BREVAN HOWARD

BH GLOBAL LIMITED

MONTHLY SHAREHOLDER REPORT:
DECEMBER 2016

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MONTHLY SHAREHOLDER REPORT: DECEMBER 2016

BREVAN HOWARD

www.bhglobal.com

BH Global Limited

Manager:
Brevan Howard Capital Management LP ("BHCM")

Administrator:
Northern Trust International Fund Administration Services (Guernsey) Limited ("Northern Trust")

Joint Corporate Brokers:
J.P. Morgan Cazenove
Canaccord Genuity Ltd.

Listings:
London Stock Exchange (Premium Listing)
NASDAQ Dubai - USD Class (Secondary Listing)
Bermuda Stock Exchange (Secondary Listing)

Overview:

BH Global Limited ("BHG") is a closed-ended investment company, registered and incorporated in Guernsey on 25 February 2008 (Registration Number: 48555).

Prior to 1 September 2014, BHG invested all its assets (net of short-term working capital) in Brevan Howard Global Opportunities Master Fund Limited ("BHGO"). With effect from 1 September 2014, BHG changed its investment policy to invest all its assets (net of short-term working capital) in Brevan Howard Multi-Strategy Master Fund Limited ("BHMS" or the "Fund") a company also managed by BHCM.

BHG was admitted to the Official List of the UK Listing Authority and to trading on the Main Market of the London Stock Exchange on 29 May 2008.

BHMS has the ability to allocate capital to investment funds and directly to the underlying traders of Brevan Howard affiliated investment managers. The Direct Investment Portfolio (the "DIP") is the allocation of BHMS' assets to individual trading books. The BHMS allocations are made by an investment committee of BHCM who draw upon the resources and expertise of the entire Brevan Howard group.

Total Assets: $453 mm[1]

1. As at 30 December 2016 by BHG's administrator, Northern Trust.

Summary Information

BH Global Limited NAV per share (as at 30 December 2016)

Shares Class	NAV (USD mm)	NAV per Share
USD Shares	59.4	14.19
GBP Shares	393.6	14.33

BH Global Limited NAV per Share* % Monthly Change

USD	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2008						1.16*	0.10	0.05	-3.89	1.13	2.74	0.38	1.55
2009	3.35	1.86	1.16	1.06	2.79	-0.21	1.07	0.27	1.49	0.54	0.11	0.04	14.31
2010	0.32	-0.85	-0.35	0.53	-0.06	0.60	-0.79	0.80	1.23	0.39	-0.21	-0.06	1.54
2011	0.09	0.42	0.34	1.20	0.19	-0.56	1.61	3.51	-1.29	-0.14	0.19	-0.88	4.69
2012	1.22	1.02	-0.54	-0.10	-0.65	-1.53	1.46	0.70	1.47	-0.72	0.81	1.26	4.44
2013	1.33	0.49	0.33	1.60	-0.62	-1.95	-0.14	-0.86	0.09	-0.13	0.95	0.75	1.79
2014	-0.98	-0.04	-0.26	-0.45	0.90	0.70	0.60	0.05	1.56	-0.75	0.71	0.44	2.49
2015	3.37	-0.41	0.35	-1.28	1.03	-1.49	-0.06	-1.56	-0.58	-0.67	3.06	-3.31	-1.73
2016	0.82	1.03	-0.83	-0.66	0.28	1.71	0.13	0.10	-0.23	0.47	3.62	0.82	7.42

GBP	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2008						1.40*	0.33	0.40	-4.17	1.25	3.27	0.41	2.76
2009	3.52	1.94	1.03	0.68	2.85	-0.28	1.05	0.31	1.51	0.58	0.12	0.08	14.15
2010	0.35	-0.93	-0.32	0.58	-0.04	0.62	-0.81	0.84	1.17	0.37	-0.20	-0.03	1.61
2011	0.10	0.41	0.38	1.13	0.04	-0.59	1.69	3.67	-1.41	-0.15	0.21	-0.84	4.65
2012	1.23	1.05	-0.51	-0.08	-0.62	-1.51	1.50	0.70	1.44	-0.72	0.72	1.31	4.55
2013	1.36	0.56	0.36	1.63	-0.48	-1.91	-0.11	-0.84	0.14	-0.11	0.97	0.77	2.32
2014	-0.97	-0.14	-0.33	-0.30	0.56	0.48	0.42	0.03	1.85	-0.76	0.78	0.48	2.09
2015	3.48	-0.34	0.33	-1.26	1.18	-1.50	-0.03	-1.44	-0.64	-0.79	3.02	-3.16	-1.32
2016	0.91	1.08	-1.04	-0.65	0.24	1.46	0.13	-0.14	-0.34	0.59	3.28	0.96	6.60

Source: Fund NAV data is provided by the administrator of BHMS, International Fund Services (Ireland) Limited ("IFS"). BHG NAV and NAV per Share data is provided by BHG's administrator, Northern Trust. BHG NAV per Share % Monthly Change calculations are made by BHCM. BHG NAV data is unaudited and net of all investment management and performance fees and all other fees and expenses payable by BHG. NAV performance is provided for information purposes only. Shares in BHG do not necessarily trade at a price equal to the prevailing NAV per Share.

* Performance is calculated from a base NAV per Share of 10 in each currency. The opening NAV in May 2008 was 9.9 (after deduction of the IPO costs borne by BHG).

Data as at 30 December 2016.

PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS

ASC 820 Asset Valuation Categorisation*

Brevan Howard Multi-Strategy Master Fund Limited

Unaudited as at 30 December 2016

	% of Gross Market Value* on a non-look through basis
Level 1	44.6
Level 2	28.7
Level 3	2.2
At NAV	24.5

Source: BHCM, sum may not total 100% due to rounding.

