# THE ECONOMIC OUTLOOK GROUP

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## ECONOMIC TALKING POINTS

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## Beware of Frothy Forecast of GDP and Inflation

**If you suddenly feel the ground shaking beneath you, it's not because an earthquake struck. What you're experiencing is a colossal stampede of Wall Street bulls trampling over their previous lower economic forecasts but are now charging ahead with frothy upward revisions to GDP growth and inflation projections.**

**What sparked this herd-like run is the realization the economy will soon receive a $1.9 trillion jolt in financial aid, along with growing confidence the Covid-19 health crisis will soon be behind us. And so in just the last few days, we have seen one investment house after another lift their 1Q growth from 3% to in some cases more than 9%.**

**Full year estimates have also jumped from 4% to as much as 10%. Even the OECD joined the wild dash this week, raising their forecast for US GDP to expand by 6.5% this year and 4% in 2022, trashing their December outlook of 3.2% and 3.5%, respectively.**

**Along with forecasting more substantial economic growth came expectations that inflation will transition from being lukewarm to turning red-hot in the coming months. So much so that analysts believe the Fed would come under intense pressure to tighten monetary policy much earlier than planned. Not only could they be scaling back QE by midyear, but perhaps also raise the fed funds rate late this year or early 2022.**

**We believe all these revisions have gone too far, too quickly.**

**Yes, the latest stimulus package has the potential to fuel faster growth. And, of course, we are also hopeful the wider roll out of the vaccine will bring this catastrophic pandemic to an end sooner. Both these developments and the prospect**

**of yet another major spending project on infrastructure could well shift economic activity into much faster gear.**

**But we still think the exuberance shown by all these sharply higher GDP and inflation forecasts is premature and excessive.**

**For one, the economic models used to make such predictions were designed for another time and another era – one that bears absolutely no resemblance to the unprecedented issues that face us today.**

**Second, there are still many critical questions that remain unanswered. Check them out:**

- **With respect to protection from Covid-19, we still don't know when the country will reach herd immunity.**

- **Will employers retain a latent fear or hesitation to bring back workers until all their people are vaccinated?**

- **How serious of a threat do Covid-19 mutations pose? It's important to acknowledge that we're not yet out of the woods.**

- **We know Americans have accumulated nearly $4 trillion in personal savings, but it's not yet clear how comfortable they are about future job and income security. Consumer confidence levels have been wobbly at best.**

- **There are also the deeper structural changes to the economic and business landscape caused by the pandemic. We are talking here about changes in the work environment as more people function remotely, the cutback in corporate travel, and finally how the coronavirus and technology will alter globalization and trade flows.**

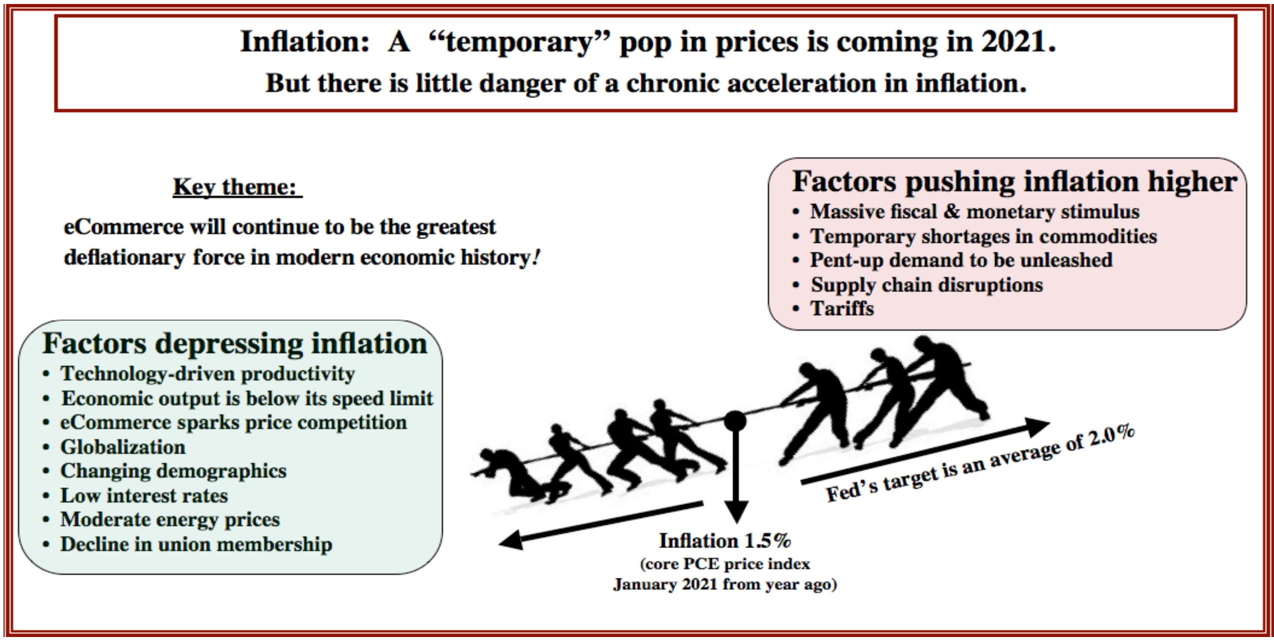
**These are all transformational events and for that reason we need to be more careful how macroeconomic projections are made in this unfamiliar environment.**

