

CROSSROADS

At the Intersection of Geopolitics and Geoeconomics

May 31, 2018 | Volume 1, Issue 5 | Andy Quirk



Here are some critical issues to watch around the globe over the coming month:

Highlights: European markets are shaken by political uncertainty in Italy and Spain, increasing fears over the future of the Eurozone and possibly the EU. The Turkish Central Bank simplifies its rates system in a move to spur investor confidence, however caution over the political environment in Turkey is still necessary. Trade tensions remain high between the US and China as the tit-for-tat trade war continues, while progress towards a US-North Korea peace summit continues, despite Trump's "cancellation" last week. The Brazilian trucker strike continues to escalate, affecting soybean exports.

Europe: markets shaken by political instability in Italy in Spain

After elections in March that resulted in no clear winner, Italy's Five Star Movement and the Lega Norde party attempted to form a populist Eurosceptic coalition government but abandoned these efforts after Italian President Sergio Mattarella vetoed their [choice for finance minister](#). As a result, the proposed prime minister, Giuseppe Conte withdrew his bid for the premiership. President Mattarella appointed former IMF official Carlo Cottarelli as interim prime minister instead. It is likely that Cottarelli will lose a parliamentary vote of confidence, resulting in new elections as early as September. Italy is the eurozone's third largest economy but has remained unstable since the Eurozone debt crisis in 2010-2011. European markets have responded negatively to the recent political instability. Investors should watch carefully as sell-offs in Italian bonds continue, affecting the cost of borrowing for the government and impacting the share price of Italian banks exposed to government debt and too many non-performing loans. Italy has the [second highest level of debt](#) of any Eurozone member. The Italian crisis could contribute to additional downward pressures for the Euro.

Political instability in Spain is also contributing to instability in European markets. Spanish Prime Minister Mariano Rajoy faces a vote of confidence on June 1st. The combination of Spanish and Italian instability represents a danger to the cohesiveness of the EU.

Elections in Iraq illustrate desire for less Iranian influence

Shia leader Muqtada al-Sadr and the Sairoon coalition – a coalition of several leftist Iraqi parties – have been confirmed as the winner of Iraq's recent parliamentary elections. Al-Sadr's coalition has been outspoken in its criticism of any foreign interference in Iraq. [Some observers interpret](#) Al-Sadr's platform as an effort to "exclude Iranian interests from policy considerations." However, other coalitions, such as the Fatah and the State of Law coalitions could limit Al-Sadr and the Sairoon coalition's effectiveness. Iran seems to have suffered a blow from this election. The Iraqi elections could indeed be an indicator that Iran is becoming more isolated regionally. This will likely result in continued geopolitical instability in the Middle East, particularly as tensions between Iran, Saudi Arabia and Israel continue to grow.

Turkish central bank simplifies rates

Turkey's central bank wants to portray independence from Erdogan. The currency plummeted to record lows last week due to concerns that the economy was overheating and that the central bank was unable to act independently to keep rates down. Erdogan has blamed the country's currency fluctuations on foreign investors. It will be worth watching whether the currency troubles have any impact on the elections set for the end of June. Turkey's economic fragility and political instability should be of concern to investors.

Asia: US-China trade tensions heat up, uncertainty regarding North Korea continues

On Tuesday May 29th, the White House announced that it would move forward with tariffs on \$50bn worth of goods from China. This decision adds to ongoing trade tensions between the world's leading economies, and comes just over a week after Treasury Secretary Steven Mnuchin declaring the administration was putting the trade war "on hold." The most recent tariffs are aimed at protecting US intellectual property. On June 30th, the administration is set to announce broader investment restrictions and export controls. The fact that the administration does not have a cohesive trade policy adds uncertainty into a market that seeks direction..

As for the proposed June 12th summit between the US and North Korea, it seems that it could be degraded to a hamburger summit (based on the CIA's report that N. Korea is rejecting denuclearization but is considering [opening a western hamburger joint](#)). On May 24th, [President Trump wrote](#) to Kim Jong-Un cancelling the summit. Stocks responded negatively. However, later the administration said that the summit is in the works. Again, the lack of consistency adds uncertainty into the market.

South America: Argentina attempts to reduce fiscal deficit to secure IMF credit line

Argentinian President Mauricio Macri is facing [pushback from the Argentinian Senate this week](#) over his attempts to raise prices on utilities in an effort to reduce the fiscal deficit. The Macri administration announced a plan to cut 20 billion pesos from this year's budget to reduce the fiscal deficit to 2.7 percent of GDP in order to secure a credit line from the IMF. The Argentinian peso has lost a quarter of its value over the last few weeks. Observers suggest that 2.7% is not far enough, noting that the IMF may ask Macri to reduce it to 2.5% in order to approve a credit line. If secured, an IMF credit line should reduce investors' fears about Argentina's deficits and debt.

Elsewhere in South America, Brazilian trucker strikes over fuel prices continue, with some protesters calling for military intervention as the

strike reaches its 10th day. The strike resulted in most port terminals [running out of soybeans](#) on Tuesday, hurting Brazilian farmers and impacting global supplies.

Africa: Ethiopia's talks over Renaissance Dam stall

Talks between Ethiopia, Egypt, and Sudan over the Grand Ethiopian Renaissance dam ended with the adoption of a new roadmap that could reduce the stalemate between the three countries involved and renew progress to completing the ambitious \$4.8bn project. However, progress still needs to be made toward resolving technical disputes between the parties. If completed, the dam would reach 500 feet, generating up to 6,450 megawatts of energy. Advocates for the dam argue that it will help spur economic development for a country where three-quarters of the population currently lack access to electricity. It could also provide cheaper electricity downstream to Sudan and would help regulate water levels prone to flooding. Egypt has consistently taken issue with the dam, citing fears over reduced water supplies from the Nile as well as a 1959 treaty with Sudan that divides the Nile's waters between Egypt and Sudan. If the project moves forward without an agreement on these issues, there is potential for a serious international dispute between Ethiopia and Egypt.

Important reads:

[The dangerous inadequacies of the world's crisis response mechanisms](#)

Adam Triggs

[How the west should judge a rising China](#)

Martin Wolf

[Italy gives complacent investors a lesson in political risk](#)

Kate Allen and Miles Johnson