Dear Members and Friends,

Welcome in out May-June issue, marked by several exciting political, economic, and geopolitical developments. Europe and China have opened diplomatic communications channels and are engaging in intense exchanges on economic and political cooperation. The feature of the month was a G7 summit hosted by the Japanese in Hiroshima, which has highlighted the horrors of nuclear war and promoted Japan's vision of the world without nuclear weapons. Leaders have also signed a political communique summarizing main points of the discussion that they can get behind, notably, on Ukraine, economic resilience, and the transition towards clean energy. Speaking of Ukraine, Europe is putting together another package of sanctions geared towards combating existing sanctions evasion, which is important for the existing sanctions' effectiveness. In the Middle East, the Turkish presidential election has been on our radar. President Erdogan was re-elected in a high turnout, despite a tight race with soft-spoken and reformist opponent, Kemal Kilicdaroglu. Major central banks in the U.S. and Europe are nearing the peak of their monetary policy tightening cycles. Finally, the majestic Brazil – this issue's Country in Focus – is on the roll to become the world's 4th oil producer amid ambitious plan to ramp up its production capacities and the stabilizing macroeconomic environment. On behalf of The Council of Slovak Exporters' we wish you a wonderful month and enjoy another issue of May-June 2023 Export Insight. On a domestic note the revolving political door of Slovak politics aims to deliver on budget cuts amid a potentially era defining election looming in Autumn, how it will impact business will remain to be seen, but changes need to be addressed and rapidly.

Foreword by the Chairman

Lukáš Parízek

THE SINO-EUROPEAN RAPPROCHEMENT

The Chinese-European relations tumbled in recent years on the back of several geopolitical factors,

including the growing U.S.-China geopolitical rivalry, the shared transatlantic interest to break out of dependence on China citing national security concerns, as well as the divergent values and policies of China pertaining to an array of issues, from human rights, trade practices, data and privacy, the handling of the coronavirus pandemic to national security and foreign policy priorities. China's failure to condemn the Russian invasion of Ukraine has put further strain on the bilateral relationship once centered around economic interests.

But Europe is currently in the process of reformulating its China strategy,

as evidenced by several high-level political and diplomatic exchanges. Last month's EU leaders' – French President Emmanuel Macron and the European Commission President Ursula von der Leyen – visit in Beijing is a case in point, while a recent visit by China's new foreign minister, Qin Gang, to France, Germany, and Norway indicates Beijing's intention to rebuild relations with the EU away from the growing tension with the United States.

The region of Central and Eastern Europe has been hoped to yield intense and pragmatic cooperation with China.

This hope has been exemplified by several economic and diplomatic formats, notably, the massive, infrastructure-focused Belt and Road Initiative and the '17+1' format bound to increase Chinese investment in the region. The '17+1' became a diplomatic mechanism, delivering an annual summit of leaders and featuring projects, such as the Port of Piraeus in Greece, where the Chinese shipping company Cosco has been the majority stakeholder since 2016. The format may have helped generate a meaningful wave of Chinese investment especially in Hungary, as evidenced by last August announcement of Chinese

Contemporary Amperex Technology Co., Limited (CATL) to open its second European battery plant in Hungary, with an investment of EUR7.3 billion, more than three times the previous one.

Besides Hungary, however, it was mostly Western Europe – notably, Germany, France, the Netherlands and the UK – that was the biggest beneficiary

of Chinese foreign direct investment in the past years, while the promises in the rest of Central and Eastern Europe largely failed to materialize. On top of that, China's posture on Ukraine crystallized as one at odds with the region's existential security interests.

In 2021, Chinese FDI in Europe was on the rise, according to the Mercator Institute for China Studies (MERICS) analytics, but Europe's east has lower buying power, population density, and sparser infrastructure, which may make some investments less profitable, compared to Europe's west.

Last year, China's global outbound investment wavered at it 8-year low. It dropped by 23% year-on-year to USD 117 billion (EUR 111 billion), facing headwinds from its zero-covid policy and the war in Ukraine. In Europe, too, it reached a decade low of just EUR 7.9 billion in 2022, down 22% compared to 2021 but structurally changed composition for the first time since 2008, from M&A to greenfield investment, geared towards EV battery factories, according to MERICS data. The UK, France, Germany, and Hungary receiving major greenfield investments by Chinese battery makers. In that way, Europe has become a cornerstone in Beijing's global electro-mobile expansion strategy.

The EU will be compelled to increase the scrutiny of Chinese investments,

including screening measures, and additional hurdles around potential acquisitions of strategic assets on the one hand, while pursuing aggressive trade link diversification, on the other hand, to safeguard the continent's long-term economic interests.