* This data is unaudited and has been calculated by BHCM using the same methodology as that used in the most recent audited financial statements of the Fund.

Level 1: This represents the level of assets in the portfolio which are priced using unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: This represents the level of assets in the portfolio which are priced using either (i) quoted prices that are identical or similar in markets that are not active or (ii) model-derived valuations for which all significant inputs are observable, either directly or indirectly in active markets.

Level 3: This represents the level of assets in the portfolio which are priced or valued using inputs that are both significant to the fair value measurement and are not observable directly or indirectly in an active market.

At NAV: This represents the level of assets in the portfolio that are invested in other funds and priced or valued at NAV as calculated by IFS.

	% of Gross Market Value* on a look through basis
Level 1	57.8
Level 2	40.4
Level 3	1.8

Source: BHCM

* This data reflects the combined ASC 820 levels of the underlying allocations (Funds and DIP portfolio) in which the Fund is invested, proportional to each of the underlying allocation's weighting in the Fund's portfolio. The data is unaudited and has been calculated by BHCM using the same methodology as that used in the most recent audited financial statements of the underlying funds. The relative size of each category is subject to change. Sum may not total 100% due to rounding.

Level 1: This represents the level of assets in the portfolio which are priced using unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

Level 2: This represents the level of assets in the portfolio which are priced using either (i) quoted prices that are identical or similar in markets that are not active or (ii) model-derived valuations for which all significant inputs are observable, either directly or indirectly in active markets.

Level 3: This represents the level of assets in the portfolio which are priced or valued using inputs that are both significant to the fair value measurement and are not observable directly or indirectly in an active market.

2016 Portfolio Update

The information in this section has been provided to BHG by BHCM.

The NAV per share of the USD shares appreciated by 4.96% during the fourth quarter of 2016. It was the second highest quarterly return since inception and the return was driven by macro trading in FX and interest rates with additional gains from credit and equity index trading. Systematic trading was a small detractor.

In interest rates the bulk of the gains during the fourth quarter were generated in EUR and USD. In USD the Fund benefitted from its exposure to higher USD interest rates following the US election. In FX, most gains arose from long exposure to the USD against a basket of currencies including the GBP and JPY. Additional gains arose in equity index trading where most profits came from long exposure to the S&P during December. In credit, the Fund made gains across MBS/ABS and corporate credit trading with additional gains in agency trading. In systematic trading the main negative driver was the strategy's long exposure to interest rates at the beginning of the quarter.

During 2016, the NAV per share of the USD shares appreciated by 7.42% and the NAV per share of the GBP shares appreciated by 6.60%. The returns were accompanied by a modest volatility of 4.1% and a maximum monthly drawdown of 1.51%. The performance compares favourably to the HFRI Macro Multi-Strat Index, which returned 4.05% for the year.

All of the underlying funds and the Direct Investment Portfolio ("DIP") contributed to the Fund's 2016 performance, with the DIP generating the bulk of the profits. The DIP is the area of the portfolio whereby the Investment Committee has the ability to allocate directly to underlying traders. For the full year the DIP was up 14.38% (gross) and the predominant contributor. The majority of the performance drivers are described below in the context of the overall Fund. The outperformance of the DIP compared to other underlying allocations was due to its increased exposures to some of the positions and trading areas, where credit and FX stood out as key contributors.

2016 was a year of significant political developments. In the UK, the decision to leave the EU was a shock to many, and in the US, Donald Trump won the presidential election against expectations. Both events created uncertainty and significant market moves, which resulted in solid trading profits.

Looking at the different trading areas, trading in interest rates was the largest contributor over the year. Profits were generated across a number of markets with key drivers being the Fund's long exposure to EUR interest rates at the start of 2016, both long and short exposures to GBP rates around Brexit and short exposure to USD rates following the US election. Additional gains arose in some smaller markets including New Zealand, Hungary and Canada.

Credit was the second largest contributor to overall profits. Gains were driven by RMBS positions on the back of strong underlying fundamentals and demand for yield by market participants. Additional significant gains arose from legacy structured products and stressed and distressed corporates, particularly the defaulted bonds of high-yield energy companies. Agency trading was also a positive contributor. Corporate hedges were a detractor given the large rally in high-yield credit markets.

FX trading contributed to the overall profits. The Fund benefitted from maintaining a long exposure to the USD throughout most of the year against a basket of currencies including GBP and JPY. Other trades including long exposures to a basket of commodity related currencies including CAD and AUD during the first half of the year added to the gains. Some of the gains were offset by losses from a short exposure to the EUR in the first quarter and a long exposure to MXN around the US election.

Trading in major equity indices, mainly EuroStoxx , Nikkei and S&P, generated losses. Most of the losses arose from long and short tactical trading. Part of the losses were offset by strong gains from a long exposure to the S&P in December.

Commodity trading was a small part of the Fund during 2016. It was a modest detractor with most of the losses coming from long exposure to oil in January.

Systematic trading was positive for the year. The annual return of the BHDGST Class Z USD shares (4.02%) compares favourably with the performance of the SG Trend Index, which returned -6.18% over the period. The bulk of the gains arose from long exposures to short term interest rates and bonds globally, with particularly strong performance at the beginning of the year and around the EU referendum. The Fund maintained a long exposure to equity indices for most of the year, which generated additional gains. Some of the returns were offset by losses in FX, energy and metals without any key drivers.

