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Markets in the second quarter: Expansion ahead

Little help from macro trends in Q1

After multiple twists and turns in Q1, the US, European and EM equity markets have delivered outcomes only a short distance from flat. In part this is due to the lack of persistence in macro drivers since the year began and their shifting configuration relative to most of last year. In a sense, we are still waiting for the curtain to rise on 'showtime' for the US recovery.

'Showtime' after a delayed opening

We think that point is now at hand: our forecasts imply an acceleration in global GDP growth, excluding Japan; the US economy is set to bounce back from the drags from weather and destocking; and China's weak start to the year should give way to something a little better, as modest stimulus falls into place. At the same time, US financial conditions are at their easiest levels post-crisis, and we expect easing measures from both the ECB (quite likely tomorrow) and the BoJ (in April or June).

A more cyclical tilt to markets

These dynamics have begun to influence market pricing more clearly in the past couple of weeks. And our Global Leading Indicator has shown tentative signs that a phase of Expansion may be starting. But we think the reality of a better cyclical picture has not yet been fully priced. If we are right, the improving cyclical environment should continue to support equities, while pushing yields higher. It should also support a pro-cyclical stance within each of the major asset classes.

Improving US and china growth would help cyclical assets

	Response of asset to shock:	US growth *higher*	+ EM/China growth *higher*	+ *Neutral* US monetary policy	= Total?
Stocks	US	++	+?	0	++?
	Domestic cylicals	++	0	0	+
	Global Cyclicals	+	+	0	+
	Defensives	+?	0	0	0
	EM	+	++?	0	++?
Rates	US yields	++	+	0	++?
FX	$	+?	-	0	-?
	$/JPY	+	+?	0	+
	$/EM	+	-	0	0
Relative equity	EM vs DM	-	+	0	0/+?
	Glob Cyc vs Def	+?	+	0	+
	Dom Cyc vs Def	++?	0	0	+

Scale shows likely response to each shock ranging from most positive to most negative on the following scale: ++, ++?, +, +?, 0, -?, -, --?, --. For negative shocks, signs would be reversed.
Source: Goldman Sachs Global Investment Research.

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Markets in the second quarter: Expansion ahead

With markets closing out their first quarter, many macro investors will be glad to see it on the ash heap of history. After multiple twists and turns, the US, European and even EM equity markets have delivered outcomes only a short distance from flat. The US 5-year yield is close to flat, while 10-year yields are clearly lower. And comparing total returns in 30 major currencies, the USD is roughly in the middle of the pack, with significant dispersion on either side.

For those who get the sense that there have been fewer good macro trends to sink their teeth into than in 2013, we show that this has indeed been the case. This relates in part to the lack of persistence in macro drivers since the year began and their shifting configuration relative to most of last year. The weakness in US growth views in particular has wrong-footed some popular positions. We said late last year that it was 'showtime' for the US recovery. But in a sense we are still waiting for the curtain to rise.

We think that point is now at hand. Our growth forecasts imply an acceleration in global GDP growth, excluding Japan. The US economy is set to bounce back from the drags from weather and destocking. And China's extremely weak start to the year should also give way to something a little better, as modest stimulus falls into place. At the same time, while the obsession over the Fed's 'dots' and what Fed Chair Yellen 'really meant' has continued, US financial conditions are at their easiest levels post-crisis. And we expect easing measures from both the ECB (quite likely tomorrow) and the BoJ (in April or June).

In the past couple of weeks, those dynamics have begun to influence market pricing more clearly. And our Global Leading Indicator (GLI) has shown tentative signs that a phase of Expansion (positive and increasing momentum) may be starting. But we think the reality of a better cyclical picture has not yet been fully priced. If we are right, the improving cyclical environment should continue to support equities, while pushing yields higher. It should also support a pro-cyclical stance within each of the major asset classes. In March, we recommended both tactical long positions in the DAX and a shift to an outright bearish stance on government bonds on this basis.

The more controversial possibility is that improving activity – particularly if China is part of it – continues to support EM and commodity-related assets. Although our structural view of the EM universe is still quite cautious, EM assets could receive further temporary support from the shift to global expansion. Last year, it proved risky to focus on these kinds of tactical considerations, and more effective to maintain conviction in the deeper macro shifts that were taking place. In particular, the last GLI expansion phase in mid-2013 came alongside substantial damage to EM assets, a traditional beneficiary of cyclical improvement. This year, we may be back in an environment where greater focus on near-term tactical drivers may make more sense again, in part because the key dynamics of US recovery, China risks and EM rebalancing are already more squarely in focus. Our comfort, of course, remains highest where tactical and strategic considerations intersect.

Little help from my trends

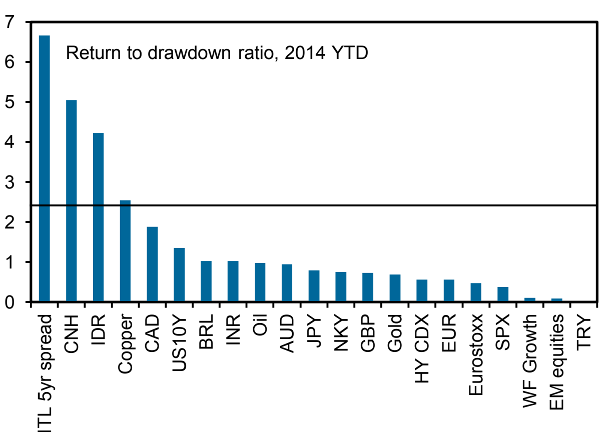
Part of the reason why the start of the year has been tough is that there have been fewer clear opportunities in the major macro assets so far, particularly relative to 2013. A simple way to illustrate this is to look at the ratio of returns in an asset over a particular time period relative to the maximum drawdown during that period, applying Alex Timcenko's earlier work here (see *Global Economics Weekly: 13/26* – 'Equity drawdowns: Bull market interrupted, not the dawn of a new era'). This gives a sense of how easy it would be to 'hold' a position in an asset over a particular timeframe. We tend to think of ratios above 2 in absolute terms (an overall return at least twice as large as the maximum drawdown in the holding period) as high risk/reward opportunities. Exhibit 1 shows the ratios for a range of macro assets so far in 2014, while Exhibit 2 compares this return-to-drawdown ratio for each asset in 2014 with 2013. Looking across this evidence, two things stand out:

