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Global Economic Review
Robin Bew, Economist Intelligence Unit

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As good as it gets?

The good times aren't rolling

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December 2015



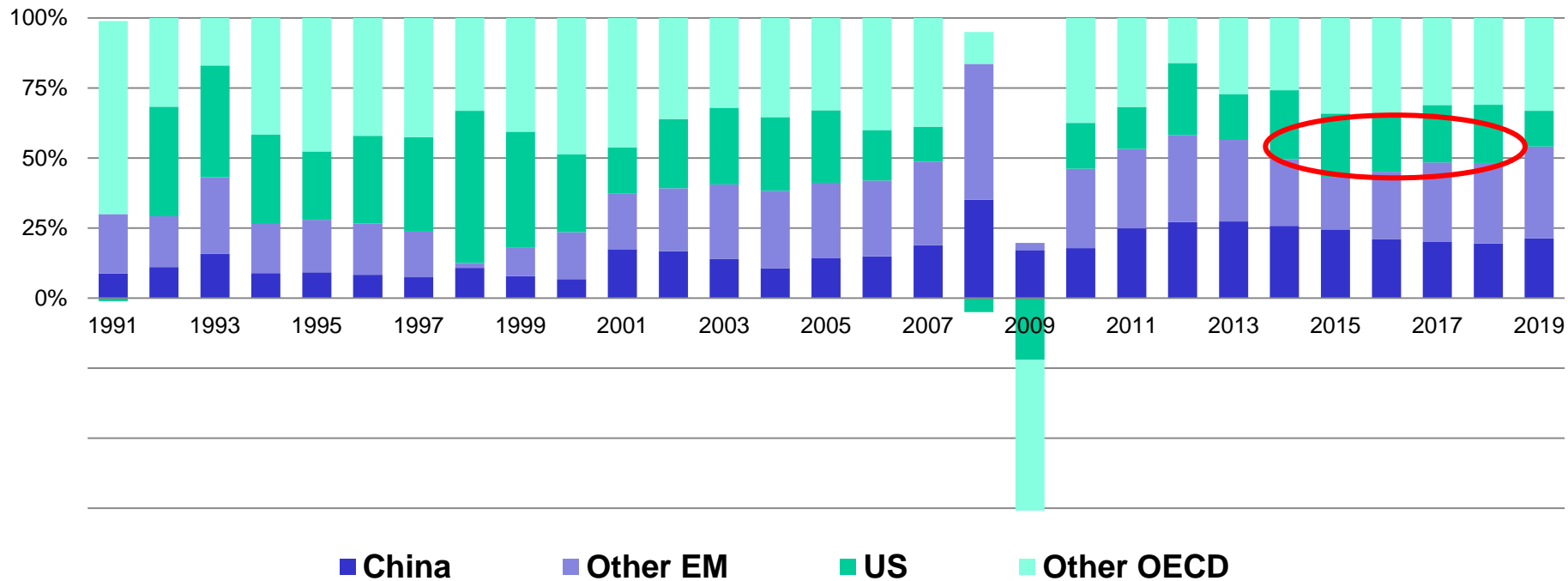
Key points for 2016

- **Developed countries: US economic growth is strong, but uneven**
 - US jobs market is powering ahead
 - Gradual Fed tightening will shape global markets
 - Europe, Japan: still fragile but recovering
- **China: slowing although decent growth, but 30% chance of hard landing**
 - Economy has been softening for some time; will slow even more
 - Growth diversifying; more services, less manufacturing
 - Equity market likely to remain weak
- **Emerging markets under pressure; little good news**
 - Commodity prices very low (but will rise slightly)
 - Volatility amid monetary policy divergence
 - Weak exports and unavoidable economic reform
 - Window of opportunity to use monetary stimulus closing for many



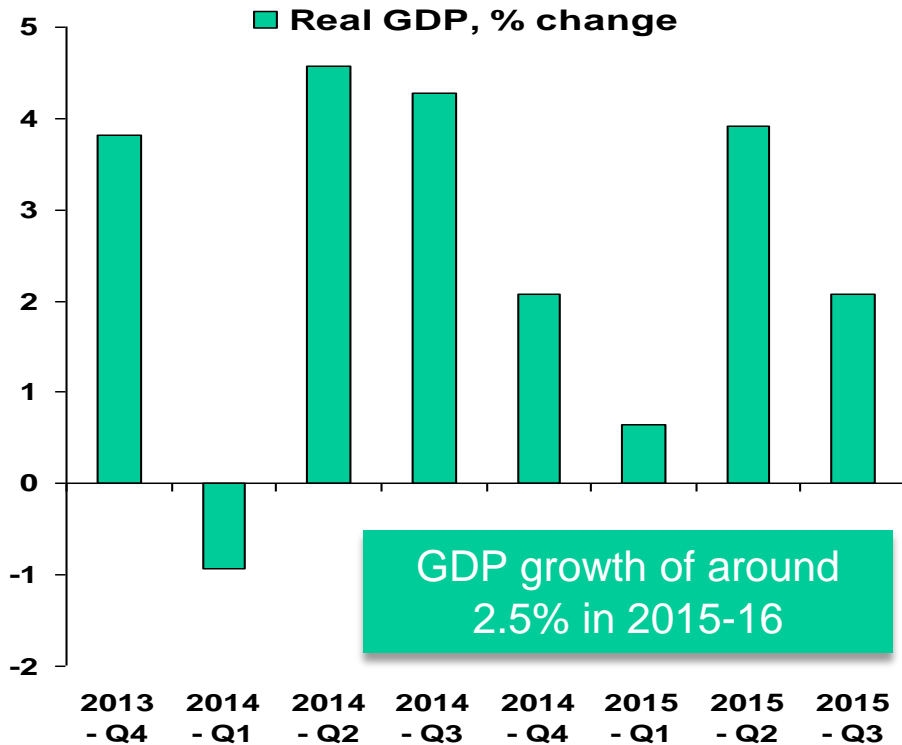
Rich countries shoulder more of the burden

Contribution to global real GDP growth (2005 US\$)



