Can Fed Inoculate U.S. and Global Economy?

26th Annual Arkansas Business Forecast Luncheon
January 30, 2020
KPMG Economics
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Potential GDP is on the decline in the developed world

OECD potential GDP growth
OECD economies, average annual % change

Demographics is also a key factor for U.S. growth

U.S. real and potential GDP growth
Annual - % change, decade averages

Source: KPMG Economics, Bureau of Economic Analysis, Congressional Budget Office, Haver Analytics
U.S. population growth 36% below previous expectations

U.S. annual population growth
July 1 to July 1

Actual U.S. population growth
Projected

825,000 shortfall

Source: KPMG Economics, Census Bureau (2019), Haver Analytics

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Inflation is slowing in conjunction with lower GDP.

Percentage of time inflation below the central bank’s target since 2008

% of time Core CPI below 2.0% since 2008

- Australia: 38%
- U.K.: 46%
- U.S.: 60%
- New Zealand: 81%
- Denmark: 87%
- Canada: 88%
- Japan: 91%
- Sweden: 93%
- Euro Area: 99%
- Switzerland: 100%

Source: KPMG Economics, National Sources, Haver Analytics

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Central banks are keeping it loose….

Policy rate targets for select global central banks

- Federal Reserve
- Bank of England
- European Central Bank
- Bank of Japan

Source: KPMG Economics, BoJ, ECB, BoE, Federal Reserve, Haver Analytics (Jan 24, 2020)
Manufacturing was the main source of recent weakness.
Chinese liquidity drives the global manufacturing cycle

Global Manufacturing PMI (SA, 50+ = Expansions, LHS)
China: Total Credit Creation (Y/Y%, 18-Mo Lead, RHS)

Index


Source: KPMG Economics, JP Morgan-IHS Markit (Dec 2019), People’s Bank of China (Nov 2019), MacroPolicy Perspectives, Haver Analytics
Slowing Chinese growth is impacting global economy

Source: KPMG Economics, China Customs (September 2019), Haver Analytics
The outbreak of 2019-nCoV to lower Chinese GDP

China: Response to GDP and retail sales of SARS

Source: KPMG Economics, CNBS, Haver Economics
“Phase One” deal estimated to lower tariffs for 2020

Average effective U.S. tariff rate on imports from China

Source: KPMG Economics, Peterson Institute for International Economics
China promises to more than double imports of select goods

U.S. exports to China
“Phase One” agreement list

- Services
- Energy
- Agricultural products
- Manufactured goods
- Other (not in trade agreement)

Source: KPMG Economics, U.S. Census Bureau, Economic and Trade Agreement Between the U.S. and China (Annex 6.1, Jan 2020), Haver Analytics

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Significant increase from the 2017 baseline...

<table>
<thead>
<tr>
<th>Year</th>
<th>Services</th>
<th>Energy</th>
<th>Agricultural products</th>
<th>Manufactured goods</th>
<th>Other (not in trade agreement)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2015</td>
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<td>2016</td>
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<tr>
<td>2019</td>
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</tr>
<tr>
<td>2020</td>
<td>+39%</td>
<td>+64%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2021</td>
<td>+39%</td>
<td>+64%</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

Source: KPMG Economics, U.S. Census Bureau, Economic and Trade Agreement Between the U.S. and China (Annex 6.1, Jan 2020), Haver Analytics
…but an even larger increase from 2019 levels

U.S. exports to China
“Phase One” agreement list

Source: KPMG Economics, U.S. Census Bureau, Economic and Trade Agreement Between the U.S. and China (Annex 6.1, Jan 2020), Haver Analytics

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U.S. Outlook
The consumer has been the backbone of the expansion

Source: KPMG Economics, BEA (Q3 2019), BLS (December 2019), Haver Analytics
Today’s full employment looks different than the past

Share of U.S. nonfarm employment by job type

- **Routine manual**
- **Routine Cognitive**
- **Nonroutine Manual**
- **Nonroutine cognitive**

<table>
<thead>
<tr>
<th>Year</th>
<th>Routine manual</th>
<th>Routine Cognitive</th>
<th>Nonroutine Manual</th>
<th>Nonroutine cognitive</th>
</tr>
</thead>
<tbody>
<tr>
<td>1985</td>
<td>27%</td>
<td>28%</td>
<td>16%</td>
<td>30%</td>
</tr>
<tr>
<td>2005</td>
<td>23%</td>
<td>26%</td>
<td>16%</td>
<td>35%</td>
</tr>
<tr>
<td>2019</td>
<td>20%</td>
<td>21%</td>
<td>17%</td>
<td>41%</td>
</tr>
</tbody>
</table>

