

Heading Towards Eleven Amidst Discord and Disruption

Bay Area Chamber of Commerce

December 14, 2018

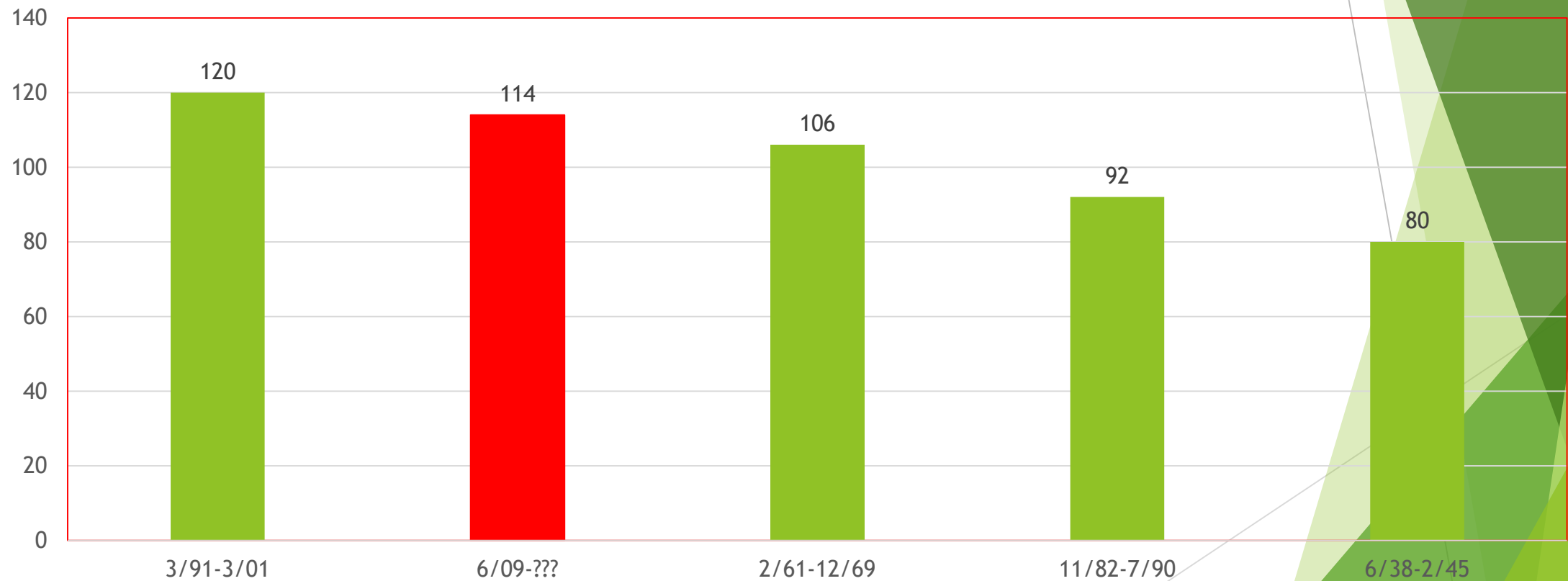
John W. Mitchell

December, 2018

- ▶ 114th Month
- ▶ Accelerated in Year 10
- ▶ Job Openings Greater than Unemployed
- ▶ Sears Bankruptcy-The Amazon of Another Time
- ▶ Trade Conflicts Reminiscent of 90 Years Ago
- ▶ Fed Targets Achieved
- ▶ Less than 4 Months from Brexit
- ▶ Divided Government
- ▶ A Shocked Generation-Rising Rates!

