Round up - October 2012

As the autumn leaves fall so do old certainties. Notwithstanding the summers optimisms, on the face of it sensible economists now seem to agree that the situation in Greece could well get even worse unless there are some fundamental changes. The sovereign debt may have enjoyed a quiet rally, with the benchmark 10-year bond more than doubling in price since late-May on the hope of more time to tackle the debt, but the bottom line is that domestic austerity and structural reforms are not working - and are being recognized as increasingly socially and politically divisive.

Street protests will inevitably get worse and democracy itself is at stake – not just in Greece but across southern Europe. Alongside Greece the Portuguese government revealed it will miss the recently relaxed targets if it fails to step up to the plate and it has therefore announced major tax increases even as debate deepens and hardens on how to deal with deficit reduction. And France has announced its toughest budget in 30 years – including €20bn in new taxes, mainly on big business and the wealthy – in a potentially vain attempt to reach the targets it set itself for next year; faltering growth will inevitably derail such good intentions.

Can the political system transform itself in the Greek state, or will it collapse and usher in extremists, demagogues and anarchy as a prelude to the equivalent elsewhere?

The IMF's highly pessimistic view in its most recent World Economic Outlook - downgrading its forecasts for global growth next year - has provided further ammunition to critics of austerity. Their warning that the failure of US and Euro-zone policy makers to tackle their fiscal woes is threatening an already "slow and bumpy" global economic recovery merely confirms our assessment that Governments and policy makers have systematically underestimated the damage being done.

And, notwithstanding the IMF assessment, as the FT rightly highlighted recently, any growth forecasts are inextricably subject to the US Congress taking action to avoid the "fiscal cliff" – the automatic expiry of tax cuts and introduction of spending reductions next year – and to Euro zone governments following the European Central Bank's plan to buy sovereign debt by committing to economic reform and closer integration.

Such moves may or may not help in the short term, but the real and underlying problem is the language of intolerance and authoritarianism that can be heard when anyone dares to question Brussels orthodoxy. The spectre of high inflation, and along with it further asset bubbles, is building, QE is running out of steam, and the fragile armistice on the trade imbalances that sparked 'currency wars' may well be short-lived.

In the wider world the US seems to be transfixed in the run-up to presidential elections; a campaign where neither candidate has set out a coherent strategy that deals directly with threats in the Middle East. Optimism born of the July elections in Libya has been replaced by uncertainty and fear, much of it stoked by the militias that helped overthrow Gaddafi's Libyan; armed Islamists may have been driven underground but an armed uprising against any government that veers too closely to the West seems increasingly likely, alongside calls for Islamic law to be imposed.

Nigel Hall
nigel.hall@nhjstrategic.com Tel: +44 (0) 787 522 4383 www.nhjstrategic.com

And as sanctions bite hard in Iran, fears are rising that a cornered leadership has nothing to lose from blocking the world's most critical oil choke point in the Straits of Hormuz. The Institute for Science and International Security has declared that Tehran could make enough weapons grade uranium for a single bomb within four months, and whilst parts of Iran still feel prosperous, despite heart stopping rates of inflation, this can't last. Protesters blame President Ahmadinejad policies for the currency crisis that saw the Rial suffer a 30 per cent fall in a single week, and in the classic style of dictators his response is to blame external players; his next move might be more serious.

In the meantime Turkey has sent Damascus a powerful message by authorising military cross-border operations after the incoming shelling from Syria. The emerging conflict between Ankara and Damascus might be escalating as a result of the international system's failure to bring effective pressure to bear, but it could ignite conflict in a fragile region where the King of Jordan has dissolved parliament on the eve of a demonstration by the Muslim Brotherhood - promising to pick prime minister to reflect the wishes of a 'new body' – whatever that might mean! And the emerging tension over oil and gas in the seas south of Cyprus can only ramp up the pressures.

In brief – eye catching/watch list snippets:

- China and Japan are edging ever closer to some form of confrontation as the island disputes get more and more serious.
- The Argentine navy ship seized in asset fight – apparently a Ghanaian court has ordered an injunction and preservation order against the ARA Libertad after an application from US hedge fund Elliot Capital!
- Demographics and aspiration are beginning to hurt in China, with factory riots as the country is beginning to realize that it can no longer rely on an endless stream of rural migrant workers flooding into the new cities ready, willing and able to accept exhausting and monotonous work for no proper reward.
- After an in-depth study the IEA reckons that Iraq would account for 45 per cent of the anticipated growth in global- oil output to more than double by the end of the decade, and by the 2030s it could be the world's second-largest oil exporter after Saudi Arabia.
- In South Africa the ripple of industrial action within the mining communities, and the resulting state violence, is forcing external investors to rethink current and potential investment plans, only adding to the country's increasing political problems.

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Nigel Hall
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