Standard Chartered Africa Focus | 10 July 2013

A wealth of diversity

Highlights

- Prospects in the Sub-Saharan African region remain largely positive, despite uncertainty related to market expectations of Fed tapering, and a slowdown in China's growth trend to more sustainable levels.
- South Africa is more susceptible to global risks, and has seen a slowdown in domestic growth momentum. Recent market volatility has limited countercyclical policy options. We lower our 2013 South Africa GDP forecast to 2.2% (2.7% previously). Elsewhere in Africa, demand is more resilient. Angola, Cote d'Ivoire, Ghana, Zambia, and a swathe of new resource economies in East Africa should all see medium-term trend growth of c.7%.
- Fears that Africa will be hit hard by a moderation in China's growth trend are misplaced. While much of Africa's growth impetus remains domestic, trade with China continues to increase.
- The impact of QE tapering on Africa will not be uniform. More liquid markets that have seen a higher level of foreign investor participation are more vulnerable. Nonetheless, with a tapering of QE now largely discounted, we expect domestic fundamentals to reassert themselves.
- We maintain an *Overweight* duration and FX weighting on Nigeria, we are *Overweight* duration on Ghana, but *Neutral* on the Ghana cedi. We maintain a *Neutral* duration stance on South Africa, and *Underweight* FX weighting on the rand. We are *Neutral* duration in Kenya and Uganda, given a less favourable demand/supply outlook. We remain *Neutral* duration on Zambia given expectations of tighter liquidity.

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China's focus on sustainable growth is right

Markets have taken a double hit from worries over tightening signals in the US and the effective tightening impact of policy in China. There is an irony in the sell-off in emerging markets. First, the Fed's intention to start paring back its quantitative easing (QE) programme suggests that it thinks the US economy is finally showing enough strength to cope with such change. In Europe, the introduction of the Outright Monetary Transactions (OMT) last year reduced tail risks significantly. The beauty of the OMT can be found in its credibility, it has been successful without spending a single euro to support sovereign bonds in the periphery. The concern right now is that the legitimacy, and therefore the credibility of the OMT are being assessed and questioned by the constitutional court in Germany.

China's policy makers are clearly committed towards rebalancing their economy. Growth in China will likely stay in a 7-8% range. This is indeed lower than the past. But it is far more sustainable. And it is worth reminding ourselves that an economy that grows by 7% a year can still end up doubling in size in a decade.

Right now, portfolios are being adjusted to take into account potential changes in global liquidity and China's rebalancing. In this environment, emerging-market (EM) assets have underperformed relative to the US. But markets will eventually have to be driven by fundamentals rather than liquidity and sentiment alone. It is imperative to look at the fundamentals underpinning markets in order to separate the 'signal' from the 'noise'. In our view, China's commitment to growth sustainability rather than growth at any cost will ultimately improve the relative attractiveness of the East versus the West over the medium term.

Fed tapering should be driven by data, not forecasts

US QE is helping to mitigate the effects of still contractionary fiscal policy

In the US, the Fed's low interest rate policy and QE have mitigated, but not eliminated, the impact of ongoing fiscal tightening. The economy has absorbed this year's fiscal pressure (the January tax hikes and federal spending cuts) with surprising resilience. Interest rate-sensitive sectors are driving the US recovery: momentum in the housing market continues unabated. QE's success is also attributable to the health of the US banking system, particularly compared to Europe.

Federal Reserve Chairman Ben Bernanke has indicated that downside risks to the outlook have diminished, and it is now time to take the foot off the QE pedal. After hinting at QE tapering in his 22 May Congressional testimony, Bernanke confirmed at the June FOMC meeting that it should start "later this year" if the economy continued on the current trend.

Bernanke expects the QE policy to end by mid-2014. By that time, unemployment should have fallen to 7%, a threshold the Fed has set for closing the door on this "unconventional policy". This compares with unemployment of 7.6% currently and 10.0% at its peak in October 2009. But the unemployment rate is not necessarily a good indicator of the true state of the underlying labour market, as it is heavily influenced by swings in the labour-force participation rate (LFPR).

The LFPR is determined by both structural factors (e.g., demographics and population ageing) and cyclical factors (e.g., withdrawal from the labour force). If the LFPR remained at its current level of 63.4% and monthly non-farm payrolls stayed at around 155,000 (the current three-month average), the unemployment rate would reach the Fed's 7% target by Q3-2014, later than the Fed's current forecast of mid-2014.

In this environment, we think it will be difficult for US growth to be much more than 2% this year

QE is unconventional by nature, and exiting from it is a risky process. Communication and timing are key. There are broadly two risks: (1) that the Fed exits too late, with inflation expectations running out of control and/or asset bubbles inflating; or (2) that it exits too rapidly, with a risk of jeopardising the recovery.

We think the Fed's QE reduction calendar looks ambitious, although not impossible. We previously highlighted four reasons why the Fed should wait more before reducing its purchases.

First, the economy still looks fragile, and the Fed's own forecasts are probably too optimistic. This is not necessarily new – since the beginning of the recession, the Fed has continuously overstated the strength of the recovery. GDP growth has averaged only 2.1% since the crisis trough.

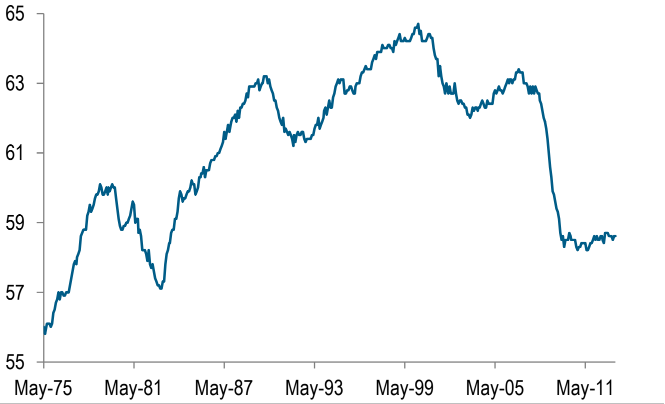
Second, the unemployment rate can flatter the true picture of the US labour market due to lower participation rates. Even though unemployment declined to 7.6% in May 2013 from a peak of 10.0% in October 2009, there are still 2.4mn fewer Americans in employment than in 2008, and the working-age population has increased by 10mn people. There is still considerable slack in the labour market.

Risks of a US government shutdown still loom in Q4-2013

Third, fiscal policy is tighter this year, and we have probably not seen the full impact of this. Consumption held up well in H1-2013 as rising asset prices boosted consumer confidence and consumers dipped into their savings. But the fiscal drag remains a headwind, and it could act with a lag. Political uncertainty could also increase after the summer, when there are a number of important deadlines – including the October deadline for increasing the debt ceiling, and the 1 October deadline for approving a new funding bill (barring a federal budget) to avoid a government shutdown. In the current political environment, one should not be overly optimistic about a smooth agreement between the Democrats and the Republicans: continued political brinkmanship could affect business confidence.

Figure 1: The US labour market remains weak

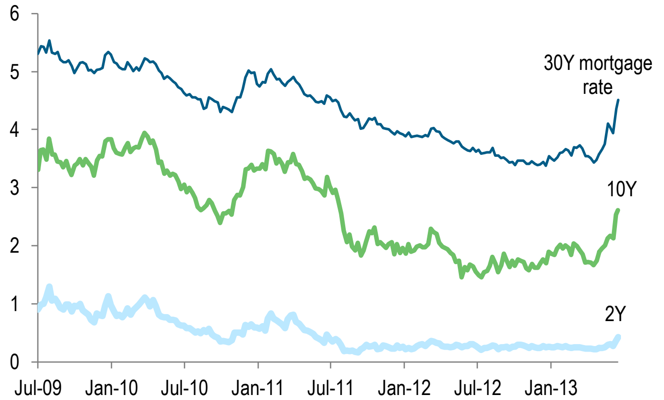
Employment to population ratio, %



Sources: Bloomberg, Standard Chartered Research

Figure 2: A confident Bernanke has pushed up yields

Selected Treasury and mortgage interest rates, %



Sources: Bloomberg, Standard Chartered Research

Finally, it is worth highlighting that inflation is on a continued downtrend, and there are no signs that inflationary pressures will pick up anytime soon. April's core PCE inflation (1.05%) was the lowest since the series began in the 1960s. This creates room to wait longer before reducing QE. Our view is that the Fed will still taper in a few months' time. Given the recent improvement in the labour market, this could start as early as September, but some risks persist.

The sharp market reaction to Bernanke's signals about QE reduction raises a critical question: what impact will the Fed's tapering of bond purchases have on global monetary and financial conditions? The US is by far the most significant driver of global liquidity. We have found that for every USD 10bn increase in US M1, global M2 increases by USD 24.4bn (*On the Ground, 25 June 2013, 'Global monetary conditions – US versus China'*)

China's authorities are determined to rebalance the economy

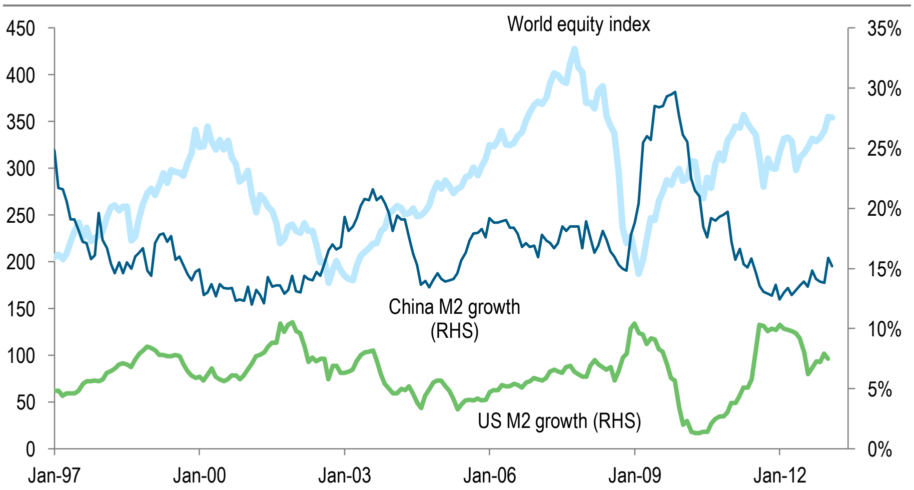
Policy makers in China are more willing than expected to tolerate short-term pain for long-term gain

The Fed is not the only central bank in the spotlight. Recent developments in China's banking system, and the reaction of the People's Bank of China (PBoC), have also received a lot of attention. China's policy makers have indicated their determination to keep interbank liquidity relatively tight as a way to rein in excessive credit growth, and control developments in the 'shadow banking' system. Markets are concerned about the potential side effects, and the repercussions of slower credit growth for GDP growth.

This is compounding fears about the de-facto monetary tightening from the Fed. The signal from China's policy makers is that they are more willing than had been expected to tolerate short-term pain for long-term gain. They are sending a message of prudence to lenders that they must review their funding and their risk management. This comes in the broader context of China's rebalancing. The authorities want to move from the 'old model' driven by cheap credit and plentiful investment to a new model that will bring lower, but more sustainable, rates of growth. Consumption and services will play an increasingly important role. Economic reform, rather than economic stimulus, is the focus in Beijing today. The transition is happening. This is good news, even if it does lead to some short-term pain.

Policy makers have now set a 7% medium-term yearly GDP growth target. Unless there is a significant deterioration in growth, they are likely to focus on broader, more long-term issues such as promoting urbanisation, fostering a level playing field for the private sector, and upgrading social services such as education and health care.

Figure 3: US and China M2 growth and world equity market



Sources: Bloomberg, Standard Chartered Research

Europe: OMT under siege

Little has been done with the time bought by Draghi's commitment to do 'whatever it takes'

The euro area has been of less concern to the markets in recent months as it continues to benefit from policy commitments, particularly from the European Central Bank (ECB). In our view, the ECB's promise to do "whatever it takes" to save the euro, and the subsequent creation of the Outright Monetary Transactions bond-buying programme, have been key drivers of improved sentiment in the euro area. Under the OMT, the ECB pledges to buy an unlimited amount of sovereign bonds in the secondary market in order to stabilise yields if necessary. The programme is credible, and because of this credibility it has been a huge success. It helped to reduce sovereign bond yields for troubled countries such as Spain and Italy, without the countries applying for assistance or the ECB spending a single euro. The OMT pulled the euro back from the brink of collapse and bought the euro area some time.

Unfortunately, this time has not been used effectively. There are still no pro-growth measures in the euro area, even in northern countries that can afford fiscal expansion. As a result of the lack of growth, fiscal and debt burdens are not declining, and unemployment continues on an upward trajectory. The constitutionality of the OMT is also now being assessed by the German constitutional court, despite the programme's clear success (at no cost to German taxpayers). Any development that undermines the credibility of the OMT may lead to renewed, and unnecessary, pressures within the euro area, in our view.

Economic pain in southern Europe continues to increase

Meanwhile, politicians are still at loggerheads over the next steps for banking union and other policies to increase regional integration. The momentum has stalled as Germany focuses on its September elections. And the continued drop in activity and rise in unemployment across southern Europe put increased pressure on governments.

The question is whether the spillover effect from rising US bond yields and the undermining of the OMT threaten to reignite the euro-area crisis. In the wake of the June FOMC meeting, Spanish yields jumped above 5%, and Italian yields are now close to this level. A sustained rise in yields could trigger a loss of confidence in peripheral debt if market participants believe that higher marginal funding costs threaten these countries' fiscal targets. Italy is too big to fail and too big to be rescued. Portugal and, to a lesser degree, Ireland are increasing pressure on the ECB to be accepted as the first OMT candidates. Draghi has renewed his verbal commitment to the OMT, saying that the Fed's decision to taper makes the OMT option "even more relevant". We could not agree more. But the Damocles sword of the German constitutional court's verdict is denting the programme's credibility.

The changing environment

A rebalanced China will help the world economy shift towards a more sustainable growth path

The current global policy environment is changing. Policy actions in China are consistent with the authorities' intentions to rebalance the economy. This is necessary for sustainable growth, even if it means that China will have to be satisfied with growth rates of 7-8%. In the US, the Fed's stated determination to start reducing QE will have to face the growth test. Although we expect modest tapering to begin in September, any weakness in growth over the summer could push back the tapering start date. An increase in yields is itself a macroeconomic headwind, although it could take weeks to materialise in the data. In the euro area, progress is slow, and developments surrounding the OMT are cause for concern. Volatility is likely to continue until markets settle into new, possibly wider, ranges.

Africa overview – Brighter prospects ahead

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Growth resilience

Growth prospects for the SSA region remain largely positive; the deceleration in our annual growth forecast for 2013 mainly reflects the downward revision to South African GDP growth

Growth momentum in Africa remains favourable overall. Despite uncertainty related to market expectations of a reduction in asset purchases by the Fed, as well as a lower (but in our view, more sustainable) 7-8% growth trend in China, prospects for Sub-Saharan African (SSA) economies remain largely positive. South Africa, the region's biggest economy, is an exception. With a greater degree of linkage with the rest of the world, including more liquid financial markets, South Africa will be impacted by the changing global environment. Weak metals prices have impeded an export recovery, the South African rand (ZAR) has been hard-hit by market volatility – complicating the policy response to deteriorating prospects, and domestic demand has weakened since the beginning of the year. We cut our 2013 South Africa growth forecast to 2.2%, from 2.7% previously, reflecting these developments. Largely as a result of this, we lower our 2013 Africa growth forecast (a weighted average of the 13 key SSA economies under coverage) to 4.7% from a previous 5.0%. However, we expect growth in the SSA region in 2014 and 2015 to rise strongly, at 5.3% and 5.6% respectively, up 0.1ppt from previous forecasts.

Domestic demand will remain a key driver of SSA growth

Elsewhere in Africa, domestic demand appears to be a lot more resilient than in South Africa, and is less influenced by global factors. This is not to suggest that cyclical slowdowns are unheard of. Q1-2013 y/y GDP data in Nigeria revealed a slowdown in activity relative to Q4-2012, despite a weak base in Q1-2012, when activity was impacted by fuel-subsidy protests and a deteriorating security situation. But as Nigeria's political cycle gets underway, ahead of elections that are likely to be held in late 2014 or early 2015, greater spending is likely to generate a cyclical uplift to activity. (In 2010, the year before Nigeria's 2011 elections, spending increased c.50% y/y.) In Ghana, as the authorities roll out much-needed fiscal consolidation measures, business and consumer confidence have declined from previously elevated levels. However, even as the non-oil economy slows, c.8% growth is expected overall in 2013, an improvement on last year.

East Africa, the region's 'new energy frontier' is expected to see c.7% growth in the near and medium term

In East Africa, a common theme of recent budgets in Kenya, Uganda and Tanzania is the expectation of 7% growth in the near to medium term. Kenyan growth surprised positively, even in Q1-2013, a quarter that we thought would be disproportionately influenced by the slowdown in activity evident ahead of March elections. While weak growth of only 1.2% y/y was experienced in the financial intermediation sector, and hotels and restaurants saw an outright contraction of almost 16% y/y, a positive performance in agriculture helped to drive overall headline GDP growth of 5.2%.

Peaceful passage of elections provided a significant boost to the Kenyan economy

Confidence in Kenya has surged since the election, now a key political test is behind it. The private sector is encouraged by a new technocrat-dominated cabinet (albeit one that may be less politically experienced). Uncertainty related to ICC trials persists, and the country must still navigate its way through the requirements of more devolved government (the announced fiscal deficit of 7.9% of GDP for FY14 even before meaningful devolution is a concern). Nonetheless, both public and private sector investment plans are gaining momentum. Loan applications in May increased 37% m/m. Kenya finds itself in the midst of an East African region experiencing a new resource boom. Tanzania is closer to becoming a gas producer. Uganda has reached agreement on the size of a domestic refinery, a step that should accelerate its progress to first oil. The growth optimism in the region is palpable.

The impact of QE tapering on Africa is limited

Suggestion of QE tapering has had an uneven impact across African markets

The impact of reduced QE expectations on SSA will not be uniform. This was outlined in our Local Markets Alert following the last FOMC meeting (*Local Markets Alert, 21 June 2013, 'Africa - Unequal vulnerability to US QE tapering'*). More liquid markets such as South Africa that have seen a higher concentration of foreign portfolio investors will be more greatly impacted. Ghana and Nigeria fall in-between, but even here, we expect domestic fundamentals to reassert themselves (our 'Local markets outlook' page 32 has more detail). Other markets, such as Kenya, Uganda and Zambia, where foreign investors account for a lower proportion of ownership of the domestic debt market, have been more resilient. In fact, bond markets in Kenya and Uganda rallied in the last quarter, largely due to domestic factors (Figure 6).

Investors view the interest in frontier Africa as more structural. An eventual end to QE will not alter this interest.

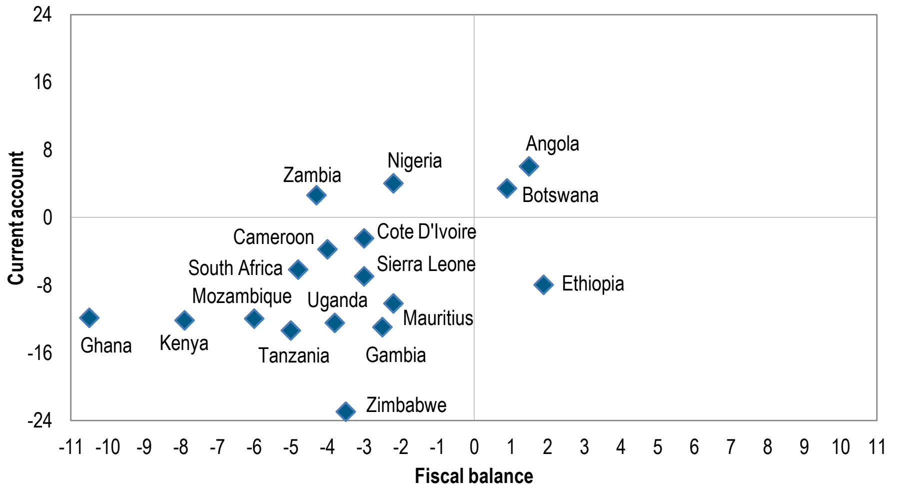
There is some debate over the extent to which demand for Africa's local currency debt had been influenced specifically by QE. We put this question to a number of our investor clients. Most respondents believed that QE had not necessarily been the main factor behind increased investor interest in these markets. More than 70% thought that the interest in frontier African markets was more structural, and would remain in place even after an eventual full reversal of QE, (allowing for some market volatility in the interim). This is borne out by Figure 5, which looks at the impact of QE on the performance of African currencies. Apart from the ZAR, it is difficult to discern other clear beneficiaries from the announcement of QE. Nonetheless, despite not benefiting in an obvious way from QE, other frontier African currencies have come under varying degrees of pressure since the end of May when Fed Chairman Ben Bernanke raised the issue of eventual QE tapering.

