December 09, 2016

Economics Group

Special Commentary

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Global Chartbook: December 2016

Executive Summary

Our forecast of 2.9 percent for 2016 global GDP growth is unchanged since the prior publication of our Global Chartbook in September. If realized, a 2.9 percent figure would mark the weakest full-year growth rate since the global recession of 2009. Even though we do not anticipate the world economy suddenly taking off, we expect to see slightly faster global GDP growth in 2017 and again in 2018, which suggests that 2016 could well mark the low point of the post-recession years in this cycle.

Figure 1

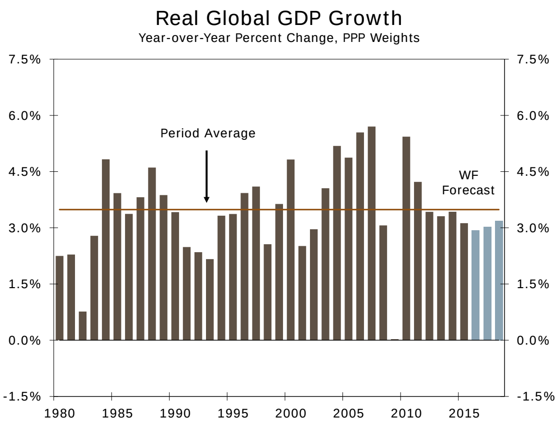
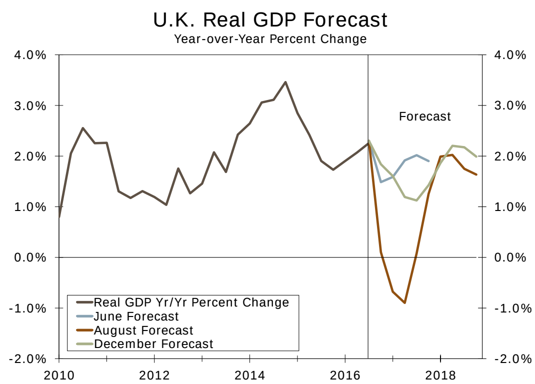


Figure 2



Source: IHS Global Insight and Wells Fargo Securities

Perhaps the most consequential revision we have made to our individual country forecasts is to reconsider our recession call for the United Kingdom. When British voters decided to leave the European Union (EU) in a referendum at the end of June, it seemed to us that a modest recession was in the cards. The economies of the United Kingdom and the other 27 members of the EU are extensively intertwined. Given the uncertainty of the unwinding process, we thought it reasonable in the immediate aftermath of the referendum that some businesses would put off at least some of their capex plans until greater clarity emerged.

Five months later, there are few indications of an imminent recession in the United Kingdom. Consequently, we have bowed to the reality of the incoming economic data and have removed recession from our British economic outlook. We still look for investment to weaken somewhat in the next few quarters, but a sharp enough downturn in capital spending to pull the entire economy into recession is looking increasingly unlikely. We currently forecast that real GDP in the United Kingdom will grow 1.3 percent in 2017 and 2.1 percent in 2018. Figure 2 shows the evolution of our forecasts of year-over-year changes in real GDP in the United Kingdom over the past few months.

Contents.........Page

Together we'll go far

The U.K. referendum was an instance of a poll data not offering a reliable gauge of actual voting and the surprising appeal of an anti-globalization message that resonated with voters in a way that was not fully appreciated until the election results were known. That also happens to be an accurate description of the U.S. presidential contest as well.

Donald Trump's surprising presidential election win means that the probability distribution of potential outcomes for the U.S. economy is now greater than it would have been in a Clinton presidency, which was the conventional baseline expectation heading into the election. In October, our full-year GDP forecast was 2.2 percent for 2017 and 2.2 percent for 2018. Post-election, those figures are unchanged. The big impact from the election is less about the actual projected growth rate and more about the increased variability of potential outcomes given the increased policy uncertainty.

Figure 3

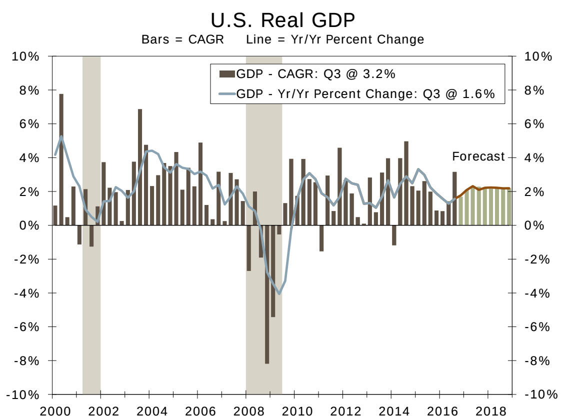
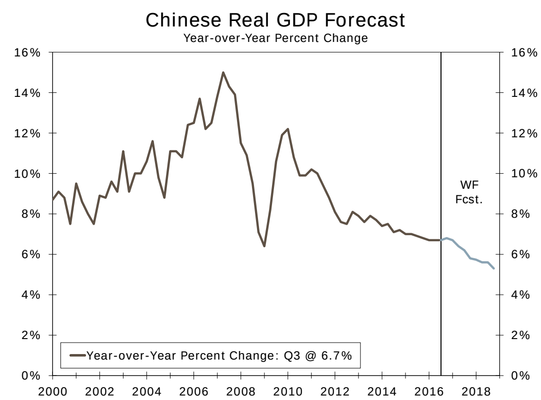


Figure 4



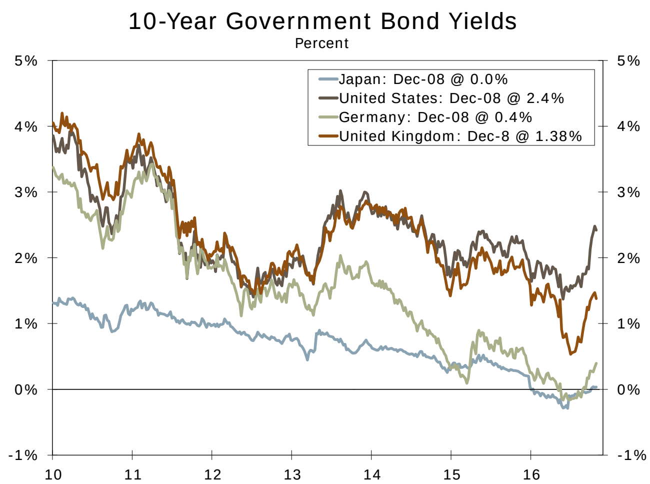
Source: U.S. Department of Commerce, IHS Global Insight and Wells Fargo Securities

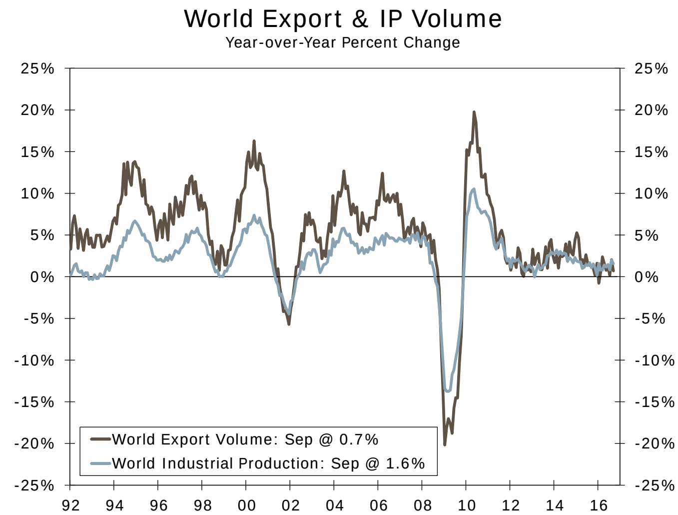
We still anticipate moderation in the growth rate for the Chinese economy, although we now have less of a slowdown in our Chinese economic forecast for 2017 and 2018 relative to the September Chartbook. This is partly due to a boom in residential investment. Lending standards have been relaxed somewhat and the People's Bank of China had guided lending rates lower, both of which have been supportive of residential investment.

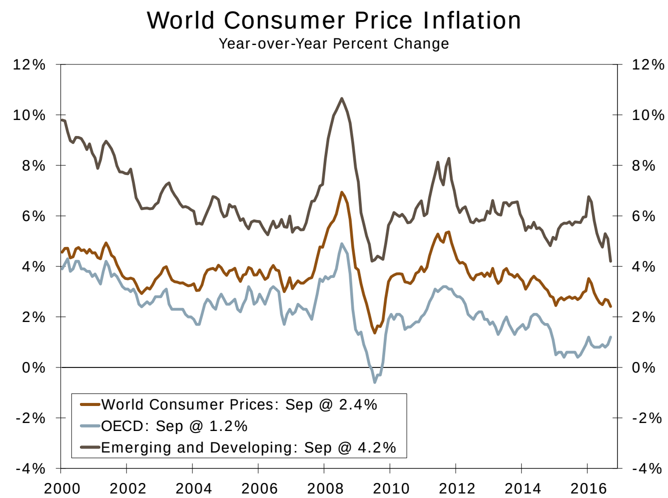
Despite the modest upgrade to the forecast for China, elsewhere our developing economies forecast for the next couple of years is a bit lower. This is largely due to downgrades for Mexico and Brazil, two economies which could be vulnerable to a protectionist U.S. trade agenda, a risk that has become more likely as a result of the U.S. election.

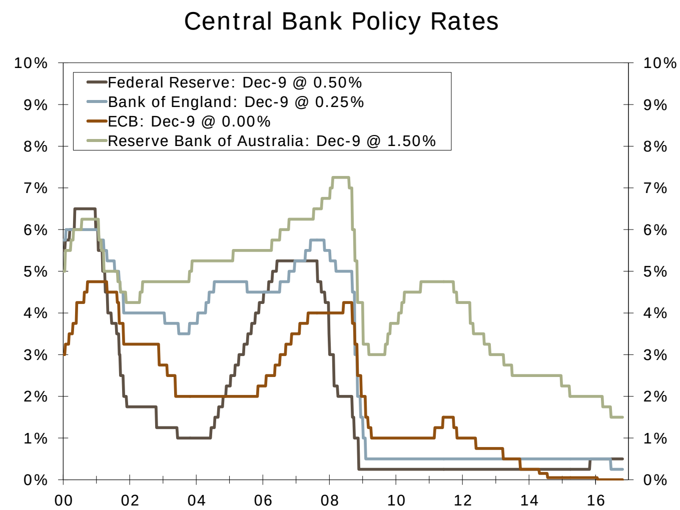
World

- Global industrial production (IP) growth showed some strength in the back half of Q3. IP growth averaged 1.8 percent (year-over-year) in September and October, the highest consecutive monthly average since early 2015. September's rate of 2.0 percent is the first two-percent rate notched since late 2014. Lackluster, global trade, however, remains a concern.
- Although the collapse in commodity prices contributed to the downturn in export values, growth in trade volumes has been weak recently. Global trade volumes were more or less flat on a year-ago basis in the June-August period. The lack of any blockbuster trade deals in recent years as well as the apparent topping out in the process of globalization appears to have depressed trade growth.
- While the recent spike in bond yields was in response to partially allayed deflationary concerns, central banks in both developing and advanced economies remain generally dovish. Negative rates are the norm for several European central banks as well as for the Bank of Japan.
- We expect global GDP to grow at 2.9 percent followed by growth rates of 3.0 percent and 3.2 percent in 2017 and 2018, respectively. While these rates are below the long-run average of 3.5 percent, the upward growth trajectory we look for in the coming years is encouraging. Moreover, we expect global CPI to close 2016 at 3.1 percent before increasing 3.4 percent and 3.6 percent in 2017 and 2018, respectively.





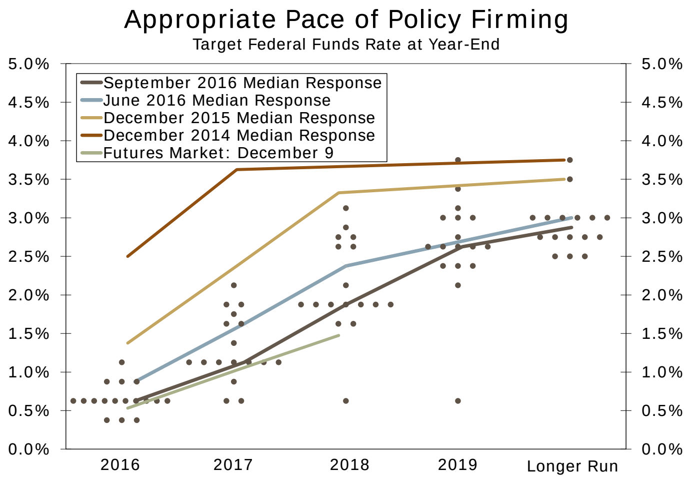


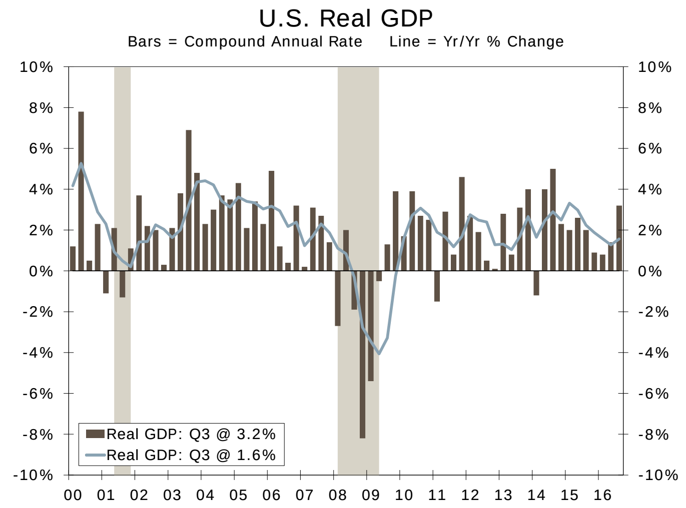


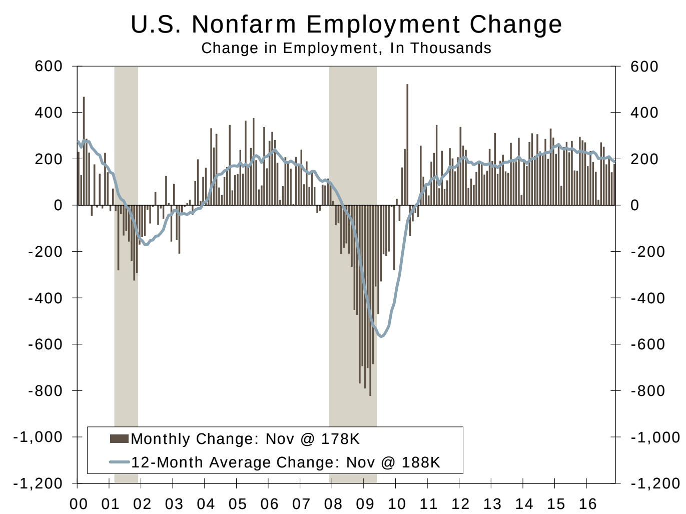
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

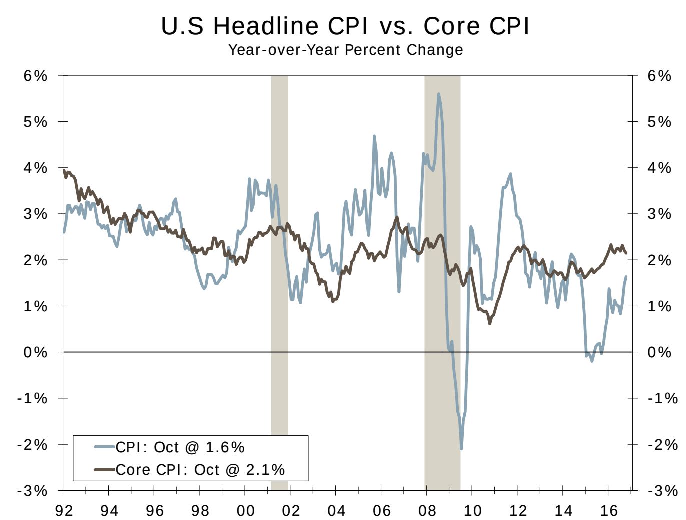
United States

- Third quarter U.S. economic growth accelerated to an annualized pace of 3.2 percent, marking the fastest quarterly pace of GDP growth since Q3 2014. Robust consumer spending, greater business investment and net exports all supported growth for the quarter. Real final sales to private domestic purchases, however, slowed during the quarter, which suggest some remaining underlying softness despite the strong Q2 reading.
- On the labor market front, monthly job gains have now averaged 180,000 year-to-date and 178,000 over the past three months. November's unemployment rate declined to 4.6 percent as more workers left the labor force than joined. On balance, the unemployment rate is well within the Fed's long-run range of full employment and indicates that the labor market is tightening, which should further encourage wage growth.
- Inflation has ticked up recently, boosted by rising energy and shelter costs. October's consumer price inflation reached 1.6 percent year over year and is trekking toward the Fed's 2 percent target, while core inflation continues to hover within that range but has softened in recent months.
- The recent firming in oil and other commodity prices paired with the stronger Q3 GDP growth and steady employment gains suggests the Fed is still on track to raise rates at its December meeting.





