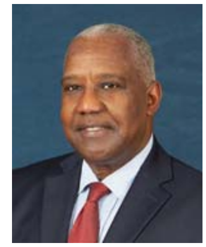
Major Country Developments
September 2017



By Byron Shoulton

Global Overview

Tensions mount over **North Korea's** advances in its nuclear defense program which has the world preoccupied. A series of tests including an intercontinental ballistic missile is a significant step in its weapons program. While the U.S., South Korea, Japan, China and Russia contemplate on how best to respond to the regime's threats and provocations, no clear solution has emerged. The U.S. won support from China and Russia for recent UN sanctions, including a ban on North Korean coal, lead and seafood exports intended to deprive the country of $1 billion a year, equivalent to a third of its annual revenues. Tightened economic sanctions against the regime and strong warnings that it should expect a forceful retaliation from the U.S. and others, have failed to deter North Korea from its increasingly aggressive actions. Tough talk notwithstanding, diplomacy may likely be the most viable option to ratchet down the crisis – even temporarily.

No one wants war with North Korea as the stakes are too high. Most experts believe taking military action against the country's nuclear and missile facilities would be too risky, as Pyongyang would almost certainly retaliate with massive conventional artillery and missile attacks against South Korea, U.S. military bases in Japan and possibly against Japanese cities. The causalities would likely be hundreds of thousands of people. Most troubling is North Korea's threat of a direct strike on U.S. territory. Whatever the response, given the now elevated nature of the threat, it is clear that the balance of forces has shifted. The U.S. and the world must now decide whether or not it can live with a nuclear-ready North Korea. And if so, how can it be contained.

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U.S. and Euro-zone economic recoveries are taking shape despite heightened political tensions and the rise of protectionist sentiments on both sides of the Atlantic. The withdrawal of monetary stimulus in Europe while inevitable [as most advanced economies and several emerging markets experience a resurgence in economic activity] may not be immediate given weak inflationary trends and a cautious attitude to avoid any action that could undercut the ongoing recovery.

U.S. employment in manufacturing and mining (which includes oil and gas drilling) is rebounding. In the mining sector the jump in hiring has had much to do with rising commodity prices. After plunging in late 2014 and throughout 2015, energy prices have somewhat recovered. That has helped to stabilize employment in the oil industry. Meanwhile, surging prices for metals like gold and copper are spurring activity in the mining sector.

U.S. manufacturers who export often find themselves at the mercy of the dollar exchange rate. When the dollar value surged in 2016, U.S. made goods became more expensive for foreign buyers. This year's decline of the dollar is a boom for manufacturers and major exporters who are dependent on overseas customers for a big portion of their sales. Still, there is plenty of catching up to do – both sectors are well below peak employment levels.

Globally, demand growth, improved job prospects, stepped up investments in infrastructure, new production and technological enhancements are forming the basis of a more upbeat global economic outlook for the remainder of 2017 and into 2018.

China is experiencing a pick-up in manufacturing activity as export growth improves and domestic demand remains strong. The momentum forced increased draw downs from China's huge stockpiles of raw materials resulting in a rebound in certain commodity prices (e.g. iron ore, copper, aluminum, et al). China's GDP growth is steady at 6.9% while both business and consumer confidence improve. The Chinese authorities appear to have succeeded in reducing real estate speculation by cutting back on excess credit availability for real estate investing, which many believe is a bubble. In the medium- term, risks from rising debt and overcapacity in certain sectors still looms. Nonetheless, the economy has become more stable as domestic output and foreign trade have provided an unexpected boost to confidence and to the short-term outlook.

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The failure of **Azerbaijan's** largest bank, International Bank of Azerbaijan (IBA), highlights the precarious state of the country's banking sector which will act as a further deterrent to an economic recovery. The economy is projected to remain on a low growth trajectory over the next year on the back of low global oil prices. Aftershocks from the oil price collapse of 2014-2015 are still being felt across the economy and the sluggish recovery of crude prices will continue to depress economic activity. Azerbaijan is among the most energy dependent economies in the world, relying on oil for around 95% of exports and 75% of public revenues.

