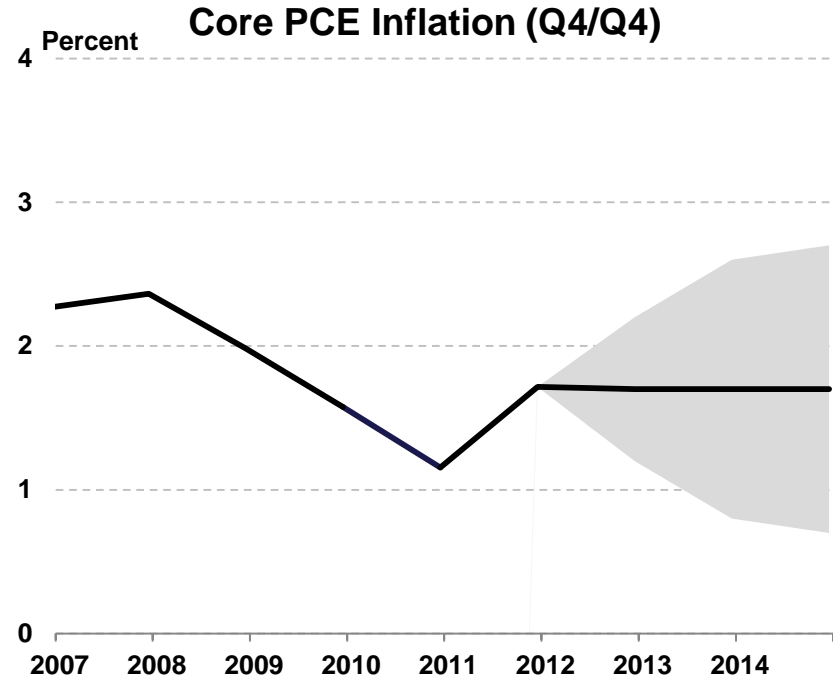
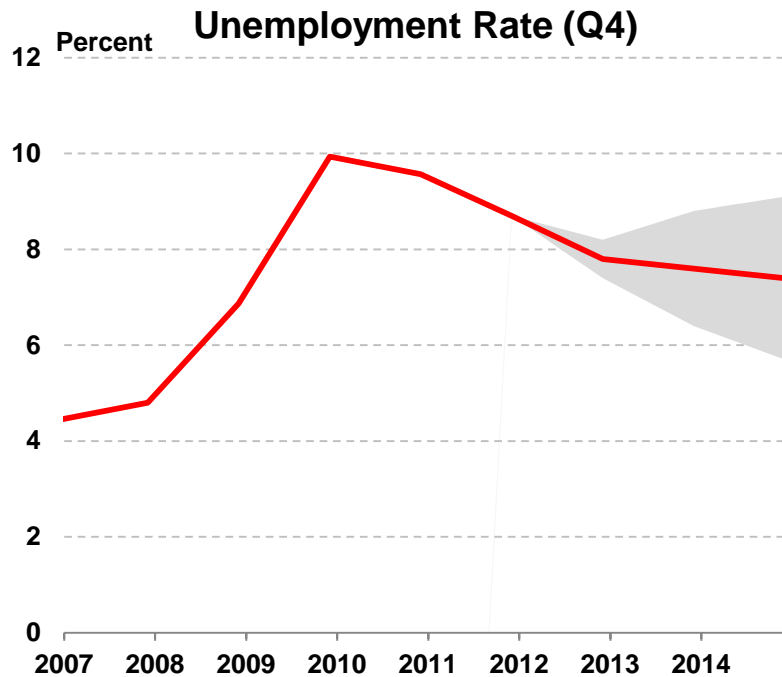

The Outlook for the U.S. Economy After the Election

David J. Stockton

November 8, 2012



U.S. Forecast Overview



Forecast	2012	2013	2014
Real GDP Growth (Q4/Q4)	1.6	2.3	2.8
Unemployment (Q4)	7.8	7.6	7.4
PCE Price Inflation (Q4/Q4)	1.8	1.4	1.7
Core PCE Price Inflation (Q4/Q4)	1.7	1.7	1.7

