

Osher Lifelong Learning Institute, Summer 2023

Contemporary Economic Policy

Oklahoma State University, OK
May-June, 2023

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: 652+ members**

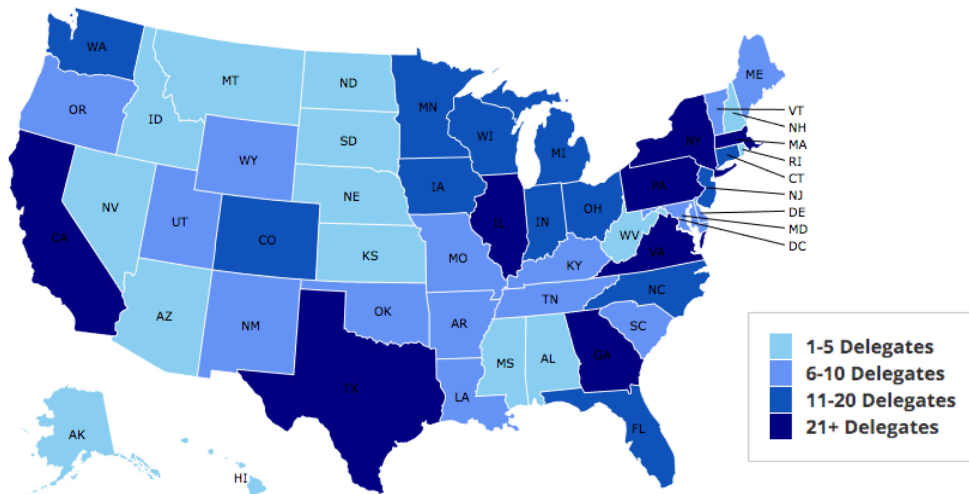
- At all levels of academia and some in government service
- All have a Ph.D. in economics
- Crowdsource slide decks
- Give presentations

- **Global Partners: 48 Ph.D. Economists**

- Aid in slide deck development



Where Are We?



Available NEED Topics Include:

- US Economy
- Healthcare Economics
- 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
- Healthcare Economics



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Course Outline

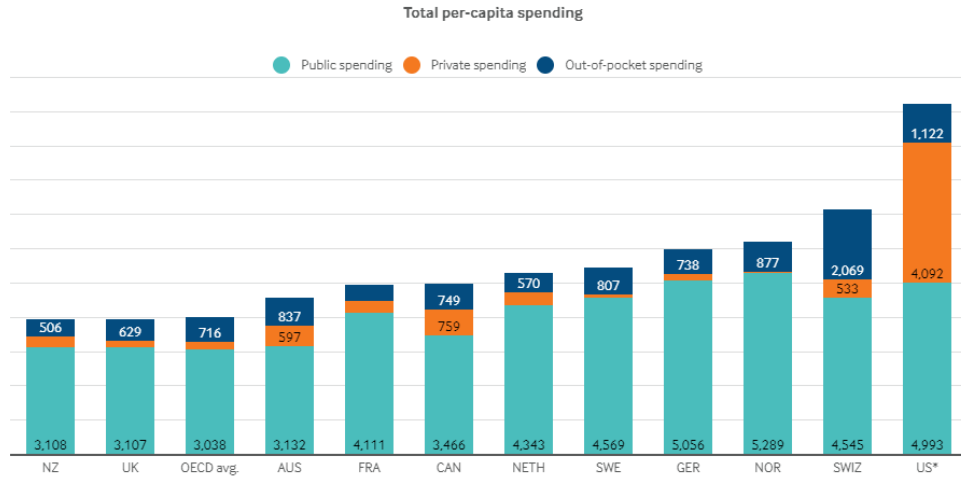
- **Contemporary Economic Policy**
 - Week 1 (5/24): US Economic Update (Jon Haveman, NEED)
 - Week 2 (5/31): Healthcare Economics (Jon Haveman)
 - Week 3 (6/7): Federal Debt (Brian Peterson, Lagrange College)
 - Week 4 (6/14): Trade Deficits and Exchange Rates (Alan Deardorff, Univ. Michigan)



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International Comparison: Health Spending

Dollars (US\$), adjusted for differences in cost of living



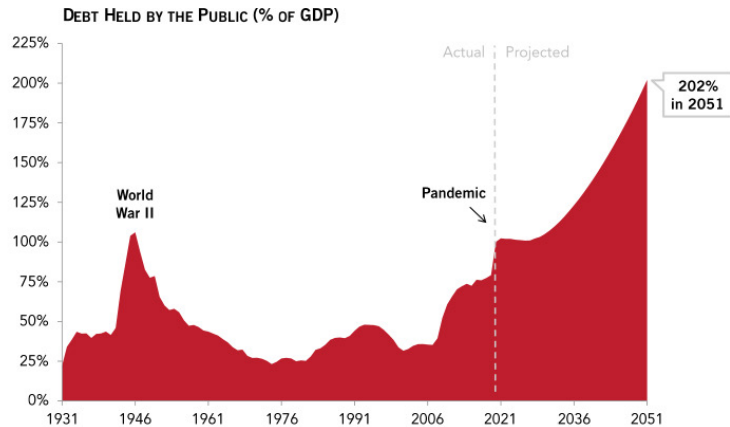
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The Federal Debt is Becoming A Problem



The national debt is on an unsustainable path



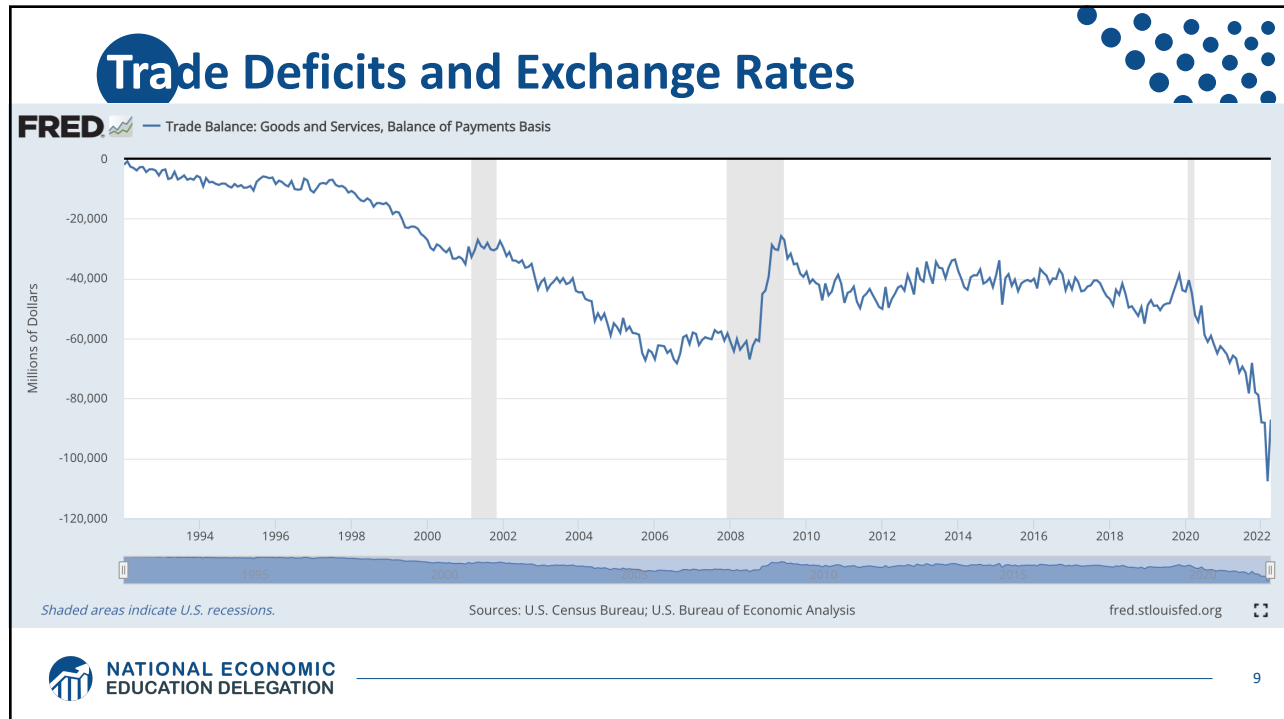
SOURCE: Congressional Budget Office, The 2021 Long-Term Budget Outlook, March 2021.
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Submitting Questions

- **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.**
- **Slides will be available from the NEED website shortly after the talk (https://NEEDEcon.org/delivered_presentations.php)**

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INFLATION



US Economic Update

OLLI – Oklahoma State University

May 24, 2023
Jon Haveman, Ph.D.
NEED



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Credits and Disclaimer

- **This slide deck was authored by:**

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- Scott Baier, Clemson University
- Geoffrey Woglom, Amherst College (Emeritus)
- Brian Dombeck, Lewis & Clark College
- Doris Geide-Stevenson, Weber State

- **Disclaimer**

- NEED presentations are designed to be nonpartisan.
- It is, however, inevitable that the presenter will be asked for and will provide their own views.
- Such views are those of the presenter and not necessarily those of the National Economic Education Delegation (NEED).



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Outline

- About the U.S. Economy
- Economic Indicators
- Inflation/Federal Reserve/Banks
- Debt Ceiling

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The U.S. Economy

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Some Basic Statistics, April 2023

Statistic:	Value
Population	334.8 Million
Labor Force	166.7 Million
Employment	155.7 Million
Gross Domestic Product (GDP)	\$26.5 Trillion
Income per Capita	\$67,676
Ave. Hourly Earnings	\$33.36

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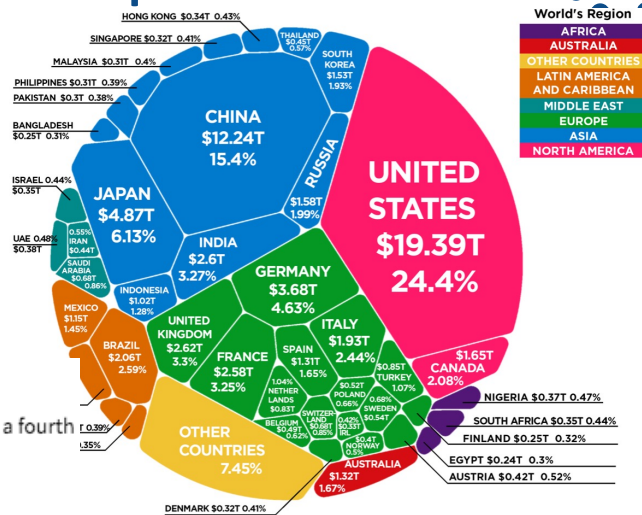
U.S. Economy in Global Perspective

U.S. Nominal GDP:

\$21.538 trillion in 2019-Q4
\$19.637 trillion in 2020-Q2
\$26.466 trillion in 2023-Q1

