

There are plenty of forecasts out there, but today Stratfor, a geopolitical analysis company, has one of the most rigorous methodologies out there, and their forecasts provide excellent insight into the outcome of world events in the coming quarter.

Europe, Syria, and China are the big three to watch the next three to six months.

### **Third Quarter Forecast 2012**



Though this may not be a quarter of dramatic changes, three evolving issues will require particularly close scrutiny: the European crisis, the Syrian conflict and China's political struggle. From Brussels to Damascus to Beijing, hard realities are setting in, threatening to dismantle decades long political constructs. Though the biggest cracks in the system will take time to appear, this quarter we will see Europe, Syria and China busily trying to stave off harsh but unavoidable consequences.

In Europe, an ideological attachment to a prosperous past is largely blinding the Continent to the consequences of their crisis. Meeting after meeting will be held to conjure a variety of bureaucratic treatments for the crisis, but the fundamental issue will remain: the weakening of the Franco-German relationship. Whereas the European crisis has been largely characterized to this point by a struggle between the economically stronger core and the deeply troubled periphery, the crisis is now starting to consume the core.

Most of the tensions in the Franco-German relationship will emanate from Paris. France's economic model relies mostly on

internal consumption and high government spending. Since the creation of the common currency, France's trade deficit with Germany has increased dramatically. The German approach to the crisis aims to curb government spending, going against France's stimulus-oriented approach. This divergence in interests carries enormous consequences for the fate of the European Union, as the Franco-German axis forms the very foundation of a Continental effort to overcome Europe's eternal geopolitical fault lines.

In Syria, there is a growing acknowledgment that the Alawite core of the regime is holding together while the critical Sunni patronage networks surrounding that core are starting to dissolve. Even as the Alawite core endures, we are coming to a point where inner circle members of the regime, as well as foreign sponsors of the regime in Moscow and Tehran, will seriously begin planning for a post-al Assad Syria. Turkey and its NATO partners still lack the appetite for a foreign military intervention in Syria. However, this environment does raise the potential for a palace coup, in which all stakeholders — Iran and Russia on one side, the United States, Turkey and Saudi Arabia on the other — will maneuver to fashion an alternative regime that best suits their interests.

In China, the Communist Party leadership is anything but blind to history and so is working to battle the consequences of an economic slowdown coinciding with an upcoming political transition. The case of Bo Xilai was a stark reminder to the Party of the dangers of regionalism when a Mao-inspired populist tries to chart a path toward perceived economic and social stability. This quarter, we will see the Party put the Bo case to rest in a decisive and public show of Party solidarity ahead of a leadership transition later in the year. But this will likely do little to conceal a growing behind-the-scenes debate over China's economic and political direction. Once again, the Party will put off any major decisions on China's biggest challenges in hopes of preventing cracks in the system from widening.

# Europe



## The European Crisis

The driving issue for the third quarter remains the evolution of the Franco-German relationship. The economic performance of France and Germany will likely continue to diverge more strongly in the coming months. Though the political rise of French Socialist President Francois Hollande has accelerated the inevitable deterioration of the Franco-German relationship, a rupture is not expected this quarter.

The French economy is not yet at a breaking point: French unemployment is lower than the eurozone average and Hollande's government will be able to manage socio-political pressures. France will be under increased pressure to reduce its budget deficit. Hollande's administration plans to address the problem by increasing the taxes paid by France's largest businesses and wealthiest households. While these measures do not address France's systemic economic difficulties, they will allow Paris to skirt a harsher backlash to austerity this quarter.

As the core of Europe weakens, calls for deeper EU integration from both the core and the periphery will grow louder. The peripheral countries will call for more integration to ensure a continued flow of financial assistance, while the more economically stable northern industrial countries will call for additional integration

to assert more control over member nations and to protect the common market for their exports. This model of deeper integration overlaying increasingly divergent interests is not sustainable, but it is a model that will endure for the next quarter as the European Union prepares for an October summit on EU integration proposals.

France's push against Germany for stimulus-led — as opposed to austerity-led — measures to manage the crisis will continue to provide countries in the European periphery with more political room to push back on austerity and demand more financial assistance (with negotiable conditionality) from European institutions. German intransigence on austerity will relax as Berlin continues to demonstrate a willingness to accommodate countries needing economic assistance in exchange for deeper integration efforts that provide Berlin with more EU-wide authority.

