US Economic Outlook

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Hallmarks of the IHS Markit US forecast

- COVID transition to endemic
- Solid but slowing trend growth of output, as fiscal support wanes and pent-up demand is satisfied
- Continued gradual improvement in the labor market as employment and labor force rise
- Declining inflation as output growth slows, commodity prices turn, and supply issues resolve
- Rising term interest rates
- Fed tightening. Taper has begun; policy rate to reach 2%+ by end 2022, 3%+ end of 2023
- Rougher sledding ahead for equities – down over 6% this year (December to December)
- Key risks: Persistent elevated inflation, policy (im)perfection, wider war and/or effects, new variants

Pace of US growth – balancing headwinds and tailwinds

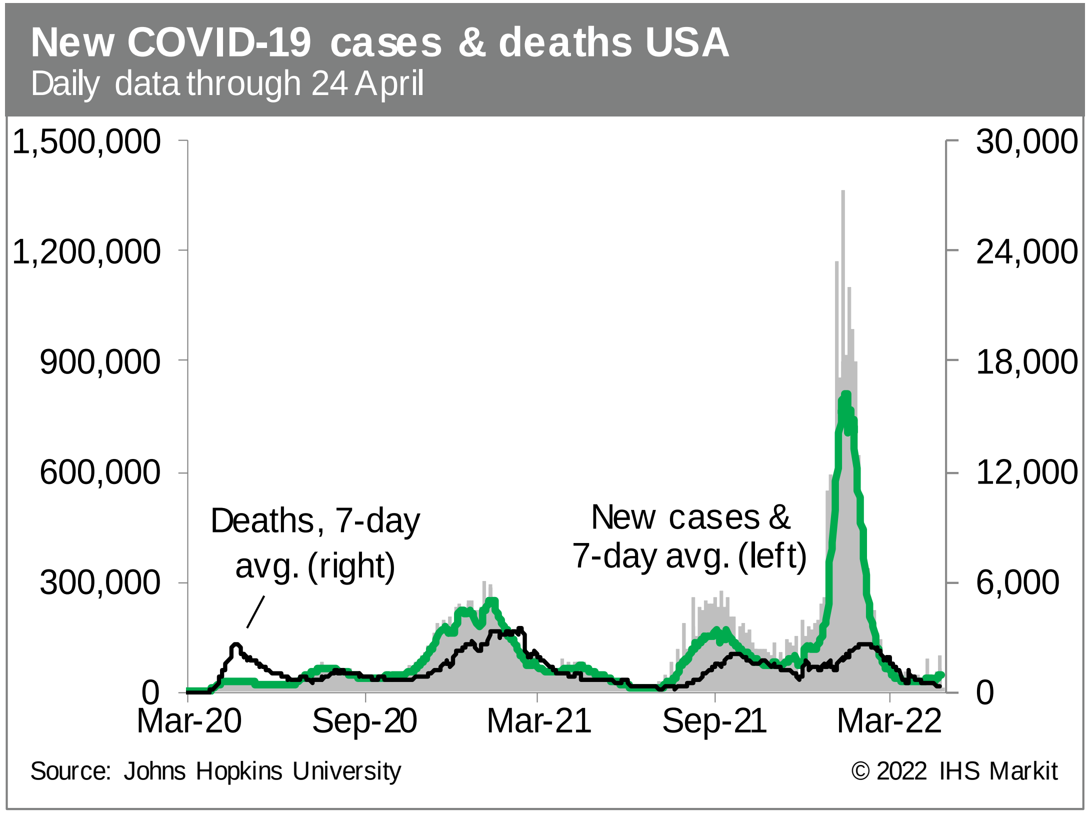
Headwinds

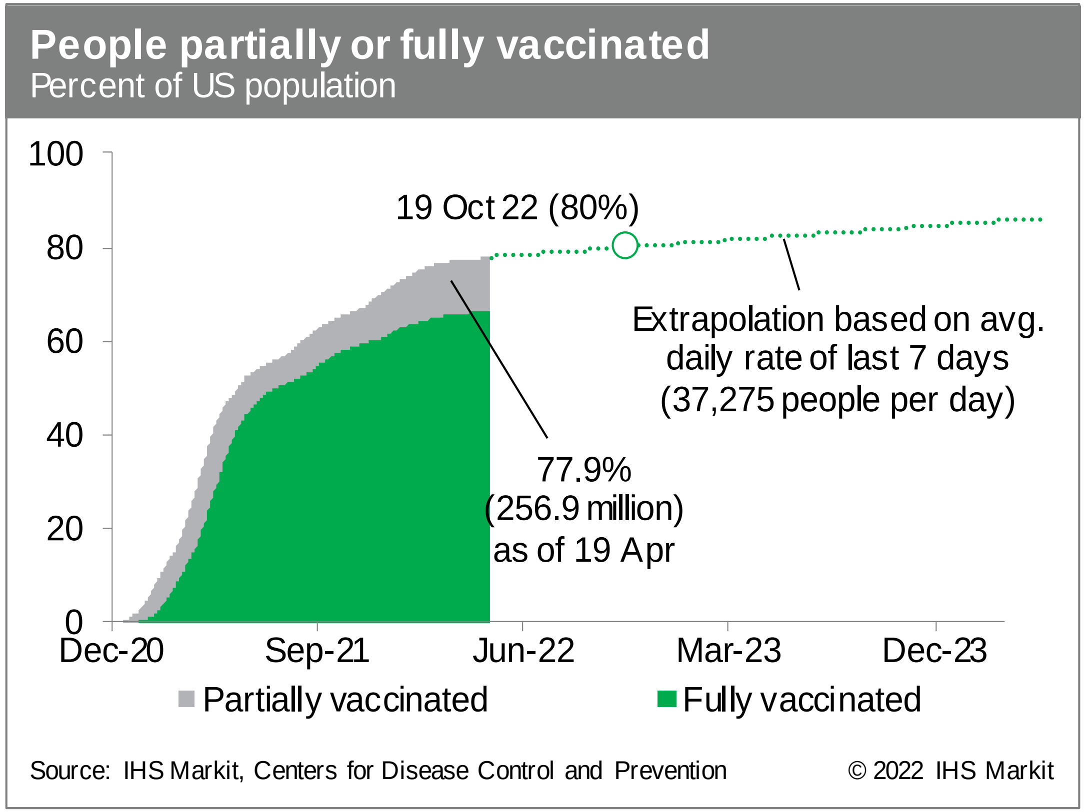
- Supply constraints, shortages of key commodities and price spikes
- Waning fiscal support
- Monetary policy tightening in face of another supply shock…term rates heading higher
- Housing has peaked
- Possible return of virulent COVID variants… … residual caution from consumers
- Still huge uncertainty; running from risk?

Tailwinds

- Widespread and still rising vaccination rates
- Release of pent-up consumer demand for socially dense spending; surge in wealth
- Accommodative monetary policy: low rates and ample liquidity, albeit accommodation lessening
- Prior generous broad-based fiscal support
- Inventory shortfalls mean re-stocking will keep factories humming
- Commodity prices turning lower … soon?

COVID-19 refusing to go quietly, but maximum impact on spending passed

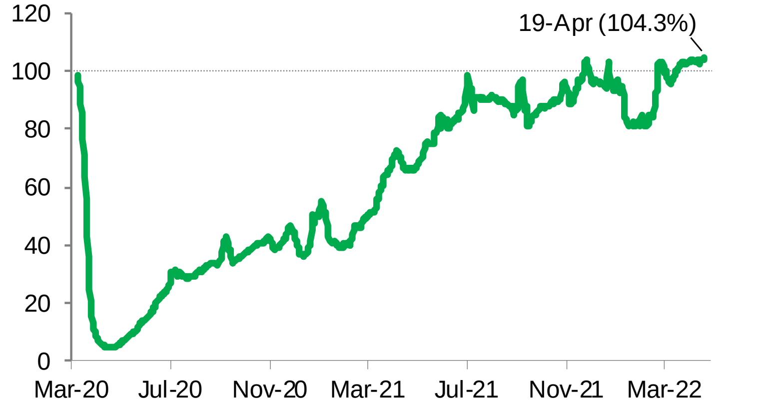




- Despite high number & % of vaccinations, the Omicron variant drove a worrying spike in new cases in areas of low vaccination rates; +75% now have at least one dose; roughly 65% are fully vaccinated
- Is the worst behind us as states lift mask mandates?

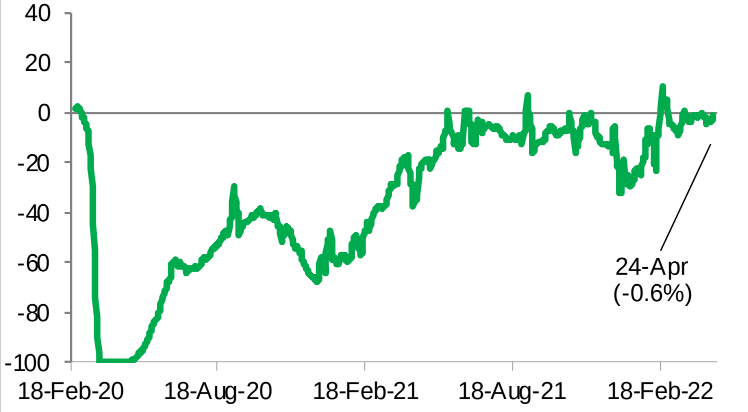
Key high-frequency indicators of consumer spending

TSA checkpoint travel numbers
Percent of January 2020 average, 7-day average, SA



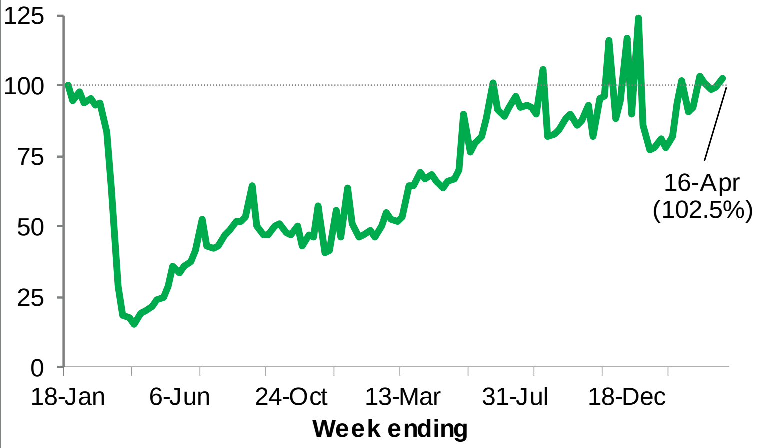
Notes: Total traveler throughput.
Source: IHS Markit, Transportation Security Administration

Seated diners at US restaurants
Percent change from comparable day, 2019, 7-day average



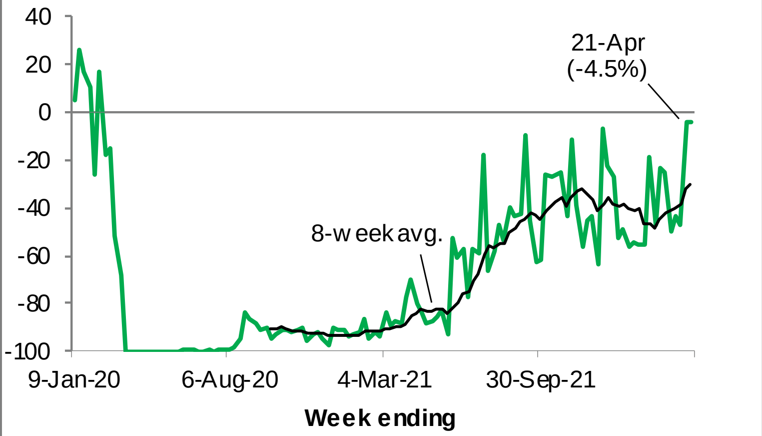
Notes: Seated diners at restaurants on the OpenTable network.
Source: OpenTable