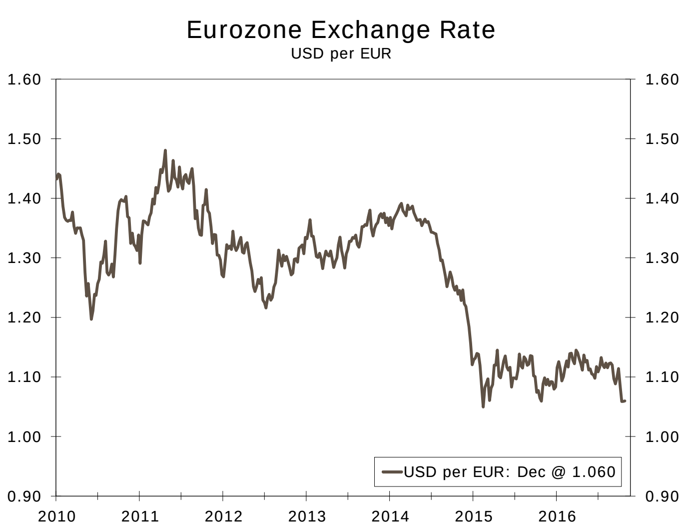


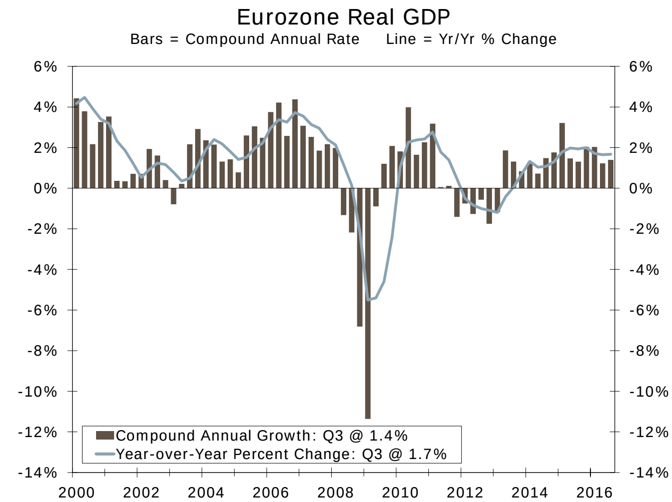


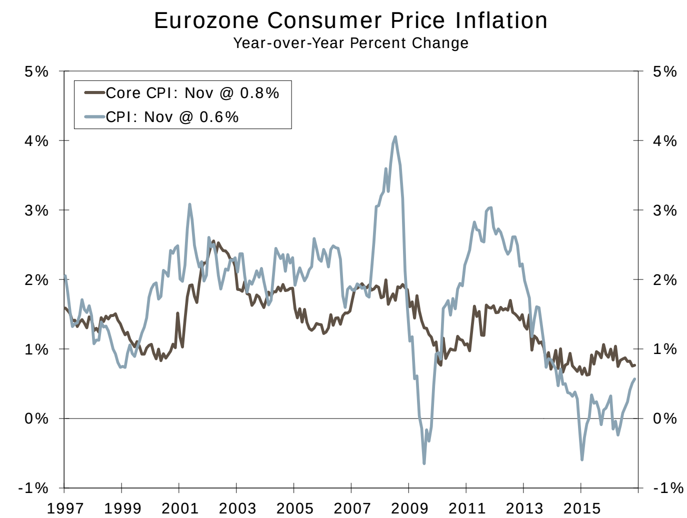
Source: U.S. Depts. of Labor and Commerce, Bloomberg LP, Federal Reserve Board and Wells Fargo Securities

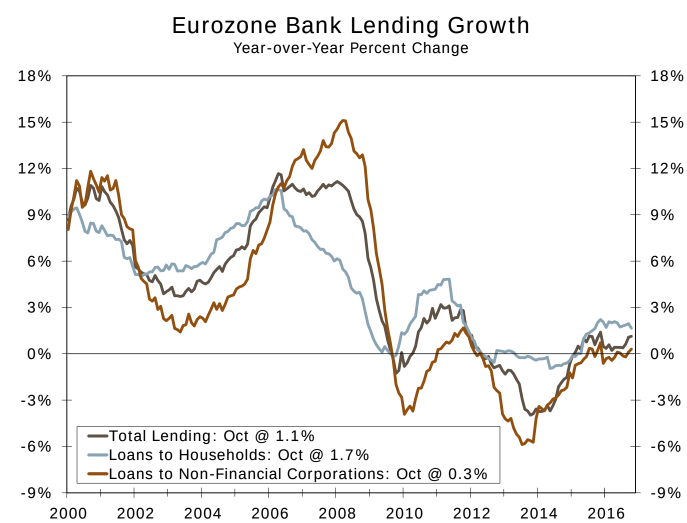
Eurozone

- GDP in the Eurozone rose 0.3 percent (1.4 percent at an annualized rate) in Q3, relative to the previous quarter. On a year-ago basis, real GDP was up 1.7 percent, unchanged from the previous quarter. Household spending ticked up 0.3 percent on the quarter while government spending grew 0.5 percent. Business fixed investment was muted, expanding only 0.2 percent from Q2.
- Inflation seems to be edging up, albeit at a slow pace. The year-over-year measure of the CPI index has increased for seven consecutive months with November's figure at 0.6 percent, well below the ECB's two percent target. The core CPI inflation rate, which excludes food and energy prices, remains depressed below 1 percent. Likewise, the producer price index (excluding energy) is in negative territory on a year-ago basis, suggesting that there really are no inflationary pressures in the Eurozone, at present.
- The European Central Bank (ECB) extended its quantitative easing (QE) program on Thursday (12/8/2016) to December 2017 from its original end date of March 2017. The ECB will slow down the purchasing program in April 2017 to a monthly rate of 60 billion euros from 80 billion euros. Policy makers kept the main refinancing rate at zero, the deposit rate at minus 0.4 percent and the marginal lending rate at 0.25 percent.





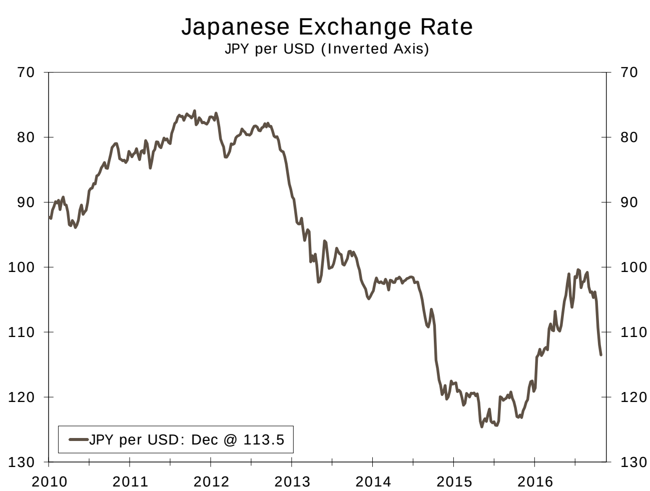


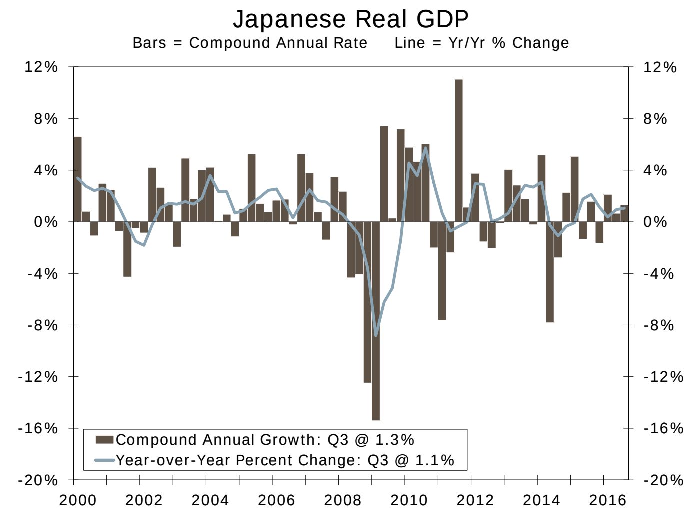


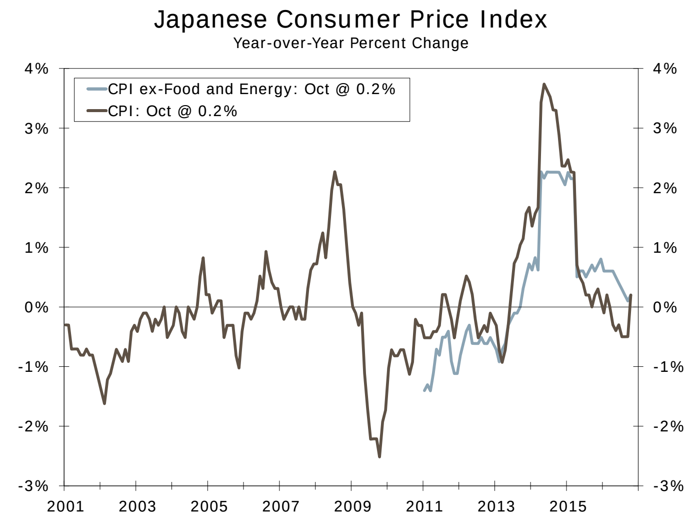
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

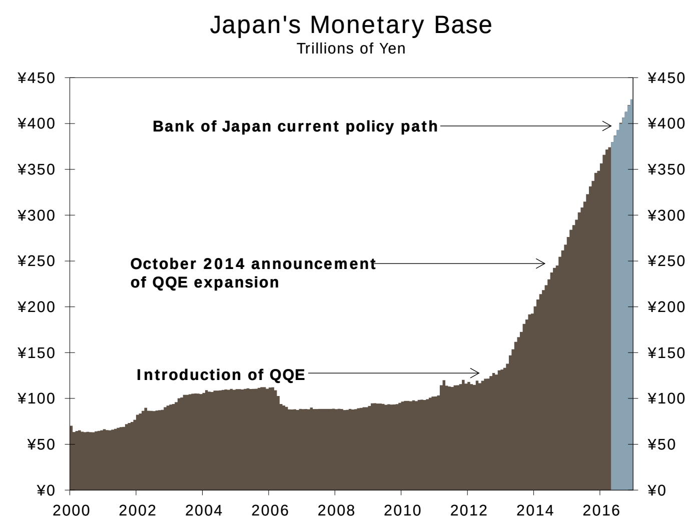
Japan

- Fueled by a boost from trade, third-quarter real GDP growth in Japan expanded at a downwardly revised annualized rate of 1.3 percent, relative to the previous quarter. However, the demand-side components of the economy were less impressive. Growth was driven mostly by net exports as imports were weak, held back by soft domestic demand in Q3. In addition, bad weather and typhoons may have played a role contributing to some of the lackluster consumer spending seen in the quarter.
- The Bank of Japan (BoJ) maintained its current monetary policy at its last meeting in November, but switched focus targeting its 10-year sovereign bond (the Japanese government bond) and promising to overshoot its inflation target of 2.0 percent. The pledge to overshoot the inflation target may prove difficult given the challenges already present, specifically muted growth and negative interest rates. Our forecast reflects that. We expect inflation to remain below target at 0.9 percent in 2017 and just 0.7 percent in 2018.
- As long as the global economy continues to expand, GDP growth should remain positive in Japan. The top challenge for Japan is the much needed structural changes. Without a greater commitment to their implementation, weak domestic demand will weigh on overall GDP growth. Until we see that structural reform, we expect Japan's economy to continue to plod along at a pace of about 1 percent for the next two years.









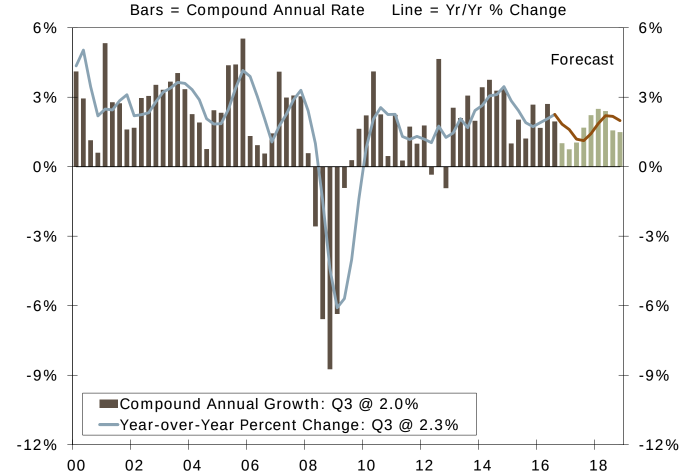
Source: IHS Global Insight, Bloomberg LP, Bank of Japan and Wells Fargo Securities

United Kingdom

- In the aftermath of the U.K.'s decision to leave the European Union, the incoming data seemed to support our initial forecast of an impending British recession. However, recent data, such as the manufacturing and service sector PMIs, have bounced back and signal strength; economic activity remains resilient. GDP grew at a sequential rate of 0.5 percent (not annualized) in Q3. Business fixed investment was especially strong during the quarter and has shown few signs of deceleration.
- Other sectors of the domestic economy have shown signs of robustness in the wake of the Brexit vote. Manufacturing production is flat on balance relative to June and real retail spending has actually accelerated in the months since the referendum. We expect some slowing in the economy in coming quarters as we still look for investment spending to weaken, especially as the invocation of Article 50 of the EU treaty draws nearer. However, we no longer believe that any downturn in capital spending that occurs in coming quarters will be severe enough to drag the entire economy down with it.
- In our view, the Monetary Policy Committee (MPC) will keep its main policy rate unchanged at 0.25 percent through 2017 before beginning a slow pace of tightening in mid-2018. Our currency strategy team looks for the British pound to depreciate modestly vis-à-vis the U.S. dollar in 2017 as the MPC remains on hold while the Federal Reserve slowly lifts rates.