In Germany, Chancellor Angela Merkel's decisions on managing the crisis at the EU level will come under increased scrutiny from within her coalition and government bodies, particularly from the parliament and the Federal Constitutional Court. Though Germany is facing rising internal pressure, Stratfor does not expect a dramatic shift in the German policy of demanding more fiscal discipline and control before discussing forms of debt mutualization and permanent financial aid.

Spain will complete negotiations for a bailout of its banking sector but is unlikely to receive a sovereign bailout this quarter. The European Union cannot afford to cut Spain off from markets because it does not have the funds to support a Spanish bailout and deal with the contagion to other eurozone countries. Should bond yields for Spain and Italy rise to unsustainable levels as these countries issue new debt this quarter, the eurozone will use the short term financial tools at its disposal — short of a sovereign bailout — to alleviate market pressure.

Greece will not leave the eurozone this quarter. Athens will receive further financial aid, which will allow the country to keep operating. The new Greek government will begin a formal renegotiation of the

bailout terms with its lenders, which will keep the Greek crisis at status quo for the third quarter.

One of the main consequences of the continued economic slowdown this quarter will be a decrease in summer employment, particularly in Southern Europe, during the tourist season. Social unrest in the form of protests will be more likely in the tourism-dependent periphery, especially in Greece, Italy and Spain.

## **Middle East**



### **Ongoing Iranian-U.S. Struggle**

Military posturing by both the United States and Iran will again punctuate the third quarter, but both sides will again steer clear of an actual military confrontation. Increased sanctions on Iran will have a limited effect as Iran continues to trade via falsely flagged tankers and shell companies, albeit at higher costs. Iran and the United States will maintain a dialogue behind the scenes in search of a broader accommodation, but Stratfor does not expect any negotiation breakthroughs in the lead-up to the U.S. presidential election. Israel will attempt to pressure the United States into taking more decisive action against Iran but will not risk unilateral action.

## **The Syrian Battleground**

The main battleground between the United States and Iran this quarter will be Syria. The defection of the Tlass family — the Sunni pillar of the predominantly Alawite regime — risks unraveling the regime's Sunni patronage networks in the military and business community.

The Alawites face an existential crisis and will likely band even closer together in the face of a broader Sunni opposition threat. Even so, the psychological impact of high-level defections raises the potential for a Syrian palace coup that would eliminate the al Assads from the regime. Iran and Russia, both of which have deep intelligence links in Syria, will continue providing critical support to the regime to facilitate stronger crackdowns, but these powers will also be maneuvering behind the scenes to produce a non-al Assad alternative that would remain friendly to their interests.

The still-fractured Syrian rebel movement will engage in rounds of diplomacy abroad to build international support but is unlikely to receive much more than it is already getting, namely weapons and money primarily from the Gulf states and Turkey and verbal support and limited intelligence and command-and-control guidance from Western powers. Continued support for both the rebels and the Syrian army from their respective benefactors will result in a steady escalation of violence on both sides. The rebels will remain unable to hold and defend significant territory.

Foreign military intervention in Syria remains unlikely, as neither Turkey nor the rest of NATO is eager to deal with the consequences of military action in another fragile, sectarian regional hot spot. Turkey will maintain a strong military posture along its border with Syria, thereby raising the potential for skirmishes as Syrian forces operate near the border to deny sanctuary to Syrian rebels.

As Syrian-Turkish tensions escalate, Syria and Iran could support Kurdish militant activity in Turkey. If Turkey draws a link between Kurdistan Workers' Party attacks and Syria, Turkish domestic

opinion could shift in favor of Turkey taking more decisive action against Syria, though any Turkish action in Syria will be limited without NATO reinforcement.

## **Turkey Recalibrating**

The constraints Turkey faces regarding Syria and other foreign policy matters is motivating Ankara to resolve Turkey's domestic issues. With less attention consumed by Turkey's power struggle and the Kurdish problem, the government hopes to be able to play a more decisive role in foreign affairs. This quarter will thus see continued efforts by Turkey's ruling Justice and Development Party to reach out to its political rivals. However, the Islamist-rooted party's agenda to transform Turkey from a parliamentary to a presidential system and other contentious proposals to reform the constitution will deny the party the consensus it seeks.

