

Presentation to the Economic Advisory Panel for the Federal Reserve Bank of New York

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April 1, 2022

MORGAN STANLEY RESEARCH
North America

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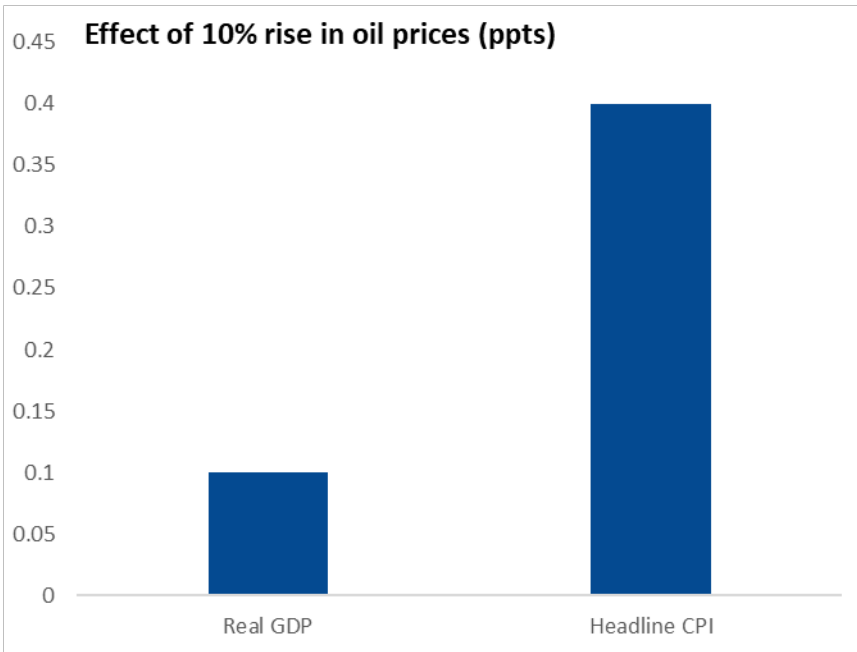
Risks and Medium-term Outlook in the Post-pandemic Economy

- A. Repercussions of recent geopolitical developments on the US economy
 - i. What are the consequences of current global developments on economic outlook, financial markets and monetary policy? What are the medium-term implications on the macroeconomy of the current geo-political developments?

- B. Prospects for the US labor and goods markets
 - i. What are the medium-term implications for labor force participation in the post-pandemic world? Is the “Great Resignation” transitory or permanent? Are all jobs and workers equally affected?
 - ii. As the economy recovers from the pandemic, what are the medium-term implications for the durable goods sector both from a consumption and production point of view (re-shoring and diversification of global supply chain)?

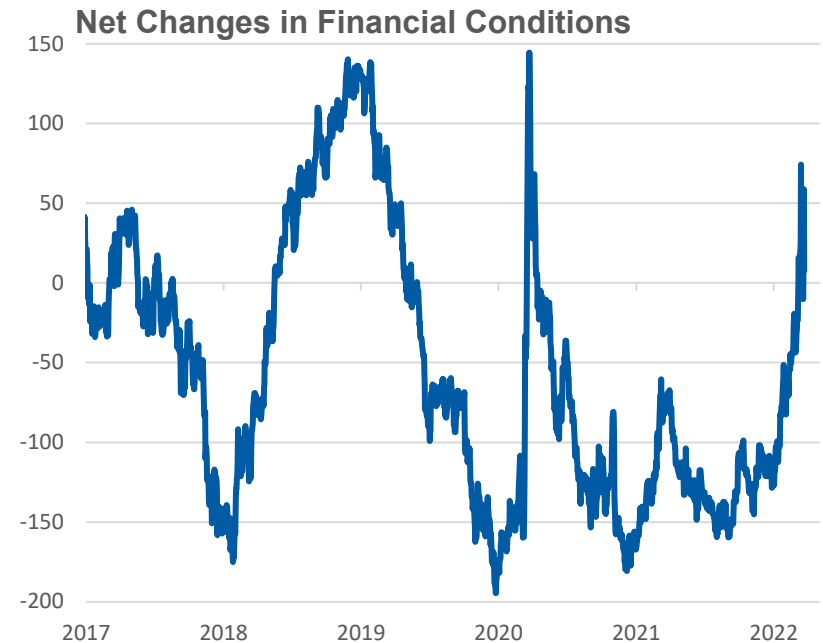
Growth effects are likely to be small but watch inflation, financial conditions

