The Economist INTELLIGENCE UNIT

Industries in 2019

A special report from The Economist Intelligence Unit

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Overview

The world's major industries are all set for further growth in 2019, but there are some worrying risks.

Two years ago, when The Economist Intelligence Unit issued Industries in 2017, we predicted that the election of Donald Trump as US president in November 2016 could bring huge changes for global business. We were not wrong. This edition of our annual report discusses the changes that Mr Trump's policies—and other global trends—have already brought to six industry sectors: automotive, consumer goods and retailing, energy, financial services, healthcare, and telecoms. And we look ahead to the challenges facing these businesses in 2019.

This report highlights five major risks that could affect our industry forecasts for the year ahead.

- **The US-China trade war:** we have cut our 2019 growth forecasts for the automotive and consumer-goods sectors in particular compared with six months ago.
- **A global slowdown:** even those countries not directly affected by growing trade barriers could be vulnerable to a change in business confidence in 2019, with the most likely impact being on emerging markets.
- **Brexit:** the UK's exit from the EU in March 2019 will be a drag on sectors including financial services, automotive and healthcare, regardless of any deal that is struck.
- **Sanctions on Iran:** the US's decision to backtrack from the international Joint Comprehensive Plan of Action could push up global oil prices in 2019.
- **Cybersecurity and technology risks:** a tussle for technological dominance is at the core of the US-China trade dispute, while regulators are also struggling to ensure safe connectivity.

Most of these risks are, to some degree, certainties. The UK will officially leave the EU on March 30th 2019, while US sanctions on Iran have already been imposed. It is not yet clear, however, what the full effects of these will be. Brexit's impact in 2019 depends on whether the transition deal that was negotiated in mid-November of this year is finalised, easing the UK's trade problems as it exits. In the case of Iran, much hinges on how successful the US—unsupported by the EU—is in blocking Iran's exports. If global oil supplies tighten sharply, then oil prices could yet soar. As for cybersecurity and technology risks, they are always present but are likely to increase in 2019 as connectivity spreads.

The power struggle between the US and China has already come to a head in 2018. In a three-stage process, the US has imposed additional tariffs of between 10% and 25% on Chinese imports worth about US$200bn a year. China has retaliated with its own trade barriers against the US, while liberalising terms with some of its other trading partners. However, a further round of retaliation now looks likely in either December 2018 or early 2019, and could cover all of the remaining trade between the two countries.

The risk for next year is that this will escalate into a full-blown global trade war, involving more than just these two countries. Although the US has agreed a new trade pact with Canada and Mexico, dubbed the United States-Mexico-Canada Agreement (USMCA), some doubts remain over Mr Trump's long-term commitment to such a deal. New tariff barriers involving the EU, Japan, Latin America and others remain possible, particularly in the automotive sector. Moreover, as companies divert trade during 2019 in an effort to avoid tariffs, other countries may resort to protectionism to stem a sudden surge in imports.

How businesses react to rising tariffs will be as important as the tariffs themselves. Faced with increases in their trading costs, they can swallow the extra expense, pass it on to end buyers, or seek out new suppliers and new markets. They may also respond by reducing investment, laying off staff and reducing costs. Should that happen, we would expect global trade to shrink, inflation to rise, consumers' purchasing power to fall and global economic growth to slow.

This could also have knock-on effects for the global financial system, particularly if accompanied by monetary tightening. We currently forecast that the US monetary tightening cycle will be controlled and relatively gradual in 2019, with inflation picking up only modestly. This view is largely built into financial markets, meaning that stockmarket volatility will be low and not long-lasting. However, markets will be extremely sensitive to any shifts in policy.

Moreover, there is a risk that contagion could spread to emerging markets. The past year has already seen currency crises in Turkey and Argentina, but pressure on emerging markets as a group could intensify if market sentiment deteriorates further than we currently expect. In this scenario, capital outflows from emerging markets would be higher and more indiscriminate. That could force some countries with external imbalances to make painful adjustments, while the most vulnerable suffer a financial crisis. Emerging-market GDP growth would fall sharply as a result, weighing on the global economy.

Several of the world's major economies—and their industries—would suffer if that happens. There are weaknesses in the economies of China, the euro zone, the Middle East and elsewhere that could all pose risks. These are all markets that companies are looking to for stable, high-value sales or for rapid growth. China in particular is now the biggest market, or second only to the US, for many goods. A hard landing there has so far been avoided but remains possible.

Even so, these remain just risks for now. Unless circumstances worsen, we still expect all six of the industries covered here to report growth in 2019, and in most cases it will be strong growth.

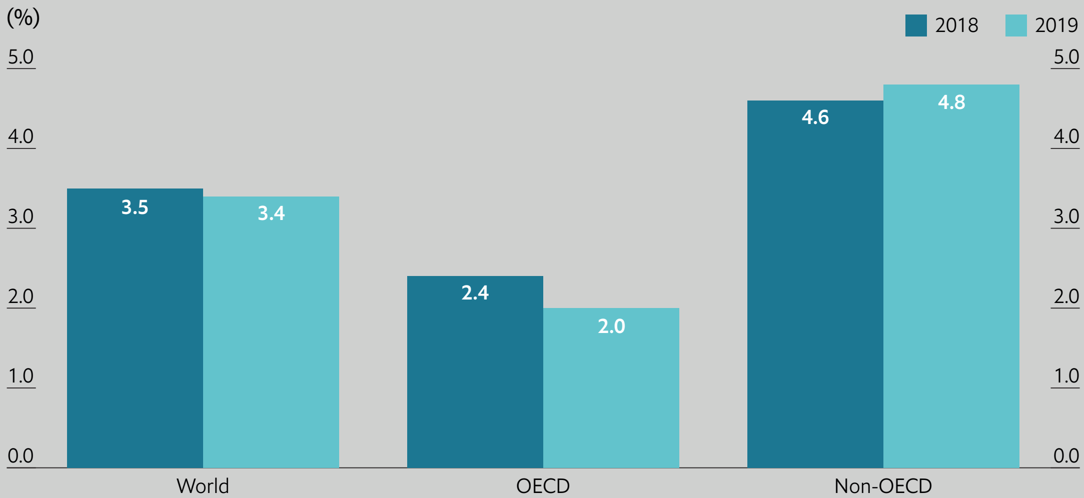
- New-car sales in the 60 markets covered by this report will rise by 2.7%, with commercial-vehicle sales rising at the same rate.
- World retail sales will increase by 2.8%, led by 6.1% growth in China.
- Global energy consumption will rise by 1.8%, with particularly strong growth for renewables, while oil prices will firm.
- Total deposits with the global financial industry will increase by 5.8%, while lending will rise by 6%.
- Healthcare spending will climb by 5.1% worldwide, including 5.7% higher spending on pharmaceuticals.

- Global mobile subscriptions will increase by 3%, fixed lines by nearly 2% and broadband subscriptions by 6%.

This overall growth will give companies some breathing space as they manoeuvre to avoid the risks. Even so, the least adaptable will undoubtedly struggle during the sometimes difficult year ahead.

EIU forecast: The global economy

OECD drag: change in real GDP



Note. At purchasing power parity.
Source: The Economist Intelligence Unit.

In 2019 we expect the trade war to dampen growth in both the US and China and to act as a drag on growth in the wider global economy. The trade war comes at a challenging time for the Chinese economy. Concerns over the strength of domestic demand have returned, as momentum in both private consumption and investment has weakened. As a result, we expect a slowdown in China's real GDP growth in 2019, to 6.2%, from an estimated 6.6% this year.

The trade war will also affect the US economy, which has so far had a stellar year in 2018. Combined with monetary tightening by the Federal Reserve (the US central bank), it will start to weigh on the economy in 2019. We expect real GDP growth to slow to 2.2%. The US manufacturing and agricultural sectors, in particular, will be hit by the trade dispute, and rising interest rates will cause private consumption to slow. Financial markets may also prove more sensitive than we currently assume.

The growing geopolitical tensions will add to the risks facing emerging markets, which have come under growing pressure in 2018 as a result of a strengthening US dollar and tightening global liquidity conditions. In many emerging markets, a significant rise in debt levels in recent years has increased their vulnerability, as has political instability.

Even so, in our core forecast we expect real GDP growth in non-OECD markets to accelerate slightly in 2019. The OECD, on the other hand, will see a fairly sharp deceleration. This will pull down growth in global real GDP to 3.4% in 2019, from 3.5% in 2018. However, we rate as moderate the likelihood of a sharp global slowdown brought about by a faster than expected increase in US interest rates.

Automotive in 2019: Supply shocks

New-vehicle sales will grow in 2019 but are very vulnerable to trade and environmental risks.

The world's new-vehicle sales have now been growing for nine consecutive years since the downturn of 2009. In 2019 they should report yet another good year, but the industry will face substantial risks that could depress sales. The US-China trade dispute has already disrupted global supply chains, while the UK's exit from the EU could add to trade barriers in Europe. Meanwhile, the move from fossil fuels (particularly diesel) to electric cars will accelerate as China enforces its sales targets for new-energy vehicles (NEVs). Thanks to the relative stability of the past few years, most vehicle-makers should be able to withstand these pressures. However, they will still need to manoeuvre adroitly to survive—particularly if consumer and business confidence also wavers.

Our key forecasts

- New-car sales will increase by 2.7% in 2019 for the 60 countries covered by The Economist Intelligence Unit's forecasts. Commercial-vehicle (CV) sales will also rise by 2.7%.
- The industry will remain vulnerable to trade shocks and uncertainty as tariff barriers rise and fall around the world.
- Global sales of new fully electric vehicles (EVs) will reach 2.2m units, spurred by new emissions targets in the EU and NEV targets in China.

Still driving forward

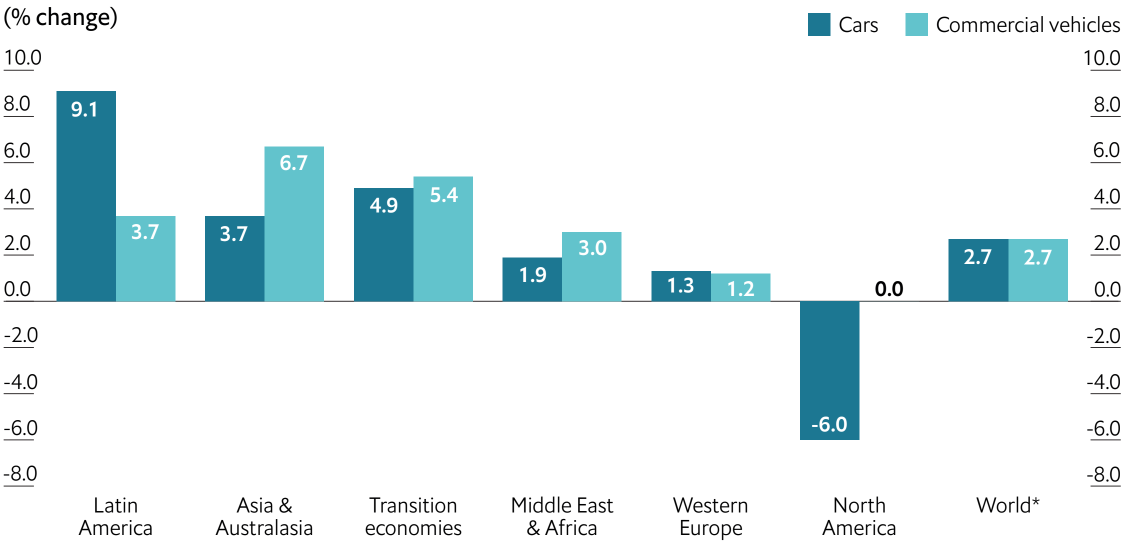
The past few years have, on balance, been unusually easy ones for the global automotive industry. Before and during the global financial crisis, there was always at least one major vehicle-maker teetering on the brink of bankruptcy. Now, however, vehicle manufacturers' finances are generally more secure, buoyed by continuing—if volatile—demand from emerging markets. After a sharp slowdown in 2017, when the slump in global oil prices affected markets from Russia to Brazil, we expect global car sales to rise by 2.7% in 2019, up from 1.7% in 2018. CV sales will also see 2.7% growth in 2019, although in this case it will mark a slowdown from estimated growth of 6.8% in 2018.

