

The (US) economic outlook: themes, issues, risks

policy pivots and “de-risking” support continued expansion

Michigan Consensus Revenue Estimating Conference

Lansing, MI; 10 January 2020

Dr. Joel Prakken, VP, Chief US Economist, Co-head of US Economics

+1 314 779 1980

Joel.Prakken@ihsmarkit.com

Confidential. © 2018 IHS Markit™. All Rights Reserved.

Assume...a can opener

- Abroad
 - > No-deal Brexit (and deep UK recession) avoided
 - > Saudi oil production restored after Sept attack; no escalation in threat to global oil supplies
 - > China avoids hard landing
 - > Other potential global hot spots (N. Korea, etc.) remain on simmer
- At home
 - > Federal govt funded through FY21 at BBA19 levels (extended); debt ceiling raised in July 2021
 - > Fed on hold in 2020, begins tightening in mid-2021 to prevent inflation rising much > 2% objective
 - > “Phase one” tariff rollback; gradual waning of trade policy uncertainty; no allowance for USMCA
 - > GM rebuilds inventories through Q1 following 6-week strike in late 2019
 - > Boeing MAX 737s production suspended in Q1, restored by H2 following re-certification in late March
 - > No negative effects from impeachment enquiry, election uncertainty

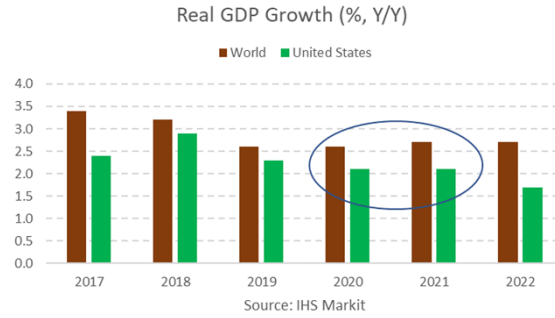
Confidential. © 2018 IHS Markit™. All Rights Reserved.

Global growth slowed in 2018-19, but now is stabilizing

Respectable, but concerns linger about downside risks: trade, Brexit, etc.; and now, US vs Iran

A Quick Look at the Numbers...

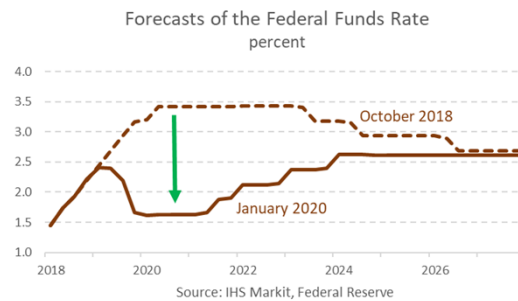
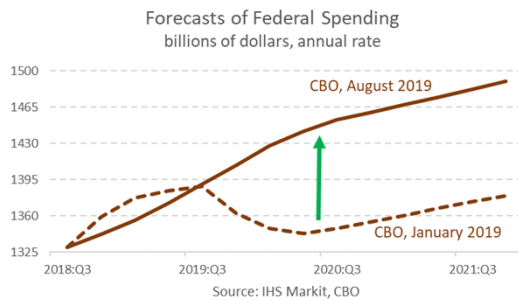
Real GDP Growth (% Y/Y)	2017	2018	2019	2020	2021	2022
World	3.4	3.2	2.6	2.6	2.7	2.7
United States	2.4	2.9	2.3	2.1	2.1	1.7
Canada	3.2	2.0	1.6	1.5	1.3	1.4
Eurozone	2.7	1.9	1.2	0.9	1.0	1.2
United Kingdom	1.9	1.4	1.2	0.6	0.8	1.1
Japan	2.2	0.3	1.1	0.6	0.7	0.4
China	6.7	6.6	6.2	5.8	5.6	5.5
India	7.1	6.8	4.8	5.5	6.2	6.7
Brazil	1.3	1.3	1.1	1.7	1.7	1.6
Russia	1.7	2.2	1.1	1.6	1.5	1.7