Eurobond yields have risen in reaction to QE tapering expectations; it is now more expensive for African issuers to borrow externally, but still attractive relative to the cost of domestic financing

Expectations of a reduction in QE will have more of an impact on Africa's sovereign eurobond market. As can be seen from Figure 4, eurobond yields have backed up since the end of May. It is now more expensive for African sovereigns to raise external debt, although Nigeria's experience in early July demonstrated still-strong demand for higher-rated SSA credits. Nigeria issued a 5Y USD 500mn eurobond, yielding 5.375%, for which it received bids of USD 1.77bn. It also issued a second USD 500mn 10Y eurobond with a yield of 6.625% (compared to 7%, previously in 2011), receiving bids of USD 2.26bn. Like many other SSA sovereigns, Nigeria plans to rebalance its external and domestic borrowing. Even following recent market volatility, it is still cheaper for most African sovereigns to borrow externally

Figure 1: End of QE will bring credit fundamentals into stronger focus

Africa current account, fiscal balance – % of GDP



Sources: IMF WEO April 2013, Standard Chartered Research rather than domestically. We do not expect a meaningful change in the number of African sovereigns planning to issue eurobonds. International capital markets are still open to African issuers, although pricing is likely to have changed.

Investors may now be more discerning about credit quality

Although expectations of the extent of QE tapering look overdone, the rise in US Treasury (UST) yields in recent week will nonetheless make investors look more closely at credit quality. For potential SSA issuers, this is not a bad thing. Concerns that the easy availability of liquidity under QE would trigger an excessive amount of external borrowing by SSA sovereigns should now dissipate. More expensive external borrowing could mean that sovereigns only borrow externally to fund development expenditure (spending that should ideally boost future growth), rather than resorting to excessively cheap external financing for recurrent expenditure. Even cheap debt must eventually be repaid. We expect the Fed to start reducing modestly the extent of its asset purchases in September, but for overall policy to remain accommodative for some time. From this perspective, QE tapering might help African sovereigns avert potential future debt crises.

Concerns over a China 'slowdown' are overdone

China was seen as key to reversing the long-standing undervaluation of African assets

A question we are consistently asked is how much a slowdown in China's trend growth will mean for Africa. Increased economic engagement between China and Africa has been closely linked with the latter's outperformance over the last decade. China grew strongly over this time. Its demand for commodities fuelled African growth. China, almost singlehandedly, helped to reverse the long-standing undervaluation of African assets. So, in a world where China starts to grow at a more sustainable rate, what will it mean for Africa?

A slowdown to a more sustainable growth rate in China will not alter the outlook for Africa

There are a number of points to consider. First, **the overall growth momentum in SSA remains largely domestic**. Although average SSA growth (all 44 economies) decelerated very slightly last year, in response to a slowdown in Europe, Africa's largest trading partner, the impact is expected to be short-lived. Medium-term forecasts (the IMF's as well as our own) all point to a recovery in trend GDP growth, driven mainly by domestic developments. A large number of African economies are growing off a low base. Domestic consumption will continue to be important to overall growth rates.

On average, **credit growth is accelerating across our coverage markets in Africa.** Unlike other more established emerging markets, there were few links between QE-induced inflows and domestic credit growth. Even an eventual reversal of QE, or a modest slowdown in China, should not impact credit growth meaningfully, where a structural transformation in the depth and scale of financial intermediation appears to be underway. In the absence of a commodity price or trade shock on the scale of that observed in 2009, there is little reason to anticipate a meaningful change in credit growth trends. Credit growth, an increasingly important domestic impetus to SSA growth, will likely remain in place.

Average trade-to-GDP ratios in the SSA region are c.30%; exports are not the sole determinant of growth

Trade shares in the SSA region are not substantial, averaging only c.30% of GDP. While individual economies have high commodity dependencies in their export profiles, economic growth does not depend solely on this. At the margin, commodity prices do matter. But softer commodity prices might benefit some African economies, while hurting others.

. Admittedly, a lot of additional growth momentum in Africa is coming from new resource exploration. East Africa with its newly discovered hydrocarbon wealth is a key example. Will such resource exploration stall because of a more subdued rate of growth in China? It is a bit of a stretch to think this. Even a 7% growth rate for China, if sustained for a decade, would be the equivalent of adding a whole, new 'China' to the global economy. If China's growth rate should slow even more, China's commodity demand would still be very significant for SSA.

What does the actual record on trade show? Africa accounts for a small percentage of China's total trade (c.5%), and Africa-China bilateral trade continued to grow, even as the pace of China's overall trade growth slowed last year. In the first four months of 2013 (Jauary-April) trade between China and Africa increased 19.6%, compared with the same period in 2012. Admittedly, this was driven more by increased African imports from China (up 25.7%y/y over this period), while there has been a slowdown in the pace of China's demand for African exports. This grew 'only' 16% y/y between January and April 2013, compared with 25.5% growth in the same period in 2012. The important point is that China's demand for Africa's exports is still growing. It is wrong to overstate the importance of a China slowdown on Africa-China economic engagement, let alone the impact on Africa's overall growth prospects. Even a China growing more slowly will contribute to demand for African exports, and to African growth. Africa still has a sizeable trade surplus with respect to China.

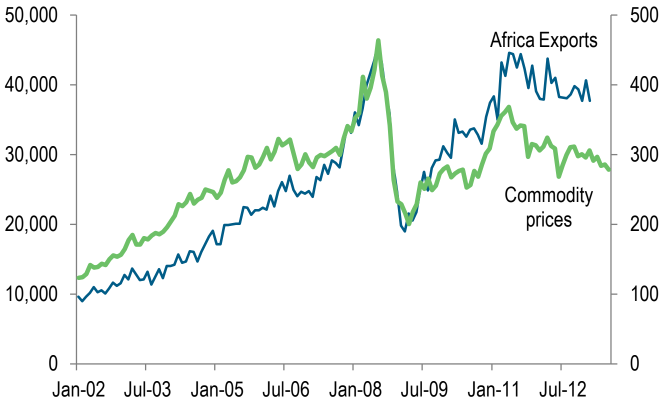
Figure 2: African economies are not uniformly vulnerable to a China slowdown (although 2nd order effects also matter)
African economies – Total trade with China, exports, imports, as % of total trade

	% Exports to China	% Imports from China	% Total Trade with China
Angola	45.8	20.9	39.8
DR Congo	54.7	15.4	34.8
Republic of Congo	39.0	13.4	31.7
Gambia	57.6	27.4	30.8
Sierra Leone	50.6	16.5	28.5
Zambia	43.4	10.4	24.7
Ghana	7.3	25.9	20.6
Tanzania	11.3	21.3	19.1
Cameroon	15.2	18.9	17.2
South Africa	11.8	14.4	13.2
Ethiopia	13.1	13.1	13.1
Kenya	0.8	15.4	12.0
Mozambique	9.0	12.3	11.2
Uganda	2.2	12.6	9.6
Nigeria	1.1	18.4	7.0
Cote d'Ivoire	1.3	10.2	5.4
Senegal	0.7	6.3	4.7

Sources: MOFCOM, Standard Chartered Research

Figure 3: Commodities dominate African exports

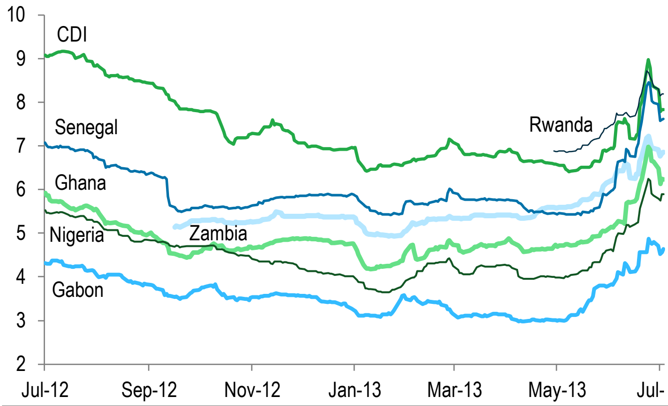
Africa exports (USD mn), commodity price index (2006=100)



Source: IMF

Figure 4: Cost of external borrowing rises on suggestion of QE tapering…

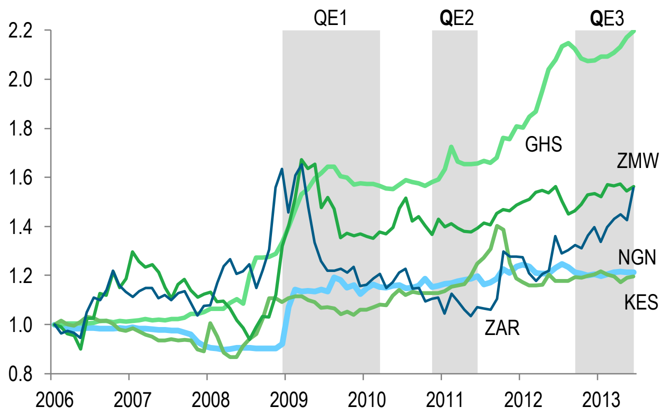
Eurobond yields, selected frontier African economies



Source: Bloomberg

Figure 5: …although QE had a less pronounced effect on African local markets and FX

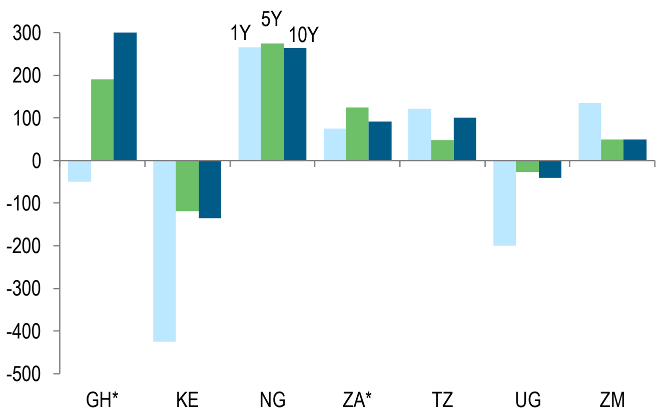
FX rate vs. USD, rebased to 2006 (2006=1)



Sources: Bloomberg, Standard Chartered Research

Figure 6: Domestic bond markets in Kenya and Uganda have rallied, driven by local factors

Q2 vs. Q1 move in benchmark yields, bps

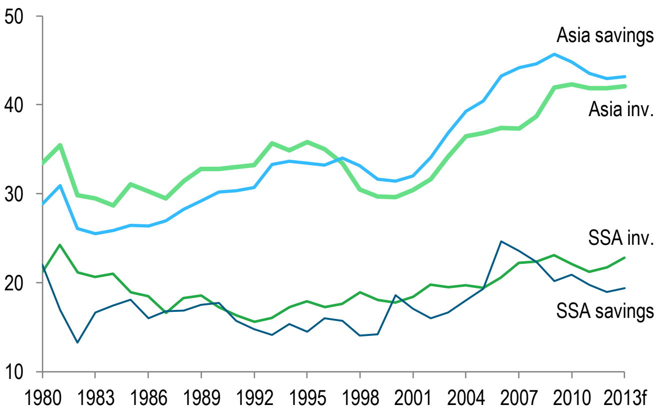


*GH 1Y, 3Y, 5Y and ZA 2Y

Sources: Bloomberg, Standard Chartered Research

Figure 7: Savings and investment – Rising in Africa, but still weaker than in developing Asia

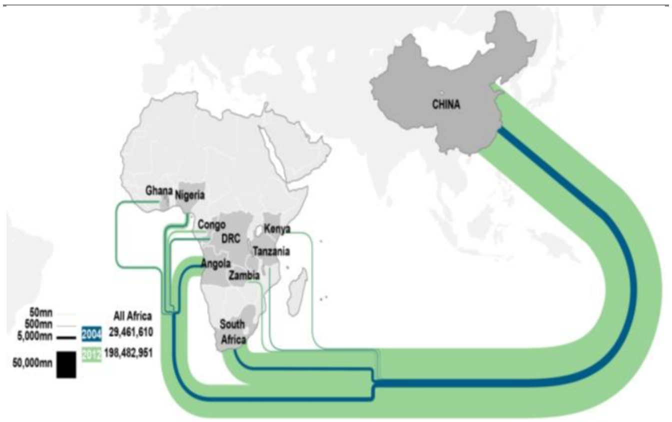
As a % of GDP, developing Asia vs. Sub-Saharan Africa



Sources: IMF WEO, Standard Chartered Research

Figure 8: Despite fears of a China slowdown, bilateral Africa-China trade still increased last year

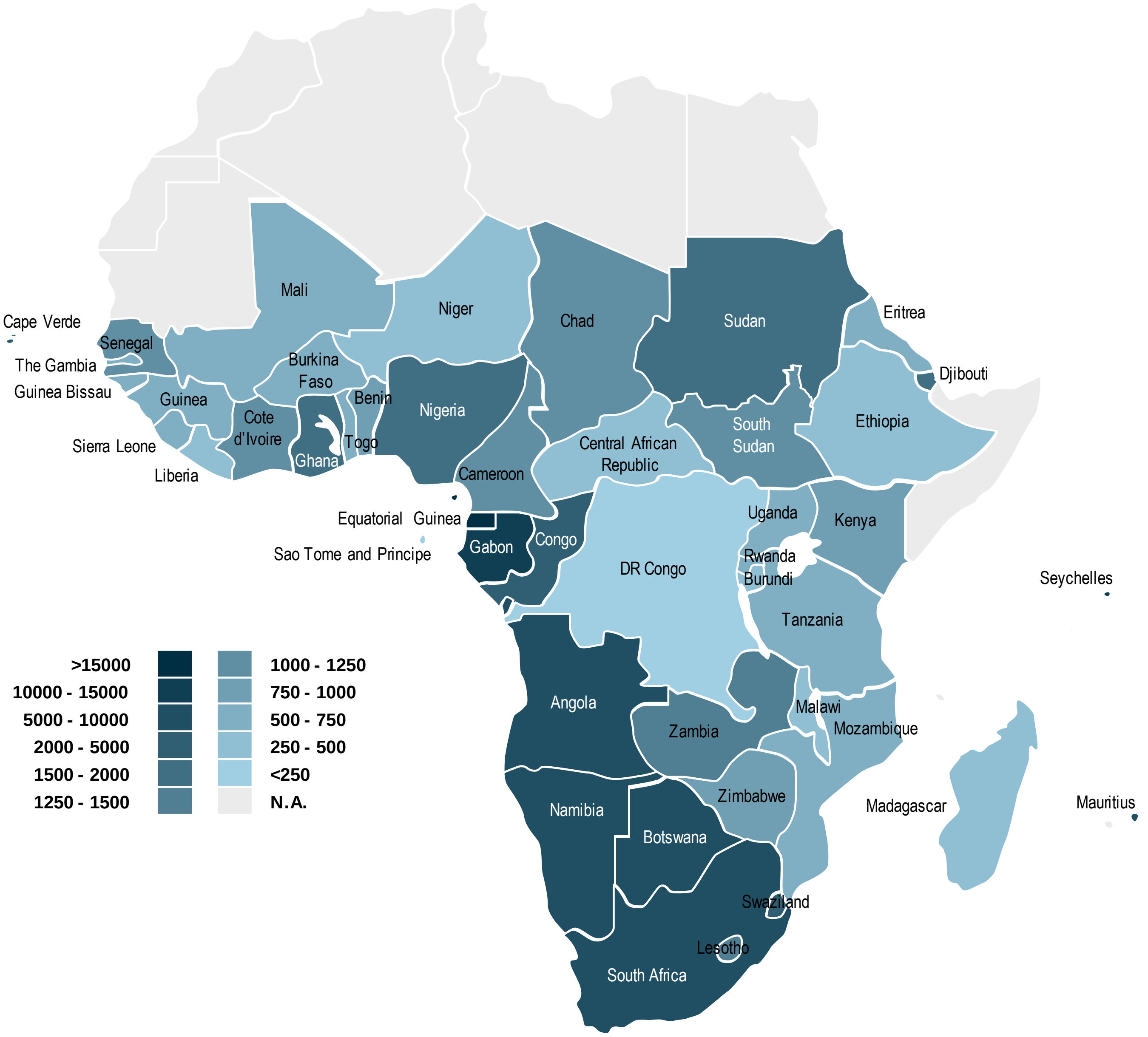
Comparison of China-Africa trade 2004 and 2012



Sources: MOFCOM, Standard Chartered Research

Figure 9: 2012 GDP per capita

USD



Source: Standard Chartered Research

Angola – Shrinking fiscal surpluses, but still strong fundamentals

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Angola's growth is set to remain around 7%, as the non-oil sector remains buoyant

Strong growth driven by non-oil sectors

Real GDP growth of 7% looks achievable this year, especially as the non-oil sector (which now represents 56% of total GDP compared with 53% in 2011) continues to grow rapidly (especially utilities, agriculture and trade) and overall non-oil growth should be around 9-10% this year. Angola's LNG project started in June and will provide some momentum to hydrocarbons growth. Medium-term prospects for oil production are positive; it is projected to increase to 2 million barrels per day (mmbd) in the next two years, from current levels of 1.8mmbd.

Less vulnerable to a potential fall in oil prices

More resilient to potential shocks

The global outlook remains uncertain and Angola is vulnerable to a fall in oil prices, as oil represents 98% of its exports, 80% of its fiscal revenues and 44% of GDP. However, the country is now better placed to cope with an adverse external environment. A fall in oil prices would negatively impact growth and development objectives. Public finances would also be challenged, but the impact would be less negative than in the past, as the country has increased its savings and improved its fiscal management since the 2009 global crisis. The government has some room for manoeuvre given (i) its high level of savings (equivalent of 26.3% of GDP in 2012 or around 8 months of spending, a more comfortable level than other oil exporters in the region); and (ii) fiscal flexibility, given the high share of capital spending (one-third of total spending) that can be cut in the event of a sustained decline in oil prices.

It has also improved its fiscal management: 'excess' oil revenues, which occur when the oil price is above the budgeted level, are saved in an account at the central bank. This revenue cannot be spent without a budget appropriation (in 2009, when oil prices collapsed, poor fiscal management contributed to an acute crisis, leading to the accumulation of large payment arrears). With IMF support, the government is working on a Medium-Term Expenditure Framework which should lead to improved fiscal planning. A sovereign wealth fund was also created in 2012 (the proceeds of 50,000bpd of Angola's 1.8mmbd oil output will be directed into the fund).

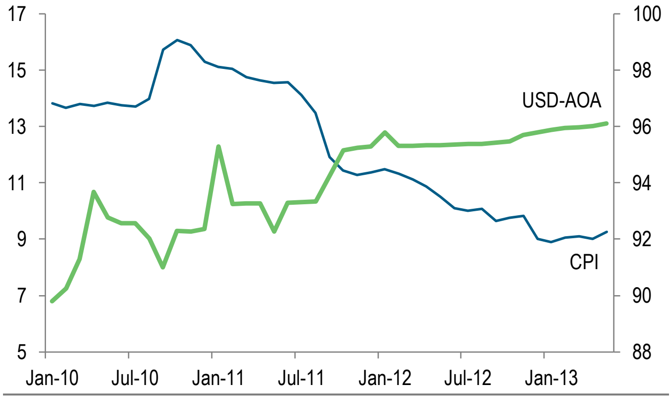
Figure 1: Standard Chartered forecasts – Angola

	2012	2013F	2014F	2015F
GDP (real, % y/y)	8.4	7.0	7.0	7.0
CPI (% y/y)	10.3	9.4	8.5	8.0
Policy rate (%)*	10.25	10.0	9.5	9.0
USD-AOA*	95.5	96.5	97.5	98.0
Current account balance (% GDP)	9.2	6.0	5.0	5.4
Fiscal balance (% GDP)	8.9	1.5	1.2	1.0

*end period; Source: Standard Chartered Research

Figure 2: Exchange rate and inflation

USD - AOA (RHS), CPI % y/y



Sources: IMF, Datastream

Higher spending leads to narrowing surpluses; necessary to meet development objectives

Expansionary fiscal policy to address developmental challenges

The government projects a fiscal deficit this year, given the increase in capital spending to 14.1% of GDP (from 11.2% of GDP in 2012). Sonangol, the state-owned oil company, will no longer engage in quasi-fiscal operations; spending it previously undertook has now been integrated into the budget, explaining the projected deficit. The budget is based on an oil price of USD 96/bbl. Based on our 2013 oil price forecast of USD 109/bbl and the fact that investment spending might undershoot its target, a budget surplus is still likely in 2013, albeit narrower.

