

UNITED STATES

Healthy gains in private consumption have helped to keep GDP growth above trend thus far this year. However, the correction in residential construction is likely to accelerate over the near term, and housing wealth could decline which, together with weaker labour market conditions, could lead to lower consumption growth over time. GDP should therefore slow to a pace below potential in 2008 and then recover in 2009, although there are considerable downside risks. Headline inflation has recently moved up, but core inflation seems to have stabilized near 2% and, assuming that energy prices level out, inflationary pressures should remain fairly moderate over the projection period.

The current stance of monetary policy, slightly accommodative, seems appropriate, but the federal funds rate should be brought back to neutral when the economy recovers. The room for fiscal manoeuvre is limited, including for widespread support to distressed borrowers, since the slowdown in activity is likely to curb revenues, pushing up the federal government deficit. In addition, the challenge of funding entitlements will become more pressing with the baby boom generation beginning to retire in 2008.

Housing is tumbling...

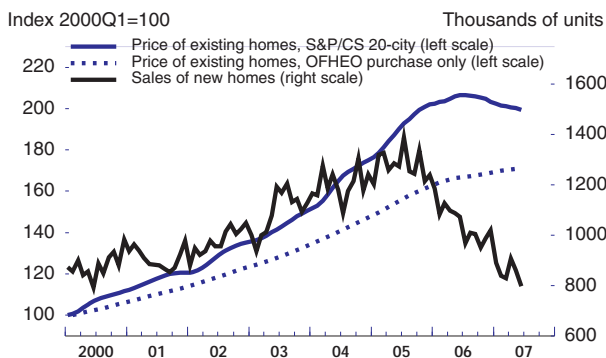
Activity in the housing sector has been contracting since the beginning of 2006 and the latest data indicate that the slump is getting worse. Home sales have declined considerably as the year has progressed and the weakness in housing demand has also shown up in prices. House prices have decelerated, and are now probably falling. Homebuilders have slashed production – housing starts are down nearly 50% from their peak – but not enough to offset the drop in demand, resulting in a substantial accumulation of inventories relative to sales.

... and financial markets are in turmoil

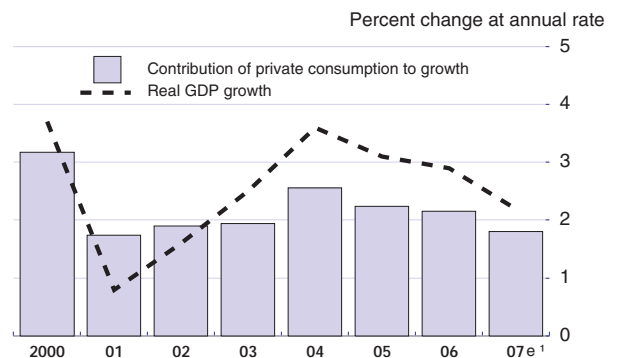
The deterioration of the housing market contributed to the financial market crisis in early August. Increasingly bad news about the performance of sub-prime mortgages led to a surge in the yields of mortgage-backed securities, as investors reassessed their risk exposure

United States

The housing market has tumbled



But consumer spending remained strong



1. Secretariat estimation.

Sources : Office of Federal Housing Enterprise Oversight, S&P/Case-Shiller, US Census Bureau, Bureau of Economic Analysis.

StatLink <http://dx.doi.org/10.1787/161112164188>

United States: **Employment, income and inflation**

Percentage changes from previous period

	2005	2006	2007	2008	2009
Employment ¹	1.6	1.8	1.1	0.4	0.7
Unemployment rate ²	5.1	4.6	4.6	5.0	5.0
Employment cost index	3.1	2.9	3.1	3.2	3.0
Compensation per employee ³	3.4	4.0	5.0	3.6	3.5
Labour productivity ³	1.6	1.1	1.2	1.6	1.5
Unit labour cost ³	2.2	3.0	3.9	2.2	2.2
GDP deflator	3.2	3.2	2.6	2.1	2.0
Consumer price index	3.4	3.2	2.8	2.7	1.9
Core PCE deflator ⁴	2.2	2.2	2.0	1.8	1.8
Private consumption deflator	2.9	2.8	2.5	2.4	1.7
Real household disposable income	1.7	3.1	3.4	2.0	2.5

1. Whole economy, for further details see *OECD Economic Outlook Sources and Methods*, (<http://www.oecd.org/eco/sources-and-methods>).

2. As a percentage of labour force.

3. In the private sector.

4. Price index for personal consumption expenditure excluding food and energy.

Source: OECD Economic Outlook 82 database.

