

Summary

- The Conservative Party's deal with the Northern Irish Democratic Unionist Party (DUP), to secure a parliamentary majority in Westminster, strengthens short-term government stability.
- Catalonia's unilateral declaration of an independence vote will escalate political conflict with Spain's central government.
- Following a general election on 24 September, Germany is highly likely to remain a stable and attractive market for investors. German chancellor Angela Merkel is aiming for a fourth term in office with a coalition led by her centre-right Christian Democratic Union (CDU).
- Azerbaijan's banking crisis increases the likelihood of interstate conflict in the Armenian-controlled Nagorno-Karabakh conflict zone; the conflict is likely to be limited in order to preserve the Azeri regime's stability.

Detailed Analysis

United Kingdom



(Picture by: Matt Crossick/Empics/PA Images)

The Conservative Party's deal with the Northern Irish Democratic Unionist Party (DUP) to secure a parliamentary majority in Westminster strengthens short-term government stability.

However, policy uncertainty will remain high regarding Brexit and the Conservative Party is unlikely to

overcome internal divisions over the options of a "hard" or a "softer" Brexit. The new administration is likely to be weak and unstable, which increases the risk of another general election in the coming six to twelve months. In addition, Prime Minister Theresa May is facing pressure from within her party to step down, making a change in leadership more likely. The Conservative Party-DUP deal also heightens the risk of destabilising the 1998 Good Friday Agreement, which stipulates that the Irish and UK governments should remain impartial in the Northern Ireland peace process. This is likely to be somewhat mitigated by the UK government's commitment to not interfere with this arrangement and the pledge to invest GBP1 billion in infrastructure and public services in Northern Ireland. However, instability in Northern Ireland is also driven by ongoing difficulties to restore the power-sharing accord between unionists and republicans to form a new regional government.



IHS™ COUNTRY RISK

Copyright notice and legal disclaimer

© 2017 IHS. No portion of this report may be reproduced, reused, or otherwise distributed in any form without prior written consent, with the exception of any internal client distribution as may be permitted in the license agreement between client and IHS. Content reproduced or redistributed with IHS permission must display IHS legal notices and attributions of authorship. The information contained herein is from sources considered reliable but its accuracy and completeness are not warranted, nor are the opinions and analyses which are based upon it, and to the extent permitted by law, IHS shall not be liable for any errors or omissions or any loss, damage or expense incurred by reliance on information or any statement contained herein. For more information, please contact IHS at customer-care@ihs.com, +1 800 IHS CARE (from North American locations), or +44 (0) 1344 328 300 (from outside North America).

Spain

Catalonia's unilateral declaration of an independence vote will escalate political conflict with Spain's central government.

The regional government in the autonomous community of Catalonia has revived efforts to seek independence from the rest of Spain and set 1 October for a popular vote on the issue. However, such a referendum would be illegal under Spain's constitution: any change to the country's national configuration would require a two-thirds majority in Spain's national Congress, followed by nationwide popular approval in a referendum, both of which are unlikely to materialise. Political pressure within Catalonia to hold the referendum despite its unconstitutional nature will escalate political risks in the region as well as tensions with the central government in the coming months. If the vote goes ahead, the central government could block it by invoking Article 155 of the Constitution. This would involve suspending the Catalan regional government's powers, including assuming temporary control of Catalonia's police force, and even triggering a new election in the region. This would considerably increase government instability risks at regional level and hamper effective policy-making. An increasing level of instability and uncertainty over Catalonia's future would also hamper the business environment, most likely forcing businesses to move from Barcelona to the rest of Spain, particularly Madrid.

Germany

Following a general election on 24 September, Germany is highly likely to remain a stable and attractive market for investors. German chancellor Angela Merkel is aiming for a fourth term in office with a coalition led by her centre-right Christian Democratic Union (CDU).

Her main challenger is former president of the European Parliament Martin Schulz, who is running for Merkel's current junior coalition partner, the centre-left Social Democratic Party of Germany

(Sozialdemokratische Partei Deutschlands: SPD). Although the differences between the leaders of Germany's two largest parties are marginal when it comes to support for European integration, views on Brexit, and other foreign policy issues, an SPD-led government would be likely to introduce domestic policy changes that would lead to an increase in public spending, and some labour market and social reforms, as well as to an overhaul of the German tax system that could result in slightly increased expenditure for domestic and international businesses. The right-wing, anti-immigration Alternative for Germany (Alternative für Deutschland: AfD) will not be part of the new administration – the AfD's electoral support currently totals around 8% nationwide and none of the other parties are willing to collaborate with it.

Azerbaijan

Azerbaijan's banking crisis increases the likelihood of interstate conflict in the Armenian-controlled Nagorno-Karabakh conflict zone; the conflict is likely to be limited in order to preserve the Azeri regime's stability.

The ongoing USD3.3-billion debt restructuring of Azerbaijan's largest bank, the International Bank of Azerbaijan (IBA), indicates unwillingness on the part of the Azeri authorities to tap into their hard-currency reserves, which as of April stood at USD38.5 billion. This could suggest that the government is anticipating costly contingencies, probably related to the resumption of military activities with Armenia over the disputed region of Nagorno-Karabakh, similar to the "four-day war" that took place in April 2016. With Azerbaijan's successful hosting of the Formula 1 weekend in Baku (23-25 Jun) out of the way, the likelihood of such brinkmanship will increase. The Azeri government's probable military objective would be limited to regaining some territory without being dragged into an all-out armed conflict that would be detrimental to the stability of President Ilham Aliyev's regime.