

## **Regime Change, Risk Factors and a Really Strong Start for 2018**

St. Louis Federal Reserve Bank President Jim Bullard is talking about regime change. Not political regimes, but economic regimes. Bullard is focused on the factors that drive monetary policy, but his broad concept of regime change is very useful now when thinking about the overall U.S. economy.

Within the world of monetary policy it is easy to see that we are in a new regime. The Federal Reserve went into crisis mode in late 2006 when it dropped the fed funds rate to near zero. It took until the end of 2015 to change that. In the meantime, the Fed initiated three rounds of asset purchases and expanded their balance sheet from about \$1 trillion, to \$4.5 trillion. Not only did the Fed press short-term interest rates to historical lows during that nine-year period, they also exerted significant influence over the long-end of the yield curve through asset purchases. In the new regime, the Fed is pushing up short-term rates with increases in the fed funds rate, at the same time that it is winding down its balance sheet, putting some upward pressure on the long end of the yield curve.

In addition to the U.S. Federal Reserve trying to normalize U.S. monetary policy, the European Central Bank is also gradually winding down its extraordinary policy. As the ECB further reduces their asset purchases this year, they too will put upward pressure on bond yields.

The fiscal policy regime has also changed. The recently signed two-year federal budget deal, along with tax reform, is expected to push out the federal budget gap. Most neutral sources estimate that the new fiscal regime will widen the federal deficit over the long term. This would require the Treasury Department to issue more bonds, putting upward pressure on interest rates as bond supply increases.

Inflation indicators are warming up gradually. As they do, financial market volatility is increasing. The historically low financial market volatility of 2017 may already be a thing of the past.

The Trump Administration is also disrupting trade regimes. A more assertive trade policy from the Trump Administration may yet bring countermeasures by our trading partners.

Finally, as we discussed previously, we are now more than 10 years out from the start of the Great Recession. Historically, that demarcation is associated with a regime change toward improved economic performance.

Even with a strong start to 2018, economic risk factors remain. By this May, we will be in the second longest U.S. economic expansion ever as we reach 107 months. By many metrics, this feels like a mid-to-late cycle economy.

However, the labor market is not cooling off. For a few years now, the consensus view among macroeconomists was that labor demand would gradually ease by this point in time, to something on the order of 100,000 to 120,000 net new jobs per month, or less. In the February labor data we saw the opposite. Payroll job growth was robust, up 313,000 for the month. Net revisions to December and January were +54,000, to bring average payroll job growth for the last three months to over 242,000 per month. Sizeable increases in the household employment survey and in the labor force kept the unemployment rate at 4.1 percent for the fifth consecutive month. We still expect the unemployment rate to drop below 4 percent this year, but the pace of declines appears to be slowing, yet another sign of economic regime change. Wages increased only moderately, by 0.1 percent in February, after jumping by 0.3 percent in January.

### **U.S. Economic Outlook, Summary**

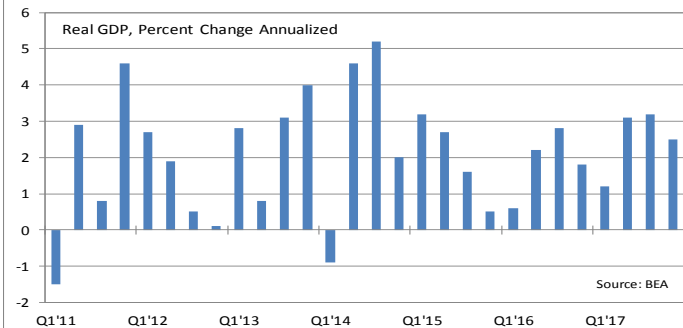
	3Q'17a	4Q'17a	1Q'18f	2Q'18f	3Q'18f	4Q'18f	1Q'19f	2Q'19f	2017a	2018f	2019f
Real GDP (Percent Change Annualized)	3.2	2.5	2.6	3.4	2.9	2.5	2.3	2.3	2.3	2.9	2.5
CPI (Percent Change Year-over-Year)	2.0	2.1	2.3	2.7	2.7	2.3	1.9	2.0	2.1	2.5	2.0
Payroll Jobs (Average Monthly Diff., Ths.)	184.3	185.4	223.8	179.4	162.8	155.6	150.6	142.2	181.4	180.4	162.1
Unemployment Rate (Percent)	4.3	4.1	4.1	4.0	3.9	3.8	3.8	3.7	4.3	3.9	3.7
Federal Funds Rate (Effective)	1.15	1.20	1.43	1.67	1.91	2.13	2.17	2.42	1.00	1.79	2.53
10-Yr. Treasury Rate	2.24	2.37	2.78	2.99	3.09	3.24	3.23	3.44	2.33	3.02	3.55

