Schroders
Economic and Strategy Viewpoint

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European forecast update: Upgrades all round (page 2)

- It is a sea of green in Europe as we upgrade our growth forecast across the board. In the Eurozone, lower energy prices, a depreciating euro, stronger banks and ECB QE should all help lift growth in 2015 and 2016. The forecast for the UK has also been revised up, but the economy is on a slowing trend. Lower energy prices will help provide a soft landing.
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Views at a glance (page 6)

- A short summary of our main macro views and where we see the risks to the world economy.
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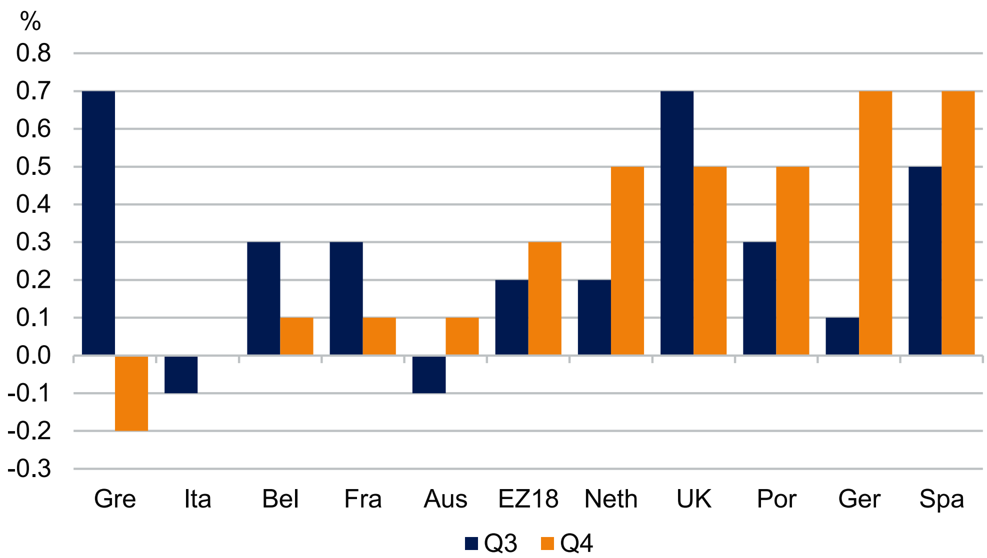
Chart: Germany and Spain lift Eurozone GDP (q/q)



Source: Eurostat, Schroders. 24 February 2015.

European forecast update: Upgrades all round

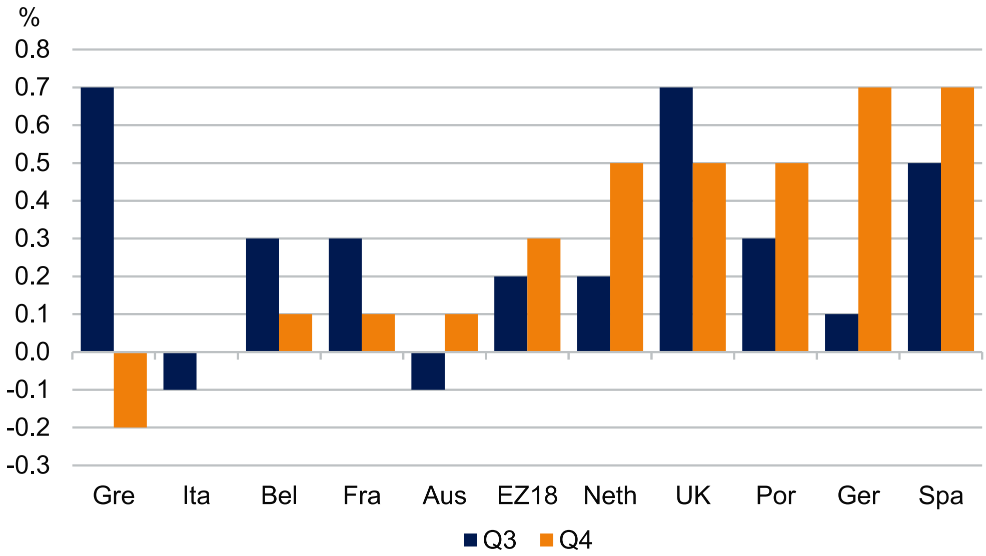
Macro data is on an improving trend in the Eurozone as the monetary union now looks ready to resume its recovery following the pause in the middle of last year. Growth should be bolstered by the recent fall in global energy prices, which at the same time will keep policymakers worried about the risk of long-term deflation. Meanwhile, the UK's slowdown is underway, but falling energy bills are likely to soften the landing.

Recovery resumes as political risk subsides

Germany and Spain lifted Eurozone growth at the end of 2014

Growth in the Eurozone accelerated at the end of last year as the monetary union appeared to be shaking off some of the concerns caused by the Ukraine/Russia conflict. Aggregate quarterly GDP growth in the fourth quarter rose to 0.3%, up from 0.2%, and was also higher than the market consensus of 0.2%. Germany and Spain led the way as both recorded 0.7% growth, while the Netherlands and Portugal also showed an improvement with growth of 0.5% each. To the downside, France and Italy underperformed the aggregate, as France eked out just 0.1% growth. Italy beat expectations by not contracting, albeit thanks to numerical rounding. GDP did however fall by €72 million, which technically keeps Italy in recession.

