



GLOBAL MACRO OUTLOOK

OCTOBER 2019

KEY FORECAST TRENDS

- + The global economy is moving into a period of protracted weakness in which growth is likely to remain positive but significantly lower than potential.
- + Central banks are alive to the risk that weak growth might turn into a deeper and more damaging downturn. The Fed and ECB have eased policy in recent weeks, and we expect more of the same over the coming year.
- + One of the keys to the 2020 outlook is policy effectiveness. We are confident that Chinese policymakers will be able to prevent a destabilizing slowdown in growth and are hopeful the Fed can do likewise. But we're more worried about Europe and Japan, where monetary policy may already have run out of road.
- + Many see fiscal policy as the answer, and we've long thought that's where the world is headed as it grapples with high debt and weak secular growth and inflation. For now, though, we're skeptical that the fiscal response will be aggressive enough or broad enough to change the business cycle for the better.
- + The result: central banks are still on the hook as the global economy weakens. This means more policy easing and low (or lower?) interest rates for the foreseeable future.

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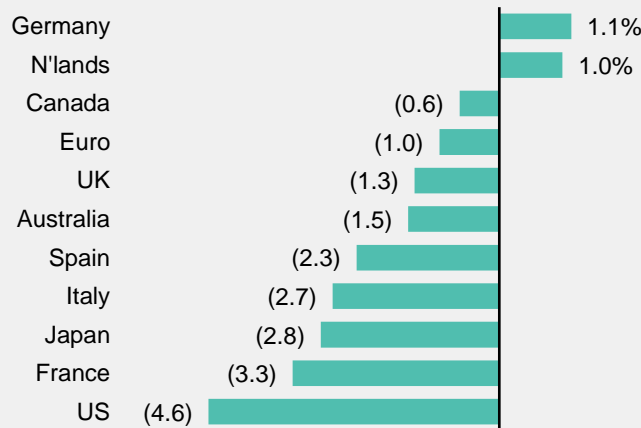
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The Baton Passes to Fiscal Policy . . . Slowly!

General Government Budget Balances (2019E)



As of April 12, 2019. IMF estimates

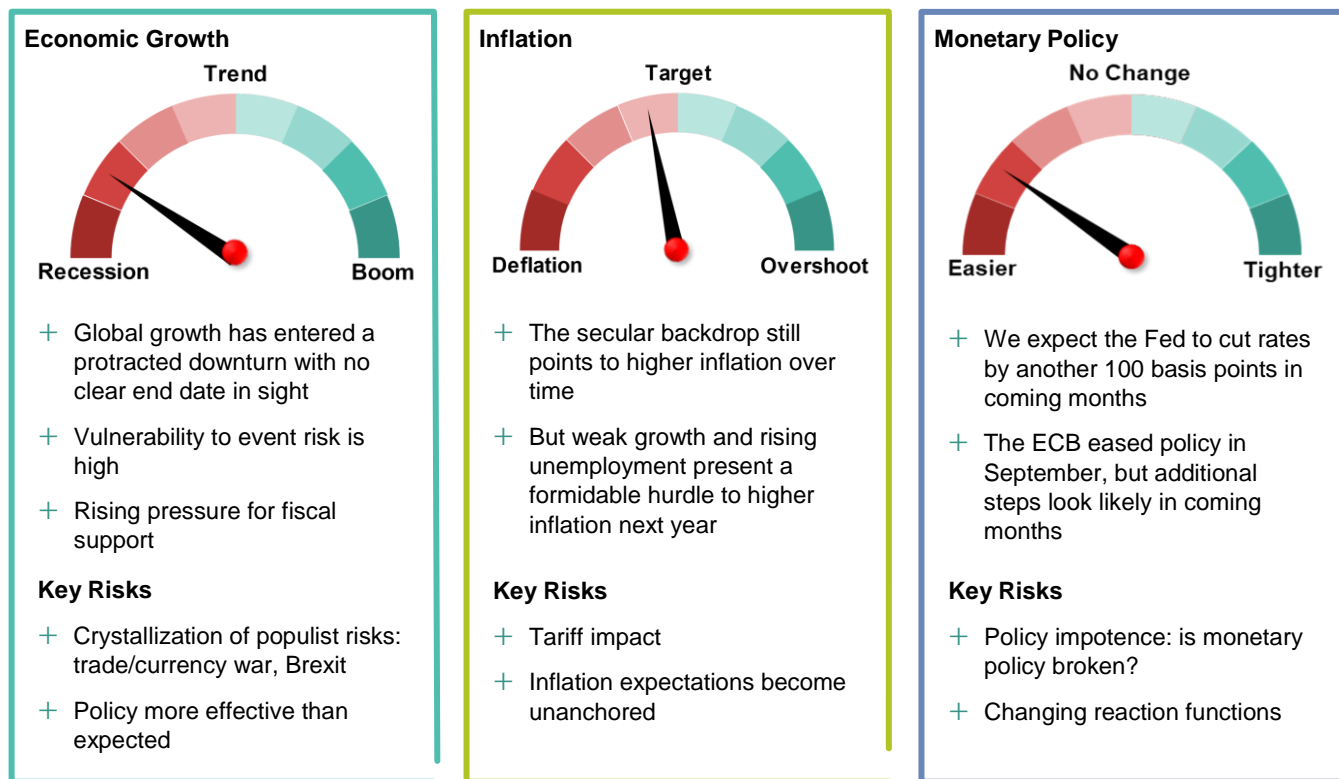
Source: Haver Analytics and International Monetary Fund (IMF)

+ With monetary policy losing traction, fiscal policy is likely to play a more active role in trying to lift growth and inflation. Nowhere is the need greater than in Europe.

+ European fiscal positions are in much better health than they were a few years ago, with ultralow interest rates providing extra room for maneuver.

+ But barring a more rapid slowdown in growth, we expect most governments to use their increased fiscal space only slowly.

