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IDEA

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Global Macro Briefing

Assessing the EM ex China Policy Mix and Fundamentals

EMs ex-China have become key contributors to the global growth acceleration during the past year. We take stock of the current EMXC policy mix and assess whether it can sustain the nascent recovery.

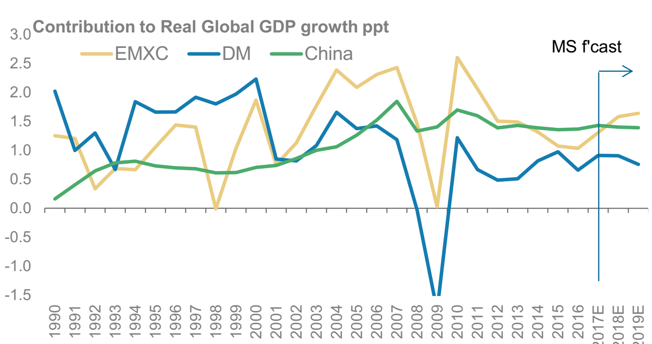
EMXC's growth has shifted into a higher gear: Real GDP growth has risen from 3.1%Y in 3Q16 to 4.4%Y in 3Q17, the strongest pace since 3Q11 and, when excluding the technical rebound in 2010/11, comparable to 3Q03. This has been driven by a better policy mix and an improved external demand environment.

How long this recovery can be sustained will depend on the policy mix: We expect the EM policy mix (monetary, fiscal and labour market policy) to remain supportive of the growth outlook. Most EMs are maintaining adequate real interest rate buffers, have taken up fiscal consolidation and are not intervening in the labour market, which we believe will ensure that macro-stability indicators remain largely in check.

EMXC's contribution to global GDP growth to rise further: We expect the recovery in EMXC to gather further momentum and hence its contribution to global growth to rise to 41% in 2018 and 43% in 2019, up from 36% last year. As the recovery continues, we do see a modest rise in inflation and wider current account deficits, but macro-stability indicators should broadly remain within policy-makers' comfort zones.

Three key risks to our constructive view: i) A shift in the political environment which either delays the ongoing fiscal consolidation or results in a deterioration in the fiscal deficit trend; ii) A quick rise in oil prices due to global supply concerns; and iii) A significant rise in trade friction which could weigh on global trade growth.

Exhibit 1: EMXC* contribution to global GDP growth set to rise further



Source: Haver Analytics, IMF, national sources, Morgan Stanley Research forecasts; *EMXC is PPP-weighted and includes all EMs under Morgan Stanley coverage.

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Exhibit 2: Morgan Stanley forecasts at a glance

	2017E	2018E		2019E	
	MS	MS	Cons.	MS	Cons.
GLOBAL	**3.6**	**3.9**	**3.8**	**3.8**	**3.7**
G10	**2.2**	**2.2**	**2.2**	**1.9**	**1.9**
US	2.3	2.7	2.6	2.1	2.2
Euro Area	2.3	2.1	2.2	1.9	1.8
Japan	1.7	1.3	1.3	1.5	1.0
UK	1.8	1.1	1.4	0.8	1.4
EM	**4.7**	**5.0**	**4.9**	**5.0**	**4.9**
China	6.8	6.5	6.5	6.3	6.2
India	6.3	7.5	7.4	7.7	7.5
Brazil	0.7	3.1	2.5	3.4	2.5
Russia	1.8	2.3	1.9	1.8	1.8
MW Global*	3.2	3.3	3.2	3.1	3.0

Source: Morgan Stanley Research forecasts; *Global GDP weighted by long-term market exchange rates instead of PPP weights, given for comparison.

Key Macro Risk Events

FRIDAY, JAN 26 - UK GDP, US GDP/DUR. GOODS

MONDAY, JAN 29 - US CORE PCE

TUESDAY, JAN 30 - EA GDP, US CONS. CONF.

WEDNESDAY, JAN 31 - CHN PMI, EA CPI, US FOMC

THURSDAY, FEB 1 - US MANUFACTURING ISM

FRIDAY, FEB 2 - US LABOUR MARKET REPORT

What's Inside

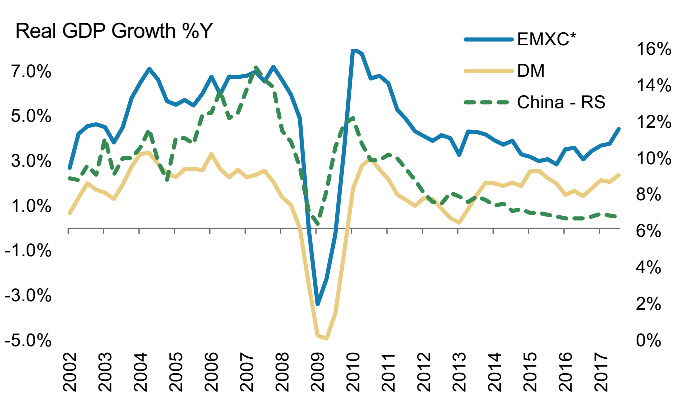
Assessing the EMXC policy mix and fundamentals

EMs ex China playing an important role in the global recovery

EM ex China (EMXC) growth has accelerated significantly over the last four quarters: During the past year, the global economy has moved from an environment of sub-par growth to above-trend growth, driven by a synchronous recovery across DMs and EMs. While DM growth has been maintained at a steady pace at relatively high levels, EMXC is becoming a key contributor to the global recovery for the first time since the early 2000s. Indeed, EMXC* GDP growth has already shifted into a higher gear, from 3.1%Y in 3Q16 to 4.4%Y in 3Q17, the strongest pace since 3Q11 and, when excluding the technical rebound in 2010/11, it is comparable to 3Q03. As global* GDP growth picked up from 3.1%Y to 4.0%Y between 3Q16 and 3Q17, about half of this acceleration is attributable to EMXC (see Exhibit 3 for a basket of countries included in quarterly growth in EMXC* and global*).

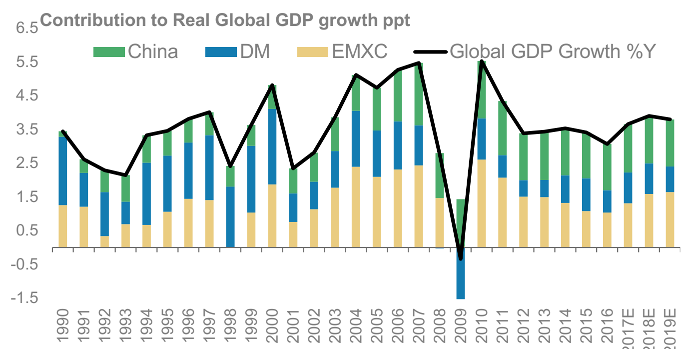
How long can this EMXC recovery be sustained? As opposed to DMs, EMXCs have just started to recover after several years of deep macroeconomic adjustment with significant economic slack still remaining. The adjustment in macro policies following the 'taper tantrum' in 2013 and commodity price shock in 2H14 have led to a significant, broad-based improvement in macro-stability indicators. The strength of the EM growth recovery will be particularly critical in the context of maturing business cycles in DMs and rising US interest rates. How long this recovery can be sustained is dependent on the trend in the macro policy mix and its impact on macro stability, in our view.

Exhibit 3: EMXC* quarterly GDP growth has accelerated and should pick up further



*EMXC is PPP-weighted and includes all EMs under Morgan Stanley coverage except Argentina, Nigeria, Saudi Arabia and Venezuela due to lack of longer quarterly history. As a result the series growth pace is somewhat higher than our more comprehensive annual dataset.
Source: Haver Analytics, national sources, Morgan Stanley Research forecasts

Exhibit 4: EMXC* is again becoming a key contributor to the global recovery



*EMXC is PPP-weighted and includes all EMs under Morgan Stanley coverage equal to 33% of world in PPP terms. Aggregate EMXC as calculated by the IMF accounts for 40% and 24% of global GDP on a PPP and nominal dollar basis, respectively.
Source: Haver Analytics, national sources, Morgan Stanley Research forecasts

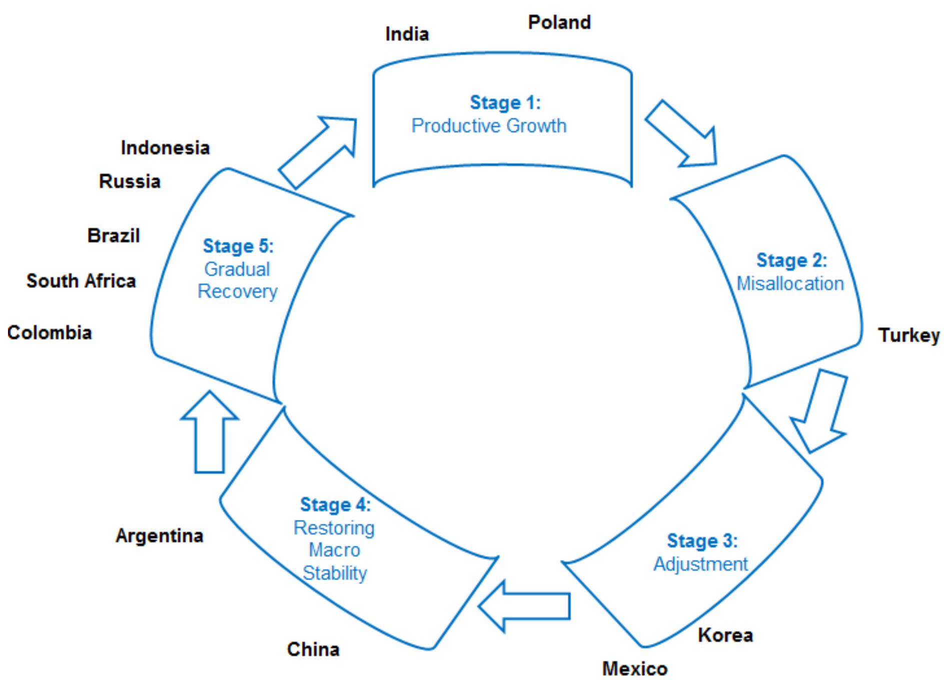
Assessing the EM policy mix – our framework

Five phases of the EM cycle: In our view, EM business cycles broadly evolve in the following phases: 1) Productive growth; 2) Misallocation; 3) Adjustment; 4) Restoring macro stability; and 5) Gradual recovery (see Box A for a more detailed description). Currently, the majority of EMs we track are in stage five (Exhibit 5). In order to gauge whether EMs' policy mix may be resulting in misallocation of capital, we track the key policy actions that influence economic incentives and their impact on macro-stability indicators.

