

Global Economics Team

Morgan Stanley & Co. International plc

Coordinators of this publication

Manoj Pradhan

Manoj.Pradhan@morganstanley.com

+44 (0)20 7425 3805

Patryk Drozdziak

Patryk.Drozdziak@morganstanley.com

+44 (0)20 7425 7483

Pratyancha Pardeshi

Pratyancha.Pardeshi@morganstanley.com

+44 (0)20 7677 0528

Global

May 4, 2016

The Global Macro Analyst

The Greenback – Back in the Green?

The US is the only economy that can absorb currency strength. The resilience of its domestic economy is rooted in an internal rebalancing that most of the rest of the world has not yet completed. US dollar strength has been a reflection of the relative improvement in the US compared to the rest of the world, as well as a conduit for the US assisting the rest of the world in its rebalancing by importing global deflationary pressures.

Our FX team has described USD weakness as a correction that has interrupted a secular **bull run for the dollar – one that is yet to run its course.** Such a path, we argue, is not only likely, but also necessary if the rest of the world outside the US is to rebalance.

In today's note, we address **three** questions:

1. Is the US economy really in a position to absorb further dollar strength? Inflation has disappointed, the manufacturing sector has seen recessionary conditions and the shale sector has been in outright recession.

2. How will the rest of the world deal with USD strength? The euro area and Japan will likely welcome it, but what about China? Won't EM economies with high inflation find USD weakness a welcome, disinflationary relief?

3. Why do we argue that fundamentals and the needs of rebalancing will lead to a stronger US dollar? What are the benign and malign paths to a resumption of dollar strength?

Risks of Secular Stagnation Higher in DM-like EMs and Euro Area, Lower in the US and Japan

	US	Japan	EA	DM-like EMs
Real Rates > GDP Growth?	●	●	●	●
Real Rates > Equilibrium Rates?	●	●	●	●
New Structural Excess Capacity?	●	●	●	●
Excess Capacity Financed by Debt?	●	●	●	●
Monetary/Fiscal Room to Ease?	●	●	●	●

Note: Legend from lowest risk to highest risk ● ● ● ● ●
Source: Morgan Stanley Research

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	Real GDP (%)			CPI inflation (%)		
	2015E	2016E	2017E	2015E	2016E	2017E
Global Economy	3.1	3.0	3.4	2.5	2.4	2.8
G10	1.9	1.5	1.6	0.2	0.8	1.9
Emerging Markets	4.1	4.0	4.7	4.3	3.7	3.4
EM ex-China	2.5	2.7	3.7	6.0	5.2	4.8
MW Global*	2.5	2.3	2.8			

Note: The above aggregates are PPP-weighted. EM and EM-ex-China CPI excludes Argentina and Venezuela. Source: Morgan Stanley Research forecasts

For important disclosures, refer to the Disclosures Section, located at the end of this report.

Outlook

The Greenback – Back in the Green?

Let's face it – the US economy is the only large economy in the world that can absorb a stronger currency: China, the euro area and (perhaps to a lesser extent) Japan are all ill-equipped to deal with a stronger currency, but there are important differences among them on this matter. A large chunk of EM-like EM economies have further to go in their adjustment to a new model of growth, and stronger currencies could tempt central banks to deviate from the commitment to adjusting they have shown over the last year. A weaker US dollar simply isn't in the interest of the rebalancing that the rest of the world needs.

USD weakness has helped to reduce risk perceptions around China at a difficult time earlier this year, but the longer that US dollar weakness persists, and the weaker the dollar gets, the more unsettled the world could become. Why? In a nutshell, dollar strength was pushing global rebalancing through in a way that only a globally coordinated policy initiative could have achieved otherwise. USD strength was a great vehicle for correcting the relative growth differential between the US and the rest of the world. Strong US growth, the result of a more advanced internal rebalancing, lets other economies rebalance as the US absorbs some of their disinflationary pressures.

Our FX strategy team has described current US dollar dynamics as a correction ensconced within a secular bull run that is not yet complete (see [FX Pulse: Temporary USD Weakness](#), April 14, 2016). In today's note, we argue that the team's description of the dollar's trajectory is not only likely to materialise, it is also far more supportive of global rebalancing than a weaker dollar.

The needs of rebalancing will probably drive us back towards a resumption of a USD bull run that our FX team expects, but whether this happens in a benign way (through better US growth) or a malign way (through more disruption in other key economies) remains to be seen.

Why the US Can Absorb USD Strength

It's not unambiguous, given the ebbs and flows of the macroeconomy, but the US is still in good shape to absorb USD strength going forward. While new questions have risen over the US housing cycle, some of the risks of the past are unlikely to be repeated. There are five reasons why USD strength is more likely to be absorbed by the US without a worrisome disruption of domestic dynamics:

1. Structural risks to growth are the lowest among most DM and EM economies: The worst of deleveraging is in the rear-view mirror, and secular stagnation risks are the lowest among key DM and EM economies (see [The Global Macro Analyst: Secular Stagnation and Negative Interest Rates – Is There an Alternative?](#) March 4, 2016).

2. If housing is the business cycle, cyclical risks are low too: Only two out of the last nine recessions in the US have occurred without a downturn in the housing market. Our US housing team argues that the housing cycle is still intact, despite recent concerns about the rental space (see [Sunday Start](#), May 1, 2016).

3. A bigger impact through imported deflation, not exports: Exhibit 2 shows that imported deflation (core goods inflation) has been responsible for the unconvincing path that US inflation has taken. Domestically generated services (ex-healthcare) inflation has been rock-solid for the last few years, suggesting that imported disinflation has been absorbed quite well by the rest of the economy. Export weakness, as Exhibit 3 shows, has been linked much more to China's growth shock and the resulting collapse in commodity prices than to economies whose currencies weakened against the US dollar.

4. Shale shock unlikely to happen again: The US shale sector, much like its brethren in commodity-producing EM economies, has been in a deep recession since the China shock materialised in early 2015. The combination of the China shock and a strong US dollar clearly played an important role in the damage that US shale has witnessed, but such damage is unlikely to play out again. The future damage to the domestic economy in the US is thus likely to be more limited.

5. The Fed is now more sensitive to USD strength and to weakness among its key trading partners: It was a lesson learned the hard way, but from a solitary mention in its statement in early 2015 to staying on hold in 2016 citing "international risks", the Fed is far more attuned to external events that could feed back to the US economy (see [The Global Macro Analyst: The US Monetary Trinity](#), April 6, 2016). A stronger US dollar has been on its radar for far longer, and the combination of the two should keep monetary policy accommodative for longer.

Perhaps the bigger question around dollar strength is not whether the US economy can handle it, but whether China would once again start seeing downside risks if the dollar was stronger thanks to the close links of the renminbi to the greenback.

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What Would a Stronger US Dollar Do to China Risks and Rebalancing?

China risks could rise again, but the origin of China's disinflationary risks is primarily domestic, with capital outflows the symptom of the pain that resulting high real rates have caused. US dollar appreciation is more likely to push policy-makers to address these issues, and we have seen in 2016 that our argument that lowering real rates need trigger neither FX depreciation nor capital outflows can hold true.

China risks could rise, but they can be dealt with: If the renminbi strengthens along with the dollar and against other currencies, disinflationary risks could intensify. This would raise real rates, hurt domestic asset prices and create the risk of capital outflows again. We've seen this movie before, but precisely because we've seen it, policy-makers should be able to deliver a better strategy for addressing these concerns. For example, breaking the 'impossible trinity' or the 'trilemma' has usually meant stricter controls over the capital account in China. More importantly, the path towards defusing the risks from a stronger US dollar is very well aligned with the needs of rebalancing in China.

The path to rebalancing will lower the risks that a stronger US dollar could create: Two years ago, shutting down excess capacity in some key sectors was not a priority for policy-makers. The growth shock to China's manufacturing has changed all that. Deleveraging, shutting down disinflationary excess capacity and creating easier monetary conditions to absorb those shocks are all now better aligned into a more composite strategy (see [Asia Economics: Five-step Solution to Manage Asian Deflation Risks](#), June 2, 2015).

A stronger US dollar should put more pressure on policy-makers to go down the path to rebalancing: If they do, monetary easing and better sentiment regarding fundamentals could provide some support for domestic assets. Even if the renminbi depreciates against the US dollar or on a broader basis in such an environment, the result need not be capital outflows.

The story is far clearer for the euro area and even Japan – USD weakness hurts.

FX Strength Is Bad News for the Euro Area and (Somewhat Less So) Japan

Investors are so attuned to this part of the argument that very little needs to be said:

- The **euro area** faces disinflationary risks at home and is exposed to external shocks. We have argued that secular stagnation risks are higher in the euro area than in the US, UK and Japan. For example, the improvement in the overall euro area masks the vast differences within, with a closed output gap in Germany, a rapidly closing one in Spain but far less impressive progress in France and Italy. Domestic dynamics in the euro area are therefore likely still creating a disinflationary impulse. External risks, particularly from EM, also create a large impact on the euro area, given the strong linkages of the corporate sector to the EM world. A strong currency creates an unwanted deflationary impulse on top of these disinflationary drivers.
- **Japan** has fewer structural risks than the euro area, but FX strength puts the nascent recovery in inflation dynamics at risk. Secular stagnation risks are lower in Japan than in the euro area. The output gap has been closed for a while and is now mildly positive, creating a moderately inflationary environment that has helped domestically generated inflation to remain resilient thus far. Even though most of the deflationary components of inflation can be traced to external shocks, FX strength will make it hard for inflation to remain steady, given that growth isn't improving at a pace anywhere close to that of the US.

