

Qatar's fiscal balance/GDP set to rise to 4.6% in 2023: FocusEconomics



Qatar's fiscal balance as a percentage of GDP is set to rise to 4.6% in 2023 from an estimated 1.3% this year, FocusEconomics said.

The current account balance (as a percentage of the country's GDP) will be 6.6% in 2023 compared with 6.7% in 2019.

Qatar's merchandise trade balance, FocusEconomics said in its latest economic update, will be \$55.1bn in 2023. This year, it will account for \$46.7bn.

Qatar's gross domestic product is expected to reach \$239bn by 2023, it said. By the year-end, Qatar's GDP may total \$196bn.

Qatar's economic growth in terms of nominal GDP will reach 5.2% in 2023 from 2.3% by the year-end.

The researcher said Qatar's public debt will fall gradually until 2023, and is estimated to be 51.7% this year, 48.4% (in 2020), 45.3% (in 2021), 42.7% (in 2022) and 40% (in 2023).

International reserves may exceed \$43bn in 2023, from the current \$37.7bn; FocusEconomics estimated and noted it will cover 12.1 months of country's imports.

The country's inflation, the report noted, will be 2.1% in 2023 and 0.1% this year.

Qatar's unemployment rate (as a percentage of active population) will remain a meagre 0.2% in 2023, unchanged from this year.

According to FocusEconomics, the economy posted a "modest acceleration" to 0.9% year-on-year growth in the first quarter (Q1) after a "weak" 0.5% out-turn in Q4 last year.

Q1's expansion was driven by the mining and quarrying sector's

return to growth for the first time since Q4, 2017.

Meanwhile, the manufacturing sector also posted a “solid” turnaround.

“The economy should gather momentum this year, driven mainly by a recovery in the energy sector and stronger government consumption growth.

“Consumer prices fell 0.4% in annual terms in June (May -0.7% year-on-year). Going forward, inflation should return later this year on stronger economic activity and a supportive base effect, but remain anaemic nonetheless.”

FocusEconomics panellists expect inflation to average 0.1% in 2019, which is down 0.5 percentage points from last month’s forecast, and 2.3% in 2020.

Alumina market roller coaster spins price to two-year lows



By Andy Home

LONDON, July 30 (Reuters) – The alumina market has collapsed over the last three months with both Chinese and Western prices now at their lowest levels in two years.

The action in China has been particularly brutal. Spot prices surged to a six-month high of 3,170 yuan per tonne in May as production in the province of Shanxi was disrupted by environmental closures.

So violent has been the subsequent sell-off to below 2,500 yuan that producers are now voluntarily cutting output to try to support prices.

Since alumina is the key metallic input to the aluminium smelting process, bombed-out alumina prices are bad news for an aluminium market that is itself treading heavy water right now.

The London Metal Exchange (LME) three-month aluminium price is currently trading just above the \$1,800 per tonne level after touching an 18 month low of \$1,745 in June.

Lower alumina prices serve to lower the aluminium production cost-curve, the break-even point for smelters that helps define the market's downside.

Global smelter profitability is once again beholden to the gyrations of the alumina price with still little evidence that such volatility is being hedged in either the CME Group's or LME's new futures contracts.

THE RETURN OF ALUNORTE

The CME alumina price, tellingly, never reacted to the May spike in the Chinese price but rather kept grinding lower to today's \$305 per tonne, a level last visited in June 2017.

The core driver has been the return of the giant 6.3-million tonne per year capacity Alunorte plant in Brazil.

Alunorte had been operating at half capacity since February 2018 under a court order related to allegations of run-offs from a tailings dam holding the “red mud” generated in the refining process.

Operator Hydro was given clearance to resume full output in May this year and Alunorte was already running at 80-85% capacity in June, the company said in its Q2 results. That should rise to 85-95% in the fourth quarter.

Alunorte’s return closes a supply gap in the Western market which had to be filled by Chinese exports, an unusual occurrence in the alumina market.

Chinese exports mushroomed to 1.5 million tonnes last year from just 56,000 tonnes in 2017.

The tide has since turned. Exports have dropped off sharply and the country has returned to being a net importer since January.

The extra supply is no longer needed thanks to the return of Alunorte, the continuing ramp-up of new capacity by Emirates Global Aluminium and stagnant aluminium production.

Metal output outside of China was down by 0.6% in the first half of 2019, according to the International Aluminium Institute.

CHINESE BOOM AND BUST

Chinese alumina prices have boomed and bust in the space of just three months.

Environmental closures in May, triggered by a “red mud” leak at Xinfu Group’s Jiaokou alumina refinery in Shanxi, spooked the local supply chain.

Any impact from those closures, however, has been fleeting. National output dipped appreciably in May but has since

bounced back to 6.41 million tonnes in June, the highest monthly run-rate since May 2017.

