



Federal Reserve
Bank of Dallas

The United States Outlook

Vistas from Texas: An Economic Outlook

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The views expressed are my own and do not necessarily reflect official positions of the Federal Reserve System.

Overview

- Real activity
 - Expect GDP growth around 2.5 percent in Q3
 - Evidence of momentum going forward
 - Expect continued growth a bit above potential, further reductions in labor market slack
- Inflation
 - Slowed over past several months
 - With anchored expectations and declining slack, it's still expected to move up over next several quarters

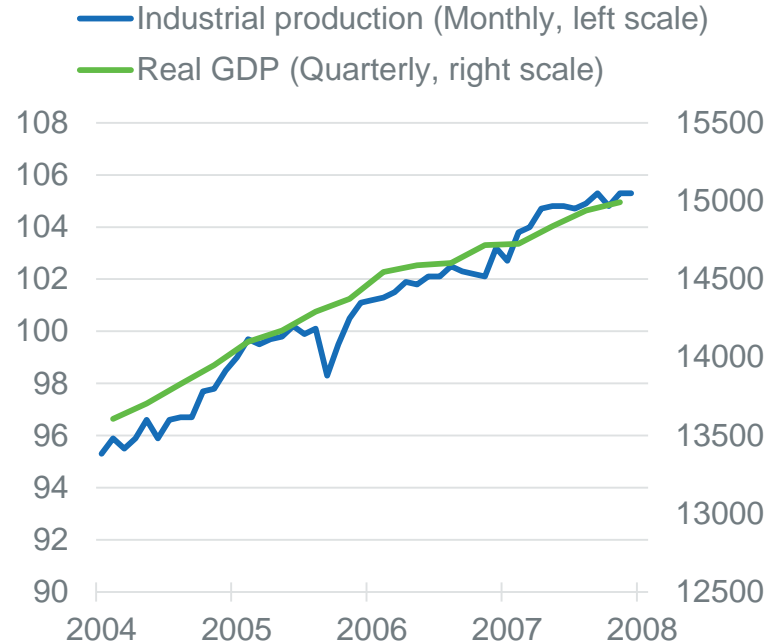
**But first—A few words on the effects of
the recent hurricanes**

The impact of natural disasters

- Disasters like Hurricanes Harvey and Irma have two sorts of effects on the aggregate economy:
 - A **disruption effect**: Production, consumption, and investment temporarily reduced. Economic activity declines, then rebounds. Some activity just shifted in time, some permanently lost.
 - A **capital destruction effect**: Triggers a rebuilding process, usually very gradual, that tends to raise future output.
- Averaged over a several months or quarters, aggregate effects of even large disasters tend to be modest.

The impact of natural disasters

- What do I mean by modest?
- If you didn't know when Katrina & Rita hit, but tried to date them using aggregate data, it's not so easy.
- Can make a good guess with monthly industrial production, not so well with quarterly GDP.



More “noise” relative to “signal” in data recorded at higher frequencies

- We’ve seen some likely hurricane impacts in weekly and monthly data so far:
 - Weekly initial claims for unemployment insurance: Jumped 62K in week after Harvey, still a bit elevated.
 - Monthly payrolls: Fell 33K in September.
 - Industrial production: Down 1 percent in September.
- Will need to “look past” some short-run wiggles in the data, want to do more “averaging” than we normally would.