The Investment Committee (“IC”) made the decision to increase the allocation to the Direct Investment Portfolio (“DIP”) and to diversify its exposure across a larger number of traders throughout the year. Since the end of the first quarter the DIP had exposure to ten underlying trading books across macro, emerging market and credit strategies. At the end of 2016, the allocation to the DIP stood at approximately 60%. The increased allocation has given the IC greater flexibility to allocate capital directly to traders, which it believes will continue to benefit the return profile of the Fund in the medium to long term. Other meaningful allocation changes during the year were a decrease to Brevan Howard Master Fund Limited and to a smaller extent a decrease to Brevan Howard Asia Master Fund Limited.

While the world faces significant uncertainties in 2017, the global economy looks to be on a reasonably sound footing with the prospect of additional fiscal spending combined with accommodative monetary policy. The ECB and Bank of Japan are continuing their unconventional monetary policy of quantitative easing combined with negative rates, while the Federal Reserve is removing accommodation at a measured and gradual pace. These policies were part of the landscape last year and will continue to be important in 2017. In summary, investors can expect some of the trends from 2016 to continue into 2017, some new initiatives to emerge and potentially plenty of surprises.

The IC will continue to take advantage of the flexibility within the Fund’s mandate in order to seek high risk adjusted returns and keep a healthy diversification across strategies, asset classes and traders.

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Portfolio Update for BHG

The information in this section has been provided to BHG by BHCM.

Monthly, quarterly and annual contribution (%) to the performance of BHG USD Shares (net of fees and expenses) by asset class*

	Rates	FX	Commodity	Credit	Equity	Discount Management	TOTAL
Dec 2016	-0.09	0.30	-0.01	0.19	0.43	0.00	0.82
Q1 2016	1.14	0.31	-0.22	0.50	-1.17	0.44	1.01
Q2 2016	0.61	-0.04	-0.12	1.03	-0.56	0.40	1.32
Q3 2016	-0.48	-0.65	-0.14	1.01	-0.11	0.38	0.00
Q4 2016	2.17	1.95	-0.11	0.35	0.56	0.00	4.96
YTD 2016	3.47	1.56	-0.59	2.92	-1.27	1.22	7.42

PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS

*Data as at 30 December 2016

Monthly, quarterly and annual figures as at 30 December 2016, based on performance data for each period provided by BHG's administrator, Northern Trust. Figures rounded to two decimal places.

Methodology and Definition of Contribution to Performance:
Attribution by asset class is produced at the instrument level, with adjustments made based on risk estimates.
The above asset classes are categorised as follows:
"**Rates**": interest rates markets
"**FX**": FX forwards and options
"**Commodity**": commodity futures and options
"**Credit**": corporate and asset-backed indices, bonds and CDS
"**Equity**": equity markets including indices and other derivatives
"Discount Management": buyback activity for discount management purposes

Monthly, quarterly and annual contribution (%) to the performance of BHG USD Shares (net of fees and expenses) by strategy group*

	Macro	Systematic	Rates	FX	Equity	Credit	EMG	Commodity	Discount Management	TOTAL
Dec 2016	0.63	0.17	0.14	0.04	-0.00	0.23	0.05	-0.00	0.00	0.82
Q1 2016	-0.04	0.63	0.14	-0.01	-0.00	-0.12	-0.04	-0.00	0.44	1.01
Q2 2016	-0.16	-0.14	-0.04	0.01	-0.00	0.97	0.28	-0.00	0.40	1.32
Q3 2016	-1.13	-0.17	0.09	-0.08	-0.00	0.91	0.02	-0.00	0.38	0.00
Q4 2016	4.88	-0.05	0.52	0.11	-0.00	0.39	-0.17	-0.00	0.00	4.96
YTD 2016	3.49	0.27	0.72	0.04	-0.00	2.16	0.09	-0.00	1.22	7.42

PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS

*Data as at 30 December 2016

Monthly, quarterly and annual figures as at 30 December 2016, based on performance data for each period provided by BHG's administrator, Northern Trust. Figures rounded to two decimal places.

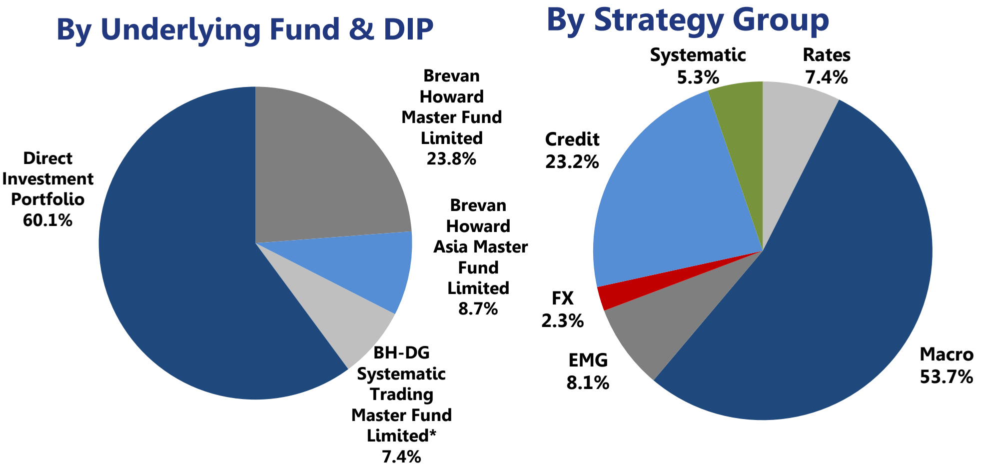
Methodology and Definition of Contribution to Performance:
Strategy Group Attribution is approximate and has been derived by allocating each underlying trader book to a single category. In cases where a trader book has activity in more than one category, the most relevant category has been selected.

