LIVERPOOL INVESTMENT LETTER

August 2017

Cardiff Business School
Ysgol Busnes Caerdydd

Julian Hodge Institute of Applied Macroeconomics

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LIVERPOOL RESEARCH GROUP IN MACROECONOMICS

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The Julian Hodge Institute was launched in autumn 1999 in a new collabouration between the Cardiff Business School of Cardiff University and Hodge. The aim of the Institute is to carry out research into the behaviour of the UK economy, and to study in particular its relationship with the other economies of Europe. The research has been particularly germane in recent years and has proved to be of significant social and political relevance as Europe has navigated the difficulties of the global financial crash, the Eurozone crisis and most recently the UK referendum on EU membership. The Liverpool Investment Letter is written by Patrick Minford, with the assistance of other members of the Group; in particular the emerging markets section is written by Anupam Rastogi, and the focus on Japan is written by Francesco Perugini. The Investment Letter is published monthly.

The Liverpool Research Group in Economics is pursuing a research programme involving the estimation and use of macroeconomic models for forecasting and policy analysis. The Group is now mainly based in Cardiff Business School, Cardiff University, and is indebted to the School and to the Hodge Foundation for their support. The Group's activities contribute to the programmes being pursued by the Julian Hodge Institute of Applied Macroeconomics. This Liverpool Investment Letter is typeset by David Meenagh and published on behalf of the group by Liverpool Macroeconomic Research Limited, which holds the copyright

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COMPLAINTS OF 'REBALANCERS'

Table 1: Summary of Forecast

	2014	2015	2016	2017	2018	2019	2020
GDP Growth[1]	2.9	2.2	2.3	2.1	2.6	2.9	3.5
Inflation CPI	1.7	0.2	1.2	2.6	2.6	3.0	3.0
Wage Growth	1.2	2.4	2.9	2.6	3.6	4.7	4.5
Unemployment (Mill.)[2]	1.1	0.8	0.7	0.8	0.8	0.7	0.7
Exchange Rate[3]	87.1	91.6	80.4	76.4	75.1	74.6	74.4
3 Month Interest Rate	0.6	0.6	0.4	0.9	1.5	2.5	3.0
5 Year Interest Rate	1.8	1.3	0.9	1.1	2.0	2.9	3.0
Current Balance (£bn)	–99.9	–103.7	–89.0	–63.7	–44.9	–14.4	0.5
PSBR (£bn)	83.3	71.2	69.0	53.4	44.8	37.2	12.8

[1]Expenditure estimate at factor cost
[2]U.K. Wholly unemployed excluding school leavers (new basis)
[3]Sterling effective exchange rate, Bank of England Index (2005 = 100)

For years now the cognoscenti of UK economics have complained about the current account deficit and demanded rebalancing; I include in their ranks Nick Clegg, Sir Vince Cable and the CBI, to name a few.

But when it happens as a result of Brexit and the resulting 15% devaluation, they complain again! Now because it was horrible Brexit that caused it, it must all be bad. They bang on about the effect on consumption without referring to the effect on exports, orders, investment and profits.

It so happens we have just had for July the most bullish CBI Survey of UK manufacturing that I can remember. For example the volume of output is the highest since January 1999, and total order books are the highest since October 1988. The CBI modestly entitles this July survey

OUTPUT GROWTH ACCELERATES TO TWO-DECADE HIGH

And yet, and yet. Have we seen any headlines about it on the BBC, or in the Guardian or the FT, or has the CBI itself drawn attention to it? Have we heard from Carolyn Fairbairn that the manufacturing economy is set fair? No, I don't think so.

Instead these people are mourning the weak first quarter GDP figures and the slowish second quarter ones just out; 0.3% after the 0.2% for the first quarter, revised down from the preliminary 0.3% estimate.

Yet this slowness is of course due to the effect on consumption of the 'pass through' of the devaluation into the CPI and its effect on real wages and private consumption. This is all straight out of the basic playbook of devaluation. Devaluation works to rebalance the economy towards a reduced current account deficit, more net exports, stronger manufacturing profits and more investment, precisely by reducing personal real incomes and consumption and pushing money instead towards producers of traded goods and services.

It is also a well-known feature of this process that there are varying lags in its operation. It tends to work faster on consumer prices and incomes than it does on producers' net exports and investment. It may even worsen the current balance in the short run because the prices of imports go up rapidly with devaluation whereas export prices may remain set in sterling terms to pass the benefit of devaluation on to foreign buyers, to increase sales volume.

Another well-known feature of these events is that different parts of GDP get surveyed with differential precision in the short run. This is why GDP figures keep on being revised years after the event, as new data is gathered that better samples what was happening. Retail sales and consumer spending is probably most reliably sampled in the short term, apart from in bad recessions when sales go into new outlets promising better value to the harassed consumer. But output and export figures of companies get sampled poorly especially when there are changes in composition or new markets involved.

So deep is the hatred of Brexit among our cognoscenti that they will stoop to any piece of data to suit their book and deliberately ignore the underlying picture.

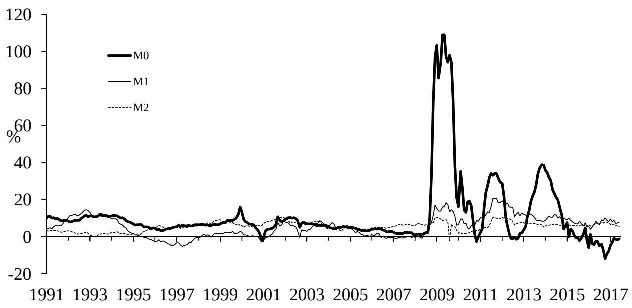
Yet the data will out and this CBI survey is a harbinger of what is to come. Already the Purchasing Managers' Surveys — of manufacturing, services and construction — are all confirming that steady growth is continuing; they are all around the 54 mark for June/July, where 50 and above means growth.

Then the latest ONS trade figures for May, excluding oil and erratics, show export goods volume growth since June last year of 10.5%. This compares with a healthy consumption-fed growth of 6.5% for import goods volume growth. This is a 4% swing on the goods volume balance since the referendum and exactly what one would be looking for after the Brexit devaluation.

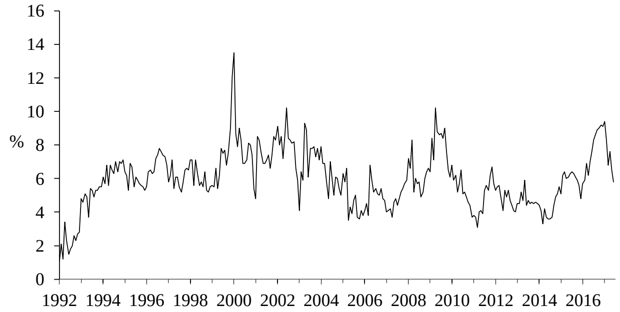
Now we have the CBI Survey for July where manufacturing is shown as going gangbusters, with strong investment intentions, export orders and so on.

When one considers the implications of all this for the UK growth forecast over 2017 and 2018, it is promising growth in the range of 2–3%. One must remember that GDP figures are indeed constantly revised and one simply must not get fixated on the latest quarterly estimates; remember too that even that 'weak' first half of this year has shown nearly 2% growth on the same half of 2016. We are now embarked on a largescale regime change with Brexit. First, we are seeing the effects of the highly stimulative Brexit devaluation helping to reshape the economy towards trade and away from consumption. Second, we will be seeing the effects via anticipations of the redirecting of our trade towards the wider world with our EU trade consolidating rather than growing. Third, we will start to see in the longer term the effects of lower prices of traded goods from that wider world showing up in the CPI and starting to create more competition in the farming and manufacturing sectors; these sectors will also need to rely less on cheap taxpayer-subsidised unskilled labour. Out of all this we should see faster productivity growth and better real wage growth as 2019 comes into view.

