SECURITIES

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# Economy

**Focus US**

N° 2017 – 05

# What if there is no fiscal stimulus in the US?

**Friday 03 February 2017**


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***The economic policy advocated by Donald Trump during his electoral campaign was largely inspired by the one pursued by President Ronald Reagan in the early 1980s (Reagonomics). This combines a strong fiscal stimulus, deregulation and some protectionism. In what proportions, no-one knows for the time being. Recently, Trump has made a lot of noise about protectionism but been tight-lipped about the budget and fiscal policy. Granted, the new US administration is not fully in place, but one can doubt that a large fiscal stimulus will really be launched in the near future.***

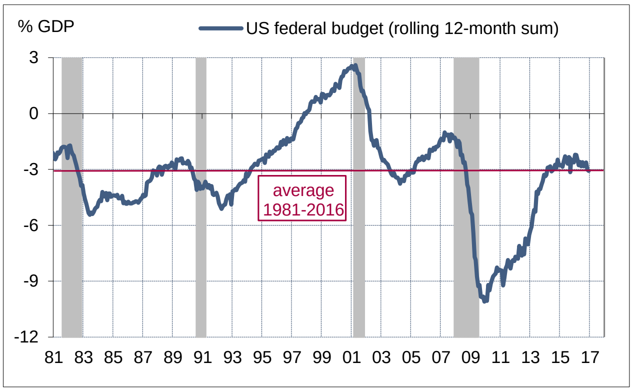

## The week's focus

While Donald Trump's election is not the sole reason for the comeback of the reflationary theme, it did encourage it. Investors appreciated his promise of a massive fiscal stimulus designed to boost economic activity and subsequently prices[1]. The stockmarket rally and the bond market correction both attest to this. But three months have passed since the election without any useful light being shed on this stimulus plan. Admittedly, the Trump administration is still being put in place and the fiscal tool takes longer to activate than the monetary tool, but this silence is striking. After all, the Republican party is not philosophically attuned to a stimulus, especially through infrastructure spending, and there is no shortage of fiscal hawks in Congress who may fear that the federal deficit is deepening at a time when the economy is approaching its cycle peak (left-hand chart). In short, if this stimulus never takes place or is postponed for a long time, how would the US economy fare?

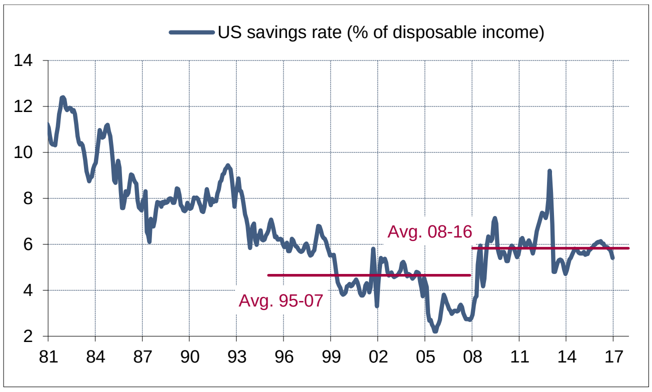
Since the US emerged from the financial crisis in 2010, GDP growth has averaged 2.1% annually. In 2016, real GDP grew by 1.6% only because of a weak first half (see page 2). Now that underemployment has been eliminated, there is no reason for the US economy to accelerate strongly, barring a stimulus by a tax cut or an increase in public spending. After all, there are several factors that could slow the pace of consumer spending (2.7% in 2016 and 2.3% annually since 2010). Real wage growth is being constrained by the rebound in inflation. What's more, while job creations remain in positive territory, the ^pace is slowing down. The savings rate is not excessively low, as was the case before the 2008 crisis, but nor does it provide protection in the event of a cold snap (right-hand chart). Without the fiscal stimulus promised by Trump, the US economy would have reasons to slow and the markets, which have rallied on *Trumpflation,* would have reasons to be disheartened.

