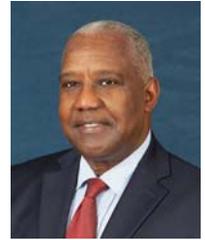


Major Country Developments January 2018



By Byron Shoulton

Global Overview

The global economy appears set to continue to grow at a robust pace in 2018. Global GDP growth forecasts of 3.7% in 2018 are driven by generally upbeat expectations among businesses and relatively strong consumer confidence in the **U.S.** and elsewhere. Furthermore, the ongoing recovery in **Europe** and the strengthening of commodity prices should positively impact trade growth and stimulate emerging market economies in the year ahead. The expected surge in economic activity, following the uptrend from 2017, is supported in part by the likelihood that the recently enacted U.S. tax overhaul will further boost sentiment, spurring new investments, employment and consumption. In addition, talk of a comprehensive infrastructure building initiative promoted by the U.S. Administration, could begin to take effect sometime in 2018 and is raising hopes that it could act as a medium-term economic stimulant once it is launched. Meanwhile, higher crude and commodity prices will result in upward inflationary pressures as higher raw material costs are passed on to manufacturers and consumers.

While commercial credit risks remain relatively stable, geopolitical risk factors remain elevated, underlining certain vulnerabilities that could negatively impact an otherwise benign 2018 outlook. A rise in demand for goods, services and an elevated need for technological upgrades across several industries are among the chief drivers influencing global investment growth, trade flows, higher employment and global consumption. Sweeping advances in manufacturing, transport and broadband capacity are creating waves of changes across the globe. These forces are driving the demand for raw materials, workers, and services and will help to undergird stronger commodity prices.

The U.S. jobs market ended 2017 on a strong footing with private sector employers adding 250,000 positions in December. The service sector drove the bulk of those gains. The unemployment rate at 4.1% over the final three months of 2017, is at its lowest since the 2008-09 recession. The tight labor market is forecast to get even tighter in 2018, which has prompted the Federal Reserve to increase interest rates in December for the fifth time since the recession. Three additional rate increases are projected during 2018. The Federal funds rate [charged on loans made by the central bank to commercial banks] is still only 1.5%, a rate that is so low that it has historically been regarded as an emergency level. This suggests that the Fed may have kept its easy money policy too low for too long. It will now seek to catch up with tightening over the course of the New Year. That said, U.S. inflation remains subdued at 1.9%.

While commercial credit risks remain relatively stable, geopolitical risk factors remain elevated, underlining certain vulnerabilities that could negatively impact an otherwise benign 2018 outlook.

Tensions over trade remain elevated as the U.S. Administration butt heads with **China** and other countries over what the U.S. regards as unfair trade practices and the lack of mutual access to those markets by U.S./western companies. Threats of higher tariffs on imports into the U.S. could begin to take effect in 2018 if there are no clear signs that U.S. complaints are being addressed by the Chinese authorities and other trading partners. The U.S. has tightened its scrutiny of inbound investments from China adding to the tensions between both countries.

Several attempts by Chinese firms to buy U.S. companies in 2017 were not approved by the Committee on Foreign Investment (or CFIUS). This reflects the fact that the geopolitical environment has changed considerably over the past year as momentum builds for closer scrutiny of Chinese investments and trade behavior that warrants a pushback from the U.S. and others who are not pleased by what they consider a one-sided arrangement.

The U.S. also accuses China [and various Chinese companies] of helping North Korea violate sanctions imposed in response to rapid advances in that country's nuclear program. While the standoff and war of words between the U.S. and North Korea appears far from a diplomatic breakthrough, North Korea recently indicated a willingness to renew contacts with South Korea and may seek participation in the 2018 Winter Olympics to be held in Seoul. The move has been welcomed by the South Korean government and could help tamp down the elevated state of tension on the Korean peninsula.

