Global Strategy Q3 2016

The Brexit vote has led to heightened political and economic uncertainty, just as the the euro zone and US economies were showing signs of good progress. Thus the Federal Reserve is likely to postpone its next rate hike further, and the ECB is likely to monitor the situation carefully for the time being, while leaving monetary policy unchanged. Safe haven flows are keeping yields on safe bonds at low levels (highly rated sovereign and corporate bonds). High yield corporate bonds and stocks should continue to benefit from the search for yield.

Investment Strategy Q3 2016:

Govt. bond yields	September 2016
Germany (10Y)	0.10
USA (10Y)	1.60

Currencies	September 2016
EURUSD	1.12
CHF	1.10

Equity Performances		September 2016
Global	↗	0%/ +5%
Europe	↘	-5%/ 0%
USA	↗	0%/ +5%

Source: Erste Group Research

Note:
Our estimates are in absolute and not in relative terms. Bond yields and equity market returns in local currencies.

All prices are as of July 5, 2016

The past performance of financial instruments is not indicative of future results.

Economy

Recent monthly data indicate a significant acceleration in US economic growth in Q2. The Brexit vote and the uncertainty and heightened financial market volatility it has triggered should, however, lead to an economic slowdown in Q3. Particularly investment and consumer spending could turn out to be weaker than hitherto expected. We have therefore revised our forecast of 2016 US GDP growth from 2.3% to 1.9%. The euro zone has exhibited a robust recovery in Q1, growing by 1.7% y/y, but there is considerable uncertainty regarding the outlook for the second half of the year. In the medium term it may well be possible to attract investments which were hitherto destined for the United Kingdom, which could even boost economic growth. We have reduced our GDP growth forecast for 2016 from 1.6% to 1.3% and expect a slight acceleration to 1.6% in 2017.

Bonds

The Brexit vote has altered the outlook for US monetary policy significantly. FOMC members most recently expected two more rate hikes until year-end on average, now they are likely to wait in order to monitor the effects on the economy and employment. We therefore anticipate the next rate hike only in December 2016. Ongoing uncertainty should lend strong support to US treasuries, we expect yields to remain fairly stable until the end of Q3. The ECB has only begun to implement a part of its monetary easing measures in June, the effects of which therefore couldn't fully unfold yet. In view of the political and economic uncertainty, we are looking for the ECB to adopt a wait-and-see stance as well for the time being. Should the situation deteriorate, it could extend its asset purchase program or lower the deposit facility rate moderately further. Safe haven flows should keep yields on German Bunds at low levels in Q3.

Currencies

The Brexit vote has changed the outlook for US interest rates and the markets therefore lack an incentive to drive the US dollar higher. As a result, we expect EURUSD to move sideways slightly above the 1.10 level. The valuation of the Swiss franc continues to be very high and we are looking for CHF to weaken slightly over the remainder of the year. Gold is benefiting from safe haven flows and the global low interest rate environment.

Stocks

While earnings expectations for the US stock market are positive, prospects for the European market are worse – on a relative basis – because of an expected earnings decline in 2016 and the uncertainty caused by the Brexit vote. Due to higher revenue and earnings growth expectations, emerging markets should actually outperform developed markets. We expect the FTSE World Index to rise moderately in Q3, targeting a range between 0% and +5%, amid continued high volatility.

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Investment Strategy Q3 2016

Yields		current	Estimates Q3 16	Q4 16	Q1 17	Q2 17
10y. Govt. bonds	**Germany**	-0,19	**0,10**	0,50	0,90	1,20
	Austria	0,13	**0,30**	0,70	1,10	1,40
	US	1,37	**1,60**	2,10	2,40	2,80
	CEE					
	Czech Republic	0,43	**0,49**	0,63	0,62	0,53
	Hungary	2,98	**3,05**	2,98	2,90	2,82
	Poland	2,85	**3,10**	3,15	3,20	3,10
	Romania (5Y)	2,49	**2,45**	2,45	2,50	2,50

Source: Erste Group Research estimates

Currencies		current	Estimates Q3 16	Q4 16	Q1 17	Q2 17
Global	**EURUSD**	1,11	**1,12**	1,10	1,12	1,14
	CHF	1,08	**1,10**	1,11	1,11	1,12
	Gold (USD)	1.356	**1.350**	1.380	1.400	1.420
CEE	**CZK**	27,1	**27,1**	27,1	27,0	27,0
	HUF	316	**317**	318	318	318
	PLN	4,44	**4,41**	4,36	4,33	4,29
	RON	4,52	**4,50**	4,51	4,50	4,50

Source: Erste Group Research estimates

Equities *FTSE Indices*		**Estimate Q3 2016**	min	max	FX
Global		↗	0%	+5%	USD
	Europe	↘	-5%	0%	EUR
	USA	↗	0%	+5%	USD
Emerging Mkts.	**CEE**	↗	0%	+5%	EUR
	BRICs				
	Brazil	↗	0%	+5%	BRL
	Russia	↘	-5%	0%	RUB
	India	↗	0%	+5%	INR
	China	↗	0%	+5%	CNY

Source: Erste Group Research estimates

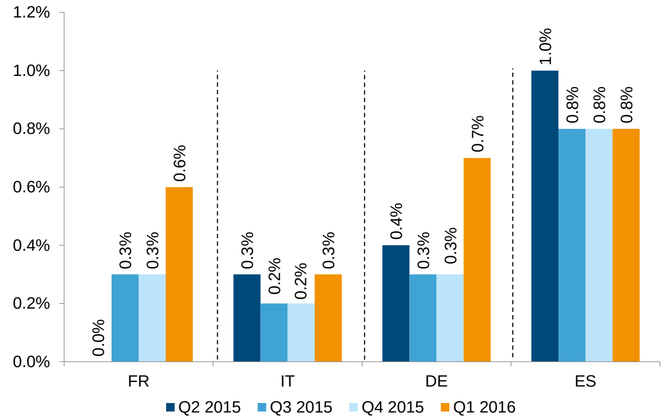
Euro Zone Economic Outlook

Stable growth in spite of financial market turmoil – Brexit weighs on outlook

GDP growth in the 1st quarter at + 1.7% y/y - with all big countries making positive contributions

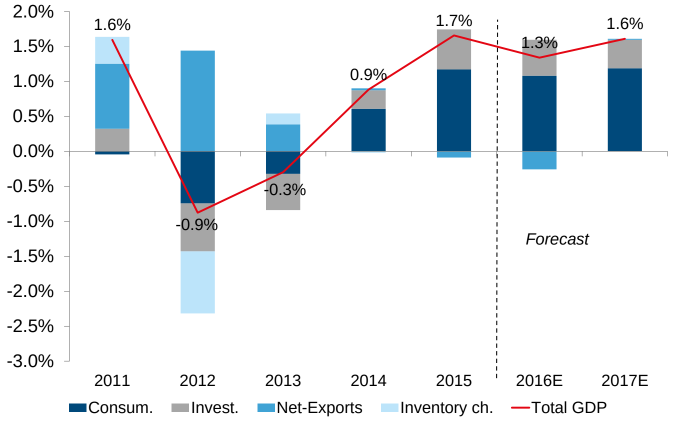
The economy of the euro zone grew by 1.7% y/y in the 1st quarter, with that economic growth has held up surprisingly well compared to the previous quarter, contrary to pessimistic expectations and in spite of intense financial market turmoil. In term of GDP components, consumer demand remained the most important pillar of growth in the euro zone. Consumption continues to benefit from declining unemployment rates as well as low inflation rates, which exert a positive effect on real disposable incomes. However, investment has in the meantime become a significant growth factor in the euro zone as well. On the country level, Spain remains the economy with the strongest growth momentum in the euro zone with a stable growth rate of 0.8% q/q, in spite of domestic political turmoil. Germany and France also delivered a convincing performance in the 1st quarter though, with growth rates of 0.7% q/q and 0.6% q/q respectively. Italy's economy still lacks momentum, as the problems of its banking sector with its large share of non-performing loans remain unresolved.

GDP growth (q/q) by region
Spain, Germany and France the pillars of growth in the euro zone



Source: Eurostat, Erste Group Research

GDP forecast for 2016 and 2017
Foreign trade to weigh on growth in 2016



Source: Eurostat, Erste Group Research

Brexit leads to considerable uncertainty regarding the outlook for the second half of 2016

The Brexit vote has led to considerable uncertainty with respect to the outlook for the 2nd half of 2016. We expect that the uncertainty will temporarily weigh on investment, trade and consumer demand. As a result we expect growth in the euro zone to be somewhat subdued in the 2nd half of the year. In the course of 2017 we anticipate a gradual improvement of the situation. In the medium term we believe that euro zone countries will succeed in attracting foreign investment which was hitherto destined for the United Kingdom. This should boost economic growth. ***Overall, we have revised our 2016 growth forecast for the euro zone to +1.3%, and expect a slight acceleration in 2017 to 1.6%.*** As a result of this it should take longer to close the euro zone's output gap. Over the medium term, growth in the euro zone should approach potential growth. According to recent estimates of the European Commission, potential growth should amount to approx. 1.1% in 2017.

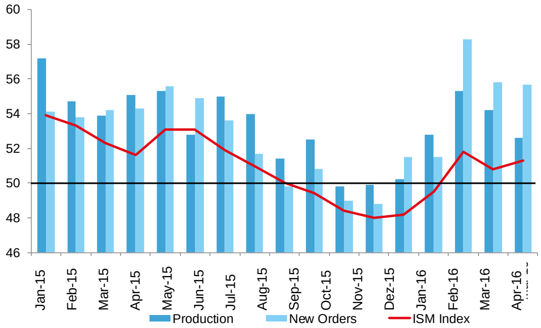
US Economic Outlook

Brexit will slow economic expansion

As expected, US economic growth in the first quarter was quite weak, and according to preliminary data was even slower than in the already disappointing 4th quarter of 2015. However, recent monthly data are pointing to a marked acceleration in economic growth in Q2. Especially consumer spending seems to have come to life and is supporting the economy. Data on corporate capital expenditures continue to be weak.
However, the result of the referendum in the United Kingdom and the uncertainty and elevated volatility in financial markets it has triggered should weigh on the economy and consequently we expect economic growth to slow significantly in Q3. Specifically investment and consumer spending could turn out to be weaker than hitherto expected due to the uncertainty. In order to assess the likely duration and depth of the slowdown we will pay especially close attention to upcoming employment data. We currently expect that the economy will get back on track again in the fourth quarter. However, should employment growth also be noticeably affected by the declining confidence, it would probably take longer for an economic recovery to take hold. This risk inter alia has to be considered as recent payrolls data were already disappointing prior to the referendum.
Coming months harbor a multitude of risks due to the outcome of the UK referendum. Among those with global implications is undoubtedly the fate of the financial industry centered in London. In addition there are political risks which consist in essence of a potential strengthening of anti-EU movements. To this we would point out though that the world is currently definitely better equipped to deal with a financial crisis than in 2008 and that an exit from the euro zone is far more complex and therefore less likely than an exit from the EU. However, these risks suffice to at least temporarily create uncertainty and with that are likely to weigh on the economy's performance.

