Global Economic Scenario
February 2016

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	2.3% (2.5%)	2.4% (2.5%)	2.1%	2.5% (n.a.)	1.5% (1.7%)	1.5% (1.7%)	2.2%	2.3% (n.a.)
Euro Area	1.4%	1.7%	1.3%	1.7% (n.a.)	0.8% (1.3%)	0.8% (1.0%)	1.7%	1.5% (n.a.)
Japan	1.1% (1.0%)	1.2%	1.0%	0.6% (n.a.)	0.3%	0.6% (0.7%)	0.3%	2.0% (n.a.)
UK	1.8% (1.9%)	2.3%	1.8%	2.3% (n.a.)	0.7% (1.1%)	1.0% (1.1%)	2.0%	1.8% (n.a.)
Switzerland	0.7%	1.2%	1.0%	1.7% (n.a.)	-0.3% (0.0%)	-0.4% (-0.3%)	0.2%	0.3% (n.a.)

Source for Consensus Estimates: Consensus Economics Inc. London, 11 January 2016

USA – Activity slowdown at the end of 2015

GDP Growth

Swiss Life Asset Managers	*Consensus*
2016: 2.3%	*2016: 2.6%*
2017: 2.1%	*2017: 2.5%*

The US economy had entered a soft patch in the fourth quarter 2015, driven by slowing activity in manufacturing and above all mining industries. Weak survey readings stemming from corporate America were also confirmed by the latest Beige Book, published by the Federal Reserve. This anecdotal summary of economic conditions compiled by regional Reserve Banks actually reported continued expansion across the country, however at a slower pace than over past months or quarters. The outlook remained mostly positive across the districts. Most companies cited stronger headwinds from the strong US Dollar or else the strong plunge of oil prices which creates additional pressure for companies related to the energy sector. Themes, which have been playing out over past quarters largely remain intact: consumer spending, auto sales and real estate have remained the most pertinent growth supports, albeit at a lower degree. Retail sales did not meet expectations, basically due to unseasonably warm weather and the resulting problem with seasonal adjustment factors. Furthermore, sales numbers from online shopping were reported to be strong, but doubts remain if those are correctly incorporated in overall published retail sales figure. Due to these weak spots cited for the last quarter of 2015, we adjusted our GDP outlook accordingly which also had a notable impact on the 2016 outlook via the base effect. Importantly, we left our growth assumptions for coming quarters unchanged. In our view, the assumption of consumer-driven growth, which is the theme for most advanced economies, remains valid. As impressively underlined by the labour market report for December, consumers' propensity to spend gets support from strong hiring and the improving sentiment of job security. Employment grew at an average pace of 284'000 in the fourth quarter 2015, which is among the strongest gains in this long and extended recovery phase after the financial crisis and in stark contrast to weak output growth as mentioned before. A renewed plunge in oil prices means that lower income households in particular have more budget available to spend on other items.

Inflation

Swiss Life Asset Managers	*Consensus*
2016: 1.5%	*2016: 1.7%*
2017: 2.2%	*2017: 2.3%*

The oil price does not seem to find a bottom. This obviously creates the need for all forecasters to revise their inflation path. We lowered the projected monthly increase for both December and January, which caused revision of the 2016 whole year forecast to the downside yet again. With the latest changes, the headline inflation path for 2016 assumes a U-shape, rising to around 1.4% with the January print, before moving closer to 1% again by mid-year and rising again in late 2016. According to our own projection, core inflation will continue to oscillate around 2% for most of 2016.

Euro Area – Sentiment remains rather upbeat

GDP Growth

Swiss Life Asset Managers	*Consensus*
2016: 1.4%	*2016: 1.7%*
2017: 1.3%	*2017: 1.7%*

Contrary to the US economy, survey data ended the year 2015 on a high note. Sentiment indicators collected by the European Commission complemented a rise in the composite PMI. Indicators showed a broad-based improvement across sectors and a further gain in consumer confidence. Unemployment declined to its lowest level in more than four years, falling to 10.5% in December, down 1.6 percentage points from its peak reached in March 2013. Therefore, most recent data confirm our view that growth dynamics in the region remain unaltered and this is reflected in our projection of quarterly GDP growth rates. The main driver remains domestic demand while growing global headwinds and geopolitical tensions only had limited impact thus far. Finally, the ECB's policy measures of the past show tangible benefits in terms of availability and cost of credit for non-financial corporations and households which should support growth dynamics going forward.

Inflation

Swiss Life Asset Managers	*Consensus*
2016: 0.8%	*2016: 1.1%*
2017: 1.7%	*2017: 1.5%.*

For obvious reasons, we had to massively revise our whole year 2016 inflation projection to the downside, solely due to changes of the December 2015 and January 2016 prints. Based on this, we expect headline inflation to average 0.8% in 2016 instead of 1.3% previously. The strong plunge yet again of energy prices towards the end of last year and at the start of this year cancelled out the strong base effect which would otherwise have pushed headline inflation well above 1%. Moreover, food inflation looks weak as well on a global scale and may feed into processed food inflation going forward. While headline inflation will remain off the ECB target now for longer than originally expected, core inflation should continue to move modestly to the upside. A weak Euro has had only limited impact so far. The obvious risk remains energy prices, but not only to the downside. Once prices rise from current levels, the impact in percentage terms on headline inflation will be noteworthy.

