

The Outlook for the U.S. Economy Recovery and Long-Term Challenge

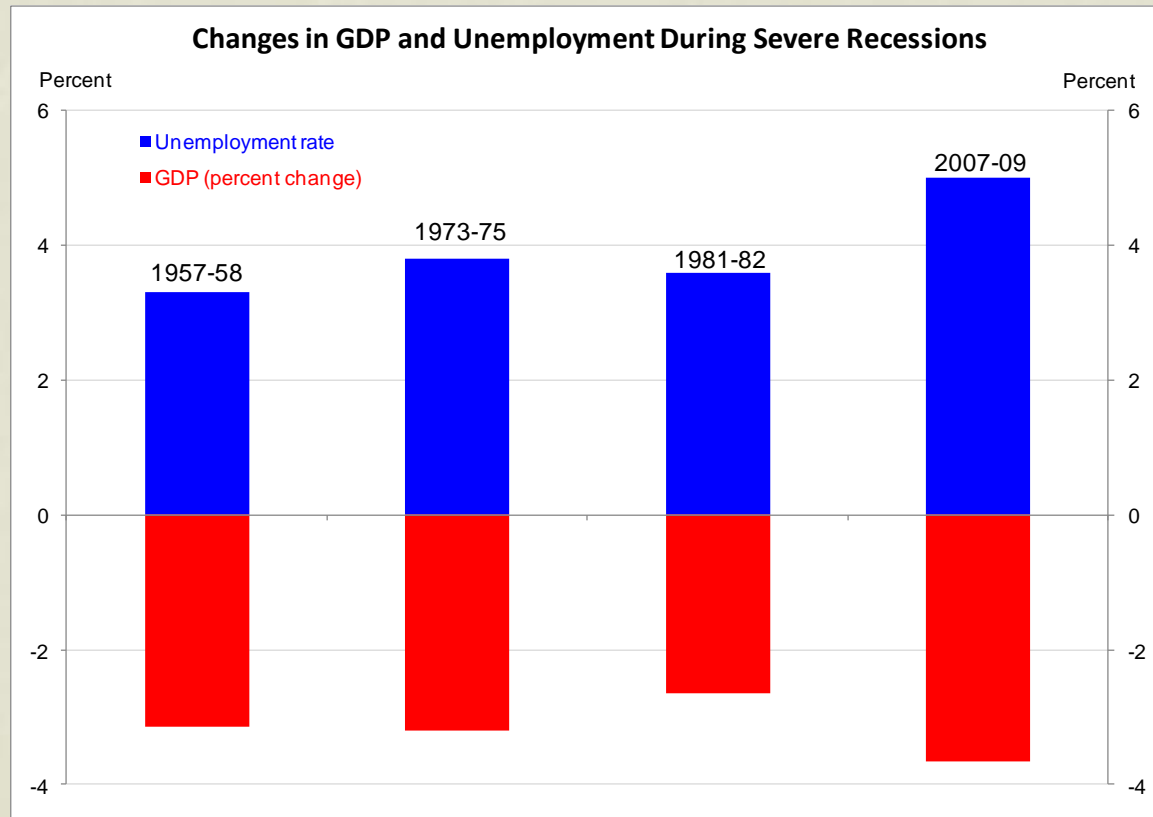
Oklahoma Economic Forums

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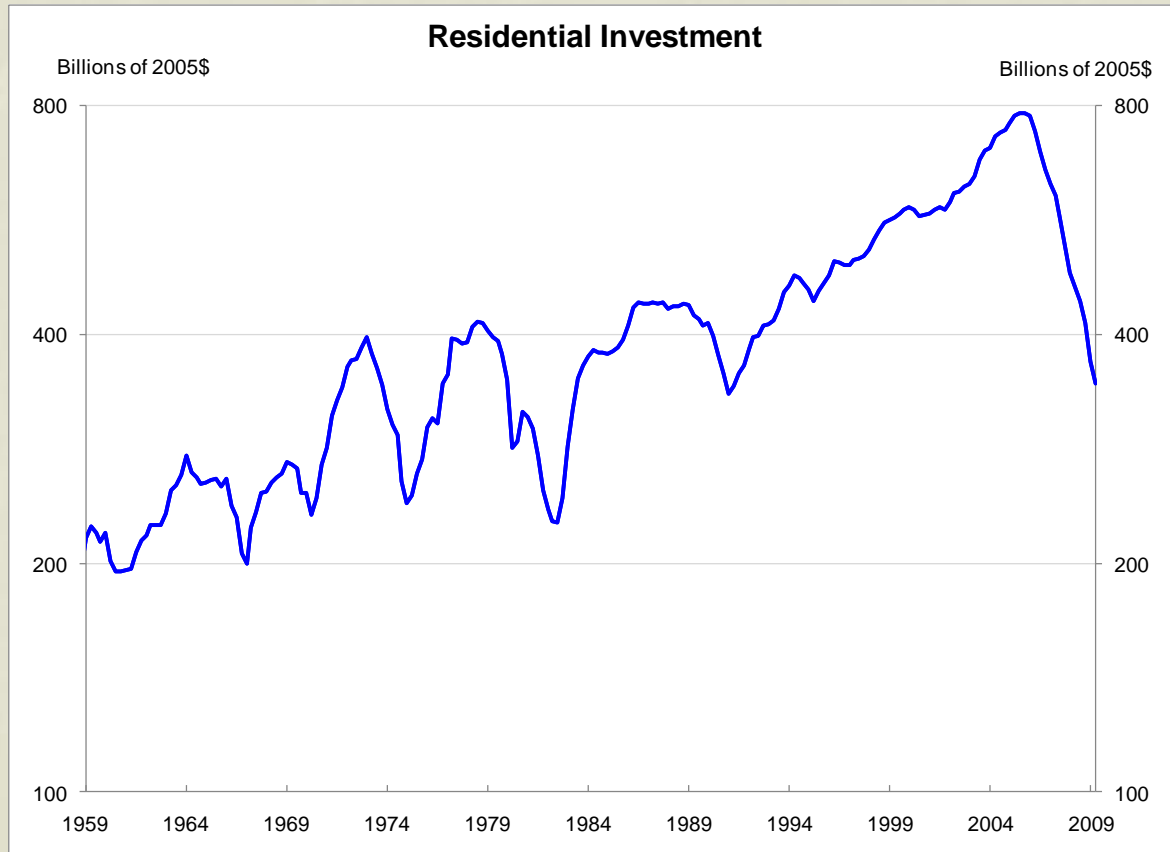
Overview

- Current conditions
 - Severe recession coming to an end
 - Improving financial conditions
- Medium-term outlook for U.S. economy: gradual recovery and low inflation
- Long-term challenge: sustainable fiscal policy

