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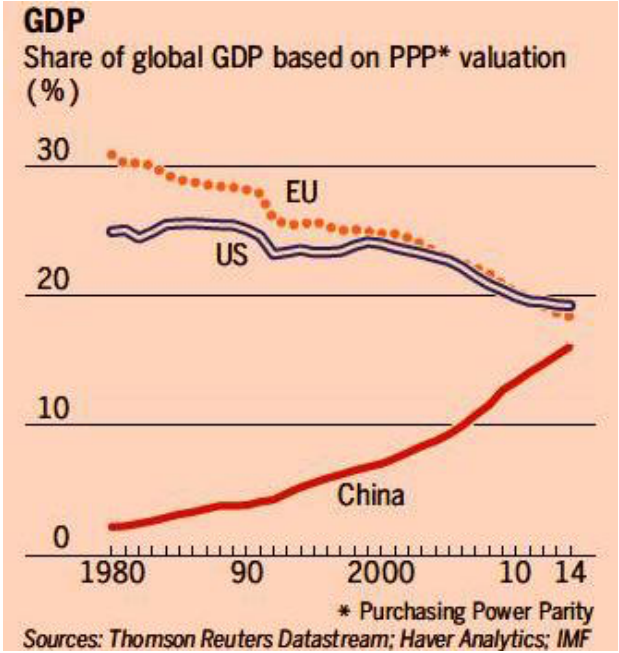
10 September 2015

Economic Tendencies and Challenges

Some Introductory Remarks
The World Economy
The European Economy
Oil prices – Effects on the Global Economy
More on Exchange Rates



Some introductory remarks

Income inequality becoming less acceptable politcally, remember Thomas Piketty.

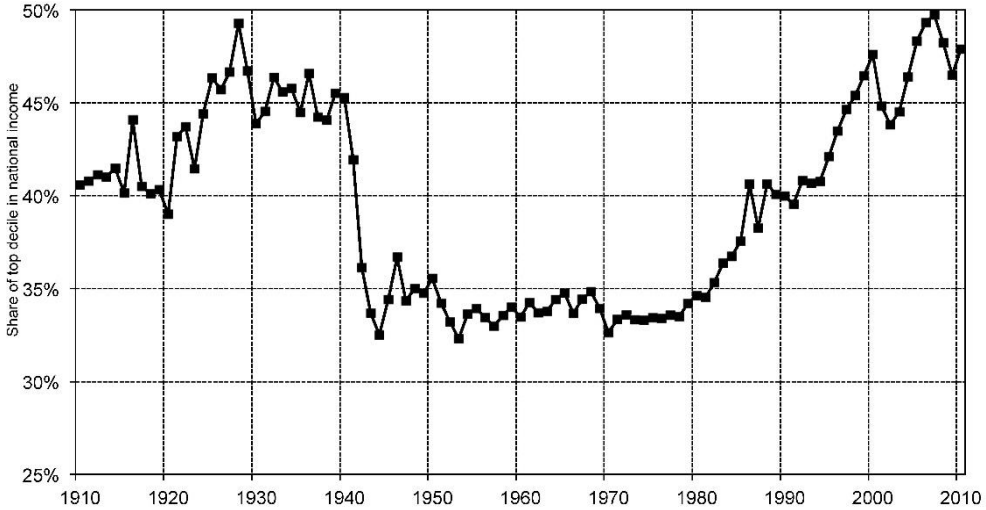
0.001 per ten thousand richest in the US,

0,5 % of total income in 1973,

up to 3,3 % in 2010,

i.e. almost seven times bigger a share.

Share of income to top ten percent 1910-2010, in USA



Øverste desilandel av USAs nasjonale inntekt falt fra 45-50% i perioden 1910-1920 til mindre enn 35% på 1950-tallet (dette er fallet dokumentert av Kuznets); deretter steg den fra mindre enn 35% på 1970-tallet til 45-50% i perioden 2000-2010. Kilder og data: se piketty.pse.ens.fr/capital21c.

….. some introductory remarks…

In Europe, how to deal with the challenge of refugees? Angela Merkel takes a bold stance.
Europe's values at stake.

In China, president Xi Jinping keeps fighting corruption, and have great plans,
i.e. the new Silk Road to link neighboring countries closer to China.
But is he short of legitimacy?

In Russia, Putin feels the heat of economic sanctions and halving of the price og oil,
but his popularity is soaring.

