

MANKOFF

The U.S. Economy In Crisis:

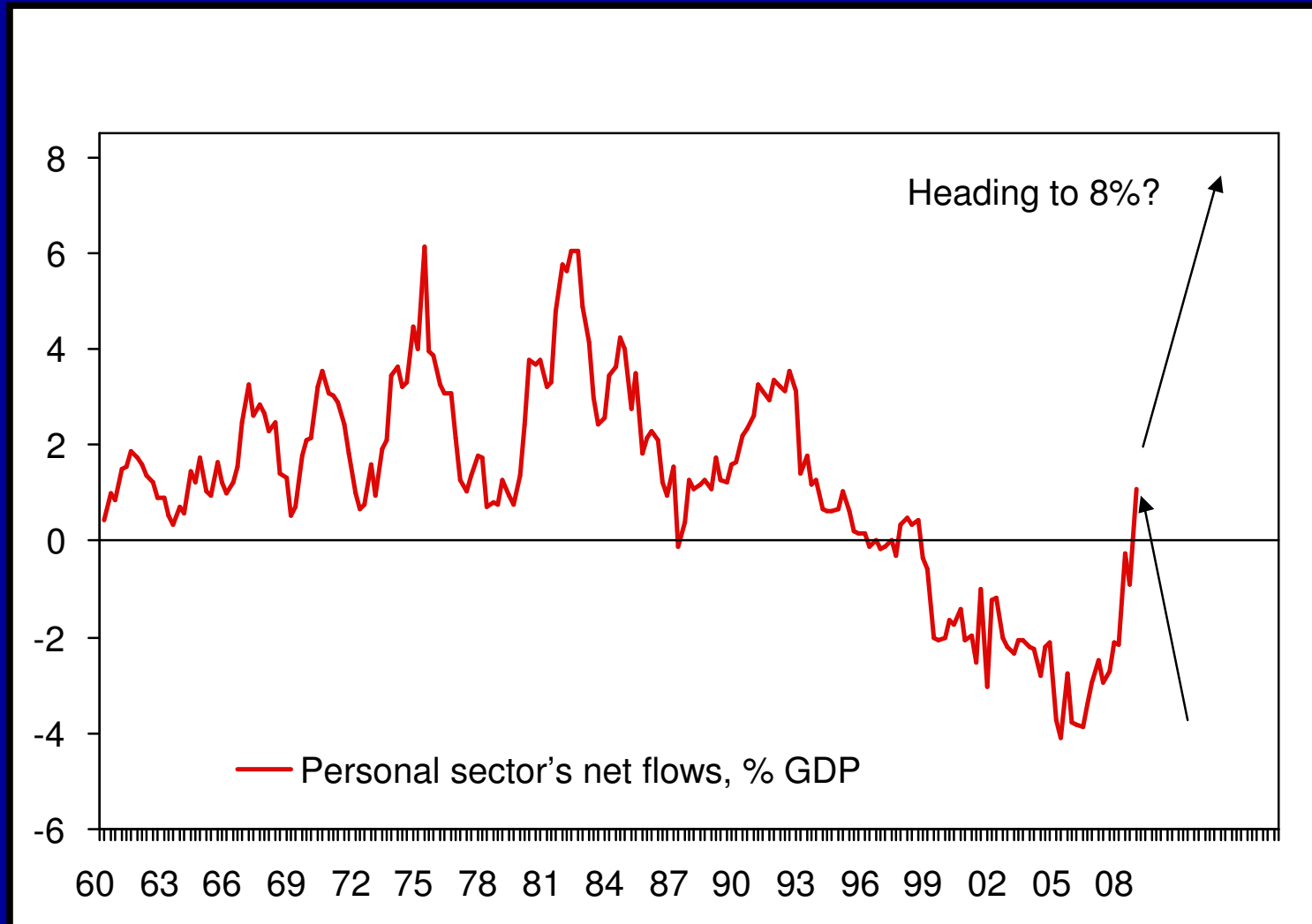
When Will It End?

Ian C. Shepherdson

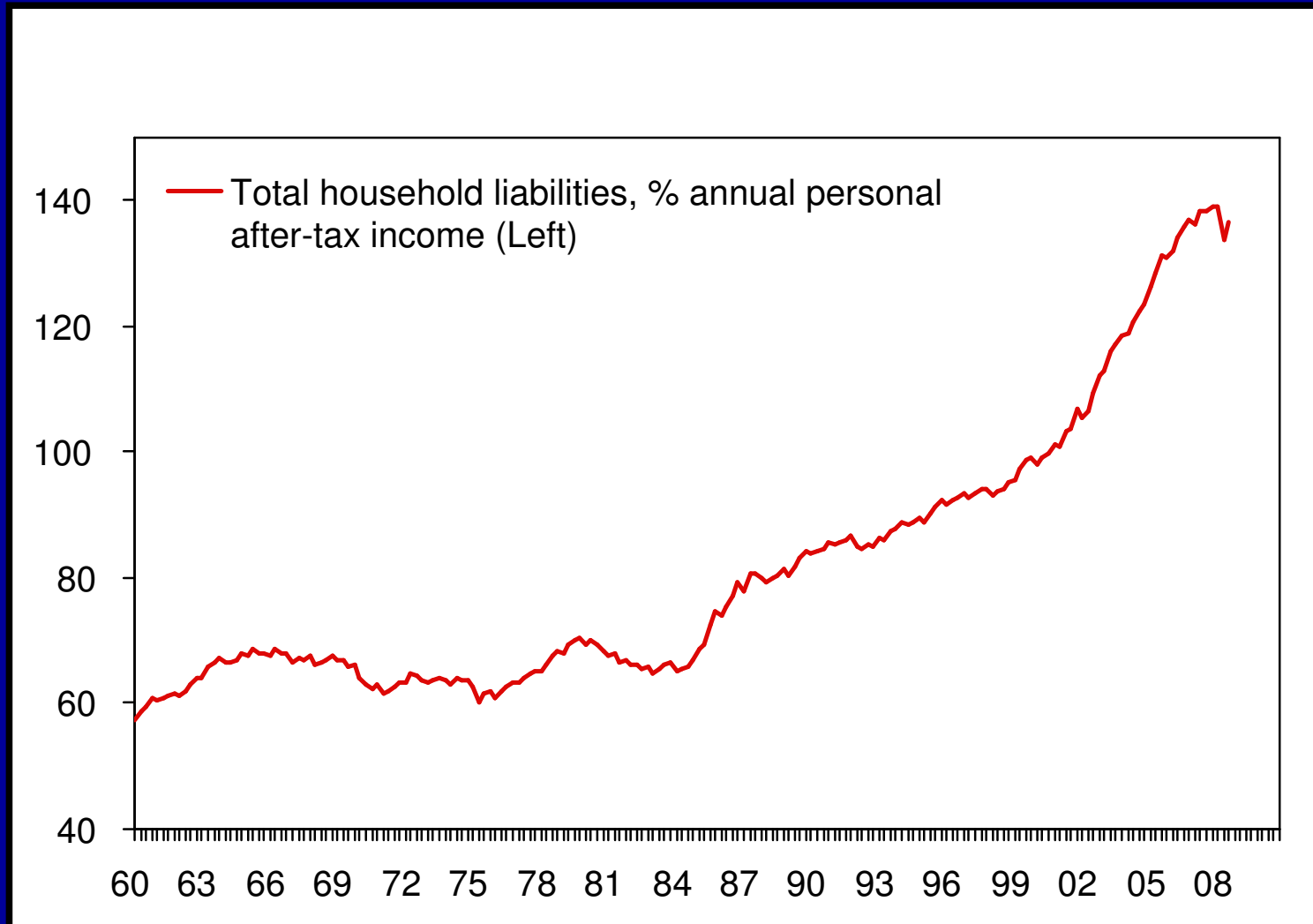
Chief U.S. Economist, High Frequency Economics

High Frequency Economics[®]
Daily Data Analysis and Assessment of the Global Economy

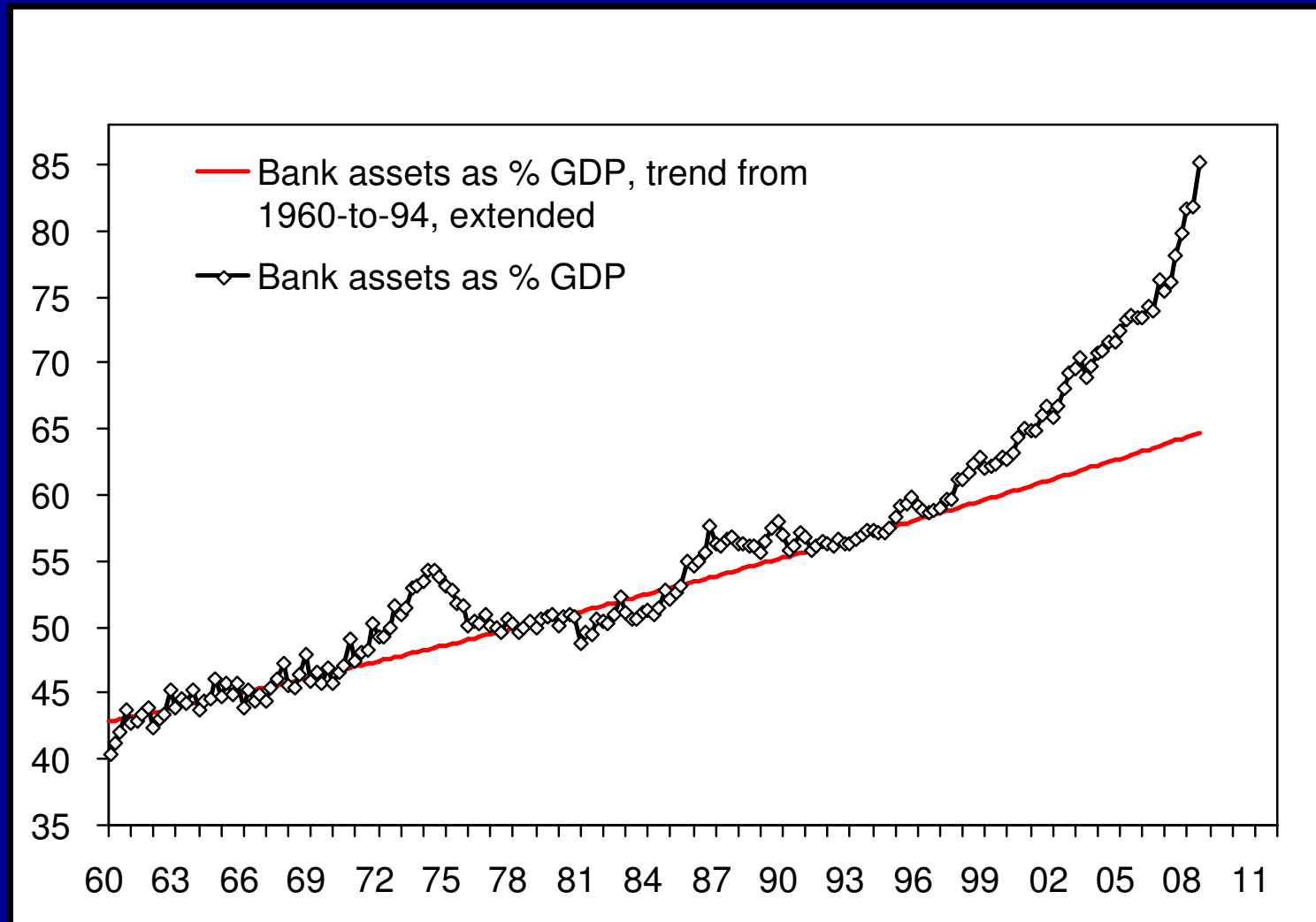
Retrenchment Underway... Long Way To Go



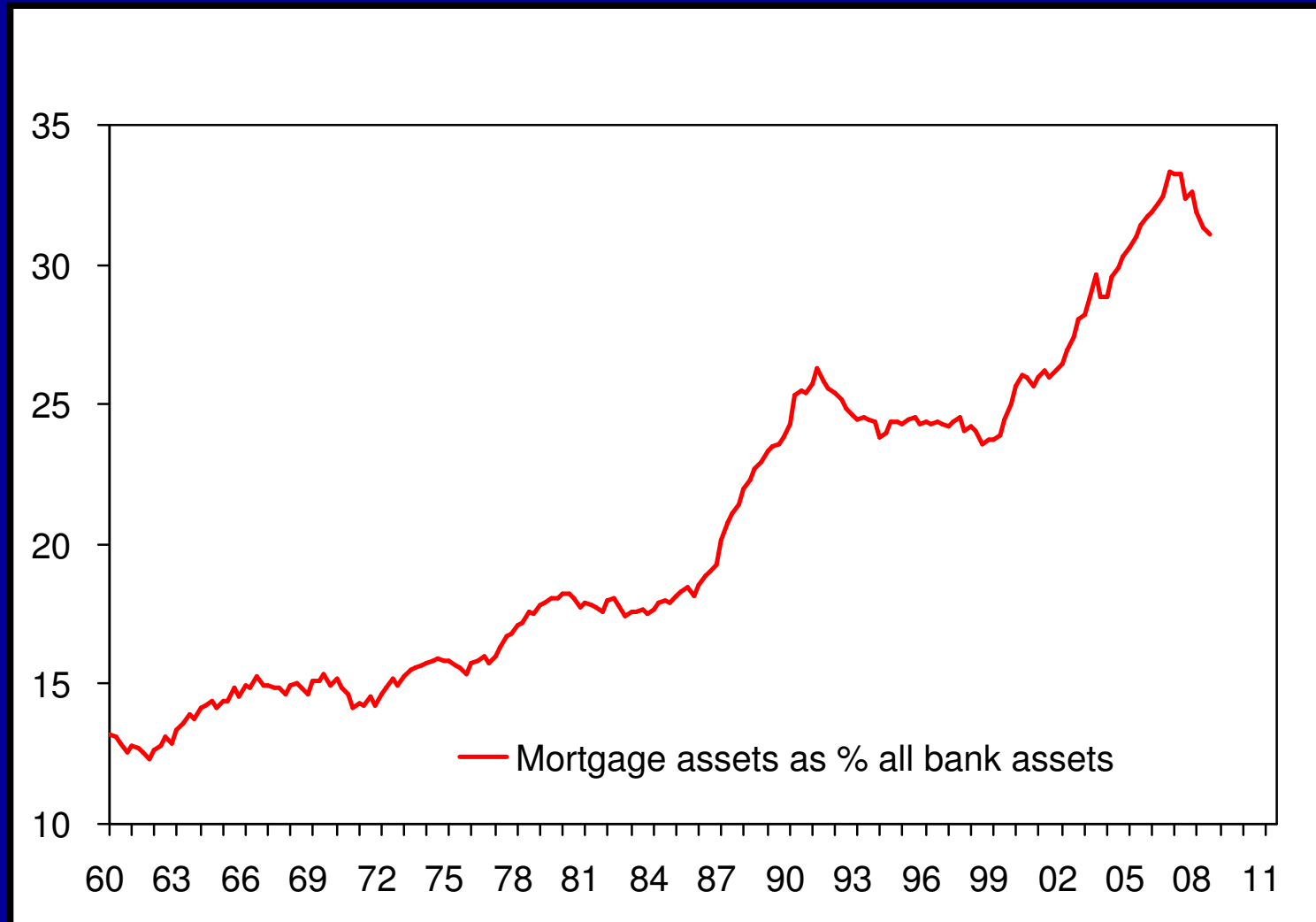
Balance Sheet Correction Has Barely Begun



