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September 25, 2023 – Economic Commentary

On September 14, the ECB (European Central Bank) hiked interest rates for the 10th time — and signaled fairly clearly that despite inflation in excess of 5%, the cycle of monetary tightening was done. On September 20th, the FOMC (Federal Reserve Open Market Committee) passed on raising interest rates, in part due to clear improvements in an inflation rate fallen to close to 3% — and Federal Reserve Chairman Powell seemed to go out of his way to create a great deal of uncertainty over whether additional monetary tightening would be forthcoming. It is a tale of two worlds that are supposed to be coordinated, though not necessarily linked in lock-step. Much of the difference between the two regions and the respective monetary authorities has to do with economic growth; in a message delivered by Chairman Powell that somehow got lost in translation, the strength of the US economy is what makes it possible (not "necessary") for the Fed to contemplate another rate hike and fight inflation aggressively, whereas Euro Area economic weakness makes it necessary to pull back on further tightening and have greater patience with inflation. In some ways, this is extreme role reversal. In the 1990s and early 2000s it was Europe, led by the Germans, singularly focused on 2% inflation irrespective of the consequences for economic growth and willing to accept unemployment rates of 12% or greater in order to adhere to the price stability goal of 2%. Europe paid a considerable, unmeasurable price for this policy stance as labor force productivity and business investment lagged that of the US and wide swaths of the population turned into a "lost generation." The US is nowhere close to these kinds of demographic consequences, but business investment is slipping— Chairman Powell specifically cited that development in his remarks last week—and labor force productivity appears to be suffering as a result. The US is the world's strongest economy at the moment, from the standpoint of the combination of size, growth, dynamic diversity and talent, and yet it is the economy with the greatest amount of uncertainty, courtesy of its monetary and fiscal policymakers (let's not forget that the US may be looking at a federal government shutdown in a short six days.)

Data to Watch:

1. US Durable Goods Orders for August, released Wednesday, September 27
2. US PCE (Personal Consumption Expenditure) Price Index for August, released Friday, September 29
3. US Personal Income and Spending for August, released Friday, September 29

Suggested Reading:

1. The east German town at the centre of the new 'gold rush' … for lithium
2. Union Deal With Ford Could Put Pressure on Other 2 Detroit Automakers
3. The Hedge Fund Meltdown That Rescued Your Stock Portfolio