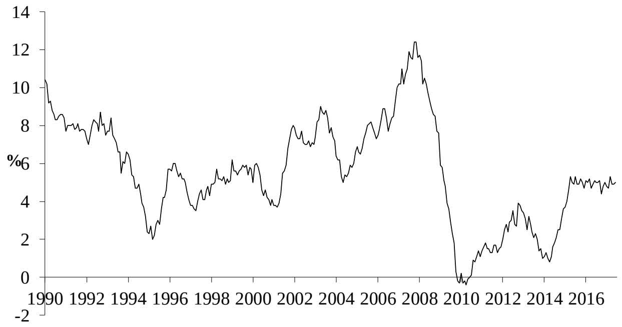
U.S.: Growth in Monetary Aggregates (Yr - on - Yr)



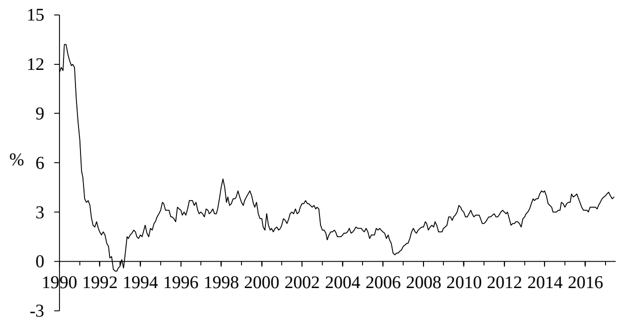
UK: Notes and Coins in Circulation Growth



Eurozone M3 Growth



Japan: Growth of M2+CD's



FOCUS ON JAPAN

Francesco Perugini

Japan's Labour Shortage Growing

Japan's labour market has tightened considerably in recent years judging by a range of standard metrics. The unemployment rate has declined among all age groups and types of unemployed, e.g., long-term unemployed and involuntarily unemployed: at 2.8% it is below its pre-global financial crisis trough of 3.7%. Alternative measures of labour underutilization taking into account discouraged workers, and part-time employment due to economic reasons confirm the significant reduction in labour market slack. Other indicators such as vacancy rates, the job applicant-to-openings ratio, and survey-based measures confirm a considerable tightening in the labour market in recent years. Last May the ratio of open jobs to applicants hit a 43-year high, rising 0.01 points to a reading of 1.49, the highest since February 1974, as companies have struggled to fill positions from an ageing and shrinking workforce.

Nonetheless, wages have remained sluggish, complicating efforts to exit from deflation persistently and to achieve stronger private-sector led growth. Indeed, labour market duality and inflexibility are clogging the pass-through from a tightening labour market, and from high profits at large firms, to wage increases, which in turn amount to a missing link in the transmission of rising corporate earnings to actual and expected inflation. A combination of cyclical and structural factors seem to be at play. First, residual slack in the economy -mainly due to a weak recovery in the manufacturing sector- is putting downward pressure on wages as employment growth is concentrated in the less productive services sectors. Second, a trend increase in female labour force participation, mainly in part-time jobs, is dampening average wage growth. Third, structural characteristics of the Japanese labour market — the low horizontal mobility of regular workers, an industrial relations system emphasizing employment stability over wage increases, and limited wage bargaining power- dampen upward wage pressures even in the face of a tight labour market. Furthermore, wage setting tends to be backward looking, based on recent actual inflation rather than the 2% target of monetary policy — a rational expectation given that monetary policy is consistently failing to deliver 2% inflation. Without strong efforts to resolve this market coordination blockage, attempts to raise nominal GDP growth will remain elusive.

Because of this residual slack in the economy, increasing tightness in the labour market does not necessarily translate into a corresponding narrowing of the output gap, which remains mildly negative, or at least not positive, according to recent OECD estimates — the output gap is defined as the difference between actual and potential GDP, or total demand for goods and services versus total output capacity. "The demand shortfall is progressively ending because of a slump in potential GDP due to the labour shortage, rather than growing demand," says Toru Suehiro, a senior market economist at Mizuho Securities. A positive GDP gap is one of the government's four criteria for beating deflation. If demand consistently outweighs supply, sellers of goods and services find it easier to raise prices. Higher profits should encourage businesses to boost wages, fueling consumer spending and driving further price hikes.

Bank of Japan (BOJ) governor, Haruhiko Kuroda, has expressed confidence that such a virtuous cycle is in progress. The central bank said in April that by its reckoning, the GDP gap turned positive in the July–September quarter (however, the report introduced changes to the calculation method that lowered Japan's estimated production capacity, shifting the GDP gap by about 0.5 of a percentage points). This alignment with the government's view suggests that "a declaration of victory against deflation is getting closer," said Takuya Hoshino of the Dai-ichi Life Research Institute. But even if Japan fights off deflation, price growth shows little sign of picking up steam. The consumer price index, excluding volatile fresh foods and energy, remained flat on the year in June.

But Japan's current labour shortage carries the potential to jar prices out of the doldrums. After a decades-long shift towards insecure contract work and a two-tier labour market, companies are having to offer permanent jobs to find employees: the ratio of openings for full-employee positions to job seekers hit a record high of 0.97 in April. Greater competition for regular workers could lead to higher wage growth. "The labour shortage has become so bad that companies can fill openings only with part-timers," said Junko Sakuyama, a Tokyo-based senior economist at Dai-ichi Life Research Institute. It could also spur consumption, because workers with the security of a permanent job are more likely to spend money. The rise in regular positions suggests companies are responding to labour shortages by improving conditions for workers rather than increasing pay.

Economists say a decades-long move toward non-regular jobs — which now make up more than a third of the workforce — is partly to blame for weak consumer demand. Many work part time, and all on average receive less pay, few benefits, little training and no real job security. It is too early to declare a trend reversal, but the number of regular jobs grew by 260,000 in March from a year ago, while part-time, temporary and contract jobs rose by 170,000, the internal affairs ministry reported recently. The impact on wages and consumer spending may be limited, though. Regular workers get paid about 53% more than non-regular ones on a comparable monthly basis, according to the labour ministry, but they have seen slower pay increases because the unions representing them often favour job security over aggressive bargaining. Those sectors hiring more regular workers offer lower pay and suffer from lower productivity, meaning they have narrower margins to grant raises.

The point is that Japanese companies are wasteful in their use of labour and have a lot of pent-up ability to raise output per worker -output per hour worked is below the OECD average and only about 60% of US levels. If Japan were to reduce unpaid overtime, higher productivity should compensate for lower hours. According to a recent BOJ research, Japanese workers on average put in about 200 hours of unpaid overtime annually. Moreover, unpaid overtime is higher among service businesses, whose productivity is lower than manufacturers that are exposed to global competition. If workers and unions are prioritising cutting hours over raising pay it may help explain why a tight labour market is turning so slowly into higher wages.

MARKET DEVELOPMENTS

Though the Russia affair grinds on, the more significant Trump development is the failure of Democrats to make any electoral gains in recent high-profile contests and Trump's continued popularity among his Republican supporters. They blame Washington intrigues for Trump's difficulties and admire his perseverance against the machinations of the insider elite. Trump will certainly deregulate and already this is affecting the debates around Basel IV. With raw material capacity still abundant world growth is set fair even if slow by earlier cycle standards. There is nothing too wrong with this: it gives time for a new wave of productivity growth to settle in via the new robotics. Bank regulation will be unwound and monetary conditions will be normalised. The stage will be set for a re-evaluation of how monetary policy can avoid the next boom-bust catastrophe. We think the way forward is via Nominal GDP targeting. This remains a good environment for equities and we look for bond prices to fall as interest rates return to normal.

