MACRO: What to watch in 2022

Our global outlook includes the views of our political risk team on the main issues to watch in each region in 2022. Please do not hesitate to contact us should you wish to discuss any of the issues covered in the report in greater detail.

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Teneo

The Global CEO Advisory Firm

What to watch in 2022

Outlooks for the year ahead from Teneo's political risk team

Contents

Africa

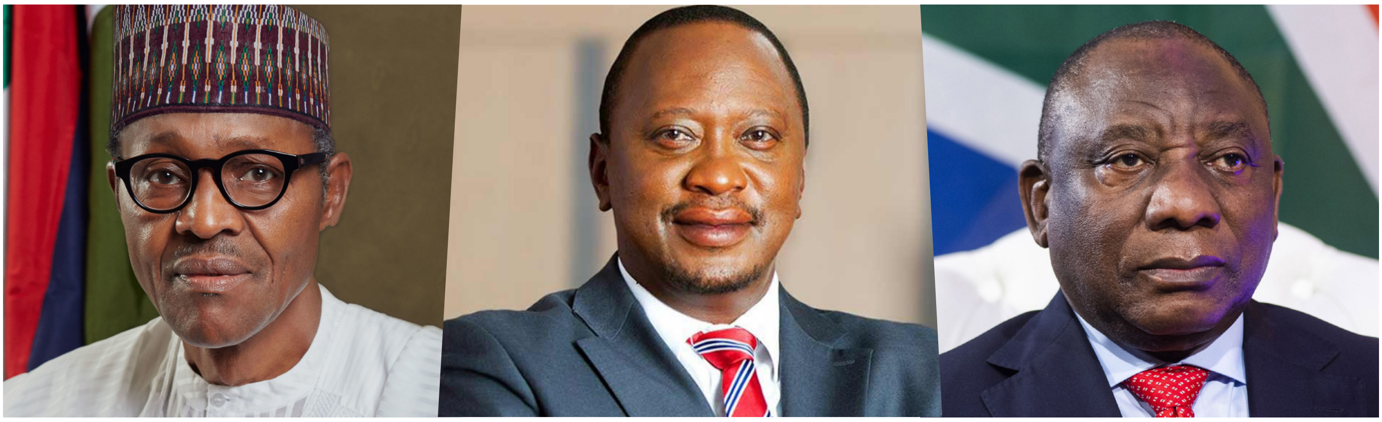
What shape will recoveries take?

The economic recovery of Africa south of the Sahara (SSA) is expected to trail all other world regions in 2021 and 2022, with the IMF forecasting a modest rebound of around 3.7%. Not only has global vaccine inequity bequeathed African countries with the lowest global vaccination rate, with just 10% of the region's population fully or partially vaccinated. What is more, from Kenya to Nigeria to South Africa, countries are managing pandemic recoveries with much reduced fiscal firepower and rising debt burdens. Yet the temporary band-aid in the form of the G20's Debt Service Suspension Initiative (DSSI) runs out at the end of 2021, while a concrete plan for redistributing a greater share of the IMF's landmark 2020 SDR disbursements has yet to emerge. For the hardest-hit cases – Zambia, Ethiopia, and Chad – debt restructurings must be completed in 2022, which will set important precedents for any private creditor participation.

> "The economic recovery of Africa south of the Sahara is expected to trail all other world regions in 2021 and 2022"

Reform paths and policy trade-offs will become even more difficult as governments confront immediate problems of rising debt, unemployment, poverty, and inflation, but also longer-term challenges of how to adapt to climate change and "green agendas" while pursuing their trade and industrial development agendas. On the back of COP26, global climate trends, coupled with policies such as the EU's Green Deal, present a mix of threats and opportunities for African countries. Threats include lack of financing for climate adaptation, financing constraints for fossil fuel projects, and future EU trade barriers. Yet global climate trends also present opportunities, including South Africa's USD 8.5bn transition finance deal and producers of minerals fueling the 'electric' revolution, including cobalt and copper.

