

M&G YouGov Inflation Expectations Survey

Q2 2015

The results of the M&G YouGov Inflation Expectations Survey carried out in May 2015 reveal that consumers' inflation expectations continue to moderate in the UK, although they were relatively stable in most parts of Europe. With European inflation picking up in recent months, short-term price expectations crept up in Germany and Switzerland, although there was a notable dip in Spain. Elsewhere, consumers in Hong Kong reported a marked increase in short-term expectations, whilst the long-term gauge was unchanged at 5.0%. Despite the current lack of inflationary pressures, all countries still expect inflation to reach 2% or higher in five years' time.

Chart 1

Inflation expectations 1 year ahead (%)

	Austria	France	Germany	Hong Kong	Italy	Singapore	Spain	Switzerland	UK
Feb 13	N/A	2.5	2.5	5.0	3.0	4.6	3.3	1.2	3.0
May 13	2.8	2.0	2.2	5.0	3.0	4.0	3.0	1.5	2.7
Aug 13	3.0	2.0	2.3	5.0	3.0	3.7	2.8	1.4	3.0
Nov 13	2.3	2.0	2.1	5.0	2.5	4.0	2.0	1.2	2.8
Feb 14	2.0	2.0	2.3	4.6	2.0	3.4	2.0	1.2	2.0
May 14	2.3	2.0	2.0	4.6	2.0	3.6	2.0	1.1	2.3
Aug 14	2.3	1.0	2.0	4.0	2.0	3.5	2.0	1.3	2.2
Nov 14	2.0	1.5	2.0	4.7	2.0	3.0	1.8	1.2	2.0
Feb 15	2.0	1.3	1.9	4.0	2.0	3.0	2.0	1.0	1.5
May 15	2.0	1.2	2.0	5.0	2.0	3.0	1.5	1.2	1.2

Inflation expectations 5 years ahead (%)

	Austria	France	Germany	Hong Kong	Italy	Singapore	Spain	Switzerland	UK
Feb 13	N/A	4.0	3.5	5.0	3.3	5.0	4.0	2.5	3.0
May 13	3.0	3.0	3.0	5.8	3.0	5.0	3.0	2.6	3.0
Aug 13	3.5	3.0	3.3	5.0	3.3	5.0	3.1	2.8	3.0
Nov 13	3.0	3.0	3.0	5.5	3.0	5.0	2.5	2.5	3.0
Feb 14	3.0	2.5	3.0	5.0	2.5	5.0	2.5	2.5	3.0
May 14	3.2	3.0	3.0	5.4	3.0	5.0	3.0	2.5	3.0
Aug 14	3.0	2.0	3.0	5.0	2.5	4.6	3.0	2.2	3.0
Nov 14	3.0	2.5	3.0	5.0	3.0	5.0	2.5	2.5	3.0
Feb 15	3.0	2.0	3.0	5.0	2.5	4.5	2.8	2.0	3.0
May 15	3.0	2.0	3.0	5.0	2.5	4.0	2.5	2.6	2.5

The inflation figures in this report reference the Harmonised Index of Consumer Prices/Consumer Prices Index as at the end of April 2015. Source: Bloomberg, 9 June 2015.



M&G YouGov Inflation Expectations Survey

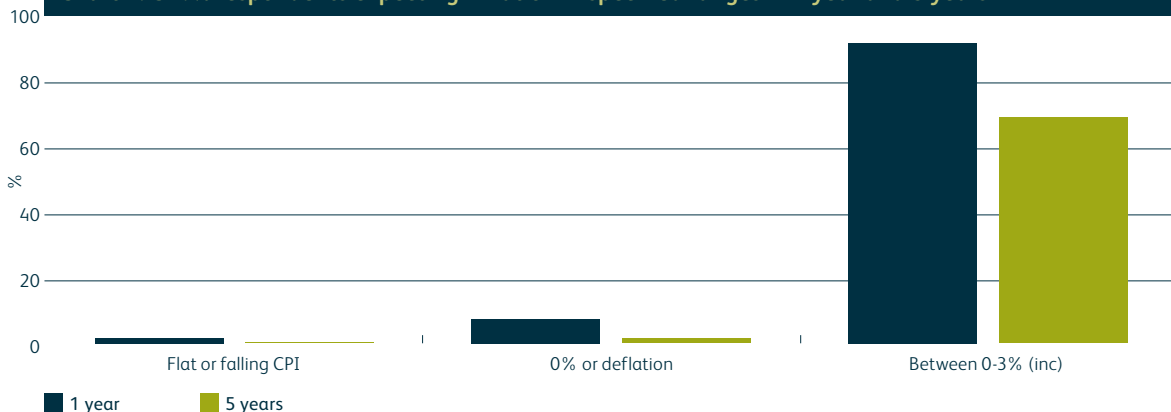
United Kingdom

Inflation expectations in the UK have moderated over both the short and the long term in the second quarter of 2015. Median expectations for one year ahead now stand at 1.2%, having edged down from 1.5% in the previous quarter. Interestingly, short-term expectations for the London area have fallen by a greater amount than the national average and currently stand at just 1.0%. Over five years, UK consumers expect average inflation to climb to 2.5%, which may provide some comfort for policymakers at the Bank of England. That said, both the one- and five-year readings are at the lowest level since

the M&G YouGov Inflation Expectations survey began in February 2013.

