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This will be the year of the US comeback

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My hunch for the surprise of 2011 is that the US will positively shake people up. For many of the past few years, including preceding the global credit crisis, I shared the worry of many others about the sustainability of the US economy due to the low savings rate, excessive reliance on over-levered consumers and the dependency on foreign capital. However, I have differed from many about the consequences of the crisis in two key respects.

First, due to the power of the so-called Bric economies (Brazil, Russia, India and China) and the other key "growth economies" (Indonesia, South Korea, Mexico and Turkey), I believed that the world economy would recover much more easily than many considered possible. That was last year's surprise. Second, I believed that in spite of the considerable challenges for the consumer, the US economy would not fall into a Japan-style abyss of a lost decade or two. The evidence that the US will not go down this route will, I suspect, be this year's surprise.

On one level, hindsight might even suggest that the global credit crisis wasn't entirely bad for the US, although it is tough for virtually anyone, especially those unemployed, to see that now. But observed from 40,000 feet and a pure macro perspective, the biggest problem the US has had was its low personal savings rate, which prior to the credit crisis was close to zero. The over-leverage of the consumer, the more questionable financial instruments and the large external deficit were all consequences of the low personal savings rate. An economy cannot live off borrowed money forever, especially when it is that of overseas investors.

In this sense, the US has been steadily seeing sizeable improvements since the horrors of late 2008 as its saving rate has risen to 5-6 per cent. Most credible research to my mind suggests that the US really needs to have a personal savings rate in the 8-10 per cent vicinity on a permanent basis, so the US is not there fully yet but arguably it is much closer.

Crucially, the post-credit bubble collapse doesn't seem to have left some other highly powerful attributes of the US economy severely damaged. Its underlying productivity performance, together with its relatively more favourable demographic dynamics, suggested to me that the US might at some stage shift back into a growth trend of close to 3 per cent. The strength of US labour dynamics are a key reason why Japan-style comparisons are far off the mark.

Another wonderful attribute of the US is the decisiveness of policymaking, despite frequent evidence to the contrary in Congress. This is also a marked contrast not only to Japan, but also the hotchpotch of indecisiveness that often characterises continental Europe. Indeed, the behaviour of both the Federal Reserve and post midterm election Congress has probably allowed the momentum to take the US back into its growth trend. The strong asymmetry in which the Fed told everyone last autumn that it was going to undertake additional monetary stimulus and minimise the likelihood of deflationary pressures was exactly what was needed. In addition, the decision by US politicians to enter a further temporary fiscal expansion while committing themselves to medium- to long-term fiscal improvement has given business that further lift that was necessary.

Against this background, most reliable coincident and leading US economic indicators have improved in an accelerating fashion since November, including the critical monthly ISM manufacturing survey and weekly job claims. Last Friday's improvement of 103,000 in monthly jobs is likely to be the start of a more substantial improvement that will bring down the unemployment rate. It will remain in 2011 a long way from where it ideally should be, but at least it will now be moving in the right direction. A number of quarters of 3-4 per cent or more real GDP growth are likely in the next couple of years.

What does this mean for the rest of the world, and markets? While there are always uncertainties, I will take a stab at a few.

First, the post-crisis mood of shifting the blame and accusations will hopefully finally ease, and a less emotional relationship will re-emerge between business and politicians, and probably not just in the US. Second, it will not mean the US will return to pre-crisis operandi but will emerge more as a powerful exporter and with domestic investment rather than consumption being a real strength. The US will share in the Bric and Next 11 (the 11 countries after the Brics in terms of global emerging power) dream and benefits.

Third, for markets, it will probably restore some value to the undervalued dollar against many, if not all currencies (the renminbi being an exception) and it will lead to another powerful leg of the global equity market rally that commenced in spring 2009. The US market might continue to outperform so-called emerging markets for a while, although this will not last. Government bonds are likely to be a net loser, but with growth and still modest inflation, any losses there will be modest.

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