Despite the potential economic benefits the region stands to gain from the African Continental Free Trade Area Agreement (AfCTA), for now, the pace of implementation – in part hampered by infrastructure challenges – remains too slow to produce substantive benefits that could offset the current risks.



Top markets heading into tumultuous elections

Tough policy choices will only be complicated by the region's key economies heading into tumultuous election cycles. Angola's 2022 polls will be a referendum on the ruling MPLA's 46-year rule and President João Lourenço's reforms in the post-dos Santos era, which have been bedeviled by multiple economic shocks. In Kenya, Vice President William Ruto and opposition leader Raila Odinga will vie to succeed President Uhuru Kenyatta in a tense race ahead of the August 2022 elections, which will be closely watched for signs of the electoral violence that has periodically disrupted Kenya's economy.

Although South Africa's next general elections are not due until 2024, the African National Congress (ANC)'s internal elective conference in December 2022 will effectively determine whether President Cyril Ramaphosa can become a two-term president. It will also define the ANC's chances of defending its majority in the 2024 general election at a time when the party faces accelerating electoral decline and internal chaos.

Finally, Nigeria's February 2023 general election and subsequent state elections will determine the political calendar in Africa's most populous nation throughout 2022. Parties are expected to select their presidential flagbearers alongside candidates for both houses of parliament and state-level elections in the third quarter. The opposition Peoples Democratic Party (PDP) hopes to reverse its fortunes this time as the ruling All Progressives Congress (APC) may struggle to sort out President Muhammadu Buhari's succession unscathed, amid the party's all-important regional and ethnic fault lines.

A new 'arc of instability'

The Sahel region may emerge as a persistent arc of instability in 2022, following the onset of a civil war and the return of coups d'état that ravaged the region from east to west in 2021. This could destabilize neighboring states, fuel transnational extremism, and shift geopolitical alignments.

Mali's second coup d'état in less than a year in May 2021 will fuel the spread of jihadist militant groups that has already engulfed neighboring Burkina Faso and Niger and is now threatening littoral coasts such as Ghana and Cote d'Ivoire. The void left by the expedited French force reduction may be filled with Russian mercenaries at the behest of Mali's military junta. The events in Mali, and the muted international reaction, also emboldened special forces to stage a coup in Guinea, one of Africa's leading iron ore and bauxite producers.

In East Africa, Sudan's generals' attempt to challenge a domestic power-sharing agreement and depose the civilian government, with tacit approval from Egypt, highlights the fragility of the country's transition and its return from decades of international isolation. Yet, the region's greatest concern is Ethiopia. Once deemed a reform success story, Ethiopia's deepening civil war could destabilize not only Prime Minister Abiy Ahmed's administration but the entire Horn of Africa region. Even worst-case scenarios of state collapse, widespread conflict, and Western sanctions have become plausible, unless the African Union's High Representative for the Horn of Africa, Olusegun Obasanjo, can secure a ceasefire and peace talks.

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Asia

China: Tough choices on economic stimulus in a transition year

China's economy has slowed sharply since the peak of its pandemic recovery, and this slowdown will force policymakers into difficult choices in 2022 about how to balance between short-term economic growth, structural reform, and de-carbonization. Weakness in the housing market – due largely to policies restricting lending to the sector – is the biggest source of the slowdown. These policies reflect a broad consensus about the need to reduce the economy's reliance on housing construction and contain the accompanying financial risks. During previous rounds of housing market stress, however, policymakers have retreated from tightening measures whenever a housing slowdown threatened to push growth below Beijing's bottom line.

The temptation to fall back on housing and infrastructure stimulus will be especially strong in 2022, given President Xi Jinping's desire to ensure strong economic growth ahead of the Party Congress in November, where he will seek to earn a third term as party general secretary. Still, the Communist Party appears more determined than in past years to tame the housing bubble, even at the cost of slower growth. Top leaders have repeatedly emphasized the need to prioritize growth quality over quantity, and housing affordability is a key plank in Xi's signature "common prosperity" agenda.