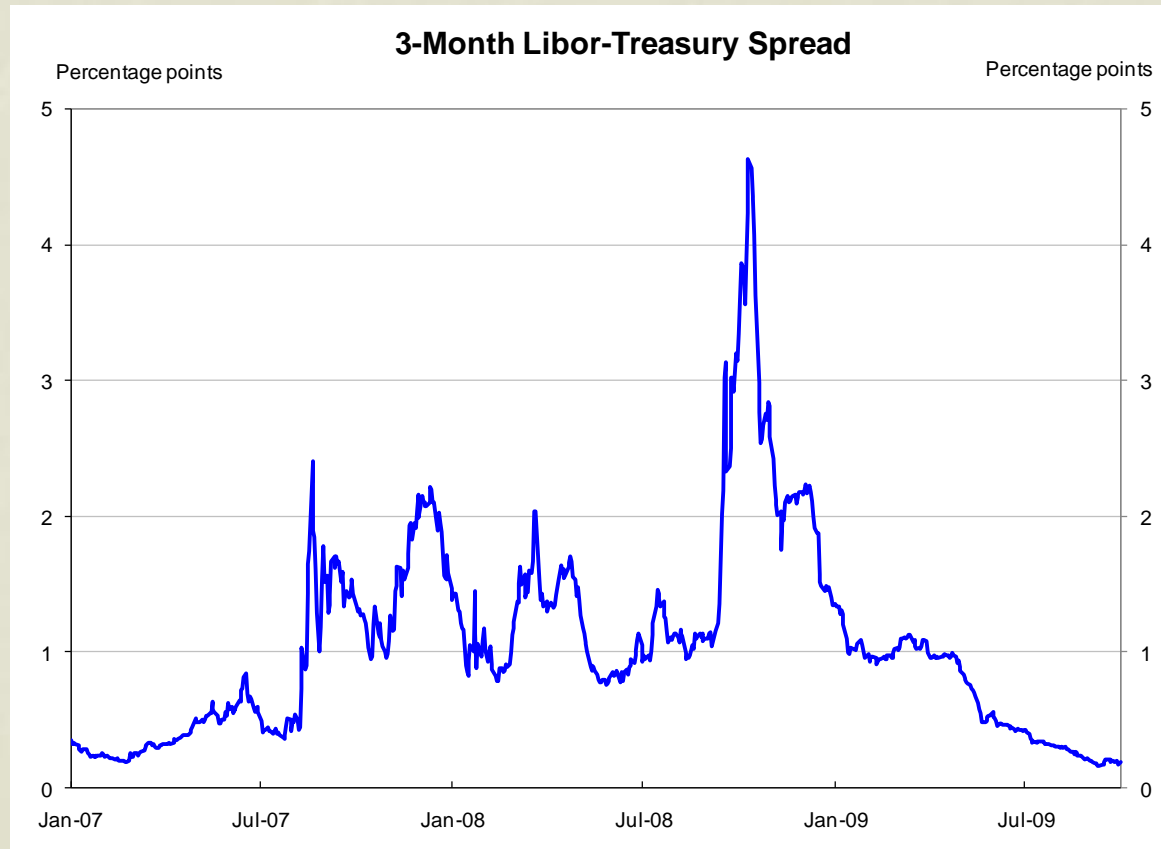
Current recession: Worst post-war



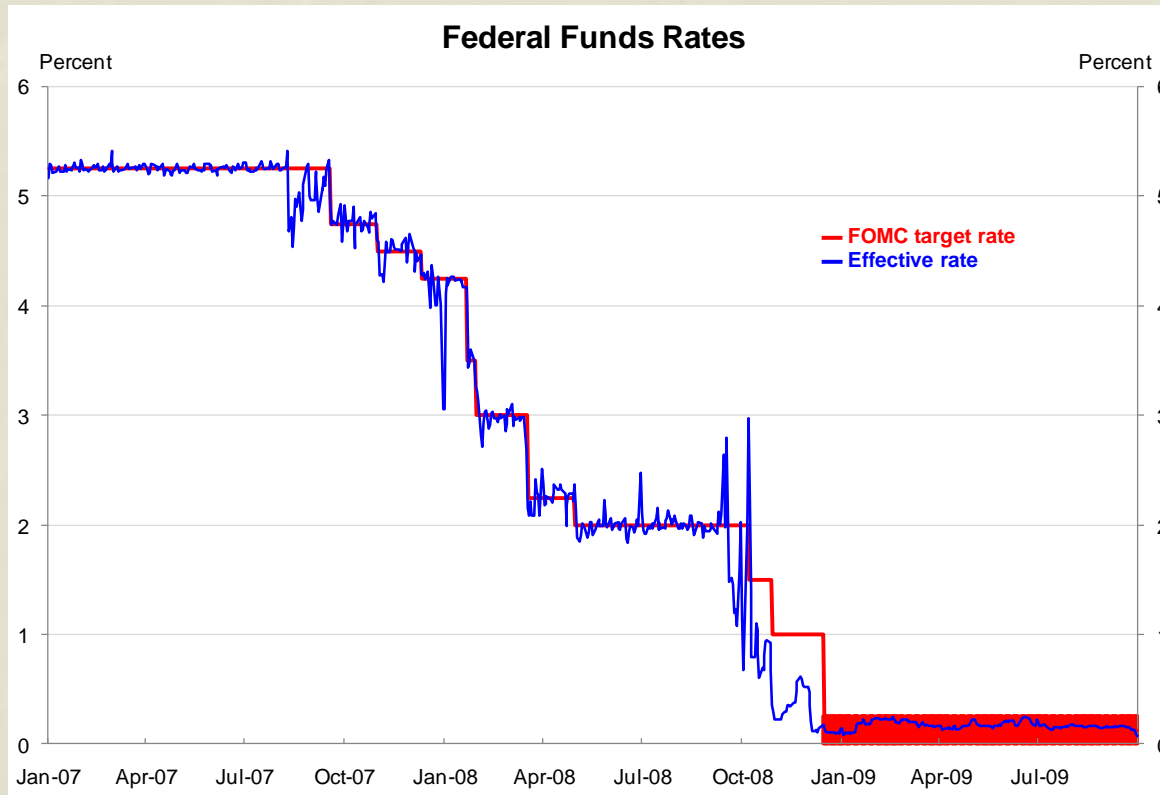
One key factor in recession: Unprecedented housing bust