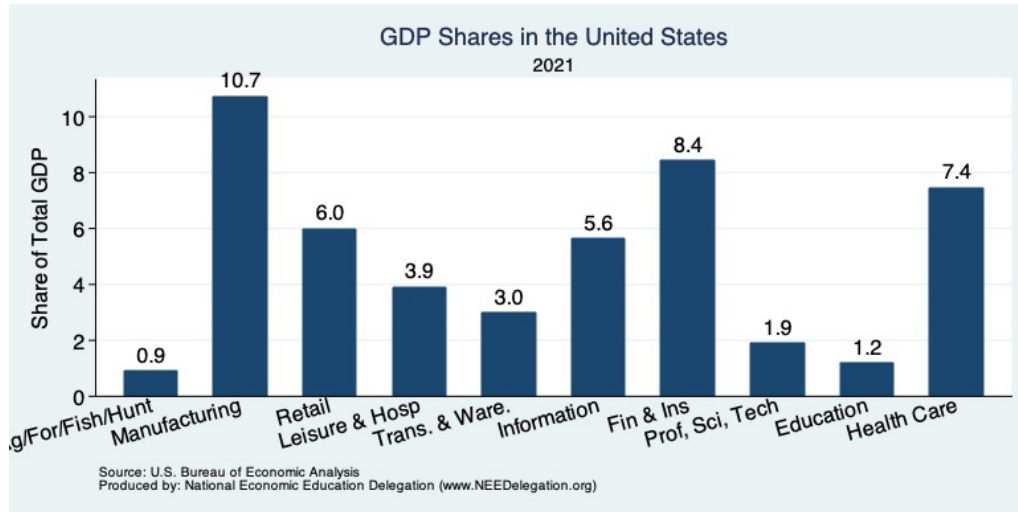
% Share of the Global Economy

The 173 countries outside the top 20 make up less than a fourth of the total global economy.



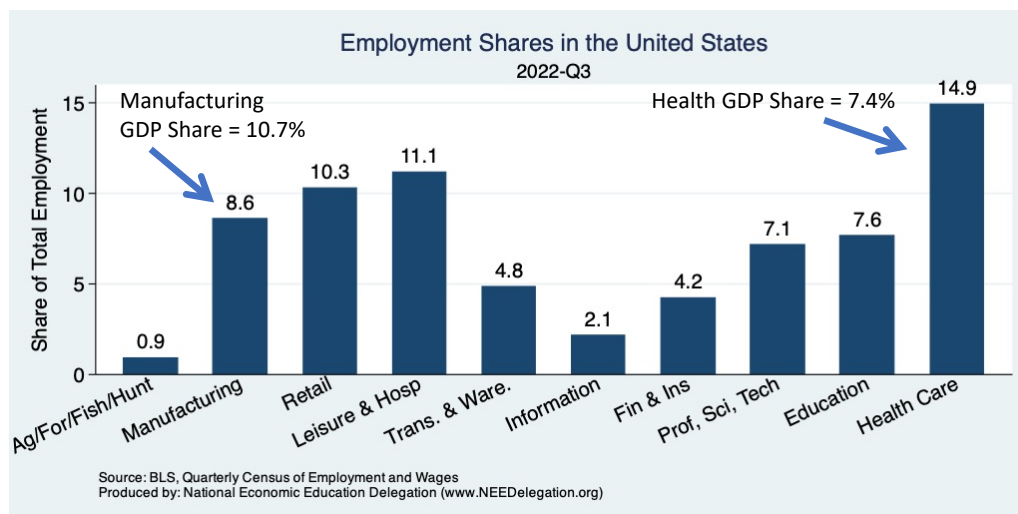
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Composition of the U.S. Economy: GDP



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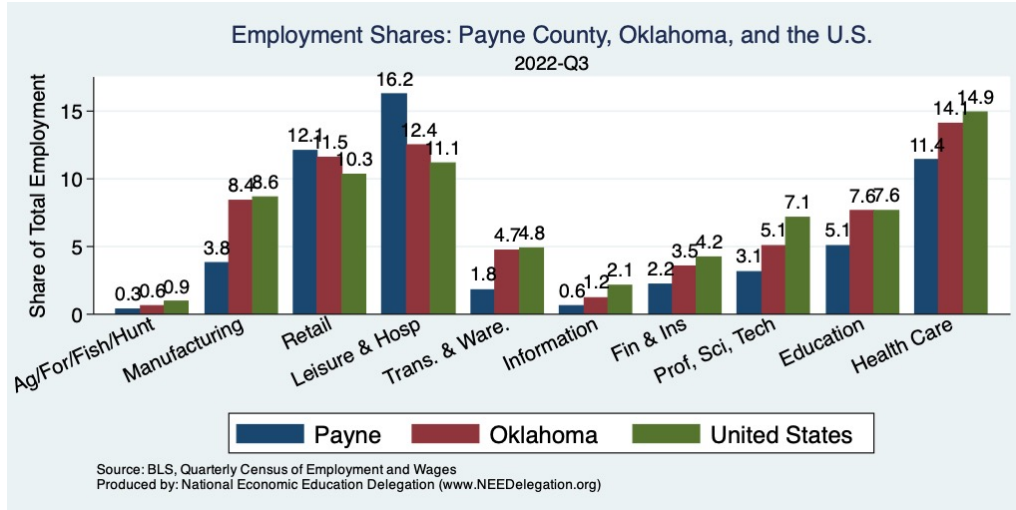
Composition of the U.S. Economy: Employment



Note: Does not add to 100% because of omitted sectors.

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Composition of the Payne Economy: Employment



Note: Does not add to 100% because of omitted sectors.

Economic Indicators

Headline: July 28, 2022

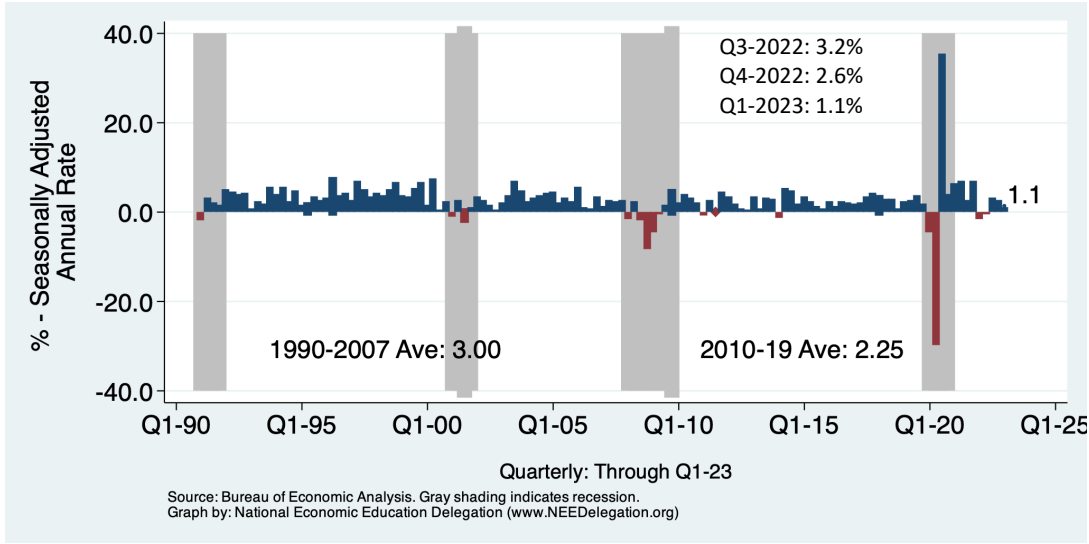
G.D.P. Report Shows a Drop, Fanning Fears of a U.S. Recession

- A key measure of economic output fell for the second straight quarter, fanning fears that the United States could be entering a recession.
- Gross domestic product, adjusted for inflation, fell 0.2 percent in the second quarter, the equivalent of a 0.9 percent annual rate of decline. Follow updates.

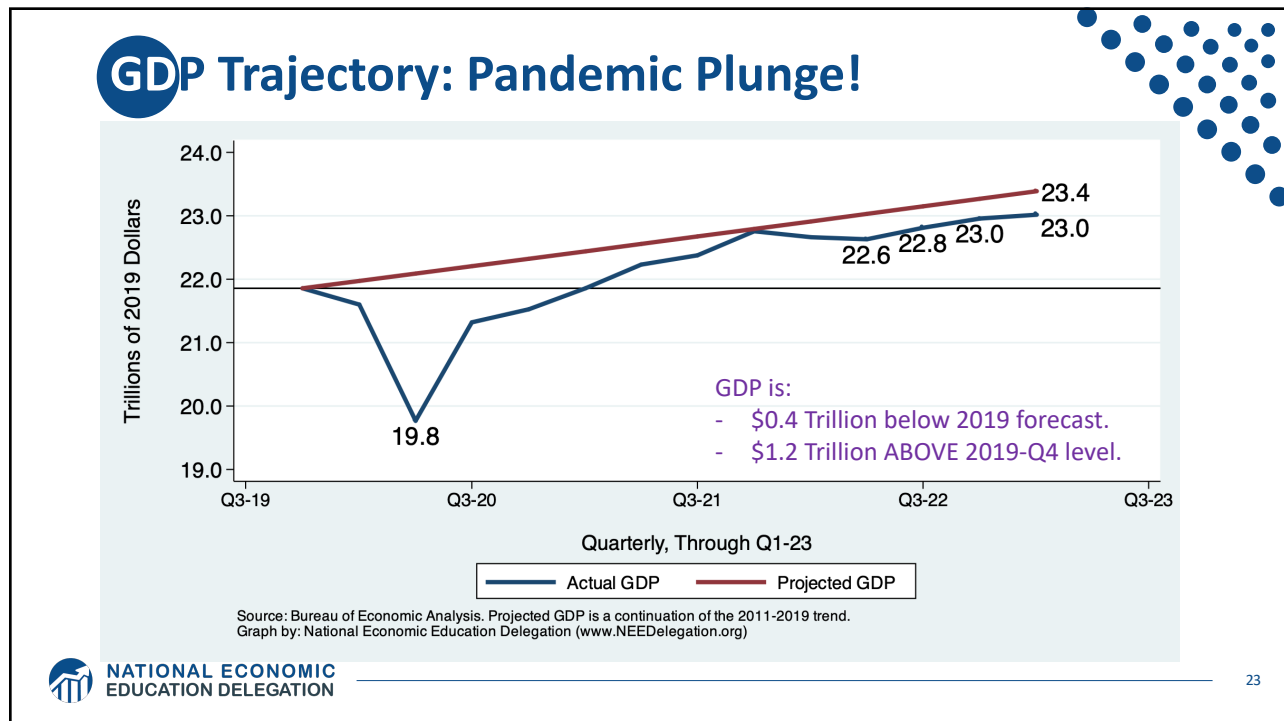
Old news...

