# Global Macro Views

January 2017

By: The Standish Global Macro Committee

Rebecca Braeu, PhD, CFA; Rowena Geraghty;

Aninda Mitra; Javier Murcio; Vincent Reinhart; Nicholas Tocchio

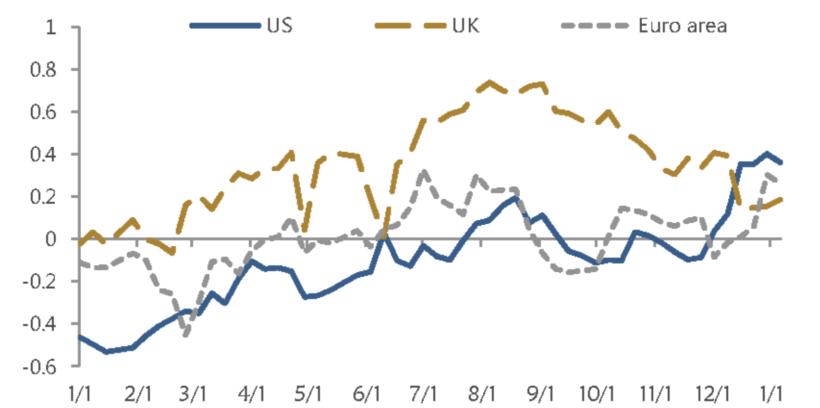
**World:**

| | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 2.9% | 3.3% | – | 3.2% | – |
| Inflation | 6.0% | 4.9% | – | 4.9% | – |

Source: Standish as of January 10, 2017

What a difference a day makes, especially when that day, November 8, 2016, brought into office as unconventional a political force committed to change as Donald Trump. Since the election, the halls of Washington, DC and the lobby of the Trump Tower in NY have been filled with talk of increased infrastructure spending, tax reform, and regulatory relief. Economic data have come in stronger than forecasted by economists, and surveys show consumers and businesses to be more confident. Equity prices have gained 8-1/2 percent, creating more wealth for households, and sufficient to offset the drag associated with a ½ percentage point increase in longer-term yields. As a result, we have marked up the Standish forecast for US real GDP growth in 2017 and expect some of this strength to be shared with trading partners in light of appreciation of the foreign exchange value of the dollar. This provides important support at a time when the Federal Reserve is tightening policy and the European Central Bank and the Bank of Japan seem unable or unwilling to ratchet up their monetary accommodation.

**Economic Surprise Indexes**




Source: Bloomberg as of 1/9/17.

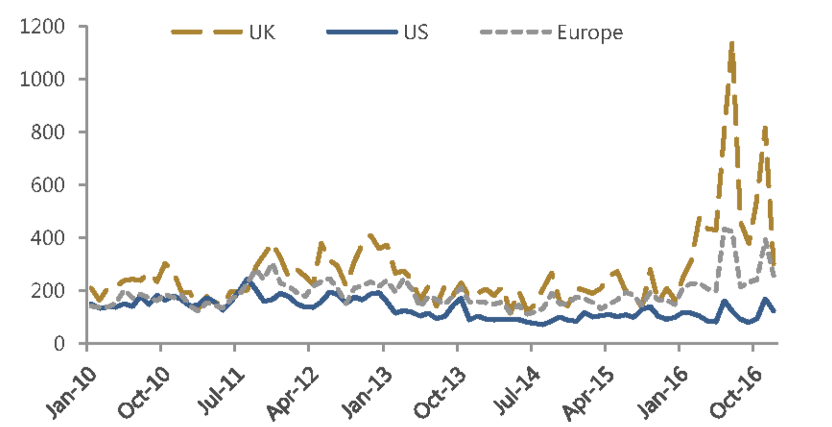
Still, we have only nudged up our growth outlook in advanced economies on the worry that financial market participants may have gotten ahead of themselves in expecting more changes, sooner, than can be delivered from the incoming team. Regulation is complicated, big companies have adjusted to the old regulations and will resist change, and legislation almost always takes longer to enact than hoped at the beginning. We expect early executive action on energy and immigration and a bill passed providing for modest infrastructure investment and corporate tax



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months – no bias
Inflation forecasts are yearly annual averages of headline CPI.

reform. After that, all bets are off. The White House, the House of Representative, and the Senate will have to negotiate across a wide range of contentious issues. This will almost surely elevate uncertainty about US economic policy even as France and Germany provide their own electoral drama and the UK negotiates its exit from the European Union. While a widely-followed measure of economic policy uncertainty has moved lower of late, it still remains high by historical standards. Until the political dust settles down more, the environment will be unconducive to longer-term capital investment that would provide a sustained lift to aggregate demand.

