



US Macro & Interest Rate Outlook



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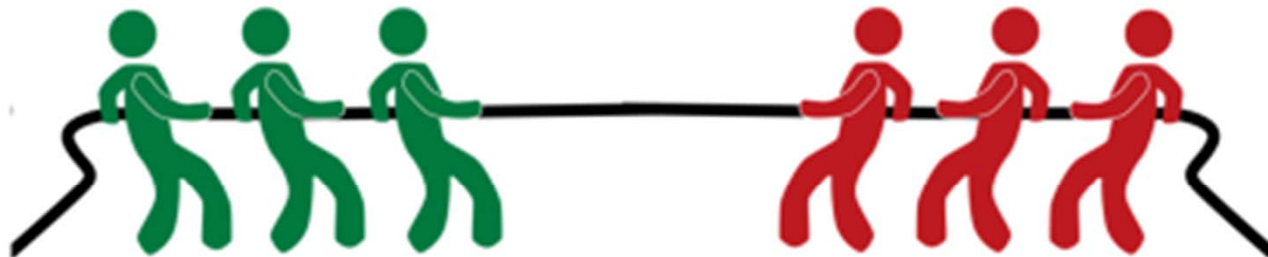
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Stronger US growth comes with risks

What will be the impact of Donald Trump?

- Tax cuts
- More infrastructure spending
- Less regulation
- Massive uncertainty
- Trade protectionism
- Anti-immigration



Elevated risk of a "trial and error" presidency

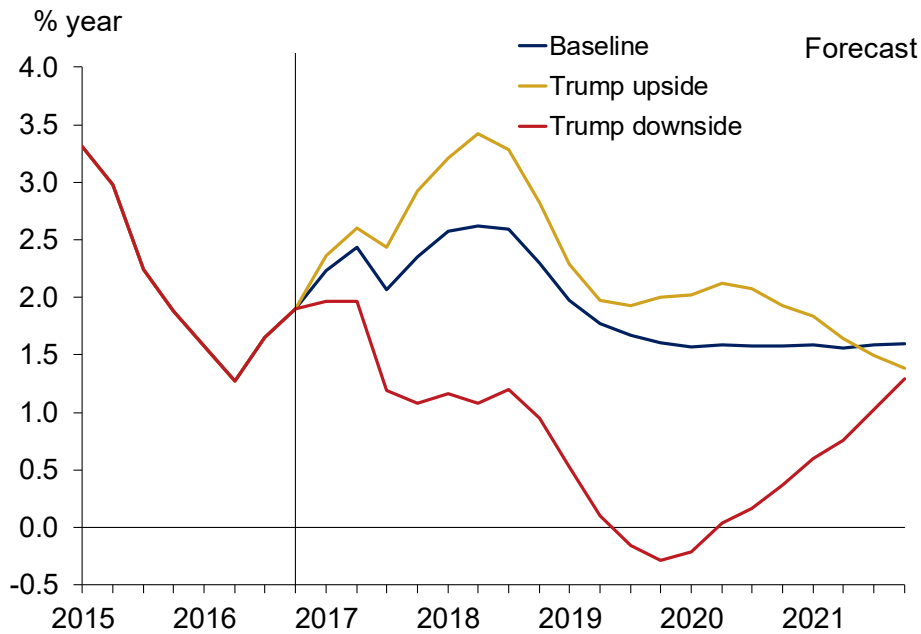


Three Trump scenarios (and an infinite set of possibilities)

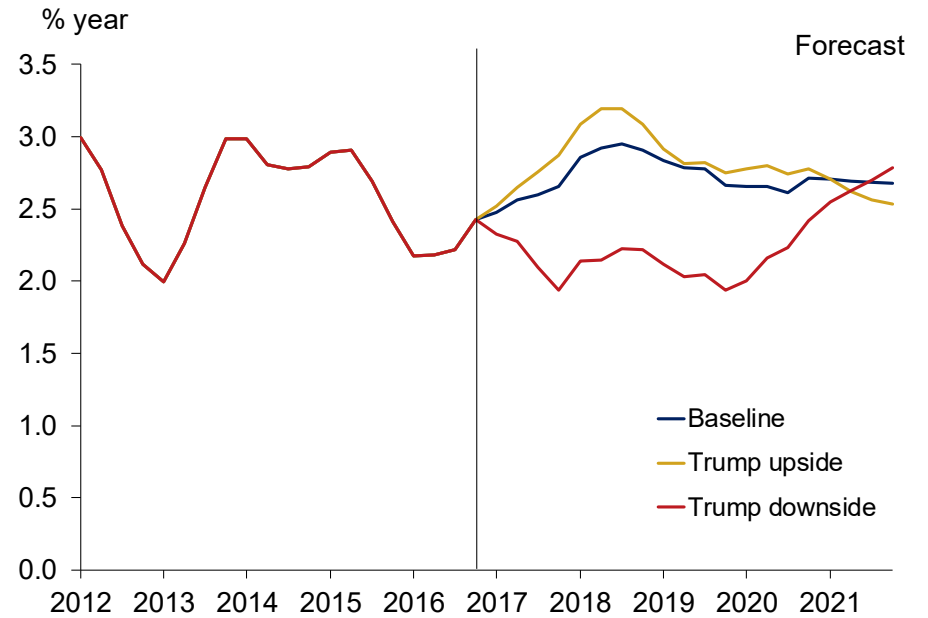
2017-2026	<u>Baseline</u>	<u>Upside</u>	<u>Downside</u>
Tax cuts	\$1 trillion (w/ some benefits to low income families)	\$2 trillion (w/ some benefits to low income families)	\$500 billion (as regressive as current proposal with 50% tax cuts for top 1%)
Infrastructure	\$200 billion	\$250 billion	-
Spending offsets	\$300 billion (back loaded)	\$350 billion (more back loaded)	\$300 billion
Tax revenue offsets	+\$225 billion (foreign profits)	+\$500 billion (foreign profits + repeal expenditures)	+\$225 billion (foreign profits)
Uncertainty	Moderate	Dissipates rapidly	Elevated
Trade	Threats to renegotiate agreements and implement tariffs on only limited & targeted restrictions	Status quo	Elevated protectionism (45% tariff on China & 35% on Mexico)
Regulation	Loosened modestly	Loosened widely	Status quo
Immigration (via labor force)	-600,000/year	Status quo	-1,000,000/year

The impact on President Trump on growth

US: GDP growth



World: GDP growth



Economy is late cycle

Stage of Cycle	Economic indicator	Coincident or Leading Indicator
Mid-cycle	Housing Permits	Leading
	Yield Curve	Leading
	Industrial Production	Coincident
	Manufacturing and Trade Sales	Coincident
Approaching late-cycle	Corporate bond debt outstanding	Leading
Late -cycle	Output gap	Coincident
	Jobless Claims	Leading
	S&P 500 Stock Index	Leading
	Manufacturing Hours	Leading
	Payrolls	Coincident
	Personal Income	Coincident

