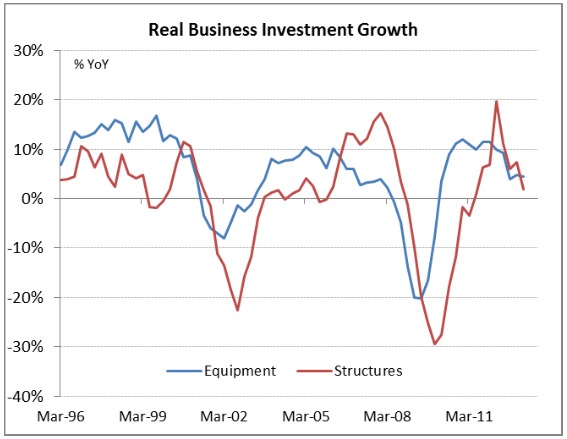
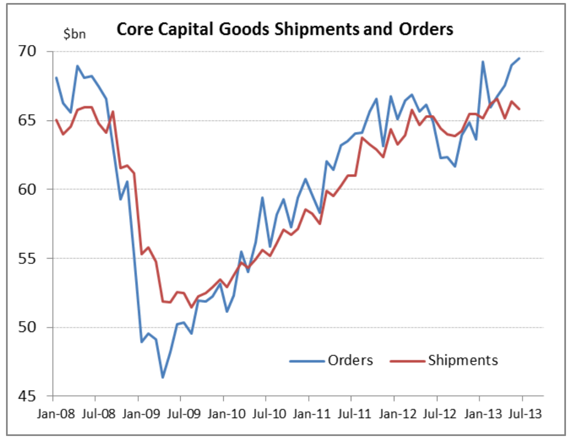
v. Business sector

Business investment intentions modestly improved

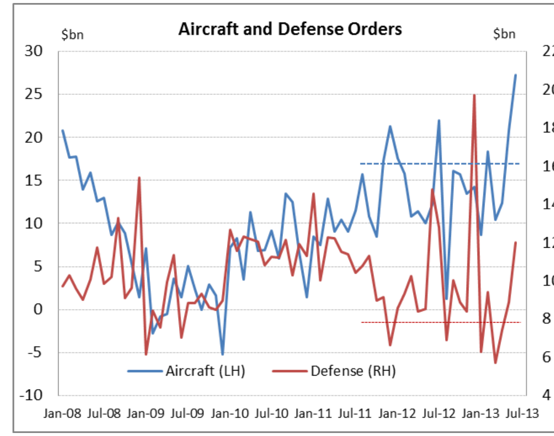
- Real business investment recovery has been tepid



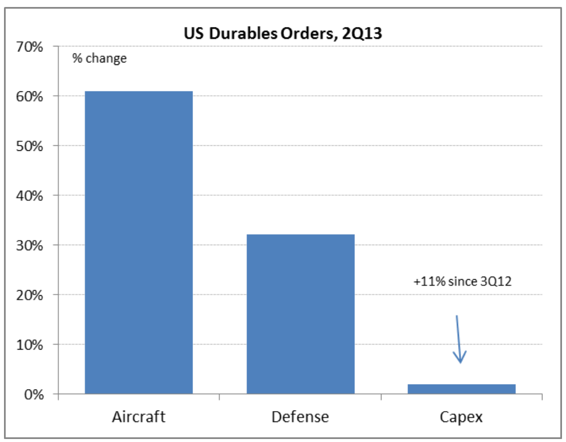
- But improving .... new orders of capital goods running ahead of shipments.



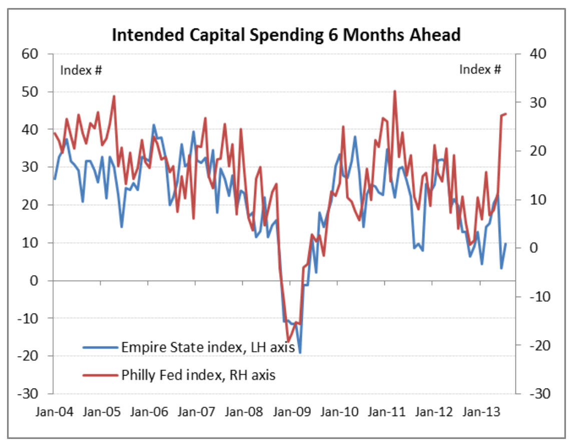
- Aircraft and defense awaken from slump.



