March 2023
Economic Overview

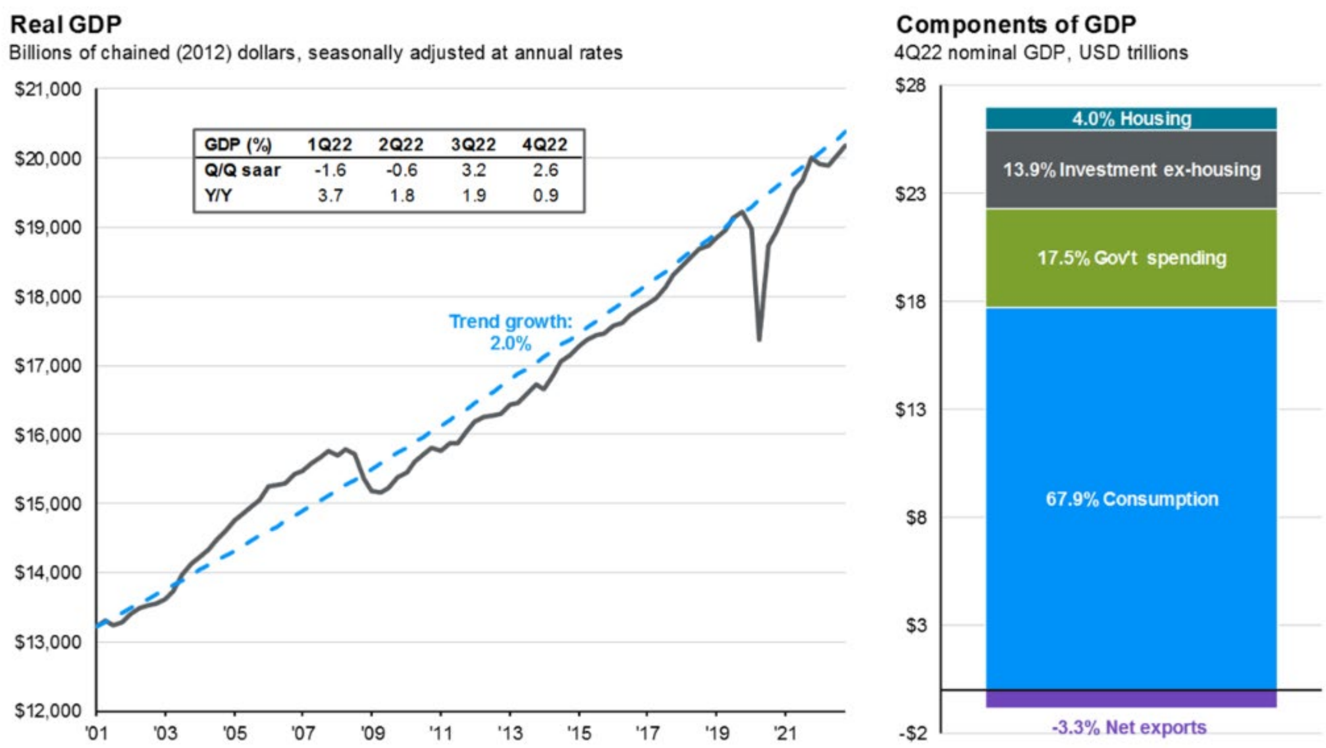
First Affirmative
FINANCIAL NETWORK
Invest for a Sustainable Future

By Richard Frankel

Summary:

- GDP growth is slow and will likely take years to fully recover to its 2% growth trend.
- We are not currently in a recession but may be heading toward a shallow recession in the near term.
- We are in a period of very slow economic growth globally.
- Inflation has moderated but is still very high.