The ruling party will make some progress this quarter in its Kurdish containment strategy. Turkey is investing in a pipeline connecting Turkey to energy resources in Iraq's Kurdish north, thereby undermining Baghdad's control over Kurdish export avenues while enhancing Turkey's. Ankara's accelerated moves in Iraqi Kurdistan will fuel tensions between Turkey and the Shiite-dominated government in Iraq. The project, which will be subject to Kurdish militant attacks as it progresses beyond this quarter, will also exacerbate the standoff between Turkey and Iran over the fate of Syria.

## **Political Accommodation in Egypt**

The accommodation between the Supreme Council of the Armed Forces and the Muslim Brotherhood that Stratfor forecast last quarter will hold through to the next quarter. The military will go along with a Muslim Brotherhood presidency and the remainder of the political transition but will ensure its authority through the drafting of the constitution. The Muslim Brotherhood meanwhile will try to focus on building political consensus with a diverse Cabinet. Overall, the political instability that has characterized Egypt for

much of the past year will quiet down this quarter. Occasional demonstrations will take place, especially by those left out of the grand bargain between the Muslim Brotherhood and the military, but Stratfor does not expect massive protests or clashes with the military and security forces.

Egypt-Israel relations will continue to experience strain as security in the Sinai Peninsula deteriorates further due to the distraction of the Egyptian military with the political transition and a growing influx of Salafist militants into the region. Amid these security concerns, Hamas will be cautious in how it maneuvers with Israel as the group looks to capitalize on the Muslim Brotherhood's political gains and as the Egyptian Muslim Brotherhood begins to engage directly with Israel. Hamas' worsened relationship with Syria will also more visibly orient the organization against the regime and in favor of the Syrian rebellion.

### **Persistent Instability in Libya**

The election of a new government, officially ending the North African country's transition, will not alleviate a deepening rivalry between the hollow authority of the Tripoli-based Libyan central government and the regional city councils (especially Benghazi and Misurata). An overall increase in militant activity in Libya is likely this quarter. We will be closely watching to see if jihadists in Libya shift their campaign from rhetoric to attacks. Given the significance of oil revenues for both the central and regional governments, both will expend efforts to defend Libyan energy infrastructure from tribal and jihadist attacks.



# Former Soviet Union



## Russia's Domestic Challenge

The Kremlin faces internal challenges in the third quarter as it and various opposition movements prepare for regional and municipal elections in the fourth quarter. The elections will be held under a law that gives non-Kremlin groups a better chance to win gubernatorial and mayoral seats in the regions. For the first time in the past decade, the Kremlin's United Russia party will have to expend considerable effort campaigning in the regions to maintain its hold over the country.

## Russia and Its Periphery

Russia will be particularly active in the Baltic states in the third quarter as it tries to rebuild its clout in the energy and security spheres there. The Baltic states will continue initiatives in energy diversification and regional security to distance themselves from Russia. Both Estonia and Lithuania already have implemented provisions under the EU Third Energy Package, which requires natural gas companies to unbundle their sales, transport and production operations, thereby undermining Russia's energy dominance in the region. Meanwhile, Finland is showing more interest in regional security groups like the Nordic Defense Cooperation. Russia may attempt to counter these moves in the third quarter by trying to exploit divisions between Poland and

Lithuania and offering economic incentives to countries like Latvia and Finland. But Russia's efforts to reverse these regional initiatives will have limited effect for now.

## **Russia and the West**

Russia's relationship with the West will continue to divide into sour relations with the United States and warmer relations with strategic European partners.

Diplomatic and trade spats will intensify between Russia and the United States in the third quarter. With European powers more concerned with their own affairs, Russia will have more room to maneuver in its efforts to keep the United States focused on the Middle East (and hence away from the Russian periphery) without harming relations with France. Russian backing of Syria through arms sales, sanctions evasion and negotiations will remain a key contentious issue between Moscow and Washington.

A recent energy deal between Russia and Germany will help Russia fortify a long-term relationship with Berlin as these two powers continue to deepen their economic ties. Other Central European states are likely to demand similar deals from Moscow, which will test Russia's ability to maintain its energy leverage in these countries.

