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**The Investment Expert:**  
Asset allocation strategies for a new investment landscape

## Mapping the Political and Economic Environment for Investment

By Brunello Rosa, Director of Macro – Strategy

Stockholm, 22 October 2013

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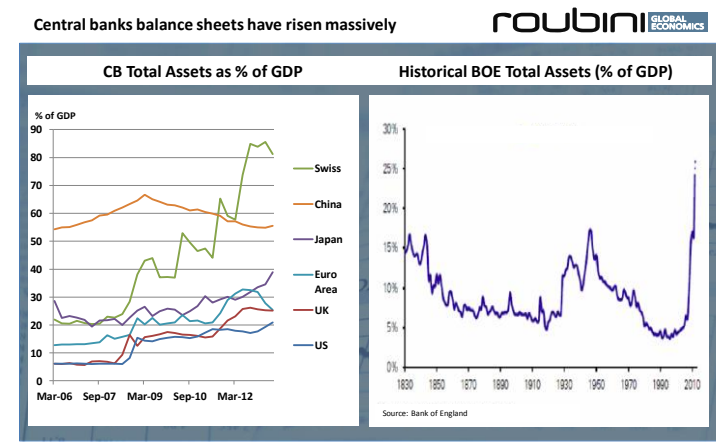
Today's Discussion:

1. The role of central banks in influencing economic recovery
  - Credible and incredible Forward Guidance
2. EZ economy: is it really the end of the crisis?
  - Debt sustainability: The dark side of "whatever it takes"
3. The outlook for the US economy
  - Desperately seeking escape velocity
4. Chinese Growth
  - Forecasting and trading the slowing Chinese economic growth

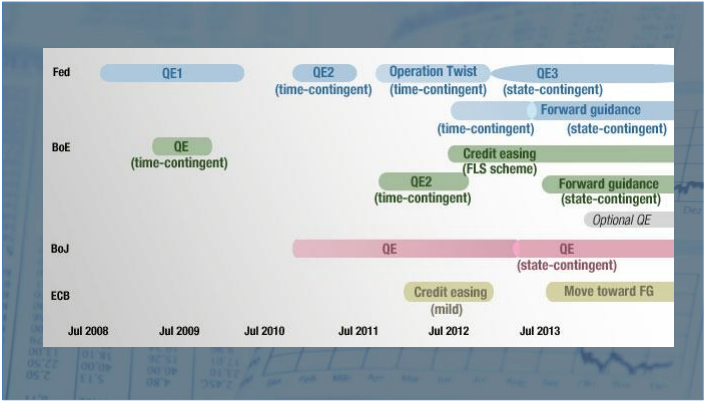
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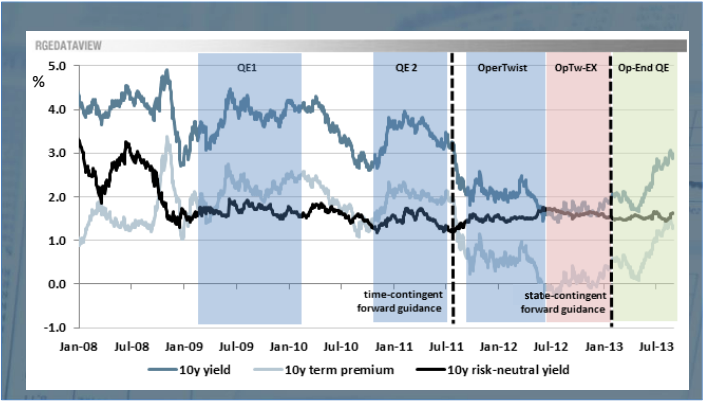
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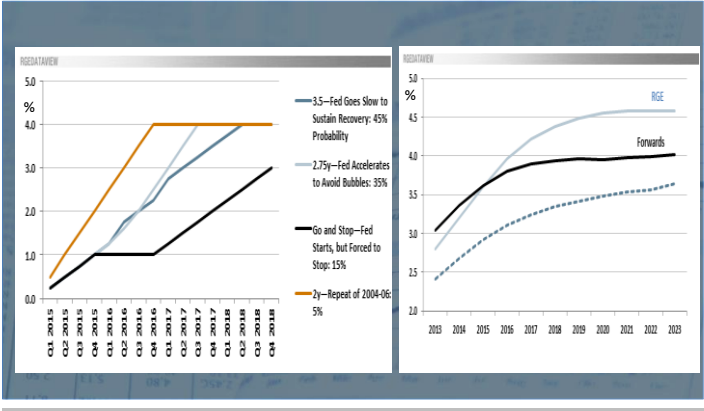
A timeline of "unconventional" Central Banks' interventions **roubini** GLOBAL ECONOMICS