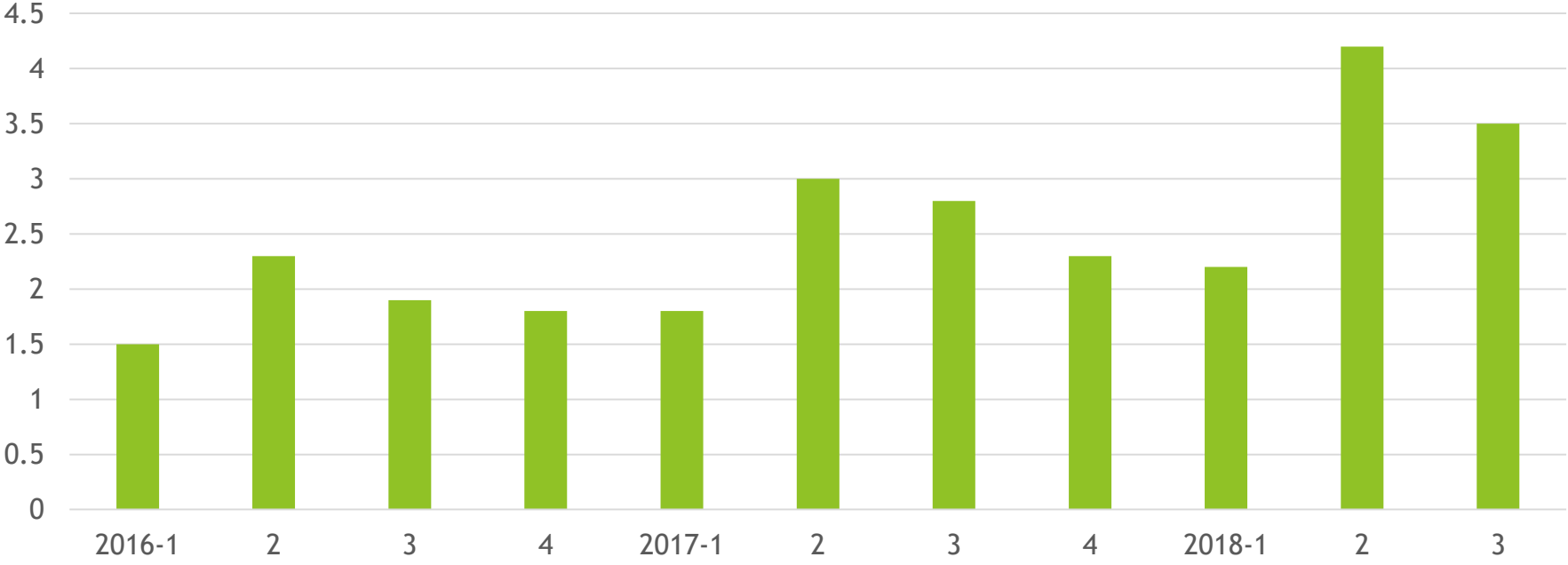
6 Months to Go Here for the Second Time

Source: NBER



Revised GDP Growth (SAAR) Trend Change or Aberration?

