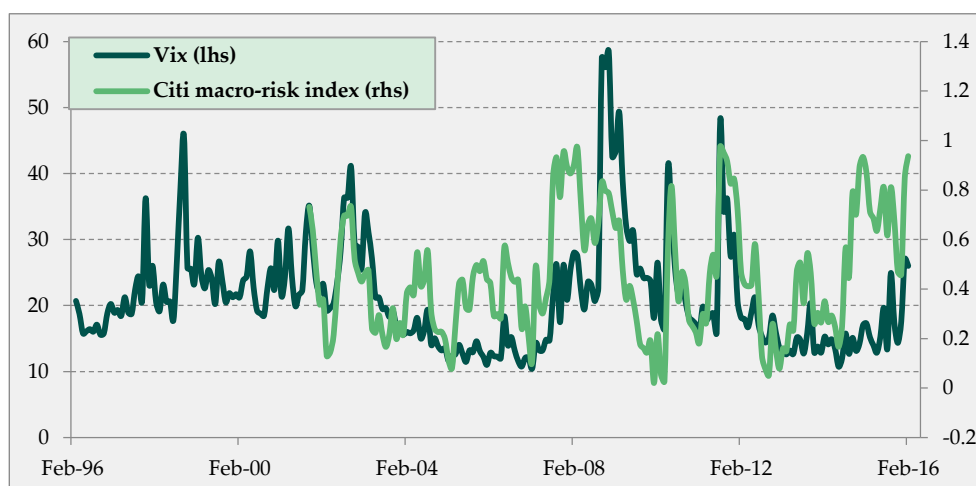


- For quite some time now financial markets are seeing lots of volatility. Investors seem to be worrying about several different factors at the same time including China's slowdown and its impact on emerging markets, clear signs of hesitation in the US economy, the non-linear fall in oil prices and its disruptive effects, geopolitical risks and the handling of the European refugee crisis, uncertainty linked to future monetary policy as well as its effectiveness to boost demand, stretched equity market valuations, high private and public debt levels and so on. Importantly, the latest market turmoil is not only about China.

Risk aversion remains high

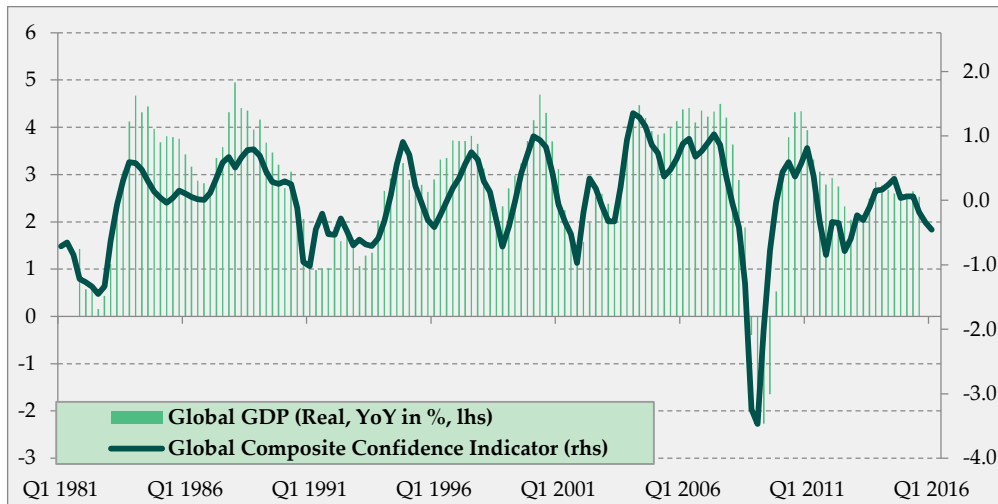


CitiMacro Risk Index is an equally weighted index of emerging market sovereign spreads, US credit spreads, US swap spreads and implied FX, equity and swap rate volatility. The index is expressed in a rolling historical percentile and ranges between 0 (low risk aversion) and 1 (high risk aversion)

