The Financial State of the Union

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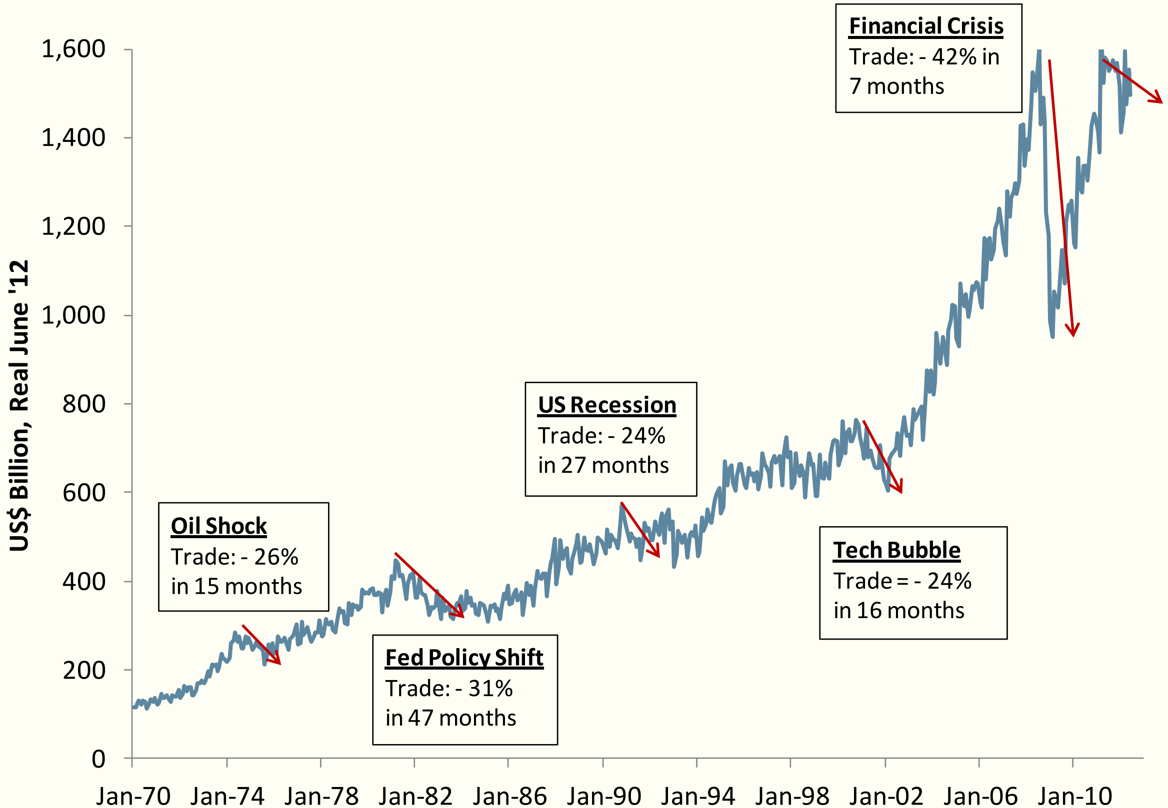
Contents

World Trade: Extreme Policy Response Limits Duration of Recession…*Distortions Remain*



Source: IMF Direction of Trade Statistics and Center for Financial Stability .

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Spectrum of Fundamental Drivers:

Why Advanced Economies look more like Emerging Markets.