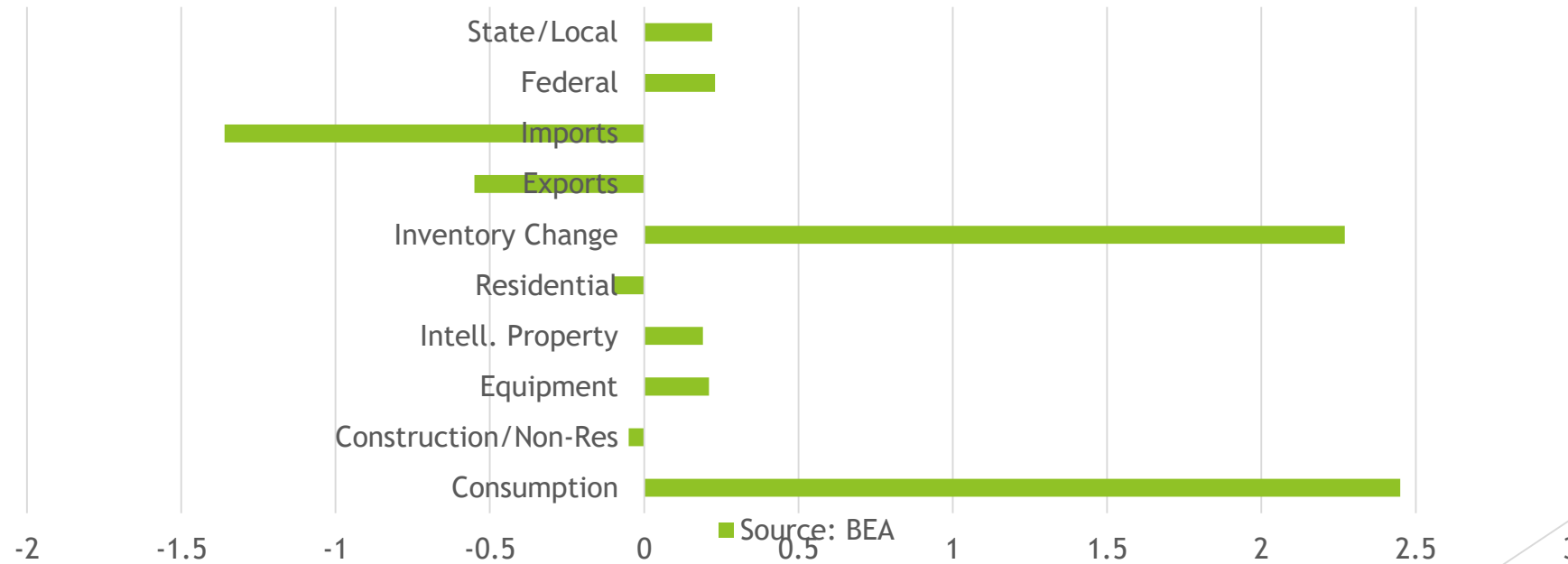
Source: BEA



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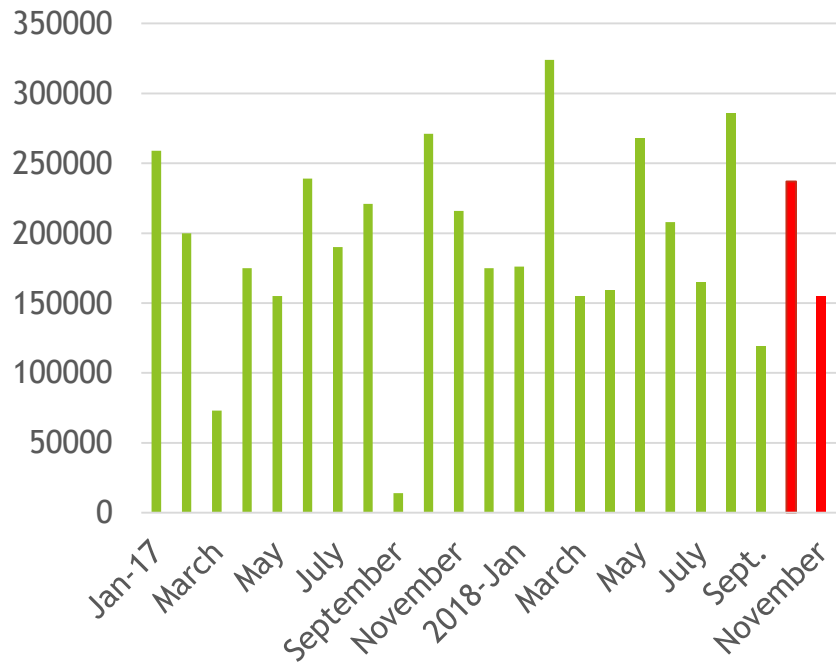
Percentage Point Contributions to Q3 GDP Growth

Source: BEA



Employment

Monthly Changes Payroll Employment 2017-2018 (BLS)