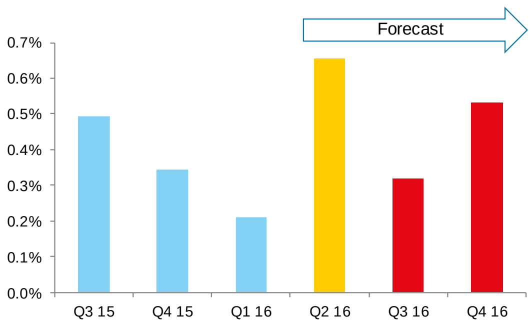
The US core inflation rate is stable and slightly below the Federal Reserve's 2% target. We essentially expect this trend to continue. Headline inflation includes the oil price as well and would only fail to rise if the price of oil were to decline again from September onward.

Monthly data point to an upswing in Q2...
Index>50 signals growth



Source: Bloomberg, Erste Group Research

...Brexit suggest upcoming soft spot though
GDP growth, q/q in %



Source: Bloomberg, Erste Group Research

CEE Economic Outlook

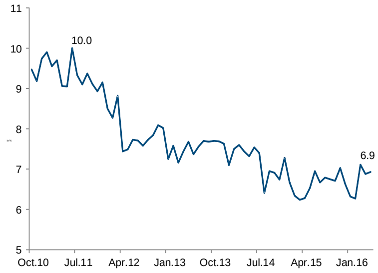
Growth in 1Q16 came in below that of the last quarter of 2015 in CEE countries, and not without reason: EU fund inflows were projected to decline already last year, given the switchover of the two programming periods, which meant a bump in the payout amounts in 2016. Consequently, construction is mostly to blame, as it has recorded double-digit declines in several CEE countries. In addition, industrial production also performed somewhat poorly in some countries, which came as a surprise to us. On the other hand, household consumption was rather strong, as expected.

As for the outlook, the somewhat poor performance in 1Q16 was most likely a temporary phenomenon. Wage growth and increases in unemployment have helped growth to stay healthy, while fiscal easing (especially in Romania, Poland and Hungary) could also help consumer demand remain the backbone of growth. EU fund inflow should also speed up after the slow inflow in 1Q16. That said, Brexit has complicated the situation to a great extent and will likely have negative spillovers on CEE economies. Due to Brexit, we have decided to cut growth projections in CEE economies by 0.1pp to 0.4pp (depending on the country in question) for both 2016 and 2017.

The strongest impact of Brexit on CEE economies comes through external trade. This might not come mainly from direct trade with Britain (this accounts for approx. 3-7% of total exports in respective CEE countries and is unlikely to vanish fully), but from trade with the euro area, with which CEE countries have strong trade relations, as Brexit will likely have a notable negative impact on growth there. Due to the export channel, countries which are more open to external trade (Czech Republic, Hungary and Slovakia) could be more strongly affected by Brexit. For Hungary and especially Poland (as it accounts for roughly 1.5% of GDP in the latter), a possible decline in workers' remittances could also be negative, although we would not overemphasize the importance of this channel as, in our view, it is unlikely that immigrant workers will return to their home countries in large numbers to earn lower wages. In Hungary, however, we expect that the government will counteract the slowdown and therefore we keep our GDP growth at 2% unchanged, but increased our expectation for the budget deficit.

BRIC Economic Outlook

China: Bloomberg GDP indicator



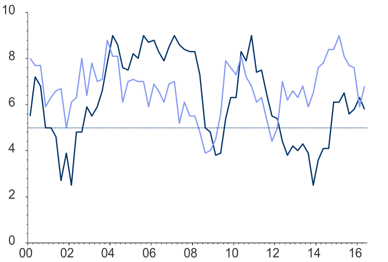
Sources:: Bloomberg, Erste Group Research

China

In the wake of a turbulent 1st quarter, the situation in China stabilized in the 2nd quarter, after China's authorities held out the prospect of slightly stronger monetary and fiscal stimulus. Based on leading indicators, China's economic growth has stabilized close to the 7% y/y level in the 2nd quarter. Bringing the previously rapid outflow of foreign exchange reserves to a halt in recent months was important for market confidence. However, the renminbi has once again lost significant ground against the US dollar in the wake of the Brexit referendum, which increases the danger that capital outflows from China could accelerate again in the summer months. As a result, concerns over China's economy could intensify again in the 3rd quarter.

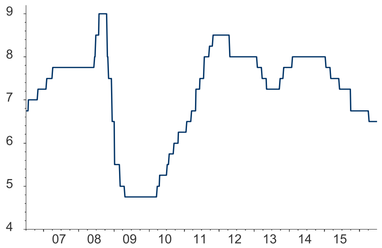
Investors should generally expect a continuous decrease in the growth momentum of China's economy in coming years. On the one hand, outsized growth rates are not possible in the **services sector, which is steadily gaining in importance** in China, while on the other hand, China will soon face **demographic problems** as well (the working age population is shrinking since 2015).

India: Ifo business climate index



Source: Datastream

India: Repo rate



Source: Datastream

India

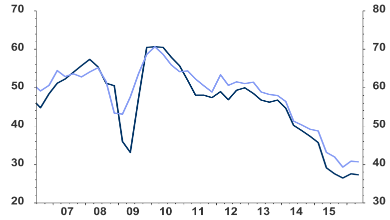
India's economy continues to post high GDP growth. A growth rate of 7.9% was recorded in Q1. India is benefiting from lower oil prices, while a below average monsoon season had a moderately negative impact on consumer spending. According to consensus estimates, Q2 growth is likely to have amounted to approx. 7.5%. For 2016 as a whole, GDP growth of 7.5% is forecast (IMF).

The manufacturing purchasing managers index improved once again in June. The index currently stands at 51.7 points, after 50.7 points in May. The increase is primarily attributable to rising domestic demand. The sub-index of new foreign orders also made a positive contribution to the overall index after declining in May.

India's central bank has lowered its repo rate by 25 bps to 6.50% in April. Inflation currently stands at approx. 5.8% and exhibits slight upward momentum. The markets expect no further rate cuts until the end of the year.

The Indian rupee has weakened slightly vs. the USD since the beginning of the year, declining by -1.6%. Last year the currency has depreciated by 5% against the USD. Compared to other emerging market currencies, the volatility of the Indian rupee remains very low.

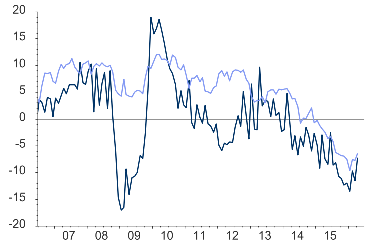
Brazil: Industrial Entrepreneur Confidence Index



Conditions: 27,3 (Q2 16) Expecations (rs): 40,7 (Q2 16)

Sources: Datastream, Erste Group Research

Brazil: Industrial production and retail sales growth negative year-on-year



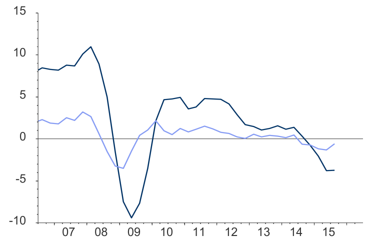
Ind. Production: -7,2% (Apr 16) Retail Sales: -6,4% (Apr 16)

Brazil

Brazil's economy remains in recession. Consensus estimates call for a GDP contraction of 3.8% this year. Only next year is the country expected to return to moderate GDP growth of 0.8%. A big problem is posed by the high inflation rate, which most recently stood at 10.3% and is expected to average 8.6% this year. Thus,the period of stagflation continues. In the wake of the impeachment of president Rousseff, political uncertainties have increased as well.

The unemployment rate has risen strongly and currently stands at 7.9%. The trend continues to point upward. According to consensus estimates it is going to increase to 10.2% in the course of this year, resp. to 10.8% in 2017. The business confidence index is one of the few detectable signs of potential economic improvement. It has slightly recovered recently, both in terms of current and expected future business conditions. The decline in industrial production continues, the pace of the contraction has however slowed. The extremely difficult situation of Brazil's economy is also reflected by a SELIC rate of 14.25% and 10-year government bond yields trading at 12.5%. Positive GDP growth rates are only expected to be reached by the middle of next year.

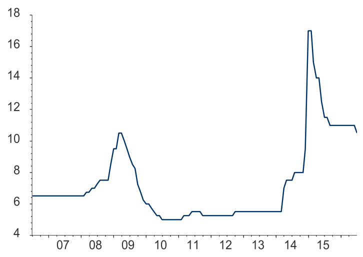
Russia: GDP, quarterly



J/J: -3,7 (Q3 15) Q/Q: -0,6 (Q3 15)

Sources: Datastream, Erste Group Research

Russia: Bank of Russia key repo rate



Refinancing rate: 10,5% (Jun 16)

Russia

With the recovery in energy prices, the outlook for Russia's GDP growth has improved. Consensus expectations call for GDP to contract by -1.0% this year, followed by growth of 1.2% in 2017.

The unemployment rate is expected to stand at approx. 6% both this year and in 2017. The inflation rate, which two quarters ago still stood at a very high 14.5%, has declined to 8.4% since the beginning of the year. The consensus expectation for consumer price inflation for 2016 as a whole is 7.7%, followed by 6.2% in 2017.

Russia's current account balance is positive. A surplus of 3.6% of GDP is expected to be achieved in 2016, which should increase to 4% in the coming year. However, the country has a budget deficit, although forecasts have improved in view of the rise in energy prices. The budget deficit is expected to amount to 3.2% of GDP this year and to decrease to 2.3% of GDP in 2017.

Signs that the economic situation is improving have recently become more pronounced. The services PMI most recently stood at 51.8 points. This indicator is signaling expansion for the fourth consecutive month. The manufacturing purchasing managers index has picked up as well. It currently stands at 49.6 points, only slightly below the neutral level of 50. For the first time in three years, employment in the manufacturing sector has increased as well. In light of the improvement in the economic situation, Russia's central bank has lowered its key repo rate to 10.5% in mid June. Yields on 10-year government bonds continue to be in a downtrend and currently stand at 8.5%.