Advanced Economies

Middle Income Emerging Markets

Fragile States

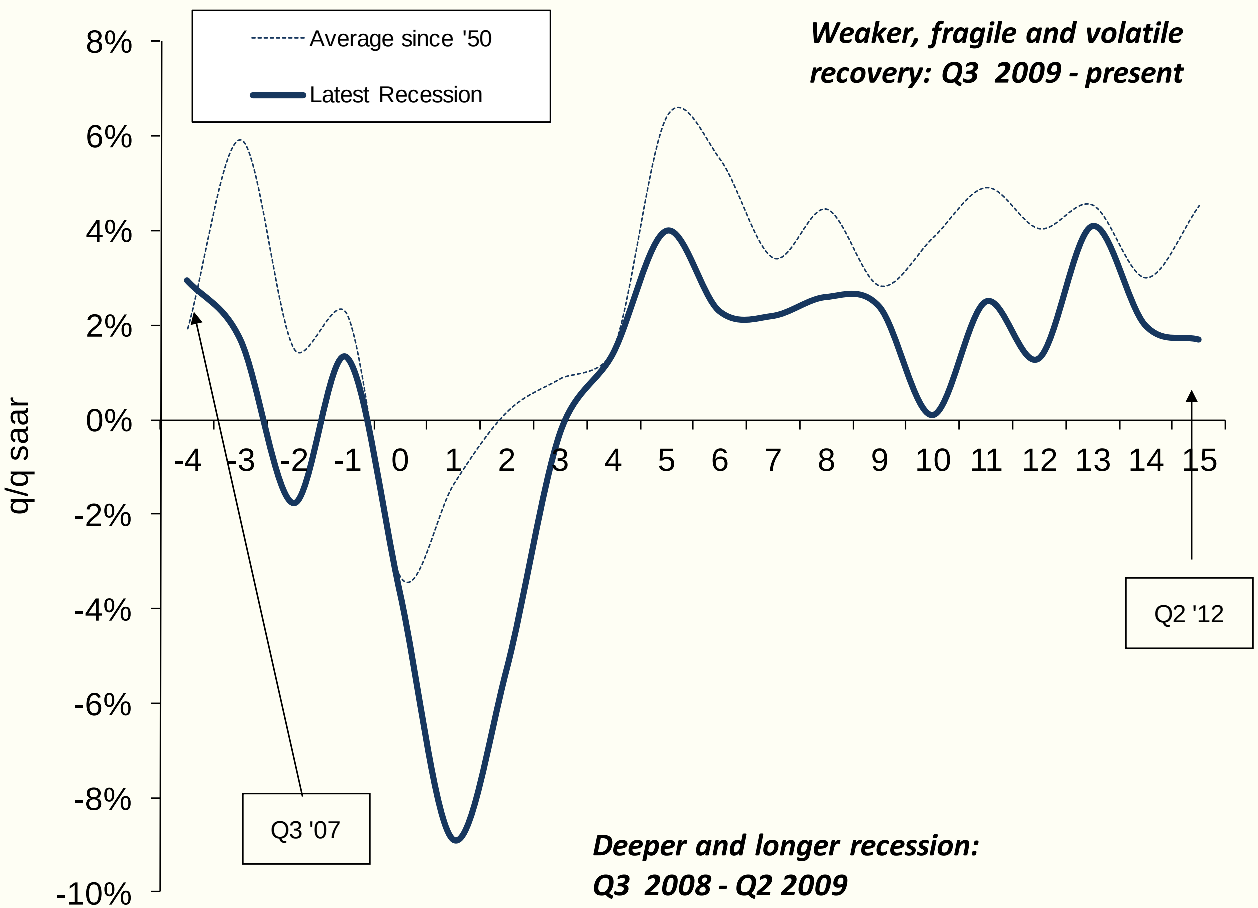
More strictly ***ECONOMIC*** analysis

More strictly ***POLITICAL*** analysis

Economics

Politics

Weak, Fragile and Volatile Economic Recovery



Source: Bureau of Economic Analysis and Center for Financial Stability .

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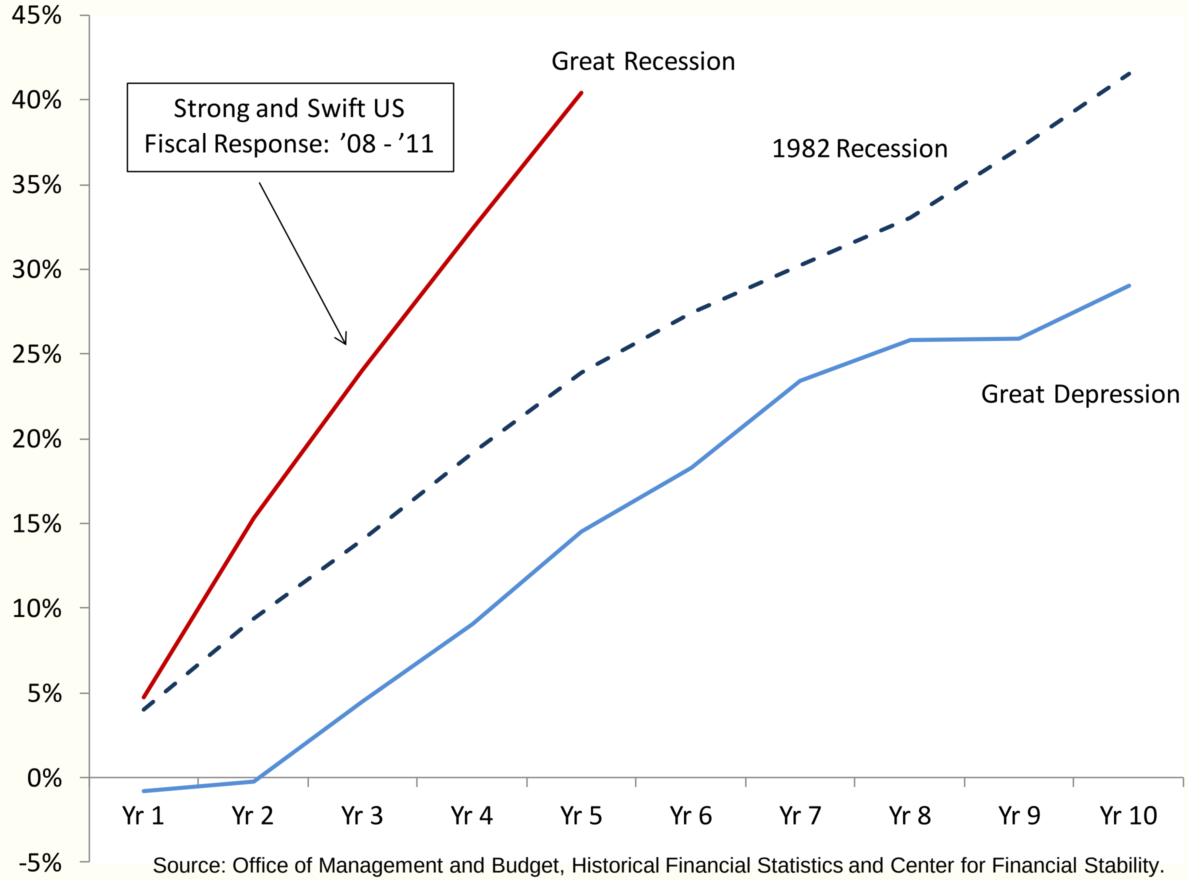
Cumulative Deficits in Deep Downturns, % of GDP