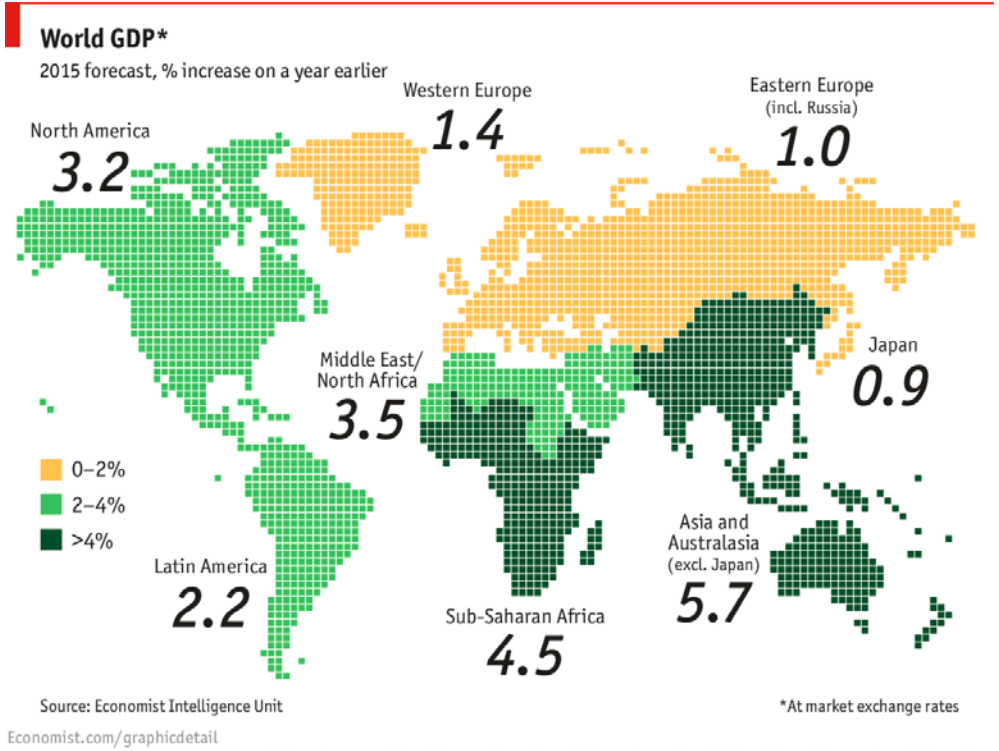
….. some introductory remarks…

In times of stress and upheavles (cf. changes in oil price,volatile exchange rates and refuges) it is hard to forecast with simple linear, economic models.

Comparing with earlier historic events can be quite useful,
i.e. price of oil halved in 1985, and the price stayed low for a decade and a half.

A final observation – both China and Russia want to establish relations with other countries, without USA being involved. A multipolar world they would like.

The World Economy



Source: The Economist

… the world economy …

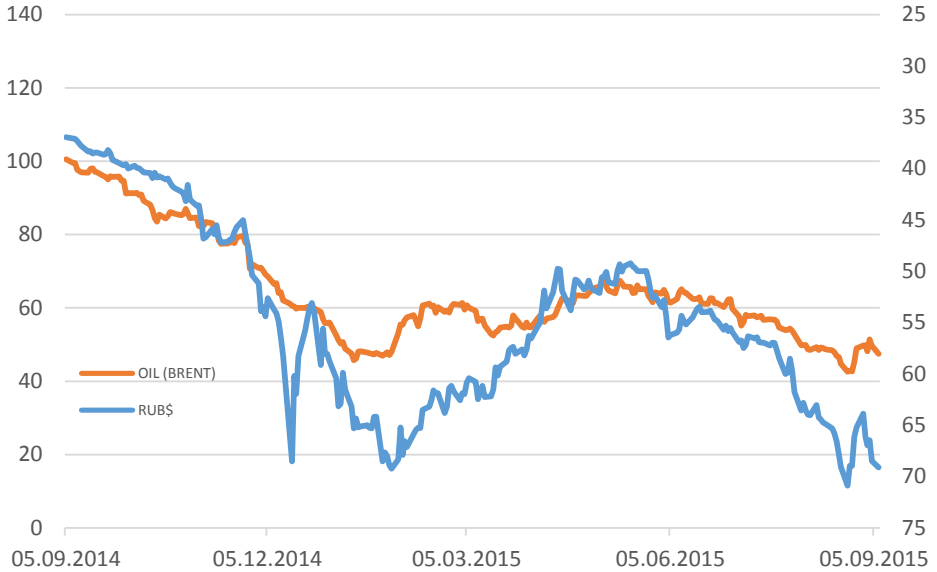
- World economy – single engine growth (USA) for the rich world, more than 3 % growth in 2015, positive sentiments.

- China will grow by less than 7 % in 2015, further down in 2016

  Mean Reversion, after having grown by about 10 % for more than 30 years

- IMF guesses 3,5 % world growth, whereas the World Bank 3,0 %.

Oil prices and the price of the rouble



Source: Datastream.

… the world economy …

Russia, minus 3.6 % economic growth 2015.

Putin not used the good years to restructure the economy

About 2/3 of exports was oil last year

And half government expenditures finances by oil

A very modest Sovereign Wealth Fund

Will the middle class stage a return?

Or will Putin put in place even more dramatic measures?

… the world economy …

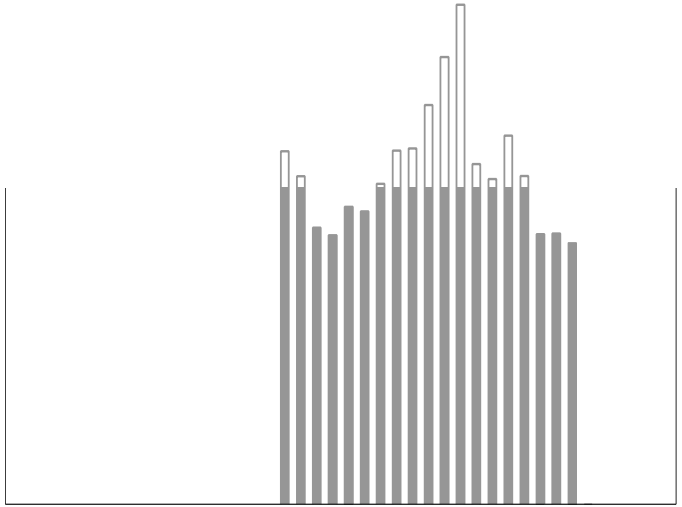
1978 – Deng Xiaoping in charge

1989 – Tiananmen Square, tanks against the students. China came to a standstill.

