Macroeconomic Outlook:

Signs of Relief on the Horizon

Claudia Sahm

Sahm Consulting and Stay-At-Home Macro (SAHM) Substack

claudia.sahm@gmail.com

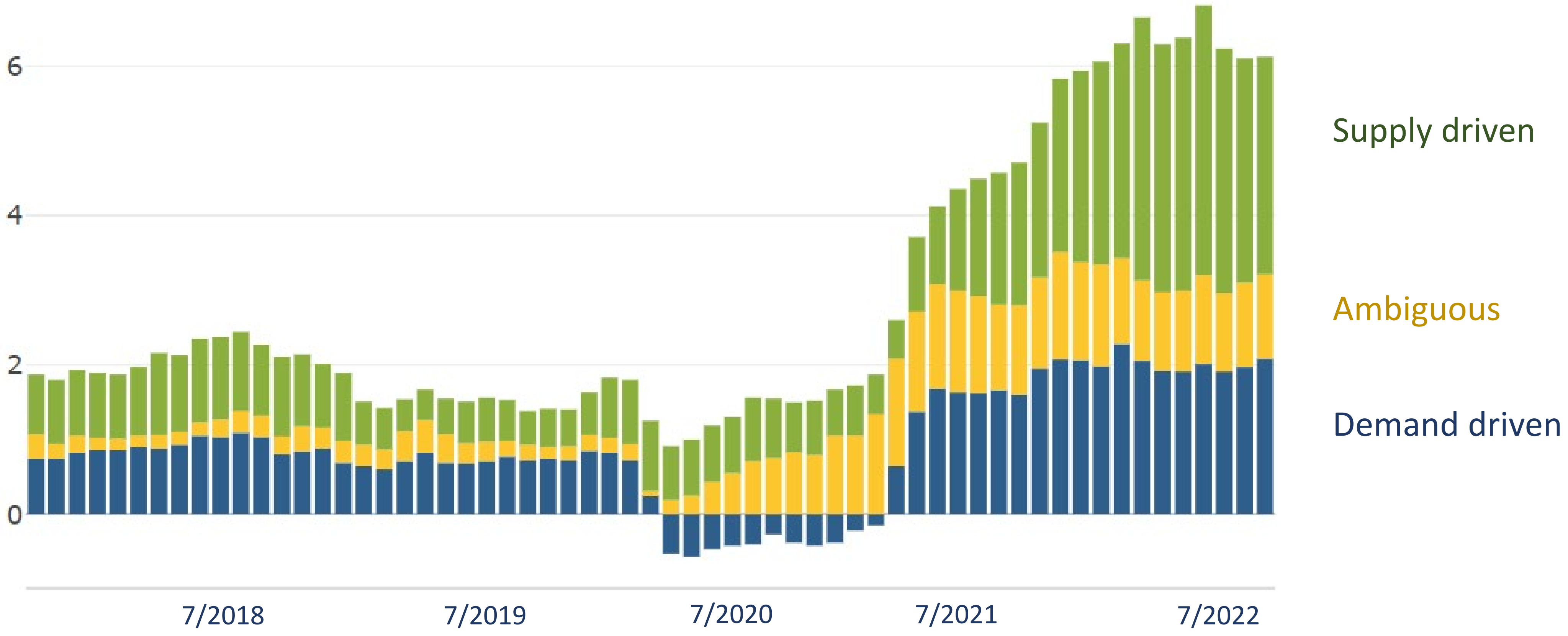
December 1, 2022

Key Takeaways

- Inflation has turned in the US and more relief coming from many sources.
- US is on track for "softish landing." Europe a recession. China no growth.
- Why optimistic on US? Solid labor market and consumer spending.
- Fed becoming increasingly aware of the numerous global risks.
- The Fed *is* slowing, but do *not* expect them to cut rates next year.
- Fiscal policy is key to sustainable, equitable growth going forward.

Covid and Putin led to supply-driven inflation

12-month percent change in total U.S. Personal Consumption Expenditures.

