



Outlook for the Economy in the New Year

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Outlook for 2014

- ▶ Most forecasters expect real GDP growth rate to be above the potential rate in 2014, as:
 - ▶ The drag from fiscal austerity wanes
 - ▶ Consumers regain confidence and increase demand
 - ▶ Housing market solidifies its nascent recovery
 - ▶ I share the view that we can expect 3 percent growth beginning this year
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Overview of My Remarks

- ▶ Improved “tone” to incoming data (and revisions)
 - ▶ Yet, the economy remains far from our 2 percent inflation target and full employment (5.25 percent)
 - ▶ Inflation, both in the U.S. and in many developed countries, is lower than the targets set by central banks
 - ▶ Prolonged unemployment can cause longer-lasting damage to individuals if skills atrophy, but also to families suffering the financial hardship
 - ▶ Prolonged unemployment also impacts the labor market and economy more broadly – possibly even after the recovery is complete
 - ▶ U.S. policymakers should remove monetary accommodation gradually, to minimize the costs and risks of not returning to full employment more quickly
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Figure 1: Payroll Employment Growth: Data and Revisions

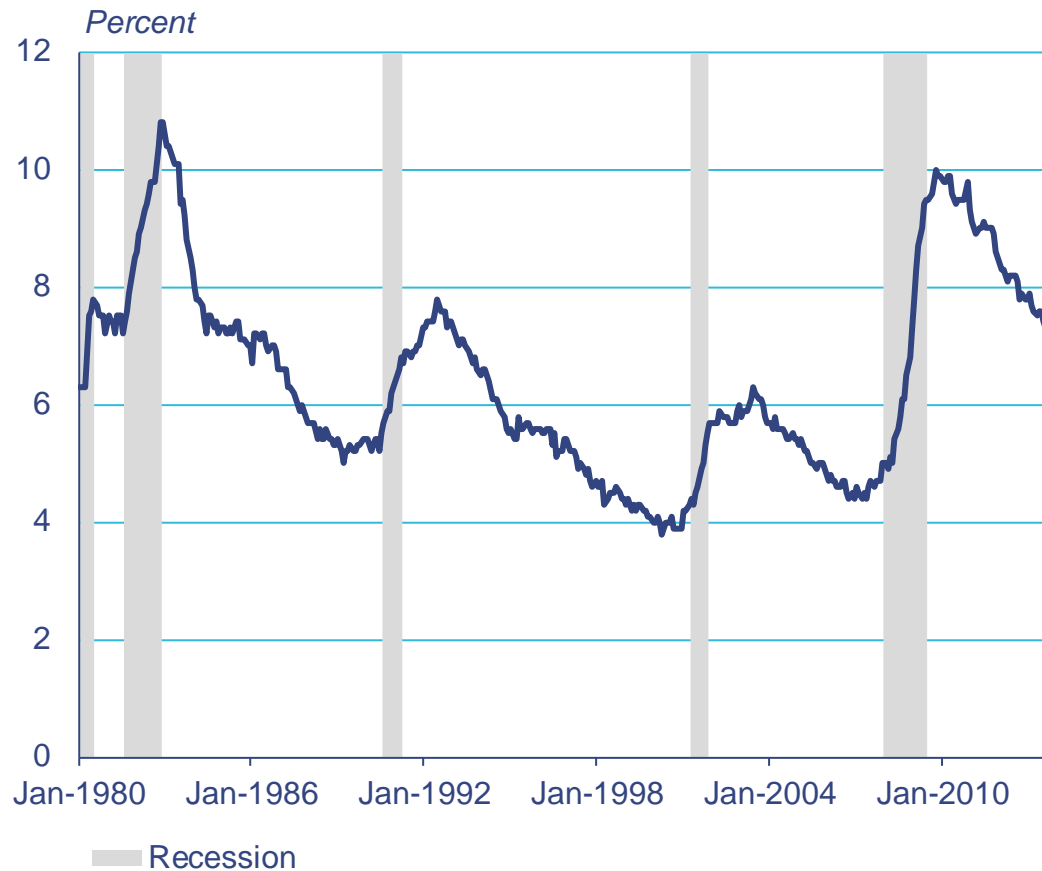
Released July 5, 2013 - December 6, 2013

Payroll Employment Growth in Thousands of Jobs Initial Estimates and Subsequent Revisions						
Month	Release Date					
	5-Jul-13	2-Aug-13	6-Sep-13	22-Oct-13	8-Nov-13	6-Dec-13
Apr-2013	199					
May-2013	195	176				
Jun-2013	195	188	172			
Jul-2013		162	104	89		
Aug-2013			169	193	238	
Sep-2013				148	163	175
Oct-2013					204	200
Nov-2013						203
Three-Month Average	196	175	148	143	202	193