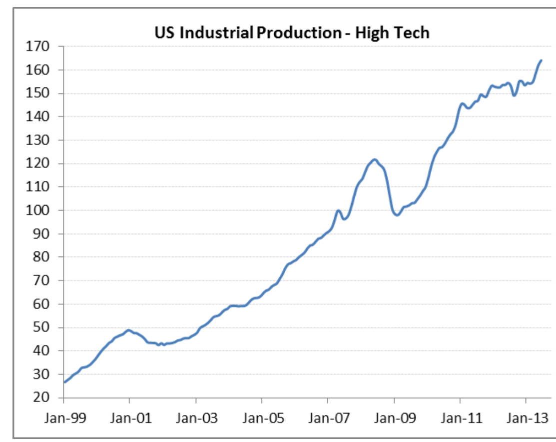
- Surge in 2Q13 orders will add to 3Q13 activity.



- Intended capex improves in Philly survey.



- Recent bounce in IT output.

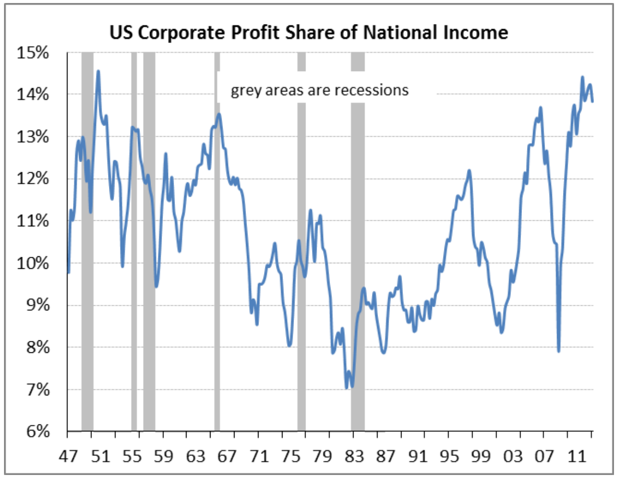


CalPERS Investment Office Asset Allocation

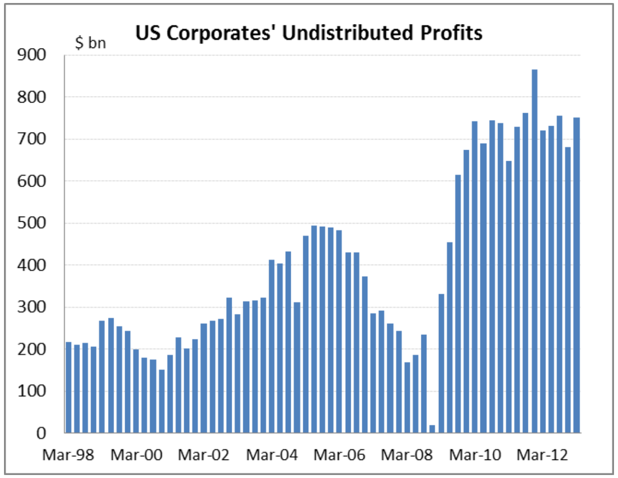
- Defense and aircraft orders are soft.

Corporate profit share still near all time highs

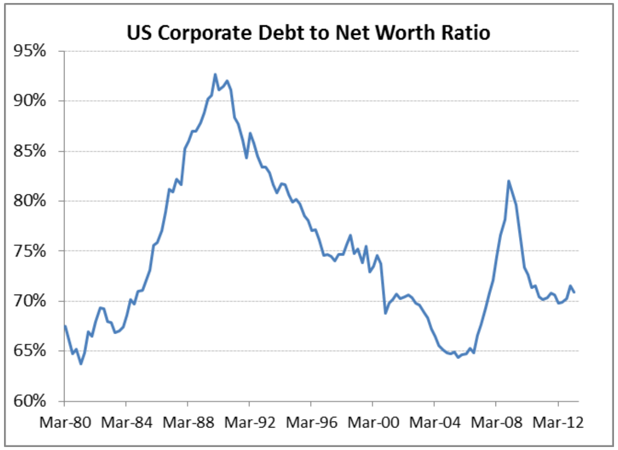
- US corporate profits fell 2% in 1Q13, but as a share of national income remain unusually high.



