



Our Perspectives:

Commentary on the economy & regulatory policies affecting financial companies

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The Longbrake Letter*

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In this month's letter, I include a final assessment of observations I made a year ago about how the U.S. and global economies might fare in 2015. You will find that I got some things right and many things wrong. The U.S. and global economies are dynamic and ever changing. Some trends are foreseeable. But, governmental policy intervention, whether it be political or economic, can alter outcomes and set in motion feedbacks that significantly affect economic developments. In this respect, 2015 was no different from any previous year.

Such will also be the case in 2016. Nonetheless, I once again attempt to summarize key U.S. and global economic developments that seem possible, perhaps likely, in 2016. I also list risks to the 2016 outlook.

I wish all a very joyous holiday season!

*The information contained in this newsletter does not constitute legal advice. This newsletter is intended for educational and informational purposes only.

I. Outlook — 2016 and Beyond

Observations about the 2015 U.S. and global economic outlook and risks to the outlook were contained in the *December 2014 Longbrake Letter* and are included below without any changes. As events unfold during 2015, this will enable the reader to track my analytical prowess. Current assessments follow each item with the following identifiers: “+” **tracking forecast**; “-” **not tracking forecast**; “?” **too soon to know**. As events unfold during 2015, this will enable the reader to track my analytical prowess.

As the year progresses, actual results for many economic Indicators diverged from beginning-of-the year forecasts, as evidenced by the large amount of red ink, “not tracking,” below. In addition, many of the risks have materialized. On balance, U.S. and global economic activity is a little less strong than expected and deflationary risks have increased. These developments are being reflected in tighter financial conditions and increased financial market volatility.

1. U.S.

- **2015 real GDP Y/Y** growth projections range from 2.7% to 3.5%. The FOMC’s central tendency Q4/Q4 projections range from 2.6% to 3.0%. (Q4/Q4 projections are highly dependent upon potential anomalies in Q4 data; therefore, Y/Y estimates, which average all four quarters, are more stable estimates.) Because the substantial decline in oil prices is likely to boost consumption growth more than it depresses investment growth, actual 2015 real GDP growth is likely to be at the high end of the forecast range.
 - *The FOMC has changed its Q4/Q4 GDP projection range several times during the year; based on the December projections, the FOMC now expects growth in 2015 to be 2.1%*
 - *Other Y/Y forecasts are also below the lower end of the original forecast range: GS = 2.5% (Q4/Q4 = 2.2%); B of A = 2.5% (Q4/Q4 = 2.1%); Bill’s Steady scenario = 2.5% (Q4/Q4 = 2.3%); Bill’s Strong scenario = 2.5% (Q4/Q4 = 2.3%)*
- **Real GDP output gap** will remain high, but will close rapidly during 2015 from about 3.4% to 2.0%. (The exact size of the output gap will be revised by CBO, probably in February 2015).
 - * *CBO revised the output gap down by 1.1 percentage points in February but then raised it by 0.5 percentage points in August for a net reduction of 0.6%*
 - *Revised output gap should decline to about 2.6% by the end of 2015, which would be a 0.7% decline over the year; this is considerably less than the forecast 1.4% decline at the beginning of the year*
- **Potential structural rate of real GDP growth** has declined significantly in recent years. I expect potential growth to be about 2.0% in 2015. Long-term potential real GDP growth will edge up in coming years to between 2.0% and 2.3%.
 - * *CBO reduced 2015 potential growth from 1.79% to 1.66%*
 - *Potential growth for my scenarios for 2015 is 1.55%*

+ Long-run potential growth for my scenarios is between 1.8% and 2.1%; it is 1.75% for GS and 2.0% for B of A; it is between 1.8% and 2.2% for the FMOC; and it is 2.1% for CBO; all estimates of long-run potential growth edged down during the year

- **Productivity** should rise during 2015 as growth improves and investment increases, but should still fall well short of the historical 2.1% average.