Chart 6: Germany and Spain lift Eurozone GDP (q/q)



Source: Eurostat, Schroders. 24 February 2015.

Ebbing political risk seemed to lift confidence and business investment

As mentioned above, it seems that Europe has begun to shake off the negative sentiment caused by the Ukraine/Russia crisis. For example, fixed investment in Germany increased by 1.2% in Q4, compared to -1.2% in Q3 and -1.7% in Q2. Net trade is also up, with both Germany and France seeing a sharp rise in exports. Consumer confidence is on the rise too according to the European Commission's survey, while the Markit PMIs have also improved recently. All of this points to a resumption of the Eurozone's recovery following the mid-year pause in 2014.

Another source of political risk which is ebbing is the latest Greek crisis. At the time of writing, Greece had just had its current bail-out extended for four more months, which will enable it to negotiate the next stage of the bail-out. Despite Syriza's pre-election promises, the party's leadership has essentially totally surrendered to the demands of its lenders. The only thing Prime Minister Alexis Tsipras has achieved is to rename the "Troika" to the "Institutions", the "memorandum" to the "agreement", and the "lenders" to the "partners".

The Greek crisis also appears to be settling down, albeit for a few months

The crisis will most likely return in the summer, as Tsipras will probably appeal for more time domestically to win concessions from the Troika. If the government does not collapse in the next four months, then the negotiations for a longer-term deal will commence. Europe is likely to continue to take a tough stance, as the erosion of trust caused by the methods employed by the Greek government lead to a loss of sympathy by other member states, especially in the periphery.

In any case, Greece is too small to have a substantial macro impact. Moreover, since 2012, the European financial sector has largely either disposed of or written off its exposure to the Greek economy – meaning the risk of financial contagion is now also minimal. The lack of contagion means that whilst we continue to put a 20% chance on Greece leaving the Eurozone, the global impact would be hard to notice.

A sea of green – upgrades all round

Lower oil prices, a weaker euro, stronger banks and ECB bond buying are four reasons to upgrade Eurozone growth

With regards to our forecast, we find ourselves upgrading growth across Europe once again. Slightly better-than-expected outturns for the fourth quarter have helped, but there are four key tailwinds all contributing to a stronger outlook over the forecast horizon:

1. Oil prices have fallen further over the past three months. As we have discussed in recent months, the fall in oil prices will lower the cost of domestic energy, thereby increasing the amount of disposable income for households, and improving profit margins for firms. This then generates a multiplier effect as those savings are spent through consumption and/or increased investment.
2. The trade-weighted euro has depreciated by 7.1% since our previous forecast in November, providing another tailwind. This will help raise demand for European exports, while domestic producers will see the price of rival imported goods rise. It will also help boost earnings for European-listed companies, where 44% of Eurostoxx50 companies' sales are from overseas.
3. The banking system is slowly returning to normal activity following the completion of the ECB's asset quality review and the preceding uncertainty. Banks are now beginning to compete with each other to win new business, which is great news for households and corporates. Borrowers are at last seeing the cuts in interest rates from the ECB feeding through to the effective borrowing costs that they face.
4. The ECB will begin to buy sovereign and agency debt as part of its expanded asset purchase scheme. This should help lower interest rates across the monetary union, but in particular in the periphery, where the monetary policy transmission mechanism has been broken. It could also encourage a further depreciation of the euro, which would be helpful for growth too.

For the Eurozone in aggregate, we have raised our forecast from 0.9% to 1.3% for 2015, versus a consensus of 1.2%. For 2016, we have raised the forecast from 1.4% to 1.6%, against a consensus of 1.7% (chart 7 on next page). On the inflation front, we have lowered the forecast from 0.8% to 0.1% for this year, versus a consensus of -0.1%, while for 2016, we forecast inflation to rise to 1.2%, an upward revision from 1.1%, which is also the consensus (chart 8 on next page).

Inflation is likely to remain in negative territory for the next few months, but as oil prices have already begun to rebound, the negative impact will begin to unwind by the end of the year. There is a risk that households begin to factor in deflationary inflation expectations, however, we feel that this needs a further slowdown in growth in the near-term for it to be a central scenario.

