

State of the Economy: Soft Landing, Sustained Growth, or Recession

Scott Baier

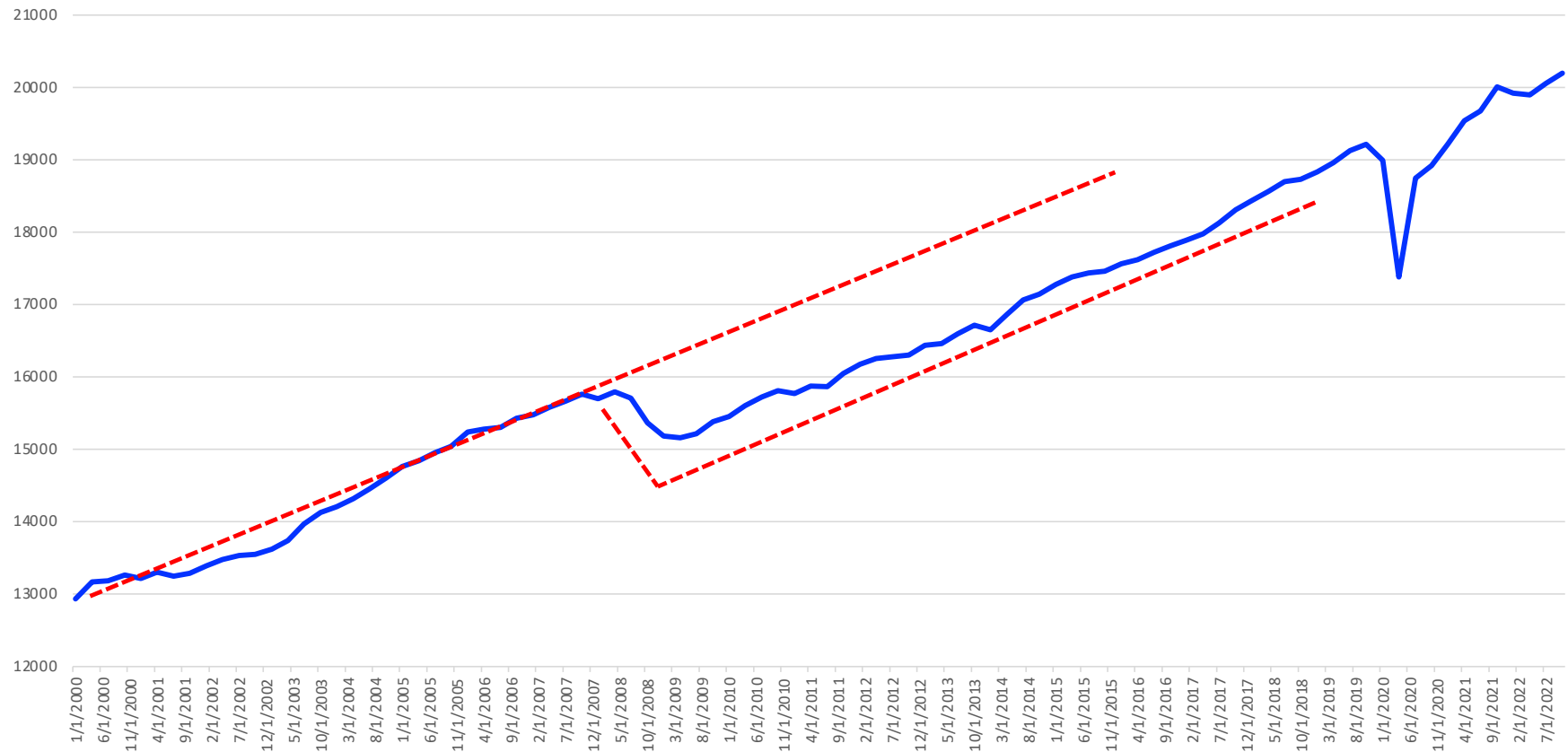
Clemson University & FTE

10/25/2023

Summary

- In the September meeting, the Federal Reserve decided to hold their targeted interest rate steady the Federal Funds Rate, to 5.25% – 5.50%
 - The Federal Reserve is expected to hold interest rate at this level when they meet next week from Oct 31 to November 3
- 2023:Q2 GDP growth was a revised down to 2.1% following a 2.2% increase in the first quarter.
 - 2023:Q3 Comes out tomorrow – expected to be 3.4 % and Atlanta Fed GDPNow comes in at 5.4%
- Inflation continues to trend down.
- Labor market continues to add jobs, but the last couple of job reports indicate that the labor is not quite as overheated as it was earlier in the year.

Real Gross Domestic Product

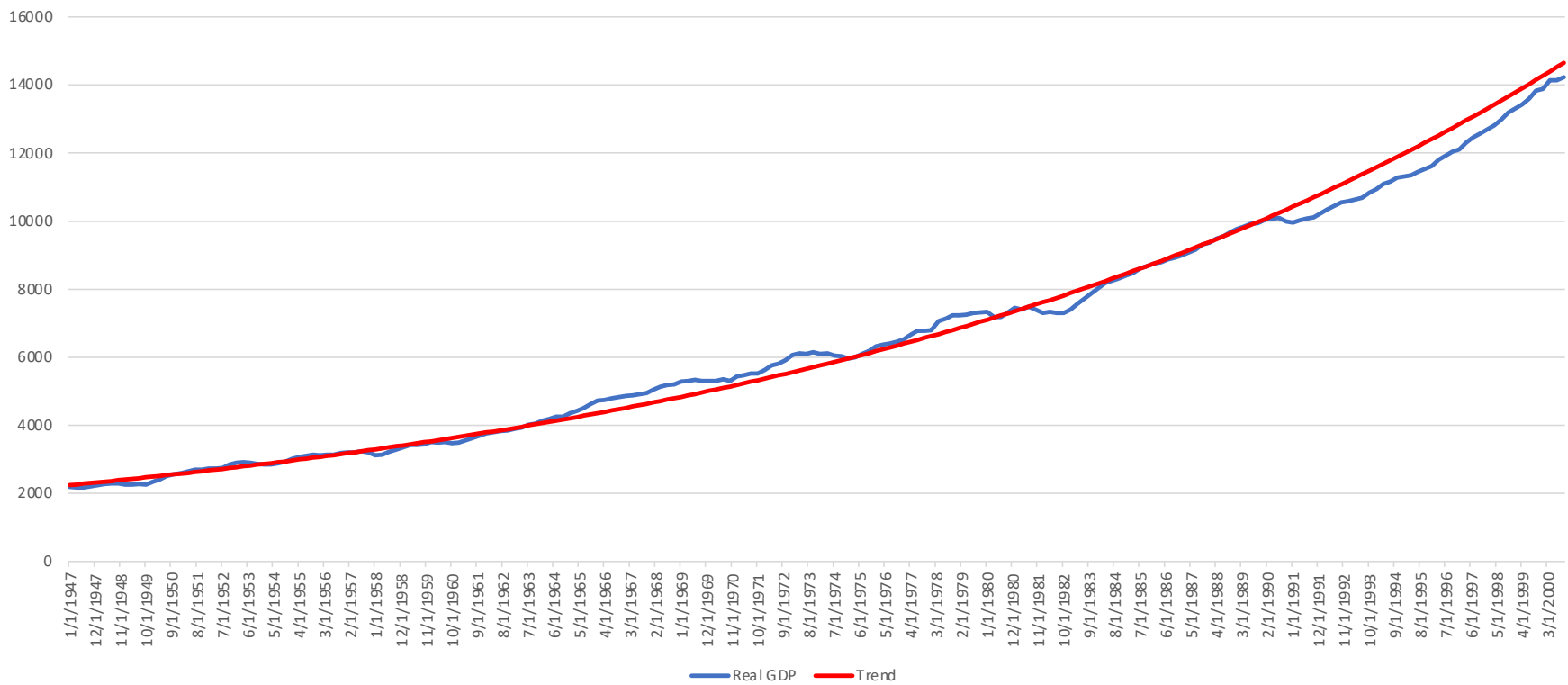


Source: Bureau of Economic Analysis

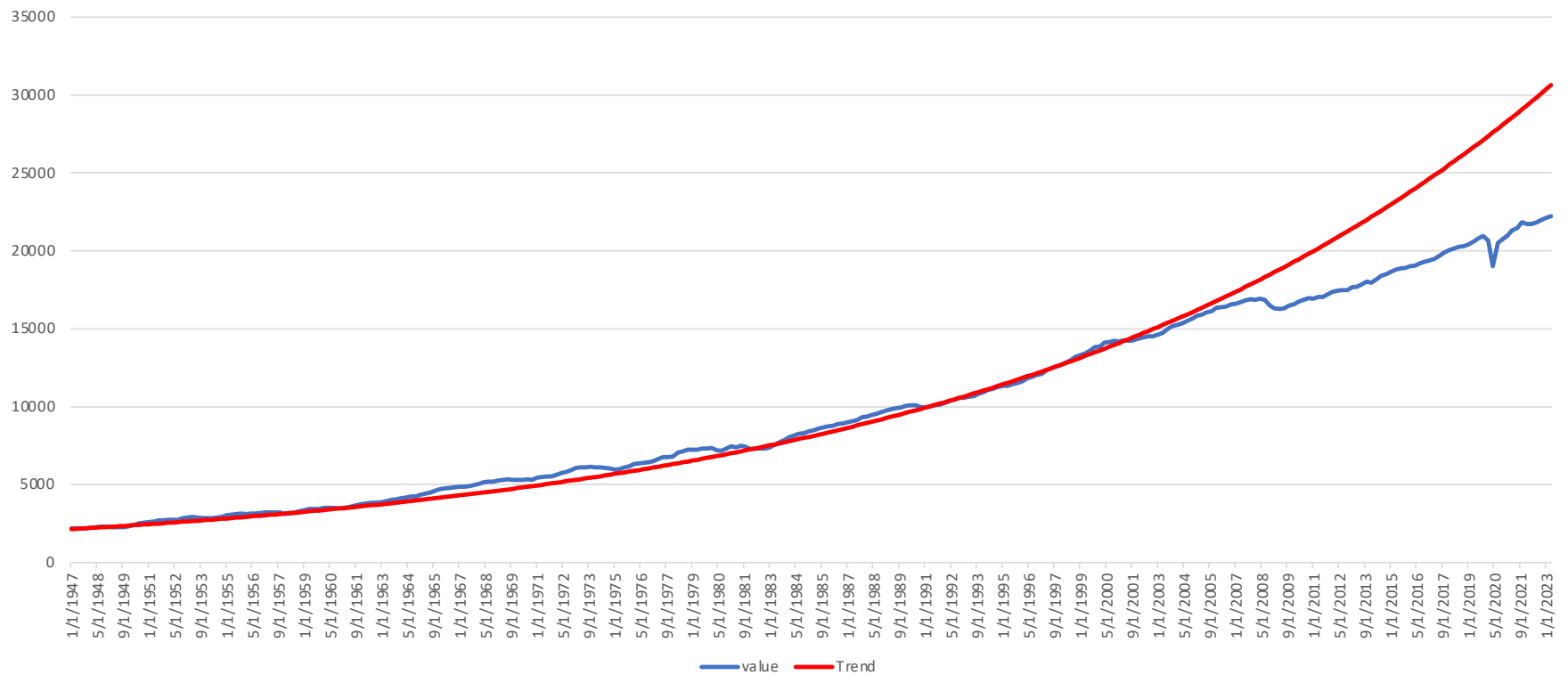
GDP Growth and Cycle

- When we think of GDP growth in the economy, it is important to remember that economic growth is the norm.
- Over time, supply side factors drive growth
 - The labor force grows and (typically) acquires more skill,
 - the productive capacity of the expands as we add more plants machines and equipment, and
 - and improvements in technology.

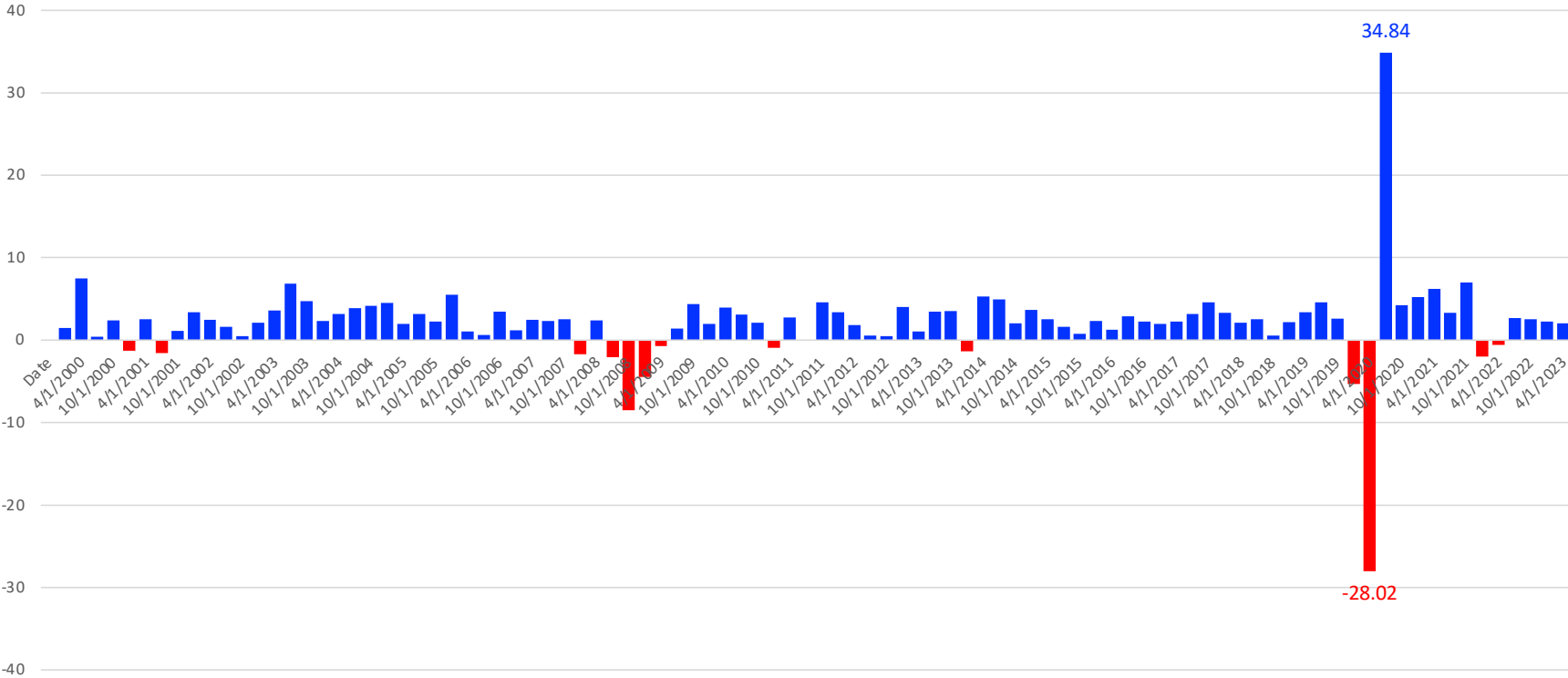
Real Gross Domestic Product: 1947-2000



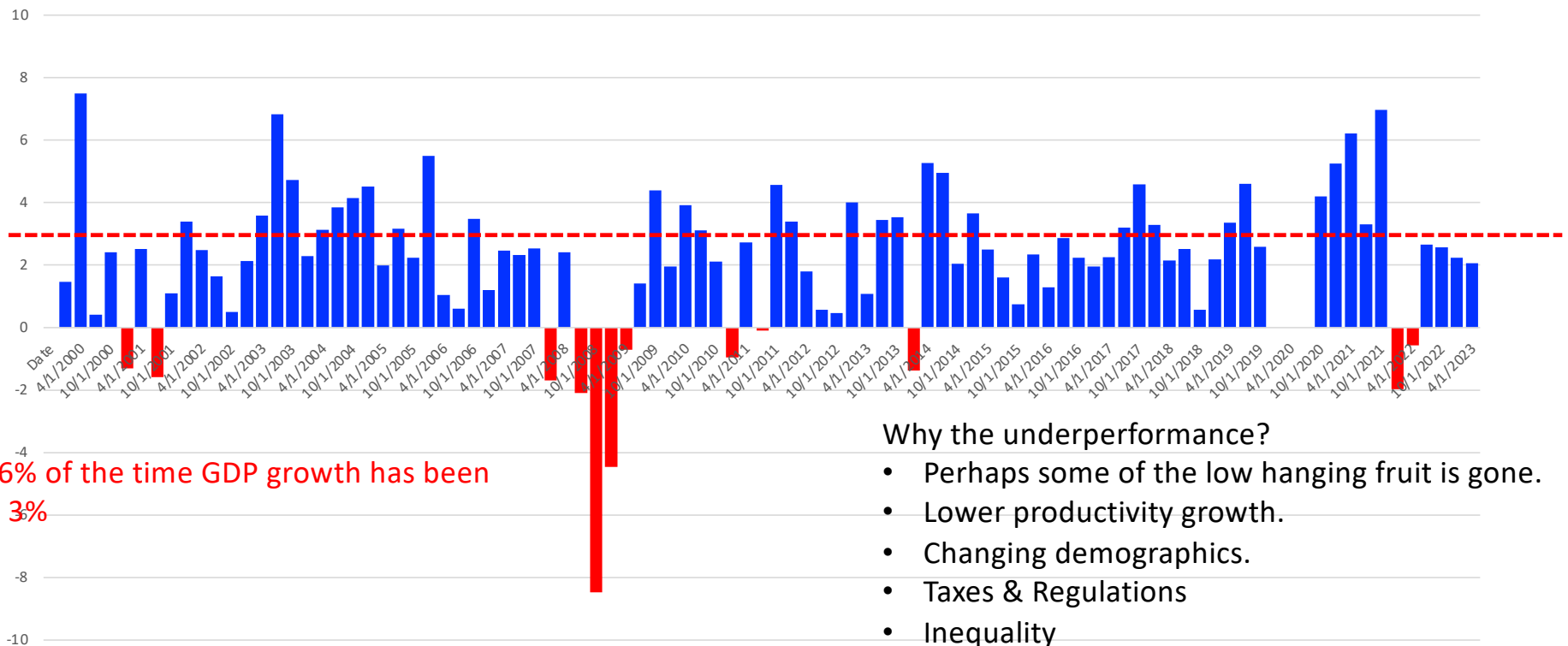
Real Gross Domestic Product: 1947:Q1 – 2023:Q2



Real Gross Domestic Product Growth Rates



Real Gross Domestic Product Growth Rates



GDP Growth and Cycles

- Typically, recessions are result of imbalances in the economy that
 - Result in periods of slack in output,
 - Can be caused by shifts in demand that are large and sustained,
 - Structure of supply is not able to adjust rapidly enough to reallocate resources across sectors,
 - Length of the cycle depends on the permanence of the demand shock and the appropriateness of the policy response.

Recession in the Future?