The fastest growth will be in those countries recovering from the drop in global commodity prices, including many in the Middle East, the former Soviet Union and Latin America. Yet, as usual, much will depend on what happens in China and the US, which between them will account for half of the global vehicle market. Given the trade dispute between the two countries, there are considerable risks to our forecasts. Both the US and China have already targeted the automotive industry in the first three rounds of tariff rises during 2018. On the US side, the tariffs have mainly affected imports of automotive parts from China, as well as imports of steel and aluminium. China, for its part, has raised tariffs on vehicle imports from the US, while lowering them for other countries.

The impact of the trade dispute on Chinese auto parts exports, which were worth US$31bn in 2017, will be painful for both sides. Although parts account for only a small share of China's exports, the US is the sector's biggest market. US vehicle-makers will have to seek out alternative suppliers, probably from countries such as Thailand. These may well be more expensive, meaning that US consumers will end up paying higher prices for their cars. We currently expect US car sales to drop by 3.6% in 2019, while CV sales edge down by 0.3%.

For its part, China accounted for almost 20% of US finished-vehicle exports by value in 2017, equivalent to goods worth US$10.3bn. Ironically, however, some of the companies that will be worst affected are German luxury carmakers such as BMW and Mercedes-Benz, which export from their US plants to China. US carmakers, including Ford and General Motors, make most of their cars destined for the Chinese market in China itself, although they have seen sales drop in recent months on the back of anti-US sentiment. We forecast that overall car sales in China will grow by 2.9% in 2019, while CV sales will rise by 7.5%.

Latin lessons: new vehicle registrations in 2019



*60 biggest economies only.
Sources: The Economist Intelligence Unit; local sources.

Rising and falling barriers

The US-China dispute, however, is only part of a bigger shift in trade barriers around the world. The US also recently concluded a renegotiation of the North American Free-Trade Agreement (NAFTA), which underpins automotive trade between the US, Canada and Mexico. This is now being replaced by the US-Canada-Mexico Agreement, which will oblige vehicle-makers to source more of their components from within North America and to seek out suppliers paying higher wages. Mexico's automotive sector is likely to lose out under these terms in 2019—although not nearly as badly as it would have done if NAFTA had been scrapped altogether.

In Europe, meanwhile, the UK's exit from the EU in March 2019 poses considerable risks for countries on both sides of the English Channel. UK carmakers such as Jaguar Land Rover have already warned that they may be forced to slash production if no long-term deal is reached. However, Brexit will also affect European carmakers, notably Germany's Volkswagen Group (which is the market leader in the UK) and France's Groupe PSA, which bought the UK's Vauxhall Motors in 2016. Moreover, EU vehicle-makers—along with those from Japan—still face threats from the US president, Donald Trump, that he could impose tariffs on their automotive exports to the US market, as well as on their steel and aluminium exports. Then there is Iran, whose automotive boom has been cut short by the reimposition of US sanctions.

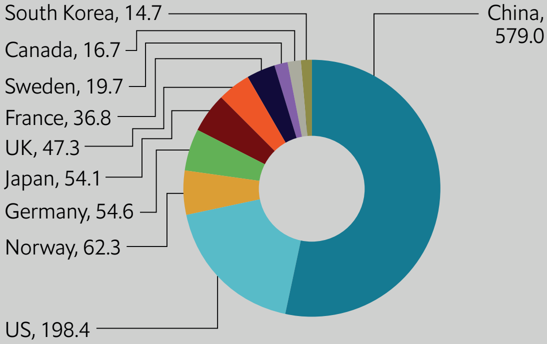
The picture will not be solely one of rising trade barriers in 2019, however. In many places, particularly in Asia, the trend is still towards liberalisation. While raising automotive trade barriers against the US, China has dropped them against other countries. It has also allowed carmakers to set up wholly owned plants in China, rather than being obliged to form joint ventures as before. Tesla, a US EV-maker, has already bought a plot in Shanghai and will probably secure the necessary building permits in 2019.

The Association of South-East Asian Nations (ASEAN) continues to head towards greater integration—and is expanding its list of external free-trade agreements with nations that already include China. Japan has secured an economic partnership deal with the EU that will see automotive tariffs fall and vehicle standards align; both sides are likely to ratify this deal during 2019. Meanwhile, the 11 remaining countries in the Trans-Pacific Partnership will continue to defy the US decision to pull out as they ratify their new deal. Several countries, including Japan, are also mulling over the idea of a Regional Comprehensive Economic Partnership or a comprehensive Asia-Pacific free-trade deal that would cover 60% of the global economy.

While all these negotiations continue, vehicle-makers will face huge uncertainty. Many are already starting to reorganise their supply chains and their production plans to fit the new world order. However, some are already seeing upsides. In particular, vehicle-makers outside the US are likely to benefit from falling input costs in 2019, as Chinese steelmakers and parts manufacturers divert their exports. The automotive industry's biggest immediate concern, therefore, is not necessarily the tariff barriers themselves, but the impact that these may have on consumer and business confidence—and therefore on the global economy. A sharp slowdown in economic growth, particularly in crucial markets such as China, would certainly dampen vehicle sales in 2019.

Global automotive: Emission critical

Before lift-off: Electric car sales in 2017
('000 units)



Source: International Energy Agency, ACEA and EIU.

Trade barriers are only one of the major risks facing vehicle-makers in 2019. The other is the continued tightening of emission controls as they come under pressure to scale back their use of fossil fuels, particularly diesel. The short-term implications of this were obvious in the autumn of 2018, when the EU introduced its new Worldwide Harmonised Light Vehicles Test Procedures. Car sales slumped in most EU markets amid a testing backlog, and will struggle to recover in 2019.

Undeterred, in January 2019 China will bring into force its NEV regulations, which state that manufacturers of mass vehicles in the country must earn NEV credits worth 10% of their sales. Although each NEV (a term that covers most types of EVs) may earn up to six credits, the rules pose a massive challenge to carmakers such as Volkswagen and General Motors. Although they are planning plenty of EV launches in 2019, they will struggle to dent the market dominance of Chinese carmakers. Those car manufacturers that fail to meet the targets will either have to buy NEV credits from rivals or face large fines.

Spurred by China, the global trend towards full adoption of EVs will become even clearer in 2019. Most other countries will continue to roll out ambitious targets for vehicle emissions or pollution, as they pledged to do under the Paris Climate Change Agreement. Indeed, many countries plan to ban sales of new fossil-fuel cars altogether over the next couple of decades. We forecast that global sales of full EVs will rise to around 2.2m in 2019, up from 1.5m in 2018, with China accounting for over half the market.

The US, as so often, is resisting the trend. In 2018 federal regulators decided to scale back the emission and fuel-economy targets previously set for 2021-25, freezing them at 2020 levels. Yet that decision, while welcomed by some vehicle-makers, has already encountered legal challenges from states, including California, that want to keep the targets in place. The uncertainty will add to vehicle-makers' challenges in 2019, as they try to plan around the risk that they will have to produce to two separate sets of standards for the US market.

Given this constraint, those strong EV growth forecasts must be put into context. Total global new-car sales are likely to touch 69m units in 2019, while CV sales top 28m—meaning that EVs will have a market share of only a little over 2%. Even so, carmakers must step up their launches of EVs over the coming year, regardless of how hard the vehicles prove to sell.

2019 calendar: Automotive

January

19-27: European Motor Show, Brussels, Belgium
14-27: North American International Auto Show, Detroit, US
23: Ford reports 2018 results
30: Volvo Car Corp reports 2018 results

February

6: Daimler reports 2018 results
9-14: New Delhi Auto Expo, India
9-18: Chicago Auto Show, US
14: Groupe Renault reports 2018 results
15-24: Canadian International Auto Show, Toronto, Canada
TBC: General Motors reports 2018 results.

March

7-17: Geneva International Motor Show, Switzerland
12: Volkswagen reports 2018 results
27-April 7: The 40th Bangkok International Motor Show, Thailand
28-April 7: Seoul Motor Show 2019, South Korea
29: UK leaves the EU unless extension to Article 50 process is agreed
30-April 8: New York International Auto Show, US
31-April 5: Zagreb Auto Show, Croatia

April

5-14: The Washington Auto Show, Washington DC, US
25-May 4: Beijing Motor Show, China
25-May 5: Indonesia International Motor Show, Jakarta, Indonesia
30-May 2: Commercial Vehicle Show, Birmingham, UK

May

16-19: The London Motor Show, UK

June

4-6: TU Automotive ‘18, Detroit, US
16-17: International Vienna Motor Symposium, Austria

July

TBC: Seoul Auto Salon, South Korea

August

26-29: MIMS Automechanika, Moscow, Russia

September
10-12: Electric and Hybrid Vehicle Technology Expo, Michigan, US
12-22: IAA International Motor Show, Frankfurt am Main, Germany
TBC: IAA Commercial Vehicles 2019, Hannover, Germany

October
15-19: Mondial de l'Automobile, Paris, France
24-Nov 4: Tokyo Motor Show, Japan

November
14-19: Dubai International Motor Show
TBC: Salon Internacional Automovil, Barcelona, Spain
TBC: Los Angeles Auto Show, US

Consumer goods and retail in 2019: Selling short

The US-China trade conflict will damage the outlook for retail sales in both countries in 2019, but especially in China.

In 2019 consumer sentiment and sales will be vulnerable to a volatile geopolitical environment, with the chief risk being the US-China trade war. Just as the global economy will suffer at the hands of protectionism, so too will retail sales, according to our new forecasts, which reflect the downgrading in August 2018 of our GDP projections. The internet continues to lure shoppers away from stores, while pricing pressures will be exacerbated by the rise in trade barriers.

Our key forecasts

- Global retail volume growth will be 2.8% in 2019, down from a predicted 2.9% previously.
- We have lowered our forecast for retail sales growth in the US from 2.5% to 2.4%.
- The biggest impact of the trade dispute will be in China, where we have cut our retail sales growth forecast from 6.7% to 6.1%.

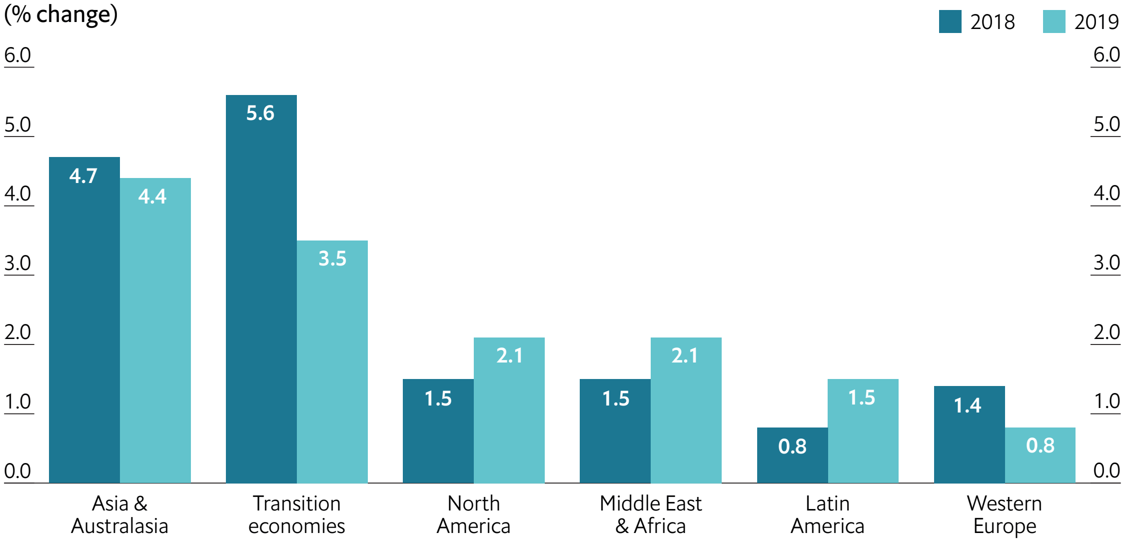
What's in store worldwide?

