July 15, 2019

ECONOMIC PERSPECTIVES

BREAKING THE RECORD: UNITED STATES ECONOMIC EXPANSION ENTERS ITS ELEVENTH YEAR

Authored by Brian Jones, FHLBNY Financial Economist

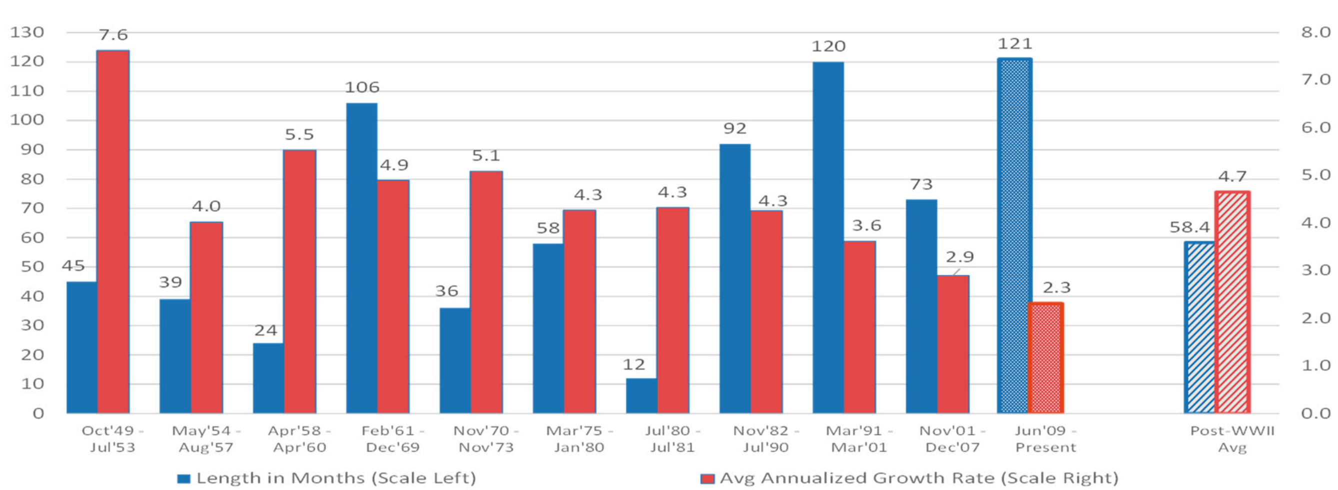
HIGHLIGHTS:

- *Current economic expansion is now the longest in U.S. history, but remains the slowest since WW II*
- *Labor productivity and compensation costs growth weakest of any post-WW II cyclical upturn*
- *Other data compare favorably to those of the previous decade-long expansion*
- *U.S. expansion third longest among developing countries, but still shy of other record holders*
- *Probability of a near-term downturn negligible, inverted yield curve remains a concern further out*
- *Official institutions and private forecasters expect the current upturn to continue through 2021*

CURRENT ECONOMIC EXPANSION IS NOW THE LONGEST IN U.S. HISTORY, BUT REMAINS THE SLOWEST SINCE WW II

Tearing June's page from the calendar, the current business cycle upturn became the longest in our Nation's history. More than double the average 58.4-month duration of prior post-World War II expansions, the recovery from the Great Recession that began in June 2009 has now eclipsed the uninterrupted decade-long period of prosperity enjoyed from March 1991 through March 2001. Yet, despite its impressive longevity, the average pace of real business activity since the spring of 2009 has been the slowest of any expansion over the past 70 years (see Exhibit 1). Indeed, real GDP has grown at an average annualized clip of just 2.3% over the past ten years – less than half the 4.7% mean pace experienced over the course of previous cyclical upturns. While the argument is often made that recoveries from financially centered contractions are often tepid in nature, the data suggest another cause: sluggish productivity growth in the nonfarm business sector.

Exhibit 1: Current Expansion Now the Longest in U.S. History, But Also Slowest Since WW II



Sources: Bureau of Economic Analysis, National Bureau of Economic Research.