## **Central Asia: Another Dynamic in Strained Relations**

Central Asia will remain in a precarious state next quarter with continuing protests in Kazakhstan and the threat of a resurgence of Islamist militancy. Now that Uzbekistan has suspended its membership in the Collective Security Treaty Organization military alliance, Tashkent will be able to entertain alternative security relationships with Washington or Beijing. Russia will seek to build its security ties with Kyrgyzstan and Tajikistan in order to contain and maintain pressure on Uzbekistan.

## **Caucasus: Increasing Security Tensions**

The Caucasus region has seen a number of developments in the past few months that will contribute to an increasingly tense security environment in the next quarter. Azerbaijan has significantly increased its security ties with Israel, signing a major defense deal with it this year. Meanwhile, Russia has been emphasizing its security ties with Armenia by signaling its intentions to increase the number of contract troops among its military presence in the country. These trends have increased tensions, spawning border skirmishes between Armenia and Azerbaijan and causing increased psychological operations between Iran and Azerbaijan — raising the potential for instability and miscalculations. Nevertheless, significant constraints will prevent a broader conflict from erupting in the region.

## South Asia



## U.S.-Pakistan-Taliban Negotiations

A breakthrough in U.S.-Pakistani talks in early July will allow limited movement toward broader U.S.-Pakistani negotiations over a post-NATO Afghanistan. In spite of many key differences between these two uneasy allies, shared fundamental interests are driving the two toward cooperation as the United States prepares its military exit from the region. Numerous obstacles remain, however, which will hamper these negotiations in the coming quarter.

The Afghan Taliban is a major presence in these negotiations. Stratfor expects the Afghan jihadist movement to use its militant arm during the politically sensitive period ahead of the 2012 U.S. presidential election to try to strengthen the Taliban's negotiating position. For its part, the United States will continue its battlefield operations to keep military pressure on the Taliban. And Pakistan will continue to face domestic political constraints this quarter that could undermine the negotiations. A power struggle between the government and the judiciary could pave the way for early elections before the end of the year. The broader negotiations among the United States, Pakistan and the Taliban will continue but are unlikely to see much progress this quarter.

## **India's Economic Reality and Foreign Policy Concerns**

The slump in Indian economic growth in the last quarter of the fiscal year of 2011-12 was unavoidable. It reveals underlying stresses on the economy and served as a wake-up call for New Delhi. The Indian government cannot engage in any meaningful short-term economic measures to offset the slowdown, especially since slashing interest rates further would risk exacerbating already rising inflation. Indian policymakers will try more superficial moves that highlight the government's economic expertise in an effort to maintain the perception that Indian economic growth remains on an upward trend. Though India will remain a significant economy, the government's efforts will not hide the fact that exuberance over India's economic prospects is waning.

On the foreign policy front, India will maintain a cautious approach toward efforts in improving Indian-Pakistani ties. New Delhi will steer clear of major commitments or concessions toward Islamabad as it keeps a nervous watch on progressing U.S.-Pakistani negotiations.

## **East Asia**



## **China's Economic, Political and Social Challenges**

In the third quarter, the Chinese leadership will juggle three interrelated issues: Continued economic problems triggered by the global slowdown and lingering European uncertainty; social pressures arising from these economic problems; and the need to build consensus and rebuild legitimacy for the Communist Party of China ahead of the generational leadership transition through the fourth quarter of 2012 and the first quarter of 2013.

On the economic front, mounting fears of a sharp slowdown mean Beijing will continue to prioritize higher growth. Beijing will continue to push infrastructure projects, reflecting the need to use domestic investment to sustain economic activity. Large state-owned enterprises will see their profits continue to fall in the third quarter, and imbalances in commodity markets may further depress state enterprises producing steel, coal and other core materials. Activity in the real estate sector, meanwhile, will pick up, particularly amid revenue difficulties for local and provincial governments and following the latest interest rate cut. Beijing may choose to ignore rising real estate prices despite an official policy of slowing sales.

Labor protests and public protests over various infrastructure projects and social and economic grievances may bring stronger local and central government responses this quarter. Beijing will seek to maintain social stability as it manages political balances amid the final preparation for the leadership transition.