Our rules of thumb imply a much larger effect of higher oil prices on inflation than on growth



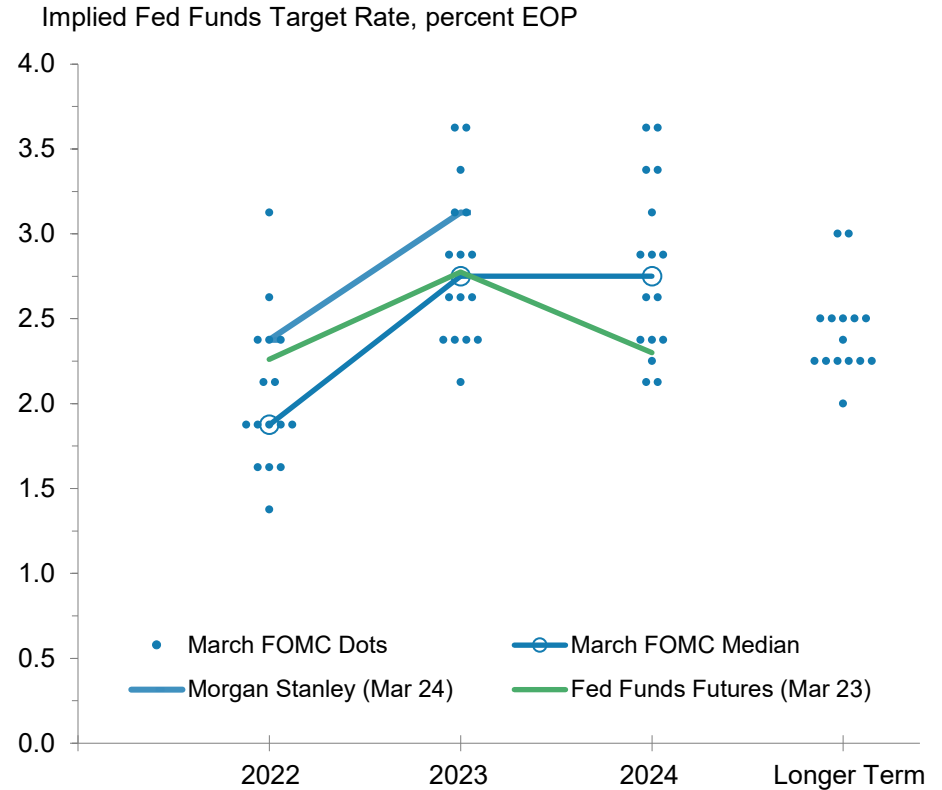
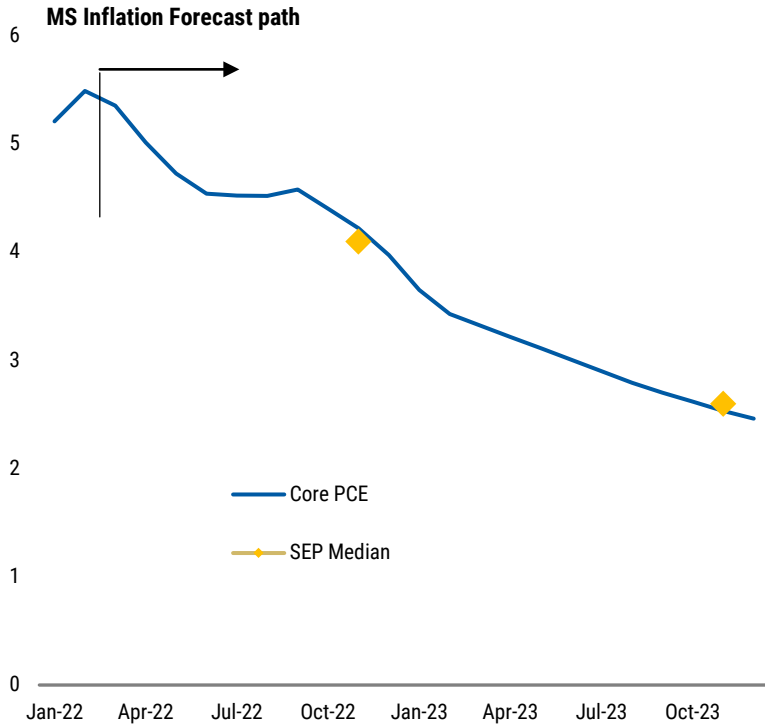
Source: Morgan Stanley Research

