LIVERPOOL INVESTMENT LETTER

January 2014

Cardiff Business School
Cardiff University

Julian Hodge Institute of Applied Macroeconomics

LIVERPOOL RESEARCH GROUP IN MACROECONOMICS

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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

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GROWTH FINALLY SPRINGS TO LIFE

Credit has at last started to flow again. So far it is just the mortgage market but confidence is likely to spread to business investment soon, which so far has been held back by uncertainty and shortage of credit. The politics of growth has taken hold, with an election soon and a new governor of the Bank who is a much-needed pragmatic realist. For the new banking era we need a new philosophy of regulation that is concerned, administered by Bank experts, and harks back to an earlier age of competition and self-regulation. We have to update the vision of practical economists like Bagehot.

At present there are still huge risks from over-regulation. The naïve politicised enthusiasm of the regulators has interacted with fears of the bankers to shrink bank balance sheets sharply. This must stop. Nevertheless it is clear from the new Governor's statements that the 'Taliban tendency' has been put to flight within the Bank. The need is now for monetary policy to take over the heavy counter-cyclical regulation of credit conditions; money supply and credit growth must be paid attention to again.

Looking at the outlook against this background it is at last possible to be reasonably optimistic. We may now start to see credit flowing to business and SMEs in particular, as the banks respond to the greater certainty in the environment. Large businesses are flush with cash and should now start to look at investment plans for the growth ahead. Small firms may do their necessary cheeky work of snatching victory from in front of their lethargic paws. Entrepreneurial Britain may be waking up again. With world commodity prices falling and oil prices steady under the impact of shale oil and gas, reflecting the slowing of the emerging countries as well as new technology and discovery, the background for some growth in real disposable income is there too. It has been growing slowly; it should gather speed, as real wages start to pick up with a tightening labour market. The stage is also set for some tightening of monetary policy once credit growth picks up; interest rates should rise and QE start to be reversed.

Table 1: Summary of Forecast

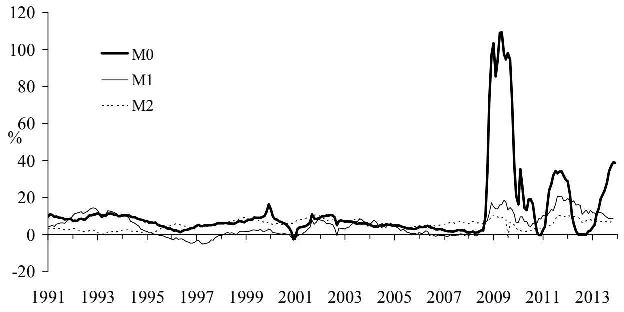
	2010	2011	2012	2013	2014	2015	2016
GDP Growth[1]	1.7	1.1	0.2	1.4	2.6	2.4	2.6
Inflation CPI	3.3	4.5	2.7	2.4	2.5	2.2	2.0
RPIX	4.8	5.3	3.2	3.2	3.1	2.8	2.7
Unemployment (Mill.)							
Ann. Avg.[2]	1.5	1.5	1.6	1.5	1.3	1.3	1.2
4th Qtr.	1.5	1.6	1.6	1.4	1.3	1.3	1.1
Exchange Rate[3]	80.4	80.0	83.1	82.6	83.0	82.3	82.5
3 Month Interest Rate	0.7	0.9	0.9	0.6	1.8	2.1	2.2
5 Year Interest Rate	2.4	2.0	0.9	1.2	1.6	2.10	2.3
Current Balance (£bn)	−40.0	−22.5	−59.2	−60.7	−62.9	−63.5	−62.0
PSBR (£bn)	139.6	118.5	115.0	112.3	109.4	94.6	84.5

[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)

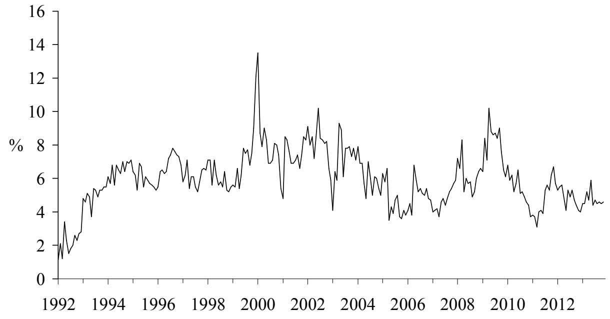
It turns out now that growth in 2013 will probably be revised up to 2%, which also happens to be the forecast we made a year ago. Essentially we did not believe the ONS' figures then and expected a big upward revision of the 'recession' data. This has transpired and will probably continue. It is astonishing that the ONS has no automatic mechanism for anticipating such revisions which have occurred regularly after recessions — the basic reason being that in bad times business switches to cheaper newer channels far more rapidly than normal. These channels are under-sampled and given too low a weight in the total relative to the older channels.

Our forecast for 2014 is for 2.6%. However, it may well be that once revisions to past data are allowed for this too will be conservative.

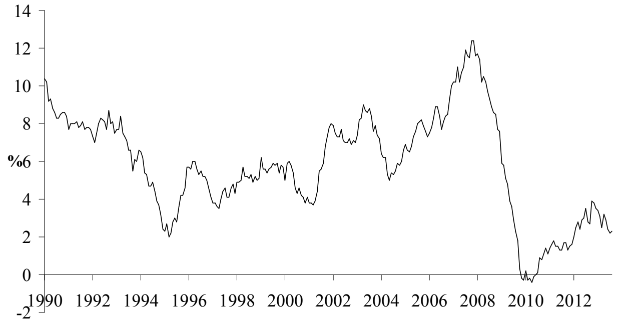
U.S.: Growth in Monetary Aggregates (Yr - on - Yr)



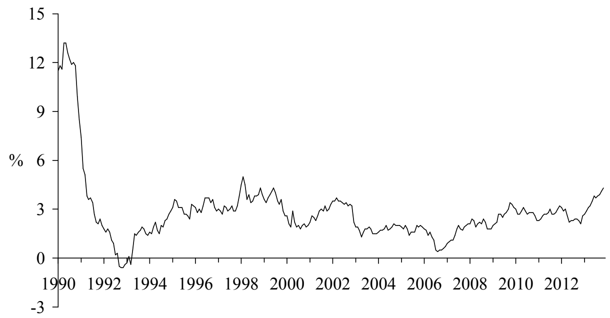
UK: Notes and Coins in Circulation Growth



Eurozone M3 Growth



Japan: Growth of M2+CD's



FOCUS ON JAPAN

Francesco Perugini

GDP Growing But Outlook Uncertain

There is still some positive news coming out of Japan. First of all, on growth, the latest (second) official GDP release on November 14 showed that Q3 was a fourth consecutive quarter of growth: the Japanese economy expanded by a 0.5% in the three months through September, backed by large-scale public investment, while the second quarter was revised upwards to a 0.3%.

Looking at demand components, corporate capital spending, which Abe's Cabinet views as key to economic recovery, was flat from the previous quarter, downwardly revised from the 0.2% rise reported in the preliminary data. Private residential investment rose 2.7%, thanks to ultra-low interest rates and an upswing in consumer sentiment, the government said. Also, private consumption, accounting for around 60% of GDP, was slightly upgraded to 0.2% growth from a 0.1% climb. Exports fell 0.6% and imports rose 2.2%, the same as in the initial report. Imports have been rising as demand for natural gas and oil has been growing from utilities for fossil fuel-based power generation as an alternative to nuclear power: this stems from the nationwide reactor shutdown since the Fukushima nuclear crisis. Japan now depends on imports for more than 90% of its energy needs.

Public investment, meanwhile, jumped 6.5%, unchanged from the initial report, on the back of massive fiscal spending, one of the three arrows of the "Abenomics" policy mix along with drastic monetary easing and an economic growth strategy aimed at invigorating private-sector investment. "While consumer spending and business investment slowed and exports fell, public investment bolstered the economy," Koya Miyamae, senior economist of SMBC Nikko Securities Inc., said. "As the effectiveness of the first arrow (monetary policy) has been waning, the economic growth has depended on the second arrow (fiscal policy)".

