



ECONOMIC AND FINANCIAL OUTLOOK

Anton Brender and Florence Pisani

Rotterdam, December 7, 2017



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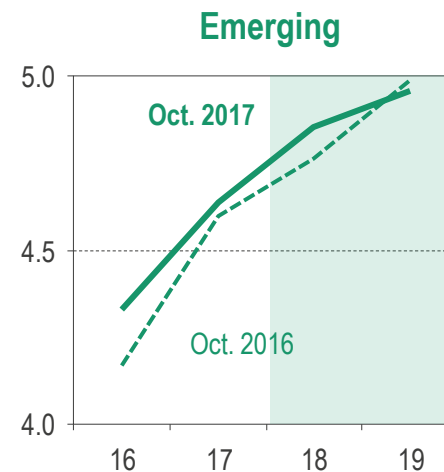
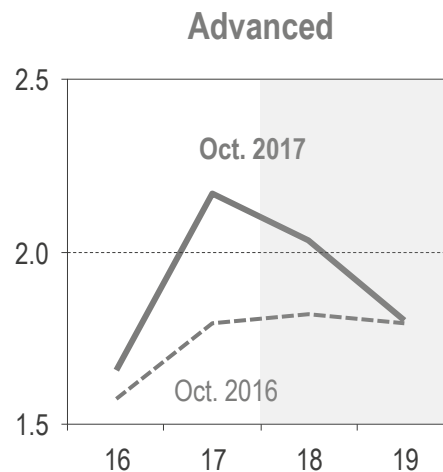
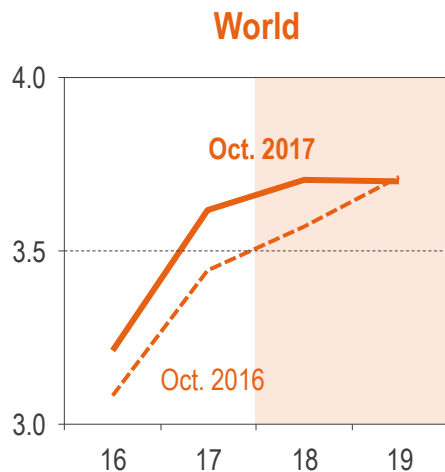
GLOBAL ECONOMY
A more stable world growth?

GLOBAL ECONOMY

Advanced economies' growth surprised positively,
but world growth is now fuelled by emerging economies

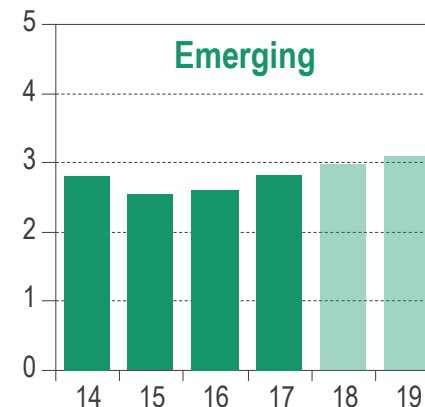
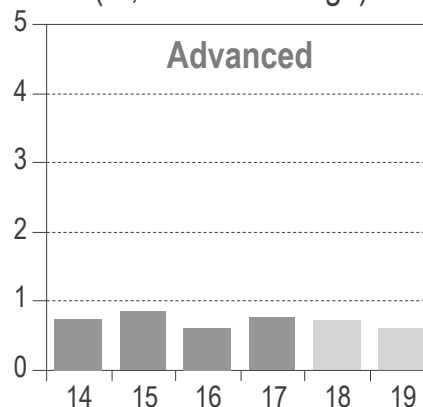
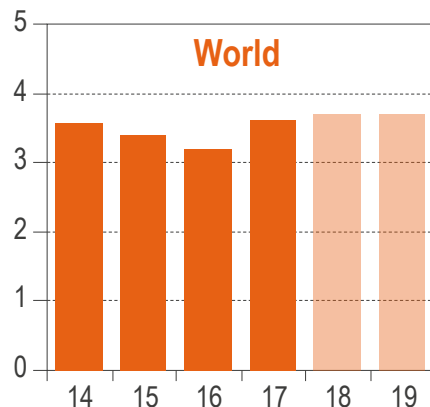
IMF GDP growth revisions

(%, annual average)



Contributions to world GDP growth

(%, annual average)



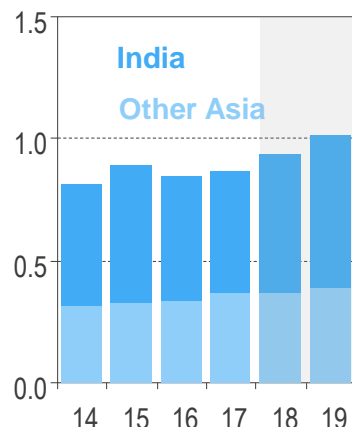
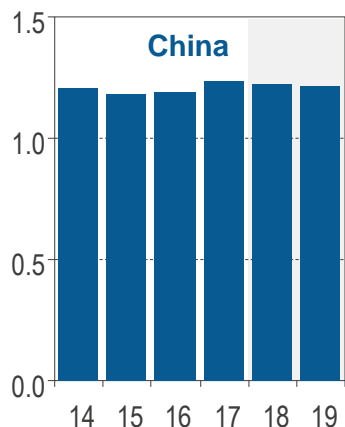
GLOBAL ECONOMY

Asia now accounts for the bulk of emerging GDP growth

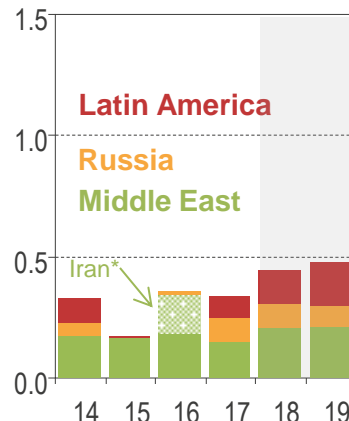
Contributions to world GDP growth

(%, annual average)

Developing Asia

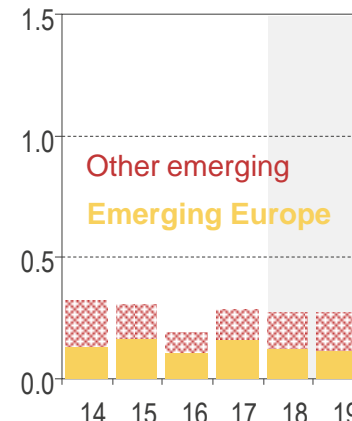


Commodity producers



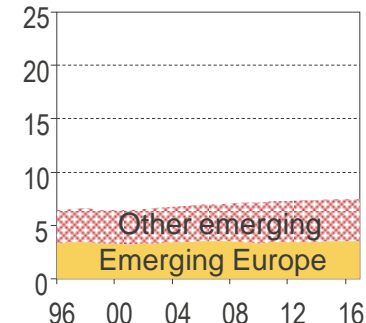
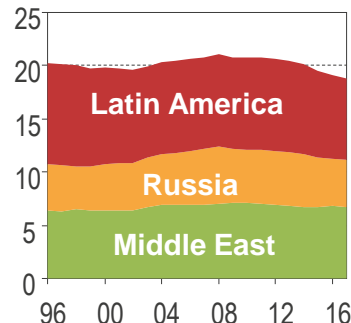
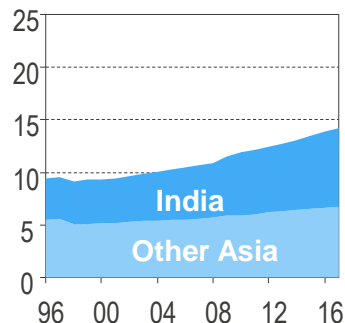
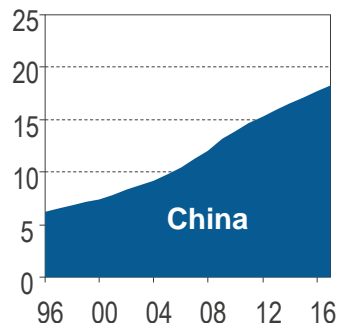
(*) Removal of international sanctions

Other emerging economies



Share in world GDP

(%, purchasing power parity)



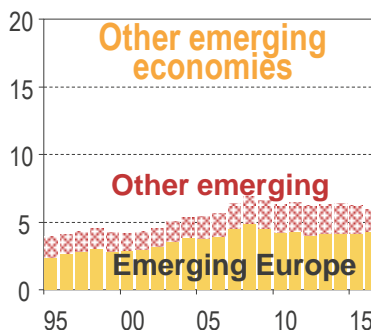
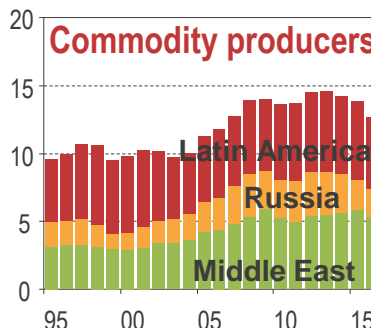
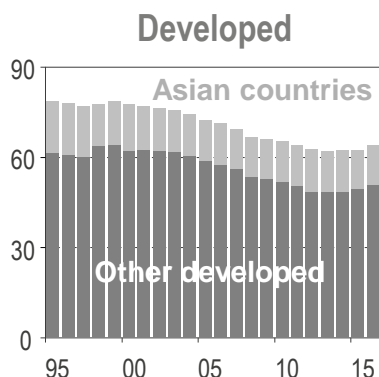
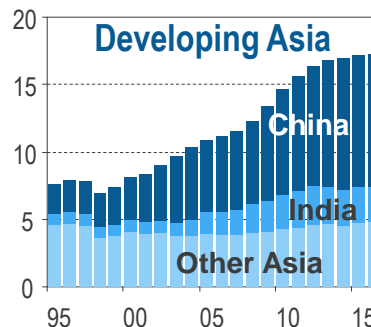
GLOBAL ECONOMY