On US-China relations, there are tentative signs that Washington may roll back some Trump-era tariffs. Still, the bigger threat to Beijing's economic ambitions is US export controls that restrict sales of advanced technology to Chinese companies. These controls are virtually certain to remain in place, and Beijing will, therefore, remain committed to industrial policies designed to achieve technological self-sufficiency in key sectors like semiconductors.

China's sharp economic slowdown will force policymakers to make difficult choices about balancing short-term economic growth, structural reform, and de-carbonization

Japan and South Korea: Traditional and economic security concerns are rising

It will be a year of two halves in Japan. Initially, new prime minister Fumio Kishida will focus on keeping the pandemic tamped down and the economy trending up, with a USD 500bn stimulus package feeding through to boost growth during the first two quarters. The ruling LDP/Komeito coalition should maintain their majority in July's Upper House national Diet elections. Then Kishida can get down to making tough choices on the security front, with Tokyo increasingly alarmed by Beijing's growing assertiveness in the Taiwan Strait and around the disputed Senkaku/Diaoyu islands.

On traditional security, a revision to the national security strategy, a 10-year defense plan, and a 5-year procurement plan are all due, and higher spending and new capabilities seem likely. In terms of economic security, strategic supply chains, domestic semiconductor production, and export controls for sensitive technologies will all be high on the agenda. Japan will work with its democratic partners, the United States, Australia, and India, to further develop cooperation on non-traditional security and strategic trade through the Quad framework and the unfolding US-Japan Partnership on Trade.

South Korea's outlook will turn on the outcome of March's presidential election. Left-wing candidate Lee Jae-myung of the ruling DP promises higher social welfare spending and greater defense independence from the United States. At the same time, conservative opponent Yoon Seok-youl offers help for the self-employed, an integrated defense approach, and a possible softening of Seoul's ossified relations with Tokyo. The accelerating arms race on the peninsula will continue, and the impact of the pandemic on North Korea's fragile economy and feeble public health system could cause even greater volatility from Kim Jong-un's unpredictable regime.

A busy electoral calendar

In addition to the Philippines' scheduled elections in May, Thailand and Malaysia may hold early elections. The leading candidate in the Philippines is Ferdinand Marcos, Jr., the son of the former autocrat, and a polarizing candidate. In Thailand, Prime Minister Prayuth Chan-ocha's leadership may be questioned by his own coalition, while monarchal politics could become the focus of political debates. Opposition dissonance and a possible swing by Malay voters back to the United Malays National Organization could encourage the erstwhile ruling National Front may lead to early elections and another change in government.

In Sri Lanka, which is scheduled to hold provincial council elections in 2022, unpopular economic decisions will impact the ruling party adversely. In India, some major states, including Uttar Pradesh, are heading for polls in the first quarter of the year. Mismanagement of COVID-19 is a vivid memory and will hurt the Bharatiya Janata Party (BJP), which is the incumbent in most states going to the polls.

Aside from the political changes at the country level, the more significant shift – and differentiator of outcomes – will be in how effectively these countries can manage both their exit from the pandemic and the economic risks that have accumulated over the past two years. Restoring tourism flows will be important for Thailand, while Indonesia will see the first full year of its pro-investment agenda. With foreign exchange reserves at historic lows, Sri Lanka is struggling to stave off sovereign default in the first quarter of 2022, and a bailout from the International Monetary Fund (IMF) is a near certainty. Pakistan will spend a large part of 2022 implementing the conditions laid down by the IMF, which came to its rescue in November 2021.

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Europe

Would Macron's re-election lead to a shift in EU fiscal policy?

France will hold a two-round presidential election on 10 and 24 April – followed by legislative elections in June. While the ongoing elevated electoral volatility can still produce some last-minute surprises, opinion polls consistently indicate that this is President Emmanuel Macron's election to lose. Far-right Marine Le Pen still seems the best-placed candidate to fight Macron in the runoff despite the recent emergence of polemist Eric Zemmour, while the center-right would have to make a strong surge in the first months of the year to break the Macron-Le Pen duopoly. In fact, the worst-case scenario for the incumbent president would be one where he faces a candidate from the center-right who would be much more competitive than Le Pen or Zemmour, considered too radical to win.