STR hotel data: revenue per available room
Percent of mid-January 2020, SA



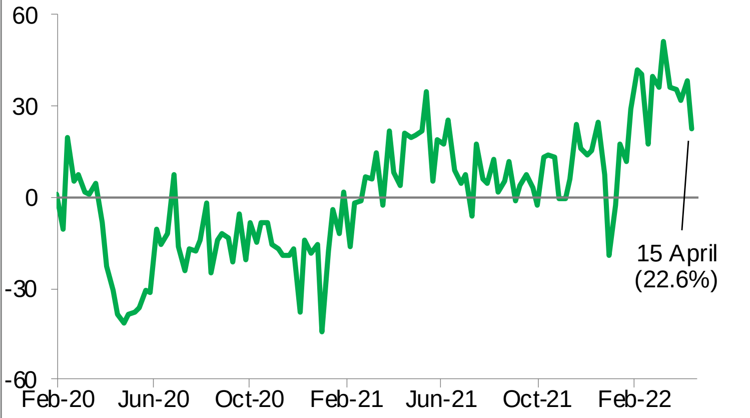
Source: IHS Markit, STR

Gross movie receipts
Percent change from comparable w eek, 2019



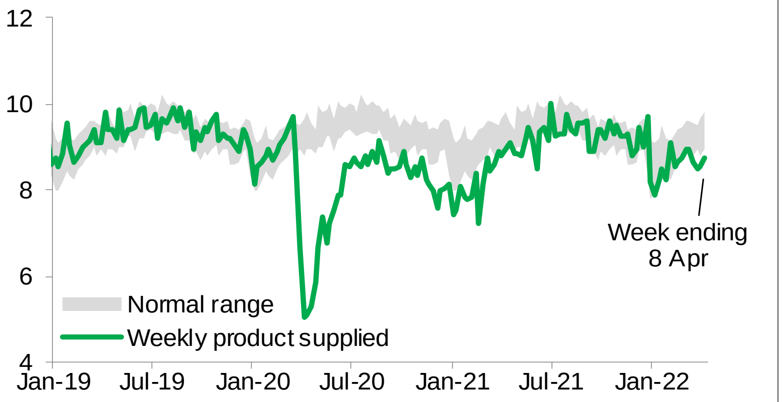
Source: Box Office Mojo

Job postings
Percent difference from Jan 2020



Source: Opportunity Insights Economic Tracker, Burning Glass Tech.

Finished motor gasoline product supplied
Million barrels per day, NSA



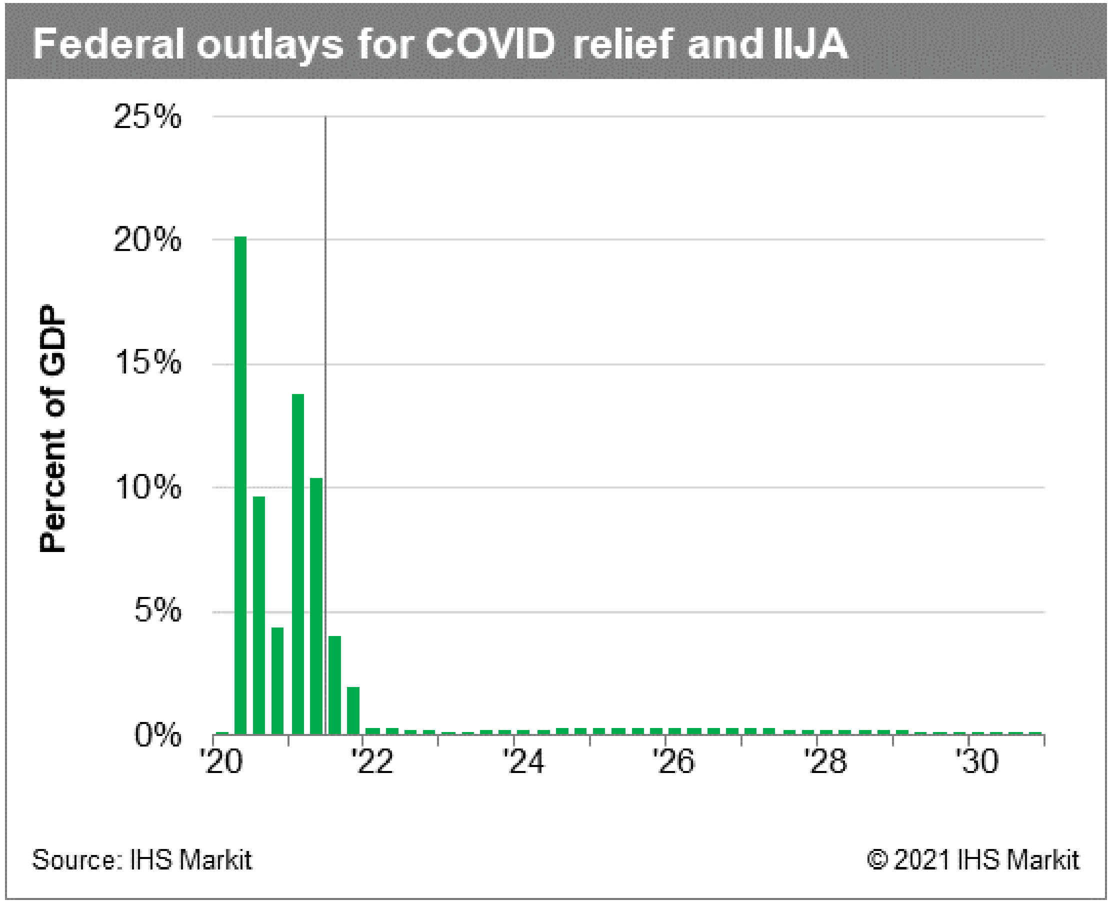
Notes: Normal range is '15–'19 average for calendar week, +/- 2 st. dev in de-cycled data
Source: Energy Information Administration, IHS Markit

Key forecast assumptions:

- Transition to endemic; containment measures, mask requirements generally gone
- Opens the way to “sustained” upturn in consumer spending, but possible residual caution
- Russia-Ukraine effects on commodities prices persists, gradually wane; sanctions remain
- Massive, but waning fiscal stimulus: $3.4 trillion of COVID-19 relief in 2020, $1.9 trillion American Rescue Plan in 2021; “new” IIJA is in the forecast with small effect; BBB not yet
- Oil prices (Brent) to peak at $119.60/bbl in Q2 2022, ease to $110 in late 2022, $87 in late 2023
- Broad non-oil commodity prices surged, but appear to have peaked, or almost
- Trade-weighted US dollar near peak, to edge higher; then fall 2½% by end 2023
- Inflation expectations remain anchored near 2%; help contain rise in inflation
- Federal Reserve ends asset purchases, begins aggressive series of rate hikes

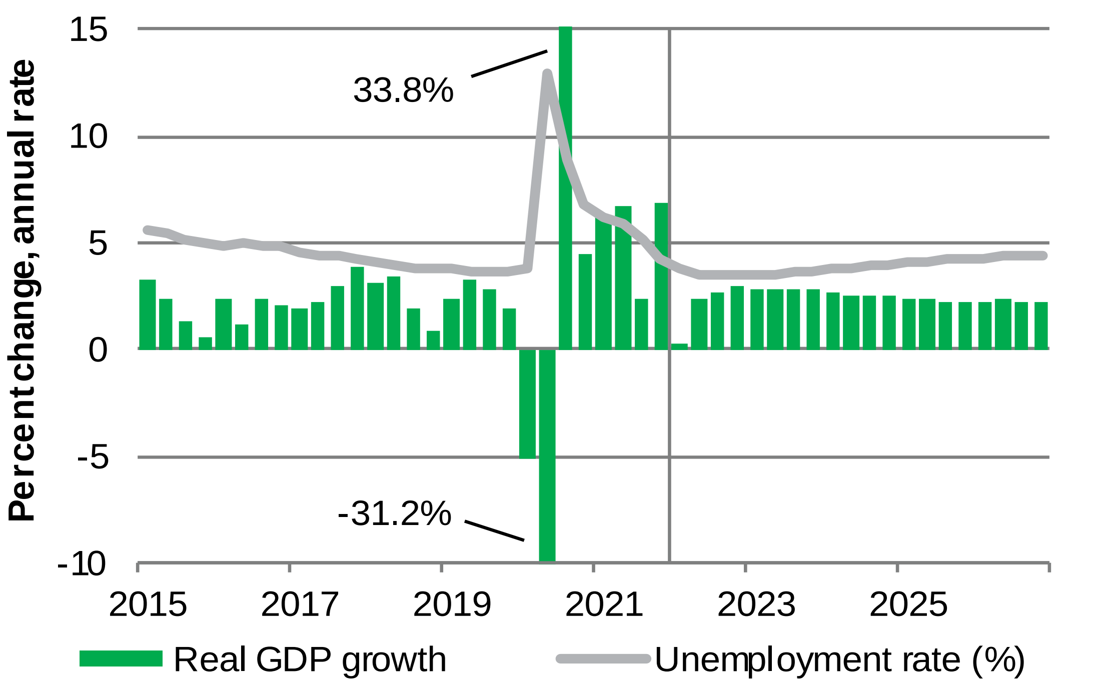
The forecast includes 6 COVID relief measures and IIJA

- COVID relief measures
  - Coronavirus Preparedness & Response Supplemental Appropriations Act
  - Families First Coronavirus Response Act
  - Coronavirus Aid, Recovery & Economic Security (CARES) Act
  - Payroll Protection & Healthcare Enhancement Act
  - Coronavirus Response & Relief Supplemental Appropriations Act
  - American Rescue Plan Act (ARP)
- Infrastructure Investment & Jobs Act (IIJA)



Waning stimulus, wealth surge, low but rising rates, rising vaccinations; intermittent virus surges, persistent inflation are risks

Growth to slow in Q1



Source: IHS Markit, BEA, BLS

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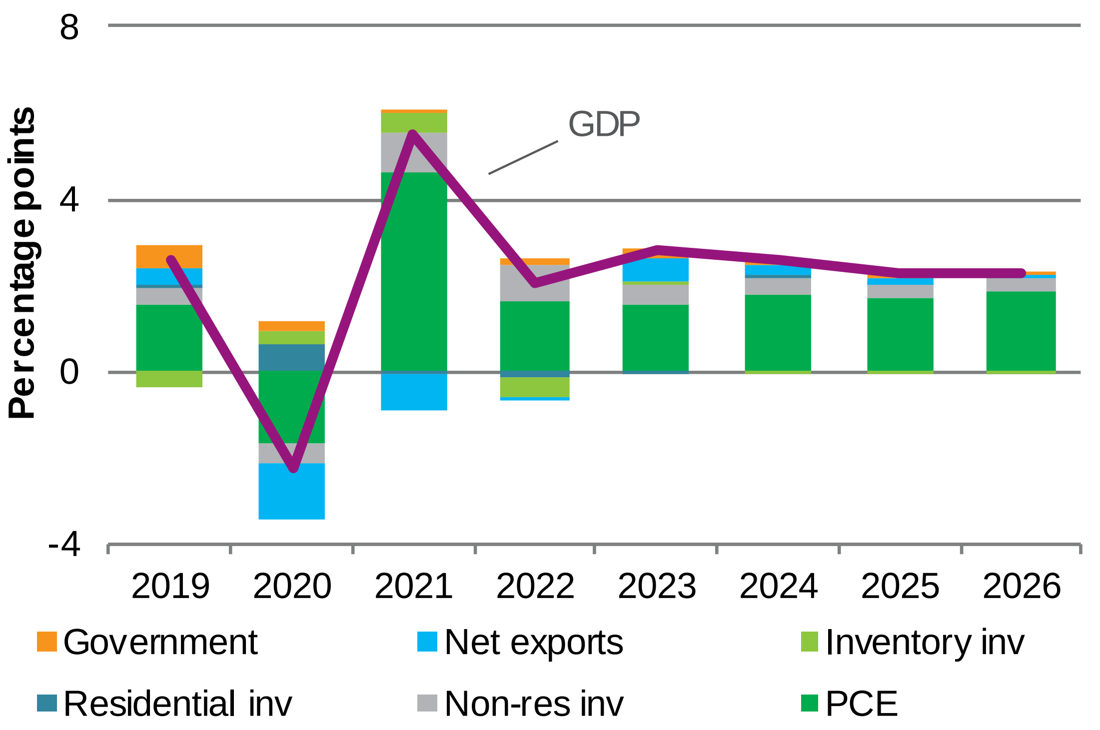
- Massive stimulus and release of pent-up demand provided strong boost to growth
  - But stimulus effects are waning – real disposable income is falling after Q1 2021
  - Pent-up demand in service consumption remains
- Virus variants, and others to follow, comprise an intermittent headwind to continued strong growth; cloud outlook
- Persistent elevated inflation further erodes real income, eliciting Fed and other CB responses
- Stagflation risk rises, especially if inflation expectations rise materially

