

# Volcker II, Vladimir, The Virus and SVB

Economic Development Partners Breakfast

March 23, 2023

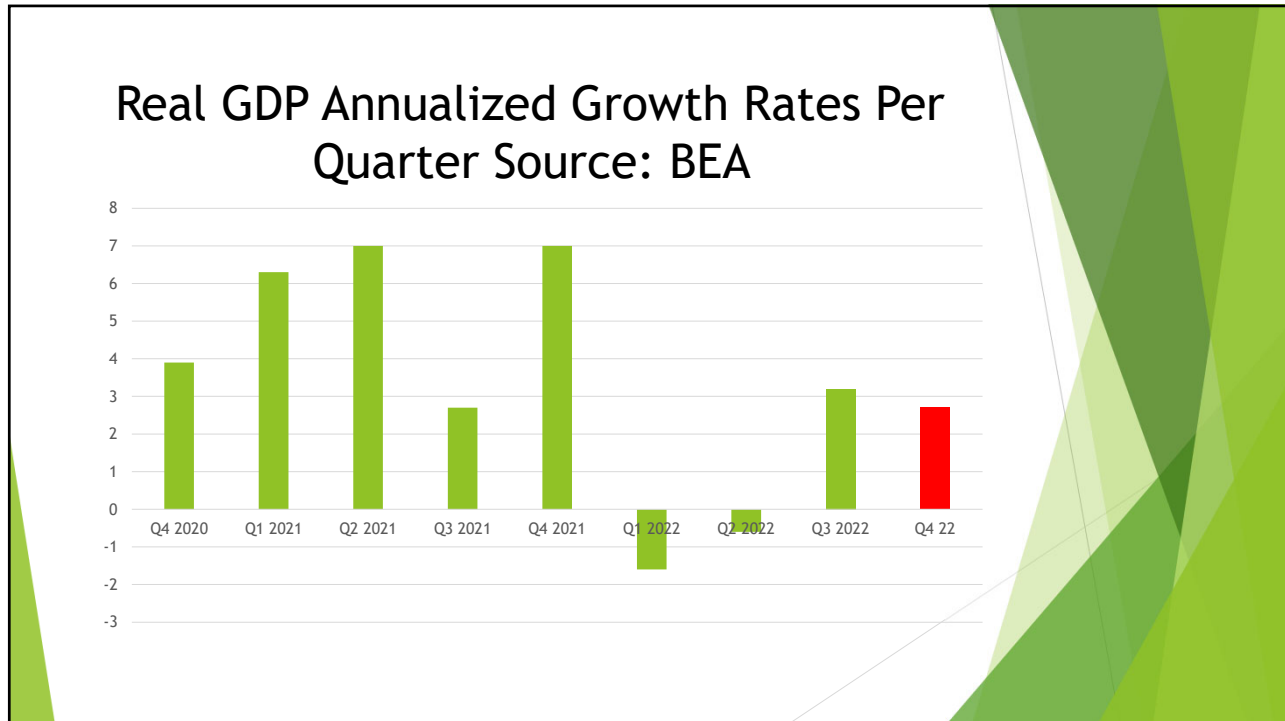
John W. Mitchell

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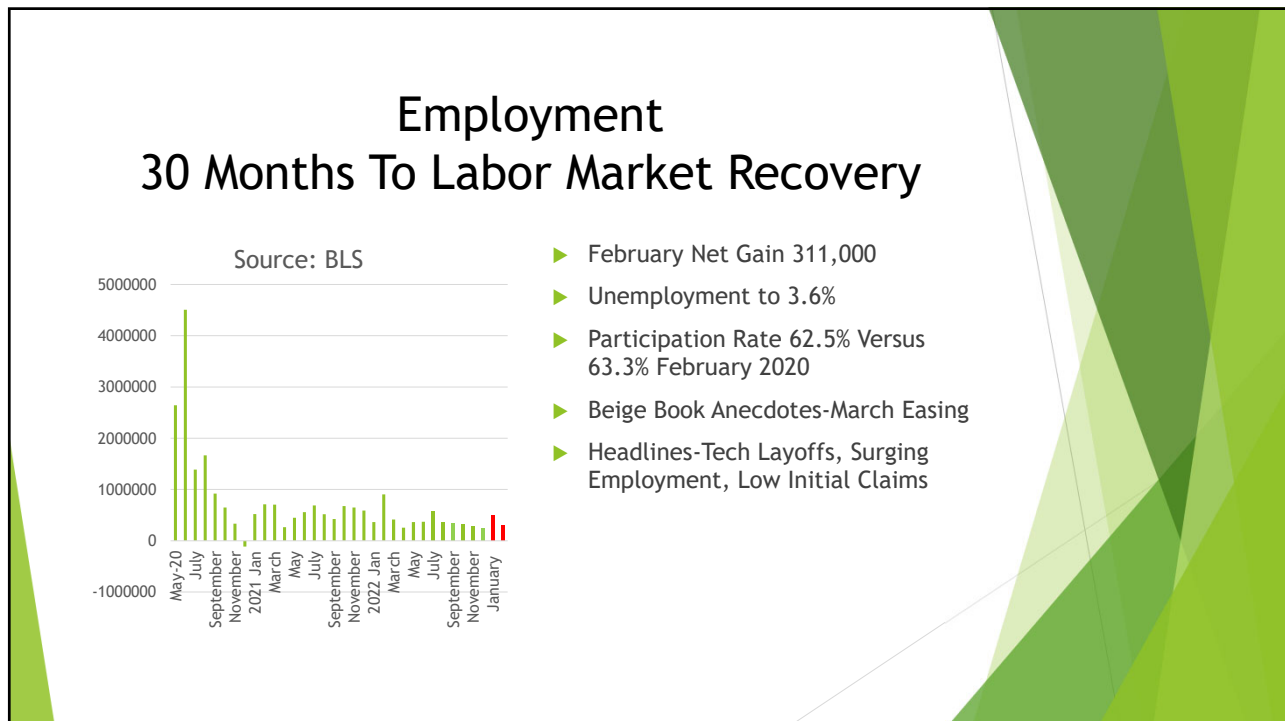
## March 2023

- ▶ For Many The Lowest Unemployment Rate and the Highest Inflation Rate of Their Lives in the last 9 Months
- ▶ Second Year of War in Europe
- ▶ The Federal Reserve Tightening-Reminiscent of the Early 1980s
- ▶ Policy Changes in Place to Restructure the US Economy
- ▶ Debt Ceiling Collision
- ▶ High Levels of Uncertainty about The Economy's Course
- ▶ Balloons, Silicon Valley Bank, March Madness
- ▶ Yesterday's Meeting?

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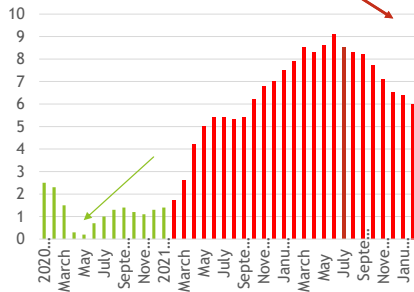
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## Annual Change CPI 2020-23

