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Insight Perspectives

Economic and political update

European Cohesion at Risk

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Insight Perspectives

Economic and political update

The Insightperspectives newsletter is produced by Insightview.eu Ltd (Private Limited Company), Denmark, and is published on a monthly basis.

The editor-in-chief is Carsten B. Pedersen. If you are interested in subscribing to the newsletter, send your contact details to info@insightview.eu

The Insightperspectives newsletter provides a summary of what happened in the month under review, plus articles about "special issues" in the global economy.

The newsletter attaches importance to identifying and analyzing current and future trends in the global economy, financial market and politics.

All articles will be linked to external sources and Insightview.eu, which includes more charts, maps, data and elaborating comments.

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"This is actually a very good newsletter if you want to get quickly informed about major economic issues all over the world"

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"Insightperspectives is a valuable supplement to the daily stream of information, received from banks and the various other providers of news and market analysis. It puts the issues discussed into context and provides a view on the long term implications, which can easily get lost in the daily flow of information"

Ole Damgaard-Nielsen, Managing Director, **Inter IKEA** Treasury

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"Insightperspectives provides an easily understandable summary of the financially most important events, news and developments around the world."

Jesper Alsing, CEO, Value **Invest Asset Management S.A**.

"Insightperspectives brings an independent viewpoint on important economic, political and financial events. Thoughtful insights - I read regularly"

Peter Bundgaard, CEO, PM and founding partner of **BLS Capital Management**

The editor of Insightperspectives is simply the best macroeconomist I have ever experienced. For more than a decade I have been a reader of his thoughtful analysis that comes with an edge. This is the only macroeconomic analysis you will need to be able to follow global trends that can make a difference in your own day-to-day decision-making, whether in business or investments.

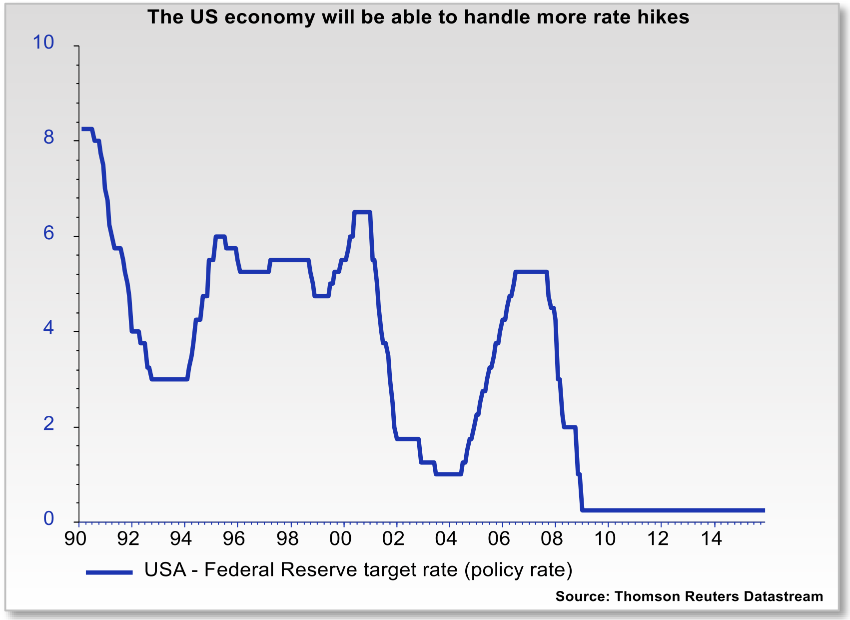
Global economic and political update

In Europe, there are no signs that the refugee crisis will end anytime soon. Instead, the refugee crisis was given a new dimension after it became known that one of the Islamic State perpetrators behind the terror attacks in Paris on November 13 may have come to Europe from Syria hidden among a group of refugees. This will make even more Europeans question what they see as Chancellor Merkel's "naïve willkommen policy" – read also the TheLocal article, PM: Sweden has been 'naive' about terror threat.

Whether this may spell trouble for the Chancellor in Berlin remains to be seen; but Insightperspectives believes there is a risk that Mrs. Merkel's autocratic approach will propel support to political parties on the far right and left in other EU countries; these parties will have a more nationalist agenda and adverse sentiments towards globalisation and the European Union. This has become the case not least after Mrs. Merkel took decisions impacting all European countries without consulting the other EU member states. Now that Mrs. Merkel has lost control of the influx of refugees, Berlin wants other countries to help bear the brunt of a "burden", which they believe Mrs. Merkel created – to see more on this issue, read the article, The Paris terror attacks and refugee crisis risk leading Europe in the wrong direction, on page 22.

Berlin's many U-turns are felt everywhere. Suddenly, Turkey's EU application is back on fast-track, at least according to Mrs. Merkel. Even President Putin is no longer an outcast. In fact, the Russian President is suddenly seen to be the key person when it comes to solving Syria's civil war and the refugee crisis – read the Russia section on page 10. These political U-turns are surely not boosting the credibility of Germany in the other European countries.

In this context, Moscow is excused for seeing Berlin and other western capitals as being somewhat hypocritical, having received only lukewarm western sympathy following the news that a Russian passenger plane was brought down by Islamic State terrorists on October 31 – read the Die Welt article, Putin vermeidet die Wahrheit zum Absturz im Sinai. The editor of Insightperspectives often sees the same interpretation in China – read the China Daily, Double standard on terrorism is symptomatic of West's view.



The news out of China is not any better. This was evident according to economic data published in November – see the China section on page 5. The same picture was also reflected by anecdotal evidence from the mainland obtained by the editor of Insightperspectives, who visited the country in early November. On the other hand, there were once again visible signs that China is moving up the value ladder, at least in some sectors of the economy – read more in the article, Travel Notes from China: No turnaround yet in sight; Internet Plus makes significant changes to the economy, on page 14.

In the global economy, it is not all bad news. The US economy remains on a solid path of growth. In fact, economic data in November were so strong that the Federal Reserve is yet again talking about raising policy rates in December. Such a decision is long overdue. This time, however, the US central bank needs to act rather than talk. In case the US central bank finally decides to raise policy rates, this will probably have a larger impact abroad than in the United States. More than five years of ultra-loose monetary policy has brought many economies and financial markets out-of-whack and highly liquidity-driven – read more in the USA section on page 4.

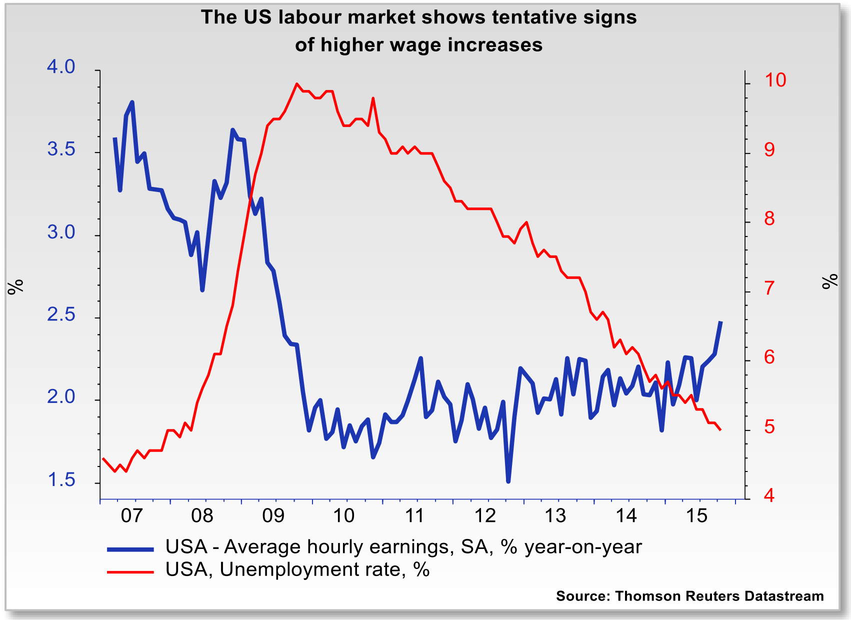
In general, the global economy is headed towards uncertainty in 2016 after policymakers have “front-loaded future growth” since 2008 by pursuing an ultra-loose monetary policy. The economic consequences are admittedly difficult to quantify; but households, private companies and other economic players are aware that this is of course not sustainable, which may negatively impact their future spending plans. In Europe, uncertainty is now reinforced by an increasing number of terror attacks in 2015, which may even hit corporate spending, according to Siemens' CEO, Mr. Joe Kaeser – read more in the Euro-zone section on page 7.

USA - Strong economy reinvigorates expectations of December rate hike

The US economy remains in excellent shape, although negative news from the manufacturing sector makes the biggest headlines in the media. In October, the leading manufacturing ISM index fell again. On the other hand, in the same month the ISM service index bounced back sharply close to an all-time high. This is far more important as the service sector accounts for approximately 80% of the economy while the manufacturing sector's share of GDP is less than 15%.

In the United States, households have no reasons to be downbeat as they are exposed to a benign price environment, a strong labour market and moderately increasing wages, which continues to boost real income going into 2016. This is also reflected in the best leading consumer surveys. In November, the University of Michigan consumer sentiment headline index jumped to 93.1 from 90.0 in October.

The positive outlook for households is expected to continue in the coming months. This is the case even though the Federal Reserve probably will raise policy rates in December. This comes after a labour market report showed strong employment growth and wage increases in October. This is in many ways a Goldilocks scenario for US households, which is highly important in an economy, where private consumption accounts for nearly 70% of GDP.

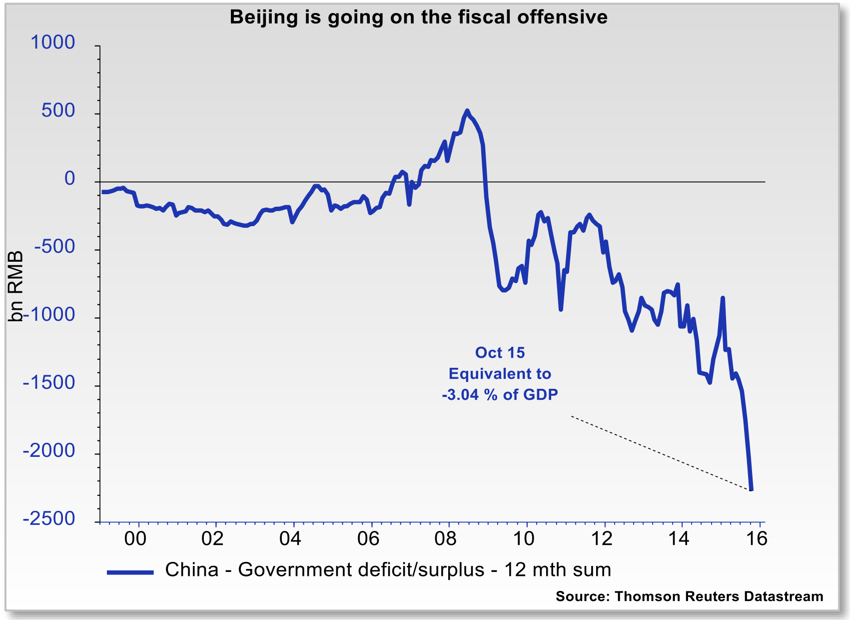


Conversely, there are no profound signs yet that manufacturing activity will bounce back. The manufacturing sector is exposed to increasing inventories as demand has slowed markedly, not least due to declining foreign demand and weak investment activity in the energy sector. In November, a report showed that the business-inventories-to-sales-ratio continued to increase to the highest level since 2009. On the other hand, the best leading regional surveys are no longer showing signs of further deterioration, at least this was the conclusion in the regional manufacturing survey from the Philadelphia Federal Reserve.

China - Fiscal deficit on the rise as Beijing faces policy dilemma

In China, the central bank tries to boost liquidity to help the economy. In October, money supply, M1, jumped by 14% year-on-year compared to 11.4% in the previous month. On the other hand, it is hard to see any signs that the manufacturing sector is using these monetary easing measures to boost borrowing, at least not according to the latest lending statistics.

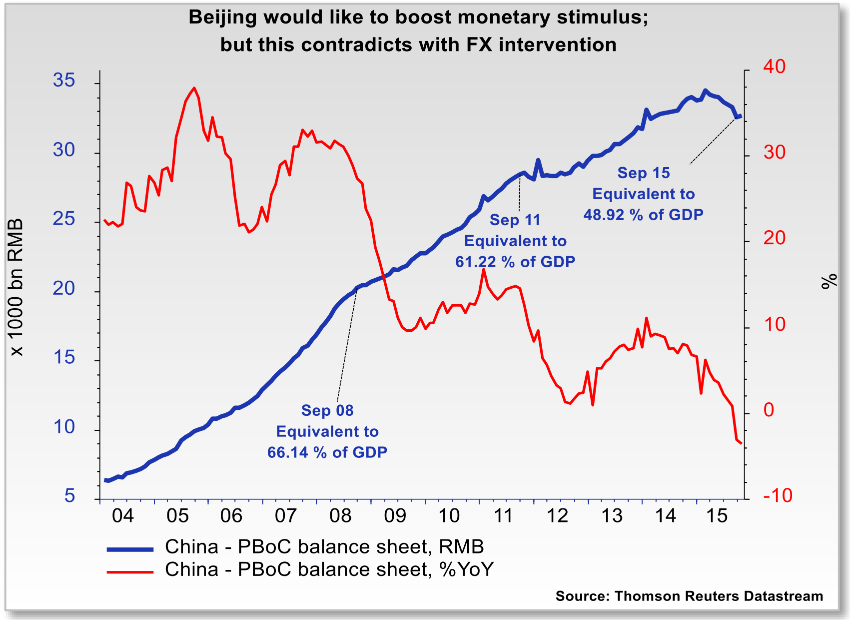
There are many reasons for this. First of all, manufacturing activity remains weak. In October, industrial production rose only 5.6% year-on-year compared to 5.7% in September. Furthermore, many state-owned banks are reluctant to lend to companies in an environment of deteriorating asset quality - read also the South China Morning article, Decline in loans at Chinas big four banks shows asset-quality concerns. In addition, the anti-corruption campaign has made many state-owned-enterprises more cautious as they try to avoid making "mistakes".



There is no doubt that Beijing is worried that growth is slowing too rapidly. At present, Beijing prefers to avoid further devaluation of the yuan. This was also why, in early November, Prime Minister Li Keqiang promised the full use of all fiscal weapons. There are signs that fiscal easing measures are gaining momentum. In October, China's fiscal expenditure jumped 36.1% year-on-year, which was the highest rate of increase since

2012. At the same time, fiscal revenue only rose 8.7%. As a consequence, the government deficit rocketed to a new high of slightly more than 3% of GDP.

Sooner or later, however, Beijing will need to devalue the yuan even more, which would be the case not least if the European Central Bank boosts monetary expansion. It is correct that China needs a “somewhat” overvalued currency to animate companies to move up the value ladder; but the country cannot afford an excessively overvalued currency.

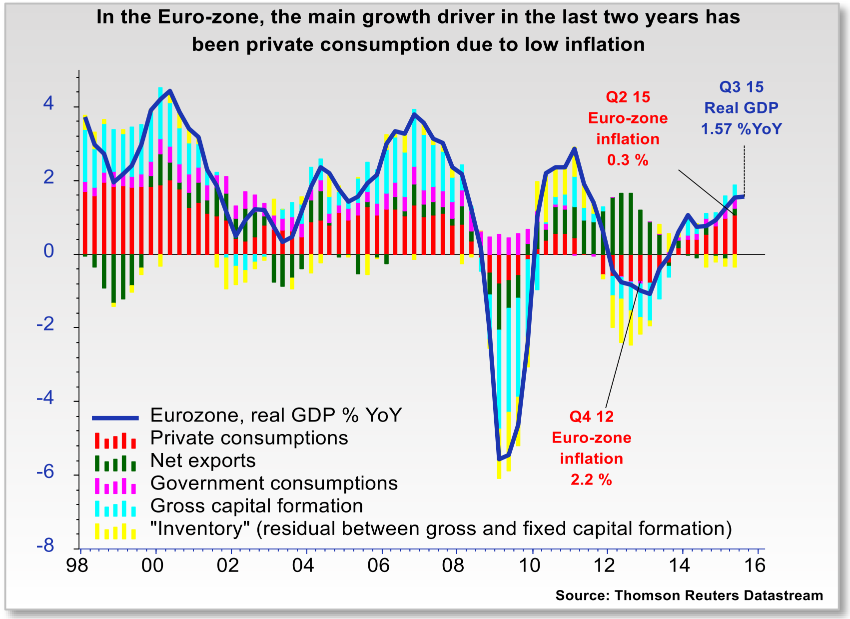


Beijing, however, is in a dilemma. It is a difficult task to boost the PBoC's balance sheet at the same time as the central bank intervenes in the foreign exchange market. Lately, the Chinese central bank's balance sheet has even declined. This is of course not sustainable. Therefore, Beijing needs to allow the market to play a bigger role in setting the price of the yuan.

Ultimately, this is also the game plan of Beijing, although the process of easing capital control will be slow, so as to not endanger price stability in the property market. In the last few years, Beijing has been able to keep property prices relatively firm, at least in tier-1 cities, due to the fact that China is still a relatively closed economic system. This was also reflected in the latest home price report from the National Bureau of Statistics covering the 70 biggest cities. In October, the home price index was up 0.3% year-on-year after declining 0.7% in September. Yet again, this was predominantly due to higher prices in tier-1 cities.

Euro-zone - Paris terror attack and refugee crisis boost economic uncertainty

In the third quarter of 2015, the Euro-zone economy expanded by 0.3% quarter-on-quarter, which was 1.6% stronger compared to the same quarter in 2014. Once again, the Spanish economy was the strongest performer growing by 0.8% quarter-on-quarter, while the French and German economy both expanded by 0.3%.



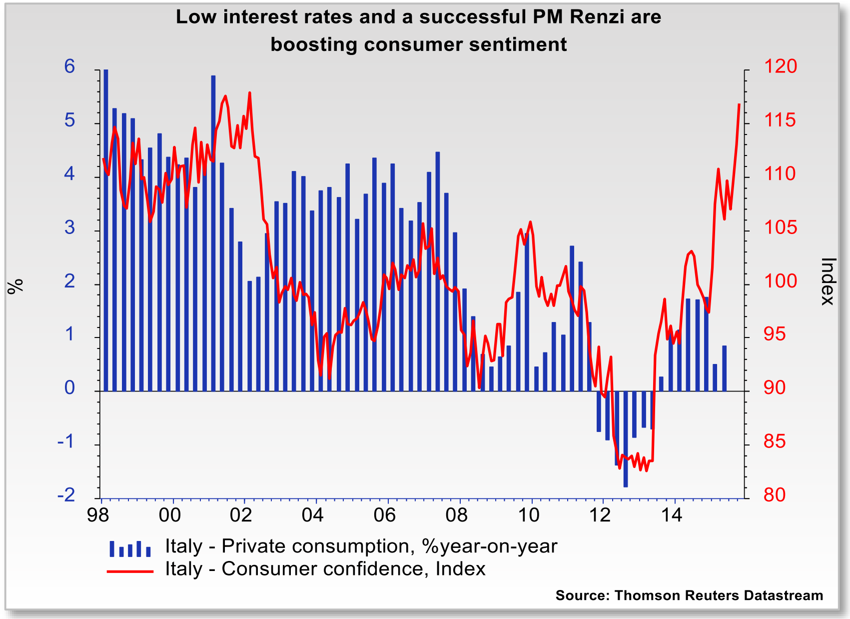
The growth outlook for the Euro-zone economy remains positive, at least in the short run, as the economy is still exposed to cyclical tailwind from low inflation, ultra-loose monetary policy and a weaker euro (click here to see Insightperspectives' updated global economic growth forecast). On the other hand, the refugee crisis may change the political landscape rather significantly. This is the case not least in Germany, where the costs of a huge influx of refugees continue to increase, which may ultimately force Berlin to raise taxes - read the Euractiv article, German economic research institute doubles cost estimate for refugee crisis.

The current situation is admittedly complicating the Euro-zone growth outlook. The fact that elected policymakers do not have a convincing refugee policy combined with the latest terror attacks could ultimately outweigh the positive impact of the influx of refugees, which will boost public sector spending, at least theoretically.

This disarray has created leeway for more political radicalisation, which will neither promote more integration in Europe nor a free market economy. On the "positive side", uncertainty may animate the European Central Bank to boost monetary easing at a faster pace. To see more about the implications of the terror attacks and the refugee crisis, read the article, The Paris terror attacks and refugee crisis risk leading Europe in the wrong direction, on page 23.