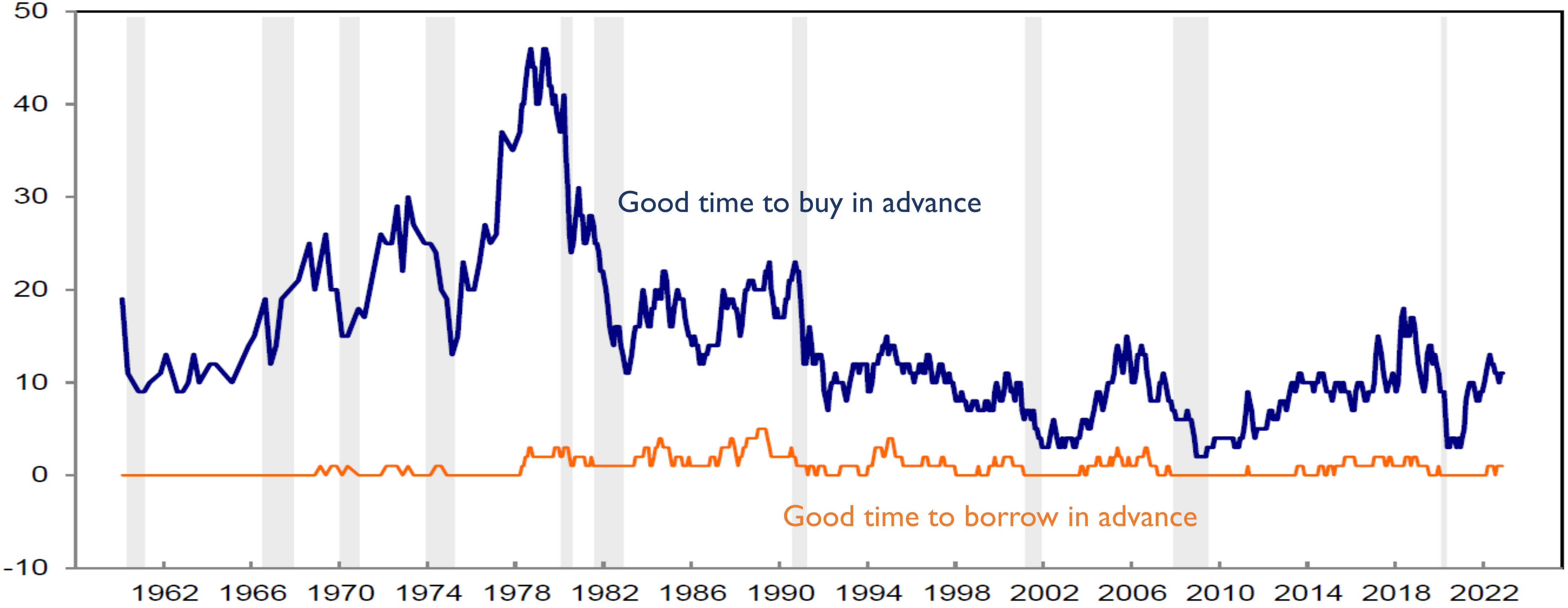


Source: Adam Shapiro, San Francisco Fed.

- Central banks cannot solve supply shortages; they will make them worse.
- The Phillips curve should *not* guide policy when supply shocks are key factor.