The **Eurozone** economy performed well in 2017. The euro currency strengthened and is back to above US\$1.20. European stocks rose and bond markets were well-behaved. The European central bank has become more upbeat about growth prospects. Instead of GDP growth forecast at 1.7% for 2017, actual GDP growth hit 2.4%. That makes 2017 the strongest year for Eurozone growth since 2007. While stronger cyclical recovery is good news, the Eurozone's crisis scars persist. Germany's economy is now 11% larger than it was in 2007 while Italy's is around 5% smaller. Unemployment across the Eurozone has fallen, but ranges from 3.5% in Malta to 20.6% in Greece, according to Eurostat. The continued economic disparities between Eurozone countries remain a chronic problem.

The European central bank has become more upbeat about growth prospects. Instead of GDP growth forecast at 1.7% for 2017, actual GDP growth hit 2.4%.

Nonetheless, a positive shift in perceptions of the Eurozone economy has already occurred. And while political risks in Europe weren't as large a problem that many feared in 2017, concerns persist. Spain still faces a thorny challenge in managing relations between Madrid and Catalonia which wants independence; and Germany has yet to form a government after elections in September. Efforts by German Chancellor Angela Merkel to form a new coalition government possibly with nationalist parties will inevitably mean compromising on migration policy. Across Europe the issue of the influx of migrants has led to the growing popularity of ultra nationalist parties in several countries. Italy's elections in early March will be a key focus in gauging growing populist and nationalist sentiments across the region. For the time being, the cyclical economic uplift being enjoyed in most of Europe counts for a lot and investors are being rewarded for their optimism. Business and consumer confidence has improved across the region (the UK being a noticeable exception). The challenge for 2018 is to maintain the momentum and avoid political setbacks that might damage the goodwill built up in 2017.

Turkey's central bank took more measures to prop up the currency, the lira, after it fell to new lows against the dollar. The central bank removed the limits on borrowing in the interbank money market and boosted liquidity. The lira slid sharply over the past three months, pushing inflation to a nine year high of 11.9%. However, the central bank is limited in its ability to raise interest rates in the face of pressure from President Recep Erdogan to keep rates low.

South Africa

The country's ruling political party the ANC elected a new leader in December. This has positive longer-term implications for South African politics, society and its business climate, although improvements will be gradual and subject to setbacks. Cyril Ramaphosa the new ANC head, was previously the country's Deputy President. He is considered a

moderate pragmatist with practical experience in the trade union movement as well as being successful in business. He will be well placed to be the next president of South Africa after the 2019 elections – replacing Jacob Zuma – provided the ANC retains a majority of the vote. However, Mr. Ramaphosa's influence may be constrained while Mr. Zuma remains president. The narrowness of Mr. Ramaphosa's victory over the candidate favored by Mr. Zuma [2,440 votes versus 2,261] and the failure of his loyalists to secure all the top leadership positions within the ANC, will also limit the new leader's room for maneuver over the short-term.

The new ANC leader's broad objectives are twofold and interlinked: boosting the ANC's chances of securing another majority in 2019 and revitalizing the economy after years of mismanagement and policy uncertainty. The change in the leadership is a blow to Mr. Zuma and at the very least a boost to confidence for the people of South Africa. The currency, the rand, had its strongest rally in five months following the vote. The ANC's electoral summit reveals a deeply divided party, split into two equally sized camps. Mr. Ramaphosa's first priority will be to rebuild a degree of unity – which will require inevitable compromises – without sacrificing his reformist agenda. He will also need to avoid becoming beholden to a range of interest groups and not make too many promises, which became the key flaw in Mr. Zuma's presidency.

On balance, President Zuma was not the cause of the 2009 recession, or the crippling drought in 2016, which both contributed to South Africa's record of increasingly sluggish growth and steadily rising unemployment. However, he does have responsibility for the confusion surrounding numerous policies (such as expropriation), for anti-business measures (such as a mooted new mining charter), for the erosion of fiscal discipline, and for the rise in corruption and patronage – all under the guise of "radical economic transformation" – which led to a loss of confidence in South Africa, declining private investment and credit downgrades by rating agencies.

