

Review of Global Politics and Economy in 2017 and Outlook for 2018

Global Economic & Political Studies Div., Mitsui & Co. Global Strategic Studies Institute
2017/12/14

Contents

I. Political Situation in Major Countries and Regions

- (1) United States – Tax Reforms Become Focus of Domestic Politics; Foreign Policy May Be Implemented by Cabinet-level discretion and Congressional Authority p. 1
- (2) China – Full Launch of Second Term of Xi Administration at National People’s Congress in March; China to Pursue Superpower Diplomacy Based on Belt and Road Initiative p. 3
- (3) Russia – Putin Reelection a Certainty in 2018 Presidential Election p. 4
- (4) Europe – Uncertainty over Brexit Negotiations; Chaotic Brexit a Realistic Possibility p. 5
- (5) Middle East – “Bipolar Confrontation” between Saudi Arabia and Iran Causing Instability in Security Environment p. 6
- (6) Situation in Other Regions and Countries – Latin America, Southeast Asia, India p. 7
- (7) Current State of Economic Partnership Agreements – TPP11, NAFTA Renegotiations, EPAs, etc. p. 8

II. Economic Outlook

- (1) Forecast for the Global Economy – Economic Recovery Rippling Across the World p. 9
- (2) United States Economy – Growth Forecast to Reach Around 2.3%, Supported by Strong Personal Consumption and Capital Investment p. 9
- (3) European Economy – Eurozone to Maintain Strong Growth, UK Dependent on Brexit Negotiations p. 10
- (4) Chinese Economy – Slight Slowdown, But Steady Growth to Be Maintained p. 11

I. Political Situation in Major Countries and Regions

(1) United States – Tax Reforms Become Focus of Domestic Politics; Foreign Policy May Be Implemented by Cabinet-level discretion and Congressional Authority

<Domestic politics>

- In 2017, the Trump administration prioritized the Obamacare repeal among other major policy issues, such as tax reform and infrastructure development. However, its approach met with a

setback, and it was unable to secure enough support of Congressional Republicans. In the lead-up to the mid-term elections on November 6, 2018, the administration aims to enact a tax reforms bill centered on the reduction of corporation tax (currently above 35%) to 20%. If the unity of Congressional Republicans can be maintained, enacting the bill is possible. However, Congress is insisting on repealing part of Obamacare and has included clauses in the tax bill. For this reason, Congressional Republicans' unity could come apart once again.

- In the mid-term elections, 33 Senate seats (of 100 in total) and all 435 House seats are on ballot. Republican Party is currently expected to maintain its majority in both chambers. Opinion polls show that support for the Democrats exceeds that of the Republicans by approximately 10 points, but considering the breakdown of the 33 Senate seats up for reelection (25 are currently held by the Democrats and just eight by the Republicans), the Democratic Party will have to fight a "defensive election" in the Senate. If Republican Party turns to minority in the House of Representatives, Republicans will not be able to lead the budget process or FTAs' ratifications. Even if the administration wraps up the NAFTA renegotiation, it would then struggle to ratify the agreement in Congress.
- The relationship between the Trump administration and the Congressional Republicans has been souring. The President has criticized the Congressional Republicans' ability to pass bills, and some Republican senators, who are not seeking re-election, have publicly voiced criticism of the President. The President now finds himself in a situation wherein he is not able to work either with the Republicans or the Democrats.
- The President's Trade Promotion Authority (TPA), which the President needs to negotiate FTAs, will expire at the end of June 2018. The Trump administration plans to seek renewal of the TPA from Congress. However, trade negotiations are a policy area for which it is difficult to produce short-term results, and the President appears to be undecided about how seriously to engage in FTA negotiations.

<Foreign Affairs>

- Discord within the Trump administration often erupts, as evidenced by a spate of reports that Secretary of State Rex Tillerson steps down shortly. There have been several instances that reveal uncertain US foreign policy, resulting from a lack of coordination between the President and the Cabinet, and inconsistent comments by the President. We will likely see some cases where Cabinet members and Congress implement policy measures within their discretion and authority, sidelining a President who has been ignoring international agreements and conventions.
- Regarding North Korean nuclear and missile development, an intercontinental ballistic missile that would put the entire US soil within its range was launched on November 29, 2017. In response, the Trump administration is expected to focus for the foreseeable future on building an international framework to cut off as much of the funding and resources supplying North Korea as possible. The US will seek cooperation from China in increasing the pressure on North Korea, at the same time building a framework to increase pressure by cohosting a foreign ministers' summit meeting with Canada in January 2018, with Japan and 18 countries that participated as United Nations forces during the Korean War. Meanwhile, the US Congress is

preparing to pass a bill that would place sanctions on foreign financial institutions that trade with North Korea, such as Chinese.

- As for relations with China, during his visit to China in November 2017, President Trump criticized previous US administrations "for allowing [the US] trade deficit to take place and to grow." He faced with a wave of criticism domestically for not taking a tougher line with China to address the trade deficit. The general view is that President Trump's visits to Asian countries produced no concrete results. Some US experts, however, have a view that the Trump administration will begin to take a tougher stance on China as soon as preparations are in place within the USTR.
- In relations with Russia, attention will be focused on whether President Trump will actually implement the law to strengthen sanctions on Russia (passed into law in the summer of 2017) as scheduled on January 29, 2018. President Trump has been rather reluctant to strengthen sanctions, but there are many legislators who, considering the gravity of Russian intervention in the 2016 presidential election, insist on the adoption of a hardline stance against Russia. If the investigation into the "Russia-gate" suspicions is even further extended to the President or his "entourage", the President's political influence will be undermined, and it would be difficult for him to implement the various policies.