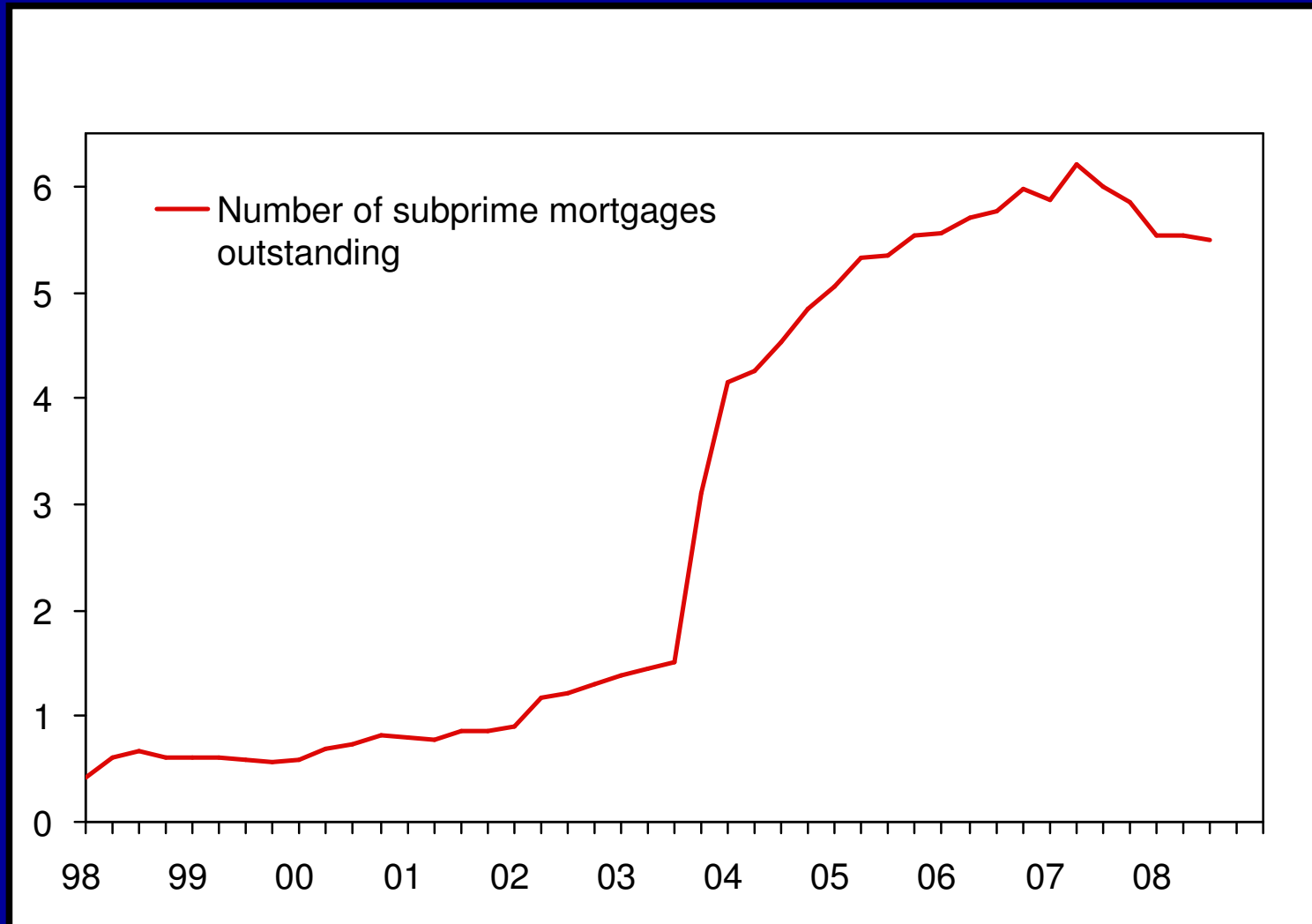
As Consumers Borrowed, Bank Assets Soared



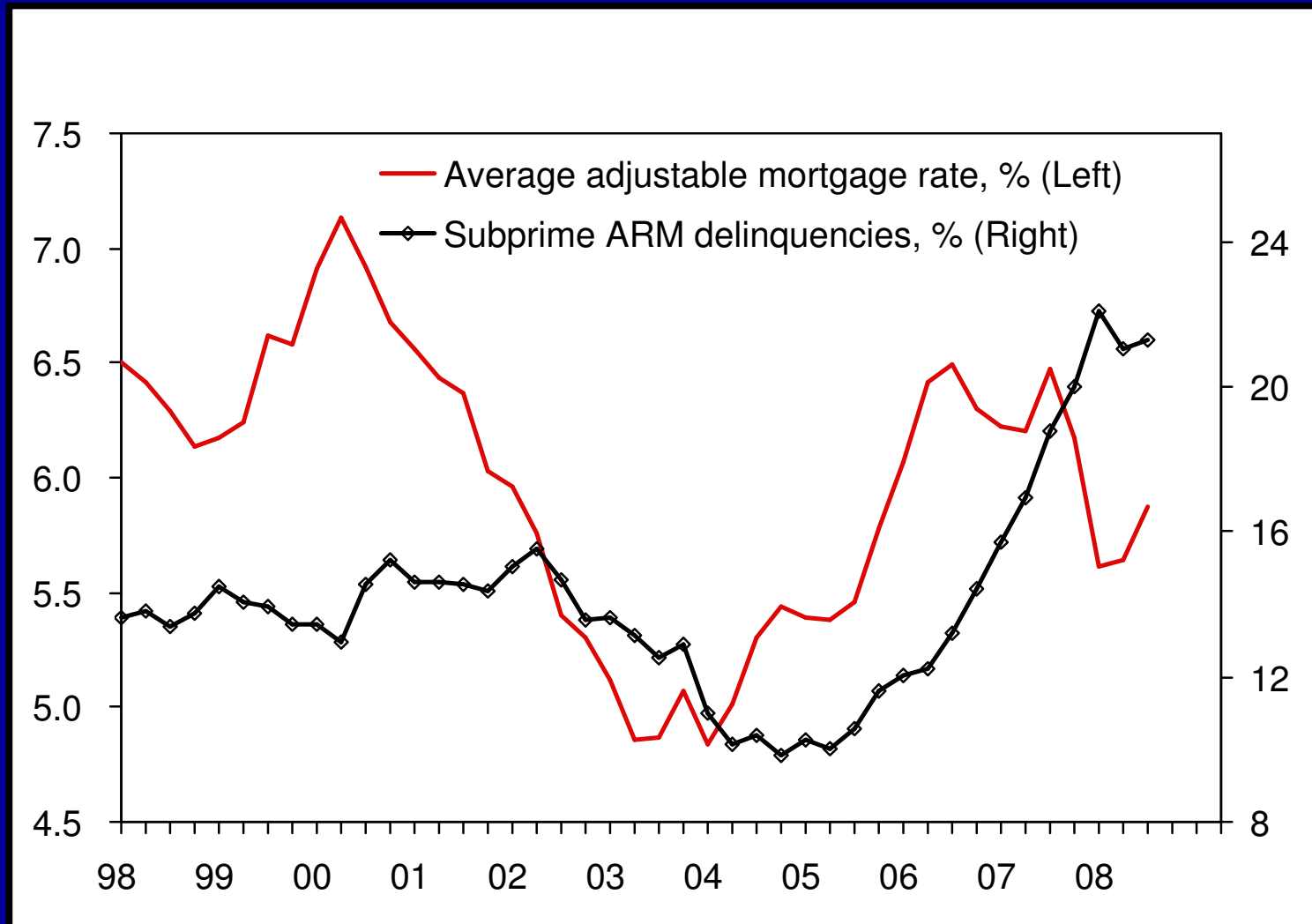
...Asset Growth Was Focussed In Mortgages