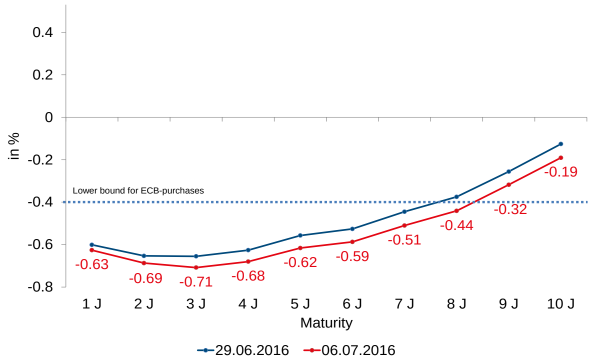
Bonds	Yield estimate Q3 2016
Euro Zone Main Refinancing Rate	0.00 %
German Bund	0.1 % (10Y)

Uncertain environment argues in favor of the highest rated sovereign bonds

In reaction to the expected slowdown of economic growth in the euro area on account of the Brexit vote, the ECB is likely to intensify its dovish rhetoric. The ECB council is likely to point out that the risks to the achievement of its objectives have increased. Assuming that the oil price remains close to current levels, the inflation rate will however rise further in the autumn, and therefore approach the ECB's target. What actions will the ECB take under these conditions? We expect that monetary policy won't be altered right away. The central bank will instead want to await the effects of the Brexit vote on the economy, as the implications for investment and consumer spending are difficult to assess. Moreover, the ECB has announced a number of additional easing measures only in March (some of which have only just begun to be implemented in June), the effects of which haven't fully unfolded yet. Should the environment deteriorate to a greater degree than we currently envision, holding out the prospect of extending the current high rate of securities purchases beyond March 2017 (the current minimum time horizon set by the ECB) would probably be the first step the ECB would take. Another reduction in the deposit facility rate should in our opinion only be expected if inflation were to weaken significantly.

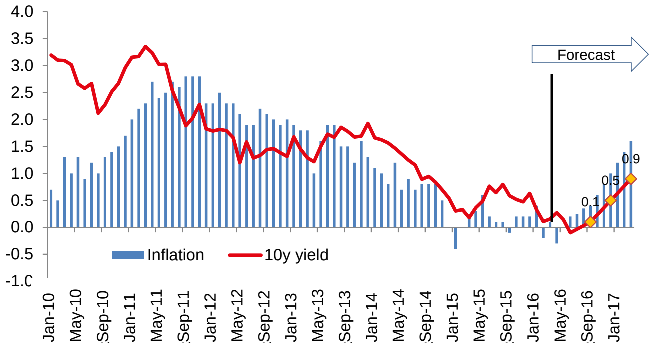
Government bonds with pristine ratings should continue to be well supported by the uncertain economic and political environment in coming months. In view of the expected increase in the inflation rate, the real yields of 10-year Bunds should decline below zero according to our forecast, which is tantamount to crisis levels. We currently expect that the situation will stabilize after several months, which should be reflected by an increase in yields most likely in the fourth quarter. In view of political uncertainties (fears of a further splintering of the EU), we believe the risks to our yield forecasts are skewed to the downside over the coming year. However, we don't believe that these risks will actually materialize, even though the associated uncertainties can potentially linger for longer in the financial markets.

More maturities have declined below the minus 0.4% threshold
German government bond yield curve



Source: Bloomberg, Erste Group Research

Yields on Bunds should remain below the inflation rate
10 yr. yields and inflation rate in %



Source: Bloomberg, Erste Group Research

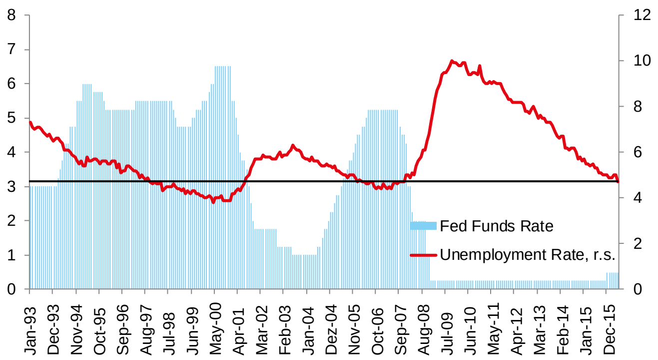
US	Yield estimate Q3 2016
Federal Funds Rate	0.25 – 0.5 %
US Treasury Notes	1.6 % (10Y)

US Treasuries will reflect uncertainty

With the result of the referendum in the United Kingdom (UK) the outlook for US monetary policy has changed drastically. The last median projection of the members of the federal open market committee in mid June calling for two rate hikes by year-end should be obsolete now. The FOMC could at least opt for a delay of several months in order to await the effects of the referendum. Since we expect the economy to initially slow down, it should take at least until year-end before the next US rate hike is implemented. Even if economic growth does slow down, the US economy remains close to its potential and interest rates continue to be very low relative to the unemployment rate. The timing of the next rate hike will ultimately depend on the extent of the slowdown.

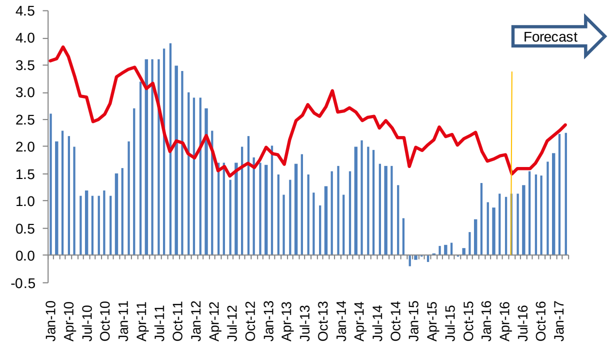
At the moment we expect that the uncertainty after the Brexit vote and the associated financial market volatility will remain in effect for some time. The unknowable consequences of the Brexit vote harbor the potential for further shocks. How will the financial sector digest the new status of the United Kingdom and the financial center London? How will the political situation in the EU/ euro zone evolve henceforth? The ongoing uncertainty should provide strong support for US Treasuries. Should additional downside risks materialize, a further decline in yields has to be expected. However, our base case scenario is for yields to remain relatively stable until the end of Q3. The outlook beyond that time horizon is currently very uncertain in view of the special situation. A stabilization of the situation and a slight increase in yields appears most likely to us though. This is not least due to the fact that inflation rates should begin to increase steadily from August onward due to higher oil prices (provided oil prices don't plummet again). If yields were to remain at current levels for a long time period, real interest rates would turn negative, which would only be justified in a crisis scenario.

The federal funds rate remains uncommonly low even if the economy slows down
Federal funds rate and unemployment rate in %



Source: Bloomberg, Erste Group Research

Nominal yields should rise, real yields should approach levels close to zero
Inflation rate y/y, 10 yr. note yield in %



Source: Bloomberg, Erste Group Research

CEE Government Bonds	Interest Rate Forecast Q3 2016
Czech Republic	0.49% (10Y)
Hungary	3.05% (10Y)
Poland	3.10% (10Y)
Romania	2.45% (5Y)

After the UK referendum brought victory for 'Leave', CEE currencies and bond markets reacted as expected: they weakened. Looking at developments a few days after the vote, however, some divergence between currency and bond markets is already observable: the Polish zloty and the Hungarian forint seem to be losing ground further, while their government bond markets (denominated in local currency) are gaining. This is because Brexit is expected to be anti-inflationary, which could prompt CEE central banks to be more accommodative, which is bond-positive. The "lower for longer" environment is, however, somewhat negative for CEE currencies.

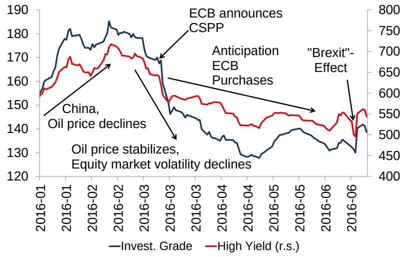
At this point, however, none of the CEE currencies is fundamentally overvalued, CEE countries are not running any significant external imbalances and central banks in CEE have much greater firepower if they opt for FX interventions. FX reserves are at a very comfortable level in all CEE countries, exceeding a full-year's gross external financing needs. At the end of 2008, ratios of FX reserves to gross external financing needs ranged within just 0.4-0.9.

As for bond yields, we definitely do not envisage any long-term increase. Inflation figures are expected to remain at low levels, a situation which has actually been exacerbated by the Brexit vote. This means that monetary authorities are still expected to keep rates at very low levels. Risks have increased after the Brexit vote that we will see easing in some (unconventional) form in Hungary. In Poland, although authorities have flagged their expectations of only a mild slowdown in Polish growth due to Brexit, any changes in risks are more to the downside post-Brexit than to the upside. In Romania, excessive fiscal loosening will send the budget shortfall to around 3% of GDP (from just 0.7% last year), in our view. Subsequent GDP growth and increasing inflation, coupled with the financing risks of the deficit, are likely to cause the NBR to hike in 4Q17, but this is still not expected to increase yields much and only likely in 2017.

Safe haven flows pushed 10Y German Bunds to a historical low and risk-off mode was behind the spread widening in CEE. Since then, spreads have narrowed again for CEE bonds. Further spread development will depend on the risks of another EU country leaving the Union (the worst would be a euro area country). On the other hand, Brexit alone brings with it a lack of confidence and thus deflationary risks to the EU – factors supporting a low yield environment.

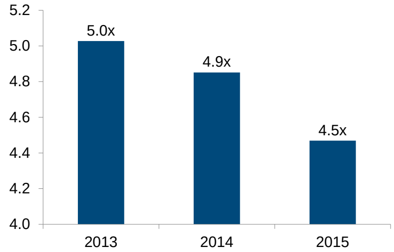
EUR-Corporate Bonds
Investment Grade
High Yield

The ECB's „CSPP*“ should mitigate the negative effects of the „Brexit“ vote
Spreads over government bonds
in basis points, average remaining term to maturity: ~ 5 years



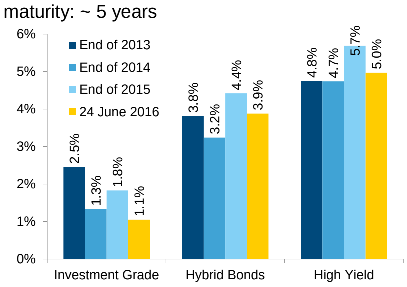
As of: 29. June 2016
“C**orporate **S**ector **P**urchase **P**rogramme“ = ECB corporate bond purchase program*
Source: Markit, Erste Group Research

The debt repayment period of European high yield issuers is declining
Financial liabilities / EBITDA (median)



Source: Moody's, Erste Group Research

Average yields-to-maturity have decreased since the beginning of the year
Average yields in %, average remaining term to maturity: ~ 5 years



As of: 29. June 2016
Source: Markit, Erste Group Research;

Three events have shaped the EUR corporate bond market in the first half of 2016. At the beginning of the year, the high yield segment in particular came under pressure due to concerns about China's economic growth and the pronounced decline in the oil price. From 10. March onward, the ECB's surprise announcement of a corporate bond asset purchase program triggered a rally in bonds of all rating categories. From early June onward, the referendum over the UK's EU membership scheduled for 23. June began to be foreshadowed in the markets: stock market volatility increased and credit spreads widened. Shortly before the referendum, market participants expected the “remain” side to win, and positioned themselves accordingly. This exacerbated the negative market reaction on 24. June. Credit spreads (i.e., spreads over government bonds) widened significantly. However, they remain below the levels recorded at the beginning of the year.