Source : Datstream. Degroof Petercam

- It's widely accepted that a severe economic crisis in China is one of the most important risks again for this year. Our scenario that China will avoid a hard landing in 2016 remains in place even though the challenges that stem from rebalancing the economy loom large and hard landing fears are likely to continue to linger around. (<https://insights.petercam.com/emerging-markets/crossing-the-chinese-river>)
- Downward risks remain substantial but we believe economic activity will not fall of a cliff against the back of loose monetary and budgetary policy and also lower energy prices. That said, our global composite confidence indicator shows clear signs of hesitation and downward risks prevail.
- Despite the general very low level of commodity prices, base effects will send headline inflation higher in late 2016. Core inflationary pressures look set to remain modest, implying that global monetary policy will stay very loose in the foreseeable future.
- The USD has appreciated significantly since the summer of 2014 and this has come with serious challenges. (<https://insights.petercam.com/developed-markets/more-thoughts-on-the-state-of-the-world-economy>).

Clear signs of hesitation in global economic activity



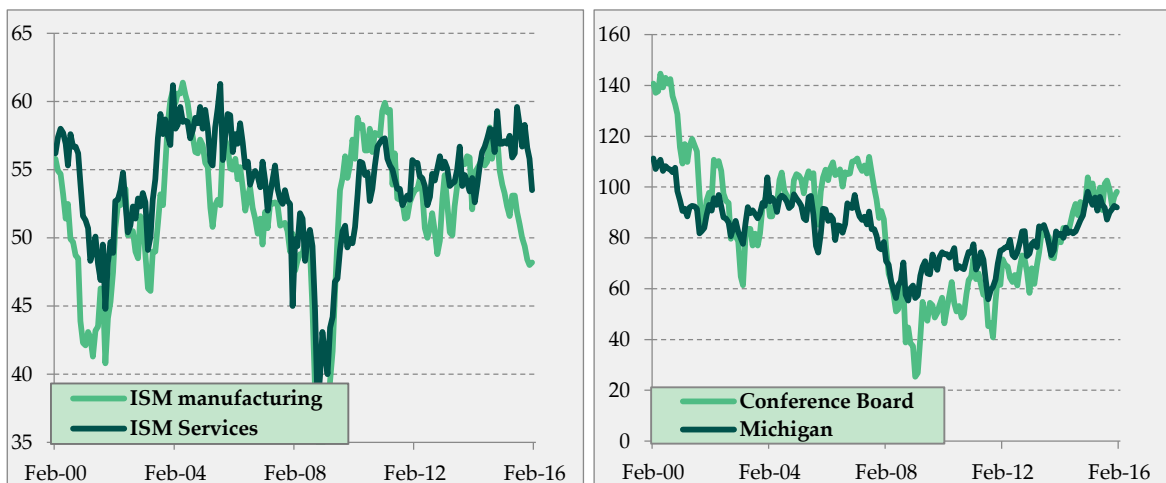
Source : Datstream, Degroof Petercam

- Looking beyond the short-term, we think the chances of a prolonged period of relatively slow growth (in combination with interest rates around the ZLB) are high against the back of strengthening demographic headwinds and less scope for debt accumulation going forward. We would not agree that bugetary and monetary policymakers have lost all ammunition to fight this extremely challenging situation. At the same time, it is not clear whether policymakers are ready to think more 'out of the box' in this respect. (<https://insights.petercam.com/developed-markets/unconventional-monetary-policy-pushing-on-a-string>).

United States

- The US economy is facing headwinds based on most recent confidence indicators. Consensus growth estimates for 2016 (2.4%) seem too high as we have been arguing several months now.
- Confidence in the manufacturing sector is suffering from a stronger USD and low oil prices, respectively weighing on exports and investment in the energy sector. Somewhat worryingly, confidence in the service sector has also come down since last October to a level that is slightly below its LT-average.