1992 – Deng's Southern Tour

2001 – Member of WTO

2012 – Xi Jinping takes over



Kilde: Swedbank

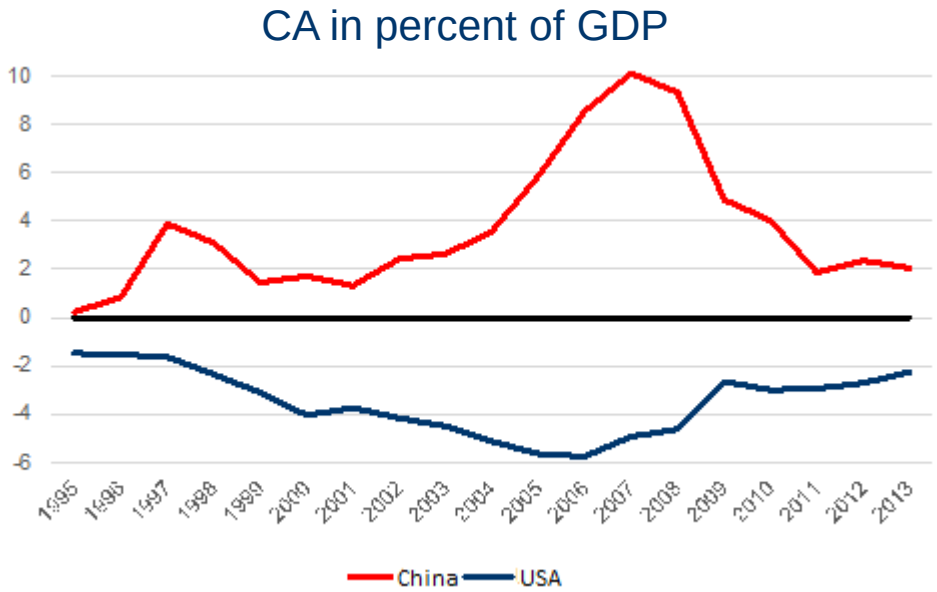
… the world economy …

China and the US – more balanced trade.

China uses her foreign reserves more actively in foreign affairs.

Silk road finance, to knit neighboring countries closer to China.

China invests in Africa and Latin-America.



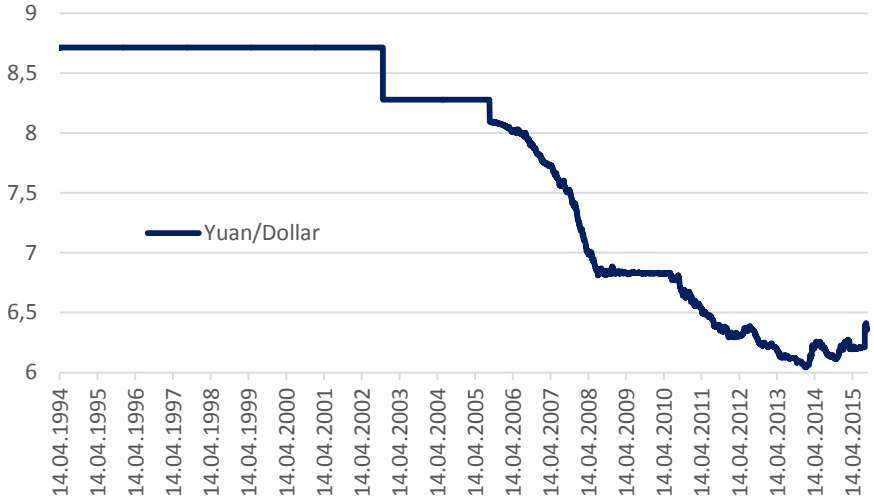
Kilde: WorldBank

… the world economy …

China keeps a tight rein on the exchange rate. Only gradually allowing capital to flow freely in and out of China.

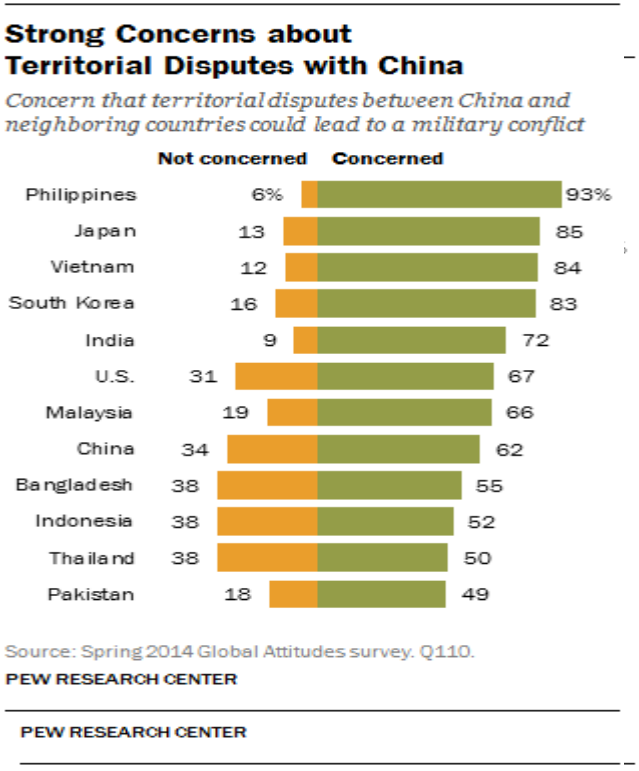
But increasingly using RMB for transactions on the trade account – to be free from the dollar.