With respect to the **EM macro policy mix,** we look at: i) Dynamics/levels of real interest rates; ii) Private sector credit/debt growth (several EMs tend to take policy measures that influence credit growth directly); iii) Fiscal deficits; and iv) Real wage growth (many EMs tend to intervene in labour markets intermittently with policy changes that push wage growth above productivity growth).

We overlay the trend in policy mix with the outcome of **macro-stability indicators** broadly characterising price, external and financial stability: dynamics/levels of inflation, current account balances and private sector debt. A broad-based deterioration would be a strong signal that a country has moved away from the productive growth phase into a phase of misallocation. If a country moves into the misallocation phase, it increases the risk that a major adjustment in macro policies will be required, which would then weigh on the near-term growth outlook. For instance, during 2010-13, among large EMXCs, Brazil, India, Indonesia, South Africa and Turkey were all pursuing a policy mix that resulted in a broad-based deterioration in macro-stability indicators. Eventually, triggers in the form of the taper tantrum and a fall in commodity prices forced an abrupt, corrective change in the policy mix and a sharp slowdown in real GDP growth.

Exhibit 5: EMs in the economic cycle



Source: Morgan Stanley Research

Box A: A stylised framework for analysing EM business cycles

The EM business cycle has evolved in these stages:

1) Productivity growth: Moderate to high productivity-driven growth, no red flags in macro-stability indicators (such as current account balance, inflation and rise in debt/GDP ratios or non-performing loans in the banking system).

2) Misallocation: Moderate growth driven by bad macro policies, particularly loose fiscal and monetary policies, accompanied by rising imbalances. The incremental capital output ratio and macro risk premium rise. Debt/GDP also tends to rise as a result.

3) Adjustment: Domestic or external factors (though for EM, it is typically external factors) trigger a growth shock. For some EMs, it was the US QE tapering which was the trigger while, for a few others, it was the sharp fall in commodity prices and attendant terms of trade shock. The macro risk premium rises.

4) Restoring macro stability: As policy-makers take corrective macro policies like tightening monetary and/or fiscal policy, domestic demand weakens but macro-stability indicators show a clear improving trend. Current account balances improve, inflation moves towards more normalised levels (from either too low or too high levels) and debt/GDP stabilises. The macro risk premium reduces.

5) Gradual recovery: As macro-stability indicators improve significantly, central banks begin to normalise monetary policy, supporting a slow recovery. Productivity also improves and the economy gradually returns towards a sustainable growth path.

Majority of EMXCs pursuing the right policy mix

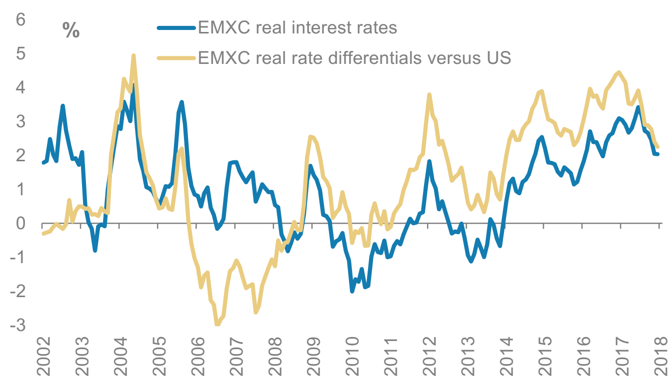
Applying this framework to the current economic environment, we conclude that the majority of EMs we cover in this report are conducting policy in a way that does not create new major economic distortions. EMXC monetary policies are more prudent than they were during 2010-12 while fiscal policies are also moving in the right direction. Moreover, the fact that real wage growth is moderate and in line with output growth suggests that policy-makers have not made major interventions in the labour market.

Turning to the details of the drivers of macro stability:

1) Adequate real rate buffers: EMXC real interest rates have been moderating from their peaks last June but are still at 200bp on an aggregate level, which is well above their post-GFC average and even slightly above their 2003-05 average (Exhibit 6). Adequate real rate buffers provide an important backstop amid rising US interest rates. In the aftermath of the 'taper tantrum' in mid-2013, net capital flows to EMs fell significantly, as investors worried about weak EM macro stability and especially low real rate buffers. As a result, central banks had to hike interest rates aggressively. However, now that EMXC real rate buffers have been restored and EMXC growth differentials versus DMs are recovering, we think that EMXC economic growth is more resilient to US interest rate hikes.

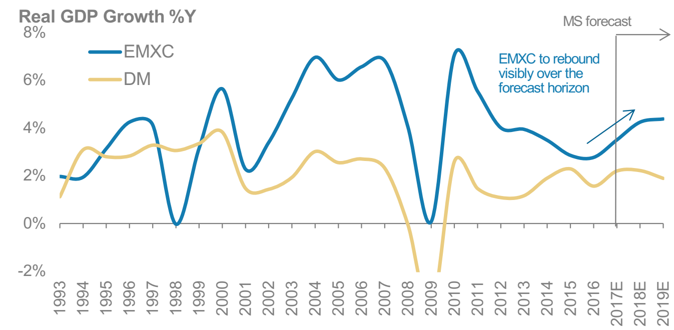
In 2018, we expect several EM central banks to hike interest rates in a gradual, countercyclical fashion, in line with a modest increase in headline inflation and growth. Real interest rates should remain broadly stable around current levels based on our 12-month forecast. Adequate real interest rate levels should keep underlying inflation in check and differentials with the US well above 2013 levels, thereby reducing the risk of a sudden reversal in capital flows.

Exhibit 6: EMXC* real interest rates still elevated



*EMXC is PPP-weighted and includes India, Indonesia, Korea, Brazil, Mexico, Russia, South Africa, Turkey and Poland. US real rate is fed funds rate minus core PCE. EM real rate is calculated as PPP-weighted 3M market rate minus headline CPI.
Source: Bloomberg, Haver Analytics, IMF, Morgan Stanley Research

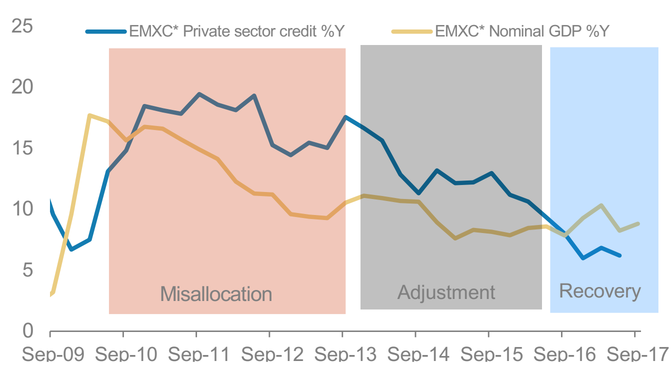
Exhibit 7: EMXC real GDP growth differentials versus US recovering



*EMXC is PPP-weighted and includes all EMs under Morgan Stanley coverage equal to 33% of world in PPP terms.
Source: Haver Analytics, IMF, national sources, Morgan Stanley Research forecasts

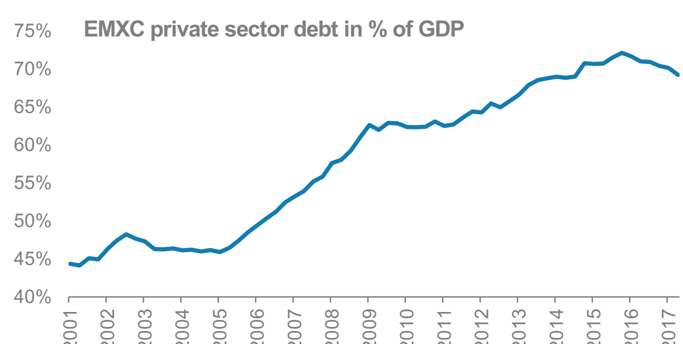
2) Decline in private sector debt has reduced financial stability risks: Post-credit crisis, debt growth was fuelled by supportive monetary and fiscal policies. Back then, private sector debt increased by a rapid 7% of GDP between 2010 and end-2013, reaching a new high of 68.7% of GDP and raising financial stability risks. However, the tightening in global financial conditions and adjustment in the EMXC macro policy mix has led to a moderation in debt growth since then. EMXC credit growth has decelerated to the slowest pace since the GFC and, in combination with a pick-up in nominal GDP growth, drove a decline in private sector debt levels by 2.6% of GDP from its peak in 4Q15.

Exhibit 8: EMXC* non-financial private sector debt growth has slowed significantly



*EMXC is PPP-weighted and includes India, Indonesia, Korea, Brazil, Mexico, Argentina, Colombia, Russia, South Africa, Turkey and Poland.
Source: CEIC, Haver Analytics, IMF, national sources, Morgan Stanley Research

Exhibit 9: EMXC* non-financial private sector debt has declined visibly since 4Q15



*EMXC is PPP-weighted and includes India, Indonesia, Korea, Brazil, Mexico, Argentina, Colombia, Russia, South Africa, Turkey and Poland.
Source: CEIC, Haver Analytics, IMF, national sources, Morgan Stanley Research

At a country level, the private sector debt overhang has mainly been an issue for South Korea, which had witnessed the largest increase in leverage among major EMs. However, the introduction of macro-prudential measures is now leading to a moderation in debt growth. Select EMs like India were also facing the challenge of weak corporate sector and banking sector balance sheets. However, over the last two years there has been significant progress in repairing those balance sheets, taking away this constraint on growth.

3) Fiscal policy on gradual consolidation path: During the past year, the combination of fiscal consolidation and a recovery in government revenues has helped to reduce the EMXC fiscal deficit to 4.3% of GDP in 3Q17 from its peak at 5.0% in 2Q16. Policy-makers have reduced fiscal support as the economic recovery progressed and became more self-sustaining, particularly in the more export-oriented EMs. However, the aggregate EMXC fiscal deficit is still somewhat high, suggesting that the adjustment is incomplete in a number of countries, for instance in Brazil, South Africa, Argentina and Colombia. In some of these EMs, monetary policy has done most of the heavy lifting in terms of restoring macro stability, while the fiscal policy adjustment has been somewhat lagging.

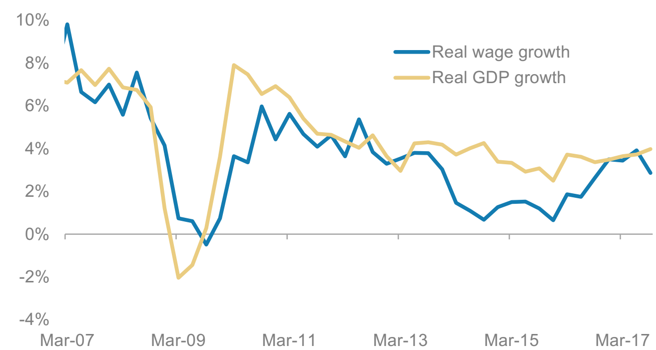
In 2018, we expect EMXC fiscal deficits to shrink further as fiscal consolidation continues and nominal GDP growth shifts higher. In select countries, for instance South Africa, where the fiscal outlook remains challenging, large deficits may require higher real rate levels than would otherwise have been the case, constraining the pace of growth recovery.