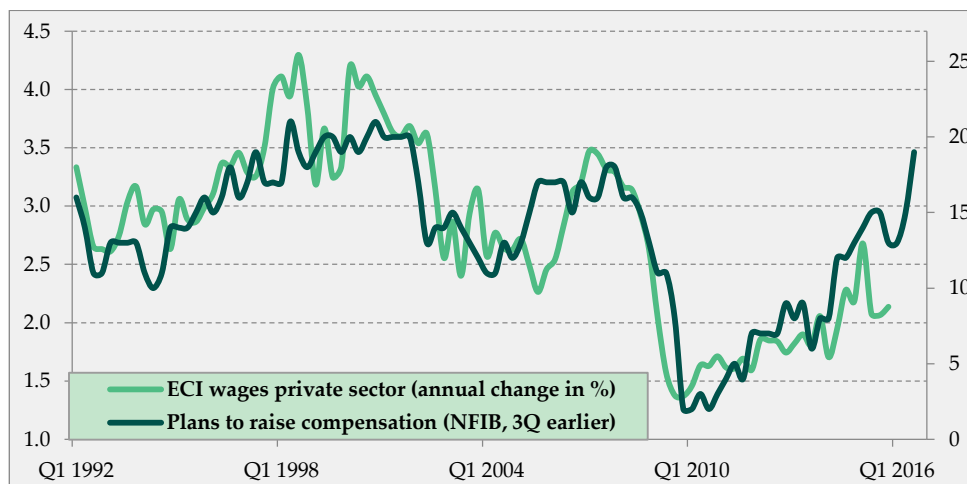
US economic activity losing steam



Source : Datstream, Degroof Petercam

- Consumer confidence has been stabilizing over the last three months and points to real consumption growth of close to 2.5%. Looking ahead, consumer spending should hold up against the back of the ongoing recovery in the labor and housing market and low energy prices. That said, there's a real chance that the recent bout of financial market turmoil affects consumer confidence in a negative way. On the other hand, the impact should be mitigated because of the further fall in energy prices, another important driver of consumer confidence.
- Most recent data on the labor market are mixed. The unemployment rate decreased further to 4.9% (=NAIRU), but initial jobless claims have increased somewhat over the last couple of months. The U6 unemployment rate remains at 9.9% (against LT-average of 8.9% between 1994 and 2007), suggesting that the labour market is not yet running at full capacity.
- Headline inflation jumped up in December (to 0.7% from 0.4% in November) as the earlier sharp drop in energy prices seen earlier starts to have less of a negative impact. Base effects linked to energy prices will make sure that headline inflation will trend higher in the second half of the year. At 2.1% and 1.4% for core inflation and core PCE inflation (which is more important for Fed) respectively, underlying inflation pressures remain subdued. In fact, over the last five years the Fed has failed to achieve its 2% inflation target. Looking forward, however, evidence is mixed with unit labor costs suggesting that core inflation should move up while other survey based price expectations are not signalling any clear acceleration in inflation.
- Future wage growth will be key in this respect. At this point, despite the acceleration witnessed in recent quarters, wage growth is still subdued at around 2.5% yoy. NFIB survey indicators suggest wage growth should continue to pick up over the next couple of quarters. If sluggish productivity growth would remain in place, than core inflation will increase further.

