IEEJ e-NEWSLETTER

No. 163
(Based on Japanese No. 189)
Published: June 17, 2019
The Institute of Energy Economics, Japan

(As of June 14, 2019)

Contents

Summary

【Global Monitoring】

1. US: Partisan Conflict Stalls Large Infrastructure Investments
2. EU: Parliament Elections and a Bid for Portugal’s EDP
3. China: Escalating US-China Trade War and Progress of the Belt and Road Initiative
4. Russia: New Challenges following Inauguration of the New President of Ukraine

Sources:
(1) DOE-EIA
(2) Investing.com
Summary

1. US: Partisan Conflict Stalls Large Infrastructure Investments
   The scheduled meeting between President Trump and Democratic leaders on large infrastructure investment was suspended. Despite high hopes from industry for its boost to the economy, infrastructure investments remain stalled due to partisan conflict.

2. EU: Parliament Elections and a Bid for Portugal’s EDP
   One of the focal points in the European Parliament elections is the growing influence of Euro-skeptics. Presidential candidates for the European Commission are supporting the present energy and climate change targets. The bid by China’s CTG for Portugal’s EDP deserves attention.

3. China: Escalating US-China Trade War and Progress of the Belt and Road Initiative
   The US-China trade war has flared up again since May. China has stated that it will not bow to US pressure and will fight a game of endurance if necessary. Meanwhile, joint construction of the Belt and Road is advancing steadily.

4. Russia: New Challenges following Inauguration of the New President of Ukraine
   As the economy struggles and frustration with the Putin administration mounts, Ukraine achieved a change of government through a free and fair election. The international community is watching whether Moscow will attempt to rattle the new government.
1. US: Partisan Conflict Stalls Large Infrastructure Investments

Ayako Sugino, Senior Researcher
Electric Power Group
Electric Power Industry & New and Renewable Energy Unit

A meeting on infrastructure policy was scheduled for May 22 between President Trump and two Democratic leaders: House Speaker Nancy Pelosi and Senate Minority Leader Chuck Schumer. The meeting came after the three agreed at the end of April to cooperate on implementing two trillion dollars of infrastructure investments. This top-level meeting was seen as the last opportunity for the administration to deliver results in infrastructure policy in its first term, as deliberations on key bills will stop once Congress enters the election season, which will run from the end of the summer recess starting in August and last until November 2020. However, the talks were suspended after House Speaker Pelosi called the administration’s refusal to comply with Congress’ subpoena on obstruction of justice to special counsel Robert Mueller a “cover-up,” to which President Trump took offense.

Since the start of the current administration, companies have had high expectations for large infrastructure investments, and were expecting a Buy America provision requiring the use of a certain ratio of US products. An infrastructure bill, if passed into law during this term which ends in January 2021, would have provided a welcome economic stimulus amid concern over an economic downturn in the US due to the US-China trade war, despite the expected rise in the cost of raw materials and equipment stemming also from the trade war.

Even if the talks had gone ahead as scheduled, however, the chances of the president and the Democrats agreeing over infrastructure policies were slim. In recent days, the president has been pressuring Congress to first pass the United States-Mexico-Canada Agreement (USMCA) if it wants to move the infrastructure bill forward. Further, since March 2018 the Democrats have been consistently supporting abolishing the income and corporate tax breaks that were implemented in 2017 and have been criticized as preferential treatment for the rich, and have called for the proceeds to be used to fund infrastructure projects. However, there is no chance that the Republicans will agree, as they see the tax breaks as their greatest domestic achievement and the driving force behind the current good economy. Meanwhile, the Republicans have not presented any alternative to replace the 1.5 trillion dollar infrastructure policy, which the president announced in January 2018 and to which the federal government contributes only 200 billion dollars and relies on state governments, municipalities, and the private sector for most of the funds.

The prolonged deadlock in infrastructure policies caused by partisan conflict in itself is not surprising. However, infrastructure was surely an area where voters had high hopes for President Trump, a self-proclaimed expert deal-maker and not bound by traditional Republican ideologies. At the beginning of his term, the president had said that raising the gasoline tax was one option for funding roads. This raised the hopes of many voters that this unconventional president, who had no political experience, could confront the Republican Party which dogmatically opposes tax raises and reach a deal with the Democratic Party which advocates infrastructure investments as a means to boost jobs and middle-class incomes.