Table 1: Market Developments

	Market Levels		Prediction for Jul/Aug 2018	
	Jul 3	**Jul 29**	**Previous Letter**	**Current View**
Share Indices				
UK (FT 100)	7377	7368	11811	11797
US (S&P 500)	2429	2472	2951	3004
Germany (DAX 30)	12475	12163	19873	19375
Japan (Tokyo New)	1614	1621	1987	1996
Bond Yields (government				
UK	1.33	1.27	2.00	2.00
US	2.34	2.30	3.00	3.00
Germany	0.48	0.54	0.80	0.80
Japan	0.09	0.08	0.10	0.10
UK Index Linked	−1.58	−1.52	−1.00	−1.00
Exchange Rates				
UK ($ per £)	1.29	1.31	1.26	1.26
UK (trade weighted)	77.48	76.95	76.50	76.5
US (trade weighted)	101.76	99.75	102.4	102.4
Euro per $	0.88	0.85	0.92	0.92
Euro per £	1.14	1.12	1.16	1.16
Japan (Yen per $)	113.3	111.0	115.2	115.2
Short Term Interest Rates (3-month deposits)				
UK	0.28	0.28	1.50	1.50
US	1.32	1.34	1.50	1.50
Euro	−0.40	−0.40	−0.20	−0.20
Japan	−0.05	0.00	0.20	0.00

Table 2: Prospective Yields [1]

Equities: Contribution to £ yield of:

	Dividend Yield	Real Growth	Inflation	Changing Dividend Yield	Currency	Total
UK	3.60	2.7	2.4	55.00		63.70
US	1.99	2.4	2.2	16.90	3.96	27.45
Germany	3.30	1.6	1.7	56.00	−3.79	58.81
Japan	1.90	1.1	1.0	21.00	0.28	25.28
UK indexed[2]	−1.52		2.4	7.00		7.89
Hong Kong[3]	2.60	6.3	2.2	−4.00	3.96	11.06
Malaysia	3.30	4.8	2.2	47.00	3.96	61.26
Singapore	3.50	2.0	2.2	7.00	3.96	18.66
India	1.40	8.0	2.2	23.00	3.96	42.56
Korea	1.10	3.0	2.2	−20.00	3.96	−10.74
Indonesia	2.20	5.4	2.2	30.00	3.96	43.76
Taiwan	2.80	3.4	2.2	4.00	3.96	30.36
Thailand	3.20	2.6	2.2	19.00	3.96	30.96

Bonds: Contribution to £ yield of:

	Redemption Yield	Changing Nominal Rates	Currency	Total
UK	1.27	−7.30		−6.03
US	2.30	−7.00	3.96	−0.74
Germany	0.54	−2.60	−3.79	−5.85
Japan	0.08	−0.20	0.28	0.16

Deposits: Contribution to £ yield of:

	Deposit Yield	Currency	Total
UK	0.28		0.28
US	1.34	3.96	5.30
Euro	−0.40	−3.79	−4.19
Japan	0.0	0.28	0.28

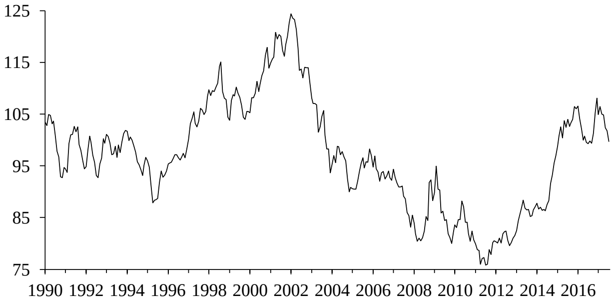
[1] Yields in terms of €s or $s can be computed by adjusting the £-based yields for the expected currency change.
[2] UK index linked bonds All Stocks
[3] Output based on China.

Table 3: Portfolio(%)

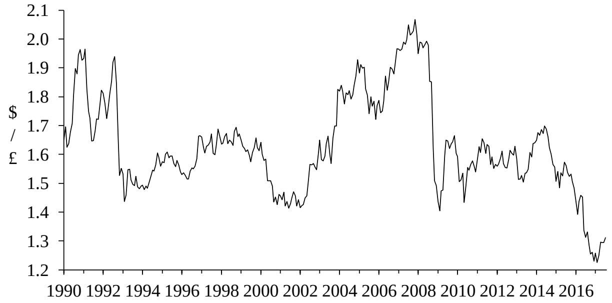
	Sterling Based Investor		Dollar Based Investor		Euro Based Investor	
	July Letter	Current View	July Letter	Current View	July Letter	Current View
UK Deposits (Cash)	5	5	5	5	1	1
US Deposits	-	-	-	-	-	-
Euro Deposits	-	-	-	-	-	-
Japanese Deposits	-	-	-	-	-	-
UK Bonds	-	-	-	-	-	-
US Bonds	-	-	-	-	-	-
German Bonds	-	-	-	-	-	-
Japanese Bonds	-	-	-	-	-	-
UK Shares	19	19	14	14	17	17
US Shares	14	14	19	19	16	16
German Shares	14	14	14	14	21	21
Japanese Shares	9	9	9	9	11	11
Hong Kong/Chinese Shares	4	4	4	4	4	4
Singaporean Shares	4	4	4	4	4	4
Indian Shares	4	4	4	4	4	4
Thai Shares	3	3	3	3	3	3
South Korean Shares	4	4	4	4	4	4
Taiwanese Shares	4	4	4	4	3	3
Brazilian Shares	4	4	4	4	3	3
Chilean Shares	4	4	4	4	3	3
Mexican Shares	4	4	4	4	3	3
Peruvian shares	4	4	4	4	3	3
Other:						
Index-linked bonds (UK)	-	-	-	-	-	-

INDICATORS AND MARKET ANALYSIS
FOREIGN EXCHANGE MARKETS

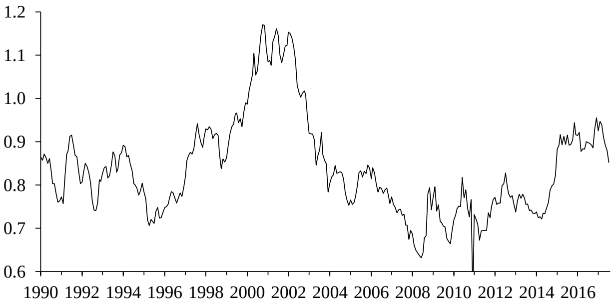
US : Trade Weighted Index
(Bank of England 1990 = 100)



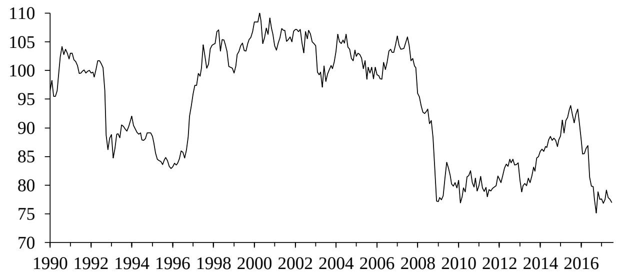
UK: Dollars Per Pound Sterling



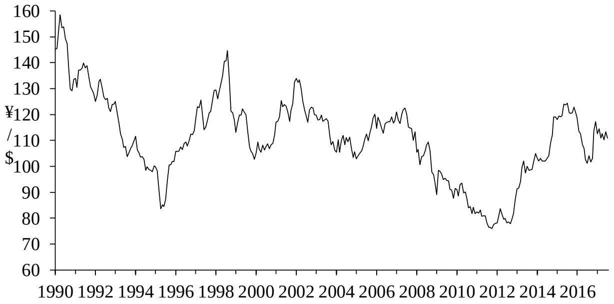
Euro per US dollar



UK: Trade-Weighted Index
(Bank of England 1990 = 100)



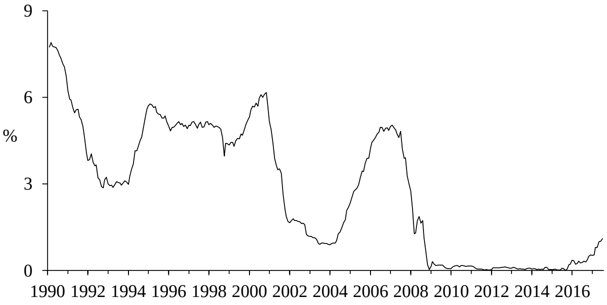
Japan : Yen Per U.S. Dollar



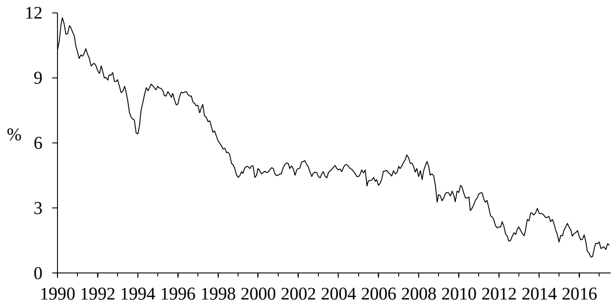
GOVERNMENT BOND MARKETS

U.S.: Yield on Long-Term Government Bonds

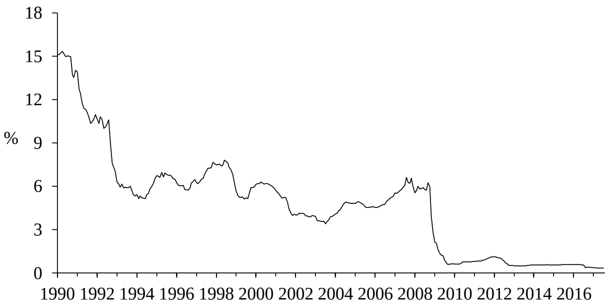
U.S. : 3-Month Treasury Bill



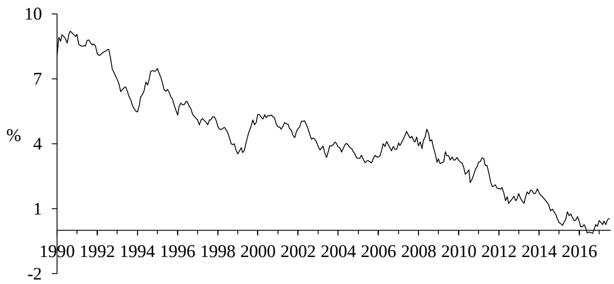
U.K.: Yield on Long-Term Government Bonds