The above strategies are categorised as follows:
"**Macro**": multi-asset global markets, mainly directional (for BHG, the majority of risk in this category is in rates)
"**Systematic**": rules-based futures trading
"**Rates**": developed interest rates markets
"**FX**": global FX forwards and options
"**Equity**": global equity markets including indices and other derivatives
"**Credit**": corporate and asset-backed indices, bonds and CDS
"**EMG**": global emerging markets
"**Commodity**": liquid commodity futures and options
"**Discount Management**": buyback activity for discount management purposes

Fund Allocations

The information in this section has been provided to BHG by BHCM.

Allocations of BHMS as at 30 December 2016 (allocations subject to change):



Source: BHCM; figures rounded to one decimal place. Sum may not total 100% due to rounding.

*Known as Brevan Howard Systematic Trading Master Fund Limited prior to 8 April 2016.

Methodology and Definition of Allocation by Strategy Group:

Strategy Group allocation is approximate and has been derived by allocating each trader book in the underlying Funds and in the Direct Investment Portfolio to a single category. In cases where a trader book has activity in more than one category, the most relevant category has been selected.

The above strategies are categorised as follows:
"**Macro**": multi-asset global markets, mainly directional (for the Fund, the majority of risk in this category is in rates)
"**Systematic**": rules-based futures trading
"**Rates**": developed interest rates markets
"**FX**": global FX forwards and options
"**Credit**": corporate and asset-backed indices, bonds and CDS
"**EMG**": global emerging markets

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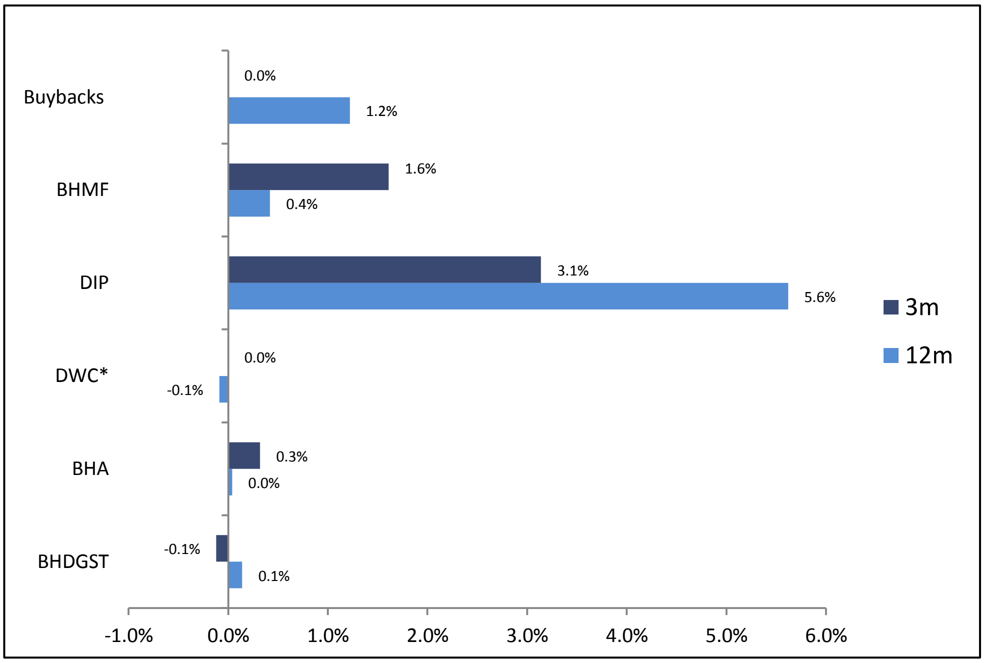
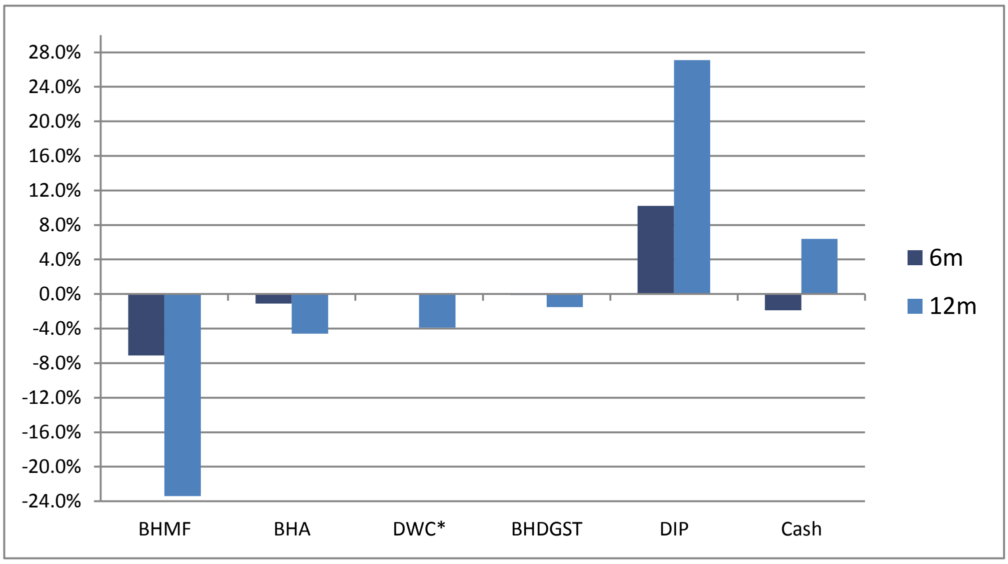
BHG Quarterly and Annual Contribution (%) by Underlying Allocation as at 30 December 2016



*DW Catalyst Offshore Fund, Ltd ("DWC") is a feeder fund to DW Catalyst Master Fund, Ltd. DWC also has the ability to make other investments. Prior 1 January 2015, DW Catalyst Master Fund, Ltd was named Brevan Howard Credit Catalysts Master Fund Limited.