**a = actual f = forecast**

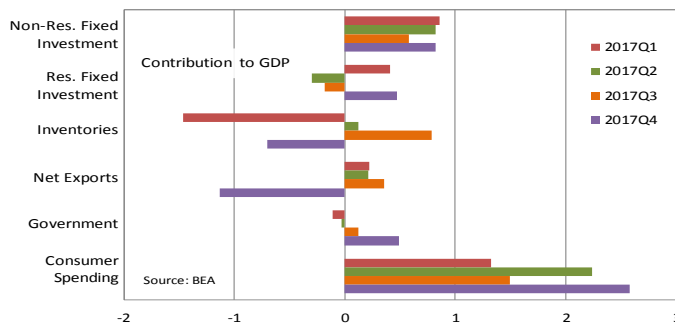
To subscribe to our publications or for questions, contact us at [ComericaEcon@comerica.com](mailto:ComericaEcon@comerica.com). Archives are available at <http://www.comerica.com/insights>. Follow us on Twitter: @Comerica\_Econ.

The articles and opinions in this publication are for general information only, are subject to change, and are not intended to provide specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of Comerica or its management team. We are not offering or soliciting any transaction based on this information. We suggest that you consult your attorney, accountant or tax or financial advisor with regard to your situation. Although information has been obtained from sources we believe to be reliable, neither the authors nor Comerica guarantee its accuracy, and such information may be incomplete or condensed. Neither the authors nor Comerica shall be liable for any typographical errors or incorrect data obtained from reliable sources or factual information.

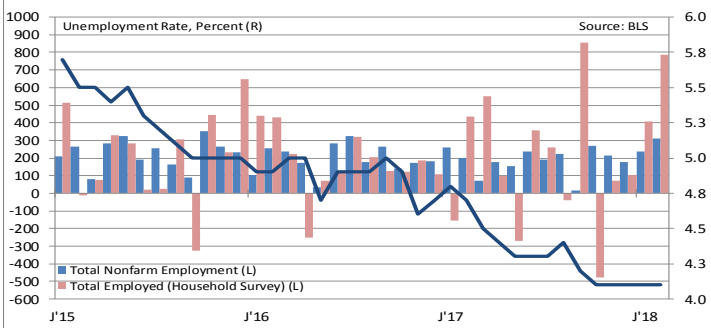
**Q4 GDP 2nd Estimate at 2.5%**



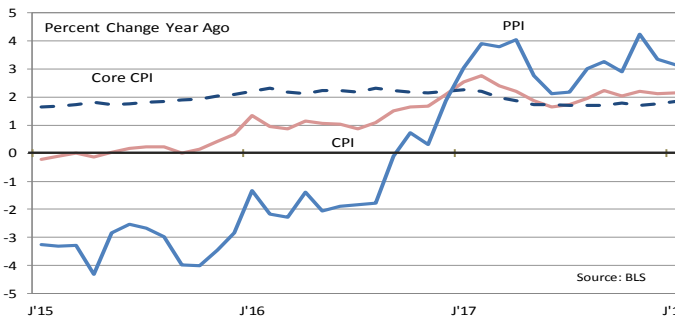
**Q4 GDP Dragged by Imports and Inventories**



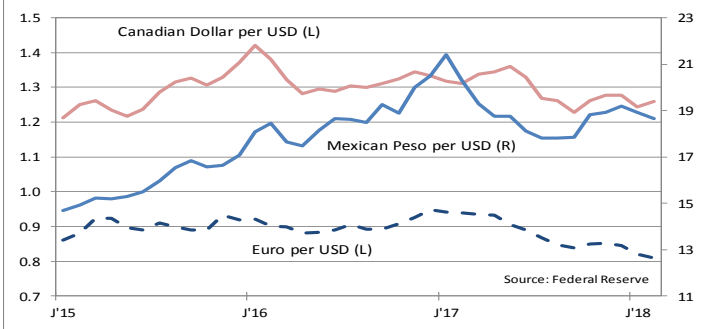
**Blowout Month for Job Growth in February**