NO signs of an inflationary mentality

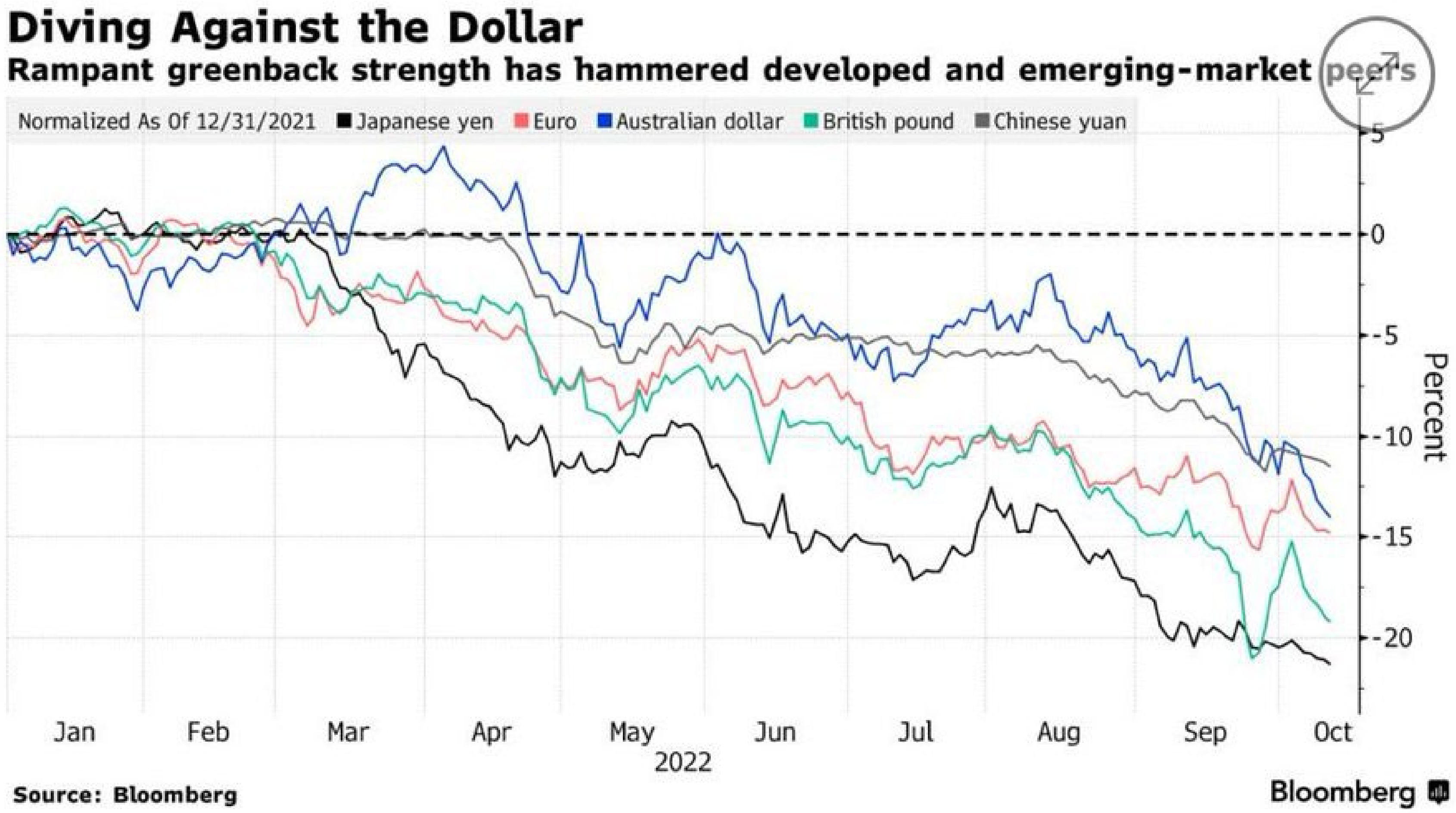
Percent among U.S. households who say it is a good time to buy large durable goods, by reason.



Source: Surveys of Consumers, University of Michigan, November 2022.