Source: Office of Management and Budget, Historical Financial Statistics and Center for Financial Stability.

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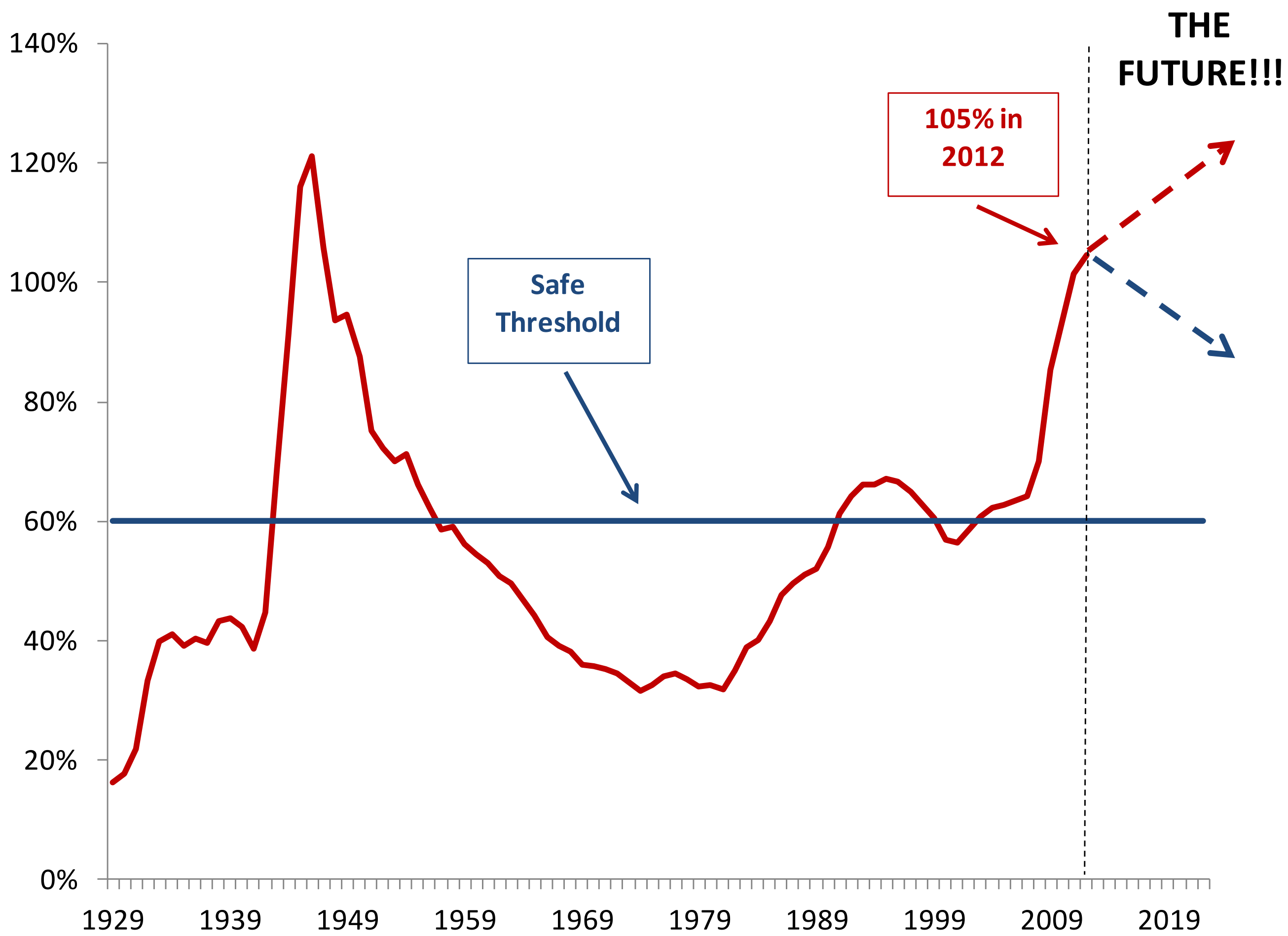
Fiscal Stimulus and Capacity to Expand



Source: US Treasury, Bureau of Economic Analysis and Center for Financial Stability.

