Trip Notes

IMF Annual Meetings Fall of 2022

Aktia

This is a marketing communication. Please refer to the prospectus of the UCITS and to the KIID before making any final investment decisions.

IMF Meetings

Overview

- The IMF-WB Annual Meetings were organised in physical form for the second time following the Covid pandemic. Aktia's Emerging Market team travelled to Washington D.C. to participate in the side-line events that were organised in connection to the International Monetary Fund (IMF) Annual Meetings. In this report, we report about our key takeaways and investor discussions on both a general level and a few chosen countries that we had meetings with.

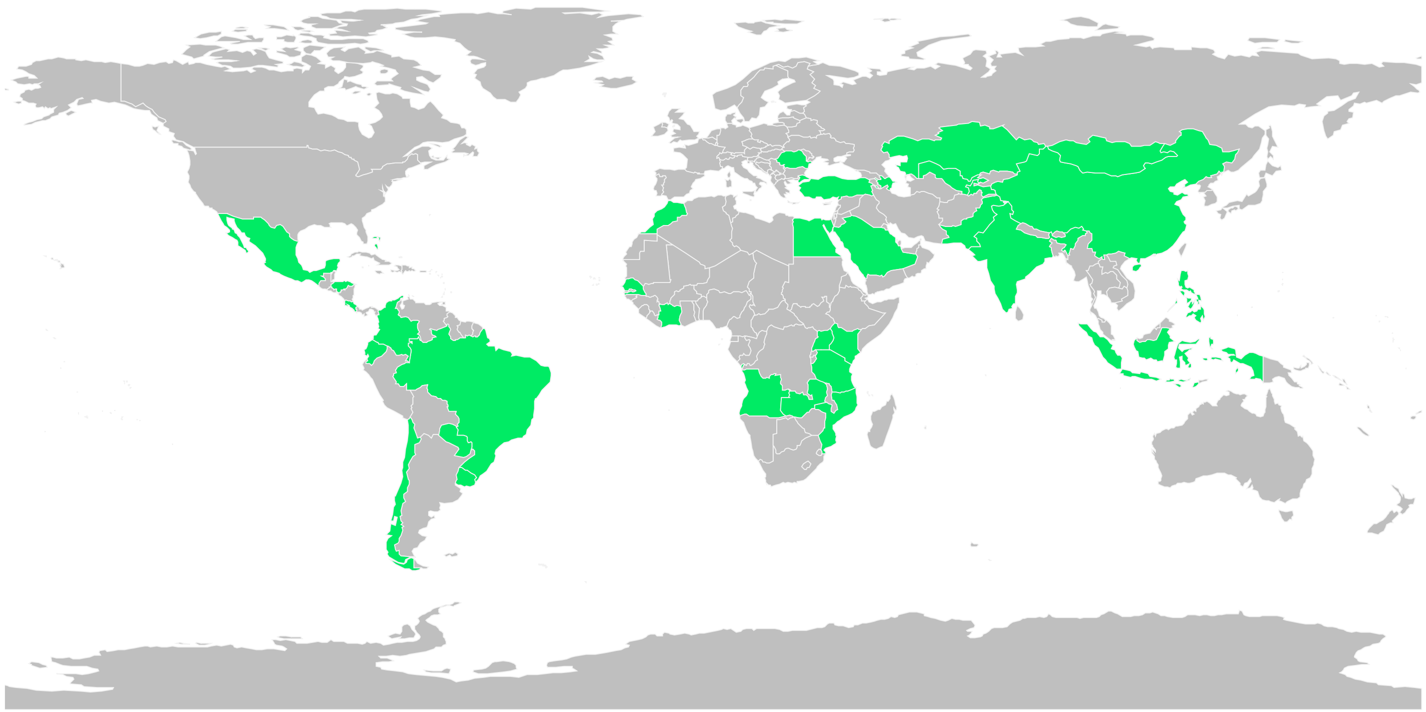
- In total, we had 42 meetings with the IMF Mission Chiefs, finance ministers, central bankers and other staff from their organisations covering 34 different emerging and frontier market countries. This year's meetings focused on multiple crisis that emerging and frontier markets are facing and how countries will get through these turbulent times.

- The IMF's latest World Economic Outlook (WEO) was published during the annual meeting. According to the WEO's outlook, growth divergence between advanced and emerging market and developing economies will increase. Emerging market and developing economies growth is expected to be more resilient as their growth for 2022 was modestly upgraded from July's 3.6% forecast to 3.7% despite being revised down from 3.9% to 3.7% for 2023

- Naturally Russia's invasion of Ukraine and its spillover effects on the global economy was on the forefront in each meeting. Uncertainty about how long the war will continue makes forecasting difficult.

- An important topic in all meetings was the role of central banks in simultaneously tackling inflation and avoiding pushing economies into recession. The monetary policy transmission mechanism for traditional emerging markets and especially frontier economies might not be working well currently. However, the role of policy signalling remains important. As interest rates rise and countries face costlier and scarcer financing, growth can be expected to slow.

