Nationwide Economics

Monthly Economic Dashboard

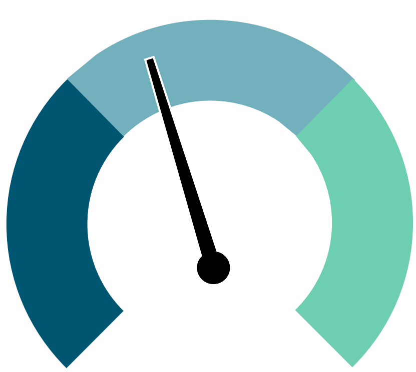
FEBRUARY 2022

Above-trend growth and rapid inflation should prompt more restrictive Fed policy

Fears of an Omicron-induced slowdown did not materialize much in January as businesses kept hiring and consumer activity remained strong. But inflation ran hot again as supply chains showed only modest improvement, further lifting expectations of a sharp policy response from the Fed — with financial markets pricing in much higher short-term interest rates by year-end.

- Job gains were strong for January as employers continued to demand more workers despite Omicron disruptions and rising costs of labor.
- Supply chain woes continue to dampen business production while helping to push up inflation (led by goods price gains) to the fastest pace in 40 years.
- The Federal Reserve is widely expected to kick off a tightening cycle in March with several more increases likely over the rest of the year. In response, interest rates (especially on the shorter end of the yield curve) have jumped so far in 2022 in anticipation of Fed action.
- Expected tighter monetary policy, geopolitical tensions, and growth concerns due to the lingering pandemic and rising inflation have buffeted equity markets and consumer confidence/sentiment, with elevated uncertainty ramping up market volatility.
- The Russian invasion of Ukraine is a new wildcard that could slow economic activity, raise inflation, or both. It is too soon to determine these impacts with any precision.

Current Scorecard



NEGATIVE POSITIVE

Future Scorecard

NEGATIVE POSITIVE

Full scorecards ▶

Nationwide Economics — Monthly Economic Dashboard

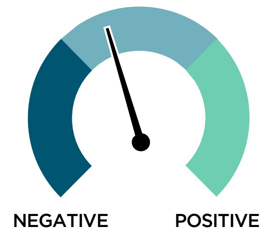
Current Scorecard – February 2022

Data through February 18, 2022

OVERALL

3-MONTH TREND

The impacts from the Omicron variant were less severe than expected with a strong pace of hiring and a surge in retail sales for January. Still, supply chain disruptions remain widespread and may have been exacerbated temporarily by the spike in Covid cases, resulting in slower growth of business activity and even higher inflation. With price gains at the fastest pace in 40 years, consumer sentiment plunged to a pandemic low while the Fed has signaled imminent rate tightening, with financial markets expecting significant moves, contributing to recent market volatility.



EMPLOYMENT

3-MONTH TREND

Nonfarm payroll growth was surprisingly strong for January despite Omicron and with upward revisions has averaged 541,000 over the past three months. The unemployment rate ticked higher, but for positive reasons, as the labor force participation rate rose to a pandemic high. Even with these gains and abundant job openings, the labor market remains tight.

	Current	Previous	Year ago
Employment growth – Jan	467,000	510,000	520,000
Unemployment rate – Jan	4.0%	3.9%	6.4%

FINANCIAL

3-MONTH TREND

Financial markets remained volatile as geopolitical concerns and the prospect of tighter monetary policy buffeted equity indices while sending interest rates higher. The 1-year Treasury note yield nearly tripled over the first 6 weeks of 2022, narrowing yield spreads despite increases in long-term interest rates. A 25 basis point (bps) rate hike at the March FOMC meeting is likely (with a chance of 50 bps).

	Current	Previous	Year ago
Yield spread – Feb	0.91 pp	1.24 pp	1.24 pp
BAA Credit spread – Feb	1.95 pp	1.79 pp	2.13 pp
CBOE market volatility – Feb	26.84	25.27	21.88
S&P 500 stock index – Feb	4,415	4,498	3,921

CONSUMER

3-MONTH TREND

Retail sales rebounded sharply in January, aided by a jump in light vehicle sales — although the supply of autos for sale remains limited by semiconductor shortages. Total home sales fell to end 2021, but demand remains strong despite the recent rise in mortgage rates. Consumer sentiment dropped to its lowest point since 2011 as inflation and geopolitical concerns increased.

