Economic Conditions and Outlook

December 1, 2022 – International Business Circle - Arvada, CO

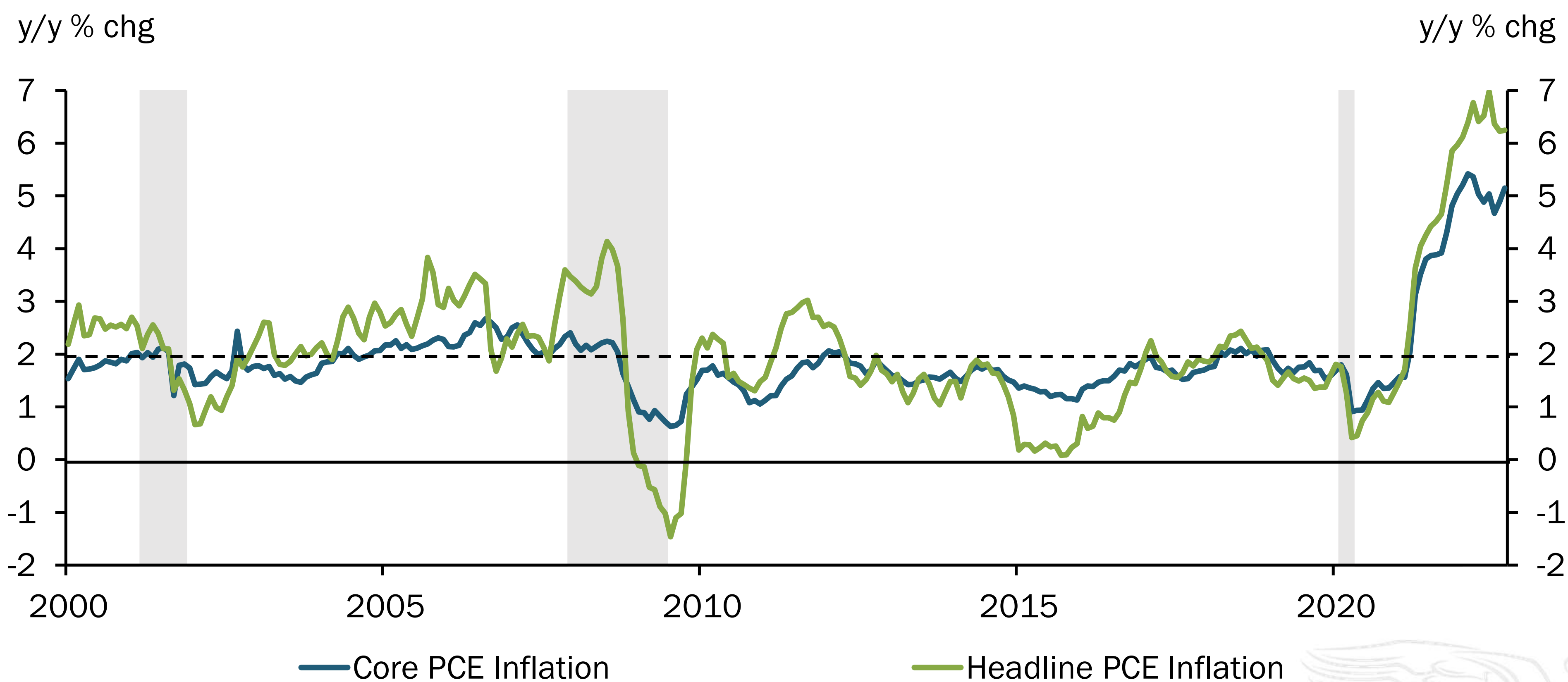
Nicholas Sly

Vice President, Economist and Denver Branch Executive

Overview

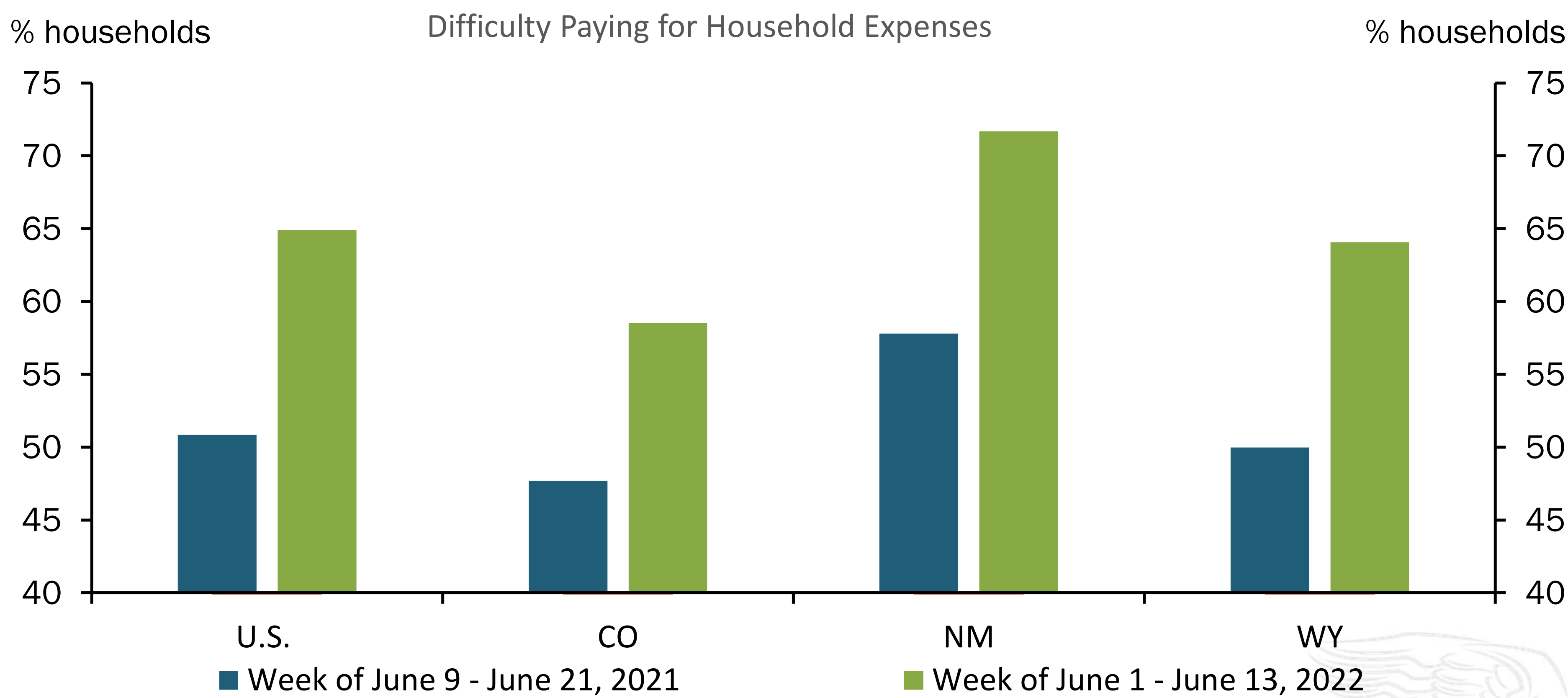
- Against a backdrop of elevated inflation levels and associated monetary policy responses, we have seen several developments in the regional economy over recent months
    - Household balance sheets began the year at historically strong levels, but more households are reporting difficulty meeting regular expenses
    - Reported growth among regional businesses was at record highs earlier this spring, but forward-looking indicators point to a softening growth outlook
    - Labor markets are historically tight, yet worker quit rates have just begun to decline