+ The four-quarter change in productivity rose from 0.0% in the fourth quarter of 2014 to 0.6% in the third quarter of 2015

- **Employment** growth should slow during 2015 as full employment approaches and grow about 185,000 per month.

- Payroll growth was stronger than expected, averaging 210,000 monthly over the first eleven months of 2015

- **Employment participation** will rise slightly during 2015 as the unemployment rate falls, labor market conditions tighten and discouraged workers find jobs. These cyclical factors will more than offset the downward pressure on the participation rate stemming from an aging population.

- The participation ratio has declined; it was 62.70% in December 2014 and 62.48% in November; more retirees and fewer prime-age individuals were employed than expected

- **Unemployment rate** should edge down to about 5.25%. A higher rate could occur if substantial numbers of discouraged workers re-enter the labor force.

+ The unemployment rate fell from 5.56% in December 2014 to 5.05% in November; employment growth has been stronger than expected while labor force growth and participation have been weaker

- **Nominal consumer disposable income**, measured on a Y/Y basis will rise about 3.2% (roughly 1.2% increase in hours worked; 1.8% increase in CPI inflation and 0.2% increase in the annual rate of growth in the hourly wage rate — *note: this relationship is mischaracterized because inflation does not factor directly into disposable income growth; disposable income growth is a composite of many sources of income, the largest of which is wage and salary income; growth in salary and wage income depends upon growth in total hours worked and growth in nominal hourly wages, which was 2.1% at the beginning of 2015 and forecast to rise to 2.3% by the end of 2015*).

- 12-month rate of change in disposable income was 4.1% through October; (total hours worked for all employees grew 1.9% through November; growth in hourly nominal wages was up slightly through November to a 2.2% annual rate of increase); growth in hours worked is much stronger than forecast which has resulted in stronger than expected growth in nominal consumer disposable income

- **Nominal consumer spending growth** on the Y/Y basis will grow slightly faster at approximately 3.5%, but could grow slightly faster if low oil prices persist.

+ 12-month rate of change was 3.2% through October

- **Household personal saving rate** will decline slightly as growth in spending exceeds growth in disposable income.

- *Saving rate averaged 5.19% over the first ten months of 2015 compared to 4.80% in 2014 as income growth outpaced consumption growth*
- **Stock prices**, as measured by the S&P 500 average, should rise between 0% and 5%.
 - + *Through December 17, stock prices were down 0.8%*
- **Manufacturing** growth will continue to be relatively strong and the PMI index will exceed 50.
 - *The ISM manufacturing index softened considerably during the course of 2015 and was 48.6 in November, which indicates declining growth*
 - + *The ISM nonmanufacturing services index remained strong during 2015, but eased to 55.9 in November compared to a peak of 60.3 in July*
- **Business investment** spending growth should remain relatively strong in a range of 4% to 6% as employment and consumer spending growth gather momentum; however, low oil prices will depress energy investment.
 - *Business investment rose at an annual rate of 2.7% over the first three quarters of 2015; forecasts for 2015 have been lowered to 3.1%*
- **Residential housing investment** should improve over 2014's disappointing level by 8% to 10%; residential housing starts should rise 15% to 20%.
 - + *Residential investment grew at an annual rate of 8.9% over the first three quarters of 2015; forecasts for 2015 range between 8.5% and 9.1%*
 - *Over the first eleven months of 2015 total housing starts were 10.1% above and single-family housing starts were 9.1% above the 2014 level and show grow 10% during 2015, short of the 15% to 20% forecast*
- **Residential housing prices** should rise about 2% to 4% in 2015, more slowly than 2014's projected 4.5% increase.
 - *According to the Federal Housing Finance Agency's home purchase price index, housing prices rose 5.07% in 2014 and 5.70% through the 12 months ending September 2015; prices are on track to rise 4.0% or more in 2015*
- **Trade deficit** should be slightly higher in 2015 as economic growth improves growth in imports and the rising value of the dollar depresses growth in exports. The **dollar's value** on a trade-weighted basis should continue to rise.
 - + *The trade deficit for goods rose slightly; it was 2.89% in December 2014 and 2.91% in October*
 - + *The trade weighted value of the dollar rose 11.6% from December 2014 through November and was 13.5% higher than November 2014*
- **Monetary policy** — the Federal Reserve will raise the federal funds rate at its June, or possibly, September 2015 meeting. Because inflation is likely to continue to fall short of the Federal Reserve's expectations, the pace of increases in the federal funds rate is likely to be slow.
 - *The FOMC raised rates at its December meeting*