The planned increase in spending highlights the fact that the authorities want to address Angola's development needs and also try to improve social indicators (social spending represents more than one-third of total spending).

On the spending side, energy subsidies accounted for 6.5% of GDP in 2012. An increase in electricity tariffs of 10-15% is being considered (the last increase was in 2006) but the larger subsidies relate to fuel. While these are under review, any adjustment in the fuel subsidy (fuel prices were increased in 2010) is unlikely in the short term, given that this could trigger popular discontent and add to inflationary pressures.

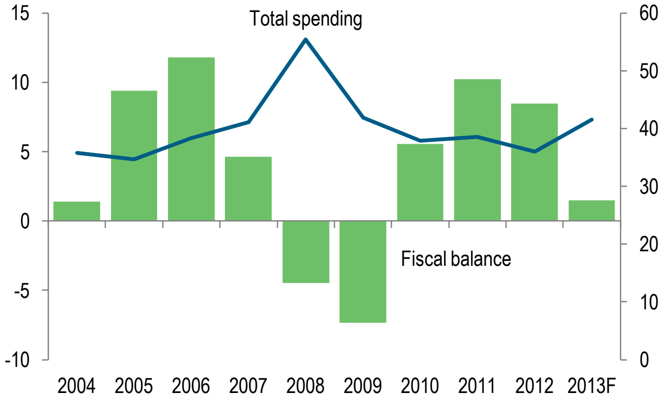
On the external front, **the current account (9% of GDP in 2012) should narrow but remain in surplus this year**, despite a boom in imports. FX reserves increased to USD 35bn in April, which represents more than six months of import cover, a more comfortable level than for many oil-producing countries in Africa. In this context, exchange rate stability should prevail, helping to keep inflation in single-digit territory.

Earlier this year, as we mentioned in our March Regional Focus, the government announced its intention to issue a eurobond. However, market conditions are now less favourable and given that the government is not in urgent need of external financing, it remains to be seen whether this goes ahead.

Overall, we remain positive on Angola's economic outlook, as growth is robust and the country's balance sheet remains solid. While the fiscal surplus will shrink significantly this year on the back of higher spending, this should stimulate growth and help reduce potential social tensions.

Figure 3: Public finances

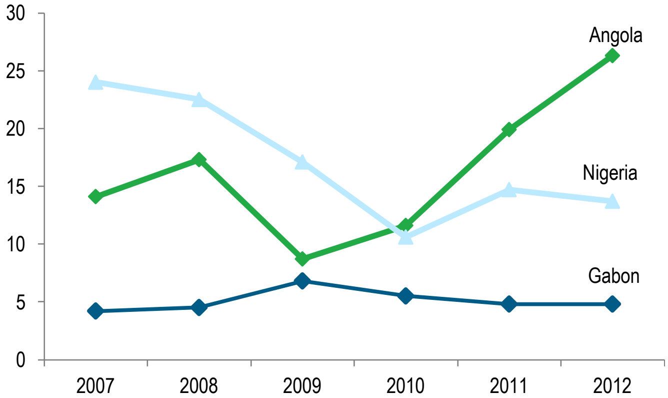
Fiscal balance and spending, % of GDP



Source: IMF

Figure 4: Government deposits

% of GDP



Source: Fitch Ratings

Cote d'Ivoire – Strong momentum continues

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Ongoing economic revival

Strong confidence

There is strong confidence that stability has returned and that the economy is moving forward

The planned return of the African Development Bank's (AfDB's) headquarters to Abidjan, announced during its recent annual meeting held in Morocco, is a significant positive for the Ivorian outlook. The AfDB had relocated to Tunis 10 years ago following the outbreak of civil war in Cote d'Ivoire. Its return is seen as a symbol of the post-war stability achieved by Cote d'Ivoire. The economy stands to benefit in terms of the positive impact on the construction and services sectors and employment. It also helps re-establish Cote d'Ivoire's weight regionally and, importantly, highlights growing confidence that peace and stability have definitively returned to the country.

International donors continue to provide strong support; this will allow the government to increase public investment, underpinning the economic revival. The government can also tap new sources of funding, notably from China to finance the Soubre Dam project; and the government is also seeking an increase in the IMF's non-concessional ceiling (under an Extended Credit Facilities programme) to USD 800mn (it is currently USD 100mn) in order to fund several infrastructure projects.

Most indicators point to strong economic growth

As we have noted previously (see Africa Regional Focus March 2013), **rising public investment has boosted growth**. Private investment, notably foreign investment (FDI reached USD 450mn in 2012 compared with USD 270mn in 2011), has also increased, which should make the economic recovery more sustainable. Credit growth has been rebounding but remains quite modest, at 15.5% y/y in March 2013. Financial intermediation is still low in Cote d'Ivoire (credit to the private sector stands at only 16% of GDP). Cocoa production has been resilient, despite initial weather-related concerns, and should not hamper economic growth. Oil production has declined in recent years but we expect it to increase in the medium term, providing a further boost to the economy.

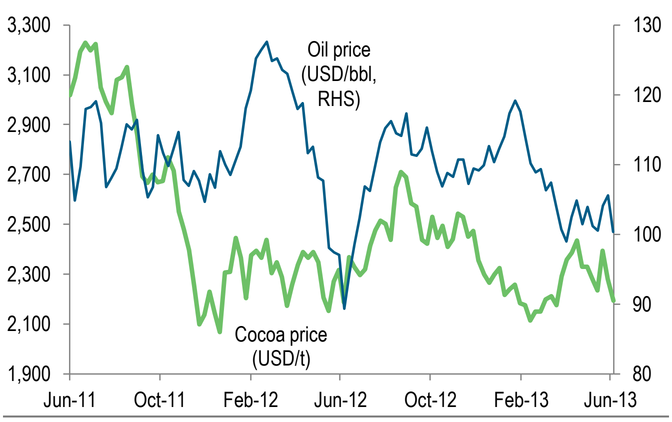
The rise in imports is evidence of the economic revival, particularly the increase in capital goods imports for several infrastructure projects. As a result, Cote d'Ivoire, which has traditionally run a current account surplus, ran a 1.8% deficit in 2012; this is likely to persist in 2013.

Figure 1: Standard Chartered forecasts – Cote d'Ivoire

	2012	2013F	2014F	2015F
GDP (real, % y/y)	9.8	8.0	7.5	7.5
CPI (% y/y)	1.3	3.2	2.5	2.5
Policy rate (%)*	4.0	3.75	3.75	4.0
USD-XOF*	511	505	517	538
Current account balance (% GDP)	-1.8	-2.5	-3.0	-3.0
Fiscal balance (% GDP)	-3.5	-3.0	-3.0	-3.0

*end period; Source: Standard Chartered Research

Figure 2: A fall in commodity prices would be negative
USD



Source: Datastream

Public finances remain challenging but are improving; the outlook is underpinned by strong international support

Budget situation continues to improve

Thanks to strong economic growth, public finances have improved. The 2012 budget deficit was better than initially expected at 3.5% of GDP (compared with an initial government target of 4.3%). For 2013, the budget targets a deficit of 3.2% of GDP, but spending will remain pressured by the need to upgrade infrastructure and by security spending. Energy subsidies, a traditional burden for public finances, should decline somewhat this year as an automatic price adjustment has been in place since April. The government continues to rely heavily on the regional debt market, having issued XOF 258bn so far this year (around USD 519mn), which represents roughly half of the total amount that it expects to issue in 2013.

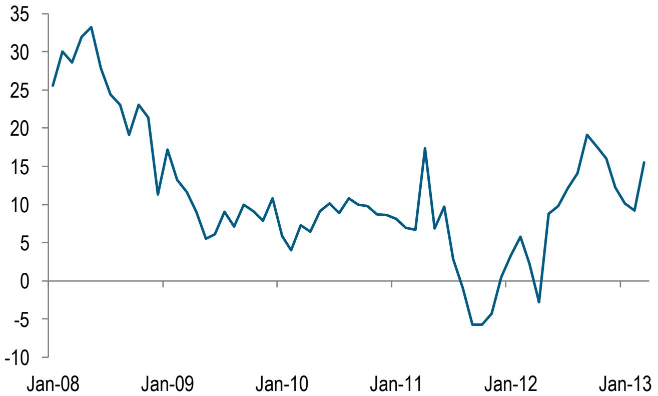
While Cote d'Ivoire's dynamics will be mainly driven by domestic factors, the uncertain global outlook also presents risks. As a large commodity exporter, Cote d'Ivoire could be negatively affected by a decline in international oil and cocoa prices (both represent one-quarter of fiscal revenues). However, risks linked to the global environment should be mitigated by the fact that the economy should continue to be driven by post-conflict dynamics (GDP growth should remain above 7% in the next few years). Also, despite economic difficulties in developed countries, international support for Cote d'Ivoire looks set to remain strong (international donors have already committed USD 8.7bn for 2013-15).

Political concerns are easing

On the political front, stability is likely to prevail despite ongoing issues of army reform, reconciliation and security. The number of violent incidents has declined, since most pro-Gbagbo supporters who allegedly promoted them last year have been arrested. The trial of former president Laurent Gbagbo has been postponed, as the International Criminal Court said prosecutors need more time to build a case, and it is now scheduled for November. While we do not think Gbagbo's trial will have any significant impact on domestic stability, its postponement will probably help reduce political noise in the short term.

Figure 3: Credit growth is recovering

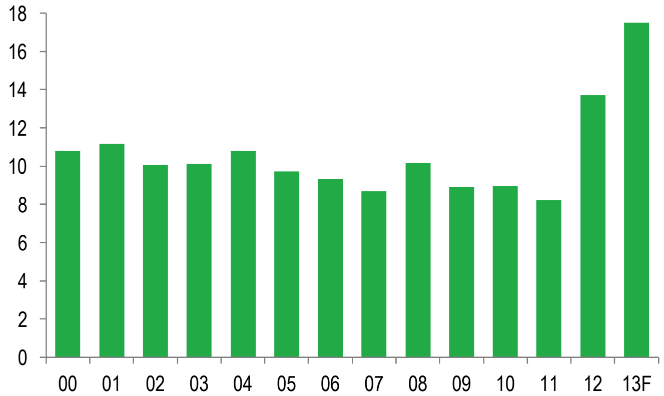
% of GDP



Source: IMF IFS

Figure 4: Increasing investment

% of GDP



Source: IMF

Gabon – Spending more, growing more

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Higher public investment drives growth

Higher public investment has led to fiscal deficits but has boosted economic growth

Higher investment transforms Gabon's growth prospects

Gabon's economic performance remains strong. GDP growth reached 6.2% in 2012 and strong economic growth rates should continue in the medium term, driven mainly by non-oil sector momentum (the non-oil sector accounts for 50% of GDP). Historically, the oil sector has driven growth, but oil production has been flat in recent years and is likely to remain around 240,000 barrels per day in the near term. Public investment (focused on energy and transport infrastructure) should increase this year to EUR 1.8bn from EUR 1.5bn in 2012.

Capital spending has picked up significantly since 2009 and reached 11% of GDP in 2012; this explains the higher growth trajectory. During the previous decade, Gabon posted poor growth (averaging only 1% from 2000-10), underperforming the rest of Africa. Now it is among the region's fastest-growing economies, with average growth of 6.7% in the last three years. Higher public investment has been a game changer.

Less comfortable public finances

As a result of higher spending, Gabon's surpluses have been shrinking and in 2013 Gabon is likely to post its first budget deficit of the last 15 years. Given the challenging global outlook, the government intends to review the 2013 budget and control the wage bill that accounts for 27% of expenditure. It intends to limit the wage bill by slowing public-sector recruitment and staff replacements rather than cutting salaries, which would be more politically sensitive.

Historically, Gabon has been characterised by a low level of savings, and given the projected deficits and rising spending, this will not be reversed anytime soon. Government deposits are estimated at XAF 250bn or 5% of GDP, representing only around 2.5 months of spending. This is a key concern, but there is flexibility on the spending side.

Any reduction in the oil price would lead to government spending cuts, as was the case in 2009. Capital spending represents 42.7% of total spending and the government could easily reduce that to avoid a severe budgetary crisis in the event

Figure 1: Standard Chartered forecasts – Gabon

	2012	2013F	2014F	2015F
GDP (real, % y/y)	6.2	6.0	6.5	6.5
CPI (% y/y)	3.0	3.0	3.0	3.0
Policy rate (%)*	4.0	4.0	4.0	4.25
USD-XAF*	511	505	517	538
Current account balance (% GDP)	12.6	11.0	8.0	5.0
Fiscal balance (% GDP)	0.4	-1.5	-1.7	-2.0

*end period; Source: Standard Chartered Research

Figure 2: Gabon is finally catching up
Gabon vs. SSA, GDP, % y/y

Source: IMF

of lower oil prices. Despite the establishment of a sovereign wealth fund, the amount saved is relatively low at present. The current account surplus should remain in double digits, driven by a strong trade surplus. FX reserves have been increasing, but the rise has not been that impressive and Gabon's FX reserves are lower than in many other countries, at 3.5 months of import cover (the lowest among BB- rated countries), but the CFA franc-zone membership mitigates liquidity risk. Debt levels should rise to 19% this year, from 16.3% in 2012, according to the Ministry of Finance; this remains a manageable level.

Challenging outlook but fundamentals remain strong

Some key credit metrics, such as the fiscal balance, look likely to deteriorate somewhat. As a result, Fitch revised its outlook to stable from positive in April, while S&P has kept its negative outlook since September 2012. The outlook is certainly more challenging but fundamentals remain strong. Fiscal deficits are leading to higher growth and despite low savings Gabon has the capacity to adjust to a fall in oil prices; such a move would impact growth but not the government's ability (or willingness) to repay its debt.

Fears of growing 'assertiveness' are overdone

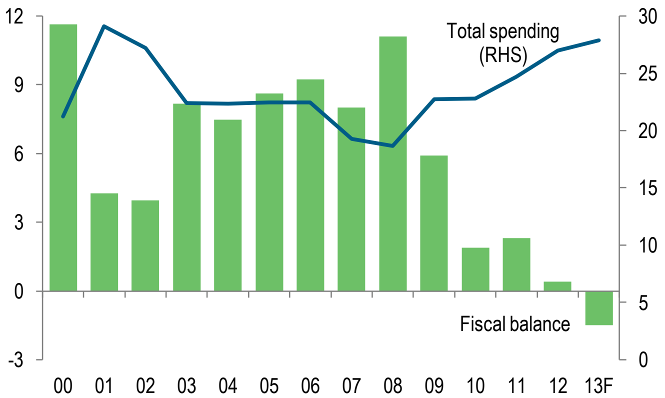
Gabon is unlikely to change its attitude towards foreign investors in general but seems to have become more wary of China

Recent news headlines suggest that Gabon's government is adopting a tougher stance on international oil companies following a dispute with the subsidiary of a Chinese oil company, in which the government threatened to seize the company's assets. We do not view this as growing resource nationalism, especially as the main operators in the sector are not being targeted. It seems more of an isolated dispute with a company that allegedly failed to comply with local regulations.

Gabon's business environment has traditionally been considered quite difficult, and in the past there have been other disputes. In line with many others countries, the government will probably try to maximise revenues from the oil sector but we do not think that Gabon is becoming more hostile to foreign investors. While relations with China are important, as Chinese companies are involved in a wide-range of projects, there appears to be growing discontent towards some Chinese companies (there has also been disagreement on the Belinga iron ore project). It is worth noting that foreign investment has been increasing recently, mostly outside the oil sector, in line with diversification efforts; we do not think these disputes will deter future foreign investment.

Figure 3: A more expansionary fiscal policy

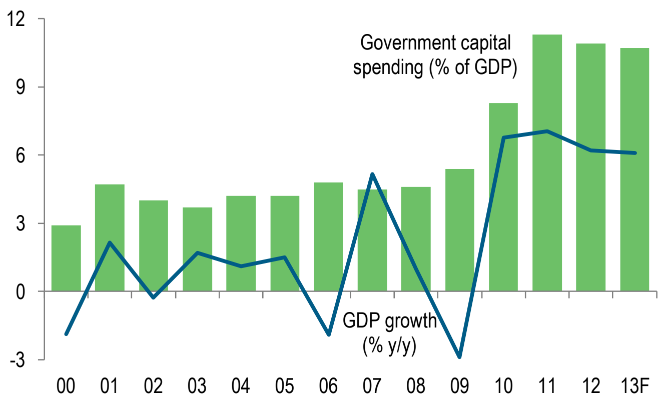
% of GDP



Source: IMF

Figure 4: Higher public investment leads to higher growth

%



Source: IMF

Ghana – Challenges ahead

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Despite attempts at fiscal consolidation, challenges persist

Ghana's economy faces challenges despite expected GDP growth of c.8% in 2013, reflecting a recovery in oil output

Ghana's economy faces a number of threats, both external and domestic. Falling prices for key commodity exports, and a substantial trade deficit threaten FX stability. Ghana has seen a rapid build-up in domestic debt following last year's outsized fiscal deficit of 11.8%. With deficit financing concentrated at the short end of the curve, the cost of servicing its domestic debt now exceeds the growth rate of nominal GDP. The Bank of Ghana's (BoG's) composite indicator of economic activity points to a slowdown in momentum in the non-oil economy. Much must still be done to achieve fiscal consolidation, but rising inflation will require near-term tightening. **We change our forecast for the BoG's prime rate, and now anticipate another 200bps of tightening this year,** to 18%, although this should allow for substantial easing next year as inflation stabilises.

The Bank of Ghana's composite indicator points to a slowdown in non-oil growth; business and consumer confidence are down from previously elevated levels

Ghana's robust headline growth rate of c.8% in 2013 is likely to mask a slowdown in the non-oil economy. Recovery in oil production following technical difficulties in 2012 will be a key driver of overall growth. However, the impact of fiscal consolidation measures (the full fuel price deregulation already seen and still-anticipated utility subsidy removal), additional measures to aid fiscal stabilisation, and energy-sector disruptions are all expected to dampen near-term growth prospects in the non-oil economy. The latest survey data indicates that both consumer and business confidence have dipped, albeit from previously elevated levels. Ghana's business confidence index declined to 99.0 in March 2013, from 104.1 in December 2012. Consumer confidence also fell to 96.1 in April, from 105.0 in January 2013.

Offsetting these influences is still-considerable consumption momentum from last year's above-inflation public-sector salary hikes. In contrast with the IMF, we do not believe that modestly higher nominal interest rates will have much impact on private-sector lending in Ghana. This is mainly because of our doubts about the strength of the monetary policy transmission. While real private-sector credit growth slowed to 17.6% y/y in March 2013, from 32.9% in March 2012, much of this may be attributable to the high base. In our view, a greater threat is Ghana's rising domestic debt burden. Unless debt-service costs are reined in, they are likely to squeeze future fiscal expenditure. A slowdown in spending would have more severe economic consequences.