The story is less clear-cut for EM economies. There are near-term benefits of a weaker US dollar, but we argue that a sustained dollar depreciation will hurt EM more than it will help.

Euro and particularly yen strength creates significant downside risks for domestic growth and inflation. EM-like EMs would appreciate some relief through USD weakness, but that would leave their domestic adjustment incomplete.

EM: FX Weakness Needed to Complete the Adjustment

In the near term, EM FX strength for the EM-like EM economies outside North Asia brings some welcome relief: Years of sustained FX depreciation and terms of trade pressure on commodity exporters in particular have raised inflation expectations and pushed policy-makers into delivering tighter monetary policy. Should the US dollar depreciate for a while longer, some disinflationary relief would be welcomed by policy-makers in highinflation economies. But would that help them turn the corner structurally? We don't think so.

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The Global Macro Analyst

Broken growth models and the great EM unwind: We have long argued that EM economies need to fix their broken growth models (see [Emerging Issues: Can the Broken EM Growth Models Be Fixed?](#) September 24, 2012). The path to that adjustment is through a triple unwind of: i) US real rates or the US dollar; ii) China's leverage and the demand for commodities; and iii) EM credit through higher real rates at home (see [The Global Macro Analyst: The Great EM Unwind](#), August 7, 2013).

The adjustment differs for EM-like and DM-like EMs: We are always careful to distinguish between EM-like EMs (the ones that depend on external funding and are fighting inflationary risks) and DM-like EMs in North Asia (that have current account surpluses, not deficits, and face disinflationary pressures). A change of the growth model in the former requires facing up to the triple unwind through higher real rates, while the latter need to respond with lower real rates while deleveraging and reducing domestic excess capacity. Most of the arguments we have made with respect to China will hold for DM-like EMs, so we focus on the EM-like EMs here.

A change in view last April after three years: After being consistently critical of the EM growth model since autumn 2012, we argued last April that this multi-year adjustment cycle was in its last phase of adjustment, particularly for the EM-like EMs – the adjustment for the DM-like EMs will be much more drawn-out. But for that adjustment to reach its end, we need the triple unwind to reassert itself, and US dollar strength is an important element of that story. The shock to China's manufacturing sector in 1Q15 has created long-lasting weakness in EM domestic demand and USD strength has created inflationary risks. Central banks have responded through tighter policy, which is a welcome development as it pushes the adjustment process in the right direction despite external tailwinds.

An internal inflection is needed: Put very simply, what we need is for the domestic fundamentals to turn around on their own merit, rather than look attractive thanks to external factors. Economies like India, Indonesia and Mexico have turned the corner and now have a new growth model in place; Russia has discarded its old model of growth and has passed the worst point of its recession back in September 2015 (see [Economics and Strategy: Is it Time to Become EM Bulls?](#) September 22, 2015); and Brazil has completed two out of the three legs of its adjustment cycle. Almost everyone else among the EM-like EMs has yet to turn the corner. In particular, Turkey and (to a lesser extent) South Africa have a long way to go.

To get Brazil, Turkey and South Africa away from their old models of growth and closer to a new one, we need the triple unwind to reassert itself. Economies that have already inflected can afford to run a more independent policy regime, while those that have not replaced their old model of growth will likely remain under pressure until they do.

But will the needs of rebalancing triumph? Will fundamentals drive a return to US dollar strength? We think so.

A Return to USD Strength? How?

There are two paths to US dollar strength – a benign one (through better US growth) and a malign one (through disruption in the euro area, Japan and EM).

A benign return to US dollar strength – through better US growth: Besides all the points of resilience that we have noted earlier in the note, international risks have dissipated – China has stabilised its growth while the housing market has shed excess inventory rapidly, euro area growth is holding up better, and Japan weakness has been driven a fair bit by the tragic earthquake. The recent run of the dollar could provide some support for not only imported inflation but also the beleaguered manufacturing sector. If the pick-up in manufacturing and non-manufacturing PMIs is sustained, and the Fed stays behind the curve, the US dollar may resume its ascent and growth in the US should once again outperform its DM and EM peers (see [The Global Macro Analyst: The US Monetary Trinity](#), April 6, 2016).

The malign path would be through disruption in the euro area, Japan and EM too: Euro and particularly yen appreciation have already raised concerns around growth. Growth holding up better in the euro area and recent ECB action have assuaged many investor concerns, but concern about Japan's economy is growing. Should sentiment deteriorate further, either policy action or a pass-through of poor sentiment into economic fundamentals could lead to a resumption of yen weakness against the US dollar.

EM central banks, as we noted earlier, have thus far resisted reacting to a weaker US dollar, but should they move prematurely into easier monetary policy, some of the good work they have done this year could be undone. An interrupted rebalancing is likely to be unconvincing, leading possibly to weaker EM currencies.

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The Global Macro Analyst

Exhibit 1

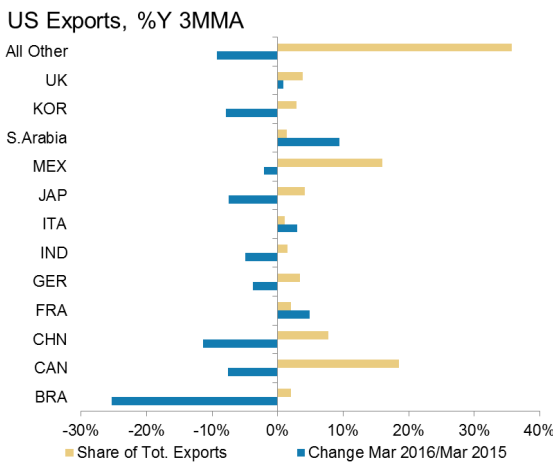
Risks of Secular Stagnation Higher in DM-Like EMs and Euro Area, Lower in the US and Japan

	US	Japan	EA	DM-like EMs
Real Rates > GDP Growth?	●	●	●	●
Real Rates > Equilibrium Rates?	●	●	●	●
New Structural Excess Capacity?	●	●	●	●
Excess Capacity Financed by Debt?	●	●	●	●
Monetary/Fiscal Room to Ease?	●	●	●	●

Note: Legend from lowest risk to highest risk
Source: Morgan Stanley Research

Exhibit 3

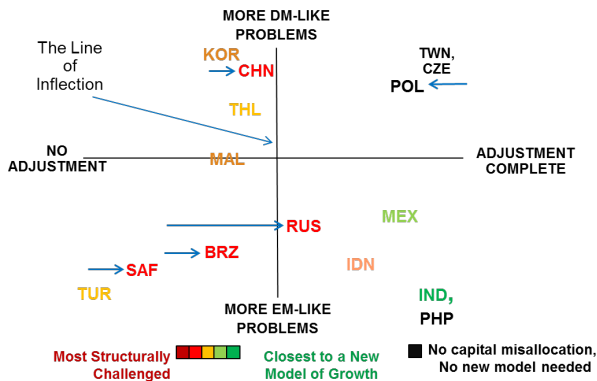
China's Indirect Impact on US Growth



Source: BLB, Census Bureau, US Economics Team, Morgan Stanley Research forecasts

Exhibit 5

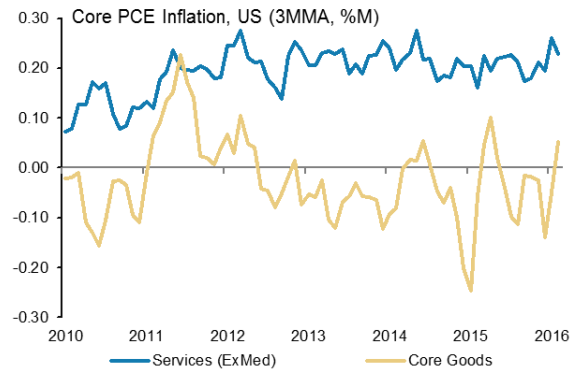
EM Adjustment Faster in EM-like EM Economies



Source: Morgan Stanley Research

Exhibit 2

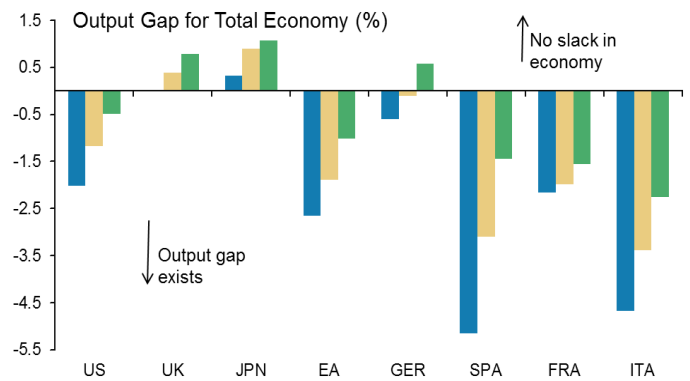
Imported Deflation Driving Core PCE Lower, While Domestic Services Inflation Remains Strong



