



Oxford Economics March 2014



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March 2014

Why a model? Why Oxford Economics?

Presentation to emerging risk seminar



Oxford Economics



- Analysis for better decisions



A world leader in quantitative economics & business research



- Founded 30 years ago as a private consultancy within Oxford University

Our international reputation was built on:

- **The quality of our staff.** 80 economists from leading organizations across our offices in **Europe , US and Asia**
- **A rigorous quantitative approach,** based on our leading **models**
- **Our ability to adress questions** in **consulting studies**
- **Our links with Oxford University and other institutions** providing access to the **latest thinking**

Independent economic advisory

Forecasts | briefs | data

190 countries

100 industries

2,600 cities & regions

Quarterly scenarios, Commodities, Investment

Retail sales splits, Trade flows, Talent, Tourism

Models | forecasting | scenario | risk

Global macro model

Global industry model

Consulting | Business Research | Out-sourced economic analysis

Impact studies

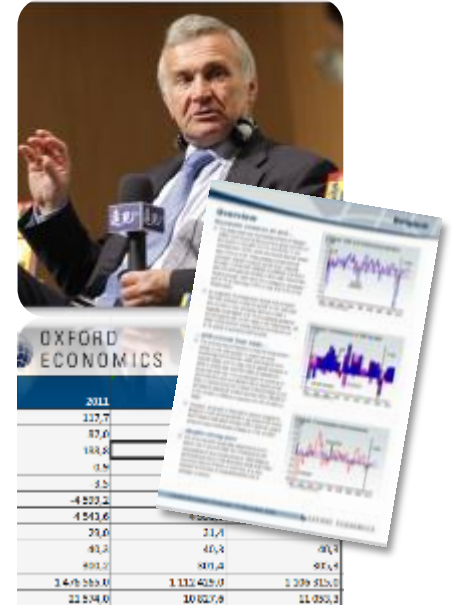
Thought leadership

Market sizing

Industry intelligence

Economic policy

Regional economics





Oxford Economics



- The outlook for 2014



Main scenario forecasts – GDP growth p a

Country		2013	2014	2015
United States	GDP	1.9	3.1	3.2
	Trend	1.9	2.3	2.4
EuroZone	GDP	-0.4	0.9	1.4
	Trend	0.8	0.9	1.1
France	GDP	0.1	0.5	1.1
	Trend	0.8	1.0	1.1
Germany	GDP	0.5	1.6	1.7
	Trend	1.5	1.6	1.6
Italy	GDP	-1.9	0.3	1.2
	Trend	0.2	0.2	0.3
United Kingdom	GDP	1.9	2.6	2.4
	Trend	1.8	1.9	2.0
China	GDP	7.6	7.3	7.2
	Trend	7.9	7.5	7.2
Japan	GDP	1.7	1.8	1.4
	Trend	1.0	0.9	0.8

Main themes

- US recovery continues and accelerates in 2014
- Europe recovering but weakly and subject to political risk, risk of deflation
- Abenomics will succeed – and fail
- Chinese growth healthy for now but will eventually slow in the longer term

Main risks

- Exogenous shocks
- Higher long-term interest rates
- EZ deflation
- EU Parliament elections
- ECB AQR in October
- Financial crisis in China
- Abenomics not working
- Renewed financial market turmoil

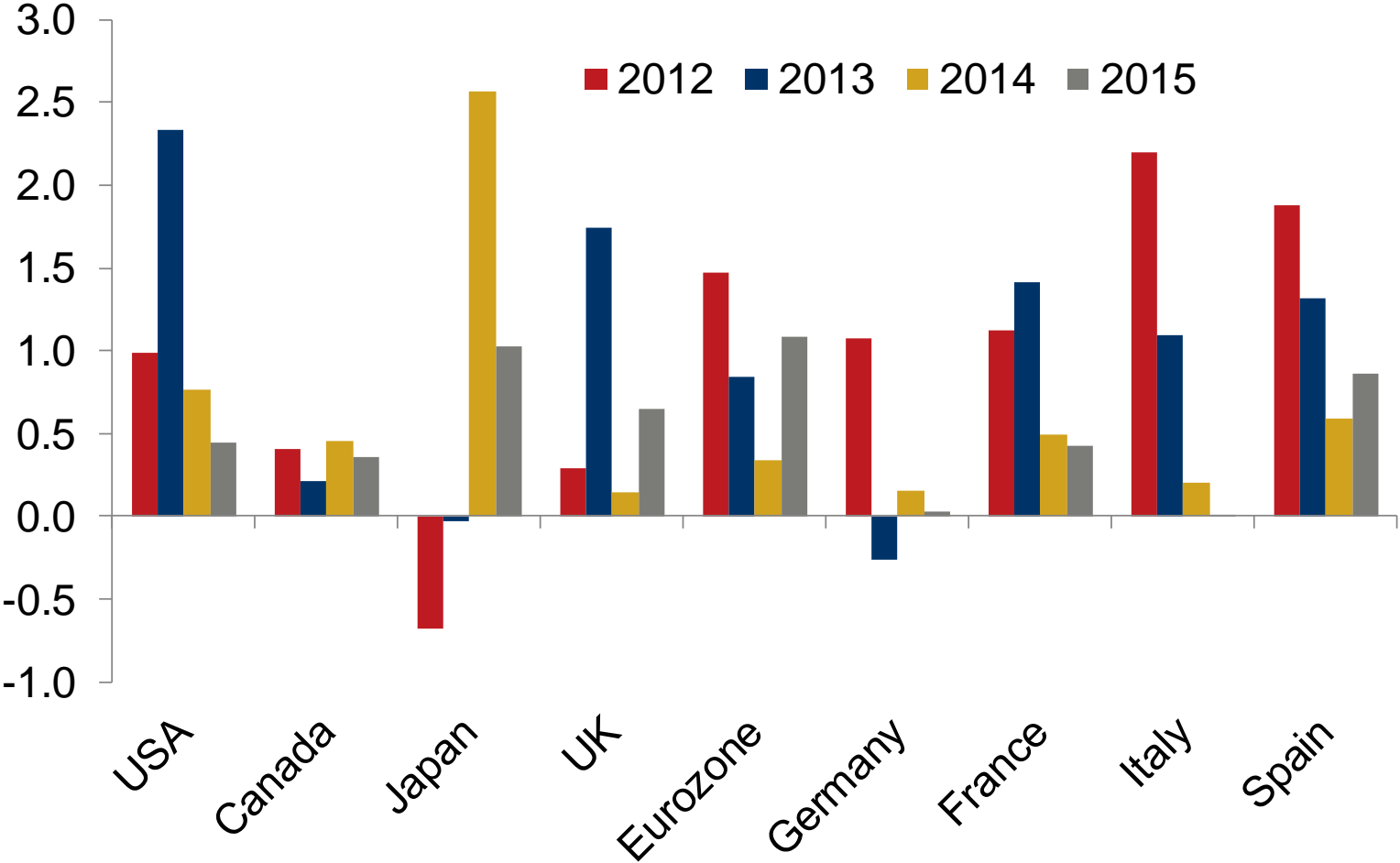
Broad asset trends

- US dollar strength on growth, interest-rate differentials
- Euro stabilises – but ECB likely to try to push it down
- Yen, EMs down
- Commodities flat to up
- US equities could see correction but trend is up
- Fixed income down
- EZ, Japanese equities up – staying power?

