

# John Dunham & Associates

“The Winning Side of Economics”

## The Current Economic Situation and Implications For the Recycling Industry

Presentation to: The Institute of  
Scrap Recycling Industries

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# John Dunham & Associates

Specialists in the Economics of Crisis and  
Controversy

Regulatory Economics

Taxation

Lobbying and Government Affairs Support

Public Affairs Messaging

Litigation Support

# Forecasting the Economy in 2022

*There are two kinds of forecasters: those who don't know, and those who don't know they don't know.* - J.K. Galbraith, Advisor to President Kennedy and US Ambassador to India

- Economic Forecasting in the best of times is difficult - not much different than throwing a bunch of sheep entrails into a circle and reading what they say.
- The Economic Machine is very easy to understand but...
- The world is not. External events (what economists dub exogenous factors) matter
  - COVID-19
  - 9/11
  - Bond Rating Scandal
  - Federal Reserve Policy

Forecasts need to be considered with a grain of salt

# What Makes the Economy Move?

*It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard for their own interest.*

*-Adam Smith, Economist and Author of *Wealth of Nations**

- The machinery of supply and demand
  - Sets prices and quantities
  - The invisible hand
- The economic law of motion of modern society
  - Falling tendency of the rate of profit
  - General law of capital accumulation
- The law of diminishing marginal utility
  - One banana good, two banana bad, three banana die
- The power of comparative advantage
  - The ability to produce a particular good or service at a lower opportunity cost than others
- The growth model
  - $Y = F(K, AL)$

# What is the Status of the Nation's Economy?

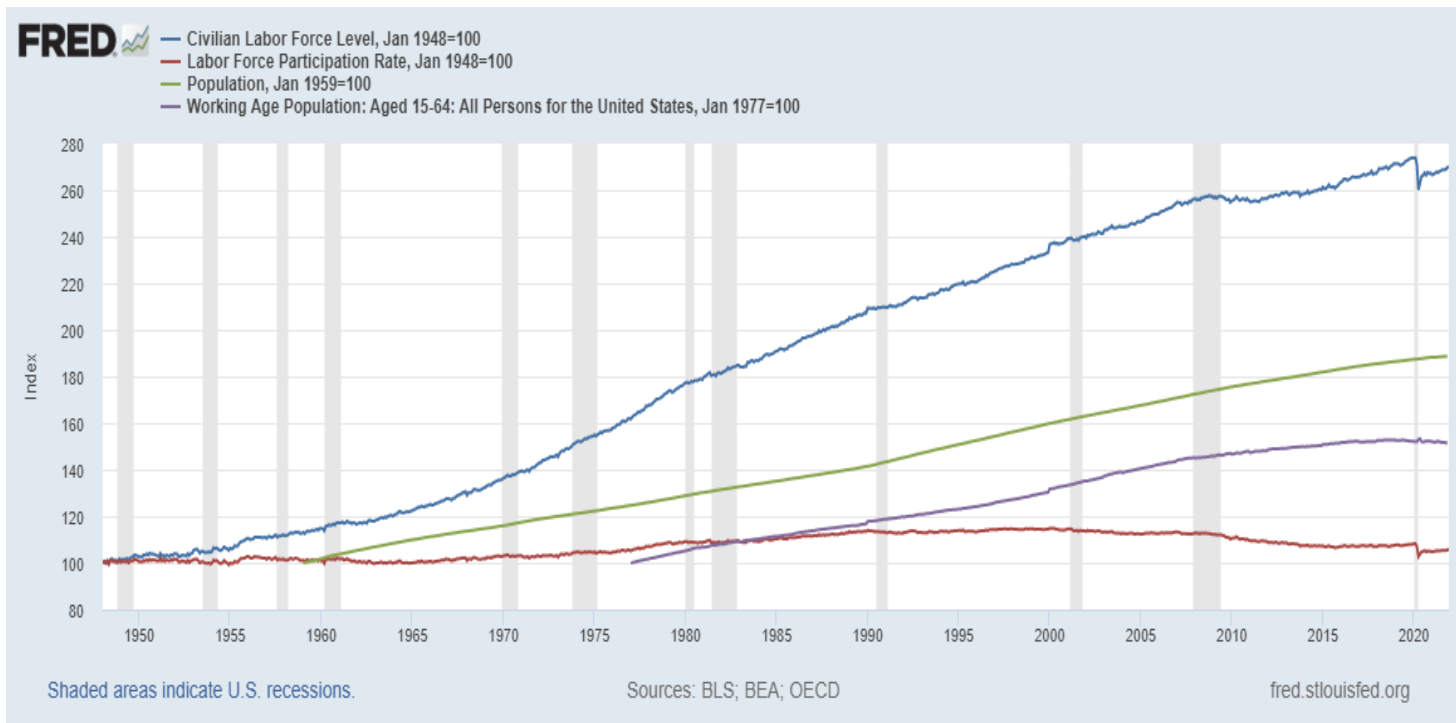
*Facts do not cease to exist because they are ignored.* - Aldous Huxley, Philosopher and author of *Brave New World*