The “Brexit” vote creates uncertainty over the future political and economic development of Europe, and above all, Great Britain. Bonds of British issuers should reflect this uncertainty to a greater extent than bonds of continental European issuers. The former represent 12% of the issuance volume in the EUR high yield market and 9% of the outstanding volume in the investment grade market. The largest British issuers (BP, Vodafone, British American Tobacco, Anglo American) are geographically widely diversified. In the medium to long term, sector-specific factors (e.g. commodity prices) should be more important for them than the “Brexit” vote. Statements on the long term effects of the vote on the ratings of British issuers and issuers with large UK exposure are premature. What alternative trade agreements between the UK and the EU, resp. third countries will be struck will be decisive in this respect. Any steps that provide greater clarity about the future relationship between Great Britain and the EU should definitely improve sentiment in the EUR corporate bond market.

From a fundamental perspective we expect credit spreads to tighten over the remainder of the year, both in the investment grade (IG) and high yield (HY) segments. The debt repayment period of EUR HY corporate bond issuers has been reduced in recent years. The “Brexit” vote should dampen economic growth in Europe, although leading indicators such as the IFO business climate index still pointed to a robust German economy shortly before the referendum. If German business confidence remains positive overall, credit risk premiums should decline all over Europe.

The investment grade segment will continue to benefit directly from the ECB's corporate bond purchase program. The purchases are underway since 8. June. To date the purchase volumes have exceeded market expectations.

Uncertainties over political developments in Europe could weigh more strongly on sentiment in the corporate bond market in the second half than the economic slowdown in emerging markets.

Negative yields-to-maturity on safe government bonds should continue to stoke strong demand for corporate bonds. In our opinion, the average risk/return tradeoff remains convincing. This assessment applies to the EUR HY segment as well.

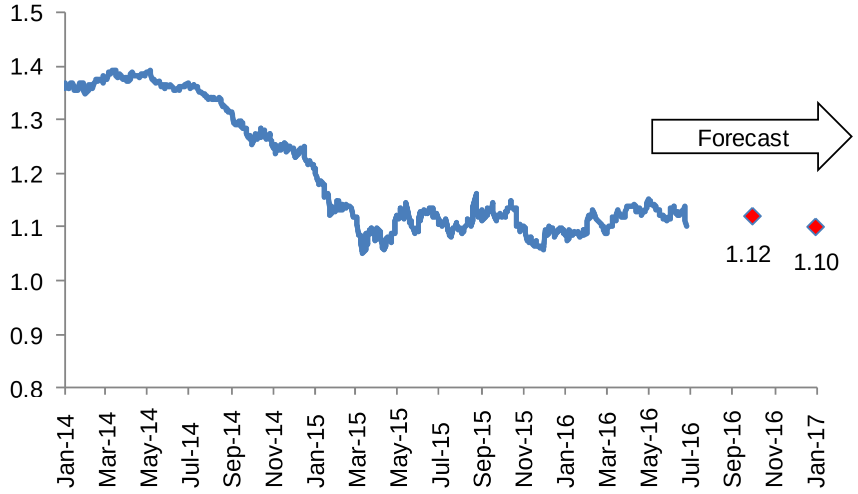
Currencies

	Outlook Q3 2016
US-Dollar	1.12

Sideways move in EURUSD appears most likely

The result of the referendum in the United Kingdom had surprisingly little effect on EURUSD. The reaction that should have been expected would have been a massive appreciation in the US dollar, confirming its safe haven status. Instead, all that happened was a brief spike of just a few percentage points on the first trading day, very little of which was left a few days later. We believe the reason for this is that the Brexit referendum has altered the outlook for developments in US interest rates as well. The uncertainties associated with the vote will make the Federal Reserve even more cautious, and cause it to maintain its wait-and-see stance. Interest rate expectations have already been the dominant driver of EURUSD in recent months. Without the prospect of higher US interest rates the market obviously has no incentive to push the US dollar higher. We therefore expect EURUSD to move sideways in coming months, slightly above the 1.10 level. The risks are however skewed disproportionately toward an appreciation of the US dollar. Should political tensions in the EU escalate and other countries want to follow the British example, a veritable crisis could be triggered in the EU, although we don't expect that the EU or the euro zone would actually break up. Moreover, the helpless reactions of British politicians in the wake of the referendum have shown that it is one thing to threaten an exit, but quite another to actually be confronted with a vote in favor of one. For EURUSD it will also be important whether the markets begin to have doubts about the continued survival of the euro zone. Should this be the case, the dollar could ultimately still rally significantly, although this doesn't look likely at the moment.

EURUSD exchange rate should remain close to current levels
EURUSD exchange rate



Source: Bloomberg, Erste Group Research

Outlook Q3 2016

Swiss Franc 1.10

After rapid and strong appreciation in the early trading hours on June 24 in the wake of the outcome of the EU referendum in the United Kingdom, the Swiss franc is now fluctuating in a range of 1.08 to 1.09 francs per euro. Relative to our expectations the reaction was surprisingly subdued and short-lived. According to numerous media reports, the SNB intervened in foreign exchange markets shortly after the result of the referendum was announced in order to stabilize the situation. Earlier this month, Thomas Jordan had already noted at a press conference that the SNB would monitor the situation very closely with the intention of stabilizing the market. If no further negative market shocks occur, we expect no significant appreciation of the Swiss franc.

In its quarterly monetary policy assessment of June 16, the SNB maintained the target range for three month LIBOR between -1.25% to -0.25%, as well as leaving the interest rate on sight deposits at the national bank at an unchanged -0.75%. According to statements by the SNB, the Swiss franc remains "...significantly overvalued". The central bank also revised its conditional inflation forecast to a significantly higher level compared to March and now expects the inflation rate to already turn positive in the course of 2016. The reason for the revision is the significant rise in the oil price since March. However, the effect of this oil price increase on annual inflation vanishes after the first quarter of 2017. In the current year the inflation rate is expected to amount to -0.4% on average, 0.4 percentage points higher than according to the March forecast. In 2017 the SNB now expects an inflation rate of 0.3% compared to 0.1% expected in March. The national bank has maintained its inflation projection for 2018 at 0.9%. These estimates assume that three-month LIBOR remains at -0.75% over the entire forecast horizon.

We expect EURCHF to trade in a range between 1.08 and 1.09 in coming weeks, with a slight weakening bias toward the end of the quarter. Over the coming year we expect the Swiss franc to lose slightly more ground against the euro (Q2 2017: 1.12). However, a minimum exchange rate is no longer enforced. Should certain risks become manifest (e.g. geopolitical conflicts, turmoil in the EU), the Swiss franc could once again appreciate rapidly and strongly.

Outlook Q3 2016

Gold in USD 1,320 – 1,380

Partly negative or very low government bond yields support the uptrend in gold

The gold price strengthened by 6.3% in USD terms in the second quarter. In EUR terms the advance amounted to 9.6%. Since the beginning of the year, gold has gained 21.4% in EUR terms.

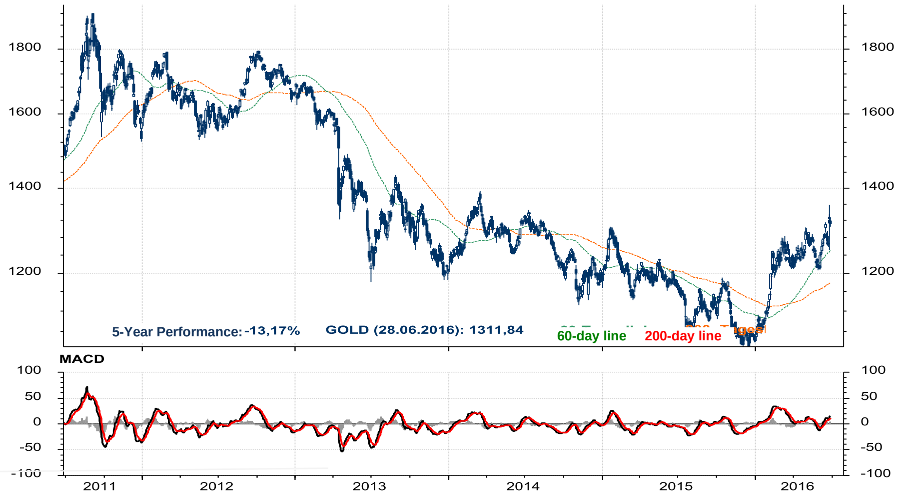
The relative strength of gold vs. global stock markets continued in the second quarter as well. The gold price outperformed all developed market stock indexes and nearly all emerging market stock markets. The uncertainty in the wake of the Brexit referendum in the UK has triggered safe haven flows into gold.

A very important reason for the positive momentum in the gold price is the world-wide low level of interest rates. Partly negative or very low yields on government bonds with long maturities are evidently triggering allocation shifts in investment portfolios. According to the most recent World Gold Council report, demand for gold has increased by 21% this year compared to the previous year.

The monetary policy focus of the ECB and BoJ on “unconventional measures”, which includes negative interest rate policies (NIRP), has amplified investor uncertainty. As a result, investment demand for gold has soared by 122% year-on-year.

The factors underlying the price trend are unlikely to change much in the medium term. Based on this, it appears likely that most global currencies will continue to lose ground relative to gold in coming months. Gold is fulfilling its function as a store of value in the current environment, while most government bonds are no longer doing so.

Gold in USD



Source: Datastream, Erste Group Research

Outlook

Positive price momentum should be maintained in the 3rd quarter as well. We are forecasting gold to trade in a range from approx. USD 1,320 to 1,380 in the 3rd quarter.

Stocks

Outlook Q3 2016

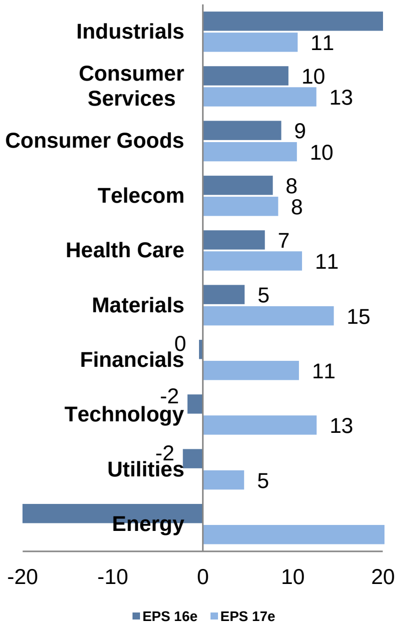
Global 0% to +5%

FTSE World consensus estimates
Earnings and revenue growth (y/y, %)

FTSE Indices	Sales		EPS	
	16e	17e	16e	17e
USA & Canada	**2.1**	**6.3**	**2.5**	**13**
Europe	-0.6	5.8	-1.2	15
Pacific Region	-0.7	3.4	9.6	8.6
EM Asia	6.6	9.9	9.4	14.0
EM LatAm	8.0	8.1	37.9	20.6
EM Europe	-1.5	12	3.1	12.9
World	**0.6**	**5.4**	**2.5**	**13**

Source: Datastream

FTSE World sectors
Earnings estimates (y/y, %)



Source: Datastream

At the end of the second quarter, the FTSE World Index exhibited a gain of +1.7% in EUR terms. In local currency terms the index declined by -2.7%. The FTSE US and the FTSE Japan Index rose by 3.3% and 3.8% respectively. However, the FTSE Europe made a negative contribution to global performance. In the course of the quarter it lost 2.9%. Europe currently has a weighting of 22% in the World Stock Index (US: 56%).