Cumulative alumina output rose by 3% in the first half of the year and with China's own aluminium production also flat-lining this year, analysts at Morgan Stanley calculate a 200,000-300,000 tonne surplus in the country. ("Stopping alumina's slide", July 29, 2019).

Previous fears of a supply shortfall have been rapidly dialled back and spot prices are now at a level where higher-cost producers in northern regions are suffering "serious losses", according to Antaike, the research arm of the China Nonferrous Metals Industry Association.

Producers have announced a collective temporary curtailment of 1.5 million tonnes, Antaike says.

As ever with such coordinated announcements by Chinese producers, there's an element of window-dressing previously scheduled maintenance work, but the real significance is what it says about the margin pain occasioned by falling prices.

Higher-cost producers have in the past been able collectively to support prices around \$300 per tonne but with alumina's own input costs falling, it remains to be seen how disciplined supply will be this time around.

There is growing speculation among analysts that China's alumina sector is heading for the same sort of structural reform treatment already imposed on the smelter segment of the production chain.

That might be a source of long-term support to the alumina price but for now it's down to whether Chinese producers can curtail output sufficiently to balance the domestic market.

RIDING THE ROLLER COASTER

Alumina has been on a high-tempo, high-volatility price trajectory over the last couple of years.

It was above \$600 per tonne as recently as September 2018 before crashing to its current producer pain levels.

The price of alumina was once linked to that of aluminium. Producers embraced spot trading several years ago, arguing that alumina supply-demand fundamentals were different from those of the metallic product.

They have turned out to be right, although not perhaps in the way they imagined. Alumina has turned out to be a much more volatile package of drivers than aluminium.

What's curious is that all this volatility hasn't inspired much interest in using the paper market to hedge price risk.

The LME's newly-launched alumina contract didn't trade at all through June. CME's contract, which started trading in 2016, has seen only sporadic volumes since inception. Activity this year has almost totally dried up with just 240 contracts traded in January-June.

The Shanghai Futures Exchange (ShFE) is undeterred and has promised its own contract later this year.

It's possible that last year's high prices actively deterred producer hedging interest but with the outlook increasingly bearish, that might change.

ADVERTISEMENT

Morgan Stanley sees "near term price support around \$300 per tonne, with risk to the downside".

However, given the excitement of the last two years, you wouldn't bet against a few more spins of what Antaike calls

the alumina “roller coaster”.

(\$1 = 6.8876 yuan)

Centrica CEO to quit after first dividend cut in years



Bloomberg/London

Centrica said its chief executive officer will step down after a tumultuous five-year run at Britain's largest energy supplier, which has lost two-thirds of its value and millions of customers during his term.

Iain Conn, 56, announced his departure along with Centrica's first dividend cut since 2015. He will leave the board in 2020 after he finishes an effort to fortify the utility against increasing competition and a government cap on what it can charge for its electricity and natural gas.

Centrica shares fell as much as 13% in London to the lowest

since 1997, the year the utility was spun out of the state-owned British Gas. Conn inherited a company that had under his predecessors diversified into oil and gas production and nuclear energy, businesses that Centrica now intends to sell. In more recent years, smaller rivals have lured away tens of thousands of customers from Britain's Big Six utilities. Centrica earnings were also hit in the first half as warm weather and operational issues cut its electricity supply by 4%.

Conn said his departure was a mutual decision with the board and the result of months of discussions. Conn is seeking to hand over a smaller entity focused on customer-facing businesses supplying power and energy services. The board will name a successor later.

While the company's share price plunged to new lows, Conn said the company was on the right track and seeing the beginning of stabilisation. He said the earnings outlook is brighter for the rest of the year.

"This set of steps is a fundamental re-positioning of the company and is the end of a journey we began in 2015," Conn said on a call with reporters yesterday. "We haven't changed our strategy. We've made some adjustments, but the board has confirmed we need to keep going toward the customer."

Unions were quick to criticise Conn's plan to maintain the pace of job cuts he announced in February and step up a cost savings target.

Centrica is targeting £1bn (\$1.2bn) of annual cost savings from this year through 2022, up by £250mn since February. The company maintained its estimate that it will shed 1,500 to 2,000 jobs this year from the some 30,520 it had at the end of 2018. "More of the same, more job cuts on top of the thousands already gone and going, are panic measures, not a credible plan for recovery," said Justin Bowden, national secretary of the GMB union. "There must be a pause under a new CEO, investment and a new plan for growth."

The board proposed an interim dividend of 1.5 pence a share,

down from 3.6 pence for the same period a year ago. For the full year, the dividend will be cut to 5 pence a share, down from 12 pence in the last four years.

"The departure of Centrica's CEO won't resolve all of its problems, in our view, as many are outside management's control," Elchin Mammadov, analyst at Bloomberg Intelligence, wrote in a note. "The new team at the helm will need to focus on delivering further cost cuts and growth in energy supply and services."

