

Explaining a Decade of U.S. Stagnation: Where Do We Go From Here?

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Steven Fazzari

Washington University in St. Louis

Departments of Economics and Sociology

Weidenbaum Center on the Economy, Government, and Public Policy

A Decade of U.S. “Secular Stagnation”

- Paradox: claiming “stagnation” when macro data look rosy
- Part 1: Addressing the paradox—stagnation in aftermath of the Great Recession
- Part 2: Key problem is weak demand, especially from the heavily indebted household sector
 - Role of rising inequality in demand-side stagnation
- Part 3: Consequences and where do we go from here?
- Acknowledgements
 - Support from INET
 - Co-authored work with Barry Cynamon

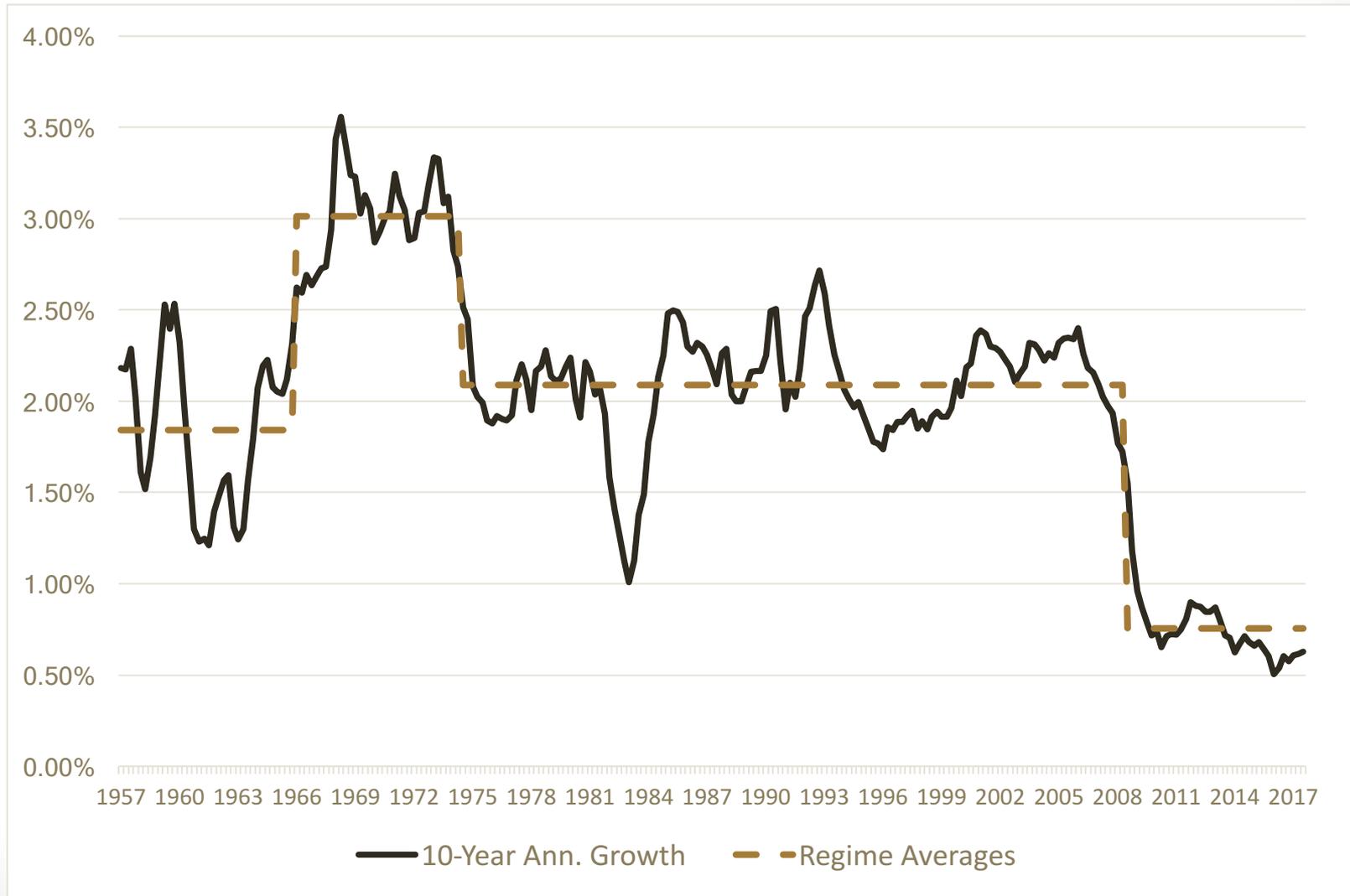
Recent Stagnation

(Peak-to-peak growth of real GDP per capita)