Source: Bureau of Economic Analysis, US Economics Team, Morgan Stanley Research

Exhibit 4

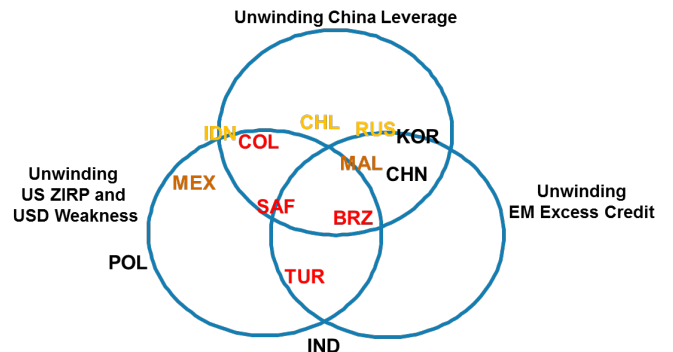
Output Gaps Almost Closed in the US, UK, Japan, but Vary in the Euro Area



Source: OECD estimates, Morgan Stanley Research

Exhibit 6

EM Needs to Face the Great EM Unwind



Source: Morgan Stanley Research

Spotlight: Life After Debt

Manoj Pradhan (44 20) 7425 3805
Charles Goodhart (44 20) 7425 1954
Patrik Drozdziak (44 20) 7425 7483

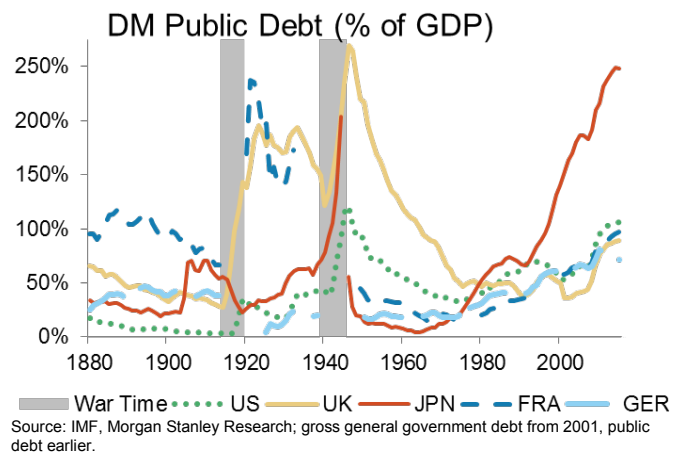
Charles Goodhart is a Senior Economic Consultant to Morgan Stanley

The great irony of the Great Financial Crisis is that a crisis borne out of indebtedness has spawned even more leverage in its wake. In fact, debt has never before increased this rapidly in peacetime. However, contrary to popular belief, it has not yet created a serious drag on global growth. But this can't continue forever. Why? Debt, we argue, is a symptom of structural and cyclical forces that raised the ability and willingness to lend and borrow. As these dynamics change course gradually, the drag from debt should rise materially over the next 3-5 years.

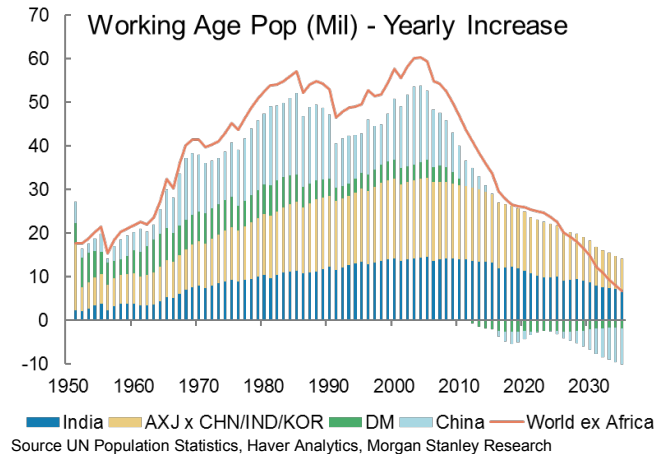
In this note, we address **three questions**:

- 1. Why has debt not been a serious drag yet, and why will the drag appear in the future?** What is the genesis of debt – if we can explain why debt has been rising since the 1980s, could we also unlock the trajectory of debt in the future?
- 2. Are we heading for another debt crisis – what form will the drag from debt take?** Debt is hardest to deal with if it has financed non-performing assets (NPAs). If the last 15 years of the debt supercycle can be deconstructed into three 'waves' according to the NPAs they financed (or not), will the toxic debt mix that led to the Great Financial Crisis show up again?
- 3. How do we delever? Addressing solvency, state contingency or collateral issues:** Are the historical remedies of debt erosion and debt forgiveness available to deal with solvency? Why is dealing with state contingency by creating equity-like instruments **our preferred mode of deleveraging**? Are GDP warrants and China's debt/equity swaps for banks a step in the right direction? Could making the leverage permanent help to 'over-collateralise' debt, and could this happen early in a benign way or only later when uncertainty has already risen?

Debt Has Never Risen This Much in Peacetime



As Demographics Turn, Upward Pressure on Interest Rates Will Increase the Drag from Debt



For full details, see [Global Issues: Life After Debt](#), April 27, 2016.

Global Macro Watch

Global: Next Stop: More Fiscal Easing and de Facto Helicopter Money?

Chetan Ahya (852) 2239 7812
Global Economics team

With global growth already tracking below the recession threshold of 2.5% for the past two quarters, we expect more debate and action on employing an activist fiscal policy stance or even de facto 'helicopter money'.

Fighting demand deficiencies with just monetary policy thus far: The global economy continues to face the challenges of demand deficiencies and deflation risks. Policy-makers are fighting this battle with a heavy reliance on monetary policy. While there are still tools available, there are increasing questions over their effectiveness.

Fiscal policy – a useful complement: With the private sector still in deleveraging mode and financial systems still hesitant to extend credit, we think that the debate on the use of fiscal policy will intensify. Indeed, we view fiscal policy or even de facto helicopter money as an effective tool to boost aggregate demand directly. To be sure, we are not arguing that the use of fiscal policy itself will lead to a sustained growth recovery, nor can it be a substitute for structural reforms.

Why a complementary use of fiscal and monetary policy is important – lessons from Japan: While both monetary and fiscal policy have been employed, they are rarely used in tandem. The BoJ has moved to a more aggressive monetary easing stance since 2013 and finally brought real interest rates into negative territory, and this initially brought the turn of the inflation trajectory and private sector leveraging. But policy-makers tightened fiscal policy prematurely, with the fiscal deficit narrowing by almost 4% of GDP over the course of three years, resulting in a slippage of growth and inflation.

Intensity of deleveraging challenge mirrors need for fiscal support – fiscal policy stance to turn more expansionary: These issues are most keenly felt by the five economies of the US, Europe, Japan, UK and China. Japan is at the forefront, and we expect a fiscal response soon. Europe is already pursuing a moderately expansionary fiscal policy. China has taken up fiscal expansion but the continued bias towards boosting investment means that deflationary pressures could persist. In the US and UK, we expect only a mild increase in the fiscal deficit, but active fiscal policy will be needed if the recent weakness in private spending is sustained.

For full details, see [Global Economics: Next Stop: More Fiscal Easing and de Facto Helicopter Money?](#) May 3, 2016.

US: Travel Log: Dominant Themes

Ellen Zentner (1 212) 296 4882

On my latest trip through Europe, conversations were dominated by thematic topics rather than monetary policy. Risks around Brexit and the US election cycle were also popular. Below I offer some thoughts:

Tracking voices: Working in Times Square, Manhattan, while conveniently centrally located can also feel like a trip to the circus when venturing outside the office. Nevertheless, I leave the office quite often to visit clients, eat, shop, and sometimes play the tourist role myself. While walking around I listen to the accents, observe the people – after all, people-watching is one of the great pastimes of New Yorkers.

In the shops I pay close attention to the languages spoken: The concentration of accents reveals a good deal about global flows themselves. For example, leading up to 2008 there was an incredible amount of British accents around Rockefeller Center. The United States was on sale at half price and British shoppers were snatching up shoes, handbags, and other goods galore. After 2008, Portuguese became the dominant language. Global flows into EM lifted the Real to new heights and reports of Brazilians snapping up Miami real estate were abundant.

Today, can you guess what the dominant language is? Midwestern: That's to say, good old generic American English. The meteoric rise in the US dollar from late 2014 through January of this year has been a boon for the domestic US consumer, but has put a dent in foreign arrivals into the US. According to consumer spending data from the Bureau of Economic Analysis, spending on foreign travel by US residents increased by 14% in 2015 (double the pace of growth in the prior year), while the latest tourism data suggests visitation from Canada dropped the most. Our consumer economist, Paula Campbell Roberts, tracks over 300 categories of consumer spending. This factoid and many others are presented in our annual exercise, [What Consumers Want](#).

Read on for more details on frequently asked questions.

For full details, see [US Economics: Travel Log: Dominant Themes](#), April 26, 2016.

May 4, 2016
The Global Macro Analyst

Global Macro Watch

Japan: BoJ's No Action Shock: What Next, What Impact?