The trade policies of the US president, Donald Trump, will not weigh too heavily on the US retail market in 2019. Although tariffs could push prices higher for some goods, conditions will remain propitious for shoppers: incomes are rising, while unemployment and inflation are low. As a result, the US will remain the world's largest centre of consumption, accounting for just over a fifth of the US$20trn of retail sales expected globally in 2019. Sales growth in the US will stay level with 2018, albeit down slightly compared with our pre-August forecast.

In the next-biggest retail market, China, the impact of the trade war will be far greater, and will be exacerbated by other factors (see box). Consumer expenditure, previously on course for growth of 7.3%, will rise by just 3%. Most significant, however, is the diminished outlook for China's retail sector, which is central to the growth plans of so many consumer-goods companies. Before the trade war flared up we forecast that retail sales would grow by 6.7% in 2019. The new outlook is for a slower expansion, at 6.1%.

Slower still will be western Europe. Sales there will be stagnant, as price sensitivity and the continued rise of discount shops crimp spending. In the UK, we forecast that retail sales will shrink by 0.7%. The Middle East and Africa, meanwhile, will recover only slowly from the low oil prices of 2014-16 and the ensuing austerity. Geopolitical risk will also hang over the region. In similarly commodity-dependent Latin America, low oil prices have weakened currencies and fuelled inflation; consumer confidence is returning only slowly.

Retail around the world: sales by region in 2019
(% change)



Sources: The Economist Intelligence Unit.

Sales in the transition economies of central and eastern Europe will sustain their pick-up, four years after the turmoil in Ukraine and the annexation of Crimea led to international sanctions on Russia. Pent-up demand and recovering global oil prices bode well for retail sales in the region.

Once again, however, the star performer will be Asia. Reliance on Asia is a mixed blessing for retail and consumer-goods companies: consumers there tend to have shallower pockets, and can be prone to swings in sentiment. The business environment can also be tough. Yet, given the travails of Western high streets and turbulence elsewhere, ignoring Asia is not an option for many. Retail volumes there will grow by 4.4% in 2019, despite China's downgrade. Fortunately, other markets are rising—notably Vietnam, the Philippines, Indonesia and Malaysia. Only India, however, will really be able to take up any slack left by China's slower than expected expansion.

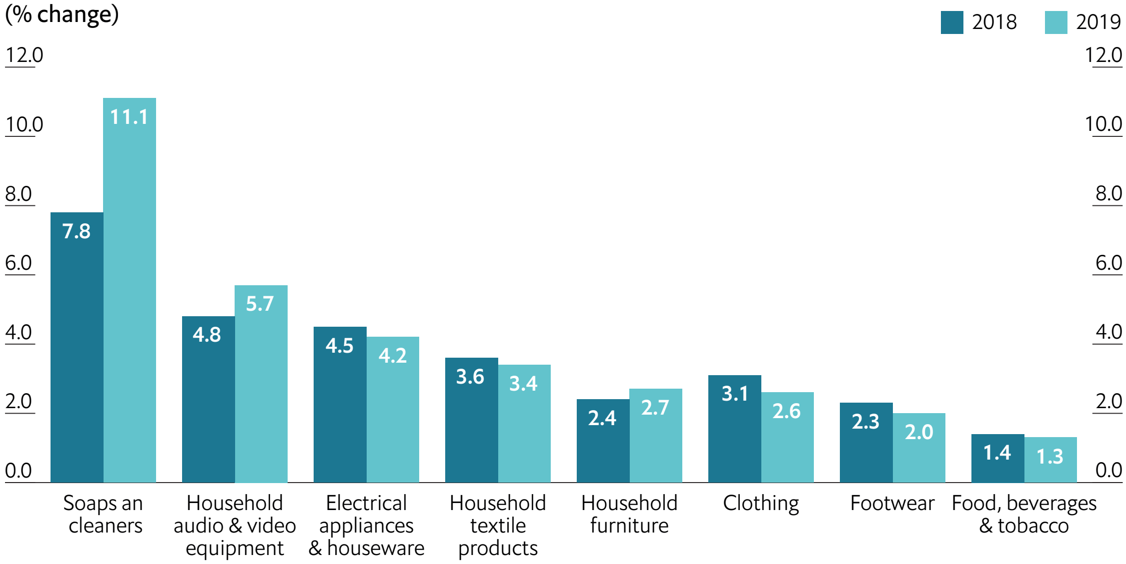
The growing and the groaning

It is India's e-commerce sector that is growing particularly quickly—as is e-commerce worldwide. Internet retailing will continue to be both a disruptor and an enabler in 2019, offering opportunities to those that succeed in selling online or through a multichannel approach, but damning those that fail. For the traditional incumbents, though, making the transition will remain a process of trial and error. Take Walmart, a giant of bricks-and-mortar retail. The company will be staking its future on its online ventures, including its recent acquisition of a majority stake in India's Flipkart. In 2019, however, that investment will mostly be a weight on profits.

How the balance between internet and bricks and mortar plays out will largely depend on the products sold. In 2019, we expect soaps and cosmetics to be the standout performer in terms of market demand (see chart next page). The consumer electronics sector, as well as household audio and video equipment, will also do well. However, the year is likely to be a far more troubled one for the food and beverage sector, where margins that are already slim could be shaved still further by rising tariffs and supply problems.

Selling high, and low: Market demand for consumer products

(% change)



Sources: The Economist Intelligence Unit.

Growth in consumption of food and beverages is slowing, most strikingly in the case of alcoholic beverages, where per-capita consumption is falling. Generally in food and beverages, established players are being harried by an assortment of challengers: cheaper private-label goods; pricier "craft" products; agile start-ups in the premium segment; and increasingly acquisitive emerging-market firms, many from India and China. Consumers' growing preference for products perceived as healthy will make life for food processors harder still, as will regulators' tightening oversight (often on health grounds). In 2019, expect major food and beverage companies to continue to shed businesses considered "non-core" and to seek to gobble up more of their smaller, faster-growing competitors.

China retail: Dimming hopes

The hopes of companies and governments around the world rest squarely on the shoulders of Chinese consumers. In the past decade, private consumption has contributed around two-fifths of the growth in China's economy. However, the US-China trade war has dimmed the outlook for Chinese consumption. It will harm consumer confidence and push up inflation from 2.1% in 2018 to 2.8% in 2019, and is the primary reason why we have lowered our forecasts for retail sales and private consumption. Even before trade frictions worsened, however, Chinese retail sales were on a slower path.

China's elevated property prices have stoked higher levels of household debt. Amid a government campaign to constrain credit, capital has become harder and costlier to come by, affecting companies and consumers alike. Cheap fast foods like instant noodles and pickles—previously thought to have peaked in popularity—have made a comeback, encouraging talk in China of a "consumption downgrade".

Yet rumours of the death of the Chinese consumer are exaggerated. The country's policymakers are acutely aware of the importance of consumption for growth, but must balance support for consumption with continued deleveraging. They are thus turning to fiscal measures to encourage spending. An increase in the tax threshold was brought forward to October 2018, while reforms to individual income tax legislation will take effect at the beginning of 2019. Subsidies and tax breaks for purchases of consumer goods and services could also be in the offing.

Also boding well for consumption, household debt is now falling. All of these factors will help to keep retail sales growth above 6% in 2019. China's retail sales will account for 20% of the global total in 2019, almost level with the US—hardly cause for a wholesale loss of faith in the Chinese consumer.

2019 calendar: Consumer goods

January

Dubai Shopping Festival, UAE
5-7: London Fashion Week Men's, UK
8-11: International Consumer Electronics Show, Las Vegas, US
13-15: Retail's BIG Show, New York, US
17-21: Paris Men's Fashion Week, France
21-24: Paris Haute Couture, France
31: Unilever reports 2018 results

February

7: Yum! Brands reports 2018 results
8-16: New York Fashion Week, Autumn/Winter
15: Metro General Meeting
15-19: London Fashion Week, Autumn/Winter, UK
19: Walmart reports fiscal 2019 results
19-25: Milan Fashion Week, Autumn/Winter, Italy
25-28: Global Food Safety Conference, Nice, France
25-March 5: Paris Fashion Week, Autumn/ Winter, France

March

29: UK leaves the EU unless extension to Article 50 process is agreed
TBC: Carrefour reports 2018 results

April

4-5: Global Retailing Conference, Tucson, Arizona
8-10: Next Generation Retail Summit US, Colorado, US
10: Tesco reports 2018/19 results

May

1-2: Retail Business Technology Expo, London, UK
14-16: The World Retail Congress, Amsterdam, Netherlands

June

18-23: Paris Men's Fashion Week, France
22-23: The Global Consumer Goods Summit, Vancouver, Canada
30-July 4 Paris Haute Couture, France

September

6-14: New York Fashion Week, Spring/Summer, US
17-23: Milan Fashion Week, Spring/Summer, Italy
23-October 1: Paris Fashion Week Spring/Summer, France
TBC: London Fashion Week Spring/Summer, UK

November

11: Singles Day, China

29: Black Friday

December

2: Cyber Monday

21: Super Saturday

Energy in 2019: The Iran effect

Renewed sanctions on Iran will create risks for global oil markets in 2019, but demand for renewables will carry on rising.

For the global energy sector, the reimposition of US sanctions on Iran's oil exports places an upside risk on oil prices in 2019. At present, concerns regarding oversupply are outweighing fears about the sanctions, dampening prices. How much prices will rise again depends on whether the US administration led by the country's president, Donald Trump, can prevent Iran from selling oil to buyers in Europe and Asia. Some importers have already secured temporary waivers from the sanctions. Moreover, the oil market will be cushioned by a slight easing in oil demand growth combined with strong non-OPEC supply, keeping the ceiling price for 2019 below US$80/barrel. Nevertheless, the upside risk is that, due to lower Iranian supply, oil markets still remain exposed to a severe supply disruption elsewhere, such as in Venezuela, Nigeria or Libya.

<u>Our key forecasts</u>

- A decline in Iran's oil output will keep prices slightly buoyant, with dated Brent blend expected to average US$75.5/b in 2019, up from an estimated US$73.2/b in 2018.
- Global consumption of petroleum products will increase by less than 1.5% in 2019, down from 1.7% in 2018, with the US, China and India all reporting slower growth.
- We forecast that global generation from non-hydro renewables will increase by 11.7% in 2019, outpacing any other energy source.

