U.S. ECONOMIC PROJECTIONS

T. ROWE PRICE®

March 2009

First Signs of Stabilization Bring Visibility to Gradual Recovery by Year-End

- Recent developments support our judgment that the 2008 Q4 – 2009 Q1 period will prove to be the recession's most intense phase. Moving into the spring quarter, policy stimulus will begin to gain greater traction, and the weight of inventory correction on manufacturing production and employment will begin to ease. Nonetheless, financial sector de-leveraging will sustain restraint on credit supply, and ongoing efforts on the part of households to shore up balance sheets in the face of withering wealth destruction will cap the recovery in aggregate demand. Thus, even after a sharp recession and benefiting from a strong tailwind of policy stimulus, real GDP growth is expected to rise only gradually over the course of 2010, reaching a 3% annual rate by the end of next year.

- Relative to this base case outlook, the distribution of risks is skewed modestly in the direction of weaker growth outcomes, which focus on continuing rapid consumer deleveraging and significant wealth destruction leading to an even higher saving rate; financial sector deleveraging based on declining asset performance; and plummeting global trade which will have second round effects on U.S. manufacturing. Stronger growth scenarios rely on aggressive inventory cuts in the first half leading the need to rebuild inventories in the second half; the prospect that elevated affordability could stabilize housing demand; and the possibility that the efforts to restart credit markets will gain greater traction.

Economic Projections: 2008-2010

	Quarterly Profile					Q4/Q4			Year/Year		
	08:Q4	**09:Q1**	**09:Q2**	**09:Q3**	**09:Q4**	**2008**	**2009**	**2010**	**2008**	**2009**	**2010**
Summary GDP Measures	*(A)*	*(E)*	*(E)*	*(E)*	*(E)*	*(A)*	*(E)*	*(E)*	*(A)*	*(E)*	*(E)*
Real GDP (% Chg., AR)	-6.2	-6.1	-2.0	0.8	1.0	-0.8	-1.7	1.9	1.1	-2.9	1.1
Chain-Weight Price Index	0.5	3.2	0.0	1.7	1.0	2.0	1.5	1.3	2.2	1.7	1.9
Real Final Sales	-6.4	-4.4	-2.4	0.3	0.7	-0.7	-1.5	1.3	1.4	-2.6	0.7
Real GDP Components											
Personal Consumption Expenditures	-4.3	0.0	-0.5	2.2	1.4	-1.5	0.8	1.4	0.2	1.3	1.3
Residential Investment	-22.2	-33.4	-29.1	-20.0	-10.0	-19.3	-23.7	-1.4	-20.7	-24.3	-8.2
Business Fixed Investment	-21.0	-23.3	-14.0	-10.1	-5.0	-5.0	-13.4	2.0	1.7	-14.5	-2.4
Government	1.6	-2.0	7.0	2.2	2.8	3.3	2.4	1.1	2.9	2.5	2.0
Exports	-23.6	-34.1	-22.0	-10.0	-5.0	-1.8	-18.6	2.5	6.2	-18.6	-2.8
Imports	-16.0	-26.8	-12.8	-7.5	-3.5	-7.1	-13.1	2.4	-3.4	-14.6	-1.2
Net Exports ($2000 bil., AR)	-373	-379	-402	-402	-403				-392	-397	-411
Inventory Change ($2000 bil., AR)	-20	-71	-70	-55	-45				-27.6	-59.8	-13.3
Key Indicators											
Personal Saving Rate (%)	3.2	4.9	5.3	5.5	5.3				1.8	5.2	6.3
Corp. Profits (% Chg., YA)	-21.0	-22.6	-26.3	-25.8	-18.3				-10.0	-23.4	-12.7
Nonfarm Productivity (% Chg., AR)	3.2	-1.5	3.9	2.7	2.1	2.7	2.8	1.0	2.9	1.8	1.5
Civilian Unemployment Rate (%)	6.9	8.0	9.0	10.0	10.1				5.8	9.3	10.7
Light Vehicle Sales (Mil., SAAR)	10.3	9.2	9.1	9.1	9.3				13.1	9.2	9.6
Housing Starts (Mil., SAAR)	0.66	0.54	0.44	0.40	0.42				0.90	0.45	0.71
Consumer Price Index (% Chg., AR)	-8.3	-2.4	0.8	1.8	1.7	1.5	0.4	2.2	3.8	-0.8	1.9

