

PODCAST  
PRESENTATION

COMING OUT OF THE DOWNTURN: PART 2  
IS THE WORST OVER?

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**TONY:** Hello, I'm Tony McMahon, and I am here today on behalf of Northern Trust to speak to Paul Kasriel Northern Trust's Chief Economist. Paul's forthright views and expert opinions make him one of the most sought after economic commentators in the industry.

Paul, let's turn first to the current state of the US economy. You say that while there is not much growth to observe the worst may nevertheless be over. What's driven you to that conclusion?

**PAUL:** Well I think the worst is over for housing. We are seeing that the ratio of house prices to household income is at a record low. It was only a couple of years ago when that ratio was at a record high. We are seeing that the mortgage rate is the lowest it's been in 40 years or so. We are seeing, for the first time really, that housing sales for single-family homes are approximately equal to sales of new single-family homes. So supply and demand are coming into relationship with each other. So in many senses today, housing is more affordable than it has been in 40 or 50 years.

Now, I won't say it's more affordable than it was a couple of years ago when you didn't need a job to qualify for a mortgage. You need a job, you have to make a down payment. But in more traditional terms housing is very affordable. So I think we are near a bottom there. We are now sending to the scrap yard more cars and trucks than we are putting new ones on the highway. So we are near a bottom in automobile and in truck sales.

And we have the Federal Government starting to gear up its Fiscal Stimulus Program. This really hasn't been a big factor, but it will be going forward especially in the second half. So there are some signs of stabilization in some very weak sectors, and we do have this Government Fiscal Stimulus coming on now.

**TONY:** You touched on the housing sector there, real estate agents have obviously been saying for a long time that the current market is a buying opportunity for a while. But is this now really true?

**PAUL:** Well real estate agents always call it a buying opportunity. But it is true now. Again, given the level of mortgage rates, given how much house prices have fallen, housing is very affordable today. It's not to say that house prices may not fall some more. But again the worst is over for house price declines. And if you can make a down payment housing is now very attractive.



**TONY:** US consumer spending patterns are proving to be quite interesting. We've seen a rise in the first quarter; you're expecting that to dip again in the second quarter and then recover again in the third and fourth quarters. Will we then see, do you think, a long-term recovery in consumer confidence?

**PAUL:** Well consumer confidence is definitely recovering. Unfortunately consumer confidence is not a very good forecaster of consumer spending. We saw a very sharp decline in consumer spending in the second half of 2008. And, I think that there was some pent up demand which led to the increase in the first quarter. Also I mentioned the car and truck sales kind of stabilised in the first quarter.

But the unemployment rate continues to rise. The unemployment rate is probably going to rise through the first half of 2010. And that is going to have a negative impact on consumer spending for the next several quarters. But there again the worst is over. In other words the largest rates of contraction occurred in the second half of 2008. And now, I think, we'll just see some rather minor contractions in the second and third quarter. In fourth quarter we'll see some actual growth again, even better than what we saw in the first quarter.

**TONY:** Assuming then that there is a recovery in the US economy the feel good factor may nevertheless take some time to trickle down to those without jobs. When would you expect the labor market to perk up?

**PAUL:** You know we are seeing signs of the labor market stabilizing now. Every week people file for new unemployment insurance claims. And those claims are now starting to trend lower. I think there are going to be some interruptions when GM closes down. But those are some positive signs. I don't think we are going to see an actual increase in employment until maybe the fourth quarter of this year. And again I don't think we are going to see a decline in the unemployment rate until the second half of 2010.

**TONY:** But what about the availability of credit that's obviously key to any sustained recovery? How do you see things developing there?

**PAUL:** We are starting to see credit markets thaw. We are starting to see this happen in the inner bank market, bank 'A' will now lend to bank 'B'. In part, because the Federal Government in the United States has said that bank 'B' is not going to fail, so you can rest assured that it will open tomorrow morning.

We are starting to see credit rates come down in a lot of other markets. In fact, in the mortgage market we are seeing spreads of mortgage rates over treasury rates back to their normal levels now. So we are seeing thawing. For the most part the credit markets are not anywhere near back to normal, but progress is being made.

Now I think a very important program to hasten the re-opening of the credit markets would be the Federal Reserves Term Asset-Backed Securities Loan Facility, known as TALF. This is a program whereby the Fed will lend to purchasers of asset-backed securities such as securities backed by credit card receivables, auto loan receivables. Now the Fed will lend to these purchasers at very attractive rates, and the Fed will accept a

good bit of the credit risk. This program is now beginning to develop some forward momentum. It's been slow getting started. This is a very important program to re-start the flow of credit.

**TONY:** So if we do see a speedy exit to this recession do you think we can thank the Federal Reserve and the Administration for this rapid turnaround of events?

**PAUL:** Well you say relatively quickly exit from this recession, this is the longest recession in the post-war era. I think the Federal Reserve deserves most of the credit. The Federal Reserve was established in 1913 by an Act of Congress with the primary mission of extending credit to banks that were having temporary funding difficulties. The Fed has been very aggressive in this.

And the Fed has also been creative in really expanding its mission to try to re-start the flow of credit to the private sector, not only through this TALEF programme but also purchasing mortgage-backed securities in the market. So the Fed has been aggressive and that has helped stabilize the financial markets. In addition for all its problems, the Treasury's TARP program, I think, played a role in stabilising the markets.

Now going forward with this Fiscal Stimulus Program, in conjunction with the Federal Reserve following a very accommodative policy, I think that's going to hasten the end of this recession.

**TONY:** Thank you Paul.


**PAUL:** Thank you Tony.

**TONY:** More great insight and perspective there from Northern Trust's Chief Economist. If you'd like to read and hear more from Paul then log onto [northertrust.com](http://northertrust.com), but for now, thank you and goodbye.

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