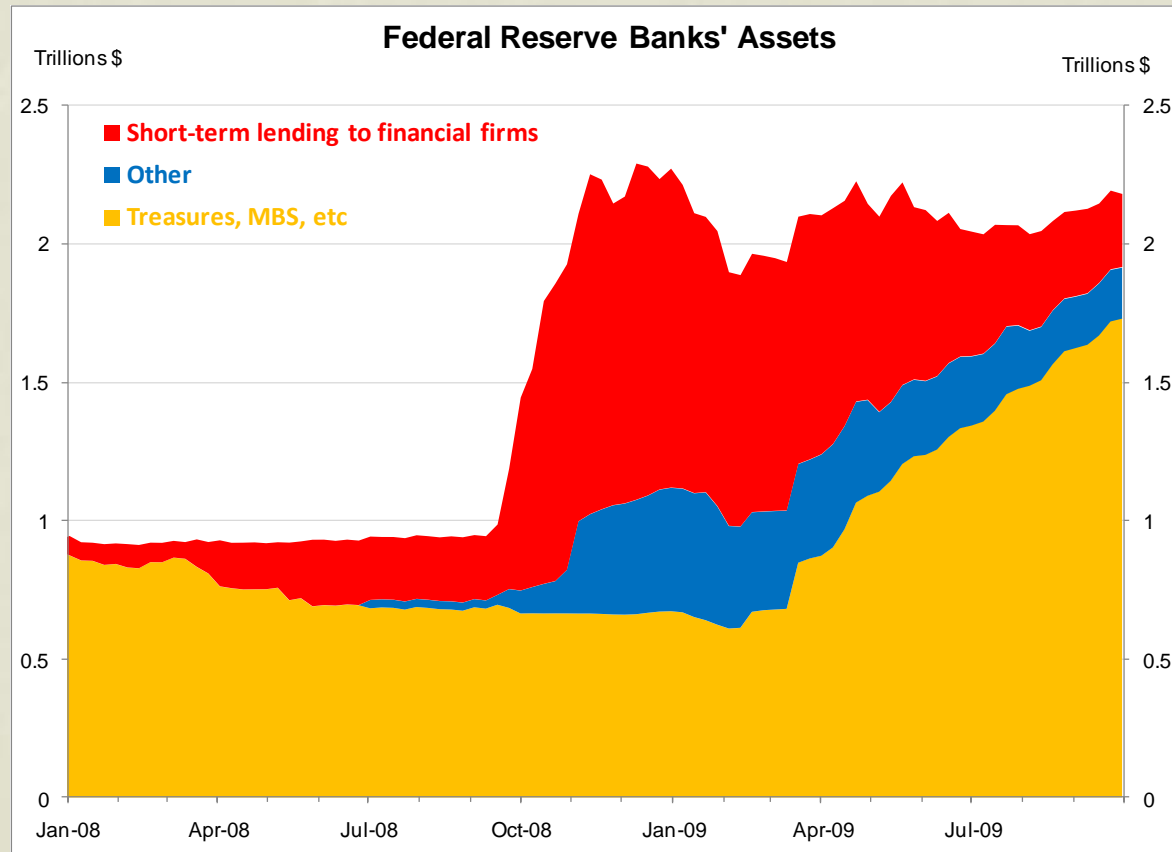
Another key factor in recession: Financial crisis



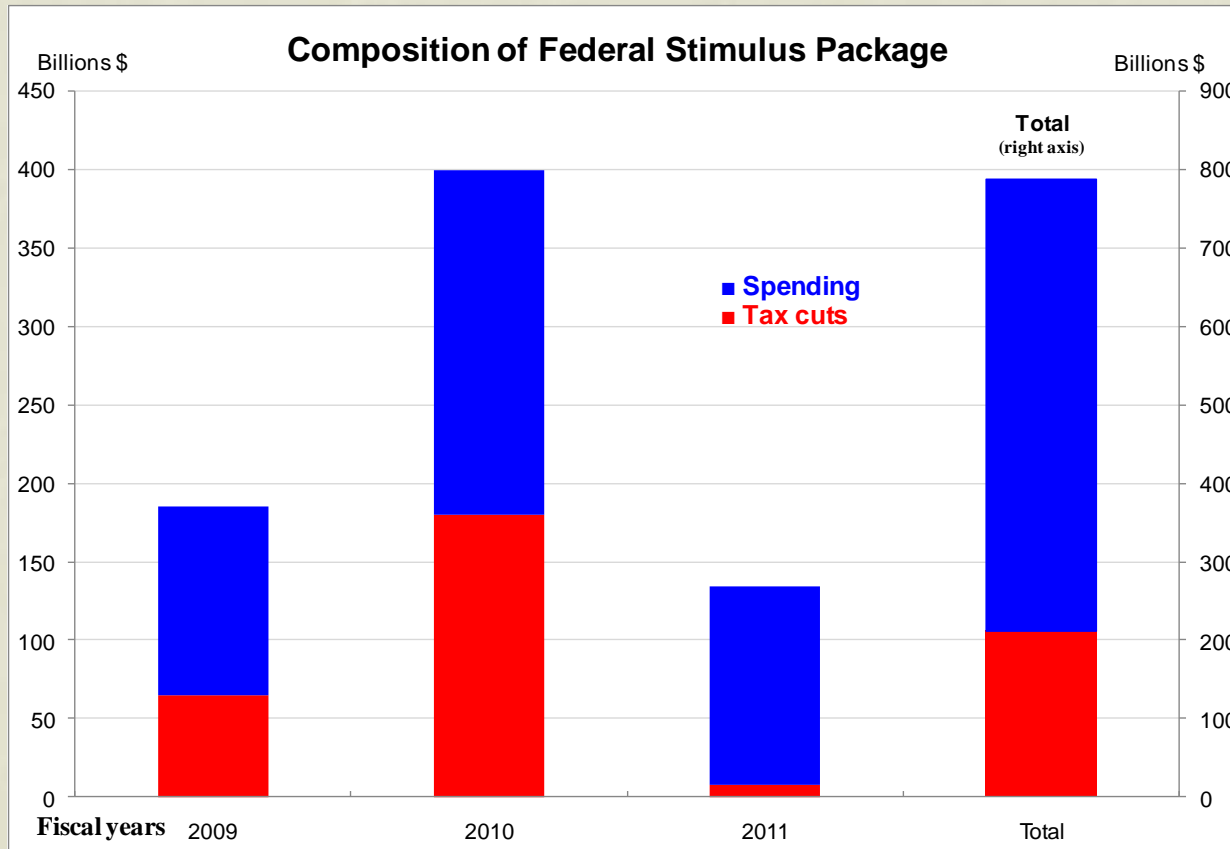
Monetary policy response: Aggressive cuts in fed funds target