Our FCI has tightened sharply in recent weeks



Source: Morgan Stanley Research

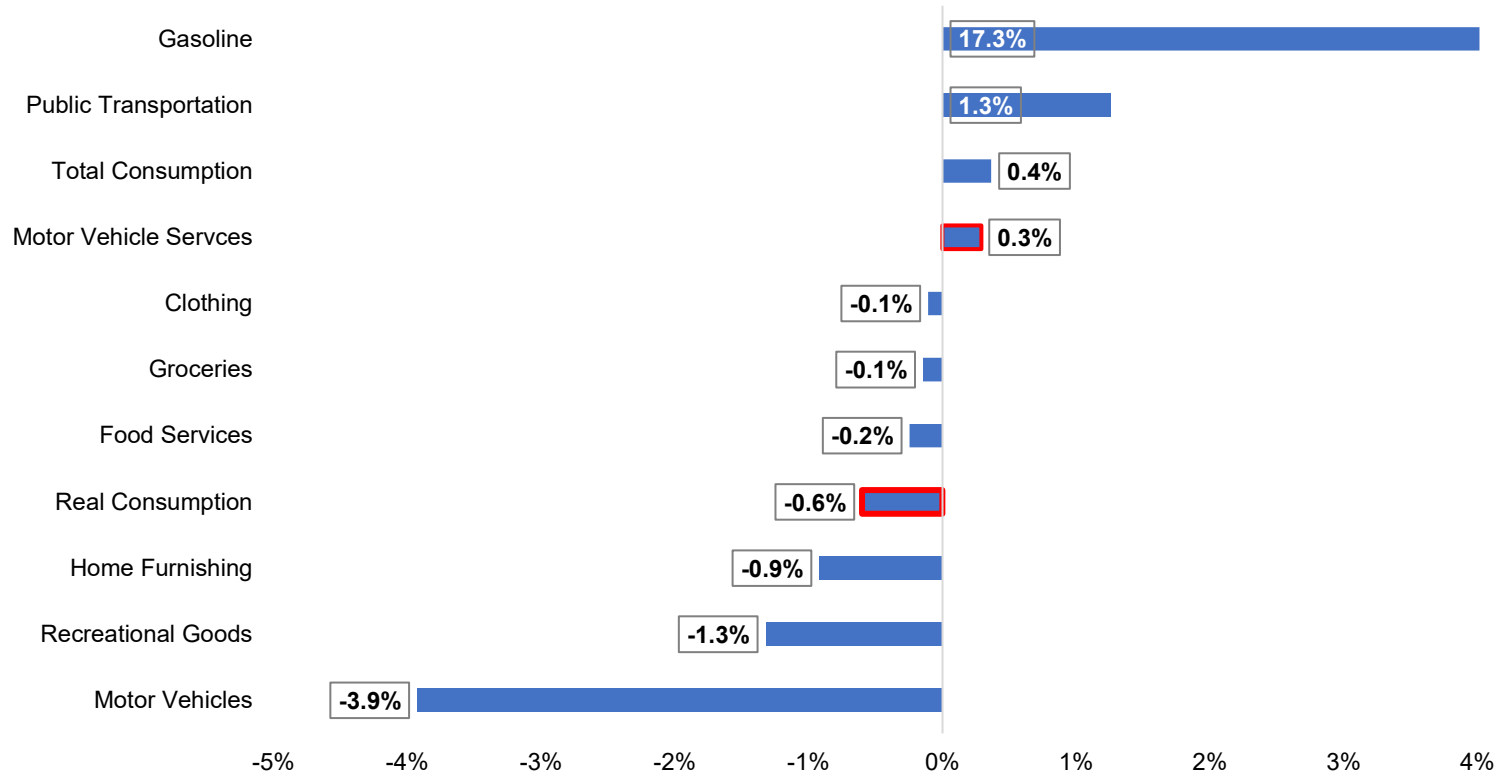
We see inflation declining in line with the SEP