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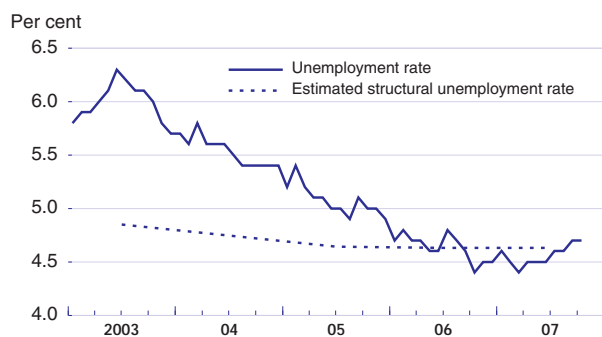
and showed greater aversion to risk. The markets for commercial paper and non-conforming mortgages came to a halt and have been continuing to show sign of stress.

No spillover to private consumption thus far...

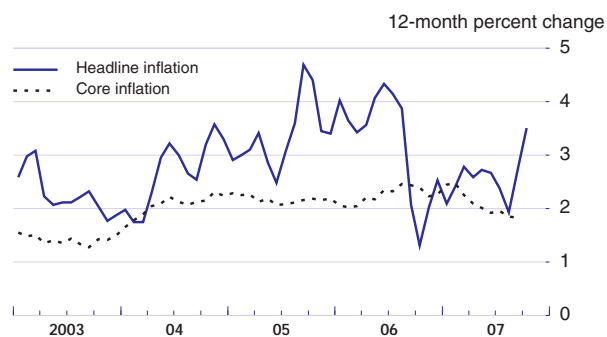
In the face of these adverse shocks, compounded by higher oil prices, the US economy has expanded at a surprisingly robust pace thus far this year. Strong consumer spending, together with buoyant non-residential investment, remained the main engine of growth. Healthy gains in real disposable incomes, partly due to large bonus payments and stock option exercises at the beginning of the year, have supported household demand.

United States


Unemployment has edged up



Core inflation has moderated



Source: Bureau of Labor Statistics.

StatLink  <http://dx.doi.org/10.1787/161117666770>

United States: **Financial indicators**

	2005	2006	2007	2008	2009
Household saving ratio ¹	0.5	0.4	0.7	0.7	1.2
General government financial balance ²	-3.6	-2.6	-2.8	-3.4	-3.5
Current account balance ²	-6.1	-6.2	-5.6	-5.4	-5.3
Short-term interest rate ³	3.5	5.2	5.3	4.6	4.7
Long-term interest rate ⁴	4.3	4.8	4.7	4.5	4.8


1. As a percentage of disposable income.

2. As a percentage of GDP.

3. 3-month euro-dollar.

4. 10-year government bonds.

Source: OECD Economic Outlook 82 database.

StatLink  <http://dx.doi.org/10.1787/158180814721>

Consumption proved particularly resilient in the third quarter when real personal expenditures, especially on durable goods, posted sizeable gains despite the onset of the financial market crisis.

**... but the labour market
has softened**

Looking through the short-term fluctuations, there are nevertheless some signs that the labour market, which supported the past gains in household income, has been gradually softening. Private employment has slowed down from the second-quarter pace, with job losses in manufacturing, construction and financial services, and the unemployment rate has edged up slightly.

**The external sector
has also helped**

Foreign trade has also contributed positively to economic activity earlier this year, as exports seem to have benefitted from a pick-up in

United States: **Demand and output**

	2004	2005	2006	2007	2008	2009
	Current prices \$ billion	Percentage changes, volume (2000 prices)				
Private consumption	8 195.9	3.2	3.1	2.9	1.8	1.9
Government consumption	1 844.1	0.8	1.4	2.0	2.4	2.1
Gross fixed investment	2 202.8	5.8	2.6	-2.1	-1.2	2.4
Public	372.8	0.6	3.7	2.5	2.9	2.1
Residential	675.5	6.6	-4.6	-17.2	-15.4	2.1
Non-residential	1 154.5	7.1	6.6	4.7	3.7	2.6
Final domestic demand	12 242.7	3.3	2.7	1.8	1.4	2.0
Stockbuilding ¹	58.6	-0.2	0.1	-0.3	0.1	0.0
Total domestic demand	12 301.3	3.1	2.8	1.6	1.5	2.0
Exports of goods and services	1 182.4	6.9	8.4	8.1	8.6	6.5
Imports of goods and services	1 797.8	5.9	5.9	2.1	3.4	4.3
Net exports ¹	- 615.4	-0.2	-0.1	0.5	0.4	0.1
GDP at market prices	11 685.9	3.1	2.9	2.2	2.0	2.2

Note: National accounts are based on official chain-linked data. This introduces a discrepancy in the identity between real demand components and GDP. For further details see *OECD Economic Outlook Sources and Methods*, (<http://www.oecd.org/eco/sources-and-methods>).

