



US Tax Reform: Implications for US inflation, US Treasury supply, and inequality

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Overview



Individual provisions:

1. Lower income taxes for most income groups
2. Higher standard deduction
3. Smaller mortgage interest deduction
4. State And Local Tax deduction capped at \$10k

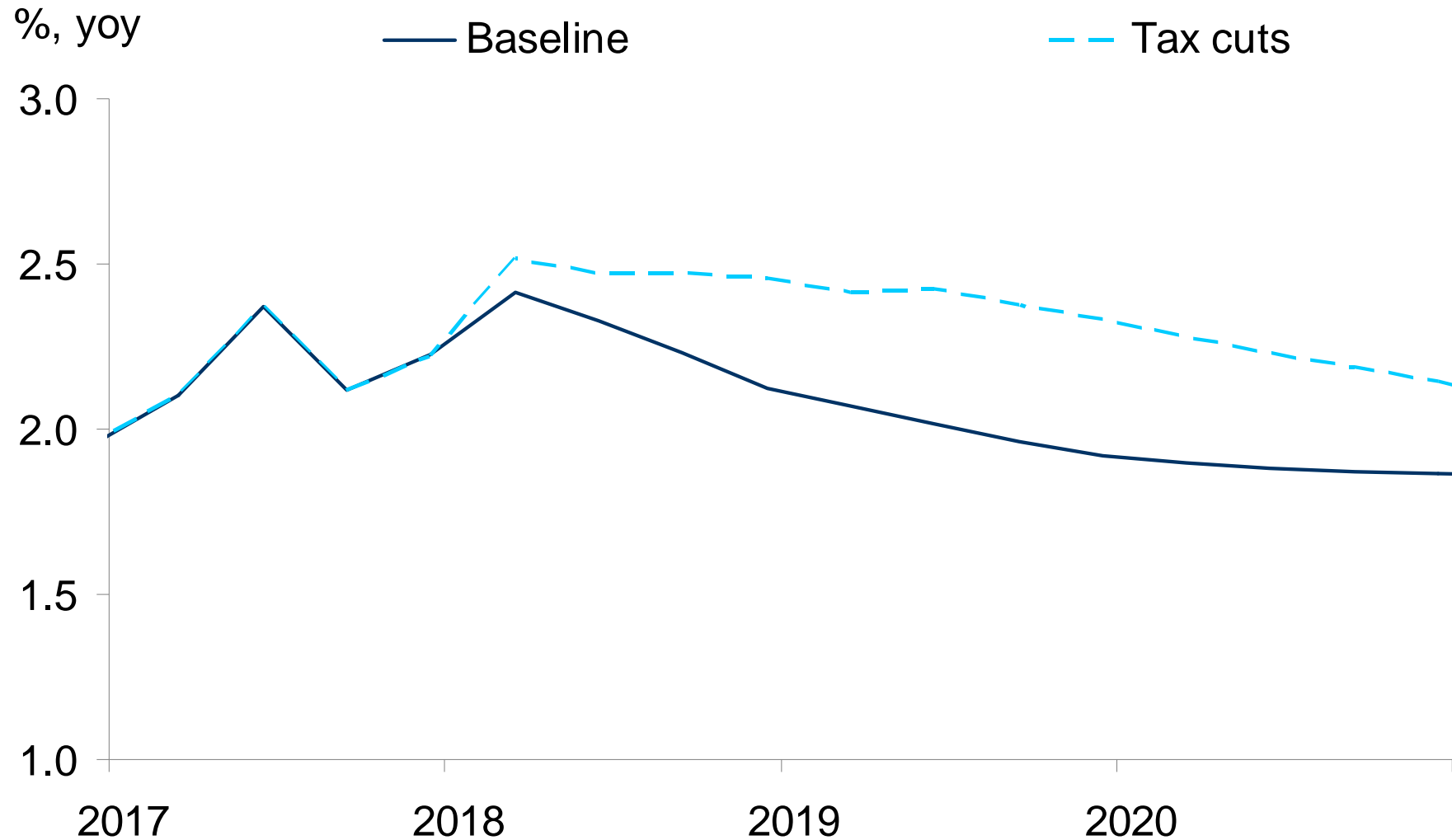
Business provisions:

1. Lower corporate tax rate from 35% to 21%
2. Full expensing of new capex

International provisions:

1. Moving from worldwide taxation to territorial taxation, ie US profits plus Base Erosion and Anti-abuse Tax (BEAT)
2. Repatriation of deferred earnings