Higher growth and lower inflation is a good mix for the region

Chart 7: EZ GDP forecast

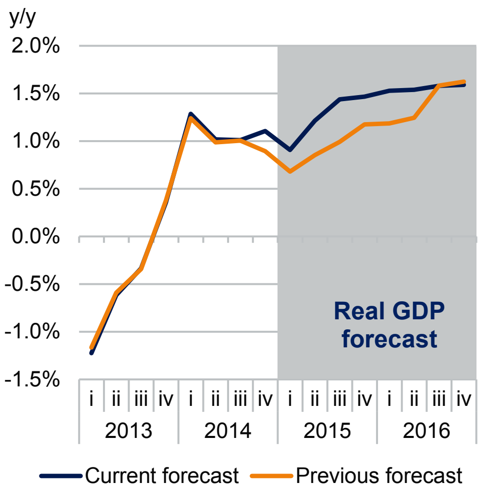
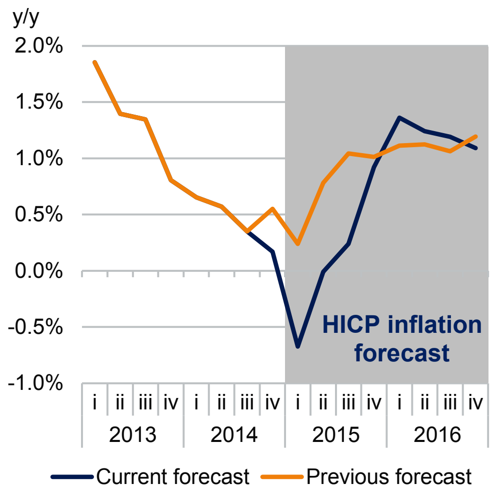


Chart 8: EZ inflation forecast



Source: Thomson Datastream, Schroders. 20 February 2015. Previous forecast from November 2014. Please note the forecast warning at the back of the document.

Within the large member states, we have upgraded all of the forecasts, although more so for the stronger reformers (table 2). For example, Spain is now expected to be the fastest growing economy of the big four over the next two years thanks to continued gains in employment, and stronger activity readings. Germany will also perform well as private and public investment is stepped up, while the household sector continues on its long-term transformation into more prominent consumers. France is likely to struggle this year and next, but the cyclical factors mentioned above will boost activity in lieu of more significant structural reforms. Finally, Italy is likely to emerge from recession in the coming quarters, and eventually begin to enjoy the fruits of the structural reforms being implemented at present.

All member states seeing growth upgraded, although Spain is set to lead the way

Table 2: Eurozone GDP forecast

	2015	Previous	2016	Previous
Germany	1.6 ↑	1.2	2.0 ↑	1.8
France	0.8 ↑	0.6	1.2 ↑	0.9
Italy	0.3 ↑	0.2	1.0 ↑	0.7
Spain	2.3 ↑	1.5	2.1 ↑	1.7
Eurozone	1.3 ↑	0.9	1.6 ↑	1.3

Source: Schroders. 20 February 2015. Previous forecast from November 2014. Please note the forecast warning at the back of the document.

Our forecast for the ECB is largely unchanged: we do not expect any changes to interest rates for the foreseeable future, while we expect the ECB to conduct QE at the stated pace of €60 billion per month until September 2016. Due to the liquidity constraints the ECB has introduced, we do not see any room for a further expansion of the scheme.

UK upgraded, but slowdown still coming

UK households are seeing improving conditions…

Much like the Eurozone, the UK will also benefit from the continued falls in energy prices. Fuel prices have been coming down as expected, while home utility prices have also fallen, but less so due to a lack of competition. Taken together with continued employment gains and rising real wage growth, the savings from lower energy prices are the icing on the cake for consumers. Retail sale volumes in the three months to January are up 5.3% compared the same period a year earlier – the fastest rate of growth since October 2004.

Despite consumers seeing an improvement in their situation, the UK economy overall had a weaker-than-expected end to 2014, posting 0.5% quarterly growth compared to consensus estimates of 0.7%. That represents the slowest rate of growth since the end of 2013. Official data suggests the construction sector contracted by 2.1% in the final quarter of the year, which is consistent with a slowdown in investment.

…although the economy is still on a slowing trend.

The residential housing market has also been slowing, as a combination of tighter lending conditions and concerns over the possible introduction of a 'mansion tax' after the general election has badly impacted sentiment especially in London. According to the Royal Institute of Chartered Surveyors, its members are widely reporting outright falling prices – roughly on a scale not seen since 2009. The provision of cheaper loans and the increased turnover in the housing market has been an important driver of growth in the UK over the past year. This now seems to be moderating to more normal levels.

In looking at our UK forecast, the first point to make is that the official data has been revised to show slower growth over 2014 compared to our previous forecast. GDP growth for 2014 has been revised down from 3.1% (estimated) to 2.6%. This mechanically lowered our 2015 forecast from the previous estimate of 2.5% to 2.3%. However, the boost from lower energy prices has led us to revise up our forecast to 2.6% (chart 9). So the downward revisions to last year's data are masking what is otherwise an upgrade to growth for this year. For 2016, we continue to forecast a slowdown for all of the above reasons, and the likely fiscal tightening after the general election. However, the fall in oil prices is helping to ensure a soft landing.