Fiscal headwinds are abating

World: Structural budget balance changes

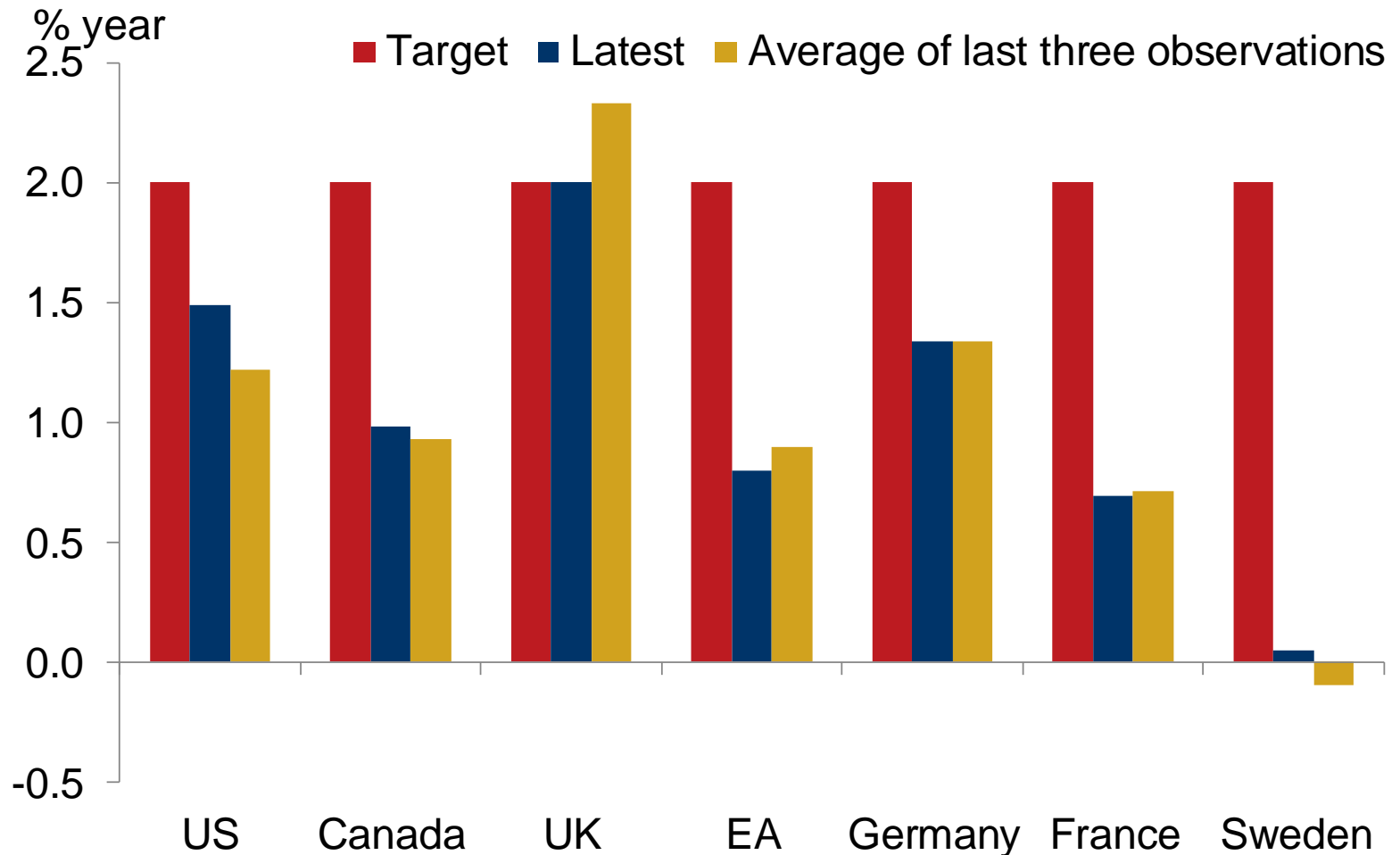
% of trend GDP



Source : IMF

Inflation is not a DM concern – deflation in Eurozone is

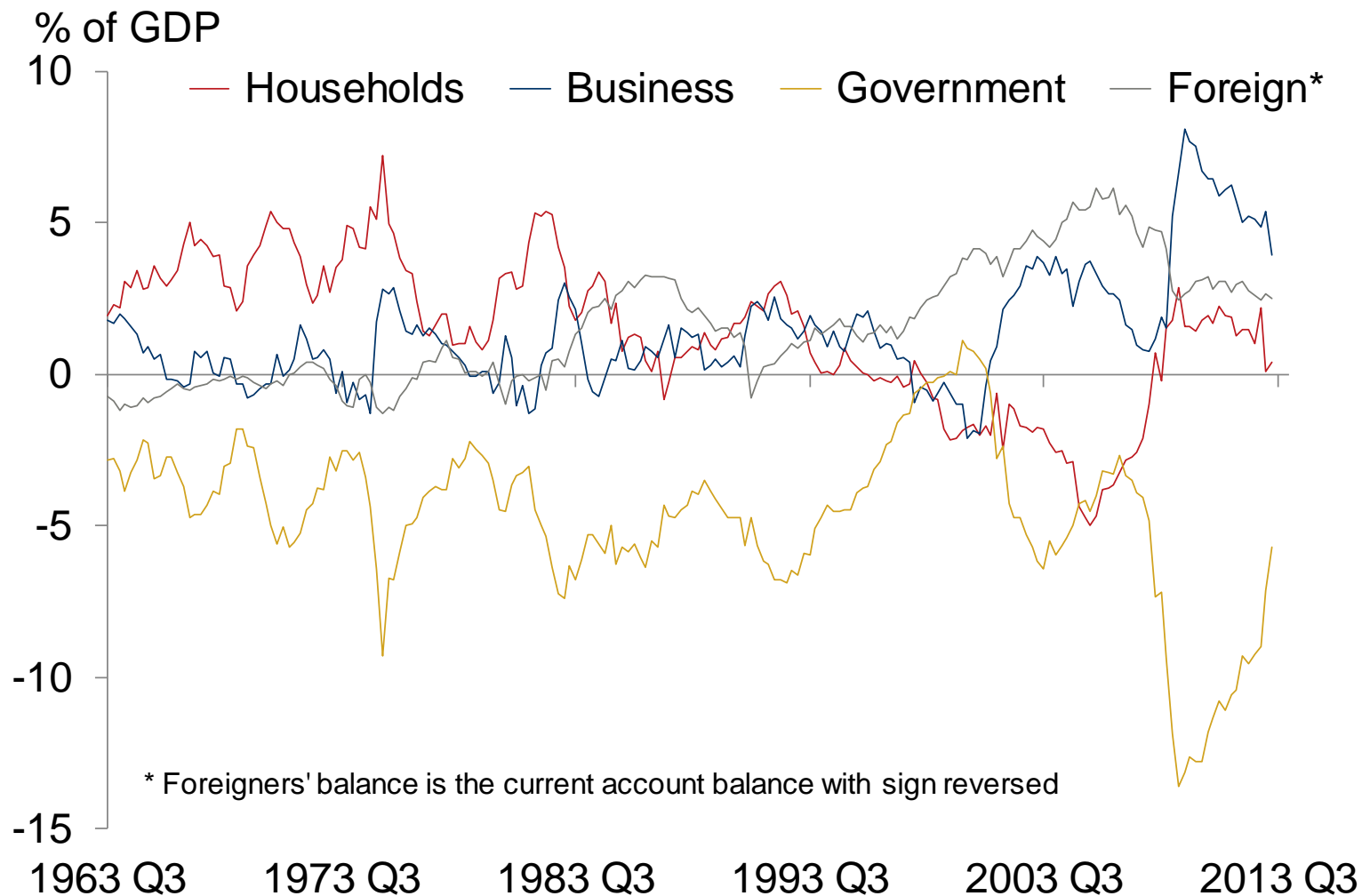
DM: Inflation



Source : Oxford Economics/Haver Analytics

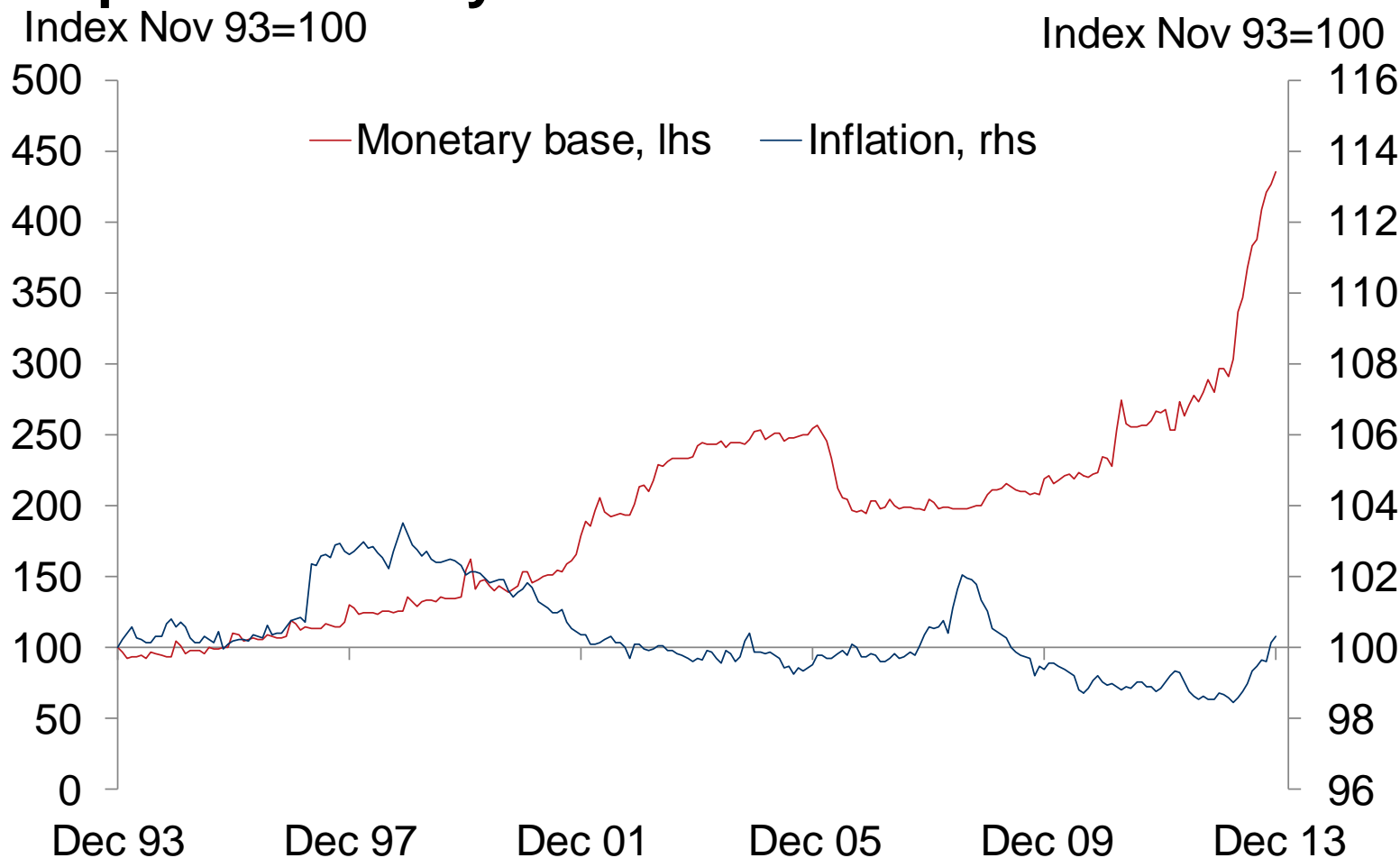
Foreign sector still reacting to domestic events