Price of USD in terms of Chinese yuan



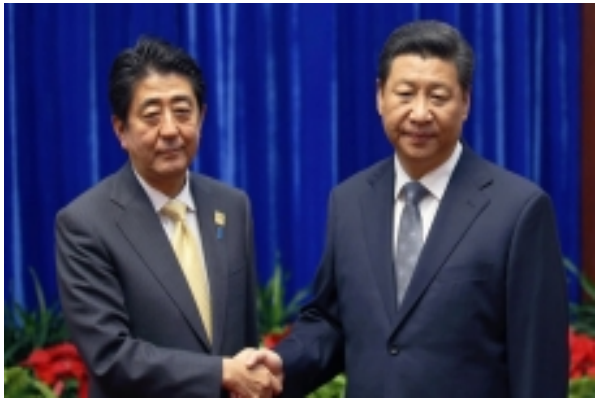
Kilde: Datastream

… the world economy …



China short of soft power.

The friendly couple?



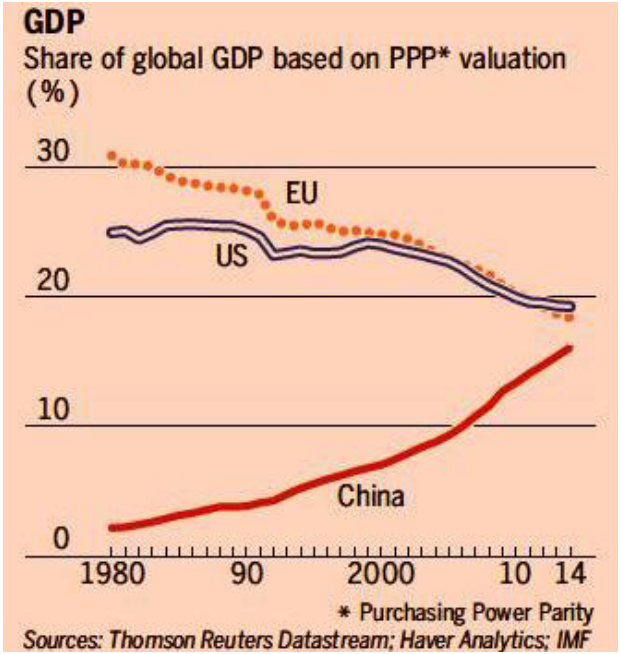
… the world economy …

EU, USA and China close to equal shares of world GDP

Demography and innovation – USA best. Also, a robust political system, although sometimes one doubts

In China, number of people in working age on the decline. Will China keep growing so fast? Middle Income Trap a danger? From Made in China to Invented in China, does that require a more open society?

Europe also getting older faster than America. The problems with the euro are far from solved. Need a better mechanism for rescheduling debt.



… the world economy …

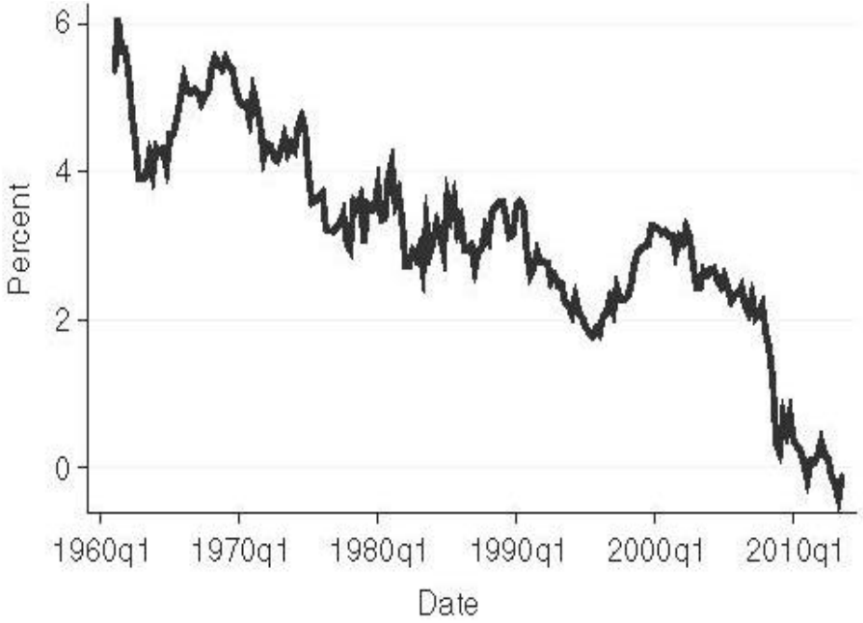
Real rate of interest that equilibrates aggregate demand and supply at full employment declining steeply

- Declining rate of population growth
- Change in income distribution, and savings on the increase
- Modest productivity growth

Low interest rate for many years

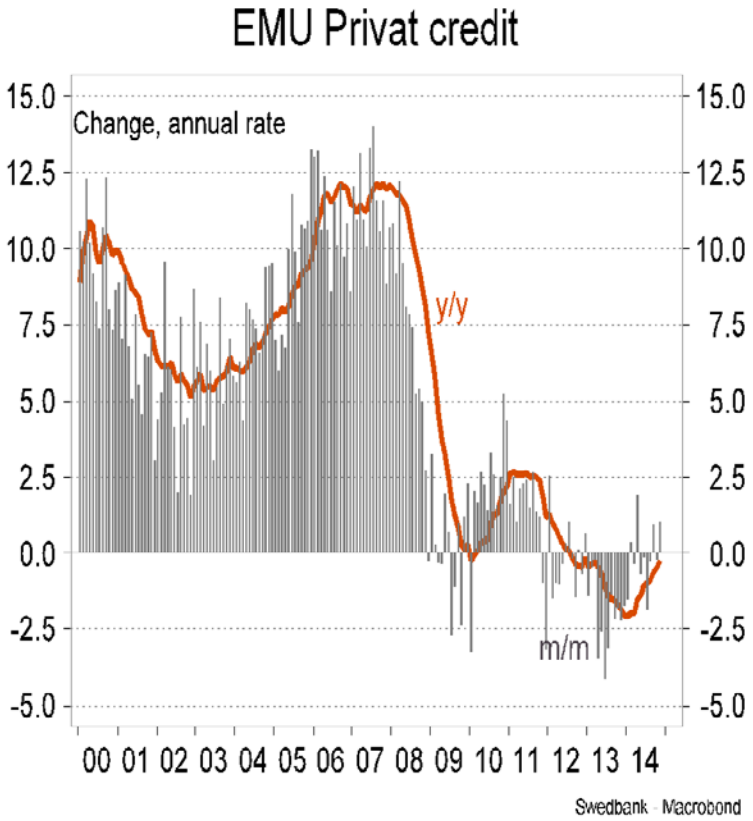
USA – raising interest rates later this year?