Despite headline inflation in the UK recently falling into negative territory, consumers do not appear to be expecting this to persist. Rather, consumers' expectations are becoming increasingly clustered around the likelihood of low but positive inflation over the coming years. For example, the share of people* who expect prices to rise by more than zero but less than 3% over one year is 93%, and 70% over five years.

Chart 2: UK: % respondents expecting inflation in specified ranges in 1 year and 5 years



Confidence in central bank monetary policy was shown to be the highest since the survey began. One in every two consumers (51%) reported that they were either very or fairly confident that the Bank of England will deliver on price stability over the medium term. Indeed, while short-term inflation expectations have fallen over the past 12 months, they remain far away from deflationary territory, and continue to be above the Bank's inflation target over the long term.

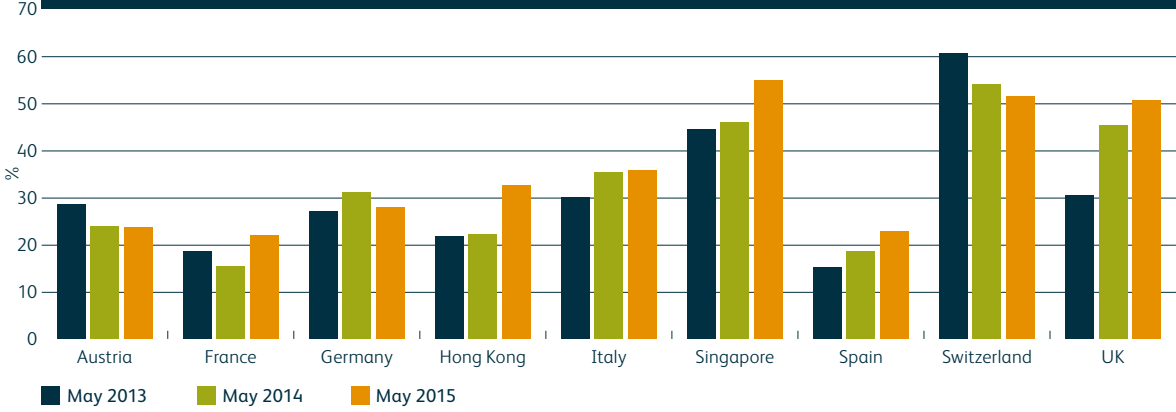
A combination of lower inflation expectations and a gradual pick-up in wage growth is likely to

support consumer spending going forward. In fact, survey results suggest that 73% of Britons expect their net income to rise or stay the same over the next 12 months. Confidence in the newly elected government is also the highest on record with 42% of respondents agreeing, or strongly agreeing, that the correct economic policies are being followed. This number has almost doubled since February 2013, when only 23% of respondents approved of the government's economic policies.

*Figure excludes "don't know" answers.

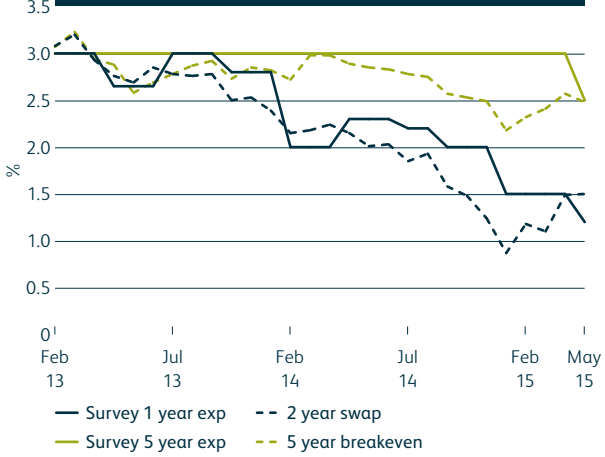


Chart 3: % respondents who are very or fairly confident towards their Central Bank



Comparing the survey responses to market-based inflation expectations (chart 4) reveals an interesting comparison. Whilst consumer forecasts have edged down in recent months, market-based measures are moving in the opposite direction and are starting to price in higher inflation over the coming years.

Chart 4: UK inflation: consumer expectations vs market based measures



Europe

Within Europe, inflation is showing signs of life with eurozone CPI rising to 0.0% in April, after five months of negative inflation figures. The inflation uptick is likely to come as welcome news for European policymakers, reviving hopes of economic recovery in the region. While headline inflation remains low by historical standards, the increase was stronger than expected and suggests the European Central Bank's (ECB) monetary policy programme might be starting to have an impact.

Although inflation expectations were broadly stable compared with the previous survey, short-term expectations in **Germany** marginally increased to 2.0% this quarter. German inflation accelerated to 0.3% in April, while increased levels

of consumer confidence (currently at eight-year highs), together with the new national minimum wage, could potentially push consumer prices higher over the medium term.