Beijing will also wrap up the Bo Xilai case in the third quarter, seeking a decisive end to domestic and international speculation over the unity of the Communist Party. The sentences for Bo and his wife will likely be harsh to signal decisiveness and confidence. Behind the scenes, however, the Party will be engaged in intense debates as Beijing seeks a cautious balance between competing economic policies and the stability of the political transition, particularly with a series of key personnel appointments to be settled in the third quarter to pave the way for the transition. In general, this means the government will not be afraid to implement short-term solutions to maintain stability, once again delaying any action on the Party's major challenges.

### **Rising Maritime Tensions**

Regionally, the third quarter will see greater attention paid to maritime territorial disputes, raising the potential for inadvertent clashes. In mid-July, the Philippines will lift a ban on fishing in disputed waters. China will follow suit in August, leading to a rush of competing fishing vessels to parts of the South China Sea disputed by the two, followed by their respective coast guards, maritime police and navies. Competition over energy resources will also spur rhetorical, and potentially physical, confrontations. The Association of Southeast Asian Nations will seek an understanding with China on a binding code of conduct for the South China Sea ahead of the group's fourth quarter summit. The Philippines continues to try to draw the United States and others into the discussions, something China strongly opposes, so Beijing may be more inclined to work through ASEAN as opposed to China's preferred bilateral path to reduce the likelihood of U.S. involvement.

### **The Rise of the Japanese Regionalists**

The expulsion of dozens of members of the ruling Democratic Party of Japan amid attempts to pass new tax legislation is likely going to bring an end to Japanese Prime Minister Yoshihiko Noda's government and necessitate a call for new elections in the third or fourth quarter. Although yet another government turnover is not very

unusual for Japan, the election will be a bellwether for determining the status of the country's emerging regionalist parties, which could begin to challenge the political and bureaucratic status quo over the next few years if they can gain momentum.

## Latin America



### **Building Strain on Mercosur**

Trade and political tensions will continue to rise within Mercosur as Brazil and Argentina pursue protectionist policies both within Mercosur and on the international market. These measures have had a detrimental impact on the smaller Mercosur members, Paraguay and Uruguay, whose relationships with larger neighbors Brazil and Argentina will come under further strain in the third quarter. Paraguay's political isolation from Mercosur after former President Fernando Lugo's rapid impeachment will add more tension to the bloc, but Paraguay is not in a position to completely withdraw without significant bilateral economic guarantees. Uruguay will push for trade opportunities outside Mercosur to offset the effects of intrabloc protectionism. Despite increasing disunity, the Brazil-Argentina relationship at the core of Mercosur will endure as both rely on the agreement to manage bilateral economic concerns and their strategic geopolitical rivalry.

### **Pre-Election Tensions in Venezuela**

During the third quarter, attention in Venezuela will focus on the lead-up to the Oct. 7 presidential election. Despite more than a year of conflicting rumors about Venezuelan President Hugo Chavez's health, the Venezuelan leader appears poised to stand for re-election Oct. 7. The election season is shaping up to be a relatively straightforward contest between Chavez and his chief rival, Miranda state Gov. Henrique Capriles Radonski, with Chavez likely enjoying more support. As with any Venezuelan election, there will be occasional bursts of violence between members of opposing political factions, bombastic political discourse and large-scale government spending and purchase announcements made by the Chavez administration to win support of key factions such as the military, petroleum sector workers and the urban poor.

### **Argentina's Search for Financing**

Argentina will spend the third quarter seeking investment in oil and natural gas production in an attempt to reverse a growing energy deficit. To do so, the government will continue to use domestic pools of capital — such as private bank and Central Bank reserves — and both the central government and provincial governments will court international investment. Argentina will not fully settle its outstanding international debts in the third quarter due to restrictions on the government's ability to meet key international demands. These include revising its inflation reporting methodology, a process that would rapidly increase Argentina's national debt. Tight budgets at the national and provincial levels will drive further rent-seeking, and the mining sector will see increased pressure to increase revenue shares and investments from provincial governments similar to the pressure initially experienced by YPF ahead of its nationalization.

### **Mexico's Political Transition and Ongoing Violence**

Mexico's politics will be in transition as President-elect Enrique Pena Nieto builds his government, tries to redevelop Institutional Revolutionary Party patronage networks and seeks backing from



rival factions on issues like energy investment, tax reform and managing the drug cartels when he enters office in December.