Chart 9: UK GDP forecast

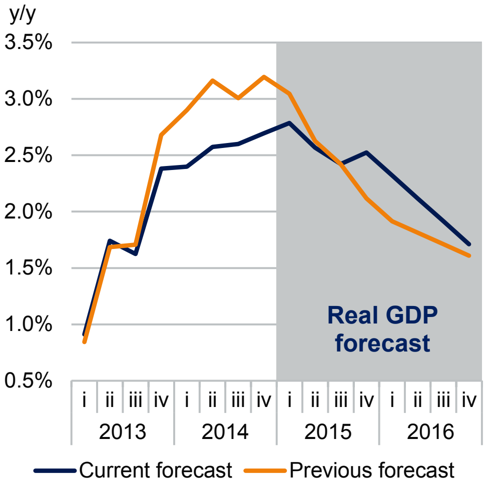
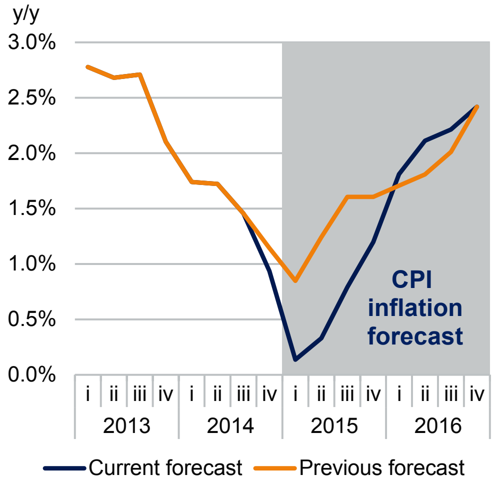


Chart 10: UK inflation forecast



Source: Thomson Datastream, Schroders. 20 February 2015. Previous forecast from November 2014. Please note the forecast warning at the back of the document.

Inflation is forecast to remain low in the near-term, but then rise faster than the BoE expects

With regards to inflation, we expect headline CPI inflation to be near zero for the coming few months, but then for it to start rising from the summer. While the Bank of England (BoE) agrees with our forecast in the near term, it assumes inflation will remain below its 2% central target for the next 2 – 3 years. We disagree and forecast above 2% inflation from the middle of 2016. This is because our analysis suggests that the output-gap (a measure of spare capacity in the economy) is largely closed. Maintaining near zero interest rates at present risks an inflation overshoot. Nevertheless, we continue to expect the BoE to start to normalise policy at the end of this year. We forecast one 25 basis point hike in November, followed by three more such hikes in 2016. However, this cautious approach in our view does not do enough to stop the inflation overshoot. Indeed, although the Bank may not publicly admit it, it would rather see a small overshoot than risk a significant cyclical downturn.