February CPI 6% Core 5.5%  
PCE January 5.4% Core 4.7%

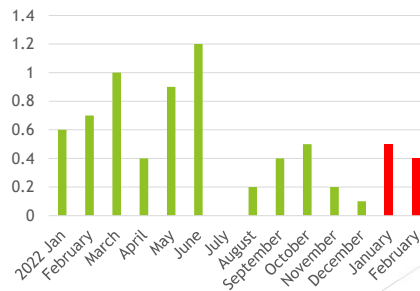
### Year over Year CPI Change

Source: BLS



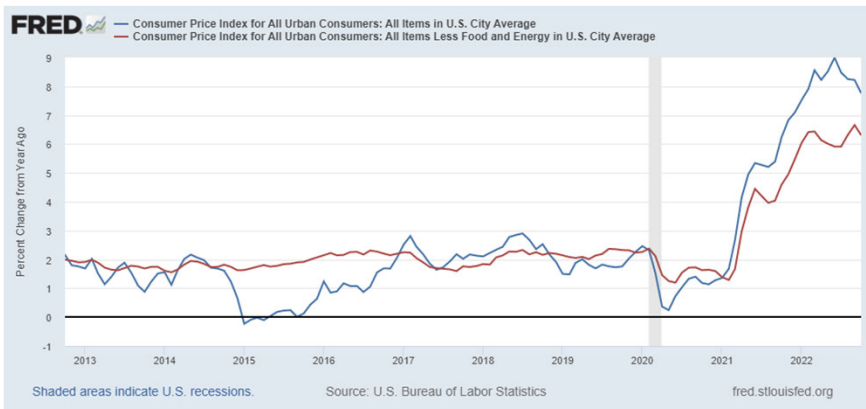
### Monthly Change 2022-3

Source: BLS



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## The Last Decade The Shock!



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## The Whys A Confluence of Events

- ▶ Pandemic Supply Impacts-Shut Downs, Supply Chain Interruptions, Demand Shifts ( Inability to Respond to Price Changes!)
- ▶ The Long Term Pattern of Weak Goods Prices Ended for a While
- ▶ Weather and Plagues like Avian Flu
- ▶ Energy Shocks-Pre-War
- ▶ Post February 24<sup>th</sup>-Invasion-Energy, Food, Metals
- ▶ Trillions in Stimulus-Omnibus Covid Relief Act \$900 Billion in December 2020, American Rescue Plan \$1.9 Trillion in March 2021, Monetary Ease-Rates and Quantitative Easing

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The FOMC “ overarching focus right now is to bring inflation back down to our 2 percent goal. Price stability is the responsibility of the Federal Reserve and serves as the bedrock of our economy.” Powell at Jackson Hole August 2022

The Committee anticipates that **ongoing increases** in the target range will be appropriate in order to attain a stance of monetary policy that is sufficiently restrictive to return inflation to 2 percent over time. 2/1/23  
Then Came SVB!

- ▶ 8 Rate Increases and End of QE now QT from \$120 Billion Buying per Month to \$95 Billion Run Off
- ▶ Implications-Transmission Mechanisms
  - ▶ Interest Sensitive Spending: Housing, Durables, Credit Cards
  - ▶ The Credit Channel-Tightens
  - ▶ The Dollar
  - ▶ Asset Prices
  - ▶ This is Paul Volcker Redone

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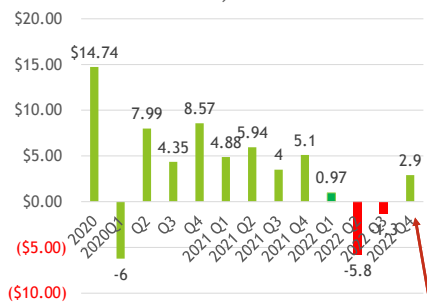
## SVB and Aftermath

- ▶ Failure of Asset/Liability Management
- ▶ Risk Free Paper Example
- ▶ Rapid Massive Withdrawals-Had Many Large Depositors-Industry Concentration
- ▶ Very Rapid Before Could Liquidate Assets or Get Capital
- ▶ Policy Response To Guarantee All Deposits in SVB and Signature-Bank Term Funding Program to Support Liquidity Needs
- ▶ Increased Perceived Risk

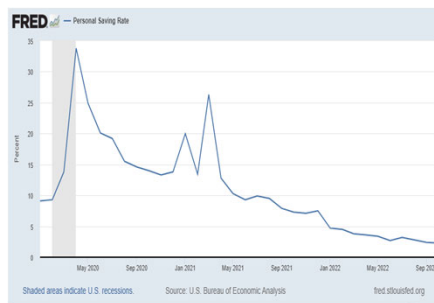
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## Households-Stocks, Bonds Financial Assets Down \$2.8T in Q1, -\$7.6T in Q2 and -\$2.1T in Q3, up \$2.7T in Q4 Changes in Net Worth HH & Non-Profits (Trillions)

Source; Fed



## Savings Rate

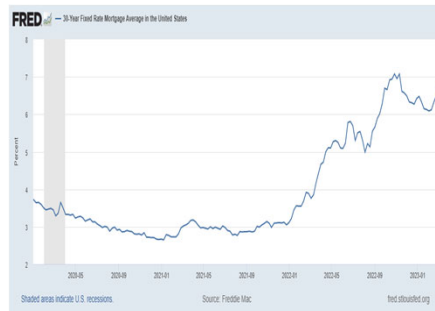


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## The Housing Boom Ends (But Not Like The Last Time!)