Robert Alan Feldman (81 3) 6836 8400
Takeshi Yamaguchi (81 3) 6836 5404

BoJ delays timing to hit the price target, but takes no action: Contrary to our expectations, the BoJ decided to leave policy unchanged at its April meeting. That said, the BoJ also postponed the timing when it expects to reach the 2% price target from “the first half of FY2017” to “during FY2017”, an effective postponement of half a year. As downside risks to the real economy and to prices strengthen, the BoJ's lack of extra easing is simply inconsistent with Governor Kuroda's statement that “If necessary to hit the 2% price target, we will not hesitate to take additional measures.” Moreover, this decision will only deepen doubts among investors on whether the BoJ has any further means of easing, and thus could reduce market confidence in the BoJ.

Next monetary steps before July: At the moment, we'd like to maintain our view that the BoJ could well take additional easing before the July Upper House election, as our base case scenario. The BoJ's action at the June 15-16 policy meeting could be perceived by markets as coordinated easing with fiscal policy after the G7 Ise-shima summit (May 26-27). Kuroda said at the press conference that the BoJ judged it time to watch the impact of NIRP for now. That said, he also said that it would not take 6 or 12 months to see the impact of NIRP, although a period of 1 or 2 months is too short. He also emphasised that, if judged necessary, the BoJ could potentially move at “each meeting”, which he did not say in the previous post-MPM press conferences.

Is the BoJ behind the curve? However, having kept policy unchanged this time while deferring the timing of achievement of the price target, additional easing at the next meeting would mean that the BoJ had not taken pre-emptive action, and would give an impression of being behind the curve. Moreover, should the BoJ take additional easing measures just before the July Upper House election, there would be a stronger impression that monetary policy was being used arbitrarily for political goals. As a risk scenario, we thus see a possibility that the BoJ could remain on hold until after the July Upper House election, depending on markets and incoming economic data.

The lack of action increases the pressure on fiscal and growth policies to support the economy: We now think that the size of any upcoming fiscal package will increase, and that the likelihood of postponement of the consumption tax hike, scheduled for April 1, 2017, has increased further.

For full details, see [Global Economics and Strategy: BoJ's No Action Shock: What Next, What Impact?](#) April 28, 2016.

Sweden: Adding to QE

Daniele Antonucci (44 20) 7425 8943

Extra policy easing in the pipeline: The Riksbank left its key policy rate unchanged at -0.50%, in line with expectations, and upped its purchases of governments bonds by a further SEK 45 billion in 2H16, to include linkers too. We'd argued that extra asset purchases were possible, but the bar was high, as the Riksbank was already set to own about one-third of the bond market, and other pools of assets are small. Yet the bank believes that, while inflation is rising, the upturn is slow and that “with continued expansionary monetary policy abroad, there is a risk that the krona will appreciate earlier and faster”.

Maintaining an easing bias: Even though we see it less likely that further monetary policy stimulation will be needed in the period ahead, as economic activity strengthens and inflation approaches the target, the Riksbank stands ready to counteract any negative surprise and do more to meet the inflation target, even between ordinary monetary policy meetings. The bank hints there's still scope to cut the repo rate further, although to us this looks more like an outside scenario. If necessary, asset purchases could be extended, and the bank is also prepared for FX intervention if the krona appreciates so quickly as to threaten the upturn in inflation.

Inflation expectations: What do they tell us? The Riksbank monitors various measures of inflation expectations very closely. They are an important factor in price-setting and wage formation, and in this way affect how actual inflation develops going forward. At the same time, however, there's a feedback loop such that actual inflation also affects inflation expectations, particularly in the short term. The correlation between expected inflation two years ahead according to Prospera's survey and CPI is relatively high. But inflation expectations are not so closely correlated with future inflation.

'Structural changes' forthcoming: In the medium term, the Riksbank response function may well change, as the bank is considering the reintroduction of ‘tolerance’ bands around the inflation target. This could make things easier if it takes longer to boost prices, as in the current situation. And it looks as if the Riksbank is open to changing the variable for the inflation target from CPI to CPIF. If the bank had *already* targeted CPIF, it would have been less worried about the sluggish improvement in inflation, and therefore somewhat less dovish, as this would have been driven, in part, by the interest rate cuts themselves.

For full details, see [Riksbank Watch: Adding to QE](#), April 21, 2016.

Global Macro Watch

Australia: Mayday from the RBA

Daniel Blake (61 2) 9770 1579
Chris Nicol (61 3) 9256 8909
Morgan Stanley Australia Limited

Couldn't wait for clear air – rate cut to 1.75%: We have long been in the camp that the RBA would be forced to cut rates below 2%, but admit the timing has been difficult to call. We think the RBA initially waited longer than we expected to confirm the success of 'supervisory actions' in reining in the housing boom, and we also saw an increasingly hawkish reaction function emerge through 4Q15-1Q16 as the hurdle for cuts was lifted. Before this meeting, we thought that despite the weak 1Q16 inflation print, the RBA would point to still mixed (rather than outright negative) macro indicators and hold at 2.00% until finding clearer air for cuts in August and November (i.e., outside of the Budget/election period). The fact that, after an extended pause, the RBA didn't wait another quarter suggests a material softening in the bank's outlook.

Statement flags downgrades: Ahead of Friday's detailed Statement on Monetary Policy, the short Governor's statement flagged that growth is continuing "probably at a more moderate pace", and "labour market indicators have been more mixed of late". The statement specifically noted that the housing market risks posed by a lower cash rate have been mitigated by the effect of supervisory (macroprudential) measures on lending standards and dwelling price pressures. And while consumer trends weren't specifically mentioned, we would not be surprised if the RBA's business liaison programme also relayed some concern about trading conditions from March onwards, which we believe have softened.

Disinflationary dynamics: The low 1Q16 inflation print was a key catalyst and showed broad-based weakness. The bank's preferred underlying measure came in at 1.5%Y, and we expect its inflation profile to be cut by some 0.5pp right through 2016. Our measure of private non-tradeable inflation was even weaker at 1.3%Y in 1Q16. Further out, with soft wage trends and an ATWI above its 12-month average, the RBA may have been looking at inflation at/below 2%Y into 2017.

We retain 1.50% trough; next step Budget: We expect another cut in August, following the quarterly pattern that has been a feature of the post-2011 era. In our base case, a 1.50% trough should manage to deliver a still-bumpy growth transition, although much will depend on how this passes through the housing market (given tighter credit standards), as well as whether the RBA finds any support from fiscal policy and reform in 2H16.

For full details, see [Australia Macro+: Mayday from the RBA](#), May 3, 2016.

China: How Long Will This Recovery Cycle Last?

Chetan Ahya (852) 2239 7812
Junwei Sun (852) 2239 7820
Yin Zhang (852) 2239 7818

Recent data points have confirmed a further pick-up in China's growth trend. We expect this recovery cycle to continue for another 3-4 months before moderating in August-September. We address key questions related to China's growth cycle and highlight the implications for the equity market.

We maintain our base case that the mini-cycle recovery will continue for another 3-4 months and growth is likely to moderate from August-September, to be reflected in MS-CHEX. We are concerned about the deteriorating quality of the cyclical improvement, as it has been mainly a government-led recovery in investment, exacerbating the structural problems of high debt, excess capacity and persistent disinflationary pressures. That said, we expect a growth moderation rather than a notable slowdown comparable to 1Q15 in our base case, as overall policy should remain accommodative. We see risks slightly tilted to the upside, considering the ongoing property recovery cycle and the recent strong acceleration in FAI new starts. However, in the medium term, this would mean more downside risks.

For full details, see [China Macro Meets Micro: How Long Will this Recovery Cycle Last?](#) April 25, 2016.

Summary of Economics Views on the Mini-Cycle Recovery

	2015-16 mini-cycle
Trigger	Growth deceleration in 1Q15 due to weakness in both external and domestic demand
Policy response	Overall defensive easing
Monetary	100bp rate cuts and 250bp RRR cuts since Mar2015
Fiscal	Fiscal spending accelerated since 2H15, and fiscal spending to GDP ratio lifted by 200bp since Mar2015
Property	Several rounds of relaxation measures
Improvement phase	Initially started in 3Q15, bumpy until Feb2016 and more broad-based recovery in Mar2016
How long will last?	The current recovery cycle to continue for another 3-4 months before a moderation in growth likely from August-September
How to monitor the potential slowdown	Policy perspective: M2 (real mortgage rates), fiscal spending, property-related regulation Activity growth: MS-CHEX
Quality of recovery	Deteriorating quality of the cyclical improvement mainly driven by government-led recovery in investment growth
Risks	Risks slightly tilted to the upside in the near term, but in the medium term, it will only mean more downside risks

Source: Morgan Stanley Research

Global Macro Watch

Russia: CBR: Signalling a Cut, Mindful of Risks

Alina Slyusarchuk (44 20) 7677 6869

Signaling a chance of a cut: The CBR kept the key rate on hold at 11.0%, in line with our and consensus forecasts. Importantly, the tone of the CBR turned more dovish versus [the March statement](#). The bank said it “will resume a gradual lowering of its key rate at one of its forthcoming Board meetings...should inflation risks fall as much as to ensure with greater certainty that the Bank of Russia achieves its inflation target”. This is a tangible change in tone compared to the previous statement when the CBR said that it “may conduct its moderately tight monetary policy for a more prolonged time than previously planned”. Hence, we see the CBR signaling a **chance of a cut in the next three meetings**.

