



# RISKS RELATED TO US MACROECONOMIC ISSUES

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## John Behringer

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John Behringer is a Risk Advisory Services Partner responsible for leading the Great Lakes Financial Institution practice for RSM. John oversees the delivery of audit, tax and consulting services to financial institutions, both domestic and international, with total assets ranging from \$1 billion to in excess of \$1 trillion. He has over 20 years of public accounting experience working specifically with community, regional and super regional banks, foreign banking offices, mortgage banks, investment companies and broker dealers focused on the delivery of risk advisory and strategic consulting services.

In addition to his industry leadership role John is responsible for the Great Lakes Internal Audit and SOX practice which delivers outsourced and co-sourced internal audit and SOX advisory services to various commercial entities ranging in total revenue of \$500 million to in excess of \$2 billion.

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# AGENDA

Topic
Overview of US macroeconomic environment
Five key macro issues
Risk considerations
Questions

## OBJECTIVES

- By the end of this course, you will be able to:
  - Identify key macroeconomic issues impacting the US economy
  - Recognize risks associated with the issues
  - Understand the potential impact of these risks on your organization

# OVERVIEW OF US MACROECONOMIC ISSUES

- Tax reform
- Changing consumer preference
- Tightening labor force
- Big data and automation
- Regulatory change

## US ECONOMIC OUTLOOK: 2018

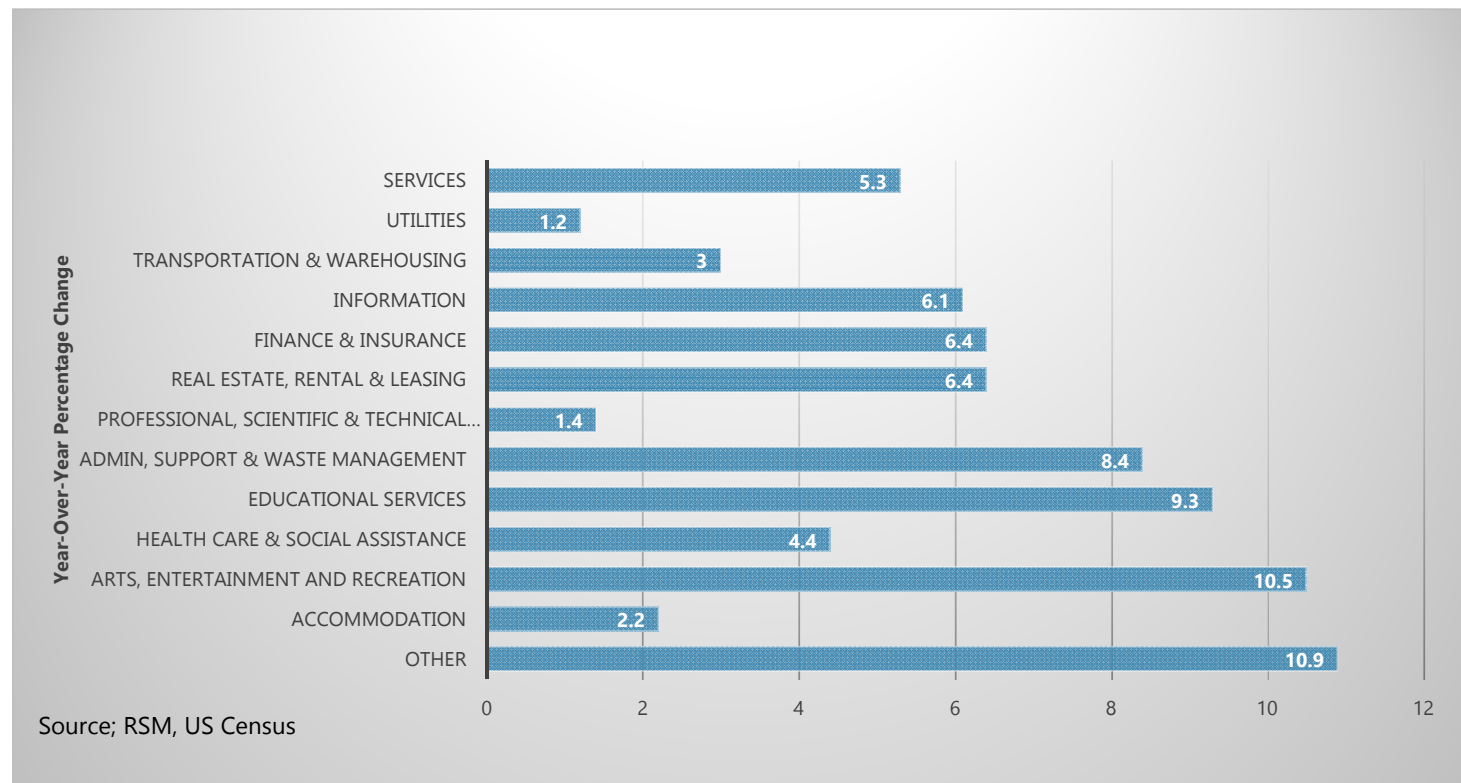
- **Base case: Growth above 3 percent in 2018**
  - **Tax cut boosts growth prospects in 2018 & 2019**
    - Current account and trade deficits explode
    - 2018: \$670 billion
    - 2019: \$900 billion
    - 2020: \$1 trillion
  - **Tax effect fades in 2020 and growth moves back toward 2 percent (long-term trend)**
  - **Household consumption of 3.5 percent**
    - Upper quintile of income earners to drive spending
  - **Strong business outlays on capital expenditures**
    - Software, equipment and intellectual property
    - Data from MMLC survey shows middle market ramping up