There are also good signs regarding business sentiment. The closely-watched Tankan survey of the Bank of Japan (BOJ) is showing that sentiment among big manufacturers rose to its highest level in six years in the three months to December — the headline index of sentiment rose to +16, up 4 points from the September quarter and compared with analyst expectations (in a Reuters poll) of +15. Sentiment among big firms in the services sector also improved, with the big non-manufacturers index rising 6 points to +20 in the three months to December, above forecasts of +16.

Good news has also come in the fight against deflation. A Reuters poll showed that consumer price inflation hit a new five-year high in November of 1.1% on a year earlier — this marks the highest since 1.9% in October 2008. Moreover, household spending rose at the fastest annual pace in eight months and, according to the poll, job availability rose to a new six-year high, showing that firm consumer spending and an improving labour market are contributing to Japan's escape from deflation.

Economics Minister Akira Amari expressed optimism about the future, citing forecasts from private-sector economists pointing to an uptick in GDP in the coming quarters because of a rush in demand ahead of the consumption tax hike next April. However, international observers are more sceptical. For instance, Ryutaro Kono, chief economist of BNP Paribas Securities, warned that the trend may not last long. "Growth is continuing even while inflation is on the rise, but the robust growth is due to the additional fiscal measures," Kono said. "This will continue to support growth for a while, but we may see a slowdown in late 2014 after this support runs out, unless further fiscal measures are introduced and the yen depreciates further."

Sentiment among Japanese corporates is also cautious. The latest Tankan survey showed that big firms in the manufacturing and non-manufacturing sectors expect business conditions to worsen slightly in the three months to March.

Most importantly, economists believe that the consumption tax hike in April to 8% may weigh on consumer spending and investment, in turn dampening domestic demand. The administration of Shinzo Abe has pledged to prevent the tax hike from hurting the economy by steadily implementing a ¥5.5 trillion economic stimulus package and a ¥1 trillion in tax cuts to boost investment and encourage companies to raise wages. However, the package, which has the central government spending more than it is due to receive in revenue from the consumption tax hike, shows that the Japanese economy has yet to enter a self-sustained cycle built on private-sector demand and investment. In other words, it is still too early to say if Abenomics, the government's strategy, will be successful. Basically, up to now it has been built on fiscal and monetary stimulus as opposed to new supply-side sources of growth; we are waiting for this 'third arrow' to be convincingly launched.

MARKET DEVELOPMENTS

Bond yields have now risen markedly and with inflation prospects still thought to be low and stable by markets, expected real yields have moved firmly into positive territory at last. Nevertheless growth is now set firm in our forecasts and our main concern is that central banks will leave money tightening too late in this cycle, having been so 'spooked' by unemployment. Central bank language has become extraordinarily doveish, stressing the need to keep rates low until unemployment is well down. While the Fed is talking about 'tapering', its reluctance to upset the equity market is palpable; hence it continues to add massively to bank liquidity — 'tapering' is merely a lowering of the rate at which liquidity is added. When the authorities are so unanimous that the main danger is unemployment it is right to be nervous about inflation.

This therefore remains an environment in which equities both offer good returns and also a hedge against an unpleasant unintended recurrence of inflation. So we are keeping to our current stance of holding almost all the portfolio in equities.

Table 1: Market Developments

	Market Levels		Prediction for Dec/Jan 2014	
	Nov 29	Jan 6	Previous Letter	Current View
Share Indices				
UK (FT 100)	6651	6731	9690	10029
US (S&P 500)	1806	1827	2290	2535
Germany (DAX 30)	9405	9428	12650	13435
Japan (Tokyo New)	1259	1292	1760	1804
Bond Yields (government long-term)				
UK	2.77	2.98	1.70	2.00
US	2.75	2.96	2.10	2.10
Germany	1.70	1.91	1.50	1.50
Japan	0.61	0.73	0.70	0.70
UK Index Linked	–0.08	0.55	–0.30	0.10
Exchange Rates				
UK ($ per £)	1.64	1.64	1.56	1.56
UK (trade weighted)	84.7	85.0	83.1	82.3
US (trade weighted)	86.5	87.1	85.5	85.5
Euro per $	0.73	0.73	0.79	0.79
Euro per £	1.20	1.20	1.23	1.23
Japan (Yen per $)	102.0	105.0	98.0	98.0
Short Term Interest Rates (3-month deposits)				
UK	0.51	0.58	1.80	2.10
US	0.24	0.26	0.70	0.70
Euro	0.26	0.25	0.50	0.50
Japan	0.07	0.09	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	3.30	2.6	2.4	44.00		52.30
US	1.90	2.8	2.0	24.00	4.94	35.64
Germany	2.80	1.5	2.0	39.00	–2.46	42.84
Japan	1.80	1.6	2.0	36.00	11.27	52.67
UK indexed[2]	0.55		2.4	–6.00		–3.05
Hong Kong[3]	2.50	7.0	2.0	6.00	4.94	22.44
Malaysia	3.00	5.2	2.0	52.00	4.94	67.14
Singapore	3.70	4.0	2.0	33.00	4.94	47.64
India	1.50	7.0	2.0	22.00	4.94	37.44
Korea	1.10	3.6	2.0	–6.00	4.94	5.64
Indonesia	2.70	5.5	2.0	40.00	4.94	55.14
Taiwan	2.70	2.7	2.0	22.00	4.94	34.34
Thailand	3.80	4.2	2.0	45.00	4.94	59.94

Bonds: Contribution to £ yield of:

	Redemption Yield	Changing Nominal Rates	Currency	Total
UK	2.98	9.80		12.78
US	2.96	8.60	4.94	16.50
Germany	1.91	4.10	–2.46	3.55
Japan	0.73	0.30	11.27	12.30

Deposits: Contribution to £ yield of:

	Deposit Yield	Currency	Total
UK	0.58		0.58
US	0.26	4.94	5.20
Euro	0.25	–2.46	–2.21
Japan	0.09	11.27	11.36

[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.

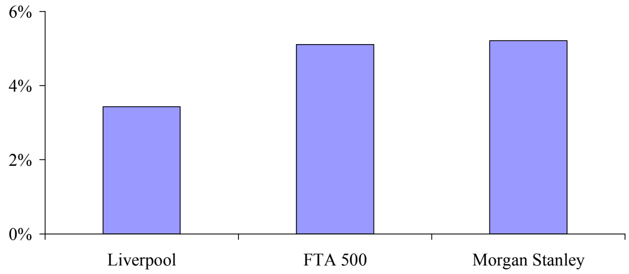
Table 3: Portfolio(%)

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

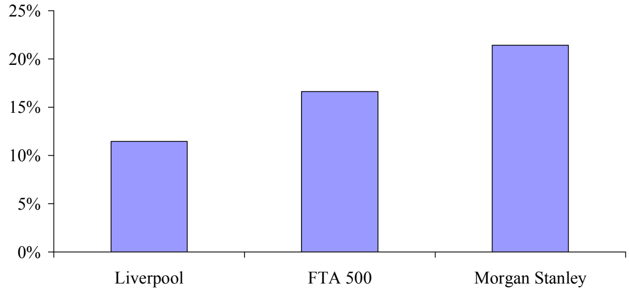
PORTFOLIO PERFORMANCE

The charts below, and the Table opposite, measure the performance of the Liverpool Model Portfolio against the FTA Non-financials share index, and the Morgan Stanley World Capital International index, over the period from June 1992 to end-January 2014.