INTERNATIONAL SPOTLIGHT

World leaders convened in Hiroshima, Japan for a G7 annual Summit on May 19-21, 2023,

in 'determination to meet the global challenges of this moment and set the course for a better future'. The leading topics discussed were the support for Ukraine 'for as long as it takes' in the face of the ongoing war; strengthening disarmament and non-proliferation efforts; undertaking a global approach to economic resilience and economic security; and, driving the transition to clean energy economies of the future through mutual cooperation. The format also launched the Hiroshima Action Statement for Resilient Global Food Security to address needs today and into the future; and talks focused also on the goal to mobilize $600 billion in financing for quality infrastructure through the Partnership for Global Infrastructure Investment (PGII). (Al Jazeera)

The European Commission proposed a new set of sanctions, the 11th packages, since the start of the war in Ukraine.

The package focuses on combating the circumvention of pre-existing trade sanctions rather than introducing new bans in still-unsanctioned areas. Contrary to Ukraine's expectations, it does not include bans on imports of Russian diamonds, natural gas, LNG, cast iron and ferroalloys, and nuclear energy cooperation, as member states are struggling to reach a consensus on these areas. Loopholes undermine the effectiveness of sanctions, so enforcing them is critical for increasing impact. The new package proposes three measures to target the circumvention of EU bans on the export of dual-use goods, advanced technologies, and critical components to Russia. Russia's military sector needs these products to produce the weapons it uses on the battlefield. (European Commission)

Now in his 20th year in power in Turkey, the president Recep Tayyip Erdogan beat his challenger Kemal Kilicdaroglu

in a Sunday second election round, which took place on May 28. Most polls predicted his rival to come on top, given the economic crisis, two devastating earthquakes, frustration among the young, and decoupling with the West and a real desire for change. Kilicdaroglu was marketed as the soft-spoken liberal leader who would roll back Turkey's increasingly authoritarian turn but Erdogan's era continues to live on. (Al Jazeera)

The month of May might have seen the peak of the U.S. Federal Reserve's monetary policy tightening,

based on the market-based measures of policy expectations. The central bank spent last year raising interest rates at a speed unmatched since the 1980s. The repricing of assets markets – as evidenced by several bank failures – and beyond. They have also sent the dollar appreciating vis-à-vis many world's currencies, with further economic knock-on effects on third countries' economies, debts, and trade. Markets are now expecting the fed funds rate to peak at around 5-5.25%. The European Central Bank's key policy rate, currently at 3.75% is expected to rise to 4.0% in the third and fourth quarters of 2023, before easing in 2024 and 2025, falling to 3.0%. (The Federal Reserve, The European Central Bank)

The U.S. is on the brink of a default, triggering its debt ceiling limit.

This means that if Congress doesn't increase the debt limit, the U.S. government will be unable to pay all its obligations in full and on time, delaying Social Security payments and Medicare benefits, food stamps, military wages, and depriving millions of Americans of income they counted on. Internationally, U.S. government bonds underpin the global financial system, so such standoff could lead to excessive volatility in equity, debt, derivative, mortgage, and commodity markets. The 2011 episode shows us that the incentives for the negotiations to drag until the very last minute are political. President Biden might trade long-term spending caps for a debt-ceiling increase that lasts until after the election but he needs to act responsibly and get the deal done to avoid default. The debt limit will be raised, the question remains, how much damage is done along the way.

V4 REGION

SLOVAKIA

WHAT'S UP

Slovakia is governed by a first-ever technocratic government led by an economist and central banker, Ľudovít Ódor. The current administration will continue to rule until the early elections in September 2023. Past government measures to help households and businesses cope with inflation, the energy crunch, and sky-high cost-of-living, increased this year's public finance deficit, the first task faced by the incoming cabinet.

WHAT'S NEXT

While in the next 5 months, the cabinet will not manage to push through fundamental reforms, it can still pave the way for the most ambitious public finance consolidation. The outgoing government pledged to reduce the budget deficit by two thirds in the next three years, which will require drastic austerity. This year, the government deficit is expected at 6.3% of GDP and should be reduced to 2.2% by 2026, the most ambitious reduction in the EU. S&P rating agency left its sovereign rating unchanged at A+ but improved the outlook from 'negative' to 'stable'.

CZECHIA

WHAT'S UP

Czechia seeks Asian export markets beyond China. Prime Minister Petr Fiala has been on a ten-day tour of six countries in South-east and Central Asia, including with stopovers in Indonesia, Singapore, Vietnam, Kazakhstan and Uzbekistan and accompanied by a business delegation which includes aerospace and defense manufacturers, such as Aero Vodochody, the Omnipol group and Excalibur Army.