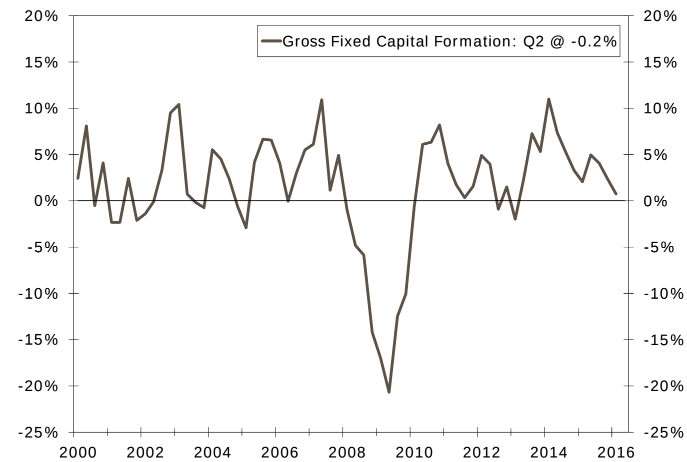
U.K. Real GDP

Bars = Compound Annual Rate Line = Yr/Yr % Change



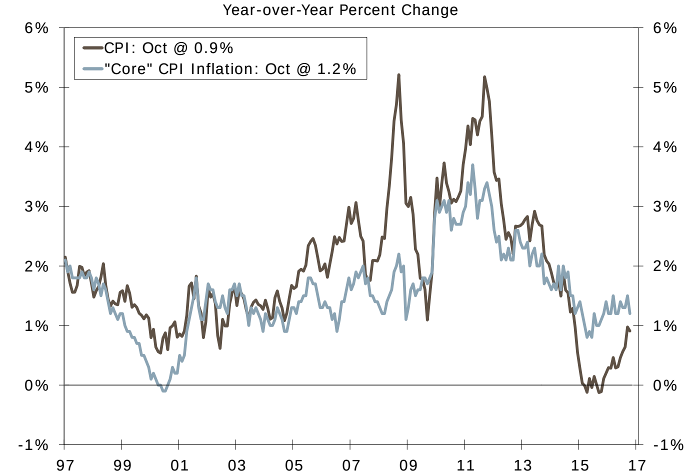
U.K. Real Gross Fixed Capital Formation

Year-over-Year Percent Change



U.K. CPI and "Core" CPI

Year-over-Year Percent Change



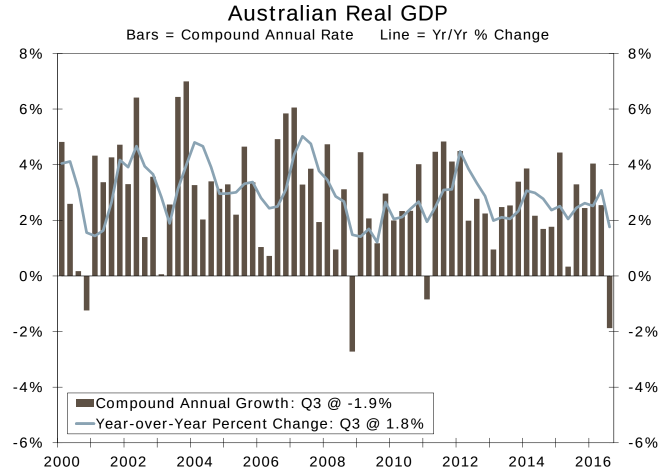
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

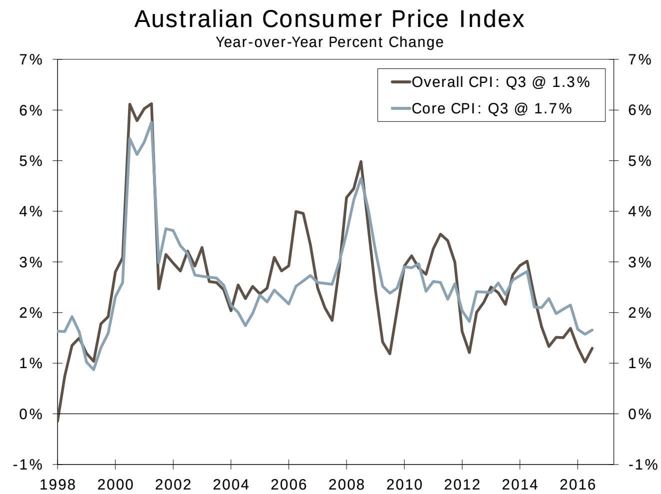
U.K. Exchange Rate

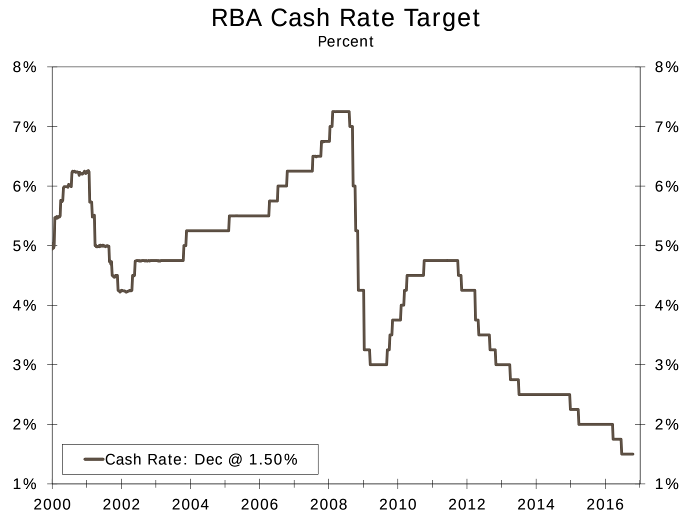
USD per GBP

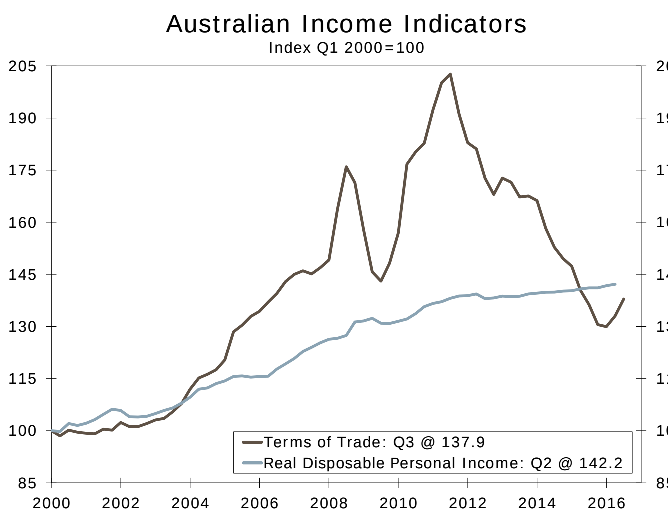
Australia

- The Australian economy contracted at a quarterly rate of 0.5 percent in Q3. It was a larger decline than was expected and it marks the first quarterly decline in more than five years. Year over year, growth slowed to 1.8 percent. Australia's streak of 25 years without a back-to-back quarterly decline in GDP (one guideline for a recession) remains intact for now. Pullbacks in spending and investments by consumers, business and the government as well as a decline in net exports detracted from quarterly growth.
- Employment in Australia particularly full-time employment, remains under pressure but is showing some improvement after declining for much of Q3. The unemployment rate now hovers at 5.6 percent but underemployment remains a concern. It will take time for all of the full-time jobs lost this year to be recovered. Moreover, the rise in full-time employment was met with modest gains in wage growth in Q3.
- As expected, the Reserve Bank of Australia opted to keep its target cash rate unchanged at 1.50 percent at its most recent meeting but acknowledged the slowdown in economic growth, viewing it as temporary, and plans to monitor the labor market closely. The recent weak print for GDP puts further rate cuts back in play for 2017.
- We do not expect Australia to spiral into a recession, although the weakness in China and still modest growth in the global economy will weigh on growth. The Aussie economy will need to see a meaningful increase in spending, investing and employment, if the country is to continue its recession-free streak.





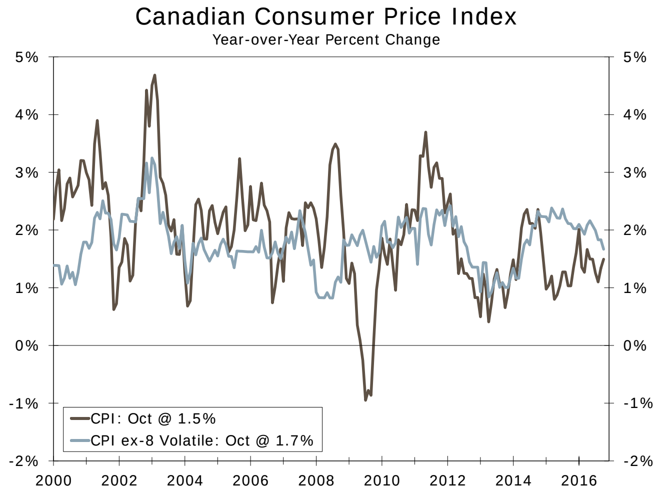


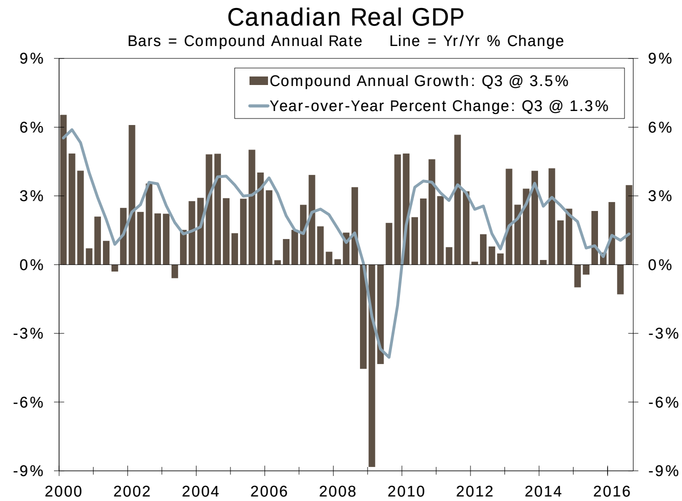


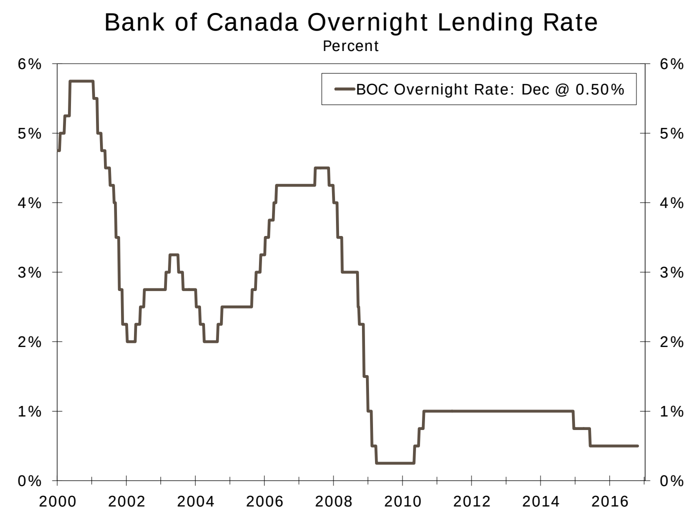
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

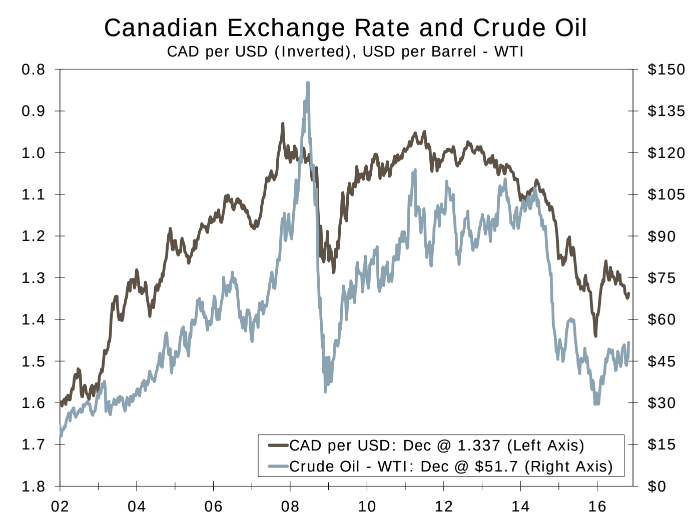
Canada

- The Canadian economy grew by a better-than-expected 3.5 percent annualized pace in the Q3 as a bounce-back in exports and increases in consumer spending helped boost economic activity. The bounce-back in exports, after wildfires in Alberta temporarily disrupted oil production in Q2, was a sizeable contributor to growth in Q3. The resumed oil production in Alberta was a welcome development, but the Canadian economy is still absorbing the impact of oil prices that remain low relative to a few years ago. Business investment, which has declined for eight consecutive quarters, was a drag on growth again in Q3 but is also showing signs of bottoming.
- The Bank of Canada (BoC) maintains a somewhat brighter tone in its latest policy report, but it did downwardly revise its forecast of GDP growth to 2.0 percent in 2017 and 2.1 percent in 2018. The BoC also renewed its inflation target agenda for five more years. We expect the BoC to remain on hold at least through the middle of next year as the output gap (difference between actual GDP and potential GDP) remains negative and the US Federal Reserve expected increase in rates weighs on the Canadian dollar.
- That said, we do not believe that 3.5 percent is a sustainable rate of growth for Canada at present. An over-levered consumer, a frothy housing market, a shifting labor market and lackluster business investments lead us to believe that growth will be closer to 2.0 percent in 2017 and 2018.







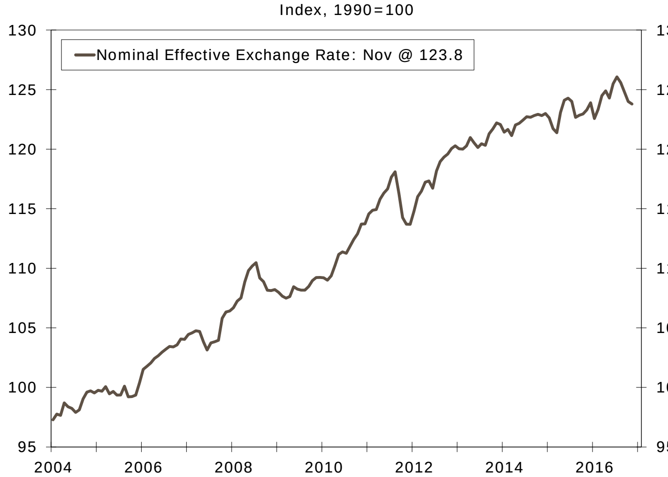


Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

Singapore

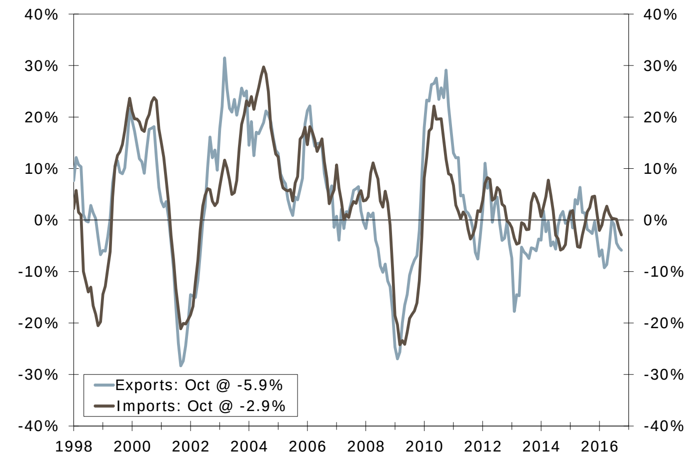
- Output in Singapore contracted 2.0 percent on a sequential basis (annualized) in the third quarter, missing the initial consensus expectation which called for a flat reading. Because Singapore is a small, open economy, its sequential rate of growth can be quite volatile. Thus, we tend to focus on the year-over-year growth rate which tends to smooth out the trends. Real GDP grew 1.1 percent on a year-ago basis, its slowest rate since Q2-2009. The manufacturing sector has returned to acting as a drag on overall GDP growth, declining 9.1 percent at an annualized rate in the third quarter. Likewise, the finance and insurance sector declined 4.7 percent quarter over quarter and is now 0.7 percent lower from a year-ago.
- Inflationary pressures in Singapore remain largely absent, which is not much of a surprise given the broad-based weakness in economic growth. Inflation, as measured by the CPI, is in negative territory on a year-over-year basis, and has been so since Nov. 2014. The core rate of inflation, which is reflective of underlying price pressures in the economy, is higher. But at only 1.1 percent, an inflationary breakout is doubtful in the near future. Because of the open nature of Singapore's economy, along with the importance of trade, the Monetary Authority of Singapore (MAS) in primarily concerned with the nation's exchange rate. Given the weakness in the economy and lack of inflation, the MAS will not likely sanction a stronger exchange rate anytime soon.

