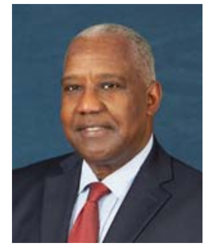
Major Country Developments
November 2017



By Byron Shoulton

Global Overview

U.S. GDP growth appears stronger than earlier forecasts. The economy grew by 3% during the 3rd quarter, continuing the trend of 3.1% growth recorded in the 2nd quarter. This is the quickest pace recorded since the beginning of 2015 and is the first time GDP has expanded above 3% in back-to-back quarters since 2014. The data indicates strong contributions from personal consumption, inventory investment and federal government spending. The U.S. personal savings rate is at 3.4% [compared to 3.8% in the second quarter]. U.S. worker productivity climbed by the most in three years and unit labor costs picked up. The 3% annualized rebound in productivity is a turnaround from the stagnation seen a year ago and suggests that real wages should begin to pick-up in the months ahead.

While there is broad support among **U.S.** business groups for cutting corporate taxes, there are concerns about new provisions that could hit certain allowances and credits. Multinationals in particular could be hit by a crackdown on tax avoidance when corporate profits are shifted out of the U.S. The recently unveiled proposals in the U.S. Tax Cut & Jobs Bill includes anti-avoidance provisions that would impose excise taxes on payments between affiliated companies with a common parent. Some estimates suggest that under current rules companies can shift up to 30% or 40% of their profits out of the U.S. The new provisions are meant to end perceived advantages which the current tax code gives to foreign companies and multinationals over U.S. based corporations. Lobbyists speaking on behalf of multinationals object to portions of the proposed changes arguing that related-party payment transactions are a legitimate and necessary part of internal supply chains that support global trade flows and the exchange of intellectual property across borders. One potential side effect of the proposed tax change would be the imposition of taxes on manufacturers importing components from their own factories located overseas. Another would be the negative impact of taxes on retailers bringing in clothing from affiliates located in foreign locations. Industries including homebuilding, high technology, electric cars and their suppliers say that are at risk of being worse-off if the tax changes are enacted into law as initially proposed.

In the **UK** there are concerns over potential tax losses to the treasury if foreign banks accelerate plans to shift staff and operations out of the UK to a EU country in preparation for Brexit. Overall, the banking system including British lenders, contributed approximately $40 billion to UK finances in the last fiscal year. The figures, which include corporation tax, value added tax and national insurance contributions paid by banks - will add to fears about the economic impact of Britain leaving the EU if its position as Europe's biggest financial center is weakened.

Meanwhile, it was revealed that several investment banks are talking with regulators about routing their Asia-Pacific trading activities through Hong Kong instead of London, while several international banks have confirmed plans to bolster their presence on the continent in response to Brexit. The movement of staff and operations out of London implies falling tax revenues, with employees moving and operations also moved overseas. This would result in a genuine diversion of profits away from the UK. The potential impact on the British treasury when that happens may be underestimated at this point.

The moves come as concerns mount about Britain's ability to secure a beneficial deal with the EU once it leaves the trading bloc in 2019, forcing businesses to consider the prospect of a 'no deal' Brexit where the UK loses the benefit of free-trade agreements. It is difficult at this point to judge how Brexit will affect the UK's future tax intake. That will depend on whether there is a deal with the EU, and the quality of that deal. There are countless challenges ahead for British companies, banks, importers, exporters, et al. Expect more red tape as rules change; and while the UK negotiates new agreements with individual countries and maps out a process for its global trade relationships going forward. This will take time and require vast amounts of talent [both technical and diplomatic].

Canada

The Canadian economy appeared to be cooling a bit following two quarters of 4.5% GDP growth. Expectations of slower growth was supported by a fall in industrial production which fell 0.3% in September. The figures reinforce the Bank of Canada's case for caution on any further interest rate increase after the benchmark rate was lifted in July and September. The central bank held rates steady at 1% at the end of October, noting that economic growth is expected to moderate. The expectation is that the central bank will raise rates, but only slowly over 2018-19, as it remains mindful of high levels of consumer debt.

At the same time, the Canadian labor market regained some of its vigor, with the economy adding a better-than-expected 35,000 jobs in October. This was the most encouraging jobs report for several months. There was a pronounced shift toward the creation of full-time positions and away from part-time work. All Canadian provinces except Saskatchewan shared in the pick-up in new job creation. The figure easily topped the 13,500 jobs the market was expecting and is a leg up from the paltry 10,000 jobs added in September. The unemployment rate is at 6.3% (up from 6.2% in September). The employment figures should provide some minor reassurance to policymakers on the economy's performance in the coming months. . While growth eased from the impressive 4.5% pace seen earlier this year, the pick-up in hiring should ease concern of a dramatic slowdown. Meanwhile, wage growth continued its recent acceleration, rising 2.4% in October; and the participation rate also increased, indicating that more Canadians have joined the workforce. The October data suggest that the labor market will continue to provide some fundamental support for growth, with more Canadians working and receiving higher wages. The Canadian dollar firmed a bit to C$1.27 against the U.S. dollar.