IBA defaulted in May 2017 after suspending scheduled debt payments on foreign currency liabilities owed to international creditors. This comes after the government was forced to rescue the bank in 2015, increasing its ownership to 80% and creating a 'bad bank' Agrakredit to absorb IBA's bad loans, costing around $6 billion. IBA's failure comes as a massive blow to Azerbaijan's reputation among international investors, in particular because the state-owned rainy day fund SOFAZ has foreign currency reserves of $33.1 billion, or around 92% of GDP, sufficient to cover the bank's outstanding $3.3 billion liabilities. Despite a recent agreement to restructure IBA's debt, the consensus is that Azerbaijan's investment and credit reputation will be tarnished over the long term. This will worsen the country's sovereign risk profile and result in higher borrowing costs as well as weaken its access to foreign credit.

Africa has had a decade of economic and political engagement by China making that country a significant player and investor on the continent. China has surpassed the U.S. in terms of the volume of investments in Africa because its investors have excelled in the areas that took the lion's share of overall investment in the region: notably construction and real estate. Real estate took the top spot for capital investment in Africa in 2016, accounting for $36.5 billion (or 40%) of announced FDI in the region; construction was the top business activity by capital investment, also accounting for 40%.

Foreign investors are gradually diversifying their interests away from traditional energy and extractives sectors and are responding to growth opportunities sparked by Africa's rapidly growing and fast urbanizing populations. The continent's population totals 1.2 billion and is forecast to more than double to 2.45 billion by 2050. Population growth and urbanization are therefore key drivers in the development of real estate across Africa. Some investors argue that this is one of the most important reasons to be bullish on Africa's prospects over the medium term. The trend shows little sign of abating, and deep-pocketed Chinese developers are expected to continue stepping in to help build houses, infrastructure and amenities that Africa's booming cities will require going forward.

Kenya

Kenya's Supreme Court surprised the world in August when it delivered a ruling on the opposition's challenge to recent presidential election results. The court ruling nullified the results due to widespread discrepancies between electronic and paper tallies (among other questionable developments) which planted doubts. It ordered new elections to be held on October 17. Not even the defeated candidate Raila Odinga who filed the legal appeal expected the historical ruling. It was the first time an election had been legally declared void in Africa and it immediately elevated the chief justice, David Maraga who delivered the 4-2 ruling to hero status for millions of Kenyans who had lost faith in state institutions. The decision was a stinging blow for President Uhuru Kenyatta, who had been declared the victor of the August 8th poll. Not surprisingly, President Kenyatta disagrees completely with the court's ruling. He has promised to "fix" the judiciary if he is reelected. His deputy said the supreme court judges had "orchestrated and executed a civilian coup against the will of over 15 million Kenyans."

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Part of the reason for the shock was because the chief justice was himself considered an establishment figure, and the judiciary has long been seen to be under the thumb of the government. Mr. Maraga had refused to overturn Mr. Kenyatta's wafer-thin victory over Mr. Odinga at the previous election in 2013, despite evidence of irregularities. This time around, Mr. Kenyatta's lead over Mr. Odinga was 1.4 million votes, according to the electoral commission, making an upset even less likely.

Yet in the 4-2 ruling the chief justice and his fellow judges were highly critical of the electoral commission, saying it had failed, neglected or refused to conduct the presidential election in a manner consistent with the dictates of Kenya's constitution. The Kenyan supreme court has now set a precedent in Africa for the judiciary acting independently, as well as establishing their ability to act as a check on the abuse of power.