1. Contributions to changes in real GDP (percentage of real GDP in previous year), actual amount in the first column.

Source: OECD Economic Outlook 82 database.


StatLink  <http://dx.doi.org/10.1787/158224000726>

United States: **External indicators**

	2005	2006	2007	2008	2009
\$ billion					
Goods and services exports	1 309.4	1 467.6	1 642.6	1 838	1 992
Goods and services imports	2 024.0	2 229.6	2 350.8	2 539	2 688
Foreign balance	- 714.6	- 762.0	- 708.2	- 701	- 696
Invisibles, net	- 40.3	- 49.5	- 60.5	- 74	- 98
Current account balance	- 754.8	- 811.5	- 768.7	- 775	- 794
Percentage changes					
Goods and services export volumes	6.9	8.4	8.1	8.6	6.5
Goods and services import volumes	5.9	5.9	2.1	3.4	4.3
Export performance ¹	- 1.3	- 0.8	1.3	0.7	- 1.0
Terms of trade	- 2.5	- 0.6	0.3	- 1.3	0.2

1. Ratio between export volume and export market of total goods and services.

Source: OECD Economic Outlook 82 database.

StatLink  <http://dx.doi.org/10.1787/158242464742>

foreign demand and the weakening of the dollar. The improvement in the international trade balance led to a decline in the current account deficit to 5.5% of GDP, having peaked at 6.5% last year.

The Fed lowered its policy rate...

The disruptions in financial markets and concerns about a credit crunch prompted the Federal Reserve to lower the federal funds rate from 5¼ per cent to 4¾ per cent in September and to 4½ per cent, slightly below neutral, in October. This easing should be viewed as a recalibration of policy to offset tighter financial conditions and keep the economy on a sustainable growth path, and therefore seems unlikely to affect adversely the outlook for inflation. Over the past few months, food and energy prices have pushed headline inflation well above 3%. Core inflation, however, seems to have stabilized near 2% and, given the projected slowdown in economic activity, inflationary pressures should remain relatively subdued.

... while room for fiscal manoeuvre is limited

Despite the recent improvements in the budget balance of the federal government, the room for fiscal manoeuvre is limited since revenue growth seems likely to ease with the slowdown in the economy and the flattening of asset prices. Therefore, while automatic stabilizers should provide some support to government expenditures, increases in discretionary spending, including widespread support for distressed borrowers, do not seem warranted. Moreover, the retirement of the first cohort of baby boomers next year should serve as a reminder of the need for reforming the entitlement programmes.

Growth is likely to fall well below potential...

With a limited role for policies, the outlook for growth is mostly driven by developments in residential construction and the flow-on effect on private consumption. Construction activity is projected to continue declining until the middle of next year as homebuilders, in the face of weaker demand amid a reduction in the availability of mortgage credit, will cut housing starts dramatically to prevent the accumulation of

unwanted inventories. Furthermore, private consumption should slow down considerably next year in response to lower housing wealth, weaker labour market conditions, higher energy prices and reduced confidence. All in all, GDP growth should decline to well below potential in 2008, easing inflationary pressures but also causing the unemployment rate to temporarily rise above 5%. In 2009, an end to the decline in residential investment and the dissipation of the effects of the financial turmoil should lead to a renewed pick-up in economic activity.

... contributing to stabilising the current account deficit...

The projected deceleration of household spending should restrain demand for foreign goods and services. In addition, export growth is projected to slow down only moderately from its recent fast pace, as the weaker dollar continues to support demand for exports. The improvement in the current account deficit is however limited by the deterioration of the income balance, which is predicted to turn negative in the first half of 2009 as the US net investment position continues to worsen.

... but risks are on the downside

The above projection is subject to substantial downside risks, as the financial turmoil and the housing slump may cause greater disruption to real activity than foreseen. For instance, a more pronounced decline in asset prices or a greater reaction of households to the projected change in wealth may further restrain consumer spending. Moreover, financial institutions may face greater difficulties managing their balance sheets, and the resulting credit crunch could quickly lead to a contraction of aggregate demand. But there are also upside risks. Above all, the resilience of US consumers could surprise again, especially if stronger labour market outcomes were to support healthy gains in real disposable income.

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This book has...



