

Prospects and Policies for the US economy

Michalis Nikiforos

Université de Genève
Levy Economics Institute

joint work with D. Papadimitriou, G. Yajima and G. Zezza

May 4, 2023

presentation prepared for the 30th Annual Levy Economics Institute Conference, May 4, 2023

The recovery

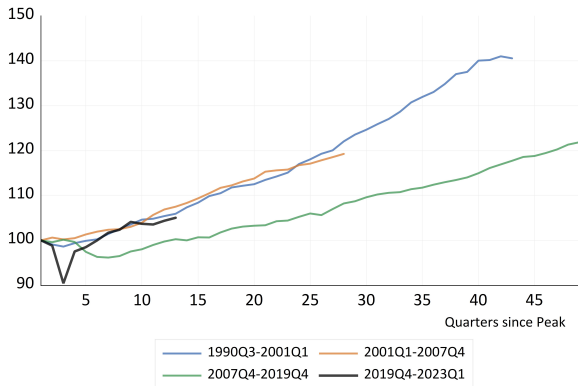


Figure: Recoveries of Real GDP in the Previous Four Cycles (peak=100)

The recovery

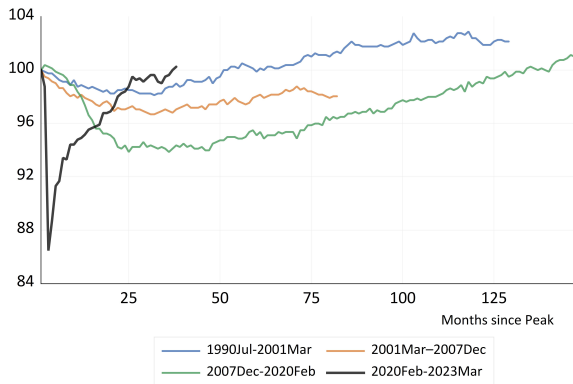


Figure: Recoveries of Employment-Population Ratio (25-54 Yrs) in the Previous Four Cycles (peak=100)

The recovery

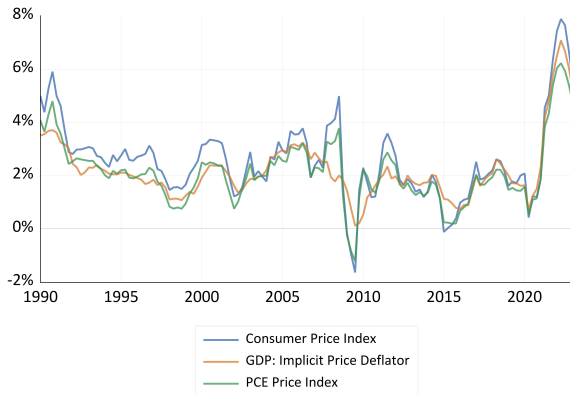


Figure: Inflation rate (percentage change from a year ago)

The recovery

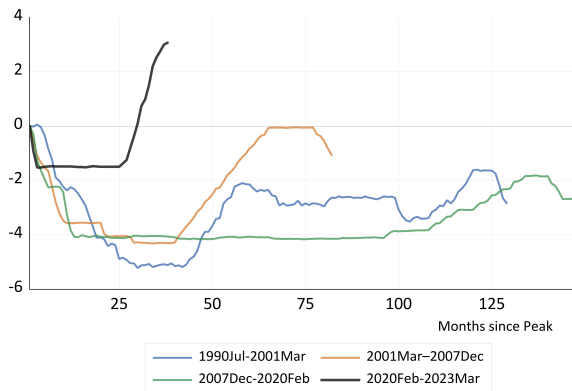


Figure: Trajectory of the Federal Funds Effective Rate in the Previous Four Cycles (difference from peak)

A (mini?) financial crisis

- Collapse of SVB and Signature Bank in March; First Republic this weekend
- Resolution:
 - 1 SVB and Signature were declared a systemic risk to the financial system
 - 2 Establishment of Bank Term Funding Program (BTFP)
 - 1 Loans of up to one year to banks that pledged collateral
 - 2 Turbocharged QE: collateral will be valued at par
- Contradictory monetary policy policy: increasing/high interest rates combined with a new round of QE

