

September 2011

## Croissance de demain



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- US economic policies and the crisis

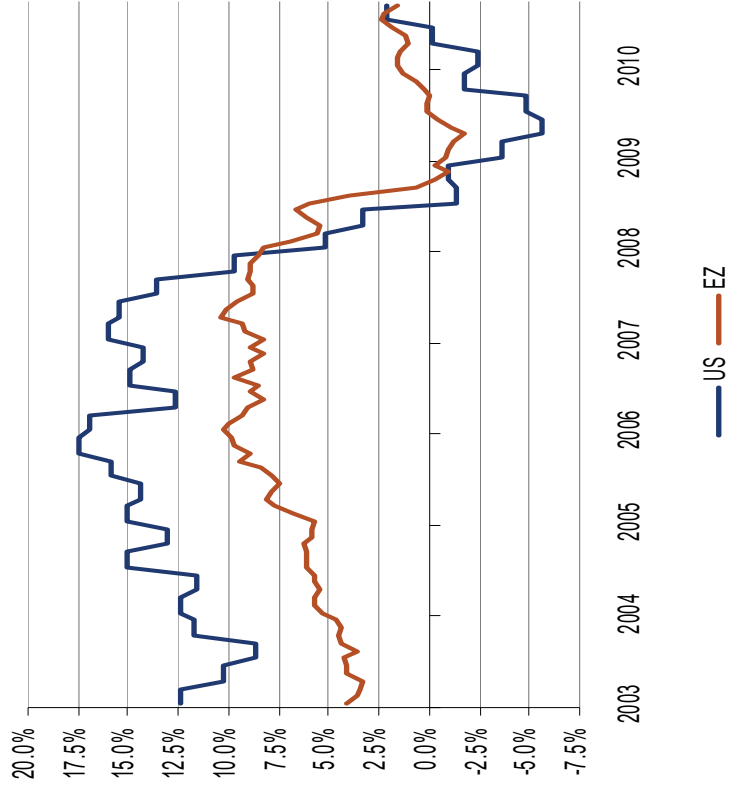
## Roadmap

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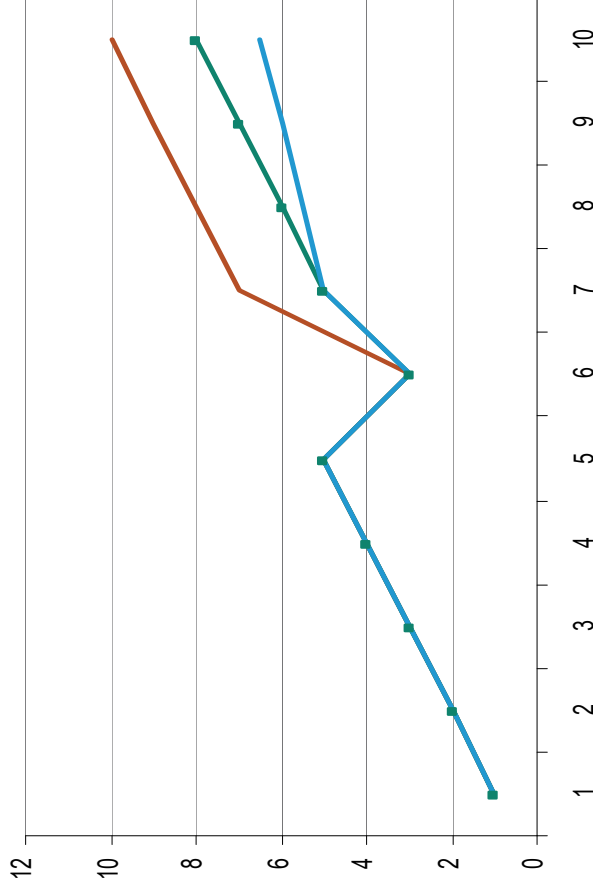
- **US**
  - Problem: deleveraging implies lower growth rate
  - For the NBER: slow growth is recession
  - Slow growth is due to a demand deficit
  - Demand deficit is dealt with monetary and fiscal policy, though doubts about the strategy rise
  - Fiscal outlook: not so bright

