Growth STRATEGIES

Trend Analysis That Builds Business Decisions

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1 – SLOW GLOBAL GROWTH TO SEE ONLY MODERATE REBOUND IN 2014

(Conference Board)

- Growth of global Gross Domestic Product (GDP) will rebound moderately from 2.8% in 2013 to 3.1% in 2014, as the world's major economies still face many structural flaws and policy constraints that hinder more investment and faster productivity growth.
- Across mature economies, the 2014 growth outlook improves somewhat to 1.7% in 2014, compared to 1% in 2013. The Eurozone is expected to return to a positive growth rate of 0.8%, coming out of recession for most of the previous two years.
- The United States is the second largest contributor to the somewhat better outlook for 2014, where growth is expected to increase from a dismal 1.6% in 2013 to 2.3% in 2014.
- GDP growth in emerging and developing economies as a whole is projected to drop slightly by 0.1% point to 4.6% in 2014. China will continue to slow down from 7.5% in 2013 to 7% in 2014.
- Among the other emerging markets, India, Latin America and Asia are to witness a slight growth improvement in 2014, up from a weaker growth performance over 2013.
- In the medium-term, the outlook for the US and other mature economies remains slightly more positive than in previous years. The US will grow at 2.4% on average per year, and the Euro Zone at 1.3% from 2014-2019.
- The medium term slowdown in the growth trend of emerging and developing markets is more dramatic, from 4.3% on average per year from 2014-2019 to 3.2% from 2020-2025.
- Emerging markets constituted just below half of world GDP in 2012, up from about one third in 2000. In the next decade this shift will continue at a much slower speed.
- The upsides for the medium term are a faster increase in public and private investment and acceleration in policy reform.

2 – THE GLOBAL ECONOMY IN 2014 – 5 KEY TRENDS

Shane Brett (Global Perspectives)

1. US BECOMES THE ENGINE OF THE WORLD ECONOMY

The US is the only major Western economy that has cleaned up the toxic legacy of 2008 – unlike in Europe where zombie banks still shuffle on and meaningful reforms are mostly non-existent. In America bad debts have been written down, banks have been recapitalized, property markets have re-balanced and companies themselves are now far leaner.

Cheap, nearly limitless energy is substantially reshaping many parts of the US economy in a way we are still struggling to understand. It will also fundamentally alter the geo-political structure of the world, as the US moves permanently away from its addiction to Middle Eastern energy.

Gas in America is currently one quarter the price in Japan. Next year more US companies will move advanced manufacturing factories back on-shore from Asia, as the cost of energy collapses and years of 20% annual wage growth in China effectively prices these workers out of the market.

Most importantly for the US, the future global crisis of long term shortages in many key commodities such as food and water (which will become apparent later this decade) will pass America by. China on the other hand can't feed even 20% of its people.

Demography is destiny and America's population is young, mobile, entrepreneurial, highly educated and demographically stable. Most of Central and Eastern Europe's population structure is collapsing. Russia's is even worse and China is aging rapidly.

America may have its share of internal problems – a paralyzed political system, glaring inequality, too much government debt and un-payable pension promises (as we saw in Detroit in 2013). But once again – as many times over the last century – the USA will be the motor that powers the world economy in 2014.

2. TAPERING PAINS IN EMERGING MARKETS

Across the world, as the Federal Reserve tapers its bond purchases, emerging markets will have to cope with a wall of money being vacuumed out of their economies and moving back into US dollars. This will cause widespread currency volatility across the continent and may lead to a series of local economic crises.

3. EUROPE GETS STRESSED

Europe will begin 2014 with its economy slowly starting to recover from the recession of the last few years – but make no mistake, the Euro Zone crisis is percolating away in the background and threatening to erupt at the slightest provocation.

4. THE COMMODITY CYCLE TURNS UPWARD

As economies improve the demand for the world's minerals, metals and commodities will start to increase. Institutions know this and are taking positions at the start of this new trend. Many miners and commodity companies have been absolutely hammered over the last few years. 2014 will be the year this starts to change.

5. AFRICA RISING

Although the north of the continent will remain a fragile mess due to the fallout and instability from the Arab Spring, Sub-Saharan Africa is expected to be the fastest growing region in the World in 2014 (at 5.5% – a rate twice as high as the United States).

Infrastructure is starting to improve across the continent as new railways and ports are being built and opened for the first time since independence. South Africa, despite its own economic difficulties, has cemented its role as the continent's leading economic power, setting up retail and telecommunications industries all across the continent.

A small African middle class is starting to appear across the continent and this process will continue to escalate in 2014.

3 – TEN TRENDS THAT WILL SHAPE ASIA IN 2014

Evan A. Feigenbaum (Carnegie Endowment for International Peace)

1. ASIA DRIVES DEMAND

First, the good news: Asia's relationship to the world economy is changing in dramatic, and positive, ways. For decades, G7 countries beat a path to *Asia's* door – buying Asian exports and investing heavily in Asian economies. But Asia has become a major factor in the advanced economies' *own* growth stories. And where others have long consumed goods *from* Asia, it is Asians who are now investing and consuming more from overseas.

This trend will continue and grow in 2014, as Asia consolidates its role as a demand driver for the world economy.

