



Global Economy Report

September-October 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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- ❖ The IMF's preparatory note for the G20 in Hangzhou, China, signals the fifth year in a row with global growth lower than long term average. The risk of being trapped in low growth forever is serious without fiscal support of demand, structural reforms and impulse in international trade.
- ❖ International trade and global industrial activity reached the minimum of the downward trend without offering convincing signals of recovery.
- ❖ We thus believe in an acceleration in the short term: the manufacturing index is close to the expansion area for the productive system, while the continuation of the recovery phase for commodities makes growth in international trade very likely. Some risks for this evolution lie in Brexit's compressive effects, in geopolitical issues, and domestic and international security problems.

- ❖ As to the main markets, the shock due to Brexit has been reabsorbed quickly on the bond market, where the search for quality and safety only for a few days mingled with a downward trend due to super-expansive monetary policy or, as in the Fed's case, due to procrastination of the wait and see approach. On the stock market, the referendum has been reabsorbed completely, with the exception of the Italian index that suffers from endogenous compressive impulses.
- ❖ The UK's exit from the EU is a structural change in the country's conditions, influencing so far mainly its exchange rate with the US dollar and all other currencies.
- ❖ The other exchange rates dynamics, mostly the depreciation against the US dollar, principally followed the swing in expectations on the Fed's intervention on rates, with the exception of the yen, as the BoJ, against consensus, didn't increase QQE.

- ❖ In the USA, the revision of GDP's historical series, coupled with a disappointing growth figure for the second quarter, forced a mechanical correction of growth forecasts for 2016 at 1.4% (from previous 2%).
- ❖ However, macro parameters appear solid. In the summer months, business confidence rebounded, both in industry and services. Consumption and domestic demand confirm their robustness. For the labour market, the June/July data on new payrolls are extraordinarily strong and make the weak statistics from May and August appear extemporary.
- ❖ We forecast a solid and constant growth in the next quarters, with an acceleration at 2.2% in 2017. Inflation under control, expected at 1.3% this year and at 2.2% in 2017.
- ❖ Fed very cautious: we foresee only one increase in rates this year. Markets still assign a rather low probability this event.

❖ In the euro area, national accounts have signalled a slowdown in growth in the second quarter of the year, in line with consensus. The decrease is stronger in France and Italy, that are in stagnation, while Germany maintains a satisfactory expansive impulse.

❖ The interesting figure for Eurozone is the better than expected performance of leading indicators and in particular of PMI, which are strongly correlated to economic activity. Thanks to this dynamic, Brexit's effect at the moment is not as bad as expected and growth rates may be slightly increased.

❖ We thus correct our growth estimate by one tenth for 2016 to 1.6% and by two tenths for 2017 at 1.2%. Inflation is forecasted at 0.2% for 2016 and at 1.3% for 2017.

❖ Japan's income has stagnated in the second quarter, registering zero change based on annualised quarterly data and +0.2% on an annualised basis and missing forecast targets (+0.2% and +0.7% respectively). It's a clear slowdown compared to the first quarter and a significant loss of macro impulse. Growth forecast for 2016 is at 0.4%, inflation forecast is at -0.2%, confirming Japan's stagnation (partly due to statistic reasons relative to the leap year).

❖ In the second quarter of 2016, Chinese product increased at a yearly rate of 6.7%, in line with the previous period, but above expectations. Looking at annualised quarterly data, the system accelerated at 1.8%, significantly higher when compared to the previous period. The figure suggests a significant resilience of the economic cycle and confirms the perspective of the system's orderly slowdown. We expect GDP growth around 6.5% for 2016 and 2017, with inflation around 2%.

EXECUTIVE SUMMARY

	2010	2011	2012	2013	2014	2015	2016E	2017E
GDP (%YOY)								
US	2.5	1.6	2.3	2.2	2.4	2.4	1.4	2.2
EUROZONE	2.0	1.6	-0.9	-0.4	0.9	1.6	1.6	1.2
GERMANY	4.2	3.6	0.4	0.1	1.6	1.4	1.7	1.1
FRANCE	2.0	2.1	0.2	0.7	0.2	1.2	1.3	1.0
ITALY	1.7	0.6	-2.8	-1.7	-0.4	0.8	0.8	0.6
UK	1.9	1.6	0.7	1.7	2.9	2.2	1.7	-0.3
JAPAN	4.7	-0.4	1.7	1.6	-0.1	0.6	0.4	0.6
BRAZIL	7.6	4.0	1.8	2.8	0.2	-3.8	-3.5	1.0
RUSSIA	4.5	4.3	3.4	1.3	0.6	-3.7	-0.7	1.3
INDIA	8.9	7.5	5.1	4.6	7.2	7.6	7.4	7.4
CHINA	10.4	9.3	7.7	7.7	7.3	6.9	6.5	6.3
AUSTRALIA	2.3	2.7	3.6	2.0	2.8	2.5	2.9	2.9
KOREA	6.5	3.7	2.3	2.9	3.3	2.6	2.6	2.7
INFLATION (%YOY)								
US	1.6	3.2	2.1	1.5	1.6	0.1	1.3	2.2
EUROZONE	1.6	2.7	2.5	1.4	0.4	0.0	0.2	1.3
GERMANY	1.1	2.5	2.1	1.6	0.8	0.1	0.4	1.5
FRANCE	1.7	2.3	2.2	1.0	0.6	0.1	0.3	1.2
ITALY	1.6	2.9	3.3	1.3	0.2	0.1	0.0	1.0
UK	3.3	4.5	2.8	2.6	1.5	0.0	0.7	2.2
JAPAN	-0.7	-0.3	0.0	0.4	2.7	0.8	-0.2	0.5
BRAZIL	5.0	6.6	5.4	6.2	6.3	9.0	8.6	5.5
RUSSIA	6.9	8.5	5.1	6.8	7.8	15.6	7.3	5.5
INDIA	12.1	8.9	9.3	10.9	6.4	5.9	5.0	5.4
CHINA	3.3	5.4	2.7	2.6	2.0	1.4	2.0	2.0
AUSTRALIA	2.9	3.3	1.8	2.5	2.5	1.5	1.3	2.1
KOREA	3.0	4.0	2.2	1.3	1.3	0.7	1.0	1.6

Banca Aletti Forecast

Cons. Bloomberg (Set16)

Historical Data

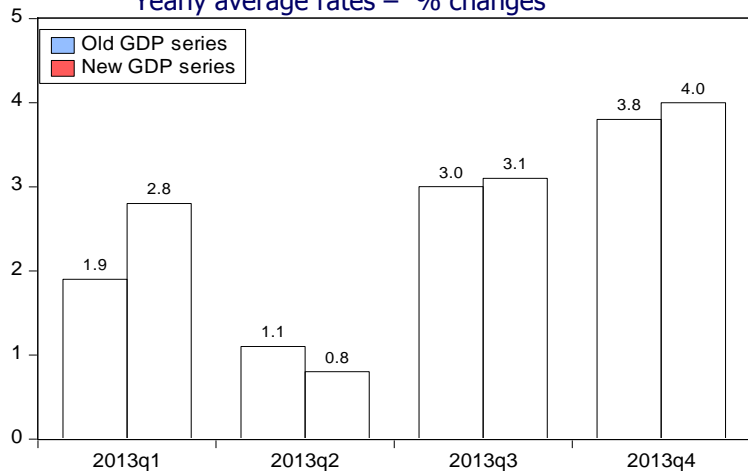
The US Outlook

GROWTH IN Q2-16

The BEA (the statistics office) has recalculated the historical series of national accounting since 2013, changing substantially the US economy's profile. The revision particularly hit the second and fourth quarter 2015...

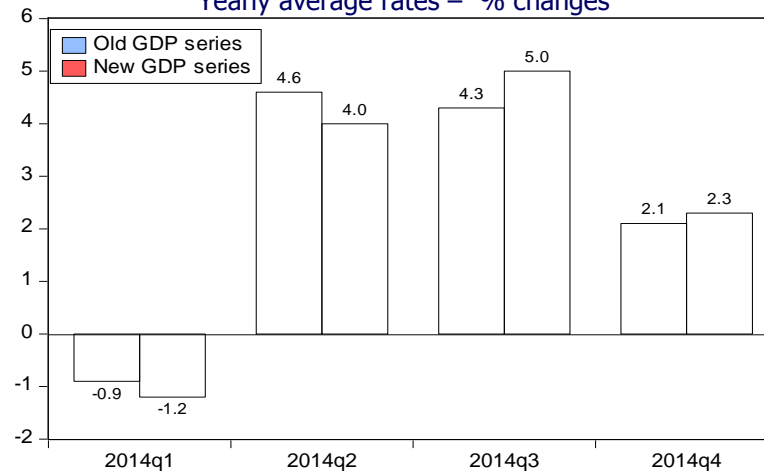
2013

Yearly average rates – % changes



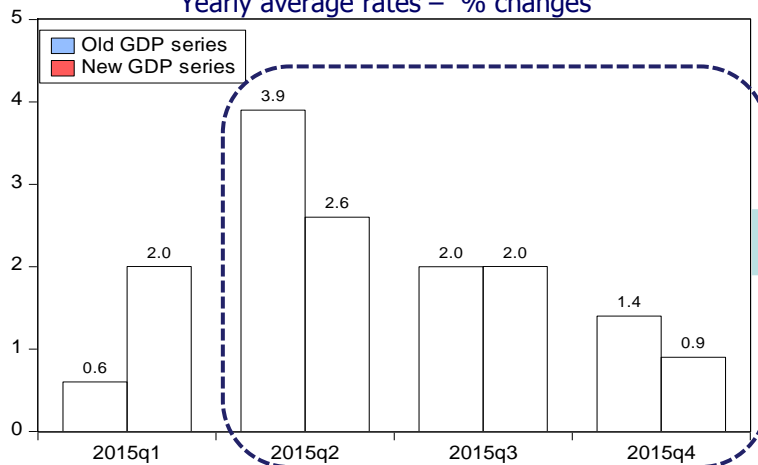
2014

Yearly average rates – % changes



2015

Yearly average rates – % changes



-1.8 GDP points in the last three quarters of 2015

Slower take off in 2016

Growth at 0.5%
Instead of 0.8%

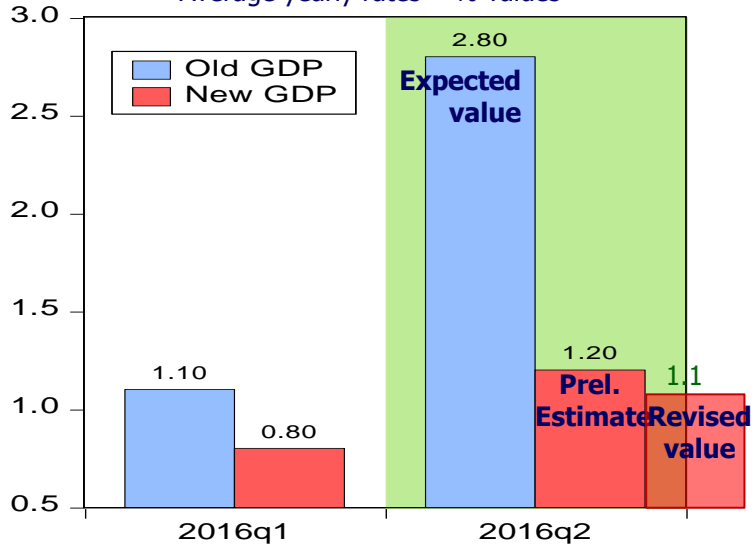
GROWTH IN Q2-16

Next to the compression due to the drag effect, 1Q 2016 income was trimmed by three tenths to 0.8%. The second quarter estimate, instead, was disappointing and far from expectations: only 1.1% versus consensus at +2.5%. The combination of these effects produced a mechanical downward revision on the expected average growth rate for 2016 from 2.0% to 1.4%, implying only a marginal correction in 2017.

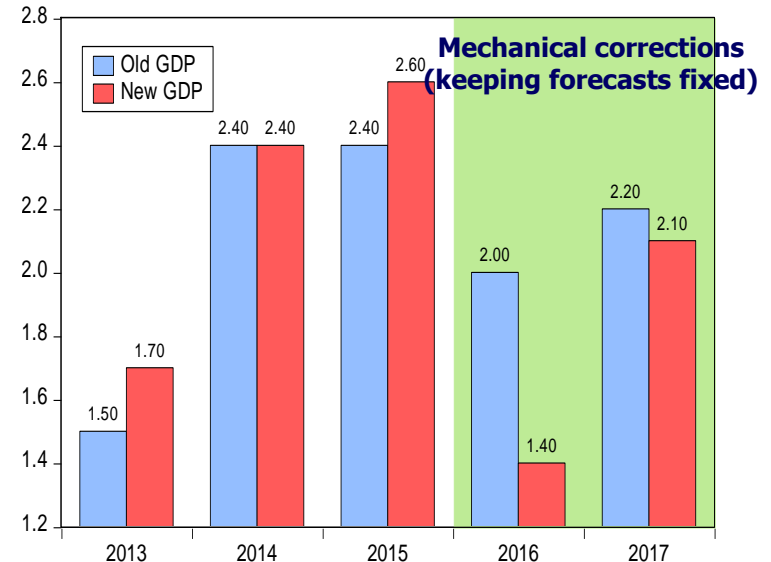


2016

Average yearly rates – % values



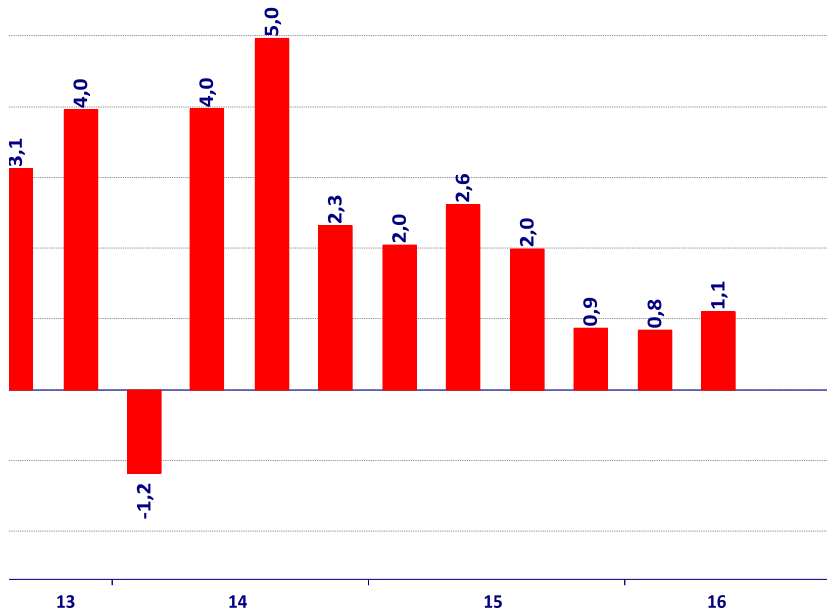
AVERAGE YEARLY RATES



In the past three quarters, the US economy grew on average at less than 1%, compared to the previous four quarters at 2.5% (from Q4-15 to Q3-16). In terms of annualised quarterly growth, growth rate is down to 1.2%, slowing down for the fifth consecutive quarter, at Q2-2013 lows, over two points below beginning of 2015 levels.