Customer numbers in Centrica's main energy supply and services business fell 2% to 23.6mn in the first half of the year. Output from its 20% stake in Britain's nuclear plants fell 19% in the first half to 4.9 terawatt-hours, reflecting outages at the Dungeness B and Hunterston B power stations.

"Centrica faced an exceptionally challenging environment in the first half of 2019, which impacted earnings and cash flows," Conn said in a statement yesterday. "This major refocusing of our portfolio will unlock further efficiencies enabling us to be even more cost-competitive, as we focus on being a leading energy services and solutions provider." Looking Ahead Conn maintained guidance for full year earnings. Nuclear plant outages that hit earnings in the first half are likely to pass, and cost savings set to kick in.

Centrica expects growth in its consumer businesses. In its connected homes business, growth accelerated 49% to 1.5mn.

In the months ahead, Centrica will work on selling its Spirit Energy unit, which produces oil and natural gas. It's already divesting its stake in nuclear power plants, although the statement yesterday said nothing new about that process. Conn said Centrica will exit Spirit via a trade sale and use proceeds to restructure the company.

"We are completing the shift we began in 2015 from a company ill-equipped to deal with changes in the energy systems to one in tune with moving toward a lower-carbon economy," Conn said. "Once we've made them, it is now time for me to hand over to a successor."

Along with its shift toward a more customer-facing business, the company also wants to make money off the expansion of electric vehicles. It announced a new partnership with Ford Motor Co yesterday to develop charging stations at hundreds of dealerships across the UK and Ireland as well as sell home charging equipment and electric vehicle tariffs. The company is in talks with other car companies to expand further into this area, Sarwjit Sambhi, head of Centrica's consumer business, said on a call with reporters.

Oil Industry Poised to Attack as Trump Boosts Ethanol in Fuels



Oil industry foes are preparing to go to court to fight

the Environmental Protection Agency regulation issued Friday that allows year-round sales of higher-ethanol E15 gasoline nationwide.

The agency's final rule offers ethanol producers and corn farmers the promise of greater market access and demand – but the coming legal battle will be the true test of that potential.

The regulation fulfills President Donald Trump's promise to unleash ethanol sales and is a potent show of support to Midwestern farmers who are suffering from Chinese tariffs on soybeans, flooding that destroyed stockpiled grain and a deluge of rain that has delayed plantings. With some 37% of America's corn production going to ethanol mills, any regulatory move lifting demand for the fuel could buttress farmers who helped propel Trump to the White House.

Iowa Republican leaders and biofuel industry boosters will celebrate the shift with EPA's Region 7 administrator during an event at Elite Octane LLC's dry mill ethanol plant in Atlantic, Iowa later Friday. Trump is expected to address the issue during a visit to the state next month.

The EPA rule waives E15 gasoline containing 15% ethanol from vapor pressure requirements that have blocked sales from June 1 to September 15 in areas where smog is a problem, said Bill Wehrum, the assistant administrator for the EPA Office of Air and Radiation. That should cause "a bump" in sales at the roughly 1,200 filling stations that already sell E15 today, while encouraging more of them to offer it, Wehrum told reporters on a conference call.

"Over time, we believe and the industry believes you will see more E15 sold as the infrastructure in the gasoline distribution system and especially at gas stations catches up to the availability of this fuel," Wehrum said. This is going to result in a "substantial increase" in E15 sales, he said.

At Trump's direction, the EPA bundled the E15 shift

with modest changes meant to boost transparency and prevent price manipulation in the trading of credits used by refiners to prove compliance with annual biofuel blending quotas. Large integrated oil companies, including ExxonMobil Corp., BP America Inc. and Chevron Corp., had argued against the EPA's initial proposal of more aggressive trading limitations.

Wehrum said the agency would continue examining allegations of market manipulation and respond to them if needed. "We're applying the theory of first do no harm," he said, noting that proposed position limits and sale requirements "could reduce the flexibility of the market and the efficiency of the market." While the agency takes the issue seriously, he said, the EPA has not yet found clear evidence of significant manipulation.

Senator Joni Ernst, a Republican from Iowa, praised the EPA's action, saying it would mean more consumer choice and savings at the pump.

"The president had made this promise a long time ago: He was really going to work hard for farmers' support and the Renewable Fuel Standard," she said by phone. "And he's coming through with that promise at a time when it's desperately needed. It's something we were going to work toward anyway, but it does bring much-needed relief at a very critical time for our farmers."

Ethanol is already a staple of America's fuel supply, accounting for about 10% of total consumption. Biofuel boosters who have lobbied for the regulatory shift are betting 15% will eventually emerge as the standard. Green Plains Inc. Chief Executive Officer Todd Becker said this month that the higher blend puts in play "year-round demand growth of at least 200 million gallons of annualized incremental demand as only the starting point."

That would come at the expense of oil.

“This action by EPA makes no sense and is contrary to the law, congressional intent and decades of agency precedence,” said Frank Macchiarola, a group director at the American Petroleum Institute. “We will challenge it vigorously.”