**US: powering the world
economy**

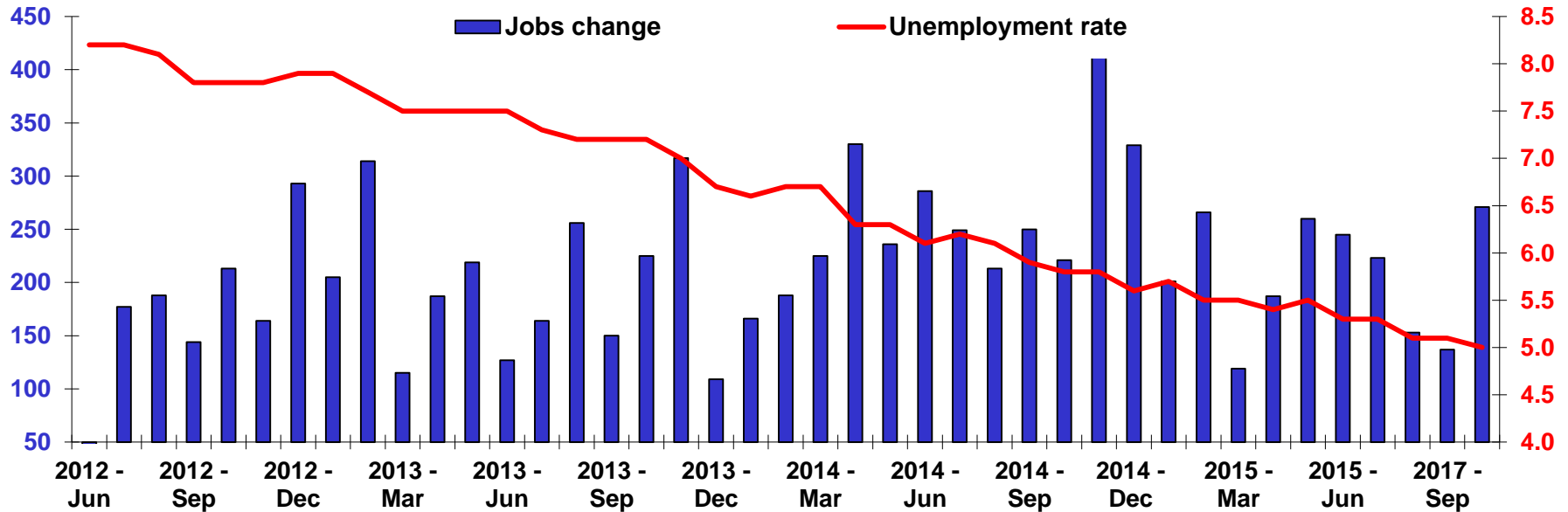
US economy has been strong but erratic



- **US economy unusually volatile**
 - In four of last seven quarters, growth has been around 4%
 - In two other quarters, GDP was flat or contracted
 - Why? Weather, one-off factors, business uncertainty; stats issues
- **Foundations look solid**
 - Jobs market strong, housing improving, energy prices low, consumer spending climbing, investment reviving, debt low
- **Headwinds**
 - Energy sector investment
 - Strong dollar

US: Job growth remains strong

Unemployment steadily falling, despite weak summer



Non-farm payrolls, thousands, monthly net job change.
Unemployment rate, %. Source: Bureau of Labour Statistics

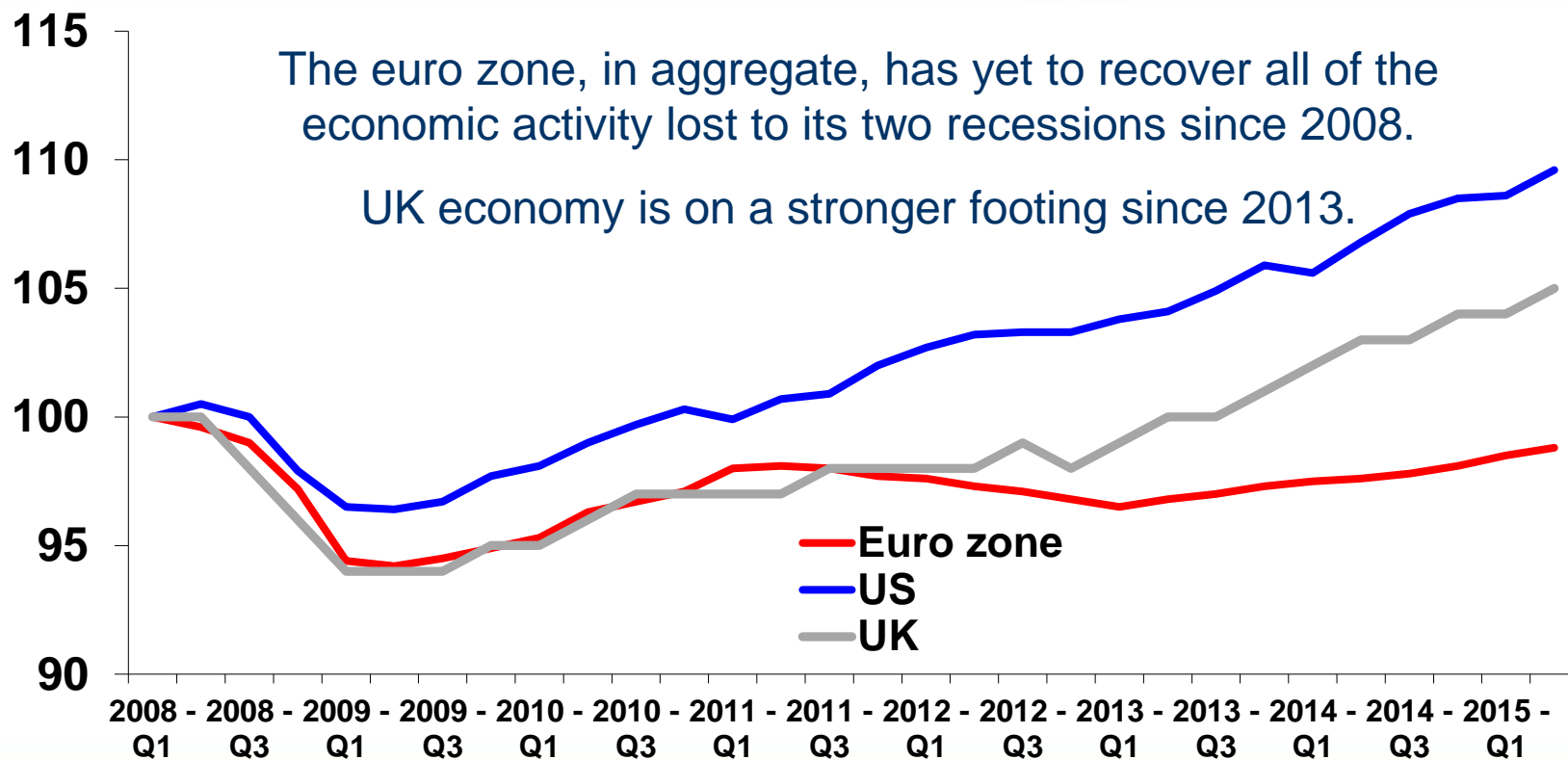
The Fed prepares to remove the punchbowl

- Dithering for months, but rate rise now imminent
 - Repeat of fast 2004-06 tightening cycle unlikely
 - Jobs market flashing but inflation is not
 - Fears of turmoil in global financial markets
 - But some action seems necessary
 - Labour market getting tight
 - Encouraging risky investment
 - Needs to create policy headroom for next crisis
- Watch out for
 - Renewed capital outflows from EMs
 - Further EM currency weakening



**Europe and Japan:
a dreary grind**

Europe: Growth seriously lags the US recovery



Real GDP growth in the US, UK and euro zone. Indexed to January 2008=100.