- ▶ July to August The largest Deceleration in S&P Core Logic Case Shiller History US Home Prices -2.6% - June to July the Second Largest Deceleration, down again in September, October, November and December
- ▶ All 20 Cities Down over the Month
- ▶ Existing Home Sales Falling 12 Months-Median Home Prices Declining
- ▶ Jan-Feb of 2023 Permits down 20.1% YoY

### 30 Year Fixed Rate Mortgage



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## WCRER and FHFA House Price Index Q4 22

- ▶ WCRER Q4 Data
- ▶ Resales Chelan -2.8%, Douglas -9.8% Over the Year State -14.6%
- ▶ Median Resale Chelan \$584,400 up 8.4%, Douglas \$442,900 -.9%
- ▶ Census Permits Wenatchee 2022 864, 2021 1,000 2020 991

	Year	Quarter	Rank
WA PO	3.7	-1.82	47
Bellingham	6.42	-4.17	233
Bremerton	6.64	-3.27	230
Longview	11.37	1.59	125
Olympia	7.86	-3.3	218
Seattle	6.22	-3.59	236
Spokane	8.95	-2.28	194
Tacoma	5.45	-3.74	240
Tri-Cities	11.27	-1.23	129
Wenatchee	9.66	-.35	180
Yakima	7.88	.67	217

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## Fiscal Policy

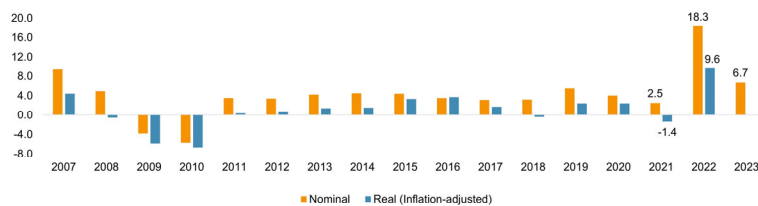
- ▶ In 2020 CARES Act, Omnibus Covid Relief Act (\$900 B in 12/20 and in 2021 the \$1.9 Trillion-American Rescue Plan
- ▶ 2021 Infrastructure Bill about \$1 Trillion-\$110 Billion for Roads Bridges, Funds for Public Transit, Rail Improvements, Electric Charging Stations, Broadband Access
- ▶ CHIPS Act-2022 Subsidies, Incentives for Semiconductor Production and Government Sponsored Research- New Industrial Policy-Partly Pandemic Legacy
- ▶ “Inflation Reduction Act”-Climate Bill, Corporate Tax Increase, IRS, Drug Price Controls, Extend Insurance Subsidies-Restructure The US Economy
- ▶ Debt Forgiveness in Courts-\$420 Billion Deficit Increase
- ▶ Omnibus Bill Passed \$1.7 Trillion for Fiscal 2023
- ▶ Federal Spending 2019 \$4.45T, 2020 \$6.55T, 2021 \$6.82T , 2022 \$6.27T CBO
- ▶ CBO Total Deficits 2023- 2033 \$21.6T
- ▶ Debt Ceiling Reached 1/19/23-Congressional Battle

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## State Funds Forecast Council: State of WA Revenues up 20.4% 2019-21 and 2021-2023

### Fiscal 2023 Enacted Budgets Show Continued Growth After Largest Spending Increase on Record in Fiscal 2022

Annual General Fund Spending Changes, Fiscal 2007 To Fiscal 2023 (Percentage Change)



Note: Fiscal 2023 figure is based on states' enacted budgets.