Aktia EMD team's country meetings alongside the semi-annual IMF meetings



Africa: Angola, Ivory Coast, Kenya, Mozambique, Senegal, South Africa, Tanzania, Uganda, Zambia

Asia: Azerbaijan, China, India, Indonesia, Kazakhstan, Mongolia, Pakistan, Philippines, Tajikistan, Uzbekistan

Central America and the Caribbean: Bahamas, Costa Rica, Honduras, Mexico

Europe: Romania, Turkey

Middle East and North Africa: Egypt, Morocco, Saudi Arabia

South America: Brazil, Chile, Colombia, Ecuador, Paraguay, Uruguay

IMF Meetings

Overview

- Many frontier countries no longer have access to international capital markets creating the demand for alternative ways to finance budget deficits. China's role as a major creditor to many frontier economies was brought into question. Additionally, there is a significant lack of transparency in the extent of the debt and the terms negotiated. Furthermore, China does not have a track record of restructurings or doing restructuring with the Paris Club (a group of major creditor countries).

- China's potential slowdown and its impact on the global economy was also mentioned. China's 20th Communist Party Congress that started right after the IMF meetings will provide clarity about the party's leadership and policy. Additionally, China's stringent zero-Covid policy and China's reopening was speculated; whether and when China will open as the rest of the world has done. Cross-border opening might be even more distant, but Asian economies will benefit when that happens.

- The G20 Common Framework for Debt Treatments, agreed in November 2020, was seen to have failed. So far three countries – Chad, Ethiopia, and Zambia – have requested for debt relief under the framework, but there have been no results. Zambia is a true test case: how long will it take for all parties to sign the Memorandum of Understanding? The real challenge is how to make the process quicker and include private investors from the beginning.

- Climate change was often mentioned by those countries most vulnerable to it as they need to take it into account, for instance, when planning new government infrastructure projects. The World Bank will launch a new fund called SCALE (Scaling Climate Action by Lowering Emissions) to mobilise billions of dollars to fight climate change.

- Domestic food production in the context of Sub-Saharan African countries was discussed. The Food Shock Window, the IMF's new program, was of interest to many investors who were eager to understand which countries would be eligible for that.

- As the Federal Reserve continues to tighten monetary policy, the strengthening US dollar has created challenges to those emerging and frontier markets that are dependent on imported goods priced in dollars or have dollar-denominated debt.

IMF Meetings

Latin America

Chile

- Chile had one of the fastest rebounds after the pandemic due to releasing pension funds for their citizens to spend. Growth in 2021 was a staggering 11.7% according to IMF which was not considered to be sustainable. Growth in 2022 is forecasted to moderate to 2% and to fall to recession territory at -1% in 2023.

- Inflation is forecasted at end of the year at 11.2% and for 2023 to be at 8.7% at year end. This is mainly driven by unsustainable domestic demand but also supported by the shock on food and oil prices. Chile is a large importer of energy which has pushed inflation higher. The current account is also in deep negative territory at -6.4% in 2022 projections and forecasted to be -4.4% in 2023 by the IMF. This is a major deficit especially as Chile is a large exporter of minerals, especially copper.

- The central bank has been active in raising rates due to heightened inflation. However, in October it announced that it will stay put after their most recent 50 basis points hike. They are monitoring the financial and economic indicators which all are pointing towards recession, which should help push inflation down and the current account towards more sustainable levels. The central bank is forecasting that inflation will fall towards its target of 3-4% in 2024.

- There was a huge fiscal balance change between 2021 and 2022. In 2021 the fiscal deficit was at 8%. Now it is forecasted to switch to a fiscal surplus of 2% in 2022. The fiscal surplus will change to a fiscal deficit again in 2023, but only at -1.2% according to IMF. The largest expenditure change will be a rise in social expenditures of 8 percentage points, but tax revenues are forecasted to grow due to the income tax reform.

- The constitutional reform was voted down, and as such a new process is under way. Interestingly even thought the reform was voted out with a clear majority, the popularity of building a new constitution is at its highest level at 80%. As such, it is expected that uncertainty over the path of the Chilean politics should calm down once the new constitution is agreed on. A pension reform proposal is planned to present to Congress at the end of October, with the new design which should allow pension firms to focus on being asset managers and adding a social security component to pensions for low pension households. It is also expected to recover the withdrawals faced during Covid within seven to 10 years.

- **View:** Despite the political noise surrounding the new constitution, we have kept our investments in Chile. The current yield level at the short end is attractive. Relative to its peers the economic challenges are manageable. We have also position in our hard currency –strategy but it is rather small (1,5 %).

Ecuador

- Fiscal numbers are solid, and growth is moderate. The IMF's GDP estimates for 2022 and 2023 are 2.9% and 2.7% respectively. The current account is in a strong state at 2.5% of GDP. The trajectory is for it to balance out by 2025. Also, the fiscal balance is in positive territory, with projections of 0.9% and 1.9% for 2022 and 2023 respectively.

- Personal consumption growth has remained strong at around 5%. This has been main driver behind GDP growth. What Ecuador is missing are investments from a growth point of view. However, the shrimp industry is booming growing 20% on an annual basis. The mining sector still is still behind the curve, but the outlook is promising.

- There are new investments both in the oil and mining sectors. Current oil production is 500,000 barrels a day and the government's goal is to maintain this level going forward. To keep and increase current production levels, there is new oil project, Intracampos II. It consists selling oil exploration and development rights to a total of six areas, worth of total of USD 3 billion in investments. The estimated future production is between 18,000 to 24,000 barrels a day. Private sector involvement is seen essential for the project. On the mining side there is a new project called Cascabel which is currently being studied for feasibility. The total size of the investments is around USD 5 billion for both construction and production. If all goes as planned, production could start from 2025 onwards and success of the project could cement Ecuador as the next copper frontier.