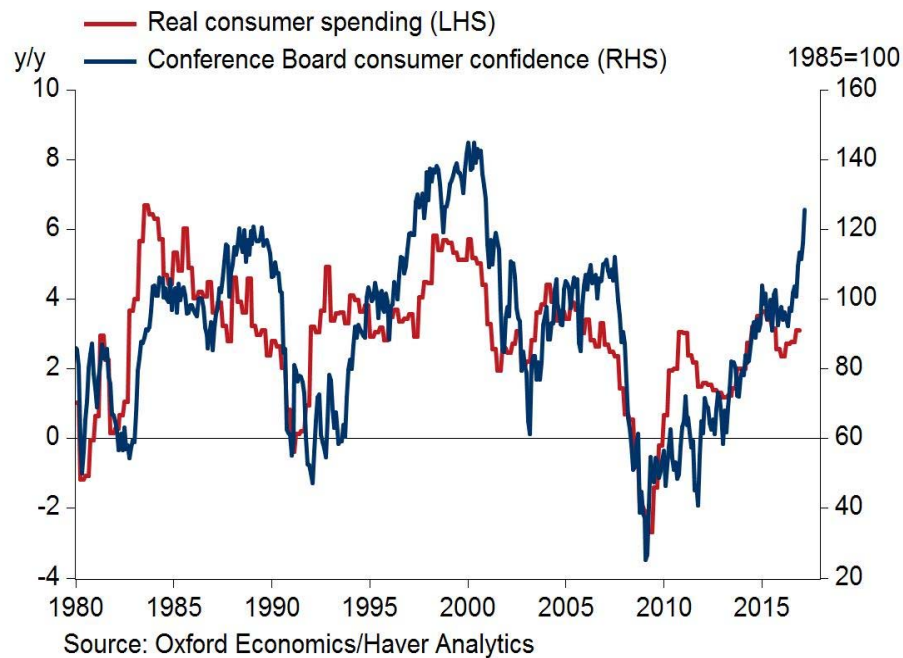
Source: Oxford Economics, The Conference Board

Trump stimulus does not lift supply side much

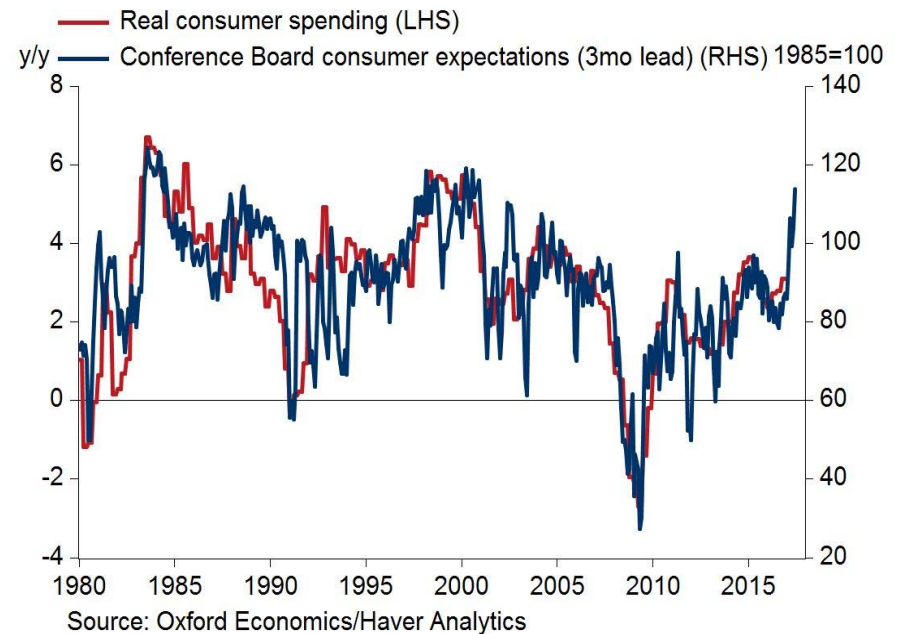
Real potential output growth (2018-2021)	CAGR (%)
Baseline	1.67
Without Trump policy mix (fiscal, trade, immigration)	1.73
With Trump fiscal stimulus, but without trade & immigration restrictions	1.84

Consumer survey data lead hard data

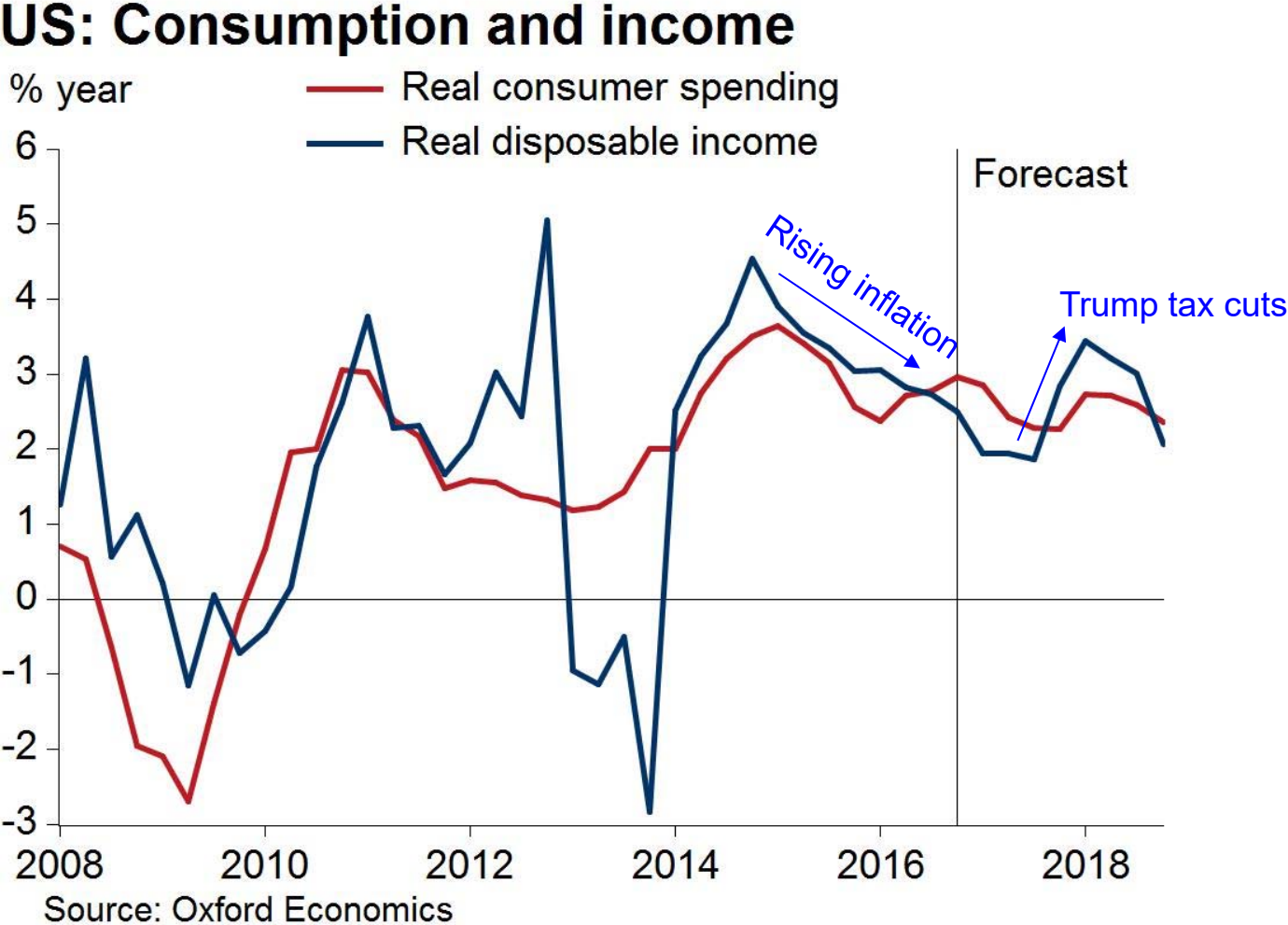
US: Consumer spending vs confidence



US: Consumer spending vs confidence



Income growth solid but *slowing* after oil 'sugar rush'



