2023 Global Policy Outlook

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Global Overview

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As we survey the global policy landscape in 2023, there is no shortage of political and policy volatility – the Ukraine-Russia war continues unabated, US-China tensions continue, democratic institutions are under assault, the post-COVID supply chain is realigning – to name just a few issues.

There have been a number of elections in the last few months that will impact geopolitics in both the near-term and long-term. President Xi Jinping secured his 3rd term during China's Party Congress, and Vladimir Putin-installed officials in Ukraine staged referendums on the Russian annexation of occupied territories. Meanwhile, Italy has elected an ultra-conservative government; Brazil is in the process of shifting left by returning former President Luiz Inácio Lula da Silva to office; Israel has also gone back to a former leader on the other end of the political spectrum – Benjamin Netanyahu; the US midterm elections rejected many Donald Trump-backed candidates in competitive races. And not to be outdone, the UK elected not one but two prime ministers over a six-week span.

If you're in search of a central theme to tie of all of these disparate election results together, the best we can offer is former US Speaker of the House Tip O'Neill's words of wisdom – "All politics is local." We're not saying that geopolitics doesn't impact the politics of individual countries. It definitely does. What we are saying is that the impact of global trends varies greatly in each country and can lead to different political and policy paths.

It's Miles' Law: "Where you stand depends on where you sit."

Consider India, for example, and its proximity to longtime nuclear rivals Pakistan and China as well as Russia. Or Japan, who sits in the shadow of China and right next to North Korea yet has a rock-bed alliance with the US. Where these countries "sit" determines how they navigate their relationships in and outside the region. Maybe, aside from getting the best price for oil, this helps explain why India continues to purchase oil from Russia, despite objections from the West, or why Japan is committed to building up its military capabilities.

For the US, how else do you explain the bipartisan passage of the $52 billion CHIPS and Science Act to build US semiconductor manufacturing capacity and invest in research and technology under the auspices of remaining competitive with China? Normally, Congress avoids bipartisanship in an election year. However, in this election year, 82% of the American people have an unfavorable view of China, which means that getting in the way of a bill to help America compete with China wouldn't make good politics.

As we look to 2023, maybe this political lens can help us sort through many of the seemingly haphazard activities across the globe.

United States

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Political outlook:

- With the US midterm elections in the rearview mirror, it's clear the Democrats will maintain control of the Senate and Republicans will take majority control of the House — both by an incredibly slim margin.
- On one hand, President Joe Biden will still be able to move his judicial and administrative nominees through Senate confirmation fairly easily.
- On the other hand, a Republican majority in the House will significantly hamper Biden's ability to enact his legislative agenda, and House oversight of his administration will take center stage as his regulatory agenda is expected to ramp up in the next two years of divided government.

Fiscal outlook:

- Polls illustrated the general discontent of Americans in the run-up to the midterms. According to the Real Clear Politics polling average in the final days before the election, only 26% of those polled said the US is moving in the right direction, while 66% said it's moving in the wrong direction.
- In a divided government, the onus will be on both parties to put forward their plans to bring down inflation, increase US energy production while remaining committed to fighting climate change, and strengthen supply chains.
- Come spring, the growing US deficit will take central stage, as Biden and House Republicans battle over a debt ceiling increase.

Geopolitical outlook:

- With Republicans taking control of the House, look for the there to be much more scrutiny of US support for Ukraine in their conflict with Russia. As expected Speaker of the House Kevin McCarthy noted before the election, there will be no "blank check" for Ukraine.
- Also, look for there to be a push-pull with respect to US-China relations. There is consensus that we need to make sure that the US stays vigilant in maintaining any economic, technological, and military advantage vis-à-vis China. However, there will be debates and tension over how aggressive a stance the US should take, especially where it benefits the US economically without jeopardizing any technological or military interests.

