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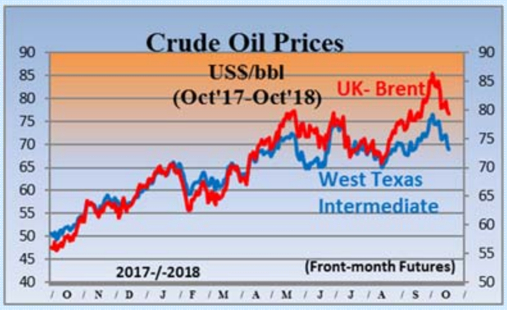
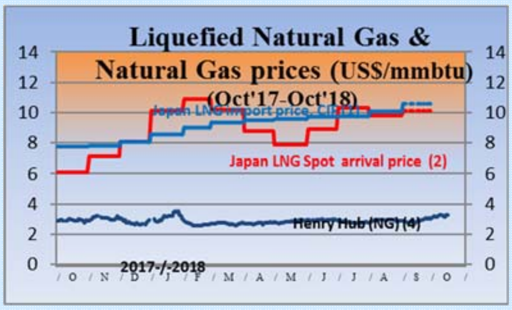


Source: DOE-EIA, Financial Times, NASDAQ



Sources:
(1) Ministry of Finance "Japan Trade Statistics"
(2) Ministry of Economy, Trade and Industry
(contract month basis)
(3) Estimated by World Bank and World Gas Intelligence
(4) DOE-EIA, NYMEX (Front-month Futures)
(5) Investing.com

Source: x-rates.com

Source: Financial Times

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1. US: Intensifying Trade War and Its Impact on the US High-Tech Industry

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An additional 10% tariff on $200 billion worth of Chinese goods has taken effect. This comes in addition to the 25% tariff already in effect for $50 billion worth of goods and is scheduled to be raised to 25% from January 2019. The US-China trade war is escalating with China announcing retaliatory measures that include American LNG and the United States threatening to impose additional tariffs on all imports from China if the country goes ahead with retaliatory measures. Chinese companies with LNG purchase contracts have reportedly stopped receiving their cargoes immediately and switched to spot purchases. There is concern that new liquefaction plant projects in the US may be delayed due to the need to secure buyers other than China.

The aim of the US is to make China withdraw “Made in China 2025,” the government-led initiative to foster high-tech manufacturing announced in 2015. The US is wary of the initiative as it aims to increase domestic content in China to 70% in high-tech industries by 2049 using whatever means possible, including subsidies, investing in and acquiring foreign companies, and forcing foreign enterprises in China to transfer their technologies to the country to boost the country’s competitiveness in EVs, IT, communications, AI, aviation, electric and electronic appliances, biotech, and other areas. The initiative had been discussed in the US-China Strategic and Economic Dialog (SED) under the Obama administration. However, US industry had grown impatient with the lack of virtual progress of the dialog and had apparently been hoping that the next administration would reset the negotiations. If the Trump administration works to fulfill such hopes and China relents, its re-election chances will be boosted.

Meanwhile, if the United States and China continue to impose additional tariffs on one another, China will run out of goods to tax before the US does in light of the countries’ trade volumes. Non-tariff measures that China could take instead include limiting exports of components and materials to US companies. If executed, this would hit the US high-tech industry the hardest as the computers and electronic devices used by the industry have the highest differential between imports and exports.

The high-tech industry is traditionally a strong support base for the Democratic Party, and respects the privacy of individuals and the rights of consumers, and welcomes highly skilled immigrants. It also tends to respect diversity in race, religion, and sexual orientation. The industry began to be alarmed by the Trump administration during the 2016 election campaign when it backed limiting immigration, and opposed the administration’s restrictions on refugees and immigrants and anti-LGBT policies that were issued soon after inauguration and saw its hostility toward the media as an infringement on freedom of speech. The industry also grew increasingly frustrated by Trump’s efforts to overturn the Obama administration’s health care policies and backpedaling on climate action. The industry is compromising with the administration in some areas, including Apple’s success in negotiating for an exemption from additional tariffs, but is united in its support of Democratic candidates for the 2018 mid-term election and the 2020 presidential election.