	First Release
	Second Release
	Third Release

Source: BLS, Haver Analytics

Figure 2: Civilian Unemployment Rate January 1980 - November 2013

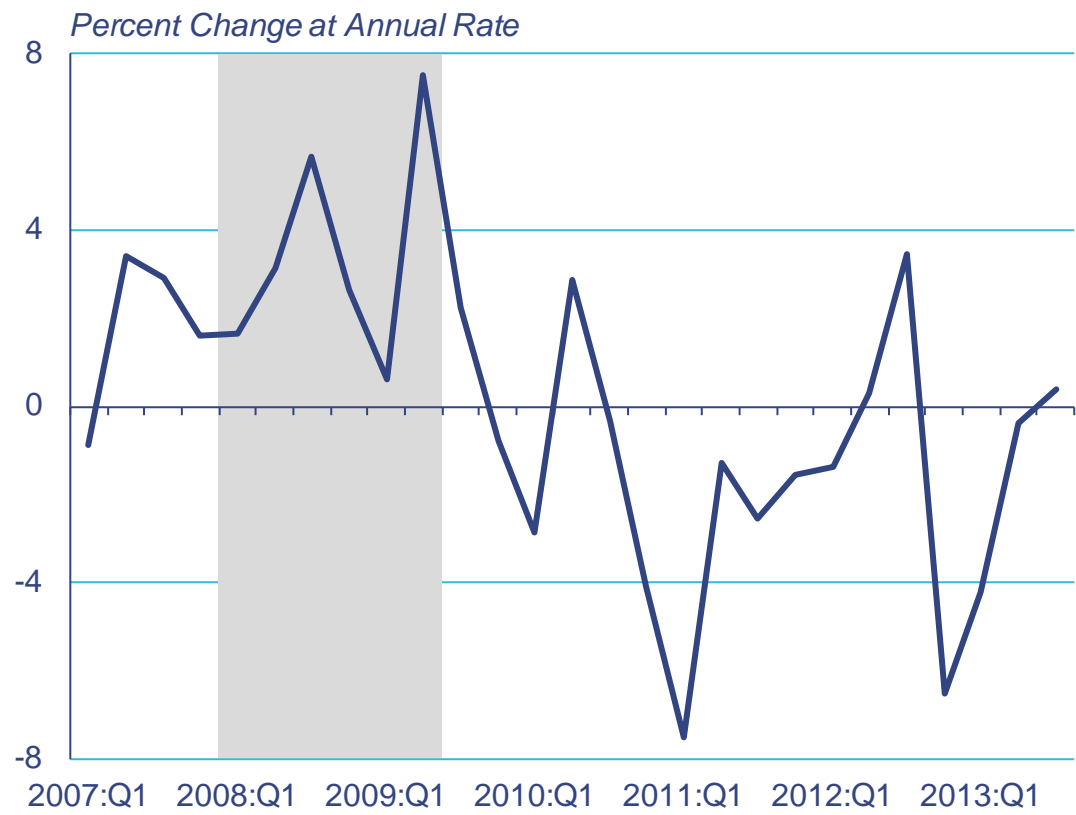


Source: BLS, NBER, Haver Analytics



Figure 3: Growth in Real Government Spending

2007:Q1 - 2013:Q3

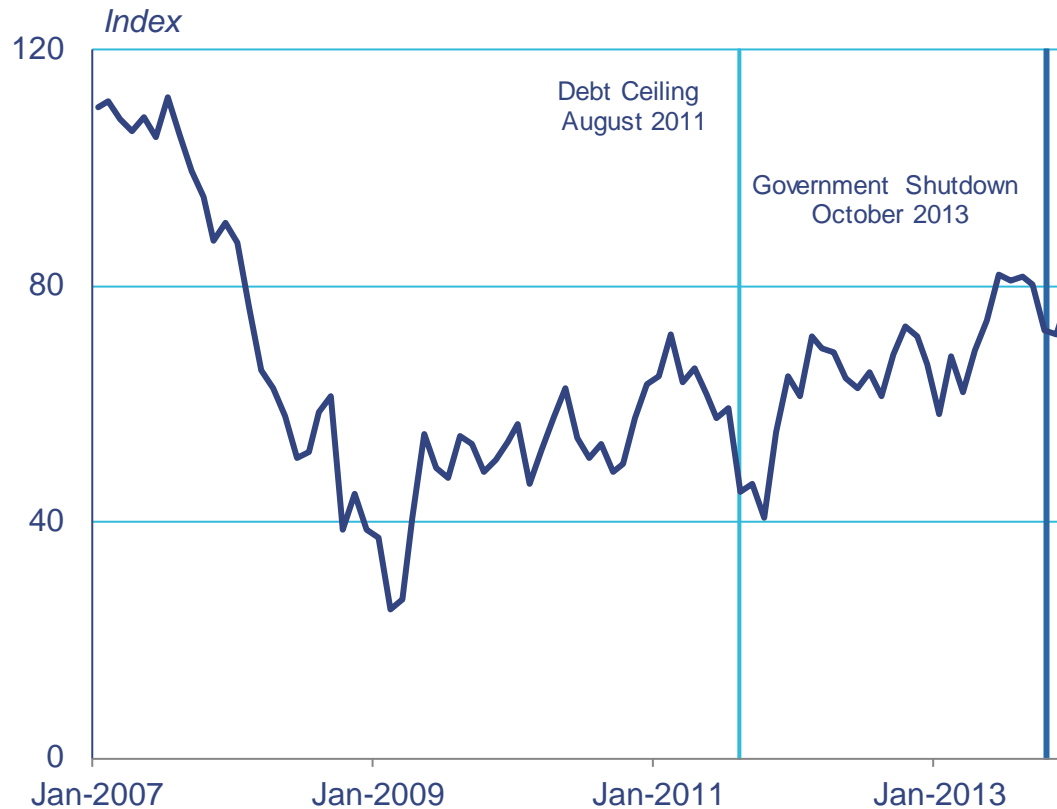


Source: BEA, NBER, Haver Analytics



Figure 4: Consumer Confidence

January 2007 - December 2013