- **2013 was an extremely good period for macro trends**. The SPX and Nasdaq recorded return-to-drawdown ratios of above 5. The rise in US bond yields, increases in the major DM equity markets, declines in a number of EM and commodity currencies and in gold, and the outperformance of US over EM equities all recorded ratios of close to 2 or more. The six-month period from November 2012 to May 2013 saw even stronger trends in the Nikkei, JPY and several other DM equity markets. But, for 2013 as a whole, what stands out is the existence of significant trends in a wide range of different asset classes.
- **2014 has so far been much less remarkable**. Of the main macro asset classes, only the fall in copper prices, the compression in peripheral European sovereign spreads, the weakness in the CNH and CAD, and the strength in the IDR have delivered return-to-drawdown ratios of greater than 2. Of these trends, only the last three (in FX) were in assets that had delivered strong trends in 2013, and in two of those cases – the IDR and CNH – the moves have been in the opposite direction this year, so to exploit them successfully would have required reversing positions.

Muddy macro waters

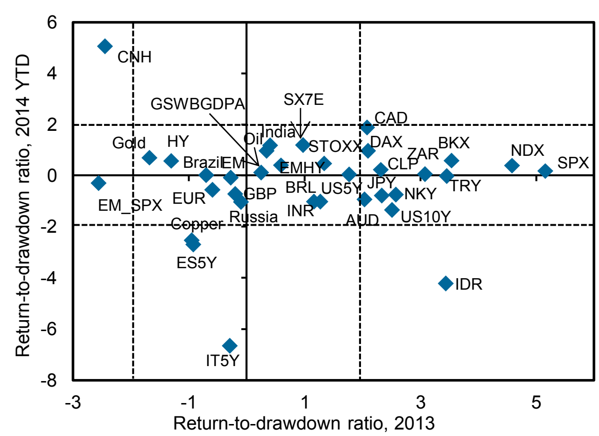
This choppiness of markets in the first quarter reflects the shifting nature of the market's macro focus. In 2013, the market changed its views on a number of key macro drivers in ways that reinforced each other in many areas. The early part of the year was dominated by the shift towards a sharp easing in Japanese monetary policy. But for the year as a whole, three major dynamics were crucial: an upgrade to the market's US growth views; a downgrade to views of China growth; and a more hawkish view of Fed policy, as the 'taper tantrum' pushed the term premium to more normal levels. Exhibit 3 shows how we see each of these dynamics mapping into the major macro assets (see *Global Economics Weekly: 13/35* – 'The post-shutdown slowdown market lowdown'). Together, this combination worked to support DM equities, pushed US bond yields and the USD higher and helped to underpin the strong outperformance of DM over EM assets.

Exhibit 1: Few strong trends in macro assets in 2014 so far…



Source: Goldman Sachs Global Investment Research.

Exhibit 2: …in contrast to strong trends in many assets in 2013



Source: Goldman Sachs Global Investment Research.

Exhibit 3: In 2013, macro drivers created consistent themes

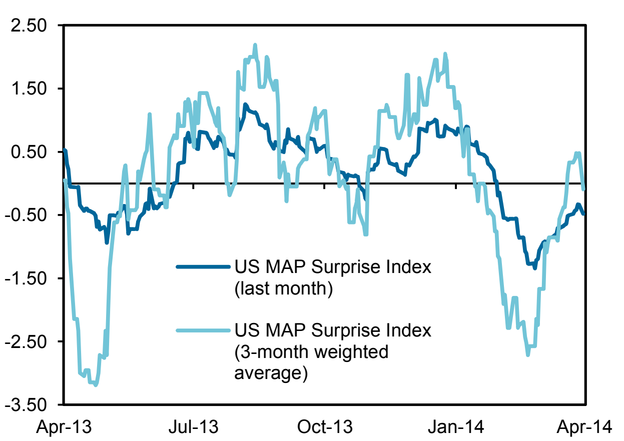
	Response of asset to shock:	US growth *higher*	+ EM/China growth *lower*	+ *Tighter* US monetary policy	= Total?
Stocks	US	++	-?	-	+
	Domestic cylicals	++	0	-	+
	Global Cyclicals	+	-	-	-
	Defensives	+?	0	-?	0
	EM	+	--?	-	-
Rates	US yields	++	-	++	++
FX	$	+?	+	+	+
	$/JPY	+	-?	+	+
	$/EM	+	+	++	++
Relative equity	EM vs DM	-	-	-	--
	Glob Cyc vs Def	+?	-	-?	-?
	Dom Cyc vs Def	++?	0	-?	+

Scale shows likely response to each shock ranging from most positive to most negative on the following scale: ++, ++?, +, +?, 0, -?, -, - -?, - -. For negative shocks, signs would be reversed.
Source: Goldman Sachs Global Investment Research.

So far in 2014, the mix of macro dynamics has been more complicated. Most obviously, the configuration of macro drivers has shifted relative to 2013. In particular, a period of negative US data surprises saw the market downgrade its US growth views somewhat and scale back its expectations of monetary tightening, particularly in January and February (Exhibit 4). Worries about Japan's growth prospects have also intensified ahead of April's consumption tax hike. Both of these concerns helped to unwind upgrades from late last year. At the same time, worries about China's growth prospects intensified again early in the year, as evidence has accumulated that GDP growth decelerated significantly in the first two months of the year. So the last few months have not been a simple reversal of last year's macro shifts.

