LIVERPOOL INVESTMENT LETTER

April 2015

Cardiff Business School
Cardiff University

Julian Hodge Institute of Applied Macroeconomics

LIVERPOOL RESEARCH GROUP IN MACROECONOMICS

LIVERPOOL RESEARCH GROUP IN MACROECONOMICS

Editorial and Research Direction: Patrick Minford†.

Senior Research Associates: Kent Matthews†, Anupam Rastogi, Peter Stoney, Bruce Webb†, John Wilmot.

Research Associates: Vo Phuong Mai Le†, David Meenagh†, Francesco Perugini, Yongdeng Xu†.

† Cardiff Business School

The Julian Hodge Institute was launched in autumn 1999 in a new collaboration between the Cardiff Business School of Cardiff University and Julian Hodge Bank. 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. This research has been given especial relevance by the ongoing discussions on the extra powers regularly requested by the European Union and also by the recent crisis in the eurozone.

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 Jane 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 Bruce Webb and published on behalf of the group by Liverpool Macroeconomic Research Limited, which holds the copyright

ISSN 0951-9262

LIVERPOOL INVESTMENT LETTER

April 2015

CONTENTS

MONETARY TARGETS IN THE MODERN ERA

The inflation target for monetary policy was new in 1992, when introduced here soon after our ejection from Europe's Exchange Rate Mechanism on Black Wednesday. New Zealand had been the first to use one a few years before. The new target has been an undoubted success here in that we have had little inflation ever since its introduction; it has also been highly credible, as evidenced by little drift away from 2% in measures of inflation expectations. Its credibility and its success in keeping inflation stable and low are just two sides of the same coin, since the credibility has stopped any group from making wage settlements or setting price increases at all far away from what 2% would imply.

But, as so often when we make strides in economic policy, a further problem has been revealed about the conduct of monetary policy according to this inflation target. We have seen poor control of credit booms and busts, as illustrated by the boom of the 2000s and the bust of 2007–9. The original idea was that monetary policy would be spurred to control the boom by surging inflation and the bust by sharply falling inflation. Neither really happened. During the boom inflation stayed moderate; it actually rose during the bust as oil and commodity surged, but this inflationary surge came after the bust and so gave the wrong signal.

What we have seen here is an illustration of how if you change the policy regime behaviour changes; in this case the key behaviour that changed was the response of inflation to boom and bust. The new policy regime assumed inflation would continue to respond strongly to these but in the event it did not, for the reason we have given that people built the new regime into their behaviour and so moderated their inflation responses.

So the question today is how we should repair our monetary policy target regime and how within it we should respond to an inflation rate temporarily zero and maybe briefly negative?

Take the first question of target first. It seems that what is missing from the previous regime was the old-fashioned response of monetary conditions to the business cycle: what a Fed Governor once famously called 'taking the punch bowl away as the party gets too merry'. This element could be supplied by varying the supply of money, as in Quantitative Easing (QE), to some degree independently of inflation and interest rates. The supply of money is supposed to affect credit and interest rates charged by banks and others like them.

Table 1: Summary of Forecast

	2012	2013	2014	2015	2016	2017	2018
GDP Growth[1]	0.7	1.7	2.6	2.8	2.5	2.5	2.5
Inflation CPI	2.1	1.9	1.7	1.4	1.7	1.7	2.0
RPIX	3.2	3.1	2.5	2.3	2.4	2.5	2.7
Unemployment (Mill.)							
Ann. Avg.[2]	1.6	1.4	1.1	0.9	0.8	0.8	0.7
4th Qtr.	1.6	1.3	1.0	0.9	0.8	0.7	0.7
Exchange Rate[3]	83.0	81.5	87.7	90.3	90.4	90.4	90.1
3 Month Interest Rate	0.9	0.6	0.6	1.0	1.6	2.0	2.1
5 Year Interest Rate	0.9	1.3	1.9	2.2	2.5	2.5	2.5
Current Balance (£bn)	–53.2	–65.9	–80.9	–72.0	–72.3	–72.7	–73.3
PSBR (£bn)	110.6	91.1	91.5	75.8	56.5	24.3	3.7

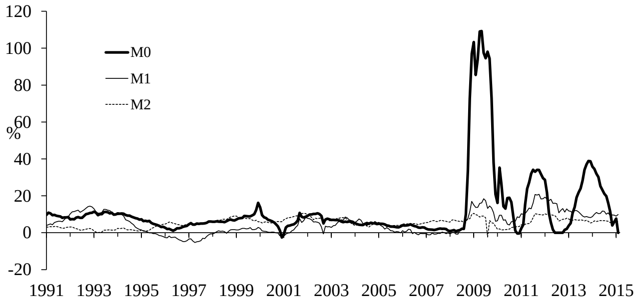
[1]Expenditure estimate at factor cost
[2]U.K. Wholly unemployed excluding school leavers (new basis)
[3]Sterling effective exchange rate, Bank of England Index (2005 = 100)

Another idea is to stiffen the response of Bank Rate itself by replacing an inflation target by a target for 'Nominal GDP', or for one element of Nominal GDP, the Price Level. Nominal GDP is defined as the economy's Output times the Price Level. Suppose one wants prices to grow at 2% (target inflation) and output to grow at 3% (target growth). Add the two together to make 5% and record the cumulative growth of both from some initial date, say 2012. Adjust Bank Rate up or down if the cumulative total exceeds or falls short of the cumulative target. The idea is that booms typically generate several years of excessive growth and so the accumulated overshoot would trigger a progressively stronger response from Bank Rate; and vice versa with busts which typically deliver several years of below par growth and inflation. Much the same argument applies if you only did this for the Price Level and excluded output from the calculation.

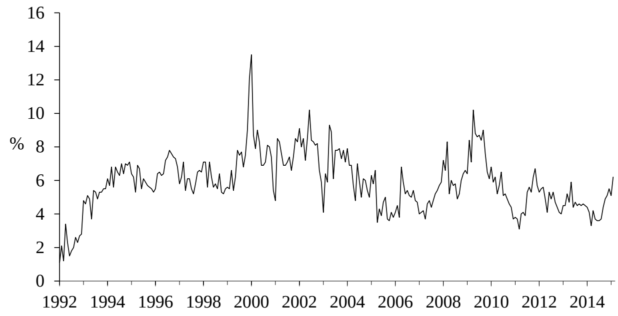
Some experiments with these ideas on models of the economy suggest they would work quite well to restore the old party-pooping responses into monetary policy, while also maintaining the control of inflation that now exists. One could combine a QE rule with such a beefed-up Bank Rate rule.

Against this background we can consider next how to respond to today's 'deflation' combined with strong growth in output and employment. Latest figures suggest that the economy is cumulatively not too far below a reasonable target level, and may even be moving above it, while the huge rise in QE has pushed asset prices up and encouraged peer-to-peer lending on a large scale. Yet Bank Rate is still glued to the floor and QE remains at £375 billion, a huge holding of government bonds by the Bank of England. We would argue it is time to move both back slowly towards normal.