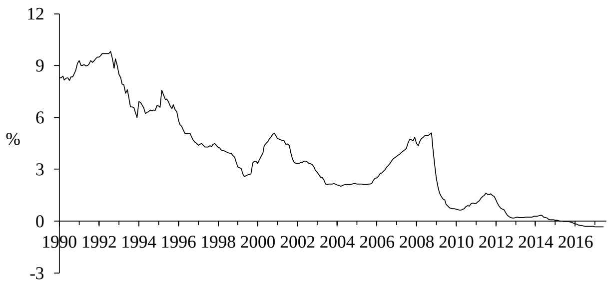
U.K. : 3-Month Interbank Rate



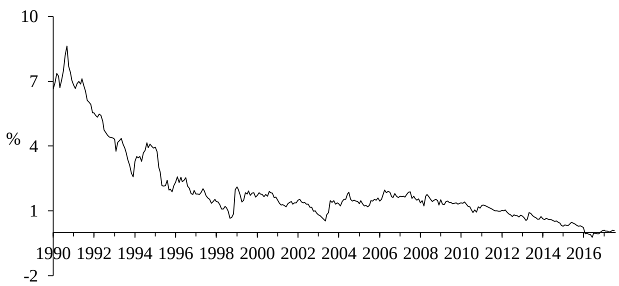
Germany: Yield on Public Authority Bonds



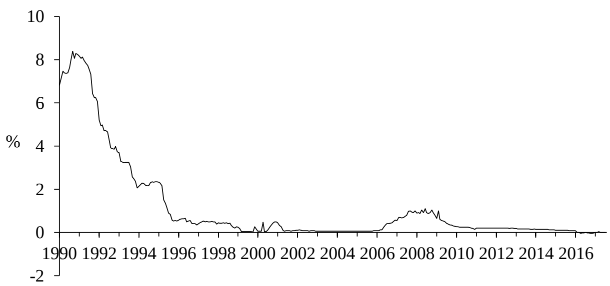
Germany : 3-Month Interbank Deposit Rate



Japan: Yield on Long-Term Government Bonds

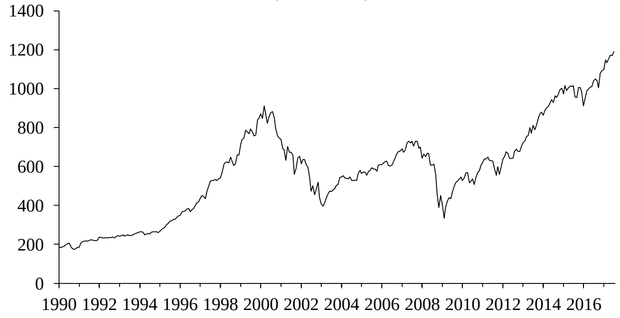


Japan : 3 Month Money Market Rate

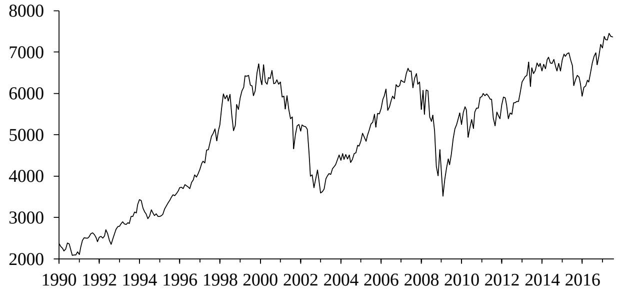


MAJOR EQUITY MARKETS

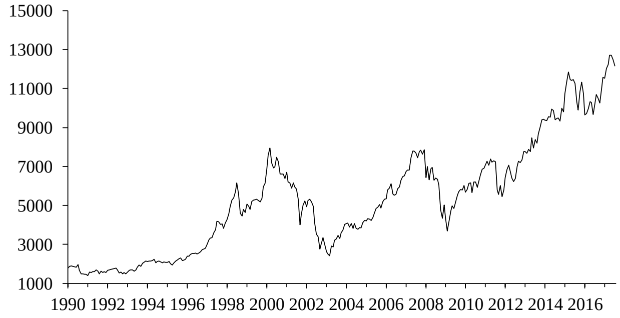
U.S. : S & P 400 Industrial (1985=100)



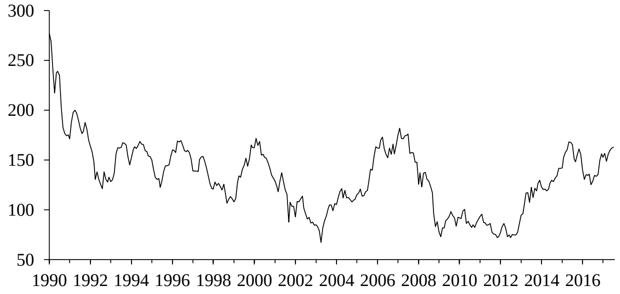
U.K. : FTSE-100 Index (10 April 1962=100)



Germany : DAX 30



Japan : Tokyo S.E. New (1985=100)



EMERGING MARKETS

Anupam Rastogi

India

The IMF has retained its economic growth forecast for India in its July world economic outlook. It has projected India's GDP to grow at 7.2% in 2017–18 and accelerate further to 7.7% in 2018–19. These estimates are marginally different from the Asian Development Bank growth forecast for India.

India seems to be enjoying a bright spot in the sun. The nation's cumulative rainfall so far has been better than expected and barring a couple of regions rainfall has been good. It gives hope that domestic consumption is going to remain strong and consumer inflation under control.

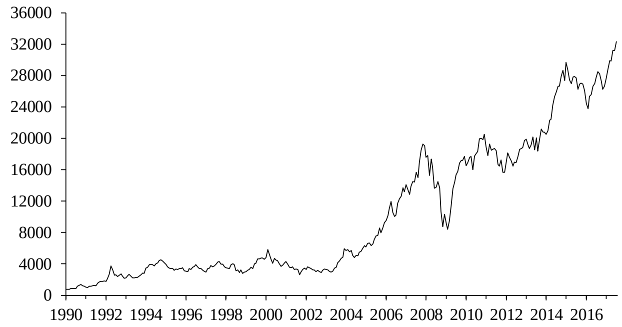
Consumer inflation in June cooled to a new record-low of 1.54% compared to consumer price inflation in May which was 2.18%. The cooling down of inflation is driven by a drop in food and oil prices. We believe this will intensify pressure on the Reserve Bank of India to cut interest rates by fifty basis points. The central bank has lowered its headline inflation forecasts to a range of 2.0–3.5% for the first half of fiscal year 2017–18 and 3.5–4.5% in the second half, down from 4.5% and 5.0%, respectively.

India's exports grew by 4.39% to $23.56 billion in June as shipments of chemicals, engineering and marine products improved. Imports too rose by 19% to $36.52 billion in June from $30.68 billion the previous year due to rise in inward shipments of oil and gold. This has resulted in the country's trade deficit of $12.96 billion compared to $8.11 billion trade deficit in June 2016.