(2) China – Full Launch of Second Xi Administration at National People's Congress in March; China to Pursue Superpower Diplomacy with Belt and Road Initiative as a Pillar

<Domestic politics>

- At the National Congress of the Communist Party of China held in October 2017, General Secretary (President) Xi Jinping successfully appointed the senior party leadership as he planned for the most part. The next focus of attention will be the National People's Congress scheduled for March 2018, which will decide the posts of President, Premier (equivalent to prime minister), and the leadership of various national bodies, including the heads of government ministries and offices. Wang Qishan stepped down as a member of the Politburo Standing Committee at the party congress, but there are predictions that he will be appointed to a new, prominent position, such as Vice President, to support the Xi Jinping administration. Accordingly, the National People's Congress in March, which marks the full launch of the second Xi administration, is attracting attention.
- Control of the party will be further strengthened. As one of the anti-corruption measures, a new National Supervisory Commission was established as an independent body alongside the State Council and the Supreme People's Court (the highest court). It is expected that the new body will have strong authority over all persons executing official power. It is thought likely that the Communist Party will continue to strengthen its supervision of corporate activities, and close attention will be paid to the question of whether, or to what extent, this supervision will have an effect on actual business activities.

<External Affairs>

- China has promoted "superpower diplomacy", skilfully adopting both cooperative and hardline

approaches, and it is increasing its influence in the global community. It plans to make the Belt and Road Initiative (BRI) function as a “global public good” provided by China, and to orchestrate harmonious development, shaped around economic cooperation, with the countries along the route of “Belts and Roads”. Furthermore, China will host its first import expo in November 2018, distinguishing itself from the US, which is leaning toward protectionism. At the same time, China is expected to maintain an uncompromising approach to issues that touch upon its core interest related to sovereignty.

- In relations with the US, it is expected that the personal trust built between Xi and President Trump during the three summit meetings held in 2017 will be leveraged to help both countries avoid any serious conflict. On the trade front, China emphasized a conciliatory stance by signing agreements of more than \$250 billion worth of major business deals during Trump’s visit to China in November 2017, and through execution of the “100-day action plan” to eliminate the trade imbalance, as well as formulation of a “one-year plan”. In terms of security, China will seek to increase exchanges between high-ranking members of the People’s Liberation Army and the US Army. At the same time, however, China will take measures to reduce American influence in areas such as the South China Sea and Taiwan.
- Regarding North Korea, China has taken the position that the dispute is basically the issue between the US and North Korea. While continuing to put pressure on North Korea, China has encouraged the two countries to adopt a “dual suspension” approach to resume talks (the US to provisionally stop military exercises in exchange for North Korea’s halting of its nuclear and ICBM development programs).
- In relations with Japan, there are ongoing efforts to arrange a Japan-China-South Korea summit meeting in Japan in early 2018 (Chinese Premier Li Keqiang’s visit to Japan). If this summit is realized in the early months of 2018, a visit by Prime Minister Abe to China, and a reciprocal visit by President Xi to Japan in 2018 will become realistic. If the mutual visits by the two leaders are realized, it would symbolize improved relations between Japan and China, adding impetus to growing expectations for cooperation between Japanese and Chinese companies on projects related to the Belt and Road initiative.

(3) Russia – Putin Looks Set for Reelection in 2018 Presidential Election

<Domestic politics>

- The reelection of President Putin, 65, in the presidential election scheduled for March 18, 2018 is seen as a certainty. The Putin administration is expected to continue through to the completion of its second term in 2024. His approval rating is hovering above 80%, and stable government administration is expected. However, the Russian constitution does not permit the same person to be appointed President for three consecutive terms. Measures, such as amending the constitution, would be required for President Putin to stay in power from 2024 onwards. The issue of a presidential successor is a medium to long-term risk for Russia.
- The IMF has forecast real GDP growth in Russia of 1.6% in 2018, and around 1.5% from 2019 onwards. It is important for Russia to diversify its resource-dependent economy in order to escape low growth. The Putin administration recognizes the importance of structural reforms,

but the top executives of Russia's state-owned resources companies have close personal links with President Putin, and it would be difficult to implement reforms that could lead to the destruction of the vested-interest structure.

<External Affairs>

- In view of the law being passed in the US in August 2017 strengthening sanctions against Russia, the growing "Russia-gate" suspicions, and domestic public sentiment that would welcome hardline comments against the US in the lead-up to Russia's presidential election, there is little prospect of an improvement in relations with the US in 2018.
- Russia's presence in the Middle East is expected to increase even further. Regarding the situation in Syria, the Putin administration has been leading talks, alongside countries such as Iran and Turkey, to stabilize the situation in Syria. The Putin administration is also deepening its relations with Saudi Arabia through the construction of nuclear power stations and weapons exports.
- In relations with Japan, President Putin is planning to have summit talks with Prime Minister Abe at the St. Petersburg International Economic Forum in May, on the assumption that he will be reelected in the Russian presidential election in March 2018. Difficult negotiations are expected on the issues of territorial disputes and the peace treaty, but agreement has already been reached on joint economic activities in the four northern islands (such as seafood aquaculture and greenhouse vegetable cultivation). It seems likely that the good relations between the two leaders will continue to benefit Japanese business with Russia.