4) Moderate pace of real wage growth: During 2009-13, some of the EMs had taken measures which distorted labour market policies and pushed real wage growth higher than output growth, adding to inflationary pressures. As a result, EMs had to enact meaningful cuts in real wage growth during the adjustment phase (2013-16). Over the course of the past year, EMXC real wage growth has rebounded, but remains at moderate levels, suggesting that policy-makers have not made a major intervention in the labour market. As the economic recovery takes hold, real wage growth should accelerate, but we expect the pace of growth to remain in line with output growth, thereby reducing the risk of an inflation overshoot.

Exhibit 10: EMXC* fiscal deficit has narrowed, but is still elevated

*EMXC is PPP-weighted and includes India, Indonesia, Korea, Brazil, Mexico, Argentina, Colombia, Russia, South Africa, Turkey and Poland.
Source: Haver Analytics, IMF, national sources, Morgan Stanley Research

Exhibit 11: EMXC* real wage growth recovering gradually



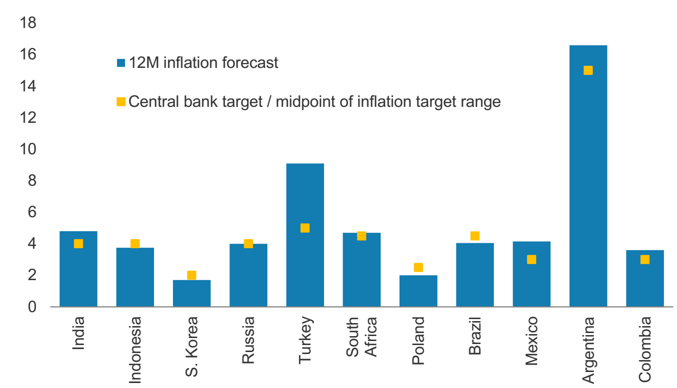
*EMXC is PPP-weighted and includes India, Indonesia, Brazil, Mexico, Colombia, Russia, South Africa and Poland.
Source: Haver Analytics, IMF, national sources, Morgan Stanley Research

Implications for EMXC macro stability: Staying within policy-makers' comfort zones

At this point, most EMs are in a situation where macro stability has been restored and economic growth is recovering. Inflation has moved within central banks' comfort zones and current account balances in the countries which were running deficits have improved significantly during the past year, while financial stability risks have reduced. Out of the major EMs we analyse in this report, only two (Turkey and Argentina) are showing broader deterioration in macro-stability indicators. However, in Argentina policy-makers are in the process of adjusting the macro policy mix, and in Turkey we expect corrective action this year (for more details, see the venn diagrams on the next page and Exhibit 15).

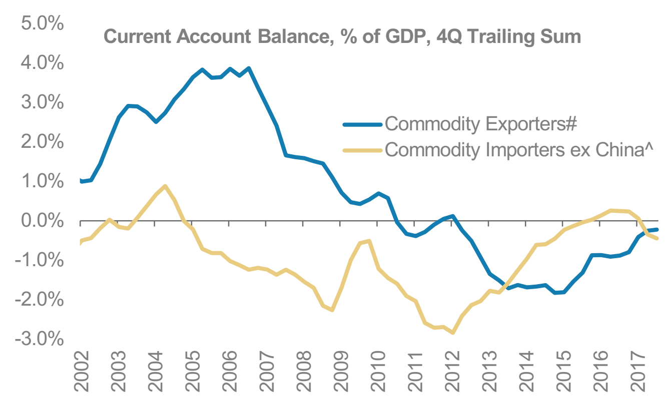
In terms of the outlook, we expect real interest rates to stay elevated across most countries and fiscal consolidation to remain on track. Hence a major deterioration in macro-stability indicators appears less likely. As the economic recovery continues, we do see a modest rise in inflation, a widening in current account balances, and a rise in private sector credit growth (but it should stay below nominal GDP growth) and real wage growth (in line with output growth). However, based on our assessment of the current and expected EMXC macro policy mix, these indicators should broadly remain within policy-makers' comfort zones. Turkey is again an exception, as inflation should moderate only gradually this year and its current account deficit will likely widen on the back of higher oil prices and the lagged impact of stimulus measures.

Exhibit 12: Inflation set to stay within central banks' comfort zones



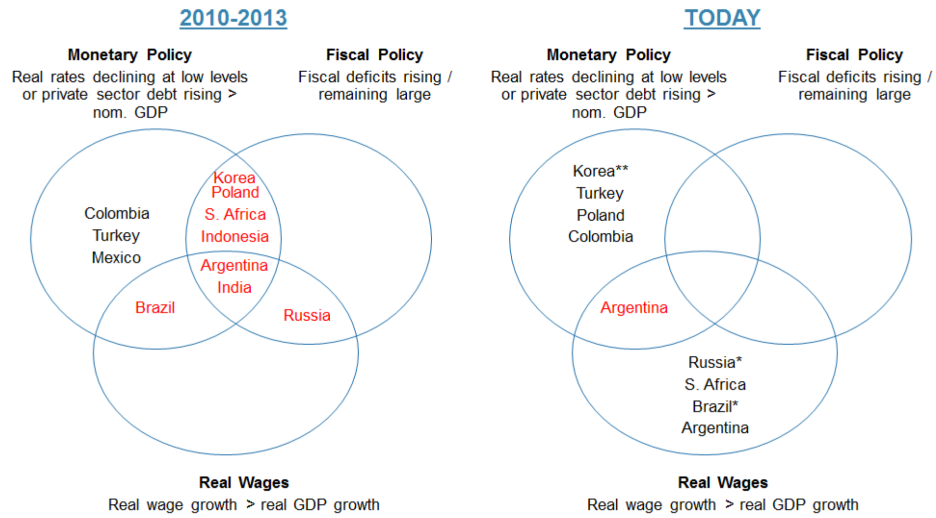
Source: Haver Analytics, national sources, Morgan Stanley Research forecasts

Exhibit 13: EMXC current account balance has improved significantly



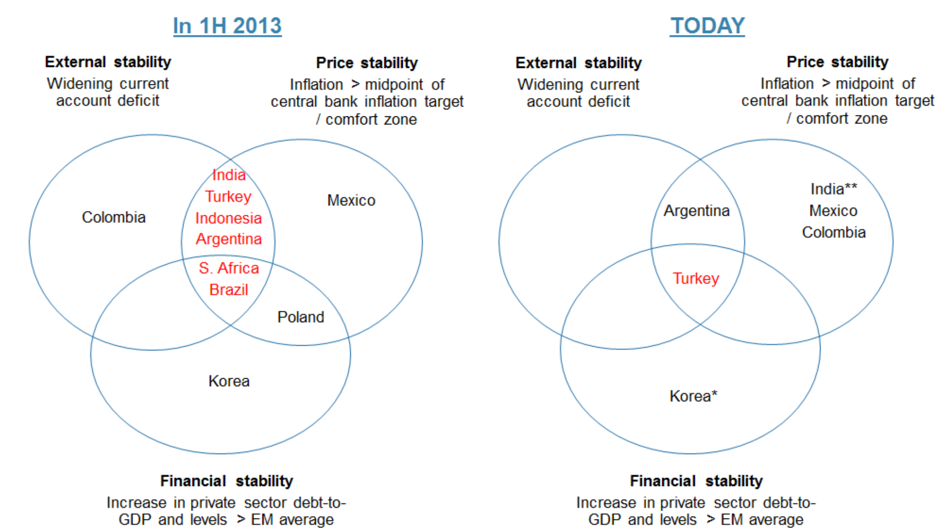
^Commodity importers (referring to non-food commodities mainly) include India, Korea, Turkey, Poland, Mexico and Argentina. #Commodity exporters include Indonesia, Brazil, Russia, South Africa and Colombia.
Source: Haver Analytics, national sources, Morgan Stanley Research

EMXC macro policy mix in 2010-13 versus today



Source: Morgan Stanley Research; *Real wage growth in Brazil, and Russia has been above GDP growth during recent quarters, but follows a period of major correction; **Korea's debt levels have been stabilising more recently as non-financial corporate leverage has declined and the increase in household debt has slowed.

EMXC macro-stability indicators in 1H13 versus today



Source: Morgan Stanley Research; *Korea's debt levels have been stabilising more recently. ** In India, while core inflation is closer to the central bank's midpoint, headline inflation is somewhat higher due to adverse base effects in food inflation.

Three risks to our favourable outlook on EMXC

We see three main risks to our favourable outlook on the EMXC policy mix and macro-stability indicators.

1) Elections: This year will be busy in terms of major elections in EMXC in the pipeline which could impact further progress on fiscal consolidation. In particular, presidential elections in Russia, Brazil and Colombia, presidential and congressional elections in Mexico as well as regional elections in India and Indonesia will be in focus this year (Exhibit 14). Those elections could either create uncertainty with regard to the near-term fiscal outlook as governments may take up pre-election spending (e.g., India and Indonesia) or medium-term fiscal outlook as progress on much-needed fiscal reforms could stall (e.g., Brazil).

2) Rising trade frictions: In addition, trade frictions may intensify against the backdrop of recently announced protectionist measures by the US and possible retaliatory measures (see US Public Policy: Trade Policy: Beyond the Hypothetical, January 23, 2018). A full-blown trade conflict, albeit not our base case, could dent the continued improvement in exports growth, with risks being largest for manufacturing exporters in EM Asia and Mexico.

3) Impact of higher oil prices: Finally, a quick rise in oil prices driven by a supply shock could bring upside risk to inflation in oil-importing EMs, such as India, Turkey, Poland and South Africa. However, with the exception of Turkey, as of now we see limited risks to our macro policy outlook, as the current underlying inflation pressures in those economies remain benign.

Exhibit 14: Political events calendar

Country	Date	Event
	2018	
India	Feb-18	Union budget announcement
Russia	Mar-18	Presidential election
Colombia	11-Mar-18	Legislative election
Colombia	27-May-18	1st round presidential election
Colombia	17-Jun-18	2nd round presidential election
Indonesia	Jun-18	Regional elections
Korea	Jun-18	Local elections
Mexico	2-Jul-18	Presidential/legislative elections
Indonesia	Aug-18	2019 budget speech
Brazil	7-Oct-18	1st round presidential/legislative elections
Brazil	28-Oct-18	2nd round presidential/legislative elections
Korea	Oct-18	Budget speech

Source: Morgan Stanley Research

Conclusion

As EMXCs stay on track in managing their macro policy mix, the EMXC recovery should continue for longer without abrupt adjustments to the policy mix becoming necessary, as was the case in 2013-14. We expect EMXC GDP growth to accelerate to 4.2%Y in 2018 and 4.4%Y in 2019 from 3.5%Y in 2016. We believe that the key domestic risk to this outlook will be a change in the political environment which could lead to a swing in the policy mix to push growth via measures that could compromise the macro-stability outlook.

