The Monthly Itinerary
The ABA Foundation's Monthly Tour Through the Economy

August 2023

AUGUST SUMMARY

I happen to live in Florida, and a large number of people who live near me tend to pull up stakes in the summer and head north. There is something to say about leaving 98 degrees and 100 percent humidity for more temperate climes. Summer is a time when things in much of the economy slow down. Congress takes long recesses, people with families go on vacation, and many professionals head to myriad conferences, conventions, and other gatherings. It's a great time for the travel industry, and hopefully everybody is benefiting from what appears to be a great summer economically.

And while the economy seems to have improved over the past few months, it is important to remember that statistics are not always what they appear to be. The philosopher and father of the study of general semantics, Alfred Korzybski, coined the phrase, *a map is not the territory*" in a 1931 lecture at an American Mathematical Society meeting. This is a very powerful statement as it applies to economics. All economic models and statistics are based on assumptions and methods, many of which may not reflect current reality. The map of statistics does not always portray the territory of the market. This is because of the process by which federal statistics are generated.

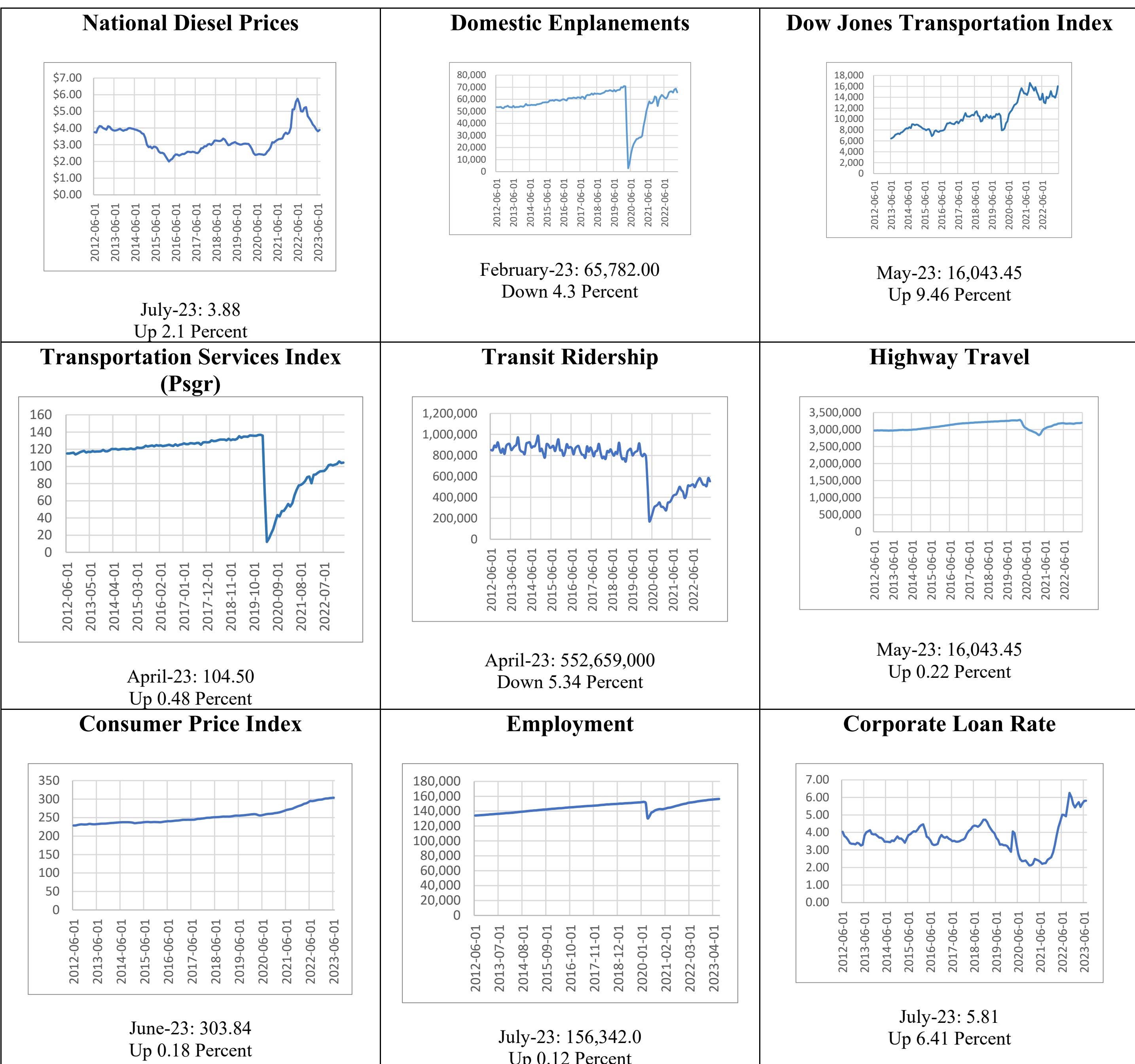
All federal statistical agencies have to follow strict formulas and model structures. This is done to ensure consistency and to make sure that bias is not purposely embedded in them. Since the process for generating federal statistics is basically fixed, and since the world itself is not, when major inflection points in the economy occur, the statistics become volatile. It's hard to think about any inflection point larger than the worldwide government shutdown of the economy in response to COVID-19, which was probably the most dramatic event to impact the economy since the end of the gold standard in the early 1970s. This suggests that there is, and will continue to be, a lot of volatility in federal statistics for a good long while.