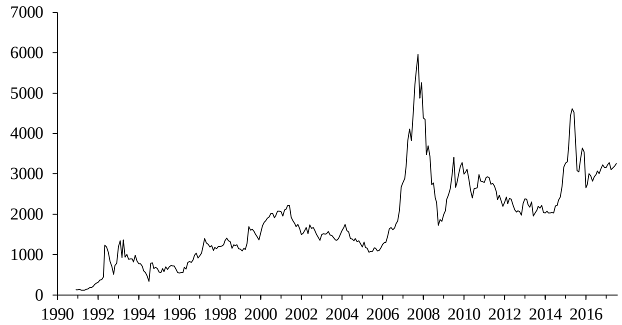
Low inflation expectations, high real interest rates and high political stability has made the Indian rupee attractive. Besides this the post-BJP win in assembly elections are viewed as strengthening government hand in accelerating reforms. The government has not disappointed on this front. Implementation of Goods and Services Tax (GST) went through without a hitch and is already showing significant efficiency gains in supply chain and transportation. Indian economic growth may be lifted by reduced transportation times and increased compliance that will boost revenue for the government that could be spent on infrastructure, sanitation and education.

India's securities regulator has suspended the issuance of offshore "masala bonds", after strong investment in rupee-denominated debt left foreign holdings pushing up against the legal limit. India's government has been keen to encourage the growth of masala bonds, which have enjoyed strong foreign interest since the first corporate issuance last year, with investors attracted by strong yields and robust economic growth.

India: BSE Sensitive



China: SSE Composite Index



	15–16	16–17	17–18	18–19	19–20
GDP (%p.a.)	8.0	7.1	7.5	8.0	8.1
WPI (%p.a.)	5.2	4.5	3.5	4.0	4.1
Current A/c(US$ bill.)	-24.0	-24.0	-26.0	-28.0	-30.0
Rs./$(nom.)	66.5	68.2	65.0	66.0	67.5

China

Chinese GDP grew 6.9% in the first and second quarters, an uptick on last year's 6.7% expansion. If the trend continues, 2017 would be the first year China's growth rate accelerates on the preceding since 2010. However, the good news as usual suffers from trust deficit. The IMF has also raised its forecast marginally to 6.7% in 2017 and 6.4% in 2018 from earlier projections.

Foreign trade has provided an unexpected boost to the manufacturing sector. After contracting 7.7% on an annual basis last year, exports grew 8.5% in the first half of 2017, reflecting strong demand from the US and Europe. Stable growth in the run-up to the Communist Party conclave in November is seen as essential to strengthening Mr. Xi's position in the political horse-trading.

China's fiscal spending surged 19.1% in June from a year earlier, more than doubling May's 9.2% growth. An acceleration in spending on public projects, such as social welfare and employment, is a reflection of the government's implementation of a proactive fiscal policy.

National government revenue growth also quickened to 8.9% in June from 3.7%.

But the outlook appears hazier because Beijing faces a policy dilemma in its battle to tame the property market, which, together with construction and home furnishings, now contributes to a third of the overall economy.

China's exports and imports both grew more than expected in June. China's exports rose 11.3% in June from a year earlier, marking the fourth straight month of gains. Imports in June also came in stronger than expected, expanding 17.2% from a year earlier, after a 14.8% increase in May. The cross-border capital flows are also under control, yuan-rate expectations have stabilized.

High-level economic talks between the U.S. and China ended without any progress, leaving the Trump administration's efforts to recast trade ties with Beijing in limbo. President Trump had told reporters earlier that the US has the worst of all trade deals with China. But, the North Korea issue may affect Mr. Trump's economic approach to China.

China's massive foreign-exchange reserves rose for a fifth straight month, edging up slightly from last month, as a weaker U.S. dollar and Beijing's stringent controls over moving money offshore helped arrest outflows. The reserves increased by $3.22 billion in June from the previous month to $3.057 trillion.

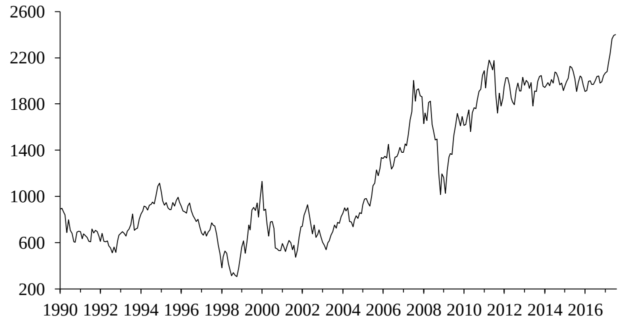
Chinese investors are not being welcomed for various reasons. Berlin clamped down on Chinese purchases of high-tech German companies. Further, the European Central Bank's supervisors are assessing whether to investigate HNA over its holding in Deutsche Bank, Germany's biggest lender. HNA became the largest shareholder in Deutsche Bank earlier this year. EU rules require supervisors to investigate investors who own more than 10% of a bank. But with a holding of 9.9%, HNA does not automatically qualify for an investigation.

	15	16	17	18	19
GDP (%p.a.)	6.9	6.5	6.7	6.3	6.0
Inflation (%p.a.)	1.4	2.0	2.2	2.0	2.1
Trade Balance(US$ bill.)	550	510	400	380	350
Rmb/$(nom.)	6.4	6.7	6.8	6.9	7.0

South Korea

The Bank of Korea Governor Lee Ju-yeol expects gross domestic product to expand 2.8% this year, exceeding the previous forecast of 2.6%, and close to the country's potential growth rate. The growth is going to get a push from fiscal stimulation.

Korea: Composite Index



South Korea's National Assembly passed a nearly $10 billion supplementary budget and approving a key component of the new left-leaning president's plan to boost Asia's fourth-largest economy through public-sector hiring. South Korea said it would boost its minimum wage by 16.4%, a sharp rise compared with recent increases in other developed economies, drawing criticism from small businesses as the country's new left-leaning administration implements its policy agenda.

President Moon Jae-in, who took office in May, is pushing for a greater role for the government in creating jobs and spurring domestic demand, and has called for a substantial increase in the minimum wage to address income inequality.

South Korea's central bank held its benchmark interest rate unchanged at 1.25% while raising its growth forecast for exports. The BOK expects inflation to fluctuate around 2% for some time. The Asian Development Bank expects South Korea's inflation to grow 1.8% this year, compared with a previous forecast of 1.7%. We believe that South Korea's central bank will begin tightening its monetary policy in 2018, despite expectations that the U.S. Federal Reserve may again raise its key rate by the end of this year.

The won appreciated gradually against the dollar to 1,140 as the trade surplus saw a large drop to $6.0 billion in May 2017 as compared to $13.0 billion in the previous month. The trade surplus in May 2017 was the smallest in the last six months, as exports fell against the rise in imports. The exports dropped 12% in May 2017 to $45.0 billion as compared to the previous month when they stood at $39.1 billion. But, exports have kept up strong growth momentum in July, gaining 22.4% on year to $30 billion in the first 20 days on strong ship and semiconductor exports. The growth in exports was mainly led by ships, semiconductors, and automobiles. Imports over the same period grew 13.3% to $25.9 billion to deliver a trade surplus of $4.1 billion.

	15	16	17	18	19
GDP (%p.a.)	2.6	2.8	2.8	2.5	2.5
Inflation (%p.a.)	0.7	1.0	1.6	1.2	1.3
Current A/c(US$ bill.)	90.0	88.0	88.0	86.0	80.0
Won/$(nom.)	1180	1160	1125	1140	1145

Taiwan

Taiwan's real gross domestic product growth estimate for 2017 is revised upward to 2.2% from 1.7% reflecting greater confidence in the economy and improving fiscal conditions at home and abroad. Taiwan reported GDP growth of 2.6% for the first quarter of the year on the back of expanded capital spending and robust export numbers.

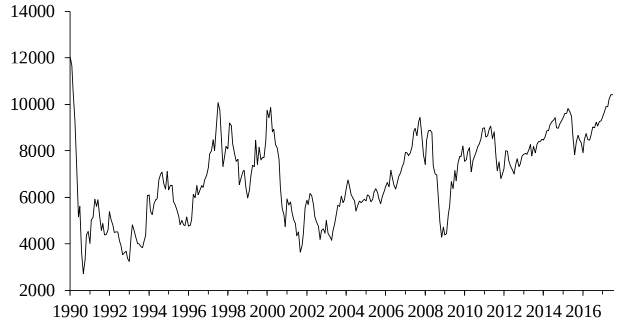
Due to increased spending by consumers and a revival in exports, the Asian Development Bank (ADB) has also revised its forecast for growth in Taiwan to 2% for this year and 2.2% in 2018.

Inflation in Taiwan is forecast to fall from 1.3% to 1.1%, due to lower domestic food prices relative to earlier forecasts and lower gas costs.