## US ECONOMIC OUTLOOK: LONGER TERM

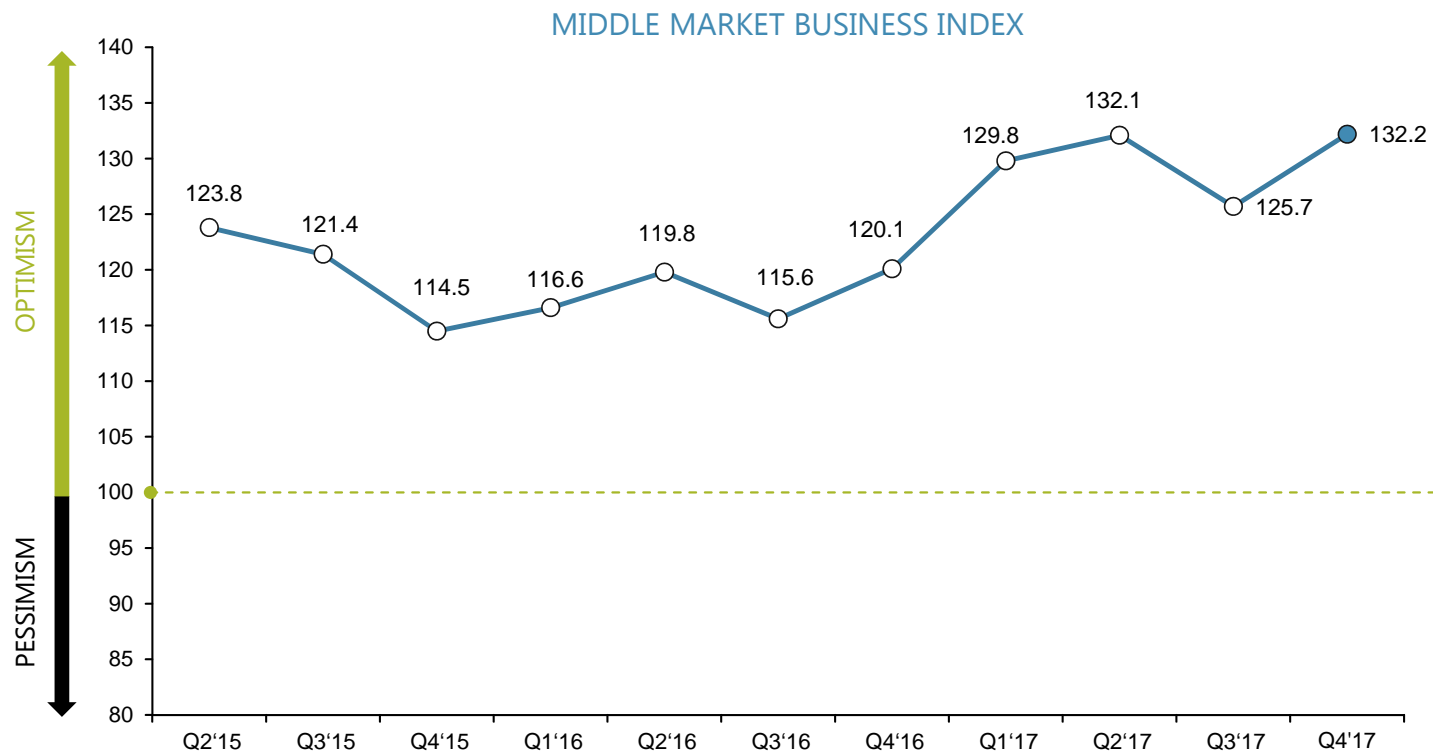
- **Medium to long-term outlook**
  - **Long-term growth trend 2 percent**
    - Productivity remains tepid near 0.5 percent per year, but will pick up on back of stronger fixed business investment
    - Economic and wage growth uneven around the country
    - RSM Middle Market Business Index at 132.1, all-time high
    - Recession probability low; 15 percent
  - **Household consumption of 3 percent**
    - Solid consumption and services demand driven by rising incomes and decline in unemployment rate below 4 percent
  - **Residential investment**
    - Forward looking permits at 1.25 million at annualized pace
    - Major supply issues in new home markets
    - Policy to impact residential investment going forward
    - Lack of labor mobility in context of tight labor market; Amazon effect