Looking back, former President Obama also was an outsider to Washington when he won the 2008 election. It will be interesting to see how the transformation of two presidents after taking office will change the view on “outsiders” in the 2020 elections and beyond.
From May 23 to 26, the European Parliament elections were held in the member countries. These elections are crucial and will affect the course of EU policies for the next five years. As has been reported, the United Kingdom, having extended the deadline for withdrawal from the EU, also took part in the elections, and the new Brexit Party is expected to defeat the two major parties. Interest in the elections focused on the extent to which the euro-skeptics would gain ground. In conclusion, pro-EU forces are likely to maintain a two-thirds majority even though the European People’s Party Group (EPP) and the Progressive Alliance of Socialists and Democrats (S&D), the two largest groups, did not win a combined majority, as the Alliance of Liberals and Democrats for Europe (ALDE) and the Greens won more seats. However, discussions among the pro-EU forces could become more complex as the groups that gained more seats may demand a greater say. Euro-skeptics won more seats this time, but not as many as had been expected.

Based on the result of the elections, the next president of the European Commission will be elected through what is known as the “lead candidate process,” in which each group in the European Parliament nominates one or more candidates and the candidate of the group that wins the majority in the election is ultimately elected as the president of the European Commission. The candidates do battle in debates, which voters watch on television or the internet (only one candidate takes the podium per group in the debate). Six candidates appeared at the public debate held on May 15. In the energy and climate change area, which is considered the highest priority, five out of the six candidates support the proposal by the sitting Commission to achieve a climate-neutral economy by 2050. While there is a consensus on the target, the actual process for achieving it will need to be examined under the next administration.

As Europe turned its attention to the European parliament elections, there was a significant event regarding foreign direct investment in energy infrastructure in Portugal. On May 15, shareholders of the electricity operator Energias de Portugal (EDP) rejected the 100% purchase offer by China’s wholly-state-owned enterprise China Three Gorges Corporation (CTG), stating that the purchase price was too low. Having already amassed a 23.4% stake in EDP, CTG offered to purchase 100% of the company for 9 billion euros in cash. CTG will reportedly make another offer. When the Portuguese government sold its stake in EDP in 2011 at the request of the European Commission and the IMF as part of a bailout scheme, CTG immediately pounced and snapped up shares. The EU is currently tightening its regulations against foreign direct investment, and in April 2019 enacted a regulation which sets a framework for screening foreign investments in the EU. The Commission and the member states will take the necessary steps to make the regulation fully effective from October 11, 2020. Portugal reportedly has no regulations in place to prevent an acquisition by a wholly-state-owned enterprise. The proposed acquisition was an attempt by a foreign company to purchase a country’s key infrastructure company in its entirety before stricter regulations are introduced. The stance of the newly-elected European Commission on this matter deserves attention.
3. China: Escalating US-China Trade War and Progress of the Belt and Road Initiative

Li Zhidong, Visiting Researcher
Professor at Graduate School, Nagaoka University of Technology

After reaching a “ceasefire” since the summit at the end of last year, the US-China trade war has flared up again from May. On May 10, in the midst of the eleventh US-China ministerial trade talks, the United States raised tariffs on $200 billion worth of Chinese imports from 10% to 25%. On the 13th, China retaliated by announcing that it will raise additional tariffs on $60 billion of US goods to a maximum of 25% from the maximum of 10% starting June 1. In response, on the same day the US released the fourth stage of sanctions in which up to 25% of additional tariffs will be imposed on approx. $300 billion worth of Chinese imports. If executed, combined with the tariffs on $250 billion worth of goods imposed under the three previous stages, additional tariffs will have been imposed on an amount equivalent to all of China’s exports to the US in 2018 ($540.3 billion according to US statistics). Meanwhile, China’s tariffs will have been imposed on $110 billion of US goods under the three stages, accounting for 70% of US exports to China in 2018 (worth $155.1 billion according to China’s statistics). The remaining $45 billion is being saved for the fourth stage of retaliation.

Why did the tariff war re-ignite in spite of several ministerial trade talks since the beginning of the year, which at one point almost reached an agreement? President Trump has said that “China reneged on the deal,” holding China responsible for failing to ink a trade agreement. Meanwhile, China’s chief negotiator, Vice Premier Liu He stressed that China will not back down on key issues of principle, which mean the complete elimination of additional tariffs imposed by both parties, maintaining numerical targets for expanding US imports as promised at the summit, and impartiality of the agreement document. The People’s Daily and others have harshly criticized the US for forcing an unequal treaty by widening the scope of negotiations to include issues unrelated to resolving trade inequalities and for escalating unreasonable demands that undermine the core interests of China.