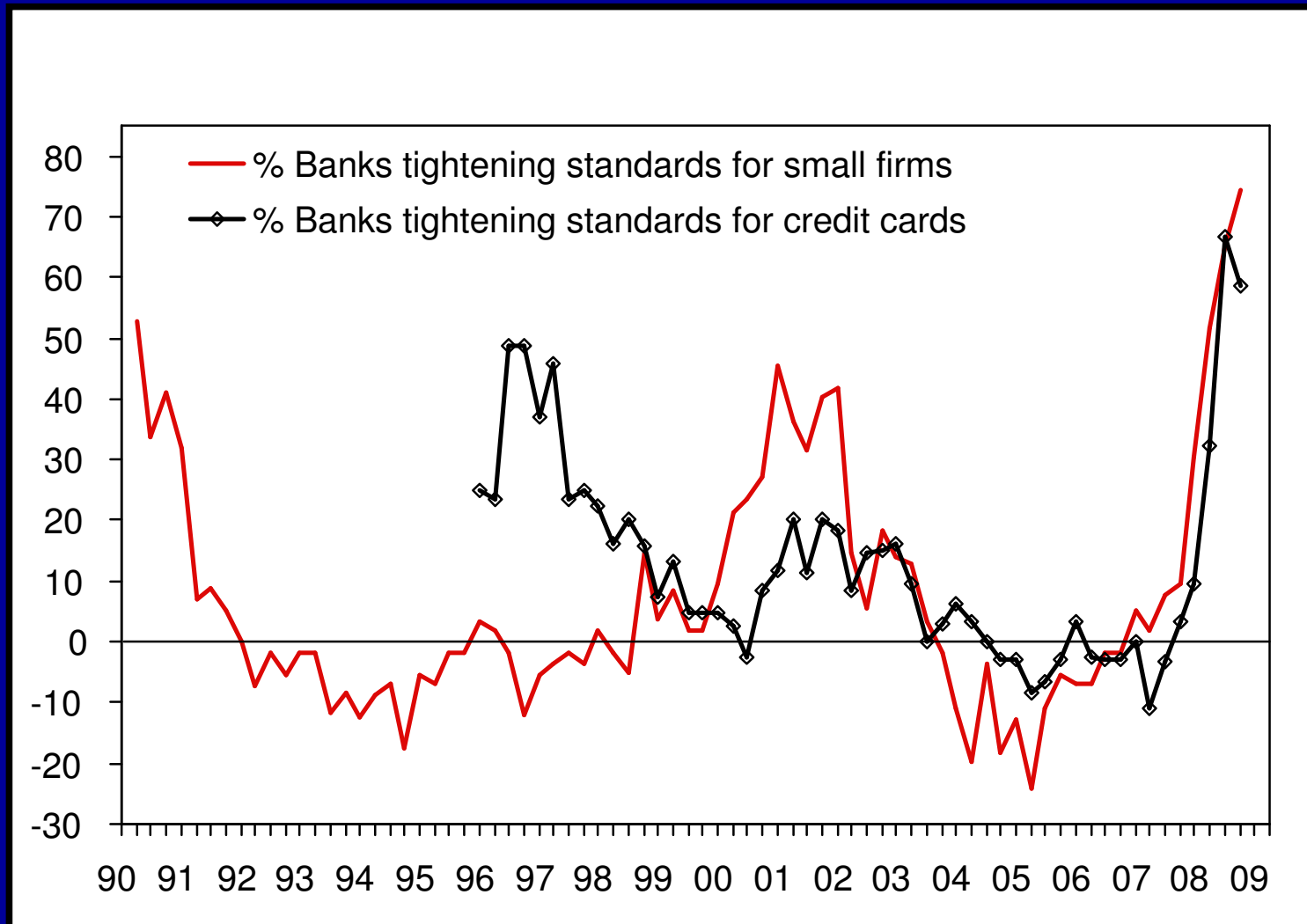
...Especially, Subprime Mortgages



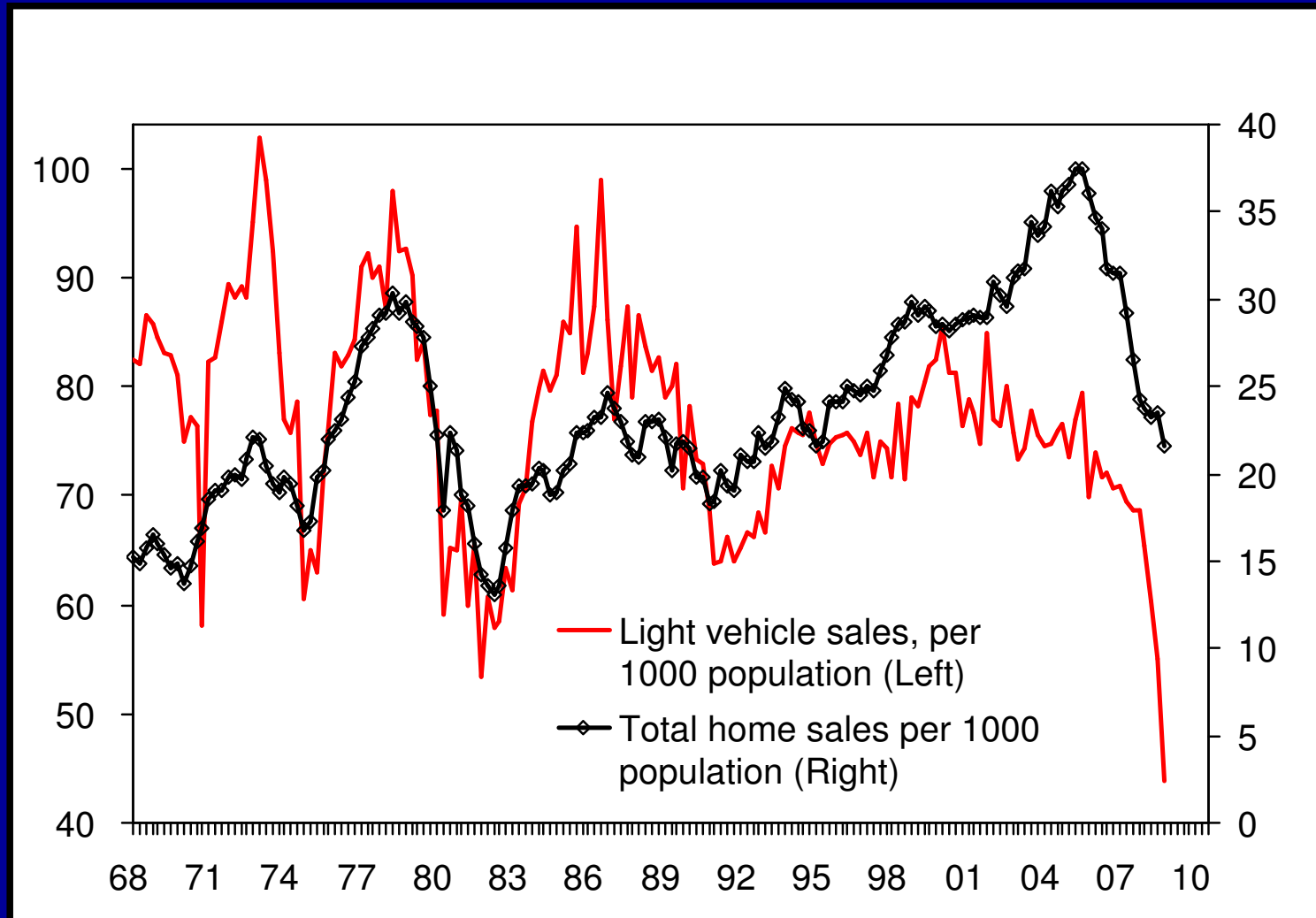
...So 17 Rate Hikes Were Disastrous



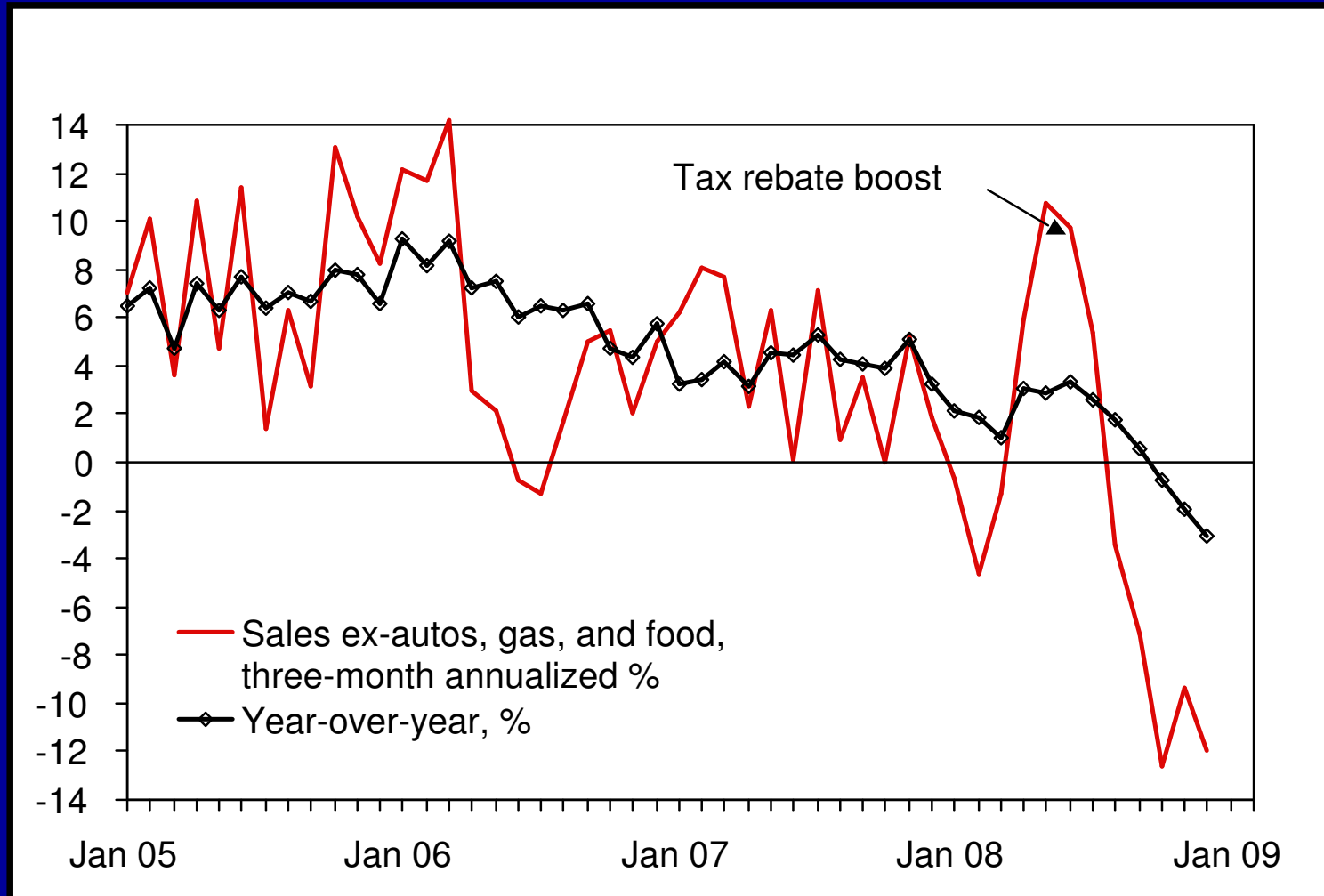
Result: Dramatic Credit Tightening



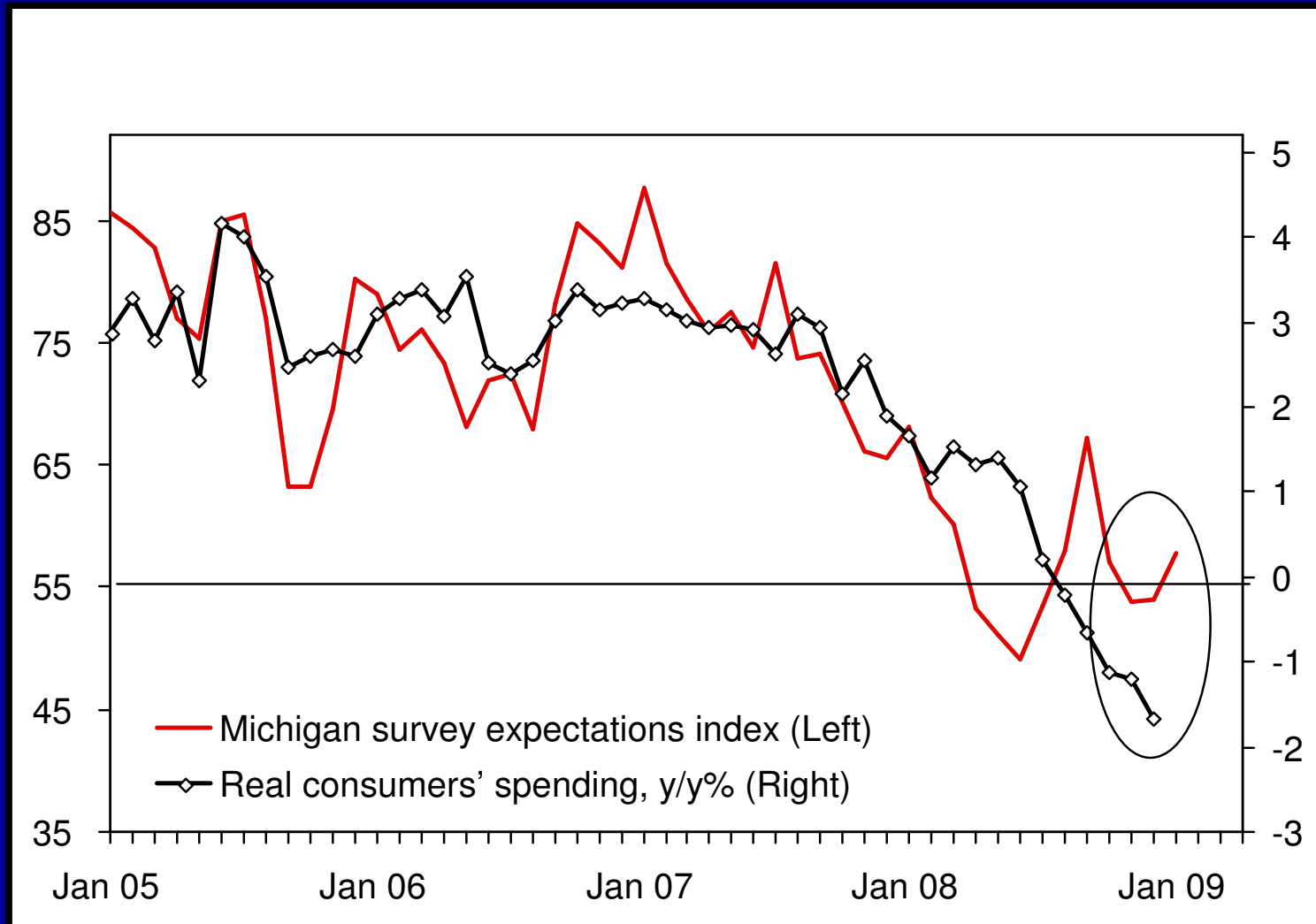
Initial Housing Shock Has Spread



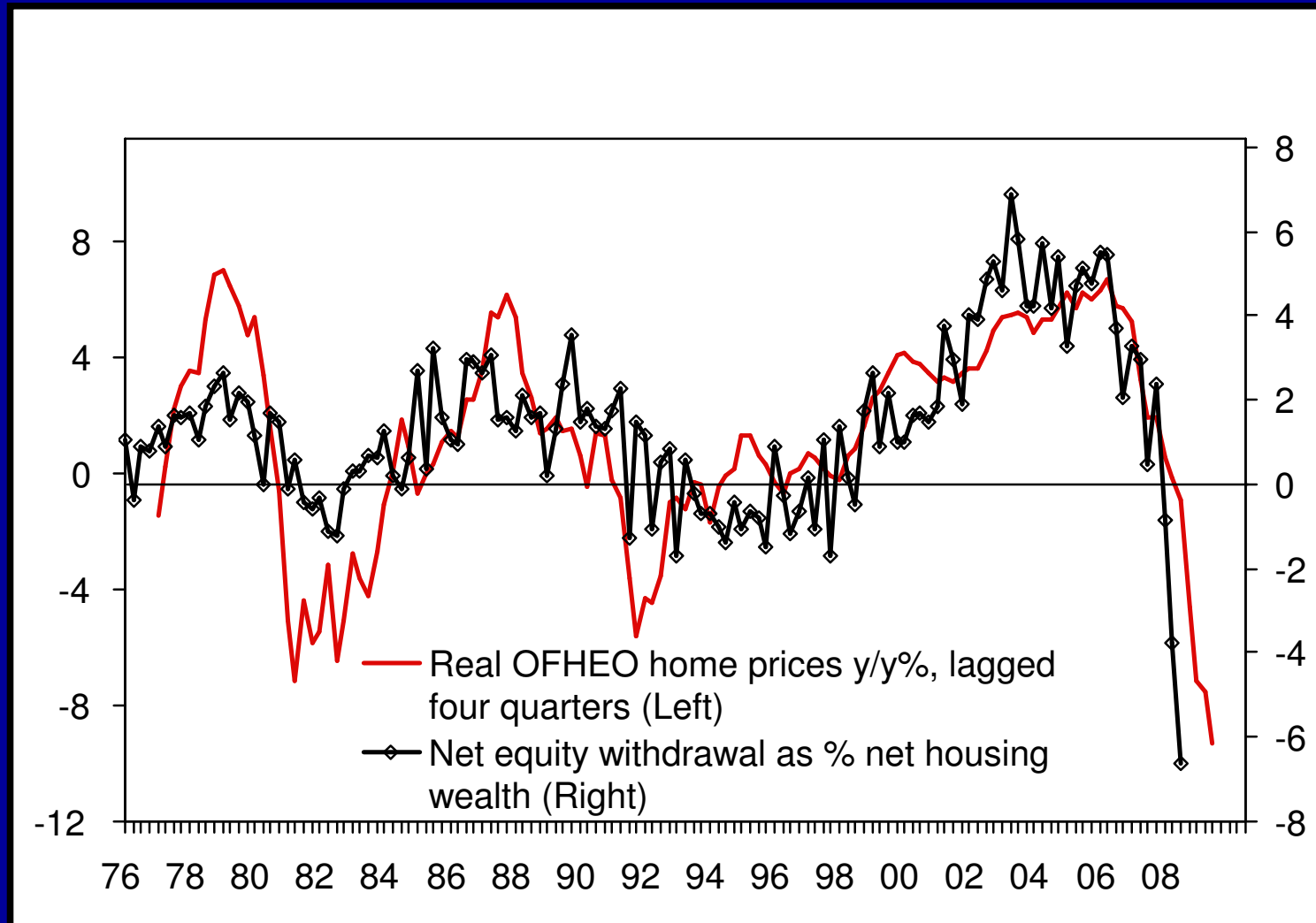
Now, Other Spending Is Dropping Too



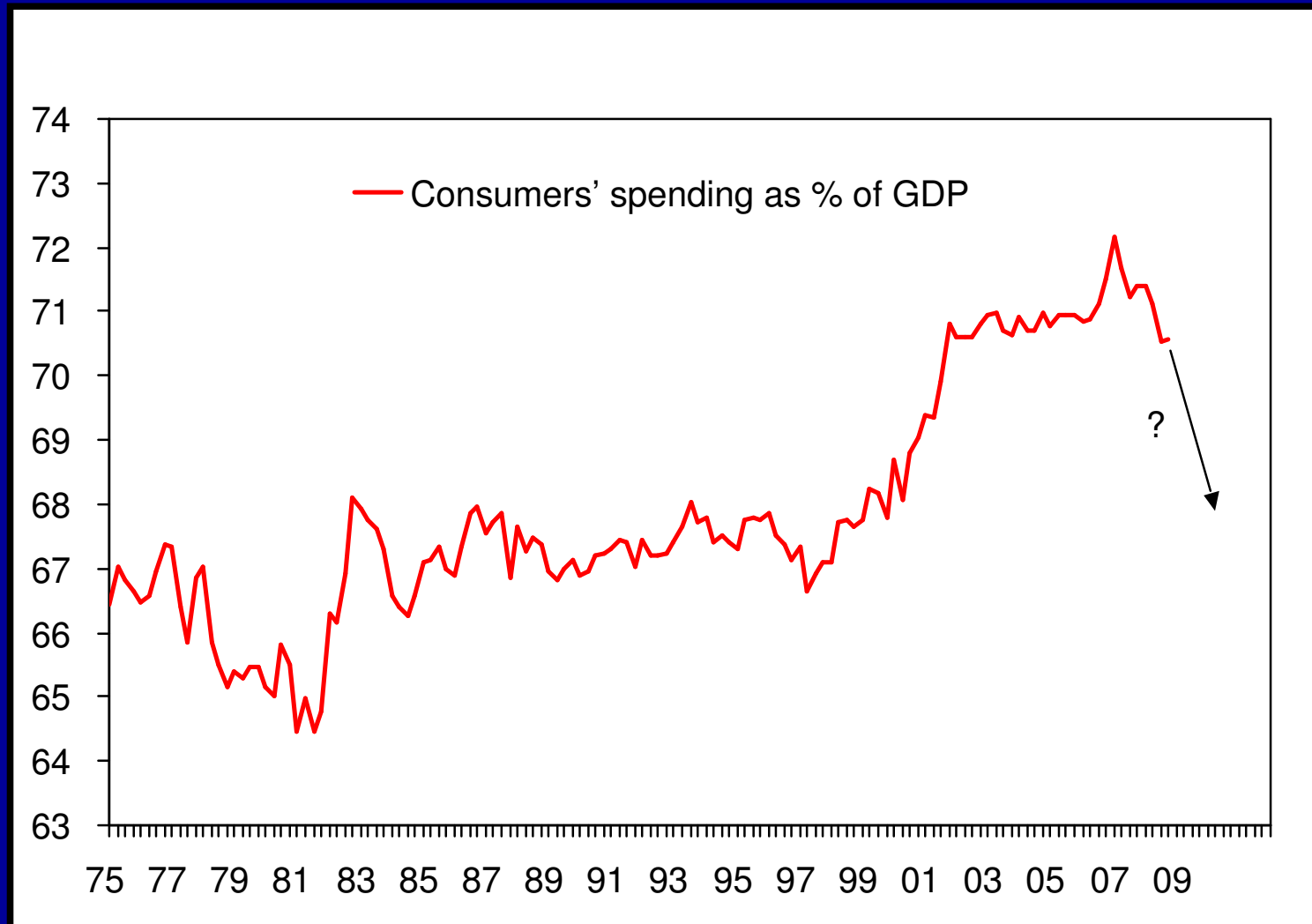
Stock Shock Limiting Impact Of Gas Prices



