Euler Hermes Economic Research

Country Report

# United States

## Weak productivity impeding growth, raising insolvencies

### General Information

| | |
|---|---|
| **GDP** | USD17,419bn (World ranking 1, World Bank 2014) |
| **Population** | 319mn (World Ranking 3, World Bank 2014) |
| **Form of state** | Federal Republic |
| **Head of government** | Barack OBAMA (Democrat) |
| **Next elections** | 2016 Presidential, Congressional, Gubernatorial |

### Strengths

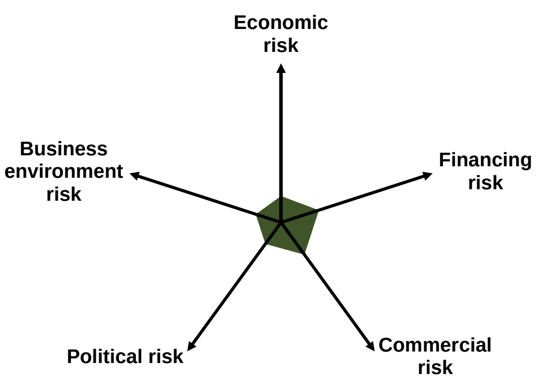
- World's largest economy
- Politically stable
- High per capita GDP
- Relatively low unit labor costs
- High data transparency
- Reserve currency
- Large oil and gas reserves
- Diverse GDP
- Strong dollar (lowers inflation, interest rates)

### Weaknesses

- Structural unemployment
- Lack of skilled workers
- Low productivity
- High corporate tax rate
- High public debt, persistent budget deficits
- Soaring amount of, and defaults on, student loans
- Bloated Federal Reserve balance sheet
- Strong dollar (widens persistent trade deficit)

### Country Rating

AA1




*Source: Euler Hermes*

### Trade structure

By destination/origin (% of total)

| Exports | | Rank | | Imports |
|---|---|---|---|---|
| Canada | 18% | 1 | 19% | China |
| Mexico | 14% | 2 | 16% | Canada |
| China | 9% | 3 | 13% | Mexico |
| Japan | 5% | 4 | 6% | Japan |
| Germany | 4% | 5 | 5% | Germany |

By product (% of total)

| Exports | | Rank | | Imports |
|---|---|---|---|---|
| Refined Petroleum | 8% | 1 | 11% | Crude Oil |
| Engines | 5% | 2 | 7% | Cars and Cycles |
| Plastic Articles | 4% | 3 | 5% | Telecom Equip. |
| Precisions Instruments | 4% | 4 | 5% | Computer Equip. |
| Pharmaceuticals | 4% | 5 | 4% | Electrical Apparatus |

*Source: Chelem*

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## Economic Overview

### Weak productivity impeding growth

Productivity has grown at an annual rate of only +0.9% annually during the recovery, less than half of the post-WWII average of +2.3%, providing a stiff headwind on the economy, and holding the 2016 GDP forecast to only +1.9%, and +2.0% in 2017. This low productivity can be explained in part by developments in the labor market. For the first time ever, the job openings rate has now exceeded the hiring rate, suggesting that there are plenty of jobs available, but few people who have the skills to fill them – the skills mis-match. And because the people who have been hired already don't have the proper skills, their productivity is low. In addition, the lack of supply of the right people is slowing job growth. Each of the past three months through May has shown progressively slower job creation, and May's employment report was very disappointing with only 38k jobs created – far below expectations. In addition, 820k workers left the labor force over the past two months, driven by the fact that 10,000 Baby Boomers will be retiring every day for the next 13 years, an inexorable demographic that will be a long-term impediment to growth. Normally less supply of labor would cause an increase in wages but wage pressure has been minimal so far because since no one is getting hired, no one is getting higher wages.

