The Economic Outlook for the U.S. and Indiana

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April 15, 2011
Global Outlook Summary

- The global economic expansion is continuing at a healthy pace, but risks are mounting.
- Japan’s economy will recover from the devastating March 11 earthquake; global supply chains face near-term disruptions.
- Turbulence in MENA presents risks to oil supplies and prices.
- Europe faces an extended period of weak growth as sovereign debt problems are resolved.
- Emerging markets continue to offer the best growth prospects.
A Growing U.S. Economy Will Cut Unemployment

(Annual percent change)

(Percent)

Real GDP Growth (Left scale)  Unemployment Rate (Right scale)
## U.S. Economic Growth by Sector

(Percent change)

<table>
<thead>
<tr>
<th>Sector</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP</td>
<td>-2.6</td>
<td>2.9</td>
<td>2.8</td>
<td>2.9</td>
</tr>
<tr>
<td>Consumption</td>
<td>-1.2</td>
<td>1.7</td>
<td>2.6</td>
<td>2.6</td>
</tr>
<tr>
<td>Residential Investment</td>
<td>-22.9</td>
<td>-3.0</td>
<td>-1.0</td>
<td>25.9</td>
</tr>
<tr>
<td>Business Fixed Investment</td>
<td>-17.1</td>
<td>5.7</td>
<td>9.0</td>
<td>7.7</td>
</tr>
<tr>
<td>Federal Government</td>
<td>5.7</td>
<td>4.8</td>
<td>-0.1</td>
<td>-3.3</td>
</tr>
<tr>
<td>State &amp; Local Govt.</td>
<td>-0.9</td>
<td>-1.4</td>
<td>-1.8</td>
<td>-1.0</td>
</tr>
<tr>
<td>Exports</td>
<td>-9.5</td>
<td>11.7</td>
<td>9.9</td>
<td>9.6</td>
</tr>
<tr>
<td>Imports</td>
<td>-13.8</td>
<td>12.6</td>
<td>5.8</td>
<td>6.7</td>
</tr>
</tbody>
</table>
Is Inflation Heating Up?

• Inflationary pressures
  • Rapid growth in emerging markets
  • Expansionary monetary policies
  • Oil supply disruptions in Libya
  • Rising commodity prices

• Countervailing restraints
  • Excess productive capacity
  • Slack labor markets
  • Global competition
Industrial Materials Prices Have Surged

(IHS Global Insight Indexes, 2002:1=1.0)

- In U.S. Dollars
- In GDP-Weighted Currency Basket
U.S. Core Inflation Will Drift Upward

(Year-over-year percent change)

-2 -1 0 1 2 3 4 5 6
All-Urban CPI Core CPI Employment Cost Index

U.S. Core Inflation Will Drift Upward
U.S. Interest Rates Will Rise in 2012

Federal Funds, 10-Year Treasury, and 30-Year Mortgage Rate trends from 1990 to 2014.
Cross-Currents Affecting Consumer Finances

Positive Forces
• Upturn in Employment
• Real Income Growth
• Stock Market Recovery
• Low Interest Rates

Negative Forces
• Rising Gasoline Prices
• High Unemployment
• Reduced Housing Wealth
• High Debt Burdens
Consumers Are Cautious: Real Spending Growth

(Annual percent change) (Reuters/Michigan Index, 1966=100)

Real Consumption Growth  Consumer Sentiment
Durable Goods Lead the Ups and Downs in Real U.S. Consumer Spending

(Percent change, chained 2005 dollars)
A Delayed Recovery in Housing Markets

- The recession led to a drop-off in household formation.
- Home affordability has greatly improved, boosting demand.
- High mortgage foreclosure rates are adding to excess supply, depressing prices and holding back new construction.
- Sustained job growth will spark a housing market recovery.
- Multifamily units’ share of housing starts will rise.
U.S. Housing Starts Have Hit Bottom: Prices Not Quite There Yet

(Million units) (Purchase-only index, 1991Q1 = 100)

Housing Starts (Left scale)  FHFA House Price Index (Right scale)
Risks to the US Forecast

Downside Risks

– Oil supply disruptions spread, causing prices to soar.
– Financial instability returns; housing recession drags on.
– Consumers retrench after setbacks to asset values and purchasing power.
– Businesses are reluctant to hire or invest.