US Recession Probability (0-1)

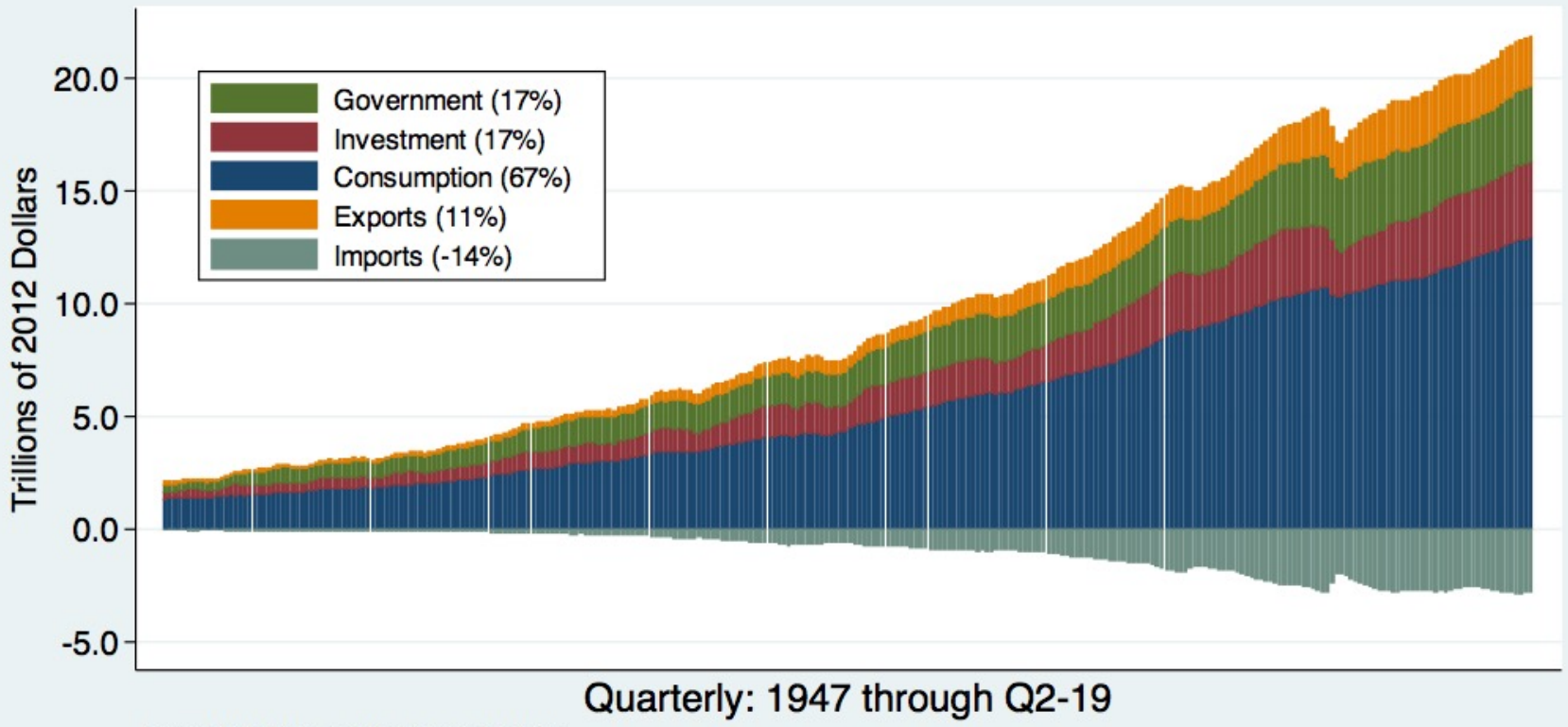


Source: The Conference Board, 2023

GDP Growth and the Economy

- For the rest of the talk, we will focus on the demand side because
 - This is where the imbalances come from,
 - It is easier to identify (historically) the nature of the imbalances,
 - It is easier to describe how components of demand also respond to economic shocks.

Composition and Contribution of Real GDP

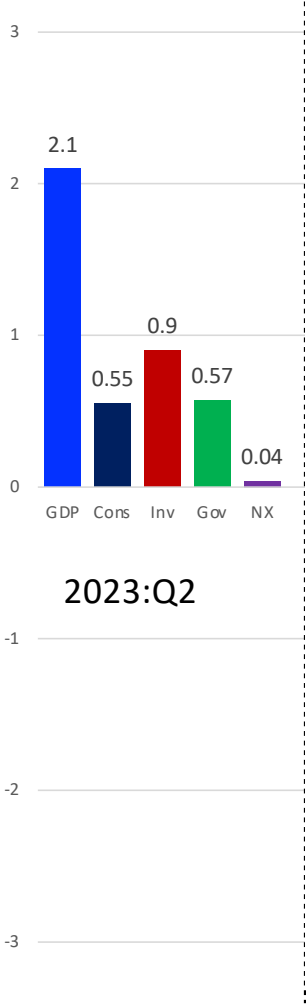


Source: U.S. Bureau of Economic Analysis

Understanding Contributions to GDP Growth

- GDP Growth is a combination of the growth in its components:
 - Consumption, Investment, Government, and Net Exports
 - It's a weighted average of these components
- For example: Consumption
 - If consumption accounts for **2/3** of the economy,
 - If consumption grew by **3%**,
 - It implies that consumption growth accounts for **2 percentage points** of GDP growth; that is, $2\% = \left(\frac{2}{3}\right) * 3\%$.

GDP Components Contributions



2023:Q1

2022:Q4

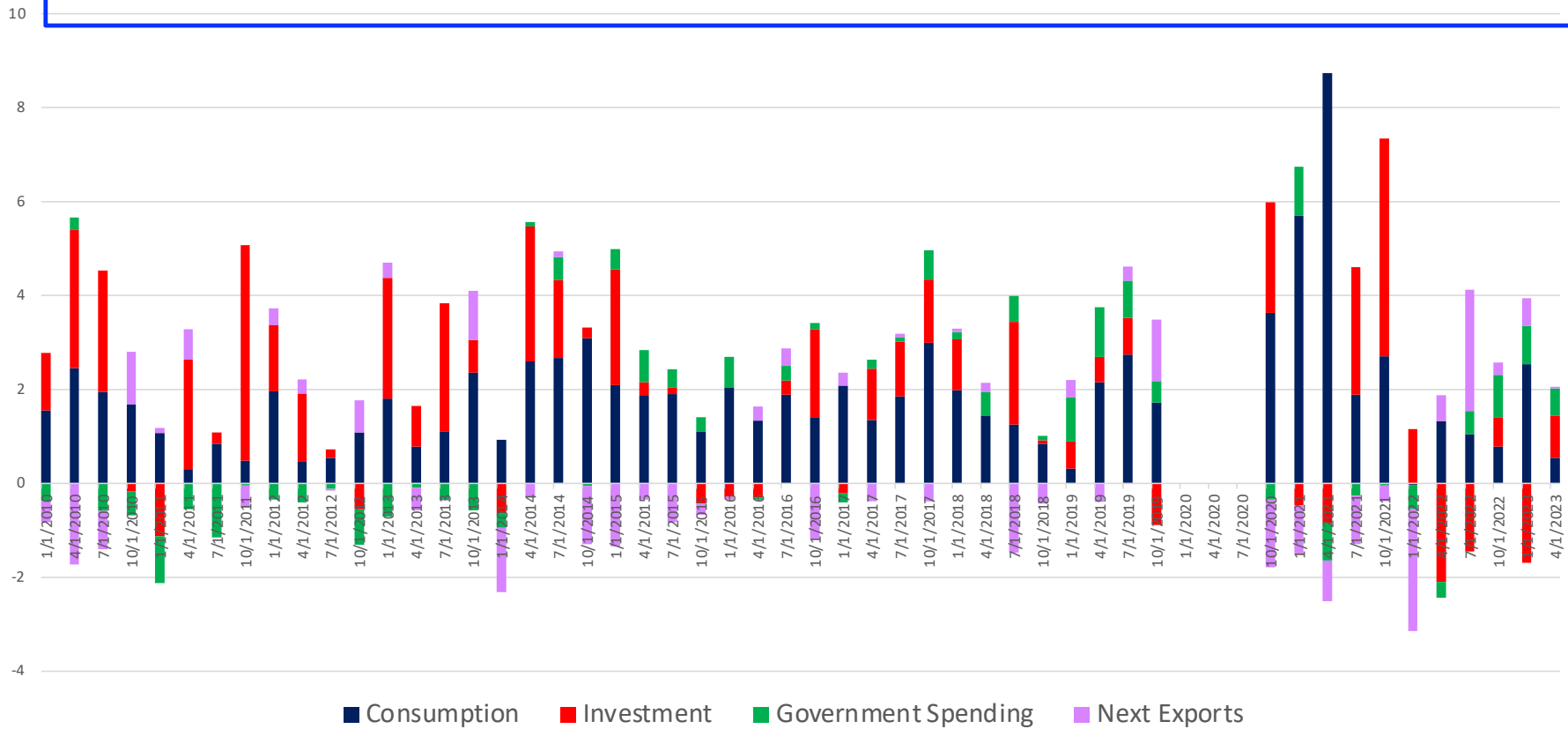
2022:Q3

2022:Q2

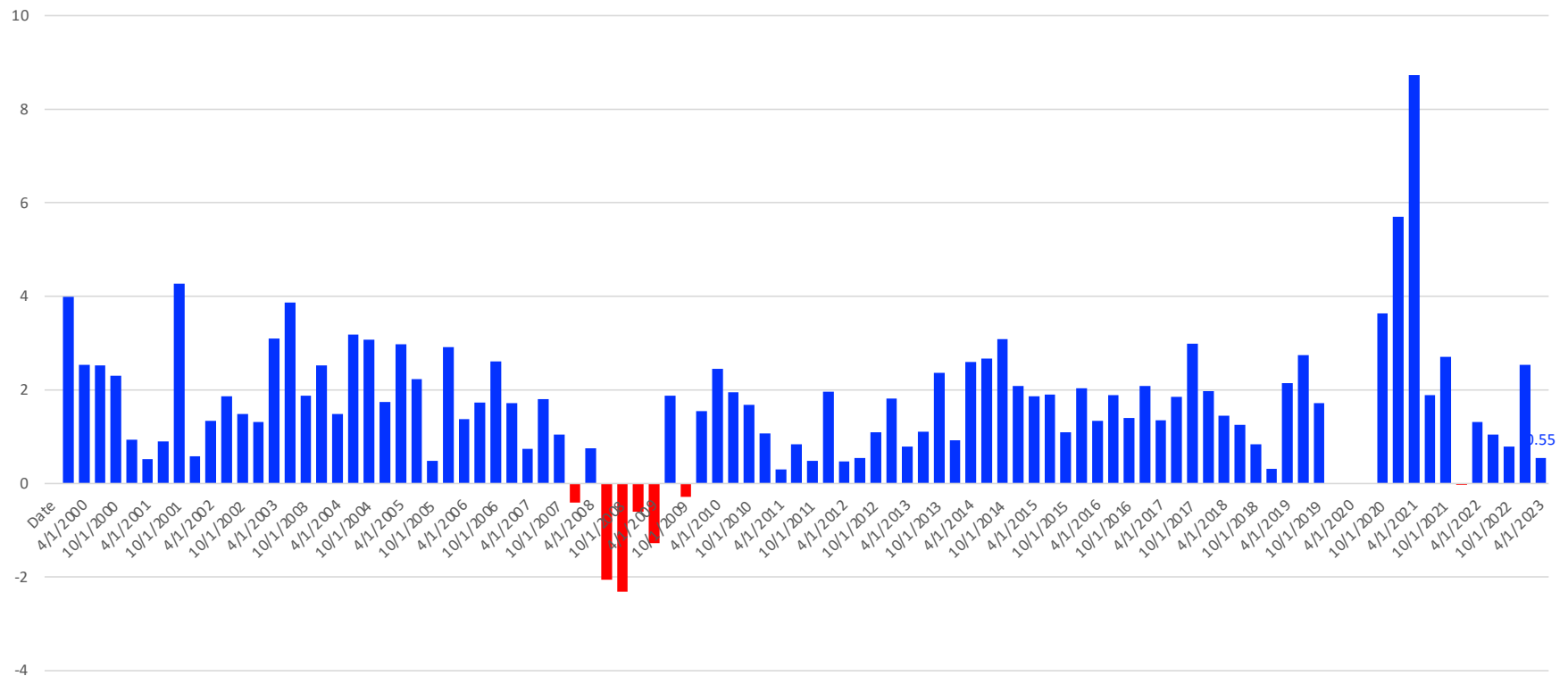
2022:Q1

:

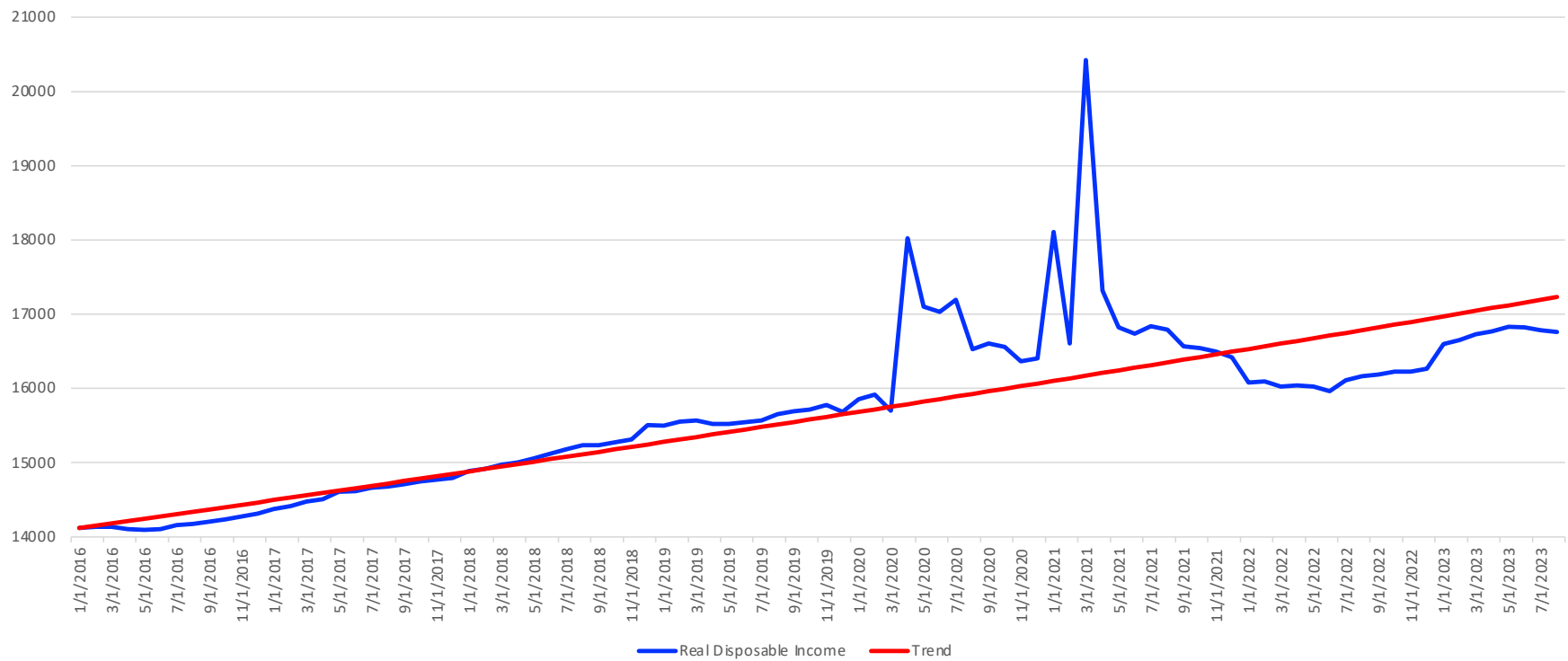
GDP Growth and Its Components



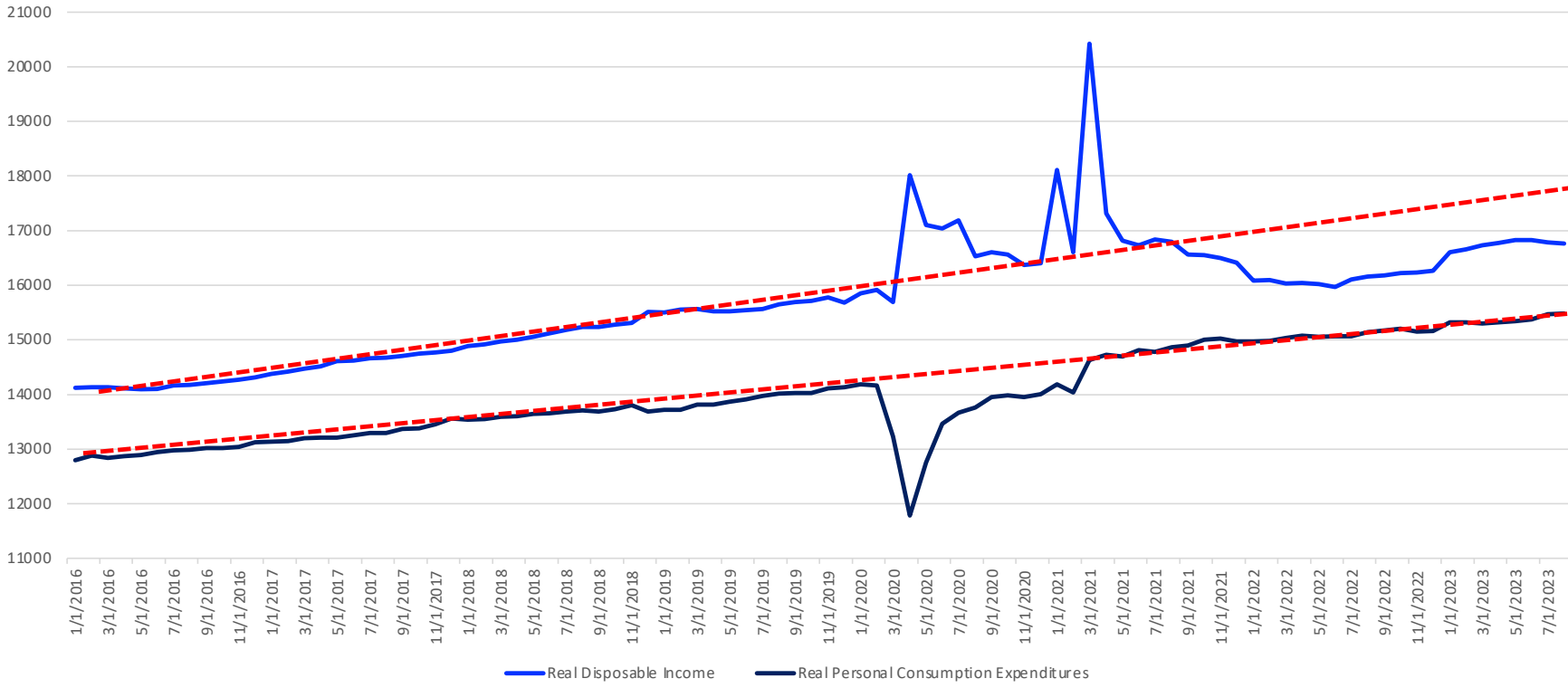
Consumption's Contribution to GDP Growth