Italy - PM Renzi creates political foundation for economic reforms; consumer confidence jumps

In Italy, the reform process has been slow until recently; but it seems as if Prime Minister Renzi is finally gaining a few important political victories. In October, Mr. Renzi succeeded in curtailing the power of the Senate (Italy has a two-chamber parliament), which could make way for more comprehensive economic reforms in the future.

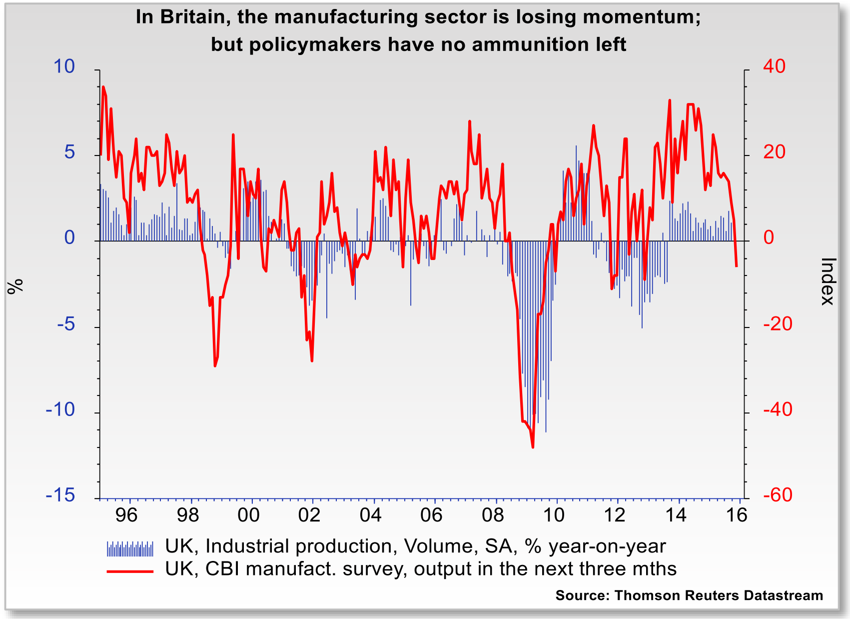


Italy's competitive position has improved by 11 places to number 45 in the World Bank "Doing Business 2016" ranking; the same extent of improvement was seen in the previous year. Furthermore, Italy is finally seeing a decline in unit labour costs due to the fact that companies fulfil increasing orders with the existing staff rather than employing more people. This was long overdue as Italian wages have not declined since the global crisis erupted which has been in sharp contrast to the Euro-zone's "real reformers" (Ireland, Portugal and Spain).

In the coming quarters, the Italian economy will benefit from significant cyclical tailwind created by low interest rates, very benign inflation and the double-edged impact of a weaker euro. The latter will support the export sector (predominantly due to higher revenues in euro terms). Furthermore, falling commodity prices should disguise the negative impact from a weaker euro on households' real purchasing power, at least in the near future. Lately, these factors have propelled Italian consumer confidence to the highest level since 2002. The Italian economy will probably see more support in the coming months as the European Central Bank considers raising monetary stimulus from "Italian" to " Japanese".

Britain – Growth has peaked and policymakers are left with no ammo

In Britain, growth has probably peaked after the economy rose 0.5% quarter-on-quarter in the third quarter – click here to see Insightperspectives “real-time economic cycle”. This was up 2.3% compared to the same quarter in 2014. Since 2010, Britain has only experienced a low-quality recovery, which has been consumer-led. This has been based on only moderate fiscal tightening and ultra-loose monetary policy, which has front-loaded "future growth" rather than improved the foundation for stronger long-term growth.



On the positive side, Britain's official unemployment rate fell in October to 5.3%, which was the lowest level since April 2008. The low unemployment rate will, admittedly, not make the Bank of England raise policy rates as the governor of the central bank, Mr. Mark Carney, still appears to have plenty of excuses to keep monetary policy unchanged - read the Reuters article, BoE's Carney: UK rate rise not a certainty.

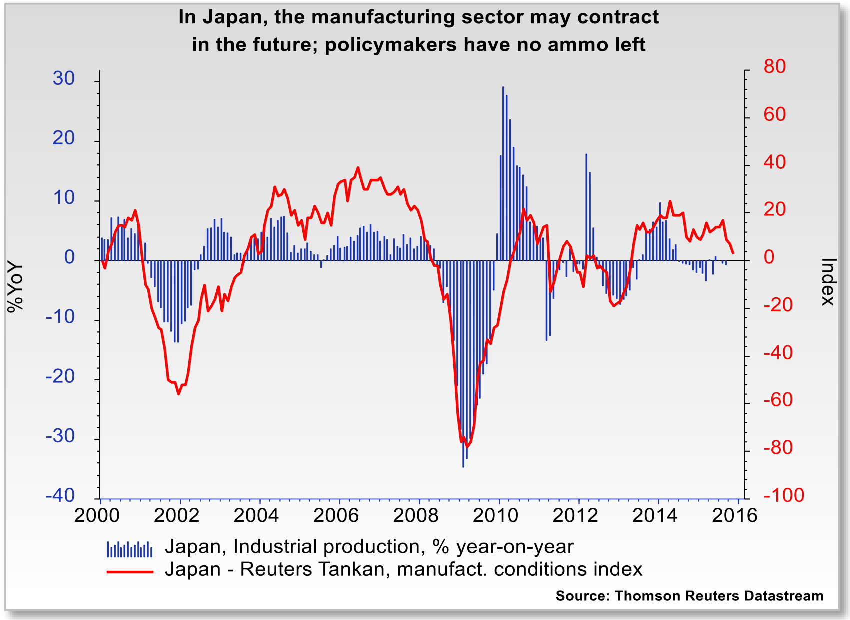
In 2016, the British economy is headed for a challenging year. The problem is that Britain has no policy tools left, as policy rates are already close to zero and public sector debt is close to a record high.

Japan – Economy enters recession; Tokyo is cornered

The Japanese economy is in recession. This became clear in the third quarter of 2015 after the economy contracted by 0.2% quarter-on-quarter. To be fair, the main drag on growth came from a negative contribution from inventories. On the other hand, the fact that corporate investment dented growth as well was bad news. The latter is the case even though Prime Minister Abe's policy measures predominantly have supported the corporate sector, since he took office in December 2012.

Unfortunately, there is really not that much policymakers in Tokyo can do if the economy stalls. At present, monetary policy is already ultra-loose. Furthermore, Japan is in a liquidity trap; this means that fiscal policy appears to be the only "valid" policy tool, if it was not for the fact that Japan is already running a huge fiscal deficit (public sector debt is close to 250% of GDP).

For some time, Insightperspectives has stressed its view that "Abenomics" is a significant policy failure. It is difficult to expect strong growth in an environment of a falling and ageing population. In fact, with a secular decline in the labour force, it makes no sense to pursue a policy of a weaker yen. The opposite is probably the case, as a stronger yen would animate economic players to boost efficiency and productivity, which is highly needed in an environment of labour shortage.



The problem, however, is that Abenomics has already cornered Japan. The current weak level of the yen is highly linked to financial market expectations that the Bank of Japan will continue on a path of money-printing. Any hints that this policy might change could trigger significant yen appreciation, which may ultimately also hit the Japanese stock market.

This is also why Tokyo will have to publish a convincing plan on how to revive growth. The best forward-looking indicators herald more manufacturing weakness. In November, the manufacturing headline index in the monthly Reuters Tankan survey fell sharply. Indeed, the situation is not expected to become any easier for Japan if ECB President Mario Draghi decides to ease monetary policy even more in the Euro-zone. Indeed, it is difficult to escape being a liquidity addict!

Russia - Economic sanctions may be lifted sooner rather than later

This newsletter has seen Russia as a very important player for some time, when it comes to finding a "solution" to the refugee crisis in Europe and the civil war in Syria – read the article, "Unwanted" military intervention in Syria seems imminent after failure in Egypt (September 2013). On the other hand, Russia was apparently not needed until the German Chancellor, Mrs. Merkel, autocratically opened the borders to all Syrian refugees a few months ago. Not surprisingly, this triggered a full-blown refugee crisis in Europe - read the

Insightperspectives article from September 2015, This time around, spontaneous and high-handed Merkel risks alienating more than just her own party.

Russia became an important player, not least after Moscow intervened militarily in Syria. Some critics assert that this worsened the refugee crisis, which is partly true. On the other hand, Mr. Putin's decision was a clever strategic decision, at least from a Russian point of view, as it made a solution to the Syrian civil war, and therefore a solution to the refugee crisis, impossible without Moscow. This became highly obvious during the G20 meeting in Antalya - read The Guardian article, G20: Barack Obama and Vladimir Putin agree to Syrian-led transition.

In fact, this seems now to boost the probability that the economic sanctions imposed on Russia linked to the Ukrainian crisis may be lifted in the near future. This was probably also part of President Putin's game plan - read more in the Insightperspectives article from October 2015, The game plan of president Putin matters to the global financial market - not least when it comes to the oil price.

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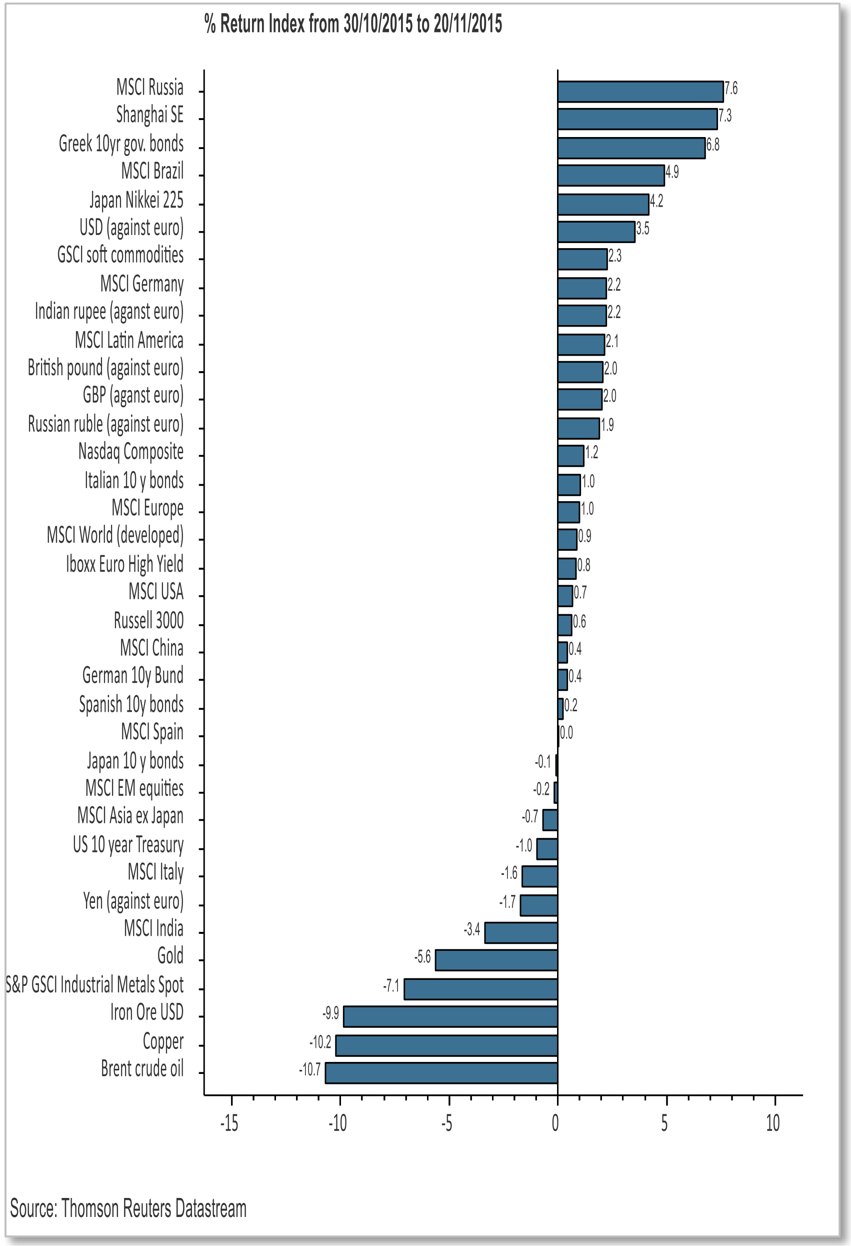
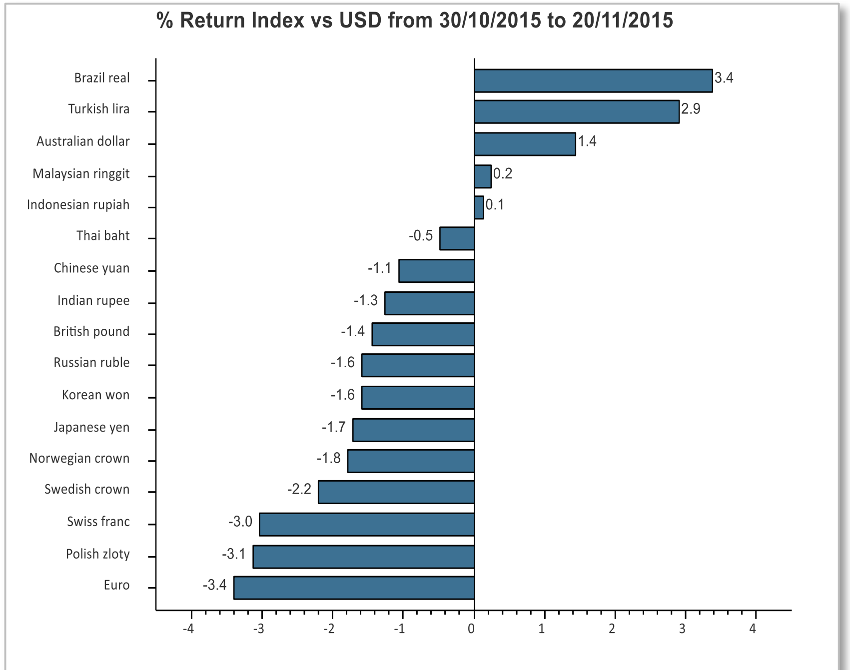
Financial Market Update



In November, Russia was among the best performing stock markets. The MSCI Russia index in local currency rose 7.6% (November 20); the market was propelled by the fact that Moscow is again back on the political scene, having intervened militarily in Syria. This may provide an escape route when it comes to economic sanctions imposed on Russia by the European Union and the United States in connection with the Ukrainian crisis – read more in the Russia section on page 10.

The domestic Chinese stock market also did well in November; the Shanghai A-shares index jumped by 7.3%. On the other hand, the MSCI China index rose only 0.4%. The MSCI India index fell sharply by 3.4% after the ruling party, BJP, was heavily defeated in local elections in the state of Bihar, which spells trouble for Prime Minister Modi's economic reforms.

In November, commodity prices were beaten yet again. The Brent crude oil price fell 10.7% while copper and iron ore prices fell 10.2% and 9.9%, respectively. This was the case as the Chinese economy continued to show weakness. The broader Goldman Sachs Metal price index fell 7.1%.



Source: Thomson Reuters Datastream

In the foreign exchange market, the US dollar continued to show strength. The euro fell 3.4% against the US dollar, which was reinforced by the European Central Bank's intentions to raise monetary expansion from "Italian" to "Japanese".

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Travel notes from China

No turnaround yet in sight; Internet Plus makes significant changes to the economy

This article was pre-published on November 9, 2015

In China, it has been evident for some time that the economy has huge problems breaking the stalemate of sluggish growth. Last week, the majority of Chinese and foreigners, whom the editor of Insightperspectives met in China, share this assessment. At present, they do not see any major growth driver in the coming twelve months. China is still struggling with the aftermath of the mother-of-all-stimulus in November 2008, which created overcapacity in many sectors of the economy. There seems to be a general perception among Chinese and foreign companies that slower growth is simply the "new normal" in the manufacturing sector in particular.

In China, slower growth has partly been deliberate after Beijing launched tightening and reform measures a few years ago. On the other hand, the latest downward pressure on “real” growth has probably become too much for comfort, according to Beijing. This was why, last week, Beijing launched a minimum growth target of "at least 6.5%" for the next five years (the 13th Five Year Plan). This is of special interest, as the general perception in China is that "real" growth is probably closer to 5% than 6.5%. This signals that Beijing intends to continue on a path of more fiscal and monetary easing. On Saturday, this was underscored after China’s

Vice Finance Minister, Mr. Zhu Guangyao, said, that a "higher fiscal deficit ratio is worth discussing". If Beijing had published a growth target of for instance 5%, this could have reinforced the current growth slowdown as such a target would have made many companies cut their investment plans significantly.

Having said that, there is no growth panic in China, at least not in tier-1 cities (Beijing, Shanghai, Shenzhen or Guangzhou). This is the case even though growth in the third quarter fell to the lowest level in six years. Conversely, the growth slowdown is far more visible in tier-2-cities and below due to a higher share of low-skilled manufacturing. Fortunately, economic dynamics is still very strong in China. The Chinese are willing to adapt, which was also the impression during last week's trip. Furthermore, entrepreneurship prevails in China. This is visible in in the more advanced service industries in particular, not least when it comes to internet-related services and software development. The positive development seen in this sector has been dramatic since the editor of Insightperspectives made his first visit to a Chinese BPO and KPO zone in 2005 in Xi'an in the province of Shaanxi.

In the last two years, however, the trend has become "explosive". If everything goes according to plan, this sector could later create the perfect environment for the next big wave in China, namely a boom in the Internet-of-Things. Granted, this is early in the development process and this sector is still far too small to make a visible impact on the broader economy, at least directly. Furthermore, profit in the sector is concentrated among a few companies, which is not necessarily conducive when it comes to moving a sector up the value ladder. Nonetheless, investors would be ill advised to ignore this sector; a huge number of well-educated engineers have poured in from universities in China and abroad. More importantly, this is a trend highly supported by Beijing - read more in the sections below.

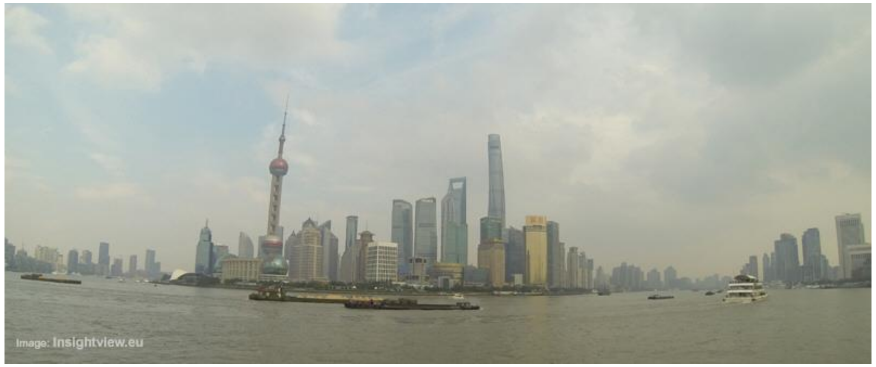
Manufacturing activity in China remains depressed; no anecdotal evidence of recovery

China remains exposed to considerable problems in the manufacturing sector. Last week's meetings confirmed this without any exception. This applies to the "lower-50%" of manufacturing, which are predominantly Chinese manufacturers; and the more advanced manufacturers (Chinese and foreign companies). Granted, this is somewhat in contrast to the fact that the China Caixin October PMI index rose to 48.3 vs 47.2 in September (the business sentiment survey focuses on smaller and medium-sized companies in the private sector), although this remains in the "contraction zone". The latter was also the case for the official manufacturing purchasing managers' index from NBS; the headline index was unchanged in October at 49.8 (the survey focuses predominantly on state-owned enterprises).

In China, more local and foreign companies noticed that Beijing's monetary and fiscal stimulus measures have had a positive impact on demand in the last few months. For instance, policymakers launched incentives animating households to buy smaller cars. In October, this bolstered car sales (units) by 11.3% month-on-month. This, however, has not changed the assessment of the companies met by Insightperspectives last week that the main issue in China remains overcapacity. A huge number of low-end manufacturers have disappeared; but Beijing still keeps many SOEs afloat to avoid creating social unrest; which is not least the case in tier-3 cities and below. This, however, could change in 2016 as policymakers recognise that this approach is not sustainable – read the article, China to speed up restructuring of zombie SOEs.