Growth and import demand have become less volatile... in emerging countries in particular

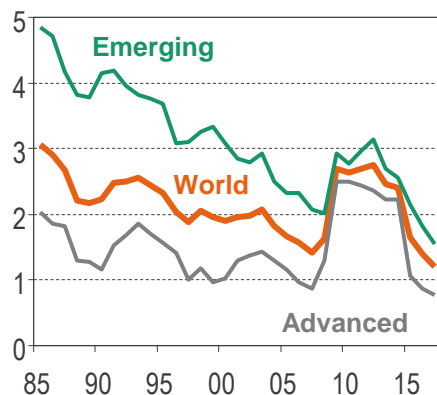
Volatility of world growth and trade

Share in world imports

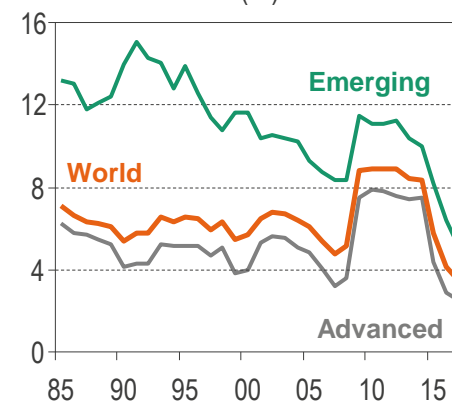
(% of world imports in dollars)



Volatility* of growth in real GDP (%)



Volatility** of growth in imports' volumes (%)



(*) 6-year rolling standard deviation of real GDP growth for 193 countries, using PPP shares in world GDP to calculate the world aggregate.

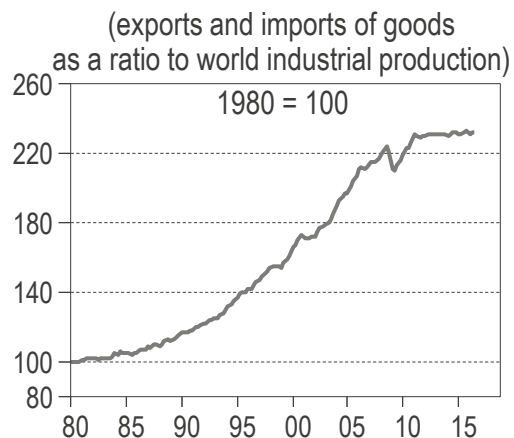
(**) 6-year rolling standard deviation of real growth of imports of goods and services for 193 countries, using dollars imports shares in world imports to calculate the world aggregate.

GLOBAL ECONOMY

Trade integration has stopped increasing... but de-globalization is a reality only for the most volatile capital flows!

Some dimensions of globalization

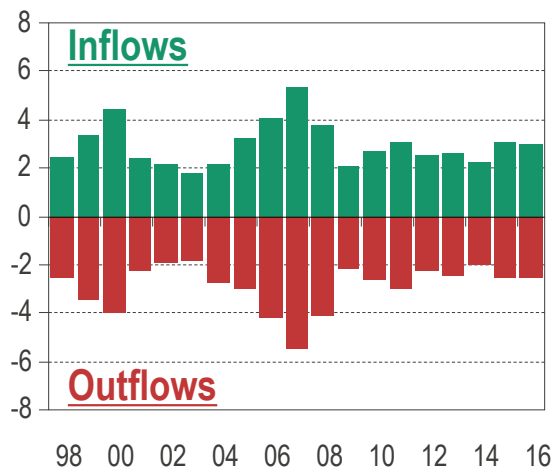
World trade



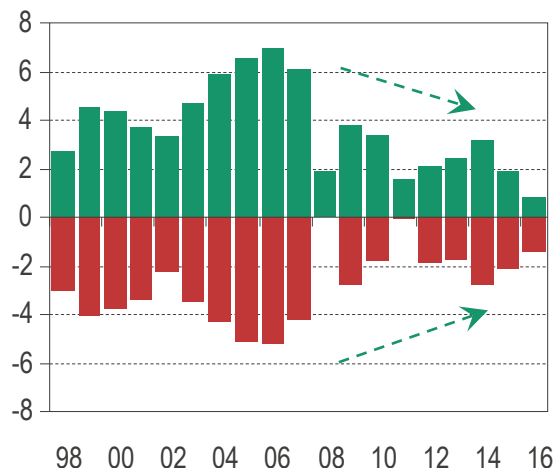
World capital flows

(% of world GDP)

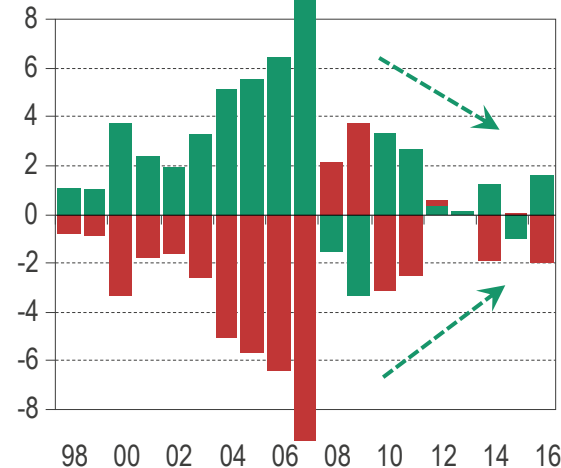
Direct investment



Portfolio investment



Other investment





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CHINA

Keeping a delicate balance



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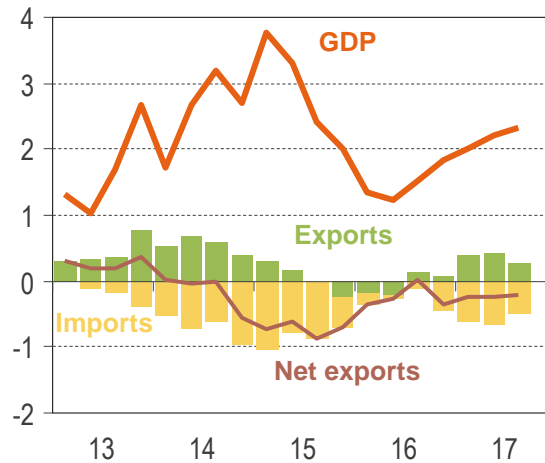
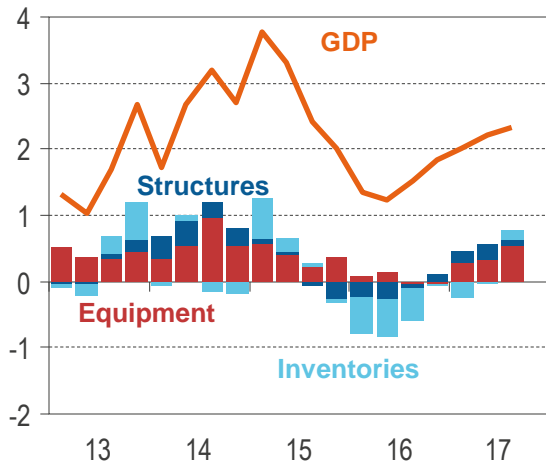
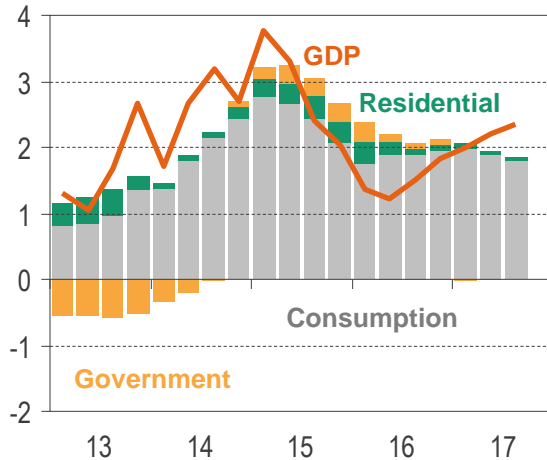
UNITED STATES
Many unknowns remain

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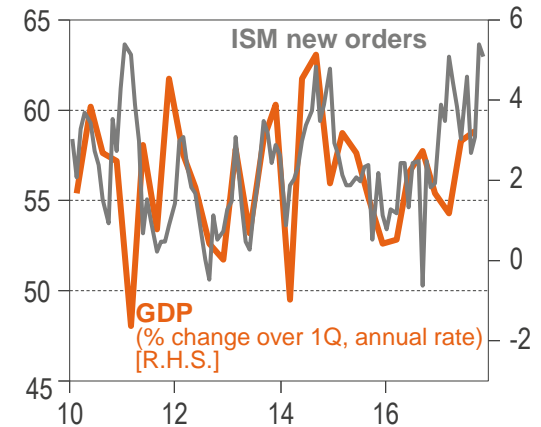
Business investment has picked up and household spending continues to provide a solid base for US growth

Contributions to GDP growth

(% year on year)



ISM composite & GDP

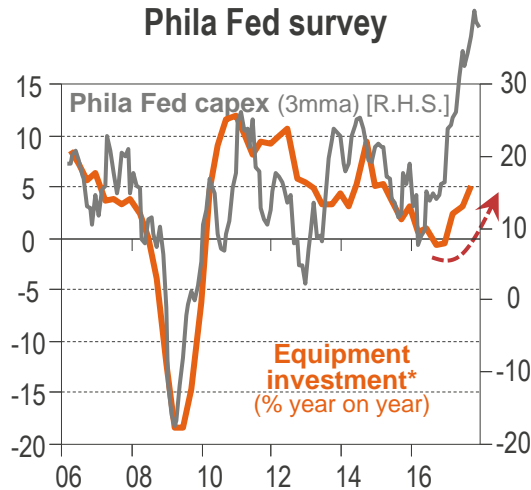


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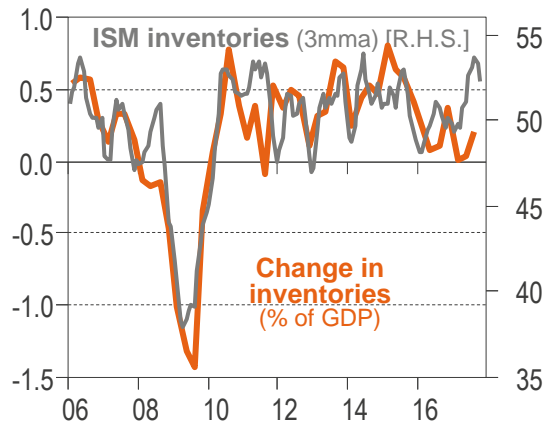
Surveys are well oriented