- **Total inflation** measures (CPI and CPE) will fall sharply during the first half of 2015, reflecting the significant decline in oil prices. **Core PCE inflation** will be stable to slightly lower in a range of 1.3% to 1.5%, reflecting global disinflationary trends. Core PCE inflation will remain well below the FOMC's 2% objective at least through 2017.

+ Total CPE was up 0.2% in October compared to October 2014 and is projected to rise only to 0.7% for all of 2015

+ The annual rate of change in core PCE was 1.28% in October and should be within the forecast range at the end of the year

- The **10-year Treasury rate** is likely to fluctuate in a range between 2.0% and 3.0% in 2015. Faster than expected real GDP employment growth will push the rate toward the top end of the range; greater than expected declines in inflation and/or heightened financial instability will push the rate toward the bottom end of the range.

+ The 10-year Treasury rate was 2.24% on December 17; because of low rates globally and aggressive quantitative easing by the European Central Bank and the Bank of Japan

- **Fiscal policy** will have limited impact on real GDP growth during both fiscal year and calendar year 2015. The deficit as a percentage of nominal GDP will probably decline from fiscal year 2014's level of 2.75% to 2.50%. The decline could be greater if economic growth and tax revenues exceed expectations or less if Congress increases spending without offsets as it did in approving the tax extenders bill for 2014.

+ The 2015 fiscal year deficit was \$436 billion and was 2.46% of fiscal year 2015 nominal GDP

- **State and Local investment** spending growth rises slightly from 0.5% in 2014 to 1.0% in 2015, which is still well below the long-term average of approximately 1.4%.

- State and local investment rose at an annual rate of 2.0% over the first three quarters of 2015; forecast for all of 2015 is 1.5%

2. Rest of the World

- **Global growth** is likely to improve to 3.7% in 2015 from 3.2% in 2014. Risks are tilted to the upside because of the substantial decline in oil prices.

- 2015 Global growth forecasts have been lowered to 3.1%; improvement in Europe has been more than offset by slower growth in China, Japan, the U.S. and emerging markets

- **European growth** will be positive but will likely fall short of the consensus 1.2%.

- Europe's growth forecast has been raised to 1.5%

- **European inflation** will continue to decline and may even turn into outright deflation. Quantitative easing, assuming it occurs, may be too late and have too limited an impact to deflect emerging deflationary expectations. Europe may well be headed to the kind of deflationary trap Japan has been in for the last 20 years.