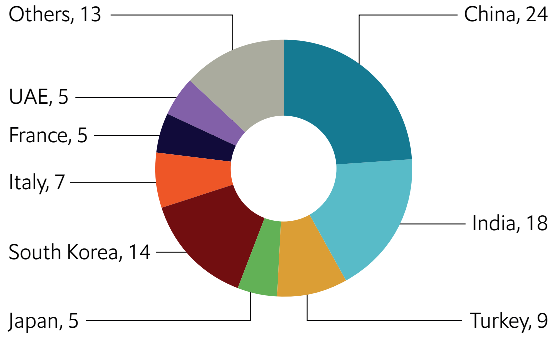
The US decision

Mr Trump's administration withdrew from the Joint Comprehensive Plan of Action (JCPOA) agreement in May 2018. The JCPOA was the agreement between Iran and the US, the UK, France, Germany, Russia and China (known as the P5+1) in which Iran agreed to restrict its nuclear programme if the EU and the US lifted the sanctions that they had previously imposed to curb Iran's nuclear activities. In August the US reimposed the first round of sanctions on Iran, impacting sectors such as automotive, as well as Iran's access to financing. This was followed in November by a second and more important round, which covered oil. However, the US did grant six-month waivers to eight countries that buy Iranian oil—China, India, Greece, Italy, Taiwan, Japan, Turkey and South Korea—on the understanding that they would reduce their intake of Iranian oil over that period.

We take the view that the sanctions will last throughout 2019. The reimposed US sanctions are now aimed at discouraging Iran's policies that go well beyond the nuclear remit, such as its military presence in Syria and its support for Hezbollah in Lebanon and the Houthi rebels in Yemen. Iran is unlikely to bow to this pressure, as changing these policies would mean giving up some of the core rationales for the Islamic Republic. Thus, the US-Iranian stand-off could last for a while.

So what does this mean for oil markets in 2019? After sanctions on Iranian oil exports were lifted in early 2016 following the full implementation of the JCPOA, Iran's production and exports returned to normal fairly quickly. Output reached around 3.8m barrels/day (b/d) in 2017, of which 2.4m b/d was exported to buyers led by China (see chart). In 2019, we expect Iran's oil exports to fall back to an annual average of 1.2m b/d.

Asia bound: Iran's crude oil and condensate exports by destination in 2017
(% share)



Source: US Energy Information Administration, Clipper Data.

This is still far higher than the US hopes: the Trump administration has said that it wants Iran's exports to fall to zero. This is an unrealistic target, given that the US has no diplomatic support from its European allies, Russia or China for its withdrawal from the JCPOA, let alone for the reimposition of its sanctions. The US has, however, given up on its "zero imports" target, at least in the short term, due to the granting of 180-day waivers to eight countries. Meanwhile, Iran continues to make overtures to key buyers such as China and India, offering price discounts, bartering and the ability to pay in local currencies, as well as the option of switching off geolocation transponders so that its oil tankers will not be detected.

That said, the reimposed US sanctions will still have a considerable impact on the volumes that Iran will be able to export (see chart next page). Mr Trump's administration intends to punish any buyer of Iranian oil unless they are given a formal waiver. Penalties include preventing the buyer from operating in the US market, trading in US dollars or accessing the US financial system. Buyers of Iranian oil will also find it difficult to get their purchases insured. Given this, many buyers will acquiesce to US demands rather than continue purchasing Iranian crude. The EU has a mechanism in place to protect European interests from secondary sanctions, but it will still find it difficult to dissuade European companies from complying with US measures if the risk of incurring penalties is too great. Indeed, many firms have already started avoiding the Iranian market.

Price calculations

However, the halving of Iran's exports will have only a muted impact on global oil markets, partly because it will coincide with a global slowdown in demand growth for oil. We expect global consumption of petroleum products to increase by less than 1.5% in 2019, down from 1.7% in 2018, with the US, China and India all reporting slower growth. This compares with 1.8% growth in overall consumption of energy.

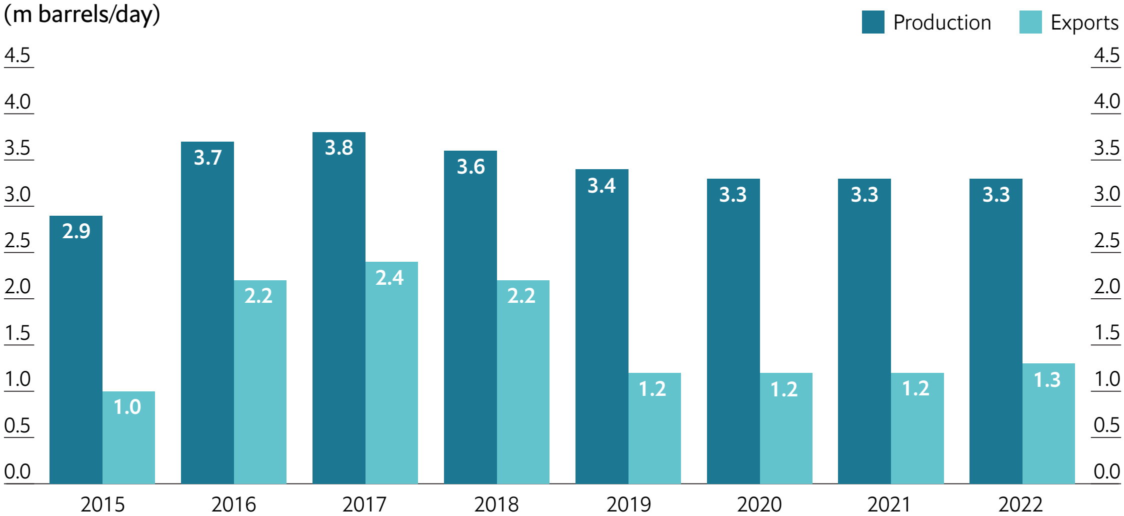
Anticipation of this slowdown in demand for petroleum, together with renewed oil stockpiling in the US and the issuing of waivers, has already pushed the price of Brent down from US$80/b in October 2018 to US$70/b in mid-November. We now estimate that Brent prices will average US$73.2/b in 2018 and expect them to average US$75.5/b in 2019 (compared with US$75.2/b and US$76.8/b previously).

Nevertheless, the extent to which Iranian supply is taken off the market will be a key issue for OPEC to watch in 2019, as it mulls how long it will keep in place its November 2016 agreement to cut output.

In September 2018 Saudi Arabia, with its non-OPEC partner Russia, rejected calls from Mr Trump to increase output, stating that the market was well supplied. The two producers had already increased output in June. Now OPEC is grappling with the possibility of an oversupplied market in 2019, amid slower demand growth, robust supply from non-OPEC sources (mainly the US) and more Iranian supply than expected, at least during the first half of the year. Even so, the loss of Iranian oil could still represent an upside risk to oil prices. If the cuts to exports go far deeper than forecast and if supply losses also occur elsewhere, such as in Venezuela or Libya, prices could yet spike.

Sanctions biting: Iran's crude oil production and exports

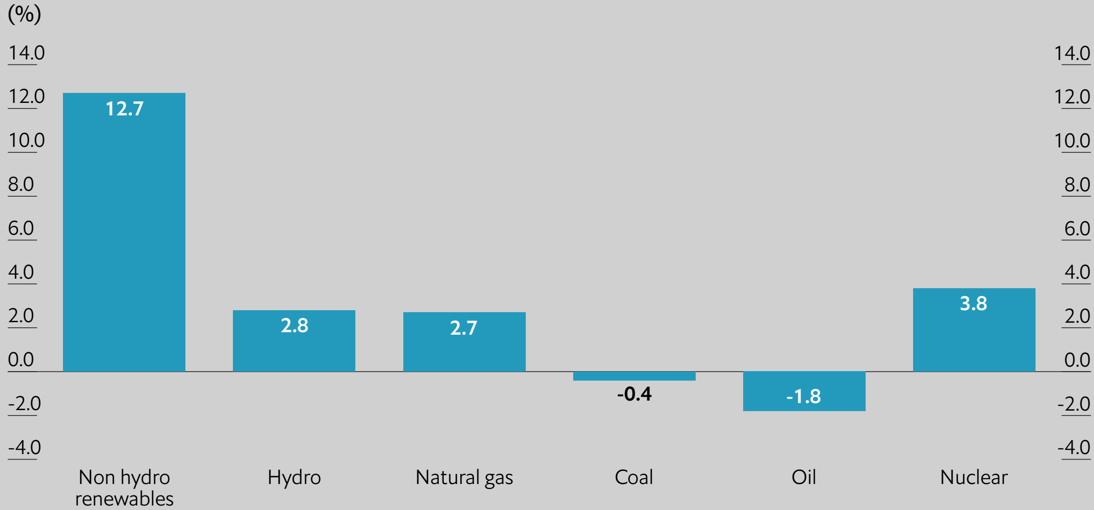
(m barrels/day)



Source: The Economist Intelligence Unit.

Global renewables: Gradual greening

Green power: electricity generation growth by source, 2019



Sources: The Economist Intelligence Unit; International Energy Agency © OECD/IEA 2018 IEA statistics, www.iea.org/statistics; Licence: www.iea.org.

Renewables will be the fastest-growing source of energy in 2019, driven by continued robust growth in solar and wind for power generation. In most major economies, power generation from renewables will be buoyed by the falling cost of deploying renewables technologies; by policy drivers such as targets, auctions and the use of feed-in tariffs; and by carbon pricing and trading. We forecast that global generation from non-hydro renewables will increase dramatically in 2019, driven mainly by growth in solar and wind power. By contrast, generation from other fuel sources will grow more slowly (see chart).

The expansion in the use of renewables will be driven in no small measure by China, as the country tries to wean itself off coal. China already accounts for a significant share of global wind and solar power capacity, and both private and public investment is rising rapidly. India, too, has ambitious targets for renewables, and especially for solar power (one government minister has said that 40 GW of solar and wind power could be added each year over the next ten years).

In western Europe, meanwhile, renewable energy deployment will be driven by national and regional policies and mandates (the EU has targeted renewables to supply 27% of final energy consumption by 2030). The UK and Denmark will expand their use of offshore wind power. In Germany, use of renewables reached a new record level in 2018 and is continuing to grow rapidly. Even coal-dependent Poland intends to pursue rapid development of offshore wind power.

In theory, the US should be the exception to this rule, given Mr Trump's decision to withdraw the US from the Paris Agreement on climate change. Despite the president's misgivings about green energy, however, the US Congress (the legislature) has maintained tax credits for wind and solar power. The outlook for solar is particularly bright, despite the imposition of tariffs on the import of Chinese solar panels. Overall, in North America we expect continued deployment of solar and wind capacity, while the US will continue to trim its coal use.