- The American economy suffered a disastrous two years beginning with the government-imposed shutdowns in response to COVID-19 in February 2020. And while things have improved:
  - Employment is down by 3,572,000
  - Inflation is up from 2.26% to 7.00%
  - The level of household debt is at record highs - \$17.6 trillion
  - Federal government debt is 122.52 percent of GDP
  - The US trade deficit is up
  - Real wages are down
  - GDP is still running at about \$225.2 billion below trend
  - Shipping costs increased by 137 percent in 2021

# Major Concerns Going into 2022?

*Why does a public discussion of economic policy so often show the abysmal ignorance of the participants? - Robert Solow, Nobel Laureate*

- The Labor Force:
  - The labor force is shrinking
  - The labor force is becoming less skilled



# Major Concerns Going into 2022

*Blessed are the young, for they shall inherit the national debt -  
President Herbert Hoover*

- Capital is being grossly misallocated
  - Overall misallocation of investments due to lack of creative destruction.
  - "Zombie" firms or those with debt servicing costs that are higher than their profits but are kept alive by relentless borrowing accounted for 18.9 percent of firms in 2020 (Axios)
  - Government Share of GDP about 27% in 1964 and 39% this year.
  - S&P 500 stock buybacks record \$234.6 billion in Q3 (Yardeni)
  - Total debt in US is 376.89 percent of GDP.
  - Productivity has stalled post COVID

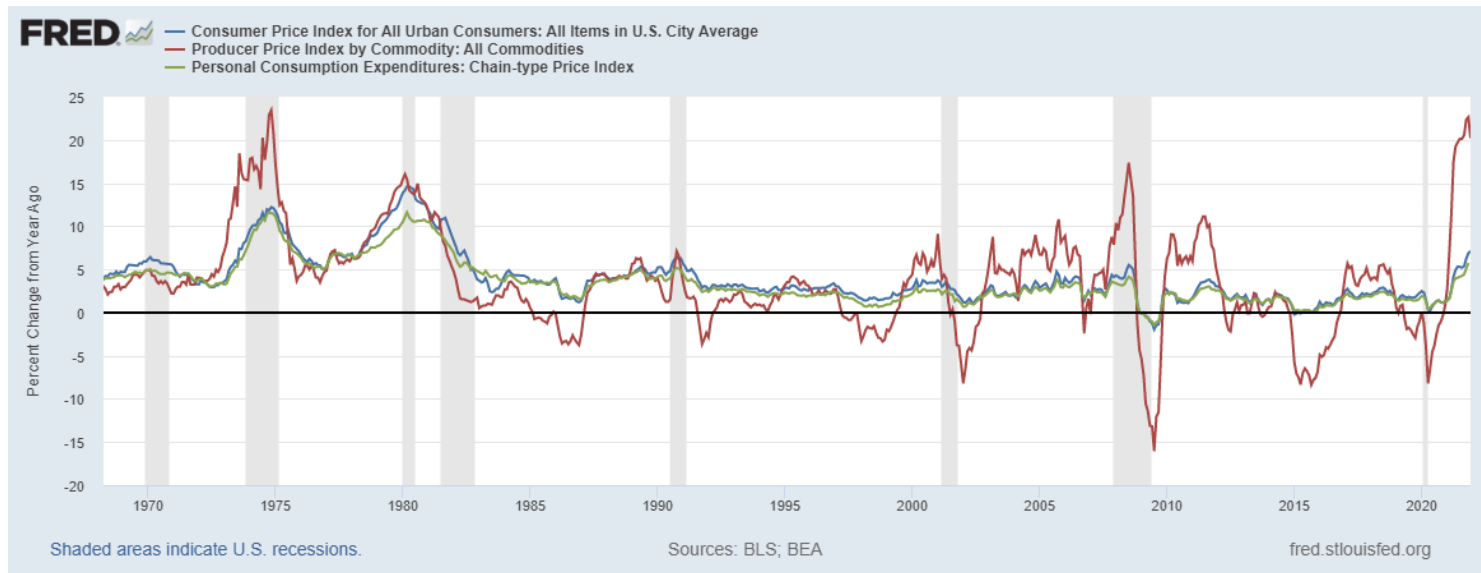
This means that the current economic pattern is unsustainable

