

The Economic Outlook

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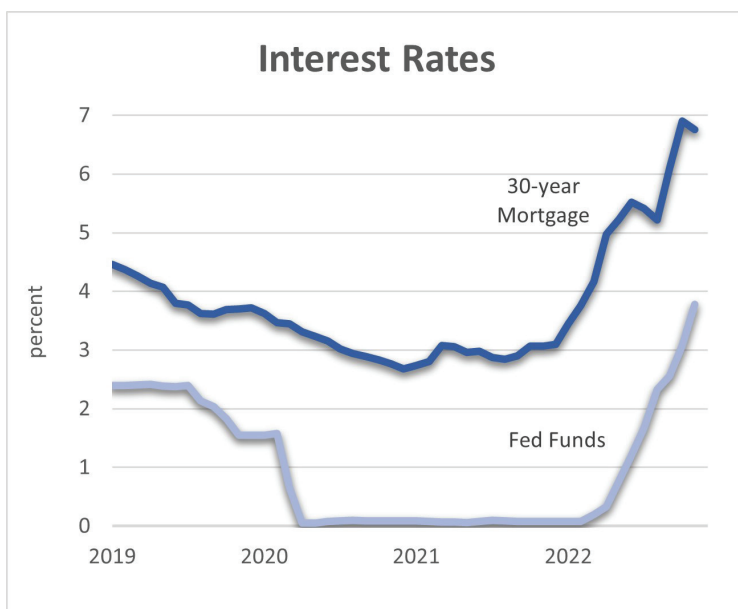
Quarterly Economic Newsletter

Inside Q4

The Federal Reserve's effort to fight inflation will impact businesses in cities small and large across the country as well as in the Pacific Northwest. The Fed will succeed, but it will take at least two years and entail significant disruptions to families and companies. The fight is worthwhile, because allowing inflation to remain high has even worse consequences in the long run.

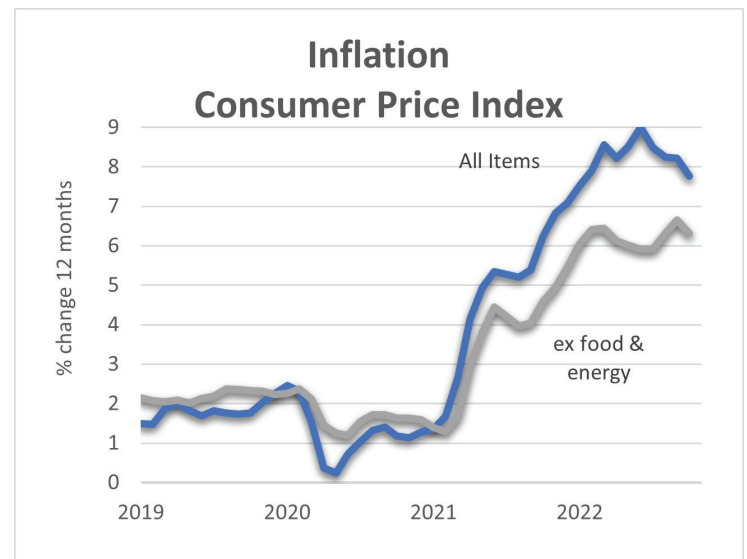
The Fed projected in September pushing short-term interest rates above 4.5 percent, but have since revised their plans to even more tightening. Rates will almost certainly rise above five percent, with little expectation of a quick reversal. Statements by the Federal Reserve officials show consistent belief that fighting inflation must be their number one priority.

The initial impacts are being felt in the housing sector: home transactions, mortgage originations and title insurance sales have all dropped sharply. Starts of single family homes are falling. Construction of multi-family residences and non-residential projects will also decline, but with a longer time lag due to the lengthier planning, permitting and construction processes.



Consumer spending usually responds as employment falls, but this cycle will be a bit delayed. Consumers saved a lot of money in the first two years of the pandemic, thanks to government stimulus and eventually pay raises at a time when spending opportunities were constrained.