Monthly surveys and indicators

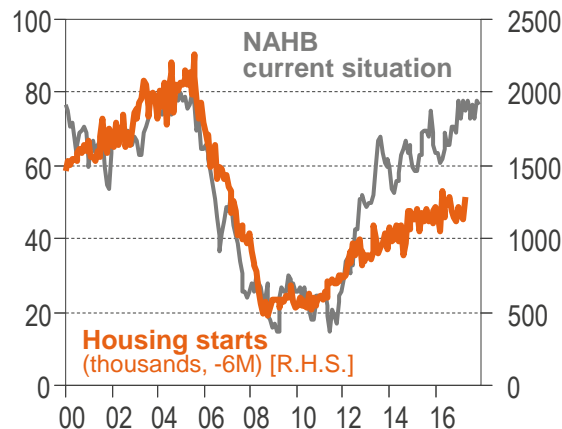
Phila Fed survey



Change in inventories



NAHB survey on home sales



Export orders



Consumption

(% change over 3 months, nominal, annual rate)

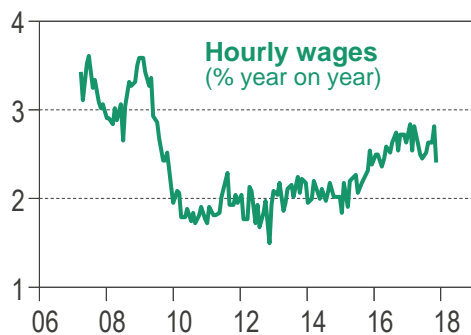
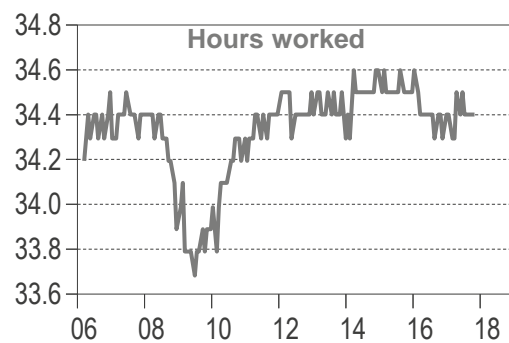
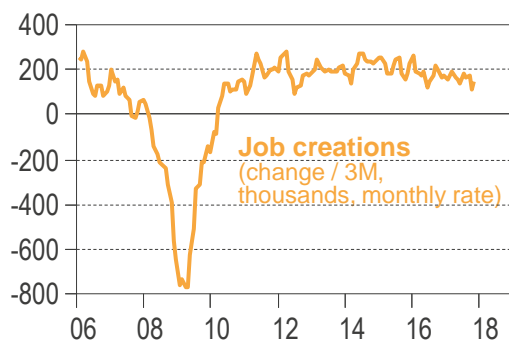


(*) including intellectual property rights

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Income growth will remain the main driver of consumption

Employment, hours worked, wages and household income growth



Observed and calculated wages (% year on year)



(*) hourly earnings x hours worked x employment

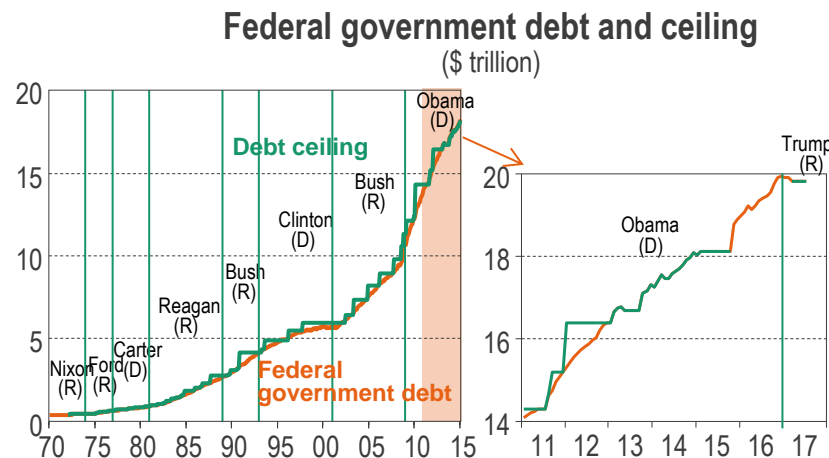
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Major fiscal issues are still pending

Two pending fiscal issues

The debt ceiling

Congress must act to increase – or suspend – the debt limit. Beginning of December, the drop-dead date was somewhere in 2018H1.

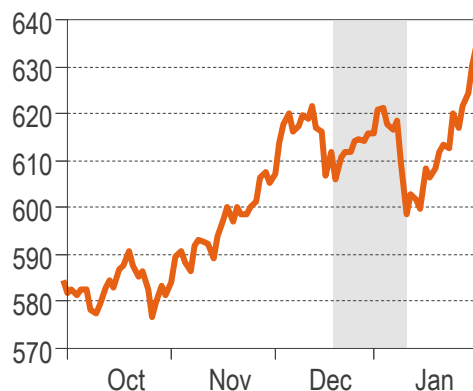


S&P500 during the 2011 crisis



S&P500 during the two longest “shutdown”

Dec. 15 1995 – Jan. 6 1996



Sept. 30 – Oct. 17 2013



The FY 2018 Budget

Since October 2018, federal spending has taken place under a Continuing Resolution. A Budget for FY2018 still has to be agreed upon.

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Two projects have been approved... they now have to be reconciled !

House	
Provision	Static
Eliminate the individual alternative minimum tax.	-\$389
Consolidate the current seven tax brackets into four and phase out the benefit of the 12 percent bracket for high-income households	-\$1,522
Increase the standard deduction to \$12,200 / \$18,300 / \$24,000	-\$1,390
Repeal personal exemptions	\$1,839
Increase the child tax credit amount to \$1,600. Initially, only the first \$1,000 is refundable. Increase the nonrefundable portion of the child tax credit by \$300 for each non-child household member, available for five years. Increase the phaseout thresholds for the child tax credit to \$230,000 for married filers and \$115,000 for other filers	-\$715
Repeal all itemized deductions except for the mortgage interest deduction (capped at \$500,000 of acquisition debt on a principal residence), the charitable deduction, and the deduction for state and local property taxes paid (capped at \$10,000), increase contribution limits for the charitable contributions deduction, repeal the Pease limitation on itemized deductions	\$1,524
Consolidate education tax benefits, repeal several personal tax credits, limit the applicability of certain refundable tax credits, repeal or limit several exclusions, and modify rules for tax-preferred retirement accounts	\$167
Index bracket thresholds and the standard deduction amount to chained CPI. Index the refundable portion of the child credit to chained CPI until it reaches \$1,600 (economic effect not modeled)	\$156
Individual subtotal	-\$330
Lower the corporate tax rate to 20 percent	-\$1,536
Create a maximum tax rate of 25 percent on qualified pass-through business income, accompanied by several anti-abuse rules	-\$531
Limit interest deductions to 30 percent of adjusted earnings for businesses with over \$25 million in gross receipts	\$147
Allow businesses to deduct 100 percent of short-lived investments for 5 years. Increase the \$179 expensing amount from \$500,000 to \$5 million, and increase the phaseout threshold from \$2 million to \$20 million	-\$340
Eliminate business credits, deductions, and other tax preferences and enact miscellaneous changes to business taxation	\$488
Move to a territorial tax system, accompanied by several rules to prevent base erosion	\$56
Enact a deemed repatriation of deferred foreign-source income, at rates of 5% and 12%	\$223
Business subtotal	-\$1,493
Other	
Eliminate the estate tax	-\$160
TOTAL	-\$1,984

Senate	
Individual	
Eliminate the alternative minimum tax.	-\$389
Adjust individual income tax rates and thresholds, creating seven rates of 10%, 12%, 22.5%, 25%, 32.5%, 35%, and 38.5%.	-\$1,912
Increase the standard deduction to \$12,000/\$18,000/\$24,000.	-\$1,023
Repeal personal exemptions.	\$1,795
Increase the child tax credit amount to \$1,650. Initially, only the first \$1,100 of the credit is refundable. Decrease the phase-in threshold of the refundable portion of the credit to \$2,500. Increase the phaseout threshold of the credit to \$500,000 for married filers and \$250,000 for other filers. Allow the credit to be claimed for children under age 18. Create a \$500 nonrefundable credit for non-child dependents.	-\$659
Repeal the deduction for state and local taxes paid, the deduction for interest on home equity indebtedness, the deduction for tax preparation expenses, and several miscellaneous deductions. Limit the casualty loss deduction, and modify limits on the charitable deduction. Repeal the Pease limitation on itemized deductions.	\$1,506
Modify or repeal other personal deductions, credits, and exclusions.	\$42
Index bracket thresholds, the standard deduction amount, the refundable portion of the child tax credit, and other provisions to chained CPI (economic effect not modeled).	\$178
Individual subtotal	-\$462
Business	
Lower the corporate income tax rate to 20 percent, effective 1/1/2019.	-\$1,396
Create a 17.4% deduction for pass-through business income. Generally, income from service businesses is ineligible, but households with less than \$75,000/\$150,000 in taxable income can claim a full deduction for service business income. In the case of partnership and S corporation income, income subject to the deduction is limited to 50 percent of the taxpayer's W-2 wages.	-\$527
Reduce the depreciable lives of residential and nonresidential buildings to 25 years. Allow businesses to deduct 100 percent of 168(k) property for 5 years. Increase the \$179 expensing amount from \$500,000 to \$1 million, and increase the phaseout threshold from \$2 million to \$2.5 million. Limit interest deductions to 30 percent of EBIT for businesses with over \$15 million in gross receipts.	\$185
Eliminate business tax expenditures, etc.	\$415
Move to a territorial tax system, accompanied by several rules to prevent base erosion.	-\$74
Enact a deemed repatriation of deferred foreign-source income, at rates of 5% and 10%.	\$179
Business subtotal	-\$1,218
Other	
Double the estate and gift tax exemption.	-\$95
TOTAL	-\$1,775

