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F. Frank Ghannadian, Ph.D.
Dean, Sykes College of Business

WHAT'S INSIDE

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Shifting Narratives and Rising Uncertainty Pose a Risk to the American Economy

By Vivekanand Jayakumar, Ph.D.

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During the past couple of years, the dominant economic and financial market narrative was centered on the notion of 'U.S. exceptionalism.' The zeitgeist was captured in an October 2024 special report published in *The Economist*, which claimed that the American economy was the envy of the world and that its stock market reigned supreme and warned that the rest of the advanced world was at risk of falling even further behind [1]. Last November's election victories for President Trump and the Republican party reinforced expectations that the U.S. economy and equity markets would continue to outperform a supposedly moribund Europe and a stagnant China in 2025.

In financial market parlance, the consensus trade heading into 2025 was to be long U.S. and short Europe and China. At the January World Economic Forum in Davos, reporters from the *Financial Times* captured the euphoric mood that prevailed at the start of the Trump 2.0 era: "Investors have warned of Europe's vulnerability to Donald Trump's "America First" policies, contrasting the continent's economic struggles with the animal spirits being unleashed in the U.S. under the new President. Trump's plans for deregulation and tax reductions prompted a burst of enthusiasm from many U.S. executives … But the mood regarding Europe was far darker, with an executive at a major U.S. bank warning of "peak pessimism" about the continent."[2]

What a difference a couple of months make? The start of the Trump 2.0 era has been characterized by capricious policymaking as the administration has embarked on a controversial agenda to profoundly remake the underlying structure of both the U.S. economy and the American government. The Trump administration is using large-scale tariffs and the threat of trade wars to attempt to drastically rewire the global trading system with the explicit aim of reducing U.S. trade deficits and reviving domestic industrial production. It is also aggressively trying to shrink government expenditure by undertaking dramatic cuts to government staff levels and by radically reducing the footprint of various federal government agencies.

Furthermore, the Trump administration is attempting to fundamentally refashion America's foreign policy goals and objectives as it downplays long-held principles and disregards global institutions. This has unsettled both foes and allies alike. A crude yet significant shift towards foreign policy realism appears to have ushered in a more transactional world order [3].

Just months into the Trump 2.0 era, both U.S. and global investors are being forced to reconsider the continuing validity of the 'U.S. exceptionalism' narrative. In fact, the initial phase of Trump 2.0 has seen U.S. equities underperform as fears of a serious economic slowdown take hold. Meanwhile, prospects appear to have sharply improved for the supposedly sluggish economies of China and the European Union.

The rest of the world is responding to tariff threats from the Trump administration by undertaking much-needed economic and policy reforms to reduce their reliance on an increasingly capricious America. In Europe, there is a fresh impetus to boost spending on infrastructure and defense.

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Significantly, after decades of self-imposed fiscal conservatism, Germany recently announced plans to setup a €500 billion fund for infrastructure investment and reached a political consensus to loosen up government borrowing rules. Meanwhile, China's AI industry has shown that it is capable of challenging Silicon Valley's dominance. The success of DeepSeek and Manus AI has raised questions about the financial soundness of the strategies being pursued by American tech giants (who are splurging hundreds of billions of dollars on fresh capital expenditure each year). China also plans to take steps to boost domestic consumption and expand its engagement with non-U.S. trading partners.

There has been a striking shift in the underlying economic narrative and, concurrently, a dramatic surge in U.S. and global economic policy uncertainty (see **Figure 1** and **Figure 2**). Financial market volatility has also risen sharply as markets reassess their initial optimism.

Abrupt shifts in policies and the lack of a coherent agenda have heightened the level of uncertainty and rendered it nearly impossible to undertake any sort of forecasting. They have also raised vital questions regarding business cycle drivers. Specifically, they have forced economists and market participants to consider whether a major shift in the economic narrative and a surge in uncertainty can significantly impact the U.S. business cycle?

Economic models that assume rational agents and efficient financial markets are not very helpful in addressing real-world economic challenges involving radical and chaotic policy regime shifts. In their book, *Shocks, Crises, and False Alarms* [4], economists Phillip Carlsson-Szlezak and Paul Swartz note that standard macroeconomics offer limited guidance to executives seeking clear answers during periods of economic turmoil or wild market gyrations. They note: "For all its scientific veneer and Greek-letter equations, the discipline offers no precise instruments for business leaders to rely on" (Carlsson-Szlezak and Swartz, 2024, p. 7).

Phillip Carlsson-Szlezak and Paul Swartz recommend that business executives embrace a more grounded approach to evaluating and understanding macroeconomic risk. They argue that the goal is "to arrive not at a settled truth but at situational judgement" and make the case for treating macroeconomics as a "set of narratives" that is "built on judicious use of data combined with context and history" (Carlsson-Szlezak and Swartz, 2024, p. 8). They also advocate for adopting an eclectic approach when undertaking macroeconomic risk analysis. According to them, such an approach requires "a mindset that frees itself from a preeminent theory, school of thought, or philosophy that presumes to offer a single, reliable lens with which to assess risks. Instead, an eclectic mindset is situationally aware, focused on causal persuasiveness and coherence in narrative" (Carlsson-Szlezak and Swartz, 2024, p. 10).