(4) Europe – Uncertainty over Brexit Negotiations; Chaotic Brexit is a Possibility

<Direction of Brexit> (Figure 1)

- In order to meet the March 2019 deadline for the conclusion of negotiations, it will be necessary to finalize talks by October 2018 and move on to ratification procedures by the European Parliament and national assemblies of the EU member states. The UK has reached a broad agreement with the EU on the terms of withdrawal, including the amount of the UK's "divorce bill." However, over the UK's future relationship with the EU, including FTAs, opinions are divided even among members of the UK Cabinet, revealing significant division within the country. If the UK government is unable to form a consensus on its negotiation policy, a breakdown in negotiations and a chaotic withdrawal will become increasingly realistic. As such, the possibility of there occurring a major shock on the markets cannot be ruled out.
- UK Prime Minister Theresa May's lowering unifying power is a cause of concern. Within the ruling party, there is fierce opposition between proponents of a hard Brexit and supporters of a soft Brexit that prioritizes economic rationality, and a path for agreement has yet to be seen on the UK and EU's "future relationship", including FTAs. If Ms. May is forced to resign as a result of an intensification in this conflict, a possibility of the chaotic exit will increase.
- Negotiations on the "future relationship" between the UK and the EU are expected to begin in the first half of 2018. Even if talks do begin, reaching agreement on FTAs and other agendas by October 2018 is still thought to be difficult. There is a general consensus that the UK and the

EU will set a “transitional period” of around two years after the negotiation deadline, effectively postponing the withdrawal with the aim of avoiding a “chaotic exit.”

<Situation in Continental Europe>

- In the series of elections held in major EU countries in 2017, pro-EU parties garnered majorities in all countries, and EU countries have maintained unity to face the Brexit negotiations. For the time being, the cause of destabilization will be the Italian general election, which will be held on March 4th 2018. It is thought that a stable government will be difficult to form because of a splintering in support for political parties among voters. Also, there is strong public criticism in Italy of the EU over the refugee problem. Depending on the outcome of the election, populist policies could gain influence and hinder the execution of overall EU policy. Another concern is an “east-west conflict” within the EU, as Poland and Hungary oppose the EU policies being led by Germany and France.
- In Germany, coalition negotiations after the federal election have stalled, and the possibility of another election cannot be discounted. There will be no major changes in EU policy, regardless of which parties form the government, but a political vacuum in Germany is likely to have a certain impact on EU reforms, such as anti-terrorism measures, refugee policies, and the introduction of a common budget in the Eurozone.

(5) Middle East – “Bipolar Confrontation” Between Saudi Arabia and Iran Causing Instability in Security Environment

- As the US loses its presence as a leading player in forming the Middle East order, a “bipolar confrontation” between two regional giants – Saudi Arabia and Iran – has taken clear shape. Saudi Arabia, which has improved its relationship with the US since the inauguration of the Trump administration, has led the formation of Iran’s encirclement. Also, President Trump has recognized Jerusalem as the capital of Israel. These issues are bringing instability to the security environment in the region. Close attention is being paid to future moves by countries such as Iran, which for now is quietly observing the situation, and Russia, which is increasing its presence in the Middle East (Figure 2).
- On November 4, 2017, Saad Hariri, the Prime Minister of Lebanon, which is influenced by Iran, suddenly announced his resignation, but later withdrew it. It is believed that the original announcement was brought about by pressure from Saudi Arabia, which has political influence in Lebanon. For Crown Prince Mohammad bin Salman of Saudi Arabia, who is seeking to retain the support of Saudi citizens by displaying strong leadership, having Iran as a hypothetical enemy itself is of use for his agenda, and Saudi Arabia is expected to continue taking a provocative line in its Iranian policy.
- A major corruption exposure is sweeping Saudi Arabia against members of the royal family, senior ministries, entrepreneurs, and other elites. The Crown Prince’s aim is to strengthen his power base by clearing out opposition forces. On the economic front, however, little progress has been made in the industrial diversification policy set out in Saudi Vision 2030 (announced in April 2016), and negative growth was posted in the first and second quarters of 2017. Should the state-run oil company Saudi Aramco’s IPO (planned for 2018) prove to be less successful

than anticipated, the Crown Prince's political power will potentially be reduced. (Figure 3)

- Regarding the US sanctions on Iran, which have been temporarily suspended under the nuclear agreement with Iran, the focus for the immediate future will be on the decision of the US administration, when the time comes to review the temporary suspension (January 2018). European countries are appealing to the US to continue with the suspension of sanctions, but President Trump has made repeated hostile comments concerning Iran. In 2018 as well, Mr. Trump's behavior in respect to Iran and political developments in the US will require attention.

