



# The US Economic Outlook

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State of Montana Teleconference  
September 14, 2012

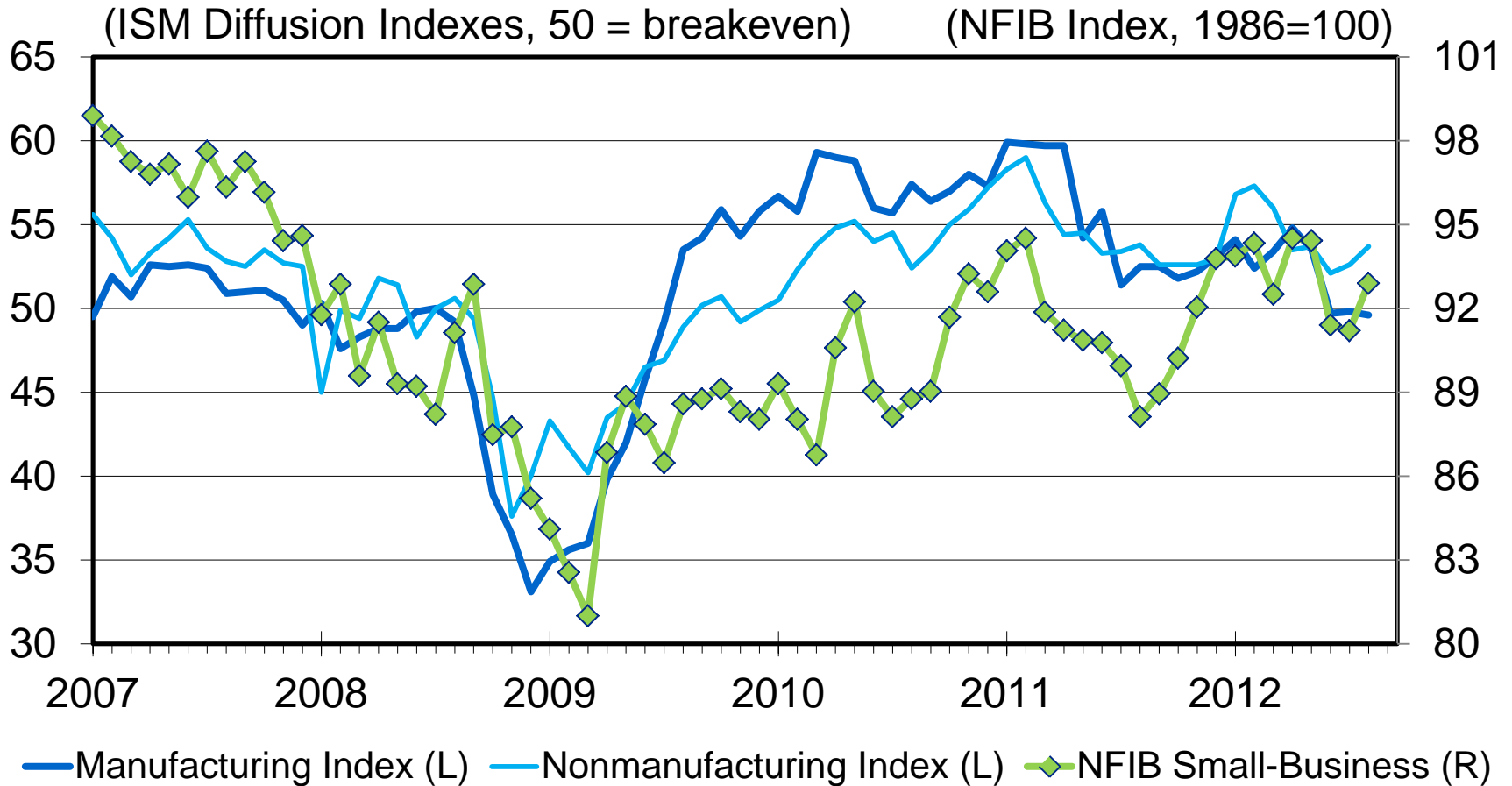
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# The U.S. Outlook: Not Yet Firing On All Cylinders

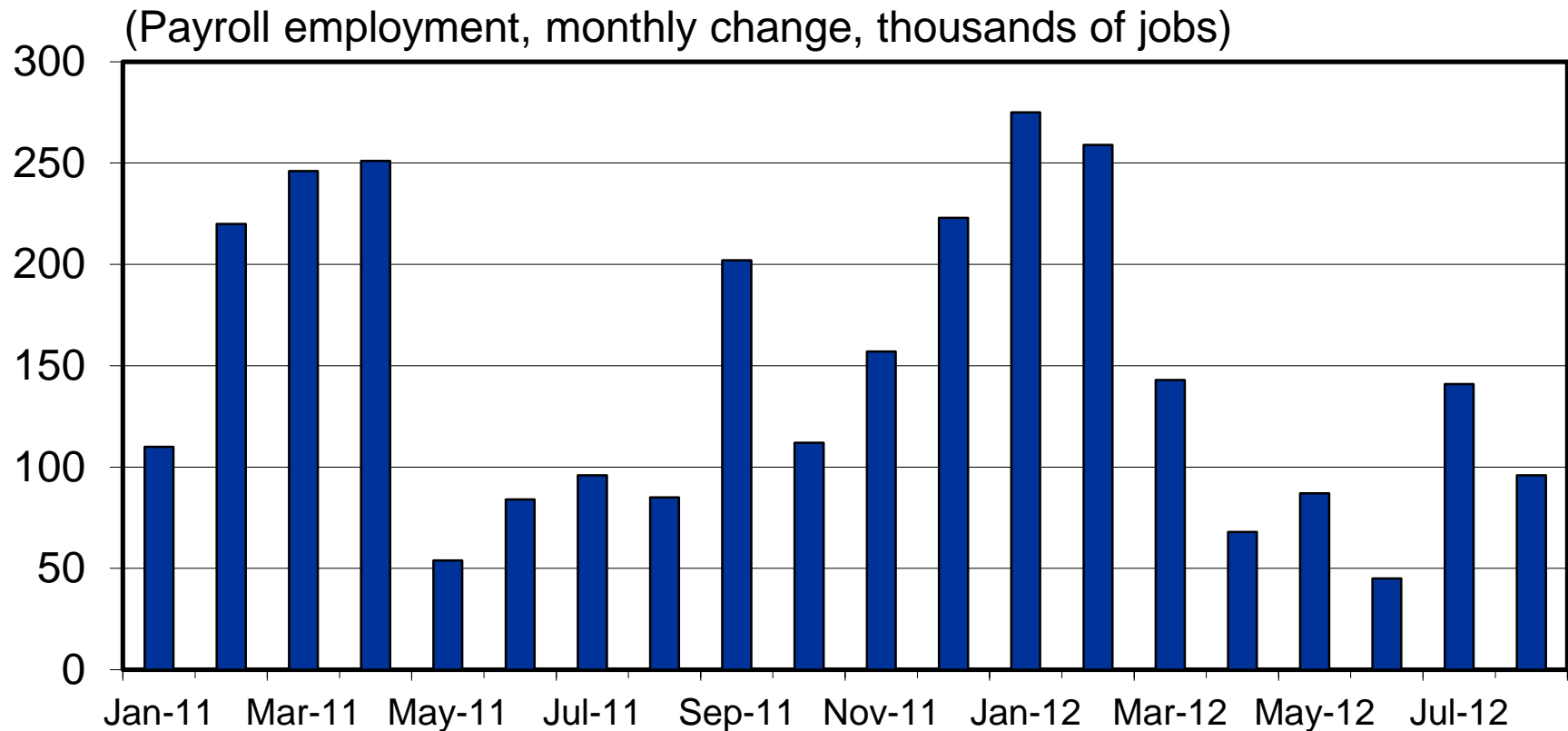
- Bad News: Domestic momentum is modest. Hiring is cautious.
- Bad News: Foreign weakness and stronger dollar dampening export growth, increasing import competition. Manufacturing has slowed.
- Bad News: Gasoline prices have risen again; and drought will raise food prices
- Bad News: No early resolution of “fiscal cliff” likely. Uncertainty dampens risk-taking.
- Good News: Housing activity and prices edging higher. Housing activity is still way below demographic norms.
- Good News: Credit conditions and demand for credit gradually improving
- Continued modest growth is the most likely outcome; recession risk 20%

# Manufacturing Led The Recovery, But Has Slowed

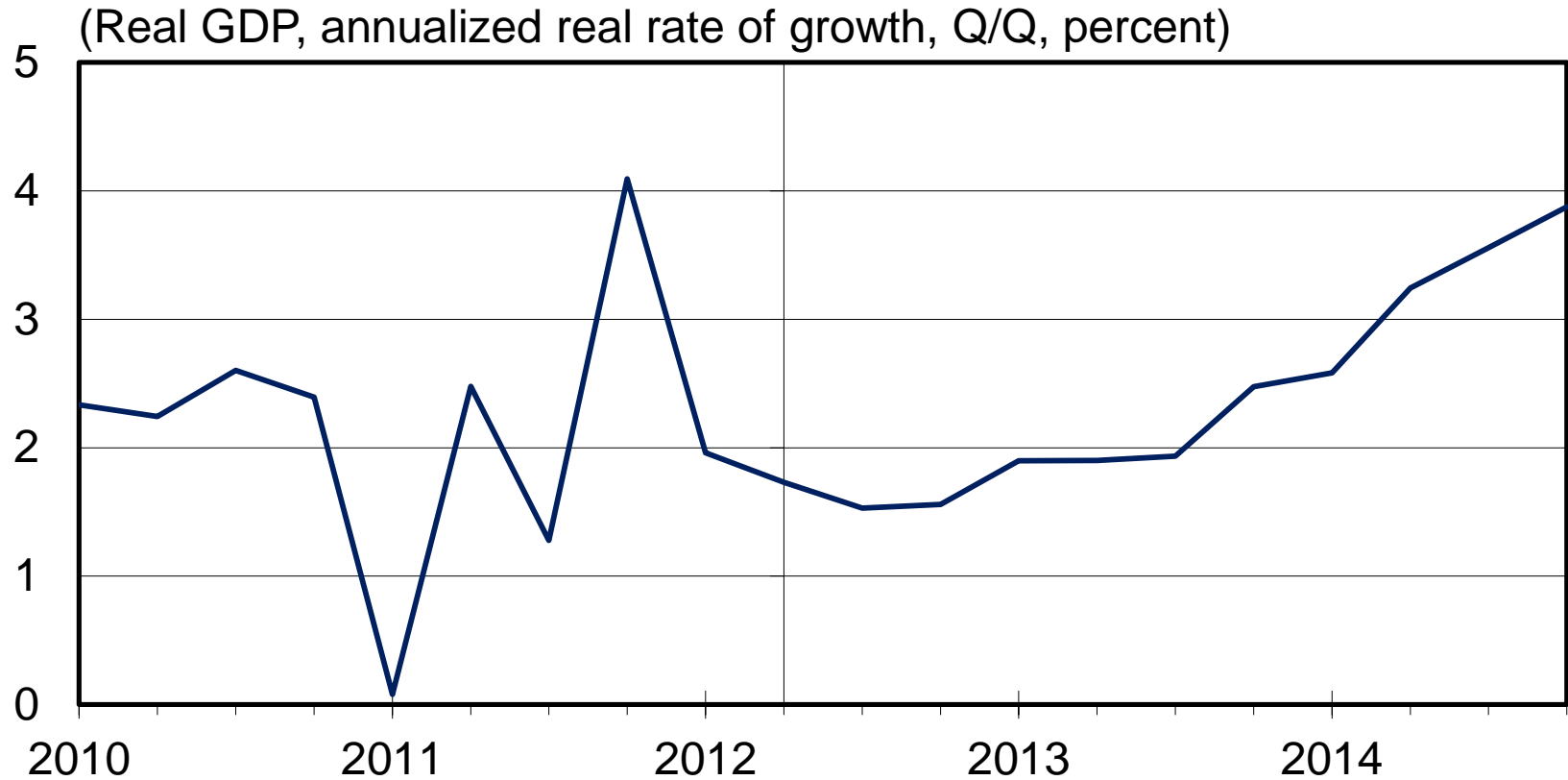


ISM = Institute for Supply Management; NFIB = National Federation of Independent Business

# August Employment Disappoints After July Improvement: Still Better Than Q2 Numbers, Though



# Recovery Struggling To Gain Traction





# U.S. Economic Growth by Sector

(Percent change unless otherwise noted)

	2011	2012	2013	2014
<b>Real GDP</b>	1.8	2.2	1.8	2.8
<b>Final Sales</b>	2.0	2.0	1.9	2.7
<b>Consumption</b>	2.5	2.0	2.3	2.6
<b>Light Vehicle Sales (Millions)</b>	12.7	14.2	14.8	15.6
<b>Residential Fixed Investment</b>	-1.4	10.8	11.8	20.2
<b>Housing Starts (Millions)</b>	0.61	0.76	0.94	1.24
<b>Business Fixed Investment</b>	8.6	8.0	4.8	7.3
<b>Federal Government</b>	-2.8	-2.5	-3.2	-3.1
<b>State and Local Government</b>	-3.4	-1.6	-0.8	0.1
<b>Exports</b>	6.7	4.0	3.7	4.7
<b>Imports</b>	4.8	3.1	4.0	5.1