2019 calendar: Energy

January

14-17: World Future Energy Summit, Abu Dhabi, UAE
20-24: Arctic Frontiers, Tromso, Norway
24: Santos reports 2018 results

February

1: Ørsted reports 2018 results
1: ConocoPhillips reports 2018 results
6: BP reports 2018 results
7: Naturgy reports 2018 results
7: Equinor reports 2018 results
7: Peabody reports 2018 results
13-15: International Conference on Clean and Green Energy, Milan, Italy
21: OMV reports 2018 results
21: Novatek reports 2018 results
26: Sasol reports 2018/19 results
26: Eni reports 2018 results
26: Pemex reports 2018 results
27: Ecopetrol reports 2018 results
27: Acciona reports 2018 results
27: Pakistan Petroleum reports 2018/19 H1 results

March

2: Petronas reports 2018 results
5: Chevron security analyst meeting
8: Engie reports 2018 results
12: E.ON reports 2018 results
15: Petrobras reports 2018 results
19: Rosneft reports 2018 results
19-21: Oil and Gas Asia 2018, Karachi, Pakistan
22: Enel reports 2018 results
22: Petrochina reports 2018 results
27: Sinopec reports 2018 results
29: Orano reports 2018 results
29: UK leaves the EU unless extension to Article 50 process is agreed

April

4-5: 2019 MIT Energy Conference, Boston, US
12-23: CNOOC reports 2018 results
19-30: Energean reports 2018 results
26: Gazprom reports 2018 results

26: TEPCO reports 2018/19 results
27: CEPSA reports 2018 results

May

2-8: KEPCO reports 2018 results
6-9: Offshore Technology Conference, Houston, US
26-30: ONGC reports 2018/19 results

June

11-13: Global Petroleum Show, Calgary, Canada

July

11-25: Novatek reports 2018 H1 results
20: Enel reports 2019 H1 results
24: Peabody reports 2019 H1 results
26: Naturgy reports 2019 H1 results
26: Acciona reports 2019 H1 results
26: ConocoPhillips reports 2019 H1 results
26: Royal Dutch Shell reports 2019 H1 results
26: Total reports 2019 H1 results
26: Equinor reports 2019 H1 results
27: Orano reports 2019 H1 results
27: Engie reports 2019 H1 results
27: Eni reports 2019 H1 results
27: Exxon Mobil reports 2019 H1 results
27: Pemex reports 2019 H1 results
31: BP reports 2019 H1 results

August

2: OMV reports 2019 H1 results
3: Petrobras reports 2019 H1 results
3-4: Cepsa reports 2019 H1 results
7: Rosneft reports 2019 H1 results
8: E.ON reports 2019 H1 results
9: Ørsted reports 2019 H1 results
14: Ecopetrol reports 2019 H1 results
20-21: Sasol reports 2018/19 results
21-23: World Renewable Energy Technology Congress, New Delhi, India
23: Santos reports 2019 H1 results
24: CNOOC reports 2019 H1 results
27: Sinopec reports 2019 H1 results
29: Gazprom reports 2019 H1 results
30: Petronas reports 2019 H1 results
30: Petrochina reports 2019 H1 results

September

12: Energean reports 2019 H1 results

18: Pakistan Petroleum reports 2018/19 results

October

12: KEPC reports 2019 H1 results

27: ONGC reports 2019/20 H1 results

30: TEPCO reports 2019/20 H1 results

November

11-22: UN Climate Change Conference (COP 24), Katowice, Poland

Financial services in 2019: Bigger buffers

Financial firms face a variety of risks, but healthy profits and stricter regulation have made them more resilient.

Banks and money managers face dangers in 2019 from a variety of forces beyond their control. A global trade war, US monetary tightening and emerging-market volatility could all pose risks to commercial flows, inflation, investment and economic output, with knock-on effects for the global financial services sector. Unlike in 2008-09, however, we expect the global financial system to be strong enough to withstand the foreseeable shocks.

<u>Our key forecasts</u>

- We expect total loans and deposits in the global financial services sector to expand by 6% in 2019, twice as fast as in 2018.
- Trade barriers and interest-rate rises in the US will bring increased risks, however, particularly in emerging markets.
- The rollout of regulation will peak as the Basel III reforms come into full force in January 2019.
- The UK's exit from the EU in March 2019 could cost the country up to 80,000 financial services jobs as foreign banks decamp.

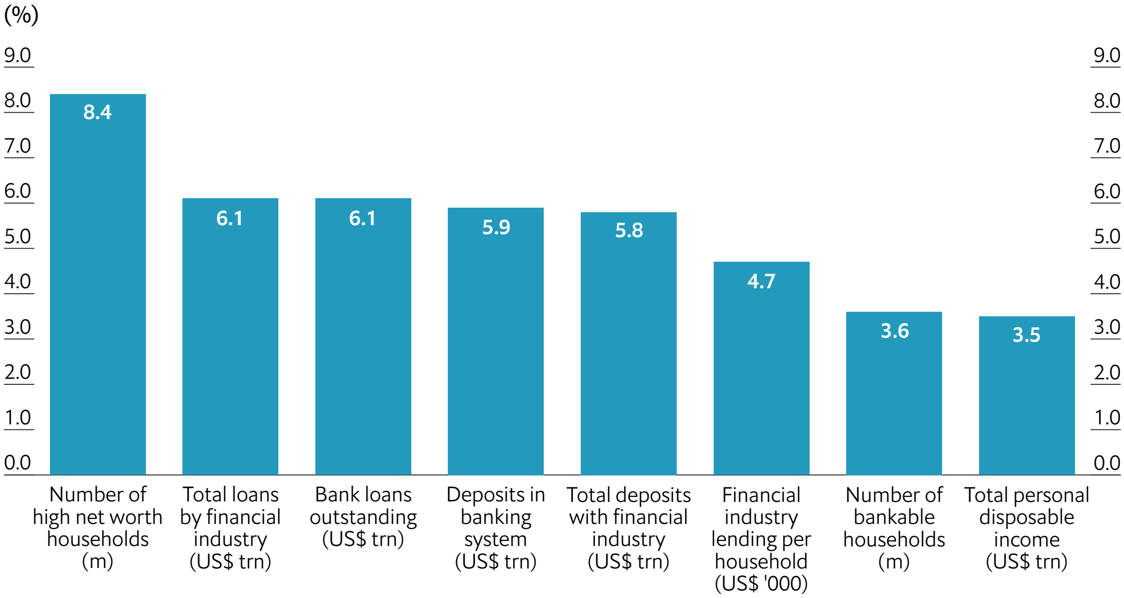
An emerging markets crisis?

The biggest risk to the financial services sector in 2019 stems from the US-China trade conflict, even though financial services companies are not directly involved. Other than within the EU's single market, financial business is rarely conducted under the terms of trade pacts. Moreover, cross-border financial services business between the US and China is limited. Nevertheless, profits at financial firms are tightly connected to GDP growth. They would find little shelter from a protracted commercial conflict between, and perhaps beyond, the world's two largest economies.

A second important danger—although it is not our central forecast—is the risk of a full-blown emerging-market crisis as global financial flows shift in response to a rise in US interest rates. We foresee the Federal Reserve (the US central bank) lifting its base rate three times more in 2019, while the UK is also due a rate rise in the second quarter. The European Central Bank and Japan are likely to hold off until 2020-21.

The tide of global funds flowing into the US has led to falling currencies and widening current-account deficits across the developing world, but so far there have been only a handful of crises—notably those in Argentina, Turkey and Pakistan. However, the additional rate rises that we expect in the US, and the tightening of the policy stance in the EU, could accelerate the flows. By contrast, a steadying of rates, or a fall in rich-world share prices, would attenuate it. One trigger would be if another major emerging market, like Russia or Brazil, were to enter a crisis. Another would be the escalation of current crises into banking sector meltdowns in Argentina or Turkey. Although the impacts would be most severe in the crisis-stricken economies themselves, lenders and investors with positions in them would also suffer.

Healthy finances: Global growth rates in 2019



Source: The Economist Intelligence Unit.

Within developed markets, higher interest rates are likely to dampen down the markets for housing and mortgages, as well as discouraging business investments made with borrowed money. However, on the positive side of the equation, financial firms generally benefit from moderately higher rates. Banks can widen the margin between the rates they pay to depositors and those they charge to borrowers. Insurers and money managers can shift their investment portfolios into newer, higher-yielding fixed-income securities. A bit of volatility bolsters trading—and hence trading revenue—in markets for shares, bonds, currencies and commodities.

Perils in Europe

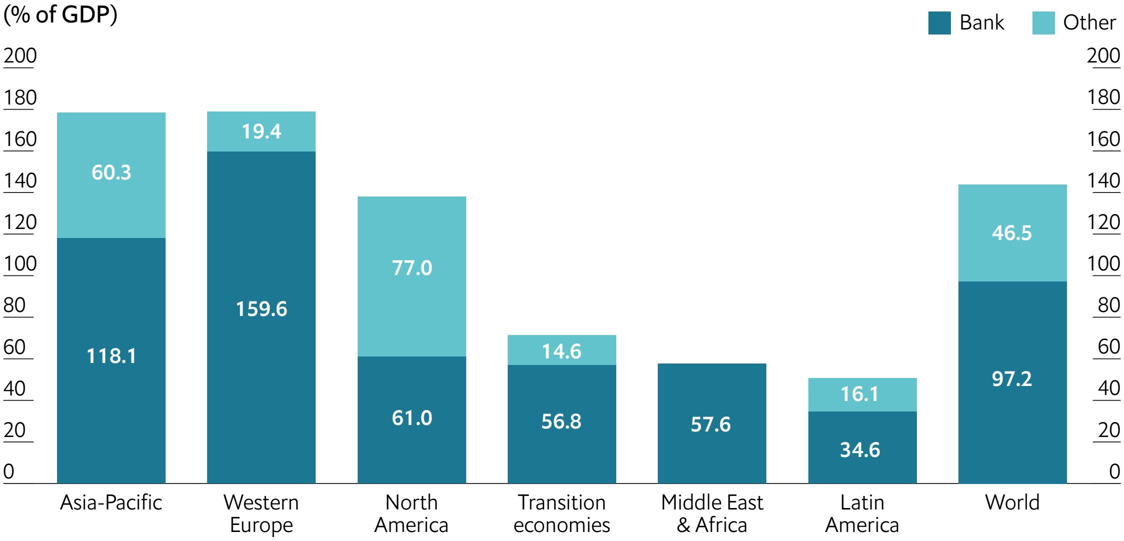
Although the EU as a whole has rebounded from its sovereign debt and banking crisis of a few years ago, the recovery has been uneven and dangers could easily reappear. Italy is a country that is big enough to matter, and its new government appears keen to take a confrontational approach to economic policy. It has proposed to boost spending and make tax cuts, driving up the budget deficit and adding to its already large pile of government debt. The plans have brought the government into conflict with the EU bureaucracy, which enforces limits on deficits in order to maintain the financial integrity of the euro area. It has also put pressure on the share prices and financing positions of weak Italian banks, which continue to be major owners of Italian government securities.

Although euro zone economies north of the Alps are in acceptable shape these days, some of their biggest banks are important financial market players in Italy and have large investment positions there. A full-blown crisis in Italy could set back lenders, particularly in France and Germany. It could even, in extreme circumstances, lead to a renewed movement for countries to leave the euro area. The UK's break with the EU (see box page 5) will also disrupt Europe's financial services sector, although London will bear the brunt of the problems.

More solid foundations

Although the date will pass largely unnoticed, the beginning of 2019 will mark a milestone in the reform of the global financial system. January 1st is the date by which countries are slated to have enacted the core Basel III banking reforms agreed to by the G20 group of major nations in the wake of the 2007-08 financial crisis. These include stiffer requirements for banks to retain base capital, holding more liquid assets in case they suffer a funding freeze, and operate under heightened regulatory oversight . Twice-yearly report cards from the Bank for International Settlements show that most G20 members are making steady progress on these reform, although not all are earning straight A grades. It is little short of remarkable that, despite international tensions and populist pressures, the world's major nations are carrying out a long-term co ordinated improvement of banking standards.

In debt: lending as % of GDP in 2019
(% of GDP)



Source: The Economist Intelligence Unit.

To meet the requirements, banks have bolstered their balance sheets by amassing more and better capital and making their cashflows less precarious. This has probably constrained their profitability, but it appears also to have bolstered their competitive position. Insurance companies, too, have strengthened in response to new rules like the EU's Solvency II, widely copied outside that economic bloc, which forced firms to hold more capital, for example through retaining earnings, to reduce the risk of insolvency.

Helped by their more solid finances, financial incumbents are seeing off what once seemed like a dire threat from more nimble financial technology (fintech) firms. Instead, the financial services sector itself has learnt a few tricks in terms of innovation, often purchasing or allying with start-ups . Many of these insurgents have lacked financial depth or have crafted business models that have worked well only in ideal market conditions.