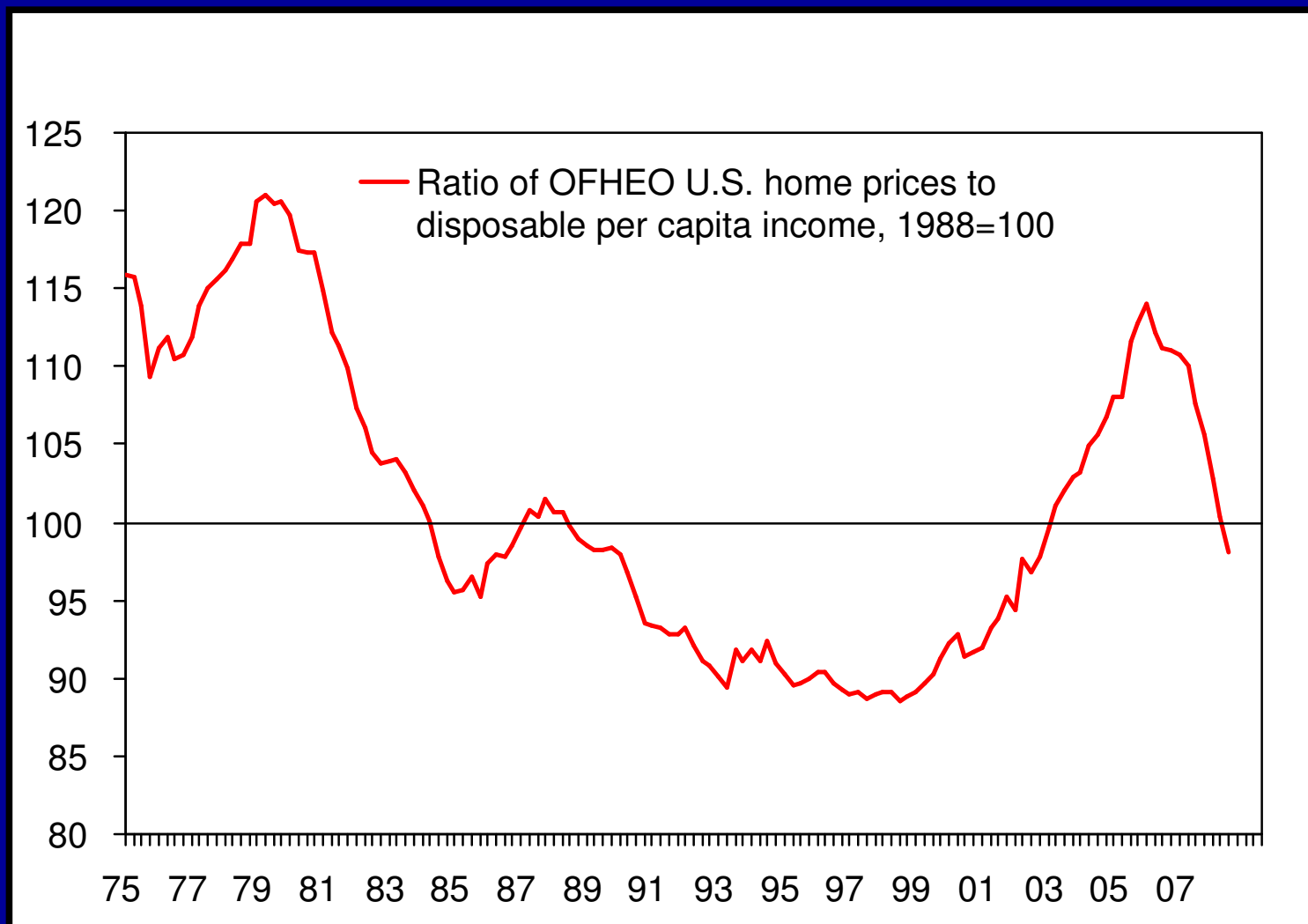
But Falling Home Prices Are The Killer



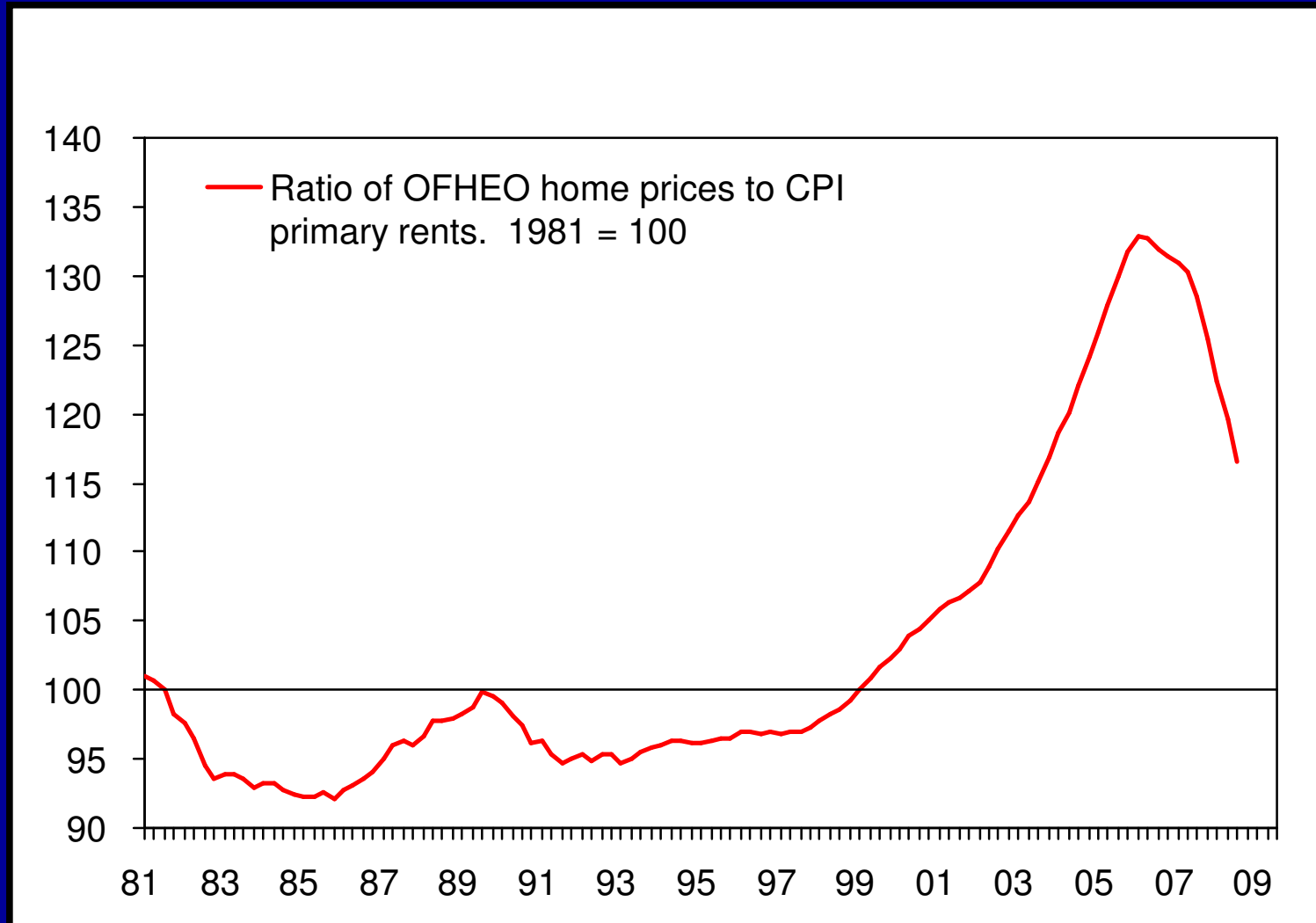
Consumption's GDP Share Has To Shrink



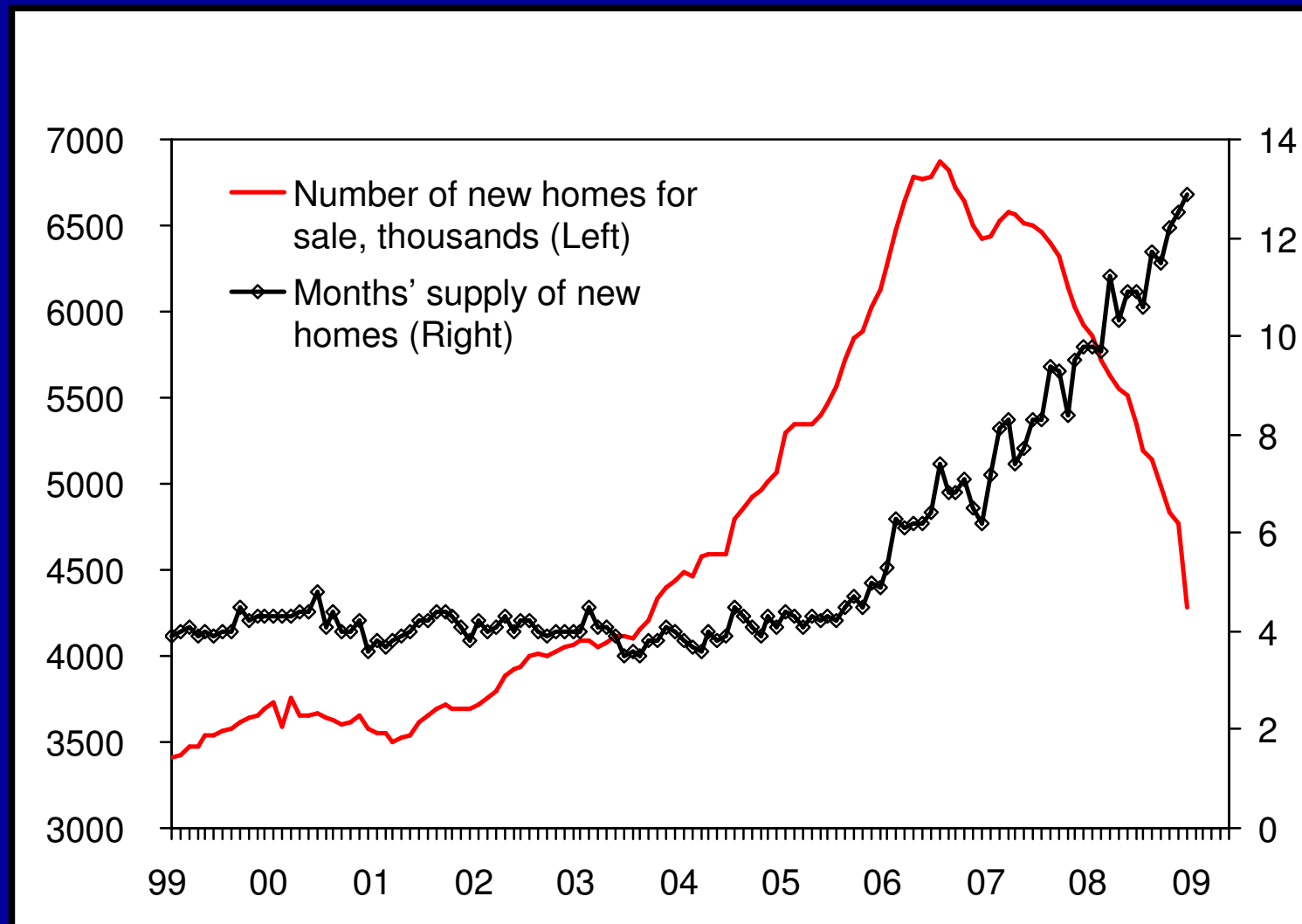
Home Prices Have To Fall Further



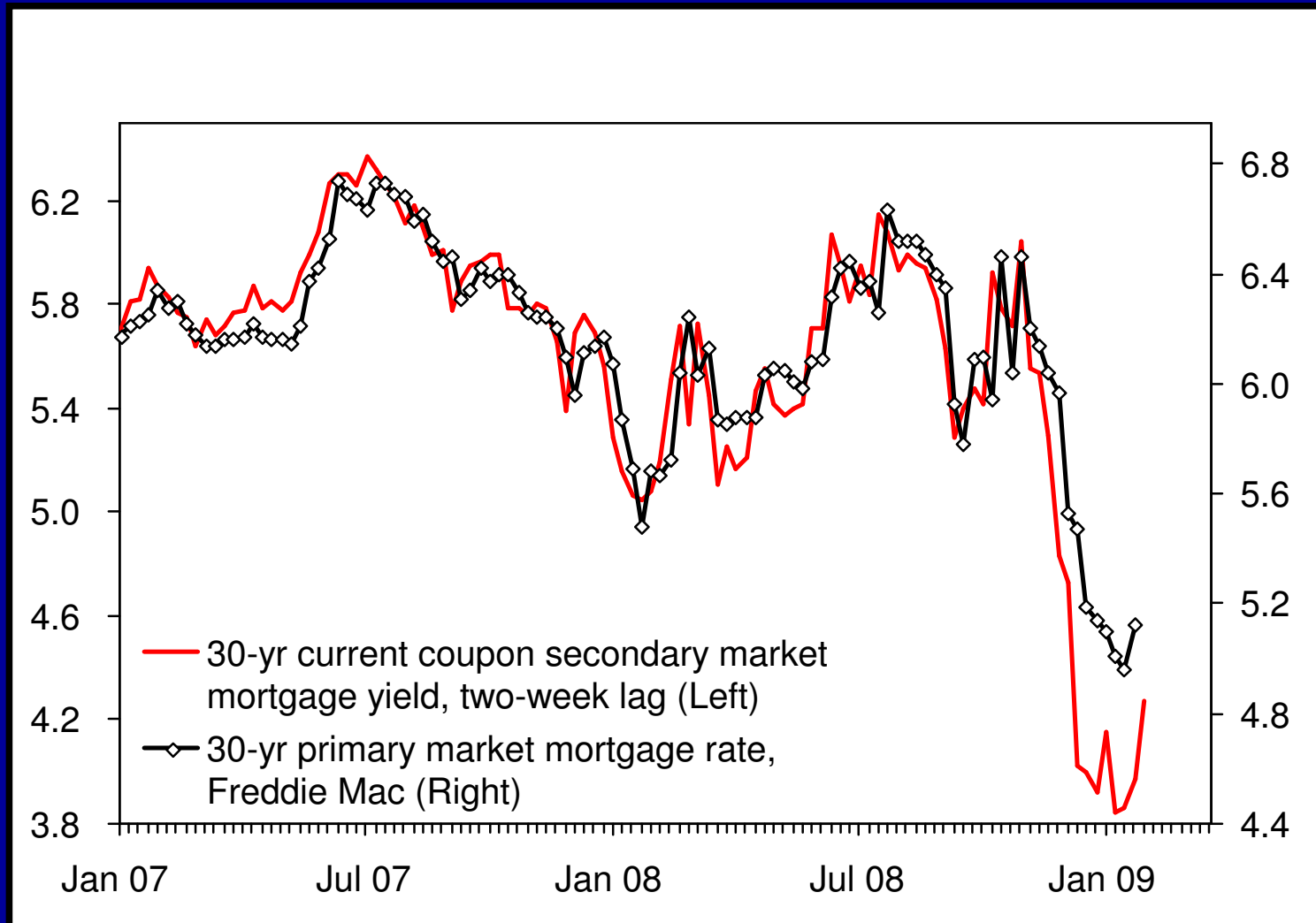
Price-To-Rent Ratio Still Far Too High



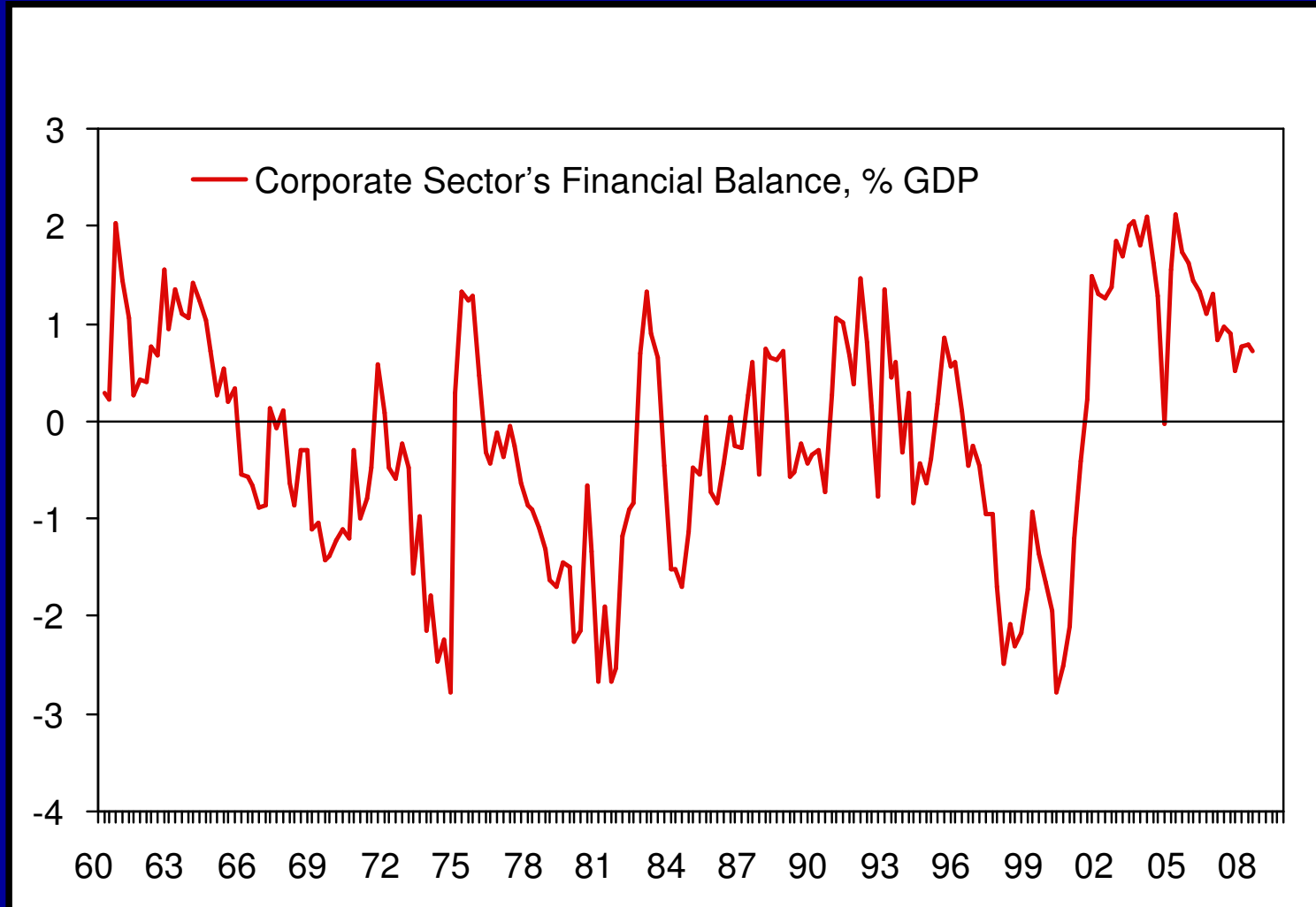
Homebuilders Running To Stand Still



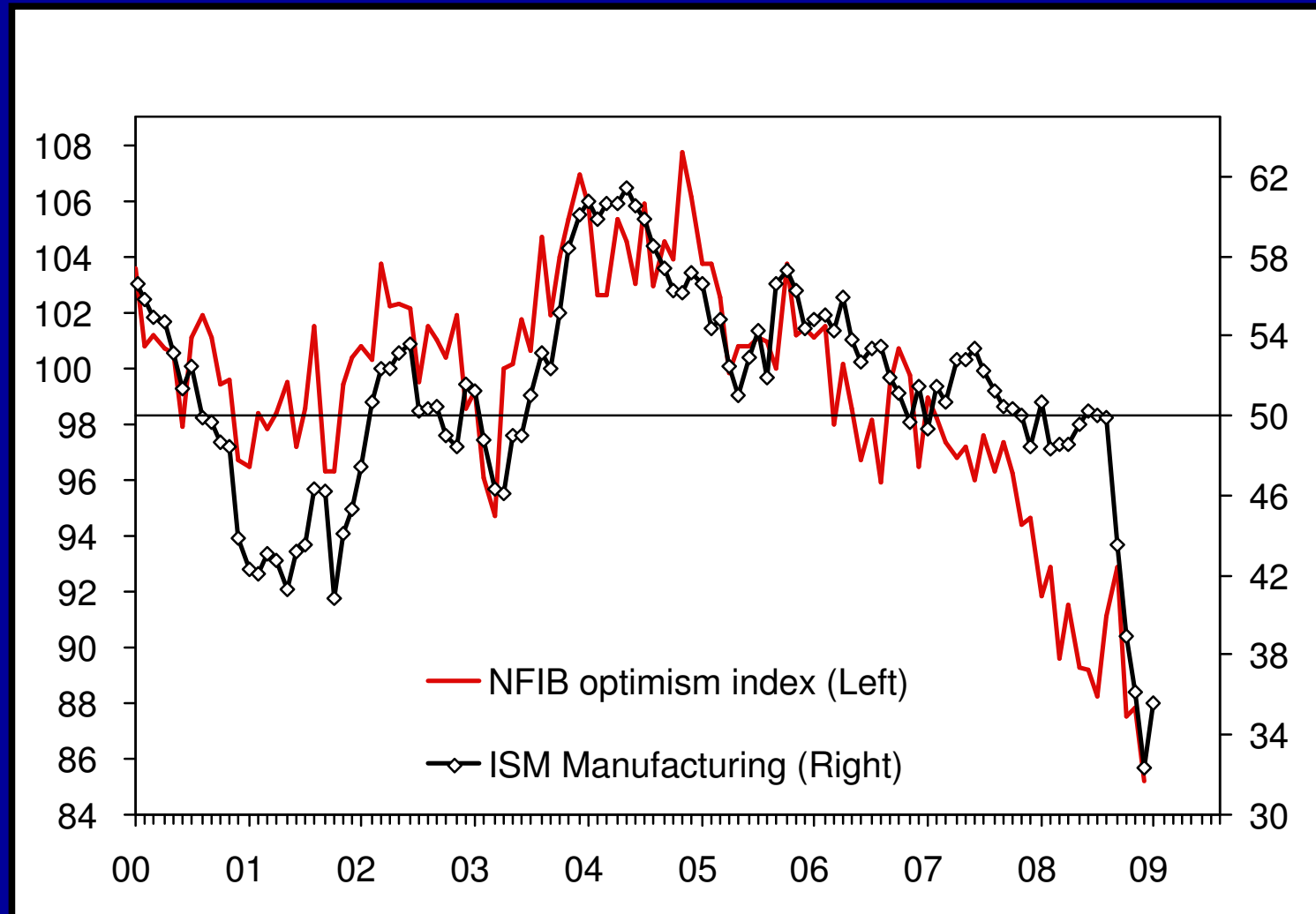
Falling Rates Will, In Time, Help



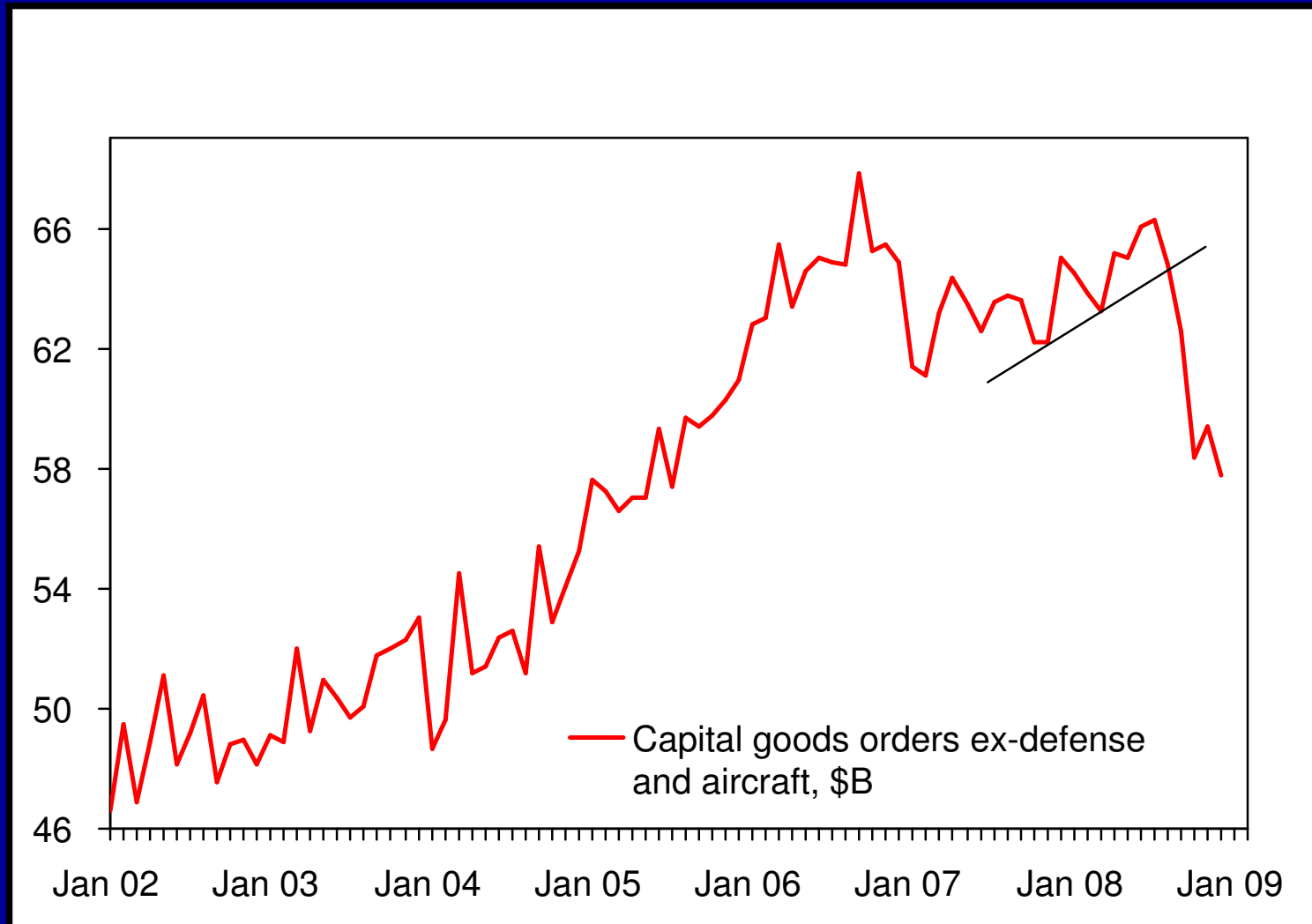