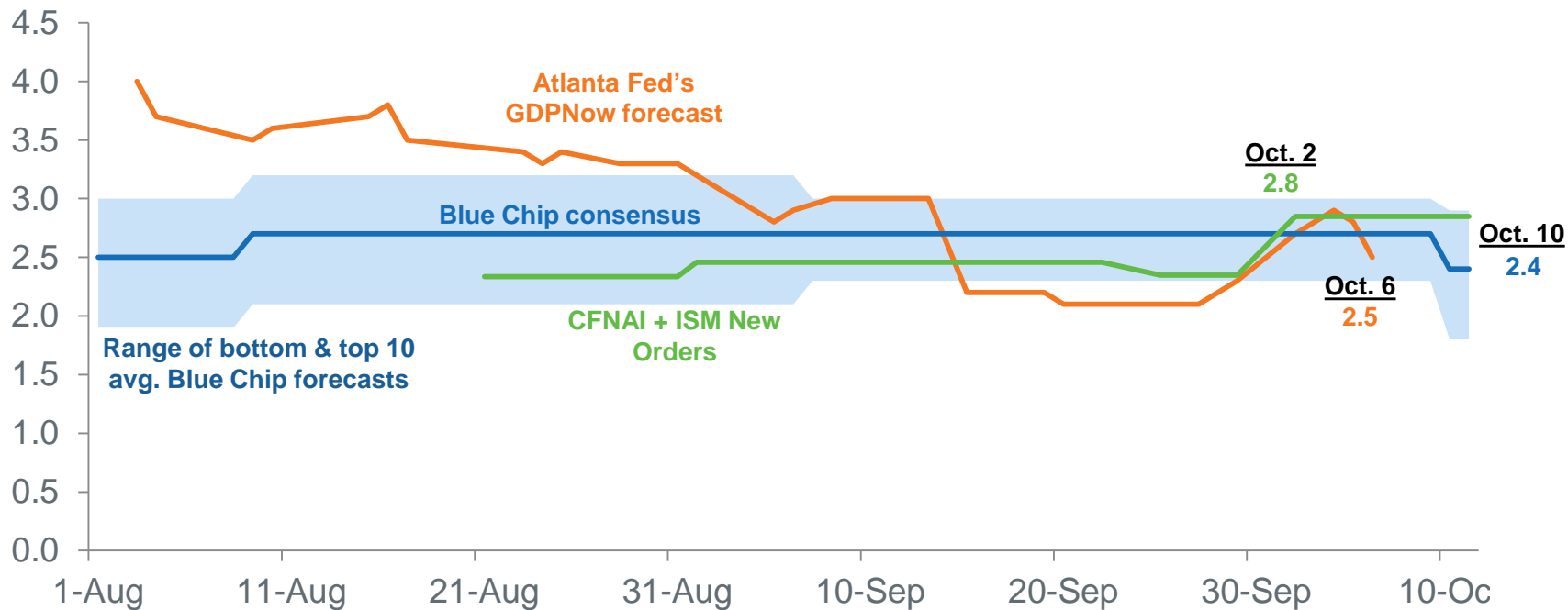
Any impact on inflation?

- Expect to see temporarily higher headline rates, owing to spike in gasoline prices.
 - Seasonally adjusted jumps of 6.3 percent and 13.1 percent in August and September.
- Effects on core inflation less certain
 - Rebuilding process raises materials prices, and that can bleed into core inflation, but likely small and spread out over time
 - Vehicle prices, rents, and energy-sensitive services may also be channels, though no clear sign of this in September CPI.