Peak Dates	Growth per Year (per capita)
1973:4 to 1979:3	1.8%
1979:3 to 1990:2	2.1%
1990:2 to 2000:2	2.2%
2000:4 to 2007:4	1.4%
2007:4 to 2017:2*	<u>0.6%</u>

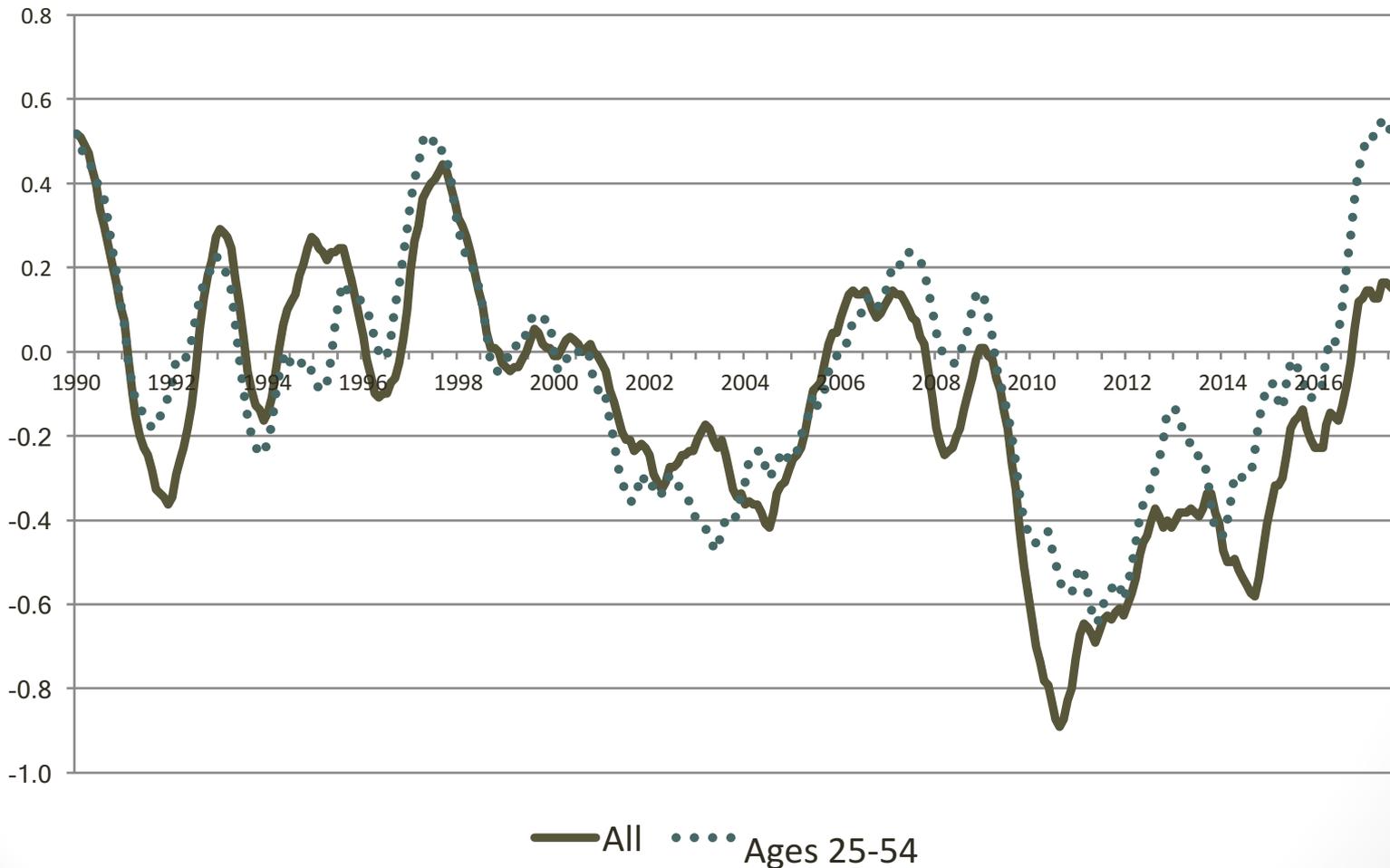