Source: Conference Board, Haver Analytics



Figure 5: Dow Jones 30 Industrials December 31, 2012 - January 3, 2014

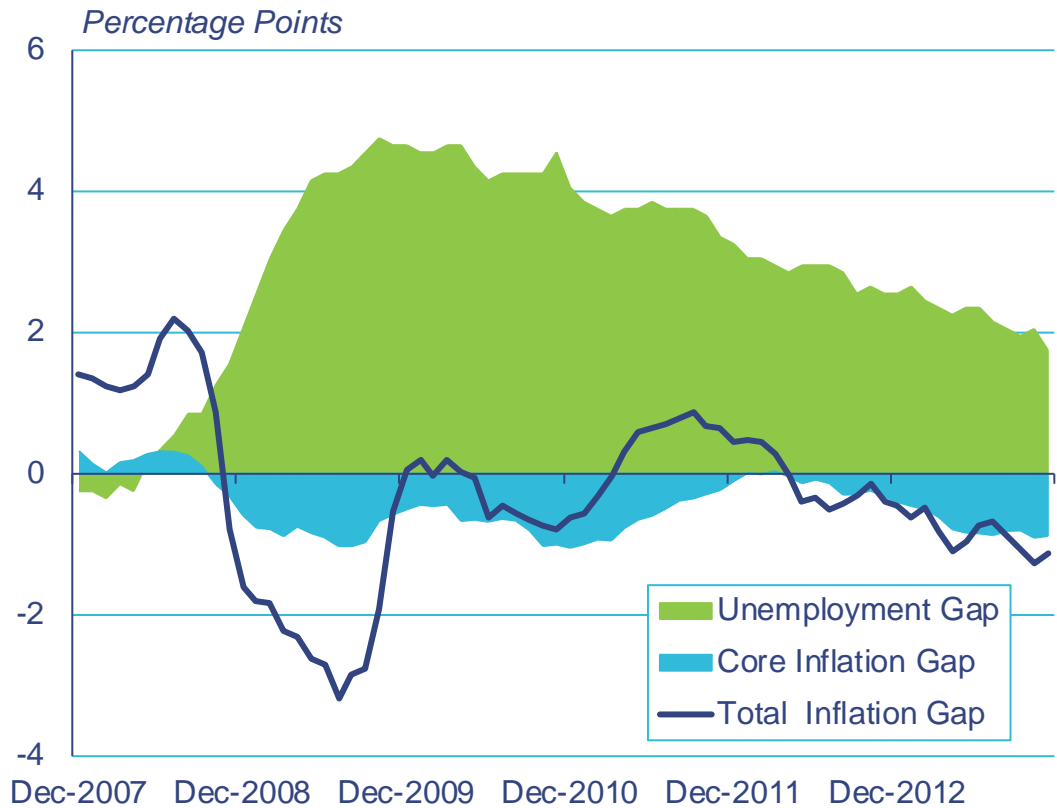


Source: Dow Jones, Haver Analytics



Figure 6: Unemployment and Inflation Gaps

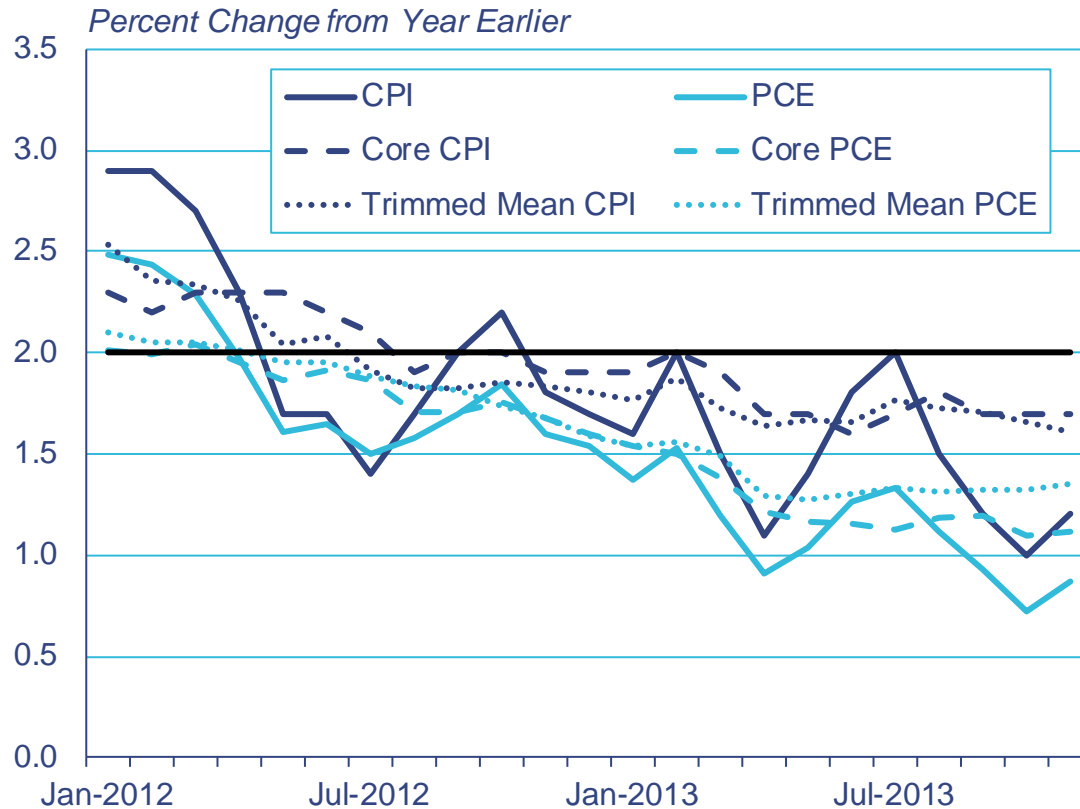
December 2007 - November 2013



Note: Unemployment gap is relative to a 5.25% unemployment rate at full employment. Inflation gaps are relative to a 2% inflation target.