(6) Situation in Other Regions and Countries

<Latin America> – Fate of Center-Right Administrations to Be Decided by Succession of Elections in Latin American Countries

- In 2018, there will be a series of presidential elections in various Latin American countries (Figure 4). The survival of center-right administrations in the major countries will be a common focus of attention across the region. In Brazil, the center-right Brazilian Social Democracy Party (PSDB) – the second largest governing party – has pledged to strengthen fiscal discipline and promote business-friendly labor reforms. The PSDB candidate is expected to perform strongly in the Brazilian presidential election (October) as the PSDB has not been caught up in corruption scandals, which is an important issue to voters, and the forecast of a return to positive growth in 2017 will work favorably for the governing party.
- In the Mexican presidential election (July), multiple center-right candidates will be running, and they are expected to struggle because of the resultant split in the vote. The leading candidate Andrés Manuel López Obrador is a left-wing anti-American hardliner arguing for the redistribution of wealth and the shutting out foreign investment from oil development. If anti-US sentiment increases among Mexicans due to tangled NAFTA renegotiations, Orbrador's support base is expected to grow even further. That said, even if he is elected president, his political party, MORENA, is expected to remain a minority party in the legislative elections held at the same time as the presidential election. That would make for a difficult government administration for MORENA.

<Southeast Asia> – ASEAN Diplomacy's Focus on Skillful Handling of Two Superpowers, the US and China

- Southeast Asian countries, mainly the ones that have been criticized by Europe and the US, such as Myanmar (which is faced with the Rohingya crisis) and Cambodia (which has stepped into the dissolution of the opposition party) are building closer ties with China, and it seems likely that China's influence on ASEAN will continue to grow. In December 2017, Myanmar agreed to deepen its economic cooperation with China even further, and in January 2018, Cambodia is expected to obtain a total of US\$7 billion in investments from China.
- As shown by Vietnam and the Philippines welcoming the leaders of both the US and China during the November 2017 APEC meetings, the ASEAN countries are investing effort in skillfully "handling" both the US, advocating an America First policy, and China, which is increasing its effective control of the South China Sea. It is expected that similar diplomatic efforts to ease

pressure from the US and China will continue in 2018.

<India> – Progress Made with Reforms, but Concern Looms over Possible Fiscal Deterioration Triggered by a Spate of Populist Policies

- In 2017, the Modi administration achieved introduction of India's most ambitious tax reform (Other two planned big reforms are, land acquisition and labor laws reform, but these two seem impossible before the next national election, scheduled for 2019) as, the GST (Goods and Services Tax), and it is working to promote other reforms, including infrastructure developments and banking reforms. India's ruling party still not in majority in the Upper House. However, this situation is expected to be resolved in 2018, and progress will be made with structural reforms. Prime Minister Modi enjoys high public approval ratings, and it is regarded as a certainty that the ruling BJP will win a general election planned for 2019. In that case, the Hindu nationalist group — the support base of the BJP — might pick up steam, and that could increase the tendency to exclude other religions. In addition to economic stimulus measures, totaling 9 trillion rupees (announced in October 2017), since government expenditure is expected to increase in the lead-up to the 2019 general election, there are concerns over a deterioration in the government's finances.

(7) Current State of Economic Partnership Agreements

- After the US withdrawal from the TTP, efforts are now being made to bring the TPP into effect among the 11 remaining countries. In November 2017, a broad agreement was reached at a ministerial meeting. However, considering the negotiating policy of the Canadian government, which is not rushing to conclusions, and the fact that agreement has yet to be reached on some outstanding issues, TPP is not expected to come into effect until 2019 at the earliest. As for RCEP (Regional Comprehensive Economic Partnership) negotiations as well, the original target of effectively reaching an agreement in 2017 has been postponed, and negotiations are set to continue in 2018.
- The renegotiations of NAFTA, for which the goal was to reach an agreement in 2017, will continue into next year. The last five rounds of talks have seen difficulties in creating a consensus on matters such as rules of origin, trade remedy measures, and a sunset clause, which requires the agreement to be reviewed every five years. The US proposals are opposed not just by Mexico and Canada, but also by US industry. While the possibility of US withdrawal from NAFTA emerges, as part of Mexico's efforts to reduce its reliance on the US, Mexico has been taking various approaches, such as the participation in TPP11, the establishment of associate memberships of the Pacific Alliance, and increasing grain imports from within the Latin America region.
- A Japan-EU EPA was agreed upon in December 2017. The aim is to sign the agreement in 2018, and for it to come into force in 2019. The ISDS clause (Investor-State Dispute Settlement), for which the EU and Japan have differing opinions, is left open for separate discussions from EPA-related ones. The EU is also aiming to reach agreement in FTA negotiations with the Southern Common Market (Mercosur), and is soon to begin FTA negotiations with Australia and New Zealand as well.

II. Economic Outlook

(1) Forecast for the Global Economy – Economic Recovery Rippling Across the World (Figure 5)

- The pace of the global economic recovery is picking up. Contributing factors are that strong US and Chinese economies have brought about knock-on effects to Japan, Eurozone countries, and major emerging economies, and that many resource-dependent nations are recovering from the worst period of the economic downturn against the backdrop of recovery in commodities prices. The IMF has forecast that global real GDP growth will recover to an annual rate of 3.6% in 2017, from 3.2% in 2016 (the lowest rate since the global financial crisis), and it predicts a similar growth rate of 3.7% for 2018.
- While economic conditions strengthen, there is a concern that excessive monetary easing might lead to a future asset bubble, and the FRB (Federal Reserve Bank) has implemented interest rate hikes and balance sheet reduction. At the same time, the ECB (European Central Bank) is moving towards a reduction of quantitative easing. While inflation rates are hovering low, both the FRB and ECB will likely maintain a cautious pace in rolling back their monetary easing policies, but careful attention should be paid to risks that lead to significant corrections in the financial markets and outflows of money from emerging economies.
- Other risk factors include geopolitical risk surrounding North Korea. If the world grows acutely aware of the risk of war breaking out, triggered by reasons such as the evacuation of Americans living in South Korea, a negative impact on the global economy, through substantial drops in stock prices and cooling economy sentiment for corporations and households, is to be expected. This would likely have a particularly significant impact on East Asian countries, such as Japan and South Korea. Potential chaos resulting from an impasse in the Brexit negotiations, and a major slowdown in investment in Chinese real estate development are other risk factors. On the other hand, if US measures such as tax reforms are realized, it is likely to contribute to boosting economies.