Ironically, weak manufacturing activity has not prevented blue-collar wages from increasing by approximately 8% every year, at least until now. This remains the case as the most important group of workers (age: 15 to 30 years) is now declining at the fastest rate seen in many years (minus 4.5% per year). In this context, Beijing's decision last week finally to alter the one-child-policy is long overdue. In fact, the decision comes far too late. Many Chinese simply cannot afford to have more than one child (education fees are sky-high). This is also why many Chinese Insightperspectives met are highly skeptical about the future impact of the changes to the one-child-policy.

In the manufacturing sector, the "lower 50%" still complain about a far too strong currency; this time in China was no exception. They should not expect much help from policymakers. Beijing appears reluctant when it comes to allowing the yuan to depreciate too much. First of all Chinese policymakers see a strong currency as a tool to animate Chinese companies to move up the value ladder. Ostensibly, Beijing is also scared about the financial consequences of devaluing more aggressively. This also is why Beijing is now back on a path of more fiscal and monetary stimulus. The current situation increasingly reminds the editor of the mother-of-all-stimulus in 2008, although this time around Beijing tries to make its efforts more low-profiled in the media (the stimulus measures in 2008 were widely seen as the main factor behind today's overcapacity problems).



Nonetheless, ultimately the yuan will depreciate to 6.70 against the US dollar to compensate for a beggar-thy-neighbor-policy in the Euro-zone in particular. This will be the case not least if the euro declines to have parity against the US dollar (which is still part of this newsletter's outlook). Last week’s strong US labour market report for October will surely boost the probability of such an outcome.

The fact that Beijing yet again uses investment spending as a major policy tool is a policy-mistake, according to many Chinese Insightperspectives met this time. This has also triggered prominent criticism from the few who still dare to stand up against a more-and-more autocratic president Xi Jinping. In October, the former China International Capital Corporation Chairman, Mr. Zhu Yunlai, who is also the son of the widely respected, Mr. Zhu Rongji, a former Premier Minister, said that the government should give up trying to prevent an economic slowdown and instead invest its efforts in finding new growth areas and reform the economy.

Private consumption remains strong; high-end sales remain under pressure

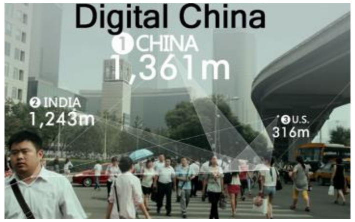
Today, China is surely no longer a cheap place, at least not if you are foreign tourist. This becomes evident every time the editor visits China. In the last few years, the yuan rose by more than 30% against the euro and the yen. On the other hand, this is positive news for private consumption on the mainland as it boosts Chinese households’ purchasing power. This is also why there are no major signs yet of any significant slow-down in private consumption, at least not in tier-1 cities, as households' real income continues to improve steadily.

Nominal wages increase in the range of 7% to 10% and inflation is low. An increasing number of Chinese, however, are yet again complaining about increasing house prices. Furthermore, there is an increasing risk that slower growth in tier-3 cities could hit wages, which may ultimately dent private consumption on a national level in 2016. In addition, high-end sales remain weak (these shopping malls are empty).

Conversely, “special" shopping centers, where consumers feel “entertained”, are still seeing strong traffic. This applies to IKEA in particular. Ten years ago, when the editor visited an IKEA shopping center in China for the first time, this was solely affordable to high-income households. Today, this has changed radically as households at the lower end of the middle class are also among the customers, which is highly visible when visiting IKEA. Interestingly, this has not necessarily been at the expense of high-income earners; the range of possible IKEA-customers has just become wider.

Internet Plus could create the foundation for China's next growth leg; yet another warning to old industries in the developed world of what lies ahead

In China, the economy has split between a weak manufacturing sector and a relatively strong service sector, which has been evident in the last few years. The strong performance of the service sector has been highly associated with an explosive uptrend in the usage of internet-related platforms, spreading of smartphones and still relatively cheap mail delivery - click here or on the image on the right to see a video showing a few general facts about "digital China".



In the last few years, Chinese IT-related companies such as Alibaba, JD.com, Tencent, Baidu, Xiaomi, ZTEand Huawei have benefited strongly from this trend. A few of these companies, not least Tencent and Alibaba, have become essential for many Chinese households (24-7). Importantly, this is with the blessing of policy-makers in Beijing. The Internet Plus plan was presented in March 2015 by Prime Minister Li Keqiang - click here or on the image below to see a video showing how smartphones are used today in Chinese cities and in the countryside.

At present, more of the features used on smartphones are of course just nice-to-have gimmicks; but there are also features, which are improving productivity significantly on an aggregated level. For instance, smartphones make appointments with your doctor, which can be quite a time-consuming exercise in China. Ultimately, smartphones may eventually circumvent a highly bureaucratic public sector in China, although this may be too optimistic, according to some Chinese who are highly familiar with public bureaucracy on the mainland.

In China, the IT-sector is admittedly still far too small to compensate for declining growth momentum in the "older part" of the manufacturing sector. On the other hand, Insightperspectives believes that the strong trend in this sector could potentially create the foundation for one of the next major growth legs further down the road. This is because China has narrowed the technology gap to the United States markedly. Until recently, this was of course partly due to copying. On the other hand, today China develops and launches many software applications ahead of the United States or Europe. These applications are spreading at a much faster pace than in many other countries. Ultimately, this will boost the possibility that the next big "internet-of-things" may come from China, as China suddenly becomes the frontrunner.

In China, companies such as Tencent and Alibaba are very well aware that this requires a different setup. This is why these companies are diversifying horizontally as well as vertically (content and development). Earlier this year, Mr. Ma Huateng, Chairman of Tencent Holdings, signed an agreement with Taiwan's Hon Hai Precision Industry and Chinese luxury auto dealer China Harmony Auto Holding to explore opportunities in smart electric vehicles. Other Chinese tech giants have announced similar strategies. To make this trend sustainable for China, however, it is essential that profit created in the IT-sector is not concentrated among a few companies. This will ensure a stronger competitive environment, which will ultimately boost research and product development.

The fact that China is moving towards the "smart city" at a much faster pace sends an even stronger warning signal to many "old industries" not only in China but in the developed countries in particular. The same warning was issued in March 2014, when Insightperspectives visited Chinese banks and retailers – read the article, Rapid and dramatic structural changes in retail and banking sector reinforce debt problems. The "smart city" is circumventing the value chain, which could abruptly undermine the very foundation for many companies within a short period (for instance traditional banking). The risk of "corporate disruption" is increasing.

This is only a question of when (and not if) the explosive trend seen in China hits the shores of Europe and the United States more aggressively. In 2013, Insightperspectives asked a Chinese financial market expert whether it would make sense for some of the conventional banks to merge with Alibaba or Tencent. At that time, the answer was “maybe”. Today, the answer is that neither Alibaba nor Tencent need a bank, as households already deposit billions of yuan directly in these companies (Alibaba and Tencent have a bank license).

China is turning left in politics and right in economics

Last week's trip to China has not changed this newsletter's overall perception of the future direction of the Chinese economy. The manufacturing sector is still having a very tough time and there is no doubt that Beijing is also worried that the current growth slowdown has become too much for comfort. This means more stimulus and ultimately more yuan weakness. In this context, the anti-corruption campaign still plays a significant role; and there are no signs that this will end anytime soon. In fact, the anti-corruption campaign is now part of the “new normal”. On the other hand, the reform process will continue, but at a slower pace and probably with a hidden bias towards supporting domestic companies at the expense of foreign companies. The latter is still the feeling among a few foreign companies.

The general perception in China is that the leadership in Beijing aims for steady rather than explosive economic development. In this context, Beijing has probably also learned from the stock market fiasco earlier this year. This weekend Beijing opened up for new public offerings in the stock market, having halted IPOs since July, when the Chinese stock market collapsed. There is no doubt that Beijing would like this decision to be seen as a prudent steep to reduce volatility, having seen the domestic stock market soar by more than 20% in the last few months. "If" successful, the decision would show that policymakers are “so much in control” of the stock market that they can afford to put a cap on prices. Granted, this may be wishful thinking; but it may enable Beijing to save face, at least in the short run, after the catastrophic stock market turbulence in July.

In general, one can say that China is moving politically left while the economy continues moving only slowly to the right. On the other hand, this is probably the best outcome from a global investor's point of view, as China has created far too much volatility in the past few years. It is far more difficult to make a firm conclusion when it comes to assessing the impact of Mr. Xi politically moving further to the left (more autocratically leadership). In China, there is no doubt that President Xi has now become the ultimate leader after the anti-corruption campaign has been a strong tool for political cleansing.

Many Chinese believe the last-mentioned initiative has been so effective that Mr. Xi has made many influential members of the Communist Party elite hostile towards Mr Xi. Apparently, they have not yet played their cards openly, according to many Chinese. In this context, former president Jiang Zemin is still spooking. On the other hand, the anti-corruption campaign has earned Mr. Xi significant support from ordinary people, since it has proved effective in fighting highly visible corruption. Conversely, the campaign appears so effective that few cadres dare to take even necessary decisions, which has also put a lid on many investment projects. This is also a highly important issue when talking to domestic and foreign companies in China; nobody dares to take the wrong decision in the current political environment.

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EU

The Paris terror attacks and refugee crisis risk leading Europe in the wrong direction

This article was pre-published on November 19, 2015

The influx of refugees in Europe made waves already before the horrific terror attacks in Paris launched by the Islamic State on November 13. This has been reinforced by the fact that one of the perpetrators apparently had a Syrian passport (the holder of this passport sought asylum in Serbia). Whatever the truth is, there is no doubt that the terror attacks will be linked by more politicians to the latest influx of refugees to Europe.

In more European countries, the events in Paris are a wakeup-call to many politicians. At least, this is the case in France, where the President has said that France is now at war. Shortly after the events in Paris, Mr Hollande even considered invoking article 5 of the NATO Treaty, which apparently worried Berlin - read the Die Welt article, Krieg? Ja, aber nur aus französischer Sicht. This is probably also why France uses the EU emergency clause in the Lisbon Treaty instead (article 42, 7) requesting military support from other member states. At the same time, France is now considering stripping dual citizens of their French citizenship if they are "deemed a terrorism risk".

Indeed, it seems the political establishment in Europe is finally responding to public opinion. In Germany, however, this process appears far more slowly, as the refugee policy seems solely to be managed by Mrs Merkel. On November 13, the Chancellor stressed yet again in a TV-interview, a few hours before the events in Paris, that she has no intention of changing Germany's refugee policy. Instead, she wants a better European distribution of the refugee burden.

The Paris terror attacks, however, may persuade even more Germans to question what they see as Chancellor Merkel's "somewhat naïve willkommen-policy".

On the other hand, no prominent politicians within the CDU have so far had the courage to be the official front-runner in any revolt against Chancellor Merkel. This is the case even though opinion polls are turning against the Chancellor - read the article, Focus-Umfrage: 38 Prozent der Deutschen für Merkels Rücktritt. The problem is that any potential front-runner is well aware that even if Mrs Merkel could be forced to leave office, her refugee policy is still supported by a majority in the Bundestag; (CDU, SPD, Die Linke and Bündnis-90).

Nonetheless, Mrs Merkel's political life is at risk, not least if opinion polls continue to show further deterioration in public support to the union (CDU/CSU). In addition, the latest opinion poll shows that the far-right political party, Alternative für Deutschland, hit a new high of 10.5%, which would make it the third biggest party in Germany. The rise of AfD is a worrying sign as the party is normally not seen to be a real political alternative due to the party's link to extreme nationalist organisations. This is indeed a warning to the political establishment that the far right could gain protest votes in the "right" political environment.

Merkel is alienating European neighbours

Regardless of whether Mrs Merkel will survive politically, there is no doubt that her autocratic approach in the context of the refugee crisis has already propelled support to political parties on the far right and left in the other EU-countries. Unfortunately, at least from this newsletter's market liberalist point of view, these parties often have an anti-EU or anti-globalisation agenda. In many ways, Mrs. Merkel has turned loose these forces. This is the case after in the last few months the Chancellor took decisions linked to the influx of refugees without consulting the other European member states.

Now that Mrs. Merkel appears to have lost control of the influx of refugees, Berlin suddenly wants other countries to bear their brunt of a “burden”. This could prove to be “mission impossible” as many Europeans believe Mrs. Merkel created the problem by issuing an open invitation to all Syrian refugees – read also the Die Welt article, Polen nutzt Paris für Anti-Fluechtlingspolitik. Interestingly, this is even an opinion shared by an increasing number of US politicians and states that oppose President Obama’s offer to receive ten thousand Syrian refugees – read the CNN article, More than half the nation's governors say Syrian refugees not welcome.

Mrs. Merkel’s decisions may be "morally correct"; but they are not necessarily based on democratic rules, according to many politicians in and outside Germany - read also the Die Welt article, Nicht Merkel, sondern das Parlament entscheidet. It is a fact that many of these decisions have been taken by Mrs. Merkel over the heads of national parliaments all over Europe. This is also why Berlin risks eroding a political goodwill in

Moscow’s game plan may succeed in lifting economic sanctions

Insightperspectives has for some time seen Russia as a very important player when it comes to finding a "solution" to the refugee crisis in Europe and the civil war in Syria – read the article, “Unwanted” military intervention in Syria seems imminent after failure in Egypt, September 2013. On the other hand, Russia was apparently not needed before the German Chancellor, Mrs. Merkel, opened the borders to all Syrian refugees a few months ago.

This has provided an opportunity for President Putin to become the key player, not least after Moscow intervened militarily in Syria. This made a solution to the Syrian civil war, and therefore a solution to the refugee crisis in Europe, impossible without Moscow, which became highly obvious during the G20 meeting in Antalya - read The Guardian article, G20: Barack Obama and Vladimir Putin agree to Syrian-led transition.

Interestingly, this seems to have boosted the probability that the economic sanctions imposed on Russia linked to the Ukrainian crisis may soon be lifted, which was probably also part of President Putin’s original game plan; read more in the Insightperspectives article from October 2015, The game plan of president Putin matters to the global financial market - not least when it comes to the oil price.

other EU-countries, which Mrs. Merkel's predecessors used decades to rebuild since the end of WWII.

The political factor is a big risk to long-term growth

In Europe, the long-term political impact of the terror attacks in Paris and the ongoing refugee crisis is probably far more important than the short-term shock to consumer and business sentiment. The refugee crisis and the events in Paris (and what comes next) could change the political landscape markedly unless the political establishment is willing to adjust to public opinion. The negative consequences to consumer sentiment caused by the terror attacks in Paris may soon disappear "if" one assumes that no more terror attacks are launched in the near future (although the jury is still out).

In the near future, the influx of refugees is still seen by this newsletter to support growth. This is not least the case if the European Central Bank uses the events to speed up monetary easing – click here to see Insightperspectives' updated global economic growth forecast. The biggest threat, however, is to long-term growth. This is the case if the refugee crisis and not least the events in Paris were to lead to more support to the political far right. This will not only be a vote against more refugees, but this would also be a vote against more European integration and more globalisation. The latter is a huge problem, not least from the point of view of the financial market and the corporate sector. In France, the first test of this is the upcoming regional elections called in December, which may further propel support to Front National, a French far-right party.

Indispensable Merkel?

Interestingly, on the very same day the terror attacks in Paris unfolded, The Economist's front-page called Mrs. Merkel "indispensable". This, however, ignores the fact that, during her leadership, the German Chancellor has neither done anything to improve Germany's economic situation nor to bolster the European Union. In fact, Mrs. Merkel's popularity has been due more to "status quo" rather than progress. This has also been noticed by many critical voices in Germany – read the Die Welt article, Seit 2010 macht Kanzlerin Merkel eine "Reformpause".

Germany is still benefiting from economic reforms launched by Mr. Gerhard Schröder, the former SPD-chancellor, more than a decade ago. When it comes to the European Union, Mrs. Merkel has made a number of compromises with Greece in particular, which has made the monetary union more fragile than ever before. Mrs. Merkel could be compared to former US president Jimmy Carter, who had all the "right opinions" although he was politically destabilising the United States in the late 1970s. In 2015, Mrs. Merkel has learned an important lesson namely that it is easy to be morally right; but this is far more difficult to implement without creating chaos!

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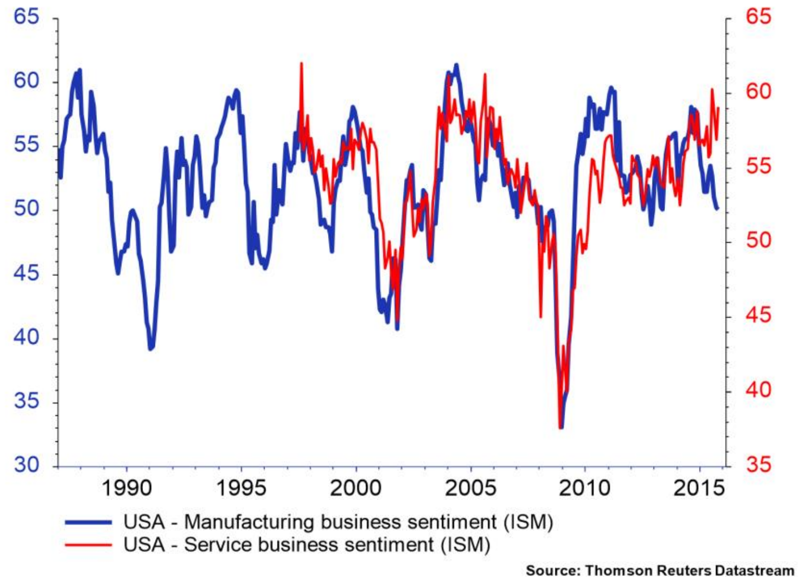
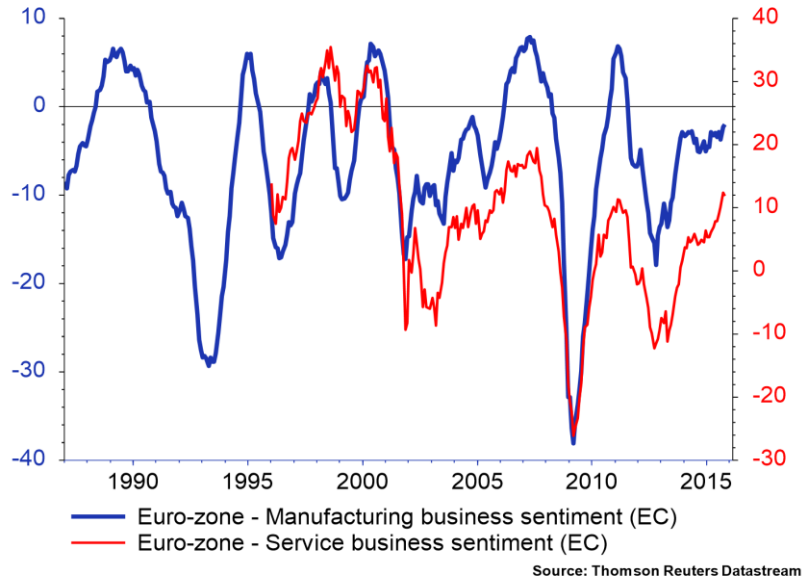
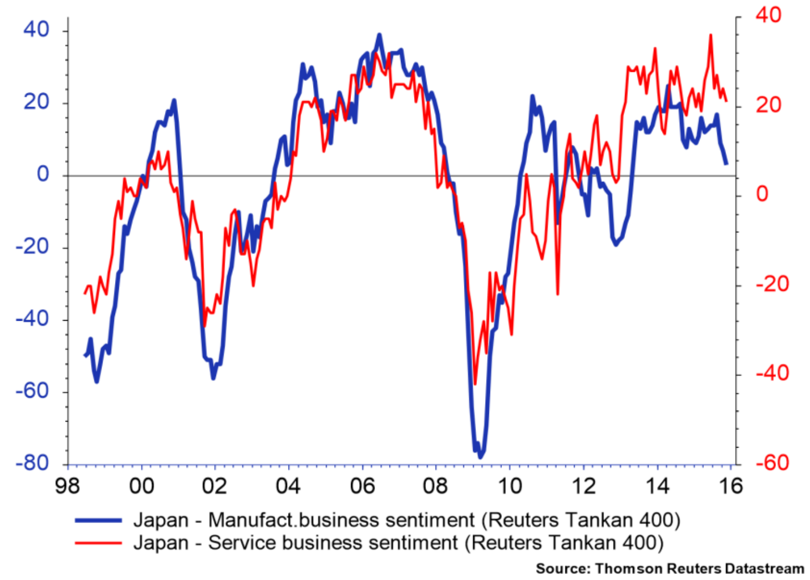
Charts

