

# The General Economic Outlook

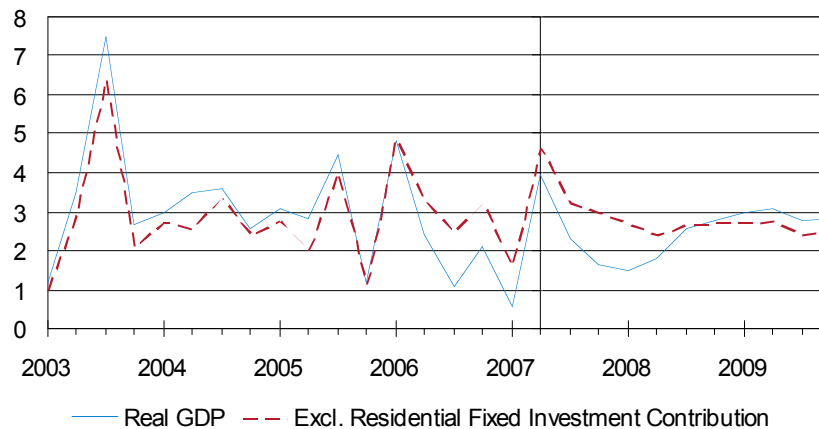
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*FTA Revenue Estimating Conference*  
*Raleigh, North Carolina*  
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## Growth Resilient So Far Despite Housing Bust – But Can It Remain So?

(Real GDP, annualized rate of growth)



## U.S. Economic Growth by Sector

(Percent change)

	2006	2007	2008	2009
<b>Real GDP</b>	2.9	2.0	2.0	2.8
<b>Consumption</b>	3.1	2.9	2.3	2.6
<b>Residential Investment</b>	-4.6	-16.4	-16.6	3.4
<b>Bus. Fixed Investment</b>	6.6	3.7	2.9	3.7
<b>Federal Government</b>	2.2	1.3	3.1	0.4
<b>State &amp; Local Govt.</b>	1.6	2.2	1.5	1.0
<b>Exports</b>	8.4	7.0	8.8	8.4
<b>Imports</b>	5.9	2.0	3.7	5.0

## Other Key Indicators

(Percent change unless noted)

	2006	2007	2008	2009
<b>Industrial Production</b>	4.0	1.9	1.5	2.5
<b>Payroll Employment</b>	1.9	1.3	0.8	1.1
<b>Light Vehicle Sales (Millions)</b>	16.5	16.1	16.1	16.3
<b>Housing Starts (Millions)</b>	1.81	1.36	1.16	1.39
<b>Consumer Price Index</b>	3.2	2.6	1.9	1.8
<b>Core Consumption Deflator</b>	2.2	2.0	1.8	1.9
<b>Federal Funds Rate (%)</b>	4.96	5.10	4.50	4.63
<b>10-Year Treasury Yield (%)</b>	4.79	4.70	4.65	5.00



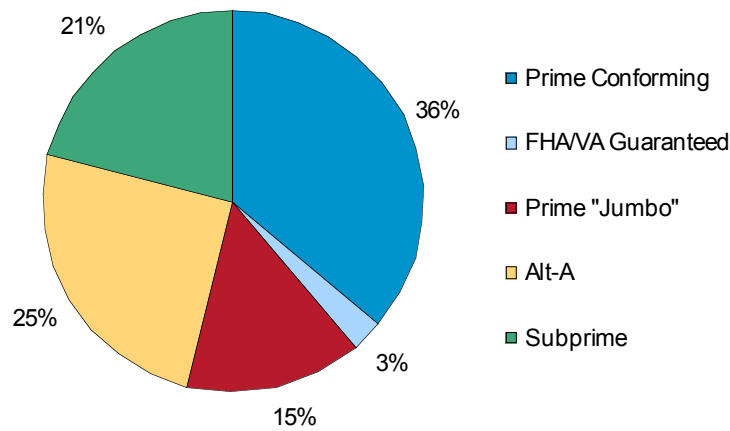
## Credit Contagion

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## Financial Fall-Out From the Subprime Debacle