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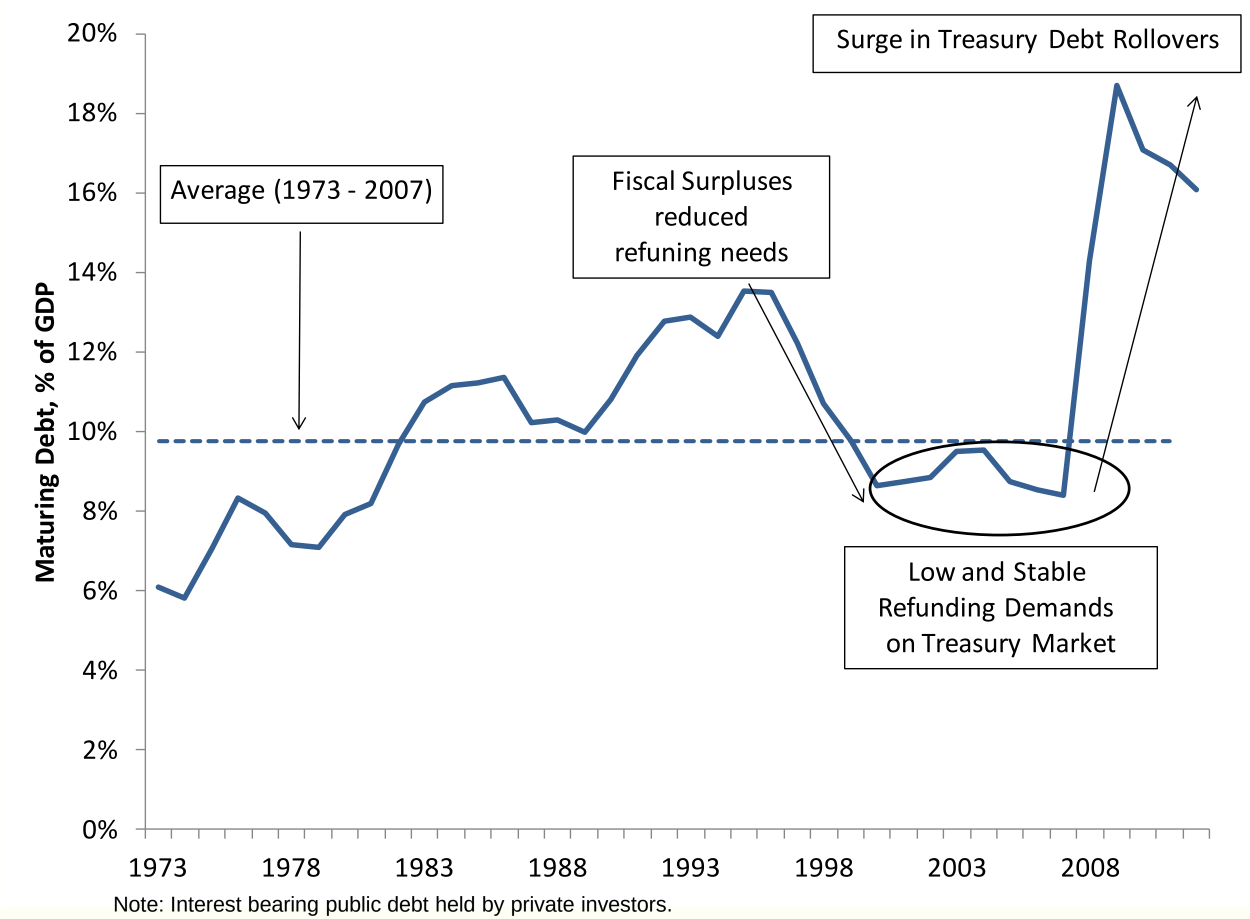
It's the *Principal* Matters!!!

Despite legitimate concerns regarding the budget deficit, large refinancings of debt represent an equally severe – yet lesser known challenge. The experience of emerging markets and some advanced economies suggests that…it is the repayment of principal that often triggers a crisis rather than simply the size of the debt or deficit.

From: "Treasury Maturities: The Other Fiscal Problem," March 10, 2011 (http://www.centerforfinancialstability.org/research/USFiscal031011.pdf)

USG Debt Maturities Spike in Coming Year



Note: Interest bearing public debt held by private investors.
Source: US Treasury and Center for Financial Stability.