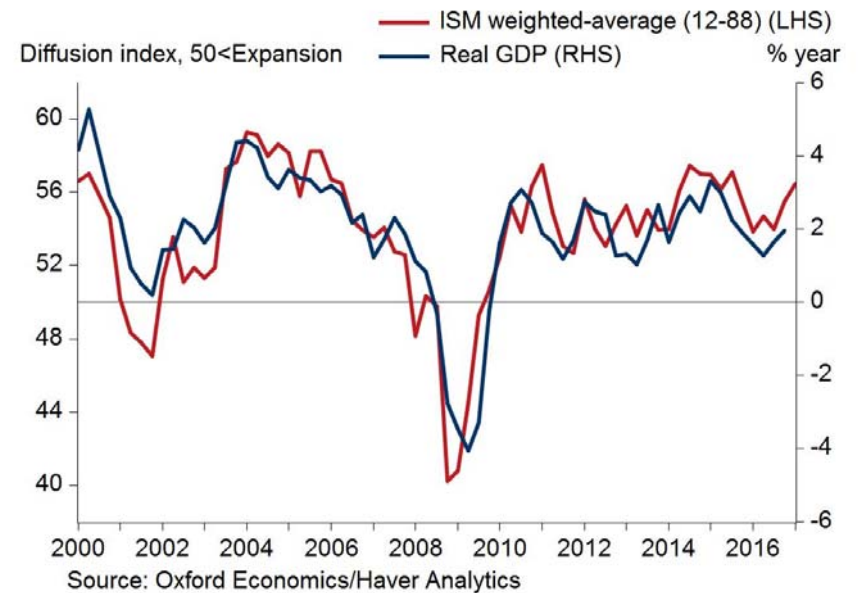
Manufacturing survey data run ahead of hard data