Natural Real Rate of Interest in USA



The European Economy

- ECB will buy for 60 bn euro a month in government bonds for 19 months.
- Easing of credit to banks, will it be followed by increased bank lending to business?
- General point: Need debt restructuring, i.e. debt being written down.



Kilde: Swedbank

… the European economy …

1999-2008 No DEM to appreciate, and trade surpluses with other euro countries (red)

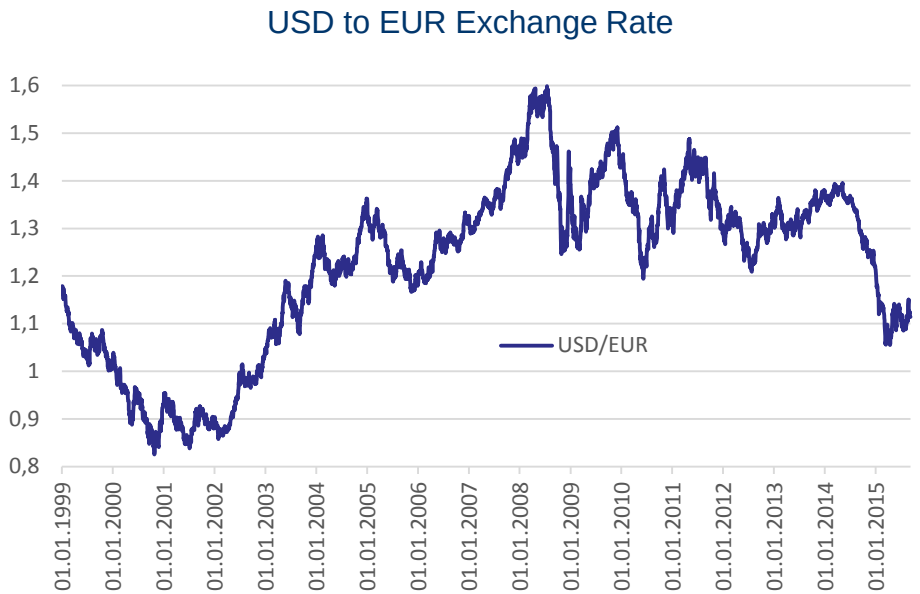
2008 – 2014 Germany's surplus with euro area evaporates. Why?

Merkel: Other euro countries need to improve competitiveness. Would help if Germany inflated a bit more.

Kilde: Swedbank

… the European economy …

Jan 1999, 1 euro = 1,18 dollar
Nov 2000, 1 euro = 0,83 dollar
July 2008, 1 euro = 1,60 dollar
These days, 1 euro = 1,12 dollar

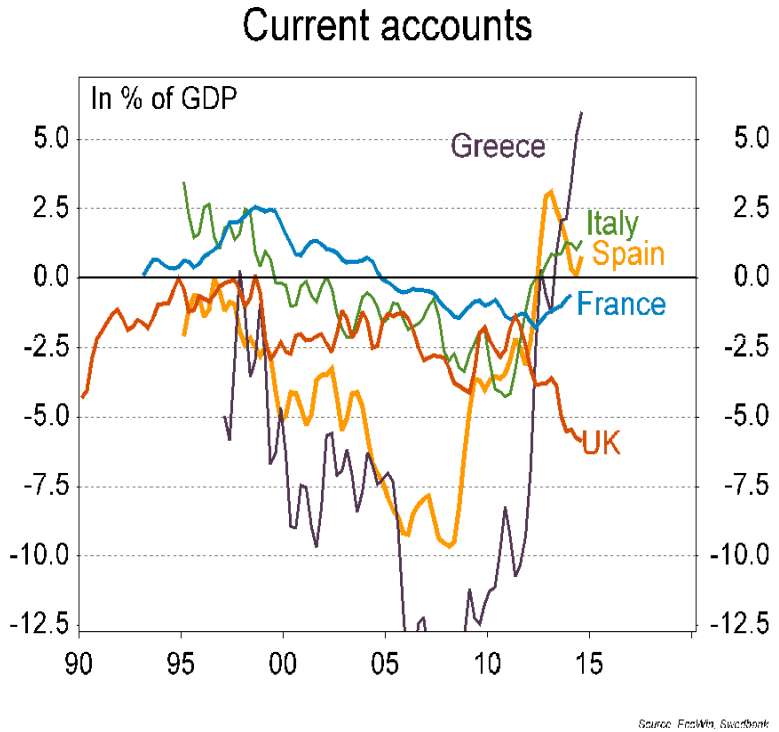


Kilde: Datastream

… the European economy …

Finally, Greece is in the black on her current account, i.e. exports exceed imports. Why?

