

The global economy—a brave new world

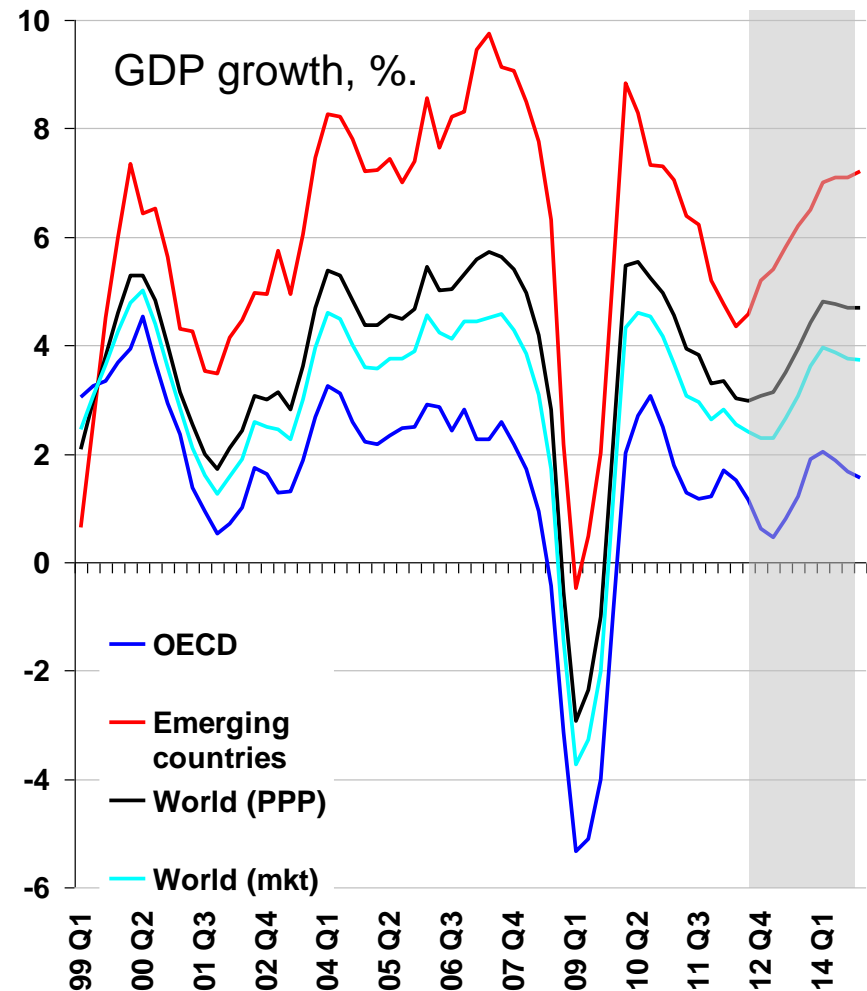
Robert Ward
Director, Country Publishing
robertward@eiu.com

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2013-14: better than 2012, but it may not feel like it

- Europe struggles will continue
 - Euro recovery anaemic—0.7% GDP contraction in 2013
 - Parts of periphery in depression
- US recovery momentum is accelerating
 - The housing market is recovering
 - Watch for cliffs and ceilings!
- Japan tries the mother of all monetary experiments
- China yoyo-ing—about 7.5% growth
 - Strongly outperforming the West
 - But experiencing growing pains as it moves to middle-income status
- Oil remains in comfortable surplus
- Asia remains the fastest growing region, but watch Africa too
- Assets will stay on their sugar high



The developed world

Euro zone: The evolution of a crisis—2009

**Policies that are
politically
feasible**

**Policies that
might
actually
work**

Euro zone: The evolution of a crisis—2013



**Policies that are
politically
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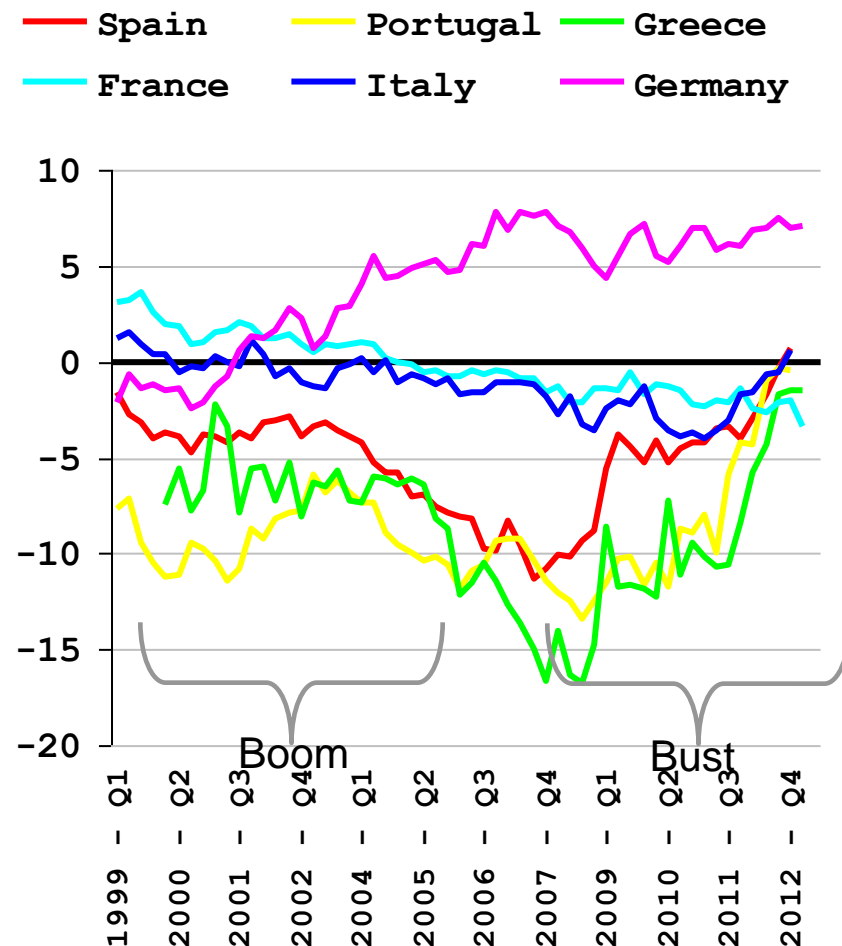
**Policies that
might
actually
work**

Euro zone: Watch the politics



Euro zone: From acute to chronic

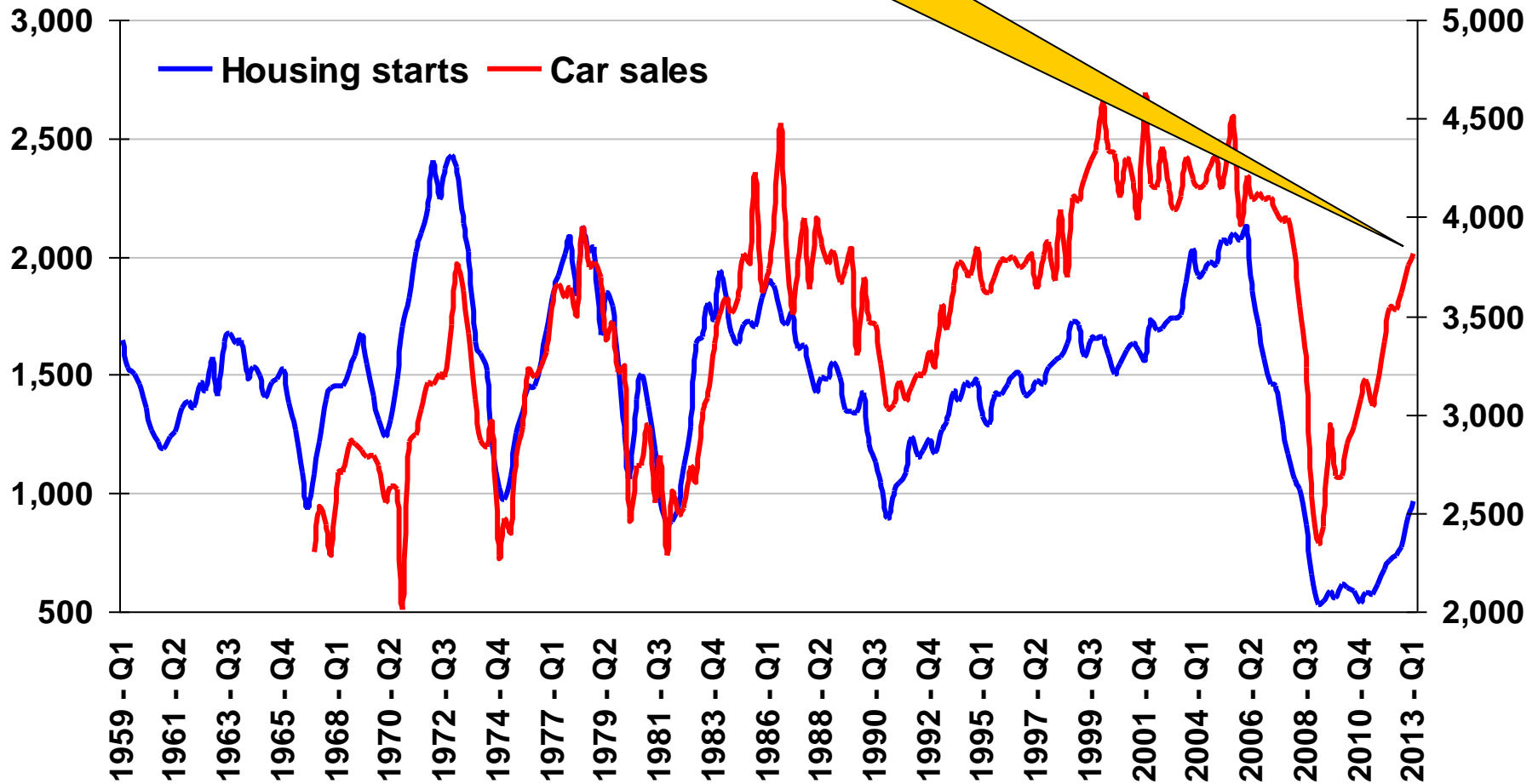
- The OMT programme removes the risk of sovereign default as a result of sovereign debt market illiquidity
- Ireland and Portugal have both returned to the debt markets
- Spain is adjusting quickly—labour costs are down and competitiveness is rising, but the road to recovery remains long
- Political stasis will limit the chances of reform in Italy
- France lacks the imbalances of Spain/UK, but badly needs reform
- The UK will come under increasing pressure to redefine its relations with the EU



Current-account balances/% GDP. Source: Eurostat.

