GLOBAL ECONOMIC RESEARCH

GLOBAL MACRO OUTLOOK

OCTOBER 2017

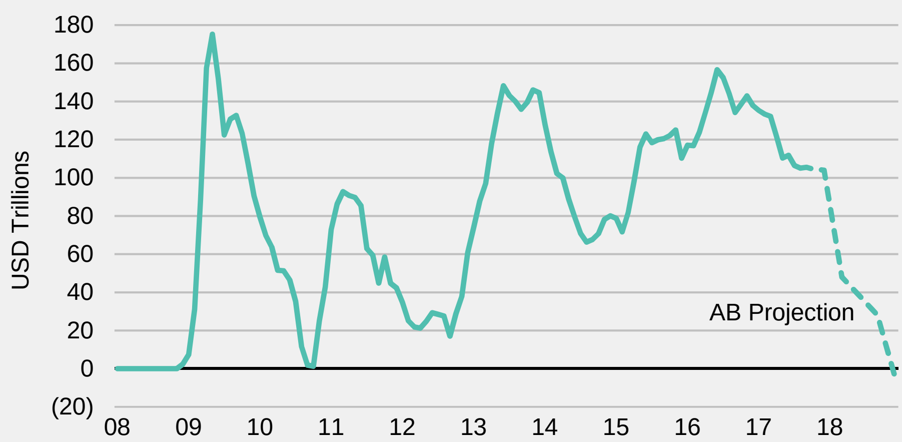
KEY FORECAST TRENDS

- With the recovery gaining strength and breadth and inflation still moderate, the cyclical backdrop is more favorable than it has been at any point since before the financial crisis.
- Despite a better-than-expected US labor market report, the failure of wage growth to respond to falling unemployment remains at the heart of the global policy debate.
- Yet this has not dented central banks' confidence in the Phillips Curve or that inflation will ultimately return to target if growth remains on track.
- So far, only the Fed and the Bank of Canada have started withdrawing monetary stimulus. In coming weeks, though, we expect the ECB and Bank of England to take their first tentative steps in the same direction.
- Only the Bank of Japan looks set to stay the course. But its efforts alone won't be sufficient to prevent global central-bank balance sheet policy from turning less bond-friendly over the next year.
- This also points to a more challenging environment for risk assets. But as long as growth remains strong, inflation low and central banks cautious, a broad-based sell-off remains unlikely.

CONTENTS

Central Bank Balance-Sheet Policy Now Center Stage

G3* Monthly Central Bank Asset Purchases

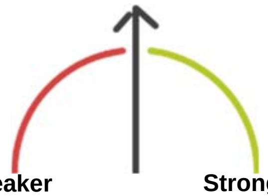


- The Fed has already started the process of balance-sheet normalization and the ECB is likely to announce a tapering of its asset purchase program at its next Council meeting.
- The Bank of Japan is set to stay the course. But its efforts alone won't be sufficient to prevent global central bank balance-sheet policy from turning less bond friendly.

As of August 31, 2017. *G3 is the US, the euro area and Japan. Three-month rolling average.
Source: Haver Analytics and AB

GLOBAL FORECASTS

Economic Growth



+ Solid growth is likely to continue in 2018, much as it has in 2017
+ Recent data suggest that risks are tilted in a more positive direction, but the probability of a significant fiscal boost has fallen

Key Risks

+ Politics and protectionism
+ Too much or too little fiscal stimulus
+ China credit crunch/hard landing

Inflation

+ The energy-related rise in headline inflation has run its course
+ Inflation expectations have moved to center stage. Labor market and wage outcomes are now key benchmarks

Key Risks

+ Uncertain labor market slack
+ Can we trust the Phillips curve?

Monetary Policy

+ Gradual Fed tightening (Fed funds rate 1.88% by end of 2018)
+ ECB to end bond purchases next year
+ BoJ to stay the course; focus on yield level, not volume of purchases

Key Risks

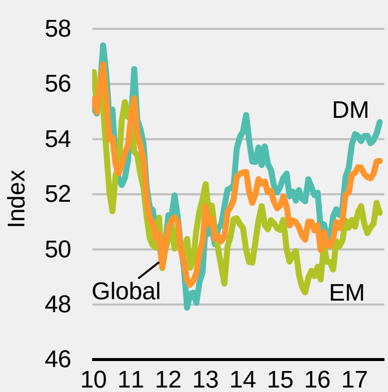
+ Shift in central bank reaction functions
+ More aggressive tightening
+ PBOC: growth vs. deleveraging

OUTLOOK

+ We expect global growth of 3.0% in 2018, the same as this year. Slightly softer growth in developed economies (2.0% versus 2.2%) is offset by a modest improvement in emerging economies (4.6% versus 4.4%).
+ We are more optimistic than the consensus on 2018 growth in the euro area (2.0% versus 1.8% consensus) and Japan (1.6% versus 1.1% consensus), but more cautious on growth in the US (2.0% versus 2.3% consensus) and China (6.0% versus 6.4% consensus).
+ We're watching the interaction between strong survey data and softer official data and the extent to which China continues to prioritize short-term growth over structural reforms.
+ We expect global inflation to remain subdued, at 2.4% this year and 2.5% in 2018. Central banks are likely to withdraw monetary stimulus very gradually.

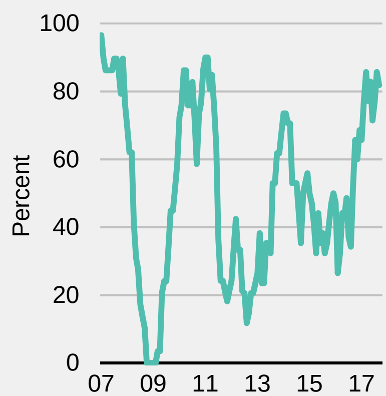
Global Manufacturing Trends: Recovery Gains Strength and Deepens

Manufacturing PMIs



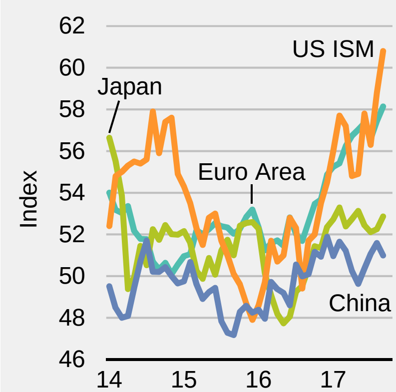
Through October 5, 2017
Source: Haver Analytics and IHS Markit

