Can A Developed Economy Permanently Atrophy?

It is not an encouraging pair of charts: U.S. manufacturing output never returned to 2008 levels, and housing production is off by 45% from pre-2008 Great Recession levels.

Yet some macroeconomists, and evidently the U.S. Federal Reserve, see enough signs of labor-market tightening and price action that they say higher interest rates are warranted. A string of hikes through 2017, no less.

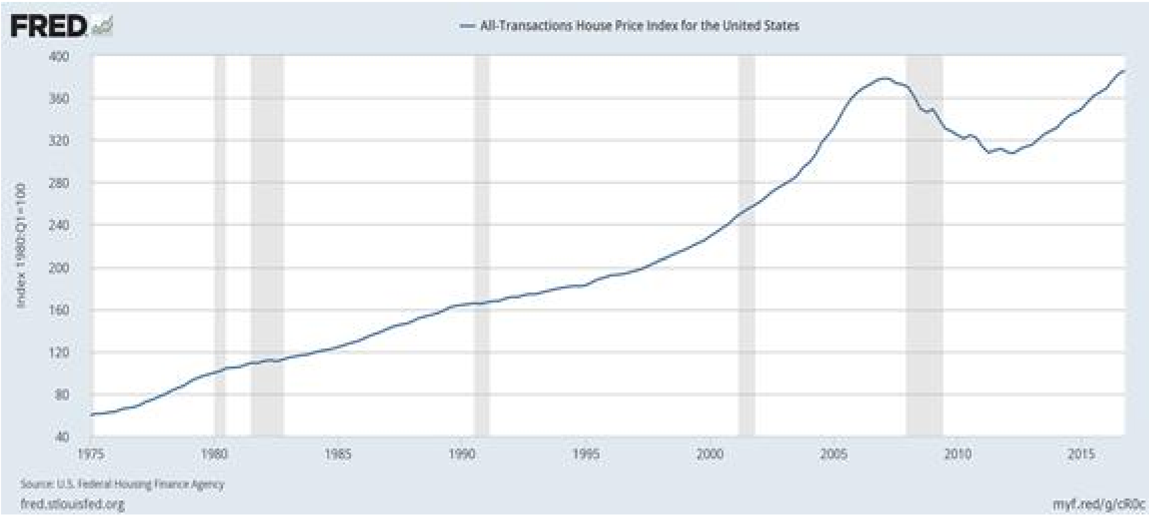
Even some Market Monetarists recite anecdotes of “labor shortages” in manufacturing and construction in endorsing the Fed tightening.

Is the U.S. entering an age of permanent economic atrophy? The U.S. cannot produce as much housing as it did in the 1960s (when the population was about one-third smaller)?

Decline?

One might posit that the reduction in manufacturing output is not vital, as factory goods can be imported. The U.S can trade land, especially housing, for imported goods, and it has been.

Of course, the above housing-production chart suggests selling housing for imported goods might lead to house price run-ups. Well, yes, house prices are now higher than in 2008 and at all-time record highs.



The New York Fed has posited that a nation running trade deficits will see domestic house price booms. Seems to be the case—see London, Sydney, and Vancouver. Try buying a house in Los Angeles. Blogger Tyler Cowen recently noted middle-class Brits could buy a house in the 1990s, a bitterly laughable prospect today requiring 30 years of saving for a down payment.

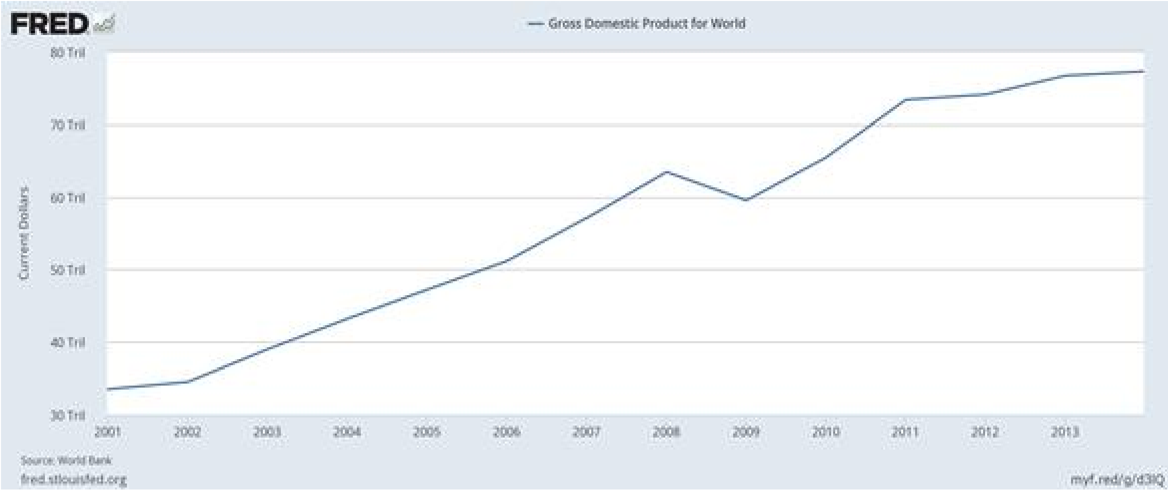
Property-zoning plays a huge role in housing scarcity, btw, yet appears so immutable and embedded as to not be a topic of discussion in macroeconomic circles.

So the US manufactures less than in 2008, builds far less housing, and that same housing is more expensive than ever. Is this a winning recipe? For who?

Defeatism

There may or may not be demographics in play with U.S. economic growth. I think less than sometimes posited, as seen by the sudden plummet of labor participation rates in 2008, including that for working-age males. Also, surely it is a truism that higher wages would result in higher labor participation rates.

But set that aside and see this graph of global output:



Yes, a sharp deceleration of global GDP growth post-2008, followed by a petering out of the recovery in 2011. Really? Why?

Work-averse Americans, or something else?

Cause?

George Mason scholar David Beckworth has pointed that about 70% of global central banking is keyed on the Federal Reserve. Indeed, after the Fed raised rates this week, the Hong Kong Monetary Authority and the People’s Bank of China did the same.

Is a reasonable explanation for the post-2008 global slowdown that the Fed choked the global economy into recession in 2008, and has starved it ever since?

Conclusion

U.S. macroeconomists have become lost deep in the ideologically correct woods, blindly following their “free trade” and “money should be tight” maps. Free trade is theoretically wonderful, but what does it mean in a nation with ubiquitous property zoning and huge trade deficits?

And why should the globe’s de facto central bank—the Fed—tighten if real global growth is so weak and prices hardly budging?