**Economic Policy Uncertainty Index, Long-term Average=100**




Source: Baker, Bloom, and Davis, via Blooomberg as of 1/9/17.

We also retain our dour view of aggregate supply, which limits how far self-fulfilling momentum can take aggregate demand. The trajectory of potential output in major advanced economies remains relatively flat, hamstrung by slower population growth and sluggish population gains. True, there is scope for structural reform in many of those countries and fiscal space for a boost to spending in a few, but such changes require a strong political will to try, are hard to execute well, and would take time to leave their imprint on activity.

The modestly more positive outlook for advanced economies is offset by a few downticks in our growth projection for emerging market economies. Cyclical momentum in Chinese GDP growth should be sustained through the first two quarters of 2017 but at the cost of delaying reforms and worsening the national balance sheet. These forces create drags that will become more evident in the second half of this year and next. The political reality, however, is that significant reforms are unlikely until the Party Congress is completed in November, which should confirm the extension of President Xi's hold on power for another four years. Mexico's budgetary situation had already taken a turn for the worse when it was hit by the external storm of a potentially protectionist northern neighbor. The inflationary impetus of significant peso depreciation will force the Bank of Mexico to run tighter monetary policy than previously expected, even as fiscal retrenchment and Trumpian trade headwinds pick up in velocity.

The easy part of 2017 for the Federal Reserve will be monetary policy. With the labor market close to full employment and inflation headed toward their goal of 2 percent, the Fed can remove some accommodation. They will go slow because an appreciating dollar does some of the work of policy firming, and Janet Yellen will need proof that maximum employment has been achieved. But they will tighten, probably two times this year (even though they said three times at their December meeting). The modest adjustment widens the policy rate gap with Europe and Japan, as we expect continued, but not necessarily increased, accommodation from the ECB and BOJ. As for the former, the contentious nature of the compromise decision of the Governing Council in



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

December to scale back the monthly purchase amount but lengthen the window of large-scale asset purchases suggests that its future actions may be similarly less predictable.

Politics may make this year otherwise hard on the Fed and adds uncertainty to the US outlook. The Congress will consider Fed reform legislation, and the appointees filling the two open Board seats will tilt the FOMC toward the hawkish side. More importantly, once the initial round of cabinet appointees is filled by the early summer, attention will turn to who will be appointed to replace Janet Yellen in February 2018.

**Developed Markets:**

| United States | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 1.6% | 2.1% | ↑ | 1.9% | ↓ |
| Inflation | 1.3% | 2.4% | ↑ | 2.5% | ↑ |

Source: Standish as of January 10, 2017

Incoming data point to ongoing momentum in US economic activity, supported in part by slightly more accommodative financial conditions and more buoyant household and business confidence. The November election, of course, is responsible for some of this, but reading the political tea leaves, or tweets, is not an especially firm basis for an economic forecast. On net as of now, we take the likely economic agenda to be a modest positive for the growth of US aggregate demand, reflected in our upward revisions since the November forecast, and an upside risk to the point forecasts for growth and inflation. The outlook for GDP, however, is anchored by our dour assessment of aggregate supply trends. Faster capital spending may arrest the slowdown in productivity, but that will take some time to get traction. For the next few years of the forecast period, potential output growth will be hemmed in by slow population growth and a sluggish increase in output per hour.

Aggregate demand, though, gets a boost. Infrastructure spending and corporate tax changes are likely to be legislated early on, with the former offering some encouragement to public-private partnerships and the latter paired in the package so as to limit the rise in the federal deficit—at least as scored by budget officials. Judging by some of the early personnel picks, the incoming administration is also likely to move quickly to lessen regulatory strictures on the exploration, extraction, and shipment of energy. Those activities are capital intensive and, over time, should help to distribute energy more efficiently through the middle part of the nation to the comparative cost benefit of manufacturing. Other reforms will take time to maneuver through the legislative and regulatory thicket, but expect a shift in financial regulation as the heads of agencies change, encouraging the extension of credit. Changes in the personal income tax code will probably be deferred to allow specific legislative proposals from Capitol Hill, while wrangling over the Affordable Care Act will consume considerable political energy but not have an immediate material economic effect.