Source: Federal Reserve Board, Bloomberg, Morgan Stanley Research

The oil supply shock will increase nominal spending overall, but dent real consumption and durable goods demand

Impact on Spending over 3 Months from 100% Increase in Oil Prices due to Supply Shocks



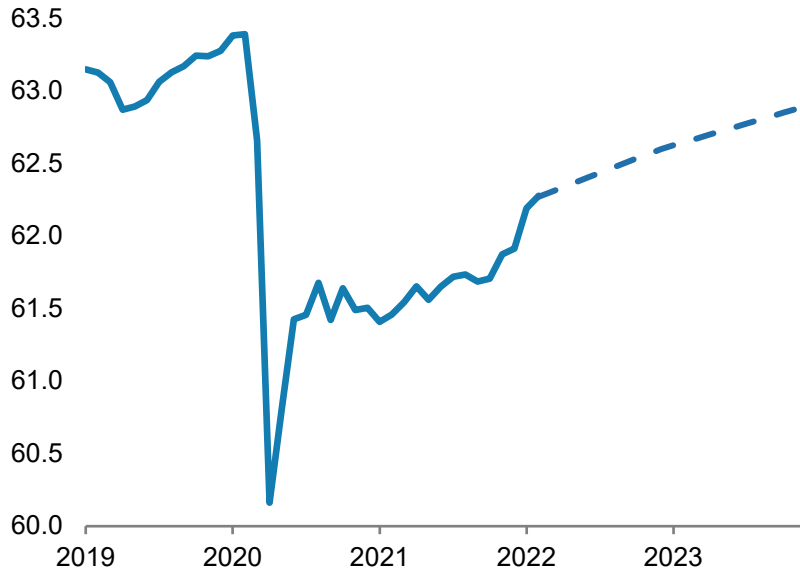
Note: Regression coefficient from an instrumental variable regression of 1-month WTI price changes on subsequent 3-month PCE spending (not annualized). We use isolated oil price shocks from a VAR with sign restrictions of oil prices and global aggregate demand as the instrument. Sample:1975-2019. Source: BLS, Morgan Stanley Research

Labor force participation is coming back

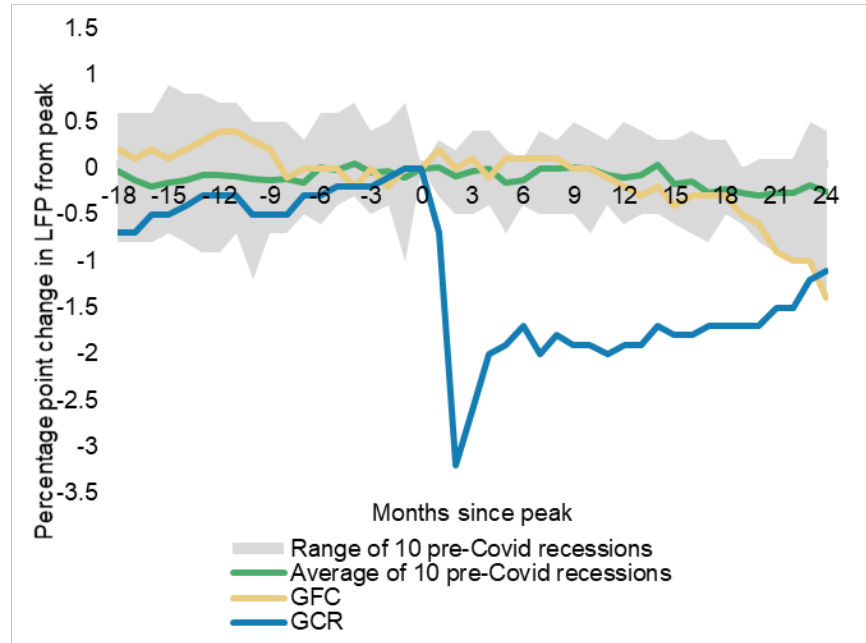
We see further gains in labor force participation as strong labor market conditions and higher wages draw in more workers from the sidelines

The decline in the participation rate is atypical for recessions but the economy is making up ground.