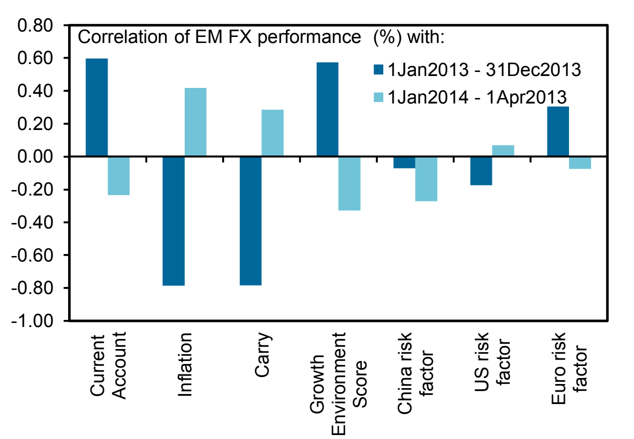
Within EM markets (Exhibit 5), the axis of pressures has also shifted from a clear focus last year on those with high inflation, large current account deficits and weak institutions to a more idiosyncratic mix since then (see *EM Macro Daily*, March 18, 2014). With many investors coming into the year largely positioned for 'more of the same', these shifts have been difficult to manage. The reversal in US growth and interest rate markets has been particularly painful and many of the most obvious reversals early in the year (in bonds, gold, Nikkei, JPY) can be traced back to that shift.

Exhibit 4: A period of negative US surprises slowly fading



Source: Goldman Sachs Global Investment Research.

Exhibit 5: Drivers of EM FX have shifted this year too



Source: Goldman Sachs Global Investment Research.

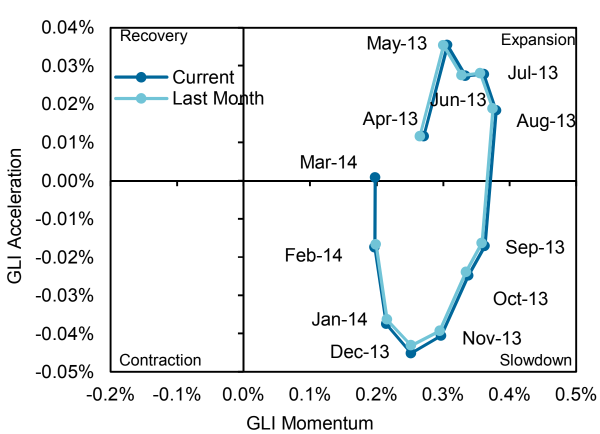
To make matters worse, the shifts in macro views have also been less persistent. Market concerns about US growth were most intense early in the year, but there has been some relaxation as the market has become more comfortable that some of the deceleration is likely to prove temporary. January saw intensifying pressures on several EM economies but rate hikes there (most dramatically in Turkey) have helped to provide more stability since then. Worries about the crises in Ukraine and Russia, and their spillovers, have fluctuated over the last month or two. And in the past couple of weeks there has also been a relaxation about China growth risks in anticipation of some modest stimulus there. So the market has effectively moved through several phases, none of which has shown enormous continuity so far.

'Showtime' after a delayed opening

Our story for the likely macro drivers in the second quarter is more straightforward. We think that the next couple of months are likely to be dominated by evidence that the growth weakness of the first quarter is giving way to the kind of recovery profile that we expected initially coming into the year. In that sense, the 'showtime' that we argued for the US recovery, which has been delayed by temporary factors, now seems likely to begin.

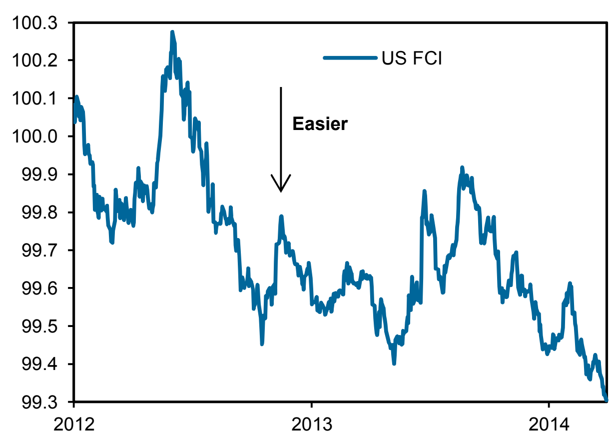
Our forecast is for US GDP growth to pick up from 1.5%qoq annualised in Q1 to 3% in Q2, as the drag from destocking fades and the impact of bad weather reverses. Although we expect Japan's growth to fall sharply into Q2 as the consumption tax takes effect, we also forecast a sequential pick-up in global growth in the second quarter. This is in large part because we expect China's growth to pick up from 5% to 7.3% as the mix of domestic easing and an improving external environment alleviates some of the extraordinary weakness from the start of the year. Indeed, our GLI suggests that the global economy may already be moving tentatively back to the Expansion phase (positive and accelerating momentum) after being in a modest Slowdown since last August (Exhibit 6). Moreover, despite perceptions of a hawkish shift from the March FOMC, our measures of US financial conditions are now easier than at any time post-crisis (Exhibit 7).

Exhibit 6: Our Global Leading Indicator flirting with 'Expansion'



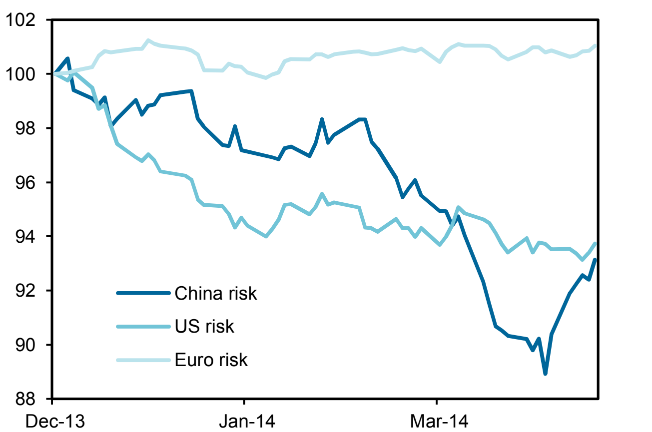
Source: Goldman Sachs Global Investment Research.