Leading indicators point to accelerating wage growth



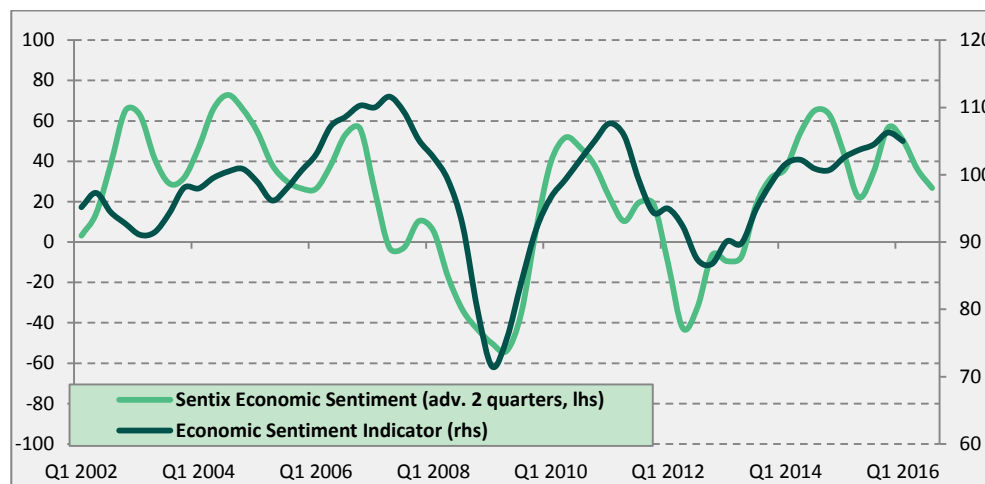
Source : Datstream, Degroof Petercam

- All in all, US policymakers are not in a hurry to raise interest much further in 2016. Clearly, recent market turmoil, signs of hesitation in the US economy and the fact that inflation remains below the Fed's target imply that it is likely to adopt a very cautious approach. The most important message is that monetary policy looks set to remain accommodative in the foreseeable future because the US economy is not doing all that great. The Fed is likely to proceed gradually and only if the underlying economic momentum remains strong enough.

Eurozone

- The European economy continues to grow at a modest pace which is fairly disappointing given several positive elements (low energy prices, accommodative monetary policy and the current low yields environment and EUR weakness) in place. Leading indicators are still in line with expansion of around 1.5%- 2%. This is encouraging after years of standstill though still nothing to cheer about. Indeed, Eurozone economic activity has just pasted its 2008 level. What's more, the upward economic momentum seems to be leveling off according to latest confidence survey data. Finally, it will prove close to impossible for the Eurozone to escape the current global growth deceleration. Therefore, consensus growth forecasts look somewhat too optimistic. It's not entirely clear at this moment to what extent risks stemming from a few players in the banking sector could spread more widely.

