National Bank of Greece | Economic Research Division

NATIONAL BANK OF GREECE

Global Economic & Markets Factbook

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See Disclosures & Analyst Certification on page 81

Concerns are rising over the future growth potential of a world economy suffering from high debt, political angst in advanced economies as middle class expectations are revised down, and with fiscal and monetary policy running out of space to manoeuver.

Regarding the short-term outlook, US GDP is expected to accelerate slightly following a disappointing first half, while modest fiscal easing should support activity in Japan. Euro area growth remains moderate, while, in the UK, the consequences of the “Brexit” vote appears less severe than expected. In China, the gradual transition of the economy continues, albeit rapid growth of private sector debt and the housing market boom pose risks.

Monetary policy appears at a crossroads. The Bank of Japan shifted its focus to yield-curve targeting and the ECB is ready to expand its asset purchases, probably by end-year. Economic data would need to deteriorate significantly for the Bank of England to cut its policy rate further. On the other hand, the Fed will likely increase rates in December, barring a significant deterioration in high-frequency indicators.

Political uncertainty remains, with the US Presidential elections the main focus. The Clinton candidacy appears to be gaining the upper hand. The fragile European recovery could be derailed by the Italian referendum on Senate reform, the elections in France and Germany, as well as “Hard-Brexit” negotiations.

In this environment, equities remain vulnerable, as their valuations are on the high side. We remain cautious regarding Government bonds, as nominal yields are expected to increase, albeit from an exceptionally low base, due to Fed tightening and increasing inflation. Corporate bonds, particularly in Europe, still offer value as the ECB and BoE purchase programme may lead to spread tightening, albeit higher yields on core government bonds could threaten the positive credit performance.

Real GDP Growth (%)

	2015	2016f	2017f
US	2,6	1,5	2,2
Euro Area	1,9	1,6	1,5
UK	2,2	1,9	1,1
Japan	0,6	0,6	0,6
China	6,9	6,6	6,2

*Seasonally adjusted YoY growth rate
Source: NBG Research, IMF, Bloomberg

Inflation (%)

	2015	2016f	2017f
US	0,1	1,1	2,3
Euro Area	0,0	0,3	1,4
UK	0,0	1,3	2,1
Japan	0,8	0,5	1,3
China	1,4	2,3	3,0

*Year-to-year average % change
Source: NBG Research, IMF, Bloomberg

Policy Rates (%)

	2015	2016f	2017f
US	0,50	0,75	1,25
Euro Area	0,05	0,00	0,00
UK	0,50	0,25	0,25
Japan	0,10	-0,10	-0,10
China	1,50	1,50	1,25

*End of period forecast
Source: NBG Research, IMF, Bloomberg

Developed Markets

Emerging Markets

United States

- US growth improved in Q2, albeit from a poor Q1 performance, with real GDP increasing by 1.4% qoq saar in Q2:16, from +0.8% in Q1. Private consumption was the main growth driver in the first half and is expected to continue to support growth in H2, amid strong job gains and rising wages, albeit at a softer pace. Indeed, households' net worth continues to increase (+5.0% qoq saar in Q2) and liquid assets as a per cent of total liabilities stand at 2.5% (l-t average of 2.2%).

- GDP Nowcast models suggest a pick-up to c. 2.0% for Q3:16 growth, as the drag from weak energy-related business investment fades. IMF estimates for real GDP growth stand at 1.6% yoy for 2016 and at 2.2% yoy for 2017 (WEO, October 2016), albeit policy uncertainty poses a significant downside risk ahead of the upcoming US elections (November 8). Clinton remains ahead in the polls, with a margin of 7 pps (as of October 21).

- The housing market remains healthy, albeit the recovery has recently lost momentum. Note that residential investment subtracted 0.3 pps from overall growth in Q2:16, following eight quarters with a positive contribution. A similar performance is expected for Q3. House valuation metrics (real estate wealth to income, price to rent) appear stretched once again (see page 12).

- Hard data, to date, suggest a slight improvement in Q3 business investment (BI) growth. Structures investment (c. 20% of total BI) is expected to have risen considerably, with the number of oil rigs up c. 25% qoq in Q3, following the rebound in oil prices. Moreover, manufacturing production stands at +0.9% qoq saar in Q3 vs -1.0% in Q2. Leading indicators, however, suggest a less positive outlook, with the ISM manufacturing index averaging 51.2 in Q3 from 51.8 in Q2.

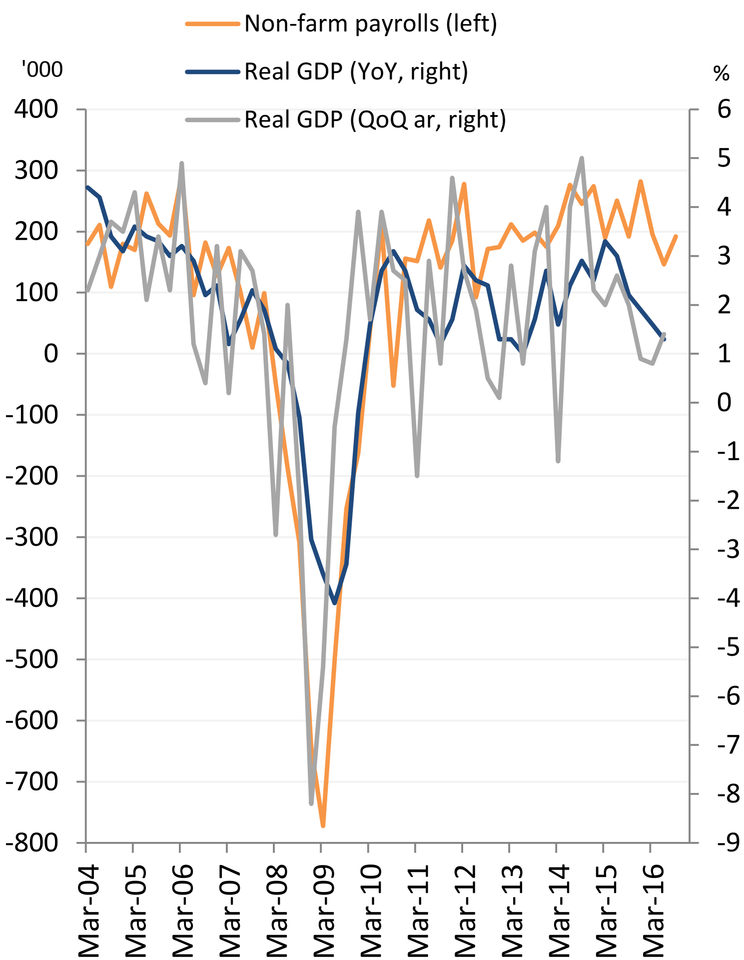
- Labor market conditions remained strong in Q3, with nonfarm payrolls (NFPs) increasing by 192k on average (+171k in H1:16). The unemployment rate was broadly stable at 4.9%, on average, due to an increasing labor force participation rate (by 0.5 pts to 62.9%). The latter suggests the existence of labor market slack, which alleviates pressure on wages.

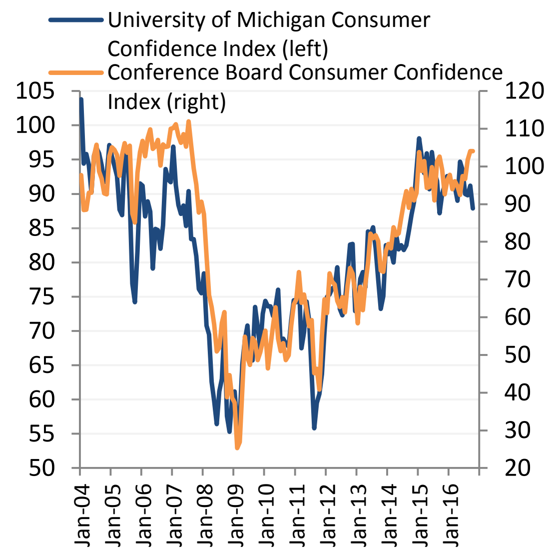
- Fiscal stimulus (change in the cyclically-adjusted primary balance) will turn positive in 2016, adding 0.5 pps to GDP growth according to the IMF, following an average subtraction of 1.2 pps per annum since 2010. Clinton and Trump have both highlighted fiscal stimulus.

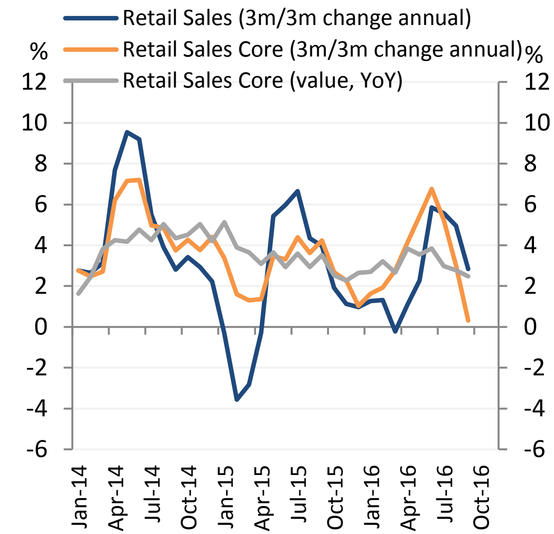
- The Fed, at its September meeting, pointed to an increased likelihood for a rate hike by end-2016 (to 0.50% - 0.75%), reiterating its confidence that inflation will revert, in the medium-term, to the 2% target (Core PCE: 1.7% and PCE: 1.0% as of August). At the same time, the Fed adopted a more dovish stance towards the future path of the federal funds rate (at 2% by end-2018).

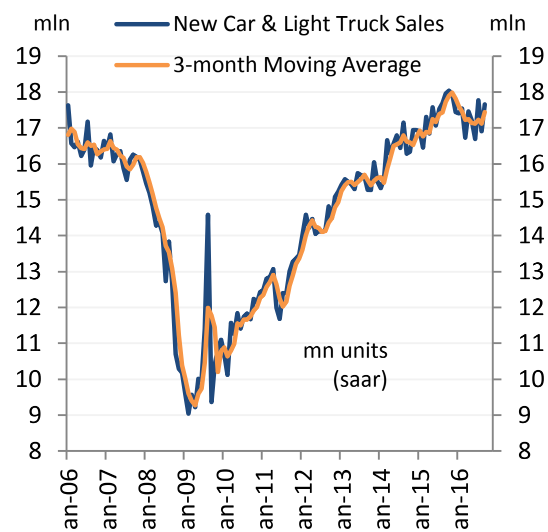
- The S&P500 underperformed its peers in Q3 (+3.3% vs +5.7% for the MSCI DM ex-US) and has remained in the range of 2125-2175 during the past two months. Investor attention will now turn to the Q3:16 corporate earnings season (S&P500 EPS so far in Q3: -1% yoy / +3.0% yoy excluding the energy sector). UST yields increased, from exceptionally low levels recorded at end-Q2:16, with the 10Yr yield up by 29 bps to 1.76% and the 2Yr yield up by 24 bps to 0.82%. In the same period, the USD (in NEER terms) rose by 0.9%.

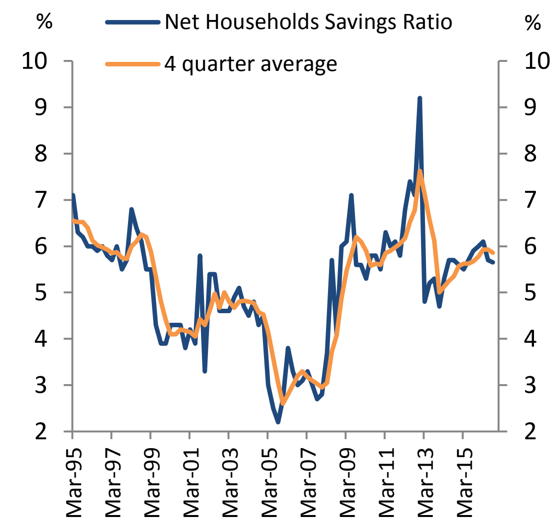
Retail spending has slowed, and the household savings rate has increased





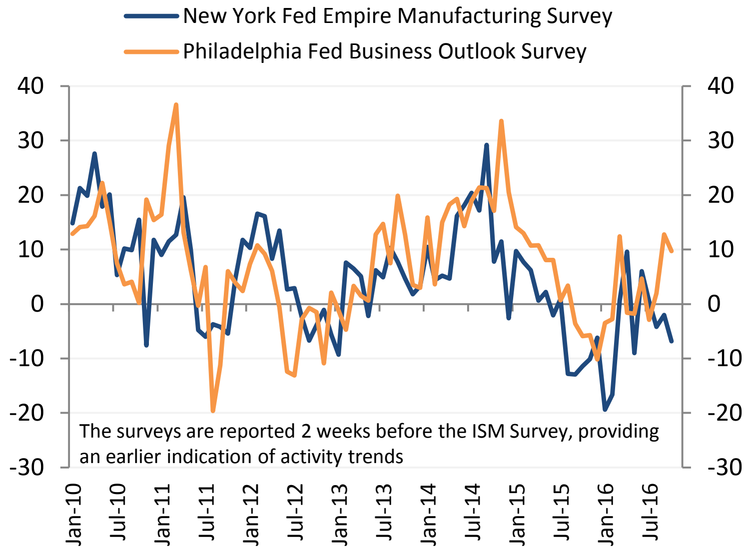


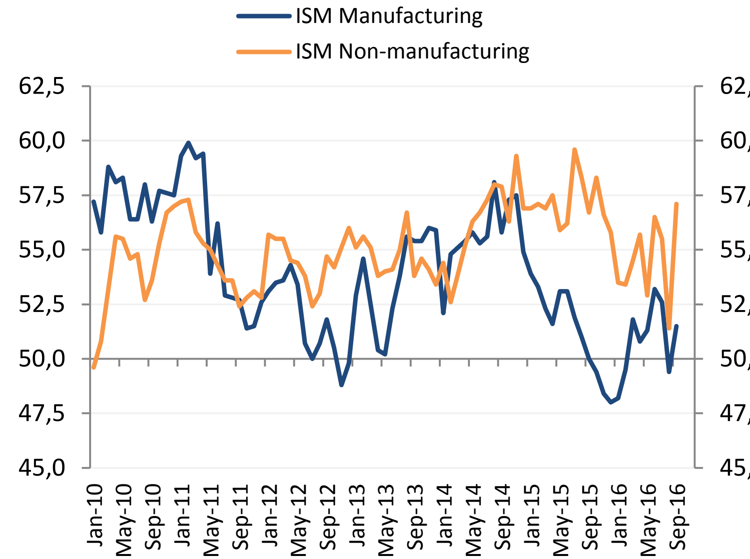


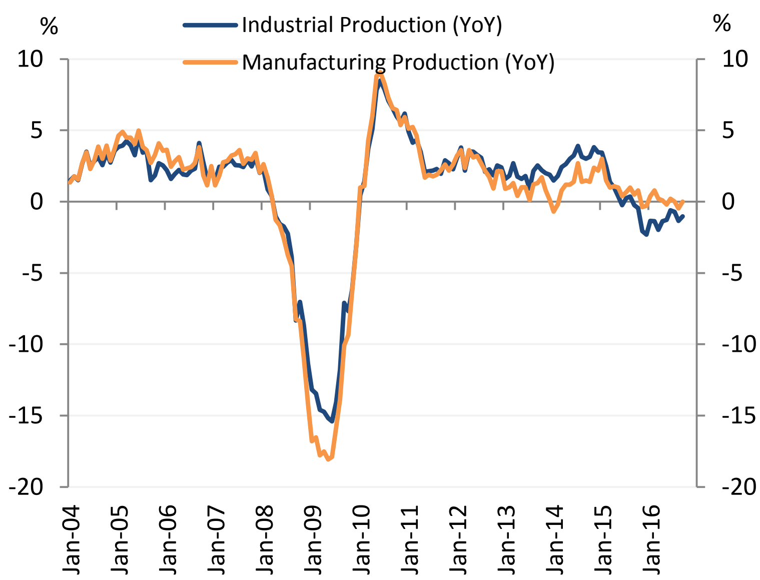


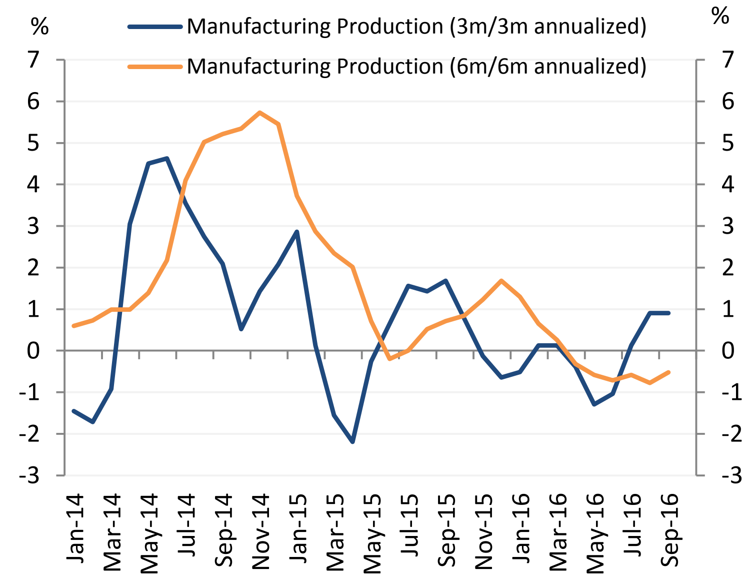
Source: US Bureau of Labor Statistics, US Bureau of Economic Analysis, Non-farm payrolls 3-month average, Real GDP QoQ seasonally adjusted annualized rate

Data suggest investment appetite remains weak







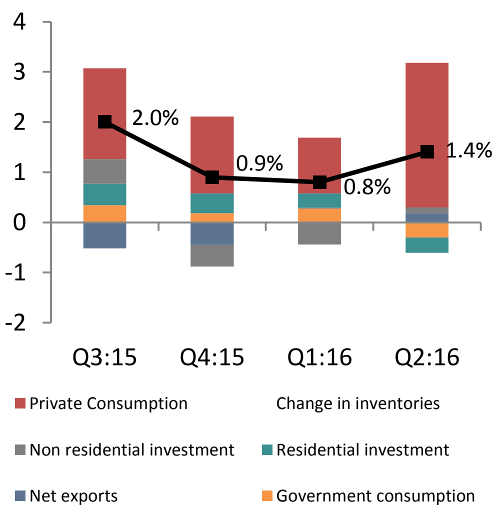


Private consumption will remain the main growth driver in Q3, albeit to a lesser extent compared with Q2

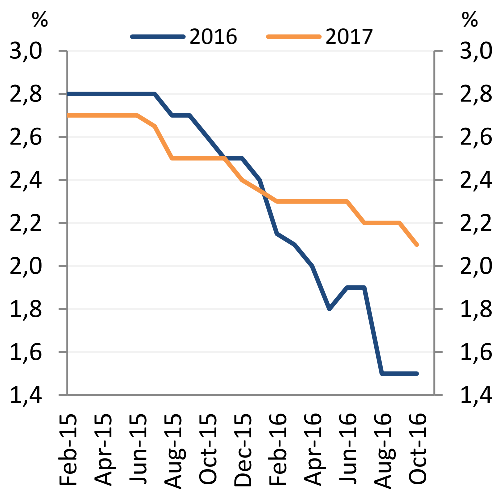
US Real GDP Growth	2014	Q1:15	Q2:15	Q3:15	Q4:15	2015	Q1:16	Q2:16	Q3:16e	Q4:16e	2016e
GDP (YoY)	**2,4**	3,3	3,0	2,2	1,9	**2,6**	1,6	1,3	1,3	1,9	**1,5**
GDP (QoQ saar)	-	2,0	2,6	2,0	0,9	-	0,8	1,4	2,1	3,2	-
Private consumption (QoQ saar)	2,9	2,4	2,9	2,7	2,3	3,2	1,6	4,3	2,0	2,8	2,6
Government consumption (QoQ saar)	-0,9	2,6	3,2	1,9	1,0	1,8	1,6	-1,7	-0,5	1,0	0,7
Investment (QoQ saar)	5,5	3,6	4,1	5,6	-0,4	3,9	-1,1	-1,0	1,1	3,3	0,7
Residential (QoQ saar)	3,5	13,4	14,8	12,6	11,5	11,7	7,8	-7,8	-3,1	8,0	4,9
Non-residential (QoQ saar)	6,0	1,3	1,6	3,9	-3,3	2,1	-3,4	1,0	2,3	2,0	-0,3
Inventories contribution (QoQ saar)	-0,1	0,9	-0,5	-0,6	-0,3	0,2	-0,4	-1,2	0,2	0,5	-0,4
Net Exports contribution (QoQ saar)	-0,1	-1,7	-0,1	-0,5	-0,5	-0,7	0,0	0,2	0,3	0,0	-0,1
Exports (QoQ saar)	4,3	-5,8	2,8	-2,8	-2,7	0,1	-0,7	1,8	5,0	10,2	0,7
Imports (QoQ saar)	4,4	5,6	2,9	1,1	0,7	4,6	-0,6	0,2	2,1	8,1	1,1

Source: BEA, Bloomberg, NBG estimates

GDP Contributions (%)

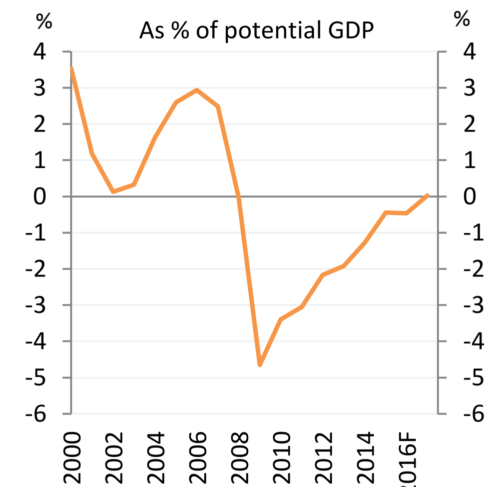


GDP Forecast Evolution



Source: Bloomberg Consensus

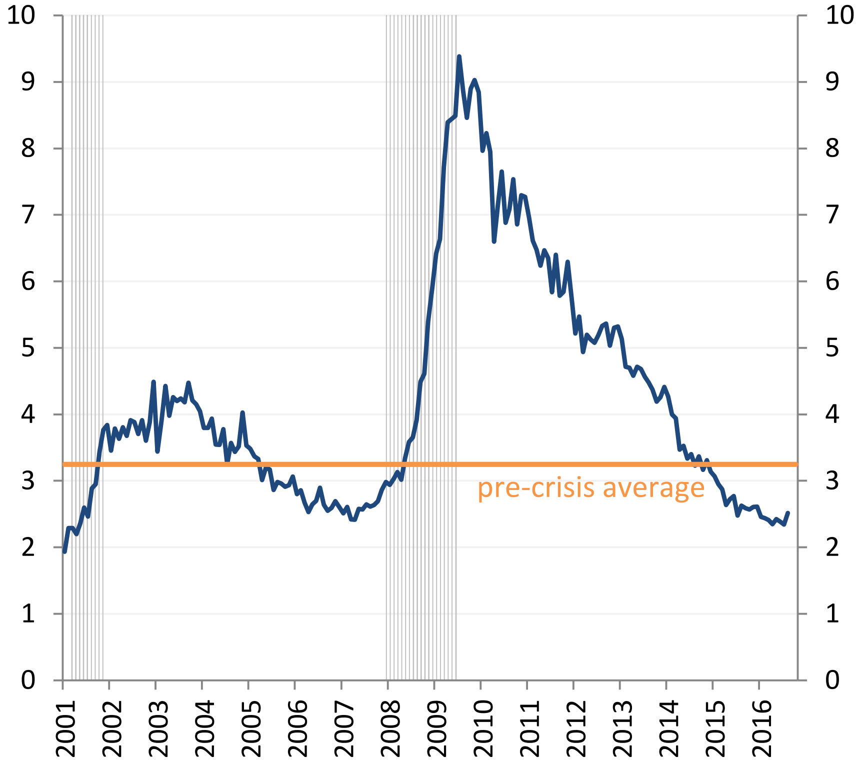
Output Gap



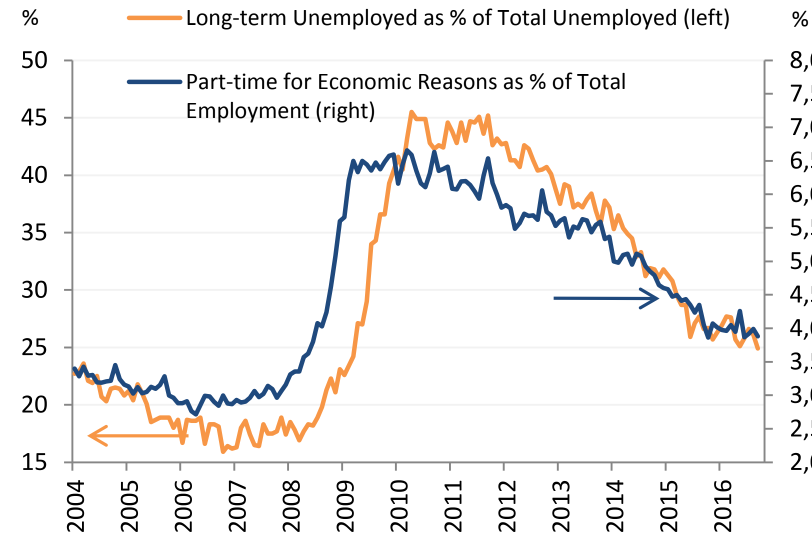
Source: IMF

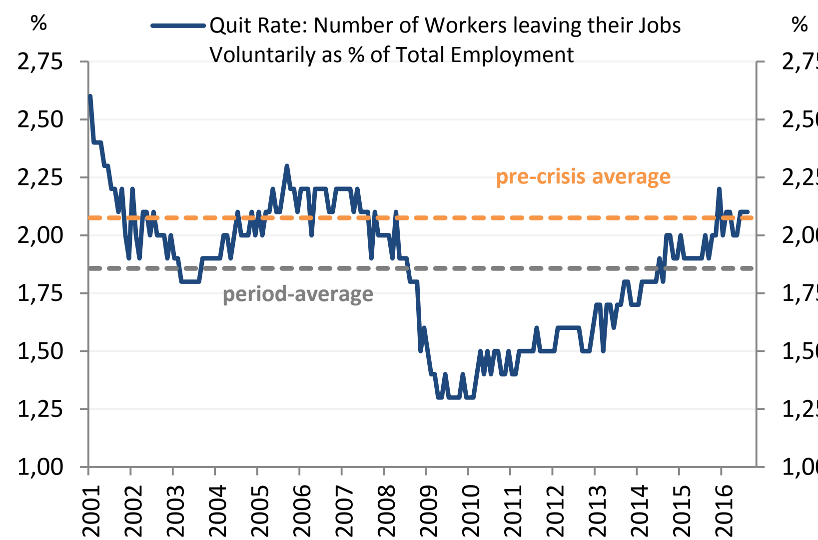
Labor market continues to tighten

People Per Job Opening Index

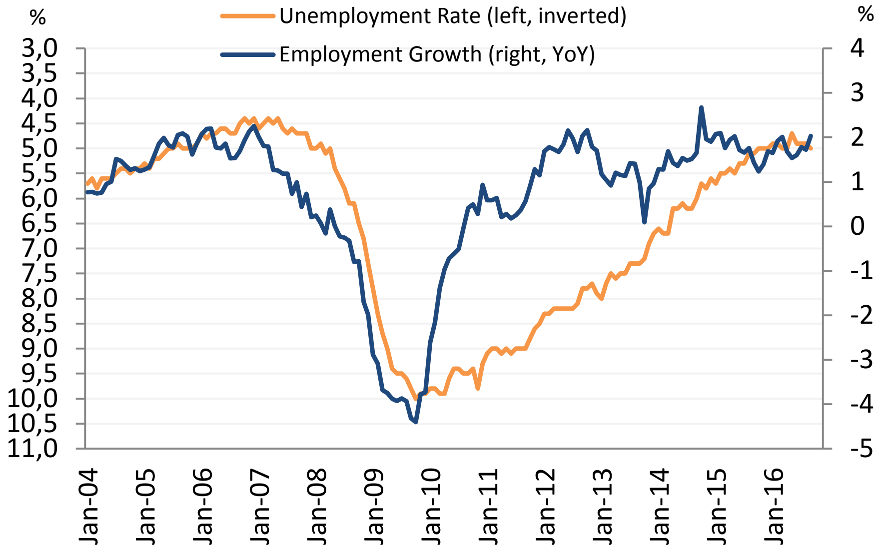


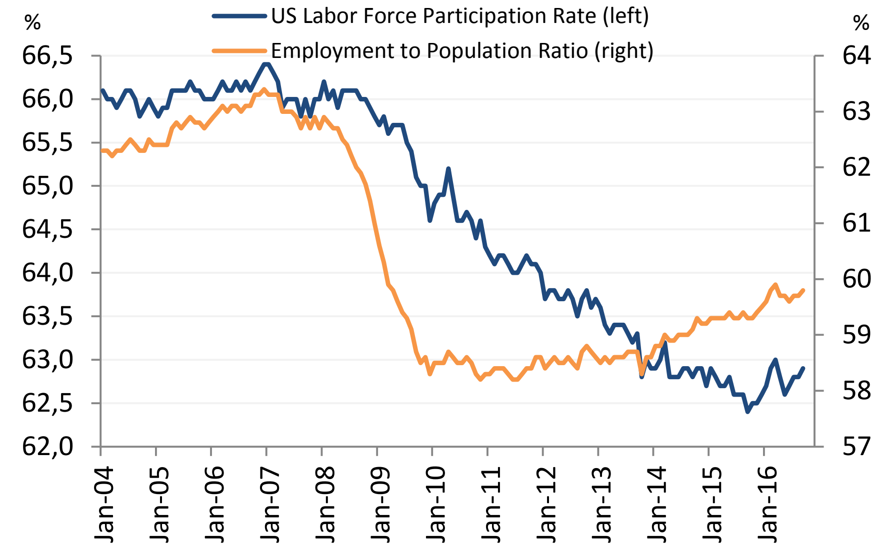
Index: Total Number of Unemployed plus People not in Labor Force but who want a job now divided by Total Number of Job Openings. US Recessions in shaded areas
Source: US Bureau of Labor Statistics, NBER, NBG Estimates

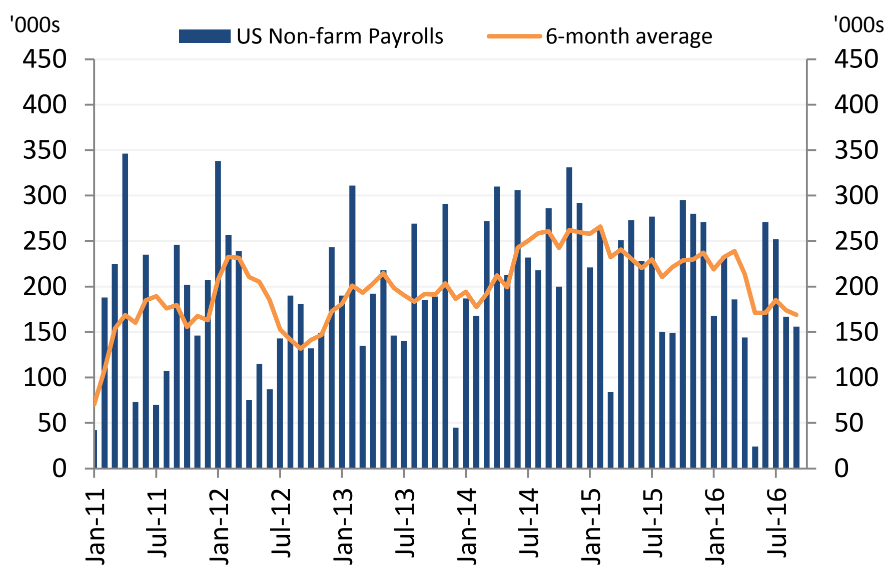


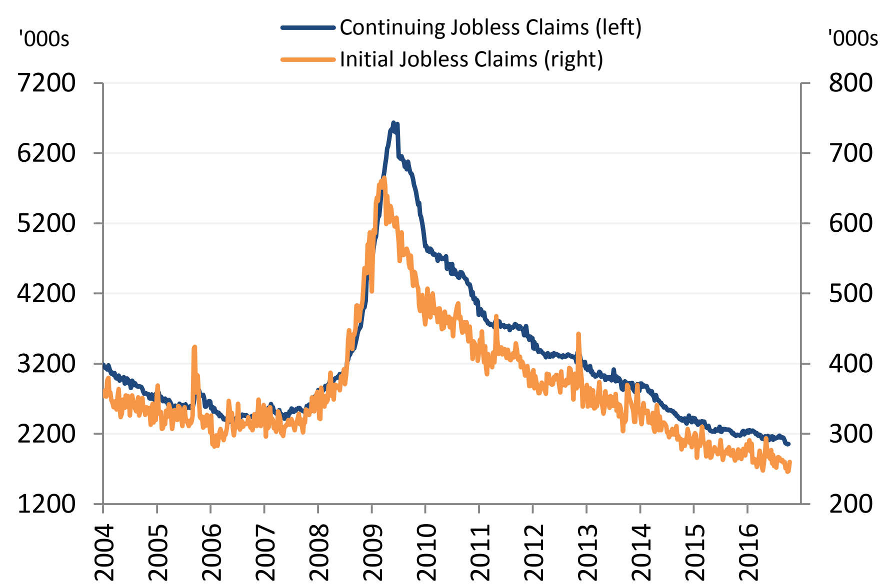


The improved labor market conditions attract more people to the workforce, with the LFPR at a 6-month high

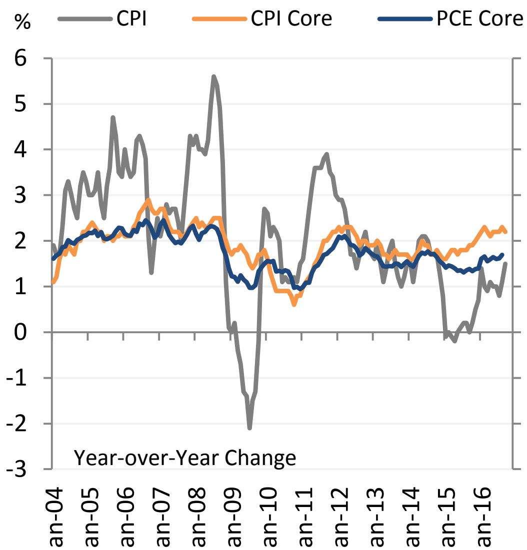


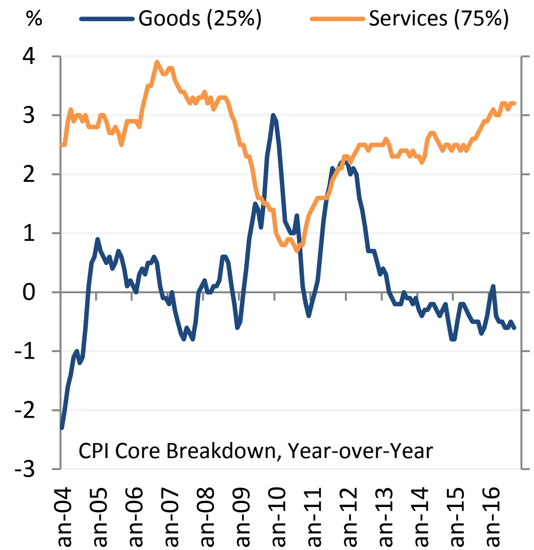


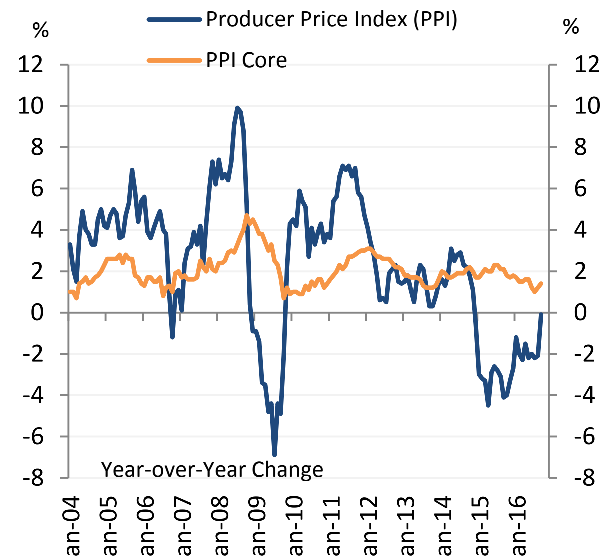




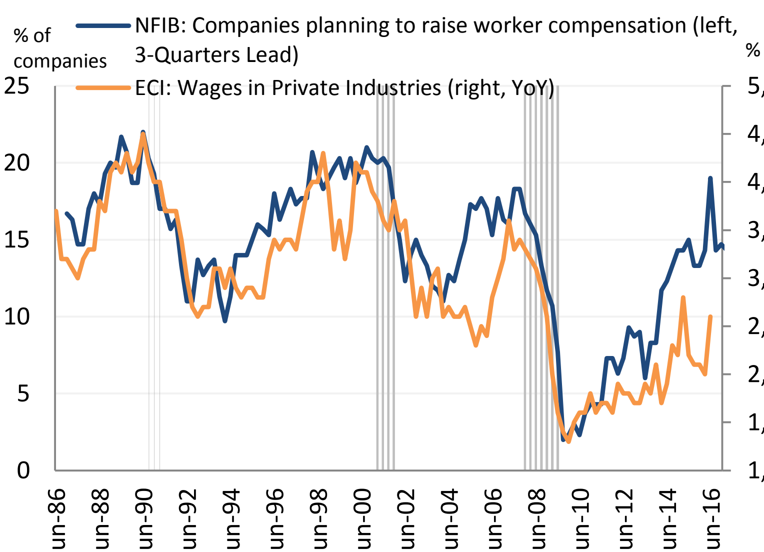
Wage gains improve, albeit not yet sufficiently to provide a substantial boost to inflation

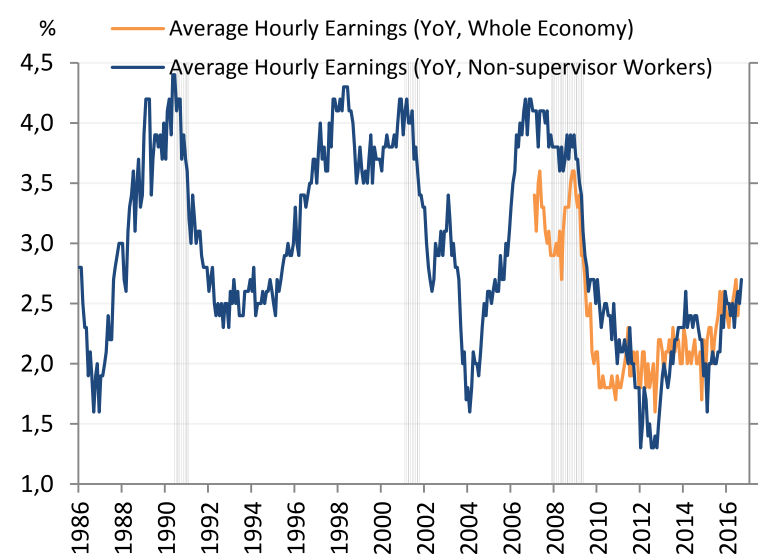






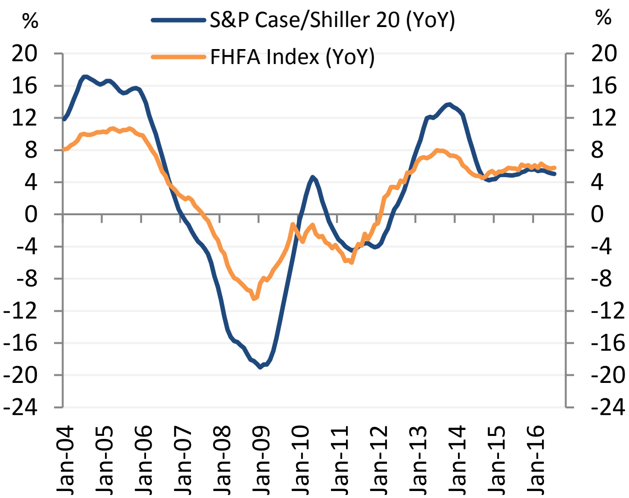
PCE Core: Fed's preferred measure to gauge inflation developments

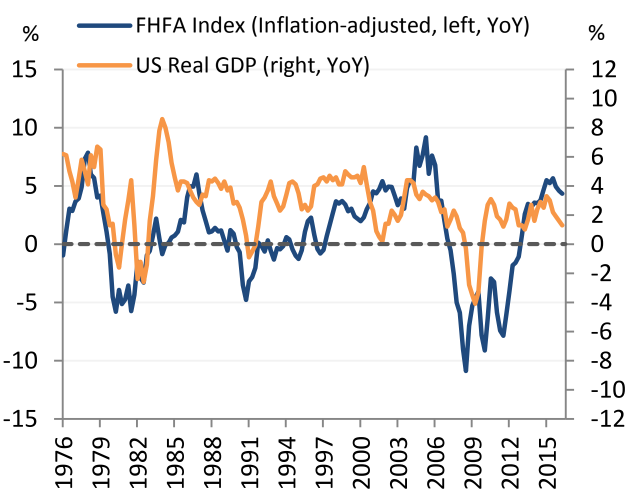




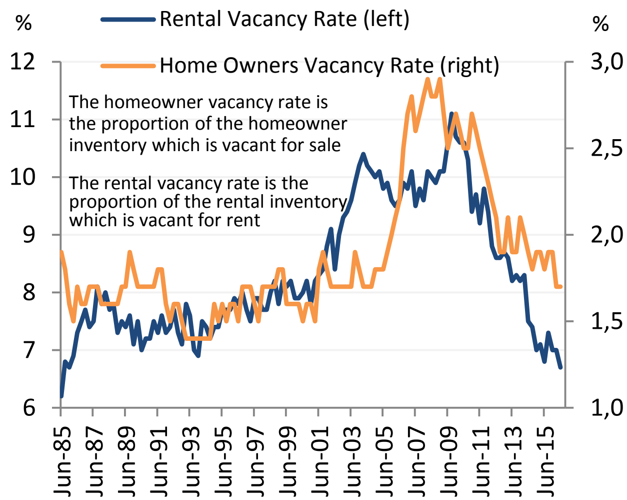
The housing market recovery continues, albeit posting some signs of moderation lately

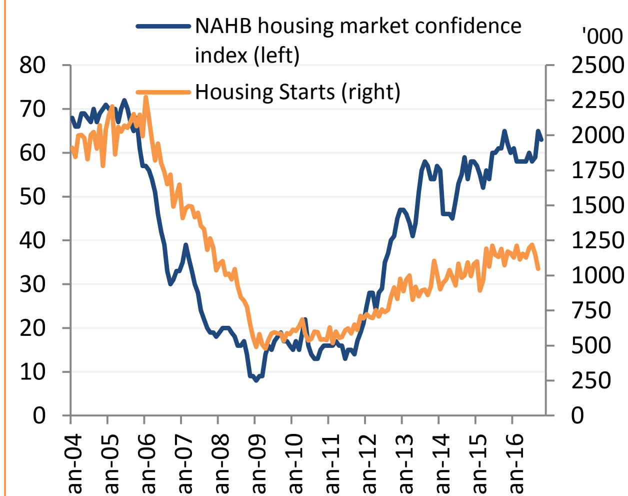
Prices



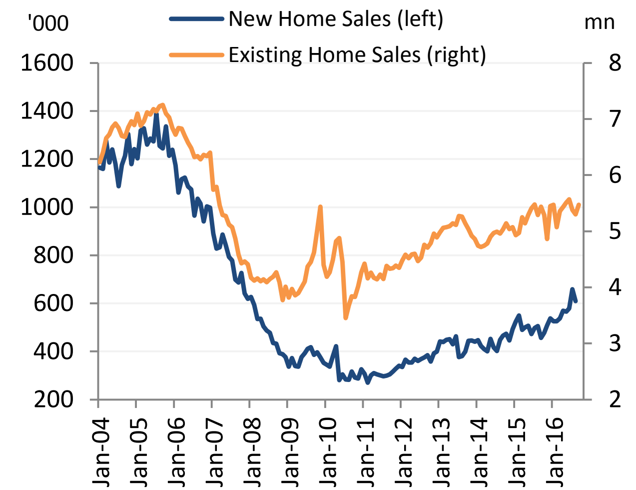


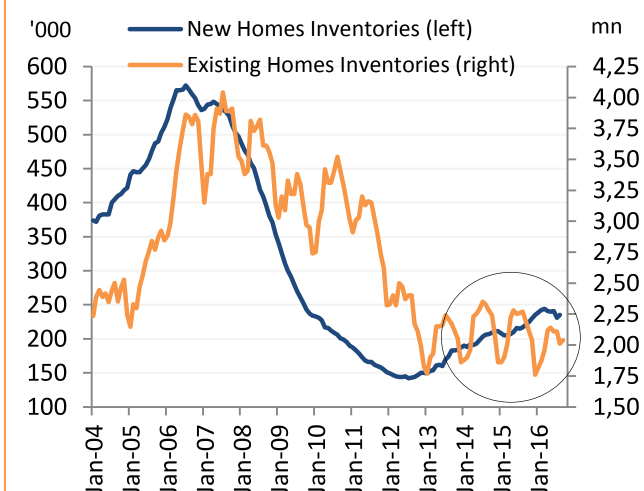
Vacancy Rates & Starts



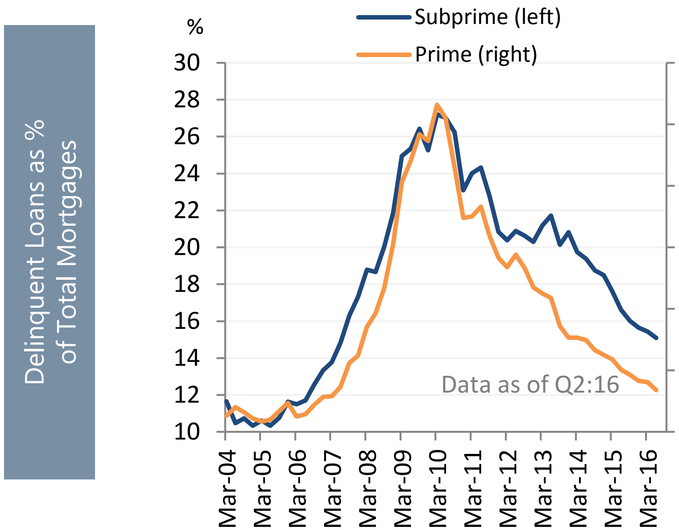


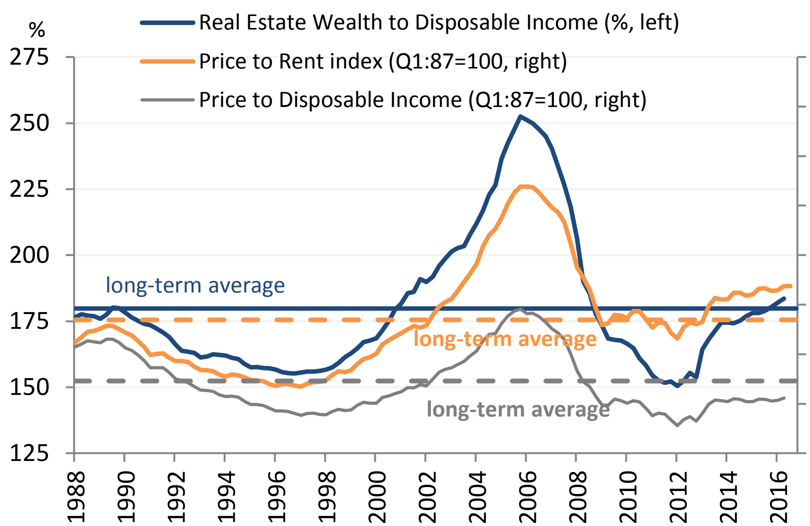
Sales & Inventories

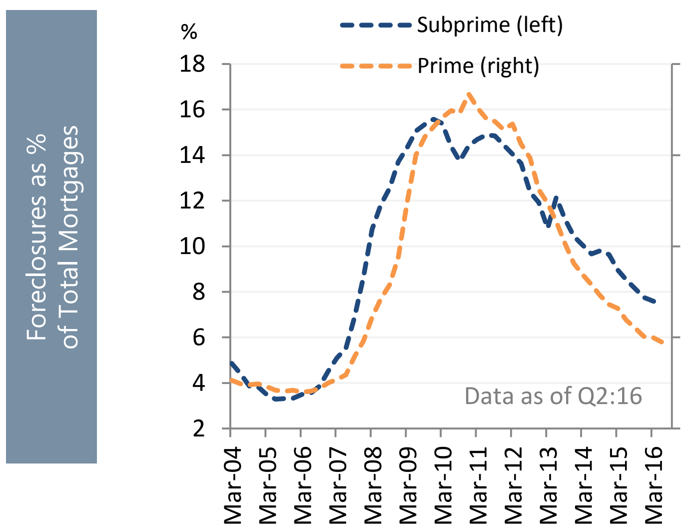


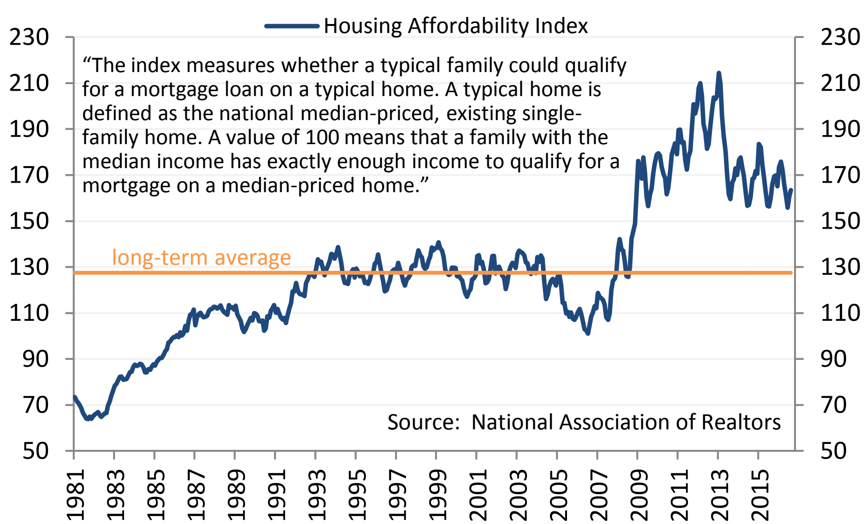


House valuations continue to increase above l-t averages



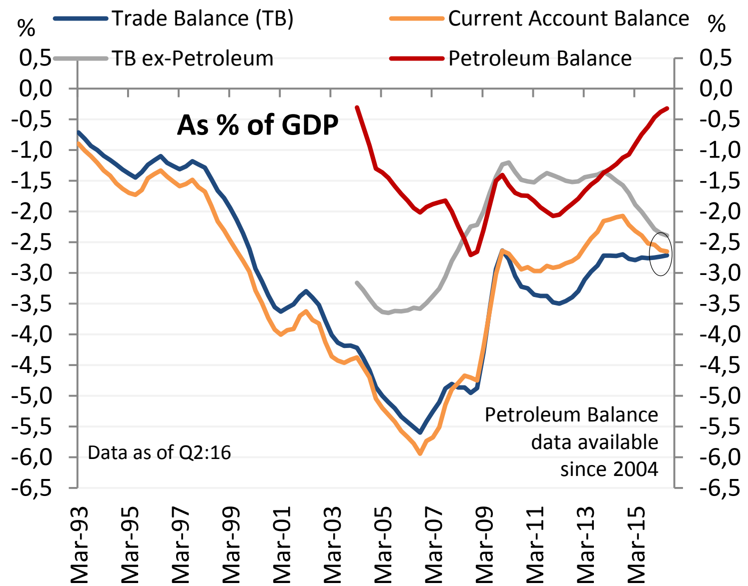


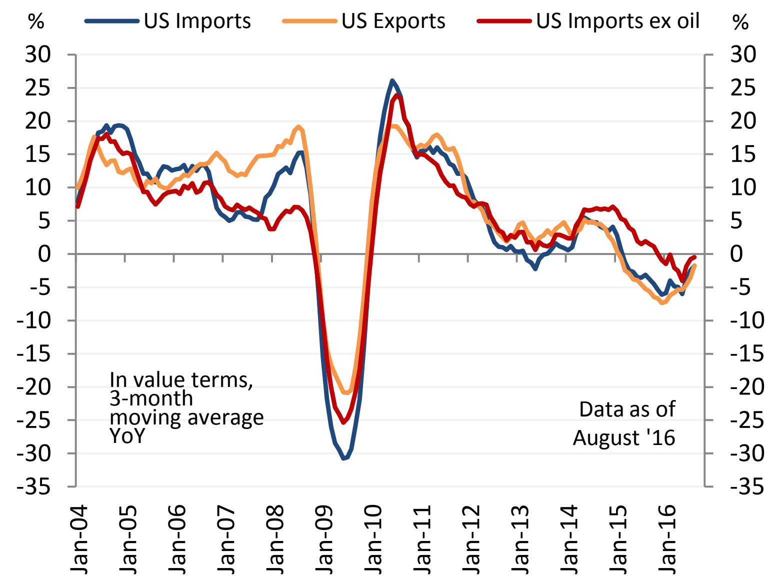


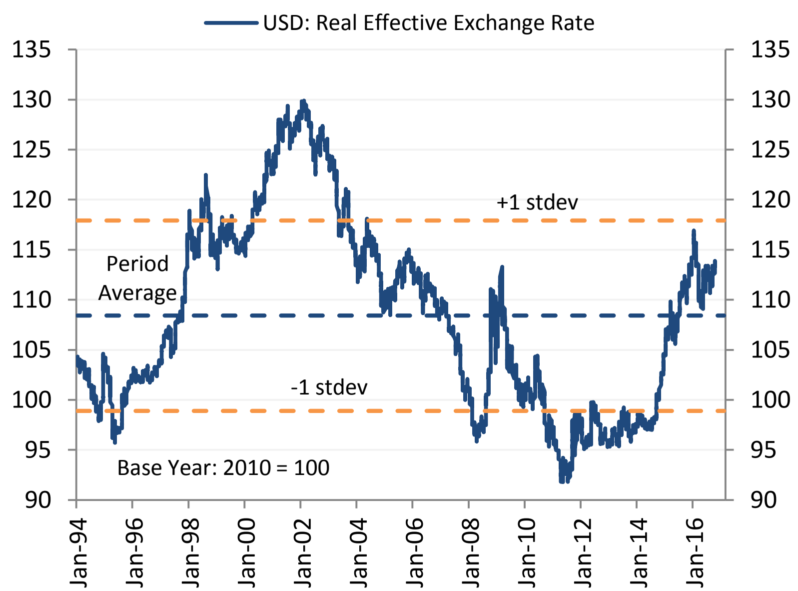


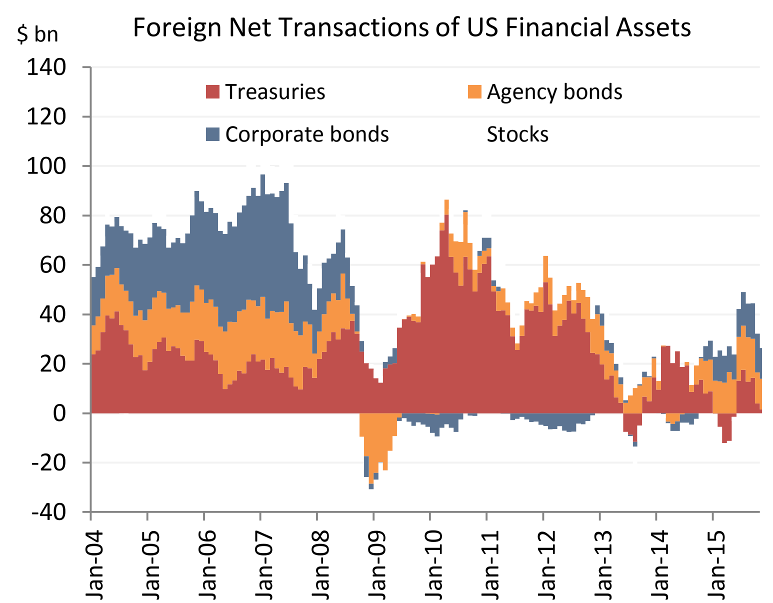
Source: Mortgage Bankers Association, Delinquencies are the total of 30, 60 and 90 days past due mortgage loans