## Entering a low growth era

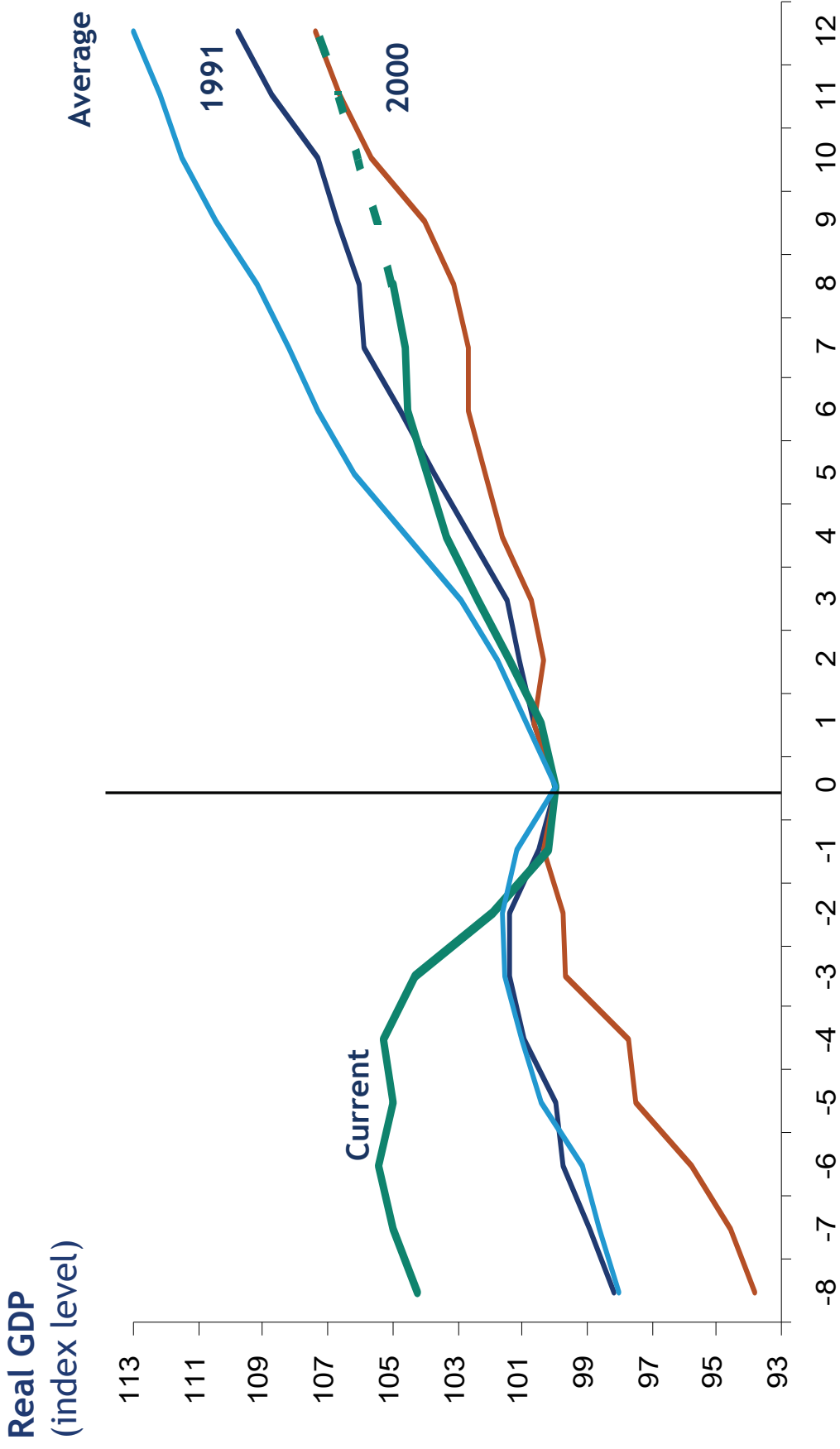
### Credit set to be slower (flows of credit, % GDP)