Labor Force Participation Rate, percent



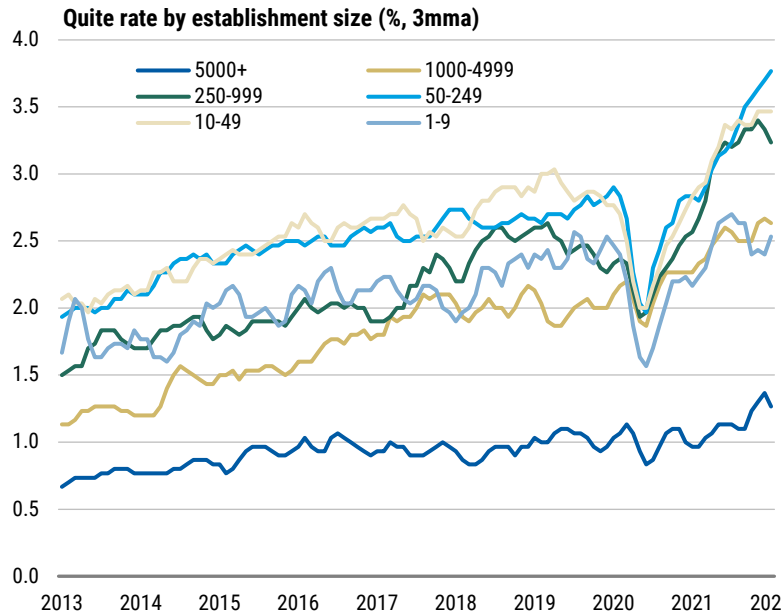
Source: BLS Morgan Stanley Research



Source: Morgan Stanley Research

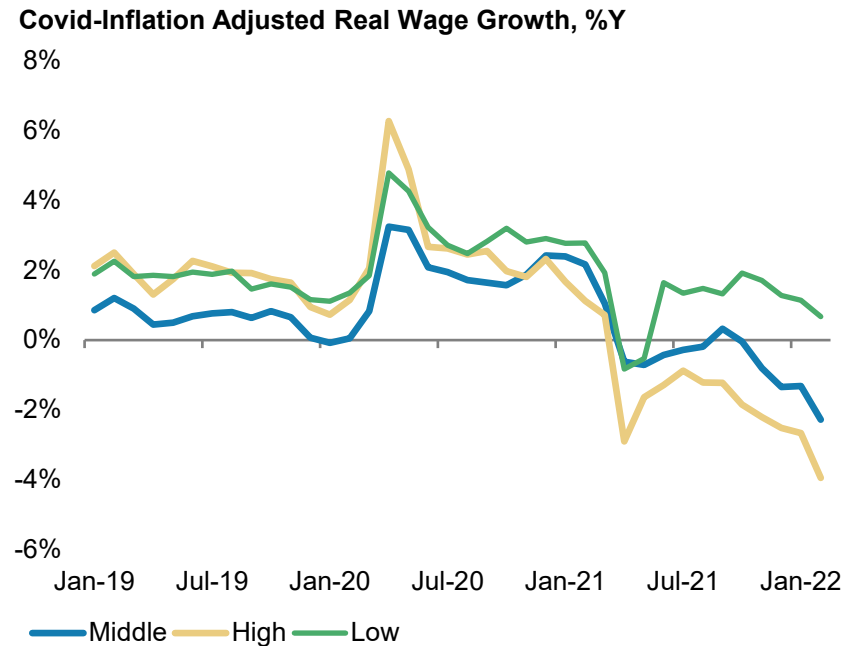
Tight labor markets are driving up quits and wages, but only in some parts