Meanwhile, Corporate Finances Look OK



...But Business Confidence Is Rock-Bottom



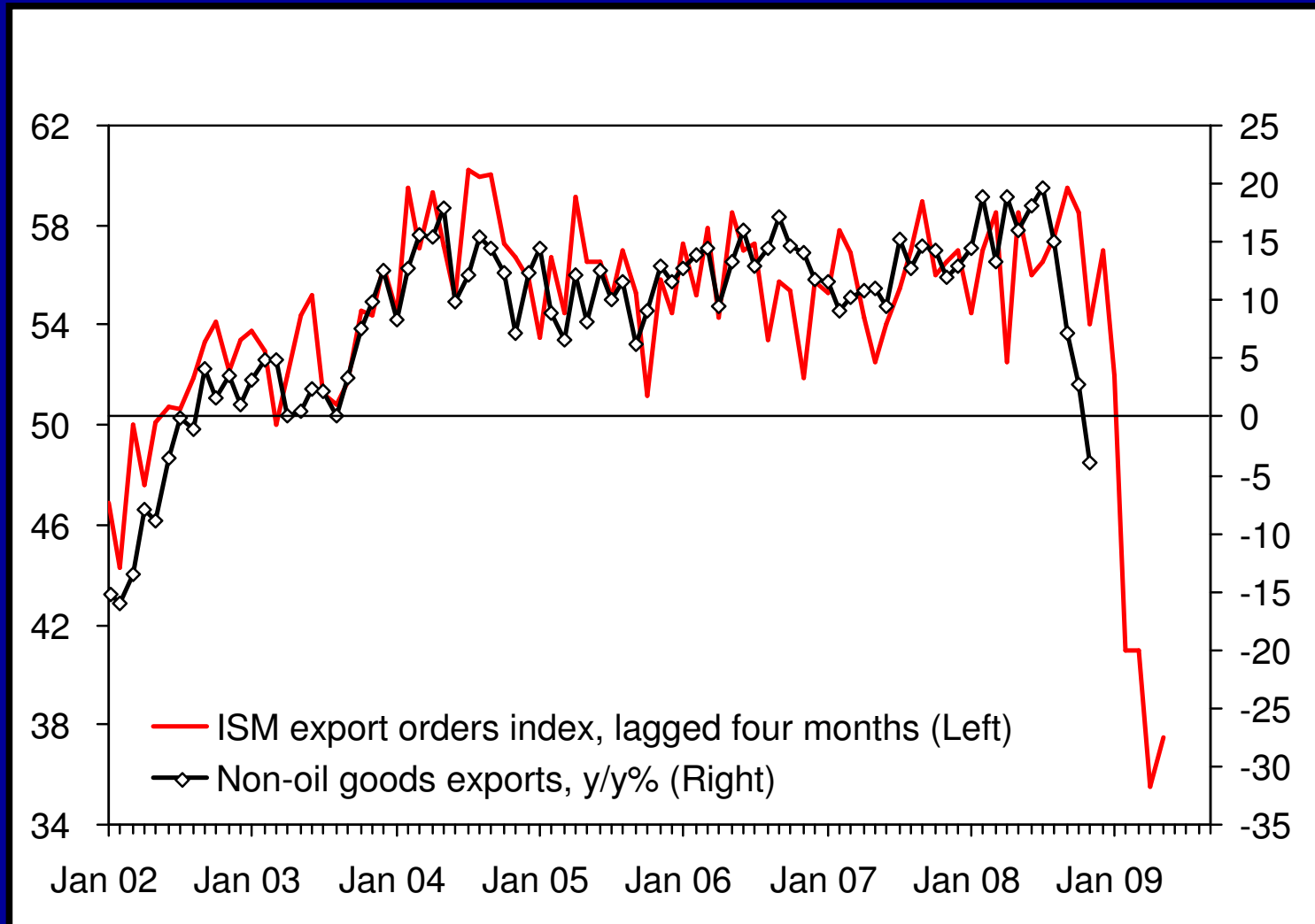
...So Capital Spending Is Rolling Over



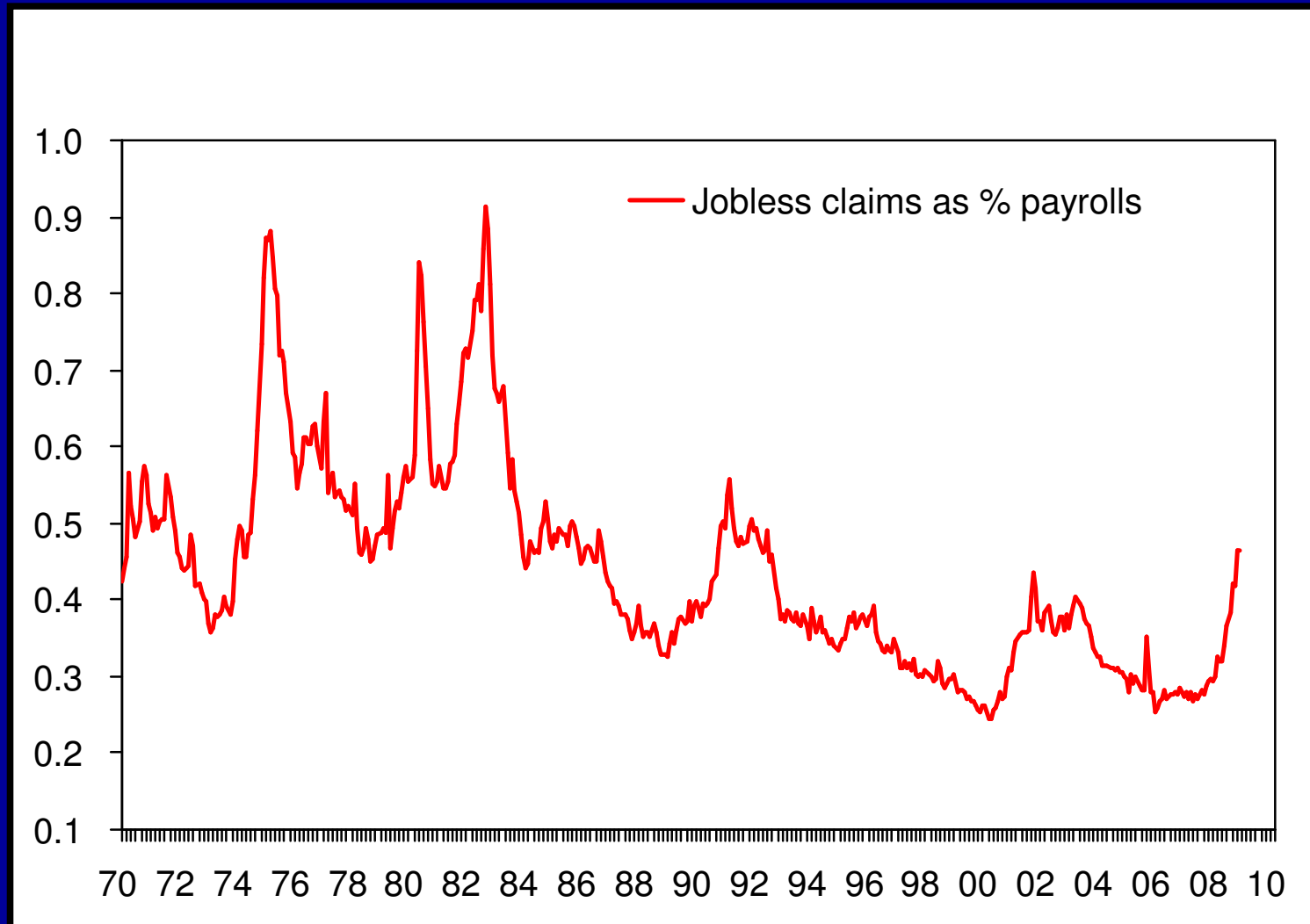
...And Inventories Have Soared



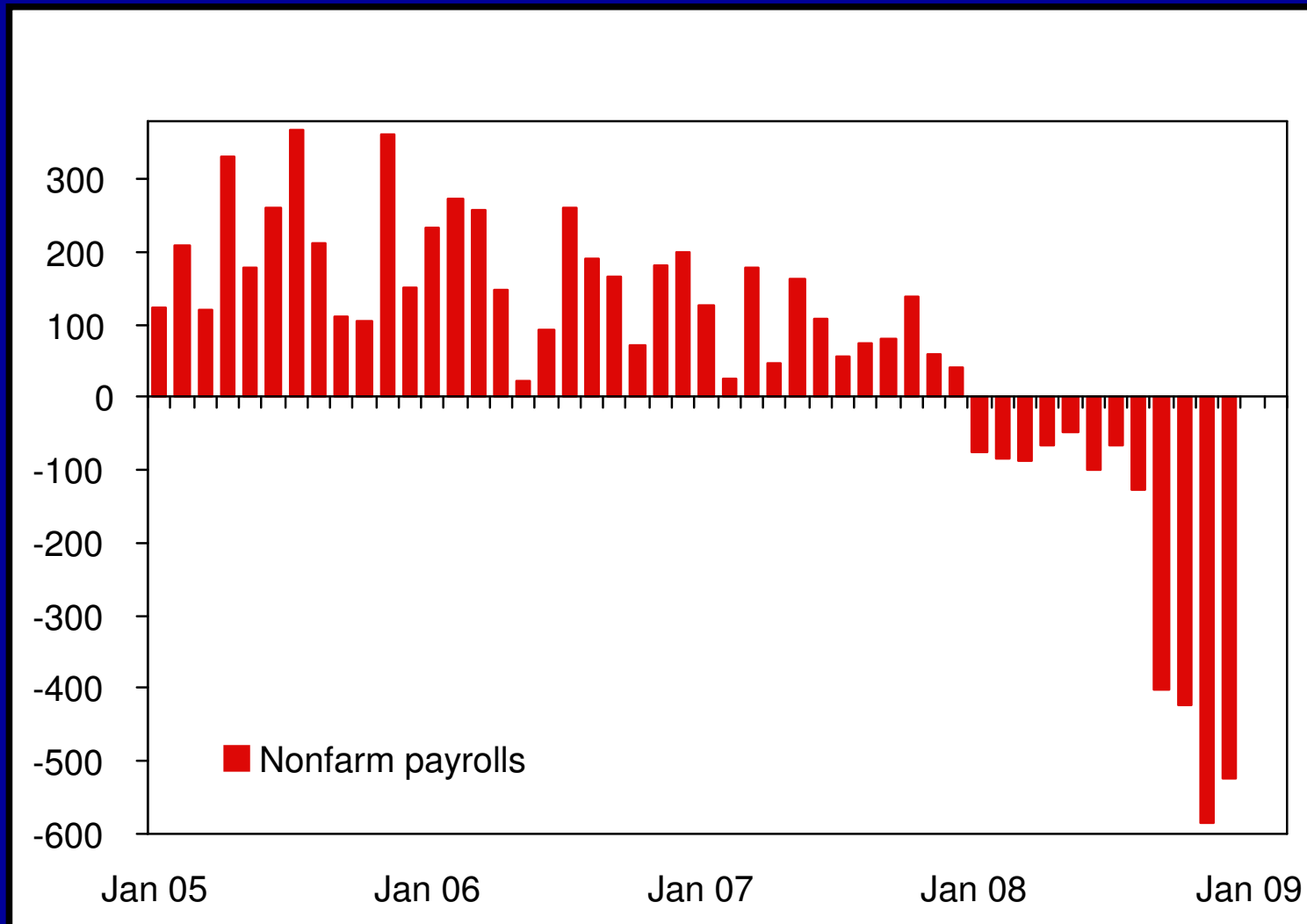
Global Credit Crunch Has Killed Exports



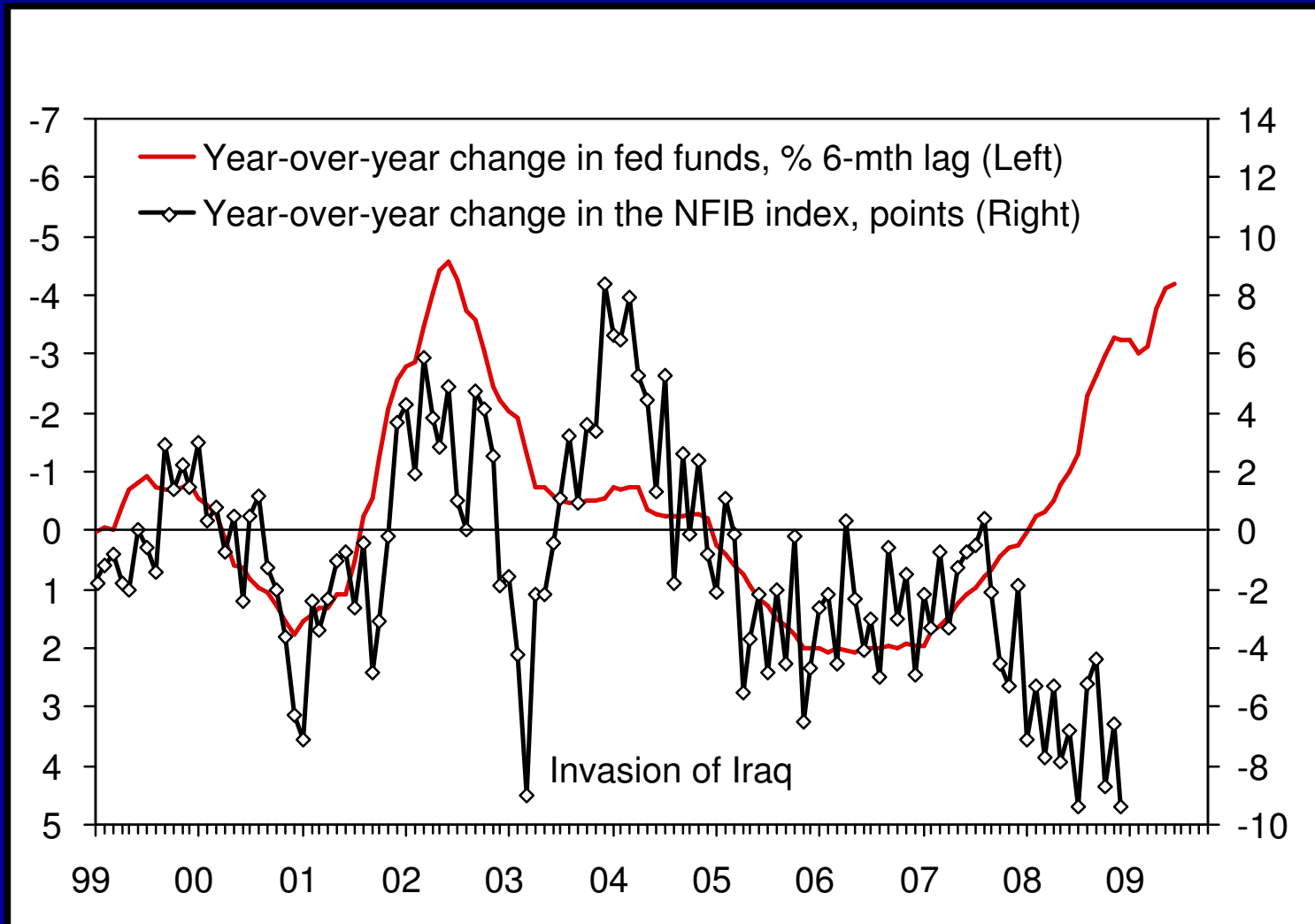
Layoffs Rocketing; Will Rise Further



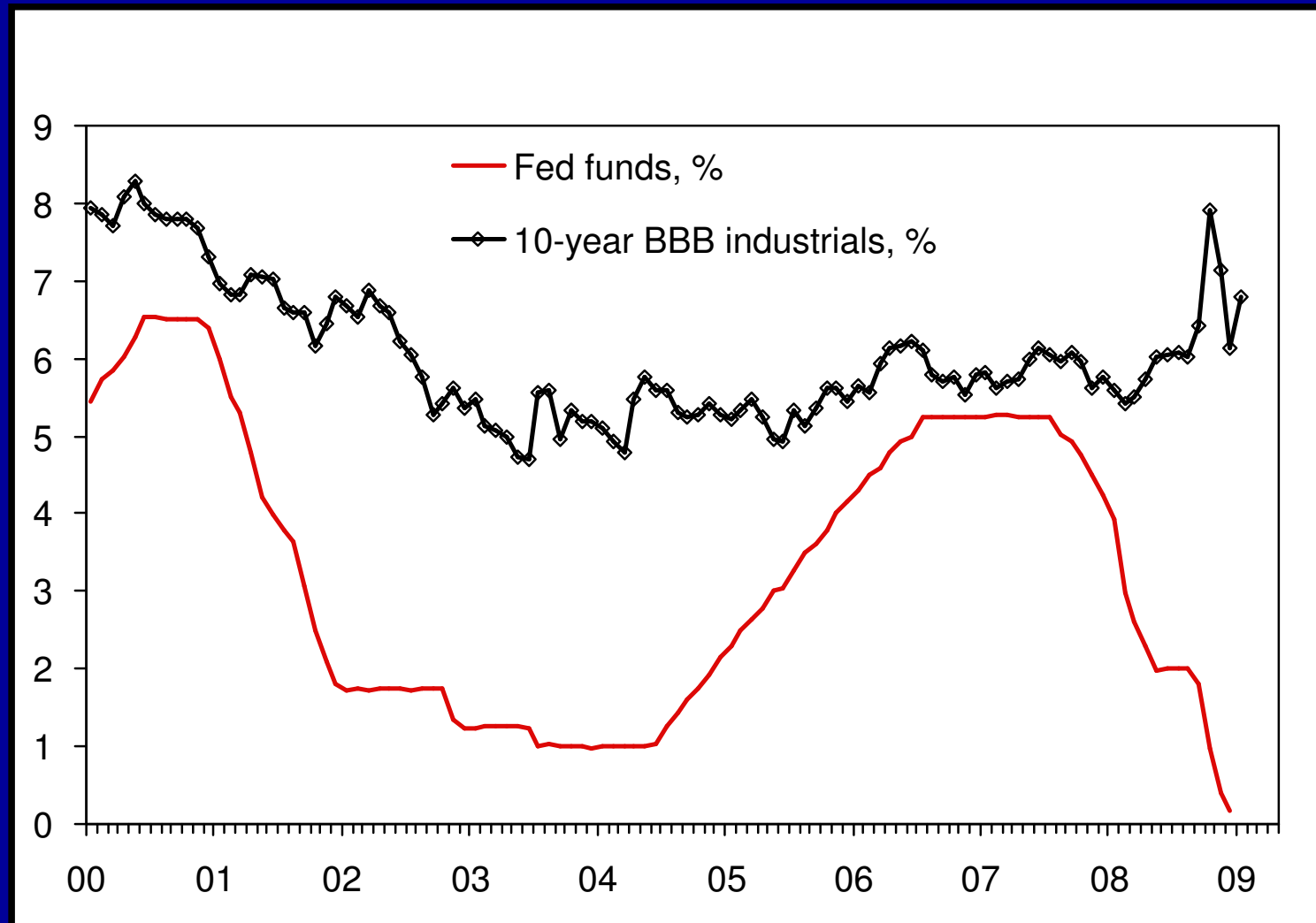
Hiring Is Dead Too, So Payrolls Collapsing