Exhibit 7: Financial conditions easier than ever



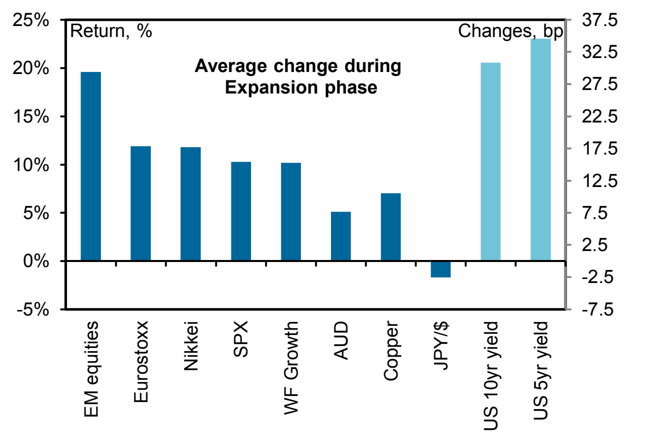
Source: Goldman Sachs Global Investment Research.

Exhibit 8: A downgrade to market's US and China growth views in 2014



Source: Goldman Sachs Global Investment Research.

Exhibit 9: Cyclical assets do well in the average GLI "Expansion"



Source: Goldman Sachs Global Investment Research.

Markets have moved to acknowledge some of these changes already, but we do not think these shifts are fully priced. Looking across the three 'macro risk factors' that we regularly track, our US risk factor has fallen significantly, domestic cyclical stocks have underperformed and longer-dated yields have declined. Although US data have moved back towards more neutral surprises in the last month, our estimates of market growth views are clearly lower than at the start of the year (Exhibit 8). Even with some relief recently, there has been a significant downgrade to our measures of China growth risk since the start of the year. The downgrade to China growth risks from December to mid-March was nearly as large as the sharp shift that we saw from May to July 2013. As a result, we think that cyclical improvement is likely to be the major theme in the next month or two as the reality of some improvement on these fronts is reflected more broadly.

A more cyclical tilt to markets

Two complementary approaches that we often use are helpful in thinking about mapping that kind of pro-cyclical view into markets. The first is to think about the phases of the global cycle as marked out by our GLI. Exhibit 9 shows the average historical performance of assets during GLI Expansion phases. In general, these phases are positive for equities and commodities and negative for bonds, while more cyclical sectors and equity indices also generally outperform. Traditionally, the Expansion phase has also been associated with stronger performance in EM assets and commodity currencies and with modest USD weakening.

Underneath the surface, the nature of the expansion matters. A second way to think about the macro shifts ahead that takes account of the source of growth and potential shifts in monetary policy is to go back to the framework shown in Exhibit 4. This requires us to consider the likely shifts in the market's views of US, China and European growth and of US/global monetary policy shifts. In simple terms, our forecasts imply: an upgrade to US growth views; an upgrade to China growth views; and a neutral to mildly positive view of European growth. In terms of monetary policy, we doubt that we will learn anything very significant about the Fed's reaction function in the next month or two. The March FOMC was more hawkish than expected but the market has digested that news and Chair Yellen provided a somewhat more reassuring message in remarks earlier this year. The removal of 'threshold guidance' – and uncertainty about what exactly has replaced it – may make markets more sensitive to improving data than before. But we still think that higher yields are likely to be driven mostly by better growth, not by a shift in policy.

Exhibit 10 shows that this combination would again naturally be more clearly positive for equities and negative for bonds than was the case at the start of the year and would normally favour cyclical indices and sectors. Rather than broad USD strength, this mix of forces would normally be associated with a pro-cyclical tilt on the crosses and a greater focus on relative monetary policy stories in the major economies (which tilt towards EUR and JPY weakness). In this framework, whether EM assets outperformed DM assets would depend on the exact mix of China and US growth surprises and monetary policy. But EM outperformance would be more likely than it has been recently in this environment.

It is easy to imagine other macro 'shocks' beyond those shown in Exhibit 10. Two in particular may be important. The first is non-US monetary policy. We expect some modest easing measures both from the ECB (with a good chance that it comes at tomorrow's meeting) and from the BoJ (in April or June). If that is right, it is likely to reinforce the pro-cyclical tilt to markets at the margin, while reinforcing the potential for differentiation within the FX universe. The second is the ongoing tensions between Ukraine and Russia. While our base case is that these will remain manageable, clearly there are potential paths of escalation. We think a better global growth environment would make it easier for markets to deflect those concerns than in the past couple of months. But this kind of dynamic would pose a risk to the pro-cyclical tilt here.

Weighing cyclical versus structural forces in EM

The notion of stronger equities, cyclical outperformance and upward pressure on bond yields fits well with our core market views for 2014. The prospect of a period of outperformance in EM and commodity-related areas fits less well with our medium-term views. We have been structurally more cautious about the EM universe, at least relative to DM, given the adjustments that we still think are needed there. So a key question is how much to reverse that view tactically.

