

# The Outlook for the U.S. Economy

## *Slow and steady wins the least ugly contest*

Adam S. Posen

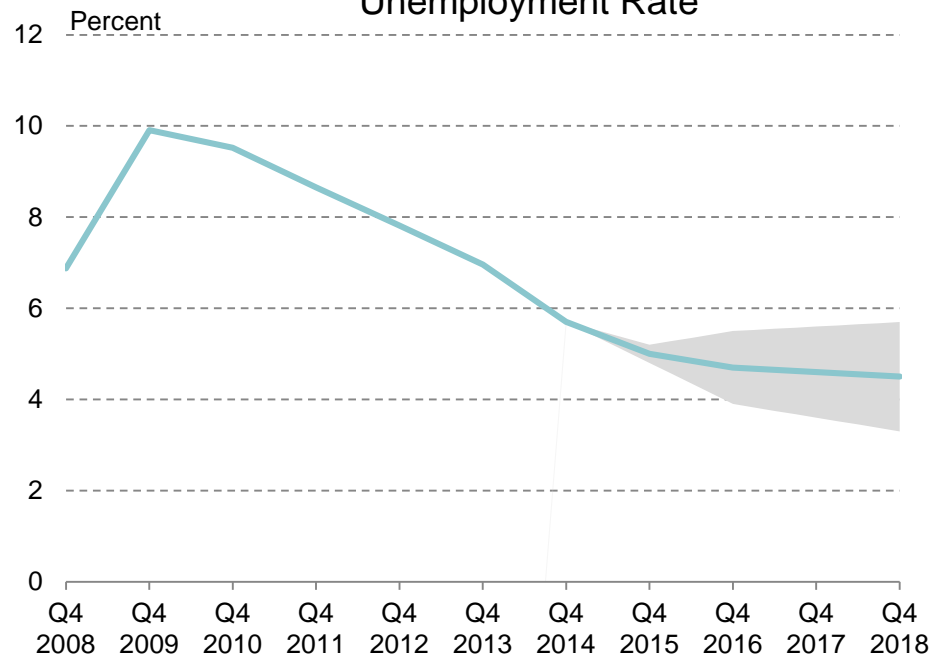
*President*

Peterson Institute for International Economics

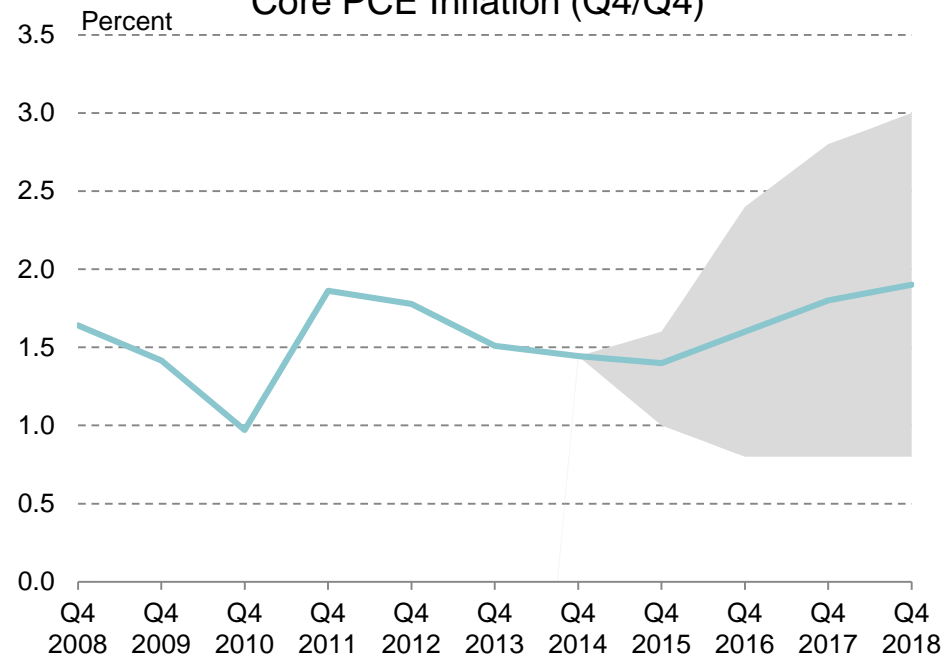
April 11, 2016

# US slow and steady: Moderate Growth, Continued Low Inflation

Unemployment Rate



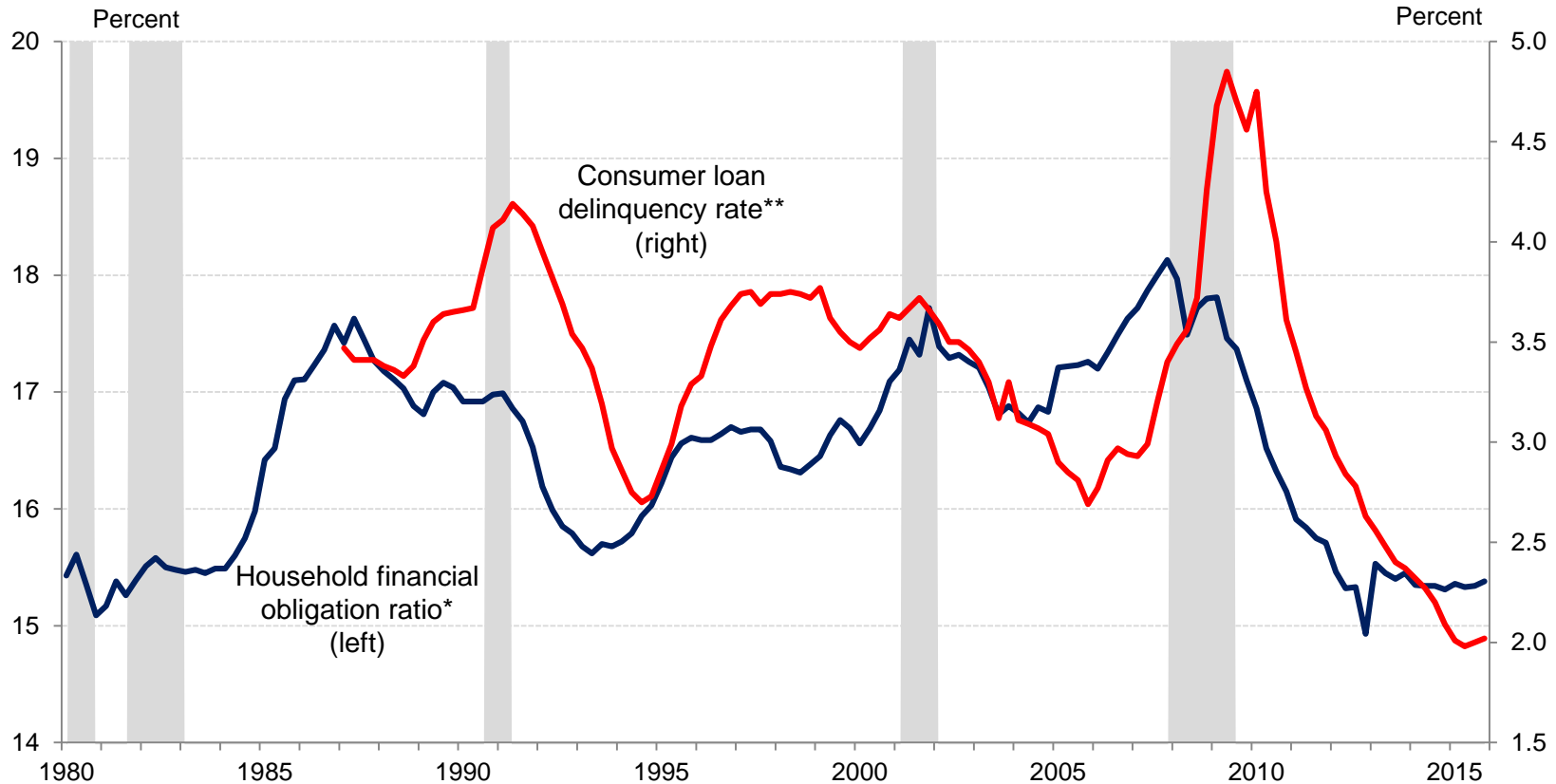
Core PCE Inflation (Q4/Q4)



Forecast	2014	2015	2016	2017	2018
Real GDP Growth (Q4/Q4)	2.5	2.4	1.8	2.0	1.8
Unemployment (Q4)	5.7	5.0	4.7	4.6	4.5
PCE Price Inflation (Q4/Q4)	1.1	0.5	1.6	1.9	1.9
Core PCE Price Inflation (Q4/Q4)	1.4	1.4	1.6	1.7	1.8

Note: Gray-shaded areas represent 70% confidence bands.