Macron's re-election would clearly be positive for European integration, as a victory by Le Pen would probably lead Paris to develop a confrontational approach towards Brussels. The fact that Germany will enter 2022 with a Social Democratic Chancellor and a Green Economy Minister would mean that two exceedingly pro-European administrations would be at the helm of the crucial Franco-German engine. However, Paris and Berlin will still have to resolve some crucial issues for EU integration to make progress.

Take, for example, the reform of EU fiscal rules. At the end of 2022, the so-called escape clause exempting member states from the fiscal straitjacket of the Stability and Growth Pact (SGP) will come to an end. France, which holds the presidency of the Council of the EU in H1/2022, has already taken the item of SGP reform off its agenda, reluctant to make any move in favor of the quick re-imposition of fiscal rules. New German Finance Minister Christian Lindner is likely to insist on returning to largely unchanged deficit rules in the EU after the pandemic (notwithstanding their relatively relaxed interpretation in recent years). In return, Germany could agree to make the pandemic recovery fund – negotiated by Scholz personally – permanent from 2023, helping to boost German green and digital investment from outside the national budget.

No elections in Turkey, up to two in Italy

Italy will hold at least one important election in 2022 and in an unlikely scenario two. Turkey, in contrast, will not go to the polls even if the country is already in election mode.

The Italian parliament will convene to choose a new head of state in late January to elect the successor of President Sergio Mattarella. While presidential elections in Italy have been usually non-relevant for business, 2022 is different as it could determine the fate of Prime Minister Mario Draghi's government. Draghi's move to the presidential palace would put an early end to his government and could plunge the country back into political turmoil, undermining efforts to enact reforms needed to secure regular installments of recovery fund cash from the EU. In the worst-case scenario (unlikely), Italy could be forced to go to early parliamentary elections. Italy is the third-largest economy in the EU and accounts for nearly 15% of the Euro area's GDP. It is also the country, along with Spain, which has received the most grants from the Next Generation EU fund. A failure of the Italian resilience and recovery package caused by a sudden return to political instability could make discussions about creating a permanent EU fiscal facility more challenging.

In Turkey, recent economic fluctuations that led to an unprecedented depreciation of the Lira have triggered calls for early elections by opposition parties. Opponents of President Tayyip Erdogan cited enormously growing economic problems as the reason to go to the polls ahead of the end of the term in June 2023. However, the opposition has no sufficient majority in parliament to trigger early elections. Erdogan, the only person with a definitive say on the matter, has no incentive to call snap polls. Even though polls are not in sight, a very difficult one-and-a-half-year period awaits Turkey, as Erdogan and his government will redouble their efforts to make elections safer for themselves.

> "The worst-case scenario for Macron would be one where he faces a center-right candidate in the presidential election runoff."

Russia's relations with the West: How low could it go?

Moscow's ties with Washington have been steadily deteriorating in recent years and reached new lows in 2021. The negative trajectory will likely persist in 2022 as diplomatic efforts to put bilateral relations on a more predictable pathway seem ineffective. The Kremlin is increasingly flexing its military and energy muscles to advance its foreign policy objectives in Central and Eastern Europe (CEE) and draw new "red lines" for Western presence in the region. Moscow's growing leverage over Alexander Lukashenko's unpredictable regime in Belarus is disconcerting and could be utilized to destabilize CEE's political and security situation further. Meanwhile, reduced diplomatic contacts between Moscow and Washington/NATO leave room for potentially dangerous miscommunication.

The ever-deepening geopolitical confrontation translates into reputational and political risks of doing business with Russia. Notwithstanding the potential for new fault lines to emerge, there is already a long list of simmering issues that could trigger new US sanctions on Russia. It includes Moscow's multi-faceted pressure on Ukraine, Russia's cyber activities and efforts to influence electoral processes in the West, the intensifying military competition with the US (including in space), the precarious health condition of Russia's opposition activist Alexei Navalny while in prison, and the lingering suspicions of Russia's hand behind the so-called Havana Syndrome affecting the health of US diplomats across the world.