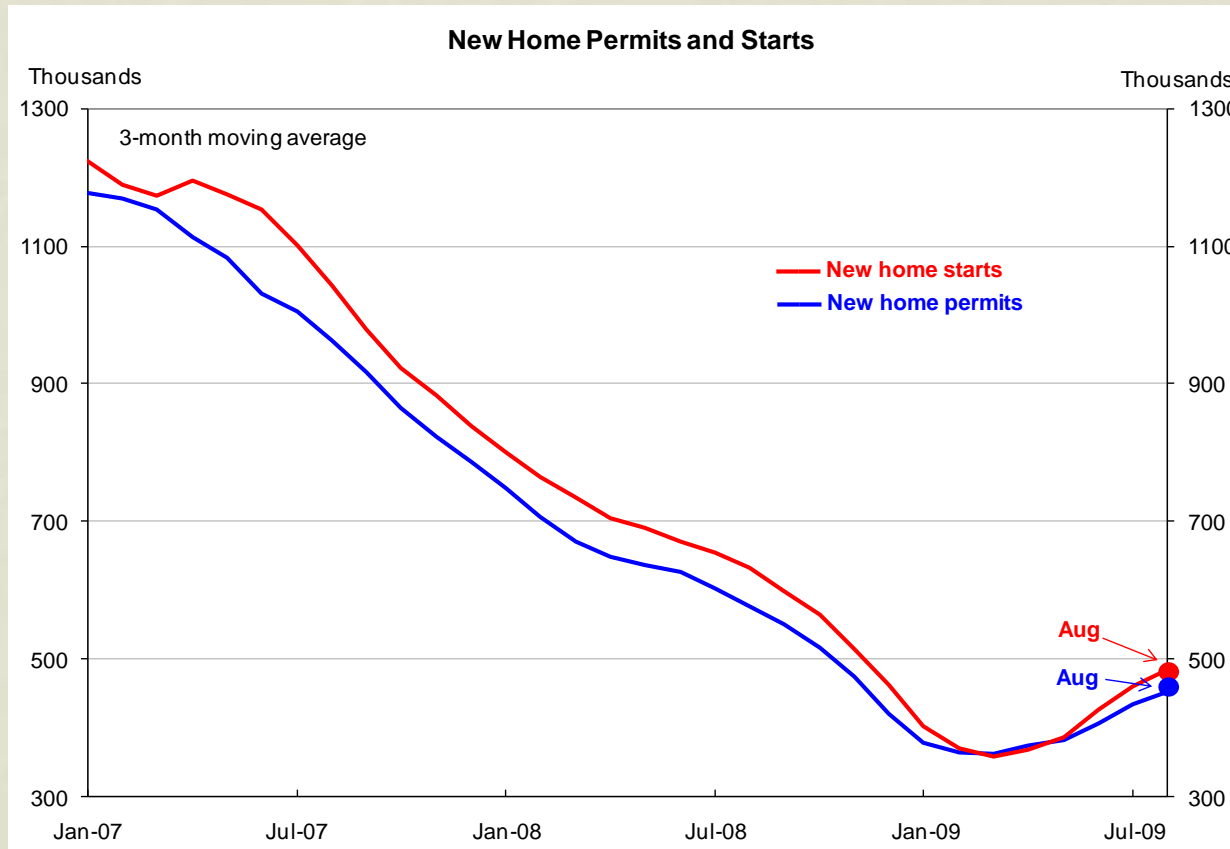
Monetary policy response: Large purchases of long-term assets



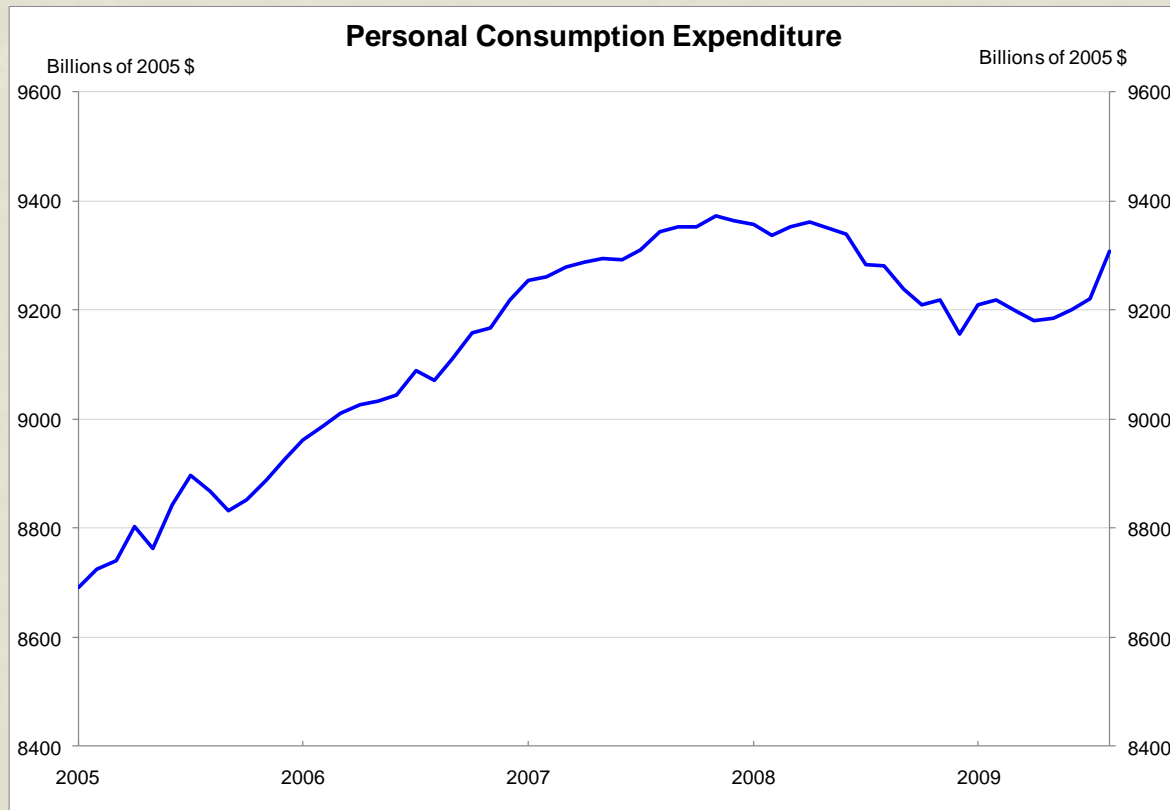
Fiscal policy response: Large stimulus package