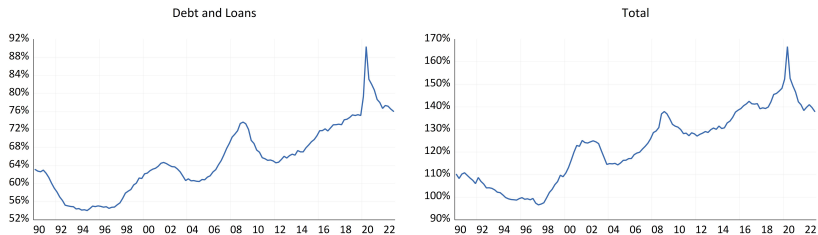


Figure: Non financial business, liabilities-to-GDP ratio 1990-2022

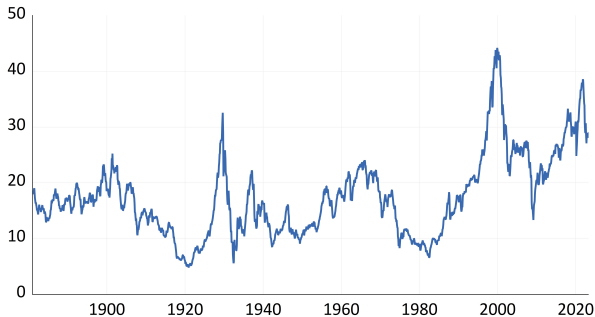


Figure: Shiller cyclically adjusted price-to-earnings ratio (1881Jan-2023Apr)

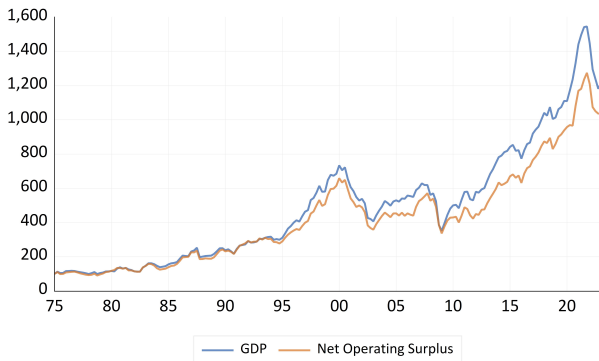


Figure: Ratio of Market Capitalization to GDP and Net Operating Surplus, 1975Q1–2023Q1 (1975Q1=100)

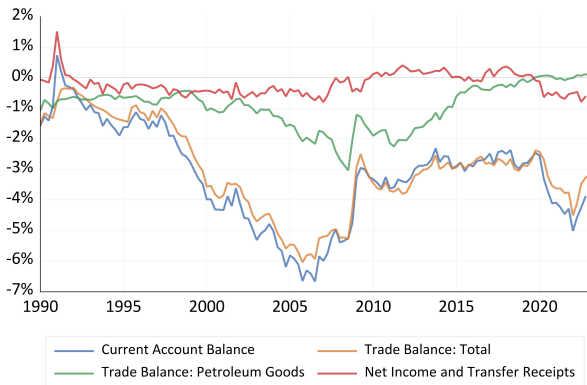


Figure: Current Account Balance and its Components (% GDP)

Baseline

- Builds on the CBO's *The Budget and Economic Outlook: 2023–2033* (published in February 2023)
- Examines the conditions necessary for these projections to materialize.
- Assumptions as neutral as possible

Year	Deficit	Outlays	Revenues	Growth Rate
2022	5.2	24.8	19.6	1.9
2023	5.3	23.7	18.3	0.3
2024	6.1	23.8	17.7	1.8
2025	6.1	23.5	17.4	2.7
2026	5.7	23.5	17.7	2.4

Note: Deficit, Outlays and Revenues as percentage of GDP

Table: CBO baseline projections, 2023-2026

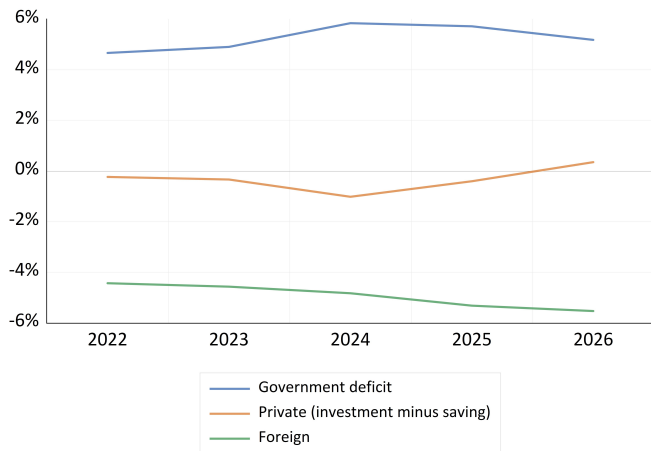


Figure: Baseline Scenario: Main Sector Balances, Actual and Projected (2022–26)

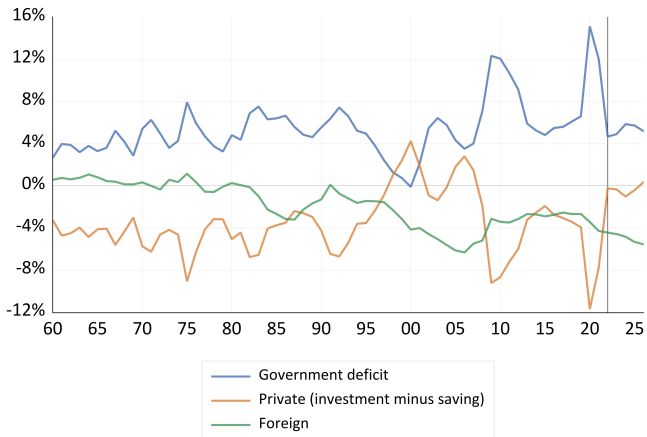


Figure: Baseline Scenario: Main Sector Balances, Actual and Projected (1960–2026)