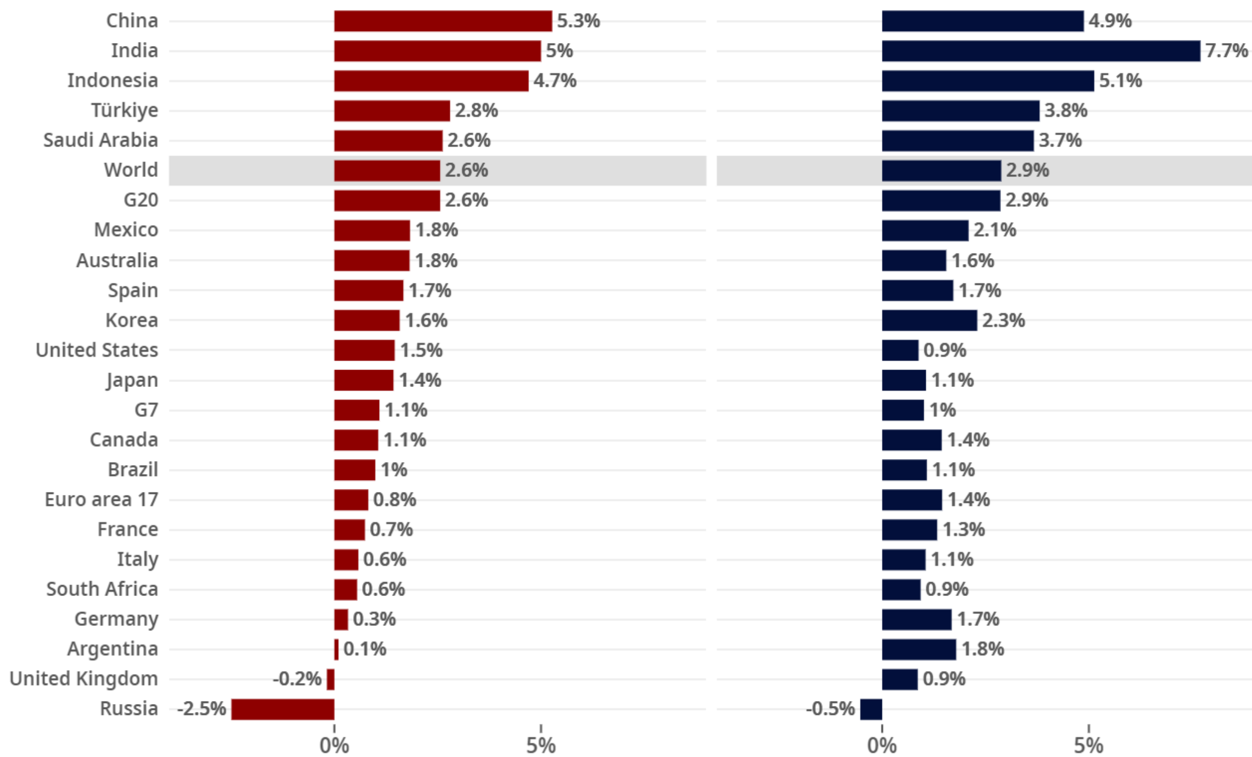
Figure 1. Economic Growth and the Composition of GDP



Source: JP Morgan Guide to the Markets 2Q23

The chart on the left of Figure 1 shows real GDP in dollars over the past 20 years. As predicted in our previous economic commentary, GDP growth has been slow to recover from its recent dip into negative territory and is unlikely to return to the annualized long-term average in the coming quarters. In fact, there is an increased risk of recession in the near term as higher rates and inflation continue to weigh on the economy. The chart on the right shows the components of GDP in the fourth quarter. As always, consumption is the largest component, which suggests the recent decline in retail sales could be a harbinger of recession, particularly with government spending (excluding ballooning interest payments) stagnating at current high levels and housing outlays likely flat to down amid higher interest rates.

