Box 1

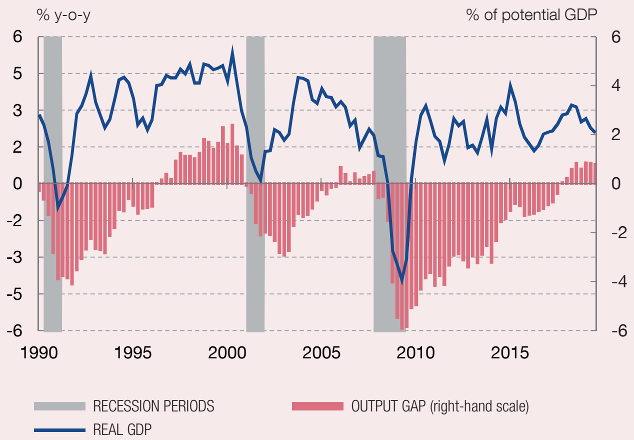
THE US ECONOMY: FACTORS OF RESILIENCE AND OF VULNERABILITY

The US economy has slowed in recent quarters. It has mainly been affected by the weakness of global economic activity and, domestically, by the exhaustion of the fiscal stimuli. Given the economy's weight internationally, it is worth assessing to what extent the slowdown is likely to step up in the coming quarters. In this connection, this box describes the main pillars that would underpin growth in this economy in the short term, the main risks and vulnerabilities it faces and the economic policy headroom available to attempt to mitigate any further downturn in activity.

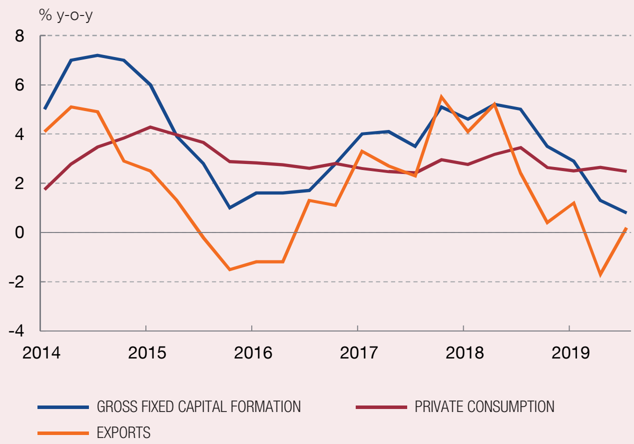
Over the past year US GDP growth has slowed from a year-on-year rate of around 3% to approximately 2%. This is a very similar rate to that of potential growth, estimated by the Federal Reserve to be 1.9% (see Chart 1.1). Headway in the US economy over this period has rested essentially on the buoyancy of private consumption (see Chart 1.2), to which the increases in household income and wealth have been conducive. Specifically, favourable labour market developments in recent years have prompted an increase in household income owing to the rise in both employment and wages, which have outgrown inflation (see Chart 1.3). Looking ahead, signs of job creation easing are discernible. But it is likely that the pace of this variable will suffice to accommodate further additions of workers to the labour force and thus hold the unemployment rate at historical lows. Other indicators