Trade relationships are more problematic. The White House could use executive authority to abandon ongoing global trade negotiations and backpedal on some existing agreements. Entrenched interest will lead large firms to push back forcefully on radical changes, suggesting relatively modest net movement associated with somewhat lower trade flows. There will likely to be limited, at best, benefit to domestic employment, modest additional pressure on costs, and an



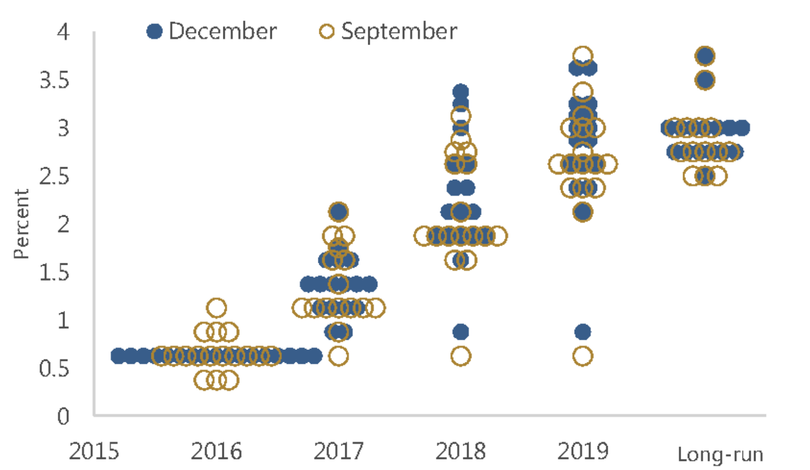
↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

asymmetric effect on our trading partners whereby the drag on their activity will be greater than the boost to ours.

Quarterly arithmetic matters. US economic expansion has been decidedly uneven this year, with GDP growth below 1 percent in the first half and closer to 3 percent in the second half, and, despite the best efforts of the Bureau of Economic Analysis, this first-quarter statistical pothole is likely to recur in 2017 and 2018. We have not changed our Q4/Q4 growth outlook much, but annual growth rates move up more notably given the back-loaded nature of the quarterly outcomes.

With resource slack shrinking and the earlier decline in commodity prices receding in the rearview mirror, US consumer price inflation picks up to around 2 percent by the turn of the year and above thereafter. While the Fed's recent interest rate guidance indicated an intention to execute three quarter-point firmings in 2016, in the Standish view the Fed moves more slowly than that, allowing inflation to breach its 2-percent goal. This inflation overshoot will be compounded by a further rise in the inflation risk premium as investors recoil from both higher volatility and the sticker shock of rapid consumer prices changes.

**Summary Of Economic Projections**




Source: Federal Reserve Board as of December 28, 2016

The majority of the Fed's Board will turn over by 2018, including those in the two most important spots, the chair and vice chair. A dovish leader matters for 2017, however, which is why we do not take the FOMC precisely at its word. Gradual policy renormalization presents opportunities for Chair Yellen to agree to the general principle of three quarter-point moves in 2017 but fret in public about an elevated risk of some sort, effectively taking action off the table at the next meeting. Do that a few times and the FOMC will run out of runway in 2017 to tighten three times, just as they only managed to sneak in one action at the end of 2015 and 2016. As a result, we believe the Fed tightens twice in 2017, with some risk of slipping in a third action, *assuming* that the White House only moves slowly to put its stamp on central bank policy.

| Euro Area | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 1.6% | 1.4% | ↑ | 1.3% | – |
| Inflation | 0.2% | 1.3% | ↑ | 1.1% | – |