Source: IHS Markit; 7 January 2020

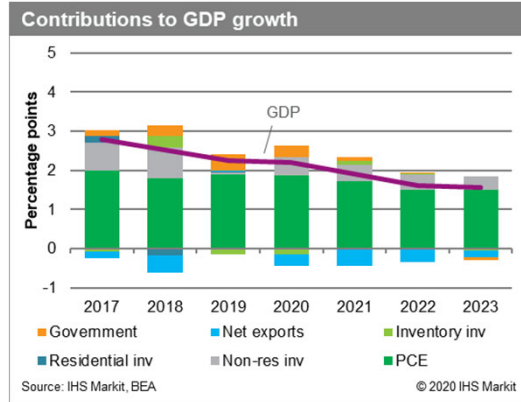
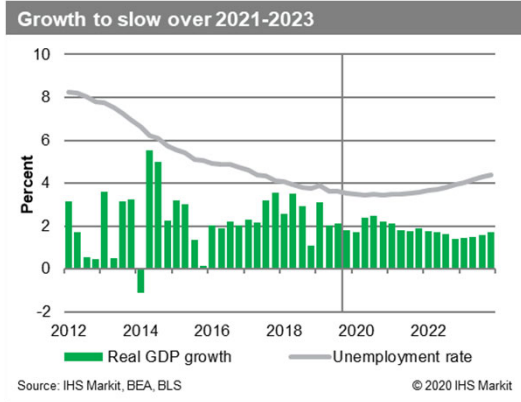
In the US, policy pivots towards fiscal & monetary accommodation

The 2019 Budget Act & Fed's 2019 dovish turn (as "insurance policy" against downside risks) supports continued expansion



Consumers carrying water for now; GDP growth to slow after 2021

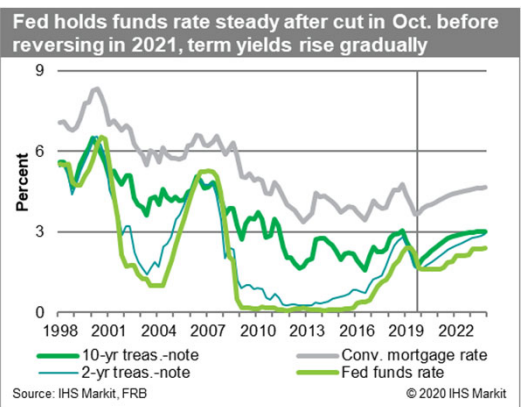
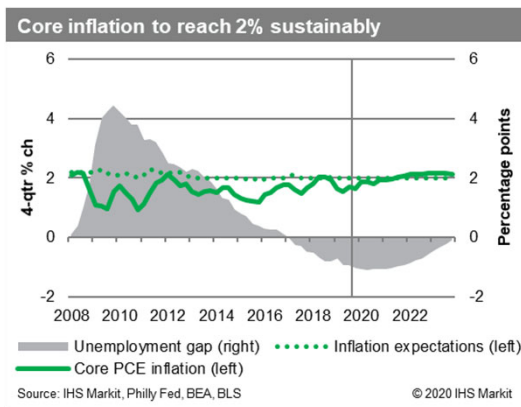
Trend-ish 2.1% growth through 2021; unemployment troughs at 3.5%; consumers, cap-ex, govt lend support; trade a drag



Confidential. © 2018 IHS Markit™. All Rights Reserved.

In tight labor market, inflation edges up; Fed cancels "insurance policy"

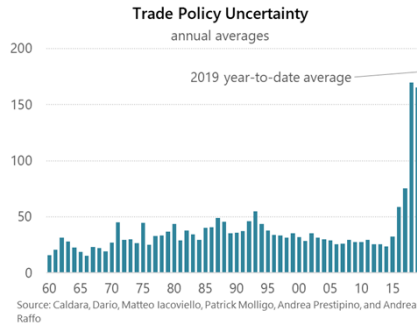
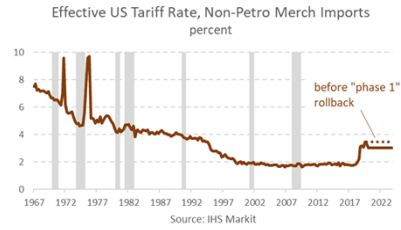
Inflation firms above Fed's 2% objective; unneeded monetary accommodation reversed; "term premium" widens



Confidential. © 2018 IHS Markit™. All Rights Reserved.