- Undistributed profits remain elevated despite higher dividends, with taxes still falling YoY.

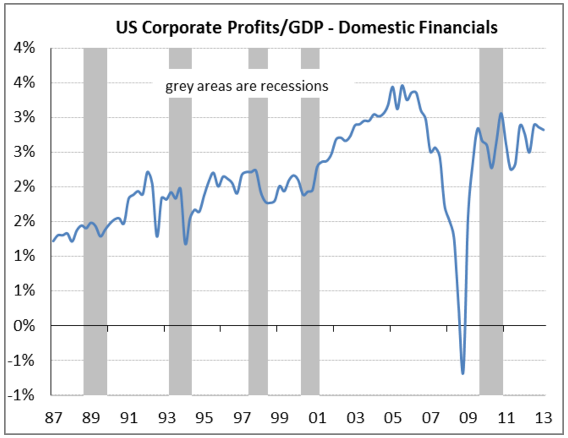


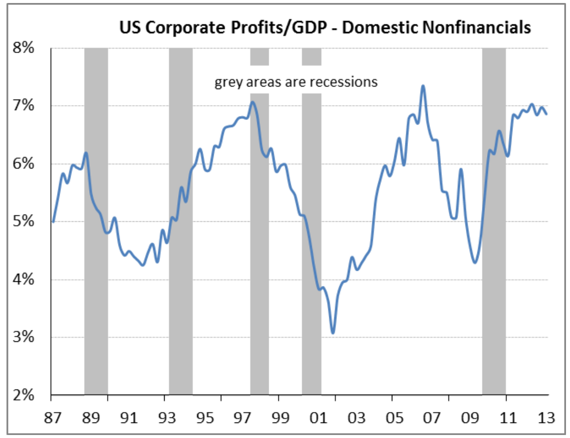
- US corporate profits leverage remains comfortably low, close to average since mid 1990s.

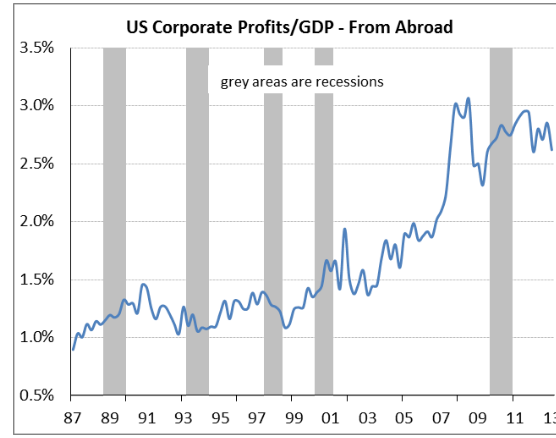


Corporate profits …. near the top

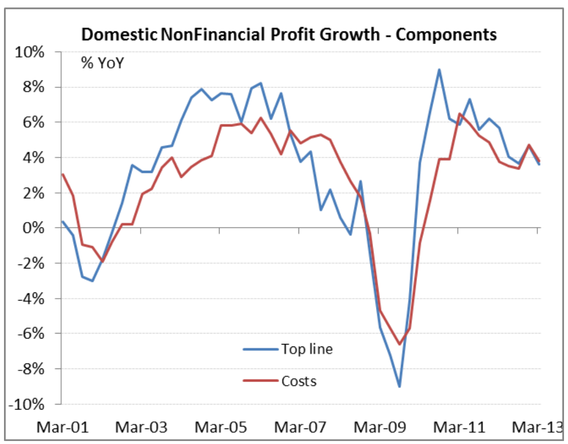
- Profits fell 2% in 1Q 2013, but for all sectors remain unusually high.