Manufacturing PMI: Diffusion Index



Through October 5, 2017
Source: Haver Analytics and IHS Markit

Manufacturing PMIs



Through October 5, 2017
Source: Haver Analytics and IHS Markit

GLOBAL MARKET OUTLOOK: YIELD CURVES

GLOBAL YIELDS

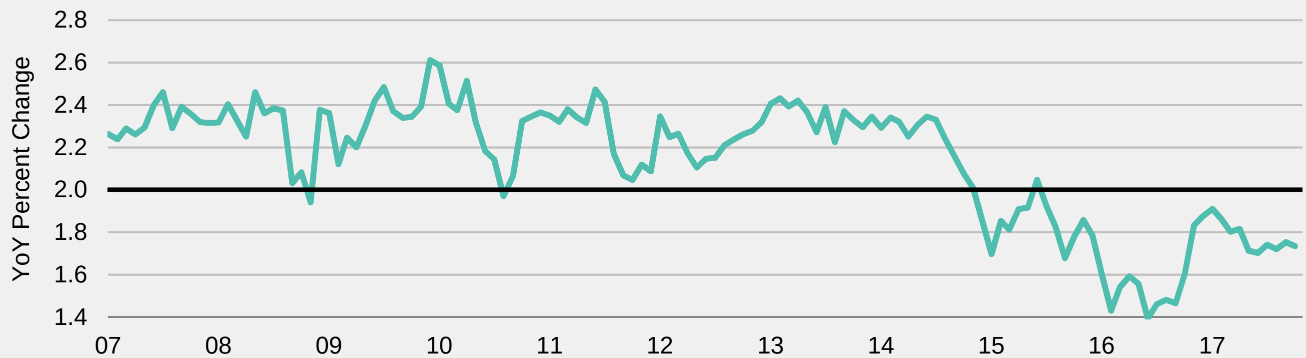
+ **Global**—Core rates likely to trend higher; central bank balance-sheet policy a key factor
+ **US**—US growth is picking up, which should push US rates higher, reaching 3.25% in 2018
+ **Euro Area**—ECB tapering to push Bund yields higher; political risks have receded for now
+ **Japan**—QQE-YCC policy to anchor 10-year yields close to zero, but commitment to quantity target to become fuzzier
+ **UK**—Bank of England (BOE) now looks to set for early policy tightening

Global Rates: AB and Consensus Year-End Forecasts (%)

	AB		Consensus	
	2017	**2018**	**2017**	**2018**
US	2.75	3.25	2.39	2.93
Euro Area	0.75	1.25	0.61	1.04
UK	1.75	2.00	1.29	1.61
Japan	0.05	0.05	0.04	0.09

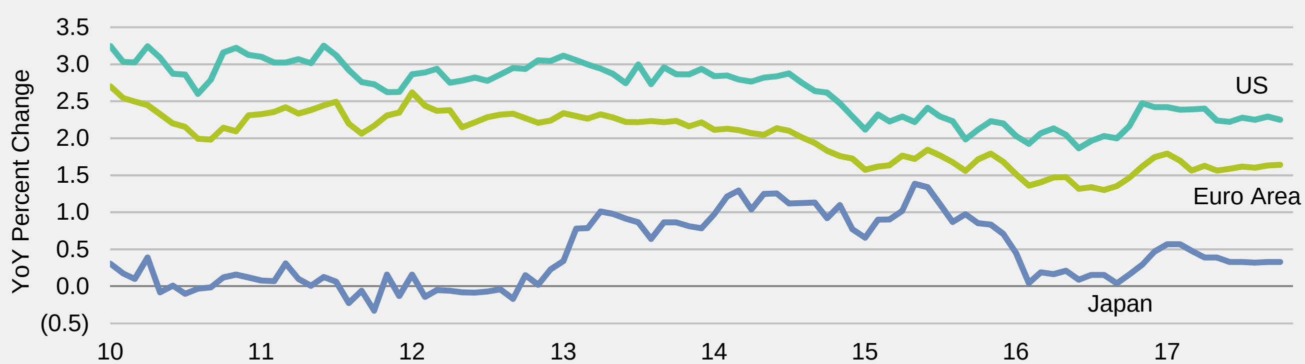
As of October 5, 2017
Source: Bloomberg and AB

G3* Medium-Term Inflation Expectations†



As of October 5, 2017
*US, euro area and Japan. †Five-year/five-year forward inflation-linked swaps
Source: Bloomberg and AB

Medium-Term Inflation Expectations*



As of October 5, 2017
*Five-year/five-year forward inflation-linked swaps
Source: Bloomberg and AB

GLOBAL MARKET OUTLOOK: CURRENCIES

FX FORECASTS

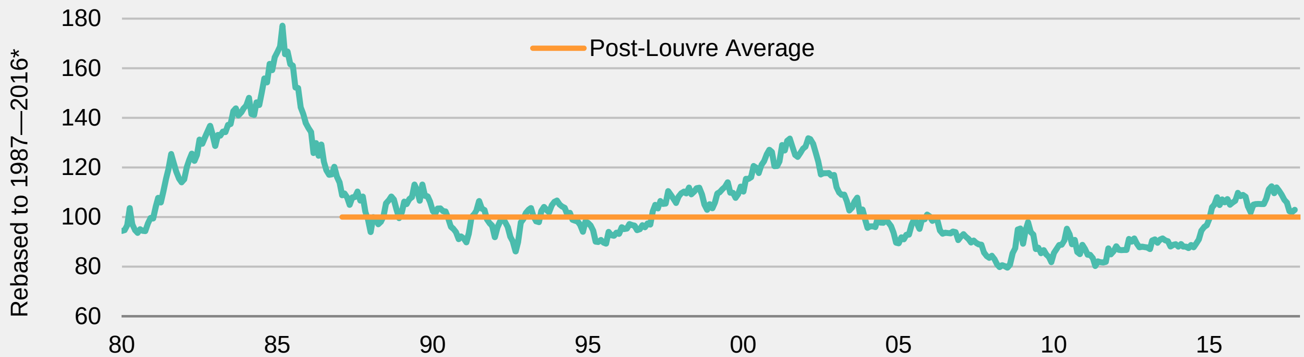
- **USD**—Fed balance-sheet shrinkage/higher rates to provide support for USD
- **JPY**—Expect modest JPY weakness as BoJ lags in policy-normalization process
- **EUR**—EUR has benefited from ECB taper talk and reduced political risk, but further gains look difficult from here
- **GBP**—Early BOE tightening provide near-term support
- **Dollar Bloc**—AUD still vulnerable to a housing correction, though now expected to play out over the longer horizon

Global FX: AB and Consensus Year-End Forecasts

	AB		Consensus	
	2017	2018	2017	2018
EUR/USD	1.15	1.15	1.18	1.21
USD/JPY	115	125	112	112
EUR/GBP	0.88	0.92	0.90	0.92
AUD/USD	0.76	0.72	0.79	0.80