Figure 2. Real GDP Growth Projections for 2023 (Red) and 2024 (Blue)



Source: The Organization for Economic Information and Development – Economic Outlook, Interim Report March 2023

Figure 2 from a recent report from Organization for Economic Information and Development (OECD) shows global GDP growth projections for 2023 and 2024. The United States is projected to have 1.5% GDP growth in 2023 and 0.9% GDP growth in 2024, both projections much lower than the long-term average of 2% growth. This remains in line with our previous projections that US GDP will be slow to recover amid the economic turmoil of high rates, and the war in Ukraine. According to the OECD report, UK GDP is set to contract this year, and the Euro zone is set for modest growth, while China is set for relatively strong – albeit well-below the 7%+ Chinese target – growth as it emerges from its COVID Zero shut-down.

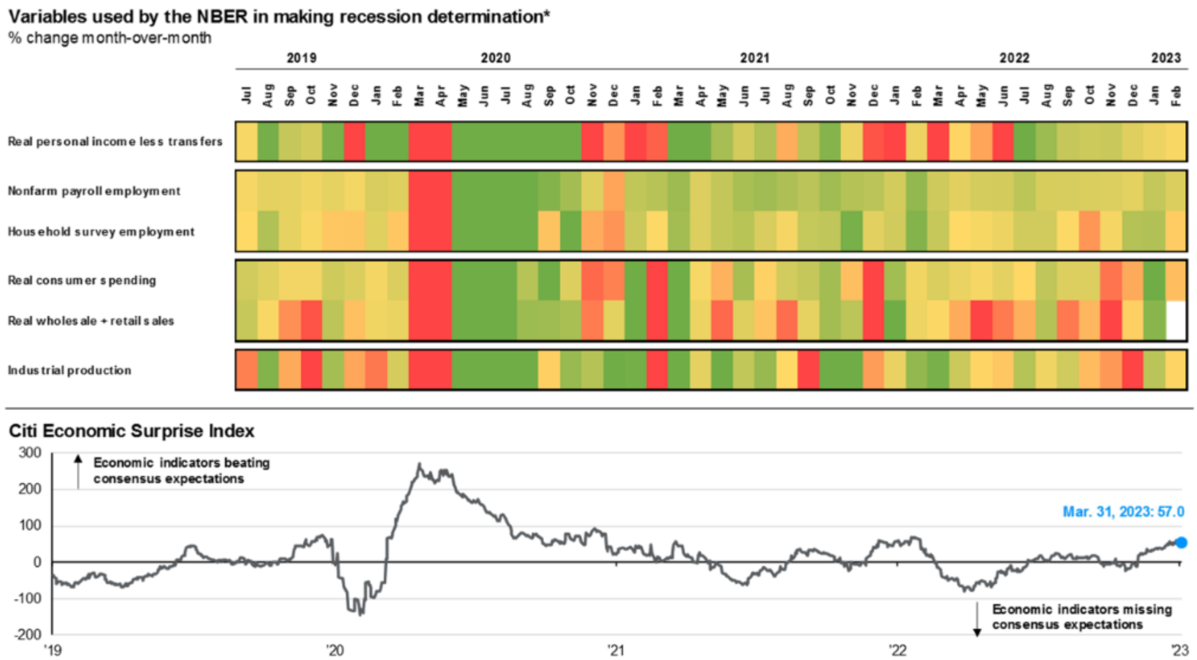
Figure 3. Overview of World Output Growth Projections for 2023 and 2024

