



Double-Dip Recession: Previous Experience and Current Prospect

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Summary

Concerns have been expressed that the United States may be about to experience a “double-dip” recession. A double-dip or W-shaped recession occurs when the economy emerges from a recession, has a short period of growth, but then falls back into recession. This prospect raises policy questions about the current level of economic stimulus and whether added stimulus may be needed. The pace of the recovery has been below average and is decelerating, falling from a 5% to a 1.7% annual average rate of growth between the fourth quarter of 2009 and the second quarter of 2010. Other indicators, such as high unemployment, falling house prices, reduced flows of credit, and the prospect of fading fiscal stimulus, are also worrisome.

Double-dip recessions are rare. There are only two modern examples of a double-dip recession for the United States: the recession of 1937-1938 and the recession of 1981-1982. They both had the common attribute of resulting from a change in economic policy. In the first case, recession was an *unintended* consequence of the policy change; in the second case, recession was an *intended* consequence.

Historically, there has been what is termed a “snap back” relationship between the severity of the recession and the strength of the subsequent recovery. In other words, a sharp contraction followed by a robust recovery traces out a V-shaped pattern of growth. However, unlike earlier post-war recessions, the recent recession occurred with a financial crisis. Research suggests that a slow recovery with sustained high unemployment is the norm in the aftermath of a deep financial crisis.

The prelude to the economic crisis in the United States was characterized by excessive leverage (the use of debt to support spending) in households and financial institutions, generating an asset price bubble that eventually collapsed and left balance sheets severely damaged. The aftermath is likely to be a period of resetting asset values, deleveraging, and repairing balance sheets. This correction results in higher saving, weakened domestic demand, a slower than normal recovery, and persistent high unemployment, but not necessarily a double-dip recession.

Several indicators, such as industrial production, business investment spending, and corporate bond yields, together with the prospect of an accommodative monetary policy, point to an economy that is expanding. Weighing these several forces, positive and negative, that are likely to influence economic activity over the near term, most economic projections suggest U.S. economic recovery will continue, albeit at a slower than normal pace.

This report discusses factors suggesting an increased risk of double-dip recession. It discusses other factors that suggest economic recovery will continue. The U.S. historical experience with double-dip recessions is also presented. It examines the role of deleveraging by households and businesses in the aftermath of the recent financial crisis in shaping the likely pace of economic recovery. The report concludes with a look at current economic projections.

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Background

Concern is rising that the United States may be about to experience a “double-dip” recession. A double-dip or W-shaped recession occurs when the economy emerges from a recession, has a short period of growth, but then falls back into recession. This prospect raises policy questions about the current level of economic stimulus and whether added stimulus may be needed.

In the recent recession that began in the last quarter of 2007, real (inflation adjusted) gross domestic product (GDP) fell sharply, down a cumulative 4.3% through the second quarter of 2009. At that point, the economy bottomed out and economic recovery began in June 2009, according to the National Bureau of Economic Research (NBER) Business Cycle Dating Committee (BCDC).¹ Since then, real GDP increased a cumulative 3.7% through the third quarter of 2010.

However, the pace of the recovery has been below average and is decelerating, falling from a 5% annual rate in the fourth quarter of 2009 to a 2.0% annual average rate over the second and third quarters of 2010. In addition, much of the economy’s current momentum stems from the transitory effects of inventory adjustments and fiscal stimulus. This deceleration and the substantial economic weakness that persists from the recession raises concern about the sustainability of the recovery and concern that a second dip into recession is imminent.

This report discusses factors suggesting an increased risk of double-dip recession. It also discusses other factors that suggest economic recovery will continue. The U.S. historical experience with double-dip recessions is also presented. Also examined is the role of deleveraging by households and businesses in the aftermath of the recent financial crisis in shaping the likely pace of economic recovery. The report concludes with a look at current economic projections.