An important aspect with respect to global stock market performance is that emerging markets continued to outperform developed markets. In the second quarter the outperformance of emerging markets amounted to 1%. Since the beginning of the year their relative strength vs. developed markets totals approx. 8%.

The relative strength of emerging markets is primarily based on the fact that consensus expectations for revenue and earnings growth in both 2016 and 2017 exceed those for developed markets. Expected revenue growth amounts to 6.1% this year and 9.8% in the coming year. Expected earnings growth rates for 2016 and 2017 are 14.2%, resp. 15.2%, i.e., higher than the estimates for developed markets. In this respect an important precondition for the continuation of the positive trend of emerging market stock prices is met.

Expected earnings growth rates for developed markets in 2016 and 2017 are significantly lower. Consensus estimates call for earnings growth of 2.5% in 2016 and 13.3% in 2017. The US and Japan should exhibit earnings growth in both years. However, this is not the case for the FTSE Europe in 2016, for which a slight earnings decline of 1.2% is expected this year. Positive earnings momentum is only seen to return to Europe in 2017.

Low interest rates and moderate valuations

The forward P/E ratio of the FTSE World Index for 2016 amounts to 16.8x. This is only slightly above the long term average of 16.1x. A factor that continues to be important for stock markets all over the world is the low level of government bond yields relative to dividend yields. The global 2016 forward dividend yield stands at 2.4%. Government bonds by contrast offer very low or even negative yields (10 yr. US Treasuries are yielding 1.5%, German Bunds -0.14%) and are therefore comparatively unattractive.

Outlook

Earnings prospects for global stocks markets are positive. This applies particularly to the US, the world's largest stock market. Due to an expected earnings decline in 2016 and the uncertainty in the wake of the Brexit decision, the outlook for European stocks is currently worse than that for US stocks. The relative strength of the FTSE US vs. the FTSE Europe should therefore persist. Emerging markets are likely to outperform developed markets due to their stronger earnings momentum. **We expect the global stock market to post a moderate gain in the third quarter in a range of 0% to 5%, amid continued high volatility.**

Global Sectors (1)

Outlook:	➚ Positive
PE 16e	16.1x
EPS 16e	8.7%

Consumer Cyclicals | positive outlook for US stocks
According to consensus estimates the sector will post earnings growth of +8.7% this year. Earnings growth of 6.3% is expected in the US and 16.9% in Europe this year. The sector's global earnings growth rate is expected to accelerate to 10.4% in the coming year. Due to the positive outlook and the political and economic uncertainties triggered by the Brexit vote, US stocks in this sector are currently more attractive than European ones.

Outlook:	➚ Positive
PE 16e	19.4x
EPS 16e	9.5%

Consumer Staples | earnings momentum improves in 2016
The consensus is looking for the sector's earnings to grow by 9.5% this year and 12.6% next year. Thus the sector's expected earnings growth rate exceeds that of the broader market this year. With respect to revenues, growth of 0.8% is expected in the US in 2016 followed by an increase of 11.9% in 2017. Estimated earnings growth rates in Europe amount to 6.4% in 2016e and 11.1% in 2017e. In our opinion stocks in this sector will exhibit relative strength vs. the overall market. This applies especially to Europe, as a result of the uncertainties triggered by the Brexit vote.

Outlook:	➚ Positive
PE 16e	16.7x
EPS 16e	6.9%

Health Care | stable growth industry
Earnings growth in this sector remains high. Consensus estimates call for earnings growth of +6.9% in 2016, resp. +11.0% in 2017. Earnings of US companies should increase by 8.7% this year, those of European ones by 6.0%. We expect this sector to outperform the World Index. Health care stocks should be able to outperform European benchmark indexes in particular, given the current environment of elevated uncertainty.

Outlook:	➔ Neutral
PE 16e	16.8x
EPS 16e	20.0%

Industrials | neutral
The outlook for this sector has improved. According to consensus estimates revenues should increase by 0.8% this year and 3.3% in 2017. Expected earnings growth is far higher. A gain of 20% has been penciled in for 2016, followed by 10.5% in 2017. On account of the strong dependence of stocks in this sector on the economic environment and due to a higher return on equity, US stocks should outperform European ones. Oil service companies should benefit from the rise in oil prices and achieve a moderate degree of outperformance relative to the broad industrial sector.

Outlook:	➚ Positive
PE 16e	16.6x
EPS 16e	-1.7%

Technology | innovation and growth
According to consensus estimates the technology sector is likely to post an earnings decline of 1.7% this year. A moderate decrease in earnings is expected both in the US and Europe. However, revenue growth will likely remain positive (2016e: +2.5%, 2017e:+4.9%). In the coming year earnings are expected to grow by 12.6%. Earnings growth of European technology stocks should be especially strong in 2017, with an estimated gain of 19.2%. We believe the sector will continue to offer positive prospects and upside potential for investors in the medium to long term.

Global Sectors (2)

Outlook:	Negative
PE 16e	51.8x
EPS 16e	-50.0%

Energy (Oil & Gas) | earnings growth expected in the coming year
Earnings prospects for this sector continue to be negative in 2016. The consensus expects an earnings decline of 50% this year. Revenues are expected to fall by approx. 13.9%. According to consensus estimates both revenues and earnings will increase strongly again in the coming year. Revenue growth is expected to amount to 21.2%, earnings growth to 135%. These forecasts are subject to high uncertainty, as they obviously depend on the assumption that oil prices will continue to rise. Should this fail to happen, the risk of price declines will be great. Given a forward P/E of 51.8x for 2016e and 22.1x for 2017e, valuations are quite high.

Outlook:	Negative
PE 16e	16.9x
EPS 16e	4.7%

Commodities | prices of agricultural commodities rise
Developments in different segments of the commodity sector are currently diverging a great deal. Prices of agricultural commodities have recently increased significantly, mainly as a consequence of firmer oil prices. Prices of industrial commodities (primarily base metals, ores) have been stable for approx. 9 months. The sector is expected to post earnings growth of 4.6% this year and 14.5% in 2017. Within the sector we favor the agricultural commodities and chemicals segments. Mining stocks on the other hand are not attractive, with the exception of gold and silver mining stocks.

Outlook:	Negative
PE 16e	14.8x
EPS 16e	-0.4%

Financials | earnings growth in the US significantly higher than in Europe
Earnings of the global sector are expected to decline by 0.4% this year. In the US the consensus expects 2.1% earnings growth in 2016 and 11.7% in 2017. European financial stocks are expected to suffer an 8% decline in earnings this year. The consensus forecast for 2017 is positive though, with an expected growth rate of 15.3%. In view of the low interest rate policy prevailing in Europe and the political and economic uncertainties triggered by the Brexit vote in the UK, the estimate for 2017 appears too high. The volatility of stocks in this sector is likely to remain elevated. The risk/ reward tradeoff appears negative at present.

Outlook:	Neutral
PE 16e	15.6x
EPS 16e	7.8%

Telecoms | US stocks attractive, European ones in most cases not
Globally the sector's revenues are seen to rise by 4.2% this year and 2% in the coming year. Earnings of US companies are expected to grow by 3.5% in 2016 and 5% in 2017. Consensus estimates of earnings growth for companies in Europe are higher, with 5.8% expected in 2016 and 13.8% in 2017. Stocks of European telecommunication companies nevertheless exhibit a far worse long term performance than the global sector. This is primarily due to their low return on equity (RoE) of only 7.5%. US companies will likely achieve an RoE of 19% this year. US telecommunication stocks are therefore attractive, while European ones are not.

Outlook:	Negative
PE 16e	16.2x
EPS 16e	-2.2%

Utilities | lack of prospects in Europe
Globally the sector's earnings should decline by -2.2% in 2016 and rise by 4.6% in 2017. Expected earnings growth in the US is positive both in 2016 and 2017 (+2.8%, resp. +4.1%). In Europe earnings are by contrast forecast to decline by 0.3% in 2016. Investors should avoid stocks of this sector in Europe.

Outlook Q3 2016

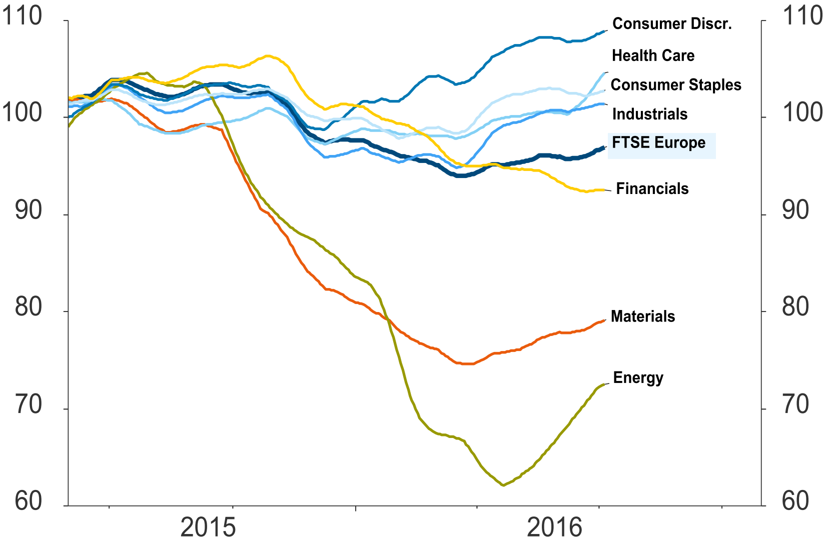
Europe
-5% to 0%

The FTSE Europe posted a negative performance last quarter, declining by -2.9%. Since the beginning of the year it has lost -10%. European stock indexes are therefore lagging significantly behind US and emerging market indexes. Volatility has increased in the wake of the Brexit referendum in the UK.

The underperformance of financial stocks, which have a large weighting in European benchmark indexes, has continued (weighting: 19%). This is unlikely to change in coming months. Consensus estimates for the sector's 2016 earnings growth stand at a clearly negative -8%. The currently expected earnings growth rate of 15.3% for 2017 seems likely to be far too high in view of rising political and economic uncertainties in Europe. Earnings estimates for the sector are currently reduced further, with foreseeable negative consequences for financial sector indexes. Other cyclical sectors such as car manufacturers, leisure & hospitality, retailers and industrial stocks are likely to exhibit heightened volatility and negative performances in the 3rd quarter as well.

Stocks in the consumer staples sector in Europe are most likely to display relative strength vs. other sectors in coming months. An important reason for this is that the sector is less dependent on economic cycles. The sector's expected earnings growth amounts to 16.9% in 2016 and 9.4% in 2017.