Notes: AR = Annual Rate; YA = Year Ago; SAAR = Seasonally Adjusted Annual Rate; A = Actual; E = T. Rowe Price Estimate.
Forecast includes data released through March 24, 2009.

Base Case Outlook: Visibility to Gradual Recovery by Year-End (55%)

Positive Developments

Consumption trends are stabilizing. Retail control, the core sales concept used to estimate consumer purchases of nonauto goods in the GDP accounts, rose 0.5% in February, and January's gain was revised up to +1.7% from +1.2% reported previously. The January-February average of retail control is +3.3% annualized vs. the Q4 average, suggesting that real consumer spending could be roughly unchanged in the current quarter after declining at 4.1% annual rate over the second half of last year.

Housing affordability at all-time highs attracting marginal and first time buyers. Sales of previously-owned (existing) homes rose 5.1% in February, with first-time buyers reportedly accounting for half of that total.

Government stimulus is coming on-line in the second quarter. Congress enacted in mid-February the American Recovery and Reinvestment Act (ARRA), a package of tax relief, aid to state governments, and federal expenditures totaling nearly $800 billion. The Congressional Budget Office (CBO) estimates that the ARRA will add stimulus of $185 billion in the current fiscal year which ends in September, representing 2¼% of GDP at an annual rate. Federal funds are already flowing to states, helping them to sustain income support programs and investment projects that would otherwise have been cut, and tax relief will begin to flow to individuals in the second quarter, and federal infrastructure projects should be significantly under way by mid-year. A further $400 billion (2.8% of GDP) is slated for fiscal year 2010.

Public-Private Investment Program could end 'legacy asset' log jam, laying groundwork for calmer financial markets. The March 23 announcement of the PPIF has helped support sentiment in financial markets – ending six weeks of uncertainty concerning the fate of toxic assets that have been clogging financial institution balance sheets and impeding the flow of credit. Full participation in such a program by a diverse set of investors, as well as momentum in the Fed-Treasury program to support asset-backed securities markets could fortify financial market sentiment and investor risk appetites.

FOMC announcement to increase the size of its purchase programs by $1.15 trillion reduces deflation risks. At mid-month, the FOMC announced further quantitative easing steps. Even as improved functioning of short-term funding markets reduces the balances in the Fed's temporary liquidity facilities, expansion of its program to purchase mortgage-related assets, and initiation of a Treasury securities purchase program give the Fed ample scope for offsetting growth in the permanent component of its balance sheet, the portfolio of securities held outright.

Negative Developments

Labor market remains profoundly weak. The pace of layoff announcements slowed in February, and weekly jobless claims have stabilized in a 630,000-650,000 range. Nonetheless, these readings are consistent with monthly job losses in excess of 600,000 and with a continued rise in the unemployment rate. Such conditions will weigh on personal income and sustain a cautious tenor in household decision-making.

Business fixed investment and global trade falling sharply. Shipments of capital goods excluding defense and aircraft – the core concept used to estimate business purchases of nontransportation equipment in the GDP accounts – fell 6.7% in January, and nonresidential construction declined by 4.3%, pointing to continued sharp contraction in business fixed investment in the current quarter. The business retrenchment is global, and continues to weigh on trade performance. As a result, real merchandise exports plunged 8.6% from December to January, and the merchandise trade deficit widened to $-44 billion from $42.9b in December and a fourth quarter average of $-43.0b.