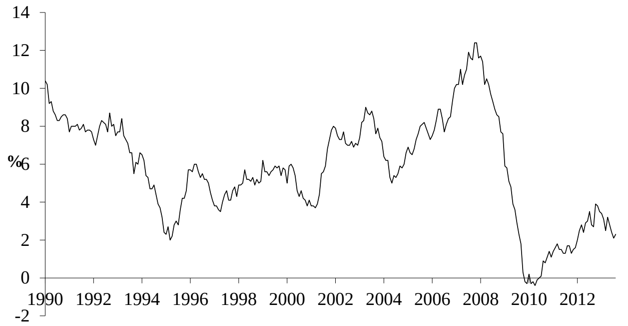
U.S.: Growth in Monetary Aggregates (Yr - on - Yr)



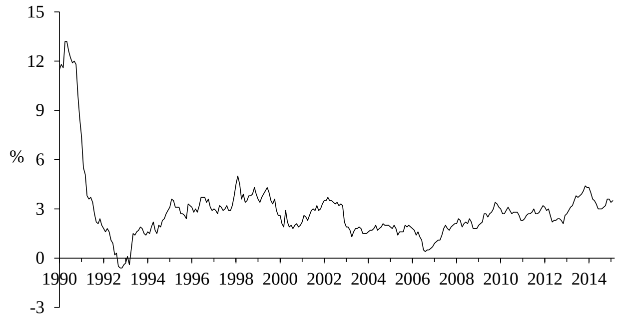
UK: Notes and Coins in Circulation Growth



Eurozone M3 Growth



Japan: Growth of M2+CD's



FOCUS ON JAPAN

Francesco Perugini

Slowing Inflation Keeps BOJ Under Pressure

The second GDP data release for the fourth quarter of 2014 shows that Japan's economy grew at a slower pace than initially thought: by 0.4% quarter-on-quarter against the original 0.6% estimate. The quarterly revision pushed down the annual GDP figure for 2014 to a slight contraction from a tiny expansion, the first annual decline in Japan's economy in three years — another piece of disappointing news.

Other disappointing news has emerged recently: Japan's core consumer price index (CPI) — when excluding the effect of last April's sales tax hike — was flat in February compared with a year earlier. This is the first time since May 2013 that the CPI has stopped rising. The Bank of Japan (BOJ) added that "tumbling energy prices could push inflation to zero" over the coming months, which is another blow to efforts to reach the two percent inflation target, a cornerstone of Prime Minister Shinzo Abe's drive to kick-start the economy.

Investors will now be following Bank of Japan chief Haruhiko Kuroda's regular news briefing for clues about the BOJ's plans for its massive two-year-old stimulus. Kuroda believes public expectations of inflation have risen and a tightening labour market will push price rises up to 2% "in or around fiscal 2015". He added that the BOJ would ease policy further if its target is no longer in sight. However, for the first time, he also acknowledged that his original promise to hit 2% inflation within two years from April 2013 had come unstuck.

Japan's central bank, on a mission to banish entrenched deflation, has been buying assets for the past two years, promising to double the country's monetary base. Last October's "double bazooka" accelerated purchases to ¥80 trillion a year. The BOJ's goal is to lower real interest rates — the expected return after adjusting for inflation — by convincing the Japanese public that future inflation will be high. In this way the bank hopes to persuade companies to invest more and consumers to buy more. Also, the BOJ is not too concerned about falling oil prices — the bigger reason for disinflation — as long as it does not push those expectations down. "Inflation expectations appear to be rising on the whole from a somewhat longer-term perspective", and "even if prices turn negative, it won't necessarily affect the underlying trend in inflation", Kuroda said in a recent policy statement.

But the gap between target and reality is now widening in a way that could undermine public belief in the BOJ programme. If the BOJ does not act, it could lose credibility both with markets and with a public that needs convincing inflation is here to stay. "Efforts to boost inflation expectations are likely to come under pressure soon," argued Marcel Thieliant, Japan economist at Capital Economics in Singapore. So some analysts expect further easing as early as next month. Others think the BOJ will do nothing more this year. Others again think the central bank will wait for the results of this year's wage negotiations, which should be clear by the summer, to judge whether it is on track to hit 2% inflation.

In his policy statement he cited Paul Volcker's historical success in changing people's mindset and bringing inflation down from 15% in the late 1970s to early 1980s when he was at the head of the Federal Reserve Board in Washington DC. "While Volcker's challenge was to break America out of a self-fulfilling cycle of rising inflation expectations, Japan's task is to break a self-fulfilling cycle of low inflation expectations", said Kuroda. So he seems confident that monetary easing measures by the BOJ are helping the Japanese public shake off its deflationary mindset.

Hence the BOJ's line in public continues to be that it can live with a temporary decline in headline inflation as long as the economy continues to recover and inflation expectations do not decline. But going from deflation to demand-led inflation may well need more than what has so far been put in place by the BOJ. True, corporate profits have never been higher, exports are strong, and even sunset industries such as shipbuilding are making a comeback. All this would help Abe to revive the economy. But only if structural reforms are forcefully implemented can Abenomics' success be ensured.

The first two arrows of Abenomics, comprising expansionary fiscal and monetary policy, have helped Japan make "an initial escape from deflation." The third arrow was announced in June 2014 with the aim to improve the country's prospects by increasing competition, reforming labour markets, and cementing trade partnerships. But so far it has not yet left the quiver.

MARKET DEVELOPMENTS

As we expected the environment has remained strongly in favour of equities. Growth looks set to continue world-wide, though at more moderate rates than in the 2000s. This remains a good equity environment. The Fed is likely to tighten which will mainly hit government bonds prices; once it does the great bond market boom should finally come to an end.

Table 1: Market Developments

	Market Levels Feb 27	Market Levels Mar 27	Prediction for Mar/Apr 2016 Previous Letter	Prediction for Mar/Apr 2016 Current View
Share Indices				
UK (FT 100)	6950	6895	10042	9964
US (S&P 500)	2111	2056	2757	2658
Germany (DAX 30)	11327	11844	15733	16452
Japan (Tokyo New)	1522	1569	2076	2140
Bond Yields (government				
UK	1.73	1.71	2.00	2.00
US	1.98	1.98	2.10	2.10
Germany	0.30	0.22	1.50	1.50
Japan	0.34	0.33	0.70	0.70
UK Index Linked	–0.79	–0.97	0.10	0.10
Exchange Rates				
UK ($ per £)	1.54	1.48	1.56	1.56
UK (trade weighted)	91.4	89.2	82.3	88.6
US (trade weighted)	100.8	102.5	85.5	85.5
Euro per $	0.89	0.92	0.79	0.79
Euro per £	1.37	1.36	1.23	1.23
Japan (Yen per $)	119.4	119.0	98.0	98.0
Short Term Interest Rates (3-month deposits)				
UK	0.56	0.56	1.10	1.10
US	0.26	0.27	0.70	0.70
Euro	0.02	0.01	0.50	0.50
Japan	0.10	0.10	0.70	0.70

Table 2: Prospective Yields [1]

Equities: Contribution to £ yield of:

	Dividend Yield	Real Growth	Inflation	Changing Dividend Yield	Currency	Total
UK	3.40	2.5	2.0	40.00		47.90
US	1.90	3.0	1.6	26.00	–5.11	27.39
Germany	2.60	1.4	1.5	36.00	9.33	50.83
Japan	1.70	1.4	2.0	33.00	13.46	51.56
UK indexed[2]	–0.97		2.4	–5.00		–3.79
Hong Kong[3]	2.60	6.8	1.6	5.00	–5.11	7.89
Malaysia	3.30	5.5	1.6	58.00	–5.11	63.29
Singapore	3.50	4.5	1.6	36.00	–5.11	40.49
India	1.40	8.0	1.6	31.00	–5.11	36.89
Korea	1.10	3.0	1.6	–12.00	–5.11	–11.41
Indonesia	2.20	6.1	1.6	41.00	–5.11	45.79
Taiwan	2.80	3.4	1.6	29.00	–5.11	31.69
Thailand	3.20	4.1	1.6	38.00	–5.11	41.79