Real GDP growth is boosted by a few tenths in the coming years due to tax cuts

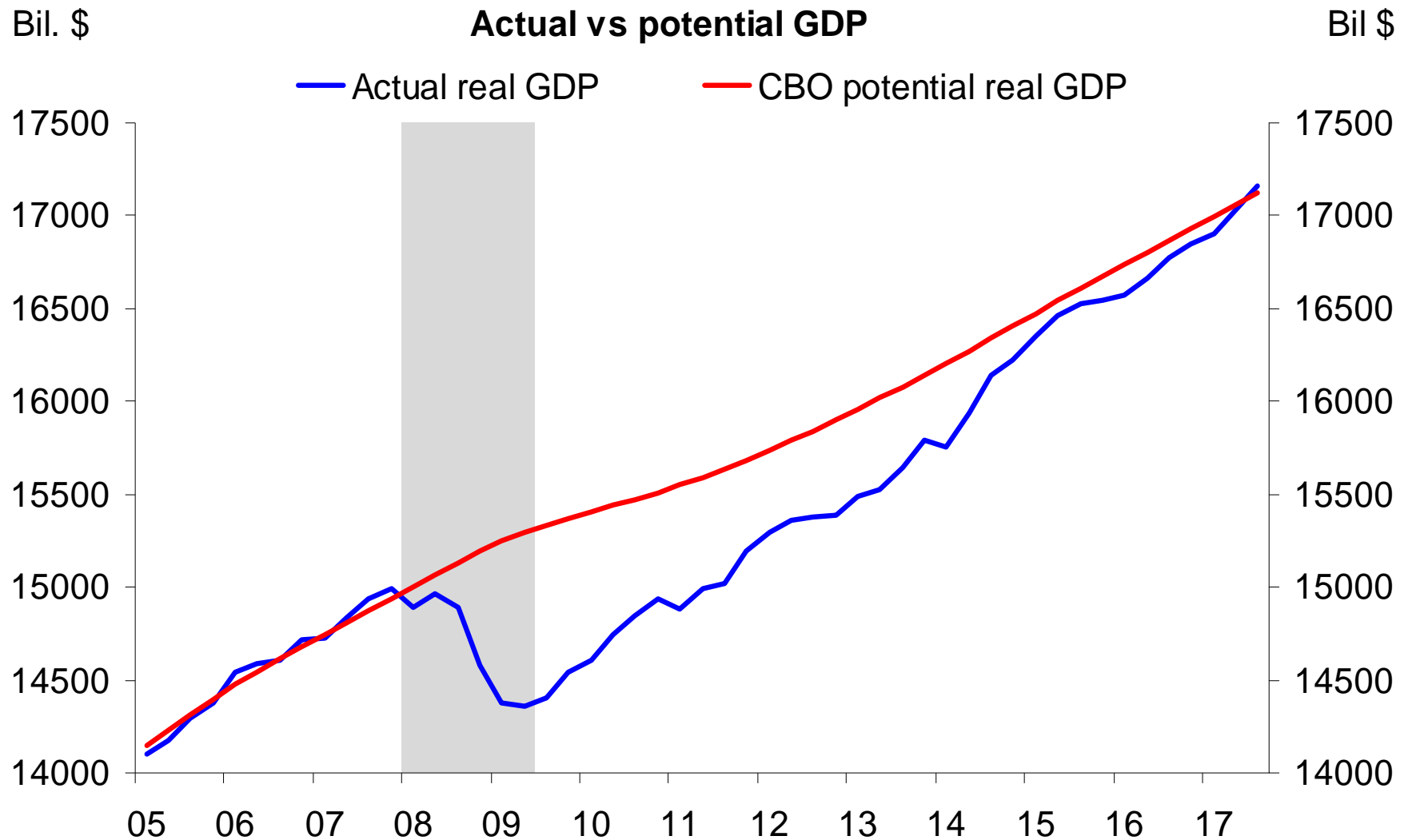


Source: FRB, DB Global Research



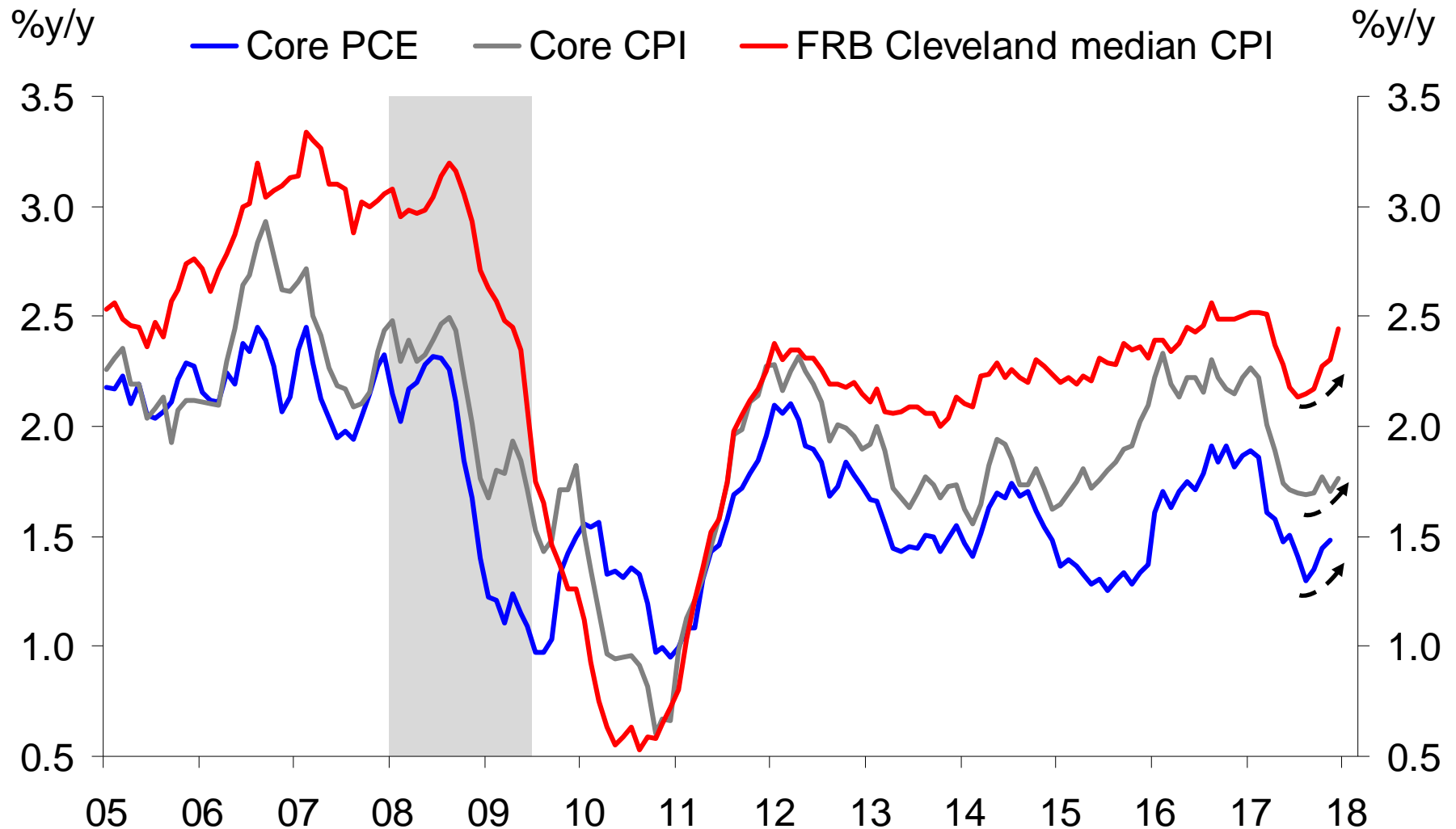
Impact of the tax package on the inflation outlook

The US economy is now operating at full capacity.
That is when inflation pressures begin to intensify



