Our American States | An NCSL Podcast

The Our American States podcast—produced by the National Conference of State Legislatures—is where you hear compelling conversations that tell the story of America's state legislatures, the people in them, the politics that compel them, and the important work of democracy.

You can subscribe through iTunes or Google Play.

Economy: Beth Ann Bovino | Episode 9 | May 11, 2017

Welcome to Our American States, a podcast of meaningful conversations that tell the story of America's state legislatures, the people in them, the politics that compel them, and the important work of democracy. For the National Conference of State Legislatures, I'm your host Gene Rose.

On this edition of Our American States, we're going to get the latest economic news from Beth Ann Bovino who is the U.S. Chief Economist for Standard and Poor's in New York. Welcome to the program Beth Ann. Tell us a little bit about your background and what you do for Standard and Poor's

BA: Sure. Well, I've lived in the Northeast for most of my life and became interested in economics starting in college, and if anything, the financial crisis and great recession just got me even more absorbed in understanding kind of what makes the U.S. economy tick and how to make it healthier. I started in the Atlanta Fed as an economist and have been an economist at S&P Global for over 13 years.

Gene: So let's talk about some broad strokes here. A lot of people are mostly interested I think right now in the U.S. economic recovery. How would you summarize the economy's performance during this recovery time?

BA: Well, it was certainly a very, very slow start. The economy really just kind of stumbled along I'd say early on in this recovery. But we have seen since some improvements in it. Indeed, at this point in time, we see the economy as still rather sluggish, but oil prices have stabilized, so that gives the energy sector a little bit more of a boost and certainly helps areas/states that have energy related business.

Business confidence actually hit record highs and has been holding relatively high for some time, and even there we've seen a pickup in private demand and certainly the jobs numbers are coming in rather strong as well. Certainly we would need to see more business investment – that still remains somewhat sluggish; but we do see sort of that animal spirit kicking in at this point in time.

We've seen people, households opening up their checkbooks a bit further, and that's been helped by higher wages as the recovery was going. It certainly was sluggish and now we're seeing that pick up as well.

One of the many final positive pieces of news is the housing market, which has been on life support for some time. Well, now that certainly has strengthened most recently in this recovery.

Finally, manufacturing has been one of the highlights of this recovery and while it's certainly been hit by the strong dollar and the drop in oil prices, manufacturing still seems to be ticking along.

I guess this all gives reason for the Federal Reserve to continue raising rates, which we expect, another two this year and a few more the next. And with that we think the Fed is going to finally address their very large four-and-a-half trillion or so balance sheet, the bond holdings that they have; we think they're probably going to start to announce how they're going to do that much later this year, and then start the process the following.

Gene: What kind of effect would that have?

BA: The common phrase is that expansions don't die of old age; they're murdered, and often by the Fed or by another central bank. And certainly that's one concern that many of us have talked about this time around. The fact really is that what drives the Fed is how strong the economy is and, of course, the inflation story. Right now inflation is still rather low. It's picking up, but it's still rather on the soft side. So that gives the Fed some time to take a gradual approach to raising rates, and, of course, managing their balance sheet.

So the Fed can move rather slowly in both aspects. In that sense, it will slow the economy down, but we suspect will not necessarily push it back into a low growth or recession environment. We think with the Fed moving on its balance sheet, they plan to take a gradual approach; we think their first step will be actually starting to cut back on reinvesting their proceeds from their bond holdings. We think they'll probably announce that by year end and do that gradually, because they do have a large size in the market.

And once they do slowly bring that down to zero, then they're going to focus on their very large balance sheet. And what we expect they will do, again, because they recognize that they don't want to unravel bond markets and the economy, we think they're going to just allow their bond holders just to reach maturity and kind of roll off their balance sheet. That will take a long time for it to get back to normal and if the economy continues at a moderate pace of growth, we think the Fed can manage that.

Gene: Getting back to the economic recovery, according to the National Bureau of Economic Research, this is the third-longest recovery… What do you think distinguishes this one from others that we've had in the past?

BA: It is indeed the third longest, and unfortunately it's also the slowest economic recovery since World War II when you look at what the average GDP growth rate for this recovery is, which has been averaging around 2 percent per year. That is the lowest going back a number of decades.

One of the plus sides at least is that the jobs market has been improving and job gains are now – in that sense we're not the lowest in terms of job gains since the recovery started. I guess we're next to the lowest. So at least we see some improvement there. And after the most recent jobs numbers that came out with job gains in April now looking at 211,000 for the month, and basically an average of around 175,000, that looks like the economy is starting to approach full employment, and with that higher wages. We are expecting wages to pick up this year. We're expecting them to top over 3 percent by year end and, while that's still on the low side as far as recoveries historically go, that's a lot better than what we saw earlier on.