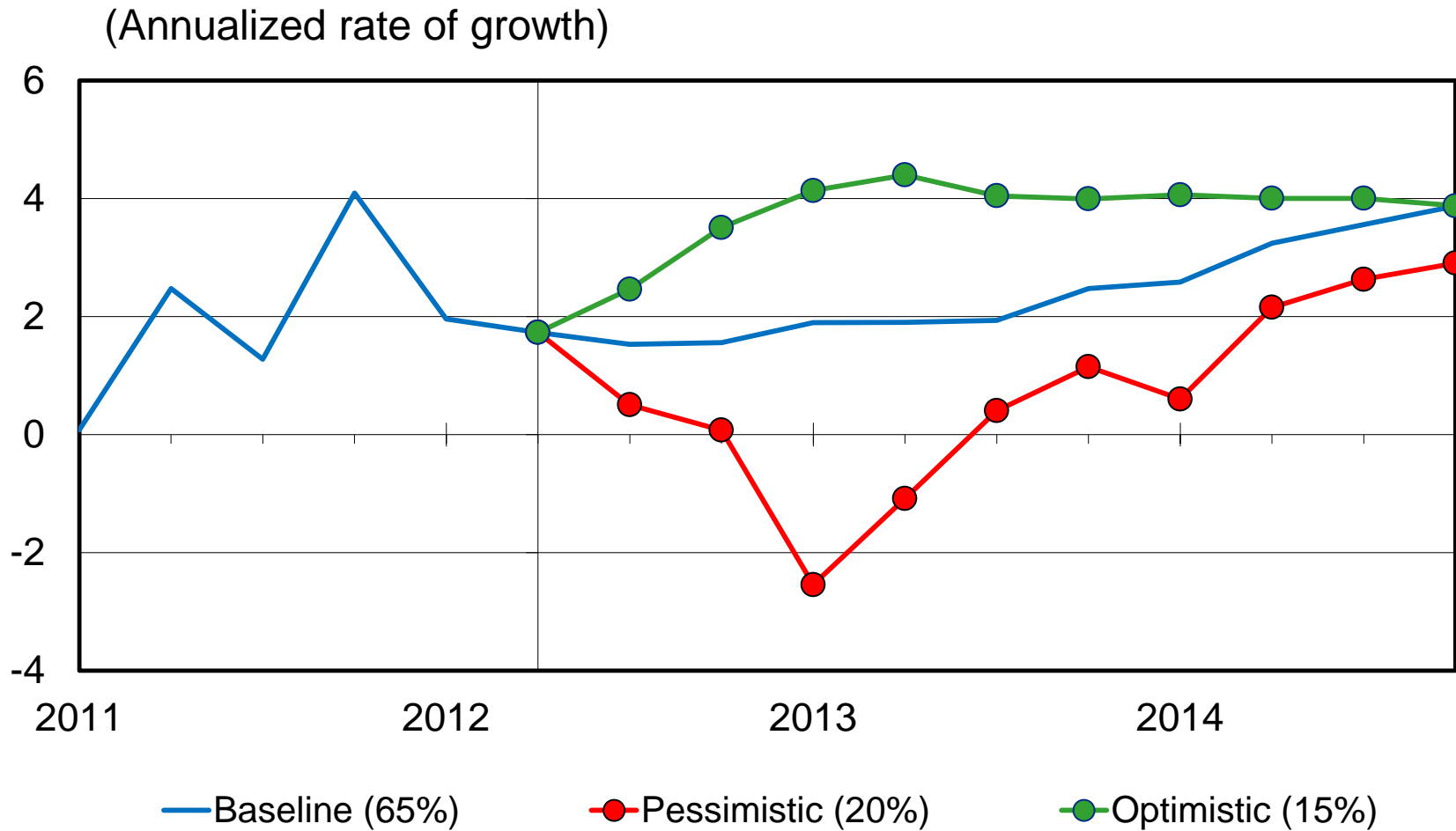
## Other Key Indicators

(Percent unless otherwise noted)

	2011	2012	2013	2014
<b>Industrial Production (% growth)</b>	4.1	4.0	2.2	2.7
<b>Employment (% growth)</b>	1.2	1.4	1.4	1.6
<b>Unemployment Rate</b>	9.0	8.2	8.0	7.7
<b>CPI Inflation</b>	3.1	2.0	1.4	1.8
<b>Oil Price* (Refiners, \$/bbl)</b>	102	100	89	85
<b>Natural Gas (Henry Hub, \$/mmbtu)</b>	3.99	2.61	3.84	4.68
<b>Core PCE Price Inflation</b>	1.4	1.8	1.5	1.7
<b>Federal Funds Rate</b>	0.10	0.14	0.16	0.16
<b>10-year Government Bond Yield</b>	2.79	1.77	2.16	2.84
<b>Dollar (Major Currencies, 2005=1)</b>	0.85	0.88	0.92	0.90

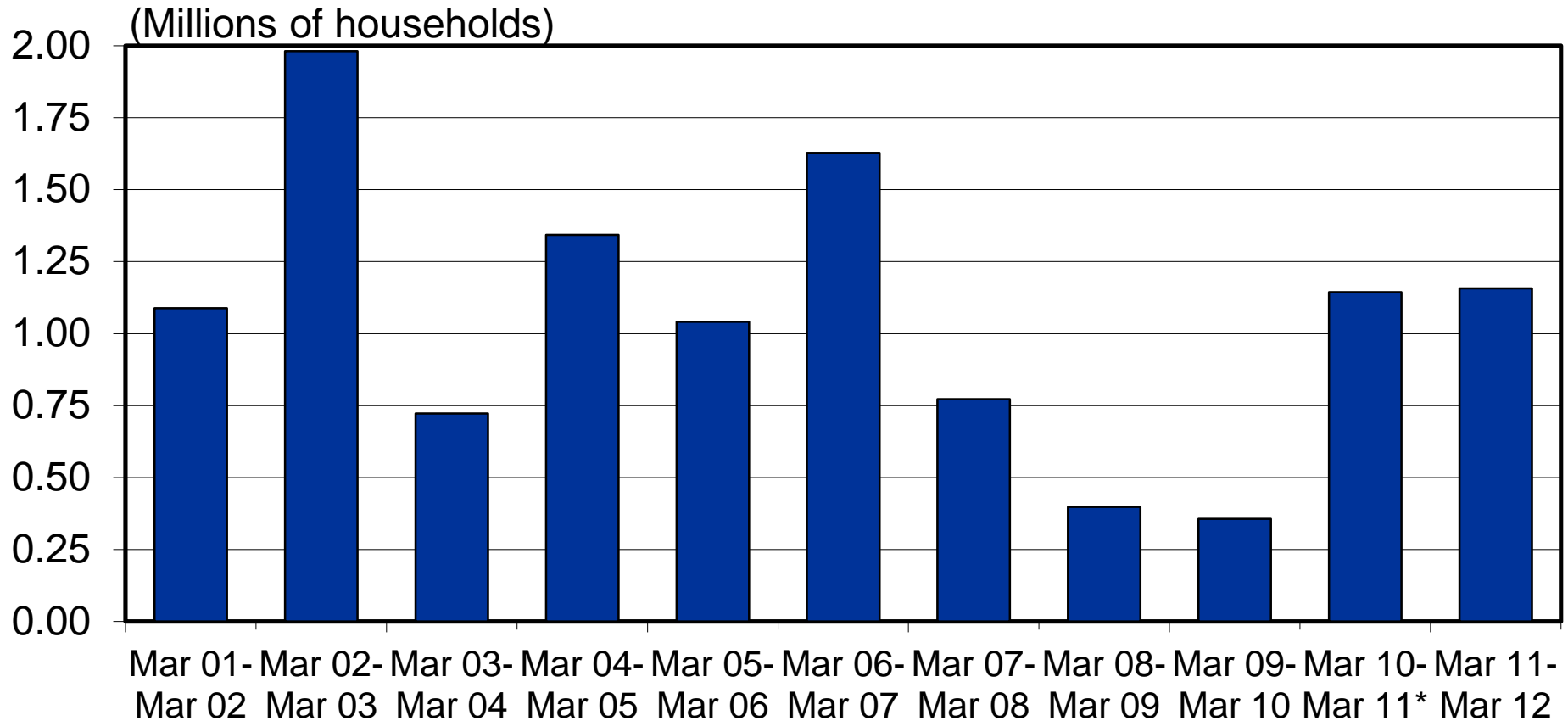
\*Refiners Acquisition Price of Crude Oil

# GDP Growth Outlook





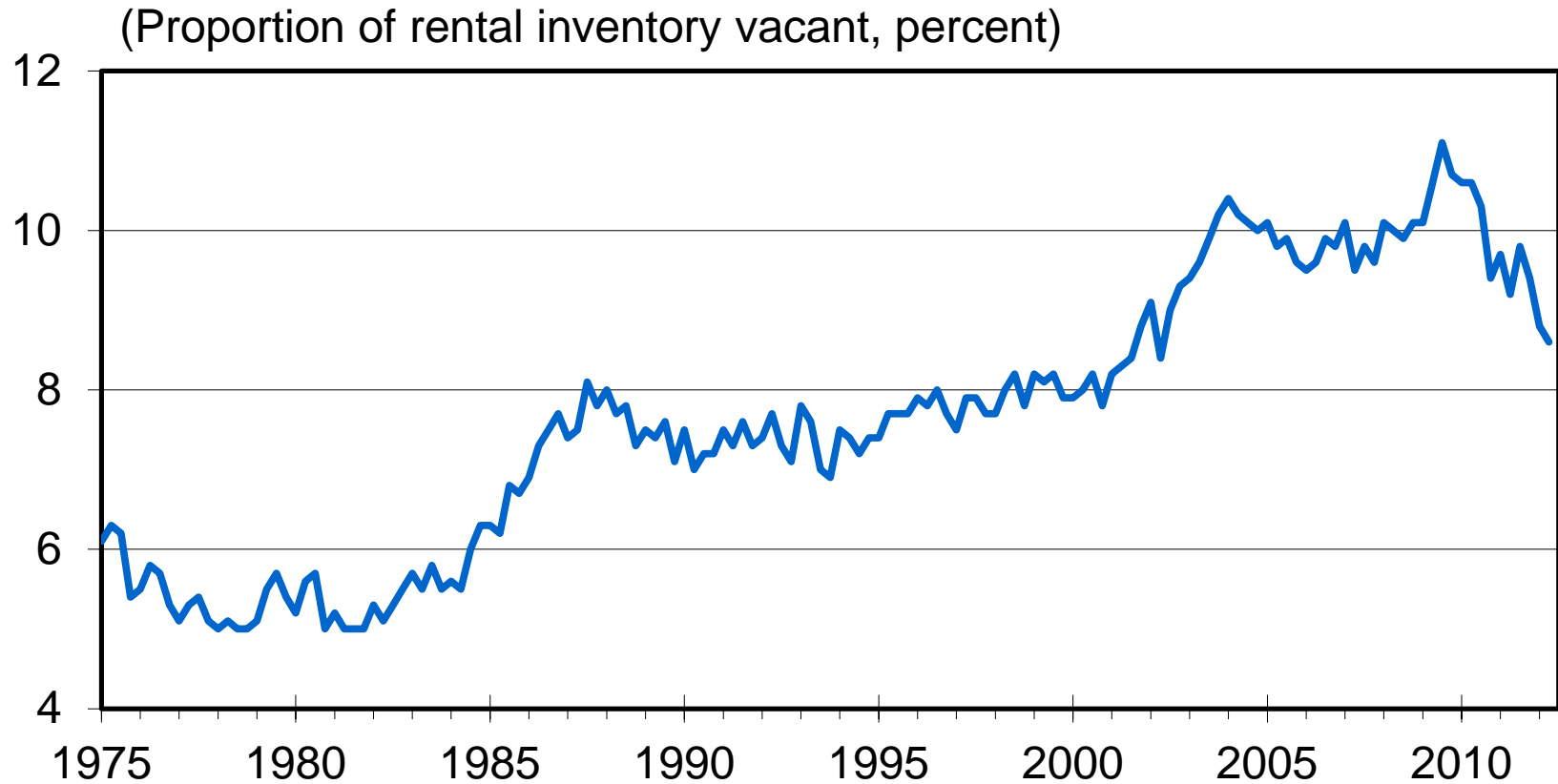
# Good News for Housing: Household Formation Is Reviving



\*The latest revised 2011 figures show 2.4 million households created, but are distorted by the introduction of new population controls. The table shows the original 2011 estimate.