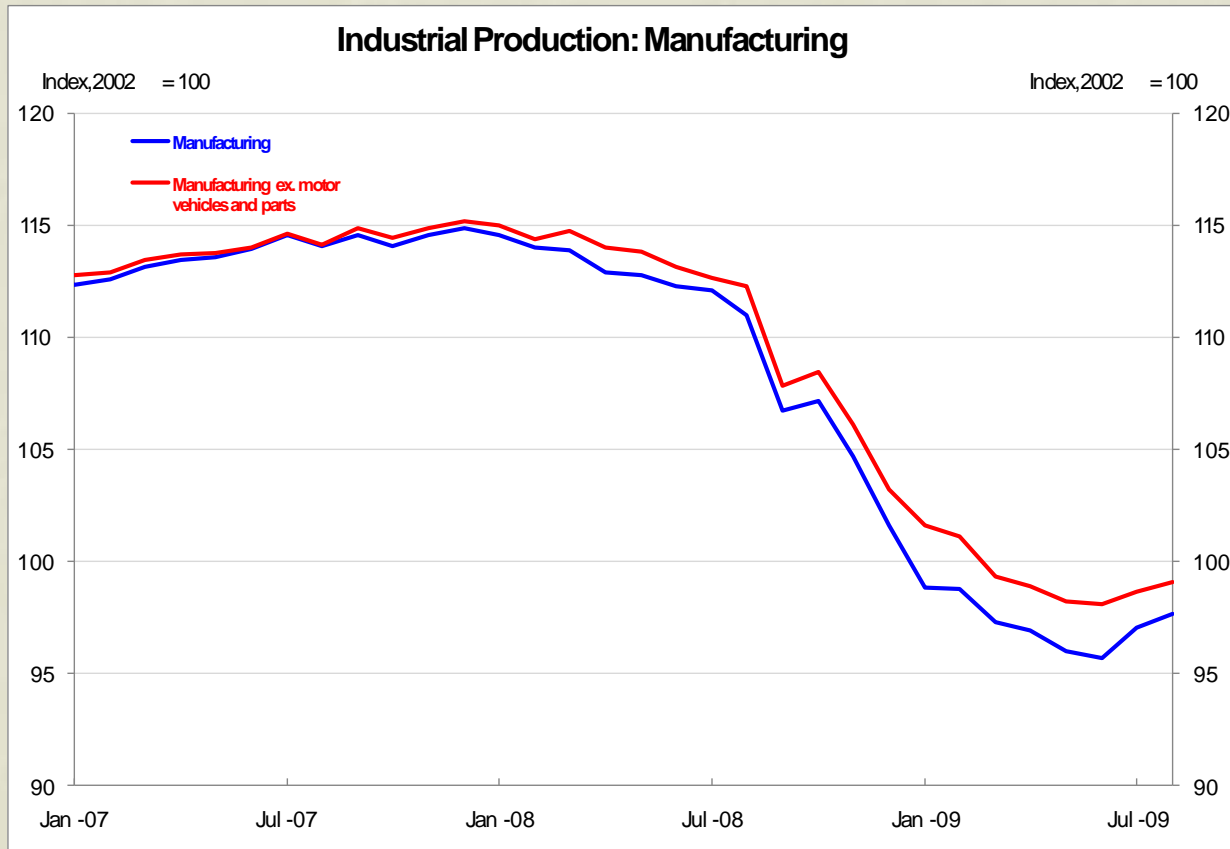
The recession seems to be ending: Housing has improved



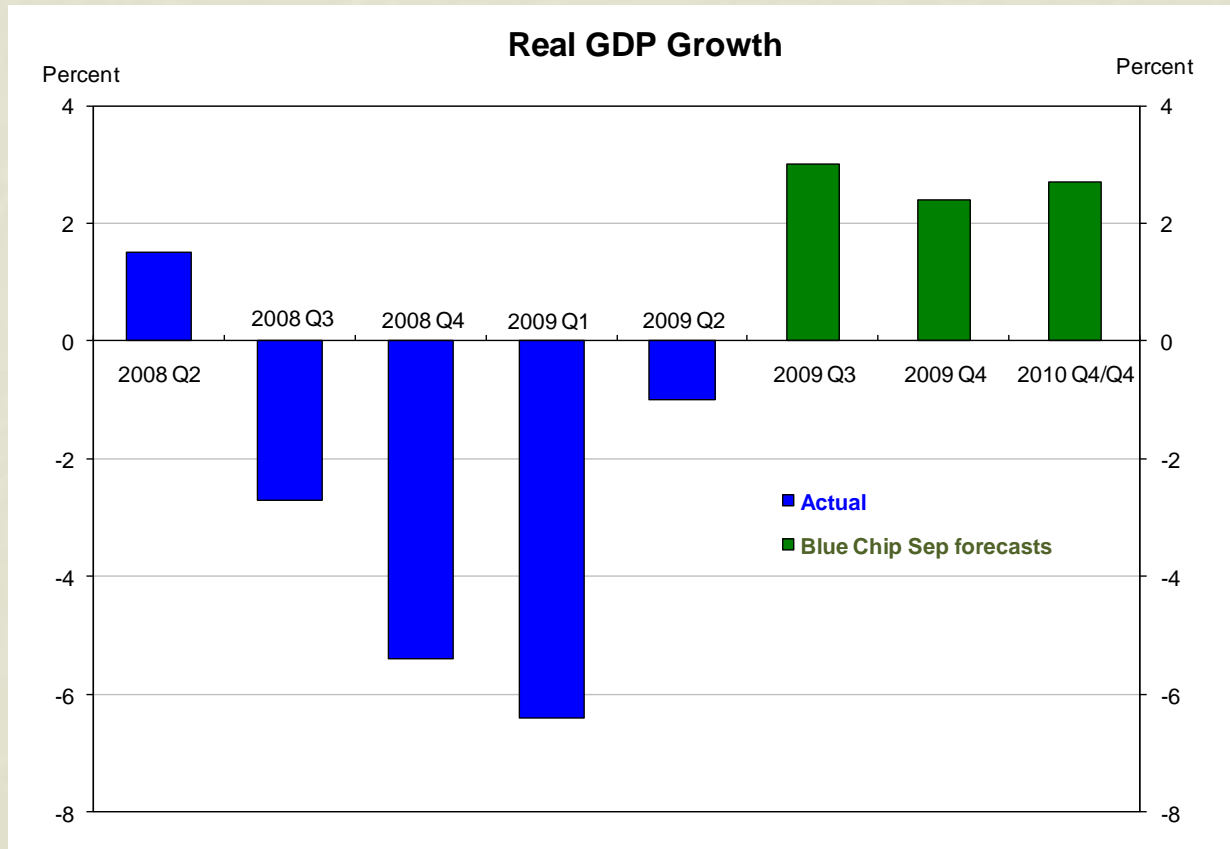
The recession seems to be ending: Consumer spending has improved