All charts are updated on November 20, 2015

Business Sentiment







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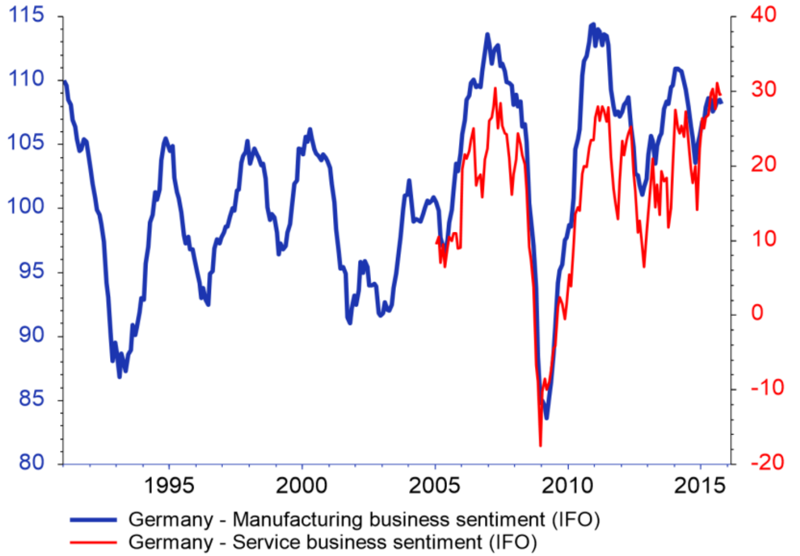

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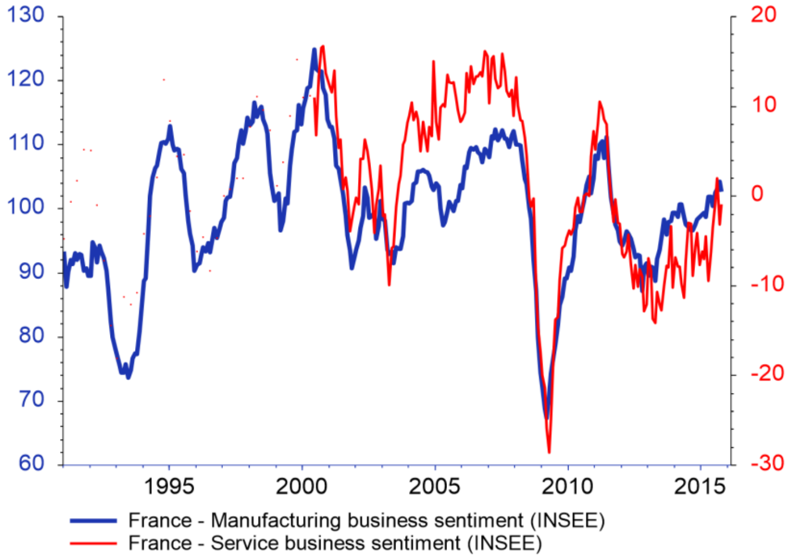

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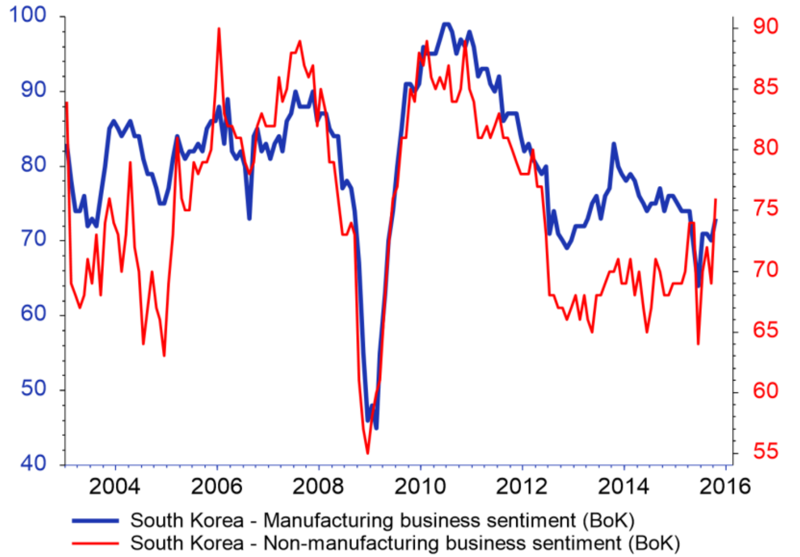

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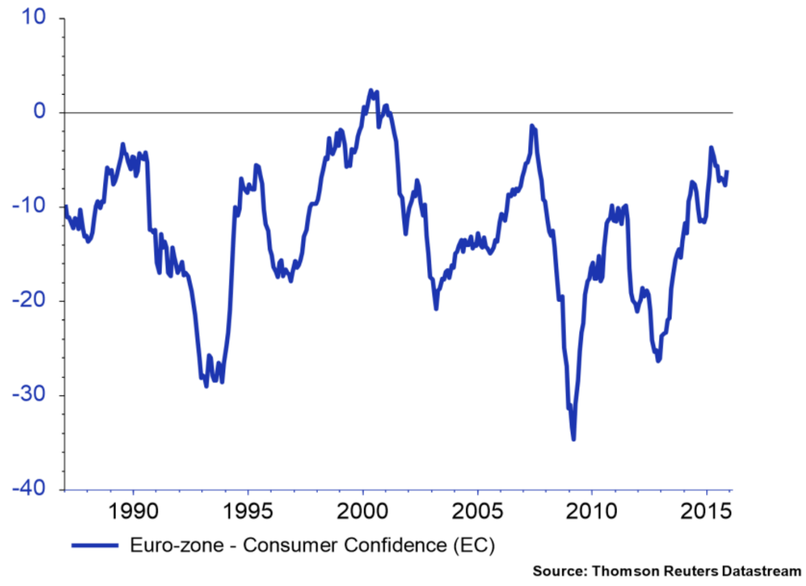
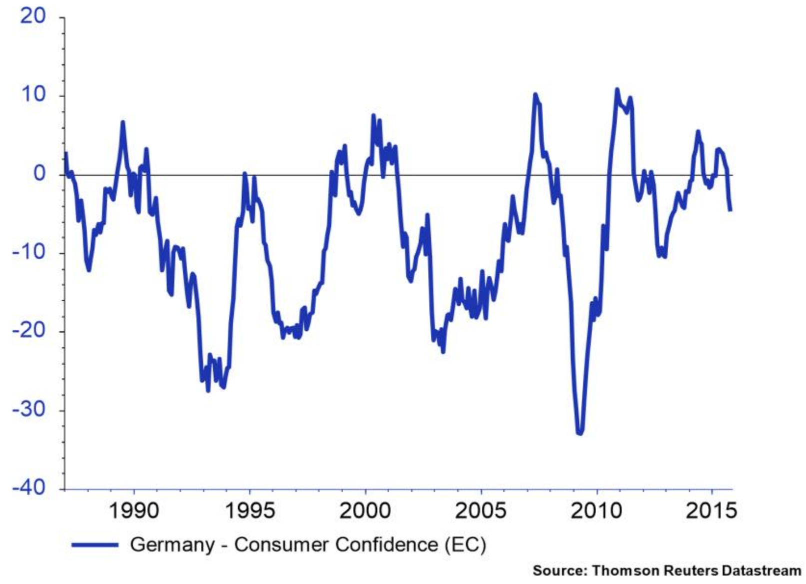
Consumer Confidence





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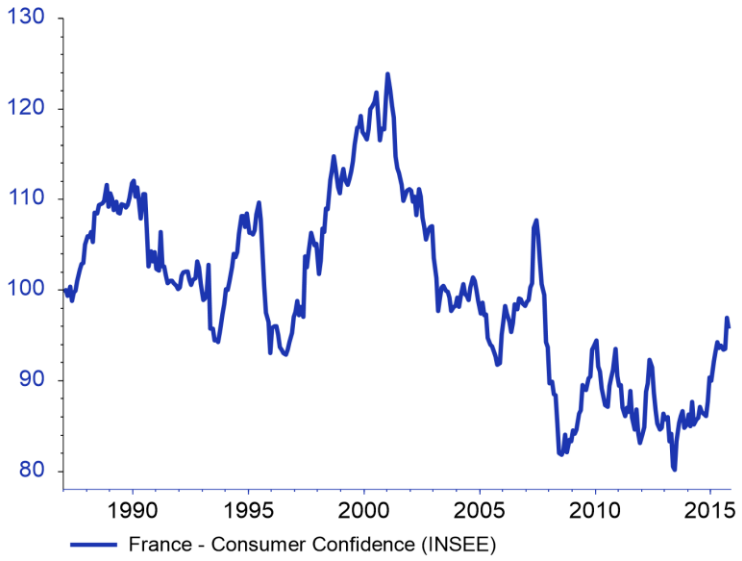

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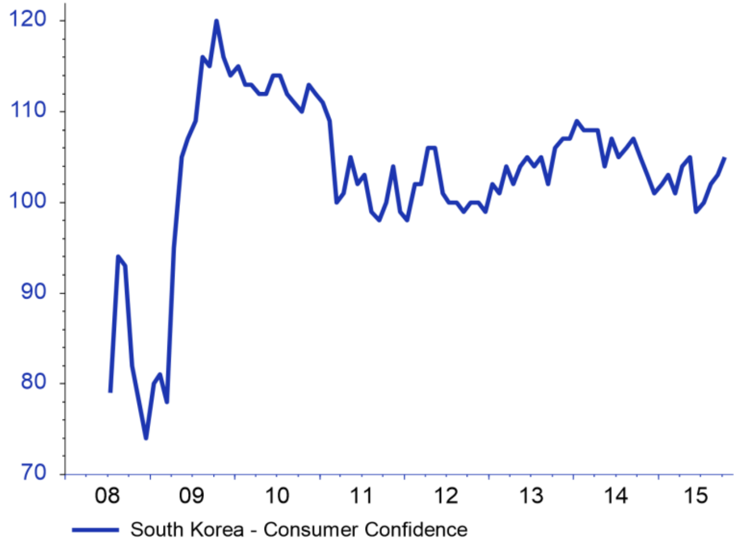

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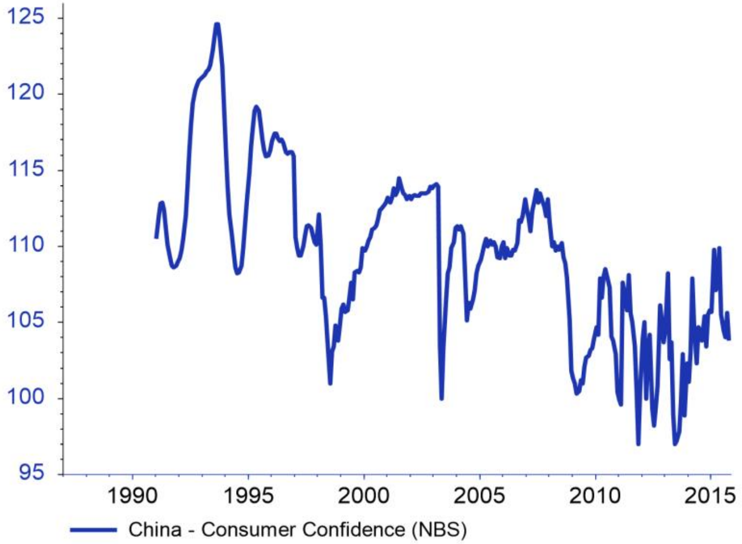

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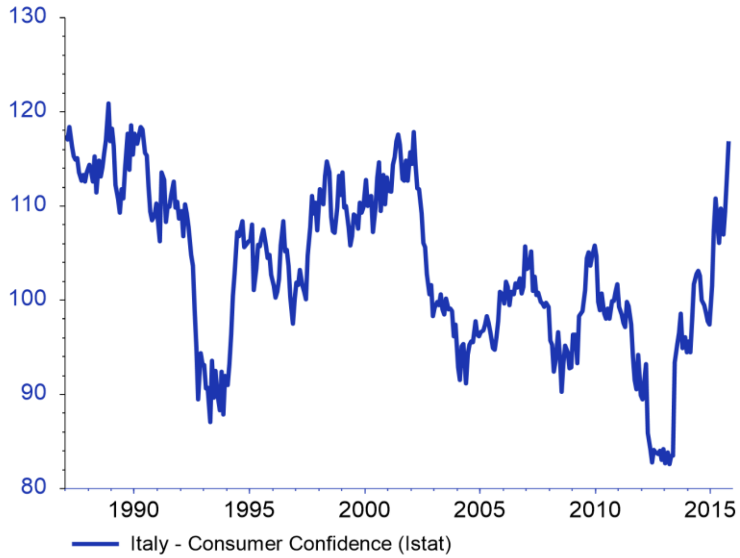

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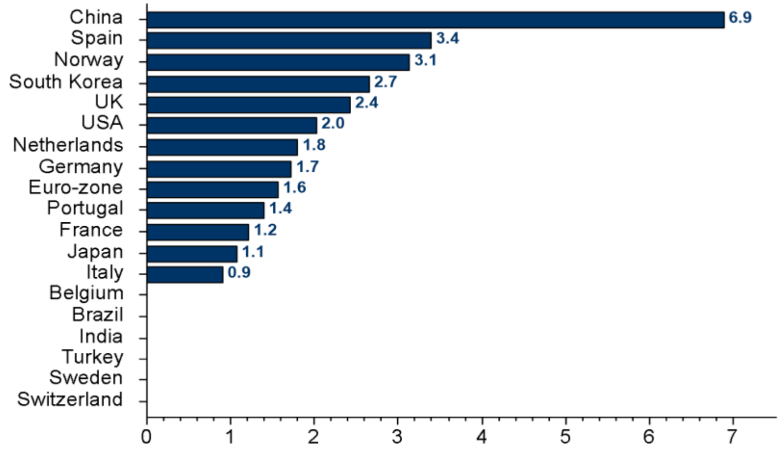
Real GDP growth

%YoY- Q3 2015



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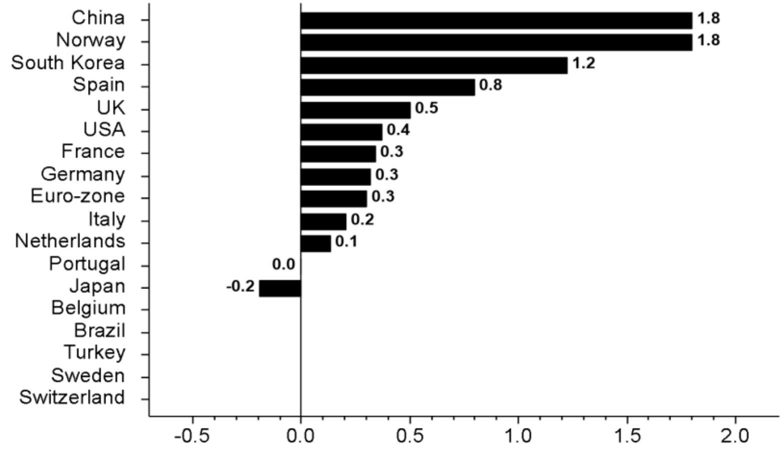
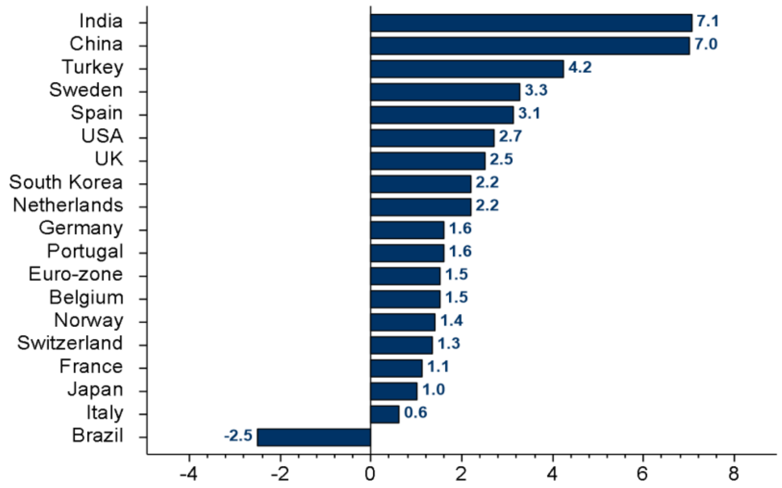
%QoQ - Q3 2015
(India is not included)



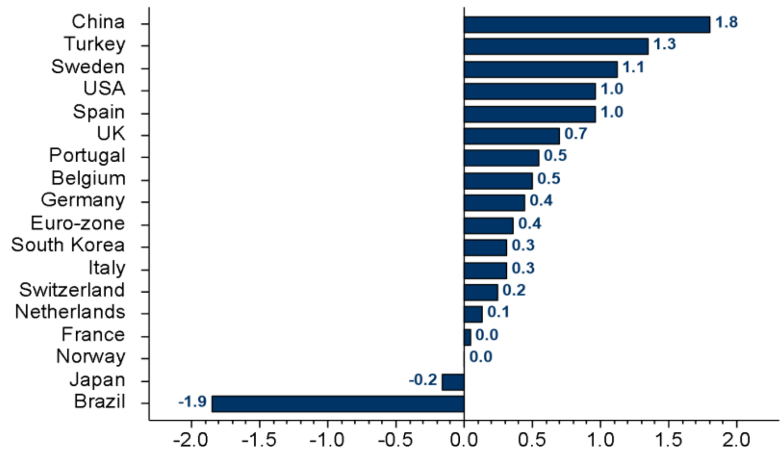
Source: Thomson Reuters Datastream

% YoY - Q2 2015



Source: Thomson Reuters Datastream

% QoQ - Q2 2015
(India is not included)



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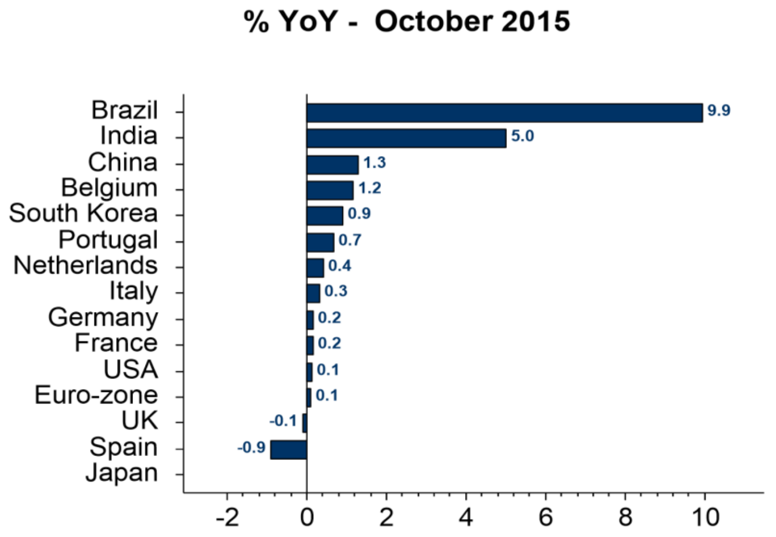
Consumer price inflation



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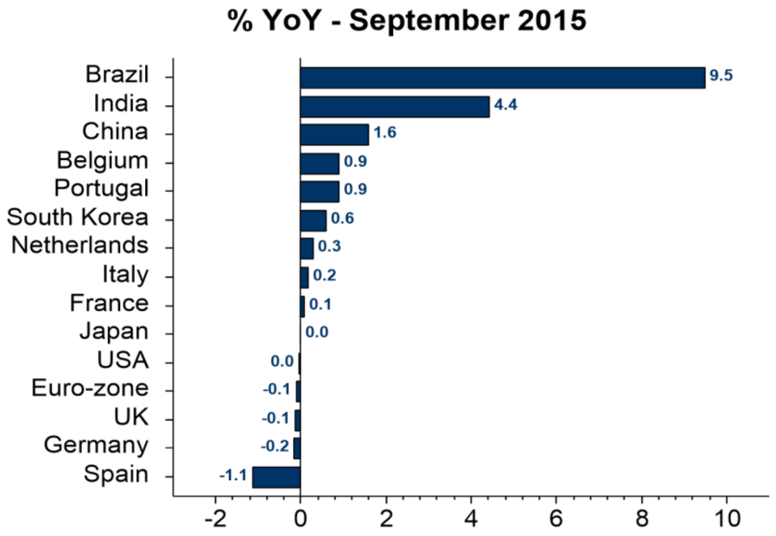