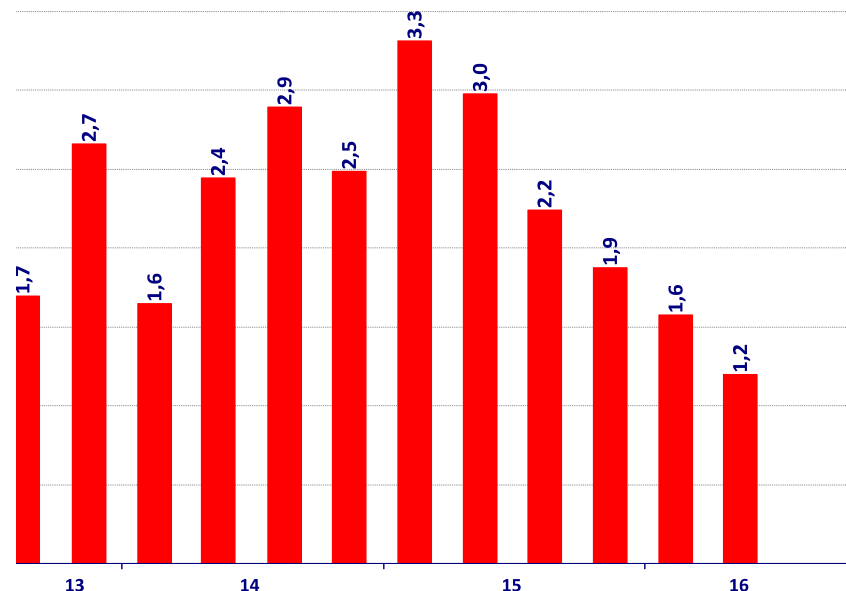
USA – GDP Q2-16

Annualised quarterly rates – % values



USA – GDP Q2-16

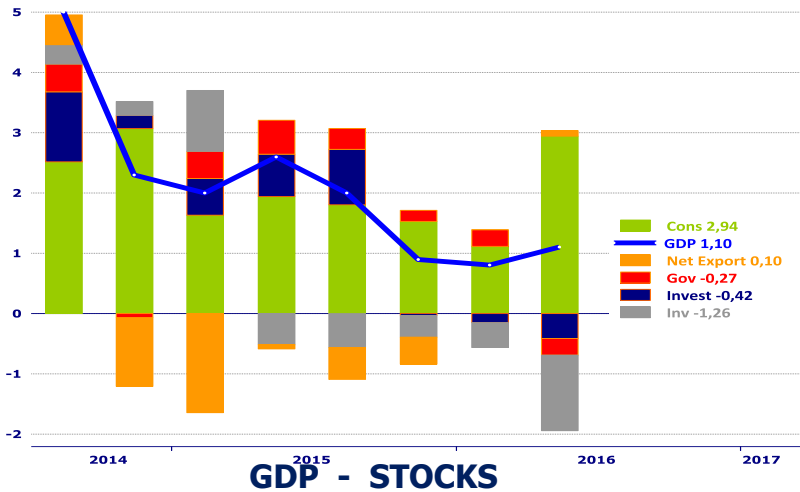
tendenziali rates - % values



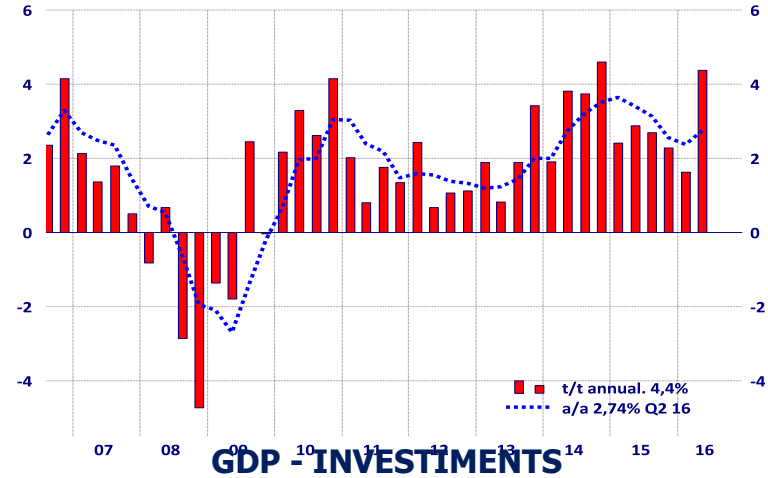
GROWTH IN Q2-16

The figure, that apparently describes a worse economic scenario than expected, reflects the negative contribution from stocks, which subtracts 1.3 GDP points, the worse figure since 2011. Consumption is the most resilient factor in the US economy, at +2.94%, more than double than in the previous period (+1.11%). Thus the expansive phase may continue, though penalised by lack of investments

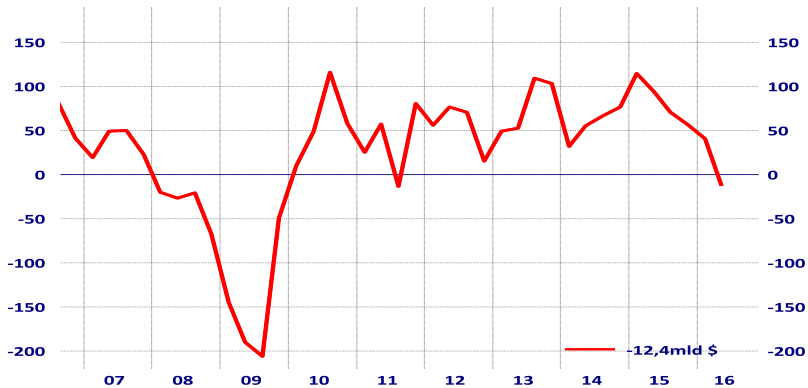
GDP – GROWTH CONTRIBUTIONS- % OF GDP



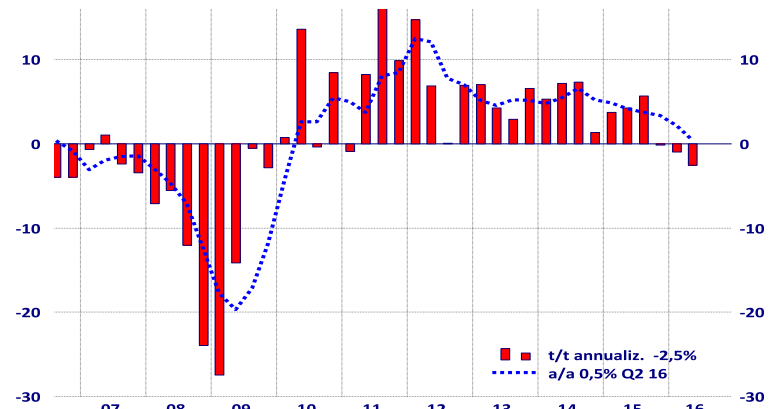
GDP - CONSUMPTION



GDP - STOCKS



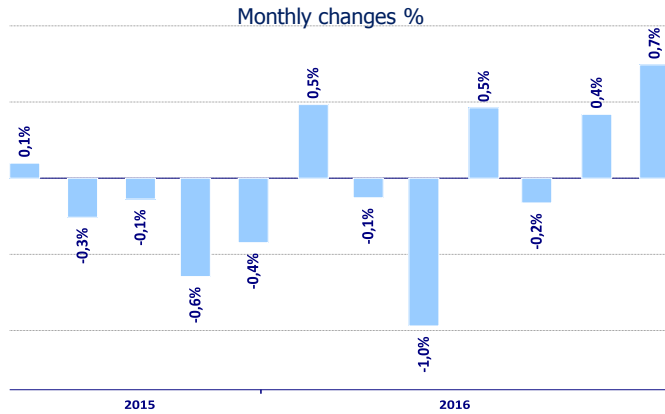
GDP - INVESTMENTS



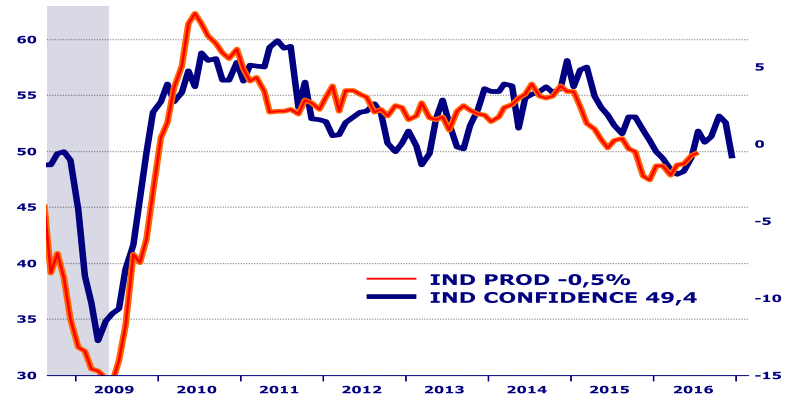
INDUSTRY

For over a year, industry has witnessed the greatest uncertainties in global growth, thus slowing down the economy. In 2016 the progressive recovery in business confidence signals the change in this sector, which is now in a clear stabilisation phase. On an annual basis, production is still declining, but the gradual improvement in orders projects a better industrial cycle. The July increase (+0.7%) is the highest of the past year and a half.

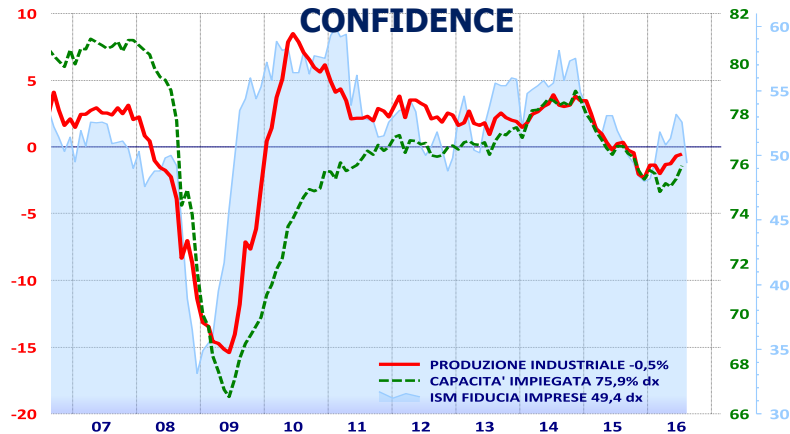
INDUSTRIAL ACTIVITY



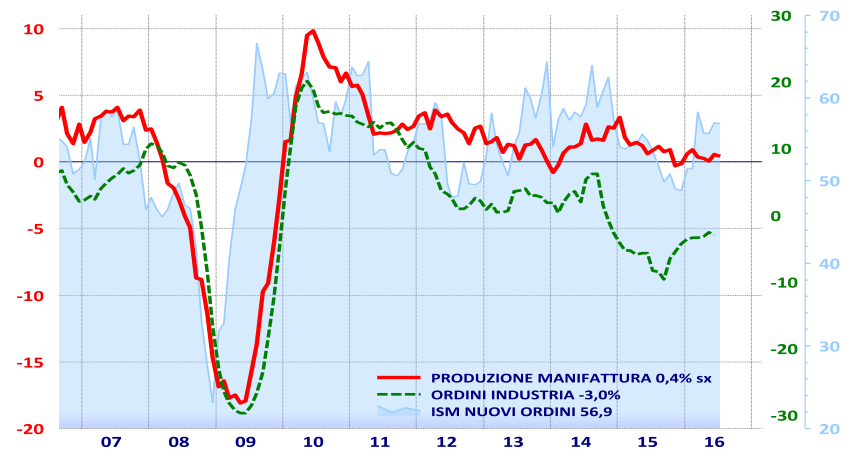
PRODUCTION AND CONFIDENCE



INDUSTRIAL ACTIVITY AND CONFIDENCE



INDUSTRIAL ACTIVITY AND ORDERS

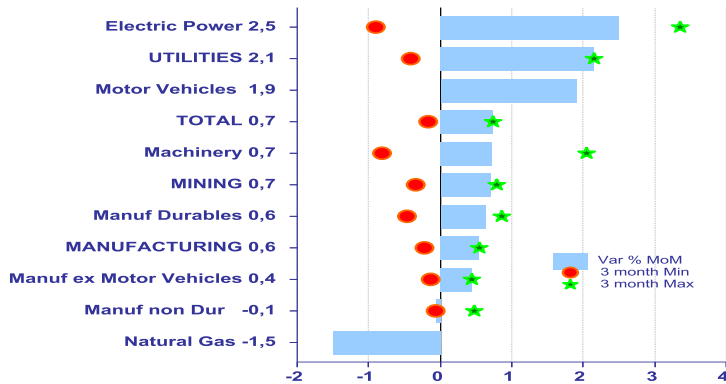


INDUSTRY

July's strong increase in manufacturing is positive. The improvement in industry has been coherent with the weaker exchange rate and the recovery of energy prices, two dynamics that in July have suffered but in August improved. International demand's lesser negative impulses have also favoured the sector's recovery, that however continues to be negatively influenced by overly high stocks. The stocks/sales ratio is still close to 2009 highs.