Not because export have picked up, but because imports are down



Kilde: Swedbank

… the Europan economy…

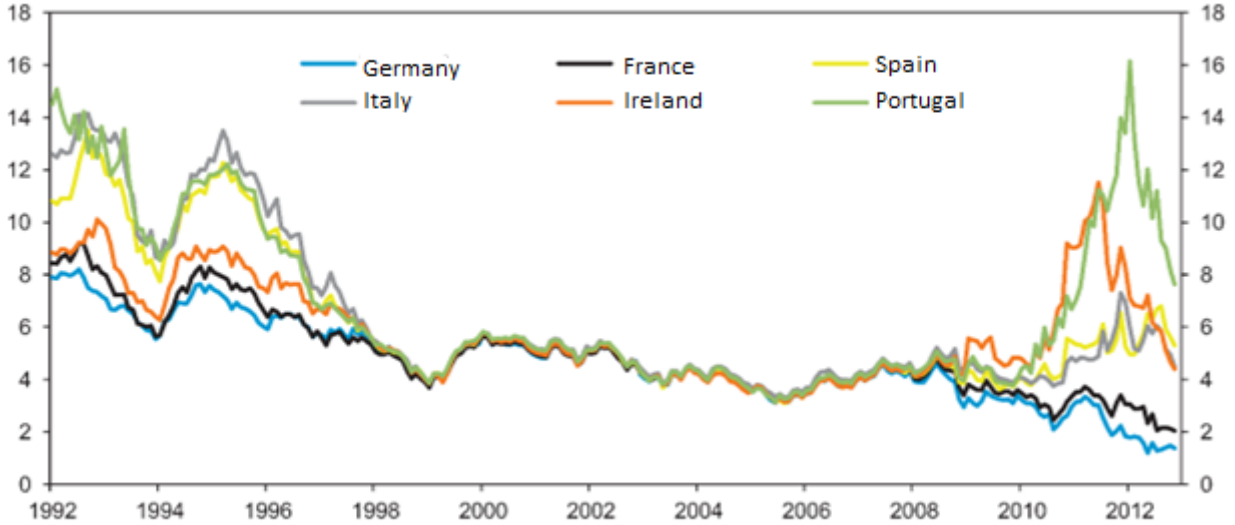
Grexit next?

The Greek people wants to keep the euro
But need to write off about half of government debt
Why is that a problem?

Can a country go bankrupt?

… the European economy …

Ten-year government bonds



… the European economy …

	2007	2015
Public debt eurozone	73 %	108 %
Net interest payment	2.5 %	2.2 %

Debt is almost doubled.

But less demanding to serve.

Jean-Claude Juncker, head of the Commission in EU:

We know what it takes. But doing it, and you will not be re-elected.

Kilde: SSB og finansdepartementet

Oil prices – Effects on the Global Economy

Price of oil down 30 %, and world GDP increases by ½ % first year. Why?

- Cheaper inputs
- Income redistributed and aggregate demand increases

….. oil prices …

Improve public finances by taking away domestic subsidies on fuel (India), or raising tax on gasoline (only 5 cents per liter, since 1993, in USA), i.e. let the price at the pump decrease a bit less than the price of crude oil. But seems not to happen.

Lower oil prices, good for growth (in importing countries).

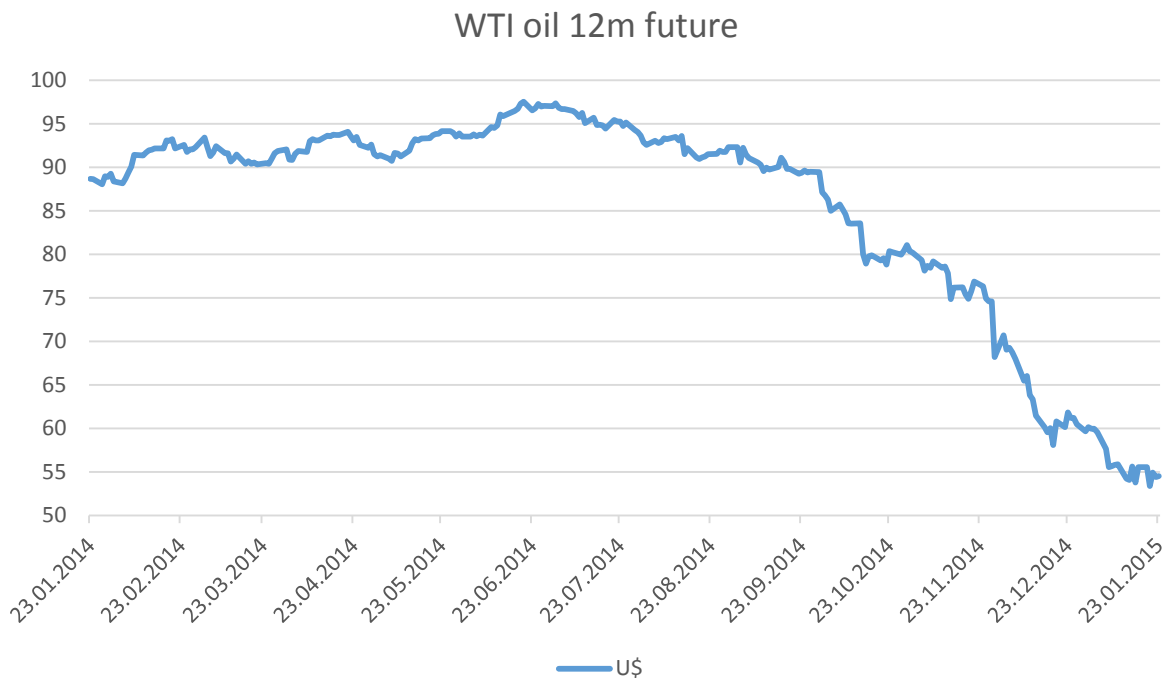
….. oil prices…

Shale production based on fracking, costs about 50 dollars per barrel. Sort of marginal global costs. Small scale production. Price on oil futures, 90 dollar in 2020.