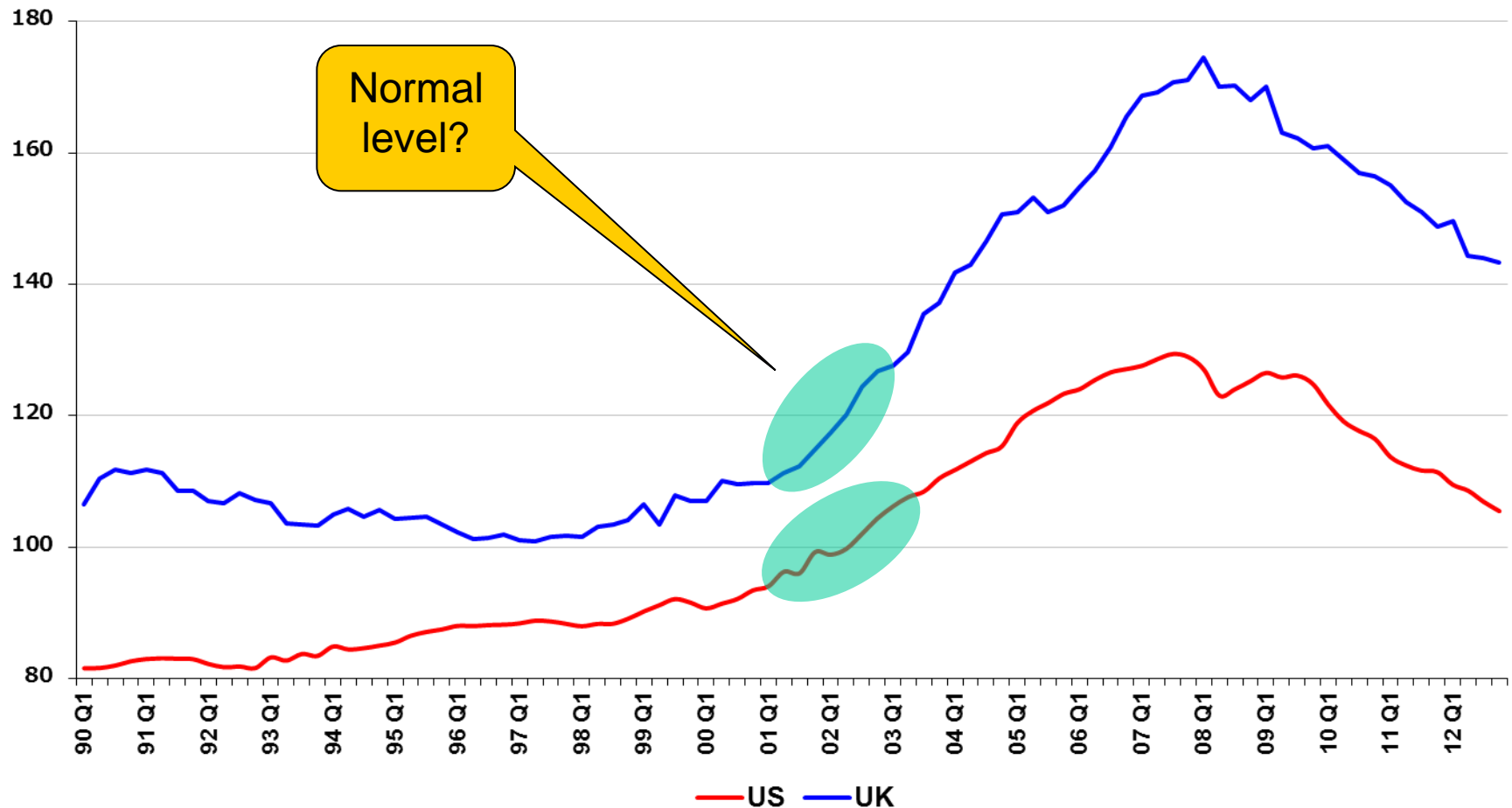
US: Green shoots

Recovery!



US: Housing starts, car sales, '000s. Source: Haver.

UK: Households—“The Great Adjustment”



Household debt as a % of disposable income. Sources: US Fed, ONS.

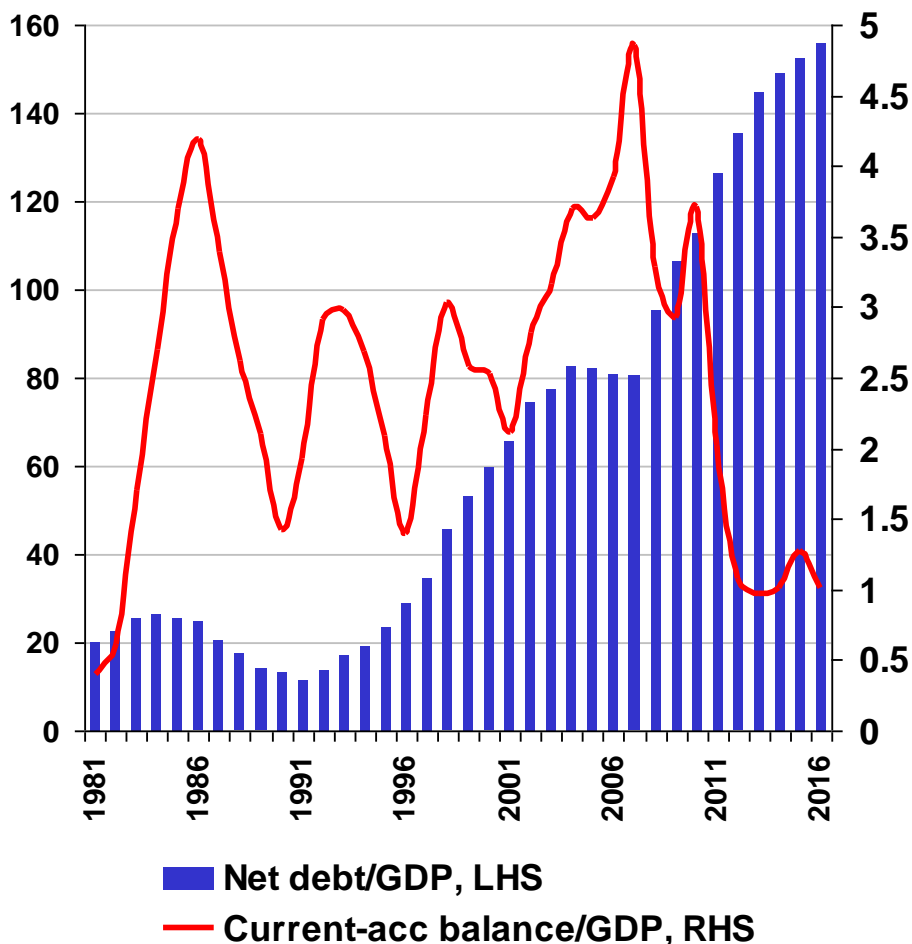
Japan: Abenomics—be careful what you wish for

Positive

- A weaker yen will boost net exports—domestic demand is too weak to do this on its own
- Japan could then import foreign demand
- Stimulus will boost nominal GDP and hence tax revenue, reducing debt ratios
- Japan is in an economic cul-de-sac, so why not try something different?!

But

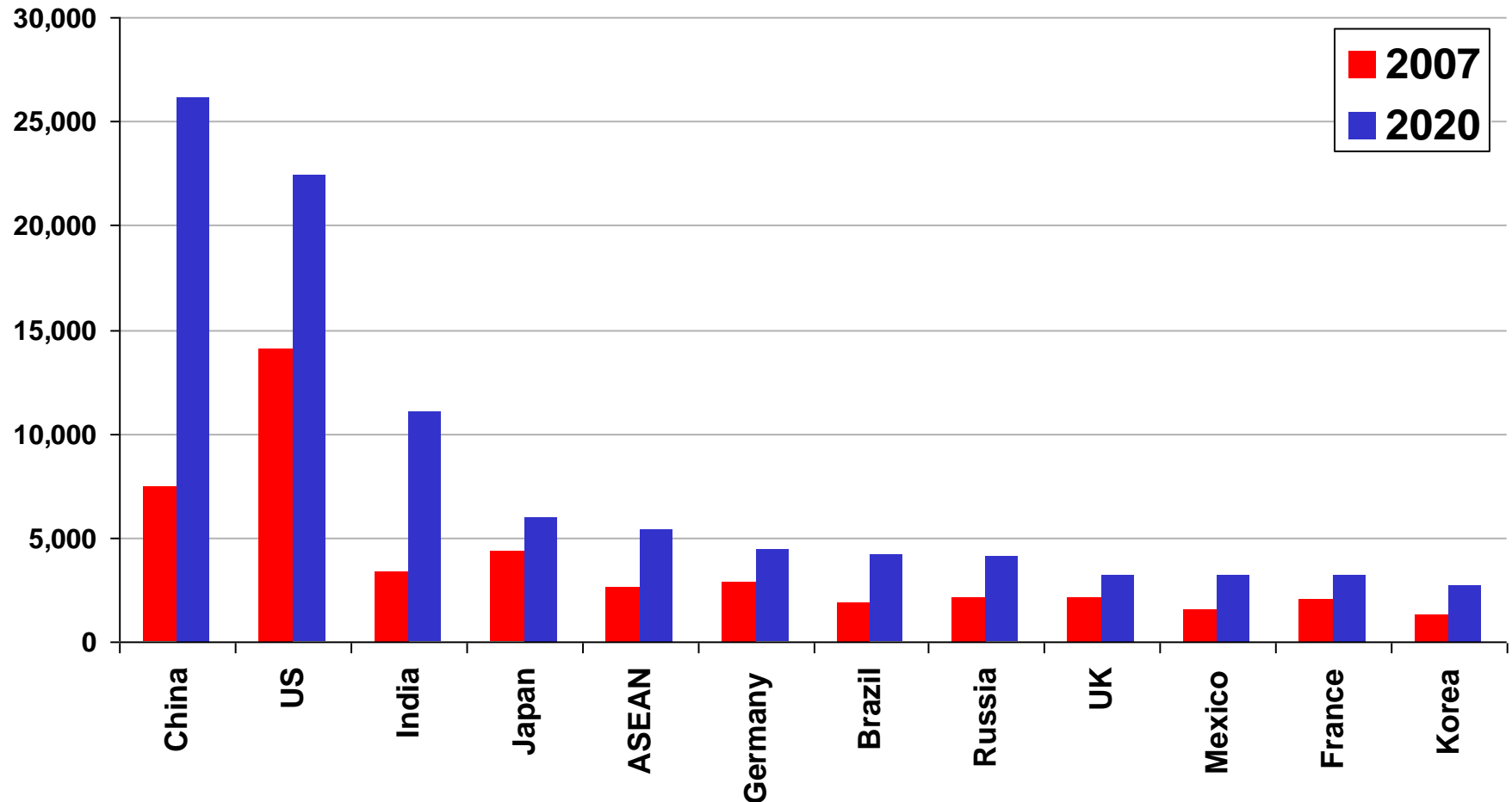
- Extreme macro policy can reduce trend growth through distortions/zombie proliferation
- Ending deflation won't automatically boost growth
- Internal currency wars suggest the yen won't weaken as much as it needs to (>¥120:US\$1?)
- In the short term, deflation needs to continue to keep real rates high, which keeps cash at home
- If inflation takes off, “independent” central bank may be needed to rein in prices



Sources: IMF, EIU.

Emerging markets

Crises accelerate existing trends



GDP, purchasing power parity; US\$ bn. Source: Economist Intelligence Unit.