### Insolvencies to rise

In addition to impeding growth, low productivity has been a headwind on corporate profits. Real, after tax corporate profits shrank at a -4.7% y/y rate in Q1-16. At the same time, the Federal Reserve is moving towards a tighter monetary policy, which in turn has encouraged commercial bankers to tighten their lending conditions. This tightening (shown as the blue line in Figure 3) indicates that the net percentage of bankers widening their spreads is sharply rising. Thus businesses are not only suffering from low productivity, they are also facing increased financing costs. These tighter lending conditions historically are highly correlated with increased bankruptcies. In Q1-16, bankruptcies rose at a +1.1% y/y rate, the first increase since just after the recession ended. Over the full year, we expect bankruptcies to increase +3%, also the first increase since the end of the recession seven years ago.

### Uncertainty over the Fed and the election

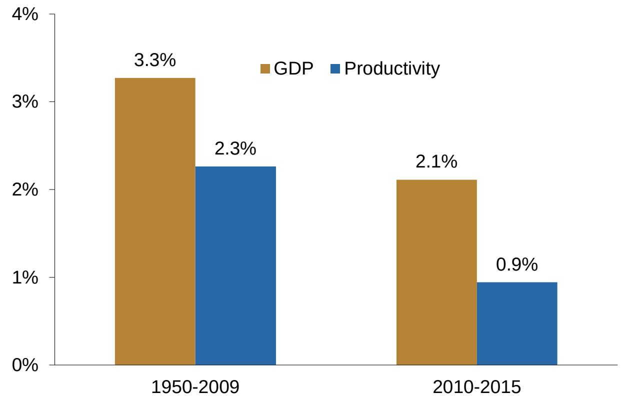
The Federal Reserve's credibility is rapidly eroding, making it difficult for financial markets and policymakers to act with conviction. After the meeting of December 2015, the Fed indicated that they were likely to hike four times in 2016. Then after the April 2016 meeting, the Fed lowered those expectations to two moves, and then accelerated the timing of the moves in the minutes from the April meeting, and then lowered expectations again to just one move after May's weak employment report. At the same time the presidential election is causing significant uncertainty. In the Consumer Confidence survey, the evaluation of present conditions is holding high, but concerns about the future are falling, and in fact the gap between the two is the widest since the recession. The gap started to widen significantly as the election campaign started in earnest, suggesting concern for the future regarding the election, likely holding down consumption.

**Figure 1: Key economic forecasts**

| | 2014 | 2015 | 2016f | 2017f |
|---|---|---|---|---|
| GDP growth (% change) | 2.4% | 2.4% | 1.9% | 2.0% |
| Inflation (%, end-year) | 1.6% | 0.1% | 1.1% | 1.9% |
| Fiscal balance (% of GDP) | -2.8% | -2.7% | -3.5% | -2.5% |
| Public debt (% of GDP) | 104.6% | 105.4% | 106.4% | 105.6% |
| Current account (% of GDP) | -2.4% | -2.5% | -2.3% | -3.3% |

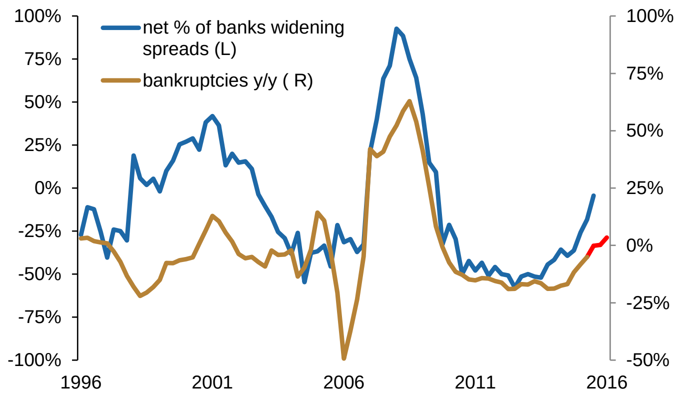
*Sources: IHS, national sources, Euler Hermes*

**Figure 2: Productivity vs. GDP, annual rates**




*Sources: IHS, BLS, BEA, Euler Hermes*

**Figure 3 : Lending Conditions vs. Bankruptcies**




*Sources: IHS, US Courts, Federal Reserve, Euler Hermes*





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