The “Great Resignation” has been most pronounced in small and mid-sized establishments and is showing signs of slowing down



Source: BLS Morgan Stanley Research

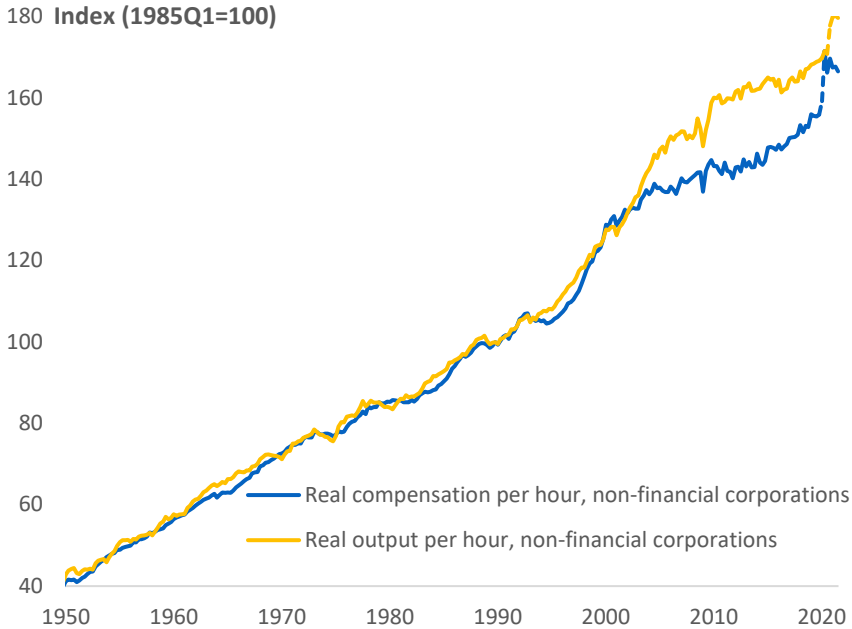
Only low-income workers have seen real wage growth recently



Source: BLS, Harvard University, Morgan Stanley Research

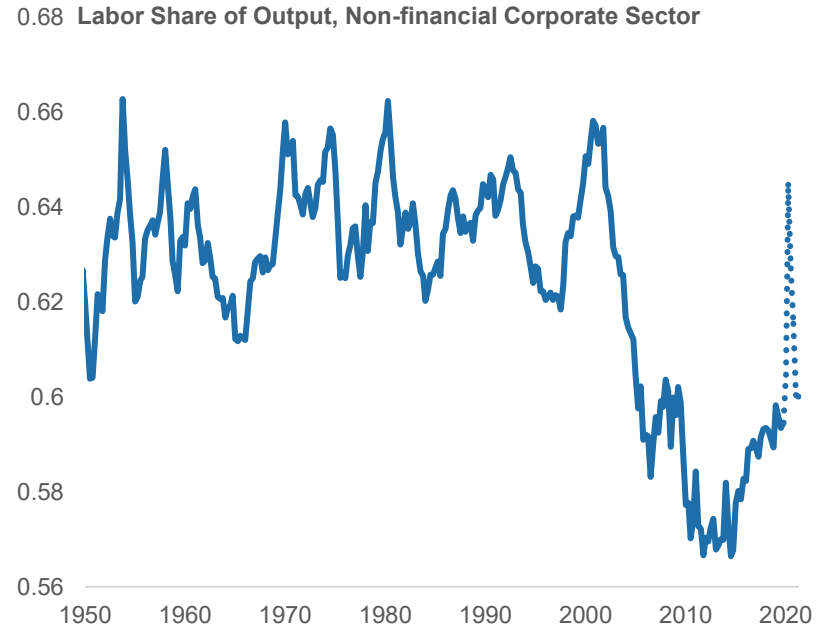
Labor market strength is driving the return of the “Workers Economy”

Real wages decoupled from productivity growth over the last two decades but are now catching up



Note: Dotted line marks the pandemic period. Source: BLS, Morgan Stanley Research