- Ecuador's current problems arise from the political side. 80% of Ecuadorians are saying that the country is going in the wrong direction – political trust is gone. Problems arise in the lack of a communication strategy, crises in police, increasing crime rate, corrupted jail system to name a few. The government lacks the capacity in execution regarding the government budget. There has been large scale protests against the government and President Lasso. The is pressure from different indigenous groups (to name one, CONAIE (The Confederation of Indigenous Nationalities of Ecuador), for example). Negotiations between Lasso and CONAIE have been going on for some time, but progress has been very slow – there has apparently been over 200 agreements, but there are still almost 100 unresolved issues on the table. The main areas of discussion have been around labour rights, education, banking, subsidies (fuel), mining and oil sector rights and so on.

- There is a high probability that the country will face a referendum vote in the near future due to these disputes. However, this would require a change in current laws before it could materialise. According to current plans, altogether there would be eight questions. However, a *no* vote would, in essence, mean the end of Lasso's presidency. The current situation is very uncertain. Around 55% are in favour of Lasso if even that. Lasso is trying to survive until the next elections in 2025. Impeachment has been on the table but the reasoning behind it has not been strong enough. Furthermore, opponents are lacking a true leader who could challenge president Lasso. A crisis scenario would stem from failed negotiations with indigenous groups (this has a 25% probability) which would mean that protests would be back, and the assembly would challenge the government (has taken a more united approach recently). Under this scenario, new elections would likely follow.

IMF Meetings

Latin America and Africa

- There is a high probability that if there is a new government, fiscal consolidation would be forgotten and there would be a spending spree to keep Ecuadorians satisfied. This was seen during the last economic model, built back in 2007.

- On the financing side, many avenues are still open for Ecuador; going to the IMF is an option and the country has signalled its willingness to have a program in place. Country could qualify already in December for IMF's RST (Resilience and Sustainability Trust). China is another option. Ecuador could raise as much as USD 5 billion via China's commercial channels. The government is also forcing local banks to take more debt which could in turn help the government.

- Currently, the government is expected to honour debt obligations according to Analytica, but one has to remember that Ecuador has a history of serial defaults.

- **View:** Ecuador is still a solid case based on economic figures. The political side is messy, however. This will also place a drag on reforms and budget execution. There are no easy solutions or quick fixes although there is some comfort in the fact that long negotiations between government and indigenous groups have resulted in more agreements than unresolved issues. We are cautious but still maintain our position in Ecuador. We believe that the current pricing of bonds reflects the issues the country is facing.

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Angola

- Angola's economic performance turned positive last year (0.8%) after five years of negative real GDP growth. The share of non-oil sector growth has been encouragingly increasing, thanks to the government's strong emphasis on reforms diversifying the economy from oil dependency. Growth trajectory is expected to continue positive, and the IMF sees real GDP growth at 2.9% in 2022 and 3.4% in 2023.

- General elections in August reaffirmed power of the ruling party MPLA and President João Lourenço, which enables reforms to continue. The same economic team continues making the IMF engagement easier in the post-program monitoring phase. The IMF sounded to be pleased with Angola's progress and the Article 4 mission is still planned to take place this year.

- The National Bank of Angola has had a very minimal intervention in the foreign exchange market after moving towards floating exchange rate regime. Angola's currency, the kwanza, has been strongly appreciating this year (nearly 40% against the U.S. dollar this year) and curbing imported inflation. Inflation is still running high, 19.8% y-o-y in August, but the central bank is determined to achieve single-digit inflation by 2024. The IMF sees single digit-inflation, 6.4%, achieved in 2027.

- Angola has been heavily relying on external debt: total debt peaked at 135.1% of GDP in 2020 after which it has been falling steadily to current levels of close to 60%. This year Angola has been proactively managing its debt burden and lengthening maturity profile. However, a big part (about 40%) of Angola's debt is owed to China and there is little knowledge about China's terms. There is a mechanism triggering repayment at certain threshold price for oil, so Angola has been repaying debt to China with oil proceeds.

- Regarding next year's budget it will be important to see that spending will be reined in (e.g. oil subsidies) and debt continues to be brought down. Privatisations of state-owned enterprises are only in initial stages and have not yet generated large proceeds. The IMF expects a current account surplus of 11.3% in 2022 and 5.4% in 2023.

- Investors are highly interested in Angola, although Angola has only very slowly and partially started to open its capital account to offshore investors. The IMF is advising Angola to do this gradually and carefully understanding challenges with process and competences to manage 'hot money' flows considering that Angola has only recently let the FX float more freely.

- **View**: Considering the current gloomy outlook Angola is one of the 'bright spots' on the African continent. Angola seems to be very committed to reforms, but as always implementation is what counts. There are huge infrastructure investment needs to diversify the economy from the oil sector. Angola's long-term goal is that in 2015 the oil-sector will account 15% of GDP and role of the agricultural sector will be large in this transformation process. In our local currency strategy, we invested in Angola through currency forwards in September. We have also positions in USD bonds in our hard currency strategy; we believe Angola has potential relative to its peers.