Source: CBO, BEA, Haver Analytics, DB Global Research

Inflation showing signs of bottoming

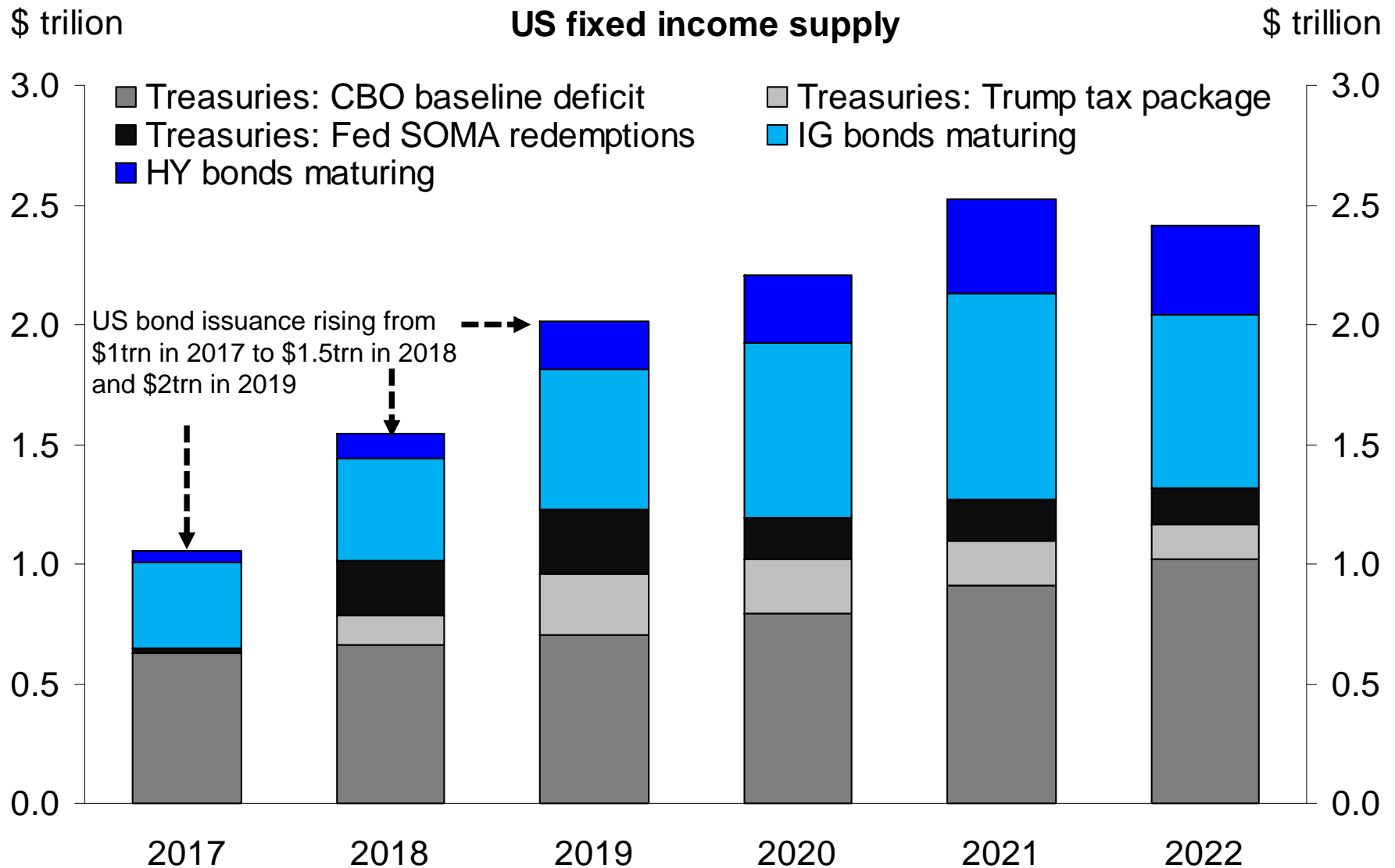


Source: BEA, BLS, FRBCLE, FRBATL, Haver Analytics, DB Global Research



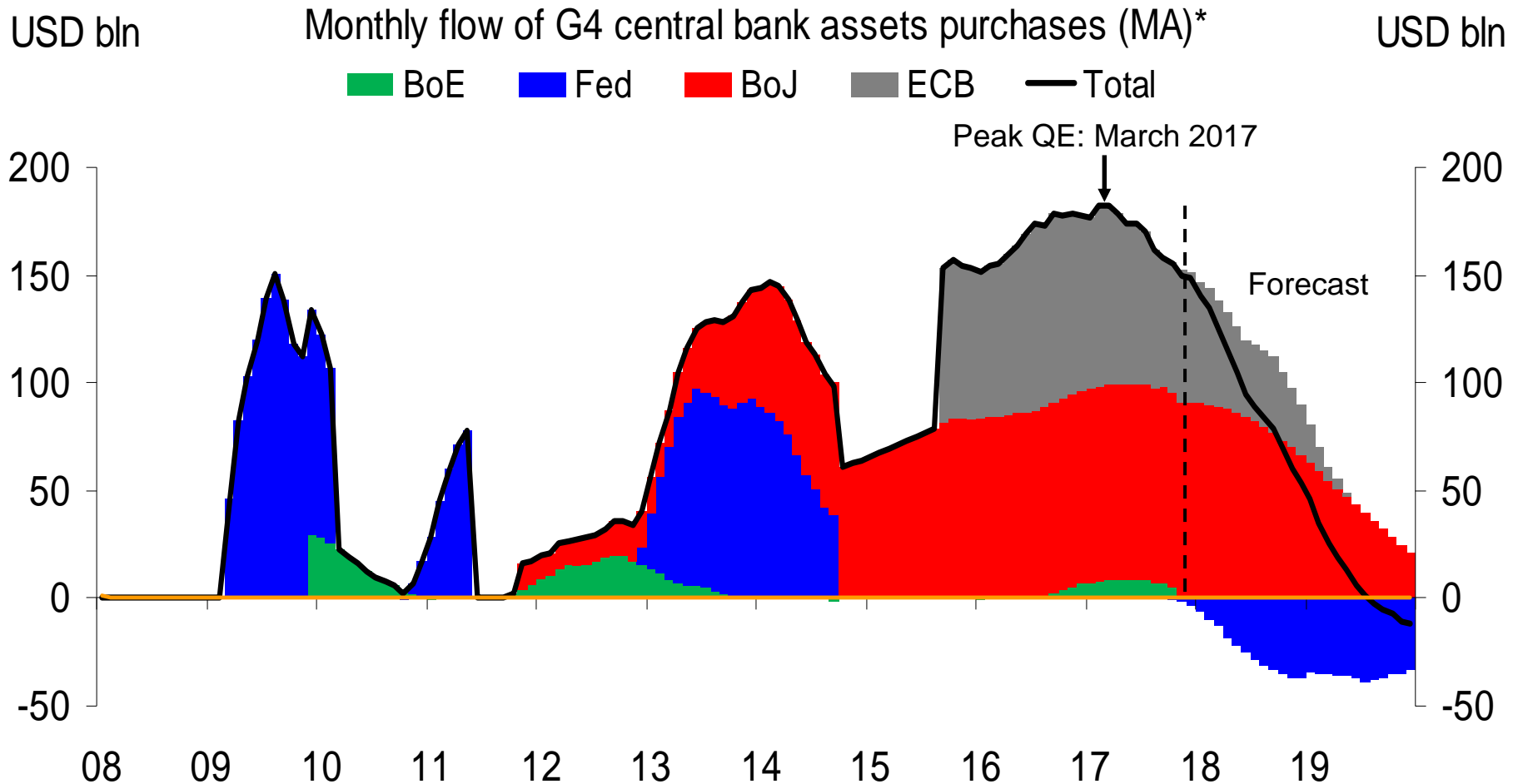
Impact of the tax package on the supply of Treasuries

Doubling of US fixed income supply risks pushing rates higher, credit spreads wider, dollar down, and ultimately S&P500 lower



Source: Steven Zeng, Michal Jezek, Standard & Poor's Financial Services LLC, DB Global Research