The election's annulment will usher in a tense period of renewed political campaigning in Kenya when the nation is deeply polarized. It will be incumbent on both candidates to be and preserve the peace. Mr. Kenyatta and his deputy, William Ruto, were both charged by the International Criminal Court after violence following the 2007 election left more than 1,200 people dead. Both cases collapsed because of a lack of evidence. The election violence cases were referred to the ICC because of concerns that they would not get a fair and proper hearing in Kenya.

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Since the advent of multi-party politics across Africa, opposition groups who believe they have been cheated at the ballot box are frequently called on to take their grievances off the streets and into the courts. Until now, such challenges have been uniformly thrown out, sometimes because they lack legitimacy, but in many instances because of the hold that the executive tends to have over the judiciary. It may be that with this ruling many regimes across Africa who exploit incumbency to perpetuate their rule through patronage, oppression and manipulation of the vote have been put on notice. That of course will depend on whether politicians will allow the judiciary to cement its newfound independence.

Uganda & Tanzania

Tanzania and Uganda have taken the first step in an agreement for the construction of a crude pipeline from Holma in Uganda to the Tanzanian port of Tanga. By providing a route to export markets, the pipeline is essential to the commercial viability of Uganda's 1.4 billion-1.7 billion barrels of recoverable oil reserves. Uganda's upstream oil developers, led by Total of France, got a fairly good deal after the government rerouted the pipeline from Kenya, (as was initially planned) to Tanzania. To secure the deal the Tanzanian government agreed to waive taxes, take shares in the pipeline project and charge a fairly competitive tariff of $12.2 per barrel. The developers are targeting completion of the pipeline by 2020.

Once construction gets underway, the economic impact of the $3.6 billion project- which includes the world's longest heated crude pipeline, a fiber-optic cable from Holma to Tanga, a high-voltage power line and a marine export terminal- will be substantial for both countries. Goods and services from the project will be largely imported from abroad, which will strain the already wide current account deficits of both Tanzania and Uganda, while significant investment can be expected. The financial impact to both countries of constructing the pipeline will depend on the shareholdings of a special-purpose vehicle (SPV) that will finance the project, and then own and operate it once it opens. This SPV will be a joint venture between the private developers and the governments of Tanzania and Uganda, but negotiations over the participation of ownership are yet to be concluded. There is the risk that these negotiations could cause delays if no agreement is reached, but with both governments and the private developers committed to the proposed timeline, substantial delays are likely to be avoided.

Qatar

On June 5th Saudi Arabia, the UAE, Bahrain and Egypt severed diplomatic ties with and closed most transport links to Qatar, but the tension reached new heights weeks later when Qatar refused a list of sweeping demands that included the closure of the Al Jazeera media network (which gave Islamist and militant groups a media platform to utilize). The demands also included halting logistical and financial backing for Islamist groups and ending defense ties with Iran. As the situation continues to evolve, the conflict will enter a new phase of tighter economic sanctions on the tiny Gulf state, with far-reaching ramifications for internal stability and business operations.

The longer Qatar remains subject to economic sanctions, the worse the implications will be for internal political stability, particularly if the welfare of Qatari citizens is affected by the crisis. The political rift with fellow Arab states will heighten geopolitical risks in the Middle East and undermine business and investment sentiment in the Gulf region, with Qatar bearing most of the brunt. Operational risks facing corporates in Qatar and in the Gulf region will rise in light of sanctions, which are expected to be tightened further.

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With mediation efforts making little progress, Qatar will now seek to build up the presence of foreign troops (especially Turkish) as a safeguard against perceived threats of foreign invasion or internal dissent by political rivals to the sitting emir and his father. The emir will also likely continue to send emissaries to foreign capitals in Europe and North America to rally international support for its cause.

