First Trust
Monday Morning OUTLOOK

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Room to Grow

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The US economy has grown at an average annual rate of only 2.1% since the recovery started in mid-2009, far slower than during the economic expansions of the 1980s and 1990s.

Many analysts tie some of the slower growth to slower expansion in the labor force due to retiring Boomers and the end of the shift of women into the paid job market. But productivity (output per hour) has been slow as well. Since mid-2009, productivity is up at a 1.0% annual rate versus a pace of 2.1% at the same point in the recoveries after the 1981-82 recession and 1990-91 recession. The expansion in 2001-07 lasted six years during which productivity grew 2.5% per year.

In other words, if productivity growth had been just as fast in the current expansion as in the expansions of the 80s and 90s, real GDP growth would have been averaging around 3.2% per year, not 2.1%. In that case, much of the current angst about the US economy would be gone.

Two popular theories try to explain why productivity growth has been so slow.

One is the "Great Stagnation" theory made famous by economist Robert Gordon, among others. Gordon believes humanity – usually, but not always, led by the US – made massive leaps in technological progress and implementation between 1870 and 1970: incandescent light bulbs, automobiles, central heating, refrigerators, the germ theory of disease, window screens, radios, telephones, television, air conditioners, airplanes, sewer systems, and indoor plumbing.

Gordon says those kinds of achievements, directly addressing problems humans have wanted to address since the beginning of time, simply can't be duplicated again, and so we're simply going to have to learn to live with slower economic growth. In turn, he proposes government policies that focus on redistributing income to lower earners.

No one doubts the transformative nature of the inventions of the late 19th Century and early 20th Century. But pretending that we can know the future path of technological advances is the kind of hubris at the heart of centrally planned economies.

Moreover, we think any slowdown in progress is due to the larger size of government, which puts politicians in charge of shifting resources around according to political expediency rather than letting those resources find their most efficient use. It's no wonder that the biggest leaps in innovation started when the US government was tiny compared to today's size.

Think about the possibilities of driverless cars or doubling the length of healthy vigorous adult life (both mentally and physically). The economic value of these kinds of breakthroughs would be enormous.

Another theory of why we have to settle for slower growth is our economy has too much debt. But debt, by itself, is not a reason for slower growth. Just think about your own situation. If you woke up this morning and had $50,000 more debt than you previously realized, would you work more or less in the future? More, obviously, which makes output go up, not down.

Debt can be a problem if debtors suddenly decide they won't pay their obligations. In that case, lenders can become insolvent, causing financial strains until the economy adapts.

But we don't see a reason for a sudden spike in defaults by borrowers. Seven years ago, consumers were 90+ days delinquent on more than a $1 trillion in consumer loans. But that figure has declined every year since and is now at $400 billion.

Although the government's debt is at a record high, net interest on the debt is still low relative to both GDP and federal revenue. Even if interest rates on government debt went to 4% across the yield curve tomorrow, net interest relative to GDP and revenue would still be lower than the average during the 1980s and 1990s.

Meanwhile, capital standards are higher and leverage ratios lower at US financial institutions. In other words, debt is not holding the US economy back.

We believe the US is at a pivotal point right now, with a chance to curb spending, cuts tax rates, and rollback the regulatory state. If it does so, many of the same analysts now telling us we have to accept slower growth will be spinning their wheels inventing theories about why growth suddenly picked back up.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
2-7 / 7:30 am	Int'l Trade Balance – Dec	-$45.0 Bil	**-$45.0 Bil**		-$45.2 Bil
2:00 pm	Consumer Credit– Dec	$20.0 Bil	**$20.1 Bil**		$24.5 Bil
2-9 / 7:30 am	Initial Claims – Feb 7	249K	**245K**		246K
2-10 / 7:30 am	Import Prices – Jan	+0.3%	**+0.8%**		+0.4%
7:30 am	Export Prices – Jan	0.0%	**0.0%**		+0.3%
9:00 am	U. Mich Consumer Sentiment- Feb	97.8	**99.0**		98.5