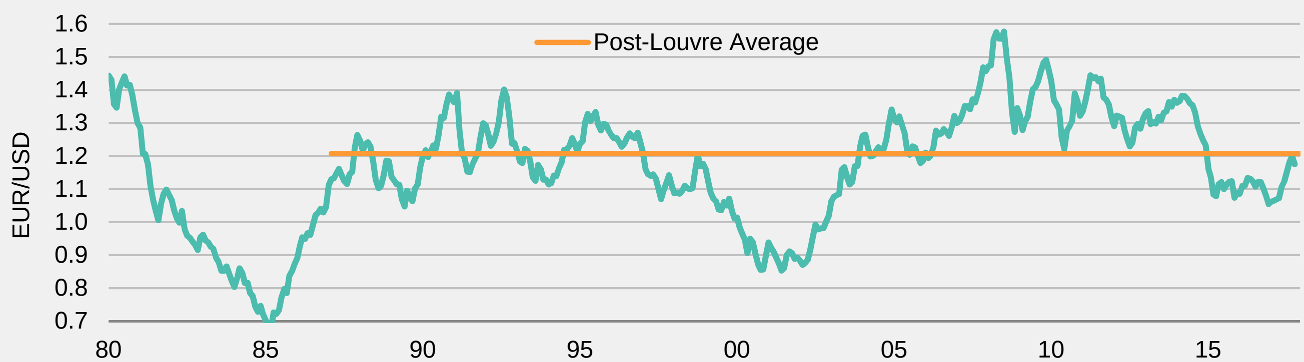
As of October 5, 2017
Source: Bloomberg and AB

USD Nominal Effective Exchange-Rate Index



Through October 5, 2017 *Average = 100
Source: Bloomberg and AB

USD per Euro



Through October 5, 2017
Source: Bloomberg and AB

GLOBAL MARKET OUTLOOK: CENTRAL BANK WATCH

Core/Developed Markets

	Policy Direction	Latest (%)	+6 Mo. (%)	+12 Mo. (%)	Comments/Unconventional Policy
US	⇧	1.13	1.38	1.88	The Fed's balance sheet is shrinking, and we expect the program to continue as scheduled even if there is a new Fed chair
Euro Area	⇔	0.00	0.00	0.00	ECB to announce tapering in the second half of 2017 and to run down the program during 2018
Japan	⇔	(0.10)	(0.10)	(0.10)	QQE-YCC policy is in play for the foreseeable future. BoJ to lag ECB and Fed in normalization process
China	⇧	2.80	2.90	3.10	Robust loan growth will offset tightening measures on shadow credits. Overtightening risk remains low
Canada	⇧	1.00	1.25	1.75	The closing output gap and strength of the labor market will likely support multiple BOC hikes
Australia	⇩	1.50	1.50	1.00	Rate cut increasingly unlikely, particularly given mounting financial stability concerns. Equally, RBA in no hurry to hike
NZ	⇔	1.75	1.75	1.75	Macroprudential policies have slowed Auckland housing. Growth backdrop sound, but inflation undershooting on hold
UK	⇔	0.25	0.50	0.75	Unless growth slips further, some BOE tightening now looks likely
Sweden	⇔	(0.50)	(0.50)	(0.40)	Next move likely to be up, though not until 2018
Norway	⇔	0.50	0.50	0.50	

KEY DEVELOPED-MARKET THEMES

+ Many developed-market (DM) central banks have grown more hawkish. This reflects a greater tolerance for low inflation and a less pressing need to drive it quickly back to target, provided that growth remains on track.
+ The main change this month is to the UK, where we now expect the BOE to raise rates by 25 basis points in November and again in the first half of next year (we had expected rates to be on hold).

Emerging Markets

	Policy Direction	Latest (%)	+6 Mo. (%)	+12 Mo. (%)	Comments/Unconventional Policy
India	⇔	6.00	6.00	6.00	Likely fiscal expansion will provide room for RBI to stay neutral after two 25-basis-point rate cuts this year
Indonesia	⇔	4.25	4.25	4.25	BI's policy easing should have come to an end with two back-to-back rate cuts over the last two meetings
S. Korea	⇔	1.25	1.25	1.25	BOK to stay put; growth-inflation mix not sufficient to lead to rate cut
Brazil	⇩	8.25	7.00	7.00	Aggressive easing priced in since 4Q:2016
Mexico	⇔	7.00	7.00	6.50	Tightening cycle over; easing to start in 3Q:2018
Chile	⇔	2.50	2.50	2.50	Easing cycle over; soft growth gave room for central bank to ease
Colombia	⇩	5.25	5.00	5.00	Inflation to decline gradually; easing cycle started in December 2016
Russia	⇩	10.00	8.00	7.50	Undershooting of inflation target opens door for bigger cuts
Turkey	⇔	8.00	8.00	8.00	The CBRT will use only the upper end of the rate corridor to manage short-term lira liquidity
S. Africa	⇩	6.75	6.50	6.25	
Hungary	⇔	0.90	0.90	0.90	
Poland	⇔	1.50	1.50	1.50	

KEY EMERGING-MARKET THEMES

+ In contrast to the major DM central banks, most emerging-market (EM) countries are expected to either loosen monetary policy or keep it on hold in coming months.

US

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
US	2.3	2.0	2.0	2.1	1.38	1.88	2.75	3.25

OUTLOOK

+ The US economy has been accelerating in the second half of the year. While the impact of Hurricanes Harvey, Irma and Maria will likely be negative for GDP in the third quarter, we expect rebuilding activity in the fourth quarter of this year and the first quarter of next year to more than offset the negative near-term impact on the nationwide economy.
+ Financial conditions have eased even as the Federal Open Market Committee (FOMC) has raised rates and started to shrink its balance sheet. That easing of financial conditions underpins upward revisions to our growth forecast for 2017 (2.25%) and 2018 (2.0%); should conditions stay easy, there are upside risks to our current forecasts as well.
+ We have no insight into the probability of fiscal stimulus, but should large tax cuts and/or increased government spending occur, both growth and inflation forecasts would likely rise.