Mozambique

- Mozambique continued its recovery from the Covid pandemic, GDP growing at 2.3% in 2021. The IMF projects growth to be 3.7% this year. Growth is driven by agriculture, construction, and tourism. A nation with several challenges is highly vulnerable to climate change. Floods and cyclones continue to trouble the country.

IMF Meetings

Africa

- The nation's opportunity lies in the liquefied natural gas (LNG) sector which is expected to start generating revenue in November as the Italian energy multinational Eni operated offshore Coral South platform should commence production. In the long term, the LNG sector is expected to account for about 20% of GDP compared to a few percentages in the medium term. Mozambique's highly negative current account deficit (-22.9% of GDP in 2021; -45.9% in 2022) is explained by big investments in the LNG sector financed by foreign direct investment. The non-LNG linked current account deficit is funded by donations and concessional money. The IMF program had a first review in September. Following the board's approval in December, this will unlock much needed disbursement. There is a possibility of accessing additional funding through the resilience and stability trust program, which would be used to fund climate change mitigation, but at earliest in spring. Furthermore, due to improved corruption mitigation Mozambique has unlocked concessional financing from the World Bank and IMF.

- Mozambique has serious security challenges in the northern province of Capo Delgado where the French energy company TotalEnergies SE LNG project is located. According to the government, the security situation is stabilised now, but there is a joint team from Rwanda and the Southern African Development Community (SADC) controlling the situation. TotalEnergies suspended the project and will make the decision of continuing the project before end of this year. Total's investment is around USD 20 billion, which is larger than the country's annual nominal GDP.

- Fiscal space is a challenge and Mozambique has ongoing bilateral discussions with its creditors to lengthen the maturity of loans to allow the government to make much needed infrastructure investments that needs to be built in a climate resilient manner. Debt is unsustainable and there are ongoing public debt litigations.

- The central bank of Mozambique has aggressively hiked rates by 400 bps this year to 17.25% to fight inflation. Annual inflation was at 8.8% in September. The IMF is expecting inflation to rise to 11.3% by the end of 2022. FX reserves have declined to USD 2.8 billion, covering less than four month's worth of imports. The country's banking system have been experiencing U.S. dollar shortages.

- **View:** The central bank is protecting the economy from abrupt moves of foreign investor money and keeping the exchange rate of the metical stable, which is attractive from a local currency investors' perspective. Access to domestic government bond markets is currently not possible, although it was earlier. We only invest through currency derivatives when there are attractive levels. If offered, we would consider DFI notes depending on yield levels. We do not hold any position on the hard currency side currently.

Uganda

- Uganda's economic outlook has also become more challenging. In addition to global challenges, there is a domestic component in the form of prolonged droughts in north-eastern Uganda. Work on the oil sector is moving forward and is considered in the IMF forecast projecting the medium-term growth of 6%.

- The EU has raised concerns about environmental issues related to the oil pipeline, but Uganda will not wait for the EU's approval as they have started oil exploration already 20 years ago and put enormous effort on this. Uganda is saying that no one is going to delay them anymore and oil extraction is expected to begin in 2025-26. The entire oil project investment is estimated to be USD 15 billion of which about 80% will be exports and 20% will be used in local expenditure. Multiplier effects have started to appear.

- Uganda's budget deficit of -7.5% of GDP is large and the current account has deteriorated sharply (IMF projection for 2022 is -8.0% of GDP) because of unfavourable terms of trade. According to Ugandan officials, Uganda does not have subsidies as they do not have fiscal capacity to provide subsidies. Revenues from the oil sector are still highly uncertain. The current IMF program is driving reforms in the areas of revenue mobilisation and spending rationalisation, governance, and budget transparency.

- The main source for Uganda to finance the twin deficit is domestic commercial borrowing, for which Uganda pays high rates of 17-18%. This has also crowded out domestic private sector lending as credit growth plummeted to 1% in August in real terms to previous year when it was 6%.

- The debt-to-GDP ratio has increased close to 50% from the lows of around 25% in 2015-16. Planned fiscal consolidation will help bringing debt-to-GDP down, but the growing interest burden is a concern.

- Inflation quickened to 10% in September and the IMF is forecasting inflation to be 6.4% in 2022. The Bank of Uganda has hiked the policy rate 350 bps in total, the central bank rate being at 10% in October. The new central bank governor is still waiting to be nominated. Also, President Museveni not having succession planning is worrying.

- The IMF has assessed the Ugandan shilling to be overvalued. The exchange rate has been under pressure this year depreciating against the US dollar over 7%. The Bank of Uganda has allowed the depreciation to happen as they do not want to risk reserves and there was significant excessive liquidity in the system after the Covid pandemic. The international reserves of USD 3.7 billion are only moderately less than in the spring around USD 4.0 billion.

- Investors were complaining about the unclear treatment of taxation of local bonds as there seem to be double taxation and there has been no action from Uganda, although the recommendation was put on already last year. The share of non-resident investors on the local government bond market has come down significantly to 8.5%.

- **View:** Despite the twin deficit and increasing debt, we are confident on the Ugandan investment narrative. Ugandan local markets provide positive high real rates to investors. In our frontier local currency strategy, we are invested both in local government bond markets and in currency forwards.