Japan – Again a debate on the consumption tax

GDP Growth

Swiss Life Asset Managers	*Consensus*
2016: 1.1%	*2016: 1.3%*
2017: 1.0%	*2017: 0.6%*

Like in the Euro Area, key survey data for Japan remained stable or even improved during the final quarter 2015, despite the negative newsflow out of China. Most importantly, Japan's purchasing managers index (PMI) continued to improve from a dip in the second quarter 2015. Japan's high-tech producers and car makers are clearly benefitting from lower energy prices and rising disposable incomes of private households in the developed world. A fair comparison of our own forecast for 2017 and the newly introduced consensus estimates is not possible at this stage. Most institutes which form part of the consensus poll have included a renewed consumption tax rate hike from 8% to 10% into their GDP and inflation profiles. Despite prime minister Abe's repeated commitment to proceed with the increase as planned "regardless of the business environment", we want to wait and see whether this measure will be implemented given the current global economic conditions and the experience of 1997 and 2014 when rate hikes had a devastating impact on domestic demand. We thus closely monitor the political debate. Once the final decisions on timing, size and exemptions to the tax hike are taken, we will adjust the 2017 forecasts for growth and inflation accordingly.

Inflation

Swiss Life Asset Managers	*Consensus*
2016: 0.3%	*2016: 0.8%*
2017: 0.3%	*2017: 2.0%*

As for GDP growth, the notable difference between our own forecast of average inflation in 2017 and the consensus view is explained by our hesitation to include a consumption tax hike in 2017 into our inflation profile. Meanwhile, we continue to see limited inflation pressure despite gradually improving wage growth. The most important reason why Japan's annual headline inflation rate held above the zero line since mid-2013 were rising import prices due to the massive devaluation of the Yen since end of 2012. This tendency is now set to reverse as the Yen's trade weighted value increased by more than 7% since end of June 2015.

UK – EU referendum most likely this year already

GDP Growth

Swiss Life Asset Managers	*Consensus*
2016: 1.8%	*2016: 2.4%*
2017: 1.8%	*2017: 2.3%*

Since early 2014, our 2015 growth forecast was comparably prudent as we expected that financial conditions to dampen activity. By April 2015, our forecast of 2.0% was far below the consensus estimate of 2.6%. Later, initial reports on strong activity through the first half 2015 forced us to lift our forecasts to as much as 2.5% in October which by then was at par with consensus. With hindsight, we had better trusted our own judgement as a substantial revision to the official first quarter data brings our latest assumption for full-year 2015 performance down to 2.2% again. Going forward, Prime Minister Cameron apparently wants to hold the referendum on whether Britain remains a member of the EU in 2016 already as renegotiations with Brussels are expected to be finished in February. We do not believe that voters opt for the "Brexit". Yet, uncertainties as regards the economic prospects in case of a majority of voters willing to leave the EU in parts explain our sub-consensus forecast for growth in 2016. Firms with alternative choices to invest or hire abroad, are likely to postpone major projects in Britain into the final quarter 2016, when uncertainties as regards the referendum are gone.

Inflation

Swiss Life Asset Managers	*Consensus*
2016: 0.7%	*2016: 1.3%*
2017: 2.0%	*2017: 1.8%*

The latest fall in energy prices results in yet another downward revision to our headline inflation forecast. Yet, as the Sterling depreciated by 10% on a trade weighted basis since November 2015, the effect of the latest commodity price declines should be less pronounced than in other developed regions. As the economy grows above potential, the output gap is due to be closed this year. Thus, once energy prices stabilise or start trending higher again, the risk of rapidly resuming inflationary tendencies is more important in the United Kingdom than in any other Western European economy.

Switzerland – Unemployment to rise to 3.8% this year

GDP Growth

Swiss Life Asset Managers	*Consensus*
2016: 0.7%	*2016: 1.2%*
2017: 1.0%	*2017: 1.7%*

According to the first publication of consensus figures for 2017, the majority of economists not only projects a return to growth dynamics seen between 2012 and 2014 for 2016 and 2017, but they also expect this recovery to be sustainable. This optimism stands in clear contrast with media headlines at the anniversary of the SNB move in January 2015 to abandon the minimum exchange rate policy. At first glance, our sub-consensus forecast could be interpreted as pointing to a country deprived of its industrial backbone. Yet, survey data suggest that industrial activity stabilised by the end of 2015. On aggregate, a majority of firms expects rising orders over the next three months according to think tank KOF's industrial survey. Thus our skeptical assessment for future dynamics in Switzerland is not based upon fears of a de-industrialisation of Switzerland. Rather, we believe that final domestic demand will grow more slowly going forward than over the past twelve months when lower prices for durable goods lured consumers into a temporary shopping spree. Besides saturated demand for big ticket items, we also believe that rising unemployment will dampen consumption growth over the coming quarters. Our labour market model predicts an increase of the unemployment rate from currently 3.4% to 3.8% until end of 2016.

Inflation

Swiss Life Asset Managers	*Consensus*
2016: -0.3%	*2016: -0.2%*
2017: 0.2%	*2017: 0.3%*

Again, we had to lower our forecast for average inflation through 2016, triggered by falling energy prices. In January, prices for heating oil and gasoline likely reduce the consumer price index by 0.18% compared with the previous month. Combined with the usual negative seasonal pattern in the first month of the year, we now assume that the consumer price index will drop by 0.4% in January, or 1.3% from the same month last year.