These efforts will likely face counter measures by the four Arab states, which will rely mostly on economic embargoes to pressure Qatar into accepting their demands (albeit with little success). Furthermore, the possibility that Saudi Arabia and Bahrain would back their tribal allies in Qatar to undermine the rule of the current Qatari Sheikh Tamin, cannot be discounted. The position of the youthful Qatari emir will likely grow increasingly vulnerable, particularly if rivals within the monarchy start to mobilize against him. However, the tight control over the Qatari military by the royal family means that the removal of Sheikh Tamin will not be an easy task. In any case, threats to Sheikh Tamin's position will also be reinforced as the dispute drags on and if it inflicts serious economic pain on Qatari citizens.

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Historical tensions between Qatar and its neighbors have undoubtedly deepened the sense of mutual suspicion. With this in mind, the Qatari royal family views its foreign policy as a means of survival in a region marred with deep rivalries. This policy, devised under Sheikh Hamad bin Khalifa Al Thani, the father of the current emir, entails a complex web of (often conflicting) alliances, which policy makers in the emirate thought would fortify the country's strategic position in the region. For example, Qatar hosts thousands of U.S. troops while working simultaneously to strengthen defense ties with Iran; concurrently, it backs extremists rebels in Syria who are aligned against U.S. interests and the Assad regime- a proxy of Iran, with which Qatar has a defense cooperation pact.

However, these very conflicting alliances are now proving difficult to sustain, and Qatar is coming under mounting pressure from regional heavy-weights, who are particularly concerned about its growing defense ties with Iran and its links to Islamist and extremist groups. Nonetheless, Qatar is not expected to embark on any radical reform of its regional policies, and nor will the boycotting countries change their positions towards Islamists and Iran, as both are seen as destabilizing forces in the region. Given the deep level of mutual distrust, it appears that this conflict will likely continue on for an extended period of time, with potentially serious implications for political stability inside Qatar.

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Local Qatari manufacturers and retailers which rely heavily in imported intermediate goods are being advised to diversify their supplier base as a precautionary measure. The Qatari authorities could potentially impose a reciprocal embargo on goods originating from or passing through Saudi Arabia, the UAE, Bahrain and Egypt. There are also sector-specific risks. For example, those operating in the food retail sector could see their profit margins diminished if the government moves to control inflation through price controls.

The tourism sector (hotels and aviation) is heavily exposed to the crisis as half of the tourists to Qatar are typically residents of the other Gulf Cooperation Council states. The sector has taken a hit, with the country's flag-carrier Qatar Airways, having to fly longer routes, adding to its operational costs. It has had to find additional revenue streams to compensate for the loss of the UAE, Bahrain, Saudi Arabia and Egypt as markets. The airline has turned to leasing out a number of aircraft rather than leaving them idle, to mitigate losses. For hotels in Qatar, occupancy levels dropped for the months of June, July and August according to recent data.

Exports of liquefied natural gas, which accounts for about 60% of the country's revenues, are facing challenges as customers use the faceoff with Qatar's Arab neighbors as leverage to lower prices. Creditors should factor in the possibility of payment delays, particularly if the government comes under financial duress. It is clearly in Qatar's interest to take steps to end the impasse that is stifling growth.
Imports are down 36%, the sharpest decline in 13 years.

Little wonder therefore that business and investor confidence is wearing thin [evident by sluggish trading on the Qatar Exchange] and the prospect of foreign direct investments is waning. Banks are facing the possibility of capital flight and the cost of borrowing for lenders has risen as rating agencies changed their outlook on leading financial institutions in the country. The cost of imports, especially food items, has climbed, stoking fears of rising inflation. The construction sector is also finding it difficult to procure supplies to continue building projects, which casts doubt on Qatar's ability to finish on time all the stadiums and infrastructure projects it needs to successfully host the World Cup soccer tournament in 2022.

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FCIA's Deals Of the Month

Multibuyer Non-Cancelable Limits Policy:
Whole Turnover coverage supporting $450,000,000 of sales to the specialty metals sector, Global

Single Buyer Non-Cancelable Limit Policy:
$20,000,000 limit of liability supporting export sales of wholesale energy and midstream services, U.S.

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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.*