Real Disposable Income

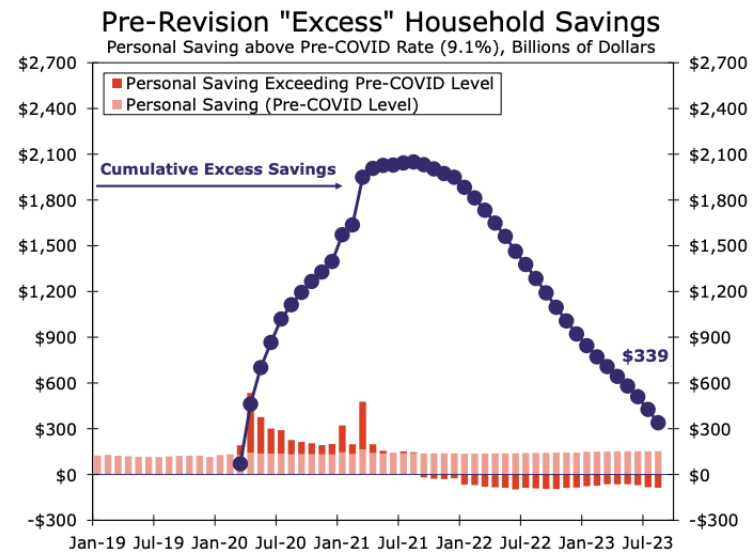


Real Disposable Income and Consumption



Excess Saving

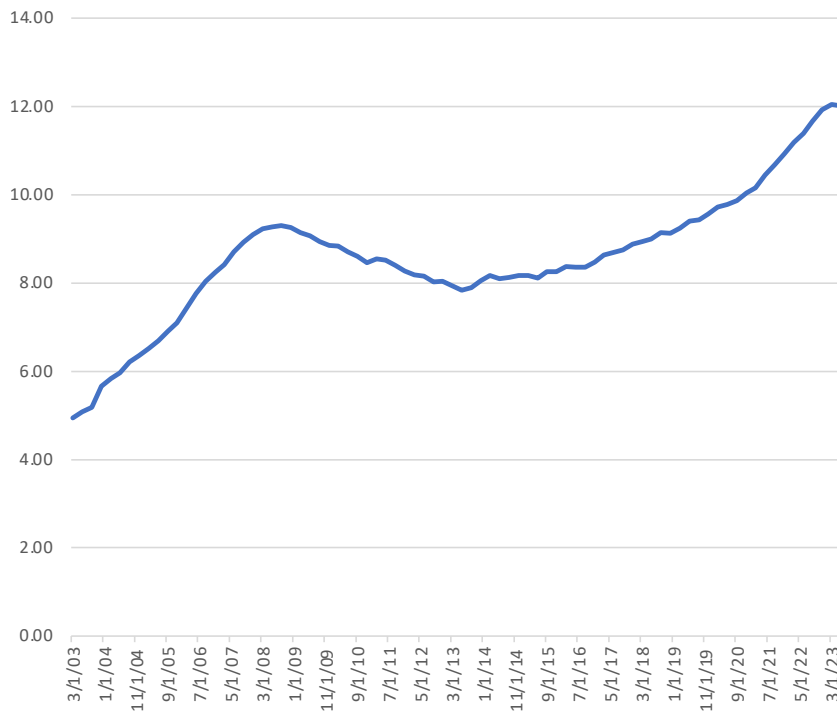
Figure 2



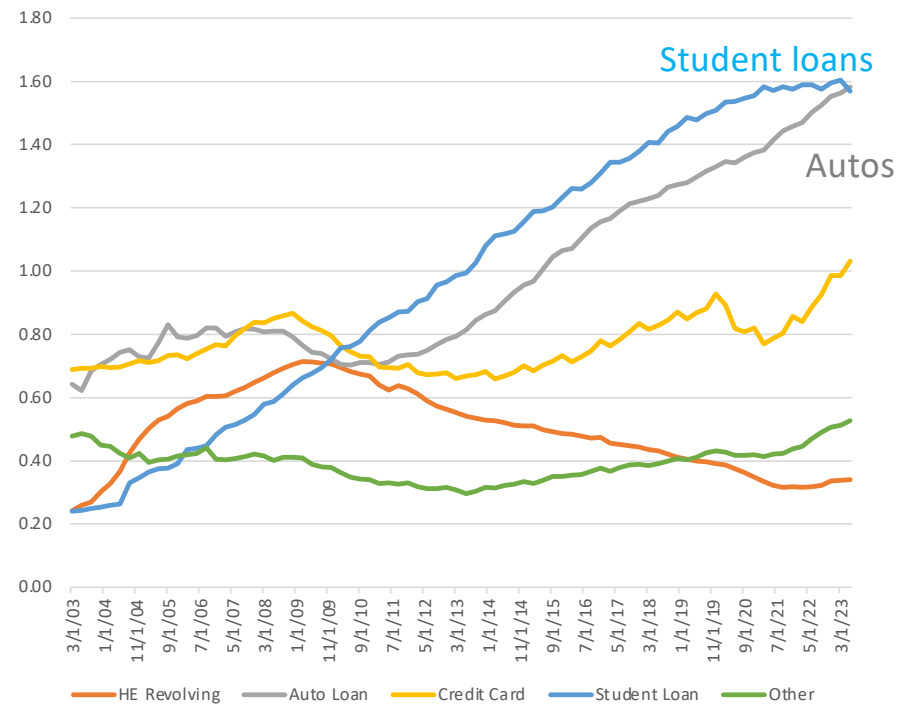
Source: U.S. Department of Commerce and Wells Fargo Economics

Source: Wells Fargo: Special Commentary Oct 5

Consumer Borrowing



Mortgage debt



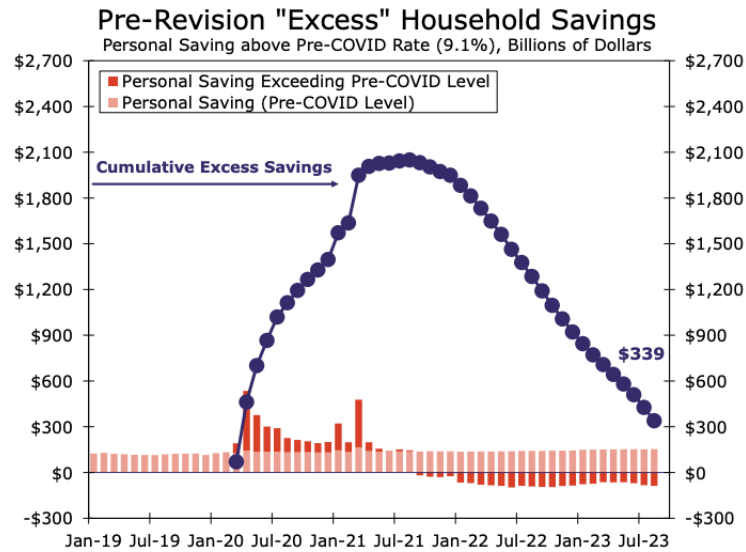
Student loans

Autos

HE Revolving Auto Loan Credit Card Student Loan Other

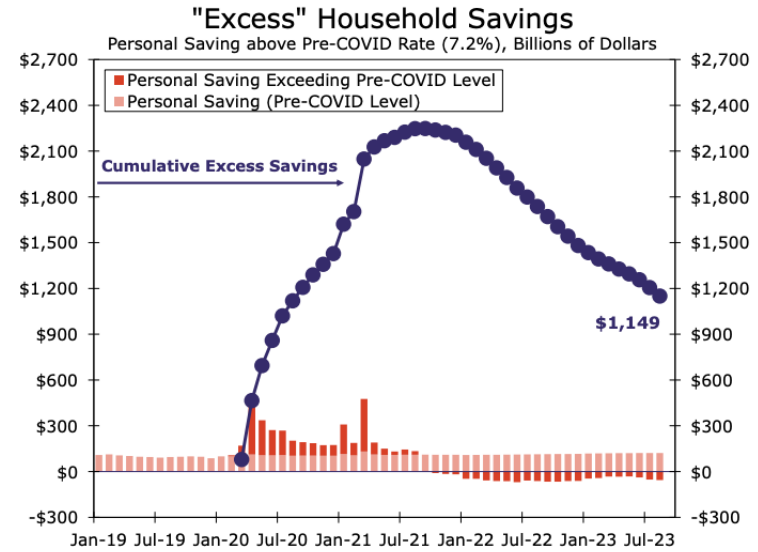
Excess Saving

Figure 2



Source: U.S. Department of Commerce and Wells Fargo Economics

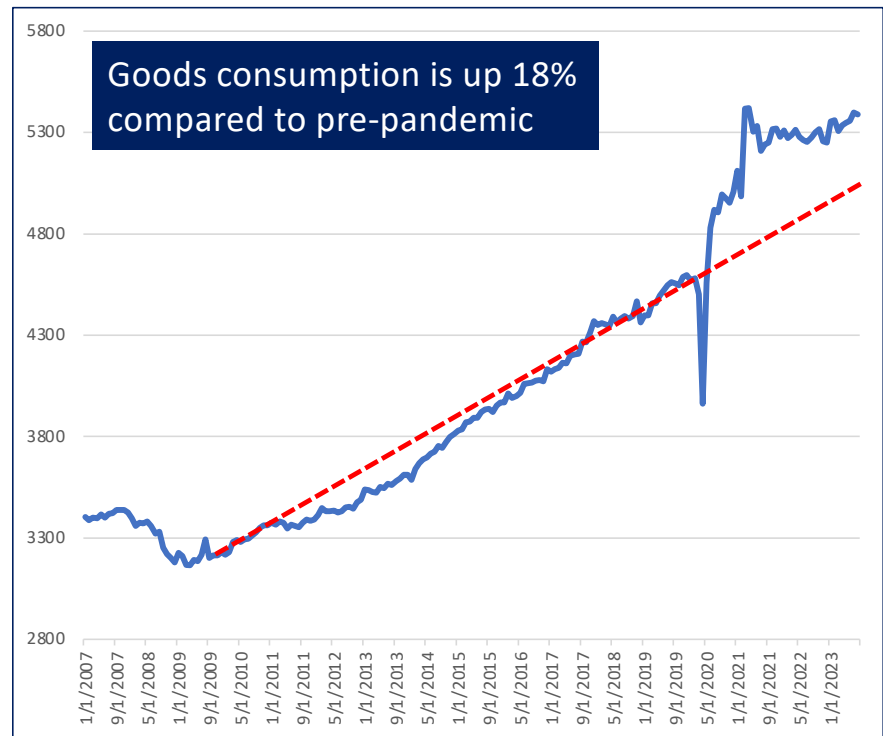
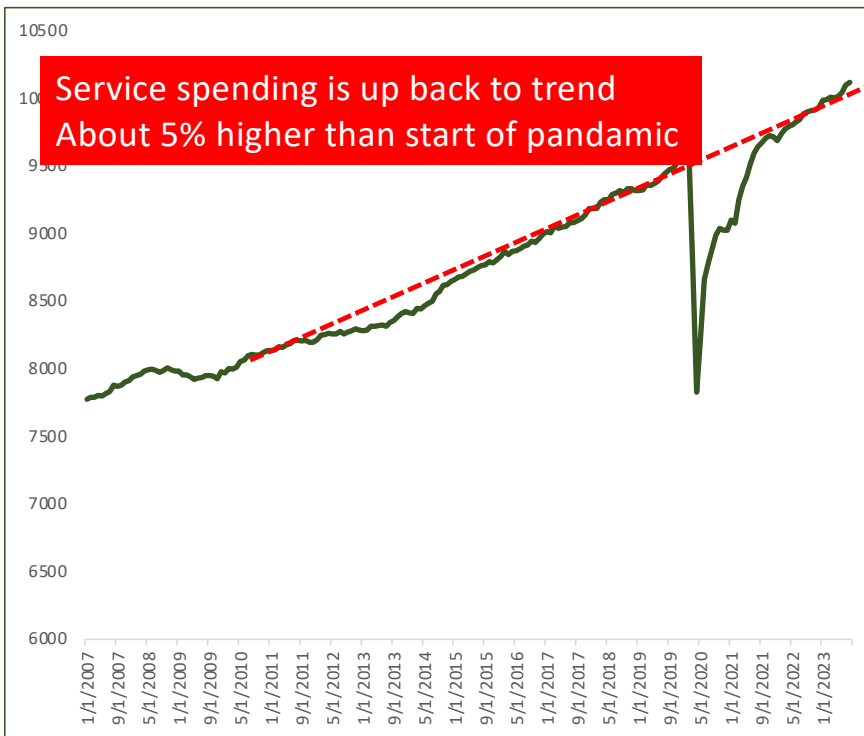
Figure 3



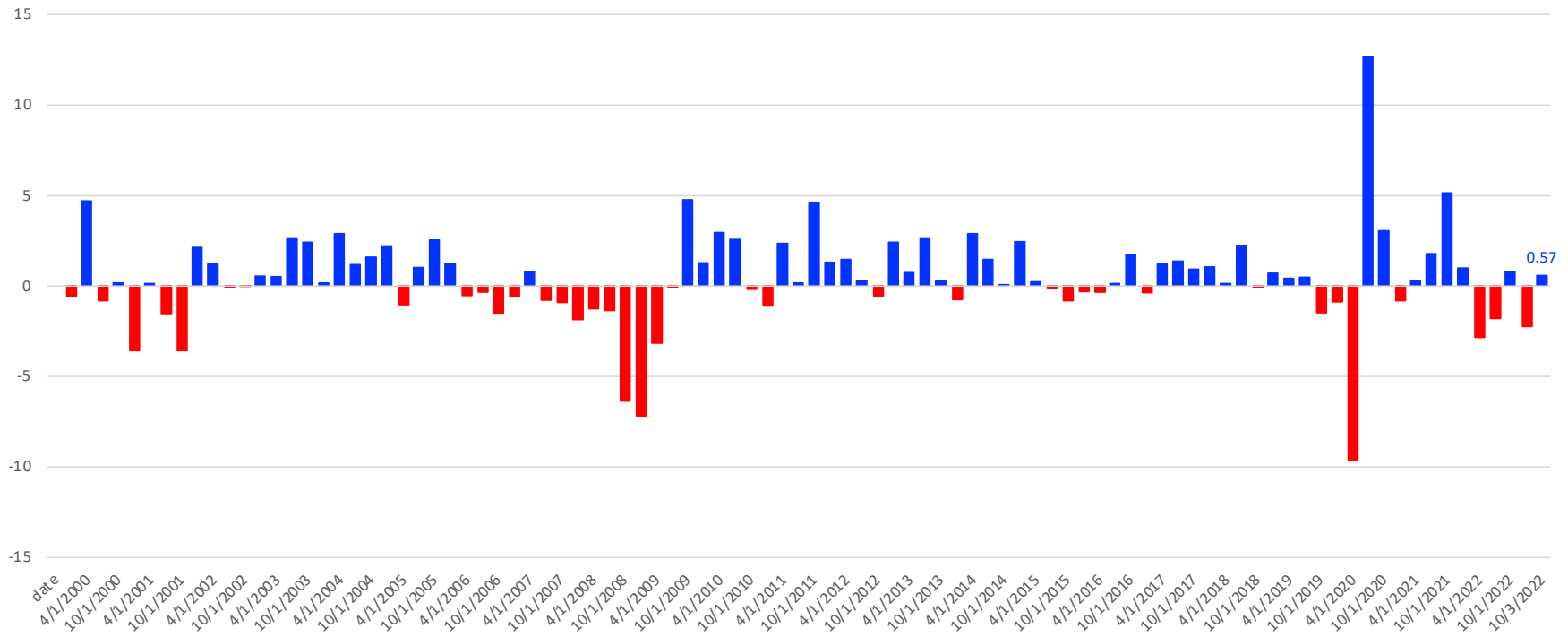
Source: U.S. Department of Commerce and Wells Fargo Economics

Source: Wells Fargo: Special Commentary Oct 5

Consumption of Real Goods and Services



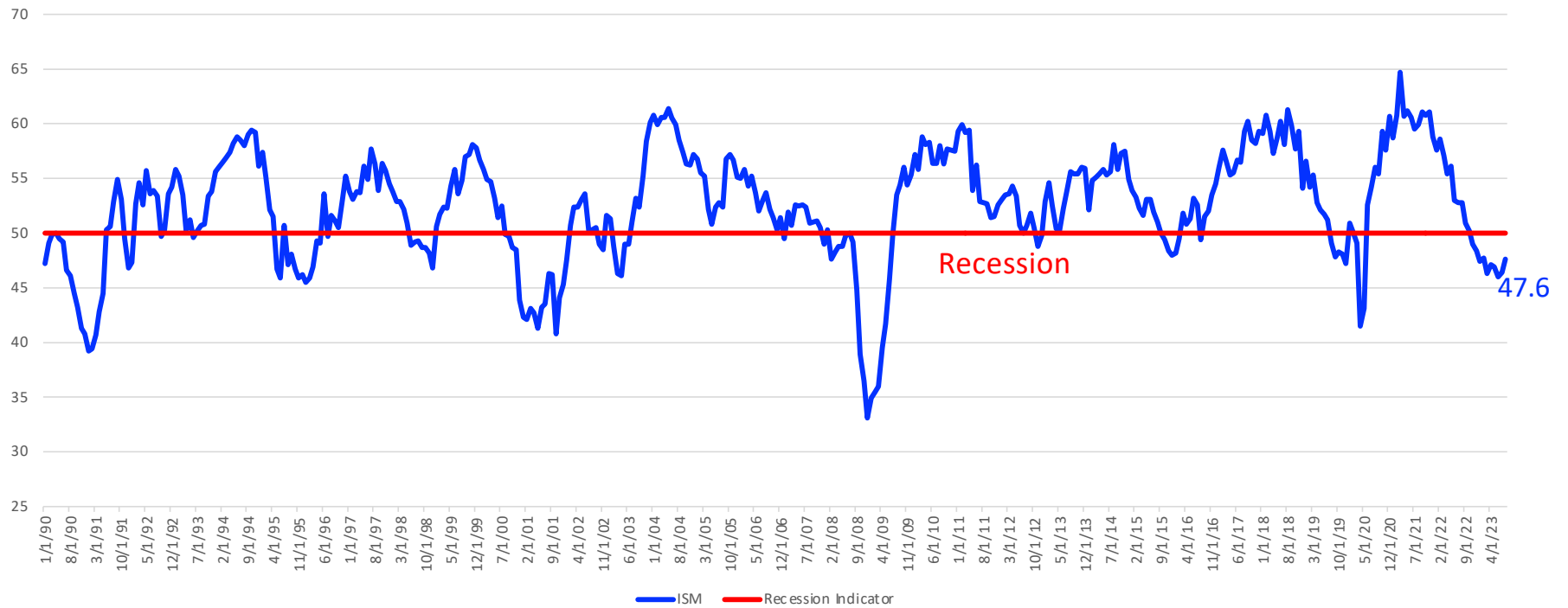
Investment Spending's Contribution



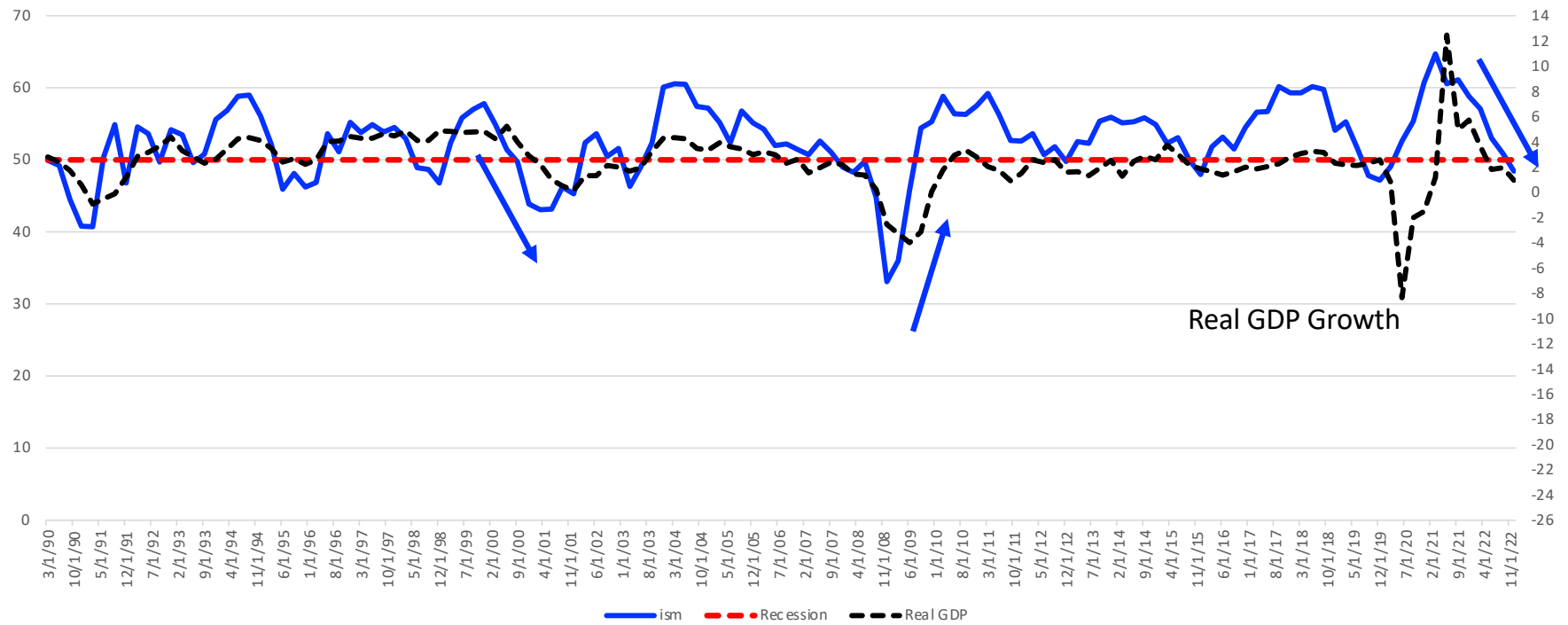
Investment Spending:

- Investment includes the:
 - purchase of plants machines and equipment,
 - changes in business Inventories,
 - and residential investment
- The drivers of each of these components are different.