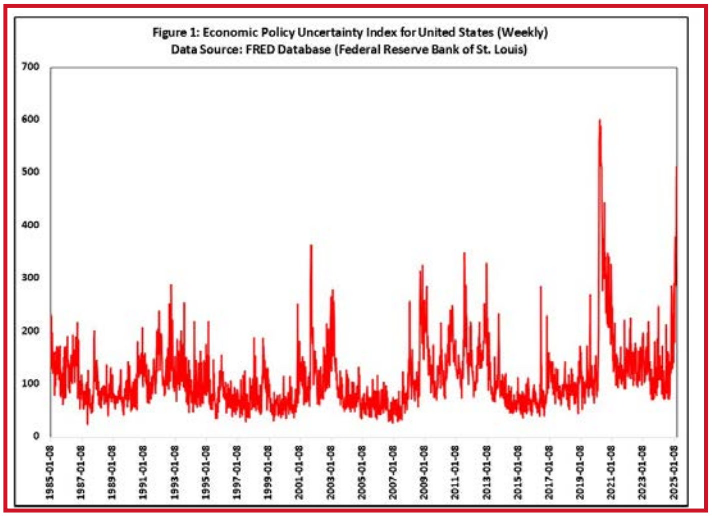


Figure 1: Economic Policy Uncertainty Index for United States (Weekly)
Data Source: FRED Database (Federal Reserve Bank of St. Louis)

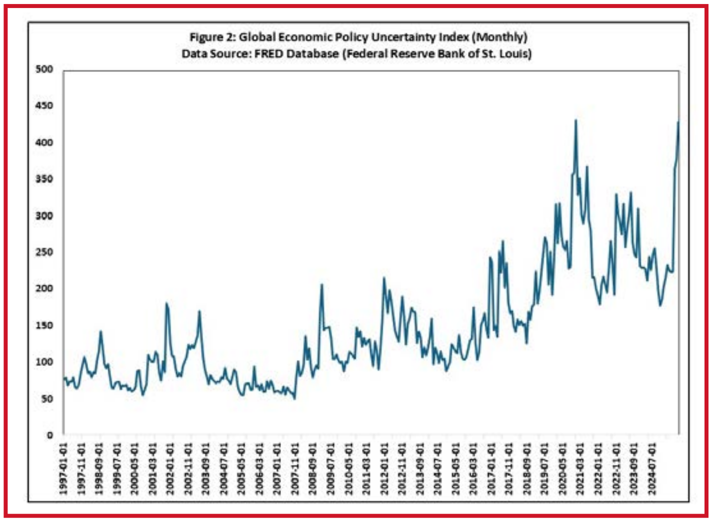


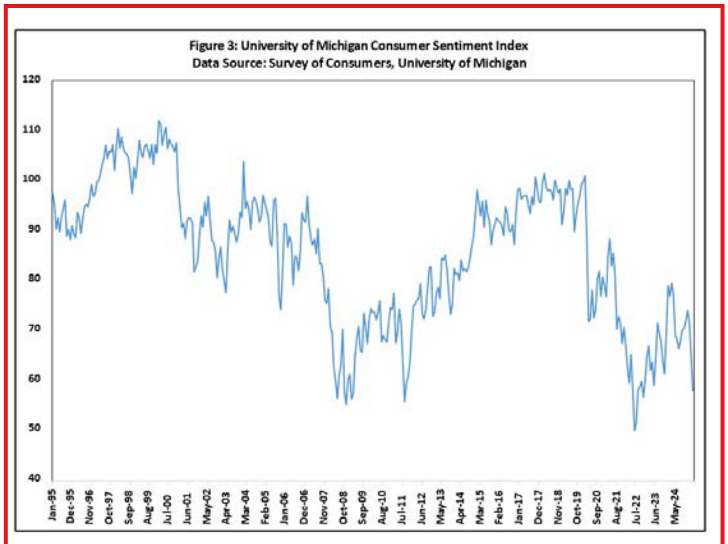
Figure 2: Global Economic Policy Uncertainty Index (Monthly)
Data Source: FRED Database (Federal Reserve Bank of St. Louis)

In many ways, the renewed emphasis on economic eclecticism harkens back to the approach taken by the founder of macroeconomics, John Maynard Keynes. In 1936, Keynes introduced the concept of 'animal spirits' in *The General Theory of Employment, Interest, and Money* [5] to describe how psychological factors, such as emotions and instincts, influence economic decision making. Keynes suggested that individuals may base their consumption or investment decisions not on purely rational calculations but on emotions such as confidence and optimism or fear and pessimism. He also highlighted the pervasive role played by uncertainty, noting that people and businesses often make decisions based on imperfect knowledge about the future (which leads to unpredictability in consumption and investment patterns).

Keynes argued that when people are confident and their spirits are high, they are more likely to spend, invest, and take risks, thus stimulating economic growth. Conversely, when confidence is low, people may become more cautious, cutting back on spending and investment, which can lead to economic slowdowns or even recessions.

Recently, several of the original insights proffered by Keynes have been revived by Nobel laureate Robert Shiller and others. In his Presidential address to the American Economic Association, Shiller (2017, p. 967) noted: "By narrative economics, I mean the study of the spread and dynamics of popular narratives, the stories, particularly those of human interest and emotion, and how these change through time, to understand economic fluctuations. A recession, for example, is a time when many people have decided to spend less, to make do for now with that old furniture instead of buying new, or to postpone starting a new business, to postpone hiring new help in an existing business, or to express support for fiscally conservative government. They might make any of these decisions in reaction to the recession itself (that's feedback), but to understand why a recession even started, we need more than a theory of feedback. We have to consider the possibility that sometimes the dominant reason why a recession is severe is related to the prevalence and vividness of certain stories, not the purely economic feedback or multipliers that economists love to model."[6]

Inspired by Shiller's call to action, economists Joel Flynn and Karthik Shastry recently used natural language processing methods to measure narratives and their influence. Using large textual databases (constructed from earnings calls and 10-K regulatory filings), Flynn and Shastry (2024, p.1) find that "optimistic narratives predict greater hiring by firms. Moreover, optimism does not predict positive future fundamentals. This is consistent with our interpretation that optimism captures a non-fundamental narrative and inconsistent with the alternative interpretation that optimism encodes firm-level news about fundamentals. Moreover, narrative optimism spreads contagiously and associatively among firms. Together, these estimates empirically discipline how narratives affect decisions and how they spread."[7]



During the first couple of months of the Trump 2.0 era, the administration has managed to dramatically raise the level of uncertainty and radically alter the underlying economic narrative. The magnitude of the tariffs and their haphazard implementation, the spending cut antics of the Elon Musk-led Department of Government Efficiency (DOGE), the aggressive and disorganized approach towards deporting illegal migrants, and the awkward geopolitical activism have all sown widespread confusion and contributed to a decline in consumer sentiments (see **Figure 3**) and business confidence. There is a clear and present danger that the continuation of such sweeping and controversial policy measures will induce an economic slowdown or, even worse, generate a stagflationary shock.

