimates:</p> <ul style="list-style-type: none"> • C/A: -1.3% of GDP • Inflation: 4.8% y/y • GDP/capita: 19638 USD <p>5y CDS: 239.2</p>	<ul style="list-style-type: none"> • Main problem is banks' dependence on short-term foreign funding and sharp increase in debt leverage among private households. Hence financial risk more than sovereign risk. • On the positive side: strong liquidity position and the current account will return into surplus next year.
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Sources: Ecwin, Bloomberg, IMF, own calculations

Earlier research from Danske Research on the risk of boom-bust in the Emerging Markets:

[Research - EU8+2: A Warning not to be ignored II](#), 14 December, 2007

[Flash Comment - CIS: Why we should care about problems in the Kazakh banking sector](#), 5 October, 2007

[Research - New Europe: Mind the ratings](#), 22 March, 2007

[Research - New Europe: A warning not to be ignored](#), 23 February, 2007

[Research - Iceland: Geyser Crisis](#), 21 March, 2006

Recent research on the impact from the credit crisis on the Emerging Markets:

[Emerging Markets: IMF's busy travel itinerary The outlook for the Emerging Markets in a deleveraging world](#), 16 October, 2008

[Flash Comment - Emerging Markets, Korea: KRW slides on Standard & Poor's move to 'negative watch' on banks](#), 16 October, 2008

[Flash Comment - Hungary: ECB to the rescue. Will the ECB also help Croatia?](#), 16 October, 2008

[Flash Comment - Hungary: S&P might downgrade Hungary - crisis intensifies](#), 16 October, 2008

[Emerging Markets Briefer - IMF's busy travel itinerary](#), 15 October, 2008

[Research - Pakistan: Badly in need of foreign assistance](#), 13 October, 2008

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[Flash Comment - LATAM currencies feel the global credit squeeze](#), 9 October 2008

[Flash Comment - Iceland: Geyser crisis unfolding](#), 7 October, 2008

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[Flash Comment - Emerging Markets: Implications of US 'bail-out' package](#), 19 September, 2008

[Flash Comment - Russia: The credit crunch marches on Moscow](#), 18 September 2008

[Emerging Markets Briefer - Running out of safe havens](#), 16 September, 2008

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