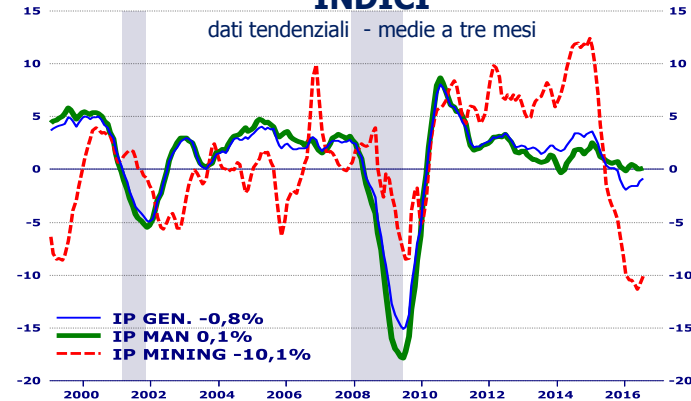
ATTIVITA' INDUSTRIALE

Scomposizione per gruppo merceologico

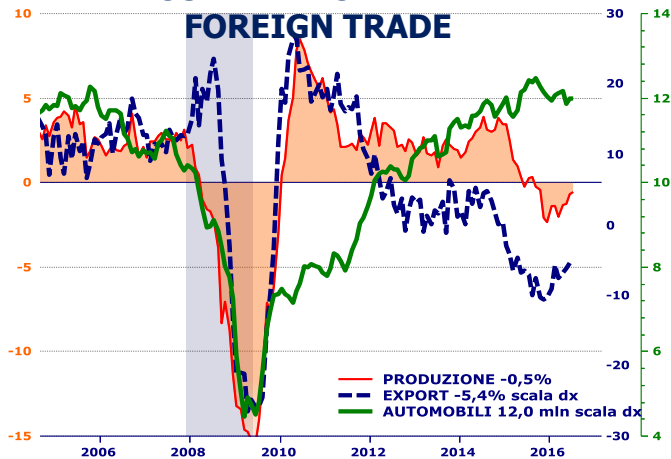


ATTIVITA' INDUSTRIALE – VARI INDICI

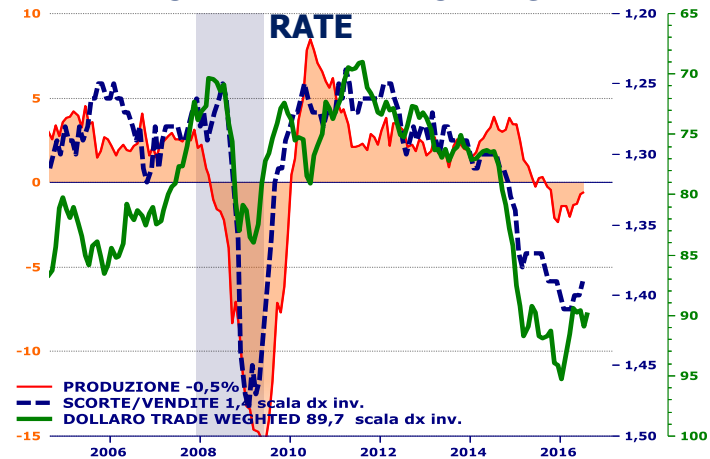
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INDUSTRIAL ACTIVITY AND FOREIGN TRADE

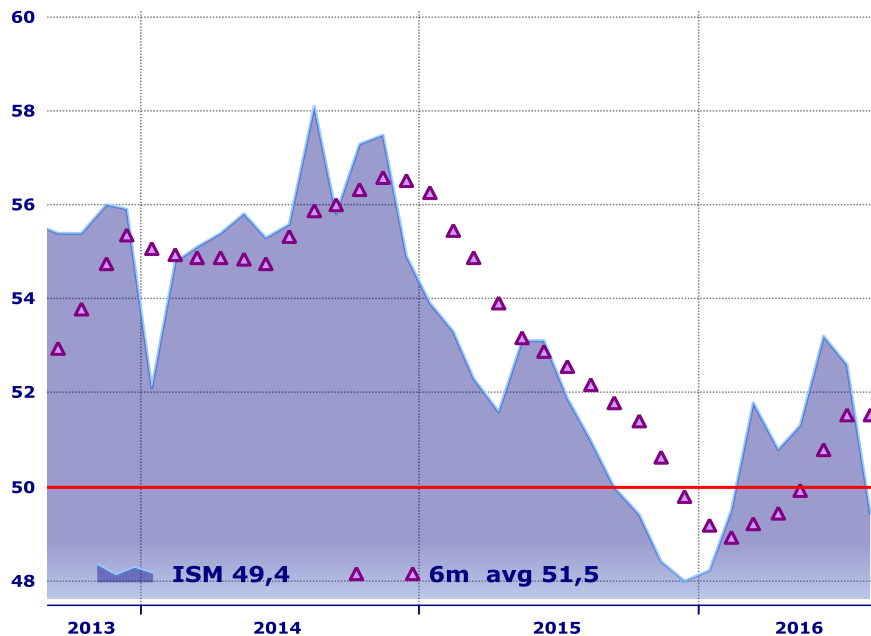


IND. ACTIVITY AND EXCHANGE RATE

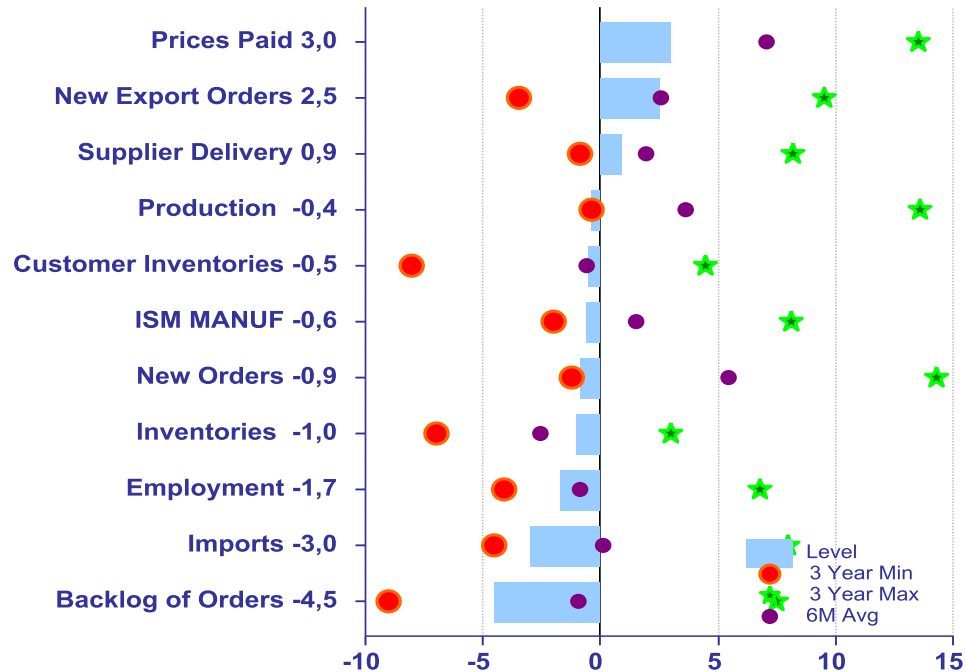


The manufacturing leading indicator in August had a significant decrease, completely unexpected, that brought it below the 50 point threshold for the first time in the past six months. The six month average signals the permanence of expansive conditions...

MANUFACTURING ISM

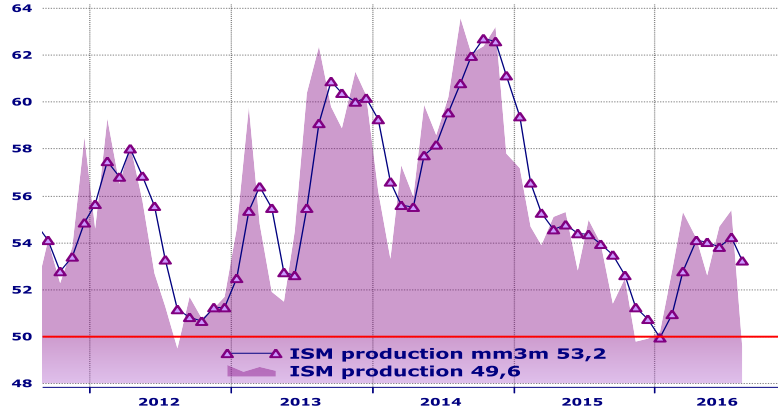


MANUFACTURING ISM – DETAIL

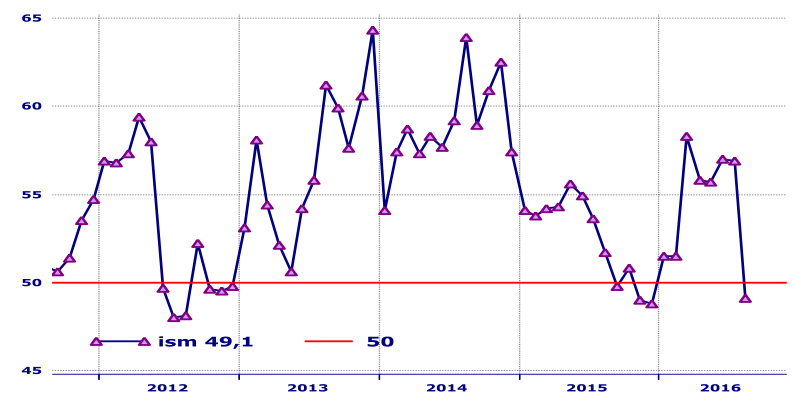


The survey shows a marked worsening of all the main segments....

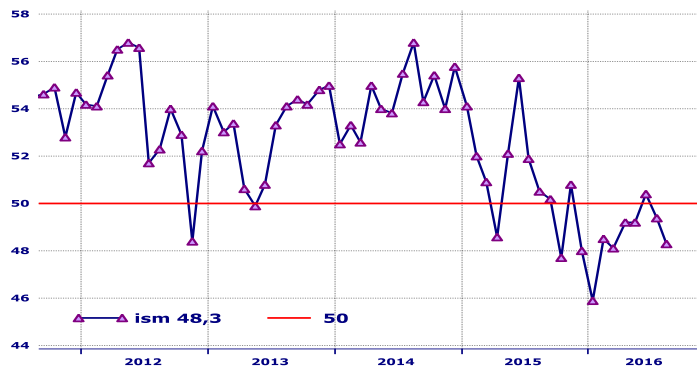
ISM PRODUCTION



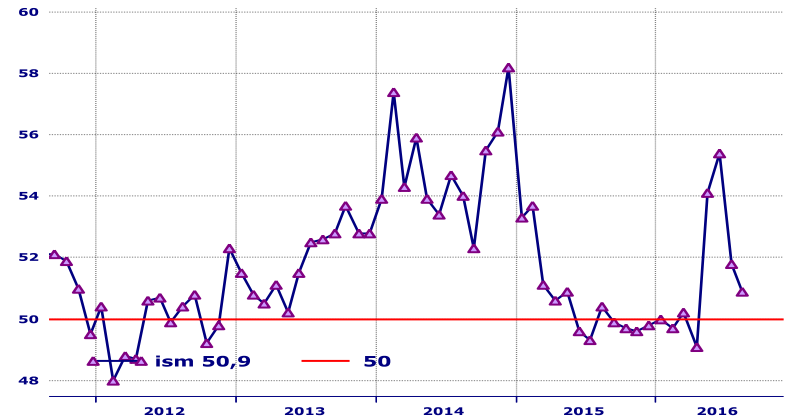
ISM NEW ORDERS



ISM EMPLOYMENT

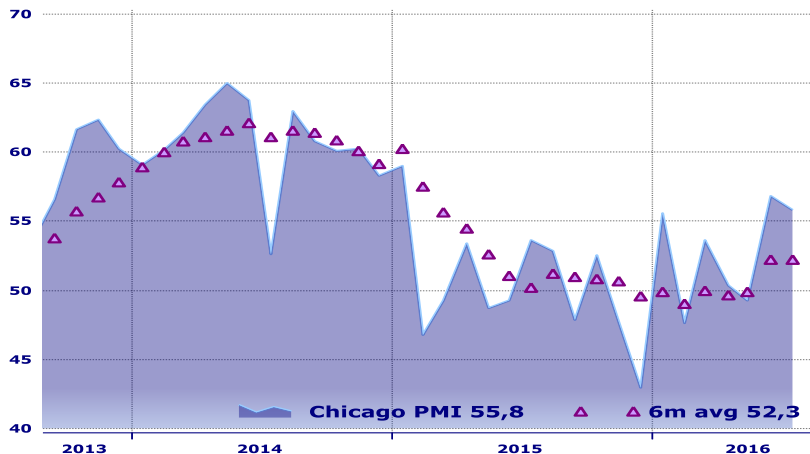


ISM DELIVERY TIME

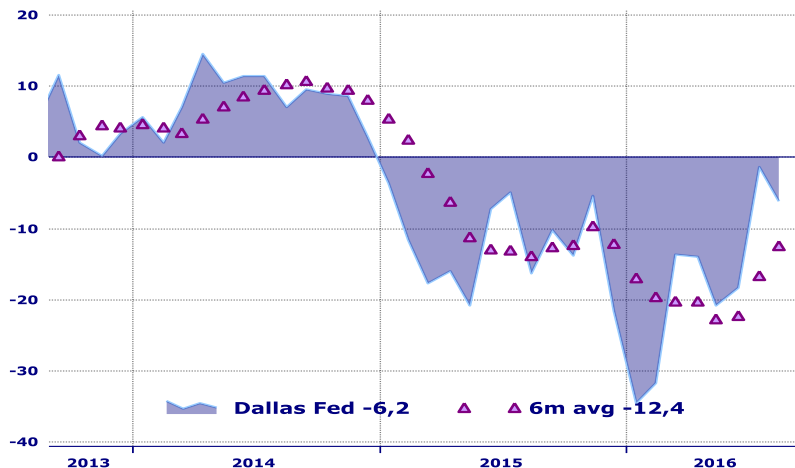


The scenario of local surveys is varied and complex, but overall characterised by a recovery since the levels of the beginning of 2016...