Inflation remains well-above historic norms and the Fed's 2 percent target



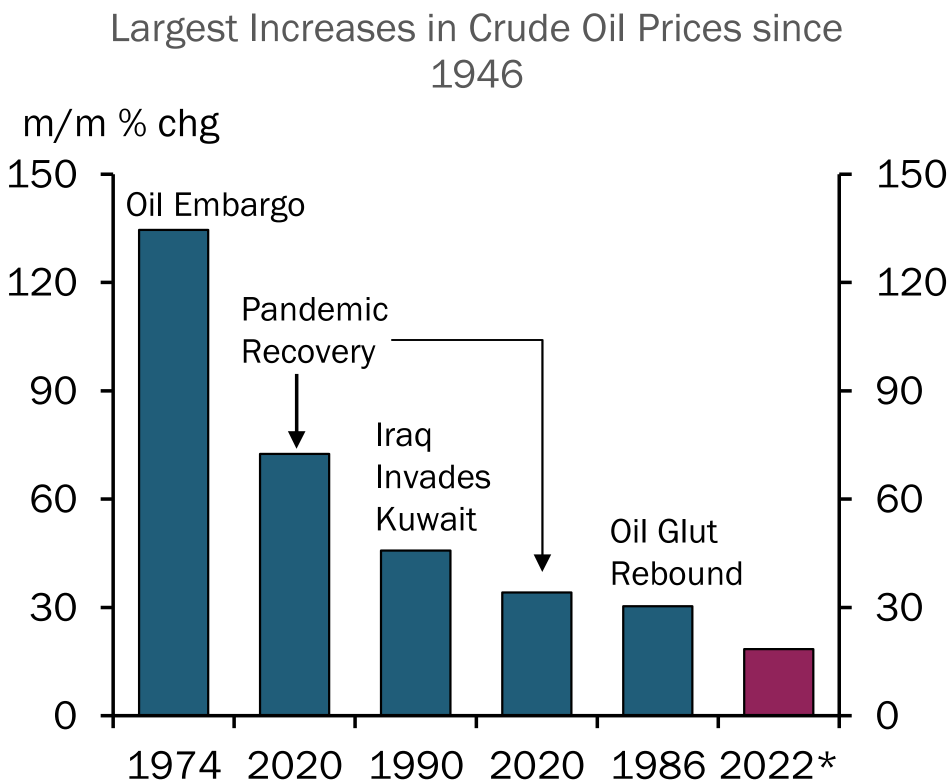
Source: BEA, Haver Analytics
Note: Grey bars indicate recession shading

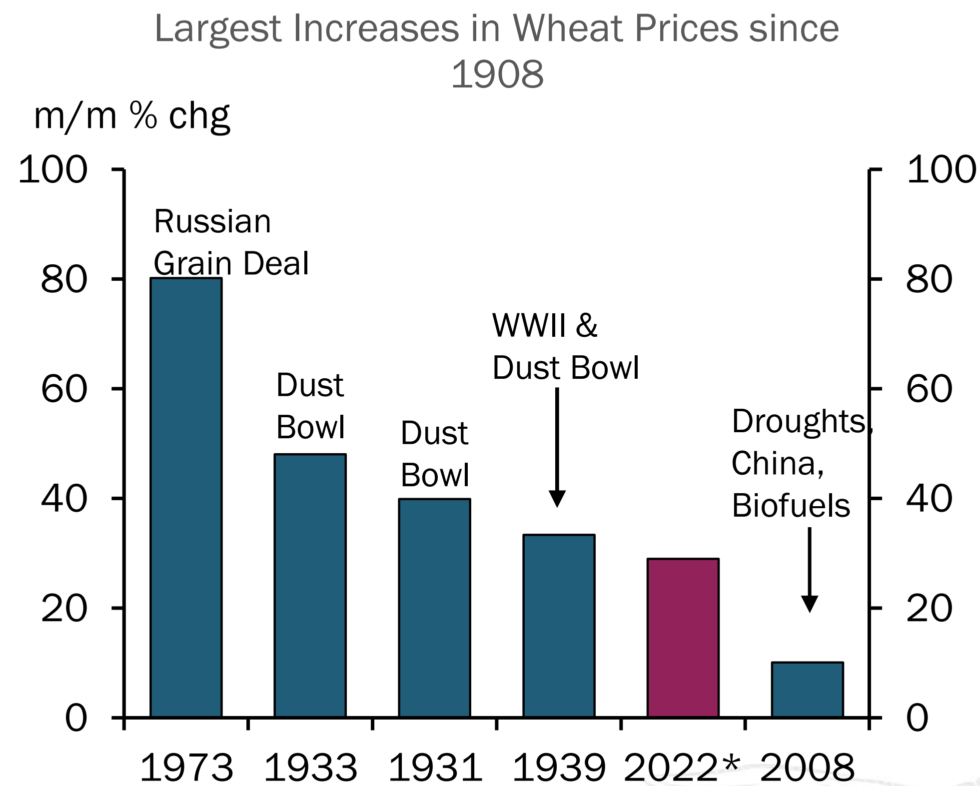
Households’ ability to pay for usual expenses has deteriorated over the past year