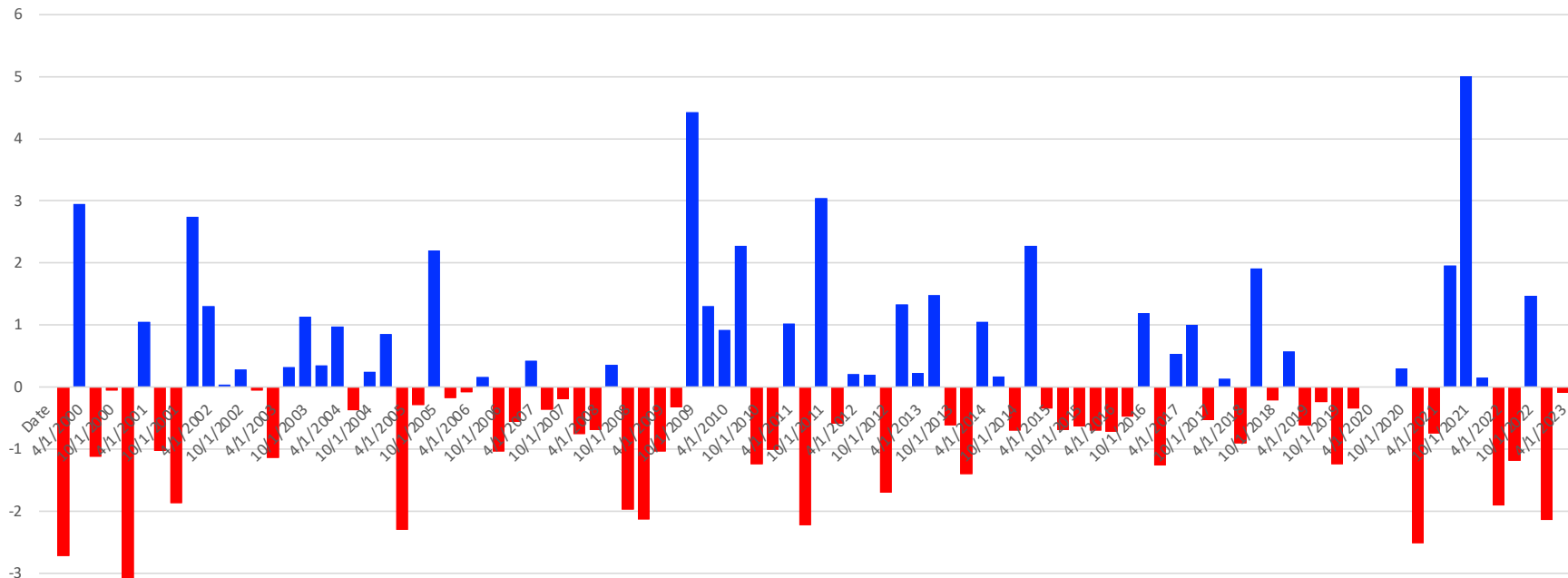
ISM Manufacturing Index



ISM Manufacturing Index and Real GDP



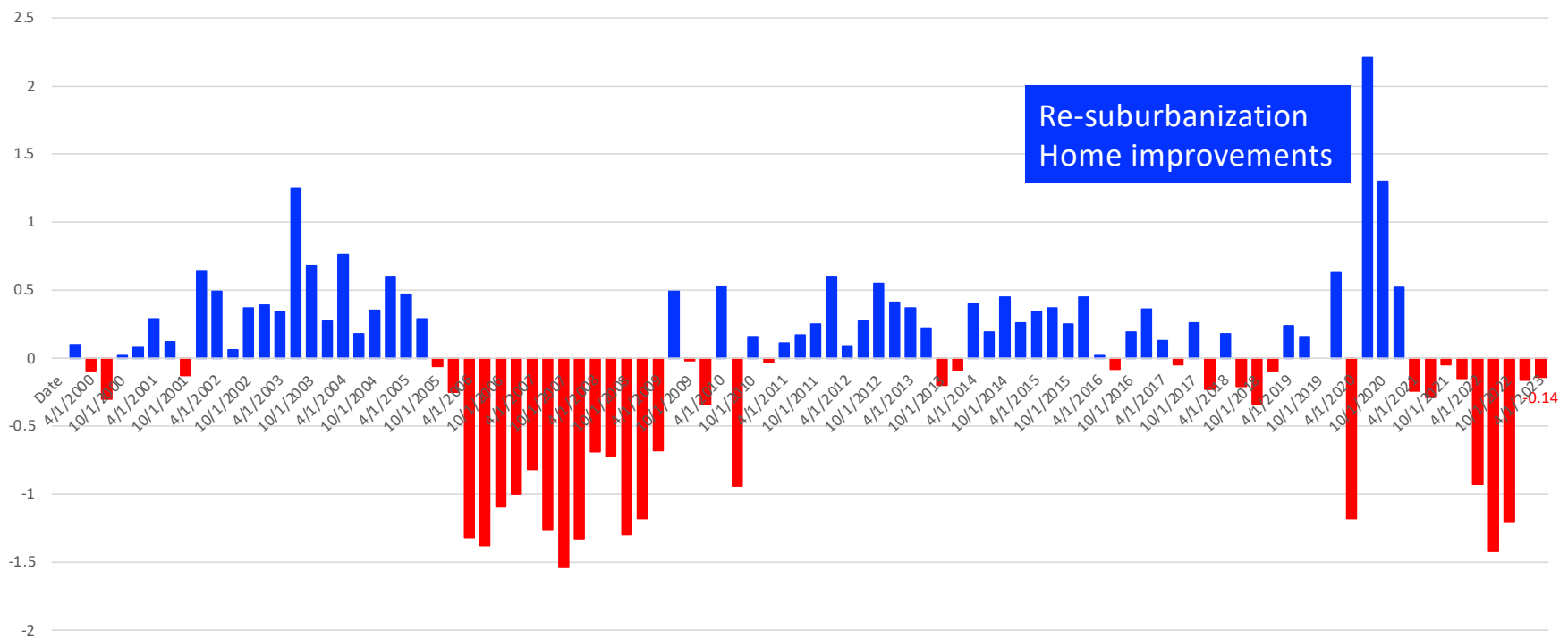
Inventory's Contribution to GDP Growth



Inventory Investment is the most volatile component.
Inventories of intermediate inputs and finished products move quickly
JIT and JIC

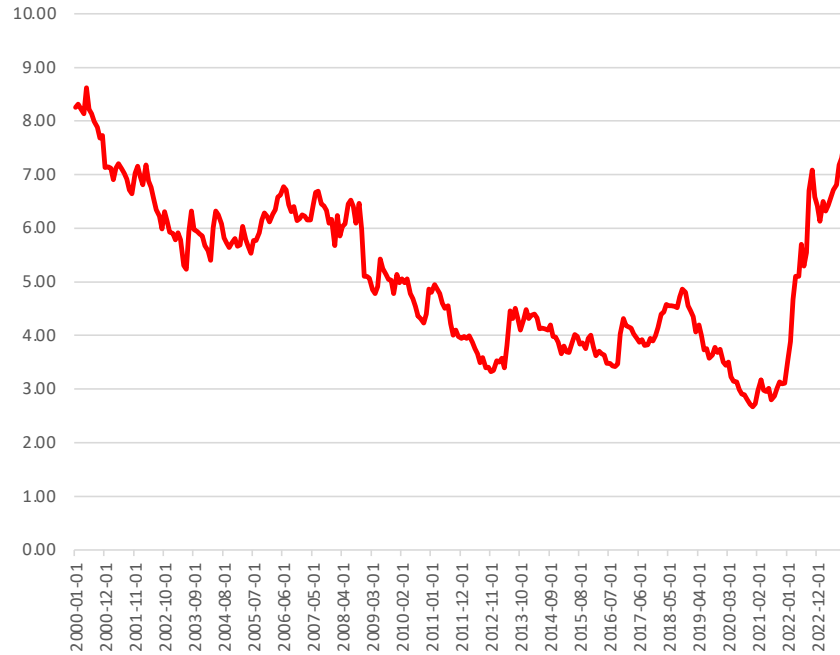
Source: Bureau of Economic Analysis

Residential Investment's Contribution to GDP Growths

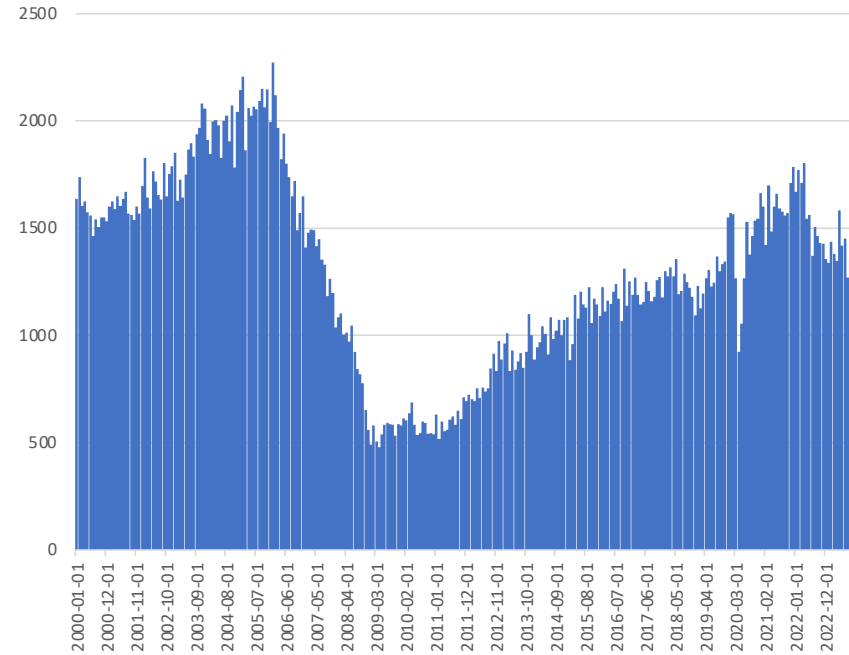


Mortgage Rates and Housing Starts

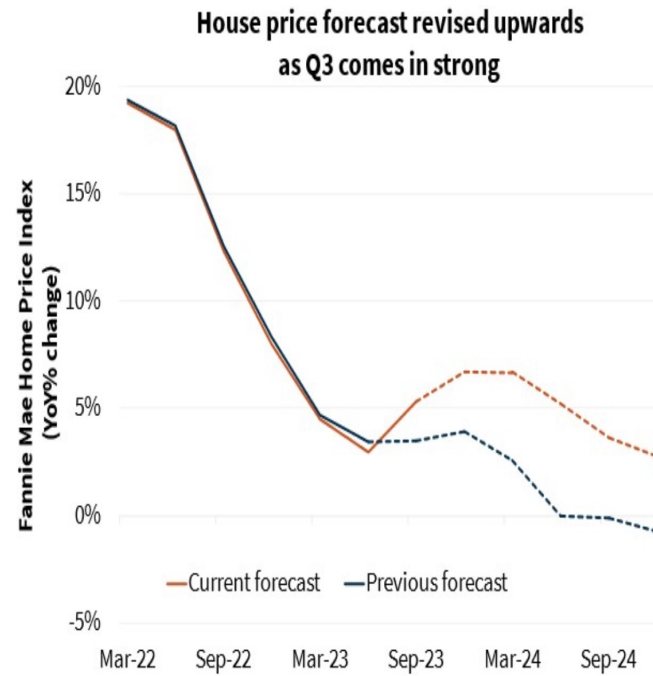
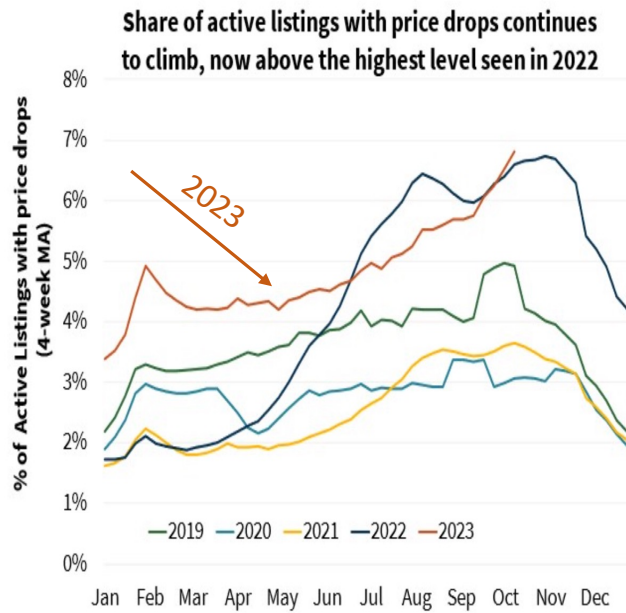
Mortgage (30-year)