Exhibit 10: Improving US and china growth would help cyclical assets

	Response of asset to shock:	US growth *higher*	+ EM/China growth *higher*	+ *Neutral* US monetary policy	= Total?
Stocks	US	++	+?	0	++?
	Domestic cylicals	++	0	0	+
	Global Cyclicals	+	+	0	+
	Defensives	+?	0	0	0
	EM	+	++?	0	++?
Rates	US yields	++	+	0	++?
FX	$	+?	-	0	-?
	$/JPY	+	+?	0	+
	$/EM	+	-	0	0
Relative equity	EM vs DM	-	+	0	0/+?
	Glob Cyc vs Def	+?	+	0	+
	Dom Cyc vs Def	++?	0	0	+

Scale shows likely response to each shock ranging from most positive to most negative on the following scale: ++, ++?, +, +?, 0, -?, -, - -?, - -. For negative shocks, signs would be reversed.
Source: Goldman Sachs Global Investment Research.

Last year highlighted the benefits of sticking to the structural story. The last period of GLI Expansion that ran from April to August 2013 was a dramatic exception to the 'average' lesson shown in Exhibit 9. EM assets underperformed sharply, the USD rallied against EM and commodity currencies and commodity prices underperformed. But that period was itself unusual. Although a clear recovery in DM activity (driven in part by sharply better European data) drove the GLI higher, there was a significant deceleration in Chinese growth over the second quarter of last year. The 'taper tantrum' caused a sharp shock to the term premium in US bonds over that period, which saw financial conditions tighten over the summer (Exhibit 11). This was particularly damaging given the low risk premium in bond markets generally and in EM in particular. Despite the improving DM growth picture, this combination was more naturally associated with EM weakness and USD strength than an 'average' GLI Expansion would be.

We do not expect these dynamics to be repeated to the same degree over the next couple of months. The China growth recovery is unlikely to be very vigorous and the medium-term constraints from the attempts to crack down on pollution, corruption and the shadow banking system are likely to reassert themselves before too long. But we doubt that further deceleration is coming in the near term, as it did in the last GLI Expansion phase. And, although we think the EM adjustments are not over, risk premia in EM rates and credit are significantly higher than they were a year ago (and their spreads to DM rates and credit are much higher), EM currencies are generally less overvalued, and significant portfolio adjustments and outflows from the asset class have been substantial.

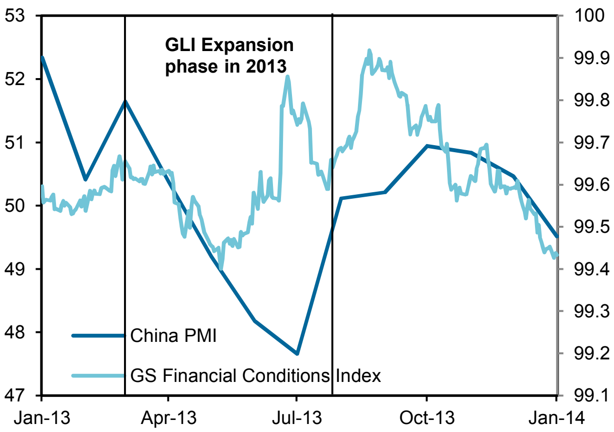
As a result, we are more willing to entertain the notion that EM outperformance can continue and that the normal tactical benefits of an improving global cycle may be reflected in these areas. At a minimum, we think this is a dangerous environment to press structural views of underperformance until fresh catalysts become clear. Our view remains that the adjustments in EM economies and assets are not yet over and that the medium-term risk/reward continues to favour DM. But we think the cyclical environment may provide some relief from the structural downtrend for a while longer, as it did in late 2012.

One foot in front of the other

The key issue, of course, is whether the acceleration in growth that we are forecasting occurs convincingly. But, in assessing the prospect that cyclical improvement can continue to drive equities, cyclical assets and bond yields higher, two other issues that we highlighted as risks earlier in the year are likely to become more prominent again:

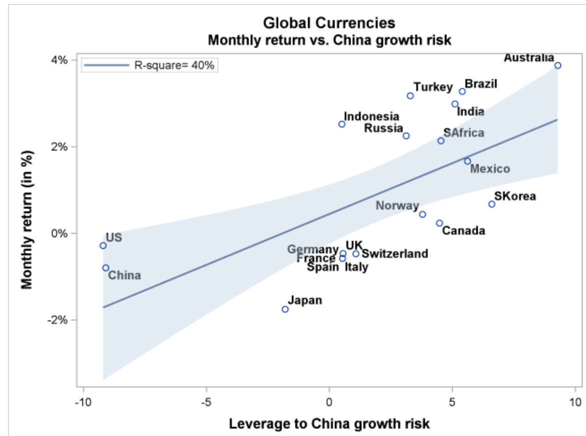
- **Whether rising bond yields will act as a brake on further progress in other assets**. As growth improves, the balancing act between rates and equities will remain an important part of the environment. The key risk to the current relief in EM assets is that US rates move up more rapidly again. We still think the risk premium in the front end of the US rates curve is too low, so there is a chance that improving growth has an outsized effect on that part of the curve. In addition, we have renewed a bearish tactical stance on bonds, as the growth picture improves. But we think the risks to longer-dated yields are much more modest than during the 'taper tantrum' and that rising yields are more likely to be growth-driven than reaction-function driven. If we are right, they should be easier to digest than last summer.

Exhibit 11: Last year's GLI Expansion coincided with China weakness and tighter financial conditions



Source: Goldman Sachs Global Investment Research.

Exhibit 12: China-exposed assets have already outperformed recently, particularly in FX



Source: Goldman Sachs Global Investment Research.

- **Whether improvement is already priced.** Consensus expectations are – like our own – for some improvement in both US and Chinese growth over the next few months. Over the last two weeks markets have already moved quite quickly under the surface to reflect the kinds of dynamics we have discussed: equities and government bond yields are higher; EM equities, credit and currencies have outperformed meaningfully; and commodity currencies such as the AUD have rebounded (Exhibit 12). So one worry is that the market is already reflecting the kind of modest growth acceleration we expect. On that front, we are more confident in the prospects and sustainability of a growth recovery in the US than in China, where the constraints of credit imbalances could outweigh attempts at stimulus.