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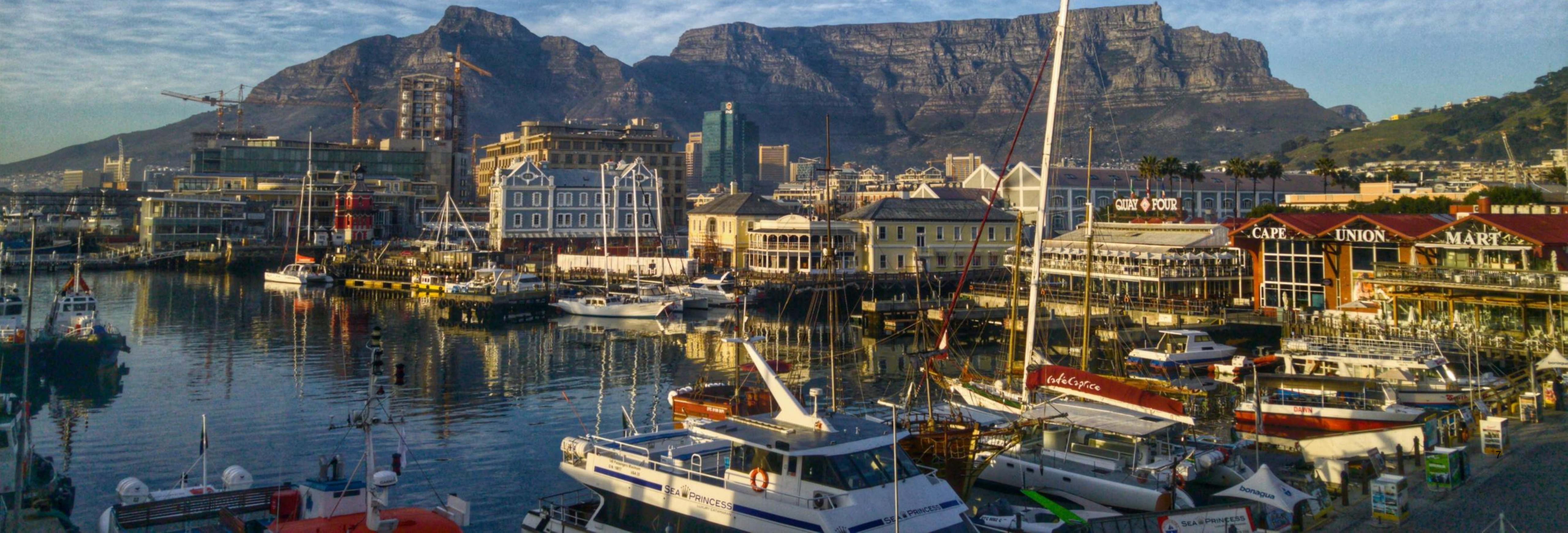

IMF Meetings

Africa

Ivory Coast

- Ivory Coast has been known to have been very stable with a solid growth story, only moderate debt and being well anchored with WAEMU (West African Economic and Monetary Union) membership. During the meetings question arise whether these positives will be challenged in the future by higher financing cost as US rates are increasing, widening current account deficit (-6 %) and no signs of improvement coupled with growing concerns on security issues. From an investors' point of view, more actual action plans to tackle these issues are needed going forward.

- Growth was 7% 2021, now closer to 6% but the trajectory is downwards. Regarding inflation, the country has been lucky and currently inflation is running at 6%. Inflation has been rising but has recently shown clear signs of moderation.

- One key factor going forward is revenue mobilisation which is needed for medium to long-term. There are already signs that reforms are going in right direction as tax revenues are increasing.

- Fiscal deficit has creeped higher due to fuel subsidies, benefits and allowances during these challenging times. For this year there is an estimate of a -6% fiscal deficit. For 2023 the respective projection is -4.8%. Budget consolidation is happening but only at a very slow pace. This is something were the IMF wants to see improvements, a more speedy consolidation of the budget and the removal of subsidies.

- Financing is done for 2022 but for 2023 all options are examined. For now, the USD 900 million Special Drawing Rights (SDR) allocation is in place as also is access to regional markets. For international investors there must also be access to regional markets – this is a clear focus area and the debt office is very robust and capable to deliver.

- With WAEMU membership there are also targets and goals to be met. The union has a goal to reach a fiscal deficit of -3 % by 2024. For Ivory Coast, the fiscal deficit is running at -3.4% for 2022 and -1.9% for 2023 based on IMF figures. The debt-to-GDP ratio is expected to reach 50% by 2024 (currently 56%). However, the IMF sees the Ivory Coast reaching a debt-to-GDP level of 50% only by 2025. Reserves are currently running at six months worth of imports. The debt service to revenue ratio for the Ivory Coast is near 60%, but still below threshold, and the IMF is not too worried about this for now.

- With oil production Phase 1 will be completed in 2023 and goal is to start moving towards Phase 2 in the next three years.

- Going forward one of the most important things for Ivory Coast is the strength of policy reform as funding channels are already in place. The government is dedicated to continuing its National Development Plan (NDP) and its second generation. The NDP consists of five pillars around peace, security and social cohesion, job creation, creating a pleasant quality of life and an attractive investment environment throughout the country, building a more efficient and committed administration.