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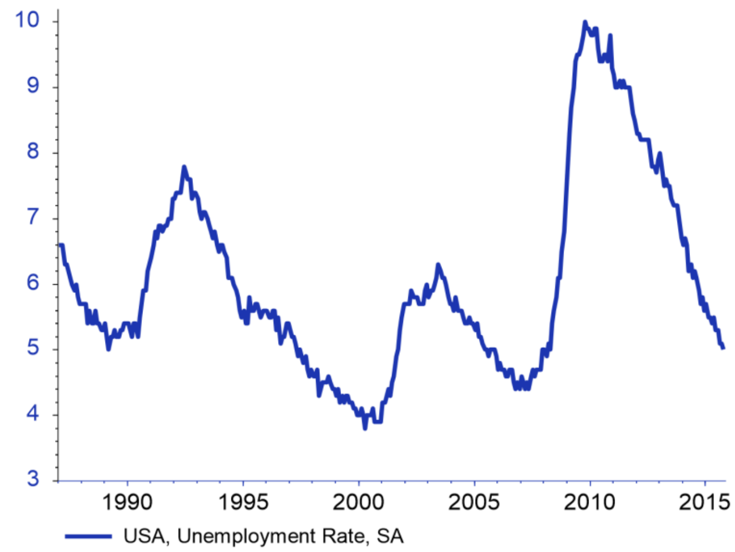
Unemployment



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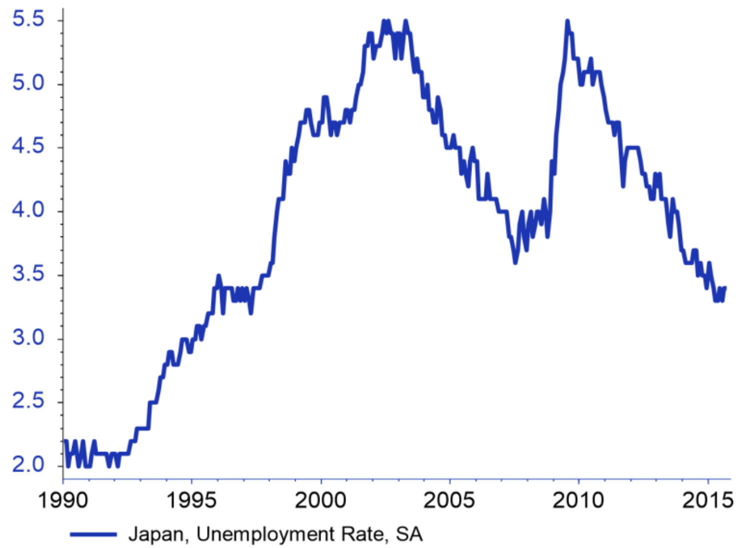

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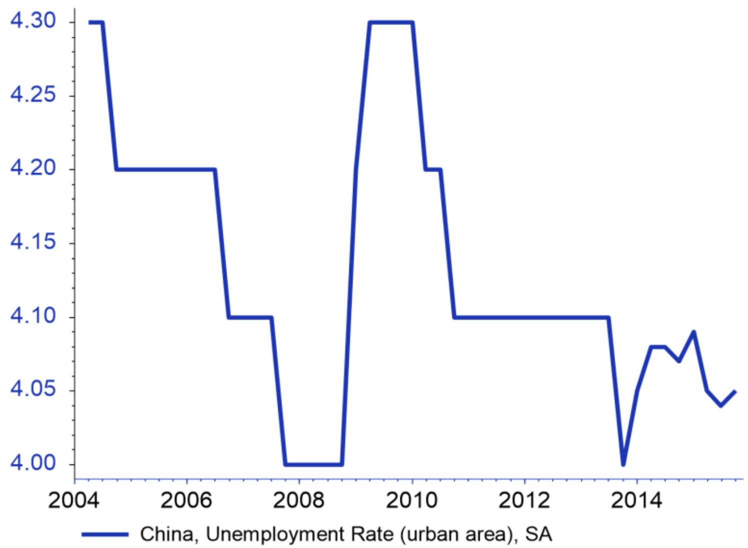

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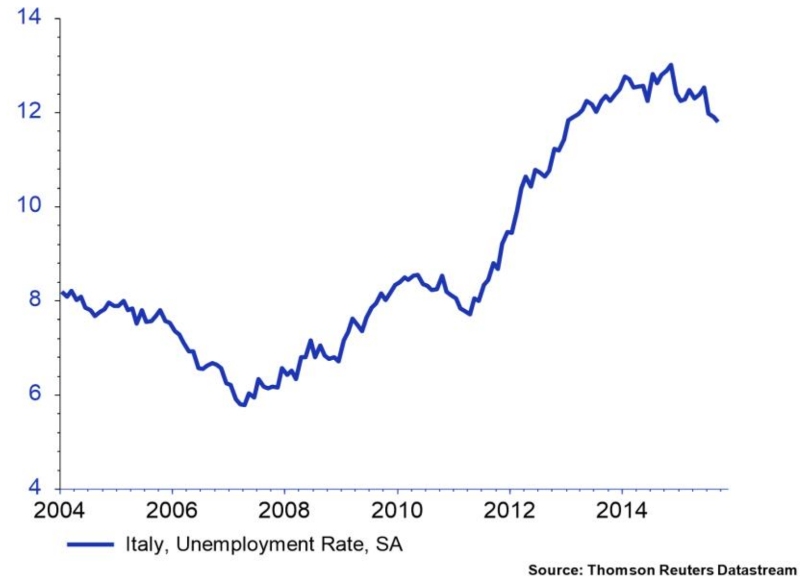
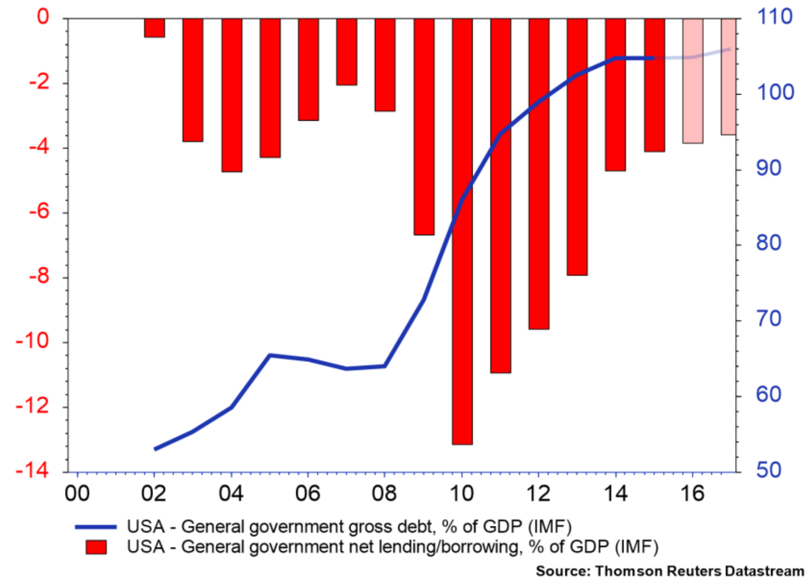
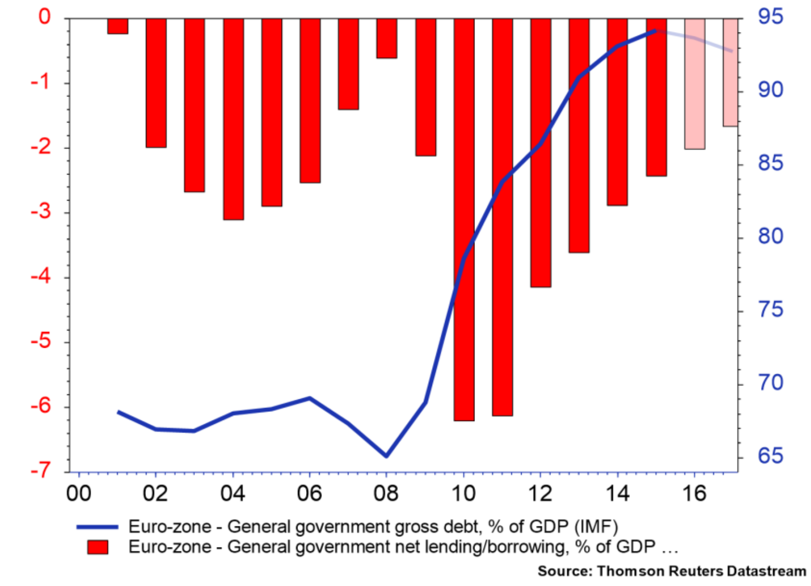
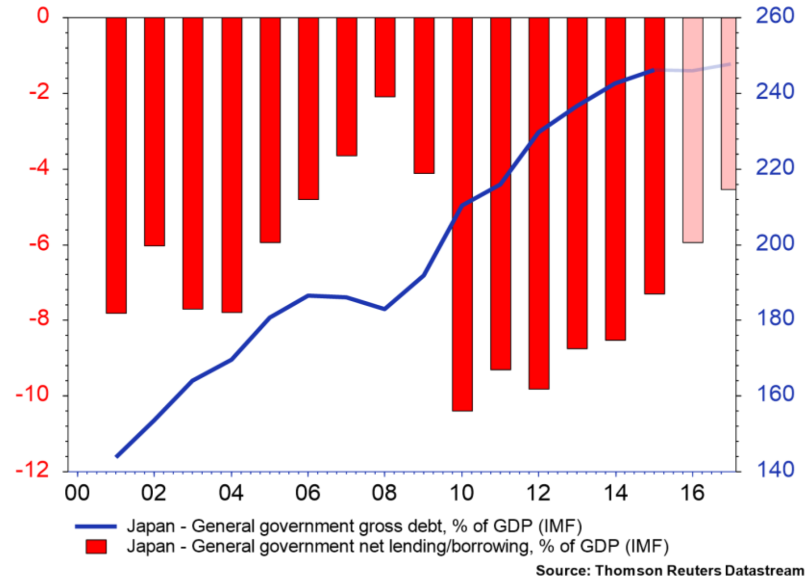


Public Sector Balances







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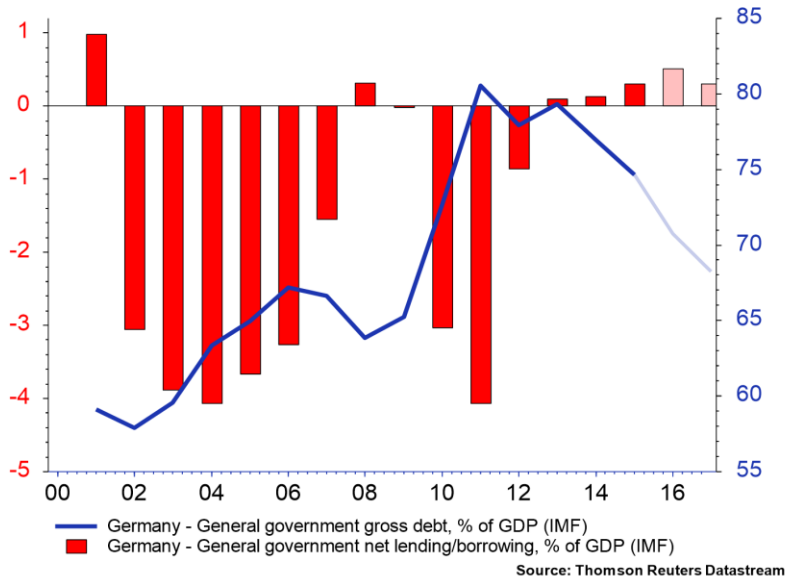
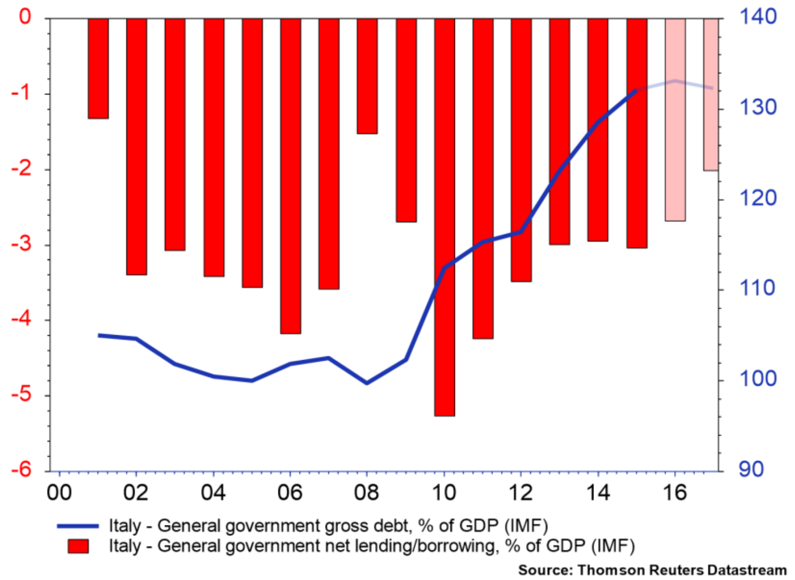
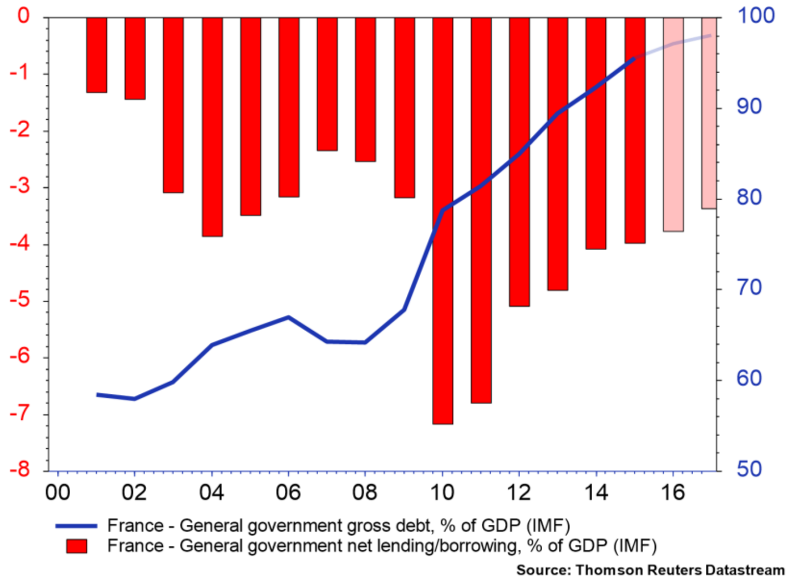
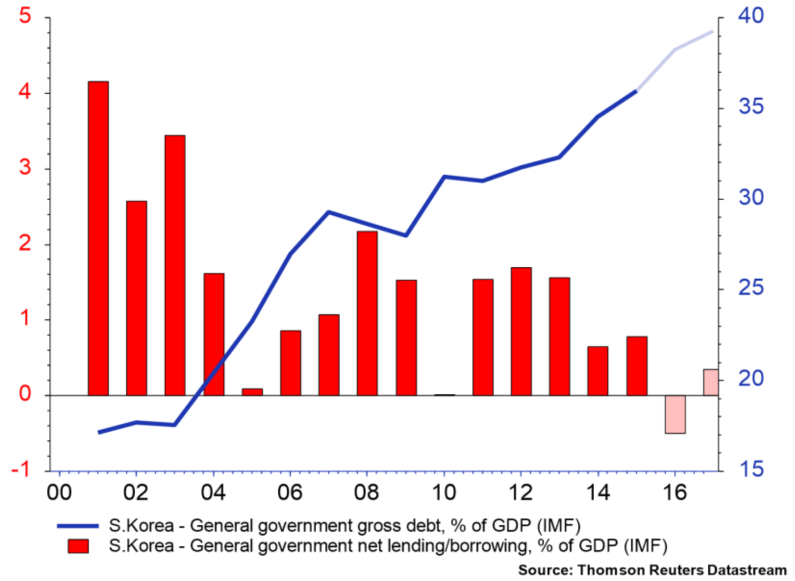
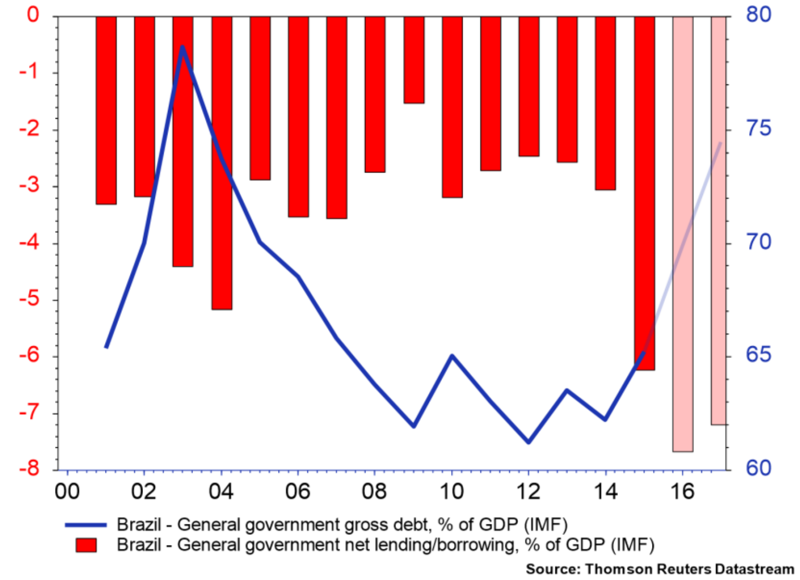


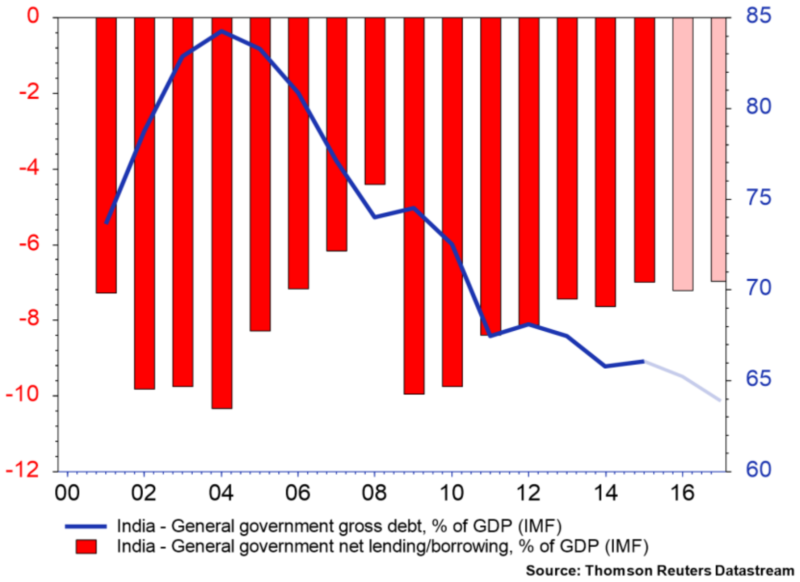




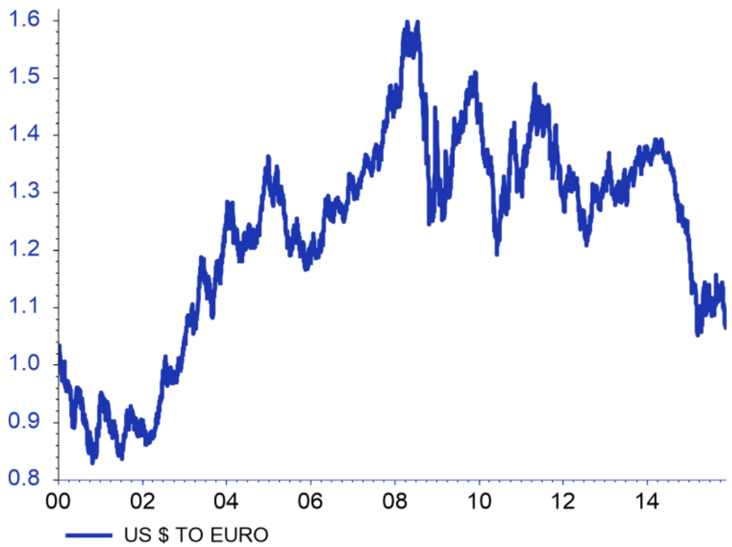


Public Sector Balances (continued)