Although the disagreements we describe here are more tactical in nature, market pricing reflects more anxiety about the pricing of the growth outlook than at the start of the year. And while the market's modal view is that the economic outlook will improve, we think the perception of risks around that forecast is firmly skewed to the downside. If that is correct, then there is still room for relief or repricing simply on the basis of realising the central case.

We suspect there is a larger lesson here. Our key structural views – a belief in a US recovery and benign DM inflation, balanced by greater concern about imbalances in China and the broader EM universe – are more widely reflected both in consensus forecasts and, more importantly, market pricing than they were a year ago. While they remain an important anchor for our core views, we think this means that gauging tactical shifts around those themes is likely to be more important than was the case last year.

Dominic Wilson

Global economic forecasts

Real GDP, %ch yoy

	2014	2015	2016	2017
G3				
USA	2.7	3.2	3.0	3.0
Euro area	1.2	1.5	1.7	1.6
Japan	1.0	1.3	1.5	1.4
Advanced Economies				
Australia	2.0	2.6	3.6	3.9
Canada	2.5	2.4	2.1	2.0
France	0.9	1.1	1.4	1.8
Germany	2.0	2.1	2.2	1.6
Italy	0.6	1.0	1.2	1.3
New Zealand	3.1	2.1	2.4	2.3
Norway	1.8	2.0	1.7	1.7
Spain	0.9	1.2	1.7	1.7
Sweden	3.6	3.4	2.8	2.7
Switzerland	1.9	2.1	1.9	1.7
UK	3.0	2.7	3.0	3.0
Asia				
China	7.3	7.6	7.6	7.4
Hong Kong	3.7	4.4	3.7	4.0
India	5.2	6.2	6.6	6.9
Indonesia	5.5	6.0	6.0	6.0
Malaysia	4.5	5.2	5.0	5.0
Philippines	6.3	6.5	6.3	6.3
Singapore	3.7	4.2	4.0	4.0
South Korea	3.7	3.8	4.0	3.8
Taiwan	3.8	3.9	3.8	3.8
Thailand	3.0	4.7	5.0	5.0
CEEMEA				
Czech Republic	2.6	2.4	2.6	2.4
Hungary	2.2	2.0	2.2	1.9
Poland	3.2	3.3	3.4	3.2
Russia	1.0	3.0	4.4	4.4
South Africa	2.4	2.9	3.6	3.5
Turkey	2.0	1.8	5.8	5.0
Latin America				
Argentina	-0.8	-1.2	2.8	5.1
Brazil	1.8	1.8	2.7	3.7
Chile	3.3	4.5	4.5	4.5
Mexico	3.3	3.8	3.6	3.6
Venezuela	-1.3	0.5	1.8	2.7
Regional Aggregates				
BRICS	5.7	6.3	6.6	6.7
G7	2.2	2.5	2.5	2.4
EU27	1.7	1.9	2.0	1.9
G20	3.4	3.9	4.2	4.2
Asia ex Japan	6.1	6.6	6.7	6.7
Central and Eastern Europe	2.9	2.9	3.0	2.9
Latin America	2.1	2.5	3.3	3.9
Emerging Markets	4.9	5.6	6.1	6.2
Advanced Economies	2.2	2.5	2.5	2.5
World	3.4	3.9	4.1	4.2

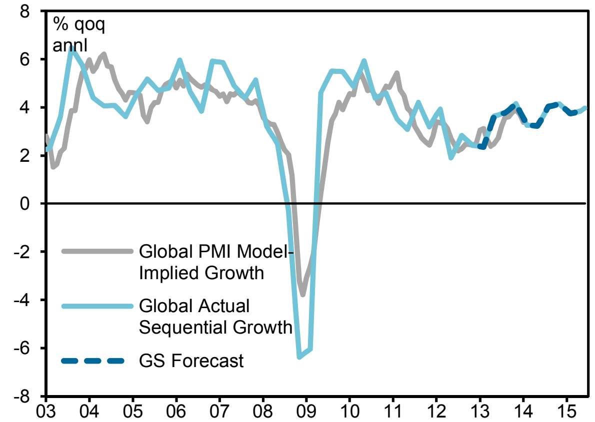
Consumer Prices, %ch yoy

	2014	2015	2016	2017
G3				
USA	1.6	1.9	2.1	2.2
Euro area	0.9	1.5	1.8	1.9
Japan	2.6	1.7	2.1	1.0
Advanced Economies				
Australia	3.2	2.6	2.8	2.4
Canada	1.5	1.8	2.0	2.0
France	1.0	1.3	1.6	1.6
Germany	1.4	2.5	2.9	2.9
Italy	0.9	1.3	1.4	1.5
New Zealand	2.0	2.2	2.2	1.9
Norway	1.7	1.5	1.8	2.0
Spain	0.3	0.6	0.8	1.0
Sweden	0.6	1.5	2.3	2.5
Switzerland	0.4	1.3	1.6	1.9
UK	1.8	1.8	1.8	1.9
Asia				
China	2.6	3.0	3.0	3.0
Hong Kong	3.3	3.3	3.1	3.1
India	6.5	6.1	5.8	5.2
Indonesia	6.8	5.5	5.5	5.5
Malaysia	3.0	2.6	2.5	2.5
Philippines	3.8	3.5	3.5	3.5
Singapore	3.3	3.5	3.2	2.8
South Korea	1.8	2.4	2.6	2.2
Taiwan	1.4	1.8	1.8	1.7
Thailand	2.6	2.9	3.0	2.8
CEEMEA				
Czech Republic	0.9	1.8	2.0	2.1
Hungary	0.8	2.7	3.1	3.4
Poland	1.3	2.0	2.4	2.2
Russia	5.8	4.2	4.1	3.8
South Africa	6.3	6.1	6.0	5.4
Turkey	7.9	7.1	6.1	6.5
Latin America				
Argentina	27.8	30.7	20.8	15.2
Brazil	6.0	5.8	5.5	5.1
Chile	3.9	2.4	3.0	3.0
Mexico	4.1	3.5	3.1	3.0
Venezuela	57.3	50.1	28.3	20.8
Regional Aggregates				
BRICS	4.1	4.1	3.9	3.7
G7	1.7	1.8	2.1	2.0
EU27	1.0	1.6	1.9	2.0
G20	3.0	3.1	3.1	2.9
Asia ex Japan	3.5	3.7	3.6	3.5
Central and Eastern Europe	1.1	2.1	2.4	2.4
Latin America	11.5	9.6	6.9	5.7
Emerging Markets	5.8	5.2	4.6	4.2
Advanced Economies	1.6	1.8	2.1	2.0
World	3.4	3.3	3.2	3.0

