The Outlook for the U.S. Economy

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Federal Reserve Bank of Dallas

Vistas from Texas: An Economic Update
Houston, 7th August 2015

The views expressed are those of the author and do not reflect the views of the Federal Reserve Bank of Dallas or the Federal Reserve System
Slow and Uneven Recovery from the Great Recession

Output Recovered in 2011 Q2, Employment and Production in 2014 Q2

Sources BEA. Note: Shaded areas indicate recessions.
Much Slower Recovery than in Previous Recessions

Many Domestic and External Headwinds/Shocks
Consumer Confidence Was Easily Rocked …

Relatively High Now Despite Dip in July

Sources: Conference Board and Reuters/U. Michigan future expectations indices
Bond Risk Spreads Rose in Crises

Spread a Little Elevated - 10 Year Treasuries Low

Sources: Federal Reserve and Moody’s (Haver)
Deleveraging Contributed to Anemic Recovery

Households and firms had to reduce their debt
Banks had to rebuild their balance sheets

Sources: BEA (Disposable Personal Income) and Board of Governors (Net Worth & Debt)
The State of the Economy
Estimate of 2.3% GDP Growth in Q2 Likely to be Revised Up

Weak 0.6% Growth in Q1

Real GDP Growth Rate

Source: BEA. Note: Shading denotes NBER dated recessions.
Momentum Regained - Economic Activity Improving

According to ADS Coincident Index

Source: BEA, CBO and Philly Fed
ISM Composite Indices Suggest Economy Is Expanding
Manufacturing Dipped a Little, Non-Manufacturing Rose Sharply in July
The Labor Market
Recent Payroll Employment Numbers Quite Strong

<table>
<thead>
<tr>
<th>Non-Farm Payrolls (000’s, SA, BLS)</th>
<th>Average</th>
<th>Monthly</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>2012</td>
<td>2013</td>
</tr>
<tr>
<td></td>
<td>188</td>
<td>199</td>
</tr>
</tbody>
</table>
Low Level of Labor Market Slack

Headline Unemployment Rate of 5.3% in June; Wage Growth Muted

Sources: BLS and CBO. Notes: The U-6 unemployment includes discouraged workers, other marginally attached workers, and those working part time for economic reasons.
Core and Trimmed Mean PCE Inflation Below 2% Target

Inflation Expectations Well Anchored

<table>
<thead>
<tr>
<th>PCE Inflation (12 month)</th>
<th>2013</th>
<th>2014</th>
<th>Jun 2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Headline</td>
<td>1.20%</td>
<td>1.33%</td>
<td>0.33%</td>
</tr>
<tr>
<td>Core (Ex. Food &amp; Energy)</td>
<td>1.34%</td>
<td>1.41%</td>
<td>1.29%</td>
</tr>
<tr>
<td>Trimmed Mean (May)</td>
<td>1.45%</td>
<td>1.57%</td>
<td>1.61%</td>
</tr>
</tbody>
</table>

Sources: BEA and Dallas Fed.
Housing Markets
Gradual Improvement in Housing Market

Starts and Permits

Source: Census Bureau
Gradual Improvement in Housing Market

Single-Family Home Sales

Annualized (000's)

Sources: NAR and Census Bureau.
Fairly Moderate House Price Gains at National Level

Lending Standards Starting to Ease

<table>
<thead>
<tr>
<th>Appreciation (YoY)</th>
<th>Dec 2013</th>
<th>Dec 2014</th>
<th>May/Jun 2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>CoreLogic house prices</td>
<td>+11.3%</td>
<td>+4.9%</td>
<td>+6.3% (Jun)</td>
</tr>
<tr>
<td>FHFA house prices</td>
<td>+7.6%</td>
<td>+5.5%</td>
<td>+5.6% (May)</td>
</tr>
</tbody>
</table>

Notes: CoreLogic single family incl. distressed sales and FHFA purchase only series.
The series are not seasonally adjusted.
Financial Markets
Limited Stress in U.S. Financial Markets

Note: The KC Fed financial stress index captures the common component in a range of financial variables, including the TED spread, various corporate bond spreads, and the VIX.
Stock Markets High ... Albeit Very Volatile