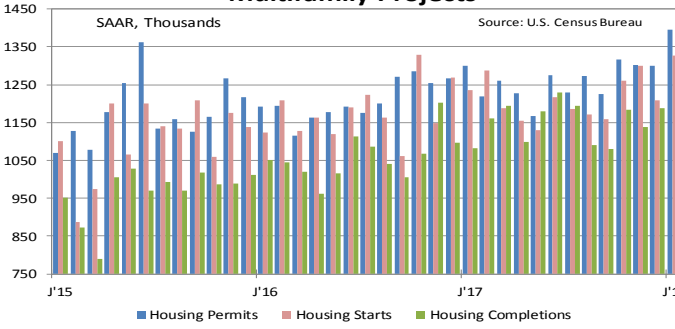
**CPI Inflation Ticking Up**



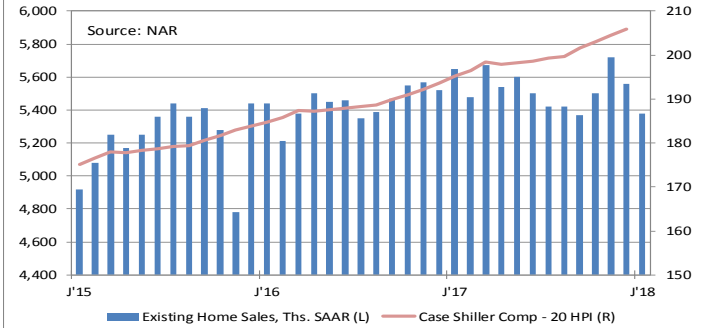
**Mexican Peso Strengthens in Early 2018**



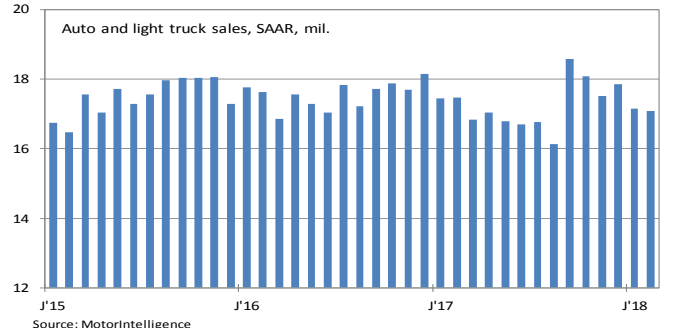
**January Res. Construction Paced by Multifamily Projects**



**Home Prices Advance With Tight Supply**



**Auto Sales Easing After Hurricane Bump**



Subscribe to economics publications and view available archive at <http://www.comerica.com/insights>.

The articles and opinions in this publication are for general information only, are subject to change, and are not intended to provide specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of Comerica or its management team. We are not offering or soliciting any transaction based on this information. We suggest that you consult your attorney, accountant or tax or financial advisor with regard to your situation. Although information has been obtained from sources we believe to be reliable, neither the authors nor Comerica guarantee its accuracy, and such information may be incomplete or condensed. Neither the authors nor Comerica shall be liable for any typographical errors or incorrect data obtained from reliable sources or factual information.