**Take today's release of the CPI, which saw February's headline increase by 0.4%. You may read how last month's top line jump was the biggest in six months and view this as evidence that prices are headed sharply higher. But this was the result of a temporary surge in energy prices caused by the unusual cold wave that hit the South and Midwest. Remove the energy component from the equation and CPI creeped up a mere 0.1% last month. In fact, when you ex-out the normally volatile food and energy factors, annual core CPI in February slipped to 1.3%, from 1.4% in January.**

**Drill down farther and you see how the pandemic directly affected several major sectors within the CPI: Airline fares for the month were down 5.1% and 25.6% over the past 12 months. With fewer people dressing up for office work, the cost of apparel keeps falling; it dropped another 0.7% in February and 3.6% annually. One especially hard hit industry has been lodging; the price of hotel rooms declined 2.7% last month and fell more than 17% over the year.**

**As the economy gradually improves, all those sectors that currently enjoy little pricing power will slowly see those dynamics reverse.**

Our main perspective on inflation remains the same. In the constant tug of war that influences the direction of prices, we still see disinflation being the dominant force as you can see from the chart below.




So will there be a pop in inflation in the coming months? Of course! But we're in agreement with the Fed that this is likely to be a transient event.

Anyone looking out for the kind of runaway price inflation we experienced decades ago will have to peer through the Hubble telescope.

Our forecast is for headline CPI to hover mostly between 2% to 3% through 2023. With respect to the core PCE price index, the Fed's preferred inflation gauge, it will trend gradually higher from 1.8% this year, 2.1% in 2022 and 2.4% for 2023.