Singapore Nominal Effective Exchange Rate
Index, 1990=100

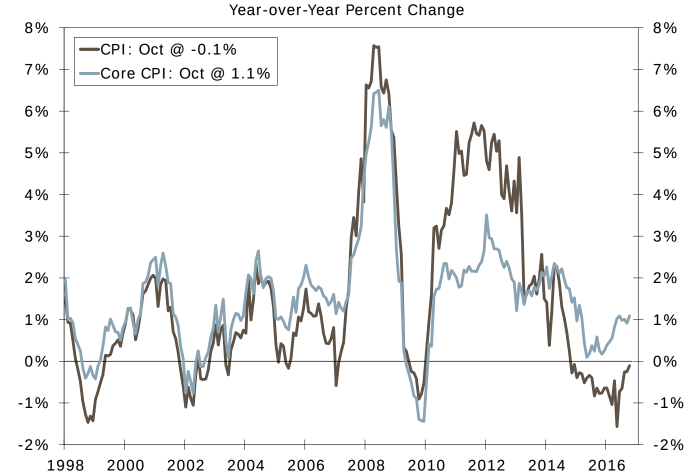


Singapore Real Output by Sector
Year-over-Year Percent Change

Singapore Non-Petroleum Trade
3-Month Moving Average, Year-over-Year Percent Change



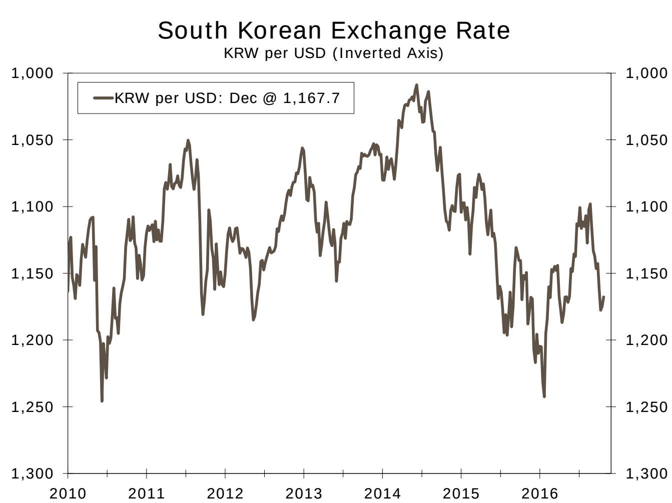
Singapore Consumer Price Index
Year-over-Year Percent Change

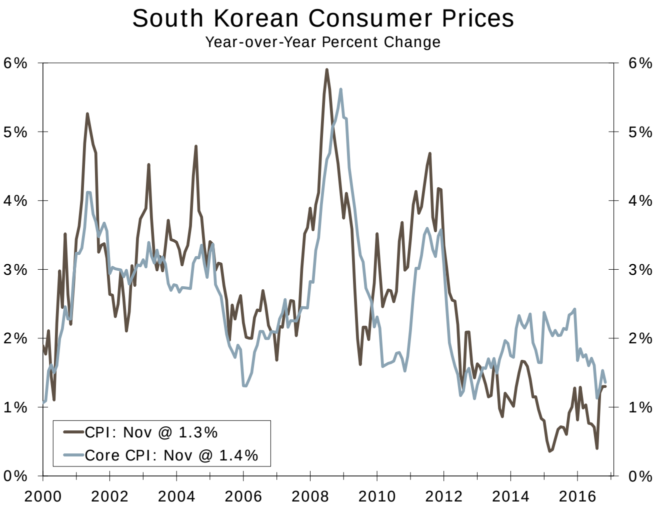


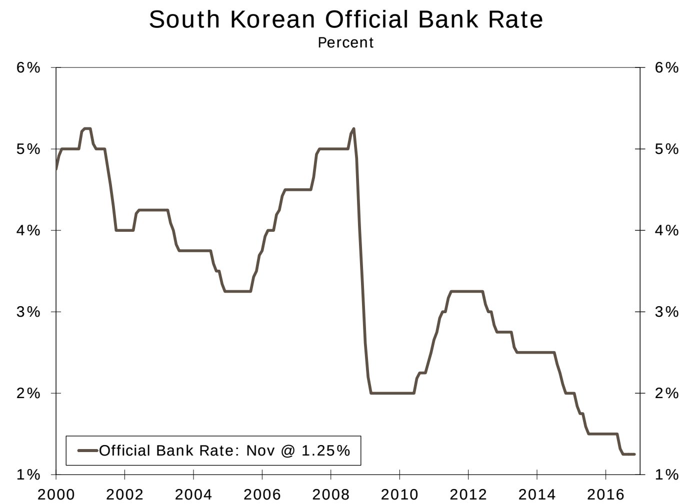
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

South Korea

- Economic growth in South Korea slowed a bit in Q3, growing by a lackluster 0.7 percent on a sequential basis, down from 0.8 percent in Q2. On a year-over-year basis, Korea economy grew by 2.6 percent. The slowing in global trade has been reflected in a drag from net exports in eight out of the past nine quarters. This was true in Q3 as well as net exports exerted a 3.1 percentage point decline on growth.
- Exports, which have traditionally been a major source of growth, have seen a decline since early last year as the Korean economy has been beset by the slowing in global trade. That said, exports have started to increase in recent months as global growth is expected to begin to pick up.
- Korean consumers have been the driver of economic growth but concerns about the sustainability of this trend are starting to arise as retail sales slow, an aging population and an increasing household debt-to-GDP ratio (85 percent) could weigh on future growth.
- At its most recent meeting, the Bank of Korea (BoK) kept its target lending rate unchanged—at a record low level of 1.25 percent. Heightened political uncertainty surrounding Korea's president and worries about trade restrictions, stemming from a Trump presidency, are complicating policy decisions for the BoK. Inflation in Korea has also picked up, helped by firming oil prices, but is still below the BoK's target range of 2.0 percent. However, if more structural reforms are not put in place the effect of the rate cuts will continue to diminish.



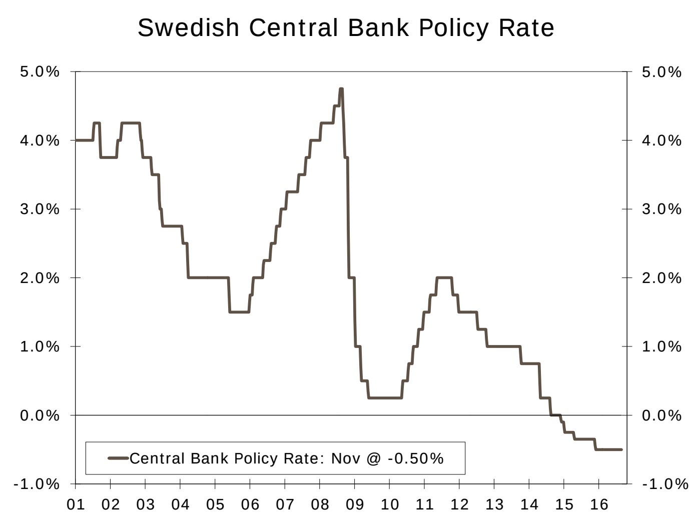


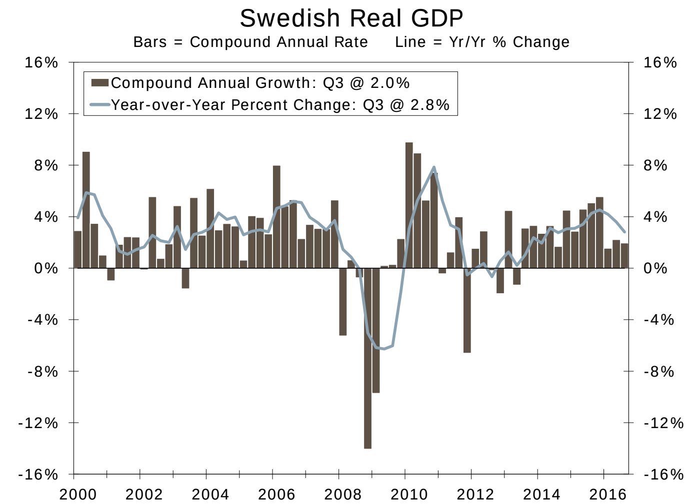


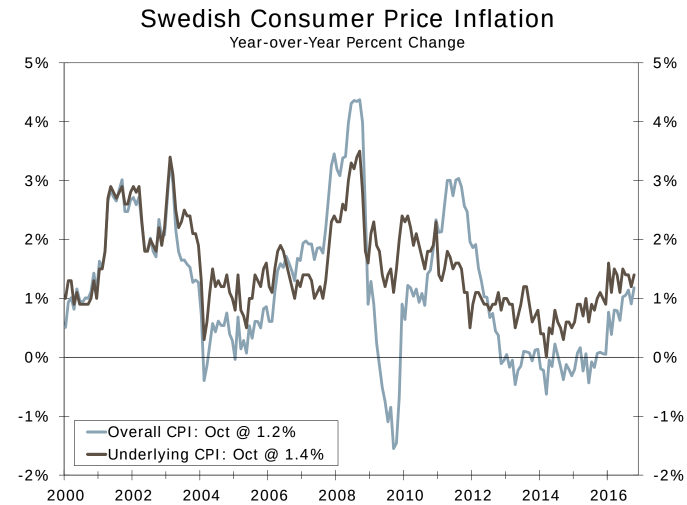
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

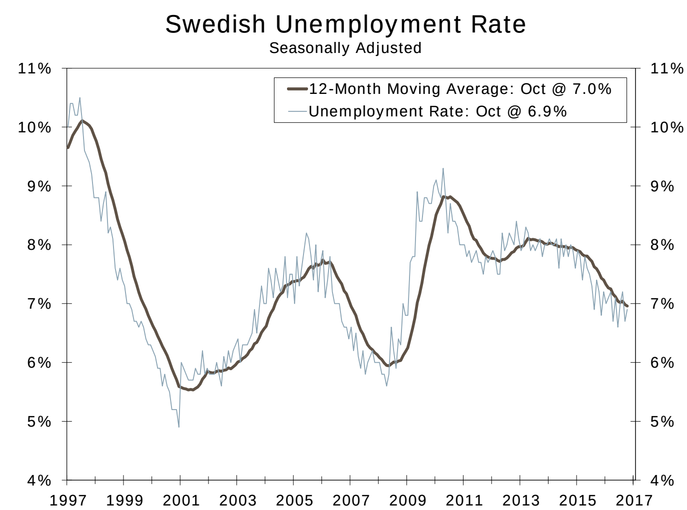
Sweden

- Output grew at a 2.0 annualized rate in Q3, and expanded 2.8 percent year over year, slightly below the expected 3.1 percent growth rate. Despite the relatively strong headline number, when compared to Sweden's European counterparts, the underlying GDP components reveal a deceleration in total domestic demand. Fixed investment spending was flat on the quarter, its first non-positive reading since Q4 2013. Likewise, government spending increased just 0.1 percent on an annualized basis, the slowest rate of growth since Q1 2011. Private consumption, on the other hand, increased 1.7 percent (annualized) in Q3, but was well short of the 3 percent growth rates that were not uncommon throughout 2015. Total domestic demand, usually a driver of GDP growth, contributed just 0.6 percentage point to the topline annualized growth figure of 2.0 percent.
- Overall CPI in October stood at 1.2 percent and has been slowly edging up since late 2015, a result that can partially be attributed to relieved downward pressure on energy prices. Although we do not explicitly forecast Swedish central bank policy moves, we believe the Riksbank will keep rates negative for the foreseeable future. Moreover, with rates expected to rise in the U.S. in the near term, our currency strategy team expects the Swedish krona to remain under downward pressure going forward. This depreciation should help to support overall GDP growth with continued growth in Swedish exports.





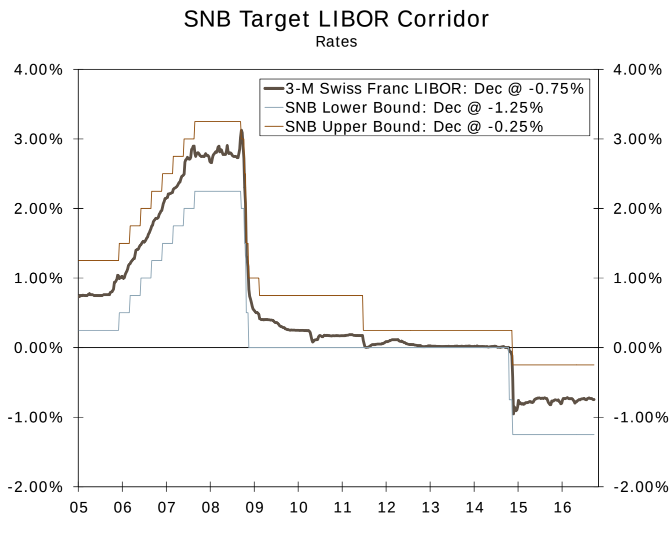


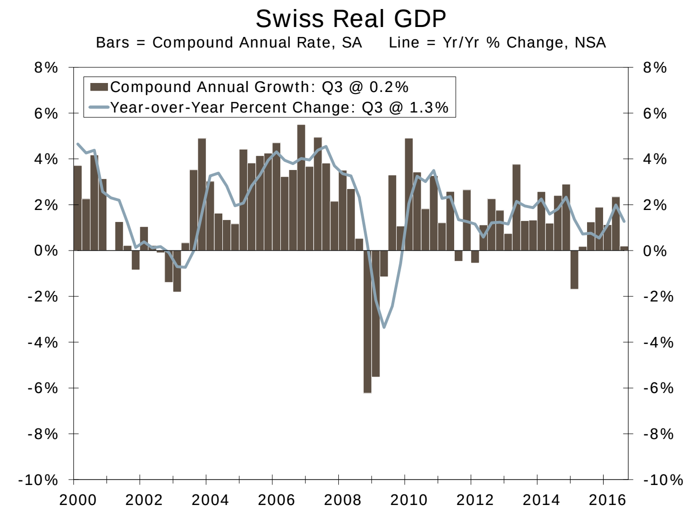


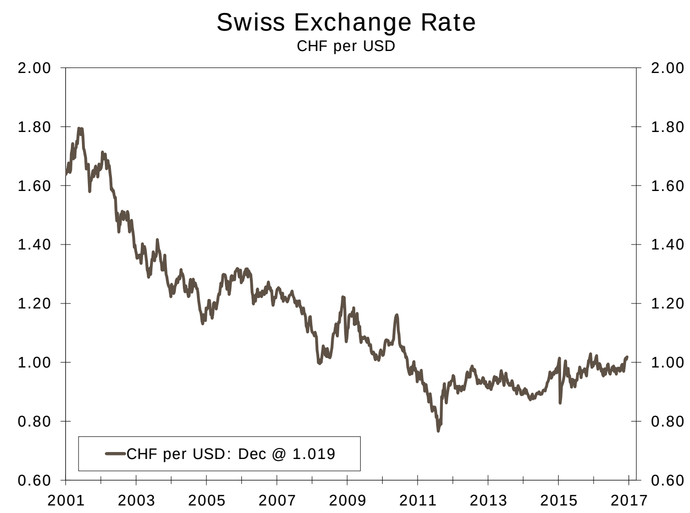
Source: IHS Global Insight and Wells Fargo Securities

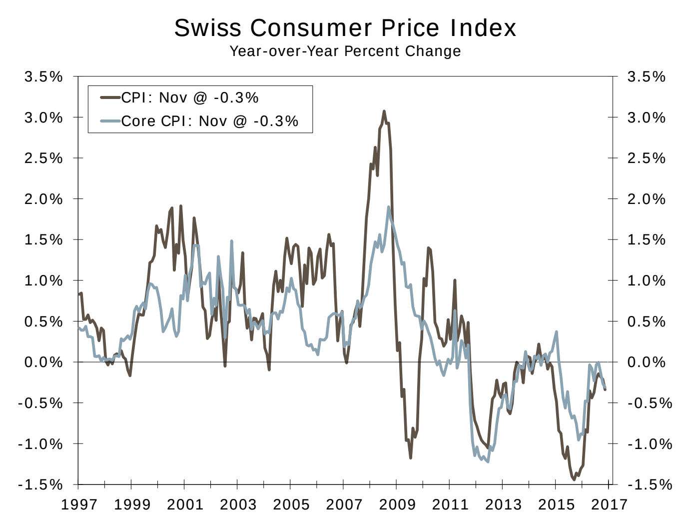
Switzerland

- Swiss Q3 GDP data revealed that output was flat on a quarterly basis. On a year-over-year basis, GDP increased only 1.3 percent, well below the market forecast of 1.8 percent. A breakdown of Swiss output into its underlying demand components shows broad-based weakness in the third quarter.
- Despite the general weakness across the GDP components in Q3, sustained economic stagnation in the Swiss economy does not seem likely. Switzerland's purchasing managers' index (PMI) has increased in five consecutive months, suggesting that we should see output firm in Q4. November's print of 56.6 jumped nearly two full points from the October figure and is the highest reading since February 2014.
- Consumer price inflation in Switzerland has been in negative territory for over two years. This should not come as a surprise against the backdrop of lackluster domestic demand. Moreover, the continued strength of the Swiss franc has served as an inflationary headwind, weighing on export growth no doubt. The Swiss National Bank (SNB) has cut its policy rate into negative territory and remains dovish, indicating scope for future easing. Policy makers have demonstrated their willingness to intervene in currency markets in order to reign in the strength of the franc, which has appreciated 10 percent versus the euro since early 2014. Our currency strategy team expects the Swiss franc to decline against the greenback as the Federal Reserve likely resumes its tightening in 2016 and through 2017.