BHG Allocation Changes as a % of NAV as at 30 December 2016 (allocations subject to change):



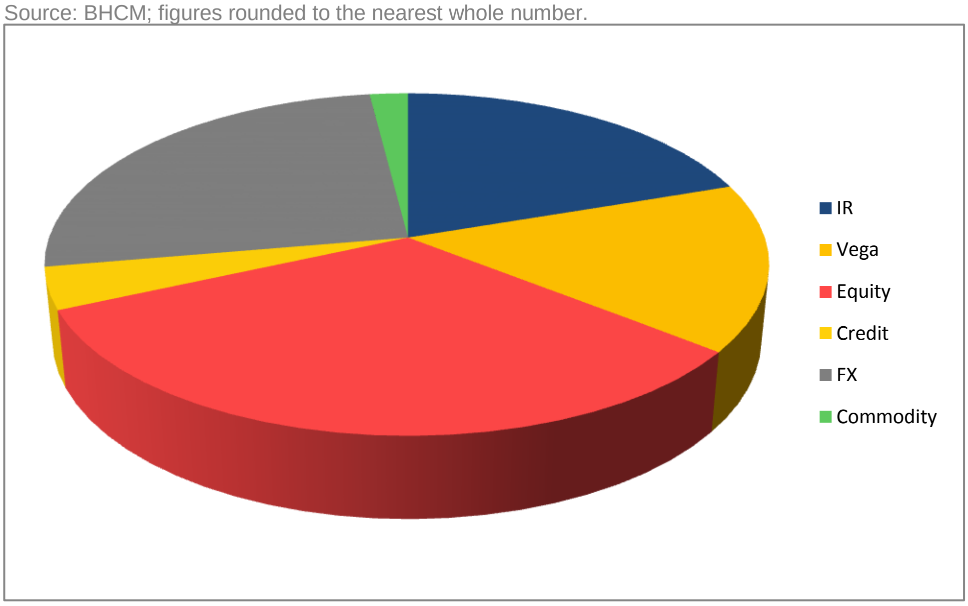
* DWC is a feeder fund to DW Catalyst Master Fund, Ltd. DWC also has the ability to make other

investments. Prior to 1 January 2015, DW Catalyst Master Fund, Ltd was named Brevan Howard Credit Catalysts Master Fund Limited. Note: Other underlying allocations defined above.

BHG Exposures by Asset Class as at 30 December 2016 (exposures subject to change):

Asset Class	VaR** by asset class as a % of total VaR
IR	20
Vega	16
Equity	33
Credit	4
FX	26
Commodity	2

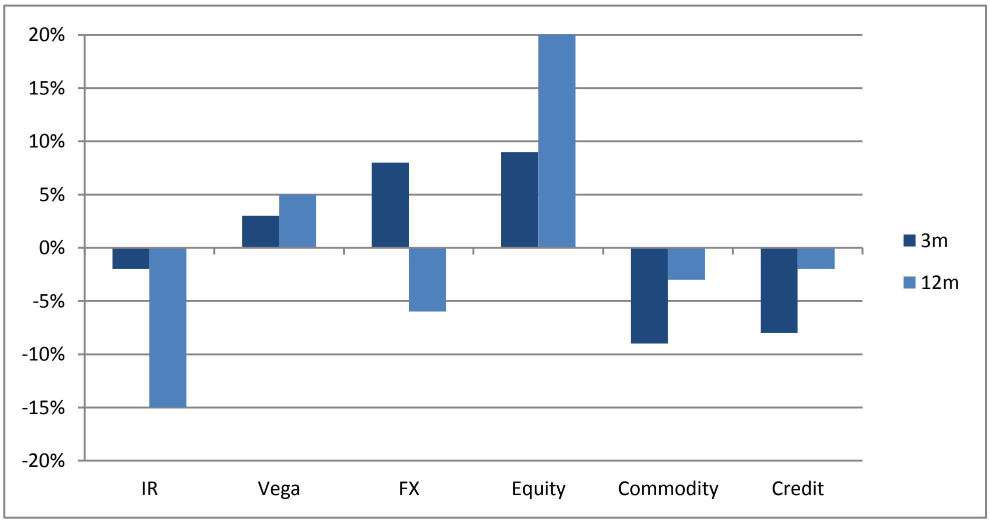
Source: BHCM; figures rounded to the nearest whole number.



Calculated using historical simulation based on a 1 day, 95% confidence interval.

Source: BHCM; figures rounded to the nearest whole number. Data may differ from those published for BHMS as BHG may hold cash for short-term working capital purposes.

BHG Exposure Changes as at 30 December 2016 (subject to change):



Source: BHCM; figures rounded to the nearest whole number.

Monthly Performance Review for BHG

The information in this section has been provided to BHG by BHCM.

BHG Monthly Commentary

The NAV per share of BHG's USD shares appreciated by 0.82% and the NAV per share of BHG's GBP shares appreciated by 0.96% in December 2016.

Monthly Performance of BHMS Underlying Allocations*

Investment	Rates	FX	Equity	Commodity	Credit	Dec 2016 Total	YTD Total
Brevan Howard Master Fund Limited Class Z (USD)**	-0.12%	-0.02%	0.15%	-0.01%	0.42%	0.41%	5.57%
Brevan Howard Asia Master Fund Limited (USD)**	1.45%	2.40%	-0.02%	-0.00%	0.00%	3.83%	4.98%
BH-DG Systematic Trading Master Fund Limited Class Z (USD)**	0.42%	0.27%	1.85%	-0.10%	0.00%	2.43%	4.02%
Direct Investment Portfolio	-0.39%	0.54%	0.96%	-0.01%	0.38%	1.47%	14.38%

*As at 30 December 2016

** The USD currency class of each fund is used as a proxy for the performance of each of the funds; BHMS also invests in other currency classes of the funds.

