

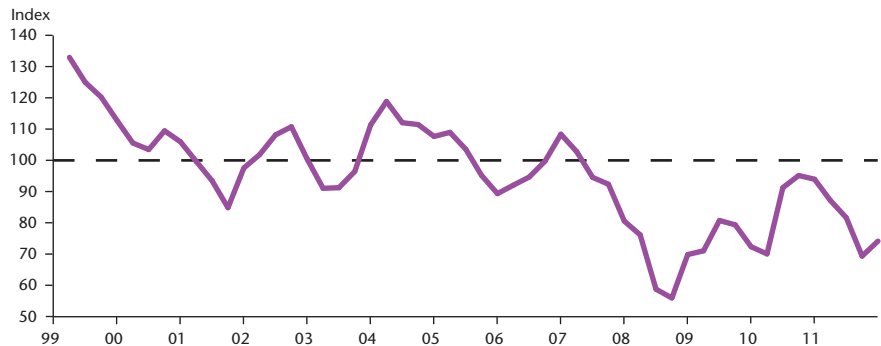
# US Financial Reality Index – Q4 2011

January 2012



In Q4 the financial situation facing US households improved for the first time since Q3 2010, according to research from the Alliance Trust Economic Research Centre. Our US Financial Reality Index rose from 69.4 to 74.2, but has remained below the critical level of 100 since Q2 2007. All three sub-indices increased over the quarter, the first time since Q3 2010 that a broad based improvement has been seen. However the two main contributors to the small improvement recorded over the quarter were a lower unemployment rate and a small increase in house prices, both of which come from very low levels. A lower gasoline price also helped to improve conditions in Q4. Despite this high prices of basic goods continue to weigh on household budgets and muted wage growth means that real earnings growth is negative. On top of this, overall economic conditions are still very weak and household net wealth is still hindered by high levels of debt. Although our index increased slightly in Q4, the muted reading still points to slower growth in consumer spending over the coming quarters.

## US Financial Reality Index



## Contact

### Shona Dobbie

Head of Economic Research Centre

Alliance Trust PLC  
8 West Marketgait, Dundee DD1 1QN

Tel +44 (0)1382 321000

Fax +44 (0)1382 321185

Email [contact@alliancetrust.co.uk](mailto:contact@alliancetrust.co.uk)

Web [www.alliancetrust.co.uk](http://www.alliancetrust.co.uk)

## Financial Reality Index

The Alliance Trust US Financial Reality Index rose from 69.4 in Q3 2011 to 74.2 in Q4 2011. The index has been below the critical level of 100 since Q2 2007.

## Economic Background – increased from 54.4 to 61.9

The economic background component rose from 54.4 to 61.9 in the final quarter of the year but, despite this,

## Economic Background



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the sub-index has been below the critical level of 100 since early 2008. The improvement over the quarter was helped by a fall in the unemployment rate but, at 8.5%, this remains high. At the same time, there was a deterioration in GDP growth which acted as a drag on the economic background index. So, despite lower unemployment, economic conditions facing households remain very difficult.

**Household Budget – rose from 92.9 to 96.3**

The household budget index rose from 92.9 to 96.3 in Q4, the first increase since Q3 2010. The improvement in Q4 was small and the index remains below the critical level of 100 for the second consecutive quarter. In Q4, the pressure on household budgets was alleviated due to a lower gasoline price. At the same time, low mortgage rates continue to keep mortgage service costs low. But, despite this, household budget conditions remain tough due to muted wage growth and still elevated levels of basic goods prices. High inflation also continues to erode household purchasing power.