USA: Sectoral financial balances



Monetary base/inflation relationship is tenuous

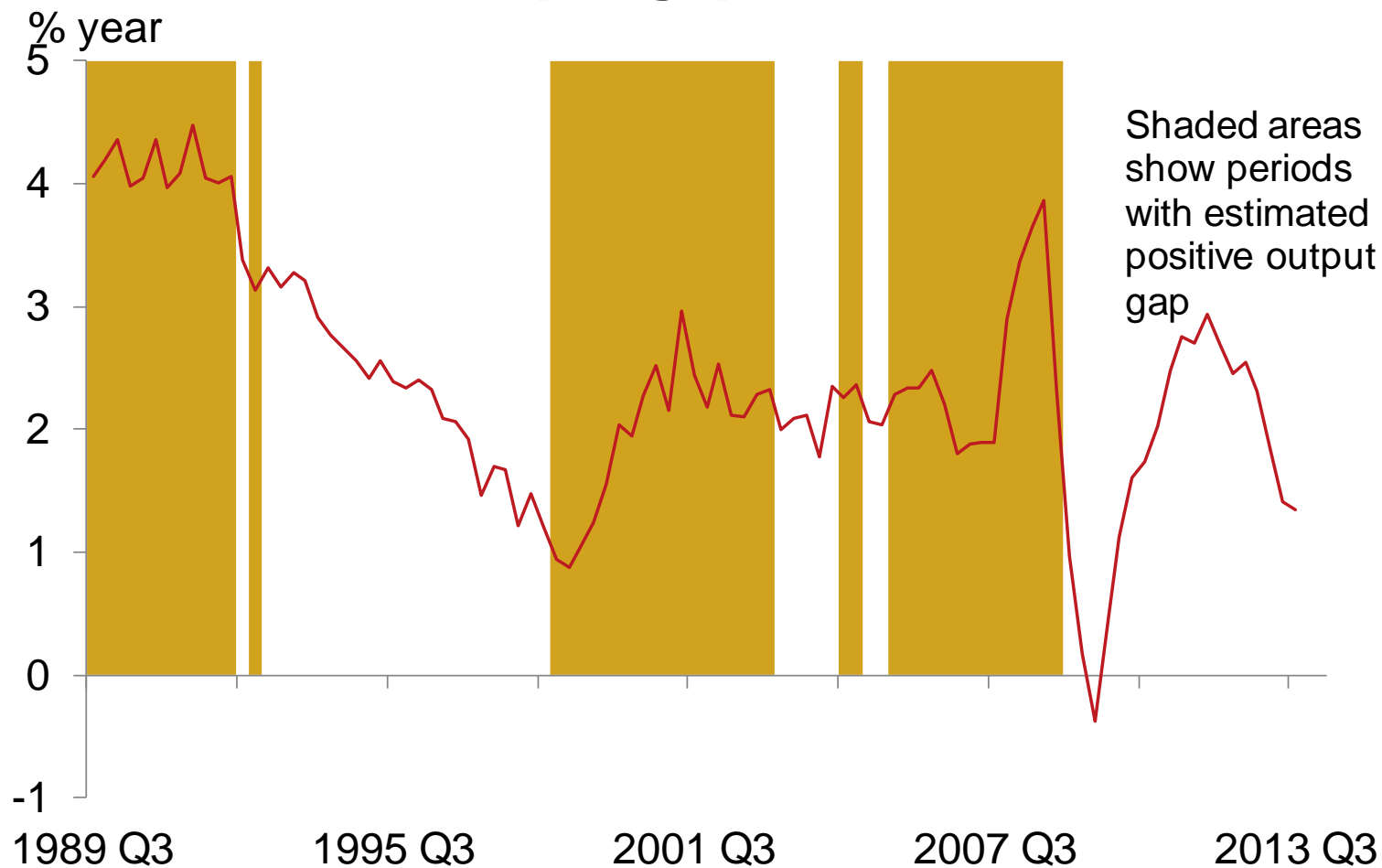
Japan: Monetary base and inflation



Source : Oxford Economics/Haver Analytics, Bank of Japan

Negative output gap points to deflation

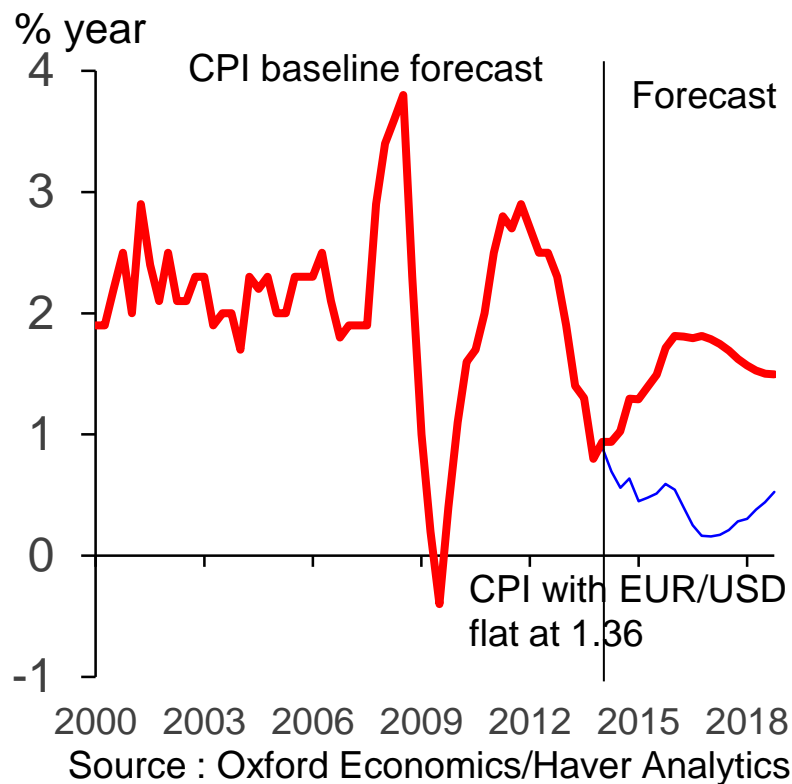
Eurozone: the output gap and inflation



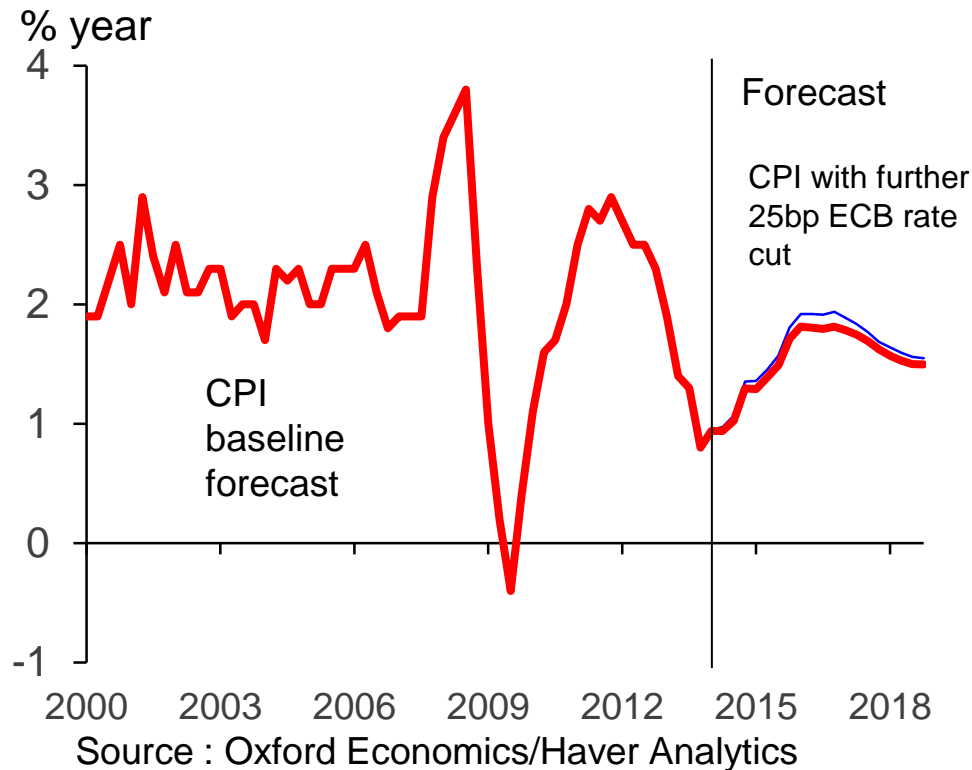
Source : Oxford Economics/Haver Analytics