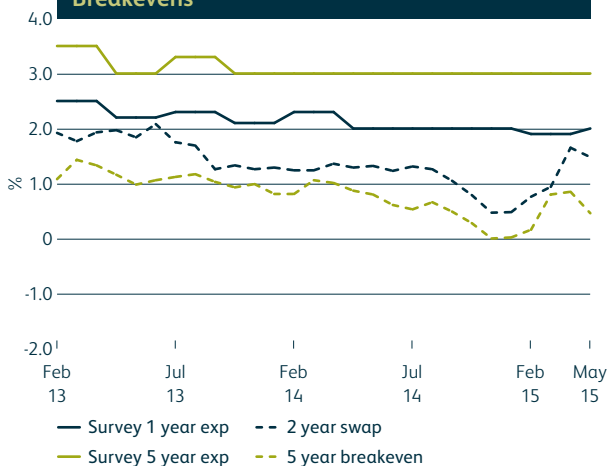
Germans have positive expectations (21%) for net annual income growth, although they continue show a high level of concern (33%) about the detrimental impact of rising inflation.

Comparing the survey responses to market-based inflation expectations (chart 5), it is evident that consumers' forecast for inflation have remained remarkably stable over both one- and five-years ahead. It appears that German consumers perceive current low inflation levels as temporary and remain confident that the ECB will deliver price stability.



M&G YouGov Inflation Expectations Survey

Chart 5: German Expectations vs Breakevens

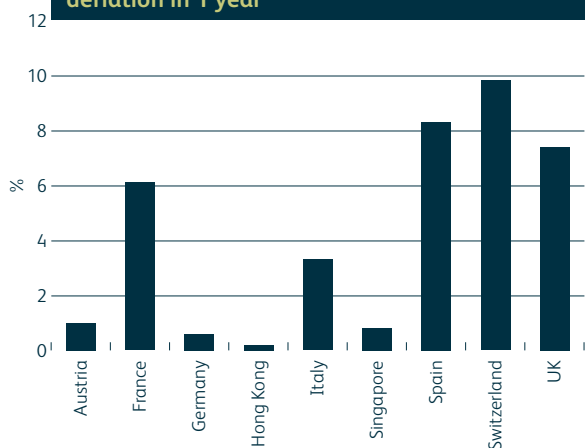


In **Switzerland**, short-term consumer inflation expectations also increased compared with the previous survey, rising from 1.0% to 1.2% over one year, and from 2.0% to 2.6% over five years.

These results might be surprising considering Switzerland is experiencing its longest run of falling prices in two years with annual inflation running at -1.1% in April. The Swiss franc has gained more than 15% versus the euro since mid-January, when the Swiss National Bank removed its euro peg. That has pushed down the prices of imported goods, while making the Swiss export market less competitive in the neighbouring euro area. Unless the currency depreciates markedly, this trend could well persist in the coming quarters.

Despite the recent spell of deflation, 30% of Swiss respondents report rising inflation as a cause for concerns. However, at the other end of the spectrum, around 10% of Swiss consumers expect either deflation or zero inflation over the next year.

Chart 6: Expectations of 0% inflation or deflation in 1 year



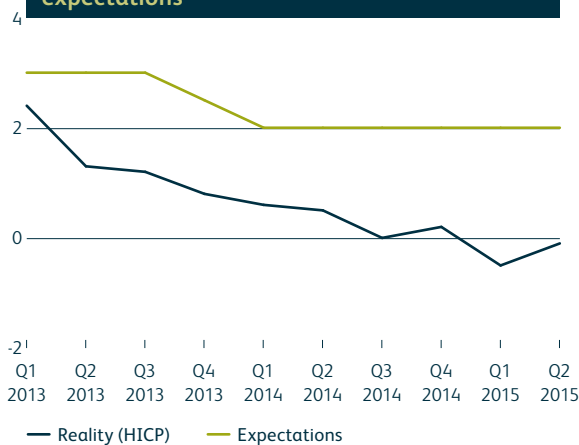
In Southern Europe, **Spain** experienced the most pronounced quarterly change, with expectations dropping from 2.0% to 1.5% over one year, and 2.8% to 2.5% over five years. **Italian** forecasts remained unchanged over both the short (2.0%) and long term (2.5%).

Nevertheless, Spanish and Italian consumers appear to remain relatively optimistic on short-term inflationary pressures, with little sign that a deflationary mentality is taking hold in either of these counties. Charts 7 and 8 show that, despite negative inflation in Spain (-0.7%) and Italy (-0.1%), expectations for inflation have remained relatively resilient.

