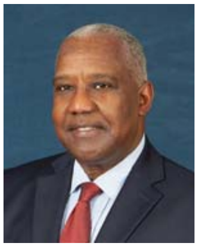
Major Country Developments
July 2017



By Byron Shoulton

Global Overview

Oil prices averaged $45 per barrel, continuing a bear market as oil traders lose faith in OPEC's ability to deliver on production cuts that were recently reaffirmed. Crude prices have dropped by more than 20% so far in 2017. Brent crude saw its worst first half performance since 1997. The sell-off in oil has accelerated since May when OPEC extended a deal with Russia and other producers to cut supplies by 1.8 million barrels per day. U.S. shale producers have increased their rate of drilling, stepping into the void and showing they can compete in a world of sub-$50 oil. Many traders believe the slide in oil prices will only be arrested when U.S. shale drillers are either forced to slow their expansion plans, or when OPEC's leading producer, Saudi Arabia agrees to even bigger supply cuts. The markets are clearly saying U.S. rig counts need to stop growing and start declining while telling OPEC that its producers need to cut some more.

The recent price slump came despite U.S. data from the Energy Information Administration (EIA) showing oil stocks in the world's biggest consumer market declining more than expected. Oil inventories have been mostly high during the three-year-old glut and traders want to see stockpiles decline faster before expecting prices to begin to stabilize. The fact that prices have not rallied following the EIA data may have presented an opportunity for bearish traders to try and push prices lower. Hedge funds amassed a record near-billion barrel position betting that OPEC could drive prices higher at the beginning of 2017, but have since reversed course.

OPEC members **Nigeria** and **Libya**, which are exempt from supply curbs due to violent disruptions affecting their oil industries, have both also successfully restored a large percentage of their output in recent weeks, undermining the supply deal. Meanwhile, Iran suggested that OPEC's members may consider further cuts but stressed no deal was close. Saudi Arabia urged patience but promised that together with Russia it will do whatever it takes to balance the world's oil market. Saudi Arabia and Russia together represent more than 20% of global oil production, but so far seem unprepared to cut supplies far enough, fearing that they could lose market share to rivals if they cut too deeply. Still, the news isn't all bad: lower oil prices give consumers more money to spend elsewhere while energy intensive industries also reap benefits.

In the **UK** the Bank of England (BoE) has put lenders on notice that they will have to build a special buffer worth sterling 11.2 billion over the next 18 months - as it tries to make banks more resilient to risks such as a burgeoning consumer-credit sector. The BoE forecast that it would raise banks' capital buffers to 1% by year-end as the central bank opined that the outlook for the UK's financial stability is moving toward normalcy. The central bank's Financial Policy Committee (FPC) reduced its warning level of risks to the financial system from elevated to standard but warned that there were 'pockets' of risk remaining that warrant vigilance.

The special buffer is a way of forcing banks to set aside capital in good times to draw down upon in bad times so as to keep lending to the wider economy at a steady level even during a downturn. The FPC has only deployed the tool once before, a year ago, but then had to quickly revoke it in the wake of the UK's Brexit vote. The Committee added that it would turn off the buffer if risks started to materialize and banks needed to release capital. The tools are not intended to dampen consumer credit, which in the last 12 months grew by 10.3%. While consumer credit is just one seventh of the size of mortgage lending, the BoE and UK regulators are concerned because write-offs within the sector are still ten times those in mortgage lending, where customers tend to keep up with repayments no matter what.

To tackle the risks from consumer credit, the BoE is bringing forward its analysis of how banks would cope with massive losses in the sector that normally would be a part of lenders' annual stress tests at the end of the year. Separately, the BoE has shifted toward monetary tightening. The bank's governor hinted that a rise in interest rates may become necessary later in the year if the economy keeps growing and in particular, if investments pick up.

Brazil's president Michel Temer was indicted for corruption for allegedly discussing bribes with the county's biggest meatpacker. If he is impeached this would be the second Brazilian president to be forced from office in a year. Brazil's latest round of uncertainty and legal wrangle will likely hinder the pace of reforms, weigh further on confidence, growth and weaken the outlook for economic recovery over the medium term.