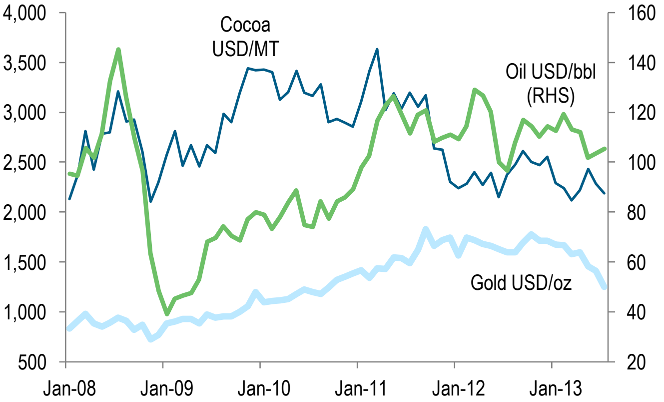
Figure 1: Standard Chartered forecasts – Ghana

	2012	2013F	2014F
GDP (real % y/y)	7.9	8.0	7.2
CPI (% annual average)	9.2	12.4	11.0
Policy rate (%)*	15	18	13
USD-GHS*	1.90	2.10	2.24
Current account balance (% GDP)	-12.2	-11.9	-11.0
Fiscal balance (% GDP)	-11.8	-10.5	-9.0

*end period; Source: Standard Chartered Research

Figure 2: Ghana at risk from weaker commodity prices

Gold –USD/oz, cocoa – USD/mt, oil – USD/bbl



Sources: Datastream, Standard Chartered Research

Ghana must urgently tackle debt-service costs

Politically contentious economic reforms, removing subsidies and reintroducing fiscal stabilisation levies, are underway

Despite a deliberately slow pace of medium-term fiscal consolidation in order to safeguard growth, the authorities have demonstrated resolve in tackling politically contentious reforms. Last year's deficit overrun, to 11.8% of GDP, created legacy problems, not least because of persistently high debt-service costs. A combination of accelerated public-sector pay adjustments (equivalent to 2.7% of GDP), pre-election spending overruns, revenue disappointment and higher debt-service costs were responsible for 2012's fiscal slippage. In 2013, the plan is to reduce the deficit to 9% of GDP, but there are already problems.

Ghana must tackle its debt-service cost; this is thought to exceed the nominal rate of GDP growth

Data for the first four months of 2013 reveals a budget deficit of 3.8% of GDP, against a target of 3% (with revenue and grants totalling only 7.1% of GDP versus spending of 10.9%). While traditionally weak revenue momentum in Q1 might be blamed, there is little room for further slippage. Worryingly, domestic interest rates in Q1 were above budget, resulting in debt-service payment overruns of 46.2% relative to 2013 budget assumptions. Payments on wages and salaries between January and May also appear to have exceeded budget assumptions by c.22.4%. Since then, fuel prices have been fully deregulated. Utility subsidy reductions are believed to be imminent, and in early July parliament approved the reintroduction of a fiscal stabilisation levy, as well as a special import levy. The fiscal stabilisation levy, a 5% tax on the profits of selected companies for a period of 18 months, should plug a GHS 88mn shortfall in Ghana's finances. The special import levy should yield an additional GHS 208mn of revenue in H2-2013.

Eurobond issuance will help, but there is an urgent need to extend the maturity of domestic borrowing

Ghana plans to issue a second eurobond in 2013, to finance capital expenditure and partly refinance public debt, reducing more expensive borrowing. With a public debt-to-GDP ratio estimated at 49.8% (BoG projections are lower), split between USD 9.5bn of foreign debt and USD 10.65bn of domestic debt at the end of March, Ghana needs to act fast to avert worsening debt ratios. It may be spending more on public-sector pay than it can afford. Despite enacting difficult reforms, if there is a slowdown in the sectors that contribute meaningfully to fiscal revenue while debt-service costs remain high, Ghana may still overshoot its fiscal deficit target. **Extending the domestic yield curve to reduce overdependence on very short-term, expensive financing of the fiscal deficit would be a relatively easy win.**

Despite limits on monetary financing of the fiscal deficit, inflation looks set to rise. Ghana's rebased and reweighted CPI rose 11.1% y/y in May, from around 10% at the start of the year. Curiously, although the new reweighting reduces the contribution of food and increases the weight of transport (to 7.2% from 6.2% previously), February's sizeable fuel price adjustment appears to have had little impact on the new m/m CPI data. Nonetheless, with the weight given to 'housing, electricity, water and gas' increasing to 9.5% of the basket from 7% previously, planned utility price adjustments should have a proportionately greater impact on CPI. (The new rebased CPI, where data is still provisional, will be published alongside the old CPI through to December 2013.) The Ghanaian cedi remains under pressure and inflation expectations are elevated. Full cost recovery for fuel and utilities will increase inflationary pressure. With a less favourable base from 2012, we forecast that inflation may rise temporarily, to c.15-16% by end-2013, even as the non-oil economy loses momentum. In line with the BoG's price stability mandate, and alongside efforts to improve the transmission of monetary policy, we believe that this could mean another 200bps of tightening in the prime rate, and forecast hikes of 100bps each in September and November 2013.

Mauritius – Growth remains sluggish

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No sign of faster growth yet

Data released so far in 2013 suggests that GDP growth will remain low at c.3.5%

Increased concern that 2013 will be another year of slow growth for Mauritius. Despite hopes of accelerating growth, real GDP is likely to remain at c.3.5% in 2013, driven by ICT and financial services growth. In Q1 growth picked up to 3.7% y/y but this should moderate in the rest of the year. In 2012, growth dropped slightly to 3.3% from 3.5% in 2011. Very real downside risks stem from slow growth in Europe. Those sectors that are most susceptible to the slowdown in economic activity in the euro area will continue to be the main drag on growth. Tourism, manufacturing and the sugar industry all registered slow growth in 2012, and recent data releases show that this trend continues. Despite the subdued short-term outlook, longer-term it should be more positive as the euro-area economy begins to recover from 2014.

Q1 data suggests that the tourist industry will grow slowly again in 2013. In 2012 the sector did not grow at all, but it should pick up slightly in 2013. In Q1-2013, although tourist arrivals were marginally higher (+1% y/y), revenue was down by 21% as hotel occupancy fell. The majority of tourists arrive from Europe, and with the economic outlook in the region still weak, the tourism sector is likely to continue to grow slowly in 2013. In May, Statistics Mauritius lowered its 2013 tourist arrivals forecast by 10,000 given slow activity YTD.

Unemployment is likely to average 8.3% in 2013 – the highest rate since 2007. In Q1-2013 the unemployment rate reached 8.7%, compared with 7.8% in Q4-2012 and 8% in Q1-2012. A slowdown in both the tourism and manufacturing sectors was the main contributory factor. Structural reform will be needed over the medium term to address this issue. The unemployment rate remains highest among low-skilled youths and women.

The BoM is unlikely to cut the repo rate again this year following a surprise cut in June 2013, given upside inflation risks

The Bank of Mauritius (BoM) cut its key repo rate by 25bps to 4.65% in June on the back of growth concerns. It also lowered its growth-forecast range to 3.2-3.7% (from 3.4-3.9%). At the June meeting, concerns about a growth slowdown outweighed those over inflationary pressures. The monetary policy board noted slow growth in key export sectors despite efforts to diversify economic partners, plus a contraction in construction-sector activity and a slowdown in domestic investment. However, the decision was not unanimous. BoM Governor, Rundheersing Bheenick, proposed a 25bps rate increase, citing inflation concerns. Further cuts to the repo rate are unlikely in 2013, given concerns over rising inflationary pressures towards year-end.

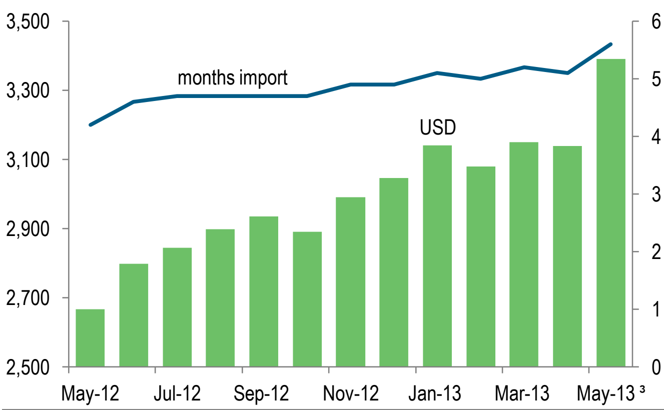
Figure 1: Standard Chartered forecasts – Mauritius

	2012	2013F	2014F
GDP (real % y/y)	3.3	3.5	4.2
CPI (% annual average)	4.8	4.4	4.5
Policy rate (%)*	4.9	4.25	4.5
USD-MUR*	30.6	31.8	31.0
Current account balance (% GDP)	-10.3	-10.2	-9.8
Fiscal balance (% GDP)	-1.8	-2.2	-2.0

*end period; Source: Standard Chartered Research

Figure 2: FX reserves accumulation on track

USD mn LHS, months import cover RHS



Sources: BoM, Standard Chartered Research

Inflation will likely reach close to 6% y/y by the end of 2013

Inflation dropped to 3.9% at the end of 2012 and remained low in Q1-2013. It is likely to accelerate towards the end of 2013 to reach close to 6%, largely as a result of public-sector wage increases, as well as any feed-through from a weaker Mauritian rupee (MUR). Although the MUR remains volatile, the general depreciation trend continues. Given renewed inflationary pressures towards year-end, the BoM will likely continue to intervene in the FX market to prevent a rapid depreciation of the MUR, and the subsequent inflationary impact this would have. The IMF estimates that Mauritius' real effective exchange rate (REER) is now broadly in line with fundamentals following corrections to REER overvaluation during 2012.

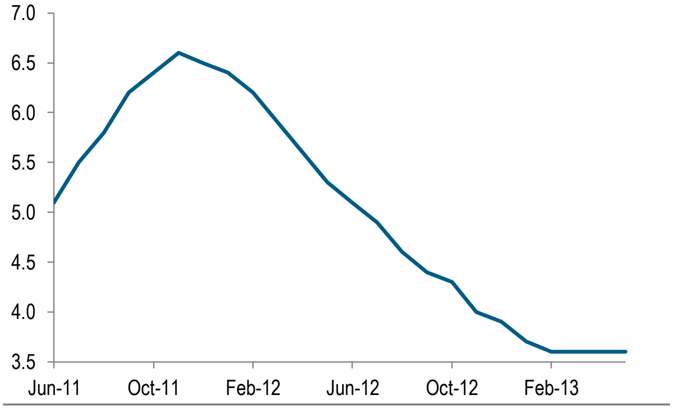
The BoM continues to build up FX reserves

Plans to rebuild external buffers to protect against external vulnerabilities are back on track. The BoM continues to intervene in the FX market. The FX reserve target of 6 months of import cover is within reach: reserves increased significantly to 5.6 months of cover in May 2013, after dropping to just 5.1 months in April, following BoM action to offset lower gold prices. The 2013 current account deficit should remain around 10% of GDP, following a 10.3% deficit in 2012. The trade deficit narrowed in Q1-2013 compared with a year earlier. This is largely as a result of increased exports of ships' stores and bunkers, combined with slower import growth because of lower growth in certain domestic industries as large projects such as the airport construction come to an end.

Mauritius' 2012 budget deficit was better than expected at 1.8%. In 2013 it should remain below 2%, although public-sector wage increases will add to expenditure. Finance Minister, Xavier Luc Duval, has stated that the government is targeting a balanced budget within the next five years as tax collection is projected to increase rapidly, combined with greater control over recurrent expenditure.

Figure 3: Inflationary pressure have eased, but will return

CPI, % y/y



Sources: BoM, Standard Chartered Research

Figure 4: MUR remains volatile

MUR-USD

Sources: Bloomberg, Standard Chartered Research

Namibia – Positive outlook

External vulnerabilities remain

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Growth should remain strong in 2013

High government spending on mining-sector investment projects should continue to drive growth in 2013

GDP growth picked up to 5% in 2012, as mining exports were less affected by the economic slowdown in key markets than had initially been expected. Growth is likely to remain strong at around 4.5% in 2013, although this is significantly below the 6.1% target in Namibia's Third National Development Plan. High government spending combined with low interest rates will remain the key growth drivers this year. However, diamond and uranium export growth is likely to slow in 2013 as a result of lower prices and slower global demand. In the medium term, growth should exceed 5%, as mining-sector investment continues and projects such as the Husab uranium mine and Kudu offshore gas field are completed and production begins. The services sector, which accounts for more than half of GDP, has benefited from government investment in tourism, housing and transport. Lower international commodity prices or a drop in global demand for commodities remain the main downside risks for the economy in the short term.

Expansionary fiscal policy will continue

The fiscal deficit is likely to widen in 2013 as SACU receipts moderate

Expenditure has increased as a result of the Targeted Intervention Programme for Employment and Economic Growth (TIPEEG), launched in 2011 and aimed at boosting economic growth and employment. As a result public debt rose to c.27% of GDP in 2012 compared with 15% in 2011, prior to the issuance of Namibia's USD 500mn eurobond; this was issued to help finance higher spending as a result of TIPEEG. Despite this increase, current debt levels are sustainable. In 2012, higher-than-expected South African Customs Union (SACU) receipts (which typically account for 35% of fiscal revenue) helped bring the deficit down to 2.8%. It is likely to widen to 6.4% in 2013, as spending remains high and SACU receipts are likely to moderate.

Namibia remains vulnerable to any deterioration in South African inflation

Namibian inflation is likely to face renewed upward pressure from May onwards. It moderated in the first four months of 2013, reaching 6.1% in April 2013 from 7.1% in October 2012. However, the majority of Namibia's imports are sourced from South Africa (c.70% in 2012). As a result, inflation trends there (we expect

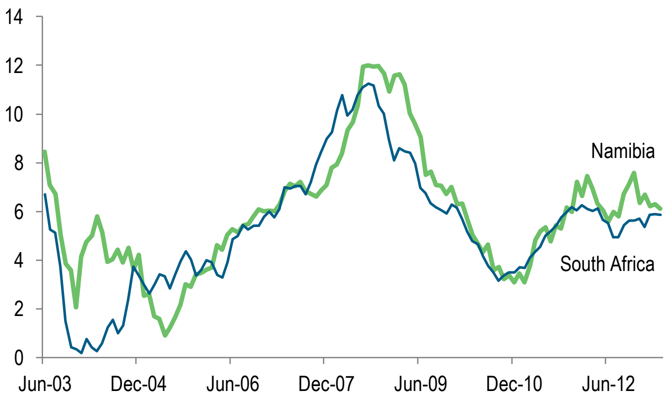
Figure 1: Standard Chartered forecasts – Namibia

	2012	2013F	2014F
GDP (real % y/y)	5.0	4.5	4.8
CPI (% annual average)	6.5	6.4	5.5
Policy rate (%)*	5.5	5.5	6.0
USD-NAD*	8.48	10.2	10.3
Current account balance (% GDP)	-0.7	-1.8	-2.0
Fiscal balance (% GDP)	-2.8	-6.4	-5.2

*end period; Source: Standard Chartered Research

Figure 2: Namibian inflation tracks South Africa's

CPI, % y/y



Sources: Bloomberg, Standard Chartered Research

inflation to peak above 6% in the middle of 2013) will continue to influence Namibian inflation. Inflation in Namibia will likely remain above that in South Africa given specific pressures, such as a 12% increase in electricity prices announced in March 2013.

ZAR depreciation is an additional risk

Inflationary pressures in South Africa and the direct feedthrough of a weaker ZAR will increase pressure on Namibian inflation this year

South African rand (ZAR) depreciation will add to Namibian inflation risks, given the Namibian dollar's (NAD) peg to the ZAR. As the NAD weakens, the subsequent increase in import costs combined with expectations of slower growth in mining exports this year will likely see the trade deficit widen. It will continue to do so as imports needed for mining-sector projects increase, and exports continue to moderate as a result of lower demand for uranium and diamonds. Uranium and diamonds accounted for 29% of total exports in 2012. The trade deficit is likely to be the key driver of a larger current account deficit this year. We forecast that it will expand to 1.8% in 2013 compared with 0.7% last year. The current account is likely to remain in deficit in the short term, following the first deficit in years in 2011, due to lower SACU receipts and exports. The completion of mining-sector projects should help reduce the deficit.

Maintaining an adequate level of FX reserves will remain the Bank of Namibia's primary target given the NAD-ZAR peg. FX reserves dropped in the first few months of 2013, but the central bank considers current levels to be adequate, at around three months import cover. The repo rate is likely to remain low this year given slowing economic growth. Interest rates continue to track the South African repo rate. At the June 2013 meeting, the repo rate was held at 5.5%, 50bps higher than the South African Reserve Bank's repo rate.

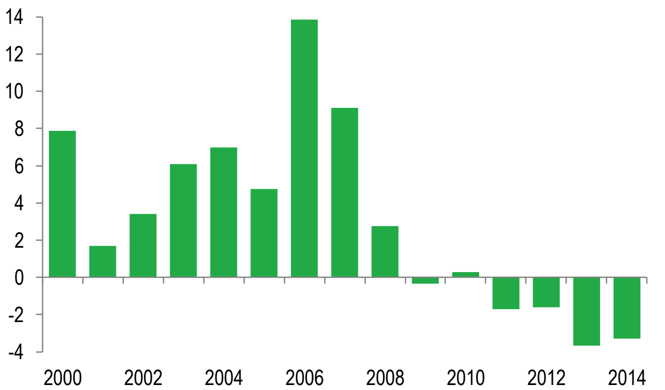
SWAPO still dominates the political scene

The political outlook remains stable with Hage Geingob likely to succeed the current President Pohamba in November 2014 elections

Hage Geingob was re-elected as the vice president of the ruling South West Africa People's Organisation (SWAPO) at the party's elective congress in November 2012. He will be the party's candidate in the November 2014 presidential elections. SWAPO should continue to dominate the political scene, with Geingob succeeding current President Hifikepunye Pohamba in 2014. At the last election President Pohamba won 75% of the vote, although voter turnout was only 38%.

Figure 3: The current account deficit has expanded

% of GDP



Sources: BoN, Standard Chartered Research

Figure 4: NAD depreciation adds to inflationary pressure

USD-NAD

Sources: Bloomberg, Standard Chartered Research

Nigeria – The political cycle and policy

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Spending scrutiny suggests MPR on hold in 2013

Growth is slowing, but we expect a cyclical recovery as pre-election spending starts to increase

Nigerian growth is slowing. Q1-2013 real GDP growth was 6.56% y/y versus 6.99% in Q4-2012, dragged down by both the oil and non-oil sectors. Illegal oil bunkering and pipeline vandalism resulted in the oil sector contracting by 0.54% y/y in Q1. The non-oil economy grew at 7.9%, although growth in key sectors was noticeably softer. Telecoms, which typically sees growth rates of more than 30% each quarter, slowed to 24.5%, reflecting increased competition and a relative maturing of the sector. Construction was a relative bright spot, growing 15.66% y/y, possibly reflecting the impact of increased development expenditure. Manufacturing also grew by a healthy 8.4%, but its sectoral share is small. Key growth risks going forward stem from the security situation in the north, as well as further disruption to oil production. Although the economy is likely to receive a cyclical boost from pre-election spending, ongoing structural reform will be required to deliver the 7%-type growth rates to which Nigeria has become accustomed. Near-term, the risk is that growth slips to c.6%. The long-awaited rebasing of Nigeria's GDP – which should provide us with more accurate sectoral shares – is not expected until 2014, at least.

Inflation is likely to remain in single digits this year, but success was hard-won; risks to the NGN will keep the CBN on hold until the end of 2013; we forecast more tightening in 2014

Inflation has decelerated, reflecting tight policy; the CBN warns that it might tighten further. Nigerian inflation has slowed to high single digits, reflecting a high base in 2012, but also the impact of tight policy – as evidenced by the improvement in m/m inflation (Figure 2). We expect inflation to remain in single digits until the end of 2013, allowing the monetary policy rate (MPR) to remain unchanged at 12% this year. Although many had predicted a greater risk of easing following the achievement of single-digit inflation, recent pressure on the Nigerian naira (NGN) – given market expectations of a tapering of QE – as well as concern about Nigeria's political cycle and spending pressures, will likely keep the monetary policy committee on hold.

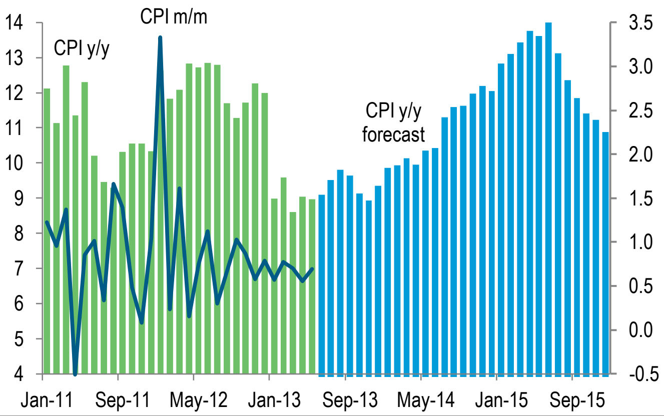
There is a risk that elections, due in 2015, are brought forward, allowing for any legal disputes to election results to be settled ahead of a May 2015 transition. If this is the case, spending may rise meaningfully ahead of party primaries which would be held in early H2-2014. **Given anticipated pressure on future inflation, we forecast a 100bps rate hike in Q1-2014, followed by hikes of 50bps each in Q3 and Q4 2014, with the MPR raised to 14% by end-2014**. Pressure on the NGN will determine the extent of tightening that is required.