Earnings estimates for selected sectors in the FTSE Europe Index over the past 12 months
12 month forward earnings per share, indexed to 100



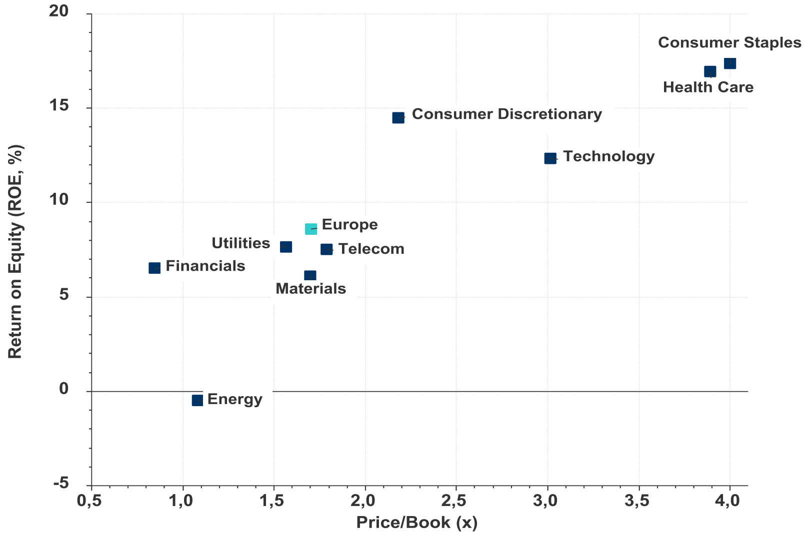
Source: Datastream, Erste Group Research

The health care sector should also significantly outperform the broader market in Europe. Earnings growth prospects are positive in both 2016 and 2017. The sector's EPS growth should amount to 6% in 2016, resp. 8.2% in 2017.

There are also a number of beneficiaries of the outcome of the Brexit referendum in the UK. British companies with a large share of export revenues are benefiting from the weakness of the British pound. Among these are inter alia a number of defensive consumer stocks, as well as shares in the pharmaceutical and technology sectors.

The price-to-book ratio of European stocks currently stands at 1.6x, and the return on equity at 9.3%. Looking at individual sectors in the index, the consumer sectors and the health care sector are stand-outs with a return on equity of approx. 18% each. The valuation of the FTSE Europe is 15.6x based on the 2016 forward P/E ratio. The comparatively high dividend yield of 3.8% reflects the current lack of earnings momentum.

Profitability vs. valuation
European sectors



Source: Datastream, Erste Group Research

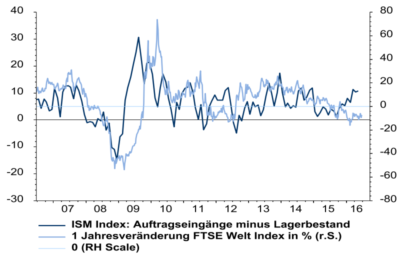
The consensus forecasts an earnings decline of 1.2% for FTSE Europe in 2016. However, corporate earnings growth is expected to rebound again in the coming year with a +14.6% growth rate. As a result, dividends are expected to remain stable in coming quarters.

Outlook
We expect the FTSE Europe to fall between -5% to 0% in the third quarter, coupled with rising volatility. Its relative weakness vs. US benchmark indexes should continue in view of the current lack of earnings growth in Europe. **The most attractive sectors in Europe based on their long-term positive earnings trends are consumer staples, as well as the health care and technology sectors.**

Outlook Q3 2016

USA — 0% to +5%

US: new manufacturing orders minus inventories and the one-year momentum of the FTSE World Index



Sources: Datastream, Erste Group Research

The FTSE US rallied by 3.3% in EUR terms in the second quarter. The S&P 500 Index gained 3.2% in EUR terms, while the Nasdaq Composite advanced by 0.7%. US stock market indexes have outperformed other developed market indexes since the beginning of the year.

Economic sentiment indicators are painting a moderately positive picture. The manufacturing purchasing managers index has improved again. Currently the manufacturing ISM stands at 51.3 points and has been in positive territory for three consecutive months. The important indicator measuring new orders minus inventories is clearly in positive territory as well. In contrast, the ISM non-manufacturing index has recently weakened. The indicator stands at 52.9 points and continues to suggests an expansion of the services sector, which has however slowed in the course of the year.

Corporate profits should increase slightly this year. According to consensus estimates, earnings per share will grow by +1.5% this year, resp. by +13.7% in 2017. Companies are also exhibiting positive top-line growth. Revenue growth is expected to amount to +2% this year and +6.2% in 2017.

Another positive factor is that according to consensus estimates nine of ten sectors should exhibit earnings growth this year. The sectors with the strongest earnings growth are consumer cyclicals (+10.7%), consumer staples (+6.2%) and health care (+8.7%). These sectors should experience an acceleration in earnings growth in the coming year. An earnings decline is only likely to be posted by the energy sector this year. The consensus expectation for this sector is a steep fall in earnings by 69% per share. However, in 2017 energy stocks by contrast are expected to post strong profit growth of 225%. The earnings situation of commodity stocks should stabilize this year (EPS 2016e: +0.5%) and improve significantly in 2017 (EPS 2017e: +14.8%).

The valuations of US benchmark indexes are reasonable against the background of low bond yields and expected earnings growth. The dividend yield of the S&P 500 currently amounts to 2.2%, the 2016 forward dividend yield of the FTSE US stands at 1.8%. Dividend yields are therefore higher than yields on US treasuries. The forward P/E ratio of the FTSE US stands at 18.4x for 2016e, and 16.2x for 2017e. Given that valuations are not exactly low either, we are looking for the benchmark indexes to post annual gains roughly in line with annual earnings growth. In this context it has to be kept in mind that particularly the consensus estimates for 2017 will in all probability be reduced over time.

Outlook:
We are forecasting a mildly positive performance for the S&P 500 Index in the 3rd quarter. Due to elevated political and economic uncertainties in Europe, US stock are likely to continue to exhibit relative strength vs. European stocks. **We expect the market to post a gain within a range of 0% to 5%.**

Outlook Q3 2016

CEE ↗ 0% to +5%

In the wake of the Brexit shock, stock markets in the CEE region have suffered sharp declines similar to all other markets, and have subsequently exhibited similar rebounds as well. In the emerging markets sector the region naturally has the greatest exposure, given that most countries of the region are already members of the European Union.

Since it is currently still far from clear when and how a Brexit will be implemented, the associated uncertainty remains a significant stress factor. We have revised our GDP growth estimates for the CEE region, from 3.1% to 2.9% in 2016 and from 3.3% to 3.0% in 2017, with foreign trade the main factor driving the downward revision.

In view of the current situation it seems fairly certain that the low interest rate environment will continue to persist and that the Fed will probably refrain from rate hikes in the near future as well. This environment prompts us to focus specifically on real dividend yields. Particularly the Czech market is a stand-out in this respect, but Austria and Romania offer attractive real dividend yields as well.

In terms of our country allocation we are taking a positive view on Hungary and the Czech Republic. Even though the Hungarian market may appear relatively expensive by now, its valuation is justified by strong earnings growth rates. The Czech Republic is primarily of interest due to its defensive qualities, but companies are in the meantime exhibiting positive earnings growth momentum as well. We like Turkey's stock market even though it cannot impress with respect to real dividends. Its price/ earnings to growth ratio remains the most attractive in the region, even though earnings momentum is weaker than in the other markets – albeit still strong in absolute terms with 17% over a 12 month time horizon. Politically there has been a lot of movement with respect to Turkey's relationship with Russia and Israel. However, the suspension of Russian sanctions is unlikely to revive the weak tourism industry in the short term. The terror attacks of recent months are weighing heavily on the sector. Fundamental qualities could however well come to the fore again in the current environment, as the highly likely postponement of the planned Fed rate hike is definitely positive for Turkey.

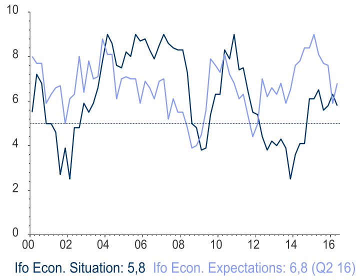
We like the Russian stock market more and more, even though it has already delivered quite an impressive performance, inter alia due to the rise in oil prices since February. Valuations are no longer quite as favorable as they once were, but in the meantime there are tangible signs of recovery in evidence, both in general macroeconomic terms, as well as with respect to corporate earnings growth.

Due to ongoing political uncertainty, we would be inclined to assign a neutral weighting to Poland. Recent news regarding plans to reform the pension system could definitely have a positive impact though. However, we remain cautious with respect to the country's fundamentals.

Outlook Q3 2016

India 0% to +5%

India: IFO Indexes



Source: Datastream

The FTSE India Index has gained 5.2% in EUR terms in the second quarter. Its performance since the beginning of the year amounts to +1.4% in local currency terms and -3% in EUR terms.

The IFO business climate indexes are clearly in positive territory above the level of 5 points. While the assessment of current conditions has slightly worsened, the index of economic expectations has improved from 6.3 to 6.8 points in the course of the quarter.

According to consensus estimates the outlook for revenue and earnings growth for the FTSE India is quite positive. Corporate revenues are expected to rise by 11% in 2016 and by 13.4% in 2017. Earnings per share growth should be even stronger. Corporate earnings are expected to grow by 24.9% this year, resp. by 22.6% in the coming year.

The forward P/E ratio amounts to 17.6x for 2016 and to 14.4x for 2017. The 2016 forward dividend yield stands at 1.7%. India's higher valuation compared to other emerging markets is due to the above average growth momentum and high profitability of Indian companies (RoE 2016e 14.2%).

Outlook:
We expect the recent positive trend in India's stock market to continue in the third quarter as well. The performance of the FTSE India should be within a range of 0% to +5%.

Outlook Q3 2016

China | Hong Kong 0% to +5%

China: IFO indexes

Source: Datastream

The FTSE China Index fell by 1.9% in EUR terms in the second quarter. Since the beginning of the year it has declined by -9.3% in EUR terms. With that the FTSE China Index is the only stock market index in the BRIC nations that has posted a negative performance in this time period.

According to the IFO Index, current economic conditions are seen as negative at present. However, a small improvement can be discerned in a semi-annual comparison. The more important expectations component is back in neutral territory.

Expected earnings growth for the FTSE China stands at 11.2% for 2016 and 13.9% for 2017. According to consensus estimates, companies should also be able to boost top-line growth considerably. Revenues are expected to rise by 9.4% in 2016 and by an additional 12.2% in 2017. The forward P/E ratio is 15.9x for 2016, and 13.8x for 2017. The 2016 forward dividend yield is 2%. This is lower than the average dividend yield of the FTSE Emerging Markets Index, which amounts to 3%.