2. SECURITY FRAGMENTATION THREATENS ECONOMIC INTEGRATION

But here's the bad news: Asia is becoming more prosperous and economically integrated, yet the central strategic challenge in Asia today is the collision between economics and security.

Over half of Asia's trade is now being conducted within the region, powering a $20-trillion-plus regional economy. But the same countries that are trading, investing, and growing together are beset by security tensions and dysfunctional diplomatic relationships. Asia's major powers are mistrustful and prone to nationalism. Their strains are increasing over the sovereignty of tiny rocks and shoals in the East and South China Seas.

3. THE CONTESTED COMMONS

These tensions are likely to play out not just in disputes over territory but in the global commons as well. Beijing's November declaration of an air defense identification zone (ADIZ) in the East China Sea raised hackles and will likely be followed in 2014 by similar declarations around China's maritime periphery. Yet the debates over China's actions raise broader questions about how competing sovereignty claims in Asia may touch public goods and the global commons – airspace, cyberspace, and the high seas.

4. JAPAN'S PIVOT TO ASIA

With a competitive eye on China, expect Tokyo to further reinvigorate its Asian diplomacy in 2014. Just one year into his tenure, Prime Minister Shinzo Abe has traveled Asia relentlessly, courted India, and pledged $20 billion in new aid and loans to Southeast Asia.

5. NORTH KOREA'S GREAT UNRAVELING?

The December execution of Jang Song-thaek, the uncle of North Korean leader Kim Jong-un, and the ongoing purge of his patronage network have highlighted internal divisions and raised underlying questions about the stability of the regime. The risk of instability will grow in 2014.

6. THE FUTURE OF THE US REBALANCE

In recent years, the US role as Asia's principal security provider has been reinforced, but as its economic weight shrinks in *relative* terms, it is unclear whether the US role is sustainable.

7. A CONVERGENCE OF MODELS?

A raft of regional preferential trade agreements now compete for attention in Asia. These include, but are not limited to, the US-backed Trans-Pacific Partnership (TPP) and the pan-Asian Regional Comprehensive Economic Partnership (RCEP), which does not include the United States.

8. CHINA'S ECONOMY: TO MARKET?

China's reform efforts have become more vigorous because its growth model, which has depended on the twin pillars of investment in fixed assets and exports, has begun to run out of steam.

To that end, Beijing ends 2013 having adopted a sweeping economic reform agenda that includes new commitments to financial liberalization, the repair of China's social safety net, protections for rural property rights, and greater reliance on market forces. Beijing has committed to increase the role of the market in the economy – for example, by boosting the *formal* role of private capital.

9. THE PUSH AND PULL OVER REFORMS

Washington and Beijing won't be the only capitals to face intensified scrutiny of their economic policies in 2014. Antsy global investors and angry domestic voters will push and pull a number of Asian governments, including India, Japan, Thailand and Malaysia, in competing directions.

10. CENTRAL ASIA IN FLUX

New economic and strategic pressures will also emerge in continental Asia in 2014. Landlocked Central Asian economies will be tested amid the US withdrawal from Afghanistan, new Chinese investment and infrastructure initiatives, Russia's efforts to extend its preferential customs union, and Iran's uncertain trajectory.

4 – 2014 CRUCIAL FOR EMERGING MARKETS, MAY SET TREND FOR DECADE

Mark Mobius (Franklin Templeton Investments)

We believe 2014 could be an important year for many emerging markets, establishing trends that may play out through much of the remaining part of the decade. In particular, Chinese government initiatives announced in late 2013 could have far-reaching significance. Some 60 proposals across a gamut of issues could have dramatic consequences in areas including health care and social security, justice and the rule of law, intellectual and physical property rights, banking and monetary policy, and environmental protection.

The proposed changes, intended to facilitate sustainable economic growth in China, could also create substantial opportunities for investors. Reforms to state-owned enterprises, aimed at improving their professionalism and efficiency in resource usage, could benefit their listed subsidiaries. Measures aimed at encouraging enterprise and innovation, as well as blocking unfair competition, could speed up the process of rebalancing the economy away from investment-led growth and toward a more entrepreneurial, consumer-focused and service-oriented model. The project has a decade-long timescale, but we nevertheless expect to see some progress in 2014, perhaps through initiatives in free trade zones such as the one announced for Shanghai in late 2013 and others hinted at in the proposals. Of course, there are likely to be casualties as a result of these reforms. Companies facing intense competition and now deprived of the level of government support obtained in the past could be negatively impacted. We, therefore, need to keep our eyes open to avoid such situations.

A number of major emerging markets will see major elections in 2014 – Indonesia, South Africa, Thailand and India in the first six months of the year, and Turkey, Brazil and Nigeria later on. As the electoral cycle peaks, we believe administrations may feel more able to address barriers to long-term growth and retreat from populist measures. In these circumstances, ongoing strengths, in terms of solid economic growth potential, strong public and consumer finances, rich natural resources, and favorable demographic trends that have helped emerging markets over the past several years, could gain new traction.

We believe many emerging markets, in addition to China, possess considerable economic growth potential. For example, Southeast Asia has been seeing a notable extension of growth and wealth away from traditional economic hubs, with previously underdeveloped regions starting to see significant catch-up growth. Thailand is most notable in this regard.