# Household Financial Conditions May Have Shifted Secularly for the Better

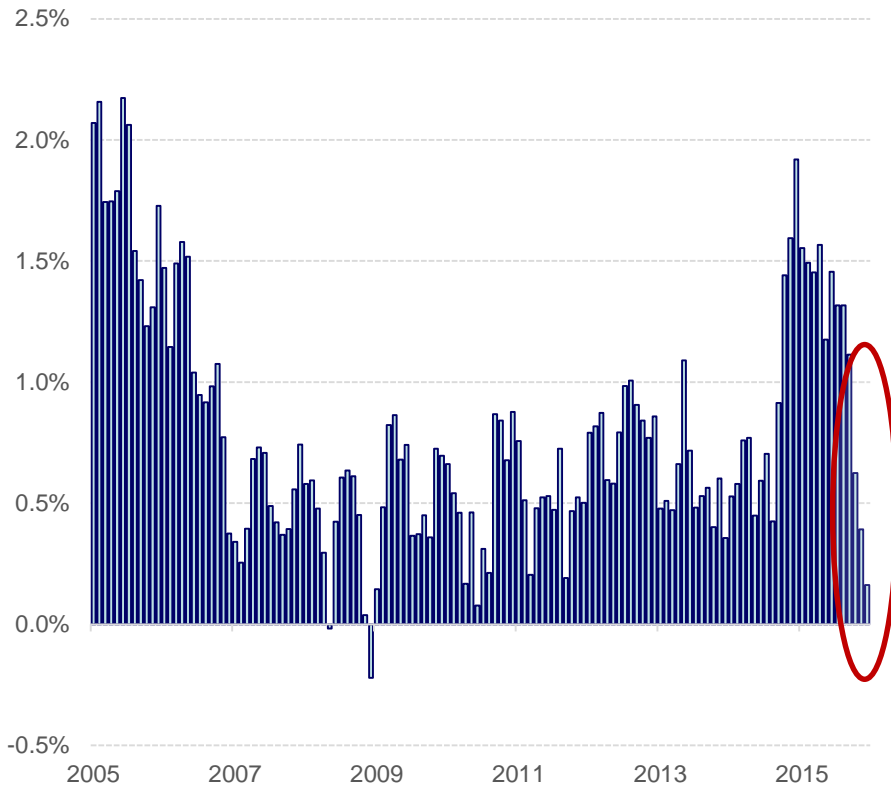


\*The ratio of debt-service pmts. to disposable personal income. Debt-service includes estimated req'd pmts. on outstanding mortgage and consumer debt, plus auto lease pmts., rental pmts. on tenant-occupied property, homeowners' insurance, and property tax pmts.

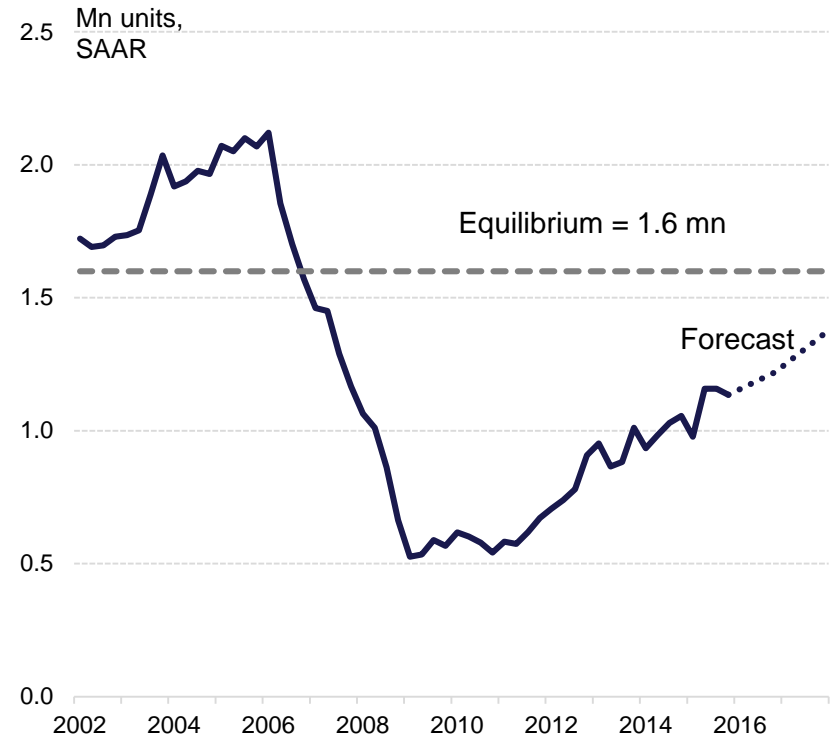
\*\*Nonaccrual loans and loans past due 30 days or more and still accruing interest.

# Housing Still Has Room to Catch-Up

Household Formation, 12-month change

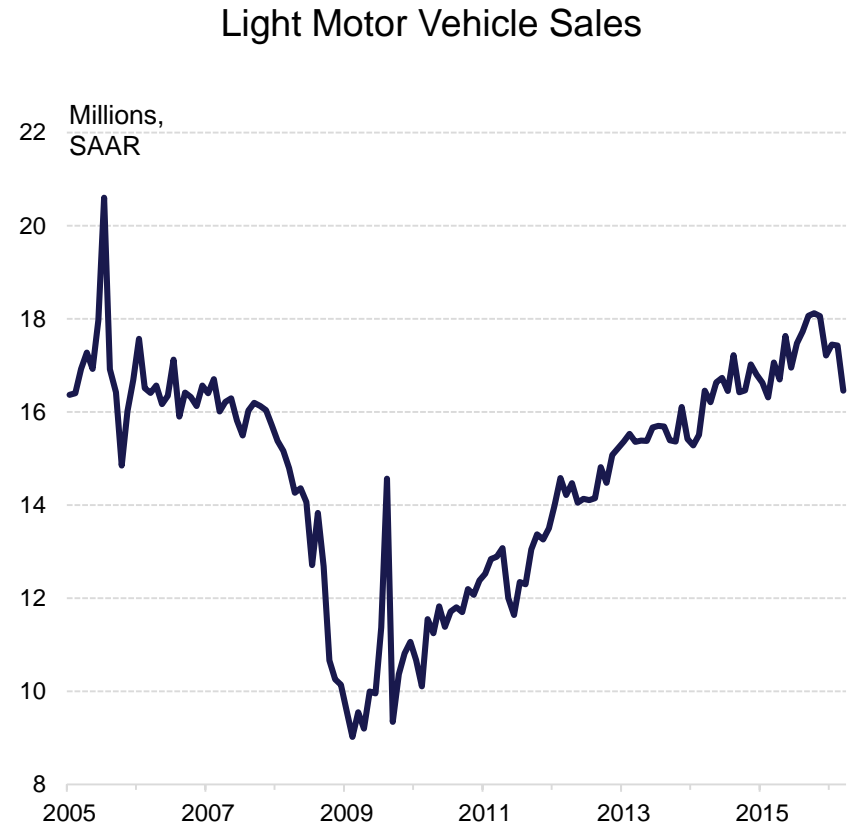
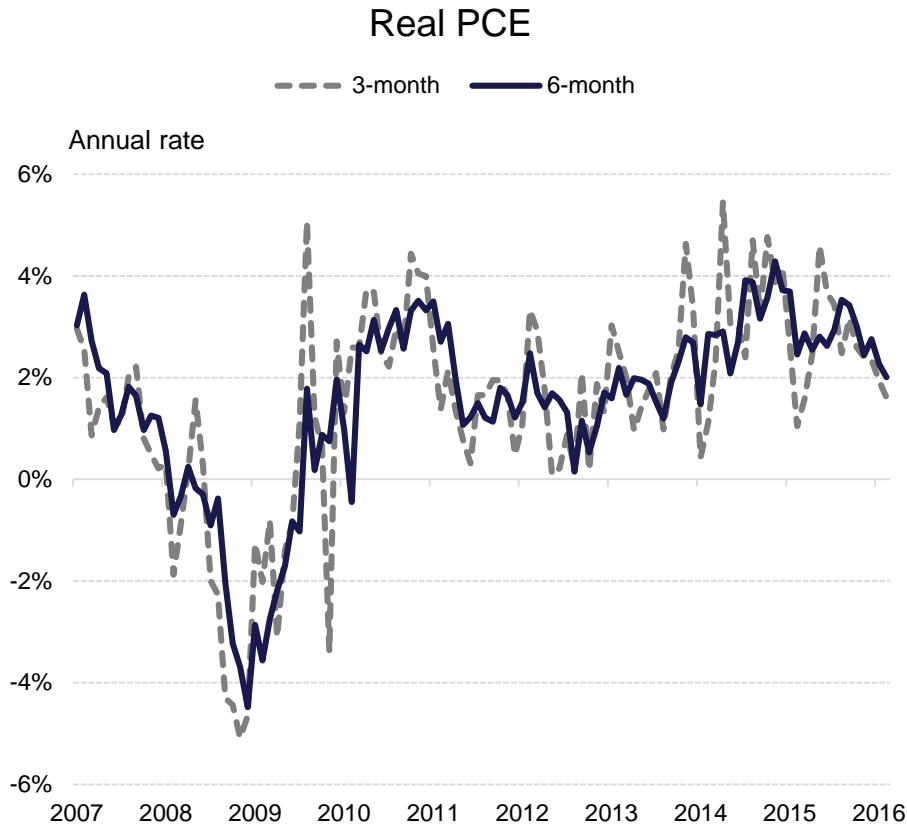


Total Housing Starts



Source: Census via Haver Analytics, Consensus Forecasts.