Canada's federal government and several provinces implemented a series of corporate tax reductions over the past few years, making Canada's tax system more competitive with the U.S. Further progress was stalled because of budget deficits (caused by low oil prices), slowing economic growth and political resistance against further tax cuts for big business. Companies incorporated in Canada are considered resident in Canada and taxed on global income.

The ongoing renegotiation of the North American Free Trade Agreement [NAFTA] between Canada, the U.S. and Mexico contains potential risks to the Canadian economy - if a new deal isn't struck between the three trading partners. All three countries have concerns about the current agreement that they want addressed. The U.S. Administration has threatened to withdraw from NAFTA, citing loss of U.S. jobs among other disadvantages to the U.S. that it perceives the trade agreement carries. Without NAFTA, companies in all three countries will likely experience serious disruptions to the trading and investment platforms that were put in place over the course of the past 20 years, when NAFTA was first negotiated.

Canada is a leading producer and exporter of crude oil, minerals & metals, autos, lumber and artificial intelligence. The government supports a competitive environment, enforced by the federal Competition Act. The law is designed to encourage fair competition within Canada, ensure that small and medium-sized enterprises have equitable market access, and provide consumers and businesses with competitive prices and product choices. There are no broad controls on prices for goods and services in Canada, though some restrictions are set in monopolistic industries. The country remains open to foreign direct investment.

Spain

The government of **Spain's** largest autonomous region, **Catalonia,** unilaterally declared its independence, following a referendum. This forced the Spanish national government to dissolve Catalonia's government and Catalonia's former cabinet ministers now face charges of treason and rebellion. The political crisis this sparked comes just as the Spanish economy showed signs of rebounding from years of recession and high unemployment. Spain has 17 autonomous communities. Catalonia's economic contribution is the highest to Spain's GDP of all the regions.

Some independence supporters have threatened a campaign of civil disobedience, leading to fears that the Spanish authorities may struggle to directly govern the region. Polls previously indicated a majority of Catalans do not want to separate from Spain. With the arrest warrants and jailing of former Catalan government ministers some polls are showing a shift in public opinion in favor of independence. This could potentially be an ominous sign for Madrid ahead of December's make-or-break regional ballot. The Spanish government is hoping that anti-independence parties win a solid majority on December 21, and wrest control of the regional government away from the separatists.

For now, in legal terms, the separatist defeat appears complete. Both the Catalan government and key pro-secession movements have lost their leaders. In political terms, however, the crackdown could give the independence movement new momentum and new focus. With a regional election looming in December, the secessionist camp has been handed a powerful campaign theme- as well as a strong incentive to reestablish the frayed unity within its ranks.

Catalonia's economic importance to Spain is huge. The region accounts for 16% of the Spanish population (7.5 million people), equivalent to more than $280 billion in nominal GDP (or 19% of the Spanish economy). In 2016 Catalonia attracted about 21% of foreign investment flows into Spain while it generated nearly 23% of Spain's foreign tourists spending. Additionally, Catalonia is responsible for 25% of all Spanish exports.

Given the economic stakes, the constitutional crisis has agitated financial markets, leading to stock market volatility and a rise in sovereign bond yields. Several major firms, including Spain's third and fifth largest banks, have moved their headquarters out of the region to minimize uncertainty. Other large companies with deeper ties to the real economy have followed suit, and local press reports suggest that departures will continue.

Catalonia's departure would be a fiscal problem for Spain. The region generates about 21% of Spanish tax revenue, and net transfers between Catalonia and Spain result in a surplus for the latter of around $16 billion each year. Catalonia's separation would cause Spain's budget deficit to deteriorate. Along with the region's economic activity, recession in the rest of Spain and heightened uncertainty over the integrity of the Spanish state, would likely lead to a significant rise in borrowing costs.

The consensus forecast is that the national government will be able to keep Catalonia within the country. Early regional elections will be called shortly. Political volatility could lead to precautionary household saving and to cancellations or postponement of business investments in the region. Employment growth will likely stall, and retail, trade and industrial production will likely suffer from the disruption. These effects will likely be mirrored to a lesser extent in the rest of Spain, causing GDP growth in the broader economy to decelerate.