Inflation expectations have risen as households and businesses consider the impact of tariffs on crucial inputs like aluminum, steel and lumber. Furthermore, a potential decline in labor supply (resulting from a highly restrictive approach to immigration) will revive fears of an inflationary spiral. Additionally, if inflationary pressures remain elevated, the Federal Reserve is likely to find it hard to ease monetary conditions even when faced with a deterioration in the labor market and a pullback in spending by households.

Capital investment may be delayed or even abandoned if corporate leaders cannot get clarity on government tariff plans. Initially, many investors and business leaders naively believed that the administration planned to use tariffs primarily as a negotiating tool to obtain concessions from key trading partners. There is now a slow but gradual realization that President Trump is committed to radically rewiring the global trading system, with potentially significant consequences for both Wall Street and the real economy.

In February, President Trump highlighted his strong desire to overhaul America's trade ties by signing a presidential memorandum[8] "ordering the development of a comprehensive plan for restoring fairness in U.S. trade relationships and countering non-reciprocal trading arrangements." Though vague in details, the memorandum stated: "The "Fair and Reciprocal Plan" will seek to correct longstanding imbalances in international trade and ensure fairness across the board."

To be fair to the Trump administration, it has to some extent correctly diagnosed the underlying symptoms that have been apparent for decades. The struggles of the industrial heartland and challenges faced by low- and middle-income workers have recently been well-documented. MIT economist David Autor and others have analyzed the impact of the so-called 'China Shock' on local and regional economies and highlighted the importance of the distributional effects of international trade. For instance, Autor, Dorn, and Hanson (2016, p. 205) note: "Alongside its heralded consumer benefits, trade has both significant distributional costs, which theory has long recognized, and substantial adjustment costs, which the literature has tended to downplay. These adjustment costs mean that trade impacts are most visible not in national-level outcomes for broad skill types, as canonical theory would suggest, but in the local labor markets in which the industries most exposed to foreign competition are

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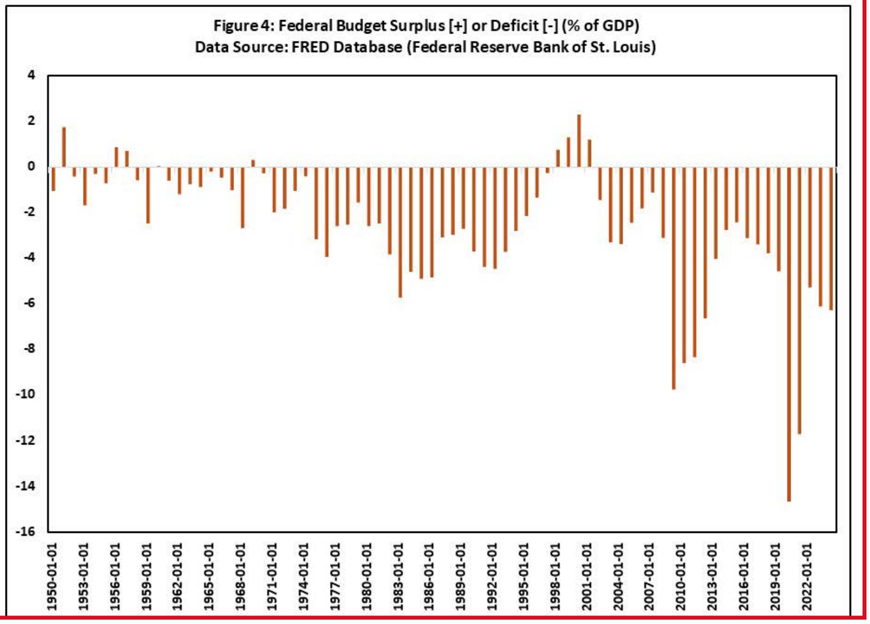
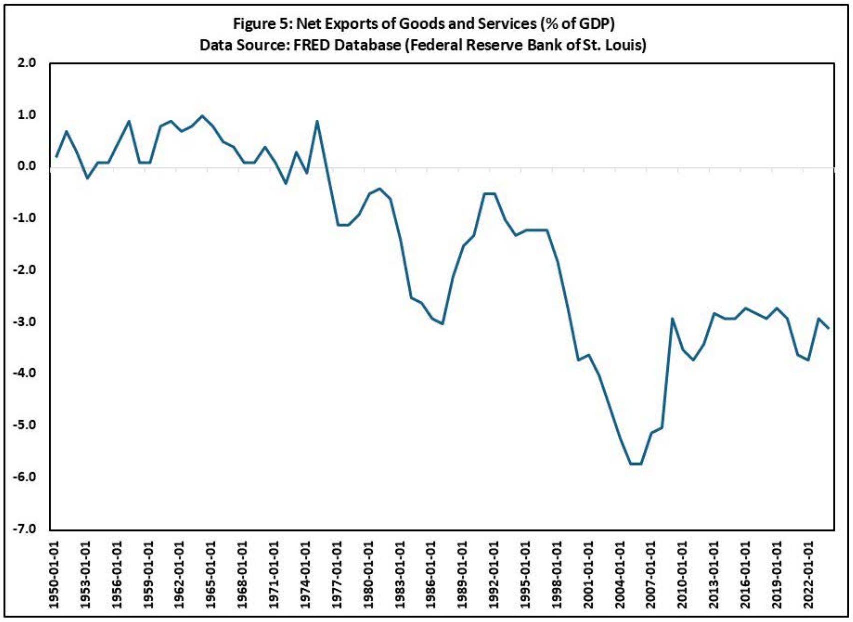
concentrated. Adjustment in local labor markets is remarkably slow, with wages and local labor-force participation rates remaining depressed, local unemployment rates remaining elevated, and public transfer benefits take-up rising across a spectrum of programs for at least a full decade after trade shocks commence."[9]

The administration is hoping to cajole foreign companies and U.S. multinationals to setup factories in America to spur a manufacturing renaissance. The basic problem is that, even if reshoring were to occur, it is unlikely to generate many manufacturing jobs as today's factories mostly rely on automation to produce goods. Furthermore, many American companies rely heavily on imported intermediate inputs to manufacture high value-added products. President Trump appears to not fully appreciate the extent to which modern manufacturing is reliant on a complex web of global supply chains that have taken decades to setup and involve an interlinked network of geographically dispersed input and raw material suppliers.