### Trend growth lower for a longer time



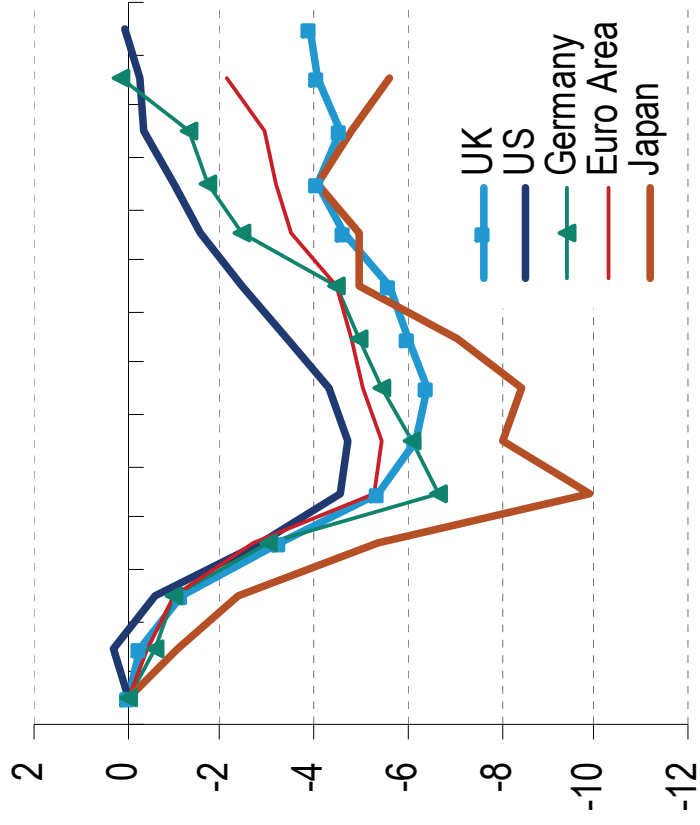
# US: Big fall; slow recovery



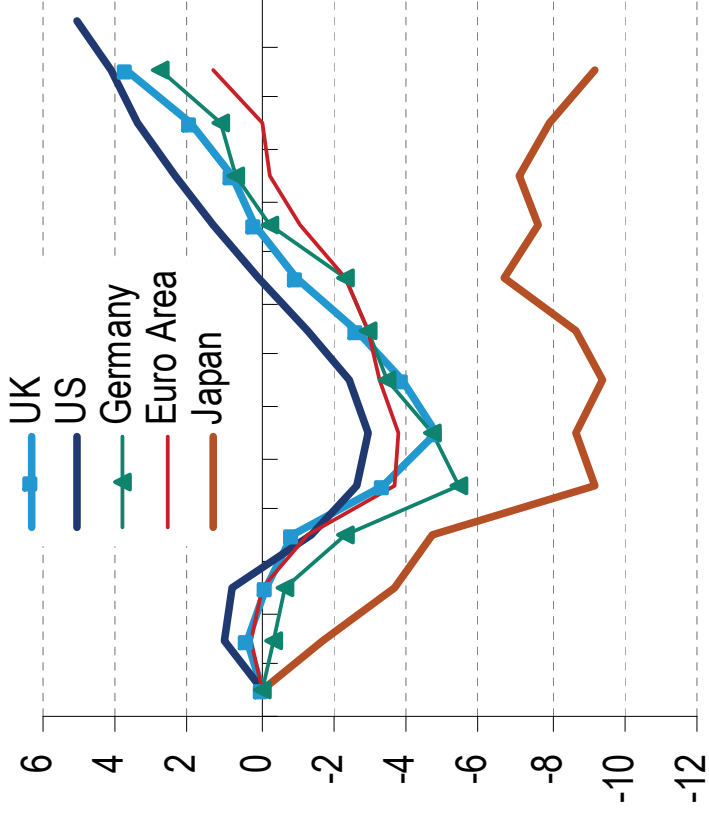
Indexed to 100 at the recession trough. Average includes all recessions after 1950 excluding the 1980 and current recessions. Dotted line represents BofA Merrill Lynch forecast. Source: Bureau of Economic Analysis, BofA Merrill Lynch Global Research

# Not so bad in comparison...

Cumulative change in real GDP since 08Q1 (%)



Cumulative change in nominal GDP since 08Q1 (%)



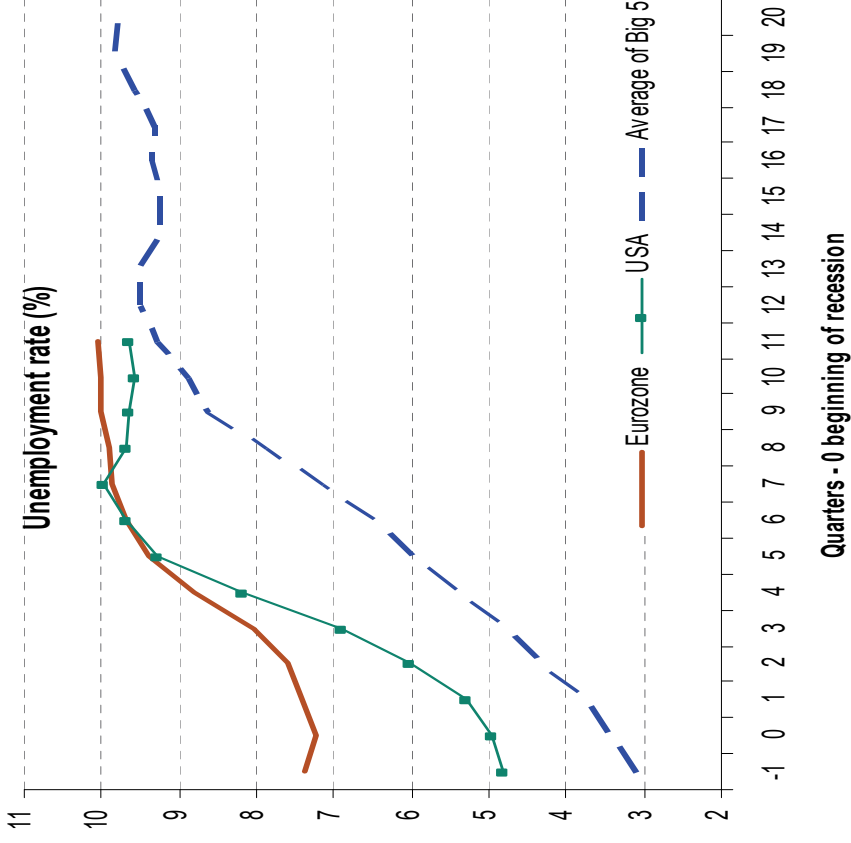
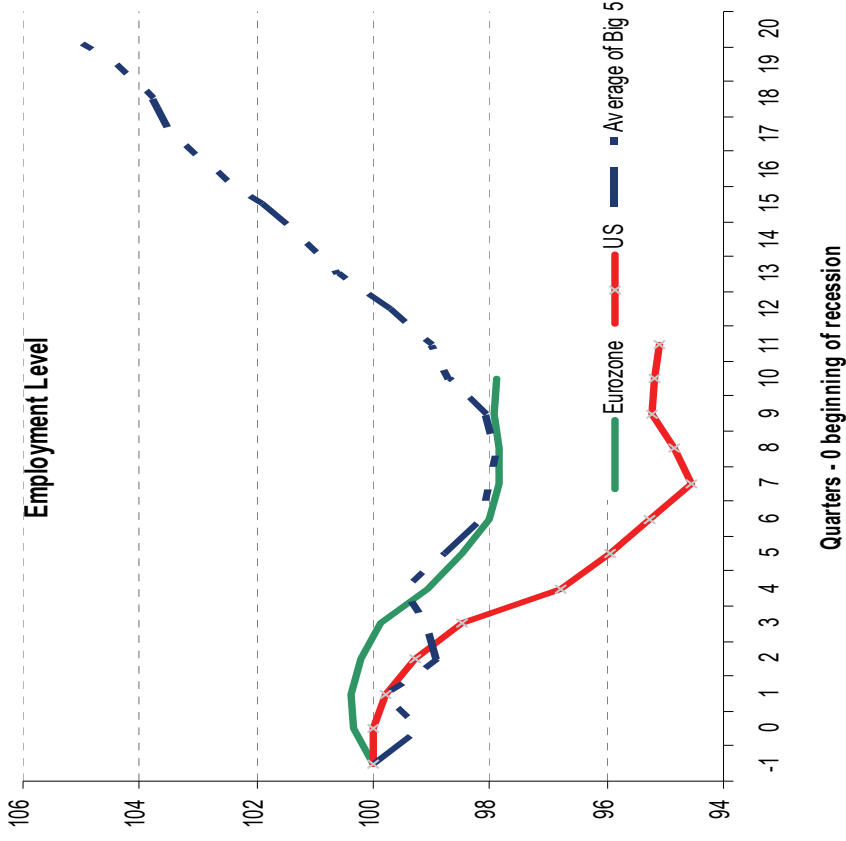
08Q1 08Q3 09Q1 09Q3 10Q1 10Q3 11Q1