Figure 1: Standard Chartered forecasts – Nigeria

	2012	2013F	2014F
GDP (real % y/y)	6.6	6.6	7.4
CPI (% annual average)	12.2	9.2	11.0
Policy rate (%)*	12	12	14
USD-NGN*	156	159.8	163
Current account balance (% GDP)	4.7	4.0	3.6
Fiscal balance (% GDP)	-2.85	-2.2	-3.3

*end period; Source: Standard Chartered Research

Figure 2: Inflation slows, but watch the political cycle
CPI m/m, y/y and forecasts



Sources: NBS, Standard Chartered Research

Oil earnings are under pressure but Nigeria's willingness to dip into oil savings is the key reason why deficit projections remain modest

Weaker oil output relative to ambitious budget targets risks fiscal deterioration, with Nigeria dipping into its oil savings. With only modest spending increases envisaged in 2013, a budget deficit of 2.17% was initially forecast. However, oil production, reportedly averaging 2.1-2.2 million barrels per day (mmbd), has fallen short of the 2.53mmbd assumed in the 2013 budget. In June, output may have hit a low of 1.9mmbd. This has necessitated more frequent augmentation of revenue from Nigeria's Excess Crude Account (ECA), the 'unallocated' earnings belonging to the three tiers of the Federation. Dipping into oil savings to finance spending may result in a narrower budget deficit for 2013. In March, officials projected a 1.85% deficit for the year. However, we think the following risks need to be monitored:

There are many risks to the outlook: spending on fuel subsidies and security are potential sources of upside pressure; even improved budget implementation is viewed with some concern; FAAC allocations suggest the potential beginning of a political cycle

(1) The 2013 budget allocates NGN 971bn for fuel subsidy payments (2012: NGN 888bn). With progress on subsidy reforms unlikely ahead of elections, this may rise.

(2) Reports suggest a supplementary budget has been requested. It is unclear if this will happen before September 2013, when the 2014 budget is read, raising the risk that spending will be influenced by Nigeria's political cycle.

(3) Expectations of QE tapering may test Nigeria's willingness to dip into its oil savings to finance spending. Short-lived portfolio outflows were comfortably accommodated by the CBN, without triggering significant pressure on FX reserves. But ECA withdrawals, even if they do not deplete FX reserves directly, may still fuel FX demand, questioning the sustainability of the current NGN band.

(4) Increased military spending following the state of emergency in the north east should be met by a contingency reserve. Further escalation may pressure spending plans.

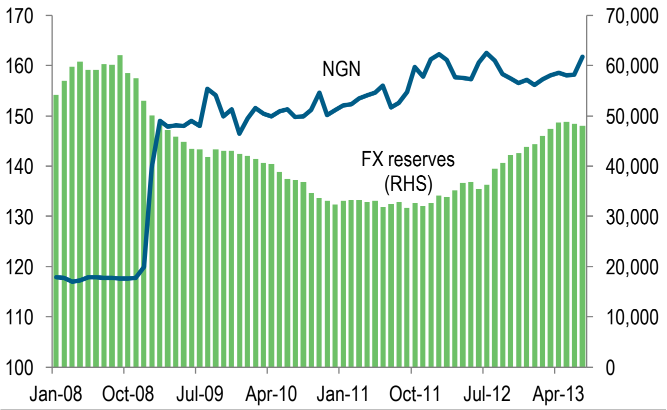
(5) Even improved budget implementation is a source of concern. Commentators are unsure if this reflects more efficient spending, or pressure to spend more. In Q1-2013, government revenue was reportedly 12.6% lower, while spending rose 15%.

(6) Federation Account Allocation Committee allocations in H1-2013 totalled NGN 3.3tn, up 13.74% versus H1-2012, and may be seen as further evidence that Nigeria's political cycle is starting to have more of an influence.

Despite the success of Nigeria's recent eurobond issuance (new 5Y and 10Y bonds were oversubscribed despite suggestions of QE tapering; pricing was more favourable than previously) and a reduced domestic issuance calendar for Q3-2013, concerns persist over the broader fiscal backdrop.

Figure 3: Despite outflows triggered by Fed tapering concerns, FX reserves are holding up – for now

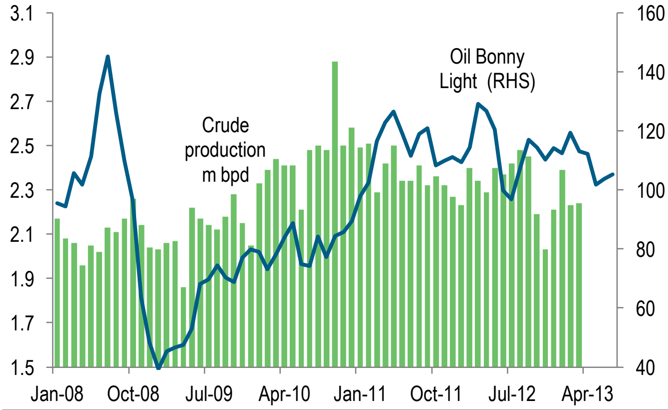
USD-NGN, FX reserves USD mn (RHS)



Sources: Reuters Datastream, Standard Chartered Research

Figure 4: Oil earnings are a source of longer-term concern

Nigeria remains vulnerable to output and price surprises



Sources: Reuters Datastream, CBN, Standard Chartered Research

Senegal – Fiscal restraint, modest growth

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Growth is picking up, but it is likely to remain modest

GDP growth to remain unimpressive

Growth has been weak, averaging only 3.2% over the last five years. GDP growth reached 3.5% in 2012 and should increase to 4% this year. In Q1-2013, it was 3.2% y/y. The primary and tertiary sectors posted positive performances (2.2% and 4.7%, respectively) but the secondary sector was poor (-0.3%), as refining-sector activity declined. Agriculture and services are dynamic, but industry is struggling.

As industry accounts for 20% of GDP, resolving structural issues affecting the sector is key to achieving growth levels more in line with other African countries. On the positive side, electricity production is improving but the situation in the energy sector is not yet optimal. Of particular concern is that higher capital spending has not translated into a higher growth trajectory, which raises the question of public spending efficiency.

A high but narrowing fiscal deficit

Fiscal deficit should narrow, but there are some risks on the revenue side if growth is lower than expected

There has been significant fiscal slippage in recent years. The budget deficit should remain high this year, but should narrow to 5.3% of GDP, from 5.9% in 2012. In 2012, the large fiscal deficit was the result of elections, high subsidies and the impact of the drought in the Sahel; but it would have been even bigger without strong government measures to contain spending. As highlighted by the IMF in its latest review, this is the first time in recent years that the fiscal target has been met, despite the challenging revenue environment. But challenges remain, as weaker-than-expected growth may further constrain fiscal revenue.

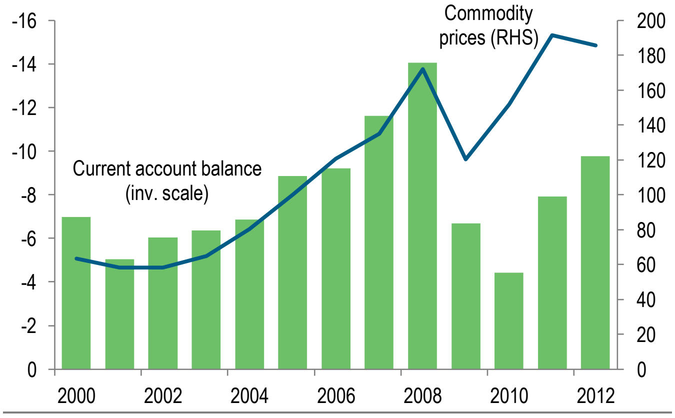
The energy sector affects public finances owing to the weight of subsidies. According to the IMF, energy price subsidies reached XOF 160bn in 2012 (i.e., 2% of GDP and 7.6% of total spending). We understand that the government intends to reduce subsidies significantly this year, as the national electricity company's situation improves thanks to lower technical losses and more efficient power stations. At some point it will be necessary to raise tariffs, but this is a socially sensitive issue and before considering such a move the government wants to improve the quality of the service.

Figure 1: Standard Chartered forecasts – Senegal

	2012	2013F	2014F	2015F
GDP (real, % y/y)	3.5	4.0	4.2	4.5
CPI (% y/y)	1.1	1.5	2.0	2.0
Policy rate (%)*	4.0	3.75	3.75	4.0
USD-XOF*	511	505	517	538
Current account balance (% GDP)	-9.7	-8.5	-8.0	-7.0
Fiscal balance (% GDP)	-5.9	-5.3	-4..5	-4.0

*end period; Source: Standard Chartered Research

Figure 2: Senegal to benefit from lower commodity prices
C/A deficit (% of GDP) vs. commodity prices (index, 2005=100)



Source: ANSD

As a result of higher deficits, debt has increased in recent years (to 45% of GDP in 2012 from 40% in 2011) and should continue to do so this year. The government intends to issue a USD 500mn bond in 2013. But given the current unfavourable market conditions, if it proceeds it is likely to be towards the end of the year. The government will continue to borrow domestically (it has issued the equivalent of USD 410mn of local bonds so far this year) and rely on concessional lending. In previous Regional Focus publications, we have highlighted the important role of international donors (especially France), which have always helped Senegal muddle through difficult times. France has recently committed further support, announcing funding of USD 78mn in 2013-14.

Lower commodity prices would benefit Senegal

The global outlook presents risks for the outlook, but lower commodity prices would benefit Senegal

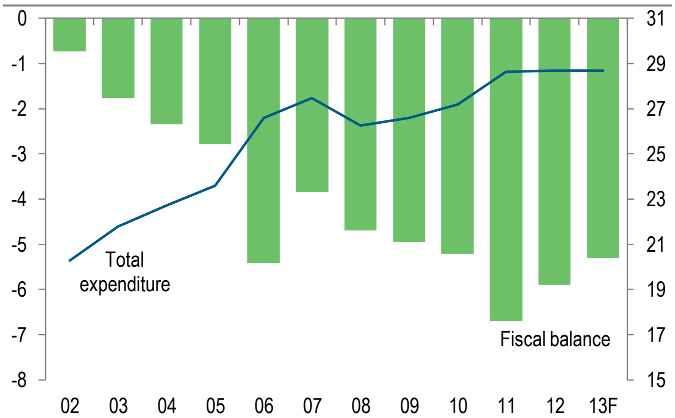
The uncertain global environment remains a risk to Senegal's outlook, notably for remittances, investment and financing flows. But Senegal is among those countries that would benefit from potentially lower commodity prices. Public finances, the external account and inflation would all be positively affected by a decline in commodity prices, especially oil and food prices.

Historically, Senegal runs a high trade deficit (which deteriorated in 2012), given its weak export base, and high oil and food imports (20.7% and 18.6% of total imports, respectively). Lower subsidies should provide some relief to public finances. (Electricity subsidies are affected by oil prices as most power generation uses fuel.) Also, last year fiscal exemptions applied to certain food products to limit the cost of living; this also weighed on public finances. While inflation is traditionally lower in Senegal than in many other African countries given the CFA franc's peg to the euro, the CPI basket is dominated by food, so lower food prices would also help the inflation outlook.

The economic outlook is not particularly bright for Senegal, but some improvements in public finances are likely following years of deterioration. In addition, the energy sector has also been improving, which should benefit both public finances and growth. Strong international support should allow Senegal to navigate through any economic turbulence.

Figure 3: Moderation in spending to narrow the fiscal deficit

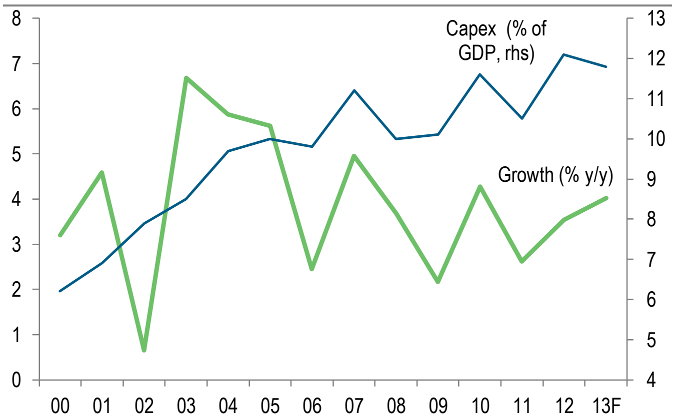
% of GDP



Source: IMF

Figure 4: Growth remains modest despite higher investment

%



Source: IMF

South Africa – Vulnerable on many counts

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Growth weakens – We change our forecasts

Growth is the lowest since the global economic crisis; consumer confidence is even weaker now than it was then: South Africa appears stuck in a low-growth environment

We lower our 2013 GDP growth forecast for South Africa to 2.2% y/y from 2.7% previously. Deterioration in high-frequency indicators, as well as weaker-than-expected GDP in Q1-2013 (only 0.9% q/q), indicate softer growth momentum. Consumer confidence has hit a new nine-year low. Despite accommodative monetary policy, households remain indebted, with debt-to-disposable income at c.76%. Real credit growth trends are modest. Given limited room for further fiscal stimulus, South Africa needs to boost export growth to bolster its own recovery prospects. But weak commodity prices and the threat of further output shortfalls at its mines, as rival unions vie for power and wages are bid up to uncompetitive levels, may mean that an export recovery remains elusive.

We think the market is wrong: at this point, the risk of new easing outweighs the likelihood of a rate hike; a further downward revision to the SARB's GDP forecast is likely at the next MPC meeting

Although June PMI rose to a four-month high of 51.6, reflecting some improvement in business conditions and new orders, the overall environment for manufacturing remains challenging. External demand is still muted; the sector must contend with high input costs; and there is little employment growth. With little real value added in either manufacturing or mining since the global economic crisis, South Africa appears mired in a weak growth environment. Household consumption expenditure provides an occasional lift to growth, but in recent quarters, it has slowed. Some evidence of structural change is in place. South Africa's black middle class continues to grow. Demand for durable goods has held up, reflecting this shift. At the low end of the income scale, increased provision of social welfare grants protects some consumption. But with weak GDP growth impacting fiscal receipts, the affordability of any scaled-up fiscal stimulus is always in question. With further downward revisions to official GDP forecasts anticipated (the Treasury currently projects growth of 2.7% in 2013, the South African Reserve Bank 'SARB' 2.4%), revenue collection may be weaker than earlier projections. Meaningful fiscal consolidation may be delayed. The risk is that the FY14 budget deficit (ends March 2014), initially estimated at 4.6%, will widen to at least 4.8%. There are implications for monetary policy too.

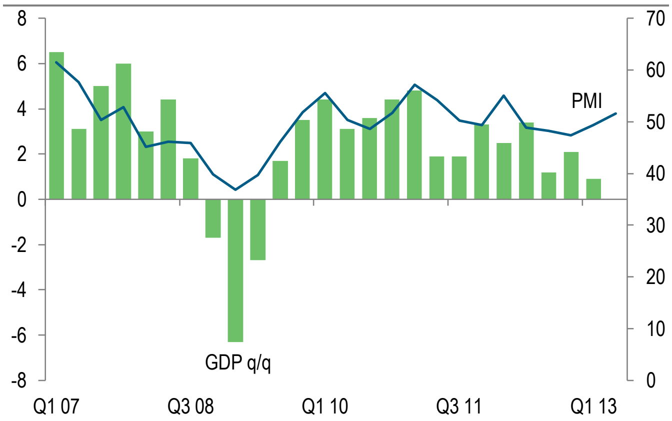
Given a substantial negative output gap, estimated by the SARB to be c.2%, monetary policy is likely to remain accommodative for even longer. Despite expectations of a Q3-2013 breach of South Africa's 3-6% inflation target, we believe the market is wrong to price in the risk of imminent rate tightening. Currently, the

Figure 1: Standard Chartered forecasts – South Africa

	2012	2013F	2014F
GDP (real % y/y)	2.5	2.2	3.1
CPI (% annual average)	5.7	5.8	4.9
Policy rate (%)*	5.0	5.0	5.0
USD-ZAR*	8.48	10.2	10.3
Current account balance (% GDP)	-6.1	-6.2	-6.3
Fiscal balance** (% GDP)	-3.9	-4.8**	-4.8

**end period*; ***Fiscal year ends March;*
Source: Standard Chartered Research

Figure 2: South Africa – GDP the weakest since the crisis
Real GDP % q/q SAAR, PMI (RHS)



Sources: Bloomberg, Stats SA

With the likelihood of weaker growth and temporarily higher inflation, the SARB faces a difficult choice

3x6 FRA is pricing in more than a 50% chance of a rate hike in South Africa. A 50bps rate hike by the SARB is fully priced in by early 2014 (the midpoint of the 7x10 FRA stands at 5.54%, relative to a repo rate of 5%). Despite this, we are changing our SARB repo rate forecast, anticipating unchanged interest rates for even longer. Weak growth *does* matter, and recent SARB communication has reinforced this message. **We now see the repo rate remaining on hold at 5% until Q4-2015, having previously anticipated the beginning of a normalisation cycle in South African interest rates as early as Q2-2014.**

Examining inflation-targeting flexibility

Although not a core view, the risk of further SARB easing cannot be entirely dismissed

The key risk near-term is that the SARB *cuts* its repo rate further, although this is not yet a core view. The SARB faces a difficult choice. It must balance the risk of slower growth against a likely breach of the inflation target. Recent South African rand (ZAR) weakness has added to inflation risks. Should the growth outlook weaken further, or the ZAR stabilise (improving the inflation outlook), then the risk of a rate cut is likely to increase. At the last SARB meeting in May, at least one monetary policy committee member argued for a rate cut, although the decision to hold interest rates steady was unanimous. Nonetheless, the debate has shifted. Further easing, not explicitly 'on the table' previously, may now be seen as a possibility.

Despite its core price stability mandate, there is now increasing debate on what 'flexible inflation targeting' may mean for the SARB. In a speech in early June, Governor Marcus alluded to the weight assigned to both price stability and output under a flexible inflation-targeting mandate. The relative weight given to each objective (price stability or growth) is likely to change over time, given circumstances. The inference? If growth undershoots potential output even more severely, then the SARB can afford to be more accommodating of a temporary, supply-side-driven breach of the inflation target, especially if it does not alter longer-term inflation expectations significantly.

The key unknown is the outlook for the ZAR, with the global environment posing new risks that lower the likelihood of any easing. SARB models estimate that the pass-through coefficient from the FX rate to consumer prices is 0.2 (i.e., a 10% depreciation in the ZAR typically results in a 2ppt increase in CPI). However, this happens with a lag, and the stage of the business cycle also matters.

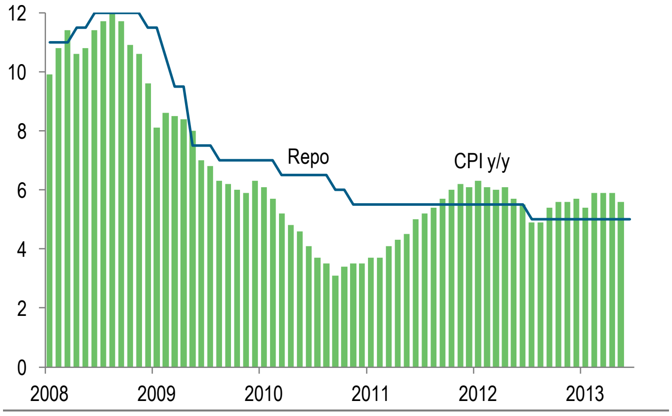
Figure 3: The ZAR benefited from QE1 and QE2; QE3, in the wake of the Marikana tragedy, had less of an impact

USD-ZAR

Sources: BoM, Standard Chartered Research

Figure 4: Policy will become more accommodative as CPI rises, even if the SARB keeps its repo rate on hold

CPI y/y, SARB repo rate



Sources: Bloomberg, Standard Chartered Research

Interestingly, the recent pass-through to inflation as a result of the weaker ZAR has been slower than might be expected, possibly reflecting the lack of pricing power. Petrol prices have been an exception. Here, the impact of a weaker ZAR is felt immediately. In July, petrol prices in South Africa rose 84 cents/litre to an all-time inland price high of ZAR 13.23. Under the new, reweighted CPI introduced this year, petrol prices have a greater weight in the CPI basket, 5.68% – up from 3.93% previously. While global commodity price softness should temper the medium-term rise in inflation (the SARB's CPI forecasts of 5.2% and 5.0% for 2014 and 2015 are not far from our own), the extent and persistence of currency weakness still matters for the inflation outlook.