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## MISTAKES with 20/20 Hindsight

- ▶ Expected More Transitory Elements on the Inflation Side-Supply Chain Fixes
- ▶ Missed The Tightness in the Labor Market
- ▶ Should Have Reacted Sooner to Excessive Fiscal/Monetary Stimulus
- ▶ Perhaps Lulled by the long period of inflation being below target. August 27, 2020 FAIT Introduced
- ▶ Not Enough Attention to the Unwinding of Years of Low Interest Rates

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### Job Growth Update January 2023 Data Year over Year Change - 50 States Up Source: BLS, ASU

- |                     |                     |                    |
|---------------------|---------------------|--------------------|
| ▶ Nevada 1          | ▶ New Jersey 17     | ▶ Kentucky 33      |
| ▶ Texas 2           | ▶ Arkansas 18       | ▶ Iowa 34          |
| ▶ Florida 3         | ▶ Arizona 19        | ▶ Wyoming 35       |
| ▶ Tennessee 4       | ▶ Delaware 20       | ▶ Minnesota 36     |
| ▶ WASHINGTON 5      | ▶ Pennsylvania 21   | ▶ Nebraska 37      |
| ▶ Hawaii 6          | ▶ Virginia 22       | ▶ Michigan 38      |
| ▶ New York 7        | ▶ South Carolina 23 | ▶ North Dakota 39  |
| ▶ Kansas 8          | ▶ Missouri 24       | ▶ Maine 40         |
| ▶ Oregon 9          | ▶ New Mexico 25     | ▶ Vermont 41       |
| ▶ Georgia 10        | ▶ Oklahoma 26       | ▶ Connecticut 42   |
| ▶ North Carolina 11 | ▶ Utah 27           | ▶ Colorado 43      |
| ▶ New Hampshire 12  | ▶ Montana 28        | ▶ Louisiana 44     |
| ▶ California 13     | ▶ Indiana 29        | ▶ Wisconsin 45     |
| ▶ Alaska 14         | ▶ Illinois 30       | ▶ Rhode Island 46  |
| ▶ Idaho 15          | ▶ South Dakota 31   | ▶ Mississippi 47   |
| ▶ Massachusetts 16  | ▶ Alabama 32        | ▶ Ohio 48          |
|                     |                     | ▶ Maryland 49      |
|                     |                     | ▶ West Virginia 50 |

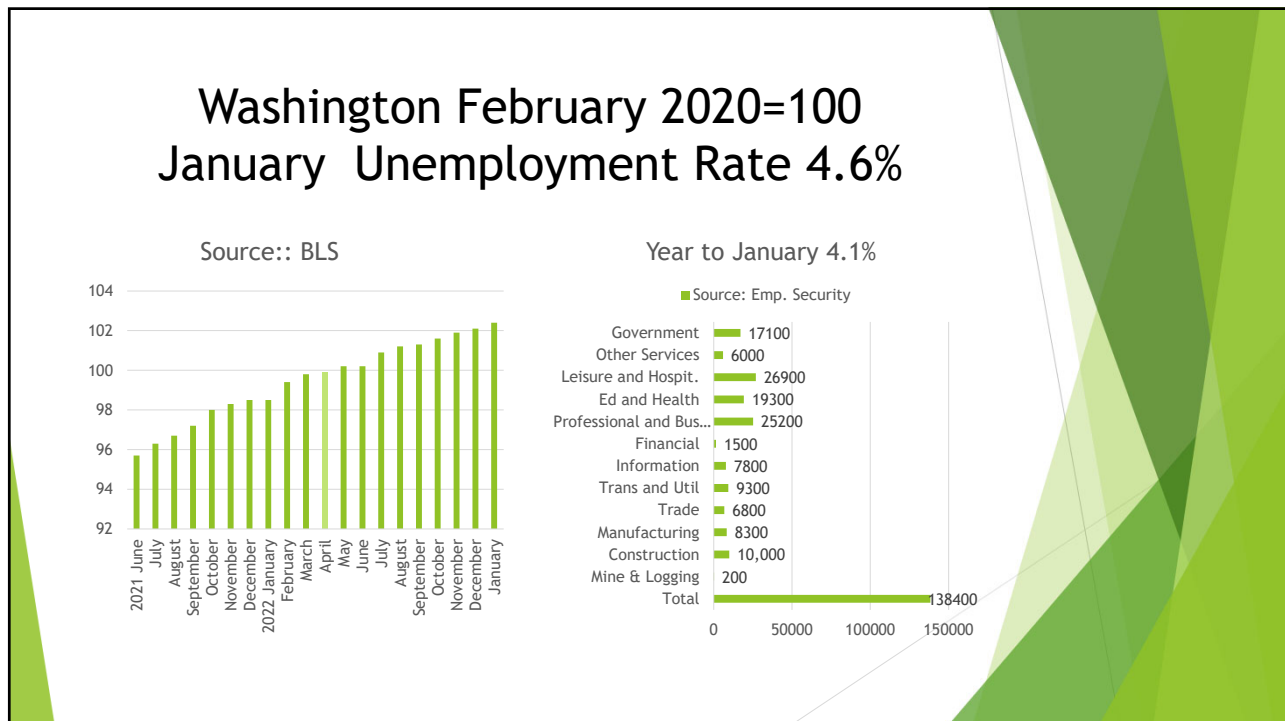
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- ▶ April, 2001 Month 1 of 8 Month Recession 14 States Declining
- ▶ January, 2008 Month 1 of 18 Month Recession 7 States Declining
- ▶ March, 2020 Month 1 of 2 Month Recession 22 States Declining
- ▶ Now NONE

