



# Global Economy Report

January-February 2016



# Global Economy Report

The Global Economy Report is prepared in cooperation by the Macroeconomic Research Division of Banca Aletti and the Global Governance Programme of the Robert Schuman Centre for Advanced Studies of the European University Institute.

The objective of the Report is to provide an analysis of the current and expected macroeconomic and financial conditions at the global level, with also a focus on key economic areas such as Europe, the USA and ASIA.

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**Report closed on January 14, 2016**

- ❖ The global cycle remains in expansion, but growth intensity is declining. The services' compartment is the main growth factor, as manufacturing is far weaker.
- ❖ There's still a double-track between major and emerging economies, with the global PMI for emerging economies still decreasing and under 50 (typically considered as the expansion/recession border), while the formers' is stable and above 50.
- ❖ Growth is limited by a series of correlated factors, among which there are China's slowdown and the renminbi devaluation, the drop in raw materials' and oil's prices, volatility in financial markets and increased geo-political risks.

# EXECUTIVE SUMMARY

- ❖ In the USA growth is robust but twofold, with some signs of recession in the industrial sector more than compensated by stable services and internal demand. Latest data are lower than expected in practically all major compartments of the economy, except the labour market where employment is growing but wages' growth is still modest.
- ❖ General inflation grew in December by 0.5%, reaching almost the highest point of the year, but downward pressures on energy prices continue. The core index registered an increase by 0.2%, with trend rate at 2.0%, highest since February 2013.
- ❖ In this context, the FED began the normalisation of its monetary policy in December, although there still is the trade off between its robust domestic economy, with the exception of issues in the manufacturing sector, and the uncertain global scenario. Forecasts are for a very slow and gradual increase on rates in 2016, in line with macro data evolution.

- ❖ In the euro area, the economy continues to expand at a moderate but steady pace. At an annualised quarterly basis, the growth rate is at its highest since 2011. A disaggregated analysis highlights private consumption's persistent contribution, while foreign trade is slowing growth and investment's contribution is still missing.
- ❖ At the moment, macroeconomic data indicate an absence of contagion from emerging economies' slowdown. Confidence is high, PMI surveys point to a solid expansion rhythm in 2016.
- ❖ Recovery continues to be supported by domestic demand thanks to lower oil prices, interest rates and improving labour market. The euro devaluation's delayed effects must furthermore still completely manifest themselves.
- ❖ The December inflation flash estimate sees the headline rate at +0.2% (same as November and well below ECB's target) and core at +0.9%. Monetary policy will thus remain very expansive, though not as much as financial markets would like.

- ❖ Japan's GDP grew by 1% in annualised terms in the third quarter of the year, boosted by private consumption and exports, with a modest contribution from investment and a negative contribution from inventories. Leading indicators for the manufacturing sector remain positive, pointing to an expansion for the beginning of the year.
- ❖ The labour market remains robust with unemployment rate close to absolute lows. Inflation remains still far from BoJ's targets, although in slight recovery net of volatile components.
- ❖ According to official data, in 2015 the Chinese economy grew by 7.0% in the first two quarters and by 6.9% in the third in annual terms. Real values are probably lower and leading indicators confirm that the slowdown scenario is still the dominating one for the close future.

# EXECUTIVE SUMMARY

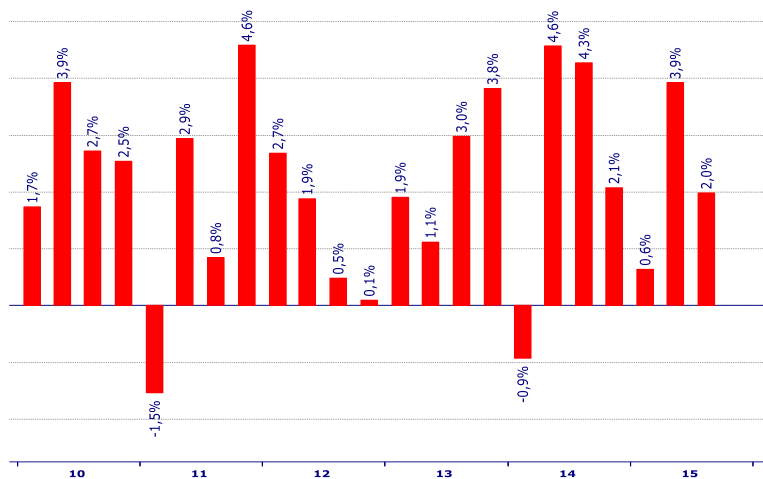
|                         | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015E | 2016E |
|-------------------------|------|------|------|------|------|------|-------|-------|
| GDP (%YOY)              |      |      |      |      |      |      |       |       |
| US                      | -2.8 | 2.5  | 1.6  | 2.3  | 2.2  | 2.4  | 2.4   | 2.2   |
| EUROZONE                | -4.5 | 2.0  | 1.6  | -0.9 | -0.4 | 0.9  | 1.5   | 1.6   |
| GERMANY                 | -5.6 | 4.2  | 3.6  | 0.4  | 0.1  | 1.6  | 1.5   | 1.7   |
| FRANCE                  | -2.9 | 2.0  | 2.1  | 0.2  | 0.7  | 0.2  | 1.1   | 1.3   |
| ITALY                   | -5.5 | 1.7  | 0.6  | -2.8 | -1.7 | -0.4 | 0.7   | 1.3   |
| UK                      | -4.3 | 1.9  | 1.6  | 0.7  | 1.7  | 2.9  | 2.4   | 2.0   |
| JAPAN                   | -5.5 | 4.7  | -0.4 | 1.7  | 1.6  | -0.1 | 0.6   | 1.0   |
| BRAZIL                  | -0.2 | 7.6  | 4.0  | 1.8  | 2.8  | 0.2  | -3.0  | -1.2  |
| RUSSIA                  | -7.8 | 4.5  | 4.3  | 3.4  | 1.3  | 0.6  | -3.8  | 0.0   |
| INDIA                   | 6.4  | 8.9  | 7.5  | 5.1  | 4.6  | 7.2  | 7.3   | 7.5   |
| CHINA                   | 9.2  | 10.4 | 9.3  | 7.7  | 7.7  | 7.3  | 6.9   | 6.5   |
| AUSTRALIA               | 1.5  | 2.3  | 2.7  | 3.6  | 2.0  | 2.8  | 2.3   | 2.6   |
| KOREA                   | 0.7  | 6.5  | 3.7  | 2.3  | 2.9  | 3.3  | 2.5   | 2.9   |
| INFLATION (%YOY)        |      |      |      |      |      |      |       |       |
| US                      | -0.3 | 1.6  | 3.2  | 2.1  | 1.5  | 1.6  | 0.2   | 1.4   |
| EUROZONE                | 0.3  | 1.6  | 2.7  | 2.5  | 1.4  | 0.4  | 0.1   | 1.0   |
| GERMANY                 | 0.2  | 1.1  | 2.5  | 2.1  | 1.6  | 0.8  | 0.2   | 1.4   |
| FRANCE                  | 0.1  | 1.7  | 2.3  | 2.2  | 1.0  | 0.6  | 0.1   | 1.0   |
| ITALY                   | 0.8  | 1.6  | 2.9  | 3.3  | 1.3  | 0.2  | 0.2   | 1.0   |
| UK                      | 2.2  | 3.3  | 4.5  | 2.8  | 2.6  | 1.5  | 0.1   | 1.3   |
| JAPAN                   | -1.3 | -0.7 | -0.3 | 0.0  | 0.4  | 2.7  | 0.7   | 0.8   |
| BRAZIL                  | 4.9  | 5.0  | 6.6  | 5.4  | 6.2  | 6.3  | 8.9   | 6.8   |
| RUSSIA                  | 11.7 | 6.9  | 8.5  | 5.1  | 6.8  | 7.8  | 15.5  | 7.9   |
| INDIA                   | 10.8 | 12.1 | 8.9  | 10.4 | 10.9 | 7.8  | 6.1   | 5.5   |
| CHINA                   | -0.7 | 3.3  | 5.4  | 2.7  | 2.6  | 2.0  | 1.5   | 1.9   |
| AUSTRALIA               | 1.8  | 2.9  | 3.3  | 1.8  | 2.5  | 2.5  | 1.6   | 2.4   |
| KOREA                   | 2.8  | 3.0  | 4.0  | 2.2  | 1.3  | 1.3  | 0.7   | 1.6   |
| Banca Aletti Forecast   |      |      |      |      |      |      |       |       |
| Cons. Bloomberg (Dic15) |      |      |      |      |      |      |       |       |
| Historical Data         |      |      |      |      |      |      |       |       |

# The US Outlook

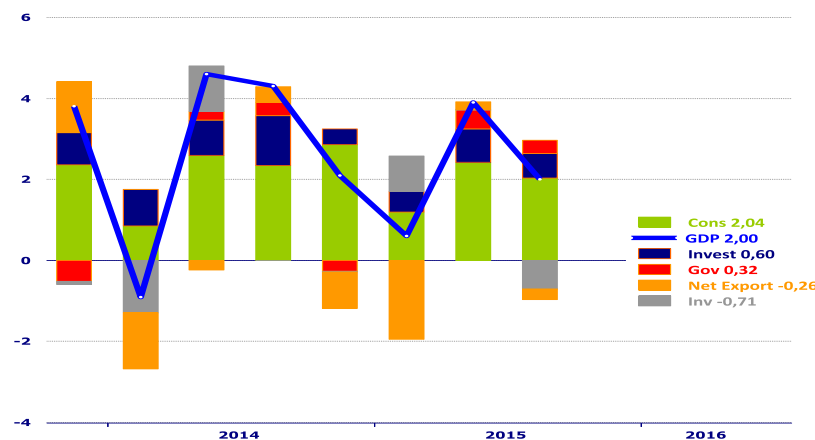


The third estimate of US GDP for the third quarter of the year has been trimmed by one tenth at 2.0%. Annualised quarterly growth rate has also been trimmed by one tenth at 2.1%, the lowest value since the beginning of 2014. A breakdown of GDP highlights the dominating contribution of private consumption, that confirms the solidity of domestic demand.

**GDP (second estimate)**  
ANNUALISED QUARTERLY RATES

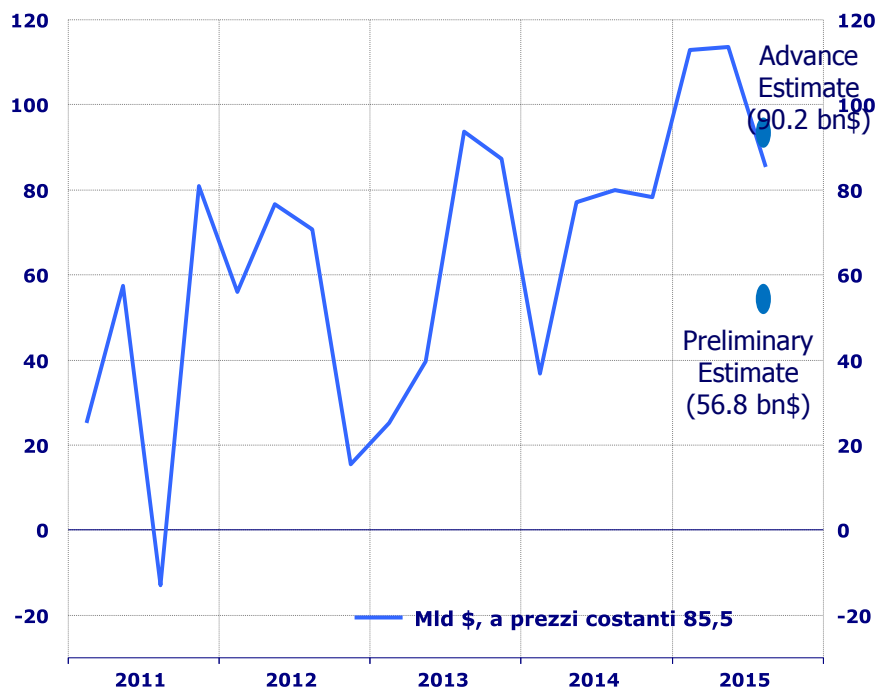


**GDP (third estimate)**  
GROWTH CONTRIBUTIONS- GDP%



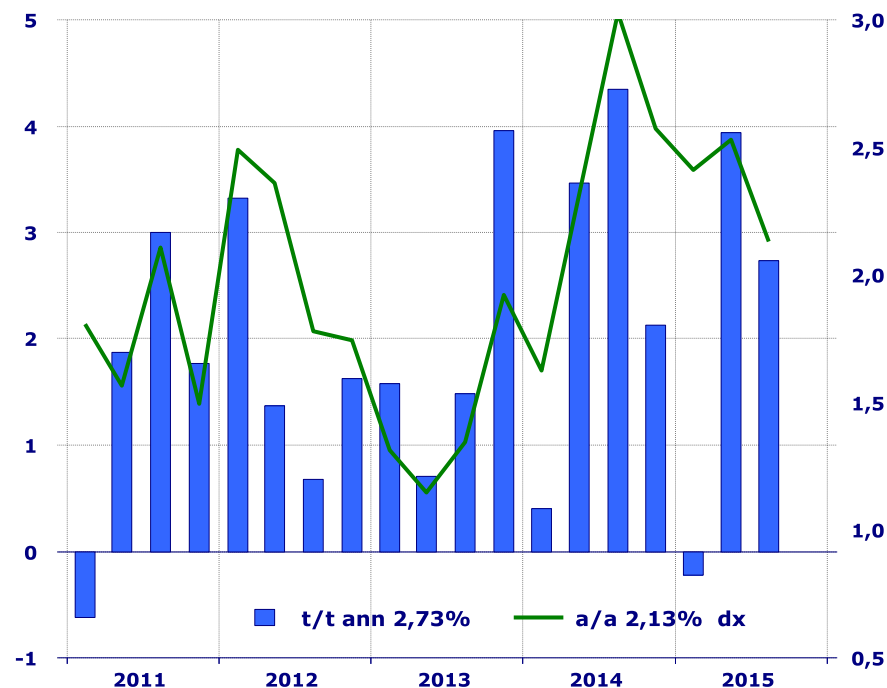
Inventories have taken seven tenths percentage point from growth and remain high, despite industry's production levels' cut. The inventory adjustment process is, unfortunately, still far from over, thus representing a risk for the fourth quarter's growth.