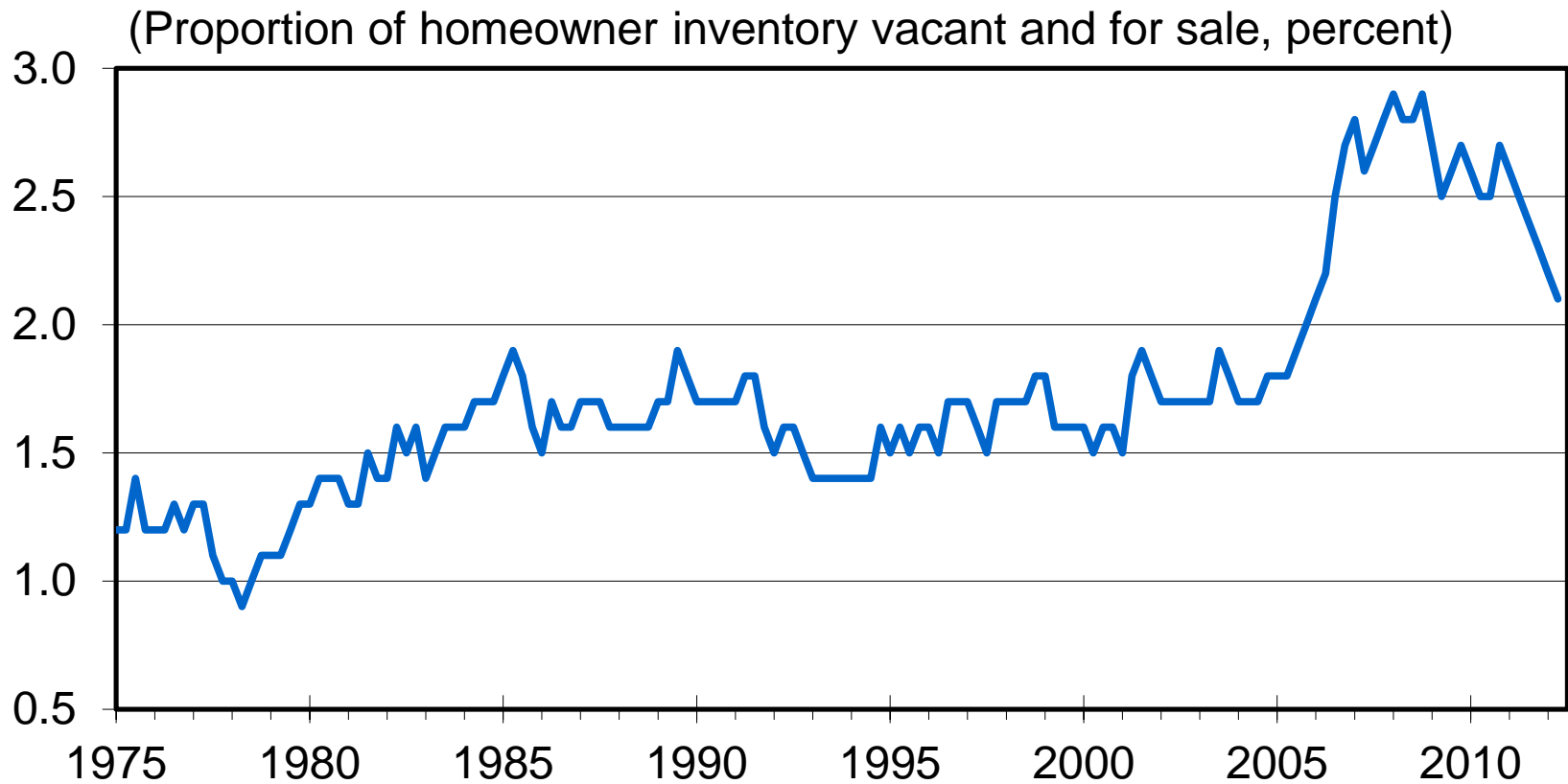
Source: Census Bureau

# Housing Market Adjustment: The Rental Vacancy Rate Has Eased



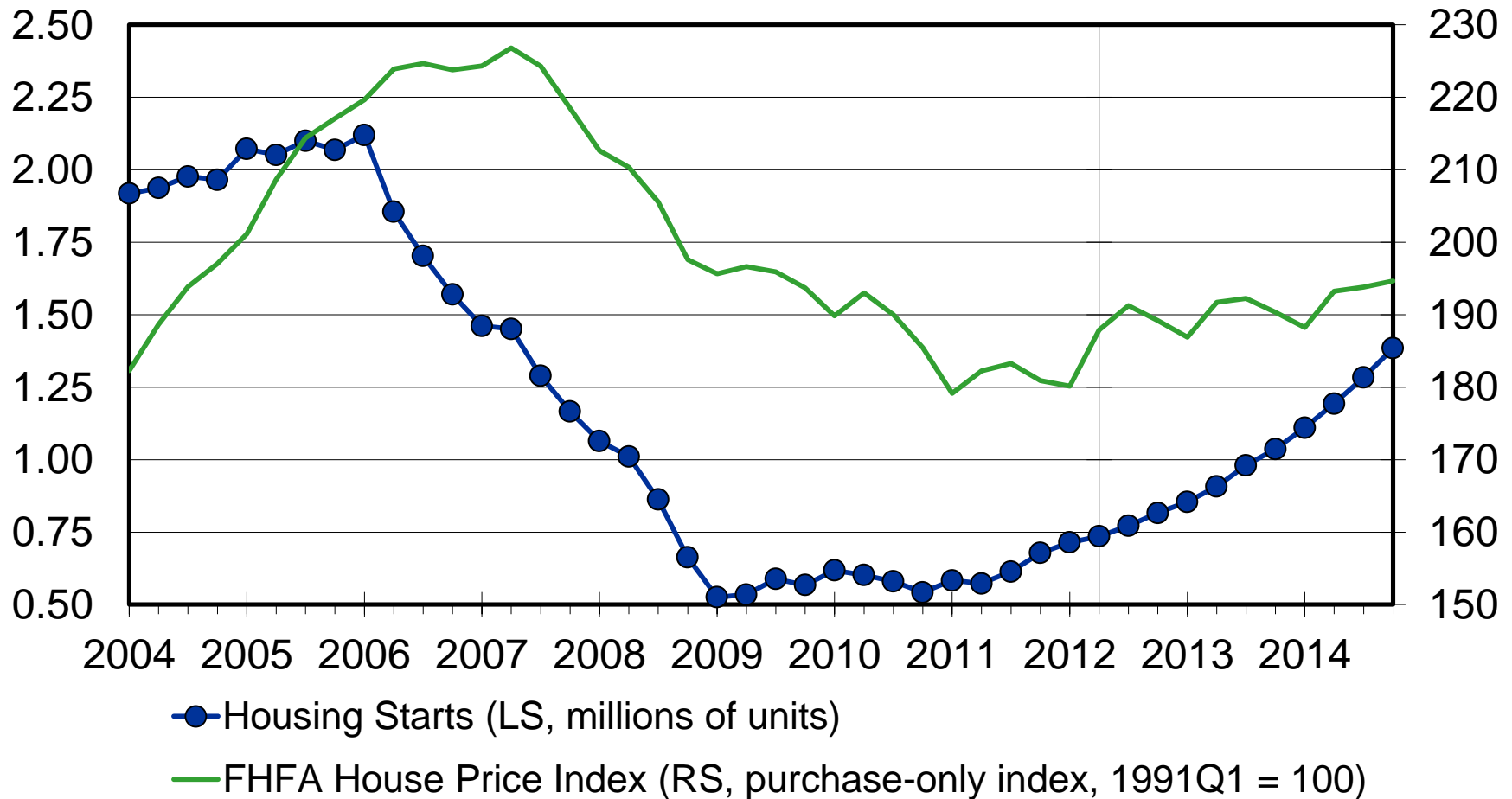
Source: Census Bureau

# Housing Market Adjustment: Homeowner Vacancy Rate on the Way Down

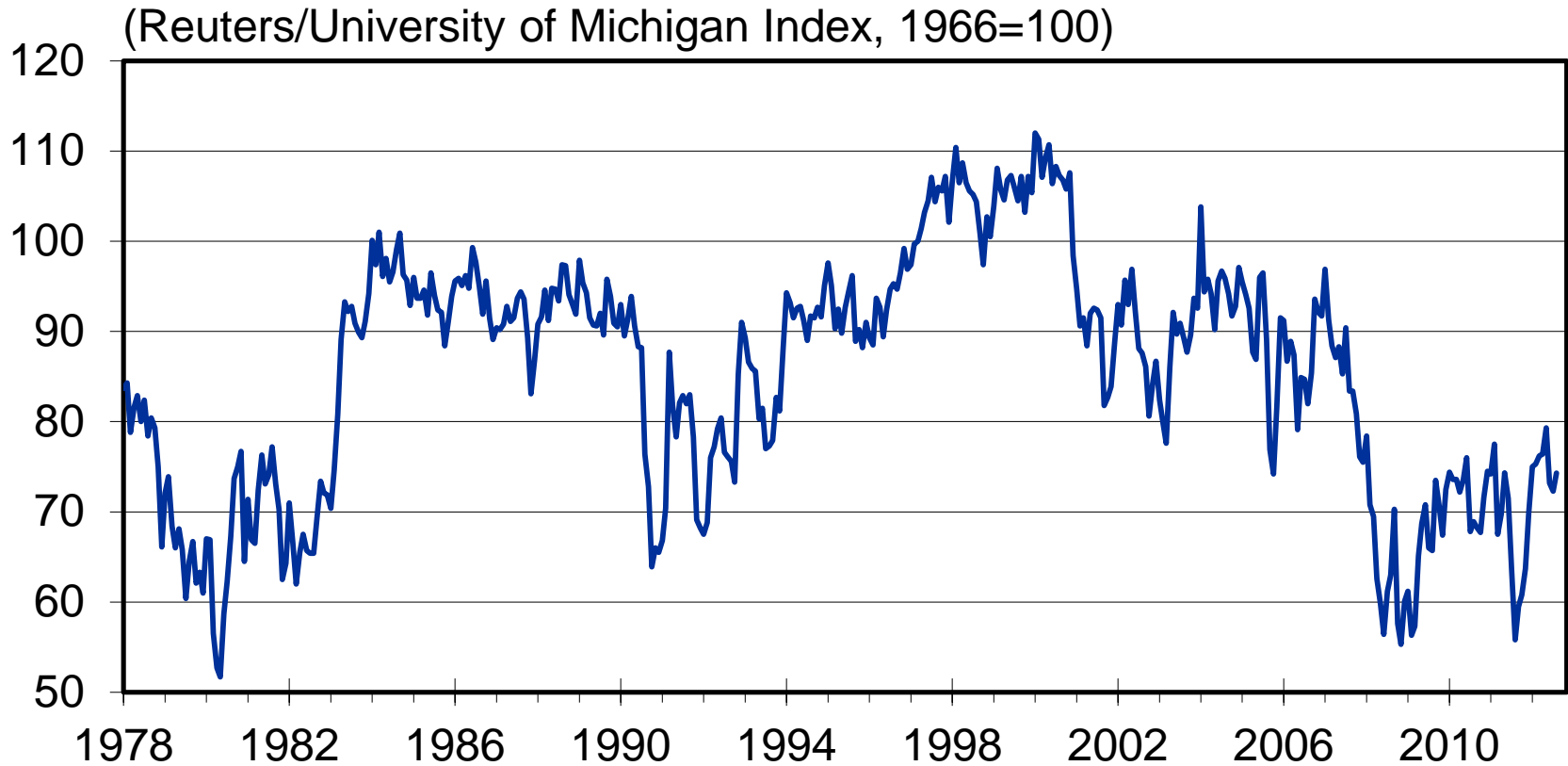


Source: Census Bureau

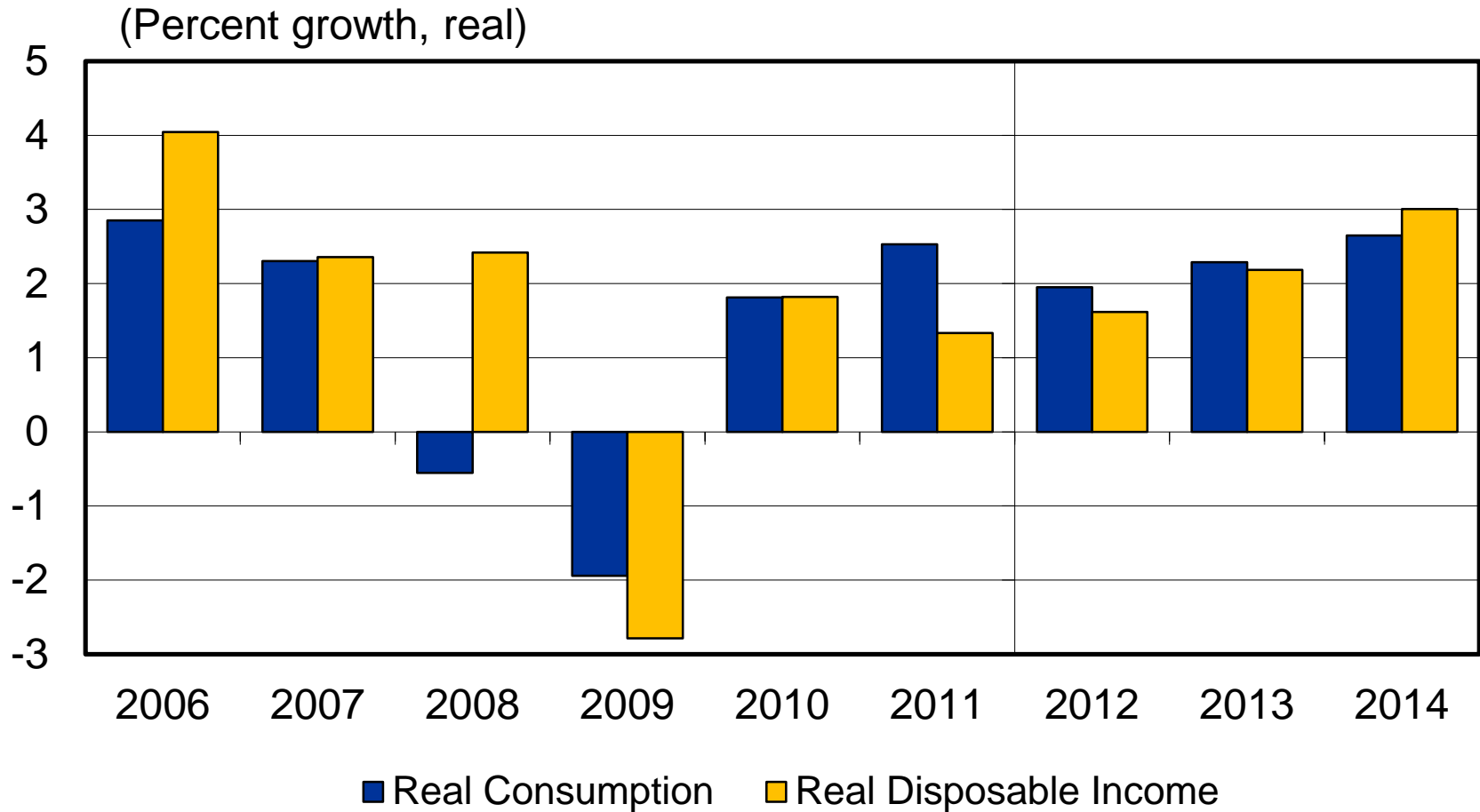
# Housing Starts Beginning a Long Climb; Prices Have Probably Hit Bottom Now