What stands in the way of a cut? Listing inflation risks, the CBR highlighted that inflation expectations are declining slowly and the nominal wages dynamics are mixed. In addition, the uncertainty over this year’s wages and pensions indexation, over the medium-term fiscal strategy and over the oil price outlook is still there.

Hence, we will be focusing on the incoming data on inflation and wages as well as the inflation expectations survey results. Importantly, the majority of inflation risks will stay for longer and will not be resolved by the next meeting on June 10. We think, given the decision of the Ministry of Finance to postpone the 2016 budget amendments until after the elections this year, the risk of the pensions indexation will remain until August. The details of the medium-term budget strategy will not be approved before October-November this year. Of course, the medium-term oil price risk will stay for longer as well. This tells us that **the pace of the rate cuts this year should be slow with monetary policy remaining moderately tight**.

We don’t see a cut as imminent: According to earlier Nabiullina statements, the wording “one of the CBR’s forthcoming Board meetings” means any of the next three meetings. We keep our rate forecast unchanged and expect the CBR to remain cautious with **the first 50bp cut coming in early 3Q on July 29**, once inflation has passed its local peak. Potentially, the uncertainty over the pre-election wages and pension indexation can be resolved by then. Overall, we see the CBR delivering **100bp of cuts in 2H16, taking the key rate to 10% by end-2016**.

For full details, see [Russia Economics: CBR: Signaling a Cut, Mindful of Risks](#), April 29, 2016.

Latin America: Trading the Adjustment

Maria Bendana (1 212) 296 5220
Thiago Machado (55 11) 3048 6249

Latin America has been hit with a negative terms of trade shock, resulting from the sharp decline in commodity prices and the region’s commodity export-intensive nature: Considering the concurrent depreciation in the region’s exchange rates, this juncture presents a clear opportunity to take advantage of competitiveness gains and to implement structural reforms to diversify the output basket and widen participation in global trade. However, although commodity prices have fallen for the past five years, we have not seen clear signs of structural rebalancing in the region’s exports. In fact, commodity export volumes have increased, while manufacturing export volumes have decreased. There are several factors behind this absence of rebalancing even in an environment of low commodity prices and depreciated exchange rates. Latin America’s inadequate infrastructure and uneven human capital make this process slower and more costly. Additionally, the region’s long-standing comparative advantage in commodities production is likely a factor postponing the rebalancing process.

Terms of trade have deteriorated markedly since their 2011 peak, falling about 24%, resulting in lower export receipts and reduced commodities-related investment: China’s transition away from a fixed investment-led growth model has had a twofold impact on the region, affecting Latin America’s export prices as well as export volumes. Additionally, the region has become more exposed to China over the last ten years due to the material increase in its exports to China, both as percentage of GDP and as a share of total exports. External demand has also softened within Latin America itself. For instance, Brazil’s deep recession has weakened trade within the region as the country’s private consumption and import demand fall. Unlike China, Latin America exposure to Brazil has decreased.

LatAm exports have not shown structural rebalancing towards more manufacturing goods, in response to lower commodity prices and weaker currencies: Of course, given that currencies depreciated the most in 2015, there could still be some rebalancing to come, but it is ever more clear that a productivity boost is needed. The region has plenty of low-hanging fruit such as infrastructure and reducing the red tape. The region continues to face the need to boost its human, physical and regulatory capital more than ever.

For full details, see [Latin America: Trading the Adjustment: Week Ahead in Latin America](#), April 29, 2016.

May 4, 2016
The Global Macro Analyst

Inflation Target Monitor & Next Rate Move

Global Economics Team. Contact: Manoj.Pradhan@morganstanley.com

	Inflation target	Latest month	12M MS Fcast	Next rate decision	Current Rate	Market expects (bp)	MS expects (bp)	Risks to our call
US	2.0% PCE Price Index	0.8%	1.4%	15 Jun	0.375	0	0	-
Euro Area	< 2% HICP (u)	-0.2%	1.6%	2 Jun	-0.40	0	0	-
Japan	2% CPI (u)	0.0%	0.9%	16 Jun	-0.10	0	-20	-
UK	2%	0.5%	1.5%	12 May	0.50	-1	0	November = earliest month for hike if Remain
Canada	1-3%	1.3%	2.4%	25 May	0.50	-6	0	-
Norway	2.5% CPI	3.3%	2.4%	12 May	0.50	-10	0	No cut if oil recovers faster than expected
Sweden	2.0% CPI	0.8%	1.1%	6 Jul	-0.50	0	0	FX intervention
Australia	2-3% over the cycle	1.3%	2.7%	7 Jun	1.75	-5	0	Extreme market volatility
Russia	4% CPI, end-2017	7.3%	7.3%	10 Jun	11.00	-	0	50bp cut
Poland	2.5% (+/- 1%) CPI	-1.1%	1.3%	6 May	1.50	-3	0	-
Czech Rep.	2.0% (+/-1%) CPI	0.3%	1.8%	5 May	0.05	-6	0	-
Hungary	3.0% (+/- 1%) CPI	-0.2%	2.2%	24 May	1.05	0	-10	Risks to the downside (more cuts)
Romania	2.5% (+/-1%) CPI	-3.0%	2.2%	5 May	1.75	-	0	-
Turkey	5% (±2%)	6.6%	7.7%	24 May	7.50	-	0	We expect 50bp cut from the upper bound.
Israel	1-3%	-0.7%	0.6%	23 May	0.10	0	0	-
S. Africa	3-6%	6.3%	7.0%	19 May	7.00	0	0	SARB hikes 25bp on CPI concerns
Nigeria	6-9%	12.4%	9.5%	17 May	12.00	-	0	50bp MPR hike on CPI concerns
China	NA	2.3%	1.0%	NA	4.35	-	0	-
India	4% ±2% from F2017	4.8%	4.2%	7 Jun	6.50	-	0	-
Hong Kong	NA	2.9%	2.2%	16 Jun	0.75	-	0	-
S. Korea	2%	1.0%	2.4%	13 May	1.50	0	0	-
Taiwan	NA	2.0%	1.3%	21-30 Jun	1.50	-2	-12.5	-
Indonesia	4% +/- 1.0%	4.4%	5.0%	19 May	6.75	-	0	-
Malaysia	NA	2.6%	3.2%	19 May	3.25	-2	0	-
Thailand	2.5% +/- 1.5% CPI	-0.5%	2.9%	11 May	1.50	8	0	Downside risk
Philippines	3% +/-1% CPI	1.1%	3.1%	12 May	2.50	-	0	-
Brazil	4.5% +/-2.0% IPCA	9.4%	7.7%	8 Jun	14.25	15	0	-
Mexico	3% +/-1% CPI	2.6%	3.5%	5 May	3.75	10	0	-
Argentina	15.5-24.2% M2 growth	32.9%	25.3%	NA	30.60	-	0	-
Chile	3% +/-1% CPI	4.5%	3.2%	17 May	3.50	2	0	-
Peru	2% +/-1% CPI	3.9%	2.8%	12 May	4.25	-	25	On hold given better behaved inflation
Colombia	3% +/-1% CPI	8.0%	3.8%	13 May	7.00	27	UR	-

(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. Japan latest month CPI is ex fresh food and VAT impact. NA = Not available. UR = Under review

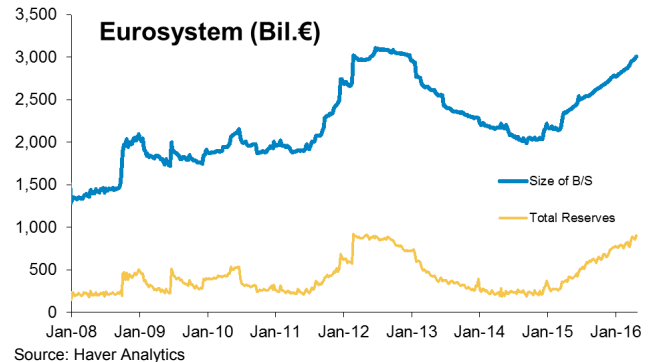
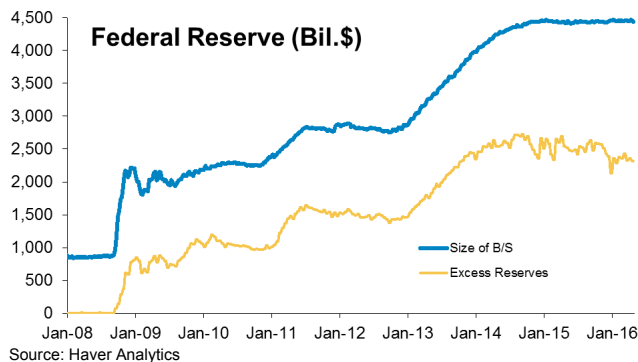
Source: National central banks, Morgan Stanley Research forecasts