Some scenarios

Eurozone: Inflation with a strong euro



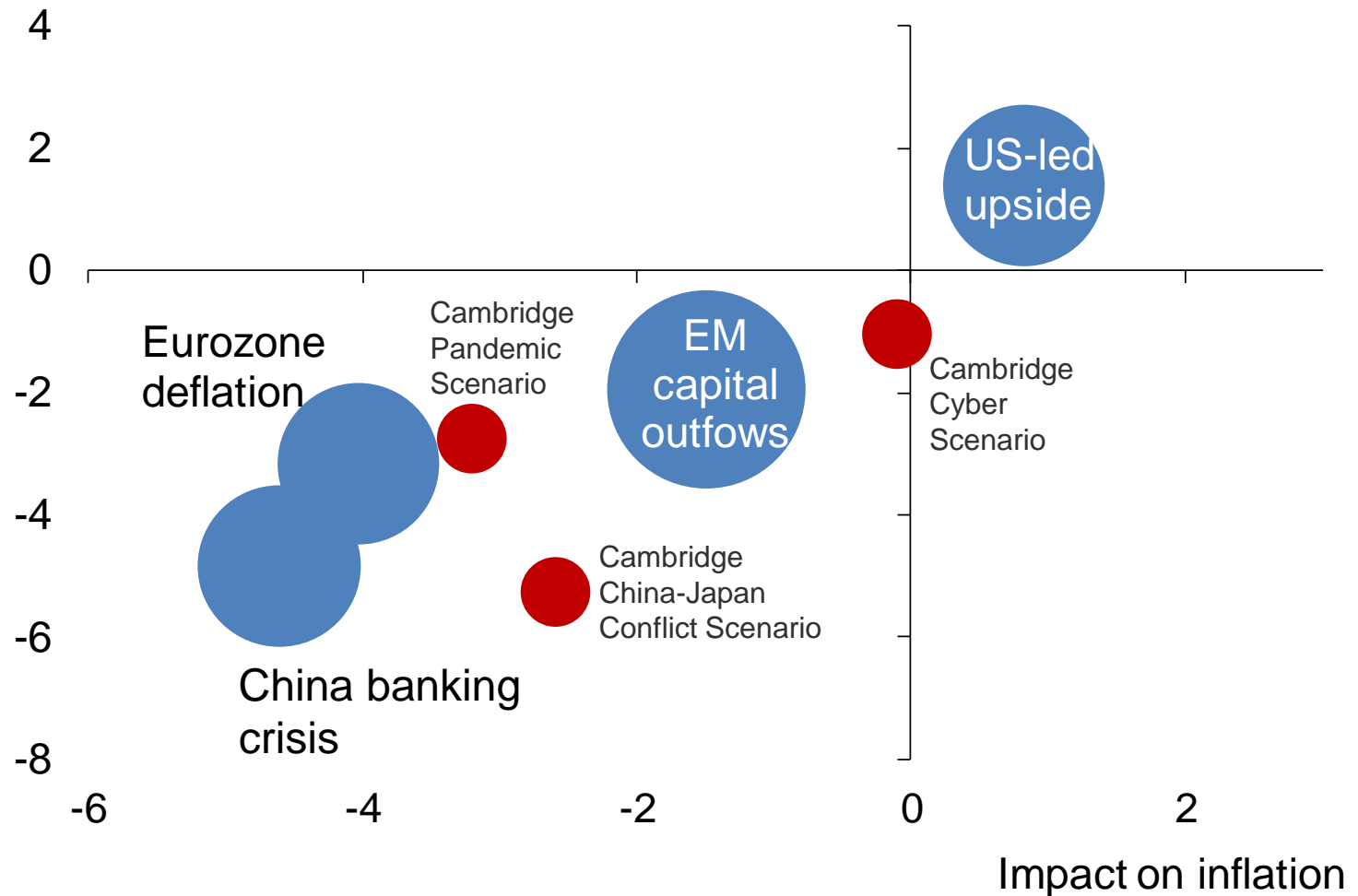
Eurozone: Inflation with a further rate cut



Alternative scenarios - impact

Global scenarios

Impact on GDP



Source : Oxford Economics

Downside scenarios – background

China banking crisis (10%)

China's credit boom quickly becomes a crisis. NPLs rise rapidly, and banks cut back sharply on new credit supplied to the economy.

Growth falls well below 5%pa, despite government intervention, and is limited by slow credit growth in the out years.

Other emerging economies are hit hard, and the Eurozone and Japan fall back into recession. The US fairs better, but growth still falls to near-negative rates.

Capital flows out of emerging markets (15%)

Renewed sharp capital outflows from emerging markets – 'fragile 5' particularly hard hit

Investment in EMs is undermined by weak infrastructure, corruption and reduced expectations for long-run growth
Spillovers to China and developed economies is limited, as affected EMs have a small share of world demand.

Baseline (50%)

US growth accelerates as impact of fiscal austerity fade and strong competitiveness drive investment .

Momentum builds slowly in Europe as austerity fades, but tax rise slows Japan's growth.

Fragile emerging markets remain under pressure and continue to tighten policy.
Rebalancing in China continues.

Eurozone slides in deflation (10%)

Weak demand, excess capacity and strong euro push Eurozone into deflation. GDP falls for another two years.

ECB only responds late with further liquidity boost. OMT is activated.

Peripherals require banking union to stay in EMU.

Global risk aversion increase as stability of EMU is again questioned.