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Conventional signs

\$	US dollar	.	Decimal point
¥	Japanese yen	I, II	Calendar half-years
£	Pound sterling	Q1, Q4	Calendar quarters
€	Euro	Billion	Thousand million
mb/d	Million barrels per day	Trillion	Thousand billion
..	Data not available	s.a.a.r.	Seasonally adjusted at annual rates
0	Nil or negligible	n.s.a.	Not seasonally adjusted
-	Irrelevant		

Summary of projections

	2007	2008	2009	2007		2008				2009				Fourth quarter		
				Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2007	2008	2009	
Per cent																
Real GDP growth																
United States	2.2	2.0	2.2	1.3	1.1	1.5	1.8	1.9	2.2	2.5	2.7	2.8	2.6	1.6	2.5	
Japan	1.9	1.6	1.8	1.7	1.5	1.6	1.7	1.8	1.8	1.9	1.9	1.9	1.3	1.7	1.9	
Euro area	2.6	1.9	2.0	1.7	1.8	1.9	2.0	2.0	2.0	2.0	2.0	2.0	2.2	1.9	2.0	
Total OECD	2.7	2.3	2.4	2.0	1.9	2.0	2.2	2.3	2.5	2.6	2.7	2.7	2.6	2.1	2.6	
Inflation																
United States	2.6	2.1	2.0	2.4	2.5	2.0	1.9	1.9	2.1	1.9	1.9	2.0	2.5	2.1	2.0	
Japan	-0.5	-0.3	0.3	-1.0	-0.2	0.1	0.1	0.3	0.3	0.4	0.5	0.5	-0.8	0.1	0.4	
Euro area	2.2	2.2	2.3	2.3	2.3	2.2	2.2	2.2	2.3	2.3	2.3	2.3	2.4	2.2	2.3	
Total OECD	2.3	2.1	2.1	2.3	2.3	2.1	2.1	2.0	2.1	2.0	2.0	2.1	2.4	2.1	2.1	
Unemployment rate¹																
United States	4.6	5.0	5.0	4.8	4.8	4.9	5.0	5.1	5.1	5.0	5.0	4.9	4.8	5.1	4.9	
Japan	3.8	3.7	3.6	3.8	3.8	3.8	3.7	3.7	3.7	3.6	3.5	3.5	3.8	3.7	3.5	
Euro area	6.8	6.4	6.4	6.5	6.5	6.5	6.4	6.4	6.4	6.4	6.4	6.4	6.5	6.4	6.4	
Total OECD	5.4	5.4	5.3	5.4	5.4	5.4	5.3	5.3	5.3	5.3	5.3	5.2	5.4	5.3	5.2	
World trade growth																
	7.0	8.1	8.1	8.2	8.0	8.0	8.0	8.0	8.1	8.2	8.2	8.2	7.7	8.0	8.2	
Current account balance²																
United States	-5.6	-5.4	-5.3													
Japan	4.7	4.8	5.2													
Euro area	0.2	-0.1	-0.2													
Total OECD	-1.4	-1.4	-1.4													
Cyclically-adjusted fiscal balance³																
United States	-3.0	-3.4	-3.4													
Japan	-3.4	-3.9	-3.6													
Euro area	-0.6	-0.6	-0.4													
Total OECD	-2.0	-2.2	-2.1													
Short-term interest rate																
United States	5.3	4.6	4.7	5.0	4.8	4.6	4.6	4.6	4.6	4.6	4.7	4.8				
Japan	0.7	0.6	0.9	0.8	0.7	0.6	0.6	0.6	0.7	0.8	0.9	1.2				
Euro area	4.3	4.2	4.1	4.7	4.4	4.2	4.1	4.1	4.1	4.1	4.1	4.1				

Note Real GDP growth, inflation (measured by the increase in the GDP deflator) and world trade growth (the arithmetic average of world merchandise import and export volumes) are seasonally and working-day-adjusted annual rates. The "fourth quarter" columns are expressed in year-on-year growth rates where appropriate and in levels otherwise. Interest rates are for the United States: 3-month eurodollar deposit; Japan: 3-month certificate of deposits; euro area: 3-month interbank rate.

Assumptions underlying the projections include:

- no change in actual and announced fiscal policies;
- unchanged exchange rates as from 12 November 2007; in particular 1\$ = 109.38 yen and 0.69 euros;

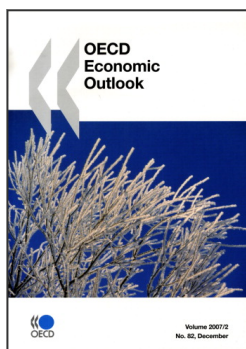
The cut-off date for other information used in the compilation of the projections is 20 November 2007.

1. Per cent of the labour force.

2. Per cent of GDP.

3. Per cent of potential GDP.

Source: OECD Economic Outlook 82 database.



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