Private estimates are assuming two quarters of contraction in the Catalan economy (currently growing at 3% year-on-year) and a moderate recovery thereafter; the region could expand by 2.5% in 2017 and by a much softer 0.2% in 2018, when the effects of the crisis would be felt most acutely. The expectation is that this would bring headline Spanish growth (currently forecast at 3.2% this year and 2.8% in 2018- to about 2.7% in 2017 and about 2% in 2018, accounting for recent upward revisions to real GDP growth in 2015 and 2016. A messier and more protracted crisis, particularly one that results in longer periods of social unrest, has the potential to lower this forecast.

Energy

Remarks from **OPEC** and **Russian** officials support an extension to existing supply cuts among global oil producers. This caused oil prices to rally above $60 per barrel, reaching its highest level since mid-2015, reflecting optimism that the energy industry has finally turned a corner after a three-year downturn. The international benchmark for crude rose 7% in October, marking a second consecutive monthly gain for the commodity, as crude demand outpaces supply, thereby reducing global inventories. The OPEC-led effort to curb supplies by 1.8 million barrels a day has helped to tighten the market amidst robust demand and a shift in focus by U.S. shale oil producers towards profitability rather than volume.

The oil rally has also supported the share prices of energy companies, whose balance sheets were battered by the price plunge since 2014, when oil was trading above $100 per barrel. The Euro Stoxx Index has rallied 14% since late August and the bullish price performance has intensified recently. Traders expect that major oil producers will continue to actively manage oil output throughout 2018, allaying fears that a rebound in output from certain countries could flood the market just as excess supplies shrink.

Russia and **Iran** have signed agreements to collaborate on strategic energy deals worth up to $30 billion that will involve Russian energy groups Rosneft and Gazprom. Six provisional deals were signed with Russian companies as part of a visit by the Russian President to Iran at the end of October. After years of sanctions the Iranian government has sought to attract foreign companies to develop Iran's energy sector. The latest announcement coincides with a Russian build-up of energy assets in the Middle East, as part of a wider diplomatic and commercial push to increase its economic and military clout in the region.

Both countries will cooperate in developing Iran's oil and gas fields while collaborating on research. When completed, Rosneft has indicated it estimates that Iran's production plateau will reach 55 million metric tons of oil per year.

Russia and Iran have long been working on oil-for-goods deals worth up to $20 billion, since cash-strapped Iran has been under western sanctions over its nuclear program. Under those agreements Moscow would buy Iranian oil in exchange for Russian equipment and technology. Iran says it needs $200 billion of investments for upstream and downstream projects by 2021. Since signing a nuclear deal with major powers in 2015, enabling many sanctions to be lifted, Iran has signed only one notable contract – with France's total in July 2017 worth $4.8 billion.
Iran is keen about engaging more western companies to prove that U.S. hostility toward it has not scared off foreign investment. However, oil experts contend that should the U.S. re-impose sanctions on Iran, Russian and **Chinese** firms would stand to benefit from the lack of competition from western energy companies.

Russia has forged a close relationship with **Saudi Arabia**, Iran's arch rival in the region and has leveraged a deal with OPEC to curb crude supply, as one way of strengthening ties with the kingdom in both the energy and military sectors. Rosneft has also become a major financial supporter of Kurdistan, by acquiring a majority stake in the main oil pipeline in the northern Iraqi autonomous region.

Kenya

A crisis-like atmosphere prevails in Kenya as new elections held in October [demanded by the Supreme Court] were boycotted by millions; with voting results showing [for a second time in 3 months] that President Uhuru Kenyatta was returned to power. Voters continue to have serious reservations about the electoral commission's ability to deliver fair and credible election results. Protests and deaths caused the postponement of voting in some regions. Some polling stations were opened hours late as police battled with protesters seeking to disrupt the election. The low turnout is a testimony to the lack of confidence in the process and a deep distrust of Kenya's political system.

We anticipate a prolonged struggle over the state of democracy in Kenya. This will hurt business investments and foreign investment inflows. Tourism will likely be also affected as prospective visitors postpone plans awaiting a resolution of the political crisis. The economy will weaken and suffer jobs loss, lower tax intake and lose momentum.

The two leading political parties and their respective leaders are acutely aware of what happened in Kenya after the 2007 elections when tribal warfare left thousands of Kenyans massacred in a virtual civil war. That outbreak reversed the international perception of Kenya as a relatively prosperous African country, with a working democracy, a growing middle class, mineral resources that attracted foreign capital, and a country with vast tourism potential. Since then, Kenya has struggled to regain its stature and the confidence of its people; and it has struggled to restore the confidence of foreign investors and visitors. The current political impasse is a further stumbling block along that long road to recovery.

Kenya is entering uncharted political territory, to the detriment of its economy. The election impasse is now becoming the main worry among investors. Combined with unsustainable state spending and a major drought that preceded the election period, the risk of political clashes threatens to derail Kenya's economic growth for the remainder of 2017 and in 2018. In September the forecast for real GDP growth was cut from 5.9% to 5.1%. The prospect of further uncertainty is bad news, because this East Africa's largest economy entered its election season on an already fragile footing.