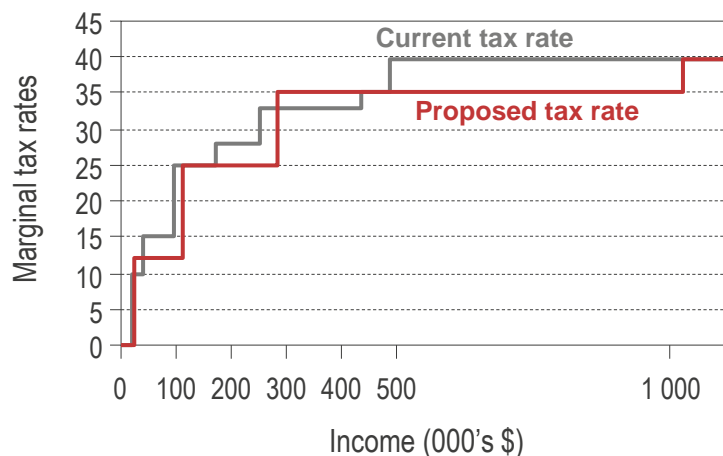
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The tax overhaul should not give much stimulus to households spending

Personal income tax reform proposal in the House bill

Personal income tax rates and brackets

(married couple filing jointly)

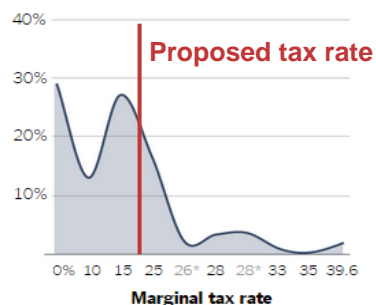


Impacts of the Tax Cuts and Jobs Act (Updated)

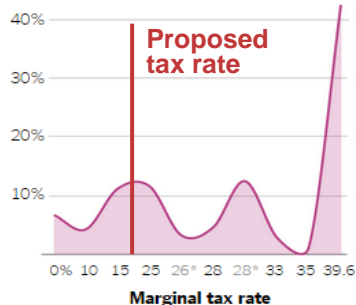


	James	Jason	Kavya and Nick	Sophie and Chad	Soren and Linnea	Laura and Seth	Olivia and Richard	Joe and Ethan
Ordinary Income	\$30,000	\$52,000	\$85,000	\$165,000	\$325,000	\$2,000,000	\$800,000	\$48,000
Pass-Through Income	\$0	\$0	\$0	\$0	\$0	\$0	\$200,000	\$0
Marital Status	Single	Single	Married	Married	Married	Married	Married	Married
Earners	1 earner	1 earner	1 earner	2 earners	2 earners	1 earner	1 earner	Retired
Children	No kids	2 kids	2 kids	2 kids	2 kids	2 kids	2 kids	No Dependents
Tax-Deferred Retirement Contributions	\$2,600	\$1,500	\$5,500	\$20,000	\$37,000	\$18,500	\$18,500	\$0
Itemization	Std. Ded.	Std. Ded.	Std. Ded.	Itemizing	Itemizing	Itemizing	Itemizing	Std. Ded.
Current Law	\$4,132	\$5,458	\$10,614	\$27,815	\$76,853	\$764,142.30	\$349,173	\$2,285
Proposed	\$3,944	\$4,563	\$9,542	\$26,443	\$70,443	\$729,024.50	\$290,043	\$2,266
Tax Liability Change	\$188	\$895	\$1,072	\$1,373	\$6,410	\$35,118	\$59,130	\$19
% Tax Liability Change	5%	16%	10%	5%	8%	5%	17%	1%
% Change in After Tax Earnings	0.73%	1.92%	1.44%	1.00%	2.58%	2.84%	9.09%	0.04%

Share of pass-through businesses per marginal tax rate



Share of pass-through net income per marginal tax rate



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Corporate taxes will be significantly cut...

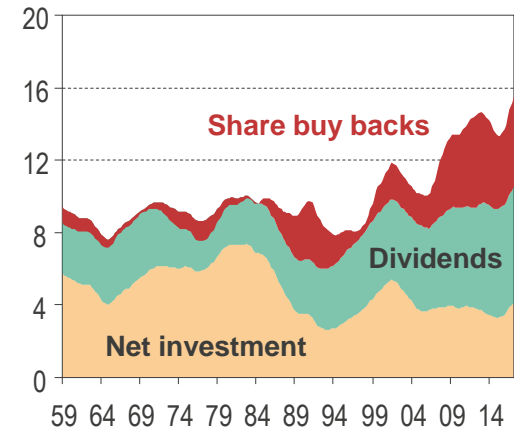
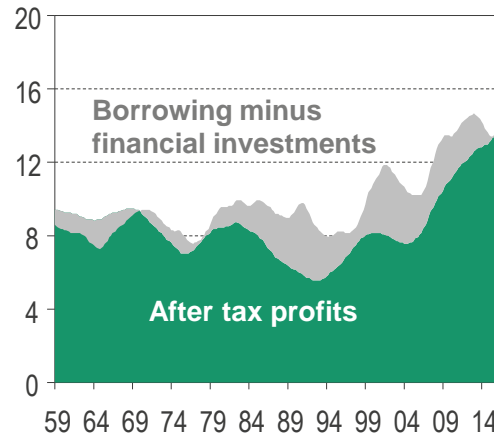
but how this will affect business investment is unclear!

Non financial corporations profits and investment

- The House and Senate both target a 20% corporate tax rate (versus the present 35%). Since this is the priority of both Congress and the President, the end result should be close to the target.
- House and Senate both have included a 5-year full expensing of equipment investment in their bills.
- Note that if the Senate proposal of postponing the corporate tax cut to 2019 were to become final, it could lead to a boom of business investment in 2018... and a bust afterwards, possibly implying a “hiccup” in activity.

Non financial corporations financial resources and uses

(% of NFC gross value added, 7-year moving average)

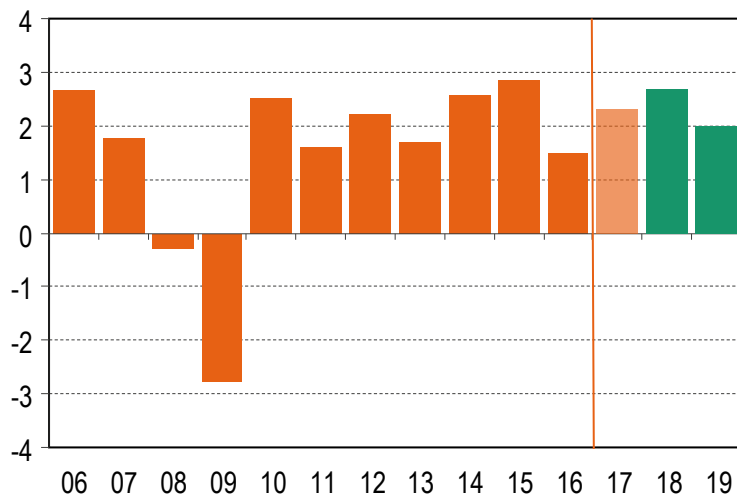


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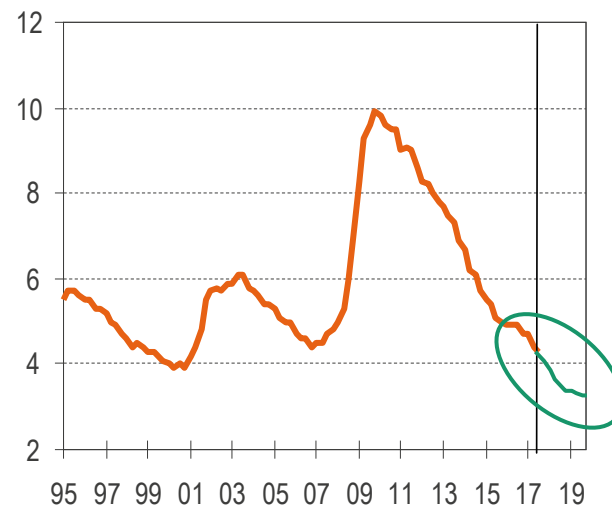
With some fiscal support, growth should be above 2.5% in 2018

Forecasts for 2018-2019

GDP growth
(%, annual rate)



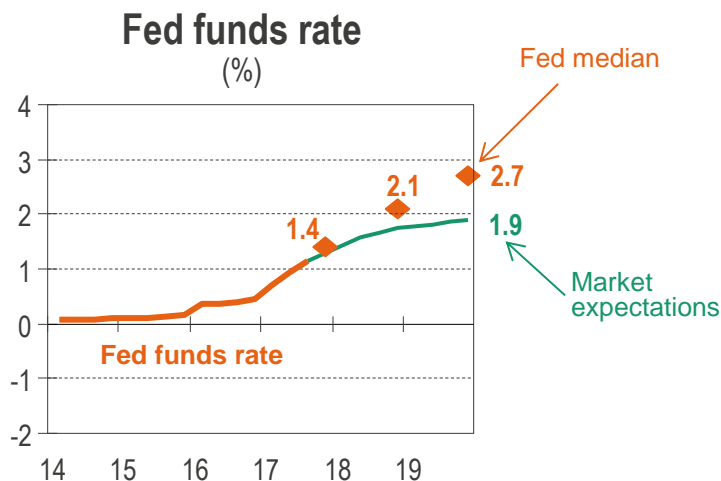
Unemployment rate
(%)