3 Month Growth



12 Month Growth



3 Year Annualised Growth

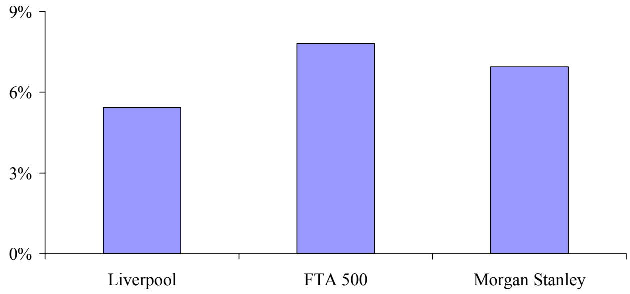


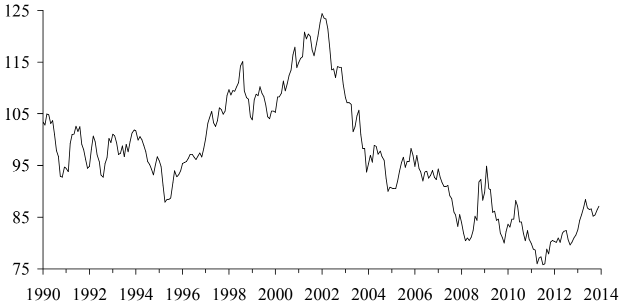
Table 4: Liverpool Portfolio Evaluation (End-June 1992 = 100)

Date	Index of Liverpool Portfolio	FTA Non Financials Index Total Return	Morgan Stanley World Capital International Index Total Return
2008			
1st Jan	396.02	411.25	403.19
Apr	389.00	367.01	365.34
Jul	387.93	381.90	355.90
Oct	400.53	324.99	335.11
2009			
1st Jan	439.02	314.73	323.33
Apr	424.38	294.99	283.79
Jul	441.61	315.62	295.72
Oct	508.20	375.37	355.96
2010			
1st Jan	526.64	408.79	365.52
Apr	564.11	436.43	399.80
Jul	531.62	382.77	351.60
Oct	572.20	435.61	378.02
2011			
1st Jan	620.58	476.51	413.02
Apr	621.29	481.43	420.69
Jul	631.17	494.36	418.86
Oct	548.00	437.69	358.02
2012			
1st Jan	575.91	482.11	384.40
Apr	630.65	495.88	414.96
Jul	605.43	480.40	398.13
Oct	631.88	507.18	410.42
2013			
1st Jan	652.78	512.06	416.11
April	723.28	559.95	477.75
Jul	702.74	542.18	476.11
Oct	703.32	568.11	480.17
Nov	736.88	591.21	502.56
Dec	724.26	584.13	500.77
2014			
1st Jan	727.46	597.17	505.19

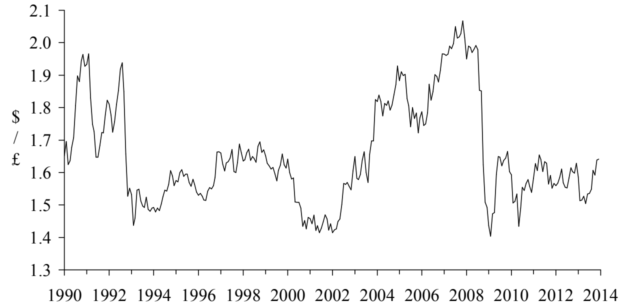
Source: Rensburg Sheppards Investment Management Limited, Liverpool Stock Exchange

INDICATORS AND MARKET ANALYSIS
FOREIGN EXCHANGE MARKETS

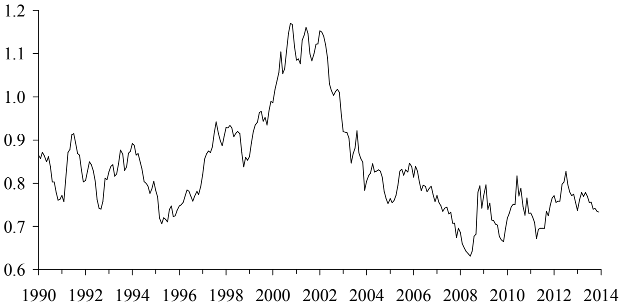
US : Trade Weighted Index
(Bank of England 1990 = 100)



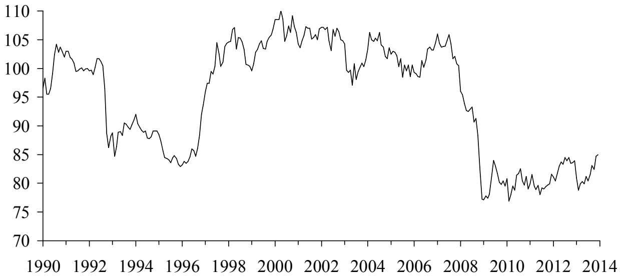
UK: Dollars Per Pound Sterling



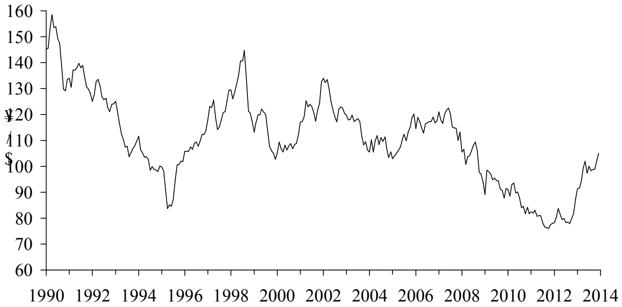
Euro per US dollar



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



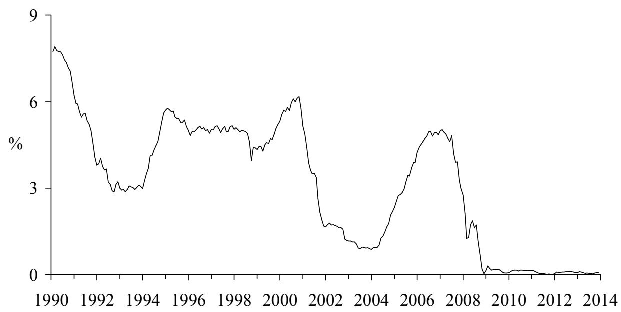
Japan : Yen Per U.S. Dollar



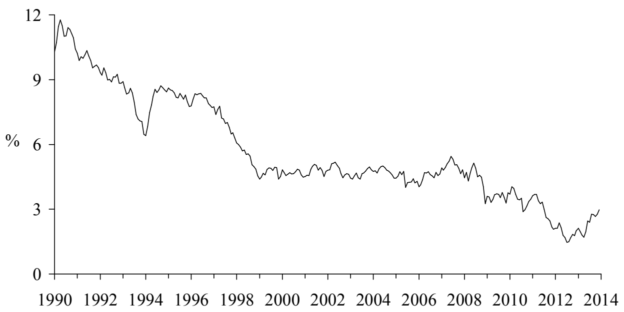
GOVERNMENT BOND MARKETS

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

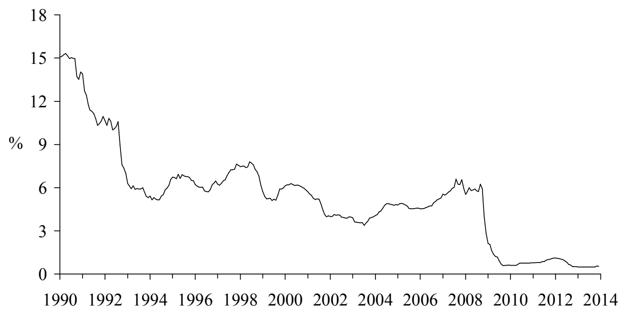
U.S. : 3-Month Treasury Bill



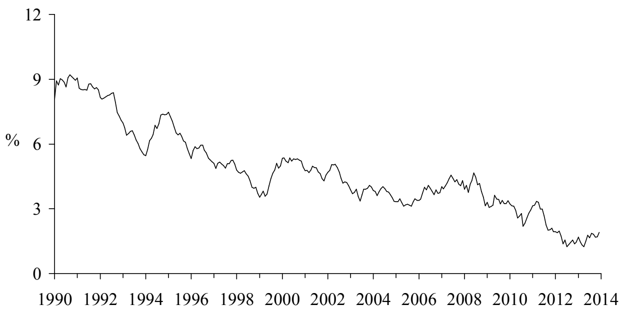
U.K. : Yield on Long-Term Government Bonds