Exhibit 15: Individual country highlights – policy mix and macro stability

Country	Recent Developments	Outlook for 2018
	1) Productive Growth	
India	• Policy-makers have been pursuing a policy mix which is supporting the productivity dynamic and reducing misallocation risks. • This has been achieved through fiscal consolidation, reduced unproductive redistributive spending (best reflected in rural wage growth) and maintaining an adequate level of real rates. • While the central government's fiscal deficit has widened to 4.2% of GDP in November 2017, this has been largely due to a front-loading of expenditure, rather than a reflection of outsized expenditure growth.	• We expect some acceleration in fiscal spending against the backdrop of upcoming elections in 2019 but think that the impact on macro stability will be moderate due to a continued focus on maintaining the efficiency of public spending. The risk would be if the government embarks on redistributive spending. • Real interest rates should remain around current levels as the RBI will likely hike interest rates by 25bp in 2H18 against the backdrop of accelerating growth and rising headline inflation. • Despite some marginal deterioration and notwithstanding the impact from higher oil prices, we are confident that key macro stability indicators like inflation and the current account will remain broadly within the RBI's target range and comfort zone.
Poland	• The policy mix has been adequate without major signs of deterioration in macro stability. • Policy-makers have been comfortable with low real rates due to core inflation, private credit and wage trends, together with some tightening in monetary conditions via a stronger PLN. • The fiscal deficit has narrowed, despite an increase in fiscal spending, reflecting the government's success in closing down tax avoidance loopholes.	• Policy-makers will likely maintain their current approach without causing a major deterioration in macro stability. • The NBP is likely to lift policy rates by 50bp in 2H18, though risks are tilted towards later hiking. • A narrowing fiscal deficit has opened up some room for fiscal expansion ahead of the 2019 elections, should the authorities deem it necessary. • More medium term, less generous provision of EU funds in the next budget is likely to hurt potential growth post-2020.
	2) Misallocation	
Turkey	• Policy easing during past year has pushed growth higher, but macro-stability risks have increased. • Real interest rates moderated as inflation accelerated at a faster pace than interest rates; fiscal deficit has risen; government introduced credit guarantee fund-backed lending of TRY200bn. • Strong acceleration in real GDP growth from 3.2%Y to 6.5-7%Y, but also a broad-based deterioration in macro stability, i.e., current account deficit back at ~5% of GDP, double-digit inflation vs. 5%Y target, private sector leverage up >5% of GDP vs. four quarters ago.	• We expect an adjustment in the macro policy mix: the blended policy rate will likely be maintained at elevated levels, which should lead to a major rise in real rates as inflation moderates; some adjustment in the guaranteed lending scheme (reduction to TRY130bn). • Macro-stability indicators to remain weak as they are affected by higher oil prices and lagged impact of stimulus measures (i.e., current account to widen further, inflation could remain elevated and cause corrective action from central bank). • Risk is that if pressures on TRY increase due to global financial conditions or more importantly idiosyncratic geopolitical factors, we are likely to experience the same vicious cycle which we got used to seeing in the last 6-7 years – a weaker TRY, higher CPI and a lower real policy rate.
	3) Adjustment	
Mexico	• Prudent policy mix has safeguarded macroeconomic adjustment after FX depreciation-driven shock (rise in inflation). • Banxico hiked interest rates on financial stability concerns and to rein in rising inflation, and fiscal policy has tightened. • Visible improvement in macro stability, i.e., improving current account balance and public sector debt ratios.	• Prudent policy mix, if maintained post-elections, should lead to visible improvement in macro stability (commitment to fiscal consolidation, slowing inflation). • Uncertainty stems from NAFTA negotiations and the presidential elections this year.
Korea	• Macro policy mix has adjusted to address the rising private sector debt problem, i.e., relatively prudent stance on both monetary and fiscal policy and macroprudential measures aiming to rein in financial stability risks. • Macro policy measures have resulted in stabilisation of private sector debt as corporate sector is already in deleveraging mode and household debt growth has moderated.	• We expect the macro policy mix to remain broadly unchanged. • The BoK is set to maintain real interest rates levels, by raising interest rates in line with the expected tick-up in inflation (we expect a hike of 25bp in 1H18). • Household debt growth should moderate further, slowing the pace of leveraging.

Source: Morgan Stanley Research

Exhibit 16: Individual country highlights – policy mix and macro stability (continued)

Country	Recent Developments	Outlook for 2018
4) Restoring Macro Stability		
Argentina	• Policy mix adjusting to ensure restoring of macro stability; will likely be a multi-year process. • Real interest rates have risen from deeply negative levels as central bank has cut policy rates at slower pace than inflation slowdown. • Large fiscal deficit is being addressed, as reflected by the recent improvement in the primary balance. • Macro-stability indicators mixed, i.e., current account deficit expanding; inflation on downward trend although regulatory rate hikes put a brake on improvement recently.	• We expect further adjustment in policy mix to restore macro stability; macro-stability indicators should show improvement. • Central bank is cutting rates, but real interest rates should increase on the back of inflation rates falling at a faster pace. • Narrowing in the primary fiscal balance should continue if growth stays on track. • Risks are that higher oil prices are fuelling inflation and place downward pressure on trade balance, but our base case is that the impact will be limited.
5) Gradual Recovery		
Colombia	• Economy is on the verge of recovery after oil price-driven policy adjustment. • Fiscal situation remains challenging but moving in the right direction as the economy recovers and oil prices rebound. • Macro-stability indicators have been improving (inflation has moderated from elevated levels and current account deficit is narrowing).	• Macro policy mix to remain adequate, allowing for gradual growth recovery without derailing improvement in macro stability. • We expect BanRep to maintain current real interest rate levels by cutting its policy rate in line with the expected slowdown in inflation (by 50bp in 1H18). • Fiscal deficit set to narrow gradually as economic recovery takes hold. • Higher oil prices support the current account balance.
South Africa	• Monetary policy has done heavy lifting in terms of adjustment in macro policy mix, while fiscal deficit remained large. • Real interest rates have declined, but are still at elevated levels and private sector debt growth remains moderate. • The fiscal balance has been on an upward trend since the GFC, but progress has stalled during the past year, which poses constraint to monetary policy easing. • Macro-stability indicators have improved across the board (inflation declined towards the midpoint of the inflation target range, the current account deficit narrowed to 4Q11 levels, and private sector debt remained stable).	• Macro policy mix should be broadly unchanged with a major deterioration in macro stability unlikely (inflation to remain in check, current account balance to widen modestly). • We pencil in an additional 25bp cut in the policy rate, which should keep real rates at elevated levels. • Main risks stem from rising oil price and loose fiscal policy (we expect the deficit to remain above 3% of GDP), which could lead to exclusion from the World Government Bond Index.
Brazil	• Adjustment in policy mix has supported restoring of macro stability. • Large fiscal deficit remains a constraint. • Real interest rates are still elevated and private sector debt growth is below nominal GDP growth. • Macro-stability indicators have shown major improvement (current account deficit smallest since the Global Financial Crisis and inflation below the midpoint of the BCB's inflation target range).	• In 2018, we expect the macro policy mix to be maintained. • We expect the BCB to hike its policy rate by 50bp in 2H18 and thereby keep real interest rate buffers elevated. • Inflation should remain in the lower part of the target range and the current account deficit widen only modestly as the recovery in domestic demand takes hold.
Russia	• Macro policy mix remains restrictive. • Elevated real interest rates (the highest among major EMs) and narrowing fiscal deficit. • Macro-stability indicators look strong as Russia is still running a current account surplus and inflation has moderated to a record low of 2.5%Y vs. the CBR's 4%Y inflation target.	• Real interest rates are set to moderate but remain elevated at 300bp at year-end. • Macro stability will likely be maintained: inflation should rise in line with the central bank's target and thus not be a major concern. • Higher oil prices should lift the current account surplus.
Indonesia	• Real interest rates have remained elevated during the past two years and the fiscal deficit is around its long-term average. • The pre-election widening in the fiscal deficit is likely to support consumption but be temporary and is unlikely to lead to a major deterioration in macro stability. • A narrowing current account balance, moderation in inflation towards the lower half of BI's inflation target range and private sector deleveraging reflect improving macro stability.	• The macro policy mix should remain broadly unchanged this year. • Real interest rates are set to stay high as BI will likely hike rates by 50bp in 2H18 and inflation remain in check. • The current account deficit should re-widen modestly, but stay well below 2013 levels.