(2) US Economy – Growth Forecast to Reach Around 2.3%, Supported by Strong Consumer Spending and Capital Investment

- In 2017, the US economy's upward momentum was accelerated in response to robust consumer spending and capital investment. The recovery was partly prompted by post-hurricane reconstruction demand, and a future reactionary decline can be expected. However, the strong conditions are forecast to be maintainable against a backdrop of improving employment and strong corporate profits trends. Real GDP growth in 2018 is likely to be close to the 2.3% level forecast by the IMF.
- If tax reforms centered on the reduction of corporate and income taxes are realized, this will stimulate corporate and personal consumption and edge up the growth rate in 2018. However, if this also leads to changes in market conditions, such as rising interest rates, the tax reforms' positive contribution to economic conditions may be limited.
- Growth in personal consumption will remain firm at above the 2% level because of increasing employment and rising asset prices. The unemployment rate has improved to its lowest level of

2000, which was the peak of the IT bubble, and the most broadly defined unemployment rate (which also categorizes persons employed part-time for economic reasons as unemployed) has also improved to its pre-financial crisis level. It seems likely that wages will continue to rise slowly as a result of further tightening in the labor market.

- However, when looking at the number of new car sales, attention should be paid to a future reactionary downturn from the sharp increase caused by temporary, hurricane demand, which led to a large-scale increase in new car sales in the second half of 2017. The delinquency rate on auto loans has risen to its highest level in four years, and there is a possibility for banks to tighten lending criteria for auto loans. Considering these factors, car sales will be sagging somewhat in the coming months.
- Since 2017, capital investment has been on an upward trend across a broad range of sectors. Behind this is the situation whereby banks' lending criteria have remained rather relaxed while corporate profits continue to improve. As oil prices rise, there are signs of a bottoming out of capital investment decrease in industries that have negatively affected its downward slide. For the foreseeable future, this environment is likely to show little change, and strong capital investment is expected to continue. If a tax reform bill that also allows immediate depreciation of capital investment is passed, this may further stimulate capital investment.
- Meanwhile, growth in housing investment is forecast to be sluggish. The low interest-rate environment will continue, but a construction industry labor shortage will lead to falling housing supply and rising prices, which will hinder a recovery.
- Under newly-appointed FRB Chairman Jerome Powell, the balance sheet reduction that was started in October 2017, along with interest rate hikes, is set to continue. The FRB is expected to continue raising interest rates carefully, at the pace of around three times per year, while keeping a close eye on the impact of its balance sheet reduction on the domestic and overseas economies and financial markets, and the Trump administration's handling of the government. If the economy exceeds expectations for reasons such as tax reforms, it is possible that there will be a fourth interest rate hike in a year.

(3) European Economy – Eurozone to Maintain Strong Growth, While UK Dependent Economy on Brexit Negotiations

(Eurozone economy)

- In 2017, the Eurozone economy was strong, against a backdrop of strong personal consumption brought by improving employment conditions, and an increase in exports in response to the recovery in the global economy. The real GDP growth rate was above 2%. Capital investment also showed strong growth in response to a high facility utilization rate and continuing monetary easing, and it is expected that the economic recovery trends will also continue in 2018, and a real GDP growth rate of around 2% is expected.
- Consumer price inflation has remained in the mid 1-2% range, and in 2018 the ECB is unlikely to achieve its policy target of “below, but close to, 2%”. With strong conditions in the economy, the unemployment rate is likely to continue falling. However, even by the end of 2018, the

unemployment rate is likely to be 8.5% (European Commission forecast), which is higher than it was before the financial crisis, and labor supply-demand conditions have yet to tighten. For the foreseeable future, there is a strong possibility that the rate of wage increases will remain low, and acceleration in inflation will not be likely.

- In October 2017, in response to favorable economic outlook, the ECB decided to cut its bond-buying to EUR 30 billion per month (from the current level of EUR 60 billion per month) from January 2018, and also decided to maintain this level until September 2018. As it struggles to meet its policy target inflation rate, and in view of governments' excessive liabilities challenges, as well as the fact that efforts to resolve bad loans in some Eurozone countries are still underway, the ECB is likely to reduce monetary easing extremely cautiously.