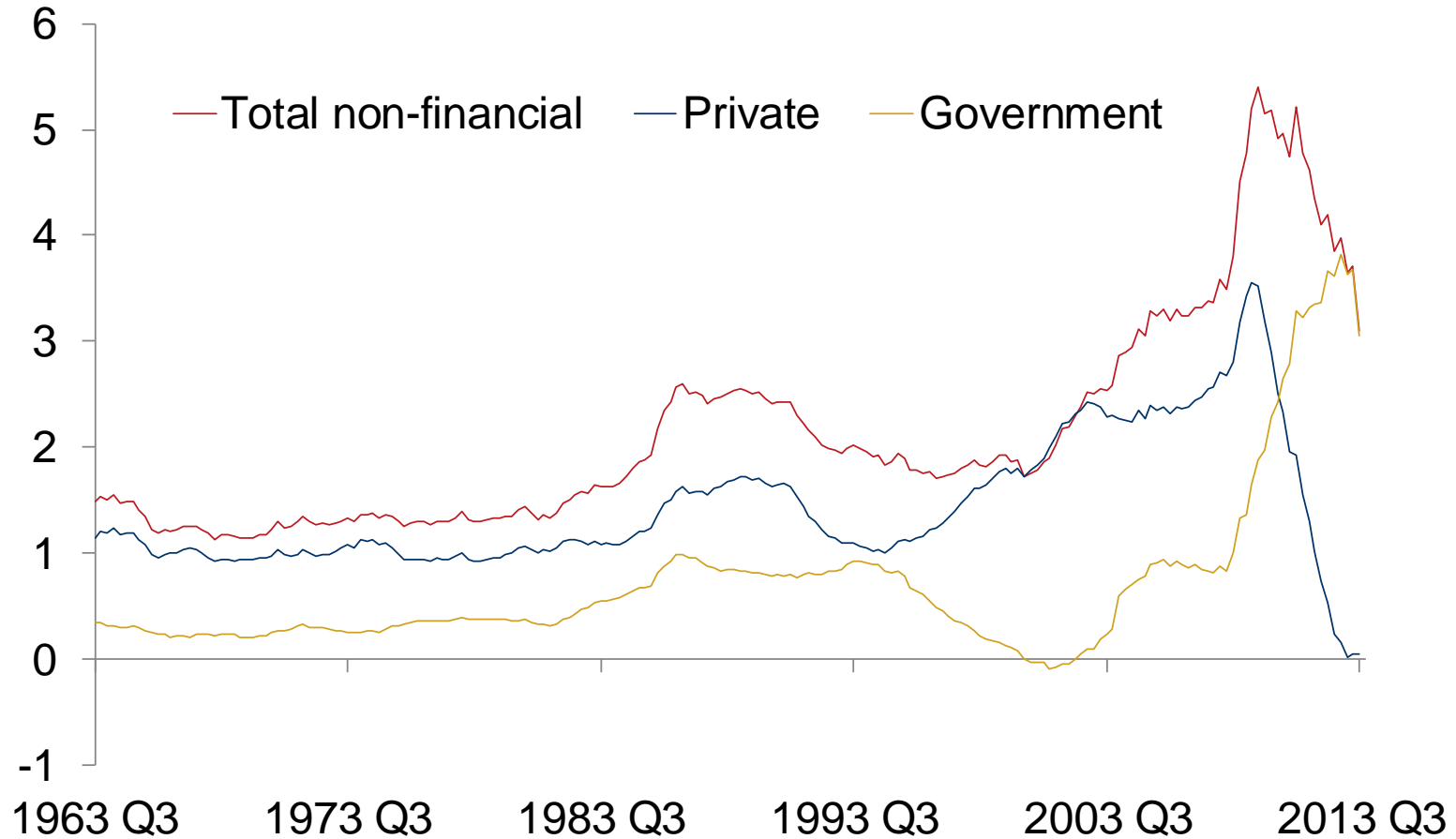
Financial fragility

Domestic demand fragility

Debt-based growth model has come to an end

USA: Debt and output growth, 5-year m a

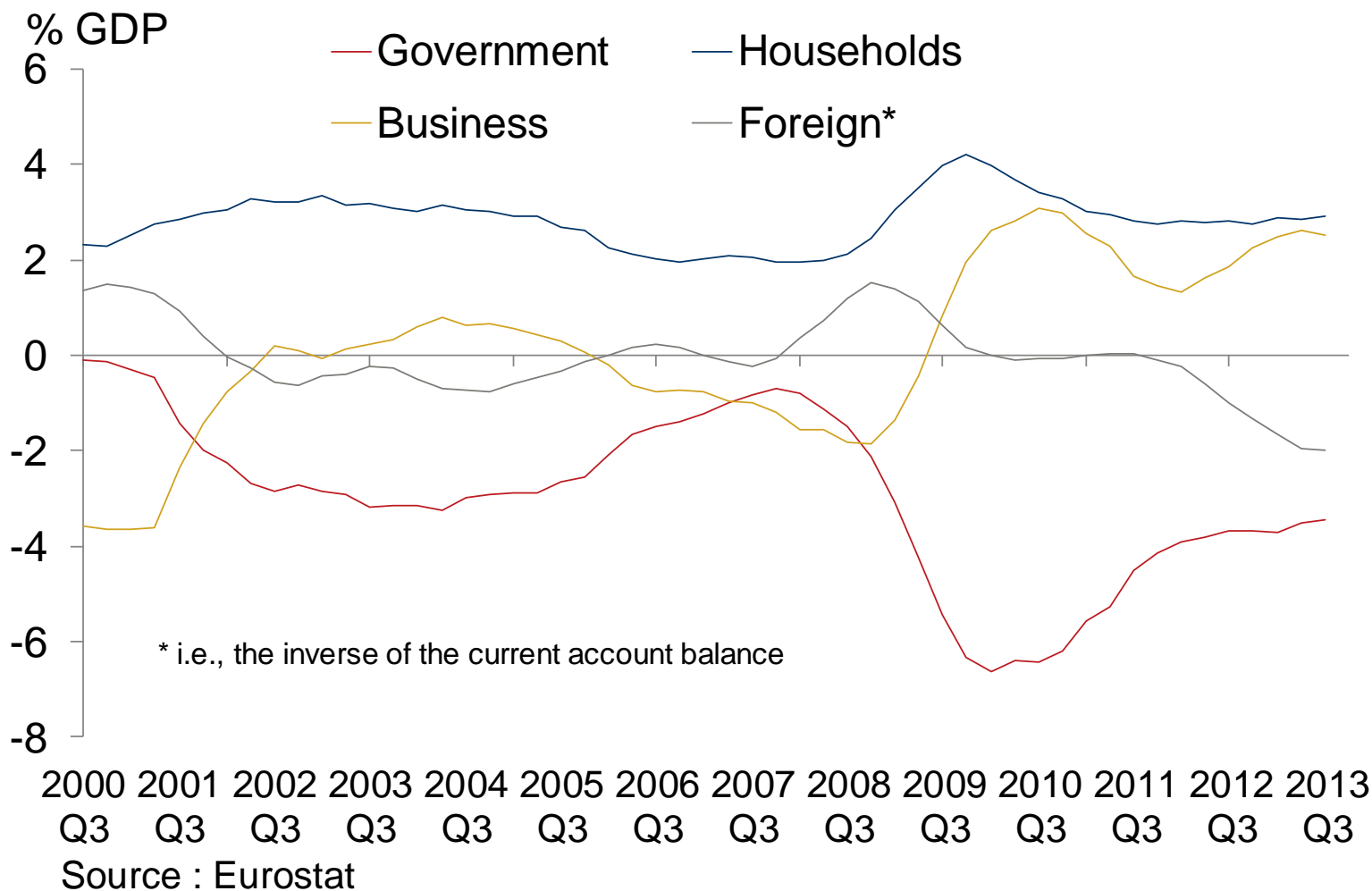
\$ debt/extra \$ GDP



Source : Financial Flows of the United States

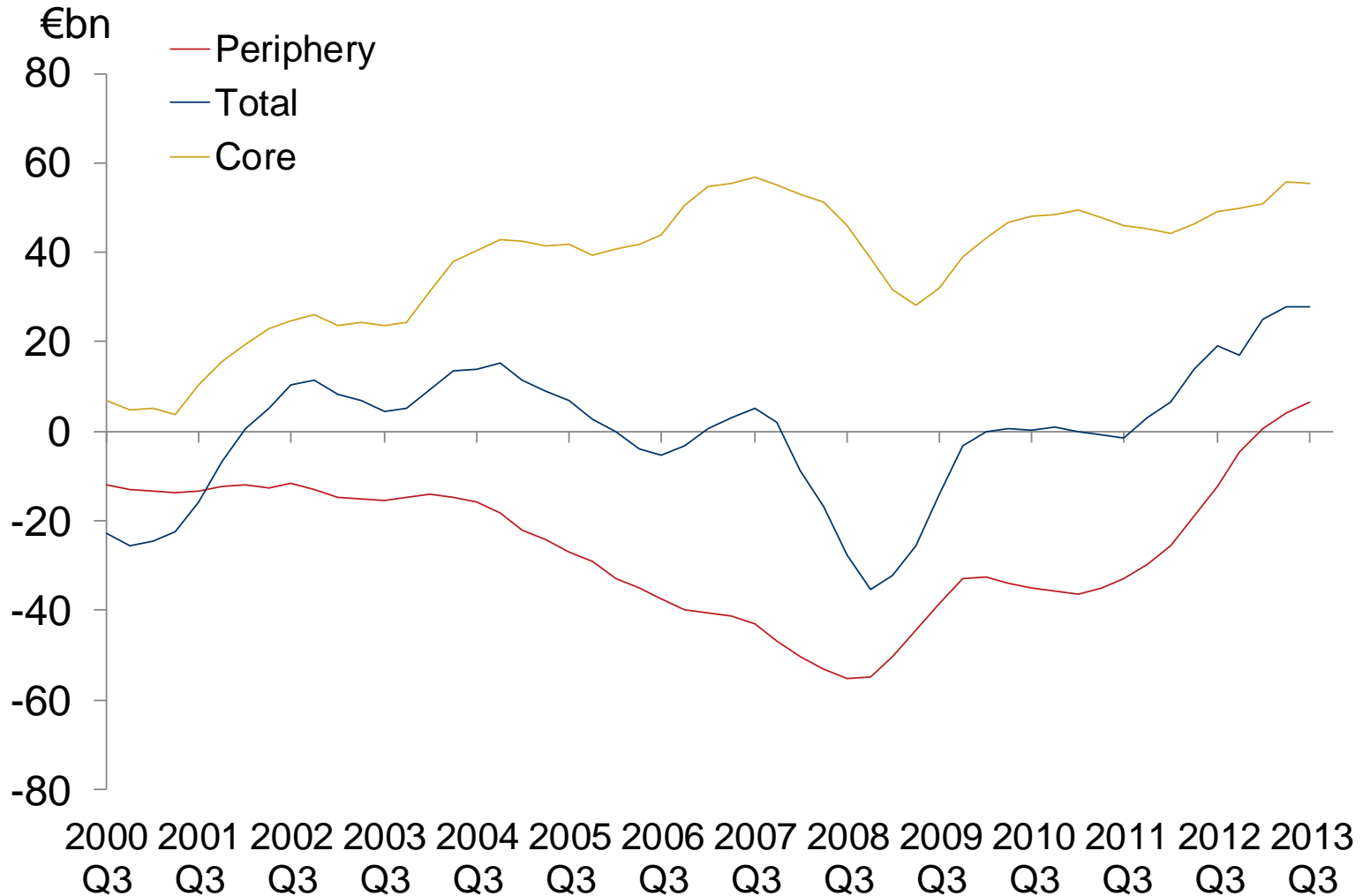
The rise of the sustained c/a surplus...

Eurozone: Sectoral financial balances



...coming from the periphery...