The exception is in China, where fintech companies such as Alipay are likely to increase their dominance in 2019 unless they are held back by regulators. Even there, financial services companies should be well placed to fight back—as long as they can withstand the wider geopolitical and economic ructions that 2019 will bring.

UK finance: Brexit and the City

Most financial firms have already accepted that Brexit, which formally take place on March 29th, will sever the single market in financial services shared by the UK with the rest of the EU. Provided that the UK and the EU can come to a negotiated break-up, financial firms will have passporting rights to operate across borders out of the UK, or into it, through the end of 2020 . However, early UK hopes of securing a "mutual recognition" deal that would allow for business as usual have been scuppered. There is still the possibility of "equivalence", in which the EU would alone decide whether it wanted to grant market access. This provision appears not to offer the security that most financial firms require, however.

As a result, the UK-based firms that rely on passporting—including many US and Asian banks that use London as their European base—have already moved to establish licensed subsidiaries in locations within the EU27. From 2019, much of their EU business will be conducted from Frankfurt, Paris, Dublin, Luxembourg, Amsterdam or elsewhere. Managers of newly granted business licences report that the French and German authorities have been keen to award them but have been thorough in their vetting. As for the reverse move, most continental European firms already have the necessary UK subsidiaries to conduct post-Brexit business .

There is no consensus on how many jobs the British financial sector will lose due to Brexit. The City of London Corporation has estimated the losses at between 5,000 and 13,000, but other thoughtful estimates run much higher. One key variable is the timeframe for each forecast. Although the number of announced job losses is low so far, the shift in jobs is likely to occur over a long period, perhaps a decade. Many of the losses will not be announced in advance, but will instead become clear as data on staffing, revenue and taxes emerge. So too will the knock-on effects on other sectors, including consultancies, retailers and the housing market.

The financial services industry is, after all, Britain's largest economic sector, generating 6.3% of GDP and 3.2% of total employment in 2017. It provides £70bn a year in tax revenue. If financial sector activities, and jobs, shift over time to other European countries as we anticipate, the UK could lose around 80,000 jobs, pushing the sector's share of the labour force down to 3%. However, the UK should remain a major global financial centre.

A more immediate risk come March 2019, however, is that many existing financial contracts could become invalid if clauses around jurisdiction no longer hold after a no-deal Brexit. In October 2018 the Bank of England (the UK central bank) issued a warned that this could affect £69trn in insurance, derivatives and other contracts. Although companies are working to reduce these risks, many appear to have been banking on a Brexit deal that is now looking increasingly unlikely.

2019 calendar: Financial services

January

1: Basel III takes full effect

1: European Banking Authority final guidelines on fraud reporting under PSD2 apply.

14: Citigroup reports 2018 results

15: Wells Fargo reports 2018 results

15: JPMorgan reports 2018 results

16: Bank of America reports 2018 results

21: UBS reports 2018 results

23: Bank of Japan releases outlook

29-30: First US Federal Reserve meeting of the year (Federal Open Market Committee)

30: Santander reports 2018 results

February

1: Deutsche Bank reports 2018 results

6: Nordea reports 2018 results

6: Raiffeisen reports 2018 results

12: Investing for Impact 2019, Economist Events, New York, US

14: Credit Suisse reports 2018 results

15: Allianz reports 2018 results

19: HSBC reports 2018 results

20: Lloyds report 2018 results

21: Barclays reports 2018 results

26: Standard Chartered reports 2018 results

March

14: Islamic Finance Summit, Economist Events, Kuala Lumpur, Malaysia

19-20: US Federal Reserve Meeting (Summary of Economic Projections)

29: UK leaves the EU unless extension to Article 50 process is agreed

31: Deadline for Indian banks to conform to Basel III

April

15-17: The Financial Brand Forum 2019, Las Vegas, US

25: Bank of Japan releases outlook

30-May 1: US Federal Reserve meeting

May

15-17: FINRA Annual Conference, Washington DC, US

June

18-19: US Federal Reserve meeting, Washington DC, US

27: General Council meeting of the European Central Bank, Frankfurt, Germany

July:

30: Bank of Japan releases outlook

30-31: US Federal Reserve meeting

September

17-18: US Federal Reserve meeting

October

29-30: US Federal Reserve meeting

31: Bank of Japan releases outlook

December

10-11: US Federal Reserve meeting

Healthcare in 2019: Health checks

Trade tensions and political pressures will fail to derail long-term progress in the healthcare and pharmaceuticals sector.

The political events of the past two years have brought considerable uncertainty to the global healthcare sector. That will continue in 2019. In the US, efforts to rein back state involvement in the health sector mean that from January 1st it will no longer be mandatory for individuals to buy insurance. In Europe, Brexit is likely to bring disruption to pharmaceutical markets, healthcare recruitment and research in the life sciences. In China, the government will continue to push through far-reaching reforms to all aspects of healthcare, as it tries to stem a rise in non-communicable diseases. And in nearly every market drug pricing will remain under pressure from strained healthcare budgets. None of this will prevent healthcare spending and pharmaceutical sales from rising in most markets, although the market will be weighed down by weaker economic growth.

Our key forecasts

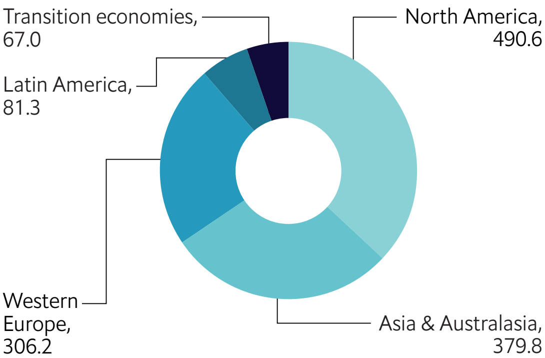
- Healthcare spending will climb by 5.1% worldwide in nominal US dollar terms, down from 8.2% growth in 2018.
- This will include a 5.7% rise in spending on pharmaceuticals in 2019, down from 6.3% in 2018.
- While the US will move away from universal healthcare, many other countries, including South Africa, Oman, India and Nigeria, will seek to widen and deepen their public insurance systems.

Healthy progress

The underlying expectations for the healthcare sector in 2019 are mostly positive, regardless of world events. Life expectancy in the 60 countries covered by our global forecast will tick upwards again, adding an extra two months, to reach 73.7 years. Every single country will benefit, including South Africa—where life expectancy has been recovering since 2010 as AIDS treatment is rolled out. Infant mortality rates, meanwhile, will carry on declining nearly everywhere, thanks to better neonatal care and wider vaccination programmes. As a result of improving health, the global population will grow by 0.8%, while the number of people aged over 65 will rise by 3.5%.

Although many of these gains will come from economic growth and improving living standards, the rollout of healthcare systems will also play a role. We forecast that global health spending

US and them: Pharmaceutical spending, 2019
(US$ bn)



Sources: The Economist Intelligence Unit; World Health Organisation.

will rise yet again, increasing by 5.1% in nominal US dollar terms. Drivers will include the expansion of healthcare coverage in developing markets, the increasing care needs of elderly populations, and advances in treatments and health technologies. Healthcare workers should also benefit from pay rises in all but the most cash-strapped countries, amid growing international competition for healthcare staff. Pharmaceutical sales will rise by 5.7% amid strong demand—and despite the continuing pressure on prices.

Not spared

Yet despite this steady growth, the healthcare sector will still be vulnerable to disruption. Global trade tensions will not target the sector specifically—most developed markets maintain zero tariffs on pharmaceuticals, while even emerging markets keep them low. Nevertheless, the industry has not been entirely sheltered from the US-China trade tensions (see box page 5). The US has imposed tariffs on some medical technology imports from China, as well as on some active pharmaceutical ingredients (APIs). That could backfire if US pharma companies end up paying more for APIs or failing to find alternative suppliers. China, in contrast, has dropped tariffs on some of its medicine imports, particularly those for cancer.

Brexit, meanwhile, still poses considerable risks for the UK's healthcare sector and its important life sciences industry. The European Medicines Agency will move from the UK capital, London, to the Dutch city of Amsterdam by the end of March 2019, and there remains huge uncertainty about how regulations surrounding drug approvals, clinical trials and drug safety will change. If a transition deal is secured, it could stave off the immediate need to stockpile drugs in case they are held up at the border in March. However, it will not solve longer-term problems, including whether the UK will still be able to secure enough research and development (R&D) funding or staff and whether its pharma companies will need to reroute their supply chains. The UK's National Health Service has also become reliant on EU staff to plug gaps during the past decade. It will now need to lure workers in from further afield.

The biggest trade risk, however, is the indirect one: whether a global trade war will slow the world economy. Many governments, particularly in the euro zone and in commodity-dependent economies, are only just emerging from a period of austerity that obliged them to rein back healthcare spending. Expenditure carried on rising regardless in nominal terms in most countries, but often failed to keep up with increasing demand for care. The strains on public health systems are still clear, meaning that there is limited room for more cost-cutting measures. This is particularly true in countries struggling with population ageing, including Japan, South Korea and most of western Europe.

Universal pressures

In most countries, however, governments will remain keen to improve access to healthcare in 2019, often by expanding or deepening public insurance. South Africa is aiming to pass its long-awaited law on a national health insurance system in 2019, with a view to rolling it out by 2025. Oman's government has also said that it aims to introduce mandatory health insurance next year, although it will struggle to implement this by January as hoped. In Nigeria, the government approved a basic public health package in 2018 and will start to roll this out during 2019. It is aiming for universal healthcare by 2030.

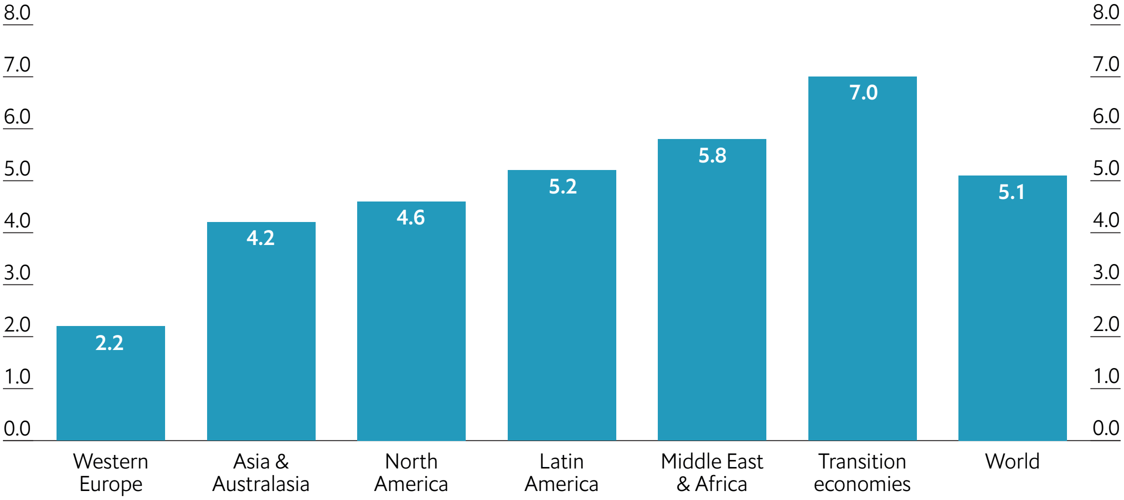
China, meanwhile, long ago set itself some ambitious health goals for 2020, by which year it aims to provide "safe, effective, convenient and affordable" healthcare to all residents. In 2019 it will scurry to implement yet more far-reaching reforms in an effort to promote this ideal. It has already been working hard to strengthen competition in the pharmaceuticals sector, reforming the distribution chain and attempting to prevent providers from demanding extra payments from patients. These efforts will continue next year, with the new National Health Commission (set up in March 2018) taking the lead. China has said that its priorities include better-trained general practitioners, a robust referral system that directs people to the right specialists, and raising health awareness among the population.