Source: Morgan Stanley Research

Key forecast profile

Exhibit 17: GDP growth, CPI inflation, monetary policy rates

	Quarterly														
	2017				2018				2019				2017E	2018E	2019E
Real GDP	**1Q**	**2Q**	**3Q**	**4QE**	**1QE**	**2QE**	**3QE**	**4QE**	**1QE**	**2QE**	**3QE**	**4QE**			
Global (%Q, SAAR)	**3.8**	**4.3**	**4.0**	**4.1**	**3.9**	**3.9**	**3.9**	**3.9**	**3.7**	**3.8**	**3.9**	**3.5**	**3.6**	**3.9**	**3.8**
G10 (%Q, SAAR)	**1.8**	**3.0**	**2.6**	**2.8**	**2.1**	**2.0**	**2.0**	**1.9**	**1.9**	**2.0**	**1.9**	**1.2**	**2.2**	**2.2**	**1.9**
United States	1.2	3.1	3.2	3.7**	2.6	2.4	2.3	2.4	2.2	2.0	1.9	1.7	2.3	2.7	2.1
Euro Area	2.5	2.9	2.9	3.1**	2.1	2.0	1.9	1.9	1.9	1.9	1.8	1.8	2.3	2.1	1.9
Japan	1.5	2.9	2.5	0.3	0.9	1.4	1.3	1.5	1.7	2.4	2.6	-3.5	1.7	1.3	1.5
UK	1.2	1.2	1.6	1.5	1.1	1.1	0.8	0.0	-0.2	2.0	1.6	1.8	1.8	1.1	0.8
EM (YoY)	**4.4**	**4.5**	**4.9**	**4.9**	**5.0**	**5.0**	**5.0**	**5.1**	**5.1**	**5.0**	**5.0**	**5.1**	**4.7**	**5.0**	**5.0**
China (YoY)	6.9	6.9	6.8	6.7	6.5	6.4	6.5	6.6	6.5	6.4	6.3	6.2	6.8	6.5	6.3
India (YoY)	6.1	5.7	6.3	7.2	7.5	7.6	7.4	7.4	7.7	7.6	7.7	7.8	6.3	7.5	7.7
Brazil (YoY)	-0.4	0.3	0.9	2.0	2.0	2.8	3.5	3.9	3.7	3.2	3.3	3.2	0.7	3.1	3.4
Russia (YoY)	0.5	2.5	1.8	2.1	2.5	2.0	2.6	2.3	1.8	1.8	1.8	1.9	1.8	2.3	1.8
Consumer Price Inflation (YoY)															
Global*	**2.7**	**2.4**	**2.4**	**2.7**	**2.7**	**3.0**	**3.0**	**2.9**	**2.8**	**2.8**	**2.8**	**2.8**	**2.6**	**2.9**	**2.8**
G10	**2.0**	**1.6**	**1.7**	**1.7**	**1.6**	**2.0**	**2.1**	**1.9**	**1.7**	**1.7**	**1.7**	**1.7**	**1.8**	**1.9**	**1.7**
United States	2.6	1.9	2.0	2.1	1.9	2.4	2.3	1.8	1.7	1.8	1.8	1.8	2.1	2.1	1.8
Euro Area	1.8	1.5	1.4	1.4	1.3	1.8	2.1	2.0	1.8	1.6	1.5	1.4	1.5	1.8	1.6
Japan	0.3	0.4	0.6	0.5	0.9	1.2	1.6	1.5	1.3	1.0	0.9	0.8	0.5	1.3	1.0
UK	2.1	2.7	2.8	3.0	3.0	2.9	2.8	2.5	2.1	2.0	2.1	2.2	2.7	2.8	2.1
EM*	**3.2**	**3.0**	**3.0**	**3.3**	**3.4**	**3.7**	**3.6**	**3.6**	**3.6**	**3.5**	**3.6**	**3.5**	**3.1**	**3.6**	**3.5**
China	1.4	1.4	1.6	1.9	2.3	2.4	2.5	2.6	2.6	2.6	2.7	2.7	1.6	2.5	2.6
India	3.6	2.2	3.0	4.3	4.3	5.2	4.3	4.4	4.5	4.2	4.4	4.4	3.3	4.5	4.4
Brazil	4.9	3.6	2.6	2.8	3.2	3.7	3.8	3.9	4.2	4.1	4.2	4.3	3.5	3.8	4.2
Russia	4.6	4.2	3.4	2.6	3.1	3.2	3.8	4.3	4.2	4.1	4.1	4.2	3.7	3.6	4.1
Core Inflation (YoY)															
Global	**2.2**	**2.1**	**2.0**	**2.1**	**2.1**	**2.3**	**2.4**	**2.5**	**2.5**	**2.5**	**2.5**	**2.5**	**2.1**	**2.3**	**2.5**
G4	**1.2**	**1.3**	**1.2**	**1.2**	**1.3**	**1.5**	**1.6**	**1.6**	**1.6**	**1.7**	**1.7**	**1.7**	**1.2**	**1.5**	**1.7**
United States^	1.8	1.5	1.4	1.5	1.5	1.7	1.8	1.7	1.7	1.8	1.8	1.7	1.5	1.7	1.7
Euro Area	0.8	1.1	1.2	0.9	1.0	1.3	1.4	1.6	1.5	1.7	1.6	1.6	1.0	1.3	1.6
Japan	0.1	0.0	0.2	0.3	0.4	0.6	0.8	1.1	1.1	1.2	1.3	1.2	0.1	0.7	1.2
UK	1.8	2.5	2.6	2.6	2.6	2.5	2.4	2.4	2.3	2.4	2.5	2.6	2.4	2.5	2.4
BRIC	**3.2**	**2.9**	**2.9**	**3.0**	**3.0**	**3.2**	**3.3**	**3.3**	**3.3**	**3.3**	**3.3**	**3.3**	**3.0**	**3.2**	**3.3**
China	2.0	2.1	2.2	2.3	2.3	2.3	2.4	2.5	2.5	2.6	2.6	2.6	2.2	2.4	2.5
India	4.9	4.2	4.3	4.7	4.7	5.1	4.7	4.5	4.7	4.7	4.7	4.3	4.5	4.7	4.6
Brazil	4.5	3.8	3.1	3.2	3.5	3.9	4.1	4.3	4.3	4.3	4.3	4.3	3.6	3.9	4.3
Russia	5.2	3.9	3.0	2.1	2.4	3.2	3.8	4.4	4.1	4.0	4.1	4.1	3.6	3.4	4.1
Monetary Policy Rate (% p.a.)															
Global	**3.2**	**3.2**	**3.1**	**3.1**	**3.2**	**3.2**	**3.3**	**3.3**	**3.5**	**3.6**	**3.6**	**3.6**	**3.1**	**3.3**	**3.6**
G10	**0.3**	**0.4**	**0.4**	**0.6**	**0.7**	**0.8**	**0.9**	**0.9**	**1.1**	**1.2**	**1.2**	**1.3**	**0.6**	**0.9**	**1.3**
United States	0.875	1.125	1.125	1.375	1.625	1.875	2.125	2.125	2.375	2.625	2.625	2.625	1.375	2.125	2.625
Euro Area	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.25	-0.25	-0.25	-0.25	-0.40	-0.40	-0.25
Japan	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
UK	0.25	0.25	0.25	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.25	0.50	0.75	1.25
EM	**5.4**	**5.3**	**5.1**	**5.0**	**5.0**	**5.0**	**5.0**	**5.1**	**5.2**	**5.2**	**5.2**	**5.3**	**5.0**	**5.1**	**5.3**
China	4.35	4.35	4.35	4.35	4.35	4.35	4.60	4.60	4.85	4.85	4.85	4.85	4.35	4.60	4.85
India	6.25	6.25	6.00	6.00	6.00	6.00	6.00	6.25	6.25	6.50	6.50	6.75	6.00	6.25	6.75
Brazil	12.25	10.25	8.25	7.00	7.00	7.00	7.00	7.50	8.50	8.50	8.50	8.50	7.00	7.50	8.50
Russia	9.75	9.00	8.50	7.75	7.50	7.25	7.00	7.00	6.75	6.75	6.50	6.50	7.75	7.00	6.50

Note: Global and regional aggregates for GDP growth are GDP-weighted averages, using PPPs. Japan CPI excludes VAT; Japan policy rate is the interest rate on excess reserves; CPI numbers are period averages. Global* and EM* Consumer Price Inflation Aggregates exclude Venezuela and Argentina. **Tracking estimate. ^The US core inflation number is core PCE.
Source: IMF, Morgan Stanley Research forecasts

Key debates in global economics

Our core views on the global economy

The global recovery is likely to gain momentum and breadth in 2018, supported by still accommodative monetary policy and more fiscal stimulus. With major economies at different stages of the business cycle, the risk of the global economy running too hot is limited though.

Growth – solid stride in DM, faster pace in EM: The global recovery is set to continue in 2018 and it is likely to broaden further as EM gains momentum. Maturing business cycles could cause DM growth to slow in 2019, but it should still stay above potential. US and China are late-cycle already, while the euro area and Japan are mid-cycle and EM commodity exporters only early-cycle.

Inflation – moving higher, but not beyond targets: While DM headline inflation is likely moving sideways over the forecast horizon, DM core inflation is likely to pick up in 2018. However, with the exception of the UK, DM inflation is unlikely to move above central bank targets. Meanwhile, EM inflation is set to rise, led by Asia.

Policy – less monetary expansion, more fiscal stimulus: Monetary policy is set to remain expansionary in 2018. Balance sheet reduction and additional rate hikes cause the Federal Reserve to inch beyond neutral, but only in 2019. Fiscal policy is likely to become more expansionary in several key DM economies, particularly the US.

Risks – faster inflation, tighter finances, trade protectionism: The key risk relates to estimating the remaining economic slack correctly and anticipating wage pressures as labour markets reach full employment. Overly rich asset valuations could cause tighter financial conditions. Lastly, a disruption in global trade could undermine the recent rebound in capex and productivity.

Country highlights

US: Midway through 2018, the US will ring in its tenth year of expansion. Though signs such as ultra-low unemployment, a positive output gap and rising interest rates continue to suggest the economy is late-cycle, a general lack of overheating in key sectors, such as housing, and rising productivity suggest this late-cycle phase has more room to run. A moderate fiscal boost also supports the macro backdrop in 2018, though its positive impulse fades somewhat in 2019. We expect the Fed to deliver three hikes in 2018, followed by a lengthy pause before hiking twice more in 2019, where we think the tightening cycle ends.

Euro area: We expect the euro area to grow by 2.1%Y in 2018 and 1.9%Y in 2019, with support from consumption and acceleration in capex. Our upwardly revised euro area forecast envisages three key shifts: the output gap turns positive, core inflation rises above its long-term average and the ECB ends QE after September 2018, with the first 15bp depo rate hike to -0.25% in March 2019.

Japan: Our constructive view on Japan's economy remains unchanged. In our latest outlook, we revised up our 2018 real GDP forecast to 1.3%Y from 1.1%Y, mainly on stronger exports and private capex. We think inflation has already bottomed with an improving output gap on the back of a tighter labour market and higher capacity utilisation rates. We expect the BoJ's first adjustment of the long-term rate target in Jul-Sep 2018, when we expect the core-core CPI (ex. fresh food and energy) to approach 1%Y.

China: We expect real GDP growth to moderate to 6.5%Y in 2018 from an expected 6.8%Y in 2017, and slow to 6.3%Y in 2019, as policy-makers' emphasis on growth quality over GDP targets means continued efforts on capacity cuts, leverage controls and housing curbs. That said, growth quality will improve with robust consumption and exports, and a major growth correction is unlikely amid a managed pace of policy implementation. The inflation dynamic should remain healthy amid a robust job market and multi-year capacity adjustments, while the debt/GDP ratio could achieve near-stabilisation by 2H19.

Brazil: The consumer should lead the economic recovery, due to strong fundamentals, even in the face of political uncertainty in 2018, but the sustainability of the recovery is more policy-dependent. Support should also come from some pick-up in investment, although at below historical levels. Inflation and rates should continue to be low amid a large output gap.

India: High-frequency indicators are showing that economic growth momentum gained further momentum in Nov-Dec. The recovery in end demand should lead to higher utilisation rates which, coupled with improving corporate return expectations, balance sheet fundamentals and a strengthening financial system, should lead to a recovery in private capital spending in 2018. This sets the stage for a fully fledged recovery in 2018. The cyclical growth recovery and normalising food prices should drive a pick-up in headline inflation. Against the backdrop of a better macro outlook, we expect the RBI to hike in the second half of fiscal year 2019.