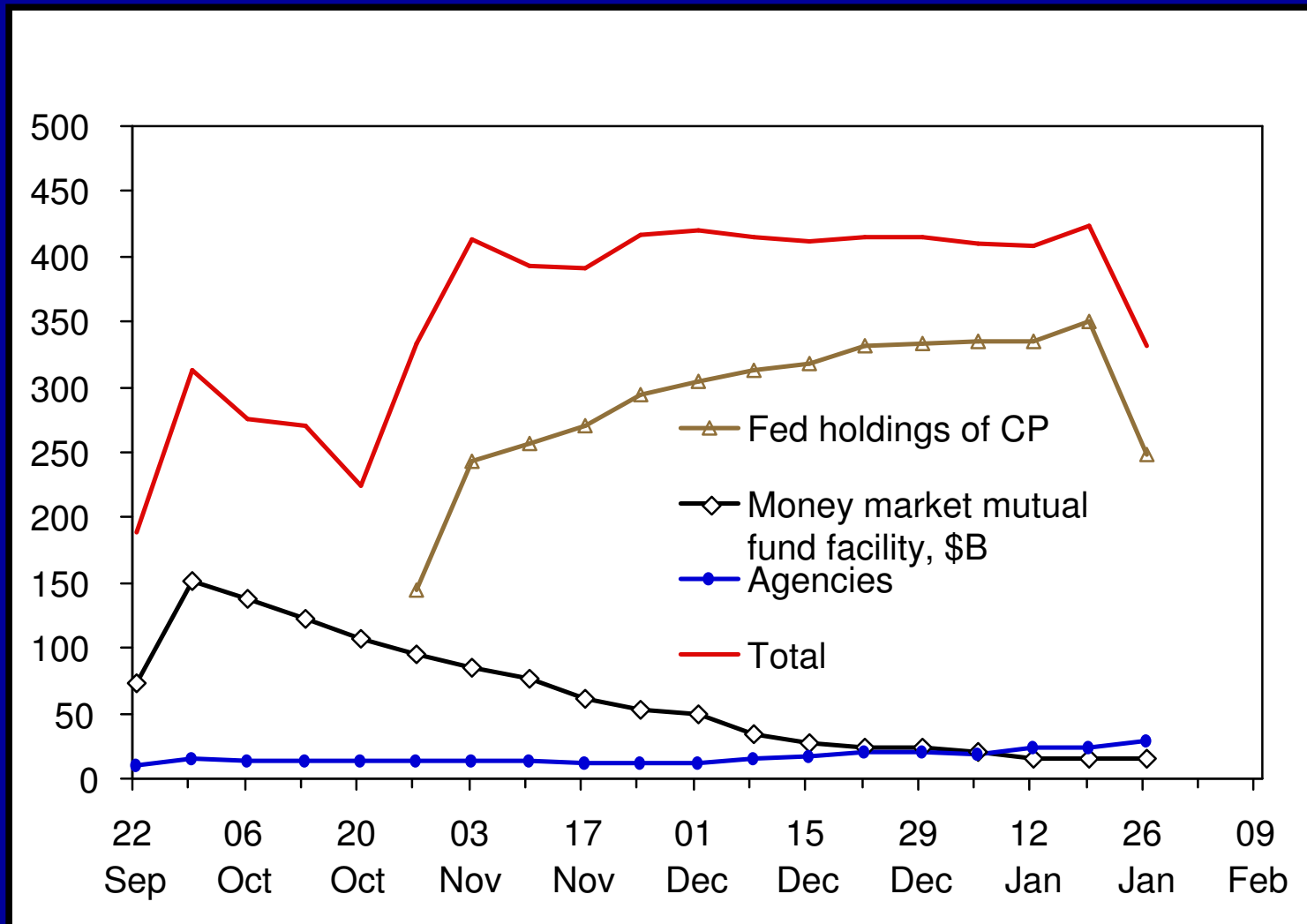
Monetary Policy Transmission Is Broken



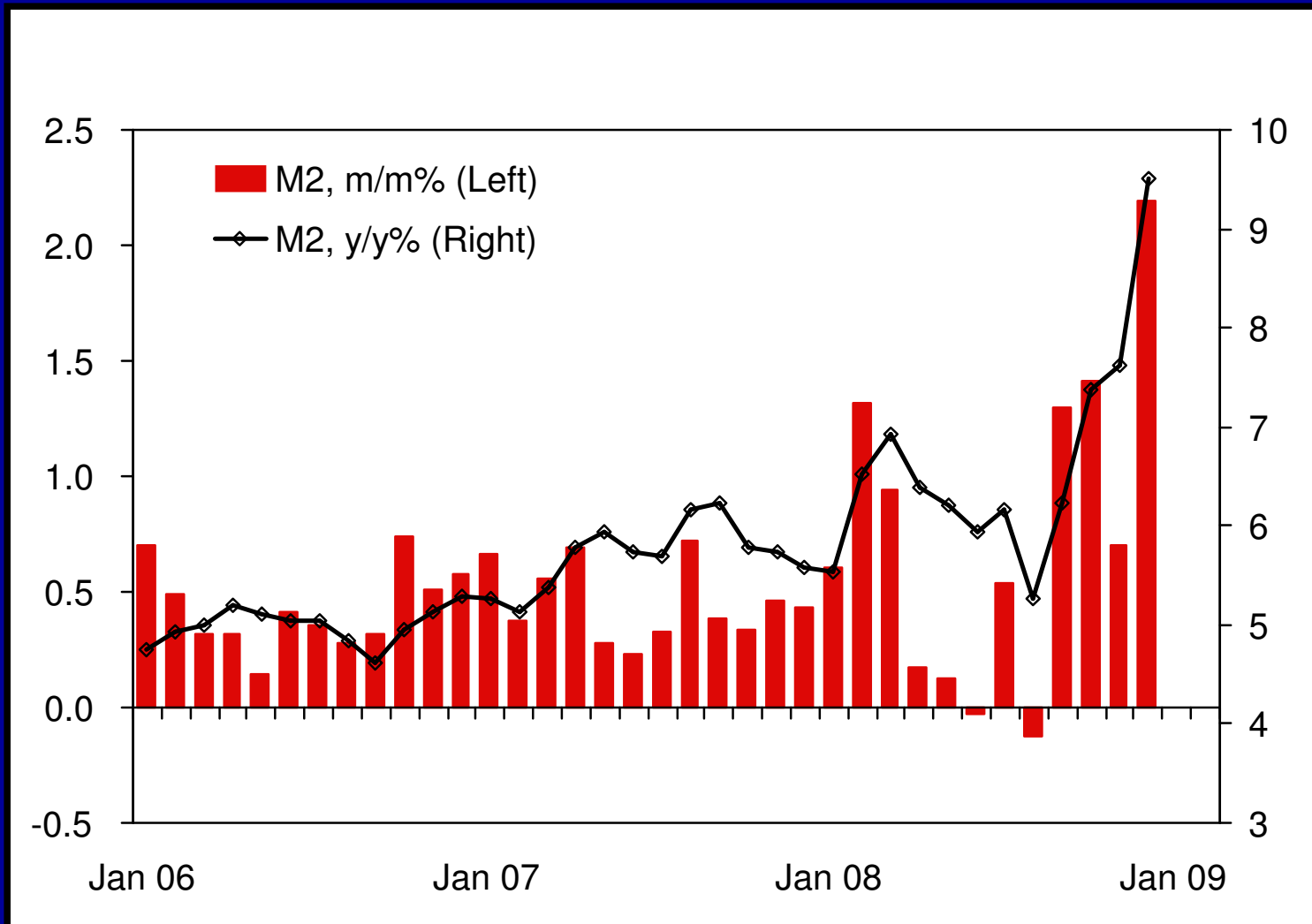
Corporate Yields Have Not Responded



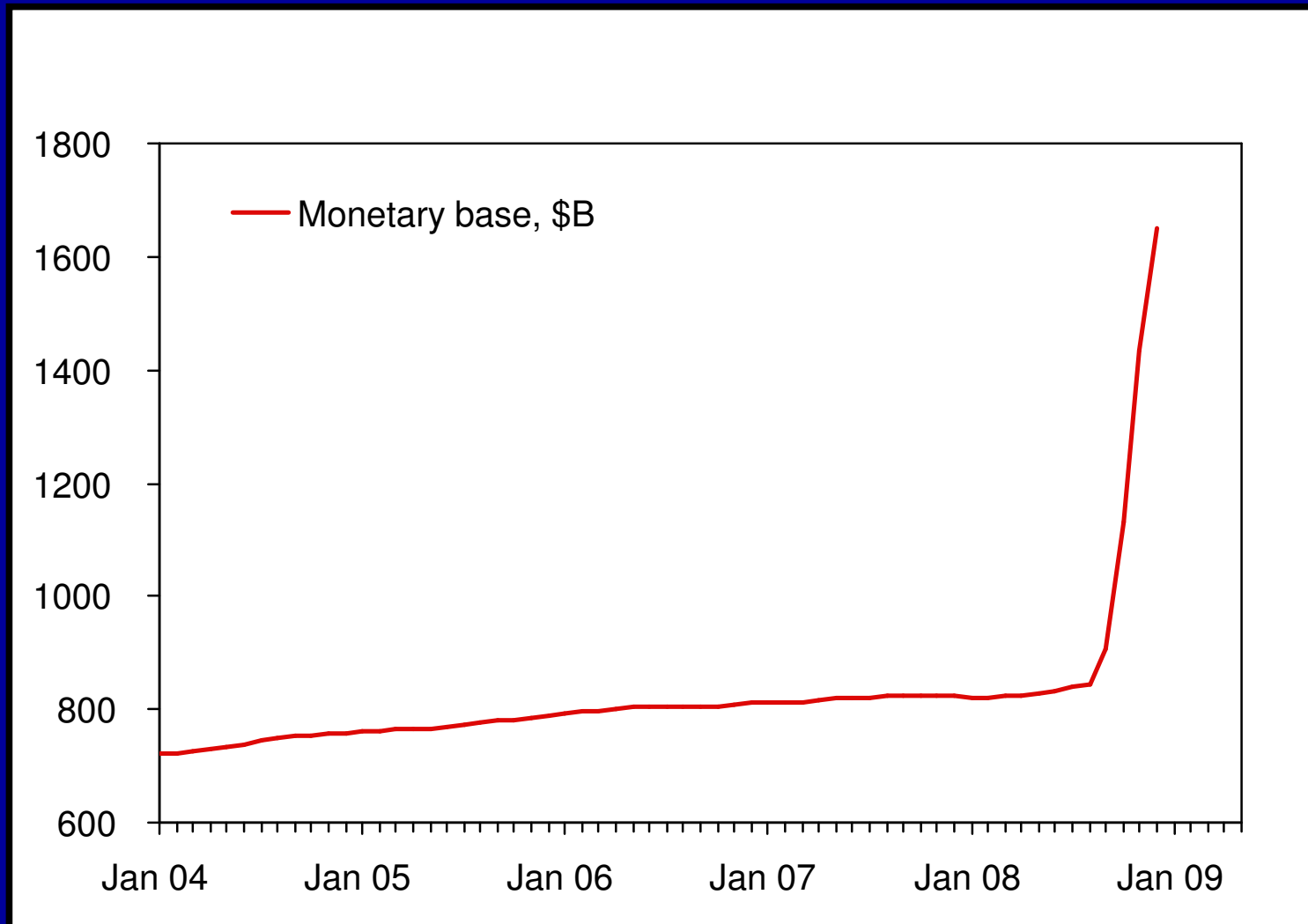
Quantitative Easing Began In September



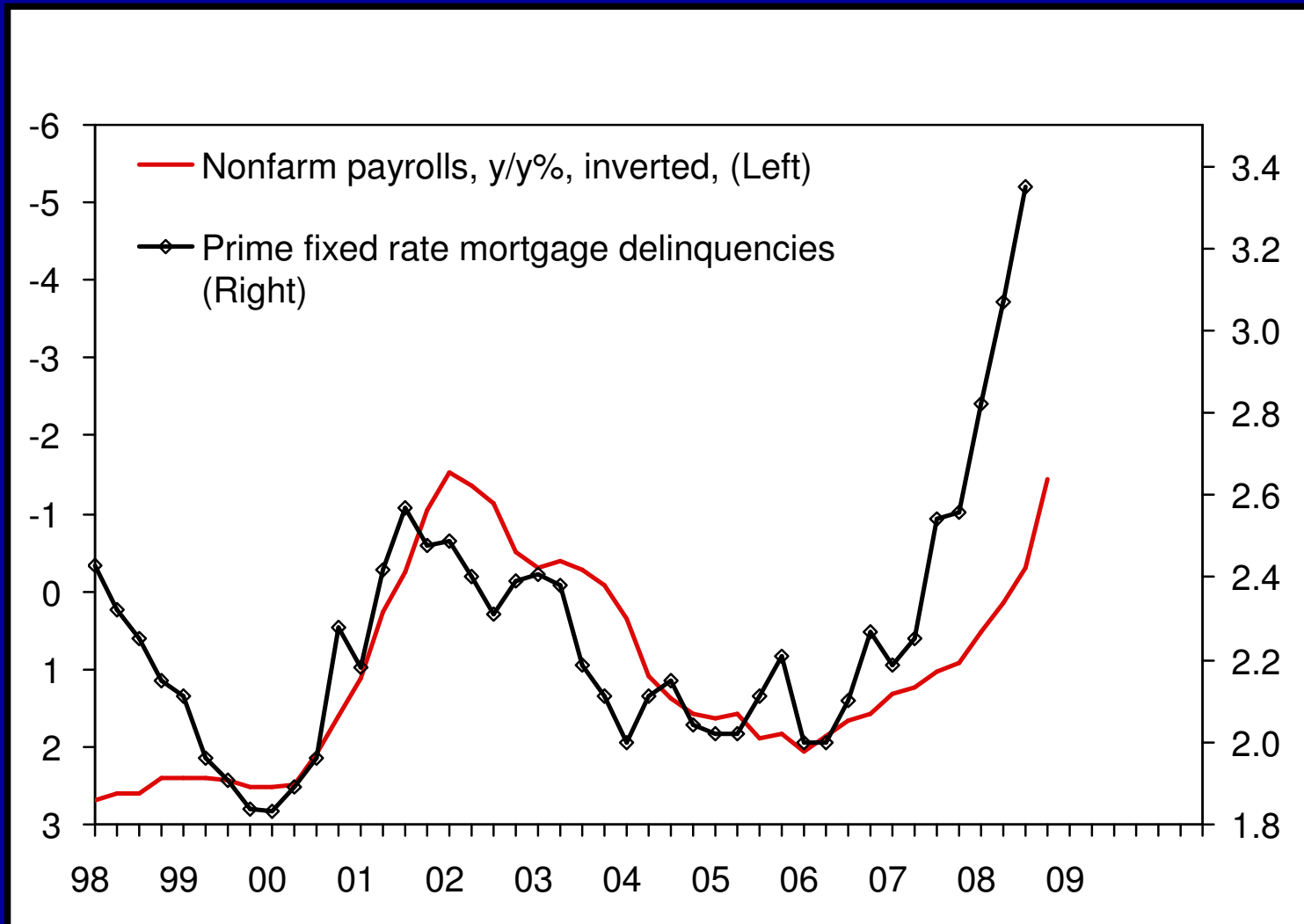
QE Has Massively Boosted M2