Another avowed goal of the tariff policy agenda is to raise revenue for the government coffers. Some of the more ambitious proposals under Trump 2.0 imagine a world where tariff revenue would be high enough to pay for various tax cuts. Such goals are inherently contradictory – if tariffs were to lead to a decrease in imports, then it is unlikely to be a major source of government revenue.

The Trump administration is also right in arguing that the American economy has gotten hooked on government largesse in recent years. In fact, a crucial but underappreciated reason for recent U.S. economic exceptionalism vis-à-vis its advanced economy peers was the massive increase in U.S. government spending since 2020. Through the Cares Act, the Consolidated Appropriations Act and the American Rescue Plan Act, the U.S. government added $6 trillion of stimulus. The Biden administration further juiced the economy with the Inflation Reduction Act and the CHIPS and Science Act. Consequently, the U.S. budgetary balances (see **Figure 4**) have deteriorated sharply, and the size of the government debt has exploded.





Large government deficits can also affect the trade balance. According to the fundamental open-economy identity, the difference between total national saving (the sum of private and public sector saving) and gross domestic private investment should equal the current account balance (which includes the trade balance). Thus, a country with excess national saving will run a current account surplus and be a net foreign lender, and a country experiencing a national saving shortfall will experience a current account deficit and be reliant on overseas borrowing. The U.S. has persistently run a trade deficit during the past five decades (see Figure 5). Perennial budget deficits (negative government saving) are a major contributing factor to the national saving shortfall. One way to reduce trade (and current) account deficits is to reduce government budget deficits and thus raise the national saving level.

Once more the underlying symptoms have correctly been identified. The problem lies with the Trump administration's approach towards improving government finances. Cutting government waste and trimming bureaucratic excesses is obviously a worthwhile endeavor. However, the chaotic nature of DOGE cuts has spread fear among federal workers and government contractors. Cuts in research grants have affected universities and research institutions. Longer term, a potential decline in the quality of services offered by key government agencies and a cut back in funding for basic scientific research may end up lowering U.S. growth rates.

President Trump is also unwilling to cut Social Security and Medicare benefits, which account for the lion's share of non-discretionary government spending. To achieve true long-term fiscal sustainability and restore fiscal sanity, the administration would have to seek unpopular cuts to social safety net programs and significantly trim the bloated military budget. The push to make permanent the 2017 Trump tax cuts (with possible inclusion of additional tax cuts) could threaten long-term U.S. fiscal sustainability if the cuts don't lead to a dramatic pickup in GDP growth rates.

Treasury Secretary Scott Bessent has suggested that the U.S. economy must go through a "detox period" to break its addiction to debt-fueled fiscal transfers and cheap imports. President Trump has noted that a "period of transition" is inevitable as he tries to drastically rewire the global trading system. The danger is that a radical agenda, when combined with incoherent policies and chaotic implementation, raises the risk of paralyzing the economy in the short to medium term. It is hard to imagine reaching the other side of the chaos without undergoing a period of painful adjustment.

There are some historical parallels. During the early days of the Great Depression, Andrew Mellon, Herbert Hoover's Treasury Secretary, was worried about the economic imbalances and financial distortions that were built up during the roaring twenties. He famously urged President Hoover to "Liquidate labor, liquidate stocks, liquidate the farmers. … It will purge the rottenness out of the system."[10] While the desire to correct past excesses may be natural, there are grave dangers to consider when dealing with the macroeconomy, especially one as large and complex as today's American economy.

The risk of engaging in rapid and chaotic policy regime shifts is that we may affect the underlying economic narrative (shifting it from one of hope and optimism to one that is dominated by pervasive fear and confusion). Heightened levels of uncertainty among private sector actors have the potential to cause a pullback in consumer spending and in business fixed investment. They may also lead to a reevaluation of risk appetite and cause a lowering of asset values. The economy may end up being pushed towards a lower equilibrium.

In *The General Theory of Employment, Interest, and Money*, Keynes introduced the concept of multiple equilibria. The notion that the economy could exist in a variety of stable states (some desirable and others not so much) was one of the key Keynesian insights. Today's policymakers need to be aware that there might not exist a single equilibrium to which the economy naturally gravitates in the absence of policy-induced distortions. Instead, the real world might be characterized by a continuum of equilibria and variations in the degree of optimism or pessimism can shift the economy from one type of equilibrium to another.

Write to Prof. Jayakumar at
vjayakumar@ut.edu

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The Tampa Bay Economy and Trump 2.0

By John R. Stinespring, Ph.D.

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It is March 2025 and the data are in for the Biden presidency. We can now ask, How did the Tampa Bay economy perform under President Biden's term? How did this performance compare to that under President Trump's term? And did we experience the soft landing the Federal Reserve attempted to engineer? Answers to these questions will provide insight into what sort of economy the second Trump term has inherited compared to their first term and how it might perform going forward. To answer, we first examine the national figures for inflation and output and then delve into the details of the labor, retail, and housing markets for our local Tampa Bay metropolitan area (consisting of Hernando, Hillsborough, Pasco, and Pinellas counties combined). We will include references to Florida and the U.S. economy where relevant.

