



Global Economic Scenario

April 2014

Revisions since last month (in brackets forecasts as per previous month)

	GDP 2014				GDP 2015				CPI 2014				CPI 2015			
	Swiss Life AM		Consensus		Swiss Life AM		Consensus		Swiss Life AM		Consensus		Swiss Life AM		Consensus	
USA	2.5%		2.8%	(2.9%)	2.4%		3.1%	(3.0%)	1.7%	(1.8%)	1.7%	(1.6%)	2.3%		2.0%	(1.9%)
Euro Area	1.3%		1.1%	(1.0%)	1.4%		1.4%		1.1%	(1.2%)	0.9%	(1.0%)	2.0%		1.3%	(1.4%)
Japan	0.8%	(0.9%)	1.4%	(1.6%)	0.9%		1.3%		2.3%	(2.4%)	2.6%	(2.4%)	1.1%		1.7%	
UK	2.4%	(2.2%)	2.7%		1.9%	(2.0%)	2.5%	(2.4%)	2.1%		2.0%	(2.2%)	2.7%		2.2%	(2.3%)
Switzerland	1.3%		2.1%		1.3%		2.2%	(2.3%)	0.1%	(0.2%)	0.3%	(0.4%)	0.6%		0.9%	(1.0%)

USA – Another step towards policy normalisation

GDP Growth

Swiss Life Asset Managers	Consensus
2014: 2.5%	2014: 2.8%
2015: 2.4%	2015: 3.1%

The current account deficit published recently for the last quarter of 2013 narrowed dramatically yet again. This marks the seventh consecutive quarter that the deficit has actually fallen and now amounts to 1.9% of GDP which is the lowest level since 1997. Consequently, the trade balance gave a notable lift to overall GDP growth in the last quarter of 2013 as exports posted the biggest positive contribution since the last quarter of 2010. A shrinking current account deficit means that US consumers are exporting ever fewer dollars to the rest of the world which should actually help to reverse the surprising weakness of the Greenback. Much of the improvement in the trade balance can be traced back to the rising energy independence and the resulting decline in energy imports. This development plays an important role in our longterm economic scenario and will in our view also result in rising repatriation of manufacturing activities as US companies appreciate access to cheaper energy. Yet, despite sound profit growth, loose financial conditions and elevated capacity utilization rates, companies have abstained from investing noteworthy in machinery, structures and intellectual property. As slack has been reduced steadily and since business confidence has brightened up substantially over past quarters, we would expect more growth impetus from business fixed investment in the second half of this year. This is evident in the Business Roundtable's CEO Economic Outlook

Index which shows confidence rising to an eight-quarter high. This also translates into more aggressive investment plans in the survey, as the share of respondents anticipating higher capital spending rose to a level not exceeded since the second quarter of 2011. Meanwhile the Federal Reserve announced to put less weight on the unemployment rate as a threshold for when rate increases will start, just at a time when new jobless claims have dropped again indicating that the unemployment rate is likely to break the threshold of 6.5%. The Fed thus shifts to qualitative guidance, considering a wider array of indicators such as “measures of labour market conditions, indicators of inflation pressures and inflation expectations and readings on financial developments”. Now that the worst of weather turbulences should be over, the housing market may potentially be facing the risk of an earlier tightening of financial conditions. Some of that risk is reflected in our below consensus growth forecast for next year.

Inflation

Swiss Life Asset Managers	Consensus
2014: 1.7%	2014: 1.7%
2015: 2.3%	2015: 2.0%

February marked the low point in our inflation path. With a reading of 1.1% headline inflation, the rate remains well below the Federal Reserve's goal. Driven by higher contributions from the housing as well as medical care components, we forecast the headline inflation rate to notch up to close to 2% by the end of this year. Furthermore, the pace of wage inflation has picked up somewhat and should accelerate as labour market slack gets worked off.

Source for Consensus Estimates: Consensus Economics Inc. London, 10 March 2014



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Euro Area – Green light for banking union

GDP Growth

Swiss Life Asset Managers	Consensus
2014: 1.3%	2014: 1.1%
2015: 1.4%	2015: 1.4%

Our simple growth model derived from the purchasing managers' index would actually indicate a quarterly GDP growth rate of 0.5% for the region as a whole in the first quarter of this year. Since such an acceleration seems a bit too ambitious, we computed a more modest 0.4% quarterly growth rate into our path which would still mark the best performance since the first quarter of 2011. The economic and fiscal adjustments of the last four years have put large parts of the Euro Area on a much more solid footing for future growth, which will help to stabilise the financial system and hopefully help to open the credit valves of commercial banks. Furthermore, the Banking Union has come a step closer and the final details have been agreed upon. The completion of the Banking Union should boost trust between Eurozone banks and market confidence in the entire banking system a bit further. Moreover, the ECB's asset quality review and stress test this year will clean the air further. Key for the sustainability of the economic recovery phase is the health of the banking system and the ability of banks to give out loans to the private sector. Certain business investments seem overdue and their realisation will help to solidify economic momentum.