+ Consumer prices in Europe are expected to rise only 0.1% during 2015

- **European financial markets** may face renewed turmoil. Markets expect the ECB to begin purchasing large amounts of securities, including sovereign debt, by March. This presumes that legal hurdles and German opposition will be overcome. Assuming that quantitative easing actually occurs, its impact is likely to disappoint.
+ The ECB's massive bond purchase initiative provided a stable backdrop for financial markets; however, volatility emerged from time to time (during the spring when speculative positions, which had driven interest down to nearly zero, were unwound; in June in conjunction with the crisis in Greece, followed in August by China's growth slowdown); credit conditions have eased
- **European political dysfunction, populism and nationalism** will continue to worsen gradually. Countries to watch include the U.K., Greece, Spain, Italy and Portugal.
+ the National Front party is gaining ground in France but did not win political in any region in the December elections; recent regional elections indicate that centrist parties may lose the Spanish elections scheduled for late 2015; the Conservative Party won an outright majority in the UK parliamentary elections but political fragmentation grew as the Scottish National Party won 56 seats; terrorism and the refugee crisis is exacerbating political pressures on centrist parties
- **U.K. growth** is expected to slow from 3.0% in 2014 to 2.6% in 2015; however, political turmoil, should the May parliamentary elections be inconclusive, could drive growth lower.
+ Expected 2015 real GDP growth is expected to be 2.4%, slightly below the expected level
- **China's GDP growth** will slow below 7% and gradually move toward 6% as economic reforms are implemented and the shift to a consumer-focused economy gathers momentum.
+ Year over year growth in the third quarter of 2015 was 6.9%; growth is headed down toward 6.5%
- **China's leadership** will focus on implementing **economic reforms** and will overcome resistance and maintain stability.
+ Chinese reform policies are being implemented more slowly than expected; the anti-corruption campaign continues and has had a chilling impact on speculation in commodities; in spite of stock market turmoil during the middle of the year, political stability has been maintained
- **Japan's** economic policies may be successful in defeating deflation, but GDP growth will be hard pressed to achieve the expected 1.6% rate in 2015 if Abenomics' third arrow of economic reforms fails to raise the level of potential growth sufficiently to overcome the effect of negative population growth on labor force growth.
+ Japanese expected growth has been lowered to 0.7%; the Bank of Japan is likely to fall short of its goal to raise inflation to 2.0% expected inflation currently is 0.5% for 2015 and is expected to be 1.0% for 2016
- **India** should experience an improvement in real GDP growth to 6.3% in 2015.
+ 2015 growth is expected to equal 7.4%
- **Emerging market countries** that are energy consumers will experience greater growth, as long as the U.S. does better in 2015; energy producing countries and those heavily dependent upon commodities exports for growth will do less well.

+ Data indicate that slower growth in China, Japan and the U.S. is dragging down growth in emerging markets

3. **Risks** — stated in the negative, but each risk could go in a positive direction.

- **U.S. potential real GDP growth** falls short of expectations
 - + Reductions in estimates of long-run potential GDP growth by CBO, FOMC and other analysts indicate this risk has been realized*
- **U.S. employment growth** is slower than expected; the **participation rate** is stable or declines rather than rising modestly
 - + Participation rate has fallen slightly*
 - Employment growth was slightly above the expected level*
- **U.S. hourly wage rate growth for all employees** does not rise materially over its 2014 level of 2.1%
 - + Through November this risk is being realized — wage growth, measured as a 12-month year over year rate of change, has edged up from 2.06% to 2.19%; the employment cost index has declined from 2.25% to 1.88% over the first three quarters of 2015*
- **U.S. unemployment rate** falls less than expected
 - The unemployment rate fell slightly more than expected and was 5.05% in November*
- **U.S. productivity** remains low in the vicinity of 1%
 - + Productivity over the last 12 months has been 0.6%*
- **Real U.S. consumer income and spending** increase less than expected
 - Consumer disposable income rose more than expected, while the increase in consumer spending was slightly less than expected*
- **U.S. financial asset prices** rise more than expected posing increased bubble risks
 - Bond prices are at the low end of the expected range*
 - Stock prices changed little during 2015*
- **Growth in U.S. residential housing investment and housing starts** is less than expected
 - + Housing starts were below expectations*
 - Residential investment met expectations*
- **U.S. residential housing price increases** slow more than expected
 - Home prices rose more than expected*
- **U.S. private business investment** does not improve as much as expected
 - + Private business investment growth is expected to be below the lower end of the forecast range*
- **Oil price declines** in the U.S. trigger bankruptcies and cause tight financial conditions with negative implications for economic activity and growth
 - + Energy-related investment reduced real GDP growth during the first half of 2015 by about 0.5%*