		Projections		Difference from January 2023 WEO *Update*[1]		Difference from October 2022 WEO[1]	
	2022	2023	2024	2023	2024	2023	2024
World Output	**3.4**	**2.8**	**3.0**	**–0.1**	**–0.1**	**0.1**	**–0.2**
Advanced Economies	**2.7**	**1.3**	**1.4**	**0.1**	**0.0**	**0.2**	**–0.2**
United States	2.1	1.6	1.1	0.2	0.1	0.6	–0.1
Euro Area	3.5	0.8	1.4	0.1	–0.2	0.3	–0.4
Germany	1.8	–0.1	1.1	–0.2	–0.3	0.2	–0.4
France	2.6	0.7	1.3	0.0	–0.3	0.0	–0.3
Italy	3.7	0.7	0.8	0.1	–0.1	0.9	–0.5
Spain	5.5	1.5	2.0	0.4	–0.4	0.3	–0.6
Japan	1.1	1.3	1.0	–0.5	0.1	–0.3	–0.3
United Kingdom	4.0	–0.3	1.0	0.3	0.1	–0.6	0.4
Canada	3.4	1.5	1.5	0.0	0.0	0.0	–0.1
Other Advanced Economies[2]	2.6	1.8	2.2	–0.2	–0.2	–0.5	–0.4
Emerging Market and Developing Economies	**4.0**	**3.9**	**4.2**	**–0.1**	**0.0**	**0.2**	**–0.1**
Emerging and Developing Asia	4.4	5.3	5.1	0.0	–0.1	0.4	–0.1
China	3.0	5.2	4.5	0.0	0.0	0.8	0.0
India[3]	6.8	5.9	6.3	–0.2	–0.5	–0.2	–0.5
Emerging and Developing Europe	0.8	1.2	2.5	–0.3	–0.1	0.6	0.0
Russia	–2.1	0.7	1.3	0.4	–0.8	3.0	–0.2
Latin America and the Caribbean	4.0	1.6	2.2	–0.2	0.1	–0.1	–0.2
Brazil	2.9	0.9	1.5	–0.3	0.0	–0.1	–0.4
Mexico	3.1	1.8	1.6	0.1	0.0	0.6	–0.2
Middle East and Central Asia	5.3	2.9	3.5	–0.3	–0.2	–0.7	0.0
Saudi Arabia	8.7	3.1	3.1	0.5	–0.3	–0.6	0.2
Sub-Saharan Africa	3.9	3.6	4.2	–0.2	0.1	–0.1	0.1
Nigeria	3.3	3.2	3.0	0.0	0.1	0.2	0.1
South Africa	2.0	0.1	1.8	–1.1	0.5	–1.0	0.5
Memorandum							
World Growth Based on Market Exchange Rates	3.0	2.4	2.4	0.0	–0.1	0.3	–0.2
European Union	3.7	0.7	1.6	0.0	–0.2	0.0	–0.5
ASEAN-5[4]	5.5	4.5	4.6	0.2	–0.1	0.0	–0.3
Middle East and North Africa	5.3	3.1	3.4	–0.1	–0.1	–0.5	0.1
Emerging Market and Middle-Income Economies	3.9	3.9	4.0	–0.1	–0.1	0.3	–0.1
Low-Income Developing Countries	5.0	4.7	5.4	–0.2	–0.2	–0.2	–0.1
World Trade Volume (goods and services)	**5.1**	**2.4**	**3.5**	**0.0**	**0.1**	**–0.1**	**–0.2**
Imports							
Advanced Economies	6.6	1.8	2.7	–0.1	0.2	–0.2	–0.1
Emerging Market and Developing Economies	3.5	3.3	5.1	0.2	0.7	0.3	0.4
Exports							
Advanced Economies	5.2	3.0	3.1	0.4	0.2	0.5	–0.3
Emerging Market and Developing Economies	4.1	1.6	4.3	–0.6	–0.4	–1.3	–0.2
Commodity Prices (US dollars)							
Oil[5]	39.2	–24.1	–5.8	–7.9	1.3	–11.2	0.4
Nonfuel (average based on world commodity import weights)	7.4	–2.8	–1.0	3.5	–0.6	3.4	–0.3
World Consumer Prices[6]	**8.7**	**7.0**	**4.9**	**0.4**	**0.6**	**0.5**	**0.8**
Advanced Economies[7]	7.3	4.7	2.6	0.1	0.0	0.3	0.2
Emerging Market and Developing Economies[6]	9.8	8.6	6.5	0.5	1.0	0.5	1.2

Source: World Economic Outlook Update – April 2023

In Figure 3, we can see the World Economic Organization's most recent world output projection for 2023 and 2024, along with the differences in the current projections between the projections from January 2023 and October 2022. Overall, world output forecasts for 2023 and 2024 declined in the most recent period as commodity prices moderated. The United States recorded a 2.1% increase in output in 2022 but is projected to have slow growth in 2023 and 2024. In 2023 growth is expected to be 1.7%, and it is expected to be even lower in 2024 at 1.1%. Both numbers are lower than the 2% or higher GDP growth the US needs to get its GDP back on trend.