Peak liquidity behind us. ECB exit will lift bund rates and widen US credit spreads



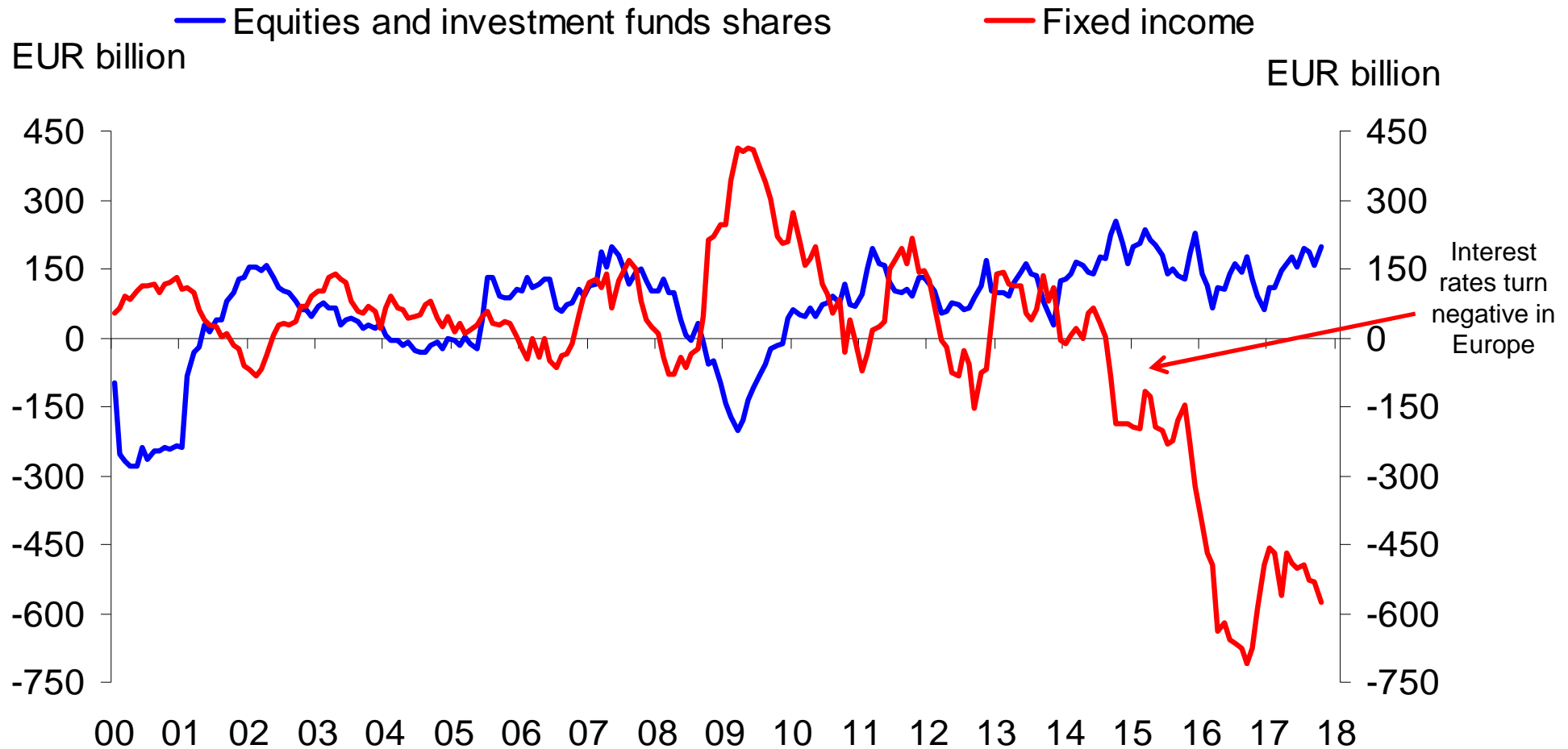
***Note and assumptions:** ECB & Fed data is 6m MA, others are 12m MA, Between Apr-2013 to October 2014 BoJ purchase of JGBs assumed to be around 7-7.5 trln Yen per month and Post November 2014, BoJs monthly purchase of JGBs assumed to be 10 trln Yen per month. Assumptions: Fed will redeem maturing assets as per the announced cap during the September decision. ECB will cut buying to EUR 30 billion per month from January 2018 and reduce to EUR 10 billion for October, November and December 2018 and eventually cut to zero in 2019. BoE assumed to remain the same as the Asset Purchase Facility to end in February 2017. BoJ to cut buying by Yen 3.79 trillion from January 2018.