Policy and regulatory outlook:

Digital assets

- Earlier this year, the Biden administration released an Executive Order (EO) outlining a whole-of government approach to identify the risks and potential benefits related to the growth of digital assets and distributed ledger technology.
- The EO focused on six key priorities:
  (1) consumer and investor protection;
  (2) financial stability;
  (3) illicit finance;
  (4) US leadership in the global financial system and economic competitiveness;
  (5) financial inclusion; and
  (6) responsible innovation.
- Various agencies released reports required by the EO, and yet the most notable report to date came on Oct. 3, from the Financial Stability Oversight Council: the Report on Digital Asset Financial Stability Risks and Regulation.
- The report identifies three gaps in the regulatory regime for digital assets:
  (1) spot markets for crypto assets that are not securities are subject to limited direct federal regulation;
  (2) crypto asset businesses do not have a consistent or comprehensive regulatory framework and can engage in regulatory arbitrage; and
  (3) crypto trading platforms have proposed offering direct retail access through virtually integrated platforms.
- To address these gaps, the report calls for:
  (1) passage of legislation granting additional authority to federal financial regulators;
  (2) enhanced regulatory cooperation and the passage of legislation regarding stablecoins; and
  (3) a study on vertically integrated platforms.
- In Congress, there is bipartisan momentum building to legislate a regulatory framework for stablecoins, which will likely be a high priority for the Senate Agriculture Committee and the House Financial Services Committee in the newly established 2023 Congress. The recent events surrounding the cryptocurrency exchange FTX will definitely influence this debate.

United States

Big Tech

- While high-profile bills regulating the tech sector have advanced in Congress, there simply has not been enough consensus on the details to move meaningful legislation across the finish line. Nevertheless, we expect the pressure campaign on Big Tech will continue into the new Congress, with bills focused on anti-trust, privacy, and political censorship.
- However, this past year did yield new federal investment for the technology sector with strong bipartisan support. The Biden administration has begun to deploy $65 billion to improve high speed internet across the country, as result of the 2021 infrastructure bill.
- Additionally, Congress passed the CHIPS and Science Act this summer to provide $52 billion to support the semiconductor industry and invest in US science and tech.

Energy

- With a Republican House majority, Biden will turn to the executive branch regulatory agencies to pursue his climate ambitions.
  - The recently passed Inflation Reduction Act gave explicit authority to the Interior Department to curtail methane leaks from oil and gas infrastructure on federal land.
  - The Environmental Protection Agency (EPA) is writing new regulations clamping down on greenhouse gas emissions from oil wells, power plants and vehicles.
  - And just two days after the election, the administration proposed a regulation that would require most federal contractors to publicly disclose their greenhouse gas emissions and require over a thousand companies to set their own emissions reductions goals.
- However, without explicit Congressional authority, major regulations will face legal challenges, and should Republicans control the White House in two years, any politically contentious rules are at risk of being reversed.
- Additionally, with a new majority in the House, Republicans are likely to conduct intense oversight of the administration's climate policy, calling the Secretary of the Interior, the Secretary of Energy, and the EPA Administrator to testify before congressional committees.
- House Republicans are also expected to focus on subagencies that facilitate permitting or approval of energy projects, such as the Bureau of Ocean Energy Management, the Bureau of Safety and Environmental Enforcement, and the US Fish and Wildlife Service. For example, the National Marine Fisheries Service is currently withholding Letters of Authorization for seismic permitting that would allow domestic oil and gas companies to increase offshore production. The rule they are updating to address this issue is currently pending at the Office of Information and Regulatory Affairs, under the Office of Management and Budget.
- In terms of a broader message, House Republicans are likely to highlight the tensions in US energy going into the winter months, specifically as it relates to fossil fuel and diesel supply.
- Energy reliability and security are especially important, as ISO New England has already requested federal emergency powers to address cold weather this winter and alluded to potential "load shedding."

ESG and climate disclosure

- On March 21, 2022, the Securities and Exchange Commission (SEC) proposed "rule changes that would require registrants to include certain climate-related disclosures in their registration statements and periodic reports, including information about climate-related risks that are reasonably likely to have a material impact on their business, results of operations, or financial condition, and certain climate related financial statement metrics in a note to their audited financial statements."
- The SEC's proposal has sparked a great deal of controversy in Congress and among many in the public issuer community. Depending upon the requirements (definition of materiality and Scope 3 in particular) set forth in the final rule, it is likely to face legal challenges.
- Due to the volume of comments received (upwards of 14,000) and the need to reopen the comment period due to a technological error, a final rule is not expected until early 2023.
- Additionally, the SEC also released disclosure rule proposals directed at the fund industry, focused on ESG fund disclosure requirements and changes to the Names Rule.
- In an effort to push back against ESG investing, several states have introduced or passed legislation to limit state money or state pension funds from being invested in ESG funds.