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The Fed should continue to gradually tighten rates...
and long term rates should gradually move up

Federal reserve monetary policy and long term interest rates



US 10-year interest rate forecasts (Treasury)

	Nov. 28, 2017	End of 2018
(I) 2-year interest rate	1.8%	2.2%
(II) 3-year interest rate in 2 years	2.3%	2.8%
(III) 5-year interest rate in 5 years	2.6%	3.3%
10-year interest rate	2.3%	2.9%



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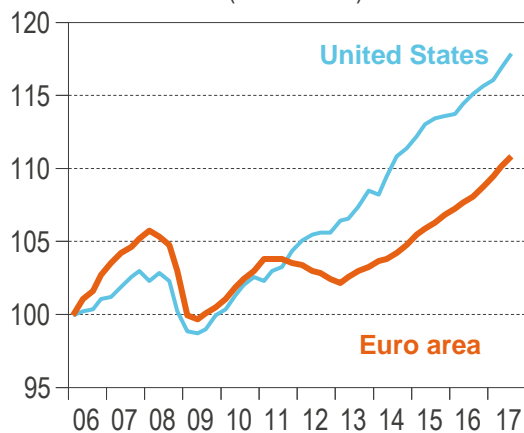
EURO AREA
A solid recovery...

EURO AREA

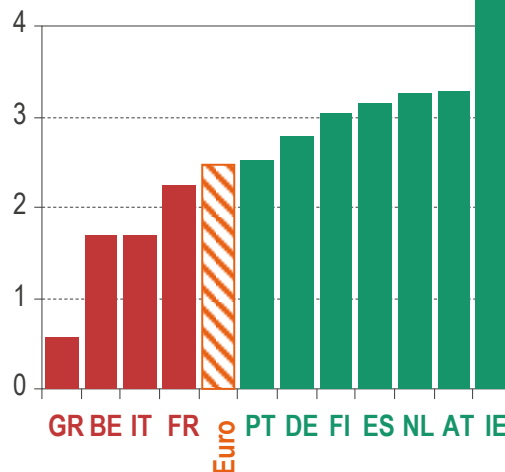
Activity has gained momentum

Activity in the euro area

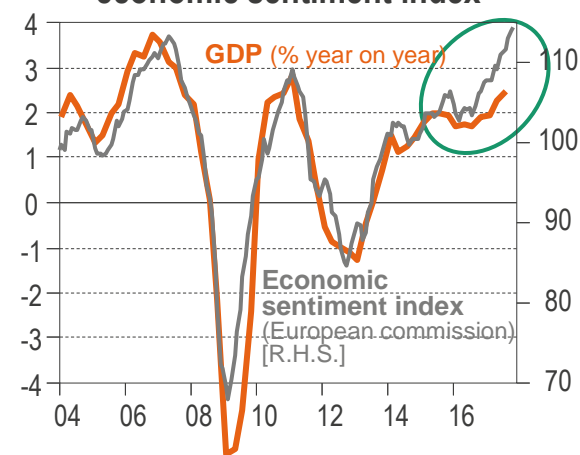
GDP level
(2006 = 100)



GDP growth by country
(% year on year, Q3 2017)



GDP growth and economic sentiment index



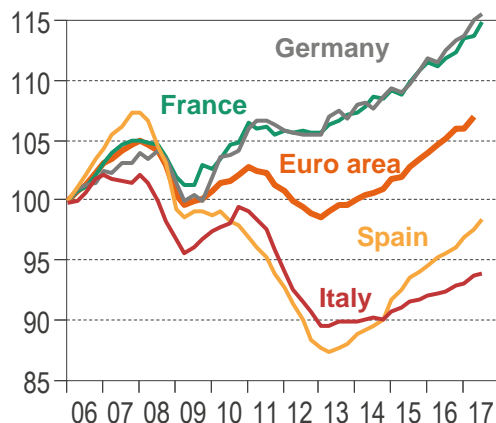
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Growth has been driven by domestic demand...

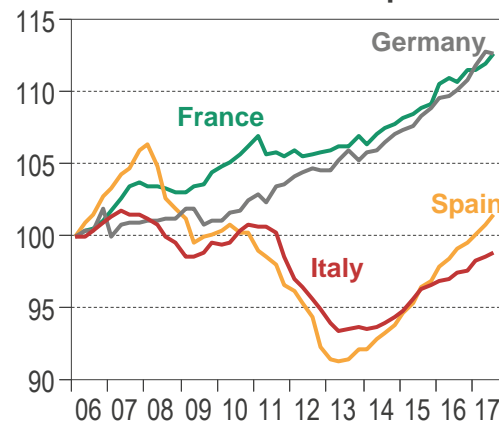
Domestic demand components

(2006 = 100, volume)

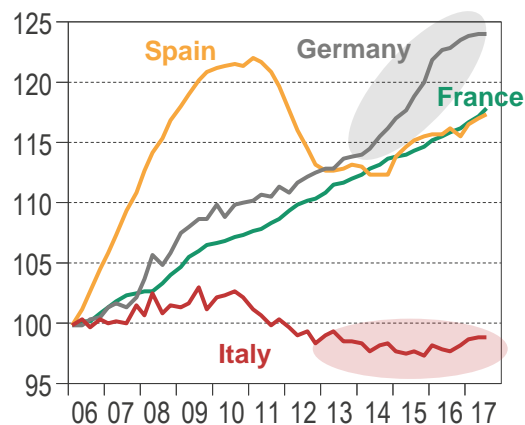
Domestic demand



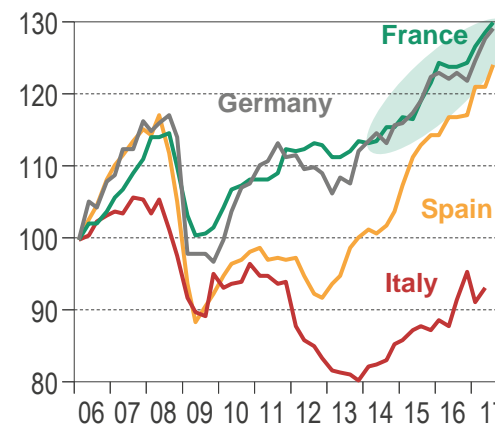
Household consumption



Government consumption



Equipment investment



EURO AREA

Emerging economies are providing the bulk of the support to euro area exports

Exports in the euro area

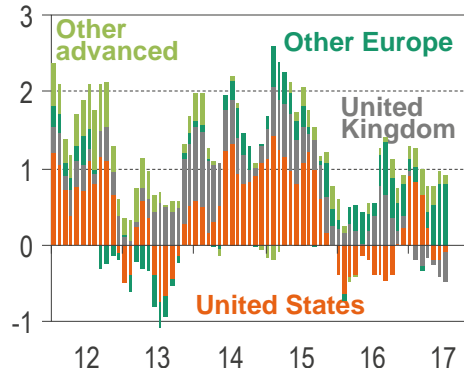
Exports orders



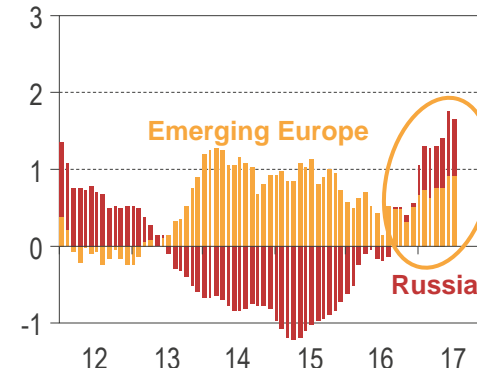
Extra euro area exports

(% year on year contributions, volume)

