The Economic Outlook

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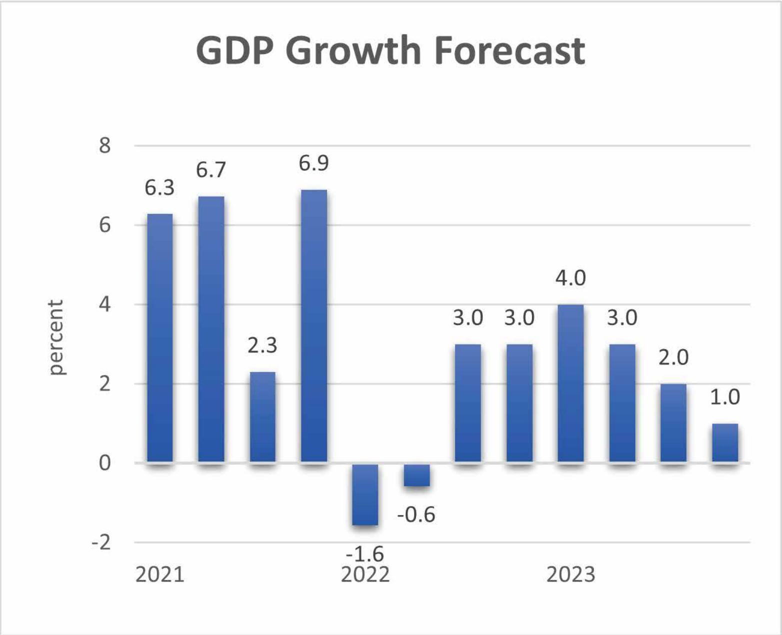
Growth is likely for the overall economy over the next nine to 12 months, but then a widespread slowdown emerges as a major risk.

The United States is not in recession despite two down quarters for inflation-adjusted gross domestic product (GDP). That's a rough rule of thumb for recession, but in this case we enjoyed growth in employment, production, and inflation-adjusted spending and business sales. It's not a recession.

Looking forward through the middle of 2023, consumer spending will be strong thanks to high consumer savings in the pandemic. Consumers will gradually use their cash to maintain spending in this high-inflation environment.

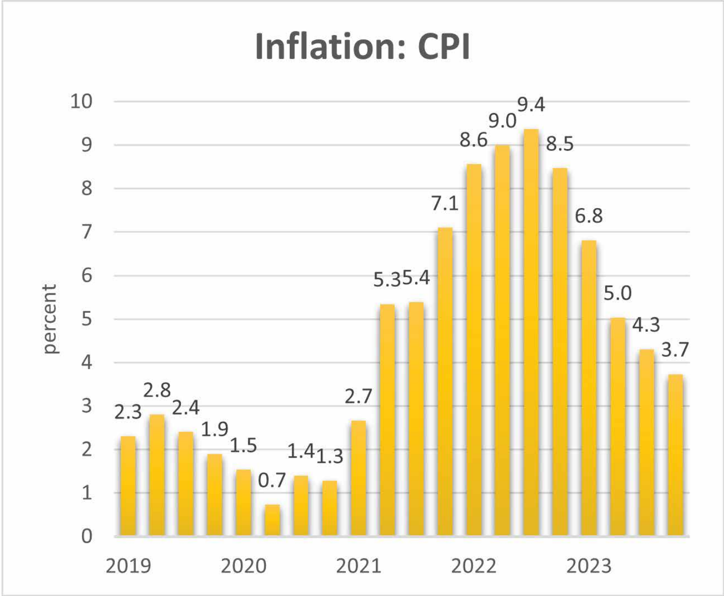
Businesses are placing orders for computers, equipment and machinery. Many of these labor-substituting products are on backorder, so actual expenditures have not grown too fast, but they are coming.

The federal government will continue spending, with student loan forgiveness also stimulative. State and local governments will boost their outlays thanks to their own rising tax revenue plus grants from the federal government.



The Federal Reserve has started tightening. Past Fed action, however, is like a rat in the snake's belly: It will take another year for monetary stimulus to work through the economy's digestive system.

The next nine months or so should be good for the overall economy. Despite the general upward trend, weakness will come to interest-sensitive sectors including construction, car sales and some business spending.



Eventually economic growth will slow and then inflation will decline. Some of the forecasted inflation drop is the end of transitory factors, such as sky-high gasoline and used car prices. The greater factor is past stimulus working through the system, and the Fed's turnaround will pull inflation down to three percent by 2024.

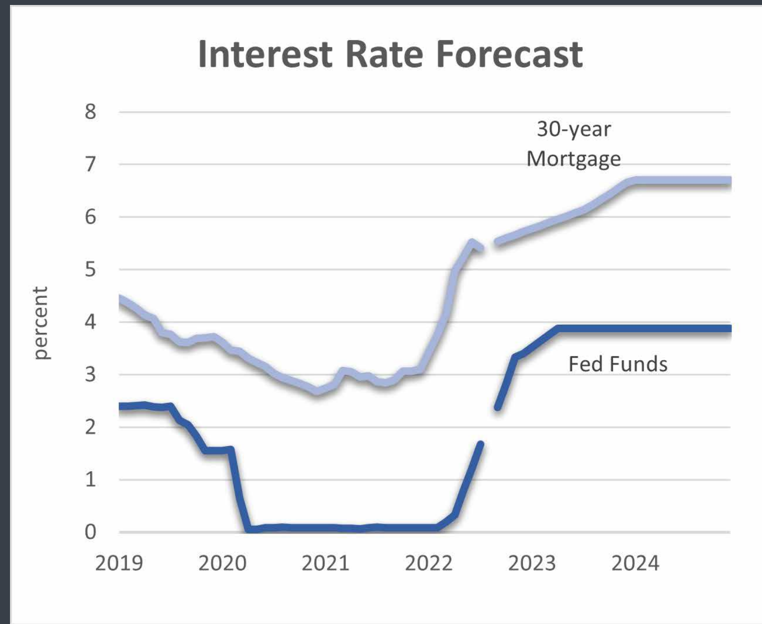
To bring inflation down, the Fed is likely to boost short-term interest rates to four percent and possibly higher. Mortgage rates and other long-term interest rates result from both Fed policy and global financial conditions. Mortgages will likely level off at six percent next year.