Base Case Outlook

On balance, these developments support our judgment that the 2008 Q4 – 2009 Q1 period will prove to be the recession's most intense phase. Moving into the spring quarter, policy stimulus will begin to gain greater traction, and the weight of inventory correction on manufacturing production and employment will begin to ease. Nonetheless, financial sector de-leveraging will sustain restraint on credit supply, and ongoing efforts on the part of households to shore up balance sheets in the face of withering wealth destruction will cap the recovery in aggregate demand. Thus, even after a sharp recession and benefiting from a strong tailwind of policy stimulus, real GDP growth is expected to rise only gradually over the course of 2010, reaching a 3% annual rate by the end of next year.

Alternative Scenarios and the Probability Distribution of Possible Outcomes

Weaker Growth Scenario: *Wealth effects spur accelerated consumer deleveraging; asset quality deteriorates; global recession takes exports growth down further (25% probability)*

- Consumer deleveraging could become more aggressive, leading to a faster increase in the saving rate. Accelerated wealth destruction, tighter credit and rising unemployment spur a sharper rise in household saving. Downward pressure on home prices is destroying wealth of all homeowners (including those with no mortgage), and financial asset values have also been pared sharply; household net worth declined by $5.1 billion (45 percentage points of disposable income) in the fourth quarter. Against this backdrop, a more aggressive move to rebuild balance sheets and curb credit use could boost the saving rate faster than envisaged in the base case outlook, reducing growth in consumer spending dollar-for-dollar relative to income.
- Deteriorating financial asset performance forces a more rapid financial sector deleveraging. Commercial bank loan performance continues to deteriorate at a rapid pace; bank loan delinquencies rose to a 17-year high 4.74% of all loans in Q4, with the rate of increase rising broadly across the range of loan categories. Mortgage delinquencies continue to run well ahead of charge-offs in the fourth quarter, pointing to further erosion of bank capital and suggesting that the quality of impaired mortgage-related assets on financial institutions' balance sheets continues to decline.
- Global recession will reverberate to a longer more protracted contraction in trade and domestic U.S. manufacturing. The base case outlook envisages a sharp decline in exports on par with the 2001 experience. The depth and breadth of the global slowdown could result in a deeper drop in exports and a sharper capital spending pullback as firms cut costs to defend profit margins. Manufacturers will suffer as both internal and export demand declines.

Stronger Growth Scenario: *Lean inventories spark a cycle of accumulation; increased affordability in housing; monetary policy takes hold (20% probability)*

- As inventories become leaner and short term borrowing rates more attractive, the inventory cycle turns positive. Just as aggressive inventory correction is adding to downside momentum in the current quarter, the opposite could hold true for firms coming out of the recession. With production on a steep downward trajectory, inventories could quickly appear too lean if demand were to stabilize, or even fall more slowly. And from a steep pace of liquidation in the current quarter, even a more gradual rate of inventory reduction would add to growth.
- Housing inventory is being worked off, valuation measures improving, and housing demand stabilizing. Recent declines in mortgage rates and the persistent weakness in home prices have helped push housing affordability to record levels. The combination of another 10% to 15% price decline, low mortgage rates, and the extension of the first-time homebuyer tax credit along (limit increased to $8,000) could help stabilize housing conditions and provide a boost to second half growth.
- Fed/Treasury efforts help restart asset securitization and broader economic activity. With the Term Asset-Backed Securities Loan Facility (TALF) is up and running, plans to expand this facility to encourage activity in a broader array of asset classes comes into clearer focus. The Treasury's Financial Stability Plan, as presented on March 23, expands the TALF to include previously-issued, high-quality asset-backed securities, including those derived from residential and commercial mortgages.'