- **Huge mortgage-related losses (\$100-\$200 billion?)...**
- **...Dispersed around the world, but nobody knows where for sure...**
- **...Have led investors to flee from mortgage-backed assets (if they can)**
- **Contagion has tainted investor appetite for all forms of risk**
- **Corporate debt and inter-bank funding markets have tightened—forcing central banks to intervene**

## U.S. Mortgage Originations in 2006 by Loan Type



## Credit Impacts on the Economy

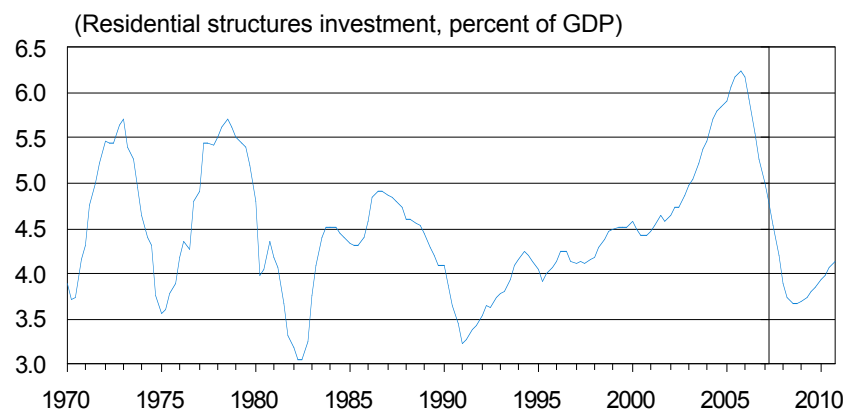
- **Home Mortgages**
  - More foreclosures, fewer qualified buyers
  - "Conforming" prime sector still intact
  - Adjustable rate resets have not yet peaked
- **Consumer**
  - Consumer credit standards likely to tighten
  - Home equity pump drying up
- **Business**
  - Leveraged buy-out market stalled
  - Increased credit spreads (but from very low levels)
  - Commercial paper market freezing up

# The Housing Downturn

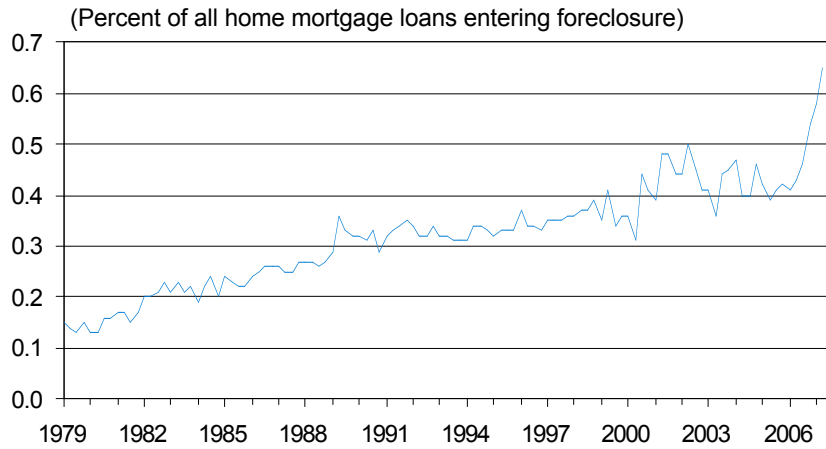


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## Residential Construction Adjustment – Much More To Come...



