

# *Osher Lifelong Learning Institute, Summer 2022*

## Contemporary Economic Policy

University of Wisconsin, Milwaukee  
July, 2022

Host: Jon Haveman, Ph.D.  
National Economic Education Delegation



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## National Economic Education Delegation

- **Vision**

- One day, the public discussion of policy issues will be grounded in an accurate perception of the underlying economic principles and data.

- **Mission**

- NEED unites the skills and knowledge of a vast network of professional economists to promote understanding of the economics of policy issues in the United States.

- **NEED Presentations**

- Are nonpartisan and intended to reflect the consensus of the economics profession.



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# Who Are We?

## • Honorary Board: 54 members

- 2 Fed Chairs: Janet Yellen, Ben Bernanke
- 6 Chairs Council of Economic Advisers
  - o Furman (D), Rosen (R), Bernanke (R), Yellen (D), Tyson (D), Goolsbee (D)
- 3 Nobel Prize Winners
  - o Akerlof, Smith, Maskin

## • Delegates: 651+ members

- At all levels of academia and some in government service
- All have a Ph.D. in economics
- Crowdsource slide decks
- Give presentations

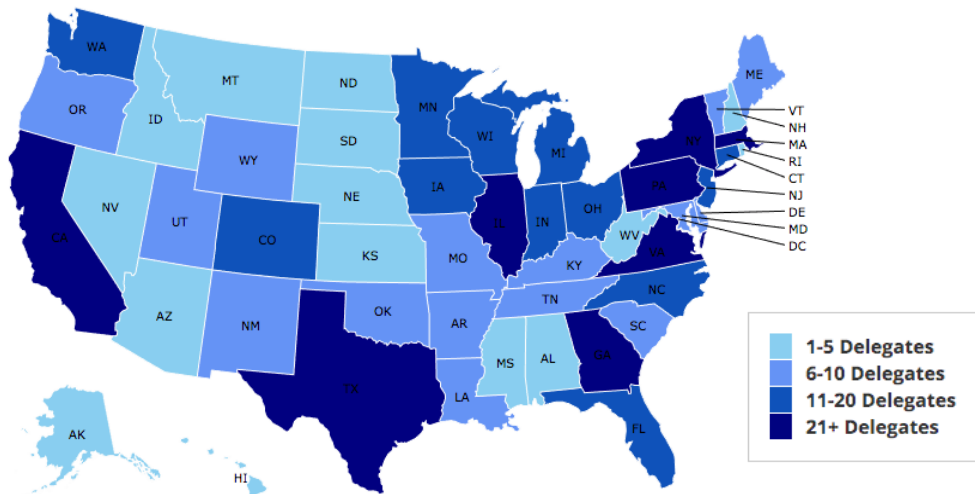
## • Global Partners: 49 Ph.D. Economists

- Aid in slide deck development



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# Where Are We?



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## Available NEED Topics Include:

- Healthcare Economics
- US Economy
- Climate Change
- Economic Inequality
- Economic Mobility
- Trade and Globalization
- Minimum Wages
- Immigration Economics
- Housing Policy
- Federal Budgets
- Federal Debt
- Black-White Wealth Gap
- Autonomous Vehicles
- US Social Policy



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## Course Outline

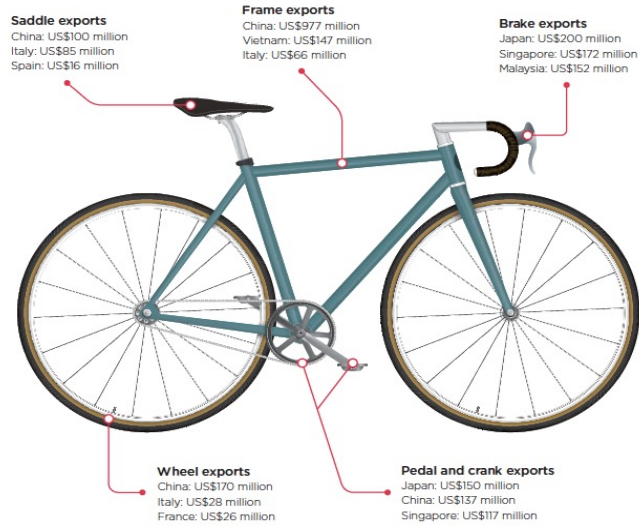
- **Contemporary Economic Policy**
  - Week 1 (7/14): Economic Update (Geoffrey Woglom, Amherst College)
  - Week 2 (7/21): Trade and Globalization (Alan Deardorff, University of Michigan)
  - Week 3 (7/28): Climate Change Economics (Sarah Jacobson, Williams College)



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# Trade: Bicycle Supply Chain

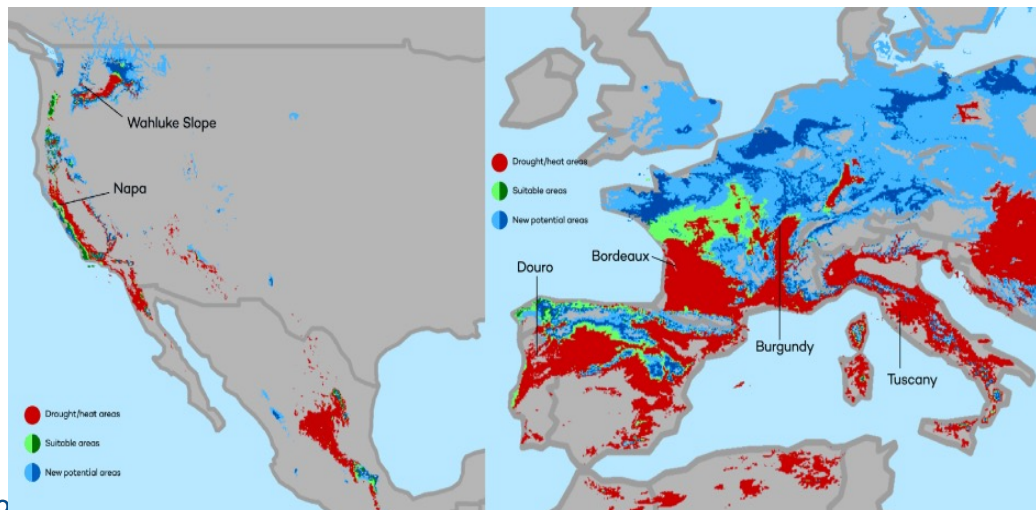
Figure 1.1 Where do bicycles come from?



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# Climate Change Economics

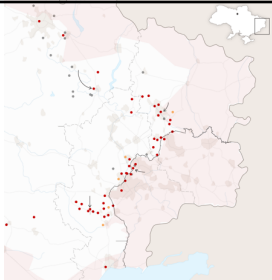
The changing map of the world's wine-growing regions.



