Global Outlook
Active Global Fixed Income

Fourth Quarter 2016
Major Macro Challenges for Markets in 2016

**CHINA**
- Risk of RMB devaluation
- Credit and Investment bubbles
- Housing % GDP over 3x US peak

**FED**
- Focus on global developments
- Cautious inflation outlook
- Slower pace of rate hikes

**GEOPOLITICAL**
- Middle-East tensions
- Oil prices - lower range
- Political instability

**EUROPE**
- Migrant crisis
- QE distortions
- Fears of “Brexit”
- Boost from weaker Euro fading

**US**
- Controversial Presidential election
- Congressional gridlock
- Weak external environment weighs on outlook

**Japan**
- 2% inflation by mid-2017?
- Diminishing return from policy actions
- Capital flows moving overseas
- Liquidity issues in JGB Market

Source: SSGA
QE = Quantitative easing
“Brexit” = Britain exit from European Union
Fed = US Federal Reserve
**Global Bond Market Landscape**

### POLICY

**Convergence**
- Fed slows normalization pace
- ECB and BOJ increase QE
- “Brexit” risk delays BOE action
- China - RMB stability preferable

### ECONOMY

**REBALANCING GROWTH**
- Loose policy in Europe and Asia
- Modest help from fiscal policies
- Shrinking output gaps – though still negative

### LOW-FLATION

**Oil, USD and Wages**
- Central bank caution – asymmetric risks in global outlook and lower oil price
- Less upward pressure on USD with fewer rate hikes
- Low productivity and subdued wage growth

Source: SSGA
ECB = European Central Bank
BOE = Bank of England
BOJ = Bank of Japan

---

**STATE STREET GLOBAL ADVISORS.**

3 GST10-2409
• Volatility is at historically low levels, which increases demand for carry
• Investors try to source carry from higher yielding sectors and selling volatility
• Negative feedback loop - increased demand to sell volatility at such low levels erodes the risk premium received by investors
• Is yield premium appropriately priced for level of risk?
• Reactions to geopolitical events or monetary policy communication mistakes could result in market corrections that are exacerbated by current positioning
• Low level of risk premium decreases “yield cushion” which helps investors to hold into volatility events
• Investors search for yield has driven portfolio allocations into lower credit, less liquid, unfamiliar sectors, which could potentially result in increased selling pressure in response to vol events

Source: Bloomberg
Data as of September 30, 2016
Key Drivers of Lackluster Global Growth

1. **Global excess slack:** Output gaps are negative and labor market slack persists
2. **Weak productivity growth:** Lack of business investment
3. **Lower potential GDP:** Demographics and weak productivity
4. **Limited policy options:** Monetary policy exhausted, little appetite for fiscal stimulus

As of September 29, 2016

Source: Thomson Reuters Datastream/ IMF
Lackluster Global Growth Continues

The above forecast is an estimate based on certain assumptions and analysis made by the SSGA Economics Team. There is no guarantee that the estimates will be achieved. This is not a prediction or projection of actual growth.

Sources: IMF, Oxford Economics, SSgA Economics Team

2016 and 2017 are forecasts.
Global Bond Yields Grinding Ever Lower

As of September 29, 2016
Past performance is not a guarantee of future results.
Negative Yields on the Rise

Global Bond Indices

- Aggregate
- Treasury
- Gov-Related
- Corporate
- Securitized

% of Index with Negative Yields

Source: SSGA
As of 30 July 2016
Past performance is not a guarantee of future results.