Chart 7: Spain – current CPI vs 1 year expectations



Chart 8: Italy – current CPI vs 1 year expectations





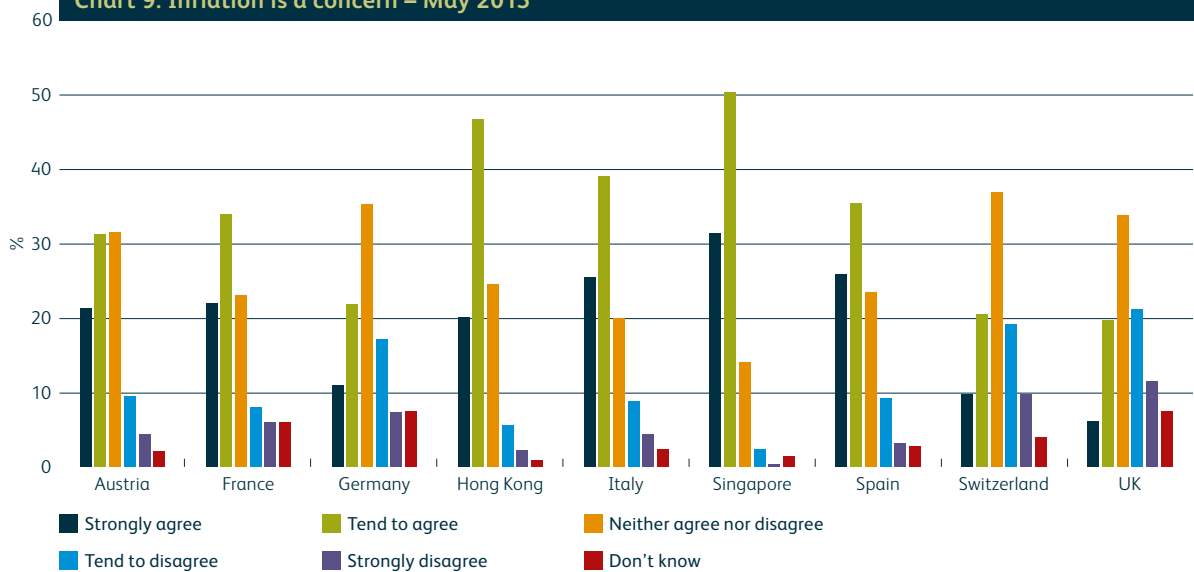
Support for government economic policy remains poor in both countries. Our analysis shows that 58% of respondents in Spain, and 56% in Italy, disagree with their government's economic policy. The highest level of disagreement in Spain was observed in those aged 18 to 24 (65%) with youth unemployment in excess of 50%, it is doubtful whether sentiment amongst this age group can improve in any meaningful way ahead of the upcoming elections.

In **Asia**, Hong Kong consumers' inflation expectations over the short term have risen firmly from 4.0% to 5.0%. This result might also seem surprising given the recent dip in CPI, which fell to 2.8% in April compared to 4.5% March. Despite the lower CPI reading, home prices in

Hong Kong continue to rise to record highs and, unless interest rates are increased, analysts expect inflation to bounce back later in the year. Perhaps for this reason, 67% of Hong Kong consumers reported concern over rising inflation (chart 9).

In Singapore, households appear to have become less worried about long-term inflation, with long-term expectations falling from 4.5% to 4.0% this quarter. Lower oil prices and fluctuating exchange rates may have had some downward impact on consumers' expectations. Confidence in central bank policy was modestly higher with 55% of Singaporeans declaring they are "very" or "fairly" confident that the correct policies are being pursued to deliver price stability over the medium term.

Chart 9: Inflation is a concern – May 2015





M&G YouGov Inflation Expectations Survey

Other highlights of the survey include:

- **Singapore** is the country with the greatest confidence in its government economic policy (49%) and central bank monetary policy (55%). Confidence levels have grown in recent quarters (chart 10).
- **The UK** has experienced the largest positive change in government confidence over the past year, with a 6% uplift in support of the government's economic policies compared to the previous survey.
- **Austria** recorded a fall in confidence in the ECB, with 70% of respondents reported to be not very, or not at all, confident that the right monetary policies were being followed. Spain followed closely behind, with 69% of consumers reporting a lack of confidence in the ECB.
- **French** consumers remain the most pessimistic about their household finances, with 41% of respondents expecting their net income to decrease over the next year.

Chart 10: % respondents who are very or fairly confident towards their government's economic policies

