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# 2012 US budget: growth as "antidote" to deficit

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## Overview

Shocks on energy and commodity prices have triggered a rebound of inflation at the global level, causing emerging economies to tighten their monetary policy. In Western economies, this negative shock takes place in a context of mounting pressure on public debt embodied by the current harsh debate in the US Congress and persisting troubles of European periphery. For the first time since the end of the crisis, the global recovery is challenged by these two concomitant negative shocks.

**Focus: The US 2012 budget: growth as "antidote" to deficit**

Encouraged by the positive results of the first stimulus package after the crisis – American Recovery and Reinvestment Act (ARRA) in 2009 and 2010, the US government continued an expansionary fiscal policy in 2011. Based on the judgment that the US economy remained fragile and that an early exit strategy would endanger the recovery, the second stimulus program focused on promotion of investment in R&D and infrastructure projects and extension of Bush era tax cuts. On the contrary, European countries organized particularly aggressive policies of fiscal austerity under market pressure.

The choice of the US government has allowed the US economy to be restructured under an accommodative monetary and fiscal policy. On the other hand, however, this approach has also resulted in a significant increase of US public deficit, close to 10% and 9% of GDP in 2009 and 2010 respectively. In terms of public debt, it increased to more than 60% of GDP compared to 50% of GDP before the crisis. The US austerity has to come sooner or later given the persisting fears on the stability of the Euro zone debt. As expected, the Obama administration has recently proposed its new budget for the fiscal year of 2012 covering various austerity measures aiming to reduce public expenditure. It should be finalized by June. The major measures are as follows.

- Freeze discretionary non-military spending over five years
- Freeze federal civilian worker pay for two years
- Cut or consolidate numerous public programs
- Reduce military spending

This report examines the current state of US public finance characterized by a higher than expected deficit in 2011 due to delay of consolidation efforts. The proposed austerity measures, covering only 12% of total public expenditure, reflect a soft approach for tackling the debt problem. The mild austerity and absence of tax hikes reveal the confidence of US government in the capacity of the US economy to create enough wealth to ensure fiscal revenues. The strategy of the US government continues to focus on fostering growth potential in investing in new energy, infrastructures and education. The proposed reform on Freddie Mac and Fannie Mae reveals the will of the US government to gradually exit its housing policy post crisis. In our view, the US debt is to remain sustainable in the short- and medium-terms. In the long-term, if the US authorities do not become more aggressive in tackling budgetary issues fundamentally, its debt might be exposed to much more pressure from the market triggering a possibly continuous increase in the long-term interest rates.

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| | Overweight | Relative performance over MSCI-China Index 5% ~ 20% |
| | Hold | Relative performance over MSCI-China Index -10% ~ 5% |
| | Sell | Relative performance over MSCI-China Index > -10% |
| | NR | Not rated |
| Sector rating | Outperform | Relative performance over MSCI-China Index >10% |
| | Neutral | Relative performance over MSCI-China Index -10% ~10% |
| | Underperform | Relative performance over MSCI-China Index > -10% |

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