Source: Goldman Sachs Global Investment Research
For India we use WPI not CPI. For a list of the members within groups, please refer to ERWIN.
For our latest Bond, Currency and GSDEER forecasts, please refer to the Goldman Sachs 360 website: (https://360.gs.com/gs/portal/research/econ/econmarkets/).

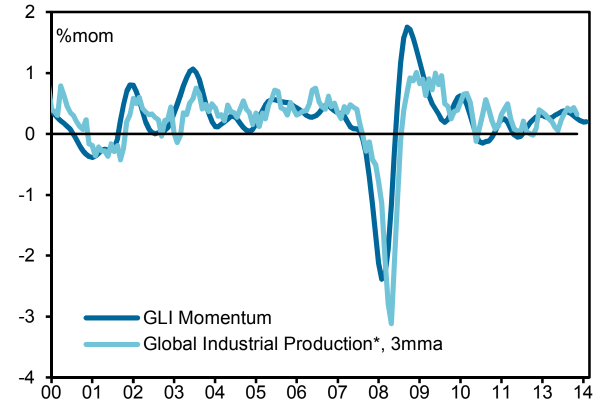
Global macro and markets charts

PMI-implied global growth



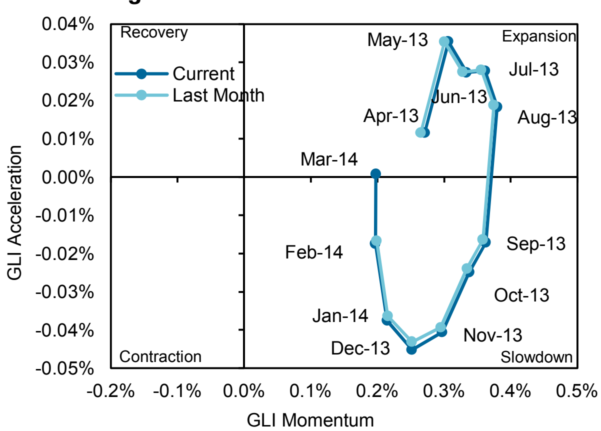
See *Global Economics Weekly 12/18* for methodology
Source: OECD, Goldman Sachs Global Investment Research

GLI momentum vs. global industrial production*



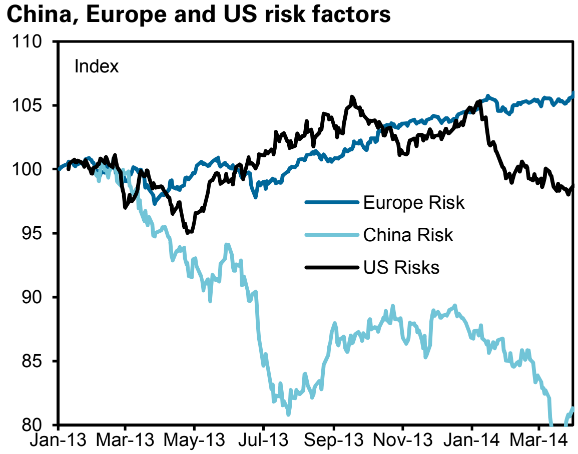
* Includes OECD countries plus BRICs, Indonesia and South Africa
See *Global Economics Paper 199* for methodology
Source: OECD, Goldman Sachs Global Investment Research

GLI 'Swirlogram'



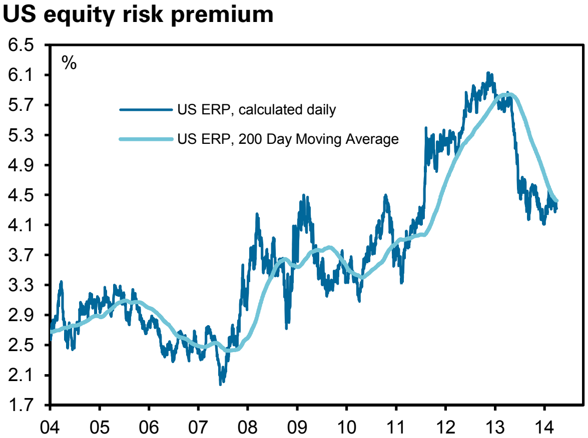
See *Global Economics Paper 214* for methodology
Source: OECD, Goldman Sachs Global Investment Research

China, Europe and US risk factors



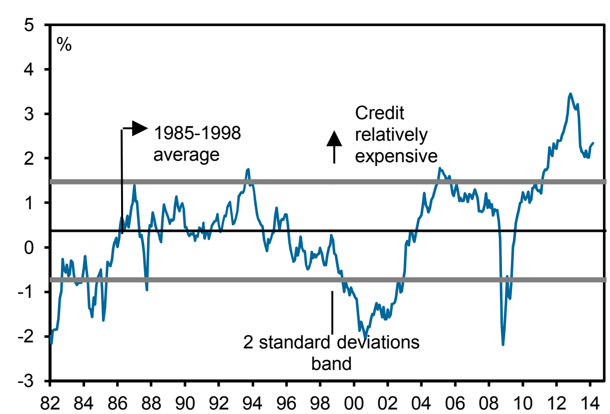
See *Global Economics Weekly 12/15* for methodology
Source: Goldman Sachs Global Investment Research