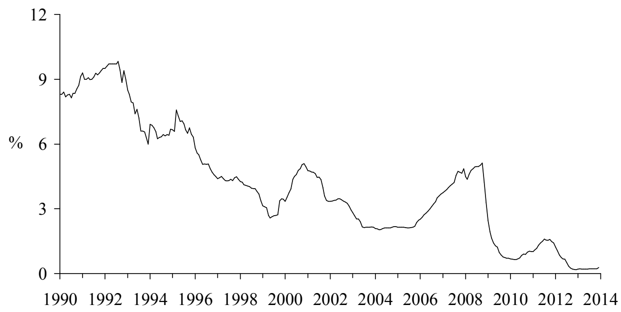
U.K. : 3-Month Interbank Rate



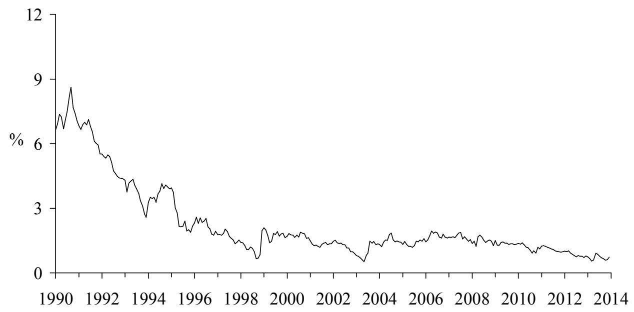
Germany: Yield on Public Authority Bonds



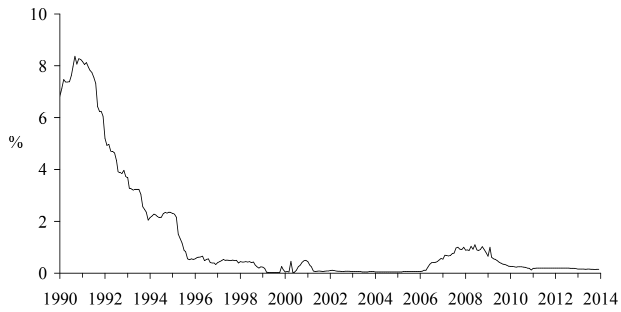
Germany : 3-Month Interbank Deposit Rate



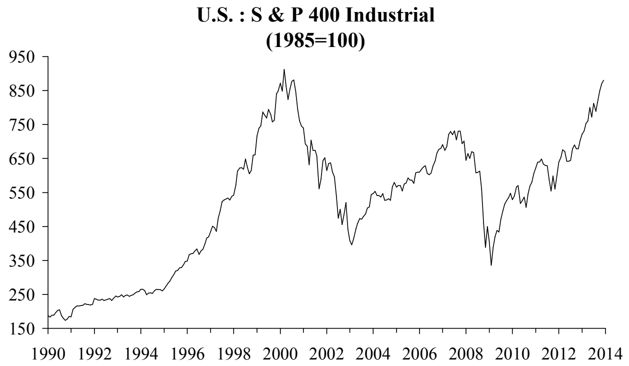
Japan: Yield on Long-Term Government Bonds

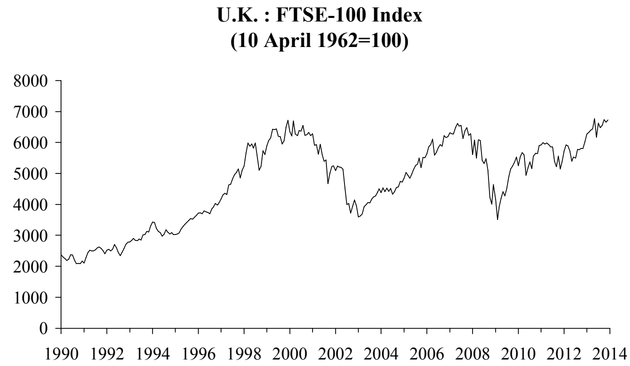


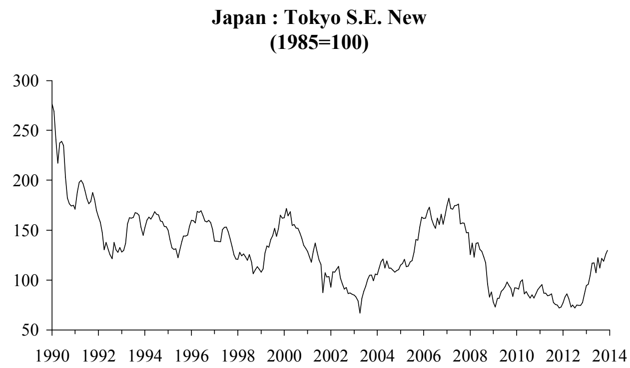
Japan : 3 Month Money Market Rate



MAJOR EQUITY MARKETS







EMERGING MARKETS

Anupam Rastogi

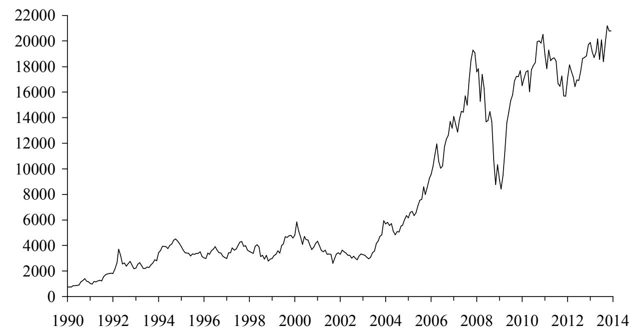
India

Indian voters in the assembly elections held in four states have rejected caste-based politics, pseudo-secularism, corruption and the politics of give-aways. They seem to be yearning for growth, opportunities, jobs and good governance. Many intellectuals, including Lord Desai, have accused the government of doing nothing about price rises since February 2009, which has affected poor people more than anyone else, as well as the profligacy of providing subsidized food and guaranteed jobs to village folks where wages are inflation indexed. In our letter (See September, 2013 issue) we predicted this change, and we hope that the same is likely to be repeated in the general elections in May 2014, for the reason that India has changed. More people live in urban India and their inspiration is not to depend upon government handouts, but on the opportunity to do well and climb the social ladder. The Bhartiya Janta Party's PM candidate Narendra Modi, an outstanding orator but economic with factual information, an extensive user of social media and old type of election rallies, backed by a dedicated and enthused party cadre, is seen as the saviour of the country. The business community and markets like him unequivocally as he has a record of the last fifteen years of governing the state of Gujarat, which has achieved one of the highest economic growth rates. He is lucky as well. In the past quarter the tide has turned: some of the firefighting done by the present government on the economic front has started to bear fruit, and will bloom in 2–3 quarters from now — by that time a new government will have been elected at the centre.

Last month, HSBC/Markit survey of purchasing managers showed manufacturing activity expanding in November for the first time in four months. And the current account deficit — the imbalance that made India a prime target in the exodus from emerging-market assets last summer — narrowed sharply to a four-year low of $5.2 billion in the three months ended September, up from $21 billion a year earlier.

India's central bank surprised markets by leaving its key lending rate unchanged in mid-December, sparking hopes that it could be easing its inflation-fighting stance and turning toward dealing with the country's economic slowdown. According to Mr Rajan, the Governor of the central bank, "Given the wide bands of uncertainty surrounding the short-term path of inflation from its current high levels, and given the weak state of the economy…

India: BSE Sensitive



there is merit in waiting for more data to reduce uncertainty." The RBI is clearly waiting and watching to see the impact of previous rate cuts, how US Federal Reserve tapering pans out and where inflation goes from here.