Risk factors for a broad-based EM crisis

China

- Hard landing
- Social unrest political instability

**15%
chance**

Euro zone break-up (exit of large member state(s))

- Damage to global financial system, real economy

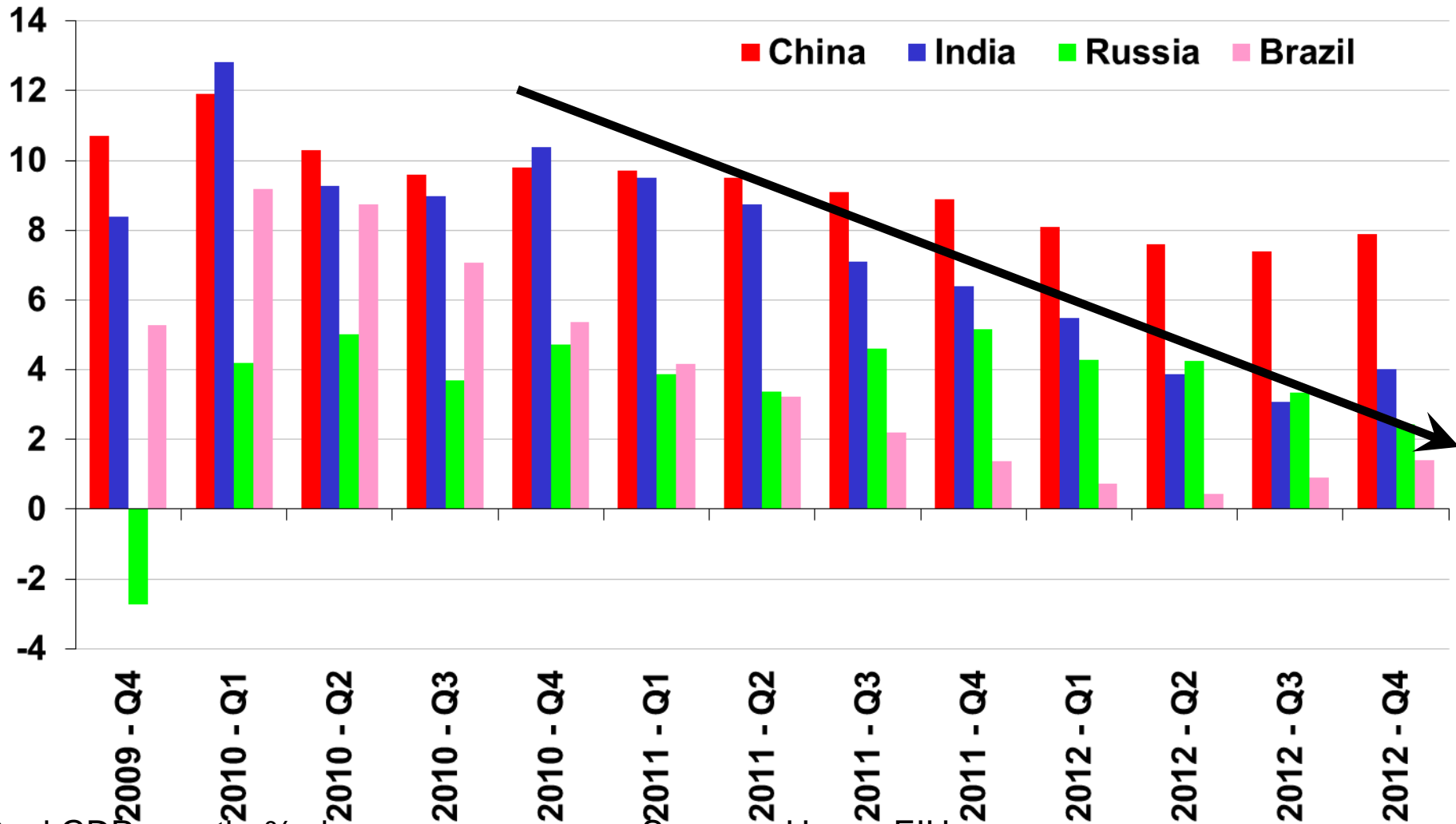
**20%
chance**

Steep rise in interest rates in developed world

- Possibly associated with exit from QE

**15%
chance**

The BRICs: So yesterday!



Real GDP growth, % change, year on year. Sources: Haver, EIU.

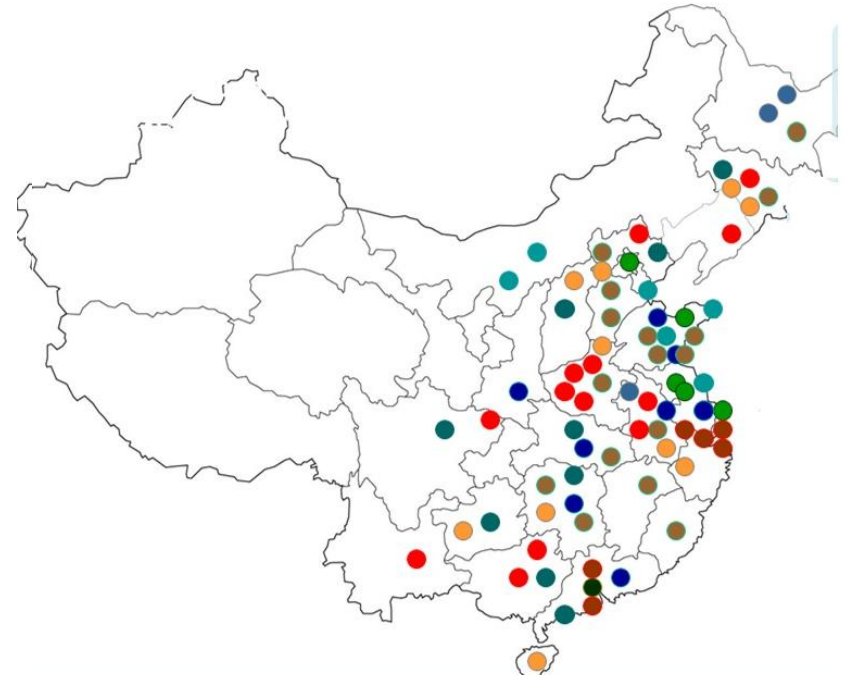
China: Urbanisation will be key

- The bad

- Slower headline growth
- Rising wages
- Worsening demographics

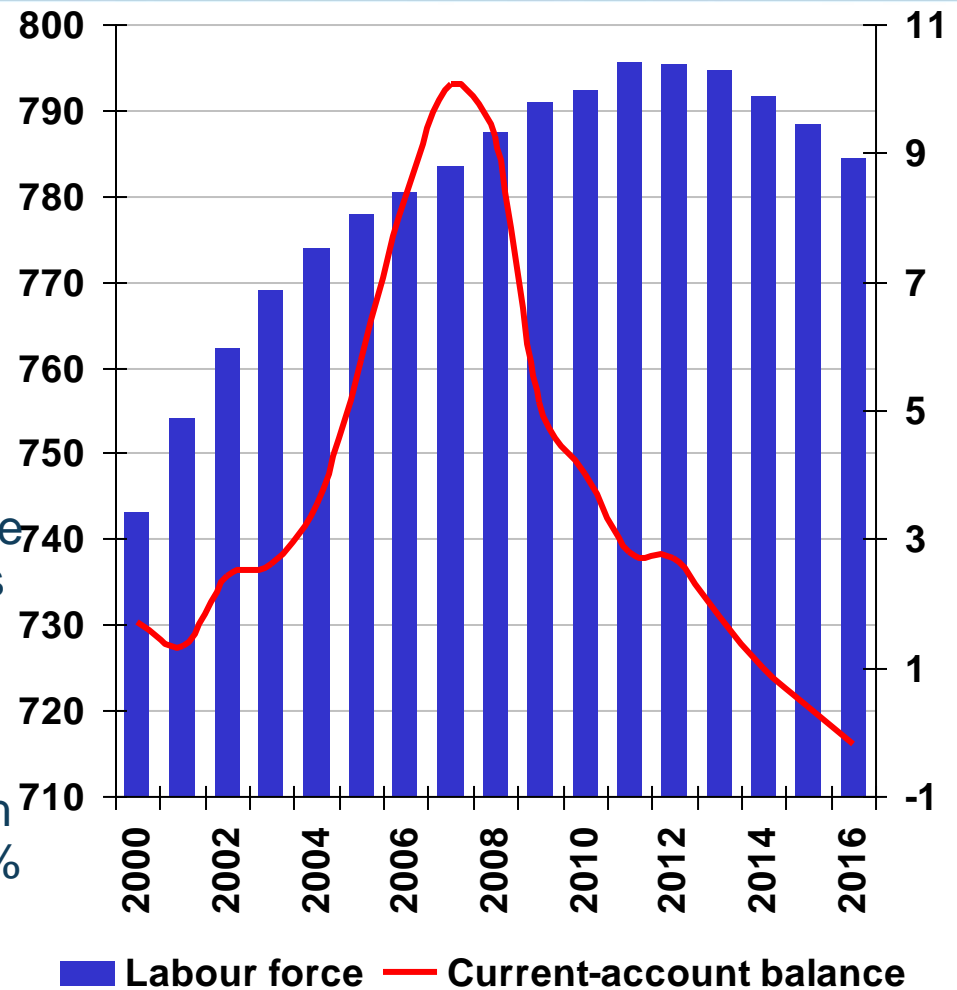
- The good

- Rising incomes
- Tipping point, opening west, demand for new services
- Urbanisation has further to run
- Government openness to foreign participation in new sectors



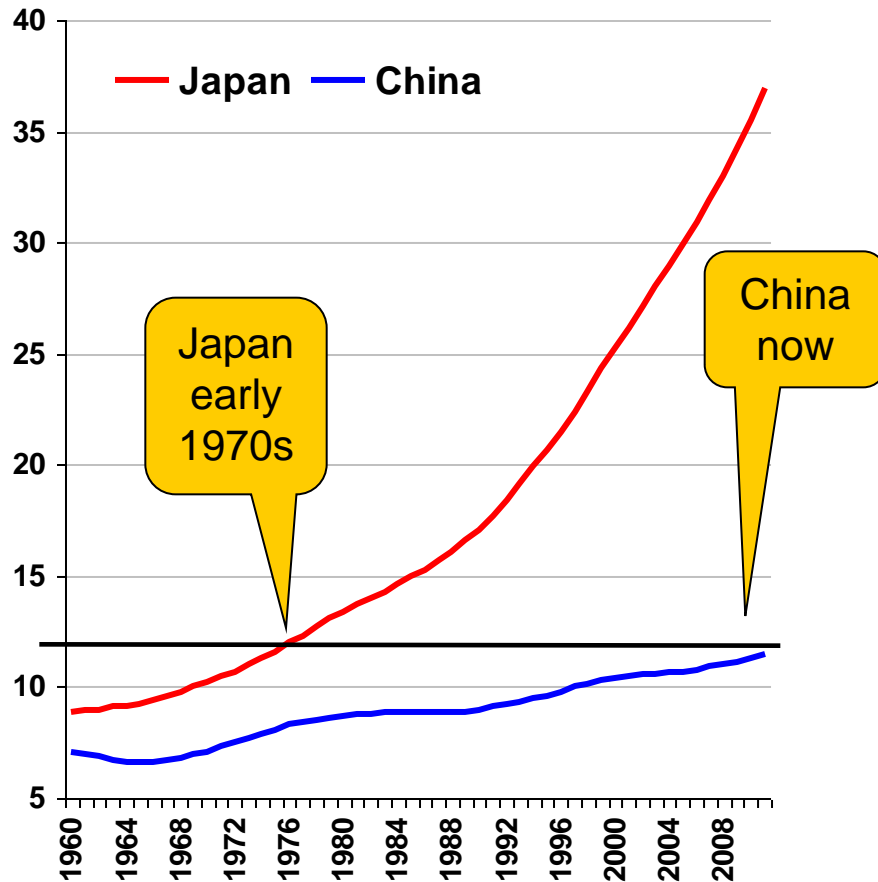
China: At a crossroads

- China is moving to a period of structurally lower growth—less growth “needed” now
- New leadership will take a cautious approach to policy
- Economic rebalancing is under way—private consumption will increasingly drive growth
- Lower level manufacturing will be shed to Asia as the shift towards higher-value added products/rising wages continues
- A relaxation of the *hukou* residence permit system would accelerate urbanisation
- RMB trading band will be widened, with RMB set to appreciate by just under 1% a year against US\$ in the next five years