## INVENTORIES



## ECONOMIC GROWTH NET OF INVENTORIES

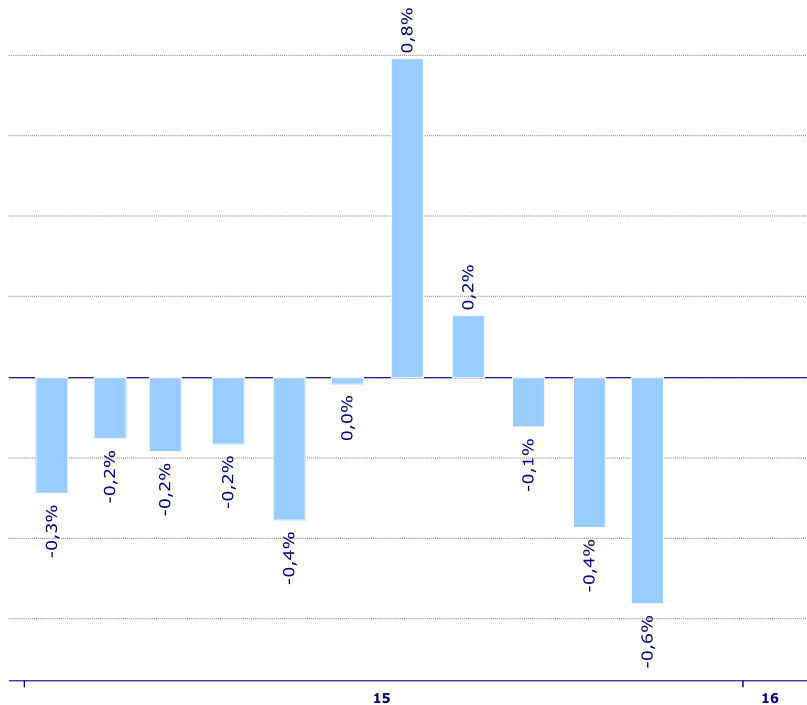
FINAL SALES. quarterly changes, annual and annualised quarterly rates



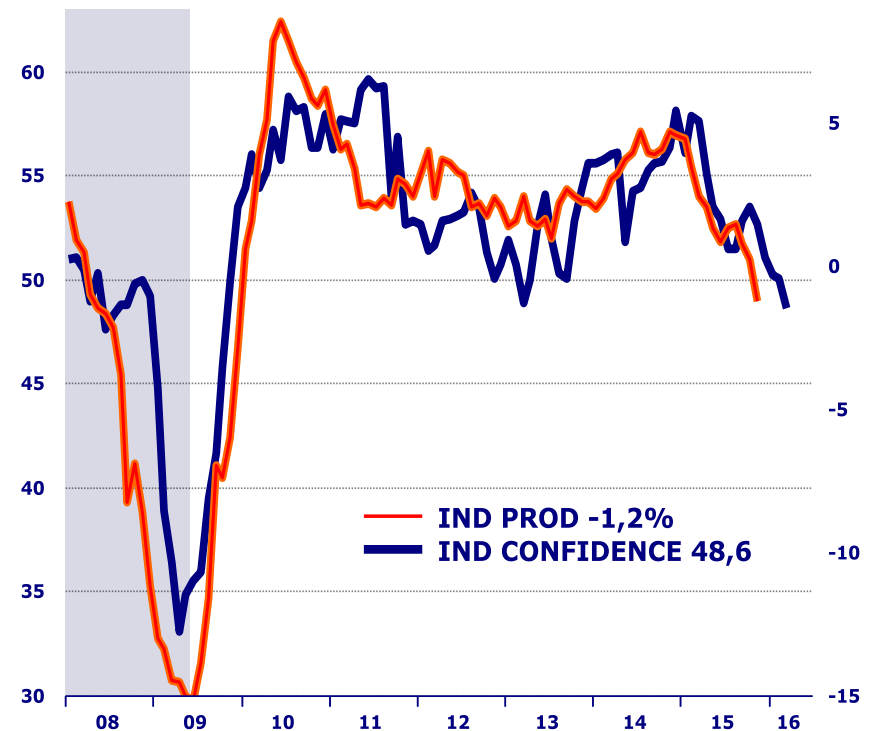
# INDUSTRIAL PRODUCTION

Industrial production decreased by -0.6% in November, down for the third month in a row, highlighting a pattern of clear weakness persistent since the beginning of 2015. The trend rate is in negative territory for the first time since December 2009, registering a decrease by -1.2% versus the previous year, lowest since six years. The leading indicator accelerated its decline, at its lowest since 2009.

INDUSTRIAL PRODUCTION  
Changes

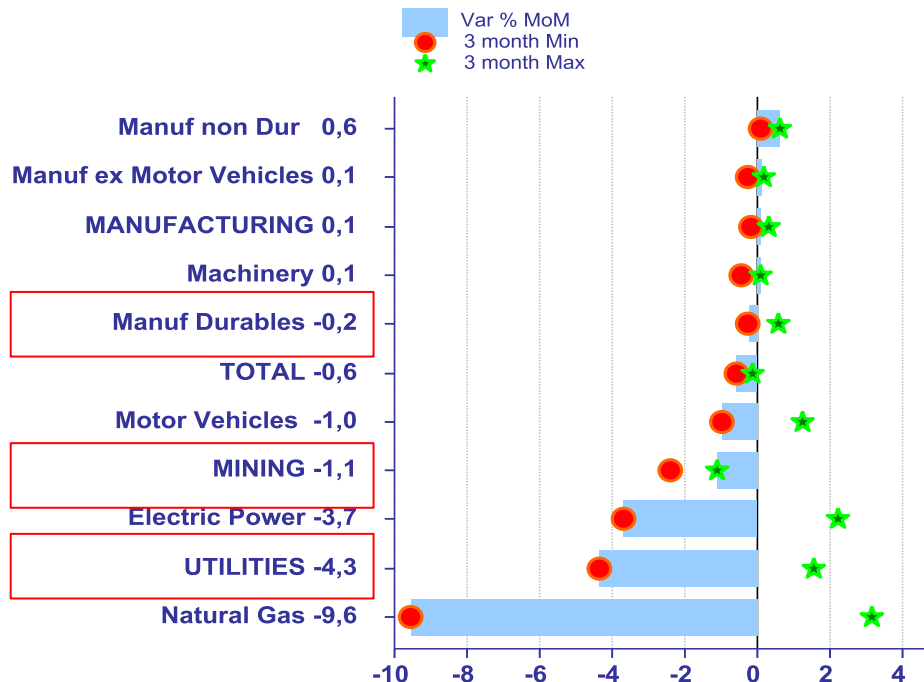


PRODUCTION AND CONFIDENCE

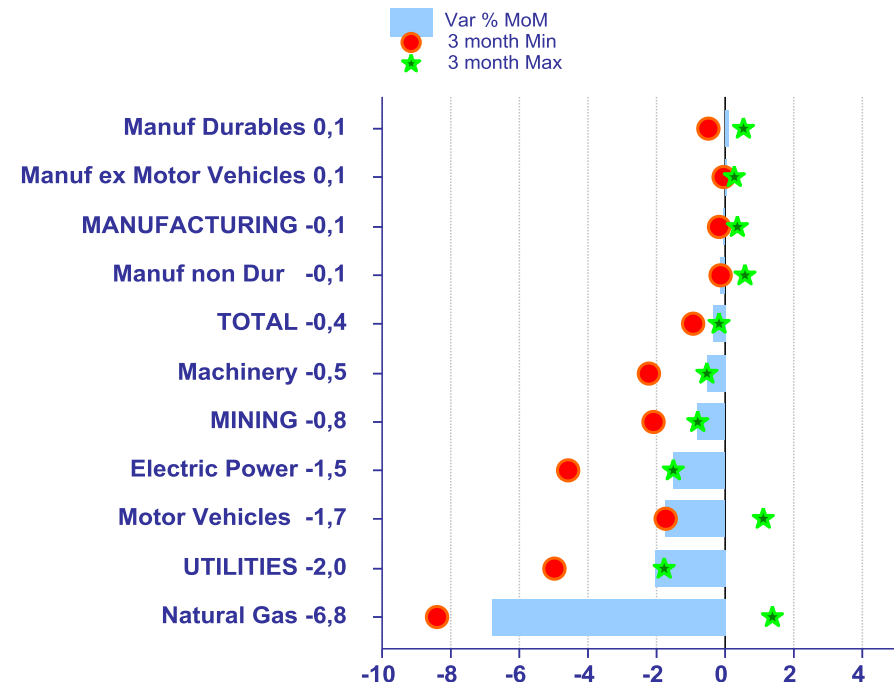


Production's negative evolution was influenced by the big drop in utilities' output (due to mild weather in November) and in mining (penalised by low oil price), but manufacturing's stagnation highlights the sector's widespread weaknesses. Machinery production, which is strongly cyclical, registers a negative balance on an annual base by almost three percentage points.

PRODUCTION: breakdown by industrial sector



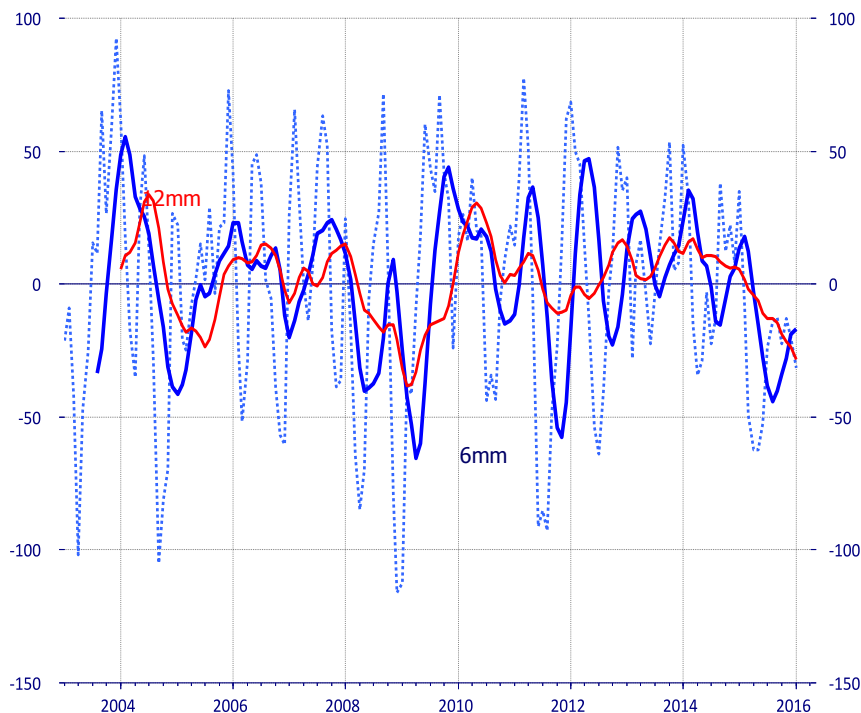
PRODUCTION: breakdown by industrial sector



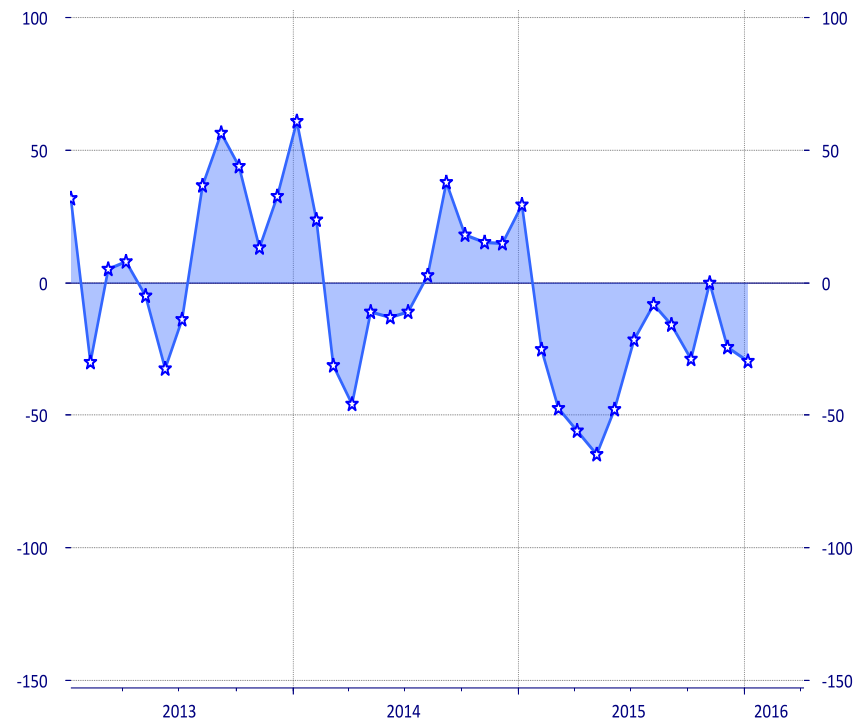
# SURPRISE INDEX

Apart from IP's negative trend, the general level in macroeconomic data has been disappointing. The surprise index entered negative territory, reaching mid 2015 lows; the twelve month average reached 2009 lows...