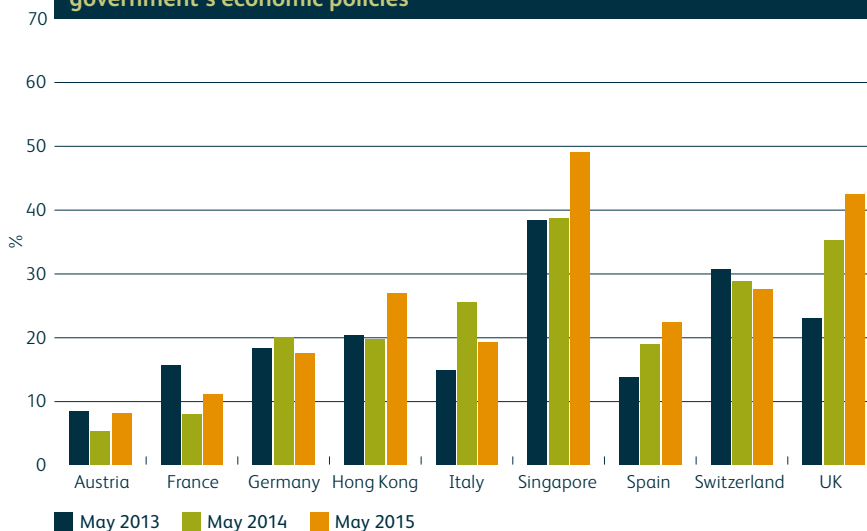
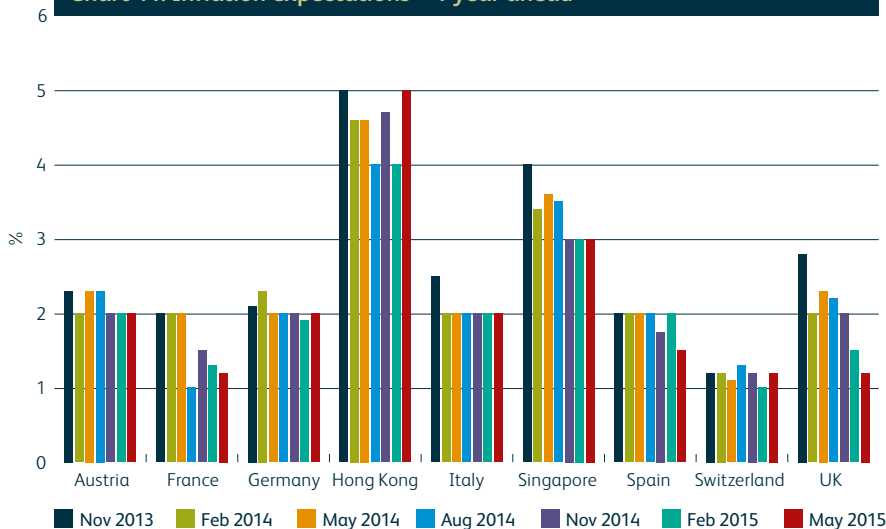


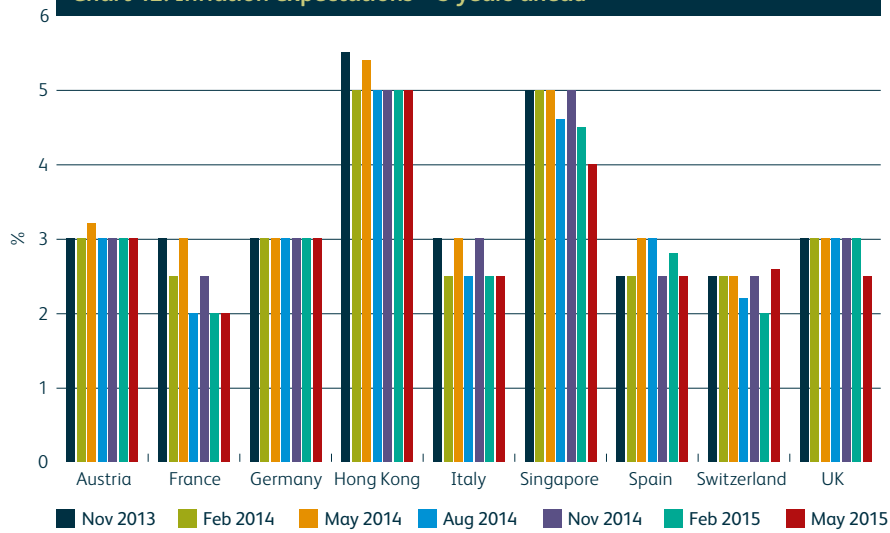
Chart 11: Inflation expectations – 1 year ahead



Consumers in Germany, Hong Kong and Switzerland reported a rise of inflation expectations in the short term.

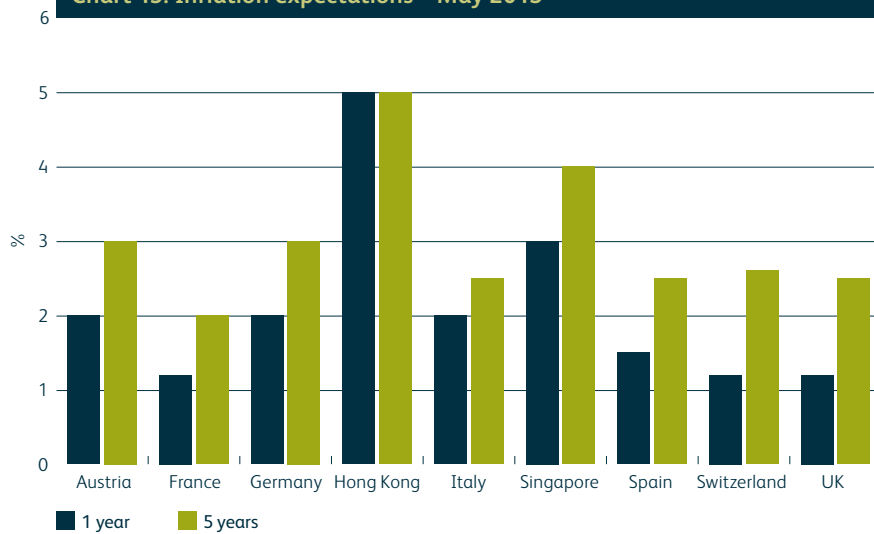


Chart 12: Inflation expectations – 5 years ahead



Consumer 5-year inflation expectations remain at or above central bank targets in most countries.