Bonds: Contribution to £ yield of:

	Redemption Yield	Changing Nominal Rates	Currency	Total
UK	1.71	–2.90		–1.19
US	1.98	–1.20	–5.11	–4.33
Germany	0.22	–12.80	9.33	–3.25
Japan	0.33	–3.70	13.46	10.09

Deposits: Contribution to £ yield of:

	Deposit Yield	Currency	Total
UK	0.56		0.56
US	0.27	–5.11	–4.85
Euro	0.01	9.33	9.35
Japan	0.10	13.46	13.55

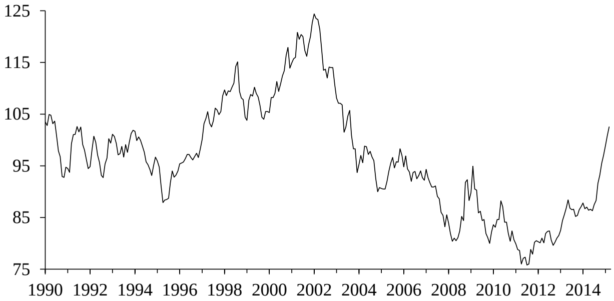
[1] Yields in terms of €s or $s can be computed by adjusting the £-based yields for the expected currency change.
[2] UK index linked bonds All Stocks
[3] Output based on China.

Table 3: Portfolio(%)

	Sterling Based Investor		Dollar Based Investor		Euro Based Investor	
	March Letter	Current View	March Letter	Current View	March 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)	-	-	-	-	-	-

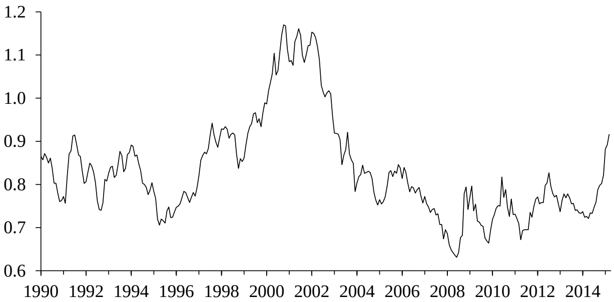
INDICATORS AND MARKET ANALYSIS
FOREIGN EXCHANGE MARKETS

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

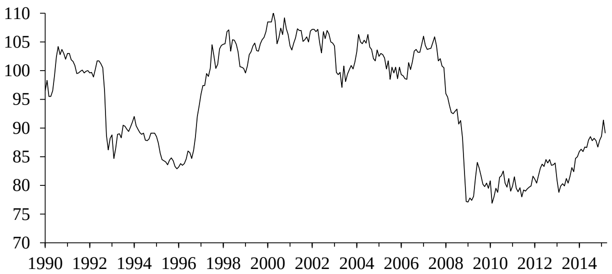


UK: Dollars Per Pound Sterling

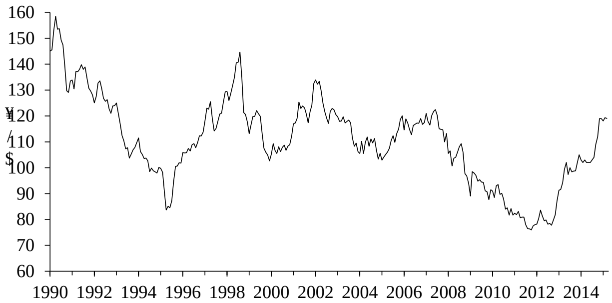
Euro per US dollar



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

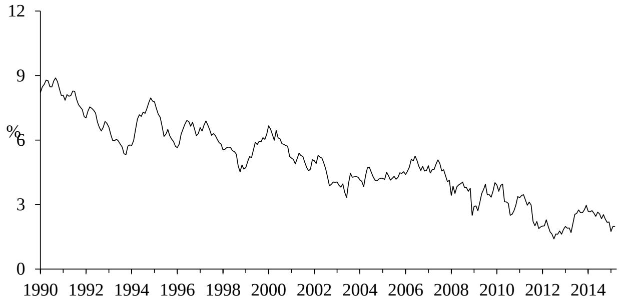


Japan : Yen Per U.S. Dollar

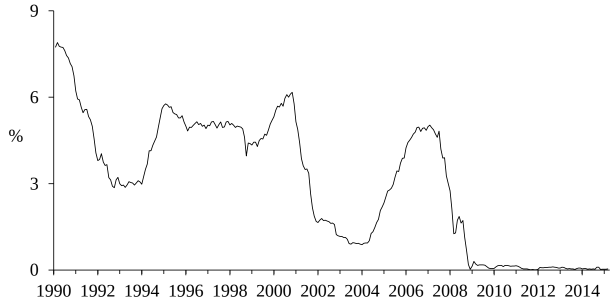


GOVERNMENT BOND MARKETS

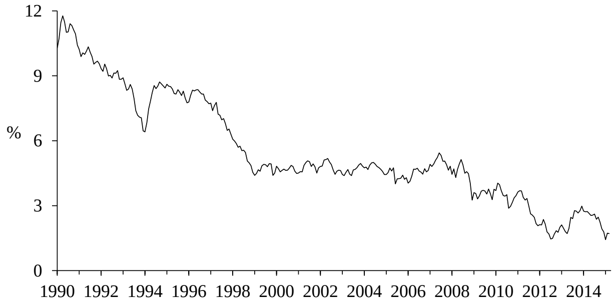
U.S.: Yield on Long-Term Government Bonds



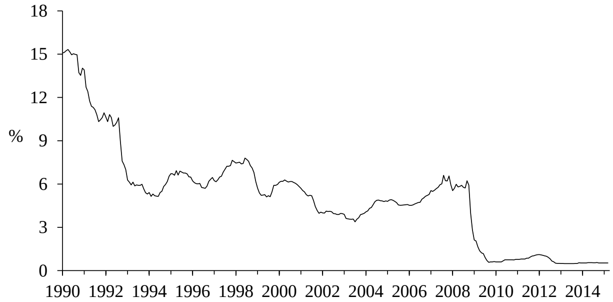
U.S. : 3-Month Treasury Bill



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

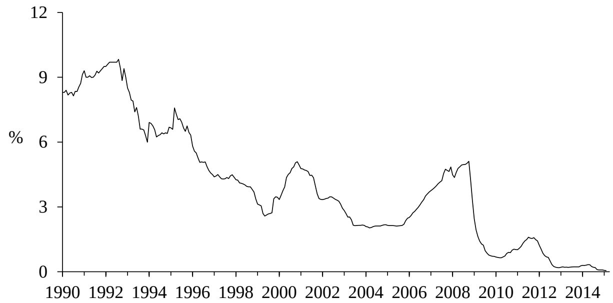


U.K. : 3-Month Interbank Rate

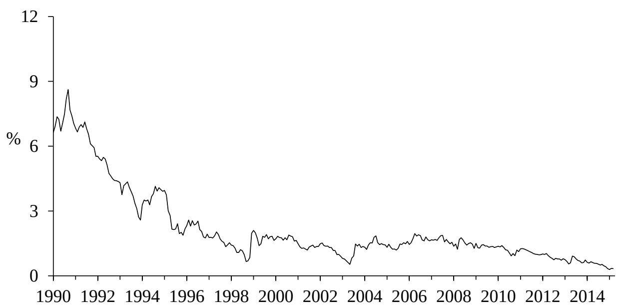


Germany: Yield on Public Authority Bonds

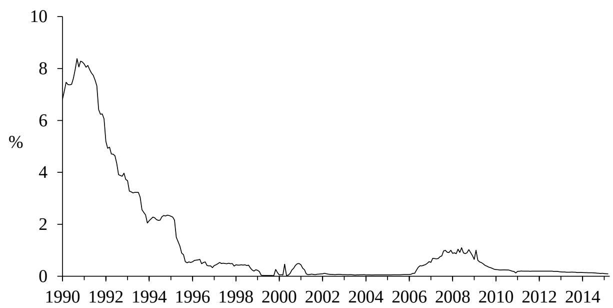
Germany : 3-Month Interbank Deposit Rate