Source: Standish as of January 10, 2017

Euro Area economic data are beating expectations, most notably including survey data such as the PMI. However, in our economic outlook, this evidences a slight manufacturing upswing that is unlikely to continue unabated through 2017 as the European election calendar gets underway, Chinese policy becomes decidedly less supportive, and the commodity cycle stabilizes within our oil range of $50-$60, rather than bursting toward $70. Together, the evidence points to near-term upside risks to headline inflation but medium term downside risks to expectations for core, hence headline, inflation are very real. The depreciated exchange rate is stabilizing the dynamics of core inflation slightly, rather than boosting prices materially. Put together, we must recognize that energy prices are better on OPEC and food prices are higher than expected as we upgrade our 2017 inflation forecast to 1.3% from 1.1% and see risks tilted to the upside. Our read of our competitors' forecasts suggests that we are comfortably below consensus. Before making any more material upgrade to our forecast, we would need to have in hand evidence that oil trades in the upper end of our range and that core inflation runs above our low expectations through year end. In short: we are comfortable with 1.4% and downside risks.

| Japan | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 0.5% | 1.0% | – | 0.8% | – |
| Inflation | -0.1% | 0.9% | – | 1.1% | ↓ |

Source: Standish as of January 10, 2017

The jump in US and global yields amid the Bank of Japan's (BoJ) yield-curve-control (YCC) and ongoing quantitative-and-qualitative easing (QQE) has widened yield differentials and accelerated Yen weakness. Alongside rising oil prices, tight labor markets and rising wages, a weaker Yen should soon begin turning around the softening trend in consumer price inflation. Market expectations of higher inflation is also reflected in the break-even 10 year yields which have been grinding higher, and firmer inflation expectations per Tankan surveys. That said, we still do not expect inflation to rise rapidly towards the BoJ's 2% target anytime soon. This is because of the dominance of adaptive price expectations, and Japan's long history of deflation as well as a near-flat Philips curve which will prove hard to overcome. Meanwhile, economic growth should be maintained at an above potential pace through 2017 on the back of accommodative financial conditions and the effects of the government's fiscal stimulus measures, as well as a gradual improvement in global demand. We are raising this year's inflation forecast, and next year's growth forecast a bit by one-tenths of a percentage point, with a generally stable balance of risk over the coming 6 months. The brightening trend in Japan's macroeconomic outlook should anchor Prime Minister Abe's popularity ratings. However, a recent effort to build a closer geo-political relationship with Russia did not result in any breakthrough on Japan's long-standing demand for a hand-over of the Kuril Islands –which were lost to the Soviet Union at the end of World War II. As a result, the prospect of early elections is now slipping to later in 2017.

| United Kingdom | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 2.0% | 1.0% | – | 1.0% | – |
| Inflation | 0.8% | 2.8% | ↑ | 2.5% | – |

Source: Standish as of January 10, 2017

The focus in the UK remains squarely on Brexit, with key events including the Supreme Court judgement on the use of Royal Prerogative to trigger Article 50, whether Article 50 is triggered before the end of Q1 2017, and the outcomes of the French and German elections.

Despite PMIs continuing to point to economic strength as we enter the new year, we continue to forecast a slowdown in the UK economy in 2017 as uncertainty casts a pall on the decisions of consumers and firms. Household consumption (fuelled by increased debt as real-incomes take a hit from higher inflation) is likely to be the main driver of growth in 2017, although the government's fiscal consolidation will be less front-loaded than previously observed. Business investment is likely to be most significantly hit by uncertainties regarding the UK's future trading relations with Europe, although net exports are likely to benefit from weaker sterling in the short-term at least.

While growth will take be negatively impacted in 2017, the significant upturn in inflation through mid-2017 is likely to be most noticed by markets—driven by sterling weakness and base effects (related to oil and food). We do not expect the Bank of England to respond to this uptick in inflation, and extend to remain in a neutral policy stance—with future policy moves potentially driven by political, rather than economic events.

**Australia and New Zealand:**

| Australia | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 2.4% | 2.6% | ↓ | 2.2% | ↓ |
| Inflation | 1.3% | 1.8% | – | 2.0% | – |

Source: Standish as of January 10, 2017

| New Zealand | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 2.8% | 2.8% | – | 2.6% | – |
| Inflation | 0.7% | 1.4% | – | 2.0 % | – |

Source: Standish as of January 10, 2017

The lift in Australia's bulk commodity export prices has recently begun to flow into the economic data—resulting in a significant upside surprise in the November trade balance. Pair this strong export data with encouraging indicators for the services industry, and Australia appears to be on firmer footing going into 2017, putting to rest worries of a technical recession following the disappointing Q3 GDP print. However, the economy still has challenges heading into 2017. In our view, the Reserve Bank of Australia (RBA) may have to ease interest rates again, contrary to current market pricing and expectations. Core inflation remains subdued, and domestic



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

headwinds should keep a lid on prices. If we get another leg lower in trimmed mean inflation, the RBA will need to lower their forecasts (again), and may deem more accommodative policy to be necessary. Our call on the RBA is more of a mid-2017 story and will take time to play out.

