BREVAN HOWARD

BH MACRO LIMITED

MONTHLY SHAREHOLDER REPORT:

DECEMBER 2016

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BREVAN HOWARD

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BH Macro Limited

Manager:

Brevan Howard Capital Management LP ("BHCM")

Administrator:

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

Corporate Broker:

J.P. Morgan Cazenove

Listings:

London Stock Exchange (Premium Listing)

NASDAQ Dubai - USD Class (Secondary listing)

Bermuda Stock Exchange (Secondary listing)

Overview

BH Macro Limited ("BHM") is a closed-ended investment company, registered and incorporated in Guernsey on 17 January 2007 (Registration Number: 46235).

BHM invests all of its assets (net of short-term working capital) in the ordinary shares of Brevan Howard Master Fund Limited (the "Fund").

BHM was admitted to the Official List of the UK Listing Authority and to trading on the Main Market of the London Stock Exchange on 14 March 2007.

Total Assets: $865 mm[1]

1. As at 30 December 2016. Source: BHM's administrator, Northern Trust.

Summary Information

BH Macro Limited NAV per Share (Calculated as at 30 December 2016)

Share Class	NAV (USD mm)	NAV per Share
USD Shares	216.3	$21.68
EUR Shares	34.7	€21.87
GBP Shares	613.8	£22.44

BH Macro Limited NAV per Share % Monthly Change

USD	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2007			0.10	0.90	0.15	2.29	2.56	3.11	5.92	0.03	2.96	0.75	20.27
2008	9.89	6.70	-2.79	-2.48	0.77	2.75	1.13	0.75	-3.13	2.76	3.75	-0.68	20.32
2009	5.06	2.78	1.17	0.13	3.14	-0.86	1.36	0.71	1.55	1.07	0.37	0.37	18.04
2010	-0.27	-1.50	0.04	1.45	0.32	1.38	-2.01	1.21	1.50	-0.33	-0.33	-0.49	0.91
2011	0.65	0.53	0.75	0.49	0.55	-0.58	2.19	6.18	0.40	-0.76	1.68	-0.47	12.04
2012	0.90	0.25	-0.40	-0.43	-1.77	-2.23	2.36	1.02	1.99	-0.36	0.92	1.66	3.86
2013	1.01	2.32	0.34	3.45	-0.10	-3.05	-0.83	-1.55	0.03	-0.55	1.35	0.40	2.70
2014	-1.36	-1.10	-0.40	-0.81	-0.08	-0.06	0.85	0.01	3.96	-1.73	1.00	-0.05	0.11
2015	3.14	-0.60	0.36	-1.28	0.93	-1.01	0.32	-0.78	-0.64	-0.59	2.36	-3.48	-1.42
2016	0.71	0.73	-1.77	-0.82	-0.28	3.61	-0.99	-0.17	-0.37	0.77	5.02	0.19	6.63

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EUR	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2007			0.05	0.70	0.02	2.26	2.43	3.07	5.65	-0.08	2.85	0.69	18.95
2008	9.92	6.68	-2.62	-2.34	0.86	2.84	1.28	0.98	-3.30	2.79	3.91	-0.45	21.65
2009	5.38	2.67	1.32	0.14	3.12	-0.82	1.33	0.71	1.48	1.05	0.35	0.40	18.36
2010	-0.30	-1.52	0.03	1.48	0.37	1.39	-1.93	1.25	1.38	-0.35	-0.34	-0.46	0.93
2011	0.71	0.57	0.78	0.52	0.65	-0.49	2.31	6.29	0.42	-0.69	1.80	-0.54	12.84
2012	0.91	0.25	-0.39	-0.46	-1.89	-2.20	2.40	0.97	1.94	-0.38	0.90	1.63	3.63
2013	0.97	2.38	0.31	3.34	-0.10	-2.98	-0.82	-1.55	0.01	-0.53	1.34	0.37	2.62
2014	-1.40	-1.06	-0.44	-0.75	-0.16	-0.09	0.74	0.18	3.88	-1.80	0.94	-0.04	-0.11
2015	3.34	-0.61	0.40	-1.25	0.94	-0.94	0.28	-0.84	-0.67	-0.60	2.56	-3.22	-0.77
2016	0.38	0.78	-1.56	-0.88	-0.38	3.25	-0.77	0.16	-0.56	0.59	5.37	0.03	6.37