Japan: Yield on Long-Term Government Bonds

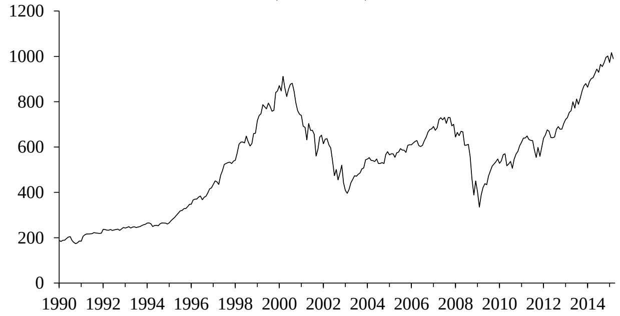


Japan : 3 Month Money Market Rate

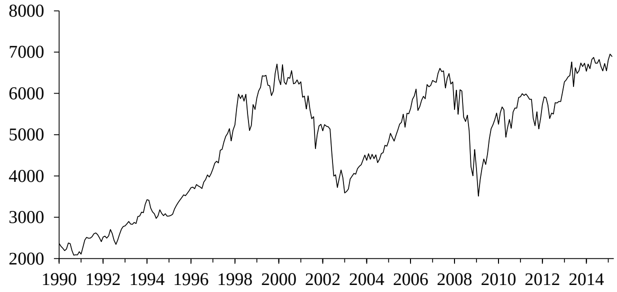


MAJOR EQUITY MARKETS

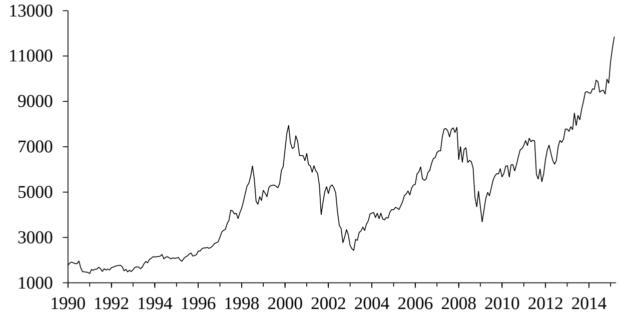
U.S. : S & P 400 Industrial
(1985=100)



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



Germany : DAX 30



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

EMERGING MARKETS

Anupam Rastogi

India

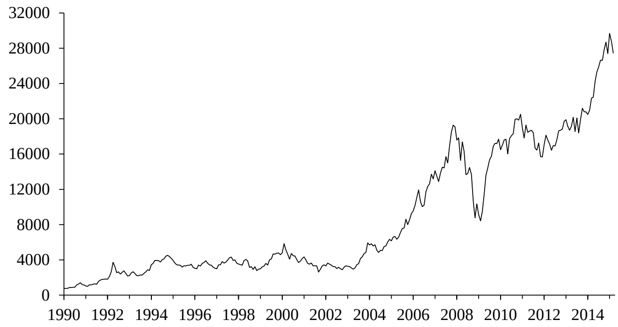
The government of India hopes that gross domestic product will expand between 8.1% and 8.5% in the coming fiscal year, which begins April 1, 2015. The current fiscal year's growth is expected to be 7.4%. For once, the ADB and the IMF also predict growth to be nearly 8% in the calendar year 2015. The forecasts were adjusted in response to the Indian government's recent revision to its methodology for estimating GDP. The positive impetus, according to the international organizations, is provided by the government's continued commitment to lowering its budget deficit while also investing more to upgrade India's roads, railways and power lines. Industrial output grew 2.6% from a year earlier in January,

The Reserve Bank of India did it again and did it in style. It took the market by surprise a second time in less than three months' time by cutting repo rate by 25 basis point. Governor Rajan rationalized it by saying that the pace of disinflation is faster than estimated earlier and inflation is well under control. After this year's two rate cuts, India's key policy interest rate currently stands at 7.5%. With its latest move, the RBI joined a dozen central banks, from Singapore to Switzerland, which have cut rates since January to stimulate economic growth and stave off deflation.

India's central bank governor has brushed aside concerns that an anticipated increase in U.S. interest rates would limit his freedom to act, saying Indian monetary policy would be driven primarily by domestic developments. A tightening of U.S. monetary policy could affect emerging markets because it would offer investors an incentive to ditch riskier assets and buy dollar-denominated securities, which would see yields rise. However, with increasing foreign exchange reserves with controlled current account deficit and government's commitment to keep the fiscal deficit in check, the Reserve Bank of India is well positioned to handle interest rate hike in the US, whenever it comes.

The country's consumer inflation — the measure the RBI uses to set rates — came in at 5.1% in January, higher than the previous month but still well on its way to reaching the RBI's target of 4% by January next year.

India: BSE Sensitive



The Indian government and the Reserve Bank of India have agreed on a monetary policy framework that will make managing inflation the key determinant in the central bank's policy decisions. As part of the framework, the RBI will aim to lower inflation to 4%, with a band of 2% on either side, by the financial year ending March 2017 and keep it around that level.

Foreign investments have been rising. India received $25.53 billion of foreign direct investment in the 10 months to January, according to the trade ministry. That is about 36% higher than the $18.75 billion investment received during the same period the previous year.

The government of India's agenda is to lay the groundwork for an expansion of manufacturing in India at a time when growth in China's booming economy is slowing and wages there are rising. The long-delayed act allows foreign investors to increase stakes in local insurers from 26% to 49%, boosting the economic reform drive of Prime Minister Narendra Modi. Increasing the FDI cap on insurance companies certainly comes as a relief to the sector. However, with the revision in FDI norms, the market is expecting these entities to unlock value in the subsidiaries very soon.

	13-14	**14-15**	**15-16**	**16-17**	**17-18**
GDP (%p.a.)	6.9	7.4	8.0	8.0	8.0
WPI (%p.a.)	7.0	6.0	5.0	4.0	4.0
Current A/c(US$ bill.)	-50.0	-34.0	-30.0	-32.0	-35.0
Rs./$(nom.)	60.0	62.0	63.5	64.0	65.0

China

China has set an annual growth target of 7% for 2015, pointing to the efforts by the Chinese leadership to remake the economy dependent more on consumption and private entrepreneurship. Policies unveiled at the annual session of China’s legislature in March called for maintaining a moderately high rate of growth — 7% — and outlined further deficit spending to support the goal. Growth last year was 7.4%, the slowest pace in nearly a quarter-century. The International Monetary Fund has forecast 6.8% growth for 2015. China hopes that it will be the No. 2 engine of growth for the global economy this year after the U.S.

China’s government is trying to keep the slowing economy from decelerating too quickly. A key challenge for the government is, working through a housing glut, industrial overcapacity and high levels of corporate and local government debt.