**SURPRISE – LONG TERM**

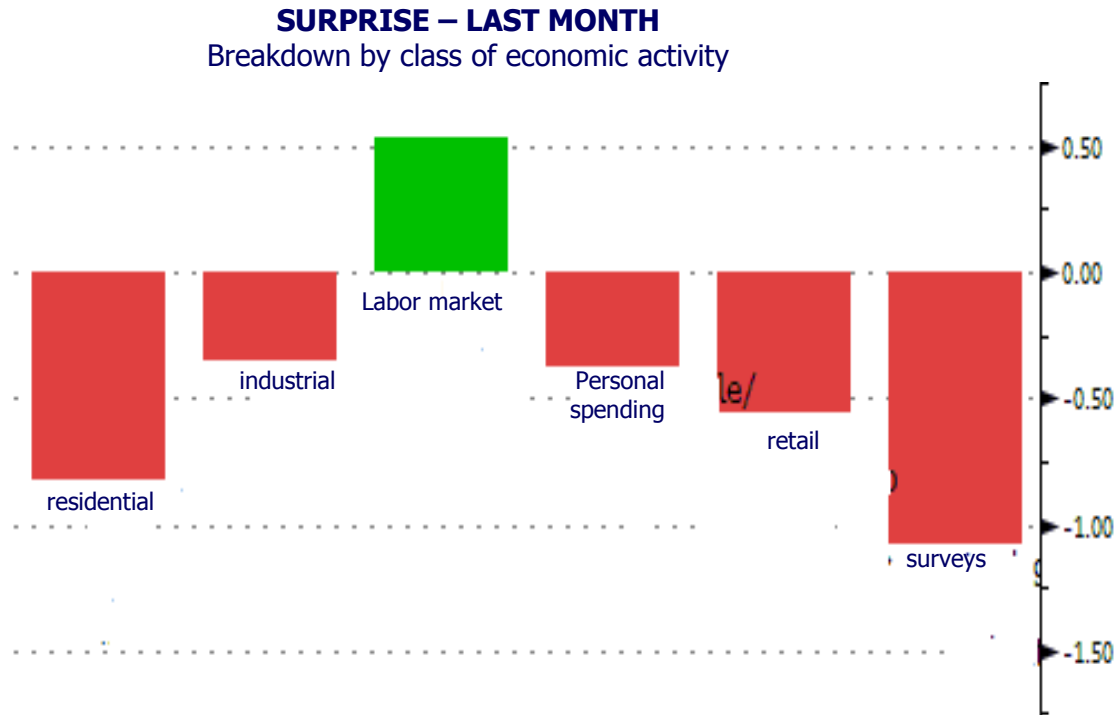


**SURPRISE – SHORT TERM**



# SURPRISE INDEX

...the analysis of last month's data flux confirms that statistics have been lower than expected in all major compartments of economic activity, excluding the labour market.



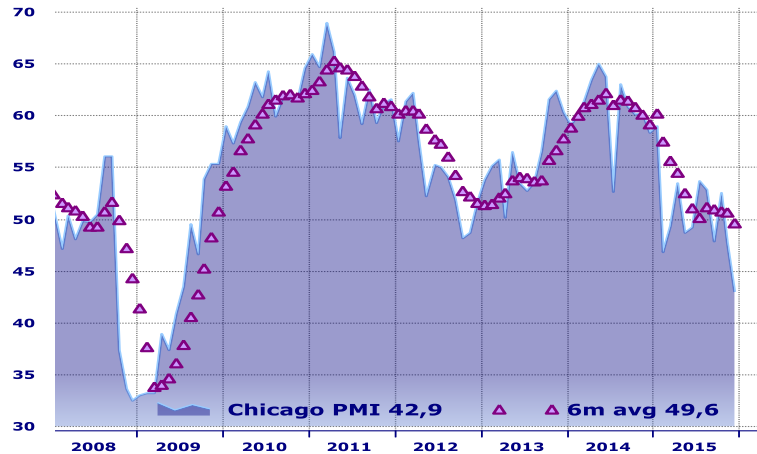
Surprise = (real data – survey median)/survey stdev  
*Height degli istogrammi is proportional to surprise intensity*

Source : Bloomberg

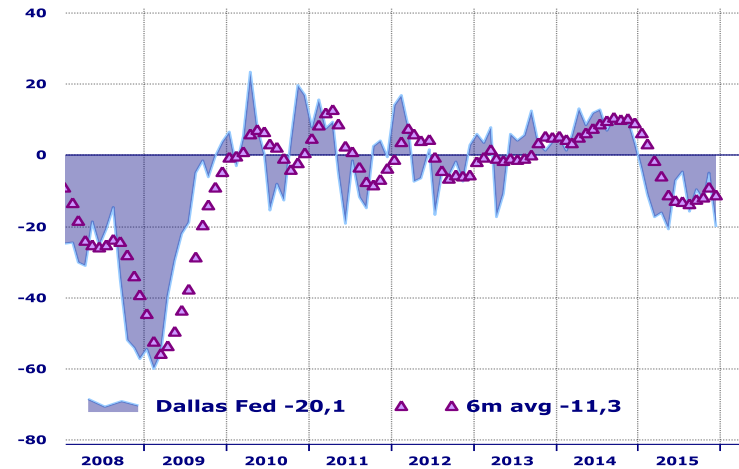
# FIRMS' CONFIDENCE

Regional surveys carried out by the Fed's local departments confirm worsened conditions in the industrial compartment, with a sensible decline in the latest major surveys of 2015.

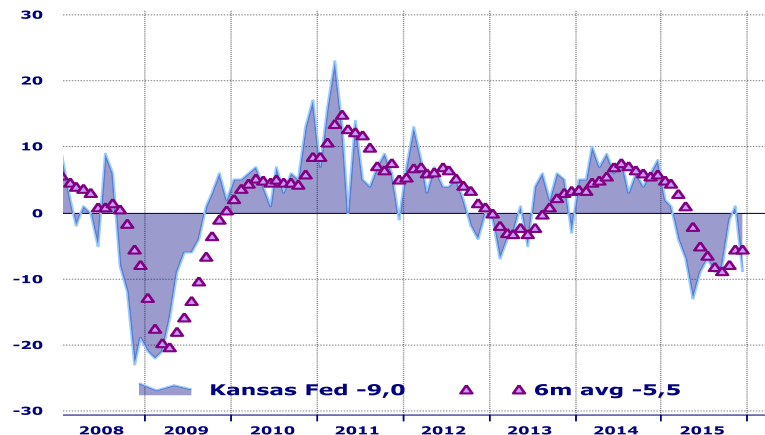
CHICAGO PMI



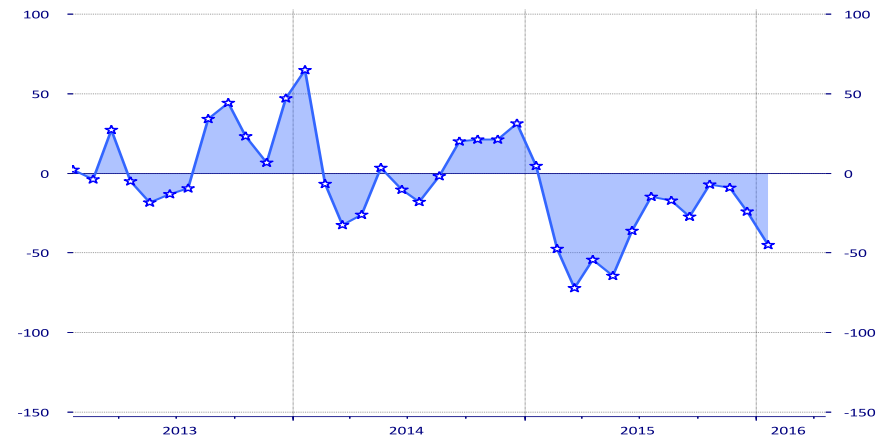
DALLAS FED



KANSAS FED



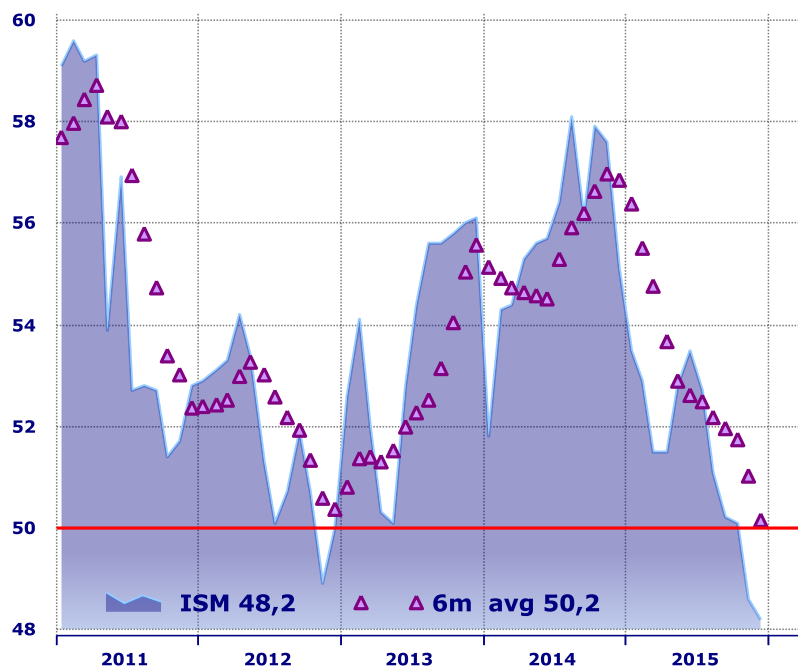
RICHMOND FED



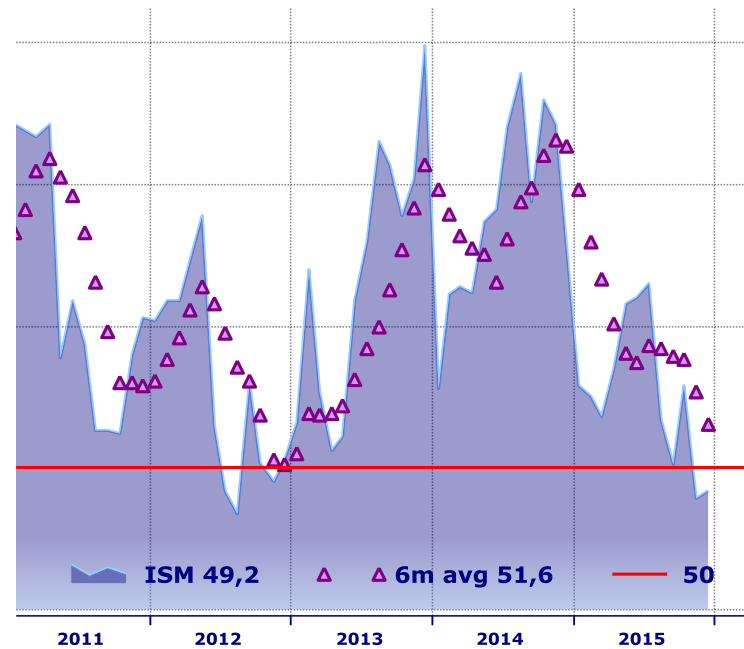
# FIRMS' CONFIDENCE

The most important signal of manufacturing businesses' confidence is at its lowest since the end of the 2009 recession. The ISM index in December was at 48.2, further down from prior month's 48.6, lowest value in six and a half years. The statistic is well under the 50 point limit, that separates economic activity's expansion from contraction and is below consensus estimates (49).

ISM MANUFACTURING



ISM NEW ORDERS

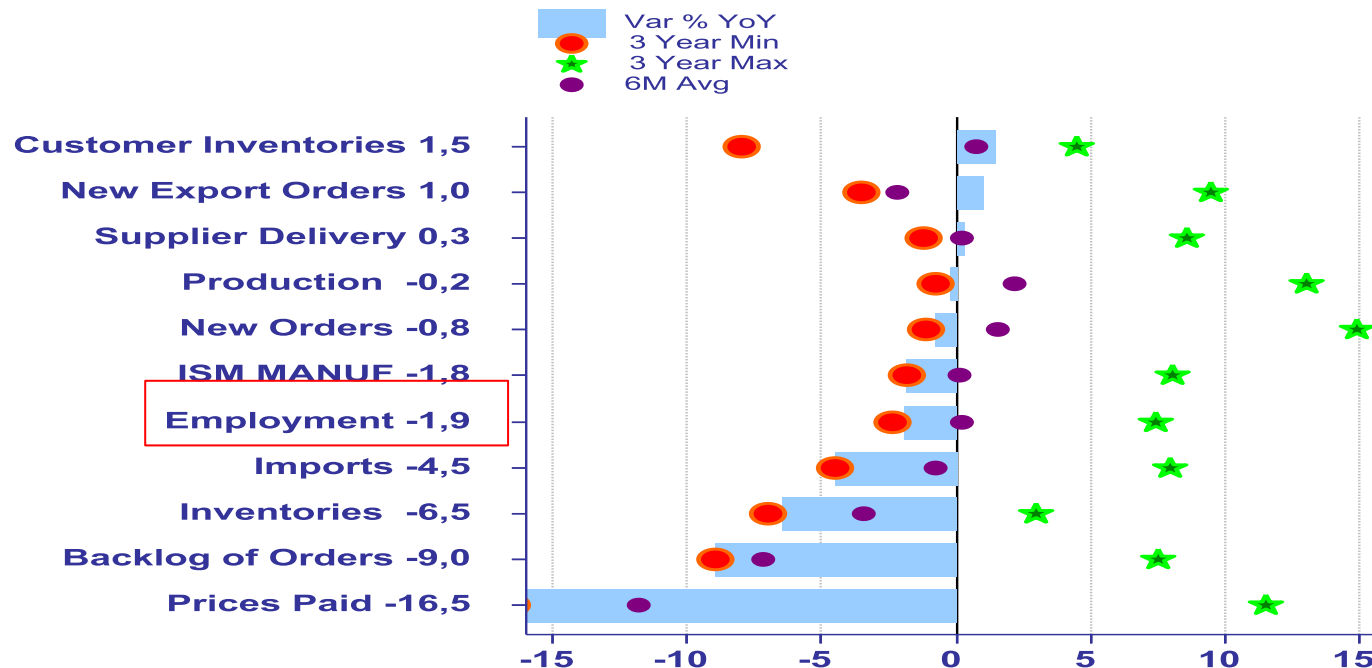




# FIRMS' CONFIDENCE

The figure is consistent with industrial production's extremely weak trajectory we've witnessed in the past year, penalised by a slowdown in global demand, by the dollar's strength and the negative turn in oil price. A partial improvement in sub-indexes relating to production (49.8 from 48.2) and new orders (49.2 from 48.9) is coupled with a marked decrease in the index on employment.