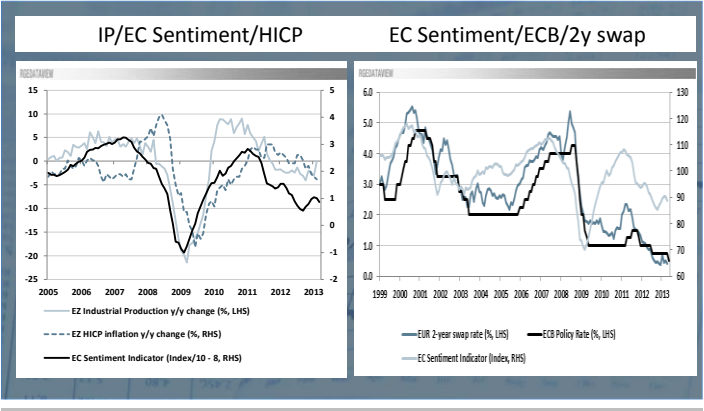
Impact of Fed's decision on long-term bond yields **roubini** GLOBAL ECONOMICS



Fed's expected policy normalization path, and the 10y yield **roubini** GLOBAL ECONOMICS

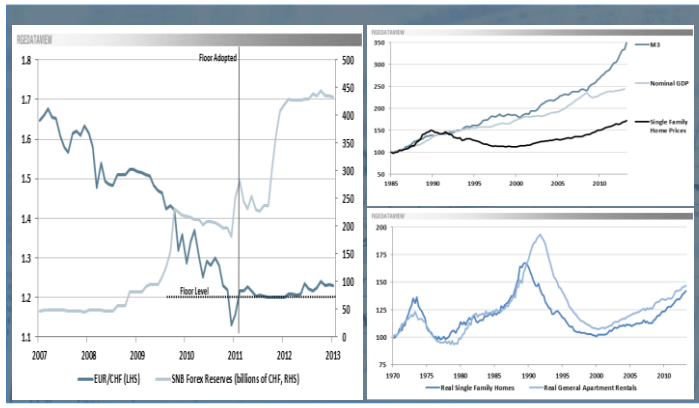


The ECB – The Belated White Knight **roubini** GLOBAL ECONOMICS

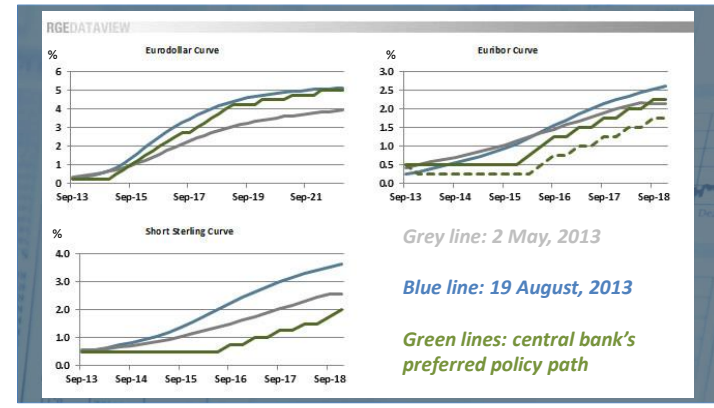


Source: *The Eurozone Malaise: From Economic Causes to Market Implications*, by Brunello Rosa, RGE, 13 May 2013