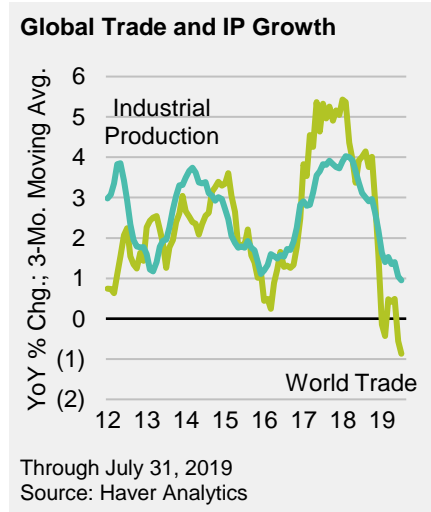
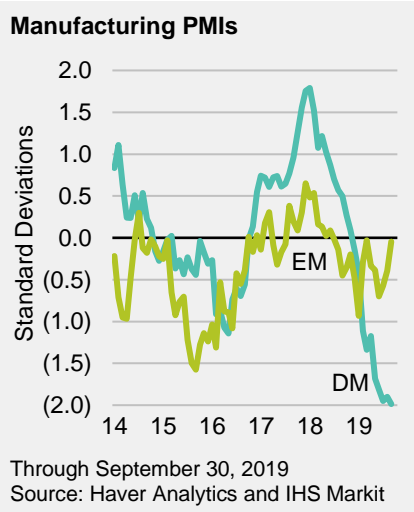
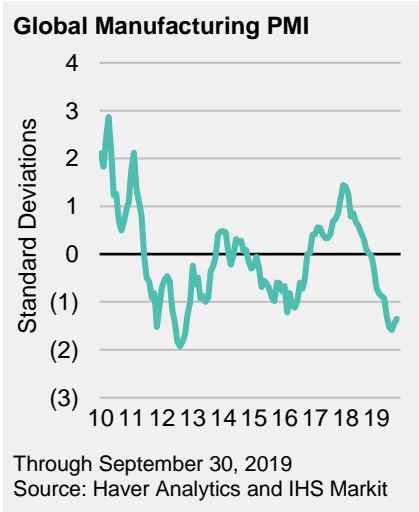
GLOBAL FORECASTS



OUTLOOK

- + We did not change our 2020 global growth forecast this month. But we did sharply downgrade our expectations last month and now expect the world economy to grow by 2.3% next year, which will make 2020 the weakest year of global growth since 2009 (when it contracted by 2.0%).
- + We are most concerned about high-income, trade-sensitive economies like the euro area and Japan. We expect the euro area to grow by just 0.3% next year and Japan to contract by 0.4%. Both are well below consensus—1.0% for the euro area and 0.3% for Japan. We are also slightly below consensus on the US (1.5% vs. 1.7%) but in line on China (6.0%).
- + The secular backdrop still points to higher inflation. But cyclical developments clearly point in the opposite direction, and we expect global inflation to fall to 2.7% in 2020 from 2.9% this year.
- + Monetary easing is under way and likely to continue. We expect the Fed to cut rates by another 100 basis points (b.p.) and the European Central Bank (ECB) to announce an additional rate cut and more aggressive asset purchases.

Global Cyclical Outlook: Moving into a Protracted Downturn



GLOBAL MARKET OUTLOOK: YIELD CURVES

GLOBAL YIELDS

Global—Bond yields in many markets have fallen to record lows. But with the global economy entering a protracted downturn and central banks injecting fresh monetary stimulus, the case for a near-term increase is weak.

US—US yields have pushed even lower as concern about low inflation and poor global growth has mounted. We remain cautiously optimistic that the worst outcomes will be avoided and thus expect a modest rise in yields over the medium term. But a near-term trigger is hard to find, so it may well be some time before any increase occurs.

Euro Area—With the economy likely to undershoot the ECB's expectations, another deposit rate cut and a faster pace of monthly asset purchases are likely to be announced around the turn of the year. The case for higher yields has dissipated.

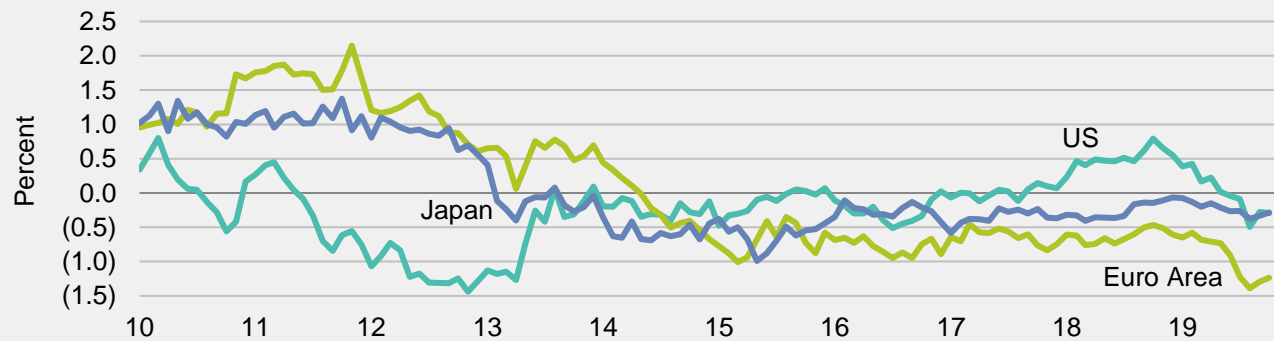
Japan—Quantitative and qualitative easing (QQE) with yield-curve control (YCC) should anchor 10-year yields close to, or below, zero over the forecast horizon.

10-Year Yields: AB vs. Consensus Year-End Forecasts (%)

	AB		Consensus	
	2019	2020	2019	2020
US	1.75	1.75	1.69	1.95
Euro Area	(0.65)	(0.50)	(0.51)	(0.20)
Japan	(0.20)	(0.20)	(0.19)	(0.08)
China	3.00	2.90	2.93	2.76

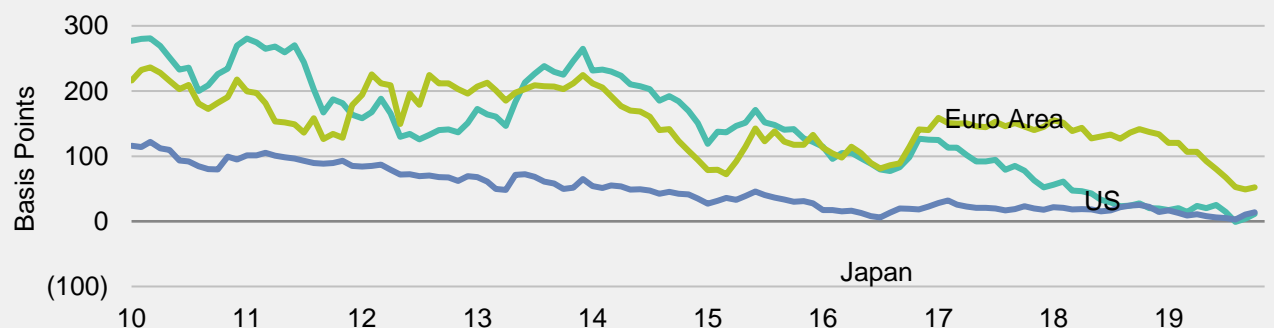
As of October 2, 2019
Source: Bloomberg and AB

Real 10-Year Bond Yields*



*Current 10-year bond yield less five-year/five-year forward inflation swap
Through October 2, 2019; Source: Bloomberg and AB

Yield Curves: 10-Year Bond Yield less Two-Year Bond Yield



Through October 2, 2019
Source: Bloomberg and AB

GLOBAL MARKET OUTLOOK: CURRENCIES

FX FORECASTS

USD—The dollar has strengthened as growth has slowed more abruptly overseas than it has in the US. But with the Fed likely to cut rates aggressively in coming months and possible currency intervention on the horizon, it's hard to see the dollar sustaining further gains.

