The global economy—a brave new world

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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 feasible

Policies that might actually work
Euro zone: Watch the politics

Same bed, different dreams
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
Crisis 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

Euro zone break-up (exit of large member state(s))
• Damage to global financial system, real economy

Steep rise in interest rates in developed world
• Possibly associated with exit from QE
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


Real GDP/head, PPP. 2011 US$. Sources: BLS, EIU.
Are there any other Chinas out there?

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

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

GDP per head. PPP, US$

Source: EIU.

Automotive sector

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)

Source: EIU.
Nigeria: The urbanisation opportunity

Major African cities

- **Turkey**
  - Istanbul: 13.5m
  - Ankara: 4.7m
  - Izmir: 3.8m
- **UAE**
  - Dubai: 1.95m
  - Abu Dhabi: .65m

**5 countries to watch**

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

**Turkey** 11.7m
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

Source: EIU.
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

Asia: China’s harmonious rise—really??

Geopolitical flashpoints

Prepare for opportunity.™
Global round-up: The top 20 fastest-growing economies in 2013

GDP growth, %. Source: EIU.

Prepare for opportunity.™