Louisiana Corporate Credit Union
ECONOMIC & FINANCIAL DIGEST
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Households Are Finally Doing Better

It's been a long slog, but things are looking up for the U.S. economy. True, headline growth is not where it should be, as gross domestic product remains stuck in second gear. But as they say, you can't eat GDP. What matters more to average Americans are jobs and living standards. The latter has been stuck in a rut for nearly two decades thanks to the battering imposed by two recessions followed by lackluster recoveries that have seen most of the income gains flow to wealthier households. Happily, that pattern is starting to change.

The median incomes of households, adjusted for inflation, staged the largest increase on record last year, with all income groups sharing the gain. Hence, after seven years of getting a bad rap, the much-maligned upturn finally deserves some accolades. What's more, the foundation set last year might well be a cause for celebration going forward. But it is too early to uncork the champagne. While the economy has come a long way from the depths of the Great Recession, it is still running well below its potential. Even the labor market, where the unemployment rate stands at a low 4.9 percent, the share of prime age adults drawing paychecks is considerably lower than it was prior to the recession.

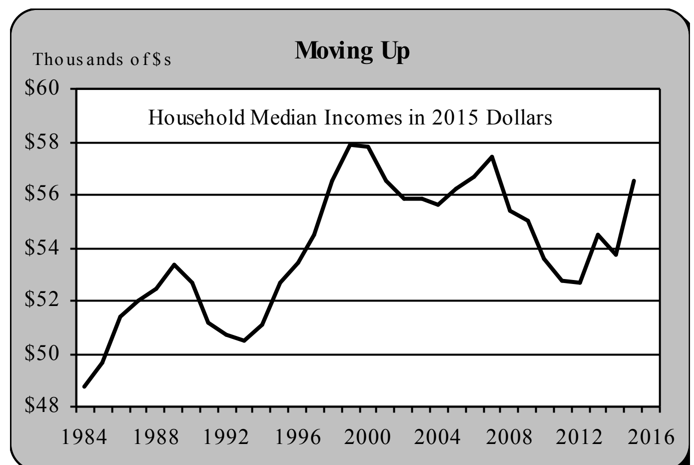
But the job market is continuing to improve, sustaining the broad-based increase in prosperity achieved in 2015 into this year. The ongoing sturdy increases in payrolls is boosting household purchasing power, adding fuel to the economy's main growth engine: consumer spending. But consumers cannot do the heavy lifting indefinitely; without help from business investment, which has been conspicuously lagging in recent years, the economy will remain stuck in second gear, leaving it vulnerable to the myriad shocks that can easily short-circuit the upturn. The good news is that growth is currently on a faster track than the tepid 1 percent pace recorded over the first half of the year, giving it a temporary buffer to withstand potential shocks. The bad news is that the buffer may not hold because business leaders remain less confident in the economy than do households. A key reason cited by the Business Roundtable is the heightened uncertainty surrounding the presidential election, which is putting capital spending plans on hold. Hopefully, this bearish mind-set will recede following the election.

Tide Rises For All

Despite lasting longer than most postwar upturns, it is hard to recall another recovery that has been as disrespected as this one. Indeed, some polls indicate that most Americans believe the economy is still in recession. That sentiment is understandable. Companies have been adding to payrolls at a muscular clip in recent years, but worker pay has not kept pace. For the typical household, median incomes have actually fallen consistently through the first five years of the recovery. What's more, workers at the lower rungs of the income ladder have suffered disproportionate losses. Not only have their real earnings declined more steeply than higher-earners, most have not benefited from the huge stock market gains since 2009, as the vast majority of stocks are held by the more affluent households.

But the tide turned for lower income households in 2015. According to the Census Bureau's annual report on income and poverty, the median income of all households surged by 5.2 percent in 2015, only the second increase since 2007 and the largest gain on record, dating back to 1967. Importantly, the biggest gainers were households on the lower end of the income ladder. That reverses a long trend of larger raises for the more affluent households that have contributed to rising income inequality in the nation. For example, people on the lowest 10 percent of the income ladder saw their real incomes jump by 7.7 percent compared to 2.2 percent for those in the upper 10 percent of the income scale. A corollary benefit: poverty rates dropped by 1 percentage point for whites and more than twice that for African-Americans and Hispanics.

To be sure, the naysayers will correctly point out that at $56.5 thousand, real median income in 2015 was still 1.6 percent below the level in 2007 and 2.6 percent below the peak in 1999. Keep in mind though that those two milestones were followed by calamitous events – the dot-com collapse that sliced 2.6 percent from real incomes from 2002 to 2004, and the 2007 financial crisis the vaporized an even larger 4.9 percent before bottoming out in



2012. Those were historic income-destroying events that are not easily recouped. Make no mistake; the 2015 gains were historic as well, not only for the magnitude of the income increase but also, and perhaps more importantly, for the breadth of the gains, encompassing all economic and social classes.