? Evidence is building, primarily in the junk bond market, that trouble is brewing; however significant financial market disruptions stemming from the fall in oil prices did not occur during 2015

- **U.S. manufacturing growth** slows as the value of the dollar rises and global growth slows
 - + *ISM manufacturing index fell below 50, indicating contraction*
- **U.S. trade deficit** widens and the **value of the dollar** rises more than expected
 - + *The value of the dollar has risen more than expected at the beginning of the year*
 - *The trade deficit has been relatively stable*
- **U.S. monetary policy** spawns financial market uncertainty and contributes to financial instability
 - + *Volatility increased during the year and financial conditions are the tightest they've been in four years*
- **U.S. inflation** falls, rather than rising, and threatens deflation
 - + *Core PCE inflation has been slightly softer than expected and with recent further declines in commodity prices and a stronger dollar is unlikely to rise by year end*
- **U.S. interest rates** fall or rise more than expected
 - *Long-term interest rates ended the year at the lower end of the expected range*
- **U.S. fiscal policy** is more restrictive than expected and the **budget deficit** falls more than expected
 - + *Tax receipts have been stronger than expected; the deficit was slightly lower than originally expected; Congress enacted spending and tax measures that will boost GDP growth in 2016*
- **U.S. state and local spending** does not rise as fast as expected
 - *Through the first three quarters of 2015 state and local spending has risen faster than expected*
- **Global GDP growth** does not rise as fast as expected
 - + *The 2015 global GDP growth forecast was reduced from 3.7% to 3.1%*
- **Europe** slips back into recession
 - *Growth improved in Europe because of the decline in the value of the euro, lower commodity prices, easier financial and credit conditions, and less fiscal drag*
- **ECB** does not engage in quantitative easing or the quantitative easing program it decides to pursue lacks market credibility
 - *This risk did not materialize because the ECB initiated a massive quantitative easing program which will continue until March 2017*
- **Europe** — financial market turmoil reemerges
 - *Speculation drove interest rates on long-term bonds too low in the spring; this was followed by a short but relatively violent correction; since then interest rates have declined in a more orderly fashion*

- **Europe** — political instability and social unrest rises more than expected threatening survival of the Eurozone and the European Union
 - *Political fragmentation built slowly during 2015 but developments do not yet threaten the survival of the Eurozone and the European Union; the Greek threat was contained, but could explode again in the next few months as the Greek economy remains mired in recession; terrorism and the refugee crisis is contributing to nascent political instability*
- **Acute political turmoil** engulfs the U.K.
 - *The Conservative Party won an outright parliamentary majority and political stability is the order of the day for the time being; however, political fragmentation is increasing slowly*
- **Chinese** leaders have difficulty implementing **economic reforms**
 - + *Implementation of reforms is proceeding more slowly than expected; at least one of the reforms involving opening up participation in the stock market led to a rapid escalation in prices followed by a crash in prices and extreme volatility*
- **China's growth** slows more than expected
 - + *Growth has slowed to 6.9% and is expected to fall to 6.0% in 2016*
- **Japan** — markets lose faith in Abenomics
 - ? *This risk has not materialized; however, both real growth and inflation have been considerably less than expected, the Bank of Japan surprised markets on December 18 with an announced intent to increase bond purchases during 2016*
- Severe and, of course, unexpected **natural disasters** occur, which negatively impact global growth
 - *This risk did not materialize*

II. Outlook — 2016 and Beyond — Forecast Summary for the U.S. and the Rest of the World, Highlights of Key Issues, and Identification of Risks

Observations about the 2016 U.S. and global economic outlook and risks to the outlook are listed below. As events unfold during 2016, this will enable the reader to track my analytical prowess.