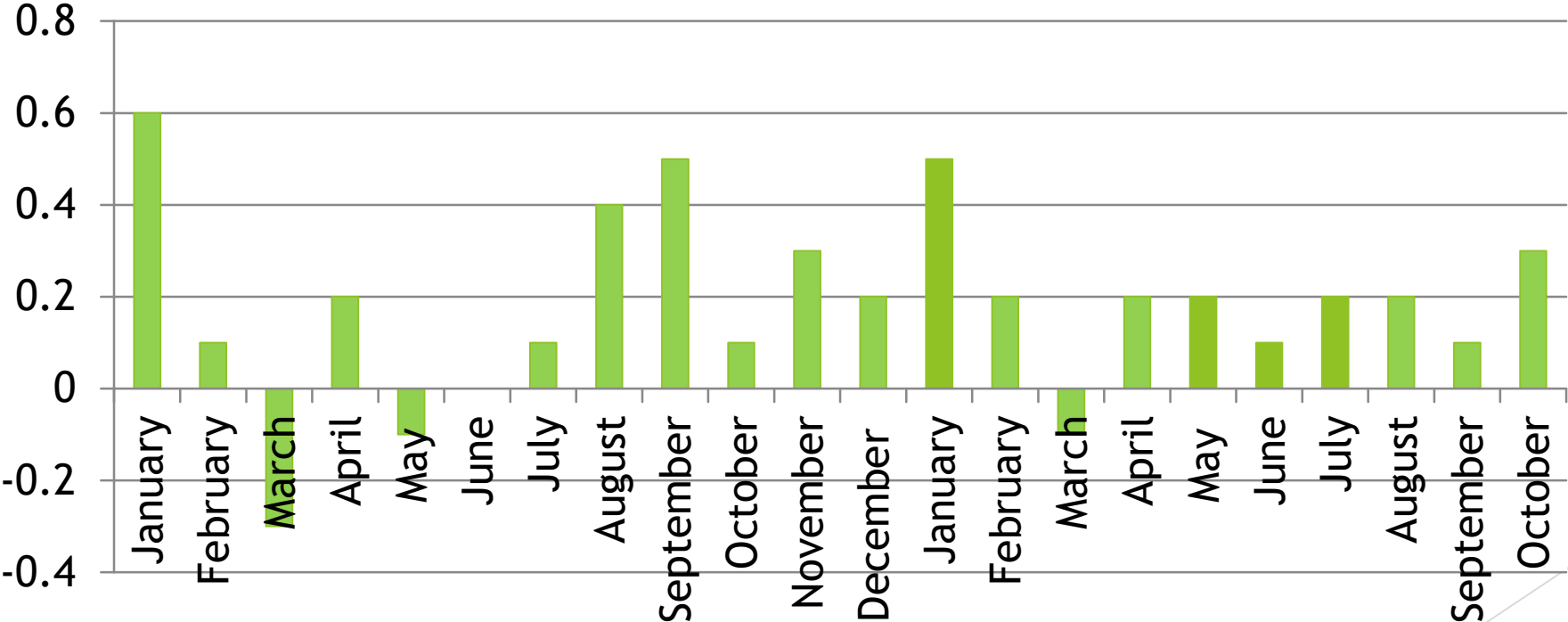
- ▶ 3.7% Unemployment Rate
- ▶ 20.17 Million Jobs Above Trough (2/10)
- ▶ Hourly Earnings up **3.1%**-Other Measures Faster
- ▶ Look Around-Signs-Self Service Motel
- ▶ Constraint on Activity
- ▶ 209,000 Jobs per Month Last Year

- ▶ Low Initial Claims-Have Been Near Half Century Lows
- ▶ Down Skilling-Felony Friendly, No Drug Tests, Opportunity
- ▶ Beige Book
- ▶ Recruitment and Retention
- ▶ Participation Rate 62.9% in November
- ▶ Gad Levanon-Conference Board- Blue Collar and Low Paid Services Wages rising faster than white collar- Declining Numbers
- ▶ Moving into a World of Slower Growth in the Labor Force
- ▶ Will the Response to the Tight Labor Market Boost Productivity?