The stabilization of external demand amid a range-bound USD supported US exports

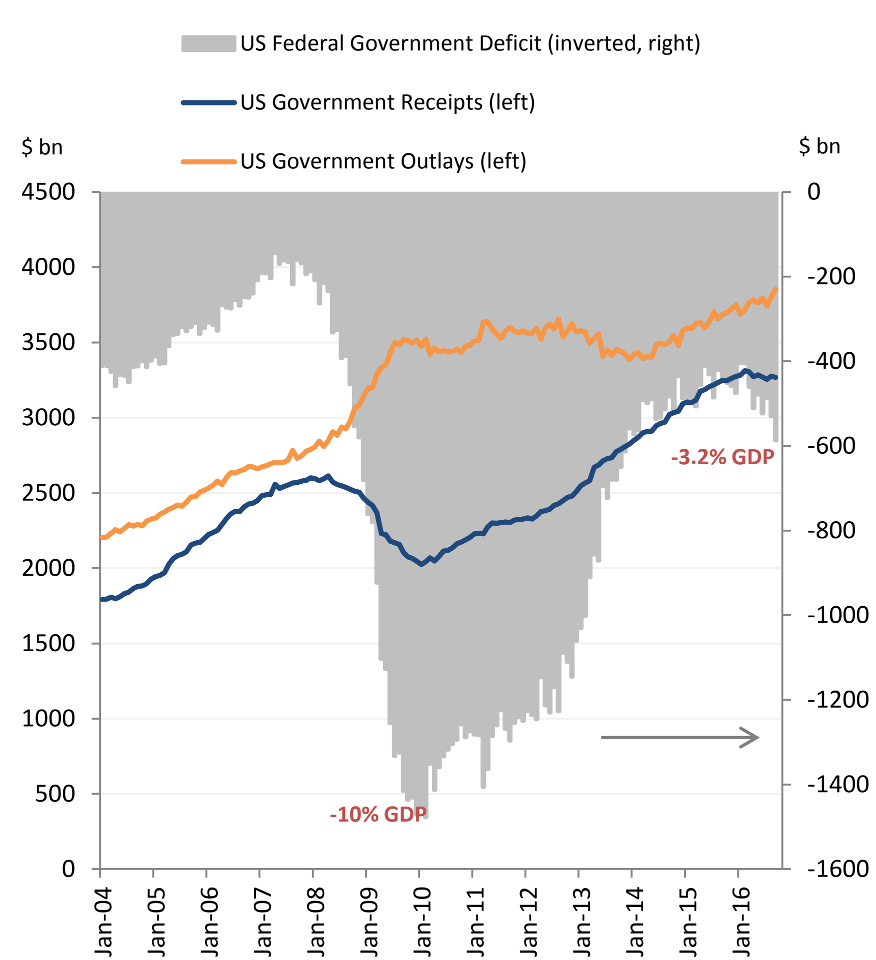




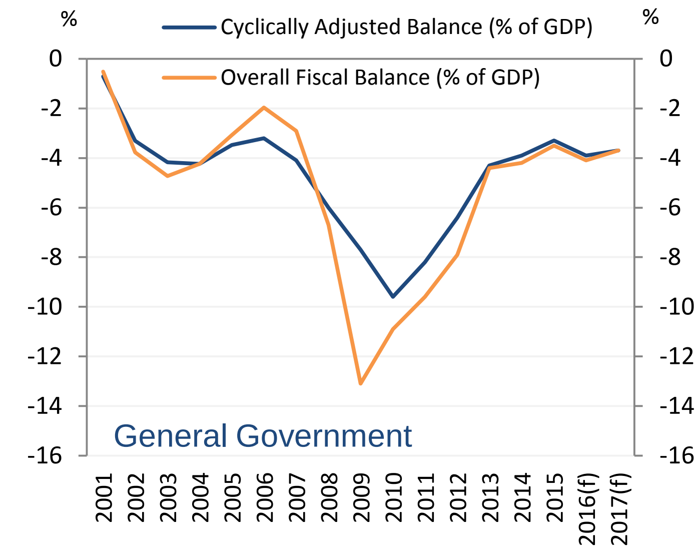




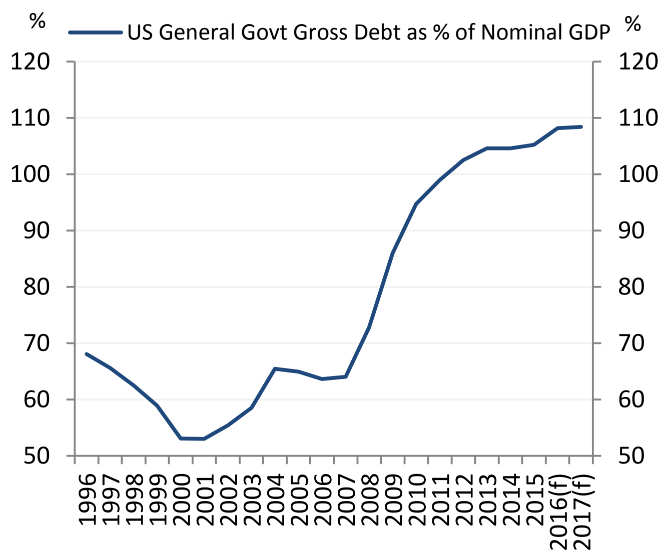
The Federal budget deficit will increase for the first time since 2009 in FY:16 (3.2% of GDP from 2.5% of GDP in FY:15)



Source: Congressional Budget Office (CBO) as of August 2016, Federal Government statistics, data appear as 12-month rolling sums

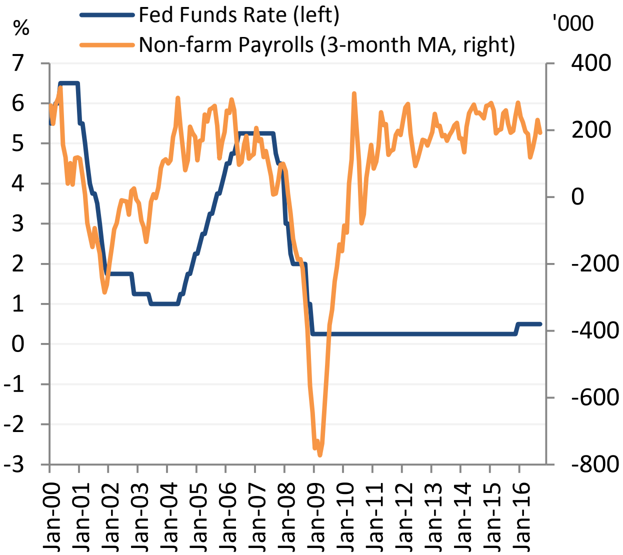


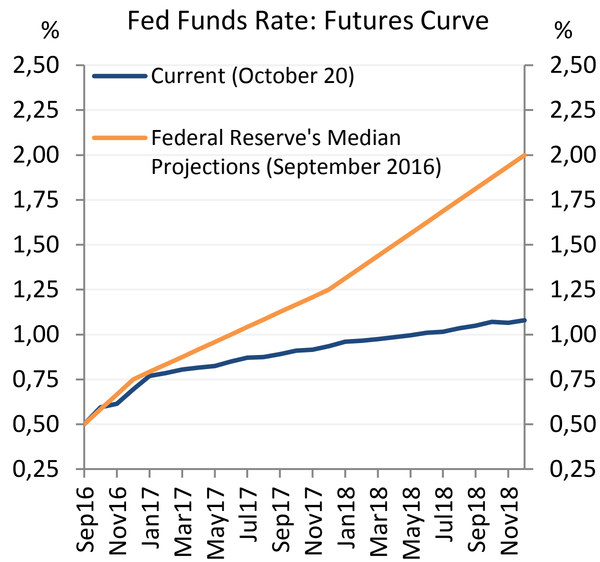
Source: IMF Fiscal Monitor, October 2016

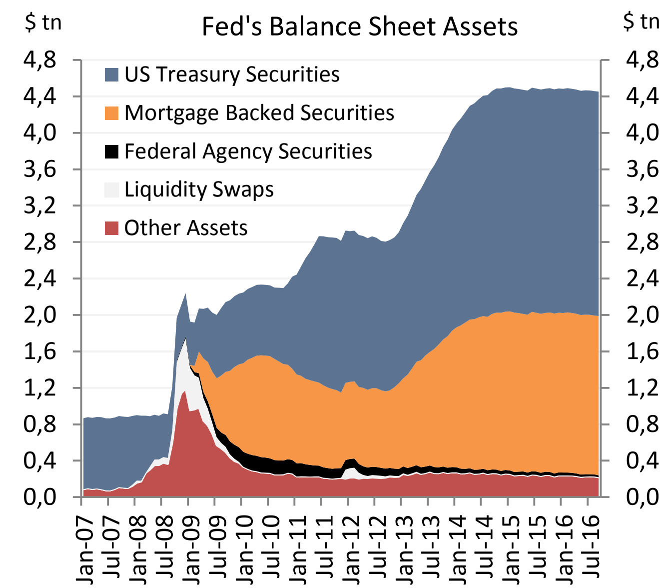


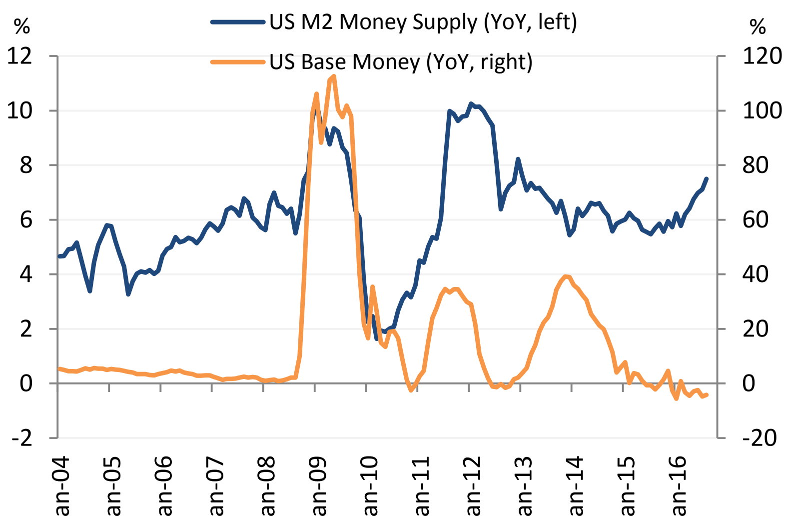
Source: IMF Fiscal Monitor, October 2016

The Fed turned more dovish, expecting only 3 rate hikes by end-2017 (vs 5 hikes in June)

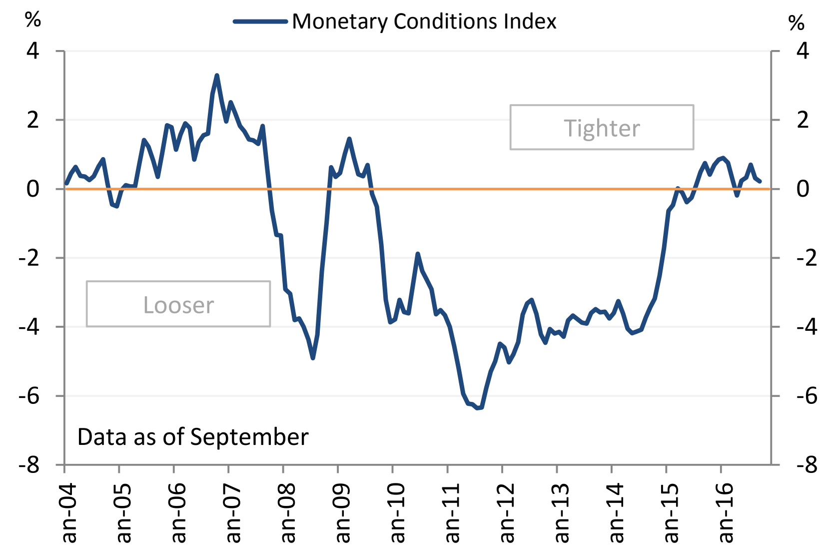






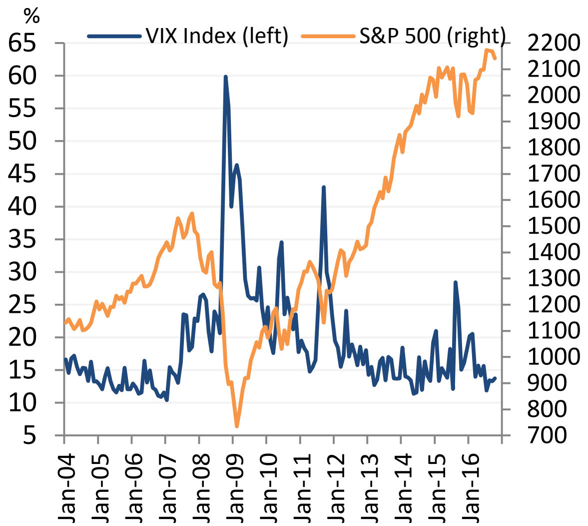


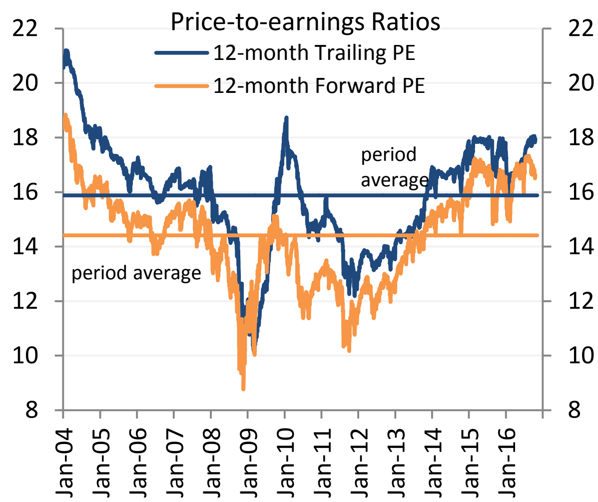
The Base Money is defined as the sum of currency in circulation and reserve balances (deposits held by banks in their accounts at the Fed



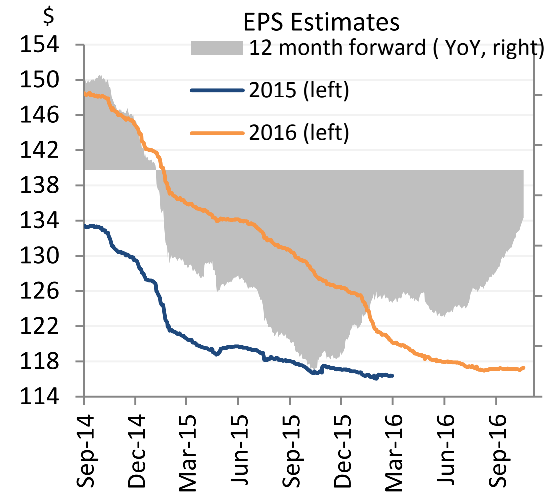
Monetary Conditions Index is a simple composite index of Real Short Term Rates (Libor less CPI) & Real Effective Exchange Rate

2016 EPS estimates stabilized, as the drag from the energy sector faded, while the S&P 500 has been range-bound recently

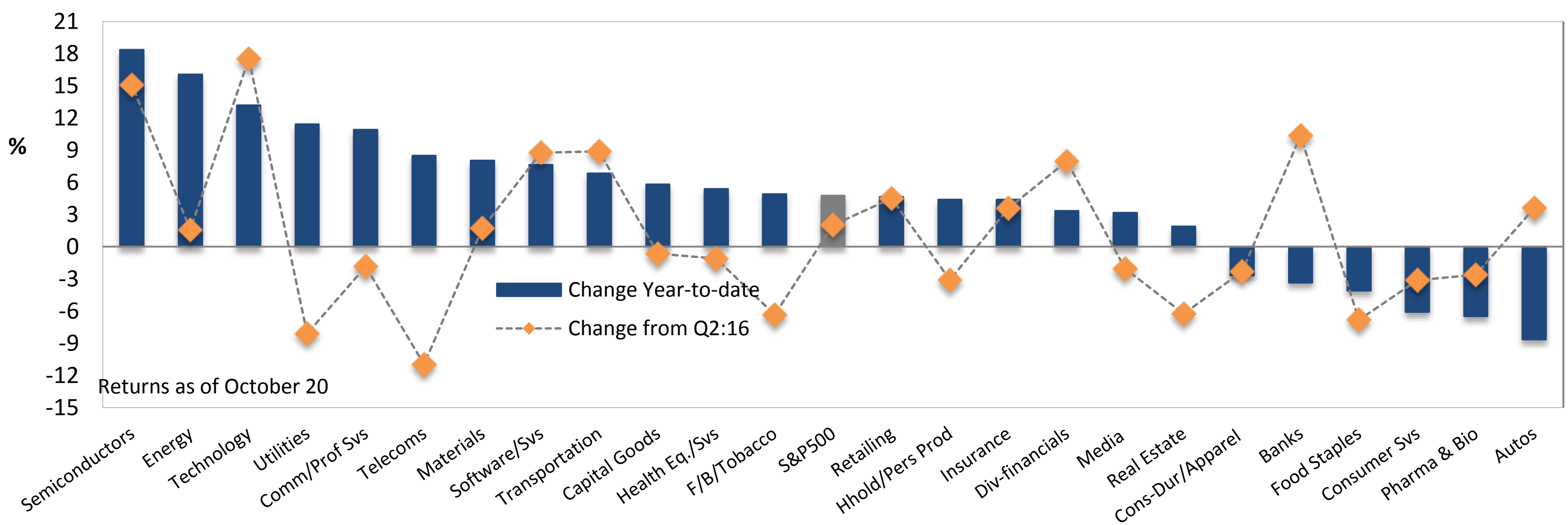




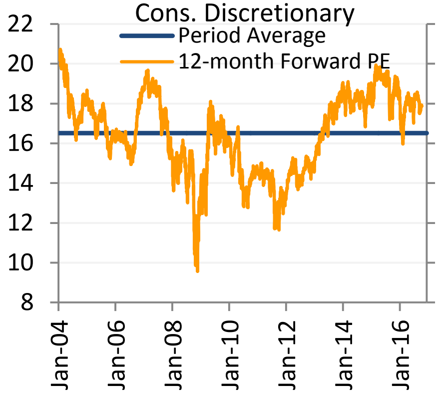
Source: Factset

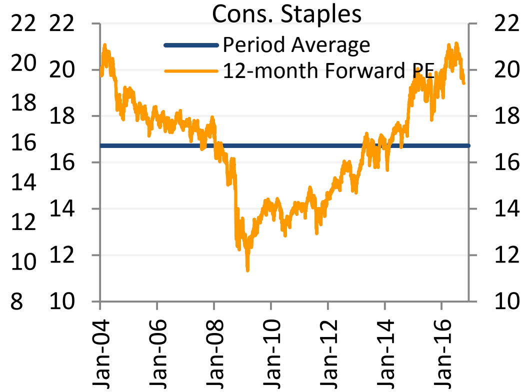


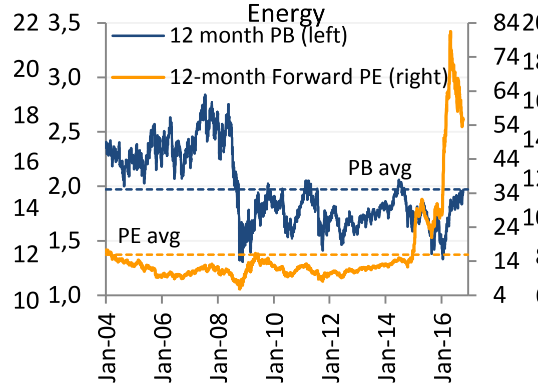
Source: Factset

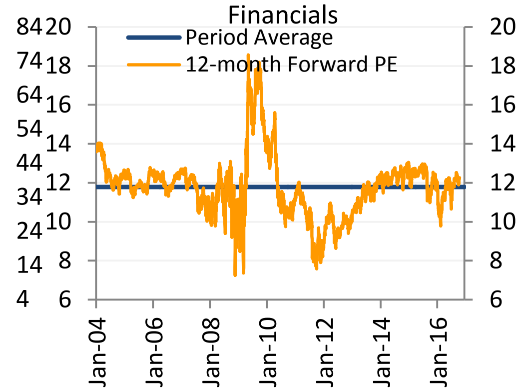


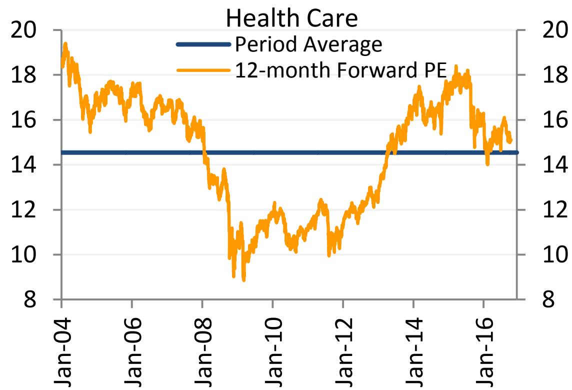
US Sectors Valuations

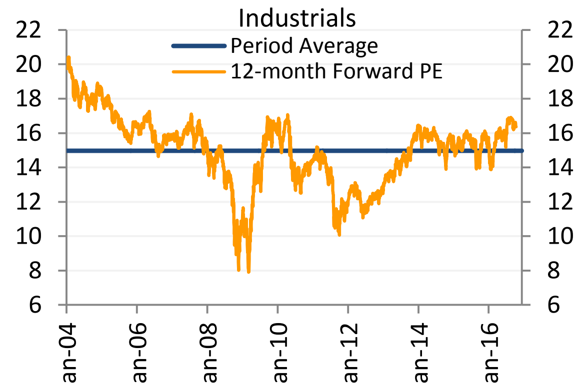


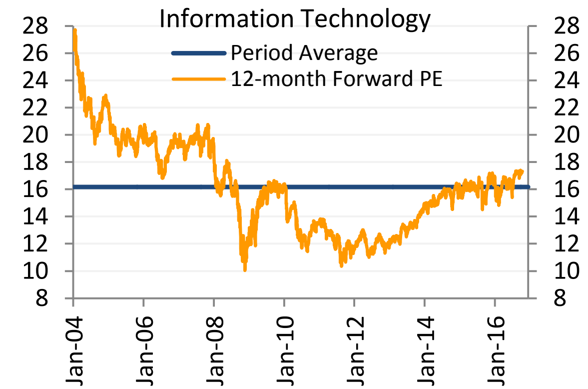


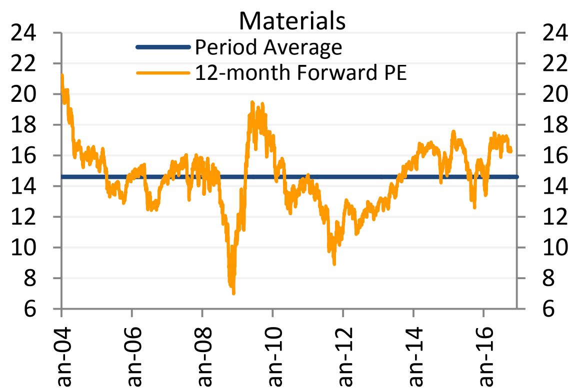


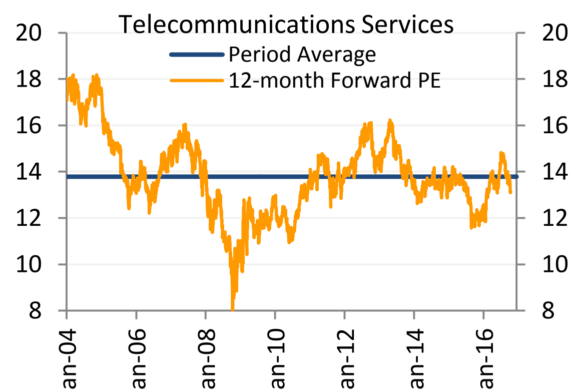


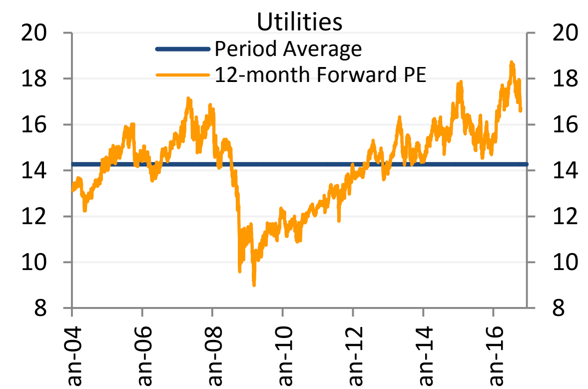




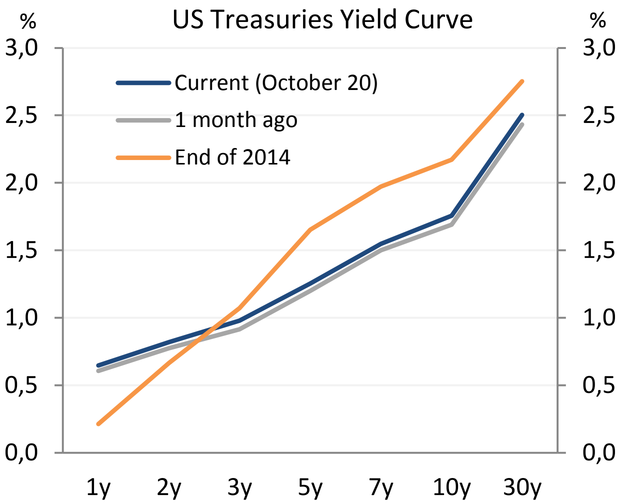


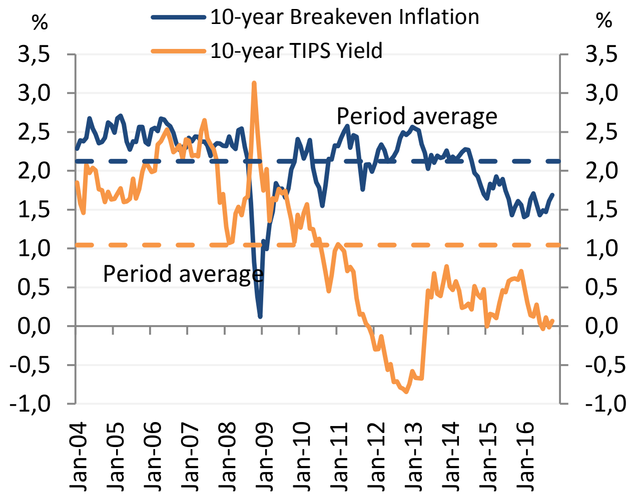


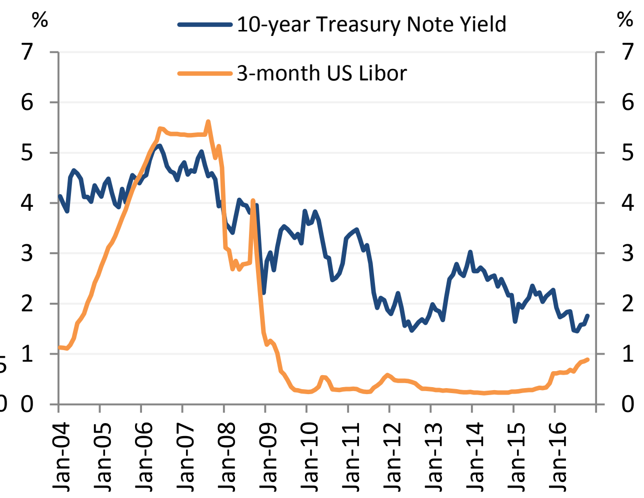


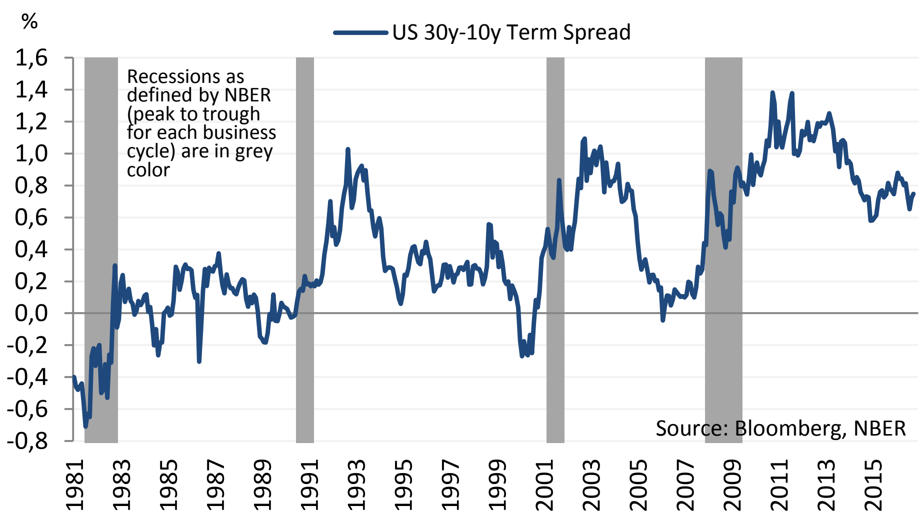


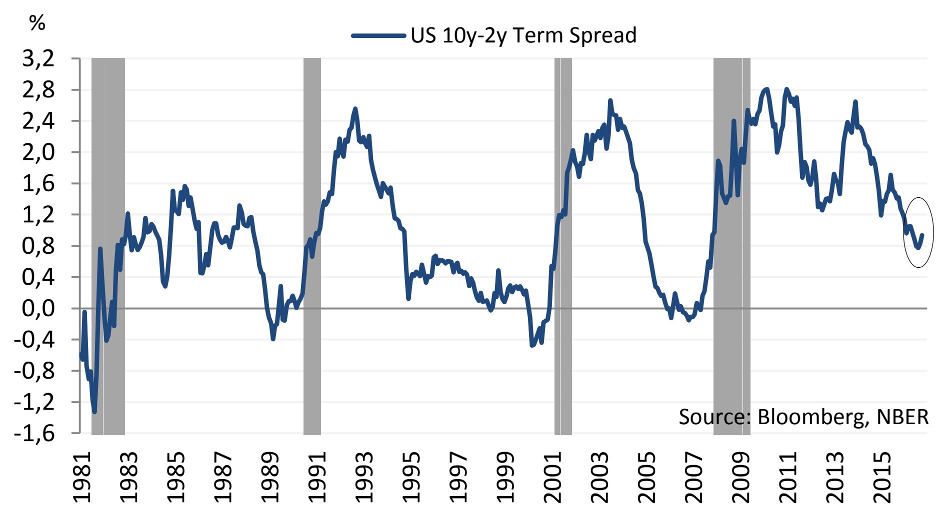
UST yields increased since Q2, albeit from exceptionally subdued levels, while the 10/2 spread remains close to its lowest level since 2007 (currently: 94 bps)





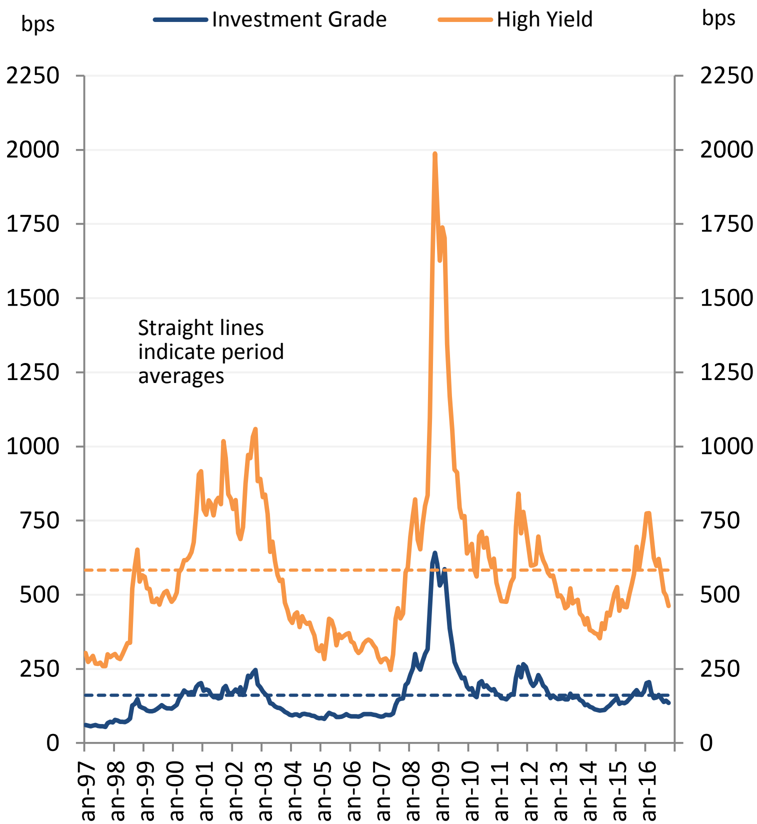






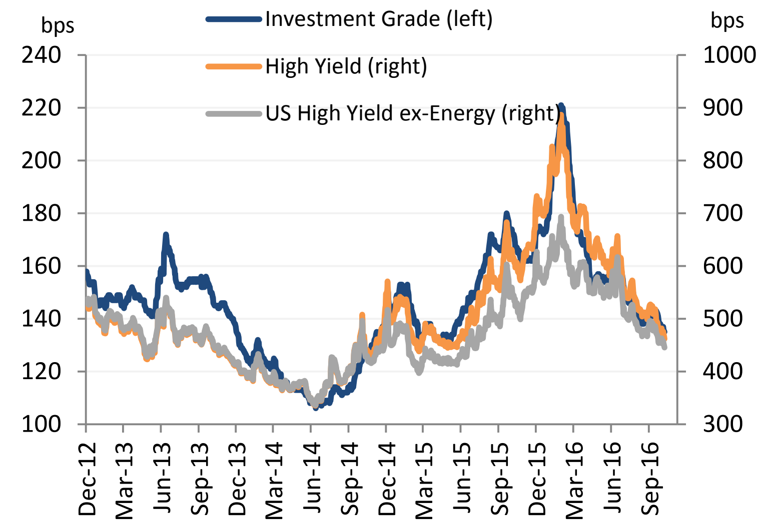
Yield hunting and easier financial conditions led US corporate spreads to decline since Q2. IG fell 27 bps, while HY over-performed (-159 bps) led by the energy sector (-274 bps)

Corporate Bond Spreads

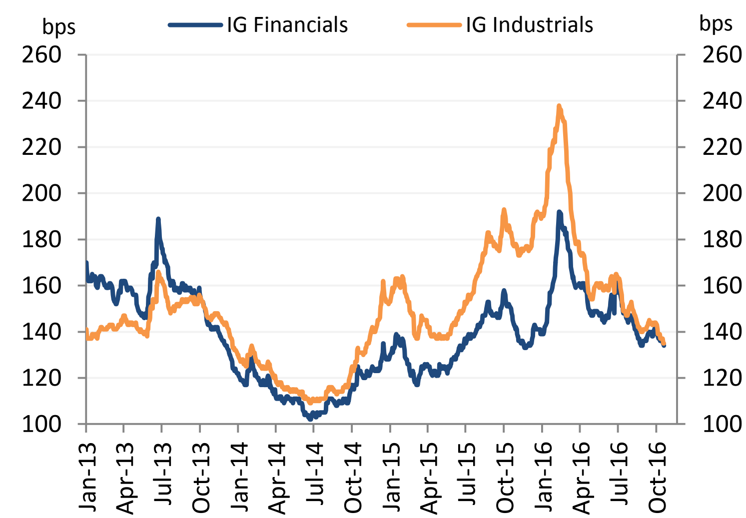


Source: Bank of America / Merrill Lynch US Corporate Bond Index (IG), US High Yield Master II (HY)

Short-term View



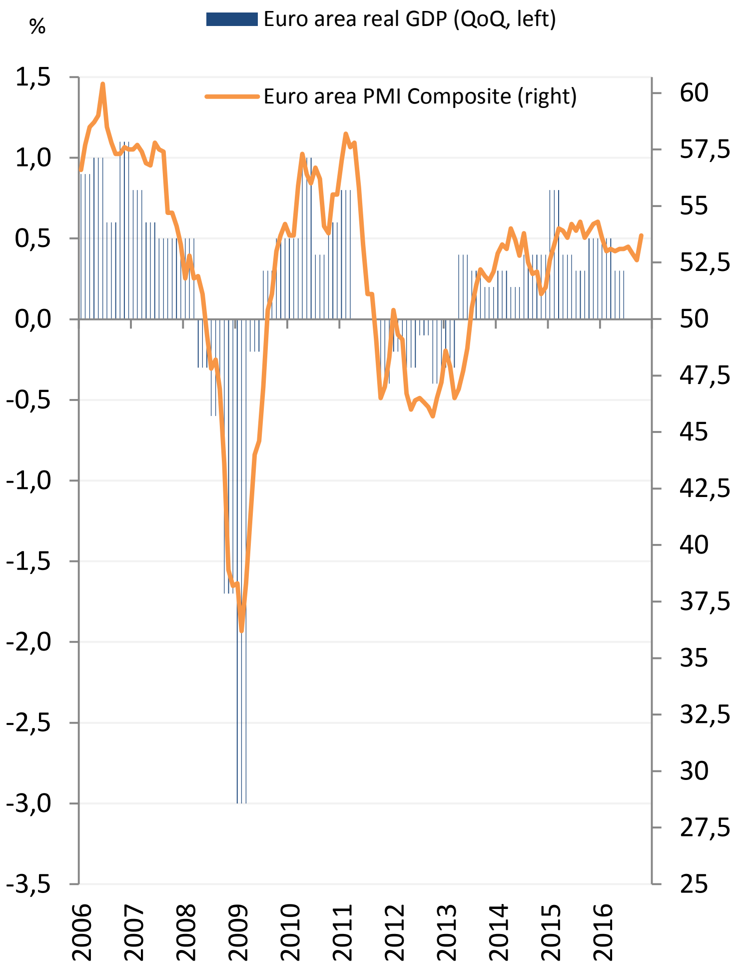
IG Financials/Industrials



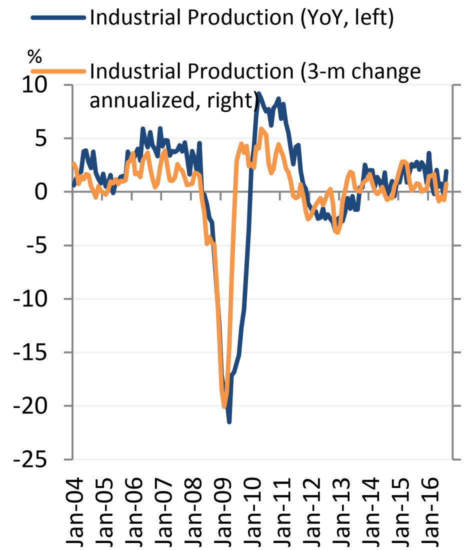
Euro Area

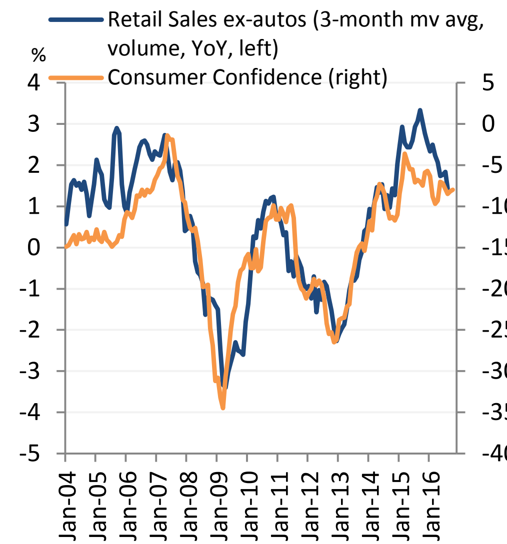
- The euro area recovery slowed in Q2, with real GDP increasing by 1.2% qoq saar in Q2:16, down from 2.1% in Q1:16. In H2:16, growth should remain subdued, supported by consumer spending and a more neutral fiscal policy.
- Households' disposable income should benefit from stronger employment gains (+1.4% yoy in Q2:16) and improving wages (+0.9% yoy in Q2:16). Retail sales (nominal) rose to 1.6% qoq saar, so far, in Q3:16, from 0.9% qoq saar in Q2:16. Moreover, consumer confidence stood significantly above l-t averages in Q3:16.
- Business investment should continue to recover in H2:16, on the back of exceptionally low funding costs, rising capacity utilization levels (81.7% on average, so far, in 2016 compared with 81.3% in 2015) and improving domestic demand. Industrial production is up by c. 0.5% qoq saar in Q3:16 from -0.9% in Q2:16. Business surveys eased slightly in Q3:16, but entered Q4 on a strong footing (Composite PMI at 53.7, a ten-month high). For FY:2016, real GDP is expected at 1.7%, and to slow to 1.5% in 2017 (IMF, WEO 2016).
- The euro area fiscal stance has eased in 2016, mostly due to discretionary fiscal measures (tax cuts, reduced contributions for social security and increased expenditure related to the influx of refugees). Specifically, the cyclically-adjusted primary surplus is expected to narrow by 0.5 pps to 0.6% in 2016, and by 0.1 pp to 0.5% in 2017, according to IMF estimates (WEO, October 2016).
- Credit conditions remain positive, albeit distressed bank balance sheets could hold back credit creation. Euro area bank loans to the private sector have been in positive territory for the past 18 months (+1.7% yoy in August) and growth for loans to non-financial corporations (NFCs) hovers at a 5-year high (+1.9% yoy). Year-to-date, new banks loans to NFCs have averaged +€7.9 bn from +€1.4 bn in 2015 and -€5.7 bn in 2014.
- The ECB has maintained its "wait-and-see" stance (MRO rate at 0.0%, Deposit rate at -0.4%, asset purchases of €80bn/month). The outlook for inflation and GDP remains broadly unchanged, as the Brexit-related drag is likely to be substantially less than initially expected. The ECB expects inflation at 0.2% in 2016 and 1.2% in 2017. Note that headline inflation has strengthened (+0.4% yoy in September) and is expected to increase towards 0.9% by year-end. Markets are increasingly focusing on the next meeting (December 8), as speculation exists that the ECB may start reducing its monthly bond purchases during the course of 2017.
- European politics remains a significant source of investor uncertainty. Italy's referendum in December, the likely start of UK exit talks from the EU in H1:17 and the upcoming elections in France (Q2:17) and in Germany (Q3:17) could disrupt the fragile euro area recovery. The ongoing refugee crisis could boost Eurosceptic populism as well. Though DBRS confirmed Portugal's credit rating at BBB-, a future downgrade of Portuguese government bonds would result in their losing their eligibility for the ECB's QE program.
- Following a disappointing H1:16 (EuroStoxx: -11%), euro area equities have recouped some of their losses in Q3:16 (+6%). Investor uncertainty, due to Brexit, has eased. Euro area banks overperformed in Q3:16 (+11%), as volatility declined and concerns for Italian banks moderated. After remaining stable at -0.12% in Q3:16 , the German 10Yr Bund yield has risen by c. 13 bps to positive territory (October 20) on the back of speculation that the ECB could begin tapering its QE purchases. The euro has gained ground by 1.3% in NEER terms, but mainly due to its gains against the GBP by 9.0% to €/0.91.

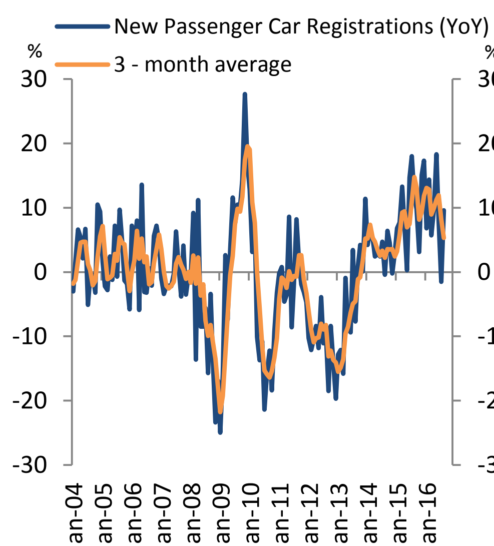
Domestic demand should find support from wage gains and improving employment conditions

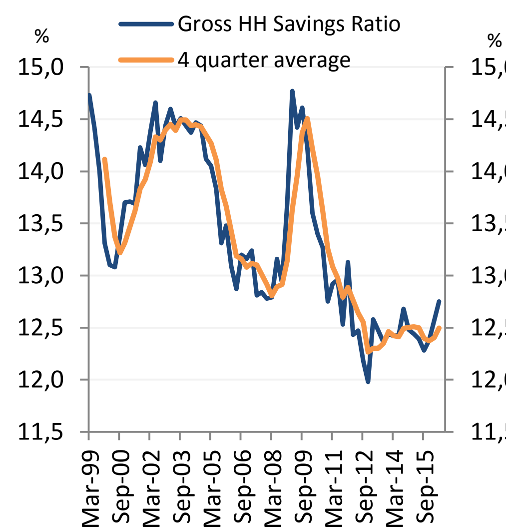


Above: GDP data as of Q2:2016, PMI data as of October 2016
Right: Industrial Production, Retail Sales & New Passenger Car Registrations data as of August 2016, Consumer Confidence as of October 2016
Source: Eurostat, Markit, Bloomberg









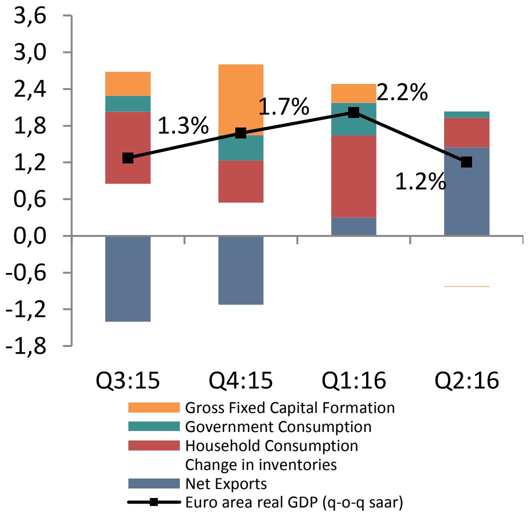
Source: Eurostat, data as of Q2:2016

GDP growth in Q3:16 is expected to be moderate to 1.6% qoq saar

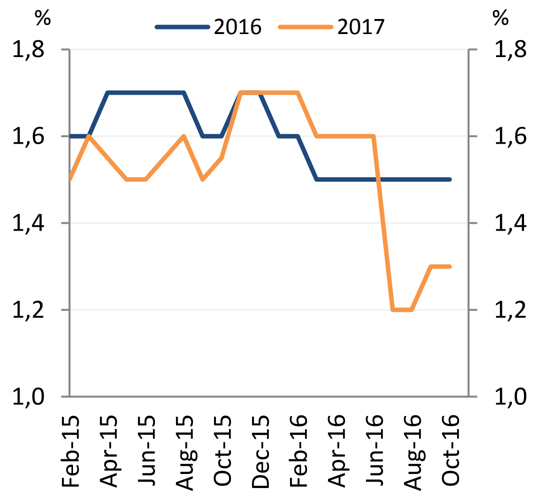
EA Real GDP Growth	2014	Q1:15	Q2:15	Q3:15	Q4:15	2015	Q1:16	Q2:16	Q3:16e	Q4:16e	2016e
GDP (YoY)	**1,1**	1,8	2,0	2,0	2,0	**1,9**	1,7	1,6	1,7	1,6	**1,6**
GDP (QoQ saar)	-	3,3	1,4	1,5	1,8	-	2,1	1,2	1,6	1,6	-
Private consumption (QoQ saar)	0,8	1,6	1,7	2,1	1,3	1,7	2,5	0,9	1,0	1,3	1,6
Government consumption (QoQ saar)	0,6	1,9	1,6	1,4	2,6	1,4	2,6	0,5	1,6	1,8	1,8
Investment (QoQ saar)	1,5	6,5	0,5	2,1	5,9	2,9	1,5	-0,1	2,7	1,5	2,2
Inventories contribution (QoQ saar)	0,2	0,1	-0,9	1,0	0,4	-0,1	-0,4	-0,8	0,1	0,1	-0,1
Net Exports contribution (QoQ saar)	0,0	0,6	1,0	-1,3	-1,1	0,2	0,3	1,4	0,1	0,2	0,1
Exports (QoQ saar)	4,4	10,4	4,9	1,5	2,8	6,1	0,1	4,5	1,7	2,6	2,2
Imports (QoQ saar)	4,8	9,8	3,0	5,0	5,7	6,1	-0,6	1,4	1,6	2,4	2,3

Source: Eurostat, Bloomberg, NBG Estimates

GDP Contributions (%)

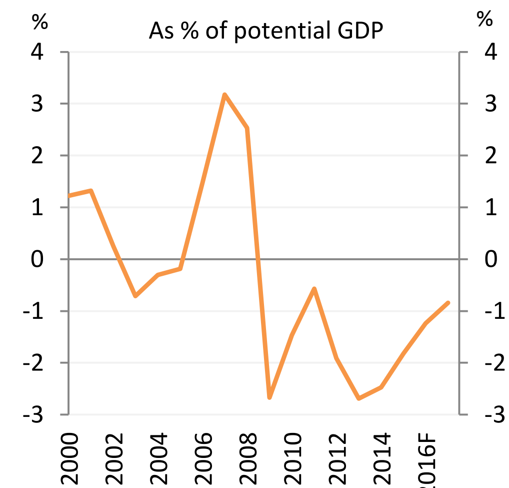


GDP Forecast Evolution



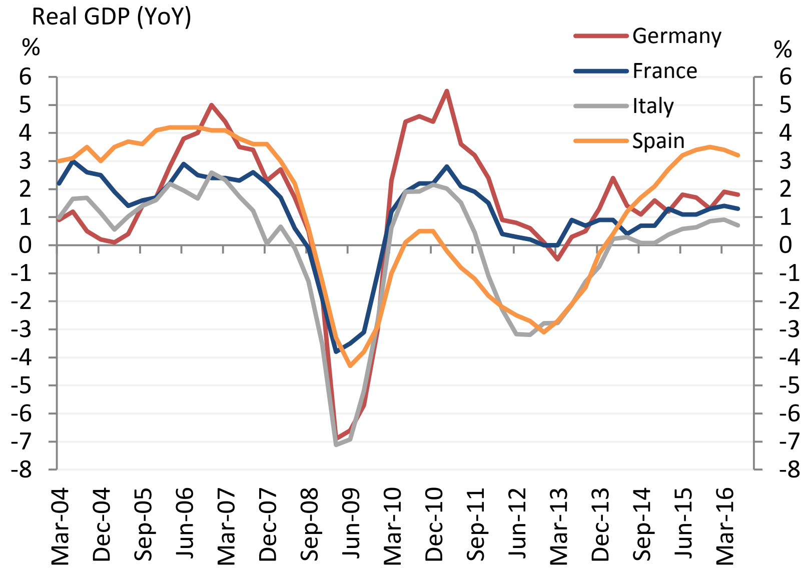
Source: Bloomberg Consensus

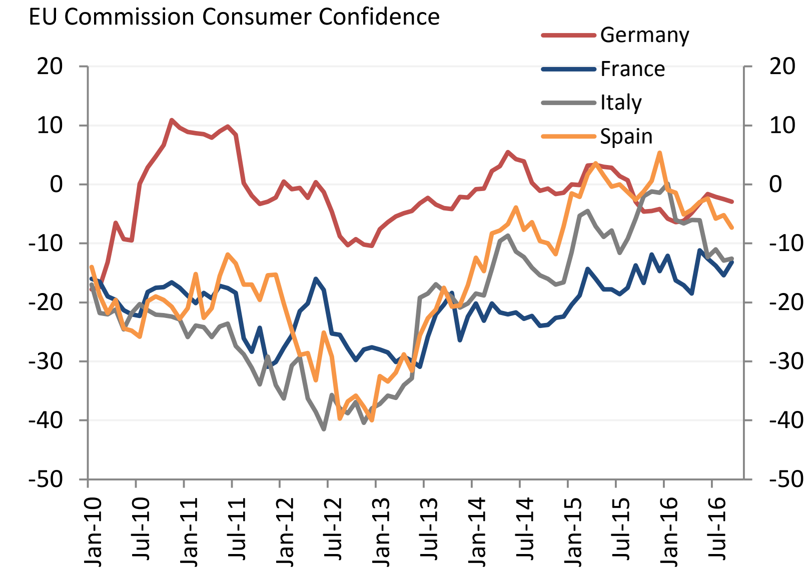
Output Gap

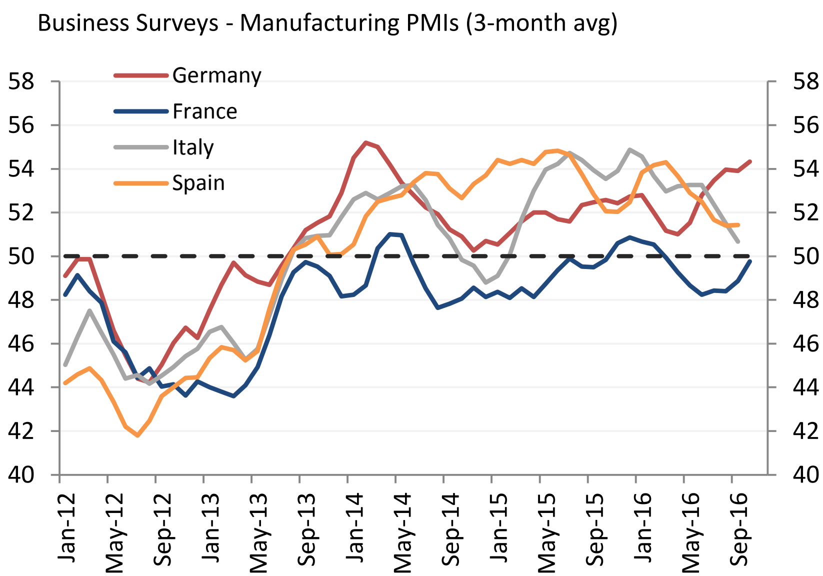


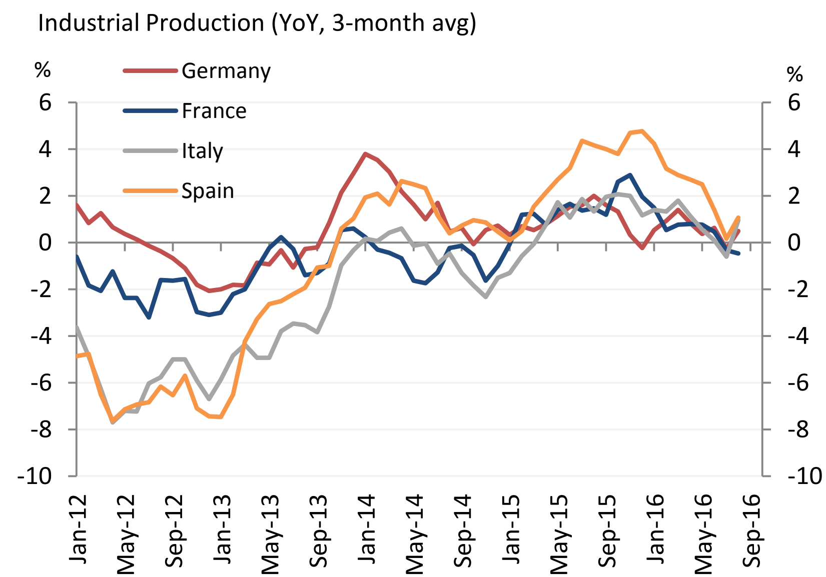
Source: IMF

Growth remains uneven across major countries, with Italy's downward trend in manufacturing PMI and consumer confidence standing out