- ▶ The labor market experience is different.
- ▶ Job Openings in January 10.8 Million down from 11.2 Million in December
- ▶ Holding on to People after the last 2 Years

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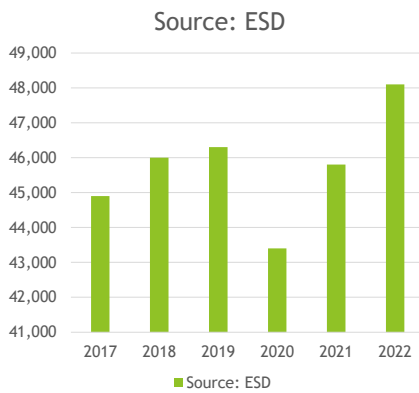
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## Metros to January 23

	Jobs	%		Jobs	%
Bellingham	3,400	3.7	Spokane	6,800	2.7
Bremerton	2,500	2.7	Tacoma	10,400	3.2
Cowlitz	2,100	5.1	Tri-Cities	5,900	5
Olympia	6,300	5.9	Wenatchee	2,700	5.9
Skagit	1,700	3.5	Yakima	4,000	4.7
Seattle	73,100	4.3	Source: BLS,ESD		

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## Wenatchee Employment, Income & Price Parity



- ▶ Wenatchee Employment in January 2023 107.4 with February 2020 =100
- ▶ Personal Income up 7.6% in 2021, 10.1% in 2020 and 5.5% in 2019
- ▶ Transfers up 15.7% in 2021, 31.2% in 2020 and 7.7% in 2019
- ▶ Price Parity US =100
- ▶ Wenatchee 2019 104.3 2020 102.55 and 2021 103.11
- ▶ Sources: BEA, BLS

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## The Ag Sector Potatoes, Tree Fruits, Grains, Cattle, Dairy, Wine

	2019	2020	2021
Net Farm Income			
WA	3B	2.8B	3.34B
Source: USDA			

- ▶ USDA Expects Farm Income in 2022 to be up 15.5% after a 49.2% Increase in 2021-Lower Income in 2023, but another strong year
- ▶ Real Farm Income in 2023 expected to be 26.6% above 2002-2021 Average

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## The Changing Population Flows Census

	2018-19	19-20	20-21	21-22	21-22 Growth
Washington	87,231	79,588	16,714	45,041	.6
Idaho	36,988	37,853	56,112	34,719	1.8
California	147	-69,532	-358,662	-113,649	-.3
Texas	362,230	373,965	326,390	470,708	1.7
Florida	237,130	241,256	238,467	418,754	1.9
Oregon	32,578	25,391	11,506	-16,164	-.4