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# Submitting Questions

- **Please submit questions of clarification in the chat.**
  - I will try to handle them as they come up.
- **We will do a verbal Q&A once the material has been presented.**
- **OLLI allowing, we can stay beyond the end of class to have further discussion.**
- **Slides will be available from the NEED website tomorrow ([https://needelegation.org/delivered\\_presentations.php](https://needelegation.org/delivered_presentations.php))**



# US Economy: Update

**Geoffrey Woglom, Ph.D.**  
 Amherst College, emeritus  
 July 8, 2022



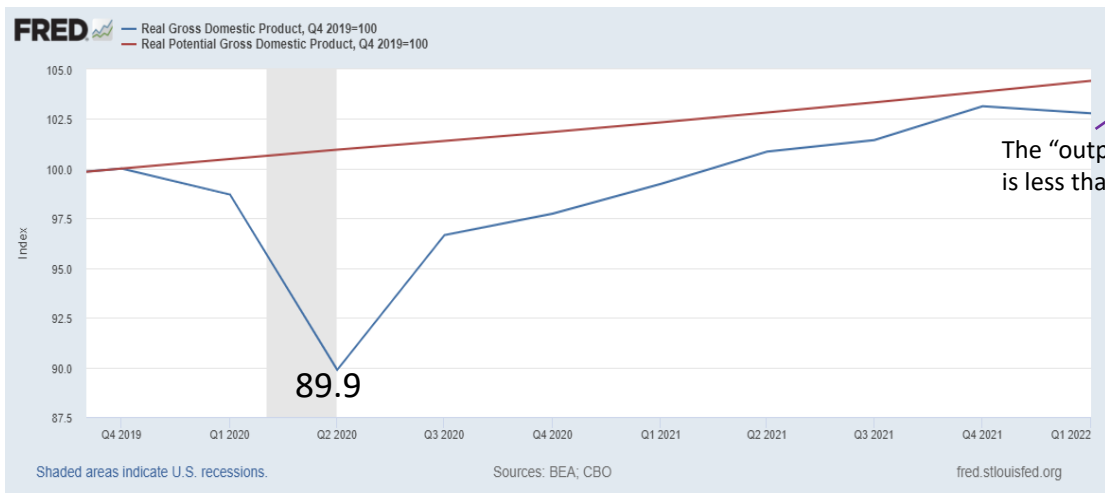
## Outline for the Talk

1. Quick summary of the state of the economy.
2. Closer look at inflation and whose to blame (in my opinion).
3. Current confusion on the state of the economy.
4. What's at stake in controlling inflation.
5. Brief thoughts on the effects of the Ukraine crisis. (if there is time)



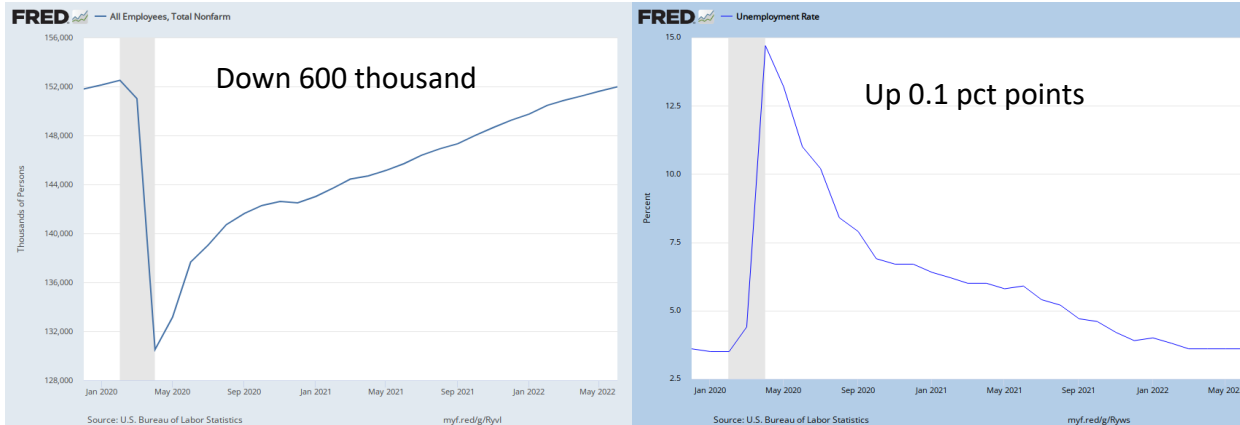
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## Real GDP and 'Potential' during the Recovery



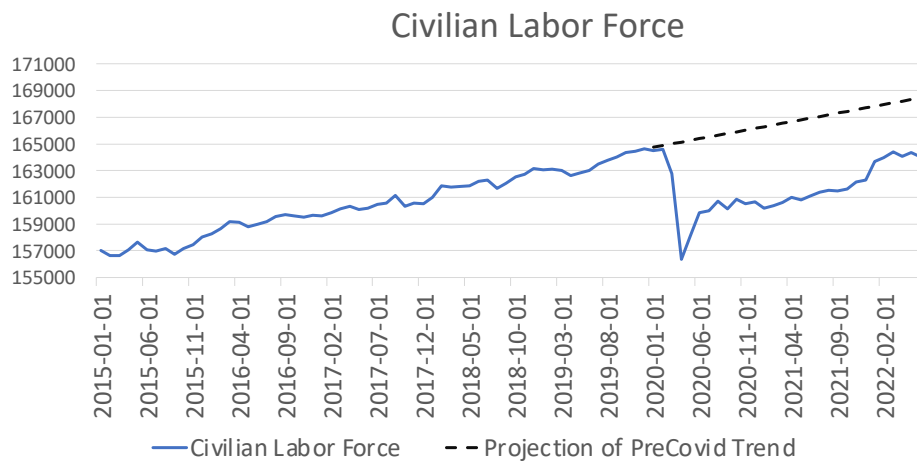
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# Labor Market is Almost Fully Recovered



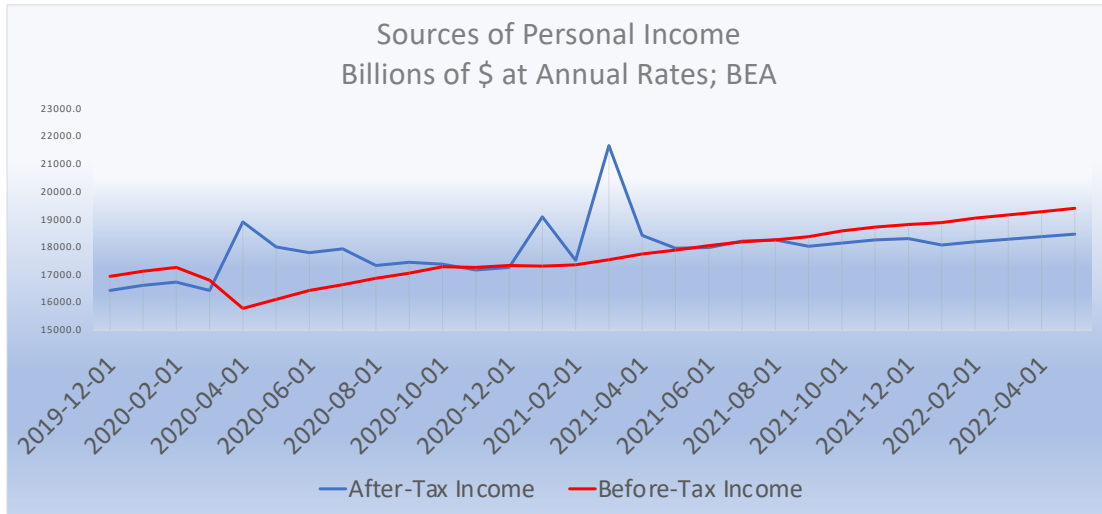
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# Where Have all the Workers Gone?