	3Q'17a	4Q'17a	1Q'18f	2Q'18f	3Q'18f	4Q'18f	1Q'19f	2Q'19f	2017a	2018f	2019f
<b>Output</b>											
Nominal GDP (Billions \$)	19501	19736	19970	20243	20500	20728	20946	21168	19386	20360	21279
<b>Percent Change Annualized</b>	<b>5.3</b>	<b>4.9</b>	<b>4.8</b>	<b>5.6</b>	<b>5.2</b>	<b>4.5</b>	<b>4.3</b>	<b>4.3</b>	<b>4.1</b>	<b>5.0</b>	<b>4.5</b>
Real GDP (Chained 2009 Billions \$)	17164	17272	17383	17530	17654	17764	17864	17968	17092	17583	18018
<b>Percent Change Annualized</b>	<b>3.2</b>	<b>2.5</b>	<b>2.6</b>	<b>3.4</b>	<b>2.9</b>	<b>2.5</b>	<b>2.3</b>	<b>2.3</b>	<b>2.3</b>	<b>2.9</b>	<b>2.5</b>
Pers. Consumption Expenditures	11917	12028	12064	12139	12210	12266	12323	12386	11889	12170	12417
<b>Percent Change Annualized</b>	<b>2.2</b>	<b>3.8</b>	<b>1.2</b>	<b>2.5</b>	<b>2.4</b>	<b>1.8</b>	<b>1.9</b>	<b>2.0</b>	<b>2.7</b>	<b>2.4</b>	<b>2.0</b>
Nonresidential Fixed Investment	2327	2364	2404	2449	2485	2517	2548	2578	2314	2464	2590
<b>Percent Change Annualized</b>	<b>4.7</b>	<b>6.6</b>	<b>6.9</b>	<b>7.8</b>	<b>5.9</b>	<b>5.4</b>	<b>5.1</b>	<b>4.7</b>	<b>4.7</b>	<b>6.5</b>	<b>5.1</b>
Residential Investment	587	605	600	607	614	620	626	632	598	610	634
<b>Percent Change Annualized</b>	<b>-4.7</b>	<b>13.0</b>	<b>-3.6</b>	<b>4.9</b>	<b>4.7</b>	<b>4.2</b>	<b>3.8</b>	<b>3.6</b>	<b>1.8</b>	<b>2.1</b>	<b>3.9</b>
Change in Private Inventories	39	8	29	41	50	60	60	60	13	45	60
Net Exports	-598	-652	-632	-635	-643	-648	-651	-654	-621	-639	-657
Government Expenditures	2900	2921	2920	2931	2939	2949	2958	2968	2903	2935	2973
<b>Percent Change Annualized</b>	<b>0.7</b>	<b>2.9</b>	<b>-0.1</b>	<b>1.5</b>	<b>1.2</b>	<b>1.3</b>	<b>1.3</b>	<b>1.4</b>	<b>0.1</b>	<b>1.1</b>	<b>1.3</b>
Industrial Prod. Index (2007=100)	104.8	106.9	107.7	108.2	108.7	109.2	109.7	110.0	105.1	108.5	110.2
<b>Percent Change Annualized</b>	<b>-1.2</b>	<b>8.3</b>	<b>2.8</b>	<b>1.9</b>	<b>2.0</b>	<b>1.9</b>	<b>1.6</b>	<b>1.4</b>	<b>2.0</b>	<b>3.2</b>	<b>1.6</b>
Capacity Utilization (Percent)	76.2	77.5	78.1	78.5	78.8	79.1	79.3	79.5	76.5	78.6	79.5
<b>Prices</b>											
CPI (1982-84=100)	245.3	247.3	249.6	250.6	251.8	253.0	254.3	255.5	245.1	251.3	256.2
<b>Percent Change Annualized</b>	<b>2.1</b>	<b>3.3</b>	<b>3.8</b>	<b>1.5</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>	<b>2.1</b>	<b>2.5</b>	<b>2.0</b>
PCE Price Index (2009=100)	112.7	113.5	114.4	114.8	115.4	116.0	116.6	117.2	112.7	115.2	117.4
<b>Percent Change Annualized</b>	<b>1.5</b>	<b>2.7</b>	<b>3.2</b>	<b>1.7</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>	<b>1.7</b>	<b>2.2</b>	<b>2.0</b>
GDP Price Index (2009=100)	113.6	114.3	114.9	115.5	116.2	116.8	117.3	117.9	113.4	115.8	118.2
<b>Percent Change Annualized</b>	<b>2.1</b>	<b>2.3</b>	<b>2.2</b>	<b>2.2</b>	<b>2.3</b>	<b>2.0</b>	<b>2.0</b>	<b>2.0</b>	<b>1.8</b>	<b>2.1</b>	<b>2.0</b>
Producer Price Index, Finished Goods	197.8	200.7	203.0	203.8	204.9	206.0	207.1	208.1	198.0	204.4	208.6
<b>Percent Change Annualized</b>	<b>1.6</b>	<b>5.9</b>	<b>4.8</b>	<b>1.6</b>	<b>2.2</b>	<b>2.2</b>	<b>2.0</b>	<b>2.1</b>	<b>3.2</b>	<b>3.2</b>	<b>2.0</b>
Crude Oil, WTI (\$/barrel)	51.0	51.0	63.0	62.0	62.0	62.0	62.0	62.0	50.8	62.3	62.0
<b>Labor Markets</b>											
Payroll Jobs (Average Monthly Diff., Ths.)	184.3	185.4	223.8	179.4	162.8	155.6	150.6	142.2	181.4	180.4	162.1