Schroder Economics Group: Views at a glance

Macro summary – February 2015

Key points

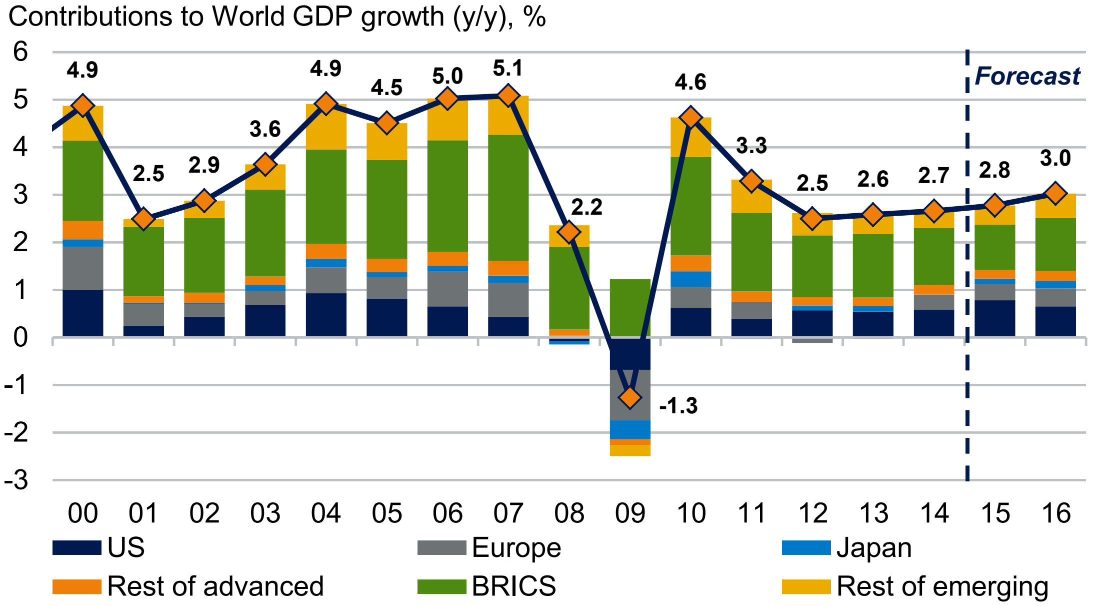
Baseline

- Global recovery to continue at modest pace as the upswing in the advanced economies is offset by slower growth in the emerging markets. Lower energy prices will push inflation in the advanced economies to its lowest level since 2009.
- US economy on a self sustaining path with unemployment set to fall below the non-accelerating rate of unemployment (NAIRU) in 2015, prompting Fed tightening. First rate rise expected in June 2015 with rates rising to 1.25% by year end. Policy rates to peak at 2.5% in 2016.
- UK recovery to moderate in 2015 with cooling housing market, political uncertainty and resumption of austerity. Interest rate normalisation to begin with first rate rise in November after the trough in CPI inflation. BoE to move cautiously with rates at 1.5% by end 2016 and peaking at around 2.5% in 2017.
- Eurozone recovery firms as fiscal austerity and credit conditions ease whilst lower euro and energy prices support activity. Inflation to remain close to zero throughout 2015, but to turn positive again in 2016. ECB to keep rates on hold and continue sovereign QE through to September 2016.
- Japanese growth supported by weaker yen, lower oil prices and absence of fiscal tightening in 2015. Momentum to be maintained in 2016 as labour market continues to tighten, but Abenomics faces considerable challenge over the medium-term to balance recovery with fiscal consolidation.
- US still leading the cycle, but Japan and Europe begin to close the gap in 2015. Dollar to remain firm as the fed tightens, but to appreciate less as ECB and BoJ policy is now largely priced in.
- Emerging economies benefit from advanced economy upswing, but tighter US monetary policy, a firm dollar and weak commodity prices weigh on growth. China growth shifting downward as the property market cools and business capex is held back by overcapacity. Further easing from the PBoC to follow.

Risks

- Risks still skewed towards deflation on fears of Eurozone deflationary spiral, China hard landing and secular stagnation. Upside growth risks on a return of animal spirits and a G7 boom, fiscal stimulus in the Eurozone and lower energy prices. Stagflationary risks centre around a further deterioration in the Russia/ Ukraine crisis culminating in a cut off in energy supply to Western Europe.

Chart: World GDP forecast



Source: Thomson Datastream, Schroders 20 February 2014 forecast. Please note the forecast warning at the back of the document.

Schroders Baseline Forecast

Real GDP

y/y%	Wt (%)	2014	2015		Prev.	Consensus	2016		Prev.	Consensus
World	100	2.7	2.8		(2.8)	2.8	3.0	↑	(2.8)	3.1
Advanced*	63.2	1.7	2.2	↑	(2.0)	2.2	2.2	↑	(2.1)	2.3
US	24.5	2.4	3.2	↑	(2.8)	3.2	2.7	↑	(2.4)	2.9
Eurozone	19.2	1.1	1.3	↑	(0.9)	1.2	1.6	↑	(1.4)	1.7
Germany	5.4	1.6	1.6	↑	(1.2)	1.5	2.0	↑	(1.8)	1.9
UK	3.9	2.6	2.6	↑	(2.5)	2.7	2.0	↑	(1.8)	2.5
Japan	7.2	0.0	1.6	↑	(1.1)	1.3	2.2		(2.2)	1.6
Total Emerging**	36.8	4.2	3.7	↓	(4.1)	3.8	4.4	↑	(4.1)	4.6
BRICs	22.6	5.3	4.2	↓	(4.8)	4.4	4.9	↑	(4.7)	5.2
China	13.5	7.4	6.8		(6.8)	7.0	6.5		(6.5)	6.9

Inflation CPI

y/y%	Wt (%)	2014	2015		Prev.	Consensus	2016		Prev.	Consensus
World	100	2.8	2.5	↓	(2.9)	2.3	3.0	↓	(3.2)	3.0
Advanced*	63.2	1.4	0.5	↓	(1.3)	0.3	1.8		(1.8)	1.7
US	24.5	1.6	0.7	↓	(1.5)	0.3	2.2	↓	(2.4)	2.3
Eurozone	19.2	0.4	0.1	↓	(0.8)	-0.1	1.2	↑	(1.1)	1.1
Germany	5.4	0.8	0.4	↓	(1.4)	0.3	1.7		(1.7)	1.6
UK	3.9	1.5	0.6	↓	(1.3)	0.6	2.1	↑	(2.0)	1.8
Japan	7.2	2.7	0.6	↓	(1.3)	0.9	1.3	↓	(1.4)	1.2
Total Emerging**	36.8	5.1	5.9	↑	(5.6)	5.8	5.0	↓	(5.6)	5.1
BRICs	22.6	4.0	4.5	↑	(4.0)	4.3	3.6	↓	(4.0)	3.7
China	13.5	2.0	1.7	↓	(2.2)	1.7	2.0	↓	(2.7)	2.1

Interest rates

% (Month of Dec)	Current	2014	2015		Prev.	Market	2016		Prev.	Market
US	0.25	0.25	1.25		(1.25)	0.84	2.50		(2.50)	1.66
UK	0.50	0.50	0.75		(0.75)	0.77	1.50		(1.50)	1.29
Eurozone	0.05	0.05	0.05		(0.05)	0.03	0.05		(0.05)	0.08
Japan	0.10	0.10	0.10		(0.10)	0.10	0.10		(0.10)	0.10
China	5.60	5.60	5.00	↓	(5.20)	-	4.50	↓	(5.00)	-