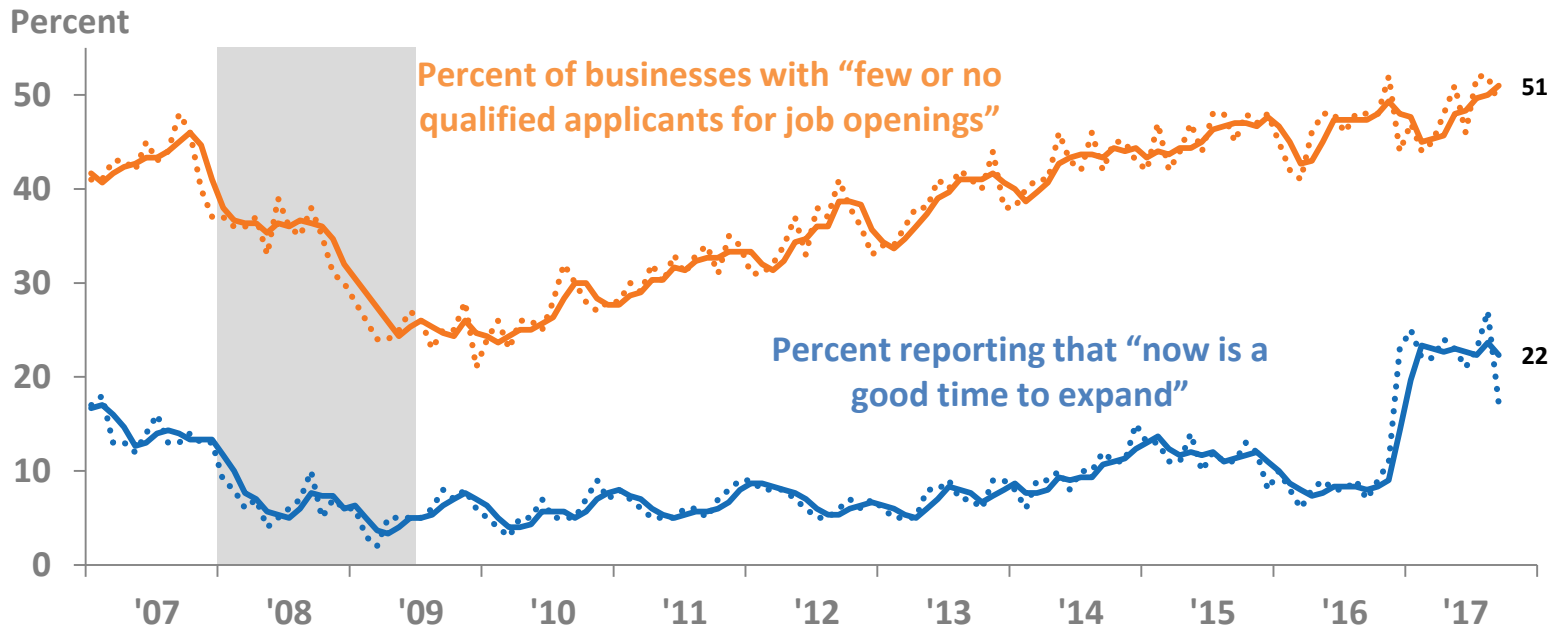
Real activity

Third-quarter GDP-growth estimates are now generally near 2½ percent

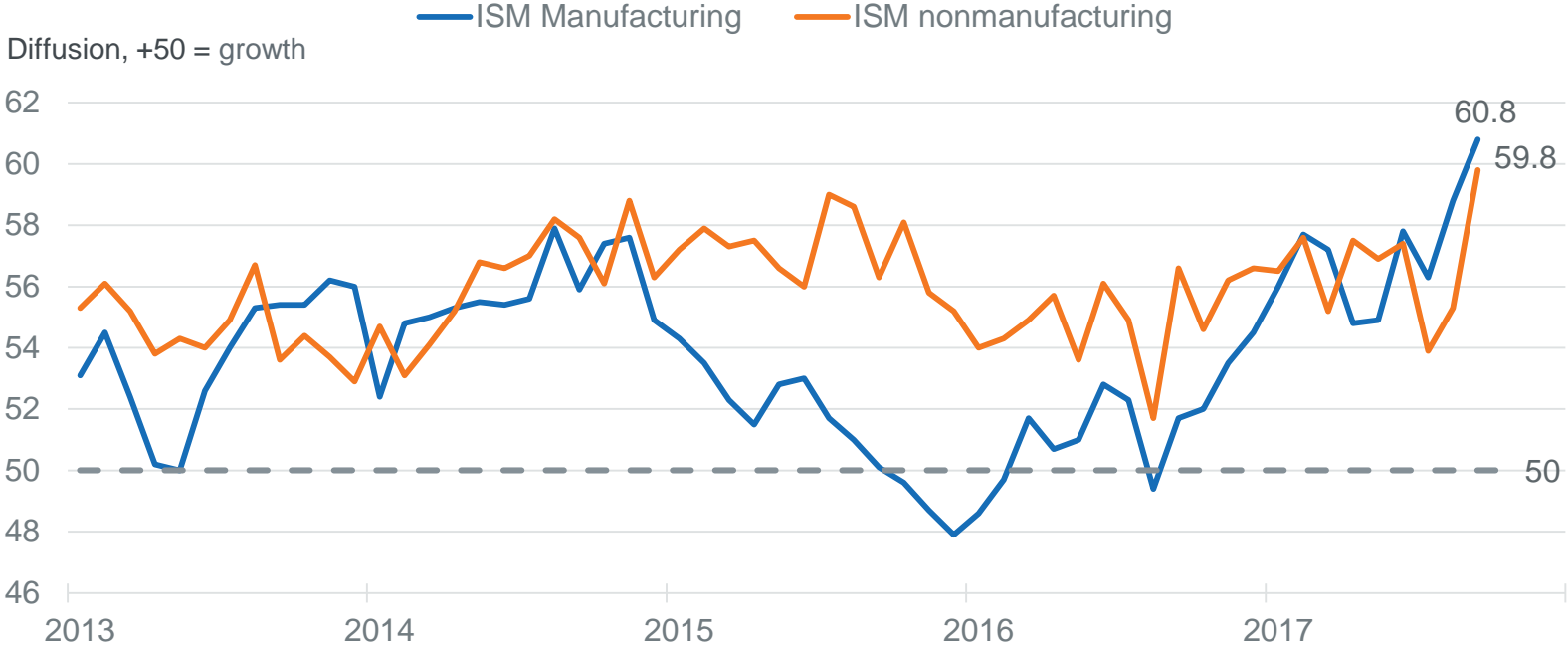
Percent, annual rate



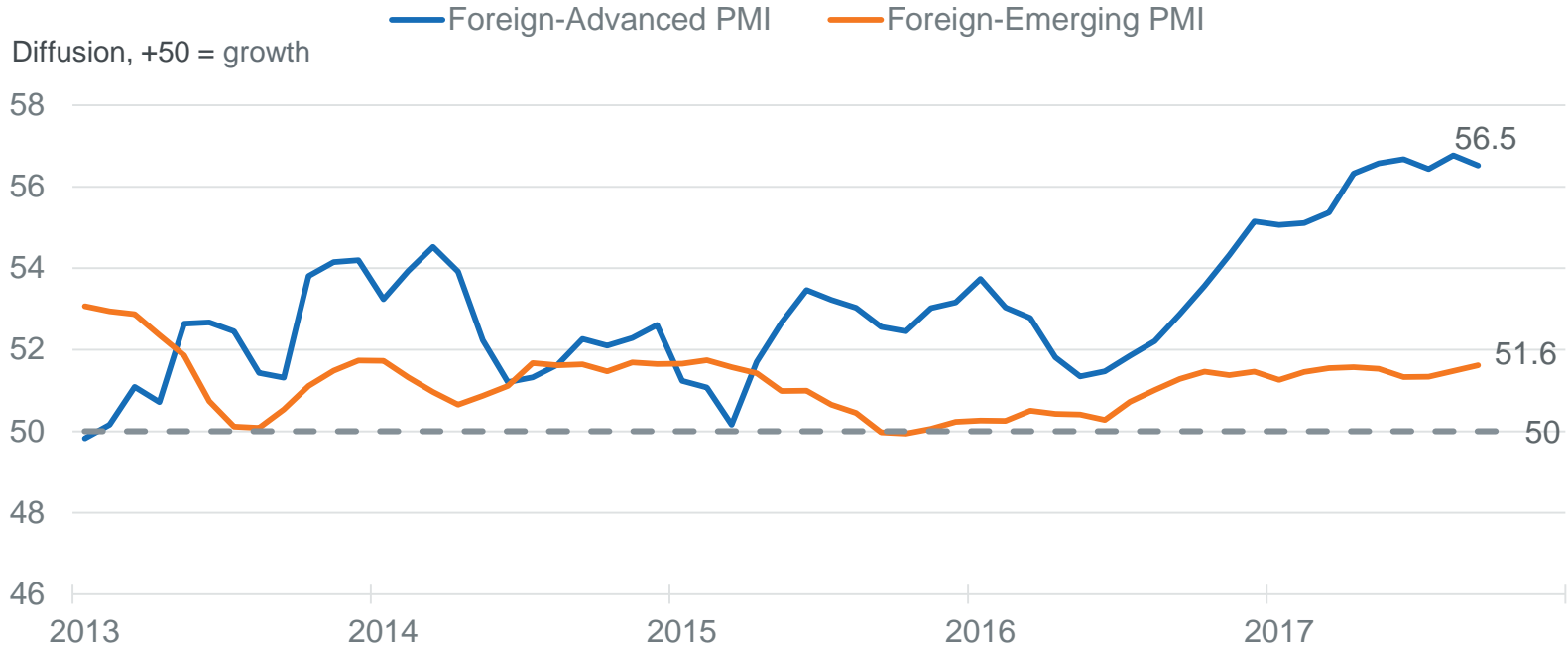