Regarding the future, President Trump said, “I think that China felt they were being beaten so badly in the recent negotiation” and “it would be wise for China to act now,” urging concession. In response, the Chinese government stressed that “China does not fear a trade war though it does not want one, and will go along with the US,” and that it will not bow to pressure from a foreign country. The Chinese media argue that the United States aims to maintain its technological hegemony and curb China’s development, and that China must take proper action to ensure it can respond to any situation, as the battle and the negotiations will continue and become the norm. Further, following the US’ announcement on May 15 that it will ban the Chinese telecom company and new 5G world leader Huawei, the national Xinhua News Agency reported that President Xi Jinping visited a rare earth production site on the 20th, signaling that China is considering retaliating by cutting off supplies of rare earths to the US, which depends on China for 80% of such materials, suggesting that China will fight a full-scale and protracted battle if necessary.

In contrast to the growing uncertainty in the US-China relationship, China-led joint construction of the Belt and Road is advancing steadily. At the end of April, the Second Belt and Road Forum for International Cooperation was held in Beijing. The number of participating countries increased to 150 from 130 in the first event, and the number of countries sending their leaders to 37 from 29. 283 inter-governmental agreements and $64 billion worth of joint business agreements were signed, and a joint communique on observing UN regulations on debt sustainability, rejection of unilateralism and protectionism, etc. was adopted. According to China’s latest statistics, Chinese trade in January through April increased by 4.8% year-on-year, while it dropped 11.2% with the US and increased 9.1% with the Belt and Road countries.
4. Russia: New Challenges following Inauguration of the New President of Ukraine

Shoichi Itoh, Manager, Senior Analyst
Global Energy Group 2, Strategy Research Unit

On April 21, former comedian Volodymyr Zelensky became the new president of Ukraine, defeating the incumbent Petro Poroshenko in a runoff by winning 73% of the votes. A complete newcomer with no experience in politics, Mr. Zelensky won the support of the people who had grown impatient with the sluggish economy and rampant corruption.

The result of the Ukraine election has been received by Russian intellectuals with mixed feelings. This is because Ukraine managed, amid the worsening economy, to hold a free and fair election without government interference, an election in which corruption and government leaders could be criticized openly.

It is considered that Russian interference in this presidential election was not as blatant as in the past presidential elections of 2014, 2010, and 2004. From the start, however, Russia made it clear that they wanted anything but another term by Mr. Poroshenko, reflecting the fierce hostility between the Poroshenko government and Russia due to the annexation of Crimea in March 2014 and the subsequent establishment of autonomous republics in eastern Ukraine by pro-Russian forces and the declaration of their independence.

Incidentally, according to a May 17 announcement by the Federal Bureau of Statistics, Russia’s GDP growth rate increased just 0.5% year-on-year in Q1 of 2019, down from 2.5% in Q4 of 2018. Disposable income fell 2.3% year-on-year in the same period, fueling people’s frustration with the Putin administration. With the West’s sanctions continuing, foreign investment in Russia has plunged and capital flight to other countries has soared (by 1.9 times year-on-year in Q1, 2019). Although the Putin administration has emphasized the “durability” of the Russian economy, some are starting to doubt the economic statistics released by the government.

Thus, the Russia-Ukraine confrontation is entering a new stage. On April 18, Prime Minister Dimitry Medvedev announced the government’s decision to ban or limit the export of energy products including oil gasoline, and coal to Ukraine starting June 1. Further, on April 24, President Putin signed an executive order that simplifies the procedure for granting Russian citizenship to residents of separatist-held areas in Ukraine. This move has sparked anger in Ukraine and the West as an attempt by Russia to create a pretext to interfere in Ukraine’s politics.

On May 20, in his inauguration speech, President Zelensky announced plans to bring forward the parliamentary elections to July this year from the original schedule of October. How to counter Russia’s attempts to rattle Ukraine is again the focus of attention. Unlike immediately after the annexation of Crimea, it is not easy for the government to boost its popularity by using Ukraine to stir up patriotism. It is not clear how Russia will solve this issue in a way the international community finds acceptable.