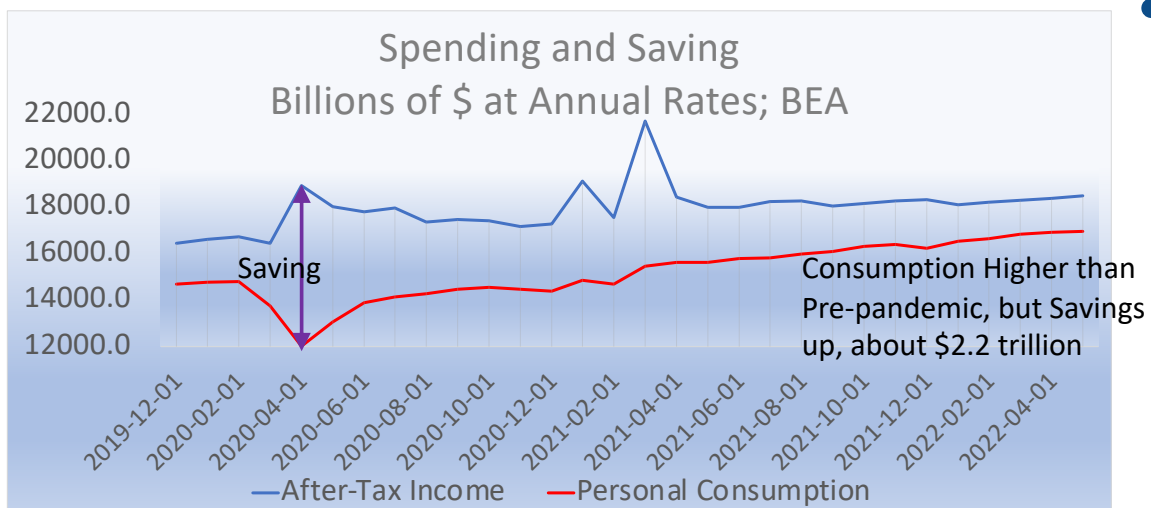
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## Fiscally Driven Recovery



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## Households Lead the Way



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# K-Shaped Recovery

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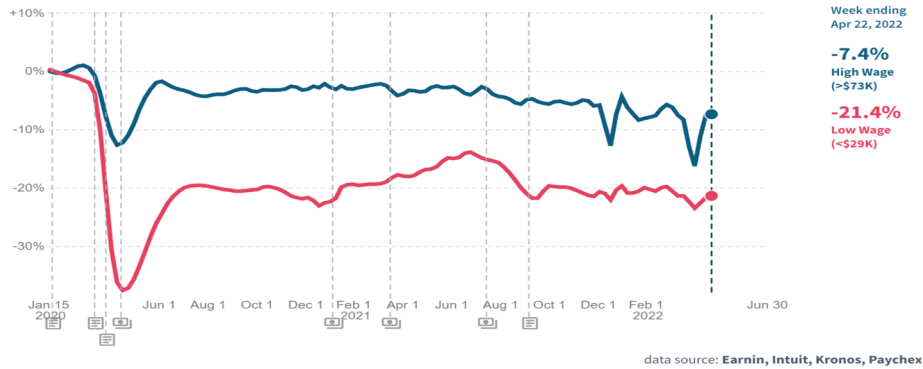
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## Percent Change in Employment\*

In the United States, as of April 22 2022, employment rates among workers in the top wage quartile decreased by 7.4% compared to January 2020 (not seasonally adjusted).



\*Change in employment rates (not seasonally adjusted), indexed to January 4-31, 2020. This series is based on payroll data from Paychex and Intuit, worker-level data on employment and earnings from Earnin, and timesheet data from Kronos. The dotted line is a prediction of employment rates based on Kronos and Paychex data.  
last updated: June 17, 2022 next update expected: July 01, 2022

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# Stimulus Payments Saved Low Wage Workers

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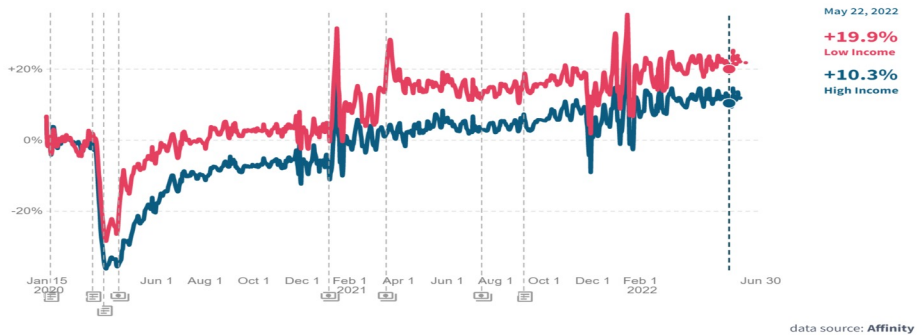
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## Percent Change in All Consumer Spending\*

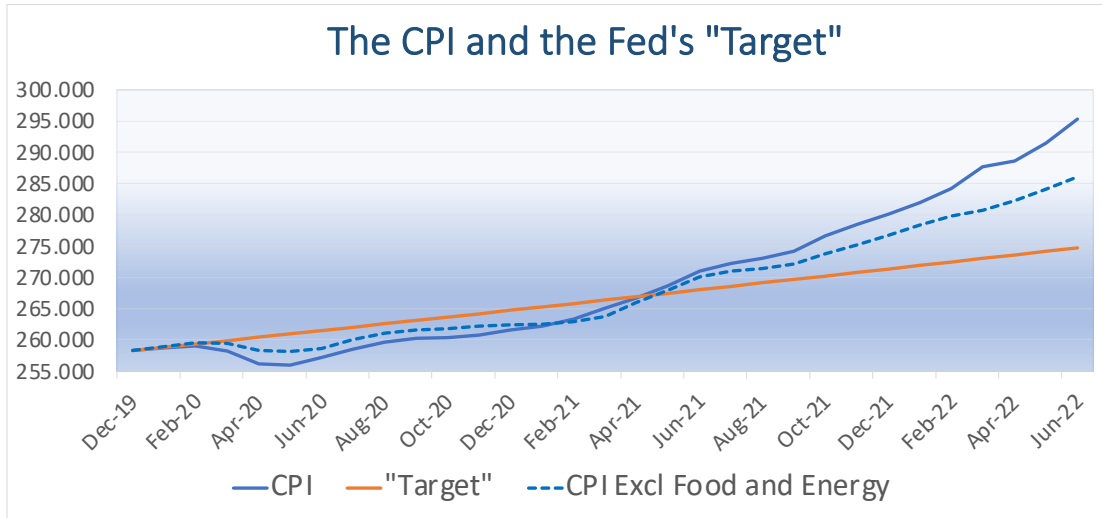
In the United States, as of May 22 2022, total spending by high-income consumers increased by 10.3% compared to January 2020.



\*Change in average consumer credit and debit card spending, indexed to January 4-31, 2020 and seasonally adjusted. The dashed segment of the line is provisional data, which may be subject to non-negligible revisions as newer data is posted. This series is based on data from Affinity Solutions.  
last updated: June 21, 2022 next update expected: July 01, 2022

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## Inflation during the Recovery



## Stabilizer in Chief: the Fed



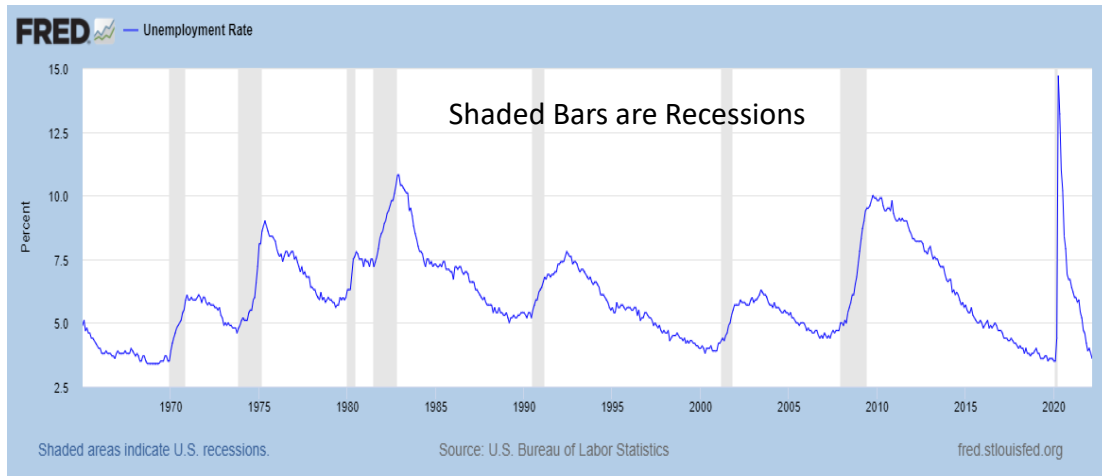
Jerome Powell  
February 2018

- **The Fed's Dual Mandate:**

1. "Stable prices" which means 2% rate of inflation in the Personal Consumption Price Index (which corresponds to about 2.5% inflation in the more well-known CPI).
2. "Maximum employment" which means the highest level of employment (lowest unemployment rate) consistent with mandate 1.