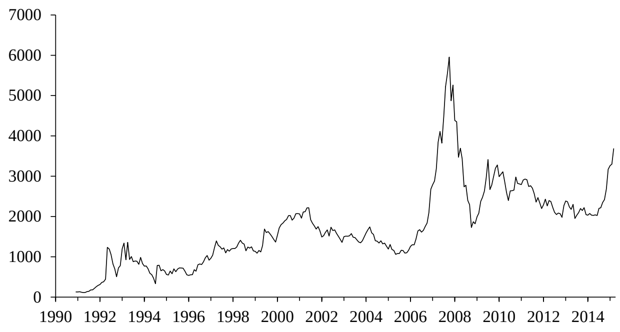
China’s central bank has taken a fresh move to lower borrowing costs for businesses in a weakening economy, just days after it cut policy interest rates for the second time in less than four months. The central bank cut the overnight interest rate to 4.5% from 5% previously and the seven-day rate to 5.5% from 7%. The decision came after the PBOC cut its benchmark lending and deposit interest rates by 0.25 percentage points, effective March 1, 2015. Given the weak state of the economy, another policy rate cut by the PBOC in the second quarter of this year cannot be ruled out.

China’s consumer-price index rose 1.4% in February mainly due to higher food prices over the Lunar New Year holiday in February. China’s deflation risks remain and inflation may be less than one percent in 2015.

Exports surged 48.3% while imports fell 20.5% in February. The February trade figures were distorted by a number of factors, including comparisons with a weak tally a year ago as authorities cracked down on export fraud, as well as the timing of the Lunar New Year holiday. The holiday began at the end of January last year but in the middle of February this year. Meanwhile, imports slumped 20.5% from a year earlier in February, surpassing the 19.9% fall in January and exceeding market expectations of a 10% decrease. The February slide was the fourth consecutive month of lower year-over-year imports. The import decline was partly due to the sharp fall in prices for key commodities such as oil and metals. Crude-oil imports fell 46% in value but were up 11% in volume.

One of the challenges faced by China is sluggish profits in 2014 of banks as the cooling Chinese economy took its toll on profitability and bad loans piled up, underscoring concerns over the health of the nation’s banking sector.

China: SSE Composite Index



Faced with growing numbers of bad loans, China’s biggest banks are ramping up efforts to get rid of them.

China Investment Corporation (CIC), China’s sovereign-wealth fund, is stepping up direct investments in long-term global assets, with a particular focus on the U.S. in a vote of confidence in the recovery in the world’s largest economy. CIC has about $220 billion in overseas assets. The fund has been diversifying foreign investments away from stocks and bonds and into assets including infrastructure and property to fit its long-term investment horizon. CIC executives have said the goal is to have a roughly even split between financial products traded in public markets, such as stocks and bonds, and long-term investments in the fund’s global portfolio. As of the end of 2013, the most recent data available, equities and fixed-income holdings represented 57.4% of CIC’s global assets, followed by 28.2% in long-term assets.

The Chinese yuan has strengthened in the past couple of weeks, and is now just about where it started the year versus the dollar. That is despite a darkening growth outlook and expectations for increasingly loose monetary policy, factors that normally should exert downward pressure on a currency. The sudden gains serve as a reminder that Beijing still keeps a firm grip on the currency and won’t allow heavy losses or one-way speculation.

China’s Central Bank Governor Zhou Xiaochuan is keen to see the yuan’s inclusion in the SDR, which serves as an accounting currency and means to move around capital among IMF members. Since 2010, China is trying the yuan’s inclusion. Getting in would be a milestone in China’s effort to position its currency as an eventual rival to the dollar in international finance. At present, the SDR has the dollar, euro, yen and pound only. The terms of inclusion state that an SDR currency must be “freely usable.” That doesn’t mean China has to fully liberalize its capital account, or even stop intervening in the level of its currency.

China's plans for a new development bank to fund infrastructure in Asia is taking shape, notwithstanding the opposition coming from Japan and the US. Most of the important European nations have signed up in the past few weeks despite U.S. opposition. Many other Asian countries are on board except Japan. Japan's reticence, in part, shows its reluctance to cede influence to China over infrastructure development in the region.

	13	**14**	**15**	**16**	**17**
GDP (%p.a.)	7.7	7.4	6.8	6.5	6.0
Inflation (%p.a.)	3.5	2.0	1.0	1.5	2.0
Trade Balance(US$ bill.)	260	382	350	320	300
Rmb/$(nom.)	6.2	6.2	6.3	6.3	6.2

South Korea

South Korea's economy expanded 3.3% in 2014, but policy makers in Seoul fret that Korean exports could lose steam in increasingly volatile overseas markets. The Bank of Korea has revised its growth forecast for this year down from 3.9% to 3.4%. We have maintained growth of 3% for South Korea in 2015. The BoK's monthly consumer confidence survey has shown results this year significantly lower than for most of last year.

Consumer price inflation fell to 0.5% last month, a 16-year low and below the central bank's target range of 2.5 to 3.5%. The Bank of Korea has eased monetary policy to help in pushing growth. The central bank surprised markets by cutting its base rate a quarter of a percentage point to a record low of 1.75%, following a rate cut by other central banks of the region. It may well cut again soon. One goal of the rate cuts is to encourage consumers to spend more by lowering mortgage servicing costs. But South Koreans are also holding back on outlays because of concerns about the economic outlook.

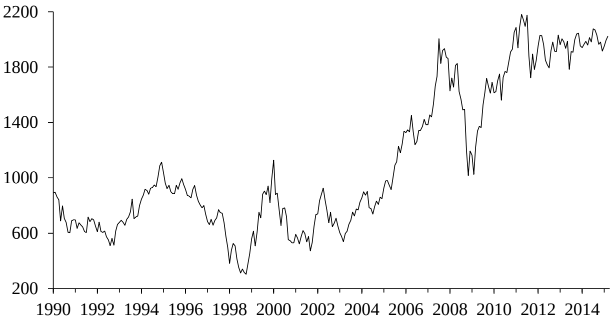
The surprise rate cut would help to arrest the won's gains as other major currencies are depressed by central bank's cutting rates.

Exports declined 3.4% from a year earlier to $41.46 billion, following a revised 0.7% drop in January, according to provisional data of the trade ministry. Imports also plunged 19.6% from a year earlier to $33.80 billion in February, following an 11% decrease in January. The trade surplus widened to $7.66 billion in February from the previous month's revised $5.40 billion.

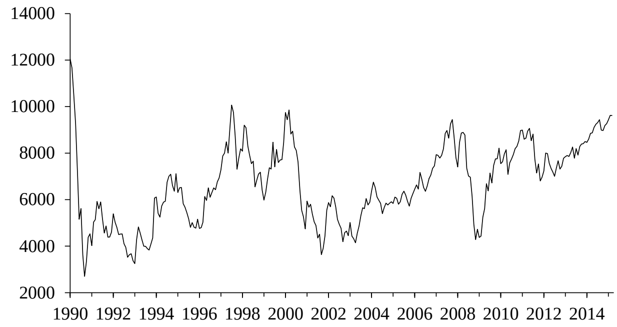
The Korean won weakened after the central bank's cut in interest rate, hitting a one-and-a-half year low against the U.S. dollar, providing some relief to Korean exporters.

South Korea has become member of the Asian Infrastructure Investment Bank despite its strong relations with the US. South Korea expects to take 4–5% stake in the China-led AIIB.

Korea: Composite Index



Taiwan: Weighted TAIEX Price Index



	13	**14**	**15**	**16**	**17**
GDP (%p.a.)	3.0	3.3	3.3	3.0	3.0
Inflation (%p.a.)	1.3	2.0	2.0	2.0	2.1
Current A/c(US$ bill.)	71.0	80.0	80.0	84.0	88.0
Won/$(nom.)	1100	1080	1120	1100	1100

Taiwan

Taiwan's economy is expected to expand by 3.50% for the first quarter of 2015 and by 3.78% for the entire year as growth is expected to advance further in the coming quarters. In 2014, the economy expanded 3.7%.

