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Lead Left Interview – Tim Hopper

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This week we chat with Tim Hopper, founder of Macro Fund Advisors. Previously Tim was managing director and chief economist for TIAA. Tim has over 20 years of experience writing and speaking about the global economy. Prior to joining TIAA, Mr. Hopper held various leadership positions in global banking and real estate. He also served as a senior economist with the Federal Reserve Bank of Dallas for over 10 years.

The Lead Left: *Tim, unbelievably it's been exactly two years since our last Lead Left interview [link]. Congratulations on your new firm, by the way. Let's start out by asking what's your biggest surprise so far this year in terms of the economy?*

Tim Hopper: The resiliency of the economy since the great recession has been nothing short of spectacular, given everything that has transpired since 2008. Despite all the populist movements here and abroad, political uncertainty and regulatory change, it's remarkable how we've been able to march forward on a stable economic footing.

TLL: *Why has that happened?*

TH: In spite of ever-stricter regulation, and an ever more uncertain political environment, the economy is awakening. The credit problems that we had are behind us, the economy is waking up. It's healing. And, the cycle is not over. In fact, it's strengthening!

TLL: *Are we still in the 7th inning?*

TH: Yes, we're still there. We're frozen in time since we spoke last. We've finally reached the point where the Fed can tighten, and they will. The ECB is also about to begin the great unwind. Going forward, the balance of risks will shift from latent weakness in the economy to the the risk surrounding the Fed's policy path.

TLL: *Are we over any kind of future taper tantrum?*

TH: There's a feeling that recent gains in equities and bonds have been underpinned by easy monetary policy. The fear is that future tightening may reverse these gains. While this notion is false on the surface, there are risks and uncertainties surrounding the great unwind.

Let me explain what I mean. On one hand, we should recognize that earnings growth should support market performance as interest rates rise and the Fed's balance sheet deflates. On the other hand, it would be unwise to assume that such a large run off of the balance sheet won't impact market performance going forward. The uncertainty comes about because the Fed's balance sheet has never been this large and we have yet to see the full impact of quantitative easing.

For example, in past business cycles low rates incentivized increased corporate debt issuance and pushed institutional investors into higher yielding assets. Rising rates generally unwound that trade. This time around, the economy has been in uncharted territory for a decade with excess liquidity. Corporate debt issuance is on the rise, and this time, all investors (institutional, high net worth and retail alike) are crammed into ever riskier and scarce high yield instruments. The distribution channels for high yielding assets have permeated all areas of the investing community, and the risk is that investors don't necessarily understand what they own. Further, the liquidity constraints surrounding newly proliferated instruments such as ETFs risk creating sharper market movements than investors have become accustomed to. But in spite of these dangers, the Fed must raise rates and it must also bring the size of its balance sheet under control.

***TLL:** Will we still see a rate hike in December?*

TH: There's still some catching up to do on rates. I said there'd be three rate hikes this year. There have been two and I expect one more. I said that in the first half of this year inflation would decelerate, which it did. And, as expected, it is picking up now as we enter the fourth quarter. The Trump trade, which spurred markets and perceptions of possible growth at the beginning of the year, has re emerged in the second half, and along with inflation, it will generate further rate hikes.

***TLL:** What's your forecast for GDP?*

TH: Year-over-year inflation measures are rising close to the Fed's target. Average earnings are also closing in on 3%. Interestingly 3.5% is the typical cyclical high for household earnings. With just a bit more earnings growth, things will really get going. 2018 will be much stronger, much better than 2017. I think GDP will average in the mid-two's for this year, high two's for 2018, and over 3% for 2019. This is where the economy is going, and I believe the global economy will also continue to strengthen, probably in the 3-4% range. The global economy is synchronized and headed up.

For the balance of this year, and all of next year, this improvement will provide demand for US products and increase US demand for overseas products.

***TLL:** Where are interest rates headed?*

TH: We'll have three rate hikes both this year and next – maybe more in 2018. The Fed is behind the curve, as I told you in our interview back in 2015, and they still have some catching up to do.

***TLL:** How about taxes? Any chance of tax reform?*

TH: Unlikely this year, but something will happen next year. Will we be able to cut corporate taxes to 20%? It's too early to tell. That's the opening salvo. But, we'll get something and anything incremental will be helpful. The same with healthcare. Both of these things will provide a positive tweak to the economy.

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