Personal consumption expenditures (PCE) and business investment lead

Contributions to GDP growth (Q4/Q4)



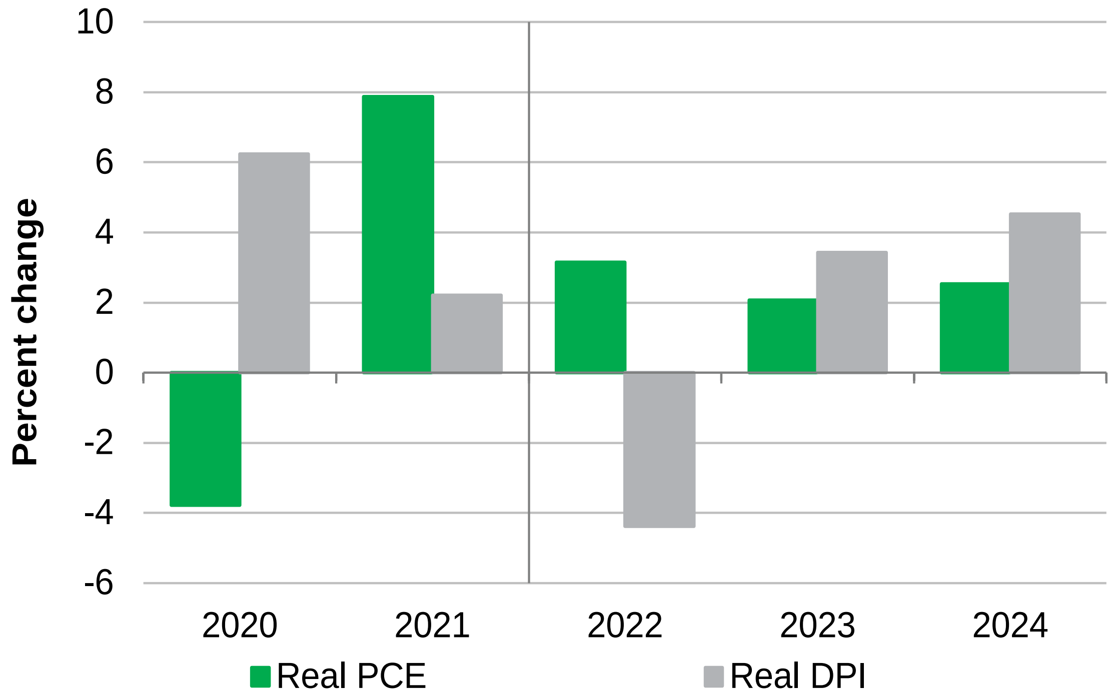
Source: IHS Markit, BEA

Consumer spending swings are the key driver, but induced effects in investment matter too

- Consumer spending is usually more stable during recessions than investment; not this time
- Stimulus, wealth, release of pent-up demand power PCE growth to 7.9% in 2021, 3.1% in 2022 (Y-o-Y)
- Business fixed investment aided by low rates and expectations that stimulus would cushion the blow = +7.4% in ’21; +5.8% in 2022
- Inventory building is a big part of the story ahead, adding 1¼ ppts to 21H2 and 22H1 growth
- Housing investment did “surprisingly” well in 2020, aided by historically low mortgage rates, and surprised to the upside in late 2021, early 2022

Fiscal stimulus drove PCE in 2020 and early 2021; wealth gains help later

Stimulus provides (waning) income windfall



Source: BEA (history), IHS Markit (forecast)

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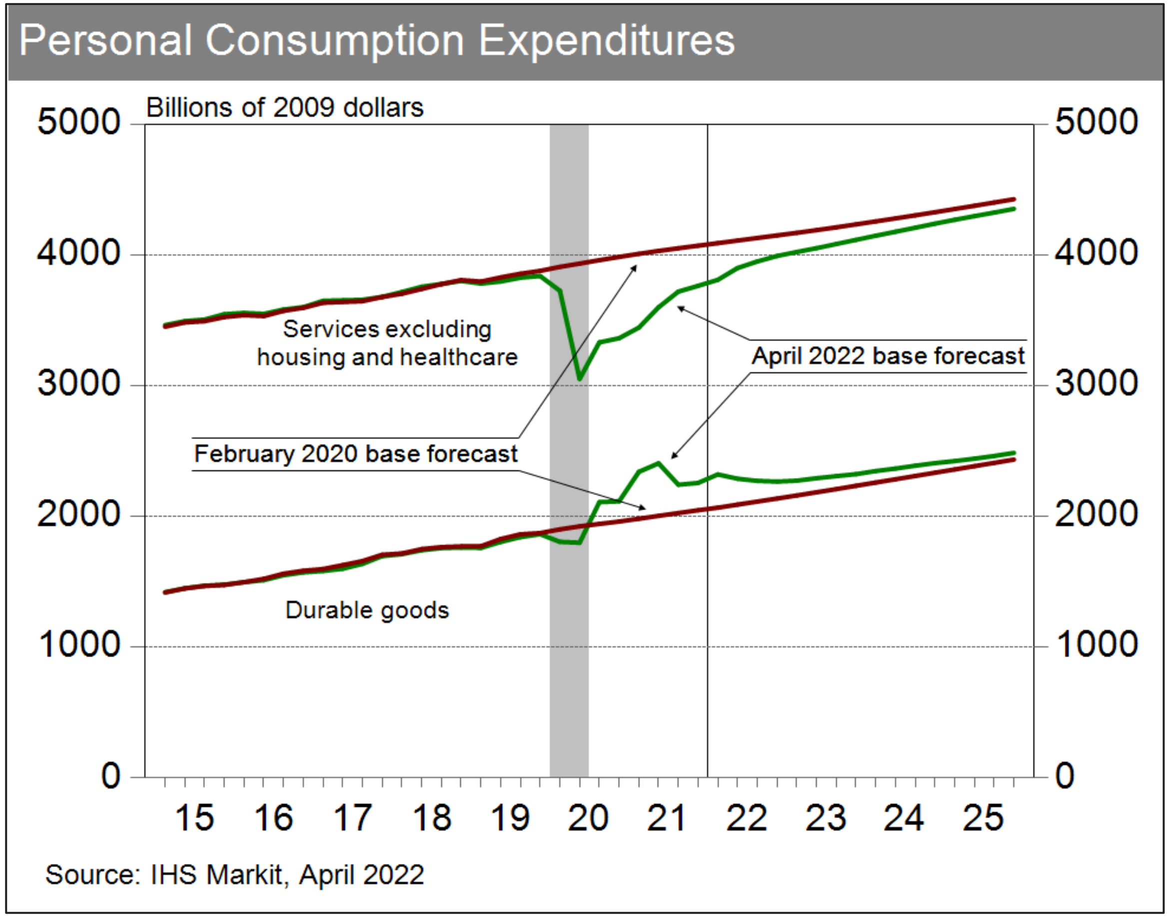
Key factors determining the rebound in PCE

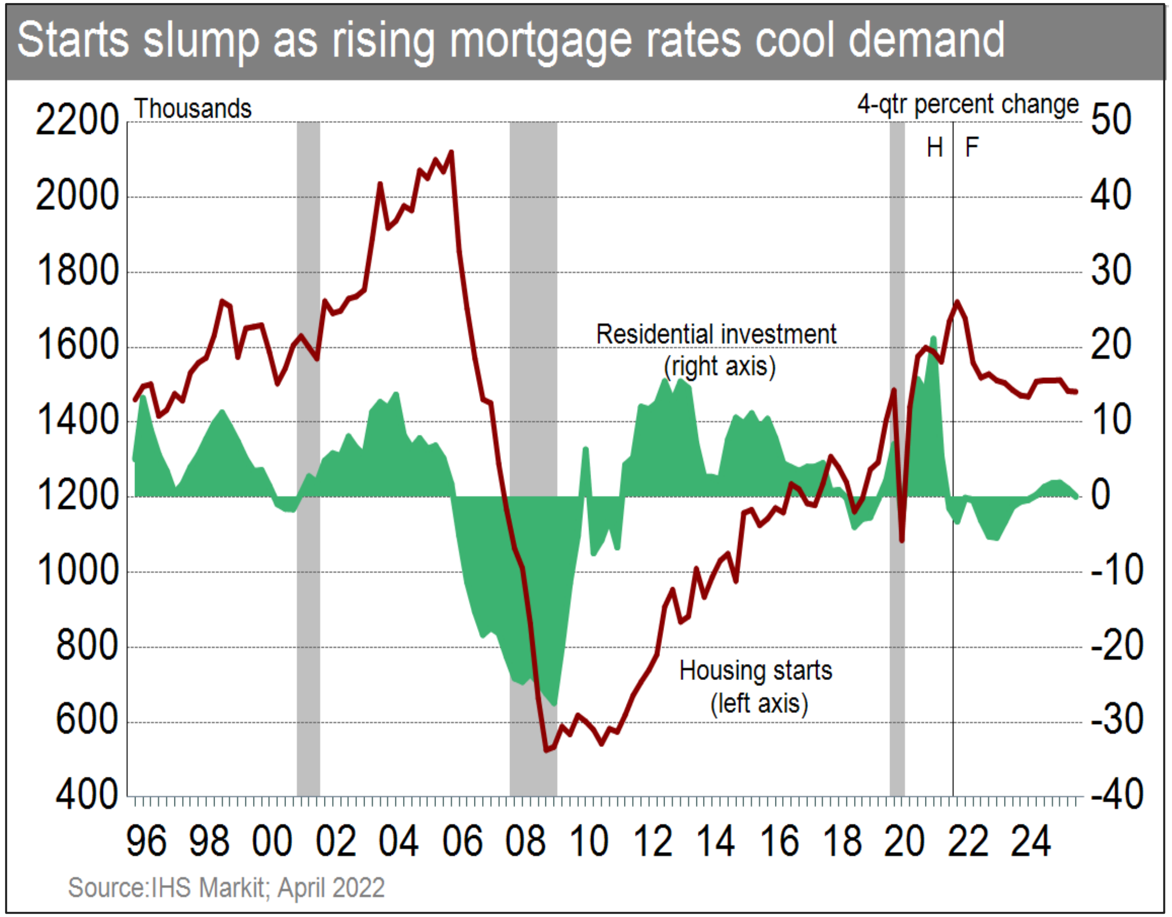
- Even assuming relatively low marginal propensities to consume out of the stimulus, consumer spending got a big boost in 2021
- PCE grew 11.4% in Q1, 12.0% in Q2, 2.2% in H2
- Y-o-Y PCE growth in 2021 at 7.9%
- Real disposable personal income declines outright after 2021Q1 thru 22Q2 and falls 4.4% in 2022 (Y-o-Y)
- Fiscal drag at work on back side of American Rescue Plan
- However, lagged adjustment to prior income gains and **extraordinary wealth gains** help sustain solid PCE growth