Chart 1
US ECONOMIC OUTLOOK

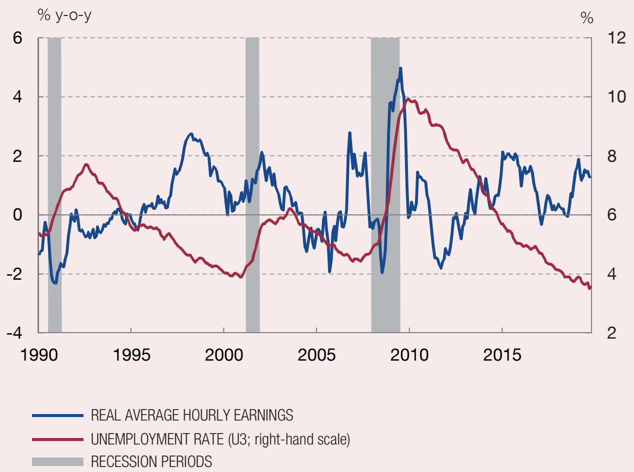
1 GDP GROWTH AND OUTPUT GAP



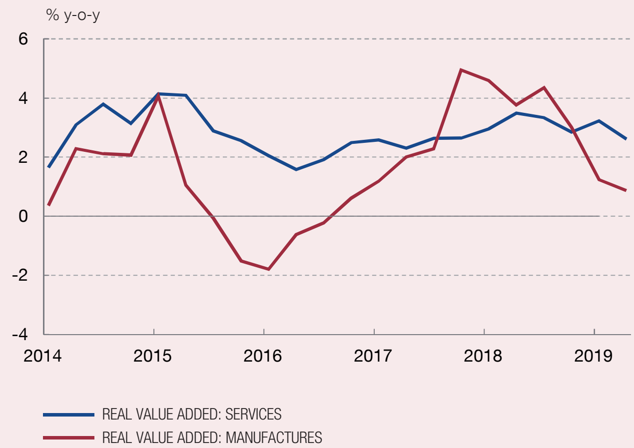
2 GDP COMPONENTS



3 UNEMPLOYMENT RATE AND WAGE GROWTH



4 GROWTH OF VALUE ADDED BY SECTOR



SOURCES: Congressional Budget Office, National Bureau of Economic Research, US Bureau of Economic Analysis and US Bureau of Labor Statistics.

also point to the soundness of the labour market in the short term, such as the low number of dismissals and the high number of employees voluntarily terminating their contracts. Moreover, net household wealth has recently hit new highs thanks to property and equity price appreciation, while the ongoing household debt deleveraging initiated in the wake of the financial crisis has taken root. Conversely, one factor offering less support to future household spending might be the low level of the saving rate which, nonetheless, has risen slightly in the most recent phase, after reaching historical lows.

Set against the strength of consumption, business investment and the external sector have recently shown signs of weakness. If these were to continue in the coming quarters, they might feed through to employment and consumption dynamics.[1] In the case of investment, the persistent escalation of trade tensions and the global economic slowdown have prompted a worsening of business expectations. That has weighed down investment, especially in capital goods, an item which has been greatly affected by the adverse impact exerted by the slowdown in world trade on the manufacturing sector (see Chart 1.4). Further, the fall in oil prices is estimated to have contributed to the recent sluggishness of investment in oil extraction. Aside from these global factors, the increase in real labour costs and the reduction in business mark-ups might also be negatively affecting the dynamism of investment.[2]

As to the external sector, the across-the-board weakness of world trade and escalating protectionist tensions have notably harmed US exports, which is expected to have contributed to the worsening observed in the trade and current account balance. The current account deficit is, at present, close to 3% of GDP. That is around 0.5 pp higher than the level prevailing ahead of the start of the global trade slowdown and of the application of protectionist measures by the Trump administration and which, on IMF calculations, is even further off the level that its fundamentals would warrant.[3]

Taken as a whole, the information available suggests that the US economy is already in a more mature phase of the cycle while the global economic weakness and some persistent sources of uncertainty such as the trade tensions might be penalising its dynamism. Yet the strength of the determinants of private consumption and, in particular, of the labour market would not indicate that the recent slowdown in activity were going to step up significantly in the short term.[4] In this respect, the Federal Reserve's forecasts signal that GDP growth in 2020 (2%) will only be slightly down on the rate expected for 2019 (2.2%).

Tellingly, however, the US economy has, during the current expansion, built up certain vulnerabilities that might influence the future course of activity. At the same time, the space available to apply countercyclical policies is currently more limited than in previous cycles. As to the vulnerabilities, high corporate debt, especially in the high-risk segments, is foremost (see Chart 2.1). There are also some signs of overvaluation on financial markets, which might bear some relation to the search for higher returns at the expense of taking on greater risk.[5] With regard to economic policy leeway, the expansionary budgetary measures approved in late 2017 have appreciably dented the public finances, in the opinion of the Congressional

1 Notably, compared with the behaviour of the equipment component, residential investment has picked up somewhat in recent months, against a background of lower mortgage interest rates, following the weakening of the attendant outlook that had been observed some months back. See, for example, Banco de España (2019), "The slowdown in the US housing market", *Economic Bulletin,* 1/2019, Box 3.