Upside Risks

– Credit channels function smoothly, supporting investment.
– Rapid technological progress boosts real income growth.
– Robust growth in many emerging markets fuels exports.
Real GDP Growth in Alternative Scenarios

(Percent change, annual rate)

-8 -6 -4 -2 0 2 4 6
2007 2008 2009 2010 2011 2012 2013

- Baseline (60%)
- Pessimistic (20%)
- Optimistic (20%)
Light Vehicle Sales in Alternative Scenarios

(Millions of units, annual rate)

- Baseline (60%)
- Pessimistic (20%)
- Optimistic (20%)

Years: 2007 to 2013
Bottom Line

• The economic recovery is on a self-sustaining course, barring a major oil market disruption.

• Job growth will enable consumers to spend more confidently.

• Business equipment investment, exports, consumer durables, and housing construction will drive the expansion.

• Although food and energy prices are accelerating, high unemployment will restrain wage gains and core inflation.

• The federal government needs an “exit strategy” from deficit spending or financial markets will eventually impose one.
Regional Outlook
Labor markets reverse coursed in 2010

Year-over-year Employment Change, December 2010, %; Indiana 0.8%
Momentum is building in most regions

Employment Momentum
February 2011

Year/year (%)
3-mth avg annualized (%)

Improving
Expanding
Contracting
Slipping

-2
-1
0
1
2
3
4
5

-1.0 -0.5 0.0 0.5 1.0 1.5 2.0 2.5 3.0

New England
Mid Atlantic
South Atlantic
East North Central
West North Central
Mountain
East South Central
West South Central
Mountain
Pacific

TX: -2.6%
But many states are still deep in the hole

Peak to February 2011 Employment Change, %

US: -5.6%
IN: -6.8%
Recovery gathers momentum in 2011

Employment Growth 2011Q4, year-over-year %

US: 1.5%
IN: 1.8%

Percent
- 0.8 to 1.3
- 1.4 to 1.6
- 1.6 to 1.8
- 1.9 to 2.4

Map showing employment growth with various shades indicating different percentage ranges.
Medium-term performance: GSP

Real Gross State Product Growth 2011-2016, % annual rate

- **US**: 3.0%
- **IN**: 2.8%
- **TX**: 3.8%
Medium-term performance: Jobs

Employment Growth 2011-2016, % annual rate

US: 1.8%
IN: 1.8%

Percent
1.1 to 1.3
1.4 to 1.7
1.7 to 2.0
2.1 to 2.6
Indiana will recover lost jobs early in 2014

Year of Return to Peak Employment

Return To Peak
- Gray: 2010 to 2011
- Blue: 2012
- Green: 2013
- Yellow: 2014 to 2015
- Red: Past 2015

Indicate Indiana will recover lost jobs early in 2014.
Bottom Line

• Deeper, earlier recession than most

• Among 2010 growth leaders early in the year
  – Transportation equipment rebound
  – Low paying temp and business services jobs

• Slow recovery, but a recovery is indeed in place

• Medium term performance near average among states
  – Outpacing other midwest manufacturing giants
Indiana Employment Forecast

![Graph showing employment forecast for Indiana with percentage change and thousands of employees.](image)
Wage Gains Return
(nominal total wages and salaries)
Cars and Houses

- Indiana New Car Registrations - L
- Indiana Housing Starts - R
# Forecast Summary

(Percent unless otherwise noted)

<table>
<thead>
<tr>
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<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
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<tbody>
<tr>
<td>Employment</td>
<td>-5.7</td>
<td>0.3</td>
<td>1.2</td>
<td>2.3</td>
</tr>
<tr>
<td>Unemployment Rate</td>
<td>10.4</td>
<td>10.2</td>
<td>8.8</td>
<td>8.5</td>
</tr>
<tr>
<td>Personal Income</td>
<td>-2.4</td>
<td>3.2</td>
<td>5.0</td>
<td>3.1</td>
</tr>
<tr>
<td>Housing Starts (000)</td>
<td>13.1</td>
<td>13.2</td>
<td>13.7</td>
<td>21.7</td>
</tr>
<tr>
<td>Retail Sales</td>
<td>-7.2</td>
<td>6.6</td>
<td>7.6</td>
<td>5.3</td>
</tr>
<tr>
<td>Real Gross State Product</td>
<td>-5.0</td>
<td>2.0</td>
<td>2.4</td>
<td>3.1</td>
</tr>
</tbody>
</table>
Thank you!

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