Other monetary policy

(Over year or by Dec)	Current	2014	2015		Prev.	2016		Prev.
US QE ($Bn)	4498	4498	4607	↑	(4594)	4662	↑	(4557)
EZ QE (€Bn)	0	0	600		-	1140		-
UK QE (£Bn)	375	375	375		(375)	375		(375)
JP QE (¥Tn)	300	295	383		(383)	400	↑	(383)
China RRR (%)	20.00	20.00	19.00		19.00	18.00		18.00

Key variables

FX (Month of Dec)	Current	2014	2015		Prev.	Y/Y(%)	2016		Prev.	Y/Y(%)
USD/GBP	1.54	1.56	1.50		(1.50)	-5.9	1.48		(1.48)	-3.8
USD/EUR	1.14	1.21	1.12	↓	(1.18)	-12.2	1.09	↓	(1.14)	-7.4
JPY/USD	118.7	119.9	120.0	↓	(125)	14.1	125.0	↓	(130)	0.1
GBP/EUR	0.74	0.78	0.75	↓	(0.79)	-6.7	0.74	↓	(0.77)	-3.8
RMB/USD	6.24	6.20	6.30	↑	(6.20)	2.5	6.40	↑	(6.35)	1.5
Commodities (over year)										
Brent Crude	60.7	55.8	61.6	↓	(82)	-49.9	69.7	↓	(86)	10.3

Source: Schroders, Thomson Datastream, Consensus Economics, February 2015
Consensus inflation numbers for Emerging Markets is for end of period, and is not directly comparable.
Market data as at 13/02/2015
Previous forecast refers to November 2014

* **Advanced markets:** Australia, Canada, Denmark, Euro area, Israel, Japan, New Zealand, Singapore, Sweden, Switzerland, Sweden, Switzerland, United Kingdom, United States.

** **Emerging markets:** Argentina, Brazil, Chile, Colombia, Mexico, Peru, Venezuela, China, India, Indonesia, Malaysia, Philippines, South Korea, Taiwan, Thailand, South Africa, Russia, Czech Rep., Hungary, Poland, Romania, Turkey, Ukraine, Bulgaria, Croatia, Latvia, Lithuania.