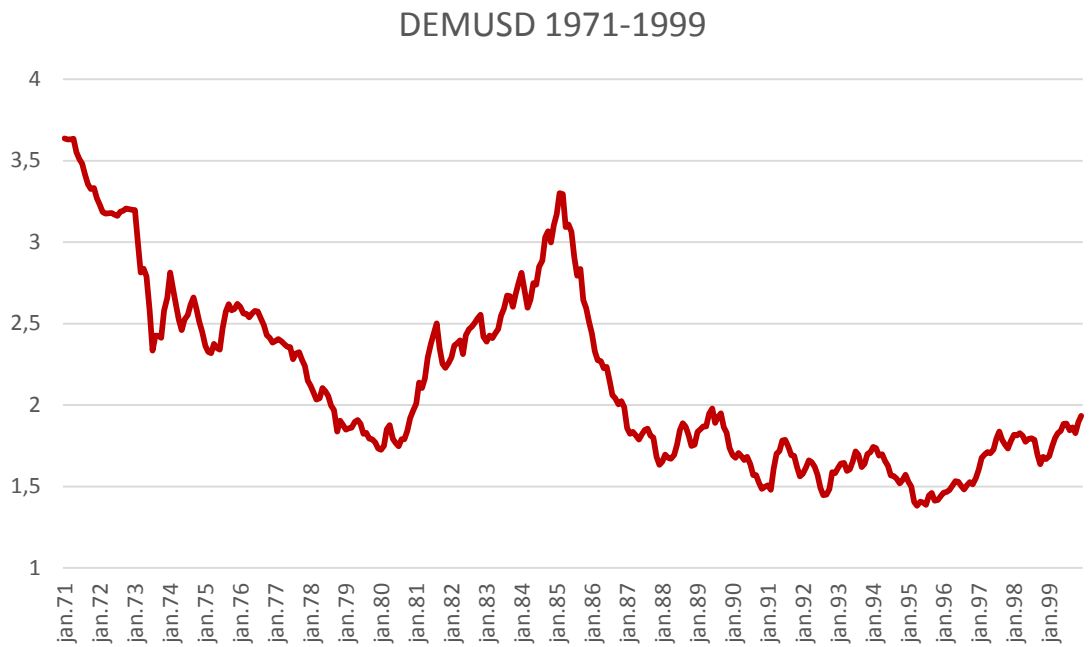
Saudi-Arabia wants the world to believe that their optimal price in the long run is signficantly lower than 60 dollar. Must keep the price below 60 dollar for some time. 1985-86 experience, and the price stayed down for almost 15 years

Hard to calculate an equilibrium price for a cartel.

Oil futures prices



More on Exchange Rates



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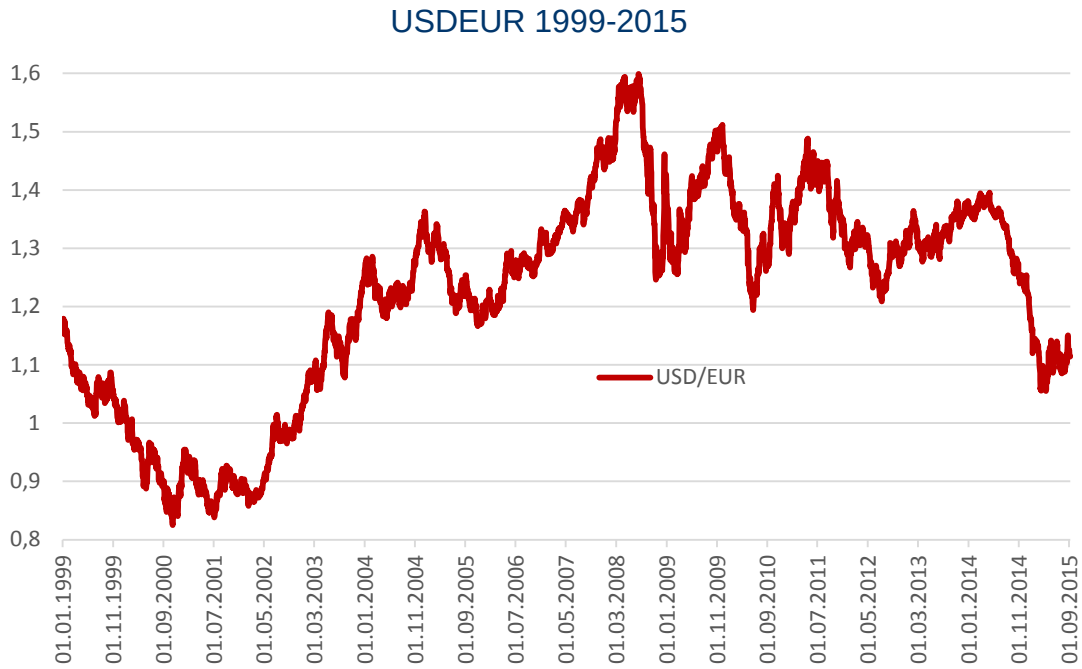

