Nationwide Economics

Monthly Economic Dashboard

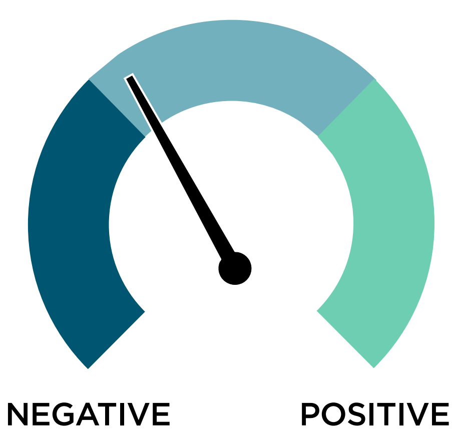
SEPTEMBER 2022

Hot inflation and rapid Fed tightening move the economy closer to a recession

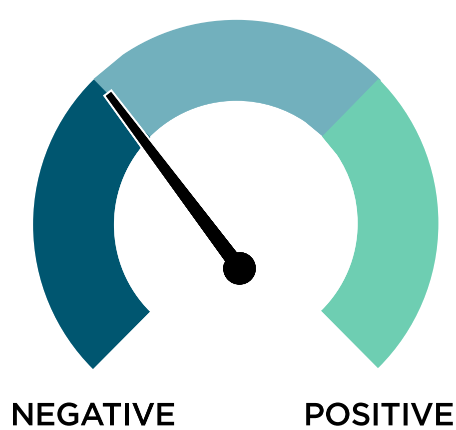
The core CPI upside surprise for August highlighted the continued cost pressures across the economy as well as the long road back to a normal price environment. The Fed pushed through another 75 basis point rate hike in September while signaling further aggressive tightening ahead. But the damage may already be done as cuts in consumer activity and business spending in response to higher rates are expected to weaken growth sharply over 2023.

- Job gains slowed for August, but employers continue to demand more workers than enter the labor force — driving wages higher across many industries.
- After adjusting for higher prices, retail spending stagnated over the summer as the weight of rapid inflation for essential items and higher interest rates slow activity.
- The Fed announced a third consecutive 75 basis point rate increase in September as inflation trends remain hot. The pace of tightening is likely to slow by year-end, but the economy is still set up to slow further (and maybe contract) in 2023 as borrowing costs climb.
- Pessimism returned to Wall Street as building recession concerns caused the S&P 500 index to reverse much of its recent rally to again post bear market declines. The yield curve inversion deepened over the month even as long-term interest climbed to year-highs.

Current Scorecard



Future Scorecard



Full scorecards ▶

Nationwide Economics — Monthly Economic Dashboard

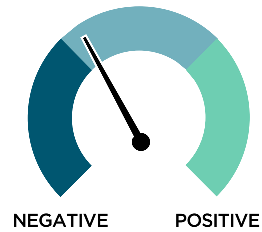
Current Scorecard – September 2022

Data through September 21, 2022

OVERALL

3-MONTH TREND

The hot core inflation print for August dimmed hopes for a rapid cooling of inflation while feeding concerns that further Fed tightening will lead to a recession. The labor market remains a source of economic strength with strong hiring demand and rising wages supporting household spending. But homes sales have dropped off sharply while poor sentiment readings from consumers and small businesses (albeit up this past month) suggest that overall activity is weakening in response to higher costs and interest rates. The stock market rally faltered over the past month as growth prospects slumped in the face of another steep rate hike from the Fed.



EMPLOYMENT

3-MONTH TREND

Nonfarm payroll growth slowed in August but the trend in hiring remains strong in most sectors. The unemployment rate increased for the first time since January, driven by a positive surge in the size of the labor force. The ratio of job openings to unemployed workers remains nearly 2-to-1 while jobless claims have leveled off — signaling little let up in demand by employers for labor.

NEGATIVE POSITIVE

	Current	Previous	Year ago
Employment growth – Aug	315,000	526,000	517,000
Unemployment rate – Aug	3.7%	3.5%	5.2%

FINANCIAL

3-MONTH TREND

The FOMC announced a third consecutive 75 basis point rate hike in September as inflation was hotter-than-expected. With Fed tightening raising recession concerns, the equity market rally fizzled in late August and September — retracing much of the gains from the prior two months. Long-term interest rates rose to their highs for 2022, but Treasury yields remained inverted over much of the curve.

NEGATIVE POSITIVE

	Current	Previous	Year ago
Yield spread – Sept	-0.52 pp	-0.38 pp	1.29 pp
BAA Credit spread – Sept	2.15 pp	2.26 pp	1.82 pp
CBOE market volatility – Sept	25.97	19.94	21.46
S&P 500 stock index – Sept	3,953	4,278	4,402

CONSUMER

3-MONTH TREND

Retail spending rebounded in August, boosted by higher prices for autos and many other goods. The owner-occupied housing market continues to slump with demand falling off sharply in response to rising mortgage rates. Consumer sentiment, although still low historically, has recovered from its June low, likely in response to the reduced inflation expectations.