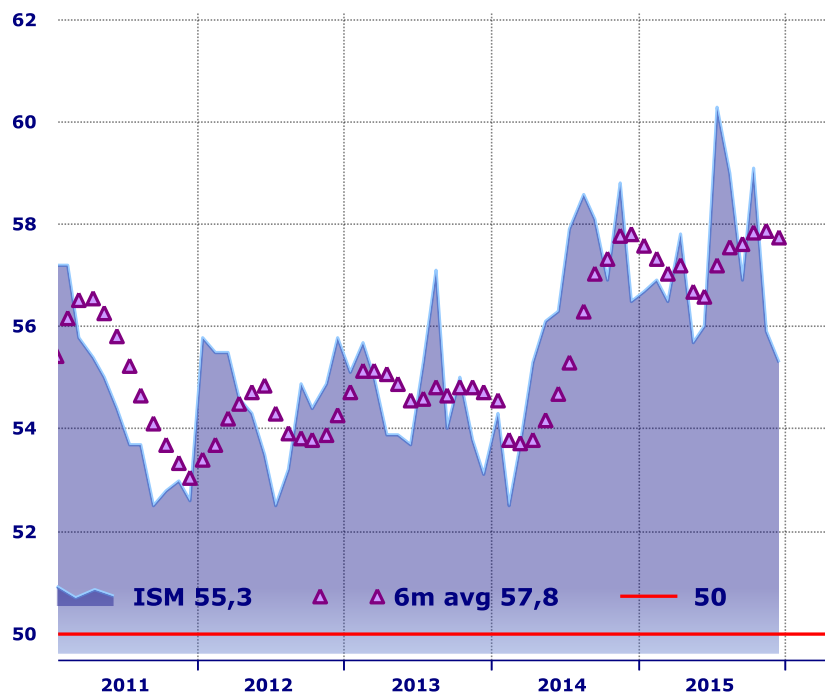
ISM MANUFACTURING – DETAILS



# FIRMS' CONFIDENCE

In December the ISM services index slid to 55.2, well under consensus (56), the worst survey in the last 20 months. While the index absolute level still points to a solid rhythm of expansion in services, the growth trend is evidently slowing down in the past months, indicating weakness in economic growth in general.

ISM NON MANUFACTURING

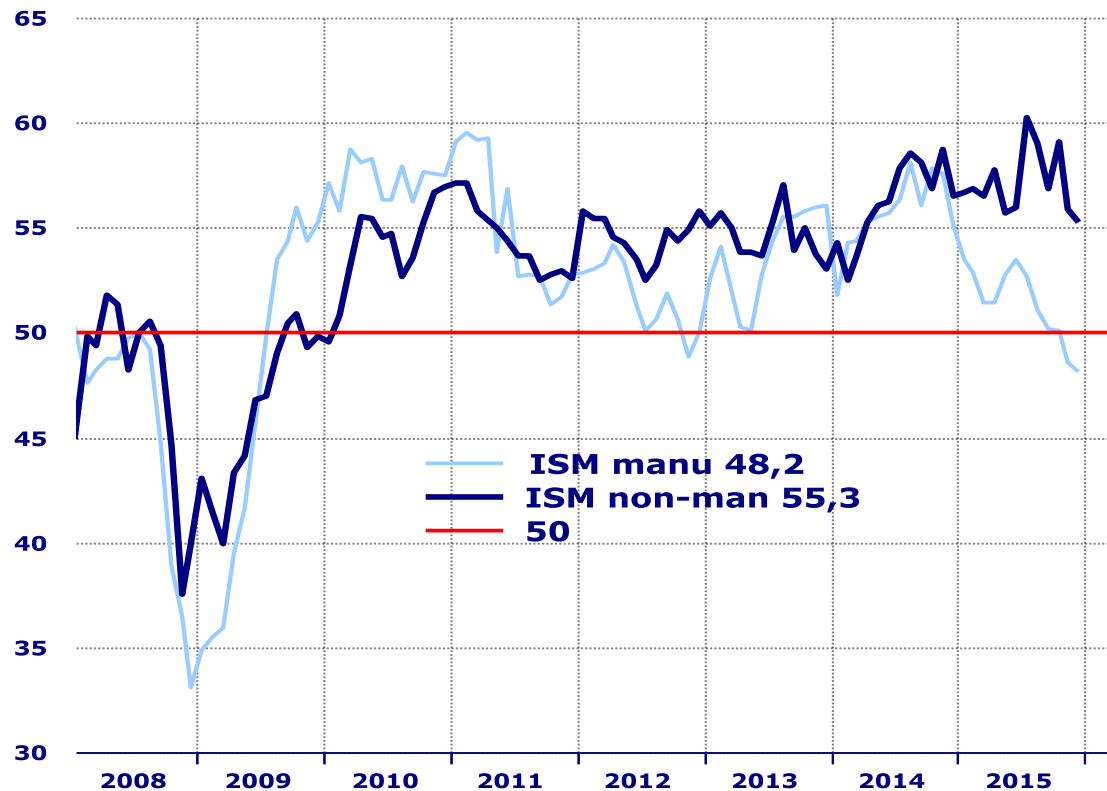


ISM NON MANUFACTURING: DETAIL



# FIRMS' CONFIDENCE

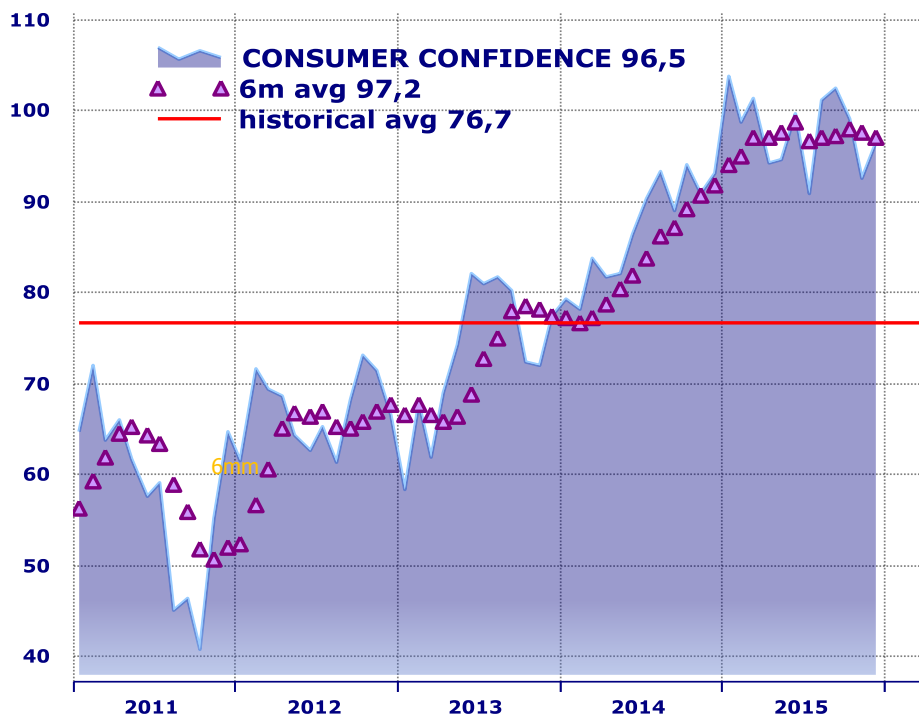
The obvious correlations between services and general manufacturing compartments are a source of concern for the intensity of US growth in the medium term.



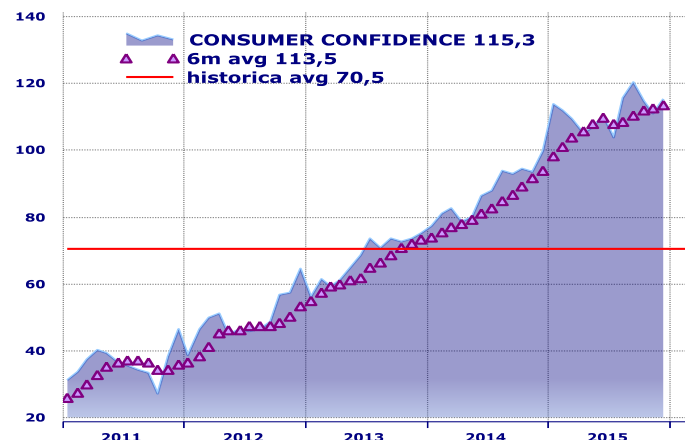
# HOUSEHOLDS' CONFIDENCE

Consumer confidence grew in December, by three points at 96.5, beating forecasts and confirming historically high levels, close to 2007 peaks. Expectations have weakly improved, as have current conditions. Furthermore, November data has been raised by over two points.

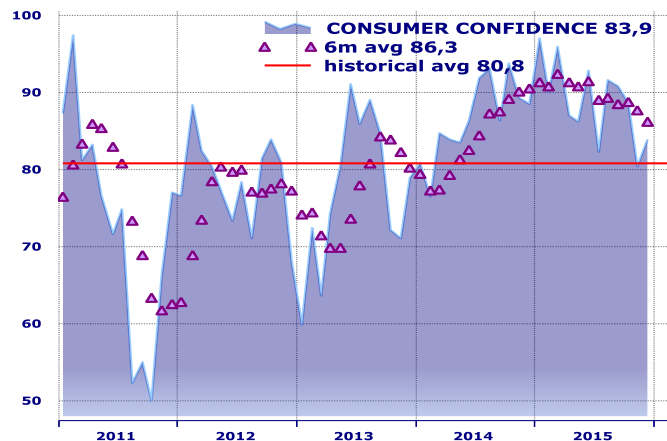
CONFERENCE BOARD



CONFERENCE BOARD: CURRENT CONDITIONS



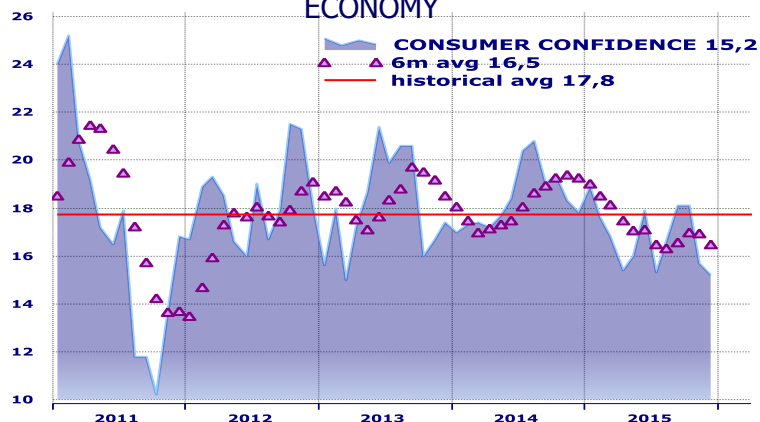
CONFERENCE BOARD : EXPECTATIONS



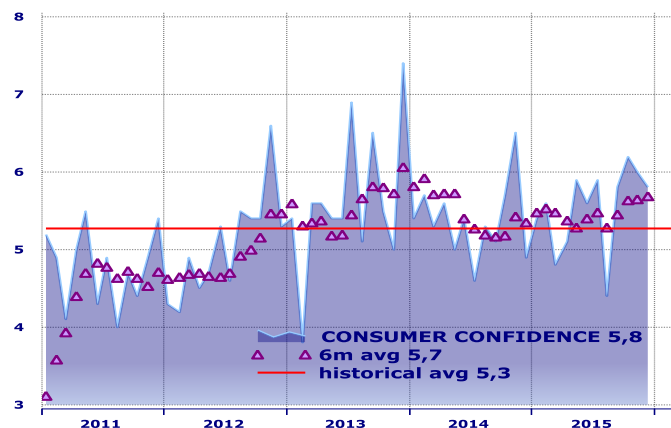
# HOUSEHOLDS' CONFIDENCE

Increase in households' confidence mostly reflects strong employment perspectives, but it's not a full fledged growth. Uncertainty persists on the medium term, due to industrial compartment tensions.