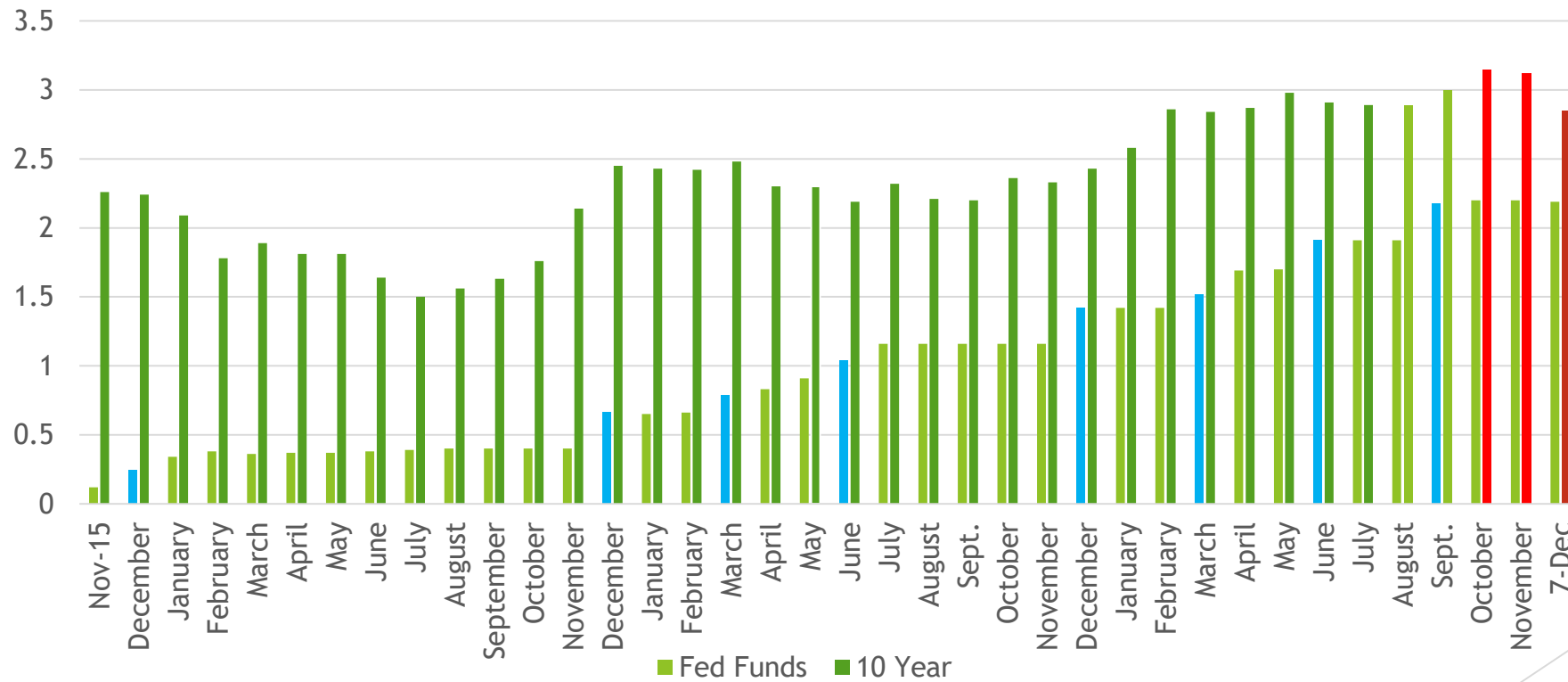
Monthly Change in the CPI 2017-18

Year over Year October 2.5% Total and 2.1% Core
PCE 2% and Core 1.8% October

Source: BLS



Removing the Punchbowl !



Thoughts From The Chairman

- ▶ Two Monetary Policy Questions (Jackson Hole Speech)
- ▶ “1. With the unemployment rate well below estimates of its longer term level, why isn’t the FOMC tightening monetary policy more sharply to head off overheating and inflation?
- ▶ 2. With no clear sign of an inflation problem, why is the FOMC tightening policy at all, at the risk of choking off job growth and continued expansion?”
- ▶ Possible Fed Errors-Moving Too Fast and Moving Too Slowly
- ▶ Brainard Principle- “when you are uncertain about the effects of actions move conservatively”
- ▶ Near Neutral and Not Predetermined Path

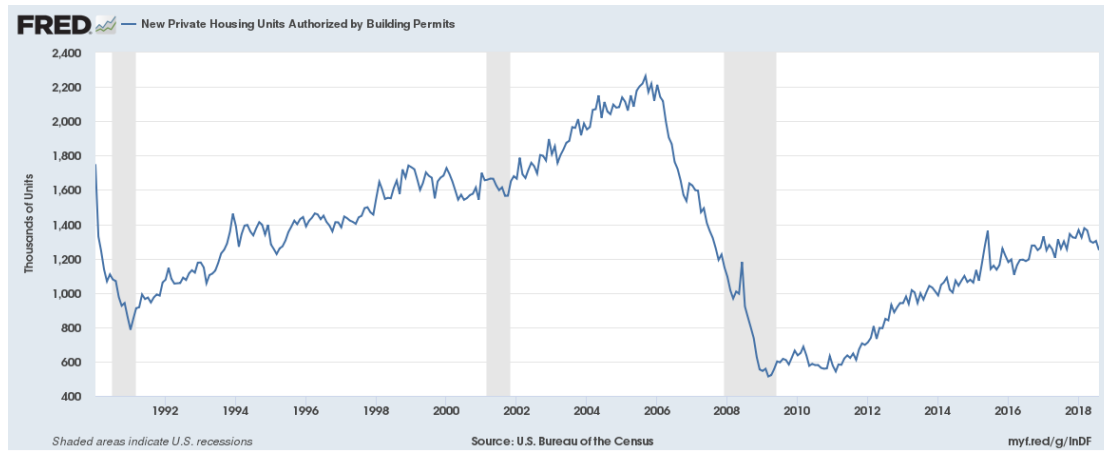
Monetary Policy

- ▶ Next Week-Then What?
- ▶ Central Banks Unwinding-Financial Asset Implications
- ▶ Normalization- Reducing the Balance Sheet Size Started at \$10 Billion A Month in October 2017-Now \$50 Billion - Gradually Increasing- Trillions to Go! This has not been done before!
- ▶ In the last Two Recession Rates were Cut by over 5 Percentage Points or more

OMG!