Russia: We pencil in 2.3%Y GDP growth in 2018, supported by higher oil prices and increases in public sector wages. With average CPI slightly below 4%Y in 2018, we see the CBR gradually cutting rates to 7.00%. We are sceptical about government delivery of reforms after the presidential elections and expect growth to moderate to 1.8%Y in 2019.

For our global forecasts, see 2018 Global Macro Outlook: Stronger for Longer, November 26, 2017.

What's new in the global economy

In the US, retail sales were solid in December, with strength in core sales (0.4%M growth) indicating solid consumption growth through the end of the year. Our GDP tracker currently stands at 3.7%Q saar for 4Q17. Core CPI rose 0.3%M in December, raising the year-on-year rate to 1.8% from 1.7%. On the political side of things the US announced that it will be imposing a 30% tariff on solar panels and washing machines.

In the euro area, the dataflow came in mostly on the strong side, with industrial production rising 1.0%M and retail sales also printing solid gains at 1.5%M. Our GDP indicator now puts growth at 0.8%Q, or 3.1% on an annualised basis, in 4Q. The ECB minutes revealed that while the central bank's forward guidance will naturally change slowly, it could be revisited soon. In Germany the CDU and the SPD have reached a preliminary deal on the blueprint for formal coalition negotiations.

In China, real GDP growth held steady at 6.8%Y in 4Q17 and with this 2017 GDP growth reached 6.9%Y in real terms and 11.2%Y in nominal terms. Industrial production growth edged up to 6.2%Y in December (vs. 6.1%Y in November), as stronger utility production more than offset slightly weaker manufacturing production. Fixed asset investment (FAI) growth held steady at 7.2%Y YTD while retail sales dipped unexpectedly to 9.4%Y in December.

Key research highlights

Ahya, Chetan

Re-emergence of protectionism risks – assessing the impact

Trade protectionism has re-emerged as a concern. We believe that the response from Asia is likely to be measured, thus avoiding an exacerbation of trade frictions. The impact on overall trade growth in Asia would be manageable unless the situation escalates into a full-blown trade conflict. read more

Antonucci, Daniele

European Economics: The Inflation Surprise in Waiting

We're more bullish on Euro inflation than market pricing. We believe that it's close to rising again as economic slack diminishes, and is likely to surprise the consensus to the upside. We expect the ECB to end QE from October and hike the depo rate by 15bp to -0.25% in March 2019. read more

Feldman, Robert Alan

Japan Economics: Growth Policy in 2018 – Words and Numbers

The government has released its macro policies and budget for FY2018. The key goal is higher productivity. Are the FY2018 measures sufficient to reach the goal? We are skeptical. read more

Global risk calendar

Date	Time (Ldn)	Ccy	Event	Ref. Period	MS forecast	Market	Previous
25-Jan	9:00	NOK	Norges Bank Rates Decision		0.50%		0.50%
25-Jan	9:00	EUR	IFO Business Climate	Jan		117	117.2
25-Jan	12:45	EUR	ECB Deposit Facility Rate		-0.40%	-0.40%	-0.40%
25-Jan	15:00	USD	New Home Sales	Dec	752k	675k	733k
25-Jan	15:00	USD	New Home Sales (MoM)	Dec	2.6%	-7.9%	17.5%
25-Jan	15:00	USD	Leading Index	Dec	0.5%	0.5%	0.4%
25-Jan	23:30	JPY	CPI (YoY)	Dec		1.1%	0.6%
26-Jan	9:00	EUR	M3 (YoY)	Dec		4.9%	4.9%
26-Jan	**9:30**	**GBP**	**GDP (QoQ)**	**4Q A**		**0.4%**	**0.4%**
26-Jan	**13:30**	**USD**	**GDP (QoQ)**	**4Q A**	**3.7%**	**3.0%**	**3.2%**
26-Jan	**13:30**	**USD**	**Durable Goods Orders**	**Dec P**	**3.4%**	**0.9%**	**1.3%**
26-Jan	14:00	JPY	BoJ's Kuroda spks (Global Economic Outlook)				
26-Jan	14:00	GBP	BoE's Carney spks (Global Economic Outlook)				
01/27-02/03	N/A	EUR	German Retail Sales (MoM)	Dec			1.8%
29-Jan	13:30	USD	Personal Income	Dec		0.3%	0.3%
29-Jan	**13:30**	**USD**	**PCE Core (YoY)**	**Dec**			**1.5%**
29-Jan	13:30	USD	Personal Spending	Dec		0.5%	0.6%
29-Jan	N/A	COP	BDRC Rates Decision		4.50%	4.75%	4.75%
29-Jan	23:30	JPY	Unemployment rate	Dec			2.7%
30-Jan	**7:45**	**EUR**	**French GDP (QoQ)**	**4Q A**		**0.5%**	**0.6%**
30-Jan	**10:00**	**EUR**	**Eurozone GDP (QoQ)**	**4Q A**			**0.7%**
30-Jan	13:00	HUF	NBH Rates Decision		0.90%	0.90%	0.90%
30-Jan	13:00	EUR	German CPI (YoY)	Jan P			1.7%
30-Jan	**15:00**	**USD**	**Consumer Confidence Index**	**Jan**		**123.5**	**122.1**
30-Jan	23:50	JPY	Industrial Production (MoM)	Dec P			0.5%
31-Jan	**1:00**	**CNY**	**Non-manufacturing PMI**	**Jan**			**55.0**
31-Jan	**1:00**	**CNY**	**Manufacturing PMI**	**Jan**			**51.6**
31-Jan	**10:00**	**EUR**	**CPI Estimate (YoY)**	**Jan**			**1.4%**
31-Jan	13:15	USD	ADP Employment Change	Jan		170k	250k
31-Jan	13:30	USD	Employment Cost Index (QoQ)	4Q		0.6%	0.7%
31-Jan	**19:00**	**USD**	**FOMC Rate Decision (Upper Bound)**		**1.50%**	**1.50%**	**1.50%**
1-Feb	1:45	CNY	Caixin PMI Manufacturing	Jan			51.5
1-Feb	9:30	GBP	PMI Manufacturing	Jan			56.3
1-Feb	12:00	CZK	CNB Rates Decision		0.75%		0.50%
1-Feb	13:30	USD	Unit Labor Costs	4Q P		1.0%	-0.2%
1-Feb	15:00	USD	Construction Spending (MoM)	Dec		0.4%	0.8%
1-Feb	**15:00**	**USD**	**ISM Manufacturing**	**Jan**		**58.7**	**59.7**
1-Feb	21:00	CLP	CBCH Rates Decision		2.50%		2.50%
2-Feb	**13:30**	**USD**	**Change in Nonfarm Payrolls**	**Jan**		**165k**	**148k**
2-Feb	**13:30**	**USD**	**Unemployment Rate**	**Jan**		**4.1%**	**4.1%**
2-Feb	13:30	USD	Average Hourly Earnings (YoY)	Jan			2.5%
2-Feb	15:00	USD	Factory Orders	Dec			1.3%

Source: Bloomberg, MS FX Strategy Research. N/A Denotes timing approximate or not confirmed / All times and dates are Ldn time and correct as of the date of publication / For a full list of economic events, see the calendar on the Morgan Stanley Matrix Platform.*

Global economic dashboard

US

1. FOMC Preview: Where's the Snooze Button?

2. US Economics: What You Should Know About the Shutdown

3. US Economics: Business Conditions: Taxes Cut, Sentiment Up

Europe

1. Euro Data Comment: Flash PMIs: At a Cyclical High

2. European Economics Weekly: The ECB's Message

3. UK Economics Chartbook: Decision Time

Japan

1. Japan Economics: January MPM/Outlook Report Review

2. Japan Economic Calendar: High Interest in the Effects of US Tax Reform and Repatriation

3. Japan Economics: Reuters Tankan (January): Manufacturing Sentiment at 11-Year High

Asia Pacific

1. China Economics: Growth Remained Stable

2. India Economics and Strategy: Five Themes for F2019 Budget

3. S. Korea Economics: BoK on Hold; Taking It Slow

CEEMEA

1. CEEMEA Compass: Oil Swell

2. CEEMEA Explorer: Back to Macro - What Does 2018 Have in Store?

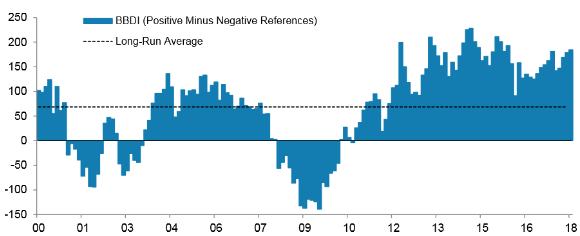
3. Turkey: CBT: Hoping for the Positive Scenario

Latin America

1. Week Ahead in Latin America: Brazil: Growth Gaining Traction

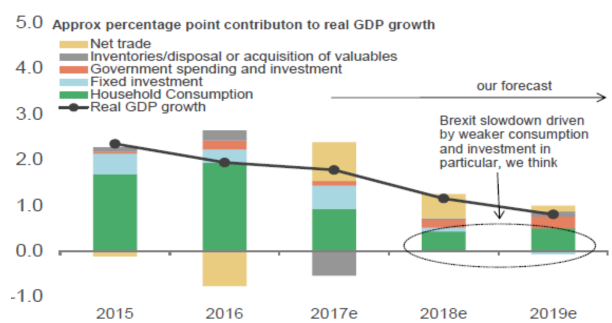
2. Week Ahead in Latin America: Latin America: While You Were Away

Exhibit 18: US: Morgan Stanley Beige Book Diffusion Index reached a two-year high



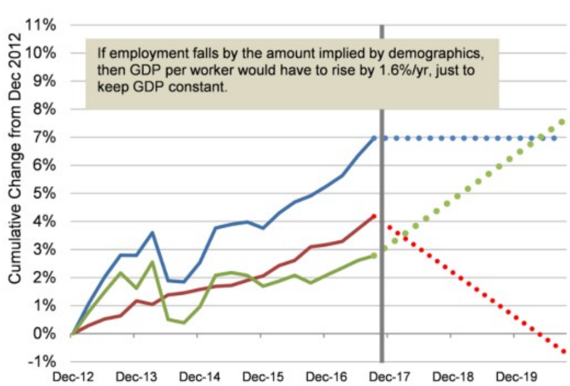
Source: Beige Book, Morgan Stanley Research

Exhibit 19: UK: Brexit slowdown to be driven by weakness in consumption and investment