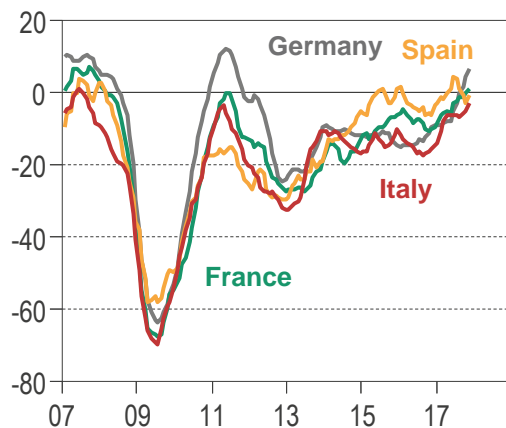
Advanced countries



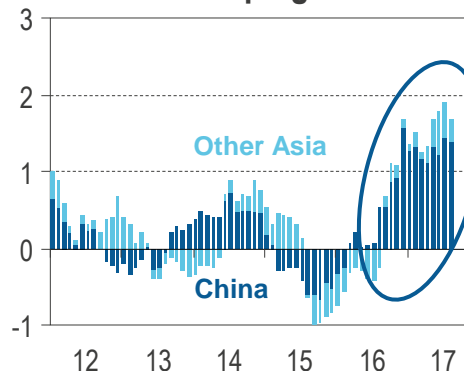
Developing Europe and Russia



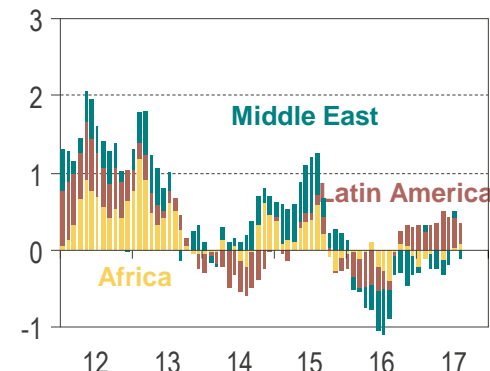
Export orders by country



Developing Asia



Other developing countries

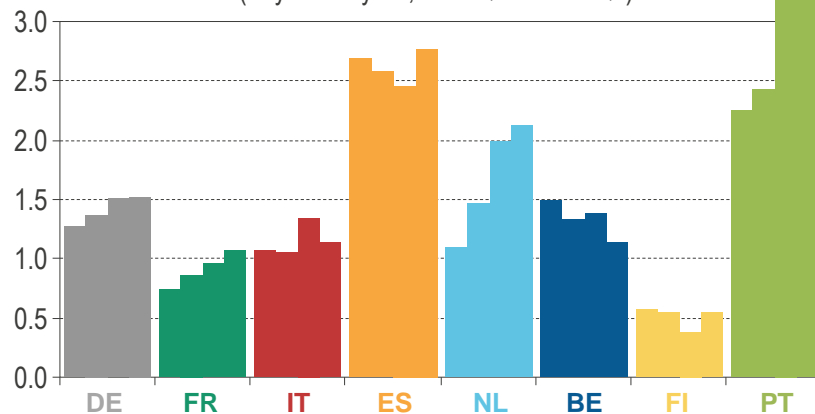


EURO AREA

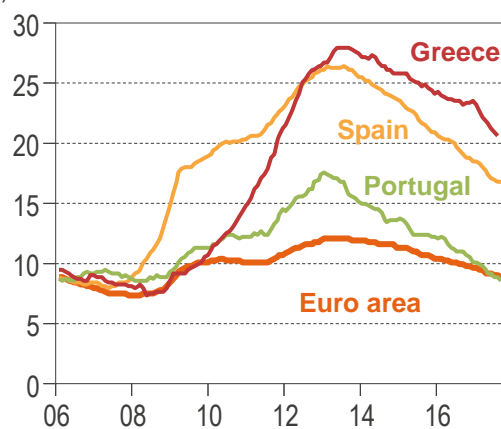
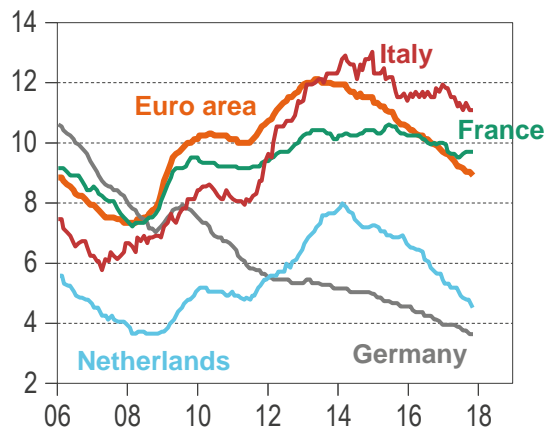
The improvement in labor markets is becoming impressive

Employment and unemployment rate

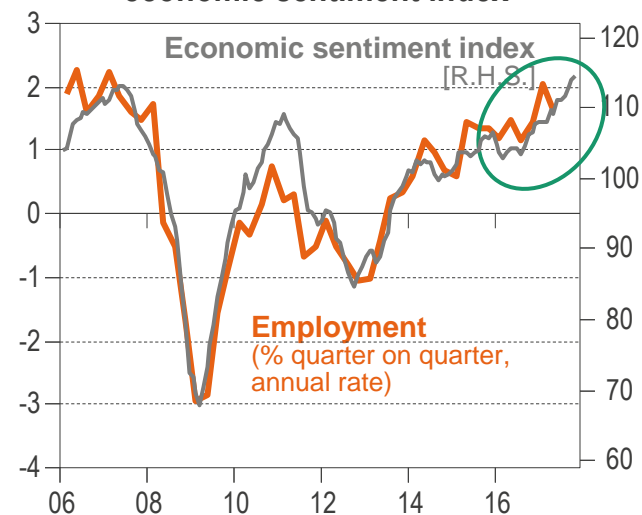
Employment growth in the Euro area
(% year on year, 2016Q3 to 2017Q2)



Unemployment rate
(%)



Employment and economic sentiment index

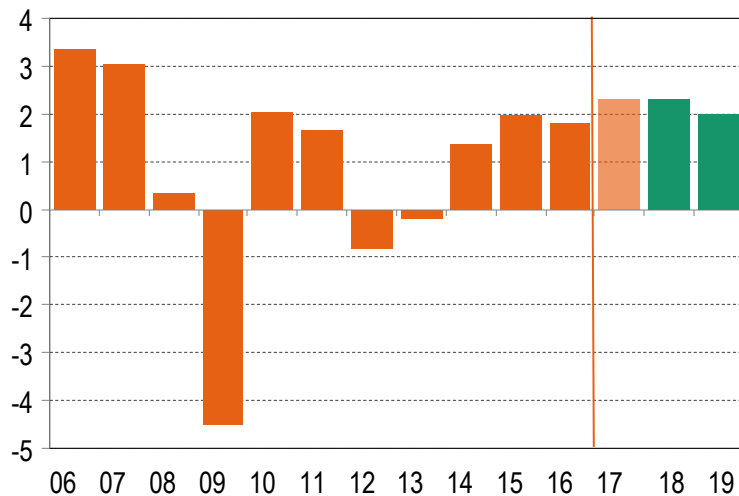


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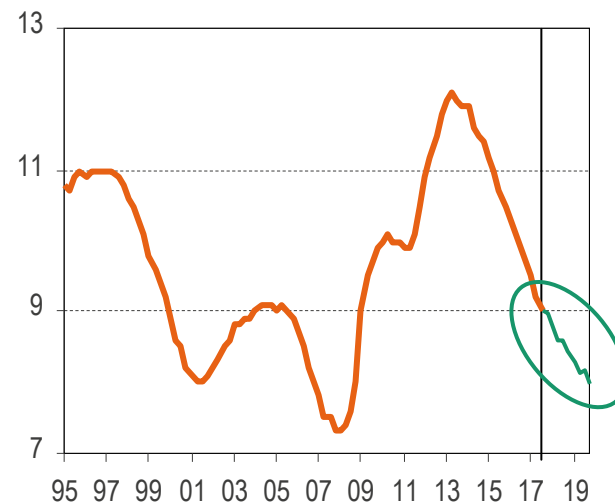
Growth should remain above 2% in 2018

Forecasts for 2018-2019

GDP growth
(%, annual rate)



Unemployment rate
(%)

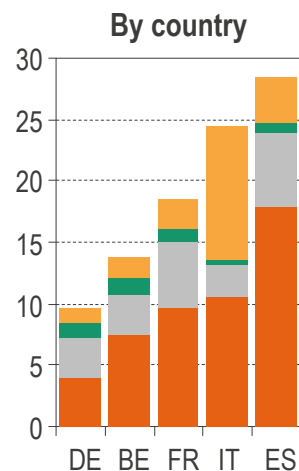
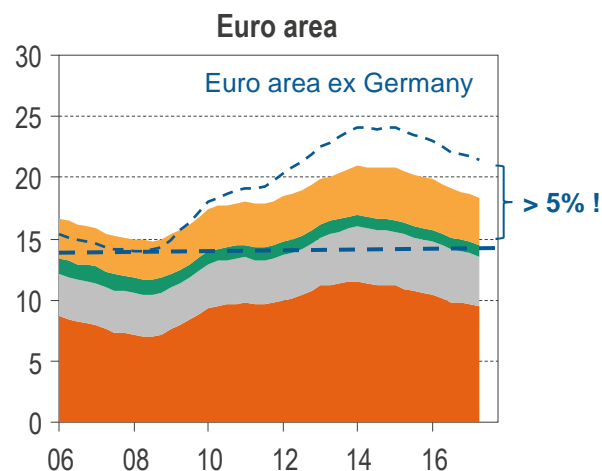


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Some wage increases could provide additional support to consumption

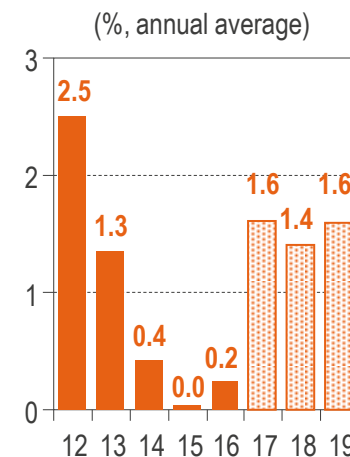
Slack in the labor market

Underemployment in the euro area (% of augmented labor force)



- Persons available to work but not seeking
- Persons seeking work but not immediately available
- Underemployed part-time workers
- Unemployed

Inflation



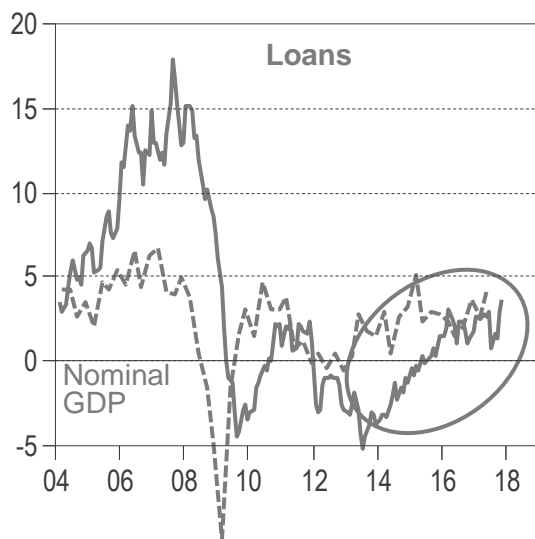
EURO AREA

ECB's policy has finally revived credit growth

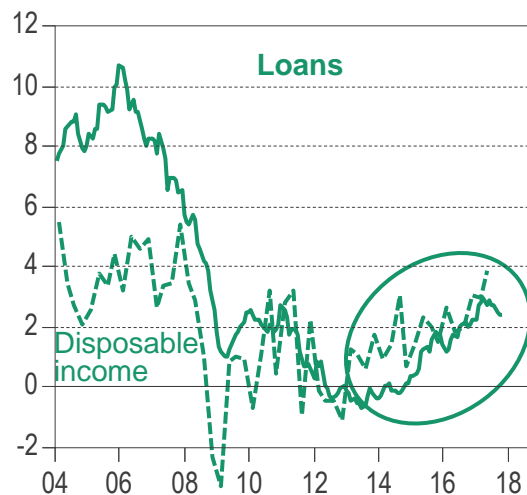
Loans to the private sector

(% 3 months on 3 months, annual rate)