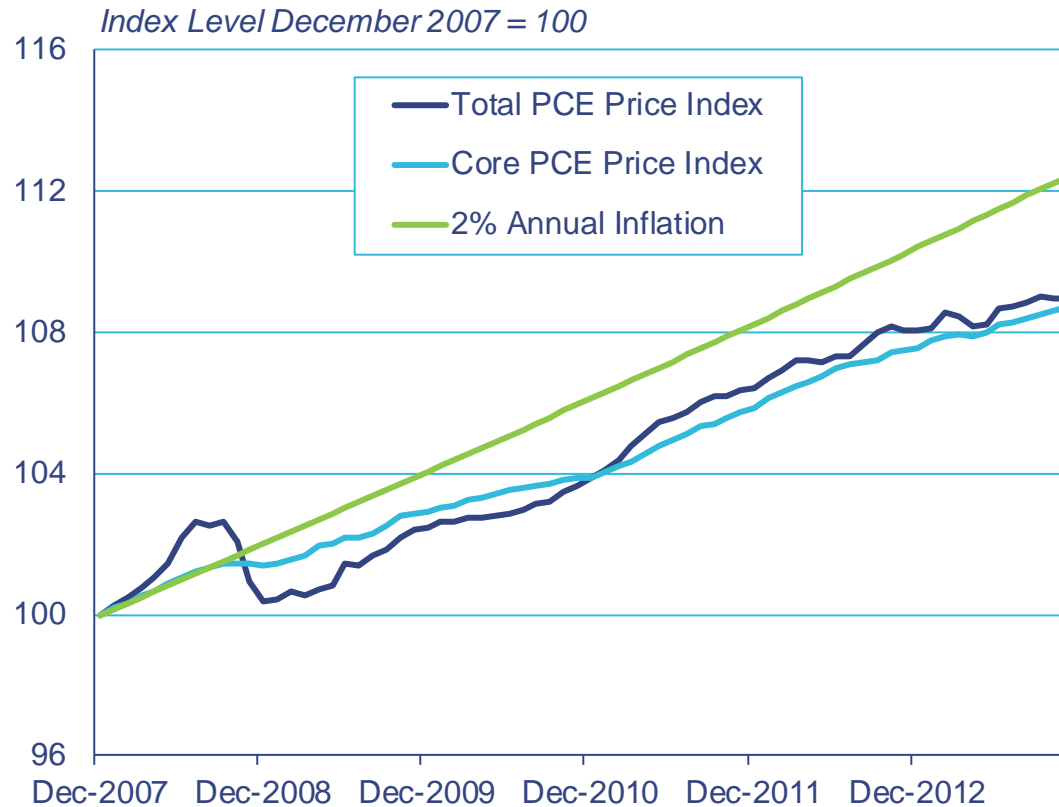
Source: BEA, BLS, Haver Analytics

Figure 7: Measures of Inflation: Changes in Total, Core and Trimmed Mean CPI and PCE Indices January 2012 - November 2013



Source: BEA, BLS, Federal Reserve Bank of Cleveland, Federal Reserve Bank of Dallas, Haver Analytics

Figure 8: Price Level Path: Total and Core Personal Consumption Expenditure (PCE) Price Indices December 2007 - November 2013