Rotation away from goods expenditures and towards services to continue



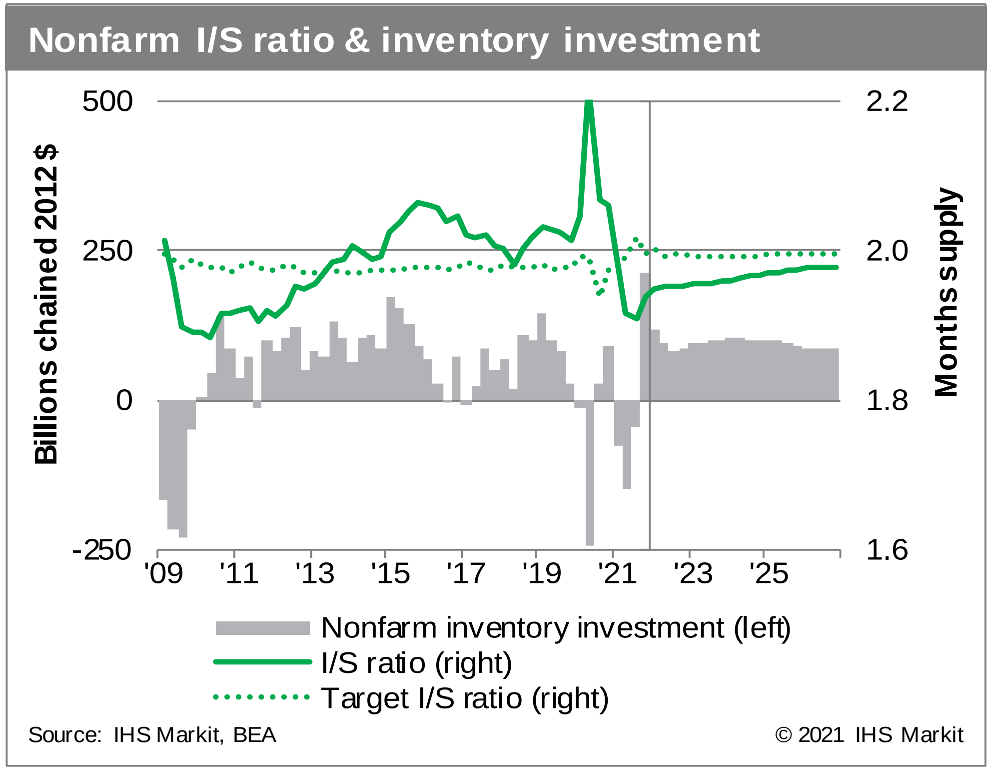
- Ongoing transition from goods toward services
- Yet on approach to new steady-state, levels are higher than prior trend due to increase in household sector wealth compared to prior path
- $2½ trillion (roughly) of excess saving
- Large increases in stock market and housing wealth fuel spending via the “wealth effect”
- Expect the “normal” relationship between spending, income and wealth to reassert itself over time
- Consumer vehicle purchases are back to “trend”

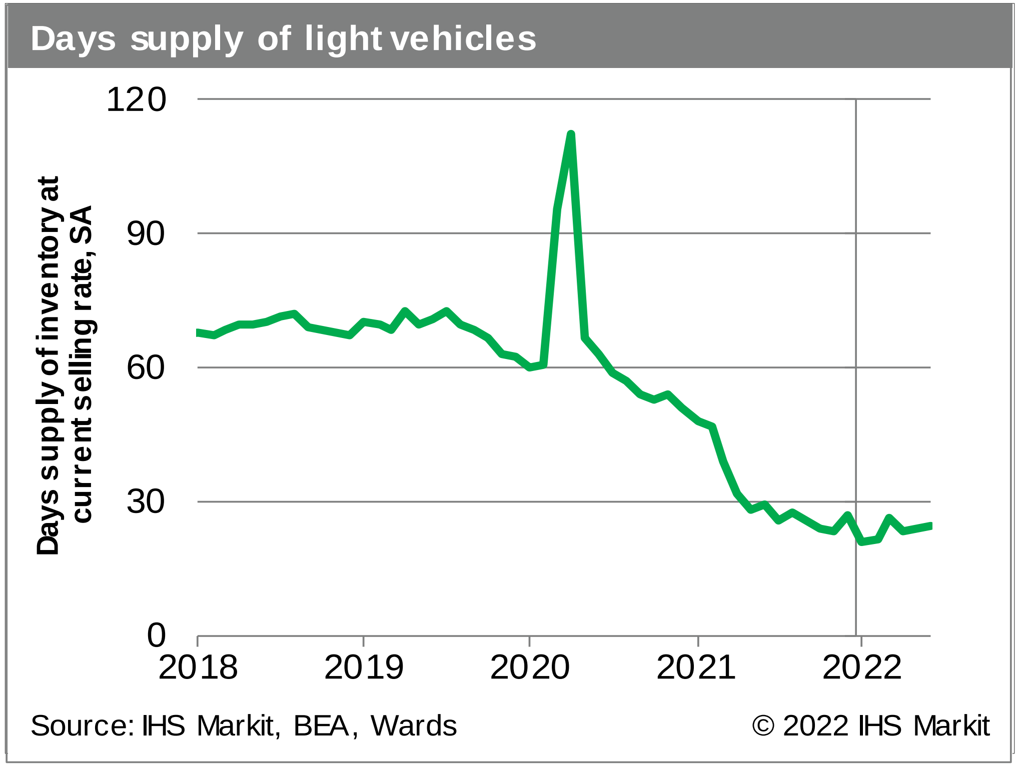
Housing's pandemic-boosted run is coming to an end



- Record low mortgage rates and stimulus cash helped to fuel the housing "boomlet"
- With mortgage rates now over 5%, expect demand to cool and construction to follow
- New and existing home sales are already declining (seasonally adjusted)
- Home price gains will cool quickly as well: 2021=18.5%, 2022=7.8%, 2023=3.0%
- Materials cost pressures expected to abate, helping to slow new home price surge

“Desired” inventory accumulation should be on the rise; is it constrained?





- Inventory sales ratio is near record low; supply chain constraints playing a role (semi conductors!)
- Demand rebounds in capex, housing construction and goods production drained inventories
- As supply bottlenecks resolve, inventory re-stocking will be a solid contributor to growth, but when?

Weak 22Q1 as Omicron and net export drop slow growth; expect a rebound

Key summary variables and differences from previous forecast - quarterly values

	21-Q3	21-Q4	22-Q1	22-Q2	22-Q3	22-Q4	23-Q1	23-Q2	23-Q3	23-Q4	24-Q1	24-Q2
Real Gross Domestic Product*	2.3	6.9	0.2	2.3	2.7	2.9	2.8	2.9	2.9	2.8	2.7	2.5
		-0.1	-0.8	-1.0	0.1	0.1	0.2	0.1	0.1	-0.1		-0.2
Dom. Final Sales Contribution	1.4	1.8	3.9	2.6	1.7	1.7	1.9	2.3	2.3	2.3	2.4	2.3
		-0.4	0.6	-0.6	0.2		-0.2	-0.3	-0.3	-0.5	-0.4	-0.5
Net Exports Contribution	-1.3	-0.2	-2.1	0.0	1.1	1.0	0.7	0.6	0.6	0.4	0.3	0.2
		-0.1	-0.9	-0.1	0.3	0.1	0.1	0.2	0.4	0.3	0.4	0.3
Inventory Invest. Contribution	2.2	5.3	-1.5	-0.3	-0.1	0.2	0.2	0.0	0.0	0.0	0.0	0.0
		0.4	-0.3	-0.3	-0.4	0.1	0.3	0.1				
Real PCE*	2.0	2.5	3.8	2.2	1.8	1.9	1.9	2.3	2.4	2.4	2.7	2.6
		-0.6	1.1	-0.4	0.6	-0.2	-0.5	-0.7	-0.6	-0.9	-0.6	-0.8
Unemployment Rate**	5.1	4.2	3.8	3.5	3.5	3.5	3.5	3.6	3.6	3.7	3.8	3.8
				-0.1	0.1	0.1		0.1		0.1	0.2	0.1
Core PCE Inflation*	4.6	5.0	5.6	4.6	3.9	3.3	2.7	2.5	2.3	2.2	2.1	2.2
			-0.3	0.5	0.3	0.3	0.1		-0.1			0.1
Federal Funds Rate**	0.09	0.08	0.13	0.69	1.28	1.79	2.29	2.80	3.10	3.11	3.11	3.06
			0.01	0.16	0.43	0.66	0.91	1.20	1.47	1.25	1.20	0.95
10-year T-Note Yield**	1.32	1.54	1.94	2.40	2.56	2.65	2.80	2.88	2.93	2.97	2.98	3.00
			0.12	0.55	0.53	0.48	0.42	0.38	0.34	0.30	0.23	0.18
S&P 500 (period end)***	0.2	10.6	-4.9	0.9	-3.1	0.4	-1.0	0.3	0.8	0.8	0.9	0.5
			4.7	-0.8	-2.8	-1.8	-2.9	-1.5	-0.7	-0.2	0.7	0.5

Notes: Positive differences from previous forecast shown in teal font, negative differences shown in red font.
* annualized % ch; ** average level; ***simple % change.
Source: IHS Markit

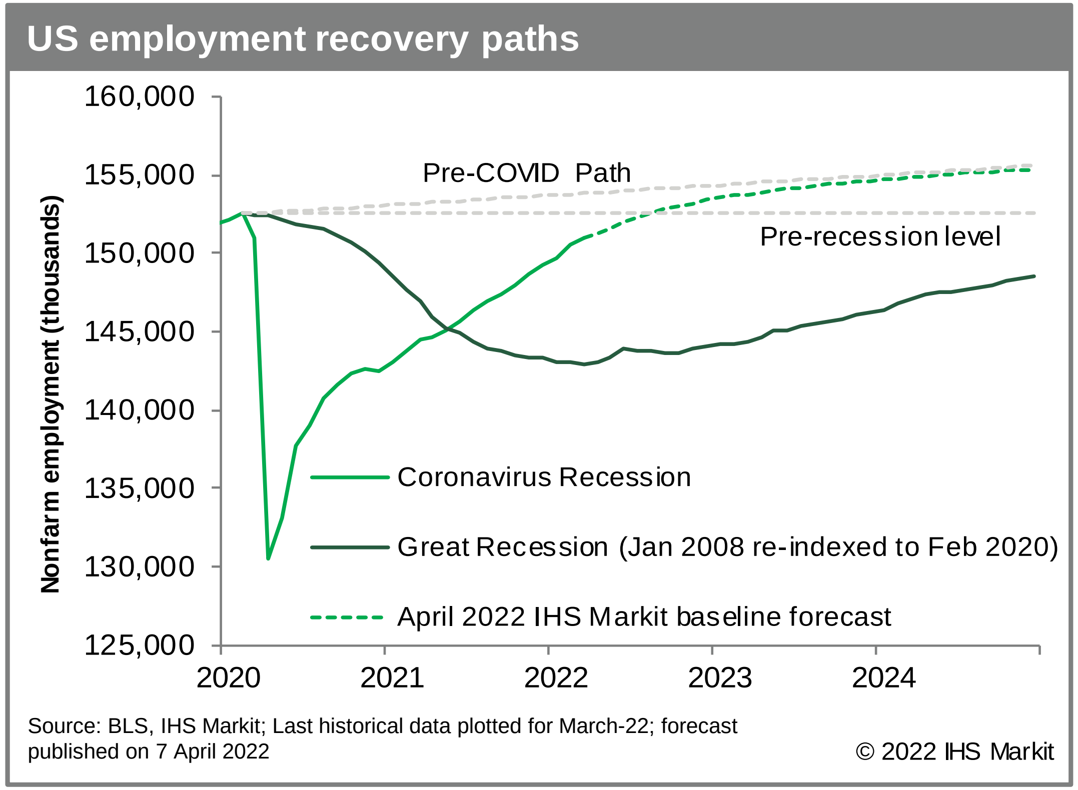
Solid, albeit slower growth expected in 2022 and beyond, but risks abound