08Q1 08Q3 09Q1 09Q3 10Q1 10Q3 11Q1

Source: Bloomberg, BofA Merrill Lynch Global Research. Note: this represents cumulative deviations from trend assuming zero output gap in Q108

# Except, maybe, for jobs

## ■ Labor Market



Source: BofA Merrill Lynch Global Research

•Big 5 recessions - Spain (1977), Norway (1987), Finland (1991), Sweden (1991), and Japan (1992).

## Is recession back?

### ■ Bad surprises and weak outcomes

- US revisions
- Low European Q2 GDPn growth
- Weak global consumption

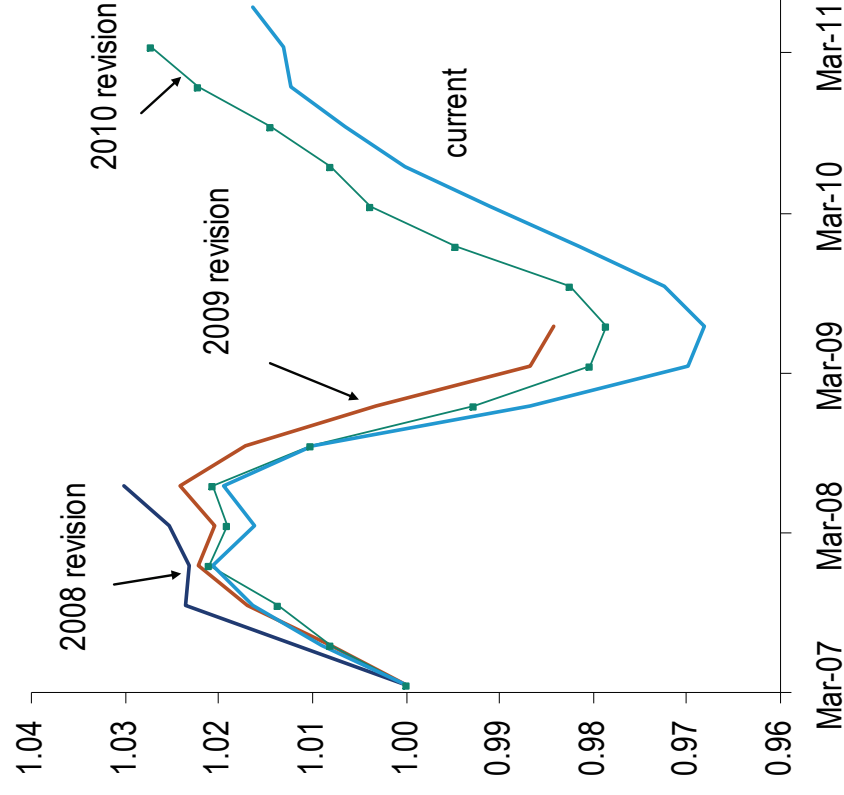
### ■ Policy « mistakes »?

- Too tight fiscal policies
- Monetary policy room for manoeuvre stertched

### ■ GEMs « soft » landing ?

- China's worries
- Other GEM: coping with developed countries fate

### GDP revisions paint a weaker picture (indexed level; 1Q07 = 1)

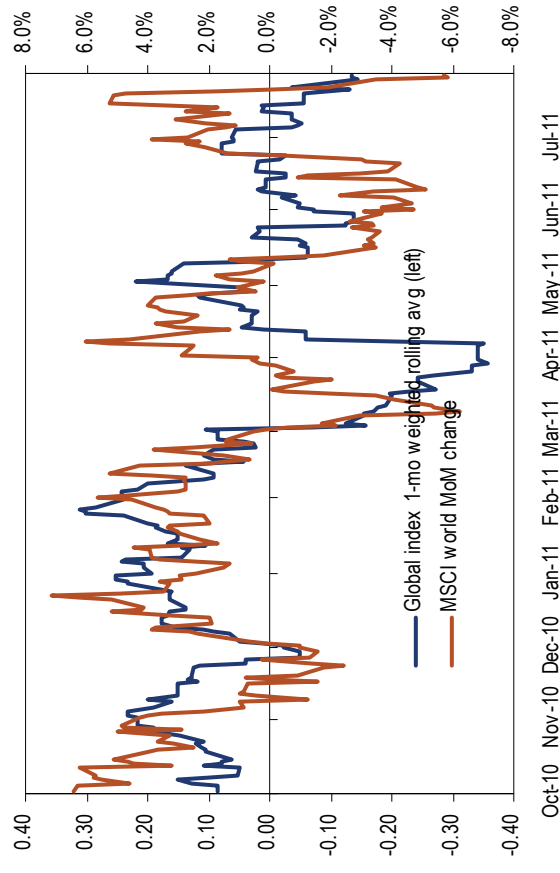


Source: BEA, ISM, Bofa Merrill Lynch Global Research

# Defining recession

- **NBER**
  - « A significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in production, employment, real income and other indicators » (NBER 2008)
  - In this definition, GDP growth as high as 2% is sometimes observed during recessions..
- **Press' rule of thumb**
  - The press often defines a recession as two consecutive quarters of negative growth
  - This rule misses the 2001 recession in the US and Europe
  - This rule also provides shorter (7m) recessions than NBER