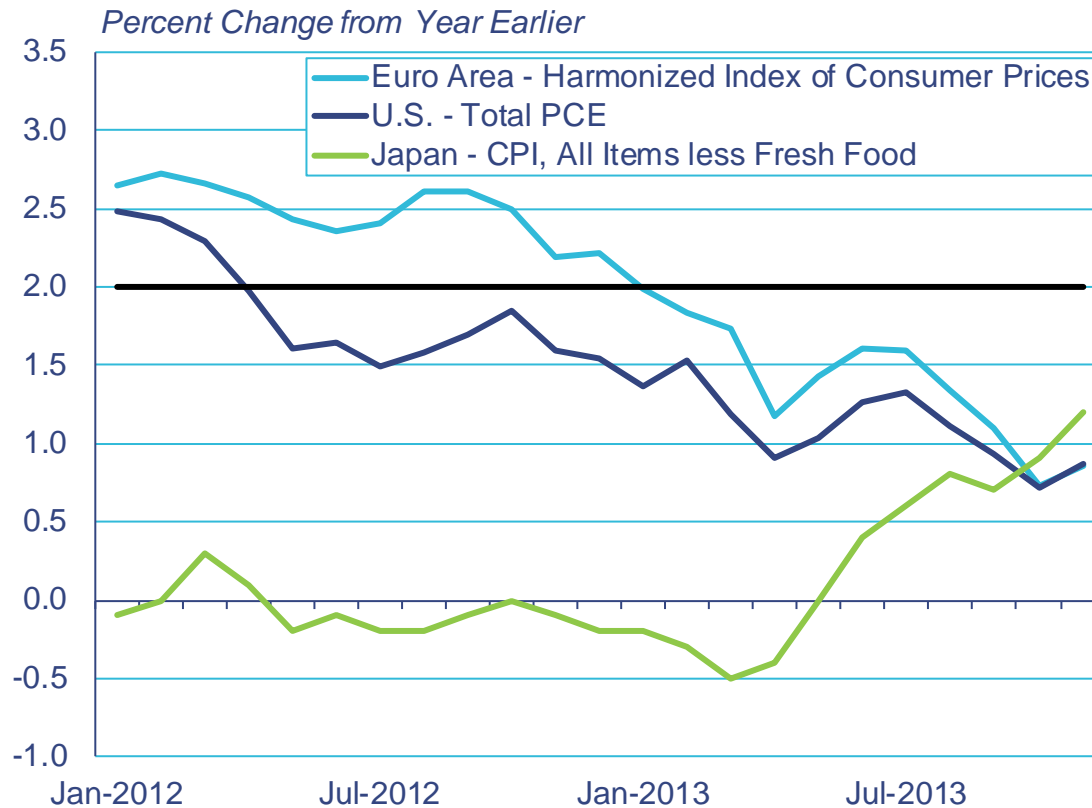


Source: BEA, Haver Analytics



Figure 9: Measures of Inflation Targeted by Central Banks

January 2012 - November 2013



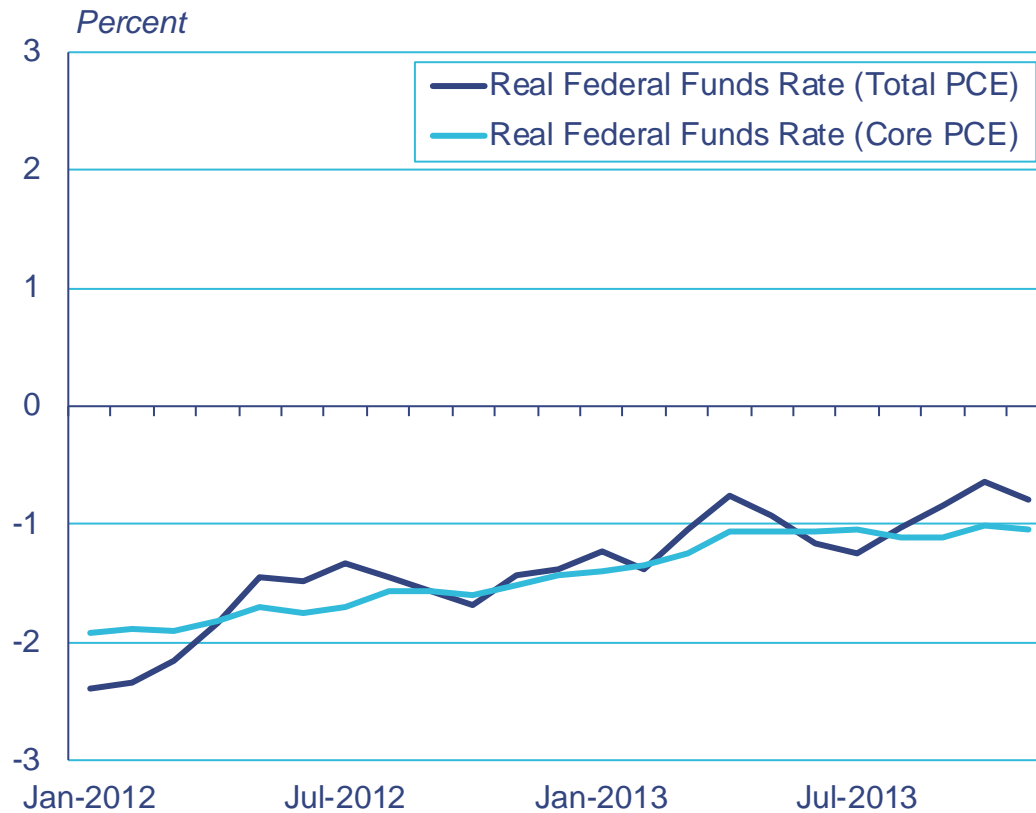
Source: BEA, Eurostat, Japan's Ministry of Internal Affairs and Communications, Haver Analytics

Problems with persistently low inflation rates

- ▶ First, at very low inflation rates, a sizable negative shock to the economy