1. U.S.

- **2016 real GDP Y/Y** growth projections range from 2.3% to 2.5%. The FOMC's central tendency Q4/Q4 projections range from 2.3% to 2.5%. (Q4/Q4 projections are highly dependent upon potential anomalies in Q4 data; therefore, Y/Y estimates, which average all four quarters, usually are more stable estimates.) Risks are tilted to the upside because of the substantial federal tax reductions and spending increases Congress enacted at the end of 2015.
- **Real GDP output gap** will remain high, but will close rapidly during 2016 from about 2.6% to 2.0%. (The exact size of the output gap will be revised by CBO, probably in February 2016; I expect CBO to reduce the size of the gap).
- **Potential structural rate of real GDP growth** has declined significantly in recent years. I expect potential growth to be about 1.4% in 2016. Long-term potential real GDP growth will edge up in coming years to between 1.8% and 2.1%.
- **Productivity** should rise during 2016 as growth improves and investment increases, but should still fall well short of the historical 2.1% average.
- **Employment** growth should slow considerably during 2016 as full employment is reached and slow growth in the labor force becomes binding; payroll growth should average 130,000 to 165,000 per month.
- **Employment participation** will be relatively stable during 2016 as labor market conditions tighten and discouraged workers find jobs, offsetting the demographically-embedded decline stemming from retirements of baby boomers.
- **Unemployment rate** should edge down to between 4.6% and 4.8%.
- **Nominal consumer disposable income**, measured on a Y/Y basis should slow as employment growth slows; this will be offset partially by an increase in average hourly wage rates; growth should be in a range of 2.2% to 2.5%.
- **Nominal consumer spending growth** on the Y/Y basis will relatively stable in a range of 3.3% to 3.5% at approximately 3.5%.
- **Household personal saving rate** will decline slightly as growth in spending exceeds growth in disposable income.
- **Stock prices**, as measured by the S&P 500 average, should be between 5% higher or lower, reflecting the slowing growth in profits and rising short-term interest rates.
- **Manufacturing** will continue to be weak with the PMI index just slightly above or below 50.

- **Business investment** spending growth should edge down slightly and be in a range of 2.0% to 3.5% as employment and consumer spending growth slows.
- **Residential housing investment** should remain relatively strong in a range of 6% to 8%, but should edge down a bit from 2015's level; housing starts should rise 10% to 15%.
- **Residential housing prices** should rise more slowly in 2016 in a range of 2% to 4% in 2016.
- **Trade deficit** should rise in 2016 as the increase in the value of the dollar continues to depress exports and increase imports. The **dollar's value** on a trade-weighted basis should rise slightly.
- **Monetary policy** — the Federal Reserve will raise the federal funds rate two to three times during 2016 in 25 basis point increments.
- **Total inflation** measures (CPI and CPE) will rebound sharply in 2016 as the depressing effects of 2015's collapse in oil prices passes out of the indices. **Core PCE inflation** will be relatively stable in a range of 1.2% to 1.6%, reflecting global disinflationary trends offset somewhat by the closing U.S. employment and output gaps. Core PCE inflation will remain well below the FOMC's 2% objective at least through 2018 and perhaps much longer.
- The **10-year Treasury rate** is likely to fluctuate in a range between 2.25% and 2.75% in 2016. Faster than expected real GDP and employment growth would push the rate toward the top end of the range; greater than expected declines in inflation and/or heightened financial instability would push the rate toward the bottom end of the range.
- **Fiscal policy** will have a positive impact on real GDP growth during both fiscal year and calendar year 2016, raising real GDP growth by 0.4 to 0.6%. The deficit as a percentage of nominal GDP will increase substantially from fiscal year 2015's level of 2.46% to a range of 3.25% to 3.50%. Stronger than expected growth would push the deficit toward the lower end of the range.
- **State and Local investment** spending growth should range between 1.5% and 2.0%.