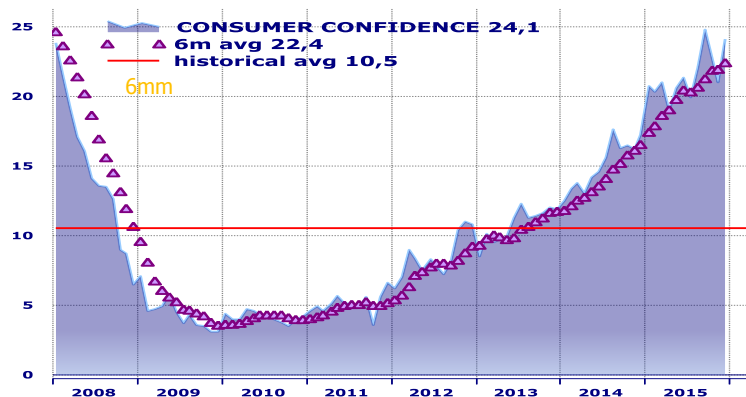
CONFERENCE BOARD: 6-MONTH FORECASTS ON ECONOMY



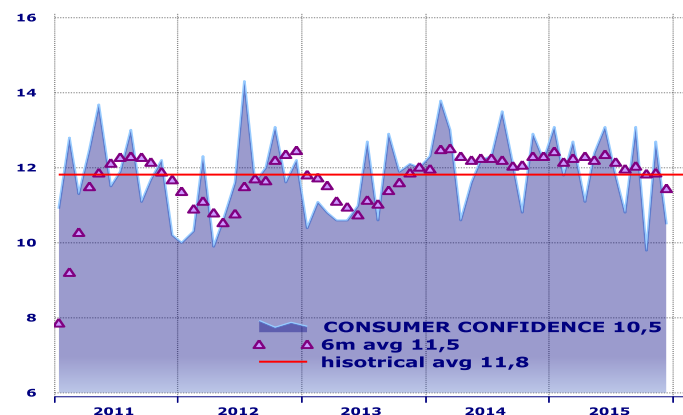
CONFERENCE BOARD: HOME BUYING INTENTIONS



CONFERENCE BOARD: JOBS PLENTIFUL

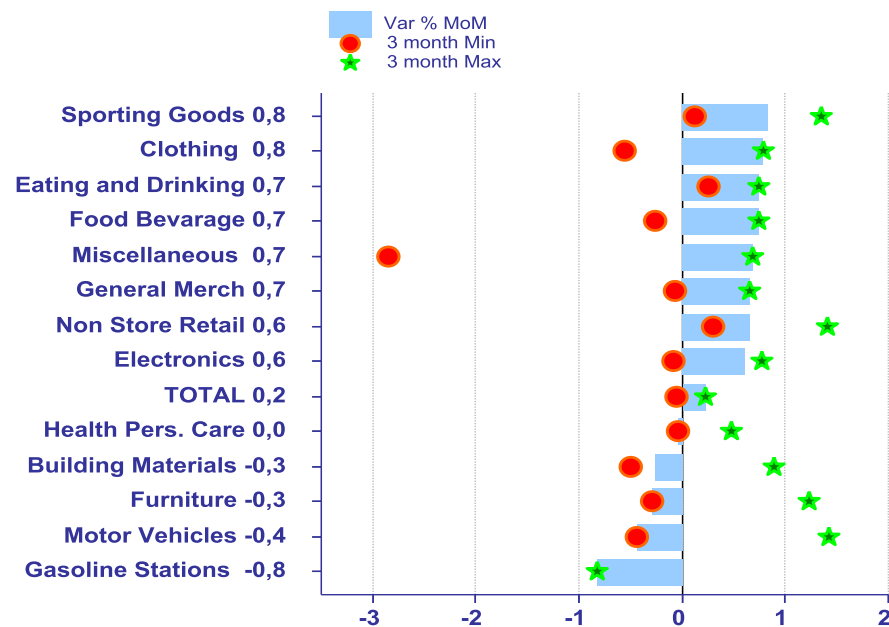


CONFERENCE BOARD : AUTO BUYING INTENTIONS

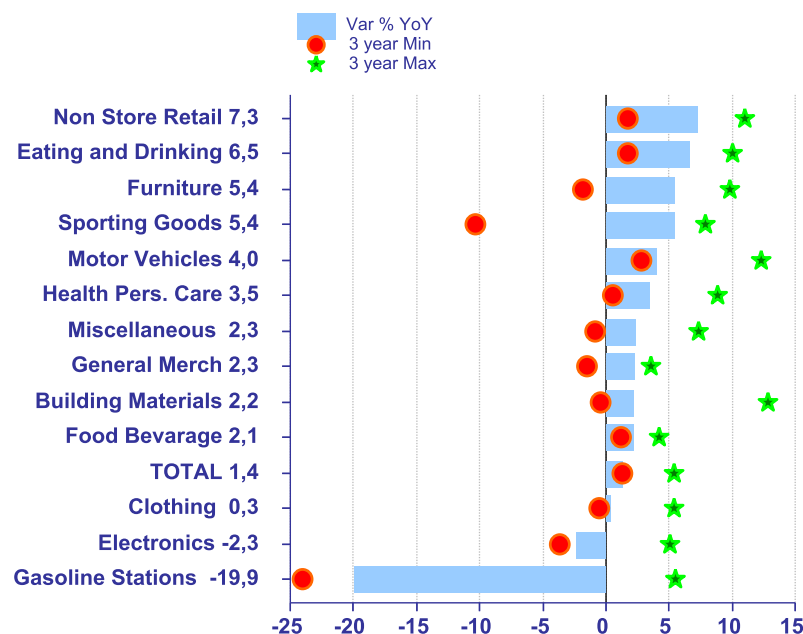


High frequency data on households' consumption in November shows signs of widespread recovery in private spending, overcoming most of the past months' uncertainty. Retail sales have grown by 0.2%, the greatest increase of the last four months, with strong increases in discretionary components like sports and leisure, clothing, electronics. Sales have still been penalised by decrease in gasoline station spending (-20% in annual terms).

RETAIL SALES – MONTHLY CHANGES

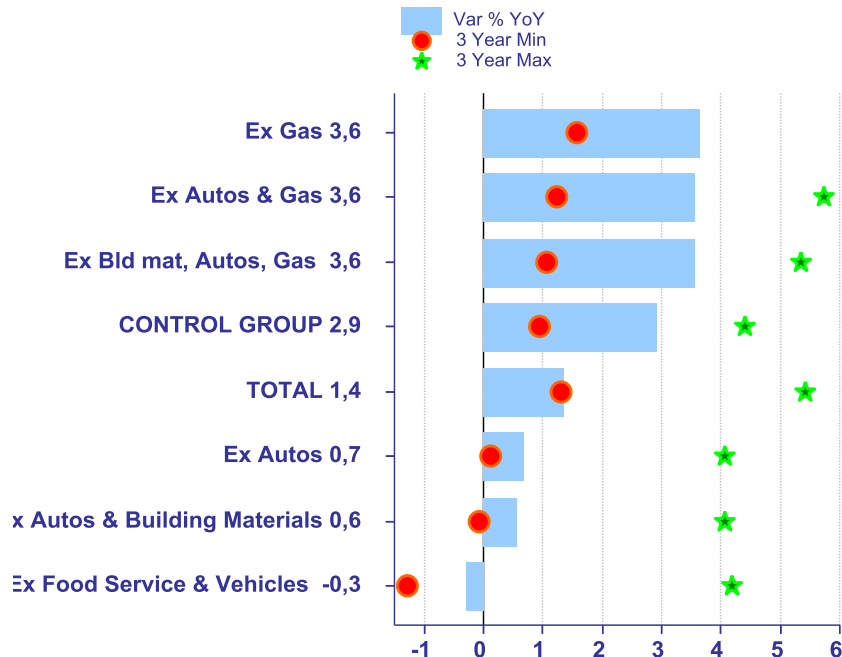


RETAIL SALES– YEARLY CHANGES



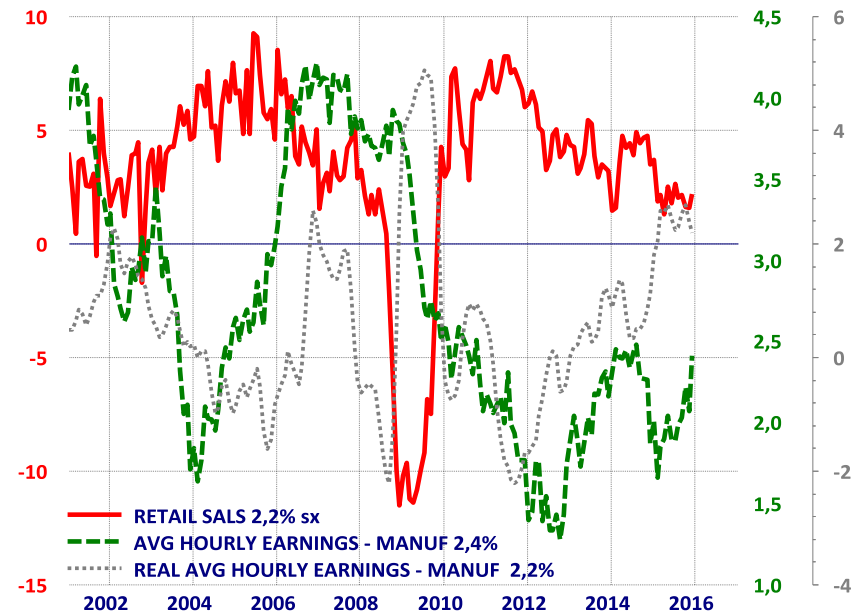
Retail sales trend growth rate (+1.4%) is only apparently weak compared to historical data. The dynamic is decidedly more robust (+3.6%) net of petrol spending, due to low inflation, which has significantly increased households' purchasing power.

## RETAIL SALES— YEARLY CHANGES

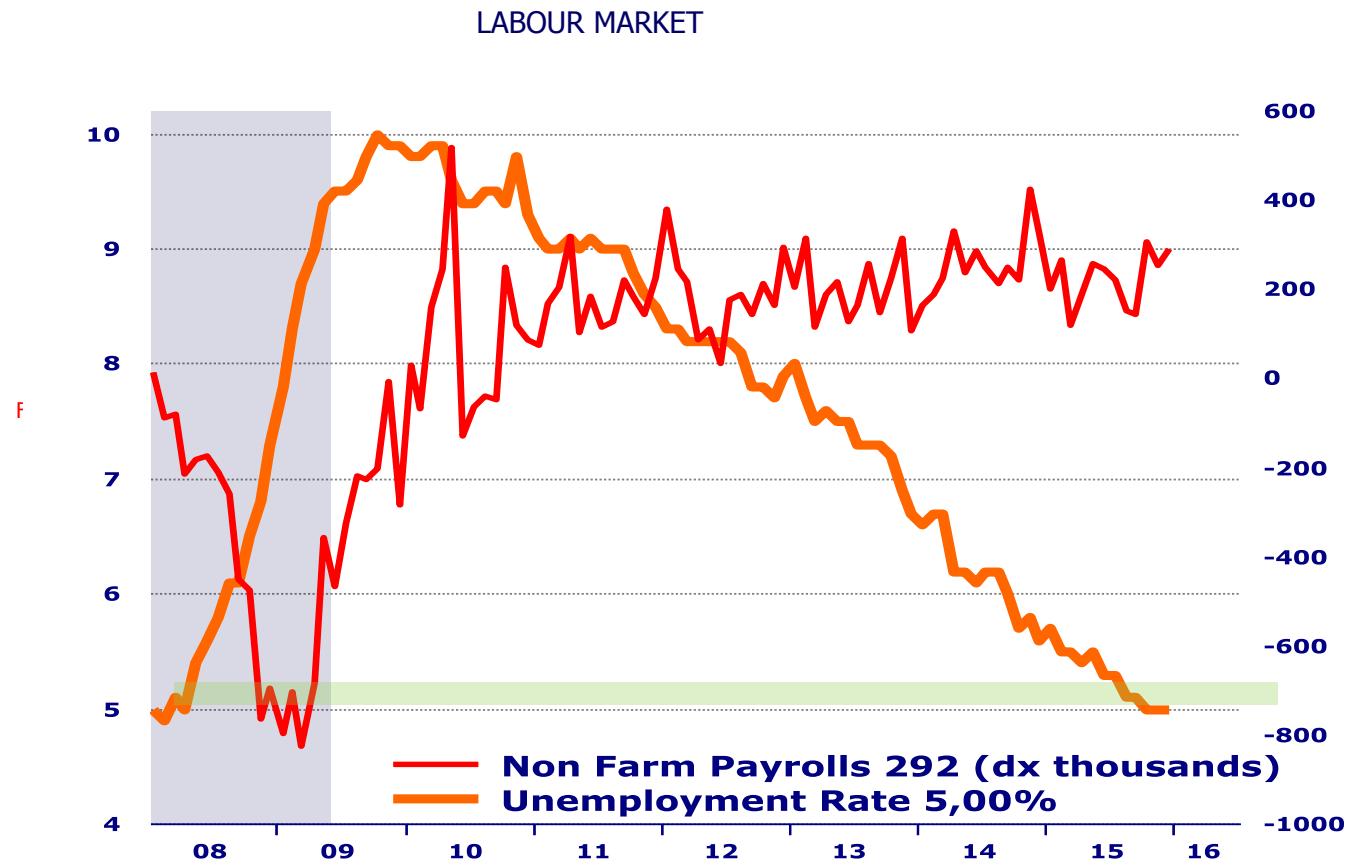


## CONSUMPTION AND WAGES

Changes— Real wages 3 month averages



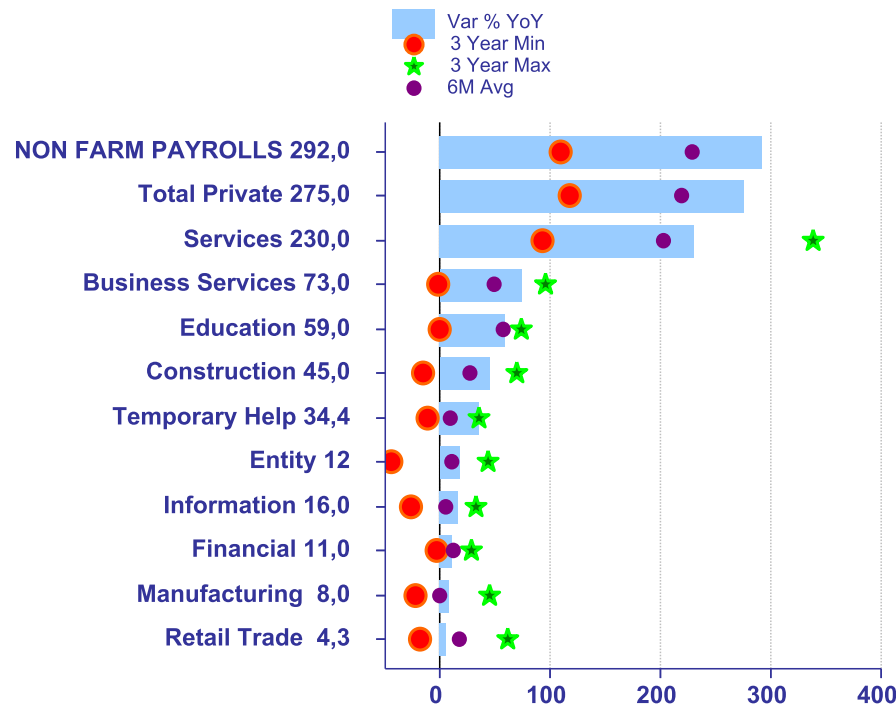
The recent persuasive labour market report supports the Fed's decision to raise the official rate. The unemployment rate is stable at a record low at 5%...