NFIB survey shows a gradually tightening labor market and markedly improved optimism



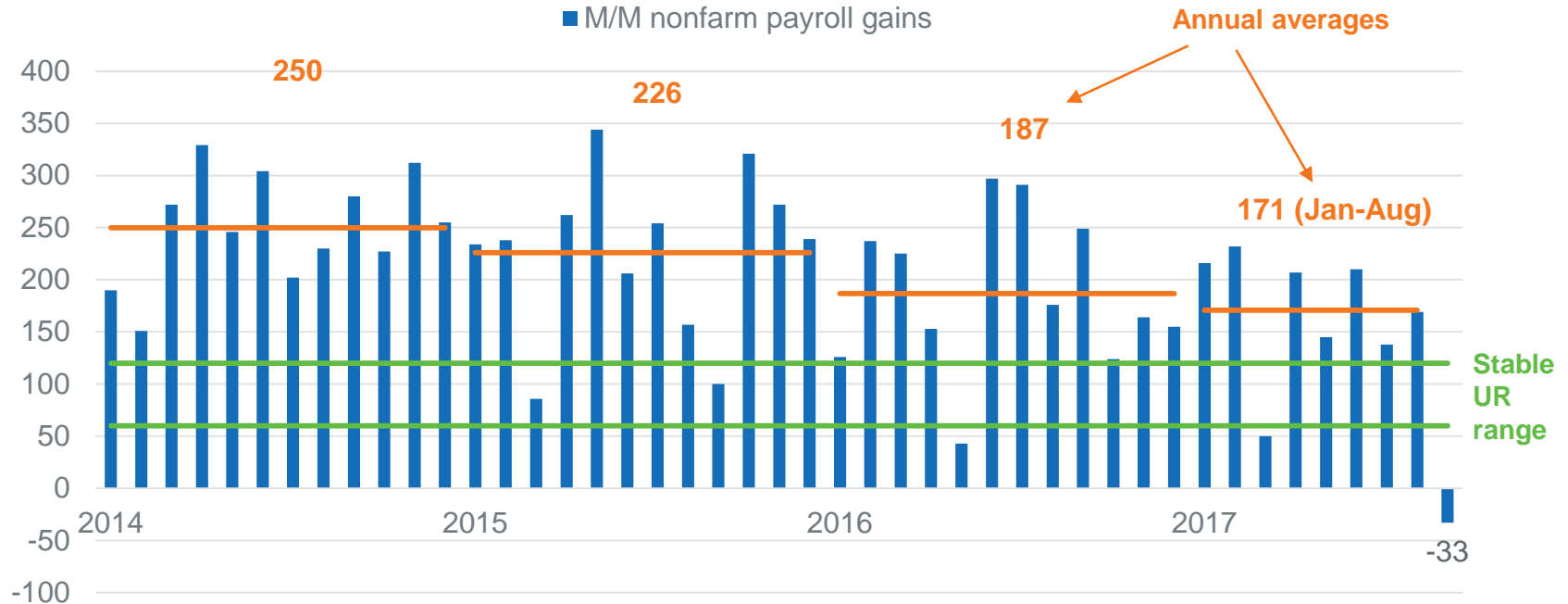
September ISM surveys point to robust growth in manufacturing, services



