2014: The U.S. Economy's Breakout Year

This year has already been the strongest year for monthly job growth since 1999.

By Katherine Peralta / December 30, 2014

Despite the harsh winter weather that chilled economic growth at the start of the year, 2014 has been undoubtedly the strongest year of the U.S. labor market recovery yet. Driven by robust job gains, the American economy has sailed smoothly through this year as overseas economies stumble.

After a sluggish first couple of years of the recovery – Amherst Pierpont Chief Economist Stephen Stanley calls them “frustratingly tepid” – 2014 is the year in which the economy’s momentum finally has picked up and looks poised to be on a more self-sustaining path moving into 2015.

America’s economy has come a long way in the five years since the end of the crisis, when businesses, shaken by uncertain demand prospects and a difficulty in obtaining credit, shed jobs by the hundreds of thousands, global unrest like the Arab Spring shook confidence and concern mounted over a federal government debt default.

“We’ve seen a significant turnaround this year with the economy now finally operating on virtually all cylinders. That is certainly manifested [in] the acceleration of payrolls,” says **Bernard Baumohl, chief global economist at the Economic Outlook Group.** “Companies are more confident about the sustainability of this expansion and they are far more upbeat and more comfortable about ramping up hiring."

Even excluding the upcoming December numbers, monthly job growth in 2014 has been the strongest since 1999 and the unemployment rate is down to 5.8 percent, the lowest since mid-2008 and almost one percentage point lower than 12 months ago. At this time last year, the Federal Reserve had projected it'd be 6.8 percent to 7.3 percent by the end of 2014.

Further, applications for unemployment benefits have been trending below 300,000 for several months, a sign that employers are holding off on firing as jobs are created and the pool of available workers shrinks.

These labor market improvements invigorate consumers, who have enjoyed another tailwind from lower costs at the gas pump as oil prices plunged in the second half of the year. As a result, Americans reported feeling the most confident about the economy in seven years, according to the Thomson Reuters/University of Michigan consumer sentiment index for December.

And happier consumers mean more spending, which helped to drive third quarter gross domestic product growth to an annualized rate of 5 percent, the strongest surge since the same quarter in 2003, the Commerce Department reported this month. That figure was up from 4.6 percent growth in the second quarter and a 2.1 percent contraction in the first, an aberration economists say was temporary.

"That in no way should reflect the fundamental strength of the U.S. economy and what's really impressive … in four of the last five quarters – the only [excluded] quarter being that contraction – the U.S. economy has been growing nearly 4.5 percent on average," Baumohl says. "That is the kind of speed that we really need to see to get more people back to work, to get inflation rising a bit more and for the Federal Reserve to finally conclude that their work is essentially done."

But the Fed's work isn't done yet. With its goal of full employment and price stability in sight, the Fed continues to hold short-term interest rates near zero to support the economy's growth. After its December meeting, the Federal Open Market Committee said it'll "be patient" in beginning to normalize monetary policy as inflation continues to run below 2 percent.

What's more, there remains a stubborn amount of labor market slack, which refers to elements of the labor market being unable to operate at their full potential, such as Americans who'd prefer full-time work but can only find part-time jobs. When and if that slack diminishes, it should prompt wage growth, which has yet to really materialize in the way that should be pushing up inflation.

"If you don't see wages picking up over the coming year, it means there's something fundamentally wrong with the recovery," says Gennadiy Goldberg, U.S. strategist at TD Securities.

Goldberg and other economists are optimistic, though, that wages will pick up in 2015. Not only is the pool of available labor shrinking, wrote Renaissance Macro Research LLC's Neil Dutta, but the number of people voluntarily quitting their jobs has also crept up. When workers quit and switch jobs, Dutta wrote in a recent research note, pay tends to rise.

A raise is already on the horizon for many. In January, 20 states plus the District of Columbia are slated to increase their minimum wages, a boost of $1.6 billion in increased earnings for 3.1 million workers, according to calculations from the Economic Policy Institute, a left-leaning think tank.

Stagnating incomes for low-wage workers, and soaring corporate profits coupled with record high equity markets this year, have helped exacerbate the gap between upper-income families and middle- and lower-income families, which has reached record high levels since the Great Recession, according to recent figures from the Pew Research Center.

"Even though corporate profits and the stock market have hit all-time highs, the typical family isn't bringing home more than they did 15 years ago," President Obama said in a Dec. 6 address. "A vibrant jobs market gives us the opportunity to keep up this progress, and begin to undo that decades-long middle-class squeeze."

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