Chart 13: Inflation expectations – May 2015



In Europe, long-term inflation expectations remain at or above the Bank of England, Swiss National Bank and European Central Bank's inflation targets.

8 Statistical Appendix

Surveys conducted between 26 May – 1 June 2015

1. What annual rate of inflation do you expect 12 months from now?

	Sample size	Mode	Median	25th percentile	75th percentile	Interquartile range (75th-25th)	Don't know responses
London	291	1.0	1.0	0.5	2.0	1.5	43.3%
UK	2,089	1.0	1.2	0.7	2.0	1.3	40.7%
France	1,003	1.0	1.2	0.8	2.5	1.7	47.9%
Germany	1,027	2.0	2.0	1.2	3.3	2.1	37.3%
Italy	1,010	1.0	2.0	1.0	4.0	3.0	37.6%
Spain	1,006	1.0	1.5	1.0	3.0	2.0	35.3%
Austria	500	2.0	2.0	1.8	3.0	1.2	39.6%
Switzerland	501	1.0	1.2	0.6	2.6	2.0	39.1%
Hong Kong	506	5.0	5.0	3.5	5.5	2.0	14.8%
Singapore	501	3.0	3.0	2.0	5.0	3.0	20.6%

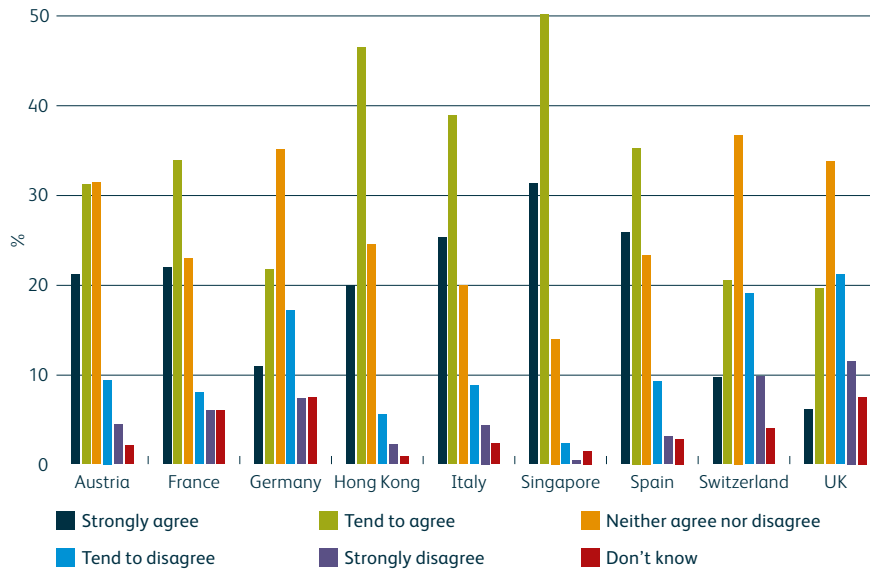
2. What annual rate of inflation do you expect five years from now?

	Sample size	Mode	Median	25th percentile	75th percentile	Interquartile range (75th-25th)	Don't know responses
London	291	2.0	2.5	2.0	3.5	1.5	50.9%
UK	2,089	2.0	2.5	2.0	4.0	2.0	45.9%
France	1,003	1.0	2.0	1.0	4.5	3.5	53.4%
Germany	1,027	2.0	3.0	2.0	5.0	3.0	42.4%
Italy	1,010	2.0	2.5	1.5	5.0	3.5	41.0%
Spain	1,006	2.0	2.5	1.5	5.0	3.5	38.9%
Austria	500	2.0	3.0	2.0	5.0	3.0	38.8%
Switzerland	501	3.0	2.6	1.1	5.0	3.9	41.7%
Hong Kong	506	5.0	5.0	4.0	10.0	6.0	17.2%
Singapore	501	3.0	4.0	3.0	6.0	3.0	20.8%