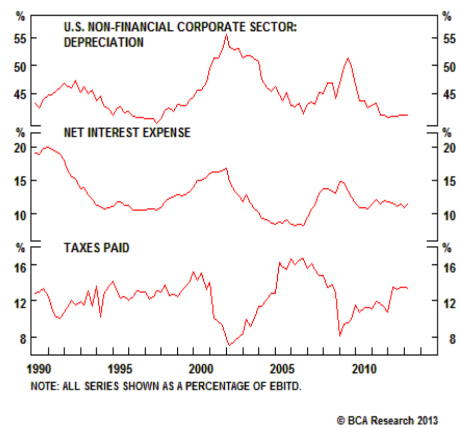


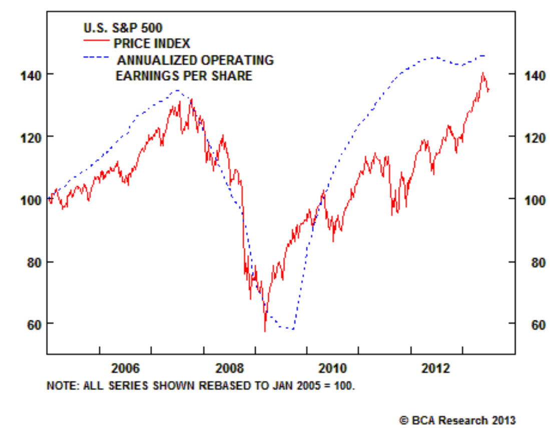




- Corporate top line and costs are both growing at 3 ½ to 4%, little different to nominal GDP.
- Caution – past tailwinds to earnings are now ending.
- And earnings growth may have peaked.

