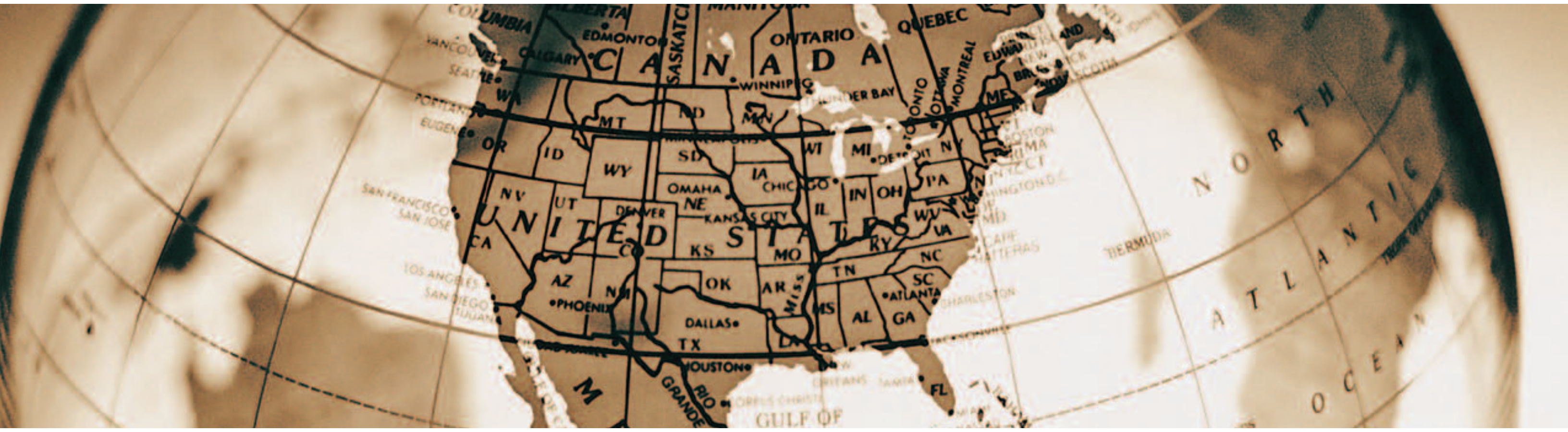
White Paper
October 2011

The Outlook for the US Economy



On the Edge of Recession

It's been a disappointing economic recovery since the end of the financial crisis in mid-2009, with US gross domestic product (GDP) growing by only about 2 percent in real terms. The main result of this disappointing growth has been the persistently high number of unemployed in the US. The current rate of GDP growth is insufficient to dent the huge pool of long-term unemployed.

By Andrew Tilton
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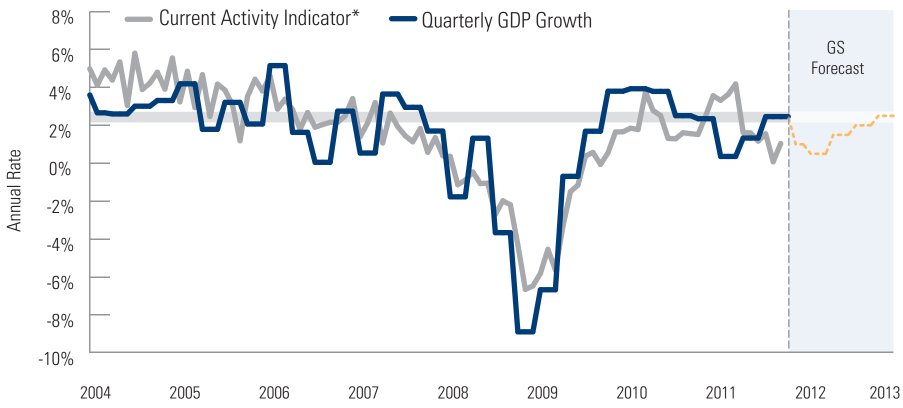
As economic conditions are subject to change, the information and opinions discussed in this outlook are current only as of October 19, 2011.

Above-Trend Growth Remains Elusive



* First principal component of 25 weekly and monthly US activity indicators. Shaded band indicates trend growth of 2.25-2.75%.
Source: Department of Commerce. GS Global ECS Research.

Impediments to Growth: Issues Weighing on the US Economy

Fiscal Tightening

Given the fiscal outlook remains difficult, we believe we're unlikely to get further stimulus, and that government will continue to be a modest drag on growth. We believe we will see an increase in the rate of fiscal tightening at the federal level over the next couple of years.
Fiscal policy was a boost in 2009, roughly neutral in 2010, and in 2011, roughly a 1 percentage point drag. In 2012, the impact depends on upcoming policy decisions. At best from a short-term perspective, if the Obama administration's package passed, which seems quite unlikely, fiscal drag would be neutralized; at worst, if all temporary stimulus expires, we'd expect a fiscal drag of more than 1 1/2 percentage points of growth in early 2012. The more likely, middle ground outcome: the administration and Congress agree on tax-related proposals and probably extend the one-year payroll tax cut for one more year.

