

# THE ECONOMIC OUTLOOK GROUP



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## ECONOMIC TALKING POINTS

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### The Fed's dilemma:

The economy is clearly slowing; yet inflation keeps plowing ahead

The inflation heat wave continues with both consumer and wholesale prices climbing faster than analysts expected in June. The former has been edging dangerously close to double-digit rates, while the latter already crossed that threshold in each of the last 7 months.

The latest leap up in inflation fueled more speculation the Fed is inclined to hike rates by a historic full percentage point later this month, with the terminal rate, by some estimates, settling well past 4%.

If that is the plan, it requires us to warn clients that such a rapid pace in monetary tightening will ultimately do more harm than good for consumers and business. By that we mean, brace yourself for an economic downturn AND stubbornly high inflation this year.

Here's why. This inflation cycle is unlike any in the past. It's a global inflation problem triggered by global shocks. So even if the Fed ratchets up rates to the point where it sucks out all the oxygen from the economy, it will still not make much of a dent in bringing inflation close to the Fed's 2% target.

That's because so long as the war in Ukraine rages on, it will continue to elevate food and energy prices. And if China repeatedly shifts back and forth between lockdowns and reopenings, it will stall any progress in global supply chains. So long as Russia reduces or shuts down the flow of natural gas to Europe, the cost to Western and

Central European countries to rebuild their inventory for next winter will surge. That will also encourage US energy companies to export even more LNG to the region.

These are all inflation dynamics of which the Fed has little control. It can certainly dampened domestic demand by raising the cost of borrowing, but can't do anything about improving the global supply of goods ---which is at the heart of the current inflation problem. So any aggressive series of rate hikes in the US designed to force inflation to roll over looks more like firefighters pouring water on a building because it's nearby when the actual blaze is happening across town.

Case in point: It's not ironic that just weeks after Jerome Powell first raised the fed funds rate in March, the number of Americans filing for unemployment benefits to turned up. And it has continued to climb every week since then on a 4-week moving average basis. New filing last week surged by 9,000 to 244,000, the highest level in nearly 8 months. Clearly, the Fed's monetary tightening is having an effect. Yet inflation keeps accelerating, utterly impervious to the slowdown in hiring, jump in layoffs, pull back in consumer and business spending and the utter collapse in confidence the private sector has about the economic outlook.

Look, we may well see CPI and PPI retreat the rest of the summer months, but the relief will likely be brief. All the economic and geopolitical forces remain in place for prices to rebound again later this year.

United States																
	I 2021	II 2021	III 2021	IV 2021	I 2022	II 2022	III 2022	IV 2022	I 2023	II 2023	III 2023	IV 2023	I 2024	II 2024	III 2024	IV 2024
<b>Real Gross Domestic Product (GDP):</b>																
%	6.3	6.7	2.3	6.9	-1.6	0.3	1.5	1.1	-1.1	-0.2	1.9	2.3	2.1	3.3	2.4	2.8
<b>Personal Consumption Expenditures:</b>																
PCE %	11.4	12.0	2.0	2.5	1.8	1.9	1.8	2.4	-0.9	1.4	2.6	2.4	2.7	3.8	2.7	2.2
<b>Inflation, end of period, year-over-year:</b>																
CPI %	2.6	5.3	5.4	7.0	8.5	9.1	8.0	6.9	6.6	6.5	6.2	4.5	3.0	2.5	2.5	2.5
<b>Unemployment Rate (end of period):</b>																
%	6.0	5.9	4.7	3.9	3.6	3.6	3.9	4.3	4.6	4.9	4.9	5.2	5.0	4.5	3.9	3.6
<b>Non-farm Payrolls, monthly avg. thousand:</b>																
	513	615	651	365	562	375	290	195	190	190	210	255	275	310	315	325
<b>Treasury 10-yr Note Yield % (end of period):</b>																
	1.75	1.44	1.52	1.51	2.32	2.97	2.90	2.80	2.75	2.80	3.05	3.07	3.07	3.10	3.15	3.20
<b>Federal funds rate % (end of period):</b>																
	0.13	0.13	0.13	0.13	0.38	1.63	2.88	3.13	3.13	3.13	2.88	2.63	2.38	2.38	2.38	2.38