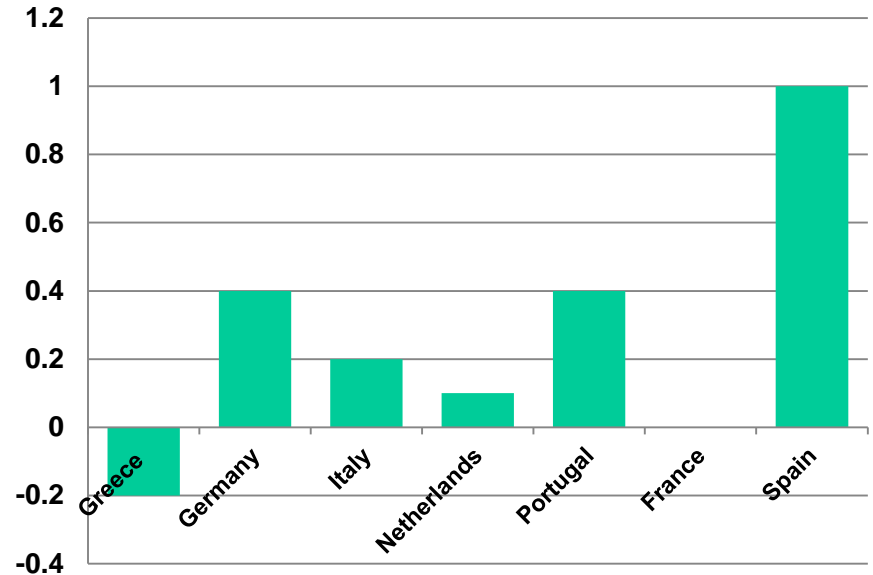
Source: Bureau of Economic Analysis, Eurostat, Haver Analytics.

Some better signs in 2015

- Banks are starting to lend again
- Consumer spending rising, helped by cheaper oil and ECB's QE
- Structural reforms having a positive impact in Spain and Portugal
- More work to do in France and Italy.

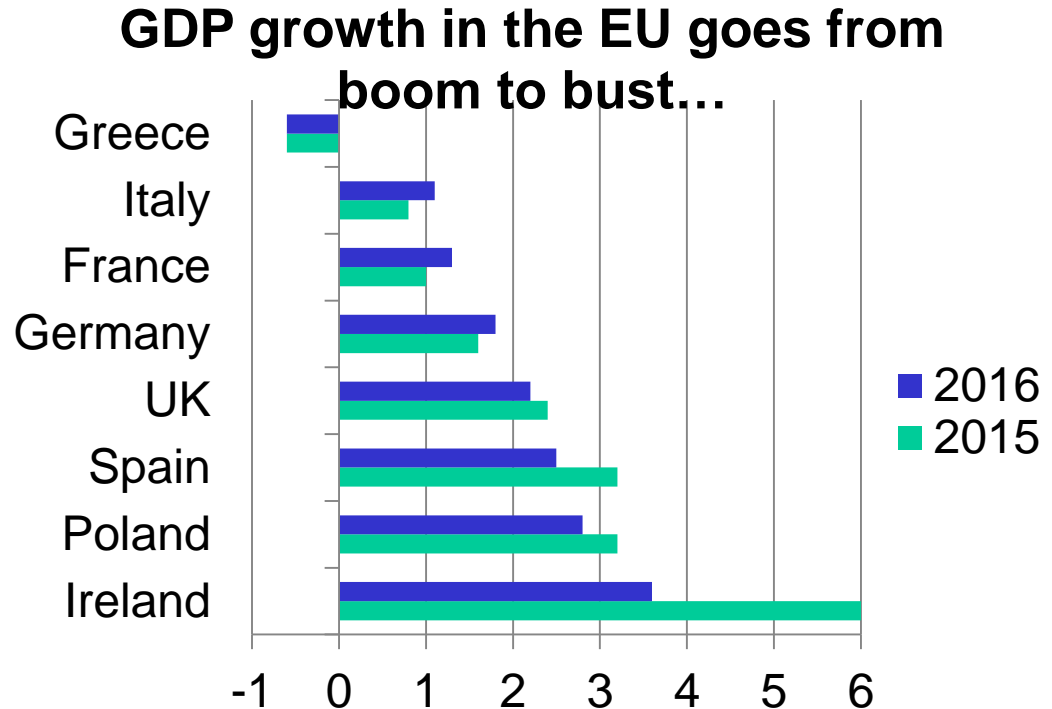
Euro zone GDP growth to pick up from 1.3% in 2015 to 1.6% in 2016

Real GDP (% change, 2nd quarter 2015 q-on-q)



But already clear those aren't going to last

- Long-standing problems
 - Debt overhang
 - Costs of prolonged high unemployment
 - Demographics
 - Productivity
- And no policy options
 - Monetary and fiscal policy have run out of room
 - Structural reform gains far in the future
 - Populism crippling reform efforts
 - Migration hitting EU solidarity

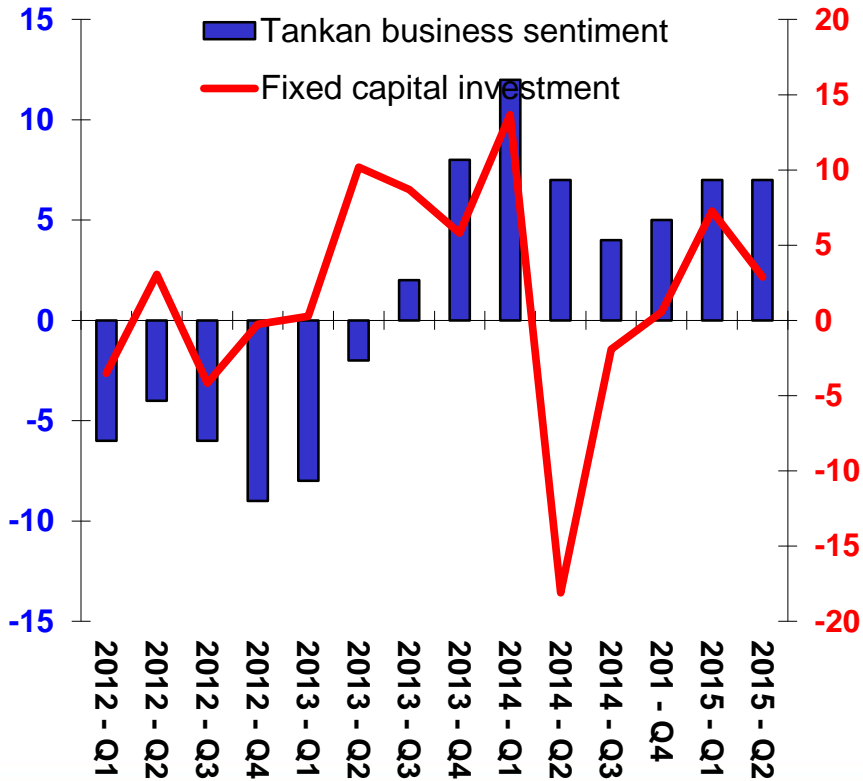


Grexit is a medium-term risk

- Political capital expended means short-term Grexit unlikely
- But domestic politics, fraying ties in the EZ and problems with implementation mean Grexit risk in next five years is still 60%