## BofAML Activity surprises indicators

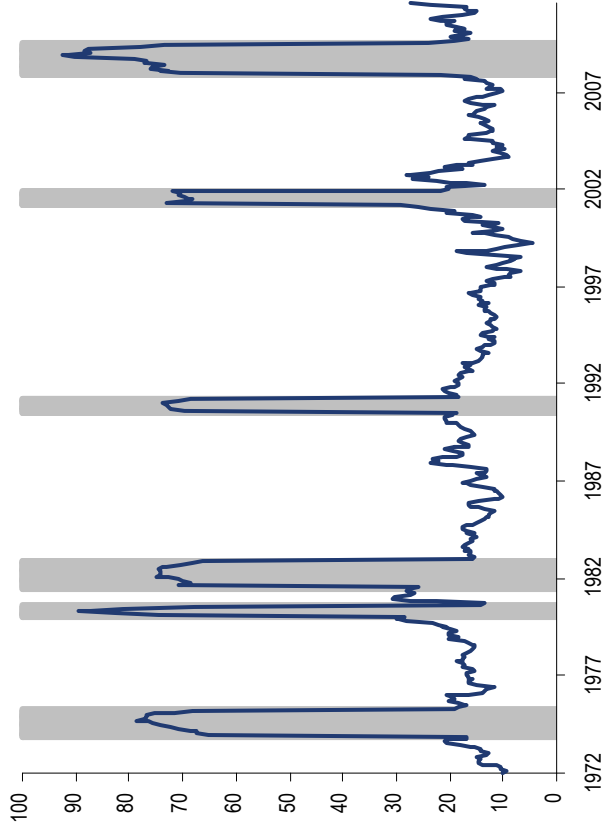


Source: Bofa Merrill Lynch Global Research. Indicators cover monthly hard and soft data for the US, the Euro zone and Germany



# US recession risks: Are we there yet?

Probably not  
(% probability)

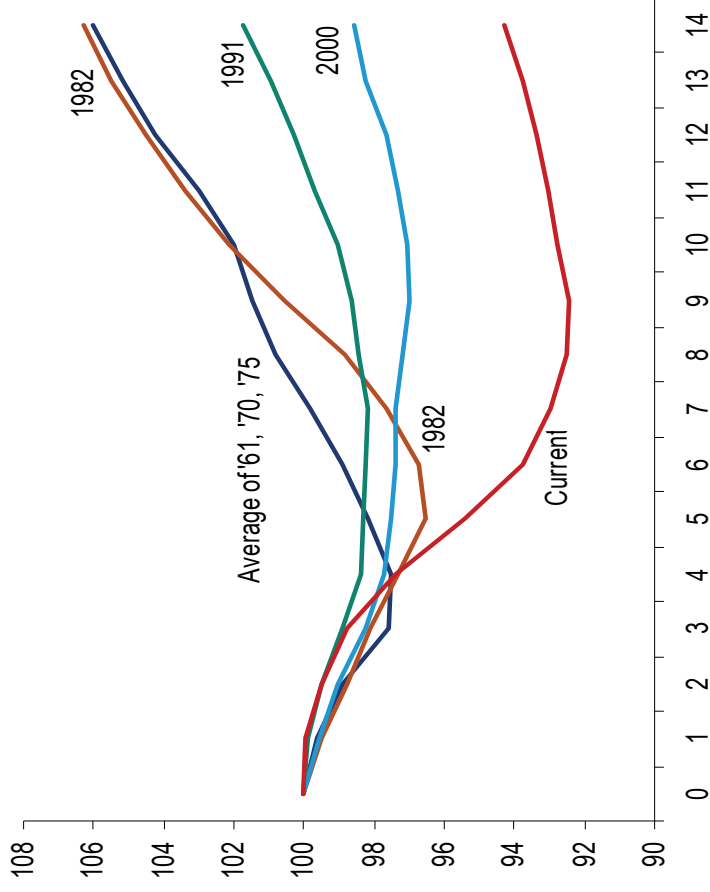


Three scenarios

	Worst	Baseline	Best
Unemployment rate (%)	10	9	8
Brent oil prices (\$/brl)	80	100	120
S&P500 (index)	1150	1300	1400
UST 10yr yields (pp)	2.20	3.00	3.60
Baa/20yr spreads (bp)	2.40	1.70	1.40
SLOS willingness-to-lend (net %)	-10	22	30
Recession probability	0.80	0.30	0.15