The labor share of corporate income is moving back towards its historical level, with negative consequences for corporate profit margins

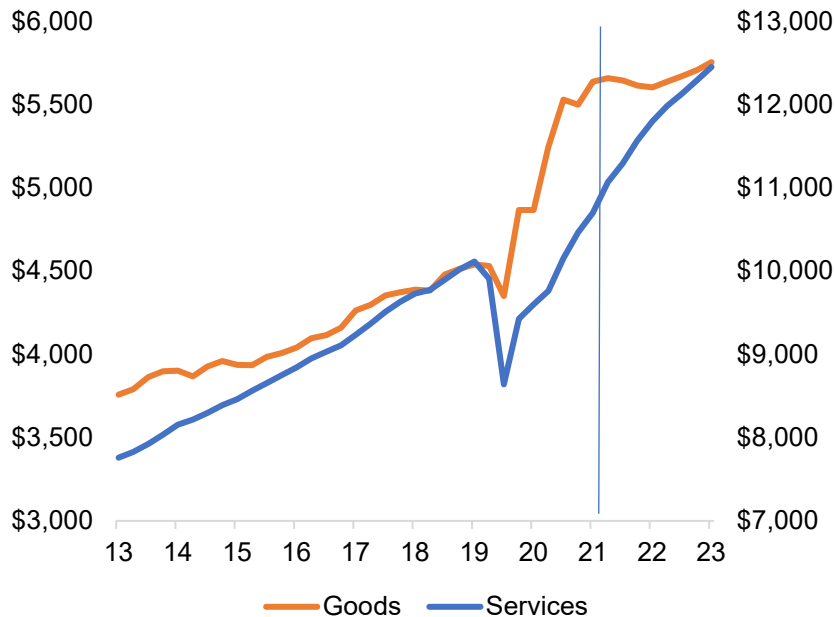


Note: Dotted line marks the pandemic period. Source: BLS Morgan Stanley Research

Share shifts in consumption and inventory build-up will be major features this year

As consumption shifts back to services from durable goods, price pressures should normalize

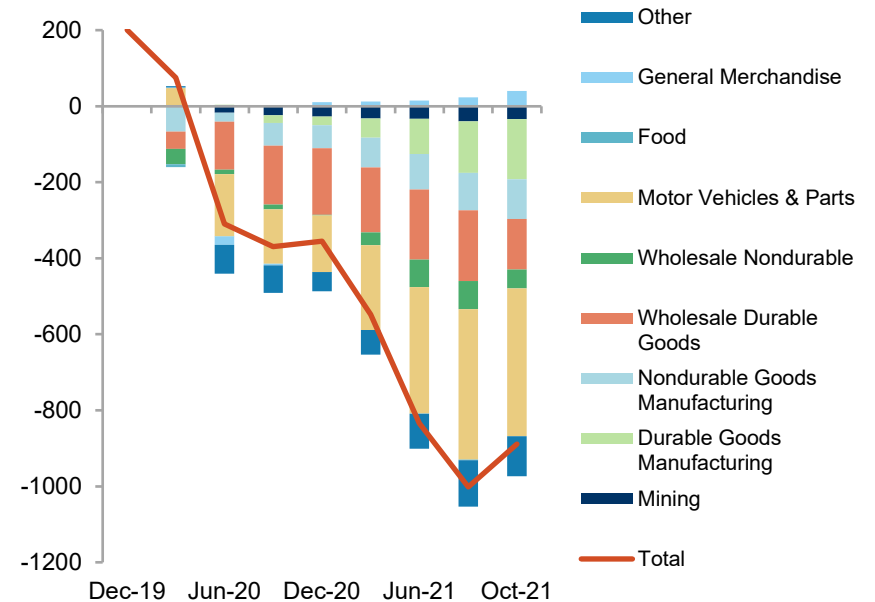
Nominal PCE, SAAR, Bil. \$



Source: BEA, Morgan Stanley Research

Inventories are still low for autos but are beginning to reverse for other goods.

1Q20-4Q21 Cumulative Inventory Shortfall
Bil. 2012 \$, SAAR



Source: BEA, Morgan Stanley Research

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