**SNB's Floor: but towards a ceiling in housing market?**



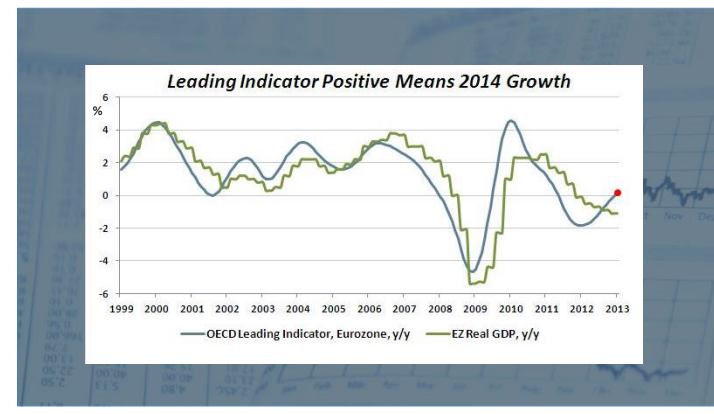
**Credible or Incredible Forward Guidance ?**



**Today's Discussion:**

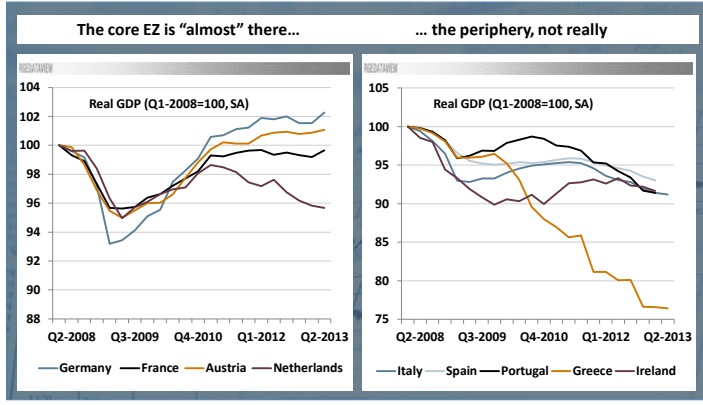
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**The tentative stabilization in EZ: growth or stagnation?**



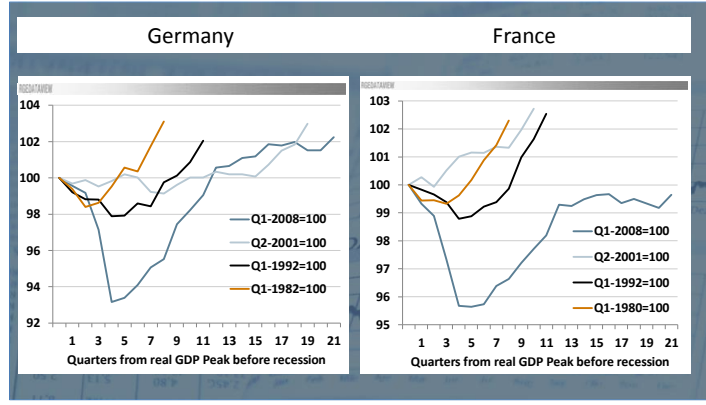
Source: Haver Analytics, RGE

GDP Growth since the peak



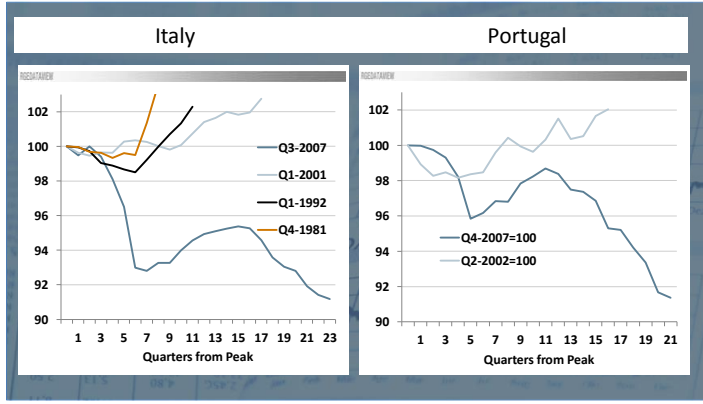
Source: Haver Analytics, RGE

Recessions: historical comparison in the core...