## US ECONOMIC OUTLOOK: SERVICE SPENDING



AFTER A SHARP DECLINE IN THE PRIOR QUARTER, THE RSM US MIDDLE MARKET BUSINESS INDEX IN THE FOURTH QUARTER SURPASSED ITS PREVIOUS ALL-TIME HIGH



# US ECONOMIC OUTLOOK

- **Policy Normalization Amidst Low Rate Structure**
  - **Central Bank**
    - Fed forecasting 3 rate hikes in 2018; we think 4 is more likely
    - Balance sheet normalization in process
    - 2018 Recession probability low; near 15 percent
  - **Interest Rates**
    - Policy rate likely to move to 2.5 percent in early 2018
    - 10-year to trade between 2.5-3 percent with upside risk as Trump tax plan implemented
  - **Inflation**
    - Modest inflation for now
    - Stirrings in both producer and consumer data
    - Technology likely to restrain inflation in near to medium term
    - Fiscal operations likely to push inflation and bond yields much higher over the long term

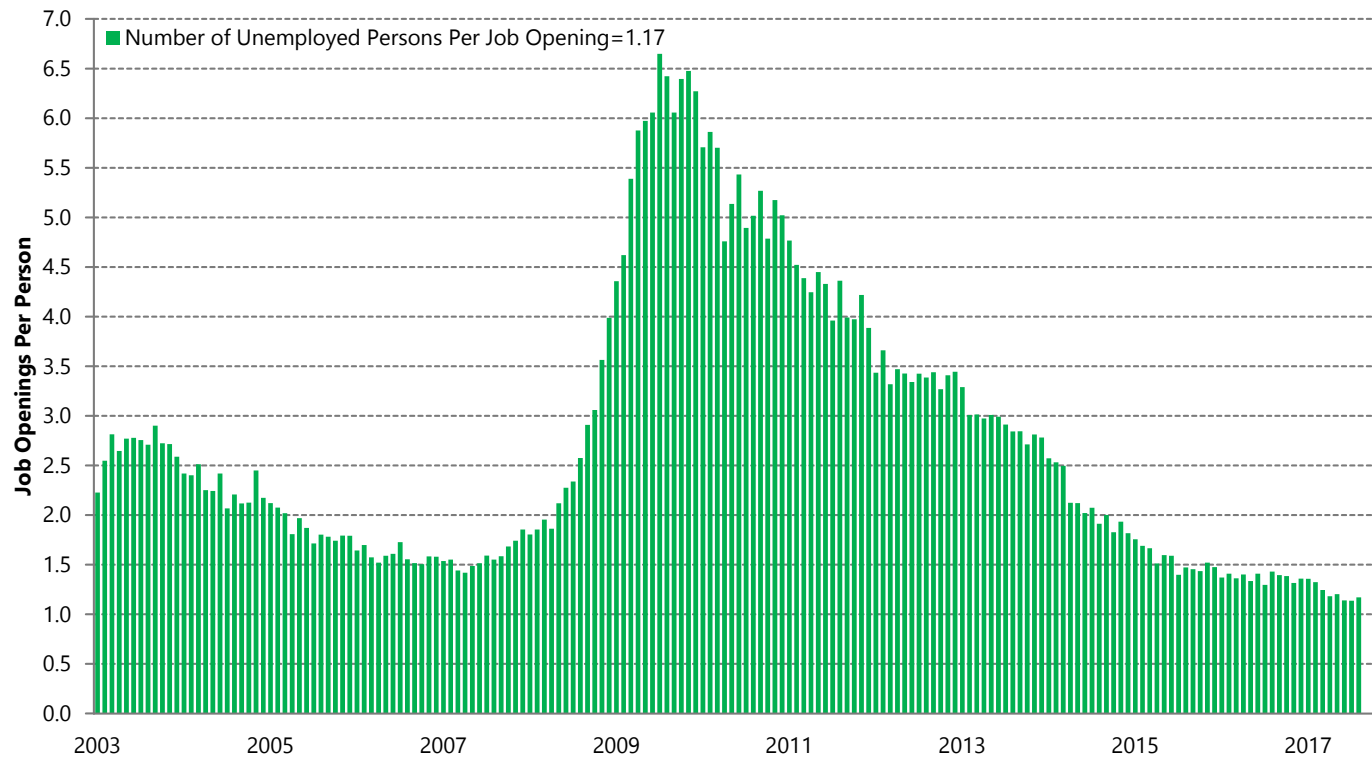
## US-GLOBAL ECONOMIC RELATIONS: A DIFFICULT PERIOD AHEAD

- **U.S. Global Trade Friction: Major 2018 Policy Issue**
- **This is the major risk to the domestic economic outlook in 2018**
  - **Selective tariffs, NAFTA and key trading partners**
    - Trump administration 15-50% tariffs on solar, washing machine
    - Targets China, South Korea
    - Expect many more over coming months
    - Asymmetric China retaliation will be designed to take market share
  - **NAFTA Modernization–Don't believe the urgency hype from media**
    - March possible, or even July concurrent with MX presidential election
    - US will push to brink–classic Trump tactic (needs the base)
    - Canada in some ways more at risk than Mexico
    - Mexico willing to work out bilateral agreement if NAFTA terminated
    - Meanwhile, prepare for short-term disruptions