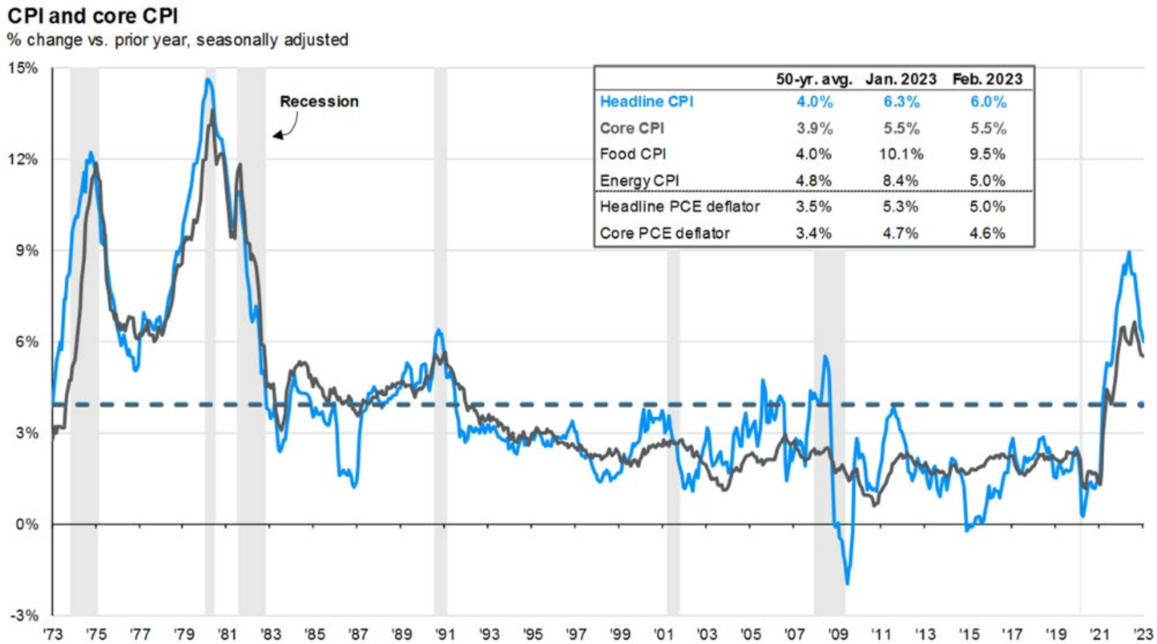
Figure 4. Recession Determinants



Source: JP Morgan Guide to the Markets 2Q23

Recession is defined by the National Bureau of Economic Research (NBER) as a broad decline in six economic variables, which lasts more than a few months, throughout the country. In Figure 4 above, green means expansion and red means we are in a recession. The shading or boldness of the color illustrates how strong the gain or loss was relative to history. While there are many shades of orange on the right of the chart, there is no red, meaning we are not currently in a recession, but instead a period of slow growth. All six determinants fell over the past month. While we are not yet technically in a recession, one may still loom on the horizon considering all of these factors did drop over the past few months. Below the heat map is the Citi Economic Surprise Index, which shows how much economic performance has outperformed or underperformed against analyst expectations. A reading above zero means that the economy has outperformed analyst expectations, while a reading below zero means the economy has underperformed against analyst expectations. Recently, economic data has been outperforming expectations, although only slightly.