Policy Assumptions

Fiscal Policy – No cliff, just a short-term resolution

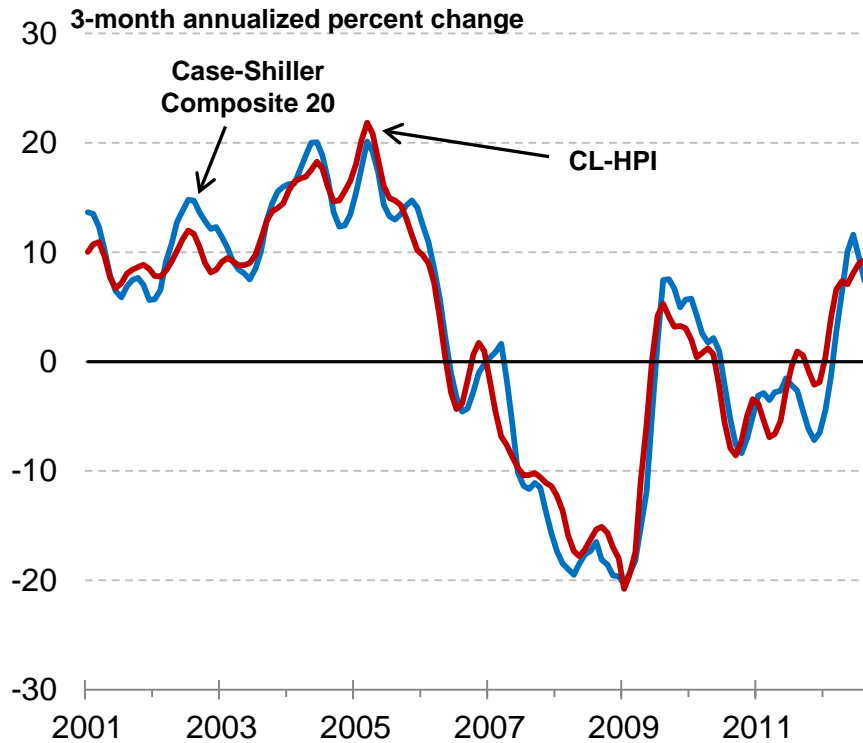
- **Drag from falling real government consumption and gross investment**
 - Direct drag of $\frac{1}{2}$ pp in 2013
 - Plus multiplier effects
- **Payroll tax holiday and emergency unemployment benefits expire in 2013**
 - Dynamically trims $\frac{1}{2}$ pp from growth
- **Assumed income tax increases in 2013 – about \$50b/year**
- **All in, implies roughly $1\frac{1}{2}$ percentage point of drag in 2013**

Monetary Policy

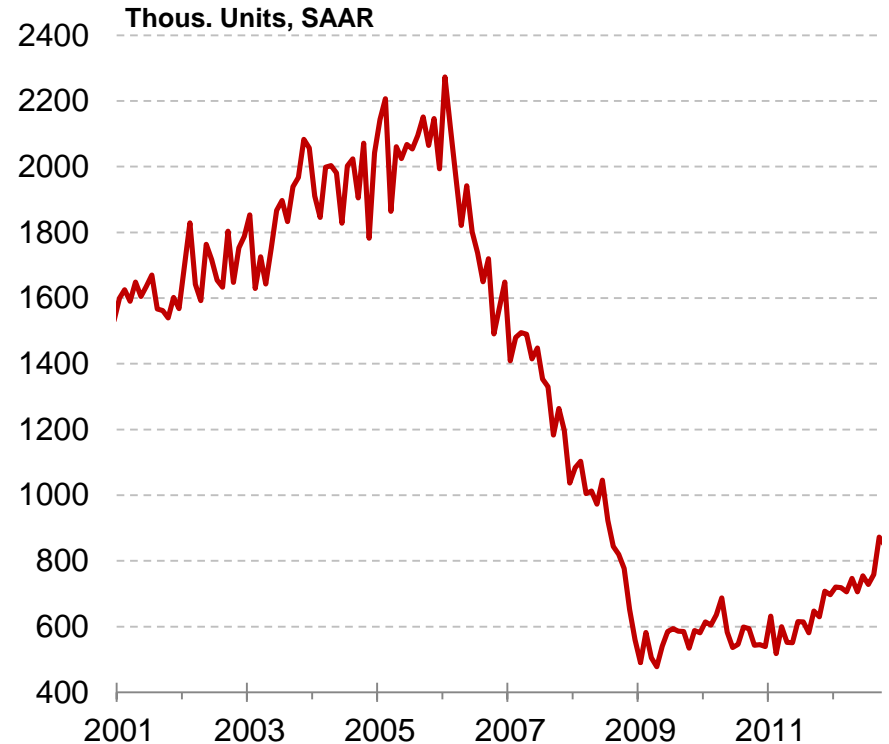
- **QE3 of \$900 billion of purchases into late 2013**
- **Extended guidance maintained**

