Economic Outlook for 2012 and 2013

The "Great Recession" ended in June 2009, but the economy expanded by just 2.1% over the past year.

The Chicago Fed National Activity Index 3-month average is near zero.

The liabilities side of the Fed’s balance sheet shows large amount of excess reserves.

The personal savings rate has recently moved lower.

Existing home prices fell by over 30%.
The stock market has improved since March 2009, but remains below previous levels.

The forecast path of the current recovery is relatively muted compared with past deep recession recovery cycles.

After peaking in October 2009, the unemployment rate has fallen by 1.9 percentage points.

Okun’s Law: for every percentage point that GDP growth deviates from its trend – leads to a half percentage change in the unemployment rate in the opposite direction.
The unemployment rate is forecast to edge lower.

Inflation has risen.

Unemployment rate

In large part due to the movement of oil prices. However, adjusted for inflation, current oil prices are below the levels that existed thirty years ago.

Natural gas prices have fallen sharply.

Expenditures on energy are below the historical average.

Removing the volatile food and energy components from the PCE, “core” inflation remains contained.

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Inflation is anticipated to rise 2.2 percent this year and next year.

Industrial output in manufacturing fell quite sharply during the recession, but has risen strongly over the past thirty-four months, averaging 6.5% and has recovered 74.8% of the loss during the recession.

Manufacturing capacity utilization has been rising since June 2009.

The recovery has also been broad-based with primary metals and automotive manufacturing leading the way.

The purchasing managers index remains above 50.
Industrial production is forecast to rise at a solid pace

Light vehicle sales have markedly improved

Increases in new domestic production share has offset losses in Detroit-3 market share

Vehicle sales are expected to improve at a good pace

Housing starts fell to a post WWII low

The forecast calls for a very gradual recovery in housing
Credit spreads between Corporate High Yield securities and Corporate Aaa securities have been edging lower.

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Monetary policy has been very aggressive, keeping the Fed Funds near zero since December 2008.

Fed Funds rate

The Federal Funds Rate is anticipated to remain very low over the forecast horizon.

Target Federal Funds Rate

The asset side of the Fed’s balance sheet has expanded in size and in composition.

Assets of the Federal Reserve

The Fed’s expansion of the monetary base has allowed the money supply to continue rising, compared with what took place during the 1930s.

Monetary expansion 1929-1933

Monetary expansion 2007-current period

Summary

• The outlook is for the U.S. economy to expand at a pace below trend this year and slightly above trend in 2013.
• Employment is expected to rise moderately with the unemployment rate edging lower.
• Slackness in the economy will lead to a relatively contained inflation rate.
• Vehicle sales are anticipated to rise at a good pace.
• Growth in manufacturing output should be solid.