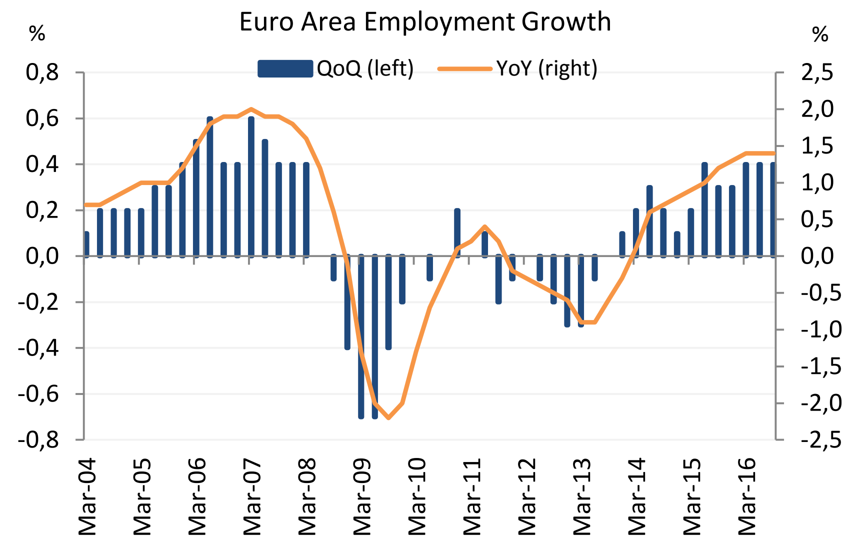


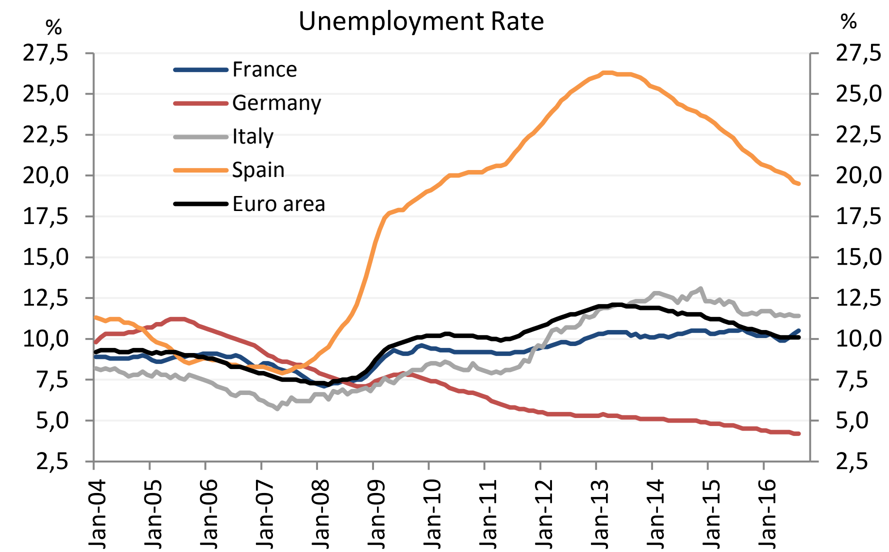


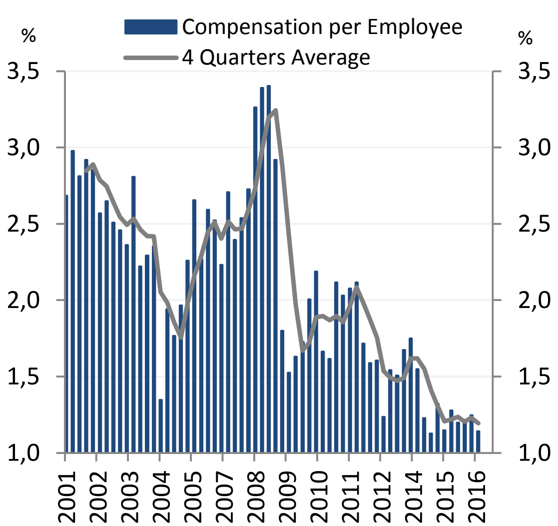


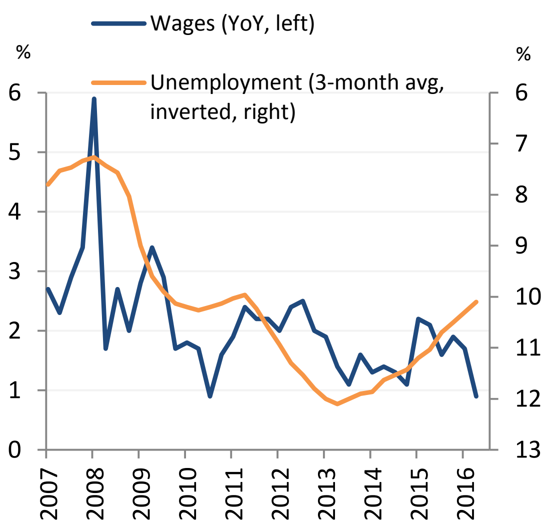


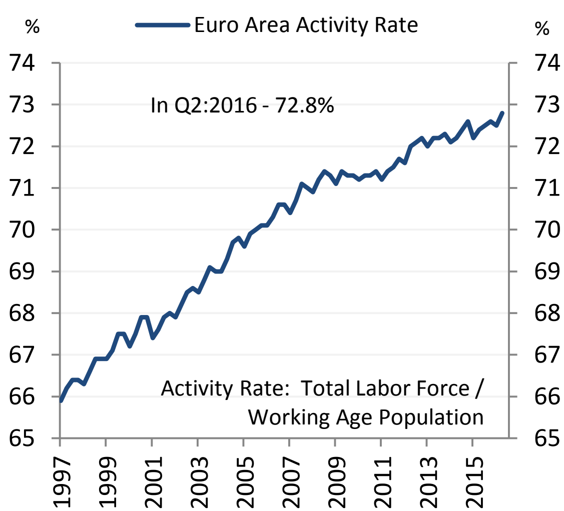
The gradual decline in the unemployment rate continues (10.1% in August). Wage growth, albeit positive, remains modest







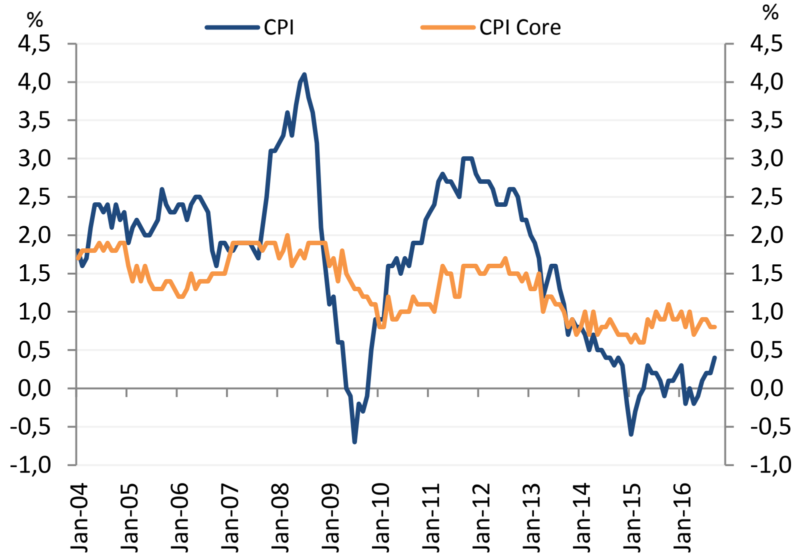


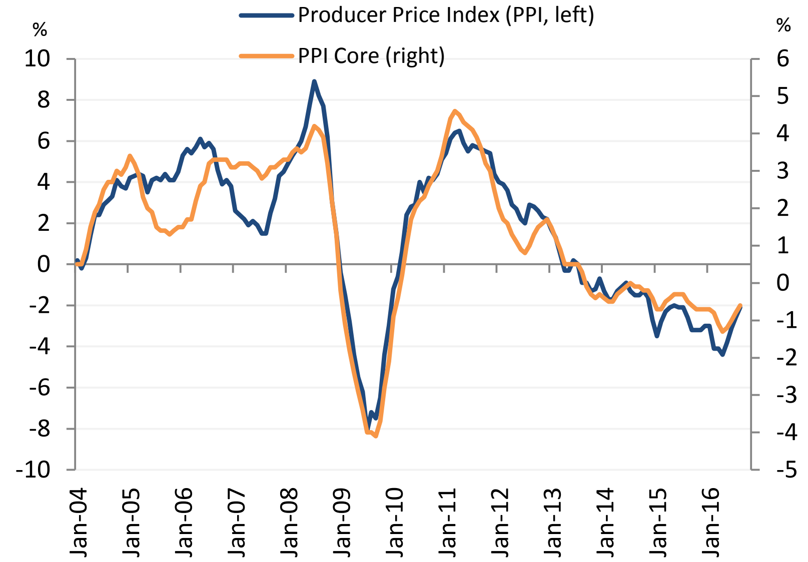


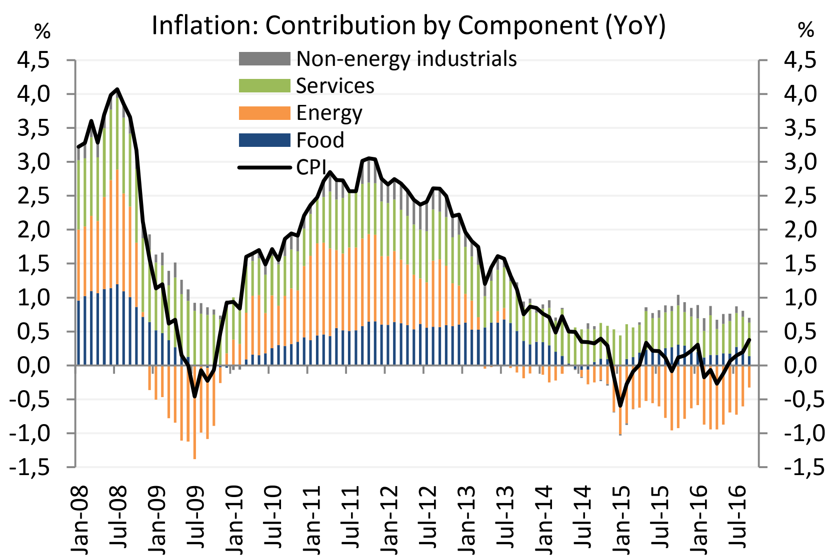
Source: ECB, Compensation per Employee: the total remuneration that is payable to employees (salaries, bonuses, overtime payments and employers' social security contributions, divided by the total number of employees / Wages: indicator of Negotiated wage rates

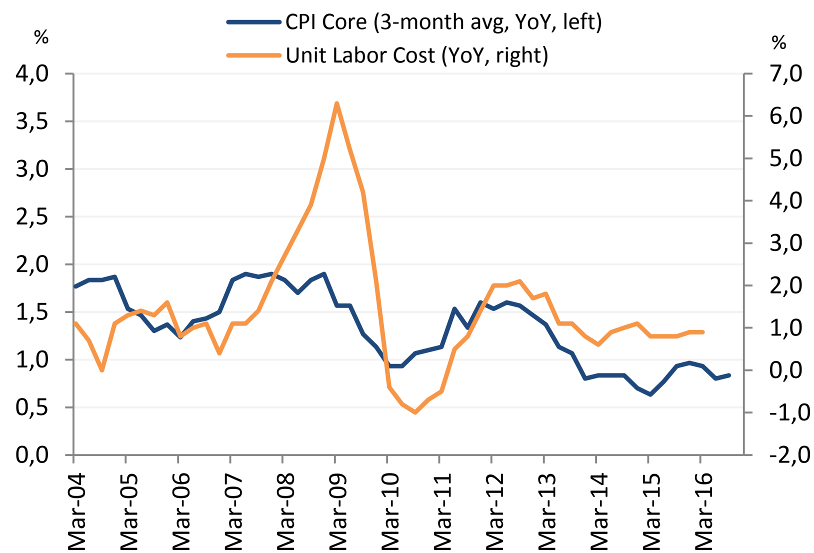
Source: ECB, Activity Rate: Total Labor Force / Working Age Population

Inflation has accelerated recently to the highest rate since November '14 (+0.4% yoy in September)



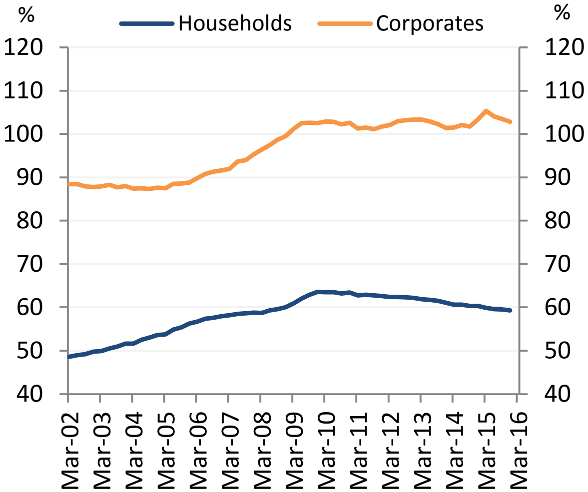






Credit conditions remain supportive, with the growth of loans to the private sector increasing to an almost 5-year high of 1.7% yoy in August (since November 2011)

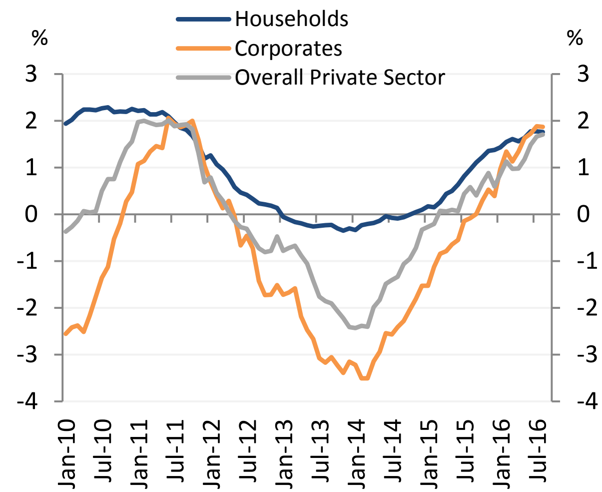
Private Debt* as % of GDP



*Private sector (Households and non-financial corporations) includes bank loans & corporate bonds, data as of Q4:15

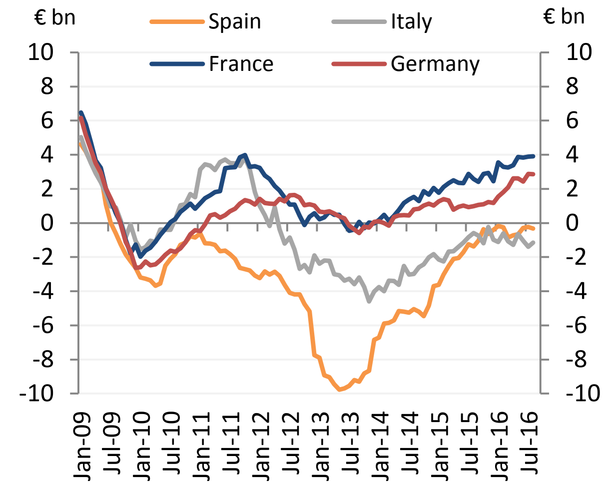
Source: Bank for International Settlements

Euro area Banks: Loans to the Private Sector



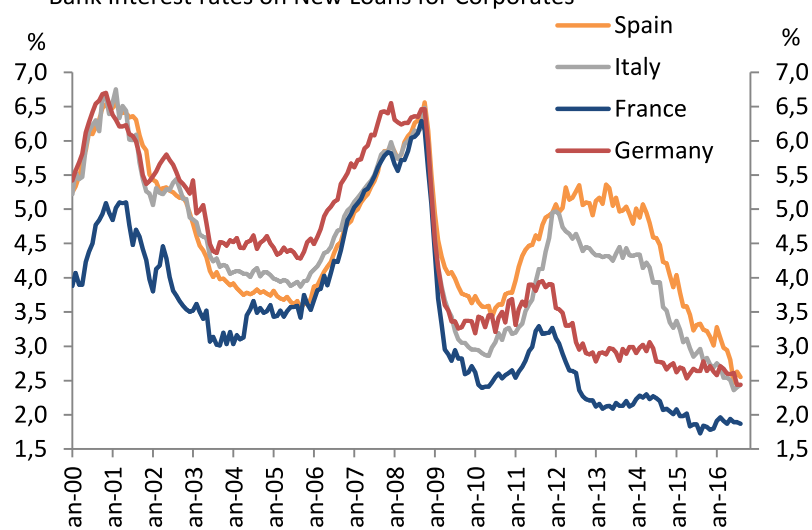
Source: ECB, data as of August 2016 / Adjusted for Sales & Securitization, YoY

Euro area Banks: Loans to Corporates



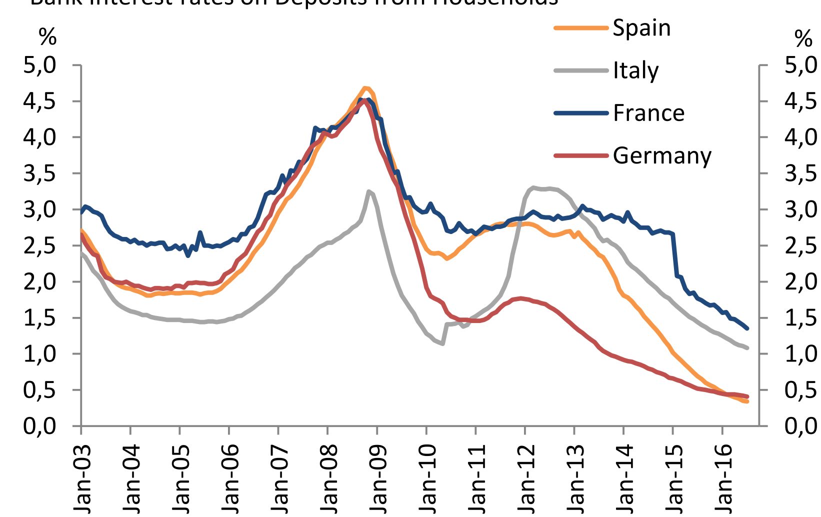
Source: ECB, data as of August 2016 / flows, 12-month moving average

Bank Interest rates on New Loans for Corporates



Source: ECB, data as of August 2016 / Interest rates on loans up to €1mn

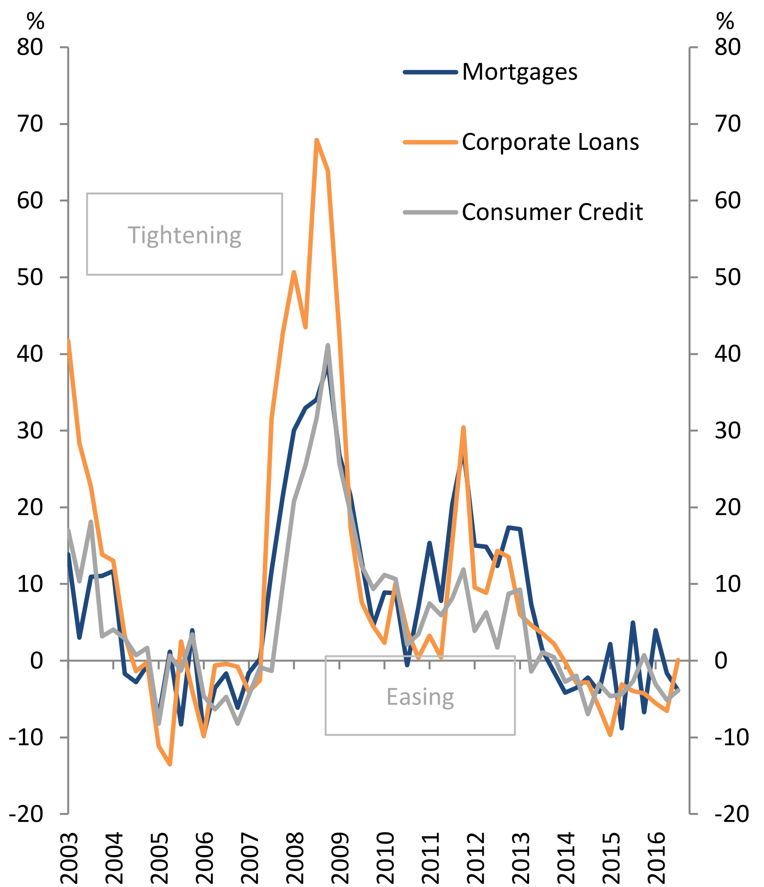
Bank Interest rates on Deposits from Households



Source: ECB, data as of August 2016 / Interest rates on deposits with agreed maturity up to 2 years

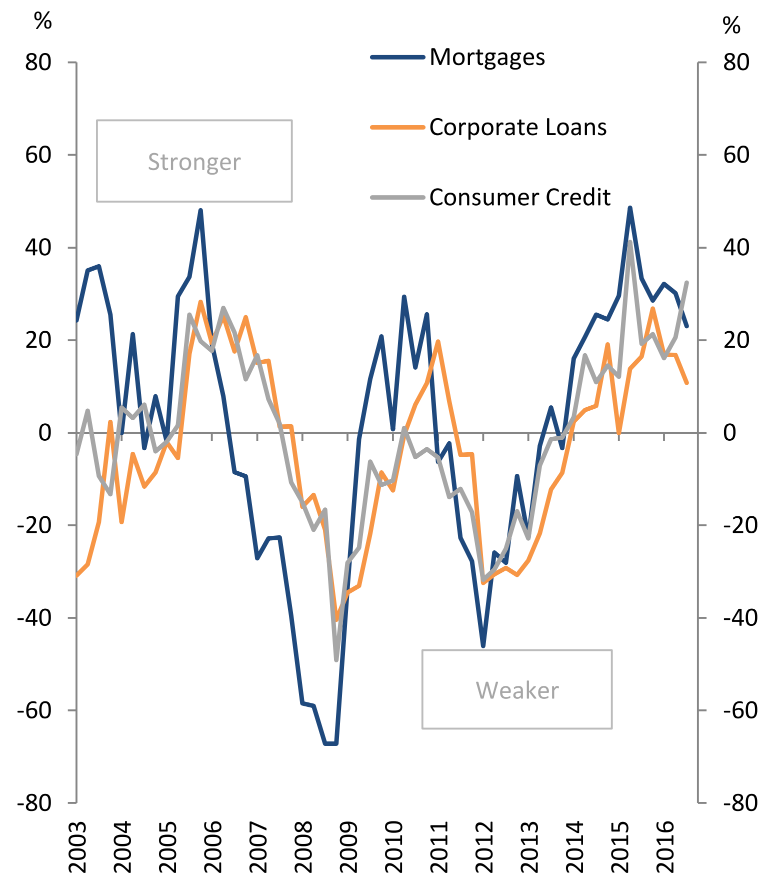
The ECB Bank Lending Survey for Q3 revealed that credit standards stop improving, albeit remaining in "net ease mode" for households. Demand for loans remain strong

Net % of Banks reporting tightening in Credit Standards



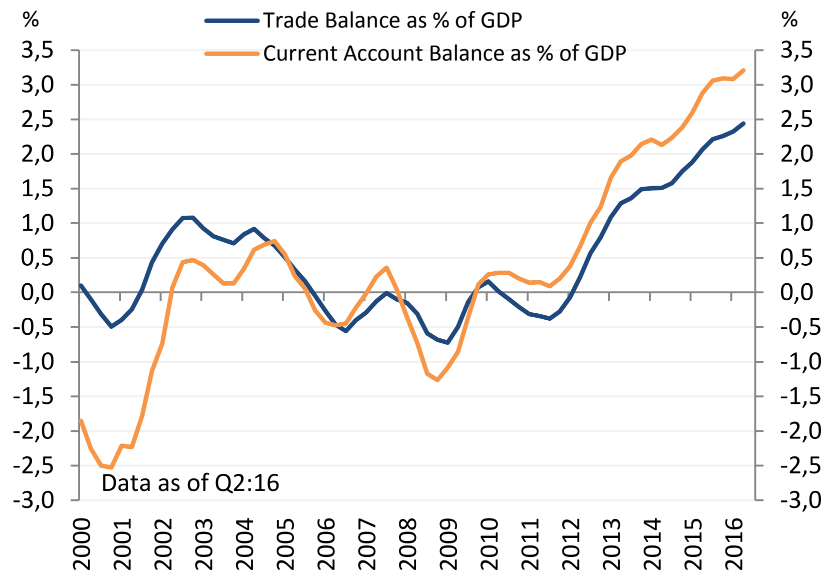
Source: ECB Bank Lending Survey

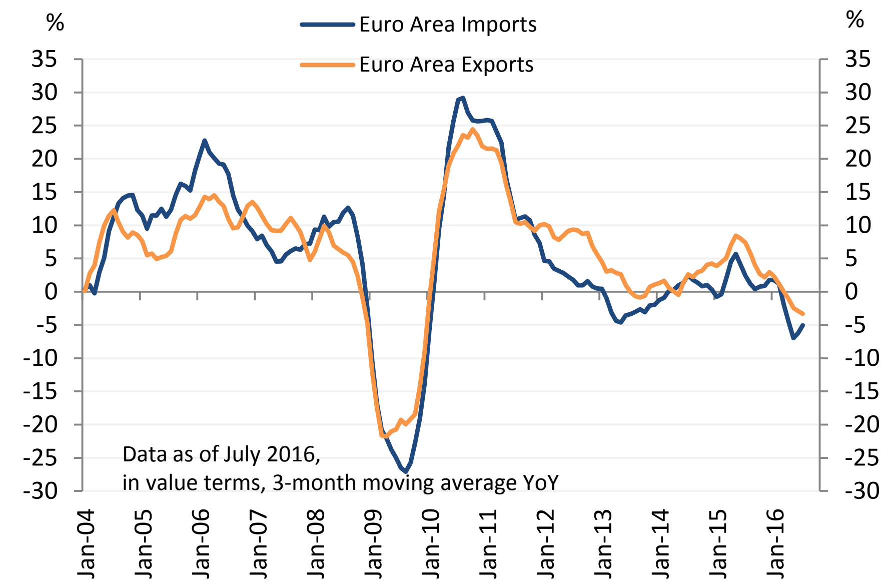
Net % of Banks reporting stronger demand for:

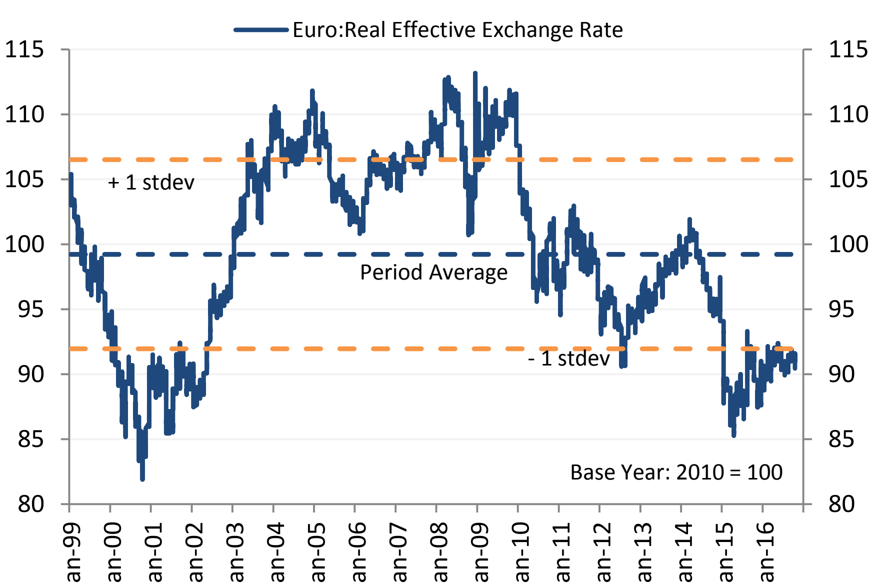


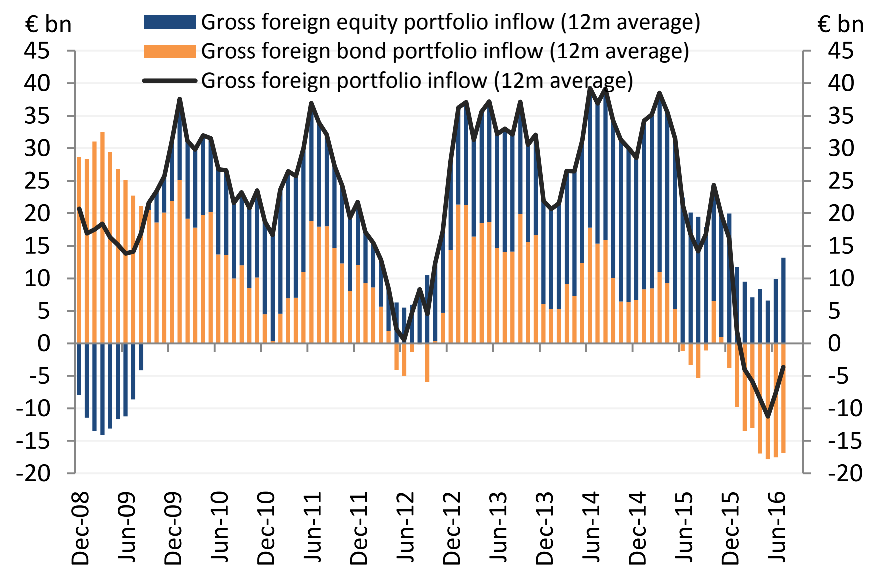
Source: ECB Bank Lending Survey

The CA rose in Q2:16 to 3.3% of GDP from 3.1% of GDP in Q1:16, reflecting significant saving investment imbalances







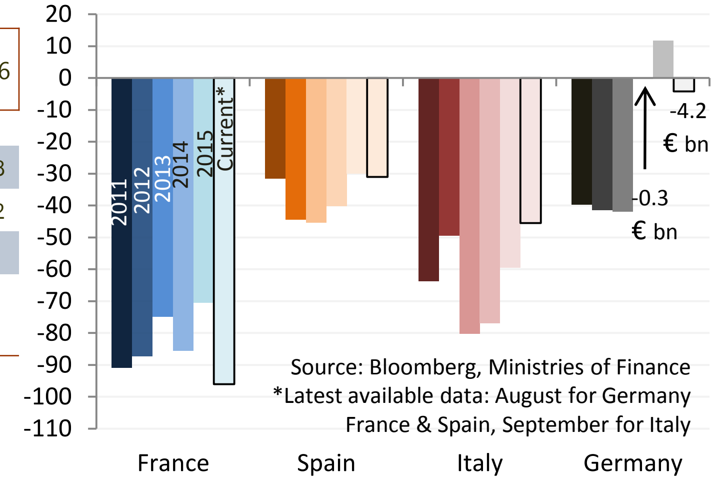


The euro area fiscal stance is expected to ease slightly, with the change in the cyclically-adjusted primary balance at -0.5% of GDP between 2015 and 2016

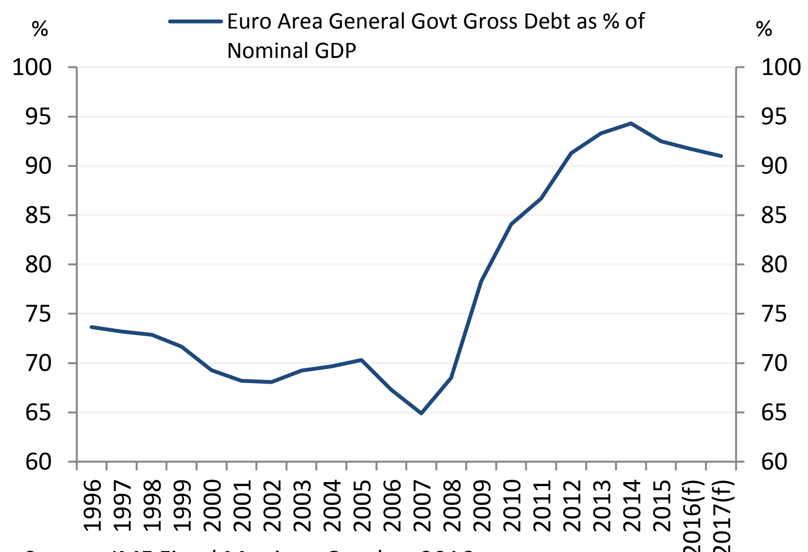
Euro area General Government Balance	Q1:14	Q2:14	Q3:14	Q4:14	2014	Q1:15	Q2:15	Q3:15	Q4:15	2015	Q1:16
(+) Revenues	1.175	1.178	1.184	1.191	4.729	1.199	1.206	1.215	1.227	4.848	1.228
(-) Expenditures	1.238	1.243	1.253	1.255	4.990	1.255	1.262	1.261	1.286	5.064	1.272
(=) Balance	-63	-65	-70	-64	-261	-56	-56	-45	-59	-216	-43
General Government Balance (% GDP)	-2,5	-2,6	-2,8	-2,5	-2,6	-2,2	-2,1	-1,7	-2,3	-2,1	-1,6

Source: Eurostat, in EUR billions unless otherwise noted

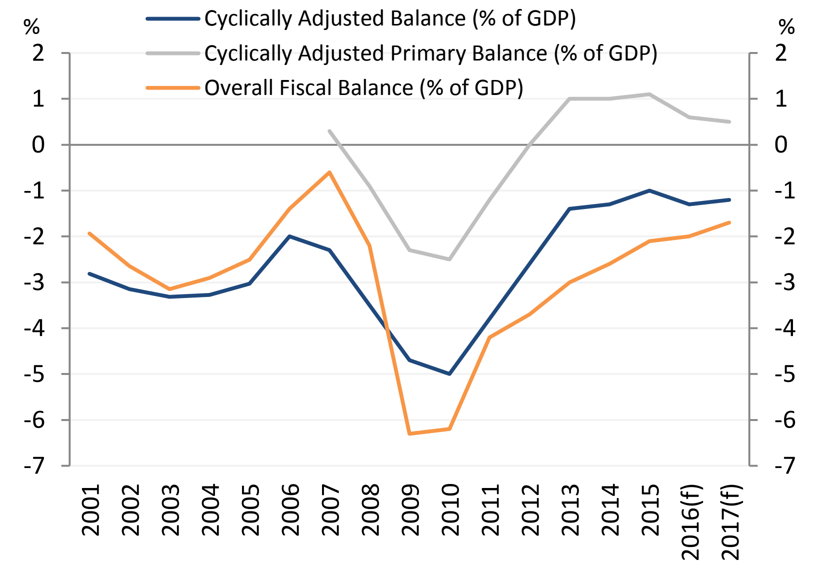
EA's G4 Countries Budget Balance (in € bn)



Source: Bloomberg, Ministries of Finance
*Latest available data: August for Germany France & Spain, September for Italy

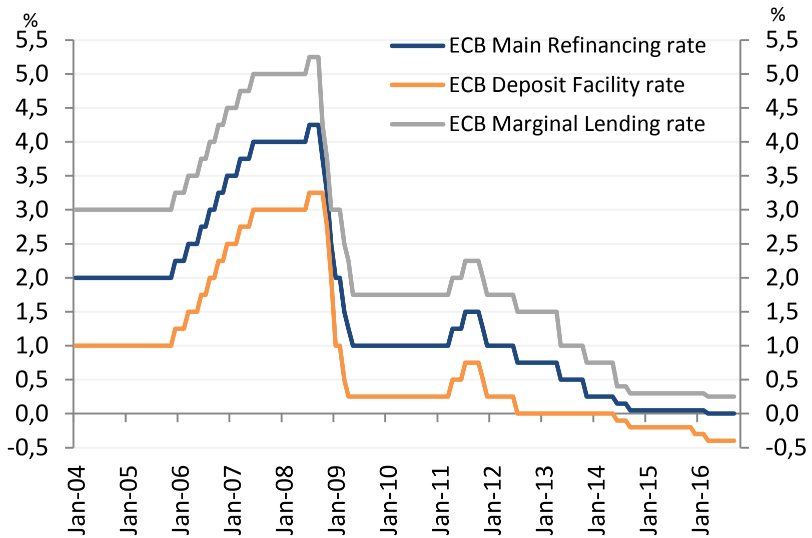


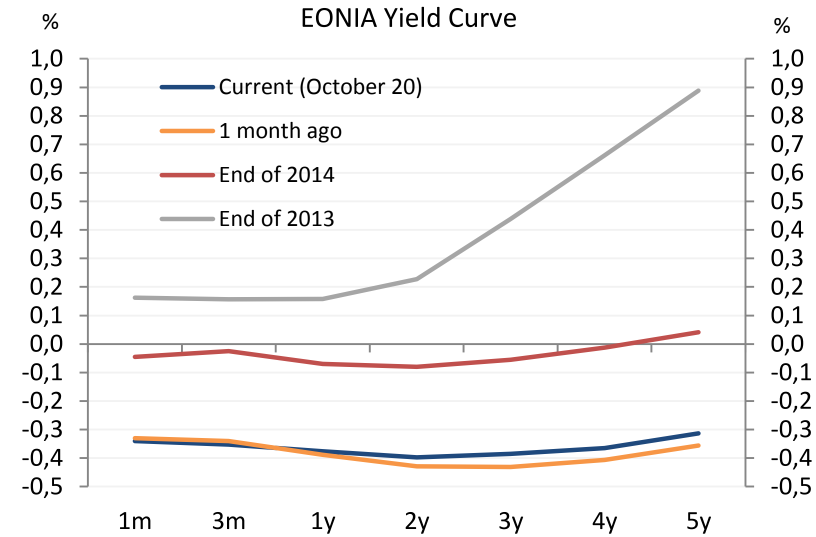
Source: IMF Fiscal Monitor, October 2016

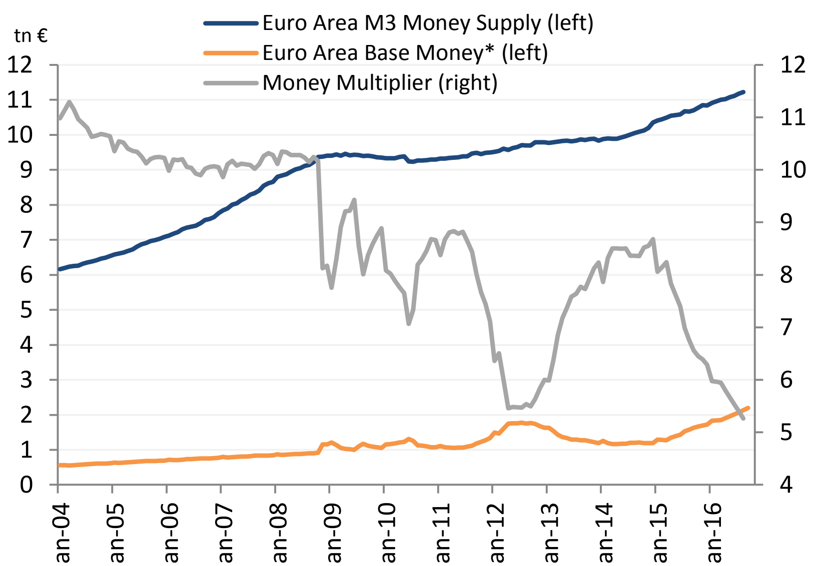


Source: IMF Fiscal Monitor, October 2016

The ECB remained on hold in October 2016, as "Brexit" has proved benign so far, and the economy remains weak

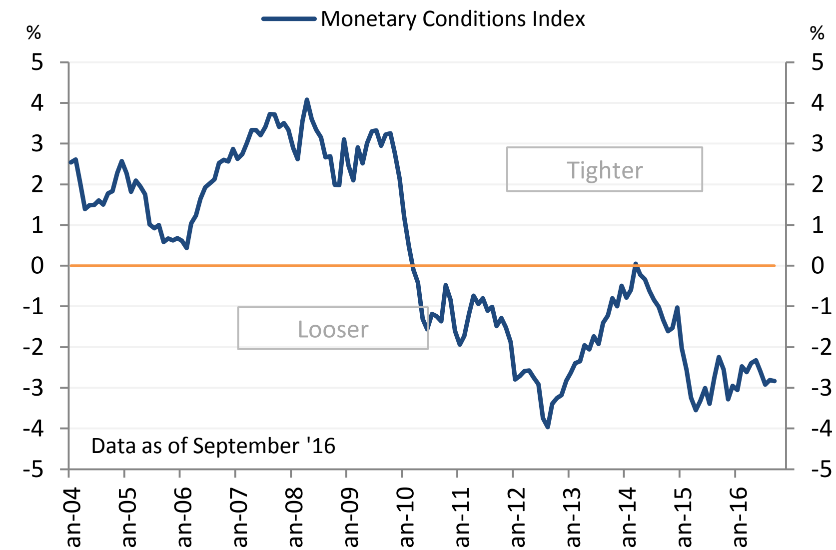






Base Money: Banknotes in circulation plus minimum required reserves & any excess reserves plus ECB's deposit facility

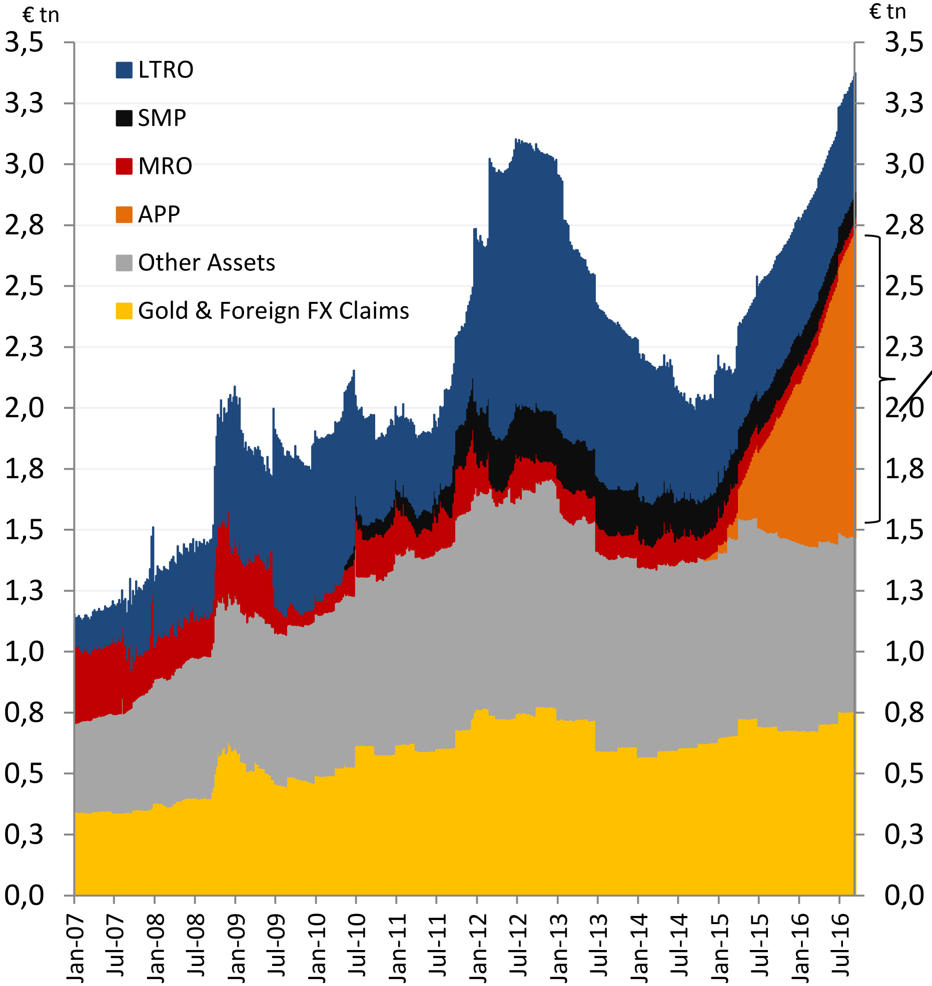
Source: ECB



Monetary Conditions Index is a simple composite index of Real Short Term Rates (Euribor less CPI) & Real Effective Exchange Rate

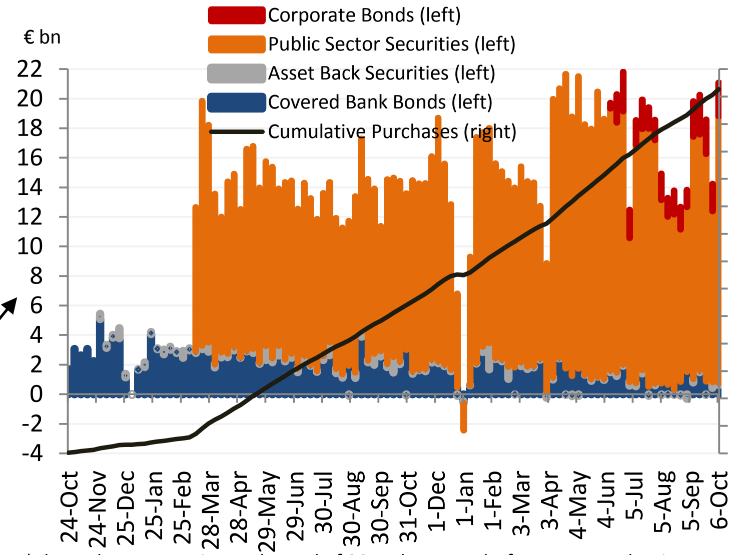
The ECB added investment grade non-financial corporate bonds to its asset purchases programme (€80bn per month)

ECB's Balance Sheet Assets



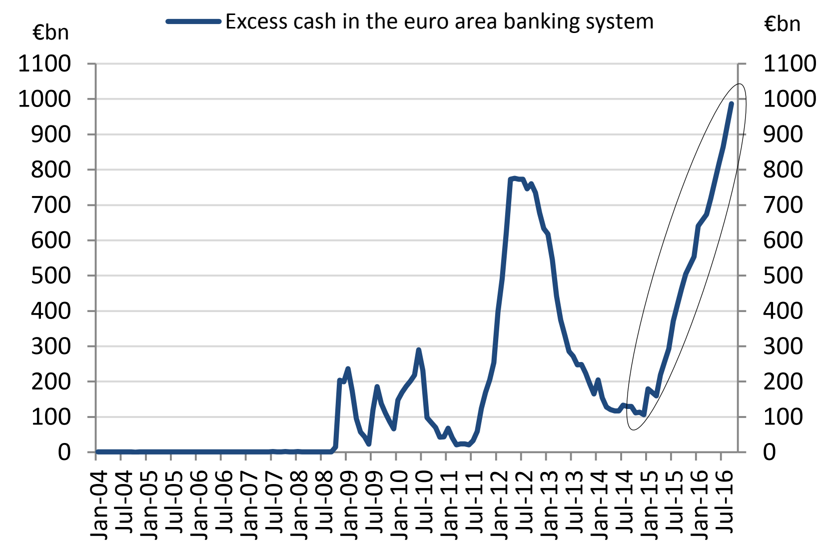
LTRO: Long-term refinancing operations, MRO: Main refinancing operations, SMP: Securities Market Programme, APP: includes Corporate Bonds, ABS, CBBPP3 & PSPP programmes, please refer to upper right graph

Source: ECB



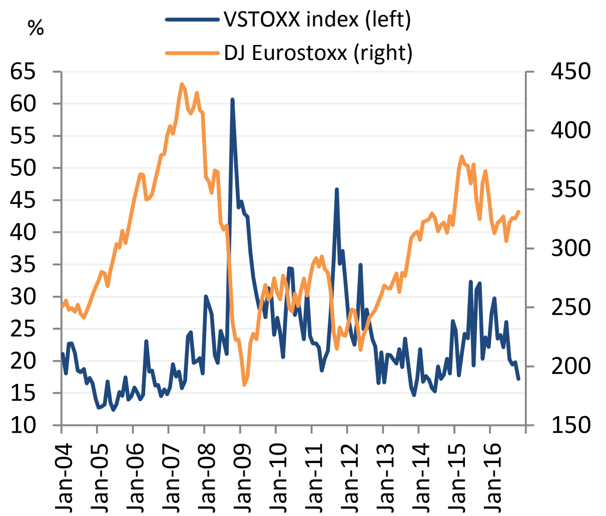
*Flows shown negative at the end of 2015 due to end-of-quarter revaluation adjustments (at market prices)

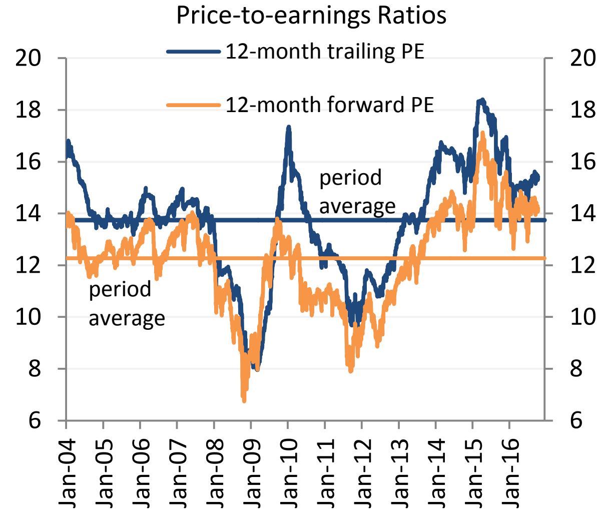
ECB New Programmes Evolution



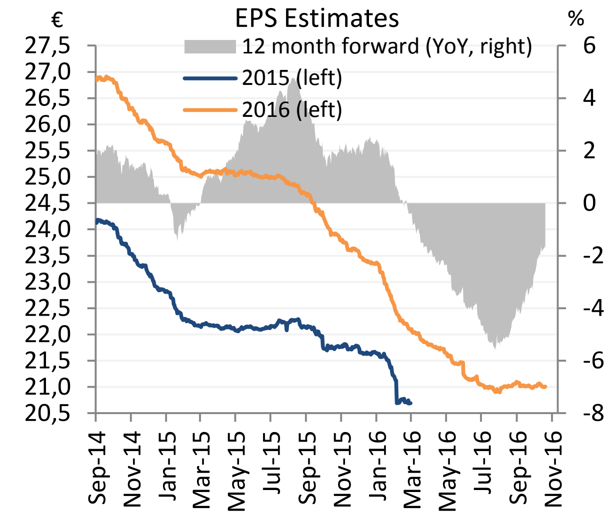
Source: ECB, Excess Liquidity: Deposit Facility minus Lending Facility + (CA reserves – Required Reserves)

EPS estimates for 2016 have stabilized since July, while market volatility has receded. The EuroStoxx has rebounded since Q2:16 by 6.3% (-4.1% ytd), with Banks (22%) and Autos (17%) overperforming

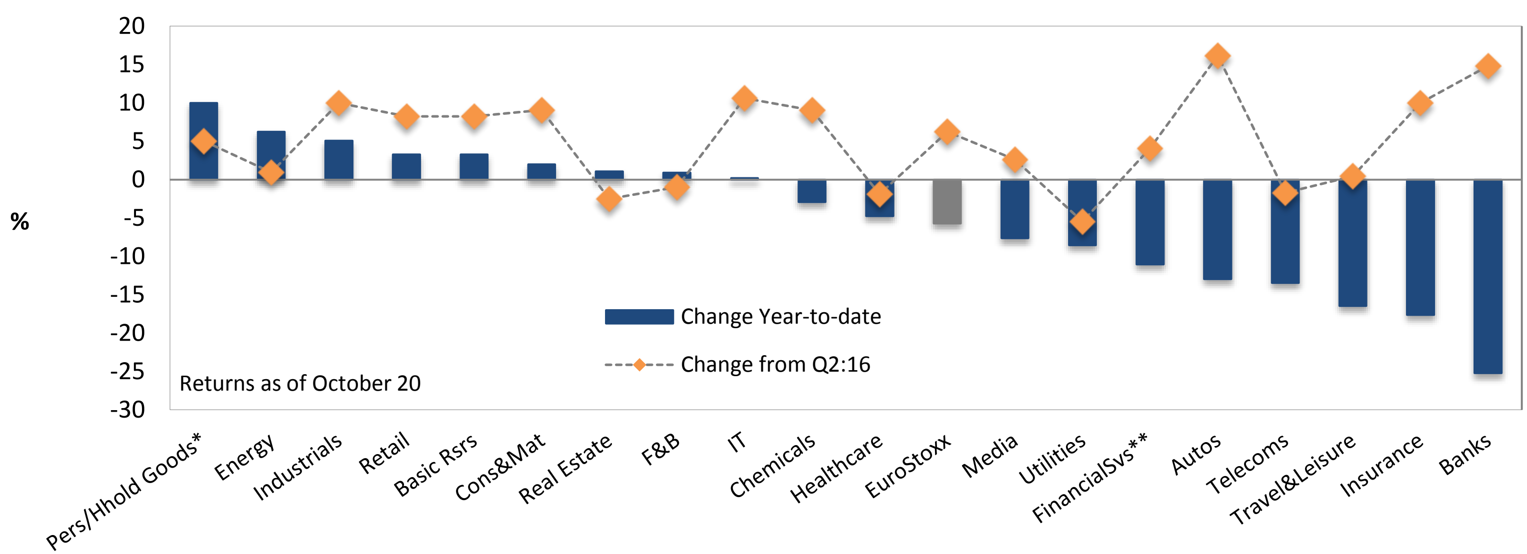




Source: Factset

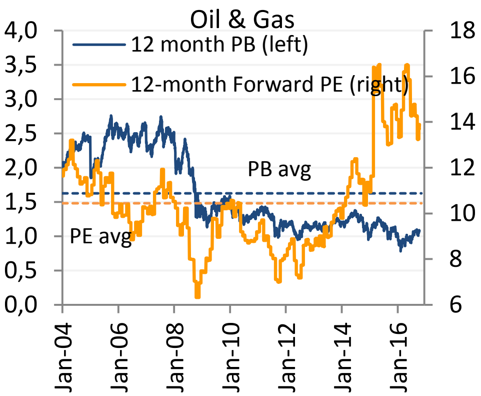


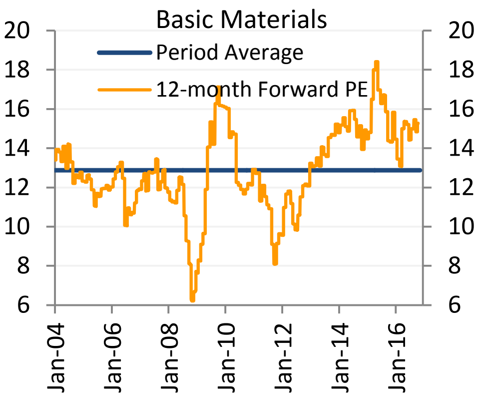
Source: Factset

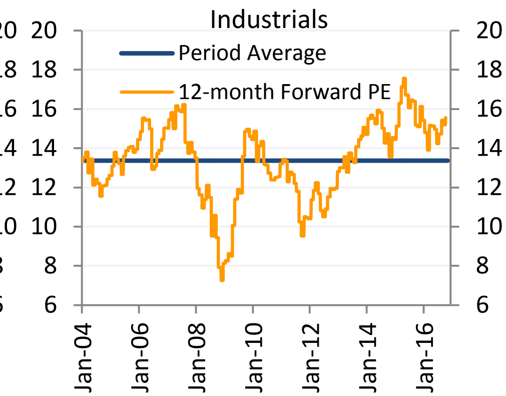


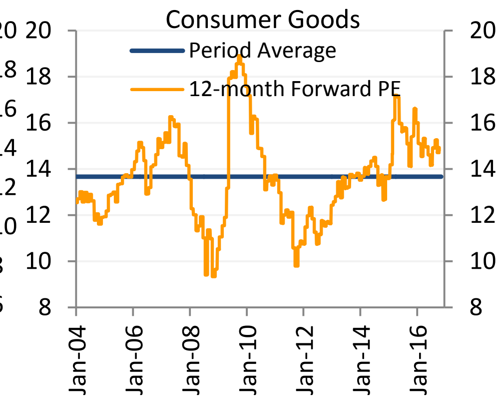
Note: *Personal & Household Goods, **Financial Services