# Major Concerns Going into 2022

*The best way to ruin a country is to debauch its currency - Vladimir Lenin, Revolutionary and First Chairman of the Council of People's Commissars of the Soviet Union*

Inflation is soaring:

- Producer Price Index increasing at levels not seen since 1970s
- Both CPI and PCE increasing at levels not seen since early 1980s
- Shipping costs are soaring



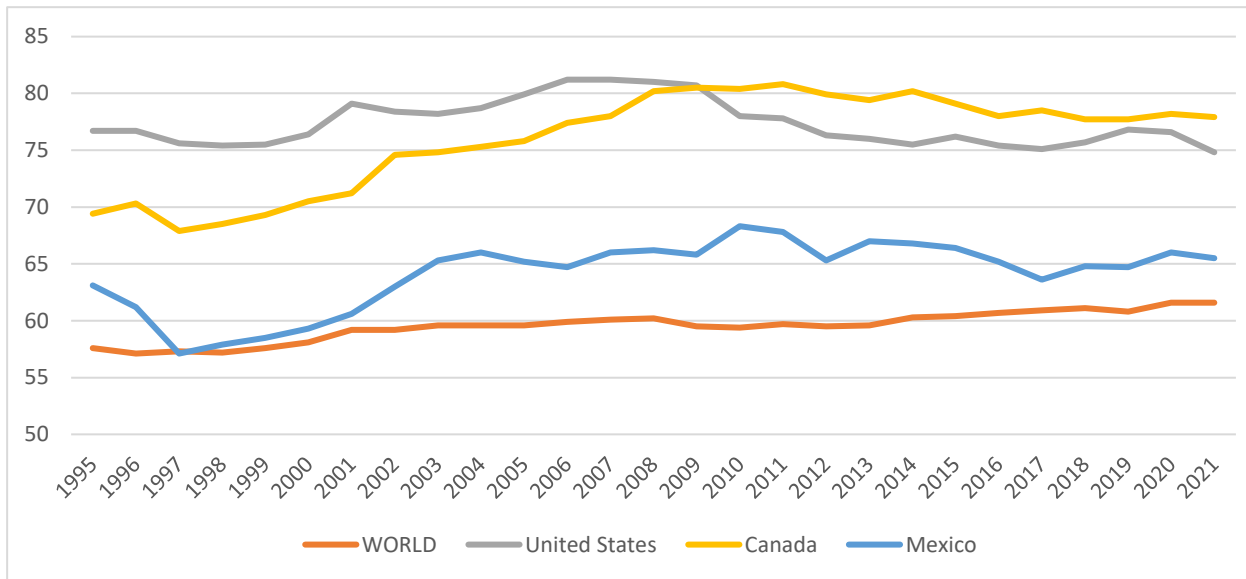


# Major Concerns Going into 2022

*We are fast approaching the stage of the ultimate inversion: the stage where the government is free to do anything it pleases, while the citizens may act only by permission. - Ayn Rand, Author and Philosopher*

Regulation is damaging the economy:

- According to the Heritage Foundation, the level of economic freedom in the US, which is closely tied to tax and regulatory policy has been declining for the past dozen years.