LABOR PRODUCTIVITY AND COSTS GROWTH WEAKEST OF ANY POST-WW II CYCLICAL UPTURN

From the end of the financial crisis through the winter of this year, real output per hour worked or labor productivity has risen at an annualized rate of just 1.2%, roughly half the average pace experienced during previous expansions and the weakest performance of the post-World War II period. While total hours worked by nonfarm employees have risen by a subpar 1.7% annualized during the current upturn – compared to a mean 2.5% – that admittedly modest rise in productivity has accounted for roughly 60% of the shortfall in real output (see Exhibit 2, left). To put the importance of productivity growth in perspective, if the current expansion's rate matched the 2.3% annualized recorded over the March 1991 to March 2001 span, real business output would have climbed by 4.0% annualized, just two ticks shy of the earlier lengthy upturn's pace. Slower increases in real business equipment investment and outlays on intellectual property since mid-2009 have been at least partially responsible for the subdued productivity growth recorded during the current expansion. Not surprising given the economy's lackluster productivity performance, both nominal employee compensation and unit labor costs have posted their weakest gains in recorded history (see Exhibit 2, right). The growth of hourly compensation to nonfarm business workers, which has been trending lower since the 9.5% annualized surge at the beginning of the 1980's, has clocked in at a post-World War II low of 2.2% during the current expansion, with unit labor costs edging just 1.0% higher.

Exhibit 2: Productivity, Compensation and Unit Labor Cost Growth All Much Slower Than Previous Expansions
(average annualized percentage change)

Source: Bureau of Labor Statistics.

OTHER DATA COMPARE FAVORABLY TO THOSE OF THE PREVIOUS DECADE-LONG EXPANSION

While real GDP provides a convenient summary measure of economic activity over the course of business cycles, there is a wide array of indicators that provide important information on relative performance across expansions (see Exhibit 3). Comparing the current expansion to the previous decade-long period of prosperity from March 1991 to March 2001 is particularly interesting. The reduction in unemployment insurance claims over the past ten years has been truly stunning. Indeed, since the trough of the Great Recession, the number of new filers has dropped by roughly 373,000 while benefit rolls have contracted by 4.8 million – both hovering near levels last experienced at the end of the 1960s. Nonfarm employers have created 20.3 million jobs since the U.S. economy bottomed in June 2009 – 3.9 million shy of the earlier expansion. The shortfall on employment using the Bureau of Labor Statistics' household survey was a narrower 3.1 million. The 5.8-percentage-point reduction in the civilian unemployment rate to 3.7% eclipsed the decline experienced over the ten years ended March 2001 by a wide margin, but the most recent business-cycle downturn was the most severe since the Great Depression. Although often pointed out as an item of labor-market weakness, the increases in nominal production worker earnings across the two decade-long upturns have been almost identical. Markedly difference inflation performances account for the differences in real wages. A near halving of the core inflation rate over the March 1991 to March 2001 period left the year-to-year growth rate of the Consumer Price Index (CPI) two percentage points lower at the end of that expansion. Significantly smaller reductions in retail energy quotes, combined with a modest acceleration in core goods and services costs, boosted the growth rate of the CPI over the course of the current cycle. In contrast to the declines experienced over the course of the earlier lengthy recovery, interest rates during the current cyclical upturn have been mixed, resulting in a dramatic flattening of the Treasury yield curve. Broad-based equity market indexes have outperformed over this expansion. Changes in the fiscal position of the federal government and the amount of debt held by the public may be the major differences between the two ten-year spans.

Exhibit 3: Comparing the Performances of the Two Decade-Long Expansions

	Mar-91	Mar-01	Change	Jun-09	Jun-19	Change
Labor Market Indicators:						
Initial Jobless Claims	498,918	387,480	-111,438	595,518	222,094	-373,424
Continuing Jobless Claims	3,431,394	2,588,746	-842,648	6,496,330	1,682,897	-4,813,433
Nonfarm Payrolls (thousands)	108,576	132,761	24,185	131,026	151,308	20,282
Civilian Population	190,381	214,305	23,924	235,655	259,037	23,382
Civilian Labor Force	126,238	143,924	17,686	154,716	162,981	8,265
Household Employment	117,652	137,783	20,131	140,009	157,005	16,996
Unemployment	8,586	6,141	-2,445	14,707	5,975	-8,732
Unemployment Rate U-3	6.8%	4.3%	-2.5%	9.5%	3.7%	-5.8%
Labor Force Participation Rate	66.3%	67.2%	0.9%	65.7%	62.9%	-2.8%
Production Worker Earnings (yr/yr)	3.0%	4.2%	1.2%	2.5%	4.0%	1.5%
Real Production Worker Earnings	-1.6%	1.3%	2.9%	4.7%	1.6%	-3.1%
Inflation Indicators:						
Consumer Price Index (yr/yr)	4.9%	2.9%	-2.0%	-1.4%	1.8%	3.2%
Excl Food & Energy	5.2%	2.7%	-2.5%	1.7%	2.0%	0.3%
Food	3.3%	3.1%	-0.2%	2.1%	2.0%	-0.1%
Energy	4.4%	6.0%	1.6%	-22.5%	-0.5%	22.0%
PCE Chain Price Index	3.7%	2.0%	-1.7%	-0.8%	1.5%	2.3%
Excl Food & Energy	3.7%	1.8%	-1.9%	1.0%	1.6%	0.6%