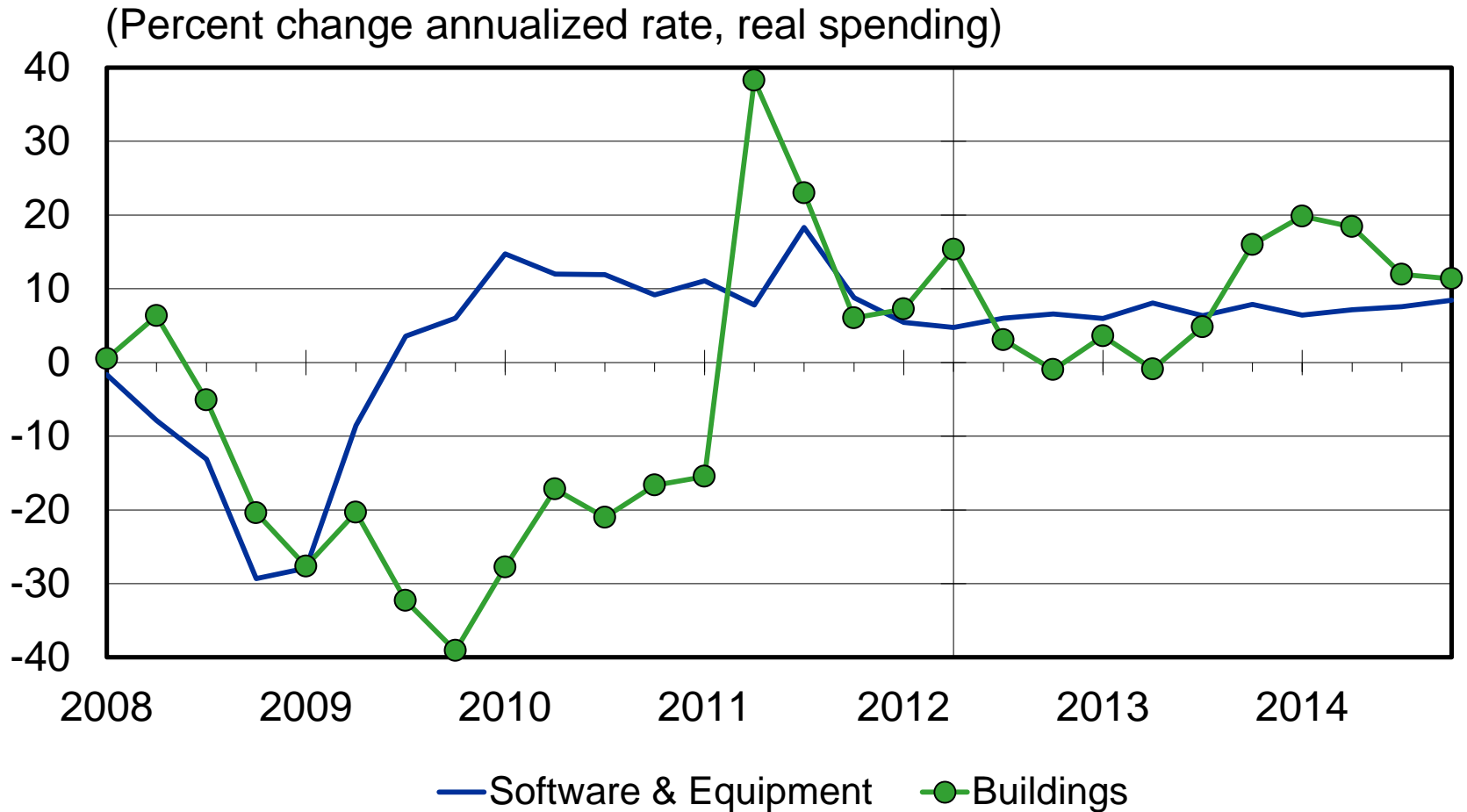
# Consumer Sentiment Off the Floor



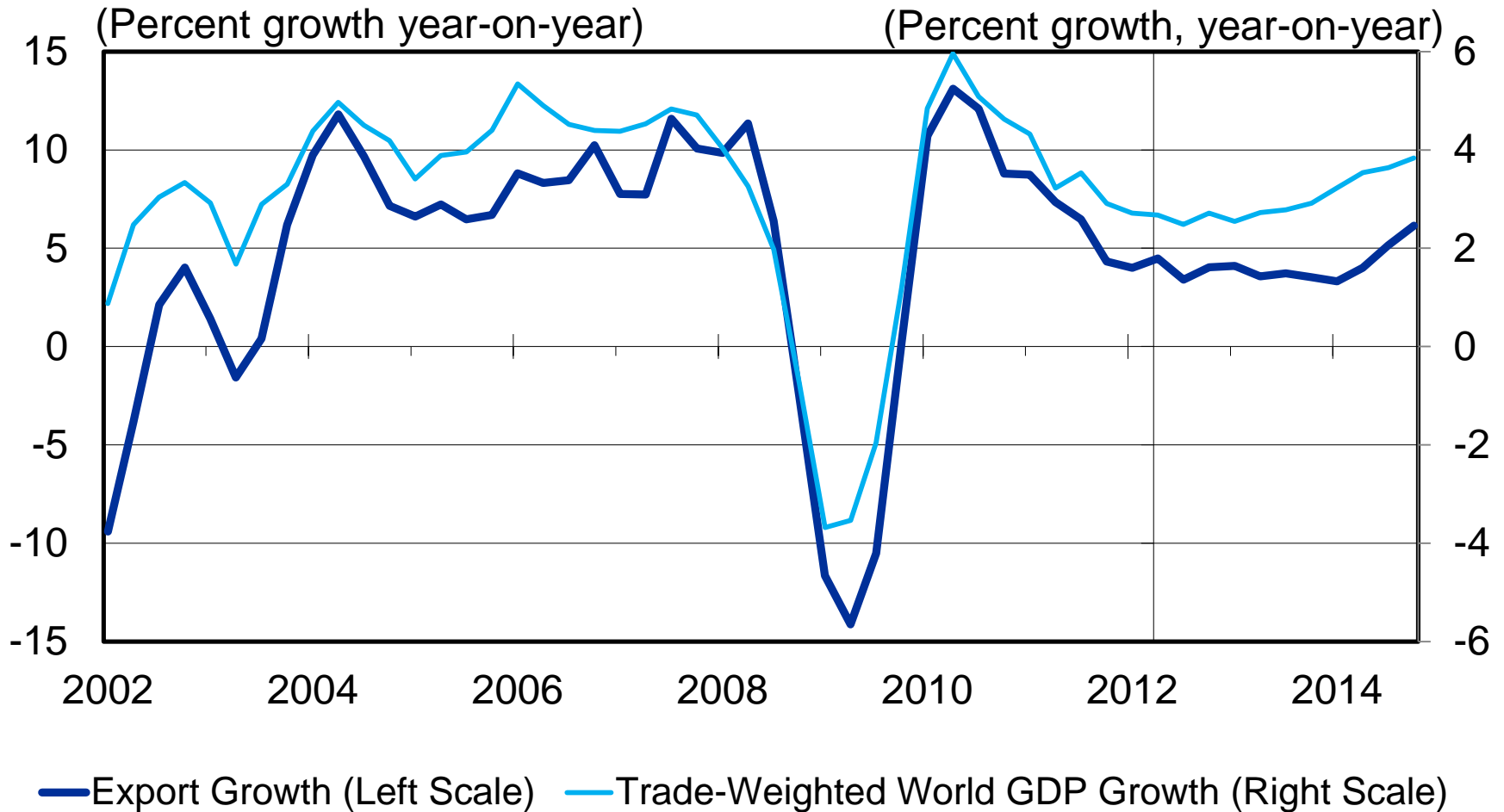
# Consumption Has An Income Problem



# The Business Capital Spending Cycle: Slower Growth in 2013



# Export Growth Cools as Trading Partner Growth Cools

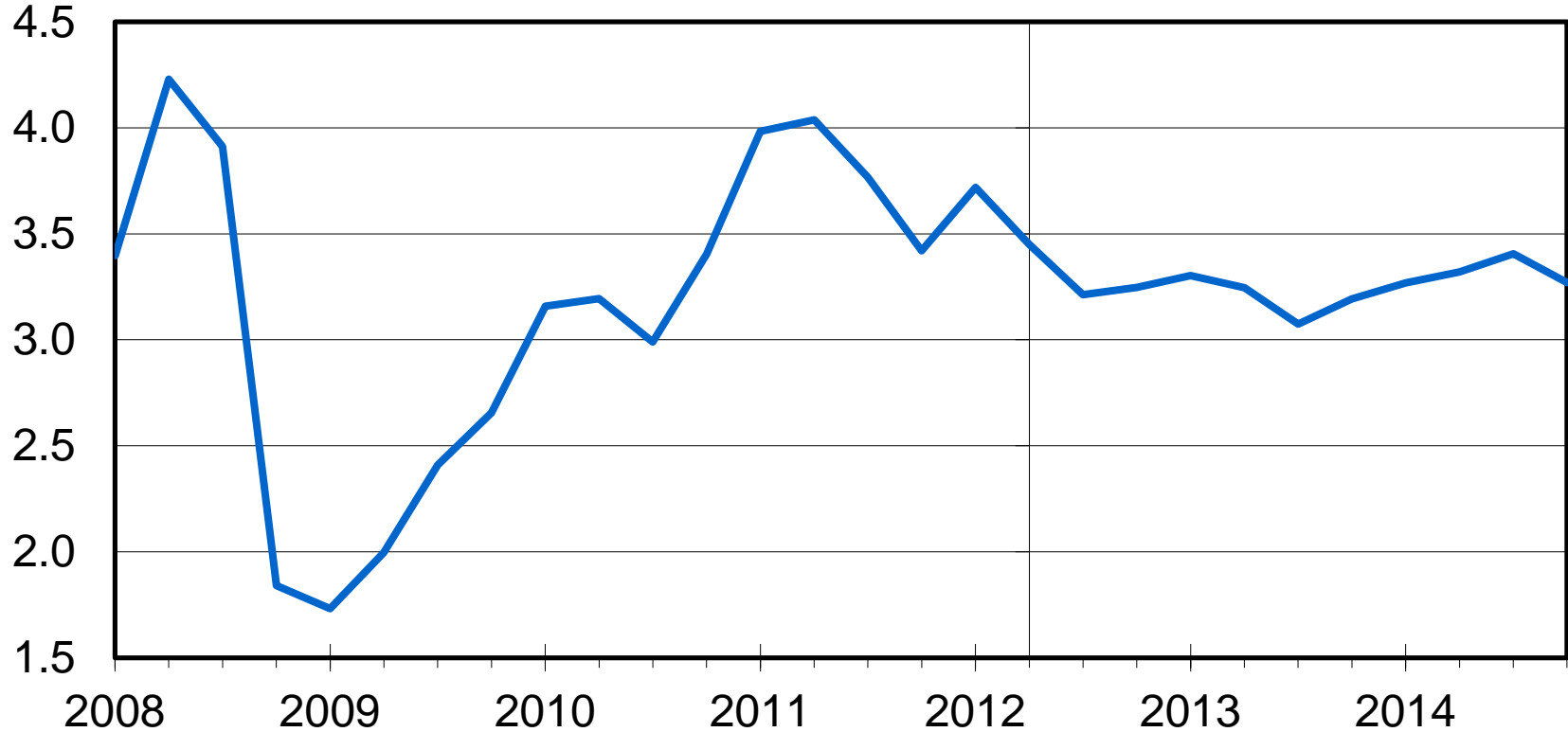




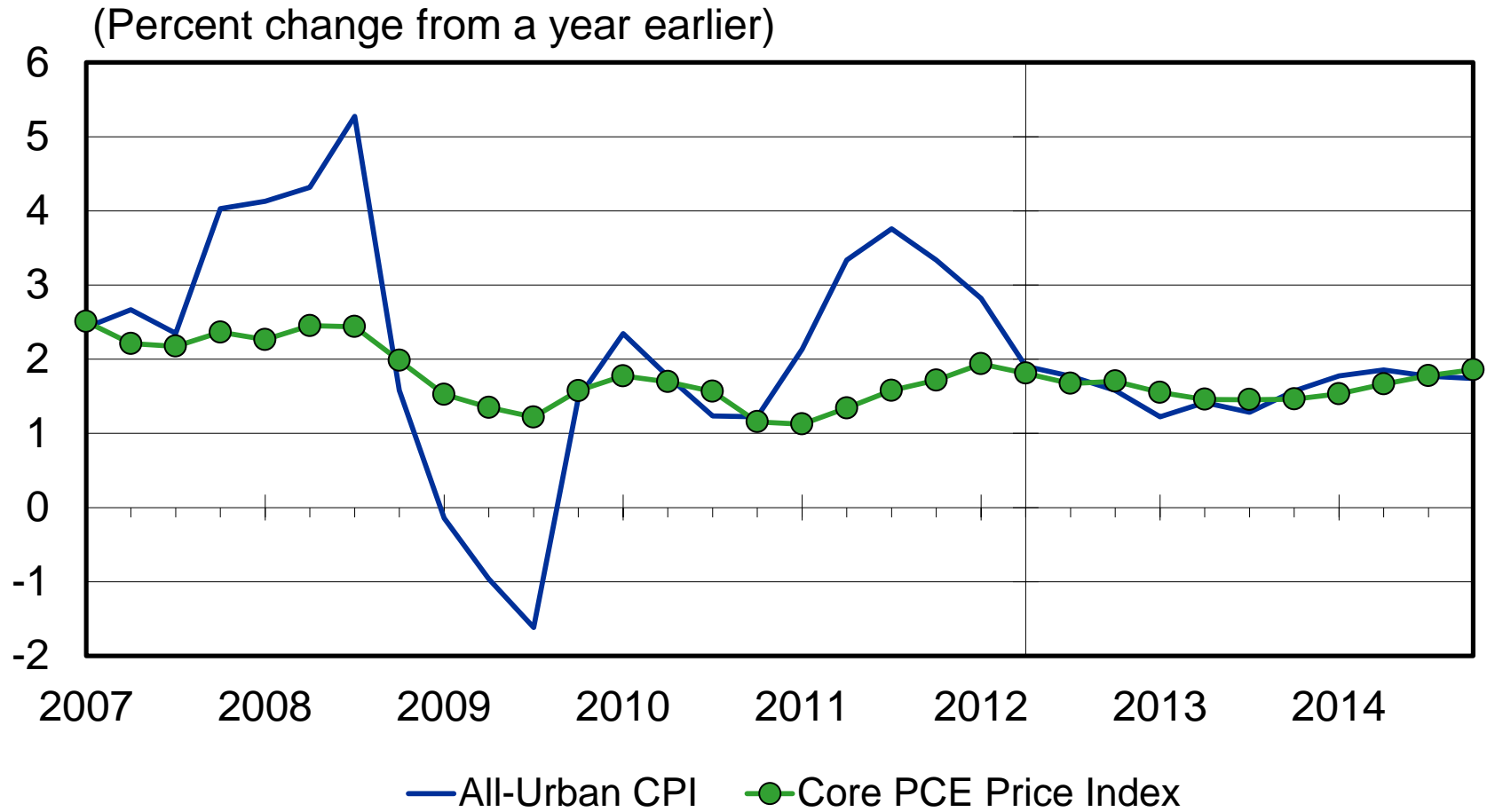
# Industrial Materials Prices: Downward Pressure From Weak Global Economy



(IHS Global Insight Index, 2002:1=1.0)