JPY—The yen is likely to benefit as global growth slows further and risk-asset headwinds intensify.

EUR—Weak growth, the prospect of more monetary stimulus around the turn of the year and the heightened risk of a no-deal Brexit mean there are few reasons to buy the euro.

CNY—The CNY outlook remains heavily dependent on developments in the US-China trade war.

Global FX: AB vs. Consensus Year-End Forecasts (%)

	AB		Consensus	
	2019	2020	2019	2020
EUR/USD	1.13	1.13	1.10	1.16
USD/JPY	102	95	106	103
USD/CNY	7.20	7.15	7.20	7.15
EUR/GBP	0.92	0.92	0.90	0.88

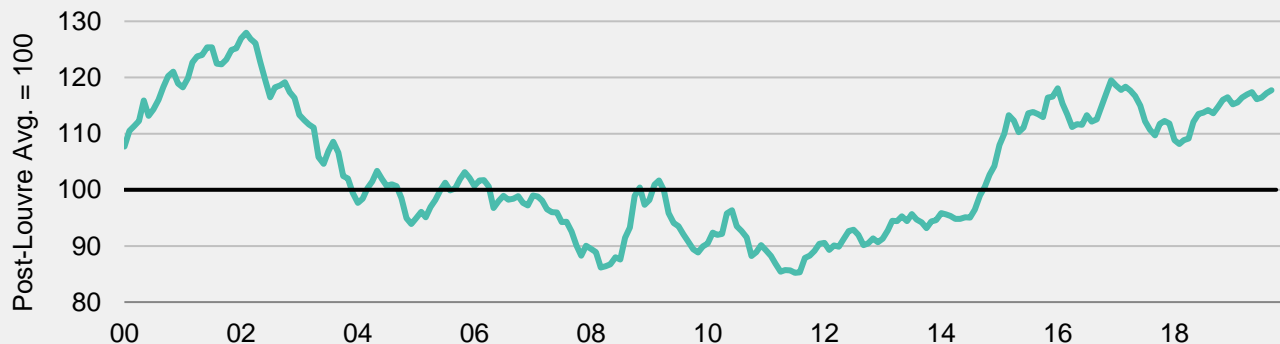
As of October 2, 2019
Source: Bloomberg and AB

Nominal USD Exchange Rate: U.S. Dollar Index



Through October 2, 2019
Source: Bloomberg and AB

Real USD Exchange Rate



Through September 30, 2019
Source: Bloomberg and AB

US

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
US	2.0	1.5	2.3	2.3	1.38	0.88	1.75	1.75

OUTLOOK

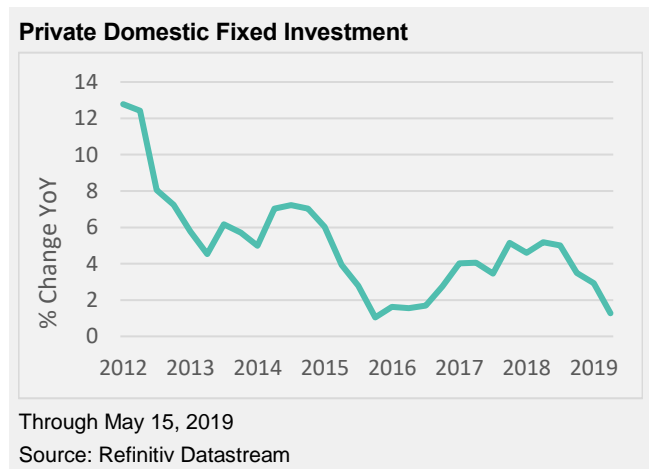
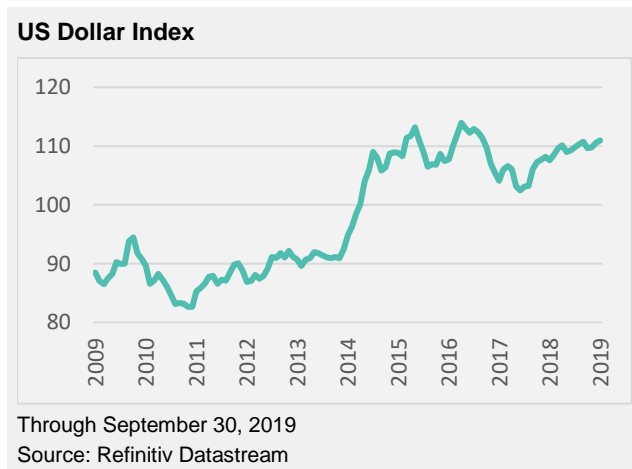
- + The US economy is looking increasingly precarious. The effects of the trade war are evident in the manufacturing sector, which has fallen into contractionary territory. The only question that really matters now is whether that slowdown will spill over into the broader economy.
- + The labor market and the consumer are the keys to the forward outlook. History suggests that the weakness in industry will eventually manifest itself in a deteriorating labor market, but this hasn't happened yet. As long as firms are willing to keep adding employees rather than laying them off, the economy as a whole can muddle through. But we are on high alert for evidence that falling business sentiment will hit employment in the coming months.
- + The Federal Open Market Committee has cut rates twice, and we expect more easing to come. That will help the economy. We do note, however, that the primary culprit for slowing growth isn't the level of interest rates—it is trade policy. We are unconvinced that lower rates alone will be enough to address the slowdown.

RISK FACTORS

- + The global economy is decelerating further, and the blowback from that slower growth is a headwind to US growth both directly and indirectly via financial markets.
- + The political climate seems to us to have deteriorated further, and with a presidential election just over the horizon, businesses could simply decide not to make investments until there is more clarity about the political cycle.

