On Thin Ice
MARK ZANDI, CHIEF ECONOMIST
The Global Economy Is on Thin Ice
Business cycle status, August 2011

Source: Moody’s Analytics
1

Downgrading the Near-Term Outlook
A Weaker Global Growth Outlook

Real GDP growth

Source: Moody’s Analytics
U.S. Debt Ceiling Drama Undermines Confidence

Consumer sentiment index, 1996Q1=100

Source: University of Michigan
European Debt Crisis Takes a Toll

Economic sentiment index, 1990-2009=100

Source: European Commission
United States:
Serious Fiscal Problems, but Improving Fundamentals
The Debt Ceiling Deal Must Be Completed
Total of $4 tril needed for long-run fiscal sustainability, 2012-2021

- Specified spending cuts ($0.9 tril)
- Supercommittee/trigger ($1.5 tril)
- To be determined ($1.6 tril)

Sources: CBO, Moody’s Analytics
Policymakers Must Ease This Fiscal Headwind

Fiscal Policy contribution to real GDP growth, %

Source: Moody’s Analytics
The Federal Reserve Must Ease Policy Further

Sources: Federal Reserve, Moody’s Analytics
U.S. Businesses Are Very Profitable…

Corporate profits, $ bil

Source: BEA
…And Their Balance Sheets Are Strong

Nonfinancial corporate businesses

The quick ratio is at a record high in the data back to 1950.

Sources: Federal Reserve, Moody’s Analytics
Household Debt Burdens Are Falling Quickly...

At the current rate of deleveraging and interest rates, debt service will be back to early 80’s lows by spring 2012.

Sources: Federal Reserve, BEA, Moody’s Analytics
...Resulting in Much Improved Credit Quality

30-90 day delinquency rate, % of $, SA

Sources: Equifax, Moody’s Analytics
Banks Are Well Capitalized and More Profitable

Commercial banks

Core Capital Ratio (L) vs. Return on Assets (R)

Source: FDIC
Europe: Severe Fiscal Problems, And Shaky Fundamentals
Europe Is Running Out of Fiscal Space…

<table>
<thead>
<tr>
<th>Country</th>
<th>Fiscal Space</th>
<th>Survival 10-year Yield</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Korea</td>
<td>252</td>
<td>15.4%</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>235</td>
<td>9.9%</td>
</tr>
<tr>
<td>Norway</td>
<td>225</td>
<td>10.2%</td>
</tr>
<tr>
<td>Australia</td>
<td>223</td>
<td>11.1%</td>
</tr>
<tr>
<td>Singapore</td>
<td>222</td>
<td>9.0%</td>
</tr>
<tr>
<td>Sweden</td>
<td>209</td>
<td>8.1%</td>
</tr>
<tr>
<td>Finland</td>
<td>181</td>
<td>8.1%</td>
</tr>
<tr>
<td>United States</td>
<td>153</td>
<td>7.8%</td>
</tr>
<tr>
<td>Canada</td>
<td>151</td>
<td>8.5%</td>
</tr>
<tr>
<td>Germany</td>
<td>149</td>
<td>6.6%</td>
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<tr>
<td>Austria</td>
<td>141</td>
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<tr>
<td>Great Britain</td>
<td>142</td>
<td>7.9%</td>
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<tr>
<td>France</td>
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<td>5.9%</td>
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<tr>
<td>Belgium</td>
<td>134</td>
<td>7.4%</td>
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<tr>
<td>Spain</td>
<td>125</td>
<td>6.4%</td>
</tr>
<tr>
<td>Greece</td>
<td>No Space</td>
<td>2.8%</td>
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<tr>
<td>Ireland</td>
<td>No Space</td>
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<tr>
<td>Italy</td>
<td>No Space</td>
<td>4.9%</td>
</tr>
<tr>
<td>Japan</td>
<td>No Space</td>
<td>Negative</td>
</tr>
<tr>
<td>Portugal</td>
<td>No Space</td>
<td>4.1%</td>
</tr>
</tbody>
</table>

Note: Fiscal space is the difference between actual debt-to-GDP ratio and debt-to-GDP ratio that results in default

Source: Moody's Analytics
...And Global Investors Are Losing Faith

Interest payments become overwhelming above 6% yields.

Sources: Bloomberg, Moody’s Analytics
Stress Mounts in Europe’s Banking System...

CDS spreads

Source: Bloomberg
...Given Their Exposure to Troubled Countries...

Banking system exposure to public & private debt, % of GDP, 2011Q1

Sources: IMF, BIS, Moody’s Analytics
...Threatening the Flow of Credit

Size of capital markets as of 2010, % of GDP

Sources: IMF, BIS, Moody’s Analytics
Policymakers Must Obey the Fiscal Speed Limit...

Change in cyclically adjusted primary balance, ppt

Source: Moody’s Analytics
...And the ECB Must Be Aggressive

ECB government bond holdings, € bil

Source: ECB
Risk of a Lost European Decade

Euro zone real GDP, 2000 € bil

Sources: Eurostat, Moody’s Analytics