We first consider the economic nemesis of the Biden administration, inflation. **Figure 2.1** shows the bi-monthly inflation from January 2017 to January 2025 on a year-over-year basis for the Tampa Bay (TB) economy and the country overall (U.S.). The first Trump term (TT) inherited a moderate 2.8 percent TB inflation rate and 2.4 percent U.S. rate. These rates were near the historical average over the years 1988-2016–TB data begins in 1988–of 2.7 for TB and 2.6 percent for the U.S. During that Trump administration, TB inflation peaked at 3.8 in January 2020 and experienced its largest decline during the TT's pandemic recession as shown on the plot by the narrow-shaded area. The Trump economy's inflation performance at the end was split: the U.S. rate of 1.4 percent was well below the historical average in January 2021 while the TB rate of 3.4 was well above it.

The Biden administration inherited these inflation rates but presided over a consistent and dramatic rise until peaking at 11.3 percent for TB and 8.5 for the U.S. in May 2022. To combat the high inflation, the Federal Reserve bank instituted an aggressive series of interest rate increases from March 2022 until July 2024. The effects of these rate hikes are seen within the plot's wide-shaded area. The Fed's policy was particularly effective in lowering the TB inflation rate to 1.2 and the U.S. to 2.4 percent by September 2024 (interestingly, the period available just before the election). By January 2025 the second Trump administration was able to begin their term with inflation rates of 2.3 for the TB and 3.0 for the U.S., again near the 1988-2016 averages.

If inflation was the economic nemesis of the Biden administration, real Gross Domestic Product (RGDP) may have been President Trump's. **Figure 2.2** shows the quarterly RGDP growth rate on a year-over-year basis and reveals that the first Trump administration inherited an economy that had grown a moderate 2.2% in the last quarter of 2016. Figure 2.2 also shows the *annual* real Gross Metropolitan Product (RGMP) for TB. These data reveal that the TT inherited a TB economy that had grown 3.4% in 2016. Up until January of 2020, the TT could claim an average growth rate of 2.7 percent for U.S. RGDP and 2.9 for the

Figure 2.1 TB and U.S. CPI Y-O-Y Inflation 2017-2025
Source: Bureau of Labor Statistics and Author's Calculations

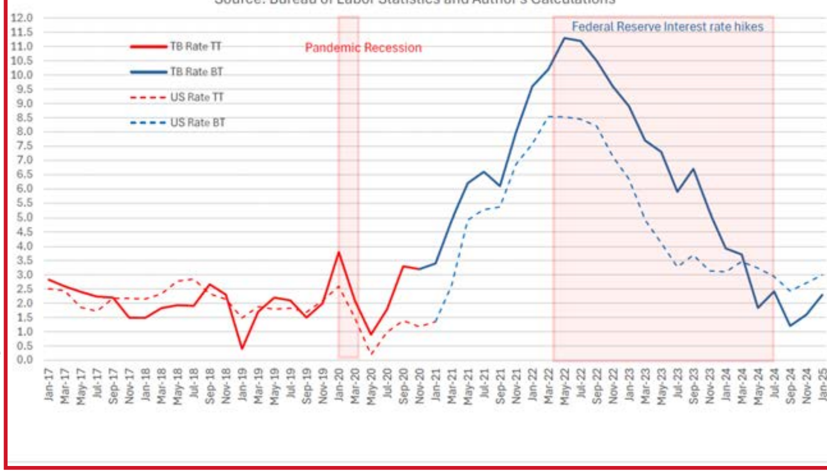
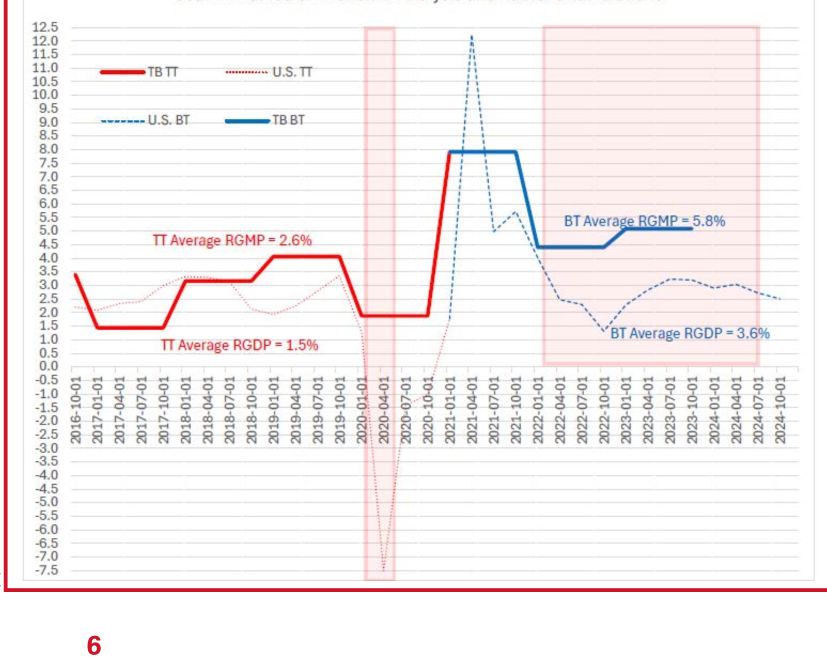


Figure 2.2 RGDP and RGMP % Change Year-Over-Year 2017-2024
Source: Bureau of Economic Analysis and Author's calculations



TB's RGMP. Though lower than Biden's term's (BT) impressive first 3 years' average of 3.9 percent for U.S. RGDP and 5.8 for the TB's RGMP, the TT figures were still above historical averages. The plot shows that the pandemic recession in March 2020 caused sufficient economic damage to lower average economic growth even more over the TT. Comparing the TT and BT terms, we see Trump averaged 1.5% in quarterly RGDP growth while Biden averaged 3.6%. Similarly, TB grew 2.6% over the TT and 5.8% over the BT (excluding the 2024 data not yet available). Note that RGDP growth was positive but declining over the 2024 period suggesting a successful soft landing may have left a soft economy in tow. In fact, the most recent data suggests we might expect the U.S. and TB economic growth to fall for the initial period of the new Trump administration as happened during his first term.