*Final cycle is incomplete

Exceptionally Weak Long-Term Growth

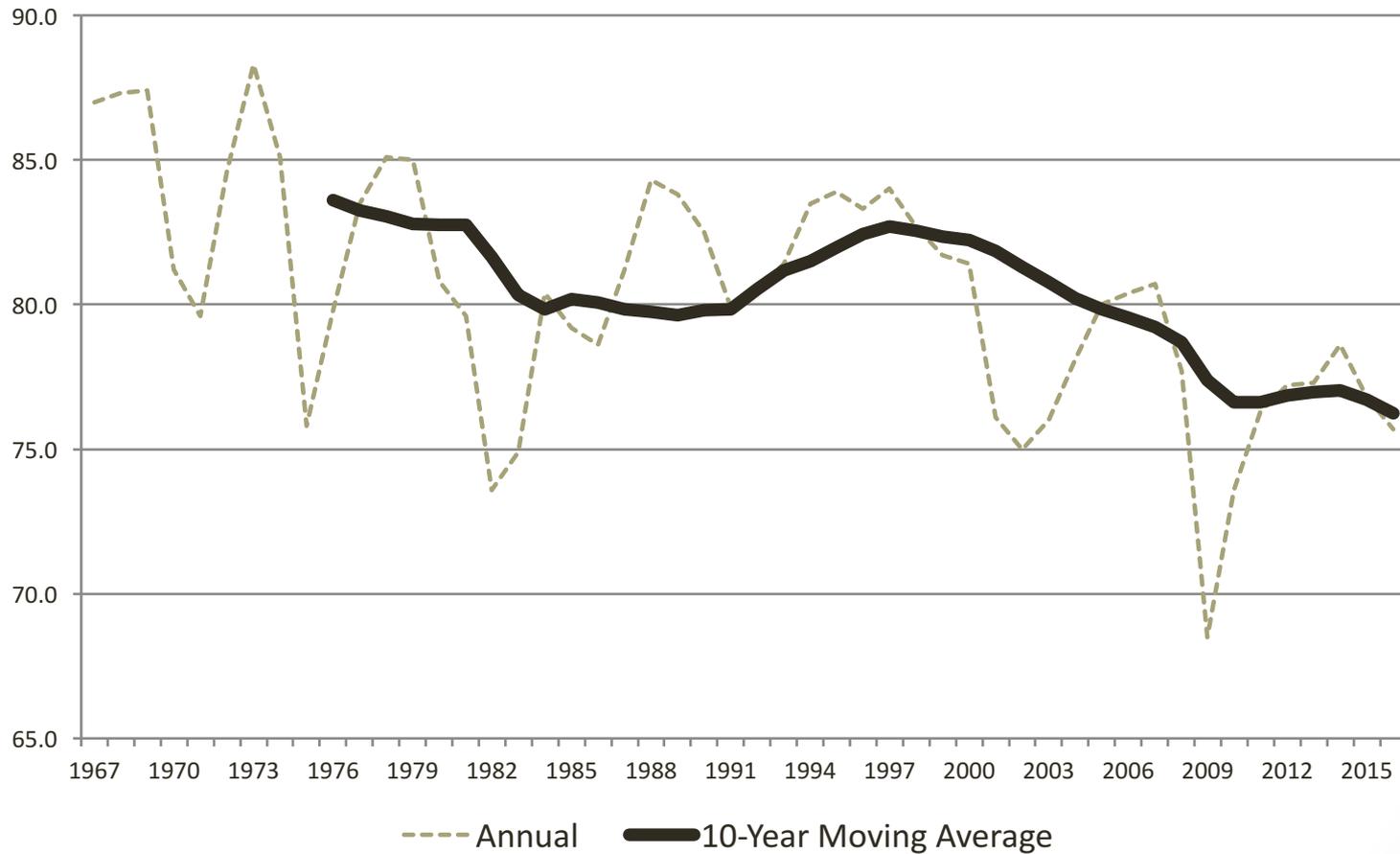


Change in Labor Force Participation

12-Month Rolling Average of Year-Over-Year Change