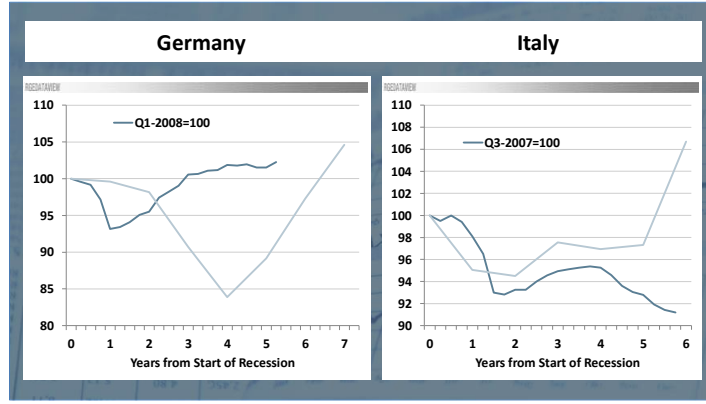
Source: Haver Analytics, RGE

... and the periphery



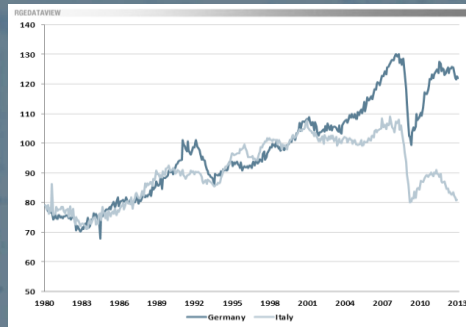
Source: Haver Analytics, RGE

How bad can "that" be?



Source: Great Depressions of the Twentieth Century, Federal Reserve Bank of Minneapolis, 2007; Haver Analytics, RGE;

German and Italian industrial production Indexes (ex-construction; base: 1999 = 100)



Source: [Italy Scenarios: Make it, Break it, or Muddle Through?](#) By Brunello Rosa, RGE, 27 March 2013

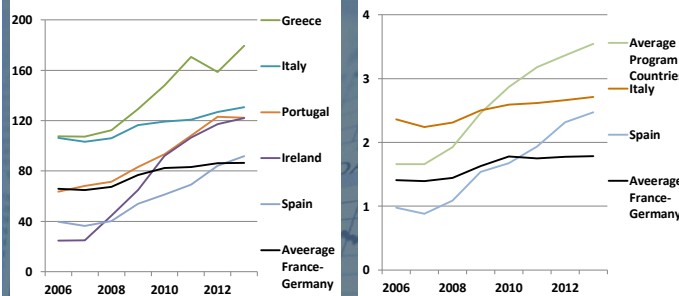
**Serious implications  
for debt sustainability**

**The dark side of  
“whatever it takes”**

The rise in public debt since the crisis

Gross Public Debt/GDP Ratio (%)

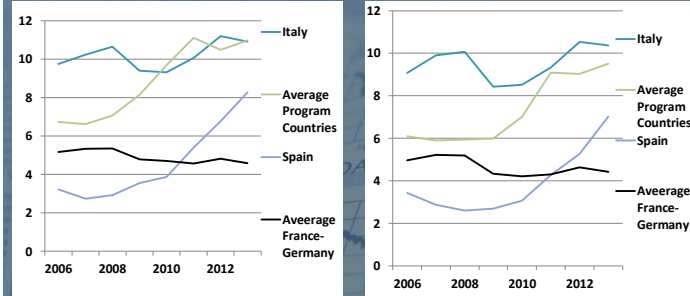
Gross Public Debt/Revenues (times)