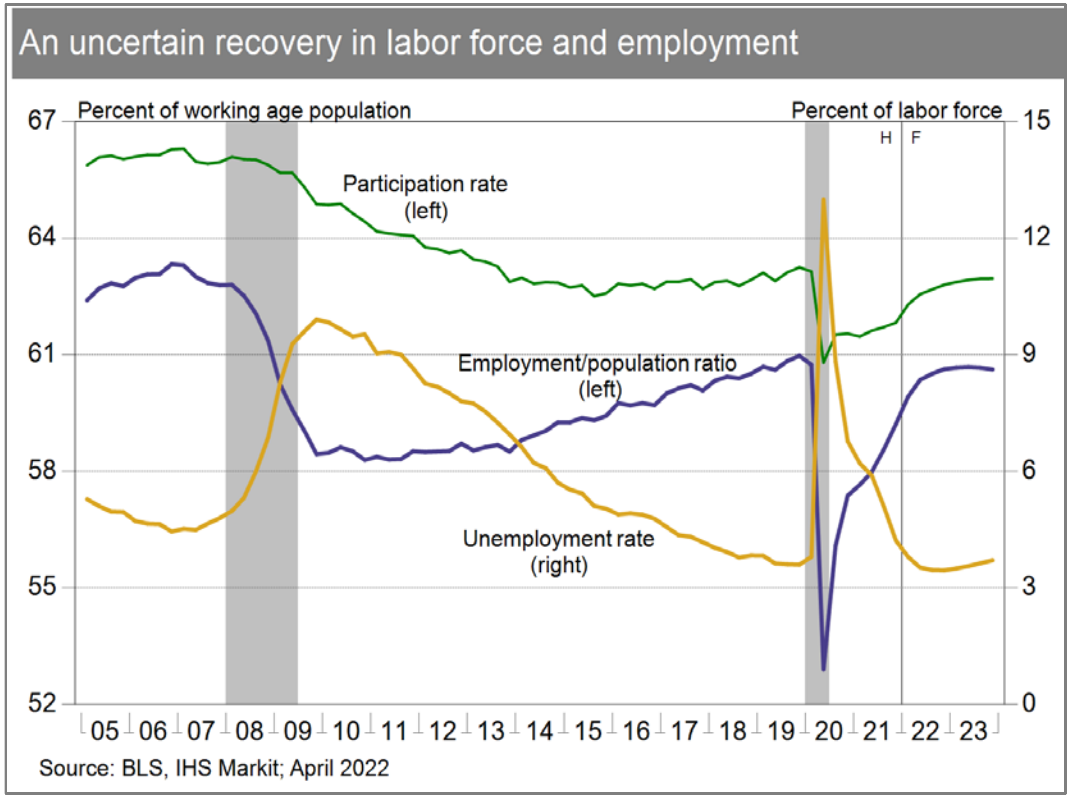
Key summary variables and differences from previous forecast - annual values

	% ch from prior year, or annual average						% ch from Q4 of prior year, or Q4 level					
	2021	2022	2023	2024	2025	2026	2021.4	2022.4	2023.4	2024.4	2025.4	2026.4
Real Gross Domestic Product*	5.7	3.0	2.8	2.7	2.4	2.3	5.5	2.0	2.8	2.6	2.3	2.3
		-0.3		-0.1	-0.4	-0.2	-0.1	-0.4		-0.2	-0.4	-0.1
Dom. Final Sales Contribution	6.7	2.8	2.0	2.3	2.2	2.2	5.5	2.5	2.2	2.4	2.1	2.3
	-0.1		-0.2	-0.5	-0.6	-0.3		0.1	-0.3	-0.5	-0.6	-0.2
Net Exports Contribution	-1.4	-0.6	0.7	0.3	0.2	0.1	-0.9	0.0	0.6	0.3	0.2	0.0
		-0.3	0.2	0.3	0.2	0.1	-0.1	-0.2	0.3	0.4	0.2	
Inventory Invest. Contribution	0.4	0.7	0.1	0.0	0.0	0.0	0.5	-0.4	0.1	0.0	0.0	0.0
	0.1	-0.1	0.1				0.1	-0.2	0.2			
Real PCE*	7.9	3.1	2.1	2.5	2.5	2.7	6.9	2.4	2.3	2.6	2.5	2.8
		0.1	-0.3	-0.8	-0.7	-0.3	-0.1	0.3	-0.6	-0.8	-0.6	-0.2
Unemployment Rate**	5.4	3.6	3.6	3.8	4.1	4.3	4.2	3.5	3.7	3.9	4.2	4.4
			0.1	0.1	0.4	0.6		0.1	0.1	0.2	0.5	0.7
Core PCE Inflation*	3.3	4.8	3.0	2.2	2.2	2.0	4.6	4.3	2.4	2.2	2.1	2.0
			0.2		-0.1	-0.2		0.2			-0.2	-0.3
Federal Funds Rate**	0.08	0.97	2.83	2.97	2.63	2.63	0.08	1.79	3.11	2.82	2.63	2.63
		0.30	1.20	0.90	0.20			0.66	1.25	0.64	0.20	
10-year T-Note Yield**	1.44	2.39	2.90	3.01	3.06	3.10	1.54	2.65	2.97	3.04	3.08	3.11
		0.40	0.40	0.20	0.10			0.48	0.30	0.12	0.06	0.04
S&P 500 (period end)***	35.5	3.6	-1.2	2.7	2.4	3.1	26.9	-6.7	0.9	2.3	2.8	3.2
		2.5	-7.5	0.6	1.2	0.6		-0.4	-5.4	2.0	0.8	0.5

Notes: Positive differences from previous forecast shown in teal font, negative differences shown in red font.
* % ch; ** annual average level or level at Q4; ***level at Q4 is last trading day of the year.
Source: IHS Markit

Where is the US labor market now?

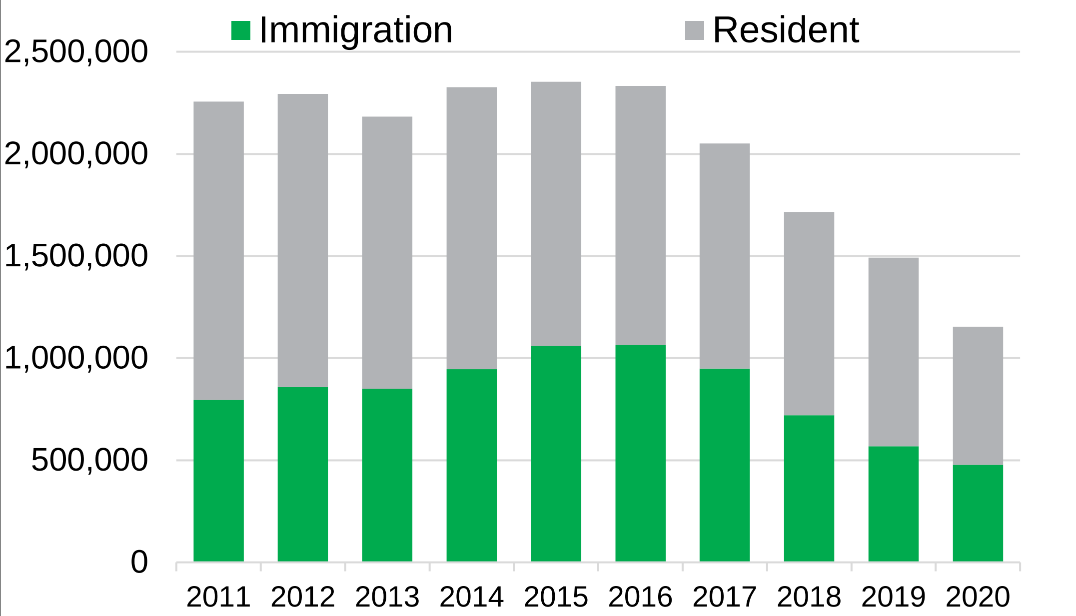




- Nonfarm payroll employment still 1.6 million below pre-pandemic peak
- Recovery in labor force participation has been slow, though shows signs of picking up more recently

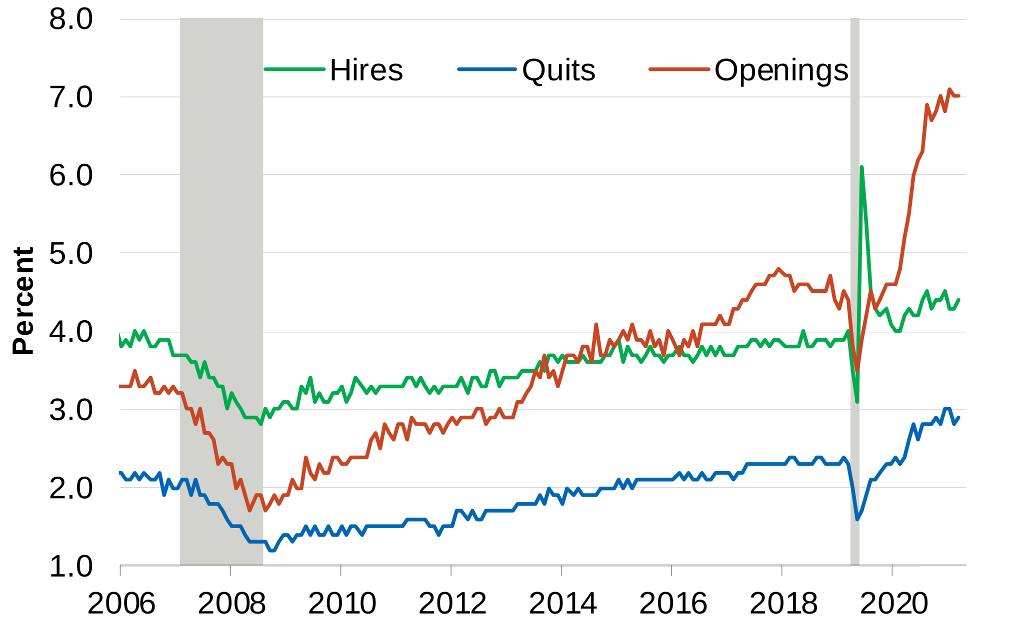
Slowing growth of working age population, slows flow into labor supply; high level of quits as workers move to take advantage of spot shortages

US population growth
Persons



Source: Census, IHS Markit © 2022 IHS

JOLTS: hires and quits



Source: BLS; Last data plotted for Feb-22 © 2022 IHS Markit

- Sharp slowing in immigration reduced labor force growth; 800k fewer multiple job holders
- Firms competing for scarce workers with wage hikes; re-sorting of the workforce leads to high quit rate

Given the (reduced) labor force - skill mismatches and location mismatches add to the labor shortage and put upward pressure on wage change