OVERVIEW

Evidence of an economic slowdown continues to mount, with the most trade-exposed sectors of the economy suffering the most. A deteriorating global environment doesn't help—it both limits US exports and tightens financial conditions domestically by pushing the dollar higher and creating financial market volatility. More predictable trade policy would help, of course, but at this point we think enough damage has been done that a slowdown is inevitable. The question is really one of magnitude. Will the strength in the labor market persist and allow the economy to remain stable? Or will slowing capital expenditures and business investment spill over into the labor market and thus impact consumption? Our forecasts split the difference: we expect some weakening of the labor market and thus of overall economic growth, but not so much as to push the domestic economy into outright recession. We expect the Fed to keep cutting rates to prolong the expansion and for those rate cuts to help, but we don't see a trigger for growth to accelerate. Slow, steady growth is now the upside scenario, while slower growth is the base case.



Euro Area

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Euro Area	1.1	0.3	1.2	1.1	(0.70)	(0.70)	(0.65)	(0.50)	1.13	1.13

OUTLOOK

- + The euro-area outlook remains challenging, and we expect growth to slip to 0.3% in 2020 from 1.1% this year. That's well below the ECB's 1.2% projection for next year, reflecting deep concerns about the region's vulnerability to weak global growth and lack of effective policy tools.
- + Core inflation has been rooted around 1.0% for the last 18 months. With growth slowing and unemployment set to rise, we see few grounds for expecting core inflation to rise, let alone move close to the ECB's target.

RISK FACTORS

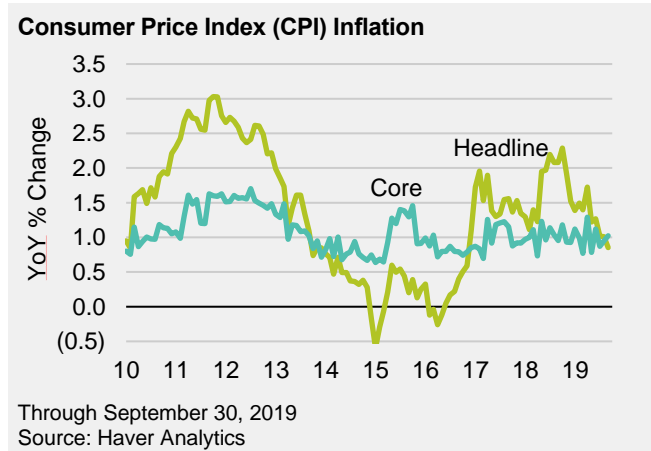
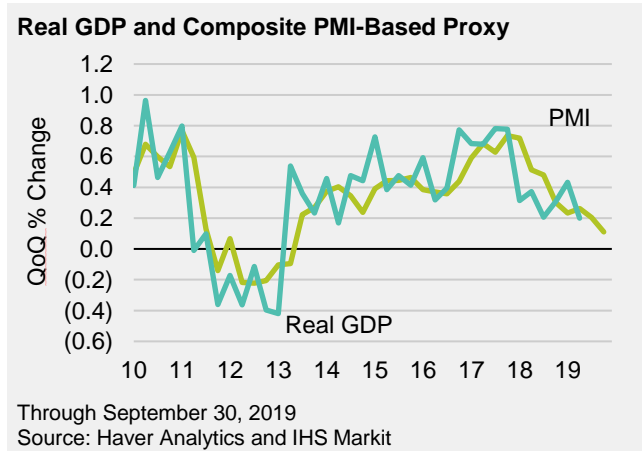
- + Risks to growth are evenly balanced. But it is still much easier to see growth surprising materially to the downside than the upside.
- + Our forecasts assume that recessionary conditions in manufacturing gradually spill over into weaker employment and capital spending growth and that policy will be ineffective in stimulating growth and inflation. If these assumptions are wrong—perhaps because of a more aggressive fiscal response than expected—growth could surprise on the upside.
- + The risk of a no-deal Brexit is an important downside risk, particularly given our concerns about policy flexibility and effectiveness in the euro area.

OVERVIEW

The composite PMI fell to 50.1 in September from 51.9 in August and is now at its lowest since June 2013, when the euro area was recovering from the sovereign-debt crisis. At current levels, the composite PMI is consistent with annualized real GDP growth of 0.5% and is tracking well below the ECB's latest expectations. The most worrying aspect of the September data was the fall in the services PMI (52.0 vs. 53.5 in August). That's still significantly stronger than the manufacturing PMI (45.7) but might be the first sign that trade-related weakness is beginning to spill over into the domestic economy.

Core inflation rose to 1.0% in September from 0.9% in August. Looking through the monthly noise, core inflation has been trendless at around 1.0% for the last three years. The ECB's latest forecasts see core inflation rising to 1.2% next year and 1.5% in 2021. But with growth slowing and unemployment set to rise, we see very little prospect of this happening.

The ECB responded to weak data and persistently low inflation by cutting interest rates and announcing a new asset purchase program at its September council meeting. While the open-ended nature of the ECB's bond purchases is a positive development, the monthly purchase pace (€20 billion) looks modest, and we expect a further rate cut and faster purchase pace to be announced around the turn of the year. While the September decision was controversial, we do not expect opposition from a minority of Governing Council members to prevent incoming President Christine Lagarde from easing policy.



Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Japan	1.1	(0.4)	0.8	0.9	(0.10)	(0.15)	(0.20)	(0.20)	102	95

OUTLOOK

- + The global trade conflict continues to undermine Japan's manufacturing sector.
- + The labor market remains tight, but there are tentative signs of a turning point. Consumer confidence has slipped.
- + As other global central banks ease, the Bank of Japan's (BOJ) options remain limited—but tweaks are likely.
- + A prolonged downturn in the global economy should lead to further yen strength.

RISK FACTORS

- + Apart from the fallout from October's value-added tax (VAT) hike, most of the key risks are external and will likely materialize through a sharp appreciation of the yen.