## US EMPLOYMENT OUTLOOK

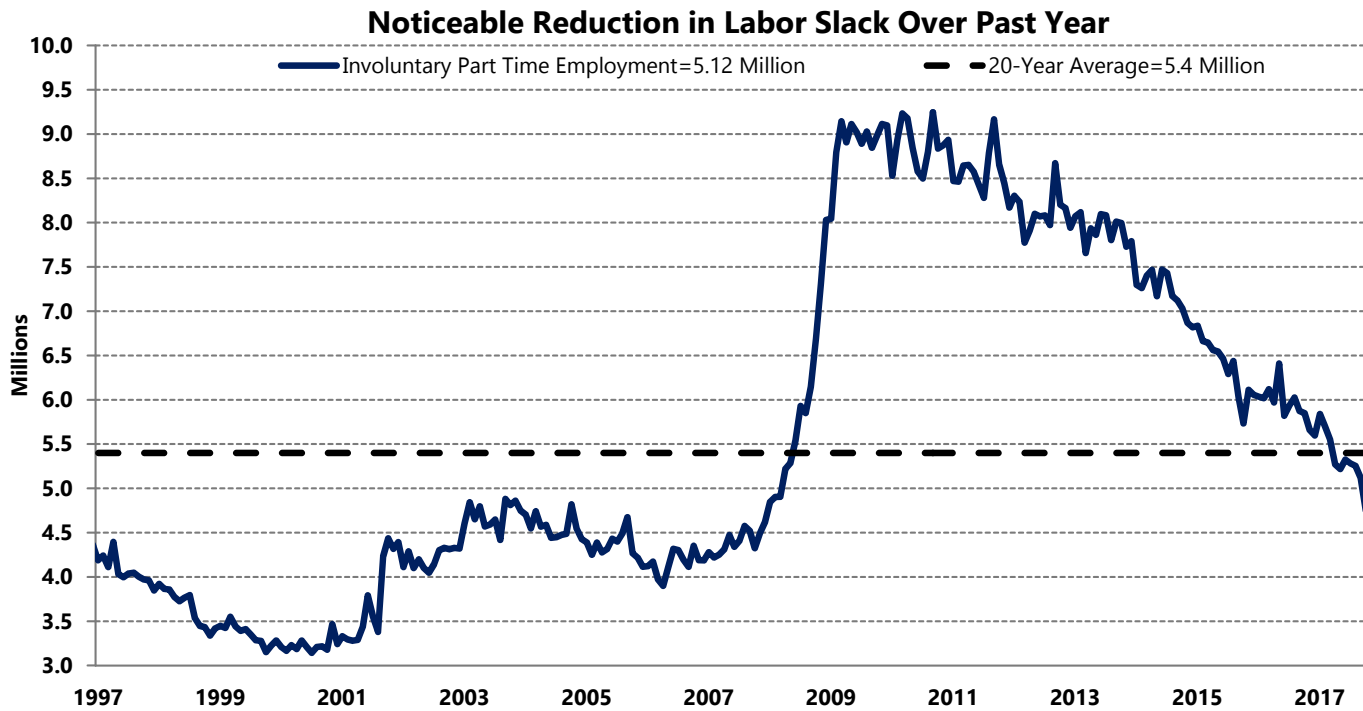
- **US Economy at full employment**
  - 173K per month gain in 2017 & 150K in 2018
  - **US Unemployment rate at 4.1 percent**
    - Heading to 3.7 percent with risk of lower rate in 2018
    - Those working part time for economic reasons below long-term average
    - Initial claims at multi decade low
  - **Tight Labor**
    - Cyclical low of unemployed individuals per job opening
    - Substitution of technology for labor

