Global Economic Scenario
December 2016

SwissLife
Asset Managers

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

	GDP 2016		GDP 2017		CPI 2016		CPI 2017	
	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus	Swiss Life AM	Consensus
USA	1.5% (1.4%)	1.5%	2.2% (2.0%)	2.2%	1.3%	1.2%	2.4% (2.3%)	2.3%
Euro Area	1.6%	1.6%	1.2% (1.1%)	1.3%	0.2%	0.2%	1.5%	1.3%
Japan	0.8% (0.6%)	0.6%	1.0% (0.9%)	0.9%	-0.2% (-0.3%)	-0.2%	0.5% (0.1%)	0.4%
UK	2.0% (1.9%)	2.0% (1.9%)	1.2% (0.6%)	1.1% (0.9%)	0.6% (0.7%)	0.7%	2.3% (2.5%)	2.5% (2.3%)
Switzerland	1.5% (1.4%)	1.5%	1.1% (0.9%)	1.5% (1.4%)	-0.4%	-0.4%	0.2% (0.4%)	0.3%

Source for Consensus Estimates: Consensus Economics Inc. London, 7 November 2016

Consensus Economics
Forecast Accuracy
Award Winner
2015 Switzerland

Consensus Economics, one of the world's leading economic survey organisation, has announced the recipients of its 2015 Forecast Accuracy Award (FAA) in June 2016. Swiss Life Asset Managers' economic research team has won this year's Forecast Accuracy Award for Switzerland. Click here for more information.

USA – Trumponomics sparks exuberance

GDP Growth

Swiss Life Asset Managers	*Consensus*
2017: 2.2%	*2017: 2.2%*
2018: 2.3%	*2018: n.a.*

Voters shocked the world for a second time this year and highlighted widespread frustration among certain social layers. Given still unclear policy positions and the political as well as legal enforceability of some of Trump's campaign promises, we abstain at this stage from substantially changing our growth and inflation outlook. In any case, if new policies on fiscal spending, taxes and tariffs pass through Congress, they will not unfold their effect much before 2018. One of the main themes during this election campaign for both candidates was the increase of infrastructure spending and this is the very theme that the President-Elect mentioned in his acceptance speech. Therefore, a certain amount of fiscal stimulus is given, even though the Republican Congress, which is usually very deficit-averse, will have a say in this as well. On top of this, some form of tax reduction for companies as well as individuals may be in the cards, aggravating the tendency for a wider public deficit further. The financing of these give-aways is less than clear. Since forecasting future policy-making still borders speculation at this stage, we will blank the election outcome for now and turn to macroeconomic realities instead. The US economy grew by almost 3% in the third quarter, well above potential, driven mainly by inventories and sturdy export growth. Thus, after a weak first half of 2016, US growth momentum accelerated notably. The quarterly growth rate in the third quarter was higher than we had expected and caused us to revise GDP growth for the current as well as the next year to the upside. At the same time retail sales in October were strong across product groups which lays the basis for a respectable contribution of personal consumption in the last quarter of this year. Our own assumption for quarterly growth in the fourth quarter stands at 2.0% which is a slight slowdown from the previous quarter's pace. It remains to be seen if exports will be able to substantially contribute to overall GDP growth as they did in the third quarter, where 1.2 percentage points of the 2.9% GDP growth actually came from exports. Turning to the longer term, we now publish our forecast for 2018. With a rate of 2.3% annual average growth, we remain optimistic that the business cycle remains intact and that fiscal spending will leave positive traces in 2018.

Inflation

Swiss Life Asset Managers	*Consensus*
2017: 2.4%	*2017: 2.3%*
2018: 2.1%	*2018: n.a.*

Headline inflation follows the script which we had drafted since quite a while, subject to the well-known base effect. The election of Trump made a difference insofar as finally inflation expectations have started to climb as well. The 10-year breakeven rate reached almost 2% in the meantime which corresponds approximately to the long-term average since the year 2000. As the economy approaches capacity limits, headline inflation will surpass 2% in January 2017 and remain above 2% for the remainder of the year. Another Fed hike is just around the corner.

Euro Area – Renzi referendum next hurdle to take

GDP Growth

Swiss Life Asset Managers	*Consensus*
2017: 1.2%	*2017: 1.1%*
2018: 1.2%	*2018: n.a.*

The Euro Area economy grew at a pace of 0.3% in the third quarter which confirmed our own forecast. As was the case after the UK's Brexit vote, the election of a populist president in the US hardly left any traces in sentiment and survey data in general. The manufacturing PMI had reached respectable levels in autumn already and continued to climb higher in the preliminary reading for November. Based on the current PMI level of 53.7 for the currency region as a whole, our model suggests a quarterly GDP growth rate of 0.5% in the current quarter. We prefer, however, to position ourselves more cautiously and forecast a quarterly growth rate of 0.4%, which still is clearly above the potential rate which the OECD attributes to the region. While the manufacturing purchasing managers index (PMI) is the preferred index to gauge the business cycle, the services PMI reveals the dynamics of domestic activity rather. The services PMI for the region reached a level of 54.1, underlining continued consumption growth, also in the peripheral countries. Risks are on the political side. Mr. Renzi's constitutional referendum on 4 December potentially revives break-up fears again should he fail to gather a majority behind him. On a more positive note, Mr. Fillon's candidature for the presidential election in France coming May equally reveals the people's longing for change, but also produces a candidate with commitment to serious economic reforms. His programme of liberalising the labour market, raising the retirement age and slimming down the public sector could be exactly what France needs to catch up with neighbouring countries.