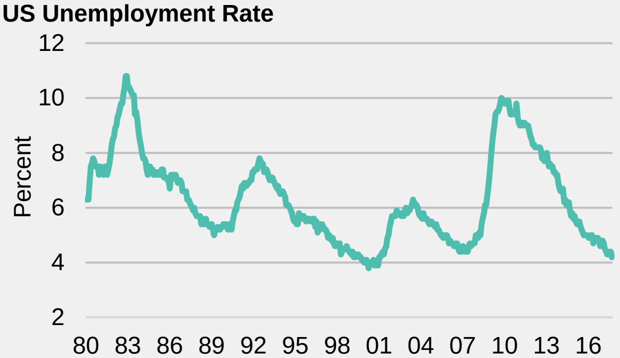
RISK FACTORS

+ The FOMC has begun the process of reducing its balance sheet. Our base case is that the reduction will not disrupt financial markets or the economy, but there remains some risk around the program, which has not been used previously. Should reduced central bank purchases push interest rates up more rapidly than we expect, it could slow the economy.
+ Much of our optimism about growth in the next few quarters stems from persistently easy financial conditions. We expect conditions to tighten gradually—driven largely by higher interest rates—into 2018. Should the pace of tightening be slower, growth could be more rapid. But should rates rise more rapidly, that would cause the economy to slow more than we are currently forecasting.
+ Political and policy uncertainty remains elevated, with Congress and the Trump administration confronting a variety of issues, from budget and tax policy to the debt ceiling, over the next few months. Markets have been able largely to ignore the political noise this year, but action on several fronts is now required to keep the government functioning. How negotiations proceed in Washington is likely to be more impactful in the next few quarters than it was in the last few.

OVERVIEW

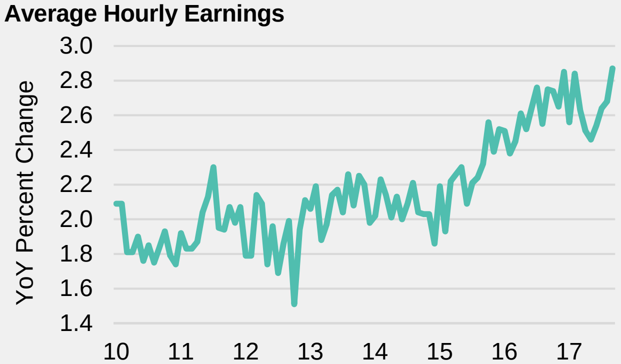
The US economy is performing remarkably well as we enter the fourth quarter, with growth clearly above trend. That is pushing unemployment down and wages up. It hasn't yet raised inflation, but we expect it will in the coming quarters. We also expect the FOMC to raise rates more aggressively than most market participants but not so aggressively as to trigger a negative economic outcome. A benign global economic picture bolsters the optimistic outlook, and we think the risks are largely political. Even so, we view the economy as structurally solid and think it would take a major shock to change the outlook materially. Absent that kind of a shock, we expect growth to remain above trend the next few quarters, supporting a gradual tightening of monetary policy even with inflation below target.

US Unemployment Rate



Through September 15, 2017
Source: Thomson Reuters Datastream

Average Hourly Earnings



Through September 15, 2017
Source: Thomson Reuters Datastream

Euro Area

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Euro Area	2.2	2.0	1.6	1.4	0.0	0.0	0.75	1.25	1.15	1.15

OUTLOOK

+ We expect the euro area to grow by 2.0% next year, slightly below this year's expected growth rate of 2.2% but still substantially higher than most estimates of the economy's potential growth rate.
+ With underlying inflation likely to rise slowly and oil prices subdued, we expect headline inflation to average 1.4% next year after 1.6% in 2017.
+ The ECB is expected to announce a tapering of its asset purchase program in the second half of 2017, probably at its October council meeting. This should put further upward pressure on Bund yields.

RISK FACTORS

+ Risks to the growth outlook appear evenly balanced and may even be to the upside over the near term.
+ The recent rise in the euro is unlikely to pose a material risk to the recovery. But a further rise from current levels would make the ECB less confident in its ability to drive inflation back to target and more cautious about withdrawing monetary stimulus.

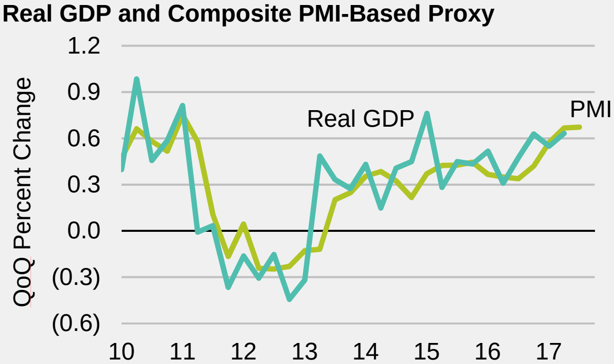
OVERVIEW

Recent data support our view that 2017 will be the best year for euro-area growth since 2007. Real GDP rose by 0.6% in the second quarter after a 0.5% gain in the first, pushing annual growth up to 2.3%. Moreover, the composite PMI rebounded to 56.7 in September from 55.7 in August, close to the cyclical peak seen earlier this year and consistent with a continuation of the second quarter's strong growth rate. Looking ahead, the euro's recent appreciation is likely to weigh on growth. But with momentum strong, monetary policy still highly accommodative and the global backdrop supportive, we do not anticipate a material slowdown.

Having surprised on the upside in recent months, core inflation eased back to 1.1% in September from 1.2% in August. Despite this setback, it does look as if core inflation has picked up in recent months and is now running a little above 1% rather than just below it, as was the case between the fourth quarter of 2013 and the first quarter of this year. And while this is still a bit short of target, it is likely to increase the ECB's confidence that inflation will eventually return to target.

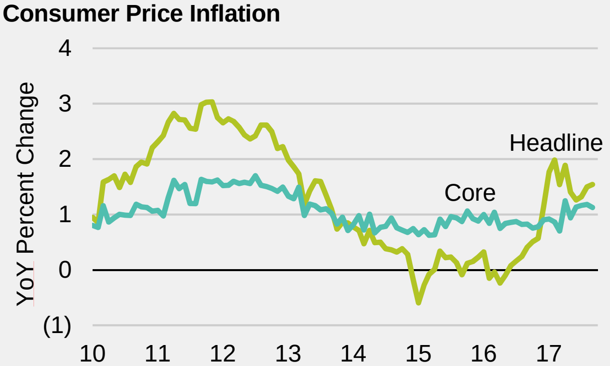
Against this backdrop, we expect the ECB to announce a winding down of its bond purchase program at its October Council meeting. The precise shape this will take is difficult to gauge at this stage. However, we expect the Governing Council to favor a flexible approach, which means it's unlikely to signal the end date in advance. With respect to the volume and duration of the program, we think a nine-month extension (until September 2018) at a much-reduced monthly purchase pace of €20 billion (from €60 billion) is the most likely scenario. This would be at the hawkish end of expectations, and if it materializes, we'd expect it to put upward pressure on Bund yields.