Loans to non financial corporation



Loans to households



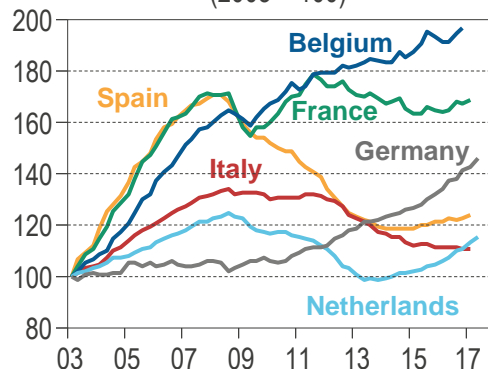
EURO AREA

Low long term rates are having secondary effects on some housing markets

Residential property prices under / over valuation

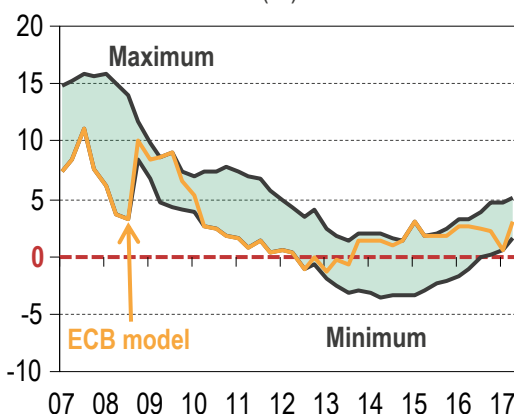
Residential property prices

(2003 = 100)



Euro area over- / under-valuation

(%)

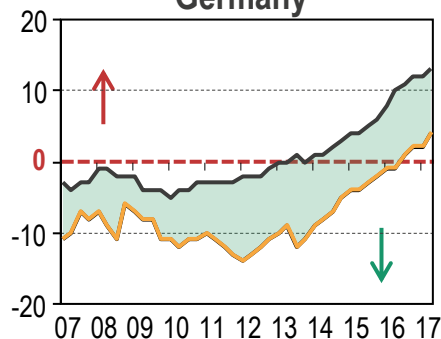


↑ Over-valuation

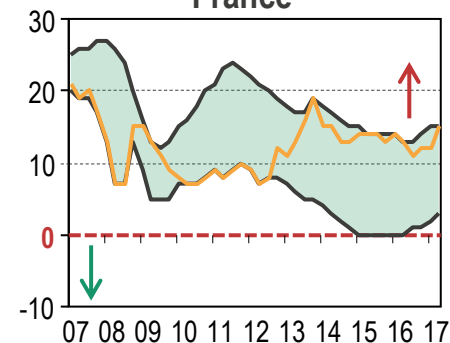
↓ Under-valuation

Germany

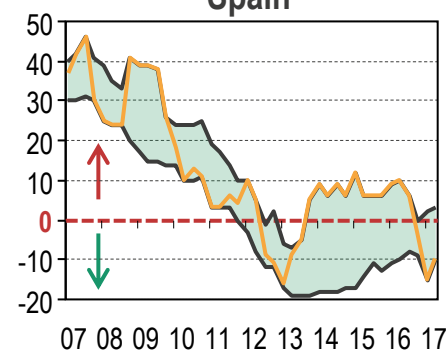
(%)



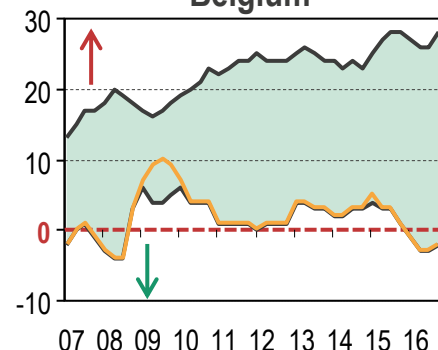
France



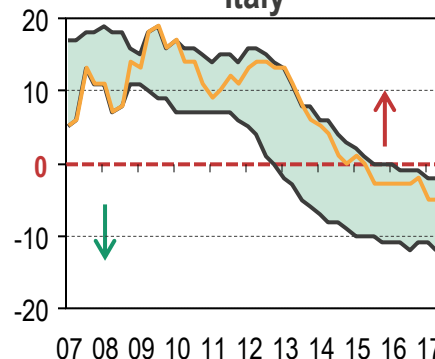
Spain



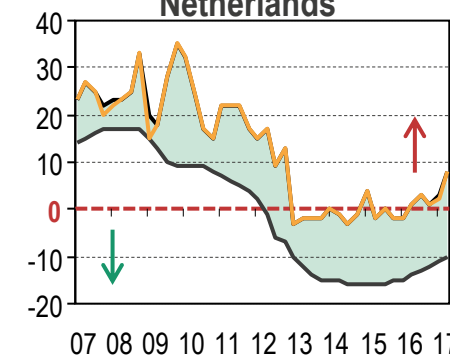
Belgium



Italy



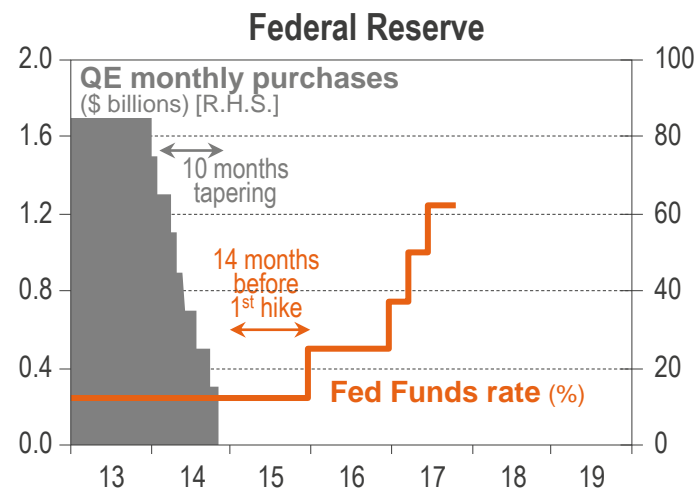
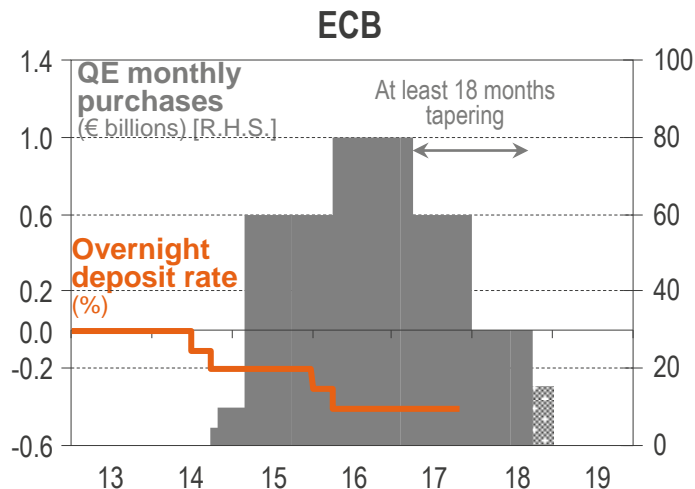
Netherlands



EURO AREA

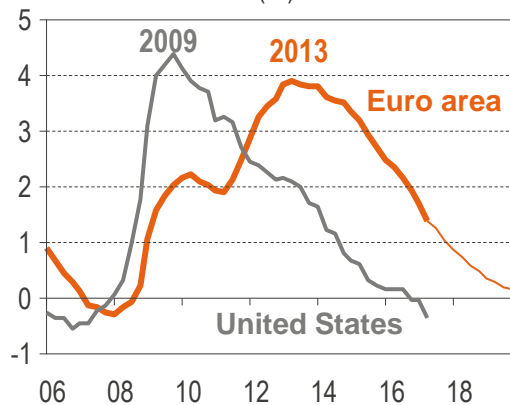
In October, the ECB has signaled a – very cautious – shift in its policy stance

Tapering and rate hikes

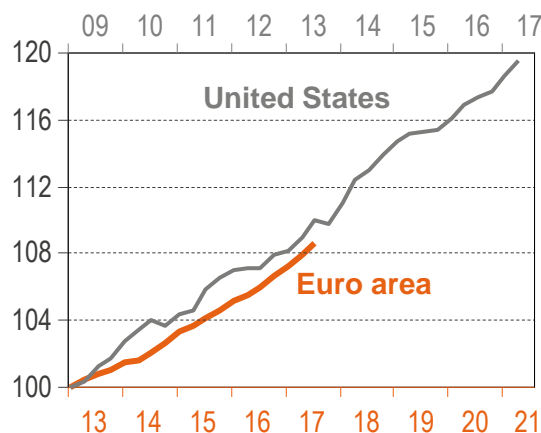


Comparison between the US and the euro area

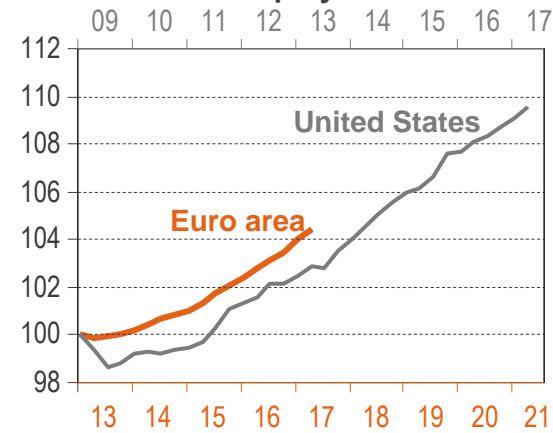
Unemployment rate minus NAIRU (%)