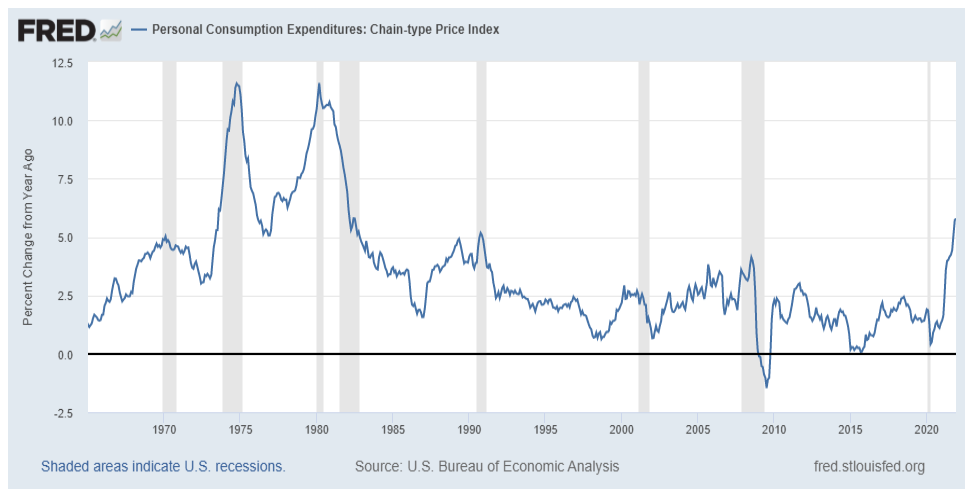
- **Fiscal Policy (taxes and spending, President and the Congress) can affect inflation and unemployment, but it is the Fed's job to achieve the dual mandate**

# Track Record on Unemployment



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# Track Record on “Price Stability”



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## Determinants of Unemployment & Inflation

- **Unemployment:** The higher the level of total spending, the lower the unemployment rate.
- **Inflation:**
  1. Too much spending and inflation rises (Vietnam).
  2. Increase in production costs (e.g., “supply chain bottlenecks.”)
  3. Expectations of high inflation can cause inflation to be high.

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## The Fed's Affects the Economy via Interest Rates

- **Higher Interest rates discourage firms from buying new plant and equipment, households from buying new homes and tend to lower stock and house prices (!).**
- **Reduced spending tends to lower production and employment and eventually lowers inflation.**

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## Become a Central Banker in One Slide!

- If you are more concerned that inflation is too high, raise interest rates.
- If you are more concerned that unemployment is too high, lower interest rates.
- Inflation and unemployment just right: keep rates the same.



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## One Big Complication: Lags

- Milton Friedman: Monetary Policy affects GDP and Inflation with Long and Variable (Unpredictable) Lags.
- Raising interest rates today does nothing to spending today nor to inflation.
- But over time spending slows and eventually inflation falls.
- Friedman believed that lags led to the Fed to “oversteering” the economy consistently.



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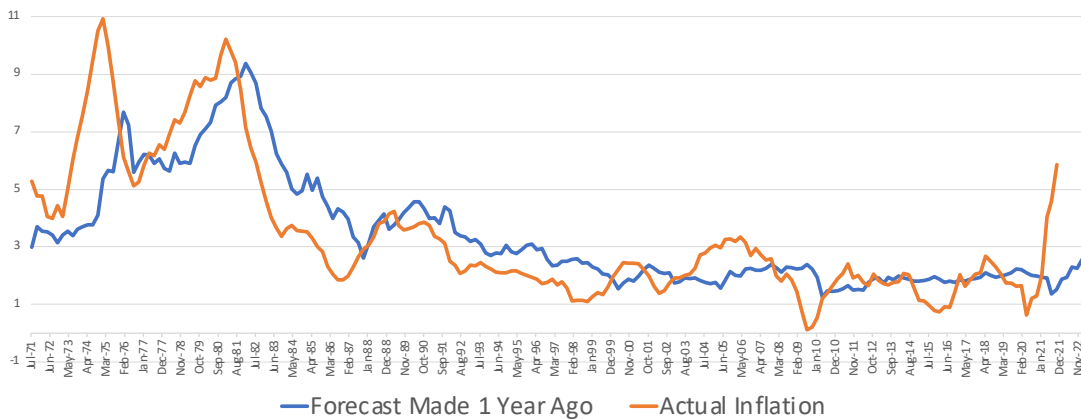
# The Great Moderation

- From 1990 until 2008, the performance of the US economy was extraordinary and even Milton Friedman gave kudos to the Alan Greenspan.
- We (economist) thought we knew why: Central Bankers finally listened to us on the importance of stabilizing inflationary **expectations**, starting with Paul Volcker.
- Volcker was determined to reduce inflationary expectations.

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# “Anchoring” Inflation Expectations

Expectations and Subsequent Inflation



Forecasts: Philadelphia Fed, “Survey of Professional Forecasters”

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## But, this Inflation is Different!

12-month, percentage price increase, selected items in the CPI			
Category:	Weight in CPI, 2022	December 1981	June 2022
All Items	100%	8.9	9.1
Services	60.1	13.0	6.2
Commodities	40.0	6.0	13.6
Housing	41.9	10.2	7.3
Transportation	18.9	11.0	19.7
Food	14.3	4.3	13.4
Medical Care	8.4	12.5	4.5
Energy	8.3	11.9	41.6
New Cars	4.0	6.8	11.4

Sources: BLS and Fred data from the St Louis Federal Reserve Bank



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## My Diagnosis for the Uptick in Inflation

- Yes, there were supply chain issues that affected some areas in particular (e.g., computer chips).
- But there is too much total spending and in the absence of bold Fed actions is likely to continue.
- Fiscal stimulus led households to increase saving over 2021 by more than \$2 trillion and today's strong retail sales numbers suggest they are prepared to spend it.
- Whose to Blame: ARP probably too big, but the Fed could have acted sooner.



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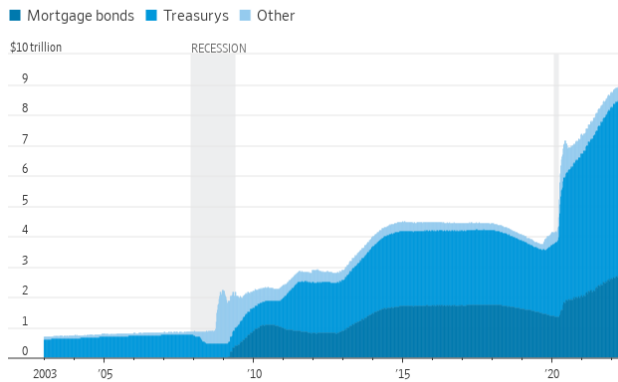
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# Fed Policy during the Recovery