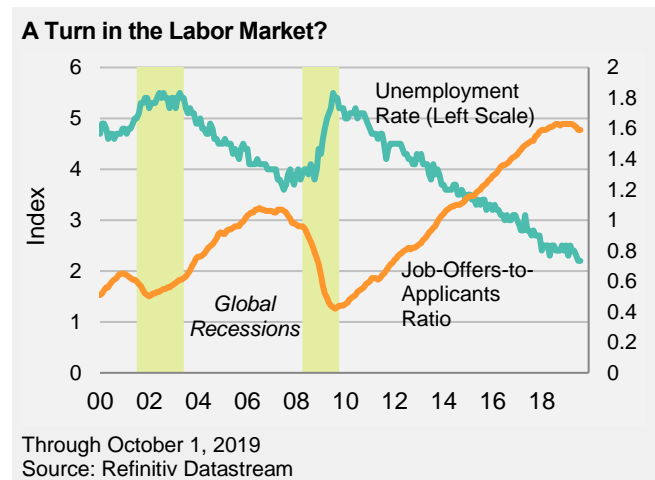
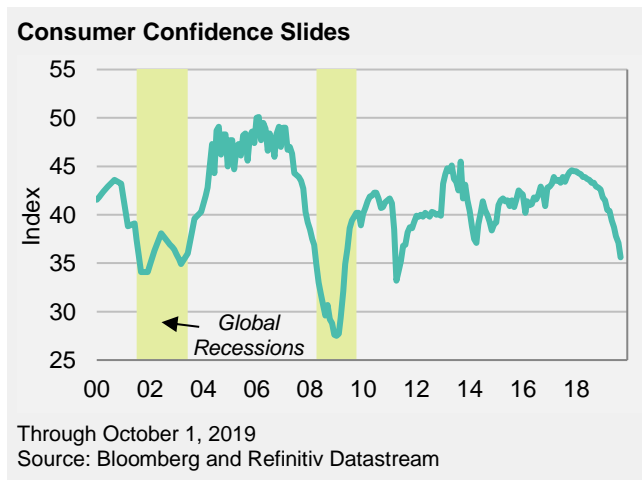
OVERVIEW

Last month we made a significant downgrade to Japan's growth outlook for 2020 so that we now expect to see a mild contraction in GDP. Nothing in recent weeks has caused us to reassess that decision.

The manufacturing sector remains under pressure, with the manufacturing PMI mired below 50, and the BOJ's quarterly Tankan survey continuing to drift lower. Industrial production growth remains in negative territory. None of this is particularly surprising because there's little sign of a turn in the global trade cycle.

At the same time, consumer confidence continues to slide, hitting 35.6 in September, the lowest level since early 2011 (following the Tohoku earthquake and tsunami). The VAT hike enacted on October 1 may be partly responsible for this slump. But the decline is already more severe than that which surrounded the (larger) VAT hike in 2014.

The VAT hike is likely to push headline CPI higher in the months ahead. But core inflation remains relatively stable, and far shy of the BOJ's target. With other central banks acting to ease policy, this continues to be a source of pressure on the BOJ. We would not be surprised to see some tweaks to the policy framework, particularly if the yen strengthens materially. But we doubt there's much in the monetary policy locker that will be effective.



China

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
China	6.2	6.0	2.5	2.4	4.35	4.10	3.00	2.90	7.20	7.20

OUTLOOK

- + The official Chinese real GDP growth rate will likely be around 6.2% in 2019, down from 6.6% in 2018, as weakness in capex spending persists.
- + We expect continued monetary and fiscal policy easing to counter downward pressure on the economy. The focus will likely be on infrastructure projects and property easing—the measures most likely to help stabilize the economy.
- + Rising pork prices may push up inflation, but we don't think the increase will limit the central bank's policy easing.

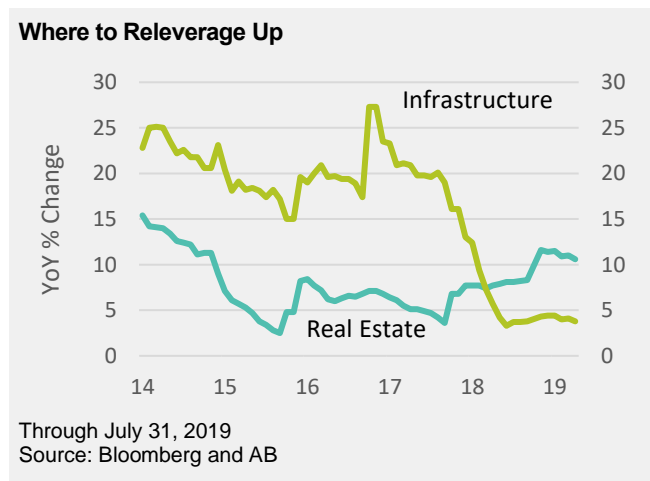
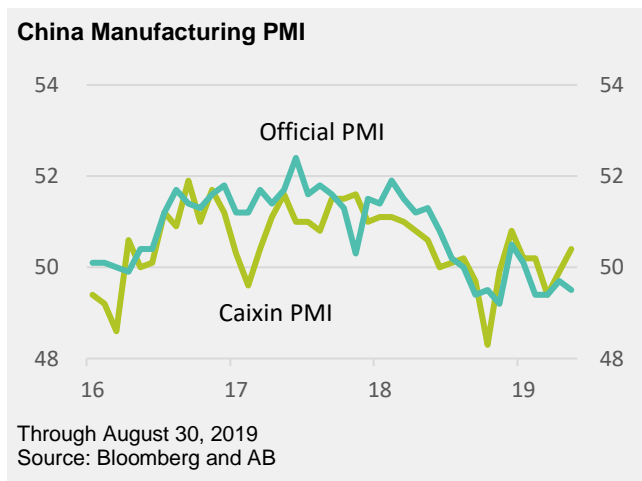
RISK FACTORS

- + Policy easing may be less effective than expected if economic data surprise significantly to the downside. This would put sustained economic stabilization at risk this year and next.
- + An underwhelming US-China trade deal—if one comes at all—would be another risk for China's economy.

OVERVIEW

Trade-related uncertainty has made Chinese capex expansion less likely. We still think that China has enough ammunition when it comes to easing policy. On the monetary side, that included the ability to cut the reserve requirement ratio and the loan prime rate again by 5 b.p. to 4.20% in September. We also expect the central bank to guide down the medium-term lending facility rate in the next month or so. On the fiscal side, the government can issue more special local government bonds. The official target is CNY2.1 trillion for 2019, but we think the government can do more, as infrastructure projects are most effective in stabilizing growth.

If the Chinese economy stabilizes this year—and we think that it will—China's currency should become a global currency stabilizer. Even so, we cannot ignore the ongoing trade tensions between China and the US. Further escalation of a 30% tariff on all US\$550 billion in imported Chinese goods would pose a bigger risk to China and the global economy, and we think it would push the USD/CNY rate toward 7.5. We continue to believe persistent downward pressure on the Chinese economy requires persistent easing. China has passed an important stress test over the last year or so of rising trade tension with the US, and will continue to deliver the easing measures needed to avoid an abrupt slowdown in growth.



Canada

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Canada	1.8	1.5	2.1	2.1	1.50	1.00	1.50	1.50	1.30	1.35

OUTLOOK

- + Canada's economy continues to plod along, neither accelerating nor sliding, while waiting for the global environment to set the course for the next few quarters. Should the US slow, as we expect it to do, Canada will, too.
- + The domestic economy argues for neither rate cuts nor rate hikes, but we expect that a risk-management approach to policymaking will push the Bank of Canada into rate cuts, given the deteriorating global picture.

