US Macro Overview
Presentation to the European Economics & Financial Centre
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Comments are those of the speaker and do not necessarily reflect the views of the Federal Reserve Bank of New York, the Federal Open Market Committee, or the Federal Reserve System.
Section 1: The Depth of the “Great Recession”

- The US economy has experienced six consecutive quarters of positive growth of real GDP, yet hours worked in the nonfarm business sector remain well below their level at the business cycle peak.
  - The unemployment rate has declined, but to a large extent this reflects the decline of the labor force participation rate.
  - Had the participation rate remained at its business cycle peak level, the unemployment rate would be about 10 ½%.
  - Core inflation has declined to a very low level, well below the Fed’s “mandate consistent” range; core inflation is an important indicator of trend inflation.
Nonfarm Business Sector: Hours Worked of all Persons
(Series Set to 1.0 at NBER Peak)

Source: Bureau of Labor Statistics
Personal Income Excluding Current Transfer Receipts Per Capita (Series Set to 1.0 at NBER Peak)

Source: Bureau of Economic Analysis
Unemployment and Labor Force Participation Rates

Source: Bureau of Labor Statistics
Total and Core CPI

% Change - Year to Year

Total CPI

Core CPI

Source: Bureau of Labor Statistics
Section 2: A Brightening Outlook

- A wide array of recent indicators suggest that the US economy entered 2011 with substantial forward momentum.
  - Real PCE grew 4.4% (AR) in 2010Q4, led by spending on durable goods.
    - The one-year, 2 percentage point payroll tax cut likely to give a significant boost to real PCE over the first half of 2011.
  - Real exports have grown rapidly of late, and growth prospects among our trading partners is promising.
  - Growth of business investment in equipment and software has been well maintained and is likely to get an added boost in 2011 from the “full expensing” provision enacted late last year.
  - Business investment in nonresidential structures is still declining but at a much reduced rate.
  - Inventories are in good balance with sales.
Real PCE, Disposable Income and Personal Saving Rate

% Change - Year to Year

Source: Bureau of Economic Analysis
Real Exports of Goods and Services

(Series Set to 1.00 at NBER Peak)

Source: Bureau of Economic Analysis
Nondefense Capital Goods Excluding Aircraft

% Change - Year to Year

New Orders

Shipments

Source: US Census Bureau
Private Nonresidential Construction over Various Horizons

% Change - Annual Rate

Source: US Census Bureau
Inventory/Sales Ratio: Total Business

Source: US Census Bureau
ISM Indices

Level

Note: Above 50 = Increasing

Source: Institute of Supply Management
Consumer Confidence

Index, 1985 = 100

Conference Board (left axis)

University of Michigan (right axis)

Source: Conference Board and University of Michigan
Confidence is increasing that conditions are now in place to support sustained above-potential growth, when it occurs.

- Aided by the second installment of Large Scale Asset Purchases (LSAPs), financial conditions have improved.
- The personal saving rate has risen to a level that is consistent with the historical relationship between that rate and household net worth relative to disposable income.
- The household financial obligation ratio has declined to the level that prevailed in the mid 1990s.
- Bank lending standards, while tight in level terms, have begun to ease.
- C&I loans on bank balance sheets and consumer credit (nonmortgage) have begun to expand.
S&P 500
Index, 1941-1943 = 100

Flash Crash

Jackson Hole

November 2nd FOMC

S&P 500 Index

Fiscal Compromise

Source: New York Times
Nominal Interest Rates

Source: Federal Reserve Board
Inflation Expectations

Percent

10-Year TIPS Breakeven

1.50
1.75
2.00
2.25
2.50
2.75
Jan-10 Apr-10 Jul-10 Oct-10 Jan-11 Apr-11

Flash Crash
Jackson Hole
November 2nd FOMC

Fiscal Compromise

Source: Federal Reserve Board
Real Interest Rates

Flash Crash
Jackson Hole
November 2^{nd} FOMC
Fiscal Compromise

10-Year TIPS

Source: Federal Reserve Board
Household Net Worth and the Saving Rate

Source: Federal Reserve Board and Bureau of Economic Analysis
Personal Saving Rate and Household Net Worth

[Graph showing the relationship between personal saving rate and household net worth.]