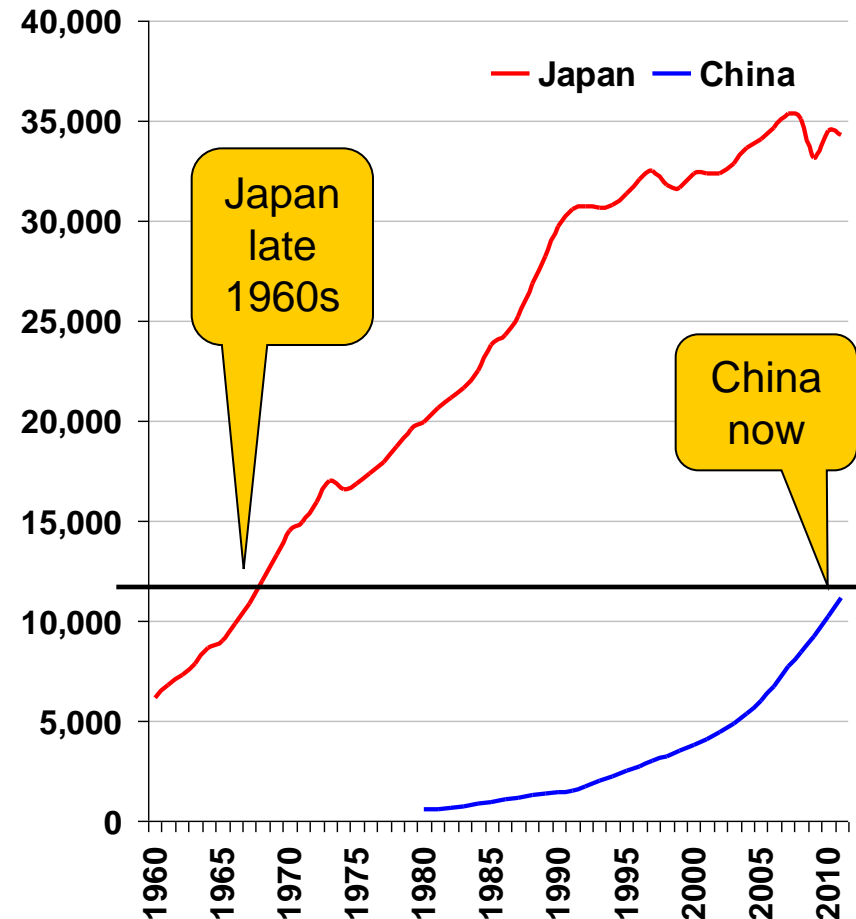


Labour force, m. C/a balance, % of GDP. Source: EIU.

China—ageing and middle income



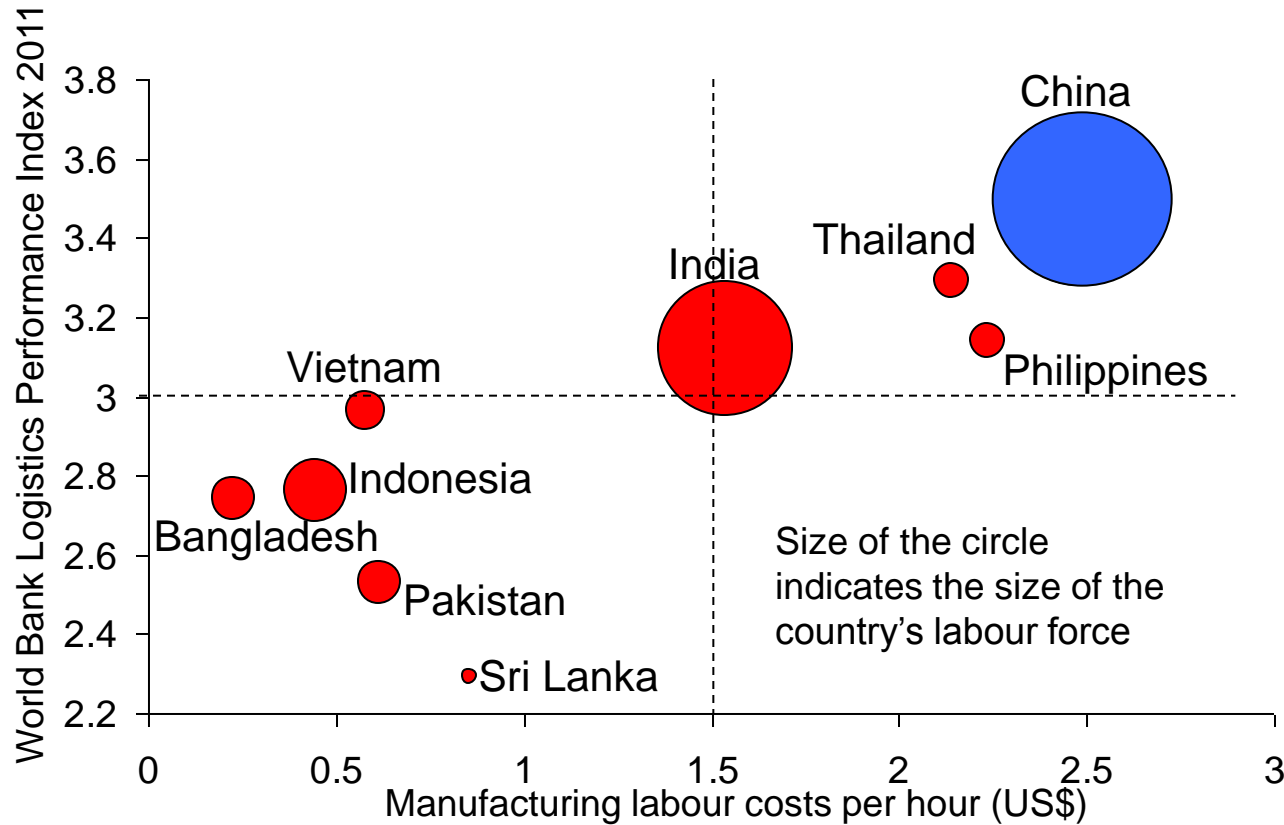
Old age dependency ratio, %. Source: World Bank.



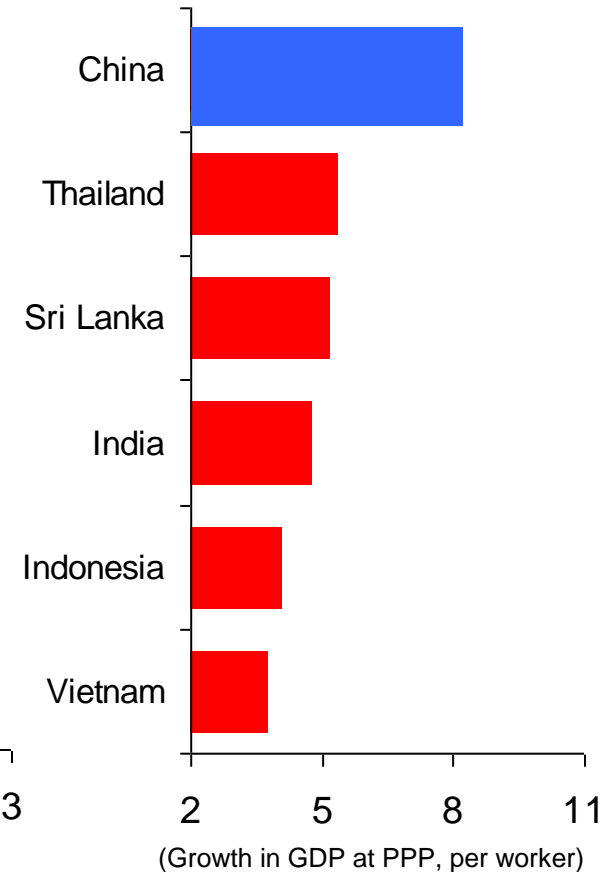
Real GDP/head, PPP. 2011 US\$.
Sources: BLS, EIU.

Are there any other Chinas out there?

Labour costs vs logistics vs labour force

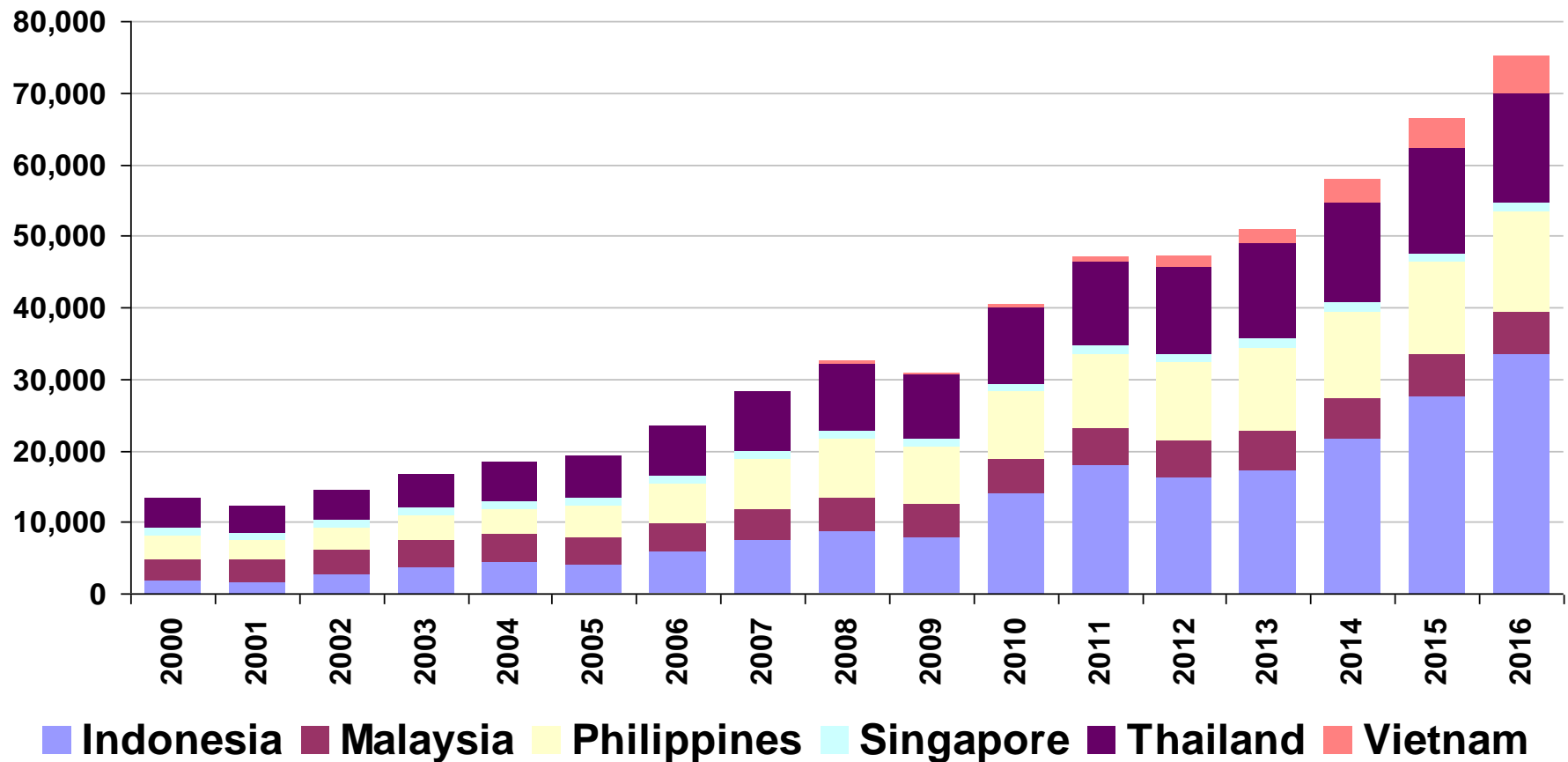


Labour productivity growth (% per annum)



