ECONOMY GROWING AT SNAIL'S PACE

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The Federal Reserve made a stark concession this week: The economy is likely to grow at a listless pace for the foreseeable future.

While the Fed left its key interest rate unchanged and signaled it could raise it twice this year, policymakers raised eyebrows by predicting markedly slower hikes in coming years amid persistent headwinds to economic growth. Those hurdles include meager productivity gains, an aging labor force, low household formation and the weak global economy, Fed Chair Janet Yellen said at a news conference following the Fed meeting.

Fed policymakers have cited these economic speed bumps before but had voiced optimism that several were temporary legacies of the Great Recession. This week, however, the Fed said it anticipates its benchmark rate will be just 2.4% at the end of 2018, down from its March forecast of 3%. And it cut its forecast of the longer run rate — to 3% from 3.3%. The Fed keeps rates low to stimulate borrowing and economic activity.

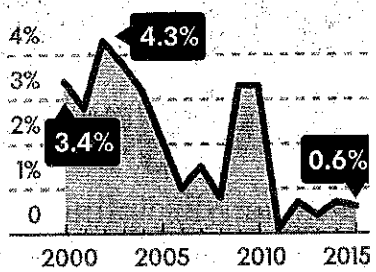
"What you saw was the Fed capitulating," economist Diane Swonk of DS Economics says. The drags on growth have "gone on long enough that they're now concerned."

Surprisingly, the Fed lowered its growth forecast only marginally, to 2% a year for 2016 through 2018 and in the longer run, just below the average pace in the seven-year recovery. But that apparently is only because the Fed expects its slower rate increases to largely offset the economic headwinds, says Dean Maki, chief economist of Point72 Asset Management. Fed policymakers, however, note that their forecasts are fluid and they'll adjust the pace of rate hikes accordingly.

Here's a look at the prospects of the headwinds easing:

PRODUCTIVITY DROP

U.S. labor productivity levels are down compared to the years following the 2000 tech bubble and the 2008-09 recession. Quarterly change in output from previous quarter.



NOTE Figures are annual rate
SOURCE Bureau of Labor Statistics
KARL GELLES, USA TODAY

▸ WEAK PRODUCTIVITY

Sluggish growth in productivity, or output per labor hour, is the biggest stumbling block because it leads to shrinking business profits, and, in turn, less hiring and investment. Productivity has grown an average of 0.5% a year the past five years, vs. 3.5% in the recovery following the 2001 recession, according to Maki and Labor Department figures.

Economists blame myriad factors. Business capital spending in labor-saving technology has been weak. Retiring baby boomers are being replaced by inexperienced Millennials. And the housing crash prevented many Americans from selling their homes so they can move to find jobs more suitable to their skills. Swonk says business investment should pick up modestly after the election alleviates political uncertainty and rising wages prompt companies to boost efficiency with new technology. Worker mobility also should improve as home prices rise. But Maki says productivity typically remains weak this late in the economic cycle because of high employment and relatively tepid growth.

▸ AGING LABOR FORCE

The labor force has been growing more slowly in recent years, mostly because millions of Baby Boomers are retiring each year. Absent stronger productivity, a modestly growing workforce means less output of goods and services. And retirees spend less, hurting consumption. The aging labor force is likely to restrain growth for the next decade, Maki says.

▸ LOW HOUSEHOLD FORMATION

Additions of owner- or renter-occupied units to the housing stock revived in 2014 but slowed last year. Sluggish wage growth has prompted many Millennials to continue living with their parents. But wage increases have edged up in recent months and are expected to accelerate as the 4.7% unemployment rate continues to fall, spurring more household formation.

▸ SLOWING GLOBAL GROWTH

China's slowdown could hamper global growth for some time as the country haltingly shifts from an economy driven by investment to consumption, Maki says. The international monetary fund expects China's economy to expand by 6.5% this year and 6.2% in 2017 after posting 6.9% growth last year.