The American Petroleum Institute previewed its legal argument in public comments, arguing that the agency is flouting the plain text of the Clean Air Act by extending an existing waiver to E15. Marathon Petroleum Corp. warned the EPA’s move to consider E15 “substantially similar” to conventional E10 gasoline is “arbitrary and capricious” – a fatal failing under a federal law governing rulemaking. And the American Fuel and Petrochemical Manufacturers insisted the EPA is taking action previously rejected by Congress.

Ethanol advocates argue the EPA is on solid legal footing. The agency’s move to grant a waiver to E15 “reflects the best, most natural reading” of the Clean Air Act, and that higher-ethanol blend is substantially similar to E10, said Growth Energy Chief Executive Officer Emily Skor.

Italy to play low 2019 deficit card to avoid EU procedure



EU Commission threatened Rome with disciplinary steps; 2019 deficit could be 2% of GDP or lower, officials say; league economics chief says 1.8% is possible; coalition still undecided how to use savings emerging Reuters Rome Italian coalition officials say the country's public accounts are throwing up positive surprises this year, strengthening Rome's hand as it tries to ward off a possible Euro-pean Union disciplinary procedure. Recent data suggest the deficit this year will not only be below the European Commission's forecast of 2.5% of gross domestic product (GDP) but could even be below the 2.04% agreed with Brussels in December, two senior coalition members said. However, it remains to be seen how far the anti-austerity government will actually slash its current 2.4% target, because some in the 5-Star Movement, one of the two ruling coalition parties, want the savings that are emerging to be quickly spent on new expansionary measures.

The other ruling party, the League, is a push- ing for deep tax cuts, but only from 2020. It is also not certain that an unexpectedly low 2019 deficit would be enough to convince Brussels that Italy's finances are on a sustainable path. But

the latest data at least give Rome fresh arguments – something that looked impossible a few months ago. The Commission on Wednesday paved the way to disciplinary steps against Italy, complaining that its debt had risen in 2018 instead of falling and would continue to do so. It said Rome had also not reined in its annual budget deficit as promised in 2018 and would continue to run excessive deficits this year and next. A disciplinary procedure, which could eventually end in fines, had already been averted at the last moment in December when Italy cut its original 2.4% deficit target for this year to 2.04%, with the agreement of the Commission. In April, Italy restored the original 2.4% target because of a slump in growth, while the Commission forecast 2.5%.

Prime Minister Giuseppe Conte surprised observers when he said on Wednesday, in response to the Commission, that a deficit of 2.1% was possible. But now, senior officials in the government of the right-wing League and the anti-establishment 5-Star say it could be even lower. Claudio Borghi, the League's economics chief, told Reuters 1.8% was possible if current trends continue. The main reason for the surprise trend is that two flagship government measures – an early retirement option and a new means-tested welfare benefit – are proving less popular, and therefore less costly than expected. Taken together, it now looks as if the combined cost of the two policies will be €4bn (\$3.4bn) less than was set aside in the 2019 budget, Borghi said.

This estimate was confirmed by a government member closely involved in economic policy, who asked not to be named. Borghi said tax amnesties allowing people to settle disputes with the authorities by paying a limited sum had yielded more than expected, as had measures against tax evasion. Among these, the requirement from January this year that a copy of virtually all transactions must be transmitted electronically to the taxman produced squeals of protest from companies but has bolstered sales tax revenues. State coffers have also been

swelled by out-of-court settlements with several large multinationals accused of tax evasion, the largest of them a €1.3bn deal with Kering, the holding company of fashion house Gucci.

A senior Treasury official declined to confirm Borghi's 1.8% 2019 deficit projection but said it now looked "possible" that the deficit would be 2% or lower. Public finance data so far this year has been encouraging. The central government deficit for the first four months was just €1.5bn above last year's equivalent figure – below the trend projected in Rome's 2019 Stability Programme, which forecasts that the full-year deficit would rise by €16bn. Tax revenues through April were up 1.0% year-on-year despite a stagnant economy, compared with an official full-year target of 0.6% growth. In addition, dividend payments by the central bank and state-owned enterprises will also exceed the projections in the Stability Programme by more than 0.1% of GDP, the Treasury said in documents sent to Brussels this month.

Airlines scramble to overcome polluter stigma



Reuters Seoul/Stockholm/London

In Lorna Greenwood's London home, there is a shelf lined with travel guides.

But the 32-year-old mother and former government employment lawyer has given up flying.

Greenwood, who grew up enthralled by the possibilities offered by plane travel, is part of a growing group of environmental activists in Northern Europe who are shunning flights as concerns about global climate change increase.

"It's a tough pill to swallow, but when you look at the issues around climate change, then the sacrifice all of a sudden becomes small," Greenwood said.

A Swedish-born anti-flying movement is spreading to other European countries, creating a whole new vocabulary, from "flygskam" which translates as "flight shame" to "tagskryt," or "train brag."