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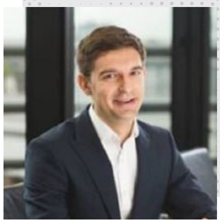

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In Focus: Global tech

This past year saw a major shift toward the regulation of Big Tech through antitrust policies, data privacy acts, and penalties such as fines against companies like Alibaba in China or Facebook in Australia. Even with this shift, global authorities are struggling to monitor and preempt a rapidly changing technological landscape. As 2022 approaches, global leaders will face challenges in designing, passing, and implementing regulations that address the everchanging nature of technology.

Why is it so hard to regulate tech?

The difficulty in tech regulation comes in a few forms. First, there is a schism in how governments approach regulation – citing either content moderation or antitrust. Countries such as the US, India, China, and Russia have moderated social media on the basis of data privacy and misinformation concerns. On the other hand, antitrust and financial regulation continues to be a primary line of defense for countries, especially actors like the US, EU, and China. These piecemeal approaches to regulation result in overlapping, or even conflicting, policies and fail to answer the question of "who" will be the lead regulator. Another difficulty stems from the lack of infrastructure needed to implement and monitor policies. In countries such as South Korea, taxation of cryptocurrency was approved but implementation was pushed to H1 2022 due to delays in developing the tools needed to monitor crypto activity. Standing up monitoring agencies, data infrastructure and human capital can slow down implementation of newly approved regulations.

Setting clear definitions and regulatory policies for the tech industry will be a top priority in 2022 and will require the support of technical actors and increased digital literacy amongst policymakers.

What can we expect in 2022?

Looking ahead to 2022, we can expect greater public debate and global attention given to tech regulations – with emphasis on the need for content moderation and privacy rights as firms like Meta come under public scrutiny for their strategies.

One technicality that policymakers will grapple with in the new year is the "one-size-fits-all" approach to regulations. Decisionmakers are having to balance the need for targeted policies with concerns about overregulation discouraging innovation. Setting clear definitions and regulatory policies for the tech industry will be a top priority in 2022 and will require the support of technical actors and increased digital literacy amongst policymakers.

A major signpost in 2022 will be whether or not the EU's Digital Markets Act (DMA) is approved and implemented. The DMA is aimed at curbing the market power of larger firms to bolster competition. Amendments to the DMA were provided by the EU Commission at the end of November, paving the way for this policy to be debated in the European Parliament in 2022. What's novel about the DMA is that it shifts regulatory approaches from ex-post to ex-ante regulation – firms must ask for permission rather than beg for forgiveness. If the DMA passes in 2022, the industry may see a greater shift to ex-ante regulations that help regulators get in front of new technologies.

If regulatory frameworks are approved in 2022, the next step will be to watch for how countries develop implementation plans for these frameworks. More specifically, who will be the implementors, monitoring agencies, and regulatory bodies who will act on behalf of these new regulations? In the US, there is increased discussion around if the Federal Trade Commission (FTC) is the appropriate body to be regulating tech firms, or if there is a need for a separate regulatory body. The new year will show the need for oversight committees and dedicated agencies whose primary mission is to monitor the tech sector. A new year's resolution for governments aiming to regulate the tech sector will be to be to focus on building up technical capacity, streamlining monitoring processes, and clearly communicating the chain of command to make regulation more responsive.

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Latin America

Precarious politics

Weak governments are nothing new in Latin America. Yet 2022 could stand out for its governability crises and unsettled politics. Argentina, Peru, and Ecuador all have fragile governments exposed to hostile legislatures in contexts of acute polarization. In the case of Peru and Ecuador, it is far from clear that either government can make it to the end of 2022 without a serious political crisis; impeachment attempts in both are not a far-fetched scenario. Argentina's government is in a slightly better legislative position, but a prolonged fiscal imbalance will force a potentially traumatic reckoning with the International Monetary Fund (IMF) in the early part of next year.