High-tech companies are on course to become a central player alongside automobile companies in the auto industry which is a key sector for all car-producing countries. How will the United States handle its high-tech industry as it affects employment no longer just through the shift to overseas component suppliers but also by automation and the replacement of humans? This question must be asked not only of the Trump administration which persists in keeping jobs within the country but also the Democratic Party for which labor unions are a support base, albeit perhaps to a lesser extent than before.

2. EU: Phase-out of Coal and Efforts on the Iran Issue

Kei Shimogori, Researcher
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On September 12, European Commission President Jean-Claude Juncker delivered his 2018 State of the Union Address in the plenary session of the European Parliament. Regarding energy, he referred to an Energy Union with a forward-looking climate policy in the context of completing the ongoing initiatives. Energy was not addressed directly as one of the 18 actions that the European Commission adopted together with the Address, but investing in renewable energy in Africa was mentioned as an energy-related area.

In the area of climate action by the EU, UN Special Envoy for Climate Action and Bloomberg Philanthropies founder Michael R. Bloomberg and European Commissioner for Climate Action and Energy Miguel Arias Cañete pledged to join forces to manage the global transition away from coal. This partnership will build on the European Commission's Platform for Coal Regions in Transition. The EU is working to ensure that no region within its boundaries falls behind in shifting away from a fossil fuel-based economy. It plans to support the development of projects for kick-starting economically and technically feasible transitions through the platform. Bloomberg Philanthropies will conduct plant-by-plant analysis of coal power to improve the knowledge base of the platform and achieve more targeted actions. This initiative will accelerate the transition of the entire EU away from coal, despite differences in levels of engagement among member states.

Meanwhile, the EU has been maintaining a consistent policy toward the Joint Comprehensive Plan of Action (JCPOA) on Iran's nuclear development since May, taking countermeasures against the US regarding the re-introduction of economic sanctions against Iran while continuing to cooperate with the country.

Specifically, the EU announced that it will protect European companies that have legal business with Iran and on August 7, put the revised Blocking Regulation into effect. This regulation aims to protect EU companies from damages resulting from economic sanctions applied outside the target region, prohibit EU companies from adhering to economic sanctions, and neutralize the influence of foreign law enforcement in the EU. The EU also adopted a support package worth €18 million for projects that support the sustainable socioeconomic growth of Iran, including €8 million for private companies. This support package will be worth €50 million in total and is considered as part of the EU-Iran cooperation based on the signing of the JCPOA. Despite these efforts by the EU, Total has reportedly admitted to notifying the Iranian authorities that it will withdraw from the 11th phase of the development of Iran's South Pars gas fields. Attention must be paid to the moves of companies in member states as well as of the EU.

3. China: US-China Trade War: Switching from Defense to Counterattacks

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The US-China trade war that erupted on July 6 entered the third phase in September. On September 17, President Donald Trump announced the imposition of an additional 10% tariff on $200 billion worth of Chinese products from September 24, adding that the tariff will be raised to 25% from early 2019 after the mid-term election and the year-end sale end. Combined with the $34 billion worth of goods affected in the first phase and $16 billion in the second phase, additional tariffs are now being imposed on $250 billion worth of Chinese goods. This equals approximately half of Chinese exports to the United States in 2017. On September 18, President Trump warned that a 25% tariff will be imposed on all imports from China if the country retaliates, while saying that he is "always open to talking." Despite the flurry of pressure and threats from the US, China is standing firm and while protecting itself, has begun to look for ways to fight back.

On September 18, the China's Ministry of Commerce (MOFCOM) filed a litigation with the WTO and simultaneously announced the imposition of an additional tariff of 5-10% on $60 billion worth of American products from September 24. This rate was lowered from the original maximum 25% in line with the reduction by the US from 25% to 10%. China announced that the rate will be raised to up to 25% in 2019 and beyond if the US does the same. Meanwhile, once again no announcement was made regarding non-trade, non-tariff measures to make up for the goods on which to impose tariffs. According to US statistics, American companies sold $481.4 billion worth of goods in China in 2015, exceeding the sales of Chinese companies in the US of $25.6 billion by as much as $455.8 billion. Under such circumstances, the American Chamber of Commerce in China and the US China Business Council announced in succession the results of surveys showing that the US-China trade friction is damaging the business of US companies in China. This apparently includes the impact of non-tariff measures such as voluntary boycotts.