Schroders Forecast Scenarios

Scenario	Summary	Macro impact	Probability*	Global vs. 2015 baseline Growth	Inflation
Baseline	An increase in our projection for the Advanced economies is offset by a cut to the Emerging markets to leave our global growth forecast at 2.8% for 2015. US growth is expected to reach 3.2% this year, the best performance for 10 years as the benefits of lower oil prices feed through to consumers and business. Europe and Japan also gain from cheap oil and a more competitive currency. However, at the global level the boost to growth from lower oil prices is largely offset by continuing structural headwinds in the emerging world particularly strength in the USD. Our China forecast is unchanged as we balance the positives of better external demand and looser monetary policy against the ongoing weakness in housing and capex. Forecasts for Brazil and Russia have been cut to reflect domestic problems with the latter becoming increasingly isolated from the world economy. For 2016, US growth moderates as the boost from oil fades and higher interest rates and a stronger USD begin to weigh on growth. However, the overall global growth forecast ticks up to 3% next year on further improvement in Europe and Japan as well as continued strength from India.	Our inflation forecasts have been cut in response to lower than expected out turns in recent months and the further fall in oil prices. Global inflation is expected to come in at 2.5% for 2015 with a significant reduction for the Advanced economies to 0.5% from 1.4% in 2014 as falling energy prices impact on CPI inflation. The US Fed is still expected to look through this fall and focus on a stable core rate of inflation and tightening labour market so as to raise rates in 2015. We expect the Fed funds rate to rise to 1.25% by end 2015 and then peak at 2.5% in 2016. Deflation concerns in the Eurozone are expected to ease as inflation picks up in 2016 thanks to the depressing effect of lower oil prices dropping out of the index. We expect the ECB to implement QE through to September 2016 and leave rates on hold, whilst for the UK, we stick with our call for the first rate hike in November 2015. In Japan, the BoJ will keep the threat of more QQE on the table, but is now likely to let the weaker JPY support the economy and refrain from further loosening. China is expected to cut interest rates and the RRR further and pursue other means of stimulating activity in selected sectors.	65%	-	-
1. EZ deflationary spiral	Despite the best efforts of Mario Draghi and the ECB, weak economic activity weighs on Eurozone prices with the region slipping into deflation. Households and companies lower their inflation expectations and start to delay spending with the expectation that prices will fall further. The rise in savings rates deepens the downturn in demand and prices, thus reinforcing the fall in inflation expectations. Falling nominal GDP makes debt reduction more difficult, further depressing activity particularly in the heavily indebted peripheral economies.	Deflationary: weaker growth and lower inflation persists throughout the scenario. ECB reacts by cutting interest rates below zero and continuing QE, but the policy response is too little, too late. As a significant part of the world economy (around one-fifth), Eurozone weakness drags on activity elsewhere, while the deflationary impact is also imported by trade partners through a weaker Euro. Global growth and inflation are about 0.5% weaker this year and 1% weaker in 2016 compared to the baseline.	4%	-0.6%	-0.6%
2. G7 boom	After a prolonged period of balance sheet repair, animal spirits return to the private sector which finally responds to ultra-loose monetary policy and the gains in asset prices. Advanced economy growth picks up more rapidly than in the base as the corporate sector increases capex and consumers spend more rapidly as banks increase lending. Stronger G7 demand spills over to the emerging markets taking global growth above 4% in 2016. Labour markets tighten more rapidly and commodity prices increase relative to the base resulting in a pick-up in inflation.	Reflationary: stronger growth and inflation vs. baseline. Central banks respond to the increase in inflationary pressure with the fastest response coming from the US and UK which are more advanced in the cycle compared with the Eurozone where there is considerable slack. Although there is little slack in Japan, higher wage and price inflation is welcomed as the economy approaches its 2% inflation target. This is likely to lead the BoJ to signal a tapering of QQE, but no change in interest rates. Inflation concerns result in tighter monetary policy in the emerging markets with China and India raising rates in 2016. The US Fed starts to actively unwind QE by reducing its balance sheet.	4%	+0.8%	+0.5%
3. Oil lower for longer	Saudi Arabia becomes frustrated at the slow response of US oil production and drives prices lower in a determined effort to make a permanent impact on US shale producers. Given the flexibility of the latter this means a significant period of low prices with Brent crude falling to $30 by end 2015 and remaining there through 2016.	Better growth/ lower inflation with the benefits primarily felt in the oil consuming Advanced economies. For the emerging economies , activity is only marginally better as gains and losses roughly offset one another although China and India are net winners. On the policy front, lower inflation allows the Fed to move slightly less rapidly, but interest rates still rise. The rate profile is also slightly lower in Chian, Brazil and India, but Russia has to keep policy tighter to stabilise the currency. No change in the Eurozone or Japan where policymakers balance lower inflation against stronger growth.	4%	+0.2%	-0.4%
4. Secular stagnation	Weak demand weighs on global growth as households and corporates are reluctant to spend. Animal spirits remain subdued and capex and innovation depressed. Households prefer to de-lever rather than borrow. Adjustment is slow with over capacity persisting around the world, particularly in China, with the result that commodity prices and inflation are also depressed.	Deflationary: weaker growth and inflation vs. baseline. Although not as deflationary as China hard landing or the Eurozone deflationary spiral the world economy experiences a slow grind lower in activity. As the effect from secular stagnation is more of a chronic than acute condition, this does not prevent policy makers from initially raising rates in the US although this is then reversed as it becomes apparent that the economy is losing momentum. Overall, global interest rates are lower than in the base and we would expect the ECB and BoJ to prolong their QE programmes.	5%	-0.4%	-0.2%
5. China hard landing	Official efforts to deliver a soft landing in China's housing market fail and house prices collapse. Housing investment slumps and household consumption is weakened by the loss of wealth. Losses at housing developers increase NPL's, resulting in a retrenchment by the banking system and a further contraction in credit and activity.	Deflationary: Global growth slows as China demand weakens with commodity producers hit hardest. However, the fall in commodity prices will push down inflation to the benefit of consumers. Monetary policy is likely to ease/ stay on hold while the deflationary shock works through the world economy.	6%	-1.0%	-0.8%
6. Russian rumble	Despite the "ceasefire", fighting continues in East Ukraine between government forces and rebels supported by Russian troops. Putin continues to supply the rebels and the West retaliates by sending weapons to the Ukraine army and significantly increasing sanctions. Russia responds by cutting gas and oil supplies to Europe. The shortage of energy pushes oil prices back to $90 p/bbl in short order.	Stagflationary. Europe is hit by the disruption to energy supply resulting in a fall in output whilst alternative sources are put in place. Higher oil prices hit global inflation and the breakdown of relations between Russia and the west damages household and business confidence and creates significant volatility in financial markets. Policy rates are considerably lower as central banks wish to avoid damaging confidence further and look through the rise in inflation.	6%	-0.5%	+0.6%
7. EZ abandons austerity	Disappointment with the results of austerity and fearful of a growing political backlash the Eurozone reverses course. Governments ease fiscal policy significantly, increasing spending and cutting taxes whilst the EU fully implements the €300bn Juncker plan of public-private infrastructure spending.	Reflationary: stronger growth and inflation vs. baseline. Eurozone growth picks up sharply and the increase in demand supports growth in developed and emerging markets. As the EZ's largest trading partner, UK GDP growth accelerates to over 3% whilst overall global growth is some 0.4% higher. Commodity prices and inflation are marginally higher but less so than in the G7 boom as the increase in activity is concentrated on the region with the most slack in the world economy. Policy rates are marginally higher, although not in the EZ or Japan. However the ECB is likely to end QE after September 2016 in this scenario.	3%	+0.4%	+0.2%
8. Other			3%	-	-

*Scenario probabilities are based on mutually exclusive scenarios. Please note the forecast warning at the back of the document.

Updated forecast charts – Consensus Economics

For the EM, EM Asia and Pacific ex Japan, growth and inflation forecasts are GDP weighted and calculated using Consensus Economics forecasts of individual countries.