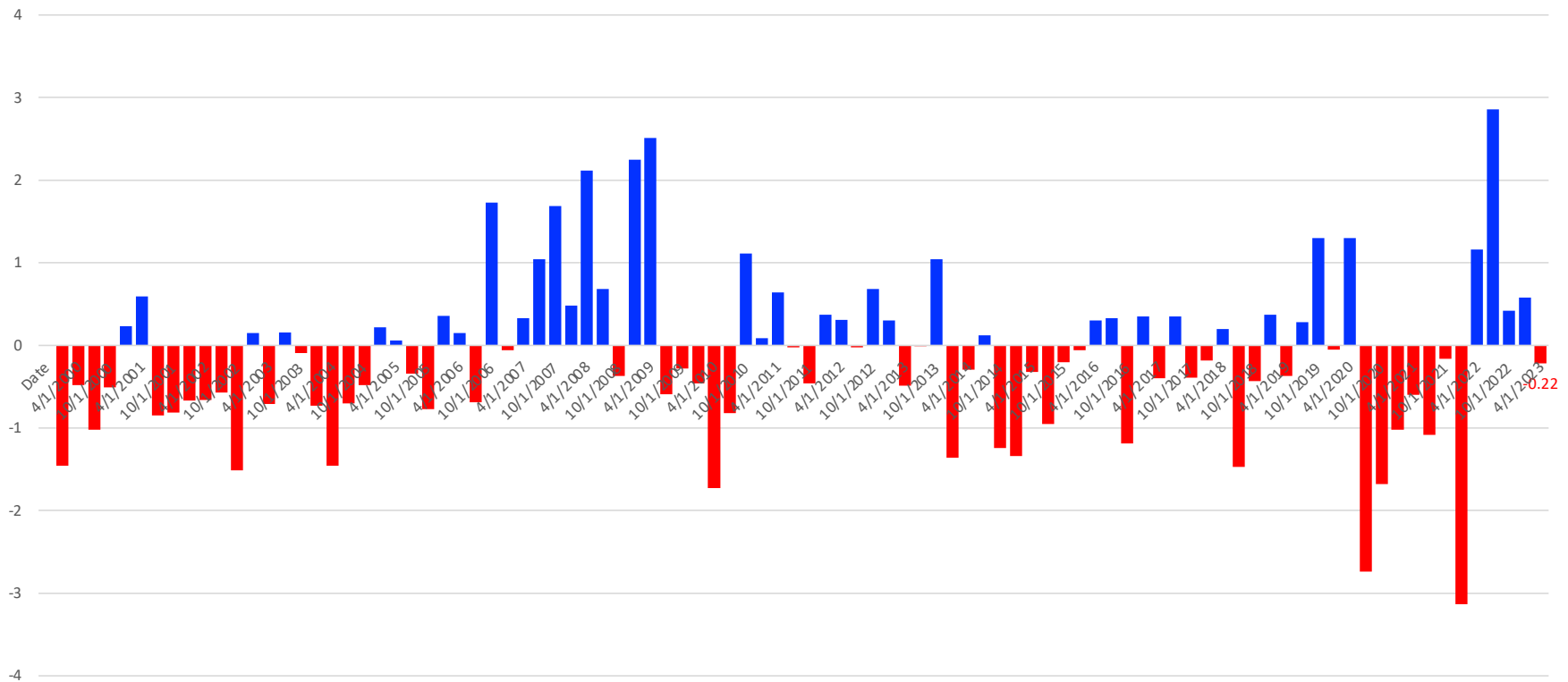
Housing Start



Housing Market

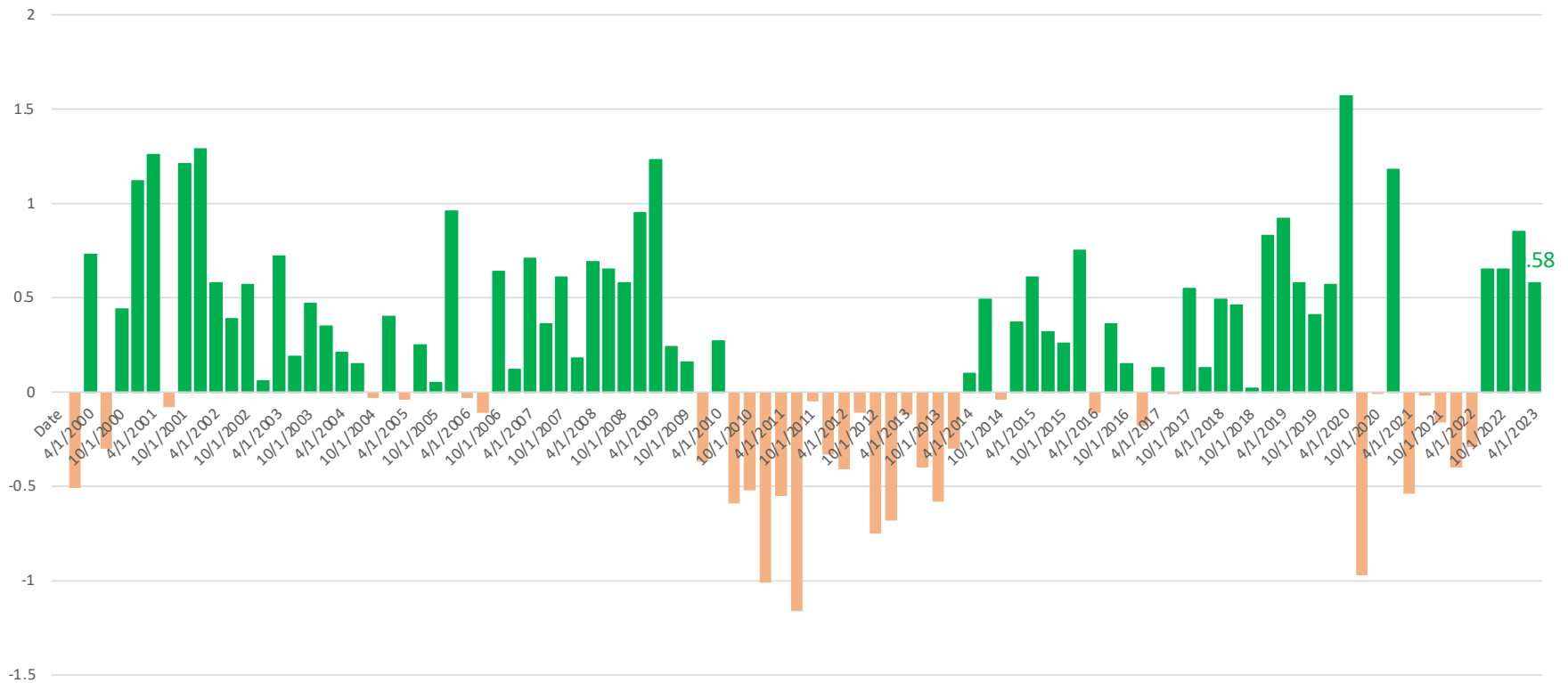


Net Exports and GDP Growth

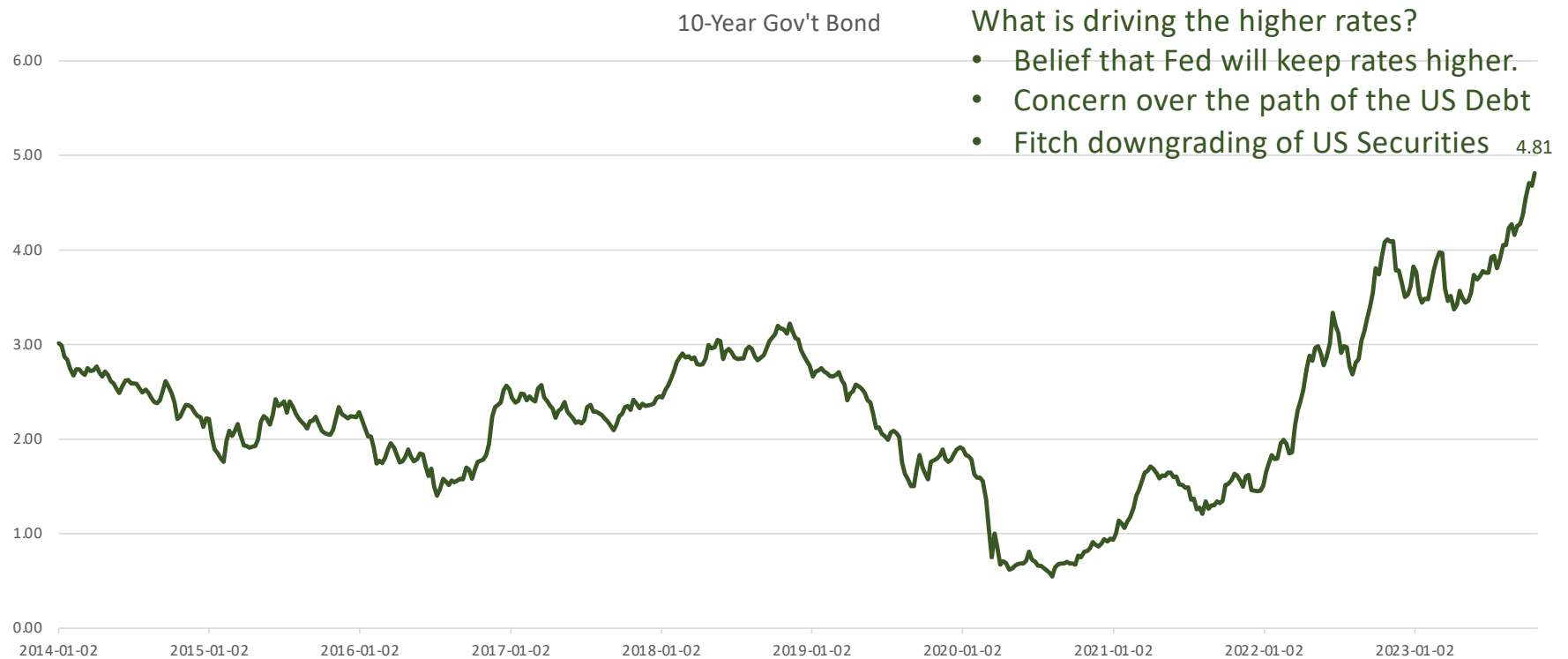


Source: Bureau of Economic Analysis

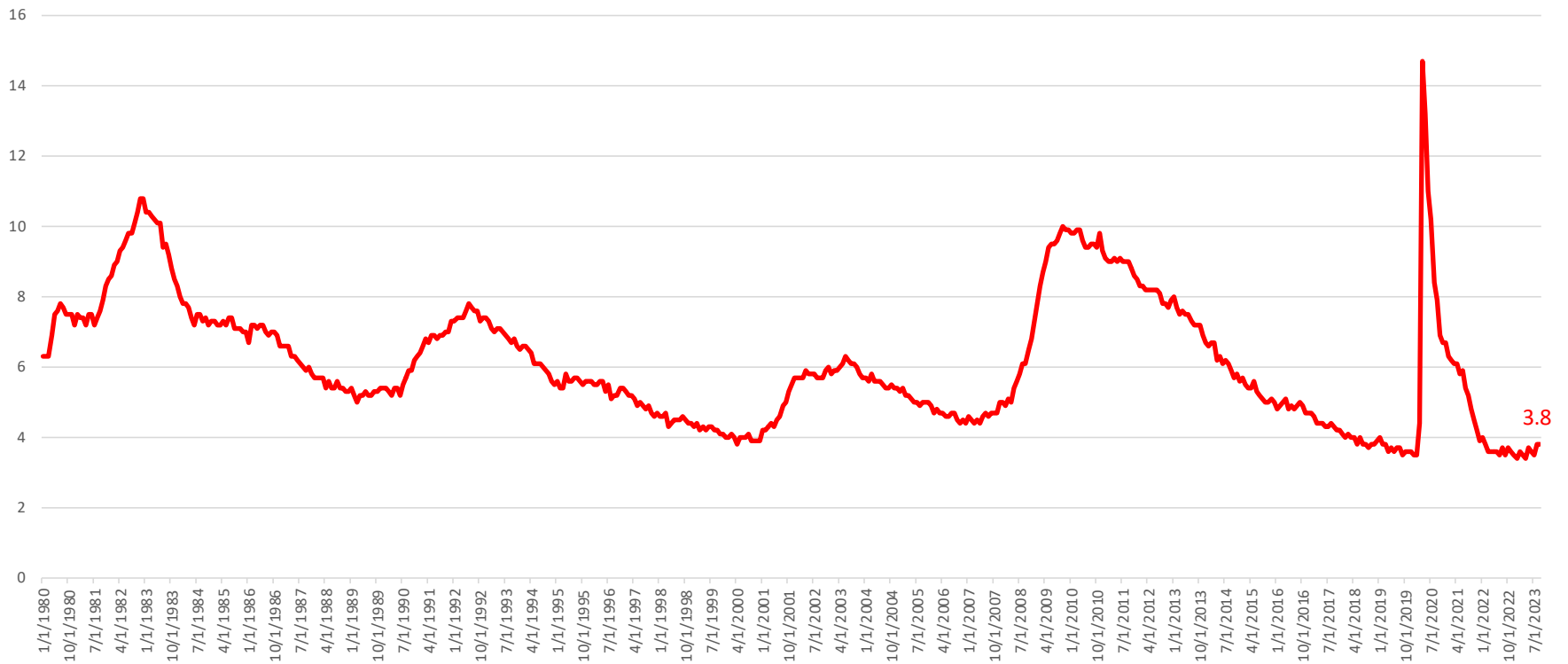
Government Spending



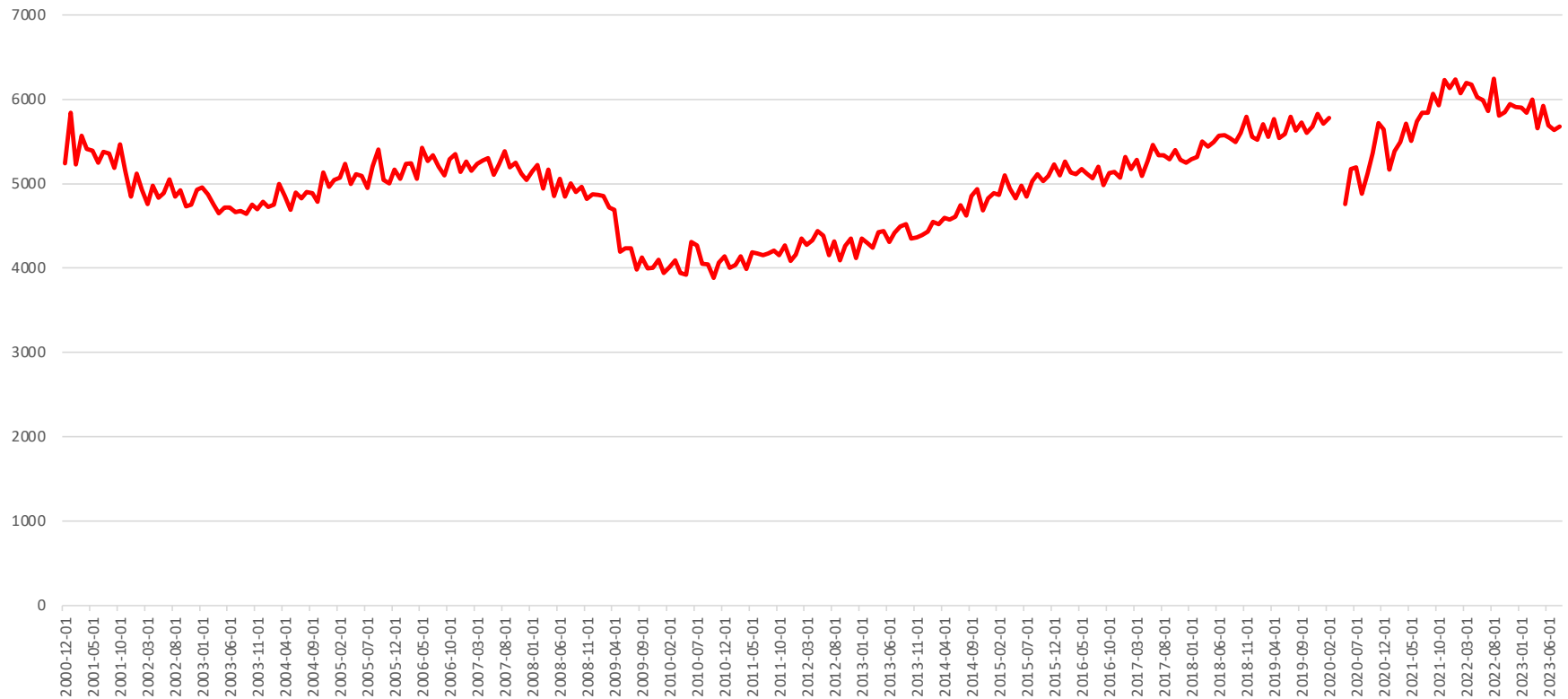
Interest Rate on 10-year US Security