## TIGHT LABOR MARKET



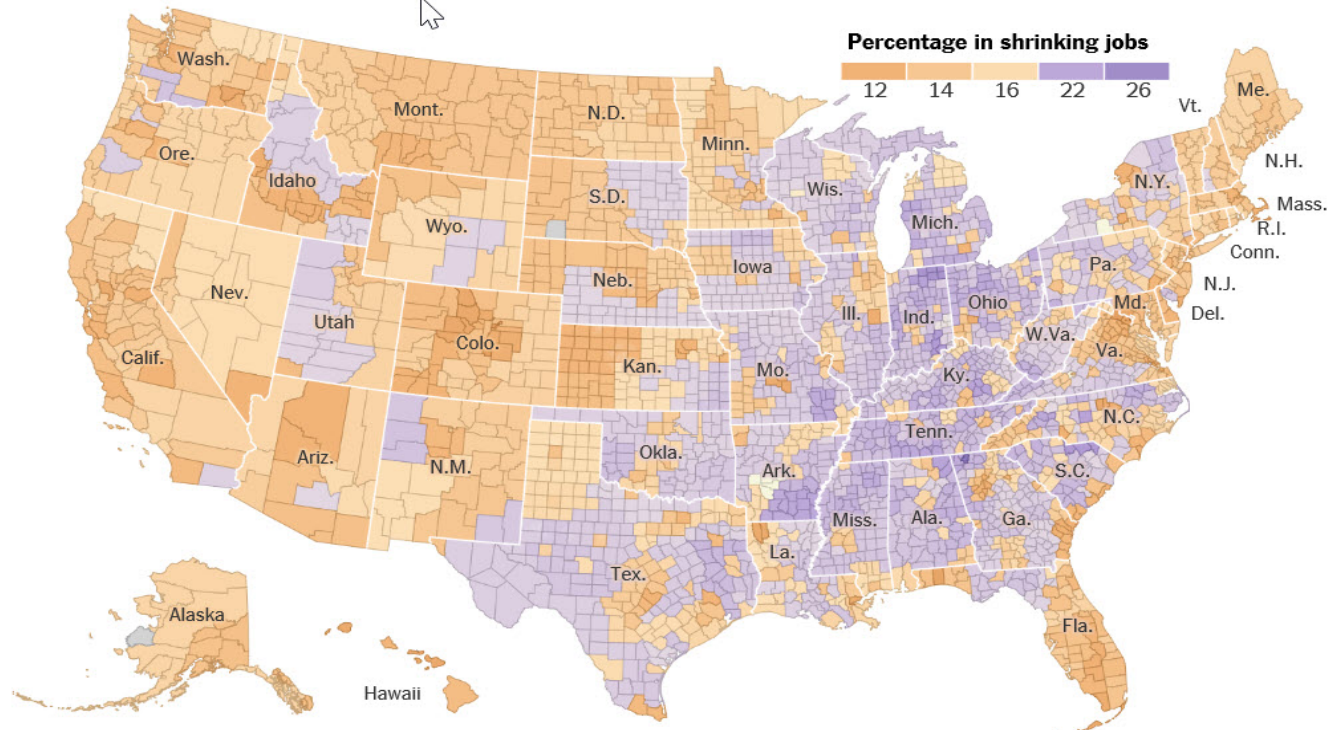
Source: RSM US, BLS

# PULLING WORKERS BACK INTO MARKET



Source: RSM US, BLS

# SHRINKING JOBS VS. GROWING JOBS



In much of the South and Midwest, a large share of the population works in fields where employment is expected to decline by 2026. Above is **the share of employed residents who work in shrinking occupations**, by county.

Source: Bureau of Labor Statistics and Census Bureau, via IPUMS

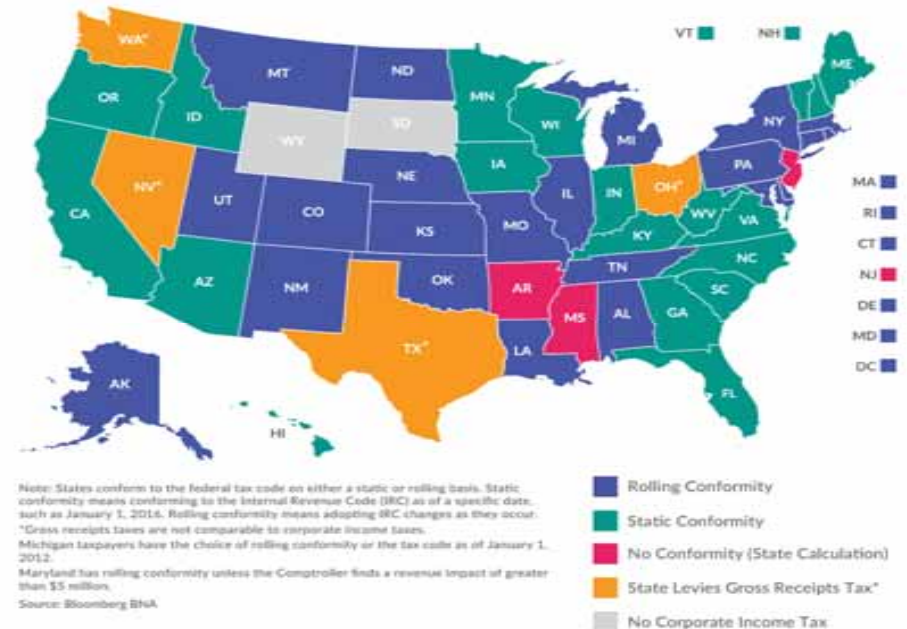
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# TAX REFORM