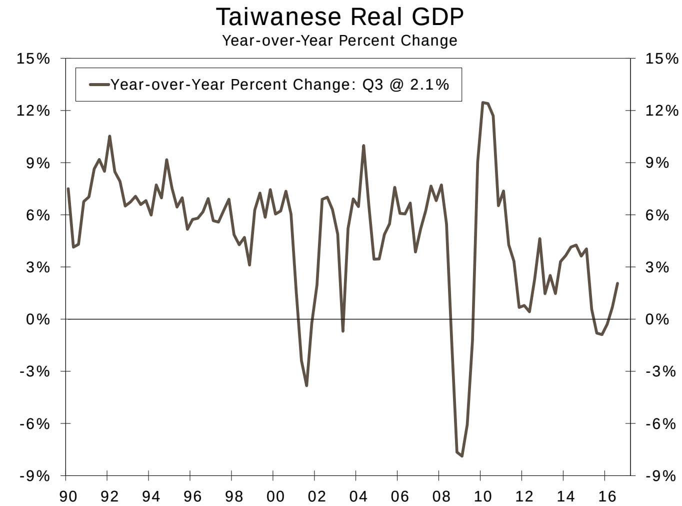


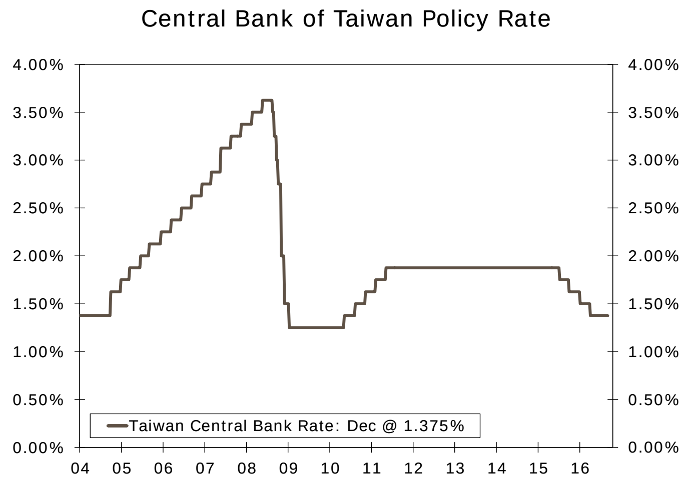


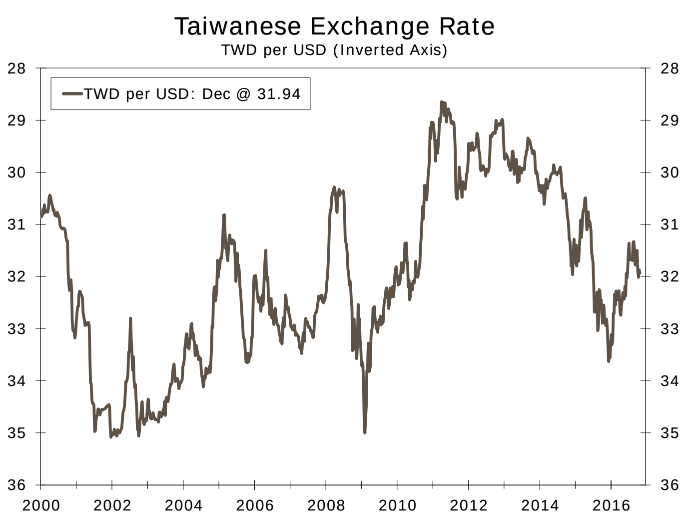
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

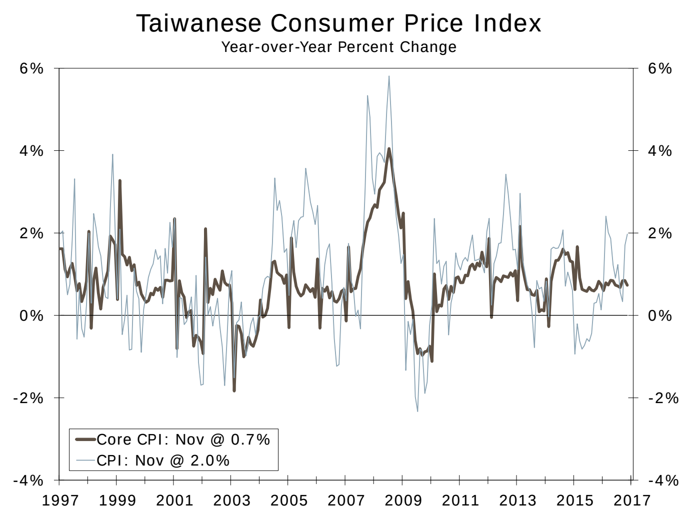
Taiwan

- Real GDP in Taiwan grew 2.1 percent on a year-ago basis in Q3 2016, which exceeded the consensus forecast that called for 1.8 percent. All components of final domestic demand strengthened on the quarter, supporting the headline number. Private consumption was up 2.4 percent from a year ago, while gross capital formation was 3.2 percent higher over the same period. Likewise, retail sales in the month of October were up over 2.2 percent from a year-ago, further evidence of a strong consumer.
- Although GDP may accelerate some more in coming quarters, a return to 5 percent economic growth on a sustained basis, which was the underlying run rate a decade ago, does not seem likely anytime soon. The working-age population in Taiwan is contracting at present and productivity growth has been weak due, at least in part, to sluggish growth in investment spending. Furthermore, the economic engine of China, which is Taiwan's most important trading partner, has slowed from its breakneck pace of the past few decades, and further deceleration on the mainland appears likely in coming years.
- The central bank's policy rate, which has been cut four times since monetary easing commenced in September of last year, currently stands at 1.375 percent. Policy makers maintain a dovish bias, noting increased downside risks to trade and economic growth.





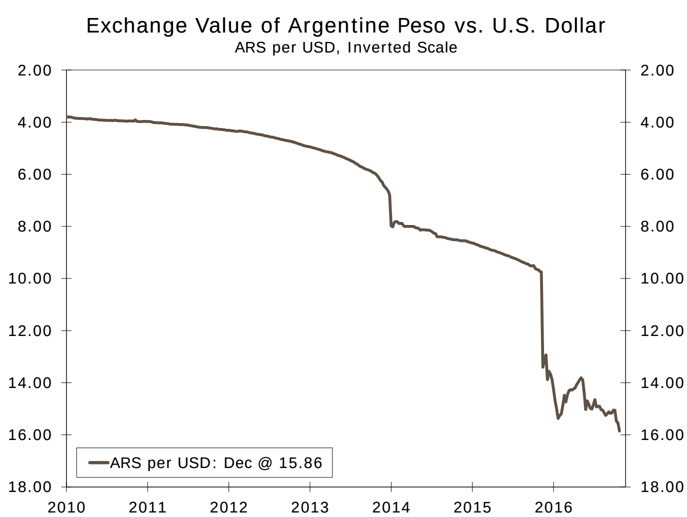


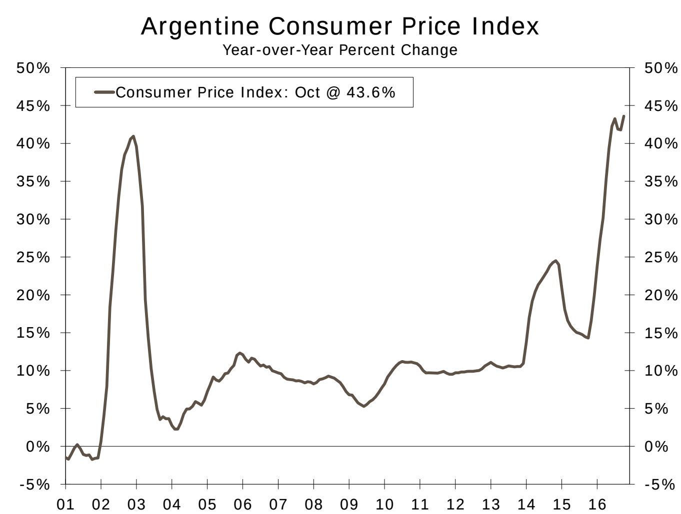


Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

Argentina

- The Argentine economy recorded a deep downturn in the second quarter—showing no signs of rebounding from its current recession—battered by a substantially weak performance from real investment, one of the sectors the new Macri administration was counting on to boost economic growth. According to the Argentina's statistical agency, the country's economy fell by 3.4 percent year over year.
- President Macri has enacted numerous business-friendly reforms (i.e. eliminating and/or reducing taxes on commodity exports) to attract investments and stimulate an economy held captive by high inflation; however, this rebound has yet to materialize as expected. The uncertainty created by the increase in inflation and the ensuing slowdown in PCE is having a larger impact on businesses' expectations for future economic growth.
- Industrial production has taken a beating over the quarter as the prolonged recession in one of Argentina's major trading partner Brazil, which accounts for more than 15 percent of exports, continues to dampen growth. Industrial production has fallen from its high seen in August and is down nearly 2 percent year over year.
- That said, we look for Argentina's economy to improve over the next two years as much needed reforms rebuild credibility, lift consumer and business confidence and allow the central bank to focus on constraining inflation.

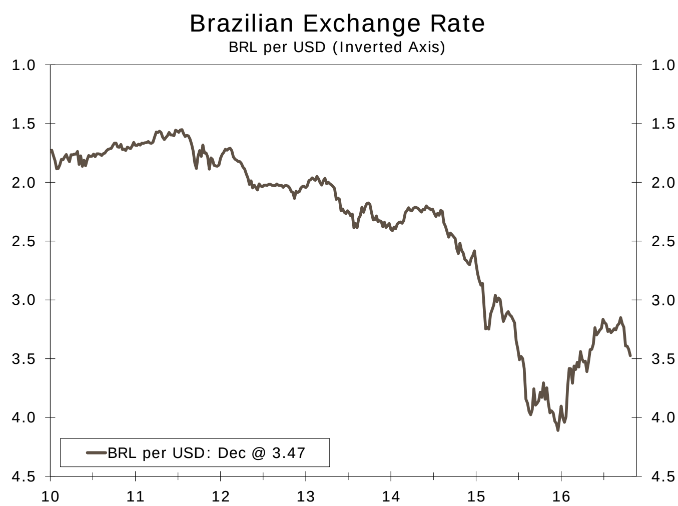


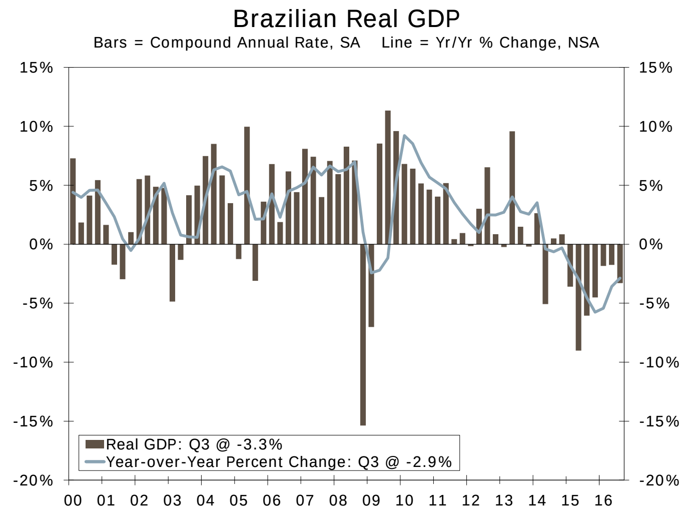


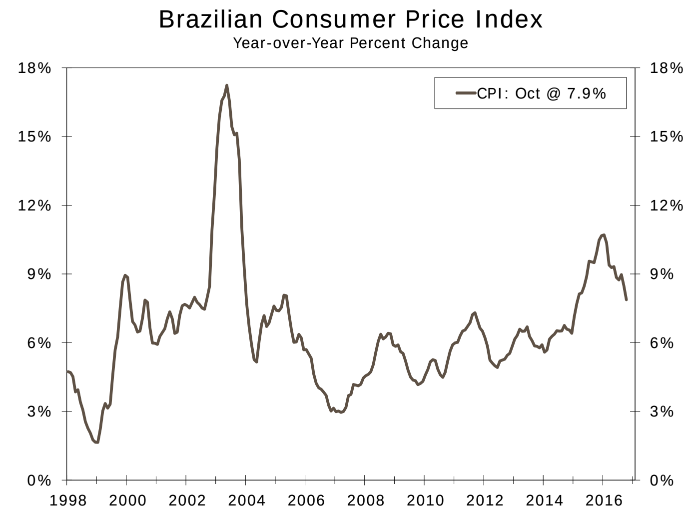
Source: IHS Global Insight and Wells Fargo Securities

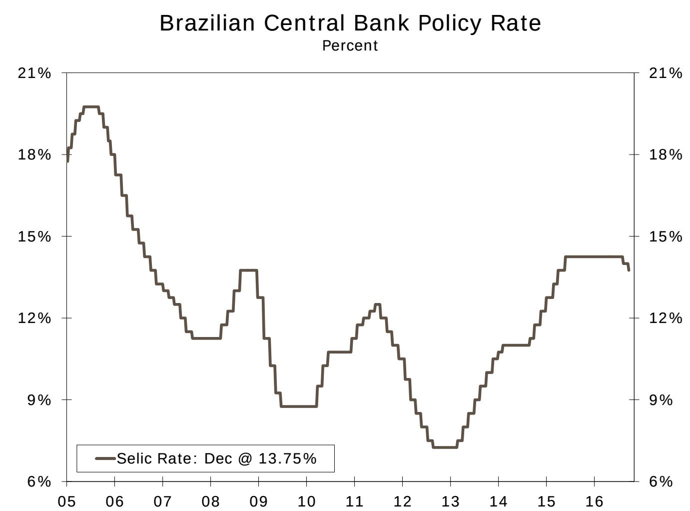
Brazil

- The Brazilian economy remained in a deep recession in the third quarter as political uncertainty has weighed on investments and consumer spending. According to the Brazilian statistical institute, Brazil's economy deteriorated over the quarter dropping 0.8 percent, much of this was expected due to the effects of the Olympic Games that quarter. However, the economy did moderately improve on a year-ago basis (down 2.9 percent). Net exports were the only component to contribute to GDP growth due to the collapse of real imports of goods and services. That said, we are cautiously optimistic about the recovery and expect some improvement for the Brazilian economy in the near future, growing by 0.8 percent in 2017 and 2.1 percent in 2018.
- The Temer administration, which came into power earlier this year after then-President Rousseff was impeached, has been trying to push legislation to limit government spending, in hopes of fixing Brazil's growing budget deficit and national debt which has raised concerns domestically and aboard.
- Brazil's central bank lowered the Selic benchmark interest rate in October by 25 bps to 14.00 percent form 14.25 percent—the first decline since October 2012—and cut the rate by another 25 bps to 13.75 percent in November as the central bank felt more comfortable with the potential path of inflation and has noted that future easing would be more gradual and moderate.