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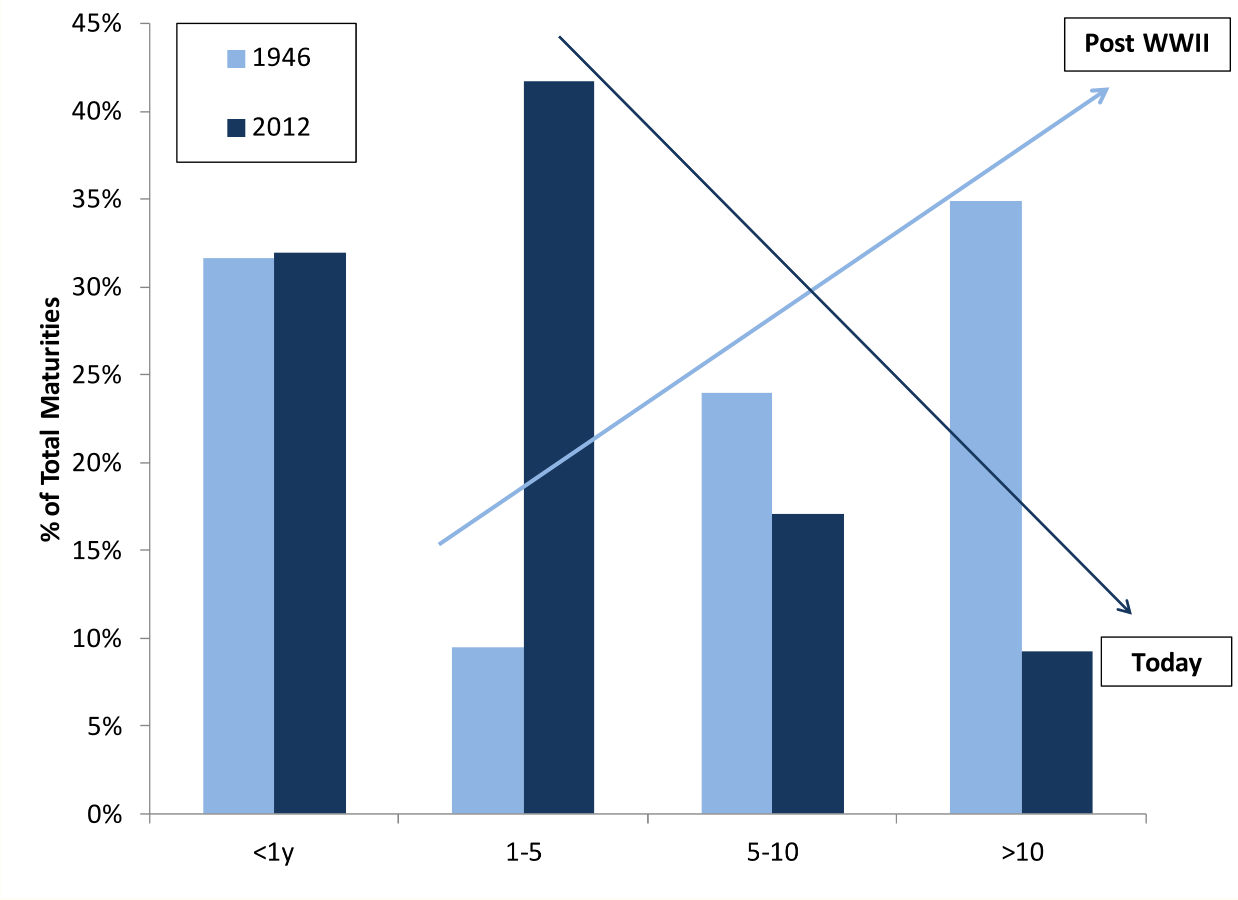
More Dangerous Treasury Debt Profile

Although US public debt-to-GDP was higher after the post-WWII period, the profile of maturing obligations was much safer!



Note: Interest bearing public debt held by private investors.
Source: US Treasury and Center for Financial Stability.