Real GDP and Composite PMI-Based Proxy



Through September 30, 2017
Source: Haver Analytics and IHS Markit

Consumer Price Inflation



Through September 30, 2017
Source: Haver Analytics and IHS Markit

Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Japan	1.8	1.6	0.4	0.8	(0.10)	(0.10)	0.05	0.05	115	125

OUTLOOK

+ We still expect fiscal and monetary stimulus, along with improved private demand and a tightening labor market, to produce above-trend growth over the next couple of years. Not surprisingly, the labor market continues to tighten.
+ Despite solid activity and tight capacity, inflation has remained low. The BoJ's preferred core inflation measure (CPI ex fresh food and energy) is still near zero. Wage outcomes remain well below levels that would be consistent with the central bank's 2% inflation target.
+ In this environment, we find it difficult to see the BoJ starting the policy normalization process. Instead, the BoJ will probably maintain its QQE-YCC program designed to cap 10-year yields at zero well into 2018, and probably beyond.

RISK FACTORS

+ Any disruption of global trade caused by the Trump administration's policies is an important risk. Japan's current account surplus (4% of GDP) leaves the country vulnerable to US criticism on trade issues.
+ Political risk is another key factor. If Prime Minister Shinzo Abe were to resign, then the "Abenomics" policy architecture would be in doubt, leading to questions about whether the BoJ's QQE-YCC program could be sustained.

OVERVIEW

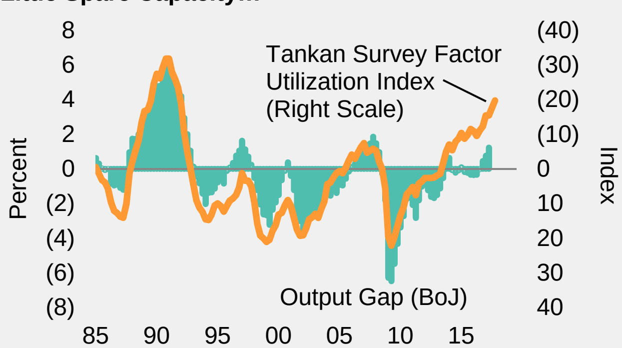
Japan is an exception to the "getting back to normal" narrative taking shape in other developed-market economies. The success of the BoJ's Yield Curve Control program at anchoring yields at low levels – even while the pace of purchases has slowed – removes any "technical" need to adjust the policy framework.

The macroeconomic data haven't changed much. Growth has been strong enough to drive the unemployment rate lower and perceptions of factor utilization higher. The BoJ now estimates that the output gap has closed and moved into positive territory. But the tightness in the economy has yet to produce higher inflation.

The BoJ remains confident that prices will eventually start to rise more quickly and that the increased job force participation by women and the elderly and the pickup in capex will soon run their course. As a result, policymakers seem content to stick with the current program, no matter what's happening with the Fed and the ECB. The turnover on the BoJ board—a reflationist has replaced some QQE skeptics—only reinforces this outlook.

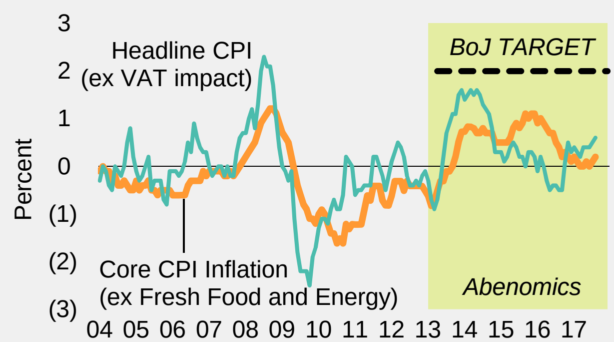
The key risks are political, namely whether Prime Minister Abe will reappoint another dove to replace BoJ Governor Haruhiko Kuroda when his term ends in April. The rise of Tokyo Governor Yuriko Koike's Party of Hope adds some spice to that risk, as does Abe's call for an election later this month. We expect the election to deliver a solid (albeit reduced) LDP majority. That would extend the status quo for the BoJ, anchor yields and lead to further softening in the yen. But the risks are clearly asymmetric. If Abe is defeated (unlikely) or if his position is weakened substantially, then there will initially be a big reassessment of Abenomics, a stronger yen and a weaker Nikkei.

Little Spare Capacity…



Through October 5, 2017
Source: Thomson Reuters Datastream

…but Inflation Remains Stuck



Through October 5, 2017
Source: Thomson Reuters Datastream

China

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
China	6.7	6.0	1.6	2.3	2.90	3.10	3.70	3.60	6.55	6.50

OUTLOOK

- A clearer picture of economic policy should emerge after October's Party Congress. We expect the government to resume some reform measures in 2018.
- The government may moderate its pro-growth policy stance somewhat. Deeper state enterprise reform, excess capacity reduction and tougher environmental protection rules should emerge.
- Replenished FX reserves and greater confidence in RMB stability might provide room for the authorities to gradually relax capital controls and allow for more two-way flexibility in the exchange rate.

RISK FACTORS

- Tension with North Korea and the related threat to US–China trade are key risks.
- A credit bubble and a structural imbalance are medium-term risks if the government sticks with its pro-growth policies.

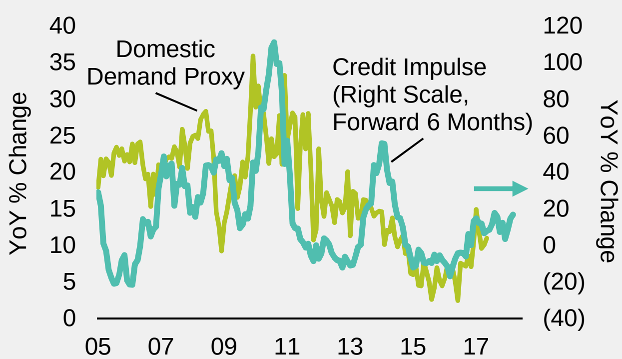
OVERVIEW

Economic data paint a picture of a strengthening Chinese economy, which has benefited from strong credit growth and government support for infrastructure investment. The housing market is running at two speeds, with transactions in top-tier major cities slowing while demand in lower-tier cities remains strong. We still expect housing investment to slow next year, which will put more pressure on the government to sustain strong infrastructure investment as the sole engine of growth.

The People's Bank of China (PBOC) selectively eased the reserve requirement ratio for banks, an attempt to earmark bank loans to the much-depressed small-and-medium-size-enterprise sector. In our view, this is a move to provide specific state guidance to support a weak growth area rather than a genuine monetary easing.