Foreign Exchange Market



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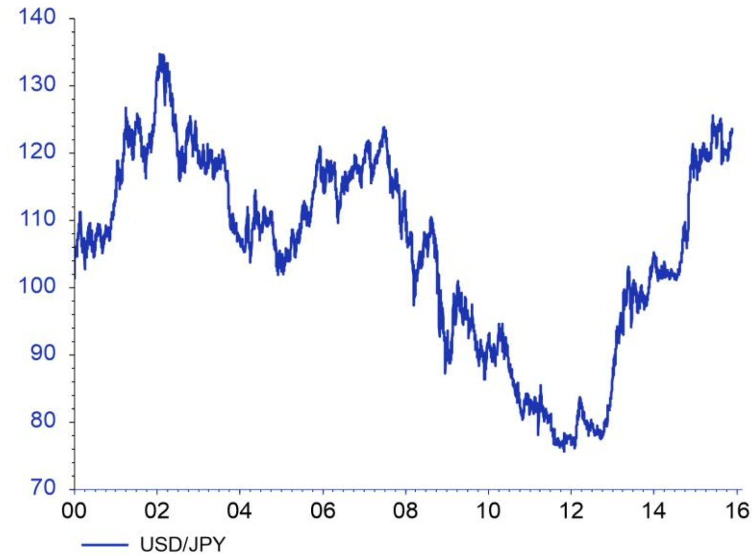

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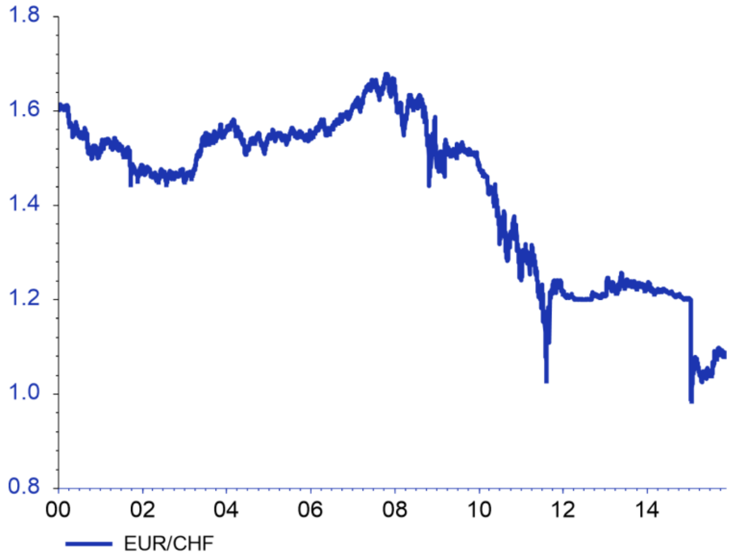

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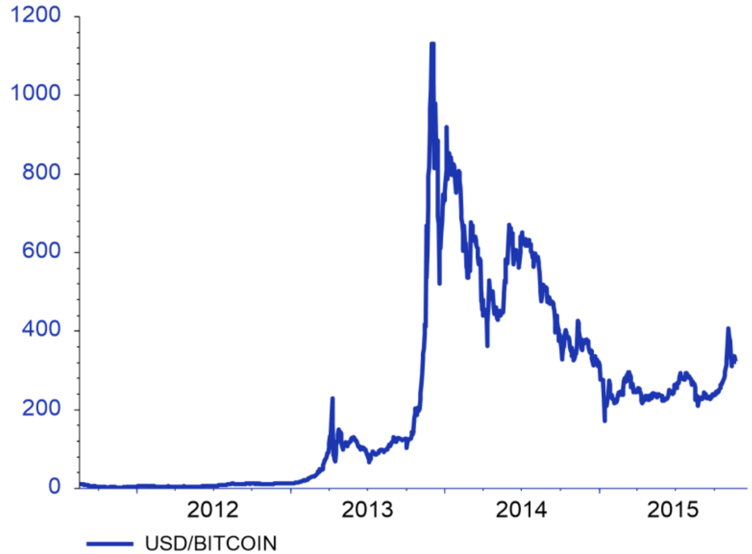

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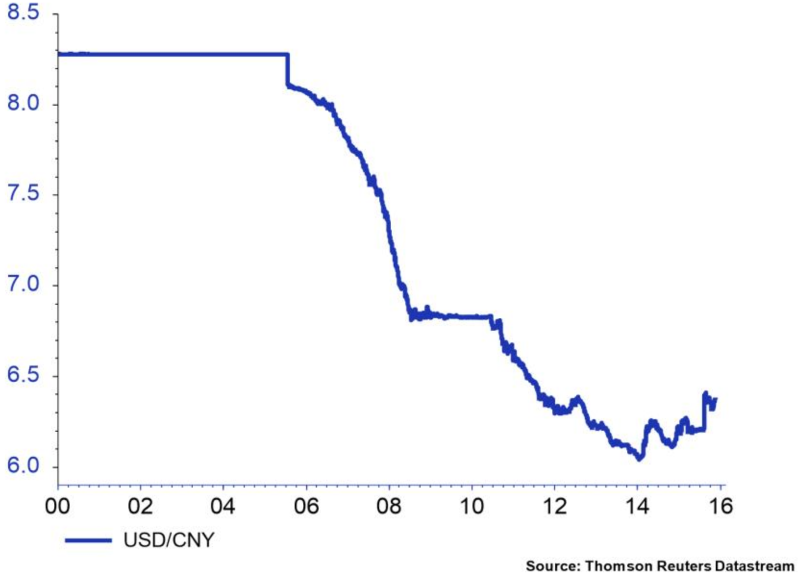
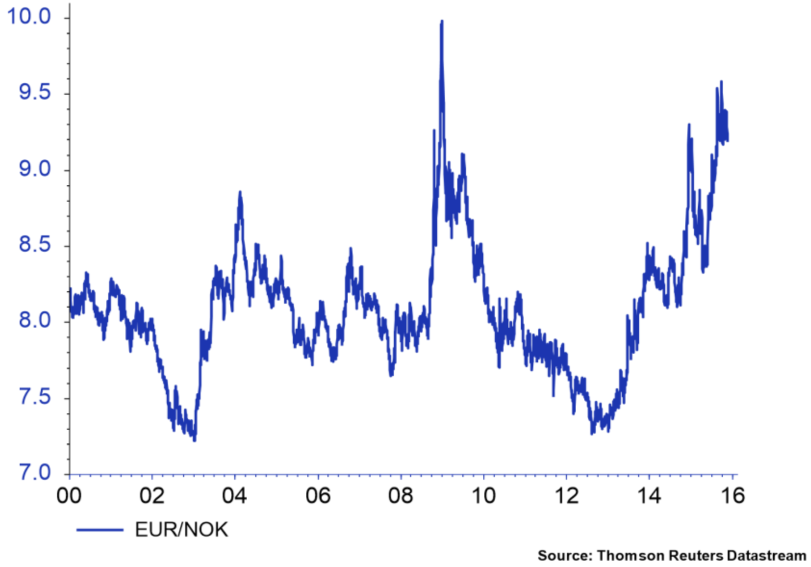
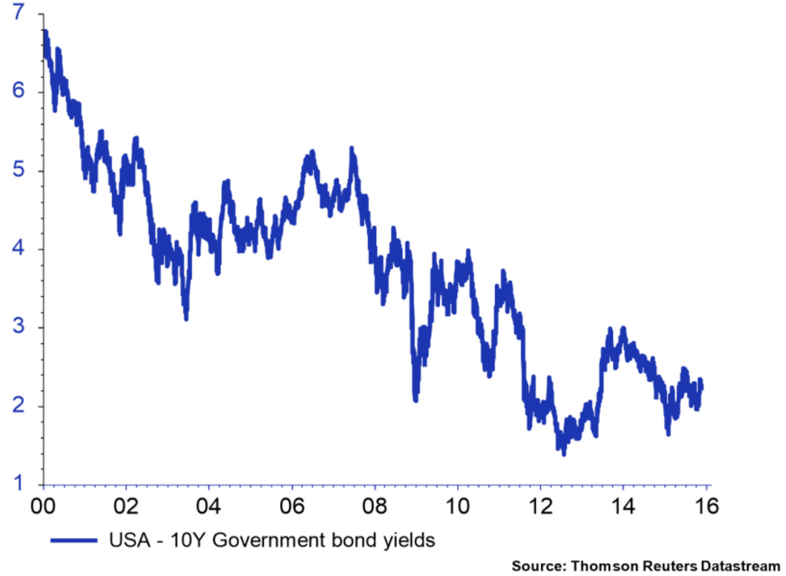
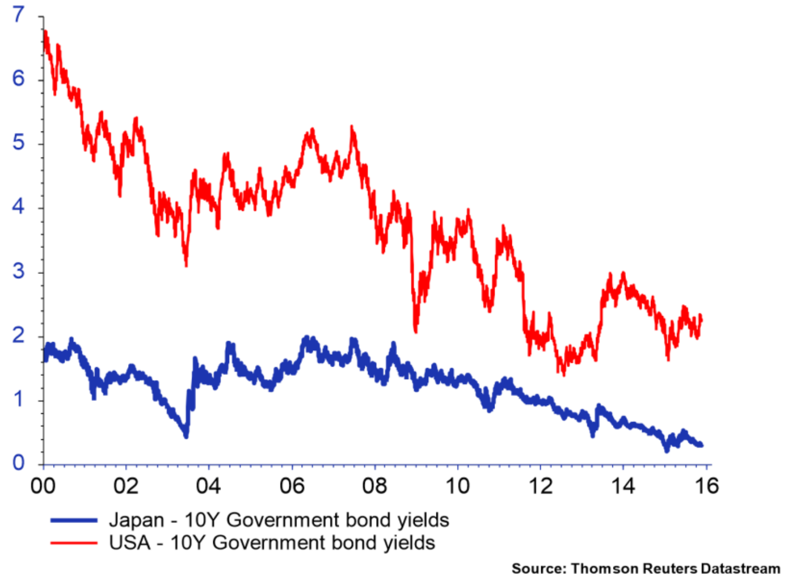


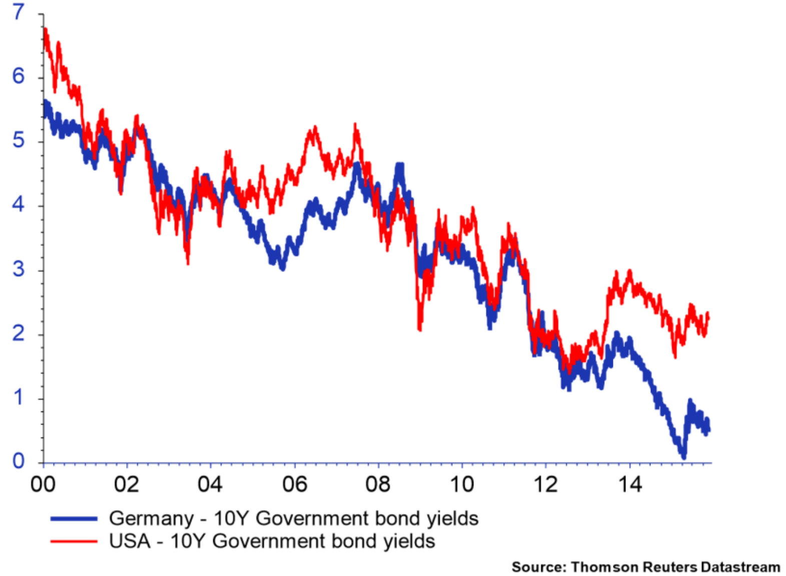


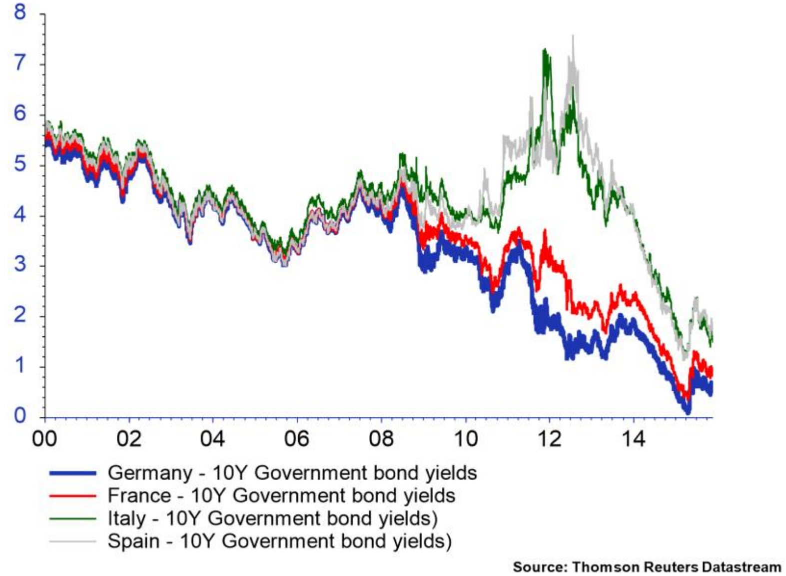
Government Bond Yields

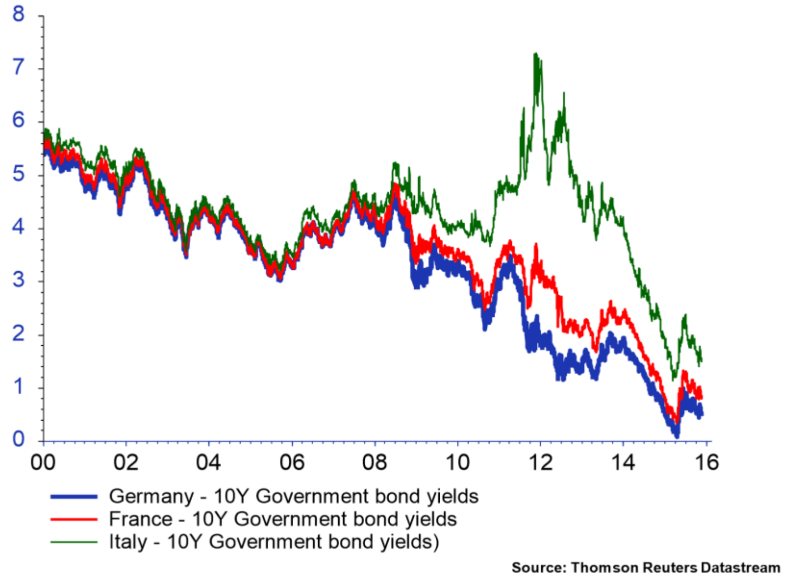


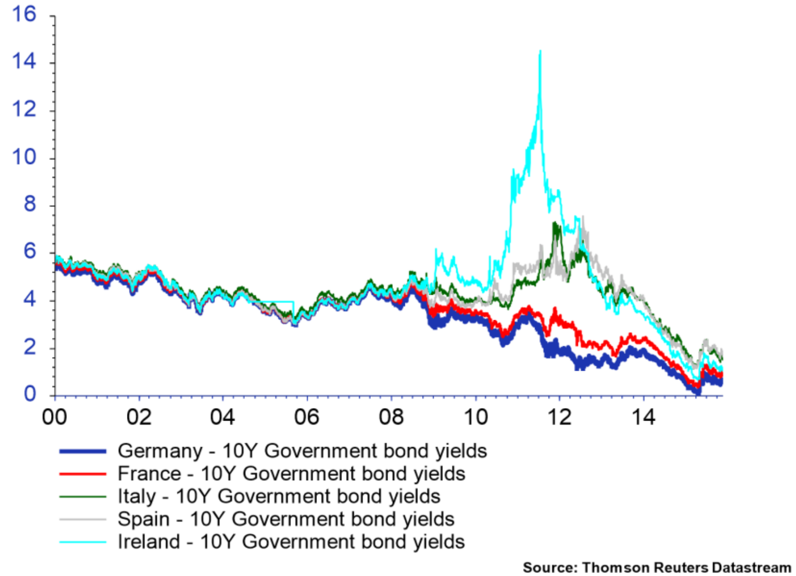


Government Bond Yields (continued)

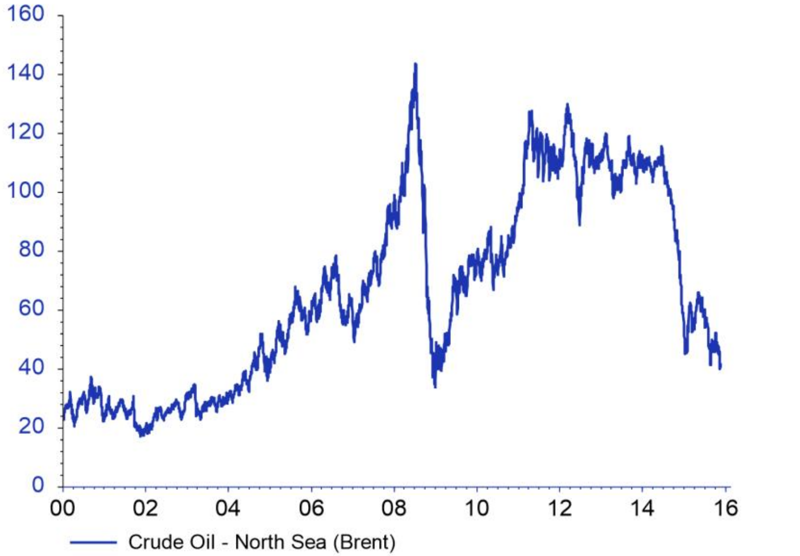




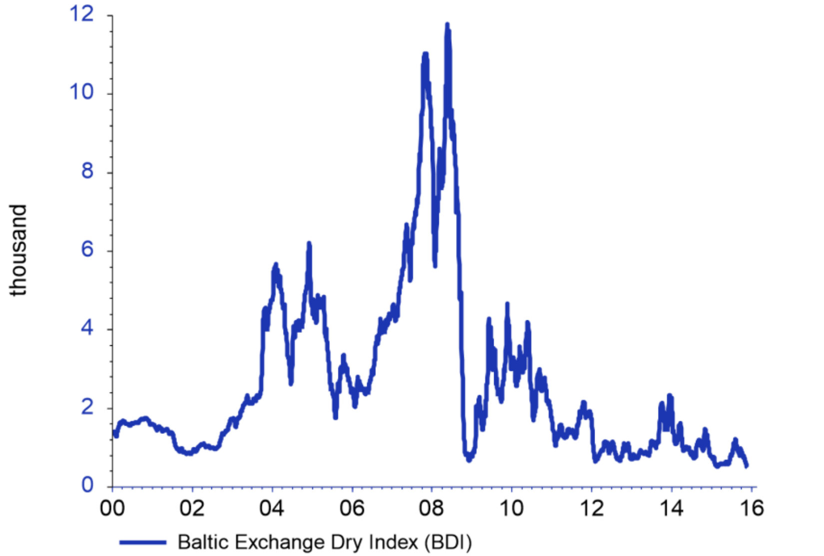




Commodity Markets



Source: Thomson Reuters Datastream



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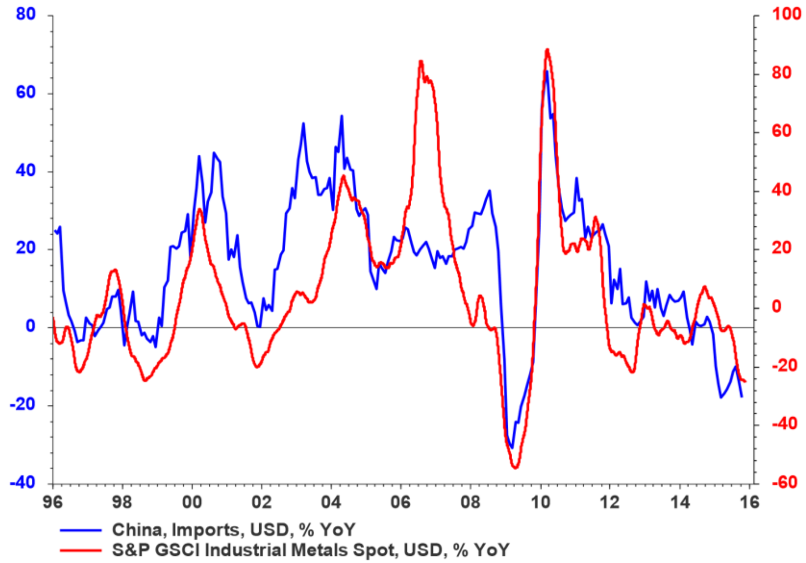
Source: Thomson Reuters Datastream