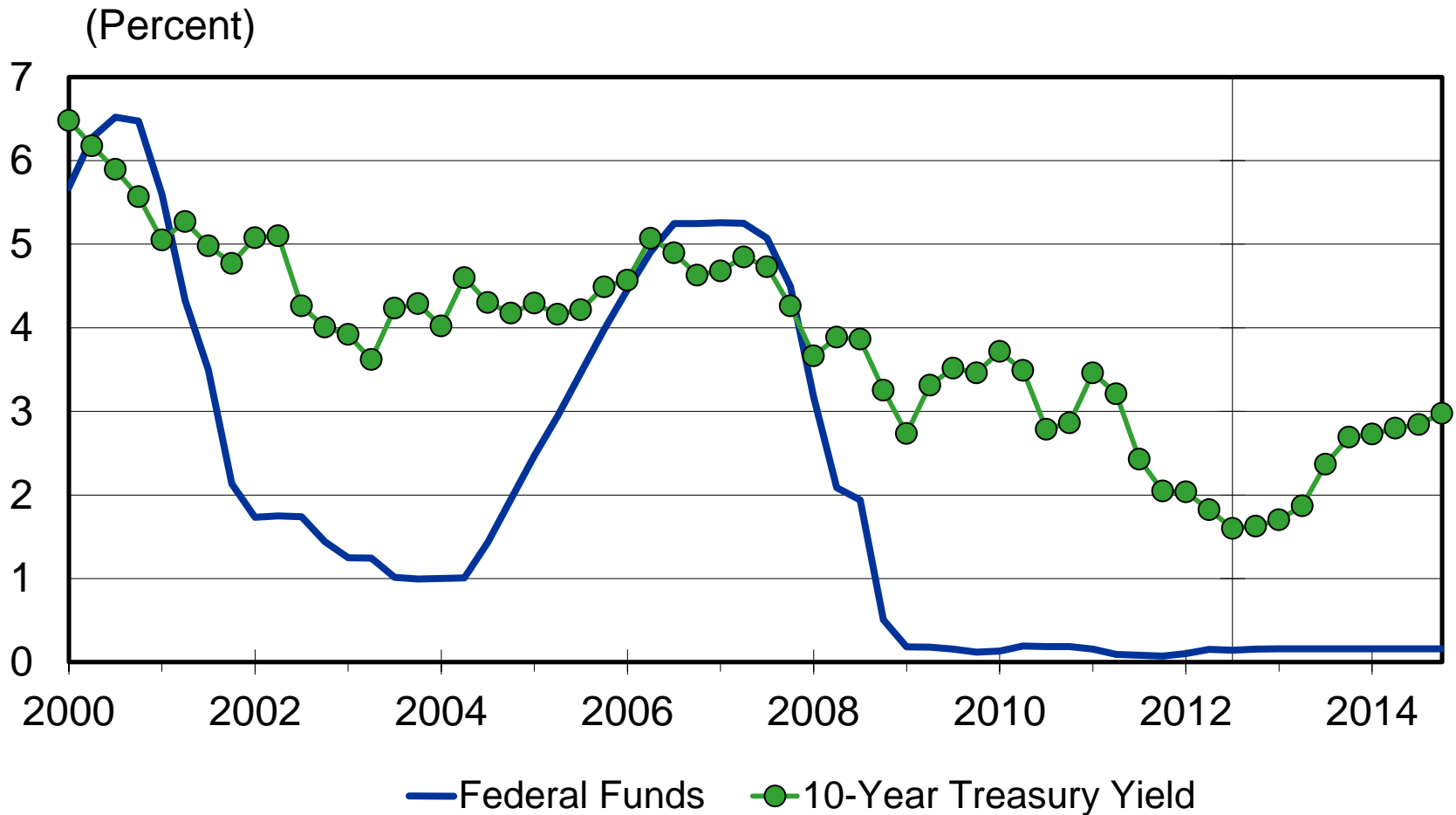
# Inflation Easing



## The Fed

- Our forecast assumes federal funds rate near zero till mid-2015, and QE3 around \$600 billion, targeted to mortgage-backed securities
- The Fed is delivering \$40 billion per month MBS purchases, open-ended
- QE3 may take mortgage spreads down 20-25 basis points
- QE3 effects on growth likely to be small...
- ...but the Fed has moved into “whatever it takes” mode...
- ...if it can succeed in inspiring confidence, the Fed’s September moves will have a bigger effect than QE3 alone...
- ...but it will hurt its own credibility if it can’t deliver the labor-market improvement it seeks

# Federal Funds Rate to Stay Near Zero Until 2015: Long Rates Stay Low



## Key Fiscal Deadlines Approaching

- September 30, 2012: Continuing Resolution Needed if no FY2013 Budget is in place
- November 6, 2012: Election Day
- January 1, 2013: Spending sequester kicks in; Bush tax cuts expire; payroll tax cut / emergency unemployment benefits will expire again

*A fiscal contraction of at least  
3% of GDP will hit if nothing is done*

- January 2013: New Congress, Presidential inauguration
- First half 2013: Debt ceiling will need to be raised again

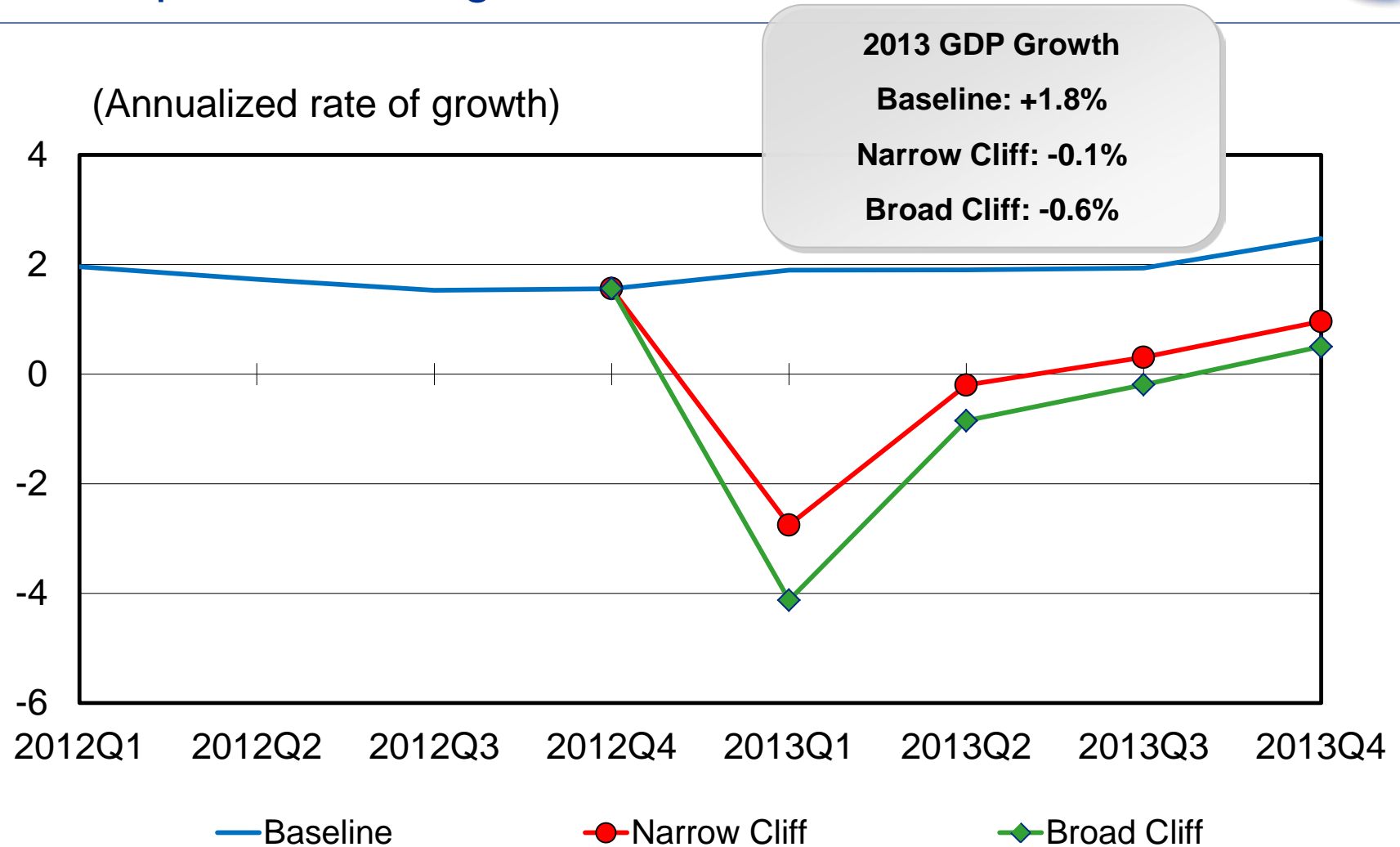


# The 2013 Fiscal Cliff

<b>All Figures Are Calendar Year Estimates</b>	<b>\$ Billions</b>	<b>Percent of GDP</b>
<i>Possible:</i>		
Bush Tax Cut Expiry	192	1.2
Payroll Tax Cuts Expiry	113	0.7
Sequester Spending Cuts	72	0.4
Emergency UI Benefits Expiry	45	0.3
Depreciation Incentives Expiry	66	0.4
<b>Total (Narrow Cliff)</b>	<b>488</b>	<b>3.0</b>
<i>Possible But Highly Unlikely:</i>		
AMT Fix Not Extended	115	0.7
Doc Fix Not Extended	13	0.1
<b>Total (Broad Cliff)</b>	<b>616</b>	<b>3.8</b>