Going against the trend, as so often, is the US. Although efforts by the administration of the president, Donald Trump, to repeal and replace the 2010 Patient Protection and Affordable Care Act (known informally as Obamacare) have failed, his administration has used piecemeal legislation to reverse some of the law's provisions. Most importantly, tax reforms in December 2017 mean that from January 2019 Americans will no longer face a penalty if they do not buy health insurance, eliminating the individual mandate. This will widen choice, but will also undermine the risk-sharing principles that underpinned Obamacare. The administration claims that enrolment will rise, while many other commentators say it will fall.

The US will also step up its pressure on pharmaceutical companies to reduce their prices. While other counties have been bearing down on pharma prices for years, prices in the US have carried on climbing. This is partly because Medicaid and Medicare, the federal funds for low-income people and the elderly respectively, have been barred from considering prices when it comes to reimbursement decisions. That is starting to change and could alter further in 2019, although the idea of "health rationing" remains hugely controversial.

Even if pricing pressures increase in the US, it will remain by far the world's biggest pharmaceutical market, accounting for around one-third of the global total (see chart). Moreover, the US pharmaceutical industry will continue to be buoyed by the tax reforms passed in November 2017, which helped to free up more money for investment in R&D. Innovations will continue to emerge: in 2019 US scientists are likely to begin their first trials using CRISPR, a gene-editing technique that holds huge potential. With artificial intelligence, robotics, stem cells and other technologies also developing, the world's health should continue to improve.

Russian recovery: health spending growth in 2019
(% change in nominal US$)



Source: The Economist Intelligence Unit.

US-China: Medtech rivals

Although the pharmaceutical industry was mostly spared, the medical technology (medtech) sector became embroiled in the US-China trade dispute during 2018. The first tranche of US tariffs, which came into effect in July, affected Chinese medtech imports worth around US$1bn a year—roughly one-fifth of all US medtech imports from China. For its part, China has imposed tariffs in the range of 5% to 25% on US imports in 33 medtech product categories, ranging from low-value medical consumables such as syringes to high-value items such as computed tomography (CT) equipment.

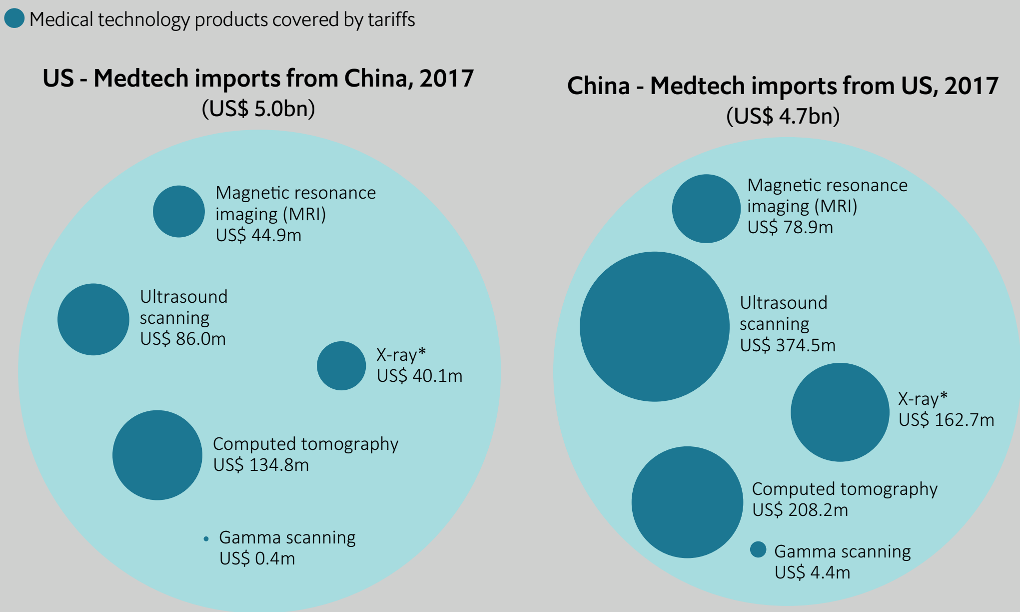
On both sides, the tariffs were intended to benefit domestic companies at the expense of foreign rivals by raising import costs. However, this aim ignores the role of global supply chains in the medtech sector. Global medtech companies with operations and manufacturing facilities in both the US and China have been caught in the middle, with those in the medical-imaging sector the clearest casualties. With the US now likely to impose a fourth round of tariffs in December or January, the trade risks to other segments will increase in 2019.

The battle over medical imaging

The Made in China 2025 plan, which aims to develop particular industries in China, has been a focus of US tariffs. So far, those tariffs have targeted only one of the many medtech categories identified under the plan: imaging equipment. This is China's biggest medtech market segment and the US is a major buyer, not only of finished products but also of inputs.

The Medical Imaging & Technology Alliance (MITA), an industry association in the US, estimates that US tariffs will cost imaging companies in the US about US$138m a year, by raising the cost of supplies. In order to pay for this, medical-imaging industry representatives surveyed by MITA say that they will have to reduce investment in research and development, hurting the competitiveness of their products in global markets.

US-China trade tariffs on medical-imaging technology and equipment



*X-ray equipment for medical, surgical and veterinary use
Sources: Flexport; Ministry of Finance (China); US Census; United States Trade Representative (USTR).

It will become even more challenging for multinationals to grasp opportunities in the fast-growing imaging market in China, where The Economist Intelligence Unit expects recent healthcare reforms to expand and develop the infrastructure for imaging.

Medtech segments at risk

Forecasting all the trade risks to other medtech market segments in 2019 is difficult. Areas where intensifying competition between the US and China can be expected—either owing to government policies such as the Made in China 2025 plan, or as a result of medtech companies driving activity and innovation in fast-growing, lucrative markets—are likely spaces for fresh trade tensions to emerge.

The other medtech areas where China wants to boost local development of high-performance, high-value medical devices include medical robots, high-value medical consumables (such as degradable vascular stents), remote diagnosis and treatment devices and gene sequencing technologies. As with medical imaging, it is the sectors that are growing rapidly that are most likely to be targeted by tariffs.

These include CT equipment. In the past five years, US imports of Chinese CT equipment have doubled, from US$64m in 2012 to almost US$135m in 2017. As a result, China has overtaken Japan as the second-largest exporter of CT equipment to the US. Chinese companies such as Shanghai United Imaging now offer buyers a wide choice of good-quality and innovative imaging equipment.

Other segments that the US may target include in-vitro diagnostics (IVD) and high-value medical consumables. These are sectors where Chinese companies have emerged as strong competitors in recent years and are hot on the heels of global market leaders. According to analysis by EIU Healthcare, four of the top ten companies in China's IVD market are domestic firms, whose sales growth has outpaced that of foreign rivals. The fast-growing companies in major IVD market segments, such as molecular diagnostics and point-of-care testing, are all domestic players.

Chinese medtech companies are increasingly winning a larger share not just of their domestic market but also of overseas markets, and are doing so in higher-value segments. During 2019 that may put them at risk from the US-China trade dispute.

2019 calendar: Healthcare and pharmaceuticals

January

Gilead to launch generic sofosbuvir (Sovaldi)

Deadline for Brazil's Anvisa to clear backlog of generic approvals

21: US implements revised Common Rule for clinical trials

24: Bristol-Myers Squibb reports 2018 results

29: Pfizer report 2018 results

30: Novartis reports 2018 results

31: Roche reports 2018 results

February

5: Gilead reports 2018 results

6: GlaxoSmithKline 2018 results

7: Sanofi reports 2018 results

9: EU's Falsified Medicines Directive comes into force

13: Eli Lilly reports 2018 results

14: AstraZeneca reports 2018 results

21: Patient Value Summit, Economist Events, Brussels, Belgium

27: Bayer reports 2018 results

March

6-7: European Pharma CI Conference, Milan, Italy

7: Merck KGaA reports 2018 results

12: War on Cancer Middle East, Economist Events, Dubai, UAE

18-20: 18th World Pharma Congress, Edinburgh, UK

24: WHO World TB Day

28: War on Cancer Asia, Economist Events, Singapore

29: UK leaves the EU unless extension to Article 50 process is agreed

29: Deadline for European Medicines Agency to move from London to Amsterdam

April

4-6: HIV and Hepatitis in the Americas, Bogota, Colombia

7: World Health Day

24-30: WHO World Immunisation Week

25: WHO World Malaria Day

28-May 1: 16th Annual World Health Care Congress, Washington, DC

May

8-9: 11th Asia Pacific Global Summit on Healthcare, Tokyo, Japan

18-22: ISPOR 24th Annual International Meeting, New Orleans, US

20-28: 72nd World Health Assembly, Geneva, Switzerland

27-29: 15th International Conference on Health and Primary Care, Barcelona, Spain

14: WHO World No Tobacco Day

June
14: WHO World Blood Donor Day
17-21: World Preclinical Congress, Boston, US
28: WHO World Hepatitis Day

August
22-23: 21st International Conference on Medical, Biological and Pharmaceutical Sciences, Kuala Lumpur, Malaysia

September
16-19: WHO Regional Committee for Europe, Copenhagen, Denmark

November
12-18: WHO Antibiotics Awareness Week

December
1: WHO World AIDS Day

Telecoms in 2019: Are we secure?

Cyber-attacks, stuttering revenue and heavy investment needs will be the main risks facing the telecoms sector in 2019.

The world of technological innovation is, by its nature, disruptive and there are plenty of disruptions on the horizon in 2019. The biggest will emerge from the rollout of fifth-generation (5G) networks, which will help to support the development of a sharing economy, autonomous technology, artificial intelligence (AI), big data analytics and an expanding internet of things ecosystem. Most of these disruptions will, in the end, be positive, but in 2019 we will also see increased risks.

Our key forecasts

- Global mobile-phone penetration will grow only slightly in 2019, to 117 per 100, from 114 per 100 in 2018, owing to market saturation. Instead of enticing new subscribers, companies are promoting value-added mobile services that will bolster average revenue per user (ARPU).
- A nervy geopolitical environment, US-China trade tensions and an uncertain Brexit outlook could result in exchange-rate fluctuations that stifle investment in technological innovations and M&A activity, jeopardising telecommunications sector growth in 2019.
- A host of major data breaches in 2018 have highlighted the risks of cyber-attacks as regulators and the private sector struggle to respond effectively. In 2019 this could undermine consumer confidence in electronic communications and transactions. In a worst-case scenario, it could also cripple national infrastructure and slash global growth prospects.