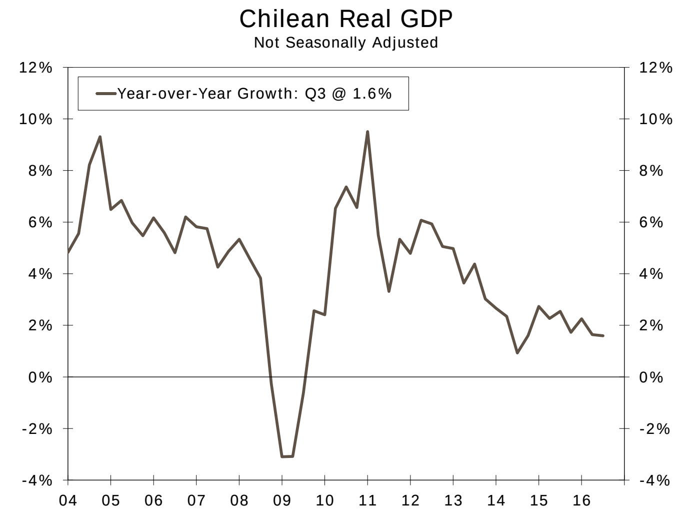


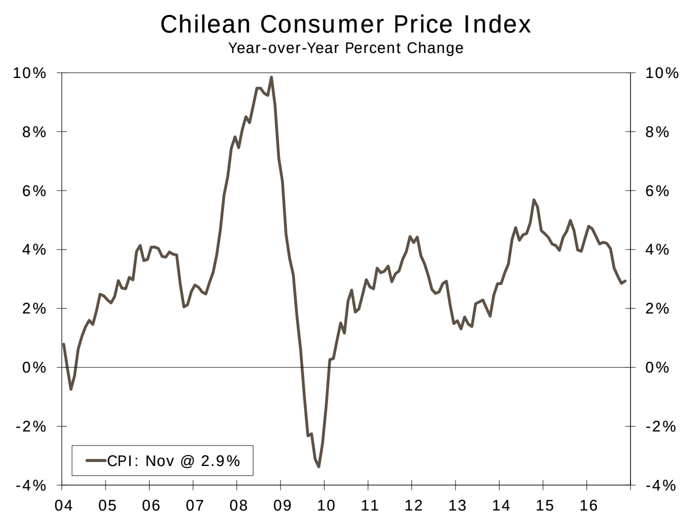


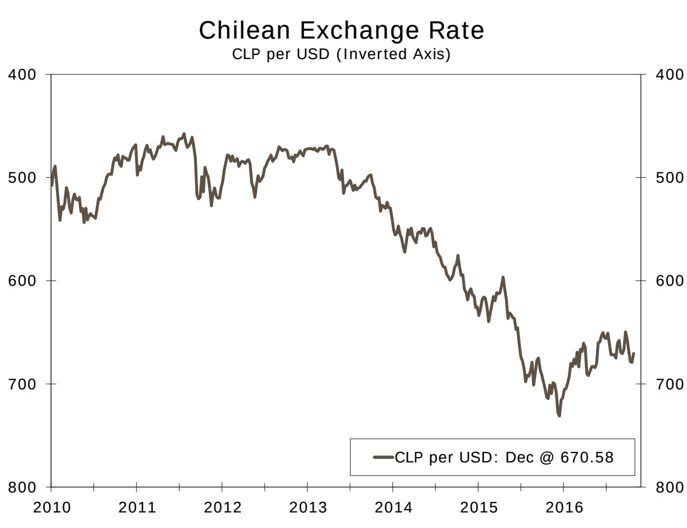
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

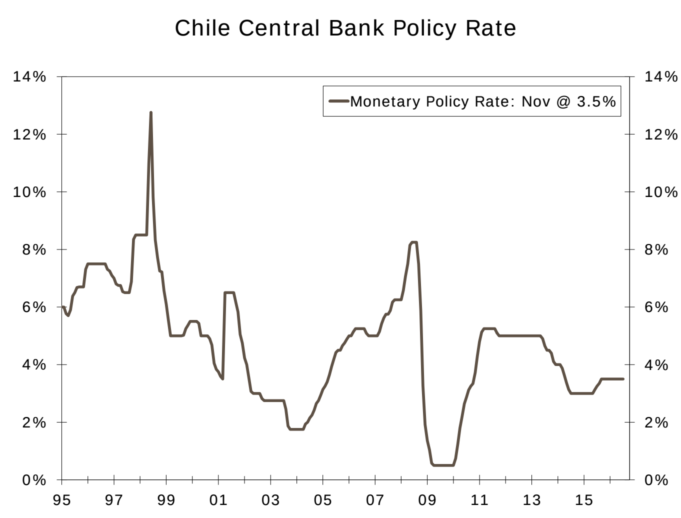
Chile

- The Chilean economy grew by a better-than-expected 1.6 percent year over year during the third quarter, helping the economy avoid a state of technical recession (two consecutive quarters of negative growth). Consumer and government spending continue to support growth, albeit at a moderate pace. Despite a relatively stronger quarter, there are no indications that economic activity is poised to accelerate in the near future due to downward pressures from slower global growth and trade. As the world's largest copper producer, the drop in prices in recent years has also led to a large decline in mining investment to levels not seen since 2012.
- Chile's central bank recently removed its tightening bias and shifted to a neutral policy bias in response to the abrupt slowdown in Chilean inflation. At the same time, it also hinted at possible easing early next year. Chile's inflation has slowed in recent months, to 2.9 percent year over year in November; this was a strong slowdown after a 4.2 percent year-over-year print in June.
- The Chilean peso has displayed modest weakness against the U.S. dollar since the U.S. elections, but has been more resilient than other Latin American countries. Going forward, we expect the peso to continue on its mild weakening trend over time due to the monetary policies of the US and Chilean central banks.





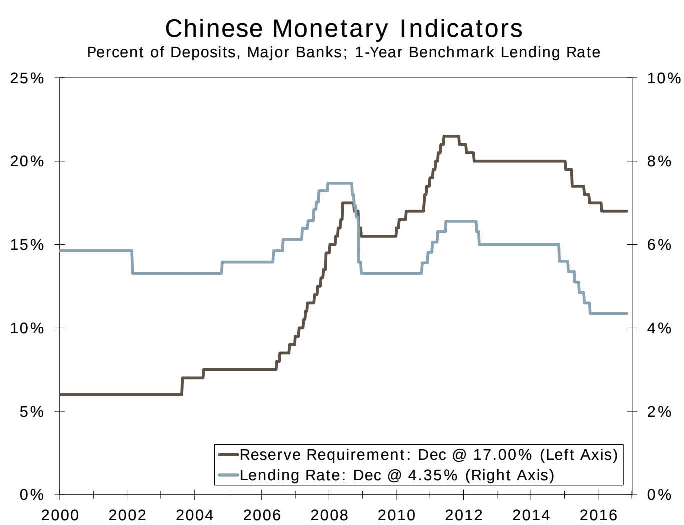


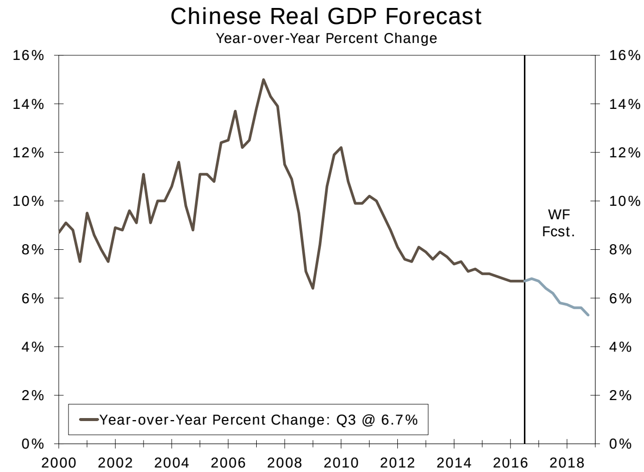


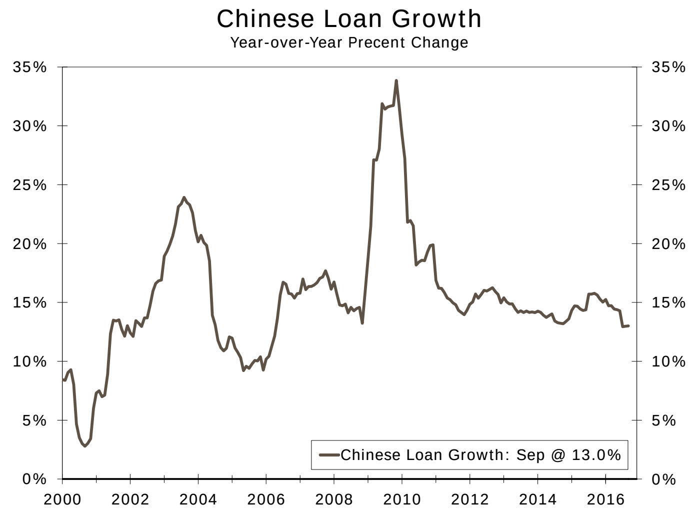
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

China

- Chinese GDP growth in Q3 was in line with the overall consensus and with our own call of 6.7 percent on a year-ago basis. After slowing for four successive quarters in 2015, Chinese headline growth has stabilized and has registered 6.7 percent for three consecutive quarters. Quarter-over-quarter growth also matched the consensus call of 1.8 percent. A breakdown of real GDP into its demand-side components is not yet available, but data by industry show that output growth in the "primary sector," which includes agriculture and forestry, and growth in the "tertiary sector," which includes services, increased year over year from Q2. Growth in the "secondary sector," a category that includes manufacturing and construction, remained flat at 6.1 percent from a year ago.
- Residential investment should decelerate in coming quarters, because lending standards are being tightened again at the margin. We are of the opinion that the Chinese economy will more or less experience a "soft landing," growing 6.0 percent and 5.5 percent in 2017 and 2018, respectively. The slowdown, we believe, will be the result of China's over-leveraged business sector, especially its state owned enterprises which are often kept afloat by the Chinese government. Furthermore, our currency strategy team sees the US dollar strengthening against the renminbi at a modest pace. The large foreign exchange reserve holdings of the central bank should help smooth out any large potential currency swings.



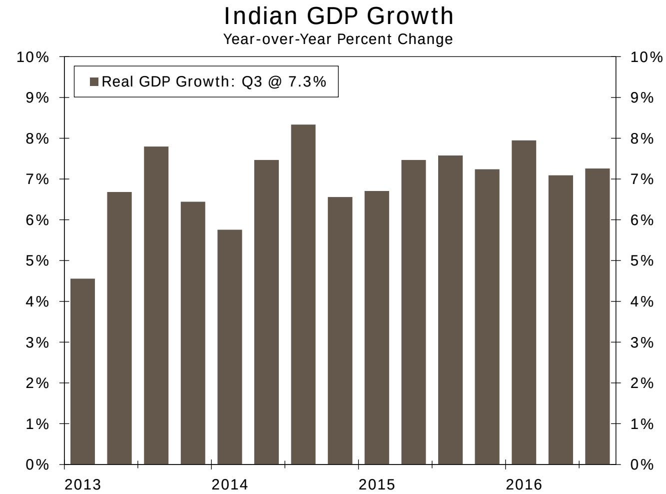


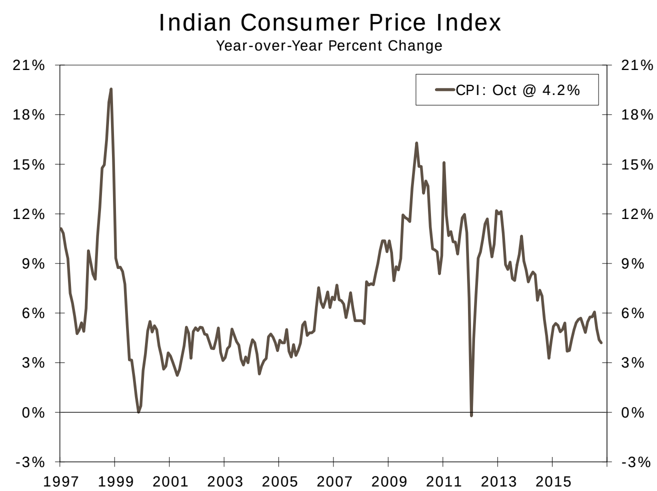


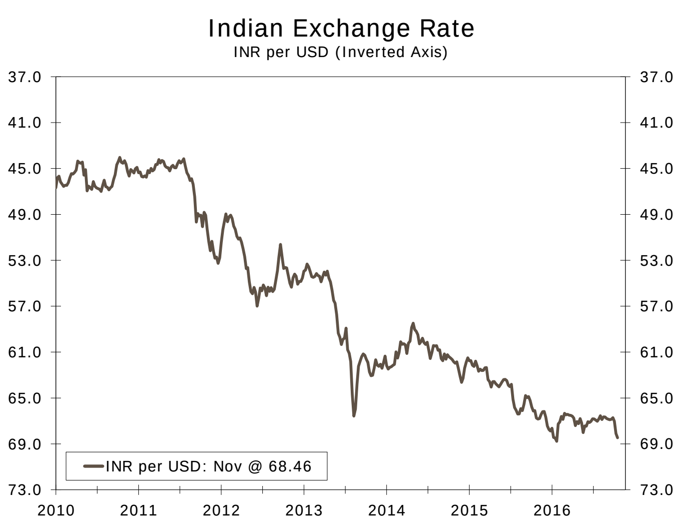
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

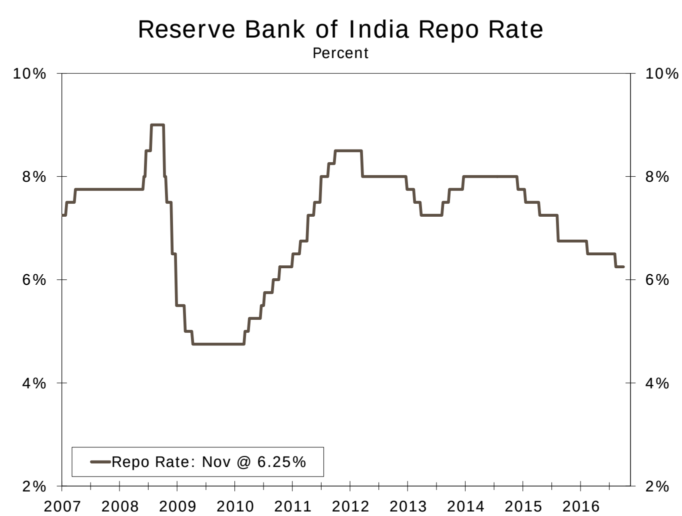
India

- Real GDP rose 7.3 percent on a year-ago basis in Q3-2016 (top chart). The outturn was stronger than the 7.1 percent rate that was registered in the second quarter, but it fell a bit short of the 7.5 percent rate that the market consensus had anticipated. A breakdown of the GDP data into its underlying demand components showed that consumer spending continues to be the primary driver of Indian GDP growth.
- It is unclear whether growth in India will strengthen further in the next few quarters. In early November, Prime Minister Modi made the surprise announcement that, effective immediately, 500 rupee and 1000 rupee currency notes would cease to be legal tender. The move to eliminate the high-denomination currency notes was intended to curb corruption and counteract rampant counterfeiting. However, the move could also disrupt legitimate commerce, at least in the near term, in the cash-based Indian economy. Although the partial demonetization of the economy could depress overall GDP growth in the near term, it is unlikely to have a lasting effect on economic growth in India in the long run.
- The recent depreciation of the currency could cause the Reserve Bank of India to hold off on another rate cut, at least in the near term. With the Fed likely to tighten in coming quarters, our currency strategy team believes that the Indian rupee will remain on the defensive vis-à-vis the U.S. dollar for the foreseeable future.