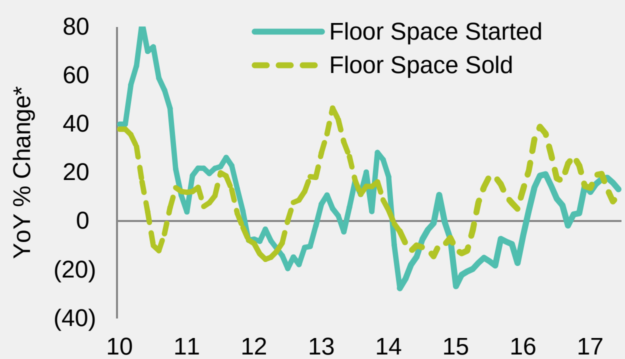
While we do not see major downside risk for growth next year, we still think that economic reform will resume somewhat after the political jockeying at this year's Party Congress ends. Recent signs suggest that the government will aim to deepen state-owned enterprise reform with an expanded public-private partnership program. We also think that, given the continuous resumption of FX reserves and greater confidence in the renminbi, the government may consider phasing out some of the more stringent capital control measures and allow more exchange-rate flexibility. We do not expect any major downside risk to the Chinese currency running into 2018.

Credit Impulse Remains Strong



Through August 30, 2017
Source: CEIC Data and AB

Slow Housing Transaction Will Moderate Investment



Through August 30, 2017 *3-month moving average
Source: CEIC Data and AB

Canada

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Canada	3.2	2.2	1.8	2.0	1.25	2.00	2.15	2.50	1.20	1.25

OUTLOOK

+ Economic activity is beginning to normalize, as expected. Real GDP was flat in July but is still growing 3.8% year over year. We see growth slowing through year-end.
+ The Bank of Canada (BoC) raised its policy rate by 25 basis points at its September meeting. We expect another 25-basis-point hike in December and more hikes next year, roughly on par with the US Federal Reserve.

RISK FACTORS

+ Home prices are still rising in key regional markets, but macroprudential measures in Toronto appear to be temporarily cooling the market. Along with historically high household debt levels, consumers will be vulnerable if there is a labor market shock or a rapid rise in interest rates.
+ Ontario is set to increase its minimum wage in January. Initially, the increase is likely to spark positive wage pressures and a welcome increase in inflation. But raising labor costs may eventually lead to higher unemployment.

OVERVIEW

Canadian growth is beginning to moderate, but that doesn't mean that the economy is headed for recession. Although the economy grew less than expected in July, it was still growing faster, year over year, than it was in the first quarter. Inflation is slowly increasing, but it's still well below the BoC's 2% target. However, the labor market is tightening and wage growth has started to accelerate. The average hourly wage rate for all employees increased 2.2% in September, the fastest growth since April 2016. Wages for temporary part-time employees—a good indicator of labor market tightness, as these are typically the most marginal workers—is growing at 4%. Expectations for higher inflation and continued fiscal stimulus provide a rationale for tighter monetary policy. The BoC may begin to be concerned about Canadian-dollar appreciation if its monetary policy continues to diverge from the Federal Reserve's. But policymakers seem to view current valuations as fair given the relative strength of the Canadian economy.

Australia/New Zealand

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Australia	2.2	2.3	1.8	1.7	1.50	1.50	3.00	3.45	0.76	0.73
New Zealand	2.6	2.7	1.8	1.6	1.75	1.75	3.25	3.50	0.73	0.72

AUSTRALIA

+ Economic data have improved, and so has the consensus outlook. Analysts have backed off forecasts of further Reserve Bank of Australia rate cuts and are now expecting hikes.
+ However, macroprudential tightening is having the desired effect, leading to slower credit growth and an orderly reduction in housing price growth, including in Sydney. Elevated household debt and weak income growth are putting stress on the household sector. Confidence is only average despite a solid labor market, and spending is patchy,
+ Even so, the hurdle to cutting rates again looks higher than it was a month or two ago. The RBA doesn't want lower rates to speed credit growth and amplify those macro stability risks.

NEW ZEALAND

+ Growth in New Zealand remains strong, but inflation is subdued. This partly reflects labor market dynamics, such as high levels of migration and higher participation. Both have acted as major shock absorbers and have limited wage growth to just 1.6%. It remains difficult to see the Reserve Bank of New Zealand changing course anytime soon.
+ The main change in risk assessment over the last month has been politics. At this writing, it was still unclear who would form the government. Both Nation and Labour-Greens could form a coalition with the populist New Zealand First Party. That could have implications for monetary policy, given a likely change in the RBNZ's mandate.

UK

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
UK	1.5	1.5	2.7	2.3	0.50	0.75	1.75	2.00	1.30	1.25

OUTLOOK

+ A sharp slowdown in real income growth coupled with Brexit-related uncertainty will likely lead to a period of softer economic growth in the UK at a time when the rest of Europe is experiencing a strong cyclical rebound.
+ Inflation is likely to run close to 3.0% in the second half of the year before moving back closer to target in 2018.
+ Although the economic outlook has not changed materially in recent weeks, the BOE has adopted a notably more hawkish tone and now looks set to raise interest rates by 25 basis points in November and by an additional 25 basis points in 2018.

RISK FACTORS

+ Despite an upward revision to the savings rate, UK household finances continue to look stretched. This makes the economy unusually vulnerable to higher interest rates.
+ Brexit continues to cloud the outlook. A lengthy transition phase is starting to look more likely but should not yet be taken for granted, especially with the British government looking far from stable.

Norway/Sweden

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Norway	2.1	2.5	2.0	1.7	0.50	0.75	1.70	2.00	8.00	8.00
Sweden	3.1	2.9	1.9	1.8	(0.50)	(0.40)	1.00	1.50	8.25	8.25

NORWAY OUTLOOK

+ The outlook is positive, with growth in the mainland economy expected at 2.1% this year and 2.5% in 2018. These forecasts, like our forecasts for the rest of Europe, are slightly more optimistic than consensus.
+ Inflation has dropped significantly to 0.9%, far below the 2.5% target. Weak wage growth, lower oil prices and subdued inflation in the rest of Europe are likely to keep it below target over the forecast horizon.
+ We expect Norges Bank to hold its policy rate at 0.5% at its October meeting and throughout most of 2018.

RISK FACTORS

+ The main risk factor in Norway is rising household debt (currently above 210% of income). The economy would also be vulnerable to a rapid decline in the oil price.

SWEDEN OUTLOOK

+ A downward revision to second-quarter growth has led us to reduce our 2017 forecast. However, with the economy still expected to expand by 3.1% this year and 2.9% in 2018, the outlook remains positive.
+ Inflation has been above target over the past few months, but this is partly due to special factors, and we expect it to fall back below target in 2018.
+ We expect the Riksbank to hold its repo rate at (0.5)% in the near term and maintain its asset purchase program until the end of the year, barring a significant deviation in the ECB's policy stance.