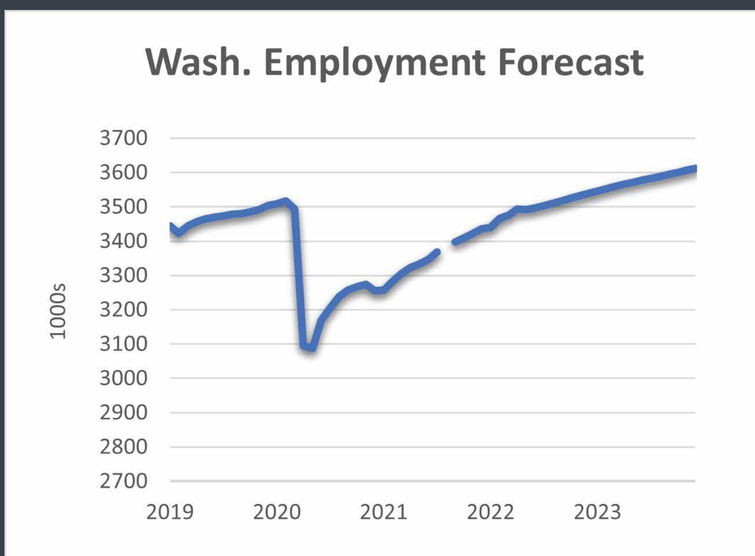
Some investors and economists doubt that the Fed will keep up the fight when employment starts to soften. Jobs weaken well before inflation comes down because of different time lags. Back in the 1970s, the Fed gave in too soon with disastrous results. Although we can't be certain what path they will take in 2023, reading minutes of the Fed meetings, listening to interviews with key decision-makers and reviewing their speeches lead to the favorable conclusion: Federal Reserve decision-makers are determined not to repeat the mistakes of the high-inflation era.

The risk of recession rises in late 2023 and early 2024. The odds of a downturn at that time are around 80 percent.

Here in the Pacific Northwest, both Oregon and Washington employment is growing faster than the long run trend. Both states should reach their pre-pandemic jobs peak in a few months.

Labor markets are tight in Washington, with unemployment below four percent and job openings exceeding unemployed people.





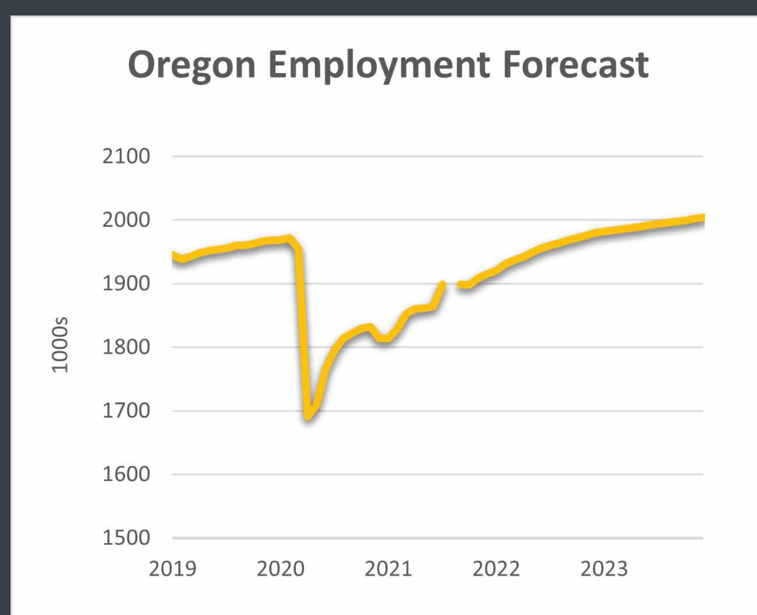
> "Here in the Pacific Northwest, both Oregon and Washington employment is growing faster than the long run trend."

Oregon similarly has low unemployment—3.2 percent—and the number of open positions sits a whopping 60 percent greater than unemployed people.

Home prices have risen a good bit in most parts of Washington and Oregon. In the Evergreen State, home prices are up 23 percent from a year ago, with the Beaver State enjoying 20 percent price appreciation.

The weakness of downtowns threatens the broader metropolitan areas. Portland is third worst of 62 cities in a recent survey of people returning to downtowns. Seattle is also well below average. Can economic activity in suburbs replace downtown business? Or will sinking downtowns pull down outlying areas? It's an open question and an important issue to watch.

Businesses in the region should watch their own industries and assess how they will fare as the Fed continues to raise interest rates. Contingency plans for recession are important, as is consideration of how to survive continued labor market tightness.



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