Eurozone recovery loses momentum



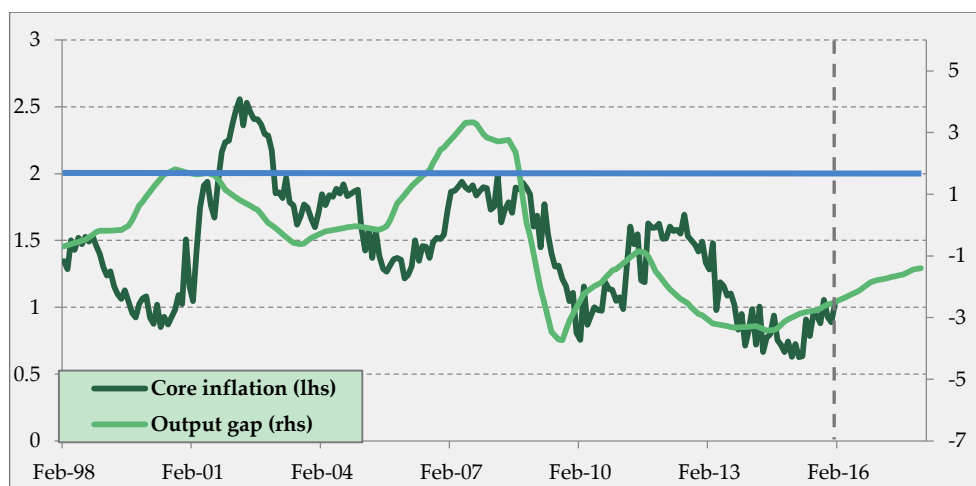
Source : Datstream. Degroof Petercam

- Looking ahead, consumption should continue to increase at a modest pace supported by the slow but gradual improvement observed within the labour market, resilient consumer confidence and low oil prices.
- Headline inflation (0.2% yoy in December) is held down by the recent steep fall in energy prices but base effects will send it higher in the second half of the year. Underlying price measures on the other hand remain very weak reflecting the slack in the labor market. Given the persistence of the large negative output gap, core inflationary pressures are expected to stay fairly weak. The ECB is likely to experience major difficulties in getting inflation up to its target of 2%.
- Our long-held stance that the ECB would be forced to do more is proven right. In its December meeting, the ECB left the size of monthly asset purchases unchanged at €60 billion but decided to extend its program until March 2017. In addition, the ECB decided to lower its deposit rate by 10 bp to -0.3. In its January meeting, the ECB implicitly committed to do more in March. A further deposit rate cut to -0.4% seems the absolute minimum the ECB will have to deliver next month in order to more or less meet financial market expectations.
- The Greek situation remains extremely difficult. Although funding is secured following the agreement reached in July, further imposed budgetary tightening will keep Greece stuck in recession with unemployment and public debt at unsustainably high levels. In this context, political and

economic risks will stay high.

- In a longer term perspective, European politics remain worrying in the sense that the currency union still faces existential challenges. Further integration, while very much needed, looks far from evident at this point. Both the refugee crisis and rising popularity of extreme political parties in recent years is likely to make things only more complicated in this respect.
- The political situation in Spain is now increasingly drawing attention because, unlike in the past, no single party has an absolute majority and forming a coalition is difficult. The ECB's QE program, however, is likely to prevent that government bond spreads widen sharply. The Catalan issue should not be a major problem at least for now. First, Catalans are highly divided. Second, EU membership would not be possible without all other EU members approving it (highly unlikely).
- The Brexit risk is real. Polls suggest opinions are highly divided (latest figures show that 'leave camp' is leading). The debate is likely to intensify in the near future. All in all, our scenario is that Brexit will be avoided eventually. That said, risks remain high. This situation once again underlines the very challenging European political context. (<https://insights.petercam.com/developed-markets/brexit-fears-likely-to-intensify>)

ECB on a very challenging mission to reach its 2% inflation target



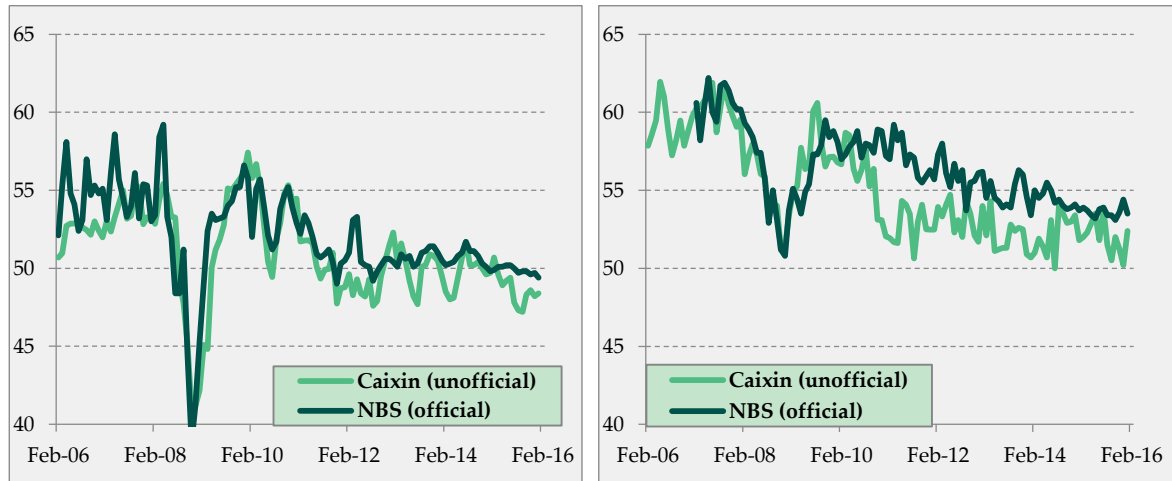
Source : Datstream, Degroof Petercam

Japan and Emerging Markets

- Economic activity is still very modest at best. The tightening labor market points in the direction of accelerating wage growth though other evidence paints a more nuanced picture. Inflation, meanwhile, remains significantly below the Bank of Japan's 2% target. The combination of modest economic activity and below target inflation, as we argued before, would prompt the BoJ to expand its monetary stimulus program. Indeed, in its latest policy meeting the BoJ applied a negative interest rate of -0.1% to current accounts that commercial banks hold at the BoJ (three-tier system). The BoJ also made clear that it will not hesitate to cut interest rates further into negative territory if necessary.
- More broadly in EM, the slowdown witnessed over the last few years reflects several factors including the negative effect of lower commodity prices, tighter external financial conditions linked to the prospect of the first rate hike in the US, the economic rebalancing in China, structural bottlenecks as well as distress related to (geo)political factors.