Tariffs: headwind, not a brick wall

- Tariffs as a tax
 - > \$70 bil (~ 0.3% of GDP) over several years
 - > Compare that to recent tax & spending stimulus; and, there are offsets
 - > So far, more trade *diversion* than *destruction*
 - > ~ 10% depreciation of the yuan
 - > Some substitution towards US production
 - > Margin compression protects consumers
- Tariff policy as a source of uncertainty
 - > Financial conditions: higher risk spreads, but (mostly) offset by lower risk-free rates
 - > Cap-ex on hold? yes, esp in mfg (more below)
 - > Macro vs micro

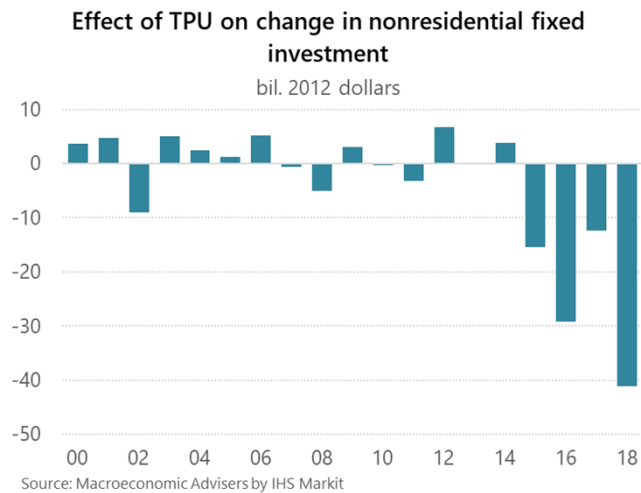


TPU, through manufacturing sector, has restrained aggregate capital expenditures

Table 3: Effects of TPU in Manufacturing

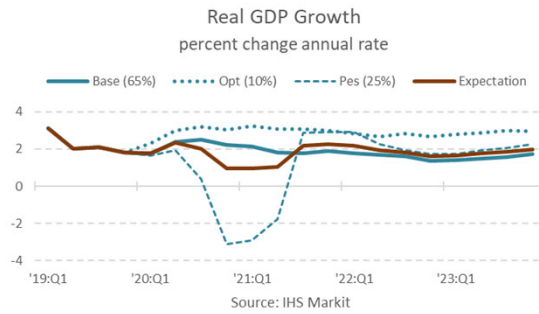
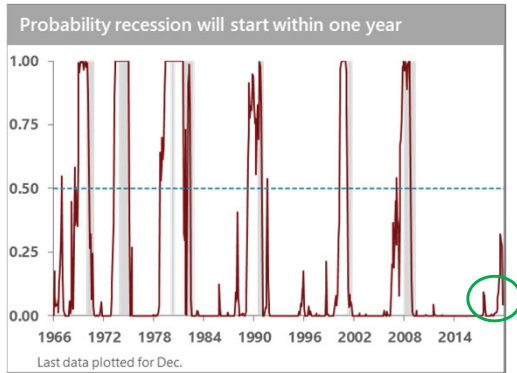
	coefficient on TPU
Wood Products	-1.0
Nonmetallic Mineral Products	-1.1
Primary Metals	-1.2 **
Fabricated Metal Products	-0.8
Machinery	-1.2
Computer and Electronic Products	-2.0 *
Electrical Equipment, Appliances, and Components	-2.1 **
Motor Vehicles, Bodies and Trailers, and Parts	-2.4 **
Other Transportation Equipment	-1.3
Furniture and Related Products	-1.0
Miscellaneous Manufacturing	-1.6 **
Food and Beverage and Tobacco Products	-0.4
Textile Mills and Textile Product Mills	-1.3 **
Apparel and Leather and Allied Products	-0.8
Paper Products	-1.7 **
Printing and Related Support Activities	-0.1
Petroleum and Coal Products	-0.9
Chemical Products	-1.1 *
Plastics and Rubber Products	-1.7 **

Notes: Sample is annual; 1965-2018. The dependent variable is the first difference of the percent change of the end-of-year real net stock (quantity index). Trade policy uncertainty is entered as the first difference of the log of a 12-month average for each year. Included as independent variables in all regressions, but not shown, are the first differences of the 4-quarter percent changes of real nonfarm business sector output lagged 4 quarters, 8 quarters, and 12 quarters. *** indicates 1% significance, ** indicates 5% significance, * indicates 10% significance.



Odds of recession have slipped; weight on “pessim” dropped from 35% to 25%

But if recession odds are 1 in 4, what “expected” economic environment should be planned for?



Time for...the lightning round!

Abbreviated answers to frequently, recently asked questions

- Inverted yield curve: believe it...or not?
- Manufacturing “recession”? Vehicle sales?
- (Settled) GM strike, Boeing 737 MAX problems?
- Recent liquidity squeeze: signs of trouble ahead?
- Stocks: repeat or consolidate 2019 gains?
- Enough policy “space” in next recovery?
- Impact of 2020 Presidential election?
- Impact of USMCA (or NAFTA withdrawal)?
- Updated odds on Brexit, no-deal Brexit? Impact on UK, global economy?
- Impact / fallout of Soleimani assassination?