# Consumption Growth Remains Solid *and is not leveraged like 10 years ago*

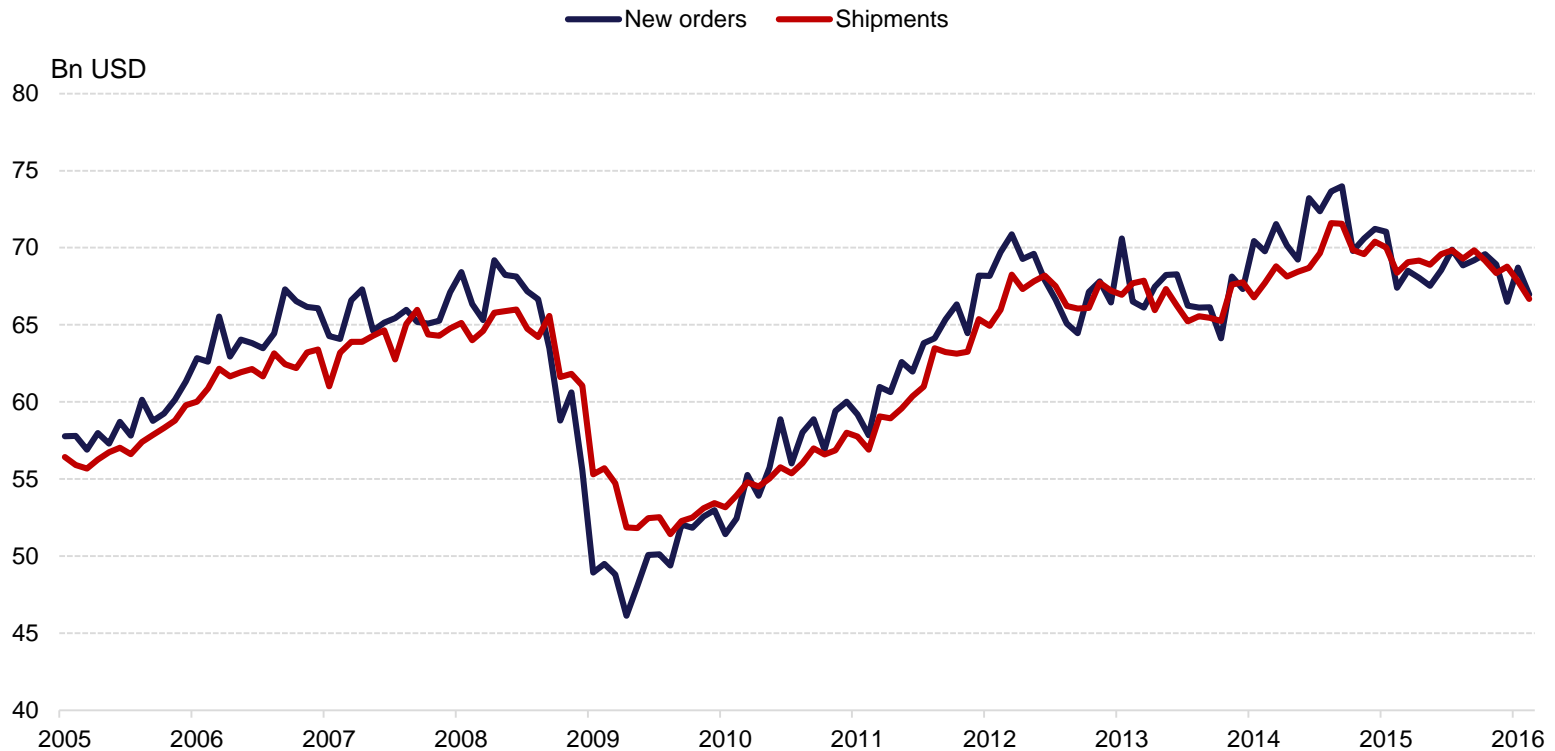


Source: BEA via FRED.

# Business Investment Remains Upside Risk

## *But only at best (less so given dollar strength)*

Nondefense Capital Goods Excluding Aircraft

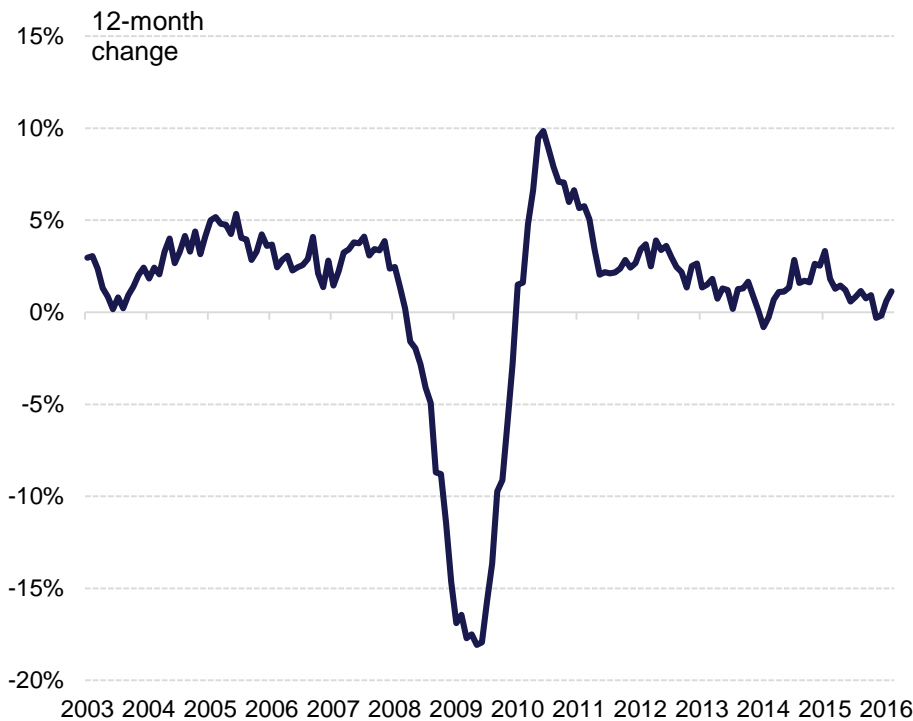


Source: Census via FRED.

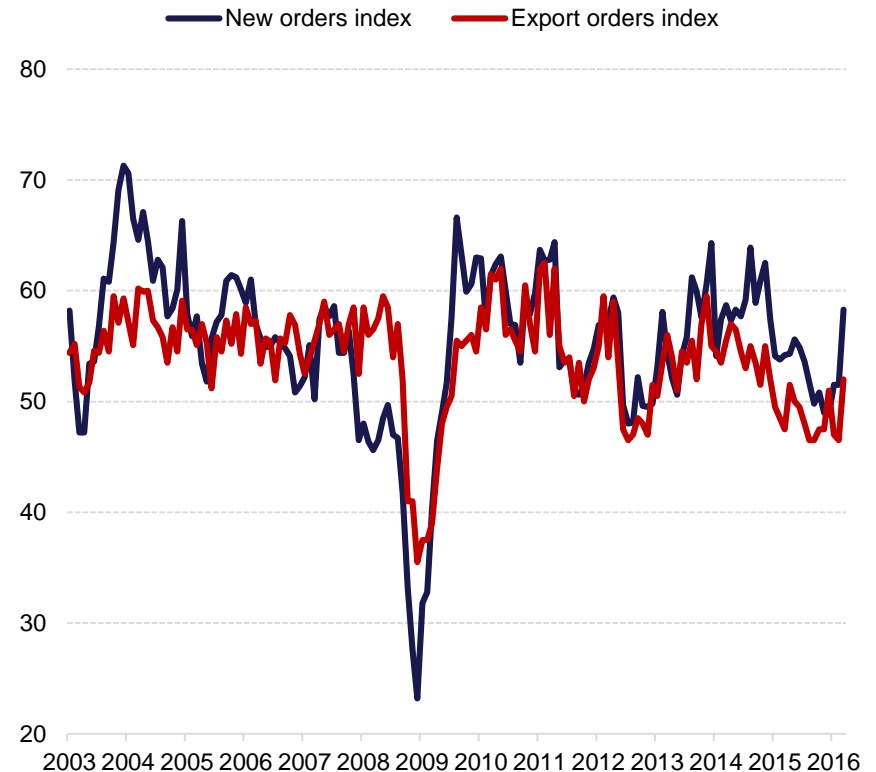
# Manufacturing Is Under Dollar Pressure