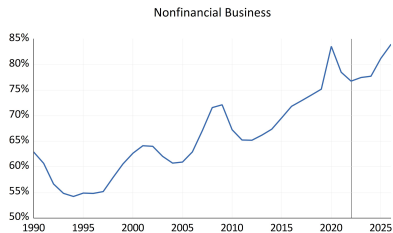
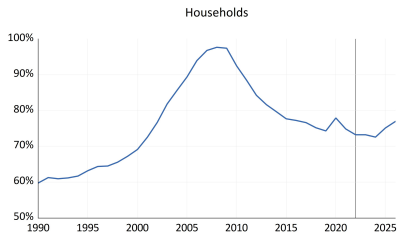


Figure: Private Sector Indebtedness (%GDP), 1990-2026

Financial fragility

The United States are facing a situation with:

- ① Historically high business indebtedness
- ② Overvalued financial asset prices
- ③ High/increasing interest rates
- ④ Credit contraction
- ⑤ Economic slowdown

Financial fragility

To evaluate the potential implications of this situation we simulate a scenario that assumes:

- 1 a further fall in the stock market
 - ▶ SP500 converges to 3000 by the first quarter of 2024
- 2 a decrease in the spending by households and firms

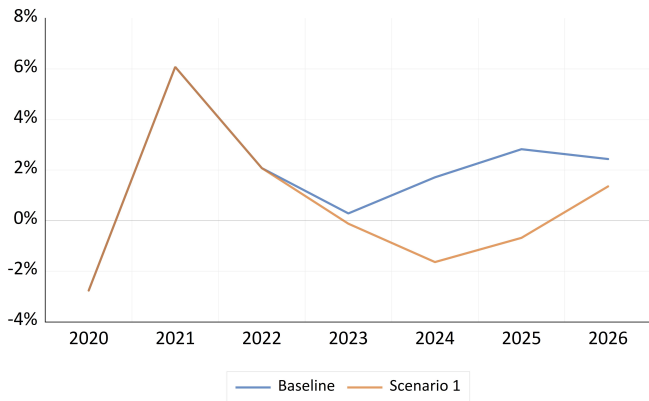


Figure: Real GDP growth rate; Baseline scenario and Scenario 1

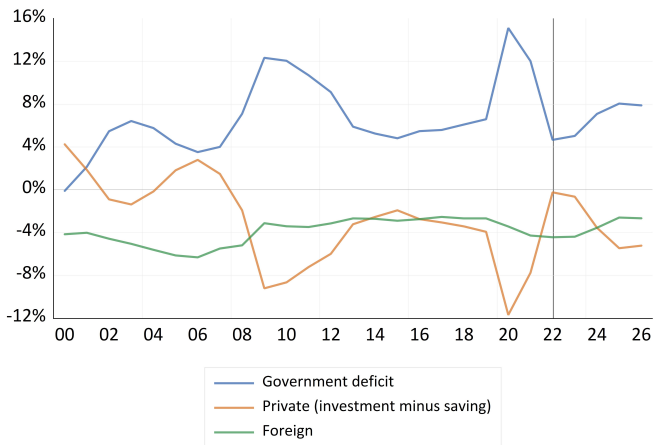


Figure: Scenario 1: Main Sector Balances, Actual and Projected (2000–2026)

Fiscal expansion

There are three interrelated reasons for fiscal expansion:

- ① Improvement of infrastructure of the US economy
- ② As part of an industrial policy plan
- ③ As means towards ecological transition

We simulate the *demand* effects of such a policy in a scenario

- Assumption: 1% GDP increase in government expenditure

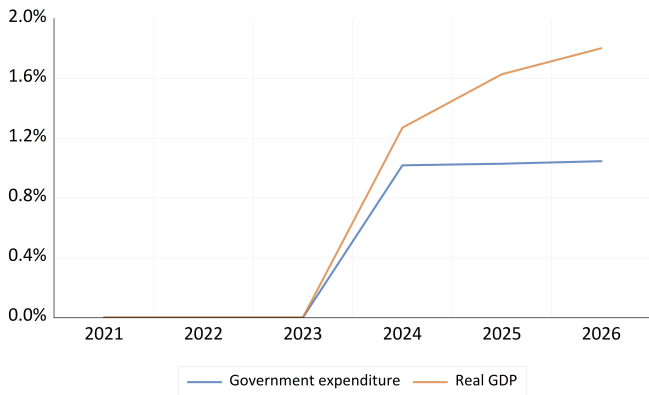


Figure: Scenario 2: Real government expenditure and GDP (% GDP in the baseline)