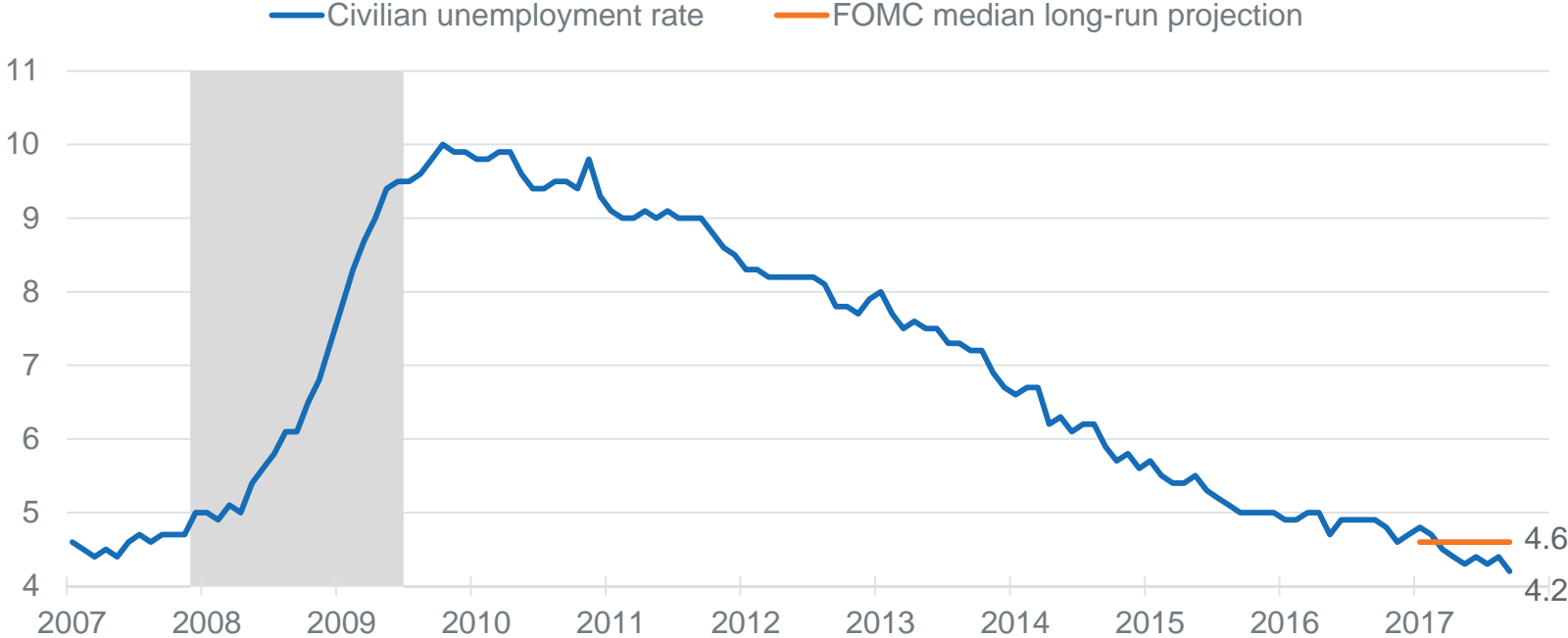
Foreign outlook has improved notably since mid-2016