Housing Recovery: Finally Under Way?

House Prices



Private Housing Starts



Source: Haver Analytics

The Fiscal Cliff

(fiscal year 2013; billions of dollars)

Revenues

Expiration of income tax cut and AMT indexation	+ 221
End of payroll tax reduction	+ 95
Other expirations	+ 65
Taxes in Affordable Care Act	+ 18

Other

+ 105

Spending

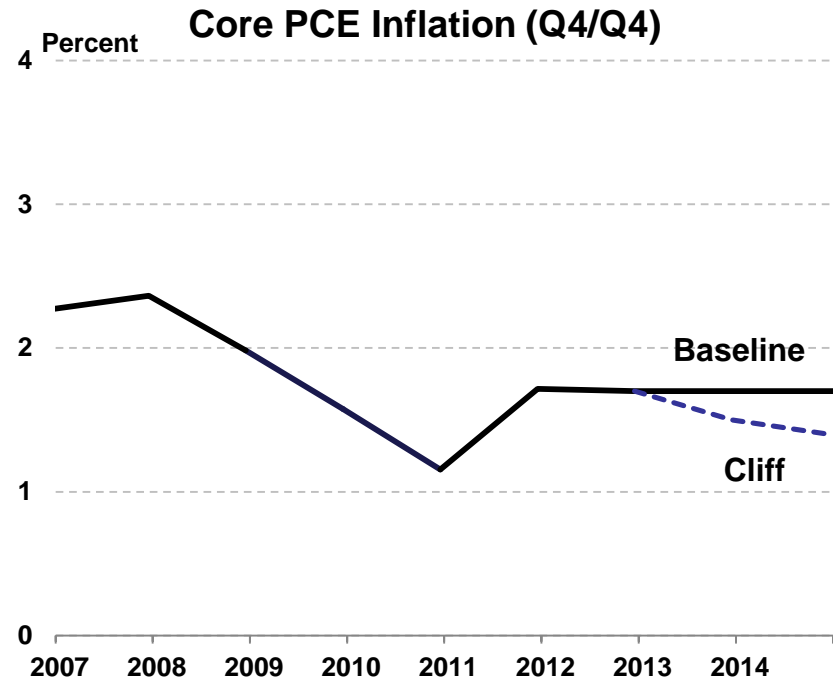
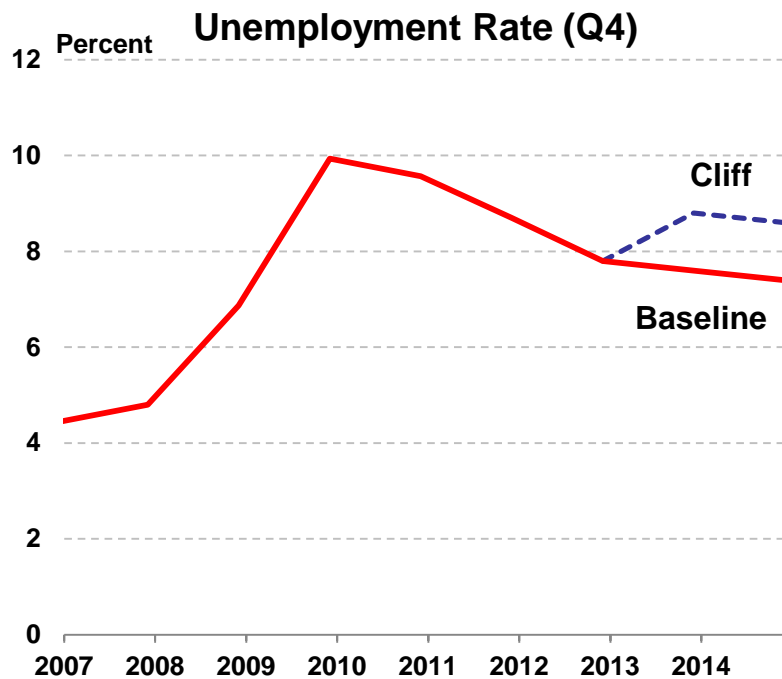
Automatic cuts	+ 65
Expiration of UI Benefits	+ 26
Reduced Medicare payments to physicians	+ 11