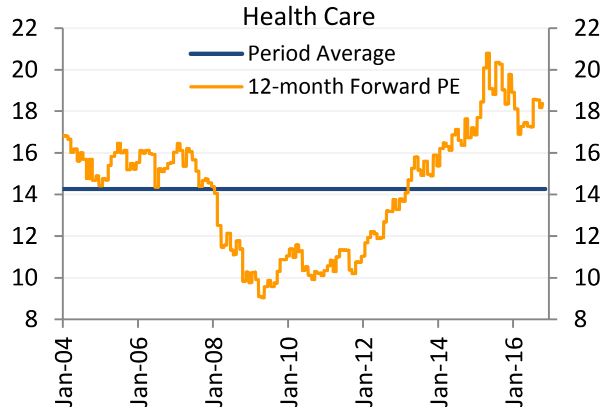
Euro area Sectors Valuation

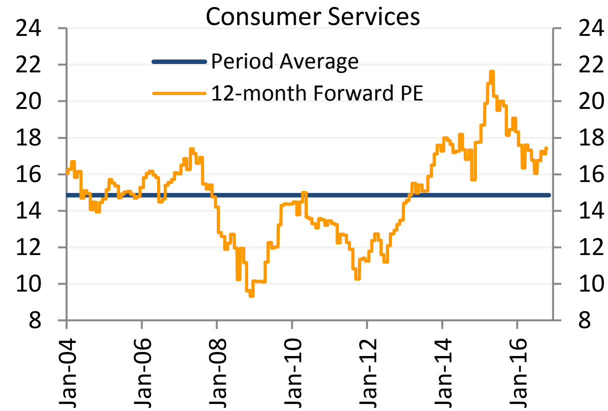


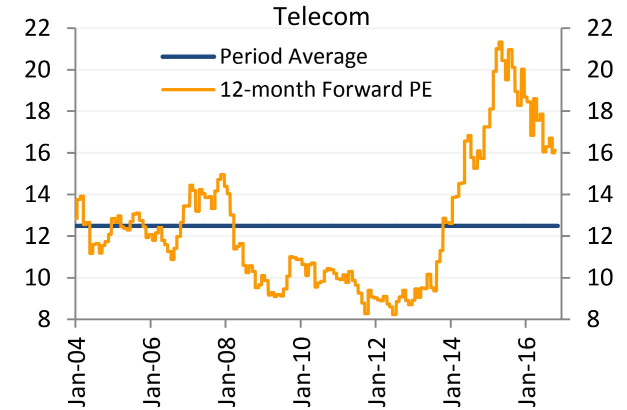


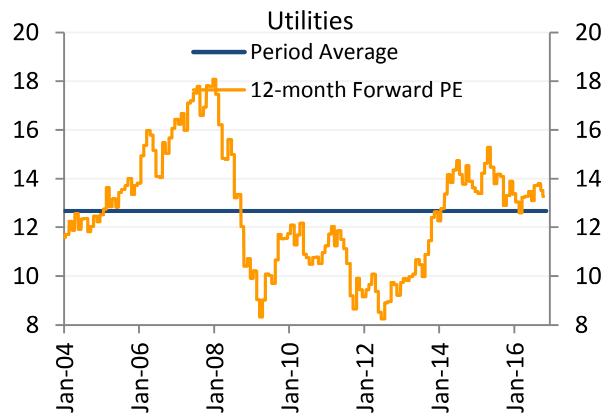


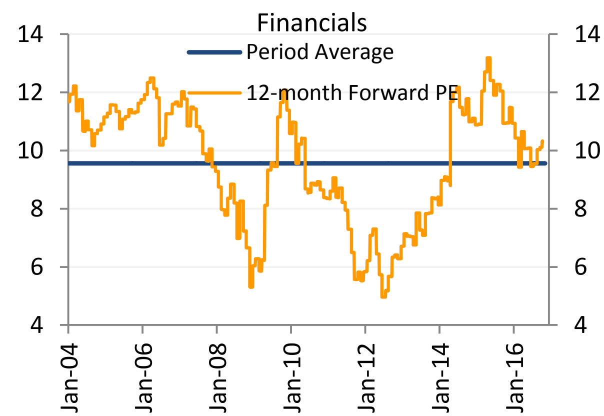


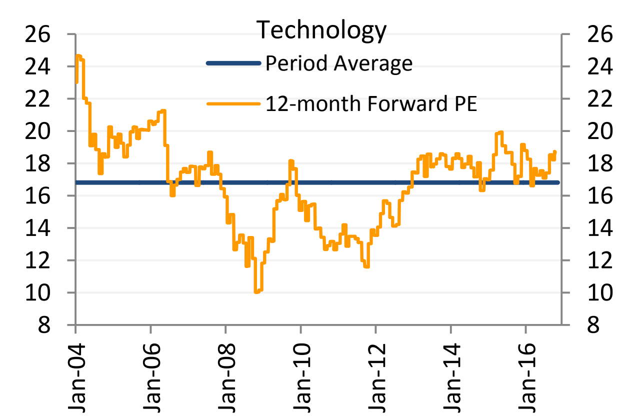




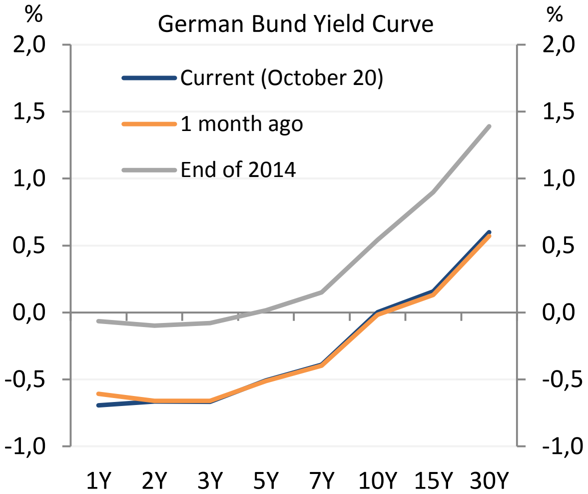


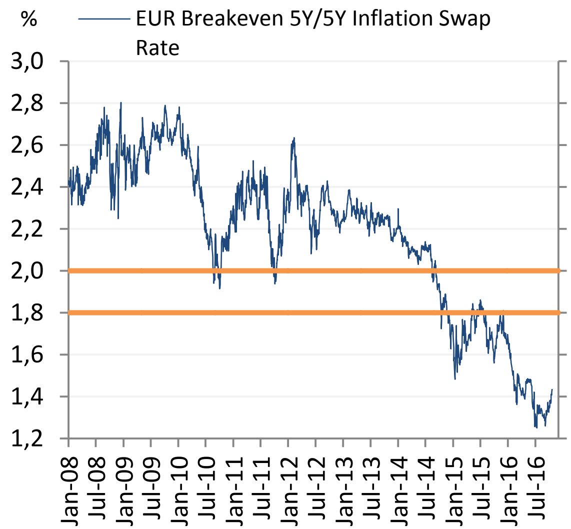


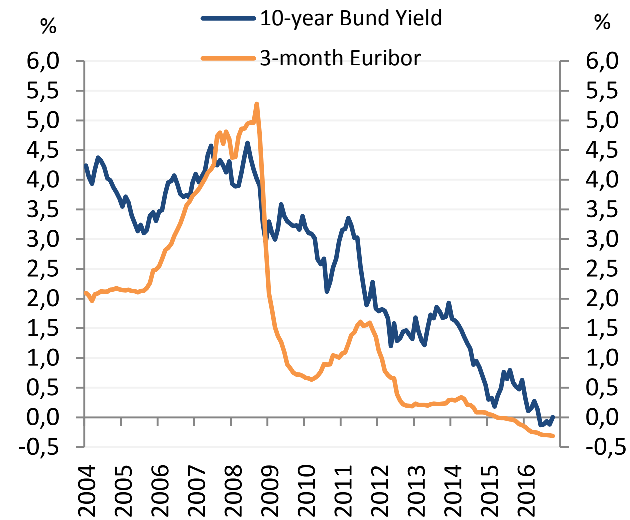




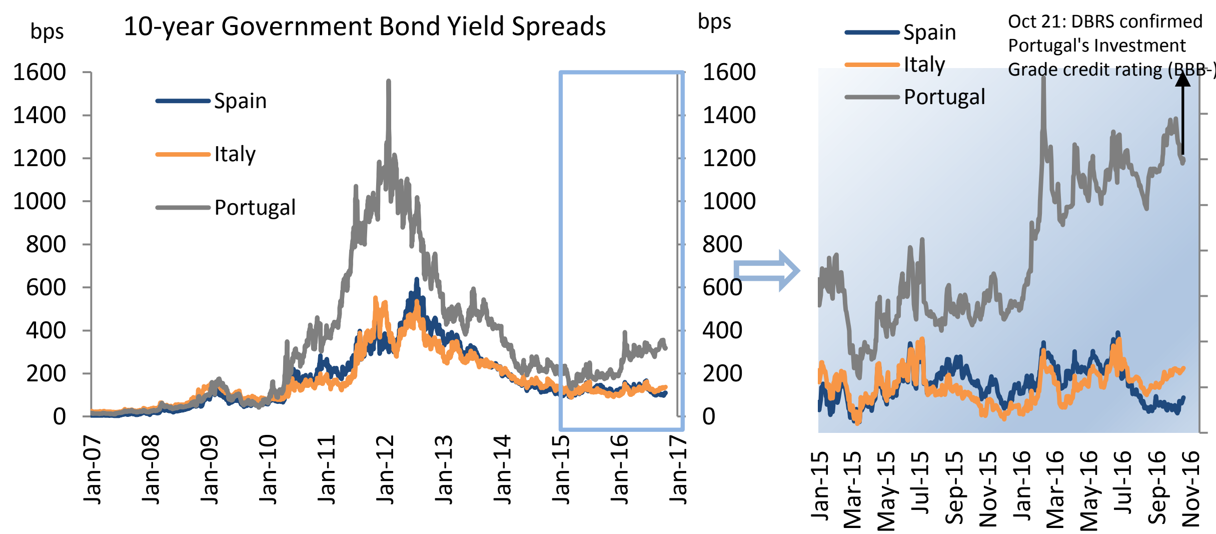
Bund yields remain close to record lows (historically), despite rising recently on the back of concerns for QE-tapering by the ECB







10-year Government Bond Yield Spreads over Bund



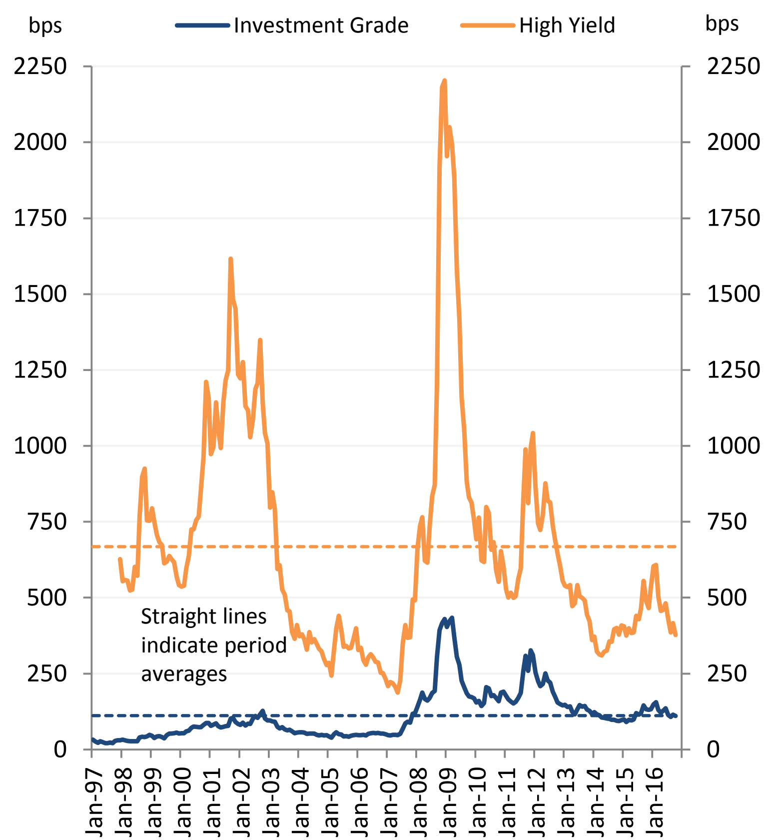
Sovereign Debt Ratings

	Moody's		S&P		Fitch	
Germany	Aaa	s	AAA	s	AAA	s
France	Aa2	s	AA	n	AA	s
Italy	Baa2	s	BBB-	s	BBB+	s
Spain	Baa2	s	BBB+	s	BBB+	s
Portugal	Ba1	s	BB+	s	BB+	s

Source: Ratings Agencies, Bloomberg (as of 20.10.16)
Outlook: p = positive, n = negative, s = stable

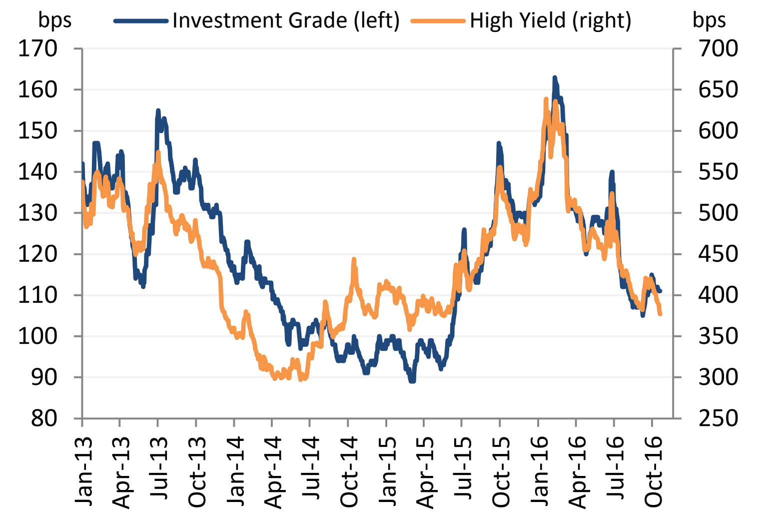
The inclusion of IG corporate bonds in the ECB's APP has benefited High Yield corporate bonds as well (HY spread: -158 bps ytd to 377 bps)

Corporate Bond Spreads

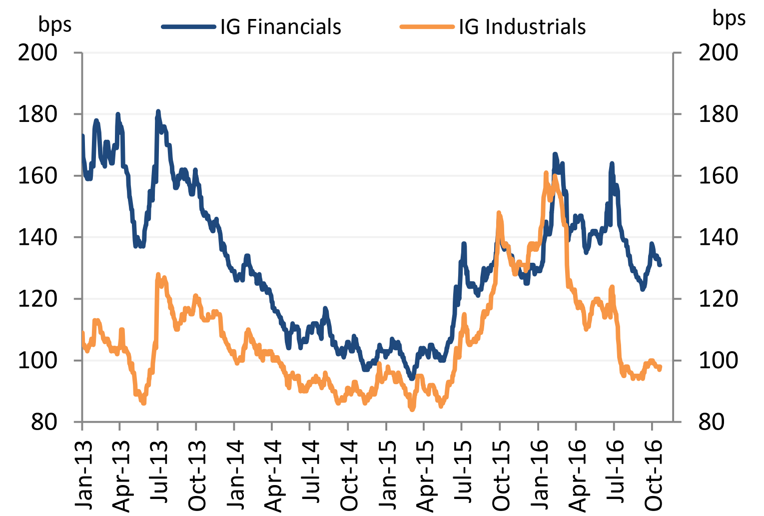


Source: Bank of America / Merrill Lynch Euro Corporate Bond Index (IG), Euro High Yield Index (HY)

Short-term View



IG Financials/Industrials



United Kingdom

- UK real GDP increased by a solid 2.2% qoq saar, on average, in H1:16 (pre-Brexit). In H2, so far, economic data suggest a smaller-than-expected negative impact on economic activity following the "Brexit" vote, partly due to the aggressive response by the Bank of England as well as the depreciation of the GBP that boosts export-oriented sectors and partly due to overblown fears from the neat-term impact of a positive Brexit vote.

- Consumption remains strong, with retail sales (in volume terms) in Q3 at +7.4% qoq saar (+5.1% qoq saar in Q2). At the same time, consumer confidence, despite an initial shock, has rebounded to pre-Brexit levels in September.

- Following a sharp decline in the immediate aftermath of the "Brexit" vote, PMIs rebounded strongly in August. Overall, in Q3:16, the composite PMI has averaged 51.7 from 52.4 in Q2:16, pointing to only a minimal deceleration in short-term growth.

- However, long-term business investment intentions surveys (CBIs) continue to decline. Moreover, PM May's increased rhetoric against EU-immigration flows suggests that negotiations with the EU could take the form of a "Hard Brexit" (likely impeding the UK's access to the EU single market), which would further jeopardize investment decisions. "Hard Brexit" jawboning and a broader sense of increased protectionism has sent the British Pound to 31 year lows. The current account deficit (4-quarter sum) of 5.6% of GDP and Gross Foreign Liabilities of 400% of GDP also contribute to GBP weakness.

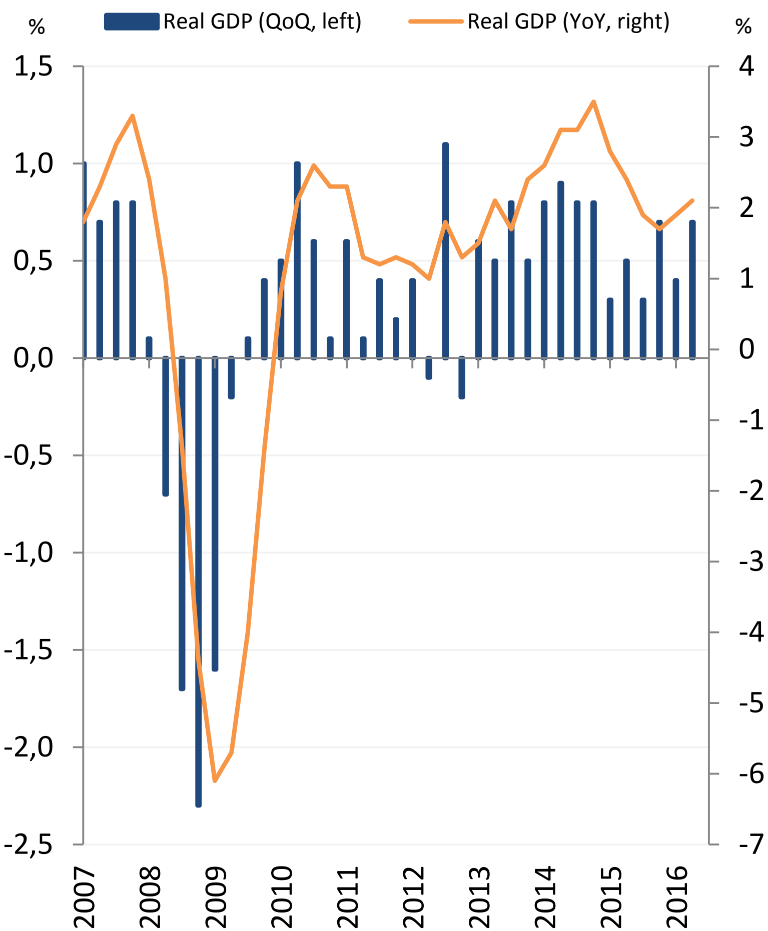
- Overall in Q3, GDP growth is expected to have decelerated towards 1% qoq saar. For FY:16 real GDP growth is expected at 1.8% yoy (IMF, October 2016). Investor attention will turn to 2017 growth due to negotiations regarding the establishment of a new relationship with the EU -- expected to begin in April 2017. IMF estimates for 2017 real GDP stand at 1.1% (compared with 2.2% yoy prior to the referendum).

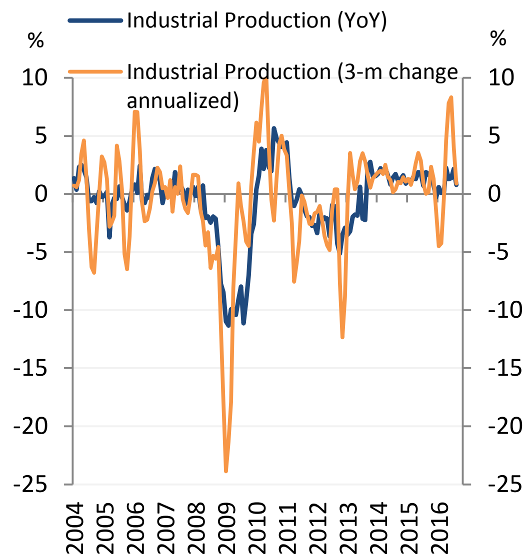
- In order to support the economy, the Bank of England, in August: i) cut its policy rate by 25 bps to 0.25%; ii) re-activated its Gilt purchases by £60bn to £435bn over the next 6 months; iii) initiated corporate bond purchases of up to £10bn over the next 18 months; and iv) introduced a 4-year Term Funding Scheme in order to incentivize bank lending to the private sector. The BoE expects to implement further easing before end-year, if economic data weaken materially.

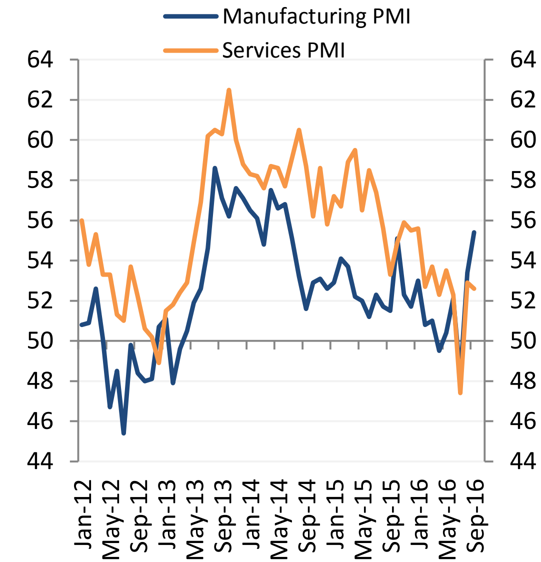
- Meanwhile, fiscal policy will turn more expansionary in order to minimize the potential "Brexit" related turbulence, with HM Treasury officials having abandoned the target for a budget surplus by 2019/20. Increased spending on infrastructure will likely be the focus of increased spending, albeit further details on the UK's revised fiscal stance are expected on November 23 (Autumn Statement).

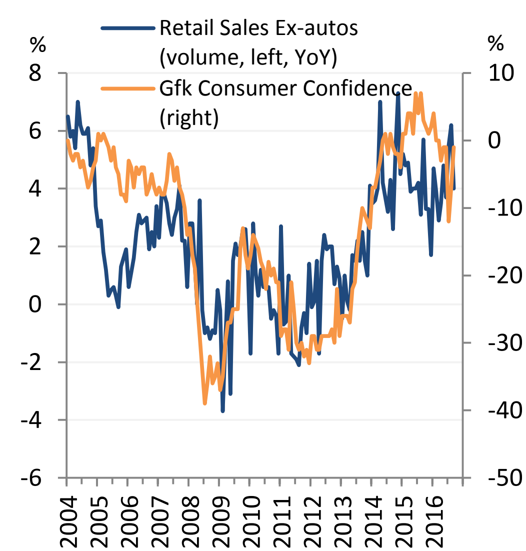
- The FTSE 100 has overperformed its developed peers since the UK referendum (+10.9% vs +2.2% for the MSCI DM excluding the UK), as the weaker GBP strengthens corporate profitability (70% of FTSE100 revenue comes from abroad). The aggressive response by the BoE initially caused government bond yields to decline sharply (10Yr: -86 bps to a historically low 0.52% in August 12), albeit rebounding later (10Yr: +57 bps to 1.07% since August 12) on the back of better-than-expected data, lower expectations for further monetary policy easing by the BoE, and alleviates Hard-Brexit concerns.

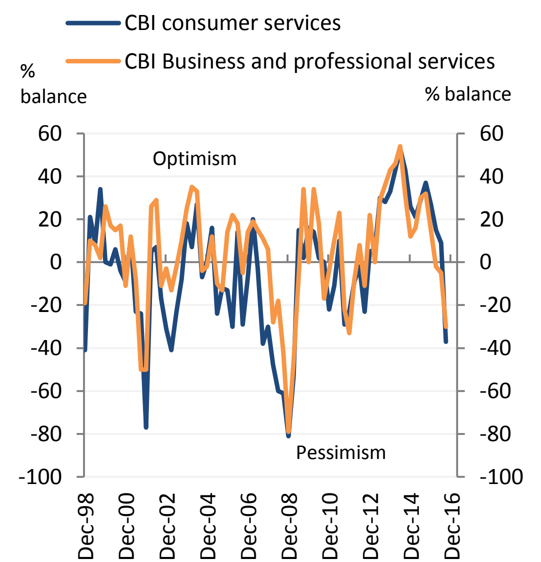
PMIs rebounded after a sharp decline in the immediate aftermath of "Brexit"











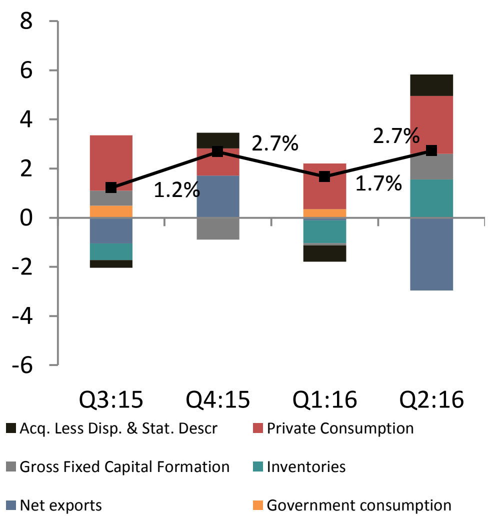
Above: GDP data as of Q2:2016
Right: Industrial Production data as of August 2016, Retail Sales, Consumer Confidence, Manufacturing PMI & Services PMI data as of September 2016, CBI survey data as of Q3:2016
Source: ONS, Markit, Bloomberg

In Q3:16, real GDP growth is expected to decelerate in H2:2016

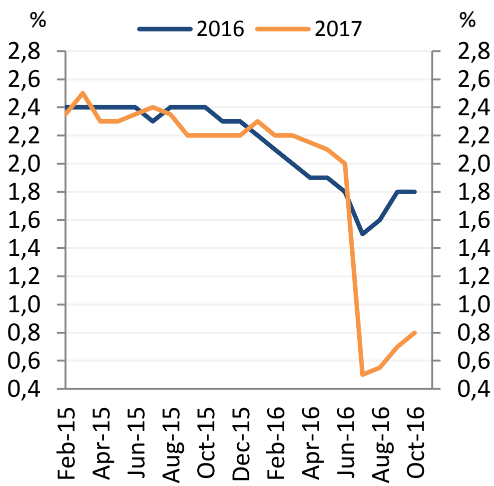
UK Real GDP Growth	2014	Q1:15	Q2:15	Q3:15	Q4:15	2015	Q1:16	Q2:16	Q3:16e	Q4:16e	2016e
GDP (YoY)	**3,1**	2,8	2,4	1,9	1,7	**2,2**	1,9	2,1	2,0	1,4	**1,9**
GDP (QoQ saar)	-	1,0	2,0	1,2	2,7	-	1,7	2,7	1,1	0,2	-
Households consumption (QoQ saar)	2,2	3,2	2,6	3,5	1,7	2,5	2,9	3,7	0,6	-3,0	0,0
Government consumption (QoQ saar)	2,3	1,8	4,2	2,5	0,0	1,5	1,8	0,0	0,7	0,0	0,0
Gross Fixed Capital Formation (QoQ saar)	6,7	7,1	3,6	3,7	-5,1	3,4	-0,5	6,4	2,7	-0,5	1,0
Inventories contribution (QoQ saar)	0,6	-1,1	-1,5	-0,7	0,0	-0,2	-0,9	1,6	-1,3	-0,1	-0,3
Net Exports contribution (QoQ saar)	-0,4	-1,8	0,9	-1,1	1,7	-0,4	-0,1	-2,9	1,4	2,4	0,0
Exports (QoQ saar)	1,5	9,2	-4,5	-1,2	18,5	4,5	0,5	-4,1	0,1	9,2	2,7
Imports (QoQ saar)	2,5	14,4	-6,8	2,2	10,9	5,4	0,8	5,3	-4,0	0,9	2,5

Source: Office for National Statistics, Bloomberg

GDP Contributions (%)

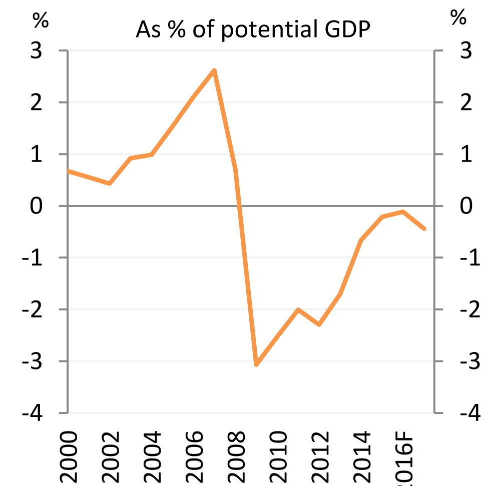


GDP Forecast Evolution



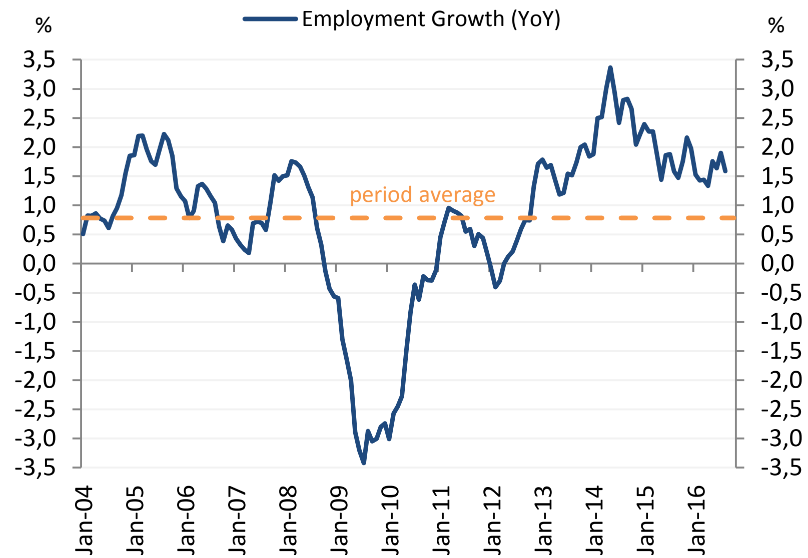
Source: Bloomberg Consensus

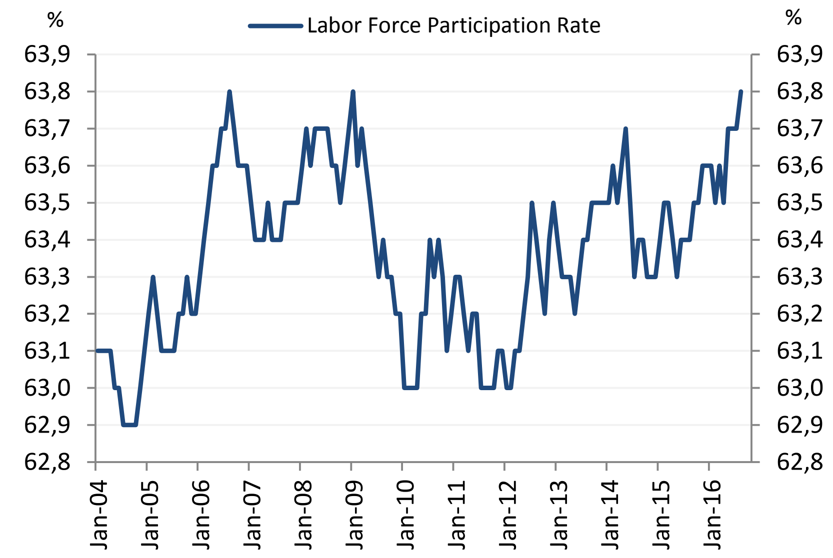
Output Gap

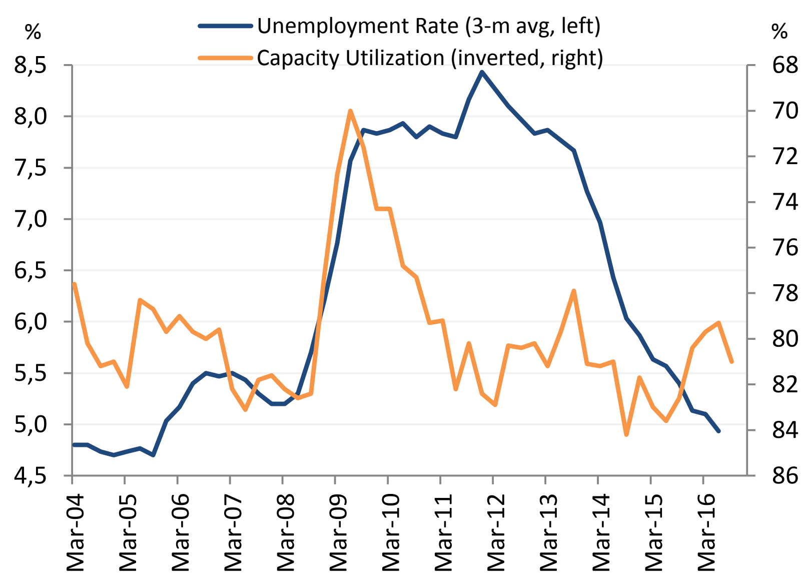


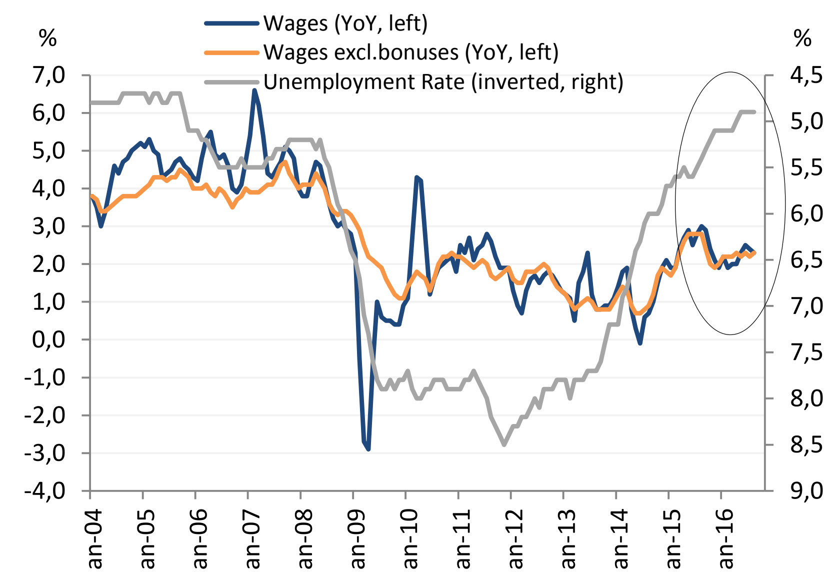
Source: IMF

Employment growth remains solid, while wage growth hovers around 2% yoy

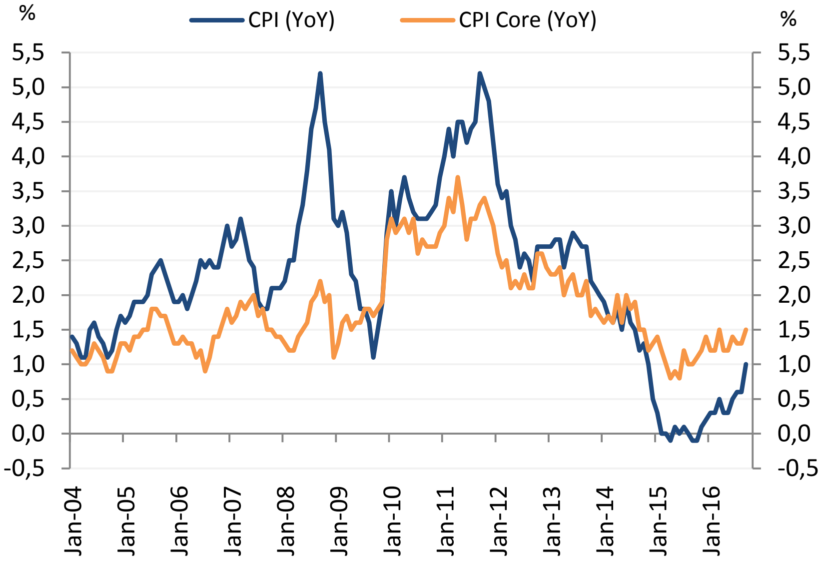


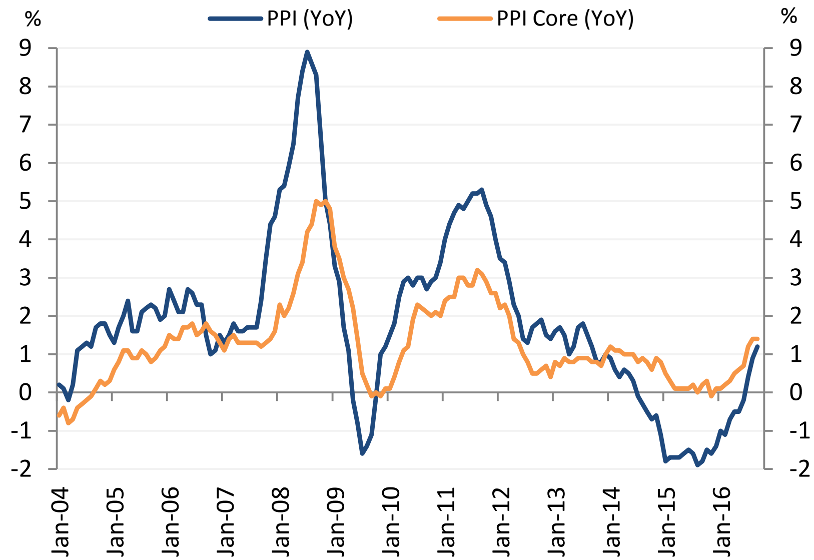


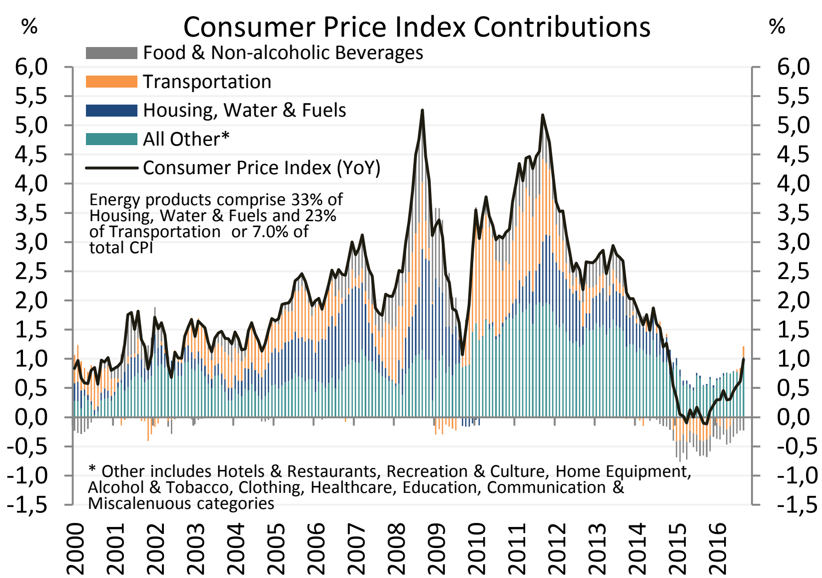


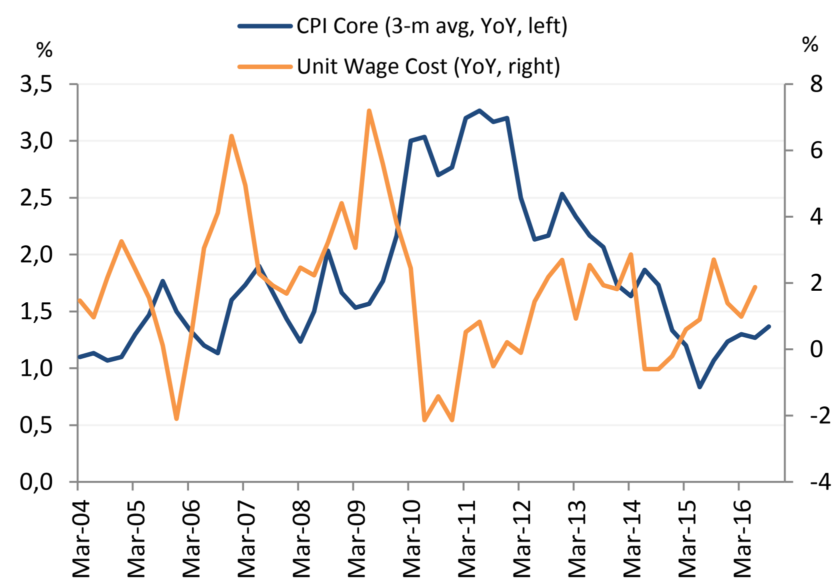


The BoE expects domestic cost pressures to remain soft, but higher import prices (due to the weaker GBP) will drive inflation to the 2% target by mid-2017

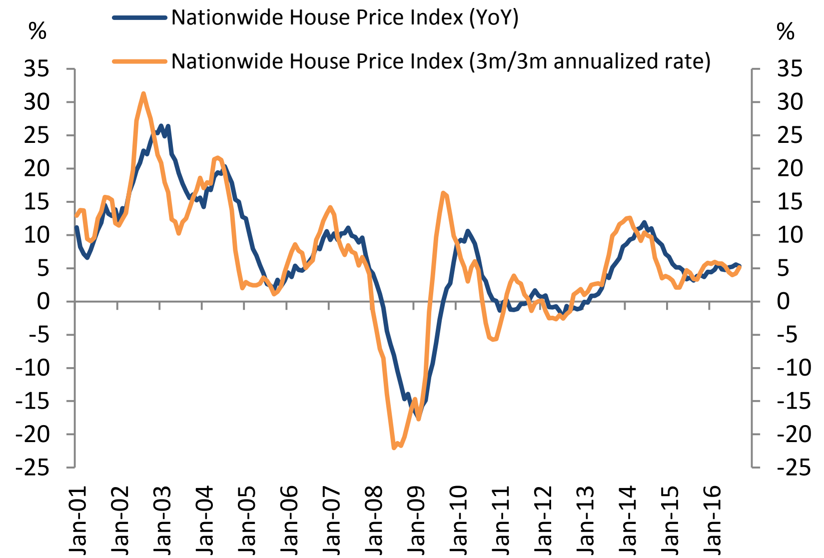


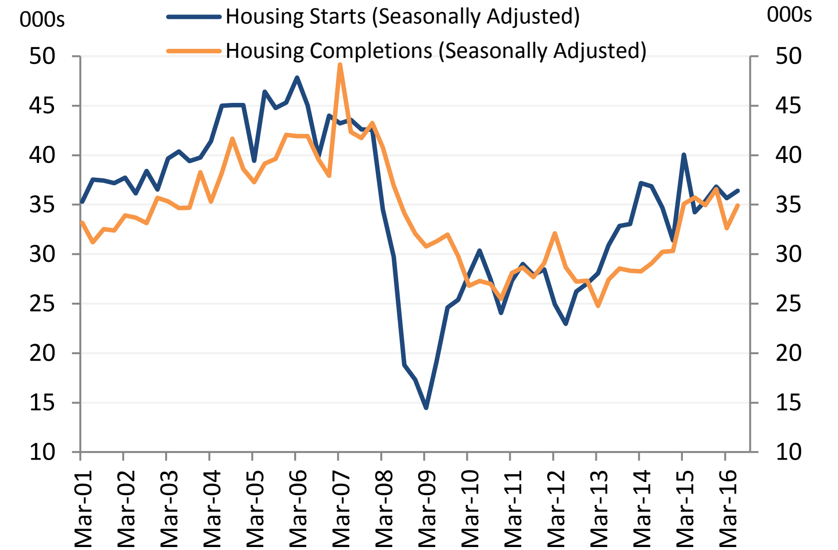


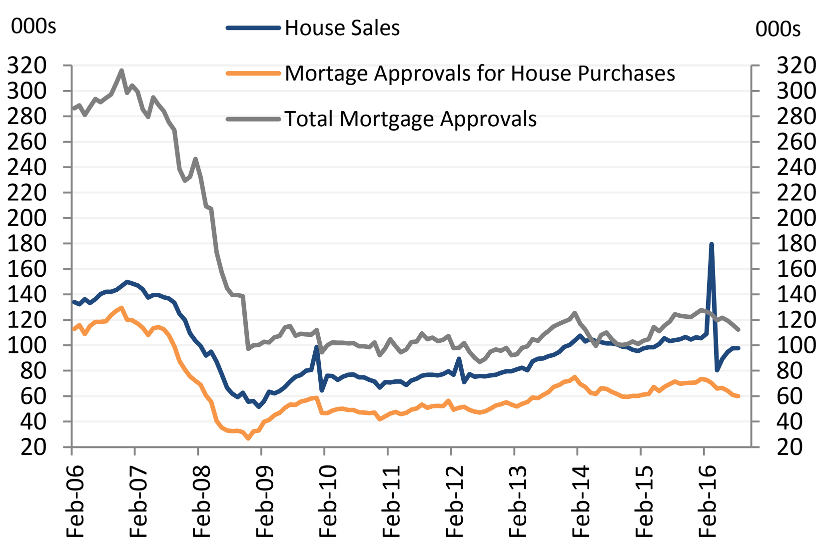




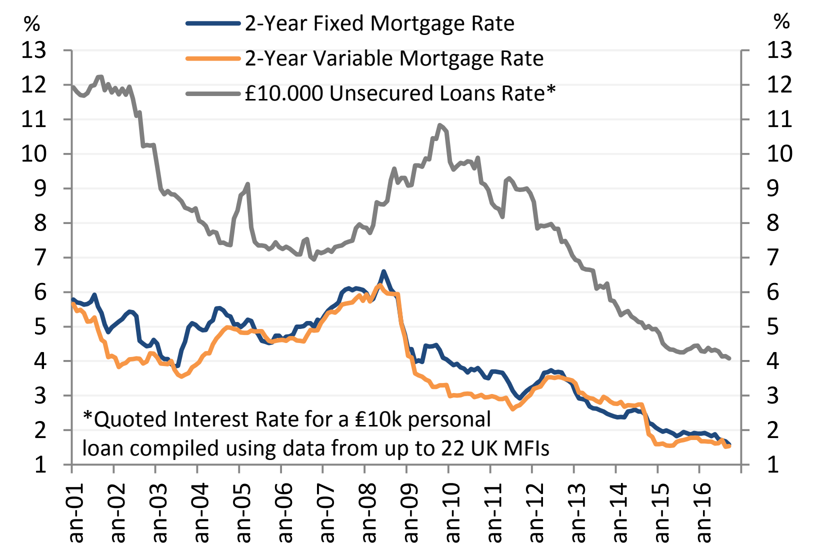
The housing market has demonstrated increased resilience, underpinned by multi-year low mortgage rates





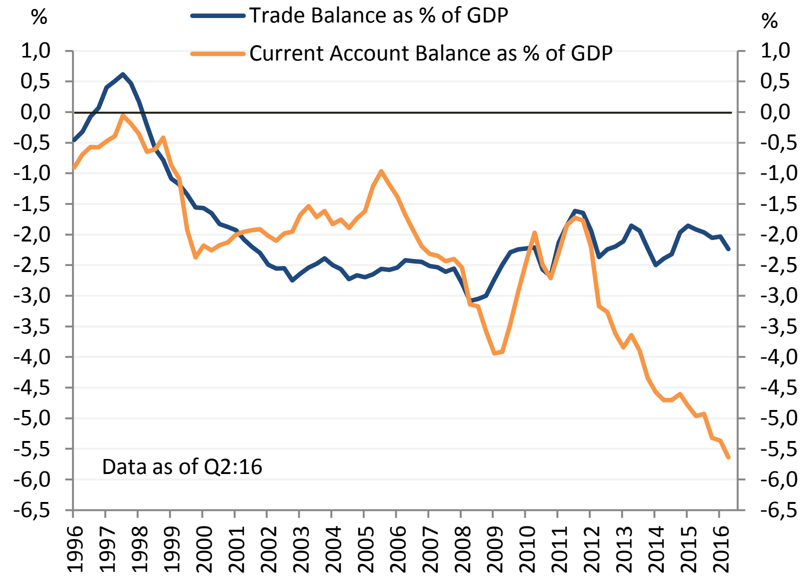


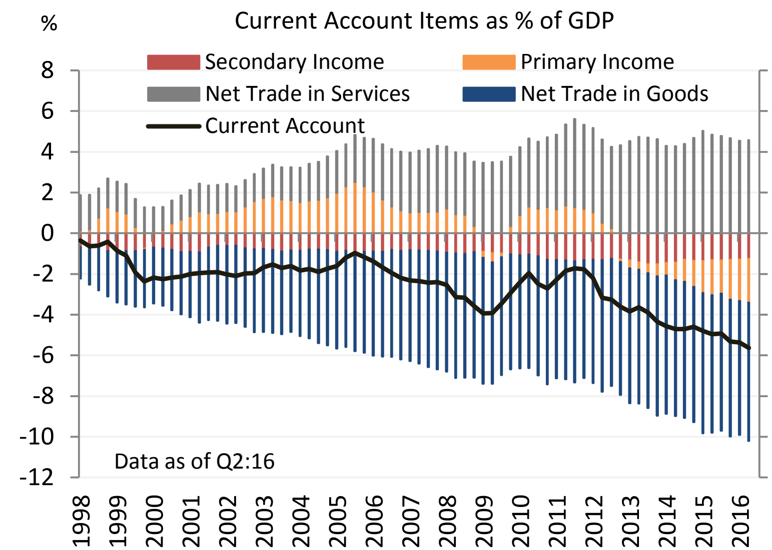
Source: Bank of England, HM Revenue & Customs

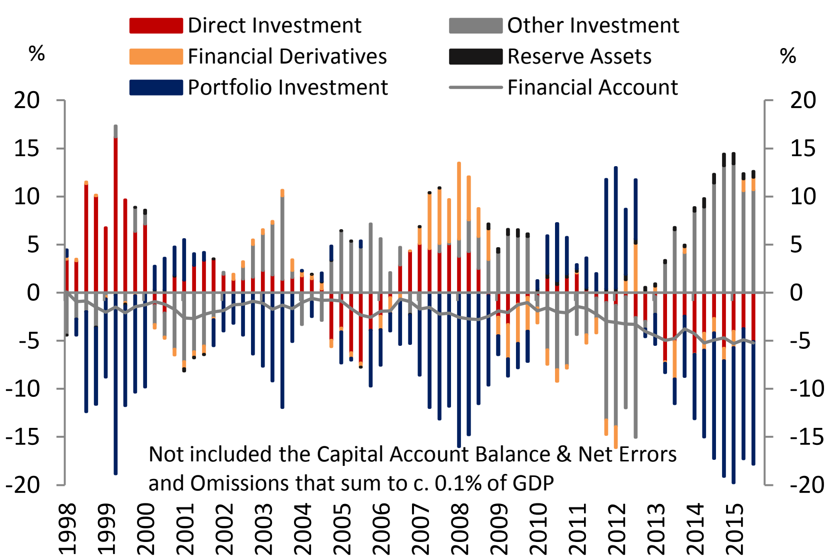


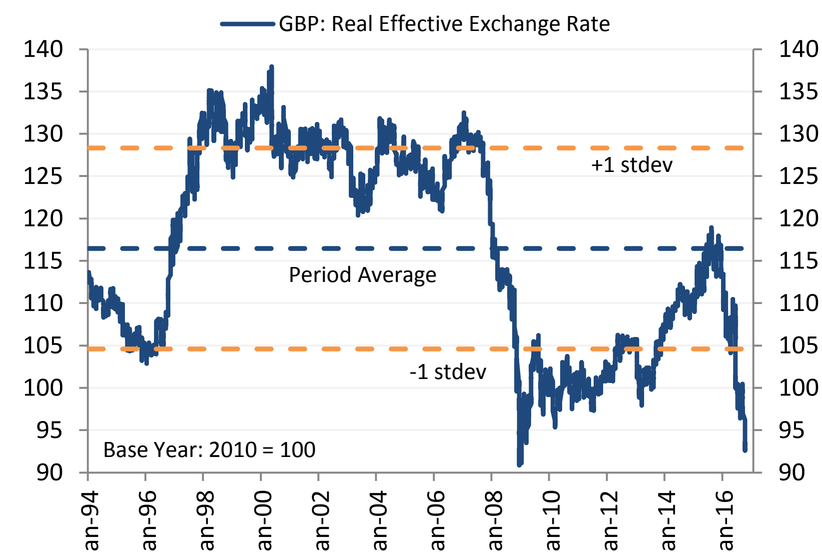
Source: Bank of England

The GBP's depreciation since the referendum (-15% in NEER terms since June 23) continues amid a sizeable current account deficit (5.6% of GDP)



