

Country Governance Research Commentary

October 2017

Country Ranking Trends

Magni upgraded Ireland following a review of the country's market integrity. This upgrade combined with other recent ones makes Ireland the most rapidly improving country in the developed or emerging markets over the last year. Despite the upgrades, Ireland still ranks below more than half of the developed markets.

Magni also completed its review of the Pakistani ETFs for inclusion in Magni Global Portfolios. There is a country-level ETF with characteristics meeting Magni requirements. The decision to include Pakistan in model portfolios as part of Magni Advisory Services will be made in consultation with each client.

Will "He" Have the Power to Reform China?

With the conclusion of the 19th National Congress of the Communist Party, President Xi Jinping has consolidated his hold on power as he begins his second five-year term. In a break with past precedent his new leadership team included no apparent successor, which may indicate his intention to remain in power past the customary two terms. Also signaling his strong position, an amendment including Xi's name was added to China's constitution, marking the first time a living leader's name has been added since Mao.

Implications: There has been some concern that his consolidation of power will also coincide with a focus on stability at the expense of economic reform. One positive sign that reform will move forward is the elevation of Liu He to the Politburo. He has an international reputation as a reformer and he is expected to be named vice premier in charge of financial markets and policy, overseeing the central bank along with the top regulator agencies for securities, banking and insurance. However, it remains to be seen whether needed structural reforms will be implemented.

No More Abe Arrows?

The Liberal Democratic Party (LDP) came in first place in early elections called by Prime Minister Shinzo Abe. With this latest election victory for his party Abe will be able to remain prime minister into 2021, which would make him Japan's longest-serving post-war leader. However, the victory was less than an overwhelming endorsement given the low turnout and a fractured political opposition. Tensions with North Korea were an important theme of the campaign, and Abe has said revising Japan's pacifist constitution is one of his main policy goals. His coalition will retain control of two-thirds of both houses of the Diet, which is necessary for any constitutional change. On the economic front Abe has indicated he will prioritize growth over fiscal austerity. The national sales tax is scheduled to rise to 10 per cent in 2019, but instead of using the additional revenue to pay down debt as originally planned Abe campaigned on using at least half of the proceeds to fund new spending. Japan's recent economic performance has been impressive, but additional reforms are needed to address its enormous debt and aging population.

Implications: Previously Abe had pushed his reform "arrows". The combination of national security issues and fiscal stimulus opportunities seem to be crowding out reforms. Japan ranks in the middle of the countries in the developed markets based on opacity; particularly related to market integrity. Should Abe continue reforms, even modest ones, Japan would likely improve its rank among countries in the developed world.

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Could Czech Populism Actually Help?

The populist ANO (Action for Dissatisfied Citizens) party won the recently held Czech elections with nearly 30 percent of the vote. The party founder, Andrej Babiš, is expected to become the next prime minister, though he is currently facing a fraud investigation. Babiš owns the conglomerate, Agrofert (the country's largest private employer) and is the second-richest Czech citizen. While the ANO platform was critical of EU immigration policies and advocated against joining the euro, the party is considered centrist and pro-Europe. The election was notable for the collapse of traditional parties. The Social Democrats have been the dominant party in Czech politics and had finished first in the previous election, but this time they came in a distant sixth place. Besides ANO, the two parties that gained the most were also outside the traditional political establishment: the Pirate Party, which came third, followed by the far-right Freedom and Direct Democracy (SPD) party, which won 10.6%. Coalition talks are under way and the grouping of parties that come together to form the next government will provide the best indication for policy direction.

Implications: The Czech Republic already has a relatively high Magni Country Score for a country in the emerging markets. Depending on the nature of the final coalition, there may be an opportunity for some additional reforms. Such reforms, if successfully implemented, could vault the Czech Republic into one of the leadership positions among the emerging markets. Conversely, populist sentiments could cause the government to enact laws undoing prior progress and thus causing the country to lose its relatively attractive position. Magni will be watching how events unfold.

Will New Zealand Fall Further Behind Korea?

Populism and anti-immigration sentiments were also a factor in the recent New Zealand elections. The Labor party, led by Jacinda Ardern, was able to gain support in part with calls to cut annual immigration. The Labor party had the second highest number of seats after the election, but Ardern will become prime minister after forming a coalition with the populist New Zealand First party. The new government ends the center-right National Party's nine-year hold on power. A weaker currency is a policy priority for NZ First and it also wants to revise the Reserve Bank of New Zealand's mandate to lessen the focus on inflation. The Labor party wants to introduce a dual mandate for the central bank that includes employment and inflation objectives. The election also represents a generational shift with Ardern at 37 years old being New Zealand's youngest leader in over 150 years. She joins several other countries including France, Canada, and most recently Austria that have elected a younger generation of politicians.

Implications: The existing score for New Zealand is already slightly lower than the score for Korea and the score is one of the lowest among the countries of the developed world. The populist tendencies of the coalition may cause changes that would reduce New Zealand's score. Only time will tell.