Grand Total: + 607

The Problem: Going Over the Cliff will be Costly

- **The Fiscal Multiplier is Larger than Generally Thought:**
 - **Zero lower bound amplifies fiscal effects**
 - **The multiplier is likely state dependent...larger when there is considerable slack**
 - **More liquidity constrained households at present**
 - **More financial stress**
 - **Effects on confidence likely to be negative**

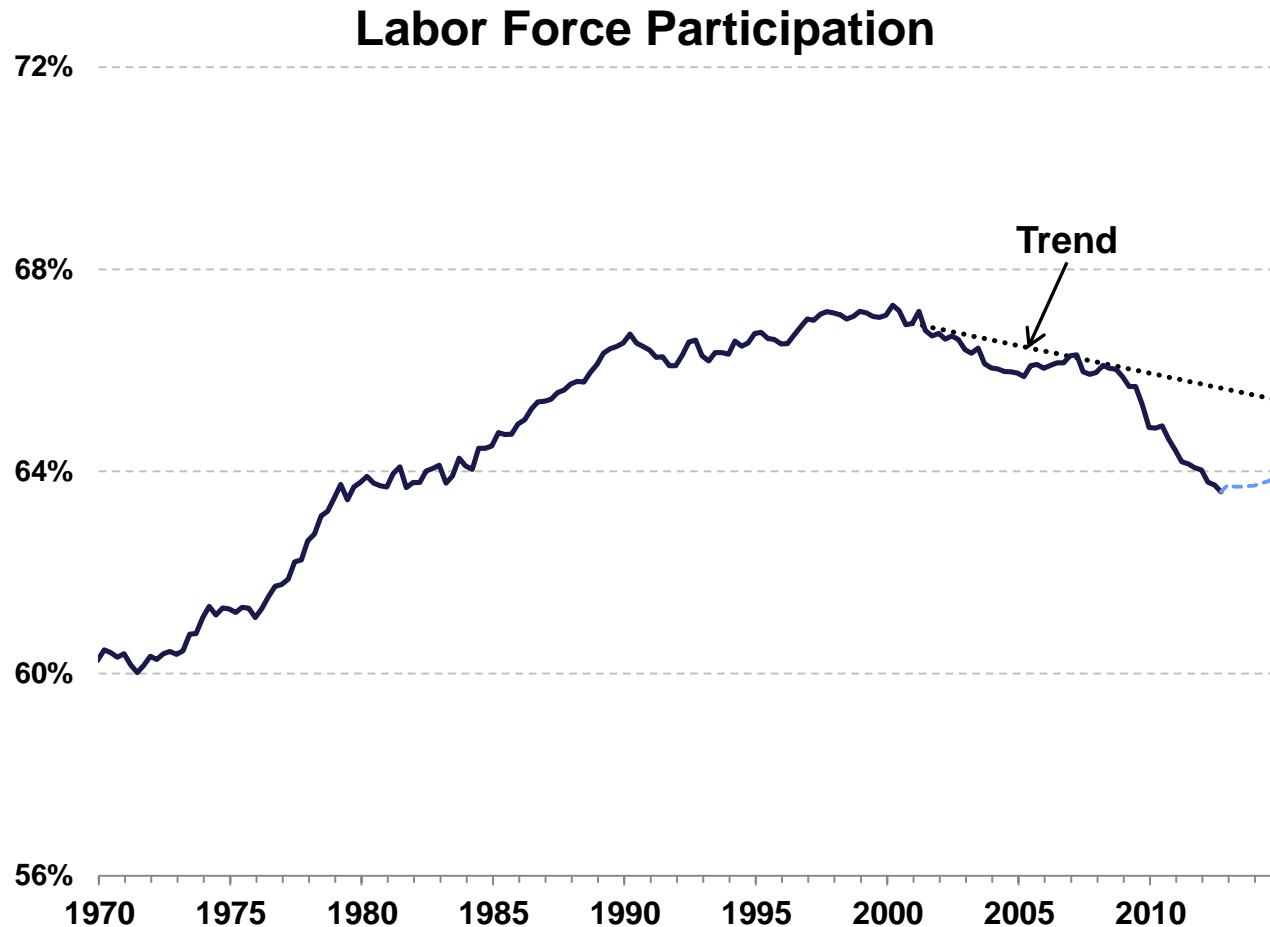