To get beneath the aggregate numbers, we consider the labor market. **Figure 2.3** shows unemployment for TB, FL, and the U.S. At the start of the TT, the local unemployment rate was 4.5% in January 2017 for Tampa Bay and 4.7% for both Florida and the U.S. These low unemployment figures that the Trump administration inherited came from eight years of what became the U.S.'s longest recorded economic expansion. The expansion continued during Trump's first three years and the unemployment rate fell by January 2020 to 3.2%, 3.0% and 3.6%, for TB, FL, and the U.S., respectively. The TT ended with an elevated unemployment rate of 5.4% for TB and 6% for both FL and the U.S. by January 2021 as the negative economic shock from COVID-19 persisted.

The Biden administration inherited a crippled U.S. labor market with the actual labor force being smaller at the end of the TT than at its beginning. The second Trump administration, on the other hand, has inherited a vibrant job market. The Biden administration left office in December 2024 with near historically-low unemployment rates of 3.3%, 3.1%, and 3.7%, for TB, FL, and the U.S., respectively. What appears evident in the data, however, is that unemployment has risen modestly but persistently since 2023. Again, suggesting a relatively stable but perhaps soft economy.

The unemployment declines and spikes over the two terms were mirrored by expansions and declines in TB payrolls data. **Figure 2.4** shows a long increase in monthly payrolls throughout the period. The TT started with 1.315 million and interestingly, like the initial slowdown in output, payrolls initially declined. Yet after stimulus packages in 2017 and 2018, the TB payrolls added 97,300, a growth of 7% by February 2020. The damage to payrolls from COVID-19, however, meant that by December 2024, only 1.373 million were on TB payrolls, reducing the overall growth of 4% for the TT. This rate was low, but at least positive, compared to the national decline.

Given these issues, the BT started with 1.373 million on TB payrolls. Even with the Fed's contractionary policy, our local economy added 192,000 jobs, a growth of 14% over the BT. Like the low but rising unemployment since 2023, payroll growth has slowed as expected if a soft landing was achieved. The contractionary policy coupled with 2024's double hurricane hit in September-

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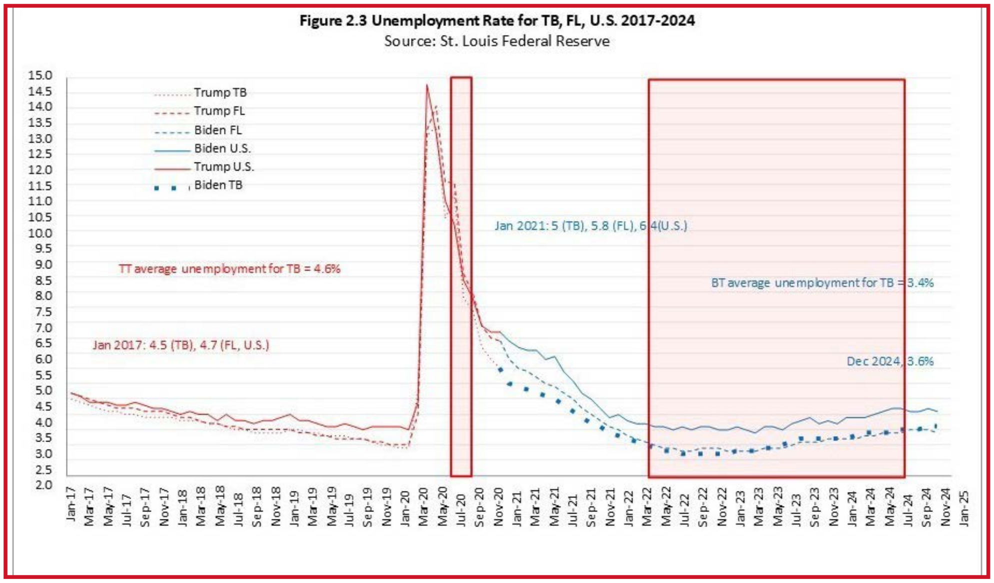

Figure 2.3 Unemployment Rate for TB, FL, U.S. 2017-2024
Source: St. Louis Federal Reserve

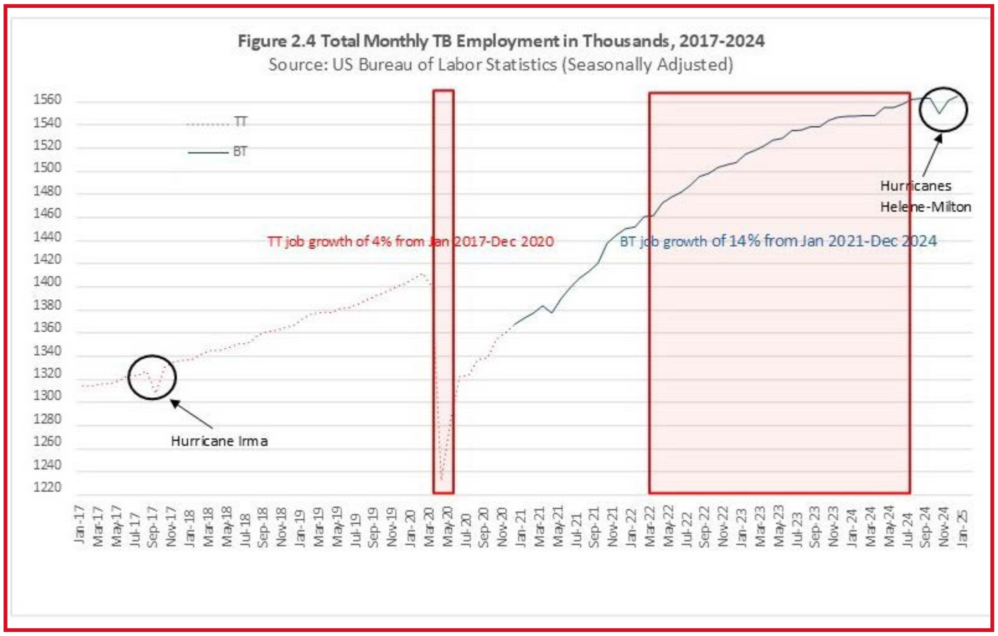

Figure 2.4 Total Monthly TB Employment in Thousands, 2017-2024
Source: US Bureau of Labor Statistics (Seasonally Adjusted)