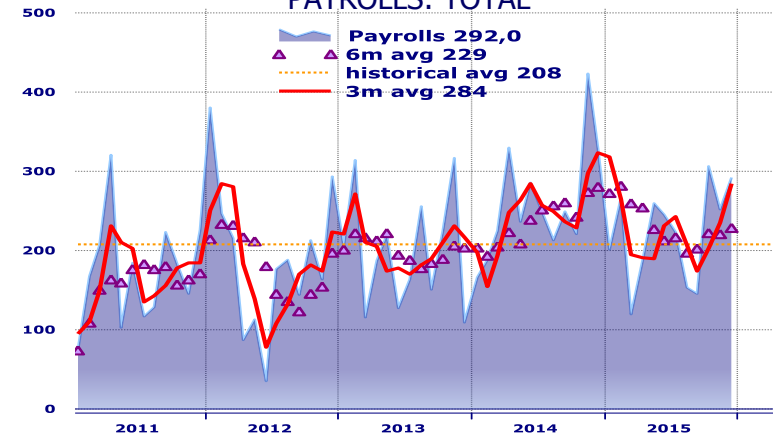


+211 K new jobs in November, above consensus (200 K); 509 K in the past two months only; 210 K on average since the beginning of the year... but weaknesses are not missing: still another negative figure for manufacturing... ..

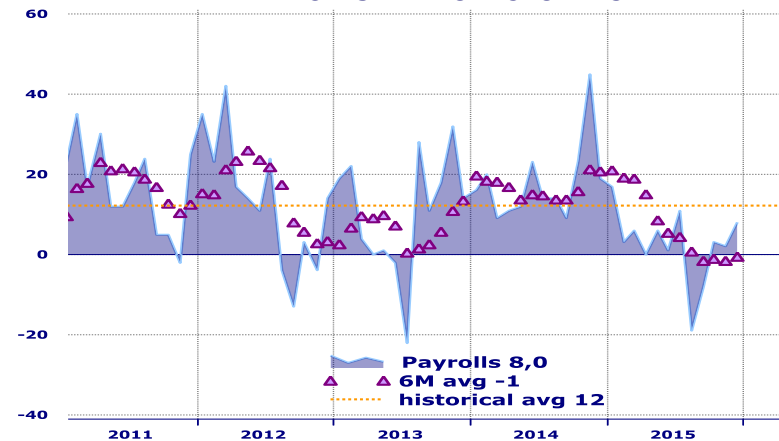
PAYROLLS: BY SECTOR



PAYROLLS: TOTAL

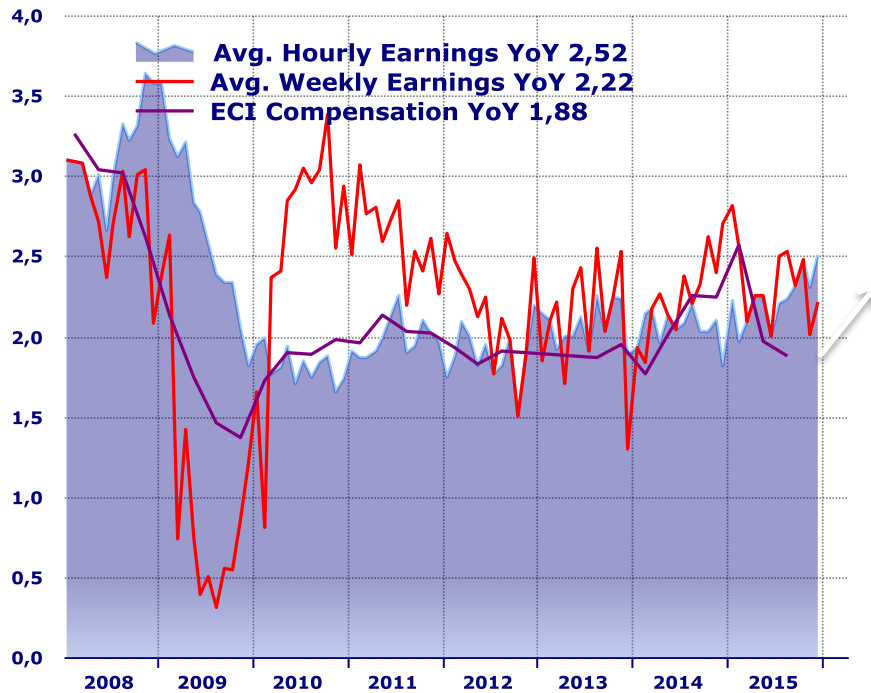


PAYROLLS: MANUFACTURING

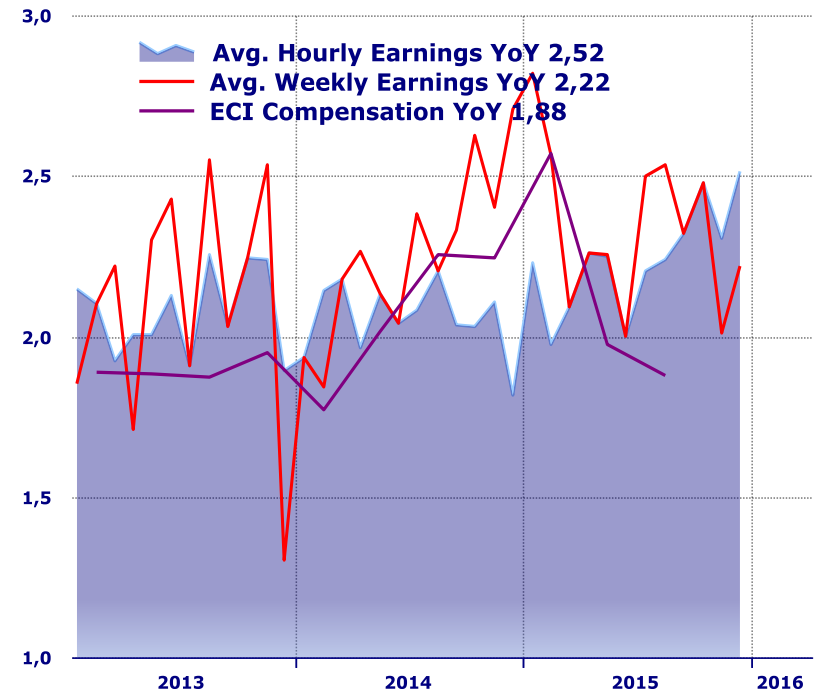


... and wages' dynamics are not too exciting yet.

LABOUR COSTS: LONG TERM

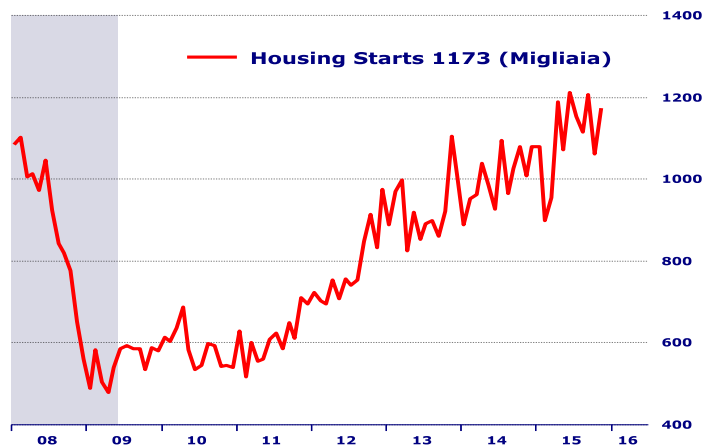


LABOUR COSTS: SHORT TERM

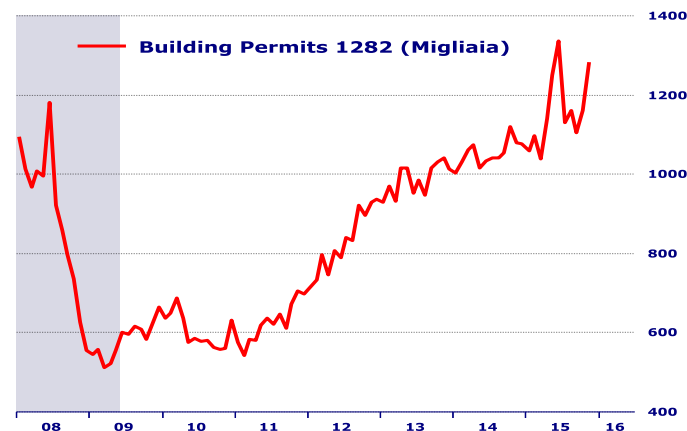


Real estate market indicators confirm their robustness although not at peak levels. After accelerating in the first half of 2015, reaching the past ten years' highs, residential compartment's growth has normalised. The sector is destined to offer moderate but persistent support to income formation.

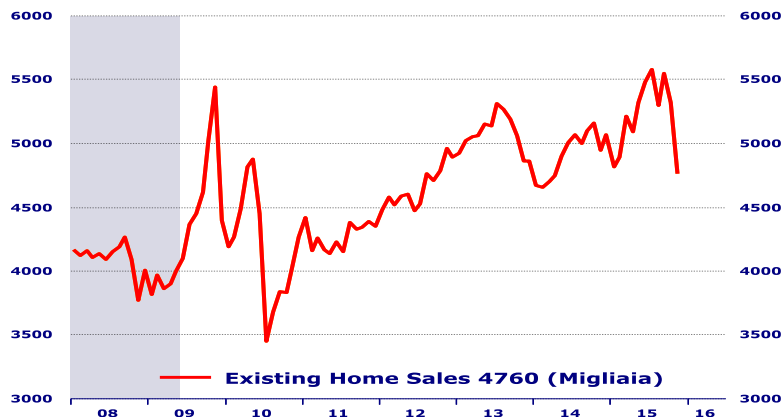
HOUSING STARTS



BUILDING PERMITS



EXISTING HOME SALES



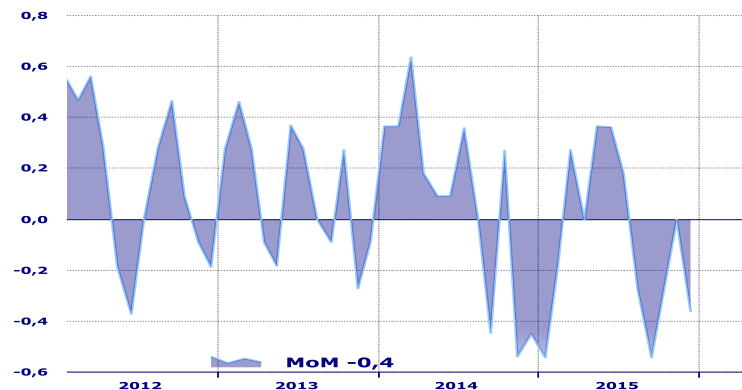
NAHB INDEX



# INFLATION

Upstream of the production line deflationary impulses still prevail, with the production prices index clearly decreasing by over one percentage point.

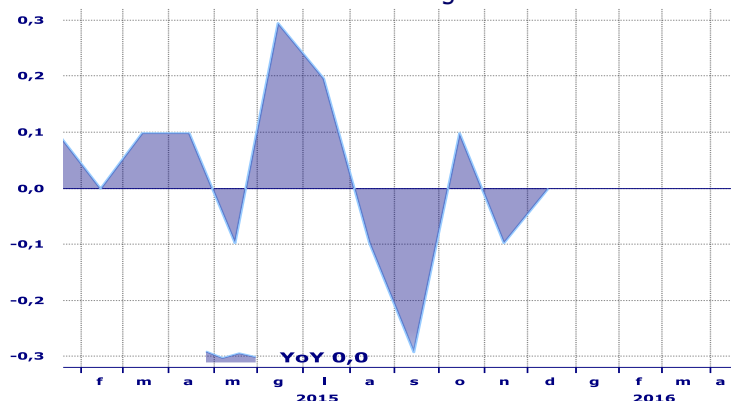
PPI – FINAL DEMAND  
MoM Changes



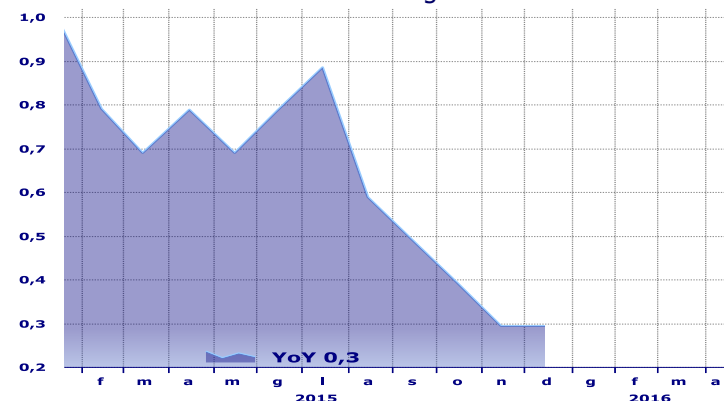
PPI – FINAL DEMAND  
YoY Changes



PPI – FINAL DEMAND ex food, energy, trade  
MoM Changes



PPI – FINAL DEMAND ex food, energy, trade  
YoY Changes



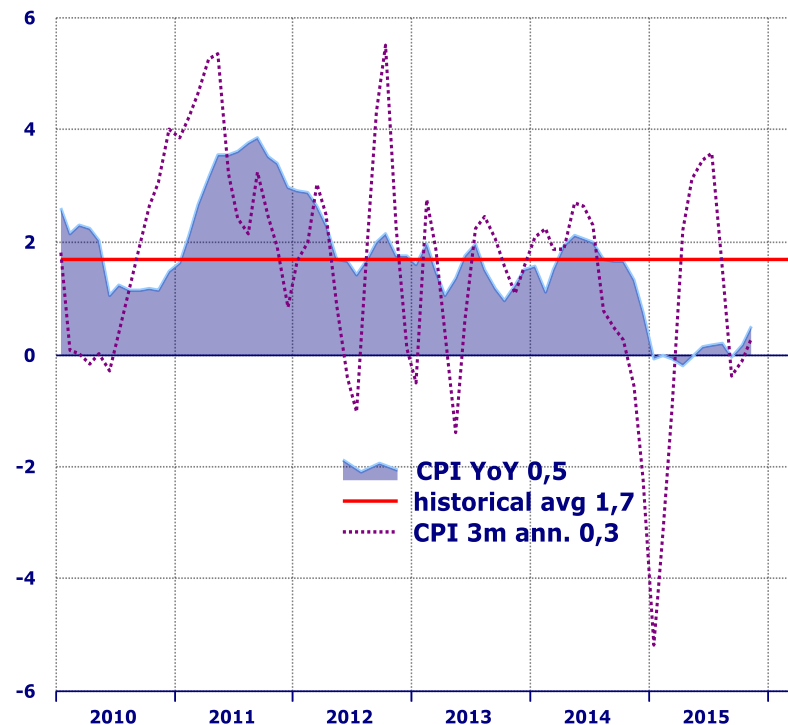
# INFLATION

General inflation grew in December by 0.5%, reaching almost a full year's highs, but downward pressures on energy prices persist.