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## Combing Through The Data

- ▶ The Fed has Shifted Gear-8 Rate Increases-Higher Rates Working Through the System-Lags Long and Variable-Public Statements-Not Done Yet
- ▶ Inverted Yield Curve-Short Term Rates above Long Term
- ▶ Supply Chains Improving-Shipping Rates, Availability
- ▶ Global Developments: China Relaxing Covid Restrictions-Massive Outbreaks, Europe Coping with Energy Cut Offs, Trade Barriers Rising-IRA, Border Adjustment Carbon Taxes, Buy American
- ▶ Tight Labor Markets-Initial Claims Still Low
- ▶ Headline Inflation Falling Since June Peak-January and February Above Expectations
- ▶ Leading Indicators Falling
- ▶ Beige Book-March-softening, inflation slowed, easier to hire
- ▶ Chinese Rebound?
- ▶ Bank Failure Impact?

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## At Least A Slowdown Most Likely a Recession and Slide into a Different World

- ▶ In 2022 GDP Growth 2.1% Down from 5.9% in 2021 and 0-1.5% in 2023
- ▶ CPI Inflation 8% in 2022 Up from 4.7% in 2021 and 3.5-4.5% in 2023
- ▶ Washington in 2022 4.7% Employment Growth and Consensus 23 1.5%
- ▶ NABE February Forecast 3.2% Point Difference 5 Highest and Lowest for 2023 GDP
- ▶ Implications of SVB Failure and Worries-still sorting out- Asset Values, Risk Perception, Watch Labor Market Data, Inflation

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## Can Inflation be Brought Back down Without a Recession?

- ▶ *Soft Landers or Now “No Landers”*
- ▶ The Labor Market Strength  
Moderation of Wage Increases
- ▶ Balance Sheet Strength
- ▶ Inflation Moderating-Transitory Forces Pass
- ▶ Supply Chains Improving
- ▶ Inflation Expectations Anchored
- ▶ Not a Financial Crisis (?)
- ▶ Fed Pivot
- ▶ *The Hard Landers*
- ▶ Tightening of Monetary Policy Not Over Yet-Lags Long and Variable
- ▶ Wage Increases not Consistent with 2% Inflation
- ▶ Inflation will be Difficult to Restrain-Higher Longer
- ▶ Depleting Savings from 20-21, Wealth Hit
- ▶ SVB Fallout

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## The Pandemic’s Legacy

- ▶ Labor Force Reduction
- ▶ Supply Chain Re-Evaluation-More Inventory, Alternatives, Friend Shoring, Security-Implies Higher Prices-Globalization Shift Out of China to SE Asia, North America
- ▶ Demonstrated Alternative-Business Arrangements and Locational Patterns-Hybrid-Distribution Models
- ▶ Broken Agreements, Forbearance, Deferrals, Rent Holidays, Payment Suspensions
- ▶ Income without Work or Production-Stimmies, Unemployment Comp More Than Earnings, Reduced Work Requirements- Long Term Implications
- ▶ Next Shock? Policy Response
- ▶ Educational Disruption-Long Lasting-National Assessment Educational Progress

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## PLUS

- ▶ Tri-Polar World-Two Run by Dictators-Dealing with Russia and Preparing for China (USNI)-Implies Higher Defense Spending-Co-operation with Allies
- ▶ Divided Government
- ▶ Aging Population-Slower Labor Force Growth-Not sure we have come to grasp this yet. What combination of goods and services and people will cross borders?

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## Looking Back From The 2030s

- ▶ Will the Supply Chain be Able to Respond to New Rules put in Place for EV's and Investment? Dramatic Change from Postwar Stance on Trade Barriers
- ▶ Subsidy Wars?
- ▶ Drug Industry and Price Controls?
- ▶ Industrial Policy Implementation-Union Labor, Limit Stock Buy Backs and Dividends., Child Care, US Iron and Steel- Government Decisions
- ▶ Are we throwing away our advantage?
- ▶ How will we cope with aging workforce? Automation/Immigration
- ▶ What will the Fed's inflation target be?
- ▶ What will Wenatchee have done with its green power?
- ▶ What will you be driving?
- ▶ What will the Black Swans have been?

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