GBP	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2007			0.11	0.83	0.17	2.28	2.55	3.26	5.92	0.04	3.08	0.89	20.67
2008	10.18	6.86	-2.61	-2.33	0.95	2.91	1.33	1.21	-2.99	2.84	4.23	-0.67	23.25
2009	5.19	2.86	1.18	0.05	3.03	-0.90	1.36	0.66	1.55	1.02	0.40	0.40	18.00
2010	-0.23	-1.54	0.06	1.45	0.36	1.39	-1.96	1.23	1.42	-0.35	-0.30	-0.45	1.03
2011	0.66	0.52	0.78	0.51	0.59	-0.56	2.22	6.24	0.39	-0.73	1.71	-0.46	12.34
2012	0.90	0.27	-0.37	-0.41	-1.80	-2.19	2.38	1.01	1.95	-0.35	0.94	1.66	3.94
2013	1.03	2.43	0.40	3.42	-0.08	-2.95	-0.80	-1.51	0.06	-0.55	1.36	0.41	3.09
2014	-1.35	-1.10	-0.34	-0.91	-0.18	-0.09	0.82	0.04	4.29	-1.70	0.96	-0.04	0.26
2015	3.26	-0.58	0.38	-1.20	0.97	-0.93	0.37	-0.74	-0.63	-0.49	2.27	-3.39	-0.86
2016	0.60	0.70	-1.78	-0.82	-0.30	3.31	-0.99	-0.10	-0.68	0.80	5.05	0.05	5.79

Source: Fund NAV data is provided by the administrator of the Fund, International Fund Services (Ireland) Limited ("IFS"). BHM NAV and NAV per Share data is provided by BHM's administrator, Northern Trust. BHM NAV per Share % Monthly Change is calculated by BHCM. BHM NAV data is unaudited and net of all investment management fees (2% annual management fee and 20% performance fee) and all other fees and expenses payable by BHM. In addition, the Fund is subject to an operational services fee of 50bps per annum.

BHCM shall waive its entitlement to a management fee in respect of any performance-related growth of BHM from 3 October 2016 onwards. In addition, BHM's investment in the Fund will not bear an operational services fee in respect of any performance-related growth from 3 October 2016 onwards.

NAV performance is provided for information purposes only. Shares in BHM do not necessarily trade at a price equal to the prevailing NAV per Share.

Data as at 30 December 2016

PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.

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ASC 820 Asset Valuation Categorisation*

Brevan Howard Master Fund Limited

Unaudited as at 30 December 2016

	% of Gross Market Value*
Level 1	79.3
Level 2	20.2
Level 3	0.1
At NAV	0.4

Source: BHCM

* 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 Brevan Howard funds and priced or valued at NAV as calculated by IFS.

Annual Manager Review: 2016

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

The NAV per share of the USD share class of BH Macro Limited appreciated by 6.63% in 2016, while the NAV per share of the Euro shares appreciated by 6.37% and the NAV per share of the Sterling shares appreciated by 5.79% in 2016. The Fund's largest exposures at the start of the year were long positions in European interest rates and short positions in the Euro currency, held in anticipation of further easing by the ECB. While these positions initially generated gains, they reversed following the ECB's meeting in March as market participants focused on President Draghi's comments downplaying the prospects for further easing. Small gains across a wide range of strategies including credit index, relative value, volatility and emerging market interest rates trading were offset by losses from short positions in US interest rates and equity trading, leaving the Fund with a small loss by the end of the first half of 2016.

During the second half of the year, in what were largely trendless markets, the Fund's performance slipped until November when, following the US election results, market volatility increased sharply. The Fund profited as US and European interest rates rose, as did the US dollar and the level of implied volatility across a range of different asset classes. November's gain of 5.02% was the Fund's sixth best-ever monthly return and followed a period of relatively low VaR usage, highlighting not only the rapid adjustment in risk levels but also the limits of the usefulness of VaR as a predictor of upside potential.