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GDP: Quarterly Growth



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“Accounting” for GDP

- **Expenditures drive GDP growth.**
 - GDP is the sum of four categories of spending:
 - Consumption
 - Investment
 - Plant and equipment, residential real estate, and inventories.
 - Government spending
 - Net Exports: Exports – Imports
- **GDP = Consumption + Investment + Government + Net Exports**

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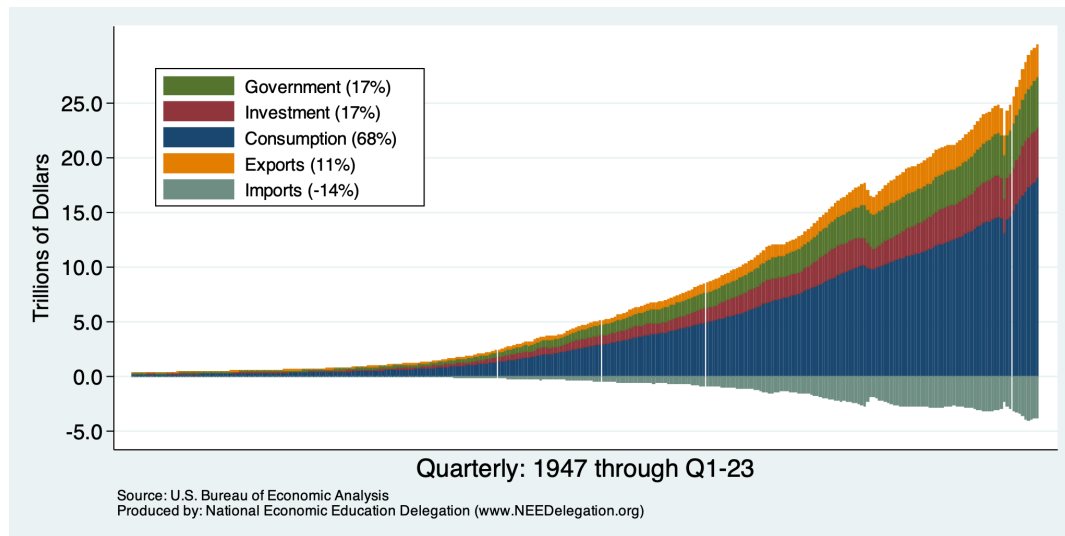
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A Note on Imports and GDP

- **GDP = Consumption + Investment + Government + Net Exports**
 - Net Exports = Exports – Imports
- **Gives the impression that IMPORTS are bad for GDP**
 - They are not.
 - They are merely subtracted from the equation because the measurement of consumption, investment, and government all include imports.
- **Calculating Gross DOMESTIC Production must exclude IMPORTS**
 - It is merely an accounting identity.

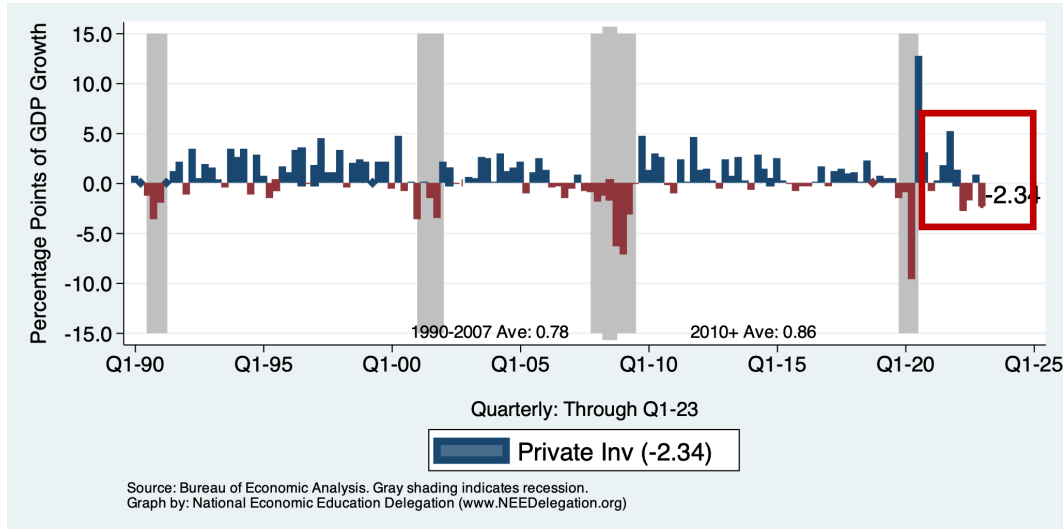
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Composition of GDP



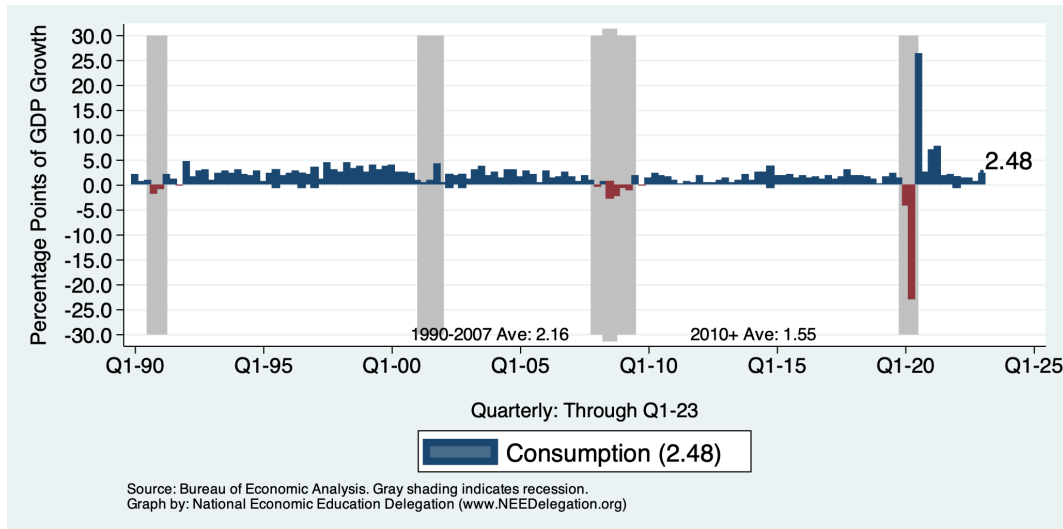
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Contribution to GDP Growth: Inventories



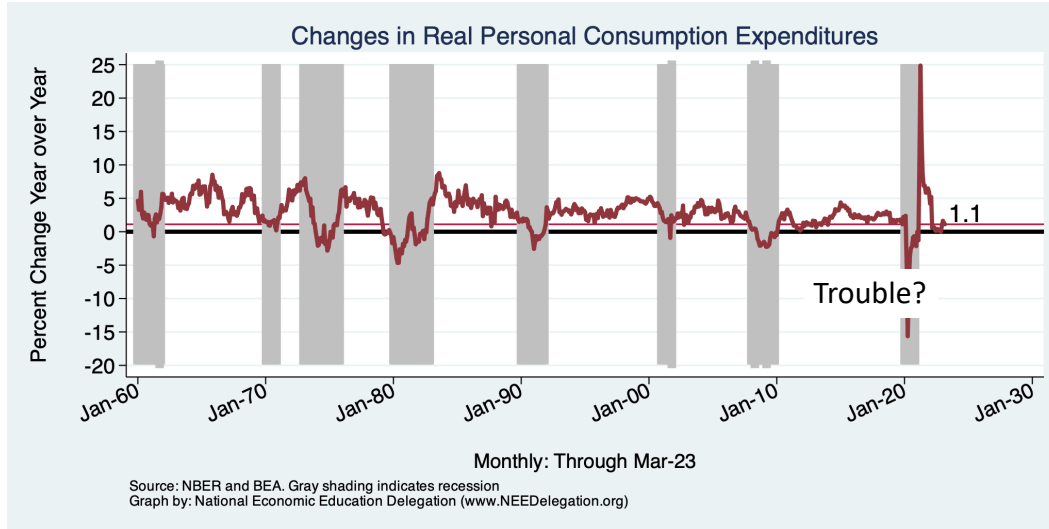
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Contribution to GDP Growth: Consumption



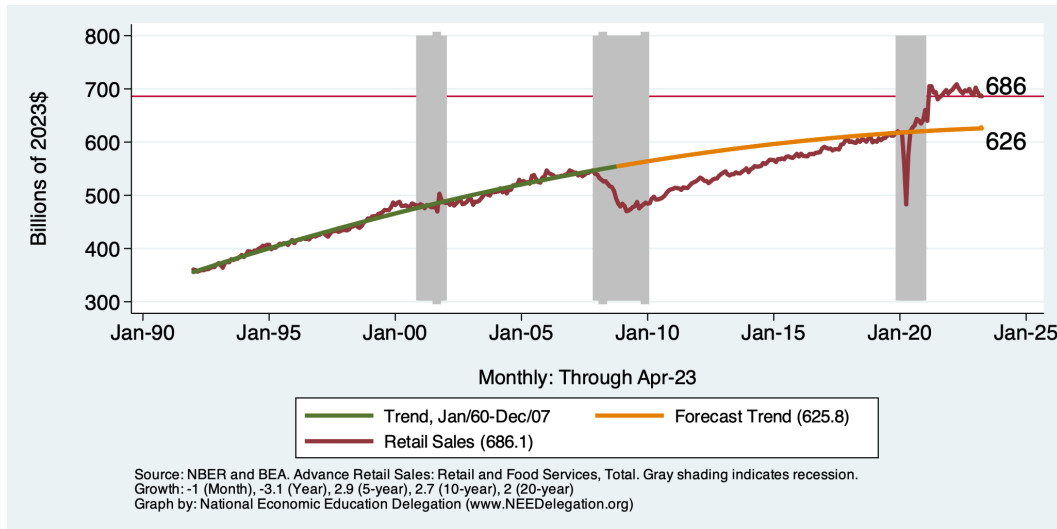
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Personal Consumption Expenditures



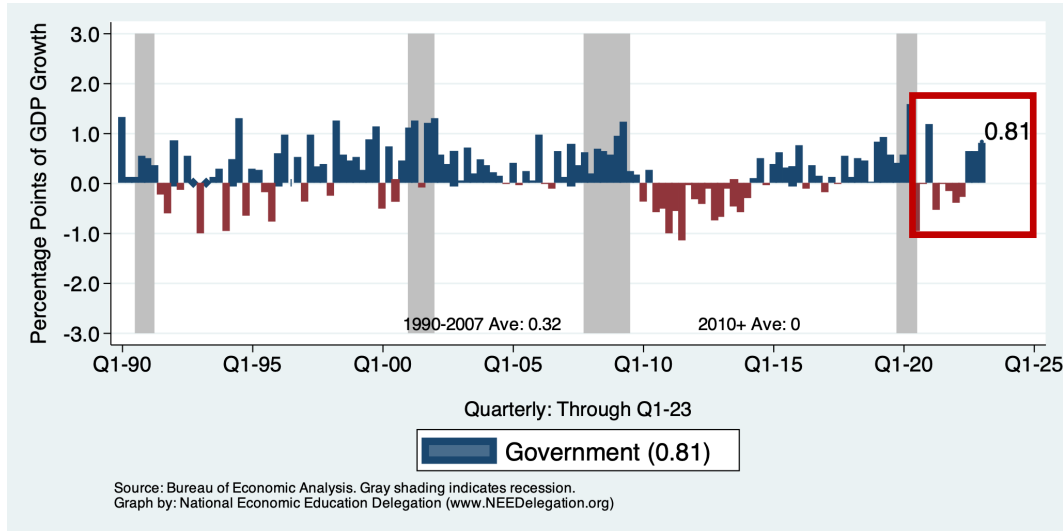
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Retail Sales Remain Elevated!