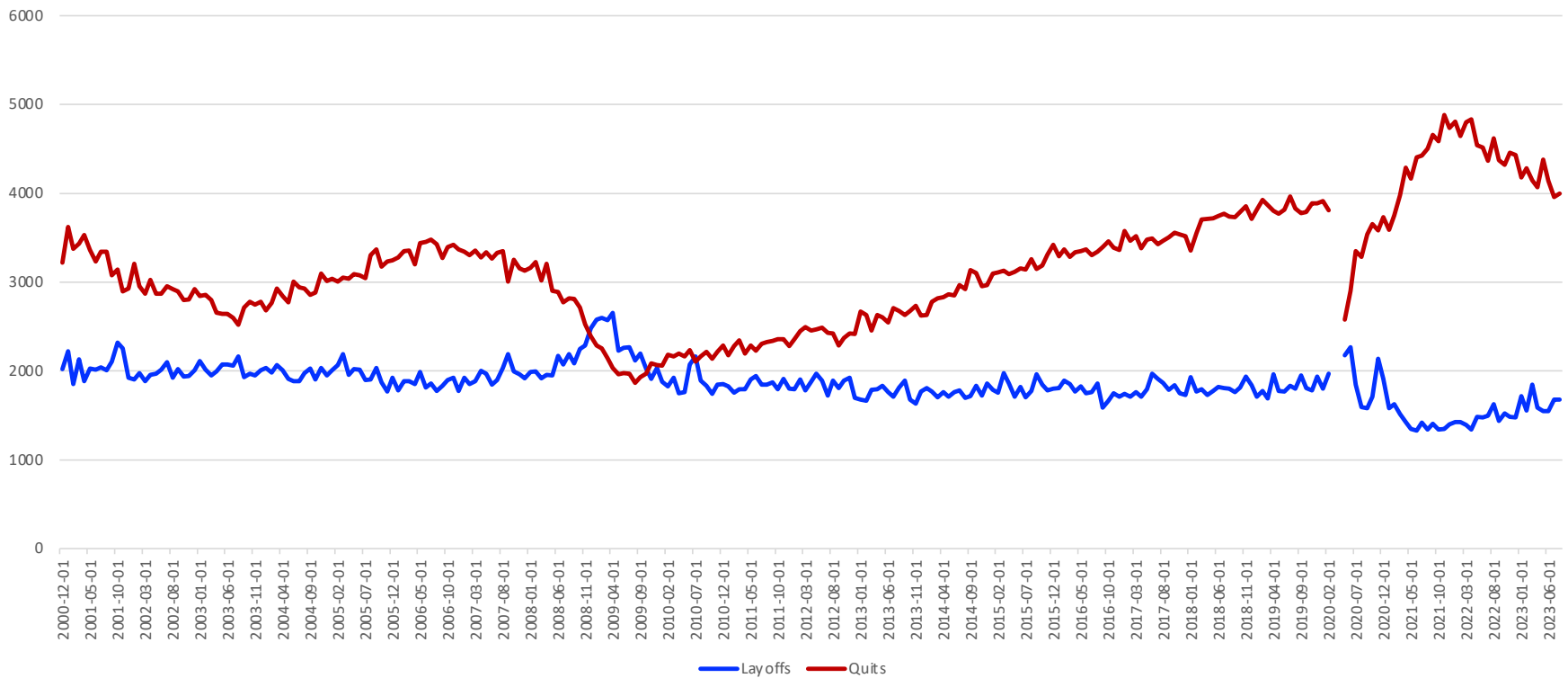
Unemployment



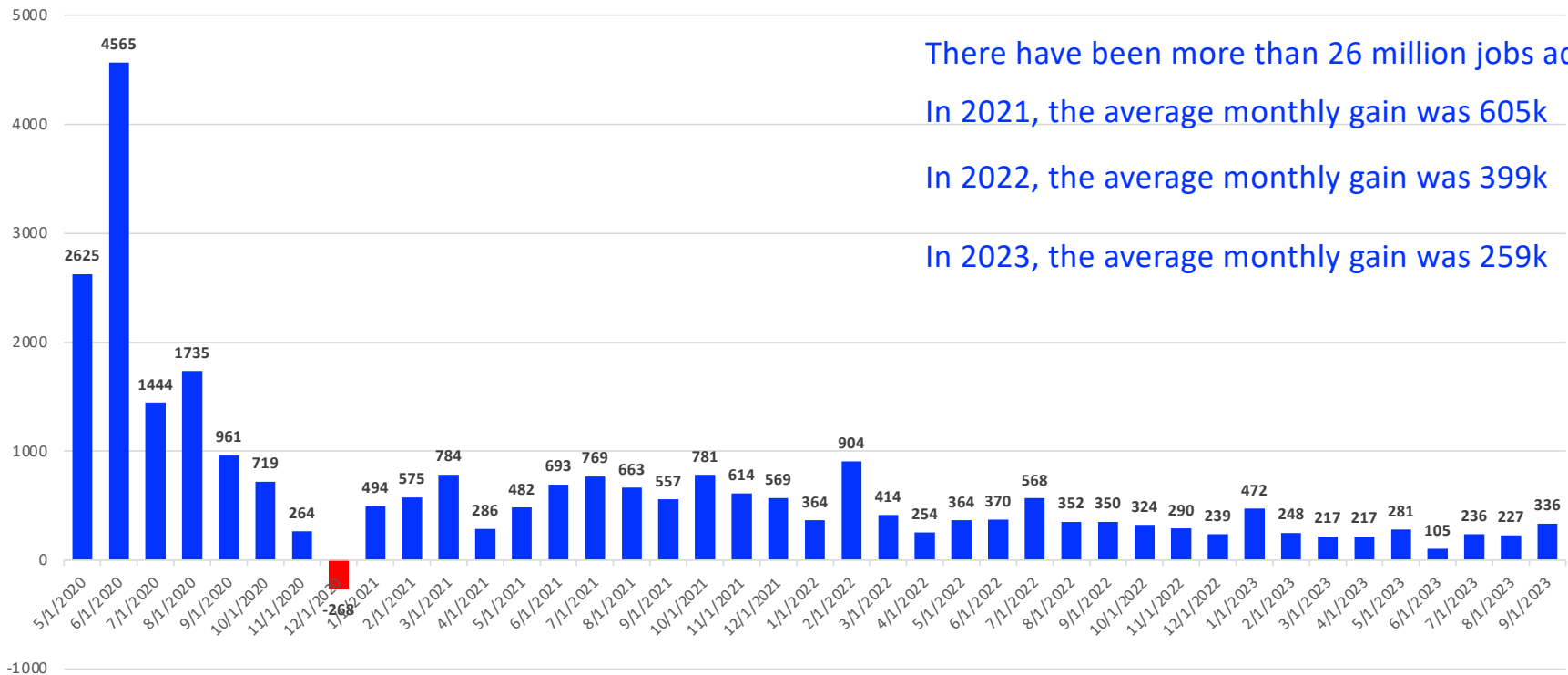
Job Separations



Quits and Layoffs



Gains in Non-Farm Payrolls



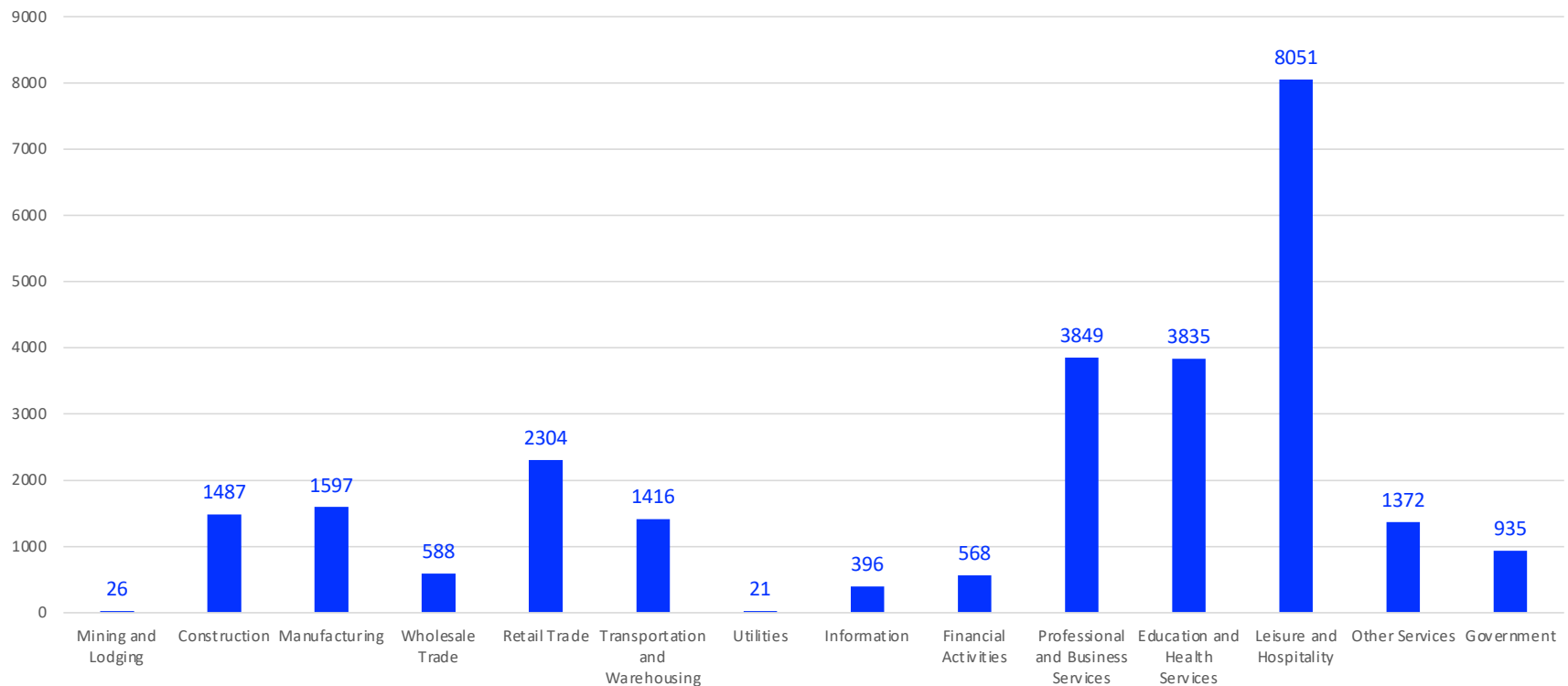
There have been more than 26 million jobs added

In 2021, the average monthly gain was 605k

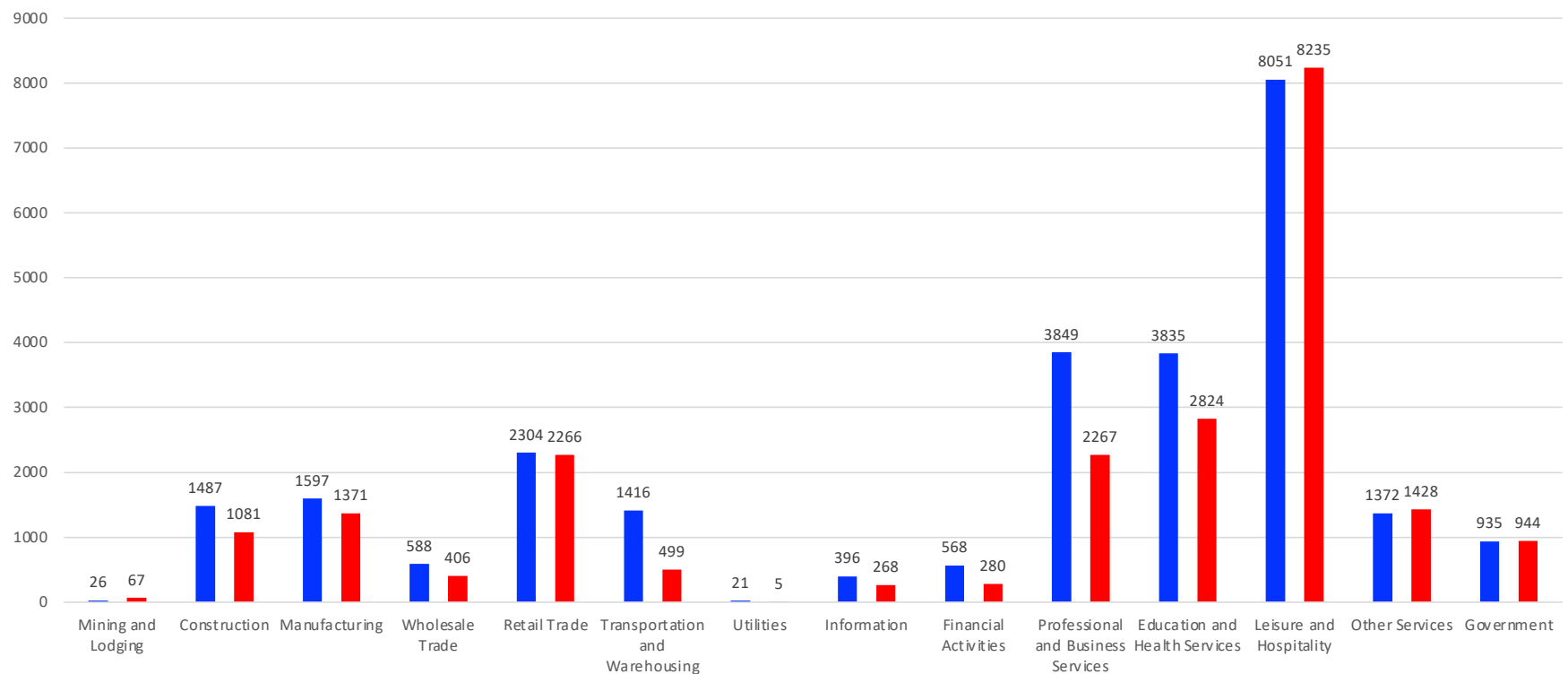
In 2022, the average monthly gain was 399k