Global Monetary Policy Rate Forecasts

	Current	2Q16	3Q16	4Q16	1Q17	2Q17	3Q17	4Q17	Market-implied EOP 2016
US	0.375	0.375	0.375	0.625	0.625	0.875	0.875	1.125	0.695
Euro Area	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.46
Japan	-0.10	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.27
UK	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	0.45
Canada	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.51
Norway	0.50	0.50	0.25	0.25	0.25	0.25	0.25	0.25	0.26
Sweden	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.25	0.00	-0.50
Australia	1.75	1.75	1.50	1.50	1.50	1.50	1.50	1.50	1.52
Russia	11.00	11.00	10.50	10.00	9.00	8.50	8.00	7.50	-
Poland	1.50	1.25	1.00	1.00	1.00	1.00	1.00	1.00	1.36
Czech Rep.	0.05	0.05	0.05	0.05	0.05	0.05	0.05	0.05	-0.04
Hungary	1.05	0.85	0.85	0.85	0.85	0.85	0.85	0.85	0.80
Romania	1.75	1.75	1.75	1.75	1.75	1.75	1.75	1.75	-
Turkey	7.50	7.50	7.50	7.50	7.50	7.50	7.50	7.50	-
Israel	0.10	0.10	0.10	0.10	0.10	0.10	0.25	0.50	0.12
S. Africa	7.00	7.00	7.00	7.25	7.25	7.25	7.25	7.25	7.39
Nigeria	12.00	12.00	12.00	12.00	11.00	10.50	10.50	10.50	-
China	4.35	4.35	4.10	4.10	3.85	3.85	3.85	3.85	-
India	6.50	6.50	6.50	6.25	6.00	6.00	6.00	6.00	-
Hong Kong	0.75	0.75	0.75	1.00	1.00	1.25	1.25	1.50	-
S. Korea	1.50	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25
Taiwan	1.500	1.375	1.375	1.375	1.375	1.375	1.375	1.375	1.476
Indonesia	6.75	6.75	6.75	6.75	6.75	6.75	6.75	6.75	-
Malaysia	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.06
Thailand	1.50	1.50	1.50	1.50	1.50	1.50	1.75	2.00	1.62
Philippines	2.50	2.50	2.50	2.75	3.00	3.00	3.00	3.00	-
Brazil	14.25	14.25	14.25	14.25	14.25	14.25	14.25	13.25	13.04
Mexico	3.75	4.00	4.00	4.25	4.25	4.25	4.25	4.25	4.23
Chile	3.50	3.50	3.50	3.50	3.25	3.00	3.00	3.00	3.67
Peru	4.25	4.50	4.50	4.50	4.50	4.50	4.50	4.50	-
Colombia	7.00				Under Review				6.92

Notes: Japan policy rate is the interest rate on excess reserves. Red font highlights rate hikes; green font highlights rate cuts; Market implied forecasts are taken from "What's in the Price"
Source: National Central Banks, Morgan Stanley Research forecasts.

Fed and Eurosystem Balance Sheet Monitor



May 4, 2016
The Global Macro Analyst

Key Forecast Profile

Global Economics Team

	Quarterly												Annual		
	2015E				2016E				2017E				2015	2016E	2017E
Real GDP (%Q, SAAR)	1Q	2Q	3Q	4Q	1QE	2QE	3QE	4QE	1QE	2QE	3QE	4QE			
Global*	2.7	3.3	3.0	2.2	2.5	3.0	3.3	3.3	3.4	3.1	3.3	3.3	3.1	3.0	3.4
G10	1.7	2.2	1.8	0.9	1.2	1.4	1.9	1.9	1.9	1.0	1.5	1.6	1.9	1.5	1.6
US	0.6	3.9	2.0	1.4	0.5	1.5**	1.8	1.7	1.6	1.6	1.5	1.4	2.4	1.7	1.6
Euro Area	2.3	1.6	1.2	1.3	2.2	1.6	2.0	2.0	1.8	1.6	1.6	1.6	1.5	1.5	1.8
Japan	4.6	-1.4	1.4	-1.1	1.2	0.8	1.6	1.9	2.6	-4.5	0.0	1.2	0.5	0.6	0.5
UK	1.8	2.4	1.8	2.4	1.5	0.8	2.5	2.0	2.4	2.4	2.5	2.5	2.2	1.7	2.3
EM (%Y)	4.2	4.1	4.1	4.0	4.0	4.1	4.0	4.2	4.6	4.6	4.7	4.8	4.1	4.0	4.7
China	7.0	7.0	6.9	6.8	6.7	6.5	6.4	6.4	6.5	6.5	6.4	6.3	6.9	6.5	6.4
India	6.7	7.6	7.7	7.3	7.3	7.4	7.6	7.7	7.8	7.7	7.7	7.8	7.3	7.5	7.7
Brazil	-2.0	-3.0	-4.5	-5.9	-6.2	-5.1	-3.6	-2.5	0.5	0.6	0.9	0.6	-3.8	-4.3	0.6
Russia	-2.2	-4.6	-4.1	-3.8	-3.0	-2.1	-2.0	-1.5	-0.2	0.7	1.2	1.6	-3.7	-2.1	0.9
Consumer price inflation (%Y)															
Global	2.4	2.6	2.5	2.6	2.7	2.2	2.3	2.5	2.7	2.8	2.8	2.7	2.5	2.4	2.8
G10	0.2	0.2	0.2	0.4	0.6	0.5	0.8	1.1	1.6	1.9	2.0	2.0	0.2	0.8	1.9
US	-0.1	0.0	0.1	0.4	1.0	1.1	1.2	1.5	1.9	1.9	1.9	1.9	0.1	1.2	1.9
Euro Area	-0.3	0.2	0.1	0.2	0.0	-0.2	0.3	0.9	1.6	1.8	1.8	1.8	0.0	0.2	1.7
Japan	2.3	0.5	0.2	0.3	0.0	-0.5	-0.4	0.0	0.5	2.3	2.6	2.7	0.8	-0.2	2.0
UK	0.1	0.0	0.0	0.1	0.3	0.5	0.8	1.2	1.5	1.7	1.8	1.8	0.0	0.7	1.7
EM	4.1	4.4	4.4	4.4	4.3	3.6	3.5	3.5	3.5	3.5	3.4	3.3	4.3	3.7	3.4
China	1.2	1.4	1.7	1.5	2.1	1.2	0.8	1.0	1.0	1.1	1.1	1.1	1.4	1.1	1.1
India	5.3	5.1	3.9	5.3	5.3	4.7	4.6	4.3	4.2	4.4	4.1	4.2	4.9	4.7	4.2
Brazil	7.7	8.5	9.5	10.4	10.1	9.1	8.7	8.2	7.6	7.5	7.3	7.1	9.0	9.2	7.2
Russia	16.2	15.8	15.7	14.5	8.6	8.8	9.3	8.8	8.1	7.3	6.9	6.7	15.6	8.9	7.3
Monetary policy rate (% p.a.)															
Global	3.48	3.28	3.18	3.18	3.16	3.13	3.04	3.05	2.94	2.96	2.96	2.96	3.18	3.05	2.96
G10	0.14	0.13	0.12	0.19	0.14	0.12	0.08	0.18	0.20	0.30	0.32	0.43	0.19	0.18	0.43
US	0.125	0.125	0.125	0.375	0.375	0.375	0.375	0.625	0.625	0.875	0.875	1.125	0.375	0.625	1.125
Euro Area	-0.20	-0.20	-0.20	-0.30	-0.40	-0.40	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.30	-0.50	-0.50
Japan	0.10	0.10	0.10	0.10	-0.10	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	0.10	-0.30	-0.30
UK	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	0.50	0.50	1.00
EM	6.26	5.90	5.72	5.66	5.67	5.62	5.48	5.42	5.21	5.17	5.14	5.05	5.66	5.42	5.05
China	5.35	4.85	4.60	4.35	4.35	4.35	4.10	4.10	3.85	3.85	3.85	3.85	4.35	4.10	3.85
India	7.50	7.25	6.75	6.75	6.75	6.50	6.50	6.25	6.00	6.00	6.00	6.00	6.75	6.25	6.00
Brazil	12.75	13.75	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.25	14.25	13.25	14.25	14.25	13.25
Russia	14.00	11.50	11.00	11.00	11.00	11.00	10.50	10.00	9.00	8.50	8.00	7.50	11.00	10.00	7.50

Note: Global and regional aggregates for GDP growth are GDP-weighted averages, using PPPs; Japan CPI includes VAT; Japan policy rate is the interest rate on excess reserves; CPI numbers are period averages. Global*: G10+BRICs+Poland, Czech Republic, Hungary, S Africa, Hong Kong, Korea, Taiwan, Mexico, Chile, Peru, Colombia, Argentina. Global* and EM* Consumer Price Inflation Aggregates exclude Venezuela and Argentina. **US tracking estimate Source: IMF, Morgan Stanley Research forecasts

	2015	2016		2017	
	MW MS	MW MS	MW Con	MW MS	MW Con
Global MW	2.5	2.3	2.5	2.8	2.7
G10 MW	1.9	1.5	1.9	1.6	1.6
EM MW	3.5	3.5	3.4	4.3	4.3

MW = 10y FX market exchange rate-weighted. Con = Consensus, MW = Market Weighted. Global and EM aggregates exclude Argentina and Venezuela. Source: Bloomberg, Morgan Stanley Research forecasts