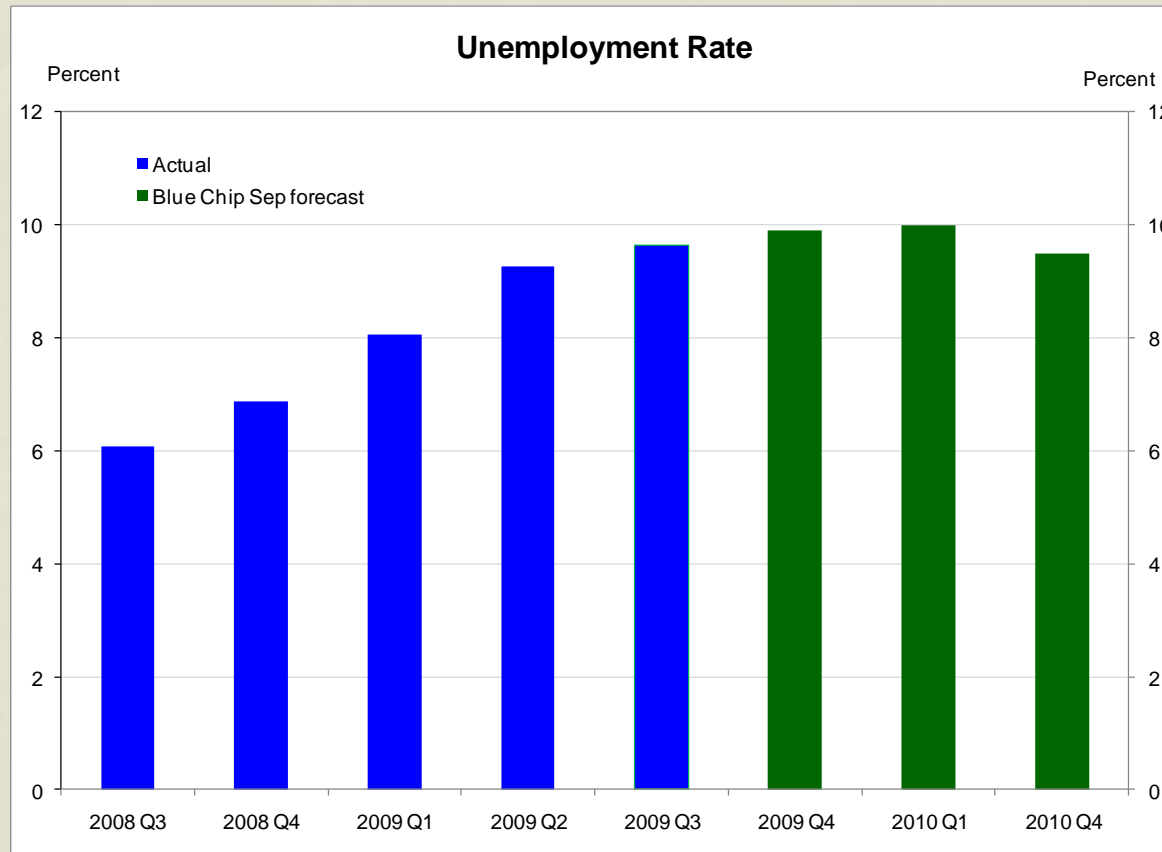
The recession seems to be ending: Manufacturing has picked up



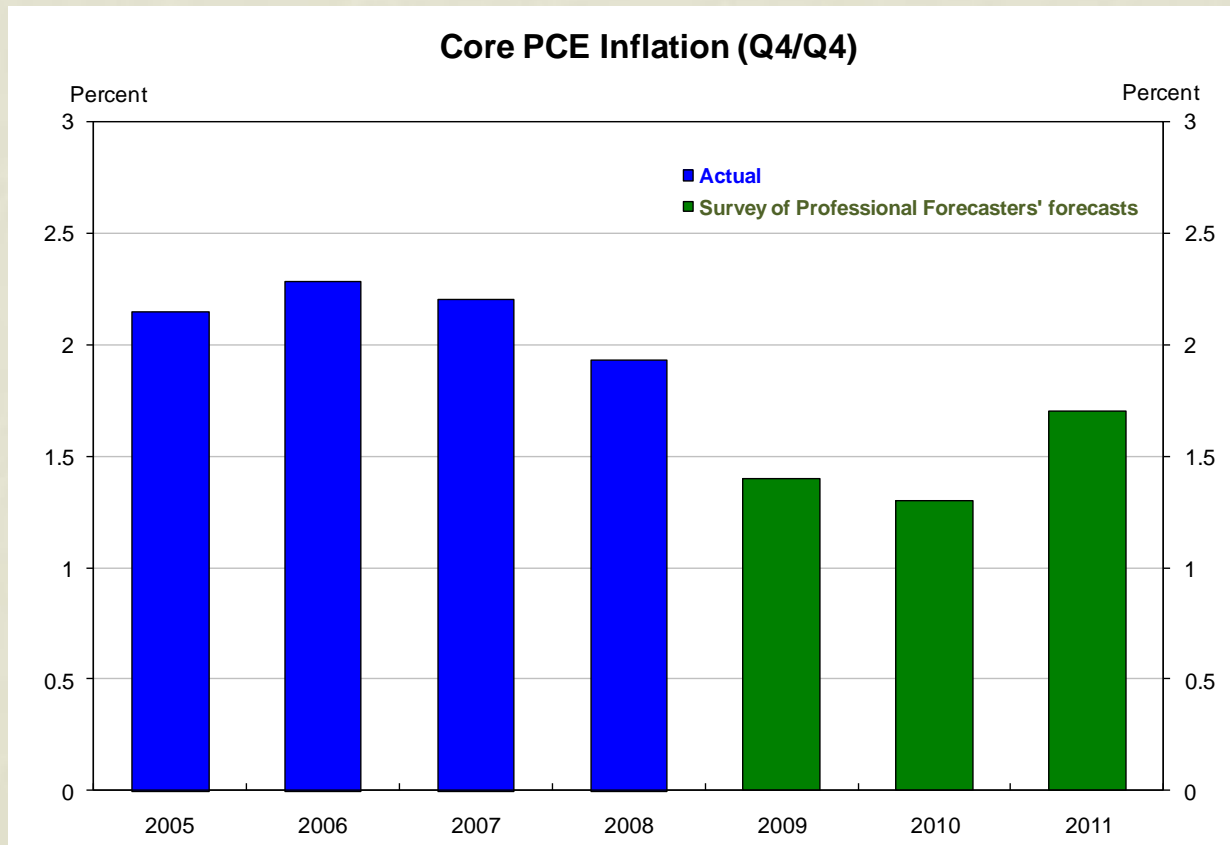
Most forecasters expect recovery to start with 2009:Q3