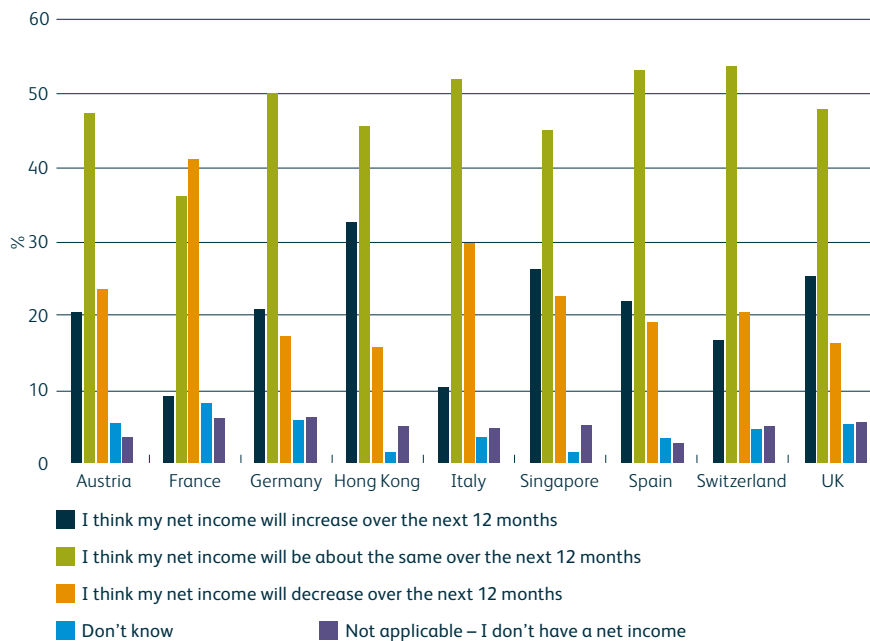
3. To what extent do you agree or disagree with the following statement?

“Rising inflation is giving me and my family cause for concern at the moment.”



In the UK, a decreasing number of people (26%) regard rising inflation as a current concern for them and their families.

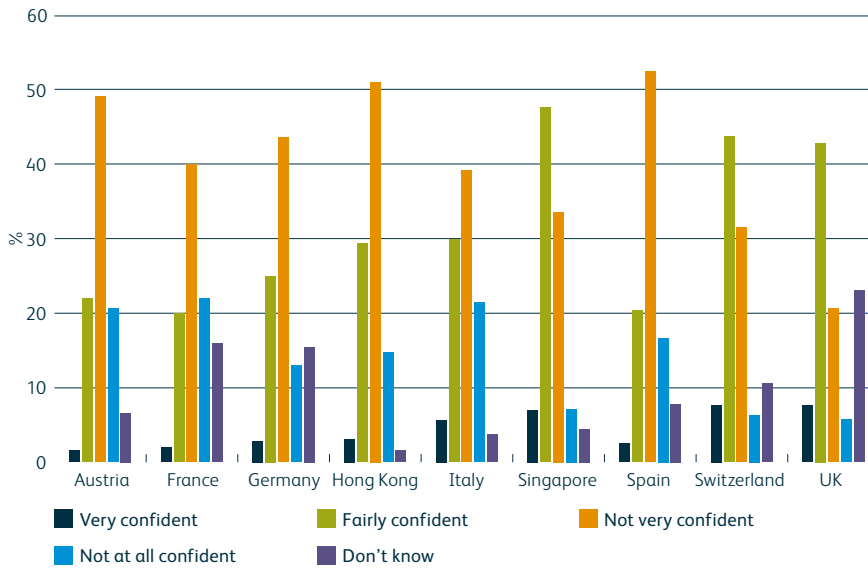
4. Thinking about the next 12 months – do you expect your net income to increase, decrease or be about the same in 12 months' time?



In the eurozone, the Spanish were shown to have the highest expectations (22%) for net annual income growth.

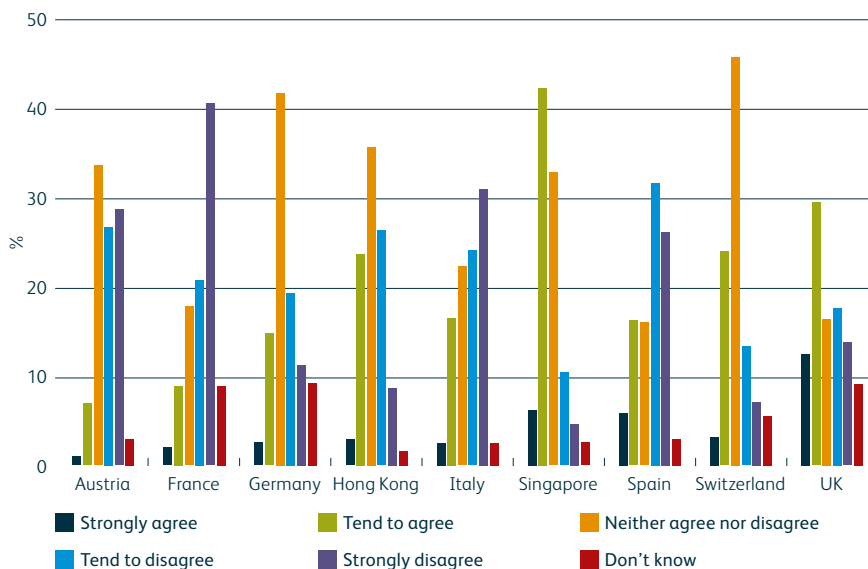


5. How confident, if at all, are you that your central bank is currently pursuing the correct policies in order to meet its target of price stability (ie inflation around 2%) over the medium term (ie the next 3-5 years)?



Just over one in two (55%) Singaporeans declare they are “very” or “fairly” confident that the Monetary Authority of Singapore is currently pursuing the correct policies to achieve price stability over the medium term.