Source: Fed, BoJ, ECB, BoE, Haver Analytics, DB Global Research

Bond investors fleeing European negative interest rates at a record pace.
 This will continue to put downward pressure on US interest rates



**Euro area: BOP: financial account: Net portfolio investment
 12 month rolling sum**



Source: ECB, Haver Analytics, DB Global Research



The tax reform bill and US inequality



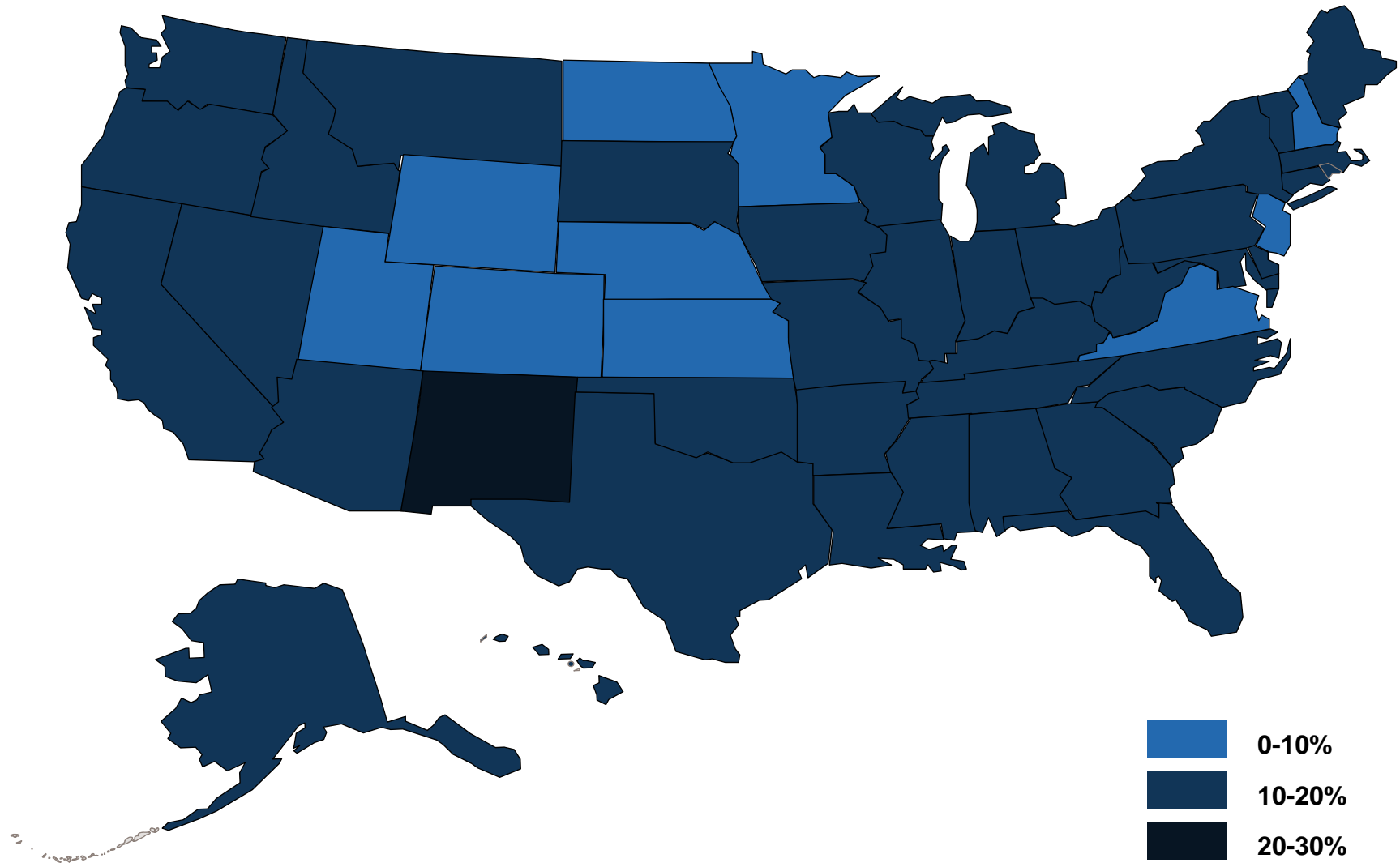
Average change in federal taxes by income tax bracket (\$)

	2019	2021	2023	2025	2027
All taxpayers	-1,466	-1,223	-817	-793	21
Less than \$10k	-21	-3	15	16	20
\$10k to \$20k	-87	93	147	138	318
\$20k to \$30k	-139	90	110	134	372
\$30k to \$40k	-338	-123	-13	7	299
\$40k to \$50k	-524	-266	-155	-121	301
\$50k to \$75k	-841	-682	-534	-505	142
\$75k to \$100k	-1,258	-1,132	-887	-875	-53
\$100k to \$200k	-2,295	-2,080	-1,554	-1,485	-180
\$200k to \$500k	-7,155	-6,522	-4,888	-4,860	-594
\$500k to \$1m	-20,878	-18,357	-11,817	-11,296	-2,551
\$1m and over	-64,428	-51,104	-16,554	-15,712	-13,506