However, unemployment will likely edge higher before declining



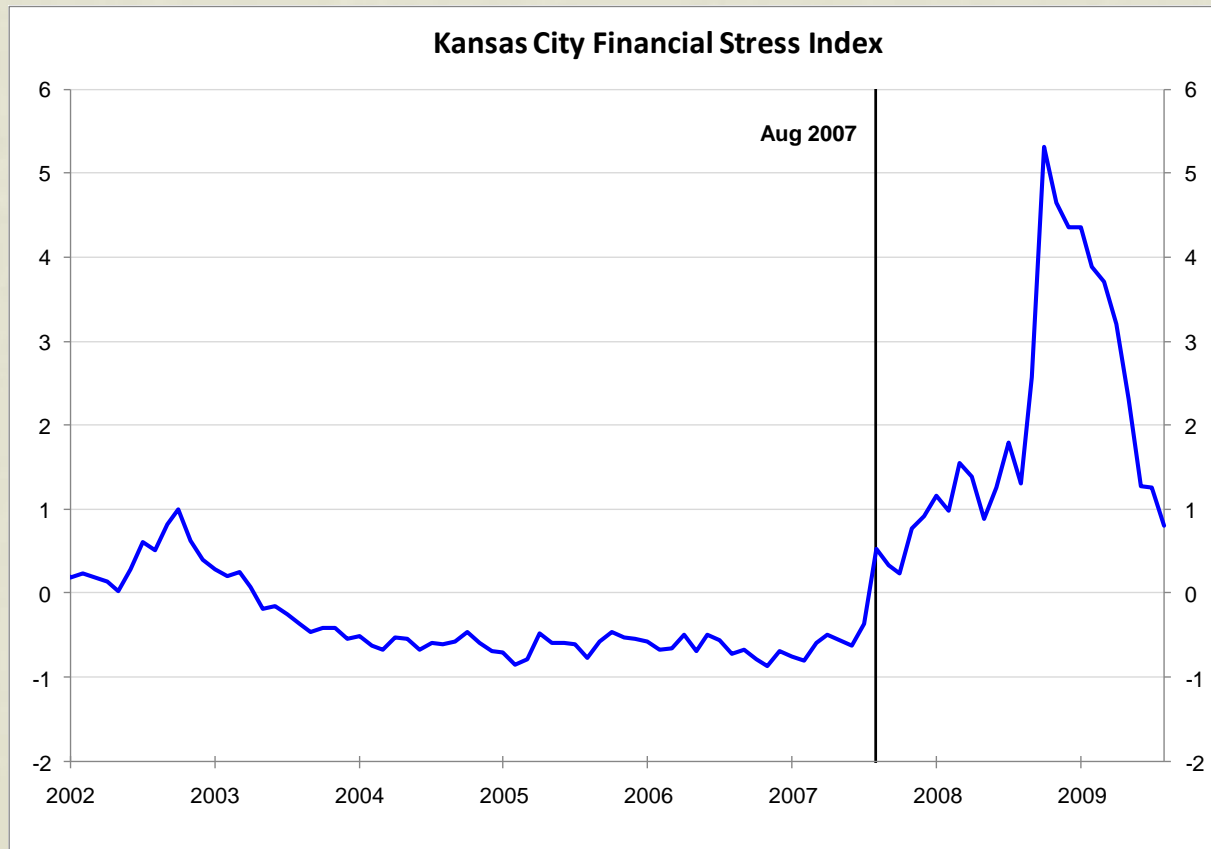
Most forecasters expect core inflation to remain low



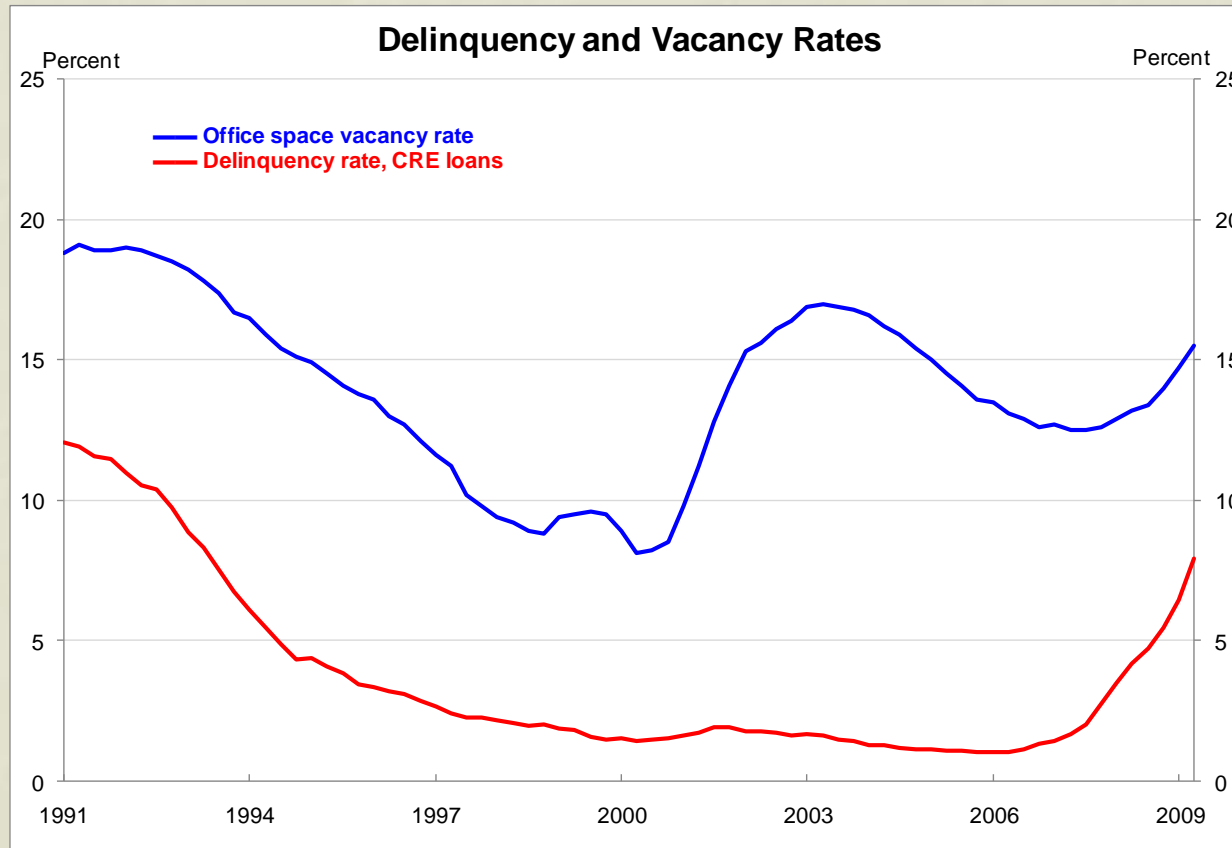
Why not a stronger recovery? International crisis experience