India's current-account deficit shrank to a four-year low last quarter as government restrictions slowed gold imports and the weak rupee bolstered exports. During the April–November period this fiscal year, the imports aggregated at $25.5 billion. It was $33.5 billion in November 2012. Going forward, we believe two key factors will shape the outlook for the trade deficit: 1) Continued efforts to rein in gold/non-essential imports and 2) Sustaining the momentum of exports revival. We expect trade deficit numbers to move up to $37 billion and CAD to be around $10 billion in Q3. For FY14, current account deficit is expected to hover around 3.3% of GDP.

Indian stocks reached record highs in 2013 but most international investors still lost money as the rupee's weakness erased returns. While the Indian benchmark, S&P BSE Sensex Index rose around 9% in 2013, touching an all-time high in early December, the MSCI India index, a widely-followed index of Indian stocks by global investors, lost close to 6% in dollar-terms because of the rupee's collapse. Comparatively, America's benchmark Standard & Poor's-500 stock index gained close to 30% in 2013. But this anomaly is more about the currency than it is about the stock market.

	11-12	12-13	13-14	14-15	15-16
GDP (%p.a.)	6.2	5.0	5.0	6.5	7.0
WPI (%p.a.)	7.5	7.0	6.5	6.0	6.0
Current A/c(US$ bill.)	-40.0	-80.0	-70.0	-60.0	-60.0
Rs./$(nom.)	49.5	54.5	62.0	64.0	65.0

China

China's economy will post a growth of 7.6% for 2013, marginally better than Beijing's 7.5% target. This compares well with a 7.7% growth rate for 2012, as government wants to move away from export led economy to a domestic based growth. China's economy posted year-over-year growth of 7.8% in the third quarter after expanding 7.7% in the first quarter and 7.5% in the second quarter amid a sluggish global economy. The state-sponsored PMI fell to 51 in December, down from 51.4 in November, marking a four-month low and highlighting the challenges facing the ruling Communist party as it tries to transform the growth model.

China's leaders have reaffirmed their intention to turn urbanization into a powerful engine to drive growth and remake the economy. They want to encourage rural residents to move to smaller cities, rather than Beijing, Shanghai and other megacities as the government believes that urbanization is a powerful agent for economic change. Rural residents who move permanently to a city earn more than they do from their agricultural plots back home and spend more freely, boosting domestic demand. Their departure from the countryside would also allow agricultural land to be consolidated and farmed more efficiently, raising productivity and income in rural areas.

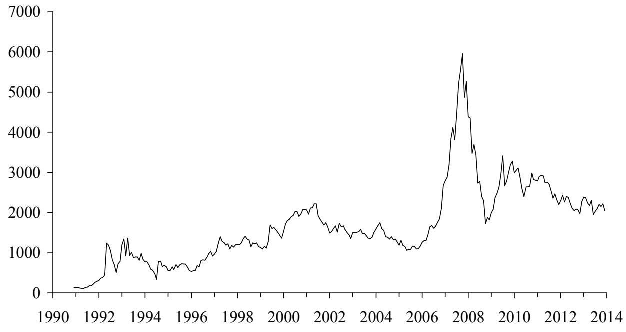
On Monday, China's central bank unveiled a blueprint to make it easier for businesses and individuals in Shanghai's free-trade zone to invest abroad, a measure partly aimed at increasing flows of yuan into and out of China and help in internationalizing yuan.

Mr. Xi, the president, seems to be redefining the roles of the president and the premier. A nearly two-decade-old division of power whereby the president, who is also party chief, handles politics, diplomacy and security, while the premier manages the economy. Recently, Mr Xi is taking active interest in setting economic policies and Mr Li is left to execute them. When U.S. Treasury Secretary Jacob Lew visited Beijing after the Central Committee meeting, he met Mr. Xi and didn't meet Mr. Li at all. Similarly, Prime Minister Cameron's meetings were rescheduled to meet Mr Xi on economic issues.

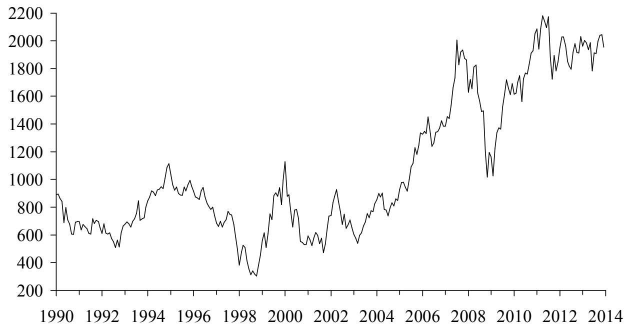
China's government holding company — the State-owned Assets Supervision and Administration Commission — is planning to allow differing levels of private ownership in many industries, depending on their strategic importance. Both financial and strategic investors will be allowed to buy stakes, according to Huang Shuhe, SASAC's vice chairman.

Local government debt levels in China, which soared to almost $3 trillion in less than three years according to an official audit, highlighted one of Beijing's most daunting challenges as it attempts to sustain economic growth while avoiding a financial crisis. In a long-awaited report, China's National Audit Office said local government debts had increased almost 70% to reach Rmb17.9 trillion ($2.95 trillion) by the end of June 2013. The NAO, whose last survey put the burden at Rmb10.7 trillion at the end of 2010, added that government debt levels were generally "under control" but identified "potential risks in some places". The Chinese government is not perturbed by this development as most of the credit funded by banks has gone to build very large infrastructure projects which are not used to their full capacity.

China: SSE Composite Index



Korea: Composite Index



	11	12	13	14	15
GDP (%p.a.)	9.2	7.7	7.6	7.3	7.0
Inflation (%p.a.)	4.3	2.6	3.5	3.0	2.5
Trade Balance(US$ bill.)	210	214	220	220	200
Rmb/$(nom.)	6.3	6.3	6.2	6.1	6.0

South Korea

South Korea trimmed its growth forecast for next year and hopes that the economy will continue to pick up with fiscal spending at home and an international recovery. South Korea's economy expanded 1.1% in the second and third quarters of 2013 — the fastest pace since the first quarter of 2011. The 2014 growth forecast is lowered to 3.9% from a June projection of 4.0% by the government. The estimate for growth for 2013 was revised up to 2.8% from 2.7% in June. The economy grew 2% in 2012.

Consumer prices are expected to rise 2.3% in 2014 — slower than its June forecast of 2.8% but faster than 2013's estimate of 1.3%. Inflationary pressure comes largely from expectations of economic recovery. This year's lower comparison base and the end of childcare subsidies next year may increase headline inflation. However, it is still below the central bank's target of 2.5%–3.5%.

South Korea's current account surplus for 2014 is likely to rise to $49 billion from its June forecast of $30 billion. The 2013 surplus will reach $70 billion. Even though exports did not grow with expectation, a widely held view is that South Korea's economy is gradually regaining momentum. Total exports rose just 0.2%, below the 2.5% forecast and far off October's revised 7.2% pace. HSBC/Markit purchasing managers' index improved to 50.4 in November from 50.2 in October, indicating that manufacturing is expanding, albeit slowly. The PMI's new export order subcomponent rose solidly in November, though it was down from October's 31-month high.

South Korea has posted a current account surplus of $US6.03 billion in November, with the accumulated surplus so far in 2013, exceeding the government's estimate. The central bank estimates surplus of $US63 billion for the whole of 2013.

Nearly a decade after South Korea's first private equity fund was set up, local funds are emerging as leading players in the domestic buyout market, encouraged by a government keen to develop the industry as a key source of corporate financing. This year private equity firms have completed a record number of buyouts in South Korea, with 40 deals worth $7.1 billion, representing nearly a quarter of the country's $31.3 billion mergers and acquisitions activity, according to industry sources. Transactions by domestic private equity groups accounted for $6.1 billion of that total, up 13% from 2012.