Source: U.S. Census Bureau

Increases in commodity prices earlier this year were historically large

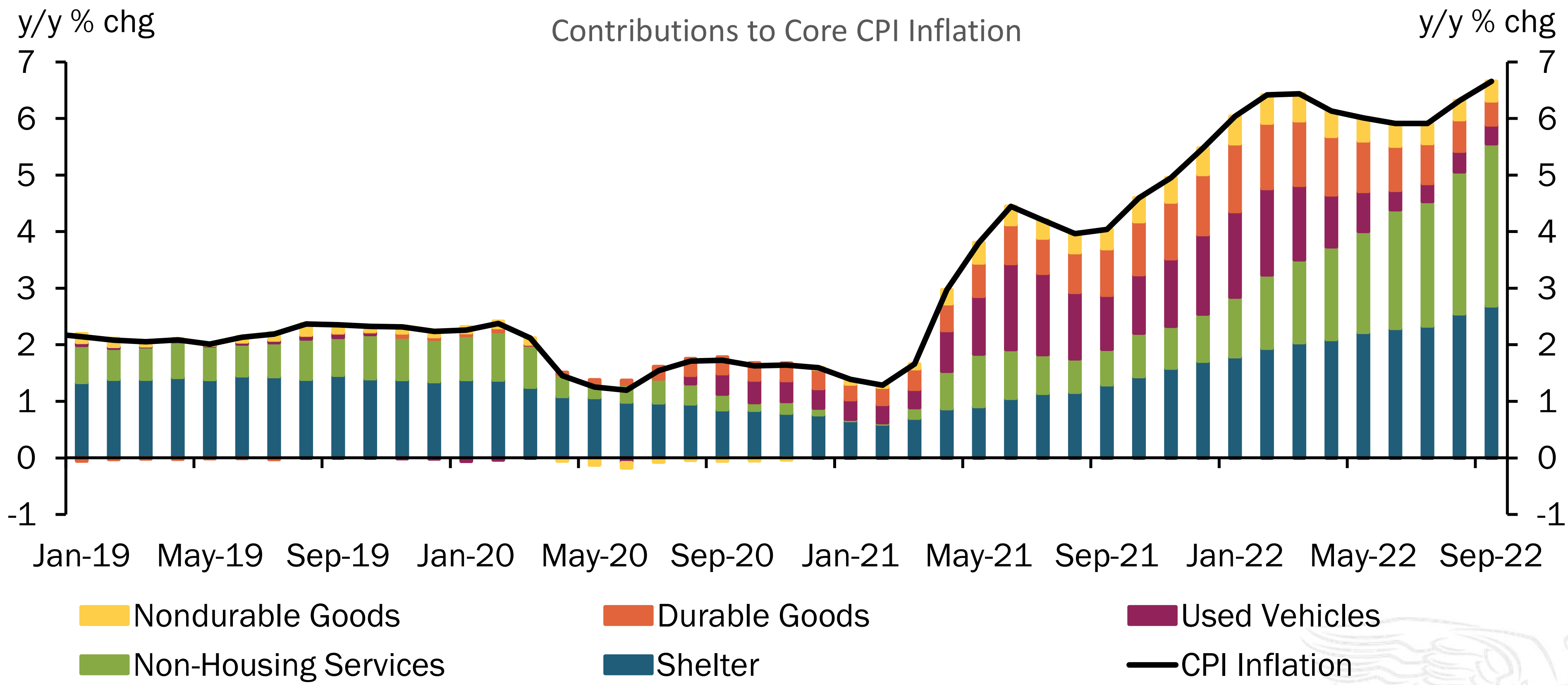




* The change in oil prices from February 2022 to March 2022 was the 16th largest on record, and the change in wheat prices in March 