The acquisition by BHM of 7,812,223 Sterling shares, 861,331 Euro shares and 3,805,094 US Dollar shares pursuant to the tender offer launched by BHM on 27 April 2016 (the "Tender Offer") was executed on 27 June 2016. The repurchase of shares under the Tender Offer resulted in the NAV per share of the remaining USD shares appreciating by 2.52%, the NAV per share of the remaining Sterling shares appreciating by 2.38% and the NAV per share of the remaining Euro shares appreciating by 2.14%.

2016 was a year of significant political developments. In the UK, the Brexit vote was a shock to many and, in the US, Donald Trump won the presidential election against expectations. Although it is possibly an oversimplification, voters seem eager to repudiate the status quo. This is important because the institutions and policies that have shaped market outcomes since the Great Recession may, as a result, face additional challenges going forward.

The good news is that 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. Recent economic developments are covered later in this report but broadly, the ECB and Bank of Japan are continuing their unconventional monetary policy of quantitative easing combined with negative rates (and, in the case of Japan, explicit yield caps), 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 in 2017, some new initiatives to emerge, and potentially plenty of surprises.

We look forward to exploiting any opportunities that these factors may create.

Performance Review

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

Towards the end of December, the Fund 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.

The performance review and attributions are derived from data calculated by BHCM, based on total performance data for each period provided by the Fund's administrator (IFS) and risk data provided by BHCM, as at 30 December 2016.

Performance by Asset Class

Monthly, quarterly and annual contribution (%) to the performance of BHM USD Shares (net of fees and expenses) by asset class as at 30 December 2016

2016	Rates	FX	Commodity	Credit	Equity	Discount Management & Tender Offer	Total
January 2016	1.14	-0.15	-0.15	-0.13	-0.22	0.22	0.71
February 2016	1.08	0.27	-0.02	-0.12	-0.63	0.16	0.73
March 2016	-1.04	-0.93	0.03	0.27	-0.29	0.19	-1.77
April 2016	-0.48	-0.27	-0.04	0.06	-0.11	0.01	-0.82
May 2016	-0.28	0.03	0.01	0.04	-0.09	0.02	-0.28
June 2016	0.77	0.15	0.06	-0.05	-0.19	2.87	3.61
July 2016	-0.25	-0.84	-0.04	0.02	0.00	0.12	-0.99
August 2016	0.11	-0.18	-0.01	0.06	-0.19	0.04	-0.17
September 2016	-0.38	-0.53	0.05	0.12	-0.15	0.52	-0.37
October 2016	-0.20	0.46	-0.02	0.04	-0.02	0.11	0.77
November 2016	3.15	1.75	0.01	0.10	0.01	0.00	5.02
December 2016	-0.17	-0.07	-0.02	0.37	0.08	0.00	0.19
Q1 2016	1.17	-0.82	-0.14	0.02	-1.14	0.57	-0.35
Q2 2016	0.01	-0.09	0.03	0.05	-0.39	2.90	2.47
Q3 2016	-0.52	-1.55	0.01	0.20	-0.34	0.68	-1.52
Q4 2016	3.18	2.15	-0.03	0.51	0.08	0.11	6.04
YTD 2016	3.85	-0.35	-0.13	0.78	-1.78	4.31	6.63

PAST PERFORMANCE IS NOT INDICATIVE OF FUTURE RESULTS.

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 & Tender Offer**": buyback activity for discount management purposes and repurchases under the tender offer launched on 27 April 2016.

Monthly VaR of the Fund by asset class as a % of total VaR*

	Rates	Vega	FX	Equity	Commodity	Credit
January 2016	41	15	20	15	4	4
February 2016	25	18	35	11	3	7
March 2016	39	19	26	7	5	4
April 2016	40	22	23	4	6	5
May 2016	34	26	22	2	9	6
June 2016	31	22	28	9	5	2
July 2016	20	27	23	13	11	7
August 2016	28	26	16	15	8	6
September 2016	37	21	22	6	6	9
October 2016	42	19	28	2	3	6

November 2016	33	16	42	5	2	3
December 2016	26	15	35	20	2	2

Source: BHCM. Data as at 30 December 2016.