Factors That Suggest Increased Risk of Double-Dip Recession

Some economists see evidence of an increased risk of a double-dip recession. Robert Shiller, professor of economics at Yale University, reportedly thinks the second dip of a double-dip recession “may be imminent,” with the second quarter of 2010 the likely beginning point.² Similarly, Nouriel Roubini, professor of economics at New York University, has reportedly stated that because the outlook for the economy has “materially weakened,” there is a 40% chance of a double-dip recession occurring within the next 12 months.³ They along with some other

¹ National Bureau of Economic Research (NBER) Business Cycle Dating Committee, September 22, 2010, <http://www.nber.org/cycles/sept2010.html>.

² Simon Constable, “Economist Shiller Sees Potential for ‘Double Dip’ Recession,” *Wall Street Journal*, August 28, 2010, at <http://online.wsj.com/article/SB10001424052748704147804575455370525902224.html>.

³ Jennifer Kwan, “Roubini: 40 pct chance of US double-dip recession,” *FOX Business*, September 8, 2010, at <http://www.foxbusiness.com/markets/2010/09/08/roubini-pct-chance-double-dip-recession/print#>.

economists have come to this assessment based in part on the following recent economic indicators:

- In the second and third quarters of 2010, real GDP growth decelerated to only a 2.0% annual rate, a pace that may not be fast enough to keep the unemployment rate from rising. Moreover, without the temporary contributions of inventory adjustments and federal stimulus spending the real economy grew only 0.5% in the third quarter of 2010.⁴ This weak performance was due to below normal rate of consumer spending and a slowing of investment spending.
- After steadily climbing over the previous year, the stock market weakened in the second quarter of 2010. Also since April 2010, yields on medium- and long-term Treasury securities have fallen about a full percentage point (100 basis points) as investors seeking lower-risk securities have bid up their market price.⁵
- Consumer credit continues to fall, down 1.4% in the third quarter of 2010. This weakened flow of credit to households reflects a mixture of demand and supply forces at work, with both timid lenders and consumers playing a role.⁶
- The economy appears to be on the brink of deflation. For the 12 months ending in October 2010, the core inflation rate was 0.6 %—the lowest rate of increase in 44 years. During August, September, and October of 2010, the core inflation rate was 0.0% .⁷ Elevating the risk of deflation are the persistence of a large output gap, below normal growth of the money supply, dollar depreciation, and the nominal federal funds rate being at the zero bound.
- Housing prices continued to decline over the four quarters ending in the second quarter of 2010, continuing to weaken household balance sheets.⁸
- Unemployment remains high, having modestly fallen to 9.8% in November 2010 from the October 2009 high of 10.1%. Slow improvement in the labor market dampens the growth of household income, raises concerns about job security, and weakens consumer confidence—all of which deter current spending.
- Federal fiscal stimulus, under current law, will soon fall rapidly. The Congressional Budget Office (CBO) projects that between FY2010 and FY2011, the federal budget deficit will decline from 9.1% to 4.2% of GDP. That would be the sharpest two-year decline since World War II. Several factors contribute to

⁴ U.S. Department of Commerce, Bureau of Economic Analysis, “National Income and Product Accounts,” news release, September 30, 2010, at http://www.bea.gov/newsreleases/national/gdp/2010/pdf/gdp2q10_3rd.pdf.

⁵ Because a Treasury security pays a fixed dollar amount, there is an inverse relationship between the market price of the security and its effective yield. Therefore, if market demand increases, the price of the security will rise and its effective yield will fall.

⁶ Federal Reserve Statistical Release G. 19, September 8, 2010, <http://www.federalreserve.gov/releases/g19/current/g19.htm>.

⁷ The CPI and other aggregate price indexes are for a number of reasons likely to have an average annual upward bias in the range of 0.5 to 1.0 percentage points. Therefore, measured inflation of less than 1 percentage point makes it likely that the economy is now actually experiencing either zero inflation or mild deflation.