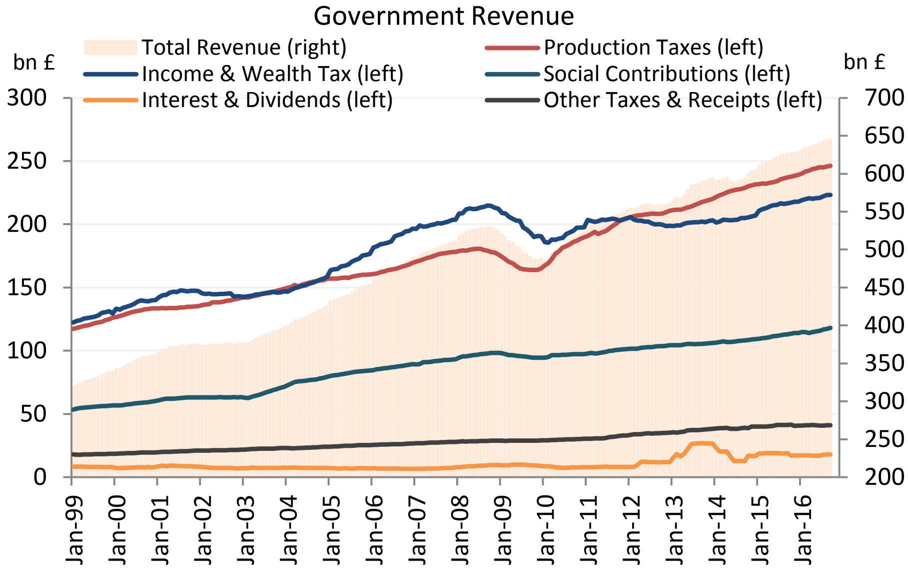


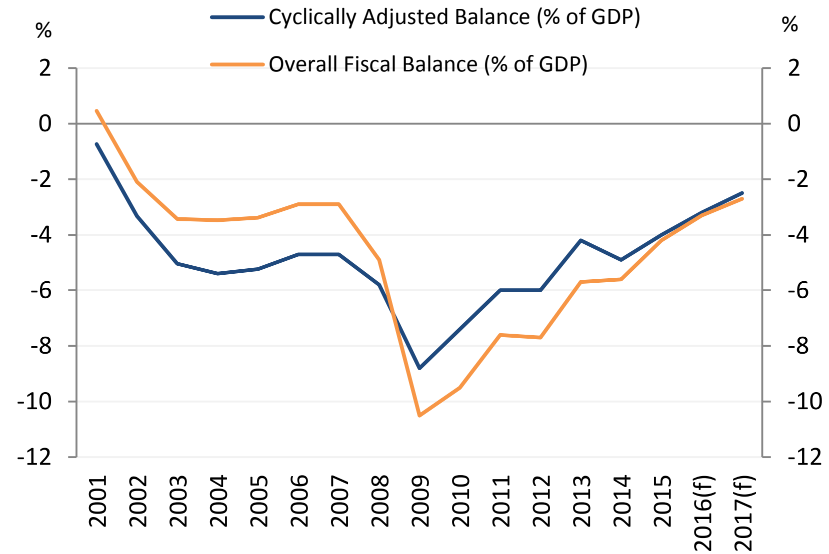




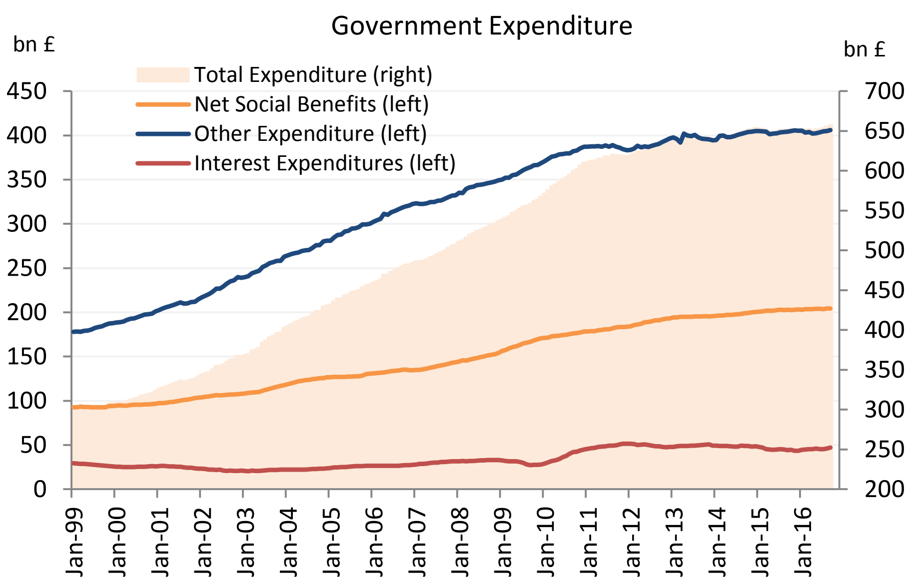
Source: Bloomberg

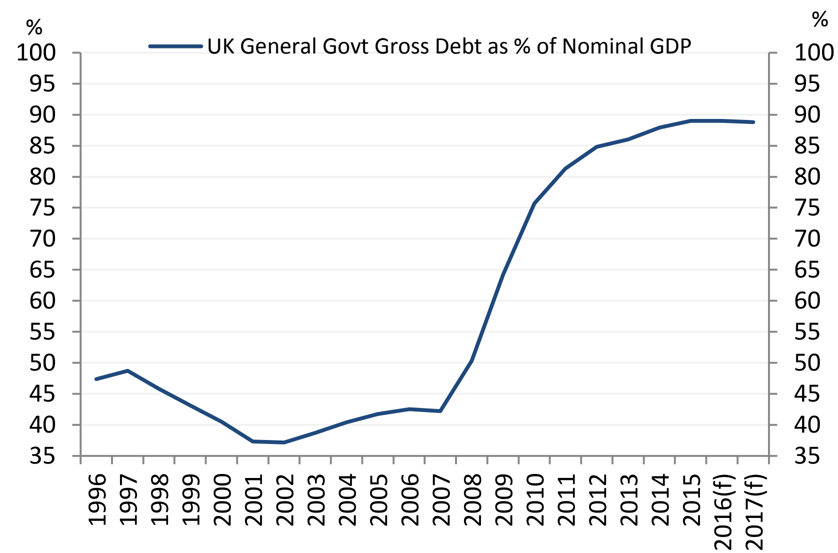
UK fiscal policy may turn more flexible in the near-term to support the economy jeopardizing the narrowing of fiscal deficits





Source: IMF Fiscal Monitor, October 2016

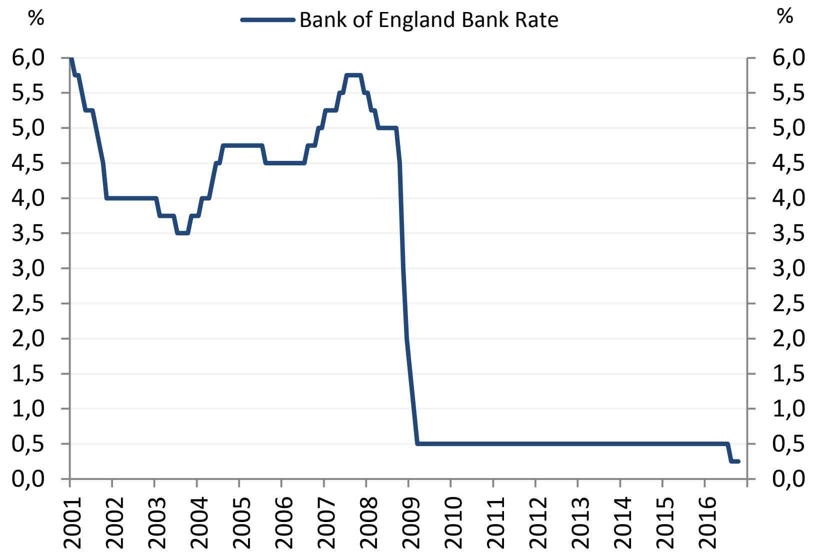


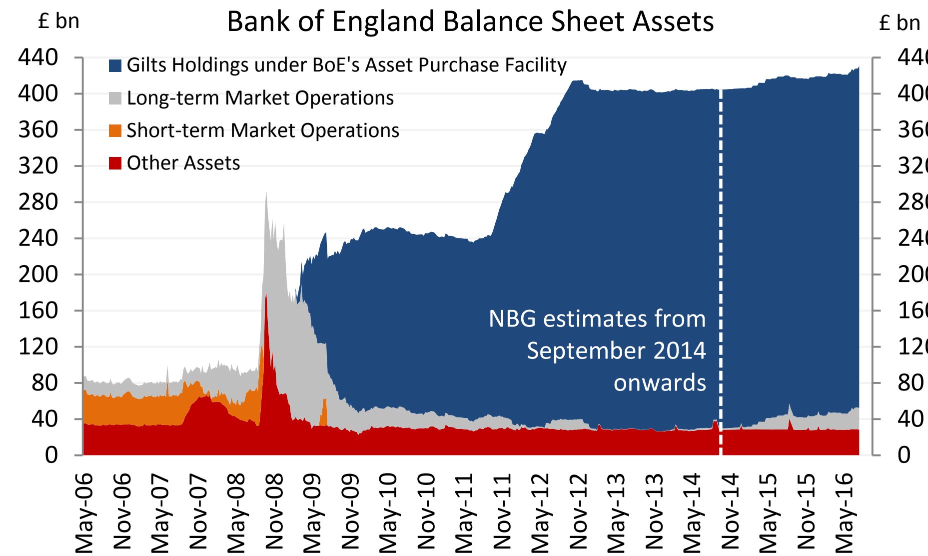


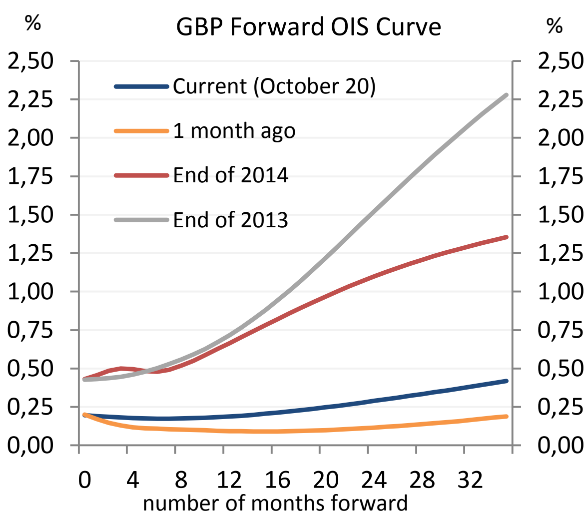
Source: IMF Fiscal Monitor, October 2016

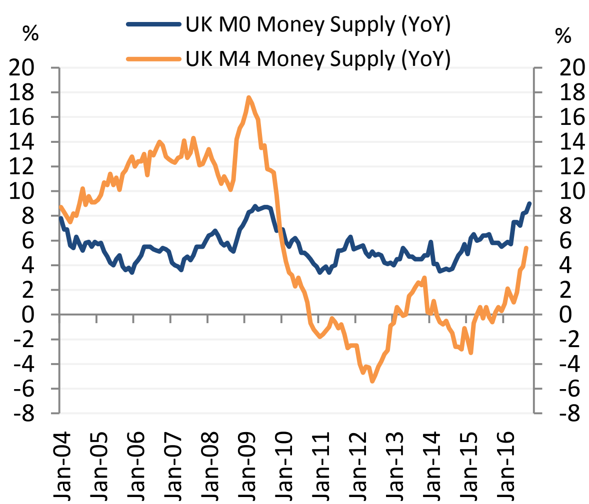
Government Revenues and Expenditures are 12 month rolling sums

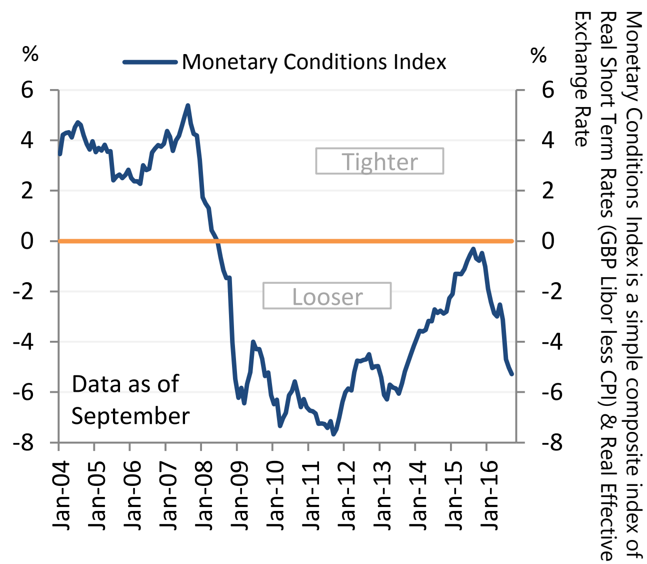
The BoE responded to "Brexit" with a comprehensive package including, *inter alia*, a 25 bp cut in the policy rate, a reactivation of QE purchases and an easing bias going forward



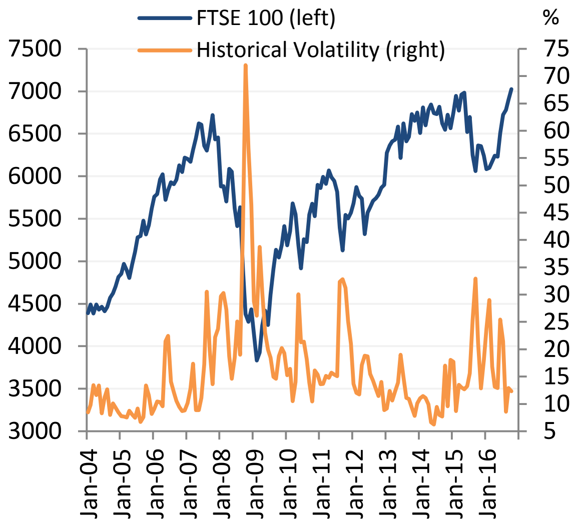


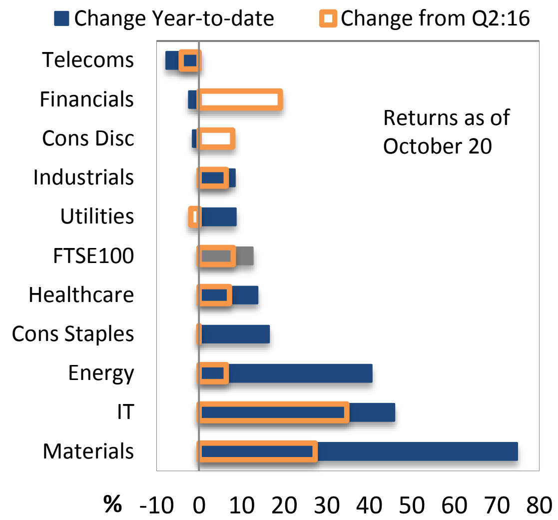


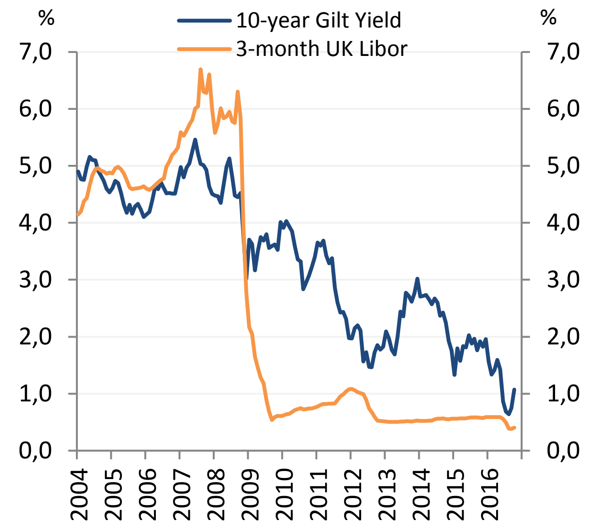


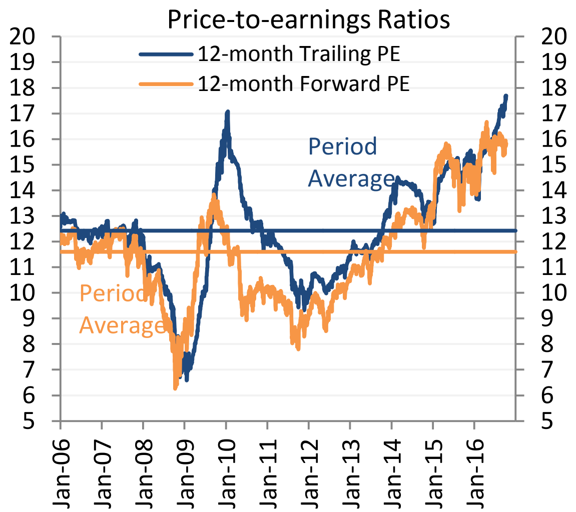


12-month forward EPS growth estimates returned to positive territory (+6.3% yoy vs -11.9% yoy in June 23) on the back of the weaker GBP, supporting (the export-oriented) FTSE 100 companies









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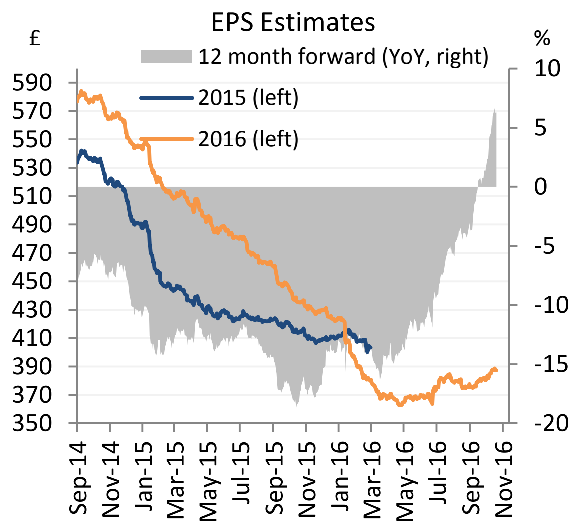

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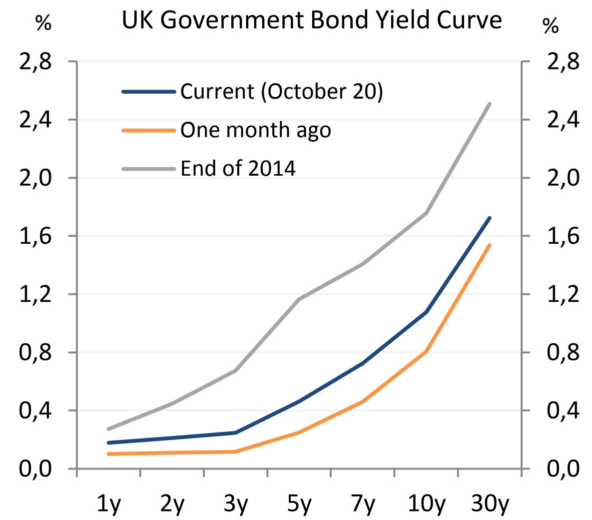
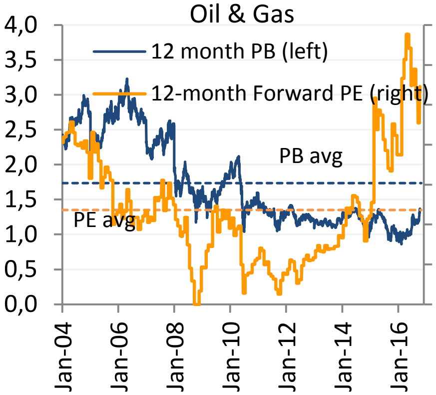
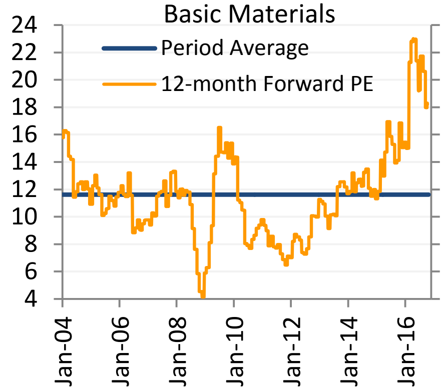
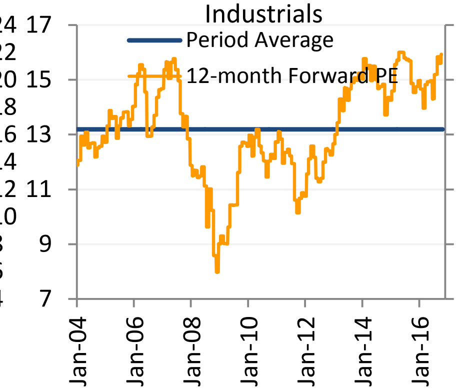
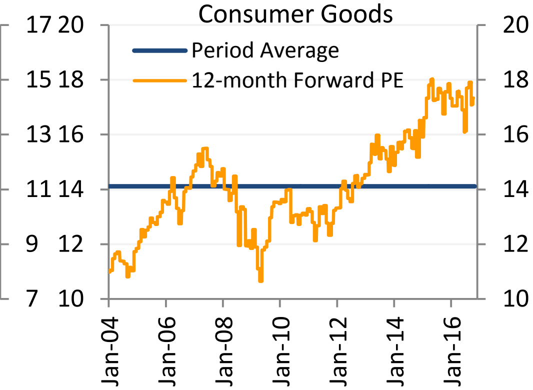


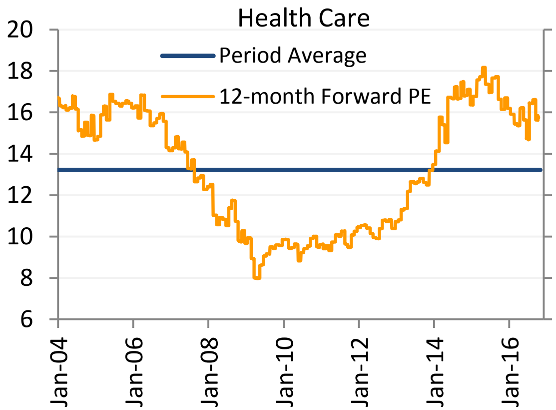
UK Sectors Valuation

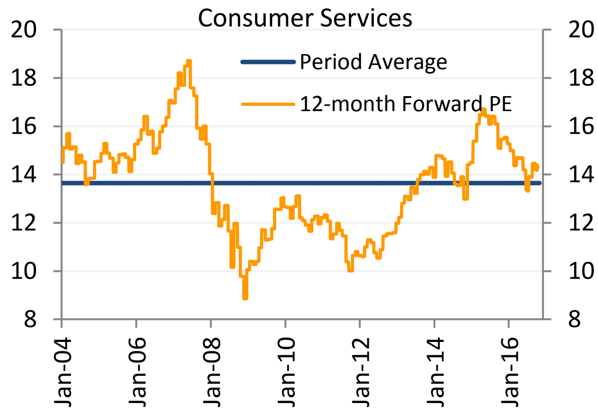


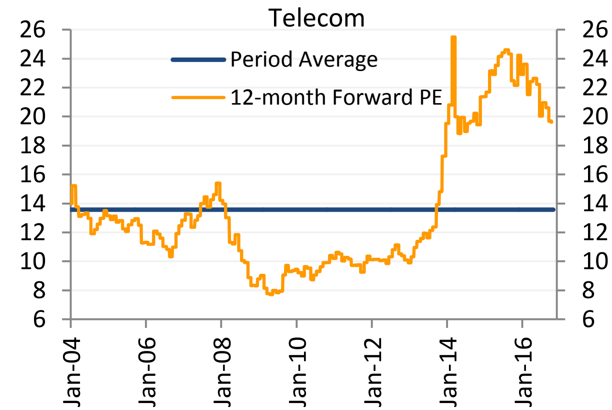


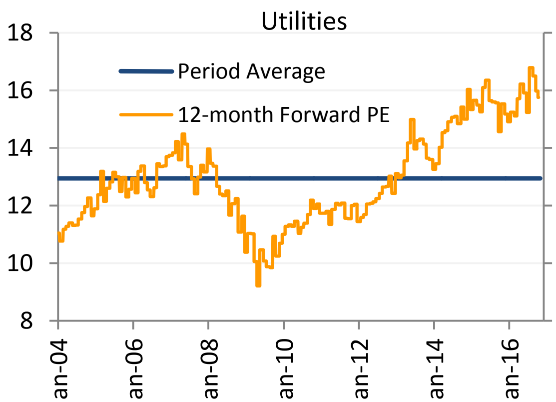


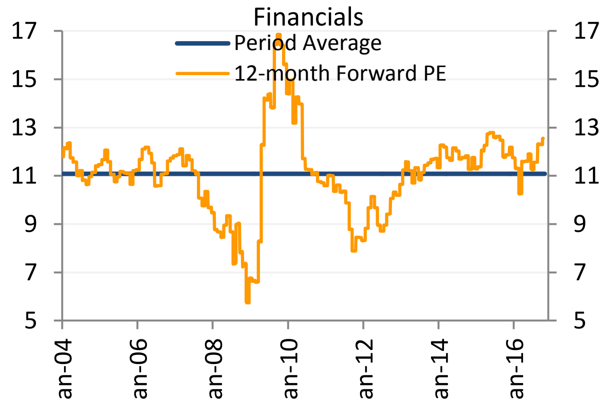


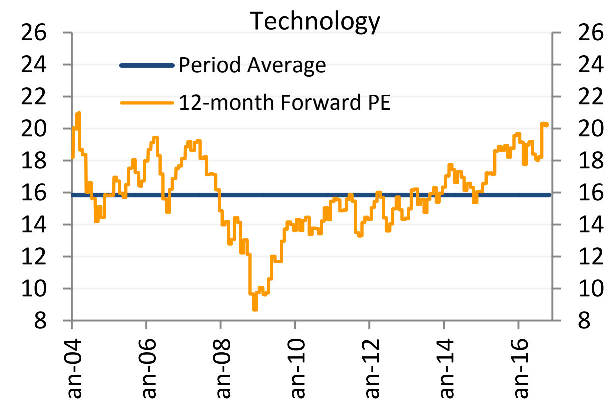












Japan

- Japanese real GDP moderated to 0.7% qoq saar in Q2:16, following a particularly strong +2.1% in Q1. Private consumption slowed (+0.7% qoq saar vs +2.8% in Q1) and net trade subtracted 1.0 pp from growth (+0.4 pps in Q1), due to a strong JPY (+5.2% qoq in real terms in the second quarter). Looking forward, private consumption is expected to continue to support growth via targeted fiscal transfers and real wage growth (0.8% yoy), albeit the Q3 figure could be negatively affected by strong typhoons and heavy rainfall.

- The outlook for business investment has also improved moderately and is expected to provide a (small) positive contribution to real GDP growth amid improving external demand. The PMI manufacturing index averaged c. 50 in Q3:16 (up by 2 pts compared with Q2) and industrial production is currently at +3.7% qoq saar, so far in Q3:16, from +0.8% qoq saar in Q2. However, the JPY appreciation (+5.3% qoq/+19.1% yoy in REER terms in the third quarter), if sustained, poses downside risks to capital expenditure plans and profits for large manufacturers (Tankan Survey).

- Overall, real GDP growth is expected to be 0.6% qoq saar in Q3:16. For FY:2016, real GDP growth is expected to be 0.5% yoy (IMF, October 2016), broadly in line with is potential growth rate.

- In order to support the economic recovery, the Japanese Government unveiled a set of new policy measures, with "true" new fiscal expenditure amounting to ¥7.5tn (or 1.5% of GDP). The Cabinet Office estimates that the aforementioned measures will boost real GDP growth by 1.3%, implying a fiscal multiplier of 0.9. The bulk of the package (60%-80%) will be spread over Fiscal Year 2016 (April 2016-March 2017).

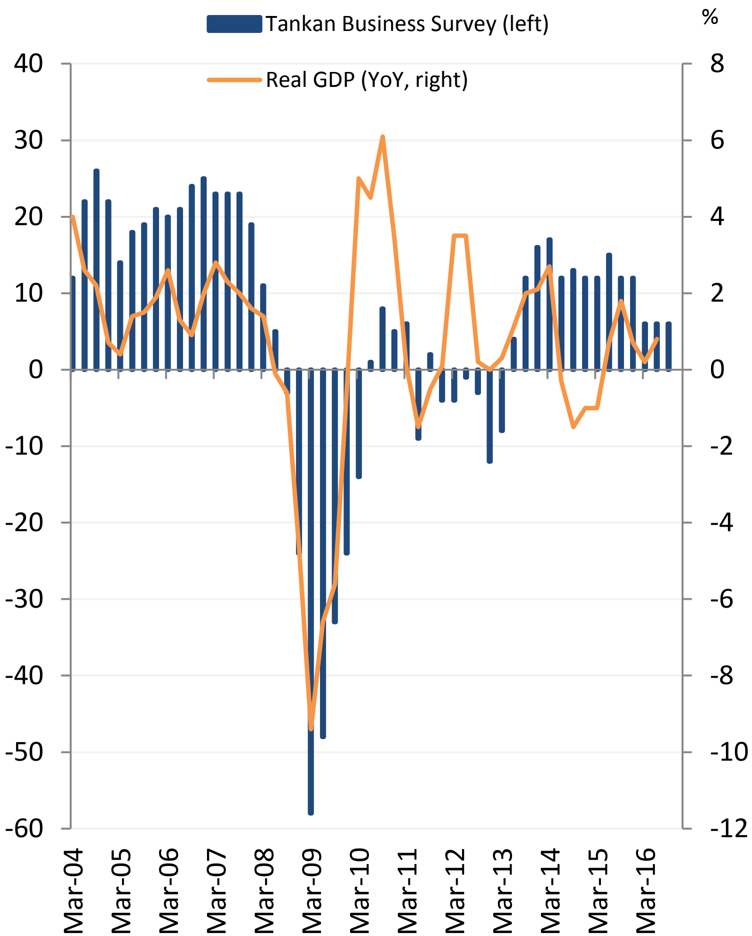
- The Bank of Japan introduced a new policy framework consisting of: i)"yield curve control" in which the Bank will specify short-term policy rates (current: -0.1%) and a target for 10-Year JGB yields at "around current levels of 0%"; and ii) a commitment to expand the monetary base (current: ¥407tn) until actual inflation (CPI excluding fresh food) exceeds and remains above the target of 2% in a stable manner (at -0.5% yoy in August / CPI excluding food & energy at 0.2% yoy).

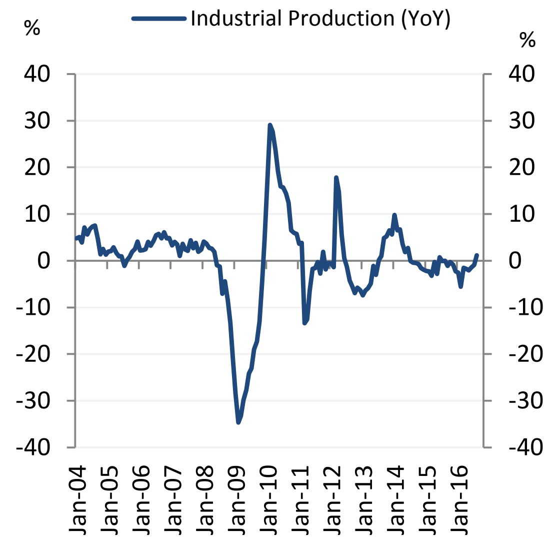
- The BoJ will continue its JGB purchases, "more or less" at an annual pace of about ¥80tn, albeit allowing for significant fluctuations in market operations so as to control the yield curve. Indeed, the BoJ reduced purchases of 5-10Yr JGBs in early October in order to raise the 10Yr yield towards its target.

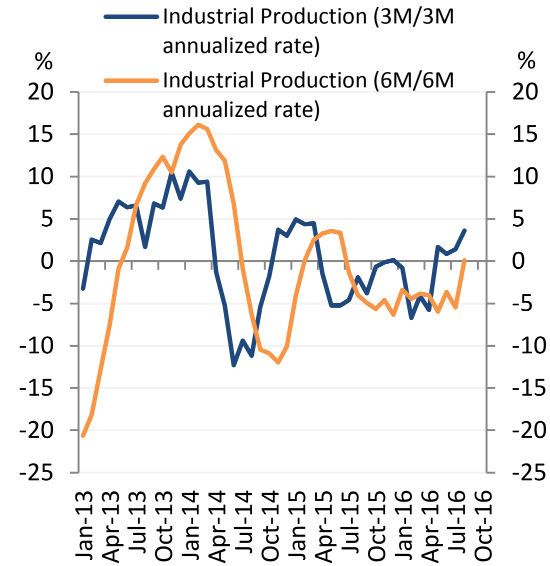
- Labor market tightening continues, with the jobs-to-applicants ratio at a 25-year high of 1.37 in August, implying that labor demand is stronger than supply. The unemployment rate stood at 3.1% in August, close to the 20-year low of 3.0% reached in July. Wages remain on an upward path (+0.3% yoy), albeit failing so far to trigger significantly higher spending.

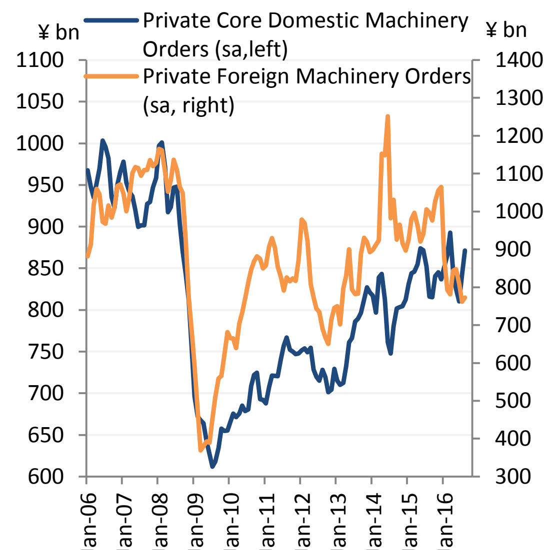
- In Q3, the Nikkei 225 moderately overperformed its peers (+5.6% vs +4.4% for the MSCI DM excluding Japan), albeit it still lags on a YTD basis by -9.4%. Meanwhile, JGB yields remain close to historical lows (10-year yield at -0.07%).

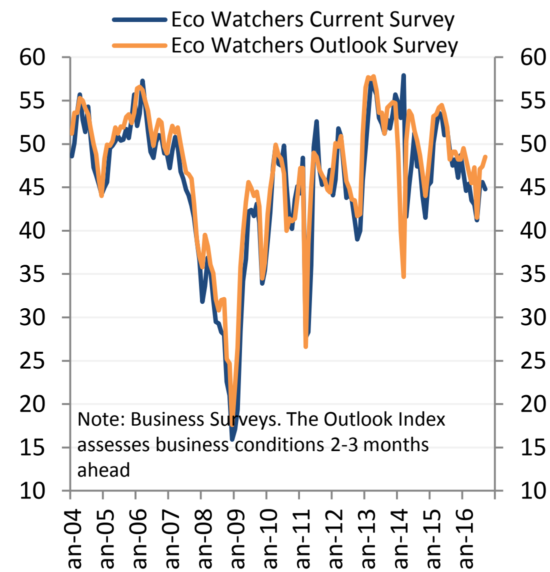
GDP expanded moderately in Q2:16, while the outlook for the business sector has improved recently





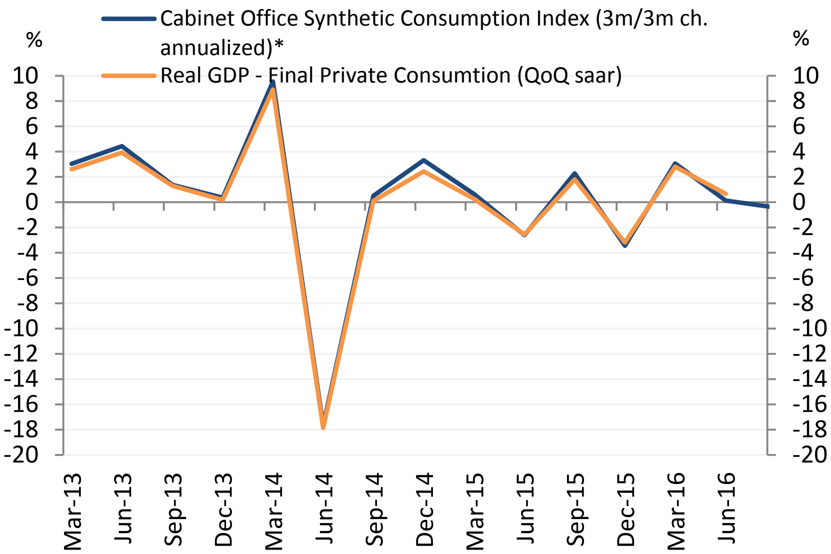


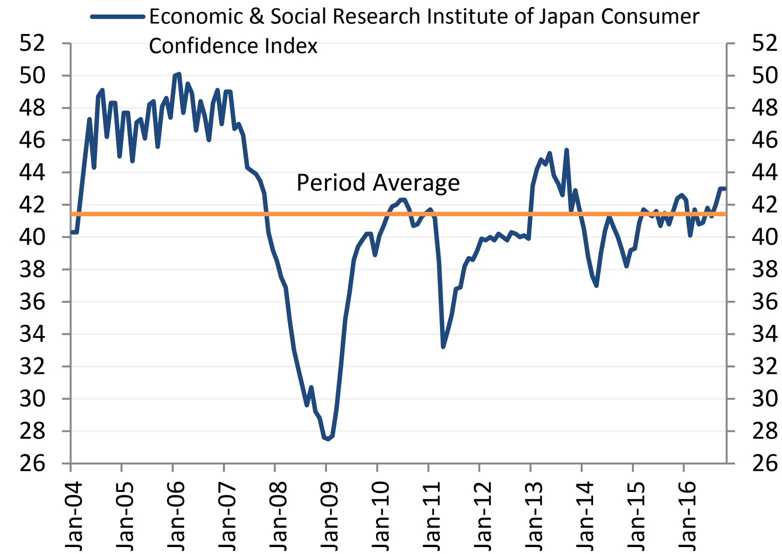


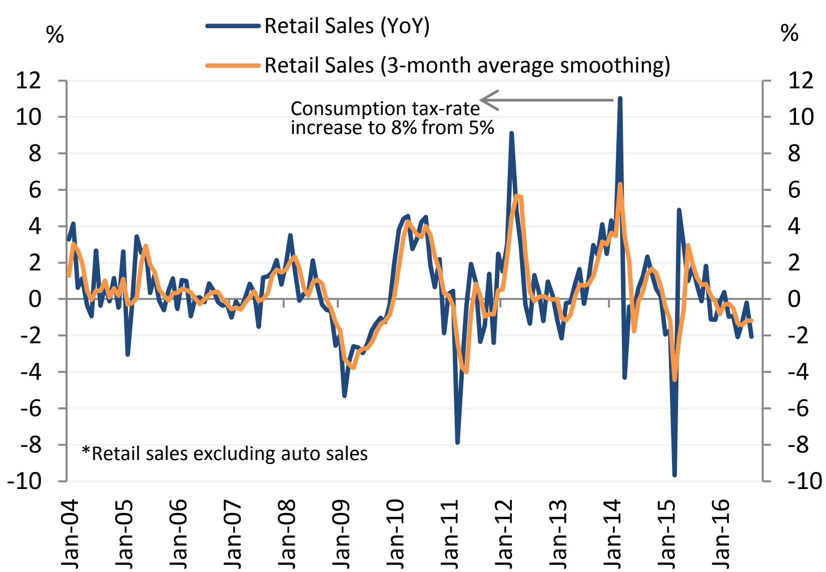


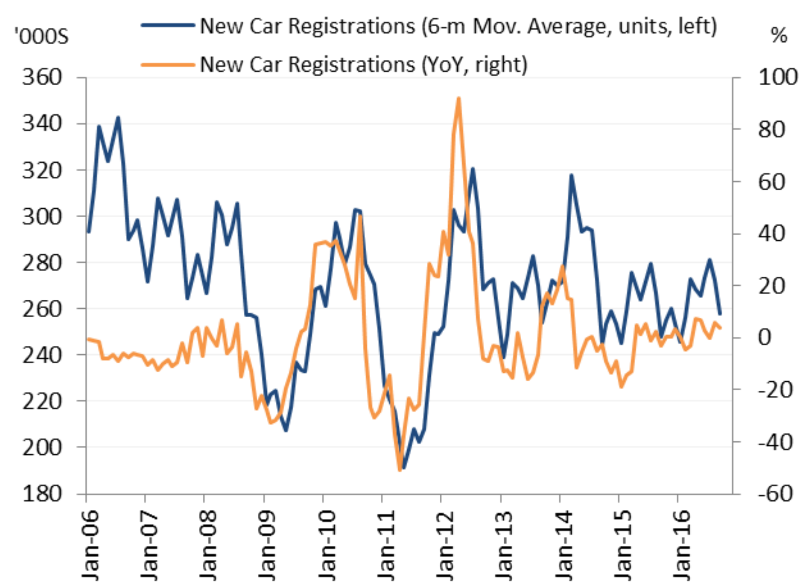
Above: GDP data as of Q2:16 Tankan data as of Q3:2016
Right: Industrial Production & Machinery Orders data as of August 2016, Eco Watchers data as of September 2016
Source: Bloomberg

Consumption growth is expected to decelerate in Q3 according to our tracker







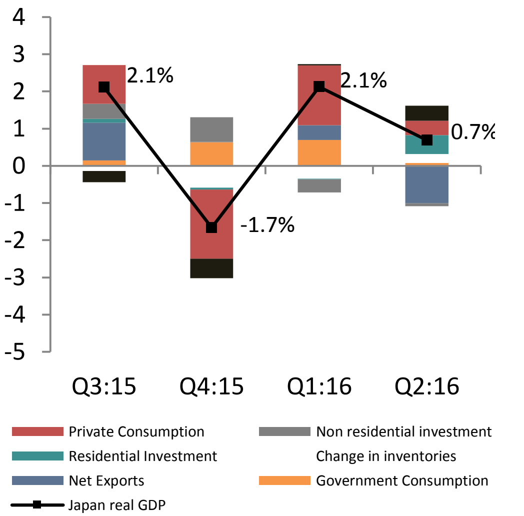


A slight deceleration in real GDP growth is anticipated in Q3:16

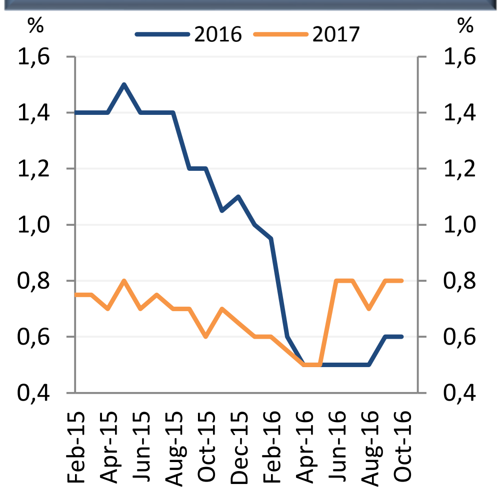
Japan Real GDP Growth	2014	Q1:15	Q2:15	Q3:15	Q4:15	2015	Q1:16	Q2:16	Q3:16e	Q4:16e	2016e
GDP (YoY)	**-0,1**	-0,9	0,7	1,8	0,8	**0,6**	0,1	0,8	0,4	1,1	**0,6**
GDP (QoQ saar)	-	5,0	-1,9	2,1	-1,7	-	2,1	0,7	0,4	1,2	-
Private consumption (QoQ saar)	-0,9	0,2	-2,6	1,8	-3,2	-1,2	2,8	0,7	-0,1	1,5	0,3
Government consumption (QoQ saar)	0,1	1,0	1,5	0,7	3,3	1,2	3,6	0,4	2,0	1,7	2,1
Private residential investment (QoQ saar)	-5,0	11,0	7,0	4,3	-1,8	-2,7	-0,5	21,6	1,2	0,8	4,5
Business investment (QoQ saar)	2,8	12,9	-3,8	3,0	5,0	1,6	-2,6	-0,6	0,7	0,4	0,4
Public investment (QoQ saar)	0,2	-5,4	3,7	-7,1	-12,2	-2,0	1,0	10,8	3,1	-0,1	-0,6
Private Inventories contribution (QoQ saar)	0,2	2,1	1,0	-0,1	-0,6	0,5	-0,4	0,2	0,0	0,1	-0,1
Net Exports contribution (QoQ saar)	0,3	0,5	-1,9	1,0	0,0	0,4	0,4	-1,0	-0,1	-0,1	-0,1
Exports (QoQ saar)	8,3	6,9	-15,8	10,6	-3,7	2,8	0,4	-5,8	0,4	1,2	-1,4
Imports (QoQ saar)	7,2	4,4	-6,9	5,0	-4,2	0,3	-2,1	-0,2	1,4	1,7	-0,9

Source: Cabinet Office, Department of National Accounts, Bloomberg

GDP Contributions (%)

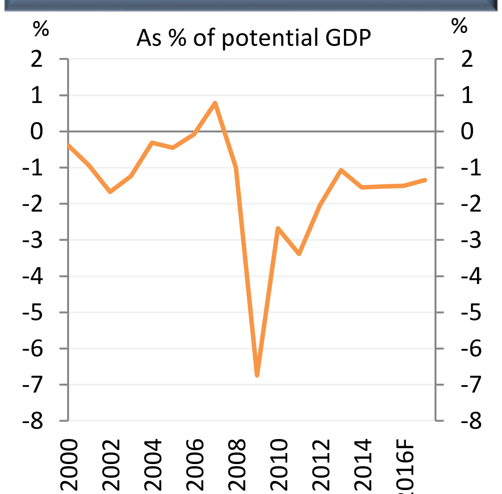


GDP Forecast Evolution



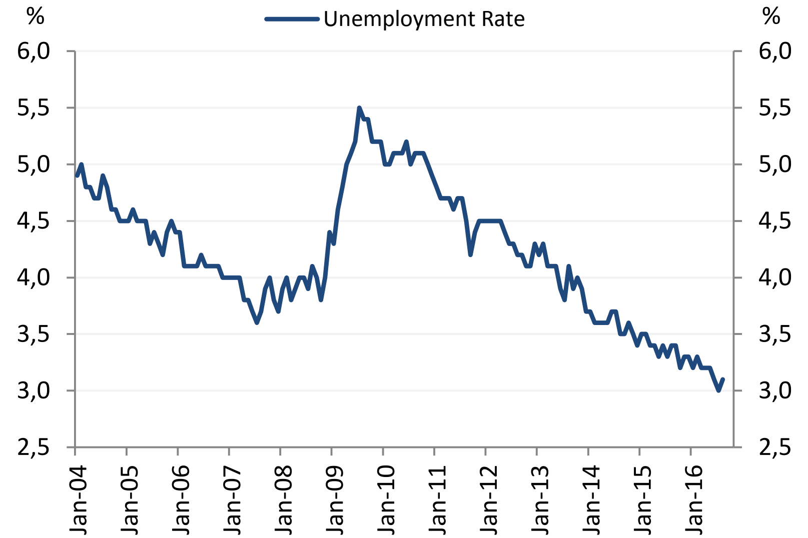
Source: Bloomberg Consensus

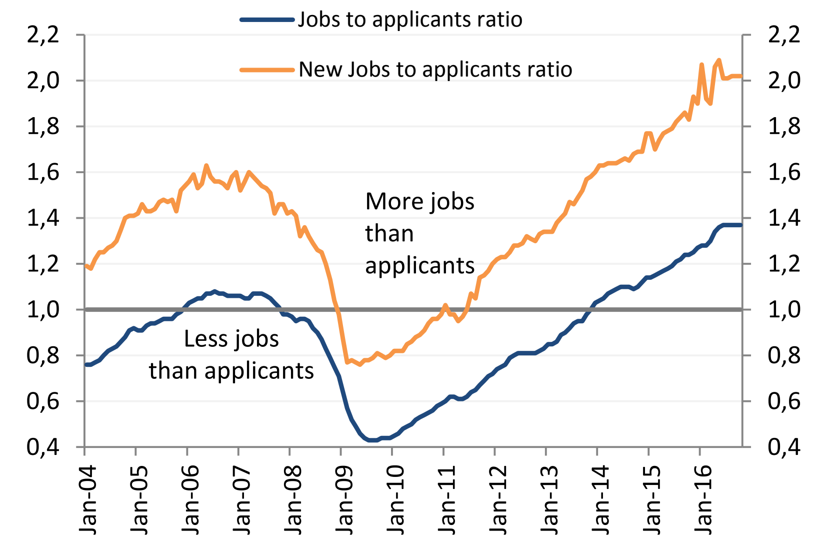
Output Gap

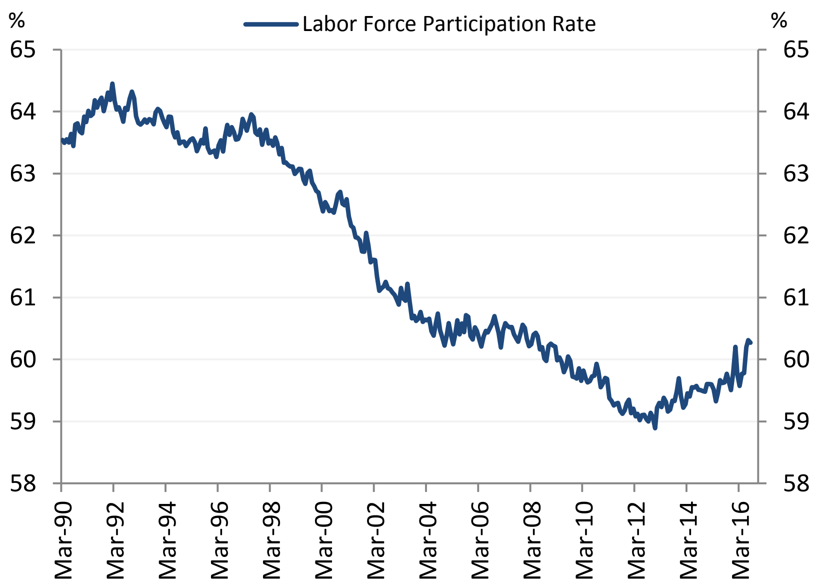


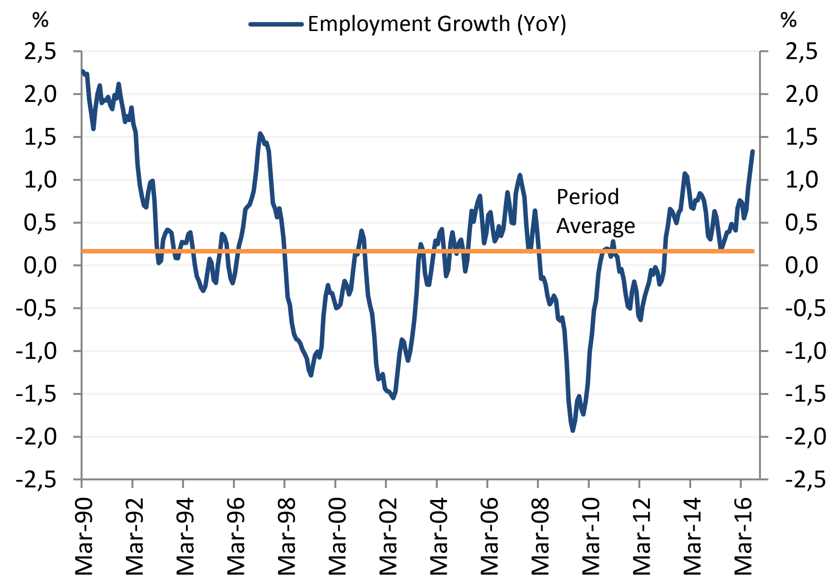
Source: IMF

Labor market tightening continues, with the jobs-to-applicants ratio at a c. 25-year high of 1.37 in August

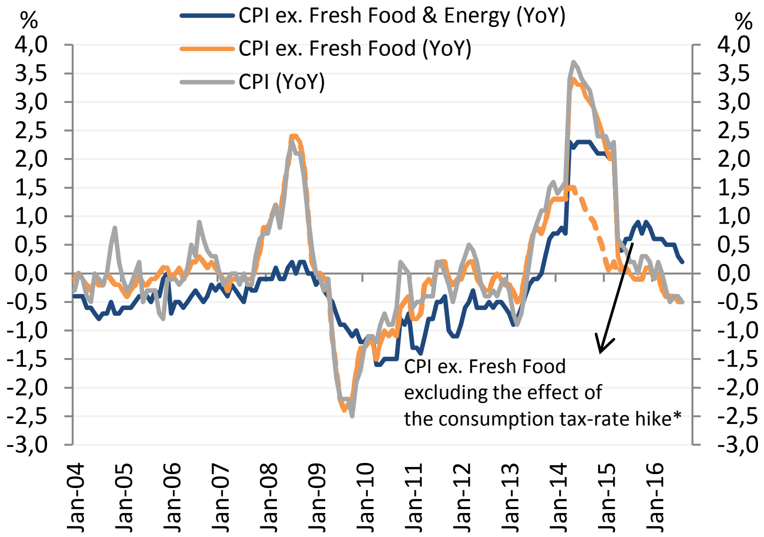




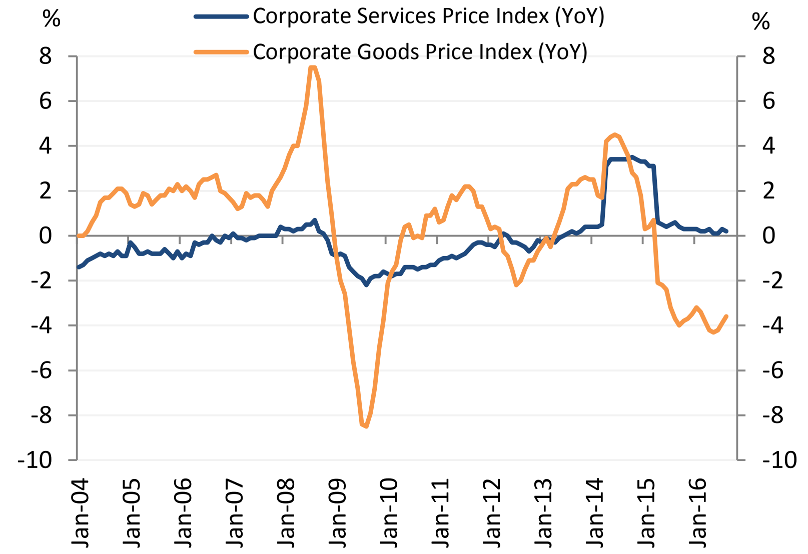


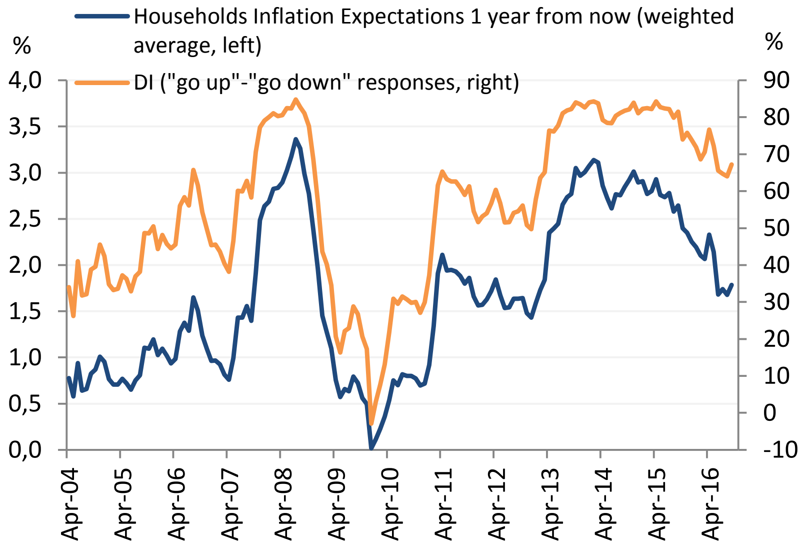


Inflation remains subdued and wage growth modest

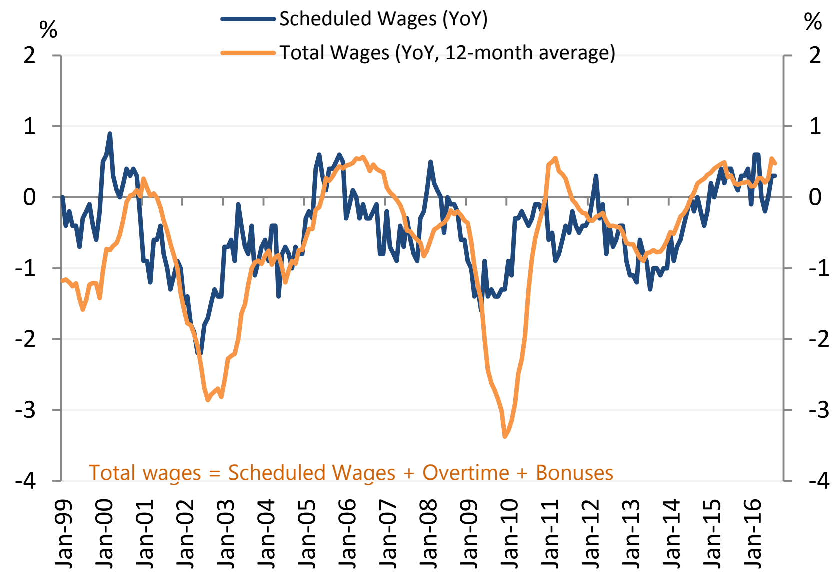


Consumption tax rate hike effect: 1.8%-2% up to March 2015, 0.3% for April 2015, no effect from May 2015, Source: Bank of Japan