Europe

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Political outlook:

- Recent election victories for far-right parties in Hungary and Italy may suggest another wave of populism is rising across Europe. While this has made political negotiations amongst Member States more challenging, the EU has so far succeeded in maintaining unity across the bloc on critical issues such as Russian sanctions. However, this is lending greater importance to nascent discussions around moving away from the EU's unanimous decision-making procedures for foreign affairs and certain taxation issues, to reduce the ability of individual Member States to hold the bloc to ransom.
- While the approach to the energy crisis so far has been fragmented and unilateral, we expect that the positive momentum created over the last few years with regards to the bloc's response to COVID, including the creation of the COVID Recovery and Resilience Facility (RRF), will ultimately prevail. This could lead to a joint approach to energy price caps, as well as fiscal support in the form of reinsurance for Member States that provides subsidies for households and businesses to help weather the storm.

Fiscal outlook:

- The energy crisis, coming so soon after COVID, is straining national budgets and is reigniting debates around joint borrowing. While fiscal hawks continue to resist any additional joint borrowing, instead calling for the dry powder left in the current COVID RRF to be redeployed, there are growing calls from Member States to create some form of EU-level support mechanism to ensure that households and businesses can be supported through the winter.
- This is a precursor to a larger debate around the long-term recalibration of the Eurozone's fiscal rulebook. The Stability and Growth Pact has been suspended since COVID, but a decision needs to be taken in May 2023 as to when and how these rules are reintroduced. The focus is currently on having less-rigid rules, which would provide more discretion to Member States to define their path back into the black, but also enabling stronger enforcement if countries fail to adhere to their commitments. Another key discussion point will be whether investments in climate, digital and other such transitionary projects should be excluded from any fiscal tightening.

Geopolitical outlook:

- The Russian invasion of Ukraine has reinvigorated discussions regarding EU enlargement and the geopolitical role of the EU. While there has been positive signalling by assigning candidate status to Ukraine, the EU has recognised that accession remains a long and tortuous process.
- While not an alternative to EU membership, the European Political Community, first proposed by French President Emmanuel Macron, aims to bring together a broader cast of countries from the region to discuss issues of common concern, including energy, migration and defence. The long-term success of this new grouping is yet to be demonstrated, but it shows the EU's increasing geopolitical aspirations in the region.

Policy & Regulatory outlook:

Digital Assets

- With the EU having put in place a legislative framework for digital assets and service providers over the last six months, the year ahead will focus on the operational aspects thereof, with the reins passing from the legislators to the regulators.
- As a result, over the next year, issuers, service providers and other business operating in this space will be figuring out how the new framework will impact their operations, and what growth opportunities exist as a result of the greater clarity brought about by the Markets in Crypto Assets Regulation and the Pilot Regime for Market Infrastructures based on distributed ledger technology.
- Meanwhile, the European Central Bank (ECB) will continue its exploratory work on the viability and utility of a digital euro, with a decision on whether to begin development expected towards the end of the year.

Energy

- The short-term focus will be on navigating the fallout from the energy crisis, including introducing price caps on gas.
- This will be complemented by more medium-term priorities, including reforming the way electricity prices are determined in the EU.
- However, work is also progressing on the EU's Fitfor55 package, a package of measures that will align the bloc with its stated ambition of reducing its carbon emissions by 55% by 2030 as a staging post towards Net Zero in 2050. This includes reforming the EU's cap-and-trade system for carbon, introducing a Carbon Border Adjustment Mechanism, and banning the production of petrol and diesel cars starting in 2035.

ESG

- While the EU has already agreed to reform its corporate sustainability disclosure rules, the technical work to define the reporting standards will take place over a longer timeframe, with the critical question being to what extent the EU will align with the international standards being developed by the International Sustainability Standards Board.
- The EU is also debating the potential introduction of a mandatory regime for companies to undertake due diligence on their supply chains for environmental and human rights issues. This is in addition to specific regimes banning products from the EU market that contribute to deforestation or that are the result of forced labour.