There will be a bigger problem in 2013 with the expiration of the Bush tax cuts, as well as any fiscal stimulus measures.

Fiscal Stress in Europe

In addition to the belt tightening in the domestic US, the turmoil in Europe continues to threaten stability, particularly within the banking sector. While a number of measures of financial stress have been elevated in past weeks, so far we have not seen a dramatic impact on real economic data in the US. In spite of this, we are concerned that tighter credit conditions could slow growth over the next few quarters.

While we're not forecasting recession, we expect the combination of slightly tighter fiscal policy and potential financial shock from the crisis to result in weaker growth in the near term.

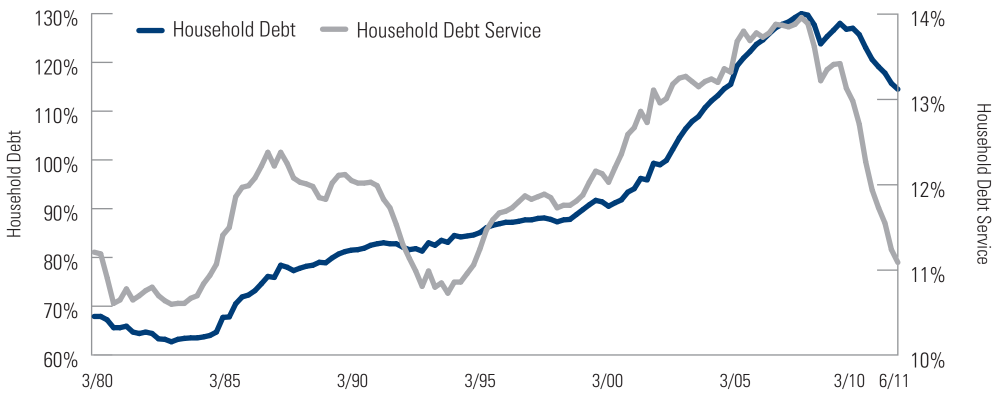
Glimmers of Hope?

In spite of the challenges facing the US economy, we highlight reasons to be optimistic.

1. Household finances are gradually getting healthier

Household debt burdens have continued to improve, with the share of income spent on debt service declining.

Percent of disposable income allocated to debt service has declined



Source: Federal Reserve Board. Department of Commerce.

2. Cyclical sectors have bottomed

While depressed and unlikely to fall much further, these sectors are more likely to experience growth instead of further decline. Homebuilding in particular hasn't kept pace with demographic demands, which we believe positions the sector to grow steadily over time.

3. Potential for additional Fed action

We believe the Fed can and will deliver more monetary policy stimulus at some point in early 2012, likely by expanding the balance sheet further. While we recognize the skepticism surrounding the Fed's ability to impact the economy at this stage, we think that at least on the margin, additional quantitative easing and/or changes in communication can affect both growth and inflation.

Inflation Outlook

We believe inflation is unlikely to be a significant problem. It has risen significantly by some measures in the last year, but we believe that trend is unlikely to continue.

We had exceptionally low inflation in 2010, but over the last six months, we've witnessed a rate of inflation well above 2%. There are three components of core inflation that have disproportionally caused the rate to be higher than the Federal Reserve Bank's long-term target:

1. Rent

In spite of ample existing home supply, many potential buyers are having trouble obtaining mortgages, and with some homeowners in foreclosure, both populations are being pushed into the rental market. We believe this is a genuine cause for concern going forward.

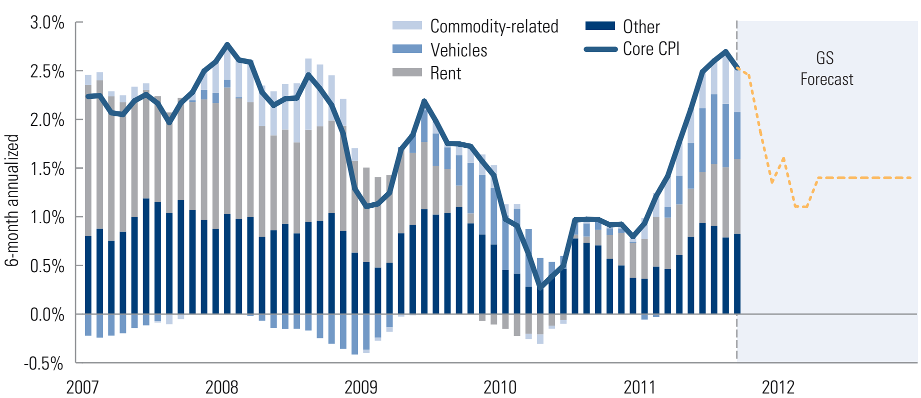
2. Vehicles

Prices have moved higher due to supply chain disruptions from the earthquake in Japan earlier this year. The tragic events that followed reduced supply and increased pricing power for manufacturers, but we believe that dynamic will gradually be unwound over coming months as production increases.

