Mitchell's Musings 3-9-15: We May be Able to Play Keynes to the World, But It's a Bad Idea

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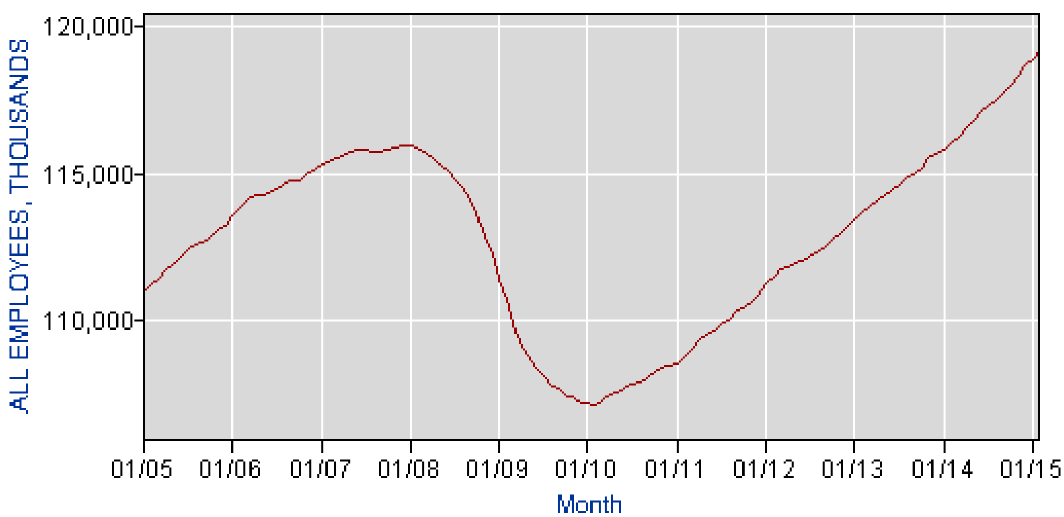
There was much excitement when the latest employment release came out from the U.S. Bureau of Labor Statistics last week. The February month-to-month change, seasonally adjusted, in payroll employment was officially 295,000, considered "good." In past musings, I have cautioned about the vagaries of one-month, seasonally-adjusted data that are preliminary and subject to revision and re-revision. But those folks who were excited about the employment gain pointed to a series of months with gains above 200,000. And the stock market took a dive on the news, purportedly because good news is bad news if you are worried about the Fed eventually raising interest rates as the economy picks up.

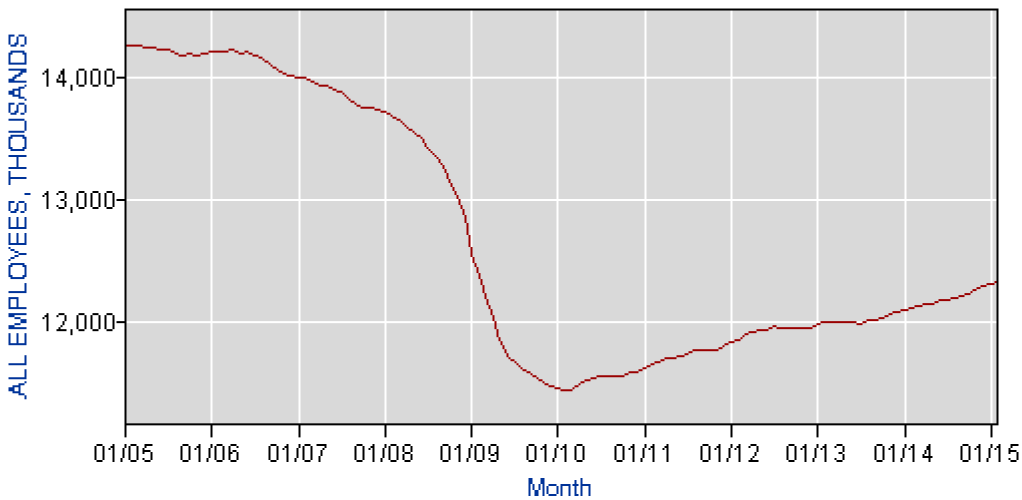
There is no doubt, however, that apart from monthly noise in the data, U.S. employment has been expanding steadily, if not rapidly, for the past five years, as the chart below illustrates. However,

Private Sector Payroll Employment



there are sectoral differences in the post-Great Recession experience. In particular, manufacturing employment (see chart on the next page), while showing gains over the past five years, is nowhere near its prior cyclical peak. While total private employment surpassed its previous peak in 2014, manufacturing employment is still depressed. As we have noted in prior musings, if you want to do something for manufacturing, offering training at community colleges or providing subsidies to this or that “greentech” company won’t do it. Photo ops at high-tech factories won’t do it. You have to look at the international side of the problem of long-term job erosion in manufacturing. And, having looked there, you have to address the issue of the chronic American trade deficit.

Manufacturing Payroll Employment



The world has grown used to the U.S. playing Keynes when job expansion abroad is needed. In the past year or so, both Japan and the Euro-zone have experienced economic slumps of varying degrees and have allowed (encouraged?) their currency exchange rates to depreciate relative to the U.S. dollar. While such foreign currency depreciation adversely affects the competitiveness of a variety of U.S. industries, the impact is particularly felt in the manufacturing sector. Import-competing sectors of manufacturing are put under additional pressure. And exports become more difficult to sell abroad. The former “good jobs” in manufacturing that aren’t there anymore are not gone because of some mysterious force of nature. Some may have gone due to technological advance. But others are gone because no one in either political party wants to address the real deficit that matters to manufacturing – the trade deficit.

As the chart above shows, just to get back to the prior peak in manufacturing would require growth of roughly two million jobs. Both political parties claim an interest in job creation, particularly in manufacturing. But neither has a program for addressing the dollar exchange rate. And in less than a year, the dollar has appreciated on a trade-weighted basis by almost 10%, as can be seen on the chart on the next page from the St. Louis Fed database. Much of that change is Euro and Yen related.

Have you heard any Congressional debate about that dollar appreciation? Are there statements from the White House? When you do hear discussion of the "deficit" from either source, it is always the federal budget deficit and not the trade deficit that is the target. Why is that? Why is there a taboo when it comes to discussing exchange rates? A 10% jump in gasoline prices creates headlines, but not a 10% dollar appreciation (about the magnitude on the chart below). Why is the U.S. the one country elected to play Keynes (i.e., to provide stimulus to other economies) when foreign economies need help? It's time to change the rules of the international game.