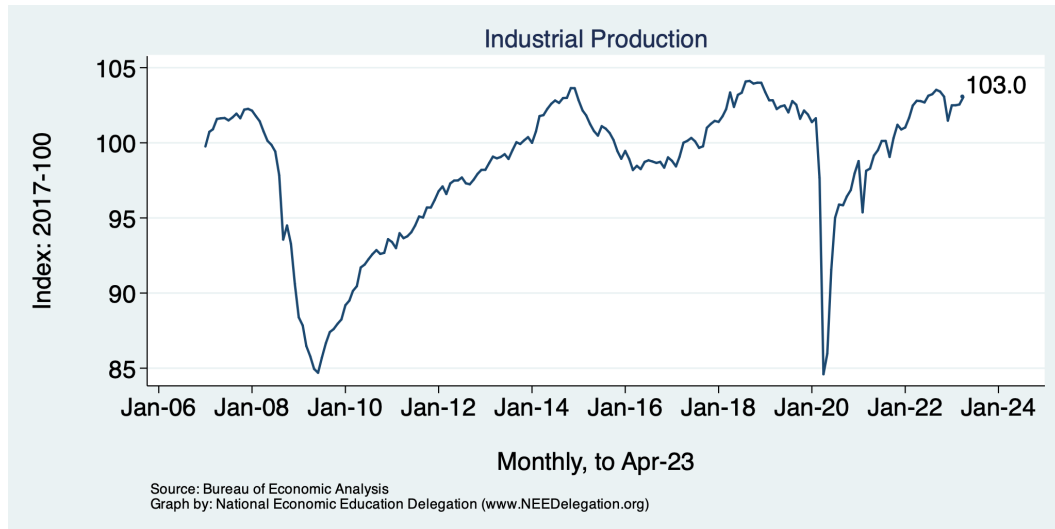
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Contributions to GDP: Government



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Industrial Production (Manuf, Util, Mining)

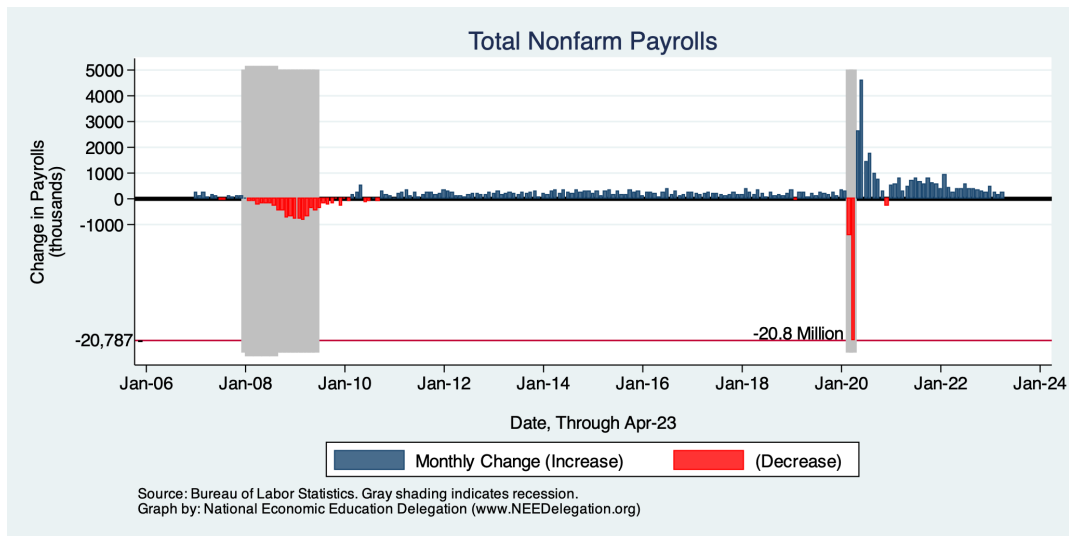


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Employment

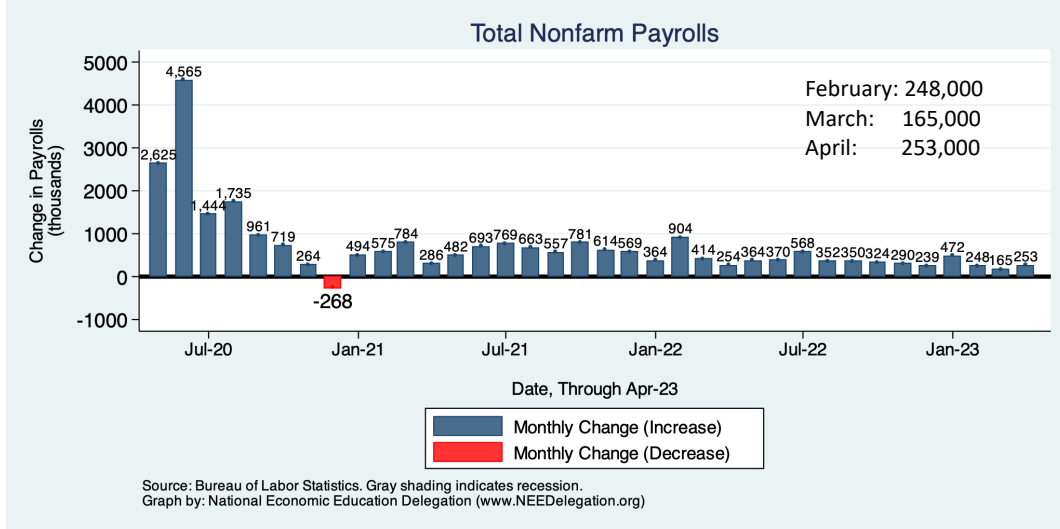
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Monthly Changes in Nonfarm Employment



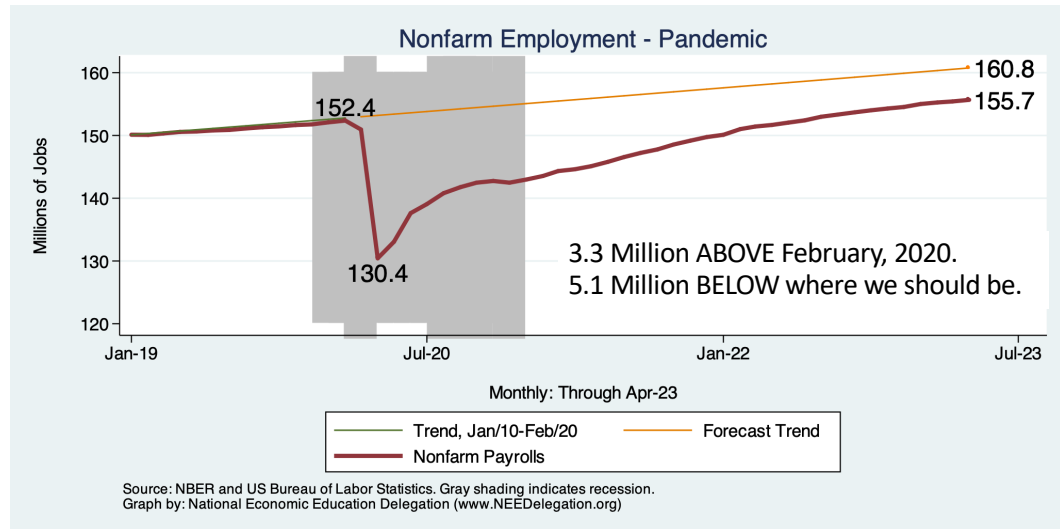
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Monthly Changes in Nonfarm Employment



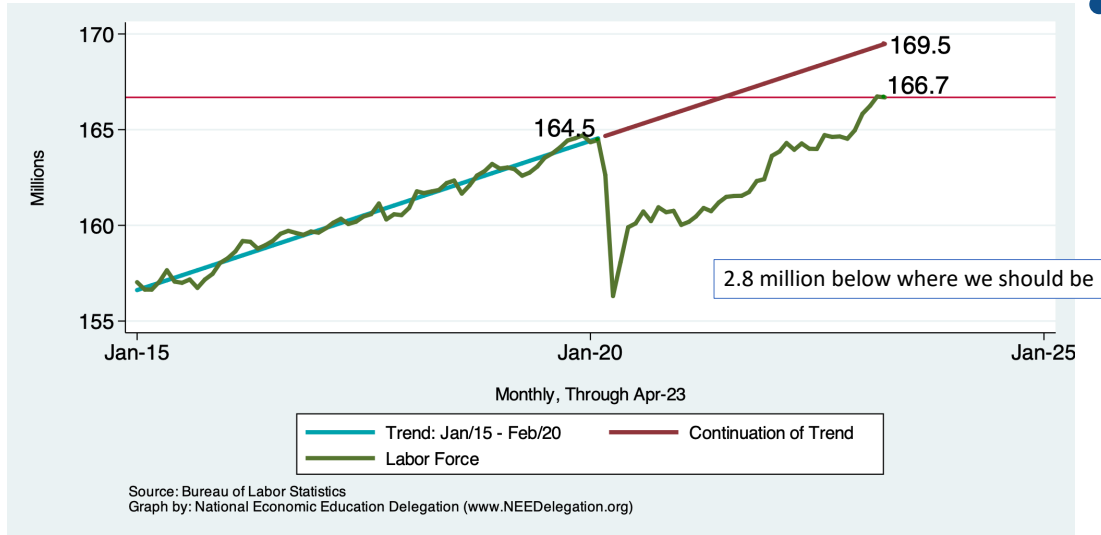
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Employment Gap



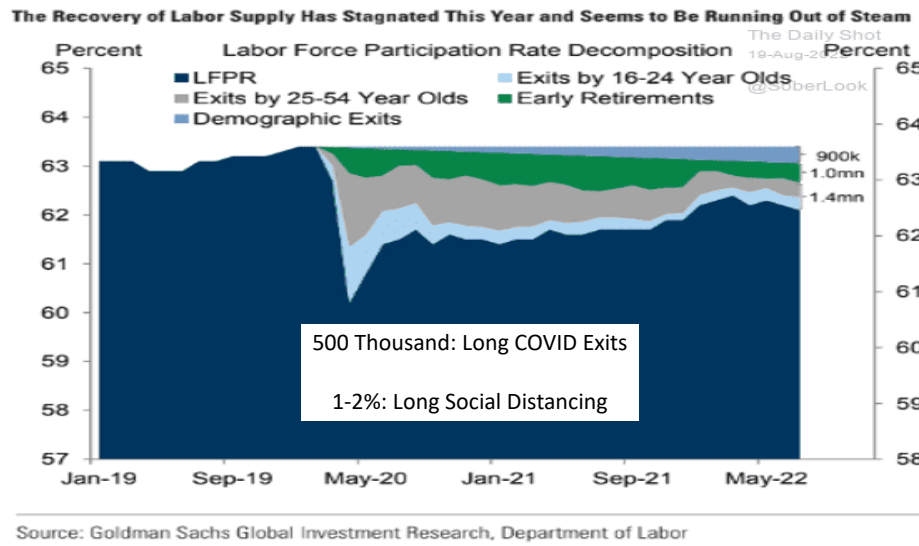
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Where Have All the Workers Gone?