⁸ National Association of Realtors, *Median Sales Price of Existing Single-Family Homes for Metropolitan Areas*, 2nd Quarter 2010, at <http://www.realtor.org/research/research/metroprice>.

the reduced fiscal stimulus. Temporary relief from the alternative minimum tax (AMT) enacted under the American Recovery and Reinvestment Act of 2009 (ARRA; P.L. 111-5) expired last year, but the economic effects will be felt in 2010 and 2011. Also, the stimulative effect of the spending increases enacted under ARRA peaked in the first half of 2010 and will fall off in late 2010 and 2011.⁹

- Tax reductions enacted in the Economic Growth Tax Relief Reconciliation Act of 2001 and the Jobs and Growth and Tax Relief and Reconciliation Act of 2003 are scheduled to expire at the end of 2010.

Historical Experiences with Double-Dip Recession

Double-dip recessions are rare. There are only two modern examples of a double-dip recession for the United States: the recession of 1937-1938 and the recession of 1981-1982. They both have the common attribute of resulting from a change in economic policy. However, in the first case, recession was an *unintended* consequence of the policy change; in the second case, recession was an *intended* consequence of the policy change. Both point to the importance of policy persistence in overcoming difficult economic circumstances.

The 1937-1938 Recession: A Premature Removal of Economic Stimulus

Beginning in 1933, the U.S. economy rebounded from its sharp fall into what has become known as the Great Depression. From 1933 to 1936, supported by expansionary fiscal and monetary policies, the U.S. economy grew briskly at an average rate of 9.0% and unemployment fell from 25% to 14%. Economic output had nearly returned to its level in 1929, but the economy was still well short of full recovery. But in 1937, the recovery halted and the economy tipped into a second recession. Most economists believe that the second dip into recession was caused by an unfortunate premature switch to contractionary monetary and fiscal policies in a still-fragile recovering economy.

On the monetary side, in 1936 the Federal Reserve began to worry about inflation. After several years of relatively loose monetary policy, the U.S. banking system had built up large quantities of reserves in excess of legal reserve requirements. The Fed feared that should the banks begin to lend these excess reserves it could lead to an overexpansion of credit and generate an inflationary surge. In an attempt to sop up those excess reserves, the Fed raised the banks' reserve requirements three times during 1936. However, banks were still nervous about the financial panics of the early 1930s and uncertain about the durability of the economic recovery, and consequently wanted to hold excess reserves as a cushion. In response to the higher reserve requirements erasing that cushion, the banks worked to rebuild it by reducing lending, leading to a contraction of credit-supported spending.

⁹ Congressional Budget Office, *The Budget and Economic Outlook:an Update*, August 2010, at <http://www.cbo.gov/ftpdocs/117xx/doc11705/08-18-Update.pdf>.

On the fiscal side, by 1936, following several years of large budget deficits, the federal government had a strong urge to declare victory and get back to normal policy—specifically balancing the government budget. The veterans bonus that was paid in 1936 was not renewed in 1937; in addition, Social Security taxes were collected for the first time in 1937. The overall effect was a fiscal contraction equal to about 3% of GDP.

The double hit of contractionary monetary and fiscal policy in an economy that had still not reached the point where private demand was capable of fully sustaining economic growth led to a recession. In 1938, GDP fell 4.5% and the unemployment rate increased to 19%.¹⁰

Economic policy quickly changed course and recovery resumed in the second half of 1938, but the policy error added about two years to the Great Depression, which ended with the step-up in war-time spending in 1941.

The 1981-1982 Recession: A Policy of Disinflation

By the end of the 1970s, inflation had become a major economic problem for the United States. Since the mid-1960s, as measured by the consumer price index (CPI), inflation had steadily ratcheted up from an annual rate of less than 2% to more than 13% by the end of 1979. In the fall of 1979, Paul Volcker, recently appointed to the Fed chairmanship, initiated a policy of *disinflation*—a reduction of the rate of inflation. Applying an aggressive contractionary monetary policy, the Fed progressively increased the federal funds rate from about 11% in the summer of 1979 to nearly 18% by the spring of 1980.