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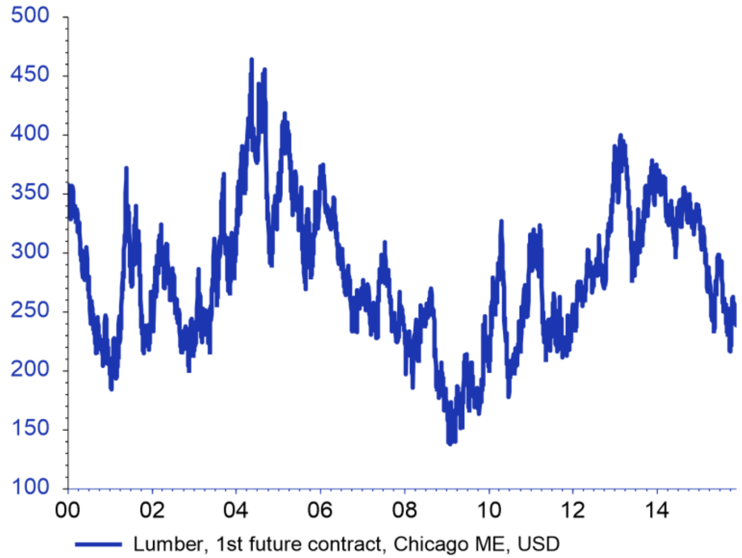
Commodity Markets (continued)



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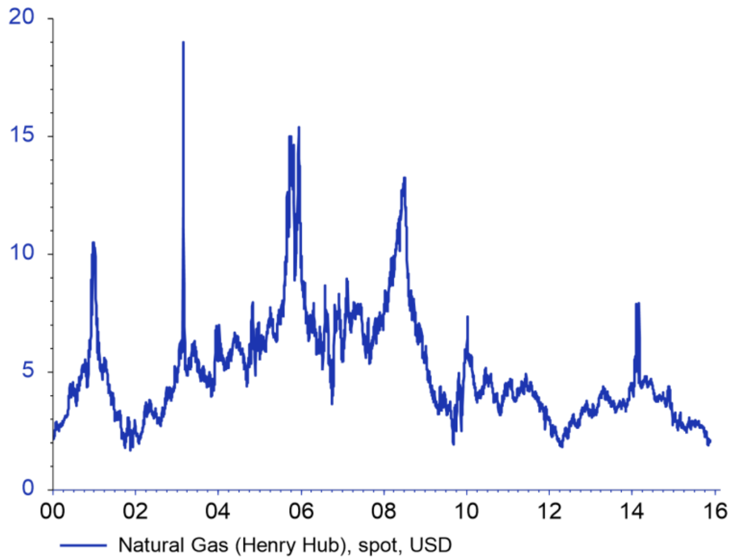

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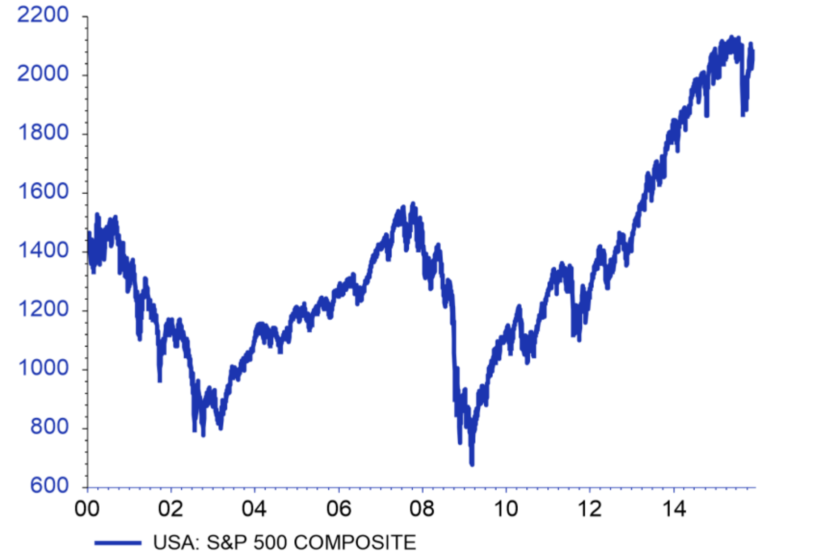
Commodity Markets (continued)

Equity Markets



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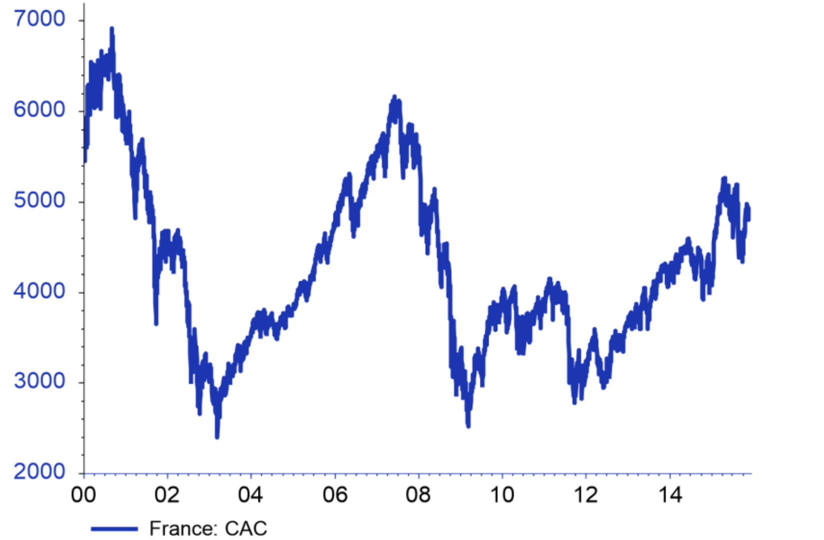

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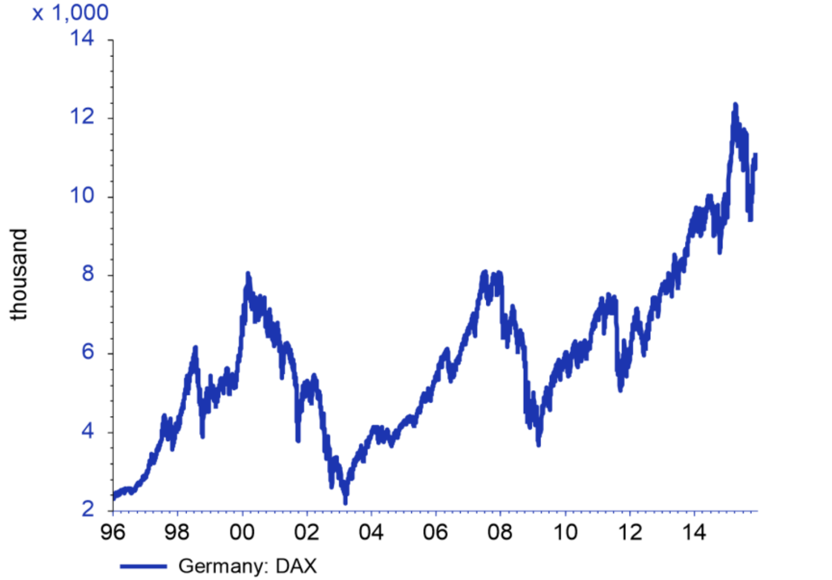

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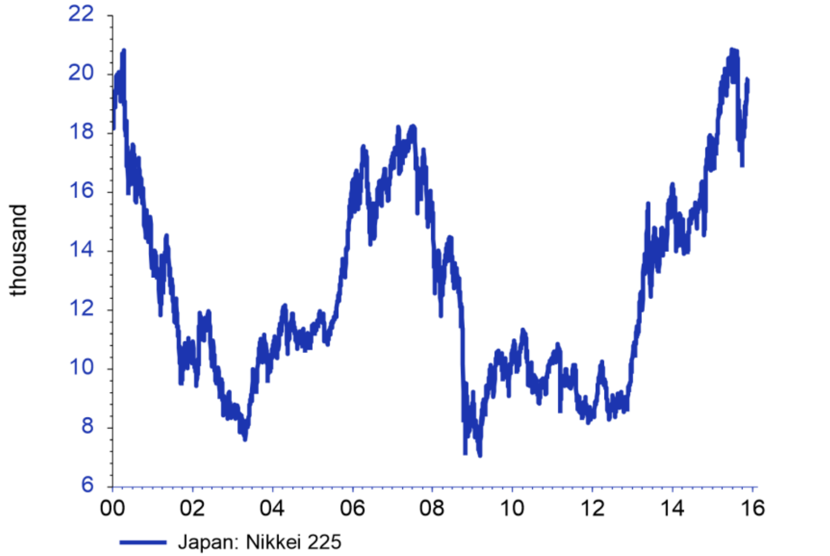

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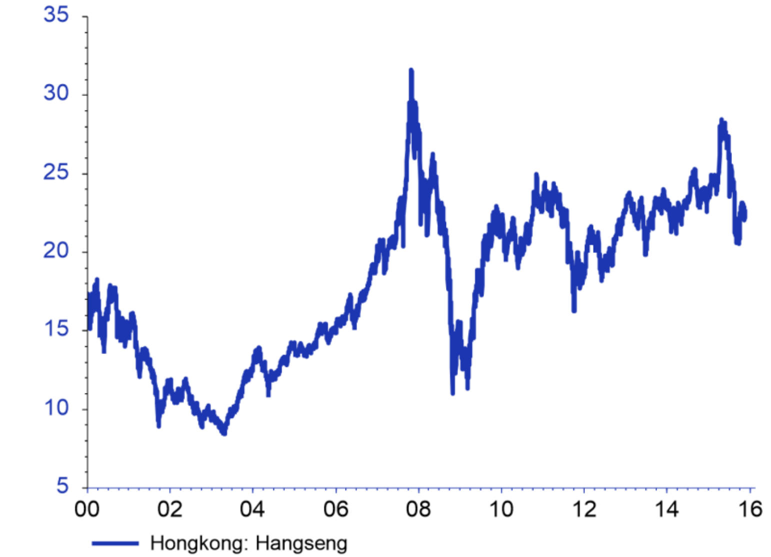
Equity Markets (continued)



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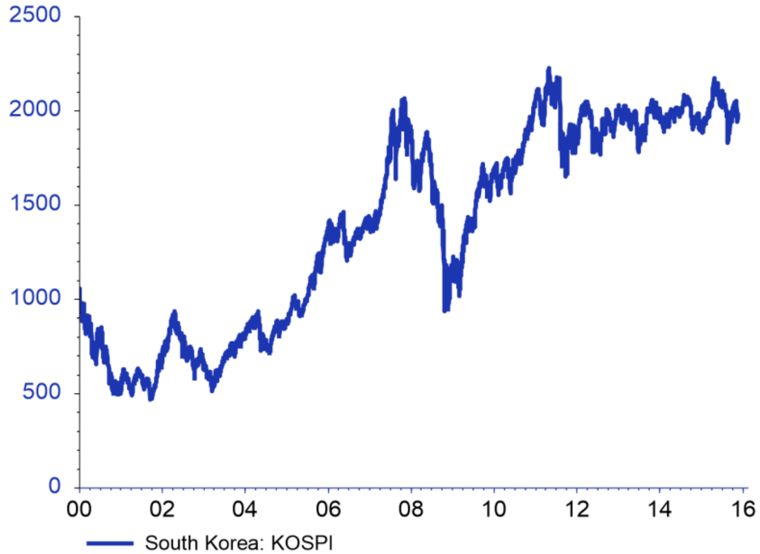

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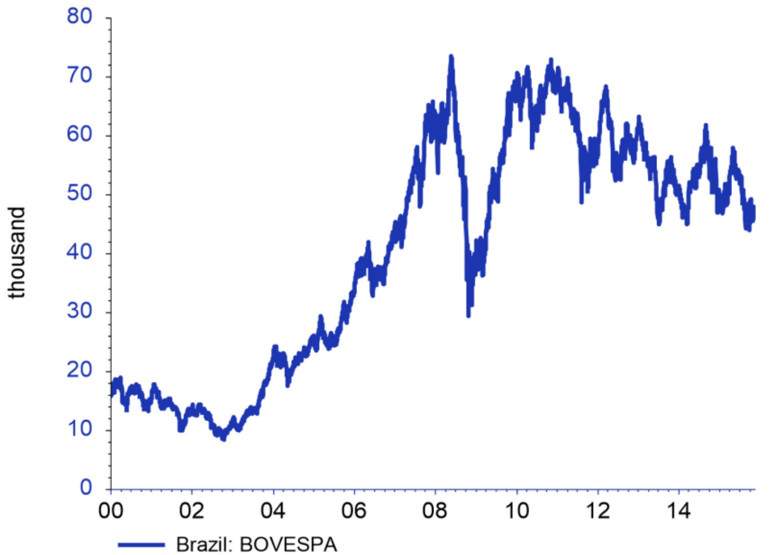

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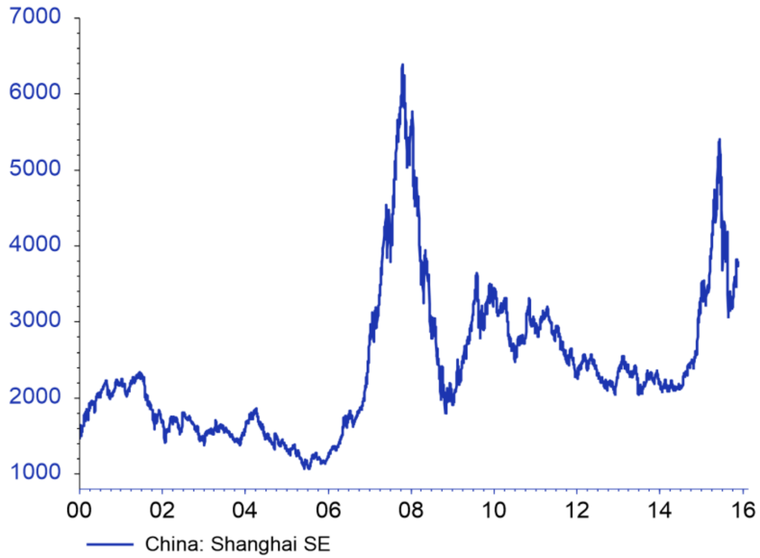

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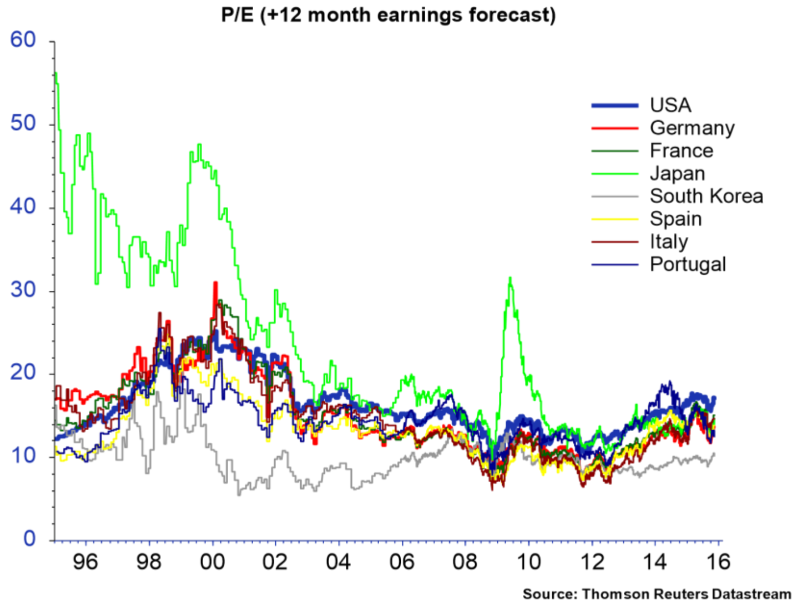
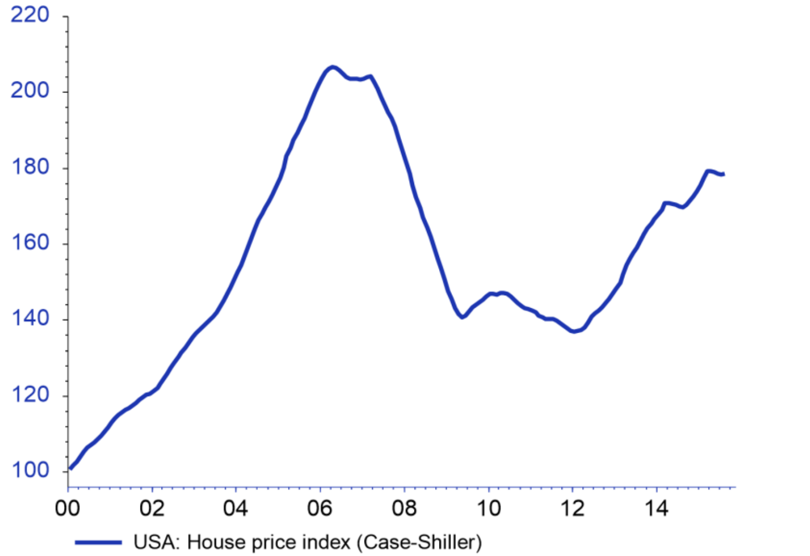
Equity Markets (continued)

Equity Markets - Valuation



Home Prices



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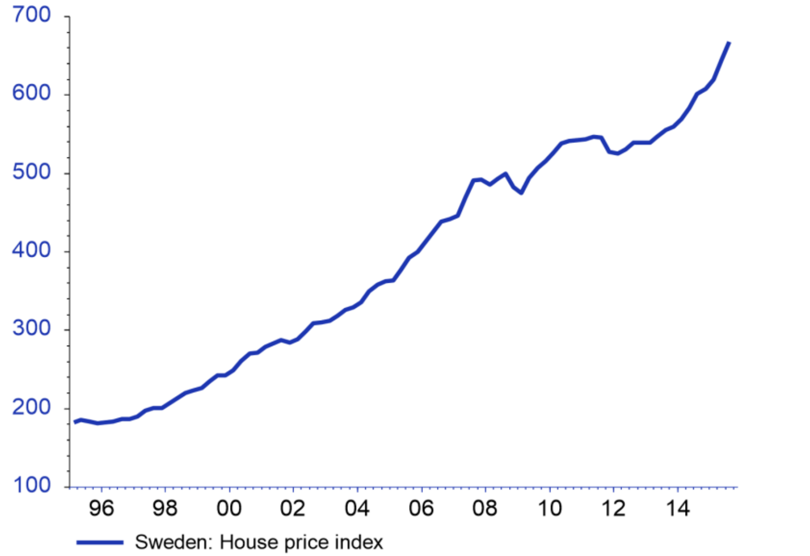

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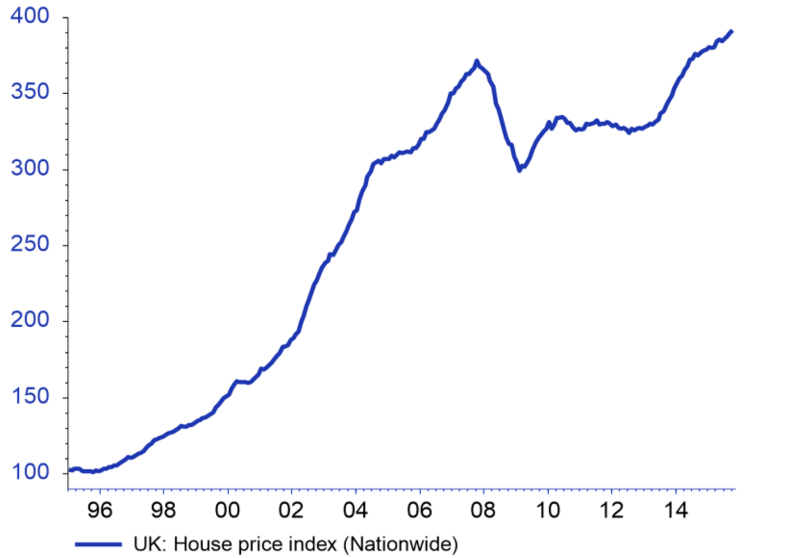