The change in the leadership is a blow to Mr. Zuma and at the very least a boost to confidence for the people of South Africa.

Complicating the situation, the ANC conference delegates approved controversial policies including a significant rise in funding for higher education (despite current fiscal constraints) and the nationalization of the South African Reserve Bank (the central bank), which is now privately owned.

Two legal judgements against President Zuma by South Africa's High Court within five days in December, cited the president's conflict of interest in appointing a judicial commission as both Mr. Zuma and members of his family were potentially implicated in the matters to be ruled on by the commission. In a separate and equally dramatic ruling the court annulled Mr. Zuma's appointment of the head of the National Prosecuting Agency, and handed the responsibility to appoint a replacement to the deputy-president. Again, the reason cited by the court was Mr. Zuma's conflict status.

Mr. Ramaphosa's assumption of the ANC leadership offers South Africa the best chance of recovery, but unless he acts with urgency, the challenge will become progressively more difficult. That he won his party's top position despite a variety of antics by President Zuma and his faction suggest that there is still hope for South Africa.

GDP growth dipped to 2% in the third quarter from 2.8% in the second quarter, reflecting a broad-based weakness. GDP growth for all of 2017 is expected to be 1%. The only exceptions to a general weakness were the agricultural and mining sectors. Trade was down by 1% for the first nine months of 2017. The current-account deficit widened to 3.7% of GDP in the third quarter of 2017. However this was a smaller deficit than the 4.2% of GDP recorded a year earlier. Exports for the year grew by 4.8% while imports dipped by 1.2%, reflecting subdued economic growth. Net financial inflows funded the current-ac-

count deficit. Foreign direct investment turned more sharply negative, as higher inflows were offset by higher outflows of capital. A modest uptick of 1.5% GDP growth is forecast for 2018. The negative factors weighing on growth in 2018 will include persistent high unemployment and a significant degree of political and policy uncertainty ahead of the 2019 general election. Business confidence will remain fragile, translating into subdued private investment and weak job creation.

Over 2018-19 expect relaxation of exchange controls on capital flows to pause in response to ratings downgrades. Selected trade tariffs may be raised to protect vulnerable industries (such as steel). Efforts to build closer ties with key emerging markets will continue.

As the most advanced economy in Africa, South Africa will continue to play an important role in regional and world affairs. The country will remain deeply engaged with Africa, particularly Southern Africa. It will continue to support peacekeeping operations in the continent's conflict zones. Zimbabwe will be high on the agenda after the Zimbabwean army forced Robert Mugabe to resign and installed his former deputy as the country's new president.

Middle East

Prospects for rapid economic growth in the Middle East remain stifled by heightened geopolitical risks, macroeconomic imbalances, policy uncertainty and corruption. Arguably, the Middle East has become the crucible for conflicts stoked by the competing geopolitical interests of regional heavyweights and global powers, particularly the U.S. and Russia. At present, seven countries in the region (Iraq, Syria, Libya, Lebanon, Palestine and Bahrain) which collectively account for one-quarter of the region's population, are either torn by civil war or destabilized by toxic Sunni-Shia rivalries. Others are still vulnerable to domestic social unrest – albeit smaller in scale than that seen at the height of the Arab Spring in 2010-11.

Geopolitical risk is also rising rapidly in the Gulf Arab region, which was long seen as a bastion of stability in an otherwise volatile area. The Gulf Cooperation Council (GCC); a political union of six Gulf Arab States, is now the center of a crisis that could further undermine investment and business prospects in the region. Last June Saudi Arabia, the UAE, Bahrain and Egypt severed diplomatic ties with – and closed most transport links to Qatar, owing to the latter's strengthening defense ties with Iran and its long-standing support for Islamist groups. As the situation continues to evolve, the conflict could enter a phase of polarization that is likely to shake up long established political alliances in the Middle East. Although Qatar is sliding deeper into the fold of Turkey and Iran, Saudi Arabia, Egypt and the UAE are redoubling joint efforts to counter Iran's influence elsewhere and rein in the threat of jihadi terrorism.