Economic growth had been sluggish in 1979 because of the effects of the second OPEC-induced petroleum price shock, but with the added negative impact of a contractionary monetary policy, the economy tipped into a short recession that lasted from January through July of 1980. However, despite the recession the rate of inflation hardly budged. It fell from an annual rate of 14.6% in the spring of 1980 to an only slightly lower rate of 13% in the fall of that year.

The economic recovery that commenced in the second half of 1980 would be short lived, lasting only through the first quarter of 1981. Because the Fed was determined to wring inflation out of the economy, it applied a second, stronger dose of contractionary monetary policy beginning in the fourth quarter of 1980. The federal funds rate, which had fallen to around 9% during the 1980 contraction, would be steadily increased by the Fed to more than 19% by mid-1981. The sharp increase of interest rates again tipped the economy into what would this time be a longer recession, lasting through the third quarter of 1982.

During this second dip, the rate of inflation did fall sharply, decreasing to below 3.5% by early 1983. Successful disinflation came at a significant cost: a 2.7% contraction of real GDP and an unemployment rate that would be pushed to a peak of 10.8% in November of 1982 and remain above 10% through the first half of 1983.

¹⁰ For further discussion of the recession of 1937, see Christina D. Romer, “The Nation in Depression,” *Journal of Economic Perspectives* 7 (spring 1993), pp. 19-39; Milton Friedman and Anna D. Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton, NJ: Princeton University Press, 1963); Francois R. Velde, “The Recession of 1937—A Cautionary Tale,” *Economic Perspectives*, Federal Reserve Bank of Chicago, fourth quarter 2009, pp. 16-36.

The Typical Pattern of Post-War Recoveries

The annual rate of growth of real GDP in the first year of recovery after a recession has averaged 6.4%. This compares to a 3.0% rate of growth of real GDP during the first year of the current recovery.

Historically, there has been what is termed a “snap back” relationship between the severity of the recession and the strength of the subsequent recovery. In other words, a sharp contraction is followed by a robust recovery tracing out a V-shaped pattern of growth. Having deferred spending during the contraction, households and businesses have typically increased purchases quickly as economic conditions improved.

Excess capacity and high unemployment generated during the recession typically means that for the near term the normal supply constraints do not apply, allowing the economy to grow faster than its long-term trend (real GDP advancing at a 2.5% to 3.0% annual rate). The more slack, the greater the possibility for above normal growth. As the recovery matures and the economy approaches full employment and high rates of capacity utilization, growth slows to the economy’s trend rate of growth that is governed by growth of the labor force and productivity.

Prior to the recent recession, the three sharpest contractions, as measured by the cumulative fall of real GDP, occurred in the recessions of 1981-1982, 1973-1975, and 1957-1958. In 1981-1982, the cumulative decline of real GDP was 2.7% and the increase in the first year of recovery was 7.7%; in 1973-1975, the cumulative decline was 2.8% and the subsequent increase was 6.1%; in 1957-1958, the cumulative decline was 3.7% and subsequent increase was 9.5%. The current recovery has not followed this pattern, however, with a cumulative decline of real GDP of 4.2%, a post-war record, followed by a 3.0% rate of growth of real GDP during the first year of the current recovery.¹¹

The Impact of a Financial Crisis on the Pace of the Subsequent Recovery

Unlike earlier post-war recessions, the recent recession occurred with a financial crisis. Carmen Reinhart and Kenneth Rogoff say in a recent book that a slow protracted recovery with sustained unemployment is the norm in the aftermath of a deep financial crisis.¹² In other words, such crises not only reduce actual output, but also may reduce potential output (the economy’s structural and institutional capacity to produce output). In this circumstance, the economy could return to its trend growth rate, but there is unlikely to be a rebound period of substantially above normal growth to quickly return the economy to its pre-crisis potential output and growth path and, in turn, quickly reduce unemployment. Protracted underutilization of resources, including long-term unemployment, results in a deterioration of the economy’s potential output. This failure to return to the pre-crisis potential output path means that the economy bears the burden of a permanent output loss.