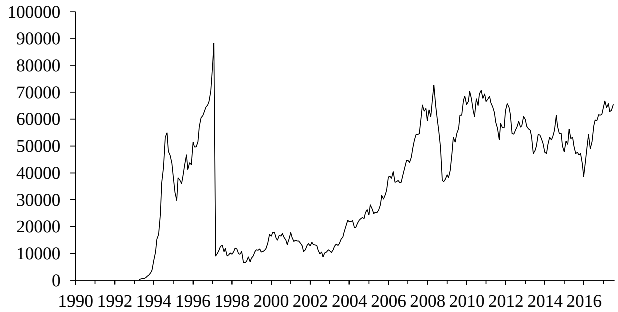
Taiwan's exports in June surged more than expected, underpinned by robust shipments into China, as the tech supply chain for gadgets that make up smartphones and ultra-thin laptops enters its seasonally-busy second half. June exports rose 13% from a year ago, increasing for a ninth straight month and beating the 8.7% forecast. Imports rose a smaller 3.7% for the same time period.

	15	**16**	**17**	**18**	**19**
GDP (%p.a.)	0.8	1.4	2.5	2.6	2.3
Inflation (%p.a.)	0.7	1.0	1.0	1.0	1.2
Current A/c(US$ bill.)	60.0	64.0	68.0	68.0	70.0
NT$/$(nom.)	32.8	32.5	32.0	32.0	32.0

Taiwan: Weighted TAIEX Price Index



Brazil: Bovespa



Brazil

Brazil's economy which suffered through its worst recession in 2015 and 2016, has hit government revenue and this has resulted in fiscal deficit. President Michel Temer has been forced to cut spending, and now raise taxes, to try make up for some of the resulting shortfall in tax proceeds. In order to cut budget deficit, Brazil will double some taxes on fuels. The measure will raise an extra 10.4 billion reals ($3.3 billion) this year.

Consumer prices in Brazil grew by 3% year-on-year in June 2017, compared with 3.6% in May 2017, mainly due to a slump in the cost of food and a decline in electricity prices. The Central Bank of Brazil expects the inflation rate on an annual basis drop below its target rate of 4.5% by the end of 2017. Inflation expectations are around 3.7% and 4.4% for 2017 and 2018, respectively. The drastic fall in inflation from a 12-year high of 10.71% at the beginning of last year will be used by Mr. Temer's government to underpin its argument that Latin America's largest economy is set to emerge from its worst recession in history.

The Selic rate fixed at 10.25% in May 2017, expected to encourage consumption, should help boost Brazil's economic recovery in 2017.

Brazil's trade balance since the beginning of 2017 indicates continuous expansion, with exports rising more than imports. Brazil recorded a $7.2-billion trade surplus in June 2017, compared with $3.9 billion in surplus in June 2016. In the first six months trade surplus stood at $36.2 billion, which was a 53.1% increase over the same period the previous year. The rise in surplus resulted from increased exports, which grew 19.3%, while imports increased 7.3% during the same period.

The Brazilian real has been on a downtrend after the allegations of corruption against President Temer strengthened in March 2017. The Brazilian real has dropped approximately 2% amid the ongoing political instability.

Brazil's Senate approved a bill that will make extensive changes to the country's labour laws, cheering investors and giving embattled President Michel Temer some much-needed good news. The bill will update the country's decades-old labour regulations, permitting more flexible employment rules, eliminating union dues and making it harder for workers to sue their employers. Mr. Temer's more controversial reforms, to Brazil's insolvent pension system and the just-approved labour proposal, have met with more resistance and the pension bill appears to be stalled in Congress while the president grapples with the corruption accusations.

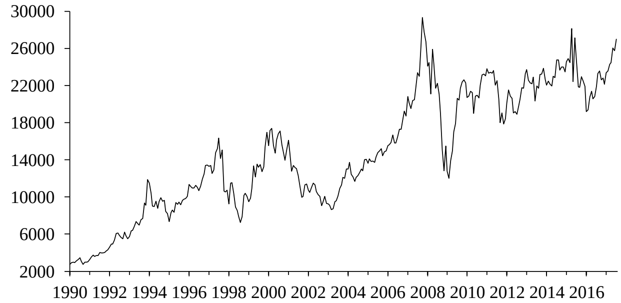
The lower house of Brazil's Congress is due to vote in coming days on whether or not Mr. Temer should face a trial in the country's Federal Supreme Court on the charges that he accepted bribes. Mr. Temer has denied any wrongdoing.

Mr. Lula, the champion of Brazil's left who served two terms as president from 2003–2011 was convicted for money laundering and corruption and sentenced to nearly 10 years in prison. He is accused of steering government contracts to the Brazilian construction firm OAS in exchange for roughly $1.2 million in bribes in the form of a refurbished beach-front apartment. Should he win next year before the appeal is concluded, the sentence and legal appeal would be suspended until he finishes his four-year term. Brazil's political maturity will be tested as much as its rule of law. On the other hand, if the conviction is upheld by an appeals court, Mr Lula da Silva will be rendered ineligible to contest next year's elections, ending his hopes of making a political comeback and removing one of the strongest potential candidates from Brazil's left.

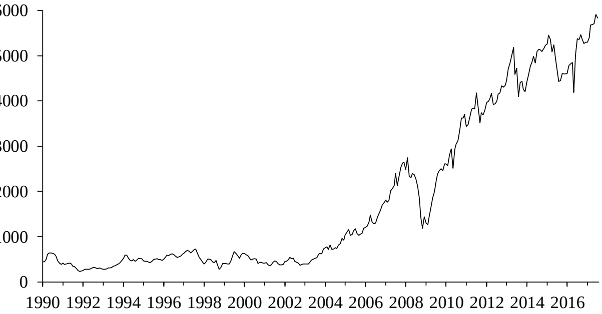
	15	**16**	**17**	**18**	**19**
GDP (%p.a.)	-3.8	-3.6	0.5	1.5	3.0
Inflation (%p.a.)	10.7	6.3	4.4	4.5	4.0
Current A/c(US$ bill.)	-70.0	-28.0	-25.0	-25.0	-32.0
Real/$(nom.)	3.9	3.5	3.4	3.2	3.2

Other Emerging Markets

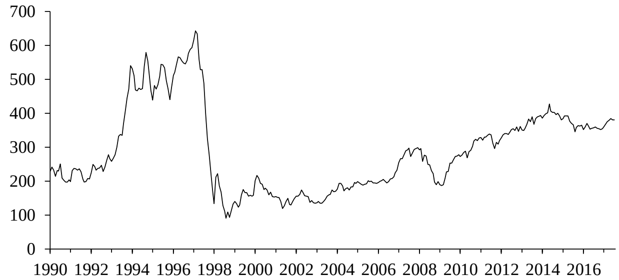
Hong Kong: FT-Actuaries



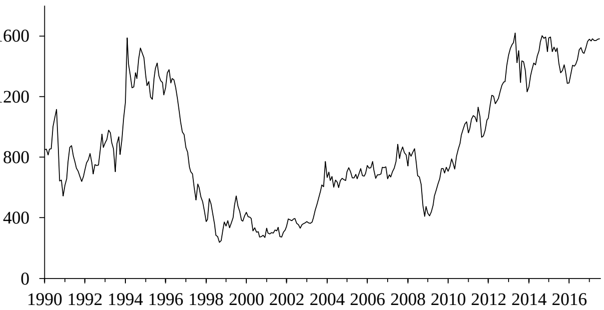
Indonesia: Jakarta Composite



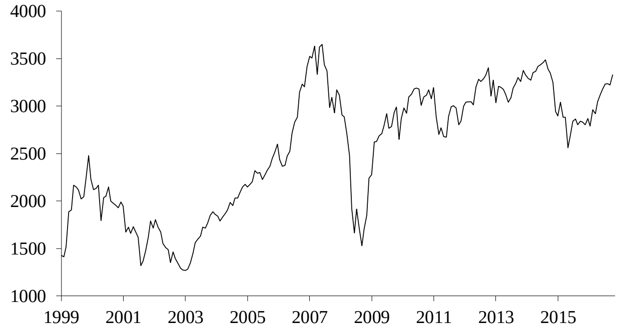
Malaysia: FT-Actuaries
(US$ Index)



