Top-10 Economic Predictions for 2010
And Implications for Trade

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Global Outlook

• The recession is over and the recovery has begun – unfortunately, for most developed economies, this recovery won’t feel like one in its early stages

• Strong tail winds (policy stimulus, improved financial conditions and pent-up demand) …

• … Are being partially neutralized by equally strong head winds (rising unemployment rates, lingering hangovers from housing bubbles and the financial crisis, and the winding down of fiscal stimulus)

• Global growth at 2.8% in 2010 will be well below the 3.5% to 4% trend rate of the last two decades
The World Economy Rebounds from the Worst Recession of the Postwar Era

(Percent change)


Real GDP  Industrial Production
The World’s Real Economic Growth by Sector

(Percent change)

GDP  Private Consumption  Fixed Investment  Government Consumption  Exports

2008  2009  2010  2011
World Trade Volumes Plummeted in 2009
1. The U.S. Recovery Will Start Slowly

- During much of 2010, growth will be stuck in the 2.0% to 2.5% range

- Consumer spending is being held back by the strong headwind of a rising unemployment rate – expected to peak at around 10.5% in the first quarter

- The housing recovery, business spending on equipment and inventory rebuilding will boost growth...

- ...While non-residential construction and state-and-local spending will be a drag on the recovery

- Despite strong growth in exports, net trade will be a negative factor as imports will grow even faster
U.S. Real GDP Is Recovering, But the Unemployment Rate Will Rise into 2010

(Annual percent change, 2005 dollars) (Percent)

Real GDP Growth (Left scale) - Unemployment Rate (Right scale)
### U.S. Economic Growth by Sector

(Percent change unless otherwise noted)

<table>
<thead>
<tr>
<th>Sector</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>0.4</td>
<td>-2.5</td>
<td>2.6</td>
<td>2.7</td>
</tr>
<tr>
<td>Final Sales</td>
<td>0.8</td>
<td>-1.7</td>
<td>1.6</td>
<td>2.5</td>
</tr>
<tr>
<td>Consumption</td>
<td>-0.2</td>
<td>-0.6</td>
<td>2.1</td>
<td>2.2</td>
</tr>
<tr>
<td>Light Vehicle Sales (Millions)</td>
<td>13.2</td>
<td>10.3</td>
<td>11.5</td>
<td>13.8</td>
</tr>
<tr>
<td>Residential Investment</td>
<td>-22.9</td>
<td>-20.1</td>
<td>5.7</td>
<td>24.8</td>
</tr>
<tr>
<td>Housing Starts (Millions)</td>
<td>0.90</td>
<td>0.56</td>
<td>0.79</td>
<td>1.24</td>
</tr>
<tr>
<td>Business Fixed Investment</td>
<td>1.6</td>
<td>-18.0</td>
<td>-0.8</td>
<td>9.5</td>
</tr>
<tr>
<td>Federal Government</td>
<td>7.7</td>
<td>5.1</td>
<td>4.1</td>
<td>-3.0</td>
</tr>
<tr>
<td>State and Local Government</td>
<td>0.5</td>
<td>0.0</td>
<td>0.4</td>
<td>-0.3</td>
</tr>
<tr>
<td>Exports</td>
<td>5.4</td>
<td>-9.9</td>
<td>9.3</td>
<td>5.5</td>
</tr>
<tr>
<td>Imports</td>
<td>-3.2</td>
<td>-14.1</td>
<td>9.7</td>
<td>6.7</td>
</tr>
</tbody>
</table>
U.S. Inventory Adjustment Is Nearly Complete

(Inventory/shipments ratio, manufacturing and trade)
U.S. Corporate Cash Flow Strengthening

(Net corporate cash flow, excluding net capital transfers, percent of GDP)
Different Cycles in U.S. Business Capital Spending: Construction Lags

(Year-over-year percent change, 2005 dollars)

- Blue line: Equipment and Software
- Red line: Structures
U.S. Households Have Increased Their Saving Rate in Response to the Decline in Net Worth

Saving Rate vs. Household Net Worth/Disposable Income

(Percent of disposable income) vs. (Ratio)


4.0 4.5 5.0 5.5 6.0 6.5 7.0

Saving Rate vs. Household Net Worth/Disposable Income
U.S. Real Export and Import Growth Patterns Reflect the Business Cycle and Exchange Rates

(Year-over-year percent change, 2005 dollars)