Because the methods for determining important government statistics including the CPI, the PPI, GDP and employment figures were developed prior to the dramatic transformation in the economy, initial statistics have been subject to extreme revisions. Even after the revisions, various statistics are not agreeing with each other. As an example, Gross Domestic Income and Gross Domestic Product should closely track each other. However, since the end of COVID, GDI has been relatively flat, while GDP has grown. This is partly due to massive military support for Ukraine but is also likely due to changes in levels of government transfer payments, which shot up during COVID and have now begun to decline. The statistical agencies are simply not able to adjust their models quickly enough to account for this, and this is likely leading to inflated GDP figures.

Employment is tracked using two surveys, one of households, and one examining unemployment insurance statistics. Regulatory changes during the Biden Administration, which have forced workers onto payrolls, have caused a huge divergence between growth in the number of people saying that they are employed and unemployment insurance statistics. Again, the BLS has not had time to adjust their processes, and the headline employment statistics are likely to be overinflated. All of this means that current economic statistics should all be taken with a grain of salt.

The Monthly Itinerary is designed to provide members of the ABA with an ongoing series of data and commentary on key economic and transportation statistics of importance to the motorcoach and motorcoach tourism industry. For more information or to comment on this report, please contact Melanie Hinton at mhinton@buses.org or 202-218-7220.

JULY STATISTICS



AUGUST ECONOMIC NEWS

- To continue to mask inflation, the federal government pulled an additional 2 million barrels out of the Strategic Petroleum reserve in July. The reserve is now at the lowest level since the same month in 1983 (just one year following the creation of the reserve). Considering that the SPR was created to ensure that the military has access to oil, this is a troubling situation, and the restocking of the reserve will end up costing taxpayers significant funds.

- Diesel prices rose throughout the month of July and are now back above $4.00 per gallon. In addition, the EIA has dramatically lowered its forecast of renewable diesel production because of increased regulations.

- According to the Bureau of Economic Analysis, 2nd quarter GDP grew at a nominal rate of 4.7 percent and 2.0 percent in real terms. These figures suggest that inflation was near the Federal Reserve's 2.0 percent target rate; however, it could also suggest that revisions will be in the downward direction.

- Meanwhile the Bureau of Labor Statistics reported that the CPI rose at a year-over-year rate of 3.0 percent in June. Statistically, the CPI will increase at a faster rate over the remainder of the year. Inflation in Canada was at 2.8 percent in June.