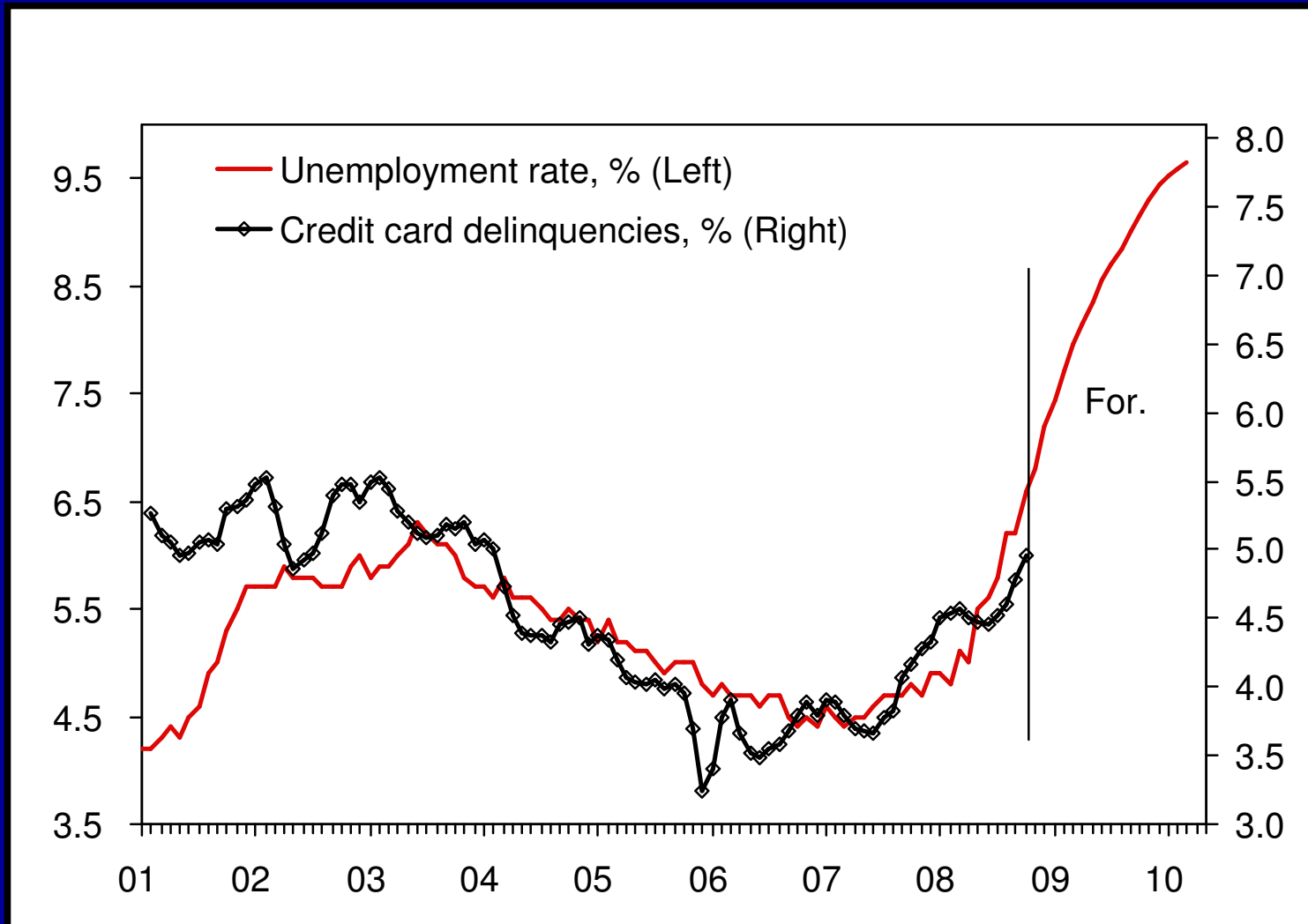
TAF And Others Have Boosted Reserves



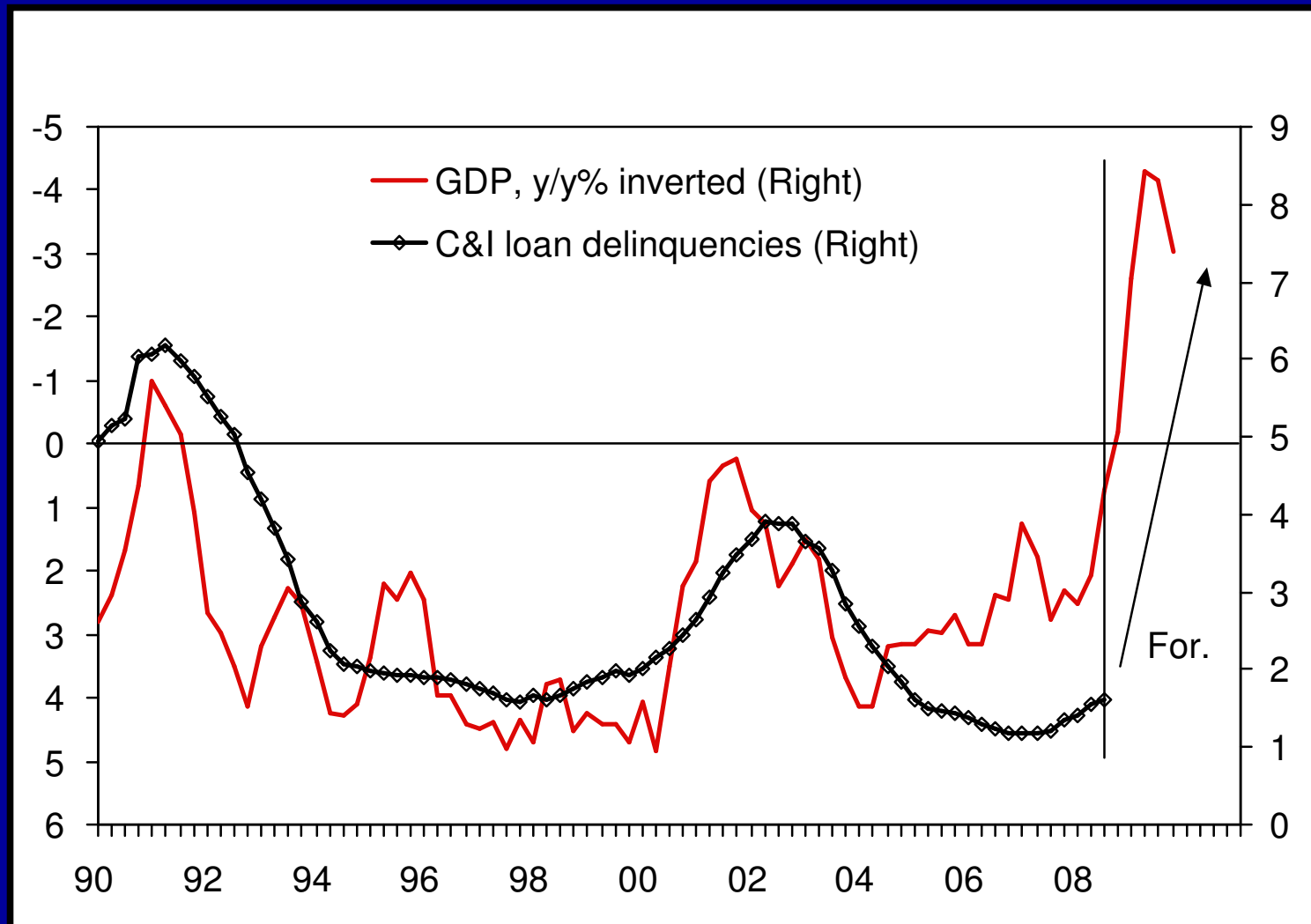
But Banks Face Further Huge Losses



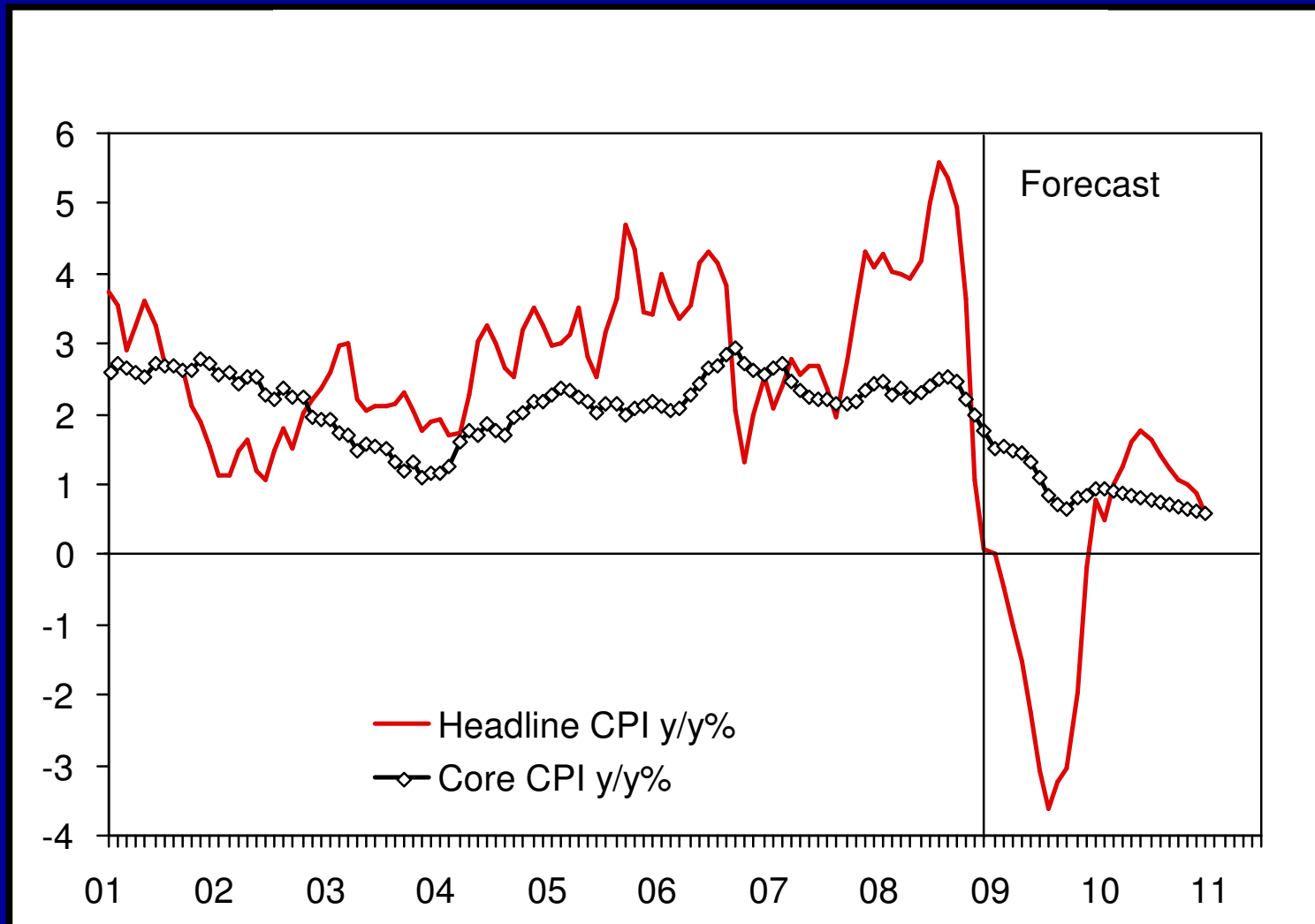
...And Not Just In Mortgages



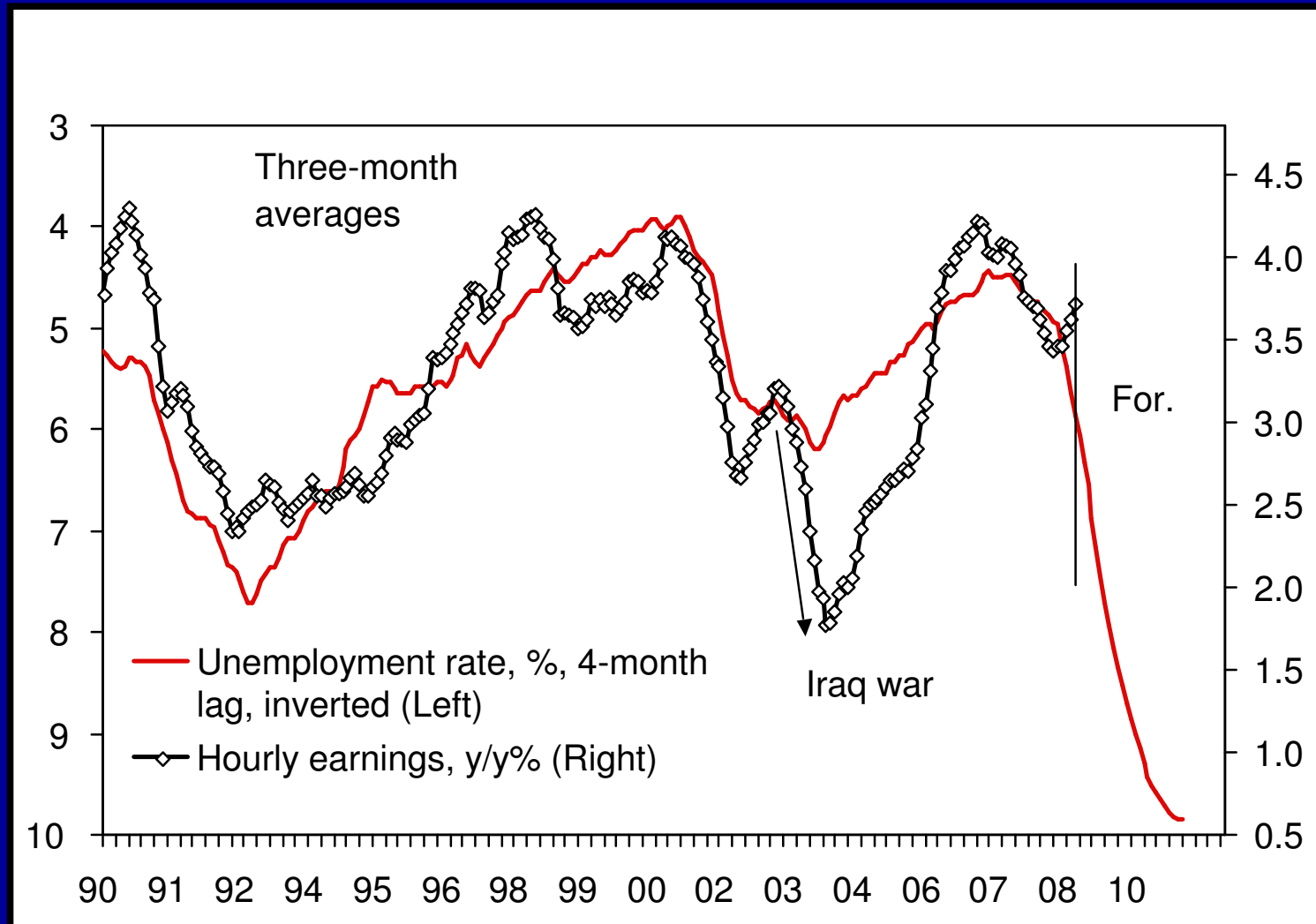
Corporate Loan Delinquencies Will Leap Too