Mexico's security situation will remain turbulent. The Sinaloa Federation and Los Zetas and their respective allies will continue to fight for territorial control in the northeast (particularly in Tamaulipas and Nuevo Leon states), while the Cartel de Jalisco Nueva Generacion will maintain its ongoing turf wars in the central and Pacific states (particularly Guerrero and Michoacan) against the Knights Templar. Los Zetas and the Cartel Pacifico Sur will continue operations against the Sinaloa Federation in Jalisco (including the state's capital, Guadalajara) and Sinaloa states.

## **Sub-Saharan Africa**



### **Somalia's Battle Against al Shabaab**

A pro-Somali government offensive led by African Union peacekeepers to flush al Shabaab from its remaining urban strongholds will intensify in the third quarter. A Kenyan-led military siege on Kismayo will occur around August while other African Union peacekeepers continue a steady buildup in Mogadishu. Al Shabaab reprisal attacks against soft targets in Kenya can be expected. Meanwhile, Ethiopia will maintain blocking positions in central and southwestern Somalia. U.S. financial rewards for information on the location of high-value al Shabaab leaders may facilitate the multipronged offensive. Rains that traditionally fall from

September to December could hamper the intervention but will not derail it. Al Shabaab fighters will retreat to their clans in the hinterlands where they can regroup. They will not be neutralized by the end of the quarter.

Somalia will hold elections for a new federal government. On Aug. 20, it will select a new president, ending Somalia's transitional government era. With limited financial resources and no established institutional support, the new government faces tremendous challenges in reversing popular support for warlords and militancy by establishing good governance out of a deeply corrupt system. The new government will try to make slow and incremental improvements to government efficiency and service delivery while taking advantage of enhanced security from the African Union Mission in Somalia and other allied military forces.

### **Nigeria's Struggle with Boko Haram**

The Nigerian government will continue operations against Boko Haram in the northeastern region of the country. Military and security forces will receive training and small equipment upgrades. Government and civil society leaders will attempt to split the movement through back-channel negotiations. Though these efforts will disrupt Boko Haram, they will not significantly undermine the group. Political opposition to President Goodluck Jonathan's administration will provide space in northern Nigeria for Boko Haram to operate. Clashes between government forces and Boko Haram militants and low-intensity militant attacks can thus be expected to continue in the third quarter.

### **Strained Negotiations Between Sudan and South Sudan**

Sporadic clashes between Sudan and South Sudan will persist in the third quarter as both sides attempt to redraw the boundaries of the oil-rich borderland through military force. Military clashes will be interlaced with strained negotiations, but a decisive military or political breakthrough is unlikely. Compared to last quarter, Sudan's military offensive against South Sudan may be more tempered in

the coming months as both sides confront growing political, military and economic constraints. With neither Sudan nor South Sudan in a position to shift the conflict decisively, external assistance, particularly from China and Japan, will remain limited as foreign players maintain a wait-and-see approach to the negotiations.

Economic austerity measures enacted by both Khartoum and Juba last quarter will weaken popular support for both governments. Demonstrations will persist in Sudan, but will not pose a significant threat to the regime. The austerity conditions may compel energy negotiations between Khartoum and Juba in an effort to revive oil revenue streams, but the two governments will remain focused on developing separate spheres of investment and oil development.

### **Islamist Militant Containment in Mali**

With backing from the Economic Community of West African States, politicians in Mali will be focused on regaining political legitimacy this quarter as civilian and military authorities in Bamako engage in power-sharing negotiations to form a new national unity government. The political distractions will prevent effective coordination or deployment of resources from the capital to counter Islamist militant gains in the northern half of the country.

Militant activity will largely be contained to northern Mali this quarter due to the fractured nature of the Tuareg rebels and their common interest with al Qaeda forces to protect smuggling routes from outside intervention.

The Economic Community of West African States will engage in military operations in Mali, but these will remain limited without Western support. Contingency plans for a West African-led foreign intervention are under discussion, but Stratfor does not expect the plans to become operational so long as militant activity is contained in northern Mali. Western powers with counterterrorism interests in the region, primarily the United States and France, will rely instead on unilateral special operations forces' strikes against al Qaeda forces in the region to contain the transnational jihadist threat.