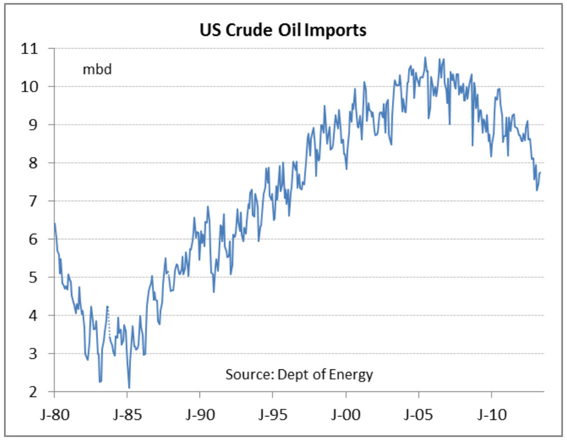


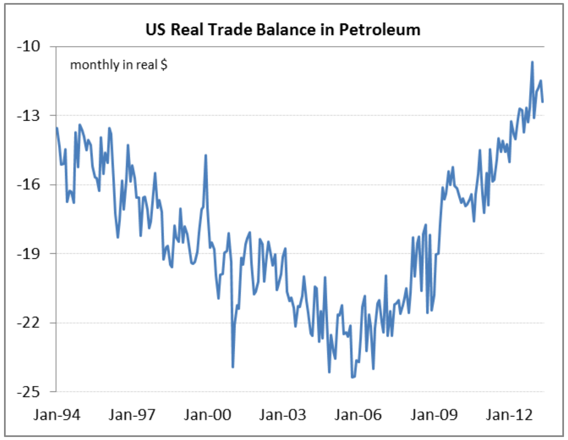


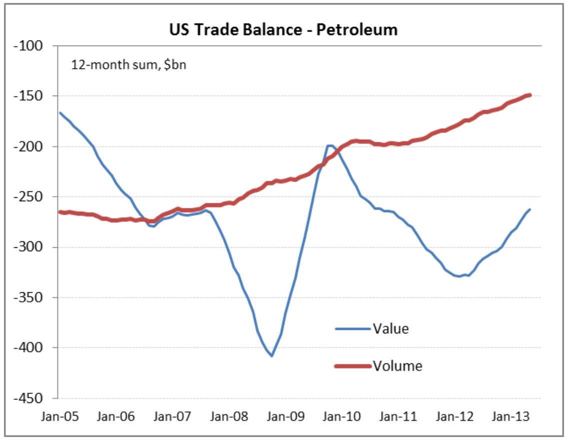


Energy sector … the most positive story

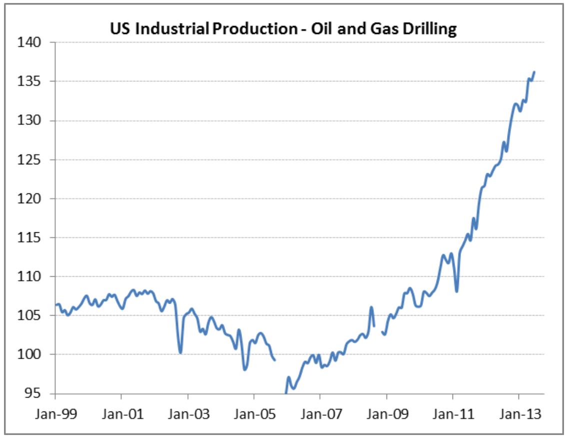
- US is importing less crude.
- This year real (volume) of petroleum product exports +5.5% YoY, real imports -8.3% YoY.
- … although the value of improvement depends on price

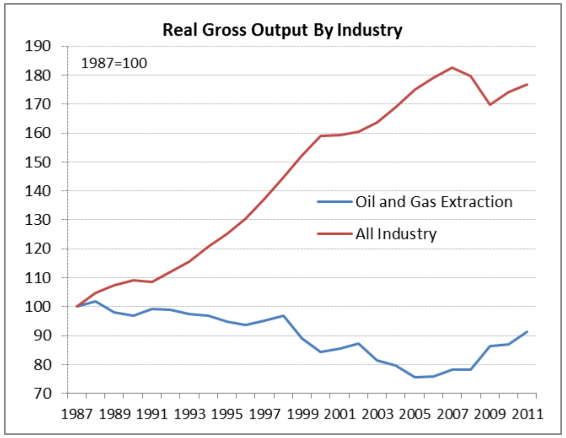


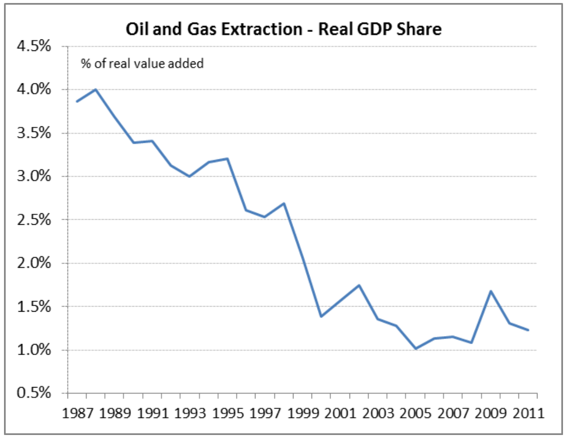




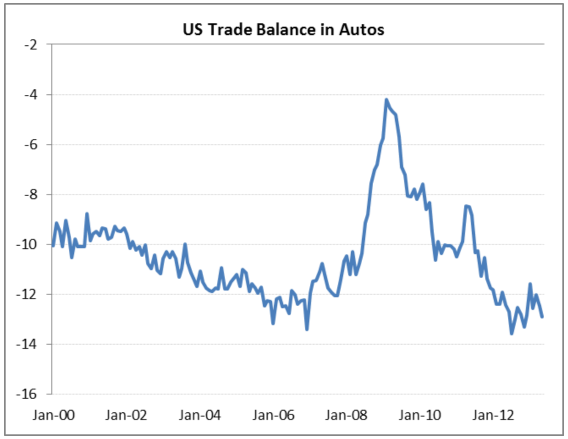
- Surge in contribution to IP since 2009.
- 10% per annum growth in real value added in oil and gas extraction would contribute 0.125% per annum to real GDP growth.