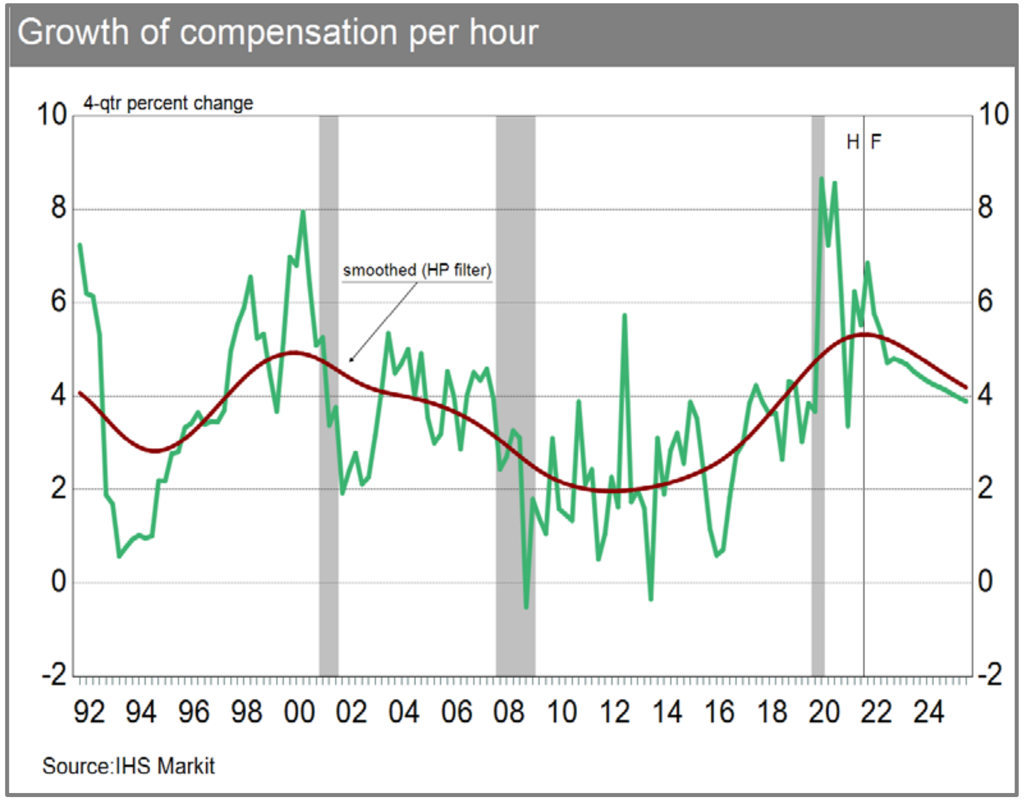
- **Skills mismatches**

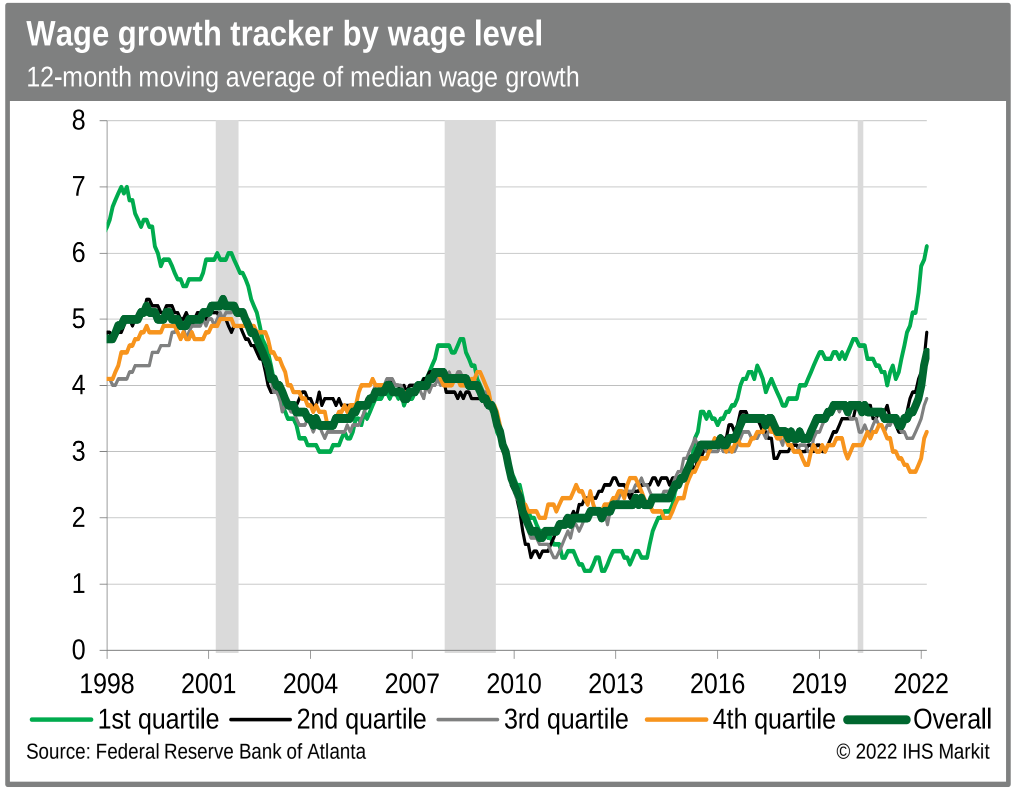
The pandemic led to a huge swing in consumer spending patterns—there is a boom in demand for manufacturing workers, however job losses have been heavily concentrated in leisure and hospitality industries creating a skills mismatch between available workers and employers

- **Location mismatches**

Job losses have been steeper in urban centers with a high concentration of leisure and hospitality industries, commercial construction, and tourism. Even in manufacturing skilled workers have been laid off in automotive and aerospace manufacturing (Midwest and Pacific Northwest) but demand for skilled workers is strongest in electronics clusters in New England and the Southwest

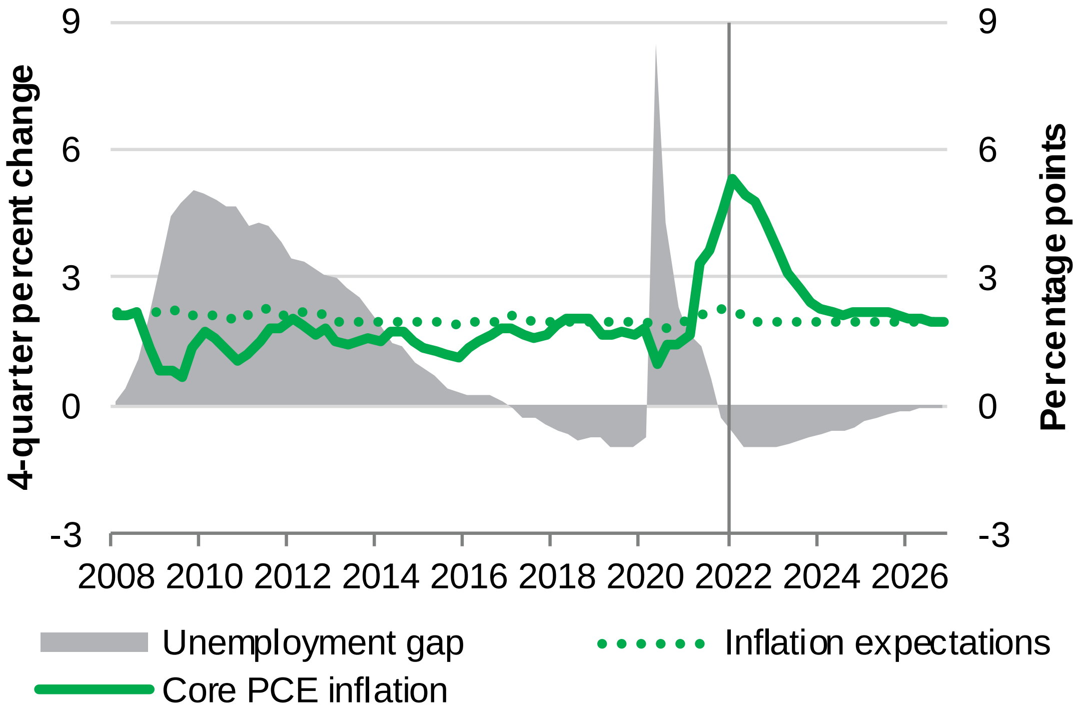
Labor costs still accelerating, but a turnaround is expected





After near-term surge, core PCE inflation to decline, reach “2%” in late 2023

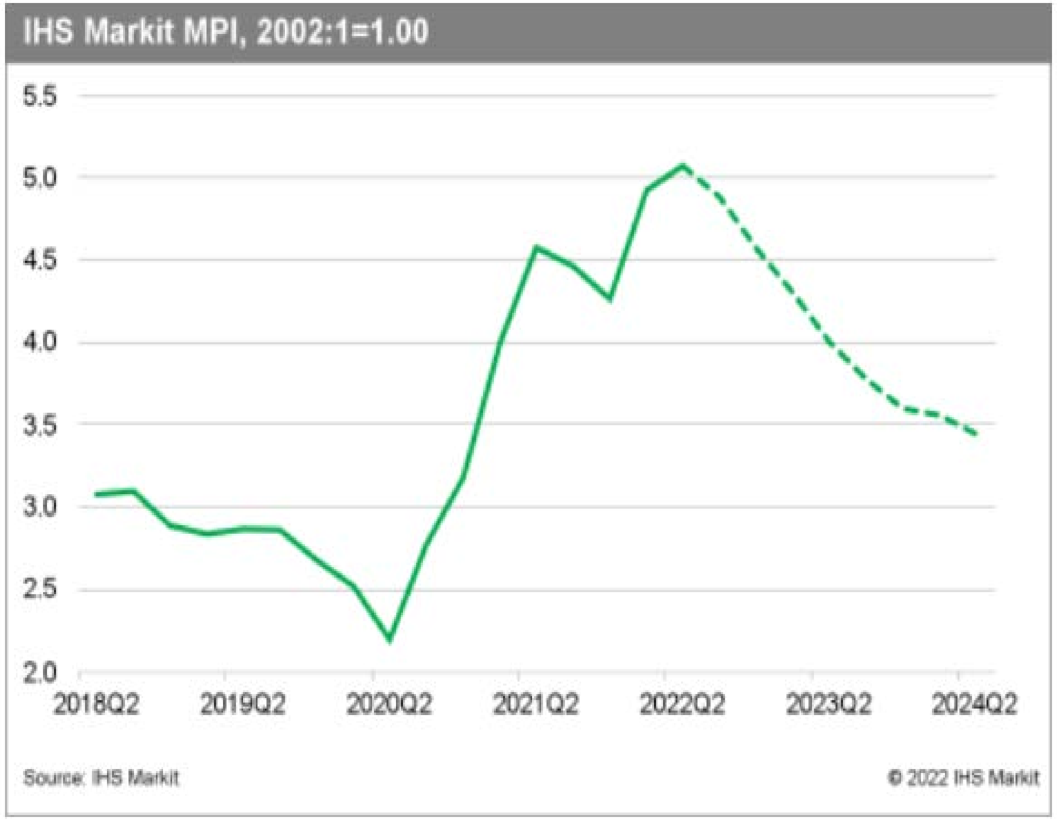
Core PCE inflation declines to about 2% after surge

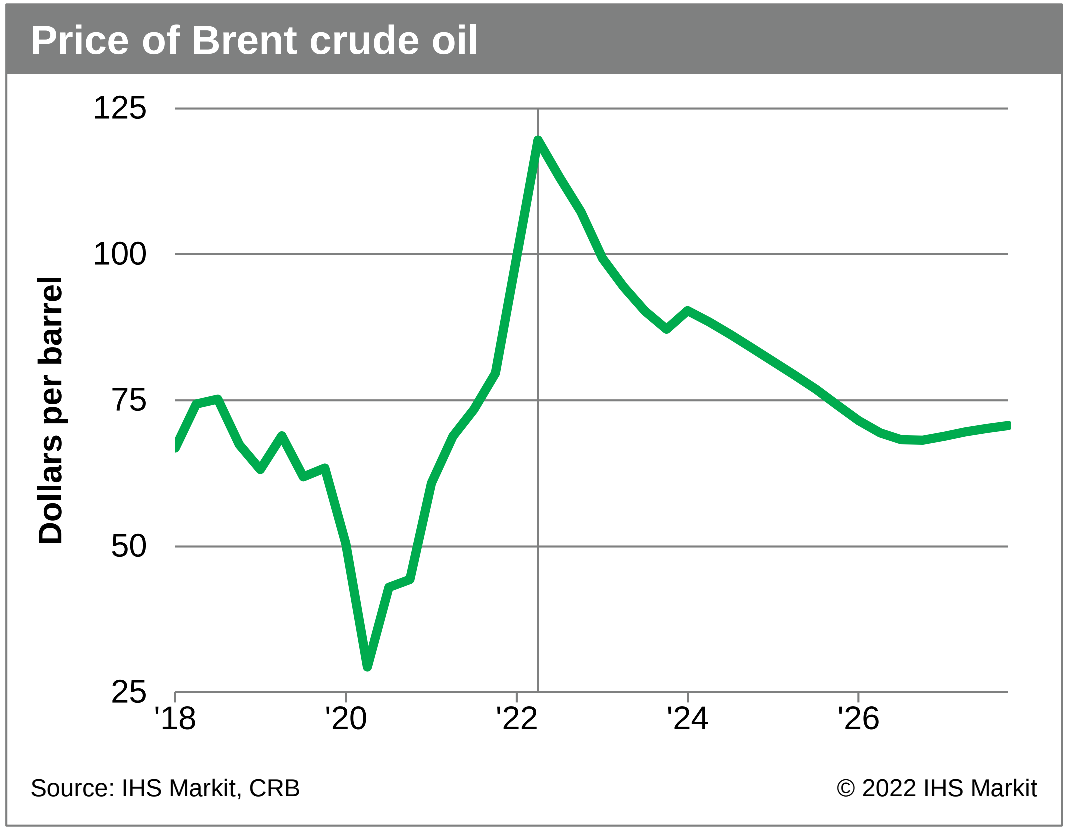


Source: IHS Markit, Philly Fed, BEA, BLS

- No global sustained excess of aggregate demand over aggregate supply, rather …
- Idiosyncratic, COVID-related, “one-time” price jumps due to mismatch of recovery in demand versus supply
- Long-term inflation expectations continue to be well anchored
- Supply-chain issues will resolve over next 12 months as demand for goods softens
- Labor market mismatches will resolve after relative wages have time to adjust … following “one-time” adjustments
- Inflation is driven now largely by “micro” issues, but inflation over the medium term is a “macro” issue