Source: EIU CountryData 2012, World Bank

ASEAN: Integration and a rising middle class

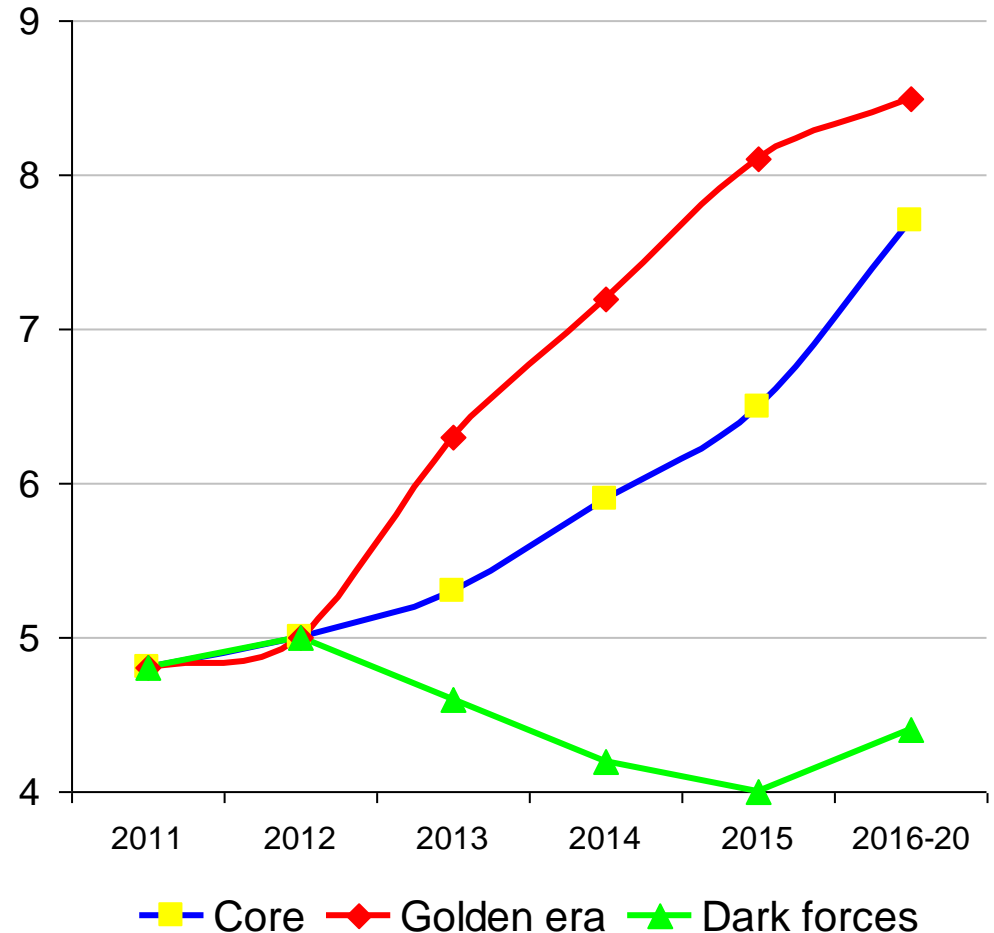


No. of households, 000's, earning more than US\$10K/year. Source: EIU.

Myanmar: Hello, Tiger

Investment opportunities

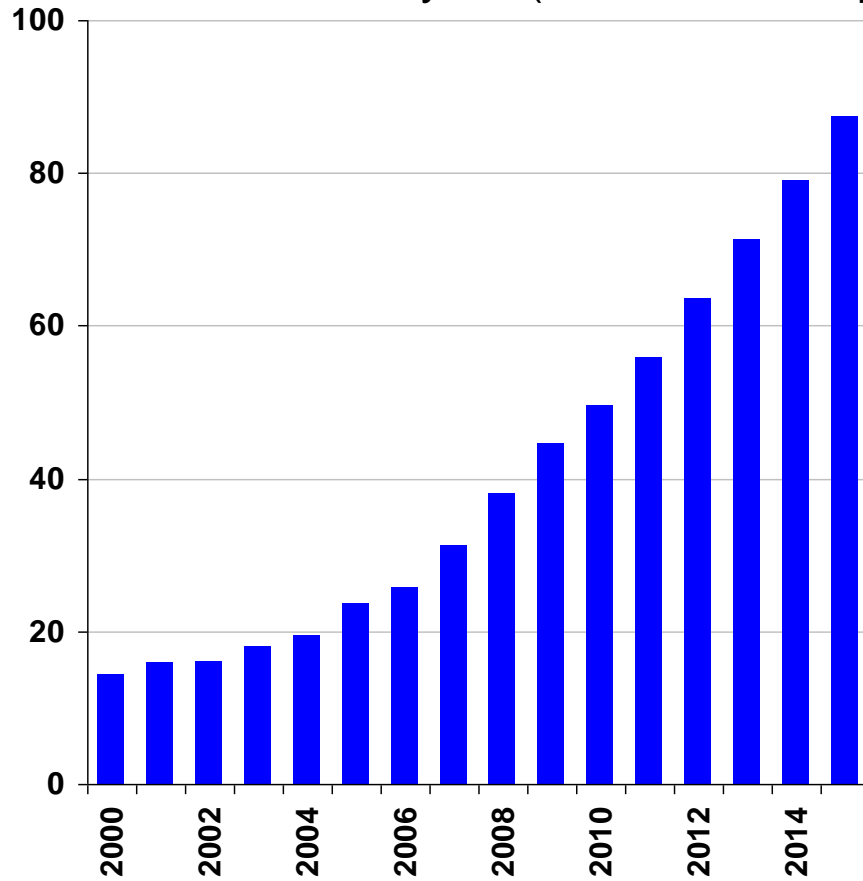
- Consumer goods—the population is poor, but markets for motorcycles, TVs, fridges, aircon offer scope for growth
- Agriculture—rice, pulses, oilseeds, forestry, fishing. Area under cultivation is low, so scope for large productivity gains by increasing farmed land area
- Minerals—oil, gas, copper, nickel, gold
- Infrastructure—raw materials for construction, affordable housing, transport infrastructure, construction equipment
- Financial services—SME lending, microfinance/rural banking, development finance, remittances/infrastructure financing. Links between banks and SOEs are too close
- Telecoms—mobile telephony, mobile towers, broadband, mobile services, fixed lines. Myanmar's ICT is ASEAN's most outdated
- Travel and tourism—hotels, hospitality, low-cost airlines, ecotourism
- Education/healthcare—health budget is rising, international agencies are expanding their presence



GDP growth scenarios, %. Source: EIU.

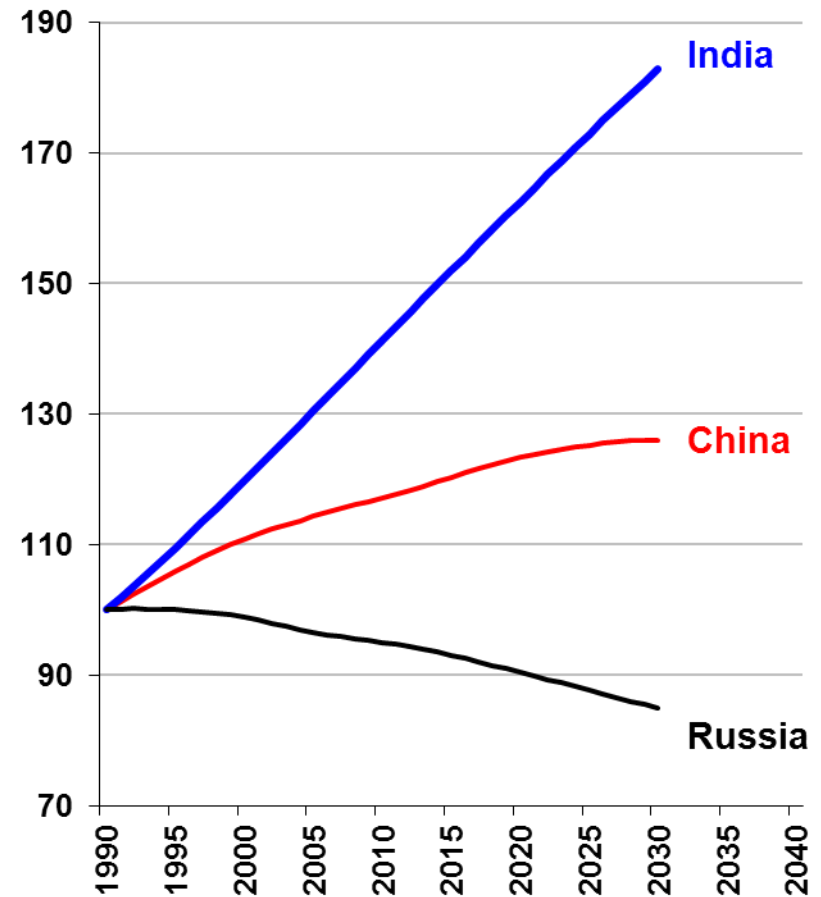
India: Consumption and demography

Number of households (m) earning more than US\$5,000 a year (constant 2005 prices)