There also exist doubts as to whether Australia will retain its AAA sovereign credit rating this year. If further fiscal slippage is revealed in the next budget released later this year, a downgrade would be likely.

In New Zealand, strong economic performance continues – but we think that interest rate hikes from the Reserve Bank of New Zealand are not likely until 2018 due to headwinds from a high trade-weighted New Zealand dollar, housing imbalances, and low inflation backdrop.

## Emerging Markets:

### Asia:

| China | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 6.7% | 6.4% | – | 6.0% | – |
| Inflation | 1.8% | 2.1% | – | 1.9% | ↓ |

Source: Standish as of January 10, 2017

The cyclical momentum in GDP growth should be sustained through the first two quarters of 2017. Fiscal policy support remains important, as will additional rounds of debt swaps to ease, and term-out, the debt servicing burden of local governments. Additional features of the authorities' countercyclical efforts will include more PPP projects to boost infrastructure investment, and even some debt-to-equity swaps to limit Chinese banks' exposure to questionable assets and shadow bank intermediaries. However, property market regulations will continue to be tightened as policymakers have become increasingly concerned about rapid real estate price increases. A centerpiece of China's counter-cyclical effort through much of 2016 was to lower nominal and real rates. But this has raised risk-taking and leverage and is elevating total non-financial private debt at more than twice the pace of nominal GDP. In this context, the central bank will acquiesce to further interest rate increases in onshore rates so as to ensure financial stability. Alongside higher nominal rates, more stringent capital controls and greater two-way volatility in the CNY fixing will also be deployed to stabilize onshore FX expectations. But these stabilization efforts will eventually result in a fading of cyclical tailwinds. We expect China's worsening structural drags to become more dominant in the second half of 2017. For the full year, the pace of GDP growth slows to around 6.4% year-over-year, from 6.7% in 2016. We do not expect much by way of significant reforms until the Party Congress is completed in November—which should confirm the extension of President Xi's hold on power for another four years. These trends accord with a stable balance of risks over the coming six months, and only a slight softening in commodity prices. The main tail-risk to the macro outlook arises from the outbreak of trade protectionism between the U.S. and China, under a Trump-presidency.



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

| South Korea | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 2.6% | 2.5% | ↓ | 2.8% | – |
| Inflation | 1.0% | 1.3% | ↓ | 1.5% | – |

Source: Standish as of January 10, 2017

The effects of recent setbacks at Samsung's Galaxy-7 production and strikes at Hyundai Auto have begun wearing off. Production and exports have begun rising, but are lagging the pickup in the electronics cycle elsewhere in the region. Despite these belated improvements, consumer and business sentiment remains weak and PMIs languish below 50. The main reason for the downbeat sentiment is the political vacuum brought on by the impeachment of President Park—which is currently awaiting approval from the country's constitutional court. As the impeachment and succession process could take another 3 to 6 months, the prospects for meaningful near-term countercyclical fiscal policy remains limited. Pro-active crisis mitigation strategies for limiting corporate and household distress, a large current account surplus, low sovereign debt and a vibrant corporate sector provide buffers against rapid credit deterioration. But until the political uncertainty clears, there will be sustained pressure on the central bank to deliver more policy easing. Meanwhile, currency pressure on the Won is also likely to persist. Additionally, growing geopolitical tensions with North Korea, alongside the prospect of an inward turn in US politics, should add to the weakening bias in the currency. Korea's growth and inflation profile will be stuck in low gear, and the balance of risk remains tilted lower until the formation of a new government.

| India | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 7.5% | 6.8% | ↓ | 7.8% | – |
| Inflation | 5.3% | 4.8% | – | 5.3% | – |