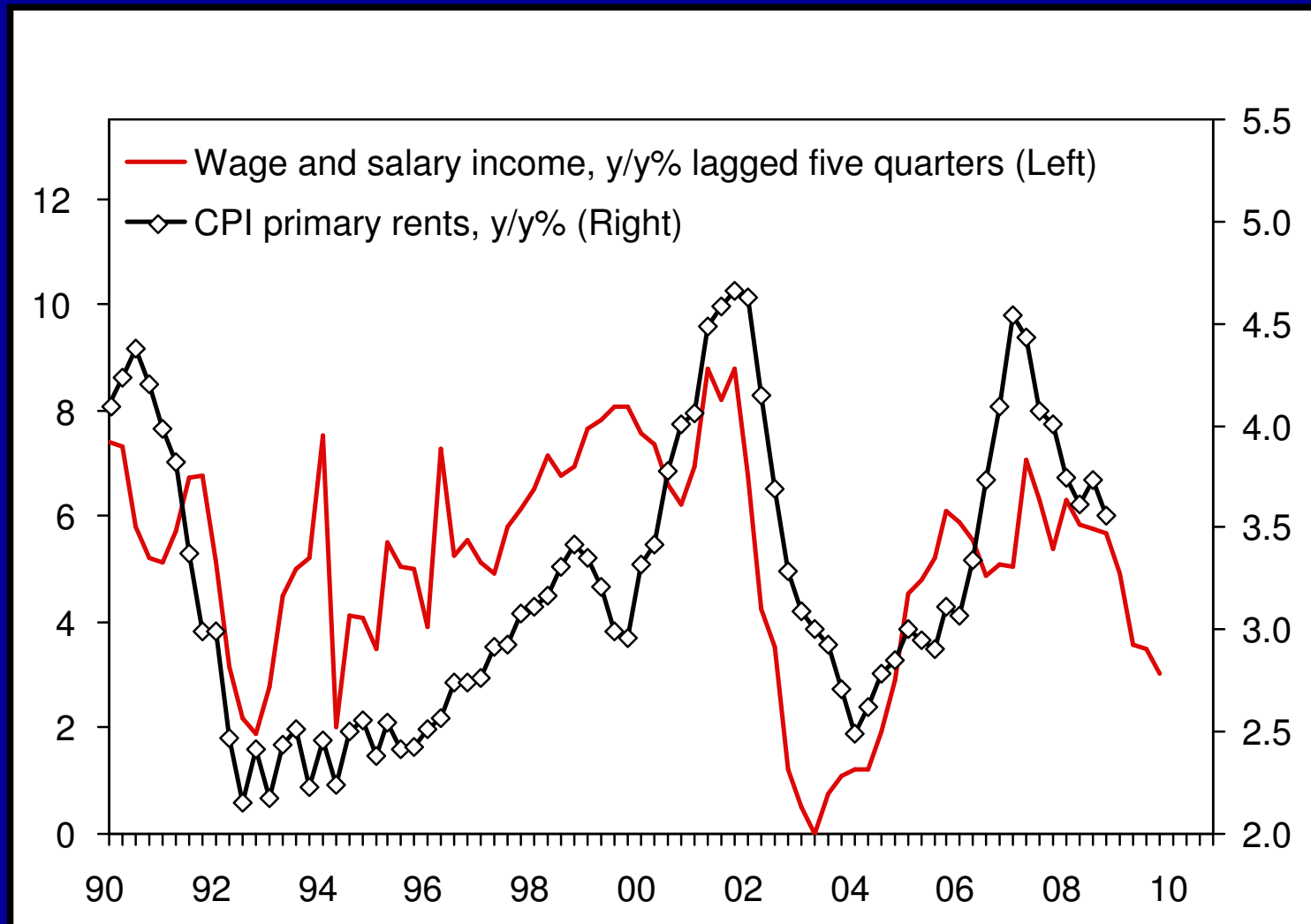
Headline Inflation Will Soon Be Negative



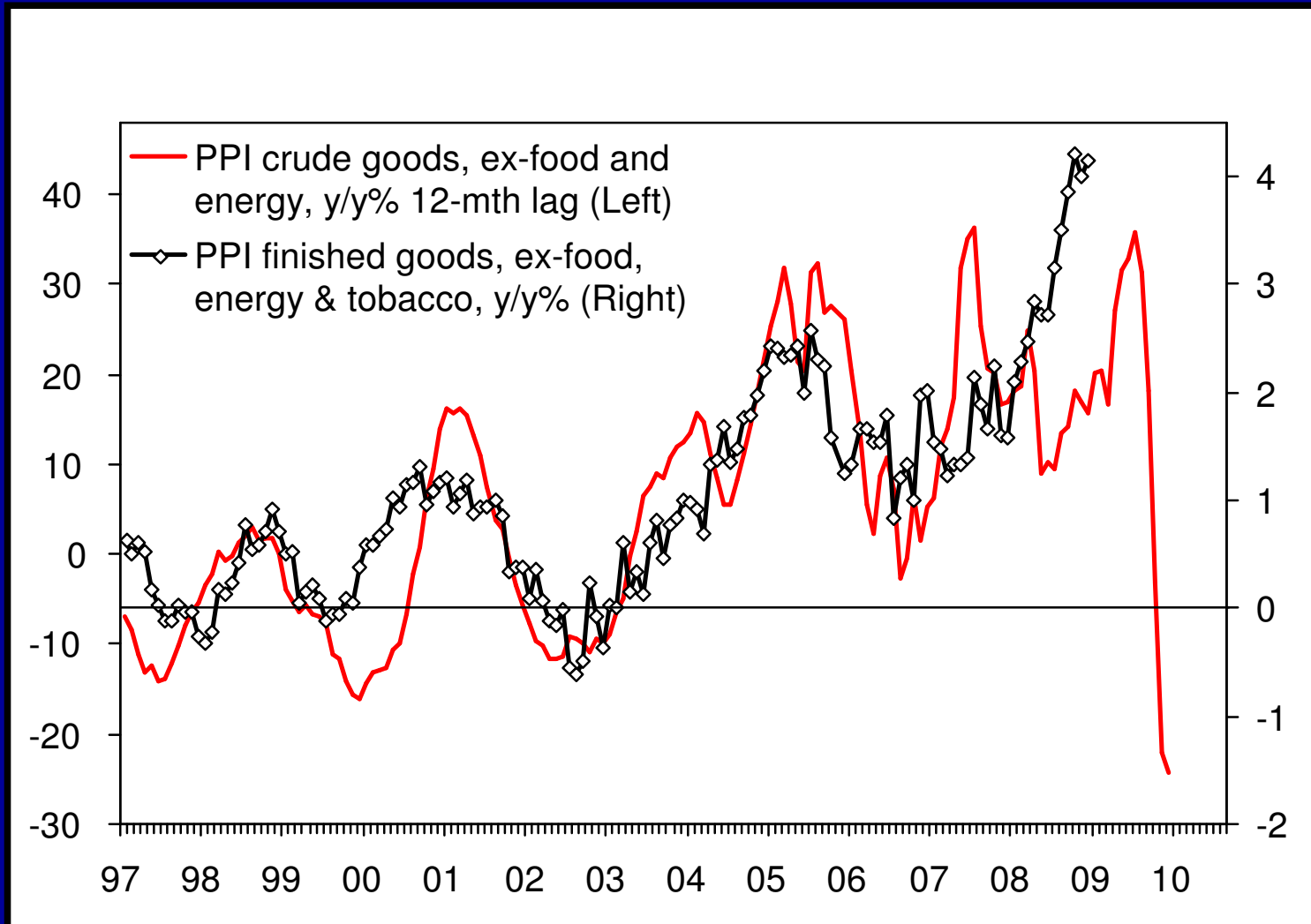
Slowing Wage Gains Will Drive Down Core



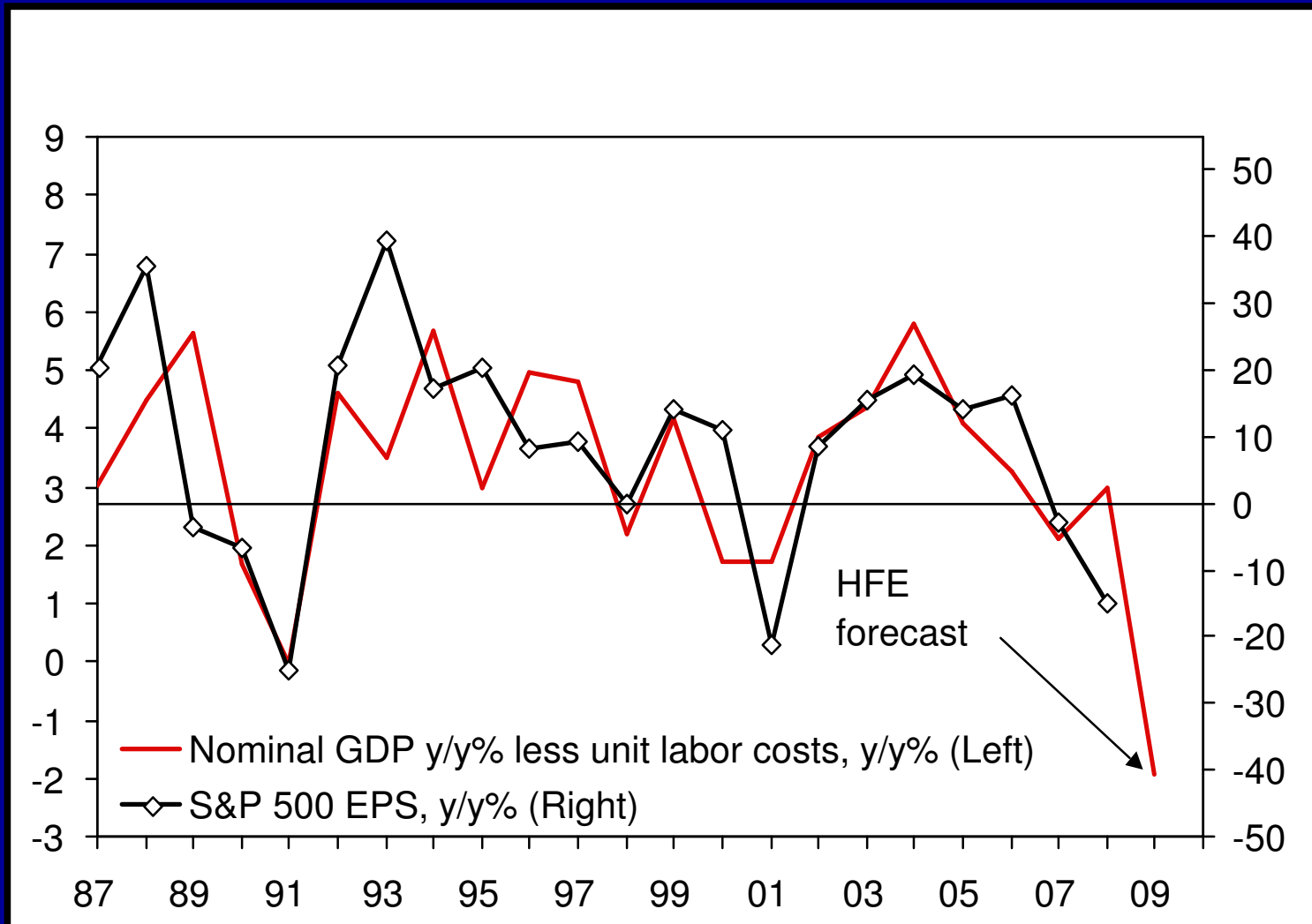
Slowing Wages Will Depress Rents



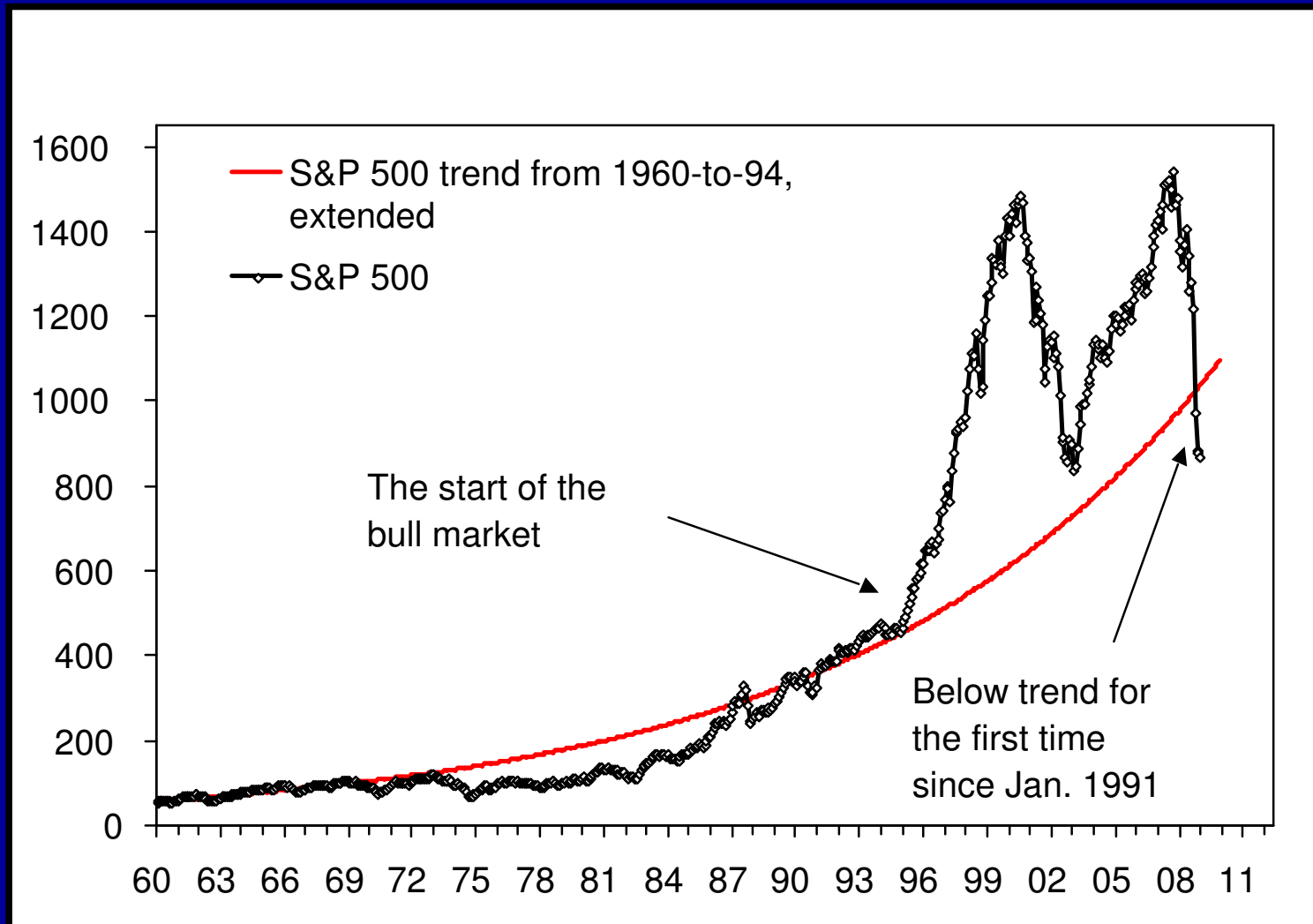
There's No Threat From Materials Prices



Equities Are Still Risky



...Though A Further Big Drop Is Unnecessary



Summary

- The consumer retrenchment will be deep and long, keeping pressure on banks
- Core inflation will drop all year; headline inflation will be negative until Q4
- The Fed will not raise rates this year and probably next year too.
- Corporate earnings will be very weak into 2010; Treasury yields can fall further