- Zero interest rates until March and a Big QE program

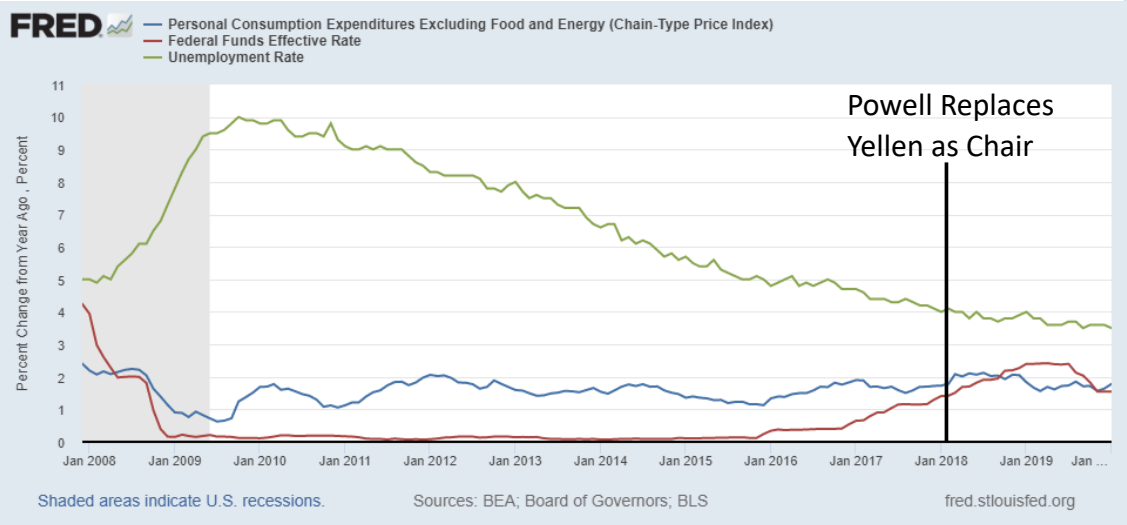
### Bond Binge

The Federal Reserve's asset holdings have more than doubled since March 2020



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# Why Did Powell Do It?



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## Policy Changes under Powell

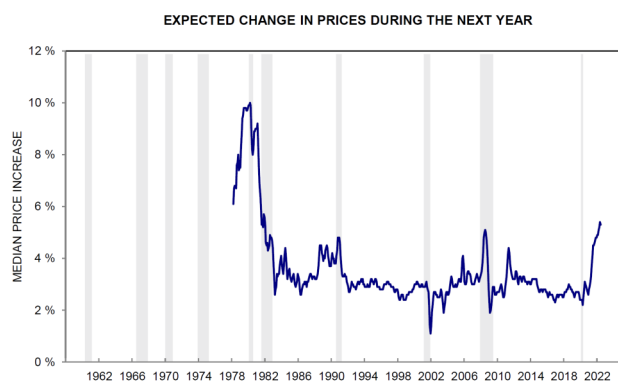
- In the Fed's dual mandate put more emphasis on the employment goal relative to the inflation goal.
- Inflation goal switched from targeting forecasted *future* inflation to trying to achieve average *realized* inflation of 2%

Have they forgotten about Lags!

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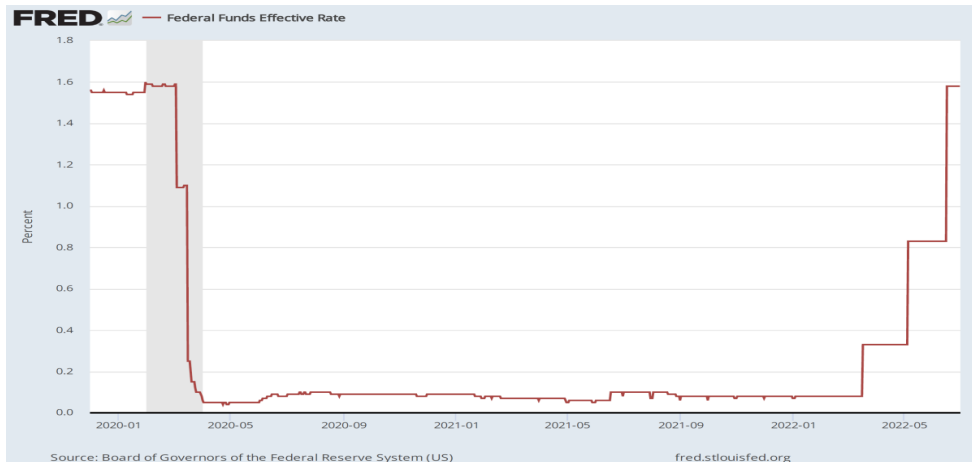
## But, Boy Have Things Changed!

- Powell's Wakeup Moment



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## Three Increases in 3 Meetings



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## Reality sets in at the FOMC, June Meeting

Percent

Variable	Median <sup>1</sup>			
	2022	2023	2024	Longer run
Change in real GDP	1.7	1.7	1.9	1.8
March projection	2.8	2.2	2.0	1.8
Unemployment rate	3.7	3.9	4.1	4.0
March projection	3.5	3.5	3.6	4.0
PCE inflation	5.2	2.6	2.2	2.0
March projection	4.3	2.7	2.3	2.0
Core PCE inflation <sup>4</sup>	4.3	2.7	2.3	
March projection	4.1	2.6	2.3	
Memo: Projected appropriate policy path				
Federal funds rate	3.4	3.8	3.4	2.5
March projection	1.9	2.8	2.8	2.4

Good Luck with these Forecasts!

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## FOMC Minutes from June Meeting

Members judged that, with high and widespread inflation pressures and some measures of longer-term inflation expectations moving up somewhat, it would be appropriate for the postmeeting statement to note that the Committee was strongly committed to returning inflation to its 2 percent objective. As the further firming in the policy stance would likely result in some slowing in economic growth and tempering in labor market conditions, members also agreed to remove the previous statement language that had indicated an expectation that appropriate policy would result in a return of inflation to 2 percent and a strong labor market.



## And, There is More!

In discussing potential policy actions at upcoming meetings, participants continued to anticipate that ongoing increases in the target range for the federal funds rate would be appropriate to achieve the Committee's objectives. In particular, participants judged that an increase of 50 or 75 basis points would likely be appropriate at the next meeting. Participants concurred that the economic outlook warranted moving to a restrictive stance of policy, and they recognized the possibility that an even more restrictive stance could be appropriate if elevated inflation pressures were to persist.



## More Reality on Wall Street Too

WSJ, SURVEY OF PROFESSIONAL FORECASTERS, JUNE (MEDIANS)		
	2022	2023
<b>CHANGE IN REAL GDP</b>	1.3	1.4
APRIL	2.6	2.4
<b>UNEMPLOYMENT</b>	3.7	4.2
APRIL	3.4	3.6
<b>INFLATION (CPI)</b>	7.0	3.3
APRIL	4.8	2.8
<b>FEDERAL FUNDS RATE</b>	3.3	3.5
APRIL	2.0	2.7

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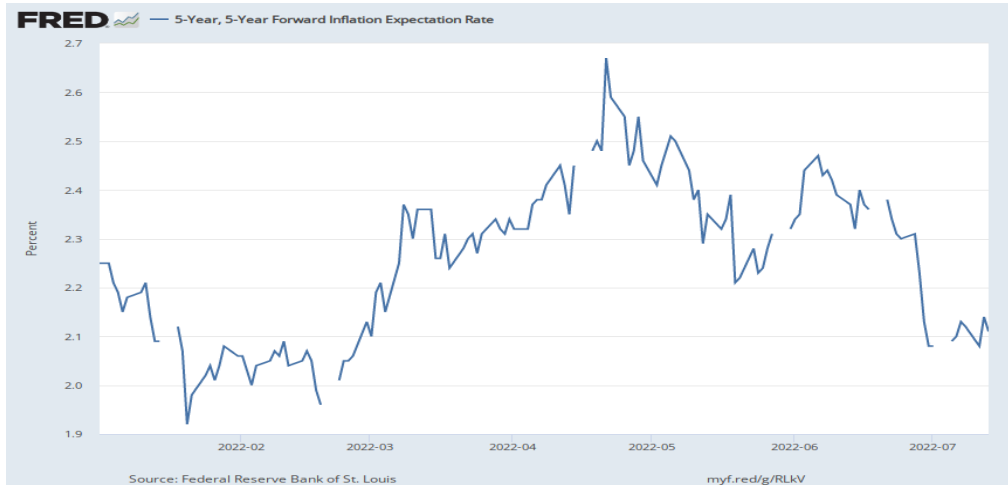
## Fed and Wall Street Forecasters are Similar