RISK FACTOR

- + After a brief spike, oil prices have declined. If they fall further, it will pose new downside risks to growth.

OVERVIEW

Canada remains a bastion of calm amid a sea of uncertainty. While domestic politics are unusually contentious and controversial, there has not yet been evidence that they are affecting the economy, and the comparatively narrow range of the Canadian political spectrum suggests that any impact should be minimal. As has been the case for most of the year, the primary risks to the outlook are global in nature, both in terms of global trade and in terms of the US economy specifically. Until those are resolved, Canada will continue to muddle along, with growth staying close to trend and inflation the same. It's not exciting, perhaps, but in the turbulent global waters, a patch of calm isn't a bad place to be.

Australia/New Zealand

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Australia	1.7	1.3	1.3	1.6	0.50	0.50	1.00	1.25	0.65	0.62
New Zealand	2.2	1.8	1.7	1.9	0.75	0.50	1.15	1.15	0.64	0.62

AUSTRALIA

- + Second-quarter GDP in Australia slowed to 1.4% (negative in per capita terms), the weakest since 2009. Extraordinarily strong government spending has been the only factor keeping growth in positive territory; private sector spending is going backward.
- + What happens to unemployment is critical. Despite some post-election relief, we still expect the housing downturn to have a material impact on overall growth, driving the unemployment rate back through the sixes.
- + Accordingly, the Reserve Bank of Australia should deliver more cuts, and we wouldn't be shocked to see AUD/USD rates revisiting the 0.62–0.64 range, particularly as iron ore prices continue to pull back from recent highs.

NEW ZEALAND

- + The shift to incorporate a weaker global backdrop into our forecasts, along with the continued slide in New Zealand business confidence, has driven a substantial downgrade in our New Zealand growth outlook for 2020.
- + Along with persistently lower-than-expected inflation, a policy rethink by the central bank (including a dovish 50 b.p. cut in August) has also driven a further shift lower in the policy rate outlook. We now expect the overnight cash rate to hit 0.50% in 2020.

UK

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
UK	1.0	0.3	1.9	1.7	0.50	0.25	0.35	0.50	1.23	1.23

OUTLOOK

- + Brexit continues to dominate the headlines. Prime Minister Boris Johnson has made new proposals to try to break the deadlock, but these are unlikely to prove acceptable to the European Union (EU). Johnson's fallback in this case is to leave the EU without a deal on October 31, but this has been blocked by Parliament. The overwhelming likelihood is therefore a further extension of the Brexit deadline, to be closely followed by a general election to break the impasse. The outcome of the latter will be pivotal. If the Conservative Party is returned with a workable majority, the UK will almost certainly leave the EU early next year, probably without a deal. Most other outcomes are likely to lead to a second referendum at which there's a high probability that remaining would triumph. As the result of the election is too close to call, though, we judge that the risk of a no-deal/hard Brexit is higher than the market currently anticipates.
- + Recent data have been soft, with the composite PMI slipping to 49.3 in September from 50.3 in August. Except for a temporary blip following the June 2016 Brexit referendum, that's the lowest reading since May 2009. Against this backdrop, pressure for a rate cut is likely to build.

RISK FACTOR

- + A no-deal Brexit would push the economy into recession. While highly unlikely, an early deal would give the economy a long-overdue boost.

Norway/Sweden

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Norway	2.1	1.1	2.2	1.7	1.50	1.50	1.25	1.25	10.00	10.00
Sweden	1.7	0.7	1.9	1.7	(0.25)	(0.50)	(0.30)	(0.15)	10.50	10.50

NORWAY OUTLOOK

- + Growth in the mainland economy remained resilient at 2.5% in the second quarter, much stronger than in the rest of Europe. Looking ahead, we doubt that Norway will be able to buck the global and regional trend, and so we expect growth to slow to 1.1% in 2020.
- + Core inflation (adjusted for tax changes and energy prices) remained slightly above target at 2.1% in July. Norges Bank raised its key rate to 1.50% in September. We expect that to be the last increase in the current tightening cycle.

RISK FACTORS

- + High household debt (currently 220% of income) and oil-price fluctuations are key risk factors.

SWEDEN OUTLOOK

- + Recent data have surprised significantly to the downside. The composite PMI fell to 48.8 in September from 53.5 in August, with the manufacturing component dropping to 46.3, the lowest reading since December 2012. Although Swedish data can be volatile, this is consistent with our view that growth will slow sharply over coming quarters.
- + Core inflation (consumer price index with a fixed interest rate, excluding energy) fell to 1.6% in August and has now been below Sveriges Riksbank's 2.0% target for two years. On a harmonized basis, core inflation (excluding food and energy) is running at just 1.2%.
- + The Riksbank has scaled back its projections for the key policy rate but still expects a gradual tightening over the coming year. We see little likelihood of the Riksbank delivering on this and think the next move is more likely to be down than up.

RISK FACTOR

- + High household debt and elevated house prices continue to represent a major risk to financial stability.

Asia ex Japan

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Asia ex Japan	5.4	5.3	2.4	2.4	3.93	3.69	3.47	3.39	—	—
Hong Kong	0.5	1.0	2.5	2.3	2.25	2.00	1.50	1.40	7.83	7.85
India	6.6	6.6	3.2	3.4	5.15	4.65	6.80	6.70	69.00	68.00
Indonesia	5.0	5.0	3.2	3.0	5.00	4.75	7.20	7.10	14,000	13,950
South Korea	1.8	1.5	0.9	1.1	1.00	1.00	1.35	1.35	1,250	1,300
Thailand	2.7	2.5	1.2	1.2	1.25	1.00	1.50	1.50	32.00	33.00

OUTLOOK

- + The drag from global trade, uncertainty about the technology cycle and geopolitical risks continue to weigh on growth in the more trade-exposed parts of the region.
- + With inflation low and exchange rates relatively stable, slowing growth is driving a broad-based easing in monetary policy across the region. The debate around the potential for fiscal stimulus is also picking up steam.

RISK FACTORS

- + Uncertainty over the global trade cycle and US-China trade tensions remain key.

OVERVIEW

Growth in the more trade-exposed parts of Asia—South Korea, Taiwan, Singapore, Malaysia, Thailand—has already slowed considerably over the last year and is running close to a full percentage point below trend. With trade conflict and broader geopolitical uncertainty intensifying, the outlook continues to darken.

To date, the spillover of external weakness and geopolitical shocks to domestic economies has been limited. But there are signs of that now happening. In South Korea, for example, capital spending has collapsed, and the labor market has started to weaken. Hong Kong's GDP report for 2Q was particularly weak (and we are watching developments related to the demonstrations very closely).

