Rabobank

Country report

UNITED STATES OF AMERICA

Summary

The US economic recovery is expected to continue this and next year, but growth will remain below trend. Political decision making is hampered by the Republican majority in the House of Representatives that Democratic president Obama faces. Any serious attempt to reduce the budget deficit is not expected until after the November 2012 Presidential and Congressional elections. Apart from current high budget deficits, the medium term challenge of reducing age related spending is big as well. It remains to be seen if the November 2012 elections will produce a result that would be more conductive to successful policymaking than we have seen over the past years. The twin government budget and current account deficit is expected to remain sizeable. As such, with continued dependence on foreign financing a disorderly adjustment of the value of the US dollar, a sharp rise in interest rates and a quick reversal of the current account deficit remain key tail risks.

Things to watch:

- Government deficit and debt reduction, political efficacy, election outcome
- Extended period of low interest rates possibly leading to asset price bubbles and inflation

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United States of America

National facts	
Type of government	Federal Republic
Capital	Washington, DC
Surface area (thousand sq km)	9,826.675
Population (millions)	310.2
Main languages	English (82.1%)
	Spanish (10.7%)
Main religions	Protestant (51.2%)
	Roman Catholic (23.9%)
Head of State (president)	Barack H. Obama
Head of Government	Barack H. Obama
Monetary unit	USD

Economy		2011
Economic size	*bn USD*	*% world total*
Nominal GDP	15094	21.88
Nominal GDP at PPP	15094	19.06
Export value of goods and services	2105	9.60
IMF quotum (in mln SDR)	42122	19.38
Economic structure	*2011*	*5-year av.*
Real GDP growth	1.7	0.8
Agriculture (% of GDP)	1	1
Industry (% of GDP)	23	23
Services (% of GDP)	76	76
Standards of living	*USD*	*% world av.*
Nominal GDP per head	48208	448
Nominal GDP per head at PPP	48208	390
Real GDP per head	42527	524

Social and governance indicators	rank / total
Human Development Index (rank)	4 / 187
Ease of Doing Business Index (rank)	4 / 183
Index of Economic Freedom (rank)	10 / 179
Corruption Perceptions Index (rank)	24 / 183
Press Freedom Index (rank)	47 / 178
Gini index (income distribution)	40.8

Foreign trade			2010
Main export partners (%)		*Main import partners (%)*	
Canada	19	China	20
Mexico	13	Canada	15
China	7	Mexico	12
Japan	5	Japan	6

Main export products (%)	
Capital goods (excl automotive)	35
Industrial supplies & materials	31
Consumer goods (non-food), excl automotive	13
Automotive vehicles, engines & parts	9
Main import products (%)	
Industrial supplies & materials	32
Consumer goods (non-food), excl automotive	25
Capital goods (excl automotive)	23
Automotive vehicles, engines & parts	12
Openness of the economy	
Export value of G&S (% of GDP)	13
Import value of G&S (% of GDP)	16
Inward FDI (% of GDP)	1.6

Source: EIU, CIA World Factbook, UN, Heritage Foundation, Transparency International, Reporters Without Borders, World Bank.

Economy on the mend

Economic growth in the US fell back sharply in the first half of 2011, partly due to high oil prices reducing household purchasing power and supply-chain disruptions caused by the earthquake and tsunami in Japan. Growth accelerated again in the second half of the year, but the 1.7% average annual growth rate of real GDP was down significantly from the 3% growth recorded in 2010. Average unemployment remained very high, at 9% versus 9.6% in 2010. But on this front, the second half of the year was also much better than the first, with the unemployment rate falling to 8.7% in the last quarter of 2011. In the first quarter of this year, this was followed by a further fall to 8.3%. After a modest increase in 2010, house prices continued their downward trajectory in 2011. The average house price for 2011 was down 4% on the year before according to the Case-Shiller index and was down 34% from the peak reached in the first half of 2006. This continued fall in house prices is hampering the deleveraging process of households, since at the same time that debt levels are being reduced the asset side of household balance sheets is still deteriorating. As a result, we expect consumption growth to remain modest both this year and next. Fiscal policy has already turned from stimulus to austerity when looking at government spending. The need to bring down the government deficit leaves precious little room for new stimulus, but further austerity is being postponed due to the deadlock in congress and 2012 being an election year. In all, we expect the economic recovery to continue, but at a projected 2% this year and 2¼% in 2013 the expansion will remain below trend and will only slowly bring down the unemployment rate. Given this outlook, after already keeping the policy rate at an exceptionally low level for almost three and a half years and with two rounds of quantitative easing, monetary policy is expected to remain very accommodative for quite some time to come. An important uncertainty in the medium term relates to the possibility of a timely and successful retracement from this policy stance to avoid new asset price bubbles or high inflation.