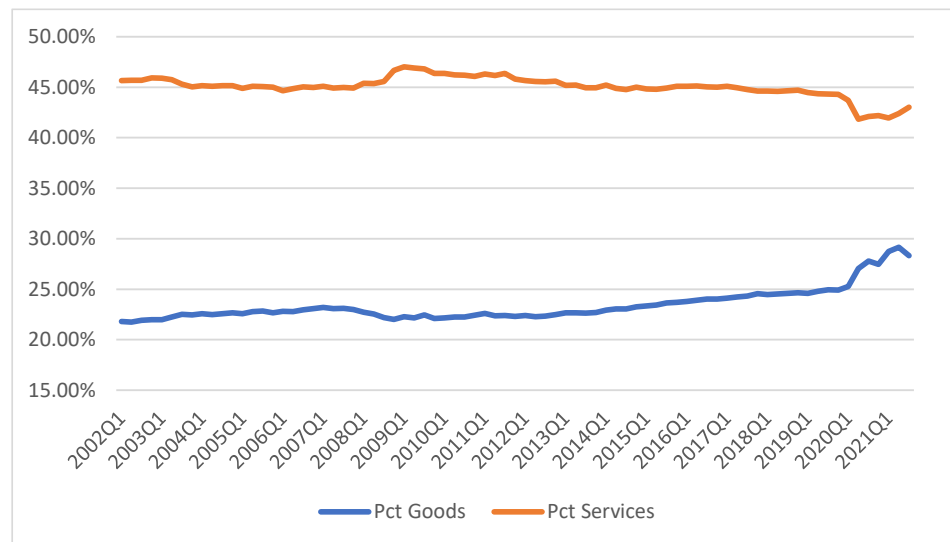


# Major Concerns Going into 2022

*If something cannot go on forever, it will stop.* - Herb Stein, President Nixon's Chairman of the Council of Economic Advisors

## COVID continues to be an issue

- There is continued fear over COVID infection, not only in the US but worldwide
- Governments are passing draconian restrictions not seen since the early 1930s
- Importantly, consumers have shifted to goods consumption over service consumption.



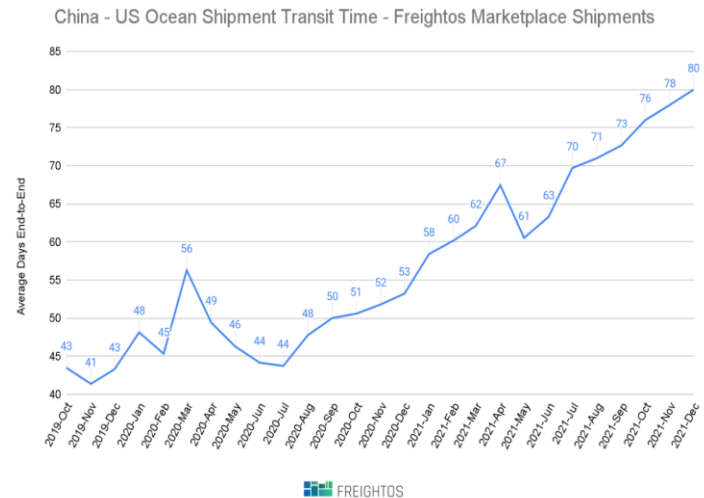
# Major Concerns Going into 2022

*No nation was ever ruined by trade.*  
- Benjamin Franklin, Founding Father

Shipping costs have exploded:

FBX Lane	Global	Asia - US West Coast	Asia - US East Coast	Asia - North Europe	North Europe - US East Coast
This Week	\$9,500	\$14,572	\$17,476	\$14,440	\$6,469
Last Week	7%	16%	6%	1%	4%
Last Year*	137%	169%	190%	89%	253%
* Compared to the corresponding week in 2021					

- Freightos Data suggests that shipping prices are up by 137 percent worldwide during the past year.
- Transit times continue to increase



# What Can We Predict Over the Course of 2022?

*A map is not the territory it represents.* – Alfred Korzybski, Developer of  
General Semantics

	2022/1	2022/2	2022/3	2022/4	2022 Average
Gross Domestic Product	2.4%	2.0%	2.0%	1.9%	2.1%
Consumer Spending	3.2%	2.8%	2.5%	2.4%	2.7%
Consumer Price Index	6.5%	6.3%	6.0%	5.4%	6.1%
Housing Starts (Annualized 000)	1200	1300	1300	1250	1260
Payrolls (000 monthly)	275	290	300	150	254
Unemployment Rate	3.8%	3.8%	3.9%	4.0%	3.9%
Federal Funds Rate	0.50%	0.75%	1.00%	1.00%	0.81%
2-Year Treasury Yield	1.25%	1.17%	1.18%	1.23%	1.21%
10-Year Treasury Yield	2.25%	3.38%	3.07%	3.20%	2.97%
WTI Oil Price	\$75.00	\$80.00	\$78.00	\$75.00	\$77.00

The economy will continue to muddle along

- The shipping crisis will continue, fiscal and monetary policy will remain dovish
- Inflation will continue to be at levels not seen in decades
- Energy costs will increase over last year
- Interest rates will rise
- Workers will remain scarce
- No recession in 2022, but .....