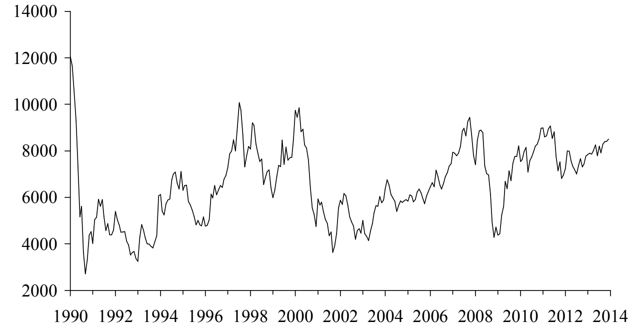
In its latest bid to cultivate private equity investment, Seoul loosened rules further, dropping the requirement that new buyout funds receive government clearance and removing a ban on their investing in real estate, stocks and derivatives.

	11	**12**	**13**	**14**	**15**
GDP (%p.a.)	3.6	2.0	2.8	3.6	3.6
Inflation (%p.a.)	4.0	2.2	1.3	2.3	2.7
Current A/c(US$ bill.)	27.0	44.0	70.0	50.0	60
Won/$(nom.)	1100	1100	1100	1080	1060

Taiwan

Taiwan's government has forecast the nation's GDP growth would expand to 2.59% in 2014 from an estimated 1.74% growth in 2013. Taiwan held its benchmark interest

Taiwan: Weighted TAIEX Price Index



rate for a 10th straight meeting after it lowered its forecasts for economic growth and inflation for 2013 and 2014. The central bank kept the discount rate on 10-day loans to banks at 1.875%. The monetary authority has refrained from adjusting borrowing costs since June 2011, the longest period of inaction, according to its data going back to 1980.

Taiwan's government needs to end its political stalemate with China to spur economic growth, President Ma Ying-jeou said in his New Year's address. He said that for Taiwan to take its economy to the "next level," the island would need a breakthrough in the "cross-strait standoff" and "boost economic and trade cooperation". Exports account for 70% of Taiwan's economy, and today 40% go to the mainland — up from 29% in 2010, when Taipei and Beijing signed a landmark cross-Strait trade agreement. Meanwhile some 80% of Taiwanese foreign investment goes into China (up from less than 50% a decade ago).

Taiwan's free-trade agreement with New Zealand went into effect last month, amid high regional tensions over China's new air-defence zone. As Beijing keeps finding fresh ways to bully its neighbours, Taiwan is trying to reverse its growing economic dependence on China.

Private-equity investment in Taiwan has plunged since the global financial crisis. In 2013 PE investments totalled less than 1% of that seen in 2007, but proposed new rules may help revive interest in the country. Investors have found successful exits from Taiwan difficult, which has deterred new investments, but they have also struggled with what they consider to be an opaque, erratic regulator that sometimes imposes unnecessarily strict demands.

	11	**12**	**13**	**14**	**15**
GDP (%p.a.)	4.0	1.3	1.7	2.5	2.7
Inflation (%p.a.)	1.2	1.9	0.6	1.0	1.0
Current A/c(US$ bill.)	18.0	20.0	22.0	23.0	24.0
NT$/$(nom.)	30.0	29.5	30.0	29.5	29.0

Brazil

Brazil's economy is unlikely to show stellar growth in 2014, despite improving conditions abroad and the 2014 FIFA World Cup. According to the National Confederation of Industries, investment in the economy is drying up. Brazil's economy shrank in the third quarter as investment declined and manufacturing and agricultural output slumped.

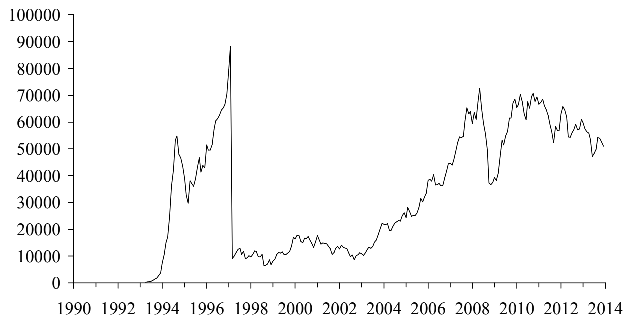
The economy contracted 0.5% compared with the second quarter, or −1.9% at an annualised rate. It was the weakest quarterly performance since early 2009, when the world was in the depths of the global financial crisis. Therefore, expansion of GDP is likely to be only 2.3% in 2013. This is far below the 4.5% growth Brazil's government estimated at the start of the year. For 2014, growth may slide further to 2.0%.

One of the reasons for this is the country's slowness in moving forward with planned infrastructure projects from ports to roads and airports. Plans to auction off contracts to operate roads and airports have faced long bureaucratic delays. Some projects, such as a much vaunted high-speed rail between São Paulo and Rio de Janeiro, have been essentially shelved. As a result, Brazil appears to be missing out on the global recovery that is starting to materialize.

Consumption remains robust in the Brazilian economy. Unemployment is low and wages have risen. This cannot continue as consumers have borrowed heavily and are having to rein in spending. The inflation rate is rising. The country's IPCA consumer-price index is touching 6%. In order to control inflation, the central bank was forced to raise its base interest rate by 3.75 percentage points since April, to 10%.

Government intervention in the economy has upset many investors. Tough negotiations over the renewal of electric power contracts in 2012 increased tension with the private sector. However, the government is confident to achieve 4% growth rate in 2014. Brazil has set an annual inflation target of 4.5%, but allows a margin of tolerance of up to 6.5%. Brazil's real has weakened more than 10% against the dollar this year as global investors anticipated the withdrawal of monetary stimulus in the U.S.

Brazil: Bovespa



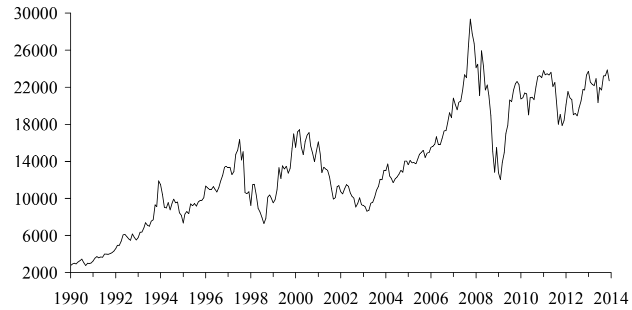
Brazil's unemployment rate remained at a record low in November. But, rising real wages have pummelled profit margins, leaving Brazilian companies with the region's lowest returns on equity, at about 6%. After emerging as an economic powerhouse on the same level as China and India with 7.5% growth in 2010, Brazil now finds itself teetering on the brink of recession after the economy shrank 0.5% in the third quarter.

Brazil's Central-Bank Governor, Alexandre Tombini, is optimistic about the Brazilian economy as the U.S. and Europe get out of an economic downturn. In his opinion the sooner the U.S. Federal Reserve begins tapering its bond-buying policy, the better. He believes that Brazil's $376 billion foreign reserves are a "cushion" that will protect the local currency, the real, against sharp volatility in global markets.