(UK economy)

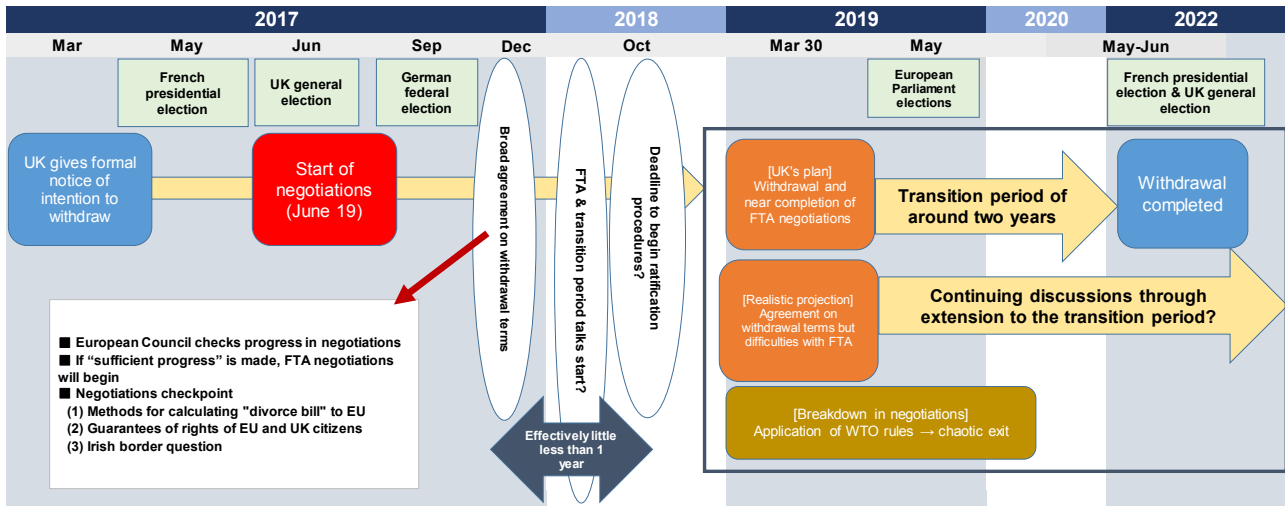
- The UK economy is weakening somewhat. The main causes are Brexit-related uncertainty making companies cautious about investment, and the fact that rising consumer price inflation caused by a weak pound has slowed personal consumption. The real GDP growth rate in the UK in 2018 is forecast to be in the mid-1-2% range. The biggest risk factor for both the EU and UK is the future direction of Brexit negotiations. If concerns about a "chaotic exit" grow, significant downward pressure on economic conditions is likely to arise.
- In November 2017, the BOE (Bank of England) raised interest rates for the first time in ten years (from 0.25% to 0.50%). The main reason was that the annual rate of consumer price inflation was around 3% per year, which is above the BOE target (2%). Considering a sense of vigilance toward Brexit negotiations, the BOE is expected to maintain its fiscal policy unchanged for a while.

(4) Chinese Economy – A Slight Slowdown, but Steady Growth to Be Maintained

- In 2017, the Chinese Economy performed strongly on the back of an increase in exports, and the real GDP growth rate is forecast to be 6.8%. The real GDP growth rate in 2018 is forecast to slow slightly. However, steady growth will be maintained at around 6.5%. The second term of the Xi administration is likely to prioritize the quality of economic growth, and manage the economy with a firm focus on controlling real estate bubbles and financial risks, and stronger environmental regulations. It is almost certain that China will achieve its target of doubling GDP and per capita national income in the decade from 2010 to 2020.
- By industry, service industries will continue to drive economic growth. In terms of demand, personal consumption is likely to be strong overall, supported by growth in incomes, despite slow growth in car sales along with the end of a tax break at the end of 2017. In particular, growth in online retail and service consumption is likely to continue. Regarding investments in fixed assets, infrastructure investments are expected to continue growing, but a slowdown is expected in investments in real estate development due to a slowdown in house sales. In view of the government's efforts of cutting excess production capacity and stronger environmental regulations, there is likely to be a weakening in capital investment in the manufacturing industry, particularly the steel industry. Strong exports are forecast to continue because of the recovery in the global economy and the weak yuan.