6. To what extent do you agree or disagree with the following statement: “I think that my government is currently following the right economic policies.”



In Spain, support for government economic policy remains poor. Our analysis shows that 26% of respondents strongly disagree with government economic policy.

All figures, unless otherwise stated, are from YouGov Plc. Total sample size for each country was Austria (500), France (1,003), Germany (1,027), Hong Kong (506), Italy (1,010), Singapore (501), Spain (1,006), Switzerland (501), UK (2,089) adults. Fieldwork was undertaken between 26 May – 1 June 2015. The survey was carried out online. The figures have been weighted and are representative of all adults in each country (aged 18+).



Inflation expectations methodology



M&G's Retail Fixed Interest team analyse the statistics for the answers to the first and second questions in the survey (ie, the expected annual inflation rates in 12 months and five years from now). To achieve this, all answers are first ranked in ascending order, and several percentiles are subsequently determined. In this context, percentiles are expected inflation rates below which a certain percentage of responses can be found. For instance, the 50th percentile, the so-called median, is the middle value of the distribution, dividing the data set into a lower and an upper 50%. If there is an even number of values, the median is determined by calculating the average of the two middle values. In the statistical analysis of the survey, we have chosen to use the median rather than the arithmetic

mean because this is less affected by extreme values. To determine the dispersion of answers, the difference between the 75th and 25th percentiles is taken. Finally, the number of 'don't know' responses is divided by the total number of responses and the resultant percentage is recorded as an indicator of respondents' level of uncertainty around inflation. Data processing for the remaining questions (three to six) is conducted by YouGov. Here, percentage values are calculated for each answer option by dividing the number of respective responses by the total number of responses.

The content of this report should not be regarded as a recommendation, advice or forecast regarding inflation expectations.



Who is YouGov?

YouGov is an international market research agency with sector specialist teams serving the financial, media, technology and telecom industries. They are considered a pioneer of online market research and are the most quoted market research agency in the UK. In August 2012, they were named as one of the world's top 25 research companies by the Honomichi Top 25 Global Firms.

For quantitative research, YouGov uses an online panel of adults, who are profiled across a range of demographic, attitudinal, lifestyle and marketing characteristics. The emphasis is put on quality rather than quantity and restrictions are put in place to ensure that only those selected from this panel are able to take part in the survey.

Incentives are used to encourage participation and prevent an overwhelming influence from those with a particular interest or 'axe to grind'. In the UK, France and Germany, the panels are constructed by YouGov and consist of 654,000, 127,000 and 178,000 adults respectively. In the other countries, a panel partner of YouGov conducts the survey using an online interview. The panel sizes for these countries are as follows: Austria (25,544), Hong Kong (14,444), Italy (75,201), Singapore (21,399), Spain (130,312) and Switzerland (21,684).

For qualitative research, they use online forums, face to face focus groups and cognitive interviews. This information is then either used stand alone or is fully integrated with their quantitative research.

Once collected, the data is weighted using either each country's census, if available, or industry accepted data, to help make the sample as reflective of the general population as possible.



For Investment Professionals only. Not for onward distribution. No other persons should rely on any information contained within. For Switzerland: Distribution of this document in or from Switzerland is not permissible with the exception of the distribution to Qualified Investors according to the Swiss Collective Investment Schemes Act, the Swiss Collective Investment Schemes Ordinance and the respective Circular issued by the Swiss supervisory authority ("Qualified Investors"). Supplied for the use by the initial recipient (provided it is a Qualified Investor) only. This financial promotion is issued by M&G Securities Limited (registered in England 90776) and M&G International Investments Ltd. Both are authorised and regulated by the Financial Conduct Authority in the UK and have their registered offices at Laurence Pountney Hill, London EC4R 0HH. M&G International Investments Ltd is registered in England, No. 4134655. It also has a branch located in France, 6 rue Lamennais, Paris 75008, registered on the Trade Register of Paris, No. 499 832 400 and a branch in Spain, with corporate domicile at Plaza de Colón 2, Torre II, Planta 14, 28046, Madrid, Spain, registered with the Commercial Registry of Madrid under Volume 32.573, sheet 30, page M-586297, inscription 1, CIF W8264591B and registered with the CNMV under the number 79. The Portuguese Securities Market Commission (Comissão do Mercado de Valores Mobiliários, the "CMVM") has received a passporting notification under Directive 2009/65/EC of the European Parliament and of the Council and the Commission Regulation (EU) 584/2010 enabling the funds to be distributed to the public in Portugal. M&G International Limited is duly passported into Portugal to provide certain investment services in such jurisdiction on a cross-border basis and is registered for such purposes with the CMVM and is therefore authorised to conduct the marketing (comercialização) of funds in Portugal. In Switzerland, this financial promotion is created by M&G Securities Limited and published by M&G International Investments Switzerland AG, Bahnhofstrasse 100, 8001 Zurich, authorised and regulated by the Swiss Federal Financial Market Supervisory Authority. JUN 15 / W54501