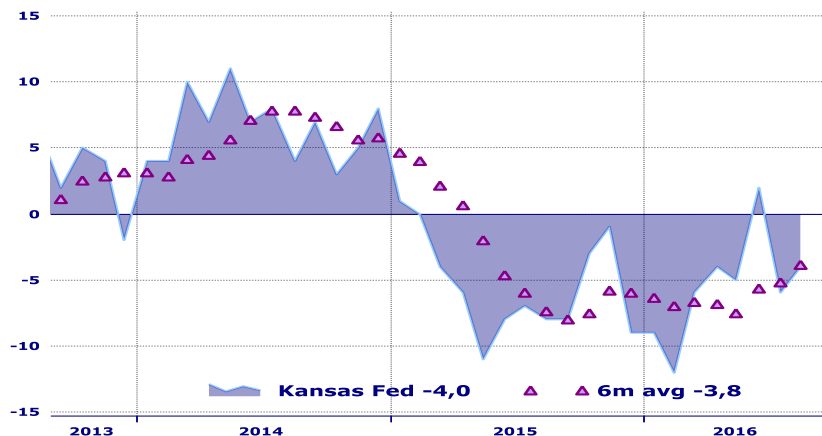
CHICAGO PMI



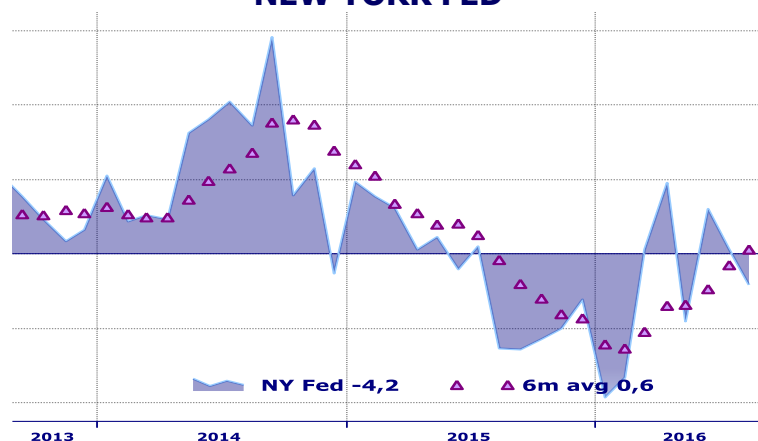
DALLAS FED



KANSAS FED

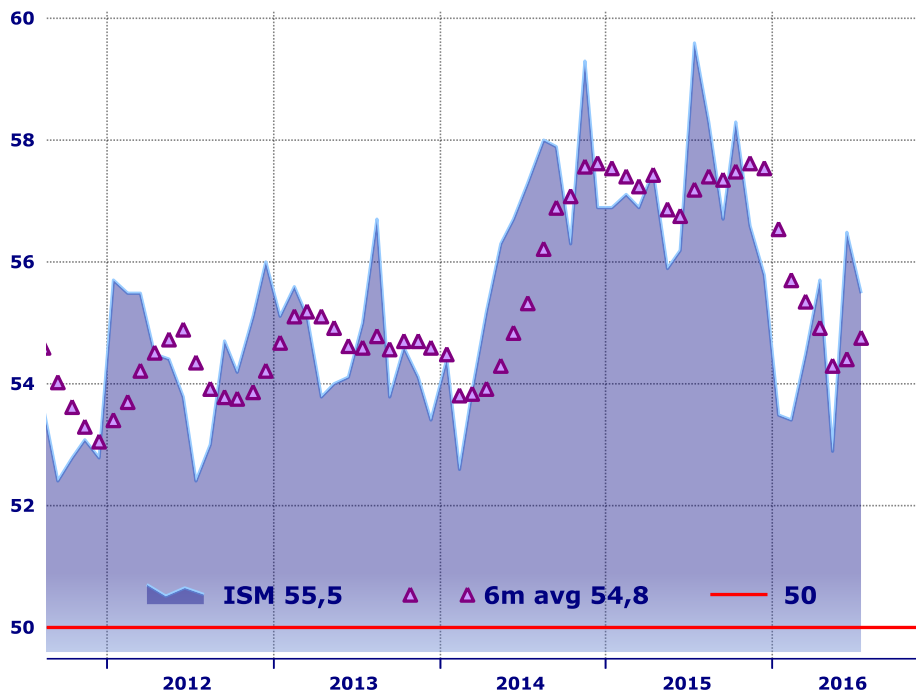


NEW YORK FED

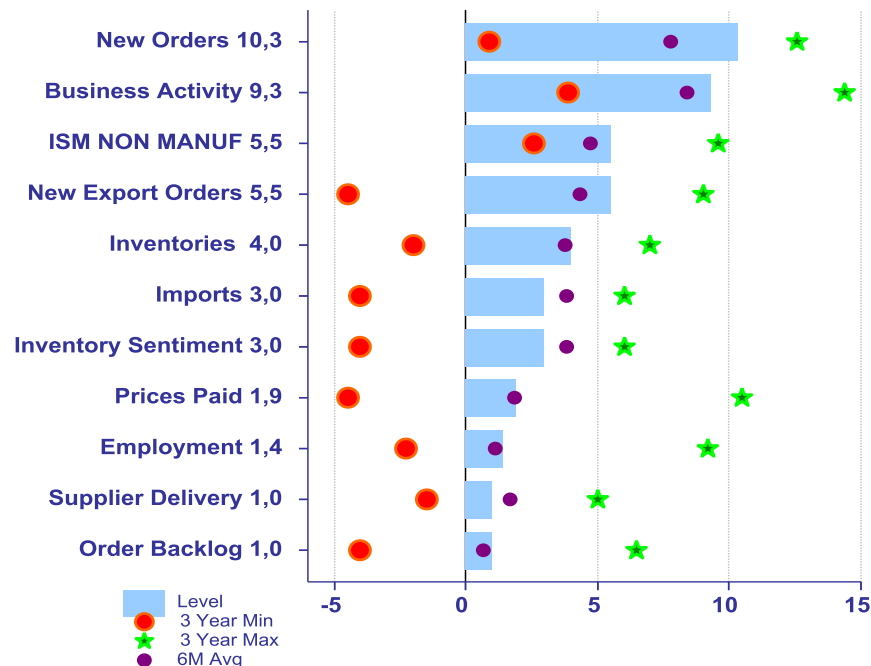


The non manufacturing ISM index – that covers services and building sectors - projects a fast pace in the economic activity in the second half of the year, despite the nominal correction registered in July. The general index is at 55.5 from 56.5 in June, which was the peak since November 2015, but the survey's details are comforting...

ISM NON MANUFACTURING



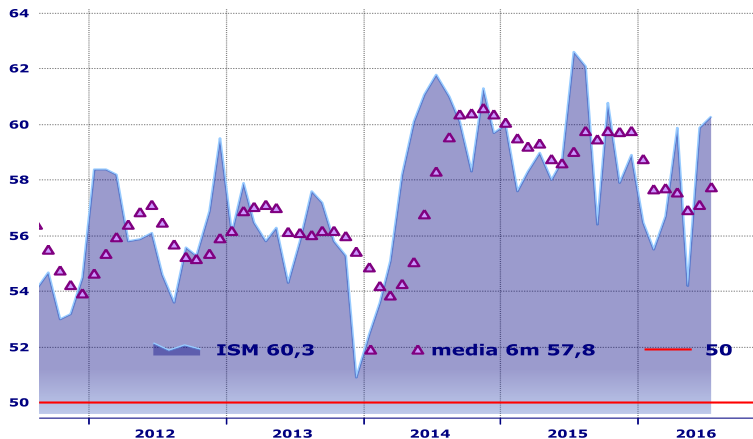
ISM NON MANUFACTURING: DETAIL



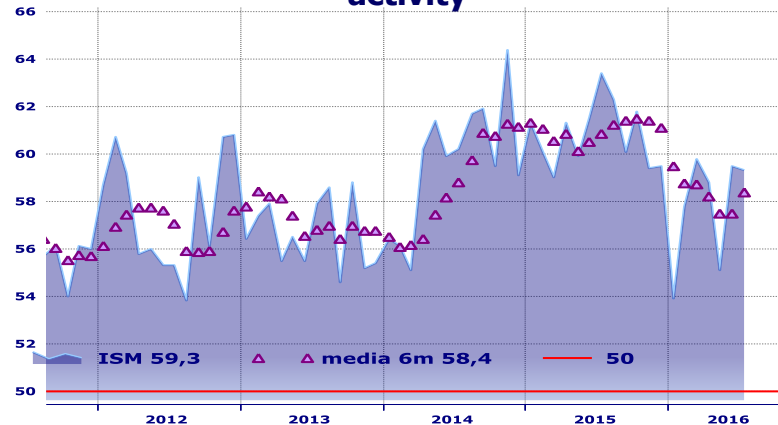
SERVICES' CONFIDENCE

New orders index reached 60.3, the year's high, while on current economic activity it has remained stable though high (59.3). As in manufacturing, the general index adjustment reflects a normalisation of delivery time. Data is compatible with a cyclical acceleration in the second semester, after the disappointing first half results.

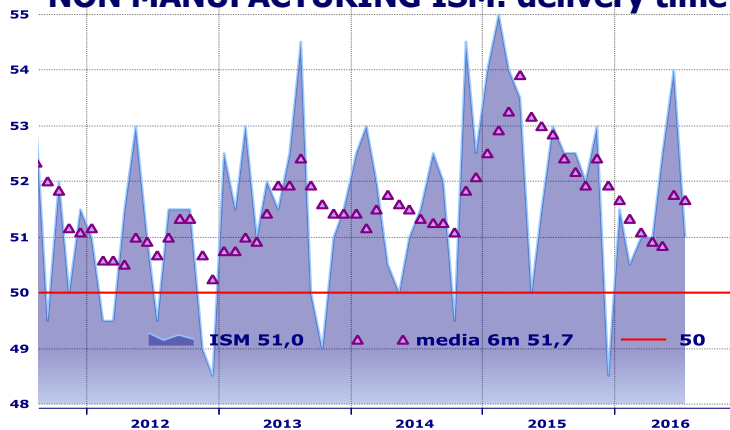
NON MANUFACTURING ISM: new orders



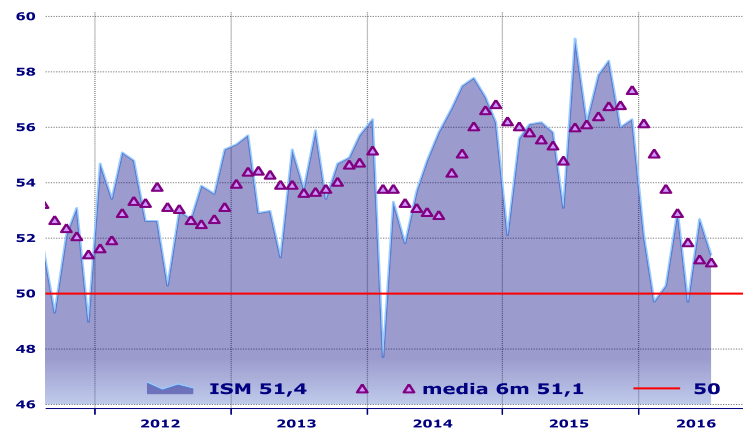
NON MANUFACTURING ISM: economic activity



NON MANUFACTURING ISM: delivery time

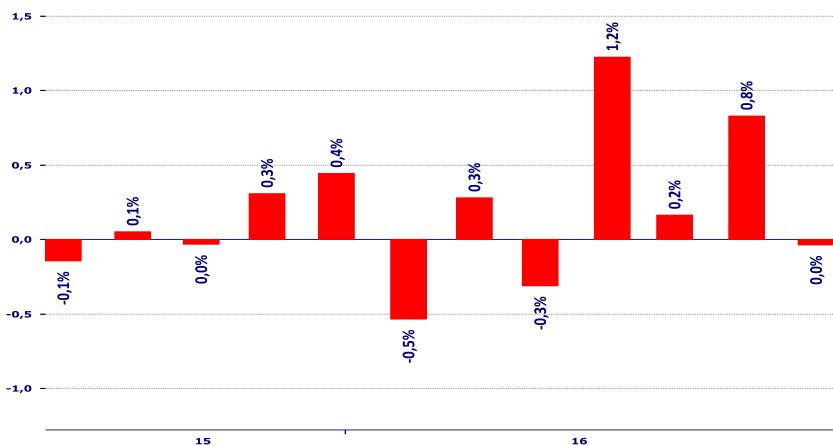


NON MANUFACTURING ISM: employment

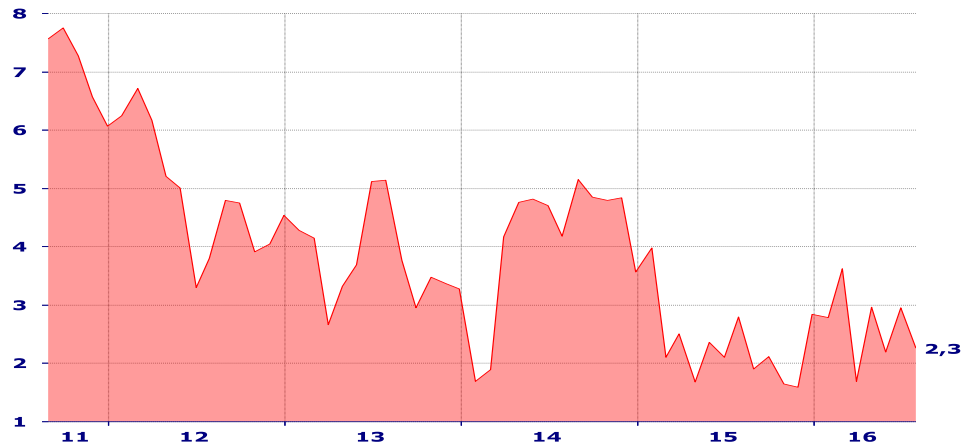


The third quarter started with a sharp slowdown in retail sales, that have not met expectations. However, this drop in trend dynamics still leaves growth rates decidedly robust, persistently compatible with the high level of internal demand.