can result in negative inflation – deflation – which can become entrenched in expectations
 - ▶ A second concern with low inflation is that with nominal rates bound at zero, *real* short-term interest rates are determined by the inflation rate and may remain too high
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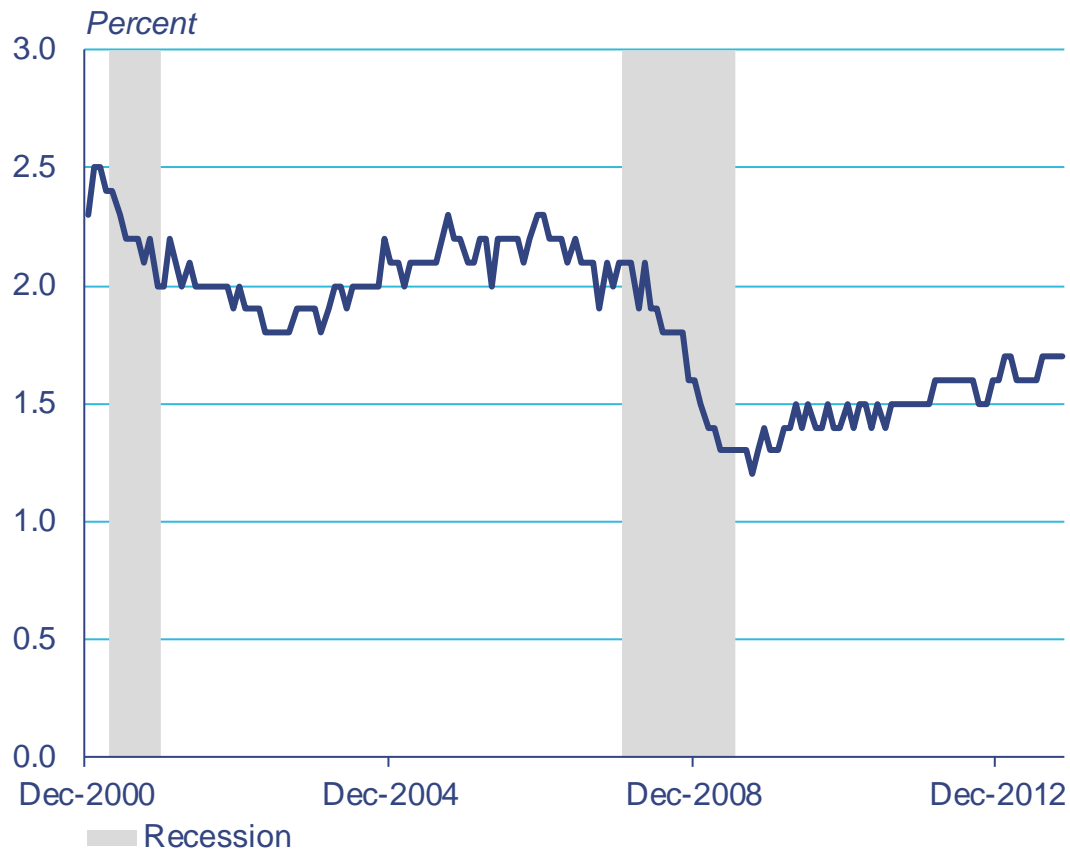
Figure 10: Real Interest Rates January 2012 - November 2013