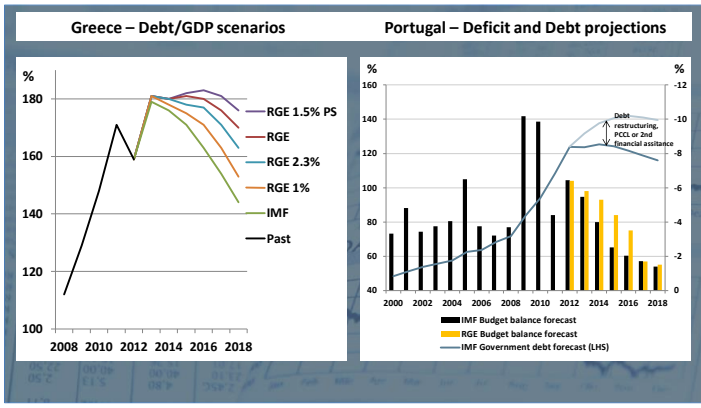
... and in debt-servicing costs

Interest Expenditure/Total Revenues (%)

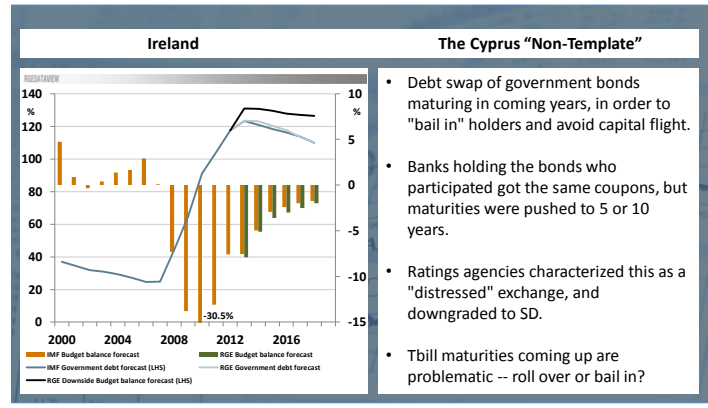
Interest Expenditure/Total Expenditure (%)



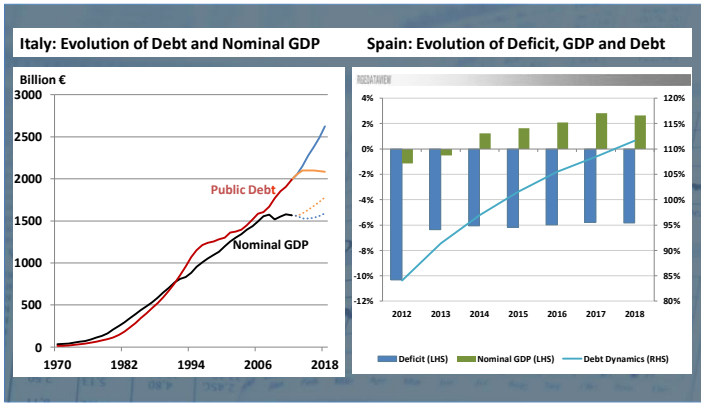
First countries in line...



... other program countries



The elephants... in the China store



Active Liability Management Exercises



- Guarantees:**
- Insurance is another possibility that would not result in residual debt.
- Collateral:**
- Secured bonds, senior to other bonds (US "tobacco bonds" EU lottery revenues)
  - Sequestration of Revenue Streams
- Liability Management:**
- Maturity extensions through debt swaps, possibly including deferral, capitalization, or PIK of interest due.
- Loans (following an ECCL program):**
- The IMF or ESM would lend long-term at low rates (compared to bond yields)
  - ESM and ECB could also conduct secondary market purchases
- OSI (when multilateral or bilateral lending large part of overall debt burden):**
- Lending gets extended and reduced in real terms through a combination of measures
- PSI (external debt and/or local law debt)**
- Default, voluntary, or forced exchanges

ECB Policy Options



1. More Explicit Forward Guidance
2. Further Reduction in the Main Refinancing Rate
3. More LTROs
4. Credit Easing Options
5. Negative Deposit Rate
6. Actions to Prevent the Euro from Appreciating Further