Why not a stronger recovery? Still a way to go in financial market functioning



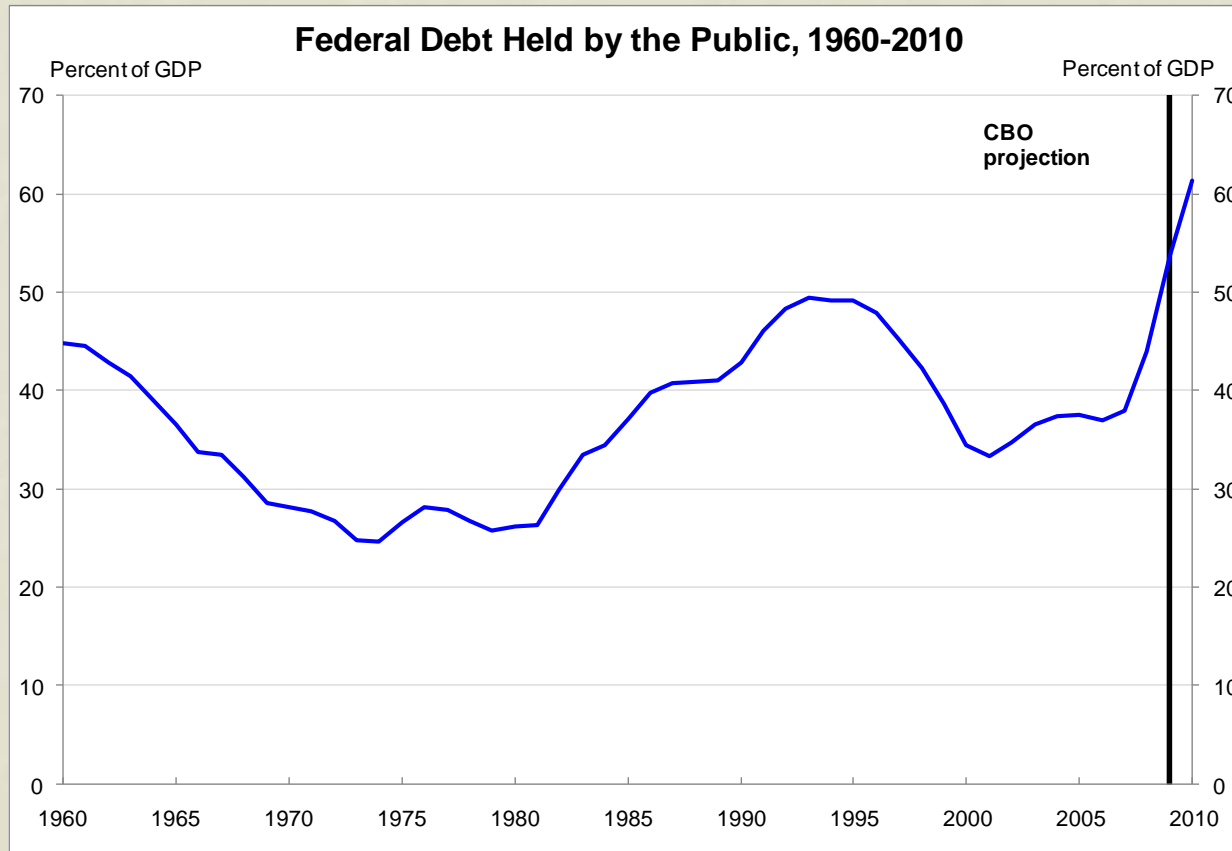
Why not a stronger recovery? Problems in commercial real estate



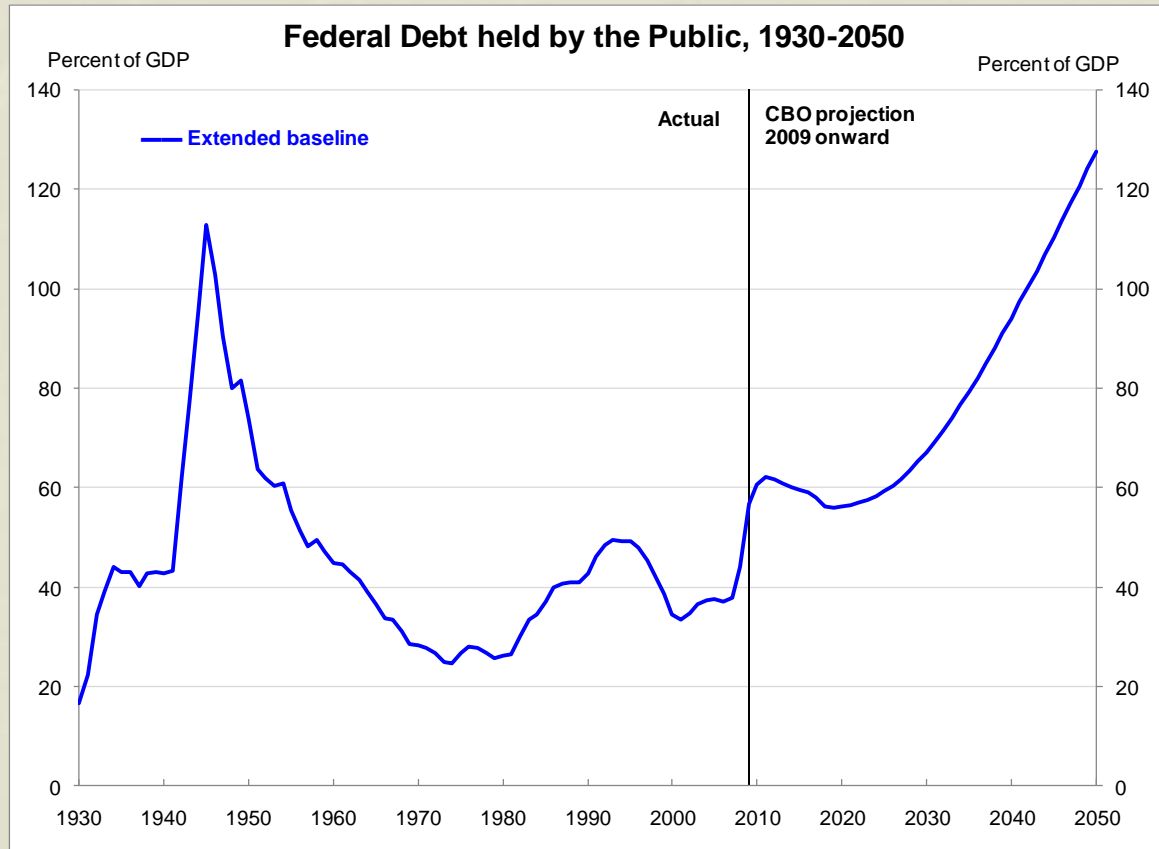
Implications for monetary policy

- Lesson from the 1930's: don't tighten too soon, to avoid choking off recovery
- Lesson from the mid-1970's: don't tighten too slowly, to avoid rising inflation
- Probably begin tightening before financial markets are fully normalized, but not so soon as to jeopardize continued normalization

Fiscal policy: Federal debt has risen significantly



Long-term challenge: Fiscal policy sustainability



Ramifications of growing federal debt

- Potential implications:
 - higher interest rates
 - reduced investment
 - reduced productivity and GDP
- Hard choices:
 - Higher taxes
 - Reduced benefits

Summary

- The sharpest recession of the post-war period is coming to an end.
- Most forecasters expect a gradual recovery and low core inflation through 2010.
- Long term, the sustainability of fiscal policy poses a significant challenge.
 - Social Security and Medicare