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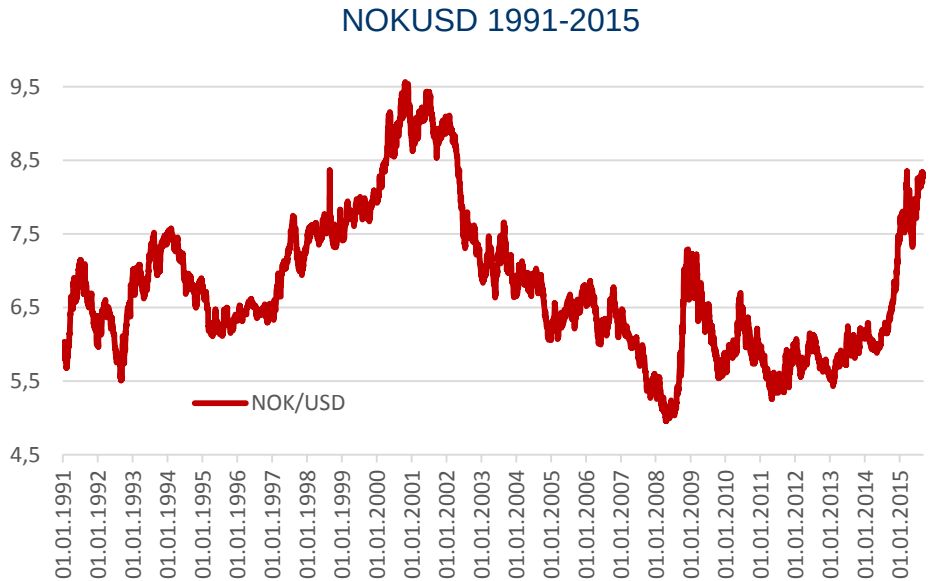

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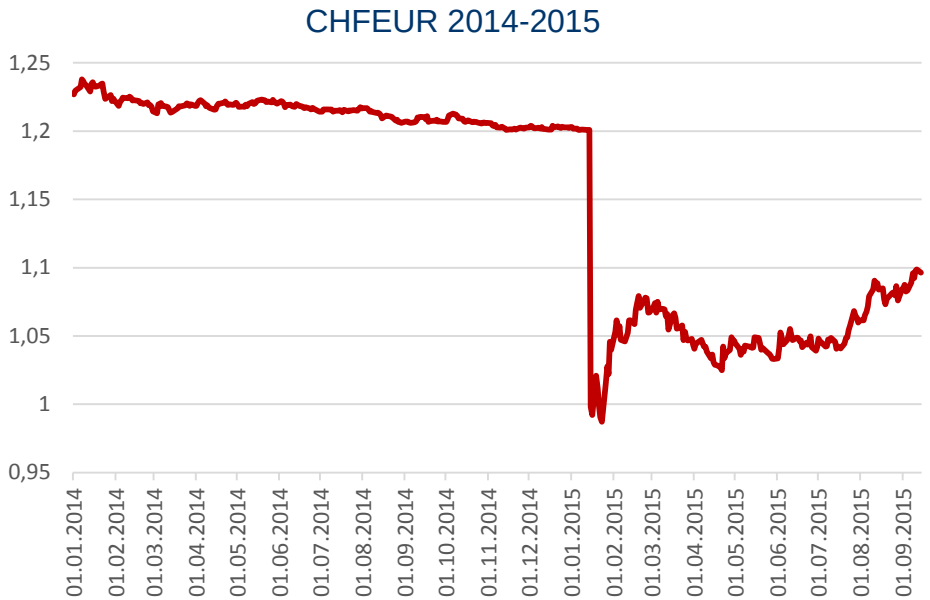
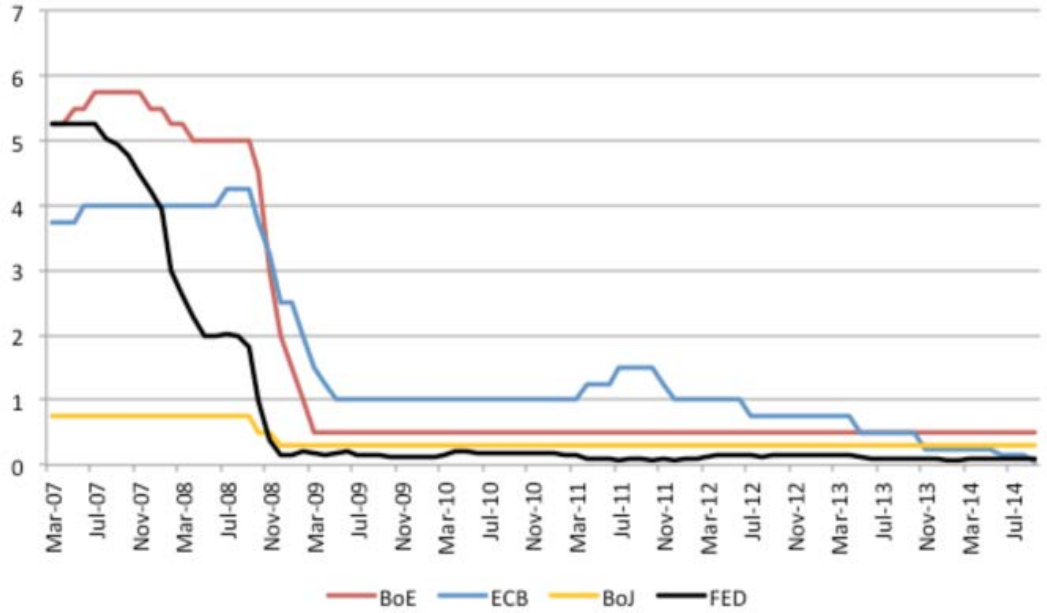


Policy rates of four major central banks



Must China rewrite the past to control the future?
Does America work that well?
Europe at the mercy of Greece?