May 4, 2016
The Global Macro Analyst

Global GDP and Inflation Forecasts

	Real GDP (%)					CPI inflation (%)				
	2015	2016E		2017E		2015	2016E		2017E	
		MS	Cons	MS	Cons		MS	Cons	MS	Cons
Global Economy	3.1	3.0	3.1	3.4	3.6	2.5	2.4	2.6	2.8	3.0
G10	1.9	1.5	1.7	1.6	1.9	0.2	0.8	0.9	1.9	1.9
US	2.4	1.7	2.0	1.6	2.3	0.1	1.2	1.3	1.9	2.2
Euro Area	1.5	1.5	1.5	1.8	1.6	0.0	0.2	0.3	1.7	1.4
Japan	0.5	0.6	0.5	0.5	0.5	0.8	-0.2	0.3	2.0	1.8
UK	2.2	1.7	1.9	2.3	2.2	0.0	0.7	0.7	1.7	1.7
Canada	1.2	1.1	1.5	1.6	2.2	1.1	1.6	1.5	2.4	2.0
Norway	1.1	0.7	0.9	1.5	1.7	2.2	2.9	2.8	2.3	2.3
Sweden	3.8	3.8	3.5	2.8	2.7	0.0	1.0	0.9	1.3	1.8
Australia	2.5	1.9	2.6	2.1	2.9	1.5	1.7	1.9	2.6	2.5
Emerging Markets	4.1	4.0	4.2	4.7	4.9	4.3	3.7	4.0	3.4	3.8
EM-ex-China	2.5	2.7	2.9	3.7	4.0	6.3	5.2	5.1	4.8	4.8
CEEMEA	0.2	0.9	1.3	2.3	2.6	10.3	7.5	7.5	6.7	6.5
Russia	-3.7	-2.1	-1.5	0.9	1.2	15.6	8.9	8.0	7.3	6.7
Poland	3.6	3.6	3.6	3.6	3.5	-0.9	-0.3	-0.3	1.7	1.7
Czech Rep	4.3	2.5	2.5	3.0	2.8	0.3	0.7	0.9	1.9	2.0
Hungary	2.9	2.5	2.4	2.7	2.6	-0.1	0.1	1.0	2.4	2.5
Ukraine	-9.8	1.1	1.0	2.3	2.2	48.5	17.0	16.1	11.2	10.2
Kazakhstan	1.2	0.6	0.7	2.3	2.4	6.6	15.1	14.2	8.0	7.0
Turkey	4.0	3.0	3.3	3.1	3.5	7.7	7.6	8.3	8.1	7.6
Israel	2.6	2.8	2.8	2.6	3.3	-0.6	-0.3	0.3	1.0	1.4
South Africa	1.3	0.8	0.6	1.5	1.4	4.6	6.3	6.5	6.4	6.3
Nigeria	2.8	2.0	3.6	3.1	4.5	9.0	10.5	10.5	9.4	9.5
Asia ex-Japan	6.1	5.9	6.0	6.1	6.0	2.4	2.2	2.7	2.3	2.9
China	6.9	6.5	6.5	6.4	6.3	1.4	1.1	2.0	1.1	2.0
India	7.3	7.5	7.5	7.7	7.7	4.9	4.7	4.9	4.2	5.2
Hong Kong	2.4	1.7	1.8	2.1	2.1	3.0	2.2	2.5	1.5	2.5
Korea	2.6	2.3	2.7	2.6	2.9	0.7	1.6	1.3	2.4	2.0
Taiwan	0.7	0.5	1.5	1.1	2.3	-0.3	0.5	0.8	1.2	1.3
Singapore	2.0	1.8	1.9	2.2	2.2	-0.5	-0.3	-0.2	0.7	1.0
Indonesia	4.8	5.0	5.1	5.2	5.4	6.4	4.0	4.5	4.9	4.9
Malaysia	5.0	4.2	4.3	4.6	4.5	2.1	2.2	2.6	3.0	2.7
Thailand	2.8	2.7	3.1	3.0	3.3	-0.9	0.7	0.6	2.8	2.0
Philippines	5.8	5.8	5.9	6.0	5.9	1.4	2.3	2.4	3.1	3.0
Latin America	-0.4	-1.0	-0.7	1.3	1.9	15.5	27.4	23.9	52.8	25.2
Brazil	-3.8	-4.3	-3.7	0.6	0.9	9.0	9.2	8.5	7.2	6.1
Mexico	2.5	2.2	2.5	2.5	2.8	2.7	3.4	3.0	3.3	3.2
Chile	2.0	1.8	1.8	2.2	2.6	4.3	4.0	4.0	3.1	3.3
Peru	3.3	3.5	3.5	4.0	4.0	3.5	4.0	3.7	2.9	3.0
Colombia	3.1	2.1	2.4	2.4	3.0	5.0	7.4	7.0	3.7	3.9
Argentina	2.1	-0.8	-0.5	3.6	3.0	26.7	35.8	34.4	19.6	19.7
Venezuela	-5.7	-5.0	-6.6	-7.0	-0.4	121.7	300.0	250.9	600.0	250.0

Note: Global, G10 and EM consensus aggregates are calculated using the same PPP weights and country subsample as MS aggregates. Consensus aggregates are not comparable to those directly available on Bloomberg. Global, EM and EM-ex-China aggregates for CPI exclude Venezuela and Argentina. Red (green) font indicates MS below (above) consensus. Japan headline CPI includes the consumption tax effects. Source: IMF, Morgan Stanley Research forecasts

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Consumer Expenditure and Investment Spending Forecasts

	Quarterly												Annual		
	2015				2016				2017				2015	2016E	2017E
Private Consumption (%Q, SA)	1Q	2Q	3Q	4Q	1QE	2QE	3QE	4QE	1QE	2QE	3QE	4QE			
Global*	0.6	0.8	0.9	0.4	1.0	0.8	0.8	0.9	1.1	0.8	0.9	1.0	3.1	3.2	3.6
G4	0.4	0.5	0.6	0.2	0.6	0.4	0.5	0.5	0.6	0.1	0.4	0.4	2.0	1.8	1.6
US	0.4	0.9	0.7	0.5	0.8	0.5	0.5	0.5	0.5	0.5	0.5	0.5	3.1	2.5	2.0
Euro Area	0.5	0.3	0.5	0.2	0.4	0.5	0.4	0.4	0.4	0.4	0.4	0.4	1.7	1.5	1.6
Japan	0.2	-0.8	0.3	-0.9	0.6	-0.2	0.5	0.6	1.5	-2.7	0.0	0.2	-1.3	0.1	0.1
UK	0.8	0.8	0.5	0.6	0.4	0.2	0.4	0.3	0.6	0.7	0.6	0.5	2.7	1.8	2.1
BRIC	0.8	1.1	1.3	0.7	1.3	1.2	1.2	1.3	1.6	1.6	1.4	1.5	4.5	4.8	5.9
China	-	-	-	-	-	-	-	-	-	-	-	-	7.9	7.5	7.1
India	3.4	1.5	1.2	0.8	2.5	1.7	1.3	1.5	2.0	1.9	1.5	1.7	6.2	6.5	6.9
Brazil	-2.1	-2.2	-1.5	-1.3	-1.5	-1.2	-0.6	-0.5	0.2	0.2	0.2	0.2	-4.1	-4.9	-0.4
Russia	-9.0	-1.2	1.1	-4.1	-1.7	-1.2	-0.4	0.1	0.9	1.0	1.0	1.1	-10.1	-5.5	2.1
Private Consumption (%Y)															
Global*	3.2	3.5	3.2	2.8	3.2	3.2	3.1	3.5	3.7	3.6	3.7	3.8	3.1	3.2	3.6
G4	1.8	2.3	2.3	1.8	2.0	1.8	1.7	1.9	1.9	1.6	1.5	1.5	2.0	1.8	1.6
US	3.3	3.3	3.1	2.6	3.0	2.6	2.3	2.3	2.0	2.0	2.0	1.9	3.1	2.5	2.0
Euro Area	1.6	1.7	1.8	1.5	1.4	1.6	1.5	1.7	1.7	1.6	1.6	1.6	1.7	1.5	1.6
Japan	-4.1	0.1	0.4	-1.2	-0.8	-0.2	0.0	1.5	2.4	-0.2	-0.7	-1.1	-1.3	0.1	0.1
UK	2.7	2.7	2.7	2.8	2.3	1.8	1.7	1.4	1.5	2.0	2.2	2.4	2.7	1.8	2.1
BRIC	4.9	4.7	4.3	4.2	4.7	4.8	4.7	5.3	5.5	5.8	6.0	6.3	4.5	4.8	5.9
China	-	-	-	-	-	-	-	-	-	-	-	-	7.9	7.5	7.1
India	6.5	6.2	5.3	7.0	6.0	6.3	6.4	7.1	6.6	6.7	6.9	7.2	6.2	6.5	6.9
Brazil	-1.5	-3.0	-4.5	-6.8	-6.3	-5.4	-4.5	-3.7	-2.1	-0.7	0.1	0.8	-4.1	-4.9	-0.4
Russia	-9.0	-8.7	-9.4	-12.9	-5.9	-5.9	-7.2	-3.2	-0.6	1.6	3.0	4.1	-10.1	-5.5	2.1
Investment (%Q, SA)															
Global*	0.8	0.5	0.6	0.3	0.6	0.6	0.7	0.8	1.0	0.8	0.9	0.9	2.6	2.2	3.5
G4	1.2	0.7	0.6	0.4	0.5	0.6	0.8	0.9	0.9	0.4	0.6	0.6	3.1	2.4	2.9
US	0.8	1.3	0.9	0.1	0.3	0.4	0.7	0.9	0.8	0.6	0.5	0.5	4.0	2.0	2.8
Euro Area	1.4	0.1	0.4	1.3	0.9	0.9	0.9	0.8	0.8	0.8	0.8	0.8	2.6	3.4	3.2
Japan	1.6	0.1	0.3	0.2	0.5	0.5	0.9	0.7	1.9	-1.9	0.1	0.8	0.2	1.8	1.8
UK	1.5	1.3	0.4	-1.1	0.7	0.3	1.2	1.5	0.4	1.4	1.5	0.5	4.1	1.6	4.3
BRIC	0.4	0.2	0.5	0.2	0.7	0.6	0.7	0.8	1.2	1.2	1.1	1.1	2.3	2.2	4.2
China	-	-	-	-	-	-	-	-	-	-	-	-	5.8	4.7	4.2
India	1.0	1.1	1.2	0.2	2.5	1.8	1.2	1.1	1.9	2.0	1.4	1.4	5.2	5.8	6.6
Brazil	-3.2	-7.4	-4.4	-4.9	-4.0	-3.0	-1.5	-0.5	0.5	0.4	0.5	0.3	-14.3	-14.0	-0.6
Russia	-3.2	-1.6	-0.9	-1.3	-2.0	-1.8	-1.0	-0.5	1.0	1.5	1.7	1.7	-7.6	-5.7	3.1
Investment (%Y)															
Global*	3.2	3.2	3.0	2.3	2.1	2.2	2.3	2.8	3.3	3.5	3.6	3.6	2.6	2.2	3.5
G4	2.9	3.5	3.0	3.0	2.3	2.1	2.3	2.8	3.2	3.0	2.9	2.6	3.1	2.4	2.9
US	4.8	4.7	3.6	3.1	2.5	1.7	1.4	2.2	2.8	3.0	2.9	2.6	4.0	2.0	2.8
Euro Area	2.0	2.6	2.5	3.4	2.7	3.5	4.0	3.4	3.3	3.2	3.2	3.2	2.6	3.4	3.2
Japan	-4.0	0.8	2.0	2.1	1.0	1.5	2.1	2.6	4.1	1.5	0.7	0.8	0.2	1.8	1.8
UK	6.2	4.9	3.4	2.1	1.3	0.3	1.1	3.8	3.5	4.6	5.0	3.9	4.1	1.6	4.3
BRIC	3.7	2.8	2.9	1.6	1.9	2.2	2.3	2.9	3.4	4.0	4.4	4.7	2.3	2.2	4.2
China	-	-	-	-	-	-	-	-	-	-	-	-	5.8	4.7	4.2
India	5.6	4.9	7.1	3.5	5.0	5.8	5.7	6.7	6.2	6.4	6.6	7.0	5.2	5.8	6.6
Brazil	-9.9	-13.2	-15.0	-18.5	-19.2	-15.3	-12.8	-8.7	-4.5	-1.1	0.9	1.7	-14.3	-14.0	-0.6
Russia	-6.9	-7.6	-7.3	-6.9	-5.7	-5.9	-6.0	-5.2	-2.3	1.0	3.7	5.9	-7.6	-5.7	3.1

