U.S. Economic Outlook

October 4, 2017

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The views expressed herein are those of the presenter and do not necessarily represent those of the Federal Reserve Bank of Kansas City or the Federal Reserve System.
Outlook Themes

• Overall GDP growth is expected to continue at a modest pace, with investment making a relatively larger contribution over the medium-term.

• The labor market continues to tighten and unemployment is below most FOMC participants’ assessment of its longer-run natural level.

• Inflation remains below 2 percent target but is expected to increase over the medium-term.

• The FOMC will begin normalizing the Federal Reserve’s balance sheet in October.
GDP growth continues at modest pace, with business investment making a substantial contribution in 2017

Sources: Bureau of Economic Analysis, Haver Analytics
Consumption growth is expected to continue as wage growth picks up.

Sources: Bureau of Economic Analysis, Haver Analytics

The graph shows monthly payroll gains (L) and average hourly earnings (R) from May 2007 to May 2016. The y-axis represents the number in thousands (3mma) and the y/y % change in 3mma. The shaded area highlights a significant drop in both metrics from May 2007 to May 2010.
Durables consumption growth has been below levels seen in previous expansion periods

Sources: Bureau of Economic Analysis, Haver Analytics
Declines in vehicle sales held down consumption in recent months, particularly following Hurricanes.
Growth in business investment has been broad based

Sources: Bureau of Economic Analysis, Haver Analytics
The supply of single family housing remains constrained, but improvements and commissions support residential investment

Sources: Bureau of Economic Analysis, Haver Analytics
Unemployment has fallen substantially in recent years and is now below FOMC’s estimate of it long-run natural level.

Sources: Summary of Economic Projections, Bureau of Economic Analysis, Haver Analytics
Hurricanes may confound upcoming jobs report

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Sources: Bureau of Labor Statistics, National Weather Service
The Federal Reserve Bank of Kansas City’s LMCI shows the labor market remains healthy
Wages are growing modestly across all skill groups

Sources: Bureau of Labor Statistics, FRBKC
Inflation remains below 2 percent target

Sources: Bureau of Economic Analysis, Haver Analytics
Wireless services inflation has been particularly weak

Sources: Bureau of Economic Analysis, Haver Analytics
Many components of overall inflation are below 2016 levels

Sources: Bureau of Economic Analysis, Haver Analytics
Balance Sheet Themes

• The FOMC announced its plan to begin reducing the Fed balance sheet by decreasing reinvestments of maturing Treasury and agency securities.

• The balance sheet will not be the primary tool to conduct monetary policy.

• Normalization will likely not return the size of the balance sheet to pre-recession levels.

• Normalization of the balance sheet is expected to have only modest effects on long-term interest rates.
“Conventional” monetary policy was exhausted by 2008, but long-term interest rates remained well above zero.

Sources: Federal Home Loan Mortgage Corporation, Federal Reserve Board, NBER, Haver Analytics
The FOMC used “unconventional” balance sheet policy to put downward pressure on long-term interest rates

Sources: Federal Reserve Board, Haver Analytics
A cap on the runoff of Treasury securities ensures that the balance sheet will shrink at an even pace.
Mortgage-backed securities holdings could remain large even after reinvestments cease

Sources: Federal Reserve Board, Haver Analytics
Looking Forward

• Temporary factors holding down inflation are likely to dissipate in the medium term, moving inflation closer to the 2 percent target.

• Over the medium term, demographic factors may lead to important labor market dynamics that influence wage growth.

• Ongoing foreign growth will boost demand for U.S. exports.

• Changes to the Fed balance sheet are expected to have only modest effects on the real economy.