Source: [Belated White Knight: ECB Policy Options for the EZ Recession and Credit Crunch](#) by Nouriel Roubini and Brunello Rosa, RGE, 24 May 2013

Political actions: incremental *muddle through*



1. **Germany's overall approach to remain gradual and cautious**
  - Adverse effects of reforms are acknowledged, but seen as necessary
  - Fiscal consolidation and reforms are believed to bring long term benefits
  - Germany will provide support, if the periphery moves in the right direction
2. **Relative stability through back door fiscal and monetary integration**
  - No explicit debt mutualisation and risk sharing possible for now
  - Partial reforms likely to calm financial markets, but bring more political risks
3. **Little risk from Germany's political front**
  - Compromise on SRM postponed, as politicians want to avoid opposition's criticism
  - Grand coalition would pursue more integration, but be stricter on banking rules

Source: [Germany Trip Report: Little Risk From Berlin](#), by Nouriel Roubini, Christian Odendahl and Brunello Rosa, RGE, 15 August 2013



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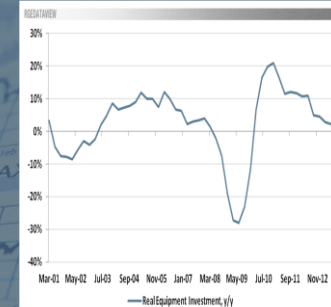
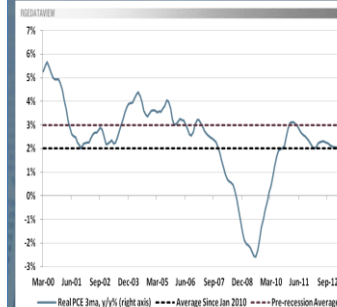
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US growth: elements to be cautious persist...



Consumer spending remains weak

Capex subdued on low final demand






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**Brunello Rosa**

Director, Western Europe, G10 Rates and Currencies

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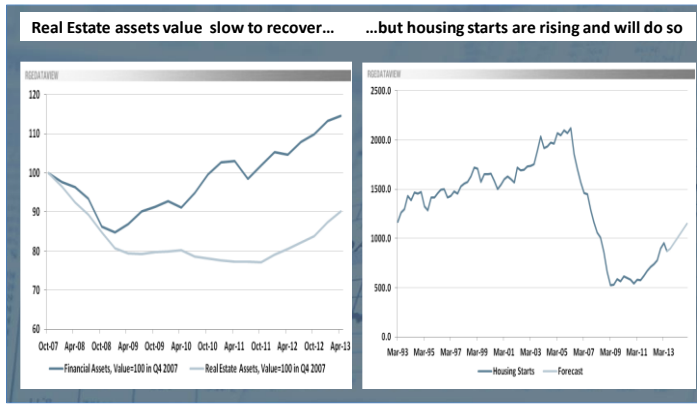
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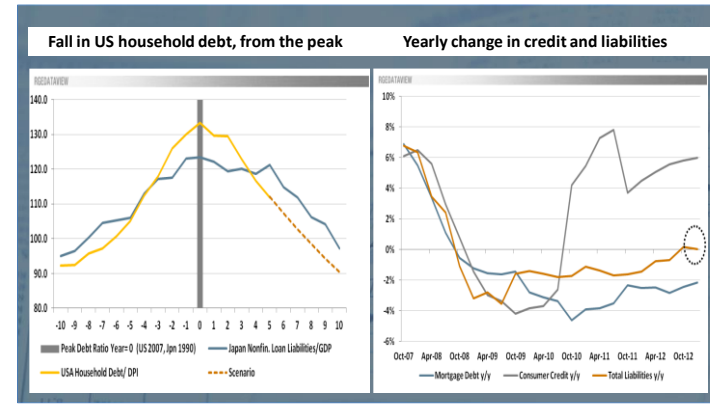
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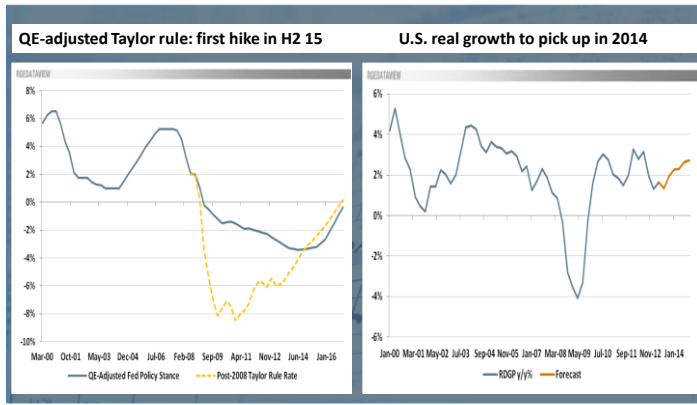
...But positive signs exist



