

Country Governance Research Commentary

January 2018

Country Ranking Trends

Magni upgraded India for initial implementation of improved banking supervision. In some areas, implementation has been surprisingly fast, such as a shift to a regulatory approach based on risk assessment. Further upgrades will require greater independence of the Royal Bank of India (RBI) and addressing some unresolved conflicts of interest.

The modest upgrade places India at a comparable score to Indonesia and still in the middle of the countries of the emerging markets. Reform has been a priority in India for a while. Further improvements would enable India to move above several countries and into the top third of countries in the emerging markets.

Déjà vu in Germany

Germany's Social Democrats (SPD) voted narrowly to enter formal talks with Chancellor Merkel's Christian Democratic Union (CDU) to form a new government that would break a four-month political deadlock. There is cautious hope that a new administration might be sworn in by April. A "no" vote would have meant early elections by the summer. The preliminary coalition agreement contained commitments to €46 billion in extra spending on social benefits, low-income tax cuts, a new immigration policy, and backing for further European integration. The SPD had initially ruled out rejoining the so-called "grand coalition" with the CDU that has led Germany for the past 8 years and there continues to be opposition from some in the party. To reassure their reluctant members SPD party leaders have pledged to pursue further policy concessions on health, labor, and refugee policies in the upcoming negotiations. The conclusion of coalition talks will be welcomed in other European capitals who are looking for German leadership.

Implications: Germany receives among the highest Magni Country Scores of any investible country. The breakthrough, if ultimately successful, will enable Germany to maintain its strong position and to play its key role in assuring the integrity of the EU.

Rising Oil Prices Key to Masking Russian Problems

Russia's economy had been improving since sanctions and falling oil prices sent it into a deep recession in 2015, but then unexpectedly it finished last year with two consecutive quarters of contraction. The gross domestic product for all of 2017 still managed to expand at about 2 percent, and recently rising global oil prices have brightened Russia's outlook. However, sanctions have hobbled important state-owned companies and banks. In compliance with a law Congress passed last summer, the U.S. Treasury Department will soon submit details on possible expanded sanctions on Russian businessmen deemed close politically to President Putin. With sanctions expected to continue Putin has said Russia needs a new stimulus to encourage the return of Russian capital from abroad, but the space for fiscal expansion is limited with their reserve fund, accumulated over years of high oil prices, having been exhausted in late 2017 to cover budget shortfalls. Putin has stressed stability in his election campaign, and his expected reelection makes it unlikely that Moscow will tackle reforms needed for the economy to reach its full potential.

Implications: Capital has fled from Russia for some time. Some of the capital was removed from it as ill-gotten gains, while some was removed to protect it from Russian corruption and governmental meddling. Russia will likely struggle given its relatively poor governance. The current system has enriched Putin's allies while allowing Putin to retain a strong grip on power.

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Can Fresh Leadership Tap Tarnished South African Strengths?

Cyril Ramaphosa narrowly won the race last December to succeed President Zuma as African National Congress (ANC) party leader, and since taking over he has begun to prod the ANC in a new direction. Ramaphosa is expected to take over the presidency from Zuma by 2019, but a departure date for Zuma has not been confirmed. For the ANC, the key is to remove Zuma before campaigning starts as part of next year's general elections. Zuma retains the support of some in the ANC leadership, but many argue corruption allegations against him have tarnished the image of Africa's oldest liberation movement. Expectations are high that Ramaphosa can reverse the entrenched corruption and economic stagnation of the Zuma years. In what was viewed as an encouraging start, he instituted sweeping changes to the board and management of state-power utility Eskom Holdings, which has been accused of illegality and undue influence in awarding tenders. The Gupta family, which is at the center of a judicial inquiry into state capture allegations, has also had assets seized.

Implications: South Africa retains a relatively high Magni Country Score for its governance when compared to countries of the emerging markets. Ramaphosa may be able to utilize these existing strengths to address corruption and improve the economy. Perhaps the "storm clouds" over South Africa are parting.

Controversial Changes at the World Bank

The World Bank's Doing Business report has faced criticism that methodology changes made to the ranking of countries on business environment competitiveness had the appearance of being unfair and misleading. In a recent interview, the chief economist said he couldn't defend the process that led to the methodology changes. A specific focus of the criticism has been the changes in scores for Chile, and the World Bank has said they will conduct an external review of Chile's indicators. However, in defense of the objectivity of the report, the World Bank highlighted that the methodology changes implemented recommendations made following a two-year independent review, which had been open to all stakeholders. They also described Chile's recent ranking decline as due to other countries, including Mexico and Colombia, stepping up their reform efforts. The chief economist has also clarified his remarks saying he had not meant to suggest that he had seen any sign of political manipulation.

Implications: Magni does use some information from the World Bank, though the specific areas causing the controversy are not part of the Magni process and Magni Country Scores should not be affected. Magni will be watching as events unfold to determine any impact on Magni's Sovereign Qualitative Factors and hence on Magni Country Scores.