The ZAR is vulnerable

With the Fed expected to reduce its asset purchases, South Africa is seen as vulnerable to any investor re-assessment of asset market valuations

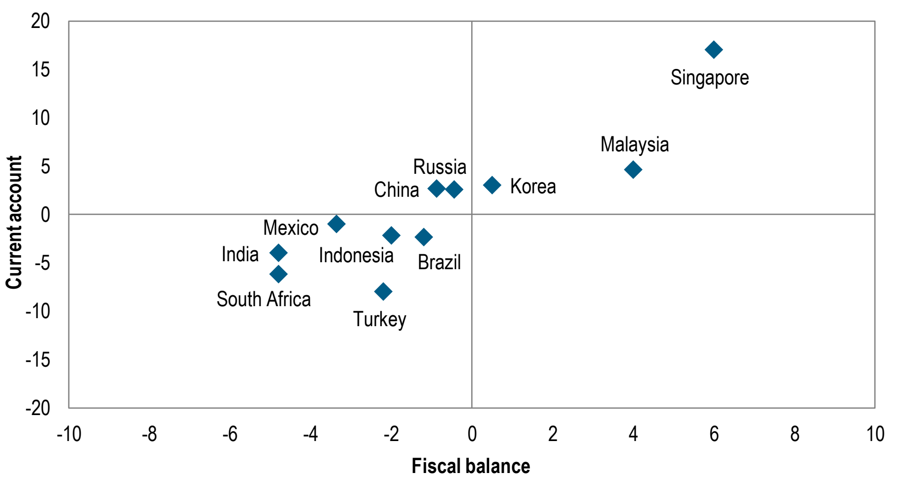
Fed warnings that it may start to taper QE later this year have been a key driver of price action in South African markets in the last quarter, adding to concerns about mining-sector unrest and a deteriorating domestic growth outlook. As a liquid emerging market, South Africa had been a significant beneficiary of increased offshore inflows as a result of global easing. By early June 2013, non-resident investors held c.38% of domestic government bonds and c.42% of domestic equities, according to SARB data, near historic post-crisis highs. Large inflows associated with Bank of Japan easing have yet to be seen. But UST yields have already risen substantially, following the suggestion that the Fed may start reducing the pace of its asset purchases later this year. This has triggered a reassessment of valuations across emerging markets.

Higher debt-service costs in anticipation of QE tapering would impede South Africa's ability to provide more of a countercyclical fiscal boost

South Africa, with its slowing growth profile, rising inflation in the near term, and twin current account and fiscal deficits, is seen as being especially vulnerable to this investor re-assessment (Figure 5). There are several reasons for this: (1) As a liquid emerging market South Africa will not be insulated from global market volatility. (2) South Africa has seen a significant increase in offshore involvement in its markets, in part associated with its World Global Bond Index (WGBI) inclusion in 2012. South Africa's countercyclical spending efforts benefited meaningfully from QE and the availability of cheaper deficit financing. Any exit of foreign investors now would trigger a spike in bond yields, exacerbating the fiscal outlook, perhaps further impeding the authorities' ability to provide a countercyclical

Figure 5: South Africa – Among the most vulnerable of emerging markets

Current account, fiscal balance – selected emerging markets (% of GDP)



Sources: IMF, Standard Chartered Research boost to growth. (3) With its twin deficits, South Africa is more dependent on inflows to meet its external financing requirement. In an environment of weak commodity prices, its current account deficit is unlikely to correct any time soon. Demand for capital goods imports is driven largely by South Africa's public-sector infrastructure programme; thus it is relatively inelastic with respect to growth. South Africa needs an export recovery, driven by improved demand in the rest of the world, to close its trade imbalance. In the absence of better export growth, concerns about how South Africa will finance its current account deficit are likely to persist. (4) Even leaving aside global market volatility, domestic fundamentals are deteriorating, adding to bearish sentiment. Investors are more concerned about political risk. This has also been reflected in recent credit-rating downgrades of the country.

In an environment of QE tapering and the eventual removal of policy accommodation, the suggestion is that emerging markets with positive growth fundamentals will still be able to cope with higher market interest rates. South Africa, with its weakening growth profile, where interest rates have not been raised at all since the global economic crisis, does not qualify.

South Africa still has important buffers in place

The South African economy should benefit from ZAR weakness; it is better for a nominal variable (like the currency) to bear the burden of adjustment to a post-QE world, than the real economy

Inflation risks aside, a weaker ZAR may help boost South Africa's external competitiveness, helping to accelerate an export recovery. While a weaker ZAR will not deal with the economy's structural challenges, currency flexibility should at least mitigate the impact of global volatility on South Africa's economy. In this case, a nominal variable – the currency – rather than the real economy, would undertake the burden of adjustment in response to higher interest rates globally and the re-pricing of risk that accompanies the Fed's tapering of QE. The South African authorities are likely to continue with their policy of allowing the ZAR to be market-determined. A rate hike in response to currency volatility, especially short-lived volatility, remains improbable.

South Africa's low leverage ratios will act in its favour. Sizeable portfolio inflows in other emerging markets may have contributed to domestic credit booms, which may now be put at risk by a reversal of inflows. South Africa's experience was different. Credit growth remained muted overall in the aftermath of the global economic crisis. Banks adopted more conservative behaviour and tighter lending standards. Although levels of unsecured lending increased, in aggregate terms this accounted for a negligible proportion of overall lending. Mortgage advances, a more important component of private-sector credit, have largely flat-lined. Despite an accommodative interest rate environment following the announcement of QE, South Africa is not at risk of a sudden reversal of domestic lending.

South Africa's public debt ratio also remains modest, at c.42% of GDP. While rating agencies have expressed concern over the extent of the central government's contingent liabilities, relating to borrowing by state-owned enterprises, contingent liabilities are not seen as an immediate risk factor. Moreover, 60% of South Africa's external debt (held by foreigners, with a cross-border element) is ZAR denominated, mitigating the risks typically associated with external financing. Although import cover of c.4.2 months is low relative to many emerging market peers, the SARB is unlikely to intervene in markets in response to ZAR weakness; hence FX reserves are seen as relatively secure. Despite its challenges, South Africa has important elements of flexibility in place.

Africa – Local markets outlook

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Sub-Saharan African local bond markets sold off sharply in Q2, with the notable exception of Kenya and Uganda, where yields rallied by an average of 200bps across the curve, driven entirely by local factors. South Africa and Nigeria were the most severely hit by panic selling from offshore investors in the wake of Fed Chairman Bernanke's comments on an early tapering of quantitative easing (QE). Despite a high concentration of foreign holdings, the sell-off in Ghana was relatively contained, confirming its low correlation with US Treasuries (USTs).

Long 10Y Nigeria, 3Y Ghana

With some risk of an early tapering of QE now priced in, we expect local fundamentals to return to the forefront. We therefore maintain an *Overweight* duration and FX weighting in Nigeria where domestic fundamentals and valuations remain compelling. We also remain *Overweight* duration in Ghana where we expect local yields to ease somewhat after the issuance of a new sovereign bond, but maintain a *Neutral* FX weighting given the current account deficit. In South Africa, we remain *Neutral* duration given heightened fiscal concerns; we see better value in the 2Y swap where risks of a rate hike appear overdone. We also maintain our *Underweight* FX weighting on the rand (ZAR) given its vulnerability to portfolio flows and the large current account deficit. We remain *Neutral* duration on Kenya and Uganda where we see risks tilted towards higher yields in the near term on a less favourable demand/supply equation, and on Zambia due to our expectations of tighter monetary policy. We recommend a *Neutral* FX position on the Ugandan shilling (UGX) and Zambian kwacha (ZMW) and *Underweight* on the Kenyan shilling (KES) where we see increased pressure from imports.

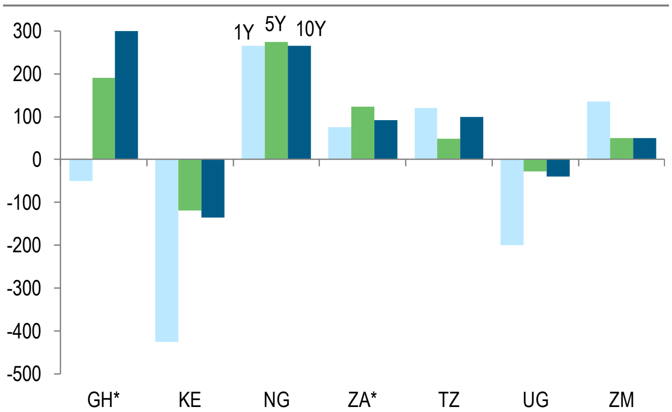
West Africa

Nigeria – Fundamentals remain supportive

Sell-off in Nigeria driven by global de-risking

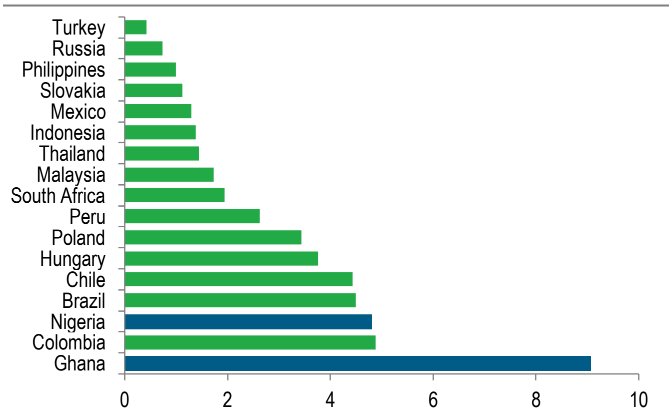
Offshore investors reduced their exposure to the Nigerian bond market in June, as pressure on both the currency and yields, which backed up by 270-325bps across the curve, indicates. We think most of the correction is being driven by global risk sentiment and precautionary positioning in one of the less liquid emerging bond markets, rather than deteriorating domestic fundamentals, which we think remain relatively supportive. We therefore remain ***Overweight* FX and duration in Nigeria and have reinstated our long position on the 10Y** (entry: 13.87%, current: 13.90%, target: 11.50%, stop: 15%).

Figure 1: Kenya and Uganda rally on local fundamentals
YTD move in benchmark yields, bps



*GH 1Y, 3Y, 5Y and ZA 2Y
Sources: Bloomberg, Standard Chartered Research

Figure 2: Nigerian and Ghanaian real yields remain compelling *(10Y yield, Ghana 5Y yield, %)*



Sources: Bloomberg, Standard Chartered Research

Limited probability of a rate cut

Although we expect inflation to remain in single digits in the coming months, the increase in government spending seems to have reduced the likelihood of an imminent rate cut. We therefore see limited room for T-bill yields to ease below 12% for now and prefer to add duration at current levels.

Debt supply remains conservative

Despite risks of increased government spending, the Debt Management Office announced another conservative bond issuance calendar for Q3, in line with our expectations. Given the lack of substantial bond redemptions in Q3, the NGN 195bn average supply remains in line with the NGN 315bn average of the previous two quarters. This should easily be absorbed by domestic demand, especially as liquidity conditions onshore are likely to remain stable. Yields have already backed up to their June 2012 high, a period when the currency and inflation outlook were much worse than we expect now. We therefore see limited risk of a further substantial bond sell-off. Valuations on the 2022 bond should also appeal to indexed investors who seem to have trimmed their exposure to Nigerian bonds in favour of T-bills in recent weeks.

Limited risk on FX

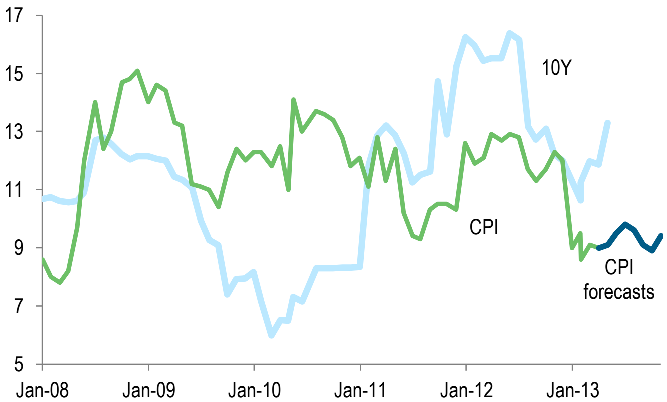
We also see limited currency risk given the relatively small size of foreign holdings in the local bond market. With an estimated USD 10-12bn of portfolio inflows entering the local bond market between 2012 and April 2013, the Central Bank of Nigeria (CBN), with FX reserves of USD 48bn, seems well equipped to counter near-term pressure. Despite a reported decline in oil production in April, oil prices have enabled export revenues to remain stable and should continue to do so in the coming months, providing longer-term support to the naira (NGN).

Ghana – Looking for a silver lining

Fundamentals remain weak but local yields could improve on lower debt supply

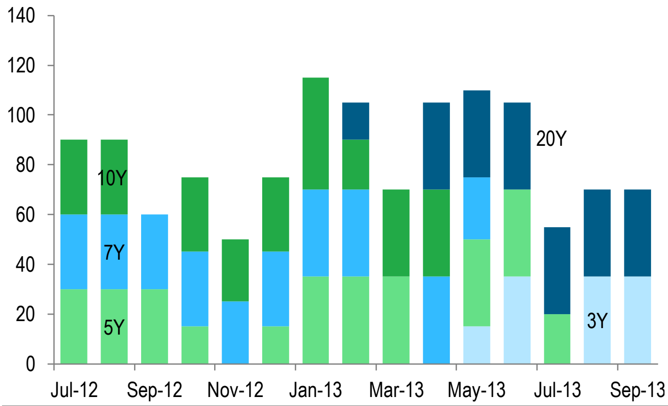
The Ghanaian curve bear-steepened in Q2, reflecting offshore investors' disappointment with a targeted deficit of 9% of GDP in 2013, from a revised 11.8% in 2012. Risks surrounding an early tapering of QE also pushed yields slightly higher in June, although the sell-off has been relatively contained so far, considering the sizable share of foreign holdings. We expect domestic debt supply to improve marginally in H2 and therefore maintain our recommendation to be **long the 3Y bond in Ghana (current: 20%, entry: 18.5%, target: 17%, stop: 21%) and expect the carry to compensate for a further weakening of the Ghanaian cedi (GHS). We remain *Neutral* on the GHS.**

Figure 3: Supportive inflation outlook in Nigeria
%



Sources: CBN, Standard Chartered Research

Figure 4: Nigeria's planned bond supply remains conservative *(NGN bn)*



Sources: DMO, Standard Chartered Research

Borrowing requirement to ease somewhat in H2

Lower tax revenues and grants led to a further widening of the fiscal deficit in the first four months of the year, to 3.8% of GDP against a target of 3%. This, however, has been more than offset by increased domestic debt issuance, well above the planned issuance calendar. Although shorter-term tenors bore the brunt of the excess issuance, T-bill yields have remained extremely stable YTD, even easing by 10bps in June. With the Bank of Ghana (BoG) now slightly ahead in terms of domestic borrowing requirement, H2 gross issuance is slightly below H1, allowing local yields to ease slightly from current levels.

Curve to remain inverted as bulk of new issuance remains on shorter tenors

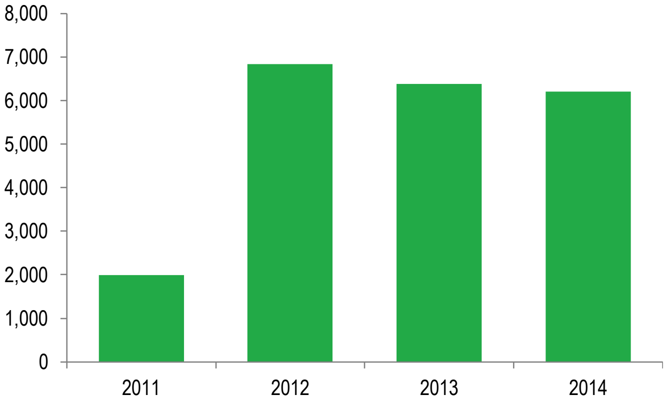
The BoG resisted the temptation to rebalance new debt issuance towards longer-term bonds, largely owned by foreign investors. Instead, the bulk of gross issuance in H2 continues to be short-term T-bills and notes, with a greater emphasis on the 1Y and 2Y notes. Short-term yields are therefore likely to remain under pressure and the curve inverted as supply at the 3Y-7Y segment of the curve is below H1. The proceeds of the larger-than-expected eurobond, due in late July, should nonetheless help alleviate pressure on domestic borrowing.

Lower gold exports to weigh on FX outlook

Demand from offshore investors will continue to depend on the currency outlook. The trade deficit widened further in Q1-2013, driven by lower export receipts and a sharp increase in oil imports. Going forward, moderating oil prices and non-oil imports, which showed a marked deceleration in Q1-2013, should help limit a further widening of the trade balance. However, the bleak outlook for gold prices (gold accounts for 40% of Ghana's total exports) will continue to put pressure on the currency. We therefore expect the GHS to weaken further, albeit at a more moderate pace than is currently priced in by the forwards. We have revised our forecasts accordingly.

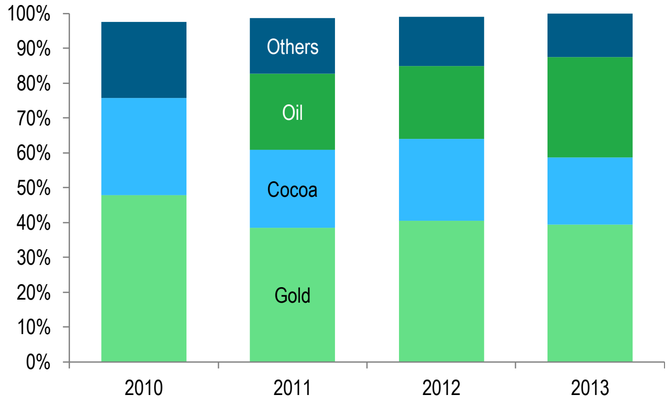
The rebasing and reweighting of the CPI basket also highlights stronger inflationary pressures, up to a revised 11.1% y/y in May versus 10.9% in April before rebasing. With inflation likely to come under further pressure via a planned removal of utility price subsidies, the BoG may need to raise its policy rate a further 100-200bps in this cycle. This could potentially help limit the currency's depreciation.

Figure 5: Eurobond issuance to alleviate pressure on domestic borrowing in Ghana *(GHS mn)*



Sources: IMF, Standard Chartered Research

Figure 6: Gold remains Ghana's main export
%



Sources: BoG, Standard Chartered Research

East Africa

Kenya – Stretched valuations amid rising inflation and fiscal risks

Stretched valuations

The Kenyan bond market rallied strongly in Q2, with the curve bull-steepening by more than 300bps on the Central Bank of Kenya (CBK)'s 100bps rate cut in May and flush liquidity conditions. Demand has been mostly local, with offshore investors focusing mainly on infrastructure bonds, albeit in small amounts. With offshore investors accounting for less than 3% of the local bond market and Kenyan yields showing a partial negative correlation with USTs, local government bonds appear less vulnerable to the removal of QE (see *Local Market Alert – Africa, unequal vulnerability to US QE tapering, 21-Jun-13*). However, with yields having rallied by 120-500bps across the curve since end-March, current valuations appear stretched and more at risk of a reversal.

Inflation to edge up in H2

Inflation started to creep up in June, at 4.9% y/y from 4.1% y/y in May. We see risks tilted towards higher CPI inflation in the second half of the year, when the base is likely to be less favourable. We therefore think that the CBK's last 100bps cut in the central bank rate to 8.5% in May likely signalled the end of its easing cycle. With T-bill yields still pricing in close to another 200bps rate cut, we expect the curve to bear-flatten in the near term, especially as a weaker currency could lead to more aggressive ad-hoc mopping up of excess liquidity by the CBK.