Real GDP level is >0.5% lower in 2016 and 2017 from NX

Manufacturing Industrial Production



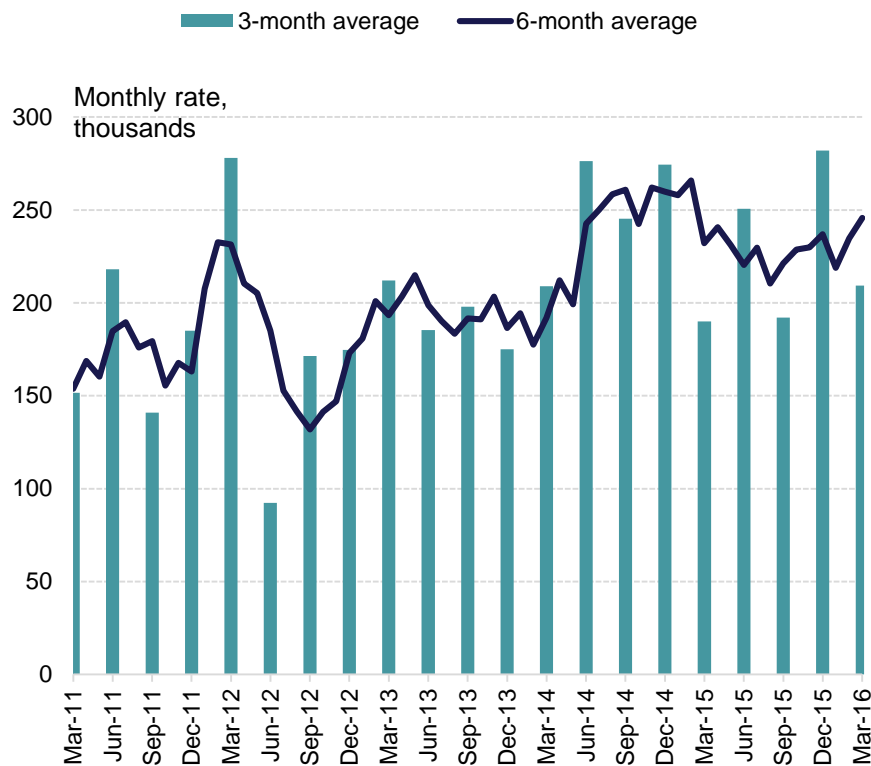
ISM Manufacturing



Source: Federal Reserve, Institute for Supply Management via FRED.

# The Labor Market Continues to Improve *Though underemployment remains in 2 senses*

### Change in Nonfarm Payrolls



### Initial Jobless Claims

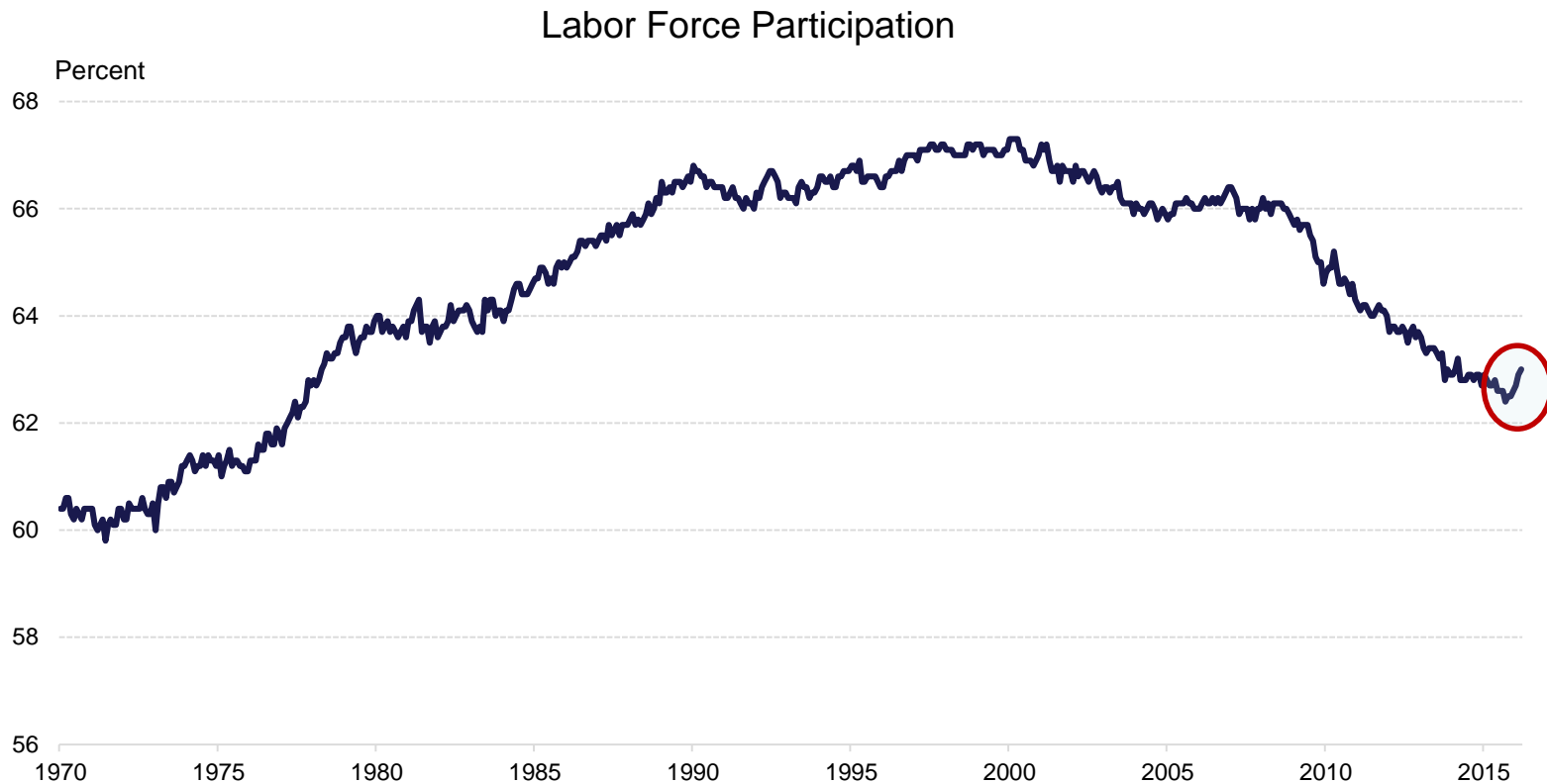


Source: BLS, Department of Labor via FRED.