Taiwan's consumer price index is expected to rise only 0.26% in 2015, compared with a 1.20% rise in 2014, largely because of lower fuel and electricity costs. Taiwan's consumer price inflation rate has been trending downward since September last year and fell to minus 0.19% in February for an average of minus 0.56% for the first two months.

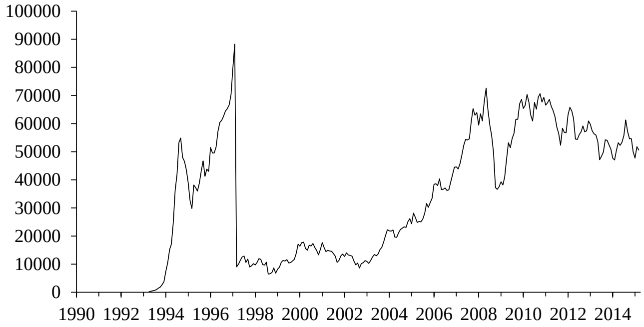
Taiwan's central bank maintained its benchmark discount rate at 1.875%, as expected, saying the current rate will help maintain price and financial stability while fostering economic growth at a time of continued uncertainties surrounding the global economic recovery. The bank has maintained its rates since June 2011, Taiwan's export orders in February fell to the lowest level in two years, but export orders grew 8.1% year-on-year in January. Trade is most likely to pick up in coming months.

Unlike most currencies, the Taiwan dollar has firmed slightly this year against the U.S. dollar, trading at 31.2 to the USD today, up 1.5% since the start of the year.

	13	14	15	16	17
GDP (%p.a.)	2.1	3.7	3.8	3.3	3.3
Inflation (%p.a.)	1.2	1.5	1.5	1.6	1.6
Current A/c(US$ bill.)	50.6	57.4	60.0	64.0	68.0
NT$/$(nom.)	30.0	31.0	32.0	32.5	33.0

Brazil

Brazil: Bovespa



Brazil's economy is facing terrible headwinds. Thanks to the change in the methodology whereby activities such as investment in research and development are included in GDP, the country's gross domestic product grew 0.1% in 2014 from 2013. However, nothing has changed in terms of the structural weakness of Brazil's economy. The central bank estimates that gross domestic product will contract by 0.5% and inflation 7.9% in 2015.

Ms. Rousseff's government is now trying to cut its budget deficit via tax increases and spending cuts. Most of the measures need Congress approval and the Congress is not obliging the government.

The weak economy, and the Petrobras scandal, have taken a heavy toll on the president's approval rating, which dropped to just 13% in a recent poll, the lowest for a Brazil president since 1999. Roughly one million people who protested in the march on March 15th called for President Rousseff's impeachment, amid revelations of alleged graft at oil giant Petróleo Brasileiro SA that largely occurred while she chaired the company's board of directors from 2003 to 2010.

Brazil's jobless rate rose to 5.9% in February, the highest in almost two years. Besides this, Brazilian consumer confidence in March was its weakest since this indicator started in 2005. Brazil's consumer prices remain under pressure mainly on an increase in transportation prices, which has been fuelled by higher public-transport fares in certain cities and increases in gasoline prices. Depreciation of the Brazilian real which is trading at about 3.2 to the dollar has further pushed inflation. The 12-month inflation rate rose to 7.9% in mid-March, well above the 6.5% ceiling of the central bank's target range.

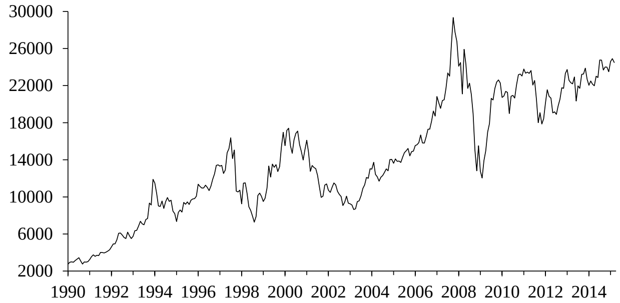
The central bank raised its benchmark rate to 12.75% at its monetary-policy meeting in the beginning of March, the highest level since 2009, as it struggles to get price increases under control amid sluggish economic growth and deepening political turmoil. The central bank's next monetary-policy committee meeting in April may see another 25 basis point increase in the Selic rate. But, the ratings company Standard & Poor's has left Brazil's credit rating in investment grade territory, with a stable outlook. The S&P cited Mr. Levy's economic plan for keeping Brazil's rating unchanged and said it expects the president and the Congress to continue to support it.

The Brazilian real reached its weakest point against the dollar in 12 years in mid-March. The real traded at 3.2622 to the dollar but soon recovered to 3.15 to the dollar. The Ibo Vespa benchmark stock index is still holding due to the Levy factor. Investors believe that the Chicago-trained finance minister will be able to pull off an austerity programme to restore Brazil's fiscal balance against the odds. As he is in charge Petrobras as well he will sort out its accounts in time for a deadline in June.

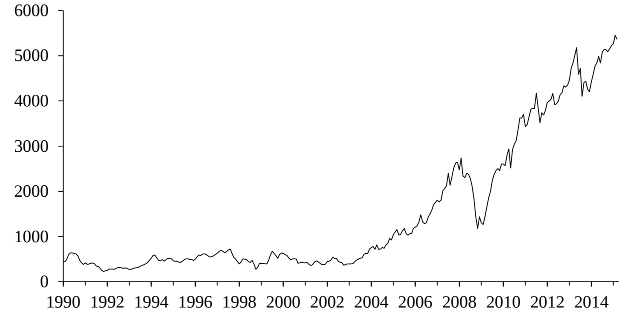
	13	14	15	16	17
GDP (%p.a.)	2.5	0.1	-0.5	0.5	1.0
Inflation (%p.a.)	5.9	6.5	7.9	6.5	6.0
Current A/c(US$ bill.)	-75.0	-70.0	-70.0	-70.0	-80.0
Real/$(nom.)	2.3	2.4	2.8	2.8	2.8

Other Emerging Markets

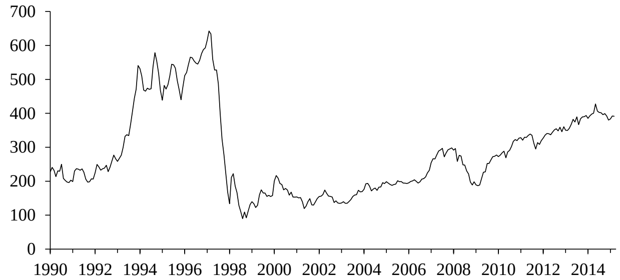
Hong Kong: FT-Actuaries



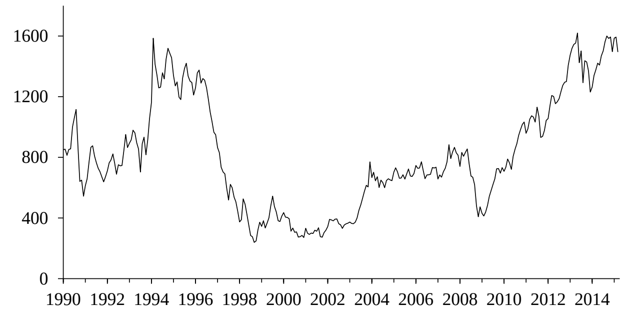
Indonesia: Jakarta Composite



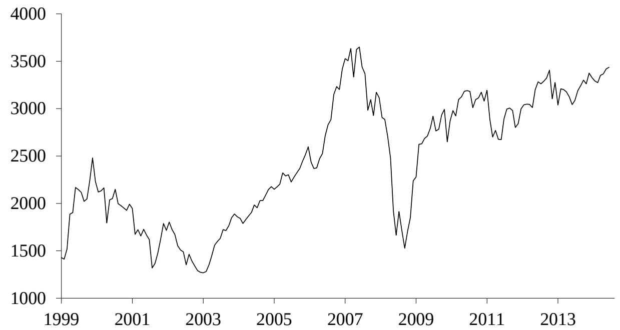
Malaysia: FT-Actuaries (US$ Index)