Japan: modest improvements



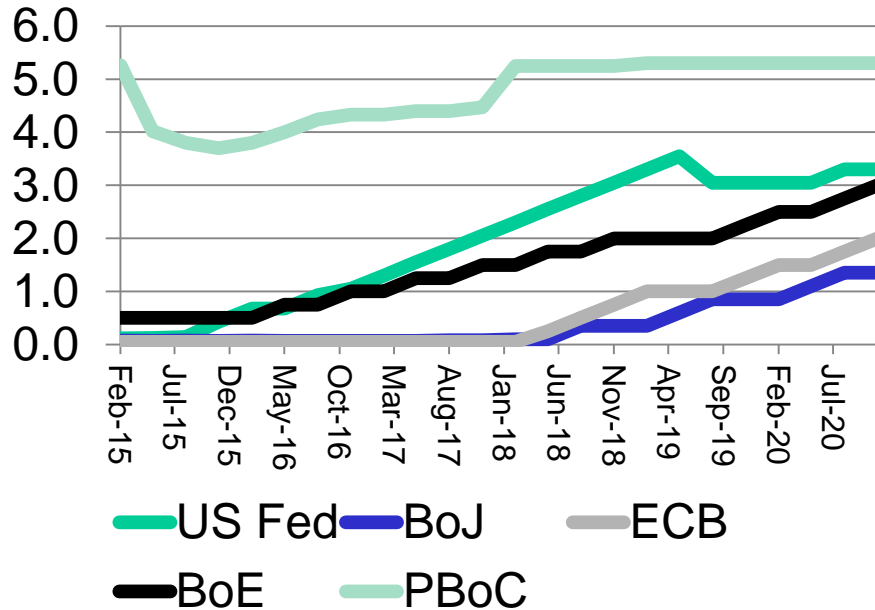
- “Abenomics”— fiscal stimulus, structural reforms, money-printing
- Two key reforms have passed
 - Nuclear restart
 - National security bills
- Monetary and fiscal targets remain elusive
- Sentiment has improved, but economic performance is uneven
- Outlook? Not great
 - Falling population risks perpetual shrinkage of economy

Tankan: diffusion index. Gross fixed capital formation, % change, annual rate.
Source: Tankan business survey, all enterprises; Cabinet office for investment

Policy on the move

Monetary policy in a new normal

Main policy rates (%, year end)

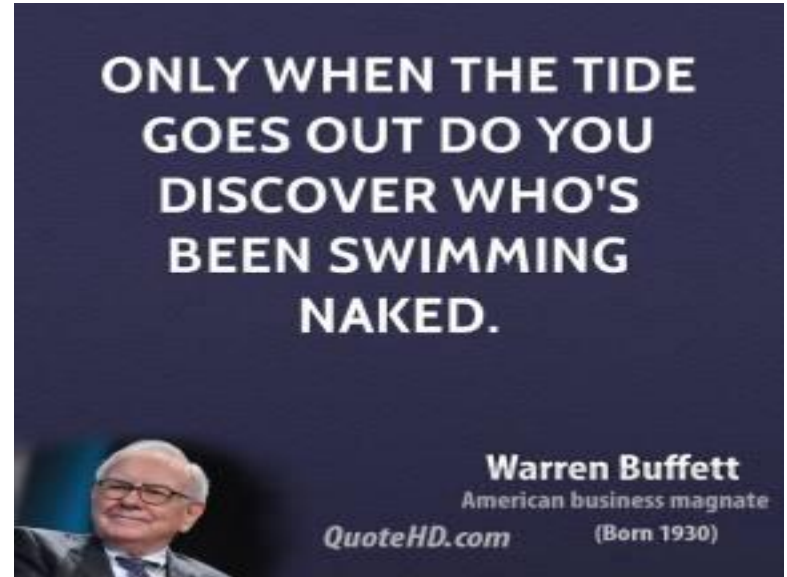


- US Fed about to raise interest rates
 - Policy divergence » volatility
 - Exchange rates
- Brazil, Indonesia, South Africa Turkey again at risk
 - Also Russia, Venezuela, Colombia
 - EM corporate debt
 - But no systemic crisis
- In historic terms, interest rates in developed markets will stay low
- Oil's wild swings will show up in inflation

Emerging world

Not a pretty picture

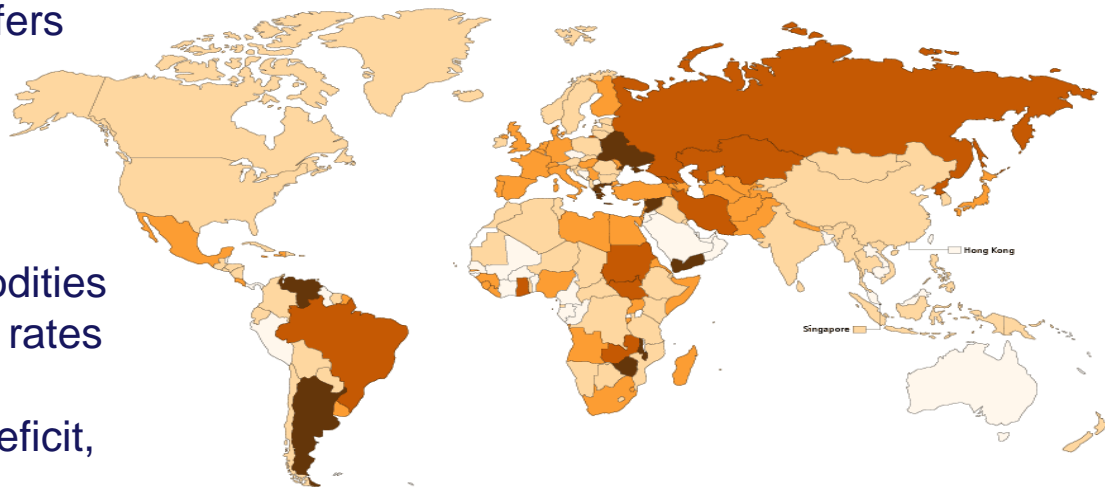
- Not expecting a widespread crisis
- But:
 - China steadily slowing
 - Low commodity prices hurting
 - Higher interest rates squeezing
 - Policy weakness exposed