3. Apparel prices

A temporary surge in commodity prices and higher wages in Asia where the majority of clothing is manufactured has led to higher prices, which we expect to ease somewhat in the coming months.

Little Sign of Broad Inflation Pressure



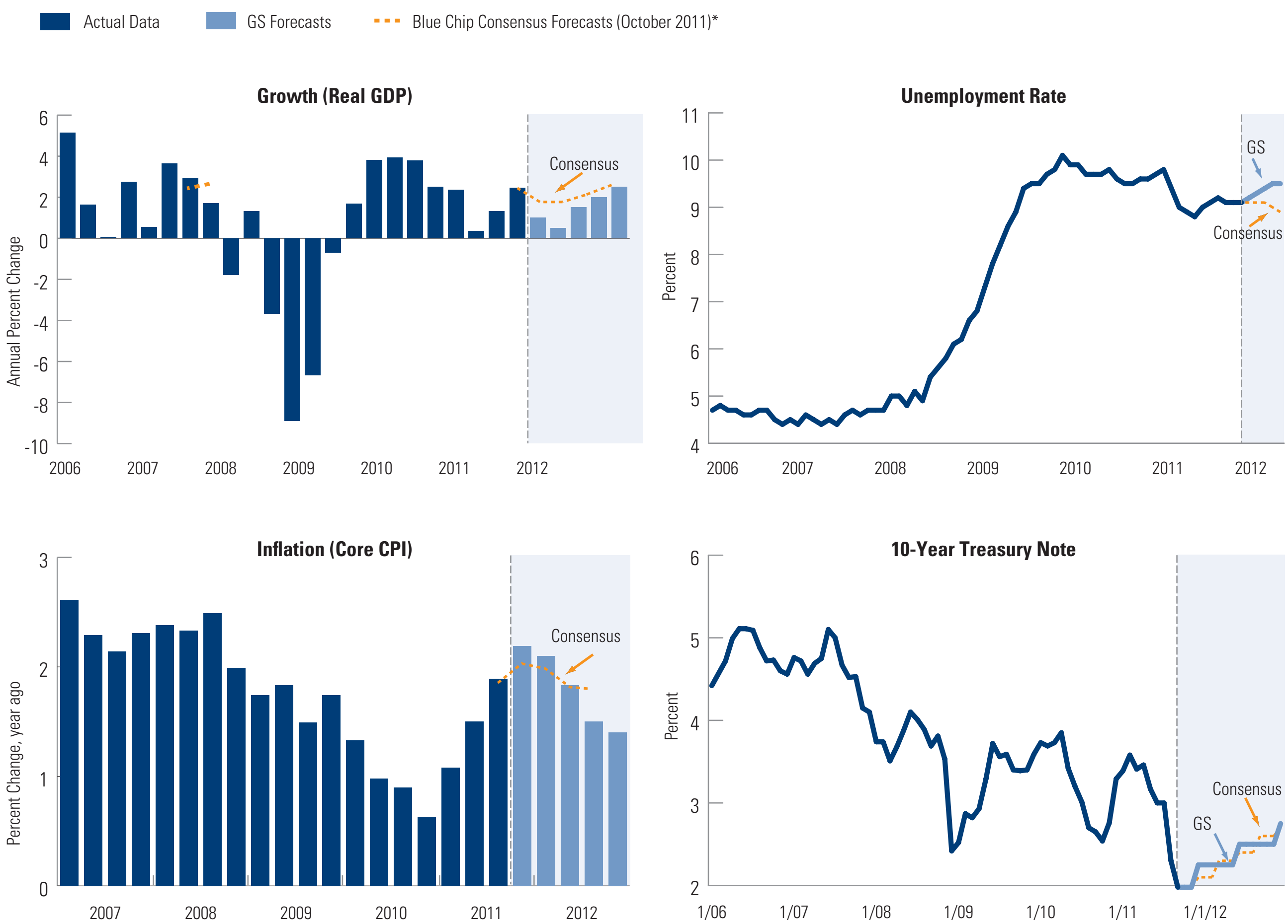
Source: Department of Labor. GS Global ECS Research.

Our Economic Outlook

We are below consensus on near-term growth and expect slight deterioration in the unemployment rate.

Goldman Sachs US Forecasts Versus the Consensus

*Inflation Consensus from Philadelphia Fed (Survey of Professional Forecasters)



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