US: ISM new orders lead core orders capital gds orders



Source: Oxford Economics/Haver Analytics

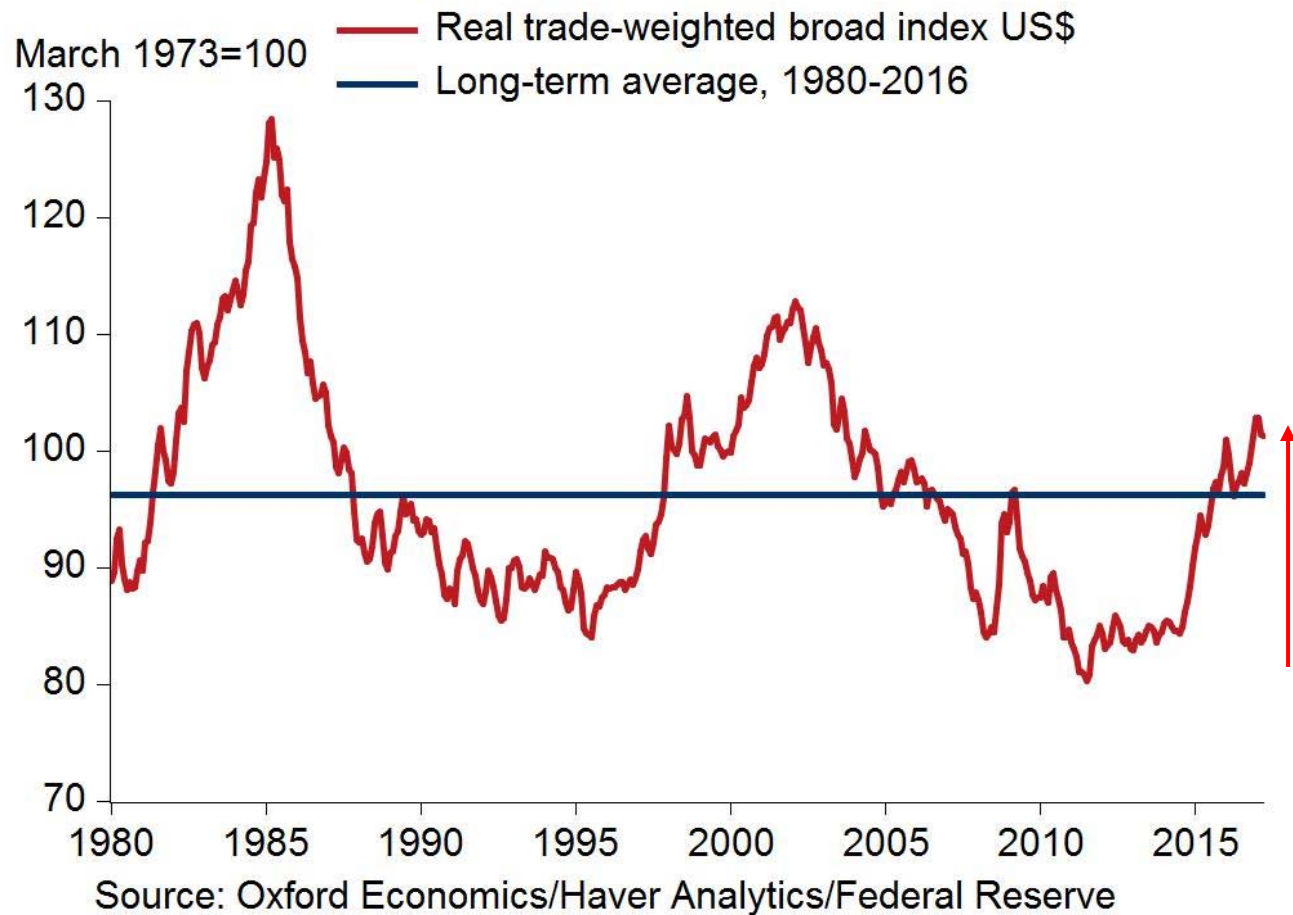
US: ISM indices and real GDP



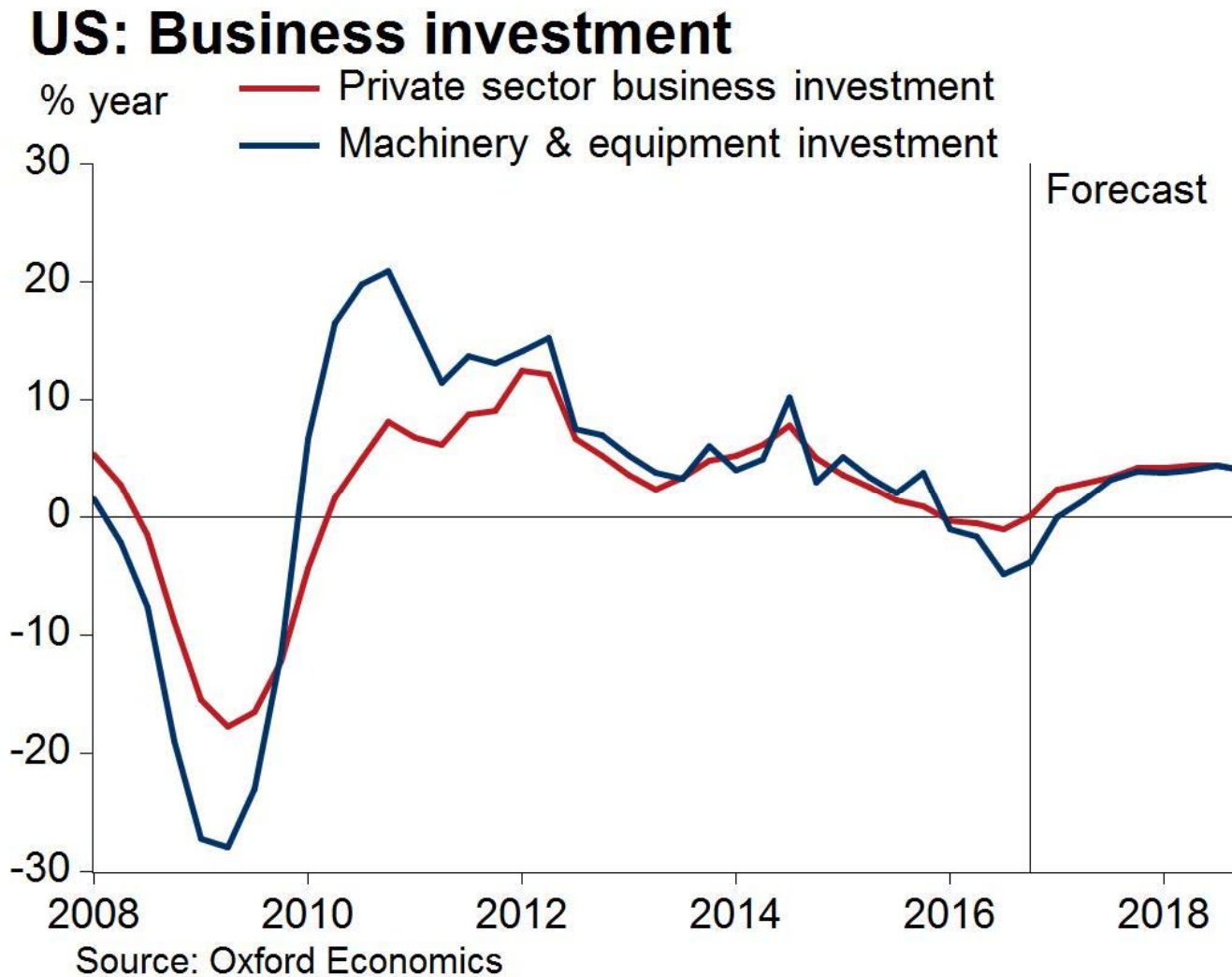
Source: Oxford Economics/Haver Analytics