A number of famous Swedes have stopped flying, including opera singer Malena Ernman, the mother of teenage activist Greta Thunberg who has thrust climate change into the spotlight.

"Flygskam" was a major topic at a three-day airline summit in Seoul this weekend, with global industry leaders launching a counter-offensive.

“Unchallenged, this sentiment will grow and spread,” Alexandre de Juniac, head of the International Air Transport Association (IATA) told some 150 CEOs.

The industry says it is shrinking its carbon footprint and its sustainability plan is among the most ambitious and globally focused of any industry.

“Come on, stop calling us polluters,” de Juniac said at a news conference after detailing the global initiative.

The IATA said the CO₂ emission for each CEO’s flight to Seoul was half the amount of a 1990 flight, largely thanks to more fuel-efficient aircraft.

Commercial flying accounts for about 2.5% of global carbon emissions today but without concrete steps, that number will rise as global air travel increases.

The aviation industry has set out a four-pronged plan to achieve carbon-neutral growth from 2020 and halve net emissions from 2005 levels by 2050.

But airline leaders acknowledge they have struggled to articulate their plans in a way that resonates with the public.

When CNN anchor Richard Quest asked a room full of aviation executives whether they had used an often available booking option to offset emissions from their own flights to the South Korean capital, only a handful raised their hands.

The industry’s plan rests on a mix of alternative fuel, improved operations such as direct flight paths and new planes or other technology.

But a widely publicised March study funded by investors managing \$13tn said airlines were doing too little.

“If we as an industry can provide better, more concrete answers...people will start to feel more comfortable that airlines are serious about this commitment,” JetBlue CEO Robin Hayes said in an interview.

Questions remain over how airlines will slow, steady and finally reduce harmful emissions.

Use of sustainable-fuel would have the single largest impact, reducing emissions from each flight by around 80%, according

to the IATA.

The problem is that it is in short supply.

"The reality today is there's just not enough and it's too expensive," KLM CEO Pieter Elbers told Reuters.

KLM last week announced a deal to develop and buy biofuels from Europe's first sustainable aviation fuel plant, due to open in 2022.

Still, the IATA targets 2% of total fuel supply from sustainable sources by 2025 and then expects a steady increase.

In Europe, eliminating dozens of national airspaces borders could reduce fuel consumption by around 6%, but lobbying for a Single European Sky has been bogged down for years.

Airlines say small steps like single-engine taxiing and the use of lighter materials are cutting around 1-2% of emissions each year.

In the absence of a quick and substantial reduction its carbon footprint, the industry has committed to a carbon-offset programme.

The global Carbon Offsetting and Reduction Scheme for International Aviation (CORSIA) allows airlines to purchase pollution credits from environmental projects.

It's unclear what will count as an "offset" and critics say such schemes hide how much effort is being made by industry and how much is being imported and at what price.

"The risk is that the price airlines are effectively paying for carbon will not be politically acceptable in 5 or 10 years," a senior aviation executive said, asking not to be named.

European Union Transport Commissioner Violeta Bulc told Reuters she favours reviewing available green technology every five years "and then seeing if we can reach even further."

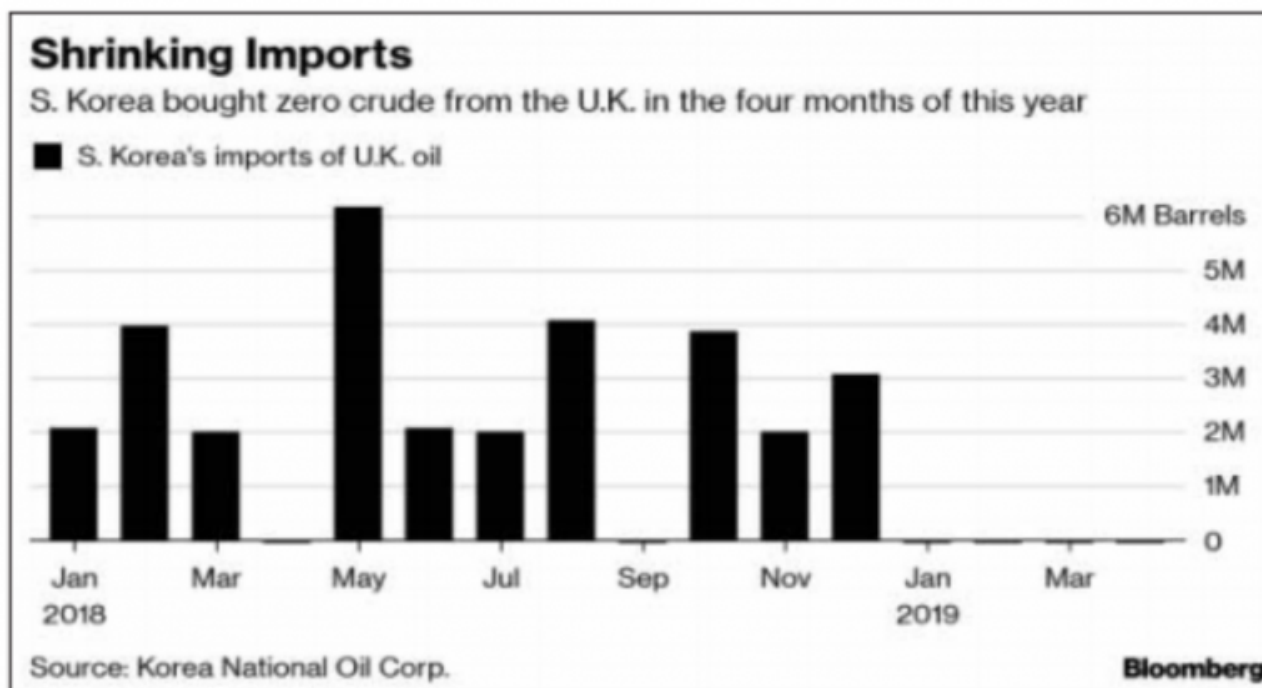
For now, trains are benefiting from the anti-flight movement, although airline bosses in Seoul said that option barely exists in their busiest new markets such as Indonesia's archipelago.