Eurozone: Current account balances

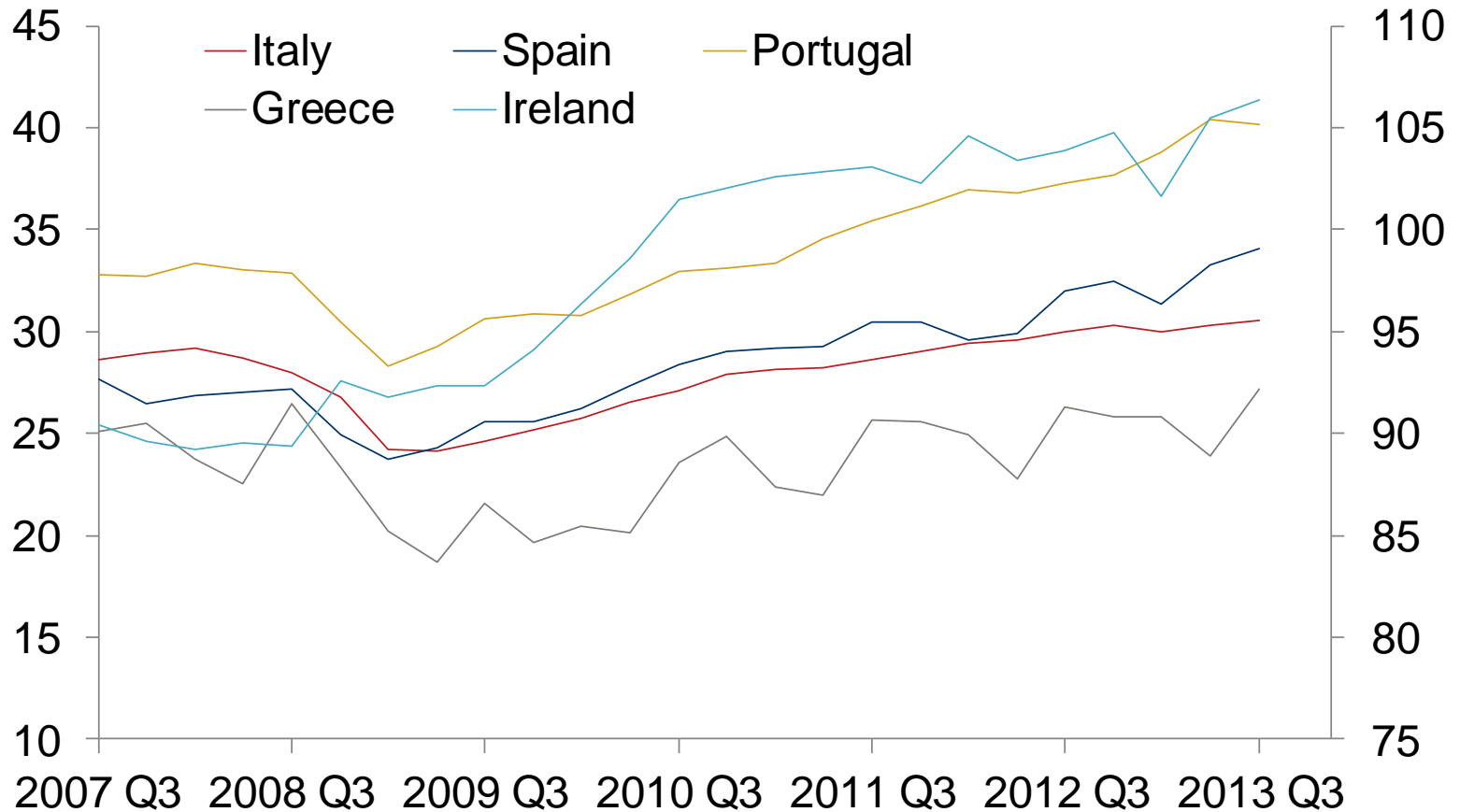


Source: Eurostat

...through rising exports...

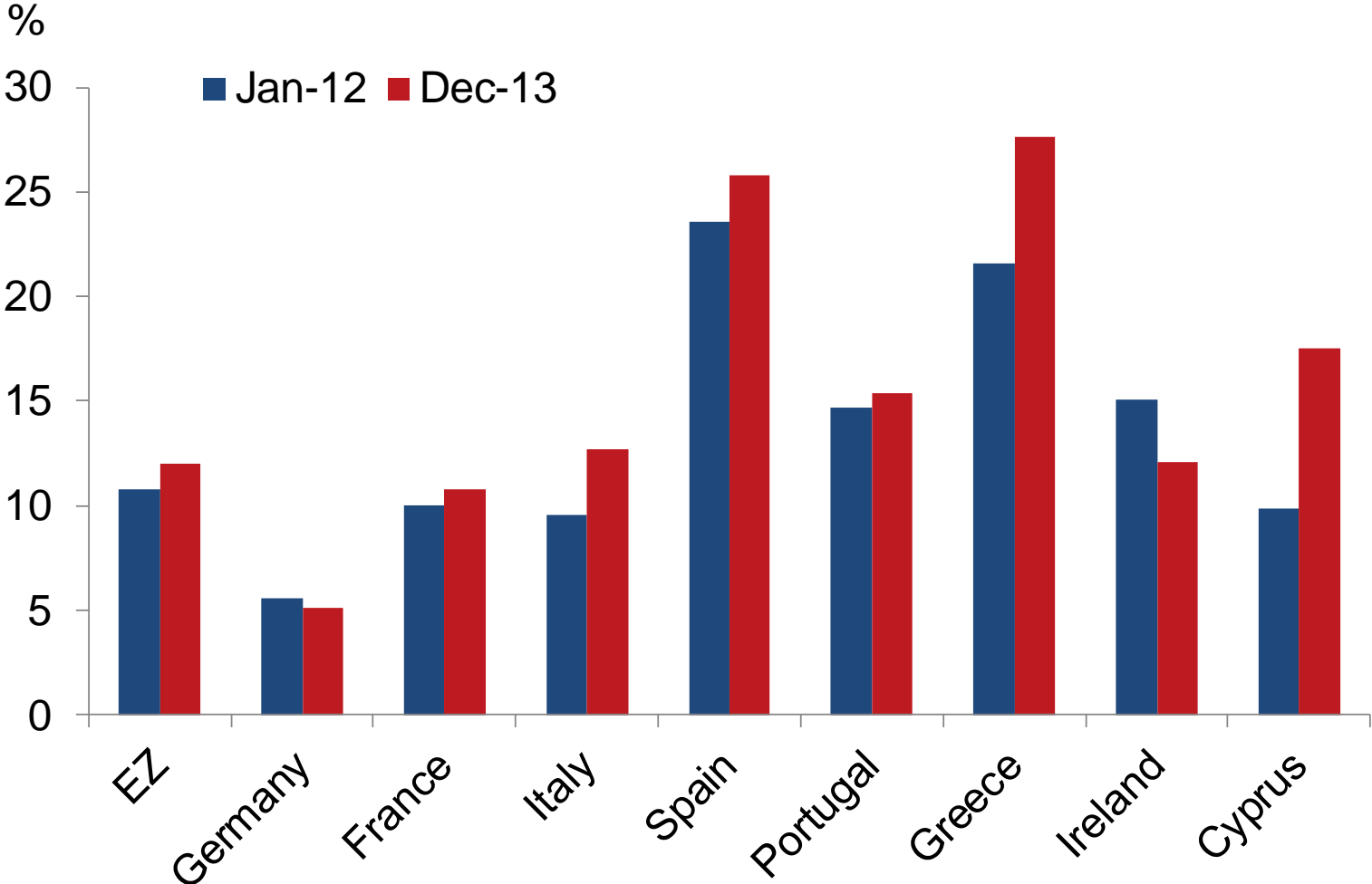
Eurozone: Periphery exports

% of GDP



Source : Oxford Economics/Haver Analytics

...and the destruction of domestic demand



Source : Eurostat

The return of demographics

Why bother with demographics?

- Interest in demographics comes and goes
 - In the 1950s it was shrinking population
 - In the 1970s it was population explosion
 - In the 2000s it is once again shrinking population
- One issue is pensions
- Another is output growth and return on assets
 - Large population doesn't guarantee power but it helps
 - Rising population doesn't guarantee growth but its absence guarantees the opposite
 - Growth doesn't guarantee return on assets but it helps
- Keep an eye on demographics!