Tighter Labor Market

The question is why has it taken so long for real incomes to rise and spread so broadly throughout all income groups? After all, the economy started to generate positive job growth in 2010, and the increases in subsequent years have compared favorably with recent upturns. One likely explanation is that the job market climbed out of an astonishingly deep hole following the Great Recession, which left an army of unemployed workers competing for jobs. While the unemployment rate fell rather swiftly, the descent began from an elevated 10 percent peak in 2009, only a tad below the 10.8 percent postwar high set in 1982.

Historically, anything above 6 percent means that employers have an ample pool of job-seekers to tap into and, hence, have little incentive to jack up wages to attract new workers. Conversely, with few opportunities to go elsewhere, existing workers have neither the bargaining power to demand higher wages nor the confidence to quit their jobs for higher salaries at other firms. But once the jobless rate pierces through 6 percent, the labor market becomes sufficiently tight to shift the balance of power. Not coincidentally, the rate slipped through 6 percent heading into 2015 on the way down to 5 percent by the end of the year.

Simply put, a good deal of slack had been wrung out of the labor market during 2015. With the oversupply of labor whittled down, an increasing number of companies, particularly smaller ones, reported difficulty finding qualified workers. Unfilled positions surged to a record 5.78 million by July and job hopping picked up considerably, with the number of workers voluntarily quitting reaching the highest level in fifteen years. Just as the less-skilled workers are the first to get pink slips when a weakening economy cuts the demand for labor, so too do they benefit the most when the job market tightens up. It comes as no surprise that many high-profile firms are voluntarily boosting the minimum wage for their workers, in many cases outdoing the legislated increases implemented by a broadening number of states.

Continued Progress

The annual Census figures on income and poverty only goes through 2015; by all accounts, however, the trend set last year has continued into 2016. True, the pace of job increases has slowed from last year – from a monthly average of 229 thousand to 182 thousand through August – but that's to be expected as the supply of available labor shrinks. The current pace of payroll increases still exceeds the number of new entrants to the labor market, estimated at about 120 thousand a month. Hence, the labor market continues to tighten, a good sign that wage pressures will continue to build.

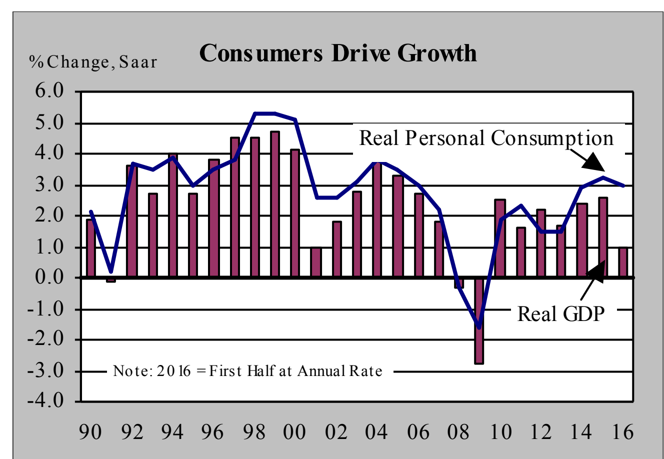
Importantly, with more of the gains accruing to lower-income households, the impact on consumer spending should be greater than otherwise. That's because the poorer segment of the population spends almost every penny of their paycheck, whereas the more affluent households puts some aside in savings. Hence, the income boost favoring the lower wage earners delivers a bigger bang for the buck in terms of consumer spending, which is the economy's main growth driver. Indeed, to say that consumers are propping up the economy would be an extreme understatement. While gross domestic product grew by a measly 1 percent annual rate over the first half of this year, consumer spending increased by 3 percent. If sustained for the entire year, that disparity would be the widest since 1982.

Needless to say, it is imperative that household purchasing power continues to strengthen, given the economy's heavy reliance on consumer spending. Odds are, worker pay will benefit as the labor market tightens further. However, the gain in real incomes last year was also helped by low inflation, reflecting the drop in energy prices. That positive input is now reversing; oil and gasoline prices have steadied this year, and climbing medical and housing costs are driving up inflation. Indeed, rising inflation is already diluting pay increases. Real average hourly earnings for all employees fell in August, lowering the annual increase to 1.3 percent from 1.9 percent in 2015.

Election Uncertainty

Clearly, for incomes to keep pace with inflation, the pick- up in worker earnings underway last year will have to continue. That means even more slack will have to be wrung out of the labor market, spurring companies to keep on boosting worker pay. Of course, the labor market will continue to tighten only if it is supported by stronger economic growth, which both underpins the demand for workers and provides companies with the profits to absorb higher labor costs. The economy appears to be on a faster growth track, thanks to stronger contributions from housing activity, some inventory rebuilding and government spending.