- **By 2023, inflation will come down substantially.**
- **The federal funds rate will stay below 4 percent.**
- **Unemployment will rise less than 0.5 percentage points.**

**I don't get it. This scenario only works if most of inflation is due to supply issues and expectations of inflation are "well anchored," so that the Fed achieves a "soft landing."**

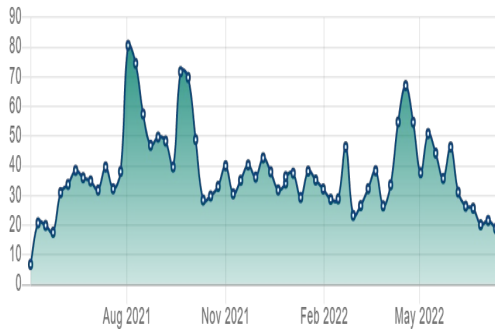
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# Financial Markets on the Expectations Story

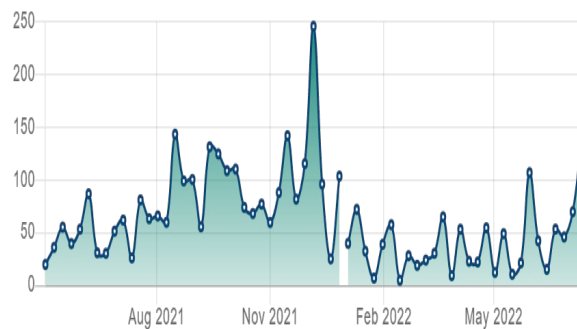


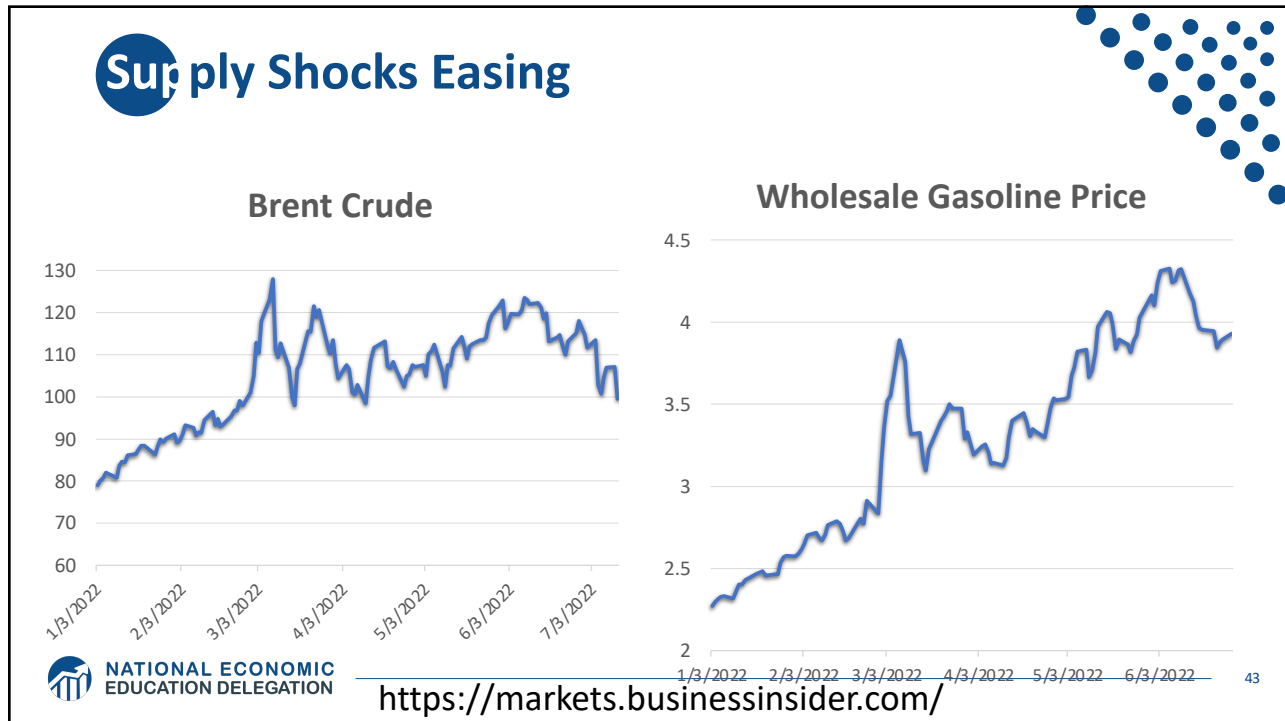
# Port Delays are Getting Back to Normal

## Shanghai

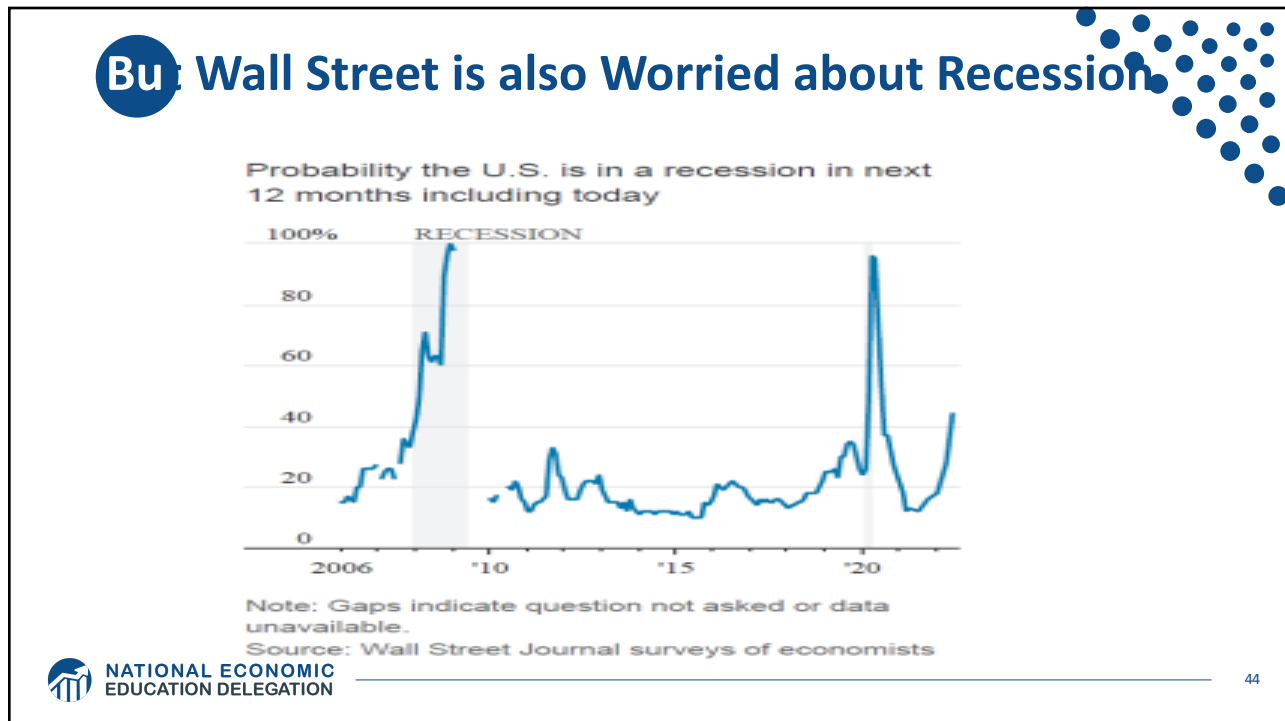


## Long Beach





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## First, What is a Recession?

- Defined by the National Bureau of Economic Research (NBER)
- “The NBER's definition emphasizes that a recession involves a significant decline in economic activity that is spread across the economy and lasts more than a few months.”
- Popular Rule of Thumb: Two or more, consecutive quarters where Real GDP falls.
- Recessions are caused by decreases in total spending.