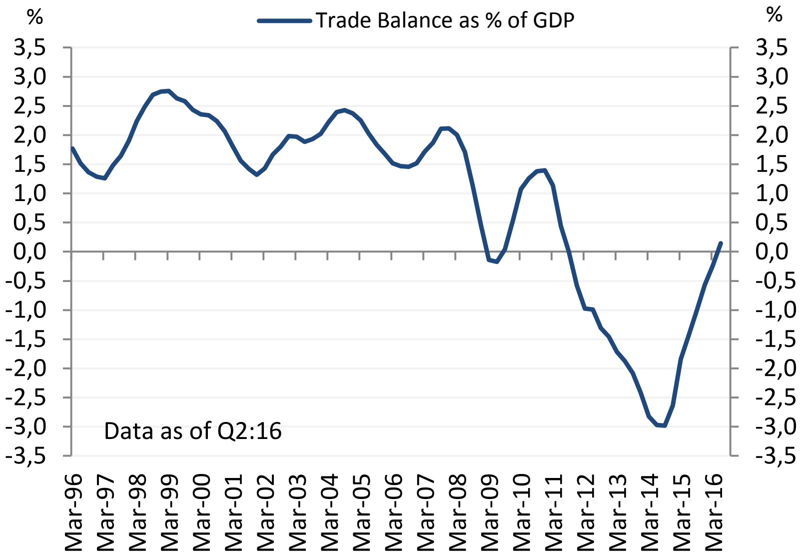


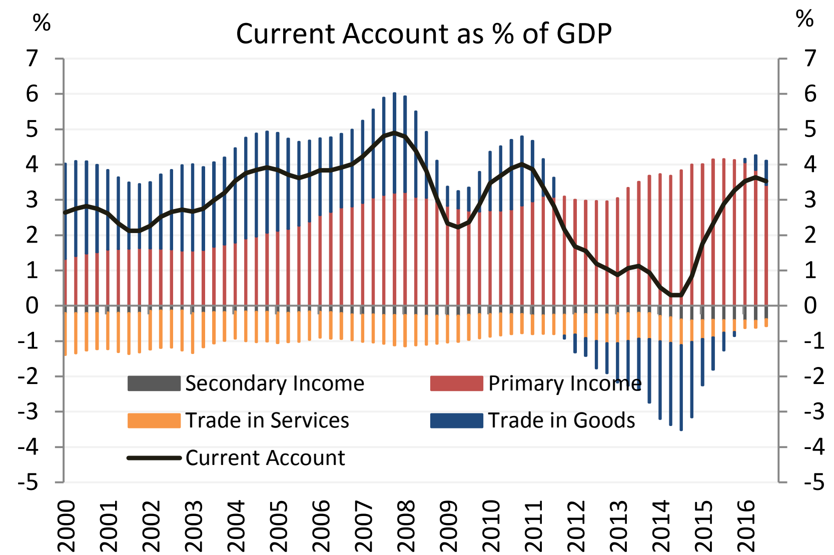


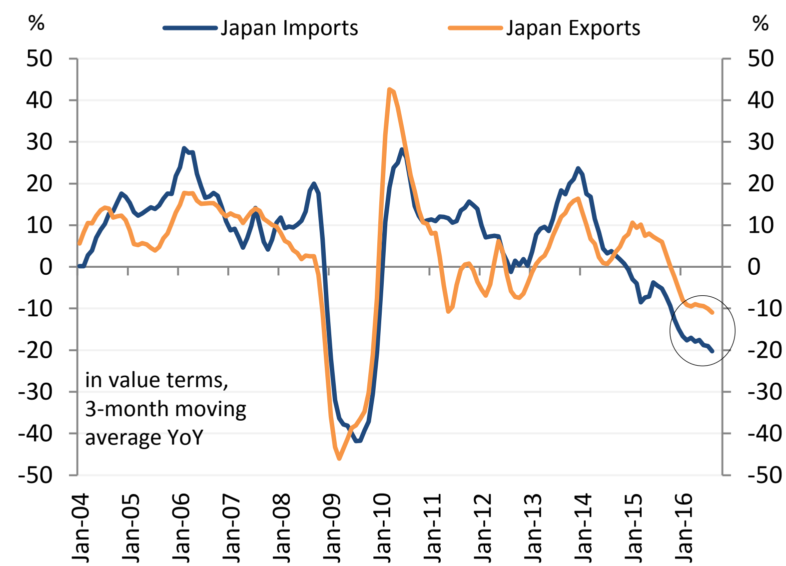
Source: Cabinet Office (September Consumer Confidence Survey)

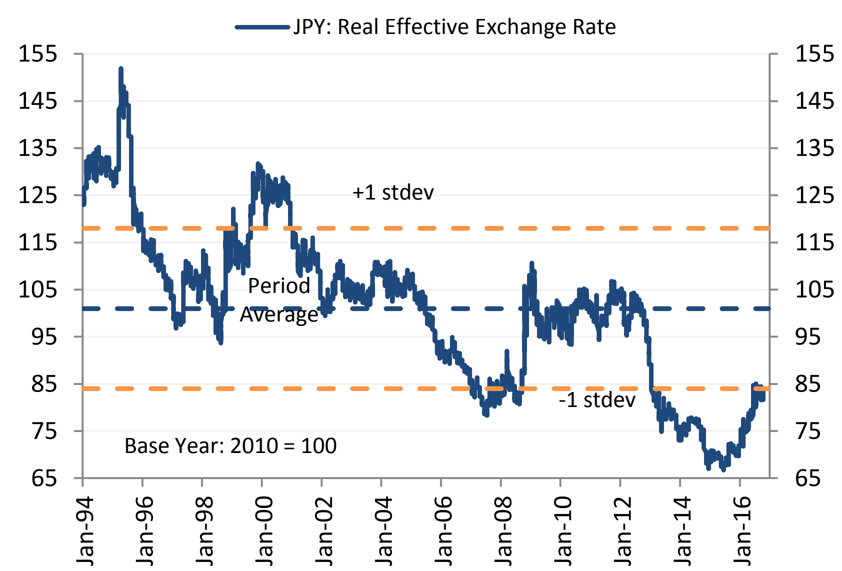


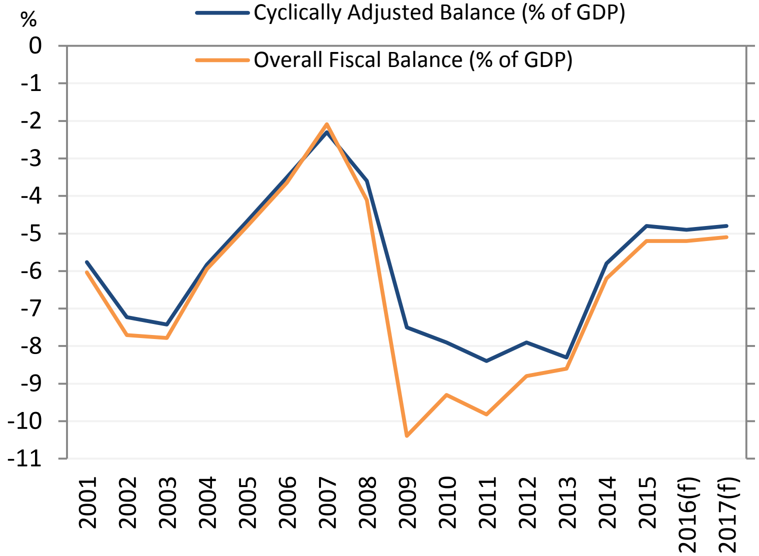
The stronger Yen (+5.3% qoq/+19.1% yoy in REER terms in Q3) jeopardizes the substantial improvement in the trade balance (12-month sum: +0.1% of GDP in Q1:16 vs -3% in Q3:14)



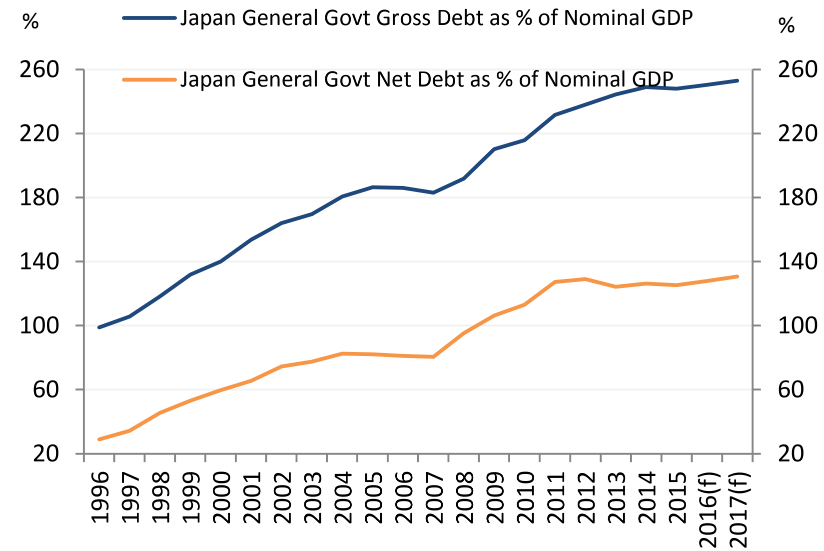




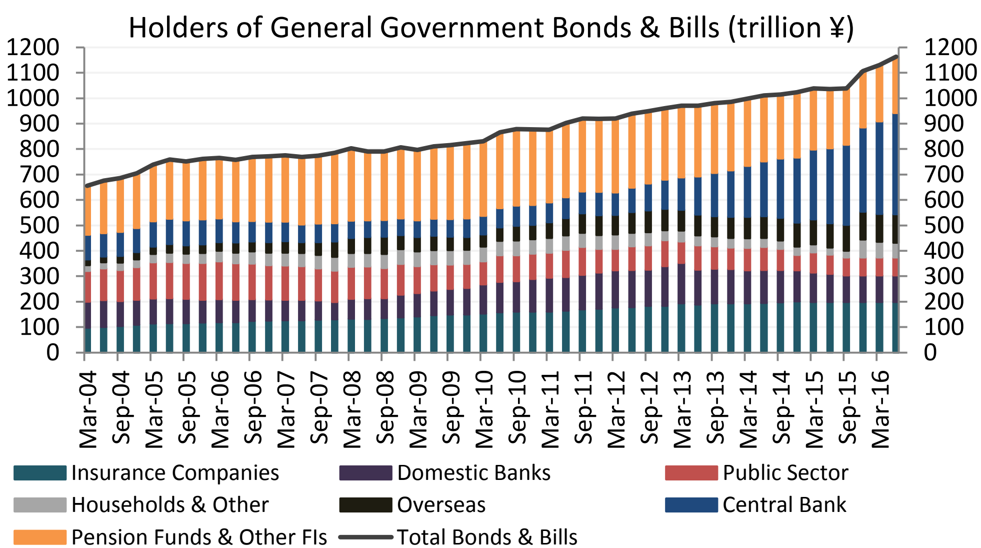




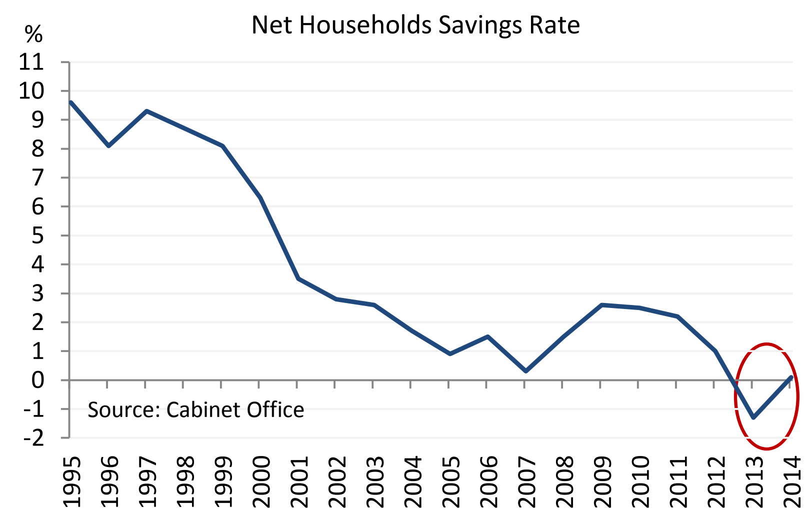
Source: IMF Fiscal Monitor, October 2016



Source: IMF Fiscal Monitor, October 2016

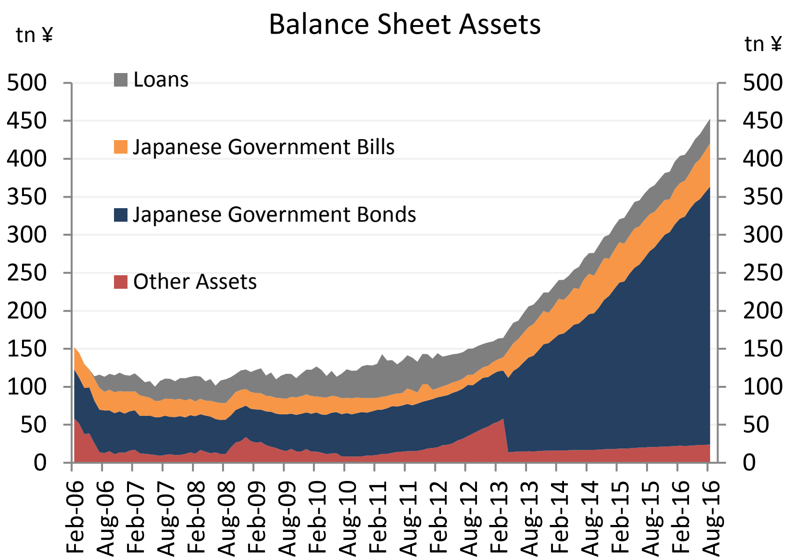


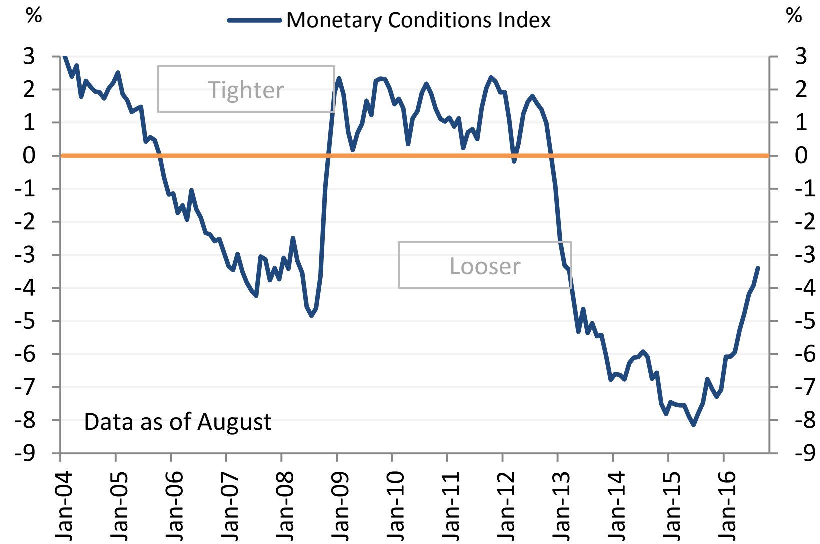
Source: Bank of Japan, Bloomberg (quarterly data, as of Q2:16)



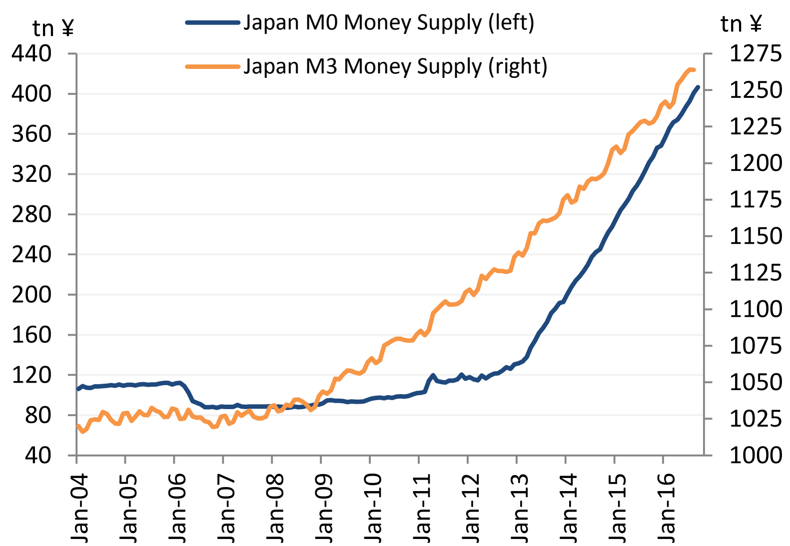
Note: Data appear for Fiscal Years, i.e. from April 1 of mentioned year to March 31 of the next year (e.g. 2013 accounts for 1/4/2013 - 31/3/2014)

The Bank of Japan introduced a new policy framework aiming, *inter alia*, to control the yield curve

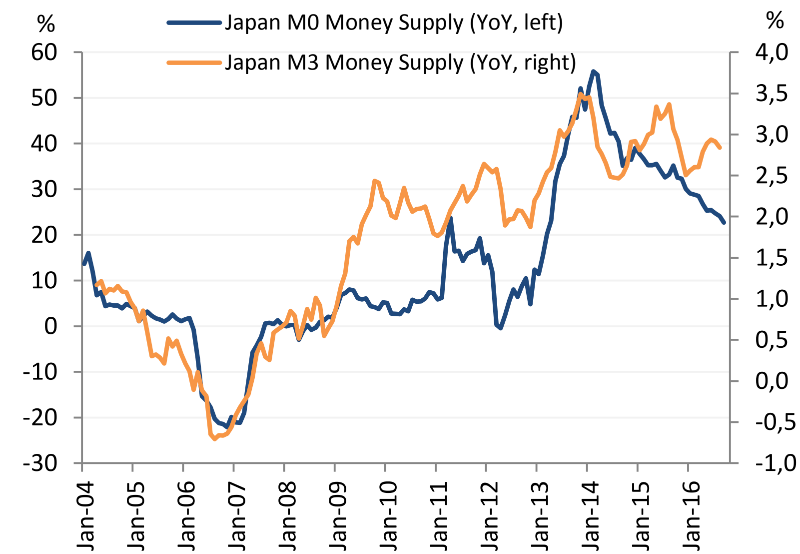




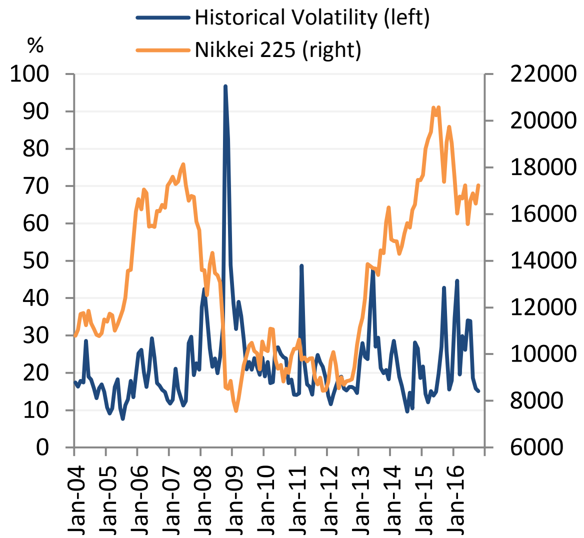
Monetary Conditions Index is a simple composite index of Real Short Term Rates (Tibor less CPI) & Real Effective Exchange Rate

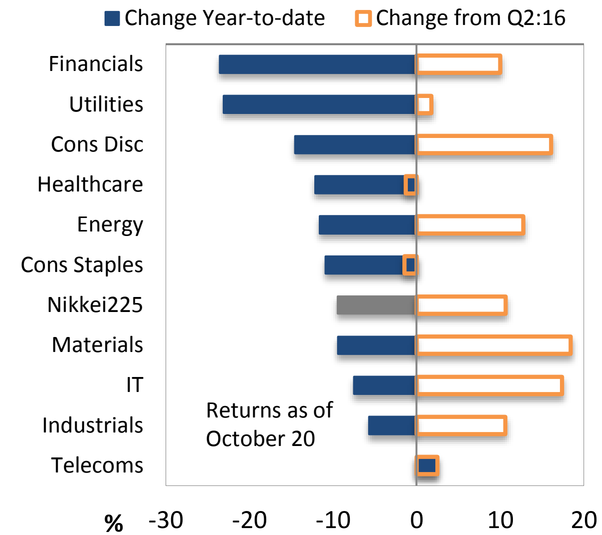


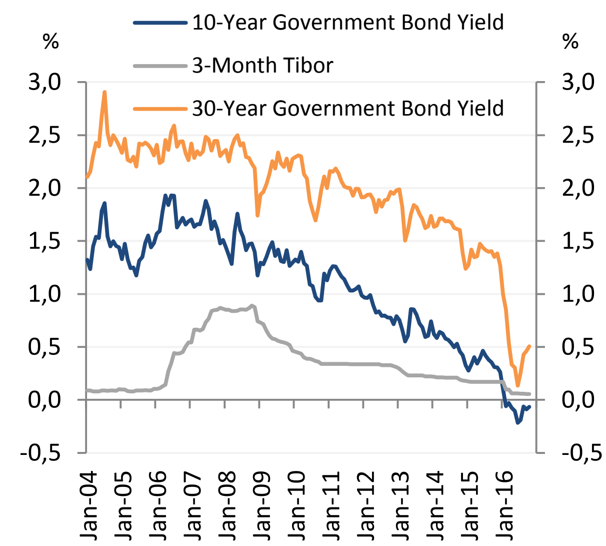
The Bank of Japan targets Monetary Base (M0) expansion of ¥80tn per annum

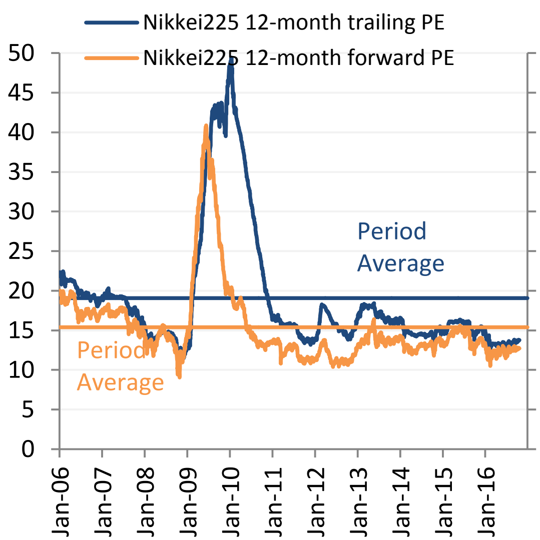


The stronger yen (16% ytd) has weighed negatively on equities (-9% ytd). Since Q2:16, however, the Nikkei225 has rebounded (+10.7%), driven by speculation for further policy stimulus and easing global growth concerns

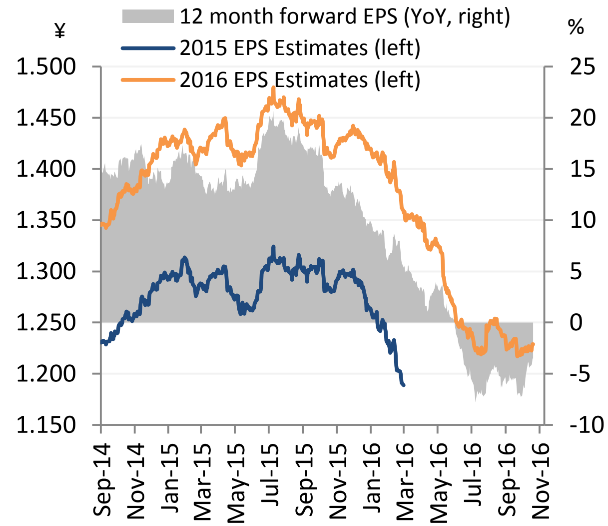




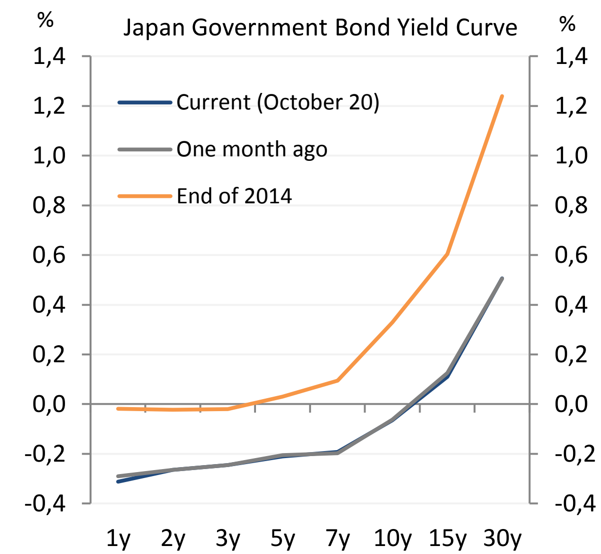




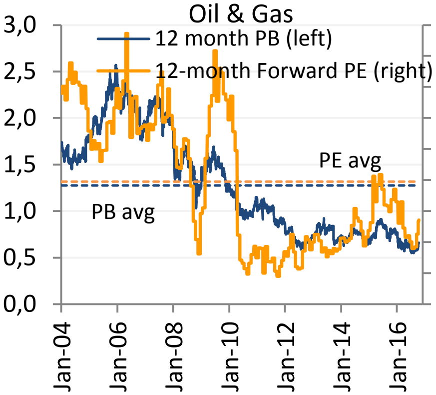
Source: Factset

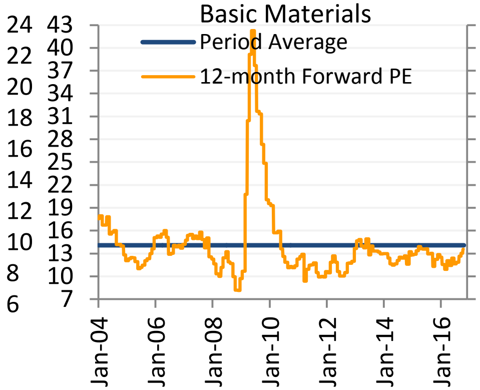


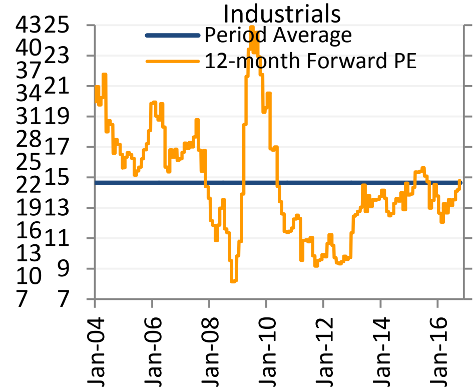
Source: Factset

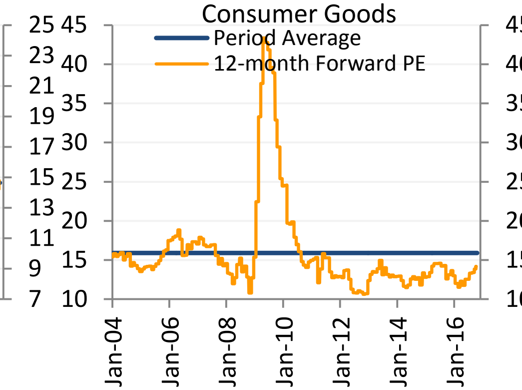


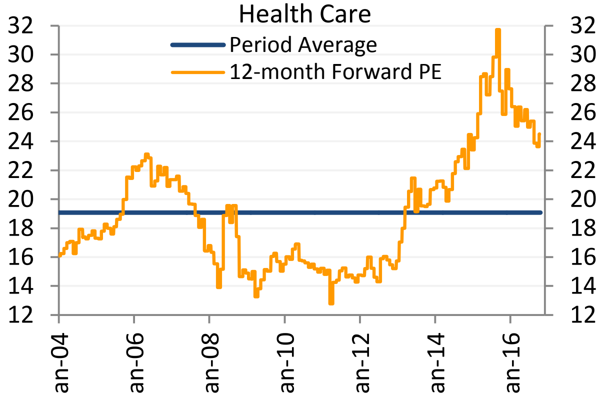
Japan Sectors Valuation

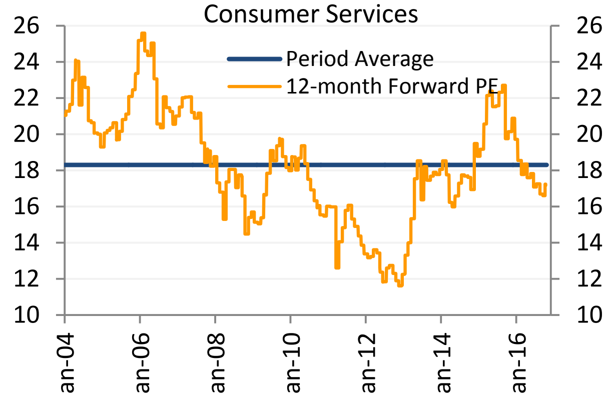


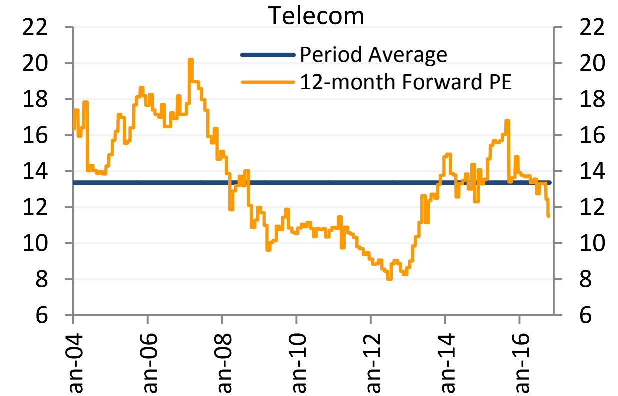


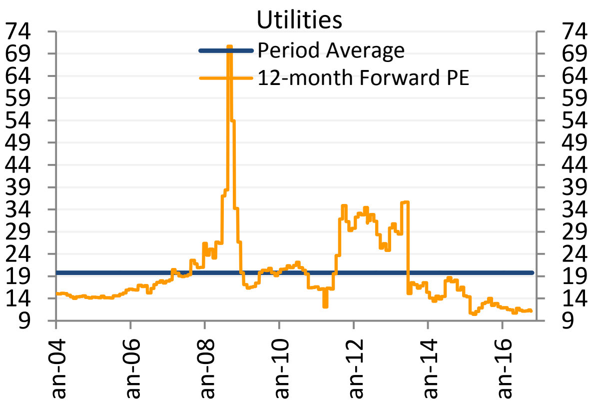


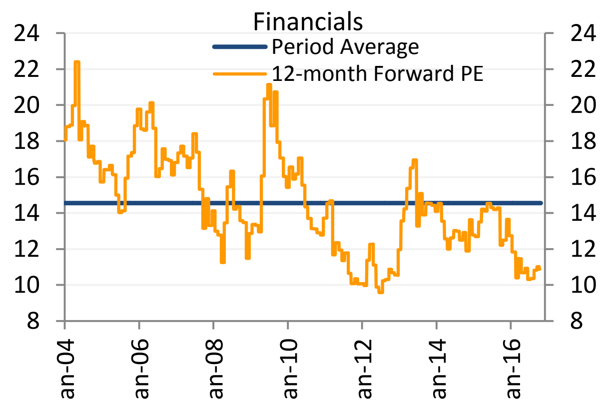


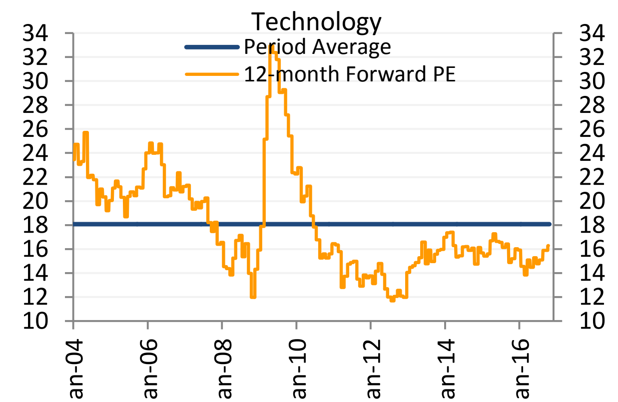








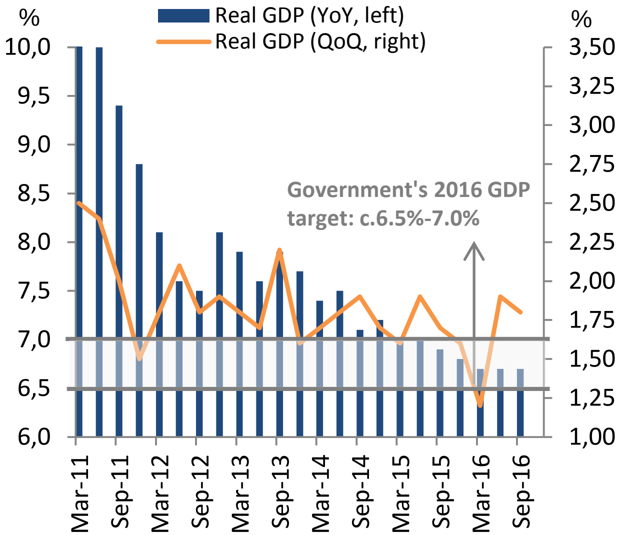


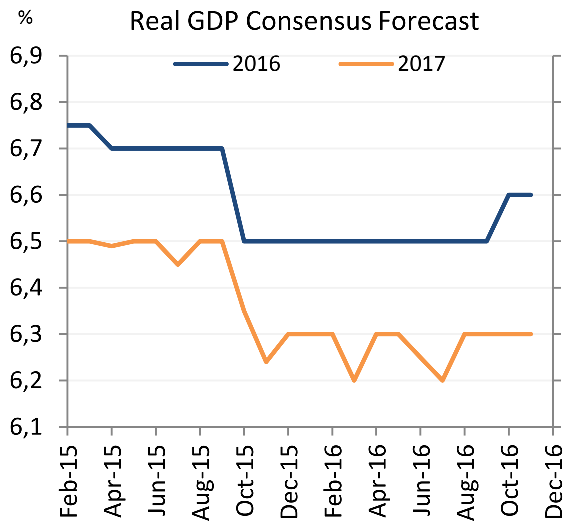


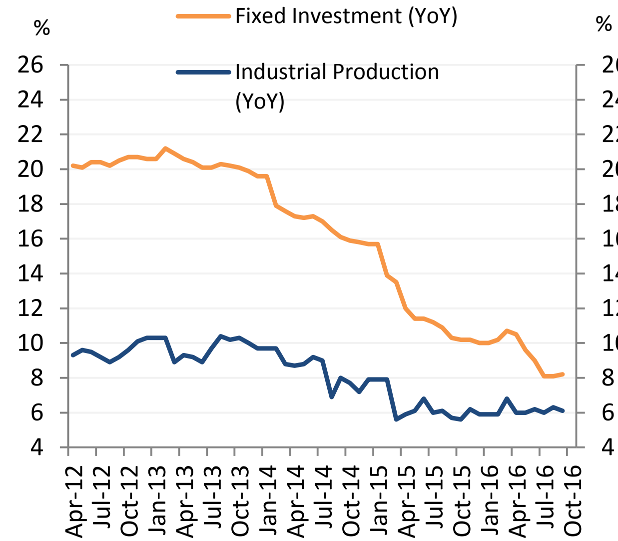
China

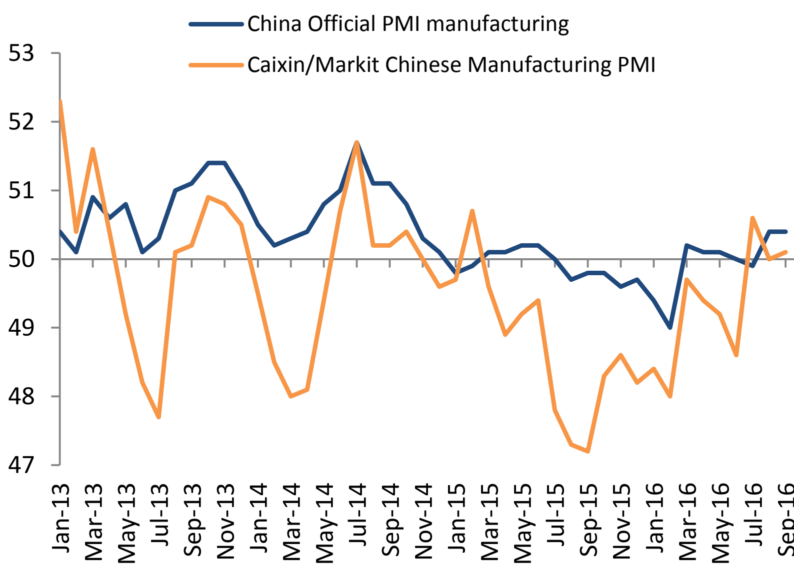
- Chinese economic growth stabilized in the first half of the year, on the back of policy support and robust credit conditions, with real GDP increasing by 6.7% yoy. In H2:16, growth should remain broadly stable (Q3 real GDP came out at 6.7%). As the economy continues its gradual transition from investment to consumption, growth is expected to ease to 6.2% in 2017 (IMF, October 2016).
- High frequency indicators (industrial production, retail sales) showed signs of resilience in September and August, following weaker results in July easing growth concerns. Fixed-assets investment has stabilized in Q3 at 8.1% yoy from 9.7% in Q2.
- Meanwhile, business surveys have improved modestly in Q3:16, compared with H1:16, suggesting a continuing momentum in activity. Specifically, the official manufacturing PMI increased to 50.2 (on average) in Q3:16 from 50.1 in Q2 and 49.5 in Q1.
- House prices continue to accelerate (+9.0% yoy in September, the highest since January 2014). House price inflation has been on an accelerating path since April 2015 (see page 60), raising concerns about a housing bubble. The valuation metrics appear stretched, with the price-to-rent ratio at 136% (>120% usually implies overvaluation for real estate prices), while the price-to-disposable income ratio is especially high at Tier-1 cities (Shenzhen: 130%, Shanghai: 126% compared with a national average of 80%).
- In response, the Chinese authorities announced a set of measures to curb this trend, introducing home purchase restrictions on families with more than 1 home, and limiting to 50% the premium paid on land auction sales. The effect of these measures should be negative for residential investment.
- Short-term risks have eased, as fiscal policy (GG balance as % of GDP is expected at -3.0% in 2016 from -2.7% in 2015) and monetary conditions remain supportive. Nevertheless, high corporate and quasi-Government debt levels raise the risk of a disorderly deleveraging that could hurt growth. Indeed, the private sector debt-to-GDP ratio stood at c. 210% in Q4:15, having almost doubled since Q4:2008 (117%). The authorities introduced recently a debt-to-equity swap programme (DES), under which banks will be encouraged to take stakes in Non-Financial Corporations, in order to reduce excessive leverage in the private sector. The DES will be performed on "market terms" and will exclude so-called "zombie" firms.
- Domestic credit growth as measured by the total social financing (TSF) exhibits resilience, rising to 11.9% yoy in September from 11.7% in August, albeit slower than the pace recorded in March (12.9% in March). The growth of outstanding RMB loans (c. 70% of TSF) was stable at 13% yoy (14.9% yoy in March).
- Capital outflows showed signs of acceleration, with FX reserves down by $39bn in Q3 from -$7bn in Q2 and -$118bn in Q1. The RMB (which was included in the IMF's SDR basket) has declined, on average, by 2.0% qoq against the USD to RMB6.66/$ in Q3:16 (-5.7% yoy). Forwards prices suggest a further depreciation of the RMB by 1.1% against the USD to 6.75 RMB/$ by end 2016. The prospect of an interest rate increase by the Fed will continue to exert downward pressure on the RMB, risking further capital outflows. Nevertheless, in conjunction with positive data surprises, Chinese equities have rebounded, with the CSI300 index up 3% qoq in Q3:16 (-11% year-to-date).

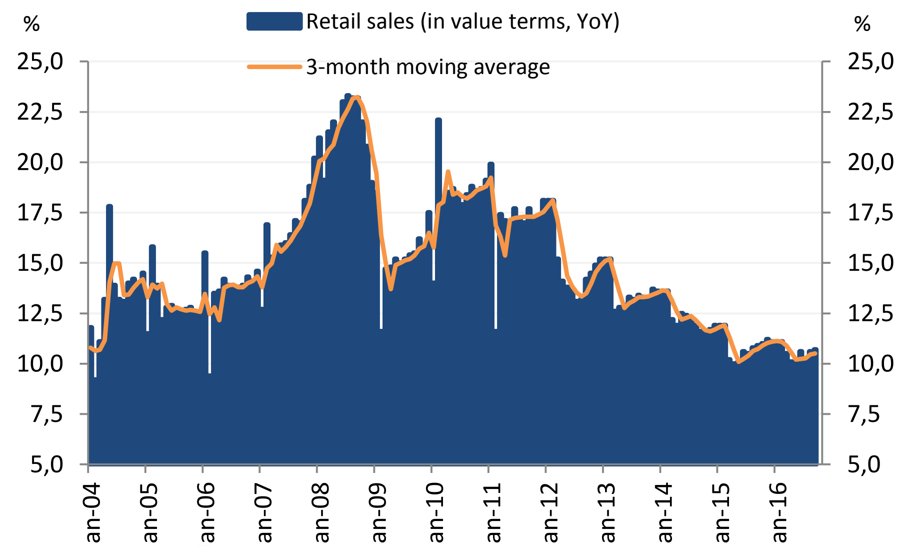
Real GDP growth was stable in Q3 (6.7% yoy), while consensus has upgraded its 2016 growth outlook marginally (+0.1 pp) to 6.6%





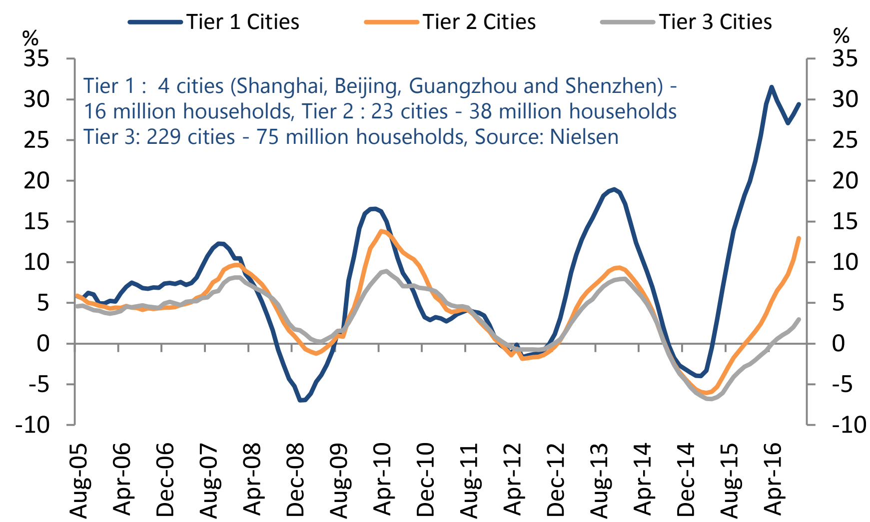




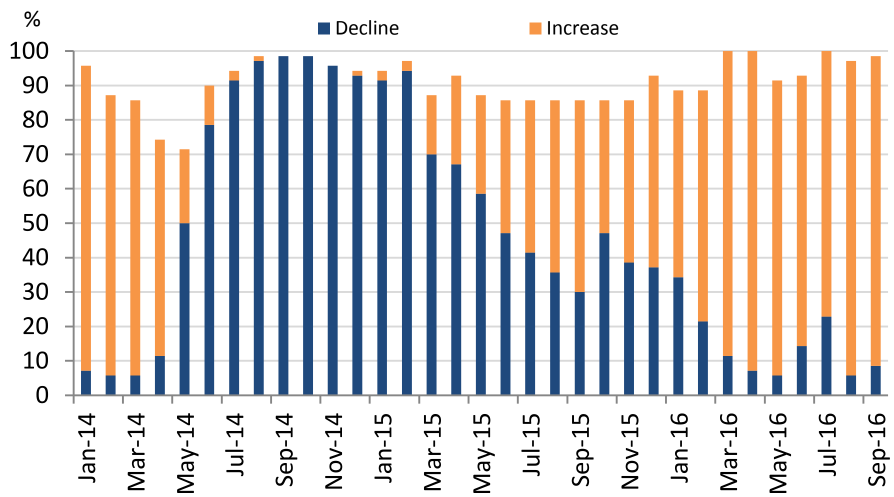


A particularly strong housing market recovery has increased concerns for the sustainability of recent price gains (80-120% compared with 2011 levels)

House Prices: Annual Growth Rate

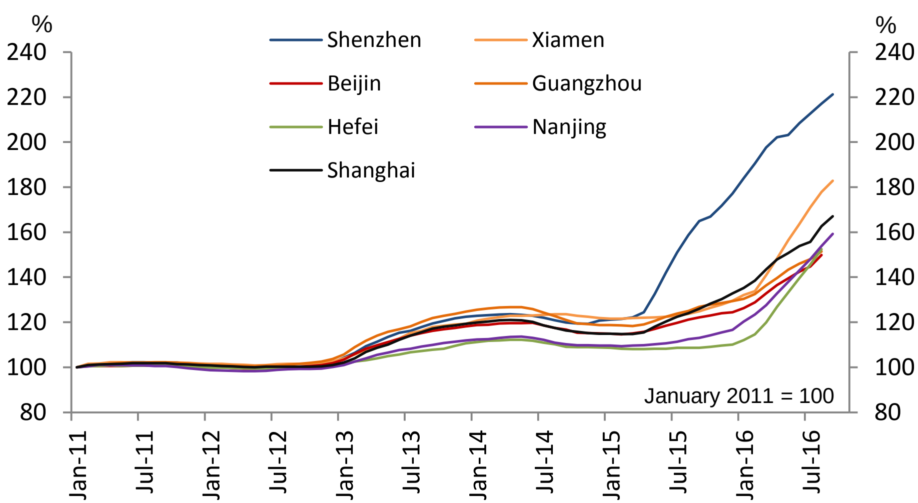


House Prices: Monthly Increases/Declines as % of Total*

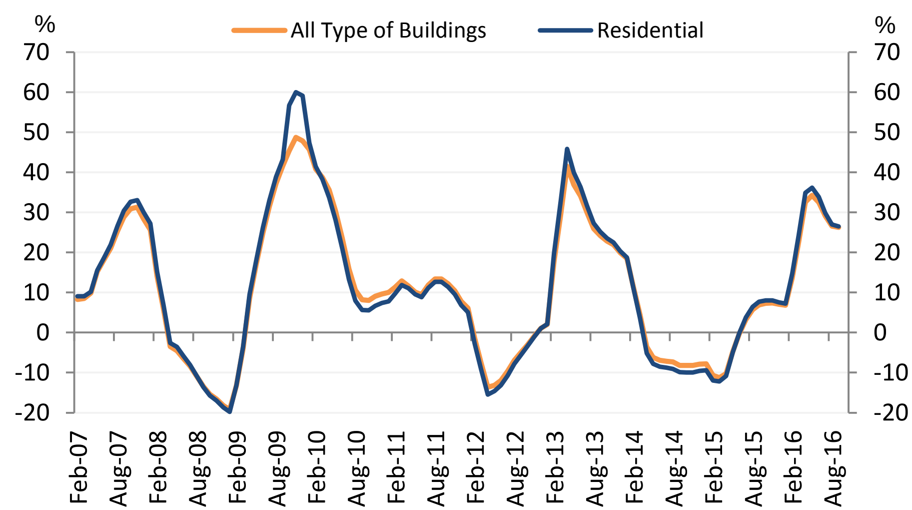


*% of cities (out of 70) where new residential apartments' prices either declined or increased

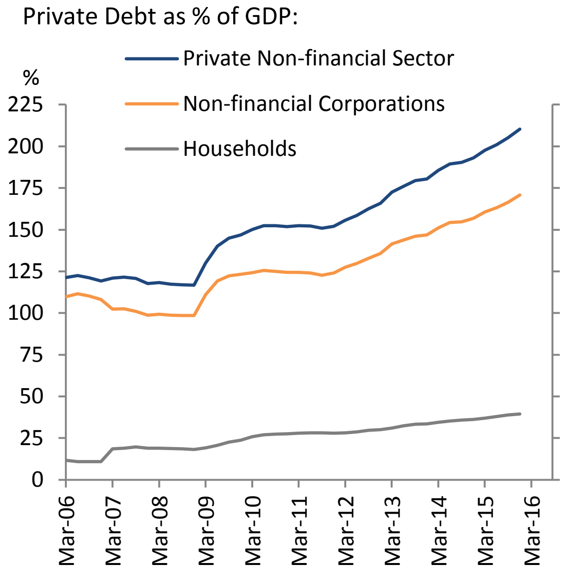
House Prices Indices in Major Cities

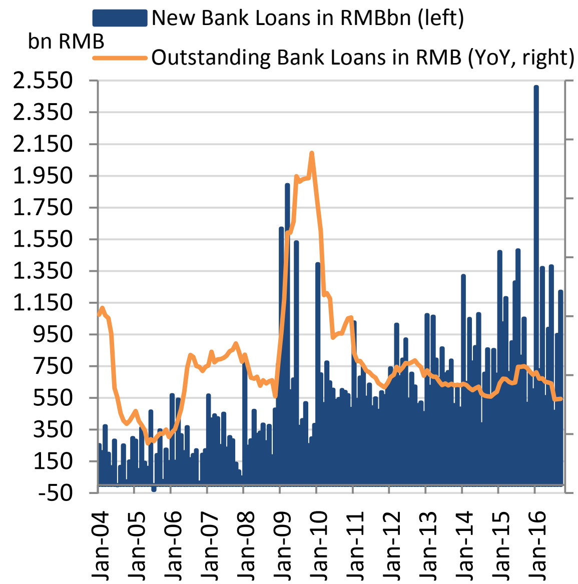


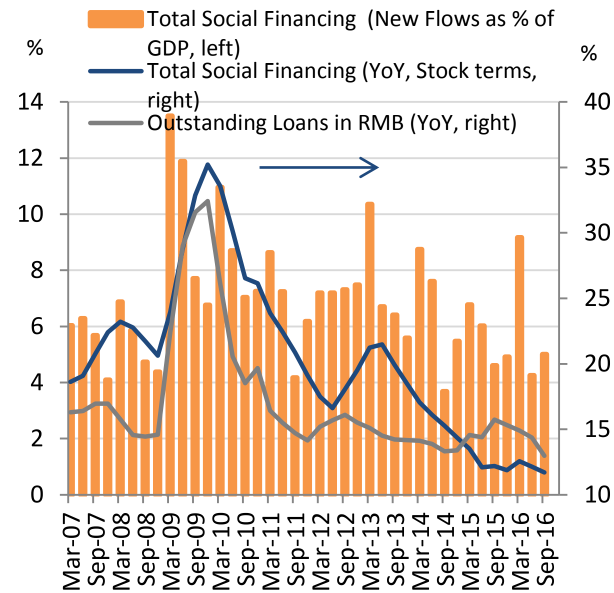
Housing Transactions: Volumes, YoY

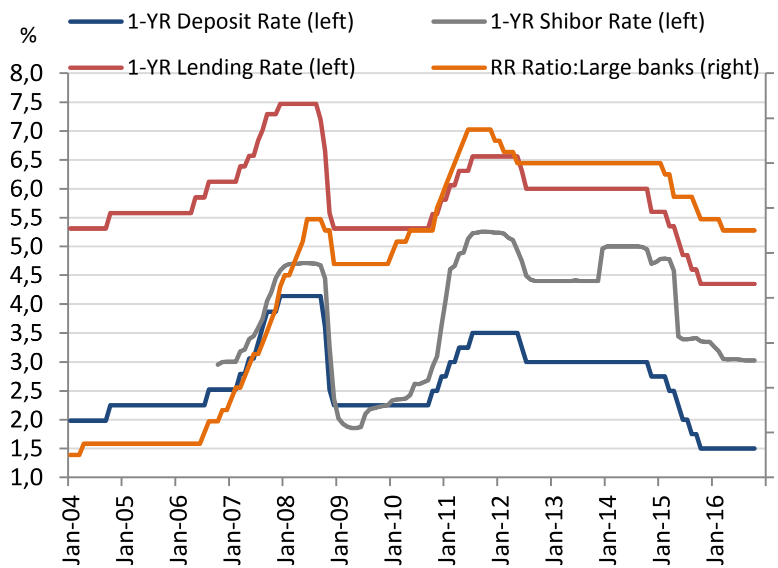


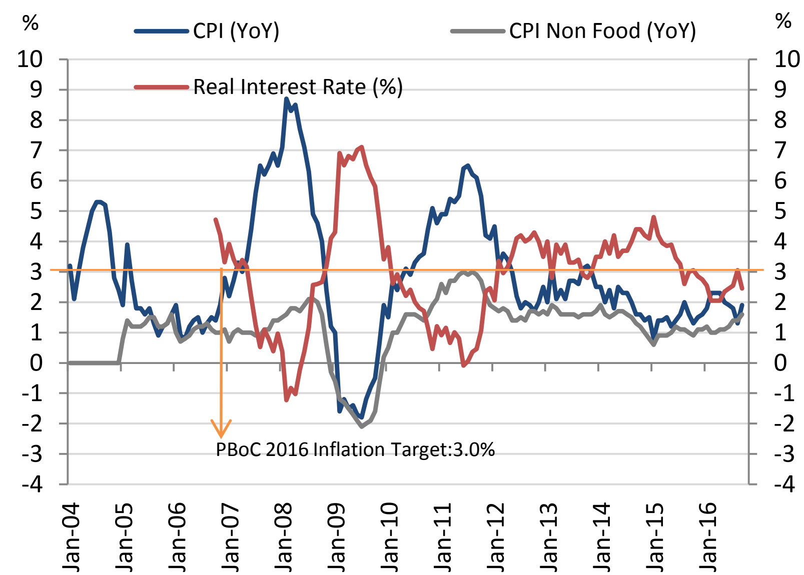
High private debt levels remain a cause for concern amidst an easing medium-to-long term growth outlook