Strong US dollar weighs on US exports

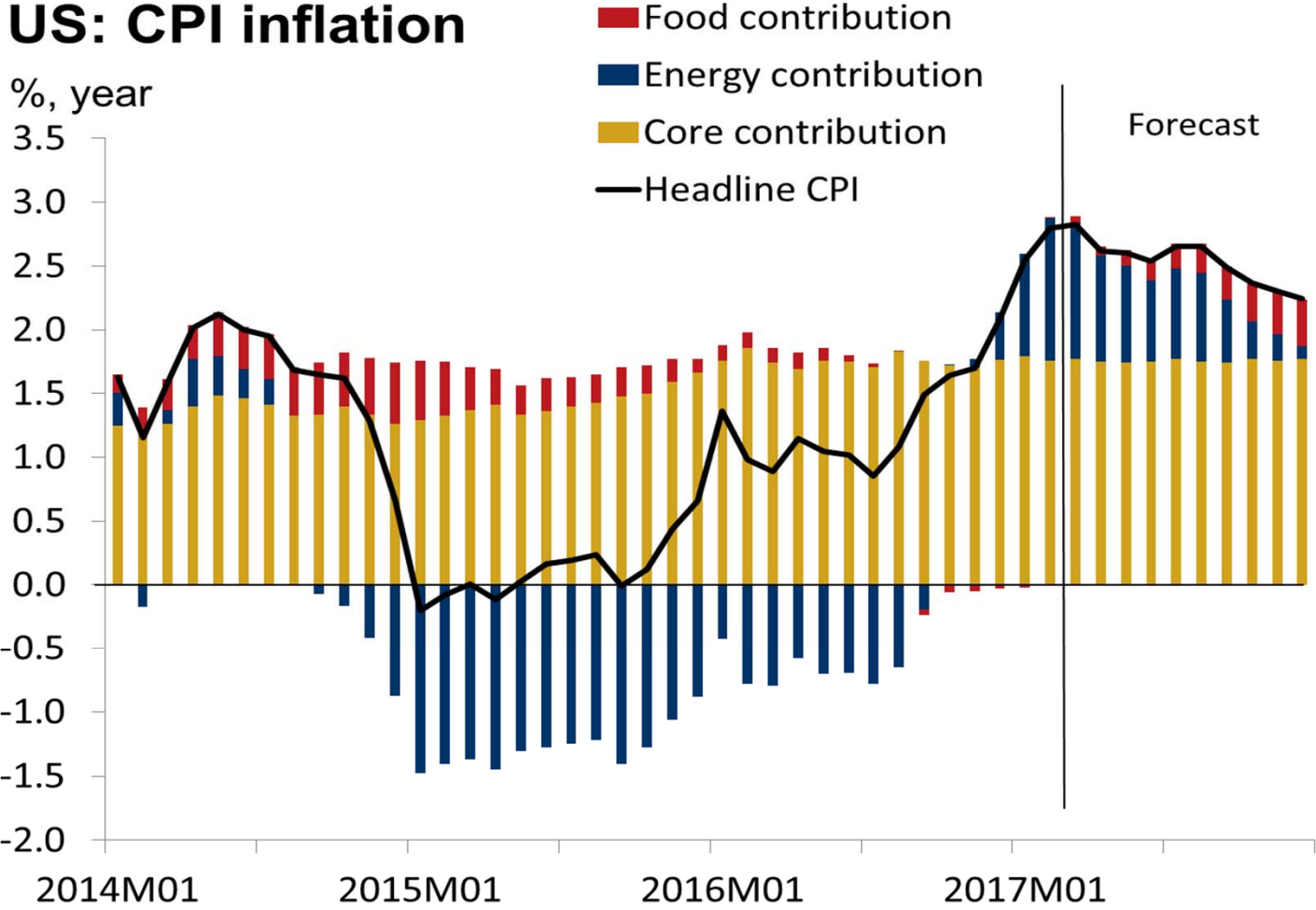
The US dollar in perspective



We expect modest US momentum going forward

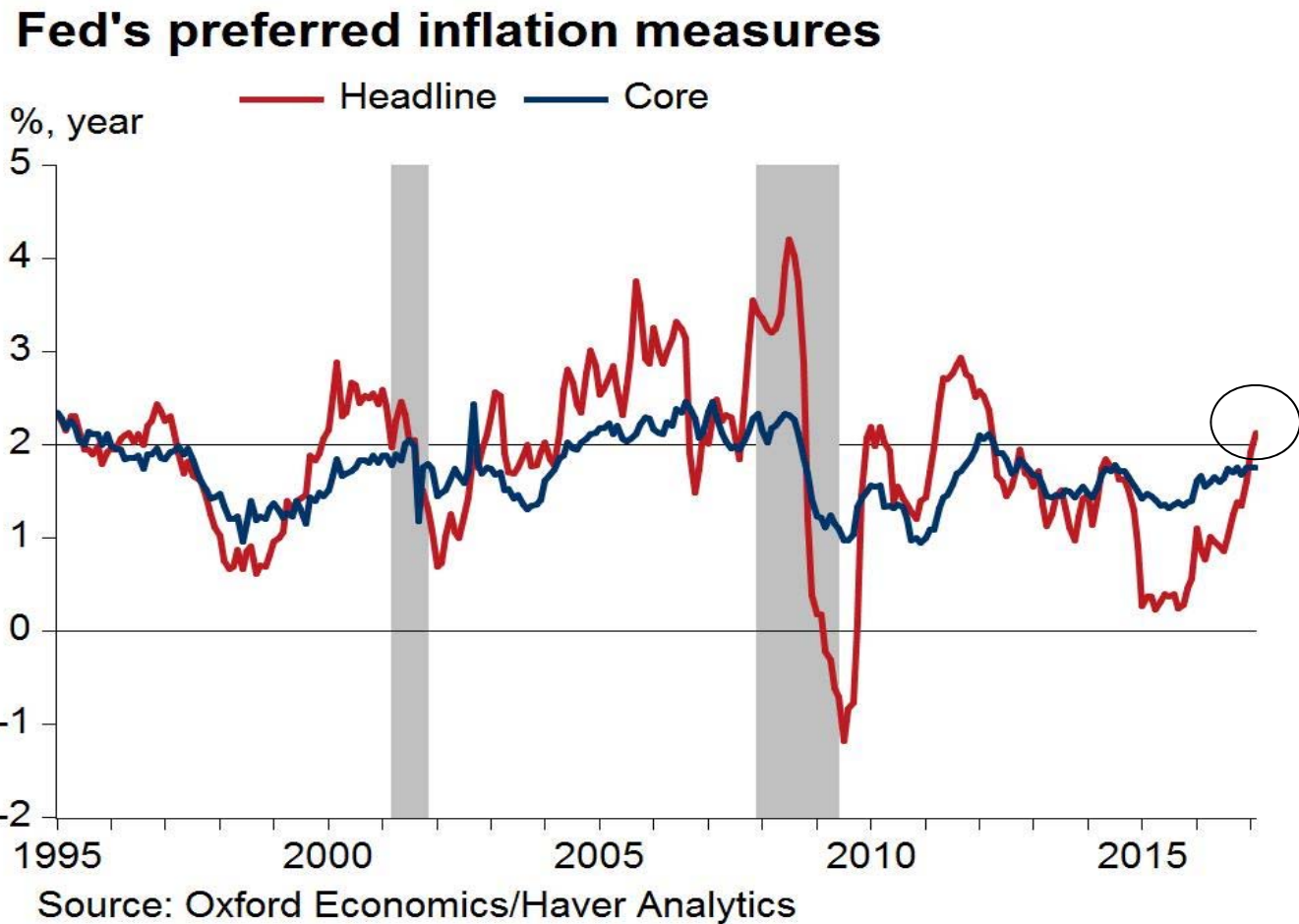


Inflation expected to firm above 2%



Source: Oxford Economics

PCE price index also reaches 2% target



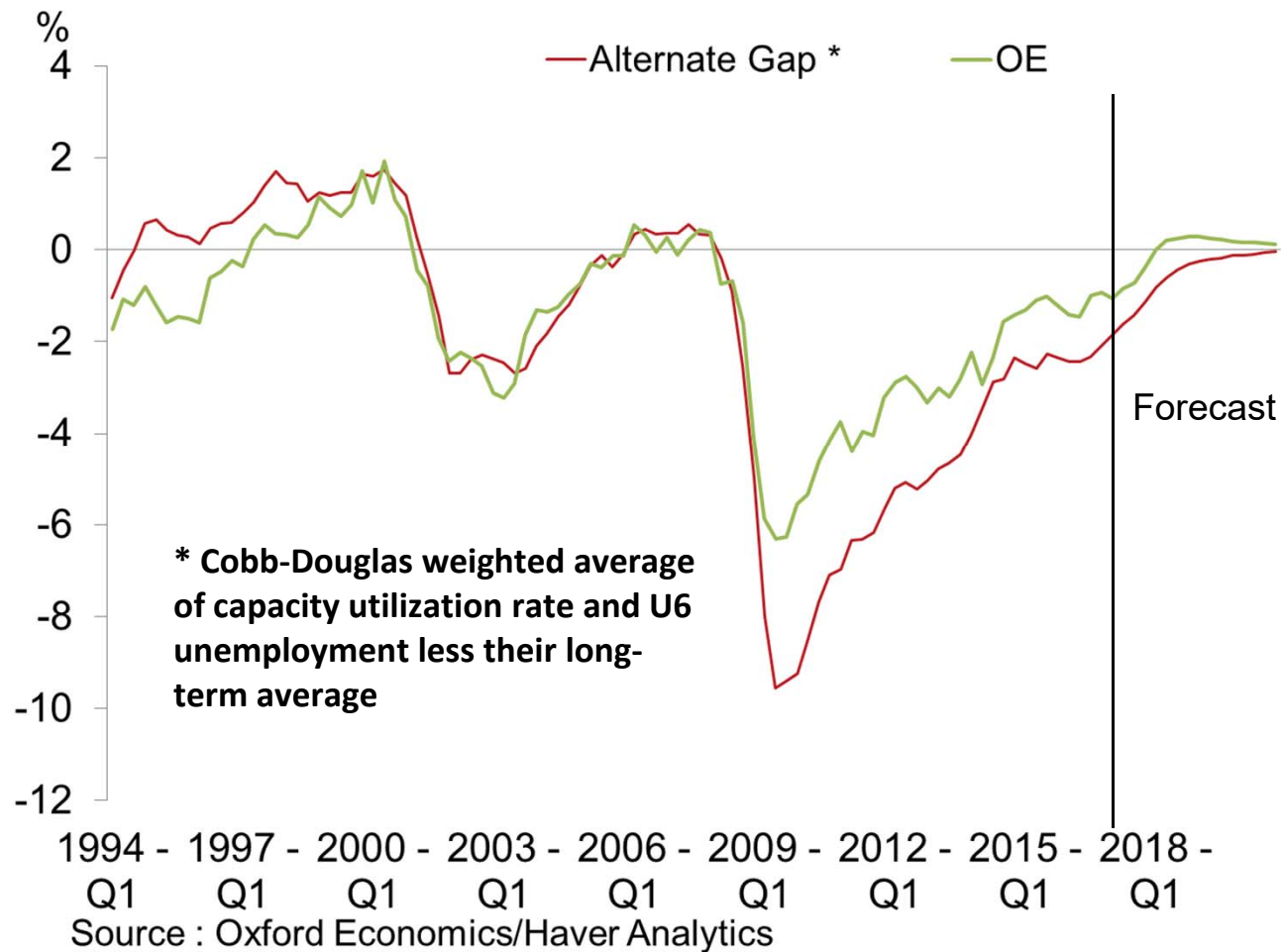
Labor market gap closed, slack closing in capital market