Source: IHS calculations based on CBO data

# GDP Impacts of Going Off The Fiscal Cliff



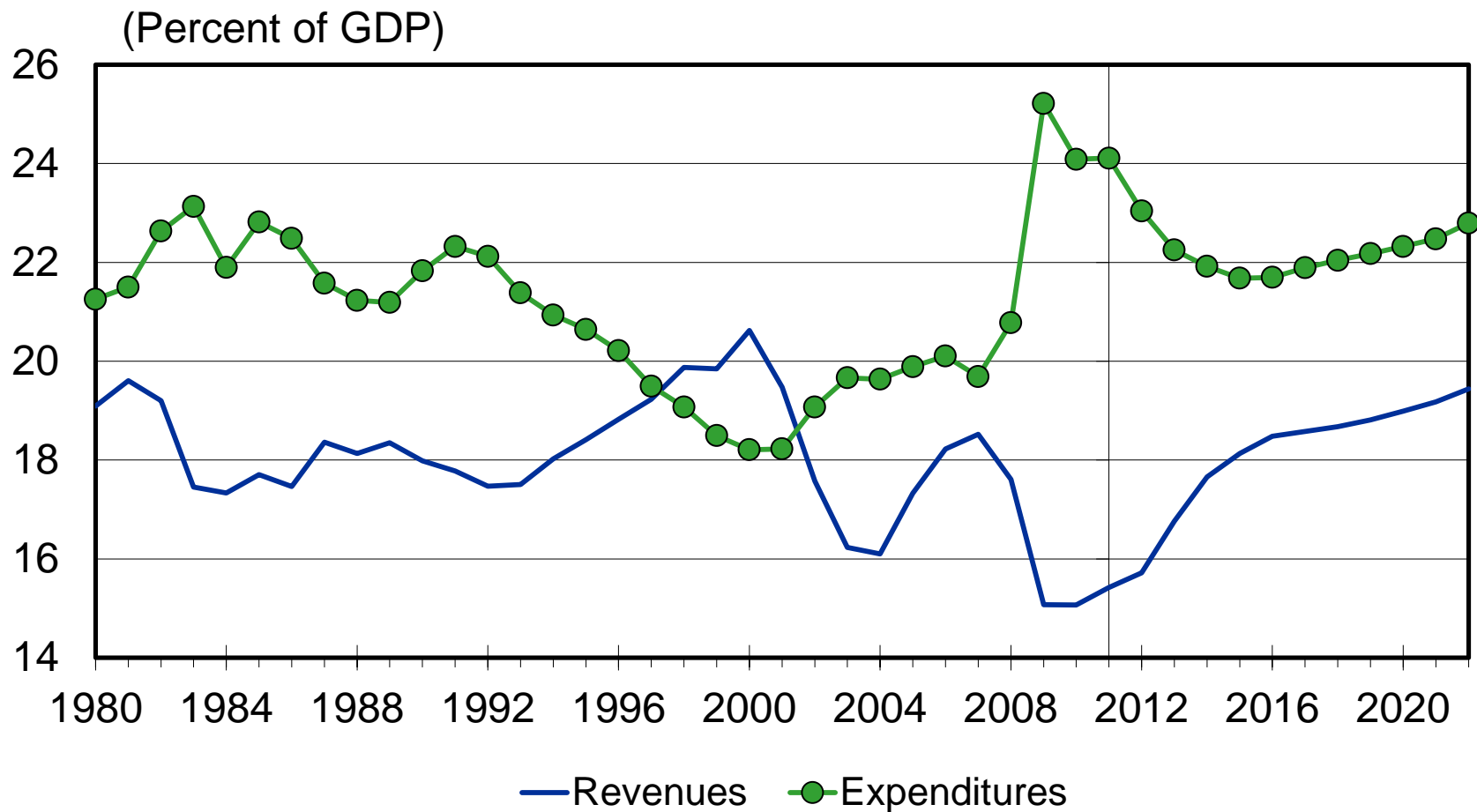


## Fiscal Policy Assumptions: We Don't Go Off The Cliff

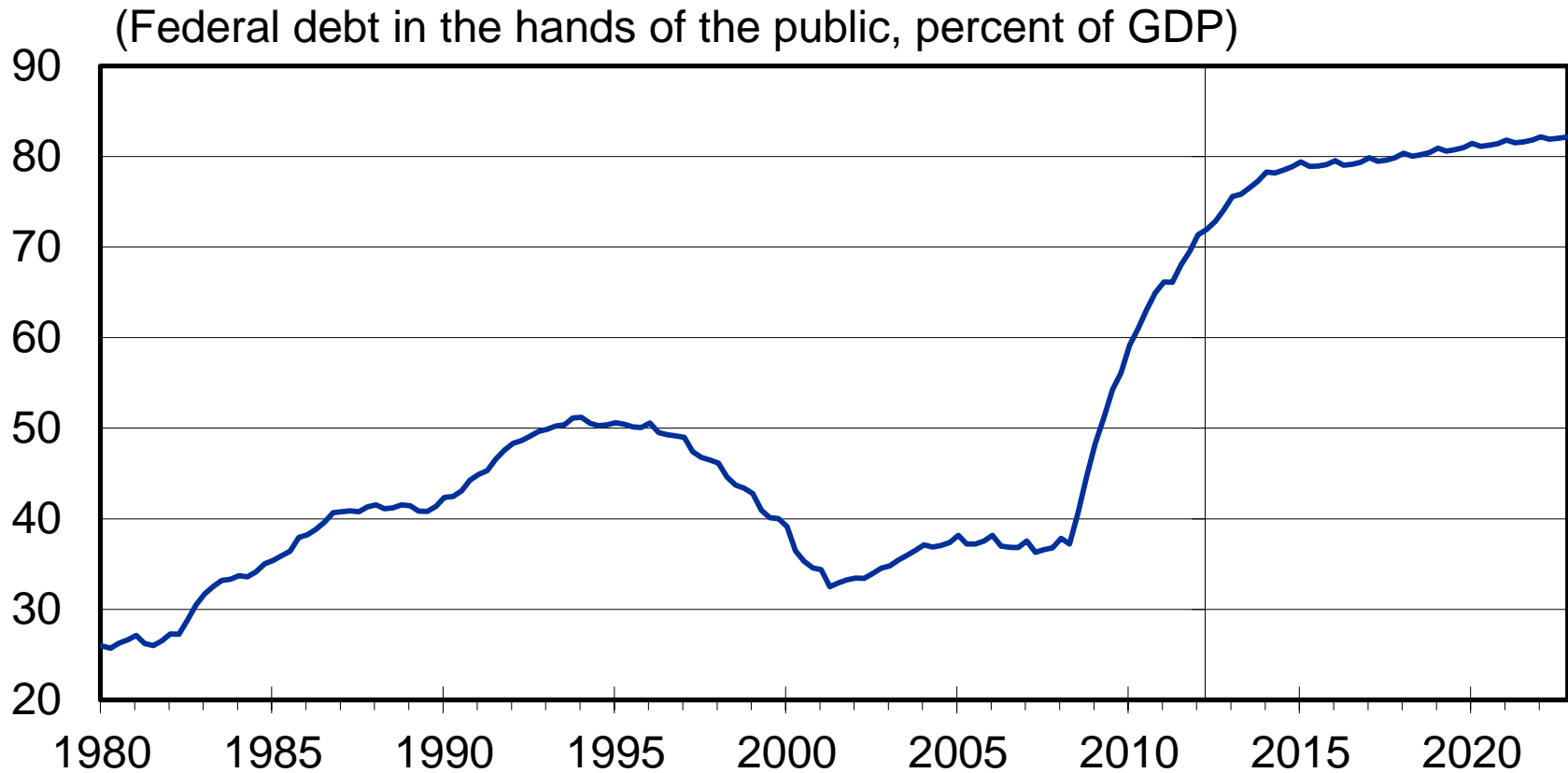
- We assume the lame-duck Congress extends the deadlines briefly to let November's winners tackle the problem
- Unless one party gains full control of the government after November there will have to be compromise
- Bush tax cuts assumed still in place in 2013
- 2% payroll tax cut and emergency UI benefits assumed extended again for 2013, and later phased out, not suddenly removed
- We assume the automatic spending cuts are replaced by entitlement savings and tax increases to be determined after the 2012 elections...and mostly beginning in 2014, not 2013
- These assumptions hold the debt-to-GDP ratio near 80% over the next ten years



# The Federal Budget Gap: We Expect Action On Both Sides of the Ledger...



# ...Sufficient to Almost Stabilize the Federal Debt Ratio (But The Biggest Problems Come Later)





## Other Major Risks

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- Eurozone debt crisis
- China hard landing
- Iran-related oil price shock



## Implications and Bottom Line

- The most likely outcome remains continued, moderate US growth
- Annual growth still doesn't beat 3% before 2015 (helped, at last, by a vigorous housing revival)
- The biggest risk remains Europe
- Still huge fiscal uncertainty – key January 1 deadlines loom
- We assume the fiscal cliff is avoided - but probably only at the last minute after another damaging episode of brinkmanship
- The election will present choices on the size and role of government – but we doubt it will deliver a clear verdict. If so, compromise will be essential.



Thank you!

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# Slow but Steady Growth in 2012-14

## The Montana Outlook

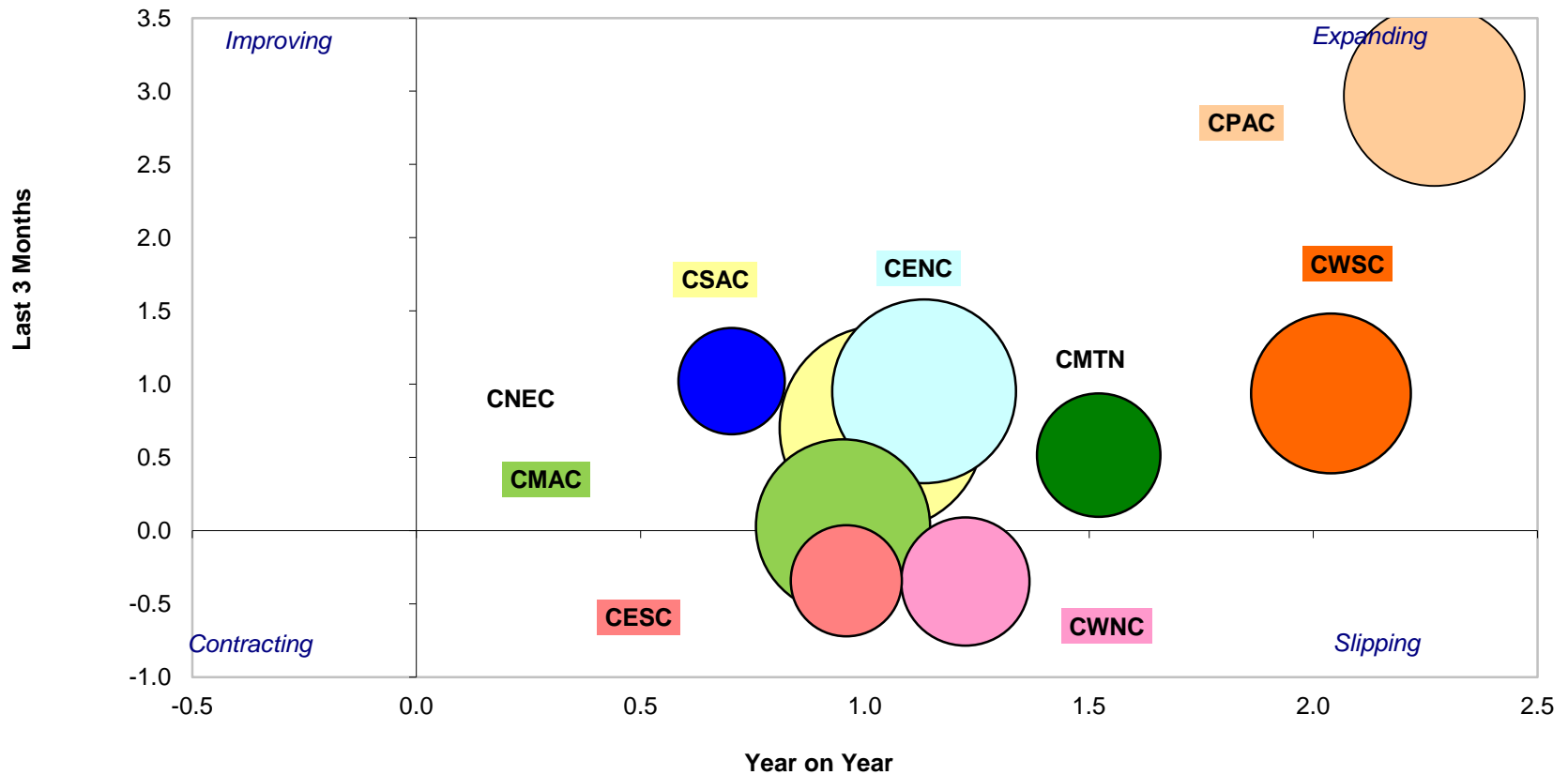
**Jim Diffley, Senior Director, Regional Economics, IHS**

September 15, 2012

# Regional Performance 2012

## Employment Momentum in July

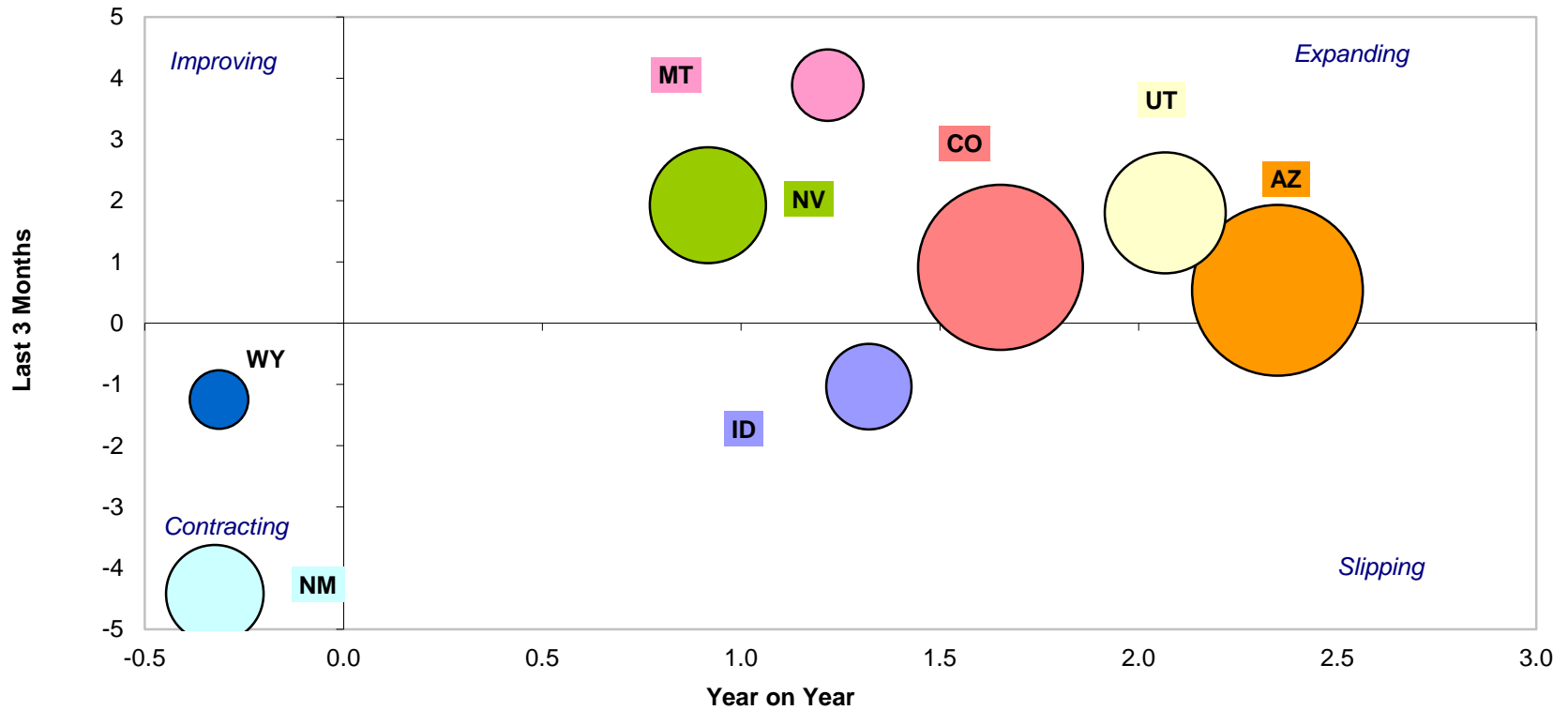
(Percent change, annual rate)