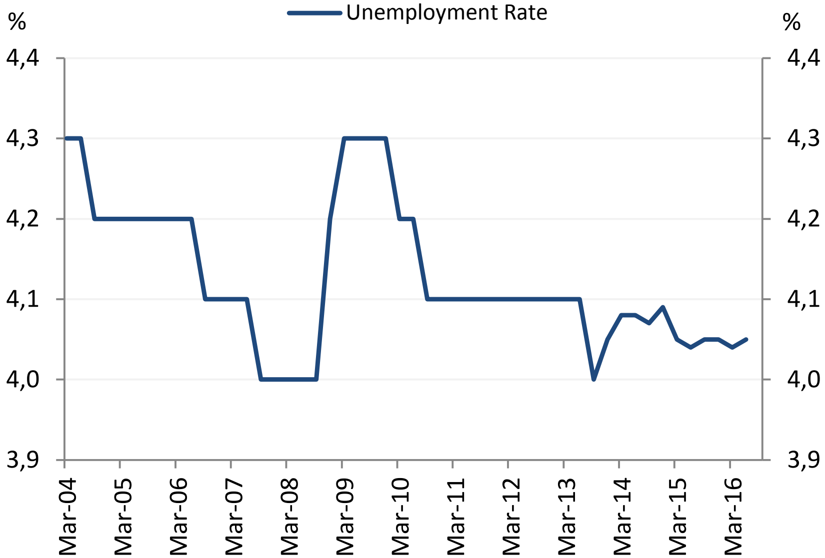




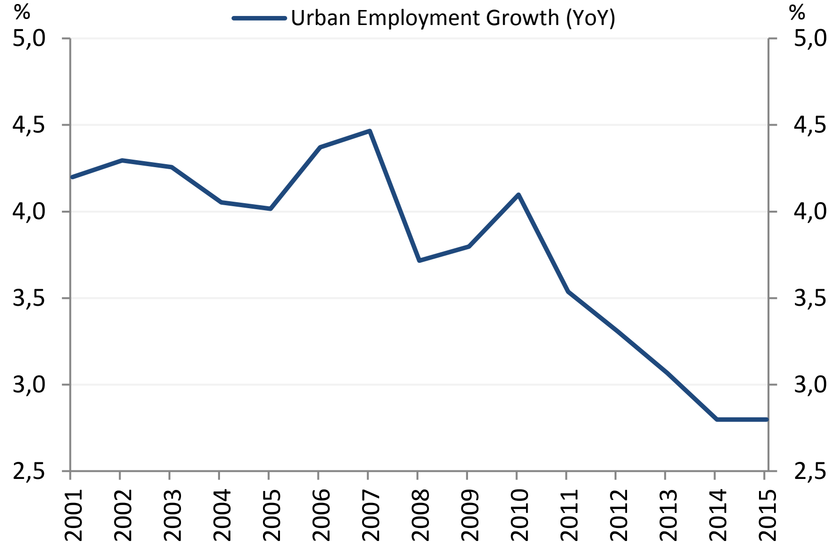




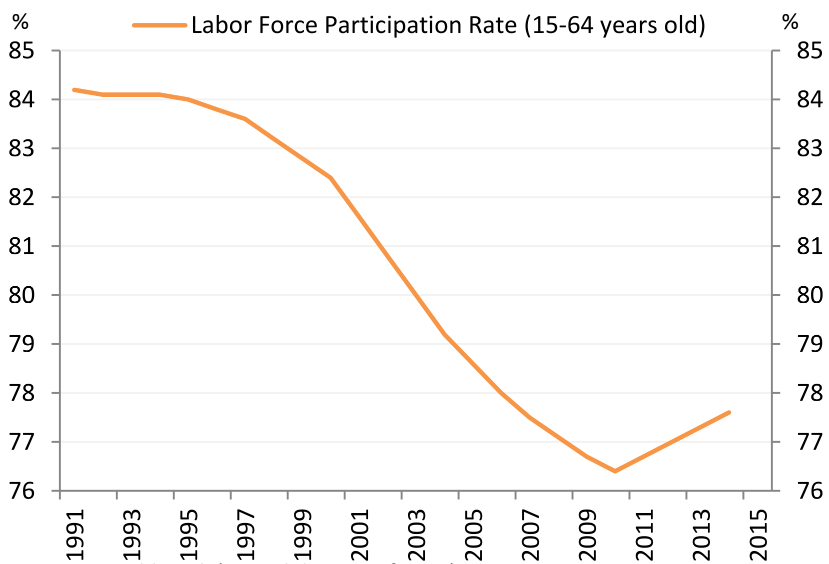
Labor market fundamentals remain solid



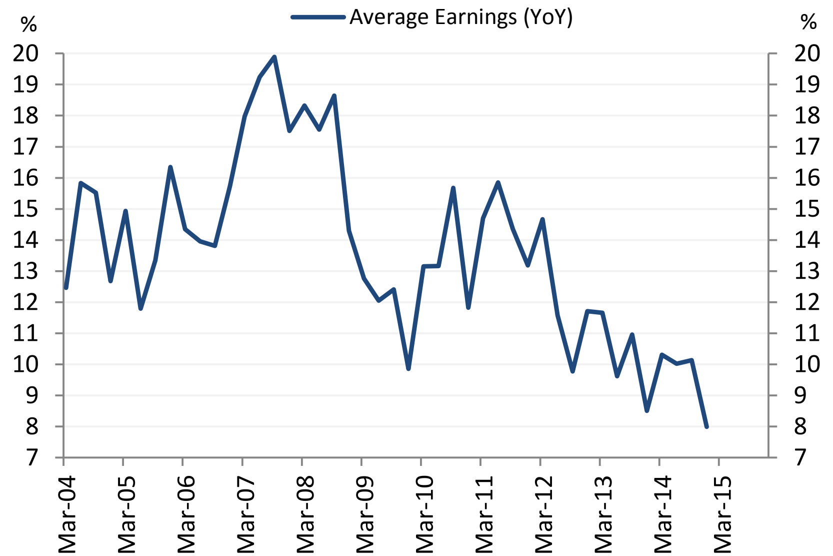
Source: Bloomberg



Source: National Bureau of Statistics, Datastream

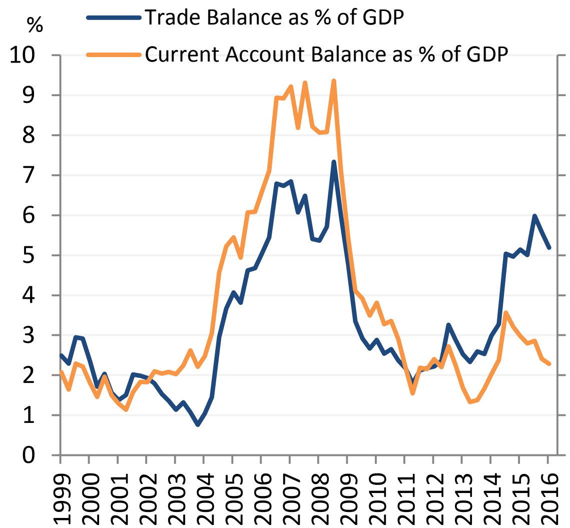


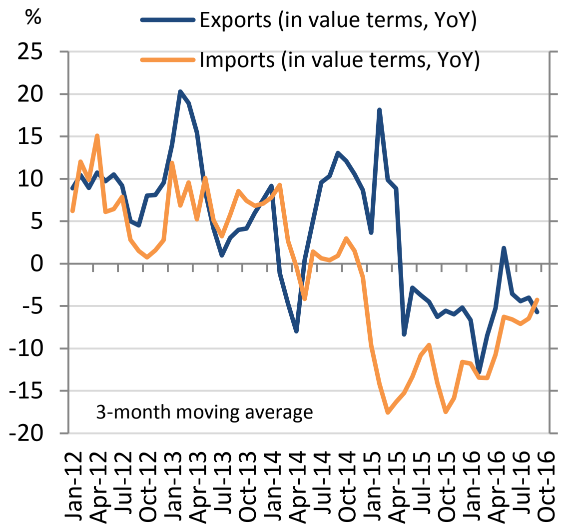
Source: World Bank (annual data, as of 2014)

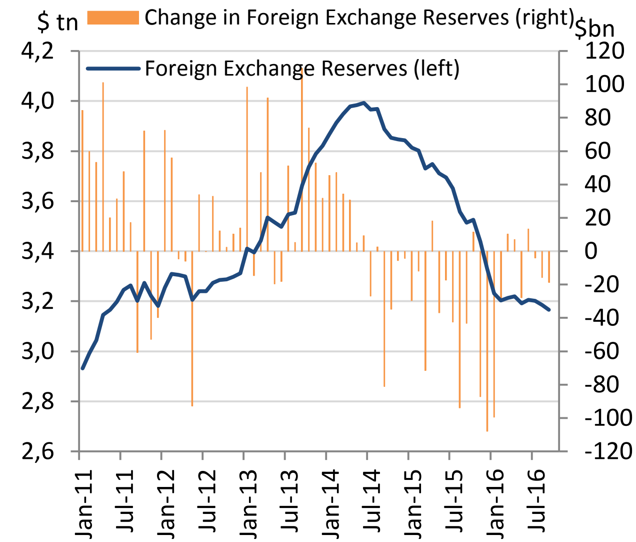


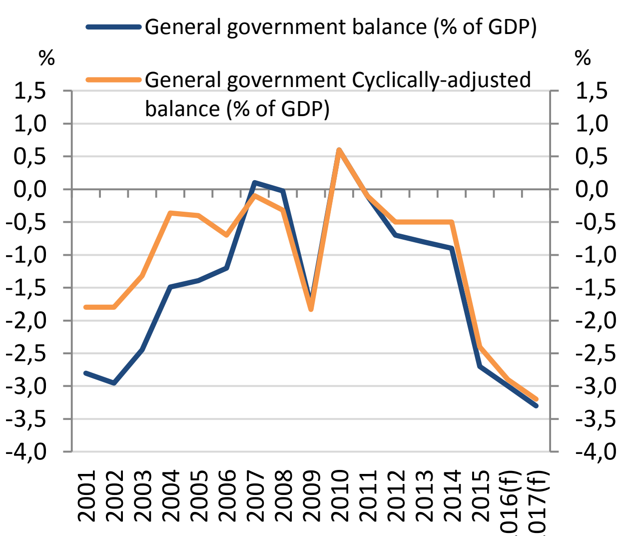
Source: National Bureau of Statistics, Bloomberg

Capital outflows showed signs of acceleration in Q3, with FX reserves down by -$39bn

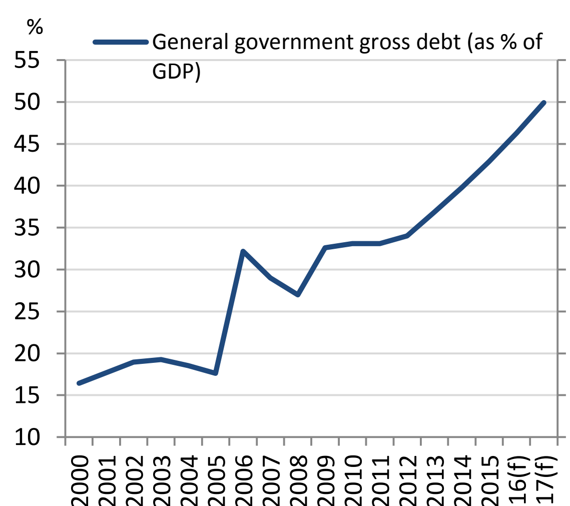




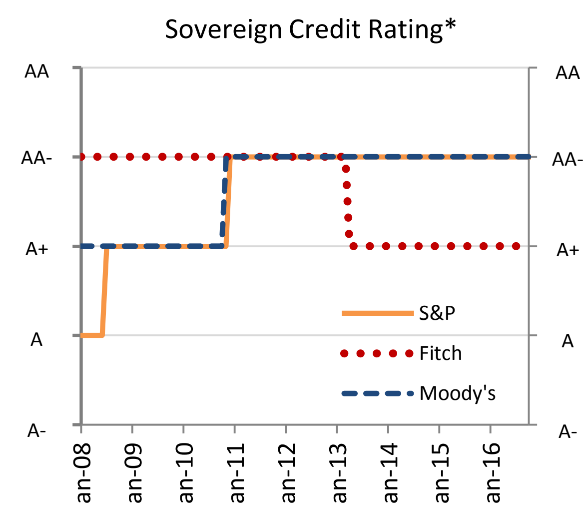




Source: IMF Fiscal Monitor, October 2016

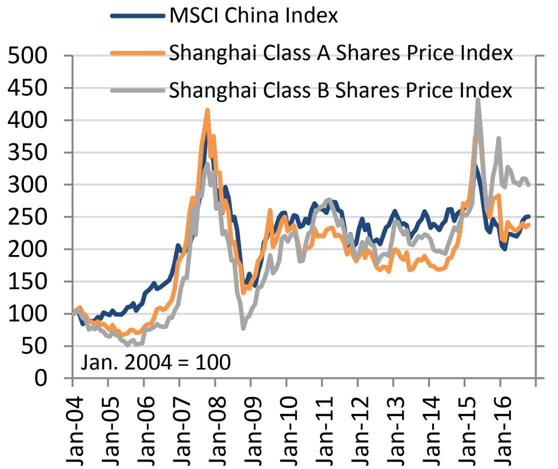


Source: IMF Fiscal Monitor, October 2016

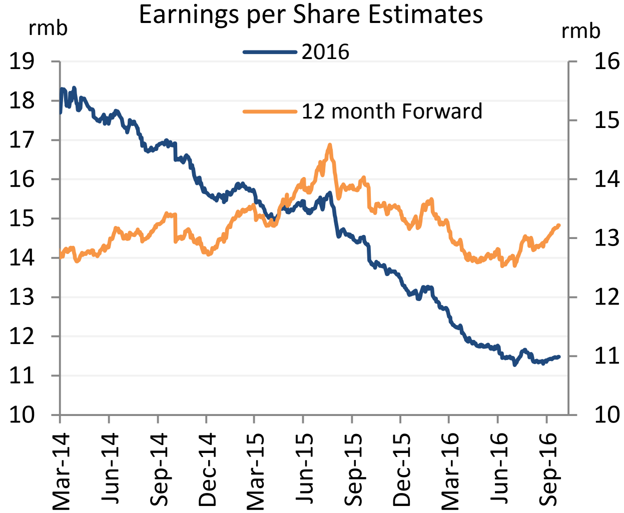


*in Local Currency

Chinese equities (A-shares) rose by 2.4% in Q3:16, in tandem with lower volatility and positive data surprises



*Shanghai B-shares are eligible for foreign investors - Shanghai A-shares are available for purchase by mainland investors



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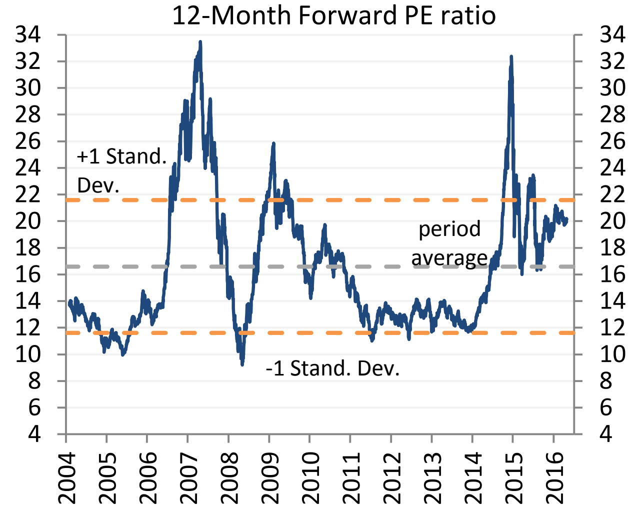

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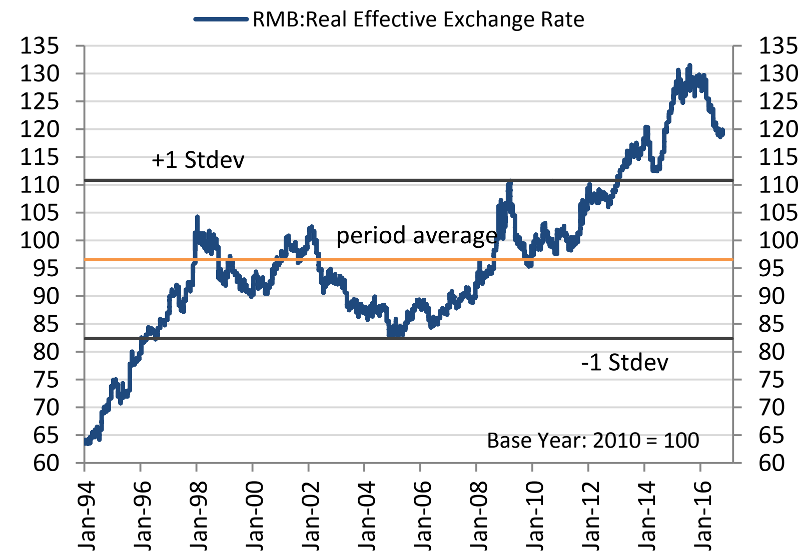
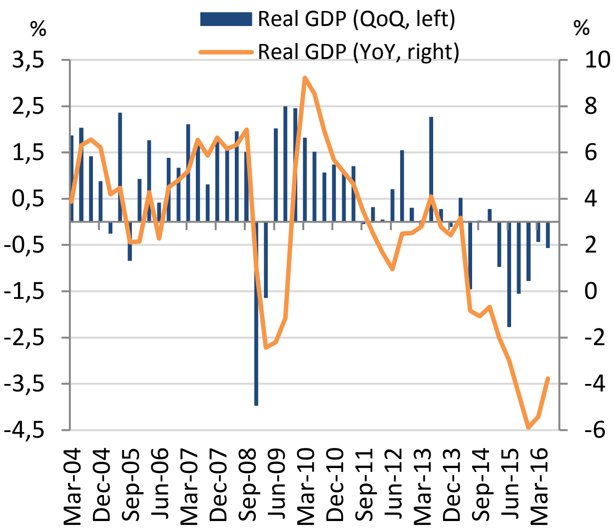
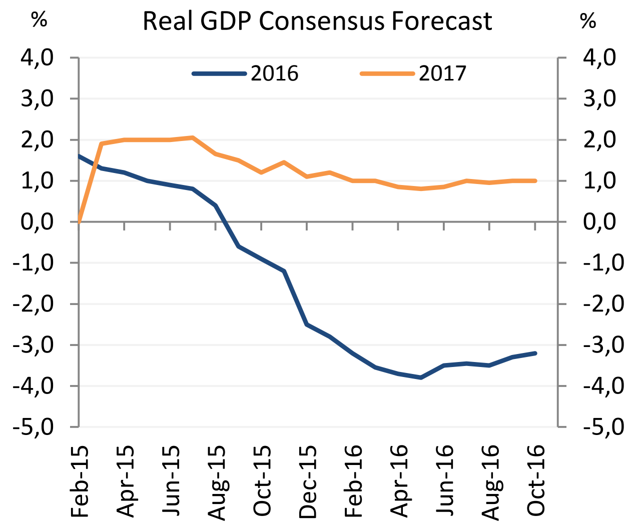
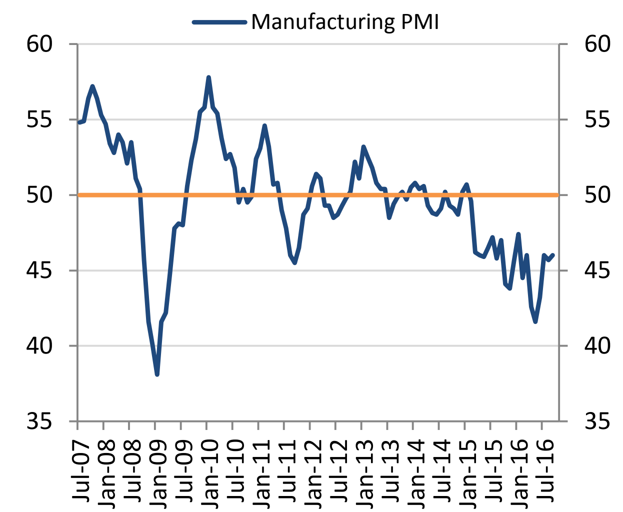
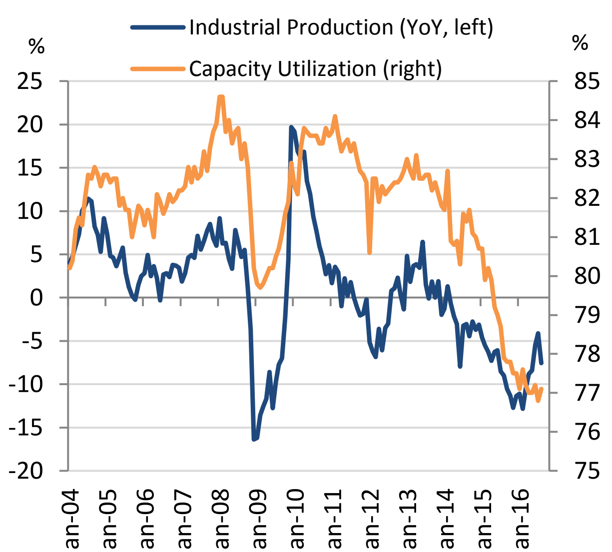


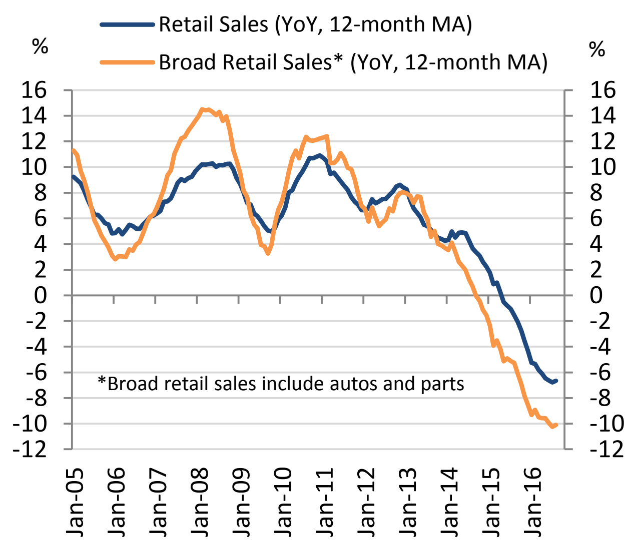
Brazil: Recession is set to continue in 2016 (-3.3% from -3.8% in 2015), according to the IMF. Growth is expected to resume in 2017 (+0.5%)

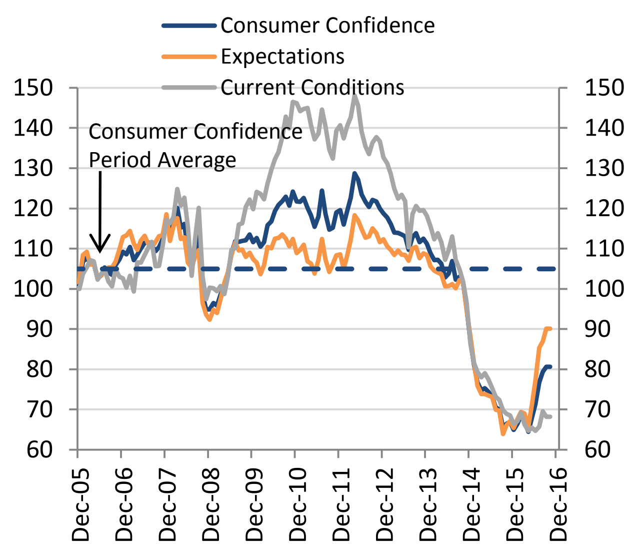




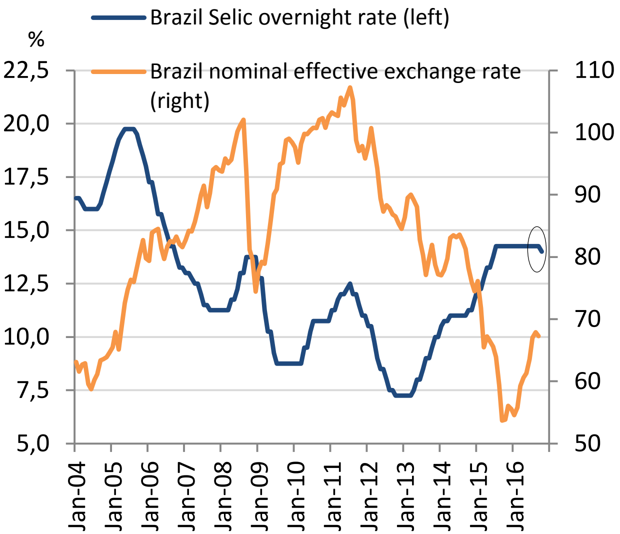


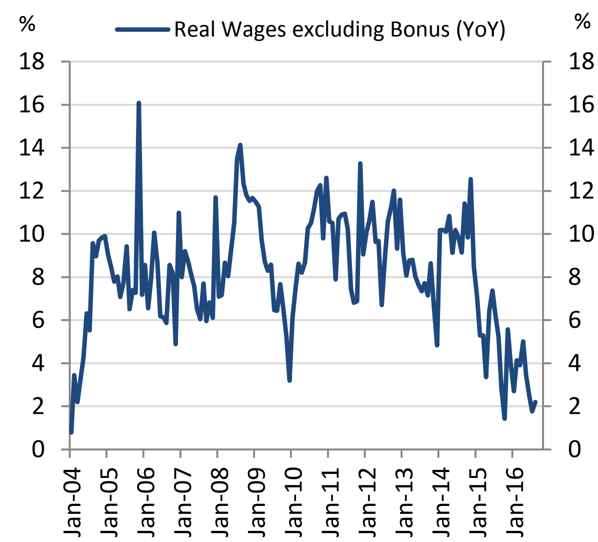


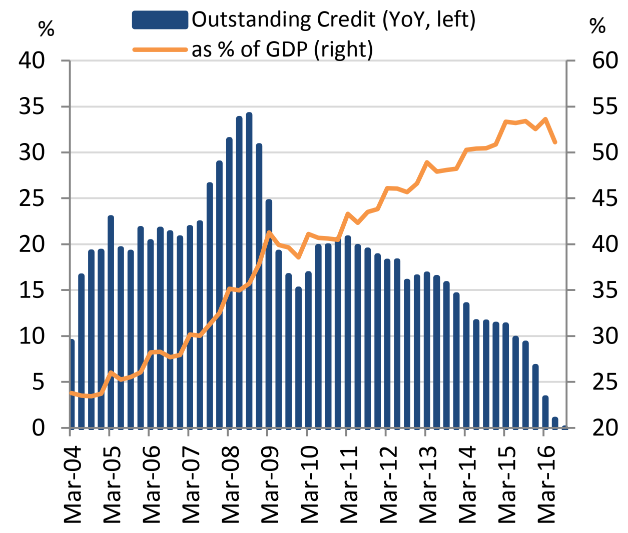


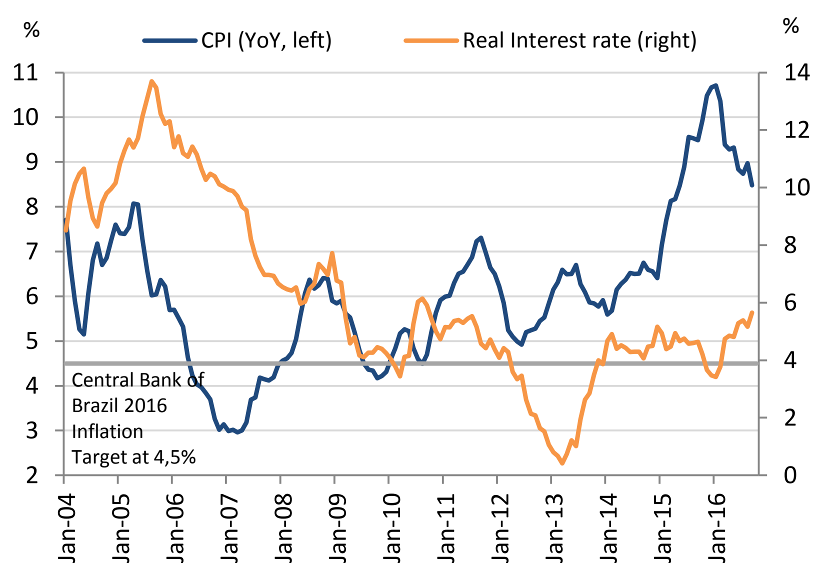


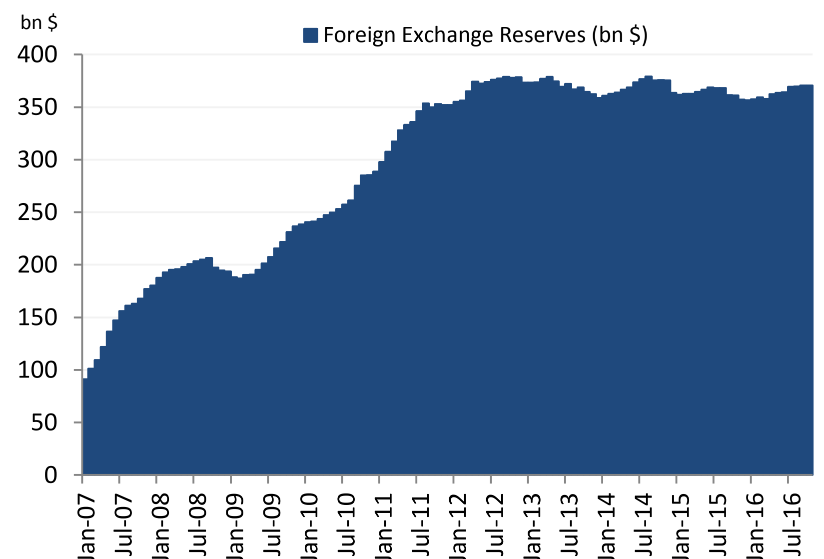
Inflation has slowed markedly, albeit remaining far above target, and is expected to continue this trend as prior currency depreciation effects dissipate



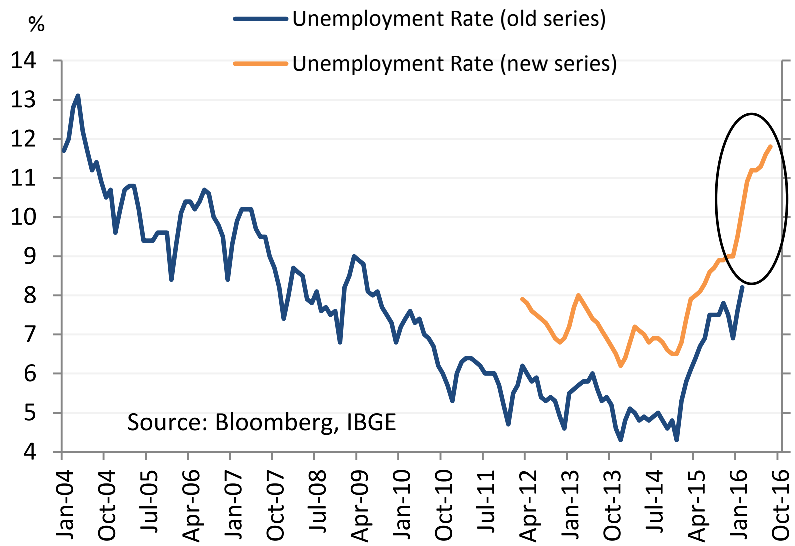


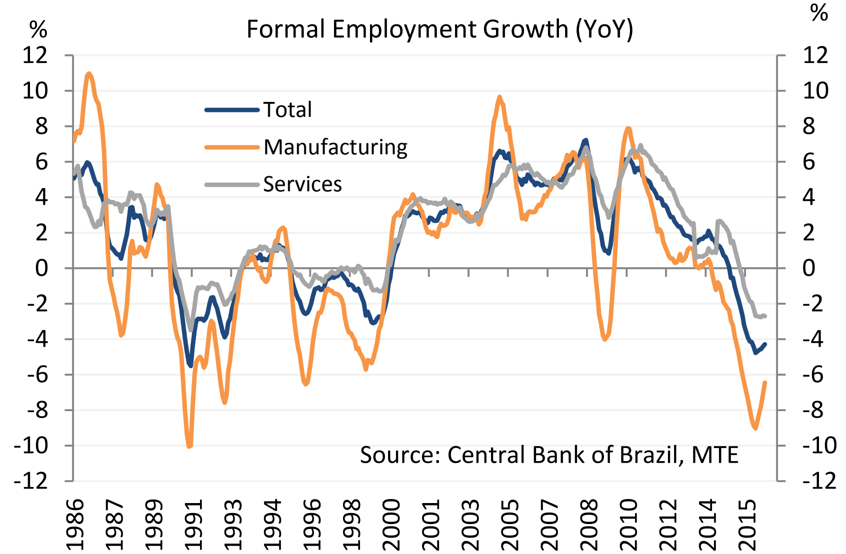


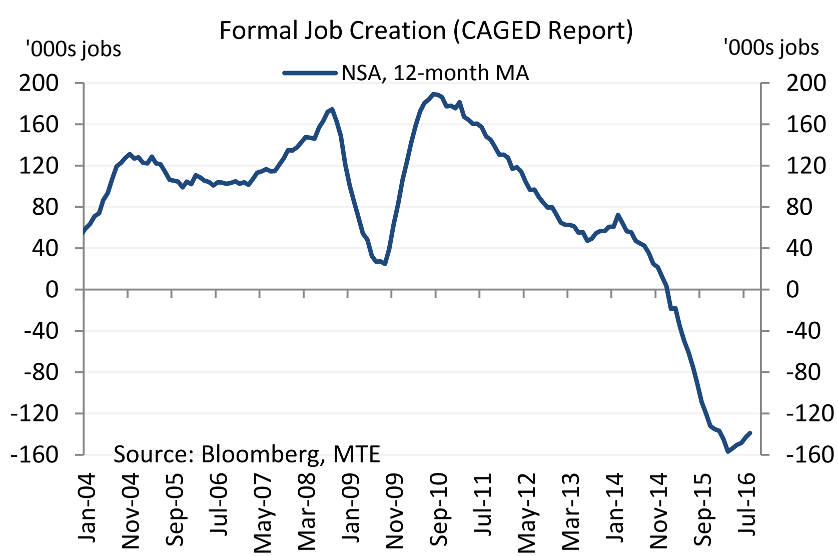


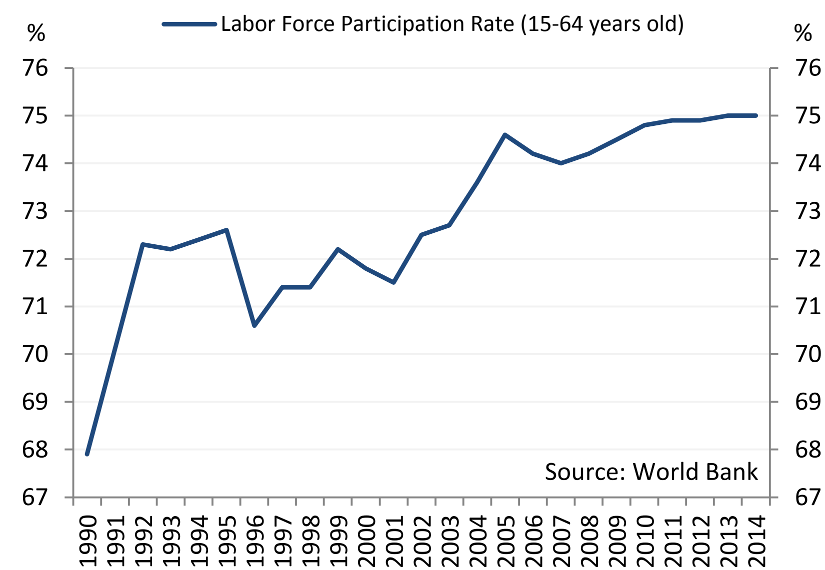


The unemployment rate remains elevated, but the deterioration in job creation appears to have eased

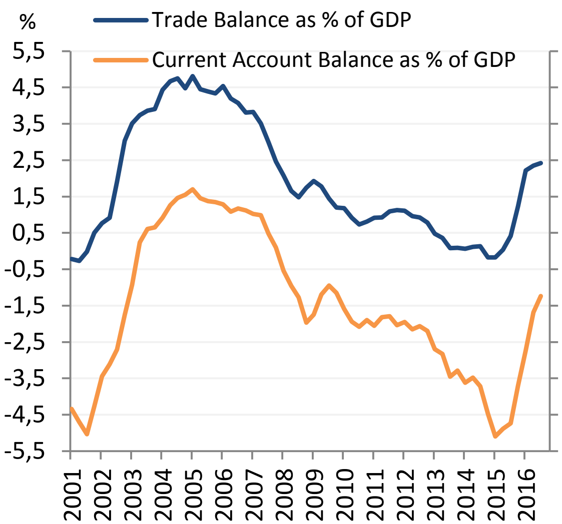


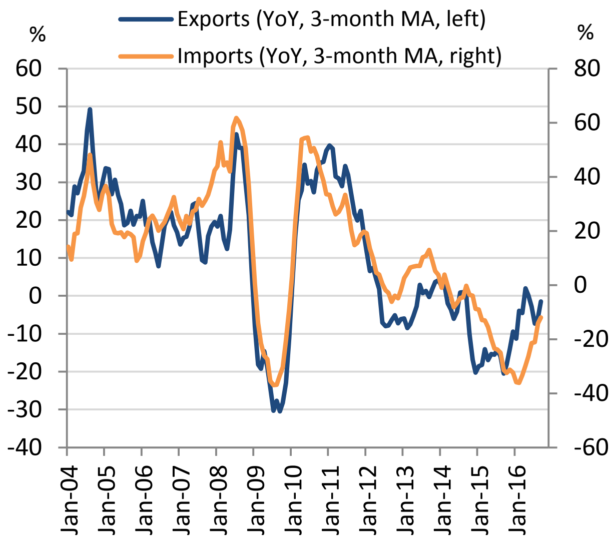


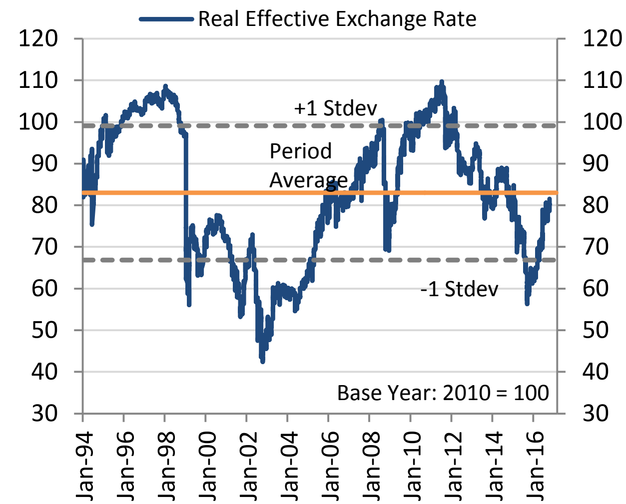


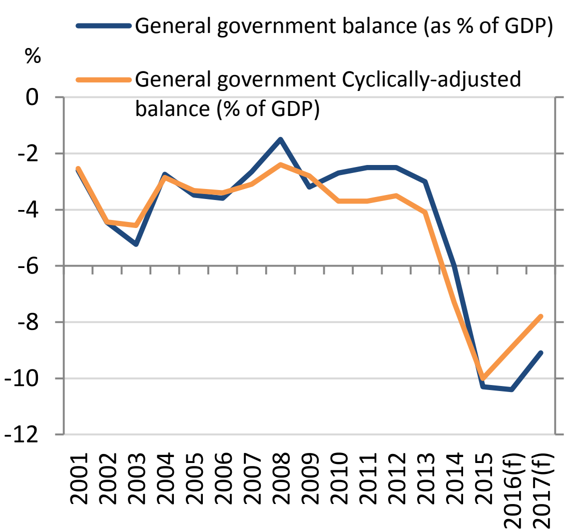


The GG deficit (% of GDP) is expected at -10.4% in 2016 and -9.1% in 2017, while the Government's fiscal overhaul (to cap annual public spending) is awaiting Senate approval

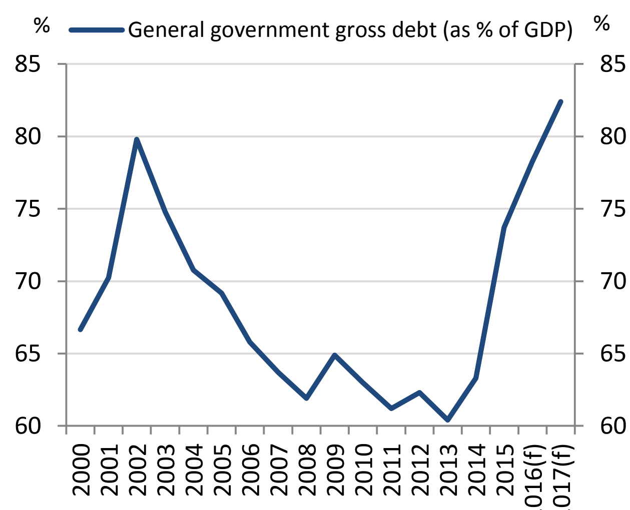




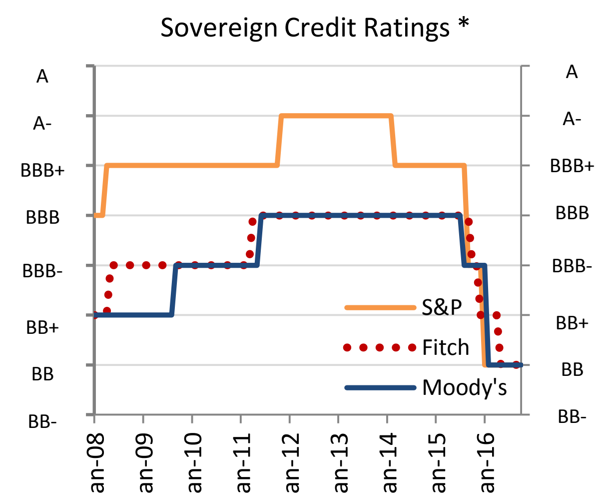




Source: IMF Fiscal Monitor, October 2016

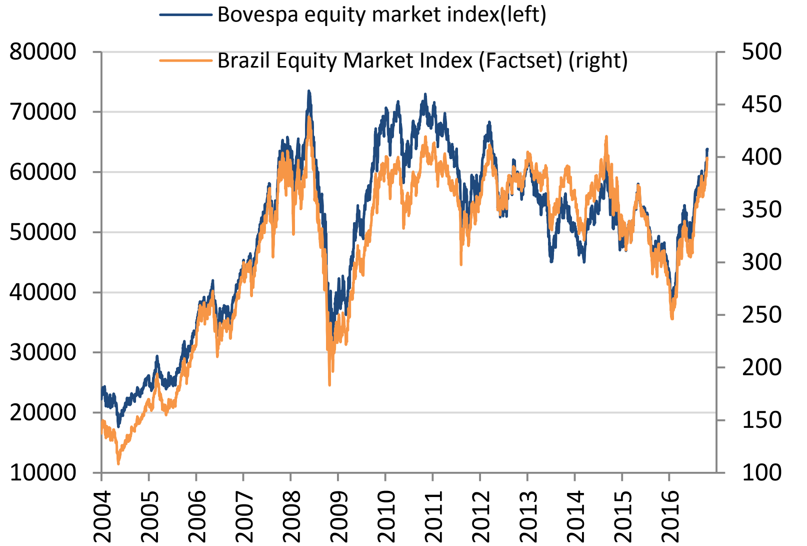


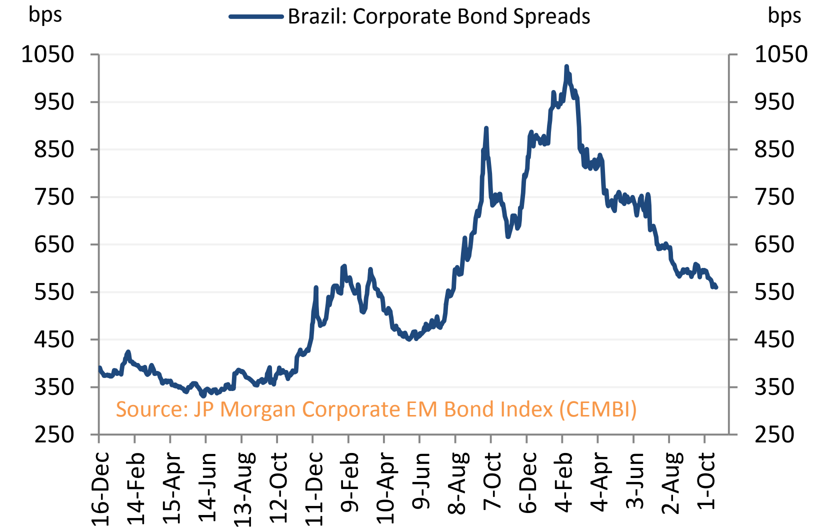
Source: IMF Fiscal Monitor, October 2016

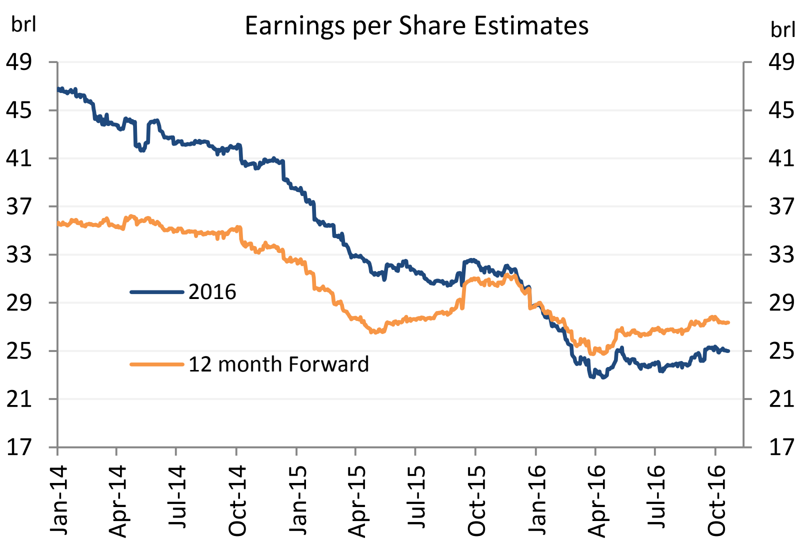


*in Local Currency

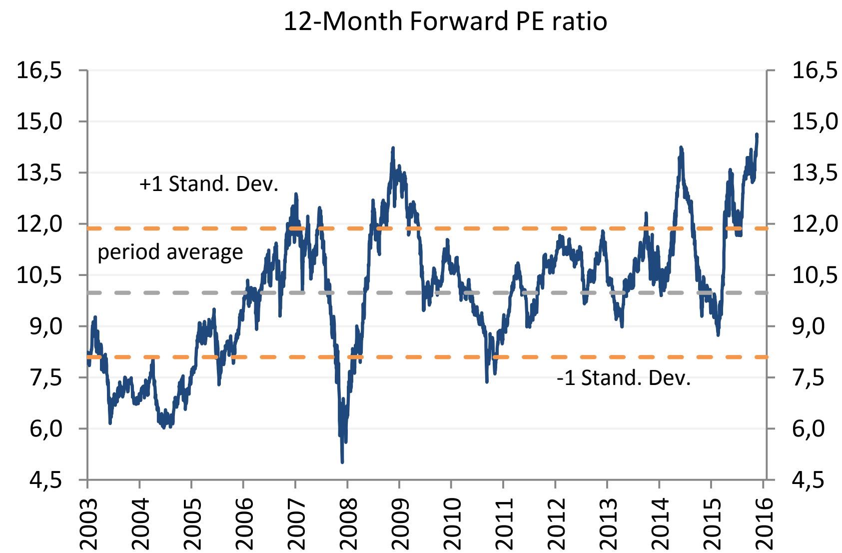
Brazilian equities have surged +47% ytd vs 11% for their EM peers, due to easing policy uncertainty and higher commodity prices. As a result, valuations appear overstretched (P/E: 14.5 current vs 9.9 l-t average)





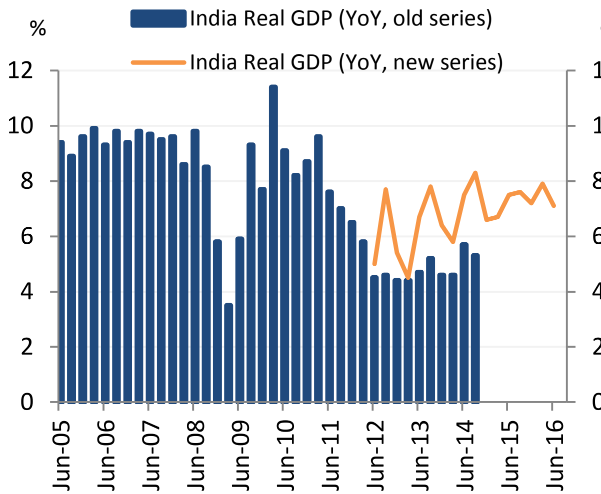


Source: Factset

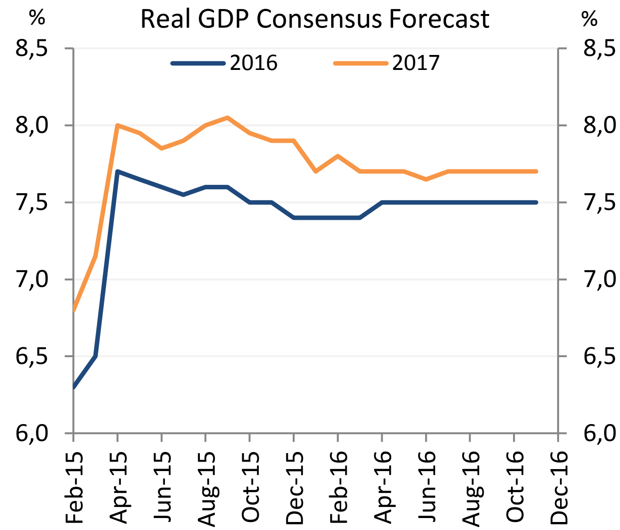


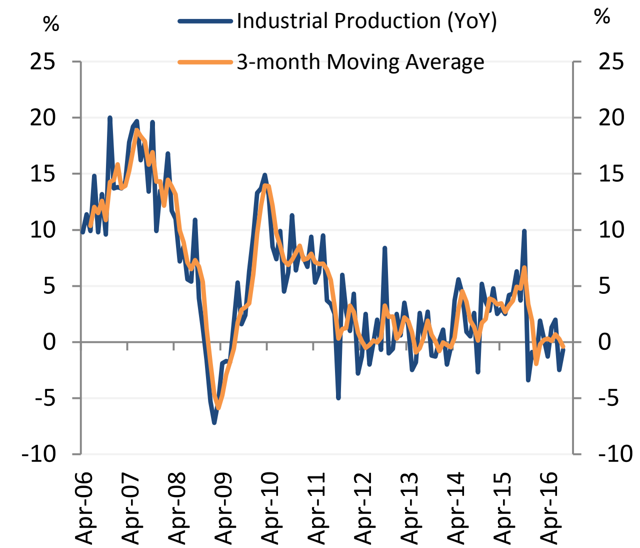
Source: Factset

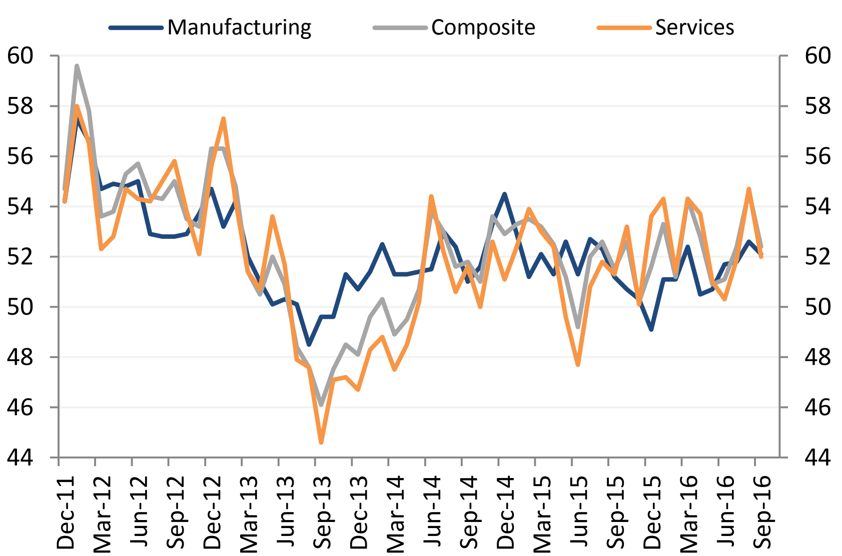
India: GDP growth remains solid (+7.1% yoy in Q2:16). The IMF expects India to show robust growth of 7.6% in 2016 (stable from 2015)