## Foreclosure Rate Has Hit New Highs



Source: Mortgage Bankers Association

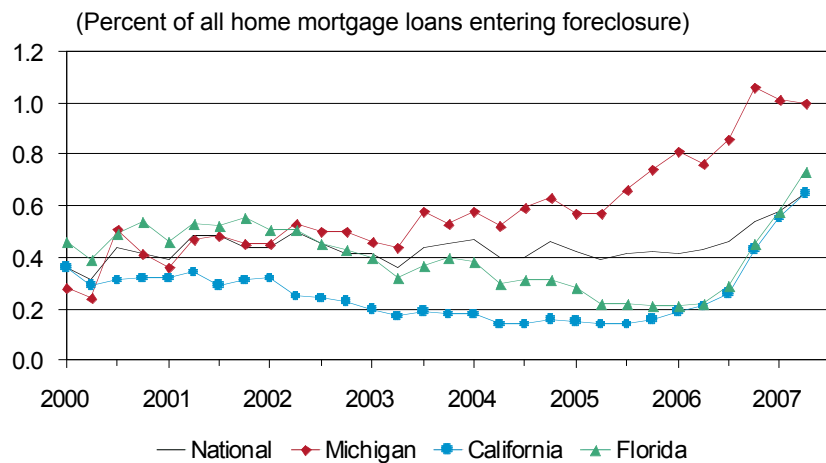


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## Key State Foreclosure Variations



Source: Mortgage Bankers Association

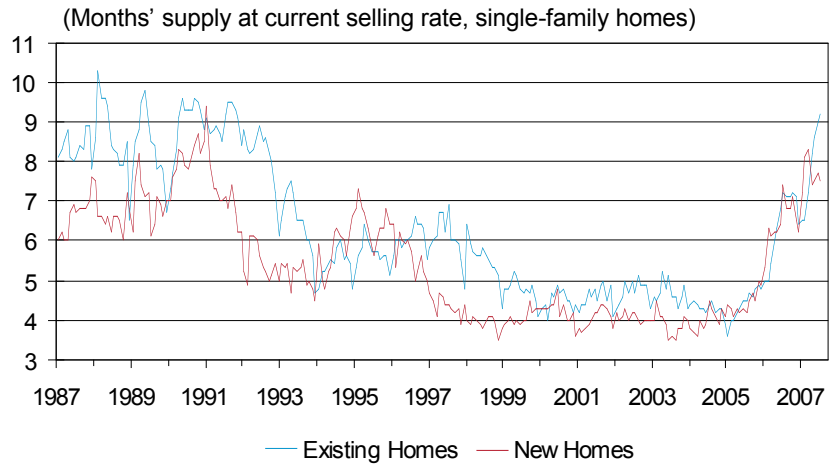


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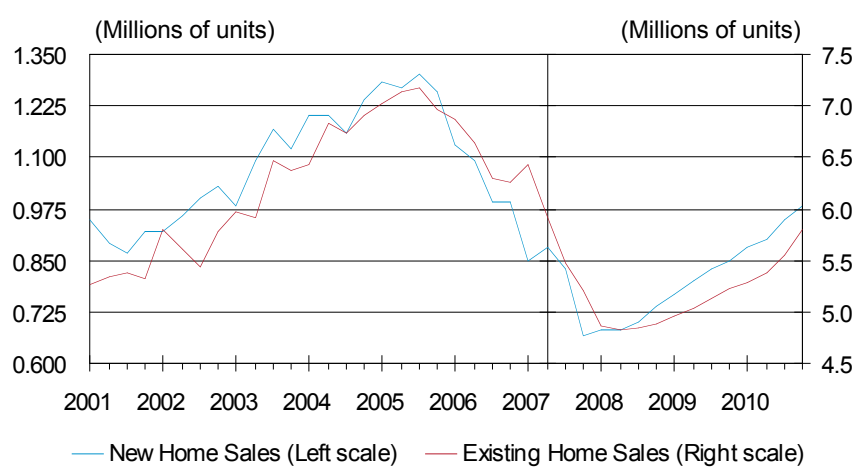
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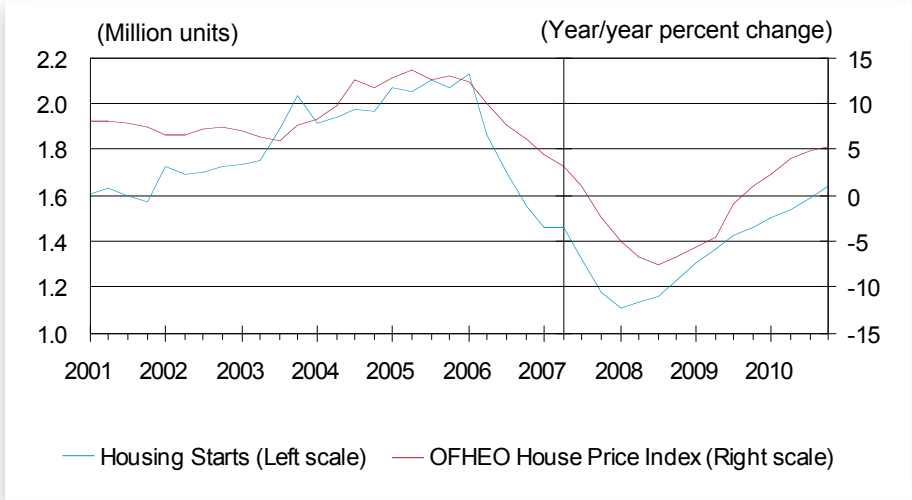
## Bloated Supplies of Homes for Sale



