The U.S. Economic Outlook

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Outlook themes

• Growth has rebounded following a soft Q1

• Labor markets continue to heal, as full employment is likely to be reached in 2015 and wage growth continues to edge higher

• Activity in the manufacturing and service sector is increasing

• Measures of inflation remain below the 2% goal, but are rising

• The euro and pound have fallen sharply against the US dollar
Growth has exceeded 3% in three of the last four quarters

Source: Bureau of Economic Analysis, Haver Analytics
The labor market is likely to reach full employment in 2015

Source: Bureau of Labor Statistics, Federal Reserve, Haver Analytics
The labor force participation rate has stabilized, but remains below its demographically-adjusted trend

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
Based on a wide set of indicators, labor markets are approaching more normal conditions.

Source: KC Fed Staff, Haver Analytics
The pace of improvement in the labor market is above average.

KC Fed Labor Market Conditions Indicator: Momentum

Source: KC Fed Staff, Haver Analytics
The wage cycle

Avg hourly earnings (production and nonsupervisory workers), y/y % chg

Number of unemployed people per job opening

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
Wage growth increased during the last expansion as the number of workers per job opening fell

Avg hourly earnings (production and nonsupervisory workers), y/y % chg

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
Wage growth slowed as the economy entered the Great Recession...

Avg hourly earnings (production and nonsupervisory workers), y/y % chg

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
...and declined further during the recovery

Avg hourly earnings (production and nonsupervisory workers), y/y % chg

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
Wage growth is well aligned with the last recovery and is likely to increase with further labor market improvement

Avg hourly earnings (production and nonsupervisory workers), y/y % chg

Source: Bureau of Labor Statistics, KC Fed Staff, Haver Analytics
Wage growth in a broader context also suggests further gains

Source: Bureau of Labor Statistics, Haver Analytics
Household debt as a share of income has declined substantially

Source: Federal Reserve Board, Haver Analytics
Household net worth has climbed with rising home and equity prices

Source: Federal Reserve Board, Haver Analytics
The service sector is expanding at its fastest pace in close to a decade

Source: ISM, Haver Analytics
Manufacturing is also increasing at a faster pace.

Source: ISM, Haver Analytics
Business fixed investment has recently moved higher

Private nonresidential fixed Investment: equipment, as a % of GDP

Source: Bureau of Economic Analysis, Haver Analytics
Spending on capital equipment appears poised to further increase

% of small firms planning capital expenditures in the next 3 to 6 Months

Source: NFIB, Haver Analytics
Economic policy uncertainty has declined notably

Source: Baker, Bloom and Davis, Haver Analytics
Housing construction remains a relatively low share of economic activity

Source: Bureau of Economic Analysis, Haver Analytics
House prices have increased over the past few years

Index, Jan 2000 = 100

Index, Jan 2000 = 100

Source: S&P / Case-Shiller, Haver Analytics
Export activity as improved, but is facing headwinds

ISM Manufacturing: New Export Orders Index (left)
Real Exports of Goods & Services (right)

Source: ISM, Bureau of Economic Analysis, Haver Analytics
The US Dollar has recently strengthened against major currencies

Source: Federal Reserve Board, Haver Analytics
Inflation is projected to return gradually towards 2%

Source: Bureau of Economic Analysis, Haver Analytics
The federal funds rate target remains near zero

Source: Federal Reserve Board, Haver Analytics
The Federal Reserve’s balance sheet continues to grow
FOMC Economic Projections

• 15 of 17 FOMC participants view short-term rates should rise in 2015 or sooner

• The midpoints of the FOMC projections have the economy back to full employment and inflation near target at the end of 2016

• The midpoint of the funds rate projection remains below its longer-run level at the end of 2016
Monetary Policy Normalization Principles and Plans

- The federal funds rate will remain the target, but new tools will be used to influence the funds rate
- Holdings of US Treasury and agency-MBS securities will be reduced in a “gradual and predictable” manner
- In the long-run, the FOMC plans on holding only the amount of securities necessary to “efficiently and effectively” implement policy