# The Decline in Labor Force Participation

## *How much is secular vs. cyclical?*

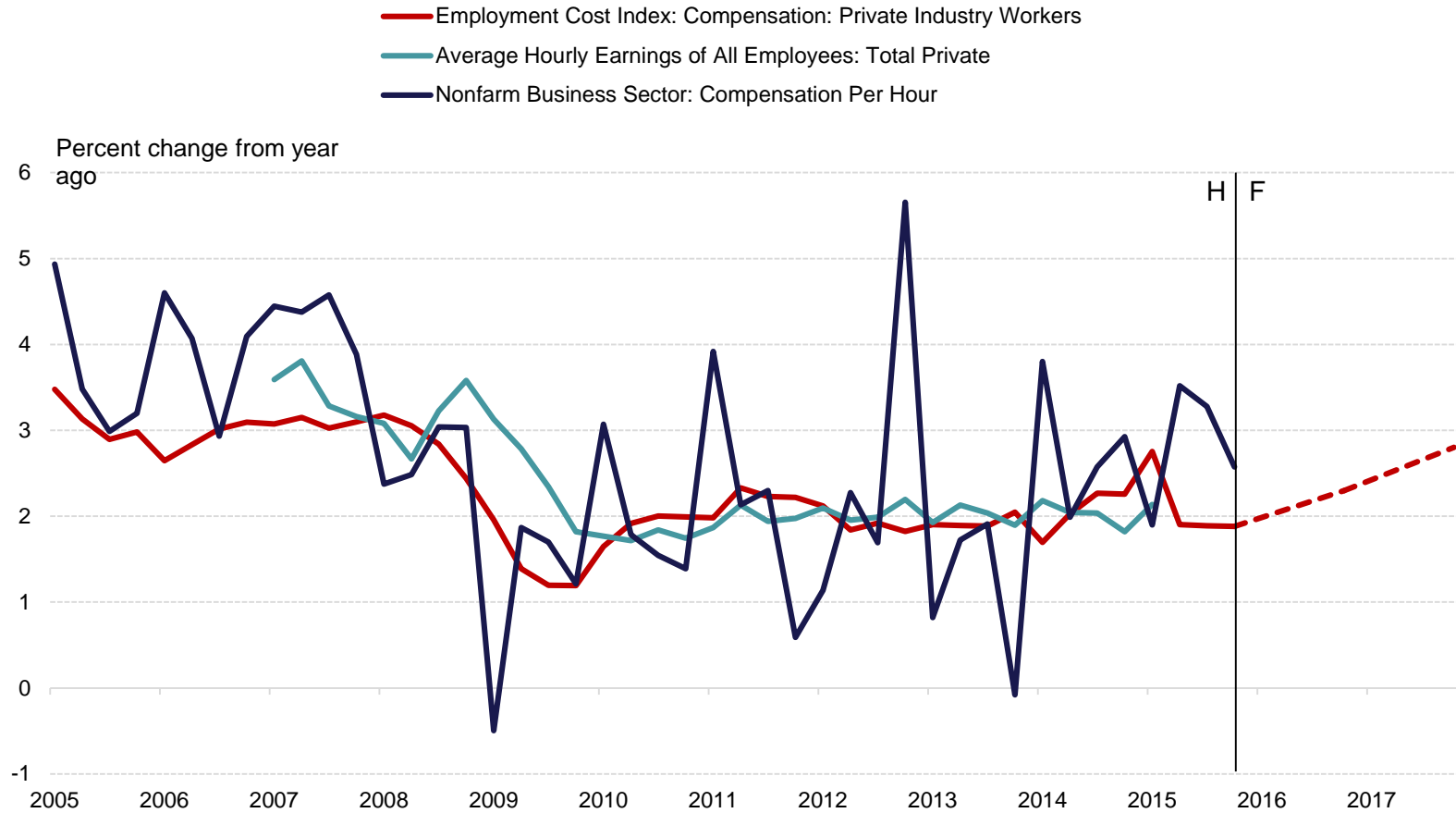


Source: BLS via FRED.

# Labor Compensation May Remain Subdued

*Ger, JP, UK have low unemployment and low wage growth, too*

Labor Compensation

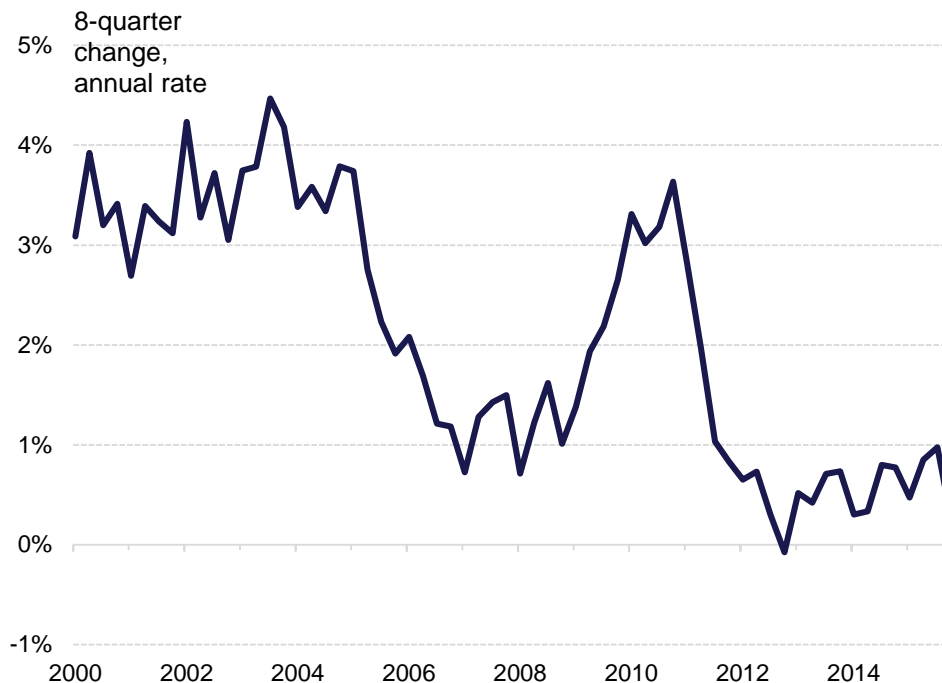


Source: BLS via FRED, Consensus Forecasts.

# U.S. Productivity Growth Will Remain Slow

## *Sustainable Potential Growth is Low*

Nonfarm Business Output per Hour



Potential Output Growth

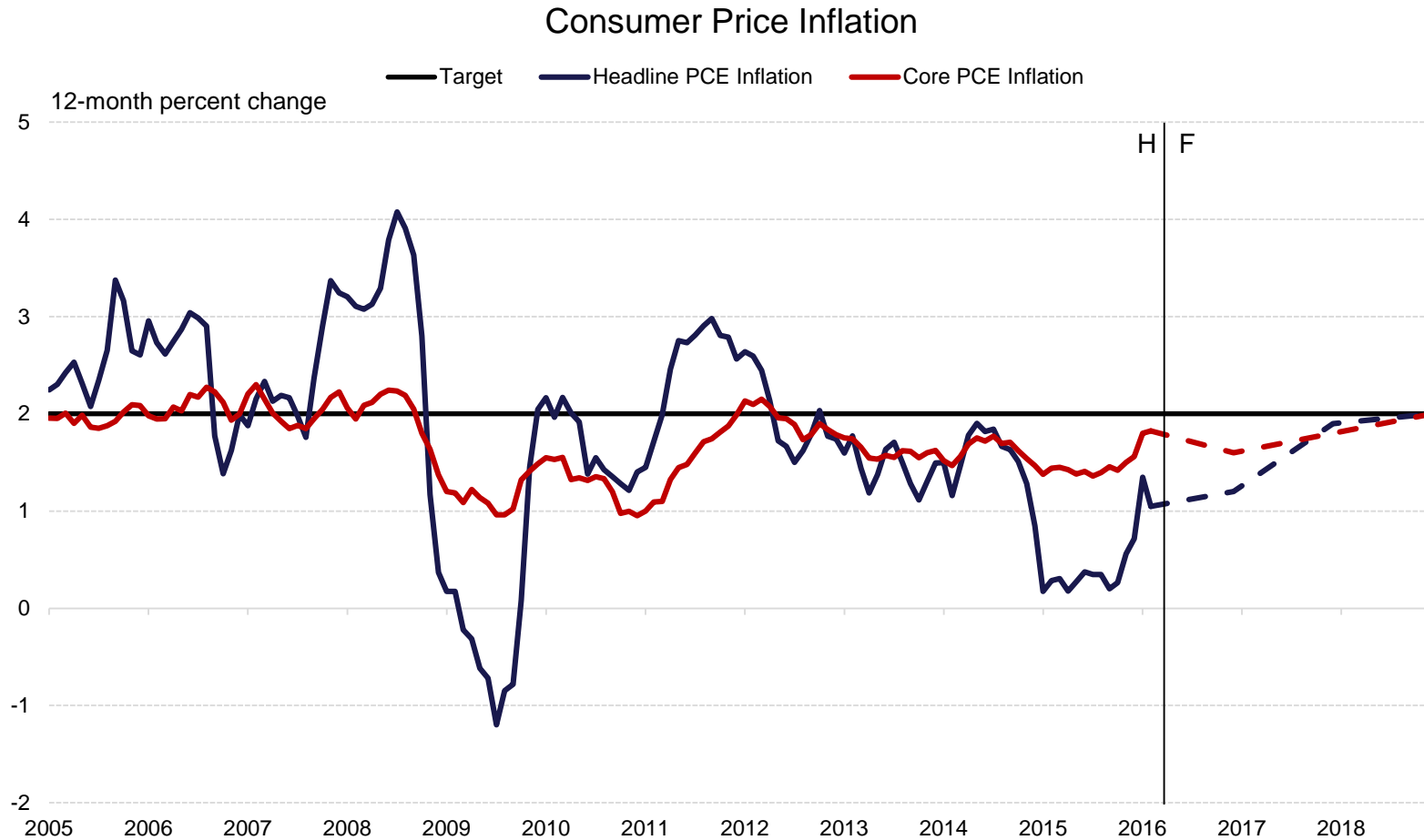
	2002- <u>2007</u>	2008- <u>2018</u>	2019- <u>2025</u>
Potential GDP	2.8	1.7	<2.0
Potential Labor Force Growth	0.9	0.5	0.5
Potential Labor Productivity Growth	1.9	1.2	<1.5

**What we see may be what we get**  
Whatever the reason for the slowdown,  
it will likely take years to recover

Source: BEA via FRED.