Source: Standish as of January 10, 2017

The government's de-monetization exercise to stamp out corruption has dented the near-term growth outlook, but, arguably, could improve India's medium-term fiscal and macro prospects. The step of annulling 85% of the face value of currency in circulation, and replacing it with new notes—so as to track deposits and exchanges and identify potential tax evaders –has adversely impacted services and consumption across the country. While the deadline for deposits, or exchanges, of old currency notes has passed, a full replenishment of the old currency will take more time. As a result, quarterly GDP growth could slip to around 6% in this quarter and the next, dragging core inflation lower as well. Moreover, banking liquidity has also risen and the structure of interest rates has compressed. De-monetization, coupled with the ongoing increase in electronic payments, should dent the future flow of illicit funds, though, not the stock of black money. That said, higher financial savings—and lower currency intensity— should lower inflation and the cost of capital over the medium term. The tax base will likely broaden on account of more easily identifiable large depositors (and potential tax payers.) All in all, in 2017, GDP growth could sink to a sub 7% rate, and inflation to below 5%; and the balance of risks are tilted lower amid the absence of a firmer countercyclical fiscal push to offset the weakness in private demand. Any fiscal



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

dividend from un-exchanged cash (which lowers the central banks' liabilities) is likely to be small, and mostly spent off budget for recapitalizing the country's worst-off public sector banks. But over the medium term, a broader tax base coupled with GST (goods and services tax) implementation in the second half of 2017 should begin to raise tax revenue and overall economic efficiency by 2018.

**Latin America:**

| Brazil | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | -3.6% | 1.5% | ↓ | 1.5% | – |
| Inflation | 8.3% | 5.1% | ↓ | 4.7% | – |

Source: Standish as of January 10, 2017

| Mexico | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 1.9% | 1.2% | ↓ | 2.5% | ↓ |
| Inflation | 3.4% | 4.5% | ↑ | 2.9% | ↑ |

Source: Standish as of January 10, 2017

The year 2017 should be a year of recovery for most Latin American economies. Economic growth disappointed in 2016, with average expansion at or slightly below potential output. Now, the recovery in commodity prices, improved outlook for developed countries (in particular the US) and fundamental stabilization in most of the LATAM-6 are leading to some rebound in consumer and business confidence. Importantly, the recovery should be accompanied also by decelerating inflation, improved fiscal accounts and external balances under control. On that basis, we expect looser monetary policy and a continuation of fiscal prudence in Argentina, Brazil, Chile, Colombia and Peru. The recession experienced by Argentina and Brazil is coming to an end and these two economies should be able to achieve growth in the 1-2% range. Chile and Peru should be able to benefit from stable metals prices, although the former will experience some volatility associated with the upcoming presidential elections. Colombia should benefit from the important events of 2016, namely, stronger oil prices, the completion of a peace agreement and the passage of a fiscal reform. In all of the countries mentioned so far, currencies are expected to stabilize against the US dollar, as external accounts remain under control and capital is beginning to flow back again. Mexico is the one country where the outlook remains extremely complicated. The outcome of the US presidential election suggests a challenging environment ahead for immigration and remittances, free trade with the US, FDI flows into Mexico, etc. Domestic pro-cyclical economic policy complicates matters even more. Rising leverage over the last four years is now being addressed with budget cuts and a poorly timed gasoline price increase aimed at helping PEMEX, the national oil company, and to rationalize fuel pricing policy. The latter is putting pressure on inflation expectations, which have been hurt already by the devaluation pressure on the Mexican peso. With the US Federal Reserve on track for further interest rate hikes, monetary policy will have to remain hawkish during the year. All of this is leading to a collapse of investor confidence; therefore, growth estimates are being revised downwards and, even though consensus growth



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

still shows a 1% handle, chances of a recession cannot be ignored in 2017. At the same time, Mexico's external accounts are not expected to show major improvement. Overall, ratings action in the LATAM-6 is likely to remain muted for most of these countries this year, with the exception of Mexico, where at least one downgrade (within the investment grade category) is likely. Overall, the major risks to the region are largely associated with US policy, particularly if protectionist policies are enacted and this leads to a global trade war. US growth is expected to be stronger than previously expected, but if this (and commodity price strength) is derailed by the international trade environment, high interest rates or a strong dollar, LATAM will suffer headwinds against its recovery.