# Mountain States

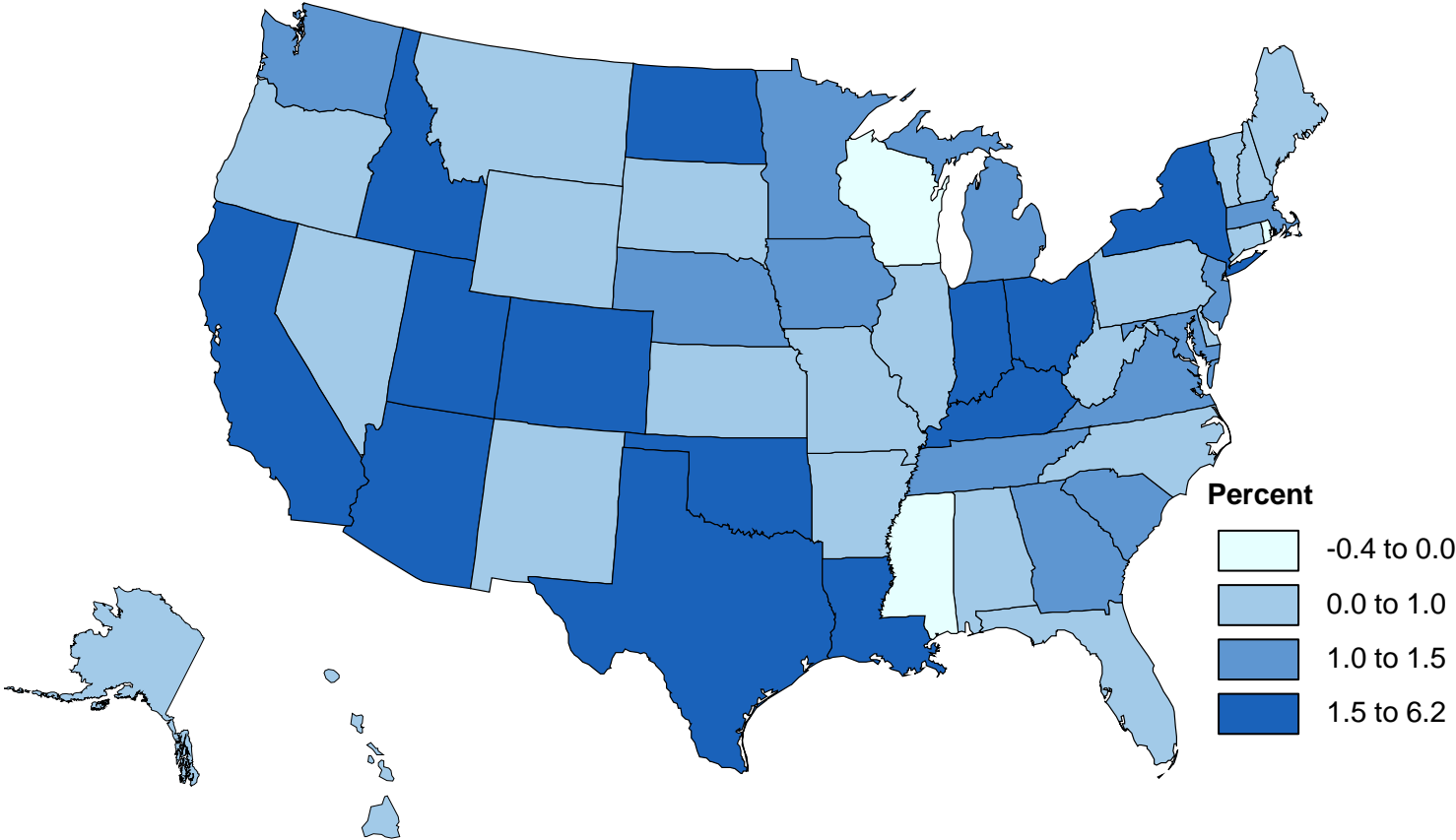
## Employment Momentum in July

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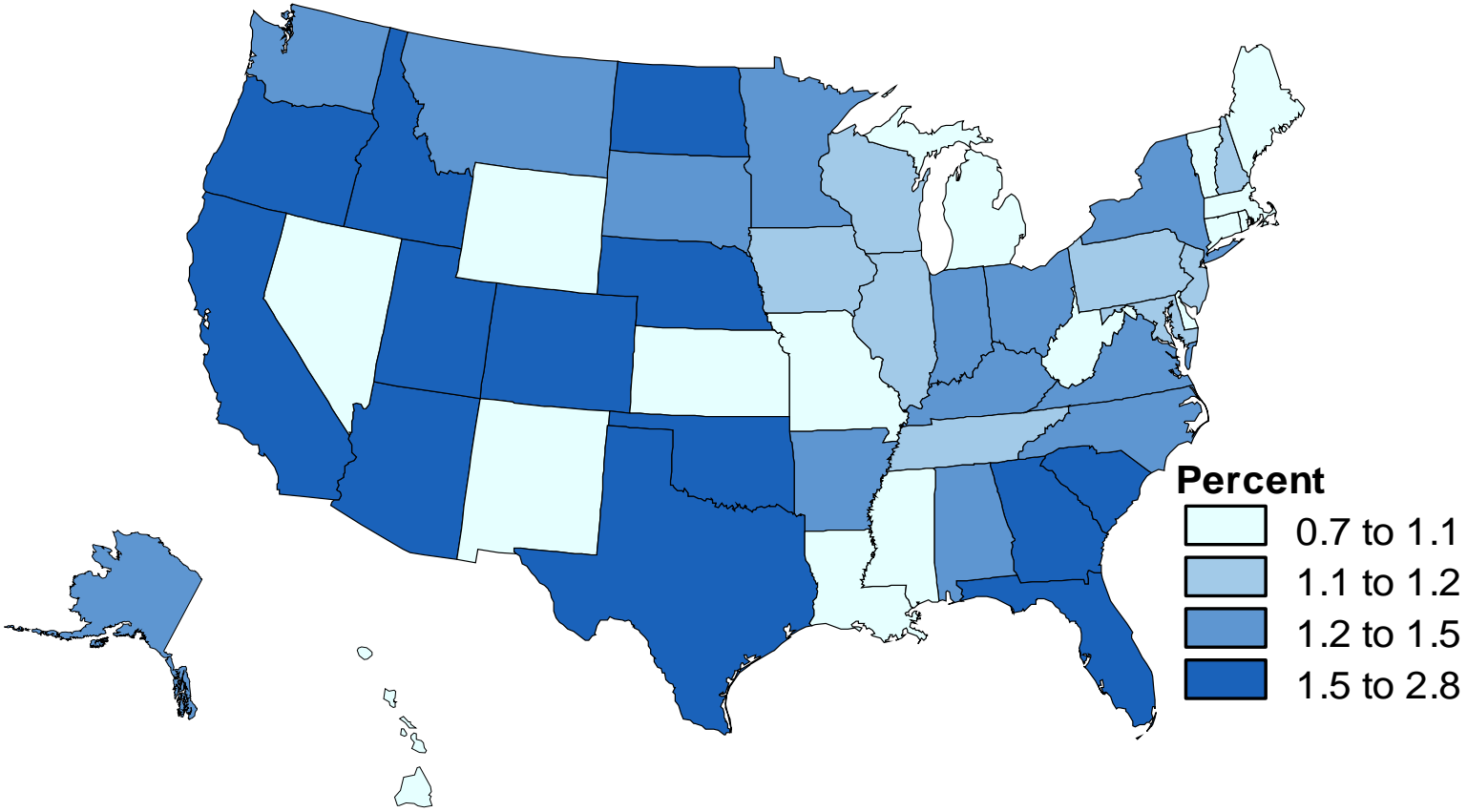