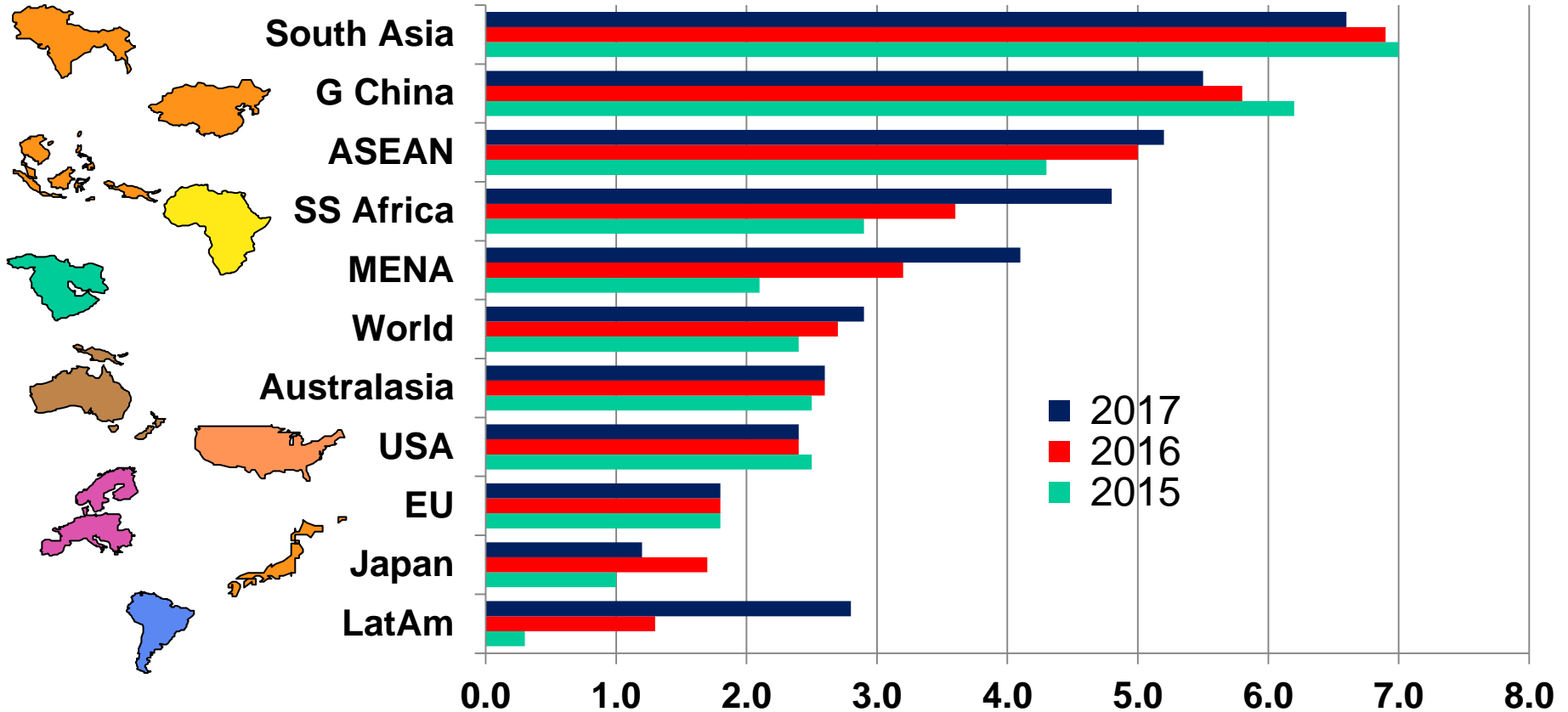
Full-blown EM crisis remains unlikely (<20%)

- Much stronger fundamentals than before Asian crisis:
 - Better external and fiscal buffers
 - Flexible exchange rates
 - Increased CB autonomy
- Determinants of vulnerability:
 - Exposure to China & commodities
 - CB capacity to raise interest rates
 - Political risk
 - Foreign exchange, budget deficit, debt position, CA balance

Macroeconomic risk

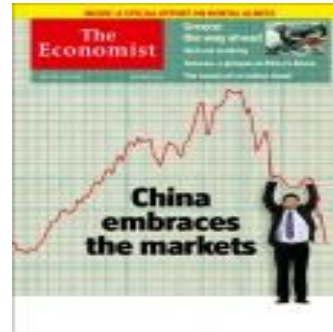


Asia's growth story still a world apart



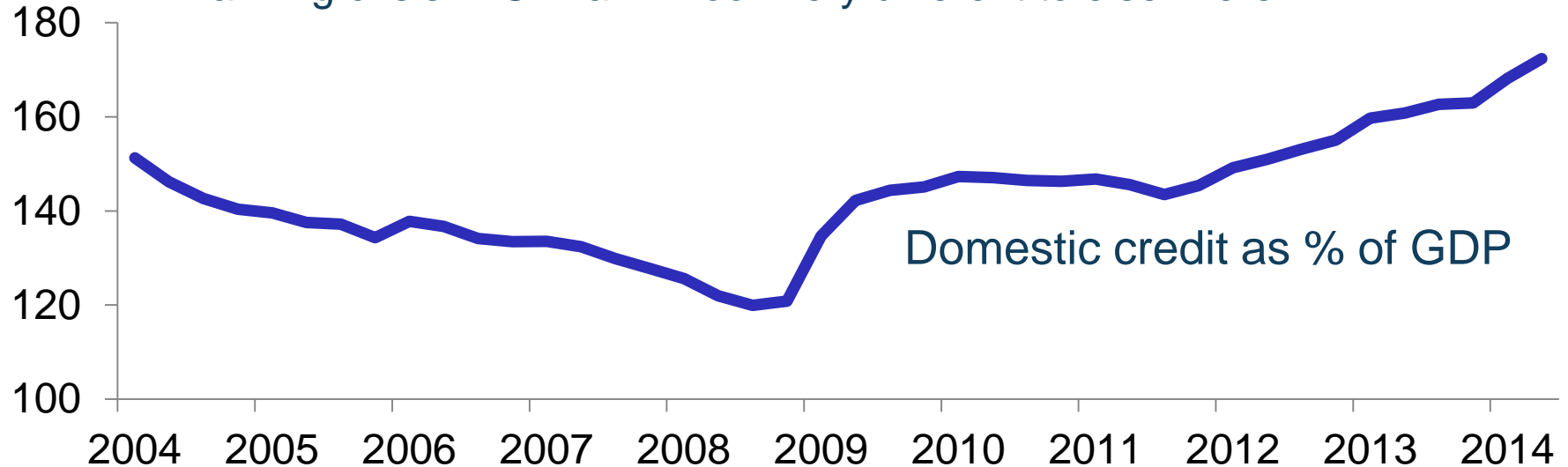
What is going on in China?

- Everyone's personal experience is less than 7% growth
- Stockmarket crash?
- Are reforms on or off?
- What next for the RMB?
- Will capital go in or out if capital account liberalised?
- WATCH: rebound in property market



Monetary easing cannot go on forever

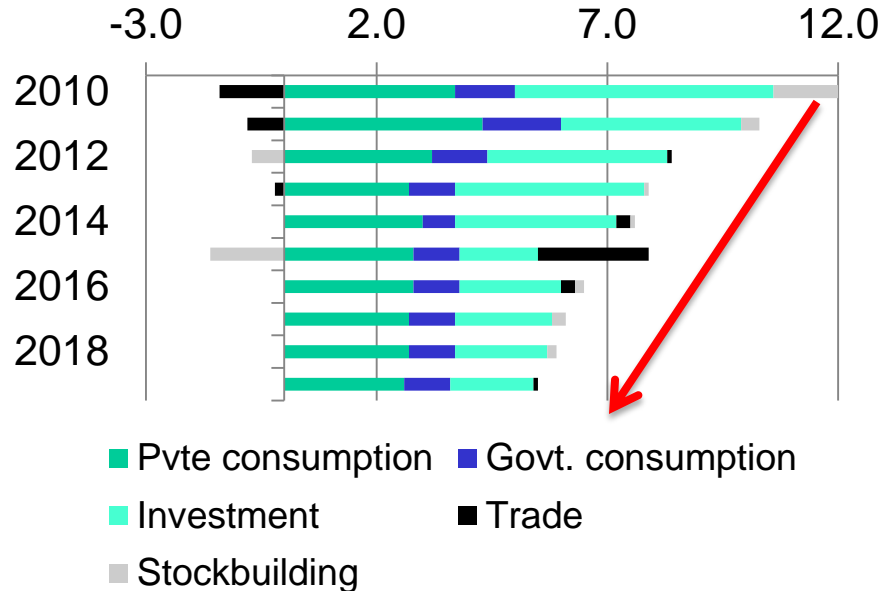
- Monetary and fiscal policy will be used to support growth
- Most run-ups in domestic credit of this scale have ended in difficulties
- Banking crisis in China will look very different to elsewhere