Outlook:
We expect China's benchmark indexes to trend higher. Our forecast calls for a moderate advance in the FTSE China Index in the 3rd quarter of between 0% to 5%.

Outlook Q3 2016

Brazil 0% to +5%

Brazilian real vs. USD: downtrend has ended for the time being
BRL/USD:

Source: Datastream, Erste Group Research

The recovery in commodity prices has facilitated the positive performance of the FTSE Brazil Index, which advanced by 14.4% in EUR terms in the 2nd quarter. The recovery in the Brazilian real contributed to the positive showing as well. With a gain of 38.5% in EUR terms since the beginning of the year, Brazilian stocks posted the strongest performance among the stock markets of the BRIC countries. Its outperformance vs. developed markets is glaring and probably not yet over.

The outlook for corporate earnings is positive. According to consensus estimates, earnings growth of 41% is expected for the MSCI Brazil Index this year. In 2017 earnings are also expected to rise strongly, with an estimated gain of 23.7%. Revenues are likewise seen to increase substantially. The expected increase is +7.1% in 2016 and +9.1% in 2017.

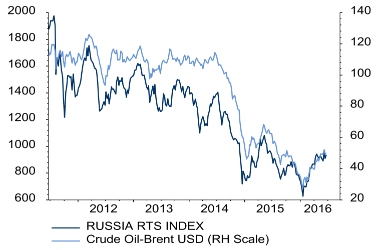
Brazilian stocks trade at moderate valuations after several years of declines in Brazil's benchmark indexes. The forward dividend yield for 2016 stands at 3.8% and the forward P/E ratio for 2016 stands at 13.7x. In view of the positive earnings outlook, current valuations leave room for a continuation of the stock market rally.

The momentum of the uptrend is likely to slow in coming months, primarily due to the strong returns achieved in the first half of the year. **We expect that the FTSE Brazil will achieve a gain at the lower end of a range from 0% to +5% in the 3rd quarter**.

Outlook Q3 2016

Russia -5% to 0%

Russia RTS Index and the oil price:



Source: Datastream, Erste Group Research

The FTSE Russia Index rose by 6.9% in the second quarter. Similar to the first quarter, the positive performance was largely driven by rising oil prices. The slow recovery of the economy has supported the financial sector and its earnings as well.

Consensus estimates of earnings trends are positive. Expected earnings growth for the FTSE Russia is 2.8% in 2016. Estimated earnings growth for the coming year stands at 14.7%. With respect to revenue growth, sales of companies in the FTSE Russia are expected to decline by 4.2% this year, and increase by 13.2% in 2017. Valuations of listed companies remain low. Thus the forward dividend yield for 2016 amounts to 3.8% and the forward P/E ratio to 7x.

Following the 18% rally in the FTSE Russia in EUR terms since the beginning of the year, the Russian stock market seems likely to consolidate in the summer months. **Seasonal trends in the oil price, resp. in the FTSE Russia Index, argue in favor of a moderate stock market correction targeting the upper end of a range from -5% to 0%.**

Tables & Appendix

Economic indicators

		GDP (% yoy)			Inflation (% yoy)		Un-employ. (%)		CA Balance (% GDP)		Fiscal Balance (% GDP)		Gross Debt (% GDP)	
		15	16e	17e	16e	17e	16e	17e	16e	17e	16e	17e	16e	17e
Europe	**Eurozone**	1.5	**1.3**	**1.6**	0.3	1.5	10.3	9.9	3.5	3.2	-1.9	-1.5	92.5	91.3
	Germany	1.5	**1.3**	**1.7**	0.5	1.4	4.6	4.8	8.4	8.0	0.1	0.1	68.2	65.9
	France	1.1	**1.3**	**1.6**	0.4	1.1	10.1	10.0	0.6	0.3	-3.4	-2.9	98.2	98.8
	Spain	3.2	**2.6**	**2.3**	-0.4	1.0	19.7	18.3	1.9	2.0	-3.4	-2.5	99.0	98.5
	Italy	0.8	**1.2**	**1.6**	0.2	0.7	11.4	10.9	2.3	2.0	-2.7	-1.6	133.0	131.7
	Austria	0.9	**1.5**	**1.7**	1.1	1.6	6.1	6.2	3.1	3.2	-1.6	-1.5	84.3	82.6
	UK	2.2	**1.9**	**2.2**	0.8	1.9	5.0	5.0	-4.3	-4.0	-3.2	-2.2	89.1	87.9
	Switzerland	0.9	**1.4**	**1.8**	-0.8	0.1	3.6	3.5	9.3	8.8	-0.3	-0.2	44.9	44.1
Eastern Europe	**Russia**	-3.7	**-1.8**	**0.8**	8.4	6.5	6.5	6.3	4.2	5.1	-4.4	-3.0	18.4	19.4
	Poland	3.6	**3.3**	**3.5**	-0.6	0.9	9.3	8.7	-0.7	-1.4	-2.9	-3.1	51.9	52.4
	Turkey	3.8	**3.8**	**3.4**	9.8	8.8	10.8	10.5	-3.6	-4.1	-1.9	-1.3	30.7	29.2
	Czech Rep.	4.3	**2.2**	**2.5**	0.6	1.3	4.1	4.2	0.9	0.9	-1.1	-1.0	40.0	39.1
	Romania	3.8	**4.1**	**3.6**	-0.9	1.7	6.7	6.7	-2.2	-2.5	-2.9	-3.5	40.6	42.3
	Hungary	2.9	**2.0**	**2.8**	0.6	2.0	5.5	5.2	4.9	4.7	-2.2	-2.7	75.1	74.3
	Slovakia	3.6	**3.1**	**3.1**	-0.3	1.2	10.0	9.3	0.0	0.7	-2.5	-2.0	53.0	53.2
Americas	**USA**	2.4	**2.1**	**2.3**	1.4	1.9	4.9	4.8	-2.9	-3.3	-3.8	-3.7	107.5	107.5
	Canada	1.2	**1.5**	**1.9**	1.3	1.9	7.3	7.4	-3.5	-3.0	-2.4	-1.8	92.3	90.6
	Brazil	-3.8	**-3.8**	**0.0**	8.7	6.1	9.2	10.2	-2.0	-1.5	-8.7	-8.5	76.3	80.5
	Chile	2.1	**1.5**	**2.1**	4.1	3.0	6.8	7.5	-2.1	-2.7	-3.0	-3.0	19.8	22.5
	Mexico	2.5	**2.4**	**2.6**	2.9	3.0	4.0	3.9	-2.6	-2.6	-3.5	-3.0	54.9	54.9
	Argentina	1.2	**-1.0**	**2.8**	NA	19.9	7.8	7.4	-1.7	-2.2	-6.4	-5.5	60.7	60.9
	Colombia	3.1	**2.5**	**3.0**	7.3	3.4	9.8	9.4	-6.0	-4.3	-3.1	-2.7	49.3	48.0
Asia	**China**	6.9	**6.5**	**6.2**	1.8	2.0	4.1	4.1	2.6	2.1	-3.1	-2.7	46.8	49.3
	Japan	0.5	**0.5**	**-0.1**	-0.2	1.2	3.3	3.3	3.8	3.7	-4.9	-3.9	249.3	250.9
	India	7.3	**7.5**	**7.5**	5.3	5.3	na	na	-1.5	-2.1	-7.0	-6.7	66.5	65.6
	Indonesia	4.8	**4.9**	**5.3**	4.3	4.5	5.9	5.7	-2.6	-2.8	-2.7	-2.8	27.6	28.4
	South Korea	2.6	**2.7**	**2.9**	1.3	2.2	3.5	3.3	8.2	7.4	0.3	0.5	37.3	37.5
	Thailand	2.8	**3.0**	**3.2**	0.2	2.0	0.8	0.7	8.0	5.7	-0.4	-0.5	43.7	44.5
	Australia	2.5	**2.5**	**3.0**	2.1	2.4	5.9	5.8	-3.6	-3.5	-2.4	-1.5	39.1	40.0
	South Africa	1.3	**0.6**	**1.2**	6.5	6.3	26.1	26.7	-4.4	-4.9	-3.8	-3.6	51.4	52.1
	World	3.1	**3.2**	**3.5**										

Source: IMF, EU Commission, Erste Group Research estimates

Forecasts

GDP	2013	2014	2015	2016	2017
Eurozone	-0.5	0.9	1.5	1.3	1.6
US	1.9	2.4	2.4	1.9	1.9

Inflation	2013	2014	2015	2016	2017
Eurozone	1.3	0.5	0.1	0.3	1.5
US	1.5	1.6	0.1	1.3	1.9

	current	Sep-16	Dec-16	Mar-17	Jun-17
EURUSD	1.11	1.12	1.10	1.12	1.14
EURCHF	1.08	1.10	1.11	1.11	1.12

	current	Sep-16	Dec-16	Mar-17	Jun-17
ECB MRR	0.00	0.00	0.00	0.00	0.00
3M Euribor	-0.29	-0.25	-0.25	-0.25	-0.22
Germany Govt. 10Y	-0.11	0.10	0.50	0.90	1.20
Swap 10Y	0.36	0.40	0.80	1.20	1.50

	current	Sep-16	Dec-16	Mar-17	Jun-17
Fed Funds Target Rate*	0.30	0.38	0.63	0.88	1.13
3M Libor	0.65	0.66	0.94	1.19	1.44
US Govt. 10Y	1.47	1.60	2.10	2.40	2.80
EURUSD	1.11	1.12	1.10	1.12	1.14

*Mid of target range

	current	Sep-16	Dec-16	Mar-17	Jun-17
Austria 10Y	0.20	0.30	0.70	1.10	1.40
Spread AT - DE	0.31	0.20	0.20	0.20	0.20