2 Using aggregate US data since 1970, Emre (2016) has found that poor business earnings usually precede declines in economic activity, particularly influencing investment. See Emre, O. (2016). "Recession probabilities". Economic Commentary, Cleveland Federal Reserve Bank.

3 International Monetary Fund (2018). "2018 External sector report: tackling global imbalances amid rising trade tensions", July.

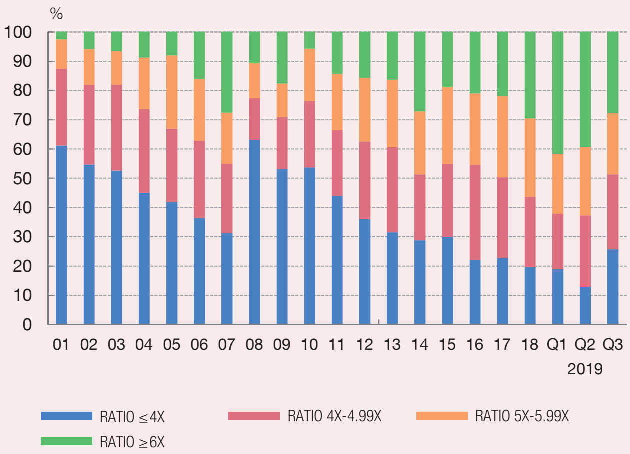
4 Models based on the US sovereign bond yield curve slope estimate that the probability of the US economy going into recession in the coming 12 months would be around 35%. However, the predictive power of these models has been called into question in the current setting, since term premia are historically compressed by the effect of the expansionary monetary policies adopted globally. See Berganza, J. C., and A. Fuertes (2018). "The flattening of the yield curve in the United States". *Economic Bulletin,* Banco de España 1/2018.

5 International Monetary Fund (2019). "Global Financial Stability Report: Lower for Longer", October.

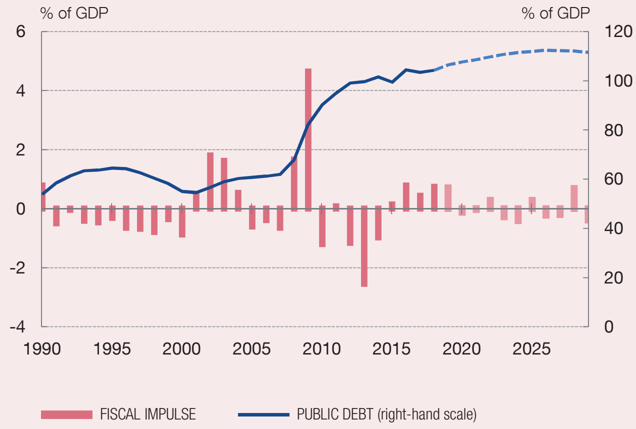
Budget Office (CBO). This might have reduced the fiscal space available to absorb any future adverse shock.[6] Moreover, the fiscal impulse associated with these measures will be reversed as from 2020, contributing negatively to GDP growth (see Chart 2.2). Also, monetary policy room for manoeuvre is more limited than in previous cycles owing to interest rates being close to their lower effective bound.[7]

Chart 2
RISKS AND VULNERABILITIES OF THE US ECONOMY

1 BREAKDOWN OF THE VOLUME OF LEVERAGED LOANS, BY DEBT/EBITDA RATIO (a)



2 FISCAL IMPULSE AND PUBLIC DEBT (b)



SOURCES: Congressional Budget Office and Federal Reserve.

a Loans with a high debt/equity ratio and which entail a high risk of default. EBITDA refers to earnings before interest, taxes, depreciation and amortisation. Quarterly data for 2019.
b Broken lines and shaded bars denote the CBO forecast.

6 Congressional Budget Office (2019). "The 2019 long-term Budget Outlook", June.

7 Párraga, S., P. del Río and J. L. Vega (2019). "The Federal Reserve review of its monetary policy framework", Banco de España, Analytical Articles, *Economic Bulletin,* 4/2019.