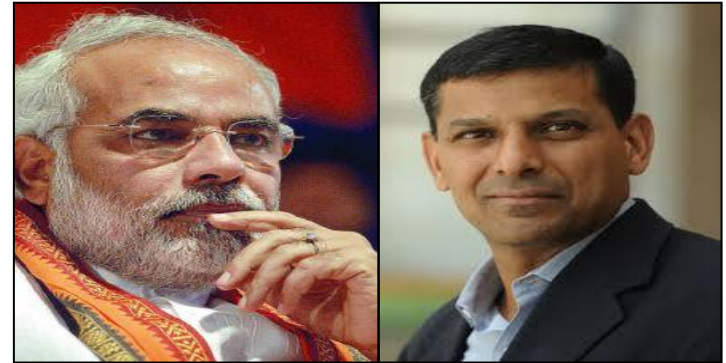
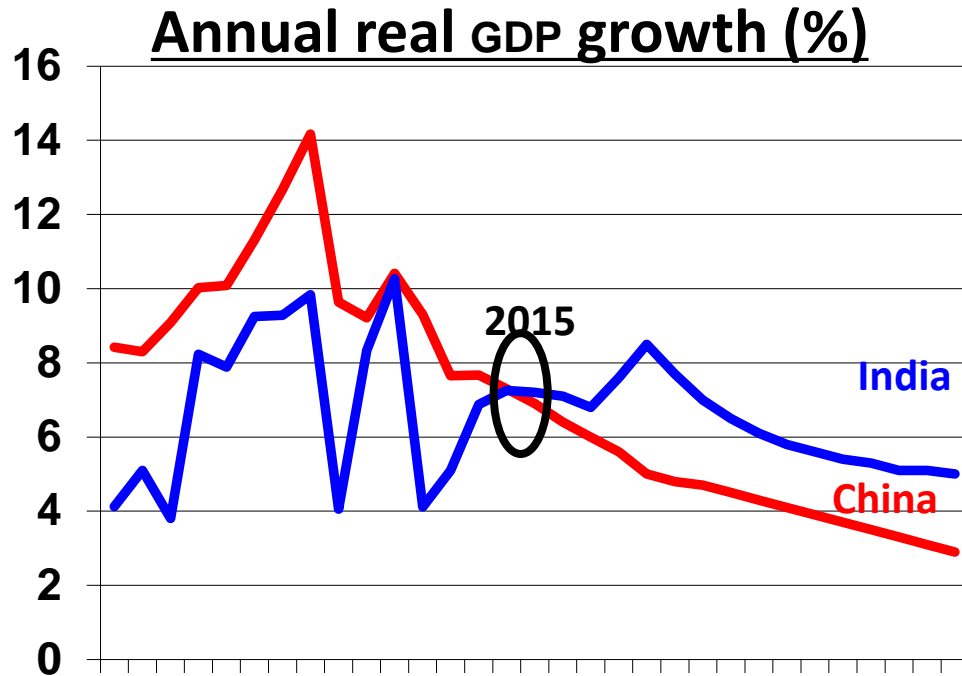
The big picture in China is unchanged

- China is engaged on a transformation of a scale and speed never seen before
 - Another decade to run
- Slowdown is all about investment
- Involves lots of tradeoffs and tensions
- Bumps on the way...both economic and – eventually – political
- Growth tied to finance....and therefore reform

**Contribution to GDP growth
(% points)**



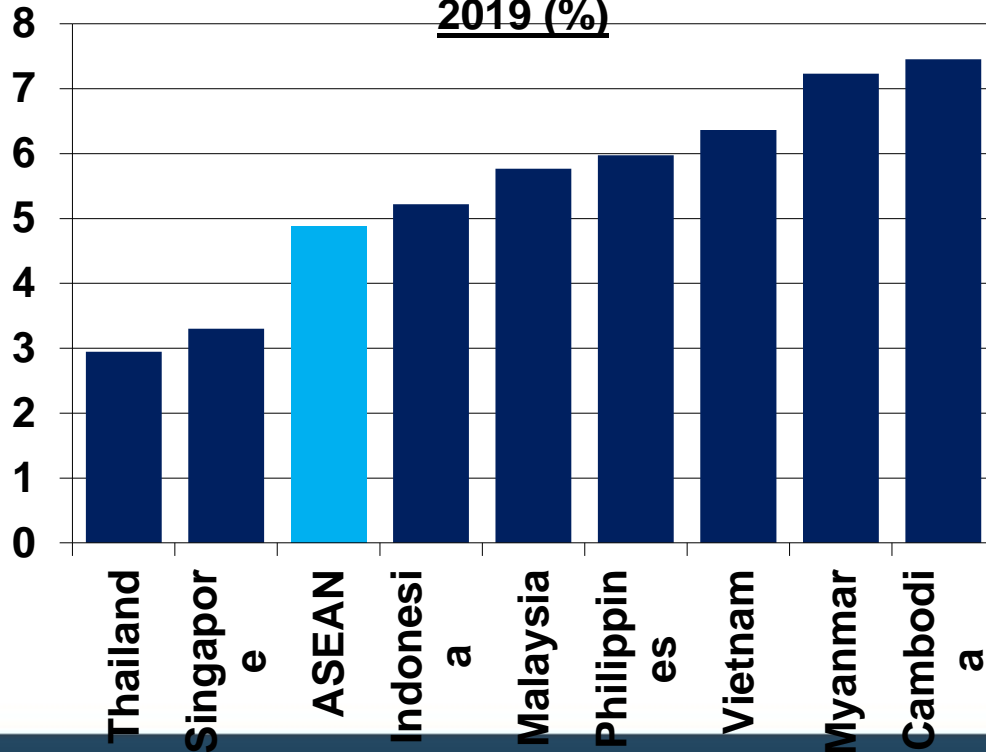
New leaders improve the picture in India



- 7th biggest economy, growing fast
- Rising infrastructure spend
- More pro-business policies
- But below potential: land reform, GST, utilities

ASEAN: A high growth region

Average rate of real annual GDP growth 2014 to 2019 (%)



- Indonesia's rapidly expanding consumer market, but slowing
- ASEAN's export-oriented manufacturing success; e.g. Vietnam's booming electronics exports
- CLMV countries to post rapid growth over next 5 years
- High, stable growth in the Philippines
- Region set to benefit as China, Japan & India seek to gain influence