Source: BEA, Federal Reserve Board, Haver Analytics



Figure 11: Quits Rate December 2000 - October 2013

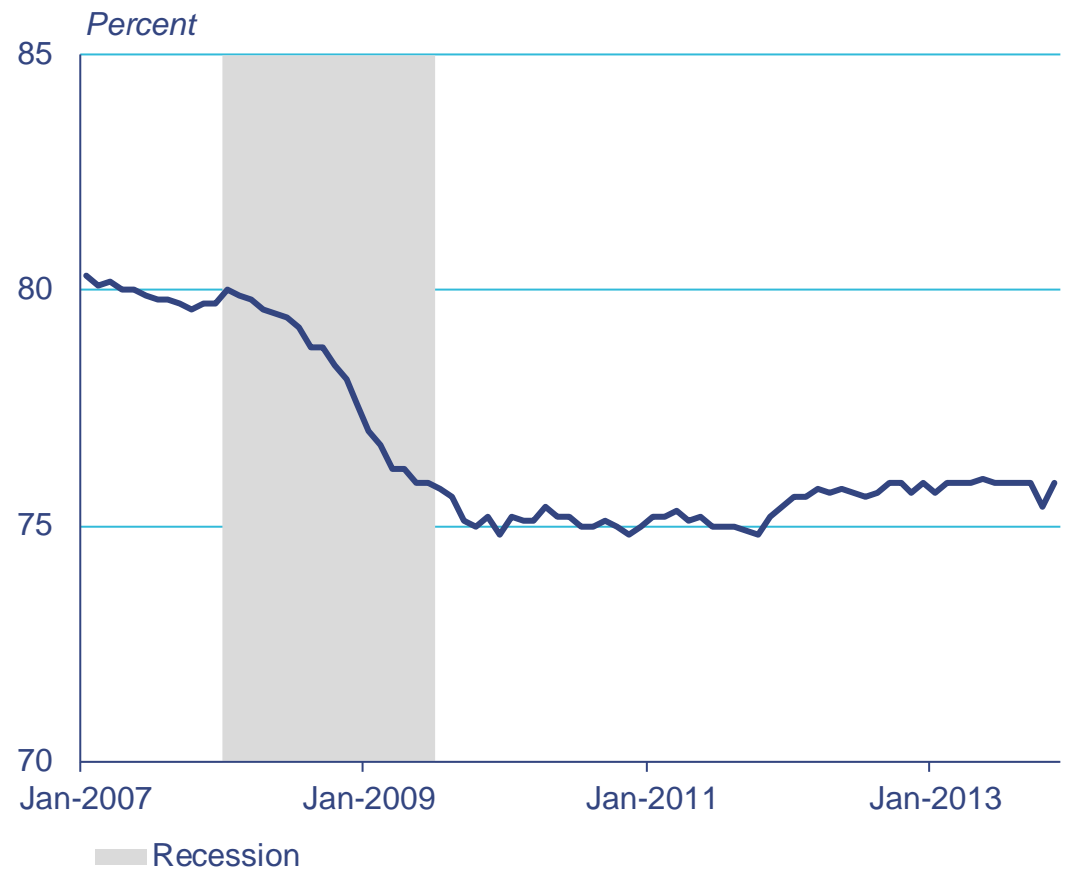


Note: Quits rate is the number of quits during a month as a percent of total employment.

