

Northwood University's Monthly Economic Outlook

January 2014

Introduction

The Brookings Institute recently released a study pointing out that over the next 5 years the bottom twenty percent of American income earners would realize a 6 percent increase in their standard of living due to subsidies from the Affordable Care Act. The study also notes that these benefits will come from higher tax burdens on the upper eighty percent of Americans. According to the Bureau of Economic Analysis (BEA), the first estimate of GDP for the fourth quarter of 2013 shows that the U.S. economy grew at 3.2 percent while annual U.S. GDP came in at a disappointing 1.9 percent for the year. Fourth quarter 2013 GDP saw growth in personal consumption expenditures and was offset by lower federal government spending and an increase in imports. Some of the headwinds that have been holding back the U.S recovery--including financially strained households and restrictive government tax and spending policies---appear to be continuing in 2014. The Federal Reserve Bank's forecast of growth at 3 percent in 2014 and above 3 percent in 2015 seems overly optimistic at this time. In his State of the Union address, President Obama suggested several new policies including raising the minimum wage, creating a new tax-free savings bond and higher taxes which would create more uncertainty in the economy.

Key December/January Data

Positive and Negative Signs

With unemployment at 6.6 percent in January, total non-farm payroll employment edged up a disappointing 113,000. Employment rose mainly in retail and wholesale trade but was down in information services. The January hiring level, slightly better than 74,000 jobs created in December, was substantially below the

178,000 monthly hiring rate averages of the last 6 months and the 187,000 monthly averages over the past year. Consumer confidence beat economists' expectations with an increase to 80.7 in January, a sign of optimism for the economy. Eurostat estimates show the Euro Area seasonally-adjusted unemployment rate at 12 percent in December 2013 while the inflation rate decreased to 0.7 percent. The Conference Board's Leading Economic Index (LEI) for the Euro Area increased 0.6 percent in December marking the seventh consecutive month of growth, signaling a promising outlook for the year. The LEI for China increased 0.4 percent making it the lowest monthly gain in 9 months with expectations of continued slowing growth. The U.S. LEI increased 0.1 percent in December but consumer expectations for business conditions forecast uncertainty. According to The National Association of Realtors, the Pending Home Sales Index dropped 8.7 percent in December, marking the lowest level since October 2011. This could be due to harsh weather conditions. The fixed mortgage interest rate average dropped to 4.39 percent with concern as to how rates will be affected if the Federal Reserve continues its 'tapering' policy. According to the Manufacturing ISM Report on Business, the Purchasing Manufacturing Index of the U.S. economy ended 2013 at 57, the second highest reading for the year, but durable goods fell by 4.3 percent in December due to weak demand. This is the largest decline since July of 2013 and effectively negating November's 2.6 percent rise. Auto sales were impressive, up 15.6 million, an increase of about 8 percent from 2012. For January the Dow Jones Industrial Average decreased 5.30 percent, while the NASDAQ decreased at 1.74 percent, and the S&P 500 decreased at 0.65 percent. The price of oil was down 1.27 percent from December while gold and silver increased 3.8 percent and 1.14 percent respectively.

Current Issues

“A Tale of Two Measurements”

“It is the best of times, it is the worst of times”...a play on the opening words from Charles Dickens, A Tale of Two Cities seems appropriate when considering the “U.S. Federal Budget Deficit” relative to the “U.S. National Debt”. It is good to see that the Federal Budget Deficit (our annual deficit) for the last fiscal year ending September 30, 2013 declined to \$680 billion which was 4.1 percent of U.S. GDP down 37 percent from 2012 levels. It is also important to note that the Federal Budget Deficit is heading in the right direction even though thoughtful people can differ on the size and pace of the decline. President Obama is correct when he argues that the most recent deficit is a vast improvement over the 2009 deficit which was more than 10 percent of annual GDP and is rather low by recent historical standards. However, the President, Congress and many in Washington fail to see that the “Annual National Deficit” can be dealt with in the short term while the national debt is growing in size and scope and becoming much more problematic in both the short term and the long term.

Once again it is important to state that a declining annual federal deficit is good, however these deficits continue to add to a dangerously high U.S. national debt. The current national debt of the United States is \$17.3 trillion or just over 100 percent of current U.S. GDP and growing. What most Americans do not realize is the cumulative national debt of the United States from 1776 to 1980 totaled \$907 billion with average U.S. per capita debt at \$3,995 and per capita debt per family of four at \$15,979. Today, the cumulative U.S. national debt has increased 1808 percent with per capita U.S. national debt at \$54,569 and national debt for a family of four at \$218,276. The U.S. national debt has increased rather dramatically over this period, while Americans ability to pay for it has lagged behind. Average U.S. household nominal income has only increased 203 percent since 1980 with inflation adjusted income increasing just under 9 percent over the same period. It is also important to note that one of the

broadest measures of growth and wealth in our economy is the Standard & Poors 500 Stock Index. The Standard & Poors Index is up less than 1500 percent since September of 1980, clearly lagging behind growth and government debt.

Another concern is the breakdown in the composition of who owns the U.S. National Debt. The broadest breakdown shows Social Security funds own 16 percent, other government programs and agencies own 13 percent, the Federal Reserve owns 12 percent, foreign governments own 34 percent, with China and Japan owning 8 and 7 percent respectively, state and local governments own 3 percent, mutual funds own 6 percent, and more than 280 other groups own the remaining 17 percent. Are foreign governments gaining undue influence over American policy via ownership of our debt?

Finally, the government paid out roughly \$420.6 billion in interest over the last fiscal year including interest credited to Social Security and other trust funds. The net interest payment on the debt totaled just under \$223 billion or 6.23 percent of all federal outlays. Of great concern is the fact that in 2013 the average interest rate on U.S. government debt was only 2.43 percent versus 6.63 percent in 2000. Imagine what the interest payment on the national debt will be if and when the U.S. economy recovers and interest rates rise?

Contact Us

Comments or questions should be directed to Dr. Timothy G. Nash at: tgnash@northwood.edu or (989) 837-4323. Dr. Nash was assisted in writing this issue by Northwood students David Valentine and Josh Campbell. To view Northwood University’s Monthly Economic Outlook Newsletters from previous months, please visit: <http://www.northwood.edu/media/publications/>. For more information about Northwood University visit www.northwood.edu.

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