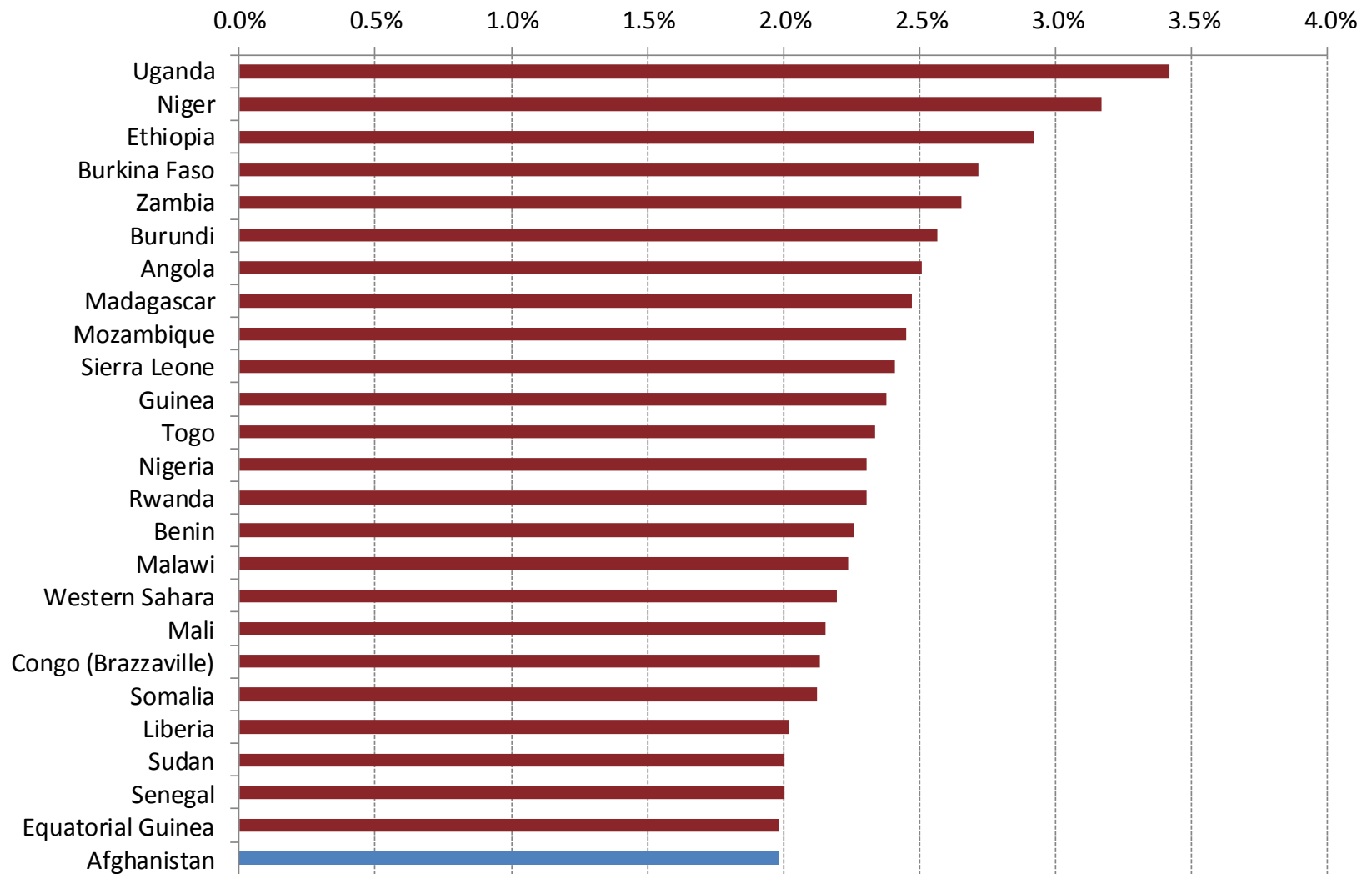
Relative stability at the top

The ten largest countries by population 2015 and 2050

2015		2050	
China	1,361,513	India	1,656,554
India	1,251,696	China	1,303,723
United States	332,371	United States	422,554
Indonesia	255,759	Nigeria	402,426
Brazil	212,346	Indonesia	313,021
Pakistan	199,086	Pakistan	290,848
Nigeria	183,529	Ethiopia	278,283
Bangladesh	168,958	Brazil	260,692
Russia	136,010	Bangladesh	250,155
Japan	126,920	Philippines	171,964

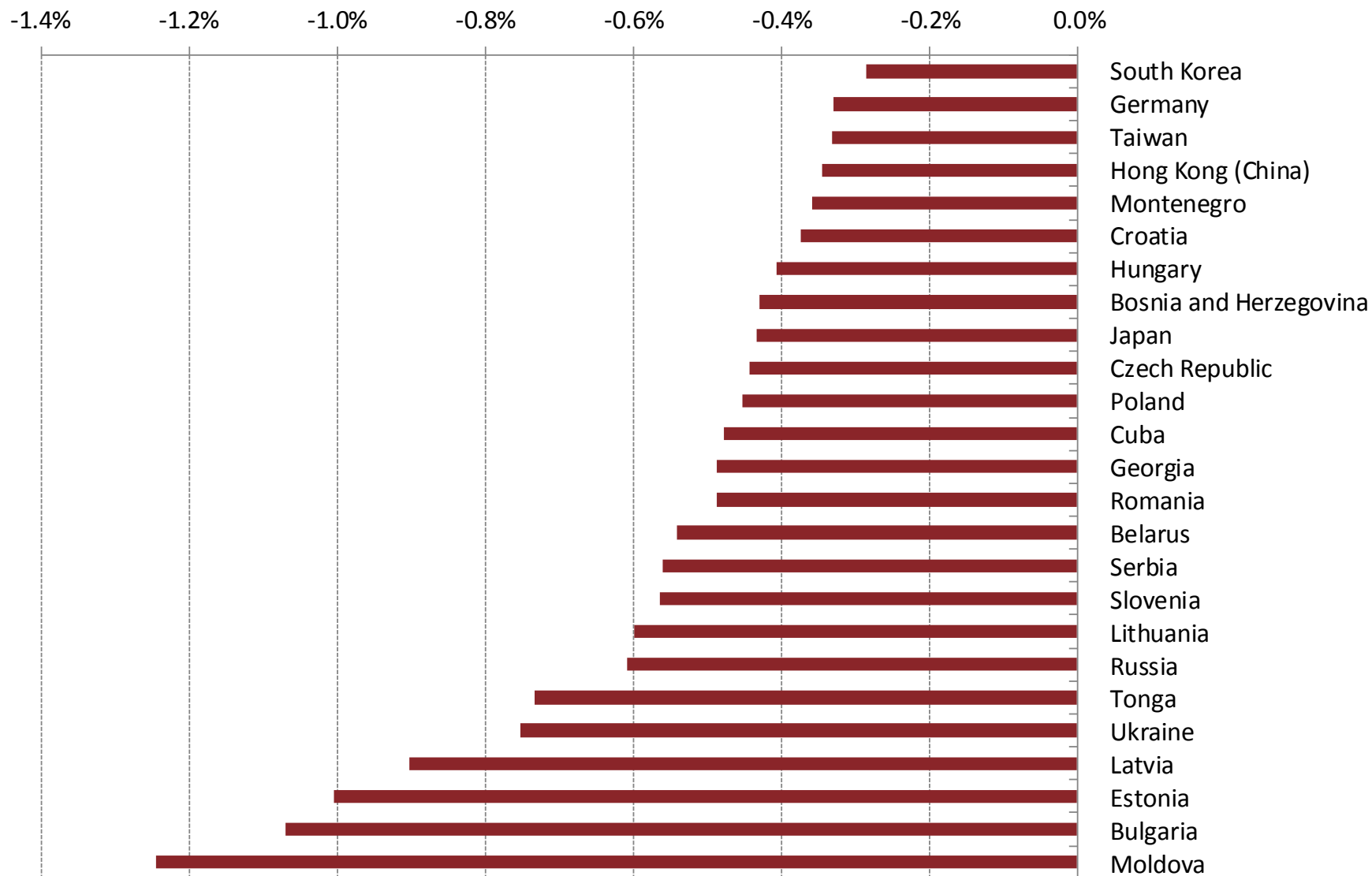
Note: Russia and Japan disappear, replaced by Ethiopia and the Philippines

Fastest population growth 2010-2050, % annual change, Africa rules



Slowest population growth 2015-2050, % annual change

Europe falters



DM demographic consequences

- Most, if not all, of the population growth will be in the cities, fuelled by immigration.
- A growing population will consume more.
- But consumption patterns may change, particularly from goods to services.
- Come back butler, come back maid, all is forgiven!
- Expect broader social and cultural changes.