Source: Bloomberg, Erste Group Research

Consensus estimates

	FTSE Index	Market Cap. (bn EUR)	Weight (%) World	Tot. Return in EUR (%) 1M	3M	YTD	Tot. Return local (%) 1M	3M	YTD	DY (%) 16e	P/CF (x) 16e	P/B (x) 16e	PE (x) 16e	17e	Sales (y/y, %) 16e	17e	EPS (y/y, %) 16e	17e
	World	**30,490**	**100.0**	**-1.7**	**1.6**	**-1.8**	**-2.3**	**0.3**	**-1.2**	**2.4**	**10.0**	**1.8**	**16.8**	**14.9**	**0.6**	**5.4**	**2.5**	**13.3**
Advanced Markets	**North America**	**17,816**	**58.4**	**-0.9**	**2.4**	**0.7**	**-1.2**	**1.6**	**2.5**	**1.8**	**11.8**	**2.2**	**18.4**	**16.1**	**2.1**	**6.3**	**0.9**	**14.0**
	Canada	908	3.0	-0.6	5.6	12.4	-1.1	3.5	7.4	3.1	9.4	1.8	17.6	14.6	4.6	7.3	-8.3	20.4
	USA	16,908	55.5	-0.9	2.2	0.1	-1.2	1.5	2.3	1.7	12.0	2.2	18.4	16.2	2.0	6.2	1.4	13.7
	Europe	**6,840**	**22.4**	**-5.9**	**-0.8**	**-7.6**	**-3.8**	**0.7**	**-4.3**	**3.8**	**8.8**	**1.6**	**15.6**	**13.6**	**-0.6**	**5.8**	**-1.2**	**14.6**
	Austria	18	0.1	-9.4	-6.5	-14.2	-9.4	-6.5	-14.2	3.4	4.1	0.8	11.1	9.4	-5.4	7.1	-11.5	18.7
	Belgium	157	0.5	-2.9	2.6	-4.1	-2.9	2.6	-4.1	3.3	8.9	1.5	14.5	13.8	4.5	3.3	16.7	5.5
	Denmark	209	0.7	-5.0	0.8	-4.3	-5.0	0.5	-4.6	2.3	14.1	3.4	20.1	17.4	3.2	5.3	13.9	15.5
	Finland	108	0.4	-1.3	0.3	-8.1	-1.3	0.3	-8.1	4.4	16.4	1.9	17.1	14.9	18.0	3.4	-17.6	14.5
	France	964	3.2	-6.6	-1.6	-6.7	-6.6	-1.6	-6.7	3.7	8.2	1.4	14.6	13.2	-1.1	5.5	-1.1	11.1
	Germany	917	3.0	-6.2	-2.2	-9.8	-6.2	-2.2	-9.8	3.2	8.1	1.5	13.1	11.8	0.7	3.4	5.8	11.5
	Greece	12	0.0	-21.0	-6.4	-29.5	-21.0	-6.4	-29.5	4.1	5.7	1.4	11.8	11.1	2.9	11.9	3.5	6.5
	Ireland	23	0.1	-14.2	-12.9	-17.2	-14.2	-12.9	-17.2	1.5	10.9	2.0	16.3	14.7	0.9	4.0	16.6	10.8
	Italy	216	0.7	-11.4	-9.1	-22.7	-11.4	-9.1	-22.7	4.7	4.4	0.8	13.8	10.7	1.4	6.4	25.3	28.8
	Netherlands	316	1.0	-7.0	-3.7	-3.9	-7.0	-3.7	-4.0	3.8	7.7	1.4	14.3	12.8	3.4	4.6	0.7	12.0
	Norway	64	0.2	-3.6	7.0	2.6	-3.2	5.1	-0.5	4.9	5.6	1.3	14.7	12.2	-8.1	9.3	-15.1	20.4
	Portugal	17	0.1	-5.9	-2.8	-4.4	-5.9	-2.8	-4.4	4.0	6.1	1.1	12.5	10.4	-0.6	3.0	5.2	20.8
	Spain	311	1.0	-10.5	-5.8	-12.7	-10.5	-5.8	-12.7	5.1	4.4	1.0	14.1	11.0	-1.4	5.0	-10.7	28.7
	Sweden	293	1.0	-6.1	-2.2	-7.6	-4.6	-0.4	-4.8	4.6	11.4	2.0	14.7	13.5	-2.3	3.6	-7.5	9.2
	Switzerland	987	3.2	-2.5	4.1	-6.0	-4.0	3.8	-5.9	3.5	14.7	2.4	17.7	15.9	0.1	4.0	0.0	11.6
	United Kingdom	2,130	7.0	-6.0	0.4	-6.6	1.4	5.1	4.1	4.1	9.4	1.8	16.9	14.5	-2.6	8.2	-5.4	16.6
	Pacific	**5,106**	**16.7**	**0.1**	**1.2**	**-3.8**	**-4.4**	**-4.4**	**-10.3**	**2.9**	**7.3**	**1.2**	**13.5**	**12.5**	**-0.7**	**3.4**	**9.6**	**8.6**
	Japan	2,670	8.8	-0.9	0.6	-7.5	-7.6	-9.6	-19.3	2.4	6.8	1.1	13.2	12.2	-0.9	2.8	14.7	8.8
	Hong Kong	391	1.3	0.8	2.0	-3.3	0.4	1.3	-1.1	3.6	10.3	1.0	14.0	13.4	-1.7	6.5	2.5	5.4
	Singapore	149	0.5	2.0	1.6	1.4	-0.4	-0.6	-1.6	4.2	10.1	1.1	12.7	12.1	-2.9	6.8	1.0	5.5
	Australia	779	2.6	-1.3	2.6	-1.0	-4.8	3.6	-1.0	4.5	9.1	1.8	16.9	15.9	-8.5	1.2	-14.0	5.7
	Korea	487	1.6	2.5	0.1	0.3	0.6	-1.0	1.4	1.7	5.6	1.0	11.4	10.3	6.9	5.6	24.5	10.4
Emerging Markets	**Emerging Markets**	**2,792.2**	**9.2**	**3.5**	**4.2**	**4.2**	**1.5**	**2.4**	**4.1**	**2.8**	**8.4**	**1.7**	**14.7**	**12.6**	**6.1**	**9.8**	**14.2**	**15.2**
	EM Asia	**1,786.9**	**5.9**	**2.7**	**3.5**	**-0.9**	**2.3**	**2.9**	**0.7**	**2.5**	**9.7**	**1.7**	**15.3**	**13.2**	**6.6**	**9.9**	**9.4**	**14.0**
	China	703	2.3	2.7	2.9	-7.5	2.3	2.2	-5.3	2.0	11.1	1.8	15.9	13.8	9.4	12.2	11.2	13.9
	India	348	1.1	0.2	6.0	-2.2	0.9	7.1	2.3	1.7	10.4	2.2	17.6	14.4	11.0	13.4	24.9	22.6
	Indonesia	79	0.3	8.0	8.1	14.0	4.3	5.4	11.2	2.2	12.3	2.5	17.4	15.0	3.5	6.7	14.6	16.0
	Malaysia	120	0.4	1.8	-3.5	3.0	0.5	-3.2	-1.0	3.3	10.3	1.3	18.7	14.7	5.4	6.4	-9.7	9.7
	Taiwan	404	1.3	4.2	3.2	4.9	3.4	1.6	5.6	4.1	8.7	1.6	14.4	13.1	0.1	5.7	0.4	11.0
	Thailand	76	0.2	2.2	3.9	15.9	0.7	2.5	15.9	3.2	8.7	1.9	16.0	14.1	4.3	10.8	8.1	13.8
	EM Europe	**245**	**0.8**	**-0.8**	**1.7**	**10.8**	**-1.3**	**2.0**	**12.9**	**4.4**	**4.7**	**0.9**	**8.7**	**7.9**	**-1.5**	**11.8**	**3.1**	**12.9**
	Czech Republic	6	0.0	-4.5	-1.8	-2.4	-4.2	-1.6	-2.1	7.0	6.1	1.2	12.7	13.8	-3.0	-0.3	-10.5	-8.0
	Hungary	9	0.0	-3.2	1.4	10.3	-2.6	2.3	10.6	3.0	4.9	1.2	11.9	10.3	-12.0	12.5	13.5	16.0
	Poland	39	0.1	-4.5	-13.3	-8.1	-3.9	-9.8	-5.3	3.8	6.0	1.0	12.3	11.9	-1.7	7.2	-6.1	4.5
	Russia	134	0.4	2.2	10.6	19.2	2.0	9.7	21.8	5.9	3.8	0.7	7.0	6.2	-4.2	13.2	2.8	14.7
	Turkey	46	0.2	1.5	-4.1	9.0	-0.9	-3.8	10.4	0.4	6.0	1.1	9.7	8.3	8.9	13.0	11.4	16.6
	EM Latin America	**461**	**1.5**	**8.9**	**6.5**	**21.0**	**2.0**	**0.5**	**13.2**	**3.1**	**5.4**	**1.8**	**15.5**	**12.9**	**8.0**	**8.1**	**37.9**	**20.6**
	Brazil	247	0.8	16.8	14.2	40.5	4.3	0.0	17.5	3.8	7.4	1.5	13.7	11.1	7.1	9.1	41.0	23.7
	Chile	41	0.1	5.7	5.6	13.7	1.3	1.3	8.2	3.5	9.9	1.4	11.5	11.0	-0.8	8.1	12.2	4.6
	Colombia	19	0.1	6.7	7.4	22.7	0.9	1.6	15.0	2.1	4.8	1.3	17.4	12.0	25.0	11.2	4.5	45.4
	Mexico	145	0.5	-1.4	-5.3	-2.6	-1.3	-0.5	6.8	2.1	NA	2.3	19.7	16.8	9.7	6.3	41.4	16.9
	Peru	9	0.0	8.2	29.6	68.2	6.0	25.2	66.1	1.9	18.2	2.2	13.8	12.6	10.9	5.2	84.6	14.3
	World																	
Sectors	Materials	1,350	4.4	-0.4	2.4	3.4	-1.2	1.0	2.9	2.6	8.2	1.6	16.9	14.8	-6.5	4.6	4.7	14.5
	Industrials	3,765	12.3	-1.9	1.1	0.6	-2.8	-0.6	0.3	2.4	10.6	2.3	16.8	15.2	0.8	3.3	20.0	10.5
	Consumer Goods	4,388	14.4	-0.5	1.3	-0.6	-1.3	-0.4	-0.8	2.6	10.8	2.5	16.1	14.5	1.3	3.9	8.7	10.4
	Consumer Services	3,496	11.5	-1.4	-0.7	-3.0	-2.1	-2.0	-2.2	1.8	11.3	3.4	19.4	17.2	6.0	5.1	9.5	12.6
	Technology	3,434	11.3	-2.8	-2.4	-3.7	-3.2	-3.4	-2.3	1.9	11.5	3.1	16.6	14.7	2.5	5.0	-1.7	12.6
	Telecom	1,130	3.7	2.4	3.1	7.1	1.7	1.6	7.3	4.2	5.4	2.2	15.6	14.4	4.2	2.0	7.8	8.4
	Health Care	3,650	12.0	0.1	6.4	-3.3	-0.3	5.4	-2.2	2.1	14.7	3.3	16.7	15.1	7.2	5.8	6.9	11.0
	Utilities	1,102	3.6	3.7	4.9	10.7	3.5	3.9	11.7	3.8	6.8	1.6	16.2	15.5	-0.4	2.4	-2.2	4.6
	Energy	2,046	6.7	2.9	11.0	12.6	3.5	10.8	15.0	3.6	9.1	1.5	51.8	22.1	-13.9	21.2	-50.0	134.6
	Financials	6,128	20.1	-6.3	-1.0	-9.6	-6.9	-2.0	-9.3	2.1	8.9	1.1	14.8	13.4	1.9	3.8	-0.4	10.7
	World	**30,490**	**100.0**	**-1.7**	**1.6**	**-1.8**	**-2.3**	**0.3**	**-1.2**	**2.4**	**10.0**	**1.8**	**16.8**	**14.9**	**0.6**	**5.4**	**2.5**	**13.3**

Source: Datastream, FTSE, IBES, Erste Group Research Calculations.

Contacts

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