US: Divergent market gaps



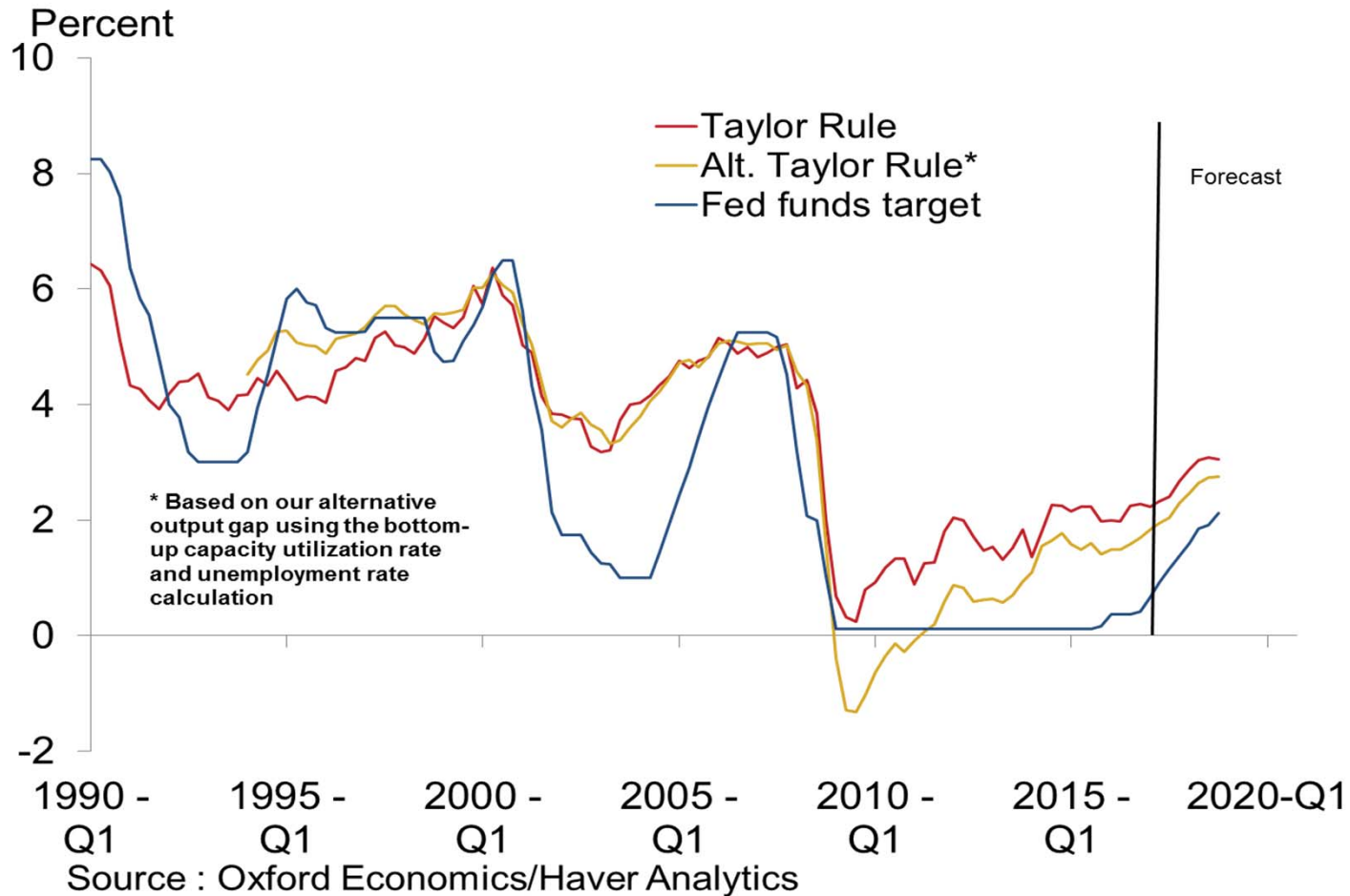
Output gaps narrowing

US: GDP output gap estimates



Fed lags behind Taylor Rule

US: Fed lagging behind Taylor Rule



Markets lagging Fed forecast – balance sheet plays a role

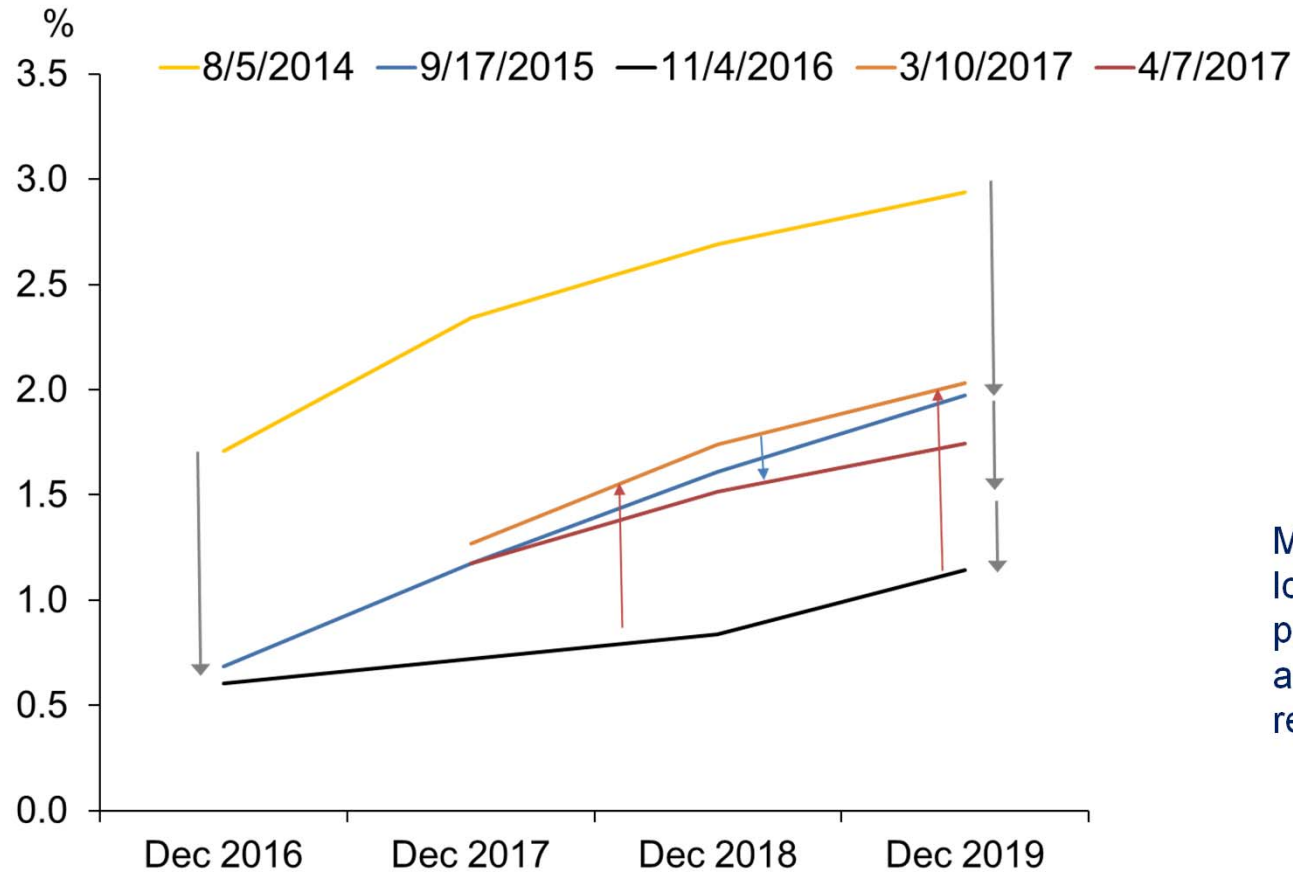
Expectations of Fed funds rate (%)			
Month	Market implied rate Eurodollar futures yield* as of April 7, 2017	Fed Dot Plot median rate forecasts as of March -2017	Oxford Economics forecast as of March-2017
