

The Economic Outlook

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Quarterly Economic Newsletter

Inside Q3

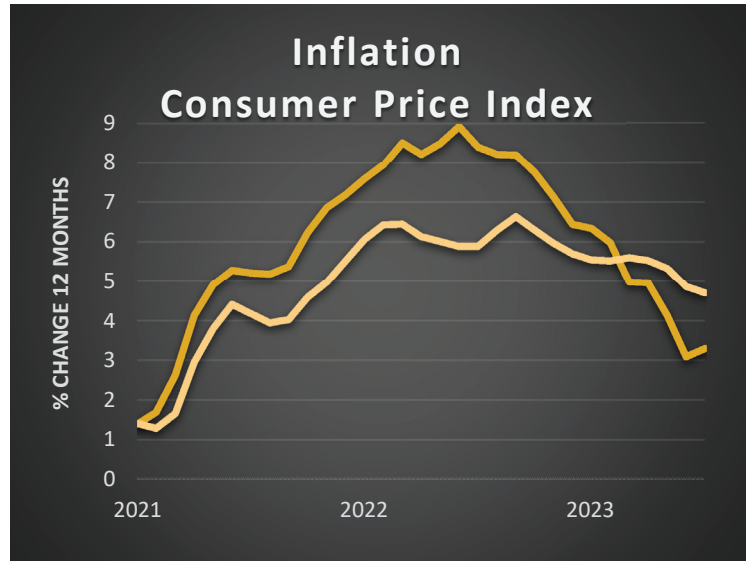
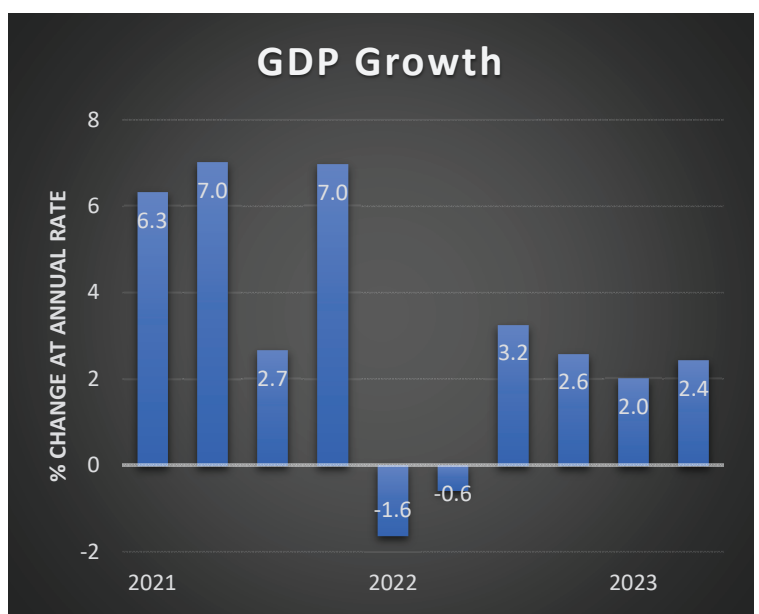
Economy surpassing expectations.

The United States economy has performed quite well so far in 2023, surpassing many people’s expectations. The effects of the Federal Reserve’s tightening have not fully spread through the economy, so a mild recession will likely begin in early 2024, but it should not be disastrous for most of the economy. The Pacific Northwest will feel the downturn, but without the sharp decline we’ve had in some past recessions.

Economic growth in the second quarter felt like a student whose final exam grade was B- after worrying that he might flunk. The gain in gross domestic product was a little above average and not nearly as bad as expected. Consumer spending grew somewhat, but business capital spending grew more rapidly.

Higher interest rates will trigger a recession, but five factors will delay the onset. Automobile sales usually fall when interest rates rise, but supply chain problems in the past two years limited availability. The pent-up demand props up current sales, but the decline will eventually come.

Single family home sales and construction also usually drop with rising interest rates, but recently have turned up. First-time home buyers find few existing homes listed for sale because current owners have low mortgage rates and don’t want to move. So new homes are selling well.



Business capital spending has also held up well despite higher interest rates and fears of recession. Part of the strength comes from buying equipment that substitutes for the workers who often cannot be found. Another part of the strength is reshoring manufacturing in light of supply chain fragility and Chinese geo-political risks.

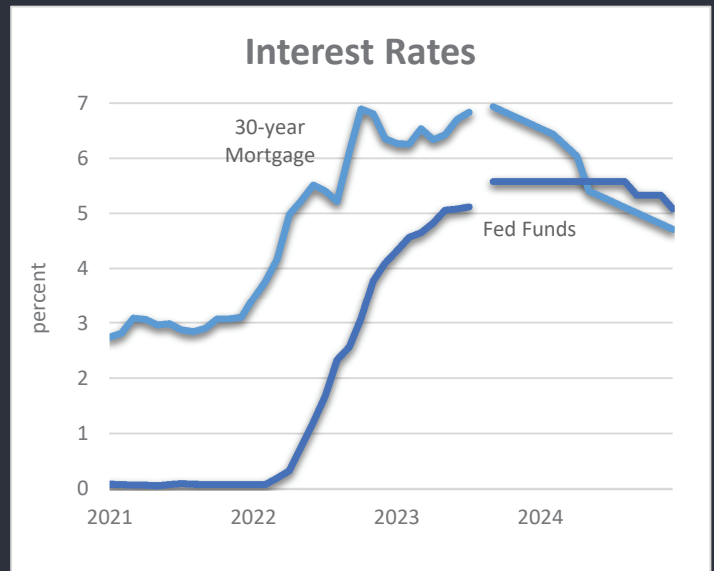
The fourth delaying factor is the tight labor market. People who have been laid off are used to driving past "Help Wanted" signs, so they often can shift to another job immediately. Every month total employment increases despite some layoffs.