Phone numbers

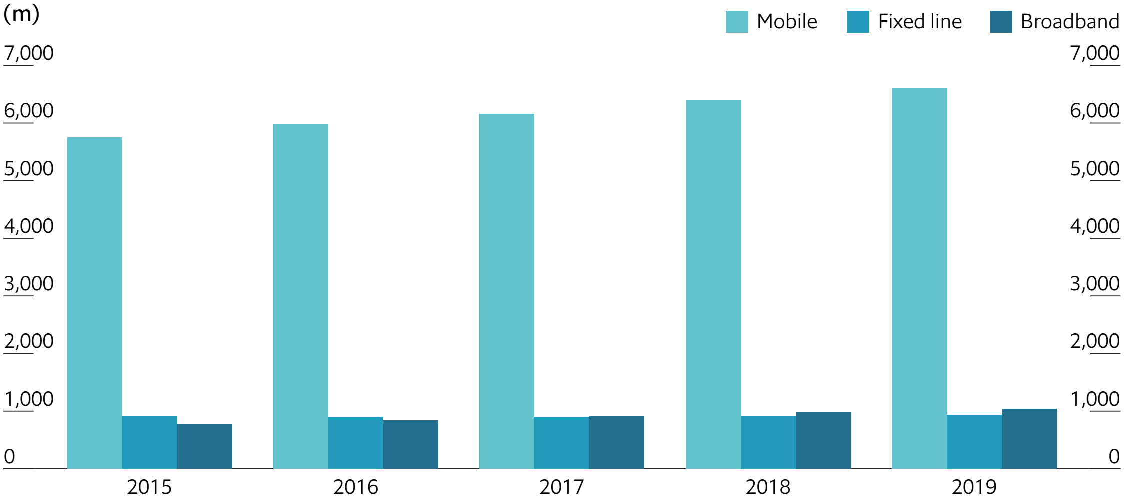
Demand for internet services is already high globally and will increase further in 2019. Businesses in all sectors are using more agile and sophisticated technology to make operations more efficient or to open up new revenue streams. Consumers, too, are turning to smartphones, tablets and wearables in ever greater numbers, stoking demand for data and forcing operators and technology companies to accommodate increasingly digitally driven lifestyles.

Mobile subscriber numbers across the 60 countries covered by our forecasts are expected to rise to 6.6bn in 2019, up from 6.4bn in 2018. Internet user penetration is also set to rise steadily to 61.3 connections per 100 population in 2019, while broadband penetration will see steady growth too, albeit from a smaller base, to 18.4 per 100 population in 2019. Many developing nations continue to push for greater internet coverage, especially among rural populations, while networks in mature markets focus on providing greater speed.

Tentative steps towards 5G

Much of this developed-market growth will come from the expansion of 5G in 2019. Co-operation and partnerships between technology companies, manufacturers and operators has ensured that

Phone numbers: global subscriptions



Sources: The Economist Intelligence Unit.

commercial 5G networks will start rolling out in several markets next year. In the UK, EE aims to roll out a 5G network by October 2019, well in advance of plans outlined by most European rivals. In the US, Sprint is preparing for 5G rollout in nine states in the first half of 2019, while its competitor, T-Mobile, is also looking at an initial rollout next year. Device manufacturers, too, will be ready to deploy 5G-ready smartphones, with Motorola and LG scheduling launches for 2019.

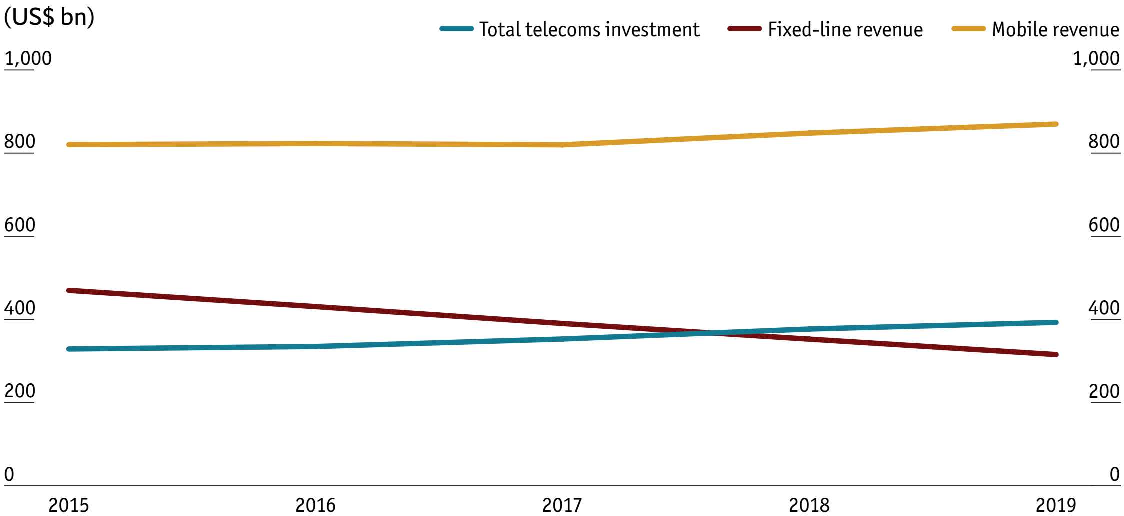
These developments will be supported by government policies in many markets. In particular, both China and the US see the development of 5G as an issue of national security, as they vie for technological supremacy and try to prevent each other from gaining the upper hand. Even so, 5G is likely to be hampered by a combination of technological obstacles and an underdeveloped regulatory framework. There remains, for example, no technical definition of what constitutes a 5G standard, with some telecoms operators using the term purely as a marketing tool.

There will also be revenue, cost and cashflow challenges for 5G operators, given that it is unclear how much consumers and businesses will be willing to pay for higher internet speeds and greater bandwidth. Moreover, 5G rollouts will require a mix of technologies, as operators work to tackle range and coverage shortfalls. All of these technologies will entail significant investment.

At the same time, operators will need to contend with increasing levels of competition, decreasing voice revenue, and slimmer margins from broadband and mobile packages. Overall telecoms revenue is set to fall slightly in 2019, to US$1.18trn, from US$1.2trn in 2018. Regulatory uncertainty, consumer demand for investment in next-generation technology and the search for new revenue streams will further constrain earnings potential. Despite this, mobile revenue will rise from US$848bn in 2018 to US$870bn in 2019, even as ARPU stalls. This revenue growth will be vital to fund the rollout of networks.

Even so, finances will be tight. Many operators will continue to push for consolidation, as a way to fund the testing and rollout of fibre broadband and 5G. If stockmarket values fall and interest rates rise in 2019, however, raising the financing for such deals may become more difficult. Some operators will instead opt for network-sharing agreements, which offer temporary respite. Others will have to lay off staff in a bid to improve productivity and operational efficiency. Developments in AI could accelerate that trend beyond 2019.

Delicate balance: telecoms investment and revenues



Source: The Economist Intelligence Unit.

Vulnerable to attack

Technical problems aside, however, increasing connectivity will also raise difficult questions in terms of cybersecurity, lifestyles and ethics. Much has been made of how advances in autonomous-vehicle technology will reshape transport use. But the technology may end up exacerbating problems of congestion, poor air quality and physical inactivity in cities around the globe. The ethical considerations, meanwhile, were highlighted by the death of a pedestrian in Arizona in 2018. If car technology is making life-or-death decisions, then what guidelines need to be programmed in and who will be liable for mistakes? This debate will rage on during 2019.

Security will, however, be an even bigger issue in 2019, bringing into sharp focus the trade-offs involved in advanced connectivity. Severe breaches at Facebook and in the Singaporean healthcare system during 2018 were just the latest in a long line of incidents. A large cyber-attack, particularly against the financial system, health systems or crucial energy assets, could pose a significant geopolitical risk. Even an attack on a company could cripple supply chains at all levels of society, from transport to food distribution.

In 2019 many countries will respond to this threat by using regulations to maintain network security, which arguably lags too far behind the speed of technological advances. In the US, the National Defense Authorization Act will include efforts to improve cybersecurity in both the military and civilian life. In the EU, member states will be putting into action the requirements of the 2016 Directive on Security of Network and Information Systems, which includes the establishment of a regional cybersecurity agency.

Vietnam, meanwhile, will in January 2019 implement a cybersecurity law that obliges telecoms and internet service providers to monitor any cyber activity that could disrupt national security, public order, or the reputations of any organisation or individual. The controversy over this law highlights the ways in which concern for cybersecurity may topple over into political controls. This has worrying echoes of the cybersecurity law introduced in China in 2017, which, rather than securing internet safety, has impeded access to information. That is an issue that will become even more high-profile in 2019.

India telecoms: A market under stress

On the face of it, India's telecoms market will enjoy strong growth in 2019. The number of mobile subscribers will rise by 4.2%, while broadband subscribers (most of whom access the internet via smartphones) will rise by 14%. But this is a market under severe pressure. An aggressive pricing strategy by a newcomer, Reliance Jio, has cut into revenue streams, cashflow and profitability across the industry. Many of Jio's rivals are imploring the government to help them find a way out during 2019.

Jio's growth has been astonishing. In little over two years the company has grown to become the second-biggest operator in India in terms of adjusted gross revenue, surpassing Bharti Airtel in early October 2018. In first place is Vodafone Idea, recently formed from the merger of the Vodafone and Idea businesses. The combined company now boasts a 38% share of the subscriber market, compared with Airtel's 32% share and Jio's 18%.

Yet the merger itself points to the cutthroat pricing competition between the three providers, as Jio used ultra-cheap—or sometimes even free—subscription packages to build up its market share. While consumers benefited, Jio's rivals saw their finances drained. The industry's debt is estimated at Rs7.7trn (US$112bn), according to the Indian Banks' Association, and it owes about Rs3trn to the government in spectrum payments.

Over the coming year the pressures could be exacerbated by the government's decision in October 2018 to double the customs duties on network equipment to 20% and to impose an additional 10% tariff on some other telecoms imports. In the same month, the Ministry of Telecommunications announced a probe into whether telecoms companies have been under-reporting their revenue. If so, they may owe additional spectrum fees.

Exactly how long the sector can hold out for under these conditions is a matter of debate. But during 2019 providers are due to roll out more next-generation technology, such as fibre broadband and 5G. This involves heavy investment that may end up forcing them to cut research and development and shed jobs, or even quit the market entirely. A more stringent approach to spectrum acquisition—approved in a government policy document published in September—is a start, but it may not be enough.

2019 calendar: Telecoms

January

8-11: The International Consumer Electronics Show (CES 2019), Las Vegas, US

25: Ericsson reports 2018 results

30-31: World Congress on Wireless Technology, Osaka, Japan

31: Elisa reports 2018 results

February

7: Millicom reports 2018 results

13-15: International Exhibition & Conference for Internet of Things, Riyadh, Saudi Arabia

21: Deutsche Telekom reports 2018 results

22-23: Global Meeting on Big Data Analytics and Data Processing, Bangkok, Thailand

25-28: Mobile World Congress, Barcelona, Spain

March

25-27: Telecoms World Asia, Bangkok, Thailand

27-28: IoT Asia 2019, Singapore

29: UK leaves the EU unless extension to Article 50 process is agreed

April

2-3: Gigabit Access, Cologne, Italy

8-12: WSIS Forum 2019, Geneva, Switzerland

25: Ericsson reports Q1 2019 results

25-26: IoT Tech Expo Global, London, UK

May

9: Deutsche Telekom reports Q1 2019 results

17: World Telecommunication Day (UN)

21 (TBC): Vodafone reports 2019 results

June

20-21: 5th International Conference on Wireless, Telecommunication & IoT, Rome, Italy

July

17: Ericsson reports Q2 2019 results

31-Aug 1: China International Internet of Things Exhibition, Shenzhen, China.

September

6-11: IFA Consumer Electronics trade show, Berlin, Germany

TBC: ITU Telecom World 2019, Budapest, Hungary

October

14-15: 6th World Machine Learning and Deep Learning Congress, Helsinki, Finland

18: Ericsson reports Q3 2019 results

28-Nov 22: World Radiocommunication Conference 2019, Sharm El Sheikh, Egypt

November

7: Deutsche Telekom reports Q3 2019 results

25-27: World Telecommunication/ICT Indicators Symposium (WTIS-19)

December

11 (TBC): Vodafone reports half-year 2020 results

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