- Not just a Federal issue
  - Illinois change in effective rate
  - Cap on deductibility of SALT expenses for individuals
  - Greater multi-state activity and aggressive state positions to drive revenues
- Risks and other considerations
  - Do you have the most efficient tax structure?
  - When is the last time state Nexus exposure was reviewed?
  - Accuracy and completeness of deferred tax inventory
  - Likely point of emphasis from a financial statement audit perspective in 2018

Corporate Income Tax Conformity

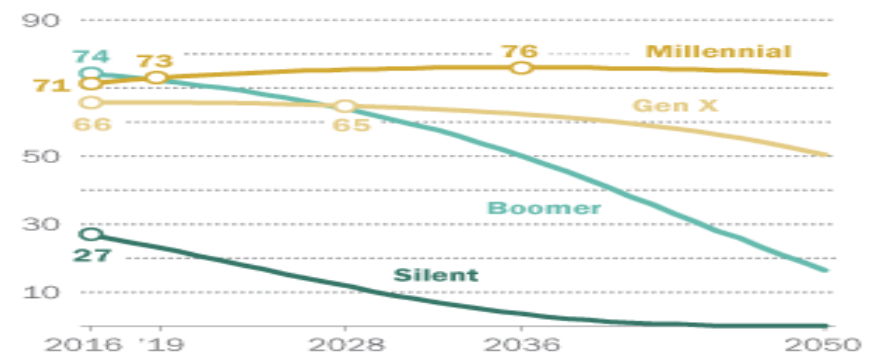


# CHANGING CONSUMER PREFERENCE

- Disruption is the “norm”
- No industry is insulated
- On-demand customer interaction—pull versus push
- “Experience” economy
  - Avoid being a commodity
- Need to leverage innovation and automation to survive which presents new and unique threats

## Projected population by generation

*In millions*



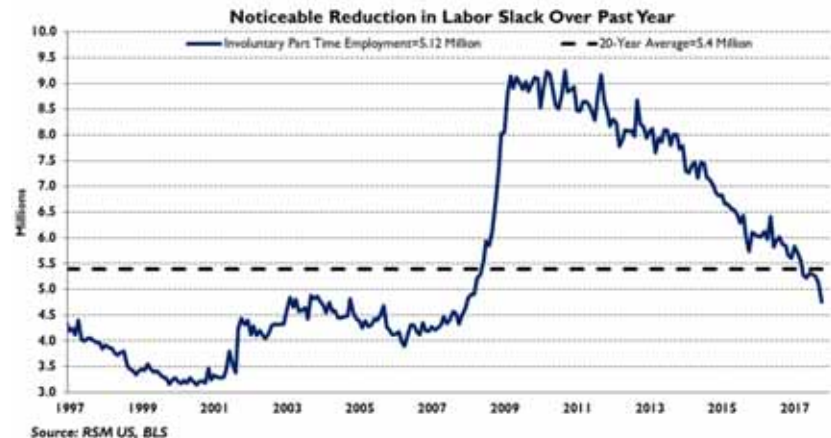
Note: Millennials refer to the population ages 20 to 35 as of 2016.

Source: Pew Research Center tabulations of U.S. Census Bureau population projections released December 2014 and 2016 population estimates.