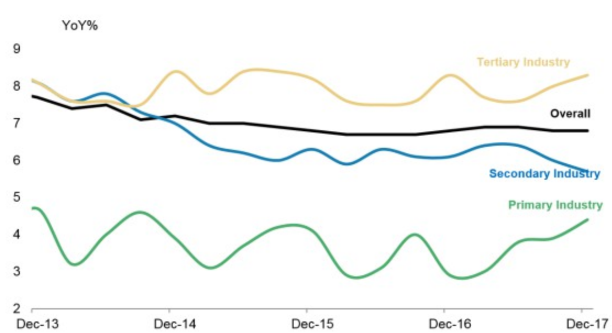
Source: ONS, Morgan Stanley Research forecasts

Exhibit 20: Japan: New economic policies would need to accelerate investment and productivity growth to offset demographics challenge



Source: Cabinet Office for GDP, Ministry of Internal Affairs and Communications for employment, Morgan Stanley Research

Exhibit 21: China: GDP growth held steady in 4Q at 6.8%Y



Source: CEIC, Morgan Stanley Research

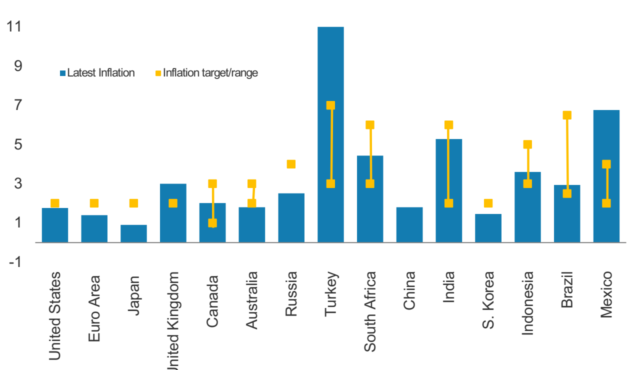
Inflation & central bank monitor

Exhibit 22: Inflation monitor and next policy moves by country

	Inflation target	Latest Month	12M MS Forecast	Next Rate Decision	Current Rate	Market Expects (bp)	MS Expects (bp)	Risks to our call
United States	2.0% PCE Price Index	1.8%	1.5%	31 Jan	1.375	0.0	0	-
Euro Area	< 2% HICP (u)	1.4%	1.9%	25 Jan	-0.40	0.2	0	-
Japan	2% CPI (u)	0.9%	1.5%	09 Mar	-0.10	0.2	0	-
United Kingdom	2%	3.0%	2.4%	08 Feb	0.50	1.0	0	Small probability of a hike
Canada	1-3%	2.0%	2.0%	07 Mar	1.25	5.2	0	-
Norway	2.5% CPI	1.1%	1.9%	14 Feb	0.50	0.1	0	-
Sweden	2.0% CPI	1.9%	2.1%	25 Jan	-0.50	-0.5	0	-
Australia	2-3% over the cycle	1.8%	2.6%	06 Feb	1.50	0.3	0	-
New Zealand	1-3% over the cycle	1.9%	2.7%	08 Feb	1.75	0.3	0	-
Russia	4% CPI, end-2017	2.5%	4.0%	09 Feb	7.75	-	0	25 bp cut
Poland	2.5% (+/- 1%) CPI	2.0%	2.0%	07 Feb	1.50	0.3	0	-
Czech Republic	2.0% (+/-1%) CPI	2.6%	2.2%	02 Feb	0.50	-	25	-
Hungary	3.0% CPI +/- 1%	2.5%	3.0%	30 Jan	0.90	0.0	0	-
Romania	2.5 (+/-1%) CPI	3.2%	3.3%	07 Feb	2.00	-	0	-
Turkey	5% (±2%)	11.9%	9.1%	07 Mar	8.00	-	0	-
Israel	1-3%	0.2%	0.9%	26 Feb	0.10	-0.5	0	-
South Africa	3 - 6%	4.6%	4.7%	28 Mar	6.75	-18.5	0	Moody's remains on hold and SARB cuts 25bps
Nigeria	6-9%	15.9%	12.6%	tbd	14.00	-	0	-
China	N/A	1.7%	2.5%	N/A	4.35	-	25	Evenly Balanced
India	2-6%	4.9%	4.8%	07 Feb	6.00	-	0	Risk of a cut given growth concerns
Hong Kong	N/A	1.5%	2.7%	01 Feb	1.75	-	0	Faster pace of rate hikes
S. Korea	2% CPI	1.5%	1.7%	27 Feb	1.50	1.0	0	Evenly Balanced
Taiwan	N/A	1.2%	1.2%	22 Mar	1.375	3.0	0	Evenly Balanced
Indonesia	3.5% +/- 1.0%	3.6%	3.8%	15 Feb	4.25	-	0	Evenly balanced
Malaysia	N/A	3.5%	2.7%	25 Jan	3.00	6.0	25	Evenly balanced
Thailand	2.5% +/- 1.5% CPI	0.8%	1.6%	14 Feb	1.50	2.0	0	Evenly balanced
Philippines	3% +/-1% CPI	3.3%	3.3%	08 Feb	3.00	-	0	Evenly balanced
Brazil	4.5% +/-2.0% IPCA	2.9%	4.1%	07 Feb	7.00	-21.0	0	-
Mexico	3% +/-1% CPI	6.8%	4.2%	08 Feb	7.25	16.1	25	-
Argentina	15% in 2018	24.8%	16.6%	NA	28.0	-	-	-
Chile	3% +/-1% CPI	2.3%	2.7%	01 Feb	2.50	-7.8	0	-
Peru	2% +/-1% CPI	1.4%	2.4%	08 Feb	3.00	-	0	-
Colombia	3% +/-1% CPI	4.1%	3.6%	29 Jan	4.75	-24.9	-25	-

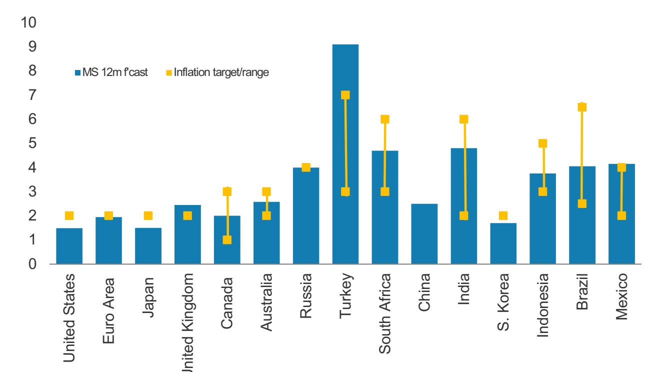
(u) = unofficial
Notes: Inflation numbers in red indicate values above target, green below; MS expectations in red (green) indicate our rate forecasts are above (below) market expectations. Japan policy rate is the interest rate on excess reserves.
Source: National central banks, Morgan Stanley Research forecast

Exhibit 23: Current inflation vs. target



Source: National data, Morgan Stanley Research

Exhibit 24: Inflation forecast vs. target



Source: National data, Morgan Stanley Research estimates

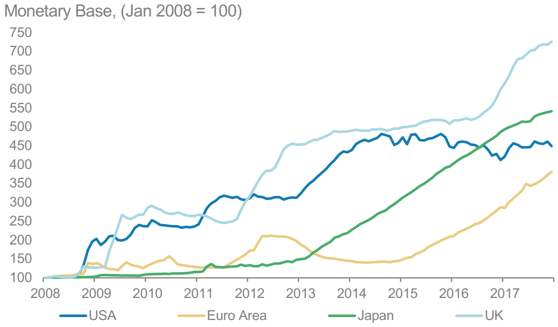
Monetary policy rate forecasts

Exhibit 25: Monetary policy rate forecasts, 2018-19E

	Current	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19	3Q19	4Q19
US	1.375	1.625	1.875	2.125	2.125	2.375	2.625	2.625	2.625
Euro Area	-0.40	-0.40	-0.40	-0.40	-0.40	-0.25	-0.25	-0.25	-0.25
Japan	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
United Kingdom	0.50	0.50	0.75	0.75	0.75	0.75	1.00	1.00	1.25
Canada	1.25	1.25	1.50	1.50	1.50	1.75	1.75	2.00	2.00
Norway	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25
Sweden	-0.50	-0.50	-0.50	-0.50	-0.50	-0.25	-0.25	0.00	0.00
Australia	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.75	2.00
New Zealand	1.75	1.75	1.75	2.00	2.25	2.50	2.75	3.00	3.25
Russia	7.75	7.50	7.25	7.00	7.00	6.75	6.75	6.50	6.50
Poland	1.50	1.50	1.50	1.75	2.00	2.25	2.50	2.50	2.50
Czech Republic	0.50	0.75	1.00	1.25	1.25	1.50	1.75	2.00	2.00
Hungary	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90	0.90
Romania	2.00	2.00	2.25	2.50	2.75	3.00	3.25	3.50	3.50
Turkey	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00	8.00
Israel	0.10	0.10	0.10	0.25	0.25	0.25	0.25	0.50	0.50
South Africa	6.75	6.75	6.50	6.50	6.50	6.50	6.75	6.75	6.75
Nigeria	14.00	14.00	13.00	13.00	13.00	13.50	14.00	14.00	14.00
Saudi Arabia	2.00	2.13	2.38	2.63	2.75	3.00	3.25	3.25	3.25
China	4.35	4.35	4.35	4.60	4.60	4.85	4.85	4.85	4.85
India	6.00	6.00	6.00	6.00	6.25	6.25	6.50	6.50	6.75
Hong Kong	1.75	2.00	2.25	2.50	2.50	2.75	3.00	3.00	3.00
S. Korea	1.50	1.50	1.75	1.75	1.75	1.75	1.75	1.75	1.75
Taiwan	1.375	1.375	1.500	1.625	1.750	1.750	1.750	1.750	1.750
Indonesia	4.25	4.25	4.25	4.50	4.75	4.75	4.75	4.75	4.75
Malaysia	3.00	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25
Thailand	1.50	1.50	1.50	1.50	1.50	1.50	1.75	2.00	2.00
Philippines	3.00	3.25	3.50	3.50	3.50	3.50	3.50	3.50	3.50
Brazil	7.00	7.00	7.00	7.00	7.50	8.50	8.50	8.50	8.50
Mexico	7.25	7.50	7.75	7.75	7.75	6.50	6.25	6.00	6.00
Chile	2.50	2.50	2.50	2.50	2.50	3.00	3.50	3.50	3.50
Peru	3.00	3.25	3.25	3.25	3.25	3.50	3.75	4.00	4.00
Colombia	4.75	4.25	4.25	4.25	4.25	4.75	5.00	5.00	5.00
Argentina	28.00				Under Review				

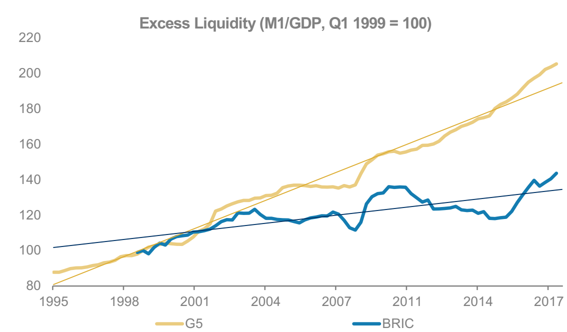
Source: Morgan Stanley Research forecasts

Exhibit 26: G4 monetary base



Source: FRB, BEA, ECB, Eurostat, BoJ, BoE, ONS, Morgan Stanley Research; 'Retail M4' used for UK.

