# Global Economic Scenario
# *November 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 | 1.4% (1.3%) | 1.5% | 2.0% (1.8%) | 2.2% (2.3%) | 1.3% (1.2%) | 1.2% | 2.3% (2.2%) | 2.3% (2.2%) |
| Euro Area | 1.6% (1.5%) | 1.6% (1.5%) | 1.1% (0.9%) | 1.3% | 0.2% | 0.2% | 1.5% | 1.3% |
| Japan | 0.6% | 0.6% | 0.9% | 0.9% (0.8%) | -0.3% | -0.2% | 0.1% | 0.4% |
| UK | 1.9% | 1.9% (1.7%) | 0.6% | 0.9% (0.7%) | 0.7% | 0.7% | 2.5% | 2.3% |
| Switzerland | 1.4% | 1.5% (1.2%) | 0.9% | 1.4% (1.3%) | -0.4% (-0.3%) | -0.4% | 0.4% | 0.3% |

*Source for Consensus Estimates: Consensus Economics Inc. London, 10 October 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 – Patches of inflation everywhere

#### GDP Growth

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: 1.4%* | *2016: 1.5%* |
| *2017: 2.0%* | *2017: 2.2%* |

No matter which of the candidates, Clinton or Trump, will win the race on 8 November, public infrastructure spending is bound to increase in the year 2017 and thereafter. Both candidates have pledged to raise fiscal spending and thus add support to overall GDP growth rates. Consequently we lifted our forecast with respect to the government contribution to GDP growth for 2017. This lifted our GDP projection from 1.8% to currently 2.0% and thus somewhat closed the gap to consensus expectations. We have spread this extra contribution from the fiscal side evenly over the quarters although the pattern may turn out differently depending on how speedy the decision process on additional fiscal spending will be. This again lastly depends on the balance of powers in Congress after the election. At the same time, the third estimate of growth momentum in the second quarter also revealed a slightly higher growth rate from the previous publication and this obviously left traces in this year's whole year forecast. As regards economic momentum in the third quarter - of which the advance estimate will be published on 28 October - our notion of a considerable slowdown of personal consumption spending has been confirmed by weak retail sales figures throughout the quarter. Given that personal consumption added substantially to GDP growth in the second quarter of this year, a certain payback was to be expected. Despite our expectation of a slim contribution from the consumer side, however, an acceleration of total GDP growth in the third quarter to 2% from 1.4% through the previous quarter is nevertheless our base case. After five consecutive quarters where inventories shaved off substantially from overall growth, we expect this drag to come to an end, at least temporarily.

#### Inflation

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: 1.3%* | *2016: 1.2%* |
| *2017: 2.3%* | *2017: 2.3%* |

Services inflation is not the only stronghold of the inflation landscape in the US. Rental vacancy rates for houses as well as appartments have reached the lowest level since 1985. Within the CPI basket, rent of primary residence makes up almost 8% of all items. Since the market is tight and getting tighter, price pressure from that side can be expected to remain intact. Rents are a subcomponent of the "shelter" complex within CPI calculations. Shelter as a whole has a weight of 33.4% and is not to be neglected when it comes to forecasting. It has reliably contributed to inflation since the beginning of 2011 at a continuously rising clip. Finally, energy and gasoline prices in particular have become noteworthy positive contributors to the monthly change of consumer prices. October 2016 will mark a turning point also in the annual change of headline inflation because it will be the first time since July 2014 that gasoline prices will be a positive driver also on a year-over-year basis. The often cited base effect is currently fully unfolding and will push headline inflation above 2% by January 2017.

## Euro Area – Attenuating the Brexit shock

**GDP Growth**

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: 1.6%* | *2016: 1.6%* |
| *2017: 1.1%* | *2017: 1.3%* |

The European Central Bank (ECB) after its last meeting was actually striking the dovish tone that most market participants had expected. At the same time, they delayed a decision on the extension of the quantitative easing programme or on changing the modalities until December, when the updated economic forecast will be discussed in the committee. We do not expect a dramatic shift in monetary policy, but stick to our view that quantitative easing will be extended beyond March 2017. Since sentiment data as well as hard economic data continue to perform better than could be feared after the UK Brexit vote, we slightly attenuated the hit on quarterly GDP growth rates which we had built into our growth projection for the moneatry union at the end of June. Growth dynamics will not reach pre-Brexit levels, but are bound to soften less dramatically. This led to a revision of our growth outlook for the current and next year. Some caution is also warranted given the fact that certain political hurdles still need to be taken over coming months. Furthermore, given the increase of energy prices, that windfall for consumers as well as energy-consuming corporates falls out of GDP calculations. Finally, according to the ECB lending survey, banks' credit standards for small and medium-sized companies have tightened somewhat. Actual loan growth to non-financial corporations hovers at the zero line ever since the spring months in a year-over-year comparison.

**Inflation**

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: 0.2%* | *2016: 0.2%* |
| *2017: 1.5%* | *2017: 1.3%* |

The headline inflation rate is slowly trending upwards and has reached a level of 0.4% in September. According to our own forecast headline inflation will climb up to reach 1.2% by January 2017 with a little help also from higher energy prices. Core inflation already stands at 0.8% just to reach 1.2% as well by January next year. One needs to stress above all that the major dampening effect, i.e. fiscal austerity, has mostly come to an end.

