Mitchell's Musings 6-15-15: Did Anything Really Happen?

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Much was made of a "slowdown" of the economy in the first quarter of 2015. According to the latest release from the U.S. Bureau of Economic Analysis – which is the second estimate for that period – in the first quarter real GDP *declined* at an annual rate of 0.7% in contrast to an initial report of an annualized *increase* of 0.2%.[1] The estimate of a decline brought headlines which didn't always reflect the fact that these are annualized numbers, i.e., the actual decline (if there was one) was only about one fourth of 0.7% per quarter.[2] CEOs are said to have revised down their growth estimates, perhaps after hearing from their corporate economists about the decline.[3] (Question: Are CEOs fully conversant with BEA methodology for producing real estimates from nominal data and then seasonally-adjusting the results? It is likely that most economists who use the BEA data would have to look up the technical details.)

Real GDP data are typically presented in seasonally-adjusted form so the fact that the winter is a slow period generally shouldn't affect the numbers. However, the winter was especially severe and therefore the seasonal factors – which are based on historical patterns – possibly understated the effects of bad weather.[4] Then again, as we have noted in prior musings, the methodology for calculating real GDP from the nominal figures is arcane. So we are talking about questionable seasonal factors imposed on arcane and preliminary estimates.

Given the uncertainties, let's look at the labor market and see if anything really exciting has occurred in early 2015. Below is a chart of twelve-month percentage nonfarm payroll employment growth. It is based on actual employment levels (not seasonally-adjusted levels) compared with the same month a year earlier.[5] So if winter was extra-severe in 2015 (which it

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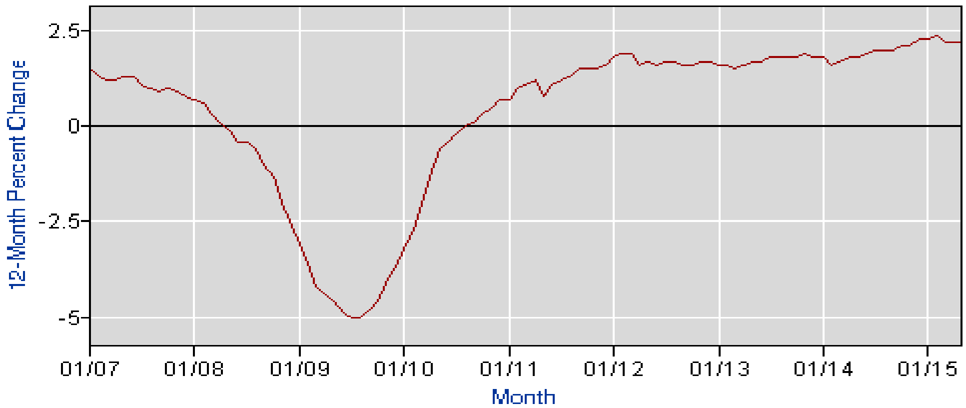
[1]http://www.bea.gov/newsreleases/national/gdp/2015/pdf/gdp1q15_2nd.pdf.
[2]The headline in the *New York Times* was "U.S. Economy Contracted 0.7% in First Quarter." See http://www.nytimes.com/2015/05/30/business/economy/us-economy-gdp-q1-revision.html. The article's text noted that the estimates were annualized.
[3]http://www.reuters.com/article/2015/06/08/us-usa-economy-ceo-survey-idUSKBN0OO24I20150608.
[4]It has been argued that there are other problems with the winter seasonal adjustment. See http://www.frbsf.org/economic-research/publications/economic-letter/2015/may/weak-first-quarter-gdp-residual-seasonality-adjustment/
[5]All employment data cited are from the U.S. Bureau of Labor Statistics.

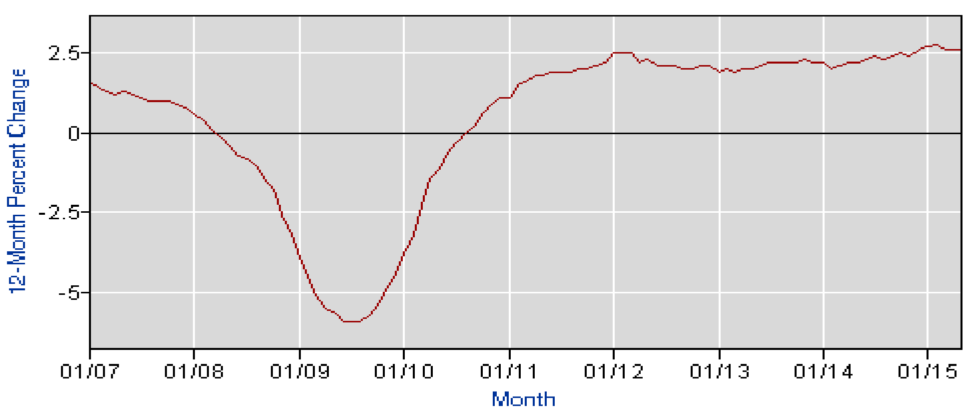
undoubtedly was), this method of dealing with the seasonal effect will understate the impact of weather.