Next, in its September 18 statement, the MOFCOM suggested that it might refuse to restart the ministerial trade talks which were proposed by US Treasury Secretary Steven Mnuchin on September 12. This is based on the judgment that the talks must be based on "reciprocity, equality, integrity, and trust," which cannot be achieved under pressure and threats.

Last, there is a growing consensus that China should stage effective counterattacks instead of just defending itself. The US has removed 286 items including smart watches, some textiles, and agricultural produce from the initial list of 6,031 items for the third phase of additional tariffs released in July, due to the large impact of those items on US industry and consumers. Controlling the export of these items to the US by setting numerical caps and raising export tariffs is now being proposed as a way of fighting back.

US LNG is included in the list for the third phase of retaliatory tariffs to be imposed by China. The additional tariff will remain at 10% this year but is scheduled to rise to 25% from 2019 as initially planned in line with the US. LNG exports to China will decline drastically if the tariff is imposed. Meanwhile, US crude is not yet included in the list. However, it will undoubtedly be added to the list and its exports to China will inevitably decline if the US imposes a fourth phase of additional tariffs.

4. Russia: Moving Even Closer toward China

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Russia's economic growth remains slow. GDP growth for Q2 of 2018 increased by just 1.9% year-on-year. As the prices of daily necessities soared due partly to the weaker ruble and higher import prices alongside increasing utility rates, real average wages dropped by 7.3% month-on-month in July despite increasing by 8% year-on-year, and real disposable income declined by 4.7% year-on-year. As the Russian people have increasingly become frustrated with the difficulty of daily life, at the end of August, President Putin announced a revision to the pension reform bill. Its original bill, raising the retirement age by five years from 60 to 65 for men and from 55 to 60 for women, had been submitted to the Duma by the government last June due to fiscal pressure, but it led the government's popularity to plummet. On September 9 when the Moscow mayoral election and various gubernatorial elections were held, people marched in more than 80 cities nationwide to oppose the bill. Several thousand people took to the streets in protest in Moscow alone, and according to humanitarian groups, more than 800 rally-goers were detained by the police nationwide.

In desperate need of foreign investments to rebuild the economy under the West's economic sanctions, Russia is rapidly pivoting toward China. Meanwhile, China has also rediscovered the importance of strategic cooperation with Russia as relations with the US continue to deteriorate. As a result, China and Russia are working more closely together in the international arena. From September 11 to 17, Russia held Vostok 2018, the largest military exercise since its beginning in 1981 during the Soviet era, covering a geographical area stretching from Eastern Siberia to the Japan Sea, with 300 thousand soldiers and more than 1,000 military aircraft. This military exercise has been held in Russia's Eastern Military District every four years and has traditionally designated China as the "potential enemy". However, this year, in an unprecedented move, the exercise was joined by a team of ground and air forces of 3,000 soldiers from China.

During the same period as the China-Russia joint military exercise, on September 11 and 12, the Eastern Economic Forum, an annual event hosted by President Putin since 2015, was held in Vladivostok. This fourth Forum had Chinese President Xi Jinping's first participation. The Russian and Chinese presidents clarified that they would stand together in denuclearization of North Korea without imposing tougher sanctions as well as opposition to protectionism of the United States. In the field of energy, an announcement was made that included agreement by the two leaders to proceed with the talk on prospective construction of the western route (30BCM/y) of the Power of Siberia gas pipeline, and the partial sale of interests in Rosneft's oil and gas projects to CNPC, though its details has remained undisclosed.

Prime Minister Abe visited Vladivostok to attend the Forum for the third consecutive year since 2016 and on September 10, met with President Putin for the 22nd Japan-Russia Summit between the two leaders. Key topics reportedly included the status of joint economic activities on the four islands of the Northern Territories, and the North Korea issue. President Putin's unexpected proposal to "sign an unconditional peace treaty within this year" caused a stir in Japan. In the field of energy, JOGMEC and Russia's largest private gas company Novatek signed and announced an MOU on cooperation in upstream development and the liquefaction business.

Given the strengthening of Sino-Russian partnership while escalating their relations with the United States, the international community is keeping close watch over Japan's move to improve ties with Moscow and Beijing.

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