Source: Haver Analytics.
Interest Rates Are Low ... Expected to Rise Gradually

Sources: Federal Reserve Board and Blue Chip.
Plunge in Oil Prices

On Net, Good for U.S. and Global Economy
But A Jolt for Texas
Plunge in Oil Prices and U.S. Economy

• Strong supply and weak global demand
  o Nov 2014 OPEC decision to maintain production
  o June nuclear deal with Iran

• For the U.S., a net importer of oil, the main effects are:
  o **Incomes** (↑): real incomes and consumption rise
    ▪ Estimated $700+ gain for typical household
  o **Costs & Profits** (↓?):
    ▪ Oil exploration related investment falls sharply
    ▪ Other investment gradually rises
  o **Inflation** (↓): headline and core inflation fall temporarily
NYMEX WTI Futures Prices
Great Uncertainty!

Sources: Haver Analytics, Bloomberg and author’s calculations
Forecasts of U.S. Economy
Forecasts of GDP Growth and Inflation

• **Very difficult to forecast GDP (output) growth** with any reasonable degree of accuracy:
  - The economy continually evolves
  - Shocks are common, but unpredictable
  - Turning points are hard to identify in real time

• **It was easier to forecast inflation** – less so now

• **Average or combinations of forecasts better than any individual forecast** e.g.
  - SPF (Survey of Professional Forecasters)
  - Blue Chip Economic Indicators
  - FOMC (Federal Open markets Committee)
# Forecasts for Current and Next Two Quarters

## Output / GDP Growth (SAAR)

<table>
<thead>
<tr>
<th></th>
<th>2015 Q3</th>
<th>2015 Q4</th>
<th>2016 Q1</th>
</tr>
</thead>
<tbody>
<tr>
<td>Blue Chip</td>
<td>3.2%</td>
<td>3.0%</td>
<td>2.7%</td>
</tr>
<tr>
<td>SPF</td>
<td>3.1%</td>
<td>2.9%</td>
<td>2.4%</td>
</tr>
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</table>

## Unemployment Rate (Ave)

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<th>2015 Q3</th>
<th>2015 Q4</th>
<th>2016 Q1</th>
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<tr>
<td>Blue Chip</td>
<td>5.3%</td>
<td>5.1%</td>
<td>5.0%</td>
</tr>
<tr>
<td>SPF</td>
<td>5.3%</td>
<td>5.2%</td>
<td>5.1%</td>
</tr>
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Sources: Blue Chip Economic Indicators, July 2015 and Survey of Professional Forecasters (SPF), May 2015.
## Annual Forecasts

<table>
<thead>
<tr>
<th>Economic Indicator</th>
<th>Forecaster</th>
<th>Actual 2014</th>
<th>Forecasts</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td>2015</td>
</tr>
<tr>
<td>Real GDP Growth, Q4/Q4</td>
<td>Blue Chip</td>
<td>2.4%</td>
<td>2.8%</td>
</tr>
<tr>
<td></td>
<td>FOMC</td>
<td>2.4%</td>
<td>1.8%–2.0%</td>
</tr>
<tr>
<td></td>
<td>SPF</td>
<td>2.2%</td>
<td>2.8%#</td>
</tr>
<tr>
<td>Unemployment Rate, Q4 Ave</td>
<td>Blue Chip</td>
<td>5.3%</td>
<td>4.9%</td>
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<td>4.9%#</td>
</tr>
<tr>
<td>PCE Inflation Rate, Q4/Q4</td>
<td>FOMC</td>
<td>1.1%</td>
<td>0.6%–0.8%</td>
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<tr>
<td></td>
<td>SPF</td>
<td>0.8%</td>
<td>1.9%</td>
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<tr>
<td></td>
<td>FOMC, Core</td>
<td>1.4%</td>
<td>1.3%–1.4%</td>
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Risks to the U.S. Economic Outlook

• Risks are pretty balanced
• Main downside risks are external
  o Further appreciation of the dollar
  o Downturn in China
  o Slow growth in other emerging economies
  o Flare up of conflict in Ukraine or Middle East