KPMG Economics, Bureau of Labor Statistics (2019), Haver Analytics
Tightening access to consumer credit impacts consumption

Fed Senior Loan Officers Survey

Willingness to Lend to Consumers

Source: KPMG Economics, Federal Reserve Board (Q3 2019), Haver Analytics
Auto and credit card loan delinquencies rising

% of loans 90+ days delinquent by loan type

Source: KPMG Economics, Federal Reserve Bank of New York (Q3 2019), Haver Analytics
Housing and autos have divergent response to rate cuts

Source: KPMG Economics, Census Bureau (Dec 2019), Autodata (Dec 2019), Haver Analytics
Housing investment should continue responding to low rates

Source: KPMG Economics, Bureau of Economic Analysis (Q3 2019), Census Bureau (Dec 2019), Haver Analytics
Workers respond to longevity and low rates

Source: KPMG Economics, Bureau of Labor Statistics (Dec 2019), Haver Analytics
Older workers largest share of the labor force

Labor force share by age group

<table>
<thead>
<tr>
<th>Year</th>
<th>16 to 24</th>
<th>25 to 34</th>
<th>35 to 44</th>
<th>45 to 54</th>
<th>55 and older</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998</td>
<td>15.9%</td>
<td>23.8%</td>
<td>27.3%</td>
<td>20.6%</td>
<td>12.4%</td>
</tr>
<tr>
<td>2008</td>
<td>14.3%</td>
<td>21.6%</td>
<td>22.7%</td>
<td>23.3%</td>
<td>18.1%</td>
</tr>
<tr>
<td>2018</td>
<td>12.9%</td>
<td>22.7%</td>
<td>20.7%</td>
<td>20.6%</td>
<td>23.1%</td>
</tr>
<tr>
<td>Projected 2028</td>
<td>11.5%</td>
<td>21.6%</td>
<td>22.4%</td>
<td>19.3%</td>
<td>25.2%</td>
</tr>
</tbody>
</table>

Millennials and Gen Z most diverse populations in history

Racial composition of U.S. generations
Share of generation by race, 2018

Source: KPMG Economics, Census Bureau (2018), Haver Analytics
Millennials are better educated than previous generations

Educational attainment distribution of 25 to 37 year olds (%)

- Bachelor's degree or higher
- Some college
- High school graduate
- Less than high school grad

Source: KPMG Economics, Pew Research, Census Bureau
Productivity growth is lagging previous expansions

Source: KPMG Economics, BEA (Q3 2019), NFIB (Q4 2019), Haver Analytics
Lack of capital investment a puzzle for economists

U.S. capital stock age

Source: KPMG Economics, Bureau of Economic Analysis (2018), Haver Analytics
CapEx growth has been slow during this expansion

Nonresidential fixed investment
Indexed to end of previous recession

Source: KPMG Economics, Bureau of Economic Analysis (Q3 2019), Haver Analytics
Greater productivity is needed to boost growth outlook

Real GDP
% change, annual rate

Historical Data

Forecast

Note: Real GDP is GDP adjusted for inflation; Real GDP is reported at a seasonally adjusted annual rate
Source: KPMG Economics, Macroeconomic Advisors by IHS (December 2019)
Economic risks are like a jenga tower
737 MAX
Cyber Attack
EU Breakup / Brexit
Climate Volatility
Coronavirus
Middle-East Instability
Government Debt
China growth Challenges
Trade Wars
Corporate Debt Levels
Why is world trade per unit of GDP falling?

Source: KPMG Economics, Shin (2020), BIS (Q3 2019), Haver Analytics, Q1 2000=100
Is world trade volume tied to the value of the dollar?

Source: KPMG Economics, Shin (2020), BIS (Q3 2019), FRB Broad Trade-Weighted Dollar (Q4 2019), Haver Analytics, Q1 2000 = 100
Global policy rates decline after Fed eases
Rate increases/rate declines

Diffusion Index: % CB reporting increases less % CB reporting decreases, 3mma.
Source: KPMG Economics, Haver Analytics (Dec 2019).
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