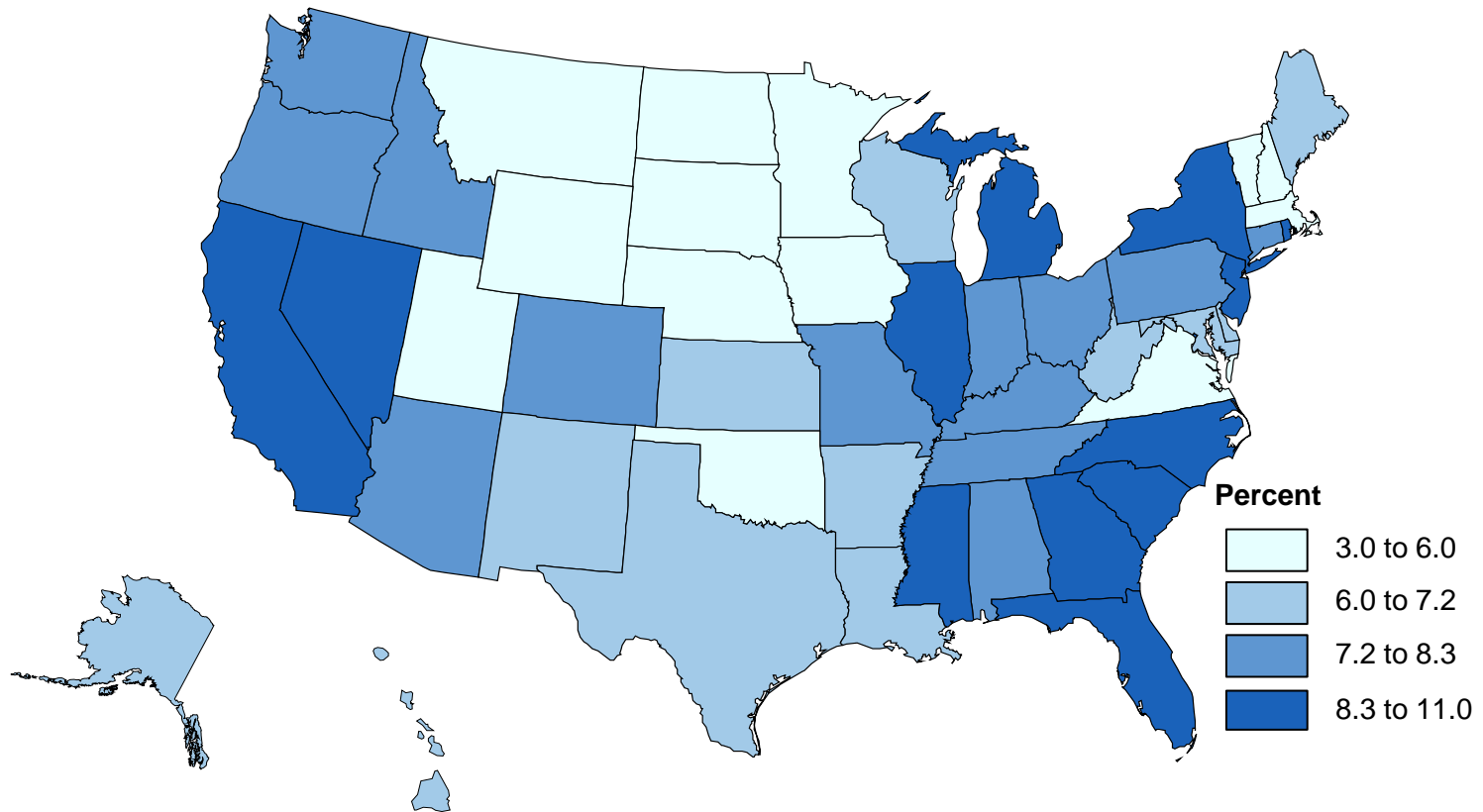
# Employment Growth 2012



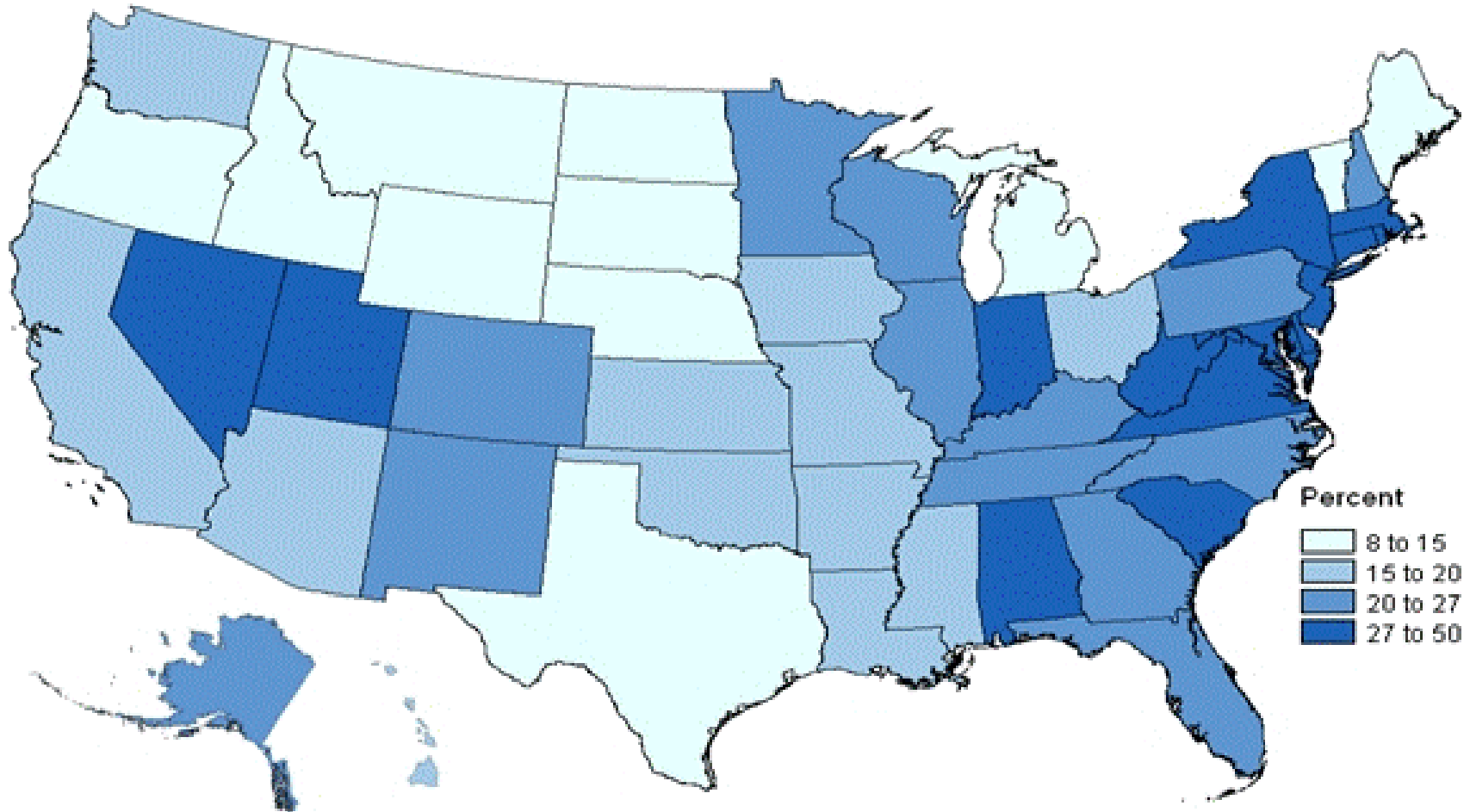
# Employment Growth 2013



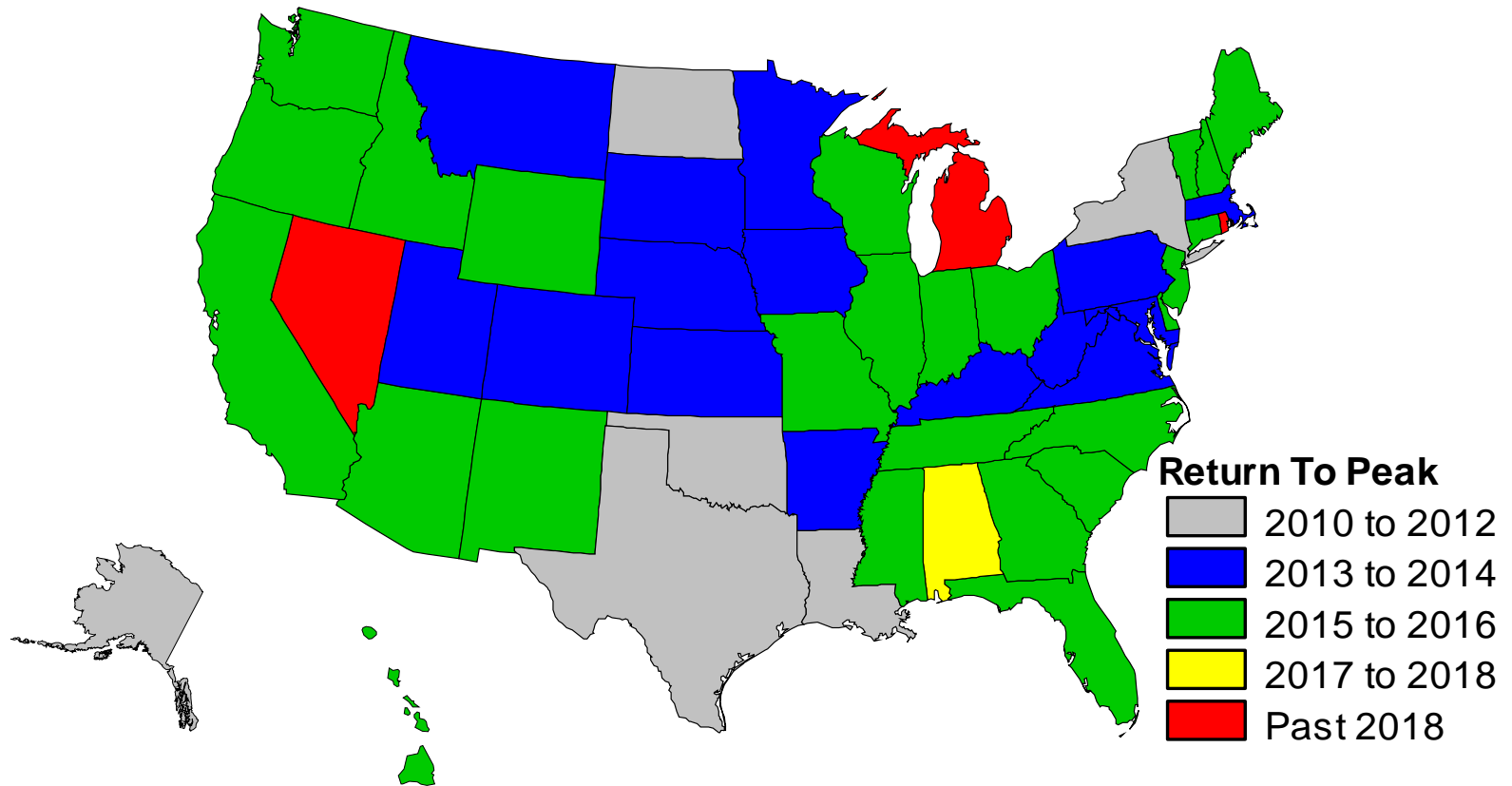
# Unemployment (2013q2)



# Exports to Europe: 2010



# Return to Peak

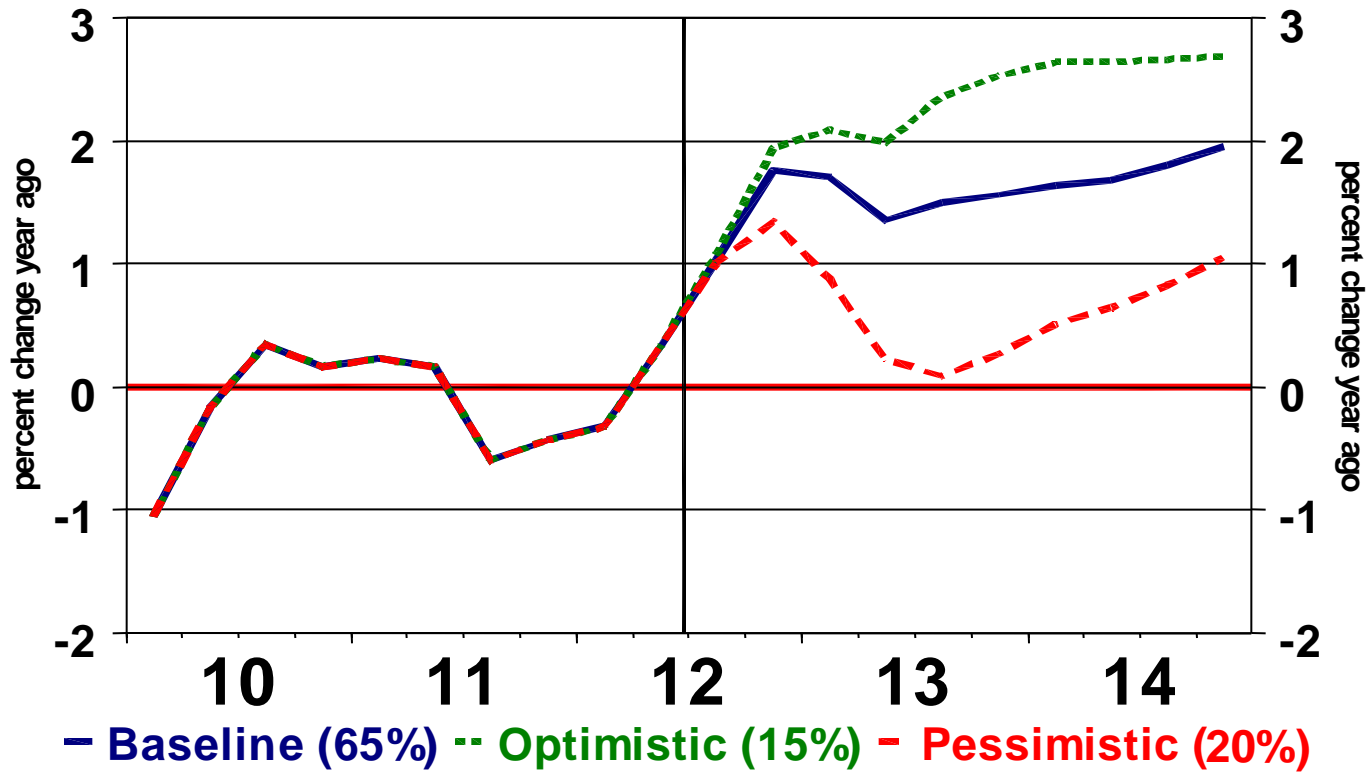




# Outlook for Key Indicators

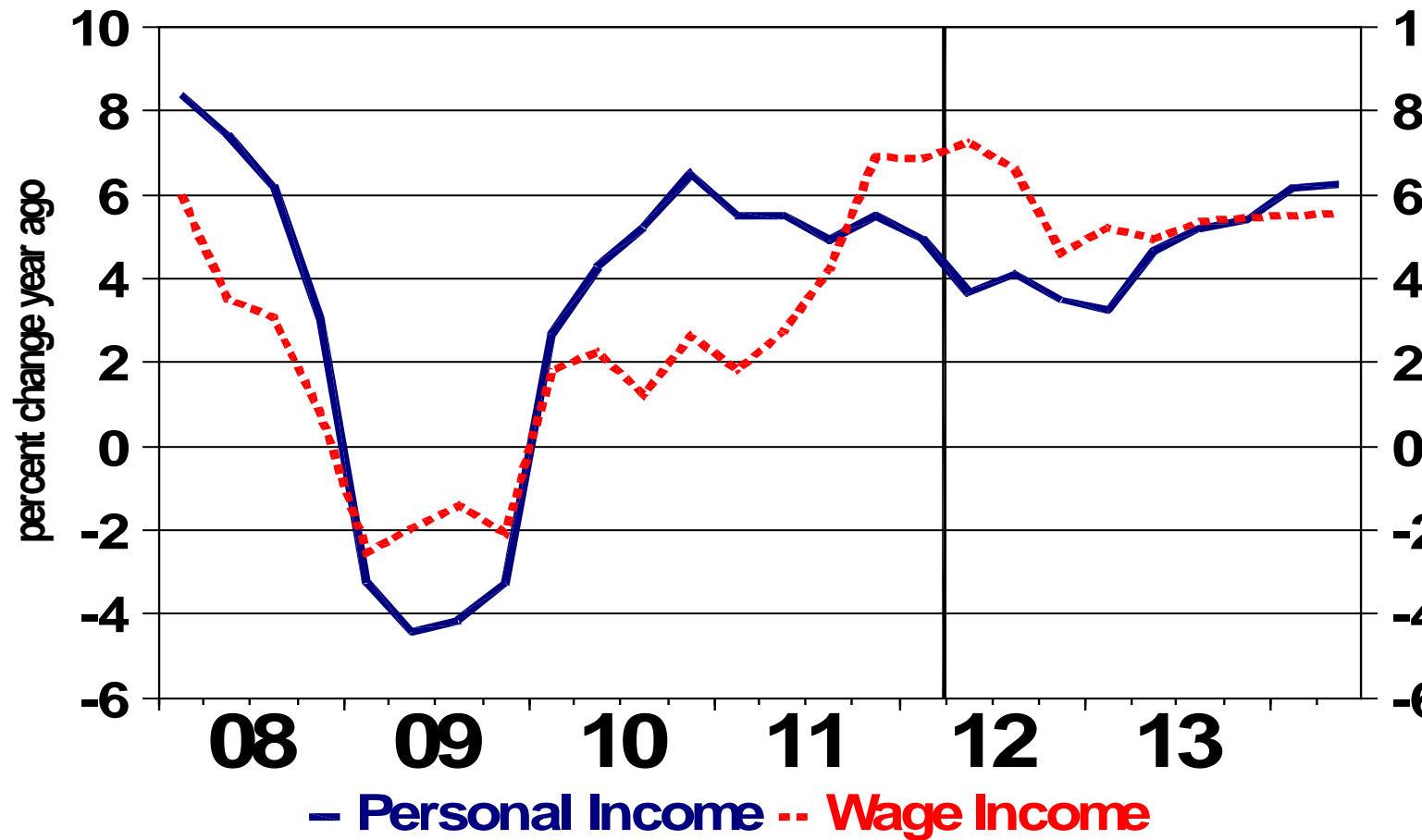
<b>Montana Outlook over the Next Four Quarters</b>										
		<b>Baseline Scenario</b>		<b>Pessimistic</b>			<b>Optimistic</b>			
		<b>Level</b>	<b>%</b>	<b>Level</b>	<b>%</b>	<b>Rank</b>	<b>Level</b>	<b>%</b>	<b>Rank</b>	
<b>Year-over-year Change (2013Q3)</b>	Employment	+6,480	+1.5	+370	+0.1	11	+10,180	+2.4	26	
	Personal Income (Mil.\$)	+1,536	+4.0	+721	+1.9	21	+1,987	+5.2	27	
	Real Gross State Product (Mil. 2005\$)	+503	+1.6	-230	-0.7	19	+1,047	+3.2	39	
<b>Level (2013Q3)</b>	Unemployment Rate (%)	5.9		6.4		41	5.6		36	
	Housing Starts	2,922		2,065		43	3,644		46	

# A Look at Forecast Risks for Montana Employment Growth



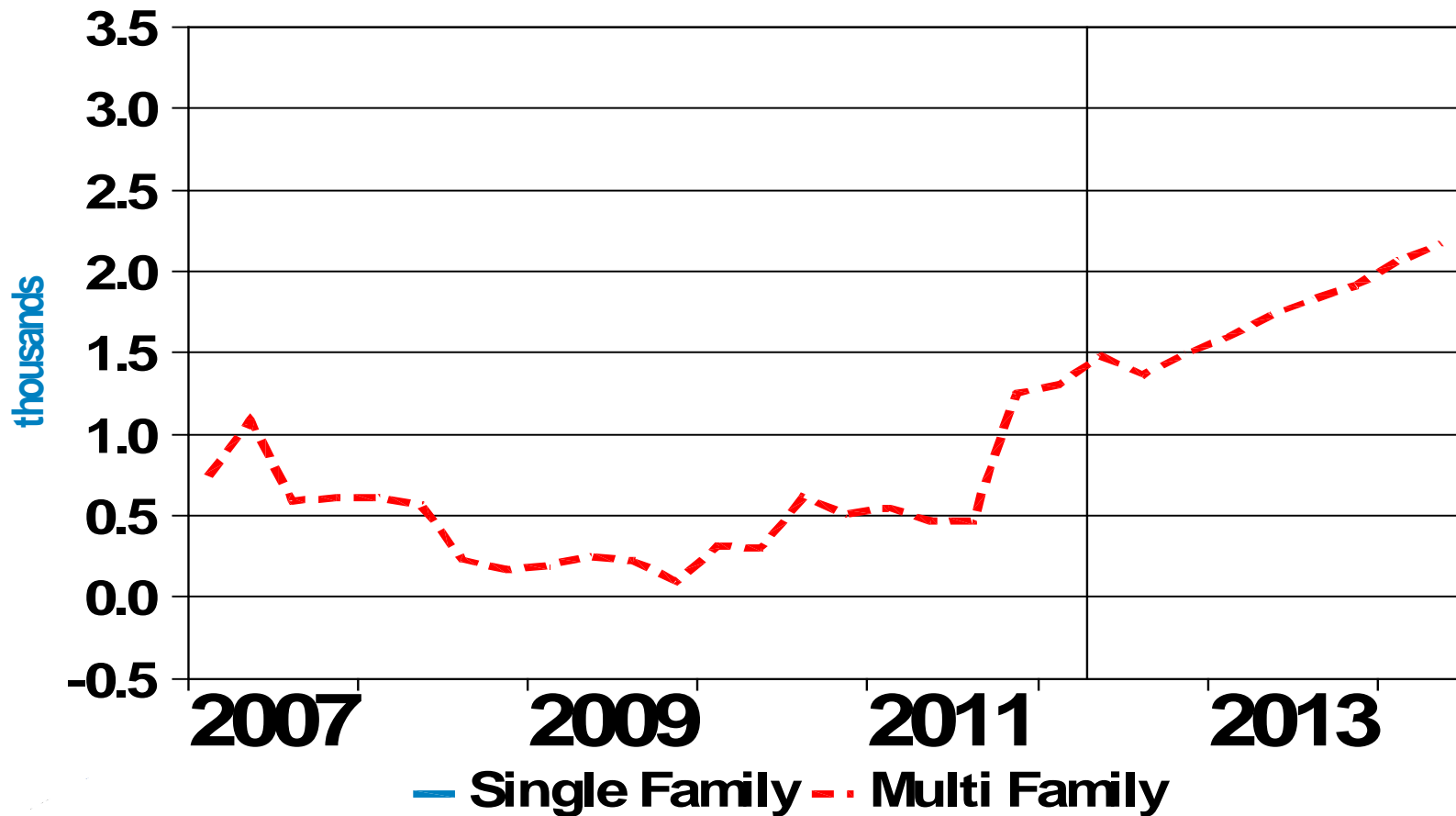
# Montana Forecast

## Income Growth





# Montana Forecast Housing Starts





Thank you!

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