## Japan – Personal consumption remains the weak link

**GDP Growth**

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: 0.6%* | *2016: 0.6%* |
| *2017: 0.9%* | *2017: 0.9%* |

Given that high frequency data point to yet another quarter of soft consumption growth, our own moderate projection of 0.2% GDP growth in the third quarter may turn out to be still too optimistic. Obviously, adverse weather conditions throughout the summer months kept consumers from shopping even though consumption figures for September have not yet been reported. On a more positive note however, consumer confidence has been rising since quite a while now and should finally translate into higher spending and a sturdier growth contribution from personal consumption. Meanwhile, the trend in machinery orders and capital goods shipments indicates that private investments may have been a growth pillar after all. This contribution may be moderated by low capacity utilisation rates (although we saw a surprisingly strong jump in August) and the fact that the Yen keeps going strong. However, industrial production largely surprised to the upside in August with a 1.3% increase from the previous month whereas at the same time the manufacturing PMI managed to climb back up above 50. Thus, the worst effects of the Yen appreciation may have been digested.

**Inflation**

| *Swiss Life Asset Managers* | *Consensus* |
|---|---|
| *2016: -0.3%* | *2016: -0.2%* |
| *2017: 0.1%* | *2017: 0.4%* |

The goal of a return to 2% annual inflation in the near or even medium term looks unachievable despite very stimulative monetary policy. The drag from tumbling commodity prices has disappeared and even reversed lately, but that does not automatically mean that underlying price pressures will climb as well. Without a pronounced pick-up in demand, core prices will hardly be able to contribute to headline inflation. Consequently, our full year inflation forecast for next year remains perilously close to the zero line, much to the sorrow of the Bank of Japan. As in other developed economies, meaningful labour market reforms are badly needed to support consumer spending also in the longer run.

## UK – Business sentiment on a roller-coaster ride

### GDP Growth

| Swiss Life Asset Managers | Consensus |
| --- | --- |
| *2016: 1.9%* | *2016: 1.9%* |
| *2017: 0.6%* | *2017: 0.9%* |

After a quiet period during which surprisingly strong data following the "Brexit" referendum dominated headlines, the political debate heats up again. Yet, short-term, the economy continues to benefit strongly from ultra-loose financial conditions. Coincident indicators have improved substantially as can best be shown by the roller-coaster ride purchasing managers indices (PMI) for various sectors were on between April and September. Immediately after the vote for Brexit, the manufacturing sector's PMI dropped below the critical 50 points expansion line, to its lowest reading since July 2012. But with growing evidence of favourable financial conditions, and most importantly, a windfall gain in exporters' competitiveness thanks to the weaker Pound, the PMI recovered to its best reading since July 2014. Under normal circumstances, this reading is consistent with 0.4% quarterly GDP growth. Although we adjusted our initial "Post Brexit" growth profile to the upside in order to mirror constructive data in the first phase, we remain more prudent than econometric models would suggest. As rhetorics around the divorce get more serious, we expect a prudent investment and hiring behaviour of those firms depending on free EU market access. Over time, such reluctance will be felt on Britain's labour market and weigh on private households purchasing power.

### Inflation

| Swiss Life Asset Managers | Consensus |
| --- | --- |
| *2016: 0.7%* | *2016: 0.7%* |
| *2017: 2.5%* | *2017: 2.3%* |

Reflation is a general trend in the developed economies, but consumer prices in the UK are set to rise particularly fast in the months ahead. Given the weak Pound, import prices are adding to inflationary pressure which so far was limited to domestically generated service prices. In September, annual inflation jumped from 0.6% to 1.0%. We expect headline inflation to reach 2% by January next year and to stay above this rate for all of 2017.

## Switzerland – Return to positive inflation delayed

### GDP Growth

| Swiss Life Asset Managers | Consensus |
| --- | --- |
| *2016: 1.4%* | *2016: 1.5%* |
| *2017: 0.9%* | *2017: 1.4%* |

Last month, we were forced to lift our forecast for GDP growth through 2016 on news of stronger than expected second quarter activity and upwardly revised GDP numbers for the first quarter. Other members of the consensus sample followed since. As a consequence, our forecast for both years is now again more prudent than the median estimate of 15 institutes. The difference remains large for 2017 with our forecast being at the bottom of the range as we think that the second quarter numbers resulted from unsustainable developments in the field of government outlays and transfer volumes traded at commodity traders' desks. Government consumption, which was the key contributor to growth in the second quarter is an unlikely candidate to repeat this strong performance. Public finances are stretched in a large number of cantons and major communities. Above all, we miss signs of improving underlying dynamics in private domestic sectors from personal consumption over corporate investments to construction. Private consumption continues to grow at a slower pace than in previous years. In parts this is a normal reaction to last year's consumption boom when households took profit of falling import prices. Another reason for slower consumption growth can be found in substantially lower net migration numbers compared with the last decade.

### Inflation

| Swiss Life Asset Managers | Consensus |
| --- | --- |
| *2016: -0.4%* | *2016: -0.4%* |
| *2017: 0.4%* | *2017: 0.3%* |

Last month, cheaper holiday packages, air traffic fees and domestic hotel prices prevented the consumer price index (CPI) from rising by the amount we had expected. Yet, the return to positive inflation rates for the first time since August 2014 is just delayed by one month. As prices for gasoline and heating oil rose strongly in October, we expect a marked monthly increase in the CPI to be published on 7 November.