## Home Sales Have Further To Fall



## Housing Starts Dip Further, Prices To Fall



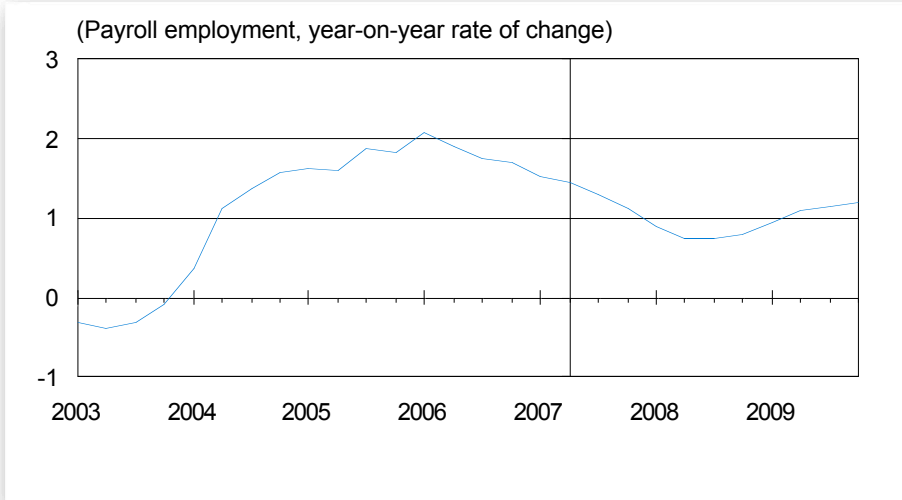
**Consumers at Risk**

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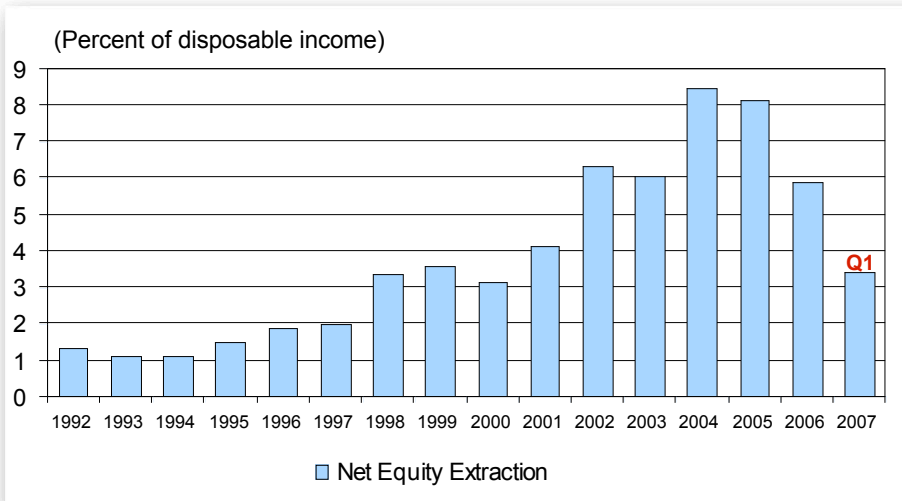
Consumers at Risk

