

**US Economic Outlook:  
Is the Recovery Sustainable?**

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**I Recovering From Recession**

- A Recovery Is Underway, But the Pace of Growth Is Likely to Moderate
- The Composition of Economic Growth Is Improving
- No Need for Additional Stimulus at this Time

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## II Transitioning From Government to Private Demand

- Consumer Confidence Is Stabilizing
- But Employment and Incomes Are Lagging
- Businesses Have Cash to Invest
- Housing Appears to Have Bottomed
- Commercial Real Estate Still Struggling

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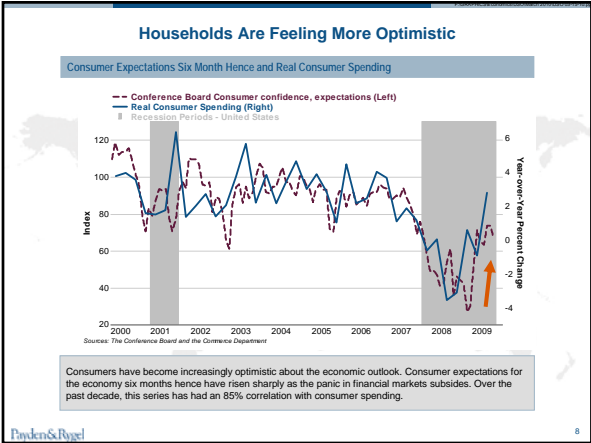
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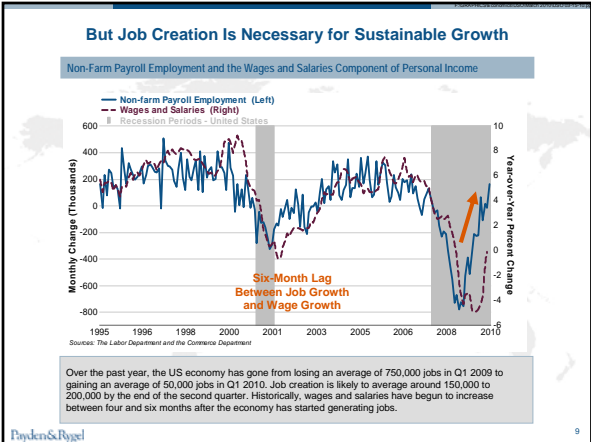
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III Policy Error Remains Greatest Risk

- Fears About Inflation Are Overblown
- Timing the First Fed Rate Hike
- Higher Taxes and Interest Rates Are Likely in the Future
- Learning from Past Mistakes

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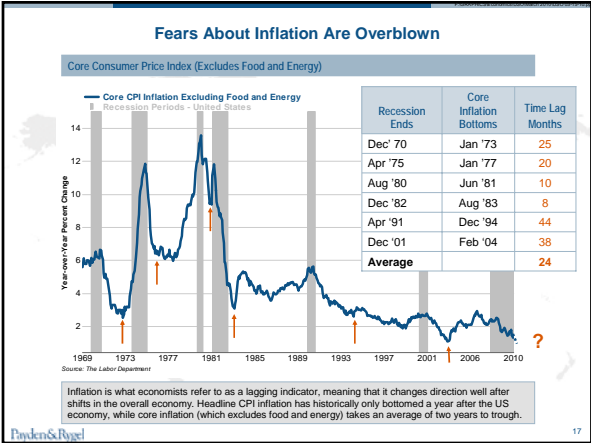
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### The Biggest Risk Is A Policy Mistake

**Short-Term Risk: Early Exit Similar to 1930s**

**1937 Tax Hike**

- After abandoning the gold standard, US GDP growth rose at a double digit pace between 1934 and 1937. However, the absolute level of GDP was still 10% lower than it was in 1929. Nevertheless, taxes were increased with the establishment of the Social Security Program in 1937.

**Reserve Requirement**

- To add insult to injury, the Federal Reserve doubled its reserve requirements that year, fearing a return of inflation. The result was a deep recession over the next two years.

**Long-Term Risk: Late Exit Similar to 2004**

**Rates Too Low for Too Long**

- The Fed lowered interest rates to their lowest levels in decades to offset deflationary forces following the bursting of the technology bubble. The Fed was reluctant to raise interest rates even after the US economy began to recover.

**Asset Bubble Develops**

- Investment banks leverage up 30:1 on their capital and increased the availability of credit to consumers. Household debt to income soared to unprecedented levels. Housing bubble ensues.



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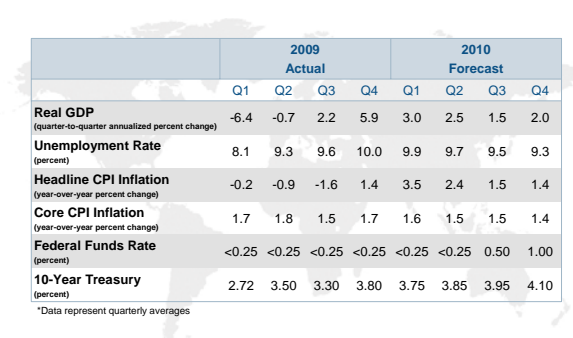
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### 2009-2010 Base Line US Economic Forecast\*

	2009 Actual				2010 Forecast			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
<b>Real GDP</b> <small>(quarter-to-quarter annualized percent change)</small>	-6.4	-0.7	2.2	5.9	3.0	2.5	1.5	2.0
<b>Unemployment Rate</b> <small>(percent)</small>	8.1	9.3	9.6	10.0	9.9	9.7	9.5	9.3
<b>Headline CPI Inflation</b> <small>(year-over-year percent change)</small>	-0.2	-0.9	-1.6	1.4	3.5	2.4	1.5	1.4
<b>Core CPI Inflation</b> <small>(year-over-year percent change)</small>	1.7	1.8	1.5	1.7	1.6	1.5	1.5	1.4
<b>Federal Funds Rate</b> <small>(percent)</small>	<0.25	<0.25	<0.25	<0.25	<0.25	<0.25	0.50	1.00
<b>10-Year Treasury</b> <small>(percent)</small>	2.72	3.50	3.30	3.80	3.75	3.85	3.95	4.10

\*Data represent quarterly averages



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- ### IV Investment Opportunities
- US Corporate Bonds Are Still Attractive
  - Emerging Market Stocks and Bonds Offer Good Long-Term Value
  - Municipal Bonds Offer Some Protection from Higher Taxes
  - US Dollar Likely to Weaken Against Asian Currencies
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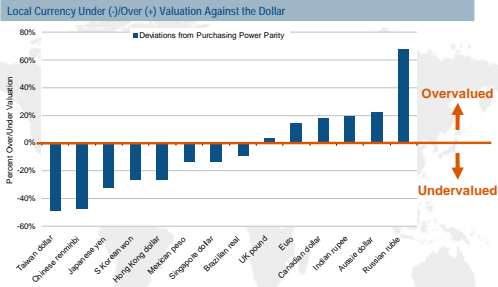
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### The Dollar Faces Further Weakness Against Asian Currencies



The law of one price states that identical goods should cost the same across borders. When a discrepancy between price levels develops, a country's currency should adjust to restore purchasing power parity (PPP). At the present time, several currencies in developing Asia appear undervalued on a purchasing power parity basis.

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#### Important Disclosures

Historical performance data represents past performance and does not guarantee future results. Investments in bonds are subject to certain risks such as interest rate, issuer, and inflation risk. Investments may be worth less than their original cost when sold.

Investment in foreign securities entails certain risks from investing in domestic securities, including changes in exchange rates, political changes, differences in reporting standards, and, for emerging-market securities, higher volatility.

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