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## United States

| | I 2020 | II 2020 | III 2020 | IV 2020 | I 2021 | II 2021 | III 2021 | IV 2021 | I 2022 | II 2022 | III 2022 | IV 2022 | I 2023 | II 2023 | III 2023 | IV 2023 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Real Gross Domestic Product (GDP):** | | | | | | | | | | | | | | | | |
| % | -5.0 | --31.4 | 33.4 | 4.1 | 4.2 | 5.1 | 5.3 | 6.1 | 3.1 | 6.2 | 5.5 | 4.8 | 2.8 | 3.8 | 3.1 | 2.9 |
| **Personal Consumption Expenditures:** | | | | | | | | | | | | | | | | |
| PCE % | -6.9 | -33.2 | 41.0 | 2.4 | 4.4 | 5.2 | 4.7 | 6.0 | 2.4 | 5.2 | 4.1 | 3.9 | 4.0 | 4.1 | 2.8 | 3.5 |
| **Inflation, end of period, year-over-year:** | | | | | | | | | | | | | | | | |
| CPI % | 1.5 | 0.6 | 1.4 | 1.4 | 1.5 | 2.0 | 2.5 | 2.7 | 2.5 | 2.5 | 2.3 | 2.2 | 2.5 | 2.6 | 2.6 | 2.7 |
| **Unemployment Rate (end of period):** | | | | | | | | | | | | | | | | |
| % | 4.4 | 11.1 | 7.8 | 6.7 | 6.2 | 6.0 | 5.9 | 5.8 | 5.8 | 5.8 | 5.6 | 5.4 | 5.4 | 4.9 | 4.4 | 4.1 |
| **Non-farm Payrolls, monthly avg. thousand:** | | | | | | | | | | | | | | | | |
| | -303 | -4,427 | 1,322 | 283 | 322 | 385 | 370 | 380 | 270 | 285 | 265 | 240 | 185 | 225 | 235 | 250 |
| **Treasury 10-yr Note Yield % (end of period):** | | | | | | | | | | | | | | | | |
| | 0.63 | 0.65 | 0.68 | 0.91 | 1.47 | 1.51 | 1.60 | 1.70 | 1.82 | 2.05 | 2.00 | 1.94 | 1.90 | 2.05 | 2.00 | 2.10 |
| **Federal funds rate % (end of period):** | | | | | | | | | | | | | | | | |
| | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.13 | 0.38 | 0.88 | 1.13 |

## GDP Growth - Global Economy

| Country | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| US | 2.6 | 1.6 | 2.2 | 1.8 | 2.5 | 3.1 | 1.7 | 2.3 | 3.0 | 2.2 | -3.5 | 5.1 | 5.3 | 3.2 |
| Eurozone | 1.7 | 1.4 | -0.9 | -0.2 | 1.4 | 2.1 | 1.9 | 2.5 | 1.9 | 1.2 | -6.8 | 3.3 | 2.5 | 2.0 |
| United Kingdom | 1.7 | 0.7 | 0.3 | 1.8 | 2.9 | 2.2 | 1.9 | 1.9 | 1.3 | 1.5 | -9.9 | 4.4 | 4.6 | 3.1 |
| Japan | 4.6 | -0.4 | 1.6 | 1.5 | -0.1 | 1.1 | 0.5 | 2.2 | 0.3 | 0.7 | -4.8 | 2.4 | 2.8 | 2.2 |
| Canada | 3.1 | 3.1 | 1.8 | 2.3 | 2.9 | 0.7 | 1.0 | 3.2 | 2.0 | 1.6 | -5.1 | 5.4 | 3.4 | 2.9 |
| India | 8.4 | 8.6 | 6.7 | 4.9 | 7.4 | 8.0 | 8.1 | 7.2 | 6.8 | 4.8 | -8.2 | 9.1 | 6.4 | 5.7 |
| China | 10.5 | 9.5 | 7.8 | 7.7 | 7.3 | 6.9 | 6.7 | 6.8 | 6.6 | 6.1 | 2.3 | 6.9 | 5.7 | 5.6 |
| Brazil | 7.5 | 2.7 | 0.9 | 2.3 | 0.1 | -3.5 | -3.5 | 1.2 | 1.2 | 1.1 | -4.1 | 2.9 | 2.7 | 2.4 |
| Mexico | 5.2 | 4.0 | 3.9 | 1.4 | 2.3 | 2.7 | 2.7 | 2.4 | 2.1 | -0.1 | -8.3 | 3.3 | 2.8 | 2.7 |
| Australia | 2.8 | 2.6 | 3.6 | 2.4 | 2.6 | 2.5 | 2.4 | 2.4 | 2.7 | 1.8 | -1.1 | 2.5 | 3.0 | 2.7 |
| Russia | 4.0 | 4.3 | 3.4 | 1.3 | 0.6 | -2.8 | -0.2 | 1.6 | 2.5 | 1.2 | -3.1 | 2.4 | 3.3 | 2.0 |
| World | 4.2 | 3.1 | 2.5 | 2.6 | 2.8 | 2.8 | 2.6 | 3.4 | 3.2 | 2.9 | -4.2 | 4.4 | 4.2 | 3.9 |