Early this year northern parts of the country faced one of the most protracted droughts in recent times, leading to nationwide year-on-year inflation of 11.7% in May. This has since subsided to 7.1% in September, mainly due to government subsidies for food staples like corn. The government is also saddled by expensive infrastructure projects, a rising public wage bill and a costly security operation in neighboring Somalia. These costs will contribute to a budget deficit of 7.2% of GDP for fiscal 2017/18. Driven by a slight worsening of the current-account deficit to 6.1% of GDP, due mainly to higher fuel and food imports, debt-service costs amounted to $2.6 billion, or 20% of revenues.

Aside from the huge pressures on the public purse caused by the elections, the threat of extended instability is hitting private-sector activity, which has already been negatively affected by the earlier annulled August election. Most sectors reported losses over the August election week, and further negative signs have appeared since the Supreme Court's ruling to annul it. Construction supplies companies, manufacturers, transport and the financial sector firms have all reported a fall in their respective businesses. Fears of violence and its impact on the economy now dominate. For those reasons it is difficult to envisage a return to business as usual over the next three to four months.

Argentina

Argentina's government unveiled sweeping proposals to cut taxes in a pro-market reform move following the ruling coalition's victory in mid-term legislative elections held in October.

The proposals, which the government hopes will be approved by congress this year, aim to reduce the tax burden by 1.5% of GDP over the next five years. The main aim of President Mauricio Macri's reforms, which are expected to also include the announcement of an amnesty plan for informal workers, is to modernize Argentina's economy and shrink the state so that its chronic fiscal deficit can be eliminated. The tax reforms, inspired by successful similar reforms in Chile and Uruguay, were designed to make Argentina's arcane and onerous tax code simpler, cleaner and fairer, while bringing it into line with global practices.

The government argues that the reforms will stimulate investment and thereby unlock the potential for sustainable growth in the economy. Investment accounted for 15% of GDP in 2016, and the government is projecting that this will improve to 17% in 2018, as confidence gradually returns after a decade of populism.

The rating agency Moody's raised Argentina's long-term sovereign credit rating from B to B+, citing higher investments and progress in improving competiveness - as factors that will help to sustain economic growth. The reforms include reducing taxes on businesses that reinvest profits from about 35% to 25%, and would see employer social security taxes slashed.

Meanwhile, Argentina's largest oil company YPF, announced it will invest more than $30 billion over the next five years to generate its own shale oil boom. This will make YPF– a state controlled company- the top investor in Argentina, while the pro-market government of President Macri step-up its drive to attract investments to consolidate an economic rebound following six years of stagnation.

YFP will develop Argentina's huge unconventional oil resource, the Vaca Muerta shale field located in Patagonia state, which contains the world's second largest reserves of shale gas. The project aims to increase unconventional energy by 150%, to reach half of total production in five years. Overall oil and gas production is anticipated to rise by 5% a year, to reach 700,000 barrels of oil equivalent a day in 2022. YPF aims to also boost electricity production – as a part of its efforts to become a fully integrated energy company.

Once a net exporter of energy, a lack of investment in recent years has led to production plummeting, leaving Argentina with a costly energy deficit and a dependence on imports that have placed heavy pressure on the country's budget.

The sitting government's strong performance in the recent legislative elections reflects improving economic conditions as well as opposition among the electorate toward the Peronist Party led by former President Cristina Kirchner. In recent weeks, corruption investigations implicating Mrs. Kirchner and several of her former cabinet ministers, help to explain the loss of support for the Peronist opposition. Although Kirchner will nonetheless have a seat in the Senate, her influence will be significantly diminished.

The central bank, BCRA, is expected to maintain higher interest rates over the coming quarters. Although inflation has remained in line with expectations in recent months, BCRA has held its benchmark rate at 26.25% since April and adopted a more hawkish tone, as it seeks to bring inflation closer to its target of 10% by the end of 2018.

Inflation is projected to end 2017 averaging 18.7% for the year. Utility costs are likely to continue to rise over coming quarters. Cutting government subsidies on electricity and natural gas usage is a key priority for the government as it seeks to narrow the fiscal deficit. However, the political sensitivity to reducing the subsidies prevented the government from acting on it ahead of the October mid-term legislative elections. Now that the elections are over, the government is likely to resume its gradual reduction of utility subsidies in the coming months. Higher global oil prices will also add to a broad rise in energy and transport costs.

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Non-Cancelable Limits Policy*: $45mm buyer limit participation in a syndicated key account multibuyer policy on domestic buyers

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* ***Non-Cancelable Limits:*** *Subject to policy terms and conditions, after issuing the policy, the insurer may not unilaterally reduce any country or buyer limits.*