# Price Inflation Will Remain Low

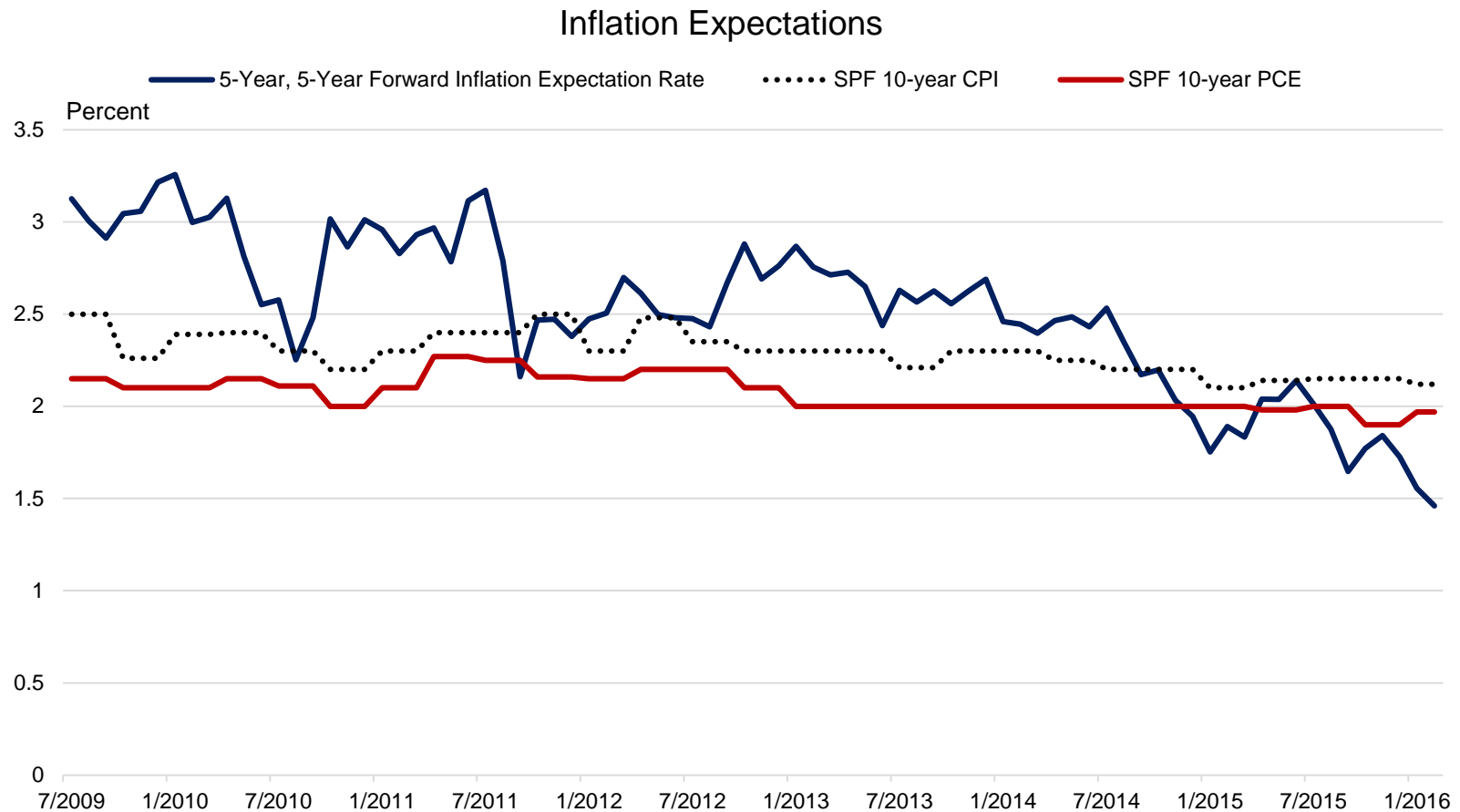
## *Do not expect dotty fine-tuning from FRB*



Source: BEA, Federal Reserve.

# Inflation Expectations: Anchored or Drowning?

## *Depends how distorted 5y5y is by risk aversion*



Source: Bloomberg, FRB Philadelphia via Haver Analytics.

# The Unnoticed Debate on Fed Strategy

- Canonical inflation targeting is not just forward looking but pre-emptive at a 2- to 3-year time horizon
- Waiting to see inflation (“Whites of their eyes”) would be a shift in strategy not dependent on data
- There are solid economic arguments for such a shift
  - Stickiness (not explosiveness) of inflation expectations
  - Structural decline in wage bargaining power
  - Room to experiment on unemployment (*a la* Solow)
  - US relative upside versus rest of world may limit upside shocks

# The Outlook for the U.S. Economy

- Slow growth is sustainable and recession risk is only mildly elevated – still no reason for expansion to end
- Slow and steady, however, is enough to win the global least ugly contest, which puts a floor under the dollar
- The risks remain skewed to the downside, but the tail is thinner than it was, and the skew is less than it was
- Fed policy is not all that critical at this point, can assume one hike before election or not, one after, no big mistake
- The absence of wage pressures or investment demand indicates that the US needs structural reform for growth