Offices and Investor Centers of the T. Rowe Price Group of Companies

UNITED STATES OFFICES

Baltimore
100 East Pratt Street
Baltimore, Maryland 21202
410-345-2000

Financial Center
10090 Red Run Boulevard
Owings Mills, Maryland 21117
410-345-2000

Corporate Campus
4515 Painters Mill Road
Owings Mills, Maryland 21117
410-345-2000

Technology Center
11550 Cronridge Drive
Owings Mills, Maryland 21117
410-345-2000

Colorado Springs
2260 Briargate Parkway
Colorado Springs, Colorado 80920
719-278-5700

San Francisco
333 Bush Street, Suite 2550
San Francisco, California 94104
415-772-9950

Tampa
4211 West Boy Scout Blvd., 8th Floor
Tampa, Florida 33607
813-554-4000

Long Beach
4401 Atlantic Avenue, Ste. 200
Long Beach, CA 90807

INTERNATIONAL OFFICES

Netherlands
Strawinskylaan 1047
1077 XX Amsterdam
The Netherlands
31.(0)20.333.62 00

England
60 Queen Victoria Street
London EC4N4TZ
England
011-44-20-7651-8200

INTERNATIONAL OFFICES

Japan
Yamato Seimei Building – 20th Floor
1-7, Uchisaiwai-cho 1-chome
Chiyoda-ku, Tokyo 100-0011
Japan
011-81-33-503-6277

Hong Kong
Room 802-809
8/F Jardine House
1 Connaught Place
Central
Hong Kong
011-852-2536-7800

Singapore
No. 290 Orchard Rd.
#14-04 Paragon
Singapore 238859
011-65-836-0098

Argentina
Carlos Pellegrini 1149, piso 12
(1009) Buenos Aires
Argentina
011-54-11-4394-4089

Australia
Levels 25 & 29 Chifley Tower
2 Chifley Square
Sydney NSW 2000
Australia
011-61-2-9293-2894

Denmark
Lautrupsgade 7
2100 Copenhagen Ø
Denmark
011-45-33-36-05-00

Luxembourg
Boulevard Royal 26
2449 Luxembourg
Grand Duche de Luxembourg

INVESTOR CENTERS

Baltimore
105 East Lombard Street
Baltimore, Maryland 21202
410-345-5757

Owings Mills
4515 Painters Mill Road
Owings Mills, Maryland 21117
410-345-5665

Colorado Springs
2260 Briargate Parkway
Colorado Springs, Colorado 80920
719-278-5700

Boston
386 Washington Street
Wellesley, Massachusetts 02481
781-263-1200

Los Angeles
Warner Center (Main Plaza Level)
21800 Oxnard Street, Ste. 270
Woodland Hills, California 91367
818-932-5300

San Francisco
1990 N. California Blvd., Ste. 100
Walnut Creek, California 94596
925-817-1900

Tampa
4211 West Boy Scout Blvd., 8th Floor
Tampa, Florida 33607
813-554-4000

Washington, DC
900 17th Street, NW
Farragut Square
Washington, DC 20006
202-466-5000

New Jersey
51 JFK Parkway, 1st Floor W
Short Hills, New Jersey 07078
973-467-6800

Northbrook
40 Skokie Boulevard, Suite 100
Northbrook, IL 60062
847-313-4500

Oak Brook
1900 Spring Road, Suite 104
Oak Brook, Illinois 60523
630-645-9700

Tysons Corner
1600 Tysons Blvd., Suite 150
McLean, Virginia 22102
703-873-1200

Garden City
1100 Franklin Avenue, Suite 101
Garden City, NY 11530
516-535-6100

T. ROWE PRICE® U.S. ECONOMIC PROJECTIONS

100 East Pratt St., Baltimore, MD 21202
1-800-225-5132/www.troweprice.com

T. Rowe Price Economics Department, T. Rowe Price Associates, Inc.

Chief Economist
Alan Levenson
Alan_Levenson@troweprice.com

Associate Economist
Jared Franz
Jared_Franz@troweprice.com

Research Associate
Linda Smith
Linda_Smith@troweprice.com