1 See several of our notes on the subject: "Stimulus, overheating, recession?" (7 December, 2016) and "What to expect from Trump's fiscal stimulus?" (12 January, 2017)

**US: federal deficit as % of GDP**




**US: household savings rate**




*Sources: Thomson Reuters, Oddo Securities*

## Economy

- On the initial estimate, real GDP grew by an annualised 1.9% q/q in **Q4 2016**. The principal source of growth remained consumer spending, up an annualised 2.5%, to which was added a strong recovery in residential investment (+10.2%, after -4.1% in Q3 and -7.7% in Q2). Capital expenditure by businesses staged a modest acceleration. As so often, the contributions to growth from inventories (+1pts) and from external trade (-1.7pts) moved in opposite directions. Imports were dynamic to satisfy internal demand, but exports suffered as expected from the repercussions of record soya exports over the summer.
- The report on household income and spending confirmed the erosion of the savings rate, already visible for several months. In **December**, it stood at 5.4% of disposable income vs. 6.1% a year earlier. It is possible that the rebound in inflation in recent months has led Americans to dip into their savings to maintain a robust level of spending.
- The Fed's preferred inflation measure (PCE index) accelerated by 0.2% point to 1.6% year-over-year, its highest level since July 2014. Core PCE inflation was stable at 1.7% y-o-y. The employment cost index was a little disappointing, growing by 0.5% q/q in **Q4** after 0.6% in Q3 and Q2. The positive trend is still in place but acceleration is very gradual.
- Consumer confidence shows no signs of flagging. The *Conference Board* index stood at 111.8pts in **January** (vs. 113.7 in December but an average of 99.8 in 2016). Note that while the present conditions component continues to improve, expectations are weakening. The same is true for vehicle sales, down 4.4% in **January** from a record level of over 18m units.
- The manufacturing sector continues to pick up. In **January**, the ISM index gained another 1.5pts to 56.0. All its components are improving: new orders to 60.4 (+0.1), production to 61.4 (+2.0), employment to 56.1 (+3.3) and prices to 69.0 (+3.5). Durable goods orders in **December** attested to this recovery. While the total figure was down 0.4%, the core index – which removes a few volatile components, such as aircrafts – put on 0.8% over the month and 2.8% over the year, the biggest increase since 2014.
- Construction spending weakened by 0.2% in **December,** but the underlying trend remains solid. Spending grew by an annualised 5.7% q/q in **Q4,** with growth of 3.2% in private spending and 13.7% in public spending.