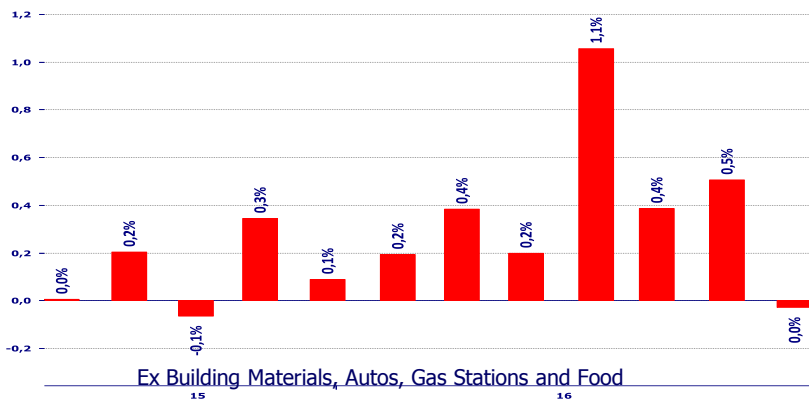
RETAIL SALES – TOTAL (MoM)



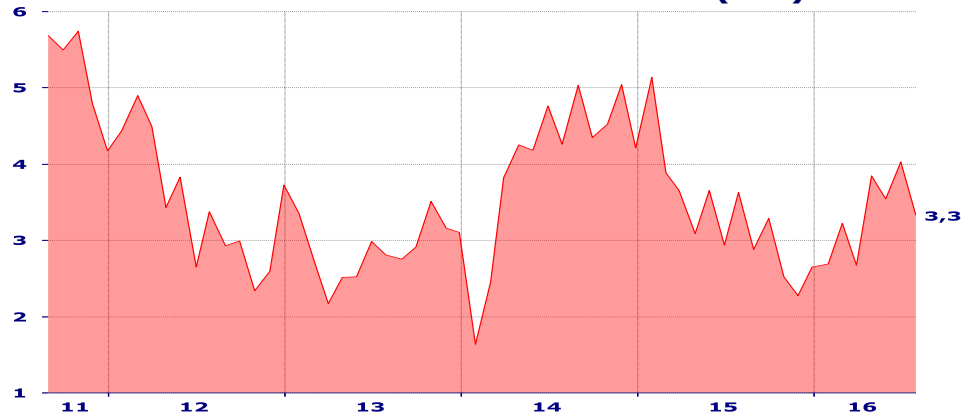
RETAIL SALES – TOTAL (YoY)



RETAIL SALES – CONTROL GROUP (MoM)

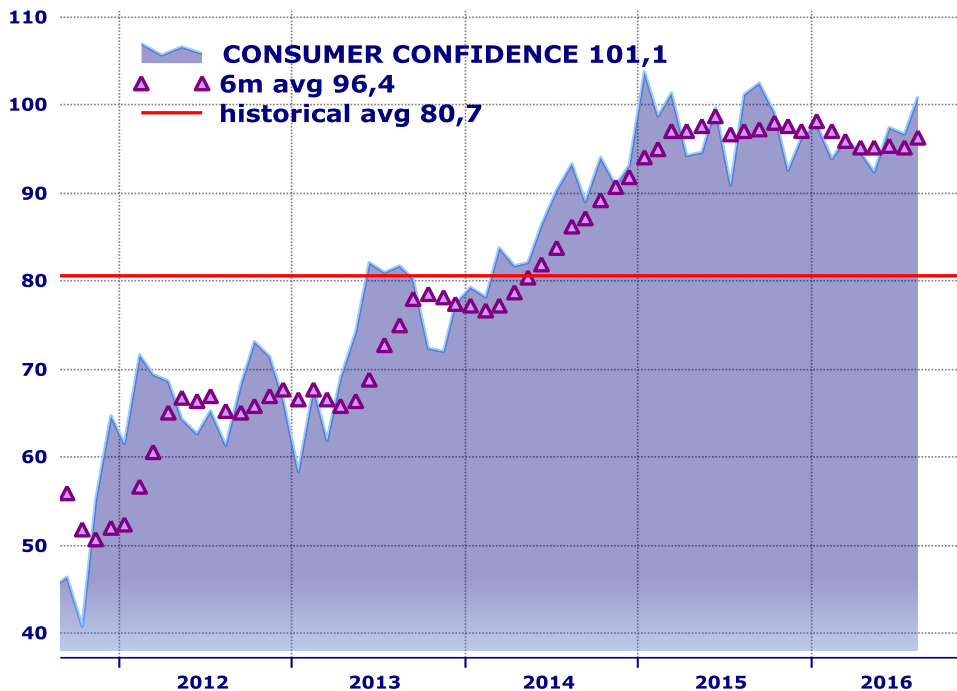


RETAIL SALES – CONTROL GROUP (YoY)



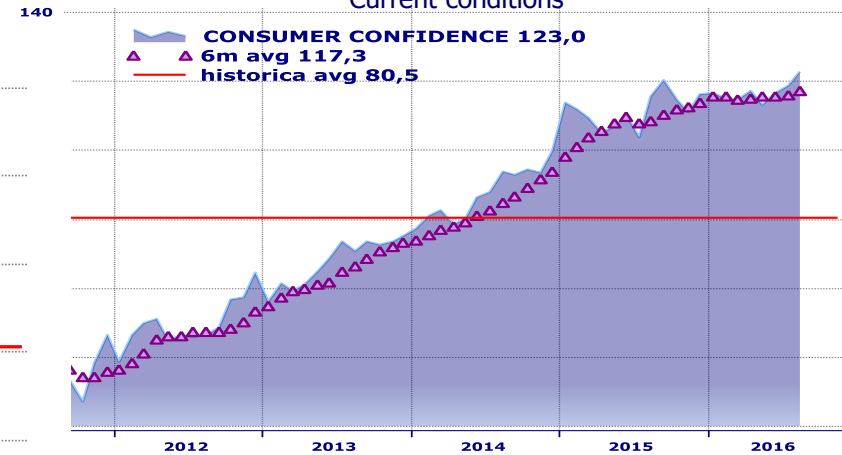
Confidence indexes' trajectory remains comforting, with the Conference Board index decidedly growing in August around 2015's highs. The improvement in data on the industrial front is coupled with summer months' inertia in private consumption, without a strong acceleration in households' spending that would guarantee growth in the second semester.

CONFERENCE BOARD
General index



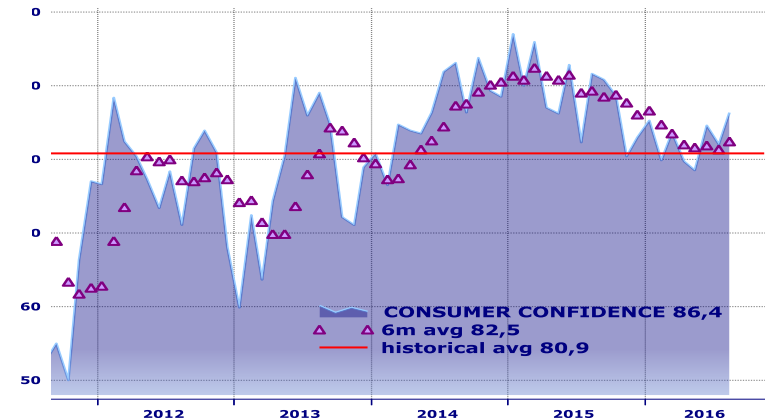
MICHIGAN UNIVERSITY

Current conditions



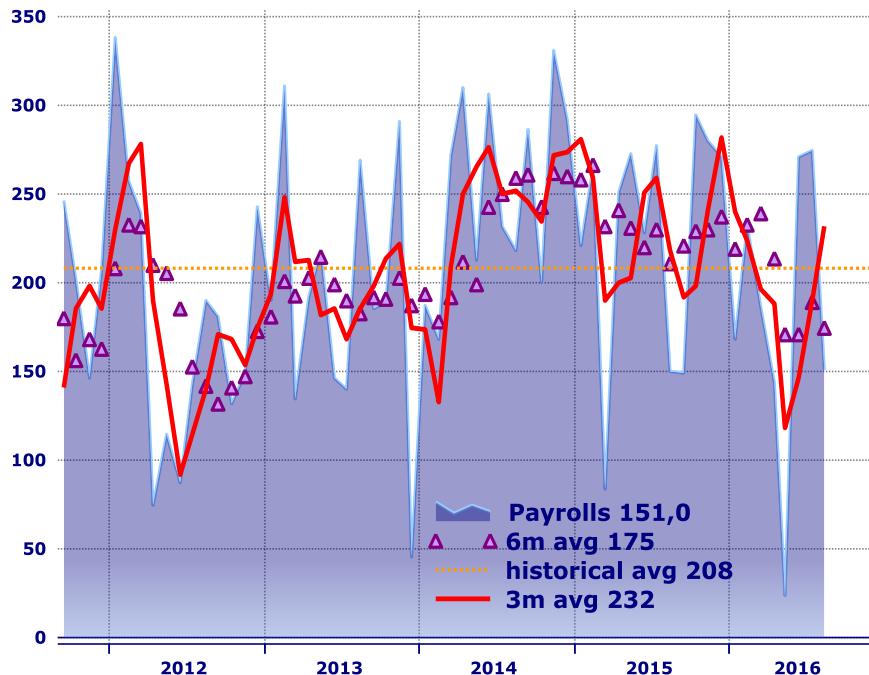
MICHIGAN UNIVERSITY

Consensus

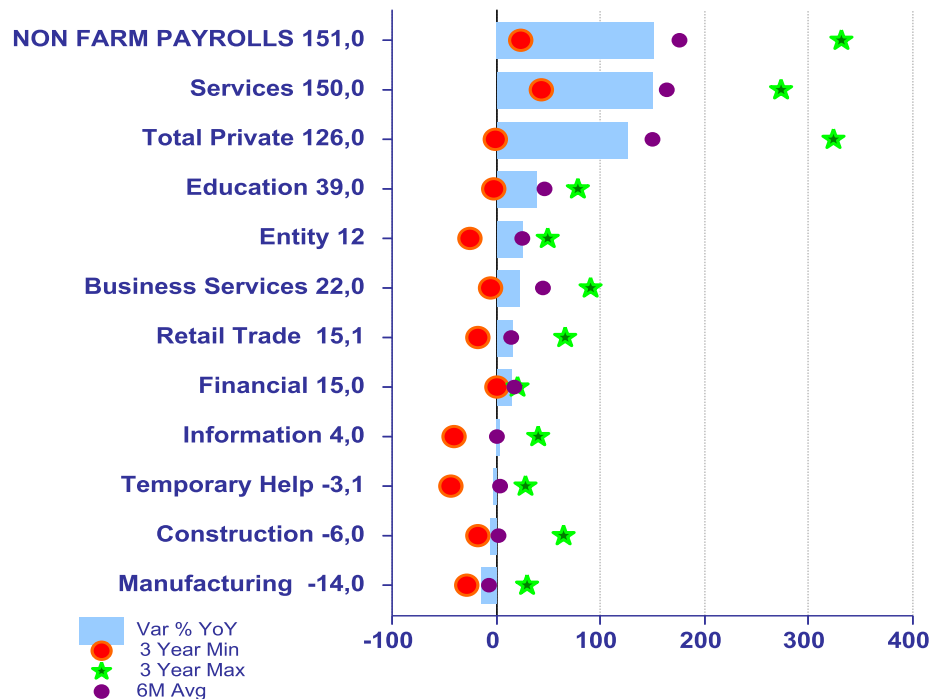


The August report on the US job market has shown lower than expected results. The figures don't suggest a worsening of occupation, however they generate doubts on the real acceleration of the economy. New payrolls are at 151 K units, 29 K below expected. Manufacturing, instead, has lost 14 K jobs compared to the previous month, 10 K more than consensus. Also the building sector registered a decline in jobs. Although lower than expected, statistics confirm the persistence of robust labour conditions.