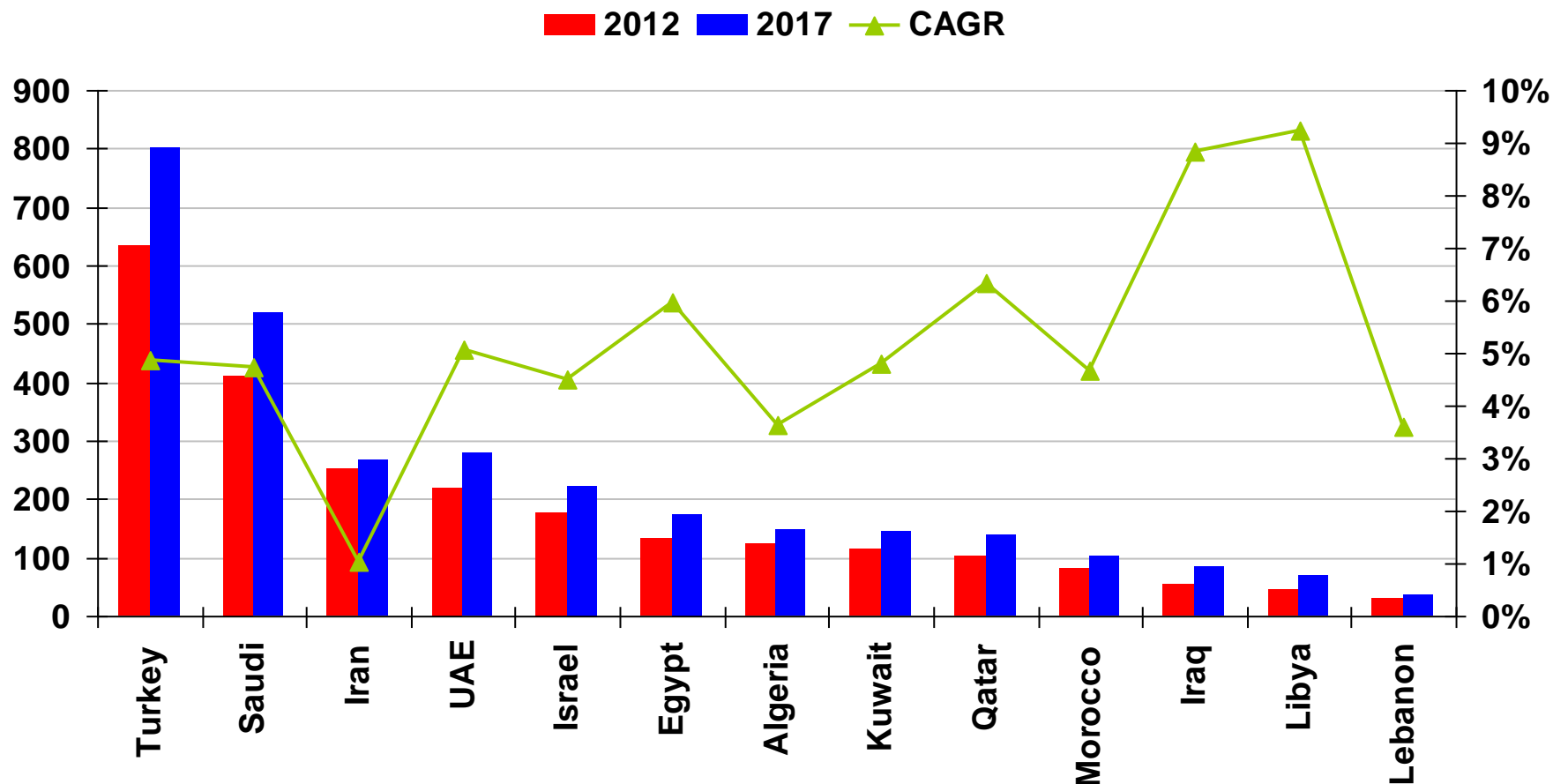
Source: EIU.

Population, 1990=100



Source: EIU.

MENA: Diverging performances



GDP growth rates, %; US\$ bn; 2005 prices. Source: Economist Intelligence Unit, CountryData.

MENA: Issues and challenges

- **GCC**

- Oil price
- Domestic political instability
- Domestic energy consumption
- Iran
- Global economic contagion
 - Financial
 - Trade

- **North Africa**

- Revolutionary transitions
- Insecurity in Sahel
- Euro zone slowdown

- **Levant**

- Syria overspill

- **Political risk**

- Instability
- Engaging with governments

- **Talent**

- Good talent: rare or expensive
- Nationalisation

- **Regulation**

- Lags behind vision and growth

- **Price pressures**

- Inflation
- Drive for value

- **Payment risk**

- Cashflow pressures

- **Supply chain**

- Cross-border trade: bureaucratic and subject to political interference

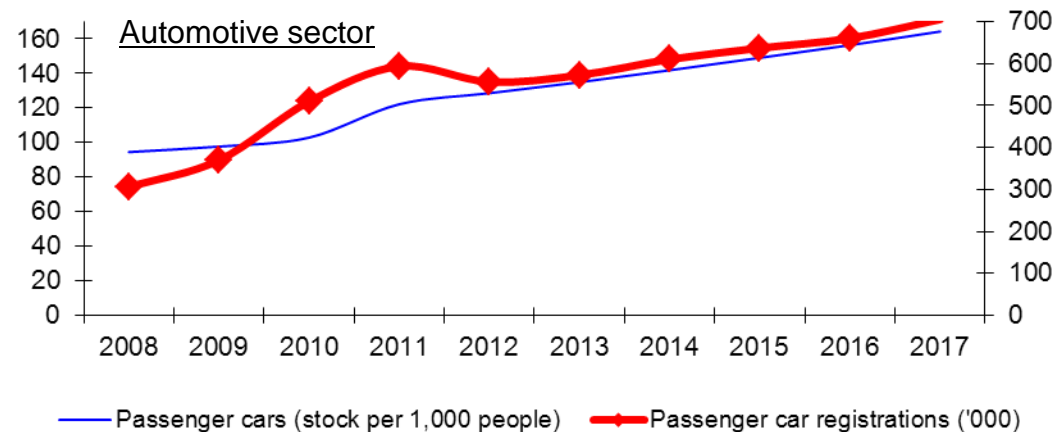
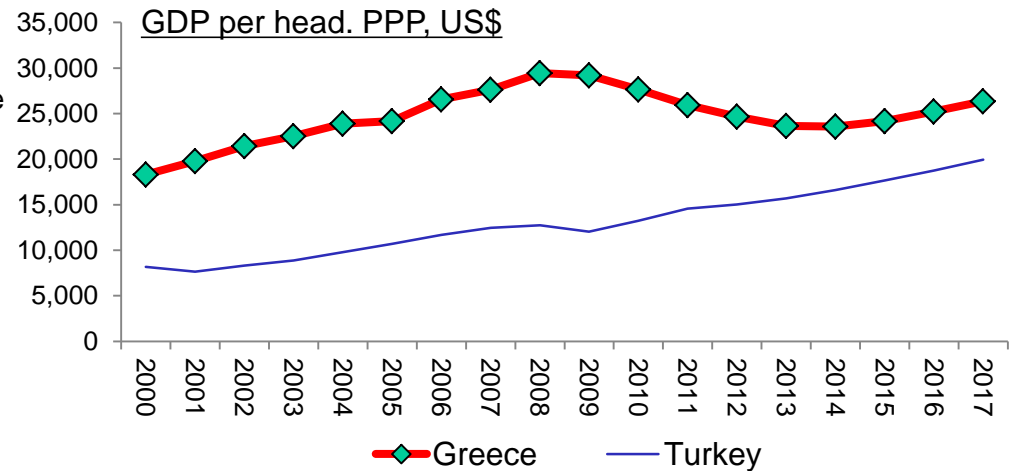
Turkey: From bridge to hub

Overview

- Politically polarised—witness recent protests
- Spillover from the eurozone crisis is a large downside risk. Spillover from regional instability may hamper growth, but the impact will not be significant
- The banking sector is sound, but the economy's reliance on external funding raises the risk of instability (large current-account deficit)
- Turkey's role as a regional production hub will rise
- The population is young by WEuropean standards
- The quality of the tax regime and the labour market are weaknesses in the business environment

Sectors to watch

- Healthcare, logistics, tourism, automotive
- Energy as the government seeks to diversify away from imported energy. Privatisations of energy firms
- Some sectors are already dominated by powerful local players, eg retail



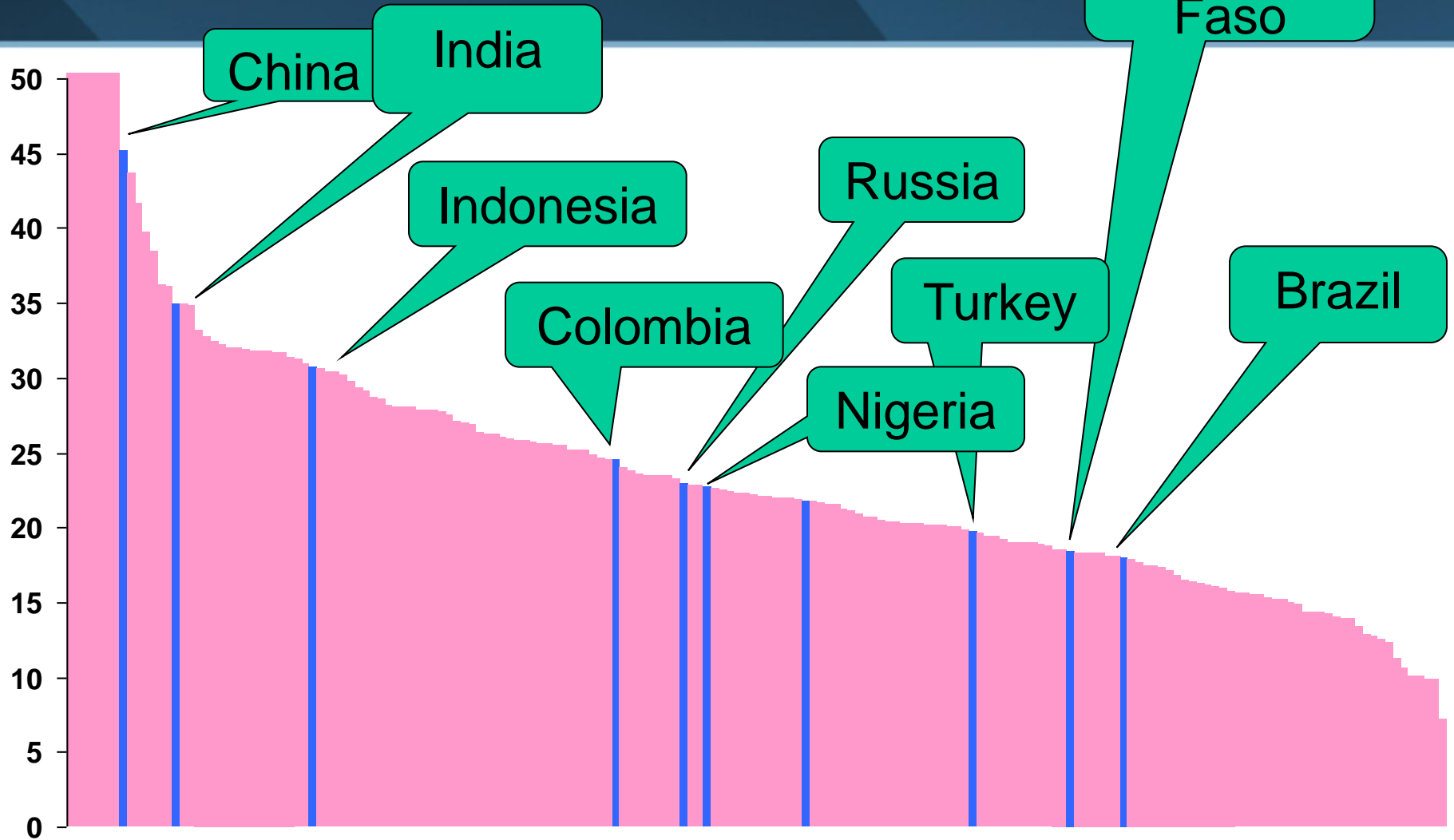
Source: EIU.