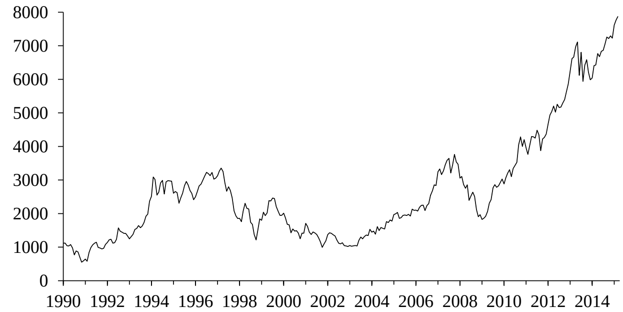
Thailand: Composite Index



Singapore: Straits Times Index

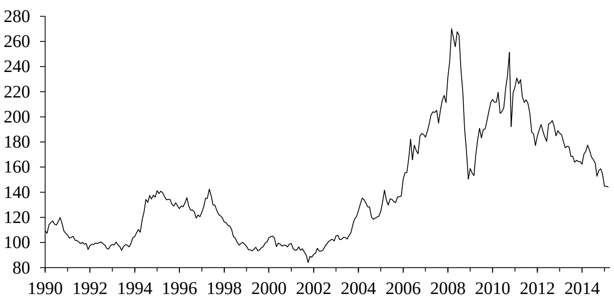


Philippines: Manila Composite

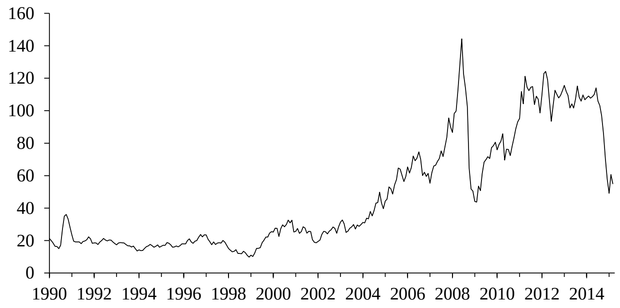


COMMODITY MARKETS

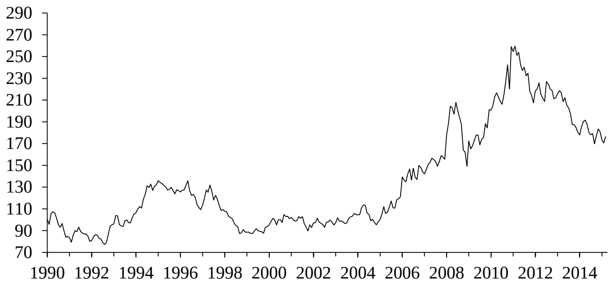
Commodity Price Index (Dollar)
(Economist, 2000=100)



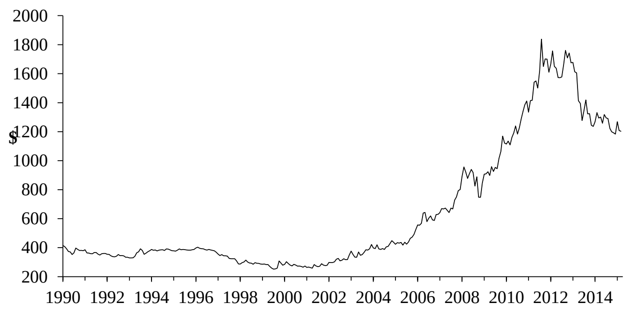
Oil Price: North Sea Brent (in Dollars)



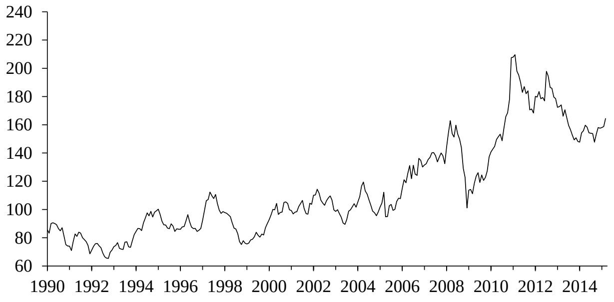
Commodity Price Index (Sterling)
(Economist, 2000=100)



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]
2013	1.9	1.3	0.6	81.5	85.4	-1.3	3.1	-0.4
2014	1.7	1.9	0.6	87.7	92.7	-1.0	2.5	0.1
2015	1.4	2.2	1.0	90.3	95.4	-0.7	2.3	0.3
2016	1.7	2.5	1.6	90.4	95.6	-0.1	2.4	0.6
2017	1.7	2.5	2.0	90.4	95.7	0.0	2.5	0.5
2018	2.0	2.5	2.1	90.1	95.7	0.1	2.7	0.5
2013:1	1.9	1.0	0.6	80.4	84.0	-1.1	3.3	-0.8
2013:2	1.7	0.9	0.5	80.6	84.1	-1.5	3.1	-0.9
2013:3	2.1	1.5	0.5	81.3	85.1	-1.4	3.2	-0.2
2013:4	1.9	1.7	0.5	83.6	88.6	-1.1	2.7	0.1
2014:1	1.7	1.8	0.6	85.6	90.4	-1.1	2.7	0.3
2014:2	1.7	1.9	0.6	86.9	91.3	-1.2	2.6	0.4
2014:3	1.7	1.9	0.6	88.0	93.1	-0.8	2.5	0.5
2014:4	1.5	1.9	0.6	90.3	95.8	-1.0	2.3	0.4
2015:1	1.4	2.2	0.7	90.2	95.2	-0.9	2.3	0.7
2015:2	1.4	2.1	0.9	90.3	95.2	-0.8	2.2	0.5
2015:3	1.4	2.2	1.1	90.7	95.8	-0.5	2.2	0.6
2015:4	1.5	2.3	1.2	90.2	95.6	-0.5	2.3	0.6

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)
2013	239.8	1.1	4.2	1.42	132.7
2014	242.3	1.0	3.0	1.05	131.9
2015	247.0	1.9	2.6	0.90	132.6
2016	255.3	3.4	2.4	0.83	134.8
2017	264.9	3.8	2.2	0.77	137.6
2018	277.2	4.7	2.0	0.73	141.3
2013:1	236.4	0.7	4.6	1.54	131.8
2013:2	242.0	1.9	4.4	1.49	134.5
2013:3	240.0	0.7	4.1	1.39	132.6
2013:4	240.8	1.1	3.7	1.27	132.1
2014:1	241.0	1.9	3.4	1.17	132.1
2014:2	241.8	-0.1	3.1	1.08	132.2
2014:3	242.6	1.1	2.8	0.98	131.7
2014:4	243.8	1.2	2.8	0.95	131.7
2015:1	244.4	1.4	2.7	0.93	132.1
2015:2	245.6	1.6	2.6	0.91	132.4
2015:3	247.8	2.2	2.5	0.89	132.8
2015:4	250.2	2.6	2.5	0.87	133.1