	Mar-91	Mar-01	Change	Jun-09	Jun-19	Change
Financial Indicators:						
Federal Funds Rate	6.12%	5.31%	-0.81%	0.21%	2.38%	2.17%
Three-Month Treasury Bill	6.09	4.54	-1.55	0.18	2.22	2.04
Two-Year Treasury Note	7.10	4.34	-2.76	1.18	1.81	0.63
Ten-Year Treasury Note	8.11	4.89	-3.22	3.72	2.07	-1.65
Slope of Treasury Yield Curve (10-yr - 3-mo)	1.01	0.55	-0.46	2.54	0.26	-2.28
Dow Jones Industrial Average	2,913.9	9,878.8	239.0%	8,447.0	26,600.0	214.9%
S&P 500	375.2	1,160.3	209.2%	919.3	2,941.8	220.0%
NASDAQ	482.3	1,840.3	281.6%	1,835.0	8,006.2	336.3%
	1990	2000	Change	2009	2019 e	Change
Federal Government Finances:						
Budget Deficit or Surplus ($ billions)	-221.0	236.2	457.2	-1,412.7	-896.0	516.7
As a Percentage of Nominal GDP	-3.7	2.3	6.0	-9.8	-4.2	5.6
Debt Held by the Public ($ billions)*	2,412	3,410	998	7,545	16,621	9,076
As a Percentage of Nominal GDP*	40.9	33.7	-7.2	52.3	78.2	25.9

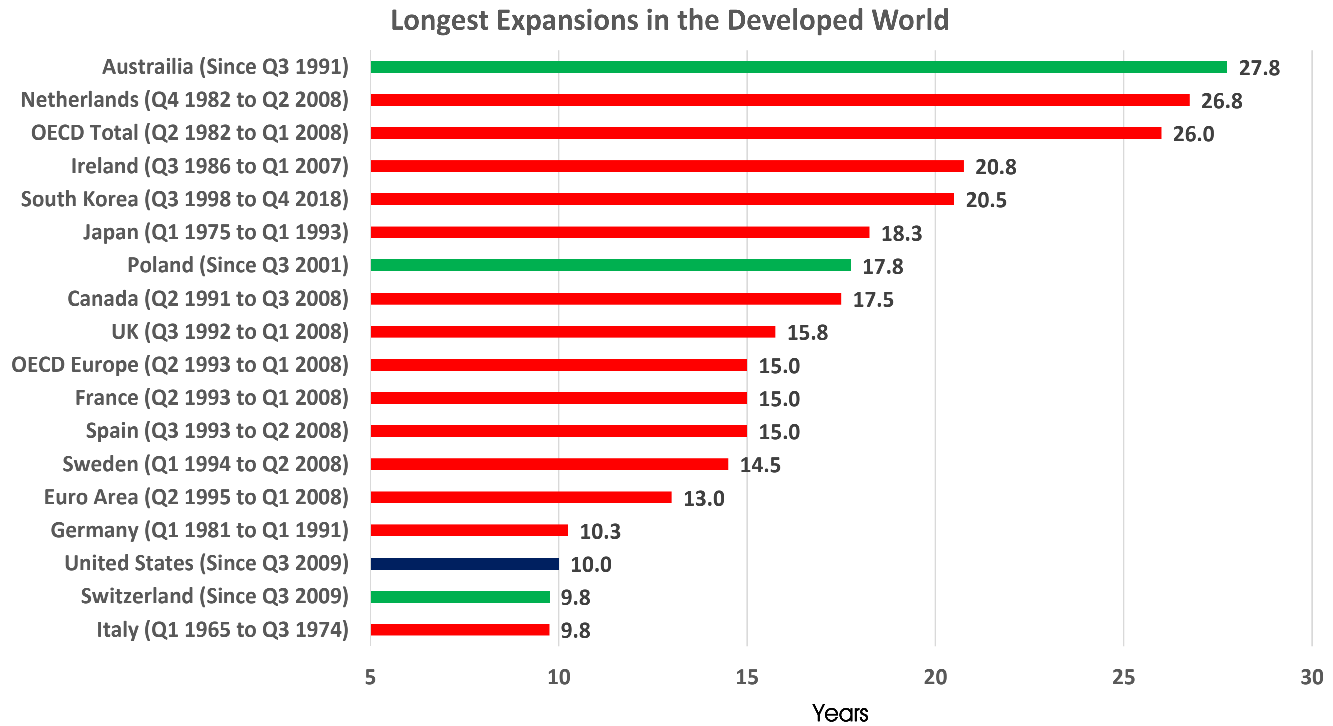
* End of Fiscal Year

Sources: Congressional Budget Office, Federal Reserve Board, Nasdaq Inc., S&P Dow Jones and the U.S. Department of Labor.