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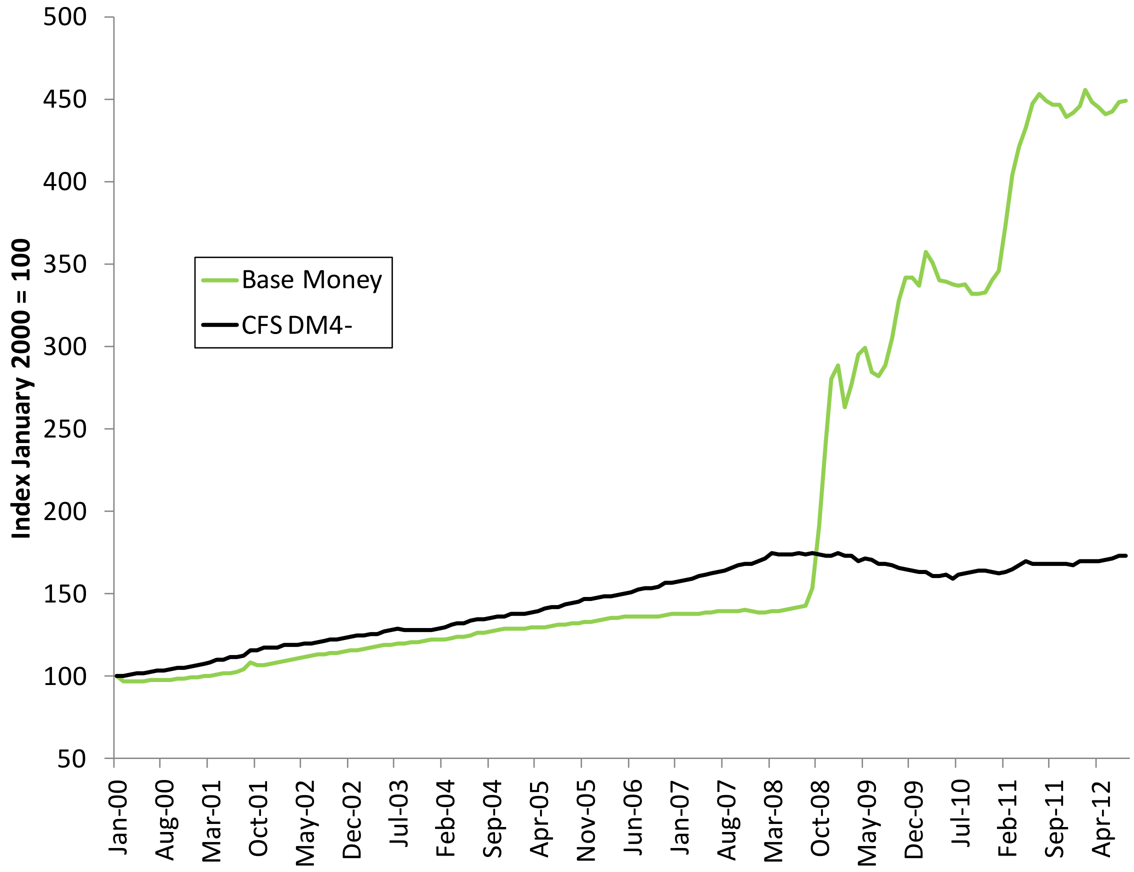
Limits to the Fed's Quantitative Easing (QE)



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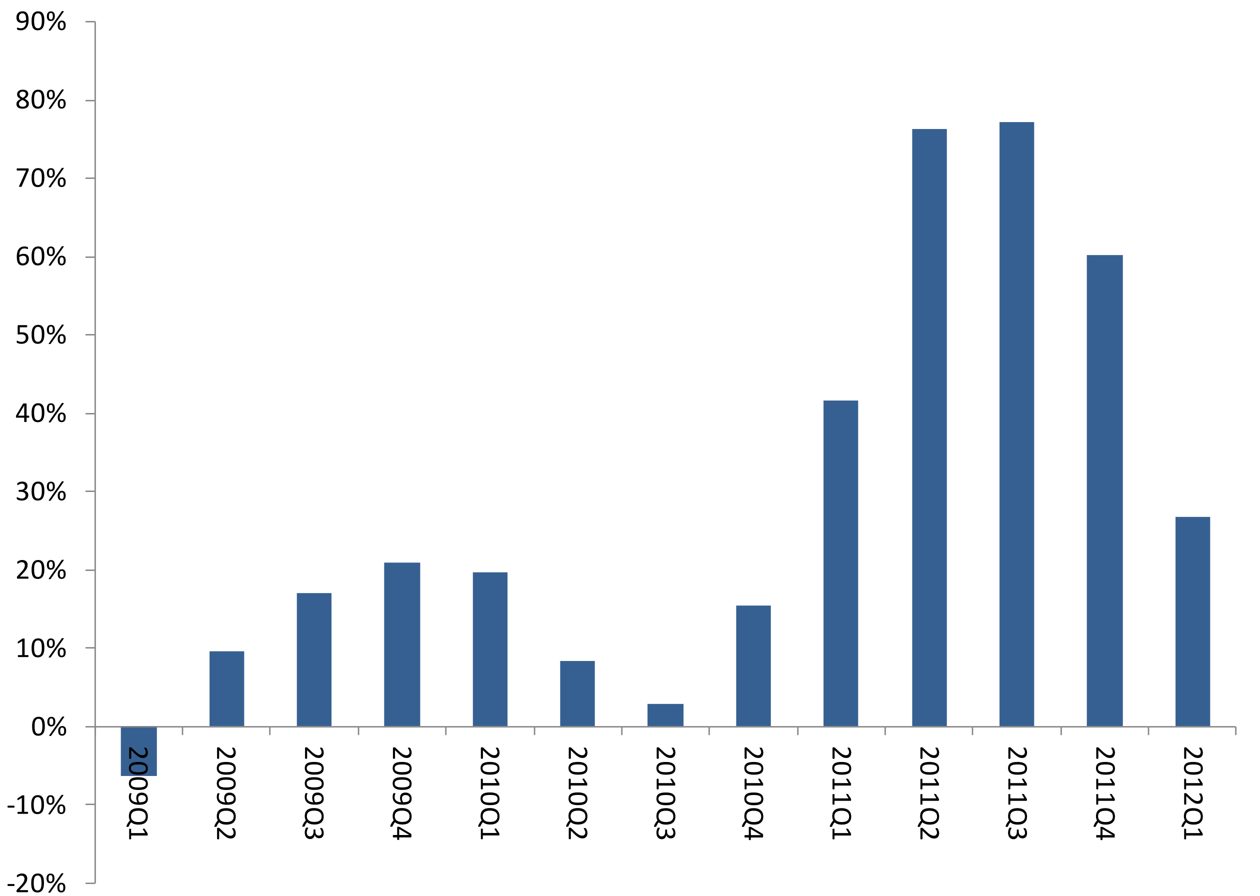
With thanks to William Barnett, Director of Advances in Monetary and Financial Measurement and Jeff van den Noort, Chief Technology Officer at the Center for Financial Stability.