United Kingdom

Graham Hook
Head of UK Government Relations and Public Policy

Political outlook:

- 2022 could scarcely have been a more volatile period in UK politics, witnessing three different prime ministers and four chancellors. Despite the more technocratic approach pursued by current Prime Minister Rishi Sunak, with an unruly governing party facing significant economic headwinds, political volatility and uncertainty will persist through 2023.
- Faced with the rising cost of living, the health system creaking at the seams, and a wave of public service strikes throughout the winter, the Conservatives will continue trailing Labour in the polls and will likely suffer losses at the local elections in May.
- As a Labour government (either majority or minority) becomes the most likely outcome of the next election, media scrutiny of Labour's policy plans will likely increase, forcing Sir Keir Starmer's party to reveal more detailed proposals.

Fiscal outlook:

- Following the failure of the September 2022 mini-budget, fiscal responsibility has been restored as a central plank in the government's economic strategy. Institutions such as the Bank of England and the Office for Budget Responsibility have emerged with their independence strengthened. Fiscal policy will no longer work against monetary policy, and independent economic and fiscal forecasts will once again be the cornerstone of future budgets.
- Despite the significant package of tax increases and spending cuts announced in the Autumn Statement, the combined effects of inflation, higher interest rates, the current recession, and continued public spending pressures mean the public finances will remain under strain through 2023. With the perennial exception of the National Health Service, demands for significant spending increases (e.g., for defence) will likely be rebuffed.
- If the economy contracts more than predicted or revenues surprise on the downside, further tax hikes will test the limits of Conservative MPs' willingness to support raising the overall tax burden – already forecast to reach the highest level as a percentage of gross domestic product since WWII – yet further.

Geopolitical outlook:

- UK-EU relations, which have been strained since the Brexit referendum, could improve significantly if a lasting solution to the implementation of the Northern Ireland Protocol can be achieved. While the political mood music on both sides is encouraging and negotiations are ongoing, serious compromises are still needed on both sides to reach an agreement. Resolving the Protocol would remove the biggest piece of grit from wider UK-EU relations and enable greater cooperation across areas such as financial services regulation and scientific research.
- The war in Ukraine and the threat of asymmetric Russian attacks against Western vulnerabilities (e.g., undersea pipelines and cables) will continue to be a dominant security challenge next year. However, as cost of living increases bite, the UK government will need to work harder to continue to persuade voters of the merits of continued military support to Ukraine.

Policy and regulatory outlook:

Digital assets

- Proposals to bring stablecoins used as a means of payment within the regulatory perimeter for the first time will become law in 2023. The government also proposes to bring a broader suite of "cryptoassets" within the regulatory perimeter, including applying financial promotion rules to crypto investments. The Treasury will also be empowered to develop financial market infrastructure (FMI) sandboxes to facilitate testing of FMIs that utilise distributed ledger technology.
- The Bank of England will continue its exploratory work on the concept of a UK central bank digital currency (CBDC). However, even if the exploratory and development phases go to plan, we do not expect a UK CBDC to be fully realised before the end of 2025 at the earliest.

Energy

- Support for households and businesses to cope with the rising cost of energy will remain the immediate. However, the war in Ukraine has underlined the need to enhance energy security in parallel to decarbonisation. With fracking firmly off the table again, the government's focus will be on incentivizing a faster rollout of new nuclear and renewables, and producing a workable package to improve home energy efficiency.

ESG

- UK ESG regulation will step up a notch in 2023 with a host of policy developments reaching fruition. The deadline for mandatory climate-related disclosures for large asset managers looms at the end of June; and the Financial Conduct Authority is due to publish its final rules on the labelling and disclosures for sustainable investment products around the same time. We also expect more detail on how the government intends to introduce corporate sustainability disclosures modelled on the standards developed by the International Sustainability Standards Board, combined with the publication of the UK's Green Taxonomy.