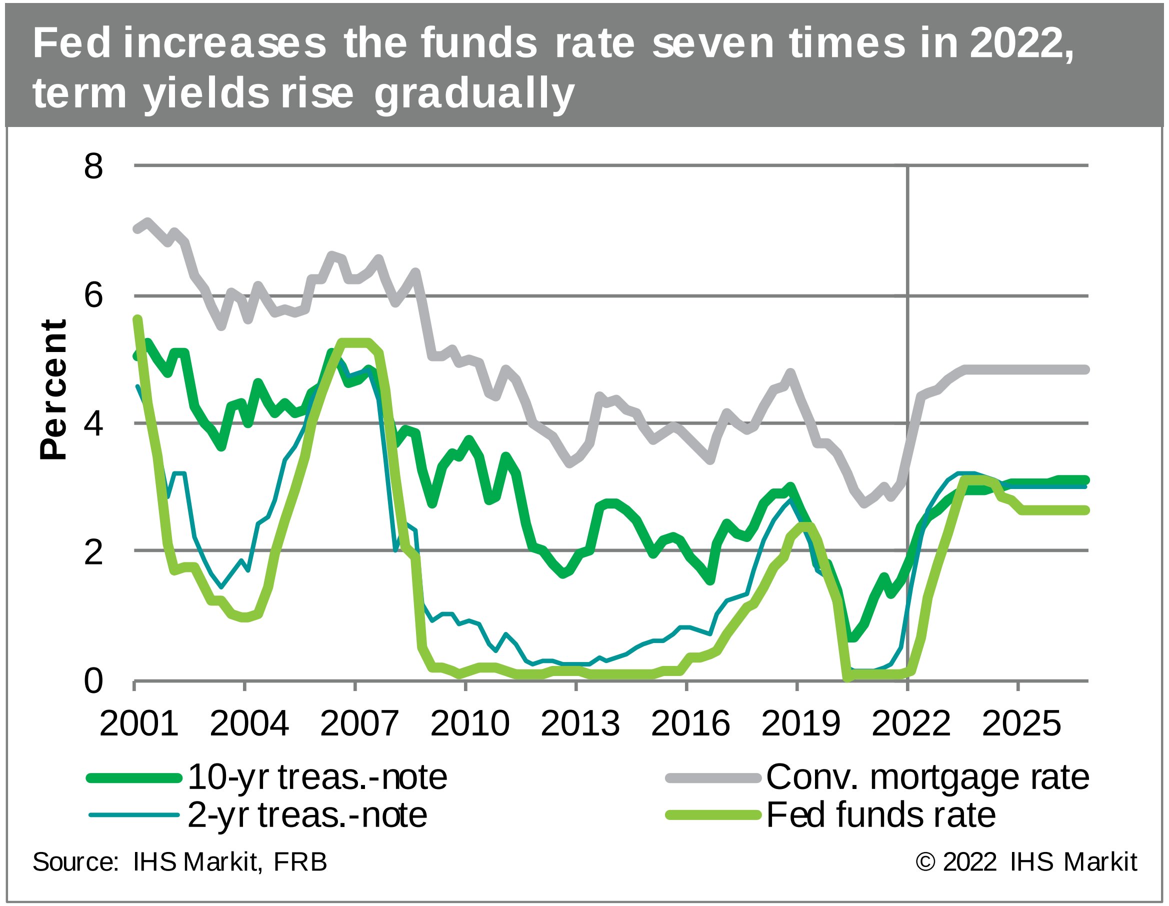
Commodity prices broadly have peaked; energy prices peaking soon





- Declining commodity prices will provide a downdraft helping to slow inflation
- Non-oil commodity prices may have fully passed through by now

An anxious Fed embarks on sharp tightening cycle

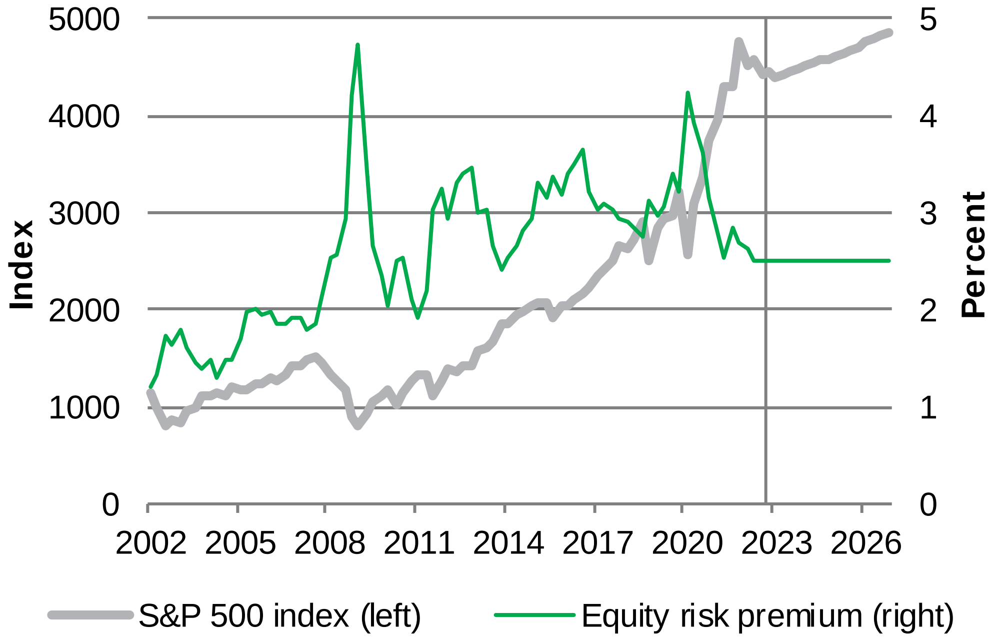


Fed getting anxious:

- Fed views inflation surge is "temporary," but not temporary enough!
- The 4-quarter change in core PCE prices slips to 4.3% in late 2022; then 2.4% in late 2023
- Unemployment rate declines to 3.5% in 22Q2
- Impatience with "transitory" inflation prompts accelerated taper
- Rate lift-off has begun; accelerates in May
- Term yields move higher

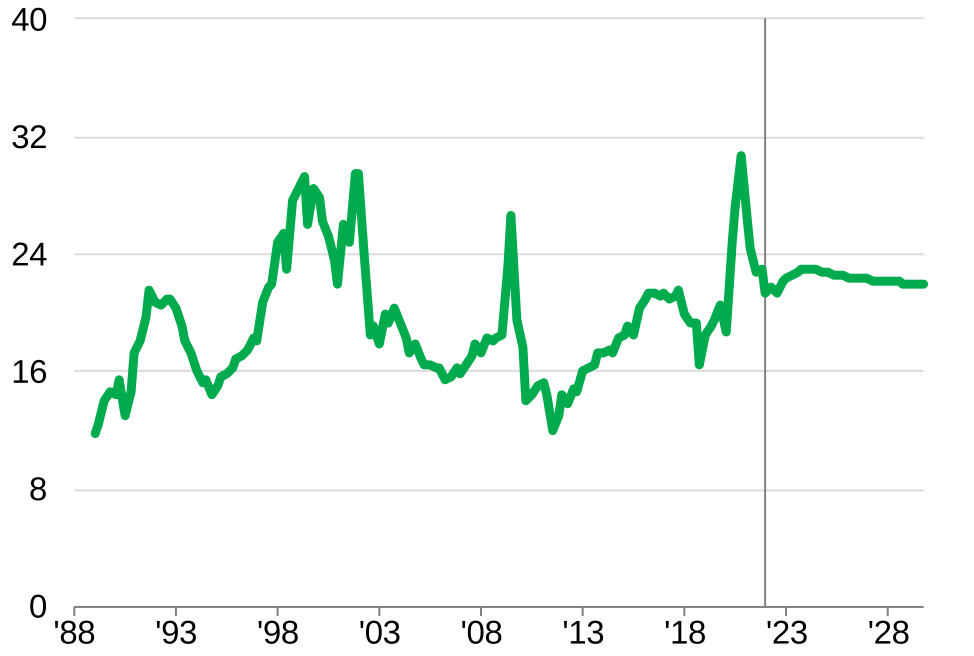
Equities rich, rates rising, nominal growth slowing … tough sledding ahead