- **View:** The Ivory Coast has been one of our and global investors favourites for some time already. The country is very stable, it has solid growth, only moderate debt metrics and it is well anchored by WAEMU membership. There are some clouds gathering, but on a relative basis we see this is still solid credit compared to some of its peers. We have a position in bonds.

Kenya

- Growth has been robust at 5.3% in 2022 according to the IMF, and growth in 2023 is forecasted at 5.1%. The new government has indicated new policies to improve growth prospects in the future. Focus is on making the investment climate better and privatisation of inefficient state owned enterprises (SOEs). The agriculture sector is a focal point to improve food security.

- The new government is committed to following the IMF's recommendations and achieving fiscal consolidation. There have already been surprises to the positive side. The government announced a new expenditure cut of 2% of GDP which will target SOEs. There is a large issue with inefficient SOEs which are supported through the government budget; the goal is to privatise these companies now. But oil subsidies are still online which has been costly for the state budget, albeit there were strong signals that they will end by the end of the year.

- Fiscal consolidation in 2022 was already a success, as the primary deficit came in at 1.5 percentage points tighter than forecasted, mainly driven by a 0.8 percentage point overperformance in tax revenues. Overall, the deficit is still high and forecasted at 5.3% per GDP for 2023. There is still a lot to be done to achieve on the fiscal consolidation front, but these are good steps. It is a positive sign that the new government is proactive in engaging with the IMF and has shown commitment to fiscal consolidation.

- There has been a dollar shortage in Kenya lately, which was a large cause for concern for many of the investors present at the meetings. It seems that the dollar shortage was due to elections where risk aversion made households increase dollarisation. Lower exports also contributed to this. The situation should improve as election uncertainty fades and the economy goes back into full action

- Kenya's largest issue right now is the large 2024 maturing hard currency bond. Right now, Kenya has no access to the market and as such is trying to find alternative solutions to finance the maturity. The new government is looking at new tools and new funding options for financing. One option that was actively discussed was a domestic hard currency bond, the reception to the idea was mixed.

- **View:** Despite recent inflation prints being above the central bank target range of 2.5 % -7.5 % at 9.2%, and is expected moderate only after Q1 2023, the local infrastructure bonds offer an attractive positive real yield. Positive developments under the IMF guidance support the investment case, with slight caution due to recent dollar shortage and strong shilling. We hold also position in USD –denominated bonds in our hard currency –strategy.

IMF Meetings

Asia

Azerbaijan

- Azerbaijan's economy has been fairing surprisingly well despite the external shocks supported by high hydrocarbon prices. The IMF is forecasting GDP growth to moderate to 3.7% in 2022 and further to 2.5% in 2023. Inflation is higher and stickier inflation due to the war, expected to be 12.2% in 2022 and 10.8% in 2023.
- There has not been an influx of Russians to Azerbaijan, only some small numbers for short-term tourism. This is probably because Russia took Armenia's side in the last war.
- Europe sees Azerbaijan as one of the new suppliers of gas, but Azeris expect Europeans to make the needed substantial investments to get gas flowing to Europe. The pipeline to Europe must go through several countries which raises several sensitive issues like environmental issues and politics. Some think that Azeris are not going to invest their money on something that does not have certainty of working. Azeri authorities are very strategic and want to keep good connections.
- Azerbaijan has a vision of going for more green energy in domestic consumption. Renewable energy (including hydropower) is currently approximately 20% of total domestic consumption.
- The IMF sees fiscal policy much more disciplined and responsible. Fiscal adjustment is needed regarding the non-oil primary balance and is achieved by tax reform and caution on spending side. Azerbaijan has revised its fiscal rule with assistance from the IMF, which is more flexible than the earlier one. Azeris have learnt their lesson about big spending leading to crisis in 2015-16 brought by a decline in oil prices and the same politicians are still there to make decisions. Oil revenue is declining, so Azeris understand that oil wealth needs to be used wisely to benefit future generations.
- Azerbaijan has a sizable current account surplus which the IMF estimates to be 31.7% of GDP in 2022 (15.2% in 2021).
- The IMF has been recommending further tightening of monetary policy, but the Central Bank of Azerbaijan has not been following the advice. Inflation is becoming stickier and across the CPI basket. Azerbaijan has the lowest policy rate in the region, but not the lowest inflation. The IMF is afraid it is too late to contain inflation.
- The new Central Bank Governor looking to modernise the monetary framework: moving gradually to inflation targeting and flexibility of the exchange rate. Currently, monetary policy transmission is weak.
- There are no major risks in the banking sector that would endanger the economy. Azerbaijan's banking sector is naturally protected because it is small relative to the economy (less than 50% of GDP).
- **View:** A hydrocarbon exporter with a very low debt burden (less than 20% of GDP), but long-term success depends on policy decisions to diversify the economy. Possible further escalation in military tensions between Azerbaijan and Armenia is a risk for the economy. We have added exposure to Azerbaijan in our frontier local currency strategy this year. We also have a position in our hard currency strategy but have reduced the size mainly for risk management reasons.