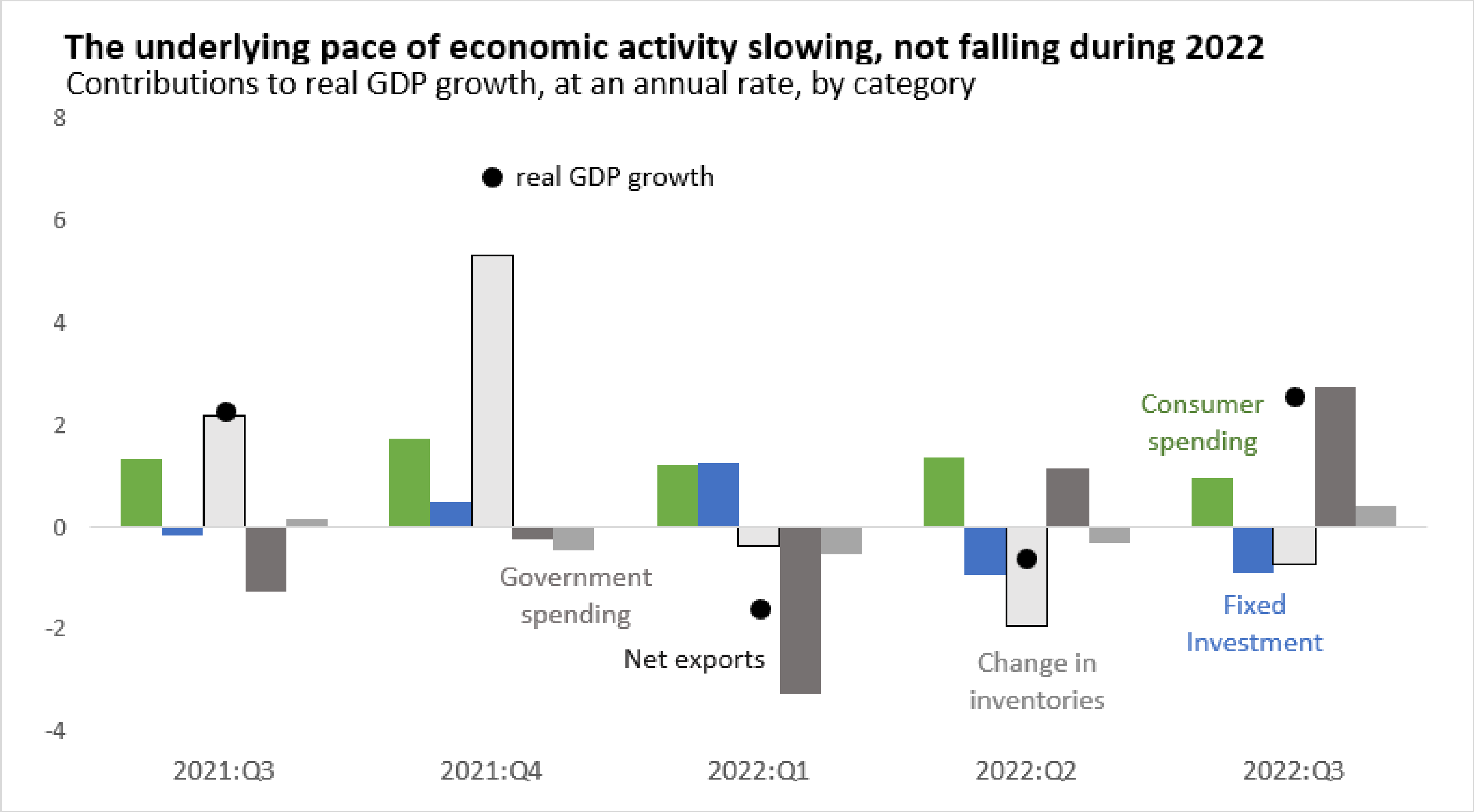
- Inflation expectations only matter if they *change behavior*. No signs!
- It is irresponsible to justify aggressive tightening on fears of de-anchoring.

The world paying (literally) for lower U.S. inflation



- Fed's rate increases strengthen the dollar and lower U.S. import prices, which is pushes down inflation in United States; the reverse is true abroad.