RISK FACTORS

+ High household debt and elevated house prices continue to represent a major risk to financial stability.

Asia ex Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Asia ex Japan	**5.9**	**5.6**	**1.9**	**2.5**	**3.08**	**3.23**	**3.95**	**3.92**	**—**	**—**
Hong Kong	3.7	3.0	1.7	2.5	2.00	2.25	1.90	1.90	7.76	7.76
India	6.1	6.7	2.5	3.2	6.00	6.00	6.60	6.50	66.00	65.00
Indonesia	5.2	5.7	3.9	3.5	4.25	4.25	6.50	6.60	13,300	13,100
South Korea	2.8	2.6	1.9	2.1	1.25	1.25	2.40	2.40	1,150	1,155
Thailand	3.7	3.5	0.4	1.3	1.50	1.50	2.40	2.60	33.00	32.50

OUTLOOK

+ We expect monetary policy to stay accommodative in Asia despite normalization in developed markets. Domestic demand has been mediocre, and inflation remains below policy targets. The Philippines is an exception and is likely to raise rates to slow an overheating economy.
+ Chinese policymakers are trying to balance between containing financial leverage while providing liquidity support to targeted sectors, including small and medium-size enterprises.
+ Asian currencies should remain stable, provided the USD does not strengthen abruptly. A stronger Chinese renminbi will also contribute to regional currency stability.

RISK FACTORS

+ Geopolitical risk from North Korea and threats of US trade sanctions are high on the list.
+ Another concern is Chinese policy risk and its impact on regional trade and investment flows.

OVERVIEW

Growth remains steady but uninspiring in the region. Recoveries in external and domestic demand have been mediocre, and inflation remains low. Apart from the Philippines, export growth remains strong across the region, but we are seeing greater divergence among countries and more signs that the momentum is peaking. South Korea's electronics sector continues to benefit from a huge global market share and expanding demand for memory devices and data center construction. But Taiwan saw disappointing export orders due to its reliance on Apple's supply chain, which has been interrupted by bottlenecks tied to the new generation of smartphones. For now, end demand remains uneven. A recent recovery in nominal exports contributed to the bottoming of regional growth, but the spillover to consumption and capital expenditure has been limited.

Monetary policy remains accommodative, but we expect the easing cycle to end and Asian central banks to stay on hold for an extended period. Fiscal policy remains restrained and neutral to growth, except for India, where there has been some talk about the return of expansionary fiscal policy.

We still think war in North Korea is a low probability, but we're concerned that the tensions could disrupt US–China trade, with wider implications for world and regional trade.

Latin America

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Latin America	**0.8**	**2.1**	**5.8**	**5.0**	**8.24**	**7.07**	**6.63**	**6.42**	**—**	**—**
Argentina	2.4	3.3	21.0	15.0	24.50	16.00	—	—	17.80	19.50
Brazil	0.6	2.4	3.1	3.9	7.00	7.00	9.50	9.00	3.20	3.50
Chile	1.3	2.7	3.2	3.0	2.50	3.00	4.30	4.65	630	660
Colombia	1.6	2.3	4.2	4.0	5.00	5.00	6.80	7.30	3,000	3,100
Mexico	2.1	2.3	5.7	3.5	7.00	6.00	7.05	7.30	18.20	18.90

OUTLOOK

- EM assets continued to attract inflows in September.
- Tighter DM monetary policy will be the most significant challenge for EM countries in the months ahead.
- Uncertainty regarding US trade policy has not subsided, while global geopolitical concerns are rising.

RISK FACTORS

- There are several: Asia–US geopolitical concerns, heightened US protectionism, uncertainty related to US tax policy, tighter-than-expected global monetary policies, and idiosyncratic political shocks in Argentina, Chile or Venezuela.

OVERVIEW

Evidence suggests a gradual recovery across the region, especially in Argentina, Brazil and Chile. On the other hand, Mexico may be decelerating at the margin. Inflation remains subdued or is declining in most countries (Venezuela is the exception). Despite the recovery, regional central banks are either on hold or in easing mode because output gaps largely remain in negative territory.

In Brazil, new charges were filed against President Michel Temer, just two months after he survived an impeachment attempt. The consensus among local political analysts is that Temer will nonetheless complete his term in office. Meanwhile, the government is making progress with reforms, including changes to electoral rules, labor market deregulation and the establishment of market determination of interest rates charged by the Brazilian Development Bank. Other micro reforms and changes to tax policy are being considered. But the government has not yet been able to change to the social security system, which it must do to ensure medium-term fiscal sustainability. Inflation has fallen below the bottom of the central bank’s target range but may have reached a bottom. The central bank has hinted that it will continue to ease policy, although less aggressively.

In Argentina, recent polls suggest that the ruling Cambiemos coalition is set to obtain a victory in the October 22 legislative election. The party stands to benefit from polarization between the government and supporters of former President Cristina Kirchner. Cambiemos’ victory in the Province of Corrientes on October 8 bodes well for its chances in the nationwide election. A strong performance for the party could help unlock private investment, which has been modest so far due to uncertainty about the election outcome. In the meantime, the green shoots of recovery in economic activity are becoming evident. But high inflation has prevented the central bank from easing monetary policy.

In Mexico, political volatility is rising. The center-right National Action Party (PAN) has split, a development that could have implications for the outcome of next year’s presidential election. The knee-jerk market reaction to the PAN split was negative, as some interpret the development as benefiting leftist candidate Andres López Obrador. But that’s far from clear at this point, since the ruling PRI may end up profiting the most from a divided PAN. Meanwhile, inflation has started to decline, but Banco de Mexico is not expected to ease monetary policy until well into 2018.

Eastern Europe, Middle East and Africa (EEMEA)

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
EEMEA	**2.4**	**2.6**	**6.3**	**5.8**	**6.66**	**6.16**	**7.77**	**8.15**	**—**	**—**
Hungary	3.6	3.3	2.6	2.7	0.90	0.90	2.85	3.50	315	317
Poland	4.0	3.4	2.0	2.2	1.50	1.75	3.55	4.00	4.30	4.22
Russia	1.7	1.7	4.2	5.2	8.00	7.00	7.60	8.00	58.50	59.00
South Africa	0.5	1.0	5.4	5.3	6.75	6.25	9.00	9.20	13.70	14.10
Turkey	5.2	3.5	9.6	8.0	8.00	8.00	10.70	11.10	3.65	4.00

OUTLOOK

+ Real GDP growth should improve over the rest of this year and in 2018, thanks to strong activity in Central and Eastern Europe (CEE) and a modest recovery in Russia. In South Africa, expect weak growth and increased downside risk tied to political uncertainty.
+ Most CEE economies are experiencing a rebound in headline CPI, while Turkish inflation has peaked but will remain above 10% for most of 2017. Disinflation should persist in Russia and South Africa.
+ Despite the CPI rebound, most CEE central banks will not tighten monetary policy in the near term. Russia and South Africa have scope to cut interest rates in 2017 and 2018, while Turkey will keep domestic liquidity conditions tight.
+ Political risks still loom large in a few EEMEA countries, especially Turkey and South Africa. Saudi-led sanctions against Qatar pose a threat to regional unity, but a mediated settlement is still likely.