PUMP PRICE FOR GASOLINE  
Average daily data; USD



HEADLINE INFLATION

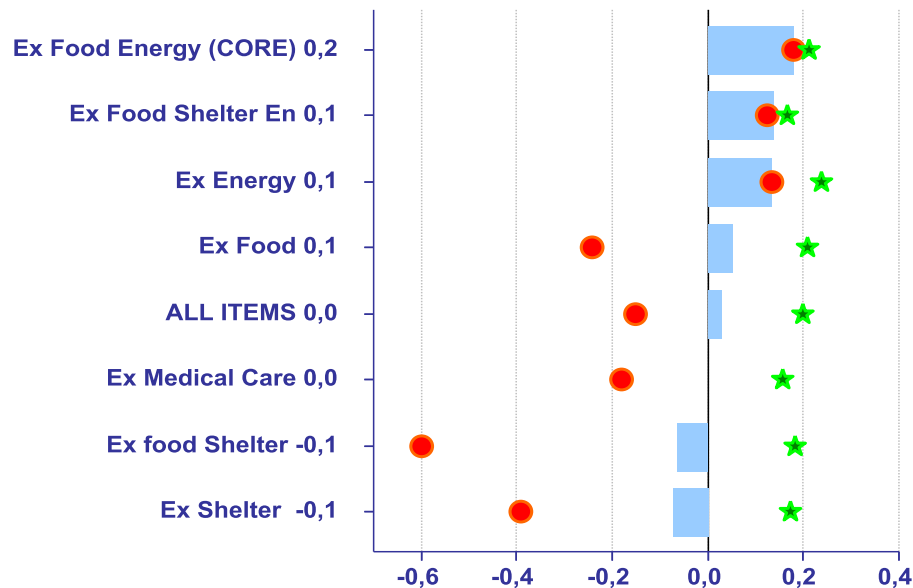


# INFLATION

The core index registered an increase by 0.2%, growing for the thirty first month in a row; the core trend rate reached 2.0%, highest since February 2013.

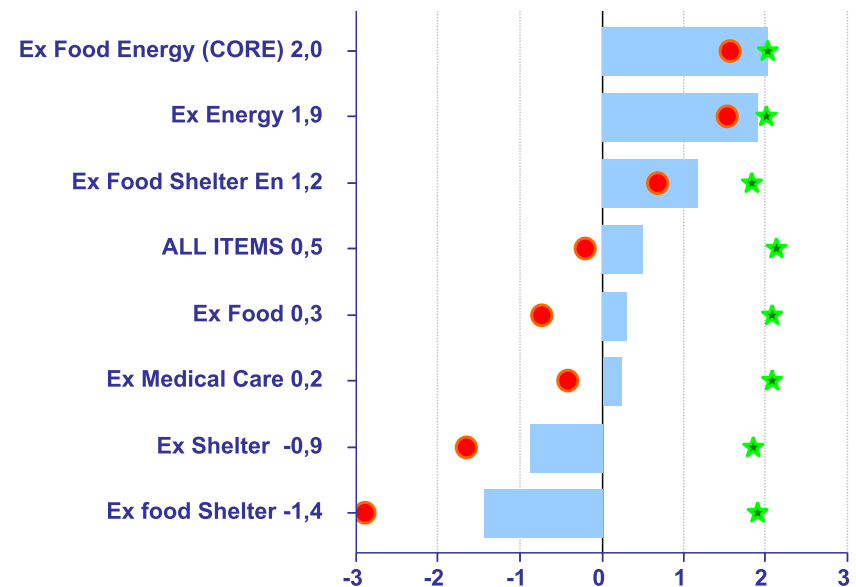
INFLATION Changes

Var % MoM  
3 month Min  
3 month Max



INFLATION Changes

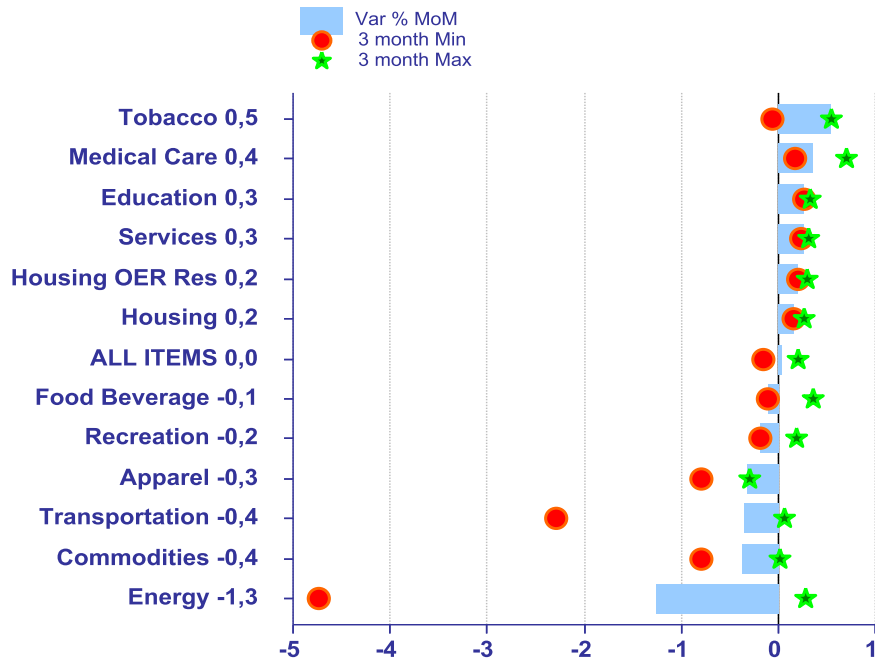
Var % YoY  
3 Year Min  
3 Year Max



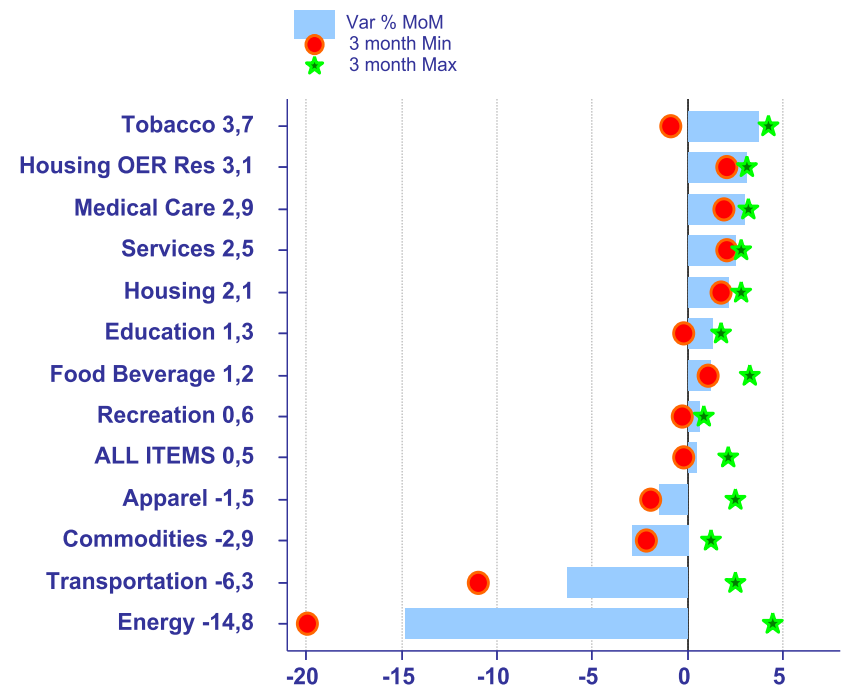
# INFLATION

The deflationary effect on energy prices is self evident.

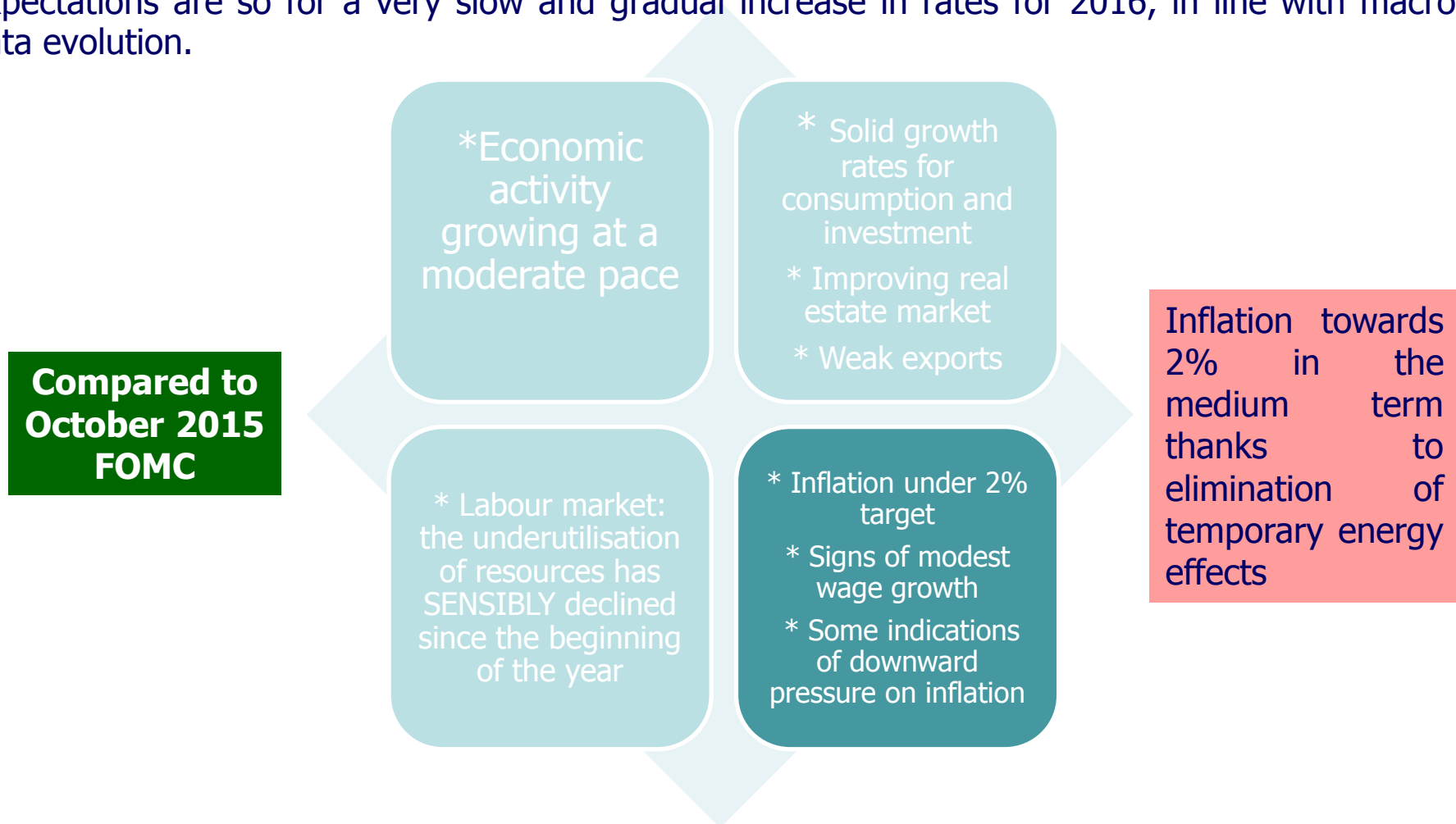
INFLATION BY SECTOR  
Changes



INFLATION BY SECTOR  
Changes



The FED has begun monetary policy's normalisation in December, despite the trade-off between robust domestic economy, except for issues in manufacturing, and global uncertainty. Expectations are so for a very slow and gradual increase in rates for 2016, in line with macro data evolution.