One of the differences also for this recovery, when you compare it to others, is that we have an aging population. We have many workers now reaching retirement age and leaving the workforce. That means that the labor participation rate has been falling lower and lower and it is now at a 38-year low. With lost productivity from people leaving the workforce, that also means less income for households and less money to spend, and it also means less productivity for the economy and slower growth going on.

We do expect the economy to continue at a modest pace, but 2 percent growth is certainly far from what we would like to see.

Gene: I understand you just released your April jobs report. I'm curious about the type of jobs that are being created. We hear a lot about that those are lower-paying jobs. Is that what you're finding as well?

BA: I'd say early on and throughout most of this recovery, the jobs that were created were very low-paying jobs in the service sector and retail and in health. Many other jobs that certainly didn't give people enough to pay down most of their bills, but certainly not much more to really spend at the mall. So we did see because of basically the lower-paying jobs that were offered early on in this recovery, we didn't really see the real pickup in spending following that.

We have most recently, say going back maybe a year, we started to see a pickup in breadth of jobs being offered. There are still certainly lower-paying jobs that are being created, but with that we are also starting to see more high-paying jobs picking up as well, both in technology and also in other aspects of the economy.

Manufacturing is also holding up relatively well, and another factor to keep in mind is that we actually have seen for low-paying jobs, we've seen a pickup in the minimum wage across a number of states, and that also suggests those low-paying jobs – we call it the "Walmart effect" – those low-paying jobs are also getting a little bit bigger paycheck as well.

Gene: What do you see as the biggest threats to the continued economic recovery right now?

BA: We have a risk of another recession over the next 12 months, between 20 to 25 percent. That's a little bit high but it's still, again, it still suggests that a recession is not likely. Probably the biggest and one of the reasons why it's a little higher is political risk. The risk of a policy mistake has certainly increased, both in the United States and abroad. When we talk about political risk, we look at the question of trade wars with either China or Mexico, NAFTA unraveling – all those factors could certainly hit the U.S. bottom line.

Other worries that seem to be allayed somewhat after the vote in France, but of course another worry is that we've had the Brexit that is now going underway, but the worry was would there be exit mania, a French exit or other European countries leaving the European Union. This could also have an impact on U.S. growth.

And we also don't want to forget political risk. We all know about ISIS and not just human suffering, but also the impact on the economy as that actually plays out. We have other political risks – North Korea and Syria come close to mind.

Gene: Speaking of political aspects of this, I know that you evaluated the first 100 days of the new Trump administration. What kind of data did you collect from that?

BA: The first 100 days, we did want to take a look at that, and probably the first thing we would say is that the first 100 days given not much has gotten out in terms of the campaign proposals, they have not necessarily come into effect. I'd say disappointment is one of the first things that we would say. Little has happened to change our outlook for the economy. We're still at pretty much the modest pace of around 2 to 2.5percent, and we think that's going to hold through the decade. So we really haven't seen the impetus that we'd hoped for.

The main reason for this is gridlock, which has made it hard for the Trump administration to push his campaign promises into policy. We did note that one silver lining is that the administration inherited a stronger economy, which we think will give him more time to right the legislative ship. While we don't expect to see major breakthrough coming out of Capitol Hill, we do expect to see a small tax package that could be passed in Congress. We think probably one of the biggest impetuses for that getting passed is the ides of the midterm elections coming due next year in 2018 will encourage Congress to come to some kind of consensus.

We also expect to see some small infrastructure package, also likely to get agreed upon as the Trump administration reaches across the aisle to the Democrats to elicit more votes for both.

Gene: Okay, thanks Beth Ann. That's a lot of information to digest. We'll let our listeners soak all this in and return with some more questions for Standard and Poor's U.S. Chief Economist Beth Ann Bovino right after this break.

BREAK

Gene: So we're back with Standard and Poor's U.S. Chief Economist Beth Ann Bovino. My understanding is that two-thirds of the economy is driven by consumer spending. What's your sense of where consumer confidence is right now?

BA: Consumer confidence is holding up certainly rather well. I would say probably the big factor is jobs, jobs, jobs, and right next in line is wages, wages, wages. We're seeing that consumer confidence has improved pretty significantly, certainly well into recovery mode. And since job gains now are averaging around 175,000 at least for the last three months, and for the last year it's probably even higher than that, with job gains coming around and with that we do see higher wages – that's one reason why people are feeling more comfortable with their economic status and also with basically their financial homes. We do think that's going to continue through this year and into the next. We think consumers are going to have a little bit more money to spend, and that's going to be a plus for both them and for the economy.

Gene: And you mentioned business confidence; you said that that seems to be improving there. What are some of the factors that go into that?