## GDP Growth - Global Economy - Year over Year

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
US	2.6	1.6	2.2	1.8	2.3	2.7	1.7	2.3	2.9	2.3	-3.4	5.7	0.7	1.0	2.6
Eurozone	1.7	1.4	-0.9	-0.2	1.4	2.1	1.9	2.5	1.9	1.2	-6.7	5.2	1.3	1.5	2.5
United Kingdom	1.7	0.7	0.3	1.8	2.9	2.2	1.9	1.9	1.3	1.5	-9.8	7.5	2.5	1.0	2.0
Japan	4.6	-0.4	1.6	1.5	-0.1	1.1	0.5	1.7	0.6	-0.2	-4.5	1.7	2.1	2.0	1.9
Canada	3.1	3.1	1.8	2.3	2.9	0.7	1.0	3.2	2.0	1.6	-5.3	4.5	2.5	2.3	2.8
India	8.4	8.6	6.7	4.9	7.4	8.0	8.1	7.2	6.8	4.8	-7.5	9.2	6.7	6.5	7.2
China	10.5	9.5	7.8	7.7	7.3	6.9	6.7	6.8	6.6	6.1	2.2	8.1	4.3	5.2	5.5
Brazil	7.5	2.7	0.9	2.3	0.1	-3.5	-3.5	1.2	1.2	1.1	-3.9	4.5	0.9	2.1	2.4
Mexico	5.2	4.0	3.9	1.4	2.3	2.7	2.7	2.4	2.1	-0.1	-8.5	5.0	1.8	1.5	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	4.7	2.8	2.4	2.9
Russia	4.0	4.3	3.4	1.3	0.6	-2.8	-0.2	1.6	2.5	1.2	-2.9	4.5	-9.0	-2.0	1.9
World	4.2	3.1	2.5	2.6	2.8	2.8	2.6	3.4	3.2	2.7	-3.1	5.9	2.8	3.1	4.4

## Key Currency Values

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016	End 2017	End 2018	End 2019	End 2020	End 2021	End 2022	End 2023	End 2024
USD/Yen	91	93	81	77	87	105	119	120	117	113	110	109	104	115	133	118	108
Euro/USD	1.40	1.43	1.34	1.29	1.32	1.37	1.21	1.09	1.05	1.20	1.14	1.12	1.23	1.17	1.05	1.16	1.22

## Oil (Brent spot) & Gasoline (Average retail unleaded, \$)

	End 2008	End 2009	End 2010	End 2011	End 2012	End 2013	End 2014	End 2015	End 2016	End 2017	End 2018	End 2019	End 2020	End 2021	End 2022	End 2023	End 2024
Crude oil per barrel	46	78	95	107	111	111	58	38	49	67	54	67	52	78	109	87	76
Gasoline	1.61	2.57	3.00	3.27	3.30	3.32	2.26	2.00	2.31	2.47	2.26	2.58	2.25	2.29	4.50	4.05	3.45

## Key Economic & Geopolitical Projections for 2022 & 2023

• Latest revision: July 11, 2022

CE

PROBABILITY	U.S.
HIGH	Forecast assumption: Russia ends war in Ukraine early 2023. Oil and natural gas prices to remain elevated in 2022.
HIGH	Fed's aggressive rate hikes doom economy to stagflation in 2H. Economic activity weakens, but inflation remains high.
Moderate	Odds of US recession 50% this year, but jumps to 80% in 2023 as higher rates choke off economic activity;
Moderate	Treasury 10-yr. yields hovers between 2.90% to 3.35% the next 12- 18 months as risk of recession looms.
HIGH	Lethal threat of Covid virus recedes. But a wave of reinfections from subvariants seen for fall/winter 2022- 2023.
HIGH	Supply chain bottlenecks to ease at ports in 2H, though some goods will lag others in terms of their availability.
	FOREIGN
HIGH	Russia's economy is cratering. GDP to contract 8% - 12% in 2022, and another 3% in 2023.
HIGH	Regime change in Russia to be a prerequisite before the country can rejoin the international community.
HIGH	Beijing fortifies naval presence in South China Sea and Taiwan Strait to counter US military support of Taiwan.
HIGH	China's 2022 growth decelerates to 4.0% - 4.5% as Covid lockdowns and property market shakeout take their toll.
Moderate	A cyber World War is underway; Prepare for periodic disruptions to global power grids and communications.
Moderate	Iran can now produce enough fissile material for a nuclear bomb. Israel is unlikely to sit by.
HIGH	Recession odds in Eurozone jumps to 80% in late 2022/2023 as the ECB lifts rates and energy prices surge.

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