Real GDP



Employment

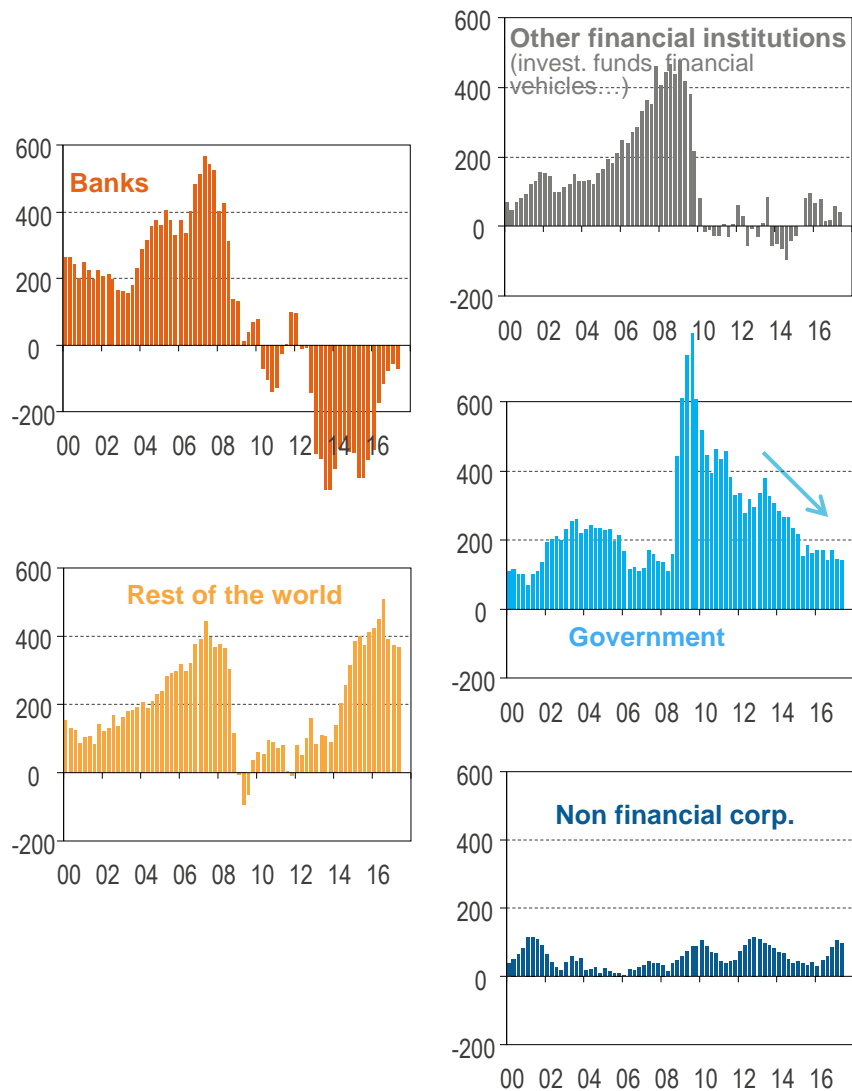


EURO AREA

Despite tapering, the upward pressure on long term rates will be moderate (I)

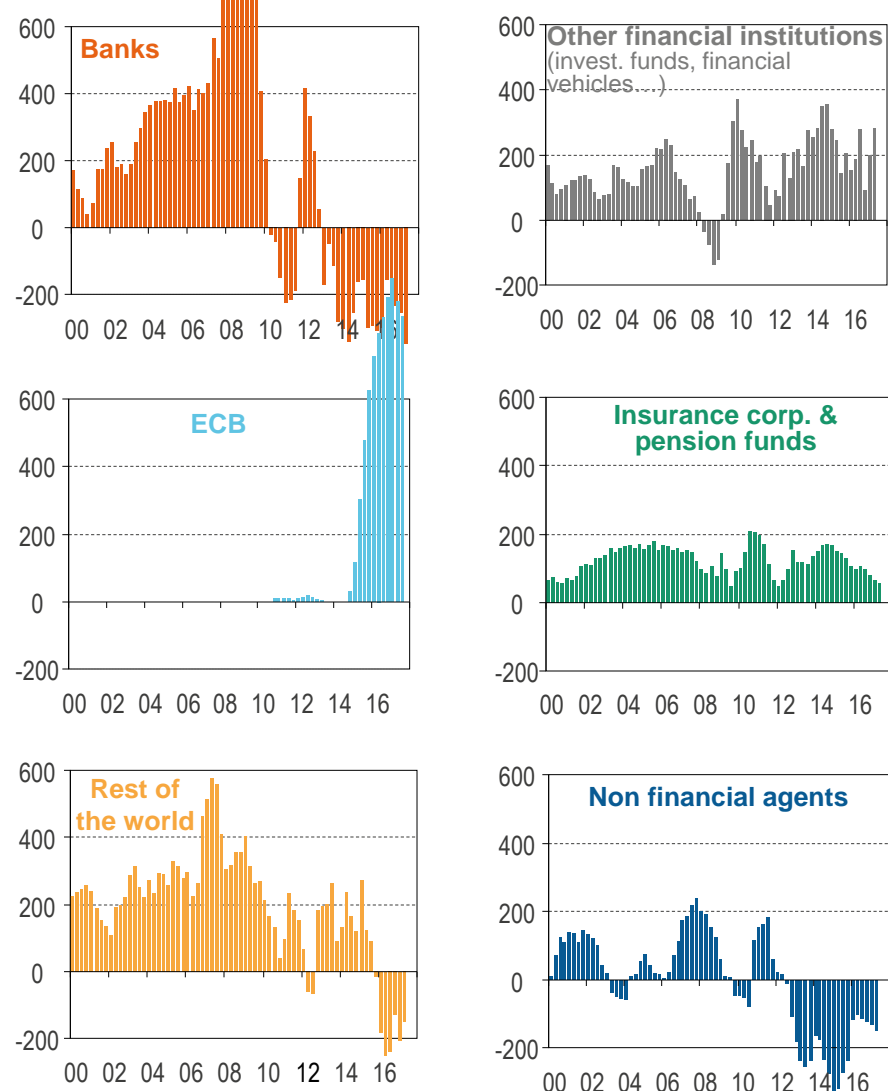
Net suppliers of debt securities

(€ billion, moving average over 4Q, annual rate)



Net buyers of debt securities

(€ billion, moving average over 4Q, annual rate)

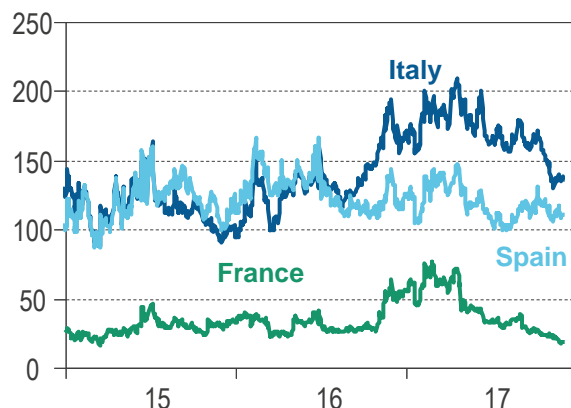


EURO AREA

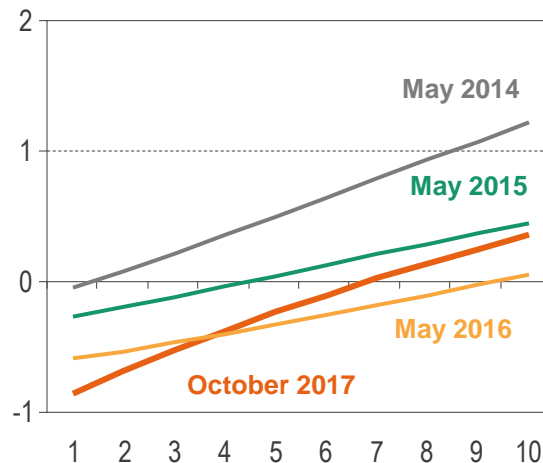
Despite tapering, the upward pressure on long term rates will be moderate (II)

Interest rates in the euro area

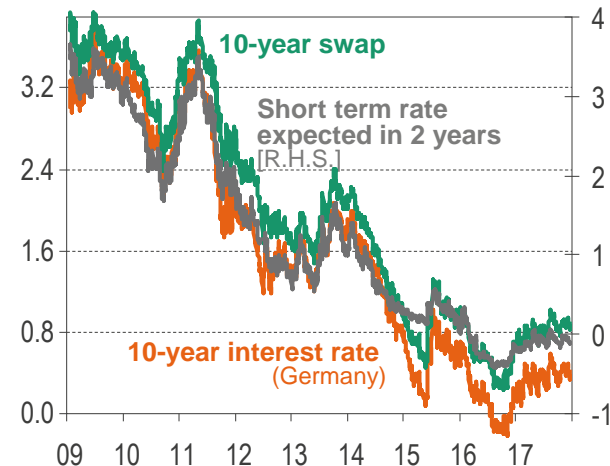
Spread versus German 10-year Bund
(basis point)



German yield curve
(%)



10-year interest rates and expected short rates (%)



Euro swap rates forecasts

	Nov. 22, 2017	End of 2018
(I) 2-year interest rate	-0.2%	0.1%
(II) 3-year interest rate in 2 years	0.5%	1.4%
(III) 5-year interest rate in 5 years	1.4%	2.3%
10-year interest rate	0.8%	1.6%

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