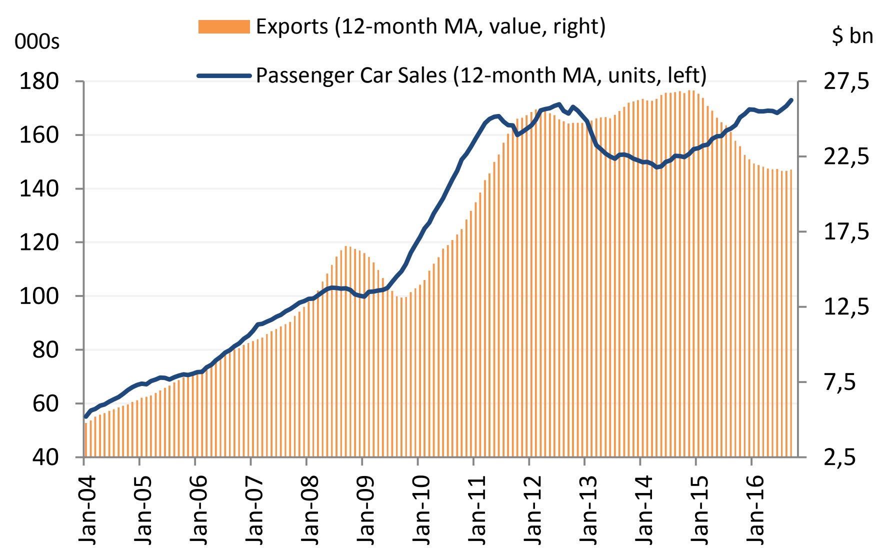


Source: India Central Statistical Organisation

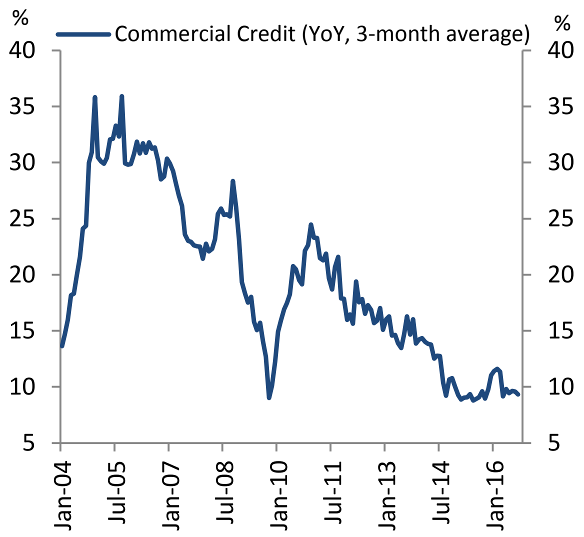


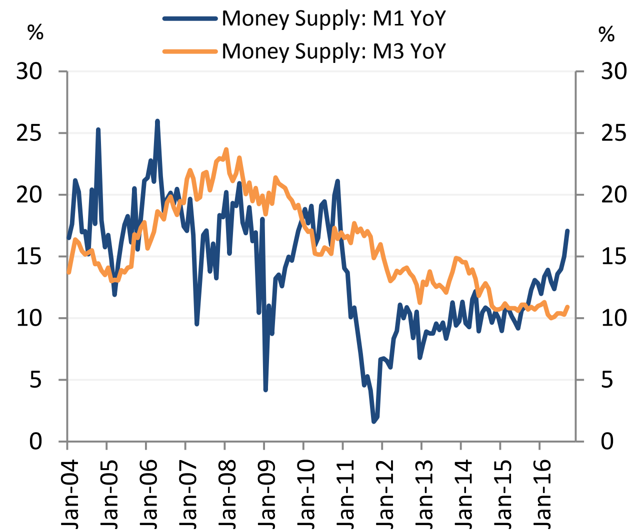


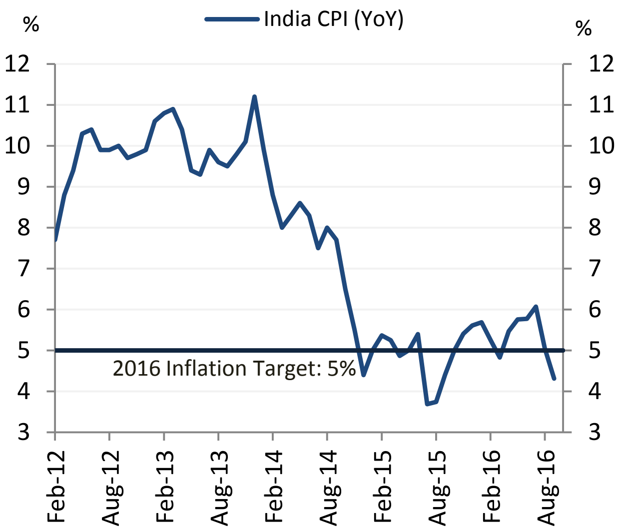


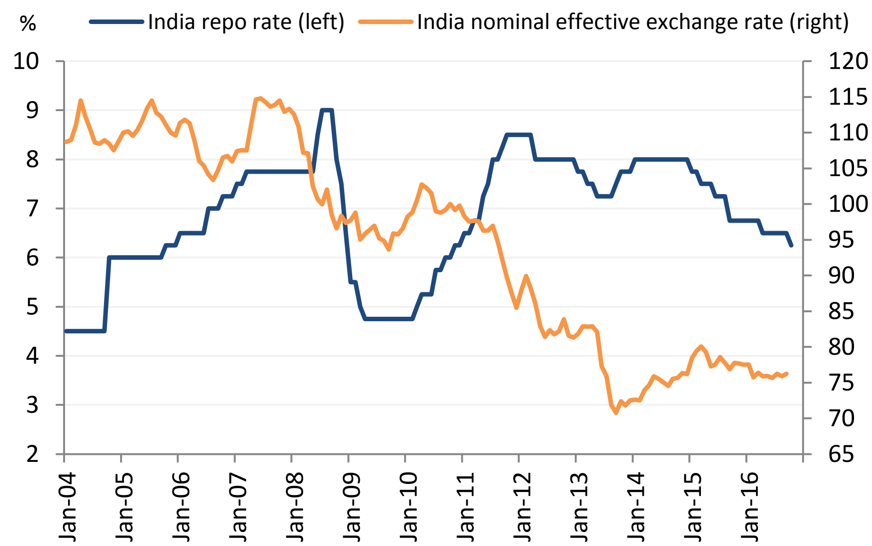


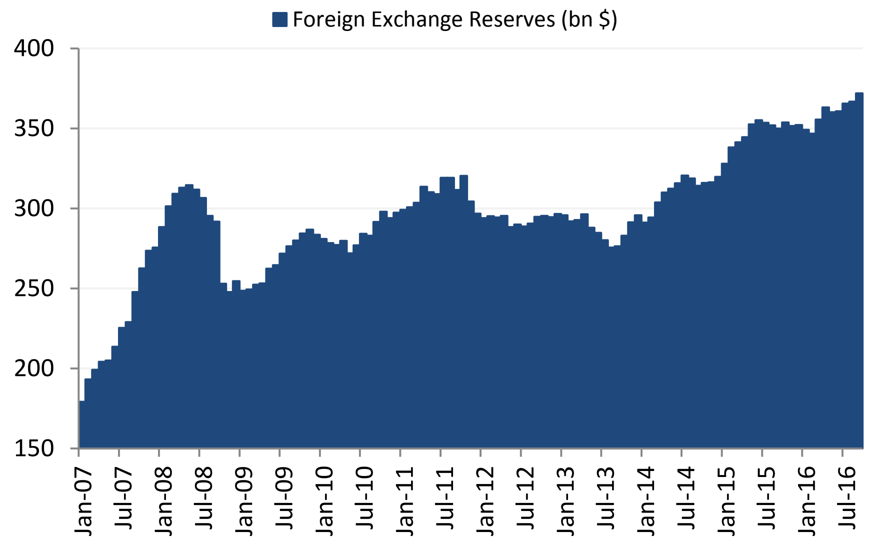
Inflation pressures have eased (CPI inflation at 4.3% in September) and, as a result, the central bank under the new Governor, unexpectedly reduced rates by 25 bps to 6.25%





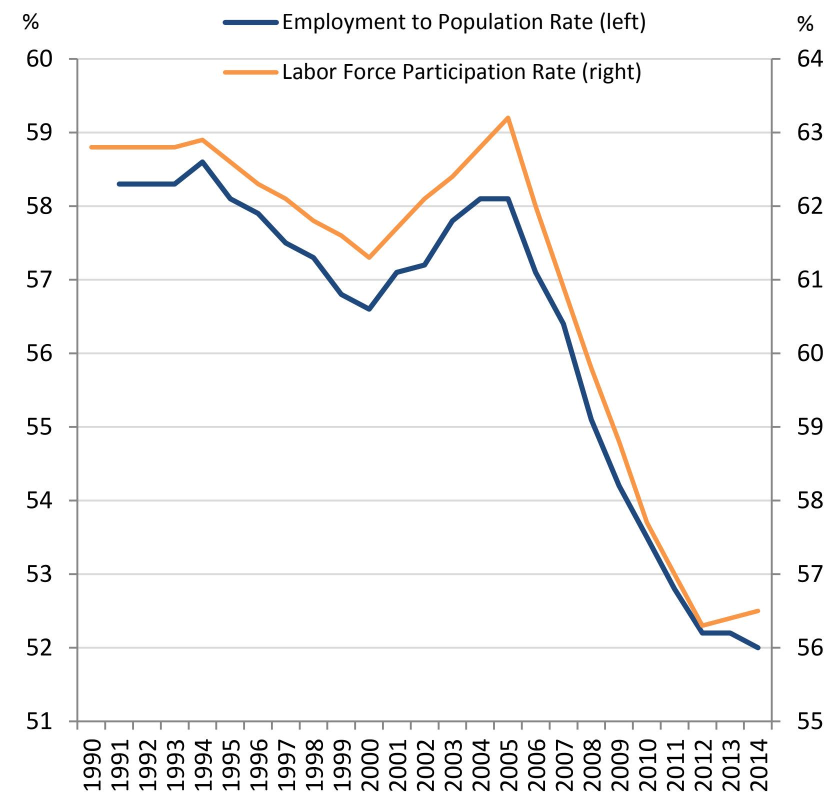






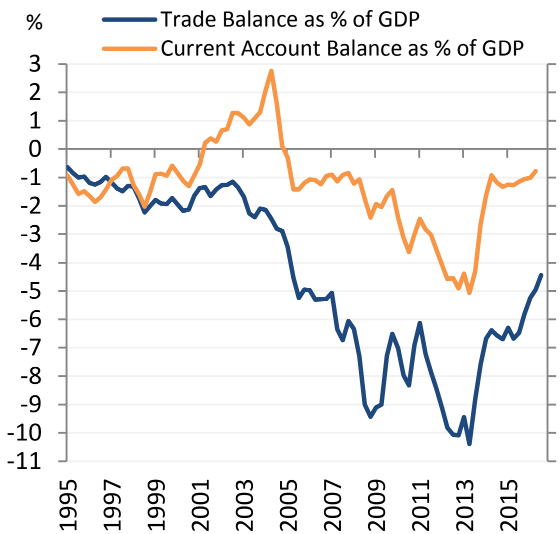
The unemployment rate is expected to decline further on the back of solid economic activity, as the labor force participation rate stabilizes

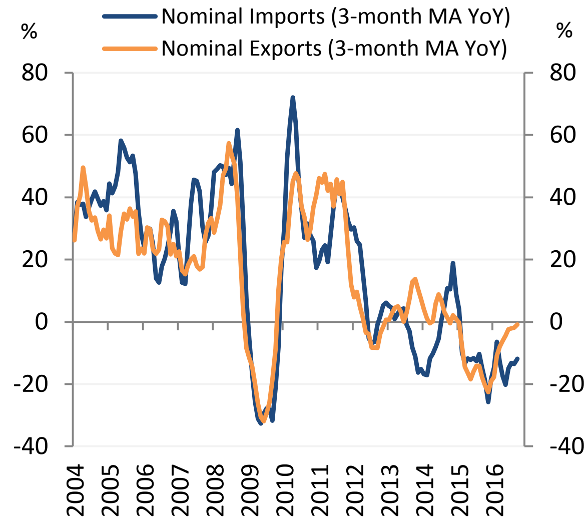
Source: Bloomberg (data as of 2015)

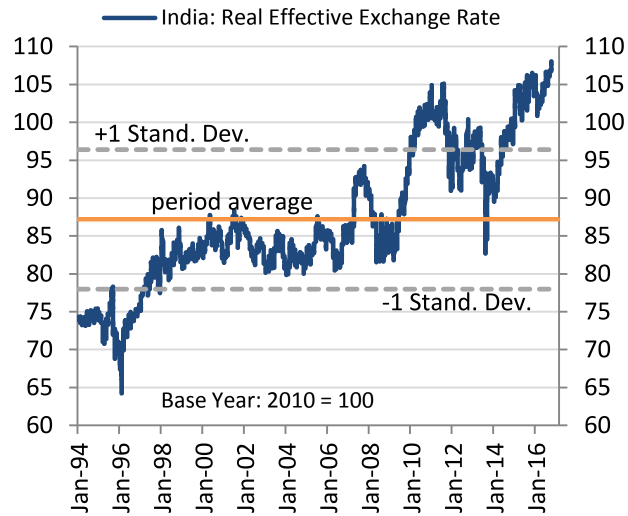


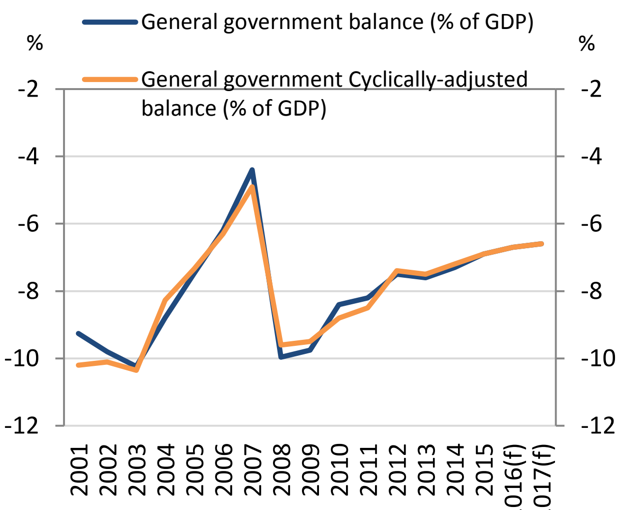
Source: World Bank (annual data, as of 2014)

The trade deficit continues to improve (-5.0% in Q2:16, from -5.2% in Q1:16 and -6.3% in 2015)

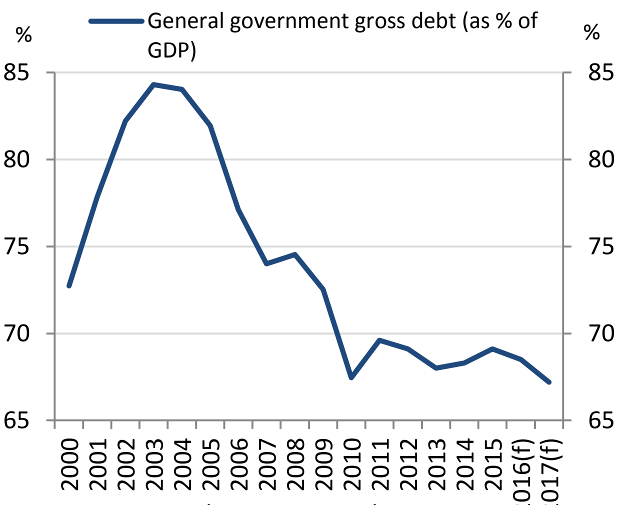




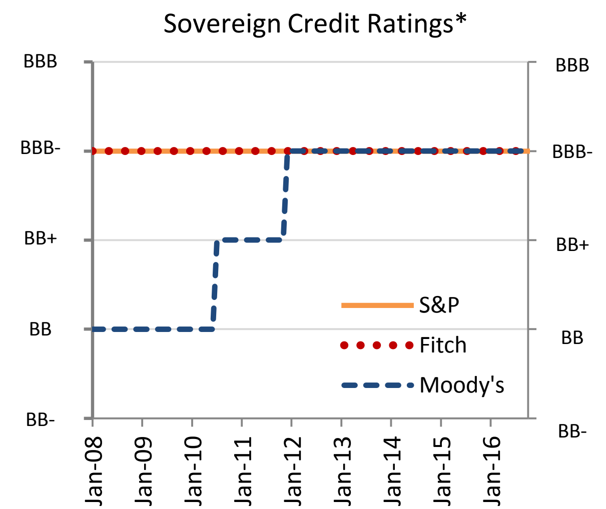




Source: IMF Fiscal Monitor, October 2016

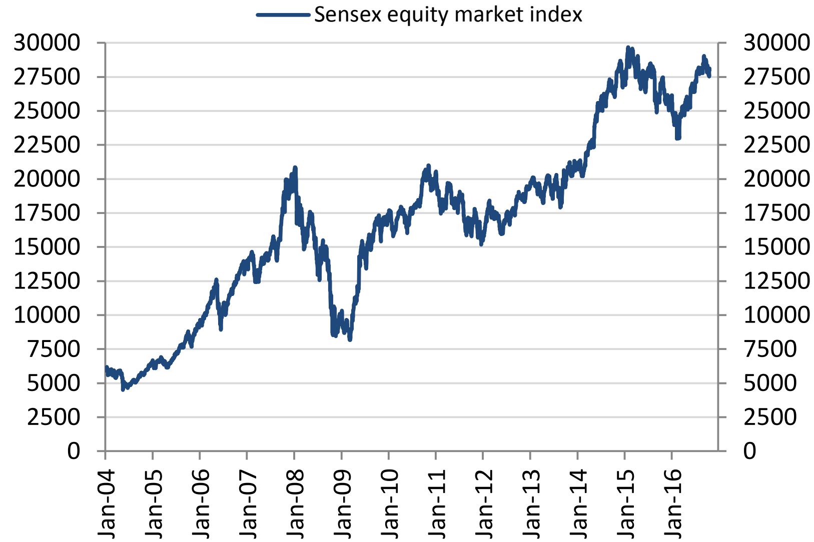


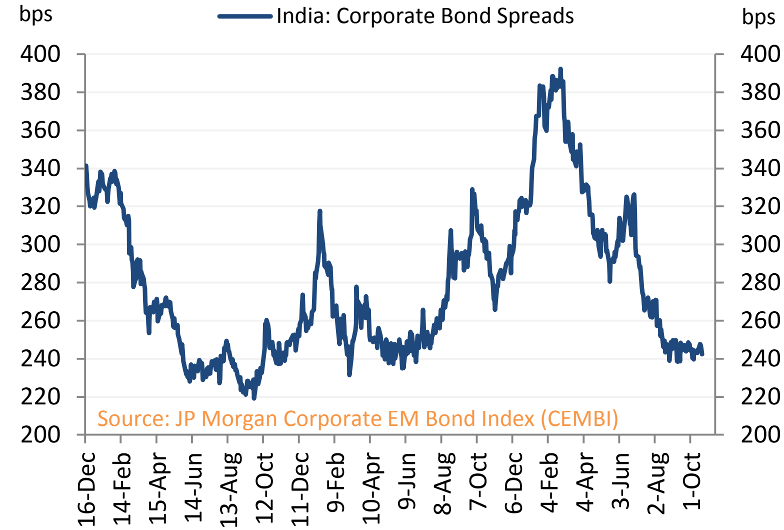
Source: IMF Fiscal Monitor, October 2016



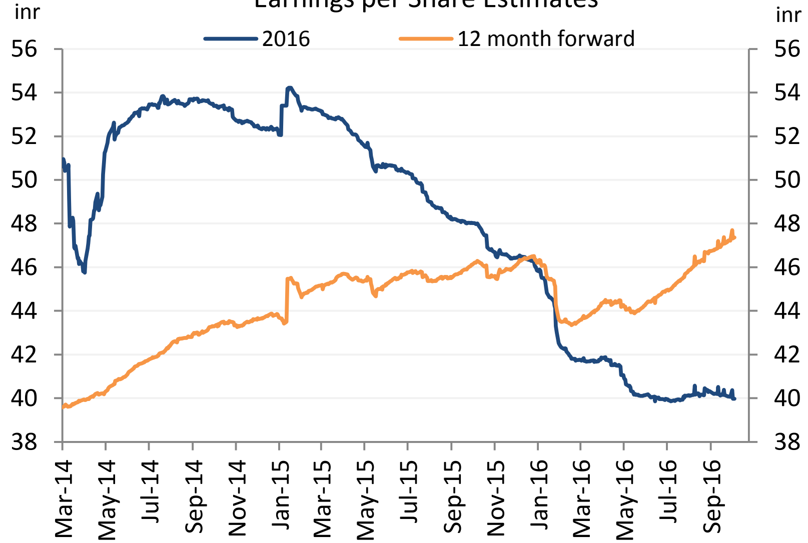
*in Local Currency

In Q3:16, equities (+3.2%) underperformed their EM peers (+6.9%), but P/E valuations continue to appear stretched



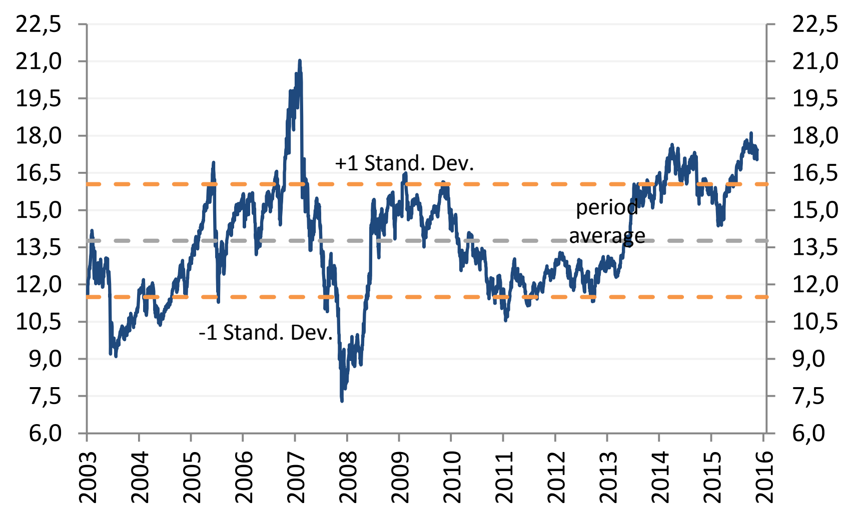


Earnings per Share Estimates



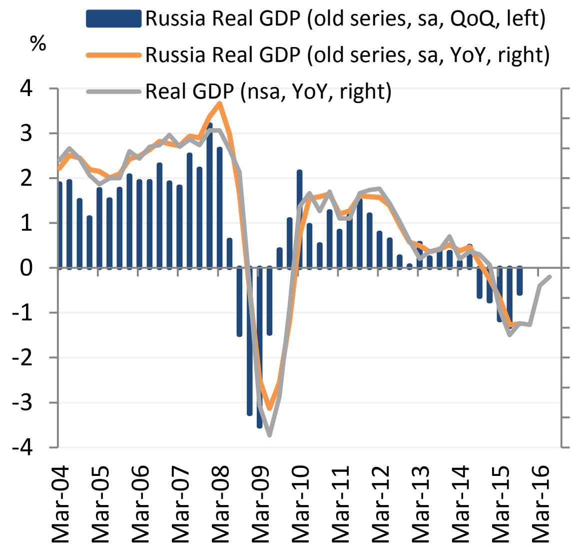
Source: Factset

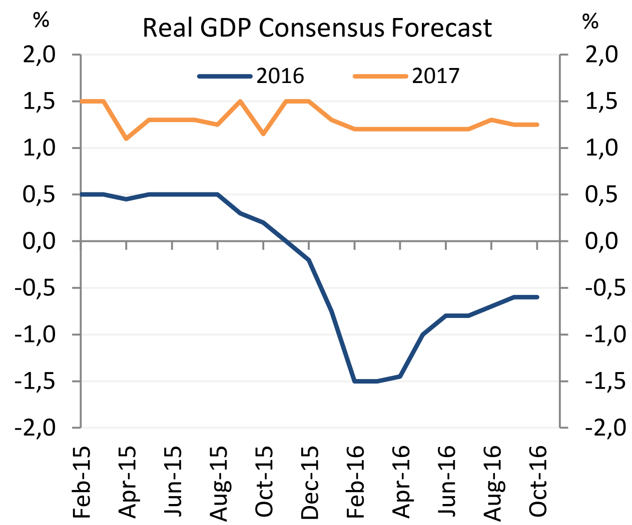
12-Month Forward PE ratio

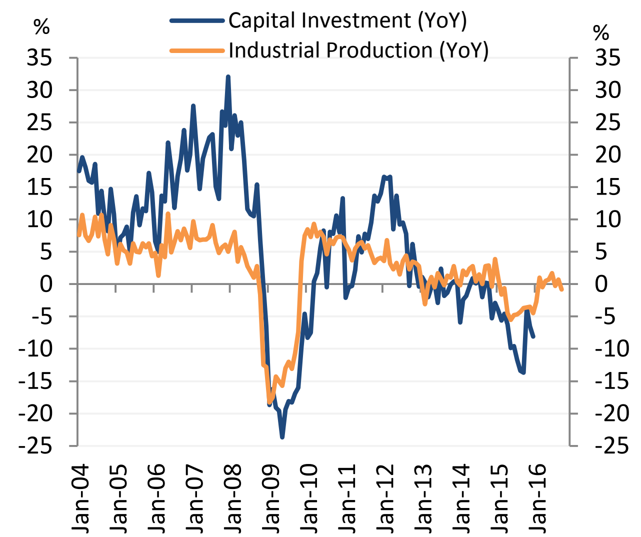


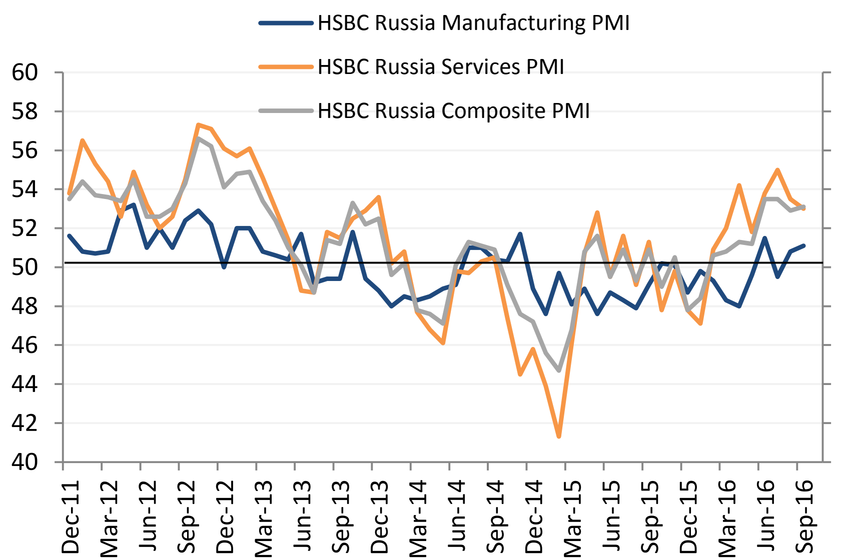
Source: Factset

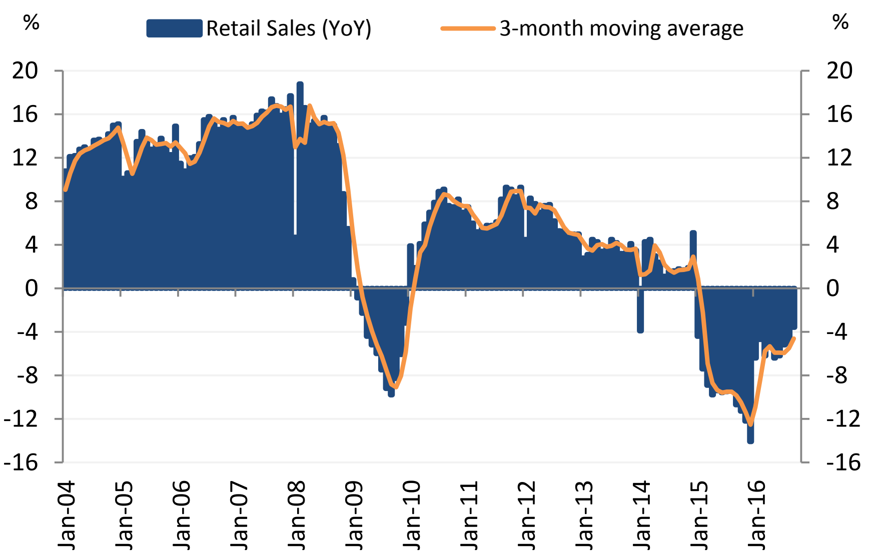
Russia: The recession bottomed out in H1:16 (-0.9% yoy vs -3.8% in H2:15), with a stronger outlook due, *inter alia*, to higher oil prices. The IMF expects Russia to exit recession in 2017 (+1.1%), from -0.8% in 2016



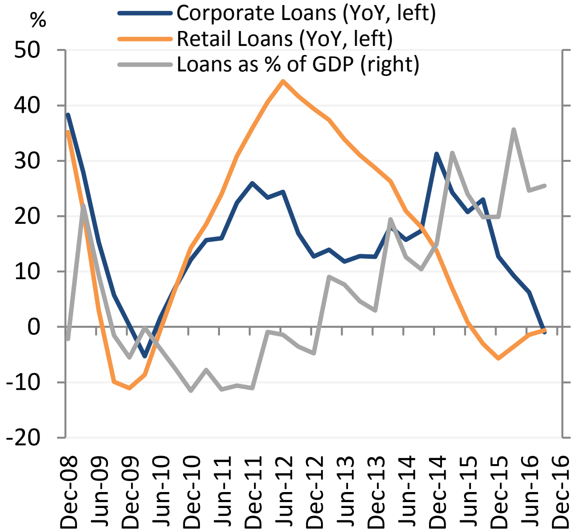


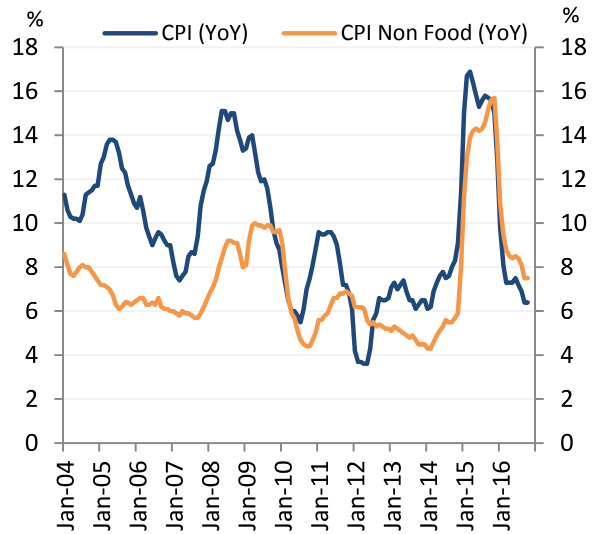


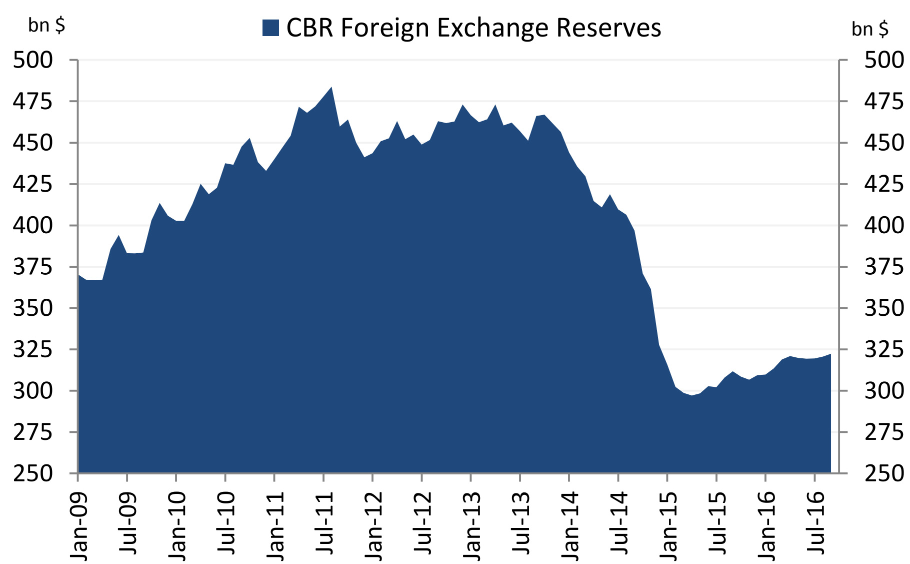


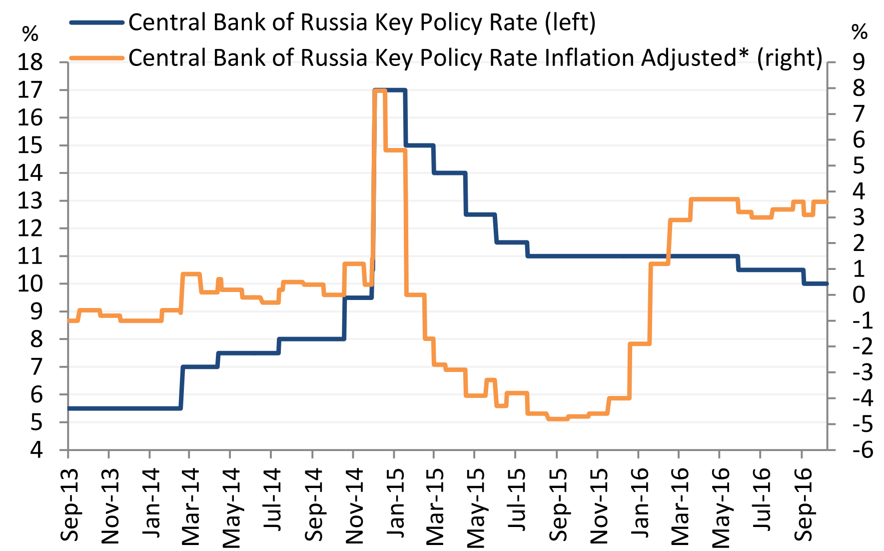


Inflation continues to decline (6.4% in September from 9.8% in January), allowing the central bank to cut rates (by 50 bps). However, the central bank has refrained from further policy easing until inflation drops below 4.0%



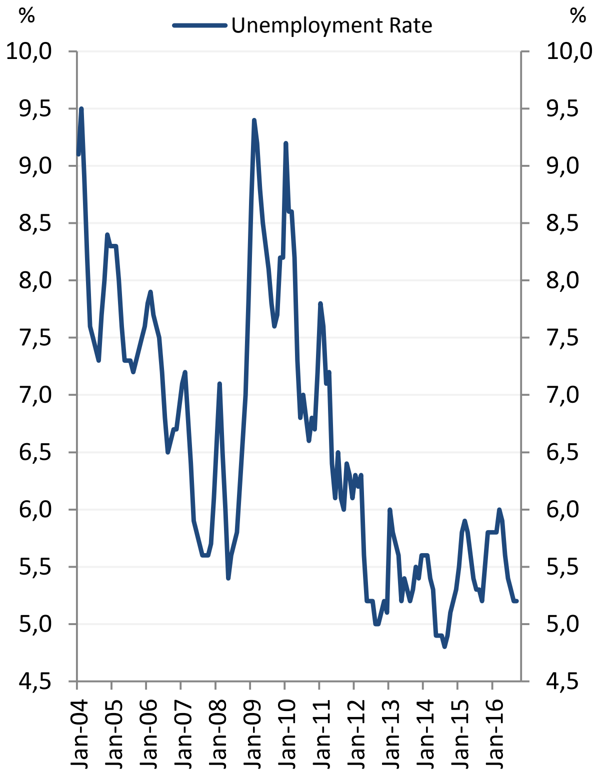




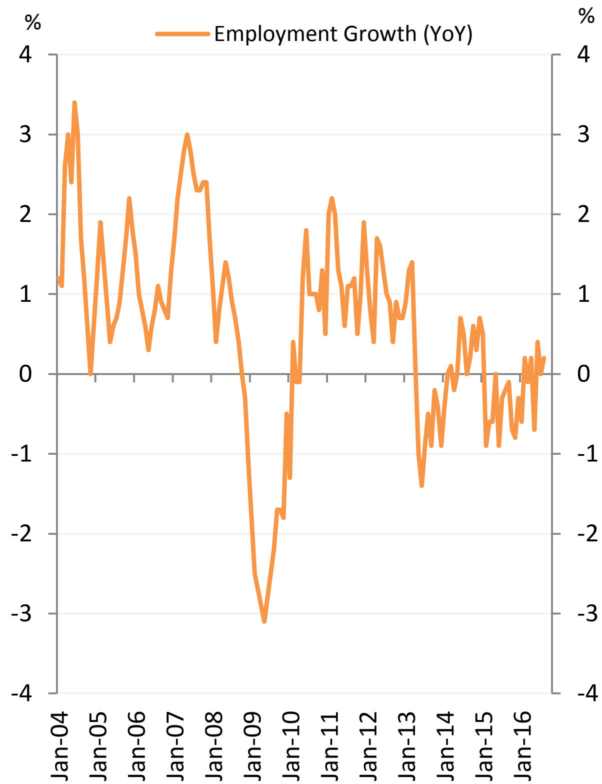


*: Using realized CPI Inflation

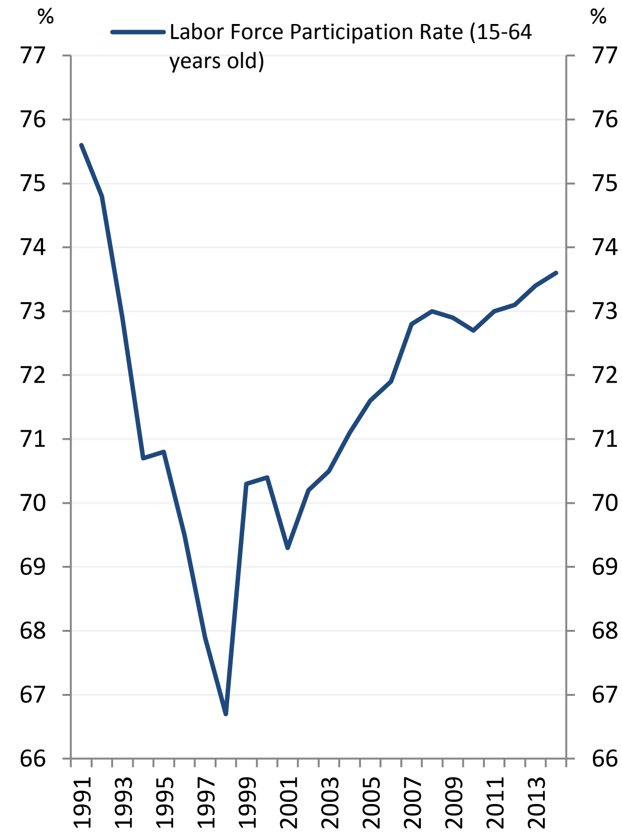
The unemployment rate declined to 5.2% in September, and employment growth has risen modestly



Source: Federal State Statistics Service, Bloomberg (monthly data as of September 2016)

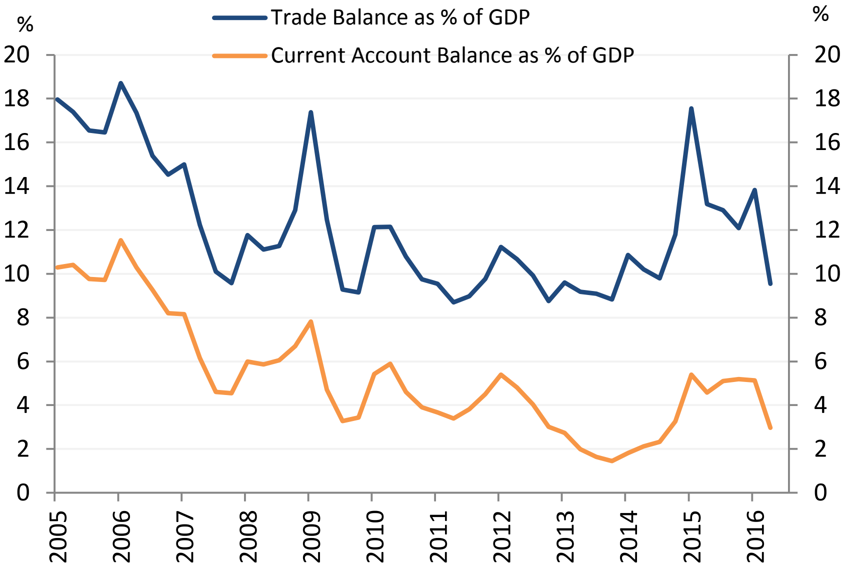


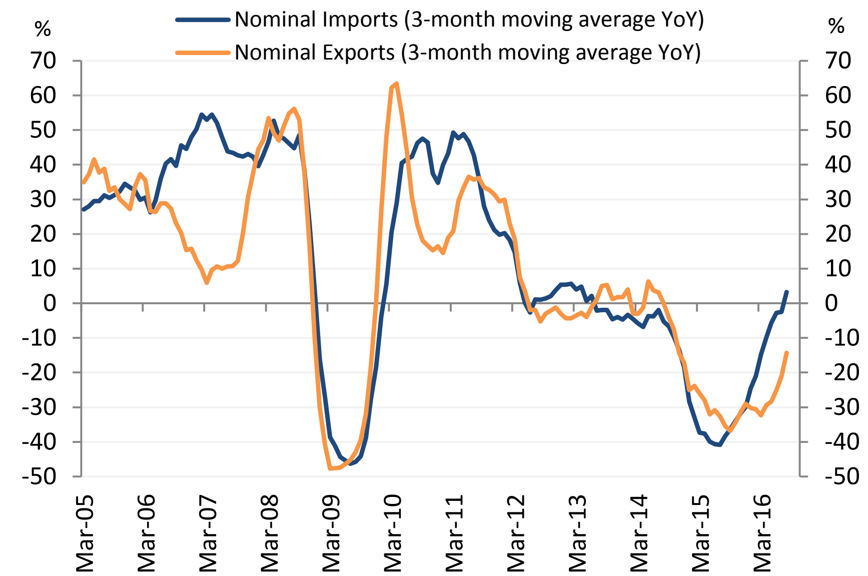
Source: Federal State Statistics Service, Bloomberg (monthly data as of August 2016)

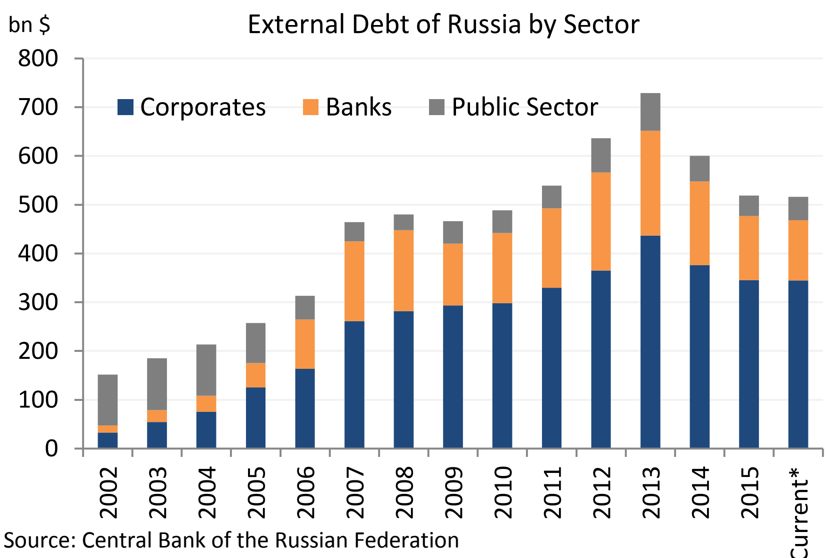


Source: World Bank (annual data, as of 2014)

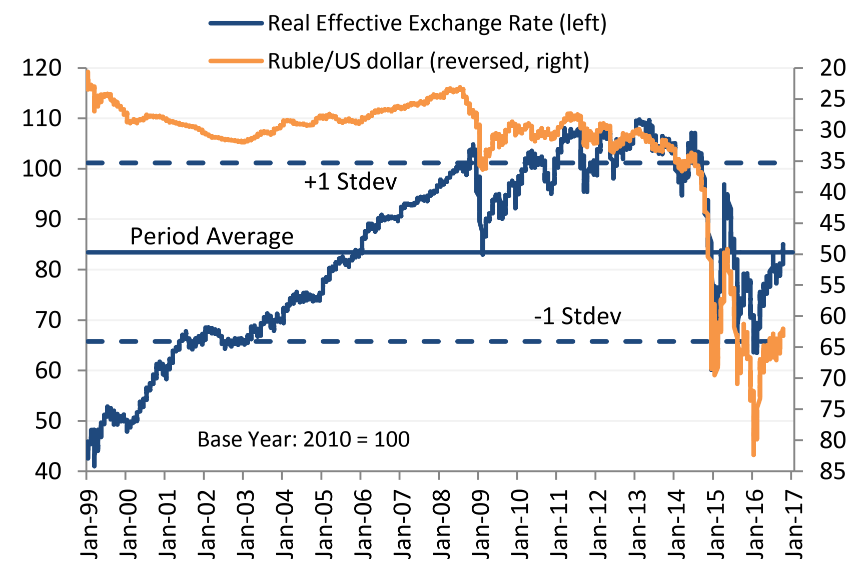
Rising imports underline improving domestic demand conditions, while the Ruble has appreciated by c. 13% year-to-date against the US dollar



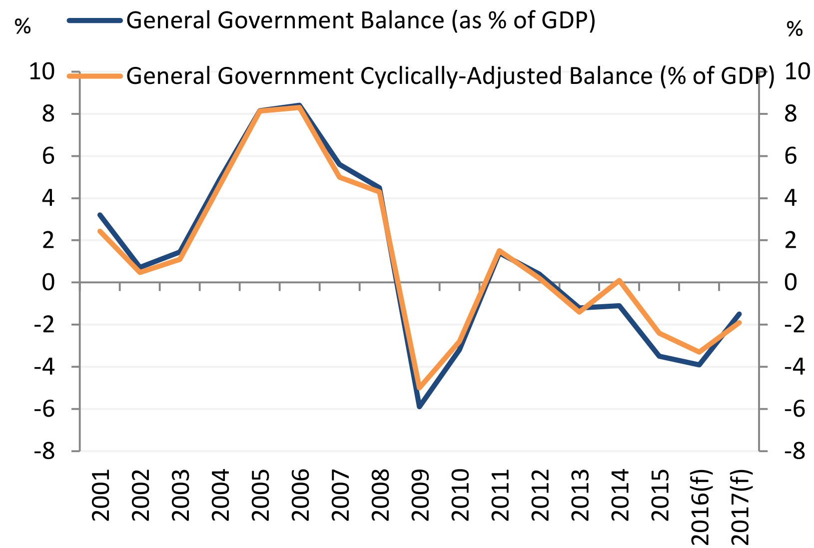




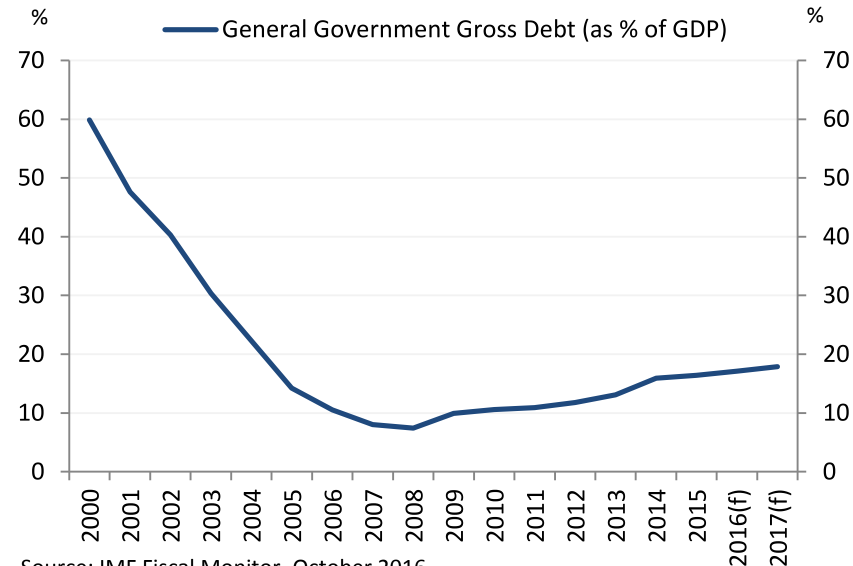
Source: Central Bank of the Russian Federation
*September 2016 (estimate)



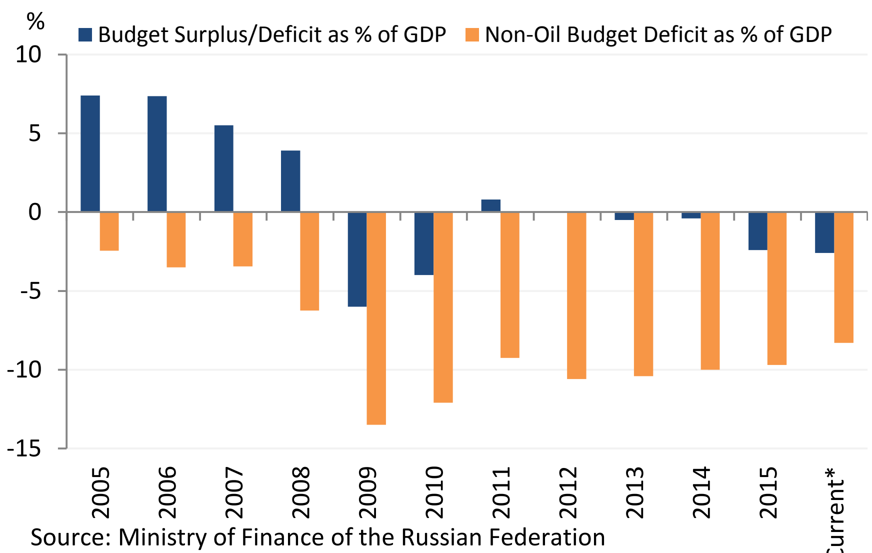
The IMF expects the general government deficit (% of GDP) at 3.9% in 2016, while the Government recently revised up its target from a range of 3.0%-3.2% to 3.5%-3.7%



Source: IMF Fiscal Monitor, October 2016

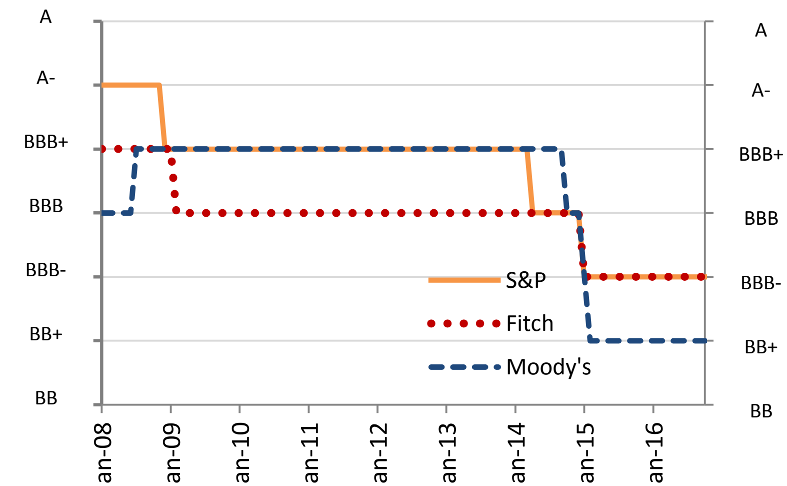


Source: IMF Fiscal Monitor, October 2016



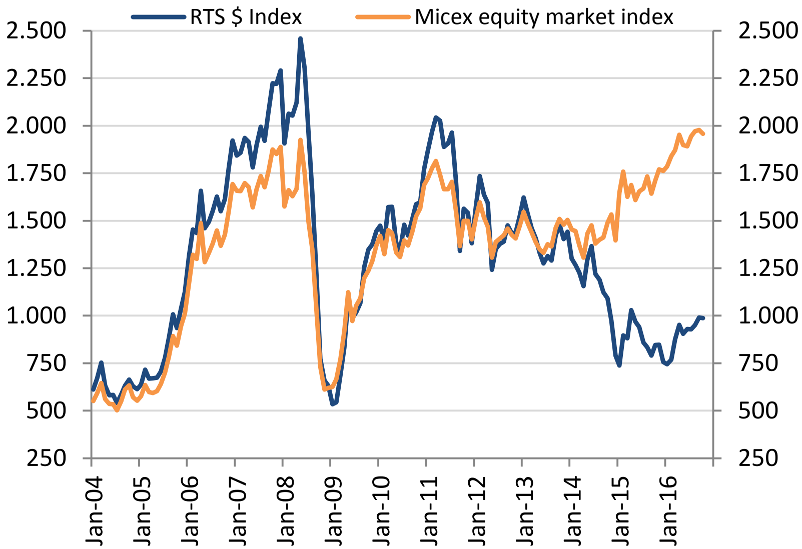
Source: Ministry of Finance of the Russian Federation
* September 2016 Y-T-D

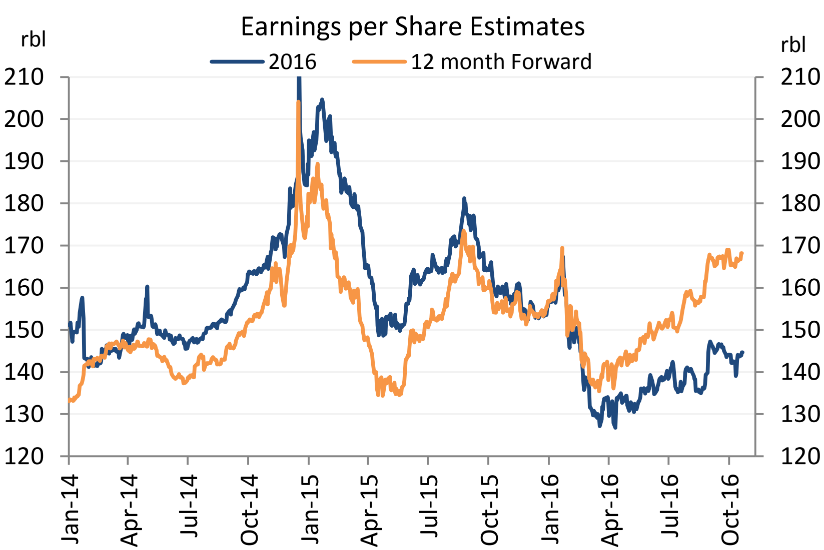
Sovereign Credit Ratings *



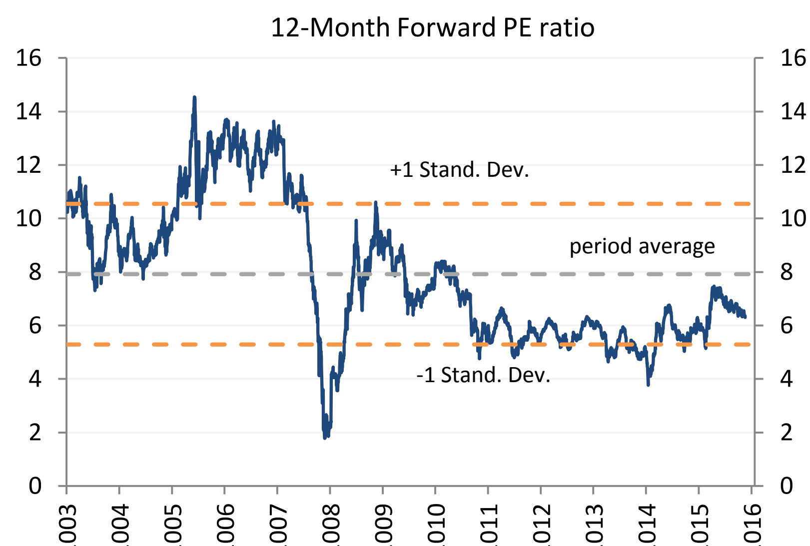
*in Local Currency

Russian equities increased in Q3:16 (4.6% and 11.1% ytd), in line with improving economic prospects





Source: Factset



Source: Factset

Disclosures & Analyst Certification

DISCLOSURES:

ANALYST CERTIFICATION:

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