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State of the U.S. Economy

The recent election has clearly affected the state of the economy. Janet Yellen, Chair of the Board of Governors of the Federal Reserve System, recently notified Congress that, “…An improving U.S. economy has strengthened the case for raising interest rates.” Her statement, which I agree with, underlines that the economy has improved gradually.

Holding the federal funds rate, the short-term interest rate that banks charge one another for loans, would raise the risks of a recession. The Fed adds securities to the bank’s reserves and takes away credit if it wants to raise rates. The interest rate is so vital because it is the way that the Federal Reserve attempts to control inflation. If there is too much inflation, prices will increase. By increasing the federal funds rate, the Fed attempts to lower the money supply making it more expensive to obtain.

 Evidence can support Yellen’s statement. An indicator affecting the Federal Reserve’s decision of whether or not to raise the interest rates is the unemployment rate. Currently, the Fed has been holding the interest rate close to zero. The percentage of the labor force that is seeking a job but does not have one has decreased. I believe we are in the expansion phase of the business cycle. We have not reached a peak yet because we do not have inflation. During expansion, businesses hire new workers as demand increases which is demonstrated by the recent release of the Employment Situation. There are escalations in health care, professional and business services, and financial activities which are positive signs for a better economy. Most of the data on the BLS website should be seen as positive, in spite of the somewhat slower pace of job growth. Most of this decline may be attributable to retirees aging out of the workforce. I believe that the growth of private sector job growth could lead to more spending. An expansionary fiscal policy can reduce national savings, raise interest rates, and stimulate growth. Additionally, the job market is definitely improving, but clearly not at full employment. This can be supported by the latest release of the U.S. capacity utilization chart. As of October, we are at 75.3% and forecasted to rise to 75.5%. Capacity utilization is a key indicator of aggregate productive capacity. Increasing percentages of capacity utilization means that we are becoming more efficient. The pool of unemployed is decreasing fortunately. Moreover, the current unemployment rate is at 4.9% which means that it is near its natural rate of unemployment. This percentage is not a negative sign since unemployment is inevitable. The economy is always changing. This rate is normal in a regular, well-functioning and dynamic market economy.

Higher GDP and lower inflation rates have aided to the improving health of the economy. The increase in GDP leads to an increasing amount of production, citizens have a higher income, and there is more spending. In fact, GDP has increased to $18,651.2 billion in October from 18,222.8 since its final release from 2015, according to the Bureau of Labor Statistics. Moreover, consumers have seen more or less little inflation. The consumer price index, the measure of the overall cost of g/s bought by a typical consumer, has increased only 0.4 percent in October. Increases in shelter and gasoline indexes were the main factors of the rise in the all items index. When the CPI rises, the typical family spends more money to maintain the same standard of living. A lower CPI, in return, keeps interest rates low, which encourages greater spending. It is at a peak that we see inflation, which, thankfully, is not a trend right now.

Fluctuations in the business cycle are definitely prevalent. As the economy has been steered towards improvement and out of the recession of 2008, real GDP started to expand in the past three years. The unemployment rate has gradually declined, and the rate has fluctuated around its natural rate of about 5 or 6 percent. However, many news resources including the New York Times and U.S. News and World Report believe that the U.S. economy might soon face a recession sometime in the next four years. Though economic fluctuations do not follow a regular, predictable pattern, I assume we are in the expansion phase of the business cycle. Our economy is slowly growing. If the economy grows more than 3% and inflations sends prices up, then we will have reached a peak.

The overall economy is in decent shape. Yellen’s recent speech is an indicator that the U.S. is in a good spot to expand interest rates gradually. Moreover, we are currently around the natural rate of unemployment, the sign of a healthy economy. Hopefully, the upcoming presidential-elect can continue this economic progress.