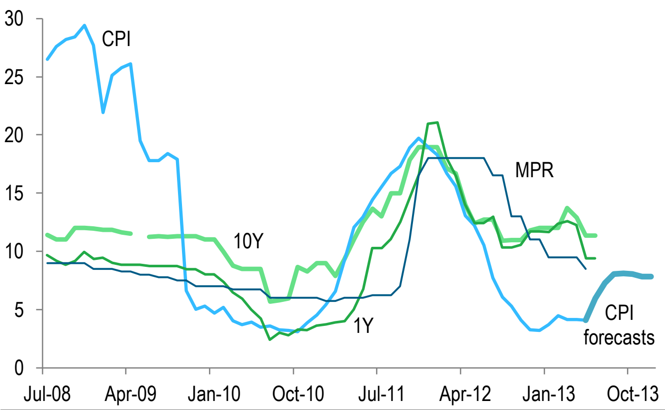
Fiscal risks on the upside

Despite an expansive budget, with the fiscal deficit expected to remain wide at 7.9% of GDP in FY14 (started July 2013), the budgeted issuance of a USD 1bn eurobond (in part to refinance the USD 600mn 2Y loan maturing in 2013) allows planned domestic borrowing requirements to err on the conservative side, at KES 106.7bn. However, upside risks remain, as growth expectations appear optimistic, at 5.8% in 2013 from 4.6% in 2012. Revenue shortfall in FY13 led to a supplementary budget, raising net domestic financing from a target of KES 106.7bn to KES 218.8bn in the year to June. The risk therefore is that revenue disappoints yet again, despite projections that GDP growth will accelerate to close to 6%.

KES to weaken on pick-up in economic activity and slower portfolio flows

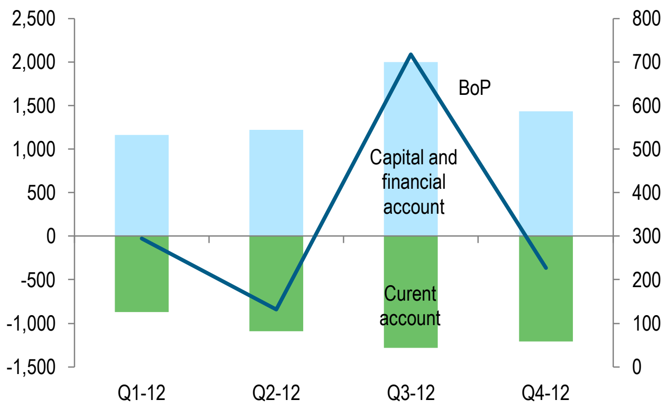
The trade deficit continued to widen in the year to February, to USD 10.54bn, on the back of surging imports. With oil imports accounting for close to 25% of the total import bill, the KES likely benefited from lower oil prices in recent months. However, capital goods imports, which have surged to 30% of the import bill on the back of oil exploration, will continue to weigh on the current account deficit, estimated at 11.4%

Figure 7: Rate cut expectations are overdone in Kenya
Benchmark rates, %



Sources: CBK, Standard Chartered Research

Figure 8: Kenya's BoP bolstered by rising portfolio flows to the local stock market *(USD mn)*



Sources: CBK, Standard Chartered Research of GDP in April. Looser monetary conditions could fuel stronger import demand in the coming months, increasing the pressure on the KES, which should also receive less support from capital inflows, with equity portfolio flows likely to slow under QE tapering. We therefore maintain an *Underweight* position on the KES.

Uganda – Bond supply to increase in FY14

Rising debt supply to weigh on local yields

Domestic sentiment turned bearish in June, leading to a bear-steepening of the yield curve amid increased debt supply. We expect yields to continue to drift higher in the near term as domestic borrowing requirements for FY14 (started July 2013) are set to increase by 23%, despite bullish growth projections.

Despite a rebound in domestic growth, to 5.1% in FY13 after a dismal 3.4% in FY12, Uganda raised its FY13 domestic borrowing requirement to UGX 844bn to compensate for the revenue shortfall stemming from the suspension of donors' budget support (60% below budget target). Although growth is expected to reach 6% in FY14, the Ministry of Finance expects domestic borrowing to increase to UGX 1.04tn, again compensating for the prolonged decline in donor aid (budget support grants are expected to decrease by 84% y/y).

Policy rate on hold near term

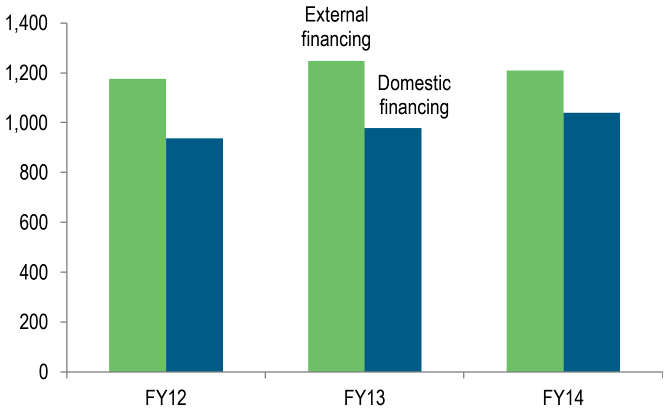
Yields backed up by 75-200bps across the curve in June on the back of increased bond supply and deteriorating sentiment, although flush liquidity conditions continued to buoy onshore demand for local government securities. A stable currency and subdued inflation allowed the Bank of Uganda (BoU) to maintain an accommodative monetary stance in Q2, delivering another 100bps rate cut at its June meeting to bring the monetary policy rate to 11%. Having expressed its concern over the food-price inflation outlook, the BoU is likely to adopt a cautious stance near-term. Should inflation turn out to be relatively benign, we could see a late-cycle easing of the central bank rate by an additional 100bps to 10% in November.

Current account deficit to widen on rebounding imports

We expect the financial and capital account to remain buoyed by strong FDI and a potential return of bond portfolio flows, albeit in small amounts, once yield levels appear sufficiently compelling. But the current account deficit, which narrowed from 11% of GDP in FY12 to 9.3% in FY13, is likely to deteriorate on the back of stronger imports and slower export growth.

Figure 9: Uganda's domestic borrowing on the rise

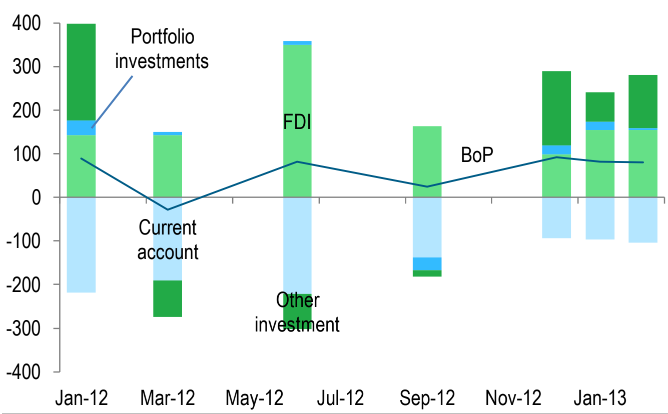
UGX bn



Sources: BoU, Standard Chartered Research

Figure 10: Uganda's BoP bolstered by FDI

USD mn



Sources: BoU, Standard Chartered Research

Given higher domestic borrowing requirements and the need to reduce borrowing costs, we expect the BoU to refrain from aggressively mopping up excess liquidity to support the currency as long as it remains within the USD-UGX 2,600-2,700 range. But any signs of increased pressure could lead to a surge in T-bill issuance and reinforce the near-term bearish trend on rates.

South Africa

South Africa – Better value in short-term swaps

SAGBs vulnerable to Fed tapering of QE

The South African government bond market has been badly hit by the EM sell-off in the aftermath of Bernanke's talk of an early tapering of QE. Portfolio adjustments from foreign investors led to yields backing up by more than 100bps across the curve, although only ZAR 10bn left the market in May-June. We **maintain a *Neutral* duration stance and *Underweight* FX weighting on the ZAR and see better value in receiving the 2Y swap (current: 5.90%, entry: 6.37%, target: 5.25%, stop: 6.80%).**

Risks tilted towards a steeper curve

We continue to see risks tilted towards a further correction of South African government bonds (SAGBs), especially given their correlation with UST yields and a still-high concentration of foreign holdings. Domestic fundamentals also point to a steeper curve, with disappointing economic data raising the risk of a further downgrade in the National Treasury's growth forecasts, and lower fiscal revenues adding to the risk of increased bond supply. In addition, the deteriorating fiscal position points to a higher probability of further sovereign credit-rating downgrades, which could also lead to a steeper curve. Inflation, by contrast, has so far been more muted than expected, with the large output gap and weaker commodity prices compensating for some potential FX pass-through.

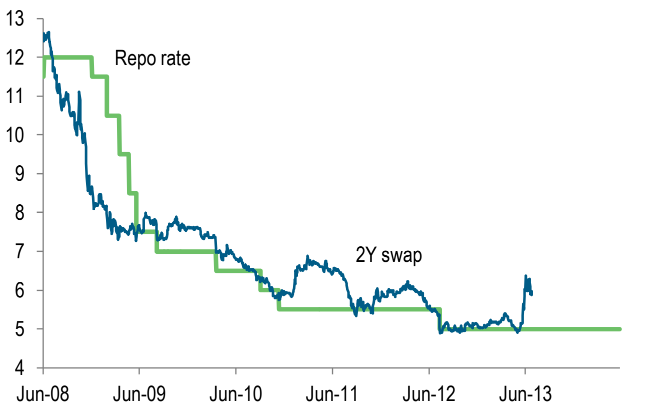
Better value in receiving 2Y swap

Despite all these factors, we remain reluctant to enter steepeners at current levels, as the 2/10Y slope has already re-steepened substantially and could even look compelling to some investors currently. We think, however, that rate-hike expectations are largely overdone and we continue to prefer receiving the 2Y swap at current levels (entry: 6.37%, current: 5.90%, target: 5.25%, stop: 6.80%).

ZAR remains vulnerable to swings in portfolio flows and the current account deficit

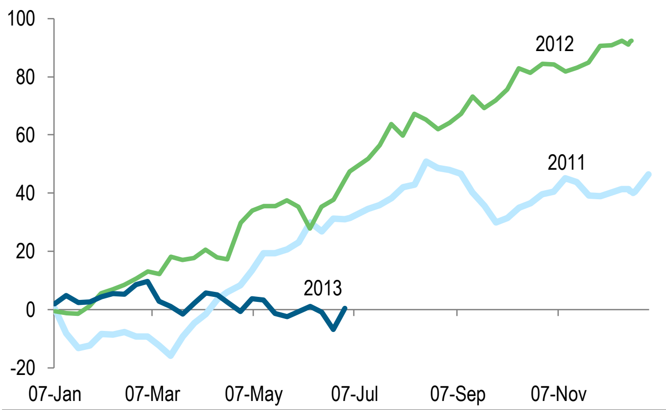
We maintain our *Underweight* weighting on the currency, which remains vulnerable to swing in portfolio flows. Although the trade deficit narrowed in May, to ZAR 11bn from ZAR 15bn in April, it is above its 2012 levels and continues to point to a current account deficit of close to 6% of GDP for the year.

Figure 11: South Africa's rate hikes expectations are overdone *(%)*



Sources: Bloomberg, Standard Chartered Research

Figure 12: ZAR remains vulnerable to a slowdown in portfolio flows *(USD mn)*



Sources: Bloomberg, Standard Chartered Research

Zambia – Risks stemming from higher inflation

Tighter monetary policy as inflation rises

Zambian yields continued to range-trade in Q2, with the belly underperforming in the latter half of the quarter on tighter liquidity conditions. Although domestic debt supply has so far remained relatively conservative, we expect Zambian yields to remain under pressure near-term as the Bank of Zambia (BoZ) tightens monetary policy to bring inflation back to its 6% year-end target.

Rising inflationary pressures led the BoZ to hike its monetary policy rate (MPR) by 50bps between May and June, to 9.50%. The removal of maize subsidies and fuel price hikes seem to have contributed to a further rise in June's CPI, up to 7.3% y/y in June from 7% in May. With inflation now firmly above the BoZ's year-end target of 6% and electricity price hikes likely to keep it higher in the coming month, we expect the yield curve to continue to bear-flatten in anticipation of further monetary tightening. Higher inflation should, however, have a limited impact on the longer end of the curve, which is already very steep.

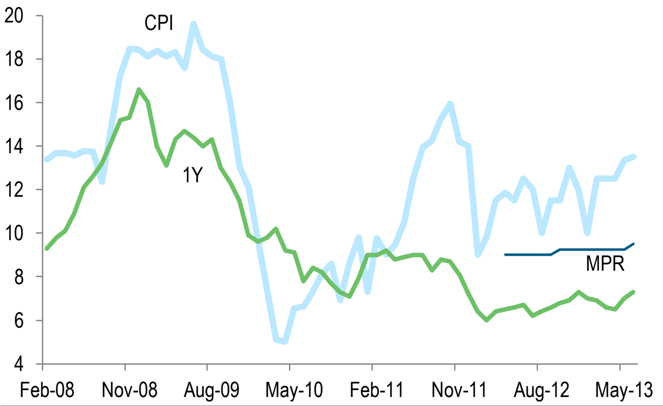
Weaker ZMW to increase risk of further monetary tightening

The BoZ kept T-bill issuance stable in Q2, at ZMW 450mn fortnightly, but increased the pace of its open market operations in an effort to realign the overnight interbank rate with its target at +/-200bps around the MPR. This, along with seasonal tax payments, led to a bear-flattening of the curve in June, which should continue after the surprise June rate hike. Despite a rebound in Zambia's trade surplus in Q2, the ZMW resumed its weakening trend in May. The BoZ's efforts at strengthening the currency, by implementing new regulation to monitor the balance of payments, should have a limited impact, given the longer-term underlying trend of deteriorating current account balance. Prolonged currency weakness could lead to more aggressive tightening by the BoZ.

Debt supply pressure remains limited

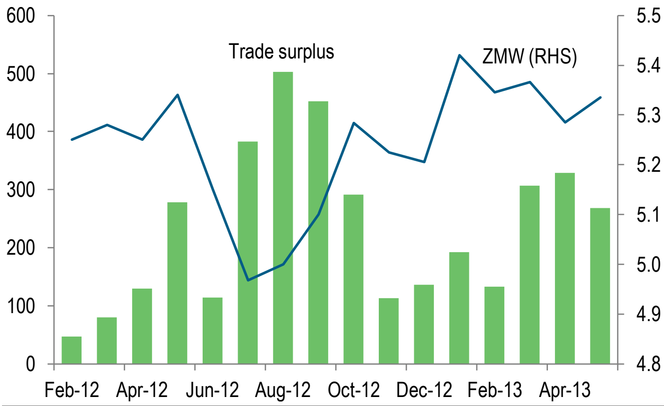
Effective budget execution allowed the BoZ to maintain stable bond issuance in the first five months of the year, at ZMW 700mn per quarter. The government registered a deficit of ZMW 2.8bn in May, in line with the 2013 target. We see limited pressure stemming from domestic debt issuance in the coming months, as tax revenues and grants exceeded the budget target in January-May (on the back of higher Pay As You Earn and trade taxes). Talk of a second eurobond of USD 500mn or USD 1bn to finance infrastructure spending also shows the government's willingness to favour external over domestic borrowing for now.