Lat Am: China has transformed the region

- China key to improvement in LA's terms of trade and expansion in export volumes
- China's share in LA trade rose from 1% in 1980 to 11% in 2011, becoming third trading partner after the US (21%) and the EU (13%)
- Trade between LA and China expanded by 51.2% in 2010 (vs 31% and 22% increase in LA trade with the EU and the US)
- China was the third largest investor in the region in 2010 (mostly extraction and natural resources but also infrastructure and manufacturing)
- China is also an increasing source of funding: since 2005 Chinese banks have lent more than US\$75bn to the region



Brazil: Investment laggard



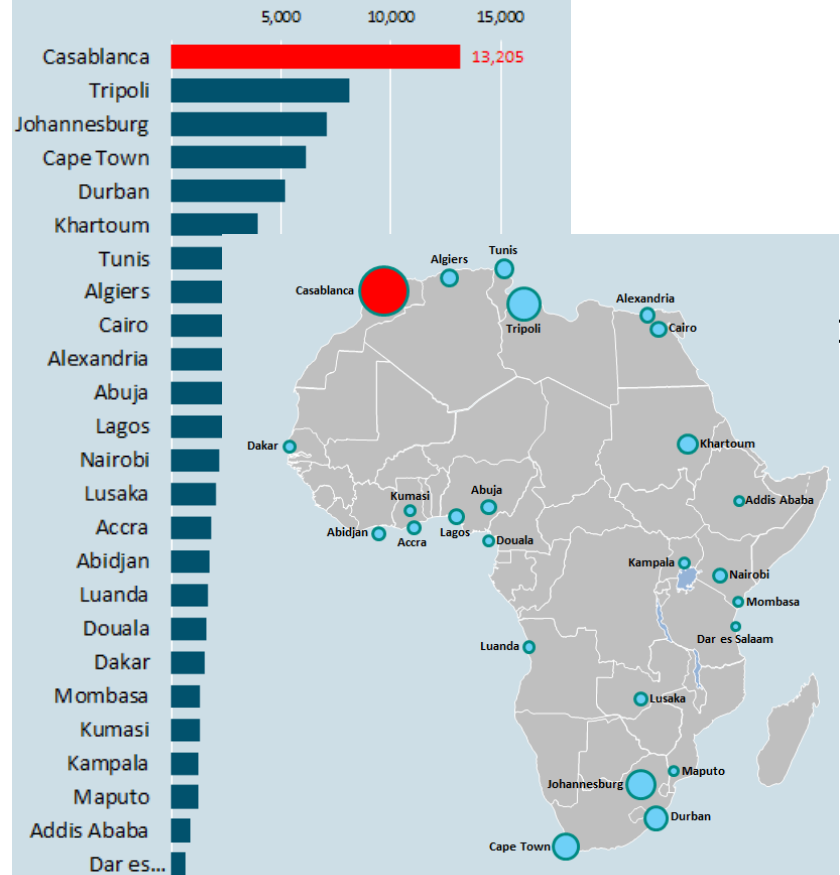
Real investment as a % of GDP. Source: Economist Intelligence Unit.

Africa: The final frontier?

- Africa is small: just 3% of the global economy
 - But includes fastest growing markets in the world
- In an ageing world, SSA's fertility rates remain high
 - 5.2 per female, cf global average of 2.5
- By 2100, on current trends
 - Nigeria's population rises to 700m
 - 950m in China
- Around 90m households earn more than US\$5,000 a year (PPP)
- Governance is improving
- Key sectors
 - banking, retail, infrastructure, agriculture, services (healthcare, education etc)

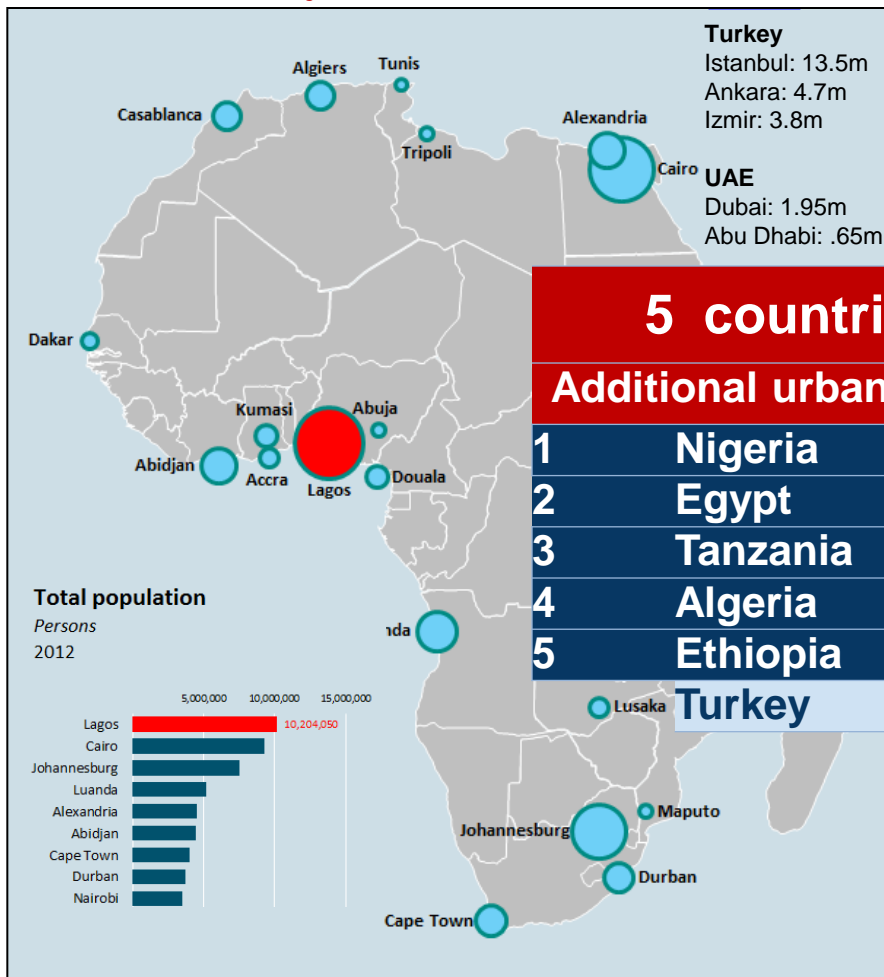
Total expenditure per capita

US\$ / capita
2012



Nigeria: The urbanisation opportunity

Major African cities

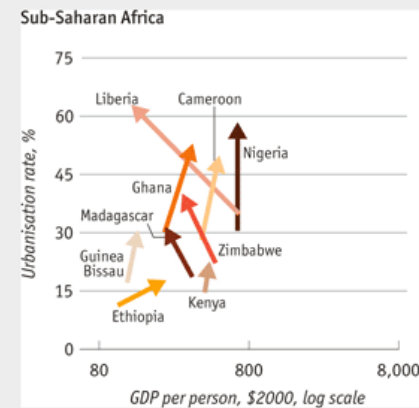
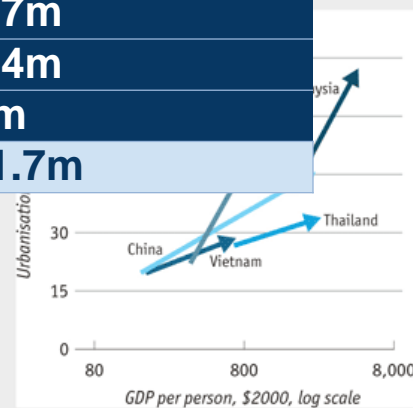
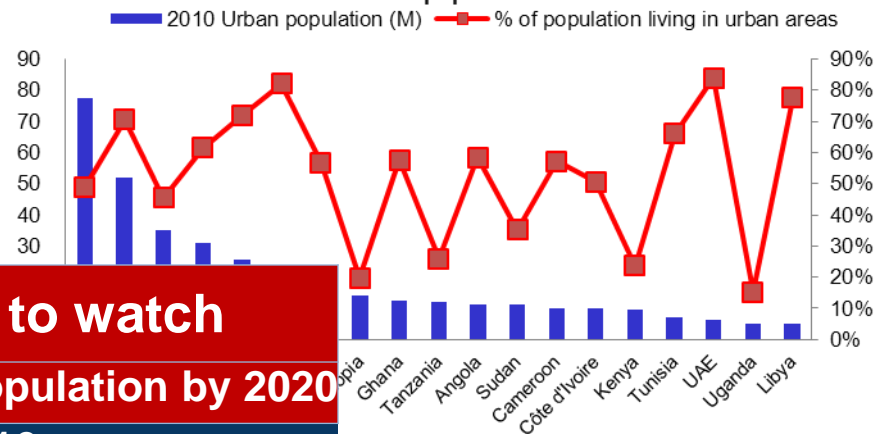


5 countries to watch

Additional urban population by 2020

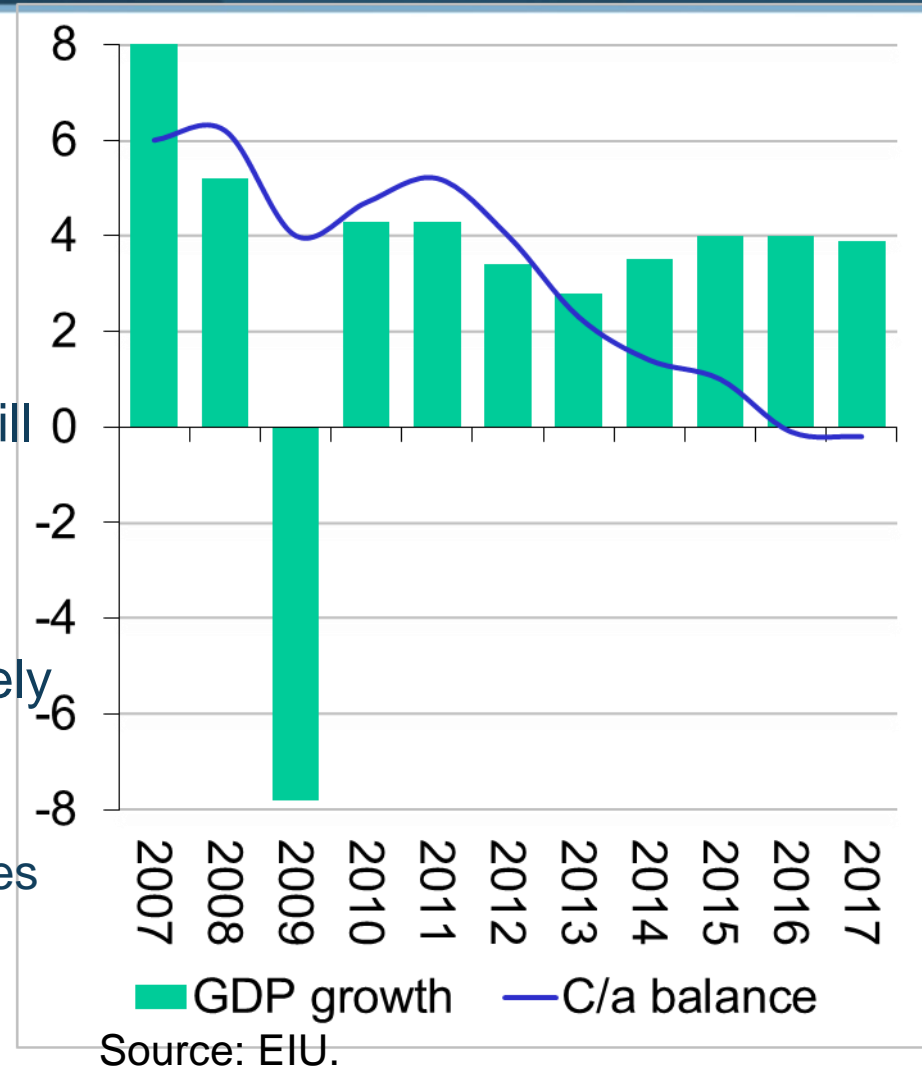
1	Nigeria	16m
2	Egypt	8m
3	Tanzania	7.7m
4	Algeria	6.4m
5	Ethiopia	6m
	Turkey	11.7m