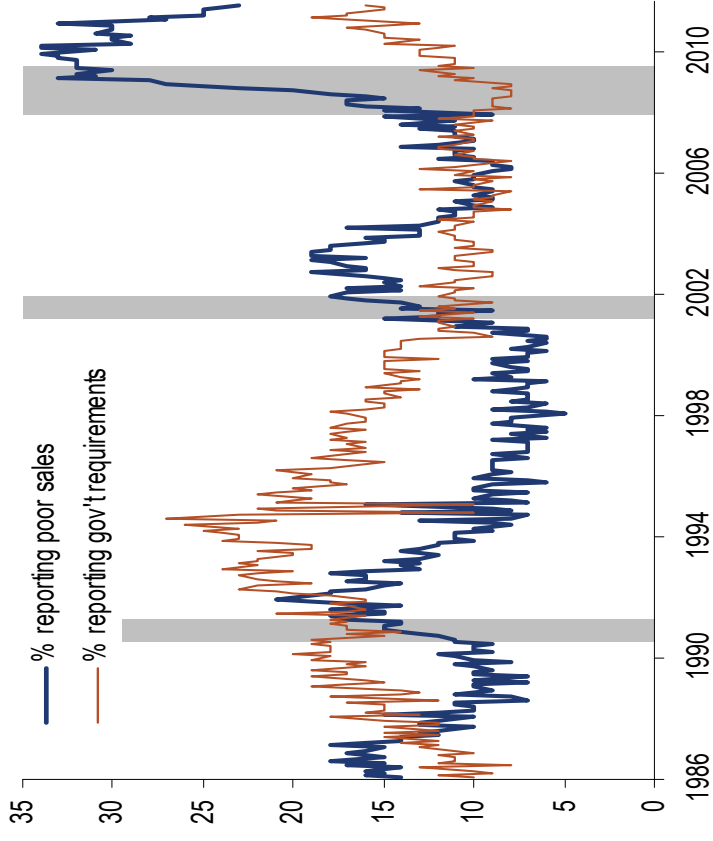
## Slow growth is due to lack of demand

- Regulation, but faster job growth in 70s/80s



Source: BLS, BofA Merrill Lynch Global Research. Note: payroll employment, 100 at business cycle peaks

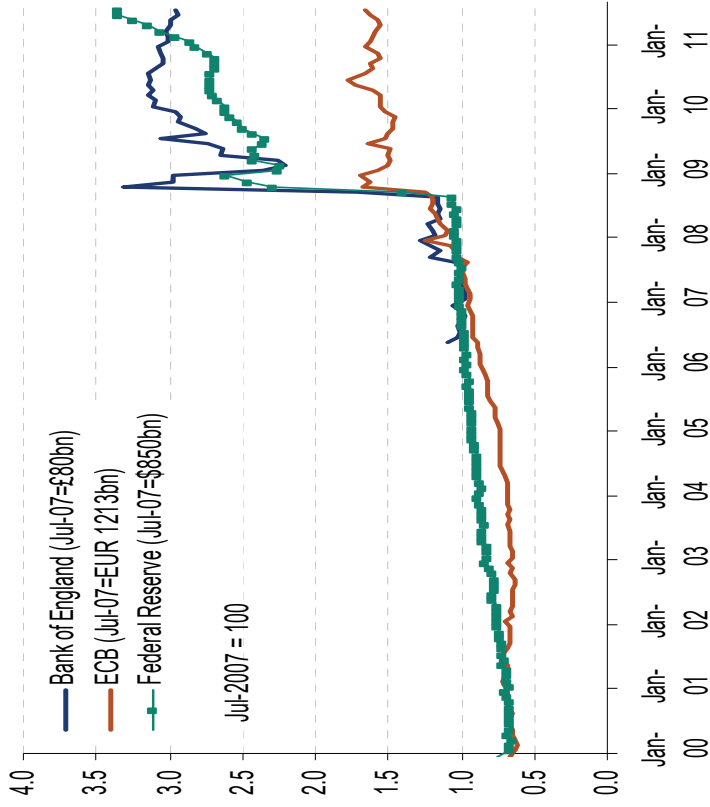
- Sales remain the biggest problem



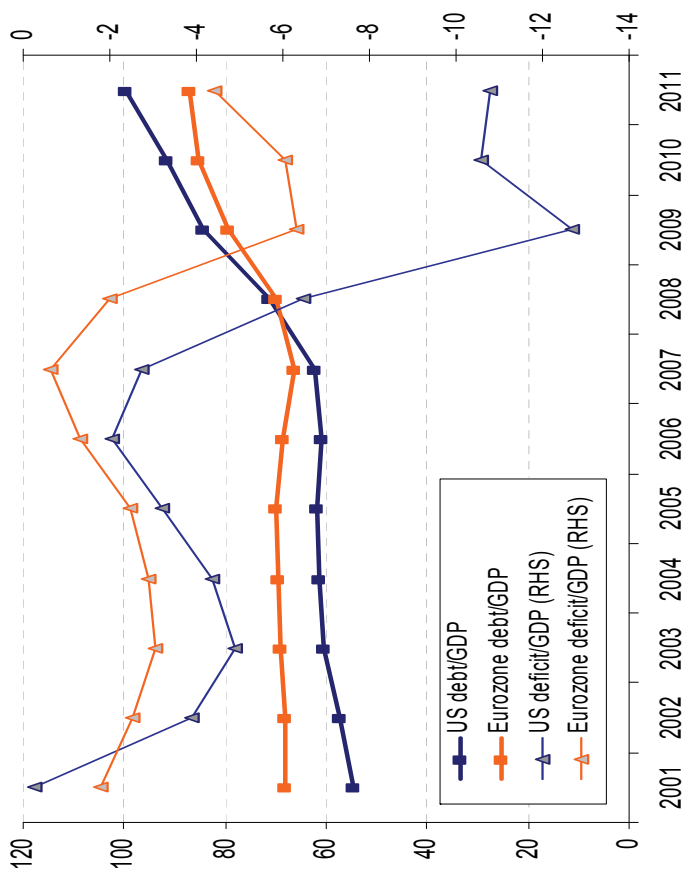
Source: National Federation of independent business  
Note: single-most important problem, % reporting

## Large policy support...

The Fed balance sheet has more than quadrupled...