Mexico – where President Andres Manuel Lopez Obrador (AMLO) maintains simple congressional majorities – is less likely to suffer a governability crisis. However, AMLO's ability to shrug off such difficulties reflects a concurrent regional trend that will also mark 2022: Latin America's authoritarian relapse. The quality of democracy is unlikely to improve in much of Central America or in Venezuela. In Mexico, AMLO will continue to undermine checks and balances on his power as he looks to reboot his presidency via a recall referendum in the early part of 2022 – his ultimate aim being political hegemony for his National Regeneration Movement (Morena) party.

Colombia may be an exception to this landscape of governability crises and/or democratic backsliding, though if the leftist Gustavo Petro wins the presidency, either or both could eventually materialize. Colombia elects a new legislature in March and holds presidential elections in May/June. One advantage for Colombia is that legislative and presidential elections do not occur simultaneously, a factor that has contributed to Ecuador and Peru's shared problem of weak executives without a solid basis of power. Chile will also get a new government from March but the parallel process to re-write the country's constitution is likely to render the new government's first year in office unusually uncertain.

> "Latin America in 2022 could stand out for its governability crises, unsettled politics, democratic backsliding, and polarized elections"

Political extremes

At the same time, the rise of radical and/or outsider political movements is unlikely to slow in 2022 as economic recovery stalls, economic dissatisfaction simmers, new waves of migration arise, and the political center struggles to adjust to the altered post-pandemic social and economic landscape.

At the time of writing, Chile is faced with a starkly polarized Right vs. Left presidential runoff vote after support for centrist options buckled in the November first-round vote. The leftist Gabriel Boric is supported by the Communist Party, which has sometimes displayed a troubling ambivalence towards violent unrest. If Boric's rival, the ultra-conservative Jose Antonio Kast, wins, it would put him at odds with the left-leaning constituent assembly designing Chile's new legal framework. Whether sectors of the Left are prepared to accept a Kast victory, or what would happen in the event that the new constitution does not win public approval in a ratifying referendum to be held in late-2022, represent major unknowns.

Chile is not alone in experiencing a surge in support for radical, anti-status quo movements. In Peru, Pedro Castillo, backed by a Marxist party, came to power in 2021. In Argentina, the ultra-free market libertarian Javier Milei recently won a seat in Congress with policy proposals such as abolishing the Central Bank. In Mexico, the radical leftist faction within the governing Morena party is in the ascendancy, as nationalist initiatives such as the electricity market counter-reform demonstrate. The big question facing Colombia is whether anyone can stop Petro. Like Colombia and Chile, Brazil looks set for a polarized election battle.

Brazil's choice

From a late-2021 vantage point, incumbent right-wing President Jair Bolsonaro would reach the runoff election in October 2022 and lose to left-wing former President Luiz Inacio Lula da Silva (2003-2010). Both are technically tied in spontaneous polls where names are not revealed, while Lula prevails in stimulated polls by five percentage points over Bolsonaro. In either case, both reach the runoff election by a large margin over seven other candidates. In the runoff, Lula is projected to win by more than ten percentage points.

The key number that must improve in 2022 for the most likely scenario not to prevail is for the centrist camp to grow from the less than 20% of the electorate that it currently has.

Despite the high rejection rates of both main contenders, a fall in their voting preference hinges on the presence of a significant challenge from the center of the political spectrum. In addition, if one considers that at least 40-50% of the electorate would go to either Bolsonaro or Lula no matter how damaging the race might be for them, any scenario with more than one centrist candidate may not be enough to prevail over one of the two in the first round.

The entry into the race of former Carwash judge and Bolsonaro Justice Minister Sergio Moro in November 2021 may improve the chances of a broad centrist concertation in 2022, particularly if his candidacy grows. Moro is already the best candidate outside the Bolsonaro-Lula duality (10%), but he needs to be sufficiently ahead in the polls by mid-year 2022 to induce others to support him. The main challenges in this context are Ciro Gomes, the center-left candidate from the PDT, and João Dória from the center-right PSDB – neither of which will abandon the race unless their chances become crystal-clear minimal.