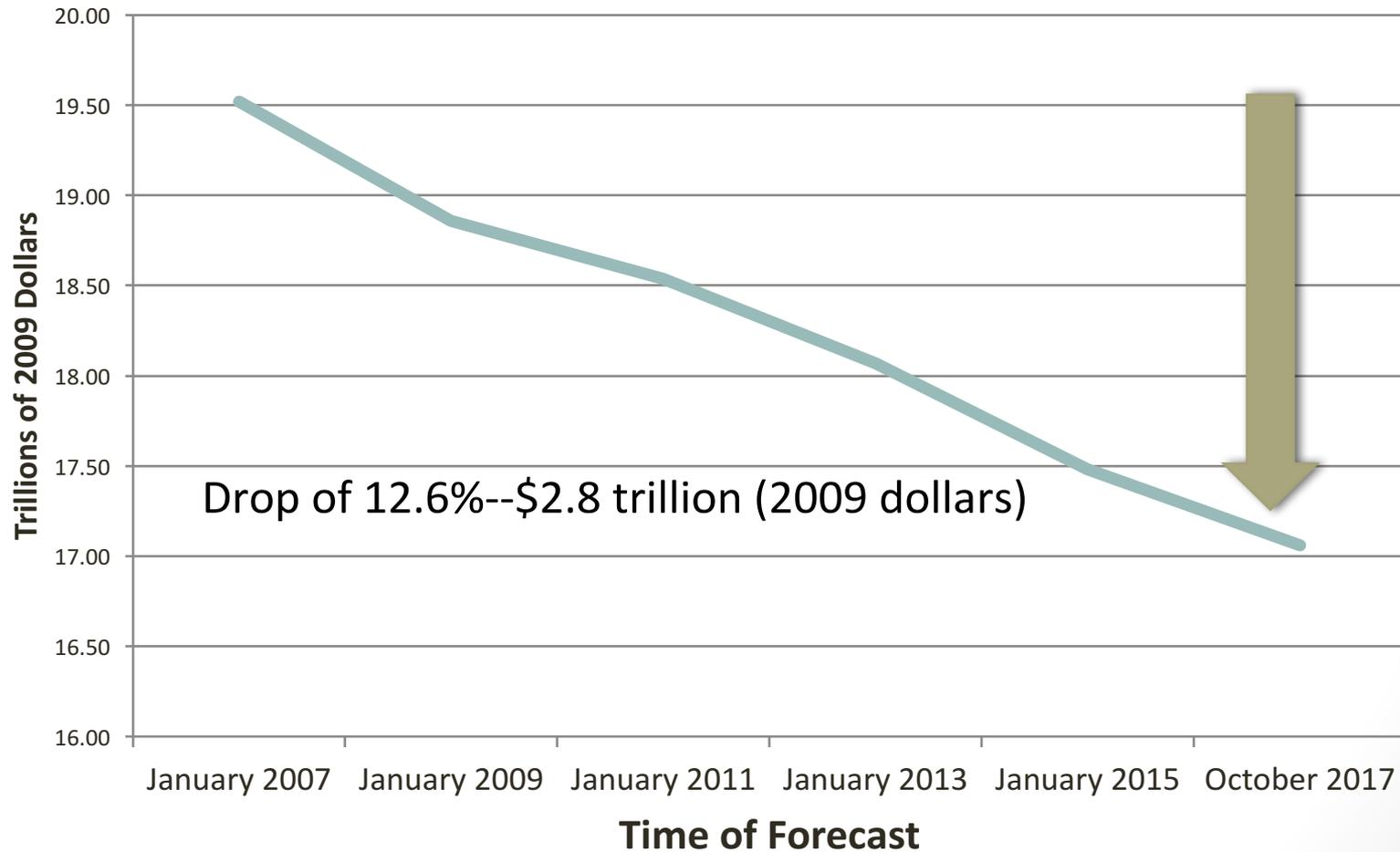


Downward Long-Term Trend of Capacity Utilization



An Excessively Optimistic Forecast

(Change of CBO Real Potential Output Projection for 2017:Q2)