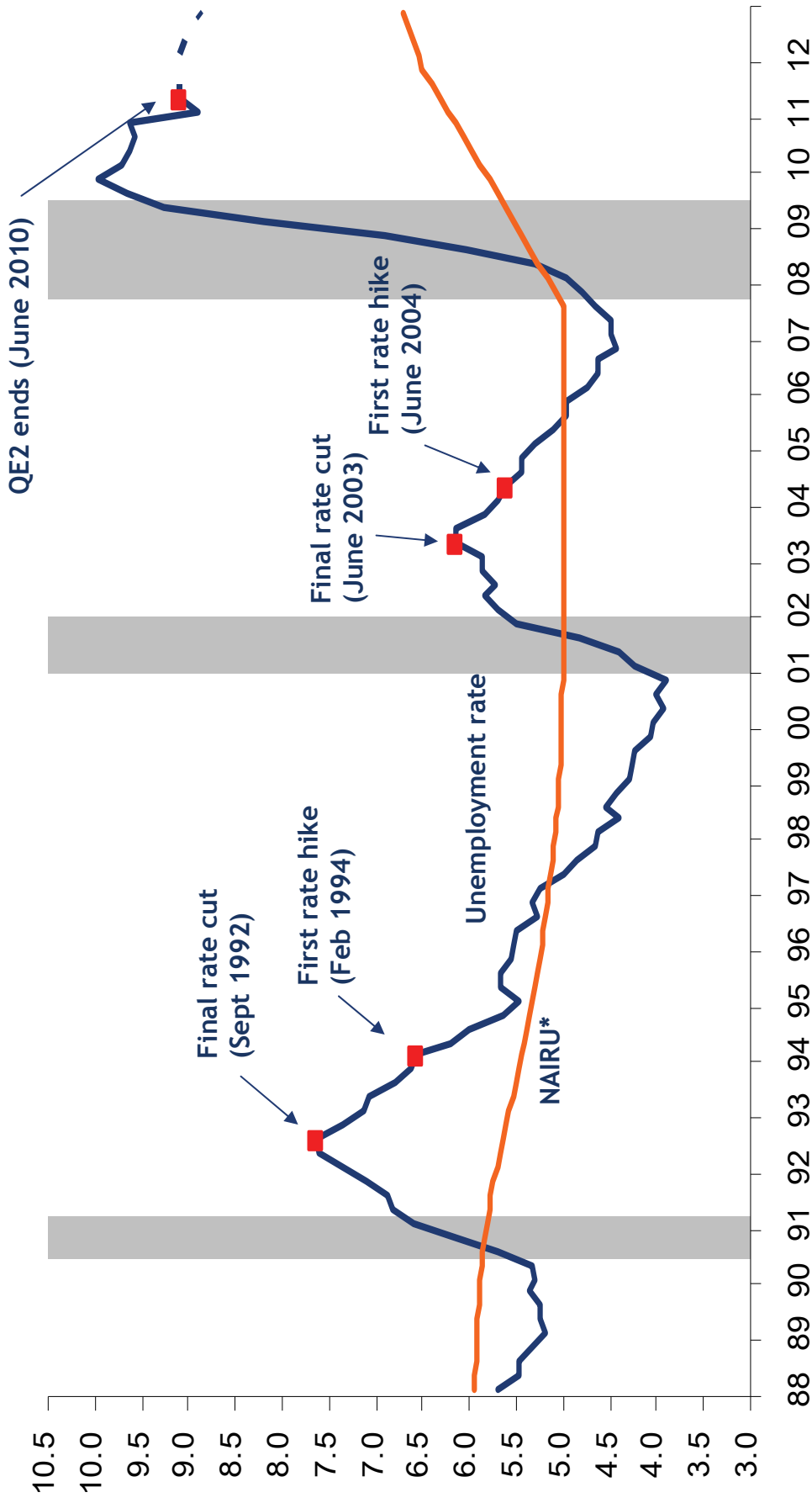


...while public finances have deteriorated



# ...not to be removed soon by the Fed

**Unemployment rate**  
(percent)



\*NAIRU is the CBO estimate of the inflation-neutral unemployment rate; Shaded regions represent periods of US recession  
Source: Bureau of Labor Statistics, Federal Reserve Board, Haver Analytics, BofA Merrill Lynch Global Research

## Fed: To QE or not to QE?

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### **QE2**

- *Only after very weak jobs...*
- *...and near zero core inflation*
- *Severely undercut by critics*

### **QE3**

- *Threshold is higher*
- *Start with language, interest rates, duration*
- *Nuclear option: “target” 10-year yields...not without danger*



## Debt deal: Automatic austerity

**2012**

Payroll tax	\$90 bn
Extended unemployment	\$40 bn
Infrastructure spending	\$40 bn
Spring cuts kick in	\$15 bn
Tranche 1	\$20 bn
<b>Total</b>	<b>\$205 bn</b>
<b>(% of GDP)</b>	<b>1.3%</b>