- Economic growth in EM has slipped below the average over the past 35 years. Moreover, Brazil and Russia are struggling with recession. Economic activity in EM is still very sluggish, particularly in Latin America where a weak growth momentum is accompanied with above target inflation. More flexible exchange rates, lower levels of external debt in general and significant amounts of international reserves should protect most EM against a full-blown financial crisis. Moreover, China's stimulus measures are likely to make sure that imminent hard landing fears will diminish somewhat for now. Finally, the currency depreciation seen in many EM since 2013, should eventually translate in improved competitiveness when combined with further productivity enhancing reforms. To be clear, as mentioned earlier, current financial and economic conditions as well as structural issues will make sure that EM are not up for a rapid recovery. Risks remain on the downside even though confidence indicators are not signalling a further deterioration in economic momentum more recently.
- A Chinese hard landing will probably be avoided for now as the stabilizing effect of earlier stimulus measures slowly starts to kick in. The latest confidence data show early signs of stabilization. On the other hand, the medium to longer term outlook still looks incredibly challenging against the back of the huge Chinese debt overhang, ageing population, less potential to catch up from behind and difficulties linked to further economic rebalancing. Hard landing fears, therefore, are likely to stay with us for many more years. (<https://insights.petercam.com/emerging-markets/6-graphs-illustrating-our-current-view-on-chinas-economy>)

Chinese slowdown but no hard landing for now



Source : Datstream. Degroof Petercam

- Although it's impossible to exclude the scenario of a large one-off RMB depreciation, we don't think this will happen in the coming months (<https://insights.petercam.com/developed-markets/sharp-cny-depreciation-just-around-the-corner>). A gradual managed depreciation remains our base case scenario for now.

GDP and CPI Outlook

	GDP			Inflation		
	2015	2016	2017	2015	2016	2017
US	2.4	1.5	1.9	0.0	1.3	2.0
		2.4	2.5		1.5	2.3
Eurozone	1.5	1.3	1.4	0.1	0.9	1.4
		1.7	1.7		0.8	1.5
Japan	0.7	1.1	1.2	0.7	0.5	1.4
		1.2	0.6		0.6	2.0
China	6.9	5.5	5.0	1.5	1.9	2.2
		6.5	6.3		1.6	1.7

Degroof Petercam forecasts as of 8 February 2016, *Consensus forecasts*

The information contained in this document is provided for pure information purposes only. Present document does not constitute an investment advice and independent investigations, assessments or analysis regarding any investment should be undertaken by the potential investors and recipients as deemed appropriate by them. This document doesn't form part of an offer or solicitation for shares, bonds or mutual funds, or an invitation to buy or sell the products or instruments referred to herein. Applications to invest in any fund referred to in this document can only validly be made on the basis of the current prospectus or simplified prospectus, together with the latest available annual report and accounts. All opinions and financial estimates herein reflect a situation on the date of issuance of the document and are subject to change without notice. Indeed, past performances are not necessarily a guide to future performances and may not be repeated. Degroof Petercam S.A. has made its best efforts in the preparation of this document. The information is based on sources which Degroof Petercam S.A. believes to be reliable. However, it does not represent that the information is accurate and complete. Degroof Petercam S.A. is acting in the best interests of its clients, without carrying any obligation to achieve any result or performance whatsoever. Degroof Petercam S.A., its connected persons, officers and employees do not accept any liability for any direct, indirect or consequential loss, cost or expense arising from any use of the information and its content. Present document may not be duplicated, in whole or in part, or distributed to other persons without prior written consent of Degroof Petercam S.A.