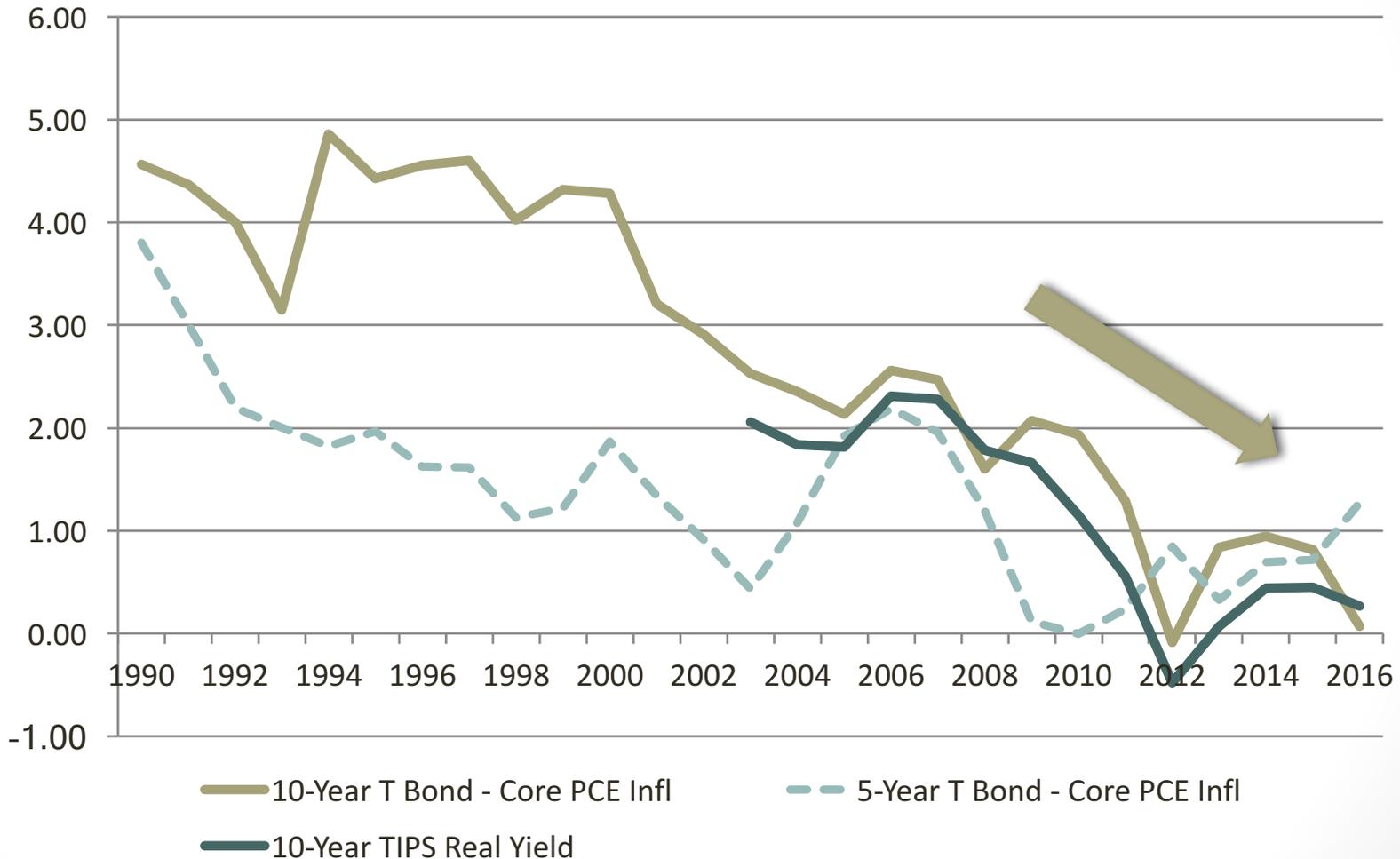
Something Has Happened, But Why?

- Textbook story: decade of persistence => supply side
 - Old story: wage and price adjustment
 - New story: wise monetary policy
- But could it be the demand side?
 - Zero lower bound
 - Heterodox models of demand-led growth
- Look at the evidence