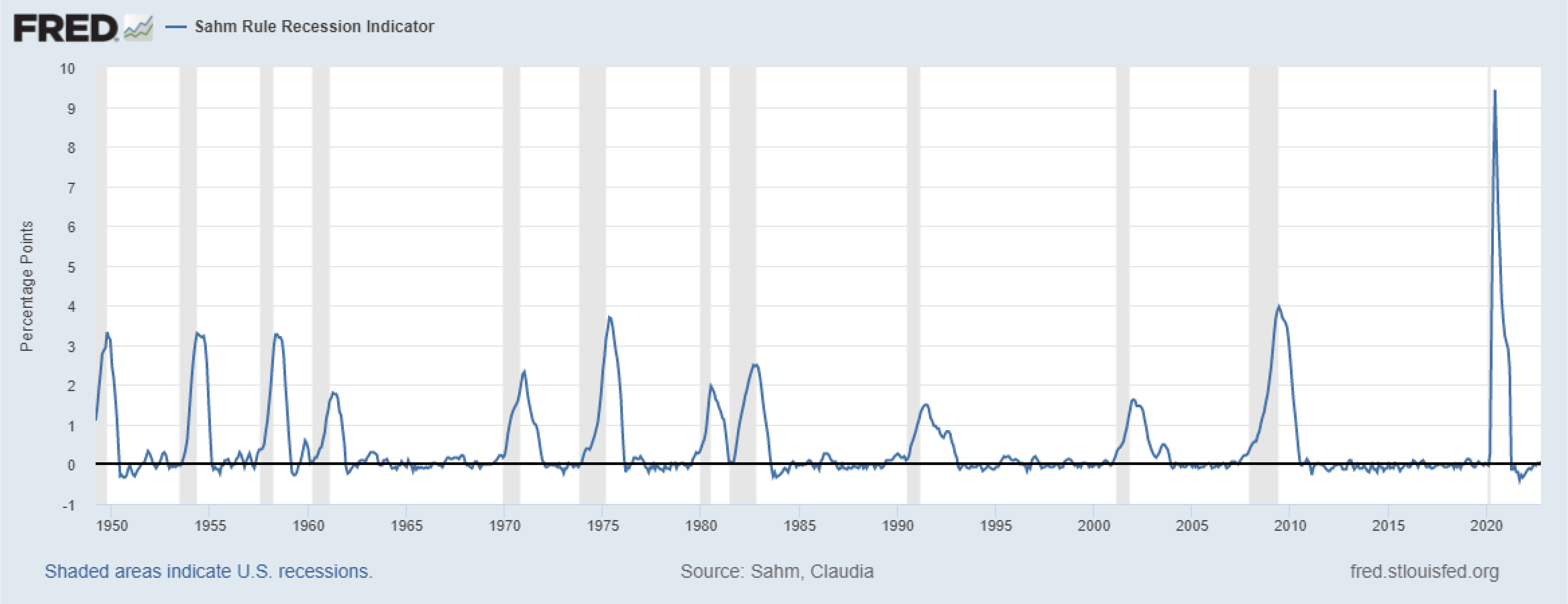
US is not in a recession, one is not inevitable



Source: Bureau of Economic Analysis. Chart by Claudia Sahm.

- GDP is nearly only indicator of a recession now. That is not enough.
- Even so, consumer spending is still growing at a solid pace.

Unemployment is *not* consistent with recession



- Sahm rule at or above 0.5 percentage point and we are in a recession.
- At 0.1 now, unemployment rate very low relative to prior 12 months.

Job postings remain very high, but below the peak

- Nearly two [openings] per unemployed, down from peak but twice pre-Covid.
- Trying to hire fewer workers as opposed to layoffs could cool labor market.

Fed has been stuck in the 1970s and is slowly waking up

- Fed doesn’t want to make the mistake of easing up too soon as in1980.
- The fast, aggressive rate hikes were risky, but the Fed is backing off some now.

Europe has *no* justification to hike, but they will

"**Current inflation [in Europe] is mostly driven by a strong increase in energy prices**. Another factor is the pandemic-related disruption to supply chains, which is making many products more expensive. We are also seeing food prices growing significantly around the world. **Our monetary policy has little impact on what is happening on global commodity markets ...**

The ECB has a clear mandate – price stability ... we are taking decisive steps to curb inflation and are making sure that it stabilises again at 2% in the medium term ...

A looming downturn would have a dampening effect on inflation ... However, the starting point of interest rates is very low, so **it is clear that we need to continue raising rates**."

– Isabel Schnabel, Executive Board, European Central Bank