Mongolia

- There are several positive developments in the Mongolian economy after returning to normal after the Covid pandemic. The economic recovery has stimulated pent-up demand reflected in a higher import bill. China's zero-Covid policy resulted in prolonged closures of the Mongolia-China border hampering exports transported by trucks, but the number of trucks crossing the border daily has returned to normal and even exceeding the pre-pandemic levels, which has depleted inventory levels. Mongolia has completed building two railway projects to China that will boost exports.
- Mongolia's economy is very dependent on China: China accounts for at least 85% of its exports, over 30% of its imports and more than 60% of its overall economy. A downside risk is that China's demand will slowdown drastically, although Mongolian authorities seem to have solid trust on high level assurances received from China and believe that exports will continue at their current levels.
- The IMF raised its 2022 GDP growth forecast for Mongolia from April's 2.0% to 2.5% in September, because the main export season is ahead in the fourth quarter. However, for 2023 the GDP growth forecast was revised down to 5.0% from 7.0% on the back of high inflation (IMF forecast: 14.8% in 2022) and exchange rate depreciation which will start to impact household consumption. The economic outlook for next year will probably weaken due to balance of payments pressures.
- Mongolia is very focused on SOE infrastructure investments which is expected to eventually lead to higher exports. However, the government is not prioritising and sequencing the investments and all capital goods are imported. Projects are financed either through the budget or exports, which is not sustainable. 2024 will bring with it elections, so this is the government's last chance to make such investments during this political cycle.
- Mongolia has started to take the right policy changes towards more progressive income taxation which would enhance revenue mobilisation. Mongolia has a flat income tax rate of 10% for all tax brackets which is the lowest in the world. Rich people are benefiting from this, and the government has been hesitant touching this, although progressive taxation would easily enhance government revenue.

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Mongolia's economy is very dependent on China: China accounts for at least 85% of its exports, over 30% of its imports and more than 60% of its overall economy.

IMF Meetings

Asia

- The country has shown strong resilience against the Covid-19 economic downturn, and the growth rebound has been strong. The growth outlook is solid with the IMF expecting growth to be 6% p.a. over the medium term (local authorities have somewhat lower growth expectation).

- The Bank of Mongolia has aggressively raised rates by 600 bps to 12% this year. It has allowed more flexibility on the exchange rate and the tugrik has sunk 19% against the US dollar this year. There is US dollar scarcity in Mongolia due to a high import bill. The dollarisation level of the economy has gone up to 35%. FX reserves have fallen 40% to just USD 2.6 billion from USD 4.5 billion from the start of the year related to significant current account deficit (IMF forecast for 2022: -20.3% of GDP).

- According to the central bank, Mongolia’s public debt amounts to 70% of GDP, but there are contingent liability risks associated to a large number of loss-making SOEs. The IMF sees general government debt to be 84% of GDP in 2022. Mongolia would need to squeeze the import bill by rationalising its investment plan to solve the situation. Mongolia’s dollar bonds are due in 2023 and 2024. Mongolia has not requested an IMF program.

- **View:** We have a mixed view on Mongolia as the country is so dependent on China which seems to be heading to a slowdown. Furthermore, the country is very dependent on imports and government policies seem to be overly focused on infrastructure investments ahead of next year’s elections. We have a very small allocation in Mongolia through development finance institution notes in our frontier local currency strategy. We have also small position in our hard currency strategy.

Uzbekistan

- The impact of the Russia-Ukraine war on Uzbekistan has not been as negative as Uzbekistan was expecting in the spring and Russia related risks did not materialise as feared. However, sanctions on Russia came as a shock and Uzbek banks have needed to learn to comply with sanctions. The IMF revised its GDP growth forecast from 3.4% to 5.2% in 2022, but down to 4.7% for 2023.

- Remittance flows from labour migrants (2 million Uzbek people) were expected to come down, remittance flows doubled to USD 10.6 billion in January - August 2022 (USD 5.7 billion in Jan-Aug 2021). Contrary to what was expected, Uzbek migrant workers in Russia did not lose their jobs, but they switched to official channels to send remittances back home. In the first half of 2022 about 262,000 people returned from abroad. Uzbekistan is receiving Russian citizens (net 67,000 people), of which 17,000 are IT workers – this also impacted remittance flows. Also, other reasons are impacting remittances flows like using Uzbek banks due to the lack of dollars in Russia. This increase in remittances is an exceptional event and expected to be lower in the next 12 months.

- Russia remains to be one of the main trade partners of Uzbekistan and the trade volumes between the two countries increased by 27.1% in January-August 2022 compared to previous year. Uzbekistan is putting more emphasis on regional trade and developing alternative trade routes such as through Afghanistan to South Asia. The Uzbek government does not recognise the Taleban government but has a good working relationship.

- Inflation has been quickening also in Uzbekistan due to imported inflation. The IMF is expecting inflation to be 11.2% in 2022.

- The reform agenda continues but the Uzbek authorities recognize opposing views, and this is taken into account in fiscal forecasts. President Shavkat Mirziyoyev, who was re-elected last year, is committed to reforms and private sector led growth. The IMF forecasts a fiscal deficit of 4.1% of GDP in 2022. Privatisations continue, but due to the overall market environment and several interested buyers being Russian there is a slowdown in the process. The Uzbek government does not need to privatise to receive funds, but privatisation is done to improve efficiency, governance, and develop business environment. Energy price subsidies are weighing on the budget (about USD 800 million in the 2023 budget proposal) and there are plans to gradually remove subsidies. However, events in Kazakhstan in January need to be kept in mind when they were trying to remove subsidies.