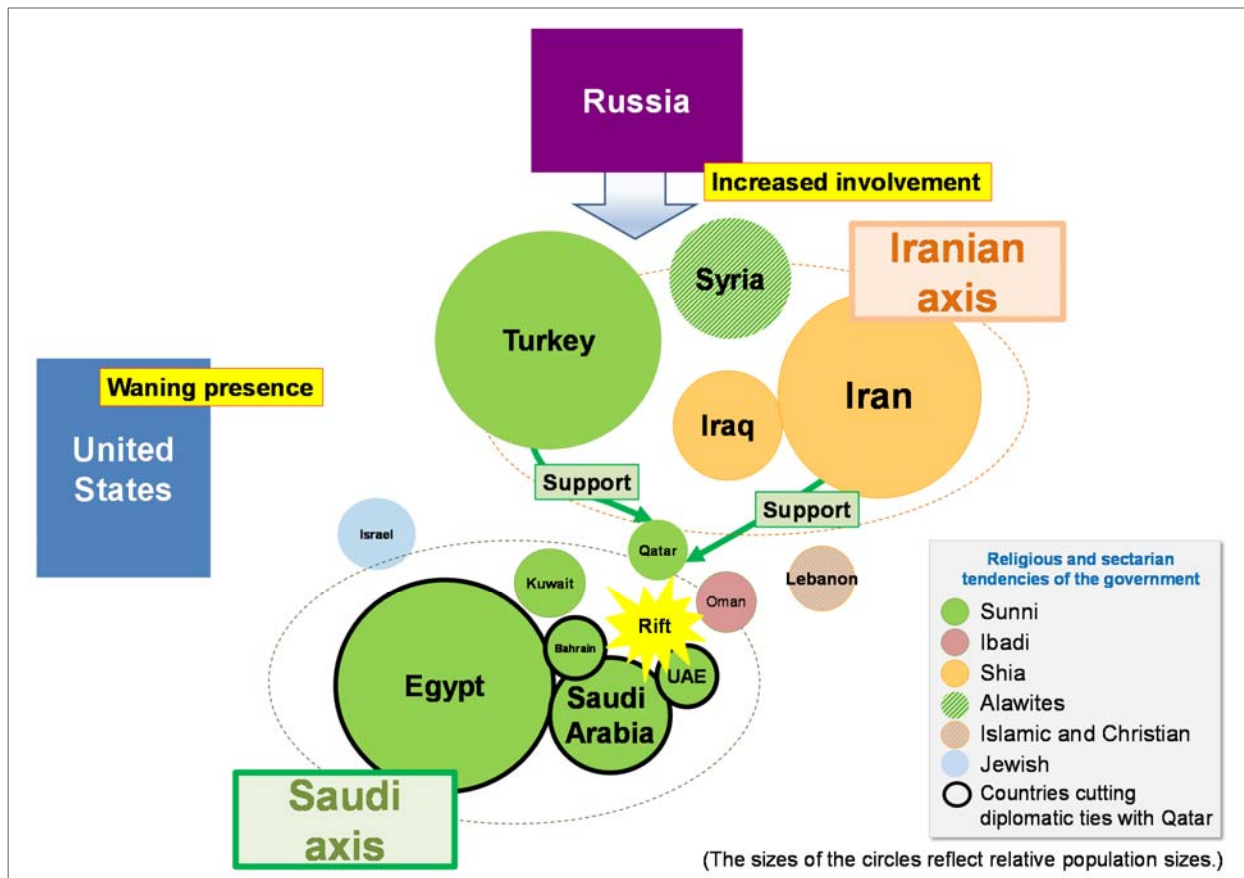
- In terms of fiscal policy, it is likely that China will maintain a slightly tighter stance in order to control the real estate bubble, prevent financial risk, and deal with interest rate hikes in the US. In November 2017, the yield on 10-year bonds reached 4% for the first time in thirty-seven months, and it is expected that market interest rates will continue to rise. Meanwhile, from 2018 onwards China plans to lower the reserve deposit rate by 0.5% - 1.5% for banks meeting certain criteria in lending to small to medium-sized companies, and it will promote a fiscal policy that ensures funds are made available in the real economy.
- The following risk factors can be cited: (1) a bigger than expected slowdown in housing sales or real estate development investments in response to measures to avoid a real estate bubble; and (2) large capital outflows from China, and a further weakening in the yuan. However, the Chinese government possesses the policy scope to prevent such risk factors emerging (for example, supporting the economy through infrastructure investments, or strengthening capital regulations), and there is unlikely to be any significant slowing of growth.

Figure 1: Schedule for Brexit Negotiations and Major EU Elections



Source: Prepared by MGSSI based on information obtained from various sources

Figure 2: Middle East geopolitics



Source: Prepared by MGSSI based on information obtained from various sources

Figure 3: Real GDP Growth Rate in Saudi Arabia (YoY)

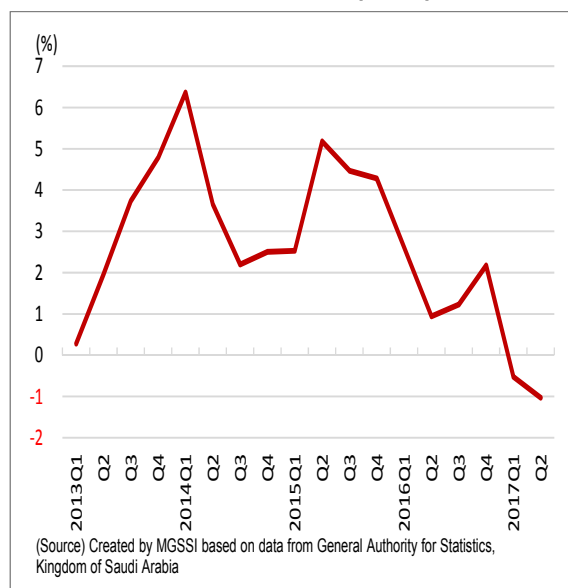


Figure 4: Schedule of Major Presidential Elections in Latin America in 2018

| Country | Leading candidates | Party | Schedule |
|------------------------|--------------------|-------------------------|---|
| Colombia | Vargas | PCR/right | Presidential election May 27, 2018 |
| | Fajardo | CC/ center | (Runoff) Jun. 17, 2018 |
| | Petro | MP/ left | Inauguration Aug. 7, 2018 |
| Mexico | López Obrador | MORENA/ left | Presidential election Jul. 1, 2018 |
| | Anaya | PAN/ center right | (Runoff) None |
| | Zavala | Indep./ center right | Inauguration Dec. 1, 2018 |
| | Meade | PRI/ center | |
| Brazil | Alckmin | PSDB/center right | Presidential election Oct. 7, 2018 |
| | Lula da Silva | PT/center left | (Runoff) Oct. 28, 2018 |
| | Bolsonaro | PSC/far right | Inauguration Jan. 1, 2019 |
| Venezuela | Maduro | PSUV/ left | Timing of presidential election undecided |
| | Falcón | AP/center left | |
| | Allup | AD/ center | |
| Cuba ^(Note) | Díaz-Canel | Communist Party of Cuba | Inauguration Feb, 2018 |