2. Rest of the World

- **Global growth** is likely to improve to 3.4% in 2016 from 3.1% in 2014. Risks are tilted to the downside.
- **European growth** will be positive but will likely fall short of the consensus 1.7% as the benefits of 2015's fall in the value of the euro wane and social and political disruptions occur.
- **European inflation** will rise from 2015's 0.1% but will probably fall short of the expected 0.9%.
- **European financial markets** should be relatively stable with periodic episodes of volatility prompted by specific events.
- **European political dysfunction, populism and nationalism** will continue to worsen gradually. Countries to watch closely include Greece, Spain, Italy and Portugal.
- **U.K. growth** is expected to remain a solid 2.5% in 2016 compared to 2.4% in 2015; some risk to this outlook could evolve from the proposed referendum for the U.K. to leave the European Union.

- **China's GDP growth** will slow below 6.5% and could be as low as 6.0% by the end of 2016 as economic reforms are implemented and the shift to a consumer-focused economy gathers momentum.
- **China's leadership** will continue to be slow in implementing *economic reforms* but financial and political stability will be maintained.
- **Japan's** economic policies will continue to fall short of achieving the 2.0% inflation target; inflation is expected to rise from 0.5% in 2015 to 1.0% in 2016. GDP growth will also continue to fall short of the policy target, but should rise from 0.7% in 2015 to 1.2% in 2016. Population decline and slow implementation of market reforms will continue to weigh heavily on both growth and inflation.
- **India** should continue to experience relatively strong real GDP growth in a range of to 6.0% to 7.0% in 2016.
- **Emerging market countries** should experience better growth in 2016 than in 2015 when falling prices for commodities depressed economic activity in many countries.
- **Brazil, Russia, and Venezuela** will continue to struggle the consequences of the steep decline in the prices of commodities and particularly in the price of oil.

3. **Risks** — stated in the negative relative to the forecast.

- **U.S. potential real GDP growth** falls short or exceeds expectations; falling short is the more serious risk
- **U.S. employment growth** is slower or faster than expected; slower growth is the more serious risk
- **Employment participation rate** rises rather than remaining stable or falling modestly
- **U.S. hourly wage rate growth** falls from its 2015 level of 2.2% or rises much more rapidly than expected; falling wage growth is the more serious risk
- **US. Unemployment rate** falls less than expected
- **U.S. productivity** remains below 1%
- **Real U.S. consumer income and spending** increase less or more than expected; less than expected increases are the more serious risks
- **U.S. stock prices** fall more than or rise more than the expected range of -5% to +5%
- **Growth in U.S. residential housing investment and housing starts** are less than or more than expected; below expectations is the more serious risk
- **U.S. residential housing price increases** are less than expected
- **U.S. private business investment** does not improve as much as or more than expected; falling short of expectations is the more serious risk
- **Oil price declines** that occurred in 2015 trigger bankruptcies and cause tighter financial conditions with negative implications for economic activity and growth

- *U.S. manufacturing growth* contracts or expands more than expected; contraction is the more serious risk
- *U.S. trade deficit* does not widen as expected;
- *Value of the dollar* rises substantially
- *U.S. monetary policy* spawns financial market uncertainty and contributes to financial instability
- *U.S. inflation* falls, rather than remaining stable or rising as expected
- *U.S. interest rates* fall or rise more than expected
- *U.S. fiscal policy* is more expansionary than expected
- *Federal budget deficit* increases more than expected
- *U.S. state and local spending* does not rise as fast as expected
- *Global GDP growth* does not rise as fast as expected
- *European growth* is considerably less than expected
- *ECB's* quantitative easing program is not successful in raising inflation and stimulating the European economy
- *Europe* — financial market turmoil reemerges
- *Europe* — political instability and social unrest rises more than expected threatening survival of the Eurozone and the European Union
- *Chinese* leaders have difficulty implementing *economic reforms*
- *China's growth* slows more than expected
- *Japan* — Abenomics and monetary policy are unsuccessful in raising inflation to the 2 percent target and economic growth continues to be below expectations
- Severe and, of course, unexpected *natural disasters* occur, which negatively impact global growth

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