Figure 13: Risks of further rate hikes as CPI creeps up *%*



Sources: BoZ, Standard Chartered Research

Figure 14: ZMW remains weak despite a rebound in the trade surplus *(ZMW mn)*



Sources: ZamStats, Standard Chartered Research

Forecasts – Economies and FX

Country	Real GDP growth (%)					Inflation (yearly average %)					Current account (% of GDP)					FX				
	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015	Q3-13	Q4-13	Q1-14	Q2-14	Q3-14
Majors	**1.3**	**1.1**	**1.0**	**1.9**	**1.7**	**1.9**	**1.8**	**1.3**	**1.7**	**1.8**	**-0.9**	**-1.0**	**-0.5**	**-0.6**	**-0.8**					
US^	1.7	2.2	1.8	2.7	3.0	1.4	1.8	1.2	1.8	2.0	-3.1	-3.0	-3.0	-3.1	-2.9	N.A.	N.A.	N.A.	N.A.	N.A.
Euro area	1.4	-0.6	-0.5	1.3	1.5	2.7	2.5	1.5	1.3	1.5	0.3	0.9	1.5	1.3	1.0	1.32	1.29	1.30	1.27	1.26
Japan	-0.7	1.9	1.9	1.1	1.3	-0.2	0.0	0.2	1.9	1.4	2.0	1.0	2.0	2.3	2.1	96.0	97.0	102.0	102.0	104.0
UK	0.9	-0.1	1.0	1.6	1.9	4.4	2.8	2.6	2.0	1.7	-1.9	-3.8	-2.0	-1.8	-2.5	1.52	1.46	1.48	1.47	1.48
Canada	2.5	1.8	1.7	2.5	3.0	2.5	2.1	2.0	2.2	2.2	-3.0	-3.2	-2.8	-2.6	-2.3	1.03	1.03	1.04	1.02	1.02
Switzerland	1.9	0.9	1.2	2.1	1.9	0.3	-0.7	0.4	0.9	0.9	10.5	12.7	12.3	10.5	10.0	0.95	0.98	0.98	1.03	1.05
Australia	2.5	3.6	2.5	2.8	3.1	3.3	1.8	2.6	2.8	2.9	-2.4	-3.7	-3.8	-3.9	-5.9	0.92	0.88	0.85	0.83	0.84
New Zealand	1.3	3.0	2.4	2.8	2.6	4.1	1.1	1.8	2.5	2.3	-4.0	-5.0	-5.3	-5.7	-6.4	0.80	0.78	0.76	0.76	0.78
Asia	**7.3**	**6.2**	**6.3**	**6.5**	**6.6**	**5.8**	**3.7**	**3.6**	**4.3**	**3.7**	**2.3**	**1.8**	**2.2**	**2.6**	**2.8**					
Bangladesh*	6.7	6.1	6.3	6.5	6.5	8.8	10.6	7.7	7.5	8.0	0.9	1.5	3.0	2.5	2.0	77.00	76.00	77.00	77.00	77.50
China	9.2	7.8	7.7	7.5	7.5	5.4	2.6	2.8	4.1	3.0	2.8	2.6	3.3	3.7	3.9	6.15	6.13	6.10	6.07	6.04
CNH	--	--	--	--	--	--	--	--	--	--	--	--	--	--	--	6.140	6.120	6.080	6.050	6.020
Hong Kong	4.9	1.5	3.4	4.5	4.5	5.3	4.1	4.5	4.5	4.0	4.8	1.3	2.5	3.5	3.5	7.765	7.780	7.800	7.810	7.800
India*	6.2	5.0	5.5	6.0	6.5	8.7	7.4	6.3	6.0	6.0	-4.2	-4.8	-4.0	-3.5	-3.5	59.00	60.50	61.00	58.00	57.50
Indonesia	6.5	6.2	6.2	6.5	6.7	5.4	4.3	6.8	6.4	4.9	0.2	-2.7	-2.2	-1.0	-0.4	9,900	9,800	9,700	9,800	9,700
Malaysia	5.1	5.6	4.7	5.3	5.0	3.2	1.7	2.1	3.3	2.7	11.0	6.4	4.6	7.0	10.0	3.10	3.07	3.00	3.08	3.07
Pakistan*	2.4	4.4	3.6	4.0	4.5	13.9	10.8	7.5	9.0	9.0	0.3	-2.1	-1.0	-2.0	-2.2	103.00	105.00	106.50	107.00	108.00
Philippines	3.6	6.8	6.9	6.3	7.0	4.8	3.1	3.1	3.9	4.0	3.1	2.8	3.3	3.6	4.3	41.50	41.25	41.00	41.75	41.25
Singapore	5.3	1.3	2.6	4.8	5.0	5.1	4.6	2.5	3.5	3.5	21.9	18.6	17.0	19.0	20.0	1.26	1.25	1.24	1.26	1.25
South Korea	3.6	2.0	2.5	3.8	3.6	4.0	2.2	1.8	2.5	2.8	2.4	3.8	3.0	2.5	2.2	1,125	1,110	1,080	1,080	1,075
Sri Lanka	8.3	6.4	6.5	7.2	8.0	6.7	7.6	7.5	7.2	7.5	-7.6	-6.6	-4.5	-4.0	-3.8	126.0	125.0	124.0	123.5	124.0
Taiwan	4.0	1.3	3.0	4.3	4.8	1.4	1.9	1.4	1.9	1.4	8.8	10.2	8.0	7.0	7.5	29.80	29.30	29.00	28.90	28.80
Thailand	0.1	6.4	4.0	5.5	6.0	3.8	2.9	2.5	3.2	4.0	3.7	0.6	-0.4	-0.9	-1.5	32.00	31.50	31.25	31.75	31.50
Vietnam	5.9	5.0	5.3	5.8	6.5	18.6	9.3	7.2	8.2	5.8	-5.5	6.4	6.0	6.5	6.7	21,300	21,350	21,400	21,500	21,550
Africa	4.9	5.1	4.7	5.3	5.6	8.5	8.4	7.3	7.2	7.4	1.6	-2.0	-2.6	-2.7	-2.8					
Angola	3.7	8.4	7.0	7.0	7.0	15.0	10.3	9.4	8.5	8.0	12.0	9.2	6.0	5.0	5.4	96.30	96.50	96.90	97.10	97.30
Botswana	8.0	3.8	4.1	4.2	4.3	6.9	7.5	6.3	5.9	5.7	2.2	4.9	3.9	3.3	3.1	8.63	8.71	8.72	8.70	8.75
Cameroon	3.5	4.7	4.7	4.5	4.5	2.6	3.0	3.0	2.5	2.5	-3.8	-4.0	-3.8	-3.5	-3.5	496.9	508.5	504.6	516.5	520.6
Cote d'Ivoire	-5.8	9.8	8.0	7.5	7.5	3.0	1.3	3.2	2.5	2.5	1.0	-1.8	-2.5	-3.0	-3.0	496.9	508.5	504.6	516.5	520.6
The Gambia	-5.0	-1.7	9.7	8.3	6.0	6.0	5.0	6.0	4.0	4.0	-17.0	-14.0	-13.0	-13.0	-13.0	32.80	33.40	35.00	36.00	36.50
Ghana	14.4	7.9	8.0	7.2	7.2	9.0	9.2	12.4	11.0	7.4	-9.2	-12.2	-11.9	-11.0	-8.7	2.07	2.10	2.12	2.16	2.20
Kenya	4.9	5.1	5.5	5.9	6.2	14.0	9.6	6.0	6.6	6.1	-9.7	-9.1	-12.2	-11.0	-10.0	86.80	87.50	88.00	88.40	89.00
Nigeria	7.2	6.6	6.6	7.4	7.5	10.9	12.2	9.2	11.0	13.4	12.2	4.7	4.0	3.6	1.0	159.2	159.80	160.40	161.5	162.0
Sierra Leone	5.2	20.0	8.0	7.0	5.0	16.0	11.0	10.0	10.0	8.0	-50.0	-9.0	-7.0	-6.0	-7.0	4,350	4,360	4,380	4,390	4,395
South Africa	3.5	2.5	2.2	3.1	3.6	5.0	5.7	5.8	4.9	4.4	-3.4	-6.1	-6.2	-6.3	-5.4	10.05	10.20	10.30	10.70	10.50
Tanzania	6.1	6.5	6.8	7.0	7.2	11.3	15.6	9.8	7.4	6.7	-13.6	-15.8	-14.8	-13.3	-12.1	1,640	1,650	1,660	1,650	1,660
Uganda	4.4	5.1	5.3	5.0	5.6	18.7	14.6	5.5	8.2	8.1	-10.2	-12.0	-10.4	-12.2	-14.1	2,620	2,670	2,700	2,680	2,730
Zambia	6.6	7.0	7.4	7.5	7.8	8.8	6.4	7.3	7.4	6.2	1.5	-3.5	-2.3	-0.4	1.0	5.19	5.24	5.30	5.35	5.40
MENA	**6.9**	**4.5**	**3.9**	**4.1**	**4.2**	**5.5**	**5.7**	**5.4**	**5.2**	**5.2**	**8.9**	**9.9**	**8.4**	**8.2**	**7.0**					
Bahrain	1.9	3.4	4.0	3.7	4.5	-1.7	3.0	2.8	3.0	3.0	12.0	10.5	10.0	10.0	10.0	0.38	0.38	0.38	0.38	0.38
Egypt*	1.8	2.2	2.0	3.5	4.5	11.3	8.7	7.7	8.5	8.0	-2.6	-3.1	-2.9	-2.5	-2.1	7.15	7.20	7.25	7.20	7.20
Jordan	2.4	2.9	3.2	3.5	4.0	4.6	4.8	5.0	5.2	5.0	-12.0	-14.1	-9.9	-8.0	-6.5	0.71	0.71	0.71	0.71	0.71
Kuwait*	6.3	3.0	3.0	3.5	4.0	5.0	4.4	2.6	3.7	3.6	30.0	40.0	35.0	35.0	30.0	0.27	0.27	0.27	0.27	0.27
Lebanon	1.5	1.5	2.0	4.0	4.5	3.1	6.4	5.5	5.0	4.5	-17.5	-18.0	-16.0	-10.0	-14.0	1,500	1,500	1,500	1,500	1,500
Oman	4.5	8.3	4.5	4.0	4.3	4.0	3.0	2.6	3.5	3.6	10.0	12.0	7.5	7.0	7.0	0.39	0.39	0.39	0.39	0.39
Qatar	16.9	6.6	5.0	5.0	4.8	2.4	1.5	2.9	2.5	3.4	32.0	30.0	27.0	25.0	24.0	3.64	3.64	3.64	3.64	3.64
Saudi Arabia	6.8	6.8	4.8	4.2	3.9	6.1	4.9	4.9	5.0	4.2	22.0	21.0	19.5	18.7	18.7	3.75	3.75	3.75	3.75	3.75
Turkey	8.5	3.0	4.0	4.5	4.8	6.5	9.0	7.6	6.8	7.0	-9.8	-7.5	-8.0	-7.2	-7.6	1.85	1.80	1.80	1.80	1.80
UAE	4.2	4.3	3.5	3.6	3.2	0.9	1.5	2.9	2.5	3.2	11.2	16.8	14.0	12.0	7.1	3.67	3.67	3.67	3.67	3.67
Latin America	**3.9**	**2.2**	**3.5**	**4.1**	**4.1**	**6.9**	**6.4**	**6.9**	**6.5**	**6.2**	**-1.7**	**-1.9**	**-2.0**	**-2.0**	**-2.0**					
Argentina	6.5	0.5	2.5	3.0	3.5	23.5	25.0	28.0	25.0	23.0	-0.4	0.1	0.4	0.0	0.0	5.45	5.65	5.85	6.05	6.30
Brazil	2.7	0.9	3.2	4.0	3.6	6.5	5.4	5.8	5.5	5.3	-2.1	-2.4	-2.5	-2.4	-2.4	2.07	2.03	2.00	2.02	2.05
Chile	5.9	5.6	4.5	5.0	5.0	3.3	3.0	2.7	3.0	3.0	-1.3	-3.8	-4.2	-3.2	-3.0	500	490	480	485	485
Colombia	5.7	4.0	4.0	5.0	5.0	3.7	2.4	2.7	3.0	3.0	-3.1	-3.1	-3.3	-2.7	-3.0	1,880	1,850	1,820	1,850	1,840
Mexico	3.9	3.9	3.6	4.0	4.5	3.8	3.6	3.8	3.8	3.8	-0.8	-0.8	-1.0	-1.2	-1.4	12.75	12.40	11.99	11.90	11.80
Peru	6.9	6.3	6.0	6.0	5.8	3.4	3.7	2.7	2.5	2.5	-1.9	-2.8	-2.8	-2.5	-2.5	2.70	2.65	2.63	2.62	2.65
Global	**3**	**2.2**	**3.6**	**3.8**		**3.7**	**2.9**	**2.9**	**2.9**		**--**	**--**	**--**	**--**						

** Fiscal year starts in April in India and Kuwait, July in Bangladesh, Pakistan, and Egypt;^ Inflation: Core PCE deflator used for US;*

Source: Standard Chartered Research

Forecasts – Rates

End-period		Current	Q3-13	Q4-13	Q1-14	Q2-14	Q3-14
			%	%	%	%	%
United States	Policy rate	0-0.25	0-0.25	0-0.25	0-0.25	0-0.25	0-0.25
	3M LIBOR	0.27	0.28	0.28	0.28	0.28	0.45
	10Y bond yield	2.44	2.75	2.90	3.10	3.30	3.50
Euro area	Policy rate	0.50	0.50	0.50	0.50	0.50	0.50
	3M EURIBOR	0.22	0.20	0.20	0.25	0.30	0.35
	10Y bond yield	1.65	1.50	1.60	1.75	2.00	2.25
United Kingdom	Policy rate	0.50	0.50	0.50	0.50	0.50	0.50
	3M LIBOR	0.51	0.50	0.55	0.60	0.65	0.70
	10Y bond yield	2.34	2.00	2.15	2.35	2.60	2.90
Australia	Policy rate	2.75	2.50	2.50	3.00	3.00	3.25
	3M OIS	2.96	2.50	2.85	3.10	3.10	3.30
China	Policy rate	0.00	6.00	6.00	6.25	6.75	6.75
	7-day repo rate	4.30	3.50	4.00	4.30	5.00	5.00
	10Y bond yield	3.61	3.70	3.90	4.10	4.30	4.30
Hong Kong	3M HIBOR	0.38	0.39	0.40	0.40	0.40	0.40
	10Y bond yield	2.09	2.00	2.20	2.30	2.30	2.30
India	Policy rate	7.25	7.25	7.00	7.00	7.00	7.00
	91-day T-bill rate	7.48	7.00	7.20	7.20	7.25	7.40
	10Y bond yield	7.52	7.25	7.50	7.75	7.75	7.75
Indonesia	Policy rate	6.00	6.50	6.50	6.50	6.50	6.50
	FASBI rate	4.25	4.75	4.75	4.75	4.75	4.75
	10Y bond yield	7.35	8.00	7.75	7.50	7.25	7.00
Malaysia	Policy rate	3.00	3.00	3.25	3.25	3.25	3.25
	3M KLIBOR	3.20	3.20	3.45	3.45	3.45	3.45
	10Y bond yield	3.59	3.50	3.70	3.75	3.80	3.80
Philippines	Policy rate	3.50	3.50	3.50	3.75	4.00	4.00
	3M PDST-F	1.33	1.75	1.50	1.50	1.50	1.50
	10Y bond yield	3.88	3.80	4.00	4.20	4.50	4.60
Singapore	3M SGD SIBOR	0.38	0.40	0.40	0.40	0.40	0.40
	10Y bond yield	2.43	1.90	2.00	2.20	2.40	2.60
South Korea	Policy rate	2.50	2.25	2.25	2.25	2.25	2.50
	91-day CD rate	2.69	2.35	2.35	2.35	2.35	2.60
	10Y bond yield	3.45	3.30	3.30	3.40	3.40	3.50
Taiwan	Policy rate	1.88	1.88	1.88	2.00	2.13	2.25
	3M TAIBOR	0.88	0.88	0.88	0.96	1.02	1.08
	10Y bond yield	1.45	1.40	1.45	1.50	1.55	1.60
Thailand	Policy rate	2.50	2.50	2.50	2.50	2.50	3.00
	3M BIBOR	2.55	2.60	2.65	2.70	2.75	3.25
	10Y bond yield	3.70	3.55	3.60	3.60	3.70	3.80
Vietnam	Policy rate (Refi rate)	7.00	7.00	7.00	7.00	7.00	8.00
	Overnight VNIBOR	1.00	1.50	2.00	2.00	2.00	3.00
	2Y bond yield	6.75	6.60	6.70	7.00	7.50	7.60
Ghana	Policy rate	16.00	17.00	18.00	18.00	16.00	14.00
	91-day T-bill rate	23.07	21.00	20.50	20.00	19.00	18.50
	5Y bond yield	20.00	18.50	17.00	17.50	17.00	17.00
Kenya	Policy rate	8.50	8.50	8.50	8.50	9.00	9.00
	91-day T-bill rate	5.50	4.90	3.80	4.20	4.80	5.20
	10Y bond yield	12.36	12.50	12.00	11.70	11.50	11.50
Nigeria	Policy rate	12.00	12.00	12.00	13.00	13.00	13.50
	91-day T-bill rate	12.50	12.80	12.40	13.00	13.20	13.60
	10Y bond yield	13.62	13.00	13.80	14.20	15.00	16.00
South Africa	Policy rate	5.00	5.00	5.00	5.00	5.00	5.00
	91-day T-bill rate	5.21	5.26	5.18	5.16	5.22	5.14
	10Y bond yield	7.56	7.65	7.55	7.50	7.50	7.60

Source: Standard Chartered Research

Forecasts – Commodities

	Market close	m/m	Change YTD	y/y	Q2 - 13	Q3 - 13	vs Fwd	Q4 - 13	vs Fwd	Q1 - 14	vs Fwd	Q2 - 14	vs Fwd	2012	2013	vs Fwd	2014	vs Fwd
	7/3/2013	%	%	%	A	F	%	F	%	F	%	F	%	A	F	%	F	%
Energy																		
Crude oil (nearby future, USD/b)																		
NYMEX WTI	101.2	+8.5	+10.2	+15.5	94	98	-3%	98	0%	98	3%	96	3%	94.2	96	-3%	99	8%
ICE Brent	105.8	+2.2	-5.0	+5.8	103	110	5%	108	4%	105	2%	102	1%	111.7	108	4%	105	5%
Dubai spot[1]	101.7	+3.0	-4.7	+4.1	101	107	-	105	-	102	-	99	-	108.9	105	-	103	-
Refined oil products cracks and spreads																		
Singapore naphtha (USD/b)[1]	-6.0	+42.5	+47.4	-43.0	-7.0	-2	-	2	-	-	-	-	-	-5.5	-2.2	-	-	-
Singapore jet kerosene (USD/b)[1]	15.9	+3.2	-9.6	-10.2	15.1	18	-	19	-	-	-	-	-	17.8	18.1	-	-	-
Singapore gasoil (USD/b)[1]	18.1	+5.4	+23.2	+8.3	16.4	18	-	19	-	-	-	-	-	17.1	18.1	-	-	-
Singapore regrade (USD/b)[1]	-2.2	+23.9	-174.9	-315.8	-1.3	-1	-	-1	-	-	-	-	-	0.6	-0.5	-	-	-
Singapore fuel oil 180 (USD/b)[1]	-2.9	+19.4	-74.3	+271.9	-3.8	-7	-	-6	-	-	-	-	-	-3.3	-6.0	-	-	-
Europe jet (USD/b)[1]	15.5	+13.2	-8.2	-14.8	14.4	15	-	14	-	-	-	-	-	18.4	15.6	-	-	-
Europe gasoil (USD/b)[1]	13.1	+9.7	-2.0	-27.1	12.6	17	-	17	-	-	-	-	-	16.3	15.3	-	-	-
Rotterdam 3.5% barges (USD/b)[1]	-12.0	-5.2	-41.2	+34.7	-11.9	-11	-	-13	-	-	-	-	-	-12.4	-12.9	-	-	-
Coal (USD/t)																		
API4	73	-10.3	-18.4	-19.1	81	84	13%	87	12%	87	8%	88	6%	93	84	11%	88	5%
API2	74	-4.8	-17.7	-18.1	81	83	9%	85	5%	88	5%	90	5%	94	84	7%	90	3%
globalCOAL NEWC*[1]	79	-10.1	-16.2	-11.6	86	86	-	90	-	92	-	90	-	97	89	-	91	-
Metals																		
Base metals (LME 3m, USD/t)																		
Aluminium	1,807	-6.8	-12.5	-7.3	1,871	2,000	12%	2,100	15%	2,200	19%	2,200	17%	2,052	2,003	11%	2,200	17%
Copper	6,993	-6.8	-12.4	-10.0	7,198	7,500	7%	7,750	11%	8,500	22%	8,500	21%	7,948	7,600	9%	8,500	21%
Lead	2,078	-7.0	-10.7	+9.1	2,066	2,200	6%	2,200	6%	2,400	15%	2,400	14%	2,074	2,193	5%	2,400	14%
Nickel	13,855	-9.4	-18.8	-18.2	15,060	17,000	23%	17,000	22%	18,000	29%	18,000	28%	17,583	16,605	20%	18,000	28%
Tin	20,055	-4.5	-14.2	+4.9	20,975	24,000	20%	24,000	20%	24,500	22%	24,500	22%	21,113	23,258	16%	24,500	22%
Zinc	1,860	-4.7	-10.1	-1.4	1,876	2,000	8%	2,100	12%	2,300	22%	2,300	21%	1,965	2,007	8%	2,300	20%
Iron ore (USD/t)																		
Iron ore[2]	124	-9.5	-	-8.8	126	112	-	127	-	127	-	129	-	129	128	-	120	-
Steel (CRU assessment, USD/t)**																		
HRC, US[1]	639	-3.5	-	-13.3	651	606	-	576	-	759	-	789	-	724	628	-	734	-
HRC, Europe[1]	614	-5.4	-	-10.6	631	606	-	559	-	564	-	581	-	666	615	-	576	-
HRC, Japan[1]	589	-3.8	-	-28.8	601	605	-	598	-	620	-	669	-	820	613	-	669	-
HRC, China[1]	605	-4.0	-	-13.7	618	562	-	600	-	650	-	675	-	654	615	-	651	-
Precious metals (spot, USD/oz)																		
Gold (spot)	1,253	-10.4	-25.2	-22.4	1,417	1,400	12%	1,500	20%	1,500	19%	1,500	19%	1,669	1,487	19%	1,500	19%
Palladium (spot)	685	-9.0	-3.0	+14.8	714	750	9%	800	16%	850	24%	850	24%	645	751	9%	850	24%
Platinum (spot)	1,344	-9.3	-12.1	-8.4	1,467	1,550	15%	1,650	22%	1,800	33%	1,800	33%	1,552	1,575	17%	1,800	33%
Silver (spot)	20	-12.8	-35.2	-30.1	23.2	24	22%	25	27%	25	26%	25	26%	31.2	26	30%	25	26%
Agricultural products																		
Softs (nearby future)																		
NYBOT cocoa, USD/t	2,250	-1.4	+0.6	-4.0	2,278	2,350	5%	2,350	5%	2,400	7%	2,400	6%	2,346	2,289	2%	2,400	6%
LIFFE coffee, USD/t ***	1,794	-1.4	-8.6	-13.5	1,918	2,100	16%	2,100	16%	2,100	15%	2,100	13%	2,016	2,041	13%	2,100	13%
NYBOT coffee, USc/lb	121	-5.1	-15.8	-32.7	132	140	15%	145	16%	150	18%	150	15%	175	140	14%	150	14%
NYBOT sugar, USc/lb	16	+0.2	-15.8	-25.3	17.1	18	10%	19	10%	20	16%	21	22%	21.6	18	8%	21	22%
TOCOM RSS3 rubber#, JPY/kg	247	-5.5	-18.4	-3.8	259.3	320	-	320	-	315	-	320	-	274.3	301	-	323	-
Fibres																		
NYBOT cotton No.2, USc/lb	84	-0.2	+12.3	+16.0	85	90	4%	80	-7%	90	6%	90	6%	80	84	-2%	90	9%
Grains & oilseeds (nearby future)																		
CBOT corn (maize), USc/bushel	678	+2.7	-2.9	-5.6	661	650	19%	625	24%	660	28%	660	25%	694	663	19%	685	30%
CBOT soybeans, USc/bushel	1,584	+3.6	+11.6	+0.7	1,468	1,450	5%	1,400	12%	1,350	7%	1,400	11%	1,464	1,441	5%	1,375	10%
CBOT wheat, USc/bushel	658	-7.2	-15.5	-15.9	695.4	725	9%	730	7%	740	7%	750	7%	750.3	722	8%	748	6%
CBOT rice, USD/cwt	15	-0.8	+3.6	+4.6	15.5	16	5%	16	3%	15	-5%	15	-6%	14.9	16	2%	15	-5%
Thai B rice 100%, USD/tonne*[1]	540	-3.4	-10.6	-13.0	571	625	-	625	-	630	-	630	-	589	606	-	630	-
Edible oils (nearby future)																		
Palm oil (MDV,MYR/t)	2,359	+0.9	+1.8	-23.7	2,356	2,600	10%	2,750	17%	2,800	18%	2,850	19%	2,959	2,541	8%	2,819	18%
Soyoil (CBOT, USc/lb)	47	-2.8	-3.9	-10.8	49	51	9%	50	9%	53	15%	47	2%	53	50	8%	54	18%

**weekly quote **monthly average ***10 tonne contract; [1]no forward price comparison available; [2]cost and freight at China's Tianjin port, 62% iron content, Indian origin; #6th contract;*

Sources: Bloomberg, Standard Chartered Research

Standard Chartered

Disclosures Appendix

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