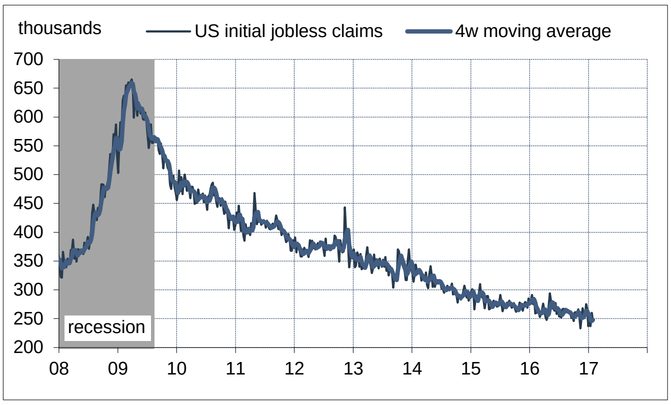
## Monetary and fiscal policy

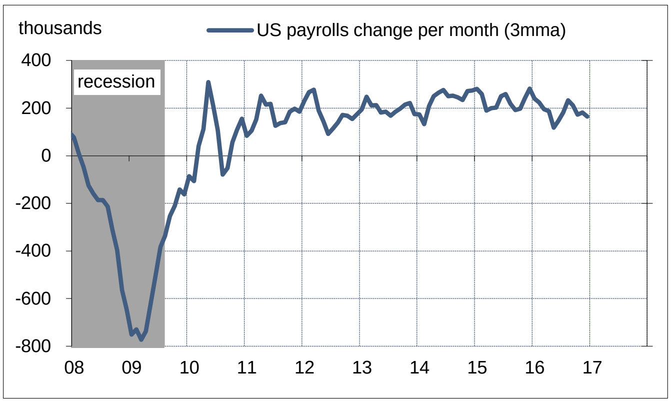
- Unsurprisingly, the FOMC voted unanimously to leave monetary policy on hold after its **1 February** meeting. The press release contained no suggestion that the Fed is in a hurry to implement another rate hike. The futures market prices in a 32% chance of a hike at the meeting on 15 March, a 50% chance by the meeting on 3 May and a 70% chance by the meeting on 14 June.
- After Mexico, China and Japan, Germany has been the target of attacks by the Trump administration through the voice of Peter Navarro, co-author of Trump's economic platform and director of the *White House National Trade Council*. It stands accused of manipulating the euro to its advantage to obtain large trade surpluses, including a surplus of over $ 60bn with the US (see our *Economic Note* of 1 February: "Germany: currency manipulator!). Mr. Navarro reiterated his usual criticisms of multilateral trade agreements and called for an end to global value chains. There is no doubt that the US would have a certain advantage in bilateral negotiations because of its size.

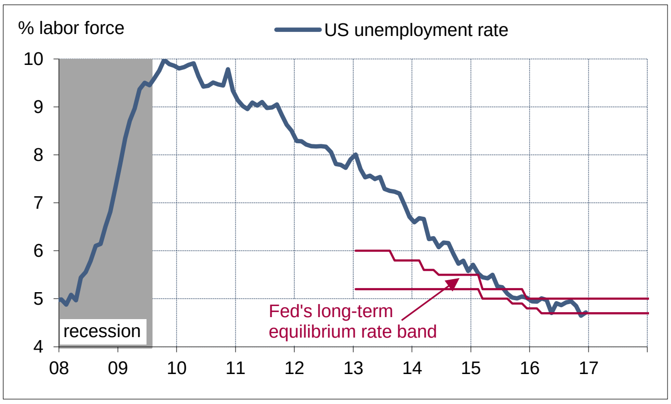
## The week ahead

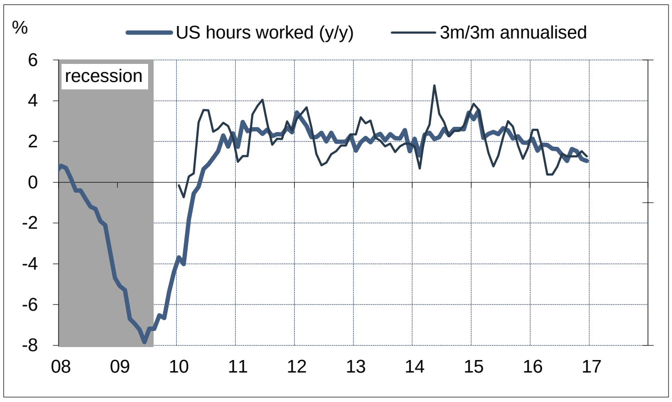
- The statistical agenda is almost empty. Interest will mainly focus on the Fed's quarterly survey of credit standards (SLOOS) published on **6 February**.