Pre-September, payroll growth was running well above range consistent with stable unemployment

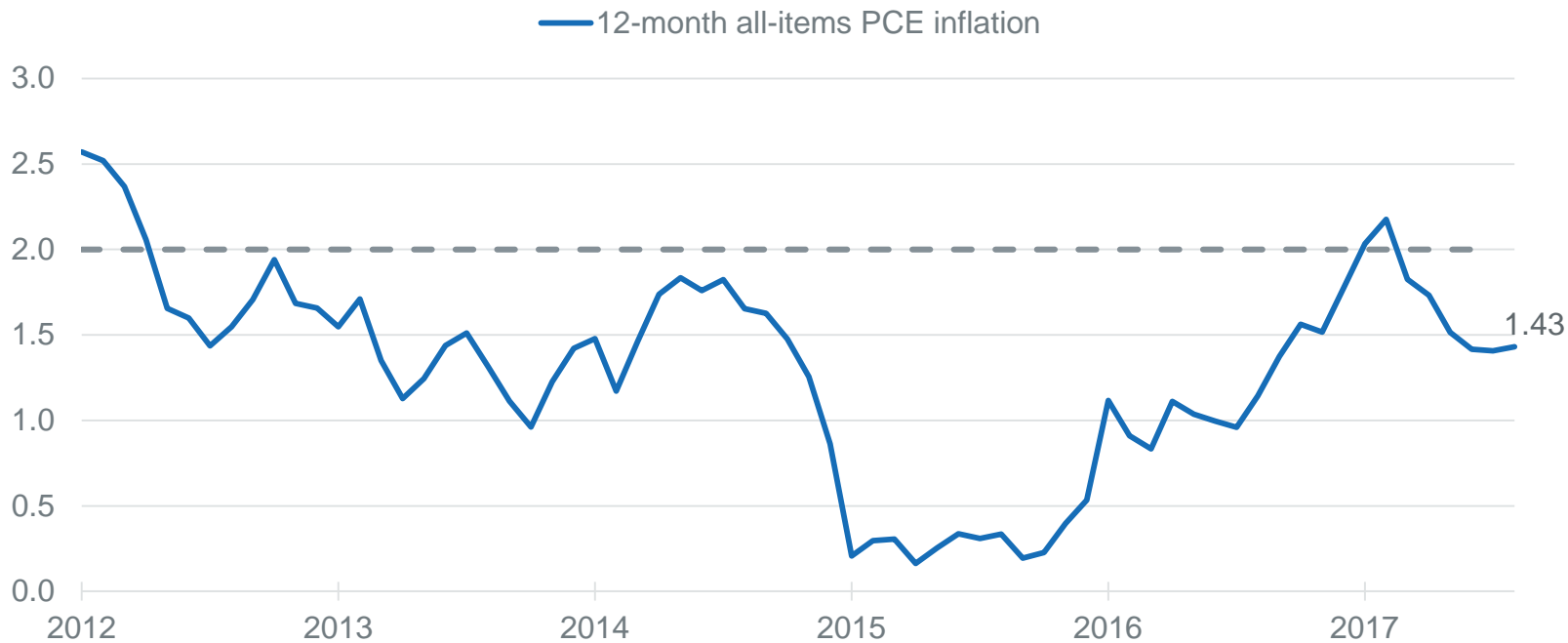


Unemployment rate declines 0.5 p.p. in 2017, below policymakers' long-run projection