Going Over the Fiscal Cliff



Forecast – Over the Cliff

	2012	2013	2014
Real GDP Growth (Q4/Q4) (Baseline)	1.6 (1.6)	-0.5 (2.3)	3.2 (2.8)
Unemployment (Q4) (Baseline)	7.8 (7.8)	8.8 (7.6)	8.6 (7.4)

The Decline in Labor Force Participation: How much is secular vs. cyclical?



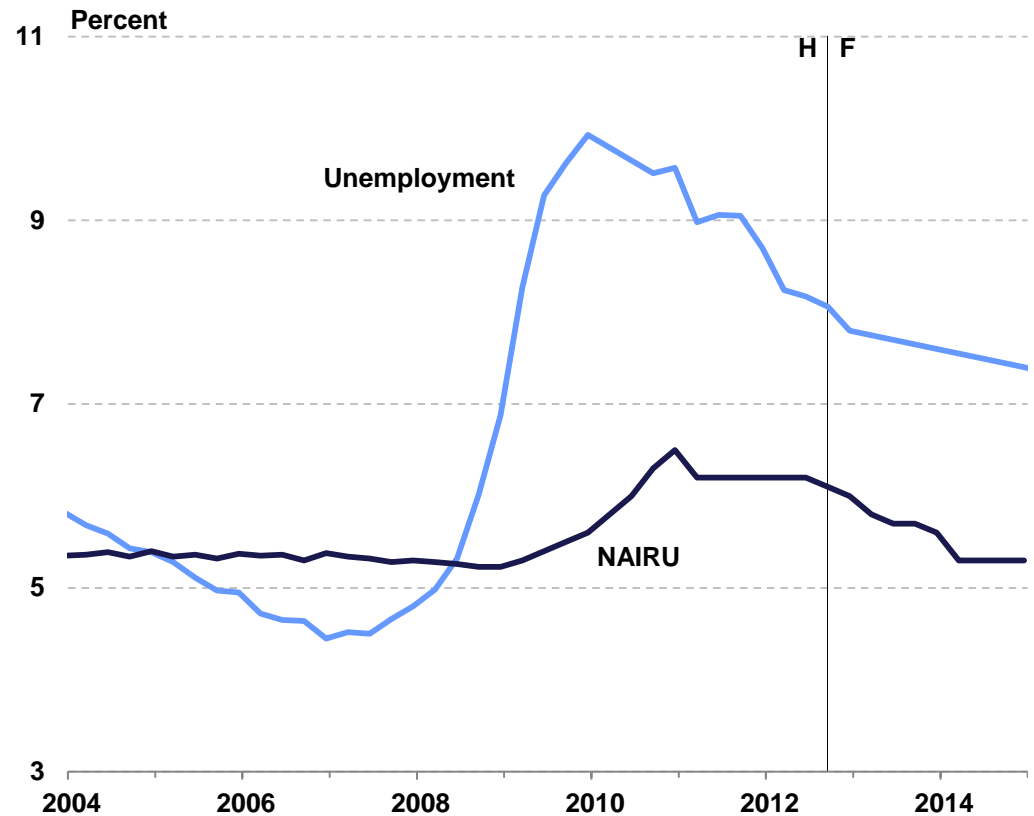
Source: Haver Analytics

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The Bottom Line on Labor Market Slack