Urban population

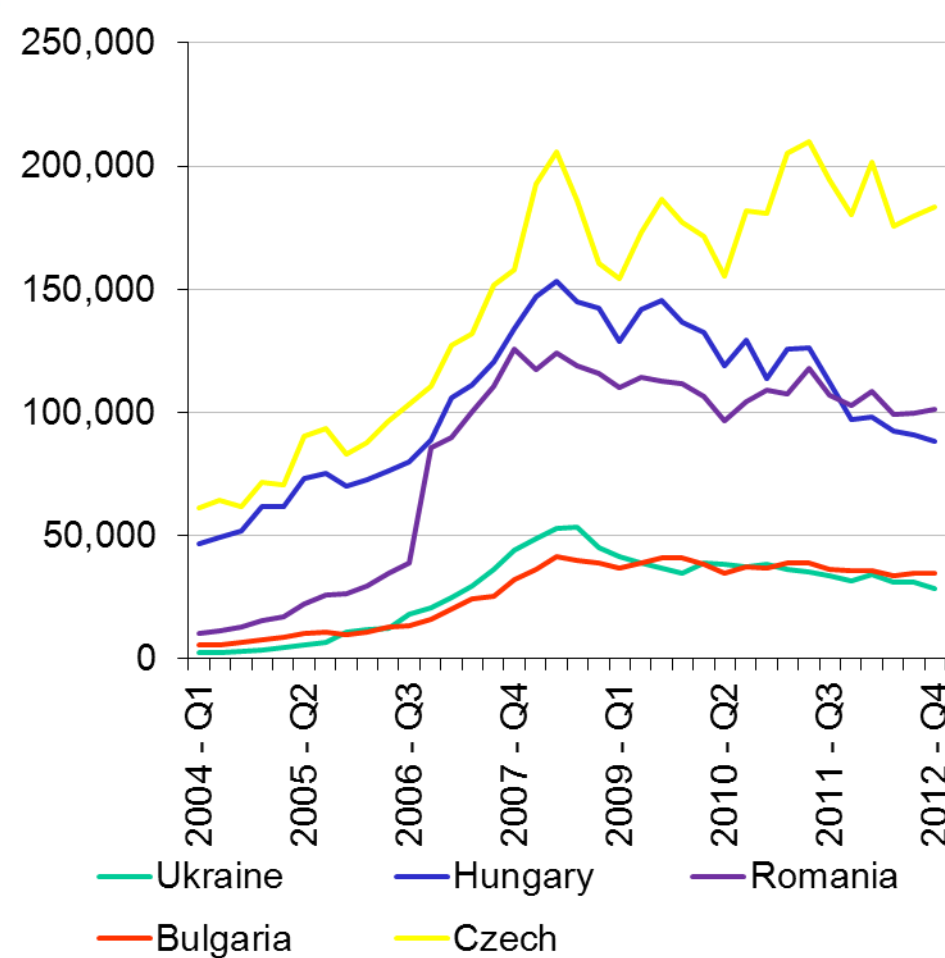


Russia: Underperforming its potential

- Putin correctly identifies Russia's problems
 - Lack of diversification
 - Low competitiveness
 - Poor infrastructure
 - Weak climate for innovation
- Putin's aura is fading, but there is still no coherent opposition
- Russia now a spoiler internationally rather than an initiator
- Fundamental change remains unlikely
 - Still leading role for state
 - Little improvement on rule of law
 - Growth won't return to pre-crisis rates
 - Resource dependence
 - Low fixed investment
 - Institutional weakness



CEB: Exposed to the euro crisis



- The region is highly exposed to euro crisis fallout via financial and trade channels
- In the medium term, catch-up potential means some growth premium over W Europe, but the best of the growth is now past
- Poland a key market to offset weakness elsewhere, but Poland needs fiscal reform
- Romania has the best longer-term growth outlook—the advantage of backwardness—but catch-up
- Czech Republic suffering because of the euro zone and austerity
- Bulgaria, Hungary, Ukraine stymied by poor political environment and demography

European bank lending by recipient country, eop, Euro m. Source: BIS.

Dei ex machina

Top business issues

- Hyper-globalisation
 - Chinese car firms come to Europe
- Manufacturing revolution
 - Rising Chinese wages
 - Helps other emerging countries
 - Erosion of economies of scale
 - Mass customisation and shrinking supply chains
 - Additive manufacturing (3D printing)
 - Reshoring in the US
- Managing for growth markets
 - Asia a growth market hub?
 - South-South innovation

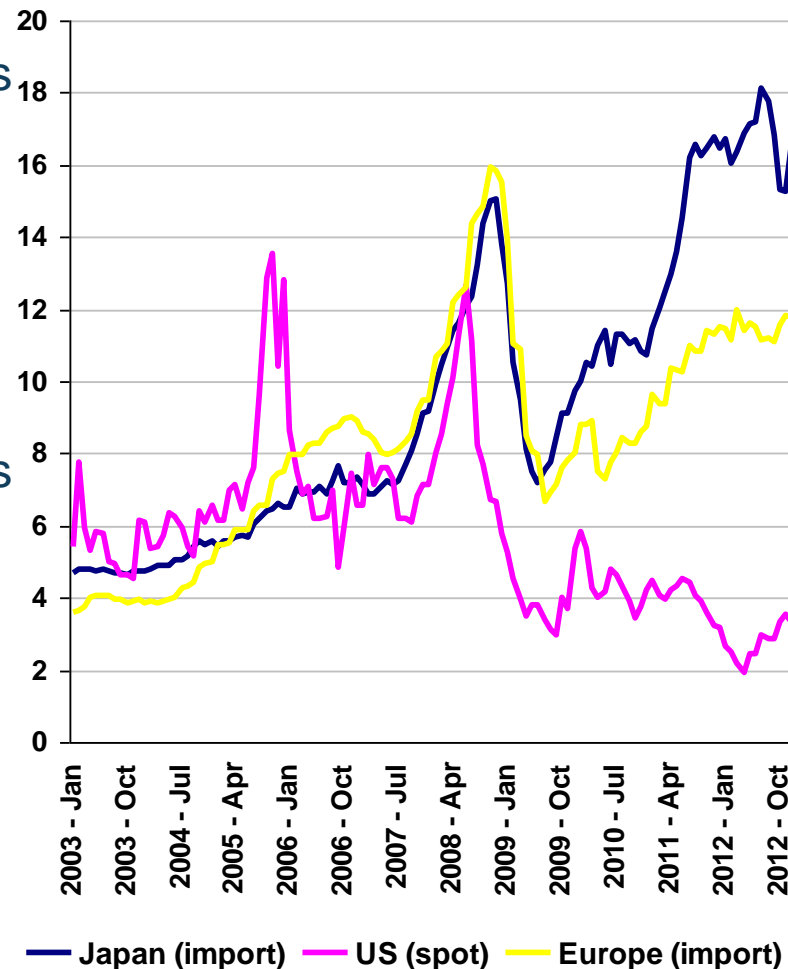


US gas: A global game changer?

- US gas exports could lower global gas prices—first licence already granted, others may follow
- Rising US gas production allowing fuel-hungry industries (aluminium, PVC etc) to move back to the US
- Some convergence between US and other global gas prices is likely
- Australia at risk from lower gas prices—gas infrastructure build-out for Gorgon project slated to cost US\$52bn (and rising)
- China has large shale gas reserves, but accessibility problems and poor regulatory environment are holding back investment

BUT:

- Fields deplete quickly
- Environmental issues abound



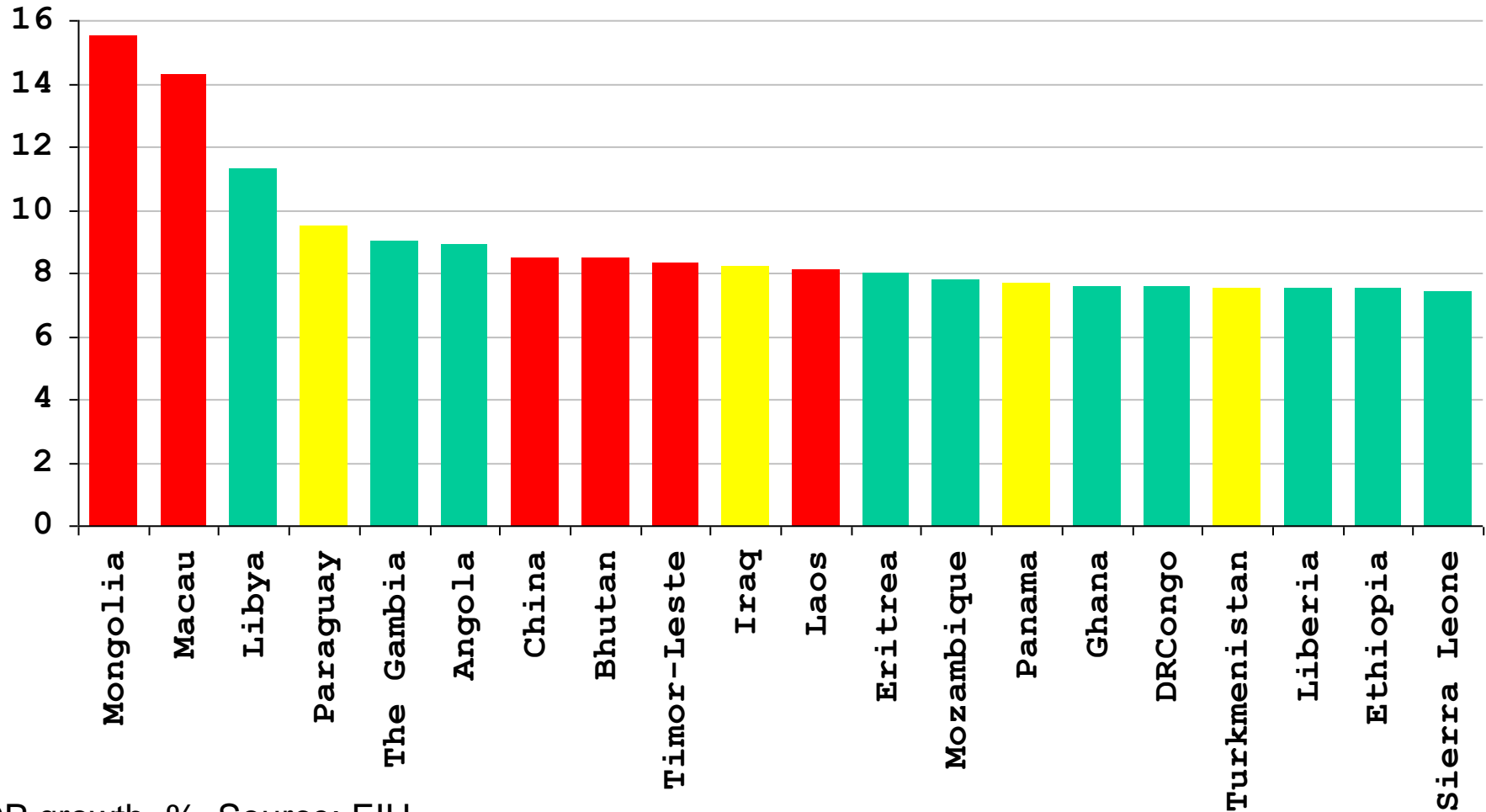
Natural gas prices, US\$/mbtu. Source: World Bank.

Asia: China's harmonious rise—really??



● Geopolitical flashpoints

Global round-up: The top 20 fastest-growing economies in 2013



GDP growth, %. Source: EIU.