RSQE FORECASTS

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***The U.S. Economic Outlook for 2009–2010***
***Executive Summary: June 2009***

## *A Gentler Slide*

*We estimate that the decline in real GDP slowed to a 3 percent pace in the second quarter of 2009 following losses of 6.3 percent and 5.7 percent in 2008q4 and 2009q1, respectively.*

- *Business capital spending and residential construction fell less rapidly.*
- *Government purchases rebounded after sliding in the first quarter.*
- *Inventory investment was less of a drag on output growth.*
- *But consumer spending retreated again following a temporary bounce earlier this year, and*
- *Net exports provided a smaller boost to the economy.*

## *Making Progress?*

*This quarter did not bring an end to the current downturn, but it now appears that a number of the building blocks of a turnaround are falling into place.*

*Workers have started to see the Making Work Pay tax credit reflected in their paychecks, and the disbursal of federal dollars for state aid and infrastructure projects has begun. Spending should ramp up in the second half of the year to jumpstart demand and production.*

*Although it's not yet healthy, the financial system is improving. A number of the banks that were required to raise additional capital following the Treasury Department's "stress test" have already raised the necessary funds. And several firms that accepted federal help under the TARP program have repaid the funds. The key here is: are healthier banks more willing to make loans?*

*Both consumer and business confidence have improved. The Reuters/University of Michigan Index of Consumer Sentiment, which had been near all-time lows in February and March, improved in April and May. The National Federation of Independent Business's Optimism Index showed similar improvement this spring. Both measures are still signaling caution about the near term coupled with the expectation of improvement down the road.*

*Payroll employment is no longer in free fall. From October '08 to March '09 the nonfarm payroll job count fell by 3.35 million, averaging losses of 670 thousand jobs per month. This spring, the pace of job loss slowed to about 500 thousand in April and under 350 thousand in May.*

*One aspect of the housing market is showing some stability. Since the beginning of the year, monthly housing starts have ranged from about 450 thousand units to 575 thousand units and averaged just over half a million starts.*

## *A Slow Start to the Recovery*

*We expect the turnaround in the economy to begin this summer, supported by the fiscal stimulus package and improving financial markets. The recovery starts off slowly with modest increases in output. Output growth averages a mere 0.5 percent pace during the second half of the year. And job losses continue beyond the turn of the year.*

*Consumer spending turns up but remains constrained by the weak labor market and the need to improve household balance sheets. A slowing pace of inventory correction adds to growth in the second half of this year, and residential building begins to recover by the closing quarter of the year.*



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***Gaining Ground in 2010***

*The economy gains momentum during 2010 as real GDP growth improves from a 1.2 percent pace in the first quarter to 3.6 percent by year's end. Business fixed investment turns positive in the spring and consumer spending strengthens over the course of the year.*

*The turnaround in housing begins to solidify. Housing starts increase from 534 thousand units in 2009 to 728 thousand units in 2010. However, this is only about half the level of 1342 thousand housing starts in 2007.*

*Sales of light vehicles fall to 9.7 million units in 2009, the first time they have been below 10 million units since 1970. Sales rebound to 11.1 million units in 2010, remaining below the level of 13.1 million units sold in 2008.*

*By 2010, economic growth begins to accelerate both in the United States and abroad. As a result, both imports and exports grow during the year. But the pace of this growth is much faster for imports, which means the foreign sector exerts a drag on the U.S. economy as recovery proceeds.*

***Unemployment and Inflation***

*The U.S. economy began to shed jobs in the first quarter of 2008, and this continues through the spring of 2010. Over this period, nearly 8 million jobs are lost. Employment begins to increase, albeit slowly, in the second half of 2010. The net result is that the unemployment rate peaks at 10.4 percent in the second quarter of 2010, but remains at 10.2 percent at the end of the year. The yearly average of 10.3 percent is more than double the rate of 4.6 percent recorded in 2007.*

*After averaging $100 per barrel in 2008, the price of west Texas intermediate crude oil fell by 40 percent in 2009. This drop, combined with the severity of the economic downturn, causes the all-items CPI to fall by 0.2 percent in 2009. Core inflation rises at 1.8 percent in 2009. As the economy strengthens and oil prices rebound, all-items inflation rises to 2.8 percent and core inflation reaches 2.2 percent in 2010.*

| | Actual | | RSQE Forecast | |
|---|---|---|---|---|
| | 2007 | 2008 | 2009 | 2010 |
| GDP (Billions of Current $s) | 13807.5 | 14264.6 | 14068.0 | 14488.1 |
| Real GDP (Billions of Chained 2000 $s) | 11523.9 | 11652.0 | 11296.6 | 11454.4 |
| % Change: Year-Over-Year | 2.0 | 1.1 | -3.1 | 1.4 |
| % Change: 4th-Qtr-to-4th-Qtr | 2.3 | -0.8 | -1.9 | 2.6 |
| Nonfarm Payroll Employment (Millions) | 137.6 | 137.0 | 131.9 | 130.3 |
| Civilian Unemployment Rate (%) | 4.6 | 5.8 | 9.4 | 10.3 |
| Capacity Utilization, Total Industry (%) | 80.6 | 77.6 | 69.3 | 72.4 |
| Inflation (Private Nonfarm GDP Deflator, % Change) | 2.1 | 1.9 | 2.3 | 1.6 |
| Inflation (CPI-U, % change) | 2.9 | 3.8 | -0.2 | 2.8 |
| Inflation (Core CPI, % change) | 2.3 | 2.3 | 1.8 | 2.2 |
| Light Vehicle Sales (Millions) | 16.1 | 13.1 | 9.7 | 11.1 |
| Private Housing Starts (Thousands) | 1342 | 901 | 534 | 728 |
| 3-Month Treasury Bill Rate (%) | 4.4 | 1.4 | 0.2 | 0.4 |
| 10-Year Treasury Note Rate (%) | 4.6 | 3.7 | 3.3 | 3.5 |
| Conventional Mortgage Rate (%) | 6.3 | 6.0 | 5.2 | 5.4 |
| Real Disposable Income (Billions of Chained 2000 $s) | 8644.1 | 8753.6 | 8928.3 | 9023.3 |
| % Change | 2.8 | 1.3 | 2.0 | 1.1 |
| Corporate Profits After Tax (Billions of Current $s) | 1435.9 | 1230.6 | 1101.2 | 1396.4 |
| Value of U.S. $ (FRB Broad Index), % Appreciation | -4.7 | -3.5 | 5.2 | -8.6 |
| Current Account Balance (NIPA Basis, Billions of Current $s) | -718.6 | -653.6 | -350.5 | -487.5 |
| Federal Surplus (FY, NIPA Basis, Billions of Current $s) | -208.5 | -440.2 | -905.2 | -1274.2 |