Twelve-Month Percent Change in Nonfarm Employment



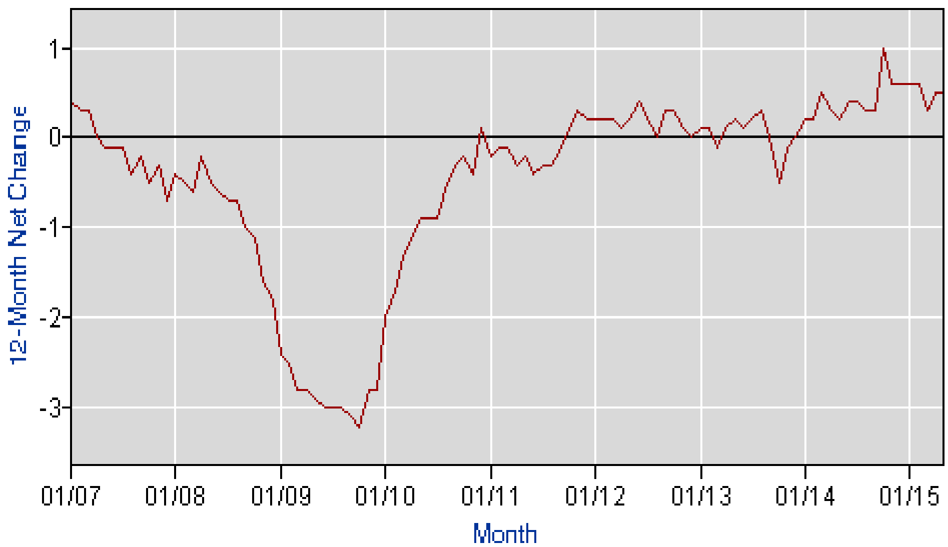
When you look at the chart, you see a slight slippage in the employment growth rate in early 2015. But even with the slippage – which may be entirely a weather-related event – the growth in employment was <u>above</u> the level we have seen earlier in the recovery. If we look only at the private sector, growth rates on a 12-month basis are a bit higher than when government is included. Nonetheless, except for a brief period back in early 2012, growth rates were generally below those so far in 2015.

Twelve-Month Percent Change in Private Payroll Employment

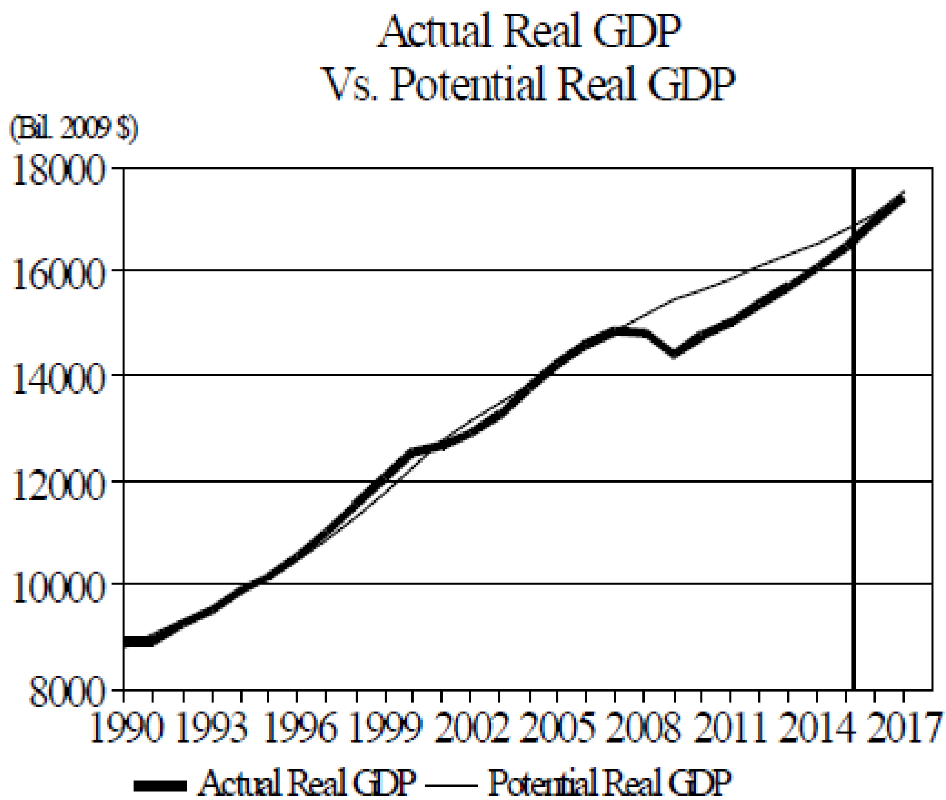


If we look at the employment-to-population ratio from the Current Population Survey (Household Survey), the results are similar. The improving trend continued into early 2015 and in fact was stronger in that period than in much of the earlier recovery. In short, when you look at the labor market and put the numbers into perspective, it appears that there really wasn't a meaningful slowdown. At most there was a snow-down, CEO pessimism notwithstanding.

Twelve-Month Percentage Point Change in the Employment-to-Population Ratio



What matters in terms of employment and the general direction of the economy is the underlying trend, not short-term noise. Blips up and down are often just statistical aberrations and should not be heralded as a structural shift. The most recent UCLA Anderson Forecast for the U.S. economy as an example tells a story of a long and painful deviation from capacity due to the Great Recession and a slow recovery thereafter. As the chart below from that Forecast indicates, at current rates of (projected) growth, it will take another couple of years to get back to where we should be. Of course, it is possible that some unforeseen events could intervene before we get there. But nothing fundamental happened in the first quarter of 2015 that should change that perception.



Source: UCLA Anderson Forecast, June 2015.