Inflation

Swiss Life Asset Managers	*Consensus*
2017: 1.5%	*2017: 1.3%*
2018: 1.6%	*2018: n.a.*

The headline inflation rate is bound to reach a level of 1.3% in January 2017, which marks the highest level since summer 2013. However, the labour market needs further healing and the outgap remains larger than in the Anglo-Saxon economies. The ECB will be in no hurry to normalise monetary policy.

Japan – Abenomics a first victim of Trumponomics?

GDP Growth

Swiss Life Asset Managers	*Consensus*
2017: 1.0%	*2017: 0.9%*
2018: 0.8%	*2018: n.a.*

Economic conditions in Japan improved until recently with third quarter GDP growth beating expectations markedly. The manufacturing PMI remained above the critical 50 points watershed for the third straight month. In October, the services sector PMI moved above 50 points for the first time since July. The improvement in sentiment was broad-based as show the growing optimism among small and medium sized firms and sturdy data from the construction sector. Real cash earnings rose almost 1% in the year until September, making us somewhat more constructive on final domestic demand. Financial services recover too with bank lending picking up since mid-year. Japan's economy is one of the many boats which are lifted by the rising tide of the first global synchronous cyclical upswing since 2010. One could argue that fiscal and monetary policy measures introduced by prime minister Abe and the Bank of Japan over the last four years are finally working. And yet, a new threat to Japan's economic model appears on the horizon: Donald Trump's withdrawal from the Trans-Pacific-Partnership (TPP) trade agreement project thwarts Abe's plans to deregulate Japan's economy with the help of foreign pressure. Japan's export industries are also a likely victim of protecionist measures potentially introduced by the new US government: Not only are 20% of Japan's exports going to the US, a termination of NAFTA would strongly impact Japanese car manufacturers operating in Canada and Mexico for delivery to the US market.

Inflation

Swiss Life Asset Managers	*Consensus*
2017: 0.5%	*2017: 0.4%*
2018: 0.1%	*2018: n.a.*

Headline annual inflation turned positive in October for the first time since February this year. Apart from the base effect from energy, prices for fresh food rose sharply and were more than 11% above the levels of October last year. This triggered a marked upward revision in our forecast. We now expect annual inflation to stay above the zero line for each month in 2017.

UK – Disproved by animal spirits

GDP Growth

Swiss Life Asset Managers	Consensus
2017: 1.2%	2017: 1.1%
2018: 0.8%	2018: n.a.

The UK economy continues to defy uncertainties about the consequences of the decision to leave the EU. The most remarkable detail in the third quarter GDP data is the strong contribution from fixed capital formation in the corporate sector. Reluctant private sector investment behaviour was generally expected as an immediate result of Brexit. Yet, instead of contracting through the third quarter, business investments rose by more than 1%. Apparently, British firms are willing to invest in order to benefit from the windfall gain in competitiveness following the fall of the Pound Sterling's external value. On a trade weighted base, the Sterling is still 12% cheaper than on June 23. With this tailwind from foreign exchange markets, UK exporters benefit disproportionately from the synchronous global economic recovery under way. Our simple econometric model based on the PMI for the manufacturing sector suggests that GDP growth accelerated to 0.6% in the final quarter 2016. If confirmed by the PMI data for November and December, our more prudent estimate of just 0.3% quarterly growth may yet again prove overly cautious. The strong monthly gain in retail sales through the month of October suggests that surprisingly firm private domestic demand adds to upside risks to our current forecast.

Inflation

Swiss Life Asset Managers	Consensus
2017: 2.3%	2017: 2.5%
2018: 2.2%	2018: n.a.

Sterling weakness and higher energy prices amplify the trend to fast rising input prices on the producer level. Producers' input prices rose by 12.2% this year until October. Things look different at the consumer level, where annual inflation remains stuck at 0.9%. Yet, we expect more pass-through in coming months. In our current base case projections, consumer price inflation should rise rapidly to 2.6% until the last quarter of 2017.

Switzerland – Held back by subdued domestic demand

GDP Growth

Swiss Life Asset Managers	Consensus
2017: 1.1%	2017: 1.5%
2018: 1.5%	2018: n.a.

The first official estimate for Switzerland's gross domestic product (GDP) in the third quarter will be published on 2 December. We expect a 0.2% quarterly growth rate for real GDP, which is slightly below the median estimate of a sample of 26 economists polled by Bloomberg. In our view, domestic dynamics remain soft with subdued growth of components such as personal consumption and business equipment. On a slightly positive note, construction activity seems to have recovered in the third quarter after contracting through the second quarter. Yet, the main driver of domestic demand over the past six quarters was government consumption. It is very unlikely that we see such a strong contribution to growth from this component again in the second half of 2016. Net trade, which was another positive contributor to growth in the second quarter requires a closer look at the details: Stabilising energy prices and exchange rates suggest that the value of imports is no longer contracting which limits the positive impact of net trade to overall GDP growth. At the same time, export data reveal that the currency shock from last year's SNB decision to abandon its minimum exchange rate policy is still not overcome. In trade weighted terms, the Swiss Franc has appreciated for the seventh straight year. Consequently, goods exports continue to fall in all major categories with the only exception being pharmaceuticals and chemical components.

Inflation

Swiss Life Asset Managers	Consensus
2017: 0.2%	2017: 0.3%
2018: 0.4%	2018: n.a.

Lower air traffic fees and falling domestic hotel prices are the predominat reason why Switzerland's consumer price index rose more slowly than we expected over the past months. This fact and slightly lower energy prices through the first half of November triggered a downward revision in our forecast for inflation both in 2016 and 2017.