FOMC's Estimate Of Longer-Run Unemployment

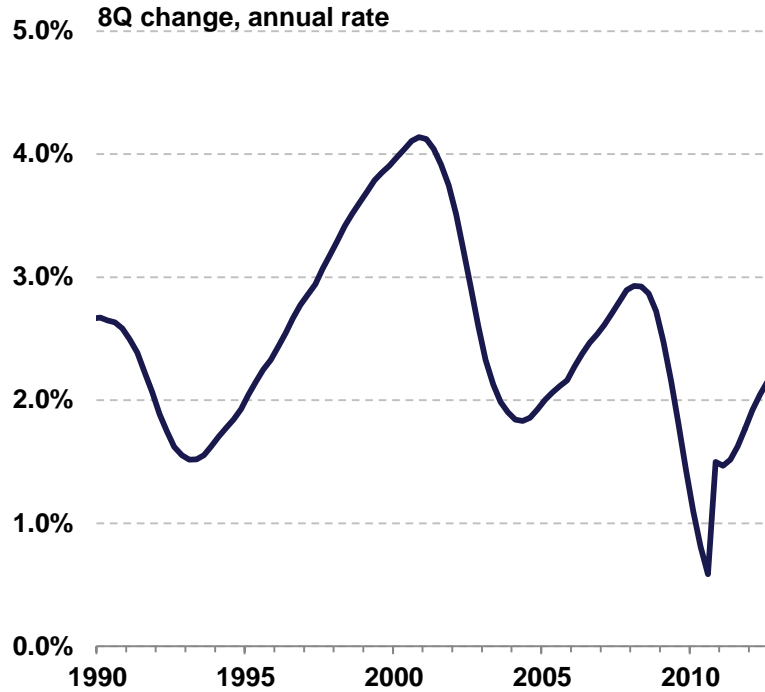
June 2009	5.1
June 2010	5.1
June 2011	5.5
June 2012	5.5



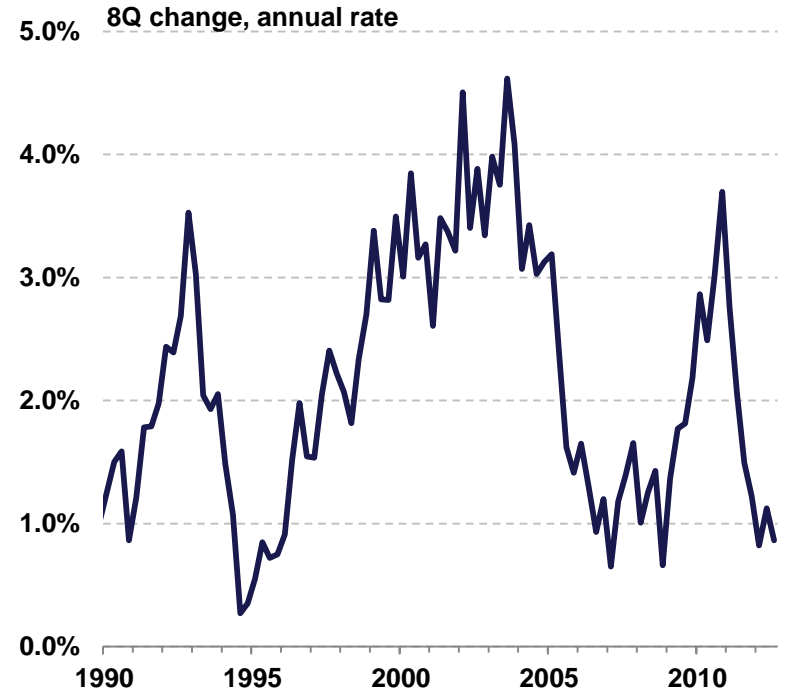
Source: Haver Analytics, Federal Reserve

Productivity

Growth of the Business Capital Stock



Growth of Nonfarm Business Labor Productivity



Source: Haver Analytics