Source: Federal Reserve, other official bank rates, and the Center for Financial Stability.

Federal Reserve Funding of Fiscal Deficit

Net Purchases of Treasury Securities by the Fed, %

Fed purchases of Treasury bonds distort market relationships.



Source: Federal Reserve, Flow of Funds Accounts and the Center for Financial Stability.

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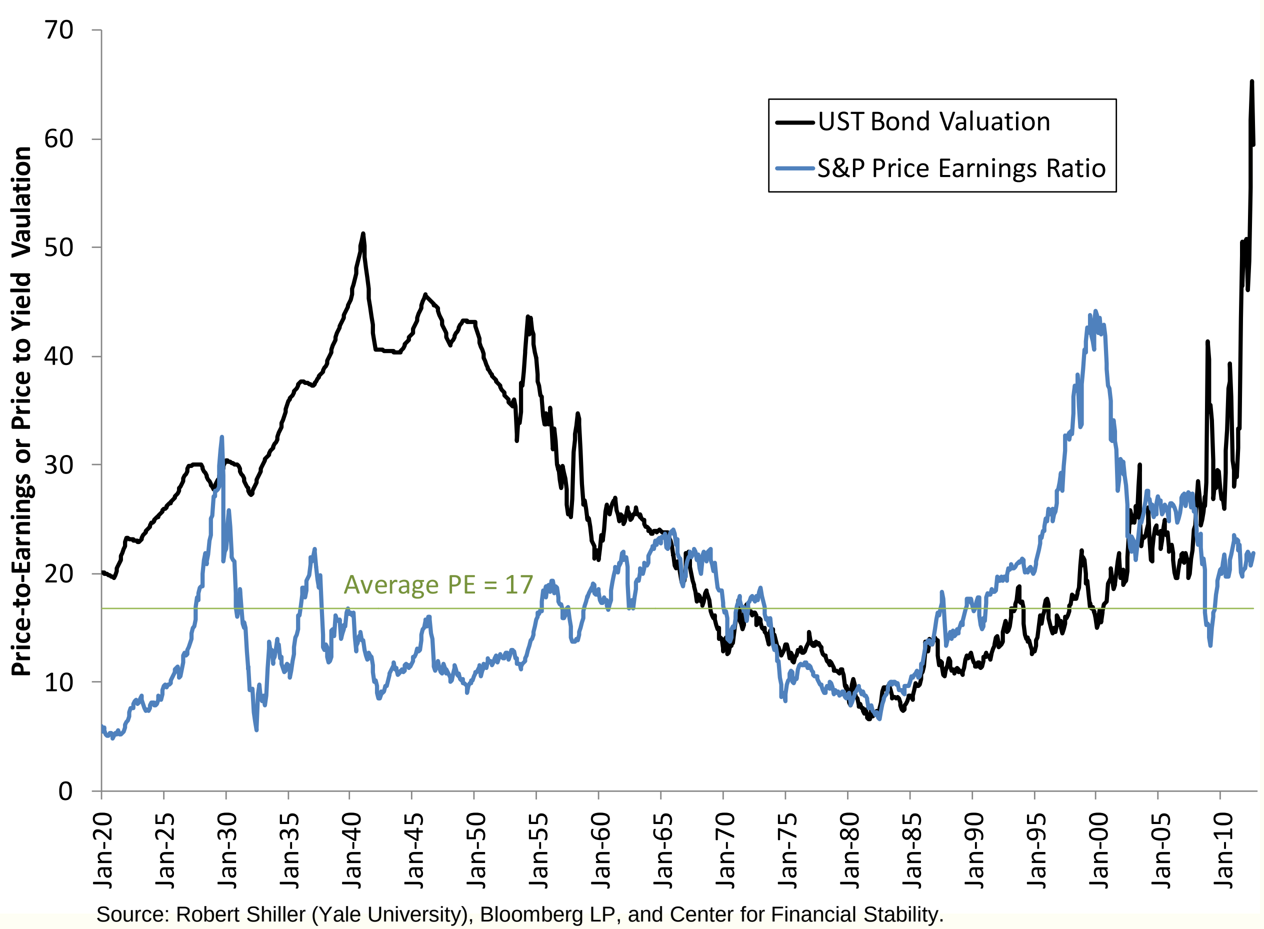
Policy Distortions: Risks for Markets and Fed



Source: Robert Shiller (Yale University), Bloomberg LP, and Center for Financial Stability.