* Calculated using historical simulation based on 1 day, 95% confidence interval. Sum may not add up to 100% due to rounding.

Performance by Strategy Group

Monthly, quarterly and annual contribution (%) to the performance of BHM USD Shares (net of fees and expenses) by strategy group as at 30 December 2016

2016	Macro	Systematic	Rates	FX	Equity	Credit	EMG	Commodity	Discount Management & Tender Offer	Total
January 2016	-0.11	0.02	0.86	0.01	-0.00	-0.12	-0.17	-0.00	0.22	0.71
February 2016	0.41	0.01	0.32	-0.00	-0.00	-0.14	-0.03	-0.00	0.16	0.73
March 2016	-1.38	-0.02	-0.62	-0.03	-0.00	-0.08	0.17	-0.00	0.19	-1.77
April 2016	-0.62	-0.01	-0.39	-0.04	-0.00	0.05	0.18	-0.00	0.01	-0.82
May 2016	-0.48	-0.01	-0.00	0.06	-0.00	0.06	0.09	-0.00	0.02	-0.28
June 2016	0.66	0.02	0.15	-0.01	-0.00	-0.02	-0.05	-0.00	2.87	3.61
July 2016	-0.77	0.00	-0.07	-0.13	-0.00	0.01	-0.15	-0.00	0.12	-0.99
August 2016	-0.36	-0.01	0.10	-0.04	-0.00	0.04	0.06	-0.00	0.04	-0.17
September 2016	-1.02	-0.01	0.10	-0.10	-0.00	0.11	0.03	-0.00	0.52	-0.37
October 2016	0.60	-0.02	-0.04	0.06	-0.00	0.12	-0.05	-0.00	0.11	0.77
November 2016	3.89	0.00	0.98	0.13	-0.00	0.08	-0.07	-0.00	0.00	5.02
December 2016	-0.40	0.01	-0.03	0.07	-0.00	0.40	0.14	-0.00	0.00	0.19
Q1 2016	-1.10	0.01	0.56	-0.02	-0.01	-0.34	-0.02	-0.00	0.57	-0.35
Q2 2016	-0.44	-0.01	-0.24	0.01	-0.01	0.08	0.21	-0.00	2.90	2.47
Q3 2016	-2.14	-0.01	0.13	-0.28	-0.00	0.17	-0.06	-0.00	0.68	-1.52
Q4 2016	4.10	-0.00	0.90	0.26	-0.00	0.60	0.02	-0.00	0.11	6.04
YTD 2016	0.31	-0.01	1.35	-0.02	-0.01	0.51	0.15	-0.00	4.31	6.63

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Methodology and Definition of Contribution to Performance:

Strategy Group attribution is approximate and has been derived by allocating each trader book in the Fund 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
"**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 & Tender Offer**": buyback activity for discount management purposes and repurchases under the tender offer launched on 27 April 2016.

Manager's Market Review and Outlook

The information in this section has been provided to BHM by BHCM

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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• The Fund will be leveraged and will engage in speculative investment practices that may increase the risk of investment loss. The Fund may invest in illiquid securities.

• Past results of the Fund's investment managers are not necessarily indicative of future performance of the Fund, and the Fund's performance may be volatile.

• An investor could lose all or a substantial amount of his or her investment.

• The Fund's investment managers have total investment and trading authority over the Fund, and the Fund is dependent upon the services of the investment managers.

• Investments in the Fund are subject to restrictions on withdrawal or redemption and should be considered illiquid. There is no secondary market for investors' interests in the Fund and none is expected to develop.

• The investment managers' incentive compensation, fees and expenses may offset the Fund's trading and investment profits.

• The Fund is not required to provide periodic pricing or valuation information to investors with respect to individual investments.

• The Fund is not subject to the same regulatory requirements as mutual funds.

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