PAYROLLS: TOTAL



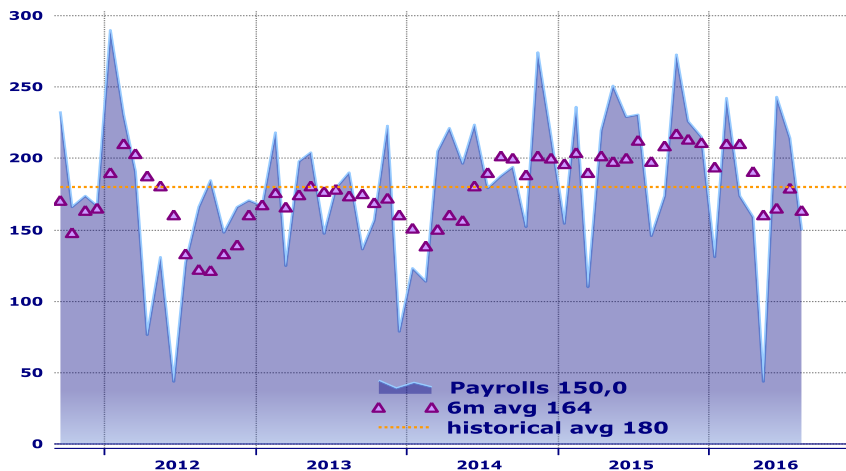
PAYROLLS: BY SECTOR



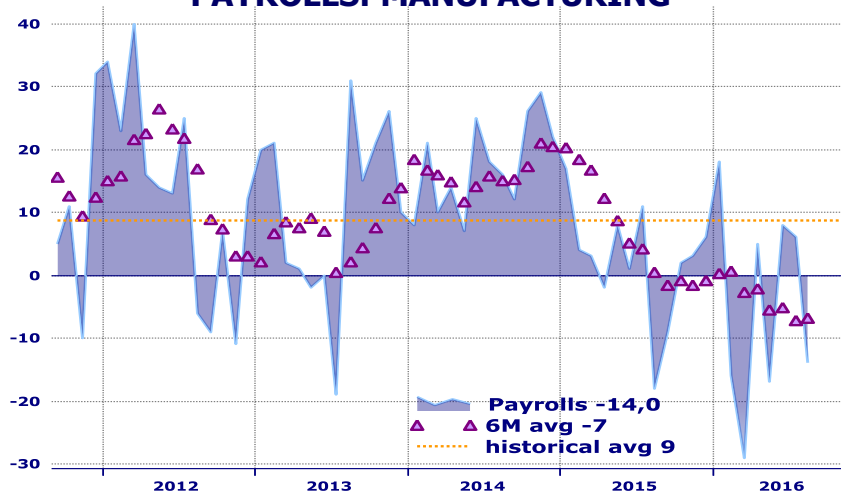
LABOUR MARKET

Also services' compartment has slowed down, at 150 K units, 60 K less than the previous month.

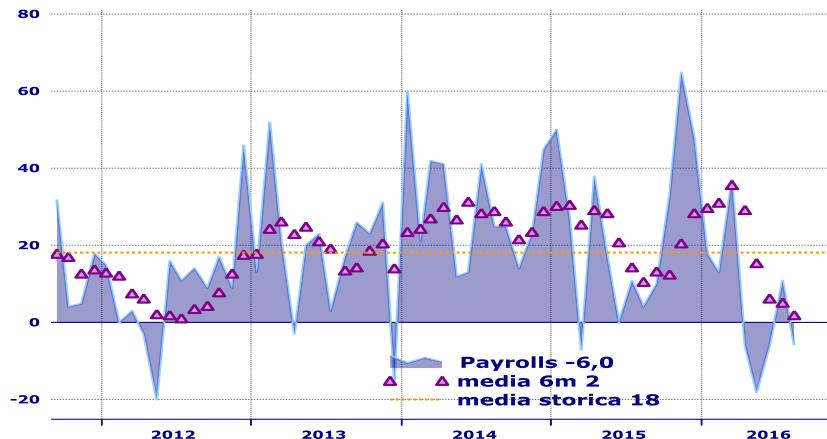
PAYROLLS: SERVICES



PAYROLLS: MANUFACTURING

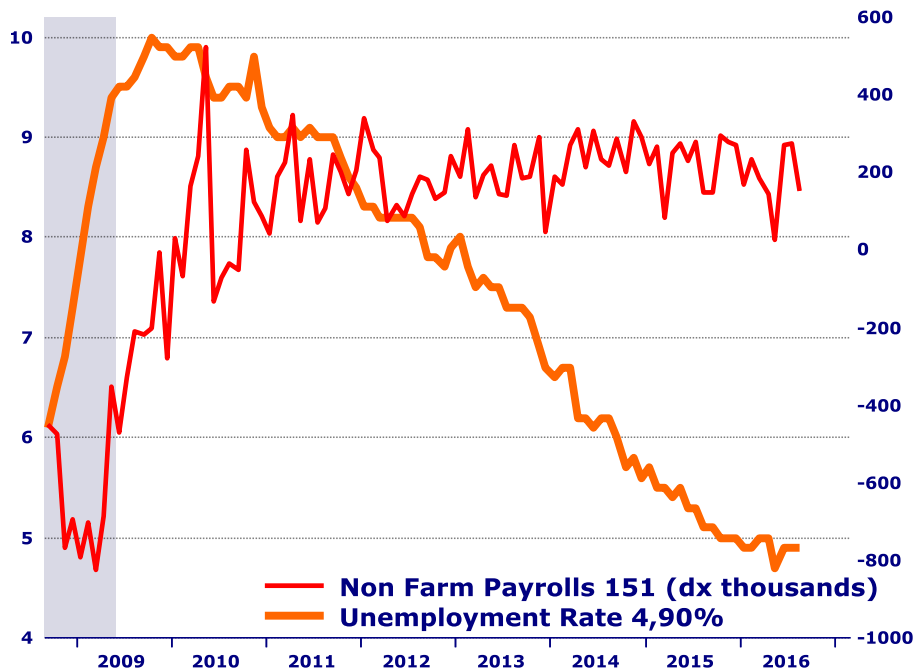


PAYROLLS: BUILDING

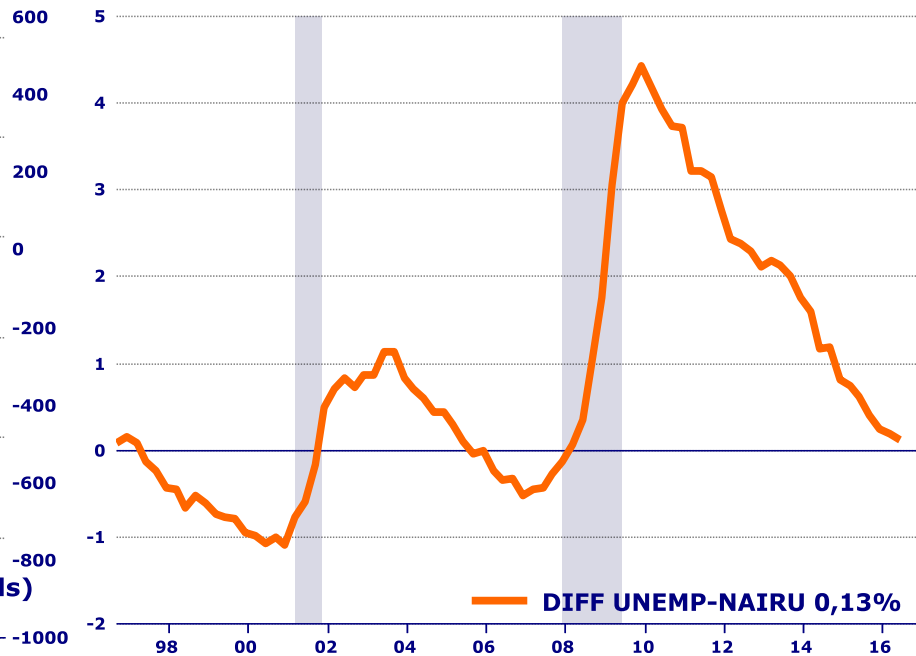


Unemployment rate is stable at 4.9% and so is participation rate (at 62.8%). The labour market is close to long term equilibrium.

UNEMPLOYMENT AND PAYROLLS



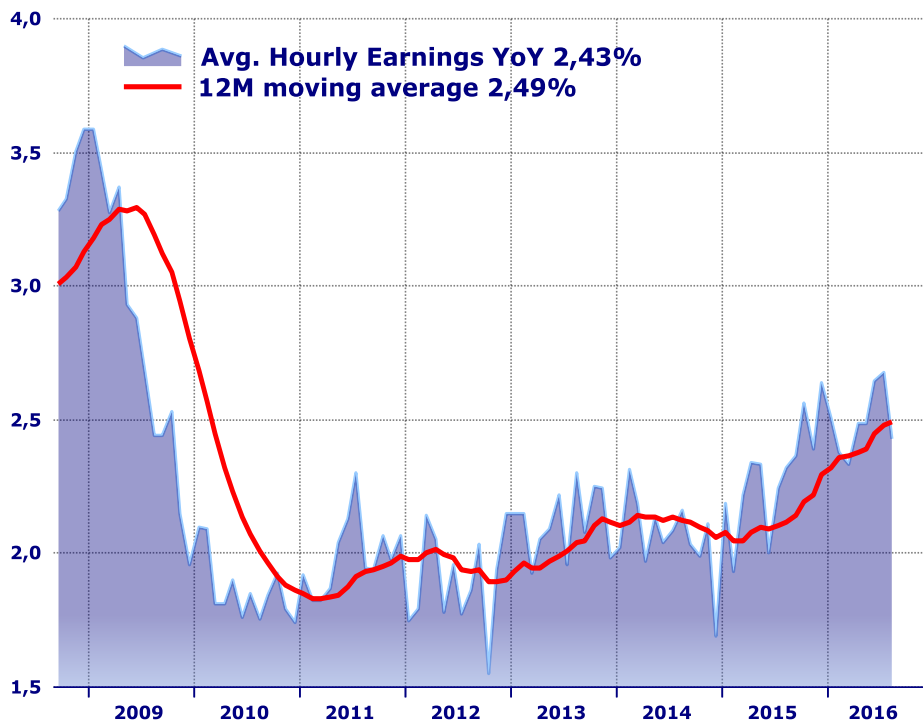
UNEMPLOYMENT AND EQUILIBRIUM



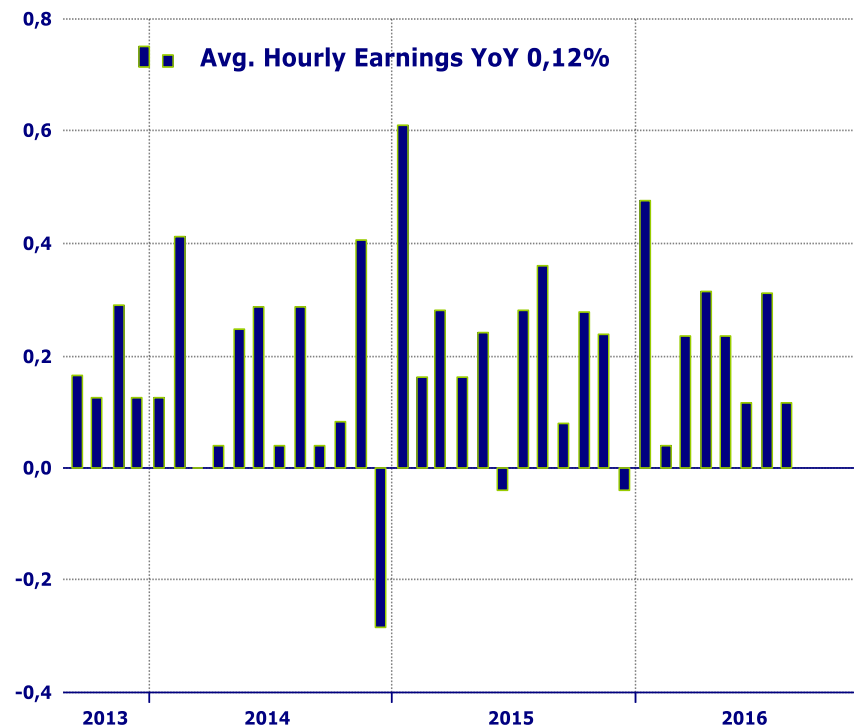
COST OF LABOUR

Statistics have a modest profile also on wages, with an increase in hourly wages limited at 0.1% on a monthly basis (consensus at 0.2%) and, in annual terms, decreasing at 2.4% from 2.7%.