Exhibit 27: G5 and BRIC excess liquidity



Source: National Sources, Morgan Stanley Research

Global GDP and inflation forecasts

Exhibit 28: Morgan Stanley real GDP and inflation forecasts, 2017-19E

	Real GDP (%Y)					CPI Inflation (%Y)				
	2017E	2018E		2019E		2017E	2018E		2019E	
	MS	MS	Cons	MS	Cons	MS	MS	Cons	MS	Cons
Global*	**3.6**	**3.9**	**3.8**	**3.8**	**3.7**	**2.6**	**2.9**	**2.8**	**2.8**	**2.8**
G10	**2.2**	**2.2**	**2.2**	**1.9**	**1.9**	**1.8**	**1.9**	**1.8**	**1.7**	**1.9**
US	2.3	2.7	2.6	2.1	2.2	2.1	2.1	2.2	1.8	2.2
Euro Area	2.3	2.1	2.2	1.9	1.8	1.5	1.8	1.5	1.6	1.6
Japan	1.7	1.3	1.3	1.5	1.0	0.5	1.3	0.9	1.0	1.0
UK	1.8	1.1	1.4	0.8	1.4	2.7	2.8	2.5	2.1	2.1
Canada	2.6	1.8	2.2	1.8	1.8	1.5	1.5	2.0	2.2	2.0
Norway	1.8	2.3	2.2	2.1	2.0	1.9	1.9	1.8	2.0	2.0
Sweden	3.1	2.8	2.5	2.0	2.2	1.8	1.3	1.8	2.6	2.1
Australia	1.9	1.5	2.8	2.5	2.8	2.0	2.3	2.2	2.7	2.3
New Zealand	2.7	3.7	3.0	3.0	2.7	1.9	2.3	1.9	2.4	2.0
EM*	**4.7**	**5.0**	**4.9**	**5.0**	**4.9**	**3.1**	**3.6**	**3.6**	**3.5**	**3.5**
CEEMEA	**2.4**	**2.7**	**2.5**	**2.6**	**2.7**	**5.8**	**5.6**	**5.6**	**5.3**	**5.6**
Russia	1.8	2.3	1.9	1.8	1.8	3.7	3.6	3.7	4.1	4.0
Poland	4.2	4.4	3.8	3.8	3.4	1.9	2.2	2.3	2.5	2.5
Czech Rep	4.5	3.8	3.4	3.0	3.0	2.5	2.5	2.3	2.1	2.0
Hungary	3.7	3.5	3.5	3.2	3.2	2.4	2.9	2.8	3.0	3.0
Ukraine	2.1	2.9	3.0	3.4	3.3	14.5	11.0	9.1	7.8	6.3
Kazakhstan	4.0	4.3	3.2	4.0	3.3	7.5	7.3	6.5	6.5	6.3
Turkey	5.6	3.2	3.8	3.7	3.9	11.1	10.0	9.5	8.4	8.7
Israel	3.2	3.1	3.3	3.4	3.1	0.3	0.6	0.8	1.6	1.1
South Africa	0.8	1.5	1.4	1.8	1.7	5.3	4.8	5.0	5.1	5.2
Nigeria	0.7	2.5	2.6	2.9	3.4	16.6	13.5	13.5	13.0	12.5
Saudi Arabia	-0.7	1.5	1.5	1.9	2.0	-0.1	2.9	3.4	2.5	3.0
AXJ	**6.1**	**6.2**	**6.2**	**6.1**	**6.0**	**2.2**	**3.0**	**3.0**	**3.0**	**3.0**
China	6.8	6.5	6.5	6.3	6.2	1.6	2.5	2.3	2.6	2.3
India	6.3	7.5	7.4	7.7	7.5	3.3	4.5	5.0	4.4	4.6
Hong Kong	3.6	3.0	2.8	2.5	2.6	1.7	2.7	2.5	3.1	2.5
Korea	3.1	3.0	3.0	2.7	2.8	1.9	1.7	1.9	1.7	2.0
Taiwan	2.7	2.9	2.5	2.6	2.3	0.2	0.8	1.2	1.2	1.3
Singapore	3.5	3.4	3.0	3.1	2.7	0.6	1.4	1.0	1.8	1.7
Indonesia	5.1	5.4	5.3	5.5	5.5	3.8	3.5	3.8	3.8	3.8
Malaysia	5.9	5.6	5.3	5.3	5.2	3.8	3.0	2.7	2.5	2.6
Thailand	3.7	3.8	3.7	3.5	3.7	0.7	1.9	1.4	1.3	1.7
Philippines	6.7	6.6	6.6	6.6	6.6	3.2	3.7	3.6	3.1	3.4
LatAm*	**0.8**	**2.2**	**2.3**	**2.6**	**2.5**	**4.3**	**3.9**	**3.7**	**3.7**	**3.7**
Brazil	0.7	3.1	2.5	3.4	2.5	3.5	3.8	3.9	4.2	4.2
Mexico	2.1	1.8	2.2	2.3	2.4	6.0	4.9	4.0	3.6	3.6
Chile	1.6	2.9	2.7	2.7	3.0	2.2	2.5	2.4	2.9	3.0
Peru	2.8	3.9	3.9	3.7	4.1	2.8	1.4	2.5	2.5	2.6
Colombia	1.6	2.3	2.6	2.8	3.0	4.3	3.7	3.4	3.6	3.2
Argentina	2.8	3.3	3.2	3.7	3.2	25.6	21.0	19.3	13.6	13.0
Venezuela	-15.6	-9.6	-4.7	-6.9	-2.3	1049.0	4073.5	1759.8	10428.3	1446.0

Source: IMF, Morgan Stanley Research forecasts. * Global, EM and LatAm CPI aggregates exclude Venezuela and Argentina.

Government budget balance and debt forecasts

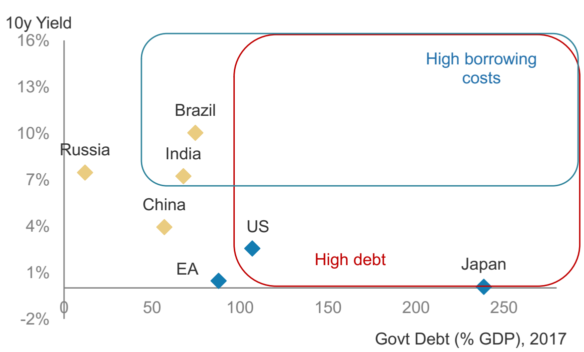
Exhibit 29: Budget balance, primary balance, gross and net government debt, 2016-19E

	General Gov't Budget Balance (% of GDP)				Primary General Gov't Budget Balance (% of GDP)			
	2016	2017E	2018E	2019E	2016	2017E	2018E	2019E
DM								
US	-3.1	-3.2	-4.4	-5.0	-1.8	-1.9	-2.9	-3.3
Euro Area	-1.5	-1.2	-1.4	-1.6	0.7	0.9	0.6	0.4
Japan	-4.2	-4.1	-3.4	-3.5	-4.0	-4.0	-3.5	-3.5
UK	-2.9	-2.4	-2.0	-1.7	-0.5	0.3	0.6	0.6
Canada	-1.9	-2.2	-1.8	-1.6	-1.2	-1.5	-1.3	-0.9
Sweden	0.9	1.1	0.9	0.9	1.3	1.3	1.1	1.1
Australia	-2.4	-2.1	-2.0	-2.1	-1.6	-1.5	-1.3	-1.4
BRICs								
Russia	-3.4	-2.0	-1.1	-0.7	-3.1	N/A	N/A	N/A
China	-3.8	-3.8	-3.8	-3.6	-2.9	N/A	N/A	N/A
India	-7.1	-6.2	-6.3	-6.0	2.1	1.7	1.8	1.4
Brazil	-9.0	-8.6	-7.9	-6.9	-2.5	-2.4	-2.2	-1.5

	Gross General Gov't Debt (% of GDP)				Net General Gov't Debt (% of GDP)			
	2016	2017E	2018E	2019E	2016	2017E	2018E	2019E
DM								
US	106.1	105.6	106.5	106.7	77.0	76.7	78.0	78.8
Euro Area	88.9	87.5	86.2	85.5	70.2	N/A	N/A	N/A
Japan	238.7	239.3	238.6	235.7	119.5	120.1	119.4	116.5
UK	88.2	86.5	86.3	86.3	53.2	51.0	50.9	50.8
Canada	92.4	89.6	87.7	85.8	27.4	24.6	22.7	20.9
Sweden	42.2	39.1	36.4	34.1	-29.5	N/A	N/A	N/A
Australia	25.4	28.7	29.9	31.5	17.9	18.6	20.1	21.4
BRICs								
Russia	12.9	13.5	14.9	15.0	N/A	N/A	N/A	N/A
China	47.2	47.1	47.8	48.6	N/A	N/A	N/A	N/A
India	68.0	66.8	65.3	63.4	N/A	N/A	N/A	N/A
Brazil	69.5	74.0	75.0	78.8	47.5	55.3	57.6	63.6

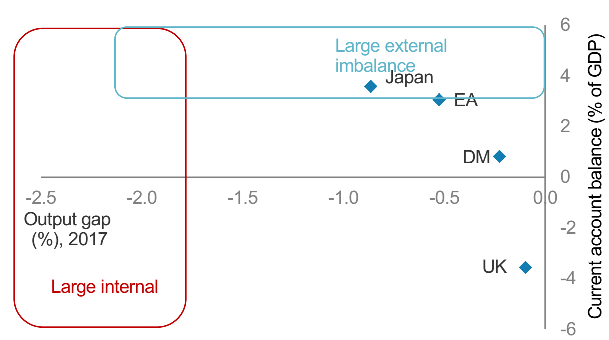
Source: IMF, Morgan Stanley Research forecasts. Note, US government debt forecasts don't currently reflect recent changes to the budget deficit forecasts.

Exhibit 30: G3 and BRIC government debt and 10Y yield



Source: IMF forecasts, Morgan Stanley Research

Exhibit 31: G3 fiscal space – output gap and C/A balance



Source: IMF forecasts, Morgan Stanley Research

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