

## *Highlights from the December 10, 2010 meeting*

### **This is Not Your Father's Business Cycle**

#### **An Economist Analyzes the Great Recession and Its Aftermath**

What got us into this mess? How far have we climbed to get out of it? What's the outlook for 2011?

Those were among the questions probed by Paul Kasriel, Senior Vice President & Chief Economist for Northern Trust, our featured speaker for December. He provided the largest ACG WI lunch meeting audience ever with perspectives on the state of the U.S. and world economies.

Paul is one of the few reputable economists who foresaw the housing bubble and the inevitable economic collapse. He doesn't believe that this problem was the result of faulty government policies. Rather, it was generated by the financial system—and the commercial banking system in particular. Their hunger for new mortgage deals, and the crazy structure of these deals, eventually created a capital shortage for banks once the bubble burst and the wave of mortgage delinquencies began.

The erosion of bank capital due to defaults produced a reluctance (and real inability) for banks to lend. In fact, 2008 was only the second year in U.S. history that bank credit contracted.

For the past two years, the U.S. government and the Federal Reserve have been trying desperately to improve the economic environment. Tried and true monetary stimulus policies had no effect. The initial wave of fiscal stimuli also did not have the intended impact. Unfortunately, while the federal government was dramatically increasing spending, consumers were dramatically decreasing their spending, as well as their debt.

As we enter 2011, Paul cited several areas of uncertainty and concern, including:

- A potentially significant increase in defaults of commercial real estate.
- Regulatory capital requirements for financial institutions are likely to be raised, adding to uncertainty in the financial markets and causing banks to continue hoarding cash and capital.
- Excess supply of housing units continuing to hold back this once large part of the U.S. economy.
- Efforts to resolve state and local governmental deficits, which could have a cooling effect on the overall economy.

Fortunately, Paul also left us with several bright spots for 2011:

- A recent Fed survey confirmed that the percentage of banks increasing lending activities has gone up.
- While QE1 did not have the intended effect, it appears the QE2 is working.
- Exports from America are likely to grow significantly, driven by demands from China and Latin America for more food, medical care technologies and other goods.

In other words, Paul said he sees the U.S. going through a fundamental transformation—from an economy driven by consumerism to one led by export-driven growth.

For a copy of the presentation, [click here](#).