At the same time, inflation has been lower than expected across the region—both headline and core. Central banks have started to deliver on the easing that markets have priced in, with cuts in South Korea, Malaysia, Indonesia, India and the Philippines. We expect more easing to come, most of which is priced in. But there may be surprises in South Korea (where the Japan-Korea trade spat is supplying an additional drag), Thailand and Malaysia, as well as in the scale of adjustment in the nominal effective exchange rate slope in Singapore.

Latin America

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Latin America	0.7	2.1	9.5	6.8	12.84	9.29	6.37	6.63	—	—
Argentina	(1.3)	1.5	50.0	30.0	65.00	40.00	—	—	65.00	80.00
Brazil	0.6	2.5	3.9	4.0	4.75	5.25	7.00	7.50	4.05	3.80
Chile	2.5	3.3	2.6	2.8	1.50	1.75	2.50	2.75	730	720
Colombia	3.0	3.0	3.6	3.2	4.25	4.00	5.80	6.00	3,400	3,500
Mexico	0.4	1.0	3.2	3.5	7.25	6.50	6.80	6.75	19.50	20.25

OUTLOOK

- + Policy measures in Argentina and rhetoric from the presidential election front-runner eased concerns about a hard restructuring of external debt and helped to stabilize the currency and bond prices. However, announcements around the first round of elections to be held on October 26 will be scrutinized and will have an impact on sentiment and asset prices.
- + Major central banks in the region eased policy rates as growth expectations continued deteriorating and inflation remained in check. But expansionary fiscal policy to counter a deeper global deceleration, should one occur, would stoke fears about credit deterioration.

RISK FACTORS

- + Idiosyncratic weaknesses and political developments may keep weighing on investment and domestic consumption across the region, magnifying the worries related to a deeper global deceleration than currently expected.

OVERVIEW

The situation in Argentina stabilized in the past month after the government enacted capital controls that limited the decline in foreign exchange reserves and the currency's depreciation. Moreover, statements from front-runner candidate Alberto Fernández and his advisors decreased concerns regarding the possibility of a hard restructuring with foreign bondholders. However, both the exchange rate and bond prices still reflect uncertainty and are likely to be affected by announcements around the first round of the presidential election on October 26. A loss of confidence on the next administration's economic plan could increase hard-currency demand, put pressure on reserves and raise concerns over debt sustainability and bond prices.

The Brazilian Senate finished the first-round vote on pension reform. At this stage, lawmakers approved the base text but added an amendment that changes the rule of wage benefits, reducing expected savings to around BRL735 billion over the next 10 years, according to analysts' calculations. A second round of discussions will start soon as lawmakers try to avoid delaying final approval of the much-awaited reform. Banco Central do Brasil cut rates by another 50 b.p. in September, after a similar cut in August, and stressed weak economic growth. That left the door open to further cuts this year. We expect easy monetary conditions and improved confidence over policy changes to boost growth during the second half of the year and into 2020.

Growth concerns intensified in Mexico as consumer confidence and external demand for manufactured goods weakened in the past month. Despite the procedure to inject capital into PEMEX, coupled with a liability management operation, doubts persist over the state-owned oil company's ability to increase crude production. That means concerns about credit ratings remain elevated. In Peru, a constitutional and political crisis worsened over the last month. President Vizcarra dissolved Congress and called for legislative elections to be held in January. This followed the government's failure to change the way that the Judiciary Tribunal is elected and its call for early general elections. We don't expect the political crisis to pose a major risk to macroeconomic policy or economic fundamentals in the short term. But when combined with slower economic growth, these developments may lead to early presidential elections and a possible surge in support for populist candidates.

Eastern Europe, Middle East and Africa (EEMEA)

	Real GDP (%)		Inflation (%)		Policy Rate (%)		10-Yr. Bond Yield (%)		FX Rates vs. USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
EEMEA	1.5	2.5	7.9	7.4	7.42	6.62	8.08	7.83	—	—
Hungary	3.8	2.3	3.1	3.2	0.90	1.25	1.80	1.80	330	325
Poland	3.9	3.1	1.9	2.5	1.50	1.50	2.20	2.20	4.30	4.30
Russia	1.2	1.7	4.3	4.0	6.75	6.50	7.00	7.15	66.00	63.00
South Africa	0.5	0.9	4.2	4.6	6.25	6.00	8.95	9.10	15.70	16.00
Turkey	(1.0)	1.5	16.5	14.3	14.00	12.00	14.50	14.00	6.10	6.25

OUTLOOK

- + Real GDP growth is expected to pick up in 2020, particularly in Turkey.
- + While headline CPI is rebounding in most Central and Eastern European (CEE) economies, price pressures are expected to ease in Russia and Turkey following fading tax and exchange-rate pass-throughs. Inflation in South Africa is expected to remain close to the midpoint of the target band.
- + CEE central banks are mostly expected to remain on hold, while Russia, South Africa and Turkey have room to cut interest rates in 2019 and potentially into 2020.

RISK FACTOR

- + The potential for higher core yields is a risk for current account deficit countries such as Turkey and, to a lesser extent, South Africa.

OVERVIEW

We returned from a recent trip to Turkey with the impression that the government's focus on stimulating growth has not changed. The latest macroprudential measures (i.e., changes to remuneration and reserve requirement ratios) are designed to do what the government does best: stimulate credit growth. The government and central bank now target credit growth of 10%–20% over the coming 12 months and will penalize banks that do not comply with lower remuneration rates for TRY deposits at the central bank. Banks, including private ones, told us they will likely try to comply to avoid the penalties. Credit growth remained close to zero in August (deeply negative in real terms), and we'd have to see credit growth of 1.0% a month over the coming year to push the annual rate up to 10%–15%, or 1.5% a month to push it up to 15%–20%. Given that the five-year monthly growth rate has been 1.0%, this is an ambitious target. Should credit growth reach this target, 4%–5% real growth next year should be feasible. But it would come at the cost of additional leverage and asset-quality concerns within the banking sector.