¹¹ U.S. Department of Commerce, Bureau of Economic Analysis, *National Income Accounts*, Table 1.6.1, <http://www.bea.gov/national/nipaweb/SelectTable.asp?Popular=Y>.

¹² Carmen Reinhart and Kenneth Rogoff, *This Time is Different: Eight Centuries of Financial Folly* (Princeton, NJ: Princeton University Press, 2009).

Recent analysis by the International Monetary Fund (IMF) examines the question of whether output will return to its pre-crisis trend after the crisis.¹³ It examines the medium-term and long-run paths of output after 88 banking crises over the past four decades in a wide range of countries (including both advanced and developing economies). A key conclusion was that seven years after the crisis, output had declined relative to trend by nearly 10% for the average country. But there was considerable variation of outcomes across crisis episodes.

The Drag of Deleveraging on U.S. Economic Growth

The prelude to the economic crisis in the United States was characterized by excessive leverage (the use of debt to support spending) in households and financial institutions, generating an asset bubble that eventually collapsed and left balance sheets severely damaged. The aftermath is likely to be a period of resetting asset values, deleveraging, and repairing balance sheets. This correction results in higher saving, weakened domestic demand, a slower than normal recovery, and persistent high unemployment, but not necessarily in a double-dip recession.

Counter-cyclical policy (fiscal and monetary stimulus) can moderate these negative effects but it cannot fully or quickly undue the underlying economic damage. That rebuilding will take time, and as it occurs economic growth is likely to remain moderate, even with the support of fiscal and monetary stimulus.¹⁴

The collapse of the housing and stock markets in 2008 and 2009 substantially decreased household net worth, which had, by the end of 2009, fallen \$10 trillion below its level in 2007.¹⁵ This large fall in net worth pushed the household debt burden to what may be an unsustainable level, especially if interest rates rise. The household saving rate has risen sharply since the beginning of 2010, averaging near 6% of disposable income, suggesting households could be making fast progress at repairing their balance sheets.

Investment and employment typically follow demand once the inventory cycle has run its course. Until consumer demand returns, business investment is likely to be weaker than normal.

Many banks and financial institutions are also deleveraging and rebuilding their balance sheets, a process that tends to dampen the flow of credit to the wider economy. Lending standards to consumers and businesses remain tight, as banks are inclined to hold a larger cushion of reserves to maintain liquidity and are more reluctant to lend long term. Large firms in good financial condition have access to credit on favorable terms. Reluctance to expand operations and employment depends on increased final demand for their products, not financing costs. However, smaller firms that are more dependent on bank lending may be having greater difficulty obtaining credit.

¹³ P. Kannan, A. Scott, and M. Terrones, "From Recession to Recovery: How Soon and How Strong?," in *World Economic Outlook* (Washington: International Monetary Fund, 2009), pp. 103-138. Also see Davide Furceri, and Annabelle Mourougane, *The Effect of Financial Crisis on Potential Output: New Empirical Evidence from OECD Countries*, Organisation for Economic Co-operation and Development, Economics Department Working Papers No. 699, May 2009.

¹⁴ See CRS Report, CRS Report R41332, *Economic Recovery: Sustaining U.S. Economic Growth in a Post-Crisis Economy*, by Craig K. Elwell.

¹⁵ Board of Governors of the Federal Reserve System, "Flow of Funds Accounts," Table B.100, June 2010, <http://www.federalreserve.gov/releases/z1/Current/z1r-5.pdf>.

The wild-card is the foreign sector. Strong net exports (exports minus imports) could take up some of the slack from weak consumer spending. Over the last year, exports have consistently accounted for about 50% of the growth of real GDP. But it is uncertain that recovery in the foreign economies that are typically large markets for U.S. exports will be strong enough to generate above normal demand for U.S. exports.