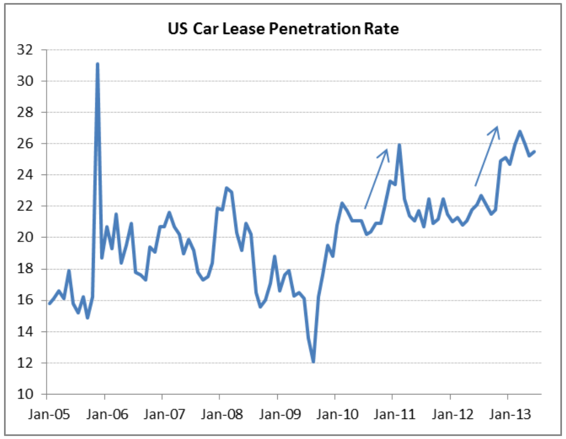




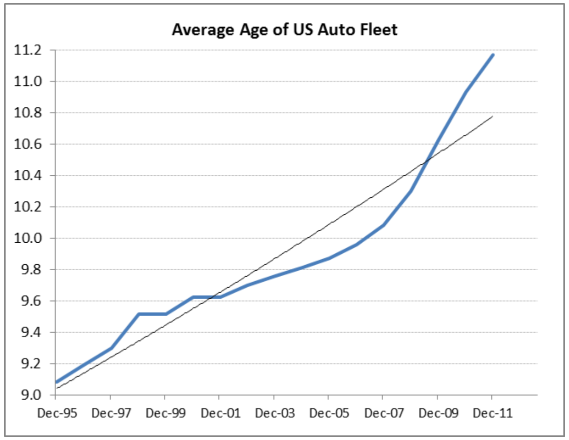
- Auto exports and imports are both growing at around 2% year on year.



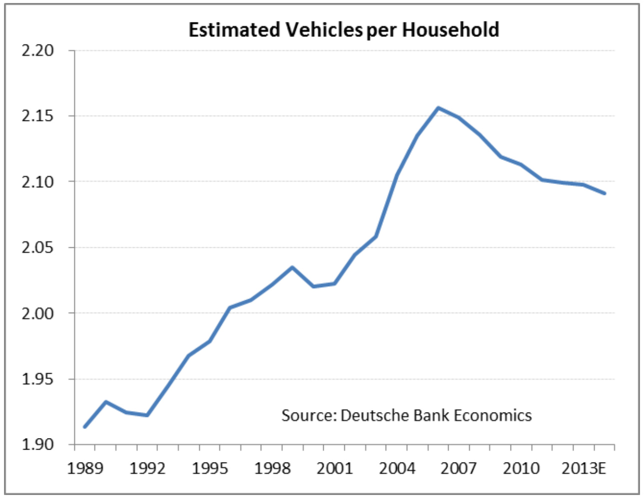
- There has been a jump in expiring leases.



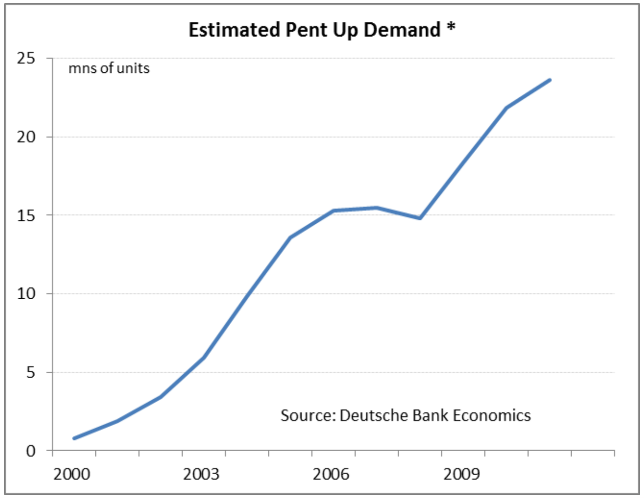
- Ageing fleet = pent up demand.



- Drop in cars per household since recession.



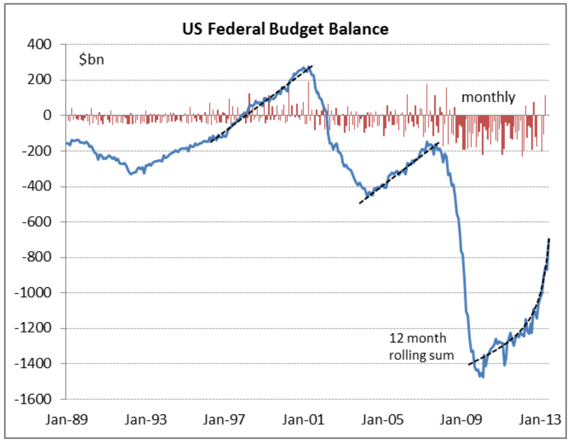
- One estimate of pent up demand for cars is in excess of 20 million units.