The ongoing focus on growth also limits scope for fiscal consolidation efforts and meaningful tax reform for 2020, in our view. In its latest three-year macro plan, the government acknowledged fiscal pressures, marking its 2019 full-year nominal deficit target up to 3.0%, from 1.8% previously. Given that the deficit already amounted to 2.5% during the first eight months of the year, we believe a deficit of 3.7% of GDP is more likely. For 2020, the government forecasts that its 3.0%-of-GDP fiscal deficit will be maintained, owing mostly to the expected increase in interest expenditure (the primary balance is forecast to switch to a small 0.1%-of-GDP surplus from (0.4)% in 2019). Considering the government's ambitious growth target of 5%, we think the risks are skewed toward a higher deficit next year, and we forecast a full-year shortfall of 3.5% of GDP. Under the government's 2020 budget assumptions, external fiscal financing requirements would be about US\$10 billion next year, assuming that the government taps 50% of its roughly US\$10 billion cash reserves. Large one-off revenues, such as the US\$8.6 billion equity transfer from the central bank, will not be available next year. Under our less favorable fiscal assumptions for 2019 and 2020, next year's external fiscal funding needs could be between US\$15 billion and US\$20 billion, unless the government manages to significantly increase local-market TRY, gold and FX issuance. Against this backdrop, we believe that supply pressures, both in domestic and in external markets, will be meaningful going into 2020.

Frontier Markets

OUTLOOK

- + Zambian asset prices might not deteriorate meaningfully from current depressed levels, but their upside seems limited, as a muddle-through scenario on the political and fiscal fronts remains likely.

RISK FACTOR

- + Zambia's external financing needs could exceed its ability to source hard currency in a protracted global slowdown.

OVERVIEW

Zambia's new minister of finance, Bwalya Ng'andu, presented the 2020 budget at the end of September, just two months after taking the reins. Ng'andu committed to creating fiscal space, ensuring debt sustainability and dismantling domestic arrears. The budget deficit for 2019 seems to be broadly on target (6.5% of GDP) and the plan is to reduce the deficit to 5.5% of GDP in 2020. Total public and publicly-guaranteed debt was, however, already close to 80% of GDP by the end of 2018, and debt is still rising. External debt (which is financing the government's ambitious infrastructure drive) represents a growing share of the budget. Although the absolute economic growth dividend from these externally financed investments remains ambiguous, the deceleration in GDP growth suggests diminishing returns. The drought has certainly exposed some of Zambia's macro vulnerabilities, but policy uncertainty (for mines in particular) is and will possibly remain a binding constraint for economic growth. The budget announcement that the value-added tax will be retained (the previously proposed sales tax has been scrapped) and the proposal of zero-rating capital equipment and machinery for the mining sector were positives, but broader tax and policy uncertainty continues to undermine investor confidence. We suspect that President Lungu gave the minister of finance some leeway to regain policy credibility. There have certainly been more references to IMF interactions since Ng'andu took over, but we are not convinced that it will lead to a funded program in the foreseeable future. Zambian asset prices might not deteriorate meaningfully from current depressed levels, but upside price movements seem unlikely, as a muddle-through on the political and fiscal fronts remains the most likely scenario, in our view.

	Real Growth (%)		Inflation (%)		Official Rates (%)		Long Rates (%)		FX Rates vs USD	
	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F	2019F	2020F
Global	2.5	2.3	2.9	2.7	2.53	2.06	2.11	2.15	-	-
Industrial Countries	1.6	0.9	1.7	1.7	0.55	0.31	0.73	0.79	-	-
Emerging Countries	4.2	4.6	4.9	4.3	6.32	5.34	4.82	4.73	-	-
United States	2.0	1.5	2.3	2.3	1.38	0.88	1.75	1.75	-	-
Canada	1.8	1.5	2.1	2.1	1.50	1.00	1.50	1.50	1.30	1.35
Europe	1.2	0.4	1.3	1.2	(0.40)	(0.45)	(0.40)	(0.26)	-	-
Euro Area	1.1	0.3	1.2	1.1	(0.70)	(0.70)	(0.65)	(0.50)	1.13	1.13
United Kingdom	1.0	0.3	1.9	1.7	0.50	0.25	0.35	0.50	1.23	1.23
Sweden	1.7	0.7	1.9	1.7	(0.25)	(0.50)	(0.30)	(0.15)	10.50	10.50
Norway	2.1	1.1	2.2	1.7	1.50	1.50	1.25	1.25	10.00	10.00
Japan	1.1	(0.4)	0.8	0.9	(0.10)	(0.15)	(0.20)	(0.20)	102	95
Australia	1.7	1.3	1.3	1.6	0.50	0.50	1.00	1.25	0.65	0.62
New Zealand	2.2	1.8	1.7	1.9	0.75	0.50	1.15	1.15	0.64	0.62
Asia ex Japan	5.4	5.3	2.4	2.4	3.93	3.69	3.47	3.39	-	-
China	6.2	6.0	2.5	2.4	4.35	4.10	3.00	2.90	7.20	7.20
Hong Kong	0.5	1.0	2.5	2.3	2.25	2.00	1.50	1.40	7.83	7.85
India	6.6	6.6	3.2	3.4	5.15	4.65	6.80	6.70	69.00	68.00
Indonesia	5.0	5.0	3.2	3.0	5.00	4.75	7.20	7.10	14,000	13,950
Korea	1.8	1.5	0.9	1.1	1.00	1.00	1.35	1.35	1,250	1,300
Thailand	2.7	2.5	1.2	1.2	1.25	1.00	1.50	1.50	32.00	33.00
Latin America	0.7	2.1	9.5	6.8	12.84	9.29	6.37	6.63	-	-
Argentina	(1.3)	1.5	50.0	30.0	65.00	40.00	-	-	65.00	80.00
Brazil	0.6	2.5	3.9	4.0	4.75	5.25	7.00	7.50	4.05	3.80
Chile	2.5	3.3	2.6	2.8	1.50	1.75	2.50	2.75	730	720
Colombia	3.0	3.0	3.6	3.2	4.25	4.00	5.80	6.00	3,400	3,500
Mexico	0.4	1.0	3.2	3.5	7.25	6.50	6.80	6.75	19.50	20.25
EEMEA	1.5	2.5	7.9	7.4	7.42	6.62	8.08	7.83	-	-
Hungary	3.8	2.3	3.1	3.2	0.90	1.25	1.80	1.80	330	325
Poland	3.9	3.1	1.9	2.5	1.50	1.50	2.20	2.20	4.30	4.30
Russia	1.2	1.7	4.3	4.0	6.75	6.50	7.00	7.15	66.00	63.00
South Africa	0.5	0.9	4.2	4.6	6.25	6.00	8.95	9.10	15.70	16.00
Turkey	(1.0)	1.5	16.5	14.3	14.00	12.00	14.50	14.00	6.10	6.25

Long rates are 10-year yields unless otherwise indicated.

Latin American Rates include Brazil, Chile, Colombia and Mexico

Real growth aggregates represent 48 country forecasts not all of which are shown

Blanks in Argentina are due to distorted domestic financial system so are not forecast.

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