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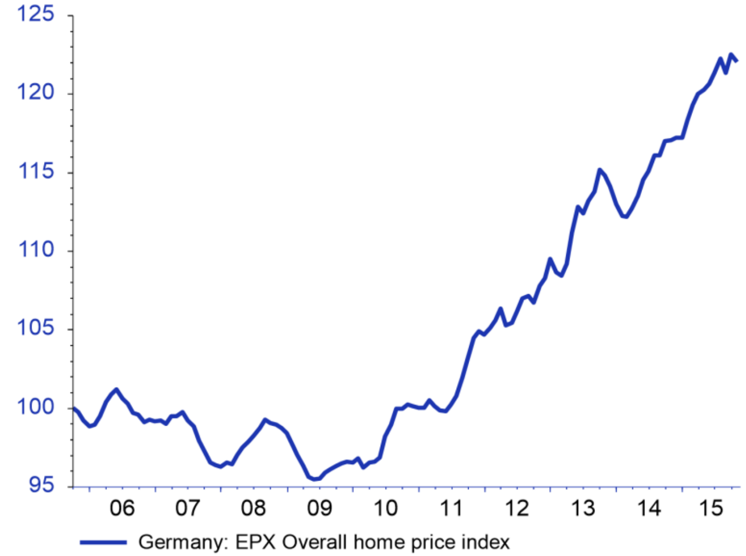
Source: Thomson Reuters Datastream

Home Prices (continued)



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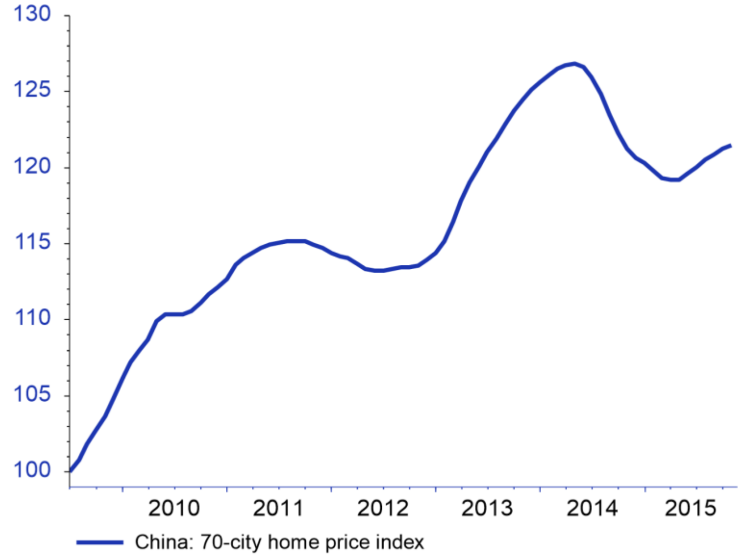

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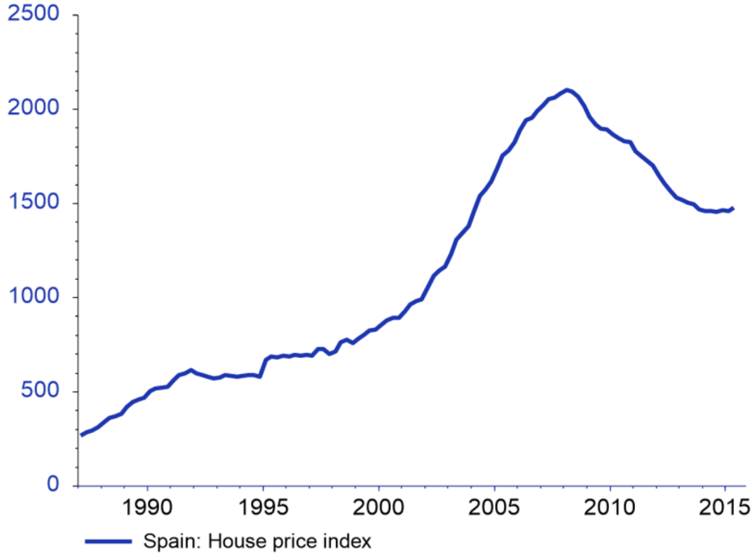

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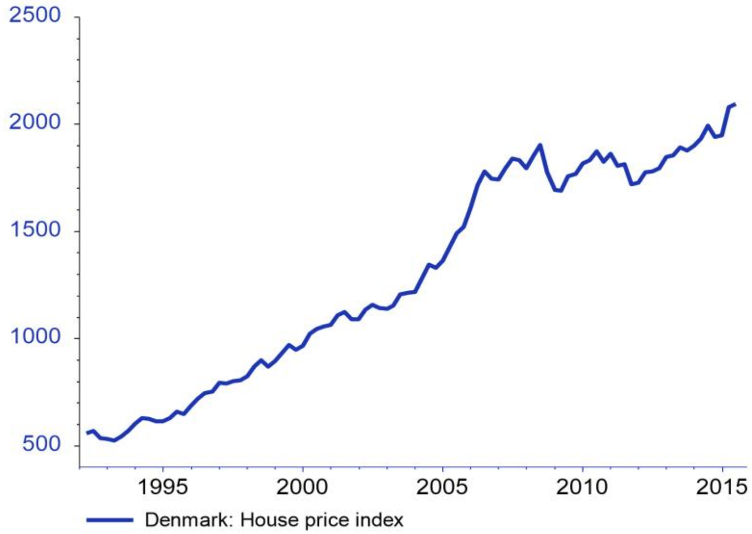

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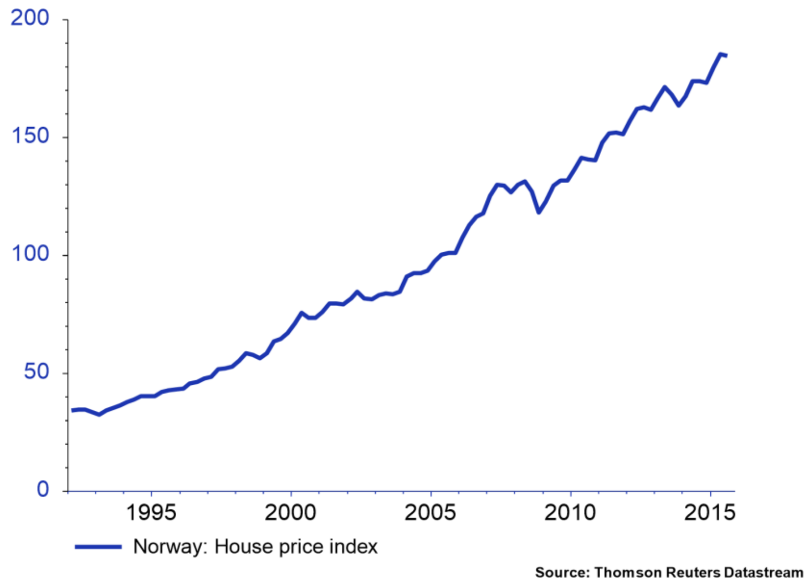
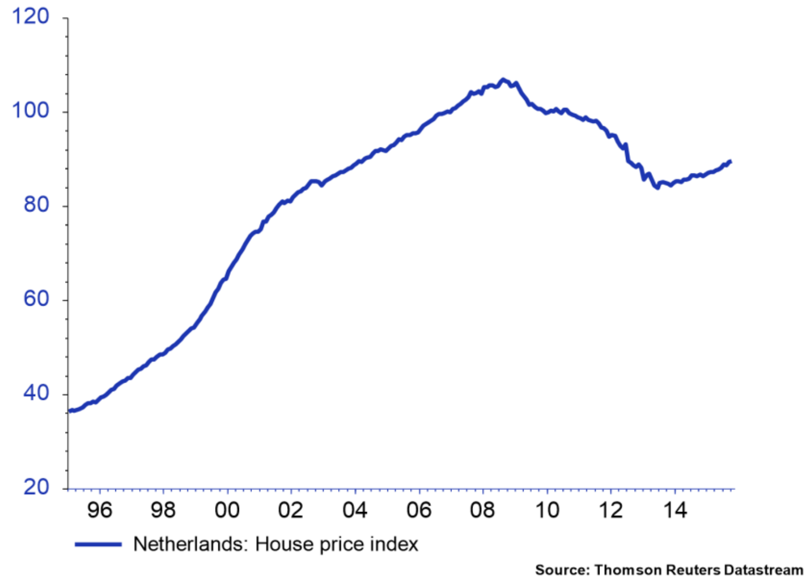
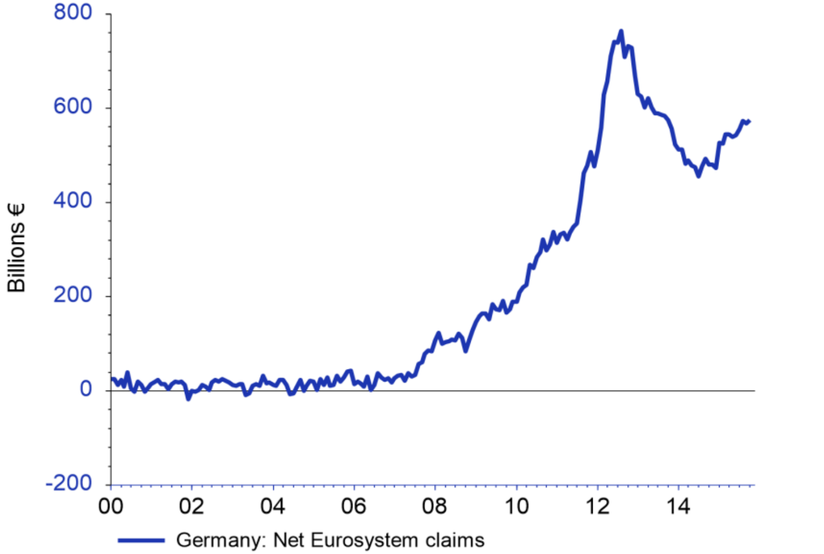
Home Prices (continued)





Euro-zone Crisis



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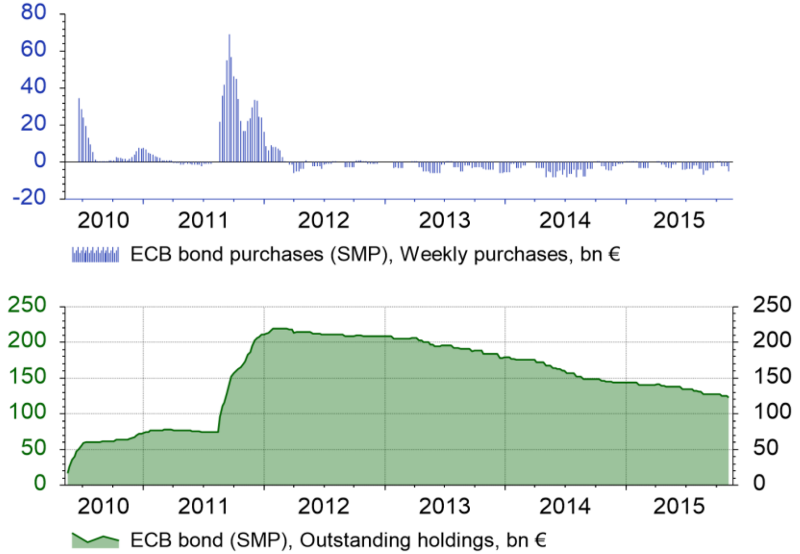

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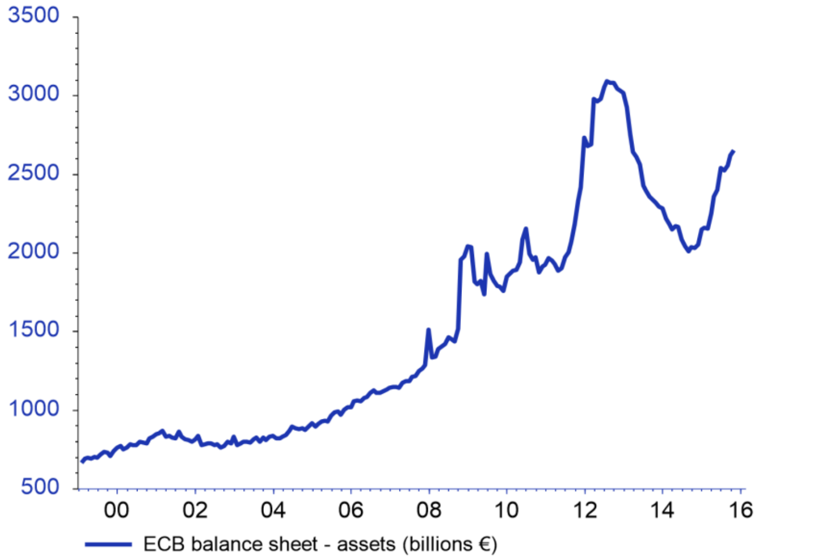

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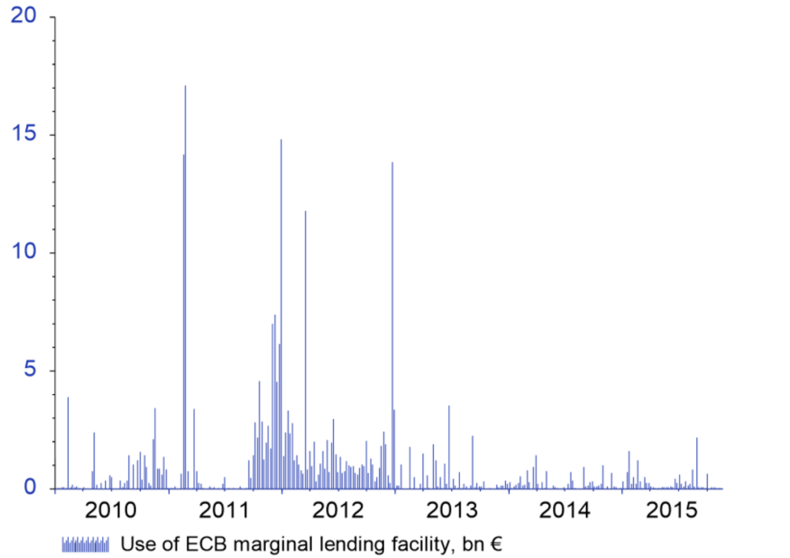

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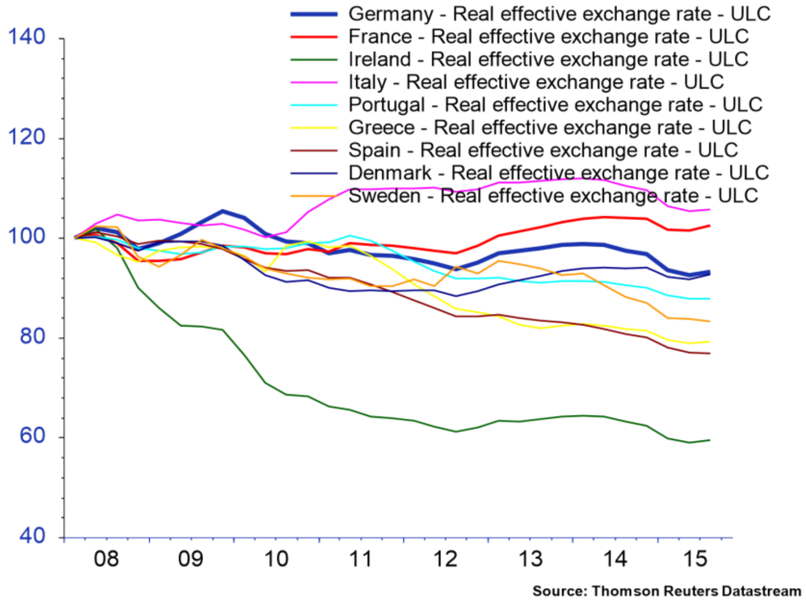
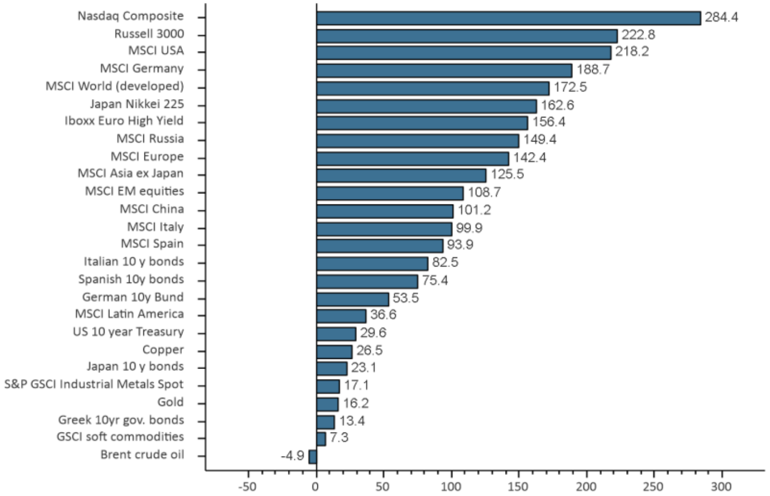
Labour costs



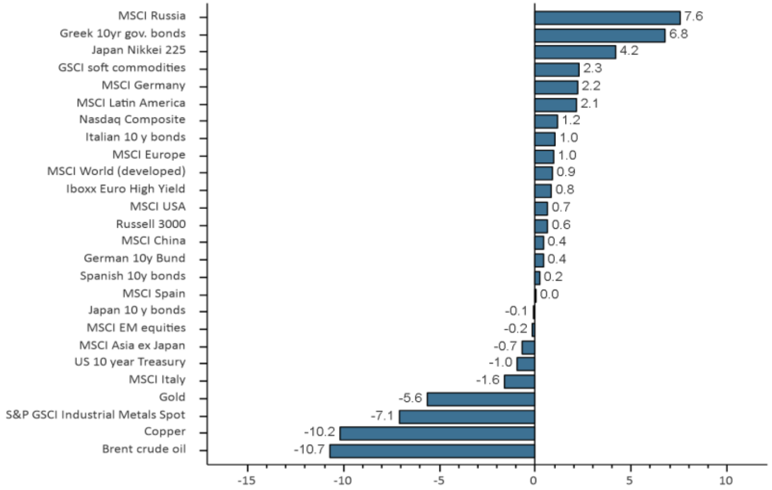
Performance of Asset types (local currency) – last update: November 20, 2015

% Return Index from 15/3/2009 to 18/11/2015



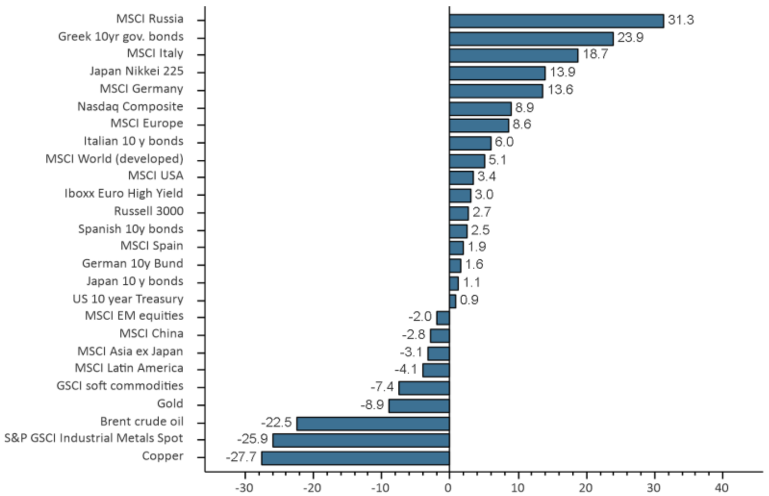
Source: Thomson Reuters Datastream

% Return Index from 30/10/2015 to 20/11/2015



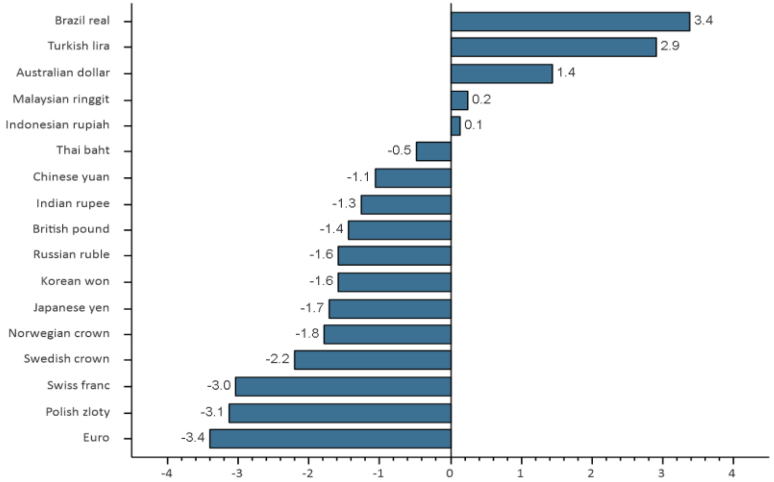
Source: Thomson Reuters Datastream

% Return Index from 31/12/2014 to 20/11/2015



Source: Thomson Reuters Datastream

% Return Index vs USD from 30/10/2015 to 20/11/2015



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