NEGATIVE POSITIVE

	Current	Previous	Year ago
Retail sales – Aug	0.3%	-0.4%	0.8%
Light vehicles sales – Aug	13.2 M	13.3 M	13.1 M
Total home sales – July	5.32 M	5.70 M	6.76 M
Consumer sentiment – Sept	59.5	58.2	72.8

BUSINESS

3-MONTH TREND

The ISM business surveys showed further solid expansion in August as demand remained strong while supply conditions are healing. But the surveys from S&P Global have weakened sharply in recent months, suggesting a mixed overall business environment. Small business optimism has improved from recent lows, but business owners continue to have a negative outlook for future sales and growth.

NEGATIVE POSITIVE

	Current	Previous	Year ago
ISM Manufacturing – Aug	52.8	52.8	59.7
ISM Services – Aug	56.9	56.7	62.2
NFIB small business optimism – Aug	91.8	89.9	100.1

INFLATION

3-MONTH TREND

The core CPI jumped again in August as housing and service costs continue to build despite the Fed's rate tightening — pushing up the 12-month core inflation rate to 6.3 percent. This offset the optimism generated by another weak overall CPI reading with gasoline prices down for a second consecutive month, although costs for food at home rose sharply again.

LOWER HIGHER

	Current	Previous	Year ago
Consumer price index (CPI) – Aug	0.1%	0.0%	0.3%
Core CPI – Aug	0.6%	0.3%	0.2%

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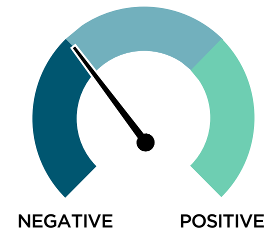
Future Scorecard – September 2022

Nationwide

OVERALL

While a recession next year remains far from certain, typical leading indicators are inching closer to recession signals. The 1- and 2-year Treasury note yields have been inverted with longer-term rates since July, historically the most reliable alarm bells for a downturn. Moreover, the 12-month change in the index of leading economic indicators turned negative in August as activity weakens broadly. This does not mean that the economy is imminently at risk of contracting. But it does suggest that the conditions for a recession are building and could culminate in a modest downturn in the second half of 2023 or early 2024.



THE ECONOMY

Real GDP growth is projected to be positive, but modest, in the second half of 2022. But the economy should slow sharply over 2023 as the full impact of the Fed's rate increases hit consumer and business activity — focused on building recession risks for the second half of the year. If a downturn does occur, we would not expect it to be severe, as imbalances aren't widespread.

	2021	2022F	2023F	2024F
Real GDP growth	5.7%	1.8%	0.7%	1.2%

CONSUMER

Home sales should slow further in response to higher mortgage rates and lack of housing supply — but positive demographics and further job gains should keep sales from falling too sharply. Auto sales should get a boost in 2023 as supply constraints in the production of light vehicles are finally easing (while also cooling prices for new and used cars), but sales will be capped by below-trend economic growth.

	2021	2022F	2023F	2024F
Total home sales	6.89 M	5.75 M	5.01 M	5.45 M
Light vehicle sales	14.9 M	13.8 M	15.3 M	16.0 M

JOB MARKET

Job gains should decelerate over the next year, depending upon how much supply is boosted by workers reentering the labor force. The unemployment rate is likely to drift higher in coming years as weak (or negative) economic growth slows hiring demand. But even if a modest recession occurs in 2023-24, unemployment is not expected to come close to the double-digit rates seen over the past two downturns.

	2021	2022F	2023F	2024F
Average job growth	562,000	400,000	190,000	160,000
Unemployment rate	5.4%	3.7%	4.5%	4.9%

INTEREST RATES

The Fed is expected to continue tightening rapidly with the fed funds rate rising to the 4.00-4.25 percent range by year-end (and maybe higher in early 2023). Assuming inflation cools as projected, the Fed could begin cutting rates later next year as the economy stagnates or contracts. The yield curve should remain inverted into 2023 with long-term rates declining modestly over the year.

	2021	2022F	2023F	2024F
Federal funds rate	0.00%	4.25%	3.50%	2.50%
10-year Treasury note	1.52%	3.90%	3.50%	2.95%

INFLATION

Prices for energy, food, and commodities should continue to fade over the next year, allowing overall inflation to moderate slowly from current peaks. But core inflation could run above the Fed's long-term goal for a while with housing and service costs still climbing — suggesting that the trend inflation rate could be 2.5 percent (or higher), up from the 2.0 percent average from recent decades.

	2021	2022F	2023F	2024F
Consumer Price Index (CPI)	6.7%	7.0%	3.0%	2.2%
Core CPI	5.0%	5.4%	3.2%	2.5%

Glossary

F	Forecast
BAA Credit Spread	Spread between 10-year treasury note and BAA-rated corporate bond rates
CBOE	Chicago Board Options Exchange
CPI	Consumer Price Index
FOMC	Federal Open Market Committee.
ISM	Institute for Supply Management
NFIB	National Federation of Independent Business
Yield Spread	Spread between the 1-year and 10-year Treasury note rates

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