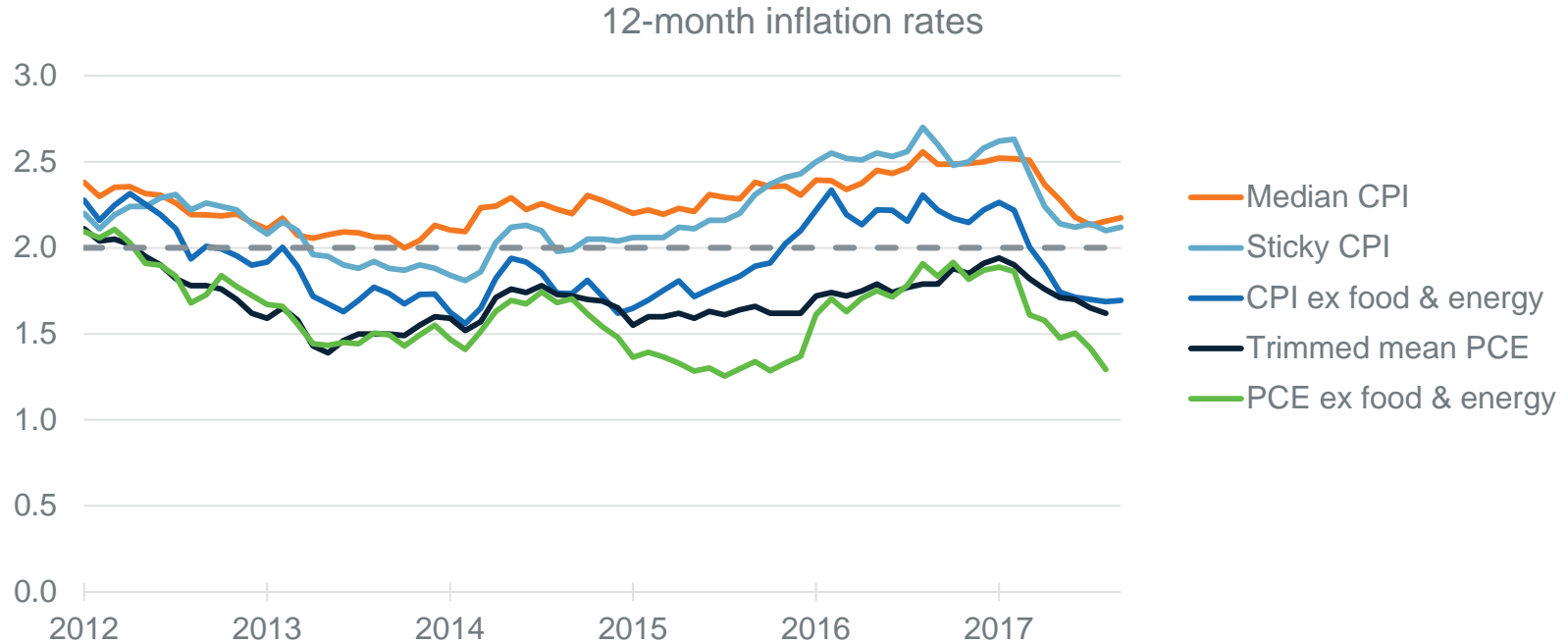


Inflation

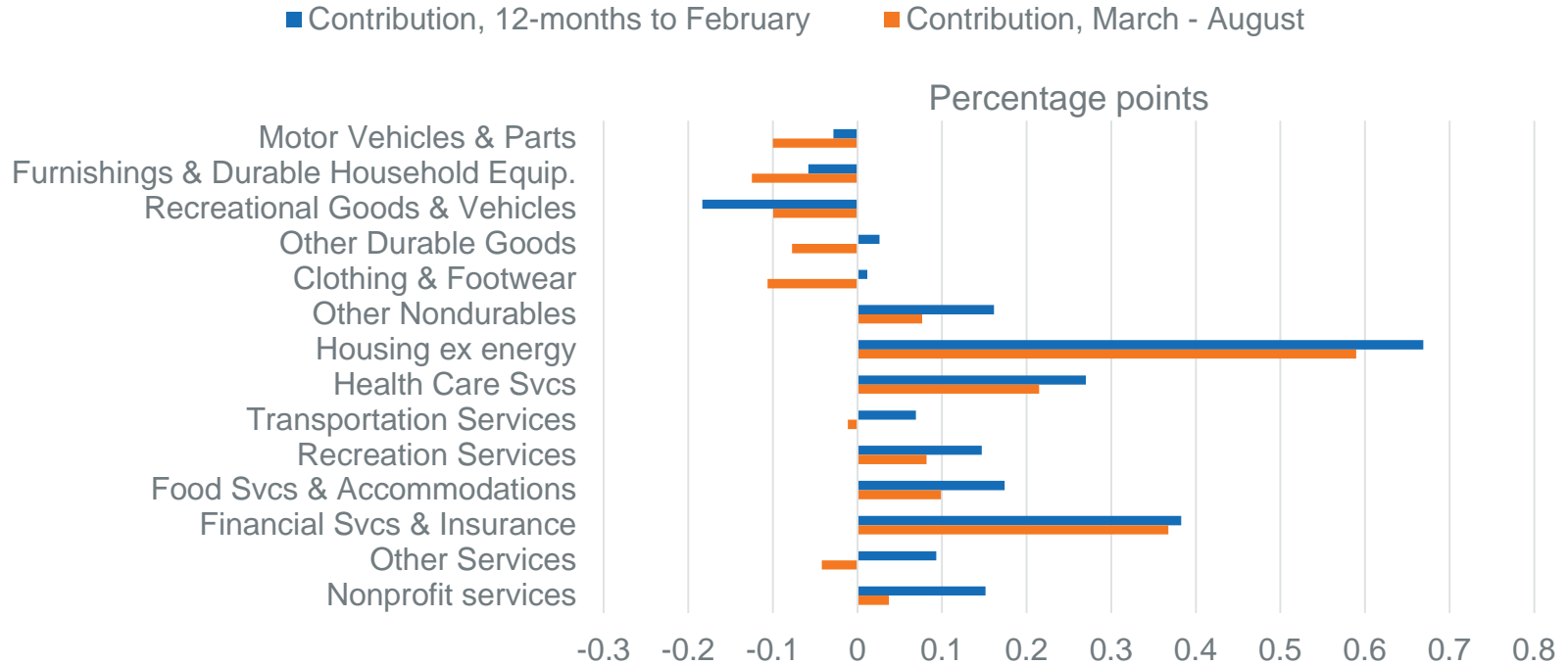
Headline PCE inflation flirted with 2 percent, slowed