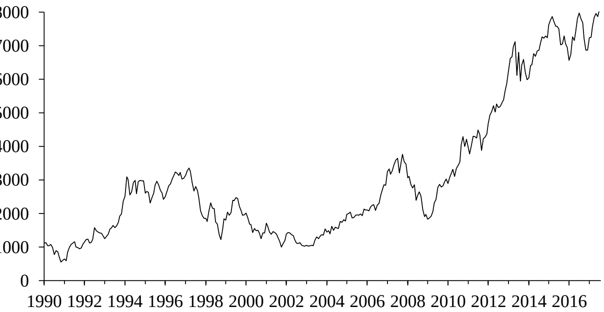
Thailand: Composite Index



Singapore: Straits Times Index

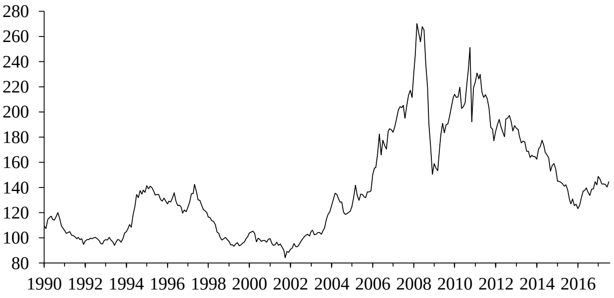


Philippines: Manila Composite

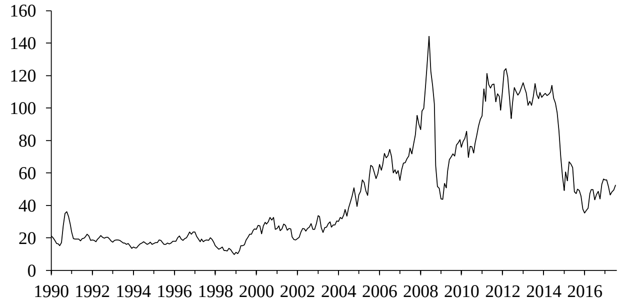


COMMODITY MARKETS

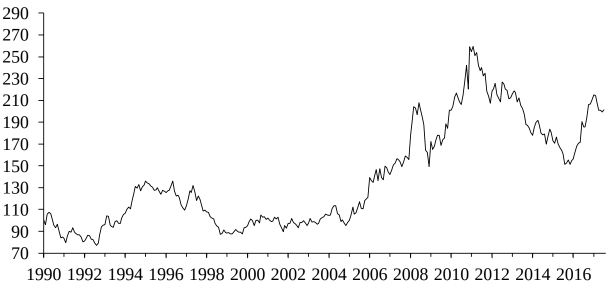
Commodity Price Index (Dollar)
(Economist, 2000=100)



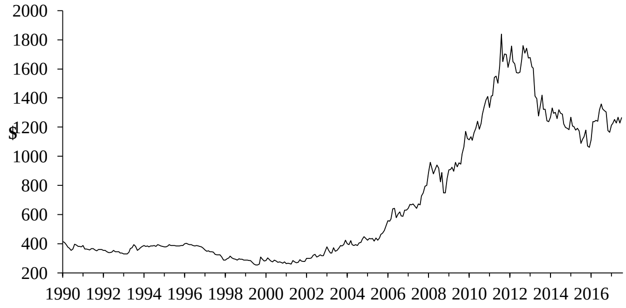
Oil Price: North Sea Brent (in Dollars)



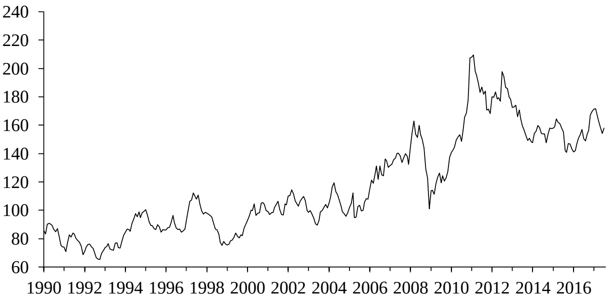
Commodity Price Index (Sterling)
(Economist, 2000=100)



Gold Price (in Dollars)



Commodity Price Index (Euro)
(Economist)



UK FORECAST DETAIL

Prices, Wages, Interest Rates and Exchange Rate Forecast (Seasonally Adjusted)

	Inflation %[1] (CPI)	Short Dated (5 Year) Interest Rates	3 Month Int. Rates	Nominal Exchange Rate (2005=100)[2]	Real Exchange Rate[3]	Real 3 Month Int. Rates %[4]	Inflation (RPIX)	Real Short Dated Rate of Interest[5]
2015	0.2	1.3	0.6	91.6	91.6	0.5	1.0	-1.0
2016	1.2	0.9	0.4	81.5	80.4	-1.6	2.1	-1.5
2017	2.6	1.1	0.9	77.8	76.4	-1.7	3.2	-1.7
2018	2.6	2.0	1.5	76.1	75.1	-1.3	3.1	-1.0
2019	3.0	2.9	2.5	74.7	74.6	-0.1	3.4	0.0
2020	3.0	3.0	3.0	73.4	74.4	0.5	3.5	0.0
2016:1	0.3	0.9	0.7	87.2	86.8	-1.1	1.4	-0.7
2016:2	1.3	0.9	0.5	81.8	81.2	-1.3	2.2	-0.9
2016:3	1.5	0.9	0.2	79.4	77.8	-1.7	2.3	-1.0
2016:4	1.8	0.9	0.2	77.6	75.9	-1.8	2.5	-1.2
2017:1	2.1	1.0	0.5	79.0	77.4	-1.6	2.8	-1.9
2017:2	2.6	1.2	0.5	78.7	77.4	-1.5	3.2	-1.9
2017:3	2.8	1.2	1.0	76.9	75.4	-1.5	3.3	-1.8
2017:4	3.0	1.2	1.5	76.6	75.4	-1.5	3.5	-1.3
2018:1	2.4	1.5	1.3	76.8	75.4	-1.5	3.0	-1.5
2018:2	2.4	2.0	1.5	76.5	75.4	-1.4	3.0	-1.0
2018:3	2.8	2.0	1.5	75.3	74.4	-1.5	3.3	-1.0
2018:4	2.8	2.5	1.5	75.7	75.4	-1.5	3.3	-0.5

[1] Consumer's Expenditure Deflator
[2] Sterling Effective Exchange Rate Bank of England
[3] Ratio of UK to other OECD consumer prices adjusted for nominal exchange rate
[4] Treasury Bill Rate less one year forecast of inflation
[5] Short Dated 5 Year Interest Rate less average of predicted 5 year ahead inflation rate

Labour Market and Supply Factors (Seasonally Adjusted)

	Average Earnings (1990=100)[1]	Wage Growth[2]	Unemployment (New Basis) Percent[3]	Millions	Real Wage Rate[4] (1990=100)
2015	247.1	2.4	2.3	0.8	141.1
2016	254.3	2.9	2.1	0.7	143.5
2017	260.8	2.6	2.2	0.8	146.3
2018	270.1	3.6	2.1	0.8	150.8
2019	282.7	4.7	2.0	0.7	155.6
2020	295.3	4.5	1.9	0.7	159.5
2016:1	252.0	2.1	2.1	0.7	143.2
2016:2	252.1	2.5	2.2	0.8	142.7
2016:3	254.4	2.4	2.2	0.8	143.5
2016:4	254.3	2.5	2.3	0.8	142.5
2017:1	257.7	2.3	2.2	0.8	143.8
2017:2	259.8	3.1	2.2	0.8	144.6
2017:3	261.9	3.0	2.2	0.8	145.0
2017:4	263.4	3.6	2.2	0.8	144.6
2018:1	266.0	3.2	2.1	0.8	145.0
2018:2	267.9	3.1	2.1	0.8	145.6
2018:3	271.4	3.6	2.1	0.8	146.2
2018:4	275.0	4.4	2.0	0.7	147.0

[1] Whole Economy
[2] Average Earnings
[3] Wholly unemployed excluding school leavers as percentage of employed and unemployed, self employed and HM Forces
[4] Wage rate deflated by CPI

Estimates and Projections of the Gross Domestic Product[1] (£ Million 1990 Prices)