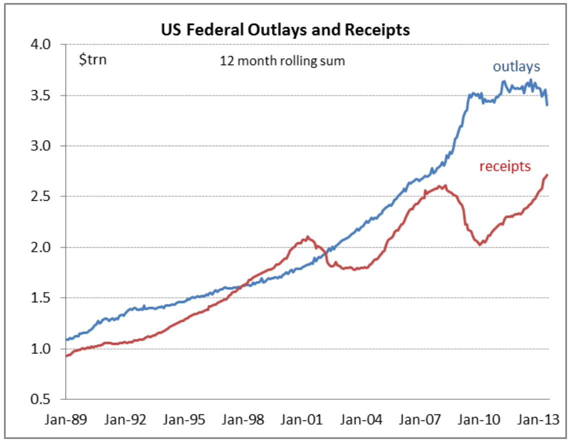
vi. Government sector

Public sector deleveraging starts to gel

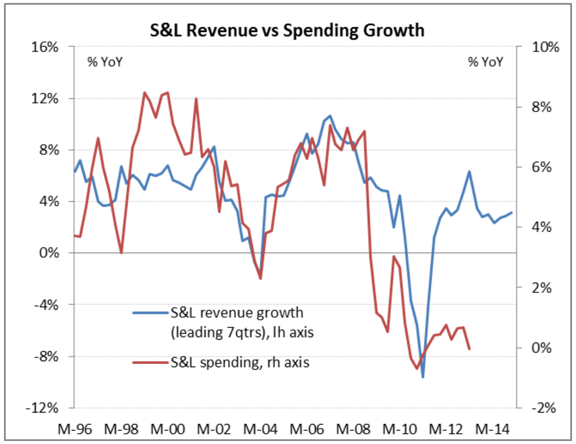
- Federal deficit down to $694bn in the year to May, from $1230bn a year earlier.



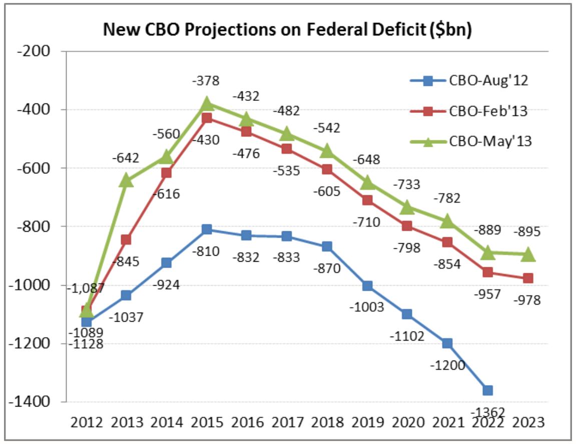
- Drop in May outlays largely due to $60bn div payment by Fannie Mae (neg outlay).



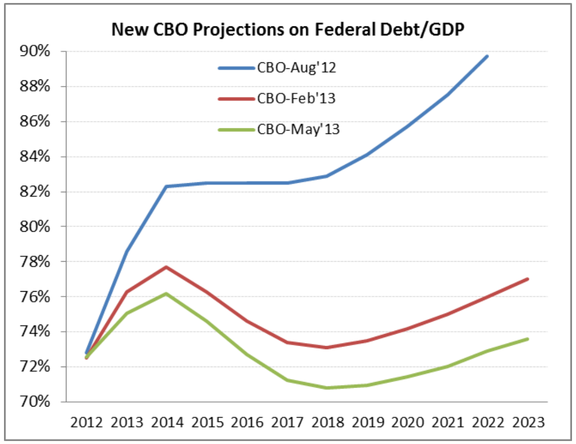
S&L deficits are narrowing too as receipts recovery leading outlay rebound.



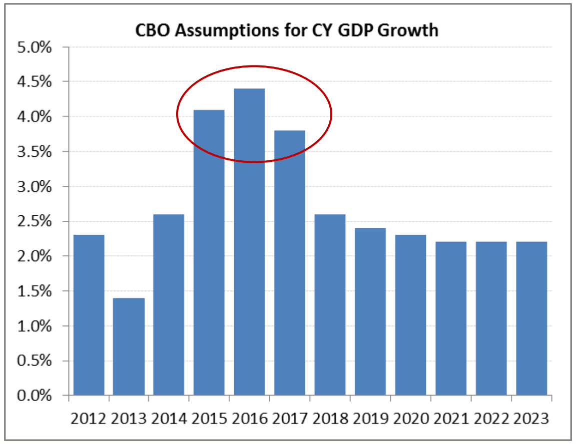
- Latest CBO estimates in May further reduce expected deficit trajectory.