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Tensions between the executive, legislature and an independent judiciary and public prosecutors' office, is a normal part of any democracy. But after three years of sweeping corruption investigations in Brazil known as "Car Wash", that have unearthed wrongdoing at the highest levels, the Temer stand-off with the judiciary shows how the battle is turning into a clash between the separate powers of the state. This is a conflict some praise as showing the strength of the institutions of Latin America's largest country but which others worry is getting out of hand and stopping the country from emerging from recession.

As the investigations advance, there is a rising uneasiness in Brazil relating to certain abuses or precipitous decisions taken by the public prosecutors or the lower courts. Beginning with state-controlled oil company Petrobras, Brazil's independent prosecutors and federal police have uncovered a series of schemes in which businesses provide kickbacks to politicians in return for favors, contracts, etc. The investigations have been popular and won praise even from business leaders as good for institutional-building. The crisis is complex but it is healthy for Brazil's long-term reputational risks. However, in recent weeks there have been signs of a pushback. First, Brazil's electoral court declined a request to cancel Mr. Temer's mandate on the alleged grounds that his 2014 campaign was funded by corruption money. Then one senator was freed and allowed to return to the senate, while charges against the former treasurer of the ruling Workers Party were overturned. In addition, Brazil's congress has been seeking to curb the powers of the judiciary, including through an 'abuse of power' bill to punish prosecutors and judges deemed to be acting 'excessively' and a bill to grant an amnesty to illegal campaign donors.

While the Car Wash investigators have suffered some setbacks, politicians know it would be political suicide to try and stop the process outright given the popularity of exposing high level corruption among ordinary Brazilians. The investigations have revealed the reality of what goes on between the wealthy and those with political power in Brazil. This exercise is very important in revealing transparency in order to address abuses; as well allowing for setting new guidelines that help to enable the long-term survival of a democratic system. Many analysts believe President Temer could yet survive the indictment given his strong support in the Congress, which under the constitution must give two-thirds approval for an impeachment trial to go forward.

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Argentina's treasury minister warned that the government will make no progress with economic reforms until after midterm elections which are due in October. The reason: a paralyzed congress has put the brakes on proposed changes. Political obstacles holding back the administration of President Macri was responsible for the refusal by the MSCI, the benchmark equity index, to allow Argentina to recover its status as an emerging market. This is despite a remarkable show of investor confidence in the country's recent 100-year bond issue. Instead, the index provider MSCI chose to continue ranking Argentina as a frontier market until after the elections, which could have a crucial bearing on the success of President Macri's reform agenda. With a minority in Congress, the ruling coalition will be unable to push through politically sensitive legislation before October – especially reforms to Argentina's rigid tax code that are fundamental to restoring competitiveness. The government faces a challenging task in trying to restore order to Argentina's chronically unbalanced fiscal accounts. There is frustration over demands to ease one of the highest tax burdens in the region while at the same time cutting the bloated fiscal deficit, which lies at the root of the country's economic woes.

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Argentina's business culture has grown dependent on generous subsidies over many years. With the loss of these privileges under the new administration, some businesses are reluctant to compete. Despite the reluctance of some Argentine businesses to adapt to the new environment, investment so far in 2017 is rising at its highest rate for the last five years. The government is confident that foreign direct investment- especially in Argentina's vast shale reserves and public private partnerships- will pick up from disappointing levels last year. Few expect the central bank to achieve its ambitious target of bringing inflation below 17% this year (compared to the current rate of 24%). Recent data show that GDP grew at 0.3% in the first quarter, while the government believes growth of close to 3% is possible for the full year. For now, its focus is on securing positive results in the October election. The government's aim to create an open economy and fix macroeconomic imbalances inherited from the previous administration will take time to accomplish. Until that's done it is hard to envision how Argentina achieves sustainable GDP growth.

USA

The IMF has lowered its forecast for the U.S. economy, saying that it can no longer assume the Trump administration will be able to soon deliver pledged tax cuts and higher infrastructure spending. The Fund questioned the Administration's plan to accelerate output and rev up U.S. GDP growth to a sustained 3% to 4% annual rate. Instead, the Fund forecasts the U.S. growth rate will steadily fall over the next five years to around 1.7%, assuming no major policy changes. A number of factors have sent the 10-year U.S. Treasury bond yields lower this year: skepticism over the Administration's capability to push through its fiscal agenda; questions toward how robustly the U.S. economy has been expanding; and slowing inflation readings over the past few months despite signs of the labor market approaching full employment.