## Appendix 1 - Labour market

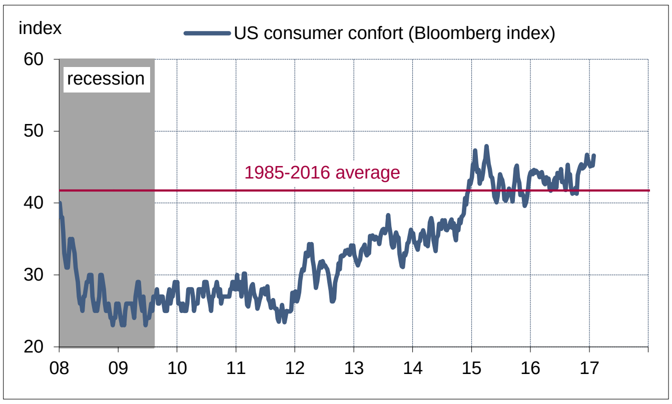


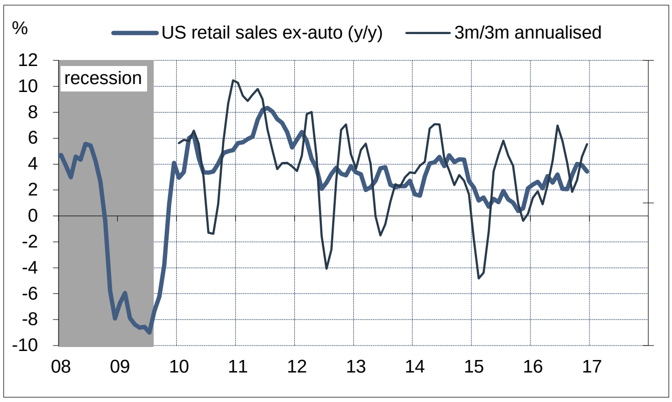



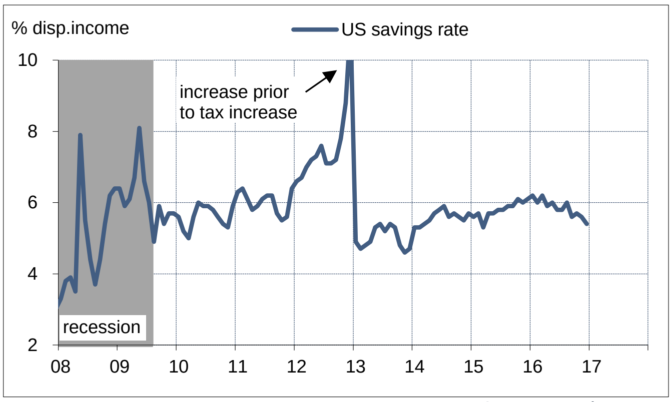



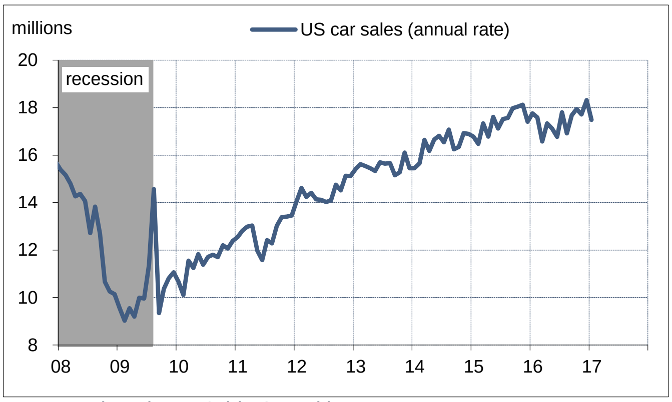




## Appendix 2 - Consumer



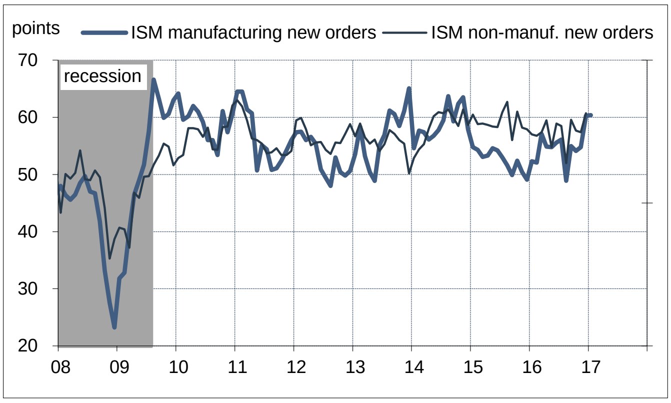