Also, increasing U.S. net exports to any degree requires that the trade deficit continue to decrease. For that to happen, trade surpluses in the rest of the world must simultaneously decrease. To achieve this adjustment of trade flows, a sizable rebalancing of domestic and external demand on the part of the deficit and surplus economies must occur.¹⁶ In the United States, as discussed above, some measure of rebalancing seems to be occurring, as evidenced by the increase in the personal saving rate.

Effective global rebalancing arguably also involves sizable adjustments by the largest surplus economies—Germany, Japan, and China. However, there are potential constraints on how substantially each of these economies can “save less and spend more,” perhaps limiting any sizable appreciation of their currencies relative to the dollar, and any associated boost in U.S. net exports.¹⁷

Factors That Suggest Economic Recovery Will Continue

A number of recent indicators suggest the current recovery is likely to continue:

- Business investment in equipment and software was up strongly in the first three quarters of 2010, rising at an annual rate of 20.4%, 24.8%, and 16.8% respectively.¹⁸ This could also be the force behind a sharp increase in imports in the second quarter of 2010, suggesting that the surge could be an indirect indicator of incipient economic vigor. The increase of imports could result from a wider and generally beneficial economic process that could in coming quarters manifest itself as stronger private spending and faster economic growth. Today’s geographically fragmented production processes can lead to a strong increase in capital spending also being accompanied by a strong increase in imports. As domestic firms increase output of capital equipment, they also tend to increase the inflow of intermediate goods that are part of the final product, from foreign affiliates and other global sources. However, for this process to generate a sustained boost in economic growth, it would soon need validation by stronger near-term consumer spending and export sales.

¹⁶ On global rebalancing, see for example Olivier Blanchard, *Sustaining Global Recovery*, International Monetary Fund, September 2009, at <http://www.imf.org/external/pubs/ft/fandd/2009/09/index.htm>; “Rebalancing,” *The Economist*, March 31, 2010; and Board of Governors of the Federal Reserve System, vice-chairman Donald L. Kohn, Speech “Global Imbalances,” May 11, 2010, at <http://www.federalreserve.gov/newsevents/speech/kohn20100511a.htm>.

¹⁷ For further discussion, see CRS Report R41332, *Economic Recovery: Sustaining U.S. Economic Growth in a Post-Crisis Economy*, by Craig K. Elwell.

¹⁸ Department of Commerce, Bureau of Economic Analysis, “National Economic Accounts,” Table 1.1.1, <http://www.bea.gov/national/nipaweb/TableView.asp?SelectedTable=1&FirstYear=2009&LastYear=2010&Freq=Qtr>.

- Initial jobless claims in recent months were high, but have consistently been below their year-earlier level.¹⁹
- Industrial production and rates of capacity utilization have been rising, particularly in manufacturing and for durable equipment. Industrial production for the overall economy continued to rise through the fall of 2010 and is up 5.3% over its year-earlier level. Industrial production of business equipment through October has been particularly strong, up nearly 10.4% over its year-earlier level. Capacity utilization in October 2010 for total industry is 74.8%, 4.1 percentage points above the rate from a year earlier.²⁰
- The dollar exchange rate (on a real trade weighted basis) has depreciated about 13% since March 2009, pointing to stronger net exports.²¹
- The trade gap (in goods and services) narrowed in September, falling to \$44 billion from \$62 billion in June, as exports increased and imports decreased. (However, falling imports could be the result of the slowing of domestic demand in the second and third quarters of 2010.)²²
- In asset markets, yields on some short-term Treasury securities have edged up since June as those on corporate bonds have edged down. This change in the recent pattern may indicate that investors are moving out of highly liquid, low-risk “safe haven” assets and into long-term corporate bonds because prospects for private industry are seen to be improving. Stock market prices have also stabilized since their second quarter decline.
- Productivity growth has slowed significantly in the second and third quarters of 2010 compared with higher rates earlier in the recovery. For the near term, this could be good news, as it may indicate that business’s ability to increase output without increased hires may be waning, meaning that employment will soon rise more strongly with advancing industrial output.²³
- The Fed announced on November 3, 2010 that due to the slowing pace of economic growth, rising structural unemployment, and the increased risk of deflation, it will apply added monetary stimulus by means of the purchase of an additional \$600 billion of Treasury securities at a pace of about \$75 billion per month, and continue the practice of replacing maturing securities with Treasury security purchases.²⁴

¹⁹ U.S. Department of Labor, Unemployment Insurance Weekly Claims Report, September 23, 2010, <http://www.dol.gov/opa/media/press/eta/ui/current.htm>.