Core inflation slows since early in the year



Core PCE deceleration fairly broad-based

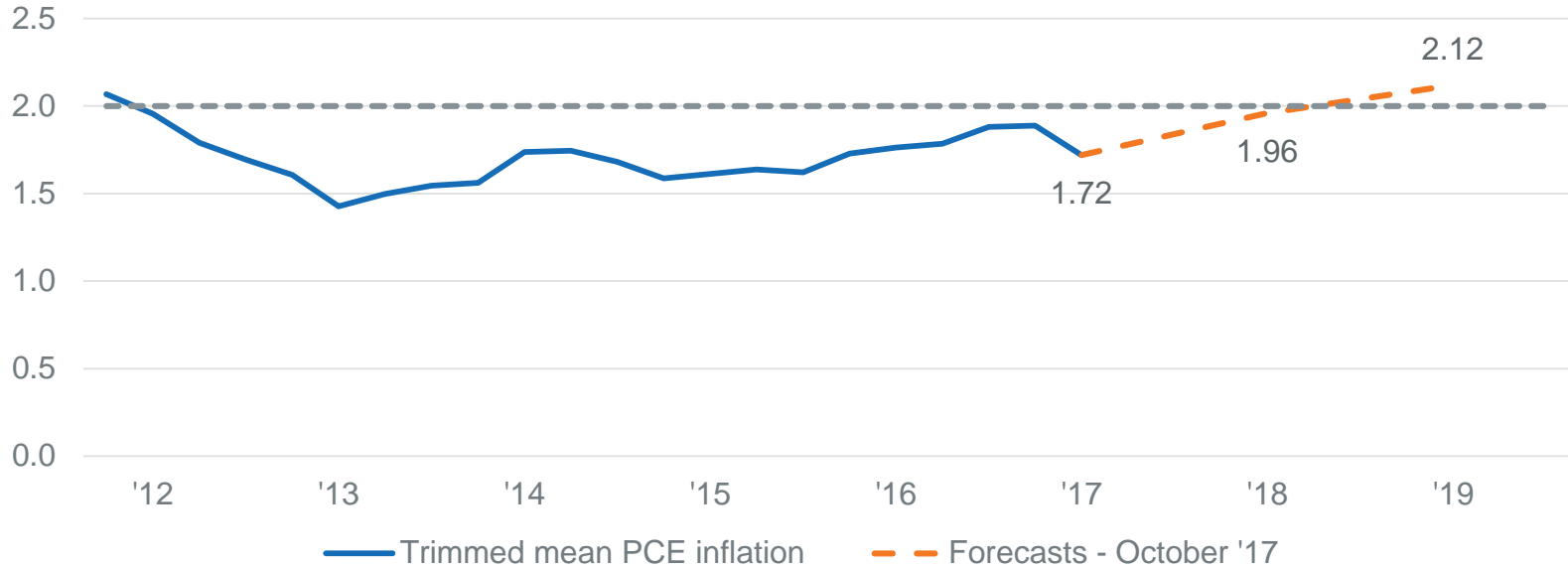


Longer-run inflation expectations appear to remain anchored

- Consumer inflation expectations (University of Michigan survey):
 - Dipped during oil price bust, but have moved mostly sideways (2.4 – 2.6 percent) this year.
- Professional forecasters (Philly Fed Survey) long-term PCE inflation expectation:
 - At 2 percent after briefly touching 2.1 percent.
- If steady expectations anchor inflation dynamics, then outlook is still for gradual rise toward FOMC's long-run goal.

Latest Dallas Fed model forecast shows trimmed mean inflation rising to 2 percent

4-quarter trimmed mean inflation



Summary

- Economy seems to have considerable forward momentum, which should lead to continued growth a bit above potential, as well as further reduction in slack in the labor market.
- Inflation has been low, but we expect this is transitory; a tightening labor market should eventually push inflation toward the Fed's longer-run goal of 2 percent in the medium term.

Questions?