(Note) In the case of Cuba, the change in the President of the Council of State is expected due to Raúl Castro's stepping down.
(Source) Created by MGSSI based on various reports

Figure 5: IMF World Economic Outlook (October 2017)

| | 2013 | 2014 | 2015 | 2016 | 2017 (forecast) | 2018 (forecast) | YoY % |
|---------------------------------|------|------|------|------|-----------------|-----------------|------------|
| October 2017 | | | | | | | |
| World Bank (market rate) | 2.6 | 2.8 | 2.7 | 2.5 | (2.9)→ | 3.0 | (3.0)→ 3.1 |
| World (Purchasing Power Parity) | 3.5 | 3.6 | 3.4 | 3.2 | (3.5)→ | 3.6 | (3.6)→ 3.7 |
| Advanced economies | 1.3 | 2.1 | 2.2 | 1.7 | (2.0)→ | 2.2 | (1.9)→ 2.0 |
| United States | 1.7 | 2.6 | 2.9 | 1.5 | (2.1)→ | 2.2 | (2.1)→ 2.3 |
| Canada | 2.5 | 2.6 | 0.9 | 1.5 | (2.5)→ | 3.0 | (1.9)→ 2.1 |
| Japan | 2.0 | 0.3 | 1.1 | 1.0 | (1.3)→ | 1.5 | (0.6)→ 0.7 |
| Eurozone | -0.2 | 1.3 | 2.0 | 1.8 | (1.9)→ | 2.1 | (1.7)→ 1.9 |
| Germany | 0.6 | 1.9 | 1.5 | 1.9 | (1.8)→ | 2.1 | (1.6)→ 1.8 |
| France | 0.6 | 0.9 | 1.1 | 1.2 | (1.5)→ | 1.6 | (1.7)→ 1.8 |
| Italy | -1.7 | 0.1 | 0.8 | 0.9 | (1.3)→ | 1.5 | (1.0)→ 1.1 |
| Spain | -1.7 | 1.4 | 3.2 | 3.2 | (3.1)→ | 3.1 | (2.4)→ 2.5 |
| United Kingdom | 1.9 | 3.1 | 2.2 | 1.8 | (1.7)→ | 1.7 | (1.5)→ 1.5 |
| Other developed economies | 2.4 | 2.9 | 2.1 | 2.2 | (2.3)→ | 2.6 | (2.4)→ 2.5 |
| Australia | 2.1 | 2.8 | 2.4 | 2.5 | (2.3)→ | 2.3 | (2.7)→ 2.7 |
| Emerging market & developing | 5.1 | 4.7 | 4.3 | 4.3 | (4.6)→ | 4.6 | (4.8)→ 4.9 |
| Emerging and developing Asia | 6.9 | 6.8 | 6.8 | 6.4 | (6.5)→ | 6.5 | (6.5)→ 6.5 |
| China | 7.8 | 7.3 | 6.9 | 6.7 | (6.7)→ | 6.8 | (6.4)→ 6.5 |
| India | 6.4 | 7.5 | 8.0 | 7.1 | (7.2)→ | 6.7 | (7.7)→ 7.4 |
| ASEAN5 | 5.1 | 4.6 | 4.9 | 4.9 | (5.1)→ | 5.2 | (5.2)→ 5.2 |
| Latin America | 2.9 | 1.2 | 0.1 | -0.9 | (1.0)→ | 1.2 | (1.9)→ 1.9 |
| Brazil | 3.0 | 0.5 | -3.8 | -3.6 | (0.3)→ | 0.7 | (1.3)→ 1.5 |
| Mexico | 1.4 | 2.3 | 2.7 | 2.3 | (1.9)→ | 2.1 | (2.0)→ 1.9 |
| CIS | 2.5 | 1.1 | -2.2 | 0.4 | (1.7)→ | 2.1 | (2.1)→ 2.1 |
| Russia | 1.8 | 0.7 | -2.8 | -0.2 | (1.4)→ | 1.8 | (1.4)→ 1.6 |
| Emerging and developing Europe | 4.9 | 3.9 | 4.7 | 3.1 | (3.5)→ | 4.5 | (3.2)→ 3.5 |
| MENA | 2.7 | 2.8 | 2.7 | 5.0 | (2.6)→ | 2.6 | (3.3)→ 3.5 |
| Saudi Arabia | 2.7 | 3.7 | 4.1 | 1.7 | (0.1)→ | 0.1 | (1.1)→ 1.1 |
| Sub-Saharan | 5.3 | 5.1 | 3.4 | 1.4 | (2.7)→ | 2.6 | (3.5)→ 3.4 |
| Nigeria | 5.4 | 6.3 | 2.7 | -1.6 | (0.8)→ | 0.8 | (1.9)→ 1.9 |
| South Africa | 2.5 | 1.7 | 1.3 | 0.3 | (1.0)→ | 0.7 | (1.2)→ 1.1 |

Note: ASEAN 5 includes Indonesia, Malaysia, the Philippines, Thailand, and Vietnam. MENA includes Afghanistan and Pakistan. Figures in parentheses are the forecasts as of July 2017. Bloomberg data was used for Australia's growth rates for 2017 and 2018, including the forecasts as of July.

Sources: IMF "World Economic Outlook (October 2017)", "World Economic Outlook Update" (July 2017), Bloomberg