In Stockholm, Susanna Elfors says membership on her Facebook

group Tagsemester, or “Train Holiday,” has spiked to some 90,000 members from around 3,000 around the end of 2017.

“Before, it was rather taboo” to discuss train travel due to climate concerns, Elfors said. “Now it’s possible to talk about this on a lunch break...and everybody understands.”

UK oil’s appeal returns for S Korea even as Brexit looms



After staying away for four months, South Korea is back in the market for North Sea crude. Hyundai Oilbank Co bought 2mn barrels of North Sea Forties crude for August delivery, a rare purchase this year, said traders who asked not to be identified because the information is private. The import was made after refiners in the Asian nation were given incentives to look beyond the Middle East for oil, and it followed a discharge of UK crude in May, the first such purchase this year. South Korea imported zero oil from the United Kingdom in

the first four months of this year as the possibility of Brexit threatened to erode the appeal of the crude to one of Asia's top refining hubs. Britain's exit will mean the return of a 3% import tariff on Forties purchases that was waived by South Korea under a free-trade agreement with the European Union since 2011. While the Asian country is a steady buyer of UK oil, purchasing an average of over 2.6mn barrels a month in 2018, refiners were reluctant to bring cargoes earlier this year as the government delayed renewing a freight rebate scheme that encouraged purchases from regions other than the Middle East. The very-large crude carrier Farhah is scheduled to load Forties crude from Hound Point on June 20 for delivery to Daesan in August, according to traders and shipping fixtures compiled by Bloomberg. Last month, supertanker Athenian Freedom also made a similar voyage, discharging a smaller cargo of the grade, ship-tracking data showed. Hyundai Oilbank operates a refinery in Daesan with crude processing capacity of 650,000 barrels a day.

Can euro replace dollar as world's dominant currency?



Reuters/ London

Should European countries want the euro to replace the dollar as the world's dominant reserve currency, the Sino-US trade war may offer a window of opportunity.

The souring of ties between the world's two largest economies will indicate the extent to which China can switch some of its giant reserve holdings to another hard currency and also point to the limitations the eurozone faces in providing a viable alternative.

In the post-World War Two era, no asset has ever fully matched US government bonds for size, liquidity and credit quality.

It is the closest any global security has come to being perceived as a cash-like, risk-free asset with over \$16tn worth of paper in circulation.

Yet, a year into a bitter tariff war, there are some signs of Beijing's discomfort at being both the United States' biggest trade adversary and one of its biggest creditors.

Recent data showed China sold more US Treasuries in March than it has in any month over the past 2-1/2 years.

If that proves to be more than a one-month quirk, speculation will rise about where it is diverting those reserves, and the eurozone – the world's biggest trading bloc – tops the list of

likely spots.

On size alone, eurozone government bonds appear to provide a credible landing pad: outstanding securities are almost two-thirds of the overall Treasury market.

There are signs already of greater Chinese interest in Europe – bankers attribute record Asian demand for recent Spanish, French and Belgian debt sales to Beijing.

And China has stepped up buying debt from Europe's quasi-sovereign entities, bankers told Reuters, in particular the European Stability Mechanism (ESM) a eurozone-guaranteed AAA/A1-rated bailout fund.

Asian investors snapped up 33% of the ESM's recent 2bn-euro 10-year bond, data from International Financing Review shows.

Asian takeup for ESM's euro issues last year was 4%-5%. But for Chinese reserve managers to shift hundreds of billions of dollars from Treasuries to Europe's single currency, the euro bloc needs to address key shortcomings.

"I find it hard to square the circle how such a huge Treasury holding can be diversified away, given the landscape we are in," said Salman Ahmed, chief investment strategist at Lombard Odier Investment Managers.