In 2023, the average monthly gain was 259k

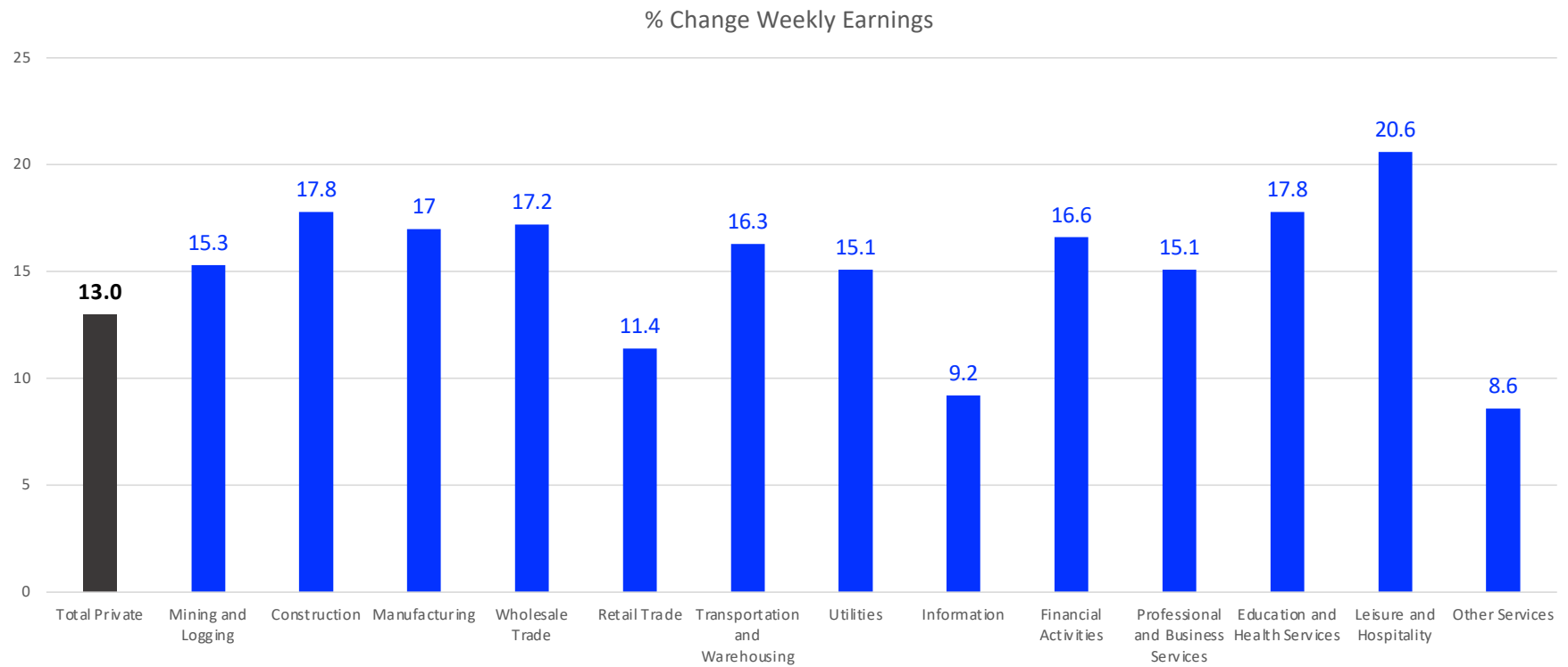
Employment Gains By Industry



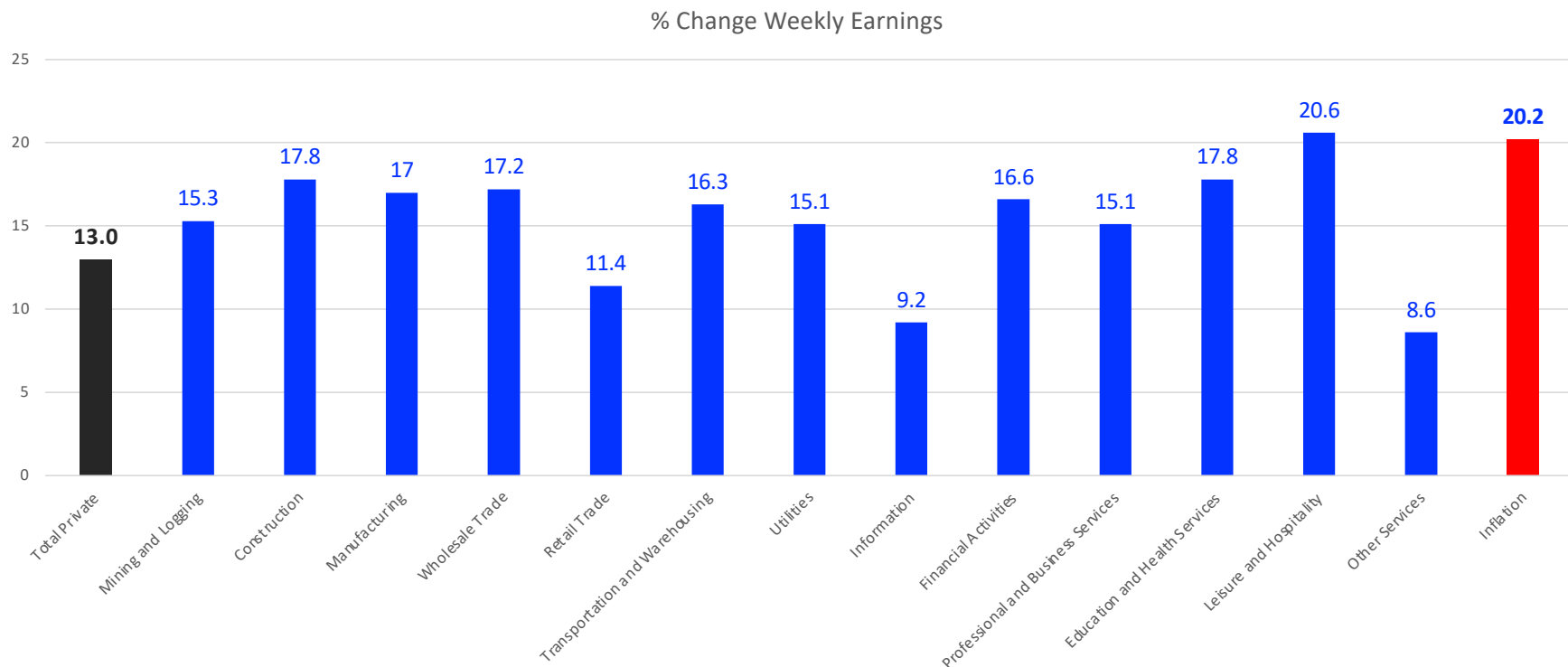
Employment Gains and Losses



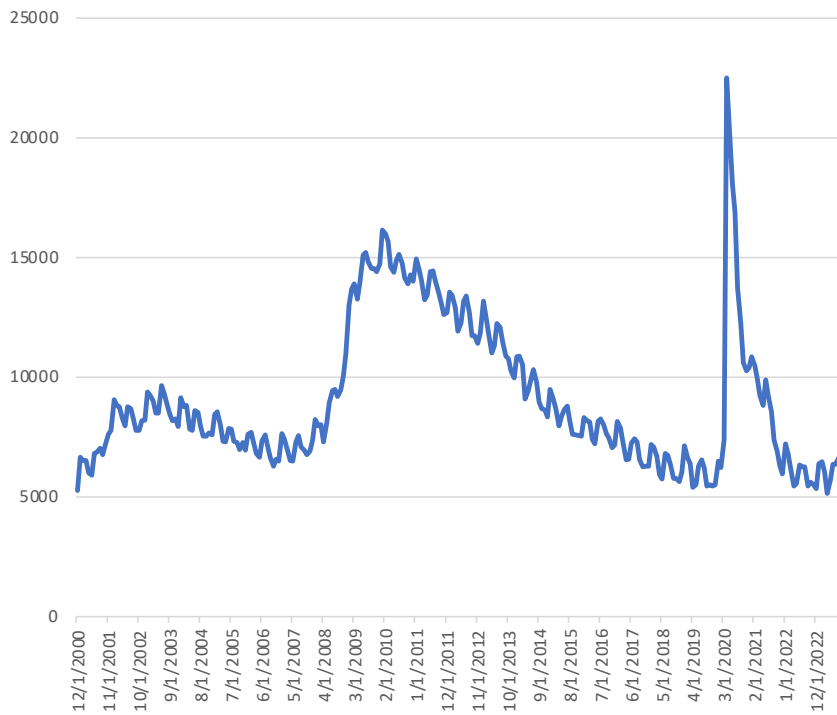
Wage Gains by Industry



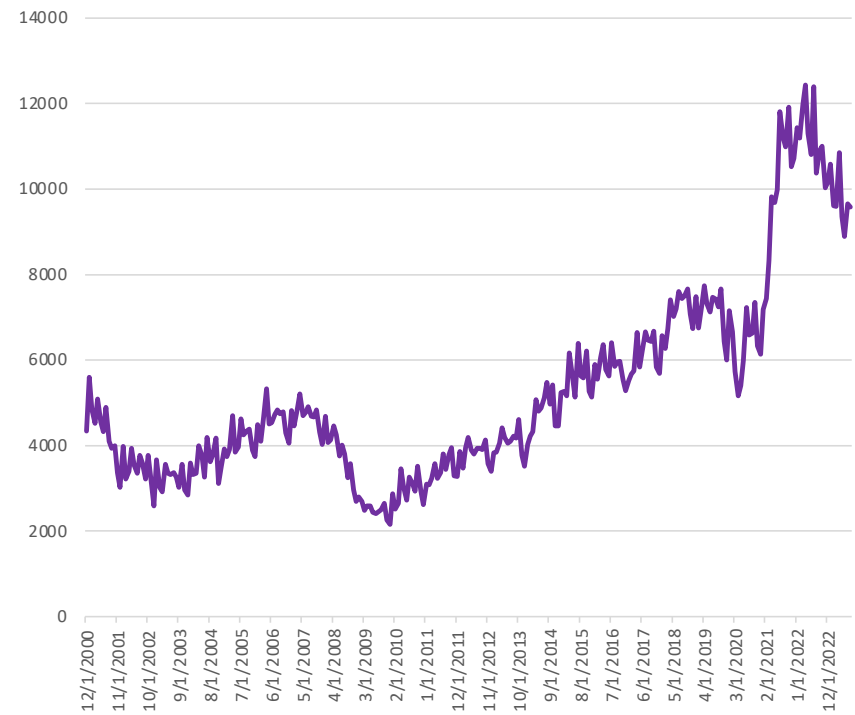
Wage Gains by Industry



Labor Market: Employment

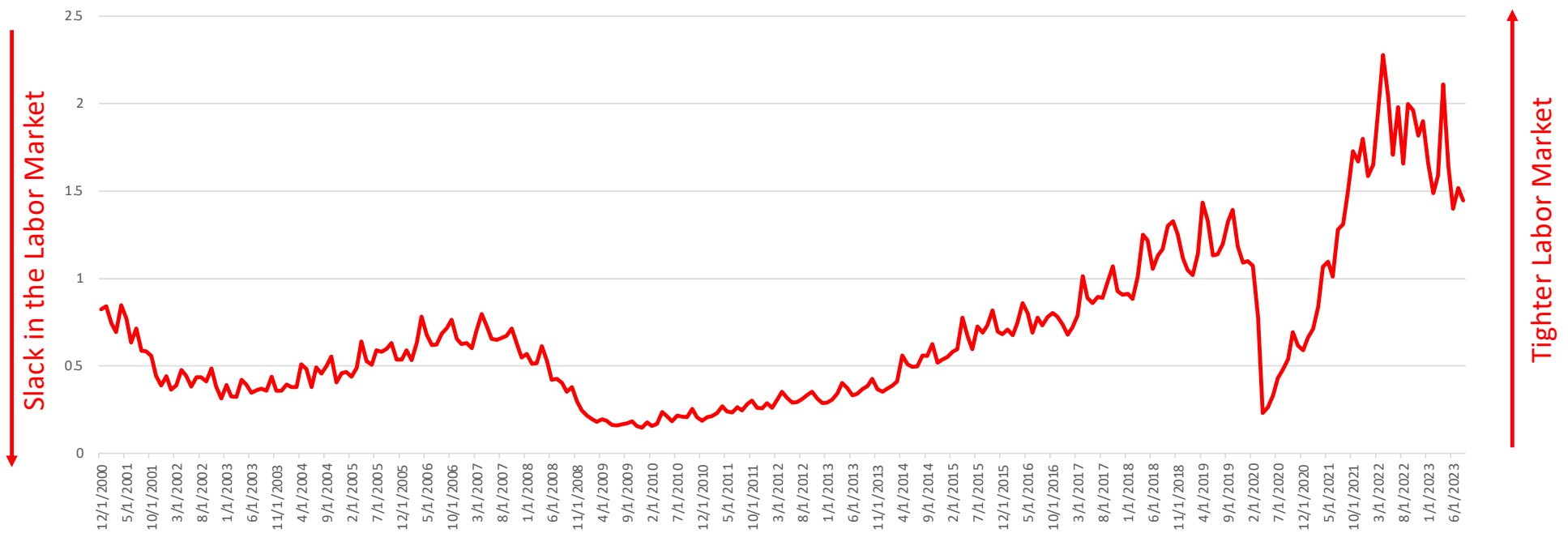


Level Unemployment



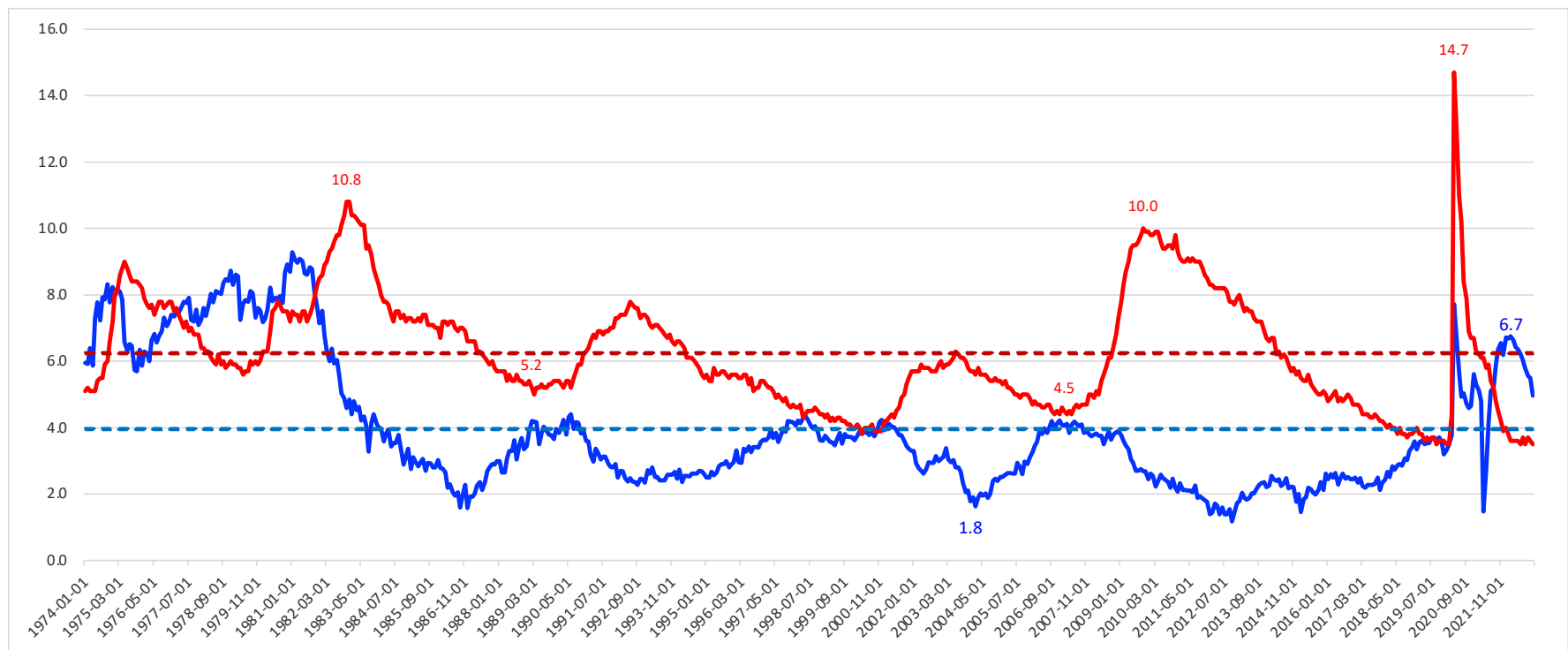
Vacancies

Vacancies Per Unemployed Worker

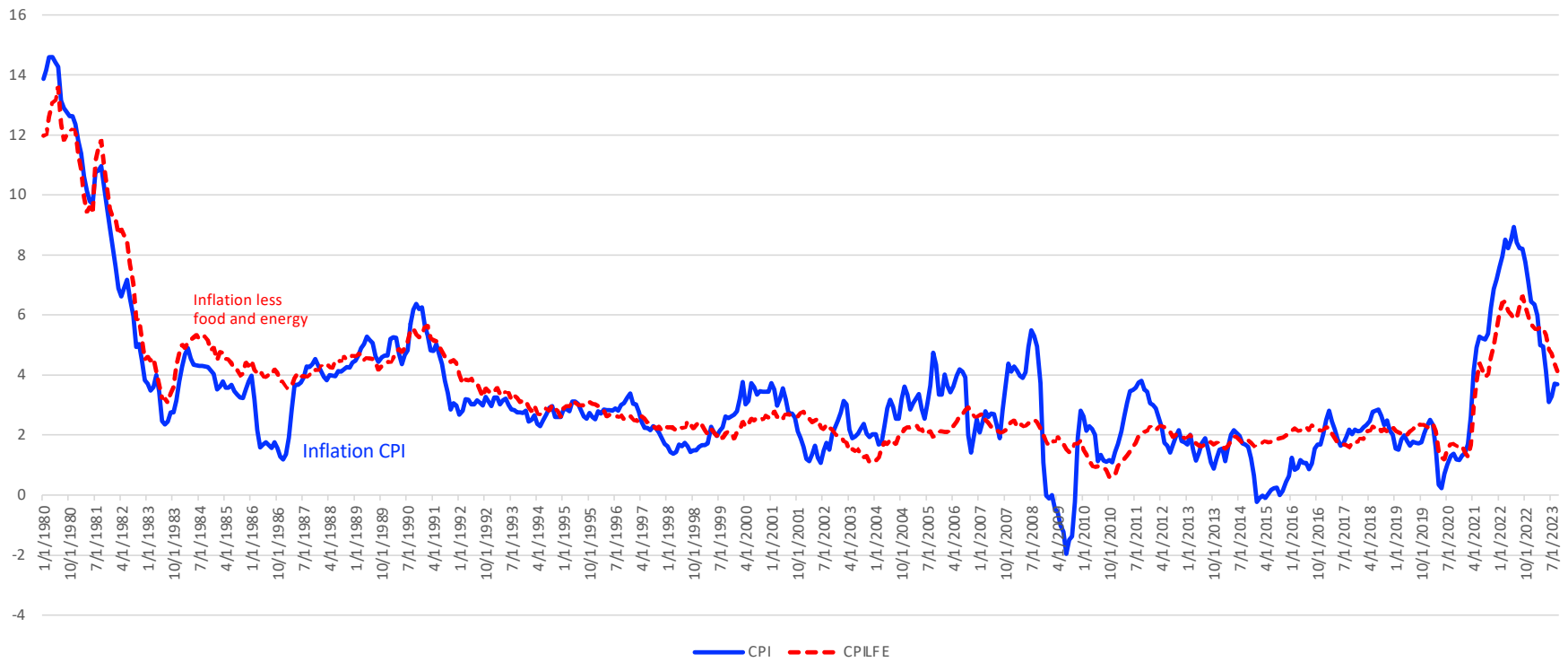


When vacancies per worker go up, more firms are competing for each worker.
This can induce pressure on wage.

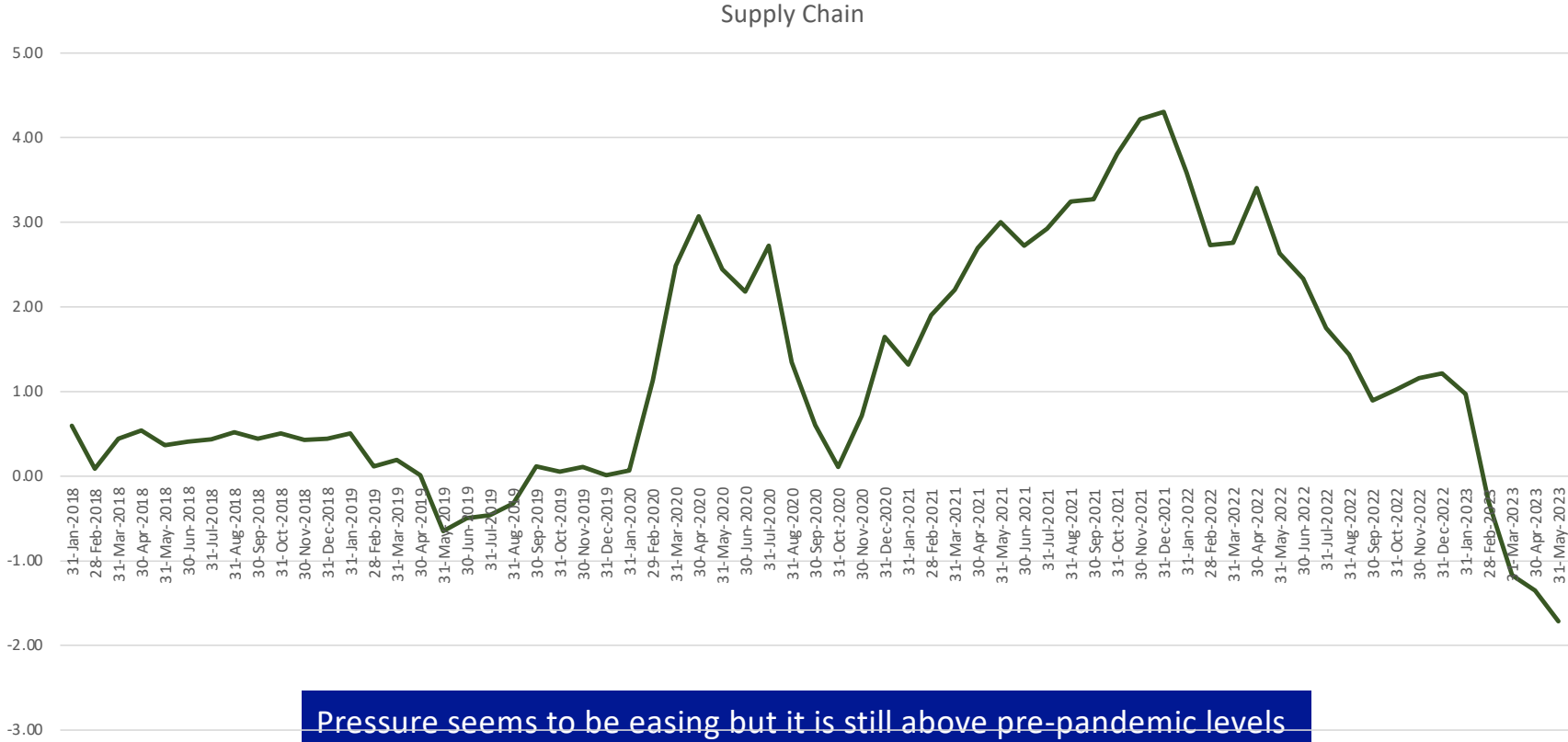
Wages and Unemployment



Inflation



Global Supply (and Demand) Chains

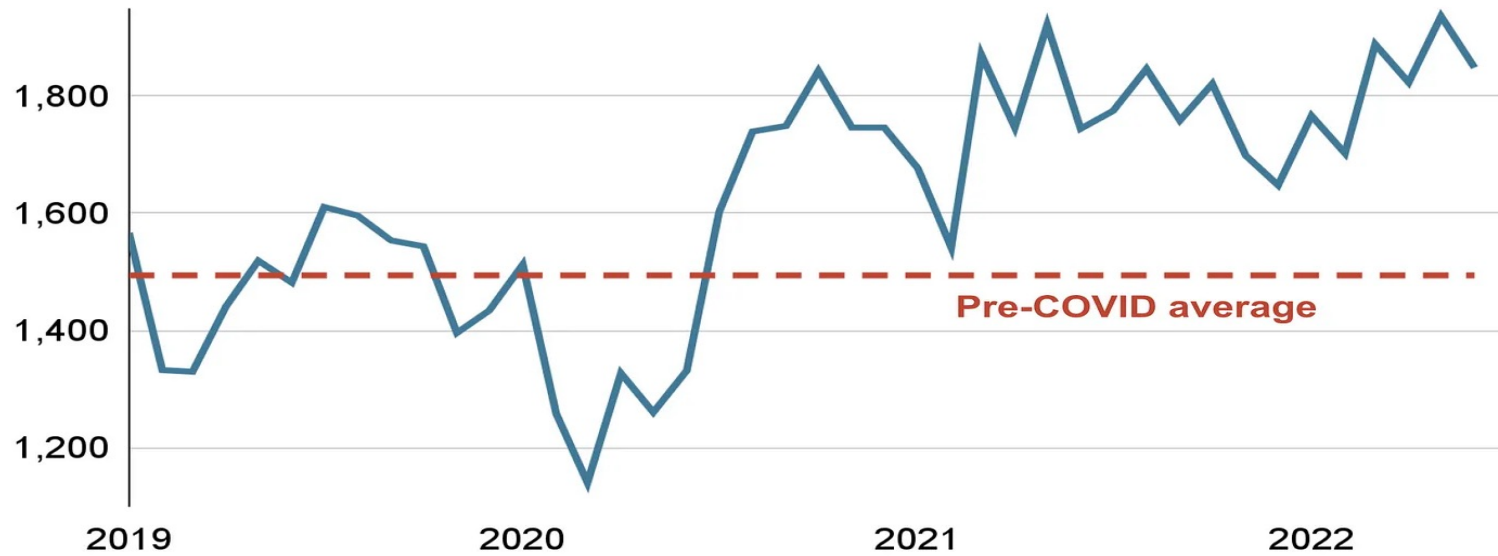


Source: New York Federal Reserve

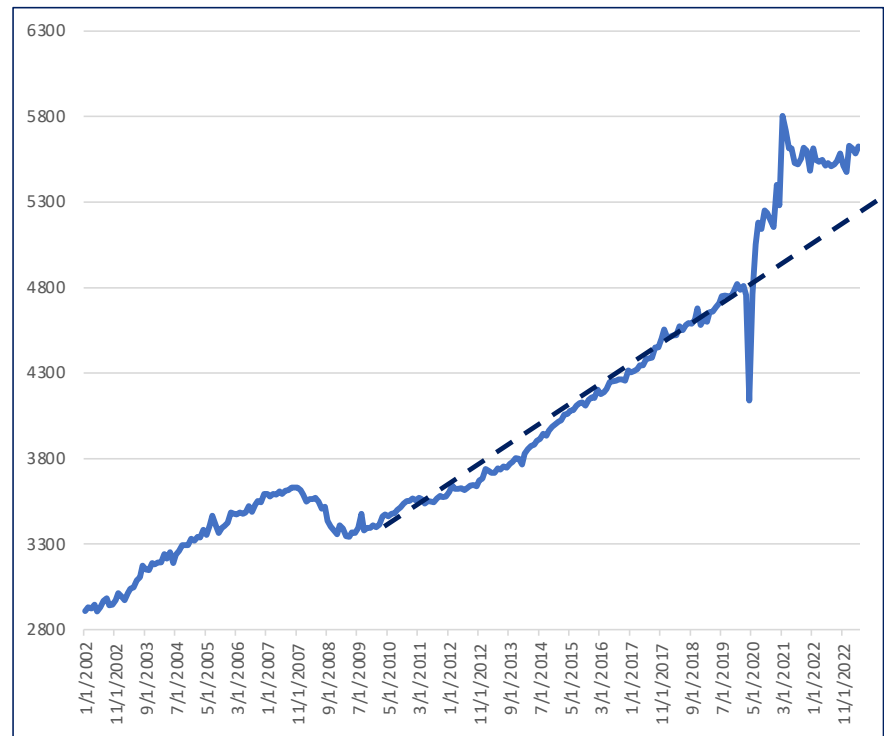
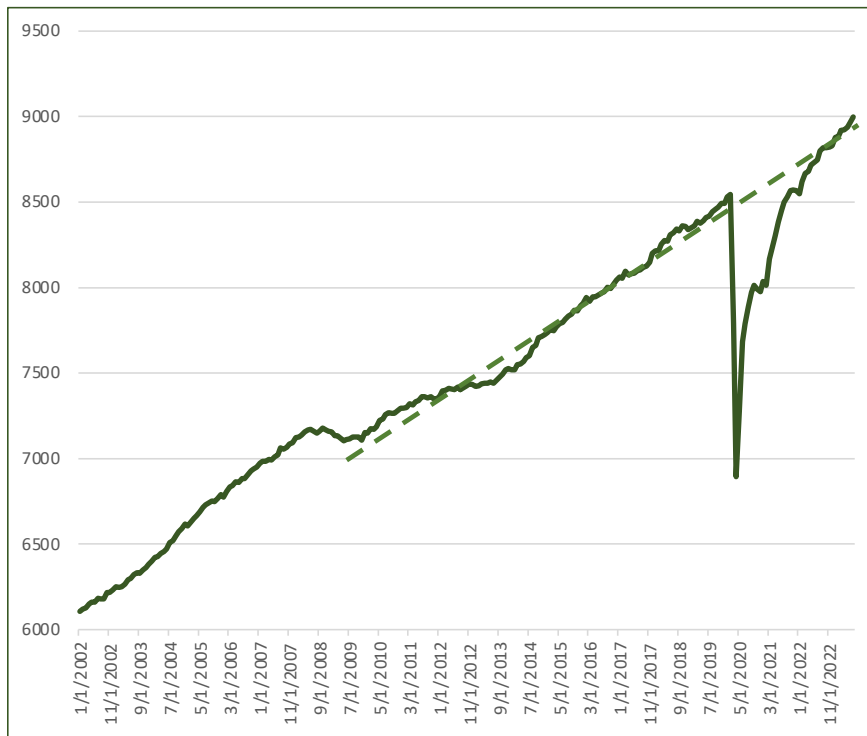
Not all Supply Disruptions