	Current	Previous	Year ago
Retail sales – Jan	3.8%	-2.5%	7.2%
Light vehicles sales – Jan	15.0 M	12.5 M	16.8 M
Total home sales – Dec	6.99 M	7.20 M	7.59 M
Consumer sentiment – Feb	61.7	67.2	76.9

BUSINESS

3-MONTH TREND

The ISM business surveys fell again for January as the Omicron variant disrupted production and the availability of inputs — but expansion continued for both manufacturing (with industrial production up again) and services. Inflation and labor issues remained top of mind for many business owners with the NFIB small business optimism index dropping to a year-low for January.

	Current	Previous	Year ago
ISM Manufacturing – Jan	57.6	58.8	59.4
ISM Services – Jan	59.9	62.3	58.5
NFIB small business optimism – Jan	97.1	98.9	95.0

INFLATION

3-MONTH TREND

Inflation remained hot to start 2022 with the 12-month trend rate for the CPI climbing to 7.5 percent for January and the core CPI spiking to 6.0 percent. Energy and goods costs continue to drive much of the inflation spike, but service costs are accelerating, too. The Fed has signaled that monetary policy will be more restrictive in coming years as it attempts to bring inflation back down.

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

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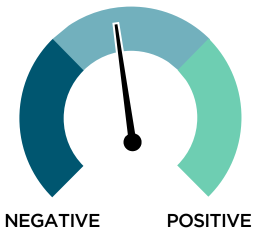
Future Scorecard – February 2022

Nationwide

OVERALL

The sustained surge in inflation is forcing a policy change by the Fed, with analysts now expecting the Fed to tighten by at least 100 bps in 2022 — and some looking for 175 bps. While inflation is expected to peak soon, annual readings should remain elevated into 2023 even if supply chains normalize over the next year as expected. The higher interest rates will help to slow demand and, thus, inflation, but much of the current price pressures are being driven by factors beyond the Fed's influence (*i.e.*, global shipping and energy) — adding uncertainty to the outlook.



THE ECONOMY

As the Omicron variant diminishes, economic activity should reaccelerate, aided eventually by healing supply chains — driving another year of solid growth. Beyond 2022, growth should slow in response to tighter fiscal and monetary policy, along with the economy nearing full resource utilization. The risks of a more substantial slowdown have increased with expected Fed tightening.

	2020	2021	2022F	2023F
Real GDP growth	-3.4%	5.7%	4.0%	2.5%

CONSUMER

Severe constraints in the production of light vehicles should ease over 2022, with elevated sales as demand is expected to remain strong. Higher mortgage rates and lack of supply will slow the pace of home sales in coming years. Strong job gains, rapid wage growth, and record household net worth should help to keep consumer spending solid, especially if goods inflation slows as supply chains normalize.

	2020	2021	2022F	2023F
Total home sales	6.47 M	6.88 M	6.80 M	6.60 M
Light vehicle sales	14.5 M	14.9 M	16.0 M	17.3 M

JOB MARKET

Job gains should remain solid this year, although slowing, boosted by more workers reentering the labor force in response to plentiful job openings, rising compensation, less impact from Covid, and reduced government support. The unemployment rate could drop below 3.5 percent later this year, reaching the lowest levels since at least the late-1960s.

	2020	2021	2022F	2023F
Average job growth	-774,000	555,000	300,000	200,000
Unemployment rate	8.1%	5.4%	3.7%	3.5%

INTEREST RATES

In response to inflation and low unemployment, the Fed is likely to hike the federal funds rate to at least 1.00 percent by year-end, followed by more moves over 2023. Long-term rates should climb over 2022-23 (helped by likely quantitative tightening), although the yield curve should still flatten over time. Risks of a recession later in the forecast period have risen with more Fed tightening.

	2020	2021	2022F	2023F
Federal funds rate	0.00%	0.00%	1.00%	1.75%
10-year Treasury note	0.93%	1.52%	2.25%	2.60%

INFLATION

Inflation should slow over 2022 as supply chain disruptions slowly heal, but elevated readings should extend into 2023 (and perhaps beyond) with lingering supply chain problems. Moreover, some price gains are likely to persist (especially in shelter and other services categories), suggesting that inflation could run above the Fed's long-term goal for several years.

	2020	2021	2022F	2023F
Consumer Price Index (CPI)	1.2%	6.7%	3.8%	2.5%
Core CPI	1.6%	5.0%	3.2%	2.7%

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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