Budget Control Act only a first step toward deficit reduction

Any serious attempt to reduce the budget deficit is not expected until after the November 2012 Presidential and Congressional elections. With a Republican majority in the House of Representatives and a Democratic majority in the Senate and in the White House, it has proven very hard to develop much needed plans to reign in the current budget deficit and make future budgets more resilient to ageing of the population. The need for deficit reduction is recognized by both parties, but there are crucial differences as to how to achieve it. The Republicans are allergic to higher taxes while the Democrats want to steer clear of cutting spending. Those differences have not been overcome. The uncertainty that resulted from this stalemate last year has largely been solved by the Budget Control Act of 2 August 2011, that stipulated $ 900 bn in deficit reductions and left another $ 1.2 bn in cuts to be decided by the Joint Select Committee on Deficit Reduction. The committee failed to reach an agreement, but importantly the Budget Control Act stipulates that if this were to happen automatic caps on spending will become active in 2013. This has resolved the uncertainty created by the political inability to reach budgetary agreements. It remains to be seen if the November 2012 elections will produce a result that would be more conductive to successful policymaking than we have seen over the past years. An outcome where both Houses of Congress have different party majorities or where both Houses of Congress have the same majority but the White House is occupied by a president of the other party will likely extend the current situation. This would be very problematic since although the automatic spending cuts will ensure some reduction in the budget deficit, the US faces a sizeable challenge in addressing long term pressure from spending on age related expenditure. At 9.6% of GDP in 2011, the general government deficit remains very high. The IMF, which basis its forecasts only on planned budgetary efforts, expects the deficit to be lowered to 6.2% of GDP in 2013 but to remain above 5.5% until 2016. The general government gross debt to GDP ratio is expected to rise to 115% in 2016 from 100% last year, with the Federal debt ratio rising to over 88%. While we would expect policy to prevent such a continuous rise in the debt ratio, an unfavourable election outcome may well lead to these IMF projections coming true.

Dollar still retains its safe haven status

Despite a sharp correction in the current account deficit, from 6% of GDP in 2006 to 3.2% last year, the situation of twin deficits (both a current account deficit and a government deficit) remains, and is expected to extend into the foreseeable future. The government deficit is expected to fall only gradually in the coming years. The current account deficit is expected to remain sizeable, although not as big as before recession. As such, the country as a whole will remain dependent on foreign financing. Despite the steep rise in borrowing, treasury yields are still low, with the 10-year rate hovering around 2% since September 2011 while the two year yield has not been above 0.5% since May last year. The US government is still benefitting from the special role of the US dollar in global financial markets, with US government debt still the world risk-free benchmark and the main safe haven in times of crisis. With the Eurozone crisis boosting demand for safe haven assets, this takes the focus firmly away from the budgetary problems of the US government for now. However, the extended period of low interest rates seen up until now can, if not managed correctly, potentially lead to inflation or inflated asset prices. A loss of confidence in the US economy and the US dollar can push up interest rates, which could lower potential economic growth. Though not our baseline expectation, the state of US public finances and the political situation has the potential to undermine global investor confidence. With the continued existence of the current account deficit, a disorderly depreciation of the dollar and a quick current account reversal remains a key, though low probability, risk.

United States

Selection of economic indicators	2007	2008	2009	2010	2011	2012e	2013f
Key country risk indicators							
GDP (% real change pa)	1.9	-0.3	-3.5	3.0	1.7	2.2	2.1
Consumer prices (average % change pa)	2.9	3.8	-0.3	1.6	3.1	2.3	2.2
Current account balance (% of GDP)	-5.1	-4.7	-2.7	-3.2	-3.1	-3.2	-3.0
Economic growth							
GDP (% real change pa)	1.9	-0.3	-3.5	3.0	1.7	2.2	2.1
Gross fixed investment (% real change pa), SA	-1.9	-7.1	-18.8	2.6	6.8	5.7	5.7
Private consumption (real % change pa), SA	2.3	-0.6	-1.9	2.0	2.2	2.3	2.5
Government consumption (% real change pa), SA	1.3	2.6	1.7	0.7	-2.1	-1.1	-0.3
Exports of G&S (% real change pa), SA	9.3	6.1	-9.4	11.3	6.7	3.3	4.3
Imports of G&S (% real change pa), SA	2.4	-2.7	-13.6	12.5	4.9	3.2	5.1
Economic policy							
Budget balance (% of GDP)	-1.2	-3.2	-10.2	-9.0	-8.7	-7.6	-6.4
Public debt (% of GDP)	36	40	54	63	68	74	76
Money market interest rate (%)	5.0	2.1	0.3	0.2	0.2	0.2	0.2
M2 growth (% change pa)	6	7	8	2	7	14	10
Consumer prices (average % change pa)	2.9	3.8	-0.3	1.6	3.1	2.3	2.2
Exchange rate LCU to USD (average)	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Recorded unemployment (%)	4.6	5.8	9.3	9.6	9.0	8.0	7.7
Balance of payments (mln USD)							
Current account balance	-710304	-677134	-376551	-470898	-473400	-511100	-500300
Trade balance	-818886	-830108	-505910	-645857	-738300	-752800	-781800
Export value of goods	1163957	1307499	1069491	1288699	1497400	1544200	1640800
Import value of goods	1982800	2137600	1575400	1934600	2236000	2297000	2423000
Services balance	122161	131771	124639	145829	178300	186400	187800
Income balance	101485	147089	128001	165225	221100	203400	248500
Transfer balance	-115063	-125888	-123281	-136095	-134600	-148100	-154800
Net direct investment flows	-192870	-18989	-145030	-115120	-178380	-45070	-27820
External position (mln USD)							
International investment position	-1796000	-3260200	-2396500	-2470900	n.a.	n.a.	n.a.
Total assets	18399700	19464700	18487000	20315400	n.a.	n.a.	n.a.
Total liabilities	20195700	22724900	20883500	22786300	n.a.	n.a.	n.a.
Key ratios for balance of payments, external solvency and external liquidity							
Trade balance (% of GDP)	-5.8	-5.8	-3.6	-4.4	-4.9	-4.8	-4.7
Current account balance (% of GDP)	-5.1	-4.7	-2.7	-3.2	-3.1	-3.2	-3.0
Inward FDI (% of GDP)	1.6	2.2	1.1	1.6	1.5	1.4	1.6
International investment position (% of GDP)	-12.8	-22.8	-17.2	-17.0	n.a.	n.a.	n.a.

Source: EIU