WHAT'S NEXT

In 2022, only 6.2% of Czech exports went to Asia compared to the whopping 85% to other EU member-states, with Singapore and Uzbekistan being prime Asian beneficiaries. But the Czech leadership seeks to expand the links now, beyond China, with some tangible plans in place. For example, Czechia-based carmaker Skoda, a subsidiary of Volkswagen, will be opening a new factory in Vietnam.

HUNGARY

WHAT'S UP

Hungary's parliament has passed a law on judicial independence in order to unlock EU funds. The reform package aims to fortify the role of the National Judicial Council and increase the independence of Hungary's courts, including the Supreme Court and the Constitutional Court. It eliminates the executive branch's right to challenge judgements of the Constitutional Court and upholds the judiciary's powers to submit cases to the European Court of Justice (ECJ) for preliminary rulings.

WHAT'S NEXT

Hungary's economy has been suffering from low growth and high inflation, hence, its leaders are dedicated to unfreezing EU assistance. However, the European Commission will take time before it authorizes the release. Another EUR8.8bn in cohesion funds and EUR12.4bn in allocations under the post-COVID Recovery and Resilience Facility will remain locked, unless Budapest fulfils additional conditions set by the EU, especially on fighting corruption.

POLAND

WHAT'S UP

Industrial output growth in Poland arrived at -6.4% on an annual basis in April, and -14.8% compared to the previous month, revealing underlying weakness and raising concerns about economic growth in the second quarter of the year.

WHAT'S NEXT

Relatively strong labor market will remain pro-inflationary resulting in more persistent core inflation, and headwinds to growth. Employment grew by 0.4% year-on-year in April, while nominal wage growth dynamics slowed to 12.1% annually.

COUNTRY IN FOCUS BRAZIL

Several headwinds have been dragging down Brazilian GDP growth in 2022,

with a contraction in the final quarter of last year. The new administration released its fiscal framework, charting how it plans to soothe government debt, which it has struggled with due to pandemic and pre-election expenditures. Inflation, while still lingering above the central bank's target, is receding. Finally, despite weakness in the global economy, exports and foreign direct investment should remain at robust levels.

In a chain of economic good news, the country has launched a program, which would step up investments in oil and natural gas exploration to use its abundant natural resources, promote regional development and foster production,

with the aim to generate private and public revenues, jobs and enhance living standards.

Based on assessments, the resumption of environmental licensing could bring vast economic benefits:

it would have the potential to generate state revenue of $200 billion, if 10 billion barrels of oil were discovered and produced in the region, in addition to generating hundreds of thousands of jobs. The oil and natural gas sectors, moreover, can become the driving force behind Brazil's development, accounting for as much as 15% of the Brazilian industrial GDP. A meaningful progress could also send a positive signal to markets and potential investors.

The program could make Brazil the 4th largest oil producer in the world,

while the country could reach 5.4 million barrels of oil per day by 2029. Amid the global competition for investments, the need to replenish oil and gas reserves and the energy transition demands, however, it will be a challenging pursuit requiring an all-hands-on-deck government approach. But the Brazilian authorities are hopeful, citing past potential with technical capacity, technology and human resources to meet the challenge.

These ambitious plans coupled with the stabilization in the macroeconomic environment could place Brazil back on the trajectory of dynamic growth.

Brazil’s trade surplus hit a record in March 2023, owing partly to a weakening of the currency and the reopening of China pushing exports in the right direction. Foreign direct investment has been notably strong, nearly doubling last year to US$90.6 billion, the highest reading in a decade. Energy, tech, and information sectors received most robust inflows. Geopolitically, Brazil may also indirectly benefit from the geopolitical tensions between the U.S. and China.

Events of Note
May-June 2023

16/05/23
General Assembly in Vienna

Council *of* Slovak Exporters will attend the 32nd General Assembly of Members – Extraordinary Session, together with the 33rd Meeting of Board of Directors – Extraordinary Session, of the Austro-Arab Chamber of Commerce, 16th of May 2023 in Vienna - Read more

21/05/23
Meeting with delegates from Kingdom of Saudi Arabia

Council *of* Slovak Exporters attended a high level meeting with key delegates from the Ministry of Industry and Minerals from the Kingdom of Saudi Arabia, at the Embassy in Vienna - Read more

22/05/23
MOU with its Ukrainian Counterparts in Kiev

Council *of* Slovak Exporters signed a landmark MOU with its Ukrainian Counterparts in Kiev, the Ukrainian Chamber of Commerce and Industry (UCCI) -Read more

23/05/23

TA3 conference

Council *of* Slovak Exporters were an active participant at the TA3 'Zodpovedne podnikanie" -Read more

29/05/23

Globsec

Council *of* Slovak Exporters looks forward to participating at the 18th edition of the Globsec conference in Bratislava - Read more

For **more information** on these or any other events please email us at **info@exporteri.sk**

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