- Real U.S. Exports
- Real U.S. Imports
Capital Goods Lead Growth in Real U.S. Exports

(Annual percent change, 2005 dollars)

- Computer Equipment
- Autos & Parts
- Other Capital Equipment
- Aircraft
- Industrial Materials
- Consumer Goods
- Foods & Feeds

- 2003-08
- 2008-13

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U.S. Housing: The Good, The Bad, and the Uncertain

- The Good
  - Housing affordability is at record highs
  - Single-family activity indicators are improving
  - Prices are showing signs of stabilizing

- The Bad
  - Foreclosure rate still rising
  - Overhang of empty homes
  - No improvement yet in multi-family indicators

- The Uncertain
  - How much payback after the new home-buyers’ credit expires?
  - What happens to mortgage rates when the Fed stops buying MBS and agency debt?
U.S. Banks Still Tightening Credit Conditions

Source: Diffusion Indexes from Fed Senior Loan Officer Survey
2. Europe and Japan Will Recover Even More Slowly Than the U.S.

• Second and third quarter growth rates in both Europe and Japan overstate the strength of the recovery

• Recent Eurozone data show a loss of momentum – how big of a risk is a W?

• While the worst of the financial crisis is over, there could be more aftershocks (including a possible sovereign default in the Eurozone), and credit remains tight

• Houses are still over-valued in some markets (Ireland, Spain, U.K. etc.) – how big of a vulnerability is this?

• Some European economies (including those of Iceland and Spain) will continue to contract in 2010

• The substantial downward revision of Japanese growth in the third quarter (from 4.8% to 1.3%) is troubling…

• …As is the sharp increase in the pace of deflation in recent months

• Recent attempts by the Japanese government to stimulate the economy are likely to disappoint

• Appreciating currencies are a major headwind for both the Eurozone and Japan
Deep Recessions, Slow Recoveries in Western Europe

(Percent change, real GDP)

Germany  U.K.  France  Italy  Spain

2008 2009 2010 2011
Japan’s Economy Has Limited Growth Potential

(Percent change, real GDP)

- Non-Japan Asia will be at the forefront, with a growth rate of over 7% next year
- Latin America, the Middle East, and Africa will see gains in the 3% to 4% range
- The laggard will be Emerging Europe, which will only grow between 1.5% and 2%
- Many emerging regions are benefitting from the sharp rebound in trade and the turn in the inventory cycle – can these be the basis for sustained growth?
- With the exception of Emerging Europe and some Gulf states, the impact of the financial crisis on the emerging markets has been modest
- Among the Big-6 emerging economies, China, India and Brazil will lead, while Russia, South Korea and Mexico will lag
Emerging Markets Lead the Global Recovery

(Percent change, real GDP)


- World
- Advanced Countries
- Emerging Markets
Long-Term World Economic Growth by Region

(Real GDP, annual percent change)

- NAFTA
- Other Americas
- Western Europe
- Emerging Europe
- Japan
- Other Asia-Pacific
- Mideast & Africa
- Sub-Saharan Africa

- 1998-2008
- 2008-18
- 2018-28
Strong Rebound in Asia

(Percent change, real GDP)

2008 2009 2010 2011
Respectable Recoveries in Latin America

(Percent change, real GDP)
Real GDP Growth in the Middle East and Africa

(Percent change, real GDP)

Saudi Arabia  Iran  South Africa  UAE  Israel  Nigeria  Kuwait

-6  -4  -2  0  2  4  6  8

2008  2009  2010  2011
Deep Recessions and Slow Recoveries in Emerging Europe

(Percent change, real GDP)

Russia  Turkey  Poland  Czech Republic  Hungary  Romania

2008  2009  2010  2011
4. Interest Rates in the G-7 and the BRICs Will Remain Low

- Some central banks (notably Australia, Israel and Norway) have already started to raise rates

- The Fed, the ECB, the Bank of England and the Bank of Japan are unlikely to hike rates until the third quarter – although the “quantitative easing” measures will be phased out before then

- The G-7 central bankers are currently more worried about the fragility of the recovery and the aftershocks of the financial crisis than inflation

- Some Asian central banks (e.g., the Reserve Bank of India and the Peoples Bank of China) may pull the trigger in the first or second quarter, due to concerns about inflation and asset bubbles
Policy Interest Rates Will Stay Low into 2010

(Percent, end of quarter)
Policy Interest Rates in BRICs

(Percent, end of quarter)

* One-year loan rate
5. Fiscal Stimulus Will Begin to Ease

• Shaky public finances and voter unease severely limit the scope for any further stimulus – some countries will actually be tightening fiscal policy next year (e.g., the U.K.)