BA: There are positives and concerns. On the positives, we've seen business confidence… a number of indicators show business confidence levels at near or at record highs. If you look at sentiment readings from the ISM indicators, both manufacturing and services have held above the 50-point mark, which indicates expansion. Indeed, they've held up or near that throughout most of the recovery, at least for services. Manufacturing got a dip when we saw the drop in oil prices and increase in the dollar, but even there they're still mainly holding up over 50. That's a positive.

The worry though that we have is that while everybody is happy and animal spirits are certainly strong, we haven't seen animal spirits turn into animal actions. Business investment is still rather sluggish. It's positive and that's good; it's in the positive territory, but still in the lower single digits in terms of business equipment spending and nonresidential construction. There we are expecting a bit of a pickup later this year.

One of the helps is going to be removal of some of the red tape, as the Trump administration talked about deregulation. That could give it a positive, although right now it's still yet to be seen. We'll keep an eye on that and that's something that we'll always watch to see if they really open up the faucets in terms of spending.

Gene: And for most of our audience, what they're mainly concerned about is what's going on in their state. Are there different parts of the country or specific areas where you see some concerns, or even some healthy growth?

BA: There I would say certainly the energy sector, the drop… oil prices fell from over $100 to I think it even hit close to $25 at one point – that huge drop in oil prices certainly hit energy related businesses and a lot of that energy related business is concentrated in areas in the West. Pennsylvania was also hurt because of the drop in natural gas prices, which still remain high. There we have seen kind of a turnaround, I guess you could say somewhat a reversal of fortunes, because the energy sector started so strong throughout most of this recovery and certainly took a dive down.

We do see some stabilization in oil prices and that should help the energy sector, but we don't necessarily see a real bounce in that sector, and that's certainly going to hurt those states that have a concentration in that.

We do see housing turning around. That's going to certainly help most states in the U.S. as we recover from the financial crisis and housing crash, particularly areas in the West, California for example, we'll finally see and continue to see improvement in housing to help their bottom line.

Areas that we could see more improvement: we do expect to see wages picking up. The financial sector, of course, the Northeast benefits from that and that could be a positive. And we also see consumer spending will continue to slowly climb higher as wages continue to pick up, and that will be a plus for many parts of the states.

Gene: And what about the stock market? It definitely took a pretty big rise when Trump was inaugurated. What's your assessment of where it's going, maybe what has happened?

BA: Well we'd say in terms of the stock market, after the election we saw the stock market climb to actually near or at record highs right now. At the point that we saw that bounce in the stock market an optimism that the Trump administration was able to get through tax cuts, tax reform, an infrastructure package, deregulation, all these things… optimism came out from the stock markets. We had said back then and we continue to say now that campaign promises are not policy. It remains to be seen whether these things will get through.

We also at that point in time thought that the stock market got ahead of itself in imagining that these things were already in place. We saw gridlock, we saw it before, and even though we have a Congress that is majority Republican, we can see the divisions among the Republican Party, suggesting that gridlock will remain.

So in that sense, while I'm an economist, not a specialist on the equity market, I would say that I think that the markets are rather rich right now. Once markets recognize that some of these things may not come into being at least as they were promised, they might be disappointed.

Gene: Okay. And Beth Ann, you are going to be at the National Conference of State Legislatures Legislative Summit in Boston this August. Can you give our listeners a preview maybe of what they can expect to hear from you then?

BA: It's going to be a few months from now and we're going to see a lot of things happen in terms of the U.S. economy. We're going to have a few more numbers and jobs and if my expectations that the jobs market and wages will be picking up, if that comes into being, we'll certainly have a lot more to talk about.

The Fed will be moving on raising rates and I think they'll have a lot more to announce on what happens with their balance sheets. And Capitol Hill will never disappoint; I'm sure we'll have a lot more to say on that. All this will have an impact on state legislators and I hope that when I'm there we'll be able to drill that down to what their needs and concerns are.

Gene: Okay, great. And Beth Ann, why don't you let us know what is the best way for our listeners to keep in touch with you and your research.

BA: Certainly. One thing that we do offer at S&P Global is the economics team basically offers our analysis and economic commentary for free on our website. Now I don't know if it makes sense for me to start reciting the www. blah blah blah. So what I'm going to tell people to do, probably the easiest way for them to do it is to do a Google search or any other search function on – type in "S&P Global ratings and economic insights" and you should be able to easily find our latest news. I hope it's easy enough. You never know, but I hope it is.

Gene: Okay, fantastic. Well, Beth Ann, we certainly appreciate your time and for being a guest on Our American States.

BA: Thanks for having me. Great talking.

Gene: And that concludes this issue of Our American States. We invite you to subscribe to this podcast on Itunes and Googleplay. Until our next episode, this is Gene Rose for the National Conference of State Legislatures. Thanks for listening.