²⁰ Federal Reserve Statistical Release, G.17, September 15, 2010, <http://www.federalreserve.gov/releases/g17/Current/g17.pdf>.

²¹ Federal Reserve Statistical Release, H.10, September 20, <http://www.federalreserve.gov/releases/H10/Summary/>.

²² See <http://www.census.gov/indicator/www/ustrade.html>.

²³ U.S. Department of Labor, Bureau of Labor Statistics, *Productivity and Costs*, September, 2, 2010, http://data.bls.gov/PDQ/servlet/SurveyOutputServlet?data_tool=latest_numbers&series_id=PRS85006092.

²⁴ Board of Governors of the Federal Reserve System, *Federal Open Market Committee*, <http://www.federalreserve.gov/monetarypolicy/fomccalendars.htm>.

Economic Projections

Weighing the several forces, positive and negative, that are likely to influence economic activity over the near term, most economic projections indicate U.S. economic recovery will continue, albeit at a slower than normal pace:

- CBO projects that the recovery will continue at a modest pace. Real GDP is projected to grow by only 2.0% from the fourth quarter of 2010 to the fourth quarter of 2011, down from a 2.8% pace over the previous four quarters. The unemployment rate is projected to fall to 9.0% in 2011.²⁵
- The Blue Chip consensus, the average of about 50 forecasts by private-sector economists, projects real GDP will continue to rise, up 2.7% in 2010 and 2.5% in 2011. The unemployment rate is projected to fall to 9.3% in 2011.²⁶
- The IMF projects real GDP in the United States to increase 2.6% in 2010 and 2.3% in 2011. Growth at this pace implies that the gap between actual and potential output will remain wide. Therefore the unemployment rate is expected to remain high at 9.7% in 2010 and 9.6% in 2011. Globally, the IMF expects modest but steady recovery in most advanced economies and strong growth in many emerging and developing economies. World output is projected to increase 4.6% in 2010 and 4.3% in 2011.²⁷
- Fed Chairman Bernanke says “despite the recent slowing, it is reasonable to expect some pick-up in growth in 2011 and subsequent years. Broad financial conditions, including monetary policy are supportive of growth, and banks appear willing to lend. Importantly households may have made more progress than we had earlier thought in repairing their balance sheets, allowing them more flexibility to increase their spending as conditions improve. And as the expansion strengthens, firms should become more willing to hire.”²⁸

Forecasts are always subject to uncertainty. That uncertainty is likely to be especially high at this time because forecasting the path of the economy near turning points in the business cycle is always difficult and because of the singular characteristics of the current business cycle (i.e., sharp financial crisis, unusual and strong policy responses, and an elevated risk of deflation.

²⁵ Congressional Budget Office, *The Budget and Economic Outlook:an Update*, August 2010, <http://www.cbo.gov/ftpdocs/117xx/doc11705/08-18-Update.pdf>.

²⁶ Aspen Publishers, *Blue Chip Economic Indicators*, September 10, 2010.

²⁷ International Monetary Fund, *World Economic Outlook: An Update*, October 2010, <http://www.imf.org/external/pubs/ft/weo/2010/02/pdf/c2.pdf>.

²⁸ Board of Governors of the Federal Reserve System, Chairman Ben S. Bernanke, “The Economic Outlook and Monetary Policy,” Speech at the Federal Reserve Bank of Kansas City Economic Symposium, Jackson Hole, Wyoming, August 27, 2010, <http://www.federalreserve.gov/newsevents/speech/bernanke20100827a.htm>.

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