## FOMC December Meeting:

### UNANIMOUS VOTE ON RATE INCREASE

Time and intensity of rate adjustment will  
depend on evolution of macro conditions

Since inflation persists below 2%, it is  
necessary to carefully monitor inflation's  
progress towards target

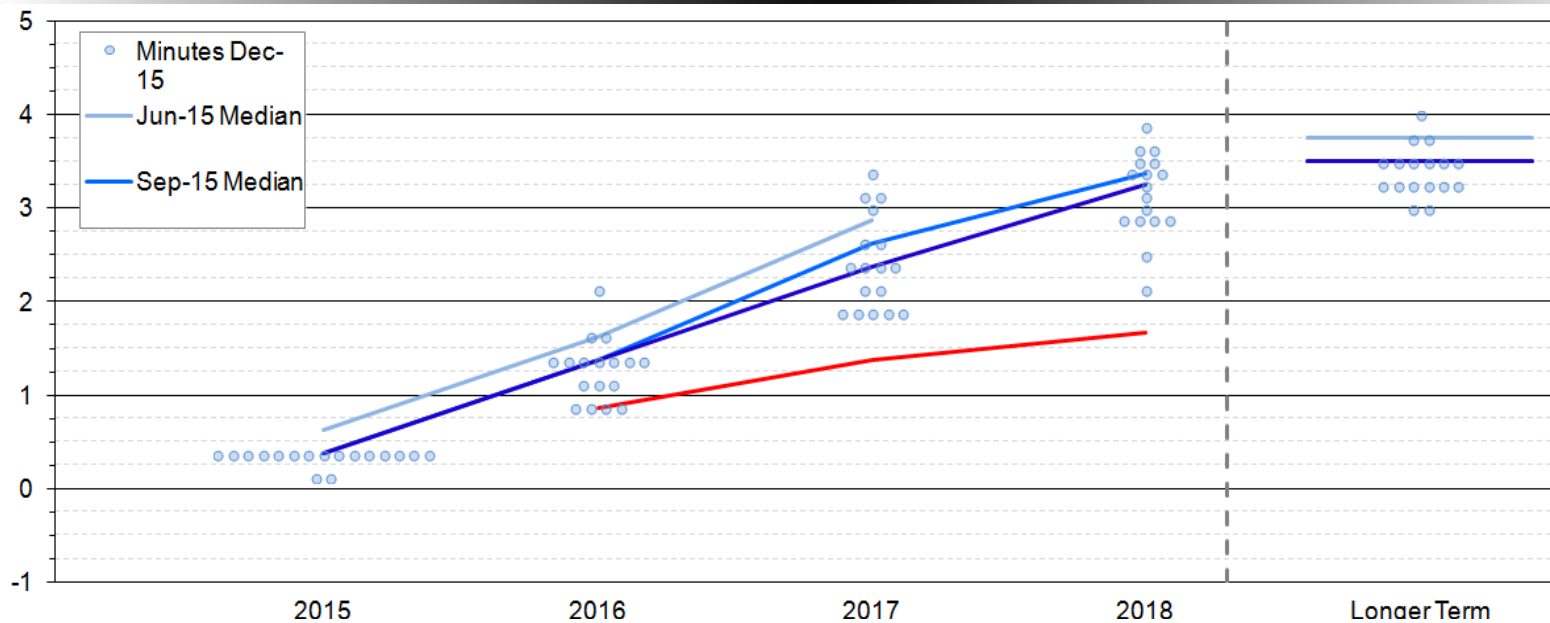
The Committee expects economic conditions  
to evolve so to require only **GRADUAL  
INCREASES** in the reference rate

Rate on Fed Funds is destined to remain for  
some time **BELOW LONG TERM  
EQUILIBRIUM LEVEL**

# MONETARY POLICY

The average expected rate for the end of 2016 according to the Fed is at 1.375, same as September; for the end of 2017 and 2018 rates are, respectively, at 2.375 and at 3.25. These values are sensibly higher than those expected by the market (OIS), more in line with Bloomberg's survey of economists, median is 1.25 for end of 2016..

## FOMC DOT PLOT



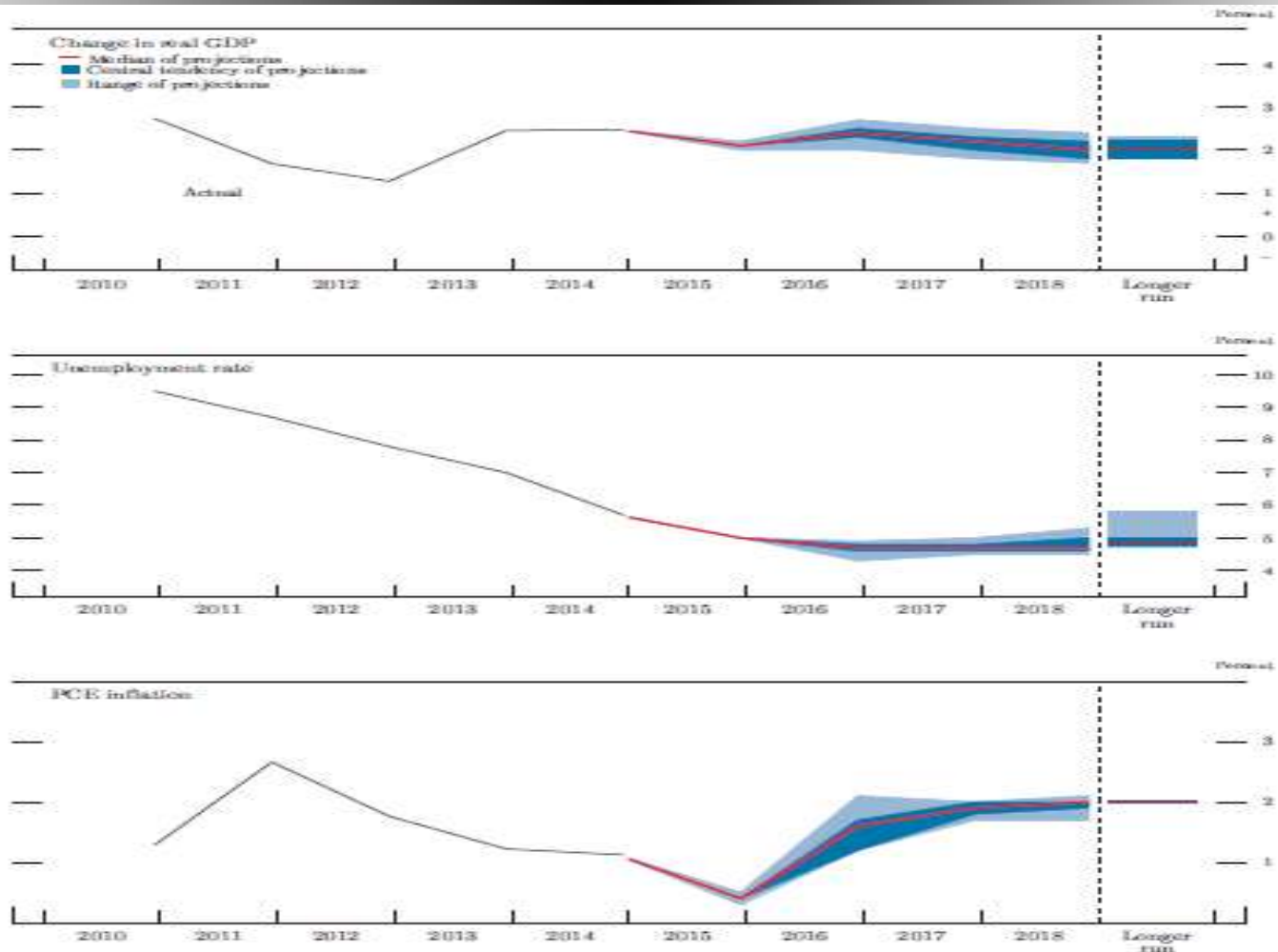
|               |       |       |       |       |      |
|---------------|-------|-------|-------|-------|------|
| Dec-15 Median | 0.375 | 1.375 | 2.375 | 3.25  | 3.5  |
| Sep-15 Median | 0.375 | 1.375 | 2.625 | 3.375 | 3.5  |
| Jun-15 Median | 0.625 | 1.625 | 2.875 |       | 3.75 |
| OIS           |       | 0.863 | 1.371 | 1.674 |      |

## FED: MACRO OUTLOOK

Percent

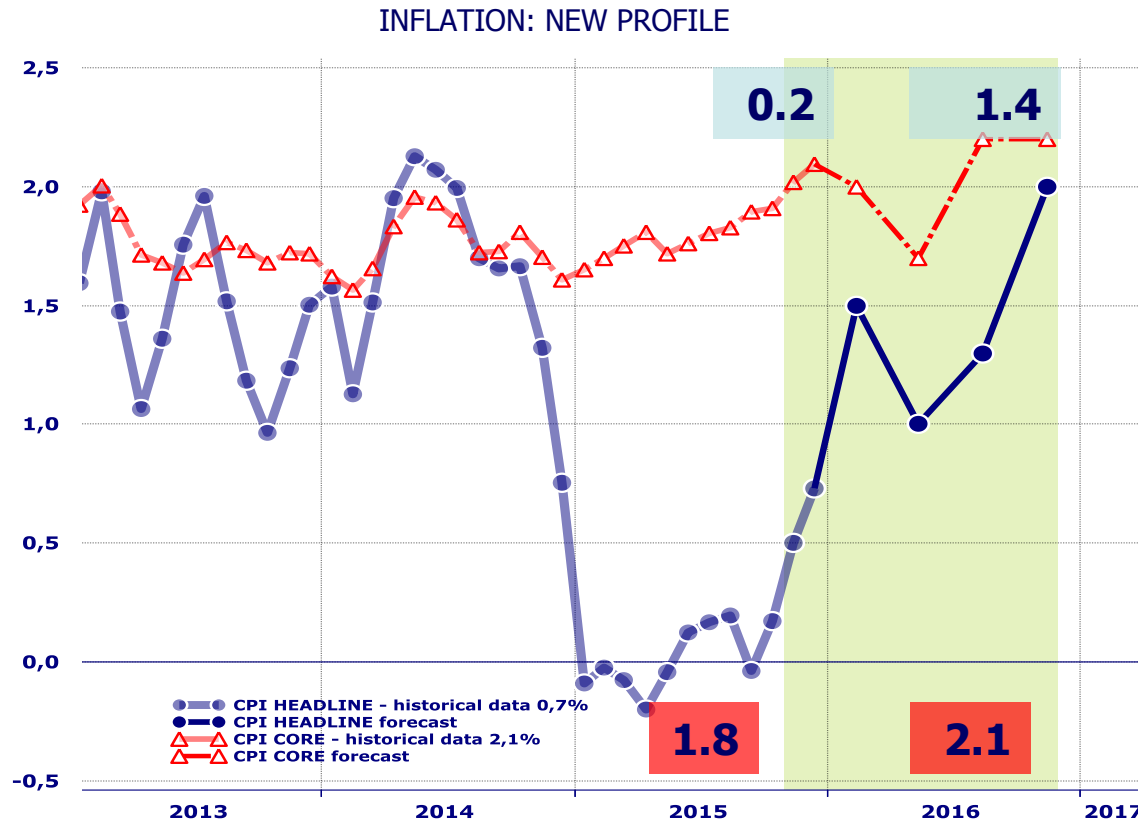
| Variable                                | Median <sup>1</sup> |      |      |      |            |
|---|---------------------|------|------|------|------------|
|   | 2015                | 2016 | 2017 | 2018 | Longer run |
| Change in real GDP                      | 2.1                 | 2.4  | 2.2  | 2.0  | 2.0        |
| September projection                    | 2.1                 | 2.3  | 2.2  | 2.0  | 2.0        |
| Unemployment rate                       | 5.0                 | 4.7  | 4.7  | 4.7  | 4.9        |
| September projection                    | 5.0                 | 4.8  | 4.8  | 4.8  | 4.9        |
| PCE inflation                           | 0.4                 | 1.6  | 1.9  | 2.0  | 2.0        |
| September projection                    | 0.4                 | 1.7  | 1.9  | 2.0  | 2.0        |
| Core PCE inflation <sup>4</sup>         | 1.3                 | 1.6  | 1.9  | 2.0  |            |
| September projection                    | 1.4                 | 1.7  | 1.9  | 2.0  |            |
| Memo: Projected appropriate policy path |                     |      |      |      |            |
| Federal funds rate                      | 0.4                 | 1.4  | 2.4  | 3.3  | 3.5        |
| September projection                    | 0.4                 | 1.4  | 2.6  | 3.4  | 3.5        |

## FED: MACRO OUTLOOK



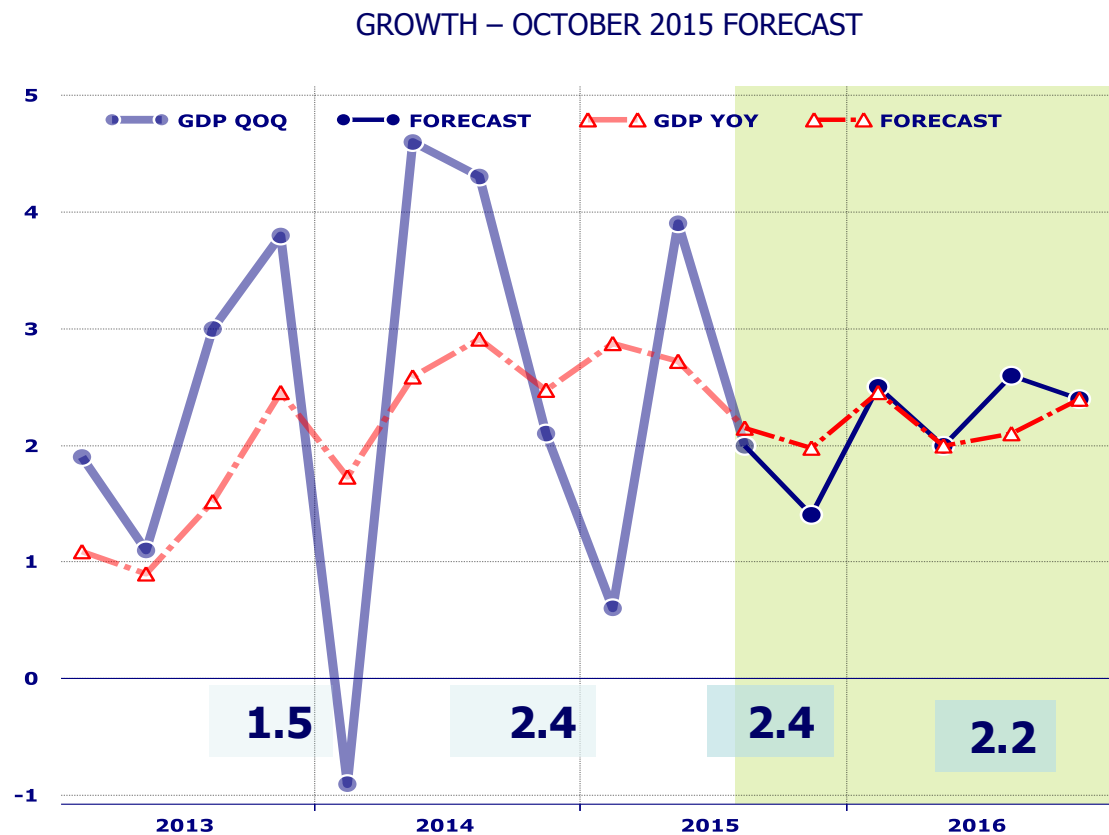
# OUR FORECASTS

The inflation profile is dominated by core index's resilience.



# OUR FORECASTS

Growth should continue, but at a moderate pace.



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