- External debt is increasing as local markets cannot provide financing for investments. External financing raised this year is going to be USD 2.5 billion of which half was meant to be borrowed from financial markets and half from international financial institutions (IFIs). Due to market conditions, all borrowing has been done via IFIs. Uzbekistan has been very successful in attracting funds from international financial institutions like the Asian Development Bank, JICA, etc. There is no need for IMF funding and Uzbekistan would not even be eligible. Next year Uzbekistan is looking to borrow another USD 2.5 billion. Offshore investors cannot now access local markets, but Uzbekistan is looking into a set-up which would allow local market access to foreigners next year.

- **View:** Uzbekistan maintains a positive investment narrative due to its reform story and its natural resources. Positive real rates are attractive from local currency investors’ perspective and Uzbekistan is one of our largest positions in the frontier local currency strategy. We have positions in hard currency bonds and have kept them throughout the year. We see that Uzbekistan is in a relatively strong position.

IMF Meetings

Asia

Pakistan

- Pakistan has recently been facing major external and internal issues and shocks. As elsewhere, the pandemic put pressures on the fiscal side. Russia's invasion of Ukraine and the subsequent increases in energy and food prices brought a second wave of issues. Higher living costs resulted in heavy resistance towards the government and last April the prime minister was ousted following an impeachment process (now former PM Khan is gaining power in opposition again and challenging the current government). Lastly, massive and devastating floods during late summer came and brought the country to the brink of collapse. The estimated losses on infrastructure due to floods are around USD 30 billion based on central bank estimates. Cotton, wheat and rice yields are in danger and the extent of losses remains uncertain.

- The central bank's growth projection for 2023 was 3-4%. For 2022 the growth expectation was lowered to 2% due to floods. Inflation is running hot at around 18-20%. The central bank's medium-term target for inflation is 5-6% and Pakistan is expected to achieve this by 2024. Due to these headwinds Pakistan's fiscal side will be very stressed. For this year, the IMF expects the current account deficit to be 4.6% and the fiscal deficit 7.8%. In terms of financing, things are better than a few months ago. Because of a constantly changing situation financing is an ongoing process. Financing channels from multilaterals, the IMF, and Saudi Arabia (already rolled forward) are open and commitments are USD 37 billion in total. There are some additional money flows coming too.

- According to the central bank, Pakistan is not seeking any debt relief from the private sector side and the current plan is to make full payments in time. The central bank also wanted highlight that it has met all targets of the IMF program so far.

- The central bank stated its objectives going forward in the following order. Domestic price stability is and will be primary object. Secondly the central bank will pursue financial stability going forward. Only thirdly will it target its tools for growth.

- There have been quite large restrictions on imports and exports, but these have almost all been removed now – 90% of imports are now flowing freely and the rest of the restrictions will be lifted in the future

- On FX management the central bank commented that it has had the goal to reduce the FX interbank markets and informal markets huge rate difference and has been lately successful on this. The outcome can be seen in growing remittances.

- **View:** Pakistan has been facing external and internal issues one after another. Fiscal situation is very challenging, and government is trying to manoeuvre between increasingly unsatisfied public (devastating floods and high living costs) and financier side wanting to see strong commitment to fiscal consolidation (remove of subsidies etc). We have position in Pakistan and situation is better now (with financings channels opened) than few months ago but at the same time we are carefully monitoring politics and how financing side are playing out after heavy losses on infrastructure.

“According to the central bank, Pakistan is not seeking any debt relief from private sector side and current plan is to make full payments in time

Indonesia

- Indonesia experienced a strong rebound in growth after the Covid pandemic shock. During the last three quarters growth has averaged around 5%. Growth has also been very broad based, but some sectors have been stronger than others. For example, the ICT sector has grown by 28% y-o-y. The IMF is forecasting growth of 5% for the Indonesian economy for 2023.

- Due to strong growth, there has been a large positive rebound in revenues as well. Tax revenues have grown 58% compared to the same point last year, which mostly can be attributed to commodity revenues due to the commodity price boom. But non-tax revenues grew 38% y-o-y as well. Expenditures grew only 8% y-o-y and as such Indonesia managed to achieve a fiscal surplus in August. The fiscal balance for 2023 is expected to be at a 2.8% deficit. Expenditures are to be cut by 3.2 percentage points.

- Energy subsidies were an issue in this year's budget. The subsidy program was planned around oil at USD 65 per barrel, which turned out to be a gross underestimate. As such, Indonesia had to cut out some subsidies and modify their subsidy plan. The new subsidy program is using USD 105 per barrel as the new pricing point. The level of subsidies has also been cut for next year.

- The central bank has practised quantitative easing during the Covid crisis. They have informed that the program will end after this year and are sticking to the plan, for now. There is an active discussion going on between the treasury and the central bank to make sure that there will not be any financial instability once the central bank starts to decrease its balance sheet.

- Due to large potential in green energy production and a large commodity sector, Indonesia is starting a sovereign wealth fund which shall be used to invest revenues and balance wealth between generations. There are large green energy investments planned, Indonesia is already a net exporter of energy and wants to improve the balance of green and hydrocarbon energy production.

- **View:** Indonesia has been one of our core holdings in both, our local and hard currency strategies. Stable politics with a strong reform agenda together with good economic fundamentals have provided steady performance.

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