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## Real GDP Growth and Recessions

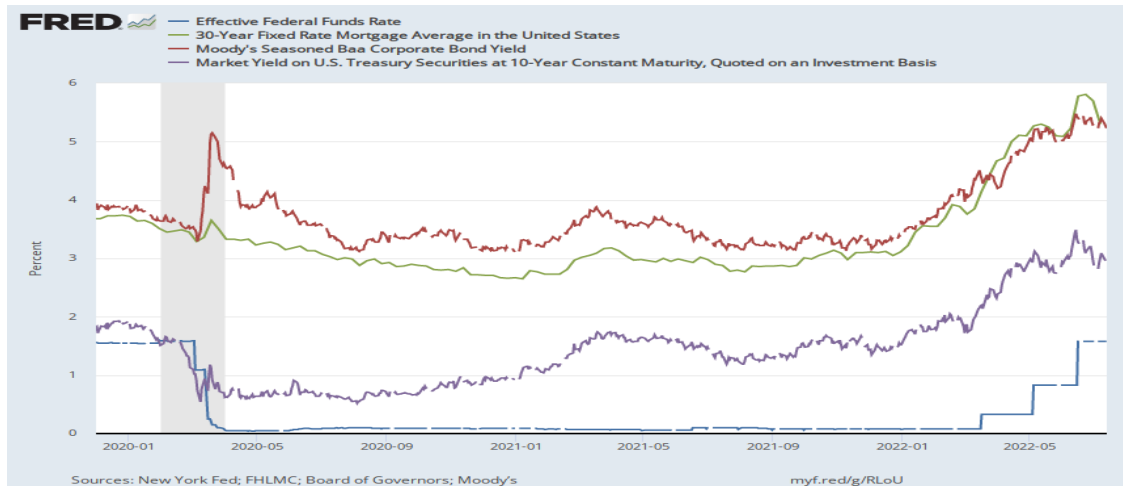


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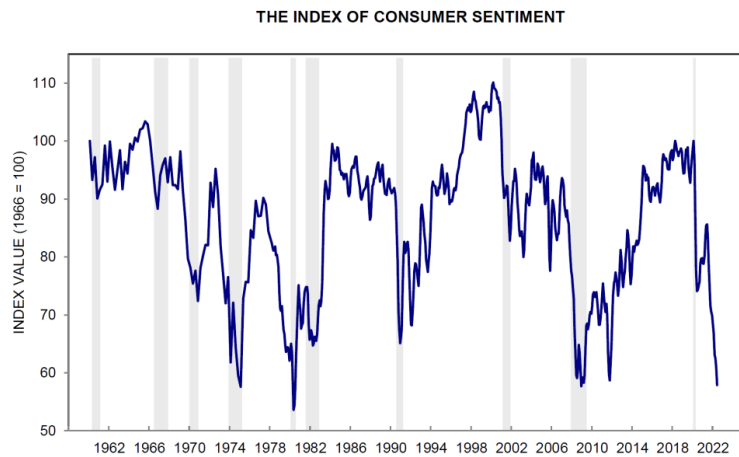
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# The Case for Recession: Long-term Rates?



# The Case for Recession: Consumers are Worried





# June Employment Report?

## • Household Survey:

- 315 thousand fewer people employed.
- 350 thousand people dropped out of the labor force.

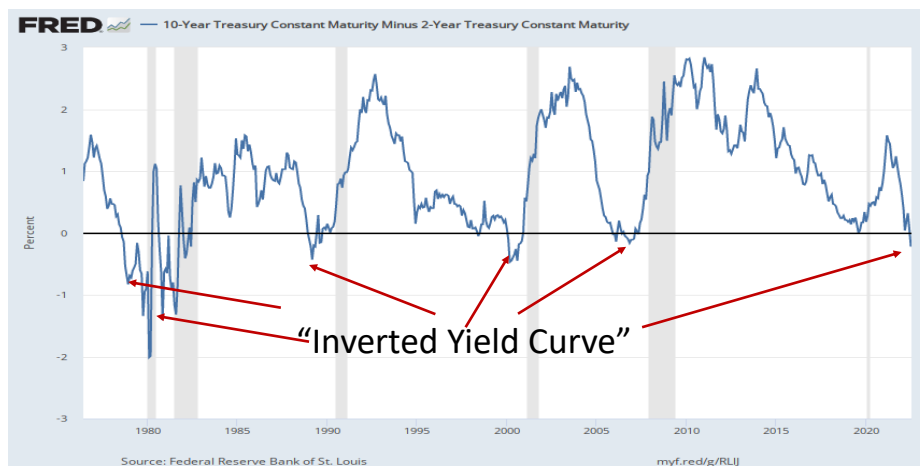
## • Firm or Establishment Survey:

- 370 thousand more jobs created in June.
- Consensus estimate was 265 thousand

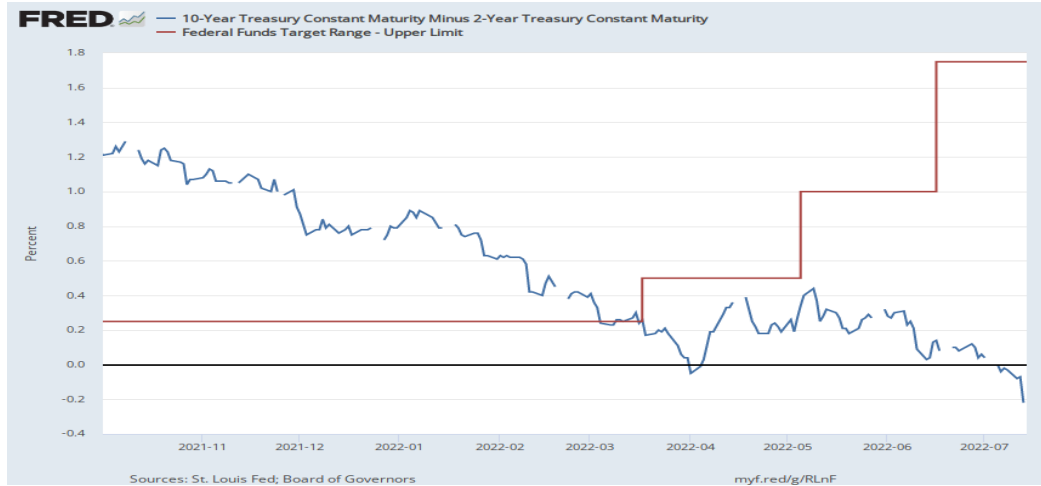
Are you confused?

I am

# The Fed is Over Doing Rate Increases!



## A Closer Look



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## Bloomberg Headline July 13

### Fed Could Weigh Historic 100 Basis-Point Hike After Inflation Scorchers

- Futures show one-in-two chance of super-sized July move
- 75 basis points now also in play for Fed's September meeting



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## So, What Will it Be?

- Darned if I know.

The Fed will have a very difficult choice

### a) Keep interest rates high(in an election year) to slow inflation

1. causing a recession recovery.
2. disrupting financial markets.

