



An Economic Overview from a Summit Perspective – 2011

Things seem better. Maybe the dark storm clouds are fading with the New Year. There are clear signs that the US economy is getting stronger; having fought its way back from a long and difficult journey of 2008 and 2009. As the outlook gains momentum (helped in part by the policy stimulus) we expect the pace of our domestic recovery to accelerate. GDP growth over the next few years is expected to hit 3.5% to 4%. Even with the recent gains in our equity markets, we feel the recovery has been sub-par. Rebounds from previous recessionary periods have moved along faster than our current recovery. Much of this is due to a still-weakening housing and stagnate credit market. Many experts feel the housing market (in general) will stay weak for many, many years. This clearly will interfere with any normal dynamics in the recovering U.S. economy. We saw the impact of this during this past summer, when we seemed to have lost some steam.

Another concern is found with a weak employment forecast. Structurally unemployment will be here for years to come. The labor market will not return to normal levels until companies can begin to feel confident in adding more jobs; hiring more and more people in response to an improving outlook for aggregate demand. We feel the jobless rate will approach 9% through 2011, and even with a growing economy remain above 8% for 2012. It will take a sustained recovery (maybe 4 to 5 years) before we would expect an unemployment rate to return to levels (5%) that existed before the 2008 downturn hit.

There are plenty of positive signs popping up. The policy stimulus packet coupled with the likely extension of the Bush-era tax rates will support further economic health this year. We have reduced our payroll tax (temporarily) and extended the unemployment benefits which should provide extra support to an already revived economy. Banks are slowly beginning to allow loans again. Even with households de-leveraging, the recent signs for consumer spending have been encouraging. Corporate cash balances are staggering, and increased future capital expenditure in 2010 should continue. We expect this to become even greater in 2011 and 2012.

As for inflation, it appears that all future expectations remain very low. For at least the next year or two, we should see inflation remain below 1.5%. Deflation is unlikely; as aggregate demand and the recent efforts of the Fed will offer stability in pricing. Inflation will drift higher as the economy begins to accelerate at a faster pace. Prices will increase.

The Fed Monetary policymakers appear quite satisfied with the results of the large-scale asset purchases (LSAP) and buy backs in driving our recovery. Though interest rates (longer term) have just recently jumped, the FOMC are likely to keep the funds rate near zero until they are confident that our recovery can sustain itself. That probably means no hikes until 2012. Bad news for those investors currently still in money markets and CD's.

So what are the risks to our forecasts? What can go wrong? Where is the danger? Here are just few to consider:

What if the recovery does not hold momentum? What if home prices begin to drop (again), while financing remains restrictive? Can the banks fully recover – 2010 saw 157 bank failures! Will companies re-hire full-time workers? And what if they don't? Will the Fed's have the courage to tighten when (if) it becomes necessary? Can our leaders ultimately find the courage, long-term, to deal with our long-term fiscal issues? There will be some hiccups along the way; you can be certain of that.