AVERAGE HOURLY WAGES

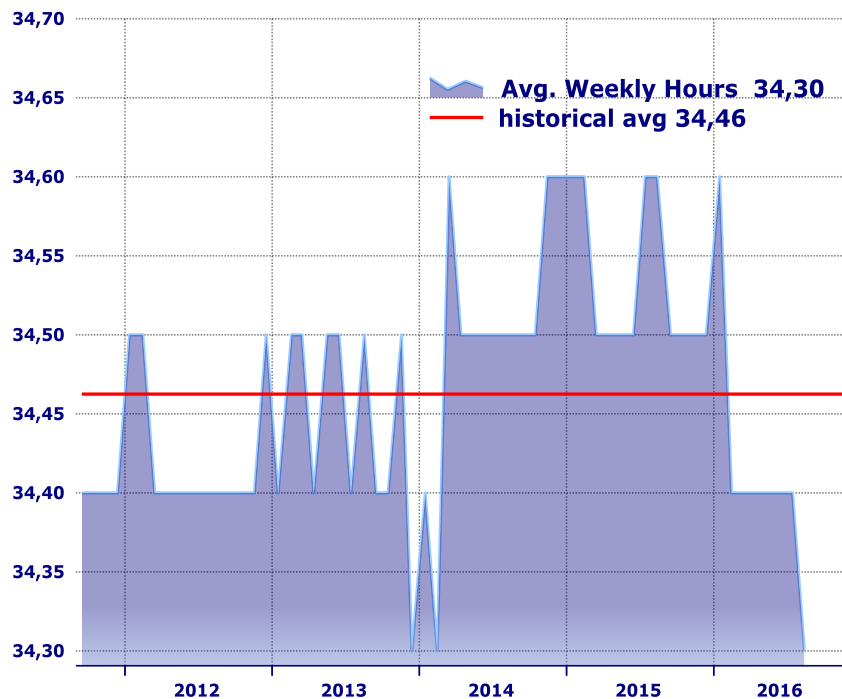


COST OF LABOUR: SHORT TERM

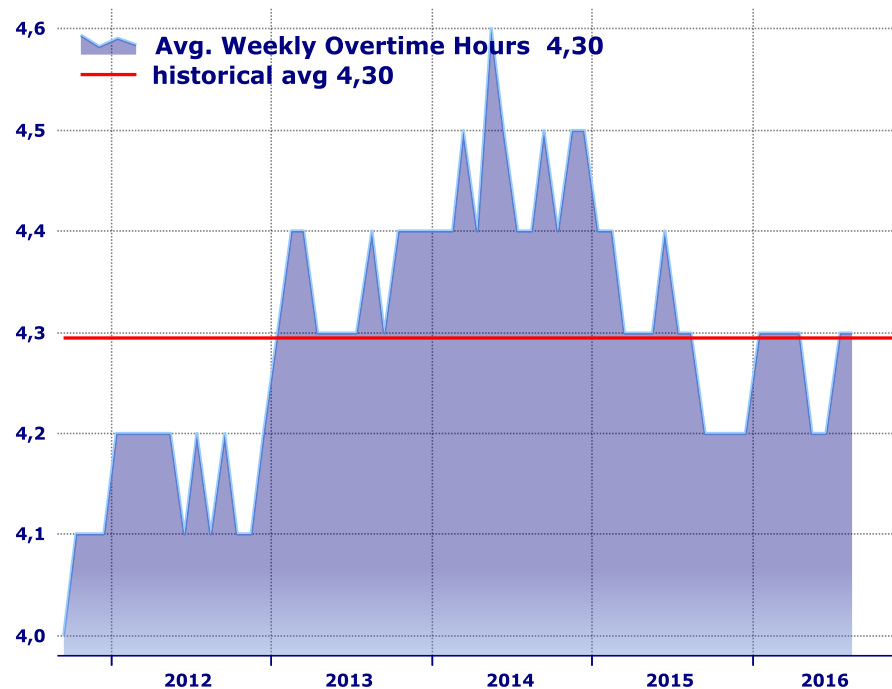


In terms of average weekly hours and overtime, we are at 2014 lows.

AVERAGE WEEKLY HOURS



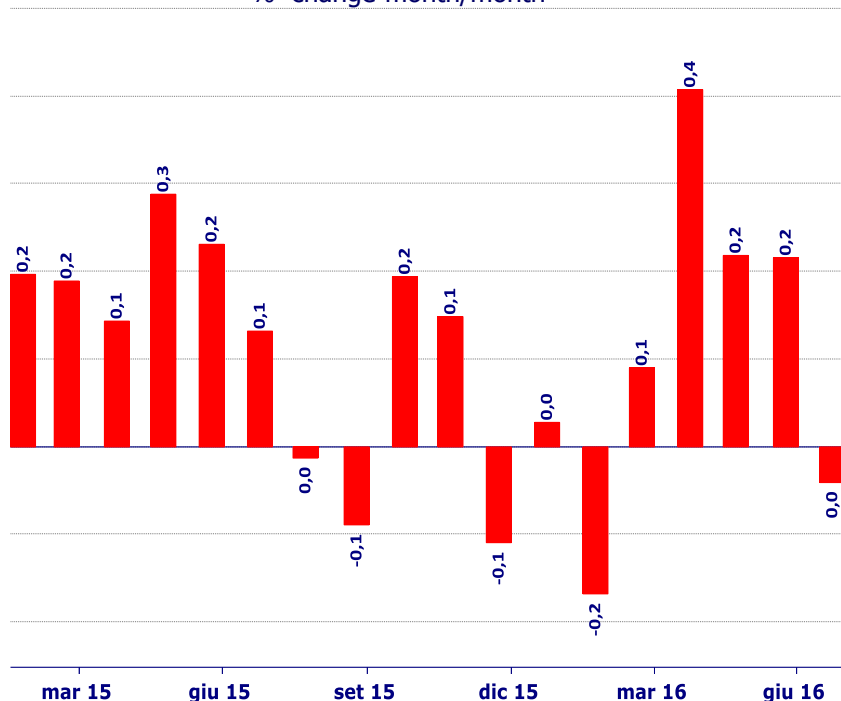
AV. WEEKLY OVERTIME HOURS



In July a modest weakening of inflationary pressure was registered. Analysing annualised quarters, the consumer price index has remained the same, after four increases in a row, held back by lower energy prices.

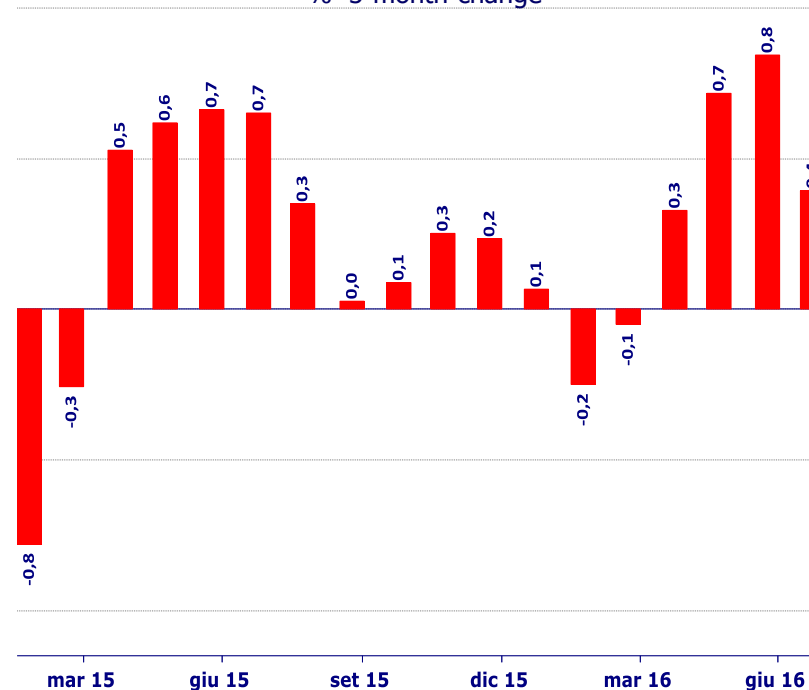
GENERAL INFLATION INDEX

% change month/month



GENERAL INFLATION INDEX

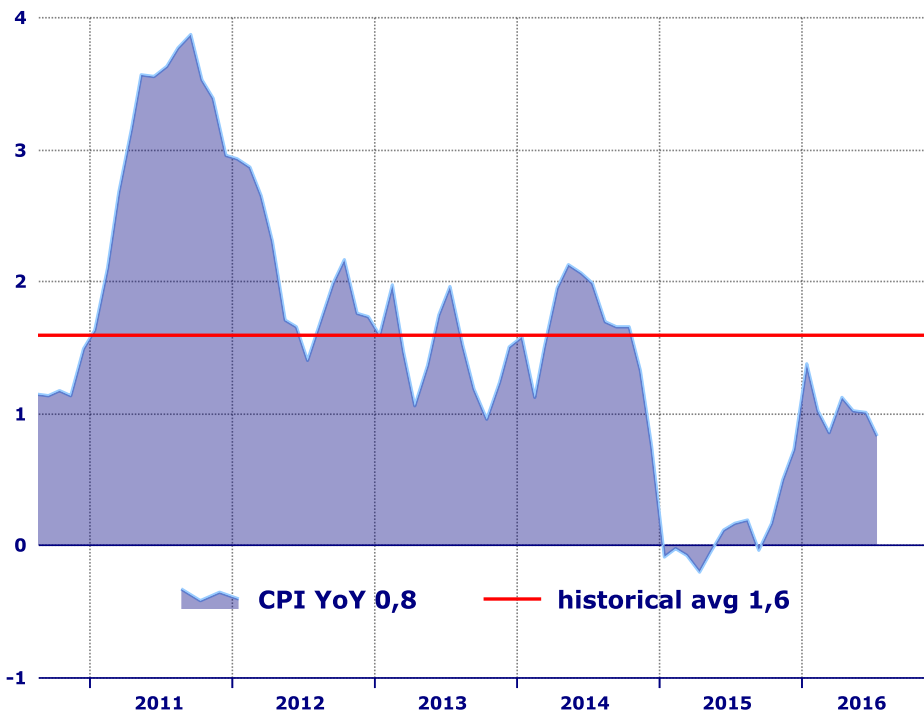
% 3-month change



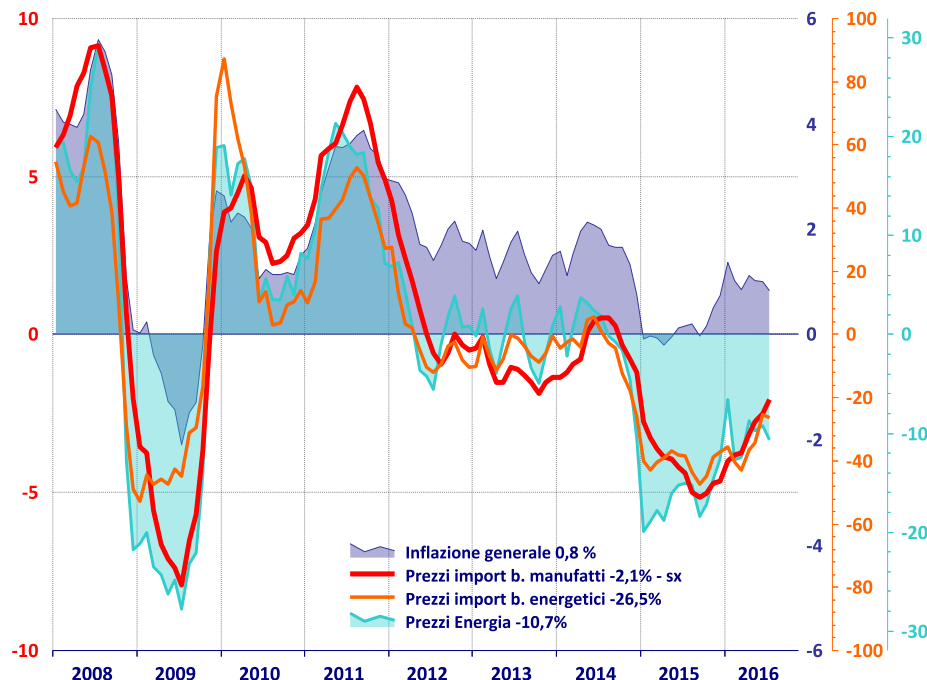
On a quarterly basis, the general inflation rate has had a stronger than expected slowdown, at +0.8% YoY from +1.0%, lowest since December 2015.

GENERAL INFLATION INDEX

change



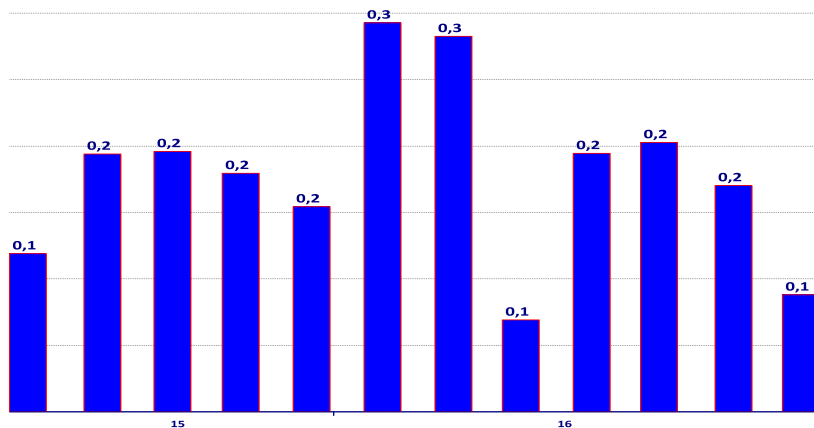
INFLATION AND IMPORT PRICES



Core inflation has seen a marginal adjustment (2.2% from 2.3%), confirming its robustness, over 2% for nine months in a row.