Restrained Advance



- ▶ Altered Financial Environment-Tighter Lending
- ▶ Capacity in the Industry-Immigration Policy, Left the Business
- ▶ Local Supply-Restrictions, Fees, NIMBY
- ▶ No Generation in Our Memory until the Millennials has seen Price Declines
- ▶ Affordability Declines-Rates, Rising Prices, Incomes
- ▶ Lock In
- ▶ Tax Law Changes-70% Do Not Itemize
- ▶ Lagging Household Formation

The Tax Cuts and Jobs Act and Bipartisan Budget Act of 2018 After Last Year's Gathering

- ▶ Primarily Business Tax Cut
- ▶ **Test**-Can the incentives boost the growth rate -Increase Capital Formation
-Offsetting Demographic Drag and Productivity Trend
- ▶ Expanded Standard Deduction, Child Credit, No Personal Exemption, \$10,000 SALT Limitation, Pass Through Income 20% Deduction, Some Simplification with less Itemizing

- ▶ Increased Spending in 2018 and 2019-Budget Act
- ▶ Opportunity Zone: Deferred Taxation and Step Up Incentives More if Hold For 10 Years- You Have One Here!
- ▶ None of Us have filed under the new system!

- ▶ Have We Disarmed for the Next Downturn?

CBO Budget Outlook

- ▶ Tax Cuts and Jobs Act, Bipartisan Budget Act of 2018 and Consolidated Appropriations Act of 2018- Reduced Revenues and Increased Outlays
- ▶ Faster Growth in 2018 and 2019-Over Time Increased Incentives to Work Save and Invest-Partially Offset by Larger Deficits
- ▶ Debt Held by Public by 2028 levels not seen since 1946

- ▶ Consequences
- ▶ Interest Spending
- ▶ Crowding Out-Less Private Investment-slower productivity and wage growth
- ▶ Less Flexibility to Use Tax and Spending Changes
- ▶ Deficit Increased to \$779 Billion or 3.9% of GDP Last Fiscal Year

Trade Excitement

- ▶ Since the End of the Second World War -Reaction to the Great Depression-
Pattern of Reduced Trade Barriers
- ▶ Series of Multilateral Trade Barrier Reductions
- ▶ GATT(1948-1994) followed by WTO (1995-)Adjudicate Disputes
- ▶ Nations have Interests They Try to Protect
- ▶ Currently Stepped Back from that Path of Barrier Reductions
- ▶ Unwinding Supply Chains and Long Term Relationships
- ▶ This is not the World We Grew Up In!

Economics Sidebar

- ▶ The US Dollar is a Reserve Currency—People and Nations want to Hold Dollar Assets
- ▶ National Income Accounts The Difference between exports and imports of goods and services is equal to the difference between a nations savings and investment and the difference between taxes and government spending.
- ▶ Deficits and Surpluses are Accounting Terms Not Moral Judgements
- ▶ When you import more goods and services than you export, you get to use more than you produce.

Issues

- ▶ Prices of Imports and Domestic Alternatives
- ▶ Where to Invest-Rules Change-or Just Wait
- ▶ Co-operation in Other Areas-Finance, North Korea, Climate Issues
- ▶ Gains from Trade Forgone
- ▶ Winners and Losers
- ▶ Assisting People Impacted by Change

Outlook

- ▶ 2018 GDP Growth Near 3% Slower Next Year 2.5-3%
 - ▶ Inflation 2-2.5%-Below Target Since 2012-Risks Upside
 - ▶ Rising Rates Probably 4 Increases in Funds Rate in 2018 and as Many as 3 in 2019 *Depending on Data*
 - ▶ Remember This will be Years 10 and 11!
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- ▶ What will the actors do?

