Nationwide Economics

Weekly Economic Review & Outlook

January 30, 2023

GDP details show waning momentum for 2023

Headline real GDP growth remained solid in the fourth quarter underpinning a rebound in the second half of 2022 that more than recovered the decline recorded in the first half of the year. Unfortunately, the underlying details of the GDP report were less impressive, showing that consumer and business spending was slowing heading into the new year. In positive news, the PCE price data for December were encouraging, but inflation remains far above the Fed's 2 percent target.

GDP advanced at a solid pace in the fourth quarter, but details were soft

Real GDP grew at an annualized pace of 2.9 percent in the fourth quarter, after a similarly sturdy 3.2 percent annualized advance in the third quarter. However, the underlying mix of the growth was much less upbeat and bodes poorly for growth in 2023. Roughly half of the increase in GDP growth (1.5 percentage points) stemmed from a jump in inventories as businesses experienced lower sales. Moreover, the unwanted accumulation in inventories will weigh on future production as companies work to reduce their inventory levels. Final sales to private domestic purchasers (referred to as core GDP) grew by a paltry 0.2 percent — its weakest non-recessionary reading since 2009.

Consumer spending rose a softer than forecast 2.1 percent in Q4, as real consumer spending declined in November and December. The pullback in consumer outlays was led by sharp declines in consumers' purchases of goods. Demand for services held up better, but even that continued to show a distinct downward trend and in December spending on services, adjusted for inflation, was flat compared to November's level. Most importantly, the languid consumer spending at the end of 2022 imparts negative spending momentum heading into this year - an ominous sign for growth in early 2023 especially since the labor market was still strong. Looking ahead, businesses are likely to make reductions in their headcounts, which will weigh more significantly on personal income and in turn personal consumption expenditures. This should lead to a recessionary downturn by mid-year.

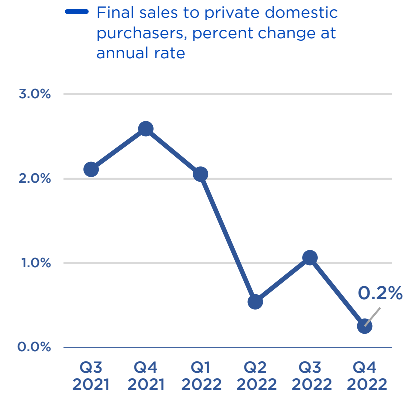
Residential investment continued to be a significant drag on growth, but there was also a significant slowing in business fixed investment. Investment in buildings remained stagnant after significant declines over the last three years—likely due to the surge in remote working. The pullback in equipment spending could be more telling, though, as businesses seem more reluctant to spend in preparation for an economic downturn in 2023.

For the full year 2022, economic growth moderated to 2.1 percent following the unsustainably strong 5.7 percent snap back in activity in 2021, which followed the pandemic-induced contraction in 2020.

Consumer inflation continues to recede

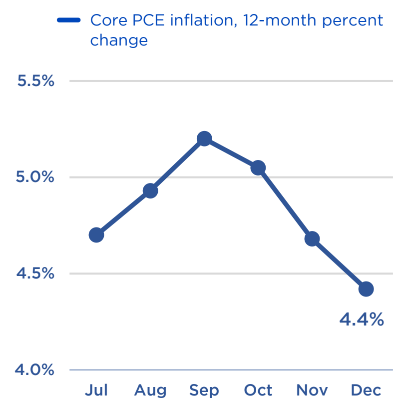
The PCE price index showed that consumer inflation slowed to a 15-month low of 5.0 percent in December while the PCE core rate slowed to 4.4 percent. Despite the improvement, housing inflation continues to climb, reaching its highest level in over 40 years. Inflation for core services ex-housing—a measure Fed Chair Powell has highlighted recently—and core goods both decelerated, news that should be encouraging to the FOMC during its meeting this week. Still, with the 12-month trend rates for key inflation measures remaining elevated we expect the Fed's tightening cycle to continue with a smaller 25 basis point increase at the conclusion of this week's FOMC policy meeting—lifting the range for the fed funds rate to 4.50-4.75 percent.

Core GDP continues to trend down



Growth in core GDP fell in the fourth quarter to a level typically only seen in or around recessions.

Core inflation falls for a third straight month



Core PCE fell in December to its lowest level in more than a year, led by a sharp decline in core goods prices.

Source: Bureau of Economic Analysis

Contributors: Daniel Vielhaber, Economist | Ashleigh Leonard, Economic Specialist

The Week Ahead

Here's what we are watching this week. Subscribe to [Daily Insight] for updates through the week.

JOLTS Job Openings

Feb 1

Slight decline for job openings but the labor market remains tight

In November, the JOLTS report showed little change in the large number of job openings, with a decline of just 54,000 to 10.458 million. The job openings-to-unemployed ratio, a key metric of labor tightness, increased to 1.74 in November from 1.73, indicating that demand for labor remained very strong. The number of job openings should continue to gradually decline in December, showing some signs of loosening in some sectors including finance and insurance which recorded a decrease of 75,000 in openings in November. The quits rate, which increased to 2.7 percent in November, should remain elevated as workers switch jobs for higher wages.