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
2013	149.7	716792.3	422942.6	280112.3	186839.5	-43986.8	129115.4
2014	153.5	735082.7	424682.2	303904.9	189743.4	-47874.8	135373.4
2015	157.8	755636.4	429872.6	315514.3	193150.9	-42988.5	139912.9
2016	161.7	774498.7	439815.9	323556.4	197878	-42985.8	143766.2
2017	165.8	793916.4	450535.5	332193.9	201835.6	-42994.6	147654.4
2018	169.9	813828.5	461630.8	340980.7	205872.3	-43013.8	151641.9
2013/12	1.7		0.8	6.9	-0.8		6.5
2014/13	2.6		0.4	9.0	1.6		5.2
2015/14	2.8		1.2	3.8	1.8		3.5
2016/15	2.5		2.3	2.6	2.5		2.8
2017/16	2.5		2.4	2.7	2.0		2.7
2018/17	2.5		2.5	2.6	2.0		2.7
2013:1	148.3	177519.5	105980.9	63263.4	48156.3	-9136.5	30744.6
2013:2	149.2	178660.4	105506.8	65944.1	45724.2	-8941.9	29572.8
2013:3	150.3	179940.8	105672.5	73909.9	46393.6	-13073.1	32962.1
2013:4	150.9	180671.6	105782.4	76994.9	46565.5	-12835.3	35835.9
2014:1	151.8	181776.6	105866.5	74932.1	48251.1	-12765.7	34507.4
2014:2	153.1	183257.9	106231.6	73897.9	46774.2	-11870.1	31775.8
2014:3	154.2	184619.2	106439.4	77309.5	47552.7	-12488.8	34193.7
2014:4	154.9	185429.0	106144.7	77765.3	47165.3	-10750.2	34896.5
2015:1	155.8	186559.3	106671.4	75321.1	49960.4	-10752.3	34641.4
2015:2	156.9	187849.0	107200.8	78870.5	47084.9	-10749.7	34557.4
2015:3	158.9	190255.7	107732.8	80635.2	47855.5	-10744.9	35222.9
2015:4	159.5	190972.3	108267.5	80687.6	48250.2	-10741.7	35491.2

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)
2013	5.9	1549.7	91.1	47.1	-65.9
2014	5.7	1613.9	91.5	52.2	-80.9
2015	4.5	1685.8	75.8	55.9	-72.0
2016	3.2	1758.3	56.5	60.5	-72.3
2017	1.3	1835.2	24.3	63.2	-72.7
2018	0.2	1919.5	3.7	64.9	-73.3
2013:1	3.5	373.6	13.0	11.9	-14.1
2013:2	8.1	374.9	30.5	11.2	-8.4
2013:3	5.0	385.5	19.4	11.5	-22.2
2013:4	8.1	394.8	32.1	11.9	-21.1
2014:1	2.3	394.6	9.1	12.4	-19.3
2014:2	8.0	393.5	31.6	12.8	-20.9
2014:3	5.1	403.1	20.6	13.0	-23.2
2014:4	7.4	407.9	30.0	13.1	-17.4
2015:1	2.3	409.4	9.2	13.3	-15.7
2015:2	6.8	412.5	28.1	13.6	-18.9
2015:3	5.0	421.0	20.9	13.9	-19.9
2015:4	5.4	425.8	22.9	14.2	-17.5

1 GDP at market prices (Financial Year)

WORLD FORECAST DETAIL

Growth Of Real GNP

	2010	2011	2012	2013	2014	2015
U.S.A.	2.5	1.6	2.3	2.2	2.3	3.0
U.K.	1.9	1.6	0.7	1.7	2.6	2.8
Japan	4.7	–0.4	1.7	1.6	0.3	1.2
Germany	4.1	3.6	0.4	0.1	1.4	1.3
France	1.9	2.1	0.4	0.4	0.4	0.8
Italy	1.7	0.6	–2.3	–1.9	–0.3	0.4

Real Short-Term Interest Rates

	2010	2011	2012	2013	2014	2015
U.S.A.	–3.0	–2.0	–1.4	–1.6	–1.2	–0.8
U.K.	–3.6	–2.4	–1.1	–1.3	–1.0	–0.7
Japan	0.5	0.2	–0.2	–2.6	–1.3	–1.3
Germany	–1.3	–0.6	–0.9	–0.8	–1.0	–1.4
France	–1.3	–0.6	–0.3	–0.4	–0.4	–0.9
Italy	–2.0	–1.6	–0.6	–0.2	–0.2	–0.9

Real Long-Term Interest Rates

	2010	2011	2012	2013	2014	2015
U.S.A.	1.2	0.3	0.2	0.4	0.7	1.5
U.K.	0.3	0.2	–0.8	–0.4	0.1	0.3
Japan	0.3	–0.2	–0.7	–1.2	–1.3	–1.1
Germany	1.2	1.2	0.2	0.1	–0.5	–0.7
France	1.6	1.7	0.7	0.5	–0.2	–0.5
Italy	1.2	1.5	0.7	0.5	–0.2	–0.5

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

	2010	2011	2012	2013	2014	2015
U.S.A.	84.0	79.8	81.6	82.1	83.0	83.2
U.K.	88.6	88.7	92.4	90.8	98.6	101.4
Japan	79.5	80.6	79.6	63.5	61.1	60.7
Germany	101.3	100.1	96.7	99.0	100.5	100.2
France	103.5	102.9	99.5	100.7	101.7	101.4
Italy	107.4	107.2	105.2	106.9	107.8	107.0

[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.

Growth Of Consumer Prices

	2010	2011	2012	2013	2014	2015
U.S.A.	1.6	3.1	2.1	1.5	1.7	1.3
U.K.	4.5	3.5	2.1	1.9	1.7	1.4
Japan	–0.7	–0.3	0.0	0.4	2.8	1.4
Germany	1.1	2.1	2.0	1.5	1.0	1.2
France	1.5	2.1	2.0	0.9	0.6	0.6
Italy	1.5	2.8	3.0	1.2	0.2	0.4

Nominal Short-Term Interest Rates

	2010	2011	2012	2013	2014	2015
U.S.A.	0.1	0.1	0.1	0.1	0.1	0.6
U.K.	0.7	0.9	0.9	0.6	0.6	1.0
Japan	0.2	0.2	0.2	0.2	0.1	0.2
Germany	0.8	1.4	0.6	0.2	0.2	0.1
France	0.8	1.4	0.6	0.2	0.2	0.1
Italy	0.8	1.4	0.6	0.2	0.2	0.1

Nominal Long-Term Interest Rates

	2010	2011	2012	2013	2014	2015
U.S.A.	3.1	1.9	1.8	2.1	2.5	3.4
U.K.	2.4	2.0	0.9	1.3	1.9	2.2
Japan	1.2	1.0	0.9	0.7	0.5	0.8
Germany	2.8	2.7	1.6	1.6	1.2	1.2
France	2.8	2.7	1.6	1.6	1.2	1.2
Italy	2.8	2.7	1.6	1.6	1.2	1.2

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

	2010	2011	2012	2013	2014	2015
U.S.A.[1]	83.73	78.08	80.90	85.50	88.60	89.00
U.K.	1.58	1.61	1.59	1.55	1.56	1.55
Japan	87.48	79.36	80.51	98.00	104.50	104.00
Eurozone	0.75	0.71	0.78	0.79	0.74	0.75

[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