The Region

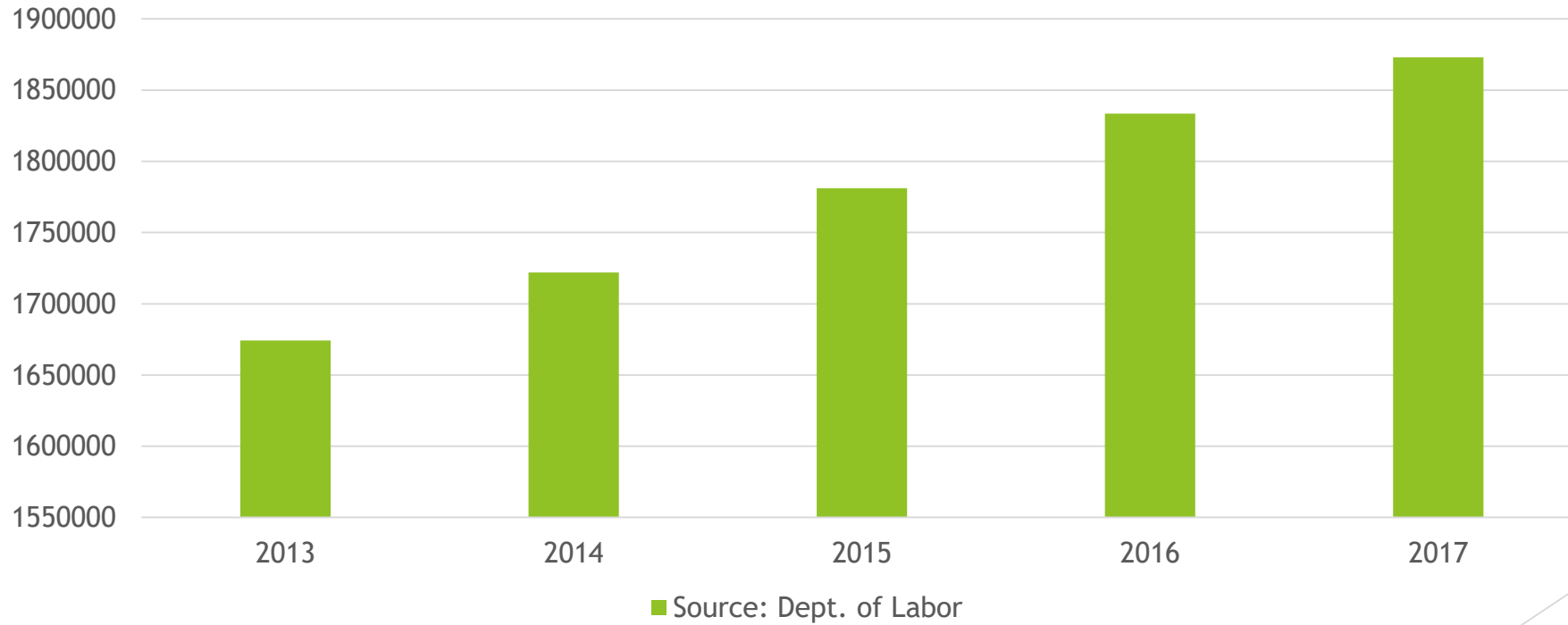
	Oct. Un. Rate %	Personal Income 2018 Q2	Populati on Growth % 2016- 17	Residential Permits to Oct.	House Price Index Q2 FHFA
Idaho	2.7	4.5%	2.2	16.4%	13.05%
Oregon	3.8	4.4%	1.4	-2.9%	7.92%
Washington	4.3	1.6%	1.7	.4%	10.99%

Job Growth Update October 2018 Data
Year over Year Change - 49 States Up
Source: BLS, ASU

- ▶ Nevada 1
- ▶ **Washington 2**
- ▶ Utah 3
- ▶ Texas 4
- ▶ Arizona 5
- ▶ New Mexico 6
- ▶ Florida 7
- ▶ Colorado 8
- ▶ **Oregon 9**
- ▶ New Hampshire 10
- ▶ North Carolina 11
- ▶ Wyoming 12
- ▶ Georgia 13
- ▶ Ohio 14
- ▶ **Idaho 15**
- ▶ Tennessee 16
- ▶ California 17
- ▶ South Carolina 18
- ▶ *South Dakota 19*
- ▶ Massachusetts 20
- ▶ Virginia 21
- ▶ Alabama 22
- ▶ New Jersey 23
- ▶ Hawaii 24
- ▶ Pennsylvania 25
- ▶ Missouri 26
- ▶ Montana 27
- ▶ Nebraska 28
- ▶ Maryland 29
- ▶ Iowa 30
- ▶ Oklahoma 31
- ▶ Kansas 32
- ▶ Michigan 33
- ▶ Rhode Island 34
- ▶ Connecticut 35
- ▶ North Dakota 36
- ▶ New York 37
- ▶ Minnesota 38
- ▶ Mississippi 39
- ▶ Delaware 40
- ▶ Maine 41
- ▶ Wisconsin 42
- ▶ West Virginia 43
- ▶ Illinois 44
- ▶ Indiana 45
- ▶ *Louisiana 46*
- ▶ *Arkansas 47*
- ▶ Kentucky 48
- ▶ Alaska 49
- ▶ Vermont 50