"In the eurozone there is not a big risk-free market...Twenty years down the line it may be different."

For Ahmed, the main issue is that credit risk in the bloc is not uniform.

The 19 members each run their own fiscal policies, budget rules are too loosely policed to ensure adherence, and euro exit remains a theoretical possibility.

So wealthier members such as Germany remain net savers that run balanced budgets or even surpluses, while others, mostly in southern Europe, are dogged by high debt.

The resulting mix of credit and political risks make it harder to see the aggregate eurozone bond market as a true mirror of the US Treasury universe.

Ross Hutchison, a fund manager at Aberdeen Standard Investments, says it boils down to the fact the United States "has a federal nature that the euro area hasn't got yet".

Additionally, distortions stemming from years of bond buying stimulus by the European Central Bank mean available euro government bonds are far fewer than may appear.

While euro government debt outstanding is around \$9.5tn, the ECB is estimated to hold roughly a quarter.

And the kind of “safe” securities that reserve managers seek are even scarcer – AAA-rated debt from Germany, the Netherlands and Luxembourg totals around \$2.5tn, less if ECB holdings are discounted.

Debt from slightly lower-rated France, Belgium and Austria would add another \$3tn.

Italy on the other hand has the bloc’s biggest government bond market, worth \$2.3tn.

But its poor debt-to-GDP ratio, sluggish economy and populist policies make its bonds riskier and its credit rating is a notch or two above junk.

So in times of stress, investors clamour for German bonds, while in Italy, yields spike, threatening to undermine local banks that hold these securities.

Italian 10-year yields are at 2.5%, versus Germany’s minus 0.22%. Such risks have chipped away at the euro’s fortunes as a reserve currency – International Monetary Fund data shows it comprises 20% of global central bank holdings, from 26% in 2009.

The decline is linked to the 2011 Greek debt crisis that then ravaged Spain, Italy, Portugal and Ireland, highlighting risks of default by a member state and redenomination of euro debt into a new currency.

European officials are keen to counter the dollar’s hegemony, and at a conference last month they debated ways to win the euro a “stronger international role”. But they made no mention of the one measure that could resolve the issue at a stroke – joint debt issuance via common eurozone bonds.

Such securities would pool the bloc’s risks, and offer safer securities than those from most individual nations.

Olli Rehn, Bank of Finland governor and an ECB governing council member, said last week a safe asset would help enhance

the euro's international role, offering hope the issue will be on the agenda of the new European Commission later this year. A common bond "would be more significant than the creation of another TLTRO in boosting demand for euros globally and reserve managers would be part of that story," said David Owen, chief European economist at Jefferies. He was referring to the ECB's cheap multi-year loans. "Maybe there will be more focus on pushing forward this agenda and taking advantage of the US and China having this trade spat," Owen added. Others, however, note that wealthier states oppose any common bond programme, fearing they will end up footing the bill. Also, across Europe populist and anti-establishment movements are on the rise, with the agenda of slowing integration and returning power to national capitals. Such groups grabbed a greater share of the vote in EU parliamentary elections last month, albeit less than expected. "If anything, the trend is towards decentralisation of power," Ahmed said.

EU must compromise on Brexit deal: Johnson



AFP/London

Prime Minister Boris Johnson yesterday urged EU leaders to drop their opposition to renegotiating Brexit, as the pound slumped on growing concerns about a no-deal departure.

Johnson, who took office last week, wants to change the exit terms struck by predecessor Theresa May but insists he will leave the European Union without any agreement at all if necessary on October 31.

Brussels has said it will not reopen the text.

"The withdrawal agreement is dead," Johnson told reporters during his first visit to Scotland. "I am confident we will get a deal but it is also right we prepare for no-deal," he said.

The government has not yet announced plans for Johnson to visit EU capitals, and a spokeswoman indicated he would not go until Brussels changes its stance.

"He obviously wants to meet EU leaders and negotiate but not to be sat down and told that the EU cannot possibly reopen the withdrawal agreement," the spokeswoman said.

The Confederation for British Industry (CBI), the country's top business lobby group, said companies now needed to be on an "emergency footing" because of the growing likelihood of

no-deal.

The pound lost more than 1% of its value against the dollar yesterday, hitting a two-year low. In a report, the CBI warned that both Britain and the EU were not prepared for a no-deal Brexit and urged businesses to step up contingency plans.

The group's head of EU negotiations Nicole Sykes tweeted that it was "like putting sandbags down for a flood".

"Your kitchen's still going to be underwater but MAYBE we can save the bedroom upstairs," she wrote.

The Institute for Government also warned that a no-deal Brexit would "dominate government for years", allowing little room for other domestic priorities outlined by Johnson such as health, education and transport.

The think-tank said such an outcome would also place the United Kingdom, which includes England, Scotland, Wales and Northern Ireland, "under unprecedented pressure".

On his first visit to Scotland as prime minister, Johnson visited a military base before meeting Scottish Conservative leader Ruth Davidson, who has been opposed to a no-deal Brexit.