**Poland, Hungary, and Romania:**

| Poland | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 3.0% | 3.2% | – | 3.0% | – |
| Inflation | -0.5% | 1.3% | ↑ | 1.8% | – |

Source: Standish as of January 10, 2017

Central and Eastern Europe will remain a relative haven within the emerging market (EM) context in 2017, featuring similar factors as core markets (continued growth, upturn in inflation, populist politics) rather than being exposed to the expected EM risks of Trump's trade policies and concerns regarding China. Stable developments in the Eurozone, combined with a catch-up in the absorption of EU structural and cohesion funds, will see growth remain resilient – driven by strong household consumption (strong real wage growth in particular) and public investment (EU funds absorption increase after a poor 2016 due to intense bureaucracy). Inflation will also rise, driven by base effects related to oil and food – although it will follow the same trends as seen in the Eurozone. Monetary policy will remain on hold in Poland and Romania, and we will continue to see unorthodox easing in Hungary. Fiscal expansion will continue across the region, although the crucial 3% budget deficit/GDP will continue to be followed by even the most populist of governments. There are no significant elections in the region in 2017, although the continued tensions between the EU/Russia over Ukraine and the threat of continued refugee/migrant flows from Turkey will remain in a year where changes in leadership in France and Germany will impact on EU relations as a whole.



↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

**Russia, Turkey, and South Africa:**

| Russia | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | -0.5% | 1.2% | ↑ | 1.2% | – |
| Inflation | 7.0% | 4.5% | ↓ | 4.5% | – |

Source: Standish as of January 10, 2017

| Turkey | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 3.0% | 2.5% | – | 2.5% | – |
| Inflation | 8.0% | 10.0% | ↑ | 8.0% | – |

Source: Standish as of January 10, 2017

| South Africa | 2016 | 2017 | Balance of Risks | 2018 | Balance of Risks |
|---|---|---|---|---|---|
| Real GDP Growth | 0.3% | 1.0% | ↓ | 1.3% | ↓ |
| Inflation | 5.8% | 5.5% | – | 6.0% | – |

Source: Standish as of January 10, 2017

As we enter 2017, the divergence seen in major local markets in CEEMEA last year will continue. Russia will continue its process of economic recovery as it emerges from recession, aided by the significant recovery in oil prices. Inflation will also continue to trend downwards and there is a sizable chance that the 4% central inflation target could be attained by the end of 2017, aiding the credibility of easier monetary policy going forward. Fiscal metrics still remain under stress, but the ability to issue Eurobonds at attractive levels will reduce the depletion of reserves. Given the incoming President Trump and more inwards looking Chancellor Merkel, there is potential for current Crimea sanctions to be lessened towards the end of 2017.

South Africa will also see economic recovery in 2017, albeit weaker than Russia's – aided by resilience in global commodity prices. Inflation will remain relatively stable near the top end of the central bank's inflation tolerance band, and we expect monetary policy to remain on hold (unless there is significant weakness in ZAR). Fiscal policy will remain constrained by debt metrics, whilst the lack of structural reforms will continue to frustrate investors. Political tensions will remain considerable given the unpopularity of President Zuma, but we do not expect to see his departure prior to the ANC conference in December 2017 (nor the departure of Finance Minister Pravin Gordhan) – with 2017 H2 relatively nosier in terms of political headlines than H1.

Turkey will be the weak spot in CEEMEA in 2017 as the first half of the year is dominated by the constitutional referendum, which is the final step in President Erdogan's quest for an executive presidency – and whilst the referendum is expected to pass, there will be tensions surrounding it. Once this political event has passed, we would expect stabilisation in Turkish assets. Growth is expected to remain relatively resilient despite such uncertainties (as has been seen in previous years), whilst inflation will remain elevated and significantly above the central bank's target. The failure of the central bank to increase interest rates despite TRY weakness has not installed investor confidence however though.

↑ positive surprise more likely over next six months. ↓ negative surprise more likely over next six months — no bias
Inflation forecasts are yearly annual averages of headline CPI.

BNY メロン・アセット・マネジメント・ジャパン株式会社
BNY Mellon Asset Management Japan Limited

金融商品取引業者：関東財務局長（金商）第 406 号
〔加入協会〕一般社団法人　投資信託協会
一般社団法人　日本投資顧問業協会
一般社団法人　第二種金融商品取引業協会