• Temporary measures (such as cash-for-clunker programs) have ended or will soon end

• The pressure on the U.S., European and Japanese governments to put in place credible deficit and debt reduction plans is likely to intensify

• The recently announced U.S. jobs program will only be feasible by using budgetary sleight of hand (i.e., TARP money)

• The biggest fiscal challenge in the medium- to long-term will be the pressure from public pensions and healthcare programs
A Record U.S. Federal Budget Deficit in Fiscal 2009

(Billions of dollars, fiscal years) (Percent of GDP)

Unified Budget Deficit (Left scale)  Deficit as % of GDP (Right scale)
U.S. Fiscal Stimulus Has Made A Difference

(Annualized rate of growth)

- Baseline
- No Fiscal Stimulus
Fiscal Balances Have Deteriorated Across Regions

(Federal budget balance, % of GDP)

Source: IHS Global Insight
Public Debt Is Rising in Many Countries

(Gross Debt, Percent of GDP)

- Canada
- Germany
- France
- United Kingdom
- United States
- Italy
- Japan

Source: IMF
6. Commodity Prices Will Move Sideways

• The recent rises in commodity prices cannot be justified by market fundamentals – demand growth is weak and inventories are high

• Some of the increases of the past few months can be attributed to investment flows – is this the start of a new “bubble”?

• Most commodity prices are likely to soften in coming months – some already have in recent weeks

• A sustained rise in commodity prices is unlikely until the global recovery picks up steam at the end of 2010
A Rebound in Industrial Materials Prices

(IHS Global Insight Indexes, 2002:1=1.0)
Crude Oil and Natural Gas Prices Diverge

Crude Oil (Left scale)  Natural Gas (Right scale)

($/barrel, WTI)  ($/million Btu, Henry Hub)
7. Inflation Will (Mostly) Not Be a Problem

• Historically-high levels of unemployment and excess capacity will limit both wage and price inflation – also strong productivity growth in the U.S. has been a powerful disinflationary force

• Central banks will most likely remove the excess liquidity sloshing around the global economy, before inflation expectations begin to rise much

• Strong growth in Asia will probably mean that inflationary pressures will be felt in that region first

• Also at risk of rising inflation are countries that peg (or strongly manage) their exchange rates to the dollar – mostly in Asia and the Middle East
Labor Market Slack Will Limit Wage Inflation

(Unemployment rates, percent in October/November, 2009)

Spain 20
France 10
United States 10
Eurozone 10
China 9
Canada 8
Germany 8
United Kingdom 7
Italy 7
Japan 5
Output Gaps Will Limit Price Inflation

(Percent of potential GDP, 2009)

Japan  United States  Eurozone  U.K.  Germany

Source: OECD
Aggressive Cost-Cutting Has Boosted U.S. Productivity and Reduced Unit Labor Costs

(Q/Q annualized growth rates)
Consumer Price Inflation Will Be Tame (Almost) Everywhere

(Percent change)

* Excluding Zimbabwe
8. After Improving for a While, Global Imbalances Will Worsen Again

- The recent sharp improvement in the U.S. current account is mostly due to the deep U.S. recession and the big drop in oil prices.

- The less dramatic fall in the current account surpluses in other parts of the world reflects the sharp contraction in world exports and the drop in commodity prices.

- The U.S. current account deficit will increase again, as the American recovery outpaces that of the other developed economies.

- Likewise, continuing dependence on export-led growth in many large economies (e.g., Germany, China and the rest of Asia) will contribute to the worsening in global imbalances.
The U.S. Current Account Deficit Will Widen Again

(Billions of dollars) (Percent of GDP)


-1,000 -800 -600 -400 -200 0 200

-7.5 -6.0 -4.5 -3.0 -1.5 0.0 1.5

Current Account Deficit - Deficit as a % of GDP
Current Account Imbalances Remain Large

(Billions of dollars)


- United States
- Western Europe
- Japan
- Asia exc. Japan
- Middle East
9. While the Dollar May Strengthen a Little, It Is on a Downward Glide Path

- The dollar is probably oversold relative to the euro and the yen, given the slightly better growth prospects of the U.S. economy – so a small appreciation in the next few months is likely