- The Federal Reserve also increased the target Federal Funds Rate by an additional 25 basis points in July, suggesting that the Fed is still concerned about price inflation. There are three more Fed meetings in 2023, and it is likely that interest rates will be increased by an additional 25 basis points this year.

AUGUST COMMENTARY

Money for Nothing was a 1985 song by Dire Straits which featured vocals from Sting. It was written by Mark Knopfler and Sting and was the first video to appear on MTV Europe when the network launched. It could also be the theme song for what was an unprecedented period on US monetary history, as between the spring of spring of 2008 and the summer of last year the Federal Funds Rate (which is the rate that banks pay each other for overnight loans) did not exceed 2.5 percent. This 14-year period was the only time since the late 1950s when interest rates and inflation were both low. Although prior to then it was rare to see the target rate go above 2 percent.

During the 14-year period of low interest rates, real (or inflation adjusted) interest rates did not reach even 1.0 percent except for one month (June 2022). Since that point they have fallen back to just above zero, as the growth in inflation has far outpaced interest rate hikes.

Of course, most people and businesses do not have access to the same interest rates as banks, but during this entire period of low Federal Funds Rates, annualized average 30-year fixed mortgage rates never went about 6 percent (except right at the beginning of the period), 4-year automobile loan rates never exceeded 7 percent (again except right at the beginning of the period), and rates for junk bonds stayed below 15 percent, except for at the start of the period and again during the semi-recession of 2016. All in all the cost of debt was relatively low, and the real cost was extremely low by historical standards.

As with any other good or service demand is induced by lower prices, so during this period total debt (corporate, personal, and government) less assets grew from about 15 percent of GDP to nearly 60 percent. This would be the same thing that would happen if motorcoach ticket prices were reduced to nearly zero or even negative levels. If companies paid people to take buses, there would be a huge surge in demand.

The problem with high demand for debt is that – over time – prices can change, and borrowers will not be able to make interest and principal payments when rates go up. This is now one of the main structural problems with the US economy. The Congressional Budget Office is currently forecasting that interest on the Federal debt alone will more than double - from just under 10 percent of revenues in 2022 to over 20 percent by 2033. The debt crisis is also showing up in corporate America. According to a recent report by the International Monetary Fund, about 8 percent of public firms and 3 percent of all private firms in the US are zombie companies, meaning that their total revenues are not high enough to just meet interest payments. Finally, while delinquency rates on personal loans are still well below pre-COVID levels, they have been rising quickly (from about 1.5 percent in the middle of 2021 to 2.5 percent today). And this is despite of unprecedented levels of money being shoveled out of the federal government to households all across the spectrum.

The bottom line is that a long period of easy and cheap credit distorted the economy, creating a large level of what the economist John Mills described as *malinvestment.* This malinvestment moved resources from productive sectors of the economy, to uses that would not be profitable without easy financing. When the taps started to dry up, the malinvestment went into receivership. This was made worse by the COVID-19 shutdowns that made what were productive assets (like center city office buildings) either non-productive or just marginally productive.

As interest rates continue to rise, or as inflation begins to weaken, the number of zombie firms and malinvestments will grow, leading to bankruptcies, job losses, and losses for lenders and investors. This will keep the economy in a state of

stagflation for some time to come. This will become more apparent as federal government subsidies begin to wane, and especially when the tax cuts enacted by President Trump expire at the end of 2025.

Money for Nothing was good for those who played the guitar on the MTV, but in the end, it will be a serious roadblock for a return of a prosperous US economy.

The Monthly Itinerary produced by John Dunham & Associates and is provided as a service by the American Bus Association Foundation. It is not intended as investment advice. If you would like more information, or if you would like us to track additional indicators, please feel free to contact Melanie Hinton at mhinton@buses.org or 202-218-7220.