Oregon Annual Average Employment

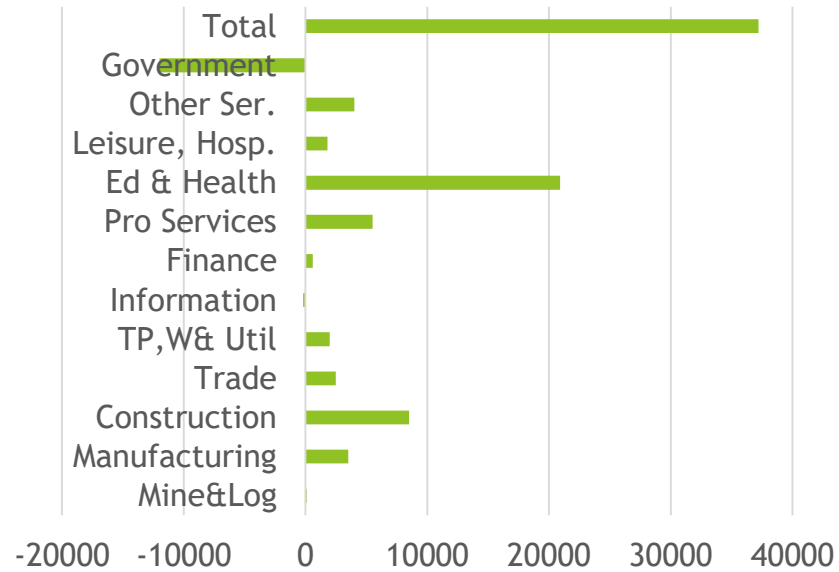
Source: Dept. of Labor



Oregon

October Employment 2.0% YoY

Source: Dept. Emp.



Metropolitan Areas

Source: BLS

	Growth	#
Albany	3.5%	1,600
Bend	4.5%	3,720
Corvallis	-.1	-40
Eugene	.4%	600
Grants Pass	3%	300
Medford	1%	860
Portland	2.2%	26,400
Salem	3.8%	6,400


Oregon Thoughts

- ▶ Still Sailing Along-Slower Population Growth PSU
- ▶ Fiscal Outlier
- ▶ PERS Problem-Squeeze on Other Spending
- ▶ Kicker Again in This Biennium-December Revenue Forecast-3.9% Above Forecast
- ▶ Rainy Day Fund and Education Stability Fund end of 2017-2019 9% of GF Revenues-after Paying Kicker
- ▶ Cap and Trade?

Cautiously Optimistic?

- ▶ Ever Since June of 2009-The Next Change in Direction is Going to be Down
- ▶ Do Upturns Die of Old Age- *No*- Other Nations have gone more Than a Quarter Century-Netherlands, Australia
- ▶ Look Around for Previous Signs
- ▶ Restrictive Policy Changes to Crush Inflationary Pressures-Late 60s or 70s
- ▶ Financial Crisis-Housing Collapse
- ▶ Oil Shock Redo? Different World-Oil Prices Leaped then Plummeted

- ▶ Balance Sheets Strong-Credit Quality Good
- ▶ Oregon Expected to Continue to Grow in 2019 but more Slowly-Testing the Limits-Consensus 2.3%
- ▶ **BUT**
- ▶ Minsky Moment-Stability Breeds Instability
- ▶ Recession Leftovers-Unwinding the Monetary Policies-The Shock of Higher Rates-It Depends on Your Age
- ▶ Fed Concerns Last Week's Financial Stability Report-High Yield Bonds and Leveraged Loans
- ▶ Trade Uncertainty
- ▶ Rest of World Weakness
- ▶ Q3 Investment Softness, Housing Plateauing?
- ▶ The October-November Financial Market Turmoil

- 
- ▶ Possible Political Shock-Election Results-Polarization
 - ▶ Unintended Consequences
 - ▶ Are We Missing Something ?
 - ▶ Remarkable Place: Achieve More Inclusive Prosperity-
Helping People Deal with Disruptions from Technology,
Trade, or Changing Tastes

- ▶ Greenspan and Wooldridge Book- *Capitalism in America*- Theme is Creative Destruction-New Stuff Replaces Old-new Technology, New Services-Source of Productivity and Prosperity
- ▶ *Start Ups, Mobility-Geographic and Social, Regulatory Constraints,*
- ▶ *Can it be Restored?*