2022 was the 7th largest on record, after the Russian Grain Deal and Dust Bowl/WWII period (three months in 1933 were in the top six, and two of those months are excluded for brevity).

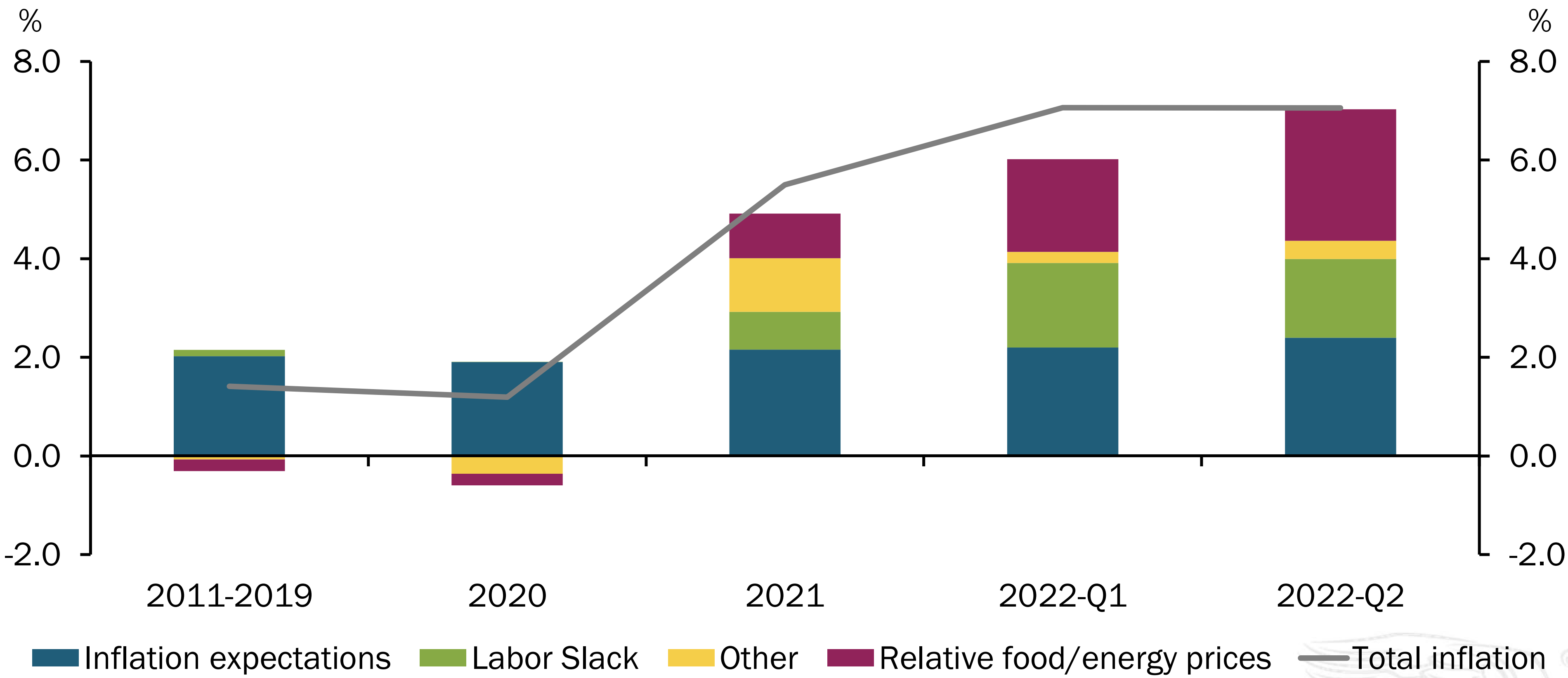
Source: The Wall Street Journal, Haver Analytics