Irish Prime Minister Leo Varadkar has also said that a no-deal Brexit would make more people in Northern Ireland "come to question the union" with Britain.

How Europe's populists lost the EU Game of Thrones



The conventional wisdom about European Commission President-elect Ursula von der Leyen's confirmation by the European Parliament this month is that Central and Eastern European populists pushed her over the line. That is wrong. Had such parties actually backed her, Von der Leyen's margin of victory would have been much larger, considering the support she had from the centre-right European People's Party (EPP) and the liberals in the EU parliament.

True, populist MEPs from Poland's Law and Justice (PiS) Party and Hungary's Fidesz were firmly opposed to Frans Timmermans, a Dutch socialist who has loudly condemned both parties over their violations of EU norms and the rule of law. But nor did they want to strengthen French President Emmanuel Macron, who supported Von der Leyen. The optimal outcome for Poland's de facto ruler, Jarosław Kaczyński, and Hungarian Prime Minister Viktor Orbán was Von der Leyen's confirmation by the smallest possible majority. Populist MEPs thus appear to have been instructed to say they were voting for her without actually doing so.

Had Von der Leyen lost, it would have been ample payback to the rejection of the PiS candidate for deputy speaker of the European Parliament and former prime minister Beata Szydło's two failed bids to chair the Parliament's Employment

Committee. Moreover, this was around the same time that Krzysztof Szczerski, also backed by PiS, lost his bid to become deputy secretary-general of Nato.

But, because Von der Leyen made it through, the populists are boasting that she owes her job to them, as though they have some kind of tacit deal with the former German defence minister. That seems highly dubious, given that a deal between Von der Leyen and PiS would have cost her the support of the socialists and liberals. But now that the populists have cast a shadow over her leadership, it is important to understand what they may want from her.

The first thing to recognise is that Central and Eastern Europe's populists – now including the Czech government – would prefer to pursue intergovernmental negotiations than to work through the European Commission. Though the Commission usually goes out of its way to back the EU's weaker members, populists, by definition, distrust institutions. They would rather install "the right people in the right positions," and then strike a deal with them.

In the view of the Visegrád Four (Poland, Hungary, the Czech Republic, and Slovakia), the weaker the Commission, the better. The V4 governments are convinced that they will always reach agreements with Germany – with which their countries have deep economic and historical ties – more easily than with the EU.

The Visegrád countries didn't even try to get their act together in the new parliament. Their approach to intra-EU relations is based not on building alliances or developing long-term strategies, but on wielding the veto. And yet, while PiS has the largest parliamentary delegation, with 26 seats, it belongs to the marginal European Conservatives and Reformists group. Fidesz has 13 seats, but is part of the EPP; and the Czech populist party ANO has six MEPs, but sits in the Renew Europe group.

Then again, the V4 has always functioned as an ad hoc coalition without a common strategic vision. This time, it didn't even try to unite to block any of the leadership

appointments. But the next test will come with budget negotiations, which is one area where the V4 has traditionally been able to form a plan and cooperate. Prior to an earlier budget negotiation, for example, Poland was able to secure Polish MEP Janusz Lewandowski's position as EU Budget and Financial Programming Commissioner.

The problem this time is that the Visegrád populists will not have any allies in key positions. That means they could soon face a problem: the disbursement of EU funds will be made conditional on a recipient government's respect for the rule of law. It isn't yet clear where Von der Leyen stands on this issue. But it is worth remembering that conditionality is a German idea, and that Germany is the largest source of EU funds.

Moreover, the V4 itself is divided on the question of whether EU funds should come with more strings attached. Hungary and Poland are staunchly opposed to the idea, of course; but the Czechs and the Slovaks have remained quiet, for fear of being thrown out of the Alliance of Liberals and Democrats for Europe or the Progressive Alliance of Socialists and Democrats. So, while the V4 governments might manage to negotiate jointly on local projects, the Czechs and Slovaks will probably stick closer to larger allies.

For Western Europeans, the fact that Eastern Europe got nothing in the leadership reshuffle is somewhat awkward. Most likely, the question of regional inclusion will be settled by making Laura Codruța Kövesi of Romania the head of the new European Public Prosecutor's Office. But this, too, would represent another blow against populists. Having made a name for herself as an anti-corruption crusader at home, Codruța Kövesi now has Macron's backing, following the withdrawal of a French candidate for the job.

Yet while Von der Leyen is German, her victory is widely seen as a triumph for Macron. In the leadership negotiations, German Chancellor Angela Merkel couldn't play the "Eastern European card" and demand that Old Europe offer the newer members some concessions to avoid offending them. The

countries to Germany's east have been offended for quite some time. – Project Syndicate

1 Sławomir Sierakowski, founder of the Krytyka Polityczna movement, is Director of the Institute for Advanced Study in Warsaw and Senior Fellow at the German Council on Foreign Relations.