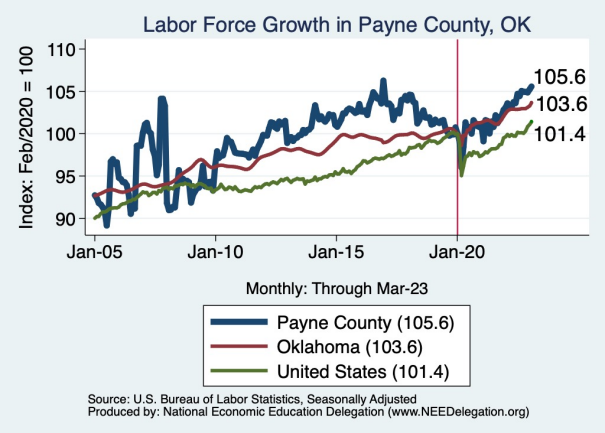
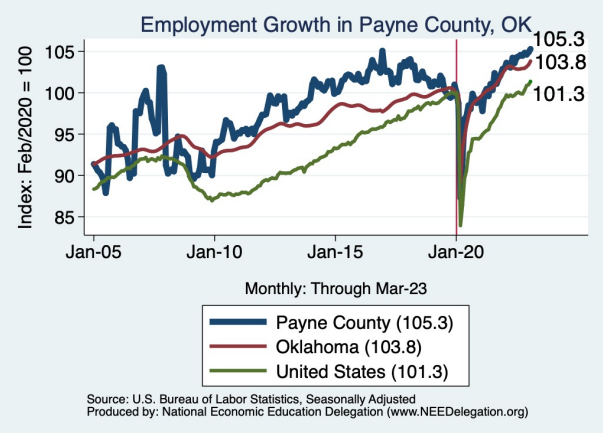
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Some Explanations

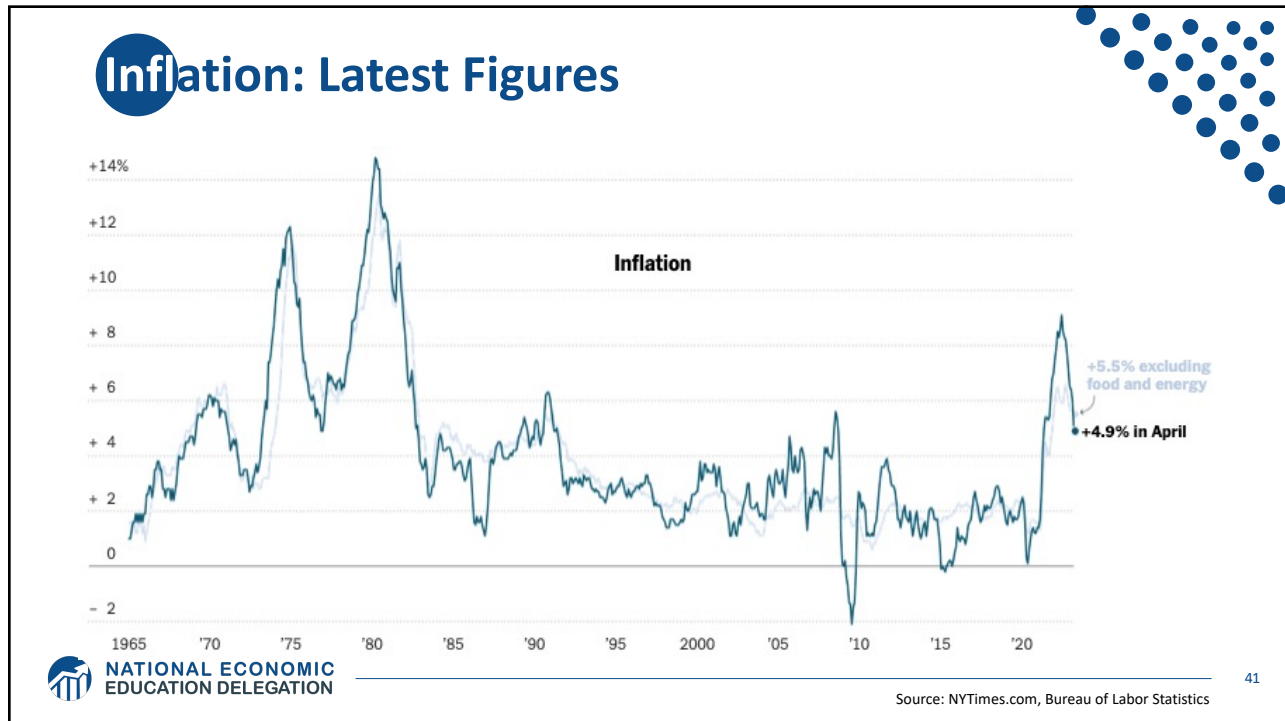


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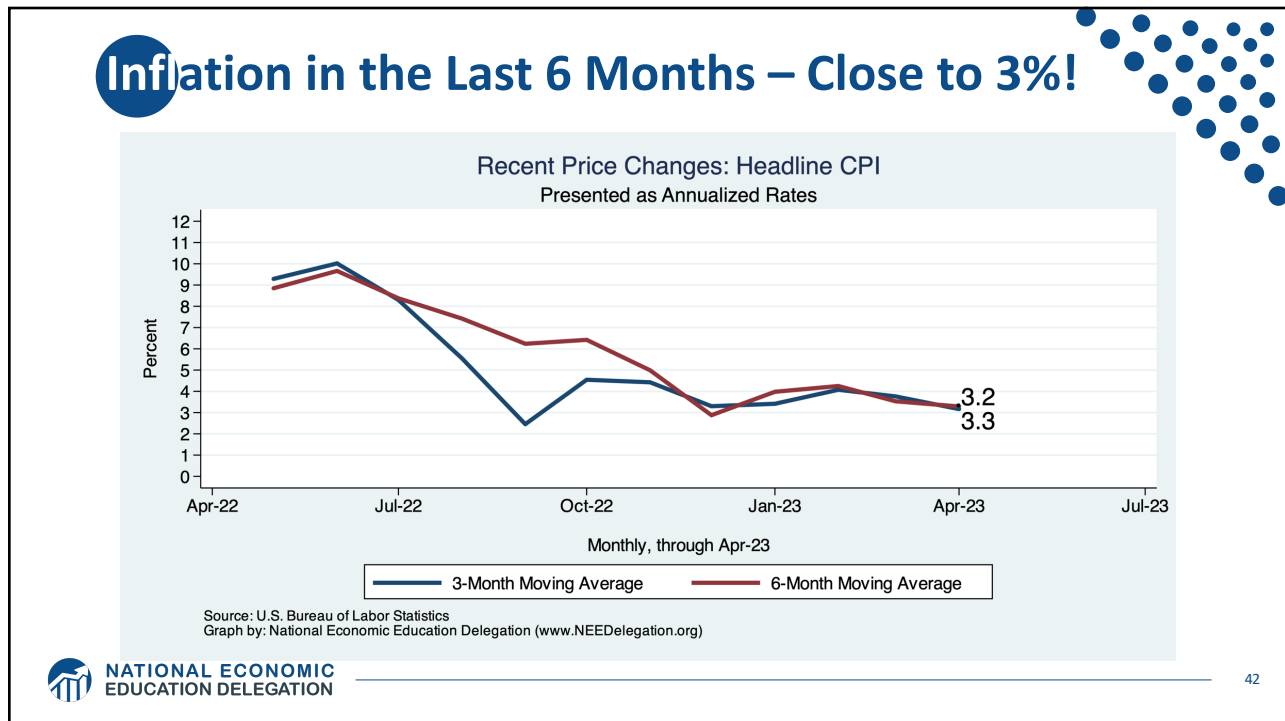
How Are Things Where You Are?



Inflation

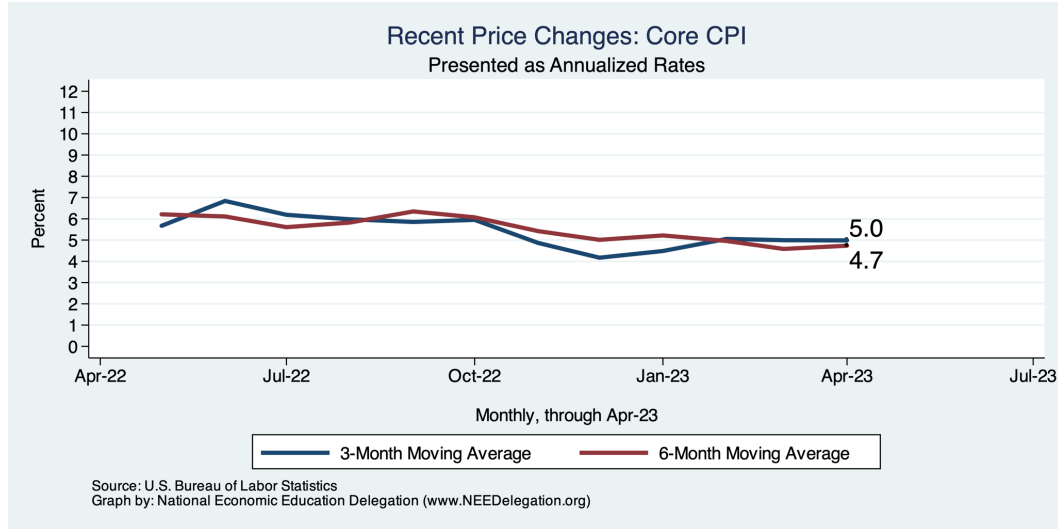


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Inflation: Core Inflation is Stubbornly High



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How Does Inflation Work?

Inflation represents the rate at which the cost of goods and services increase over a period of time.

Demand-Pull



When demand for goods/service exceeds production capacity.