	Expenditure Index	£ Million '90 prices	Non-Durable Consumption[2]	Private Sector Gross Investment Expenditure[3]	Public Authority Expenditure[4]	Net Exports[5]	AFC
2015	156.5	749593.1	430478.9	302953.3	196562.0	-50539.3	129861.8
2016	159.4	763130.9	440238.4	297248.0	198473.7	-55145.2	117683.9
2017	163.1	781039.6	458510.3	276002.6	201835.6	-31228.2	124080.0
2018	167.4	801728.0	469801.9	276816.4	205872.3	-23275.3	127485.1
2019	172.2	824788.8	481547.0	275786.6	209989.8	-11175.3	131356.0
2020	178.2	853457.0	493585.6	287525.6	214189.6	-5675.3	136174.4
2015/14	2.2		1.6	3.8	1.1		-2.3
2016/15	2.3		3.3	-6.3	1.0		-3.7
2017/16	2.1		1.3	0.5	0.9		3.5
2018/17	2.6		1.9	0.8	1.0		2.7
2019/18	2.9		2.2	-0.6	1.2		3.0
2020/19	3.5		2.3	3.9	1.9		3.7
2016:1	158.1	189138.4	108678.4	72398.4	50736.1	-13542.0	29132.6
2016:2	158.9	190275.7	109825.3	73785.0	48907.3	-12813.4	29428.6
2016:3	159.7	191226.4	110456.6	75298.0	49388.4	-16711.1	27205.5
2016:4	160.8	192490.5	111278.1	75766.5	49441.8	-12078.7	31917.3
2017:1	161.3	193068.3	110289.9	73007.2	51174.2	-10116.5	31287.1
2017:2	162.2	194226.4	111206.1	74520.6	49141.5	-10103.9	30538.0
2017:3	163.3	195469.2	111967.0	75369.8	49891.8	-11094.1	30664.8
2017:4	164.2	196638.6	112632.2	75930	50099.3	-10691.5	31330.6
2018:1	165.6	198242.7	112567.2	73572.7	51892.3	-8179.1	31610.3
2018:2	166.6	199460.3	113264.8	76217.0	49423.6	-7778.1	31666.7
2018:3	167.2	200136.3	113966.8	74803.9	50232.4	-7096.8	31769.2
2018:4	168.5	201737.9	114673.1	76633.7	50696.1	-8167.1	32097.0

1 GDP at factor cost. Expenditure measure; seasonally adjusted
2 Consumers expenditure less expenditure on durables and housing
3 Private gross domestic capital formation plus household expenditure on durables and clothing plus private sector stock building
4 General government current and capital expenditure including stock building
5 Exports of goods and services less imports of goods and services

Financial Forecast

	PSBR/GDP %[1]	GDP[1] (£bn)	PSBR (£bn) Financial Year	Debt Interest (£bn)	Current Account (£ bn)
2015	4.6	1533.1	71.2	52.0	-103.7
2016	4.3	1592.4	69.0	52.3	-89.0
2017	3.2	1662.4	53.4	55.7	-63.7
2018	2.5	1756.4	44.8	61.6	-44.9
2019	2.0	1861.6	37.2	66.6	-14.4
2020	0.7	1477.6	12.8	51.5	0.5
2016:1	-0.1	384.6	-0.5	13.1	-33.7
2016:2	5.8	392.0	22.9	13.1	-14.0
2016:3	2.4	394.5	9.5	12.9	-13.1
2016:4	5.8	402.2	23.2	13.0	-28.2
2017:1	4.1	403.3	16.6	13.1	-18.4
2017:2	3.0	407.5	12.2	13.2	-17.6
2017:3	3.2	412.4	13.1	13.7	-17.2
2017:4	3.1	419.3	13.1	14.3	-10.4
2018:1	3.6	423.3	15.1	14.4	-15.3
2018:2	2.4	429.2	10.2	14.9	-13.8
2018:3	2.6	434.9	11.3	15.1	-10.1
2018:4	2.6	442.2	11.4	15.7	-5.7

1 GDP at market prices (Financial Year)

WORLD FORECAST DETAIL

Growth Of Real GNP

	2013	2014	2015	2016	2017	2018
U.S.A.	1.5	2.4	2.4	2.1	2.1	2.4
U.K.	2.2	2.9	2.2	2.3	2.1	2.6
Japan	1.4	–0.1	0.5	1.0	1.4	1.1
Germany	0.3	1.6	1.7	1.8	1.6	1.6
France	0.7	0.2	1.1	1.4	1.4	1.5
Italy	–1.7	–0.3	0.8	1.1	0.9	0.9

Growth Of Consumer Prices

	2013	2014	2015	2016	2017	2018
U.S.A.	1.5	1.6	0.1	1.3	2.4	2.2
U.K.	2.3	1.7	0.2	1.2	2.6	2.6
Japan	0.4	2.7	0.8	0.2	0.7	1.0
Germany	1.5	0.9	0.3	0.5	1.8	1.7
France	0.9	0.5	0.0	0.4	1.3	1.3
Italy	1.2	0.2	0.1	0.2	1.4	1.3

Real Short-Term Interest Rates

	2013	2014	2015	2016	2017	2018
U.S.A.	–1.5	–0.1	–1.1	–1.4	–1.1	–0.4
U.K.	–0.8	–2.2	-1.0	–1.6	–1.7	–1.3
Japan	–2.5	–0.6	0.0	–0.7	–1.0	–1.5
Germany	–0.6	–0.2	–0.6	–2.0	–2.0	–2.2
France	–0.2	0.1	–0.5	–1.5	–1.6	–1.8
Italy	0.1	0.0	–0.3	–1.6	–1.6	–1.9

Nominal Short-Term Interest Rates

	2013	2014	2015	2016	2017	2018
U.S.A.	0.1	0.0	0.2	1.0	1.1	1.6
U.K.	0.6	0.6	0.6	0.4	0.9	1.5
Japan	0.2	0.2	0.2	0.0	0.0	0.0
Germany	0.3	0.1	–0.1	–0.2	–0.3	–0.2
France	0.3	0.1	–0.1	–0.2	–0.3	–0.2
Italy	0.3	0.1	–0.1	–0.2	–0.3	–0.2

Real Long-Term Interest Rates

	2013	2014	2015	2016	2017	2018
U.S.A.	1.6	0.7	0.3	0.3	0.5	1.0
U.K.	–0.8	–0.7	–1.0	–1.5	–1.7	–1.0
Japan	–0.8	–1.1	–1.3	–1.2	–1.3	–1.5
Germany	0.8	–0.8	–1.0	–1.6	–1.4	–1.2
France	1.1	–0.5	–0.8	–1.4	–1.0	–0.8
Italy	1.2	–0.5	–0.7	–1.3	0.4	0.6

Nominal Long-Term Interest Rates

	2013	2014	2015	2016	2017	2018
U.S.A.	3.0	2.2	2.2	2.4	2.6	3.0
U.K.	1.3	1.8	1.3	0.7	1.1	2.0
Japan	0.7	0.3	0.3	0.0	0.1	0.1
Germany	1.9	0.5	0.6	0.4	0.5	0.8
France	1.9	0.5	0.6	0.4	0.9	1.2
Italy	1.9	0.5	0.6	0.4	2.3	2.6

Index Of Real Exchange Rate(2000=100)[1]

	2013	2014	2015	2016	2017	2018
U.S.A.	82.1	83.9	93.0	94.0	94.5	94.8
U.K.	86.5	93.1	91.6	80.4	76.4	75.1
Japan	63.5	59.8	56.0	58.4	58.3	58.1
Germany	99.0	99.9	94.7	95.0	94.3	94.9
France	100.7	100.8	96.2	96.0	95.4	95.2
Italy	106.9	107.5	102.1	102.0	101.2	101.1

[1] The real exchange rate is the domestic price level relative to the foreign price level converted into domestic currency. A rise in the index implies an appreciation in the real exchange rate.

Nominal Exchange Rate
(Number of Units of Local Currency To $1)

	2013	2014	2015	2016	2017	2018
U.S.A.[1]	85.61	89.04	103.08	101.91	102.20	102.40
U.K.	1.55	1.65	1.53	1.35	1.28	1.26
Japan	98.20	106.70	120.00	118.40	113.50	115.20
Eurozone	0.75	0.76	0.90	0.95	0.93	0.92

[1] The series for the USA is a trade weighted index (1990=100); the series for the UK is $ per £

* Forecasts based on the Liverpool World Model