Source: Data for the funds in which BHMS invests in is provided by their respective administrators, calculations by BHCM.

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Brevan Howard Master Fund Limited ("BHMF")

The NAV per share of BHMF Class Z USD shares appreciated by 0.41% in December. Towards the end of December, BHMF gave back some of the gains generated earlier in the month. These moves were primarily driven by short positioning in US interest rates, long exposure, via options, to the S&P as well as long positions in the US dollar against a range of currencies including the Euro and the Yen. Additional gains came from credit trading while short positions in European and GBP interest rates detracted modestly from performance.

Brevan Howard Asia Master Fund Limited ("BHA")

The NAV per share of BHA Ordinary USD shares appreciated by 3.83% in December. Gains were driven by FX and interest rate trading. FX gains came primarily from directional, relative value and volatility trading of Chinese Renminbi as well as short positioning in the Japanese Yen and Singapore dollar. Further gains came from short positioning and curve steepening trades in US and Hong Kong dollar interest rates, together with curve steepening positions in Korea and Japan. Equity index trading in Europe and Korea detracted modestly.

BH-DG Systematic Trading Master Fund Limited ("BHDGST")

The NAV per share of BHDGST Class Z USD shares appreciated by 2.43% in December. The final month of the year saw gains realised in all financials, energies and FX sectors. BHDGST made mixed adjustments across bond futures, leaving overall risk relatively unchanged. Short positions in the US 5-year, 10-year and Ultra Bond were increased, but short positions in the 30-year and 2-year treasury futures were conversely cut. Within short term interest rates, substantial cuts to euribor and short Sterling positions were matched by equally significant additions to short positions in Canadian Bankers' Acceptance and Eurodollar futures. The Strategy's top-five winners were all long equity index positions in December, with the S&P e-mini position topping the list. Within currencies, the US dollar's increasing strength saw BHDGST extend its long bias versus AUD, GBP and JPY.

Direct Investment Portfolio ("DIP")

In December the Direct Investment Portfolio ("DIP") appreciated by 1.47%. The bulk of the gains arose from macro trading in equity indices and FX. Trading in credit generated additional gains whereas interest rates were a detractor. In equity, the bulk of the gains arose from a long exposure to the S&P equity index. In FX, most profits were generated from long exposure to the USD against JPY and GBP with additional gains from trading in other markets including ZAR, KRW and AUD. In interest rates, the DIP benefitted from exposures to higher USD rates. The gains in USD were more than offset by losses from short exposures to EUR rates, which rallied during second half of the month. A decline in EUR interest rate volatility generated additional small losses. In credit there were no predominant drivers with gains arising in a number of positions across structured and corporate credit as well as agency trading. The portfolio benefitted from small gains from an unexpected CDS credit event in an US media company and from long positions in legacy CMBS bonds. Corporate index hedges were a detractor from P&L. The DIP held no meaningful exposure to commodities during the month.

Manager's Market Review and Outlook

The information in this section has been provided to BHG by BHCM.

Market Commentary

US

The year ended with modestly above-trend growth, a tightening labour market and tame inflation. Real GDP growth appeared to have moderated to approximately 2% in the fourth quarter, and forward-looking indicators pointed to a similar pace in the first quarter. Business investment has improved after having been a strain on growth for much of the last year. Inventories are being restocked, which added to growth in the second half of the year. Outlays on equipment have finally flattened out after having contracted for four consecutive quarters. Structures investment is moving up as energy investment picks back up. Residential investment also has bounced. The most notable hindrance has been from a decline in exports that reversed the one-time surge in agricultural exports seen in the third quarter. Overall, the growth outlook looks solid.

The unemployment rate ticked up to 4.7% in December following the surprising drop to 4.6% in November. December was the second month of readings below most observers' estimate of the long-run sustainable rate of labour-market utilisation. Broader measures of labour market underutilisation continue to improve as well. As would be expected when the economy is operating in the neighbourhood of full employment, wages are accelerating. In particular, the latest year-over-year gain on average hourly earnings was 2.9%, the fastest pace of the expansion. Payroll employment gains slowed in the fourth quarter to a still-solid average increase of more than 150,000 job gains per month.

Core Personal Consumption Expenditure inflation rose 1.6% in the year ended in November, little different from the pace seen during most of 2016. With a strong US dollar exerting downward pressure on import prices and tighter labour markets translating only weakly into consumer prices, consumer inflation trends appear restrained.

Monetary policy took a back seat to political developments in Washington. The Federal Reserve raised rates in December and pointed to a somewhat faster pace of rate hikes in 2017 and beyond, partly because of the prospects for fiscal stimulus. Meanwhile, President Trump appointed most of his cabinet and Congress turned its attention to an ambitious legislative agenda, which includes repealing and replacing Obamacare, corporate and personal tax reform, infrastructure spending, additional defence outlays, immigration, and de-regulation. As Chief Executive, the President has direct control over the trade agenda, parts of immigration policy, and some regulation. President Trump has promised to act quickly in these areas over the coming months.