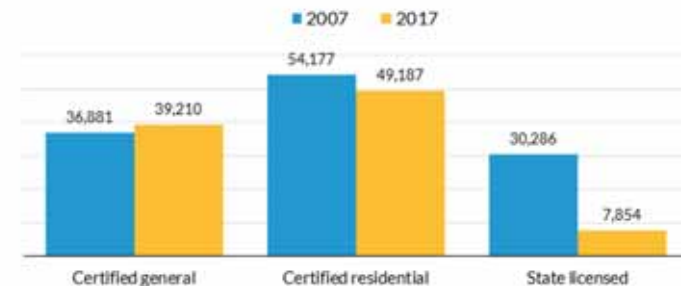
PEW RESEARCH CENTER

# TIGHTENING LABOR FORCE

- Impacting all industries and segments with overlap
  - Appraiser example
- Increase in competition for “qualified” talent driving up labor costs while productivity gains remain flat to slight gains (less than 1.0%)
- Mismatch between open positions and skills available in the marketplace
- Consideration of impact on succession plan for key roles



**Licensed Appraisers Plunged from 2007 to 2017**



# BIG DATA AND AUTOMATION

- Do we manage data effectively?
- How much data is “too much data?”
- Can we drive better decisions through data?
- What is our automation strategy?
- Is your BCP sufficient given your current operations?
- Consideration of privacy laws?
- Key man risks?

## DATA IS TRANSFORMING MULTIPLE INDUSTRIES

Aerospace  
 Agriculture  
 Automotive  
 Banking  
 Chemical  
 Communications  
 Consumer Packaged Goods  
 Electric  
 Electronics  
 Entertainment  
 Finance  
 Fitness  
 Government  
 Healthcare

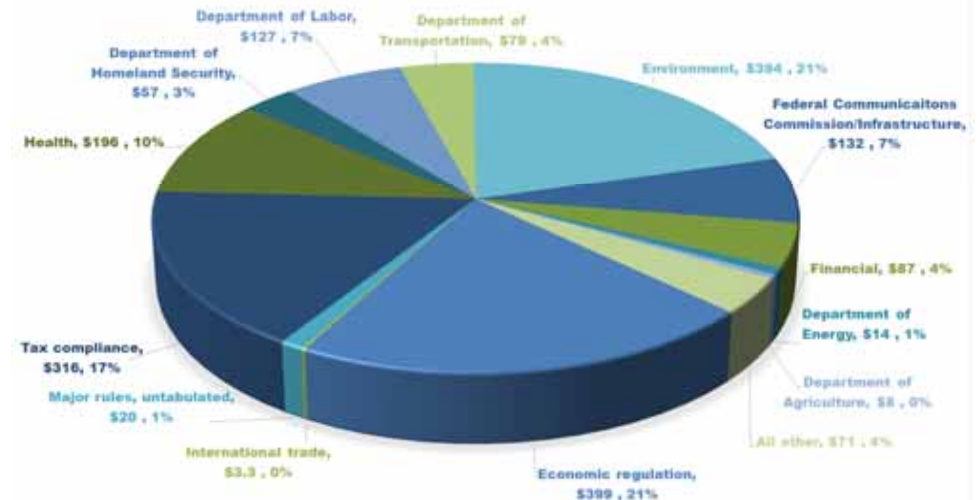


Hospitality  
 Information  
 Technology  
 Insurance  
 Media  
 Mining  
 Oil & Gas  
 Pharmaceuticals  
 Real Estate  
 Retail  
 Robotics  
 Sales  
 Shipping  
 Telecommunications  
 Travel

# REGULATORY CHANGE

- Regulatory landscape and focus is changing
  - Technology and social media companies moving to the forefront of focus for regulation by government agencies
  - Rise in cryptocurrency transactions
  - Fintech activities and impact on transaction chain
- Personal information and privacy concerns driving consumer protection activities
- Outsourcing or co-sourcing a viable option given tightening labor market

**ANNUAL COST OF FEDERAL REGULATION AND INTERVENTION 2017 ESTIMATE, \$1.902 TRILLION**  
(\$ IN BILLIONS)



# QUESTIONS AND ANSWERS?

END OF PRESENTATION

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# THANK YOU FOR YOUR TIME AND ATTENTION!

IIA CHAPTER CHICAGO | 58<sup>TH</sup> ANNUAL SEMINAR