But the biggest headwind continues to be the absence of business investment, reflecting the contraction in energy-related spending on oil rigs and mining equipment over the past two years, as well as the lack of incentive to expand capacity in a slowly growing global environment. Oil prices have stabilized, stemming the cutbacks in the energy sector. However, corporate leaders remain very cautious about expanding capital budgets, largely due to election uncertainty as both presidential candidates are espousing restrictive trade policies that in their eyes would inhibit growth. That mind-set would change abruptly if the expected second-half pick-up in growth were sustained through the elections. It looks like consumers with some help from the housing sector will have to continue their heavy lifting for a while longer.



KEY ECONOMIC AND FINANCIAL INDICATORS

*FINANCIAL INDICATORS**

	August	July	June	May	April	March	February	12-Month Range High	12-Month Range Low
Prime Rate	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.50	3.25
3-Month Treasury Bill Rate	0.30	0.30	0.27	0.27	0.23	0.29	0.31	0.31	0.02
5-Year Treasury Note Rate	1.13	1.07	1.17	1.30	1.26	1.38	1.22	1.70	1.07
10-Year Treasury Note Rate	1.56	1.50	1.64	1.81	1.81	1.89	1.78	2.32	1.50
30-Year Treasury Bond Rate	2.26	2.23	2.45	2.63	2.62	2.68	2.62	3.07	2.23
Tax-Exempt Bond Yield	2.85	2.83	3.20	3.29	3.30	3.38	3.30	3.79	2.83
Corporate Bond Yield (AAA)	3.32	3.28	3.50	3.65	3.62	3.82	3.96	4.15	3.28
Conventional 30-Year Mortgage Rate	3.44	3.44	3.57	3.60	3.61	3.69	3.66	4.05	3.44
Dow Jones Industrial average	18495	18341	17755	17692	17844	17302	16300	18495	16300
S&P 500 Index	2177	2149	2084	2067	2076	2022	1918	2177	1918
Dividend Yield (S&P)	2.11	2.11	2.17	2.16	2.18	2.17	2.31	2.31	2.11
P/E Ratio (S&P)	20.4	20.4	19.8	19.5	19.2	19.1	17.6	20.4	17.4
Dollar Exchange Rate (vs. Major Currencies)	89.8	90.9	89.7	89.8	89.4	91.5	93.2	94.1	89.4

** Monthly Averages*

ECONOMIC INDICATORS

	August	July	June	May	April	March	February	12-Month Range High	12-Month Range Low
Housing Starts (In Thousands)	1142	1212	1195	1128	1155	1113	1213	1213	1073
New Home Sales (Thousands of Units)		654	582	572	570	537	525	654	457
New Home Prices (Thousands of Dollars)		295	311	291	321	311	311	321	291
Retail Sales (% Change Year Ago)	2.1	2.3	2.8	2.2	2.9	1.7	3.6	3.6	1.6
Industrial Production (% Change Year Ago)	-1.1	-0.6	-0.6	-1.2	-1.3	-2.0	-1.4	0.4	-2.3
Operating Rate (% of Capacity)	75.5	75.9	75.5	75.1	75.2	74.9	75.6	76.7	74.9
Inventory Sales Ratio (Months)		1.39	1.39	1.40	1.40	1.41	1.41	1.41	1.38
Real Gross Domestic Product (Annual % Change)			1.1			0.8		2.0	0.8
Unemployment Rate (Percent)	4.9	4.9	4.9	4.7	5.0	5.0	4.9	5.3	4.7
Payroll Employment (Change in Thousands)	151	275	271	24	144	186	233	295	24
Hourly Earnings (% Change Year Ago)	2.4	2.7	2.6	2.5	2.5	2.3	2.4	2.7	2.3
Personal Income (% Change Year Ago)		3.3	3.1	3.2	3.4	3.6	3.5	4.2	3.1
Savings Rate (Percent of Disposable Income)		5.7	5.5	5.8	5.8	6.2	6.0	6.2	5.5
Consumer Credit (Change in Mil. Of Dollars)		17713.0	14529	22570	20483	23163	13860	23163	6561
Consumer Prices (% Change Year Ago)	1.1	0.8	1.0	1.0	1.1	0.9	1.0	1.1	0.0
CPI Less Food & Energy (% Change Year Ago)	2.3	2.2	2.3	2.2	2.1	2.2	2.3	2.3	1.8
Wholesale Prices (% Change Year Ago)	0.0	-0.2	0.3	-0.1	0.0	-0.1	0.0	0.3	-1.6

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