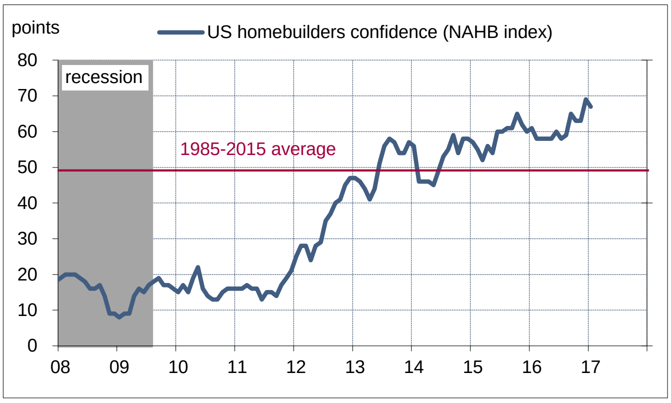



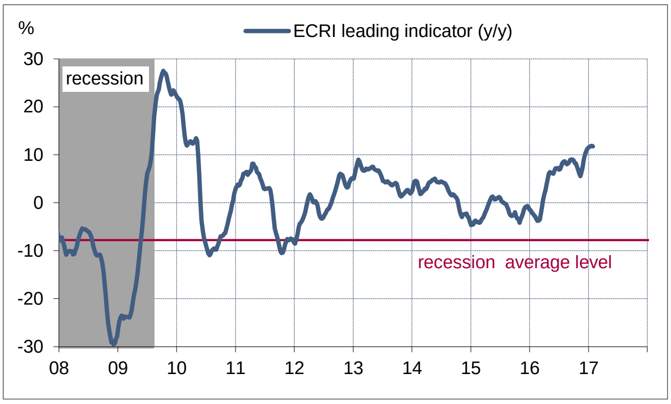




*Sources : Thomson Reuters, Bloomberg, Oddo Securities*

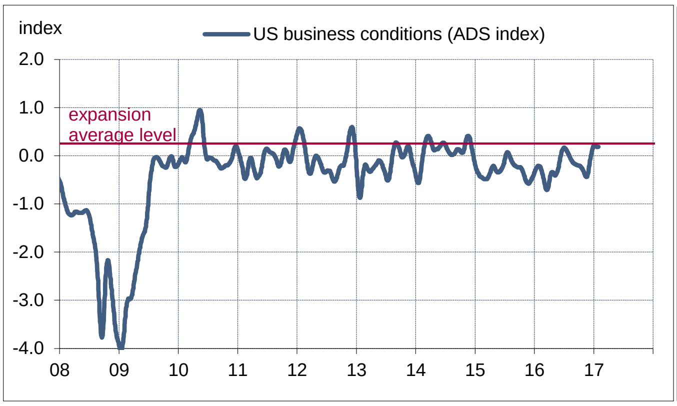
## Appendix 3 - Business climate

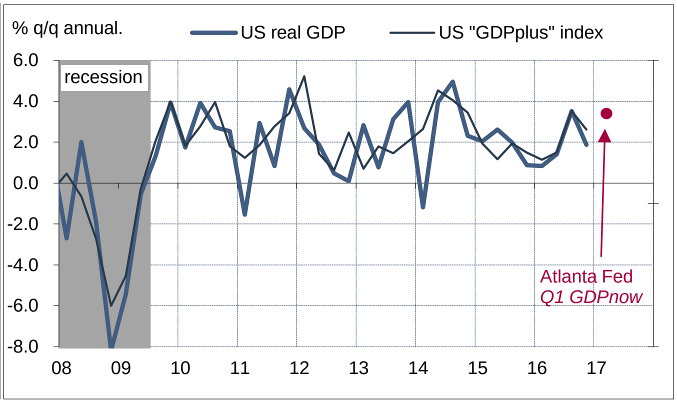



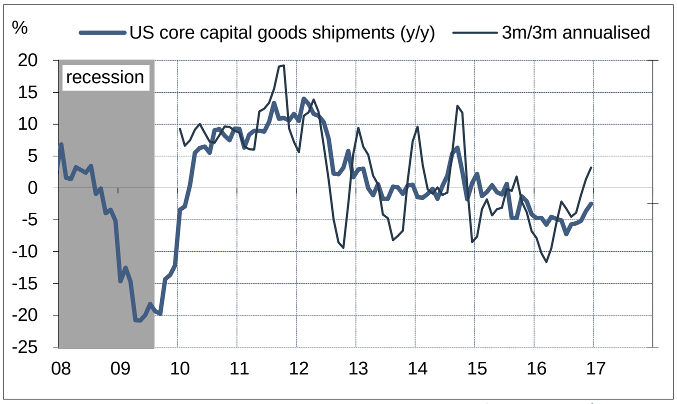