U.S. EXPANSION THIRD LONGEST AMONG DEVELOPING COUNTRIES, BUT STILL SHY OF OTHER RECORD HOLDERS

Entering its eleventh year, the U.S. expansion is now the third longest ongoing cyclical upturn in the developed world, eclipsed only by those of Australia and Poland at 28 and 18 years, respectively (see Exhibit 4). While impressive historically, the current period of prosperity still has considerable ground to make up before seriously challenging other record holders – the vast majority of which terminated in the wake of the 2007 financial crisis. While economic expansions do not necessarily die of old age, prudent fiscal and monetary policy choices will be necessary to keep the good times rolling.

Exhibit 4: U.S. Cyclical Upturn Has a Very Long Way to Go to Match Other Developed Country Record Holders

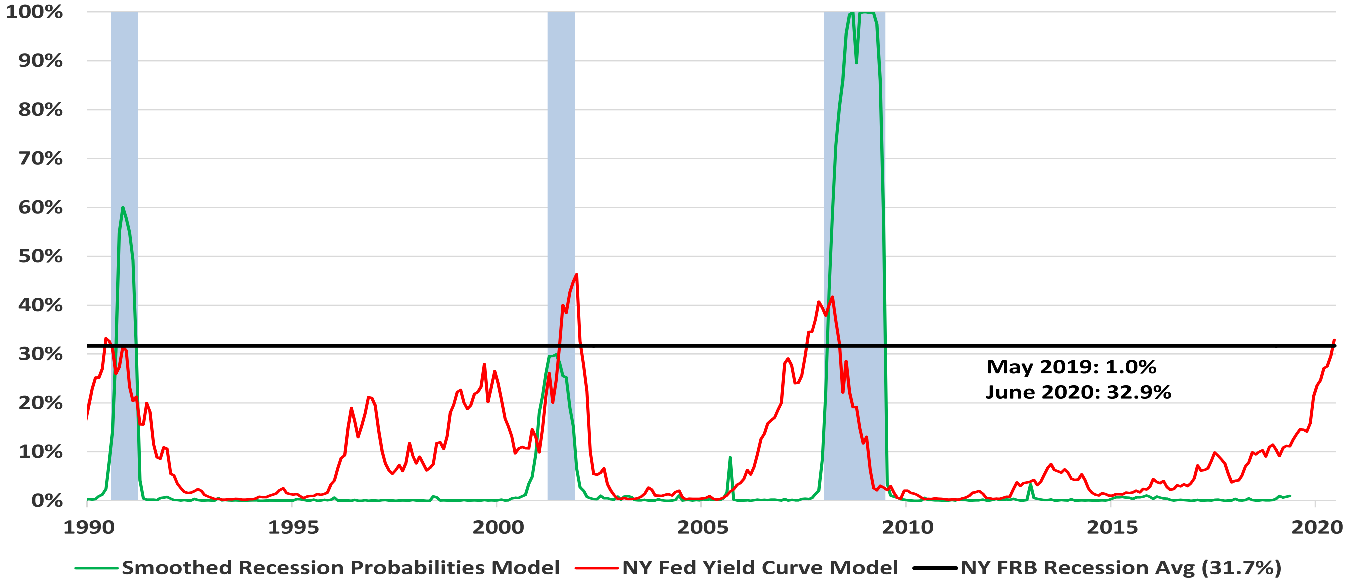


Sources: Bureau of Economic Analysis, Organization for Economic Co-operation and Development.

PROBABILITY OF A NEAR-TERM DOWNTURN NEGLIGIBLE, INVERTED YIELD CURVE REMAINS A CONCERN FURTHER OUT

Available information suggests that the current expansion will move deeper onto record territory in coming months. The smoothed U.S. recession probabilities model maintained by Professor Jeremy Piger of the University of Oregon, which relies on nonfarm payrolls, industrial production, real personal income excluding transfer payments, and real manufacturing and trade sales – series considered by the National Bureau of Economic Research in determining business cycle turning points – placed the probability that the U.S. economy was in recession in May at just 1.0%. Moreover, Federal Reserve Bank tracking estimates for the spring quarter are currently centered at 1.9%. While down from the 3.1% first-quarter clip, the estimate likely masks a marked pickup in the pace of real domestic demand. Of more concern is the continuing inversion of the Treasury yield curve. Based on the bond-equivalent interest-rate spread between the Treasury's ten-year note and three-month bill, the Federal Reserve Bank of New York put the chances that the economy will be in a business-cycle downturn in June 2020 at 32.9%, up from the prior month's 29.6% reading, and above the average 31.7% prevailing immediately before the last three cyclical downturns (see Exhibit 5). Assuming that the Federal Open Market Committee embarks on a series of reductions to the federal funds rate target range, the probability of a recession 12 months out should soon reverse.