Dec. 2017	1.18	1.38	1.38
Dec. 2018	1.52	2.13	2.13
Dec. 2019	1.75	3.00	2.88
Dec. 2020	1.92	3.00	2.88
Long-Term	---	3.00	2.88

Source: CME group, Federal Reserve, Oxford Economics

*Adjusted for estimated risk and term premiums

Market rate expectations – shifting down/up/down

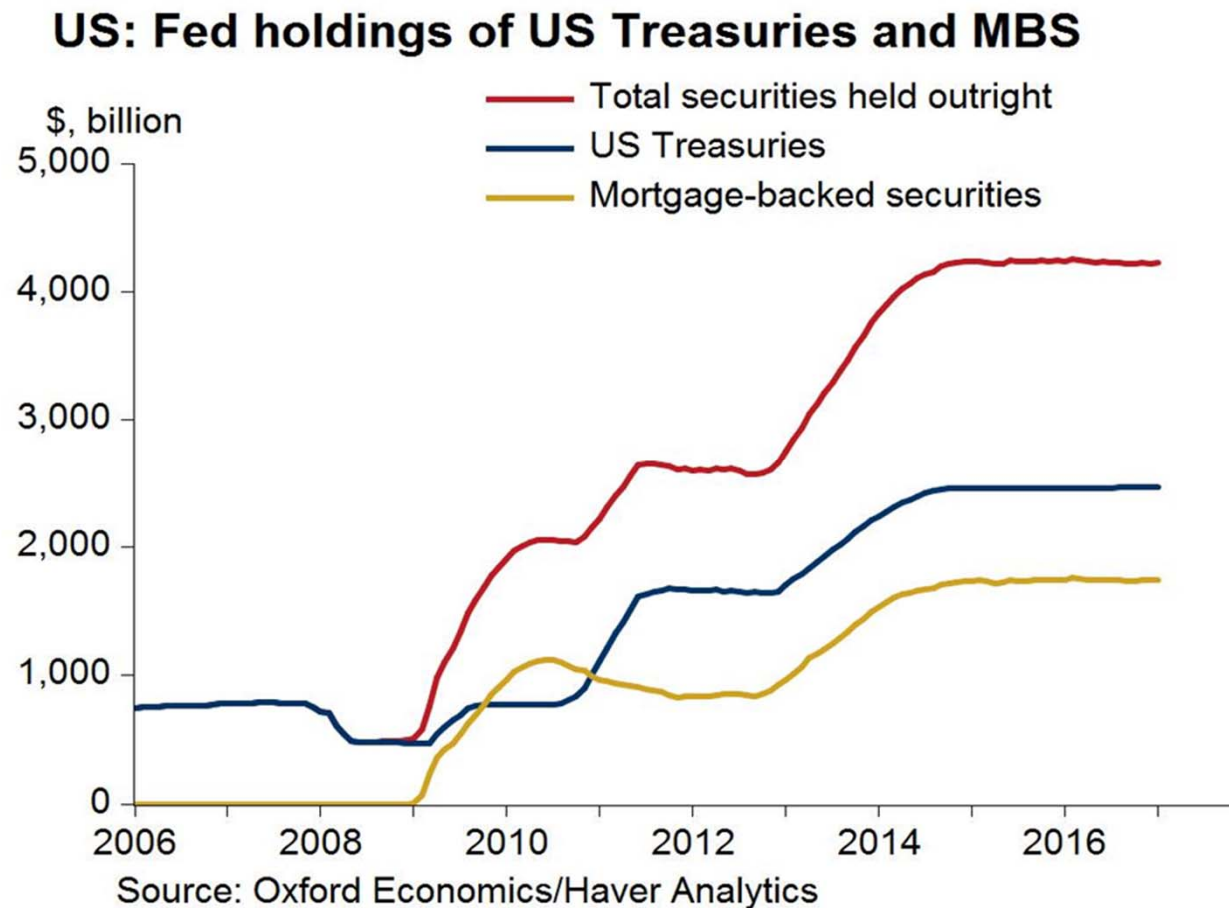
US: Federal funds rate expectations



Markets should not look for a protracted pause in rate hikes as balance sheet reduce.