**2013**

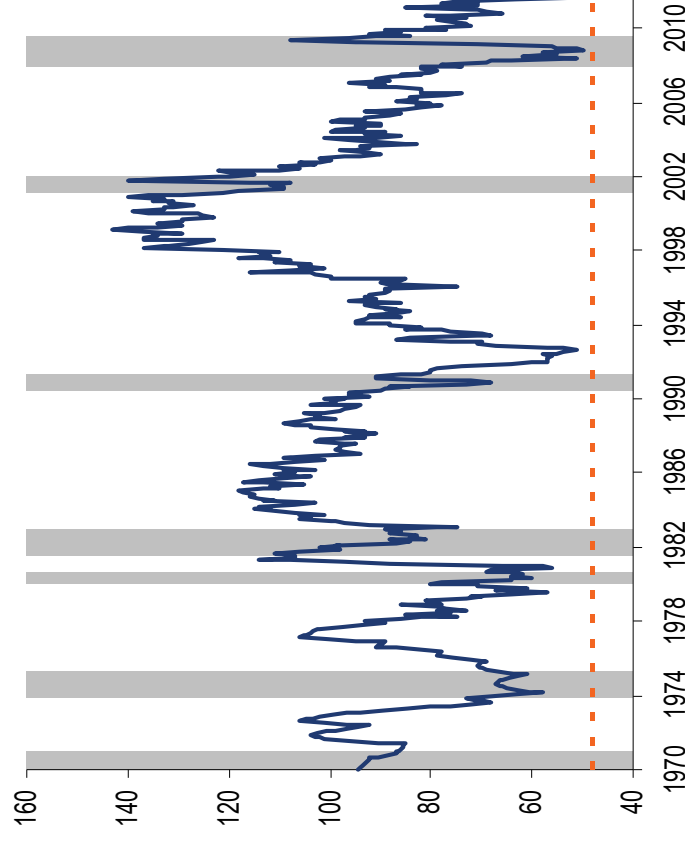
Tranche 1	\$40 bn
Tranche 2	\$110 bn
Upper income tax	\$50 bn
Other	\$40 bn
<b>Total</b>	<b>\$240 bn</b>
<b>(% of GDP)</b>	<b>1.5%</b>

## What can go wrong: Washington's message

### Four implicit messages...

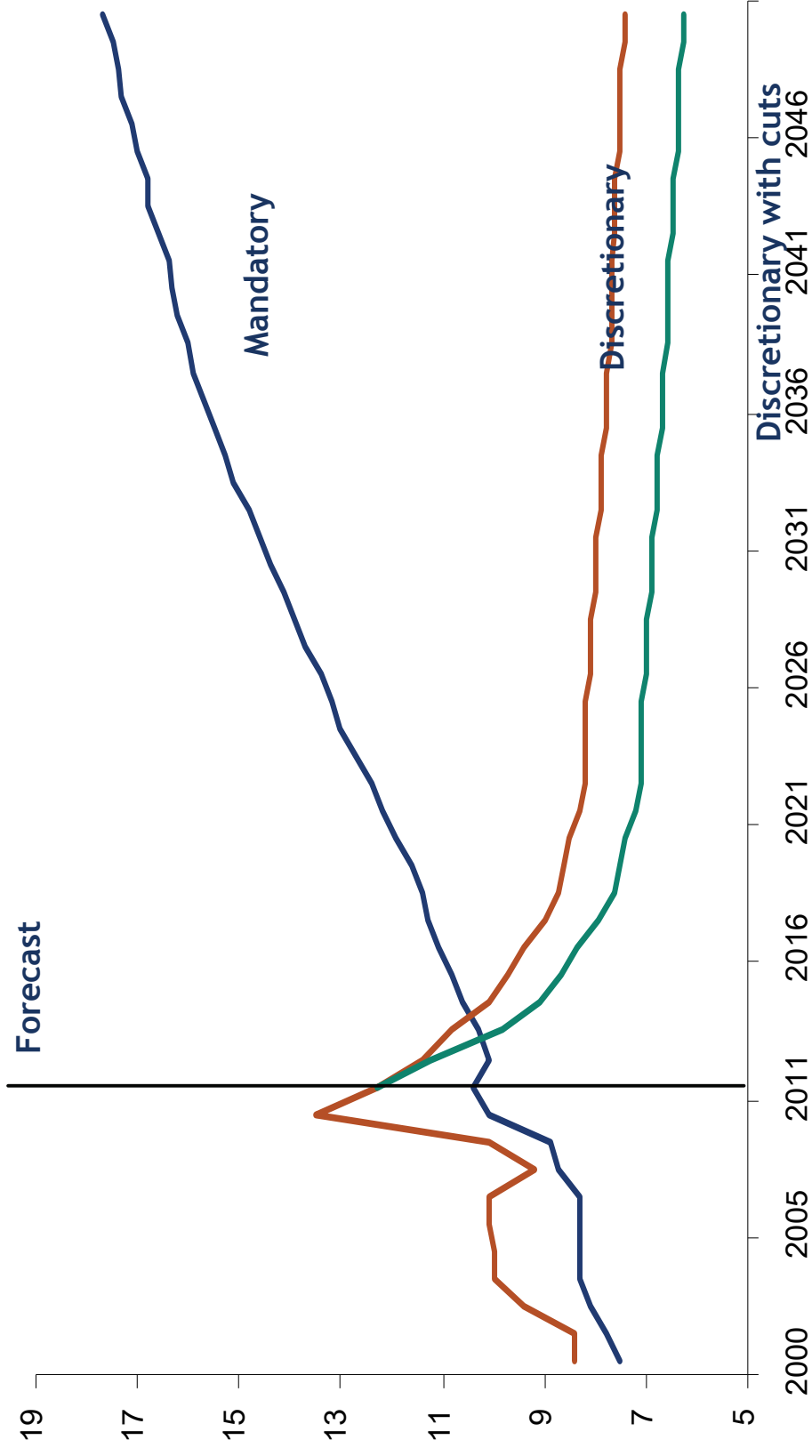
1. We have a serious debt problem
2. We are too dysfunctional to fix it
3. Threatening to default is an acceptable negotiating tactic
4. There is no fiscal-easing safety net

### US government gets a low grade



# Debt deal: Unbalanced budget cuts

**Government spending  
(% of GDP)**







**Bank of America**  
**Merrill Lynch**

September 2011

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September 2011

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