Unemployment Rate (Percent)	4.3	4.1	4.1	4.0	3.9	3.8	3.8	3.7	4.3	3.9	3.7
Average Weekly Hours, Prod. Works.	33.6	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7	33.7
Population (Millions)	326.4	327.0	327.7	328.3	329.0	329.7	330.3	331.0	326.0	328.7	331.3
<b>Percent Change Annualized</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.8</b>	<b>0.7</b>	<b>0.8</b>	<b>0.8</b>
<b>Personal Income</b>											
Average Hourly Earnings (\$)	22.12	22.24	22.38	22.52	22.68	22.84	23.01	23.18	22.05	22.61	23.27
<b>Percent Change Annualized</b>	<b>2.6</b>	<b>2.1</b>	<b>2.5</b>	<b>2.6</b>	<b>2.9</b>	<b>2.9</b>	<b>3.0</b>	<b>3.0</b>	<b>2.3</b>	<b>2.5</b>	<b>2.9</b>
Real Disp. Income (2009 Billions \$)	12787	12822	12883	12986	13065	13142	13223	13304	12763	13019	13345
<b>Percent Change Annualized</b>	<b>0.7</b>	<b>1.1</b>	<b>1.9</b>	<b>3.2</b>	<b>2.5</b>	<b>2.4</b>	<b>2.5</b>	<b>2.5</b>	<b>1.2</b>	<b>2.0</b>	<b>2.5</b>
Personal Saving Rate (Percent)	3.3	2.7	3.0	2.8	2.8	2.8	2.8	2.8	3.4	2.9	2.8
<b>Housing</b>											
Housing Starts (Ths., Ann. Rate)	1172	1256	1286	1308	1324	1338	1349	1360	1208	1314	1364
Ext. SF Home Sales (Ths., Ann Rate)	4793	4960	4898	4904	4921	4934	4949	4963	4910	4914	4969
New SF Home Sales (Ths., Ann Rate)	587	652	623	633	639	645	651	656	615	635	657
Case/Shiller HPI (Jan. 2000=100)	192.5	196.3	199.7	203.2	206.4	209.7	213.0	216.3	191.7	204.8	218.0
<b>Year/Year Percent Change</b>	<b>5.9</b>	<b>6.1</b>	<b>6.2</b>	<b>7.0</b>	<b>7.2</b>	<b>6.8</b>	<b>6.6</b>	<b>6.5</b>	<b>5.9</b>	<b>6.8</b>	<b>6.5</b>
<b>Consumer</b>											
Household Economic Stress Index	0.3	0.1	0.2	-0.3	-0.7	-0.7	-1.0	-0.8	0.6	-0.4	-0.8
Auto Sales (Millions)	17.2	17.8	17.0	16.9	16.7	16.6	16.4	16.3	17.3	16.8	16.2
<b>Interest Rates (percent per year)</b>											
Federal Funds Rate (Effective)	1.15	1.20	1.43	1.67	1.91	2.13	2.17	2.42	1.00	1.79	2.53
Prime Rate	4.25	4.30	4.53	4.77	5.01	5.23	5.27	5.52	4.10	4.89	5.63
1-Month LIBOR	1.23	1.34	1.64	1.84	2.08	2.30	2.34	2.59	1.11	1.96	2.70
3-Month LIBOR	1.31	1.47	1.90	2.16	2.31	2.47	2.48	2.71	1.26	2.21	2.83
1-Yr. Treasury Rate	1.24	1.55	1.94	2.10	2.20	2.36	2.36	2.58	1.20	2.15	2.69
5-Yr. Treasury Rate	1.82	2.07	2.54	2.73	2.83	2.98	2.97	3.18	1.91	2.77	3.29
10-Yr. Treasury Rate	2.24	2.37	2.78	2.99	3.09	3.24	3.23	3.44	2.33	3.02	3.55
30-Year Fixed Rate Mortgage	3.88	3.92	4.27	4.57	4.69	4.84	4.82	5.02	3.99	4.60	5.12

a = actual f = forecast

March 13, 2018

Subscribe to economics publications and view available archive at <http://www.comerica.com/insights>.

The articles and opinions in this publication are for general information only, are subject to change, and are not intended to provide specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of Comerica or its management team. We are not offering or soliciting any transaction based on this information. We suggest that you consult your attorney, accountant or tax or financial advisor with regard to your situation. Although information has been obtained from sources we believe to be reliable, neither the authors nor Comerica guarantee its accuracy, and such information may be incomplete or condensed. Neither the authors nor Comerica shall be liable for any typographical errors or incorrect data obtained from reliable sources or factual information.