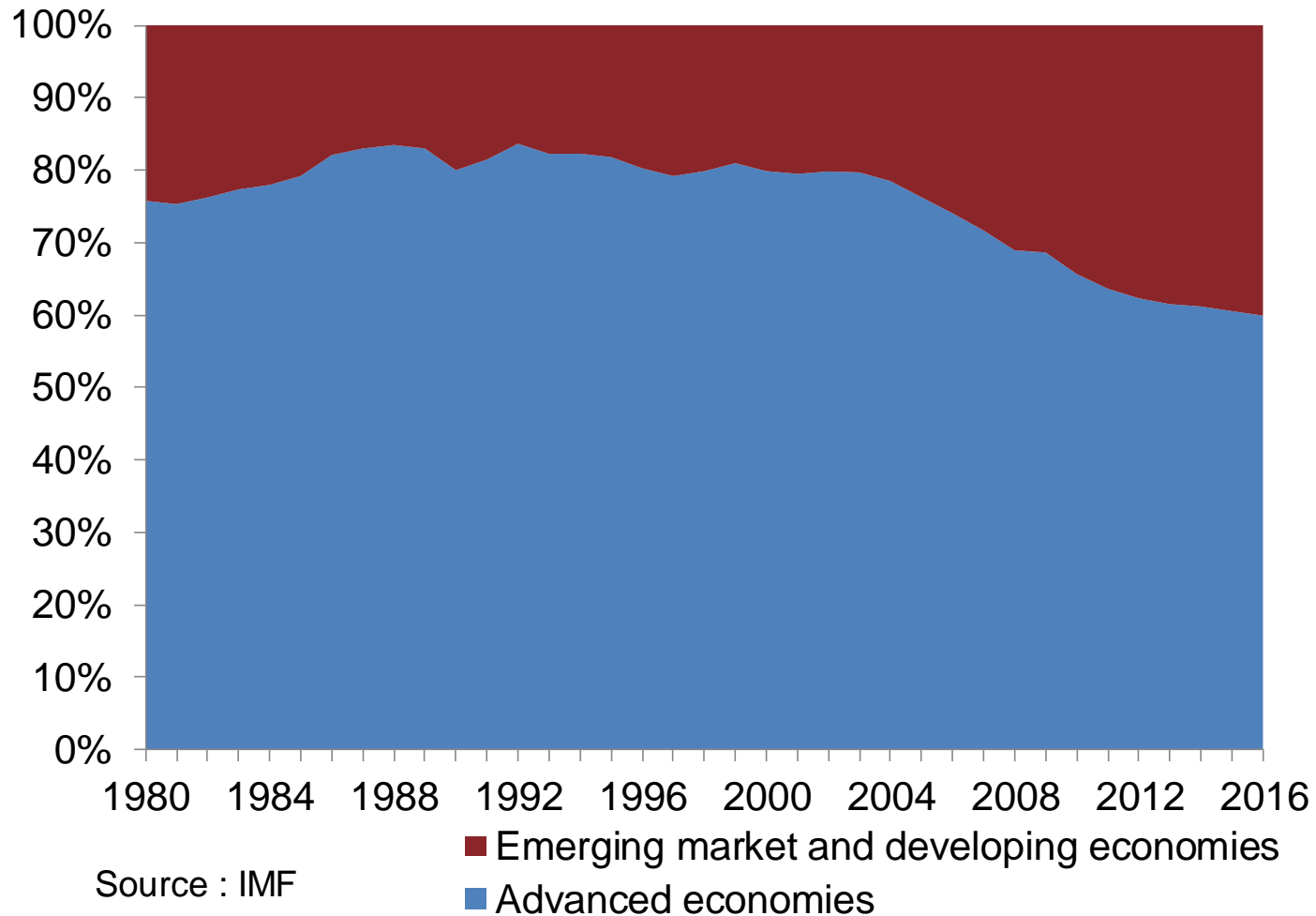
Conclusions

- Plan for an increasingly urbanised region – with all that this entails
- Separate strategies for each country
- For producers – consider labour, rather than capital intensive sectors
- Follow the policy

The new world masters

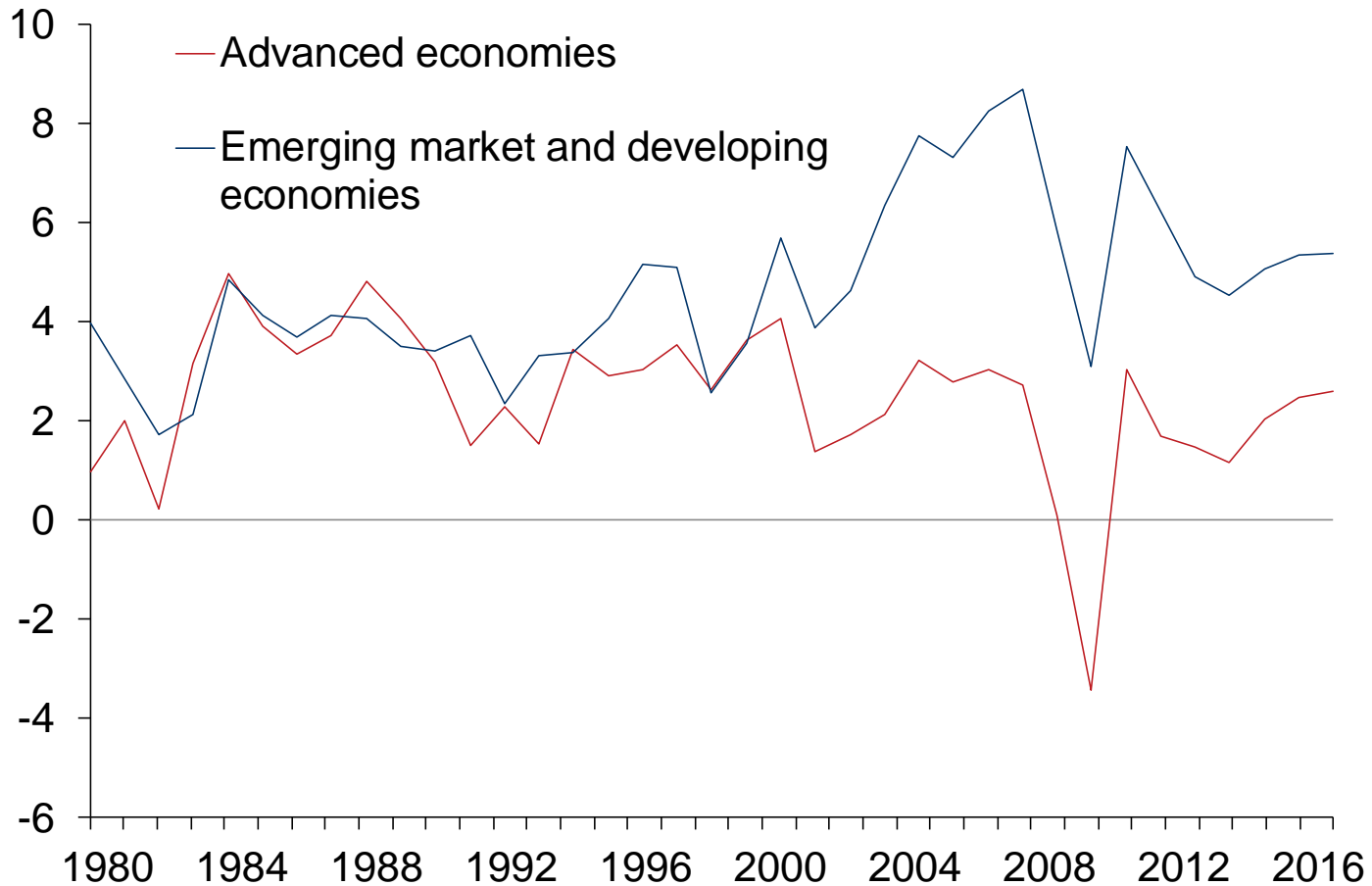
World: GDP, US\$, current prices

Share of GDP



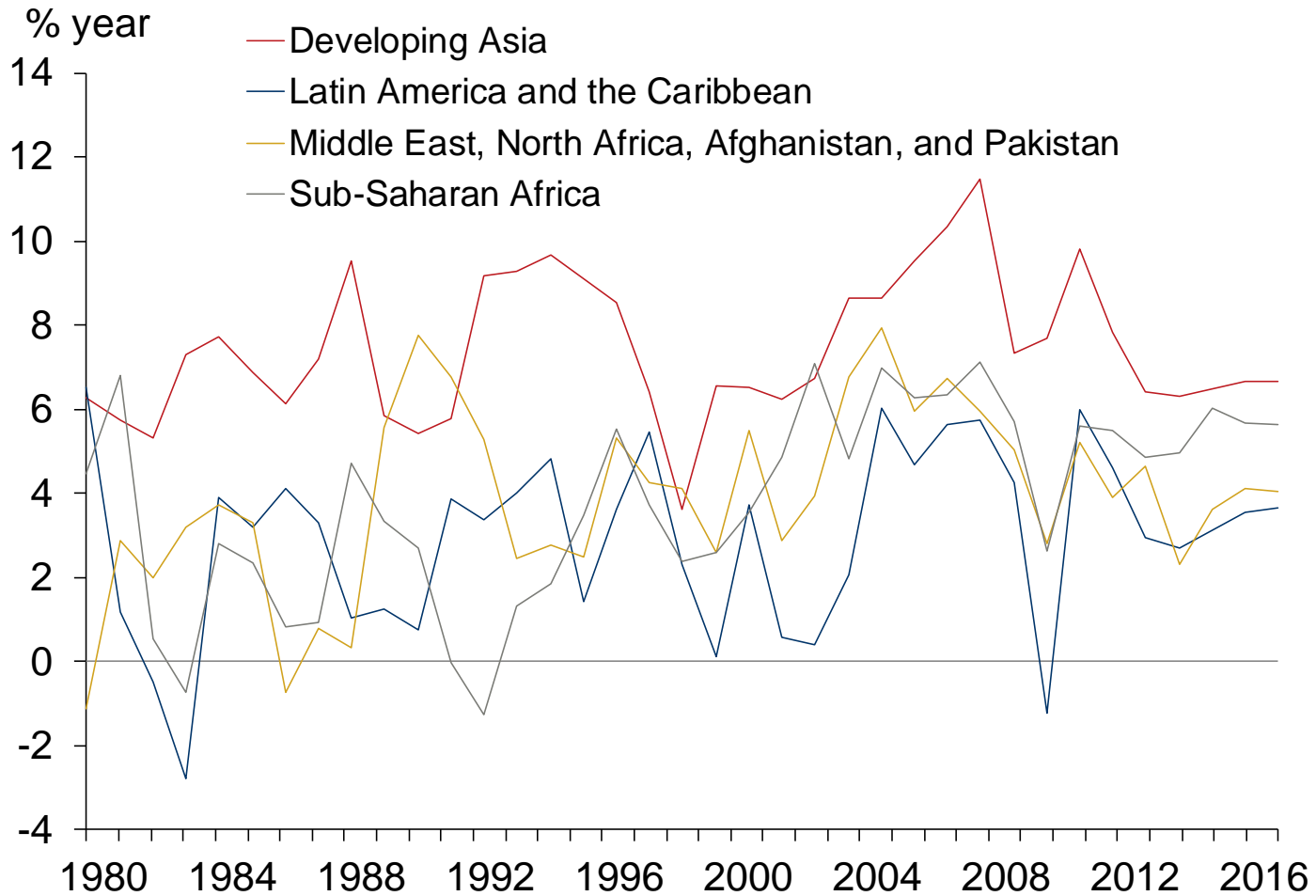
World: Real GDP growth

% year



Source : Oxford Economics\IMF

World: Real GDP growth by region



Source : Oxford Economics\IMF