Weak Evidence for Supply-Side Stagnation

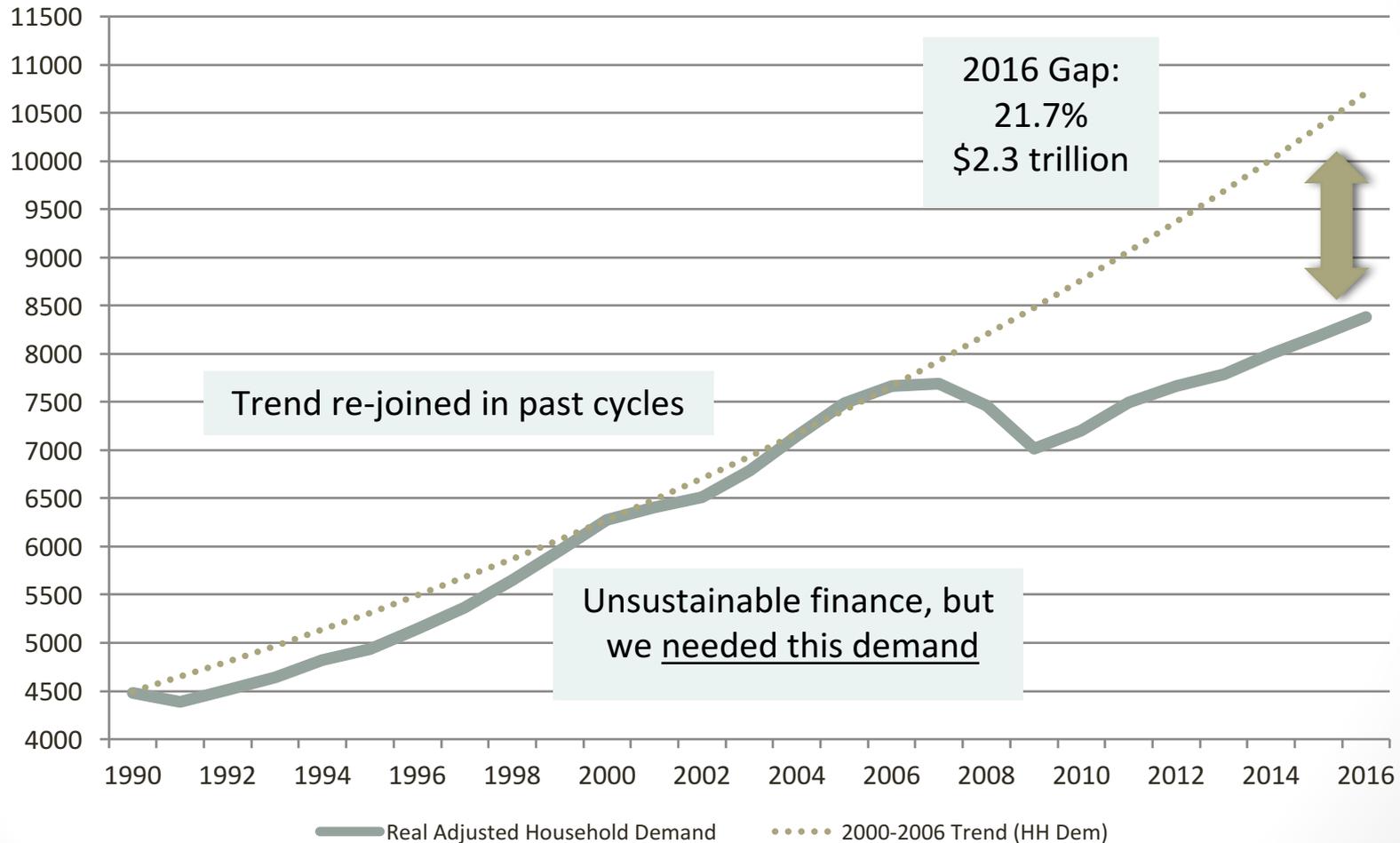
- More slack in the labor market than suggested by low unemployment rates
- Business investment not particularly low given slow growth
- Weak inflation contradicts textbook analysis of a negative “supply shock”
- Key test: persistent supply-side stagnation should cause high real interest rates