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## Employment Growth Decelerating

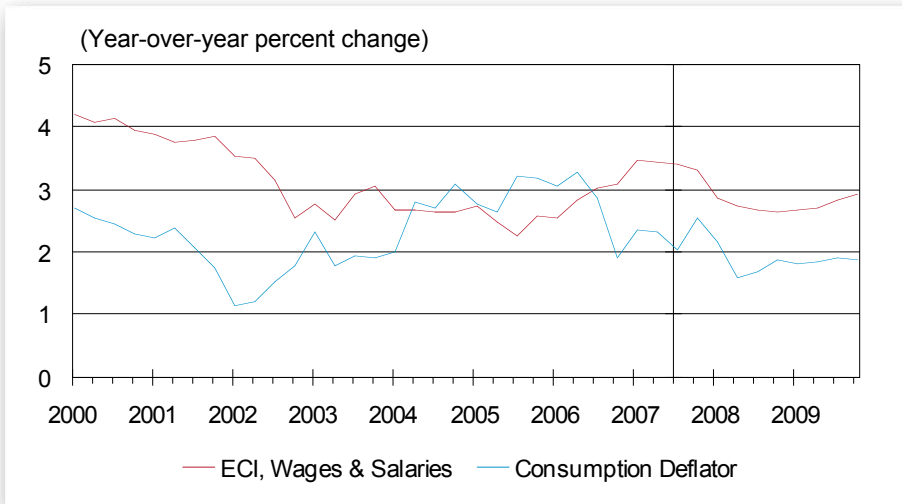


## Mortgage Equity Withdrawal Has Been Fueling Consumer Spending, and Is Fading

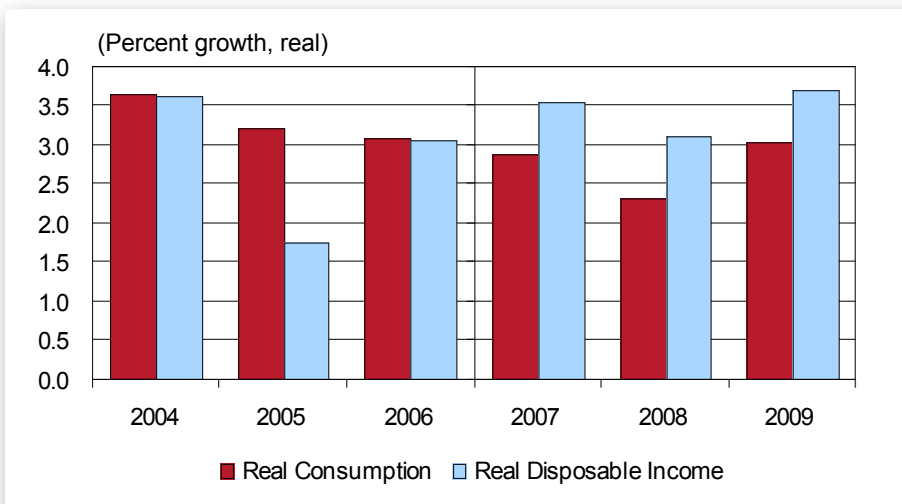


Source: Federal Reserve - Kennedy/Greenspan data updated as of June 2007

## Good News: Wage Growth Outpacing Price Inflation



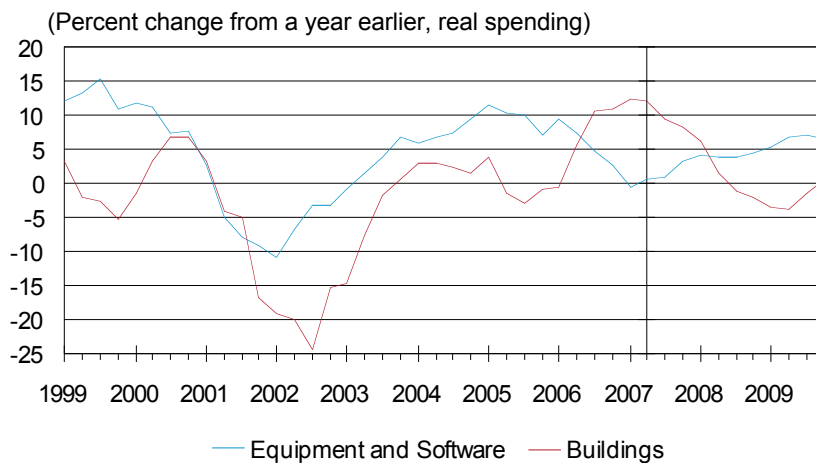