Finally, many of those who lack jobs still have savings left over from the pandemic stimulus, so spending cutbacks are milder than typical.

The stronger business capital spending strength will not only delay the downturn but also make it milder than an average recession when it comes.

Inflation will gradually drift down to the two percent target the Fed is aiming at.

The Federal Reserve is not hoping for a recession, but they accept that possibility in order to bring inflation down. They will likely push short-term interest rates up another quarter point and then hold them steady for 12 months. Unlike the Fed of the 1970s, today's monetary policy decision makers will persist until it's clear that inflation is coming down. Short-term interest rates will remain high through most of 2024. Mortgage and other long-term rates will probably drop earlier, when securities markets anticipate eventual Fed easing.

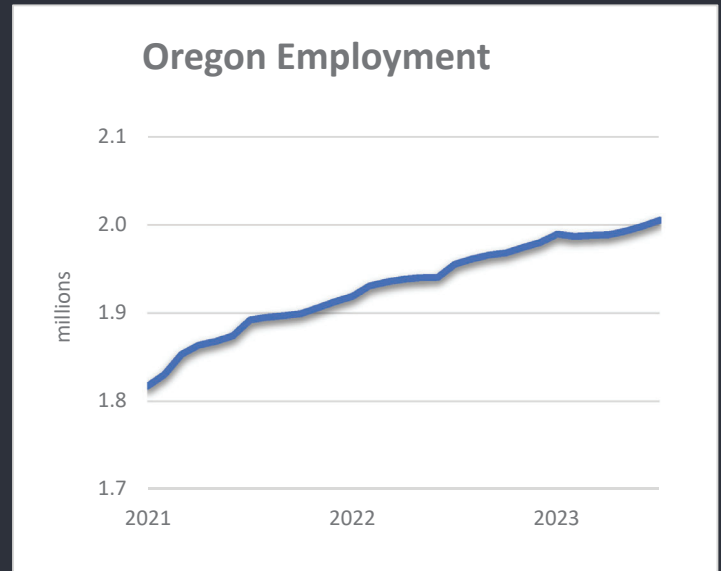


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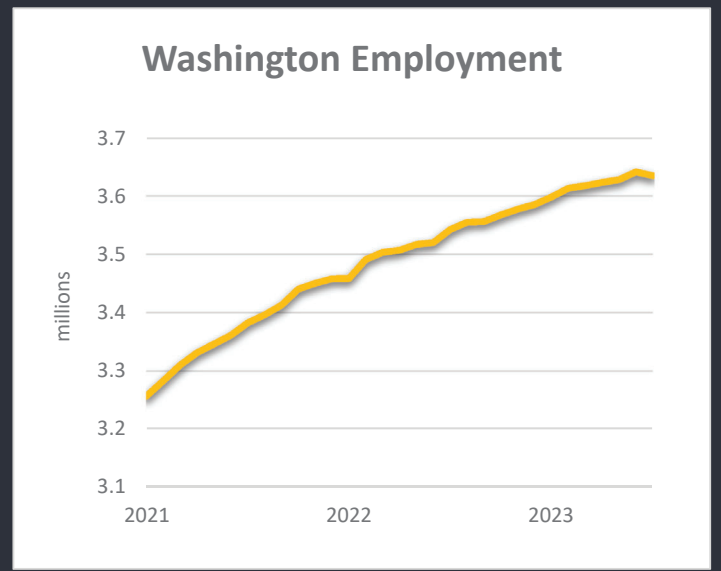
This picture of the domestic economy derives partly from soft global economic growth. Europe will hardly expand at all but not fall into recession. China is decelerating rapidly and may actually shrink in economic magnitude. China's weakness will spread to neighboring East Asian economies.

The Pacific Northwest matches national data more closely than usual. Job growth is just a hair faster in Oregon and Washington than in the U.S. overall,

with unemployment about the same. Boeing's production rebound helped Washington manufacturing. Intel has plans to develop additional space that could boost Oregon employment. Both states have increased healthcare employment as well as jobs in bars and restaurants. The labor market is tight here as it is in the rest of the country.



New construction of single family homes dropped last year but have rebounded in recent months, reflecting the national pattern. Apartment rents have declined on both sides of the Columbia River as people consolidate households, living with roommates or family members to save on costs.



Economic weakness in China threatens our region, as that country is the largest buyer of exports from both Oregon and Washington. A recession in China would remove a long-standing source of strength here.

Both Oregon and Washington will survive a national recession, though with rising unemployment and some bankruptcies. Like the rest of the country, the two states will fare better in a low inflation environment. We should be back there in a couple of years.