Source: BLS, NBER, Haver Analytics



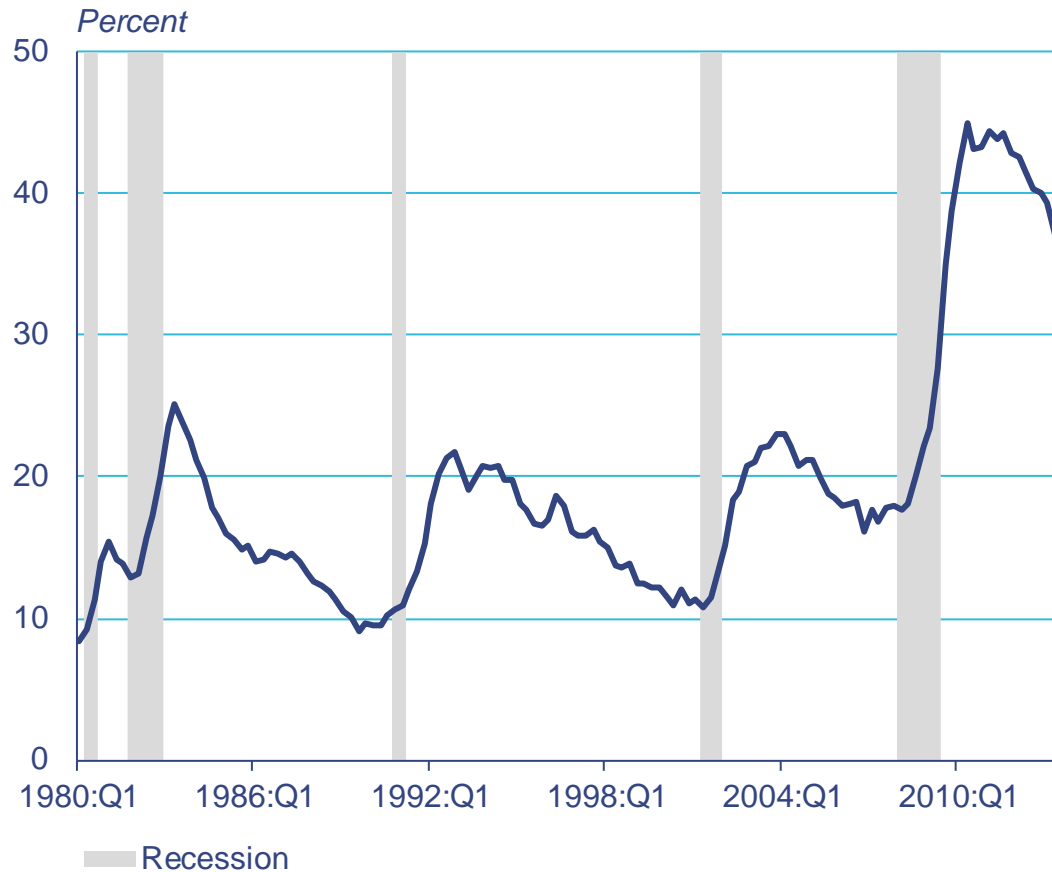
Figure 12: Employment-to-Population Ratio for Individuals Age 25 - 54 January 2007 - November 2013



Source: BLS, NBER, Haver Analytics

Figure 13: Long-Term Unemployment: Percent Unemployed for 27 Weeks or More

1980:Q1 - 2013:Q3



Source: BLS, NBER, Haver Analytics



Still Significant Slack in Labor Markets

- ▶ Implications of a continued slow recovery
 - ▶ Permanent loss of workers from the formal labor force
 - ▶ Skills atrophy and workers despair of a match to existing jobs
 - ▶ Policymakers need to consider the cost of a slow recovery relative to the risk of taking actions that would more quickly return the economy to full employment
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Concluding Observations for Monetary Policy

- ▶ The FOMC reduced purchases of long-term securities from \$85 billion to \$75 billion, but noted:
 - ▶ The removal of accommodation would be gradual
 - ▶ Short-term interest rates were likely to remain at the zero lower bound well past the time the unemployment rate fell below the 6.5 percent unemployment threshold
 - ▶ There are significant costs to a slow recovery, and this one has been too slow
 - ▶ Gradual normalization of support is very appropriate given that the unemployment rate remains high and the inflation rate remains low
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