Source: Bureau of Economic Analysis and Federal Reserve Board

Note: Fitted line is from 1983Q1 to 2005Q4.
Household Financial Obligation Ratio

Source: Federal Reserve Board
Consumer Debt by Credit Score Quintile

Source: FRBNY Consumer Credit Panel
Banks Tightening Terms and Standards for Business Loans to Large and Mid-Sized Firms

Source: FRB Senior Loan Officer Opinion Survey
Section 4: Major Sectoral Challenges

- We still face painful structural adjustments in the housing and the government sectors that pose significant downside risks.
  - The excess inventory of vacant homes, particularly single-family units, remains substantial.
    - Still a large pipeline of loans in foreclosure and loans seriously delinquent.
    - Home prices have come under renewed downward pressure.
  - State and local governments have been cutting employment and will likely continue to do so over the year ahead.
  - Federal fiscal policy is widely acknowledged to be on an unsustainable path for the long term and must be addressed.
Excess Supply of Housing

Source: US Bureau of the Census; calculations by the Federal Reserve Bank of New York.

Note: Shading represents NBER recessions.
Housing Starts

Per 1,000 People

CA, AZ, NV, and FL
U.S. Total
U.S. Excluding Combined States

Source: U.S. Census Bureau
CoreLogic National Home Price Index

Includes Distressed Sales

Excludes Distressed Sales

Source: CoreLogic/Haver Analytics
90+ Day Mortgage Delinquencies and Foreclosures Started

Source: Mortgage Bankers Association of America
Real State and Local Government
(Series Set to 1.00 at NBER Peak)

Source: Bureau of Economic Analysis
Federal Debt Held by the Public as a Percent of GDP

Source: Congressional Budget Office
Section 5: Challenges for Monetary Policy

- While trend inflation is quite low at the moment, we see it likely to be near the low point of this cycle.
  - The rate of inflation for nonenergy services is beginning to increase, led by faster increases in apartment rents.
  - Firming of demand along with decline of the exchange value of the dollar should begin to put upward pressure on nonfood, nonenergy goods prices.

- However, underlying inflation fundamentals suggest relatively low trend inflation for some time:
  - A substantial amount of slack in the economy.
  - Relatively wide profit margins, and
  - Inflation expectations remain well anchored.

- Rising commodity prices are an indicator of strengthening demand around the globe.
  - Higher energy prices likely to boost overall inflation in the near term.
  - For the past 20+ years, we see little evidence of pass-through of higher commodity prices into underlying inflation.
CPI: Core Goods and Core Services Inflation

% Change – Year to Year

% Change – Year to Year

Core Services

Core Goods

Source: Bureau of Labor Statistics
Rental Market Conditions

% Change – 3-month AR

Above 50 = Tighter

Rent of Primary Residence (left axis)

Apartment Market Conditions (right axis)

Source: Bureau of Labor Statistics, NMHC
Implicit Price Deflator and Unit Labor Costs

8 Quarter % Change - Annualized

Source: Bureau of Labor Statistics
TIPS Implied Inflation: 2-3, 4-5, and 5-10 Year Horizons

Source: Federal Reserve Board

Note: Carry-adjusted.
Commodity Prices and Core CPI Inflation

% Change – Year to Year

Source: Commodity Research Bureau, Bureau of Labor Statistics

Correlation

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<thead>
<tr>
<th></th>
<th>Pre-1990</th>
<th>Post-1990</th>
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<tr>
<td>t + 12</td>
<td>0.47</td>
<td>-0.26</td>
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<tr>
<td>t + 24</td>
<td>0.38</td>
<td>-0.28</td>
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KR-CRB Index (Left Axis)
Core CPI (Right Axis)
Section 6: Market Expectations for Monetary Policy

- The last statement of the FOMC:
  - The Committee …continues to anticipate that economic conditions, including low rates of resource utilization, subdued inflation trends, and stable inflation expectations, are likely to warrant exceptionally low levels for the federal funds rate for an extended period.

- Current market expectations are that:
  - The Fed will purchase the full $600 billion of Treasury securities by mid 2011.
  - The Fed will begin to raise the federal funds rate in the second half of 2011.

- Policy conditional on the performance of the economy.
- U.S. economic conditions are currently quite far away from levels consistent with the Federal Reserve’s dual mandate.
Actual and Expected Fed Funds Target

Source: Federal Reserve Board
Federal Reserve Balance Sheet: Assets

Source: Federal Reserve Board