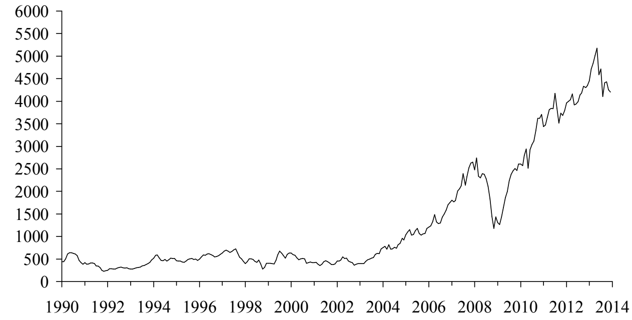
	11	**12**	**13**	**14**	**15**
GDP (%p.a.)	2.7	0.9	2.3	2.0	3.0
Inflation (%p.a.)	6.5	5.8	6.5	6.0	6.0
Current A/c(US$ bill.)	-52.6	-60.0	-75.0	-70.0	-70.0
Real/$(nom.)	1.5	2.0	2.3	2.4	2.4

Other Emerging Markets

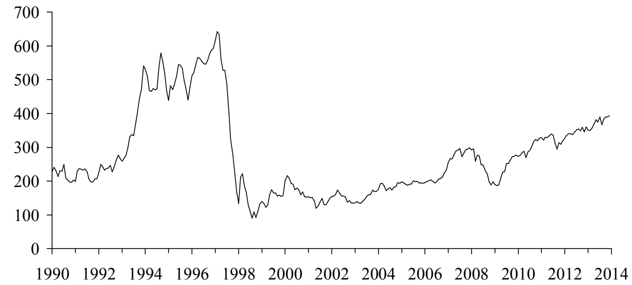
Hong Kong: FT-Actuaries



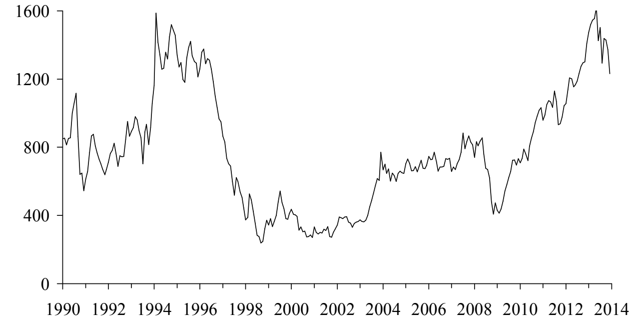
Indonesia: Jakarta Composite



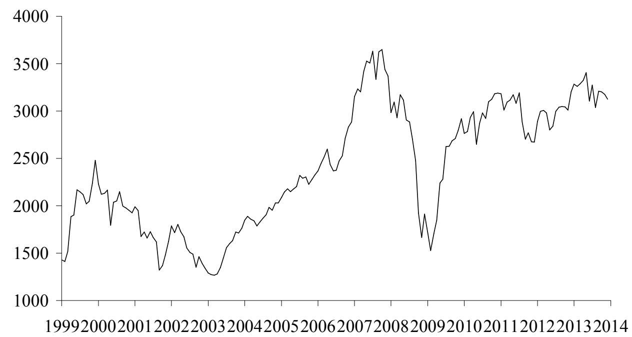
Malaysia: FT-Actuaries (US$ Index)



Thailand: Composite Index



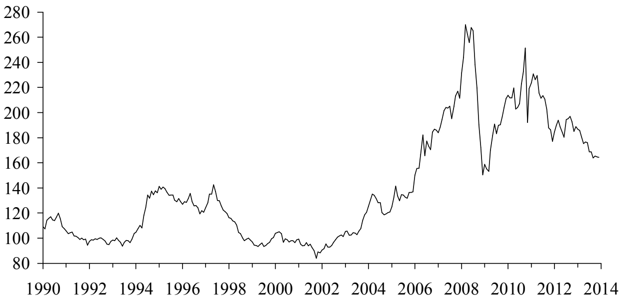
Singapore: Straits Times Index



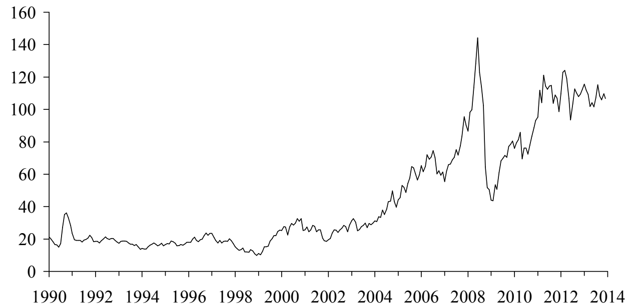
Philippines: Manila Composite

COMMODITY MARKETS

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

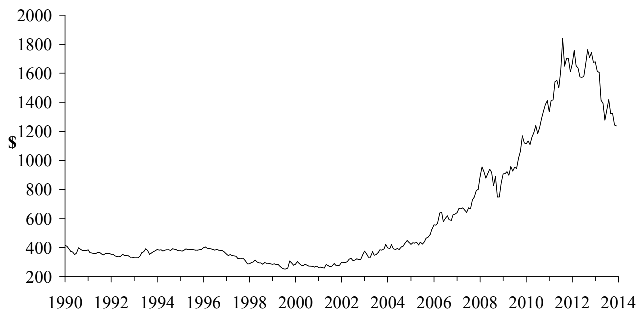


Oil Price: North Sea Brent (in Dollars)

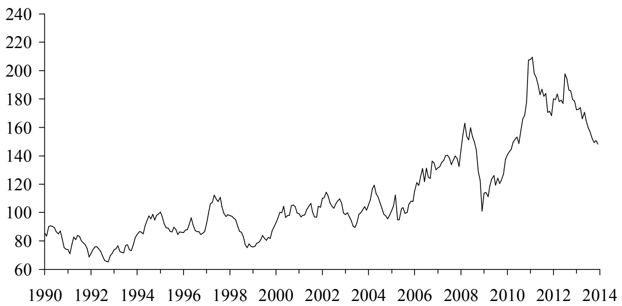


Commodity Price Index (Sterling)
(Economist, 2000=100)

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]
2010	3.3	2.4	0.7	80.4	88.6	−3.5	4.8	−0.2
2011	4.5	2.0	0.9	80.0	89.8	−2.8	5.3	−0.2
2012	2.7	0.9	0.9	83.1	93.9	−1.8	3.2	−1.4
2013	2.4	1.2	0.6	82.6	92.5	−1.7	3.2	−1.0
2014	2.5	1.6	1.8	83.0	94.1	−1.6	3.1	−0.5
2015	2.2	2.0	2.1	82.3	95.4	0.1	2.8	0.1
2012:1	2.7	1.1	1.1	81.2	91.6	−1.9	3.8	−1.3
2012:2	3.1	0.9	1.1	83.1	94.2	−1.4	3.2	−1.4
2012:3	2.5	0.7	0.8	84.1	95.2	−1.8	2.9	−1.6
2012:4	2.5	0.8	0.6	83.6	94.8	−2.0	3.0	−1.5
2013:1	2.6	1.0	0.6	80.3	90.9	−1.7	3.3	−1.3
2013:2	2.3	1.0	0.6	80.6	92.6	−1.9	3.1	−1.3
2013:3	2.4	1.5	0.5	81.2	93.2	−1.5	3.2	−0.7
2013:4	2.5	1.5	0.7	81.0	93.2	−1.9	3.2	−0.7
2014:1	2.6	1.6	0.8	81.3	93.7	−1.7	3.1	−0.6
2014:2	2.5	1.6	0.8	81.2	94.0	−1.6	3.1	−0.6
2014:3	2.4	1.7	0.9	81.3	94.0	−1.6	3.1	−0.4
2014:4	2.4	1.7	0.9	81.8	94.6	−1.5	3.0	−0.4

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)
2010	227.1	2.4	4.6	1.50	135.6
2011	232.7	2.5	4.6	1.53	133.5
2012	237.0	1.9	4.7	1.59	132.4
2013	240.2	1.4	4.3	1.45	131.0
2014	246.3	1.6	3.9	1.33	131.1
2015	235.1	2.2	3.9	1.31	133.3
2012:1	236.6	0.7	4.8	1.61	132.6
2012:2	238.1	1.8	4.8	1.59	132.2
2012:3	238.1	1.9	4.7	1.57	132.9
2012:4	236.6	3.3	4.6	1.56	131.8
2013:1	242.1	0.6	4.5	1.54	130.1
2013:2	240.1	2.4	4.4	1.50	132.3
2013:3	242.1	0.8	4.1	1.39	130.8
2013:4	243.8	1.7	4.0	1.37	130.8
2014:1	245.9	3.1	4.0	1.36	130.7
2014:2	246.5	1.6	3.9	1.34	131.1
2014:3	248.8	2.7	3.8	1.31	131.1
2014:4	235.1	2.8	3.8	1.30	131.2