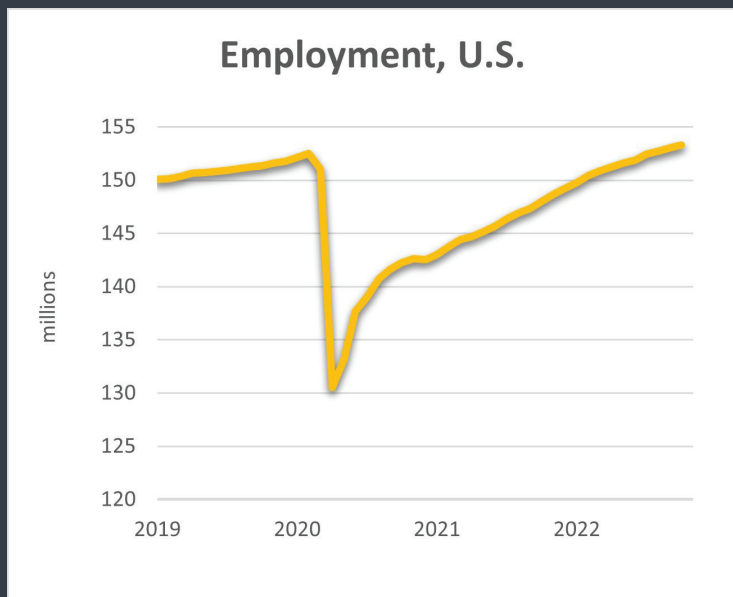
Business capital spending also declines in the typical business cycle, as profits drop and companies don't see the need for capacity expansion. This time around, however, companies are ordering computers, machinery and equipment to make up for the personnel they have been unable to hire.



The first layoffs in a recession usually come as business sales decline, and already some highly cyclical companies are cutting back on staffing. But at most businesses, open positions will be cut first, and there are many openings across all sectors of the economy.

The combined effects of the high savings of households and the extreme number of open positions will be to delay the start of the recession. Although stock market investors feel like the downturn has already begun, the actual economic recession will begin in late 2023 or early 2024, with only a small chance—perhaps just five percent—that we'll enjoy a soft landing.

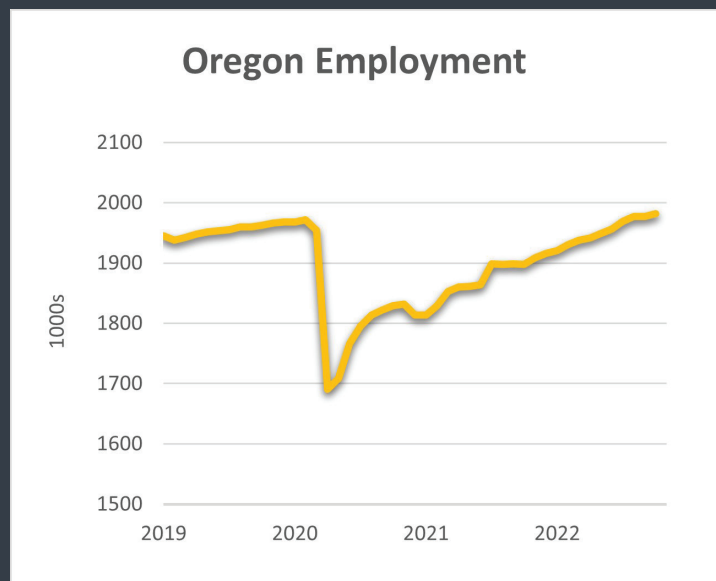
The upcoming recession will hurt only half as much as the 2008-09 recession (though this is just a rough estimate). Lenders have been cautious about credit standards for home mortgages as well as business loans, so financial hardship will not have the ripple effects that devastated the economy last time.



In the Pacific Northwest, job gains continue. Both Washington and Oregon have surpassed their pre-pandemic peak employment levels, though the pace of growth has slowed in recent months. Unemployment remains in the neighborhood of four percent, with job openings exceeding the number of unemployed individuals in the two states.



Population estimates for Oregon through July 2022 showed very slow growth, just a third of a percent. The figures are less reliable than usual due to weak data collection in the pandemic and incomplete alignment with the 2020 census. Washington State had previously released its annual estimates showing solid growth through April 2022.



Home price gains in our region were strong through the middle of 2022, but prices softened in recent months as buyers were reluctant to both pay high prices and finance at high interest rates. The local multiple listing services report declines in transactions and longer average times on market.

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Apartment rents are also declining in the Pacific Northwest, at least in the metropolitan areas for which monthly data are available. Weak demand for housing, both single family and multi-family, indicates that people are either moving in with family members or taking on roommates.

Nonresidential real estate markets in Puget Sound and the Portland metropolitan area are generally good except for office space, which has very high vacancy and softening rents. Industrial space is in high demand despite a good bit of new construction, reflecting online sales activity that needs warehouse space. Retail has weathered the transition to increased online sales pretty well, though the large malls are still challenged.

The Pacific Northwest will not be immune to recession, but it enters the dangerous period with good momentum and a long history of growth exceeding the national average.