Lower income groups will see taxes go up

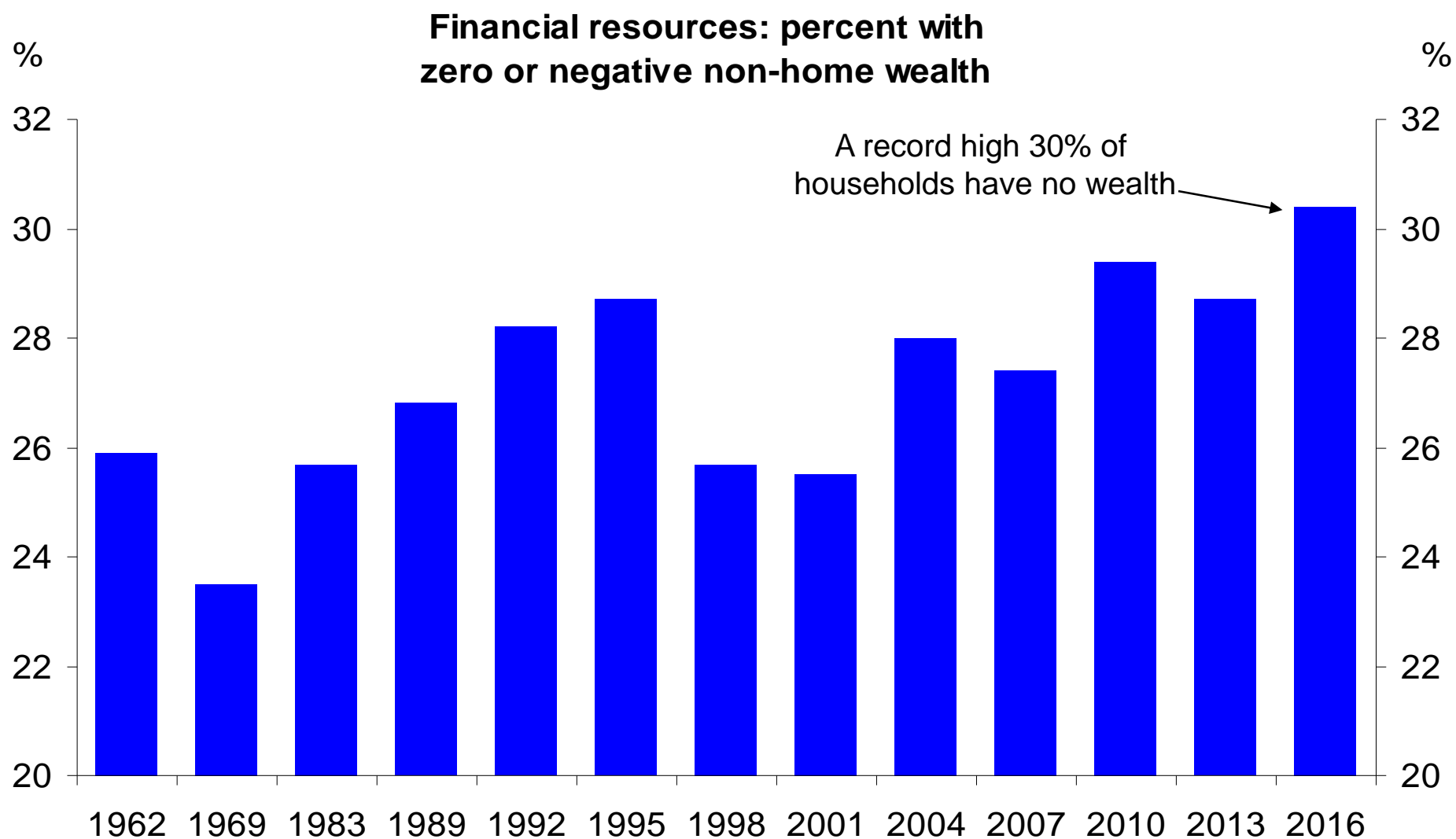
Source: Joint Committee on Taxation, DB Global Research