Imports are up significantly since the pandemic

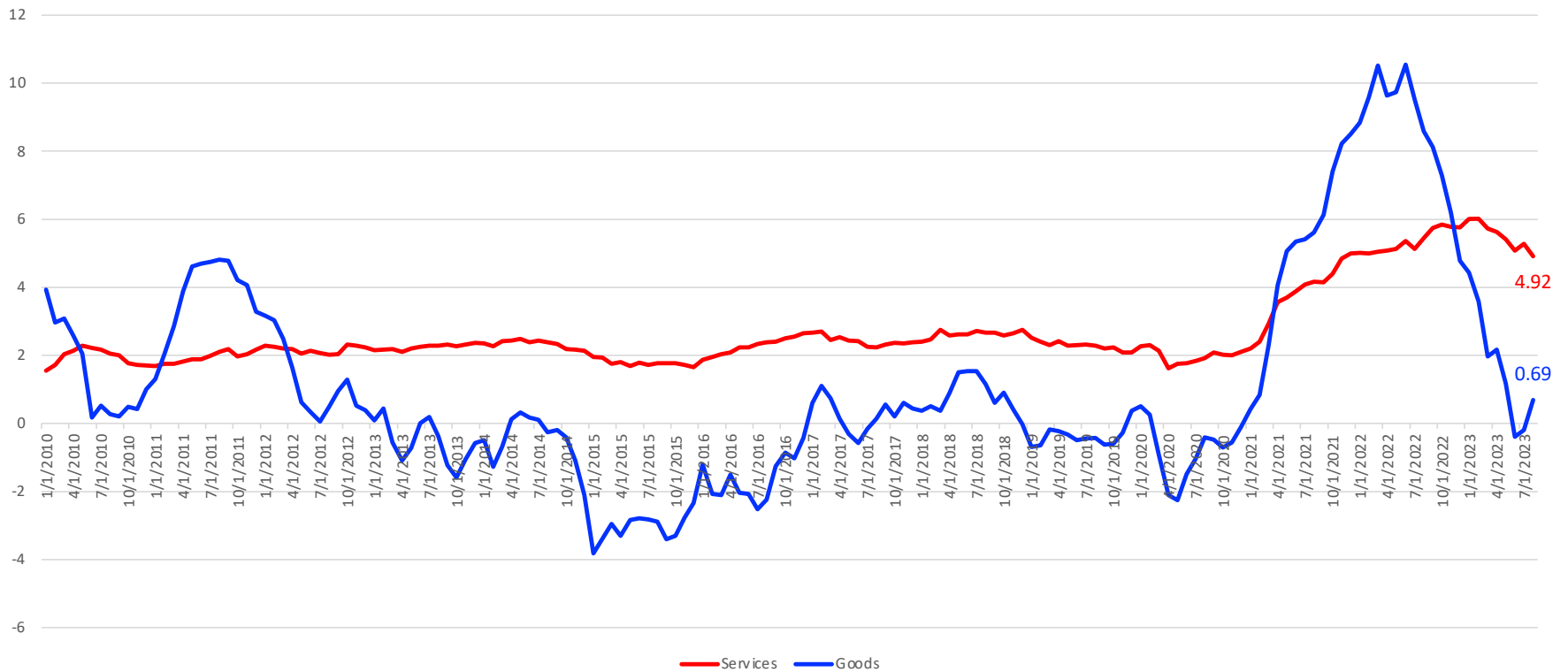
Thousands of TEUs of containerized imports through six major US ports



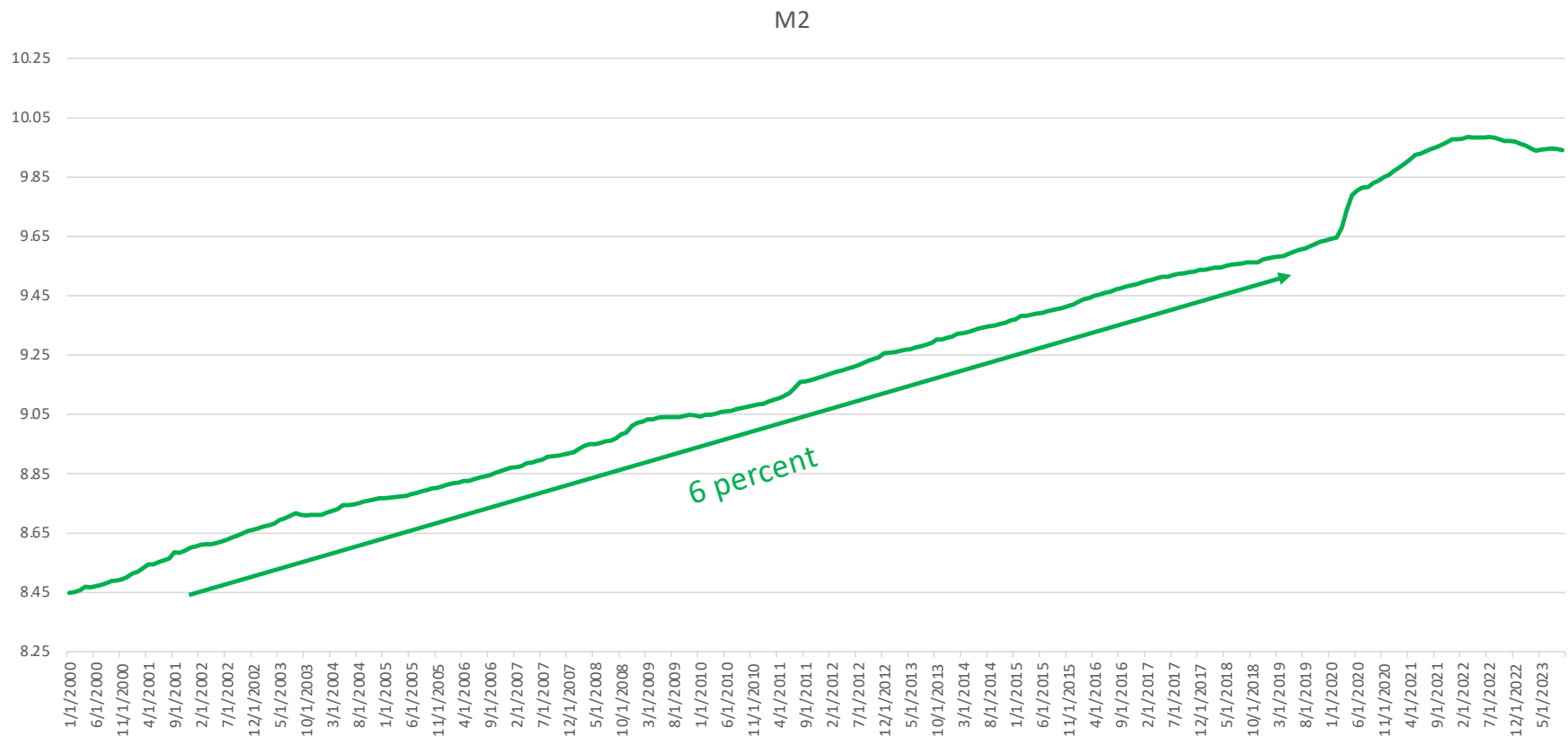
Goods and Service Consumption



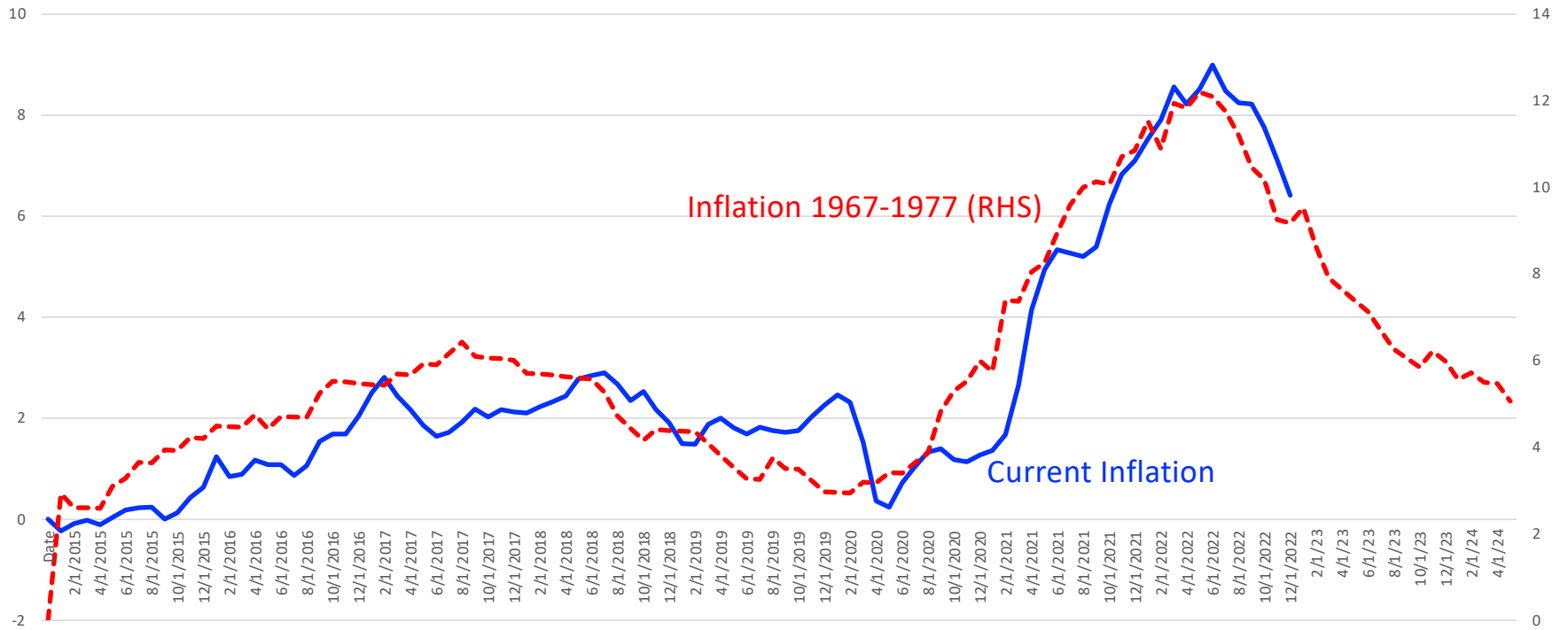
Goods and Service Inflation



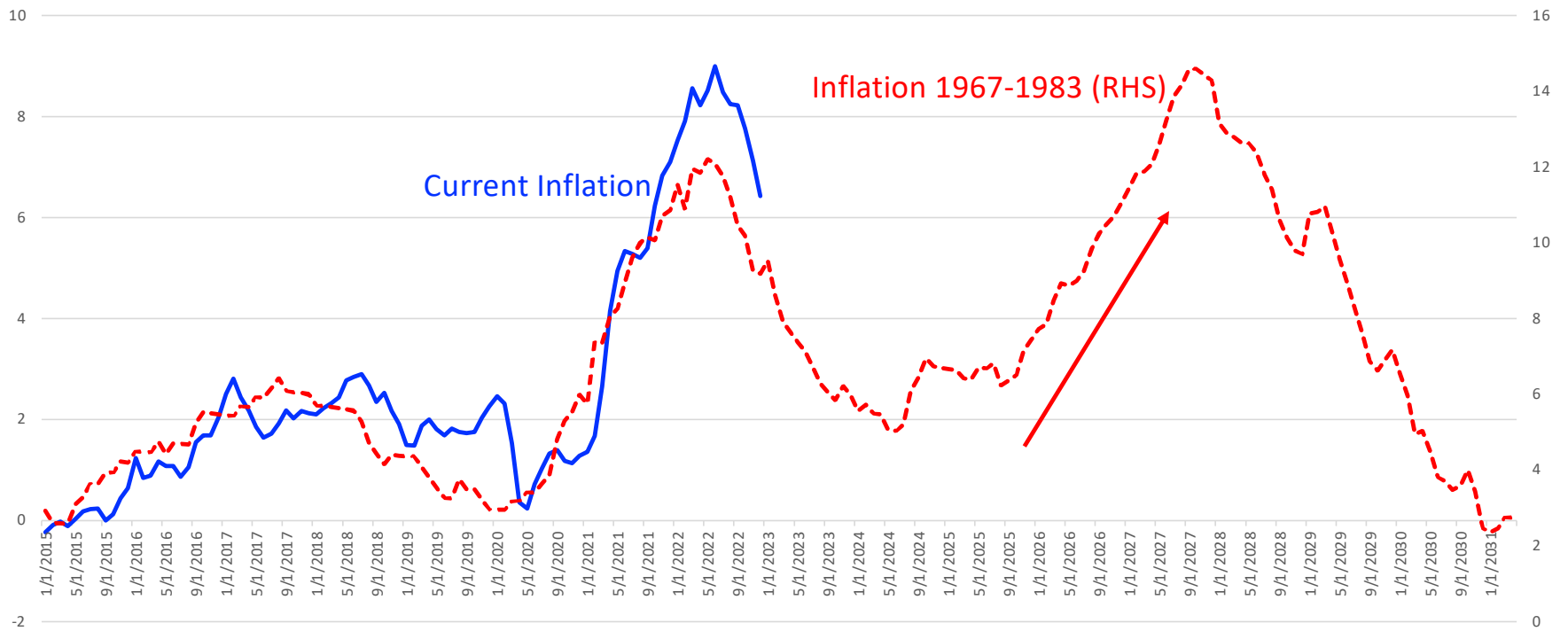
Money Growth: M2 (Transactions Money)



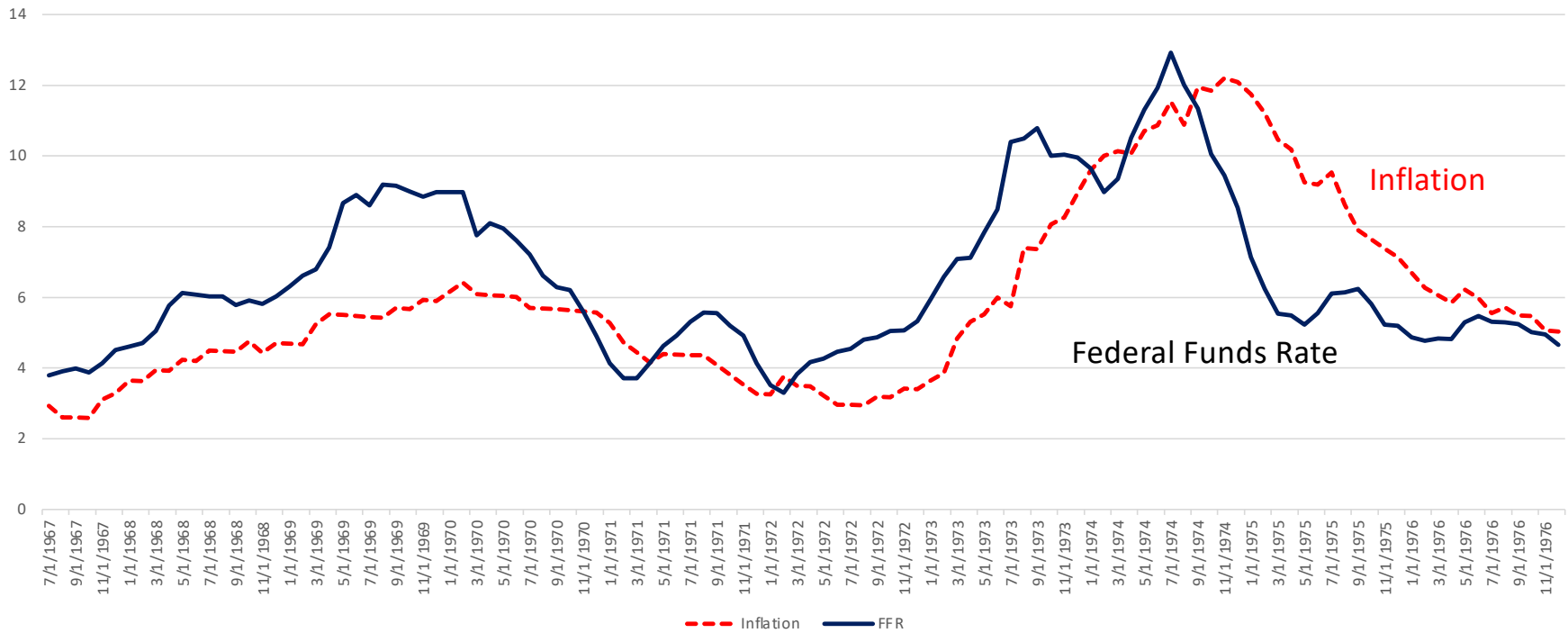
Inflation: Comparison



Inflation: Comparison



Inflation and Federal Funds Rate: 1967-1976



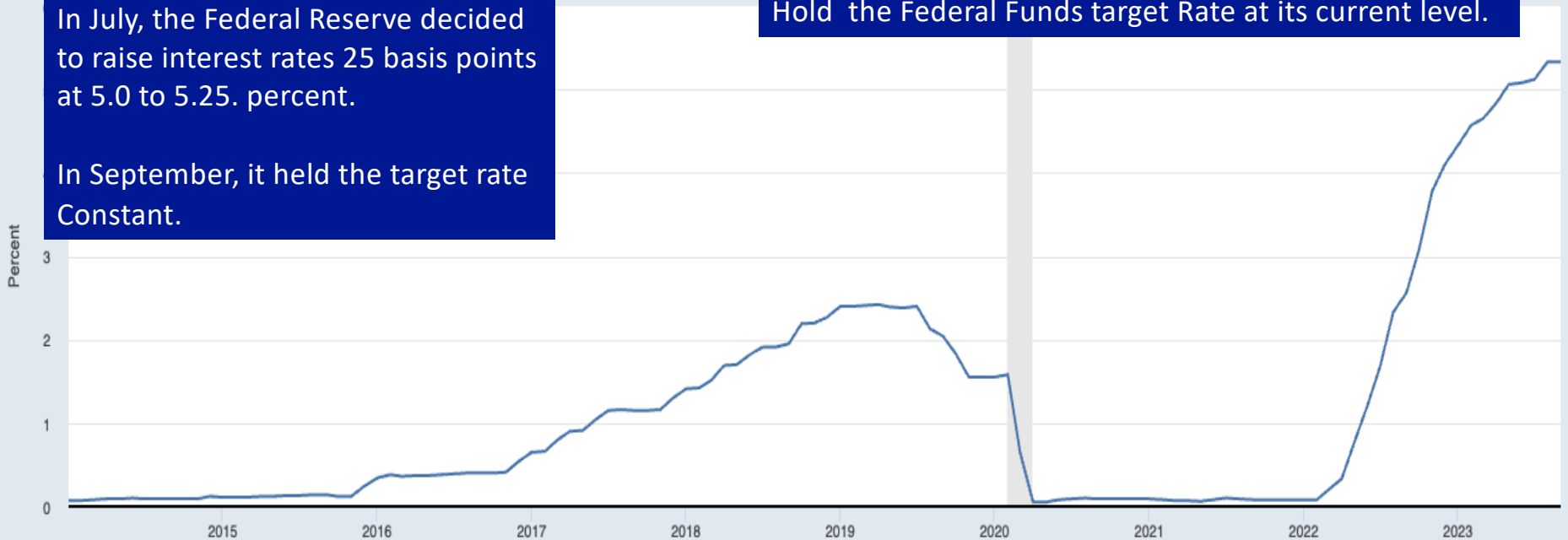
Federal Funds Rate

FRED — Federal Funds Effective Rate

In July, the Federal Reserve decided to raise interest rates 25 basis points at 5.0 to 5.25. percent.

In September, it held the target rate Constant.

Next week, the Federal Reserve will likely Hold the Federal Funds target Rate at its current level.



Shaded areas indicate U.S. recessions.

Source: Board of Governors of the Federal Reserve System (US)

fred.stlouisfed.org

Inflation Outlook

- The inflation outlook is improved:
 - Falling commodity prices,
 - Supply chain improvements,
 - Higher interest rates cooling demand,
 - Reduction of the money supply.
- Still issues – core inflation is well above the target rate of 2 percent.
- Main question: How much lower does inflation have to go before the Fed takes off the breaks?

Summary

- In the September meeting, the Federal Reserve decided to hold their targeted interest rate steady the Federal Funds Rate, to 5.25% – 5.50%
 - The Federal Reserve is expected to hold interest rate at this level when they meet next week from Oct 31 to November 3
- 2023:Q2 GDP growth was a revised down to 2.1% following a 2.2% increase in the first quarter.
 - 2023:Q3 Comes out tomorrow – expected to be 3.4 % and Atlanta Fed GDPNow comes in at 5.4%
- Inflation continues to trend down.
- Labor market continues to add jobs, but the last couple of job reports indicate that the labor is not quite as overheated as it was earlier in the year.