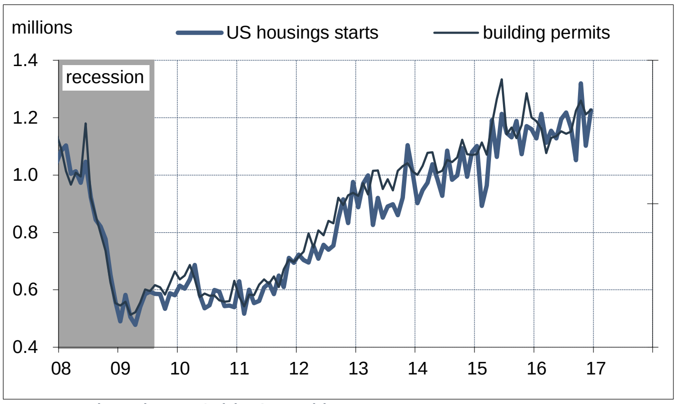




## Appendix 4 - Conditions of economic activity



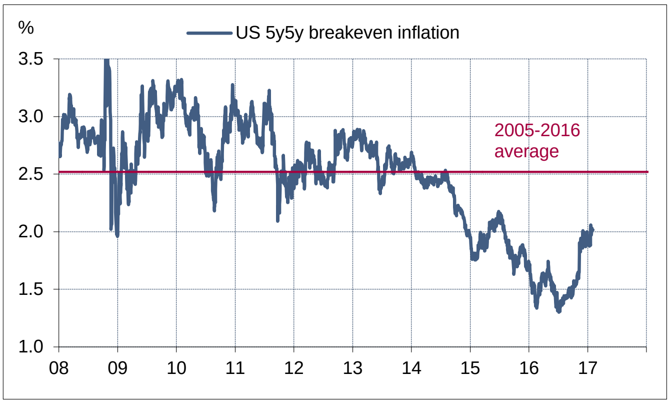



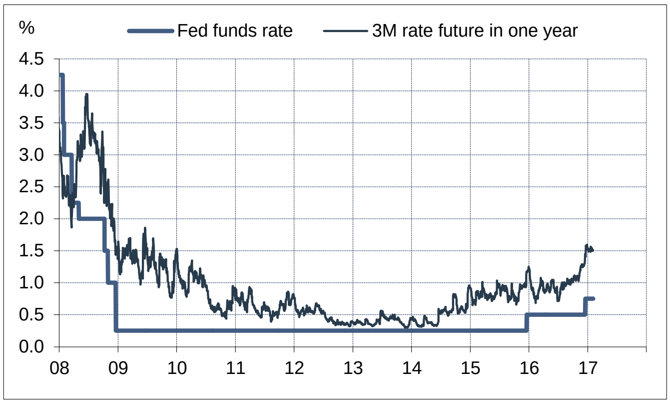



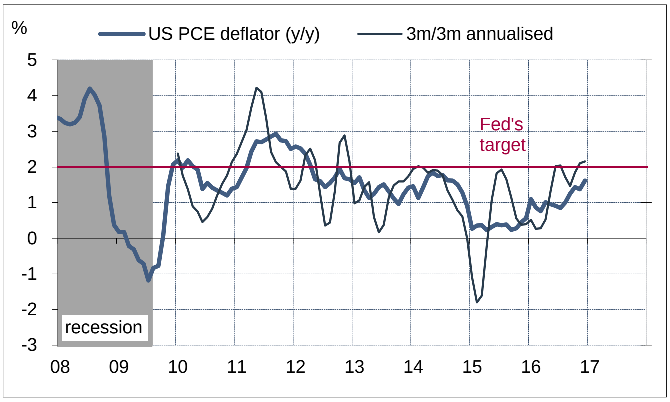



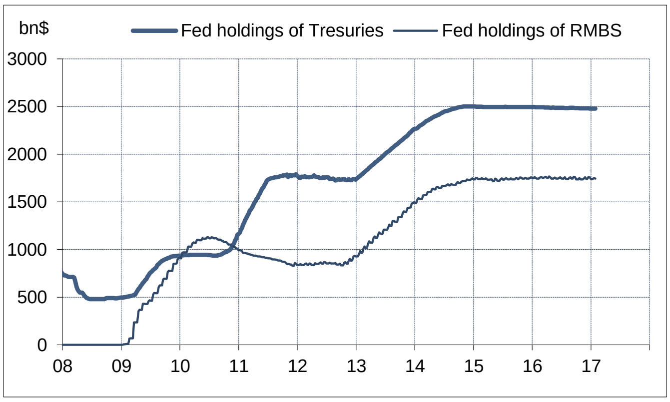

*Sources : Thomson Reuters, Bloomberg, Oddo Securities*