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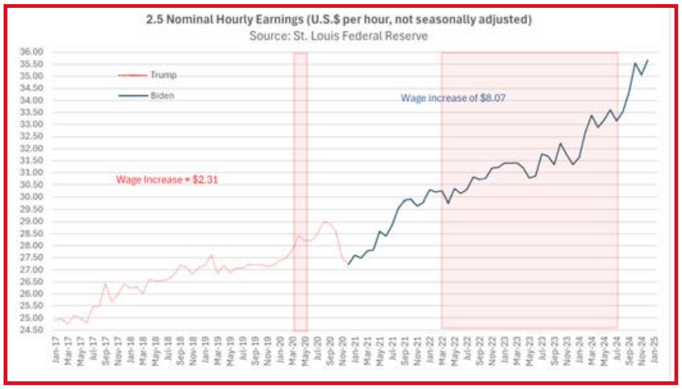
October lend credence to the notion of the Trump administration inheriting a stable but soft economy.

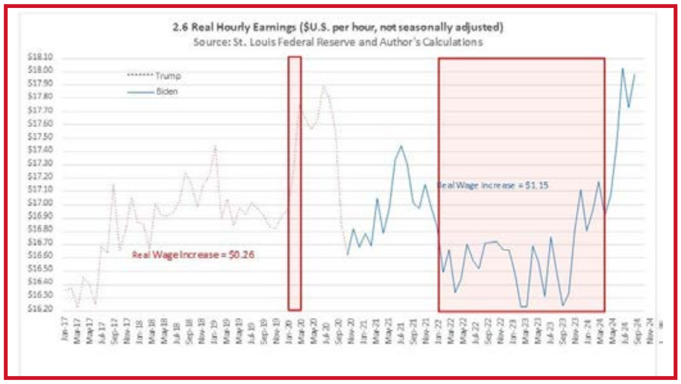
The job growth and low unemployment over the last four years combined to put upward pressure on nominal hourly earnings as seen in **Figure 2.5**. The BT saw an increase of $8.07 in the hourly wage while the TT saw a $2.31 increase. Real earnings, however–that is nominal earnings adjusted for the price level–tell us what these nominal wages actually can purchase. **Figure 2.6** shows that over the TT real hourly earnings initially grow significantly but then plateau around a volatile $17 prior to the pandemic then fall precipitously with nominal wages declining while inflation rose. Overall, the TT experienced a $0.26 increase in real wages. The BT saw real hourly earnings initially grow but then rapidly decline as inflation continued to rise and the Federal Reserve initiated its contractionary policy. When the Fed finally initiated its interest rate cut in September 2024, real hourly earnings rose dramatically and ended at $17.97 by December 2024. In terms of real wage changes, the BT experienced a $1.15 increase. This also has placed the Trump administration in a positive economic position.

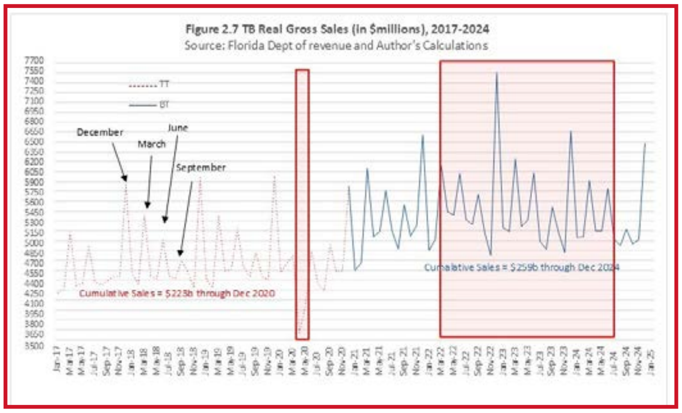
What did overall demand look like in our local economy under the two administrations? **Figure 2.7** shows real TB Gross Sales depicted in millions of inflation-adjusted dollars. Sales are a coincident business cycle indicator that declines during recessions and grows during expansions with seasonal spikes in December, March, June, and September for each year. Real Gross Sales for TB trended upward over the two presidencies. Given that real wages grew more under the BT than the TT, higher inflation-adjusted sales for the BT is expected and apparent from the graph. The TT experienced cumulative sales of $223b through December 2020, while the BT experienced cumulative sales of $259b through December 2024. (In terms of the reported nominal data, cumulative sales were $565b under the TT and $766b under the BT.) Though sales over the last few years were robust in TB, a plateauing appears in the data for 2024. As a coincident indicator it suggests the local economy was near a goldilocks position in the business cycle experiencing economic growth that was neither too fast nor too slow.