Note: Global and regional aggregates GDP-weighted averages, using PPPs; *G4+BRICs. Quarterly consumption and investment data for China is unavailable; hence, there are no official forecasts.
Source: IMF, Morgan Stanley Research forecasts

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Global Economics Team

Global Co-Heads of Economics

Chetan Ahya	Chetan.Ahya@morganstanley.com	+852 2239 7812
Elga Bartsch	Elga.Bartsch@morganstanley.com	+44 (0)20 7425 5434
Jonathan Ashworth	Jonathan.Ashworth@morganstanley.com	+44 (0)20 7425 1820

Global Economics

Manoj Pradhan	Global	Manoj.Pradhan@morganstanley.com	+44 (0)20 7425 3805
Patryk Drozdziak	Global	Patryk.Drozdziak@morganstanley.com	+44 (0)20 7425 7483
Pratyancha Pardeshi	Global	Pratyancha.Pardeshi@morganstanley.com	+44 (0)20 7677 0528

Americas

Ellen Zentner	US	Ellen.Zentner@morganstanley.com	+1 212 296 4882
Ted Wieseman	US	Ted.Wieseman@morganstanley.com	+1 212 761 3407
Paula Campbell Roberts	US	Paula.Roberts@morganstanley.com	+1 212 761 3043
Robert Rosener	US	Robert.Rosener@morganstanley.com	+1 212 296 5614
Michel Dilmanian	US	Michel.Dilmanian@morganstanley.com	+1 212 761 3247
Luis Arcentales	LatAm, Chile, Mexico	Luis.Arcentales@morganstanley.com	+1 212 761 4913
Arthur Carvalho	LatAm, Brazil	Arthur.Carvalho@morganstanley.com	+55 11 3048 6272
Maria Bendana	Latam	Maria.Bendana@morganstanley.com	+1 212 296 5220
Thiago Machado	Brazil	Thiago.Machado@morganstanley.com	+55 11 3048 6249
Fernando Sedano	Argentina, Colombia, Venezuela	Fernando.Sedano@morganstanley.com	+55 11 3048 6605

Europe & Africa

Elga Bartsch	Euro Area, ECB, Germany	Elga.Bartsch@morganstanley.com	+44 (0)20 7425 5434
Daniele Antonucci	Italy, Spain, Greece, Portugal	Daniele.Antonucci@morganstanley.com	+44 (0)20 7425 8943
Carmen Nuzzo	Sustainability, France	Carmen.Nuzzo@morganstanley.com	+44 (0)20 7677 0209
Joao Almeida	Italy, Spain, Greece, Portugal	Joao.Almeida@morganstanley.com	+44 (0)20 7425 6838
Jacob Nell	UK	Jacob.Nell@morganstanley.com	+44 (0)20 7425 8724
Melanie Baker	UK	Melanie.Baker@morganstanley.com	+44 (0)20 7425 8607
Pasquale Diana	Poland, Hungary, Czech, Romania	Pasquale.Diana@morganstanley.com	+44 (0)20 7677 4183
Andrea Masia	South Africa, Nigeria	Andrea.Masia@rmbmorganstanley.com	+27 11 282 1593
Alina Slyusarchuk	Russia, Kazakhstan, Ukraine	Alina.Slyusarchuk@morganstanley.com	+44 (0)20 7677 6869
Ercan Erguzel	Turkey, Israel	Ercan.Erguzel@morganstanley.com	+90 212 398 0223
Georgi Deyanov	Bulgaria, Serbia, Croatia	Georgi.Deyanov@morganstanley.com	+44 (0)20 7425 7006

Asia

Chetan Ahya	Asia ex-Japan, India	Chetan.Ahya@morganstanley.com	+852 2239 7812
Derrick Kam	Asia ex-Japan, Hong Kong	Derrick.Kam@morganstanley.com	+852 2239 7826
Jenny Zheng	Asia ex-Japan	Jenny.L.Zheng@morganstanley.com	+852 3963 4015
Junwei Sun	China	Junwei.Sun@morganstanley.com	+852 2239 7820
Yin Zhang	China	Yin.Zhang@morganstanley.com	+852 2239 7818
Robert Feldman	Japan	Robert.Tokyo.Feldman@morganstanleymufg.com	+81 3 6836 8400
Takeshi Yamaguchi	Japan	Takeshi.Yamaguchi@morganstanleymufg.com	+81 3 6836 5404
Shoki Omori	Japan	Shoki.Omori@morganstanleymufg.com	+81 3 6836 5466
Upasana Chachra	India	Upasana.Chachra@morganstanley.com	+91 22 6118 2246
Gaura Sengupta	India	Gaura.Sengupta@morganstanley.com	+91 22 6118 2245
Devi Tan	ASEAN, Korea, Taiwan	Devi.Tan@morganstanley.com	+65 6834 6703
Zhixiang Su	ASEAN, Korea, Taiwan	Zhixiang.Su@morganstanley.com	+65 6834 6739
Fuxin Lu	ASEAN, Korea, Taiwan	Fuxin.Lu@morganstanley.com	+65 6834 6743
Daniel Blake	Australia	Daniel.Blake@morganstanley.com	+61 2 9770 1579

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The Americas

1585 Broadway
New York, NY 10036-8293
United States
Tel: +1 (1)212 761 4000

Europe

20 Bank Street, Canary Wharf
London E14 4AD
United Kingdom
Tel: +44 (0)20 7425 8000

Japan

1-9-7 Otemachi,
Chiyoda-ku,
Tokyo 100-8104, Japan
Tel: +81 (0)3 6836 5000

Asia/Pacific

1 Austin Road West
Kowloon
Hong Kong
Tel: +852 2848 5200