US equity risk premium



See *Global Economics Weekly 02/35* for methodology
Source: Goldman Sachs Global Investment Research

US equity credit premium



See *Global Economics Weekly 03/25* for methodology
Source: Goldman Sachs Global Investment Research

The world in a nutshell

THE GLOBAL ECONOMY

	OUTLOOK	KEY ISSUES
UNITED STATES	We expect annual growth to accelerate to 2.7% in 2014 after 1.9% in 2013. Growth should then remain above trend in 2015 and 2016 at 3.2 and 3.0% respectively. On an annualised sequential basis, we expect growth of 1.5% in the first quarter of 2014 and 3.0%-3.5% for the rest of the year.	We expect the US to lead the reacceleration in global growth in 2014. The rationale is a sharp reduction in fiscal drag, which should allow the continued recovery in underlying private-sector spending to translate into a stronger growth picture. In particular, we expect positive impulses from personal consumption and business fixed investment to add significantly to growth in 2014.
JAPAN	We expect real GDP growth of 1.0% in 2014 and 1.3% in 2015. On a sequential basis, we expect volatile growth over the coming quarters as forthcoming consumption tax hikes in 2014 and 2015 will affect personal consumption expenditures. We expect positive private demand dynamics to continue but worry about increased fiscal drag.	Structurally, Japan is poised to reach above-trend growth rates in step with an improvement in the global economy. The new leadership at the BoJ has led to a regime shift in Japanese monetary policy, with much more aggressive, Fed-style easing capabilities. While this potentially offers a way out of more than a decade of deflation, reaching the 2% inflation target remains a tall order.
EUROPE	For the Euro area as a whole, we expect a return to positive growth of 1.2% in 2014, followed by 1.5% in 2015. The growth outlook at the country level looks friendlier than in 2013 but it still shows a divergent trajectory, with growth in Italy, Spain and France around or less than 1% and in Germany at 2%. At the same time, private-sector headwinds remain as banking lending standards have continued to tighten.	We expect the Euro area to continue pulling out of recession, driven by modest improvements across all major components of domestic demand. Still, the list of necessary adjustments in the periphery remains long, ranging from cleaning up the banking system and labour market reform to increasing competitiveness.
NON-JAPAN ASIA	For Asia ex-Japan, we expect growth of 6.1% and 6.6% in 2014 and 2015, respectively. We expect the economies in the region to benefit from the stronger DM recovery in 2014, but with significant differentiation across countries.	In China, we expect real GDP growth of 7.3% in 2014, and 7.6% in 2015. Although growth is slightly below trend, the recent tightening in financial conditions sends the signal that policymakers are willing to tolerate somewhat lower growth in order to tackle structural problems and foster more sustainable medium-term growth.
LATIN AMERICA	We forecast that real GDP growth in Latin America will be 2.1% in 2014 and 2.5% in 2015. Against a more favourable global backdrop, the divergence between those economies with more challenging (Brazil) and more stable (Mexico) policy outlooks is likely to increase.	In Brazil, we expect real GDP growth of 1.8% in 2014 and 2015. Despite two consecutive years of sub-par growth, inflation has been sticky above the inflation target of 4.5%. BRL weakness will likely force the Copom to continue to hike policy rates.
CENTRAL & EASTERN EUROPE, MIDDLE EAST AND AFRICA	With growth across the region forecast at 2.3% in 2014 and 3.0% in 2015, we expect CEEMEA to continue to recover. Helped by improvements in external demand conditions, large output gaps provide fertile ground for recovery from the 2012 soft patch, although current account deficit countries in particular will continue to face stiff challenges.	The EM differentiation theme is again visible across the region. While we forecast strong and steady growth in Israel and Russia, we see a similar recovery in Turkey as less sustainable. Growth in South Africa and Ukraine will likely be dragged down by idiosyncratic political and economic risks.

CENTRAL BANK WATCH

	CURRENT SITUATION	NEXT MEETINGS	EXPECTATION
UNITED STATES: FOMC	The Fed funds rate is at 0%-0.25%. The Fed initiated a new round of asset purchases and extended its rate guidance on September 13, 2012.	Apr. 30 June 18	We expect the Fed to keep the funds rate near 0% through 2015, and to continue asset purchases until 3Q2014, albeit at a reduced pace.
JAPAN: BoJ Monetary Policy Board	The overnight call rate is at 0%-0.1%. The BoJ significantly extended asset purchases, as well as the related maturity horizon, on April 4, 2013.	Apr. 8 Apr. 30	We expect the BoJ to expand its monetary easing efforts through ongoing asset purchases and to enact another round of QQE in 2Q2014.
EURO AREA: ECB Governing Council	The refi/deposit rates are at 0.25%/0.00%. The ECB announced the OMT programme for conditional purchases of Euro area sovereign bonds in Sept. 2012 and cut the refi rate by 25bp on Nov. 7, 2013.	Apr. 3 May 8	We expect the ECB to cut the MRO and deposit rate by 15bp at its April meeting.
UK: BoE Monetary Policy Committee	The BoE policy rate is currently at 0.5%. The BoE announced threshold-based forward guidance for the path of the policy rate on August 7, 2013.	Apr. 10 May 8	We expect the BoE to keep the policy rate unchanged until mid- 2015.

Disclosure Appendix

Reg AC

We, Dominic Wilson, Kamakshya Trivedi, Noah Weisberger, Aleksandar Timcenko, Jose Ursua, George Cole and Julian Richers, hereby certify that all of the views expressed in this report accurately reflect our personal views, which have not been influenced by considerations of the firm's business or client relationships.

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