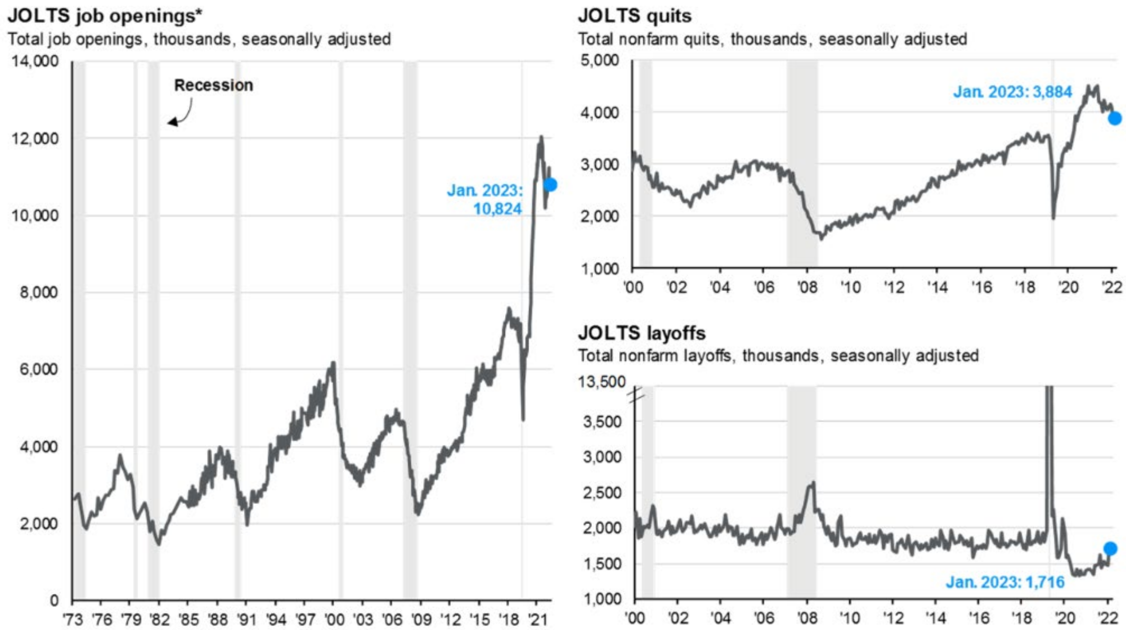
Figure 5. Inflation



Source: JP Morgan Guide to the Markets 2Q23

Although headline Consumer Price Inflation is cooling, as shown in Figure 5, it was still at 6% as of February 2023, which is higher than the 50-year average by 2% and well above the Fed's 2% target. This level of inflation has not been seen since the recession of the 1980s, despite the decrease in CPI in recent months. Inflation is down from its high of nearly 9% last year, which bodes well for a moderation in interest rate increases and points toward a shallow recession, at worst. If inflation continues to fall, consumers will be able to afford more goods again, raising consumption and thereby increasing GDP growth.

Figure 6. Labor Demand



Source: JP Morgan Guide to the Markets 2Q23

Figure 6 shows the current number of job openings in the US on the left. On the top right, there is a chart showing how many workers are quitting their jobs. On the bottom left, there is a chart showing how many layoffs are currently happening in the US. As shown on the left chart, while job openings have come off record highs, they remain extraordinarily high by historical standards. This is important because even if a recession weighs on labor demand, there is a large buffer before demand falls behind supply and results in unemployment. The top right chart shows that quit levels have fallen from recent record highs, suggesting that workers still feel emboldened by a hot labor market – albeit less so – to search for better job opportunities. The bottom right shows layoffs, which have ticked up from recent record lows as companies continue try to retain existing workers while "pruning" around the edges. The good news about these charts is that if there is a recession, there is unlikely to be a shortage of job openings, and labor demand is likely to level off soon as economic growth slows.

Things to watch out for:

- Slow economic growth through 2024
- Possibly a shallow recession
- Moderating inflation rates
- A more stable labor market

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