Autumn 2024

As it pertains to the economy and your portfolio, we will, of course, get to the upcoming U.S. presidential election. But first, a trip down under, and back in time.

In 1988, New Zealand's inflation had come down from a high of 15% earlier in the decade to about 10%. Roger Douglas, the country's finance minister who'd gotten some of the credit for the drop, was asked in a television interview whether he was satisfied with the number. Douglas extemporarily responded that he'd ideally like to see the rate between zero and one percent.

At the time, nobody paid much attention to Douglas' response, but it would eventually have enormous sway on central banks around the world for decades to come.

How? Not long after the interview, New Zealand's government passed the Reserve Bank Act of 1989, which called for the central bank to determine a formal target for inflation and gave them the freedom to use interest rates to reach that target.

Don Brash, the Bank of New Zealand governor at the time, made this decision not through extensive research and due diligence, but based on Douglas' off-the-cuff answer. He simply bumped it up a bit (0% to 2%) to give policymakers more flexibility.

This became a self-fulfilling prophecy. New Zealand's inflation, according to Stats NZ, New Zealand's official data agency, went from 7.2% at the end of 1989 to 1% by the end of 1991. And central banks, from Canada to England to Japan, took notice, adopting 2% as their inflation targets. The number was officially adopted in the U.S. in January 2012, by then-Federal Reserve Chair, Ben Bernanke.

Which is why when news came out recently that U.S. inflation had hit 2.5%, a three-year low, we were once again reminded we've not quite met the Fed's goal of…2%!

Sound arguments can certainly be made for why 2% is a logical number. But the same is true for 4% or 6%. But Douglas' response, and New Zealand's success some three decades ago, has largely made 2% global gospel.

And, for the U.S., the 2% target may be working again. The Fed, like a skydiver pulling one tog or the other to circle, or both to slow down, has slowly brought inflation down, hovering just above the drop zone. Money supply has actually shrunk in the U.S., a first. (Historically, money supply growth is around 4% annually to accommodate the needs of expanding outputs.) Inflation, as measured by the Consumer Price Index (CPI), has dropped from 9.1% in June of 2022 to 2.5% today.

The same is true in Canada, where CPI is 2% today compared to a peak of 8.1% in June of 2022, and money supply has slowed to a sustainable level.

All of this in the Fed's pursuit of, to expand the skydiving analogy, a "soft landing," a cyclical economic slowdown that ends without recession. Which now seems even more likely given the latest jobs report, which shows hiring and wages growth are strong, and unemployment remains low.

This brings us to the U.S. presidential election, where we'll hear both sides taking credit for the good economic news and blaming each other for the bad and keep promising their economic policies will make things even better.

As for who gets credit, presidents from both parties, as we've noted in pre-election *folios* of the past, have far less control over the economy than we imagine. The Inflation Reduction Act of 2022, for example, really had nothing to do with inflation. It was a climate bill. The unclogging of supply chains mucked up by the pandemic undeniably helped lower inflation, but government didn't play a major role in that. And ex-presidents aren't responsible for the high stock market.

As for the many plans and promises, we'll just note two. Presidents have limited effect on the cost of oil, a globally traded commodity. And Congress, under either party's leadership, is highly unlikely to pass a federal ban on hard-to-quantify and even harder-to-define price gauging.

We, of course, hope everybody votes and we encourage you, while making your decision, to consider this: study after study has shown a president's economic record is largely determined by where the nation is in the economic cycle. In a word, and perhaps like Douglas' answer to the ideal target number for inflation, luck.