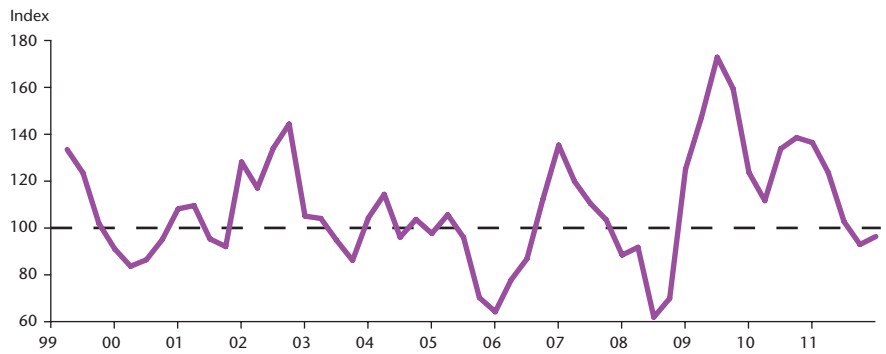
**Net Wealth – increased from 45.0 to 49.5**

The net wealth index rose from 45.0 to 49.5 but, despite this small improvement, the index has been below the critical level of 100 since Q4 2005. The net wealth index is also the weakest sub-index for the second consecutive quarter. The slight increase in Q4 was helped by a stabilisation in equity markets and a small improvement in house prices. The house price index is, however, still very weak and levels of household debt remain high.

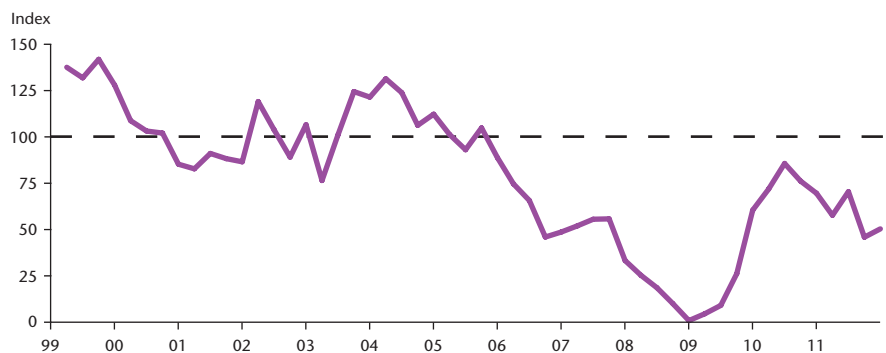
**Summary and conclusions**

Our US Financial Reality Index has recorded a small improvement in Q4 after falling to its lowest level since Q3 2008 in the previous quarter. The index remains below the critical level of 100, indicating that financial conditions facing households are still negative when compared with the long run average. Over the quarter, all three sub-indices

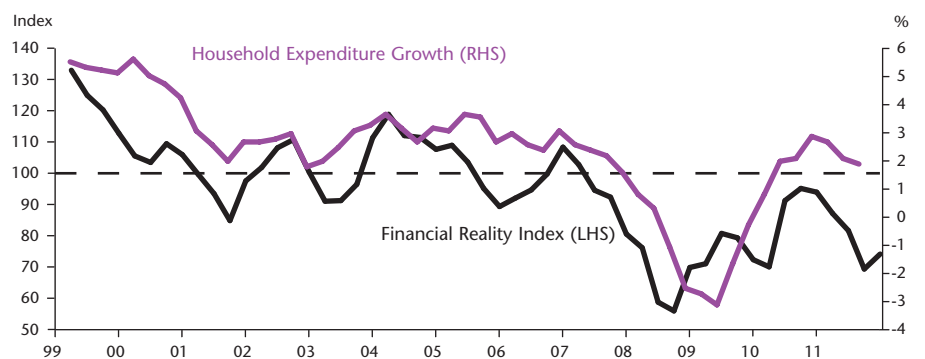
**Household Budget**



**Net Wealth**



**Financial Reality Index v Household Expenditure**



recorded small improvements. A lower unemployment rate helped to boost the economic background index, the lower gasoline price was supportive of household budgets and a small increase in house prices, from a very low level, lifted the net wealth component. But, despite these improvements, all three sub-indices are below the critical level of 100 for the second consecutive quarter, highlighting that conditions facing households remain very difficult.

Index and actual consumer spending growth, as can be seen in the chart above. In Q3 2011 consumer spending posted growth of 2%, having slowed for the past three quarters. Despite a small increase in Q4, our index points to continued difficult financial conditions and a further deterioration in consumer spending growth.

Sources: Reuters EcoWin, In-house Analysis

Over the course of our 13 year study there has been a very close relationship between our US Financial Reality