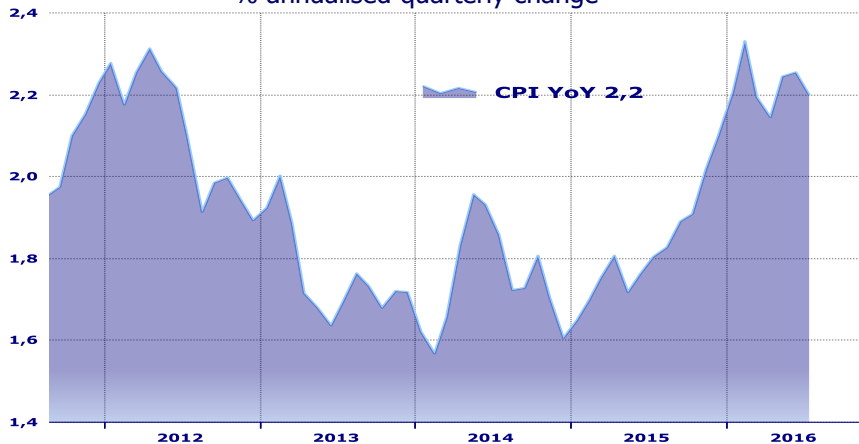
CORE INFLATION

% change month/month



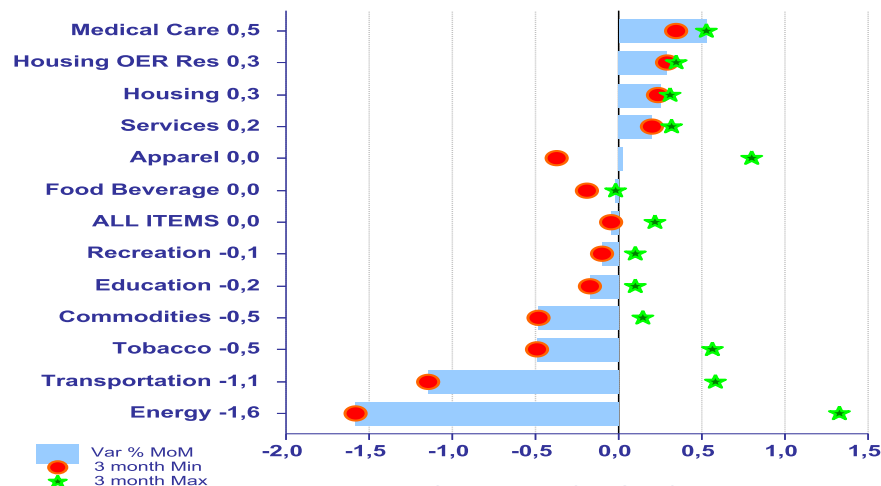
CORE INFLATION INDEX

% annualised quarterly change



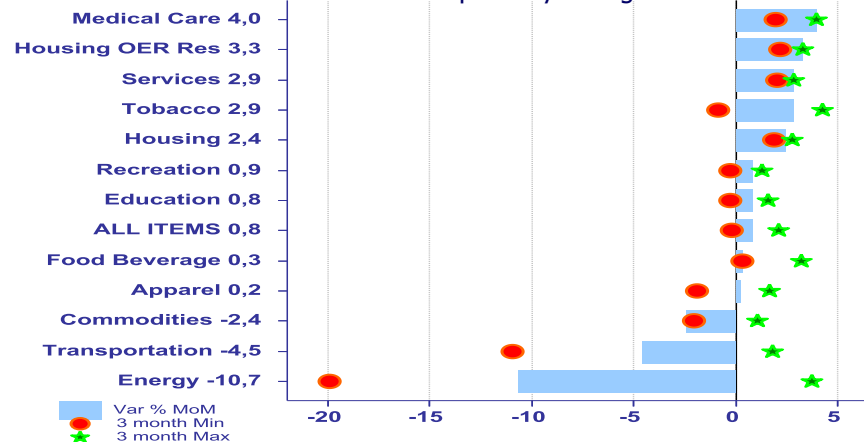
INFLATION BY SECTOR

% change month/month



INFLATION BY SECTOR

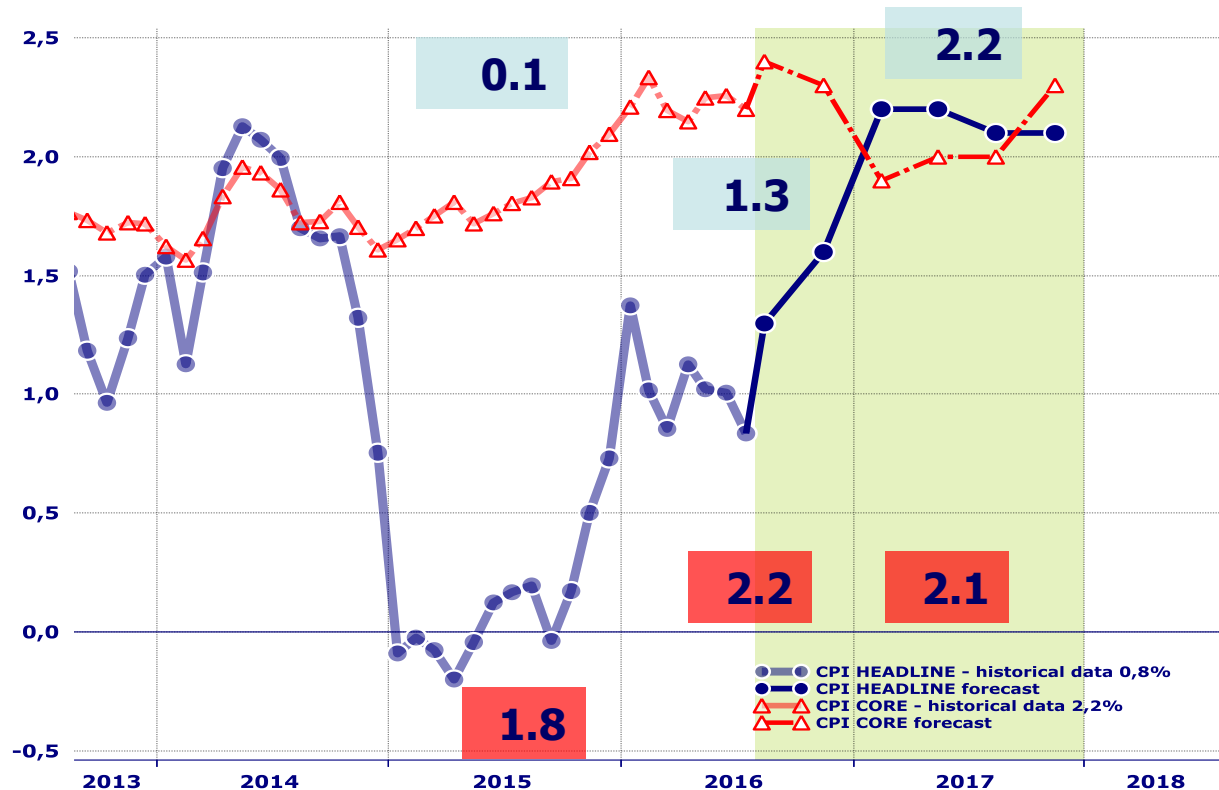
% annualised quarterly change



GENERAL INFLATION: gradual increase toward 2% (end of 2016 forecast: 1.9%); then stabilisation above 2%.

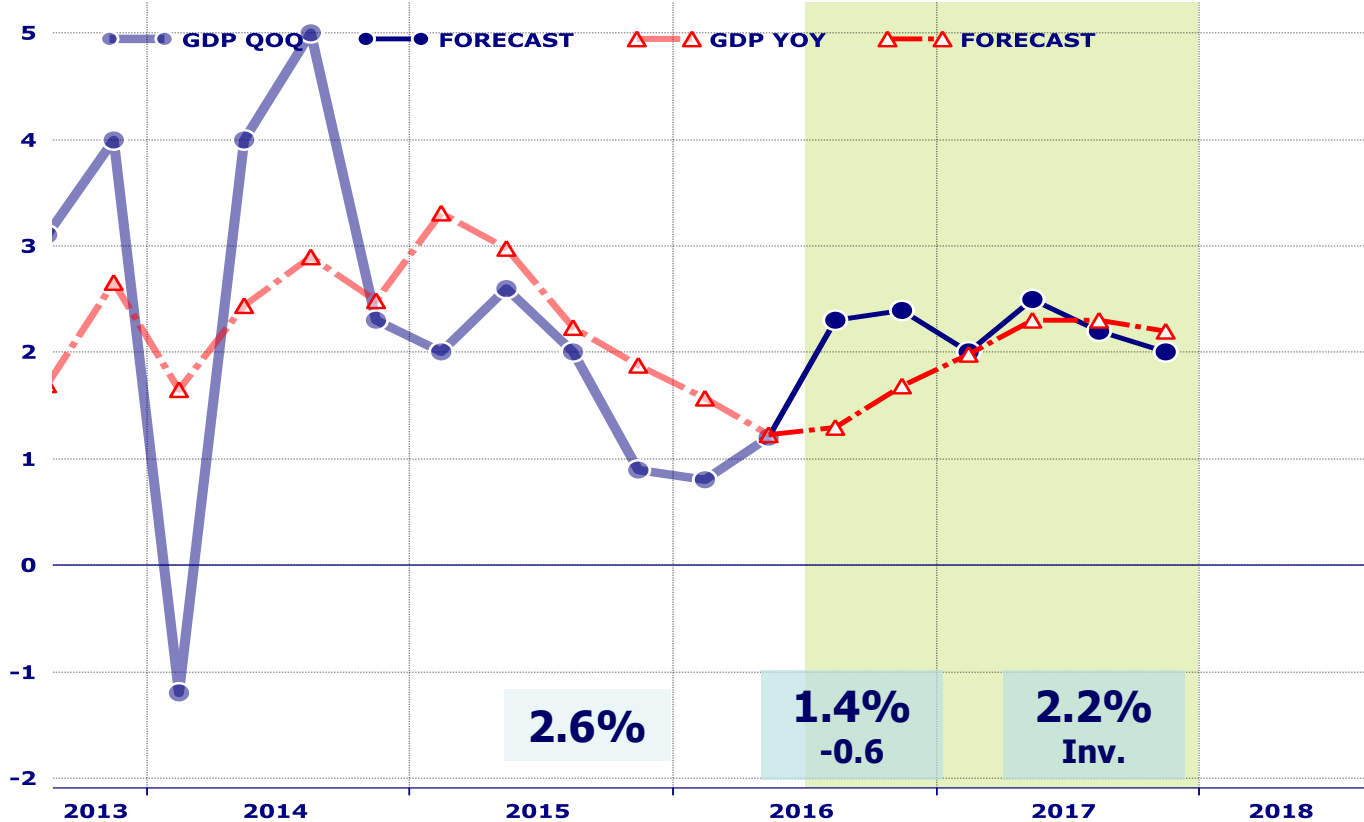
CORE INFLATION: fluctuations around 2%

INFLATION: NEW FORECASTS



Constant growth above 2% in the next quarters...

USA GDP – GROWTH FORECASTS



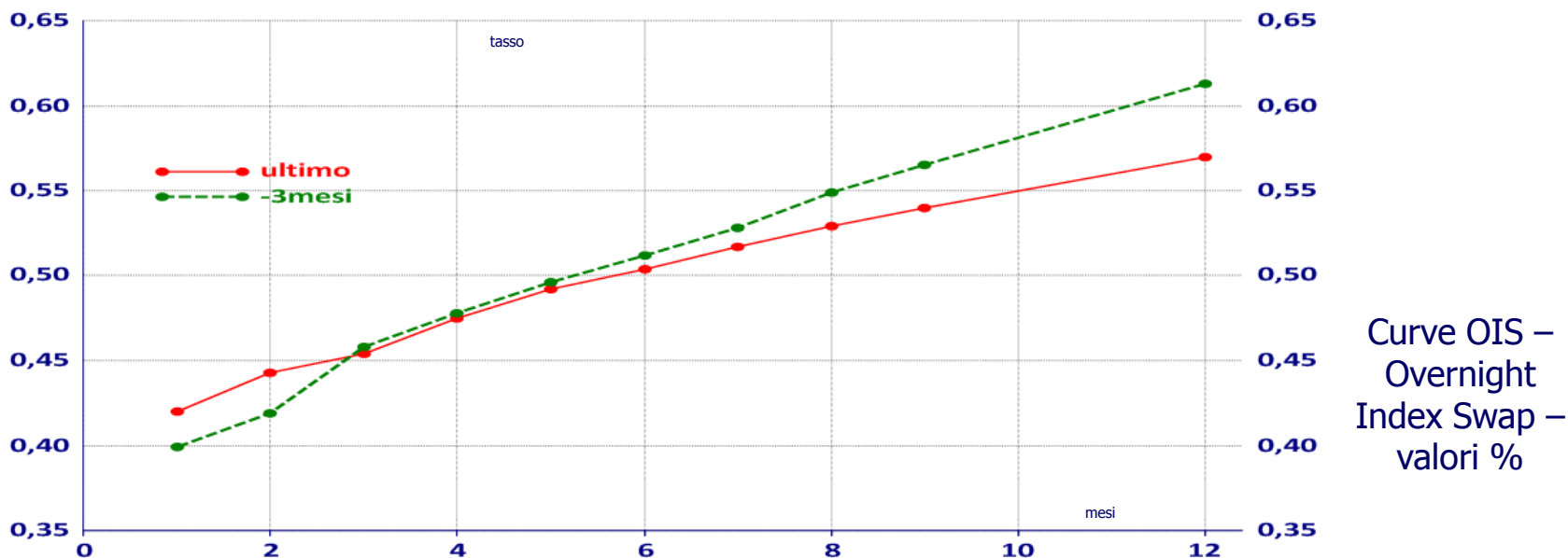
For the whole summer, the central bank's official statements have been extremely prudent signalling endogenous conditions that are not yet completely satisfying and many exogenous risks (emerging economies' slowdown, China, geopolitical factors, Brexit)

The discrepancies between the Committee members and the Governors continued also in August, with the usual divide between those who favour a tightening (Fischer, Dudley, Lockhart...) and those who prefer to *wait and see*, if not an increase (Williams, suggested higher inflation targets).

At the traditional annual meeting at Jackson Hole, at the end of August, the Fed's Governor repeated the positive tones talking of the economy's evolution, as already stated by several of the central bank's members, thus confirming the intention to increase the official rate. Yellen, however, didn't give an explicit time frame for these measures.

The mixed tone of the Fed’s statements (cautious in official talks and documents and more aggressive in single members’ informal statements) has prevented the formation of clear market expectations.

At the end of August, financial markets still assign rather low probability to a rate increase in September or November, with a higher probability for an increase in December.



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