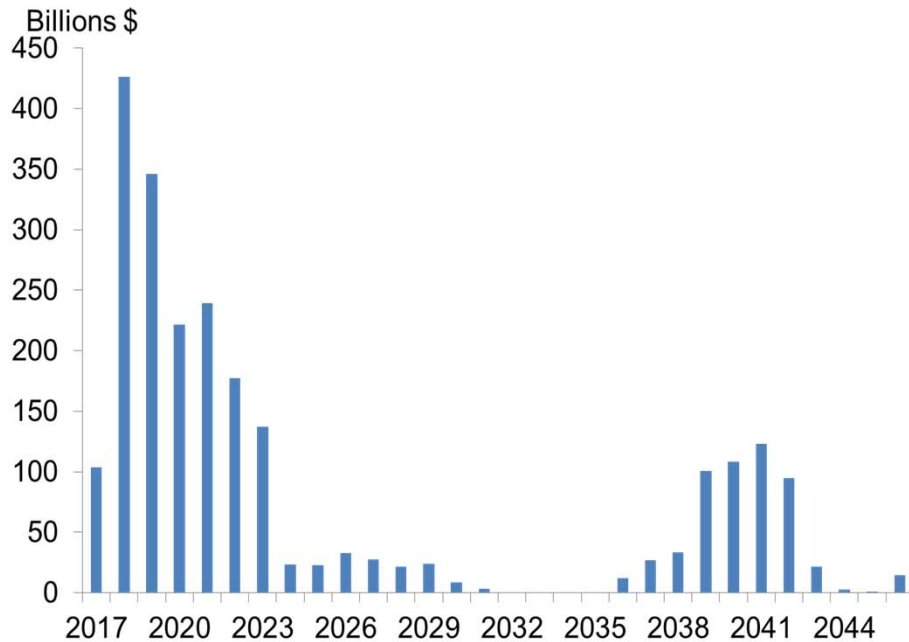
Source: CME/Federal Reserve/Oxford Economics

Fed balance sheet holdings – time to start shrinking



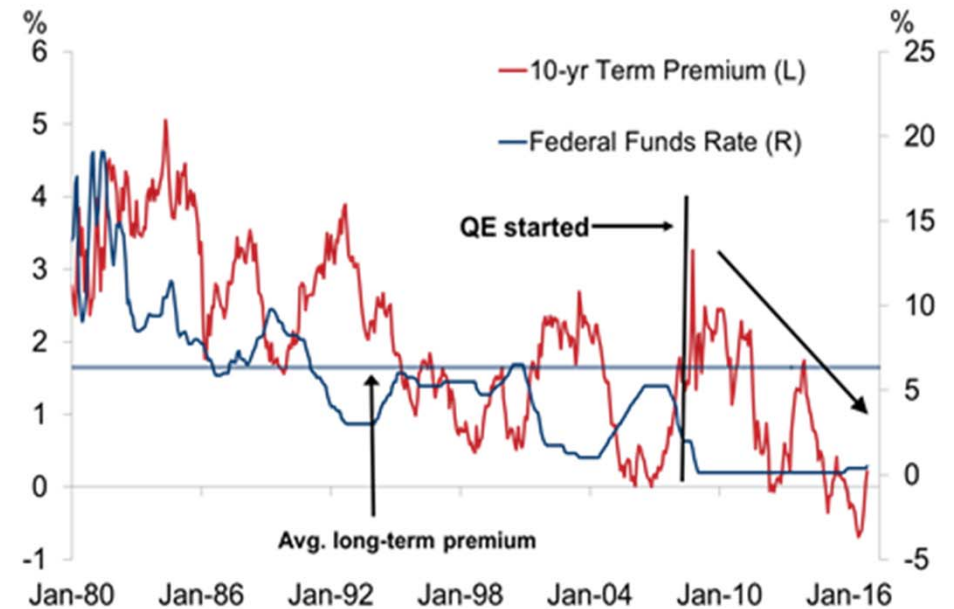
Fed considering timing & mechanics of shrinking its balance sheet

US: Fed's holdings of US Treasuries by maturity



Source : Oxford Economics/Federal Reserve

US: Bond term premia key variable as Fed unwinds QE

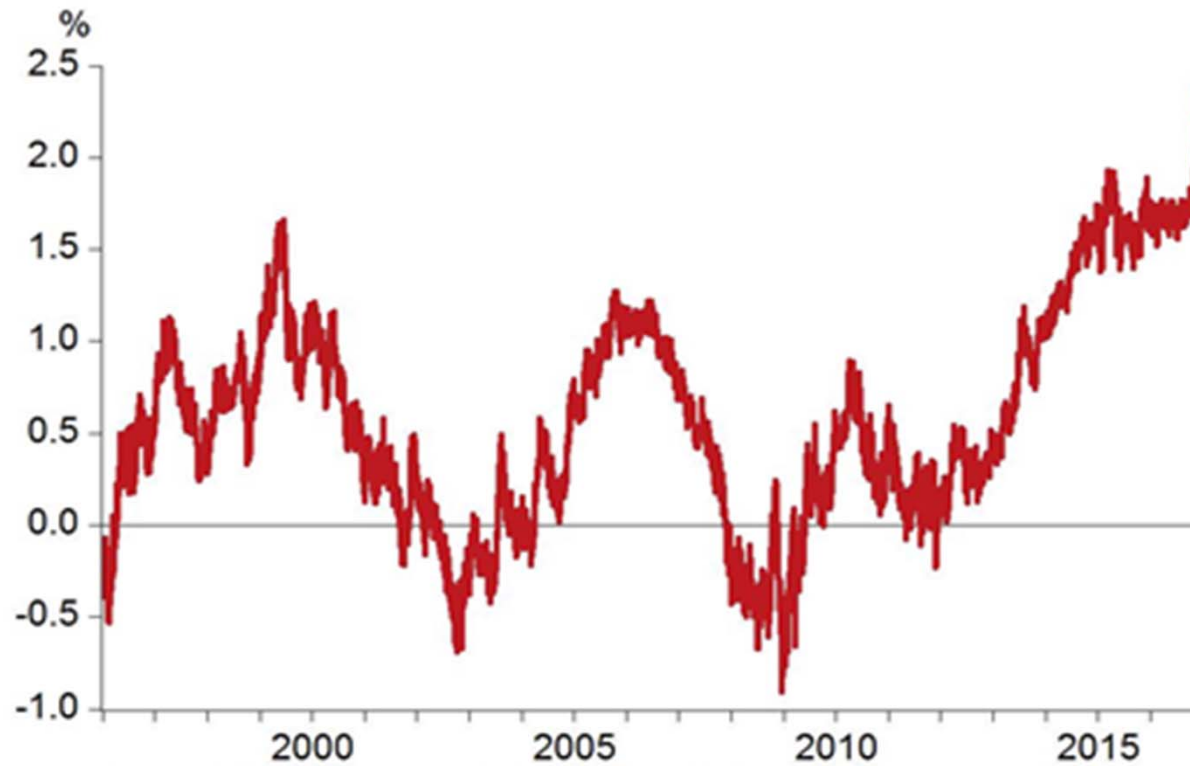


Source: Oxford Economics/Haver Analytics

Foreign capital inflows due to interest rate differentials

US: Gap in yields relative to Germany at historic highs

— US 10-year yield less German 10-year yield



Source: Oxford Economics/Haver Analytics

OE interest rate forecasts – moderate rise

Interest rate forecasts (%)			
Quarter-end	Fed funds	10-year note	Spread 10-FF
2017 Q2	1.13	2.48	1.35
Q3	1.38	2.58	1.20
Q4	1.38	2.63	1.25

Source: Oxford Economics

Interest rate forecasts (%)			
Quarter-end	Fed funds	10-year note	Spread 10-FF
2018 Q1	1.63	2.74	1.11
Q2	1.88	2.84	0.96
Q3	2.13	2.95	0.82
Q4	2.13	3.06	0.93

Thank you!

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