- Resulting in a less onerous near term peak in debt/GDP.

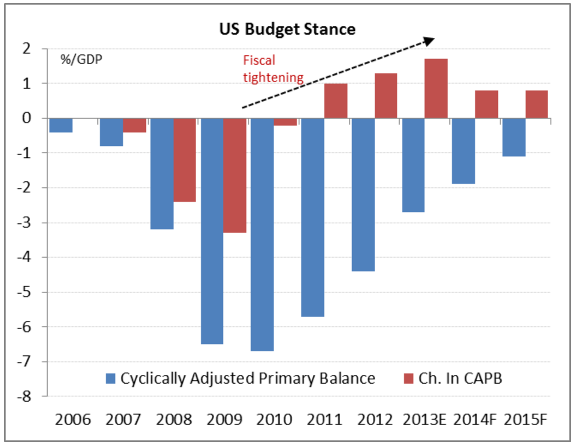


- That said, the CBO growth projections might be optimistic in 2015-17.

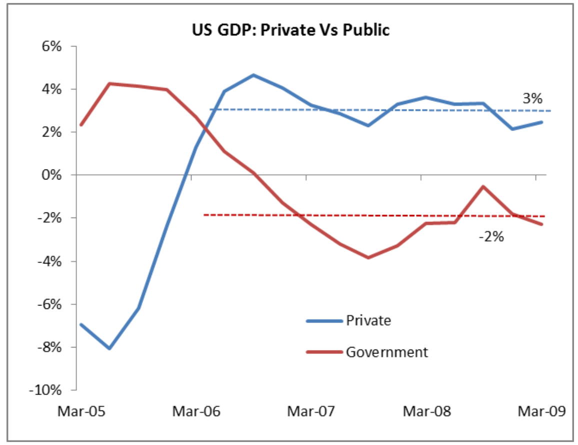


Near the max. point of fiscal drag

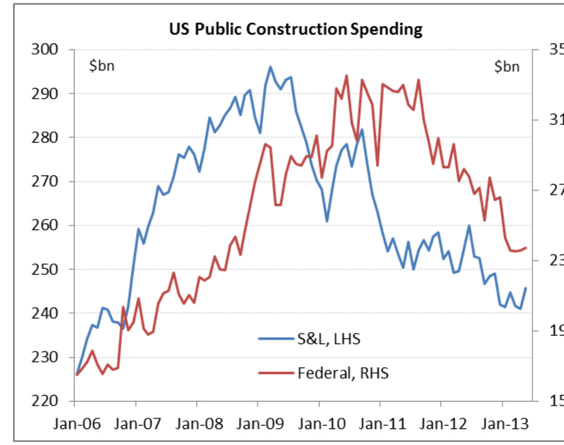
Fiscal drag reaching its max point



Might the economy grow at 3% when fiscal drag ends?

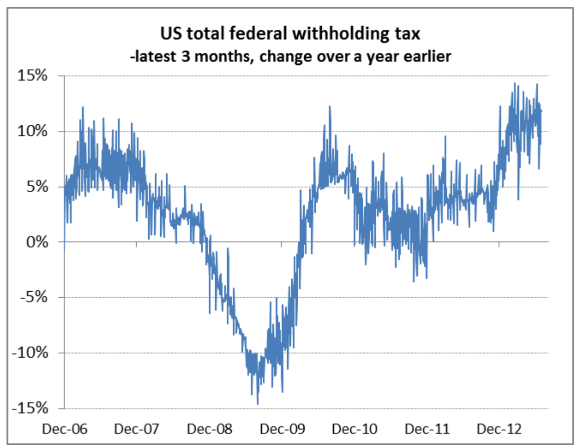


Public sector construction spending appears to be bottoming.



Sequester may show up in July income data for government workers.

- Private income growth also restrained by around 12% YoY growth in w/holding tax.



…. and federal Income tax refunds are down