# What Can We Predict Over the Course of 2022?

*We know that advanced economies with stable governments that borrow in their own currency are capable of running up very high levels of debt without crisis. - Paul Krugman, Nobel Laureate*

## Monetary Policy and Interest Rates

- Paul Krugman is an advocate of so-called modern monetary theory
  - The idea that governments can borrow an almost infinite amount of money
  - MMT has generally been the policy of the US government since the George W Bush Administration
- There is no free lunch as the current bout of inflation shows.
- Federal Reserve forced to raise Federal Funds Rate and stop QE - 25 bps hikes in March, May and likely June. Maybe one more if GOP wins majorities
- Short term interest rates (2-year) about 1.3% by end of year
- 10-year rate at about 3.2%

# What Can We Predict Over the Course of 2022?

*Inflation is like toothpaste. Once it's out, you can hardly get it back in again.* - Karl Otto Pohl, Economist and President of the Bundesbank

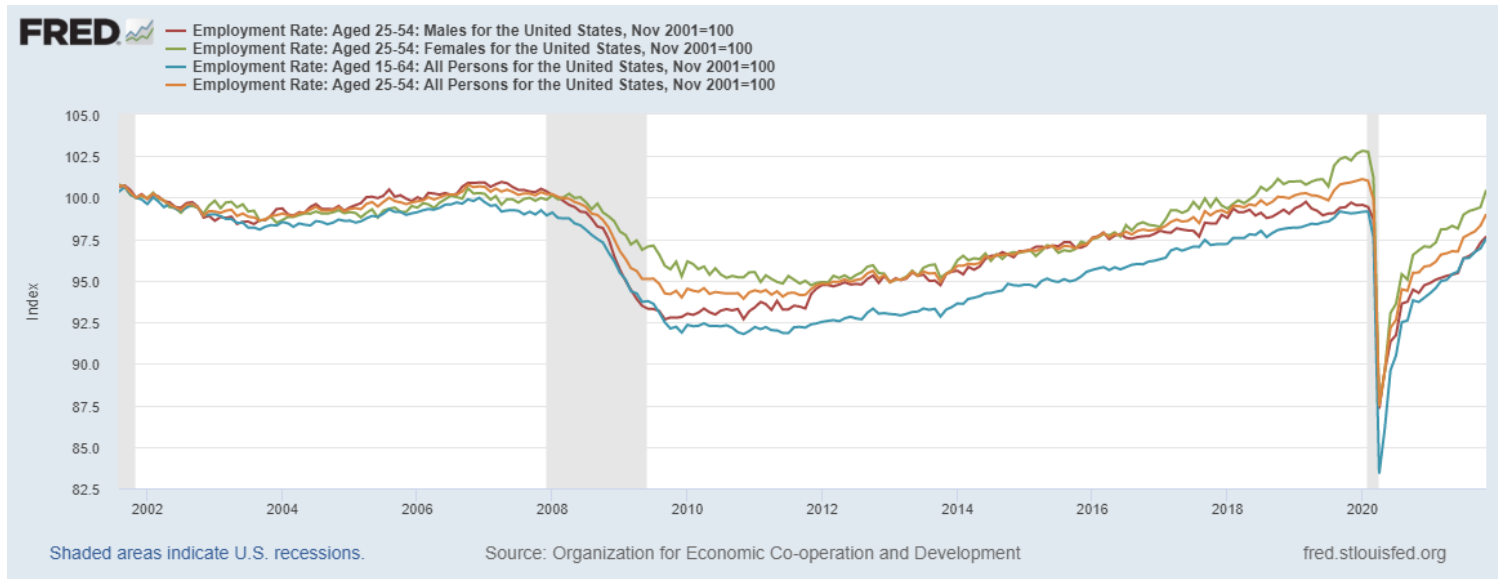
Inflation will mellow but not go away

- Large increases in PPI will manifest in the CPI over the next few months
- Energy costs will continue to rise, and will spike dramatically depending on what happens in Ukraine and Taiwan
- Shipping capacity will remain tight, and prices will stay elevated
- Higher borrowing costs will be passed through to consumers
- Shortages and product rationing will not go away
- Expect to see CPI average around 6 percent for the year IF no additional shocks occur