- Nevertheless, given that progress on the global imbalances has been temporary, the downward pressure on the dollar will continue

- The depreciation of the dollar is likely to be the largest vis-à-vis some emerging market currencies (especially the “floaters”)

- Notwithstanding complaints about a weak dollar, many developed country currencies have been declining on an inflation-adjusted, trade-weighted basis – this is especially true of the yen

- Despite being fixed relative to the dollar, the Chinese renminbi, is sharply down against the euro and on a real trade-weighted basis
U.S. Dollar Exchange Rates

**Canadian Dollar**
(Canadian dollars per U.S. dollar, quarterly averages)

**Euro**
(Euro per U.S. dollar, quarterly averages)

**Japanese Yen**
(Yen per U.S. dollar, quarterly averages)

**Chinese Renminbi**
(Yuan per U.S. dollar, quarterly averages)
Real Effective (Trade-Weighted) Exchange Rates

(Index, base year 2005=100)


United States

Germany

Japan

China
10. The Risk of a “Hard W” Is Still Uncomfortably High

- The risk of a “hard W” is about one in five, and the list of possible triggers is long
- Fiscal and monetary policies could be tightened prematurely
- Consumer spending could collapse in the face of rising unemployment
- Oil prices could rise either because of a supply disruption or increased speculative activity
- A few large financial institutions could still fail
- It would probably take a combination of these factors to drag the global economy back into negative territory
- The good news is that the risks to global growth are evenly balanced, with upside risks including a quicker and stronger release of pent-up demand
U.S. Scenarios

(Annualized rate of growth)

2008 2009 2010 2011

Baseline (60%)  Pessimistic Scenario (20%)  Optimistic Scenario (20%)
Risks on Both Sides

• Downside Risks
  • Private demand not ready to take over when stimulus is withdrawn (perhaps a policy error is made)
  • Productivity keeps booming—household incomes suffer, firms save the profits
  • Commercial real estate woes reignite the financial crisis
  • Policy fears—e.g. health care, cap-and-trade

• Upside Risks
  • Massive fiscal and monetary stimulus still in the pipeline
  • Pent-up demand is accumulating after the “panic” spending cuts during the end-08/early-09 economic free-fall
  • Prolonged growth surge in Asia, weak dollar boost exports more than expected
Global Scenarios

(Percent change in real world GDP)

2009 2010 2011

Baseline (60%)  Hard W (20%)  Faster Recovery (20%)
Trade Implications
World Trade Typically Grows Faster Than Real GDP

(Percent change)

GDP  Trade
U.S. International Trading Partners Are Shifting

(Exports, trillions of U.S. dollars)

Source: Global Insight World Trade Service
Growth in Global Merchandise Trade

(Trillions of U.S. dollars)

Source: Global Insight World Trade Service
## Containerized Trade Movements

(Thousands of TEUs)

<table>
<thead>
<tr>
<th>Year</th>
<th>Transatlantic</th>
<th>Transpacific</th>
<th>U.S. Atlantic/Asia</th>
<th>Europe/Asia</th>
<th>Intra-Asia</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>5,397</td>
<td>16,425</td>
<td>3,661</td>
<td>14,774</td>
<td>23,227</td>
<td>94,216</td>
</tr>
<tr>
<td>2010</td>
<td>4,623</td>
<td>17,364</td>
<td>4,559</td>
<td>17,595</td>
<td>27,708</td>
<td>114,429</td>
</tr>
<tr>
<td>2020</td>
<td>6,523</td>
<td>31,194</td>
<td>8,259</td>
<td>31,270</td>
<td>51,442</td>
<td>196,976</td>
</tr>
<tr>
<td>2025</td>
<td>7,705</td>
<td>40,437</td>
<td>10,713</td>
<td>40,682</td>
<td>66,198</td>
<td>250,028</td>
</tr>
</tbody>
</table>
Transatlantic Container Trade

(Millions of TEUs)

North America to Europe  Europe to North America
Transpacific Container Trade

(Millions of TEUs)

Asia to North America

North America to Asia

Container Growth Rates By U.S. Coast

(Percent change in TEUs)
Implications for the Port

• The trade recovery from last year’s low has begun

• Pace of trade volume recovery is slow

• Export growth to Asia will be strong …

• … While European trade will remain weak

• This explains the East Coast/West Coast differences in container traffic

• Bottom line: it will get better but slowly
Thank you!

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