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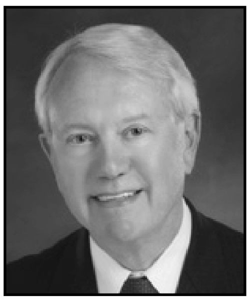
POLITICAL ECONOMY

A look at inflation and supply chain crisis

By Jim Flinchum

The third quarter of 2021 started with a boom but ran another into another COVID wave, a surprisingly severe supply chain crisis, and gnawing fears about inflation.



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Coronavirus drag

We know over 700,000 Americans have been killed by this virus. Assuming half had jobs earning an average of $30,000 annually, then the annual loss of GDP is over $10 billion. Because a dollar spent is income to someone else and then re-spent, we assume every dollar earned is spent, say, five times. That means the actual economic loss is $50 billion — every year. What a waste!

The coronavirus has been studied in the U.S. since the chicken outbreak in the 1920s. Research ramped up considerably in the 1960s when it was first discovered in humans. It spiked more when investigating SARS in 2003 and MERS in 2019. It is small wonder that the vaccine was discovered so quickly.

Supply chain

Today, the post-pandemic economy is being hurt by supply-chain problems, which have been more severe than expected and will exacerbate inflation pressure. The delays in shipping are a huge part of the problem. Nike says shoes imported from China that normally take 40 days now require 80 days. That increases the level of needed working capital, as the shoes have already been paid for but cannot be sold until they get here. Worse, it hurts profits.

Off the port of Los Angeles, there are about 70 ships — full of things that Americans have ordered. Part of the problem is that the port doesn't have enough berths, but that's because ships are taking more time at the berths to offload cargo. Think about the costs — the crew gets paid whether under sail or not and taxes and insurance expenses still must be paid by ship owners. Plus, the profit they would normally make if they were promptly offloaded — the extra cost totals billions of dollars. What a waste!

You cannot blame the crisis on unions, but one part of this problem is 20th-century union rules — that they won't work on Sundays, that shifts are limited to only two per day, not three and trucks that don't show up to remove containers if terminal traffic is "bad." There are not enough truck drivers, largely due to technical training requirements that could be temporarily waived. Our supply chain problem is a national security issue and should be treated that way.

If employees cannot be hired, then the National Guard should be activated. Last year, our doctors and nurses worked countless hours for the good of our country. This year, the Longshoremen and Teamsters need to do the same — for the good of our country.

Inflation

Everybody who remembers the 1970s has an understandable fear of inflation, often conflating it with stagflation. Because our economy is still snapping back nicely from the pandemic crash, stagflation is unlikely. However, inflation is a different story. Initially, fear of inflation resulted from the increase in money supply to offset the pandemic crash. The Fed argued that the tsunami of liquidity would drain too quickly to ignite inflation, which was reasonable.

Then, the disruption in the supply chain was worse than expected — far worse. The increased inflation results from the sudden 30% increase in demand from quarantined consumers combined with the economy's limited ability to increase supply, creating inflationary pressure. In addition, we now have energy prices reaching seven-year highs, adding more inflationary pressure.

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Interest rates

The benchmark yield on 10-year Treasuries is now over 1.6%, a significant increase from recent lows. The late former Fed Chief Paul Volcker was able to break inflation in 1980 by raising interest rates enough to cause a recession, and there is plenty of room for the current Fed chief to do the same. As inflation rises, upward pressure on interest rates will develop. Have you already refinanced your mortgage?

The labor force

Historically, economists have viewed the unemployment rate as an indicator of the demand for labor. Today, it may be a better indicator of the supply of labor. While that rate is better than expected, at only 4.8%, I don't believe it. "Real" unemployment is higher.

My Republican friends expected the labor force participation rate (now 61.6%) to increase when the enhanced unemployment benefits expired. So far, it has decreased. In fact, for men over age 20, it has dropped to an all-time low.

Economists expected 500,000 new jobs last month, but only 194,000 emerged. One reason is the booming stock market is giving boomers time to think about retirement. Some people are too afraid of COVID. Another reason is that the lack of child care is keeping an estimated 2 million women out of the workforce. Women lost jobs at a slower rate than men during the Great Recession in 2008-2009 but were four times more likely to lose their jobs last year. Welcome to the "Great She-cession!"

The stock market

Investors are pleased with the almost 16% growth of the S&P so far this year. Looking a little deeper, the market appears to be rolling over. While up 15.92% year to date, it was flat during the third quarter and lost 4.65% last month. The pattern was similar for small-cap and mid-cap stocks. (However, history tells us that the fourth quarter brings the best stock market performance.) For September, growth stocks were down 5.79%, compared with less volatile value stocks, which were down 3.29%. I expect that to continue.

The best-performing sector this year has been energy, which was up 43.22%. Last month, it was the only sector to improve, up 9.44%. With interest rates moving up, the financial sector was the second-best performer, up 29.14% year to date.

Worldwide, Canada was the best performer, up 19.5%, compared with second-place U.S. at 15.92%. Europe was up 10.78%, followed by Australia at 8.18%. Note: All the best performers have the most capitalistic economies.

In the long history of Congress doing dumb things, my nomination for the single dumbest congressional creation was the debt limit. Conceived to force the opposing parties to negotiate with each other with the hope of slowing down the growth of our debt, it has done neither!

The debt ceiling is merely a tool for the out-of-power party to torment the in-power party and to terrorize Wall Street. It was created by Congress, and it can be eliminated by Congress. It doesn't work. Great risk, no reward. Just dumb!

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