# Slides on Call

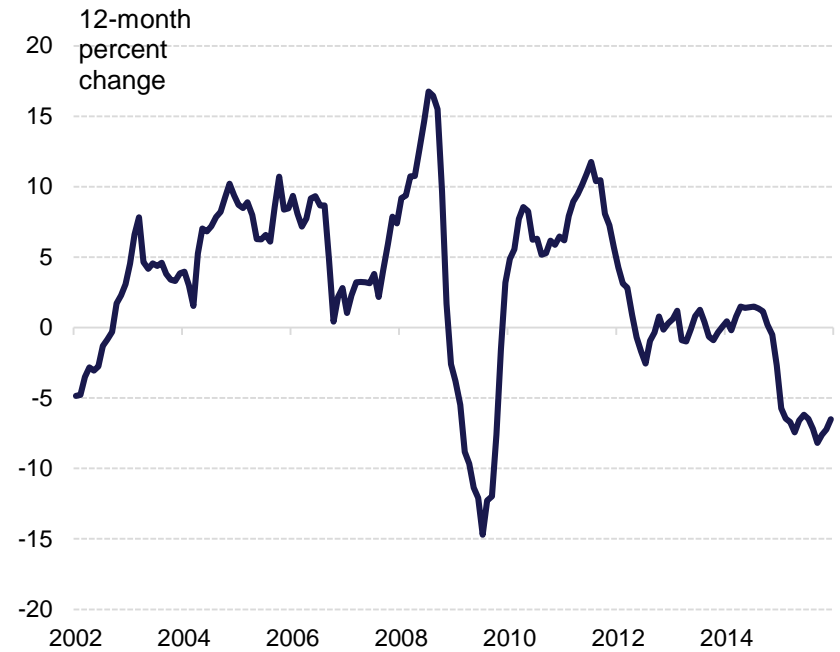


# No Price Pressures in the Pipeline

Import Prices Excluding Fuels



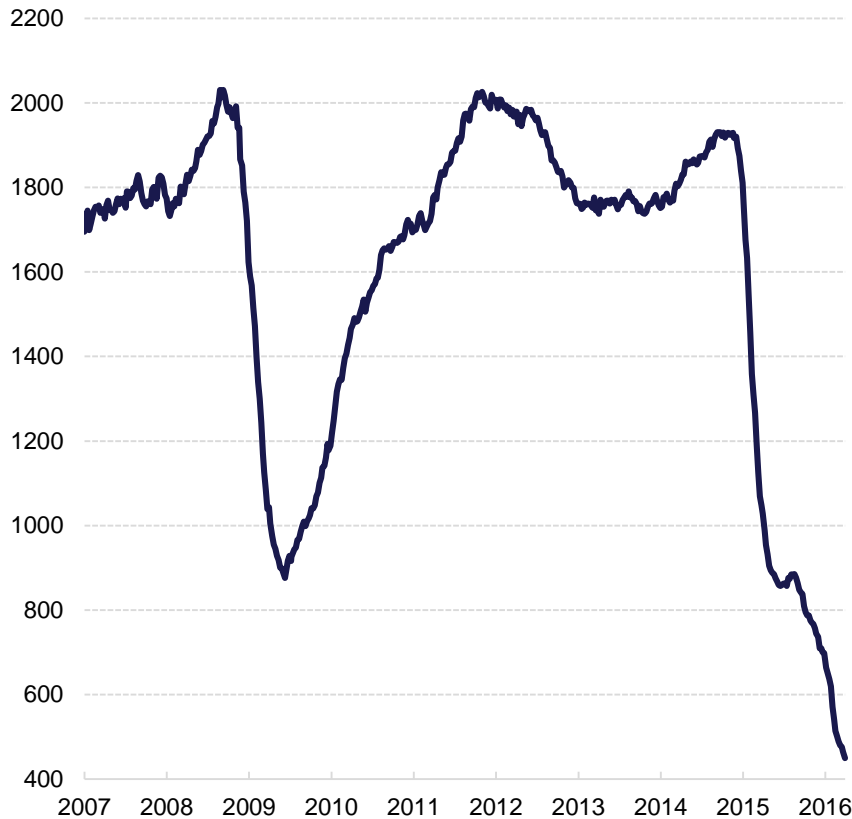
PPI Processed Intermediate Goods



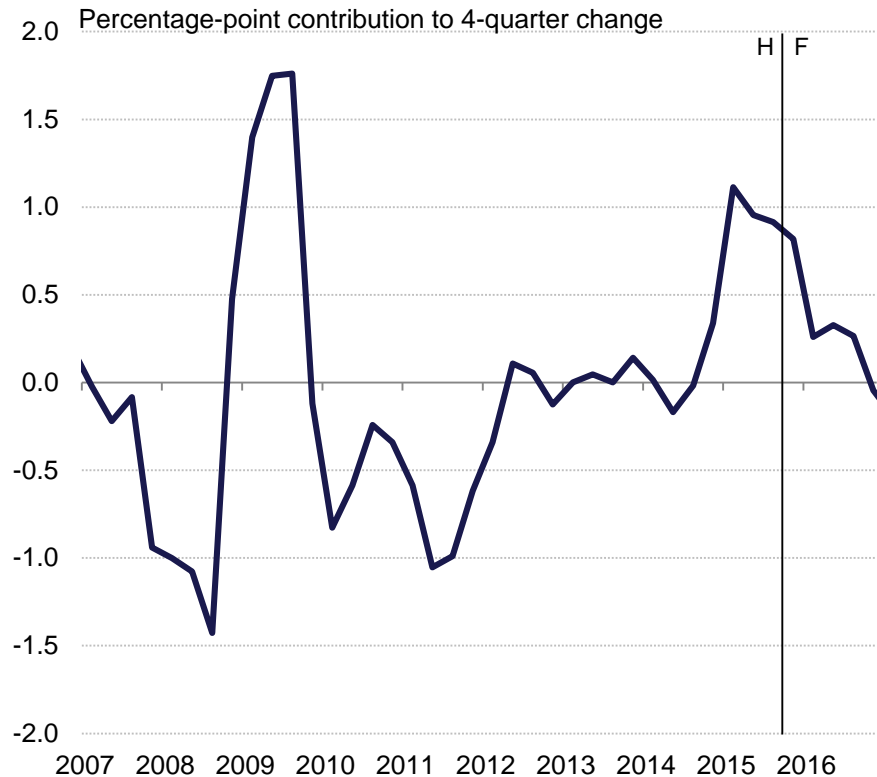
# Energy Sector: Don't Overthink This

*It's not that big, the sign is right*

### U.S. Oil and Gas Rig Count



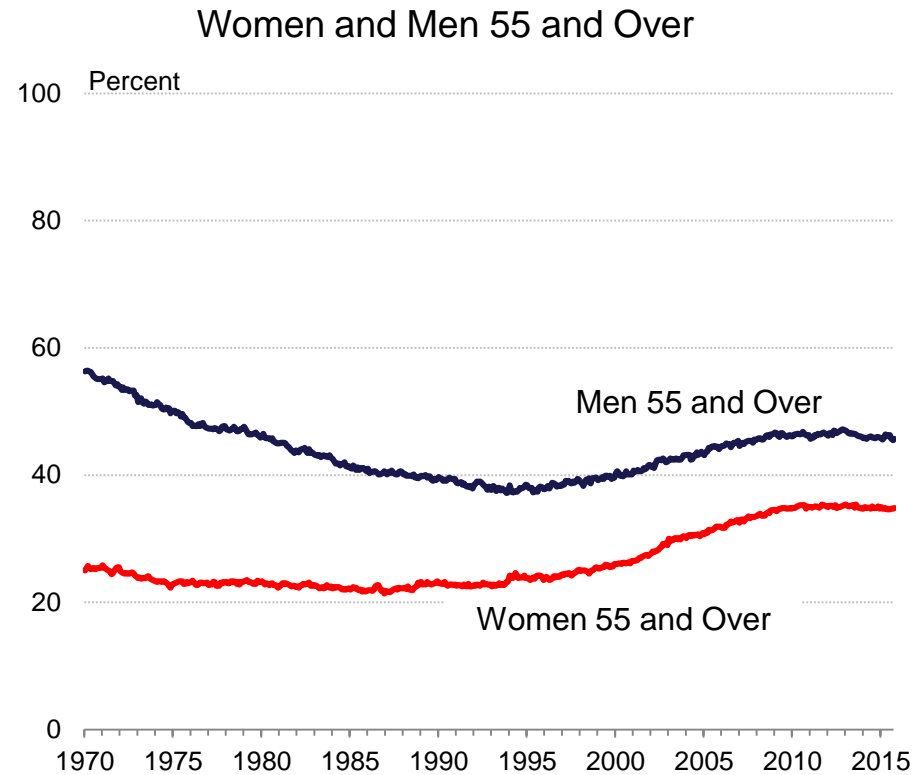
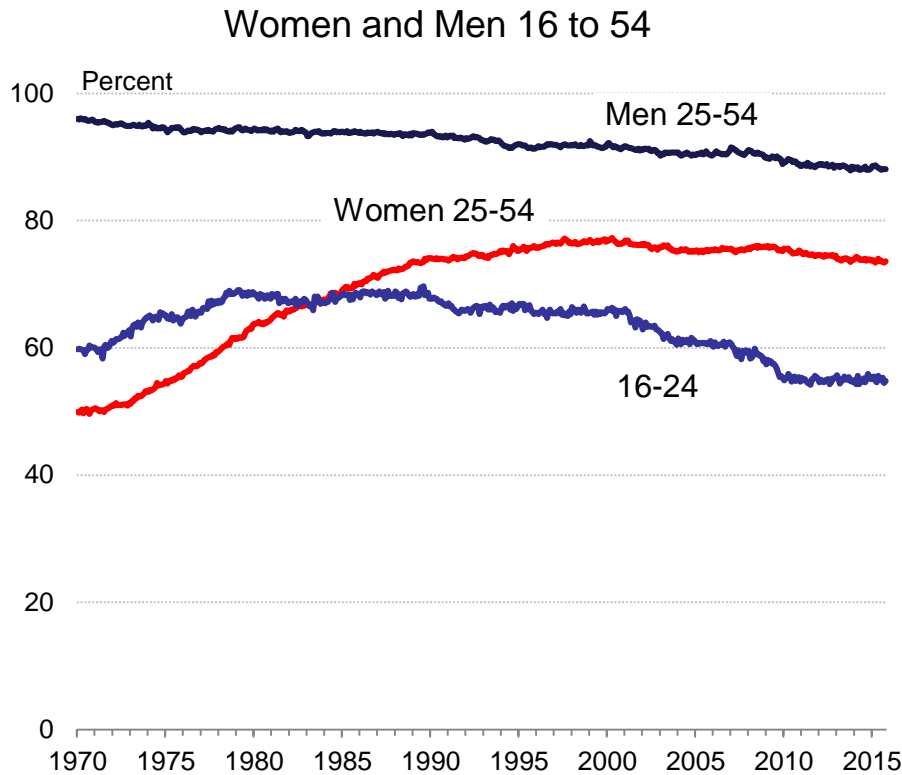
### Contribution of Energy Price Changes to Growth of Real Disposable Personal Income



Source: Baker Hughes, MPI/Macroeconomic Advisers, BEA.

# Demographic Shifts Have Reduced Participation

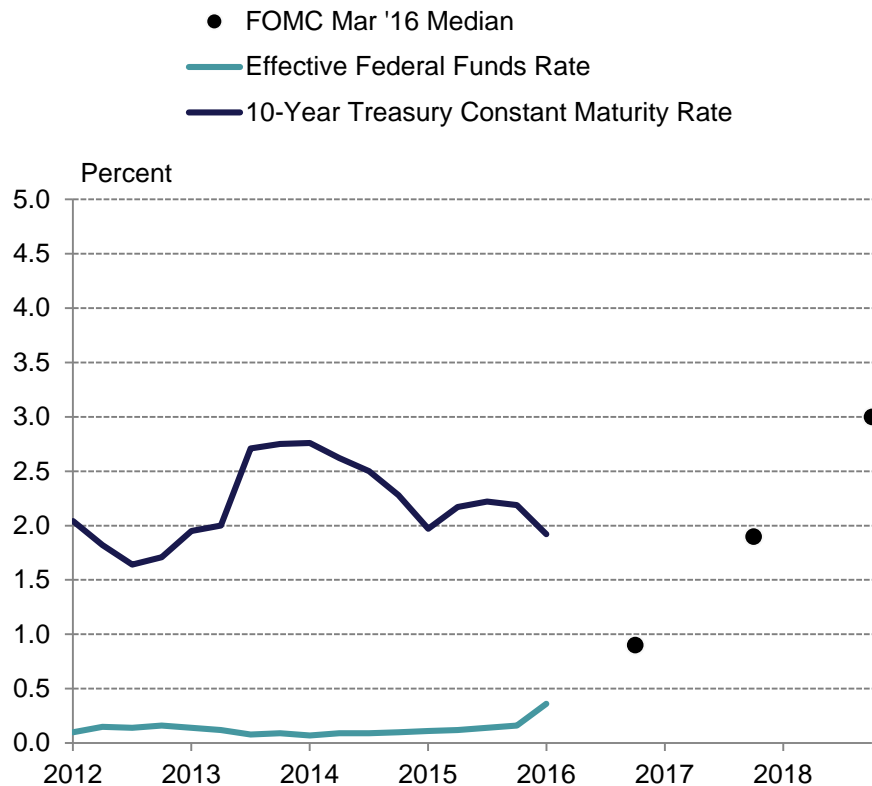
## Participation Rates by Gender and Age