RISK FACTORS

+ Balance-sheet normalization at DM central banks and the potential for higher core yields are risks for current account deficit countries such as Turkey and South Africa.

OVERVIEW

Geopolitical risks—especially in the Middle East—have taken center stage over the past month and will likely remain a focus within the region. First, the Kurdistan Regional Government (KRG) held its disputed independence referendum on September 25, with official results suggesting that 92% of the electorate supported the motion (turnout stood at 75%–80%). The risk that the KRG will unilaterally declare independence is low for a number of reasons: (1) on the ground, no logistical preparations have been made for succession from Iraq; (2) almost no major government supports independence, including the US, a key sponsor of the Kurds for decades; and, importantly (3), the independence vote is in part a tool to garner popular support for KRG President Barzani ahead of his region's parliamentary and presidential elections in November. Since the KRG will not declare independence unilaterally and seems committed to peaceful negotiations with Baghdad, we see little risk of military intervention by Turkey, Iran and Iraq.

Second, diplomatic tensions escalated significantly between Turkey and the US after the latter suspended visa services following the arrest of a US embassy staff member in Istanbul. It seems that the Turkish government gravely miscalculated how far it can push the US, especially after a seemingly successful bilateral meeting between Presidents Trump and Erdogan on the sidelines of the UN summit two weeks ago. The incident highlights yet again that relationships built with the US president do not necessarily extend to the wider US administration and its diplomatic corps. Despite an often aggressive stance, we believe that President Erdogan and his government pursue a calculated foreign policy and will attempt to de-escalate the crisis eventually to preserve Turkey's strong political and economic ties with the US.

On the macro front, South Africa's medium-term budget policy statement on October 25 will be closely watched, following recent fiscal underperformance. Aside from likely stronger revenue performance, the government is also likely to implement further expenditure cuts and is apparently already seeking advice from the IMF on how to do so. While risks are rising, we currently believe that ratings agencies, especially S&P and Moody's, will see through these deteriorations on the fiscal front, especially since they're related to growth and revenue rather than expenditures. Also, the ratings agencies will want to see the outcome of the ANC elective conference at the end of December, where a leadership change could lead to more meaningful policy changes in 2018.

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	Real Growth (%)		Inflation (%)		Official Rates (%)		Long Rates (%)		FX Rates vs USD	
	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F	2017F	2018F
Global	3.0	3.0	2.4	2.5	2.16	2.26	2.97	3.22	-	-
Industrial Countries	2.2	2.0	1.7	1.7	0.75	1.03	1.76	2.19	-	-
Emerging Countries	4.4	4.6	3.7	3.7	4.87	4.59	5.27	5.18	-	-
United States	2.3	2.0	2.0	2.1	1.38	1.88	2.75	3.25	-	-
Canada	3.2	2.2	1.8	2.0	1.25	2.00	2.15	2.50	1.20	1.25
Europe	2.1	1.9	1.7	1.5	0.08	0.14	0.96	1.41	-	-
Euro Area	2.2	2.0	1.6	1.4	0.00	0.00	0.75	1.25	1.15	1.15
United Kingdom	1.5	1.5	2.7	2.3	0.50	0.75	1.75	2.00	1.30	1.25
Sweden	3.1	2.9	1.9	1.8	(0.50)	(0.40)	1.00	1.50	8.25	8.25
Norway	2.1	2.5	2.0	1.7	0.50	0.75	1.70	2.00	8.00	8.00
Japan	1.8	1.6	0.4	0.8	(0.10)	(0.10)	0.05	0.05	115	125
Australia	2.2	2.3	1.8	1.7	1.50	1.50	3.00	3.45	0.76	0.73
New Zealand	2.6	2.7	1.8	1.6	1.75	1.75	3.25	3.50	0.73	0.72
Asia ex Japan	5.9	5.6	1.9	2.5	3.08	3.23	3.95	3.92	-	-
China	6.7	6.0	1.6	2.3	2.90	3.10	3.70	3.60	6.55	6.50
Hong Kong	3.7	3.0	1.7	2.5	2.00	2.25	1.90	1.90	7.76	7.76
India	6.1	6.7	2.5	3.2	6.00	6.00	6.60	6.50	66.00	65.00
Indonesia	5.2	5.7	3.9	3.5	4.25	4.25	6.50	6.60	13,300	13,100
Korea	2.8	2.6	1.9	2.1	1.25	1.25	2.40	2.40	1,150	1,155
Thailand	3.7	3.5	0.4	1.3	1.50	1.50	2.40	2.60	33.00	32.50
Latin America	0.8	2.1	5.8	5.0	8.24	7.07	6.63	6.42	-	-
Argentina	2.4	3.3	21.0	15.0	24.50	16.00	-	-	17.80	19.50
Brazil	0.6	2.4	3.1	3.9	7.00	7.00	9.50	9.00	3.20	3.50
Chile	1.3	2.7	3.2	3.0	2.50	3.00	4.30	4.65	630	660
Colombia	1.6	2.3	4.2	4.0	5.00	5.00	6.80	7.30	3,000	3,100
Mexico	2.1	2.3	5.7	3.5	7.00	6.00	7.05	7.30	18.20	18.90
EEMEA	2.4	2.6	6.3	5.8	6.66	6.16	7.77	8.16	-	-
Hungary	3.6	3.3	2.6	2.7	0.90	0.90	2.85	3.50	315	317
Poland	4.0	3.4	2.0	2.2	1.50	1.75	3.55	4.00	4.30	4.22
Russia	1.7	1.7	4.2	5.2	8.00	7.00	7.60	8.00	58.50	59.00
South Africa	0.5	1.0	5.4	5.3	6.75	6.25	9.00	9.20	13.70	14.10
Turkey	5.2	3.5	9.6	8.0	8.00	8.00	10.70	11.10	3.65	4.00

Long rates are 10-year yields unless otherwise indicated.
Latin American Rates include Brazil, Chile, Colombia and Mexico
Real growth aggregates represent 48 country forecasts not all of which are shown
Blanks in Argentina are due to distorted domestic financial system so are not forecast.