Chart A: GDP consensus forecasts

2015 | **2016**

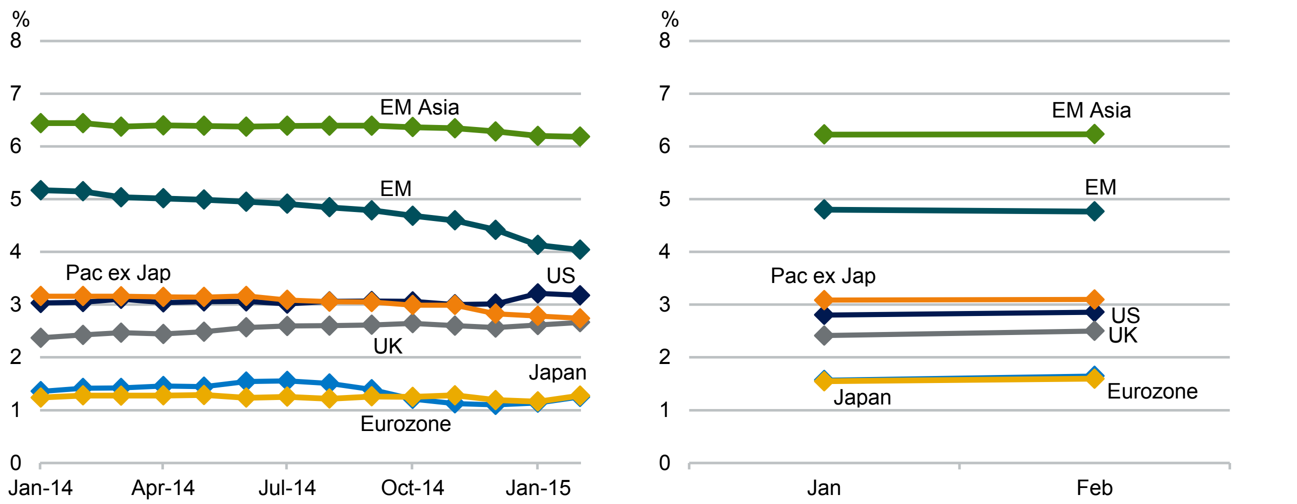
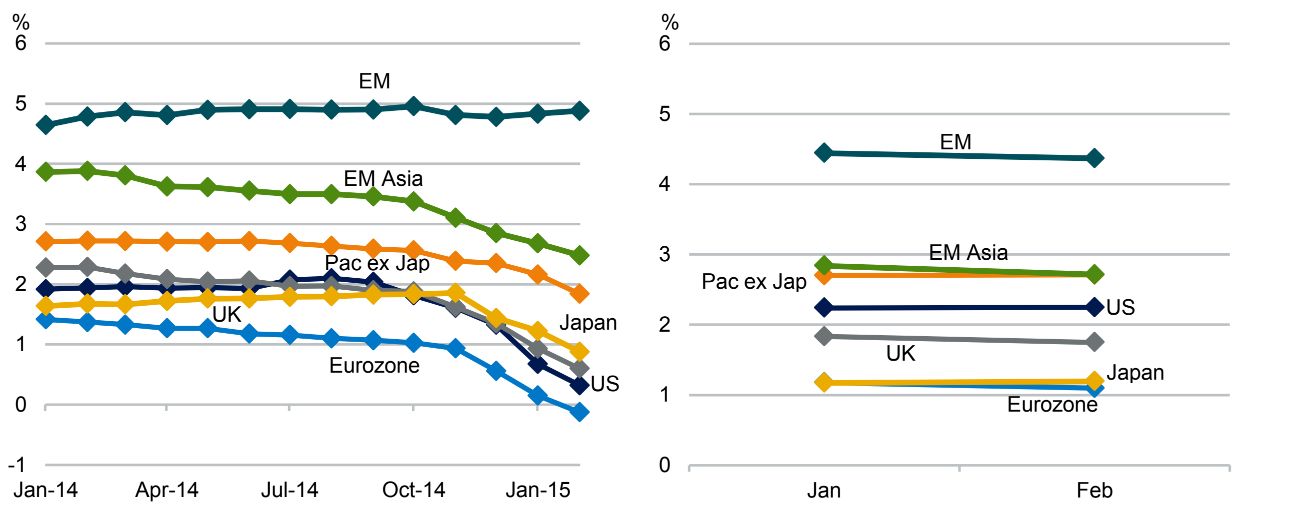


Chart B: Inflation consensus forecasts

2015 | **2016**



Source: Consensus Economics (February 2014), Schroders
Pacific ex. Japan: Australia, Hong Kong, New Zealand, Singapore
Emerging Asia: China, India, Indonesia, Malaysia, Philippines, South Korea, Taiwan, Thailand
Emerging markets: China, India, Indonesia, Malaysia, Philippines, South Korea, Taiwan, Thailand, Argentina, Brazil, Colombia, Chile, Mexico, Peru, Venezuela, South Africa, Czech Republic, Hungary, Poland, Romania, Russia, Turkey, Ukraine, Bulgaria, Croatia, Estonia, Latvia, Lithuania