Real Interest Rates: No Evidence of Supply Stagnation



The Demand Side: Household Demand

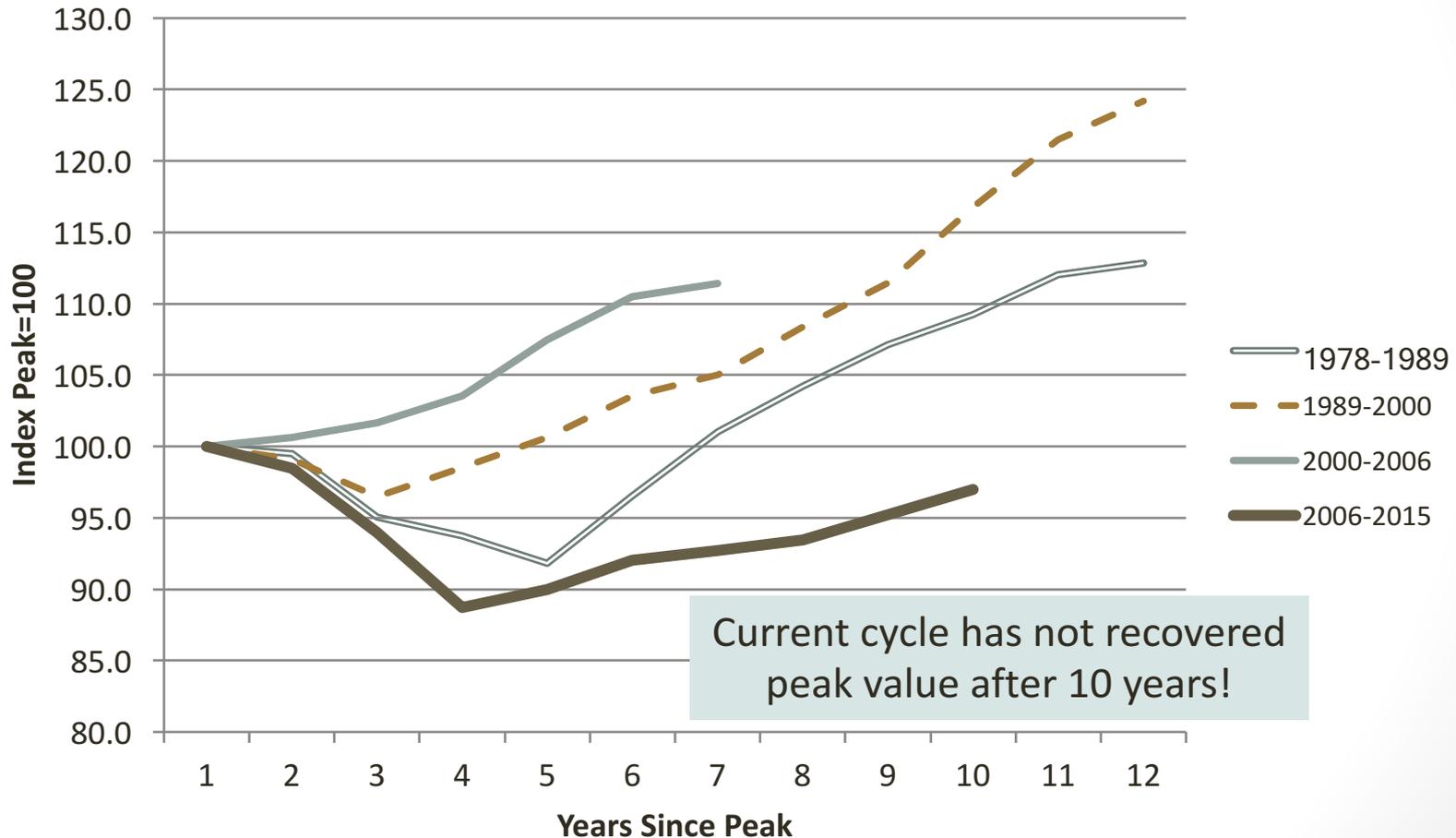
(Adjusted household demand based on Cynamon & Fazzari, 2017)