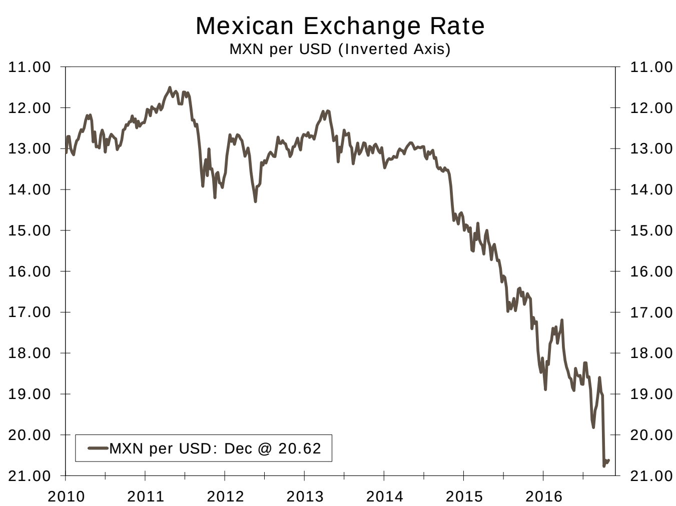


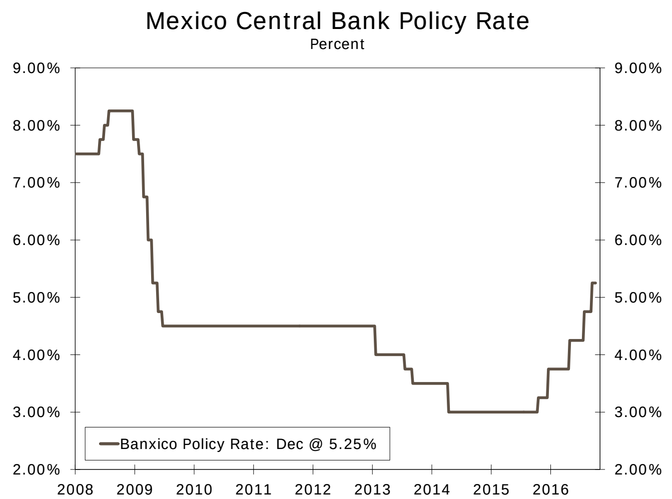


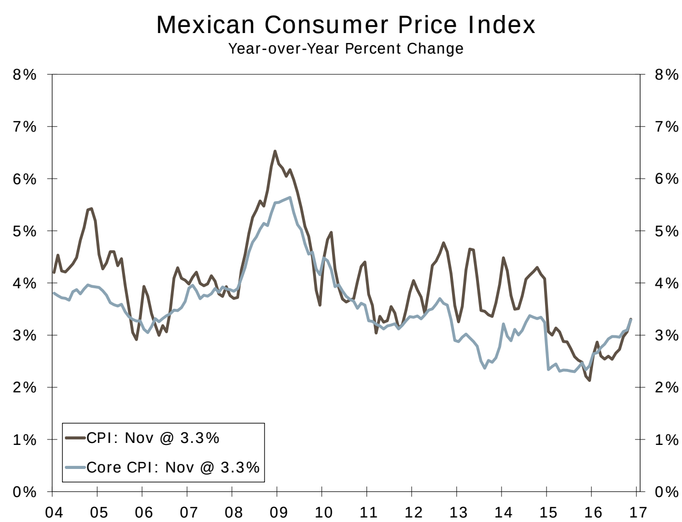
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

Mexico

- The Mexican economy strengthened further in the third quarter, growing by 2 percent year over year. However, the weakness did not come from the manufacturing sector; instead it was concentrated in the mining and construction sectors. This is somewhat good news for the Mexican economy as it entered the fourth quarter.
- The weakness in mining and construction caused a drop in industrial production which fell 0.1 percent in Q3. Meanwhile, output in the agricultural sector increased 1.2 percent, while the service sector increased a stronger 1.5 percent. The recent increases in interest rates has started to have an impact on the construction sector, while the energy reform approved several years ago has yet to show any positive effect on improving the country's petroleum production capacity.
- Mexico's currency hit an all-time low after Donald Trump's surprise presidential election win, falling around 13 percent.
- Post-U.S. election, we expect the Mexican central bank to continue to raise interest rates to counteract raising inflation expectations, a weaker currency and slower growth as a Trump presidency raises further concerns over Mexico's economic outlook, but especially over exports and remittances. As such, we look for economic activity to contract by 1.1 percent in 2017 and then resume growth in 2018, up 2.0 percent.



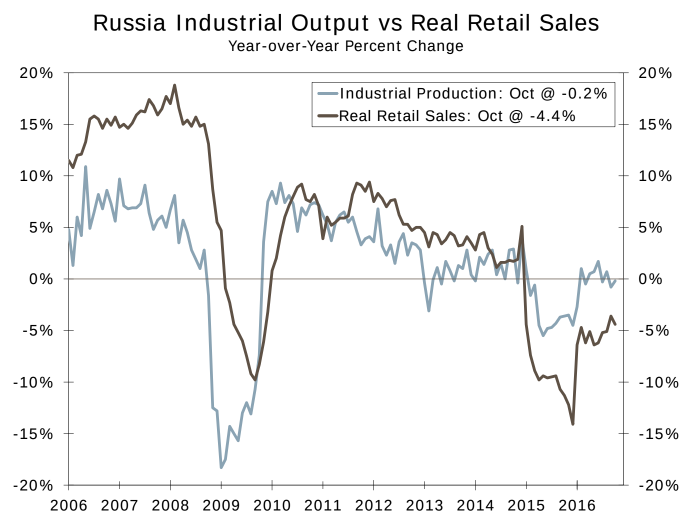


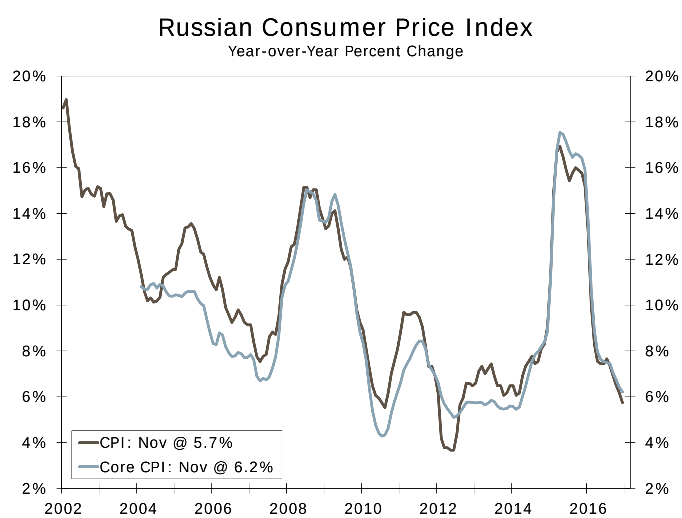


Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

Russia

- Russian GDP in Q3 contracted 0.4 percent from a year ago. However, the reading was less negative than analysts had expected and provides further evidence that the Russian economy is bottoming following its deep recession over the past two years. We look for the year-over-year rate of real GDP growth in Russia to turn positive again in the current quarter and maintain positive growth throughout 2017. Russia's trade surplus in September grew to $7.4 billion from August's $4.9 billion as both export and import values bested consensus forecast expectations. Relatively high oil prices in Q3, compared to the previous quarter, certainly helped boost the total value of Russian exports.
- As inflationary pressures continue to abate, real wages should strengthen further into positive territory. Real wages, which only recently emerged from negative year-over-year growth rates, are beginning to show signs of stability. As inflation has come down, interest rates have followed suit, which in turn should support investment spending and overall growth, everything else equal. The central bank has slashed its main policy rate from a high of 17.00 percent in early 2015 to 10.50 percent today.
- Despite the potential for renewed ruble weakness and inflationary concerns, we look for the Russian economy to recover in coming quarters.

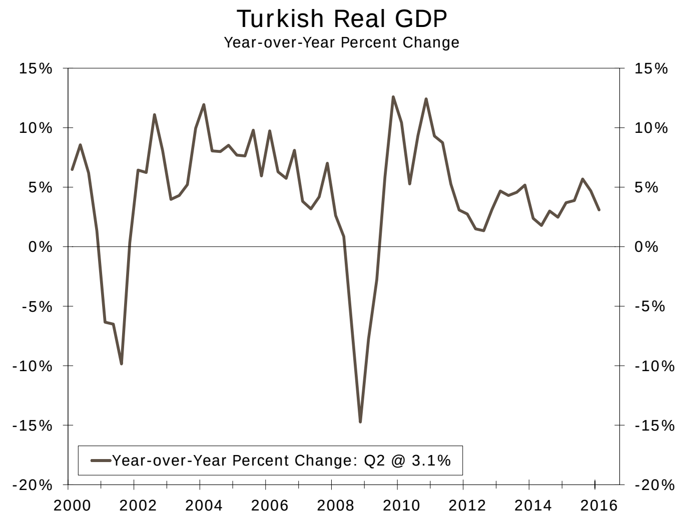


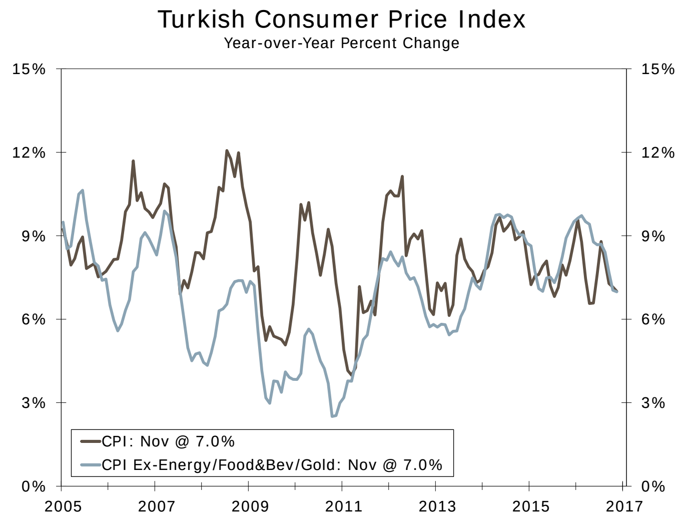


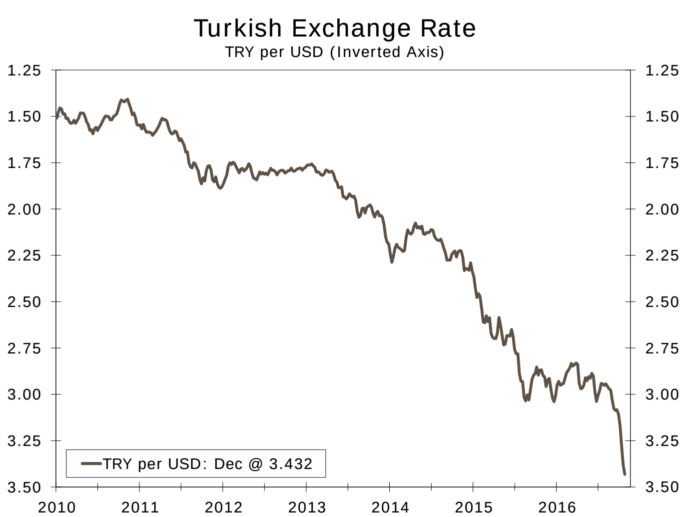
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

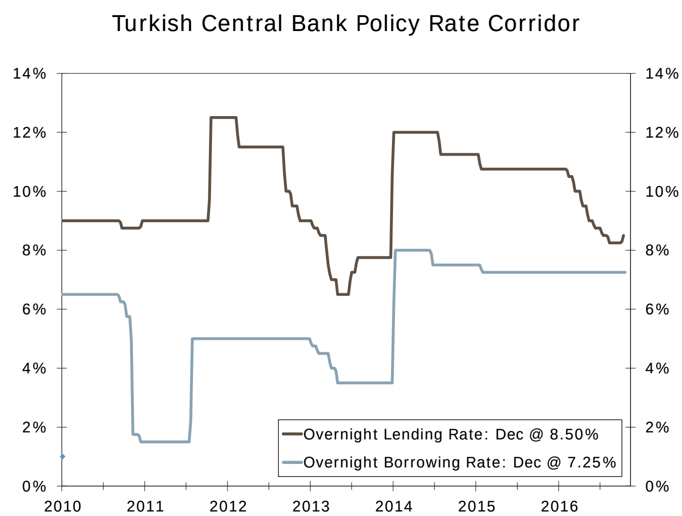
Turkey

- Real GDP in Turkey grew 3.1 percent from a year ago during the second quarter, marginally below the consensus forecast which called for 3.7 percent growth. A return to the boom years of the last decade and the early years of this decade do not appear to be in the cards anytime soon.
- While economic activity has continued to grow at a fairly healthy pace, recent political turmoil in Turkey has raised some doubts over growth stability. The attempted military coup in mid-July caused the lira to sell off sharply and has continued its path of depreciation through November. November's CPI reading of 7.0 percent was a notable decline from the previous month.
- Turkey's central bank guided interest rates lower over most of the year via cuts in its main policy rates. However, it reversed course on November 24 when it hiked rates again due, at least in part, to recent currency depreciation that threatens to undue the progress made on reducing CPI inflation.
- Our currency strategy team predicts a weaker lira against the greenback in coming quarters, softening at a very gradual pace. The trajectory of the lira is likely to be a key factor affecting the outlook for growth and central bank policy.





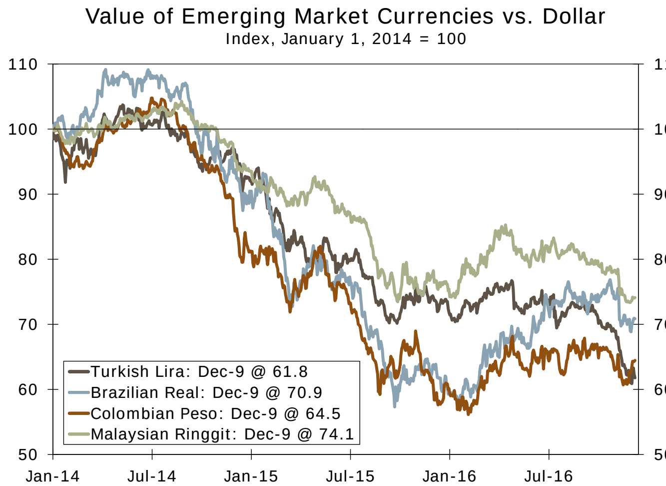


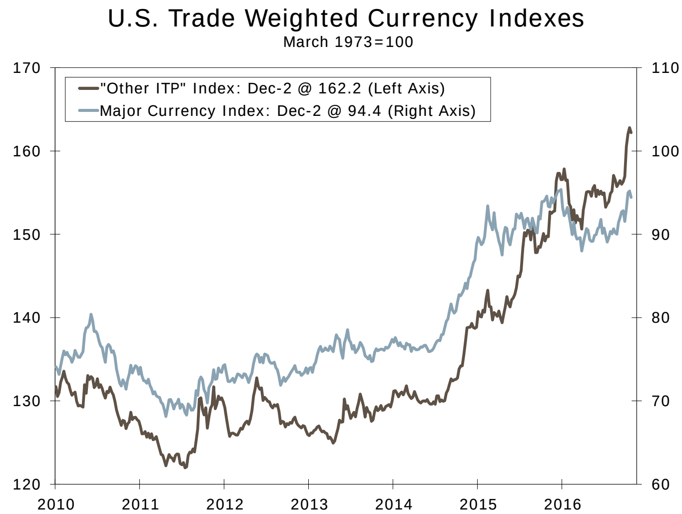


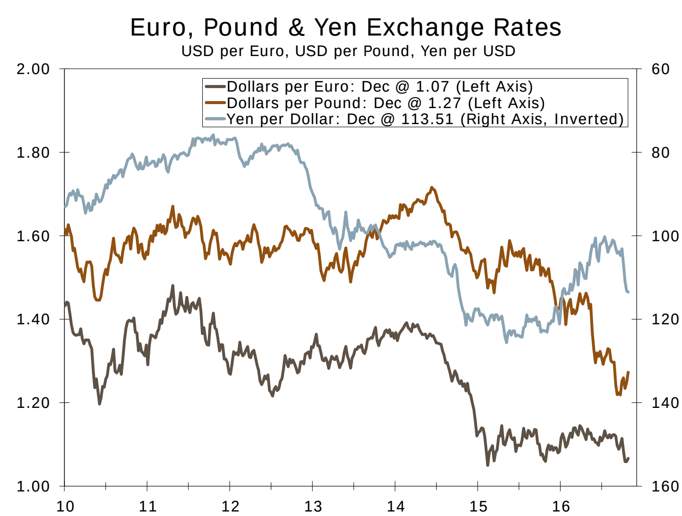
Source: IHS Global Insight, Bloomberg LP and Wells Fargo Securities

Dollar Exchange Rates

- The U.S. dollar has displayed robust strength over the past month, with the broad trade-weighted U.S. dollar index at its highest level since mid-2002. The renewed strength of the dollar comes in the wake of the U.S. presidential election. Markets appears to have priced in an increased likelihood of fiscal stimulus, which has pulled up U.S. interest rates and all but guaranteed a December rate hike by the Fed, providing a boost for the greenback.
- Among the G10 currencies, the Japanese yen has seen the most pronounced weakness. The Canadian dollar is little changed since early November, reversing losses seen earlier in the month in part due to the recent rally in oil prices. Moreover, the British pound is outperforming on hopes for a more favorable outcome for the United Kingdom in its impending exit from the European Union. While easing measures among the major central banks seem to be on hold, their current monetary policies remain, on balance, dovish—certainly a boon for the U.S. dollar.
- The Fed remains on course for rate increases in December and throughout the coming quarters, which should add to the dollar's strengthening momentum. Our currency strategy team expects overall U.S. dollar strength in 2017. Based on these forecasts, by late 2017/early 2018, the greenback's long-term up-cycle will have lasted around 6.5 years and seen an appreciation of approximately 45 percent, a length and magnitude that is historically consistent with the U.S. dollar's broader long-term cycles.