Equities decline over 2022, rise gradually thereafter



Source: IHS Markit, S&P © 2022 IHS Markit

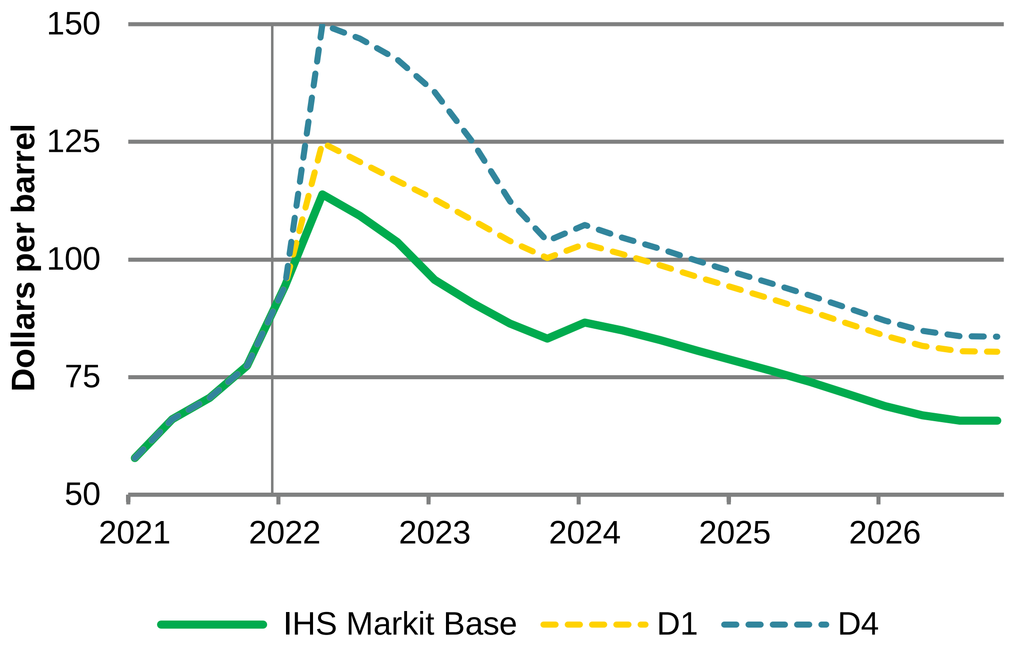
S&P 500 price-earnings ratio



Source: IHS Markit, S&P © 2022 IHS Markit

Downside (D1) and recession (D4) risks elevated, but not the base case

Price of West Texas Intermediate Crude Oil



Source: Commodity Research Bureau, IHS Markit

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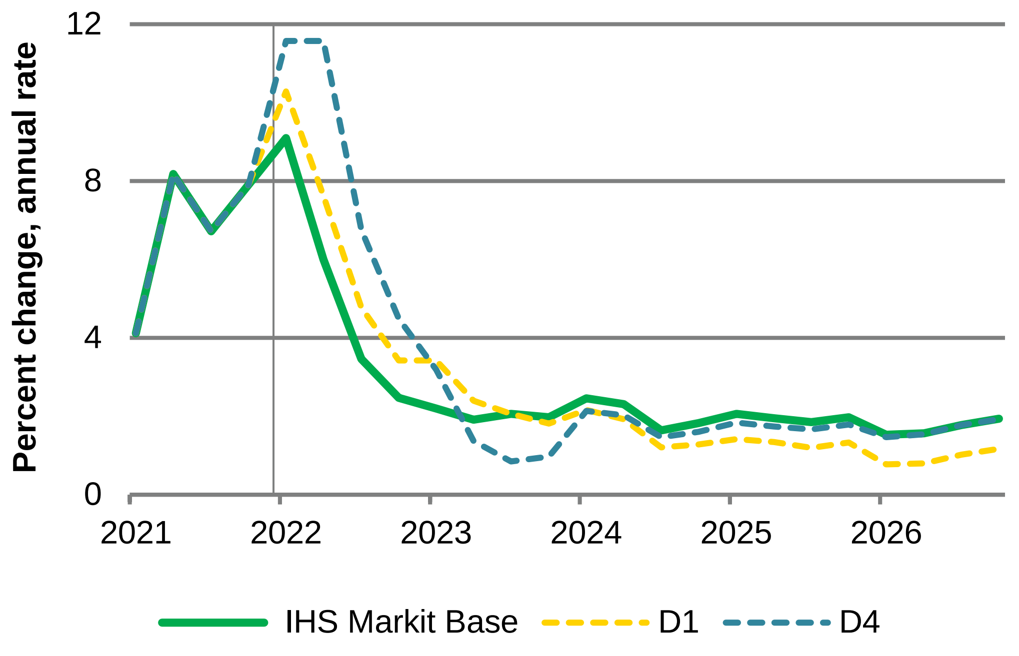
Consumer price index



Source: Bureau of Labor Statistics, IHS Markit

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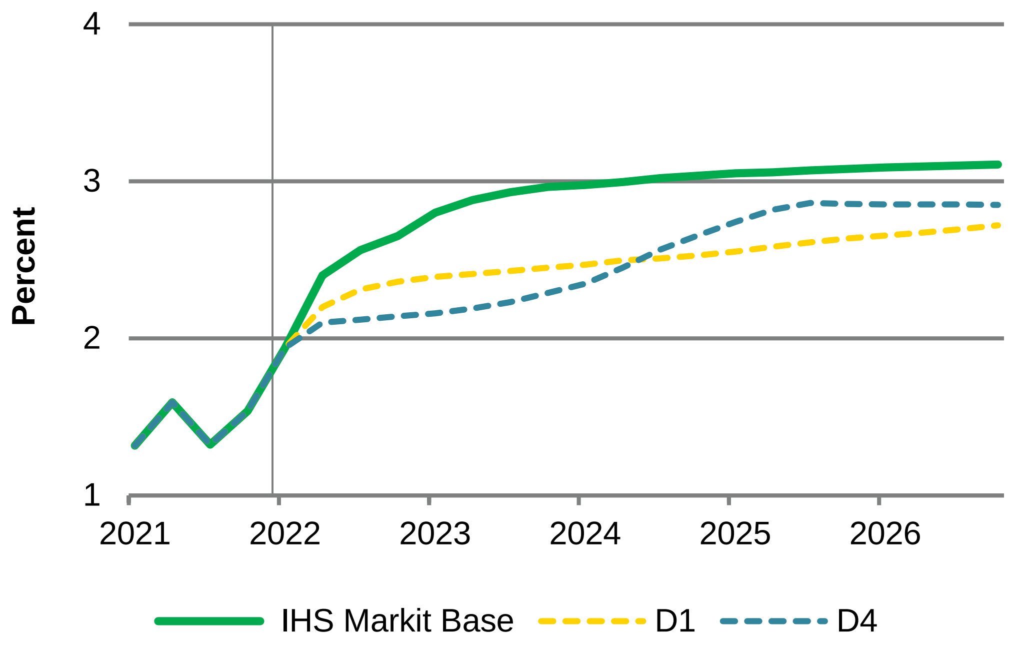
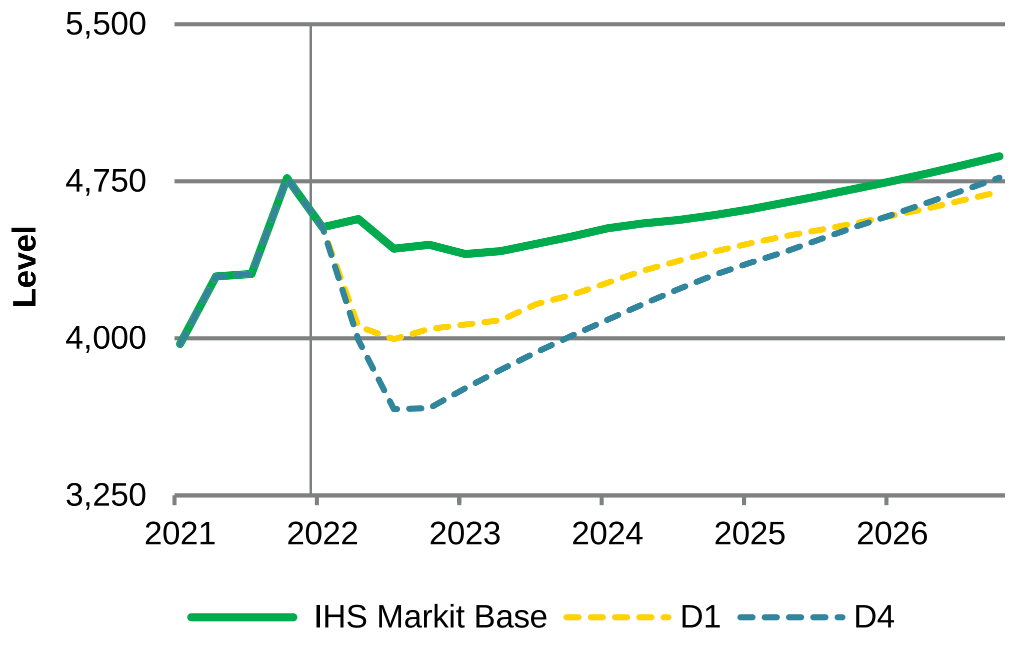
Downside (D1) and recession (D4) risks elevated, but not the base case

10-year treasury note yield



Source: Federal Reserve Board, IHS Markit

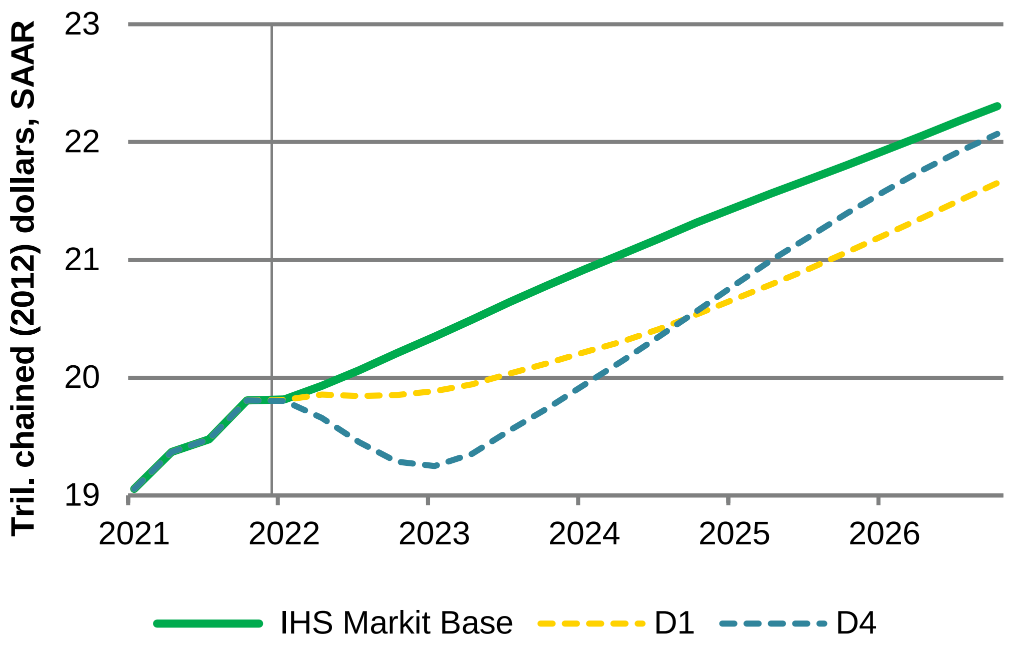
Equities index: S&P 500



Source: Standard & Poor's, IHS Markit

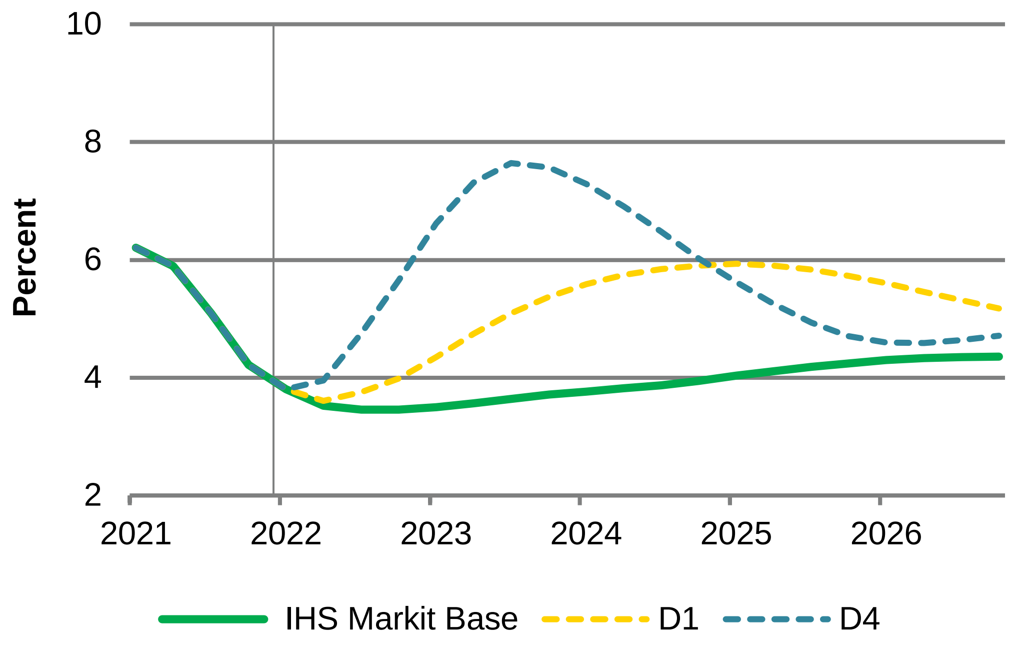
Downside (D1) and recession (D4) risks elevated, but not the base case

Real gross domestic product



Source: Bureau of Economic Analysis, IHS Markit

Unemployment rate



Source: Bureau of Labor Statistics, IHS Markit

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