East Europe

- Russia crippled by sanctions, low oil prices
 - Not much ability to offset through policy
 - Institutions too weak to be effective
- Other CIS countries dragged down
- Central Eastern Europe better
 - Cheaper oil, more credit
 - Also fiscal policy more supportive

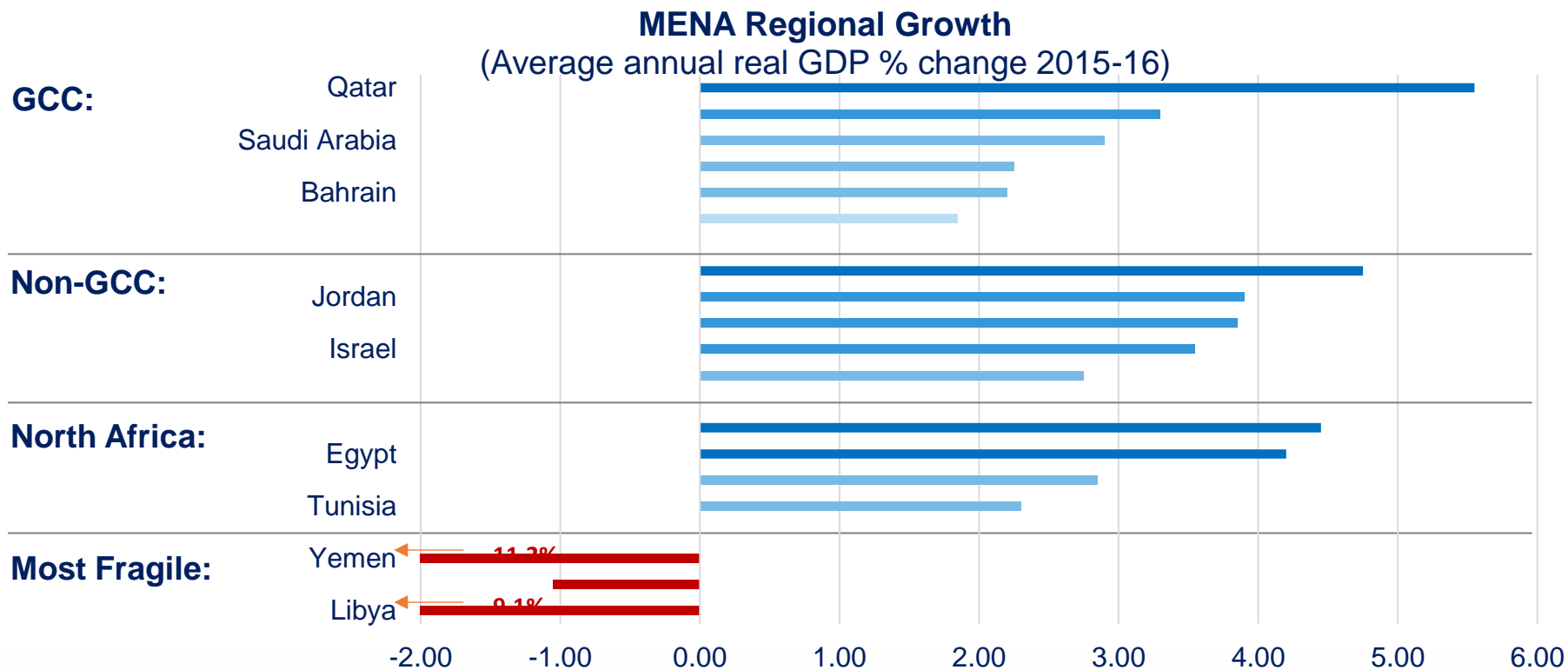


Latin America

- Grim now, and only slowly getting better
 - Poor policy in many markets
 - China weakness
 - Commodity prices
 - Risk aversion in west
- No impeachment in Brazil
 - But no policy either
- Mexico
 - Reforms will work, but will take time
- Argentina
 - Massive to-do list, and most of it short-term damaging



The great Middle East divergence



Iran is opening up for business

Nuclear deal paves the way

- Compromise despite strong objections
- Unease from hardliners in US and Iran
- Sanctions lifted as deal implemented

Transformative effect on economy

- Oil exports to rebound
- Access to overseas assets
- Boost to trade and investment

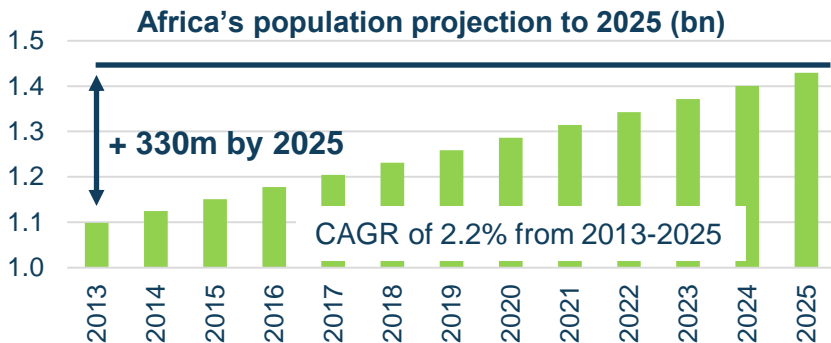
Opportunities across many sectors

- MENA's 2nd largest economy
- US\$400bn (US\$1.8trn at PPP) in 2019
- Economic growth > 5% p.a. 2016-20
- But business environment is challenging

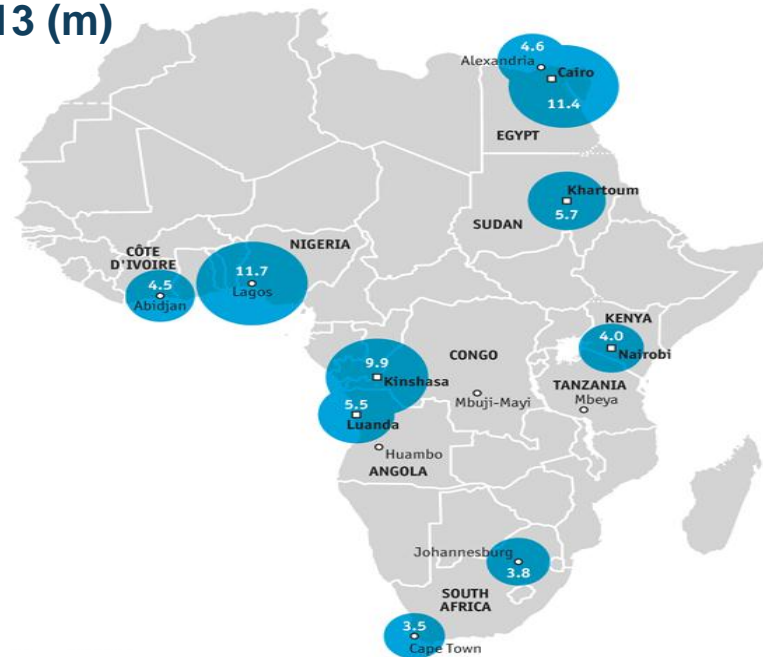


Africa is emerging but long way to go

- The African population will increase by 30% (or 330m people) from 2013 to 2025, taking the population to 1.4bn (or 18% of the global total).
- Urbanisation and income growth will ensure the continued emergence of top tier and second tier cities over the coming decade.
- These changes will boost demand for basic and higher value consumer goods and associated distribution and retail networks.