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
2010	143.2	685816.8	412464.1	222982.1	180596.2	−35977.3	94248.2
2011	144.8	693480.0	405707.9	232196.6	179249.7	−24641.9	99032.3
2012	145.0	694345.6	405044.8	241788.1	182996.5	−31204.8	104279.0
2013	147.1	704061.8	408532.0	244321.9	181864.1	−32814.9	102184.1
2014	150.8	722173.8	414751.1	266188.7	175499.7	−38621.7	95765.2
2015	154.4	735702.5	414580.1	250992.1	193479.8	−31157.8	92210.8
2010/09	1.7		0.3	11.0	0.1		8.3
2011/10	1.1		−1.6	3.8	−0.8		4.5
2012/11	0.2		−0.1	2.5	3.0		3.0
2013/12	1.4		0.9	1. 1	−0.6		−2.0
2014/13	2.6		1.5	9.0	−3.5		−6.3
2015/14	2.4		1.5	7.0	2.3		3.1
2012:1	145.2	173789.2	101182.0	58927.4	47960.2	−6985.4	27295.1
2012:2	144.5	172990.1	101166.9	58367.1	44720.2	−8453.9	22810.2
2012:3	145.4	174050.5	100983.7	61663.0	45063.8	−7626.9	26033.1
2012:4	145.0	173515.9	101712.2	62830.6	45252.2	−8138.6	28140.5
2013:1	145.5	174176.5	102040.8	59115.5	46685.8	−7448.6	26217.1
2013:2	146.5	175320.9	101998.8	59299.2	44851.2	−7561.4	23266.9
2013:3	147.6	176705.8	102780.2	63076.6	45074.9	−9666.3	24559.6
2013:4	148.6	177858.6	102637.0	67168.4	42397.4	−9663.9	24478.8
2014:1	149.3	178747.9	103029.0	66015.6	43049.0	−9664.1	23431.4
2014:2	150.2	179820.4	103449.6	66632.0	43319.2	−9655.3	23693.8
2014:3	151.4	181259.0	103898.6	64834.9	45886.2	−9650.6	24248.6
2014:4	152.3	182346.5	104373.9	68706.1	43245.3	−9651.8	24391.5

[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)
2010	10.5	1319.8	139.6	36.6	−40.0
2011	8.4	1399.3	118.5	43.0	−22.5
2012	8.0	1429.6	115.0	46.4	−59.2
2013	7.6	1471.7	112.3	48.0	−60.7
2014	7.1	1537.0	109.4	52.8	−62.9
2015	5.9	1613.2	94.6	60.3	−63.5
2012:1	5.9	356.4	21.0	11.5	−12.5
2012:2	10.5	350.3	36.7	11.4	−17.8
2012:3	7.2	358.6	25.7	11.8	−15.3
2012:4	10.6	364.3	38.6	11.8	−13.6
2013:1	3.8	364.3	14.0	12.0	−14.5
2013:2	9.3	363.3	33.7	11.6	−17.1
2013:3	6.2	369.4	23.1	12.0	−15.9
2013:4	7.6	374.6	28.3	12.3	−13.2
2014:1	7.2	375.2	27.3	12.7	−16.3
2014:2	6.9	379.8	26.2	13.1	−17.3
2014:3	7.1	384.4	27.3	13.5	−16.0
2014:4	7.1	390.1	27.9	13.6	−13.3

[1] GDP at market prices (Financial Year)

WORLD FORECAST DETAIL

Growth Of Real GNP

	2009	2010	2011	2012	2013	2014
U.S.A.	–2.6	2.4	1.8	2.2	2.2	2.8
U.K.	–3.9	1.7	1.1	0.2	1.4	2.6
Japan	–6.3	4.7	–0.5	1.9	1.8	1.6
Germany	–4.7	4.2	3.0	0.7	0.6	1.5
France	–2.5	1.6	2.0	0.0	–0.4	0.7
Italy	–5.1	1.7	0.5	–2.4	–1.8	0.4

Real Short-Term Interest Rates

	2009	2010	2011	2012	2013	2014
U.S.A.	–1.6	–3.0	–1.8	–1.9	–1.3	–1.2
U.K.	–0.3	–3.5	–2.8	–1.8	–1.7	–1.6
Japan	1.1	0.4	0.4	0.3	–1.6	–1.6
Germany	–0.4	–1.9	–0.5	–1.5	–1.5	–1.4
France	–0.8	–1.7	–0.5	–1.4	–1.5	–1.4
Italy	–0.8	–2.4	–1.5	–2.6	–2.0	–1.4

Real Long-Term Interest Rates

	2009	2010	2011	2012	2013	2014
U.S.A.	1.3	1.0	0.9	–0.2	0.1	0.6
U.K.	–0.3	–0.2	–0.2	–1.4	–1.0	–0.5
Japan	1.2	0.4	–0.2	–0.8	–1.3	–1.1
Germany	2.2	1.8	–0.1	–0.4	–0.5	–0.1
France	2.2	1.9	–0.1	–0.4	–0.5	–0.1
Italy	1.5	1.2	–0.7	–0.8	–0.6	–0.1

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

	2009	2010	2011	2012	2013	2014
U.S.A.	88.7	87.4	85.7	90.4	97.3	99.1
U.K.	76.7	88.6	89.8	93.9	92.5	94.1
Japan	89.0	92.0	97.1	98.3	119.7	122.0
Germany	105.8	102.9	105.5	104.3	107.4	108.2
France	104.3	103.1	105.5	104.9	107.9	108.6
Italy	105.4	103.6	106.9	107.4	111.8	113.2

[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

	2009	2010	2011	2012	2013	2014
U.S.A.	–0.3	1.6	3.1	2.1	1.6	2.0
U.K.	1.3	3.3	4.5	2.7	2.4	2.5
Japan	–1.4	–0.7	–0.3	0.0	0.0	2.0
Germany	0.4	1.2	2.0	2.0	1.7	2.0
France	0.1	1.5	2.1	2.0	1.6	1.5
Italy	0.8	1.5	2.8	3.0	2.8	1.6

Nominal Short-Term Interest Rates

	2009	2010	2011	2012	2013	2014
U.S.A.	0.2	0.1	0.3	0.1	0.7	0.8
U.K.	1.1	0.7	0.9	0.9	0.6	1.8
Japan	0.1	0.1	0.4	0.3	0.4	0.4
Germany	0.7	0.4	1.5	0.2	0.5	0.6
France	0.7	0.4	1.5	0.2	0.5	0.6
Italy	0.7	0.4	1.5	0.2	0.5	0.6

Nominal Long-Term Interest Rates

	2009	2010	2011	2012	2013	2014
U.S.A.	3.2	3.1	1.9	1.8	2.1	2.6
U.K.	2.8	2.4	2.0	0.9	1.2	1.6
Japan	1.3	1.1	1.0	0.8	0.7	0.9
Germany	4.0	3.8	1.8	1.5	1.5	1.9
France	4.0	3.8	1.8	1.5	1.5	1.9
Italy	4.0	3.8	1.8	1.5	1.5	1.9

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

	2009	2010	2011	2012	2013	2014
U.S.A.[1]	85.98	83.73	78.08	80.90	85.50	85.40
U.K.	1.57	1.58	1.61	1.59	1.55	1.55
Japan	93.54	87.48	79.36	80.51	98.00	98.00
Eurozone	0.72	0.75	0.71	0.78	0.79	0.78

[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