... driven by good progress on household deleveraging



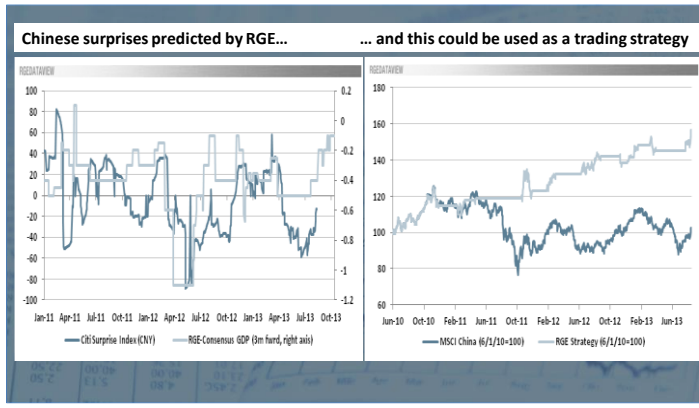
... and loose monetary policy



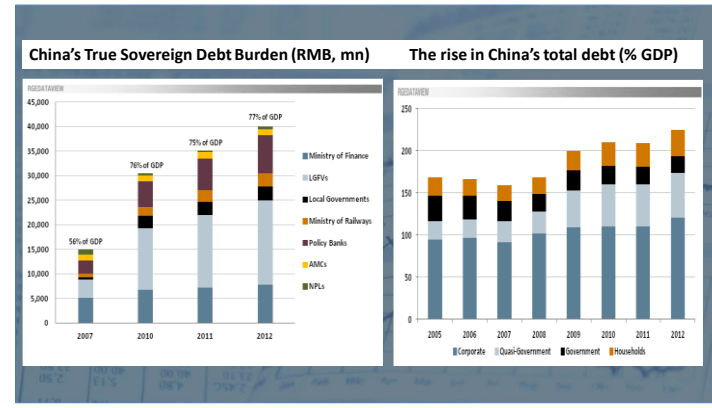
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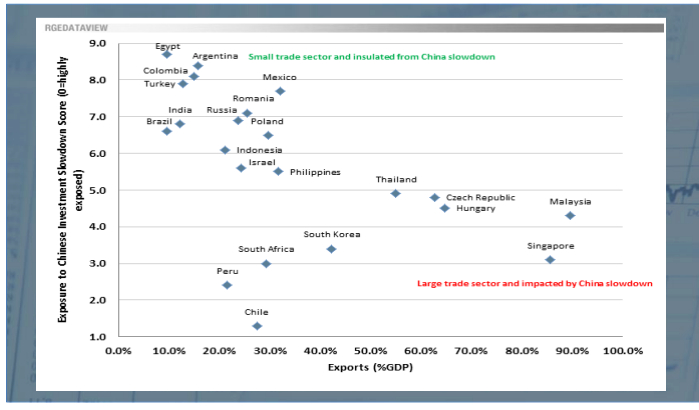
RGE projections: a good leading indicator



China's debt: a closer look



Impact of Chinese investment slowdown on EMs



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