Something Has Shifted in How People Are Talking About the Economy

By Joe Weisenthal

What's that? A glimmer of hope about the economy?

For some reason, over the last several days an increasing number of prominent voices have expressed optimism that the US can avoid a recession and pull off the proverbial "soft landing." Maybe inflation can actually come down without a substantial increase in the unemployment rate.

Larry Summers said last week to Bloomberg's David Westin, "We have to recognize the figures are better than what someone like me would have expected three months ago… It's still a very, very difficult job for the Fed, but the situation does look a bit better."

Speaking about the global economy, IMF Managing Director Kristalina Georgieva echoed something similar, that the situation is "less bad than we feared a couple of months ago."

Perhaps the most crucial comments of all came on Friday from Federal Reserve Governor Christopher Waller, whose speech was titled A Case For Cautious Optimism. The basic gist of the speech is that a soft landing is possible and that he doesn't see the need for much more hiking at this point. The key line: "Six months ago, when inflation was escalating and economic output had flattened, I argued that a soft landing was still possible—that it was quite plausible to make progress on inflation without seriously damaging the labor market. So far, we have managed to do so, and I remain optimistic that this progress can continue."

In a note to clients, Tim Duy, the chief US economist at SGH Macro, wrote that Waller's comments basically end the debate about whether the Fed will do something other than a 25 basis point hike as its next meeting. What's more, says Duy, "Waller isn't even pounding the table for a May rate hike; I was particularly struck by Waller's declaration that the difference between market pricing and the Fed's terminal rate was not particularly meaningful."

Meanwhile, markets have started to shift. Stocks are off to a strong start in 2023, reflecting the improving mood. According to JPMorgan Chase & Co., seven of the nine asset classes that it tracks for its model are indicating a less than 50% chance of a recession. A few months ago, the market was signaling that a recession was basically guaranteed.

Sentiment often follows price, so it's not particularly surprising to see optimism grow as the stock market goes up. But also the data so far is exactly what you'd up to see for the soft landing to line up. The unemployment rate is at a roughly 50-year low amid increasingly convincing signs that inflation has turned the corner. In theory, it's rare and difficult to see a big decline in inflation without major labor market damage. But in practice, it appears that that's what's happened over the last three months.

Obviously there are still plenty of risks. Not a day has gone by lately, where some big tech company announces that they're slashing high-paying jobs. This could snowball into diminished spending and more layoffs elsewhere across the economy. Meanwhile gasoline and other commodity prices have stopped falling, perhaps putting ongoing upward pressure on inflation. But for now, the data and the market are driving positive sentiment from observers and the officials setting monetary policy.