



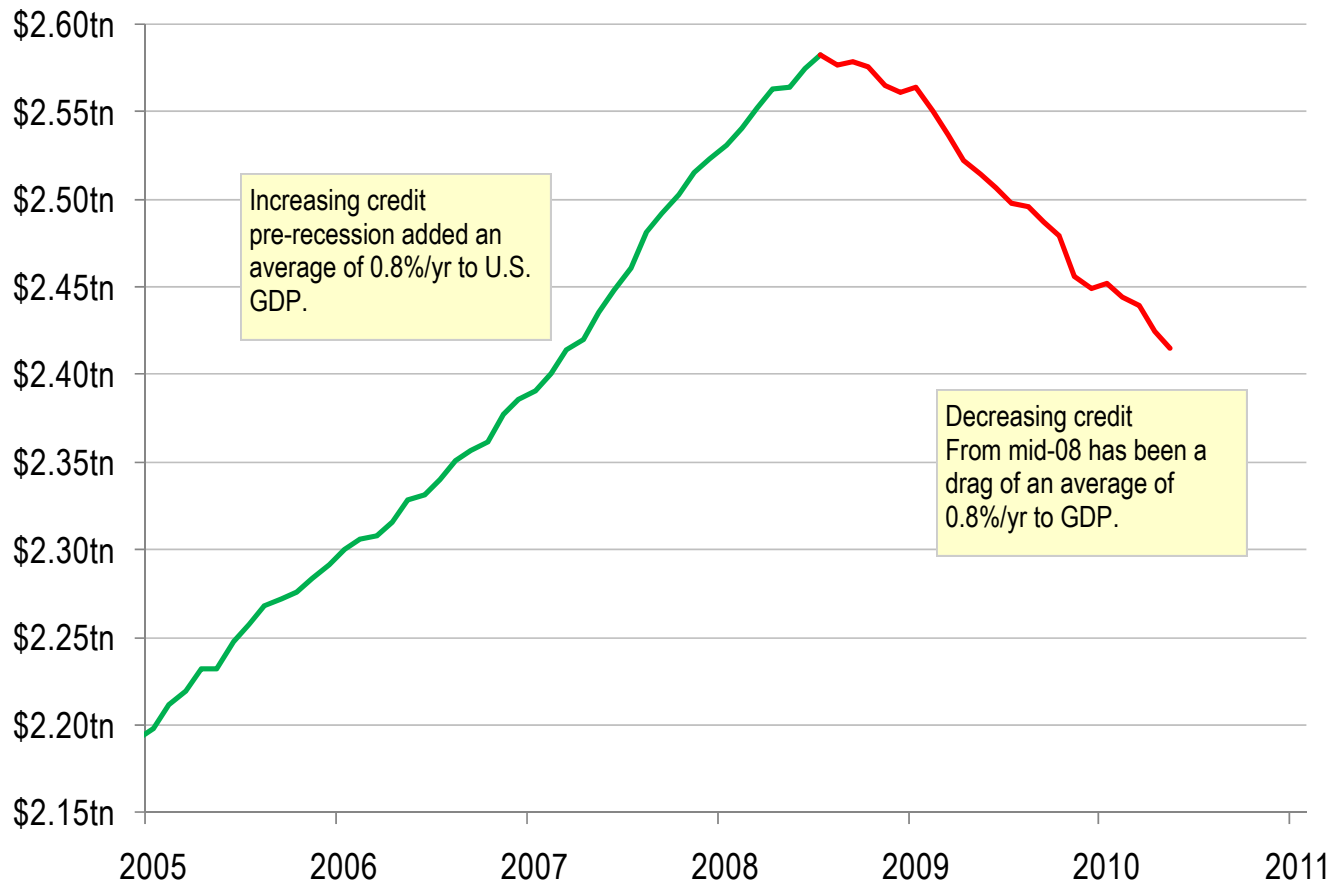
De-leveraging continues

Yesterday afternoon (July 8th, 2010), the Federal Reserve released the consumer credit report for the month of May (this is all household debt ex. mortgages). The report reinforced a continued trend of precipitous de-leveraging by the consumer. The difference vs. what economists had predicted paired with the prior month's downward revision, amounted to a shockingly large decrease in outstanding credit of \$20.7bn.

The chart below shows the last 5 years of outstanding consumer credit. When times are good, credit increases which adds to GDP through consumer spending (an avg. of 0.8%/yr over the last 15 years), however what has been purchased before, must be paid for at some point. The de-leveraging trend we've seen since mid-08 is subtracting an average of 0.8% from GDP. This transition from leveraging to de-leveraging has tremendous implications for the economy because it represents a 1.6% shift downwards from prior real GDP averages (3.2%). From the experience of the credit recessions in Japan and the Great Depression, this deleveraging trend will continue to the point where households feel confident enough to spend from real (not borrowed) money. Until this time, the United States will face continued disinflationary forces.

Outstanding Consumer Credit

(all household debt ex. mortgage)



Data Source: Federal Reserve G.19 release