UK

A continuation of the recent trends in the UK economy has been observed. Contrary to certain expectations, the vote to leave the European Union has not dented economic activity. Growth has proved remarkably resilient, with companies continuing to invest and consumer spending remaining buoyant. More recently, a pick-up in global demand has also provided a more constructive backdrop. The relevant question going forward will be to what extent consumer spending will slow in response to the deceleration in real incomes, as inflation is expected to pick up materially. So far, some of the outperformance in consumption over real income growth can be explained by faster credit growth and rising house prices. It is possible that this trend continues and consumption spending defies the upcoming slowdown in real incomes, but it is also possible that some adjustment is finally seen. This has also been identified as one of the key judgements by the Bank of England (“BoE”). The UK labour market has remained broadly stable in recent months. So far, no clear signs of the rise in unemployment that the BoE expects for 2017 have been detected.

Inflation has started to move higher, driven by energy-price base effects and the weaker Sterling exchange rate. In November, the Bank of England forecast a material overshoot of inflation relative to its target in the next few years, largely on account of the sharp depreciation of Sterling over the past year, prompting the Monetary Policy Committee to abandon its easing stance and move to a more neutral policy stance. The BoE could be forced to tighten monetary policy if the exchange rate resumed its downward trend or inflation expectations started to move higher in an environment where consumption spending remains resilient. For the time being, however, the BoE has adhered to its forecast for a gradual slowdown in economic growth, which should in turn bring inflation back to target over the medium term.

On 17 January, Prime Minister Theresa May outlined her 12-point plan for Brexit during a speech at Lancaster House. As expected, May took the hard Brexit stance, announcing the UK would leave the Single Market. Although, attempts to maintain “the greatest possible access to it” by negotiating an ambitious Free Trade Agreement with the European Union. However, the Government lost the appeal at the Supreme Court on 24 January. The ruling means the Government cannot trigger Article 50 without an act of Parliament, although this is expected to happen in time for the Government’s 31 March deadline. Further information on the Brexit process will be released in the coming weeks.

EMU

2016 began with increasing downside risks in view of emerging market uncertainties and financial market volatility. Given these risks and weak inflation dynamics the ECB decided upon further measures in March, having disappointed financial market expectations in December 2015. In March 2016, the ECB cut the deposit rate by a further 10bp to -0.4% and the main refinancing rate by 5bp to 0%. The Asset

Purchase Programme ("APP") was increased to €80bn per month (from April 2016) from the initial pace of €60bn per month, although purchases were still intended to run until the end of March 2017, or beyond, if necessary. The ECB also added investment grade euro-denominated (non-bank) corporate bonds to the APP (purchases started in June 2016) and launched four targeted longer-term refinancing operations (TLTROII), each with a maturity of four years and the opportunity for banks to secure a negative funding cost in line with the deposit rate if net lending exceeded a benchmark. Euro area GDP growth remained relatively strong at the start of the year (0.5% q/q) before moderating in Q2 as uncertainty increased ahead of the main risk event – the UK's EU membership referendum at the end of June. While the vote for Brexit was unexpected, it caused only a transitory dip to confidence indicators over the summer. The German IFO business climate index dropped cumulatively around 2.5 points in July and August but then rebounded over 3 points in September and continued to increase in Q4. The euro area composite Purchasing Manager's Index dipped marginally during the summer before reaccelerating throughout Q4 to reach its highest level (54.4) since May 2011 by the end of the year. Euro area GDP seems poised to end the year growing back at a 0.5% q/q pace which will result in GDP growth of 1.7% in 2016 after 1.9% in 2015. During the year the euro area unemployment rate continued to decline, falling from 10.4% at the end of 2015 to 9.8% in November 2016. However, wage growth has yet to pick up despite this improvement in the labour market in recent years. Euro area negotiated wage growth remains low at just 1.4% y/y in Q3 2016, its slowest annual growth rate since Q4 1991. As a result, core inflation has remained sluggish throughout 2016, averaging just 0.85% in 2016, barely up from 0.83% in 2015 (and compared to the December 2015 ECB staff core inflation forecast of 1.3% for 2016). Headline inflation averaged just 0.2% in 2016, albeit up from 0.0% in 2015.

The lack of sufficient progress towards achieving a sustained adjustment in inflation resulted in the ECB announcing on 8 December 2016, a nine month extension to Quantitative Easing ("QE") until the end of December 2017 (or beyond, if necessary), albeit at a slower pace of €60bn from April 2017 (as deflation risks had diminished). This nonetheless will add a further €540bn of purchases, taking the total intended stock of QE to €2.28trn (or 21% of GDP). In order to achieve this expansion, the ECB also changed some of the parameters to accommodate an expanded QE programme, notably expanding the maturity of eligible bonds by decreasing the minimum remaining maturity to 1yr from 2yrs and allowing purchases with a yield to maturity below the deposit rate "to the extent necessary". There was also a dovish warning that the ECB intends to increase the programme in terms of size and/or duration should the economic outlook deteriorate or financial conditions tighten unduly, although for now the forward guidance around the potential for lower rates seems surplus to requirements as the deposit rate looks to have reached its effective lower bound at -0.4% (with the ECB seemingly content to see a steeper yield curve in order to reduce the negative impact of its monetary policy on the banking sector). More recently, the combination of stronger oil prices following the OPEC agreement and energy price base effects has resulted in an increase in euro area inflation to 1.1% y/y in December. Looking forward, inflation is expected to continue to rise at the beginning of 2017. Core inflation, however, is likely to remain more sluggish, falling short of the ECB's forecast for a more robust pick-up, as the weakness in wages will continue to weigh on core inflation. The ECB's account of the 8 December policy meeting confirms divergent views on the Governing Council regarding inflation risks. The dovish camp has warned of the over-prediction of inflation in recent years (with the largest forecast error said to be on wages and still no clear signs of labour market pressures), while the more hawkish camp noted some indications of stronger headline inflation, which they believe could be expected to have an influence on future wage dynamics. These arguments will persist for some time to come, hence why the minutes confirm that both downside and upside risks to the inflation outlook warrant close monitoring.