Nonetheless, the U.S. economy experienced a 10.4% uptick in investments in capital equipment, new plants and other big-ticket items during the first half of 2017, the largest such increase recorded in five years. Most of that spending was by energy companies ramping up drilling for crude and natural gas from shale. Oil prices have retreated since then, with a barrel lately fetching $44.93 in New York trading. With energy prices showing no signs of upward momentum in the short term, the rebound in spending in the energy sector is unlikely to hold. Some argue that the likelihood of a sharp dip in oil prices to a level that chokes off U.S. drilling has increased. But even if that doesn't happen, capital spending is still likely to be lower over the 2nd half of 2017. A recent survey showed energy firms had become less optimistic than they were during the early months of the year, and that fewer firms were increasing their capital spending. Slower energy-sector spending may be why overall spending figures have been soft in recent weeks.

Technology is certainly reshaping product and labor markets, but U.S. productivity growth isn't picking up. An aging workforce is keeping a lid on labor-market expansion, a growth-sapping dynamic that may be exacerbated by more restrictive immigration policies going forward. High U.S. government debt prevents a spending-led stimulus. And a strong dollar- estimated to be 10%-20% overvalued- is weighing on U.S. competitiveness. Meanwhile, buoyant stock prices, one of the longest expansions on record and an improving jobs market (the economy is considered currently to be close to full employment) belie an economy facing considerable challenges. A recent larger-than-forecast decline in orders for durable goods by 1.1%, a broad gauge of U.S. business investment trends, is adding to questions about U.S. economic growth momentum. The economic data continues to disappoint and is making the bond market very skeptical of any more interest rate hikes in the near future. Higher interest rates from the Federal Reserve reduce money flowing into the broader economy.

Middle East

An arrangement that illustrates how diplomatic relations can change between countries, and how businesses find ways to survive those changes - were on display when Saudi Arabian exporters reportedly negotiated with Turkish logistics companies to transport cargoes of goods to Qatar. The latter is in the midst of spat with the governments of Saudi Arabia, Bahrain, the UAE and Egypt which have broken diplomatic and some commercial ties with Qatar, in protest over Doha's financing, adopting and sheltering of extremists. The regional stand-off with Qatar has provided Turkish companies with an unexpected bonanza. Qatar regards the measures taken by its neighbors as unjustified and denied interfering in the domestic affairs of other members of the six-member Gulf Cooperation Council. So far, the dispute is hurting Qatar's economy with little or no sign of an early resolution.

Meanwhile, Turkey's increasing reliance on business with Gulf Arab States, especially in light of Ankara's deteriorating relations with its European allies, is a major reason why Turkey's President Recep Erdogan is working to mediate the dispute that has destabilized regional energy, retail and air travel and cargo markets. So far, Turkish diplomacy hasn't adversely affected business on either side of the dispute, according to business groups.

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Turkish logistics companies have seen orders jump 110% since the political crisis erupted on June 5, 2017. Companies booking shipments are mainly Turkish entities selling to Qatari firms; and Saudi companies trying to honor contracts with Qatari companies but have found themselves blocked from sales or deliveries by the Saudi embargo on business with Qatar. Reports are that some 60 plus tons of Saudi products bound for delivery in Doha is being transshipped via Turkey. Some shipments have been delayed due to lack of capacity on boats and cargo planes. Cargo spaces have been full for all orders to Qatar during June. Participants anticipate space openings will begin to show up during July. Turkey confirmed that some 110 cargo planes have delivered goods to Qatar, where public service ads have popped up on social media explaining the Turkish words for basic goods like milk for the Arab –speaking Qataris.

Turkey also relies heavily on both Saudi Arabia and Qatar to achieve its foreign policy goals in the Middle East. Both nations fund Turkish-backed rebel forces in Syria, and both nations have expressed support for President Erdogan's purges of so-called Gulenists and other political dissidents (who Erdogan blames for the unsuccessful coup attempt against him a year ago).