Percentage of population receiving food stamps, 2016



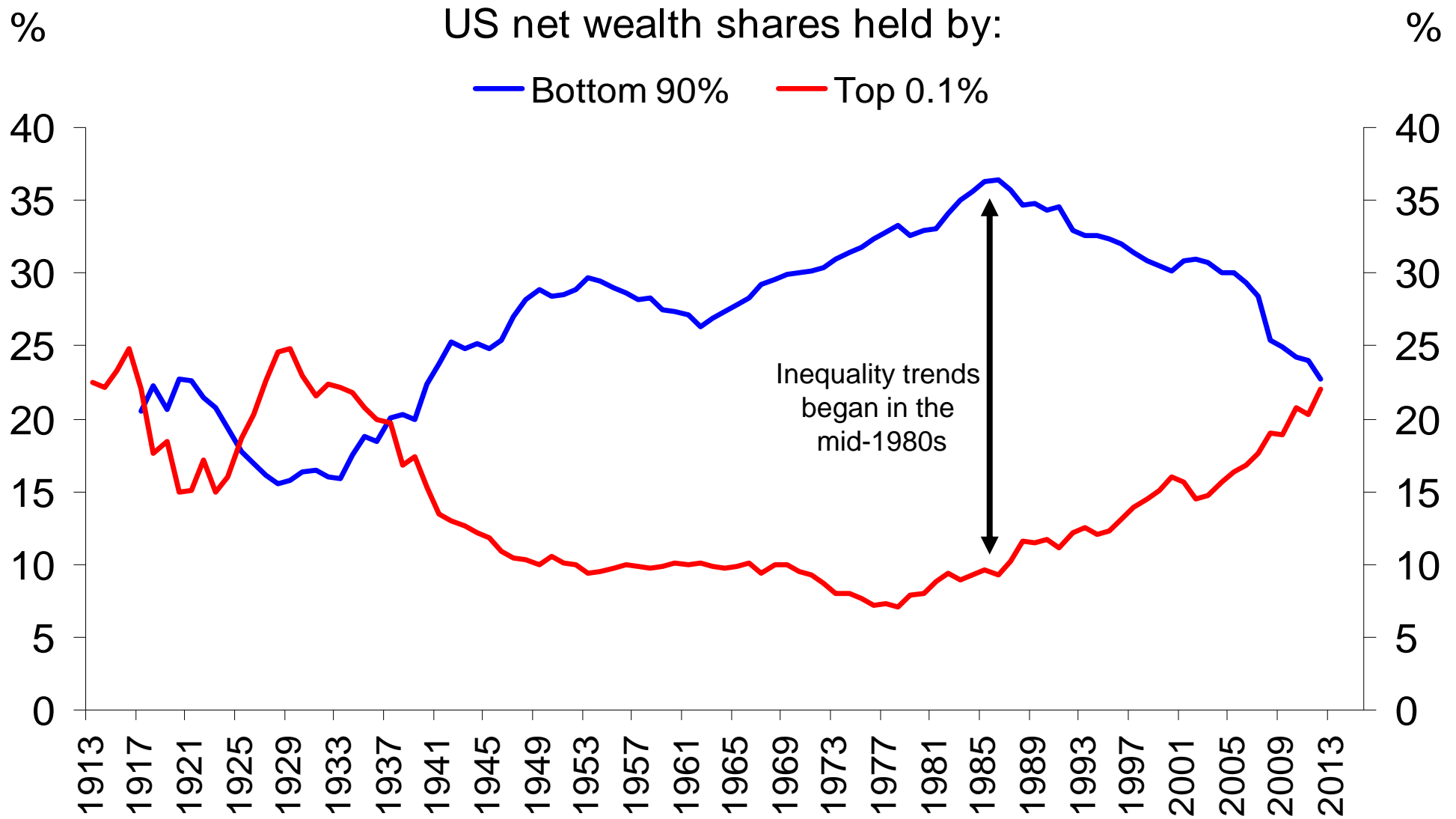
Source: CBPP, DB Global Markets Research

More families than ever before have zero or negative non-home wealth



Source: Edward N. Wolff (2017). Survey of Consumer Finances, , DB Global Markets Research

US: Top 0.1% owns as many assets as the bottom 90%



Source: The World Wealth and Income Database, DB Global Research



Investment implications/Markets

Investment implications summarized



<p>Fed outlook – Fed hikes continuing</p>	<p>Fed will hike rates four times in 2018. In 2018Q2 higher US inflation and ECB exit will push US and European rates higher.</p>
<p>Bond markets - Rates gradually higher</p>	<p>Key forces driving long rates are 1) US inflation and 2) ECB exit. US 10s will be 3% by end-2018. German 10s will be 1% by end-2018.</p>
<p>Stock markets - Stocks higher, populism a risk</p>	<p>Low rates, plenty of liquidity, deregulation, and tax reform all likely to be positive for equities. But populist backlash a risk in November.</p>
<p>FX - EUR/USD higher</p>	<p>EURUSD going to 1.30. European growth surprising to the upside and associated ECB exit will continue to support EUR/USD.</p>
<p>Commodities - Moving higher</p>	<p>Global growth very supportive. But property bubble and problems in financial system in China are worrying.</p>
<p>Emerging markets - Many imbalances in EM</p>	<p>EM normally suffers from higher US rates but higher commodity prices is helpful. Still many structural problems in a number of emerging markets.</p>

Source: DB Global Research



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- **Deutsche Bank Securities, Inc.**
- Torsten Slok joined Deutsche Bank Securities in the fall of 2005.
- Mr. Slok's Economics team has been top-ranked by Institutional Investor in fixed income and equities for the past five years. Slok currently serves as a member of the Economic Club of New York
- Prior to joining the firm, Mr. Slok worked at the OECD in Paris in the Money and Finance Division and the Structural Policy Analysis Division. Before joining the OECD he worked for four years at the IMF in the Division responsible for writing the World Economic Outlook and the Division responsible for China, Hong Kong, and Mongolia.
- Mr. Slok studied at University of Copenhagen and Princeton University. He has published numerous journal articles and reviews on economics and policy analysis, including in Journal of International Economics, Journal of International Money and Finance, and The Econometric Journal.



Appendix 1

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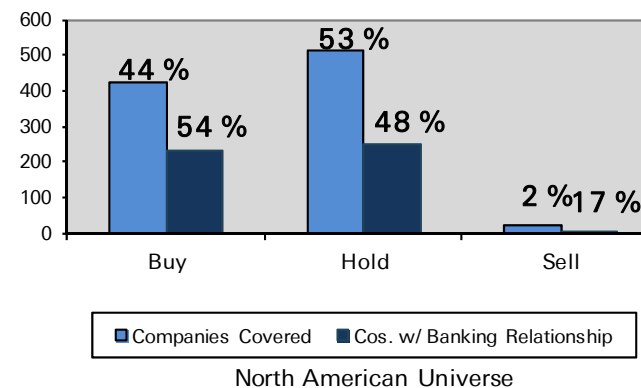
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