Part of the ECB's explanation for a nine month extension of QE was also to ensure a sustained market presence and source of stability in an uncertain environment. The region managed to broadly weather political risks in 2016. This was especially the case in Italy where there was no significant market fall-out from the resignation of Prime Minister Renzi after his heavy loss in the constitutional referendum (59.1%-40.9%). Furthermore, the new Government under Prime Minister Gentiloni was able to secure Parliamentary approval for borrowing of up to €20bn (1.2% of GDP) for the banking sector to facilitate a bailout for Monte dei Paschi (estimated at €8.8bn, of which €6.6bn is expected to be at the cost of the Italian state) after it finally requested a "precautionary" capital increase (with bond/equity burden-sharing and some move to compensate mis-sold retail bondholders). The other task for the new Government will be to approve a new electoral law ahead of new elections.

Looking ahead, the focus in 2017 turns to politics and the electoral surprises delivered in the UK with Brexit and in the US election will likely keep uncertainty and fears over the rise of populism high. General elections are on the horizon in The Netherlands (15 March), France (Presidential elections on 23 April/7 May) and Germany (likely September). Elections in Italy could be as early as Spring 2017 but may also be delayed until its natural deadline (i.e. Spring 2018). In addition, Greece has to conclude the second review of its bailout programme. Having announced its intention to continue QE at a reduced pace of €60bn from April 2017 until the end of 2017 (or beyond, if necessary), it is not expected the ECB will contemplate any further policy changes until the second half of this year when focus on tapering will likely build again. Core inflation is expected to remain subdued (and below ECB forecasts), which seems likely to result in the ECB maintaining a market presence via QE well into 2018.

China

During 2016 growth has somewhat stabilised at around 6.7% due to the Government's easing effort. Policy easing before Q4 was mainly in the form of growth, i.e. credit-driven investment, especially in construction and infrastructure, which led to a continued rise in leverage. GDP growth in 2016 slowed further from 6.9% to 6.7%, the lowest level in 30 years, although broadly in line with the Government's target.

Looking forward, 2017 is a unique year due to the scheduled leadership change every five years. In the baseline scenario, five out of the seven Central Politburo will have to retire, leading to an unprecedented reshuffle of power, especially given President's Xi's power consolidation. In that setting, the Government will likely focus on the political issues for 2017, meaning that risk aversion of policy makers will likely rise accordingly. That would lead to policy mainly targeting a stabilisation scenario in growth and finance markets. The official GDP growth target for 2017 is likely to be maintained at approximately 6.5%, with the rising probability of it being lowered to 6-6.5%. Fiscal policy is likely to be expanded further, but the major lift will have to rely on quasi-fiscal deficit, i.e., investment financed by local governments which is not included in the official fiscal deficit.

Japan

During 2016, the Bank of Japan ("BoJ") slowly rejected its reflation project. The Bank began the year with one last shot, pushing short rates into negative territory.

Markets, however, did not co-operate. The yen appreciated sharply against the dollar. Inflation slowed to the point where consumer prices excluding food and energy were essentially flat, and consumer inflation expectations continued to deteriorate. For half a year, the BoJ kept policy on hold. In September, the Bank then switched tactics again, announcing its so-called yield-curve control policy, no longer targeting a fixed quantity of asset purchases but setting its bond buying to keep the ten-year Japanese Government Bond ("JGB") rate around zero. The BoJ's operative theory is that when inflation starts to move up, the suppression of the long rate will become extra stimulative as real long rates fall; knowing that will happen sometime in the future, investors and consumers should raise their inflation expectations now. In the event, BoJ bond purchases have slowed somewhat and the ten-year rate is now a little higher than when the Bank announced the new policy. While inflation expectations have recently flattened out, they remain at a relatively low level.

Despite the BoJ's capitulation, external events set up 2017 for some pick-up in inflation. Since the election of Donald Trump as President of the United States the yen has depreciated almost 10% against the US dollar. At the same time, oil prices have moved up, some of which should be passed on generally. Altogether, inflation won't approach the BoJ's 2% target, but western core inflation should lift off the current 12-month rate of 0.1%.

While US election results have helped Governor Kuroda, they have created a new set of challenges for Prime Minister Abe. Obviously, the Trans-Pacific Partnership is dead; Japan's ratification of the deal in December was a gesture to what looks increasingly like the peak in globalisation. The President's campaign promises to raise tariffs or Congressional Republican plans for tax reform with a border adjustment, if enacted, will bite into the global trading system and risks setting off responses elsewhere in Asia that Japan will have to manage. Moreover, geopolitical risks, whether they are in the East China Sea or on the Korean peninsula, feel like more of a wildcard than before. For his part, Abe's party did well in the upper-house elections over the summer. Along with smaller like-minded parties, the Prime Minister has the necessary two thirds supermajority necessary to amend the country's constitutional restrictions on the military, though it will still take a lot of effort to push that project forward. Altogether, the Prime Minister will have his plate full; that reduces the bandwidth and political capital needed to guide additional structural reforms this year. At least he won't have to contend with the fallout from a second hike in consumption taxes. Last summer, Abe announced a delay until October 2019.

Prime Minister Abe should benefit from decent momentum in economic activity. Last year GDP rose slightly faster than expected, closing some of the output gap. The latest survey data are satisfactory. The appreciation in the yen over the first half of 2016 will probably cut into net exports, though the most recent reversal should help limit that drag to activity. Meanwhile, although the stimulative effects of the spending package passed over the summer were probably overemphasised, it will still be supportive of growth this year.

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