Asia Pacific

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Political outlook:

- President Xi Jinping's third term as General Secretary and Chairman of the Central Military Commission of the Chinese Communist Party (CCP) was reaffirmed at the 20th Party Congress.
- Li Qiang, the current Shanghai party secretary, now occupies the No. 2 position within the CCP and will likely be appointed premier in March 2023.
  Li is a newcomer to central government. Li was known to be pro-business and to have overseen many foreign investments during his term as party chief of Shanghai, so his ability to revive the Chinese economy and advance market reforms will be an area of focus for market participants.
- There should be opportunities for some relaxation or fine-tuning of the zero-COVID policy as we enter 2023 and expect less deadly variants and subvariants to become dominant in China. It remains unclear whether Xi will be able to take advantage of those opportunities to open up China fully to the world, and whether he will send a clear message of such to local government officials so that the new approach can be applied consistently across the country.

Fiscal outlook:

- We expect a reshuffle of leadership at China's financial regulatory bodies. Depending on who takes over the helm from the outgoing technocratic leaders, bolder fiscal decisions to deal with China's sluggish economy may be expected in the coming year or so.
- Compared to the 19th Party Congress five years ago, terms such as "reform" and "opening" were featured less in the 20th Party Congress Report. We can expect some paring back of market-oriented reforms in favour of a more statist economy with continued support for state-owned enterprises.
- The six largest Chinese state-owned banks announced in October that they will extend their credit support to the property sector. People's Bank of China and China Banking and Insurance Regulatory Commission also jointly announced on Nov. 11 sixteen high level measures to provide support to the healthy development of the property sector (including the extension of loan payment terms for one year for certain developers), as well as jointly instructed commercial banks on Nov. 14 to issue letters of guarantee to high quality developers allowing them to withdraw up to 30% of pre-sale funds in escrow to complete project construction and repay debts. These may indirectly alleviate the burden on local governments' finances, which are impacted by mass testing and movement restrictions as part of the zero-COVID policy.
- China will continue to increase its central government spending in infrastructure as well as science and technology development to jumpstart its economic recovery and to become self-sufficient in industries of strategic importance to the nation.

Geopolitical outlook:

- As expected, the in-person meeting between Xi and US President Joe Biden during the G20 Summit did not produce substantive results. But both agreed to maintain regular strategic communication and emphasized the need to work together on issues such as climate change and food security. Biden reiterated that the One China Policy has not changed, and that the US does not support "Taiwan independence." Such acknowledgement is precisely what China is looking for and should help to relieve some tension in the Taiwan Straits. The likelihood of near term military action over Taiwan Straits has declined and engagement between US and China is expected to increase.
- China's current foreign minister, Wang Yi, is expected to lead the Central Foreign Affairs Commission, which signals that an assertive diplomacy stance will stay.
- Strategic competition between China and the West, especially in the technology and semiconductor space, will further intensify. China may apply its Anti-Foreign Sanction Law more readily to counter the technology containment imposed by the West.
- There was little mention of the Belt and Road Initiative in the 20th Party Congress Report, which indicates that investments and loans offered to other nations will likely be significantly scaled back.

Policy and regulatory outlook:

- Enhanced climate risk disclosure requirements are expected to be introduced in China. Policymakers will continue to pursue green economy measures, but that does not eclipse the importance of coal to the economy. Xi made clear in the 20th Party Congress Report that fossil fuel will continue to be used until there is certainty of energy security.
- As outlined in the National Development and Reform Commission's "Opinions on Further Improving the Policy Environment and Increasing Efforts to Support the Development of Private Investment" issued on Nov. 7 (the NDRC Opinions), private enterprises are encouraged to invest in renewable energy production and to invest or co-invest with the government in infrastructure and urbanization projects. Public-private partnerships shall also be established to further investments in specified projects.
- The NDRC Opinions also include a clear statement of support for private investment to participate in pilot projects of infrastructure real estate investment trusts, as well as support for ESG evaluation of investment projects. This is in line with the shift from a high rate of growth to high-quality growth as signaled in the 20th Party Congress Report.
- New regulations may be introduced to address income disparities and redistribution of wealth. In the name of achieving common prosperity, we may expect increased enforcement of antitrust regulations and more focus on Big Tech and market leading businesses.

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