### b) Don't let rates rise too much cushioning the effect on employment

1. avoids a recession (maybe).
2. inflationary expectations become unanchored

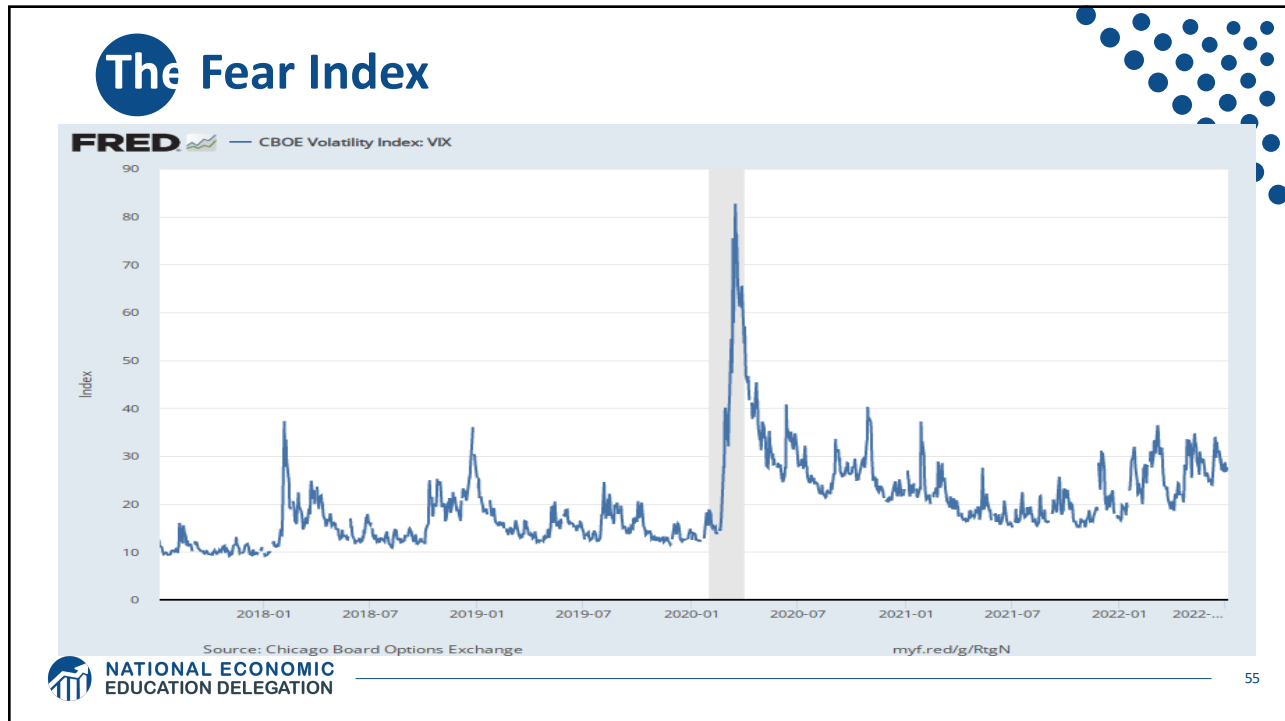
## The Conflict in Ukraine and the US Economy

### • Short run

- Uncertainty
- Increase in Cost of Food and Fuel

### • Long run

- Decrease in Globalization
- The Role of the Dollar as a International Reserve Currency.



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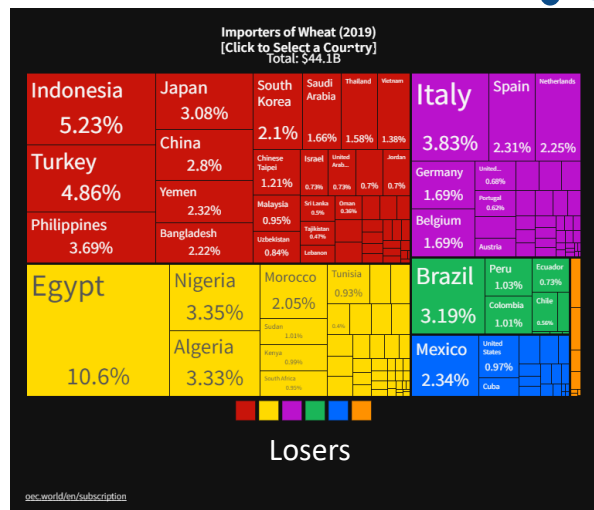
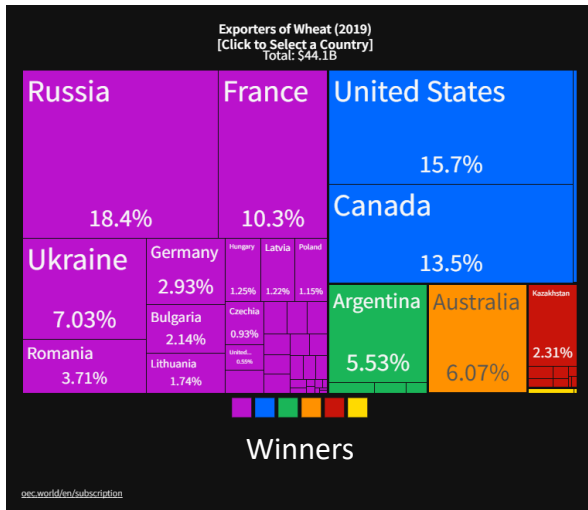
# Wheat Prices Also Look Scary



Wheat Futures Prices  
 Source: <https://www.macrotrends.net/2534/wheat-prices-historical-chart-data>

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# The Price of Wheat: Winners and Losers



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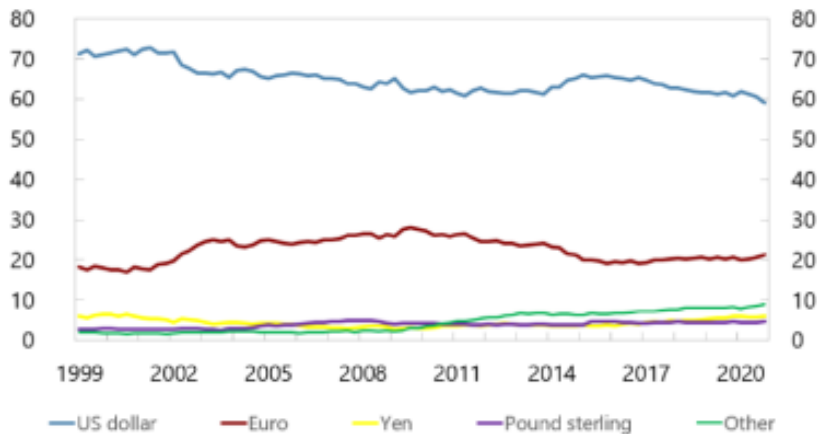
# Long-run Effects

- **Deglobalization to Protect Supply Chains.**
- **New Developments to avoid-US imposed financial wars.**
  - China’s alternative to SWIFT
  - Rise (or fall?) of crypto currencies
  - The Dollar’s Role as a reserve Currency

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# Demand for Dollars by Central Banks

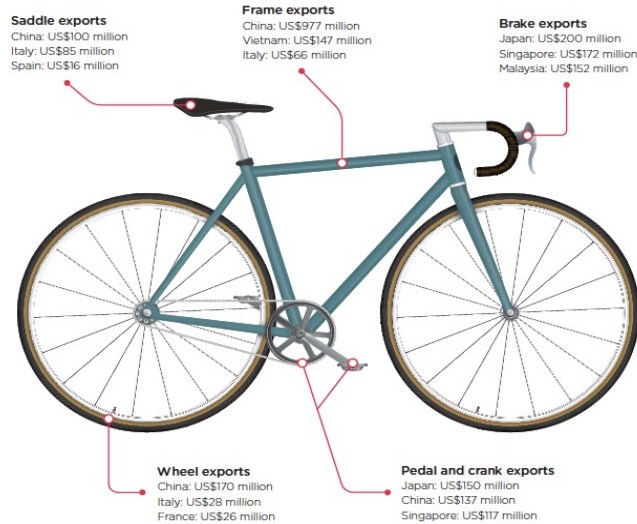
(currency composition of global foreign exchange reserves, percent)



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## Trade: Alan Deardorff, University of Michigan

Figure 1.1 Where do bicycles come from?



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## Questions?

[www.NEEDelegation.org](http://www.NEEDelegation.org)  
Geoffrey Woglom  
grwoglom@amherst.edu

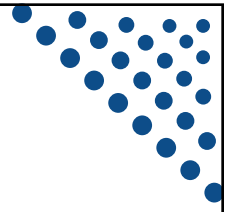
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For every state and county in the United States.  
Detailed graphs on employment, housing, moves, and other statistics.