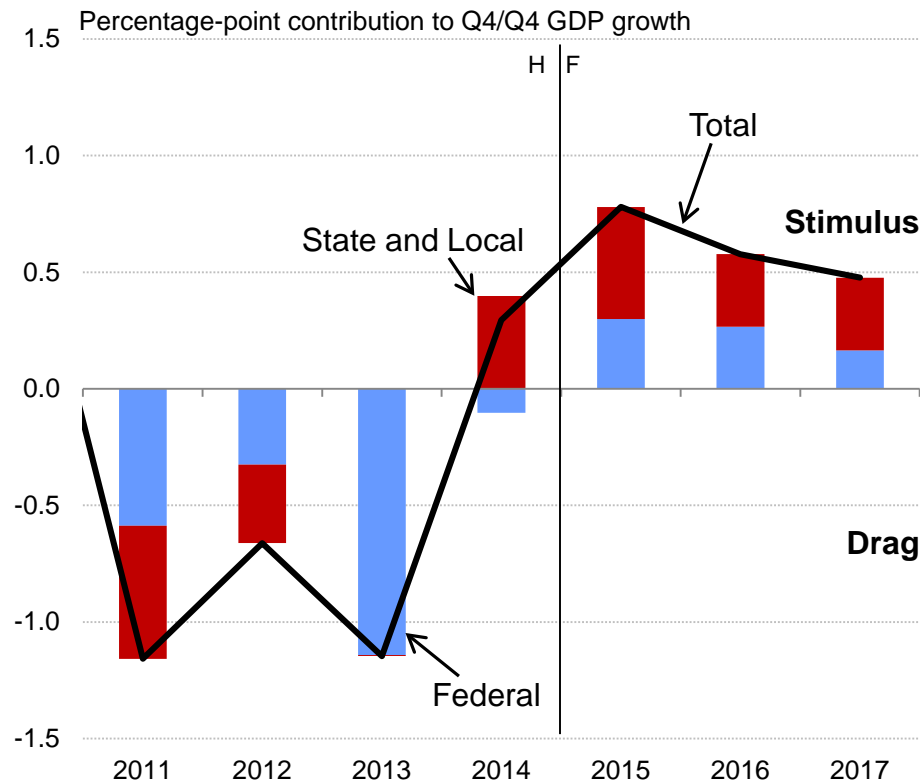
Source: BLS.

# Tighter Monetary Policy and a Fiscal Boost from State and Local Governments

## Interest rates



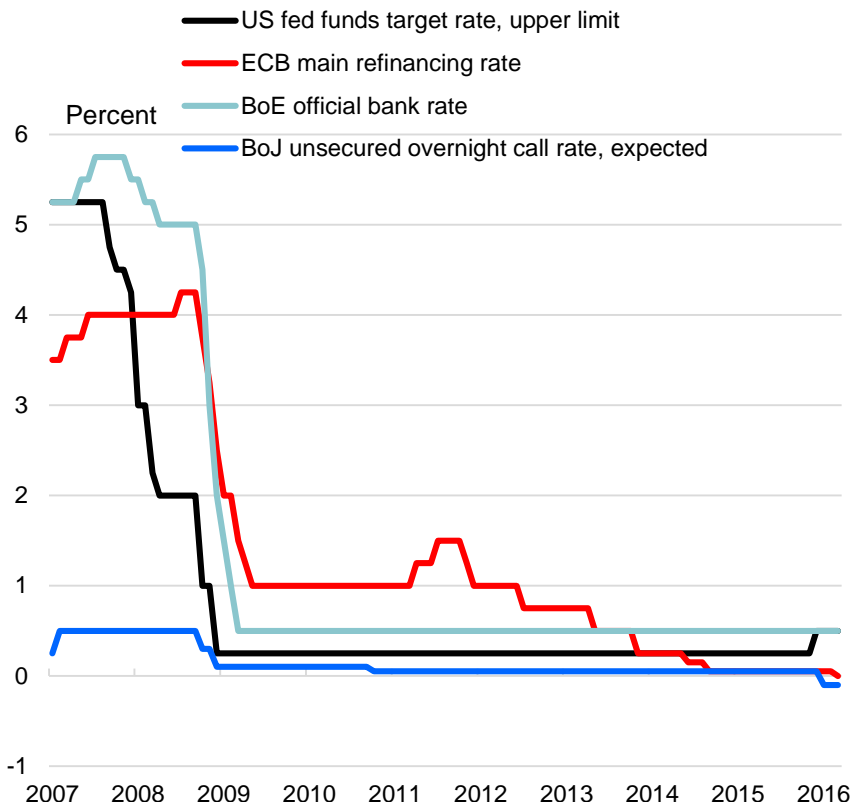
## Fiscal Impetus



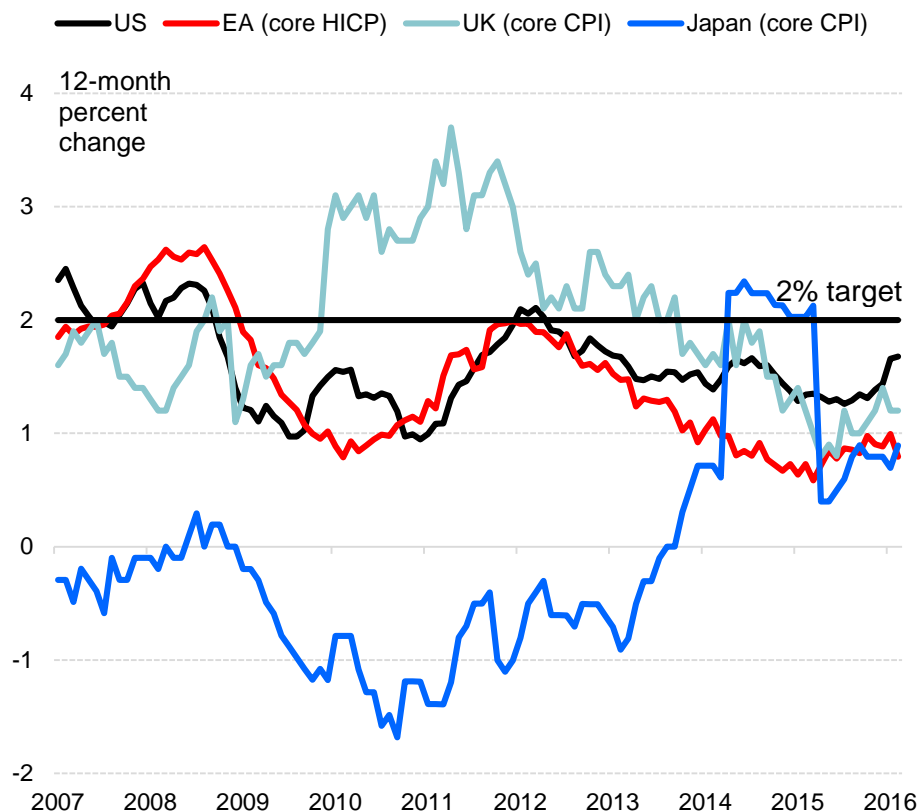
Source: MPI/Macroeconomic Advisers, Federal Reserve.

# The Advanced Economies: Less Room to Respond to Adverse Shocks

## Policy Interest Rates



## Core Consumer Price Inflation



Note: there was a sales tax increase from 5% to 8% in Japan in April 2014.

Source: Federal Reserve, ECB, BoJ, BoE via Haver Analytics and Bloomberg, OECD.

# The Global Outlook

Real GDP Growth (Y/Y)	2015	2016	2017
<b>Global Output Growth (PPP weights)</b>	<b>3.1</b>	<b>3.3</b>	<b>3.6</b>
<b>US:</b>	2.4	1.8	2.0
<b>Euro Area:</b>	1.5	1.5	1.6
<b>Japan:</b>	0.6	0.7	0.6
<b>UK:</b>	2.2	2.0	2.2
<b>Brazil:</b>	-3.8	-3.5	0.6
<b>Russia:</b>	-3.7	-1.5	1.1
<b>China:</b>	6.9	6.4	6.2
<b>India:</b>	7.3	7.5	7.6

Source: IMF WEO, Consensus Forecasts.