In June President Erdogan spoke with Saudi, Emirati and Qatari rulers, and his cabinet ministers have engaged in several rounds of shuttle diplomacy aimed at easing tensions over the embargo against Qatar. Turkey has been so far the most outspoken ally on Qatar's behalf in the face-off with its neighbors. Late in June, Turkey sent some two dozen troops to Qatar as part of a military base agreement with Doha, which Turkey strengthened in the wake of the political crisis. Ties between both countries have been deep for several years, including in the business/commercial sphere. Despite this, Saudi partners to major Turkish businesses haven't stepped back from their projects or contracts in response to the current crisis.

Separately, Turkish Airlines launched its new direct summer flights from Saudi Arabia to multiple tourist destinations in Turkey. In 2016 some 530,000 Saudi tourists visited Turkey, making them a huge revenue stream for Turkish tourism and retail businesses.

India

The Indian government's plan to revolutionize its tax code may have to wait a while. Business groups and experts warned days before the new system was to go live, that a litany of problems with the proposed goods and services tax (GST), which should have been effective on July I, 2017, would create more problems, be ineffective and hence its implementation should be delayed.

The reform was one of those championed by Prime Minister Modi who has put it at the center of his economic reform agenda since coming to power in 2014. The measure was intended to boost India's output by as much as 2% a year, if handled well. However, apparent flaws in the new system have forced many to warn that if it is allowed to go forward without changes, it could do irreparable damage to Mr. Modi's reputation as a modernizer with a talent for delivery. Leading Indian industrial groups have called for the whole system to be put on ice until the problems can be sorted out. Groups are calling for a range of changes. They include dropping the requirement for companies to file information three times each month, cutting states out of the entire process and paying tax credits quickly. Also, plans for all companies in India to file their income tax returns digitally for the first time is causing big problems and is the source of immense stress across the system.

The new tax policy was supposed to bring benefits as it would allow goods to travel freely across state borders for the first time. However, ministers at both the state and national levels have been unable to agree on the exact terms. Another reason for caution is that the GST was being introduced eight months after Mr. Modi made a similarly radical economic change, unexpectedly scrapping 86% of India's currency in a move that dented the country's economic growth. Analysts have warned that a similar chaotic handling of the GST would be fatal for the prime minister's image as a pragmatic reformer with an ability to cut through the country's messy bureaucracy. One observation is that Mr. Modi ought to be conscious that economic reform under his tenure has, so far, been insufficient and halfhearted. In terms of detail-oriented planning, the Modi government's record appears less than successful at this point.

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Nevertheless, the authorities in India continue to exude confidence in the wake of the country's high rate of attracting foreign investments, relatively high business and consumer confidence and its rising trade volumes. US- India bilateral trade flows total $115 billion a year, and is poised for a multifold increase over the next few years. Indian companies are adding value to the manufacturing and services sector in the U.S., with total investments of approximately $15 billion and a presence in more than 35 states. American companies have likewise fueled their growth by investing more than $20 billion in India in the last few years.

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The ongoing attempt at transforming the Indian bureaucracy and modernizing the economy, presents many commercial and investment opportunities for U.S. and western business interests. The vision to convert India into a unified, continent-sized market of 1.3 billion people is far-sighted and difficult but not impossible. A planned building of 100 smart cities, the ongoing massive modernization of ports, airports and roads and rail networks, and the construction of affordable housing by 2022 – the 75th anniversary of India's independence – are seen as ambitious goals which will bring about great urban renewal within India while boosting economic activity and job creation at a pace not realized in the country's history. All of this will require enormous funding, take time and bump up against numerous challenges and road blocks.

India's rapidly expanding aviation needs, and its increasing demand for gas, nuclear, clean coal and renewables are also areas of future expansion and opportunities for trade and investment. In the coming years Indian companies are expected to import energy in excess of $40 billion from the U.S., and more than 200 U.S. made aircraft could join the private Indian aviation fleet. The U.S. and India are forging a deeper and stronger partnership that could pay dividends in the years ahead if managed skillfully.

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Non-Cancelable Limits Policy: Named Buyer Policy supporting an estimated $185,000,000 in sales of computer peripherals to buyers in the US.

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