## Appendix 5 - Inflation and monetary policy

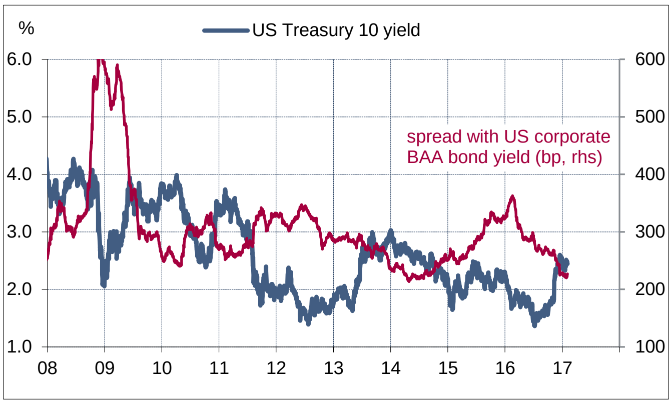


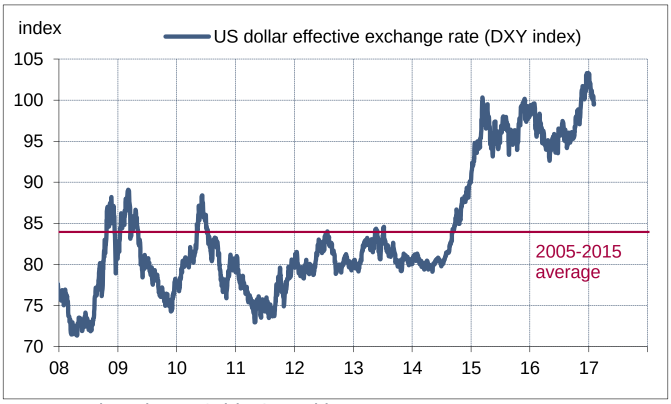




## Appendix 6 - Financial markets






*Sources : Thomson Reuters, Bloomberg, Oddo Securities*

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