## Consumption Growth Will Slow Further



## Business Investment Has Been Less Supportive Than Hoped

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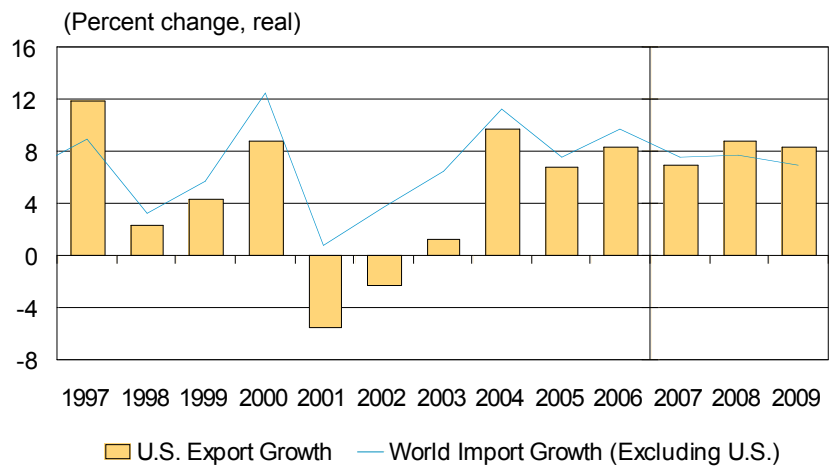
### The Business Capital Spending Cycle: Construction Has Taken the Lead



## Foreign Trade: Export-Led Growth

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### U.S. Export Growth Is Catching Up with World Trade Growth — Helped By the Falling Dollar

