



NABE Economic Policy Survey[®]

National Association For Business Economics

FOR FURTHER INFORMATION CONTACT:
Stuart Hoffman 412-762-3101
Melissa Golding 571-236-2820

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NABE Panel: \$100 per Barrel Oil Would Cause Recession August 2006

*The NABE Economic Policy Survey presents the consensus of a panel of 195 members of the National Association for Business Economics. Conducted semiannually, this survey was taken August 1 – August 15, 2006. May be reprinted in whole or in part with credit given to NABE. View the survey results, including complete tabulations, online at www.nabe.com. This is one of three surveys conducted by NABE. The other two are the NABE Outlook and the NABE Industry Survey. **David Wyss** of Standard & Poor's, **Kathleen Camilli** of Camilli Economics, and **Catherine L. Mann** of the Institute for International Economics, conducted the analysis for this report.*

“NABE members believe that oil prices above \$100 per barrel would probably cause a recession but don’t believe they will go that high,” says **Stuart Hoffman**, NABE President and Chief Economist, PNC Financial Services Group. “They see little prospect of significant substitution of other technologies for oil in the next decade.”

Survey Highlights

Terrorism continues to be the biggest short-term problem facing the U.S. economy, according to 34% of respondents, up from 26% in March. Energy was the biggest fear of 29% of respondents, up from 23%. Worries about inflation moved into third place, ahead of the trade deficit.

In the longer run, the federal deficit and an inadequate educational system are the primary problems, each chosen by over one-fifth of respondents. The largest strength continues to be the flexibility of the economy, with technology close behind.

Monetary policy is about right. Although 71% of respondents said current monetary policy is about right, the panel split on where it should go, with 29% wanting further rate hikes, 17% wanting cuts, and 53% preferring to leave rates at their current level. Only 57% of respondents expect the Fed to tighten, down from 89% six months ago. Most (53%) of respondents feel that press reports of poor communication by the Fed are overplayed, and that communication is no worse than usual.

Fiscal policy is too loose, according to 68% of respondents. Although 75% thought budget deficits should be cut, only 17% thought deficits would actually drop, while 35% expect deficits to increase. How to reduce the deficit was less clear; the panelists voted that extending the tax cuts was their first fiscal priority, while raising taxes or allowing the cuts to expire ranked second, showing a sharp division of opinion.

Most economists believe that the Middle East violence will not result in major disruptions to oil supplies. Only 35% thought that war would expand. The median estimate of next summer’s oil price was \$75 per barrel, about the level that it was when the survey was taken. About 25% expect prices to drop by at least \$10 per barrel, and a similar percentage expect a \$10 per barrel or more increase. On average, the panelists thought that oil would have to reach \$100 per barrel to cause recession.

How to reduce oil dependence was less unclear. Only 38% of respondents thought that any combination of policies could allow the U.S. to eliminate reliance on non-North-American oil. On a scale of 1 to 5 (1 most promising), ethanol and biodiesel were seen as the most promising at 2.3, followed closely by nuclear (2.4). Hydrogen was seen as least

likely to succeed (5.3). Nearly half (48%) of respondents think the world has sufficient oil, but that we should reduce dependence on the Middle East.

Health care costs are not likely to be controlled, according to 53% of respondents, but more costs will be pushed onto patients. The new Medicare Part D drug benefit, which has added to costs, should be controlled by allowing more bargaining with the drug companies, but only 12% thought it should be repealed, although a further 16% recommended it be restricted to only indigent patients.

Survey Details

Greatest Short-Term Risk to the U.S. Economy: Terrorism remained the major short-term worry for the U.S. economy. The economists have become much more worried about both energy prices and inflation, but federal deficit fears have dropped off, although the trade gap remains a concern.

Short-Term Risks to the U.S. Economy (Percent of survey panelists responding)

	Survey Month				
	Aug 2004	Mar 2005	Sep 2005	Mar 2006	Aug 2006
Defense/terrorism	40	24	20	26	34
Energy prices	6	11	30	23	29
Inflation	9	6	5	3	12
Current account deficit	5	15	11	13	11
Excessive household/corporate debt	5	2	9	7	5
Govt spending/ deficit	23	27	13	14	2
Unemployment/employment	6	2	1	1	1

Greatest Long-Term Challenges to the U.S. Economy: Worries about the health care system have diminished, but economists are less happy with the education system and more worried about energy issues than six months ago. The federal deficit has become the primary long-term worry, although short-term fears have dropped off.

Longer-Term Challenges to the U.S. Economy (Percent of survey panelists responding)

	Survey Date				
	Aug 2004	Mar 2005	Sep 2005	Mar 2006	Aug 2006
Federal deficit	17	21	22	22	23
Education system	19	16	21	16	21
Growth of elderly population/dependency ratio	23	22	18	21	17
Health care	22	23	23	22	16
Energy issues	6	4	4	8	13
Competitiveness	6	8	7	5	4

Strengths in the U.S. Economy: Flexibility remains our economy's greatest strength, followed by the U.S. capital market and technological lead. All other choices (including monetary policy, quality of the work force, democratic government, and legal and judicial institutions) were under 5%.

U.S. Economic Strengths (Percent of survey panelists responding)

	Survey Date				
	Aug 2004	Mar 2005	Sep 2005	Mar 2006	Aug 2006
Flexible labor markets/economy	36	35	42	35	39
Productivity/ technology	35	35	26	29	27
Deep capital markets	10	12	11	16	18

Monetary Policy Is About Right: The panelists give the Federal Reserve another strong vote of confidence, with 71% saying monetary policy is about right, up from 65% a year ago. Only 13% feel monetary policy is too tight, with the same number (14) saying it is too loose. Looking ahead, only 29% believe monetary policy should tighten over the

next six months, down from 66% 18 months ago, with 53% saying it should remain unchanged. Most (57%) think short-term interest rates will increase, with respondents split between a 0.25 and a 0.5 percentage point increase over the next six months.

NABE Panelists' Views on Monetary Policy

(Percent reporting)

Survey Date	Current monetary policy is:		
	Too restrictive	About right	Too stimulative
Aug 2006	13	71	14
Mar 2006	8	76	16
Sep 2005	5	65	30
Mar 2005	3	63	33
Aug 2004	4	59	36

Fiscal Policy: Over two-thirds of respondents felt current policy is too stimulative, down from 76% in March, while only 8% believe it is too tight. An even greater percentage (75%) of respondents believe fiscal policy should become more restrictive, but only 17% believe fiscal policy will tighten, while 35% believe it will become even looser.

Panelists Views on Fiscal Policy

(Percent reporting)

	Current fiscal policy is:			Fiscal policy <u>should be</u> in two years:		Fiscal policy is <u>expected to be</u> in two years:	
	Mar 2006	Aug 2006		Mar 2006	Aug 2006	Mar 2006	Aug 2006
Too Stimulative	76	68	Tighter	82	75	16	17
About right	12	20	Same	9	13	47	47
Too tight	6	8	Looser	7	10	35	35

Note: Dates refer to survey dates.

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