Cost-Push



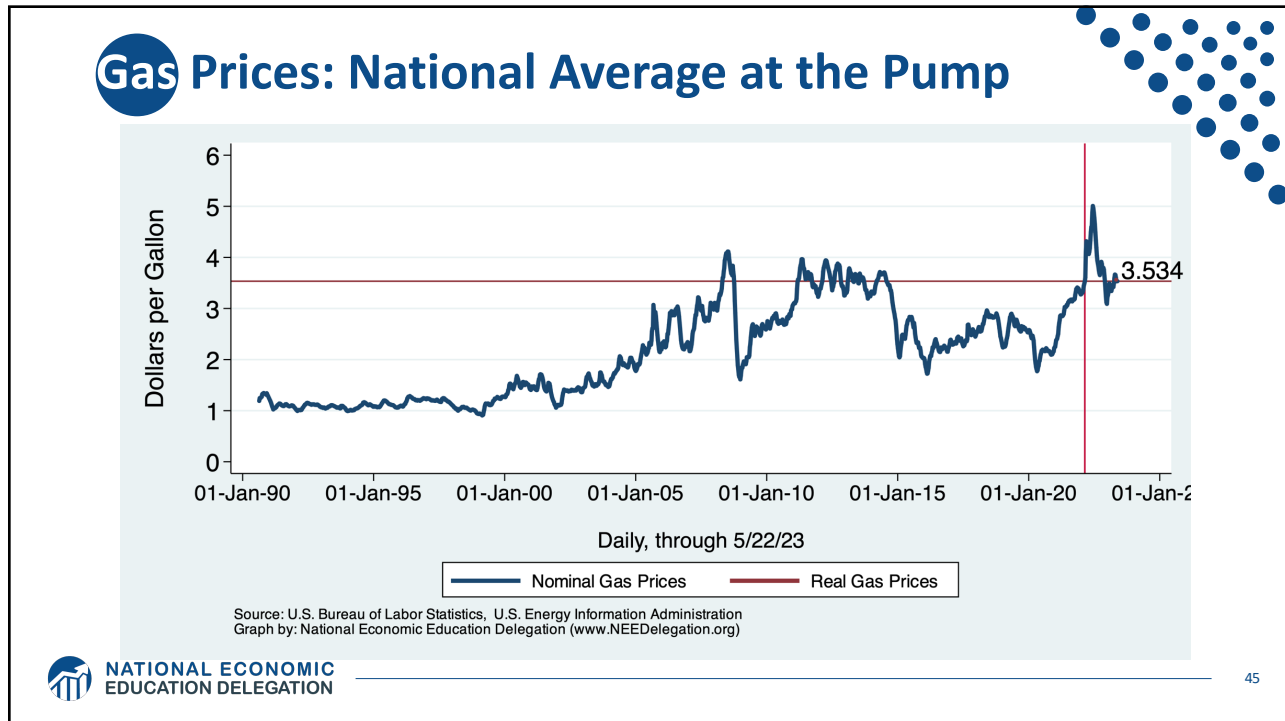
When production costs increase prices.

Built-In

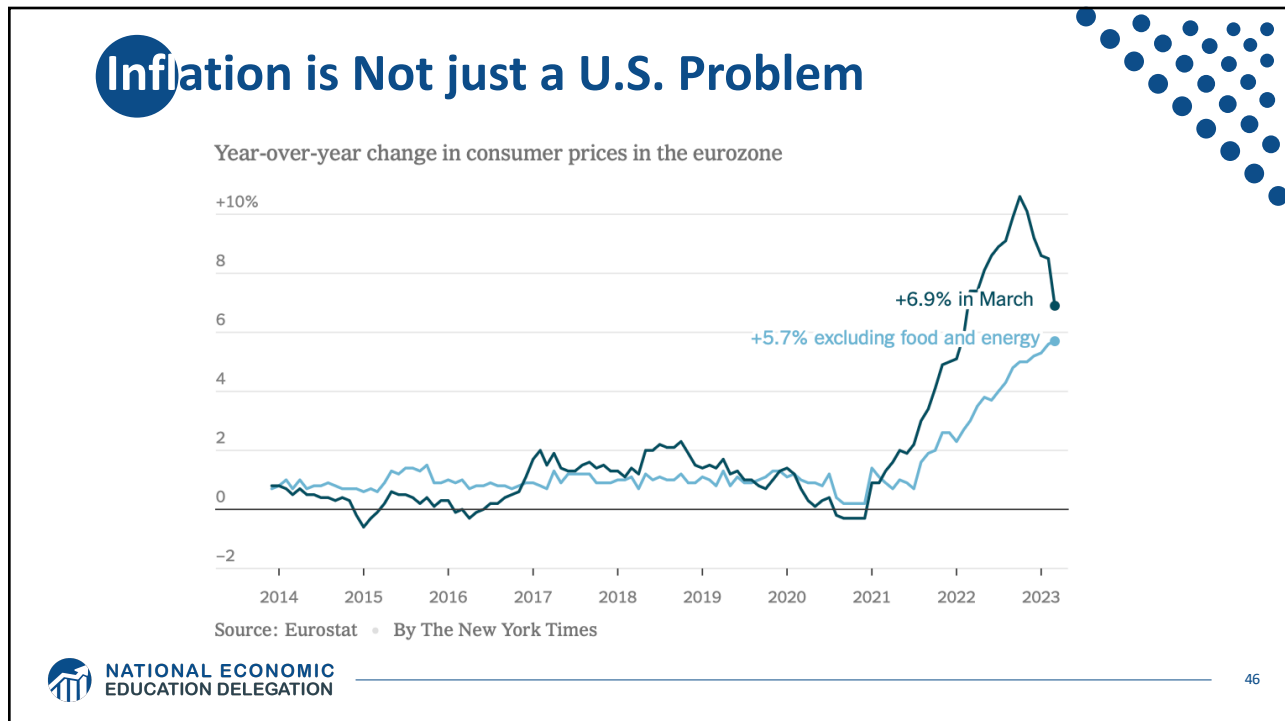


When prices rise, wages rise too, in order to maintain living costs.

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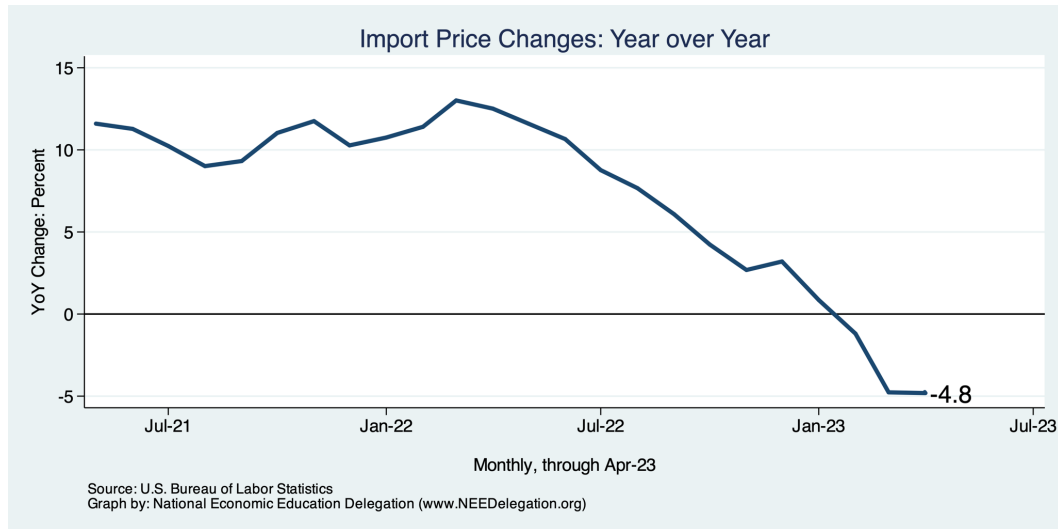
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Supply Chains



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Import Price Inflation WAS High



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Two New Types of Inflation

- **Excuseflation**

- “The cost of my inputs is going up, so I have to raise my prices.”
- You rarely hear: “I’m lowering my prices because costs are going down.”

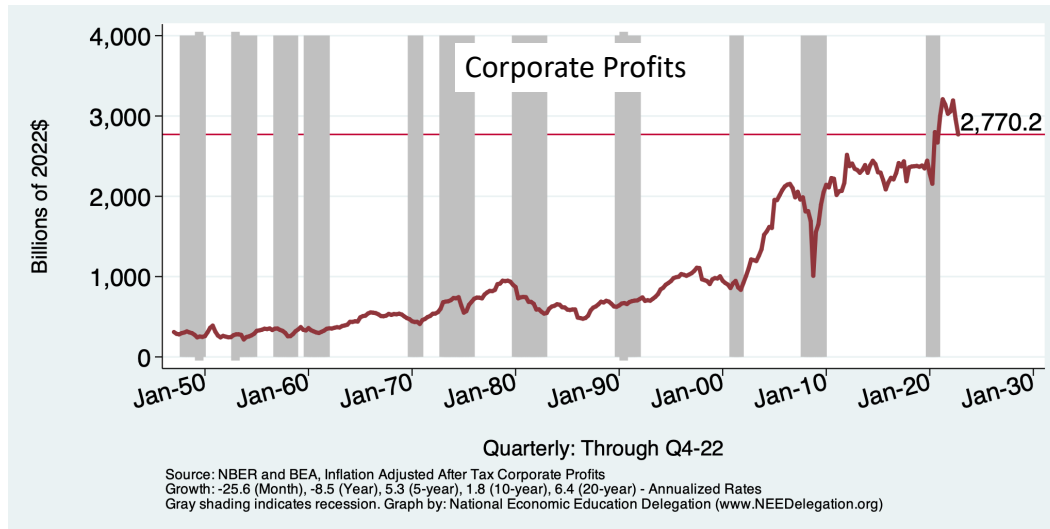
- **Premiumization**

- Taking your product and spicing it up so that you can raise your margins.

- **Together, have led to a Profit-Price Spiral**

- Raising prices to cover costs plus a little extra.
- Raising margins with extra frills.

Corporations Have Pricing Power!



My Thoughts on the Sources of Inflation

- **Supply Chain issues were significant – less so now.**
- **Import price inflation was high – negative now.**
- **Composition of spending changed significantly.**
 - Is now bouncing back, as are prices.
- **Corporations have used the cover of inflation to raise prices more.**
- **But there was too much total spending.**
 - Fiscal stimulus led households to increase saving over 2021 by more than \$2 trillion. Strong retail sales numbers suggest they are prepared to spend it.
- **Whose to Blame: ARP possibly too big, but the Fed could have acted sooner.**
- **Bottom line: Recovery from a dramatic economic disruption is seldom painless.**



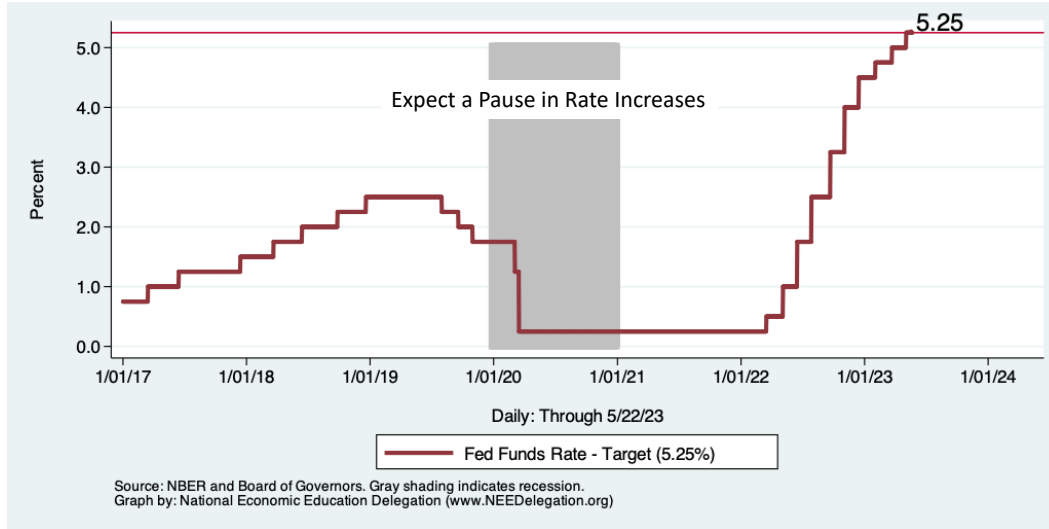
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What's the Fed Doing About It?



