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Is the economic slog really over?

Robert J. Samuelson — Economic Commentary

WASHINGTON — Hello, 2015.

We now are in the sixth year of economic recovery since the end of the Great Recession in mid-2009, says the National Bureau of Economic Research, a group of academic economists that dates business cycles. But, if upbeat economic forecasts come true, this could be the first year that *feels* like a recovery. There would be huge implications. It would soothe Americans' bruised sense of self-worth and alter popular psychology for the 2016 elections.

It's been a slog. Below, you'll find some economic indicators comparing where we are now with the peaks of the last economic expansion, which ended in the fourth quarter of 2007. Generally, the numbers aren't impressive. At best, they show modest gains from those previous peaks.

Consider:

•The economy's annualized output (gross domestic product) of $17.6 trillion is, after adjustment for inflation, only 8.1 percent higher than its peak in the fourth quarter of 2007.

• Payroll employment of 140 million in November exceeded January 2008's 138.4 million by a mere 1.2 percent.

• Industrial production in November was only 6.7 percent higher than the 2007 average.

• New housing starts of nearly 1 million units in 2014 were about half of 2005's peak of 2.1 million units. (But recall: Overbuilding in the early 2000s contributed to the financial crisis.)

• At 5.8 percent in November, the unemployment rate remains well above the low of 4.4 percent in May 2007.

This plodding is over, say many economists. Or soon will be. IHS Economics, a major forecasting firm, predicts that GDP will grow 3.1 percent in 2015 and that monthly job creation will average a solid 230,000. If these gains occur, 2015 will be the recovery's best year. Since 2010, annual GDP growth has averaged only 2.2 percent.

The United States would overshadow Europe and Japan, whose economies are stagnating. "The United States has been faster at deleveraging [reducing household and business debt burdens] and increasing bank capital," argues Nariman Behravesh, IHS' chief economist. Europeans and Japanese are still deleveraging. "As consumer deleverage, they spend less," he says. "As banks deleverage, they lend less."

The U.S. economy would also approach "full employment." That's the lowest level of unemployment consistent with stable inflation. If unemployment falls further, the theory goes, competition among firms for scarce workers will trigger a wage-price spiral. The precise unemployment rate for full employment is uncertain and controversial, though the range is usually put between 4 percent and 6 percent.

Whatever it is, we've been far from it for years. Now we're closer or, perhaps, already there. Unemployment by year-end could be as low as 5.4 percent, says Behravesh. There will also be glad tidings for corporations. Economist Beth Ann Bovino of Standard & Poor's expects operating profits to rise about 6 percent in 2015 and stocks to make a roughly comparable gain.

Naturally, all these predictions won't come true. An old military adage warns that "no battle plan survives contact with the enemy." The same can be said of economic forecasts. None completely survives contact with reality. There's a long history of surprises — for good and ill — obliterating plausible predictions. In 2014, the collapse of oil prices and the war in Ukraine again reminded us of this.

Some threats to the consensus optimism are plain. Economist David Levy of the Jerome Levy Forecasting Center judges there's a 65 percent chance that slumps and slowdowns in Europe, Japan, China and "emerging market" countries will cause a global recession that ultimately drags down the United States. American vulnerability would arise from weaker exports and reduced foreign profits — they represent almost a third of corporate earnings — as well as a general blow to confidence.

The Federal Reserve also poses a danger. It might miscalculate on interest rates. The Fed is widely expected this year to begin raising short-term rates, which have been near zero since late 2008. Fed officials have said the increases would be small and slow so as not to disrupt the recovery. But if investors react by pushing up long-term rates on home mortgages and corporate bonds, the economy could suffer. An even bigger surprise would involve higher inflation that causes the Fed to raise rates more quickly than expected.

It's worth remembering that all this occurs against a backdrop of heightened anxiety bred by the financial crisis and Great Recession. The reaction to these unforeseen calamities was to hunker down — for both consumers and companies to skimp on spending. This is the largest cause of the weak recovery. The question now is whether almost six years of this has had a calming effect — no further disaster has ensued — and restored some optimism. Is the economic slog really over? Or are we just fooling ourselves?

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