Inflation

Swiss Life Asset Managers	Consensus
2014: 1.1%	2014: 0.9%
2015: 2.0%	2015: 1.3%

The inflation print for March will again move slightly lower and thus has the potential to trigger renewed fears as regards the slide of the region into deflation. From March onwards, however, our forecast implies a modest but continuous increase in headline inflation and a level of 1.6% by the end of this year. A certain downside risk to our inflation forecast is the latest appreciation of the Euro. As the US Fed is closer to policy tightening than the ECB, we consider the Euro strength to be a temporary phenomenon.

Japan – Macro data post negative surprises

GDP Growth

Swiss Life Asset Managers	Consensus
2014: 0.8%	2014: 1.4%
2015: 0.9%	2015: 1.3%

Since last month, nothing happened in Japan to make us rethink our view that Abenomics is about to fail. We reiterate our sub-consensus forecast for growth this year and in 2015. The economy already started to lose steam by the end of last year as shown in the downward revision to the GDP numbers for the final quarter 2013. We highlighted many times that prime minister Abe's ambition to reflate the economy on a sustainable basis requires more than one-off effects on the level of prices via a sharp devaluation of the currency and the introduction of two sales tax hikes this year and in 2015. Anecdotal evidence so far suggests that the current round of wage settlements will result in 2% to 3% nominal wage increases this year. With Japan's labour force shrinking by around 1% each year, the aggregate increase in disposable incomes is not enough to compensate for the higher sales tax coming into effect next month. Real incomes thus continue to shrink. Accordingly, consumer confidence continued to deteriorate further, reaching the lowest level in 18 months. Investors as well are losing faith in Japan's economic policy experiment: The government's call for higher wage settlements to be awarded by the corporate sector would result in a margin erosion. This together with the recent strengthening of the Yen made Japan's equity market clearly underperform relative to its peers in other developed regions over the last two quarters.

Inflation

Swiss Life Asset Managers	Consensus
2014: 2.3%	2014: 2.6%
2015: 1.1%	2015: 1.7%

As per April, the sales tax hike from 5% to 8% will finally be implemented. Throughout the second quarter, economists will be eager to find out how much of the higher tax burden on retailers can be passed on to consumers. We expect inflation to temporarily surge to 3.2% in the next quarter, but remain highly skeptical about the sustainability of this measure in Japan's fight to reflate its economy.



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UK – Earnings growing faster than inflation

GDP Growth

Swiss Life Asset Managers	Consensus
2014: 2.4%	2014: 2.7%
2015: 1.9%	2015: 2.5%

As the first quarter 2014 is approaching its end, the data so far available allow a rough estimate on the economic performance over the last three months: Those indicators correctly signalling the economic recovery last year, namely our model based on the purchasing managers index (PMI) covering activity in the manufacturing sector and the tracking growth estimate provided by the National Institute of Economic and Social Research (NIESR), suggest an acceleration to 0.8% quarterly GDP growth. We currently expect a somewhat slower pace of just 0.6% given the slightly disappointing real economic data related to industrial production, retail sales and also foreign trade. Drags in the form of continued fiscal austerity and tighter financial conditions via the gradual removal of extraordinary monetary policy measures and the recent strengthening of the British Pound explain our cautious forecast for growth in 2015 relative to the consensus estimate.

Inflation

Swiss Life Asset Managers	Consensus
2014: 2.1%	2014: 2.0%
2015: 2.7%	2015: 2.2%

According to our projection, inflation is set to climb from an average 1.8% in the first quarter 2014 to 2.3% during the fourth quarter. Recent trends in workers' earnings growth suggest that real wages are set to grow for the first time since many years. It is thus justified that retailers' selling price expectations rebounded since mid last year according to a Confederation of British Industry (CBI) survey. This survey is statistically significant to explain trends in core inflation and usually leads actual turning points in the inflation cycle by six months.

Switzerland – Still no meaningful inflation in sight

GDP Growth

Swiss Life Asset Managers	Consensus
2014: 1.3%	2014: 2.1%
2015: 1.3%	2015: 2.2%

On March 18, the State Secretariat for Economic Affairs (SECO) went to the press with its revised economic forecasts. Compared with last December, SECO lowered its estimate for 2014 slightly to 2.1% from 2.2% as they now expect a significantly lower contribution to growth from the public sector. Frequent readers know that a fiscal impulse of approximately zero in 2014 is one of the reasons why we expect moderating domestic growth. Yet, the assessment of public sector demand is seemingly the only area where we are in agreement with the SECO. For them, accelerating private sector growth dynamics at home and abroad over the coming quarters should feed into lower unemployment next year. Our own labour market model suggests that unemployment will likely go the other direction. We observe that the impulses from low interest rates and demographics on domestic private demand are slowly running out their course. In addition to that, our below the consensus view for most other regions covered in this paper may explain a comparably moderate forecast for future export growth.

Inflation

Swiss Life Asset Managers	Consensus
2014: 0.1%	2014: 0.3%
2015: 0.6%	2015: 0.9%

We lower our forecast for annual average inflation this year yet again to a mere 0.1%. When it comes to forecasting inflation we find ourselves in the same camp with most other houses: In response to a surprisingly weak inflation print for February, the consensus estimates for 2014 and 2015 were revised lower as well last month. The same can be said about the latest forecast revisions by the Swiss National Bank and the SECO.

Released and approved by the Economics Department, Swiss Life Asset Management AG, Zurich

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