Swiss Re

Early 2014 tapering is expected to last six months, says Swiss Re Chief Economist, Kurt Karl

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New York, 30 October 2013 – After today's decision by the Federal Reserve to maintain the target fed funds rate at zero to 25 basis points, Swiss Re's Chief Economist, Kurt Karl, commented that tapering is now expected to begin in early 2014 and end by Q3 of next year.

Karl said: "The tapering and an improving growth outlook will push up the yield on the 10-year Treasury note to 3.1% by end-2014."

He continued that Real Gross Domestic Product (GDP) growth has been weakened this quarter by the government shutdown and from the uncertainty created by the debate on the debt ceiling, but Q4 growth is still expected to be stronger, at 2.3%, than Q3, which was likely to have expanded by close to 1.2%. This improving growth outlook will continue next year and into 2015, lowering the unemployment rate to below 6.5% by Q1 of 2015. Thus, the Fed is expected to begin raising the fed funds rate in early 2015, which will help boost the yield on the 10-year T-note close to 4% by end-2015.

He further added: "Prospects for growth in Europe continue to improve, with Spain posting its first positive GDP growth in two years, the UK economy strengthening and continental Europe pulled along by the German juggernaut. The euro area recovery is expected to continue, but at a moderate pace, and remain fragile. A more robust upswing is being prevented by fiscal austerity, private sector deleveraging, structural rigidities and tight credit conditions in the peripheral economies. Yields on the 10-year German bunds will rise to 2.3% by end-2014."

He commented that the modest slowdown in growth in the US is not expected to significantly affect the rest of the world. Our outlook for the Euro area, the UK and Japan remain unchanged from last month with real GDP growth in 2014 expected to be 1.0%, 2.2% and 1.5% respectively. The yield on the 10-year gilts will be about 3.3% by end of next year, while Japan's 10-year government bond yield will climb to 1.1% as inflation picks up.

He also said: "China is expected to avoid a hard landing and grow by 7.8% next year. Credit conditions will be monitored carefully by the authorities, but allowed to be sufficiently loose to support this slight increase in growth. The tax increase in Japan is expected to be implemented on schedule in April, but will not cause a recession given the monetary and fiscal expansion already underway."

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