Population of Africa's ten biggest cities in 2013 (m)

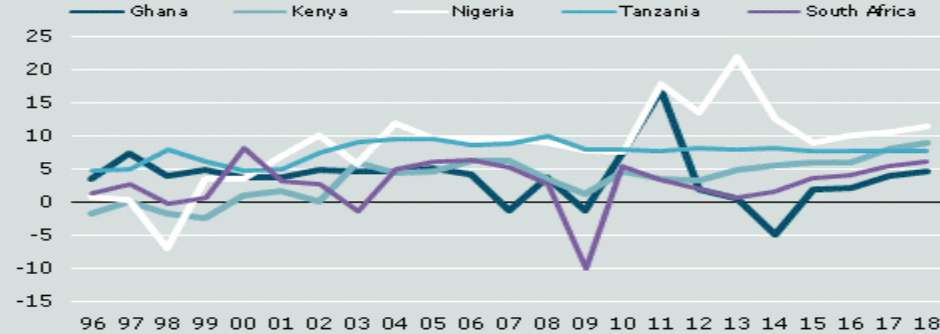


Sources: UN, US Census Bureau; IMF

Can Africa make it as a manufacturing hub?

Manufacturing growth in Sub-Saharan Africa

(% real change pa)



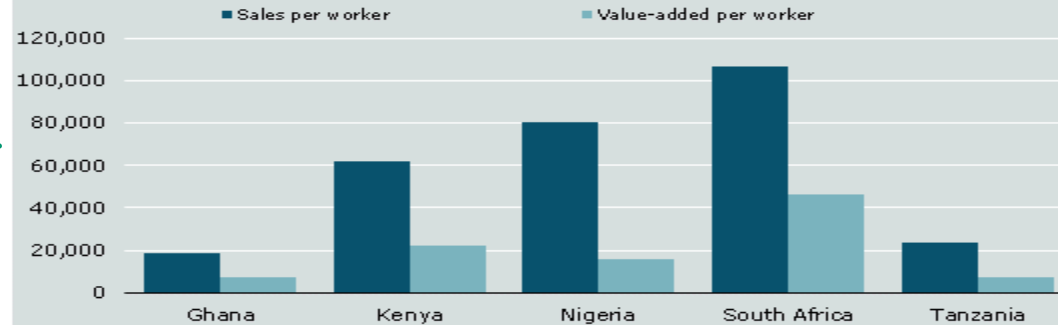
Source: Economist Intelligence Unit.

Manufacturing growth not yet fast enough to cause major transition

Great diversity within Africa, creates opportunity

Manufacturing firm performance in Africa

1996 \$PPP



Source: Baptist and Teal (2014)

What does this mean for you?



What does it mean for education?

- Don't be fooled by slowing growth
 - Incomes and aspirations still rising
 - Many emerging countries still pushing up the value curve
 - China, but also Brazil, Malaysia, Gulf states, Central Eastern Europe etc
 - ▶ Education becoming a vital part of macro-economic strategy
 - Affordability improving
 - What is the need – vocational vs degree
- Cities are where the action is – find the hotspots
- Local vs international
 - Fees, visa negative for UK. But migrant backlash crisis negative for everyone
 - Importance of the broader environment
 - ▶ Education, real estate, financial openness, **work experience**, social experience
- Impact of instability abroad
 - Sadly positive

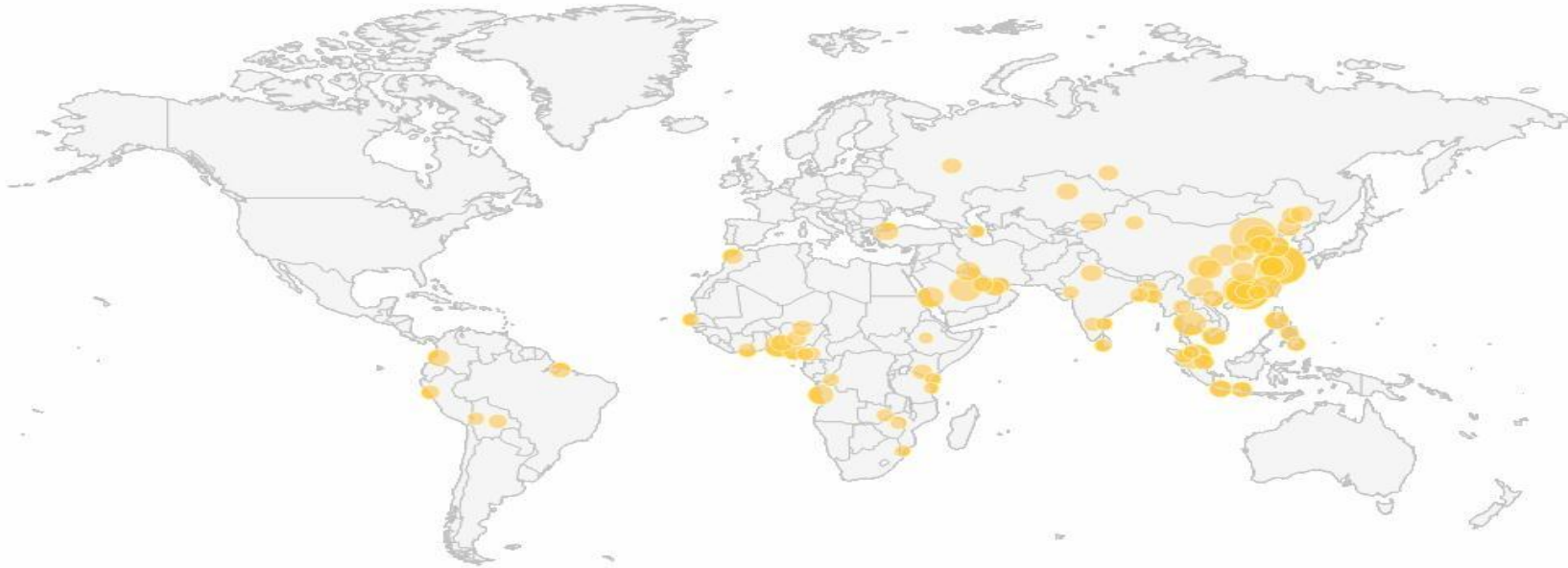
Hotspot cities to watch in 2016

The
Economist

Intelligence
Unit

Canback

Market Explorer



Income over \$20K, growth more than 5%

Questions?

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The map in Robin's presentation, which showed the location of cities around the world with a critical mass of middle income households, comes from a new service the EIU has just launched called Market Explorer. This service covers 200 cities (to be extended to 1,000 cities by April).

If you want more information on the Market Explorer service, you can see more details here: <http://www.eiu.com/market-explorer>

or you can contact peterreardon@eiu.com who manages the EIU's relationships with academic clients.