ISM Manufacturing & ISM Services

Feb 1 & 3

ISM indices likely to stay in contractionary territory

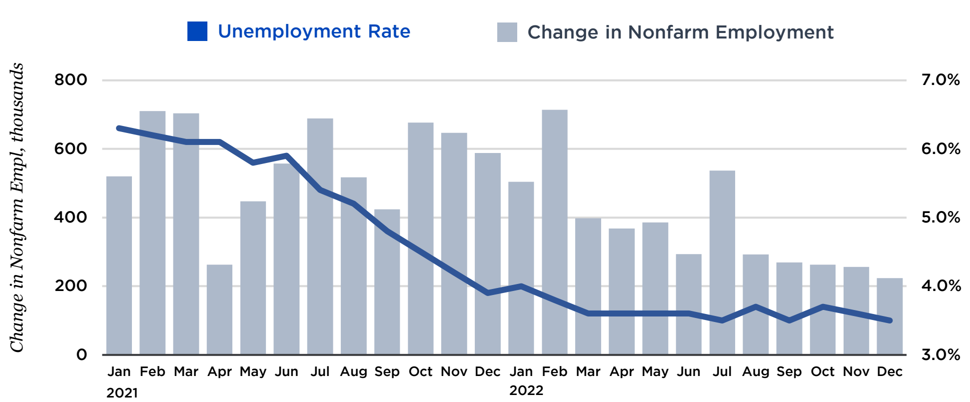
New orders, a leading indicator for demand and production, dropped steeply in December for both services and manufacturing, reflecting a sharp retrenchment in customer demand. Moreover, the drop supports signs of an unwanted buildup in inventories for firms. The ISM services index plunged in December to join manufacturing in contraction territory. Both indexes are expected to remain below the 50-mark in January as readings of widespread weakness build across the business sector. Prices paid, which have weakened sharply amid supply chain improvements, should still show broadly lower costs. The top six manufacturing industries did not report price increases in December signaling that cooler input costs are continuing to ease price pressures for consumer goods inflation.

Unemployment Rate, Payroll Growth

Feb 3

Solid hiring expected again in January with strong wage growth

The labor market continues to be strong, though we forecast a moderation in net new jobs created in January to 175,000 following a 223,000 advance in December. Despite the low level of claims and employers generally holding on to workers, companies are being more cautious to hire new employees given slowing economic activity. Gains in hiring should continue to be led by the service sector including education and health services and leisure and hospitality, the latter of which is still recovering from its pandemic-related fall. The unemployment rate should rise just 0.1 percentage point to 3.6 percent, signaling the labor market remains incredibly tight. Average hourly earnings likely increased another 0.3 percent in January, placing the year-over-year rate at 4.3 percent, down from 4.6 percent in December. This is a welcomed development, but wage growth still runs faster than its pre-pandemic pace of around 3.0 percent.



Sources: Bureau of Labor Statistics/Haver

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Additional Economic Indicators

Previous Week's Indicators

	Period	Actual	Previous
GDP Annualized QoQ	4Q 1st	2.9%	3.2%
Advance Goods Trade Balance	December	-$90.3b	-$83.3b
GDP Price Index	4Q 1st	3.5%	4.4%
Core PCE QoQ	4Q 1st	3.9%	4.7%
Durable Goods Orders	December	5.6%	-2.1%
Initial Jobless Claims	Week ending January 21	186k	190k
New Home Sales	December	616k	640k
New Home Sales MoM	December	2.3%	5.8%
Personal Income	December	0.2%	0.3%
Consumer Spending	December	-0.2%	-0.1%
Real Consumer Spending	December	-0.3%	-0.2%
PCE Deflator MoM	December	0.1%	0.1%
PCE Core Deflator MoM	December	0.3%	0.2%
U. of Mich. Sentiment	January	64.9	64.6

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Employment Cost Index	Tuesday	4Q	1.2%	1.2%
Conf. Board Consumer Confidence	Tuesday	January	107	108.3
Construction Spending MoM	Wednesday	December	-0.2%	0.2%
ISM Manufacturing	Wednesday	January	47.5	48.4
FOMC Rate Decision (Lower Bound)	Wednesday	Week ending February 1	4.5%	4.25%
Wards Total Vehicle Sales	Wednesday	January	15.1m	13.31m
Factory Orders	Thursday	December	2.0%	-1.80%
Change in Nonfarm Payrolls	Friday	January	175k	223k
Unemployment Rate	Friday	January	3.6%	3.5%
Average Hourly Earnings MoM	Friday	January	0.3%	0.3%
Average Weekly Hours All Employees	Friday	January	34.3	34.3
ISM Services Index	Friday	January	49.5	49.6

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