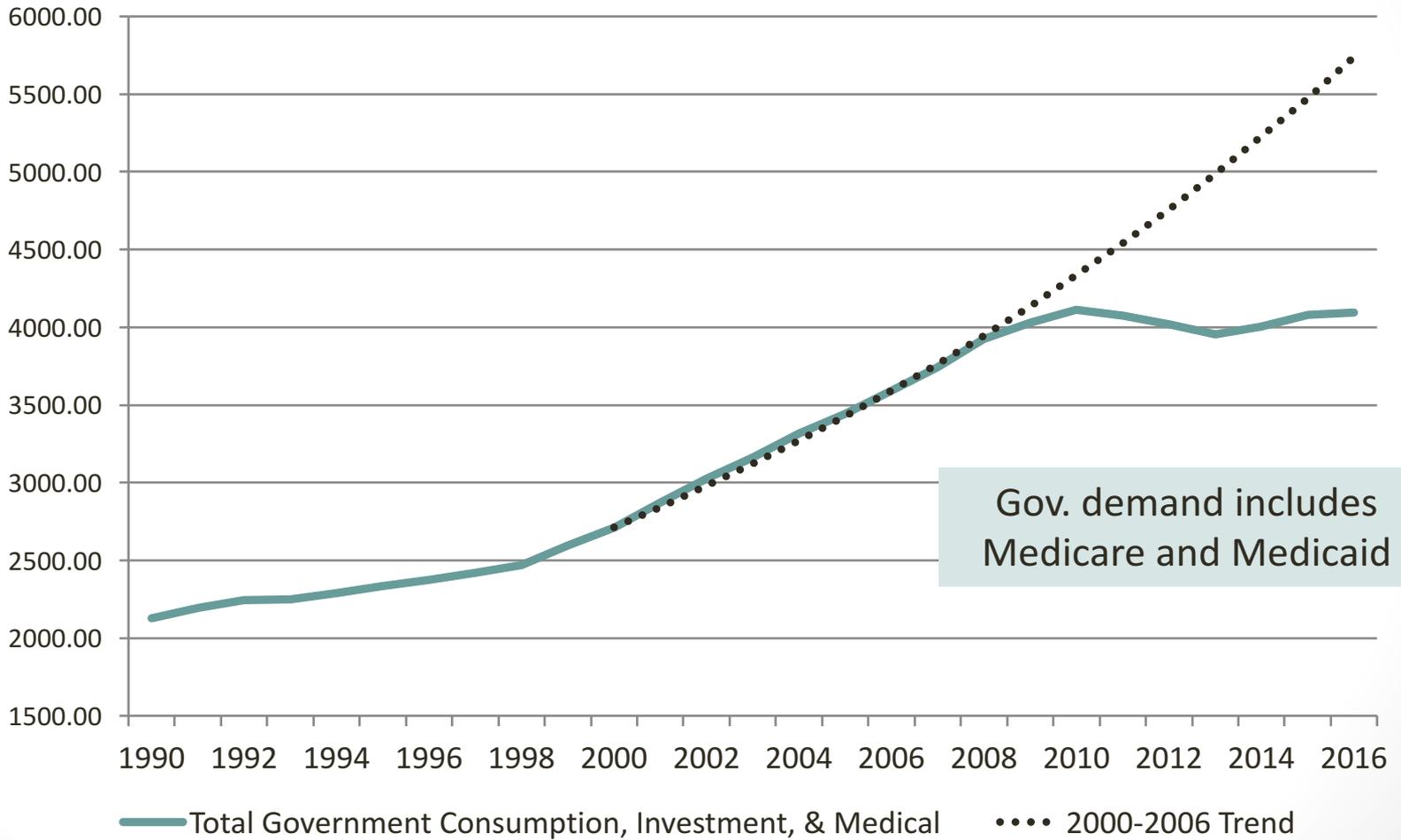
Weak Household Spending and the Stagnant Recovery

(Based on Cynamon-Fazzari Review of Income & Wealth, 2017)

Real Household Demand Profiles (Population Adjusted)



Government Demand Did Not Replace Households



Nuanced Role for Inequality

- Rising inequality as explanation for stagnant demand
 - Rich spend or “recycle” a smaller share of income than others
- Timing problem
- Borrow-and-spend era postpones demand drag
- Great Recession forces middle-class demand down
 - Middle-class demand now more in line with stagnant incomes
 - But we needed that demand
- Rising inequality can explain at least 10% slowdown of demand path since mid 1980s (Cynamon & Fazzari, EJEEP, 2015)

Consequences

- Disappointing recovery and secular stagnation “beyond the short run”
- Deleveraging not enough to restore robust demand growth
 - Household financial sustainability (chart)
- No strong case for growth acceleration
 - Good chance that the string of 3% quarters will end in 2018
 - Interest rate path likely to remain low

Share of Sustainable Households

PSID Data from Cooper-Cynamon-Fazzari



Future Engines of Demand Growth

- Government?
 - Inconsistent calls for smaller government
 - Infrastructure investment could help both demand and supply sides
 - Tax policy to address household demand
- Growth relies on spending of the affluent (chart)
 - Implications for macroeconomics and structure of society
- Reconnect productivity and wages
 - Wage growth across the income distribution
 - Critical goal, but no easy policy fix

The Affluent as Growth Engine?

Index of Real Consumption, Bottom 95% and Top 5% (1989=100)