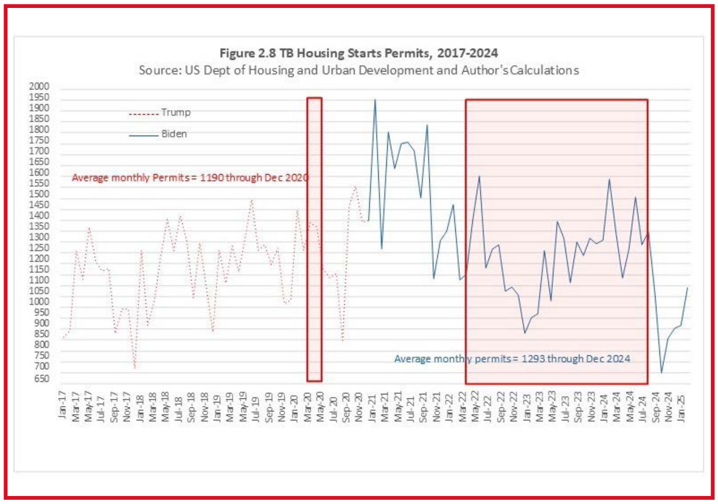
Our final market, housing, is a *leading indicator* that predicts the direction of the economy in that sustained increases in construction lead economic expansions while recessions are presaged by sustained declines. Recent data for this market lends support to the notion of a soft landing leaving a soft economy in its wake. **Figure 2.8** shows TB building permits over the two presidential terms up to January 2024. Average monthly permits over the TT were 1,190 through Dec 2020. After the steep pandemic decline, permits made up losses by overshooting the trend from January 2021 to October 2021. Precipitous declines occurred by May 2022 shortly after the Fed contractionary policy was enacted. Permits returned to their higher pre-COVID levels in January 2024 but have shown volatile declines and increases since July 2024. Even with such headwinds, average monthly permits over the BT were 1293 through December 2024, 8.6 percent higher than the TT. Yet the 2024 decline provides another piece of evidence suggesting a softening economy.

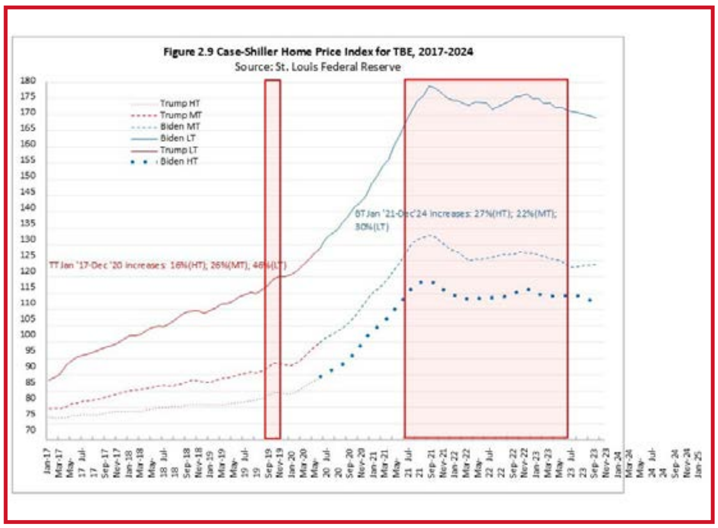
The housing market's resilience to COVID-19 and vulnerability to the Fed's contractionary policies are even clearer in the home price data. **Figure 2.9** shows the Case-Shiller housing price index (adjusted for inflation) for low-, medium-, and high-tier home prices in TB (where index = 100 for year 2000 and adjusted for inflation). All tiers of TB homes experienced a relatively steady increase over the TT up to December 2020. Prices in December 2020 were 16, 26, and 46 percent above their January 2017 levels for high-tier, mid- tier, and low-tier, respectively. Over the BT through January 2024, the increases were 27, 22, and 30 percent above their January 2021 levels, respectively. These significant increases came to an abrupt halt shortly after the Fed's contractionary policy. By June 2022, prices began a persistent, if not monotonic, decline through December 2024.

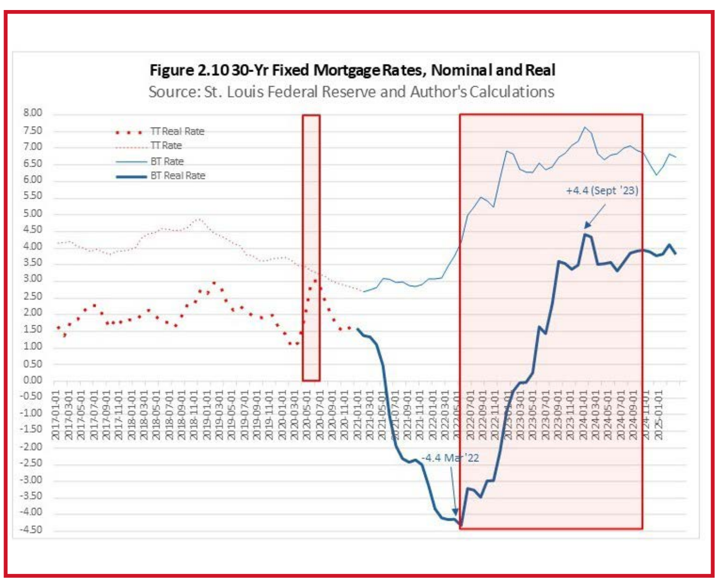












Yet the 2024 decline provides another piece of evidence suggesting a softening economy.

The correlation between these housing movements and 30-year mortgage rates is evident from **Figure 2.10**. The nominal mortgage rate declined over the TT while the real rate moved up and down around 2 percent. The nominal rate rose throughout the BT while the real rate fell immediately upon taking office and then went negative by mid-2021 as the growth in inflation exceeded that in the interest rate. The decline continued until the beginning of the Fed's contractionary policy in March 2022. In fact, we saw a move from the low of a negative 4.4 real rate to a positive 4.4 real rate over the March 2022 through December 2024 period. These reversals explain the subsequent permit slowdown and price plateauing.

This update has answered three questions using the U.S. and Tampa Bay economy data over the Biden and Trump presidential terms. The Biden administration inherited a recovering economy with a weak labor market. It faced a problem of rapidly rising inflation and the resulting sharp interest rate hikes to tame it. Yet through these hikes, the Federal Reserve Bank seems to have engineered a soft landing for the economy by lowering inflation without creating a recession. The BT ended with strong economic growth, low unemployment, and moderate though elevated inflation. Thus, the economic conditions inherited by the second Trump administration are similar to those inherited by the first. If history acts as our guide and the Trump administration implements volatile policies causing increased uncertainty—which they have at this point—we should anticipate slower economic growth in the first-quarter. The administration's early actions combined with the signs of softness described herein only increase the likelihood of an initial slowdown.

Write to Prof. Stinespring at
jstinespring@ut.edu

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