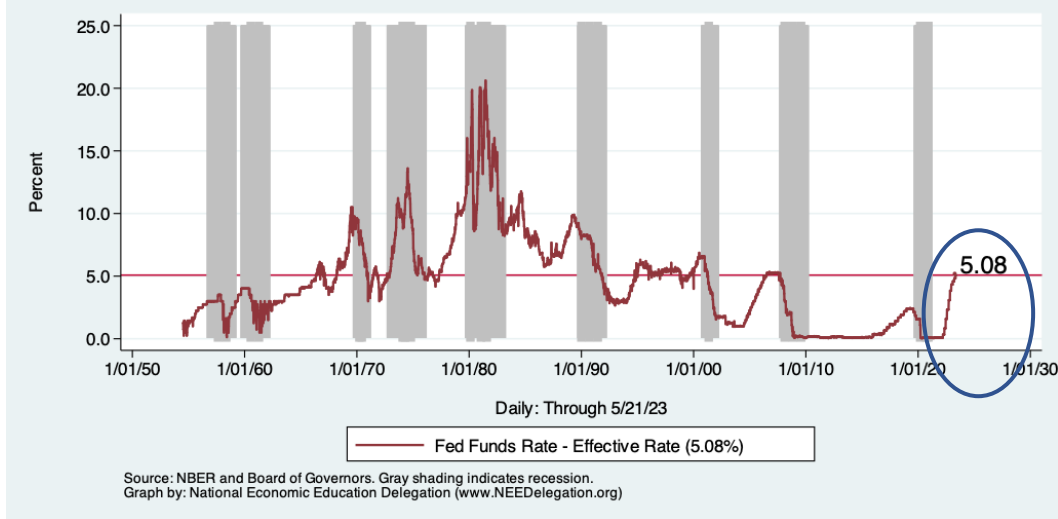
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Federal Funds Rate – Recent Activity



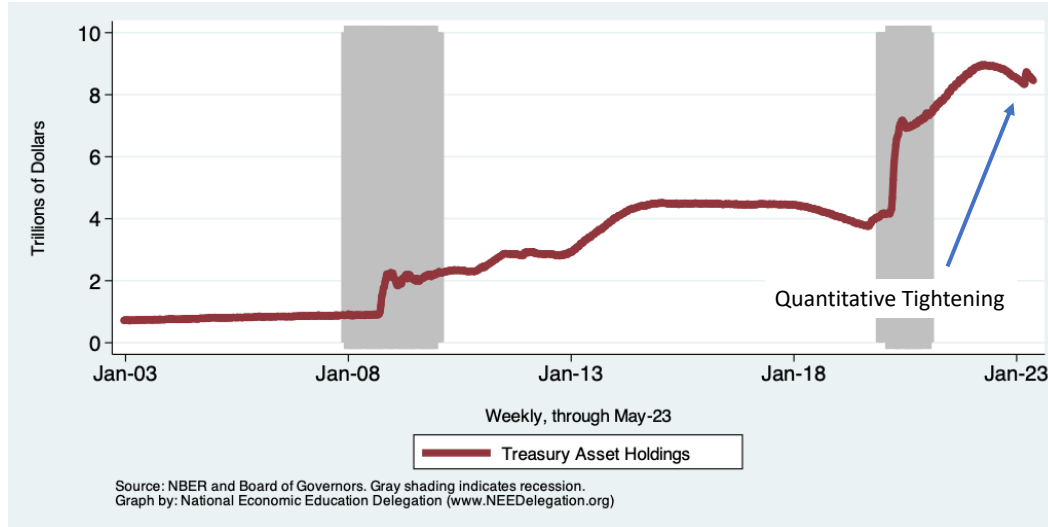
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Raising the Federal Funds Rate



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Fed: Also Reducing its Asset Holdings



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Implications for Demand

- Investment borrowing
- Home loans – tied to 10-year Treasury
- Car loans
- Credit cards
- Savings accounts – positive
- And more....

- All of which slows the economy.

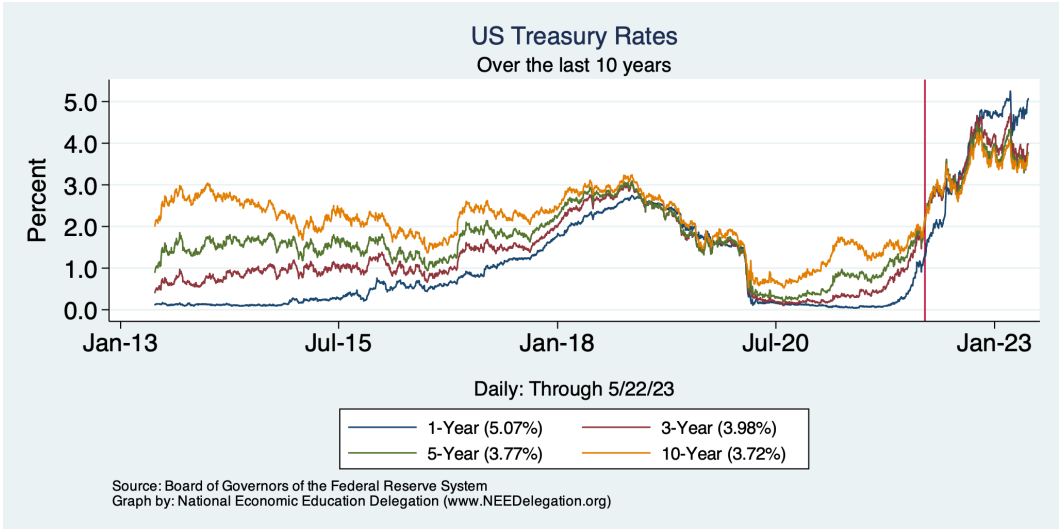


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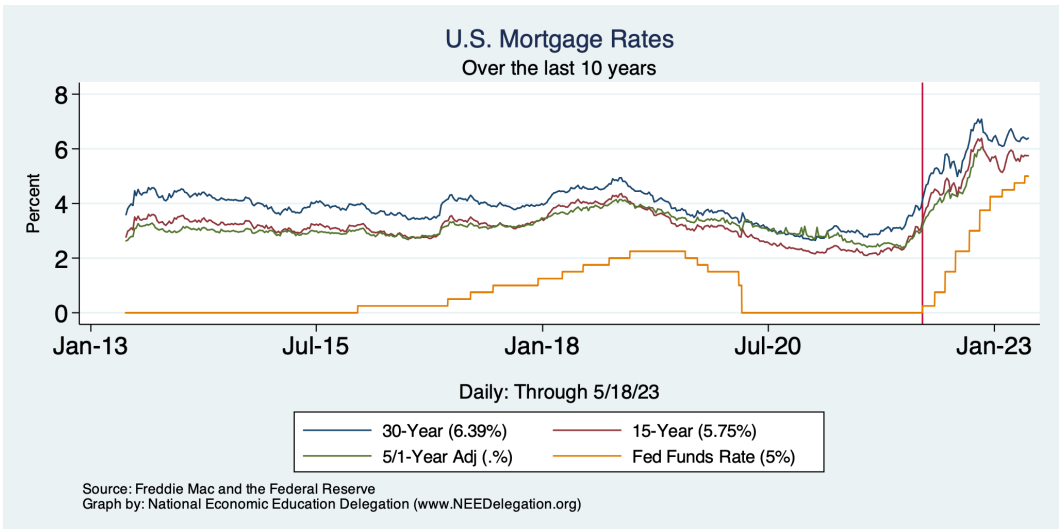
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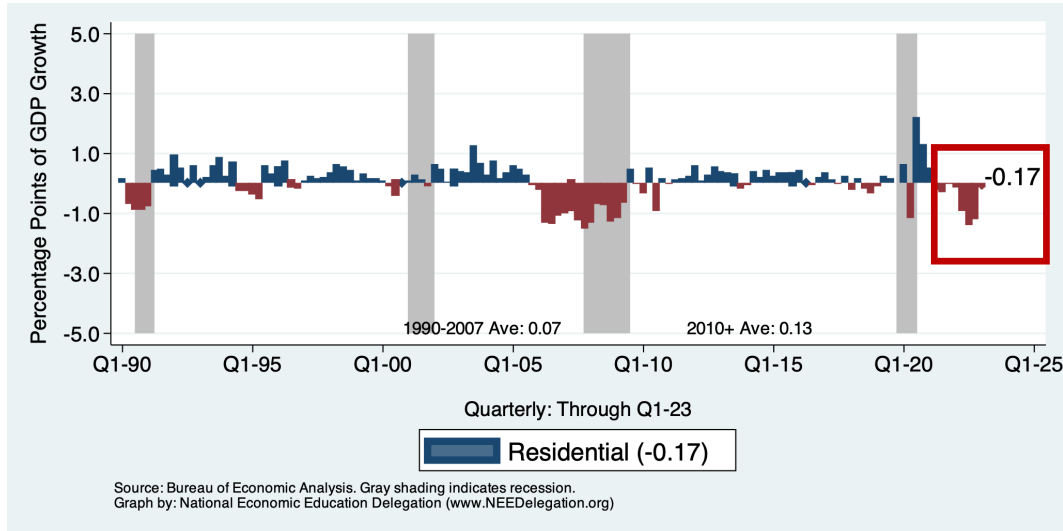
Treasuries