# What Can We Predict Over the Course of 2022?

*As capital accumulates, the lot of the laborer must grow worse.*

- Karl Marx, Economist

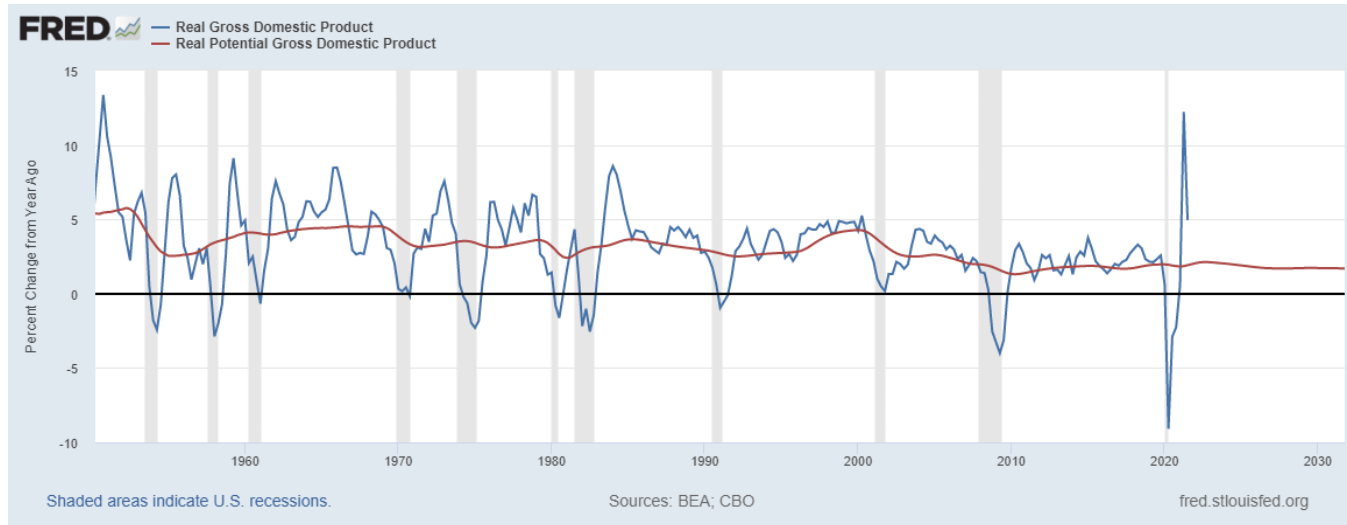


## Employment will continue to stagnate

- Employment to population ratio peaked in 2019
- Now more pressure to stay out of the labor force - particularly for older people and women
- Elevated job growth numbers (250,000 range) through next year and headline unemployment staying below 4.0 as the number of people entering the labor force matches job growth.

# What Can We Predict Over the Course of 2022?

*A recession is when your neighbor is out of work. A depression is when you are out of work.* - President Harry Truman



## Economic Growth

- “Potential” GDP growth is really just a smoothed trend but it does give a baseline for where GDP will head.
- In today’s economy, less any exogenous effects, GDP is expected to grow at a rate of about 2 percent.
- The concerns for 2020 will keep post recession growth muted
- Expect to see GDP fall back to the trend after Q4-2021



# Implications for the Recycling Industry

*Plans are worthless, but planning is everything* - President Dwight D. Eisenhower

If we are correct and the country (for that matter the world) economy muddles along, the industry should be prepared for:

- ✓ Not much relief in the logistics situation. Costs, capacity constraints, increased surcharges, and delays will continue to plague the ocean freight, rail, and trucking industries. The underlying causes for this include increased regulation, COVID restrictions and labor shortages, and high demand for goods. Backhaul to Asia will continue to be an issue.
- ✓ Continued price inflation at the wholesale level (PPI) at much faster rates than have been seen historically. It is likely that 4 to 5 percent inflation will be the new normal. There will continue to be product rationing (shortages) at least through the end of the year.
- ✓ Elevated scrap metals demand should moderate through 2022 as the economy continues to weaken. Paper scrap will continue to be soft due to supply/demand incongruences, while plastic scrap demand is likely to begin to recover as more regulations requiring scrap content percentages are passed.
- ✓ Labor shortages will continue but start to moderate. Higher wage rates, and even faster growth in benefit costs both through insurance cost increases (as they make up for COVID losses) and through regulatory benefits like paid sick leave requirements.
- ✓ Higher (though still negative) interest rates. This means that capital investment will still be relatively inexpensive from a financing perspective.

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[www.GuerrillaEconomics.com](http://www.GuerrillaEconomics.com)

John Dunham  
212-239-2105  
[jrd@GuerrillaEconomics.com](mailto:jrd@GuerrillaEconomics.com)