Exhibit 5: Probability That U.S. is Currently in Recession Negligible, But Slope of Yield Curve Remains a Concern

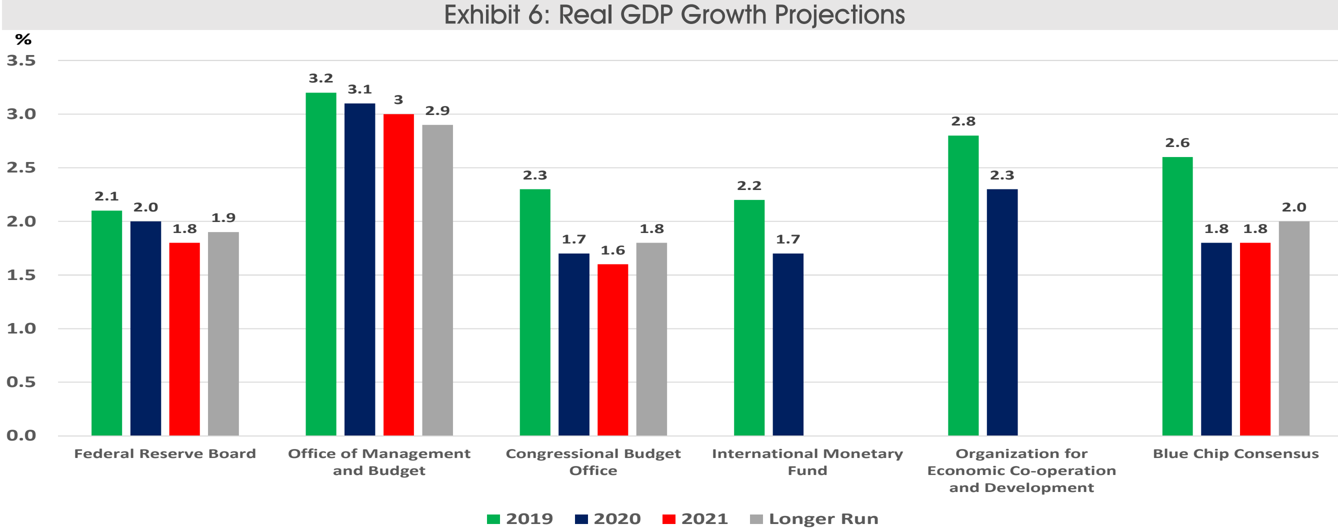


Note: Shaded areas denote recessions. Sources: Federal Reserve Banks of New York and St. Louis, National Bureau of Economic Research.

OFFICIAL INSTITUTIONS AND PRIVATE FORECASTERS EXPECT THE CURRENT UPTURN TO CONTINUE THROUGH 2021

Looking out over the next two and half years, domestic official institutions, international organizations and private-sector firms generally anticipate a gradual deceleration to trend growth, with none calling for a recession (see Exhibit 6). If those projections prove correct, the current expansion would soon be on the verge of challenging the length of those experienced by European nations before the Great Recession.

Exhibit 6: Real GDP Growth Projections



Sources: Congressional Budget Office, Federal Reserve Board, International Monetary Fund, Organization for Economic Co-operation and Development, and the Office of Management and Budget.

QUESTIONS / COMMENTS?

The *Economic Perspectives* newsletter is authored by the FHLBNY's Financial Economist, Brian Jones. Contact your Relationship Manager at **(212) 441-6700** to discuss the information shared in this newsletter and any potential business opportunities with the FHLBNY as your partner.

The Federal Home Loan Bank of New York ("FHLBNY") is providing this report for informational purposes only. This report should not be construed as an opinion, recommendation, or solicitation regarding the use of any financial strategy and/or the purchase or sale of any financial instrument. The recipients of this report are advised to conduct their own independent due diligence and consult with financial advisors, accountants, and attorneys before making any investment, credit, or any other financial decisions. FHLBNY does not warrant the completeness or accuracy of this report. The past performance of any FHLBNY service or product should not be viewed as a guarantee of future results. The information contained in this report, as well as the services and products provided by the FHLBNY, may change at any time without notice.