Mortgage Rates

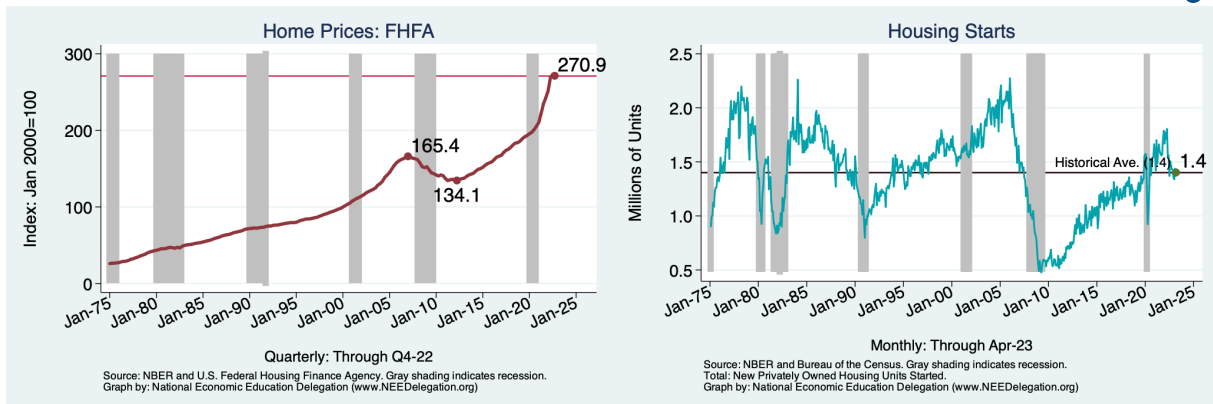


Contributions to GDP: Residential Investment



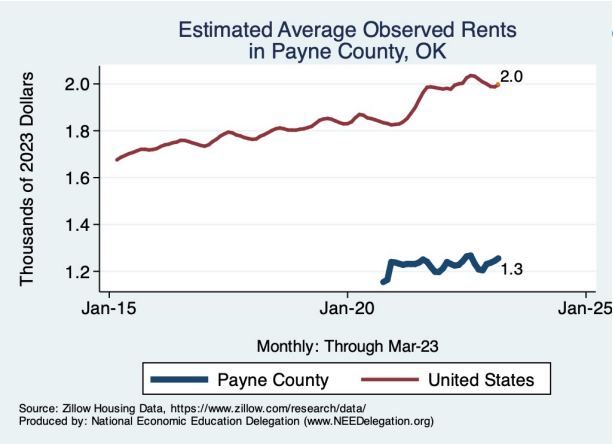
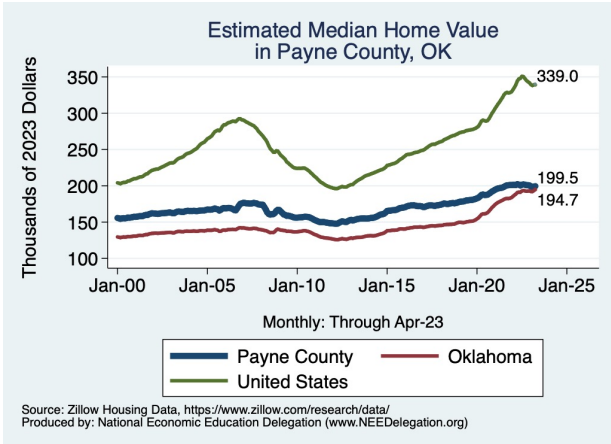
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Home Prices and Housing Starts



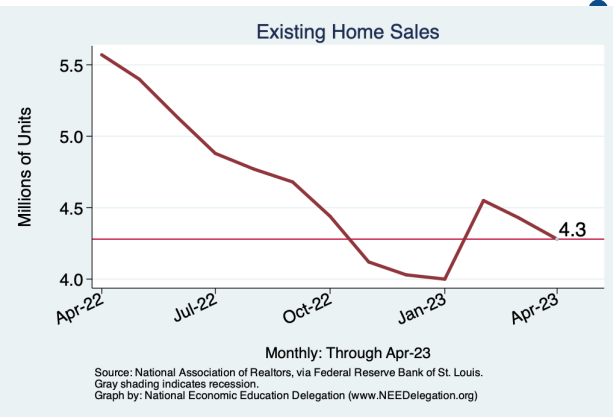
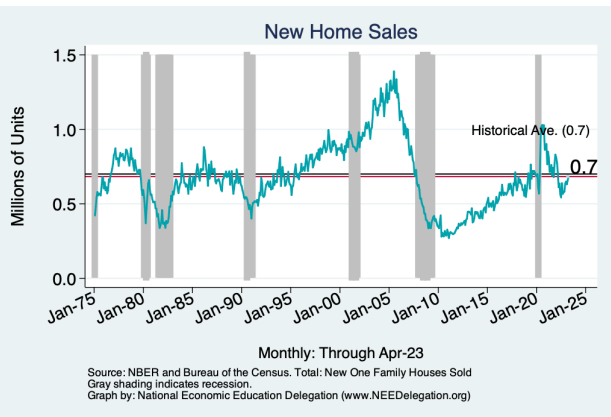
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Home Prices ... Depends on Where You Are



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Home Sales are Turning Around...Maybe



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What About the Banks?

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Banks...

- Silicon Valley Bank
- Signature Bank
- First Republic Bank

- Banks were too long on long-term Treasuries.

- Have we reached the end?
- Rising interest rates are like the tide going out....
 - They expose who is swimming with no clothes on.
 - The tide isn't completely out.

- Bank balance sheets seem ok, it's stocks that are not.

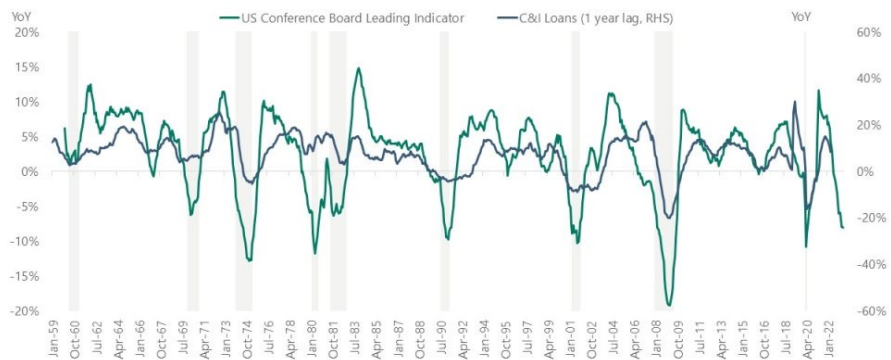
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A Couple of Notes on the Banking Scare

- **Banks like their customers to be:**
 - Sticky – they won't leave.
 - Sleepy – they'll accept close to zero interest rates.
- **Silicon Valley Bank's customers....**
 - Were neither.
 - It's likely that none of this would have happened if they didn't have mobile/connected customers with LOTS of uninsured deposits.
- **Regulation surrounding the share of uninsured deposits is likely coming.**
- **Small bank stocks are rebounding, so we may have dodged this bullet.**

They May Present A Challenge to Growth

Tighter credit conditions dragging down the economy



Existential Threat: Coming This June!



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What is the Debt Ceiling?

- An amount of debt that the federal government can not exceed without congressional approval.
- From the Constitution: only Congress can authorize the borrowing of money on credit of the United States (Article I, Section 8).
- During WWI, requests came so fast and furiously, that Congress put in place the Debt Ceiling.
 - Approvals then occurred only periodically.
- And it continues today.

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5 Things to Know about the Debt Ceiling

1. The debt limit has been raised continually for more than a century.
2. Raising the debt limit is not about new spending; it is about paying for previous choices policymakers legislated.
3. Only one other advanced country—Denmark—has a separate debt limit rule like ours (but theirs isn't binding).
4. Now that the debt hit the ceiling, the Treasury Department is using several extraordinary measures to postpone the day of reckoning.
5. The economic consequences of a large-scale, intentional default are unknown, but predictions range from bad to catastrophic.



How Bad Could It Be?



Lessons from 1979 & 2011

- **Accidental partial default in 1979:**
 - Increased borrowing costs by \$40 Billion!

- **Government shutdown was very costly:**
 - Stock markets plunged (17%).
 - Employment growth stuttered.
 - Treasuries – downgraded credit ratings.
 - Borrowing costs rose.



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An Estimate of the Potential Damage:

- **Moody's Analytics**

- **A prolonged breach could lead to**
 - Could cost up to 7 million jobs,
 - Drive unemployment up to 8%, and,
 - Wipe out \$10 trillion in household wealth.



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Countdown to Default



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What Are the Available Options?

- **A clean debt ceiling lift.**
 - And perhaps default if other side doesn't capitulate.
- **A debt ceiling lift with budget cuts.**
 - And perhaps default if other side doesn't capitulate.
- **Plead the 14th Amendment.**
 - *The validity of the public debt of the United States, authorized by law, including debts incurred for payment of pensions and bounties for services in suppressing insurrection or rebellion, shall not be questioned.*
- **Mint a platinum coin.**

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Economics of the Options

- **What about tax increases?**
 - Nothing in economics remotely suggests that revenue cuts are NECESSARILY preferred to tax increases.
- **Just defaulting isn't enough.**
 - Our monthly expenditures are more than the interest on the debt.
 - Some bills would go unpaid, or perhaps a partial shutdown would be necessary.
- **The cuts being proposed are also not enough.**
 - Saves \$4.8 Trillion over 10 years.
 - CBO projects deficits of \$22 Trillion over 10 years.



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In Order to Solve the Problem...

- **We must address the major contributors to the debt going forward:**
 - Between 2025 and 2033, Social Security and Medicare are the largest contributors to growing debt.
- **These may well be third rails, but they are also the source of the problem.**



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Takeaways

- **Is a recession on the horizon?**
 - Perhaps, but shallow?
 - Many indicators are still in the black.
 - o 2021-Q1 GDP growth was ok!

- **Threats to continued growth:**
 - If inflation starts to rise again, which seems unlikely.
 - Layoff contagion.
 - Broader banking crisis – too much tightening.
 - Borrowing and lending seem to be low and shrinking.
 - Debt ceiling negotiations
 - o Significant cuts to government budgets may well result.

- **Everything changes with a default on the U.S. debt.**



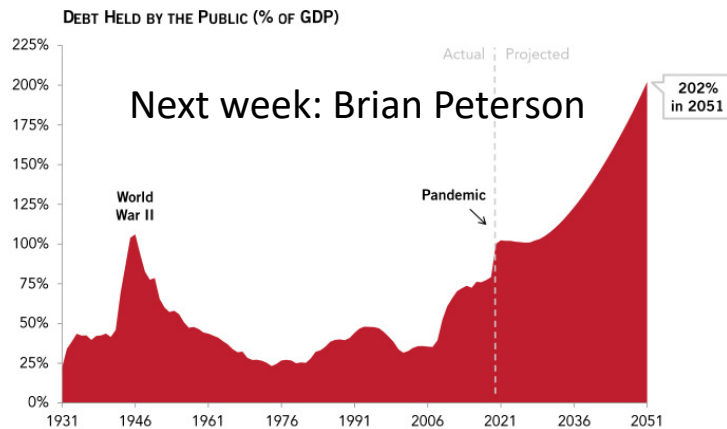
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The Federal Debt is Becoming A Problem



The national debt is on an unsustainable path



SOURCE: Congressional Budget Office, The 2021 Long-Term Budget Outlook, March 2021.
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Thank you!

Any Questions?

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