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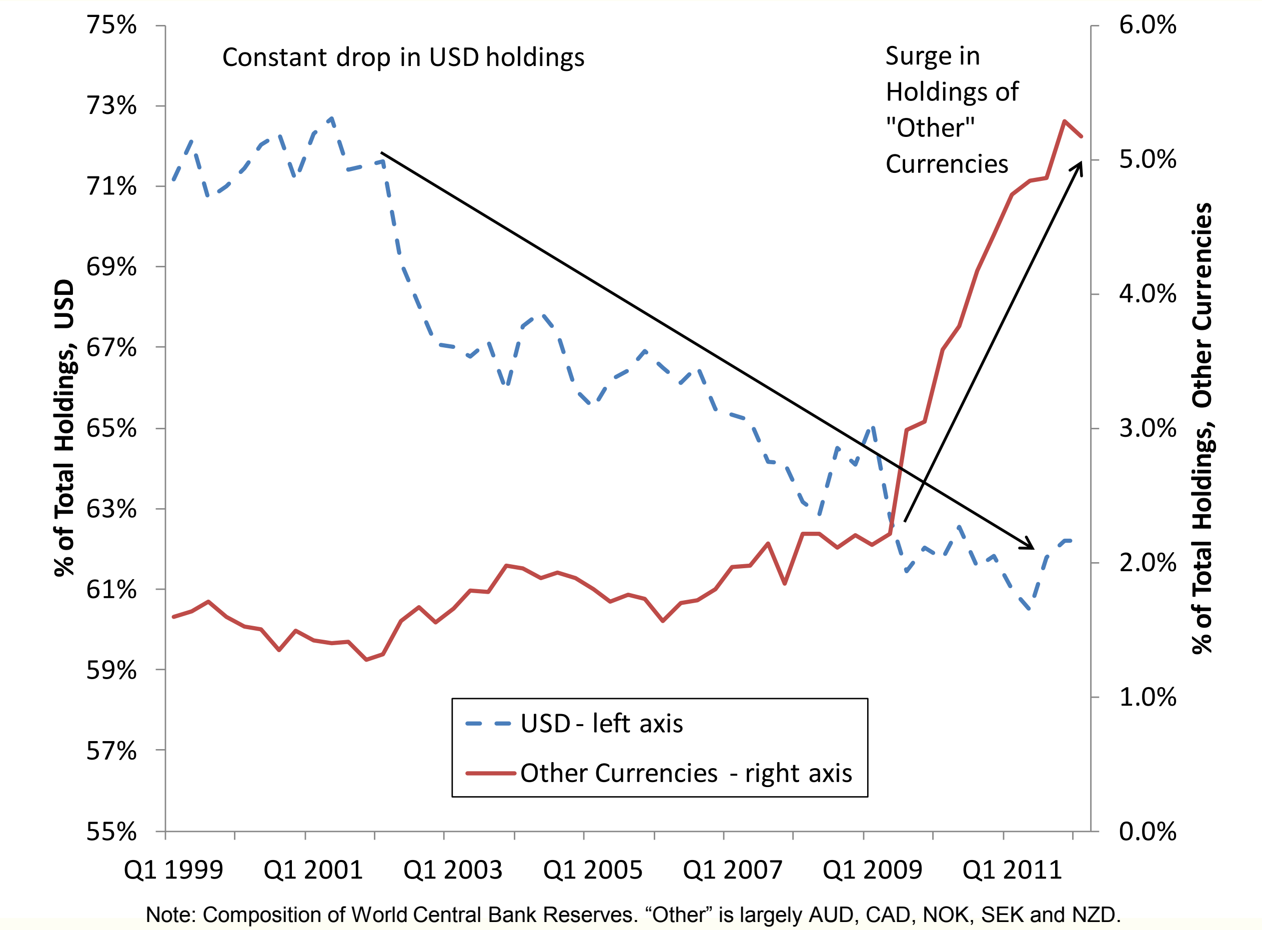
Reserve Currencies: Shifting "Stores of Value"



Note: Composition of World Central Bank Reserves. "Other" is largely AUD, CAD, NOK, SEK and NZD.
Source: Datastream, International Monetary Fund (COFER) and Center for Financial Stability.

About CFS and Disclosure

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