Arguably, the Middle East has become the crucible for conflicts stoked by the competing geopolitical interests of regional heavyweights and global powers, particularly the U.S. and Russia.

It is not out of the question that the GCC could fracture, albeit gradually, amid these two newly forming alliances in the region. Meanwhile, the Saudi-Shia rivalry will only intensify, although any potential warfare will remain confined within the borders of traditional proxy battlefields such as Lebanon, Yemen and Syria, owing to the mutual recognition that direct confrontation would exact a heavy economic price on both countries. The conflict in Yemen is set to intensify, particularly after the death of Ali Saleh, a former president, who recently sought rapprochement with the Saudi kingdom. His assassination by the Iranian backed Houthi rebels will harden the positions of both sides, leading to a short-term increase in the intensity of the fighting. Few observers believe there are realistic peace prospects in Yemen over the medium term. These political linkages and machinations will provide a challenging environment for

regional investors and foreign creditors.

U.S. foreign policy changes in the region are likely to also stoke renewed unrest among Palestinians. If nothing else the long running Israeli-Palestinian conflict and a two-state solution, has been placed back on the front burner after an apparent lull in activity. President Trump declared in December that the U.S. will go forward with an American recognition of Jerusalem as Israel's capital, but there was little support for the idea from regional players.

More positively, despite the intensification of geopolitical risk, large economies such as Saudi Arabia and the UAE will continue to offer lucrative business opportunities, assuming that direct warfare with Iran is avoided. With this in mind, capital will continue to flow into the sort of long-term infrastructure investment projects that are needed for economic diversification. Moreover, efforts to diversify financing sources for state-led capital projects mean that short-term securities, backed by ample central bank reserves, sovereign wealth fund holdings or similar, will remain attractive to investors, suppliers and creditors. According recent EIU forecasts Saudi Arabia's public debt will rise from an estimated 29% of GDP to above 50% by 2022, driven by domestic and international bond issues to finance mega-infrastructure projects.

However, downside risks continue to pose threats to this outlook. Low oil prices and crude volume cuts agreed between OPEC and other producers have led to capital spending cuts in the GCC, and this suggests that economic diversification could proceed inconsistently owing to occasional domestic liquidity constraints. Notably, the smaller economies in the Gulf region- Bahrain and Oman- will remain beholden to Saudi and Emirati largesse. Liquidity constraints will be most severe in Bahrain, given stretched public finances and poor solvency indicators, which could leave creditors exposed to potential rollover and payment risks.

Markets have been rattled by the ongoing unprece-

ded anti-corruption efforts in Saudi Arabia. With the arrest of princes, leading business people, government ministers and scores of former government officials; and the freezing of thousands of bank accounts. Since November, the Saudi All Shares Index (TASI), and to a lesser extent the stock markets of neighboring Gulf states, have fallen sharply. This suggests that in the short term, regional shares will become less liquid, although the trend is expected to be temporary. While the arrests are motivated in part by a desire to concentrate power in the hands of the crown prince, they also appear to be an attempt to curb official and business corruption in the kingdom ahead of the forthcoming flotation of a 5% stake in the state-owned oil company Saudi Aramco. Nonetheless, the crackdown could prove destabilizing to the kingdom if the crown prince (next in line to become king on the death of his father) fails to deliver on his promises of further social reform or a swift turnaround of the economy's fortunes.-

FCIA's Deals Of the Month

Multibuyer - Key Account Limits Policy:

\$20,000,000 limit of liability supporting sales to the Domestic Auto Sector. Policy obtained for nonpayment risk mitigation.

Letter of Credit Policy: \$15,000,000 limit of liability supporting non-honoring of a letter of credit on sales of Capital Equipment, 5 year tenor, Egypt

What is Trade Credit Insurance?

If you are a company selling products or services on credit terms, or a financial institution financing those sales, you are providing trade credit. When you provide trade credit, non-payment by your buyer or borrower is always a possibility. FCIA's Trade Credit Insurance products protect you against loss resulting from that non-payment.

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