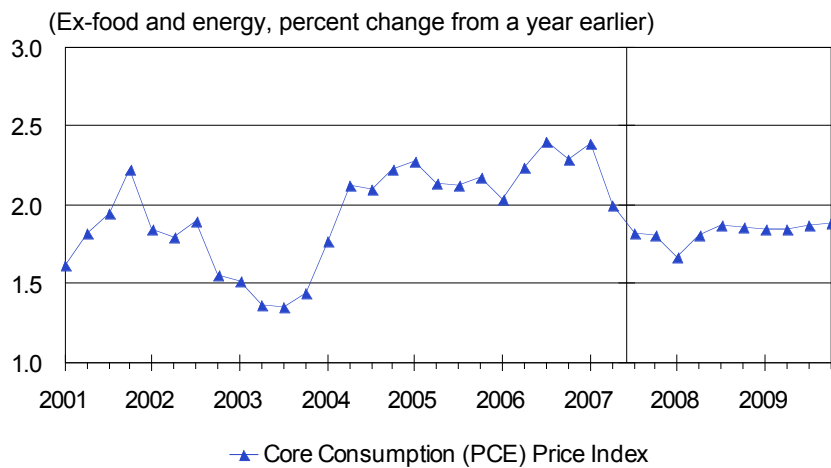


# Inflation and Interest Rates

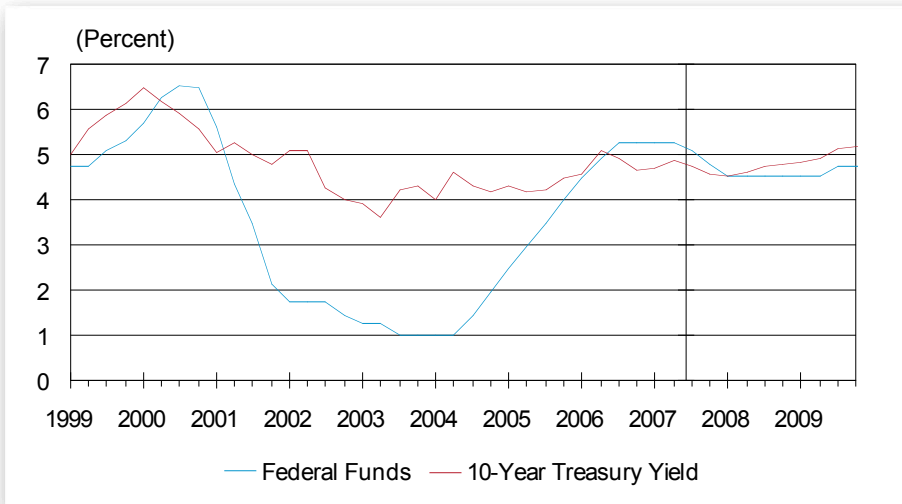


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## Core Consumer Inflation Moving Below 2%

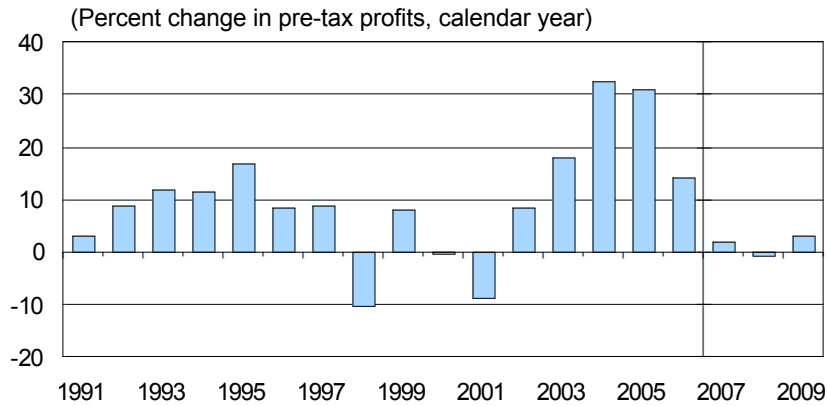


## We Expect the Fed To Cut Interest Rates

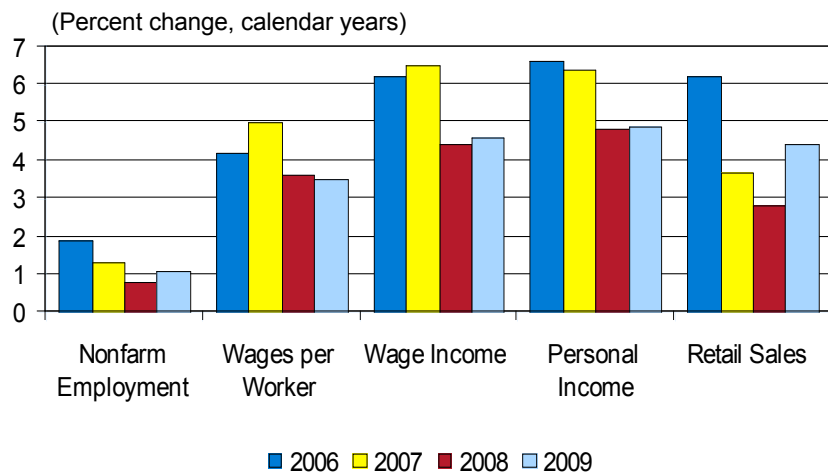


## Government Revenue Issues

## The Profits Boom Is Out Of Steam



## Other Key Indicators Affecting State Budgets



## Bottom Line

- **Sluggish growth at best; housing has further to fall, the consumer will be cautious**
- **A deeper slowdown is the main risk (recession risk: 30%)**
- **The prospect of growth sliding below 2% should trigger rate cuts**
- **Downside Risk (1): Credit contagion worsens, spills over more severely to the U.S. and global economies**
- **Downside Risk (2): Vulnerability to another energy shock remains high**
- **Downside Risk (3): Mutual Assured Destruction: Protectionism at home, buyer's strike against Treasuries by China**

# Thank You!

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