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Middle East & North Africa

Oil market volatility

The conversation about the energy transition is causing growing uncertainty in the Middle East. Hydrocarbons represent more than 90% of government revenues in Iraq, more than 70% in Kuwait, Qatar, Oman, and Bahrain, about 65% in Saudi Arabia, 60% in Algeria, and 40% in the UAE. Hydrocarbon revenues also find their way to energy-importing states, partly through foreign assistance from energy exporters and partly through remittances from citizens working there.

As already seen in 2021, global energy markets are likely to grow more volatile in the near and medium term. Investor pressure on ESG criteria has diminished multinational corporations' investments in exploration and production, and national oil companies are already seeking to invest in expanding market share to avoid stranding assets whose value will diminish as global oil demand falls in the coming decades. Meanwhile, the use of natural gas as a transition fuel will give gas producers a leg up over oil producers in the next decade. The increased volatility in global energy markets will complicate budgeting and threaten the discipline necessary for economic diversification throughout the Middle East.

US repositioning

The Biden administration says it is focused on diminishing the US military presence in the Middle East, although the regional perception is that all aspects of the US presence are in retreat. Some argue that the signs of a US rebalancing away from the region have spurred conversations between Iran and many of its regional antagonists and between Israel and a growing number of Arab states.

The perception of a waning US presence is likely to affect economic ties – not only the arms sales that dominate US exports to the region but also industries such as infrastructure and pharmaceuticals. China is investing in expanding its regional ties, its state-owned enterprises often come in with financing, and government regulatory processes are often faster. The widespread perception that China represents the region's future while the US represents its past is overblown, and US companies remain the gold standard for organization and outputs. Nevertheless, the attraction of deepening ties with governments that are willing to invest in the region versus those who are seeking to diversify away from it will be a growing part of the agenda, and will be especially notable in Saudi Arabia, Egypt, and the UAE.

> "Increased volatility in global energy markets will complicate budgeting and threaten the discipline necessary for economic diversification."

Iran

US-Iran tensions will rise significantly over the coming year, and there is likely to be at least one crisis episode as Iran seeks markedly better terms for its engagement with the world than the 2015 nuclear deal. The Iranian objection was not so much to the terms of the agreement per se, but to the US ability to repudiate the deal with impunity. From the Iranian perspective, the country was able to withstand the resultant "maximum pressure campaign" from the world's most powerful country; with so many sanctions in place, they judge the US as lacking many more tools to use. Also, the US and China are much less successful compartmentalizing their differences than the US and Russia, and rising US-China tensions will make it much harder for the US to gain Chinese acquiescence to greater international pressure on Iran.

Iran has replaced its veteran nuclear negotiating team with newcomers, it has moved slowly to resume negotiations, and it has advertised its intention to focus attention on its ties with Asia and the Middle East rather than on the nuclear file. The country is accelerating its production of highly enriched uranium, and its cooperation with the International Atomic Energy Agency is increasingly strained. While the Biden administration's strategy on Iran is to show patience and determination (as befits a stronger power), Iran will seek to redress the power imbalance by forcing negotiations on its own terms. It may do either by an attack that is difficult to attribute (such as its May 2019 limpet mine attacks on ships in the Gulf of Oman and its missile and UAV attacks on Saudi oil facilities in Abqaiq and Khurais in September 2019), or by a nuclear breakthrough.

The challenge of the latter course would be provoking an Israeli military response. Israel is impatient with the Biden administration's Iran strategy and reportedly is agitating for a "Plan B" that would involve a military strike on Iran if negotiations fail to halt Iranian nuclear progress. Israel's newly enhanced ties with the UAE and Bahrain, and quietly growing connections to Saudi Arabia, make some military operations possible that would not have been a year ago.

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