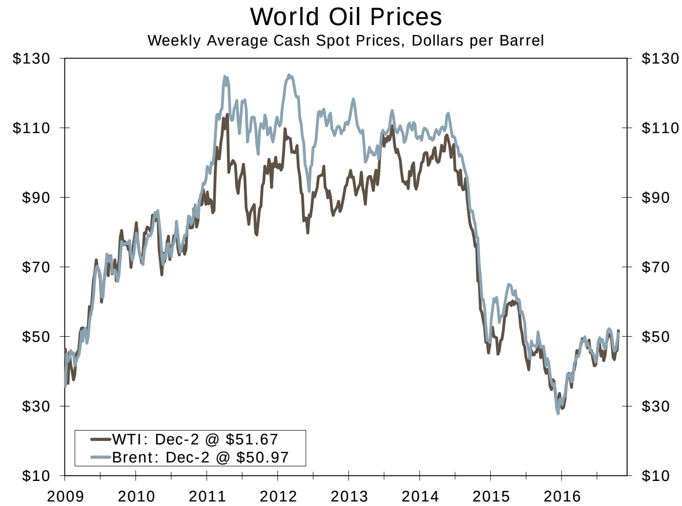


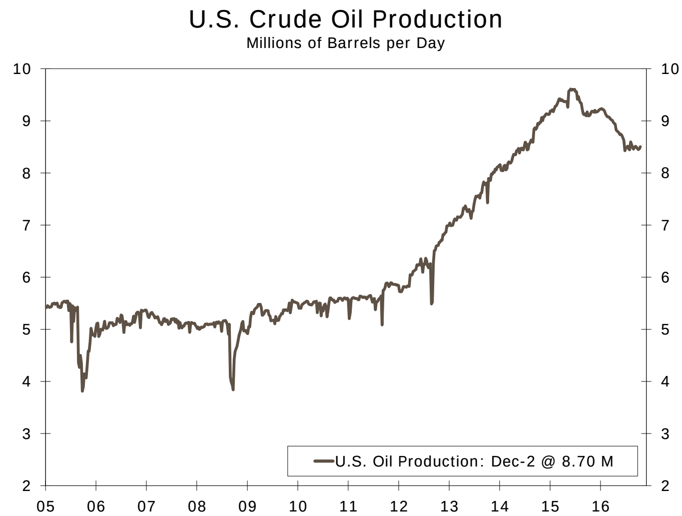


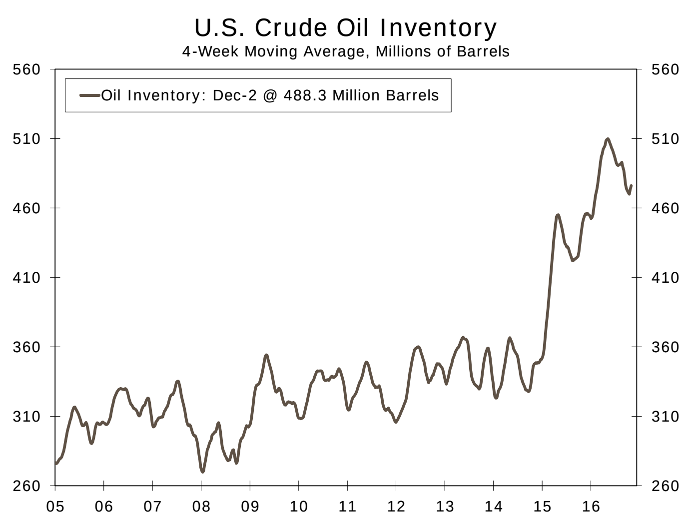
Source: Federal Reserve Board, Bloomberg LP, IHS Global Insight and Wells Fargo Securities

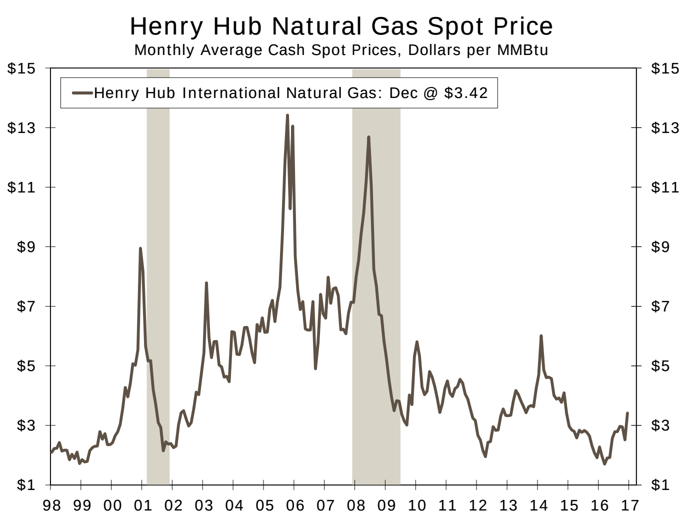
Energy

- Oil prices have climbed back near their highs of the year as OPEC and a select number of non-OPEC countries came to an agreement on November 30 to cut production by 1.2 mbpd beginning in January.
- Global inventories remain elevated, however. Even with global production cuts of around 1.0 mbpd, it would take nearly a year and a half to return oils inventories to more normal levels.
- Meanwhile, U.S. production has stabilized since the middle of the year. The number of rigs in use is at the highest level since February, suggesting U.S. production is unlikely to decline further in the near term.
- The tendency for OPEC members to not fully comply with agreed upon cuts and negligible compliance from non-OPEC members has kept our energy team's forecast for oil unchanged. Prices for Brent are expected to stay within the $50-55 range in H1:17 before climbing to around $60 by the end of 2017 as inventories are gradually worked down.
- Natural gas prices have climbed to about a two-year high in recent weeks. Prices had already moved up over the summer as hotter than average weather boosted demand for electricity generation, but recent forecasts for below-average winter temperatures have raised demand expectations. Natural gas in storage is virtually unchanged from year ago after two straight years of rising inventories.





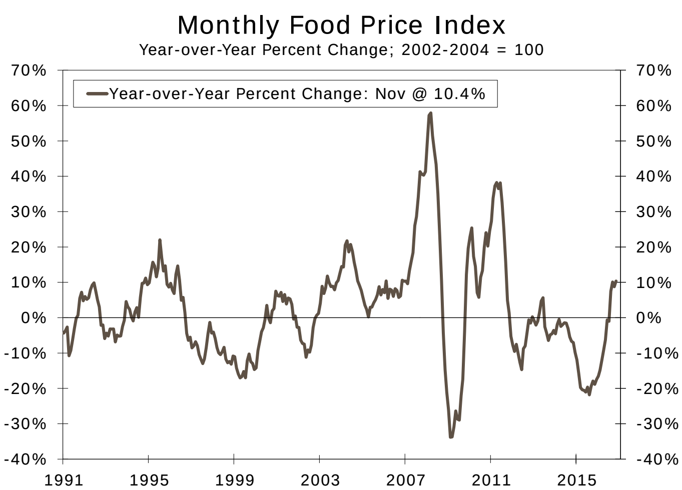


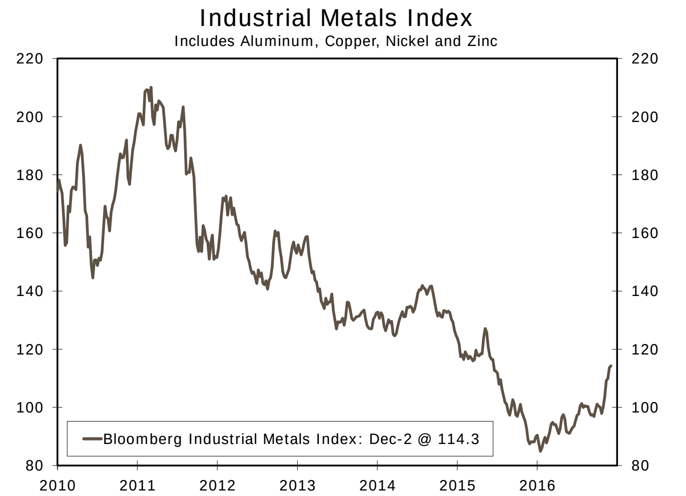


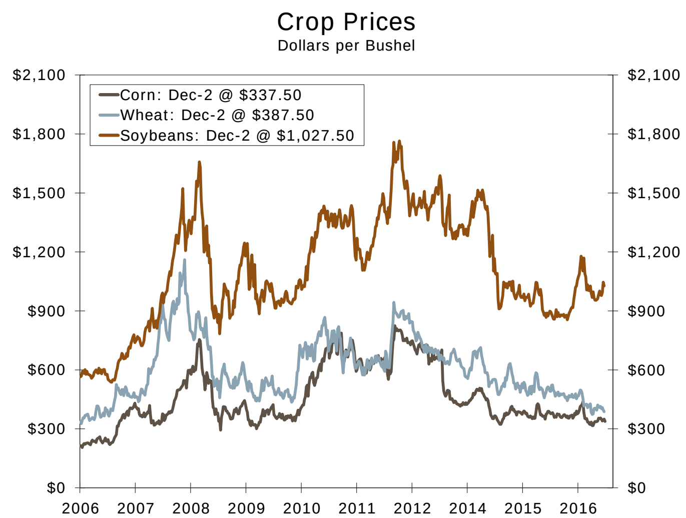
Source: IHS Global Insight, Moody's Analytics and Wells Fargo Securities

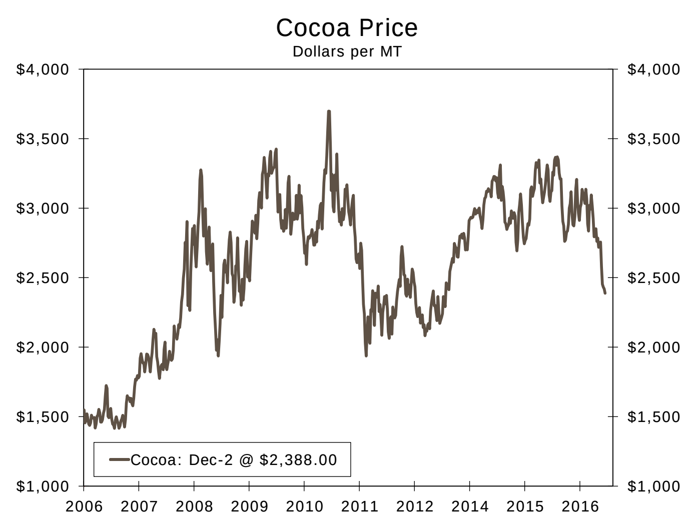
Other Commodities

- After little change from July to October, prices for industrial metals jumped amid expectations for greater U.S. infrastructure spending following the presidential election. The Bloomberg industrials metals index is now near a one-and-a-half year high. Copper prices have seen the biggest increase, but prices for aluminum, zinc, lead and nickel have all risen.
- While markets may be expecting greater demand in the United States, global demand is likely to remain challenged by the continued sluggish growth environment overseas. Stimulus efforts in China—the largest consumer of industrial metals—has supported demand in the recent months, but we still expect activity in China to moderate over the next two years as growth shifts away from the industrial sector. Prices should get some support, however, from more disciplined production.
- Prices for agricultural commodities have rebounded slightly since the fall, with the CRB foodstuff index at a three month high. Soybeans, sugar and livestock have driven the uptick, while prices remain near the lowest levels since the recession for staples such as corn, wheat and rice. Cocoa prices, which bucked the trend of lower commodity prices the past two years, have plummeted to more than a three year low amid good weather and lackluster demand.
- After falling for the about four years, the UN food price index is up 10.4 percent over the past year on higher dairy, oils and sugar prices.









Source: Bloomberg LP, Commodity Research Bureau and Wells Fargo Securities

Wells Fargo International Economic Forecast

(Year-over-Year Percent Change)

	GDP			CPI		
	2016	2017	2018	2016	2017	2018
Global (PPP Weights)	2.9%	3.0%	3.2%	3.1%	3.4%	3.6%
Global (Market Exchange Rates)	2.6%	2.8%	3.0%	3.1%	3.4%	3.6%
Advanced Economies[1]	1.7%	1.9%	2.1%	0.7%	1.8%	2.0%
United States	1.5%	2.2%	2.2%	1.3%	2.5%	2.6%
Eurozone	1.6%	1.6%	2.0%	0.2%	1.1%	1.5%
United Kingdom	2.0%	1.3%	2.1%	0.6%	1.9%	1.7%
Japan	0.6%	0.5%	0.7%	-0.1%	0.9%	0.7%
Korea	2.9%	3.1%	2.3%	1.0%	1.7%	2.0%
Canada	1.4%	1.9%	1.9%	1.5%	1.3%	1.8%
Developing Economies[1]	4.1%	4.1%	4.3%	5.5%	4.9%	5.1%
China	6.7%	6.3%	5.6%	2.0%	1.8%	1.8%
India[2]	7.6%	6.8%	7.7%	5.0%	4.3%	5.3%
Mexico	2.2%	-1.1%	2.0%	2.8%	4.4%	5.2%
Brazil	-3.5%	0.8%	2.1%	8.8%	5.0%	4.8%
Russia	-0.3%	1.5%	2.1%	7.1%	5.6%	5.6%

Forecast as of: December 08, 2016

[1]Aggregated Using PPP Weights [2]Forecasts Refer to Fiscal Year

Wells Fargo International Interest Rate Forecast

(End of Quarter Rates)

	3-Month LIBOR						10-Year Bond					
	2016	2017				2018	2016	2017				2018
	Q4	Q1	Q2	Q3	Q4	Q1	Q4	Q1	Q2	Q3	Q4	Q1
U.S.	1.05%	1.05%	1.25%	1.25%	1.50%	1.50%	2.42%	2.45%	2.48%	2.51%	2.54%	2.58%
Japan	-0.07%	-0.08%	-0.10%	-0.12%	-0.12%	-0.12%	0.00%	0.02%	0.05%	0.07%	0.10%	0.12%
Euroland[1]	-0.33%	-0.33%	-0.33%	-0.30%	-0.25%	-0.20%	0.30%	0.35%	0.50%	0.60%	0.70%	0.90%
U.K.	0.38%	0.38%	0.38%	0.38%	0.40%	0.45%	1.40%	1.50%	1.60%	1.80%	1.90%	2.00%
Canada[2]	0.90%	0.90%	0.90%	0.90%	1.15%	1.15%	1.60%	1.70%	1.75%	1.90%	2.00%	2.10%

Forecast as of: December 08, 2016

[1] 10-year German Government Bond Yield [2] 3-Month Canada Bankers' Acceptances

Source: IMF and Wells Fargo Securities

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