Over the past year, the drivers of inflation rotated back toward services, with growth in goods prices softening over the last several months



Source: BLS, Haver Analytics

Inflation pressures reflect the imbalances of persistently strong demand relative to ongoing shortfalls in supply

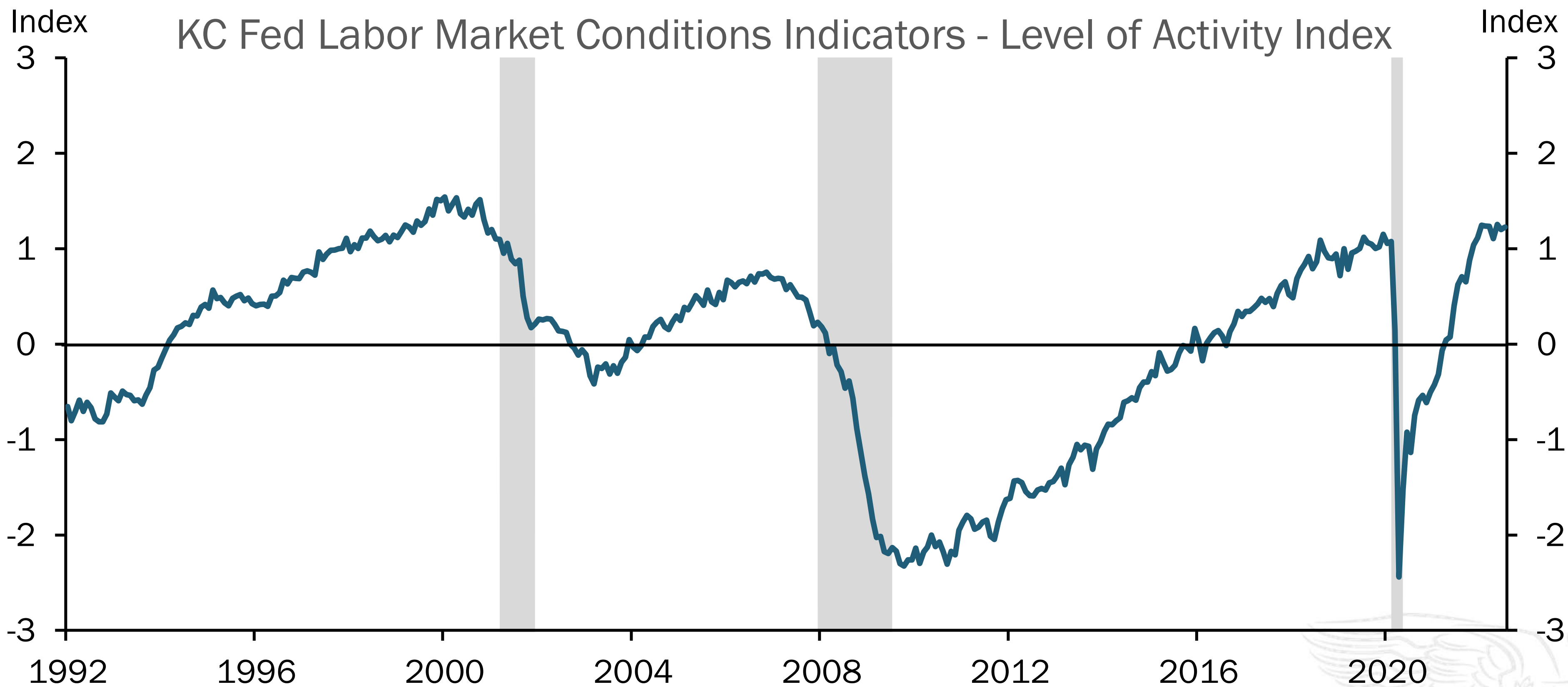


Sources: Staff, BEA, BLS, CBO, SPF

Note: Annualized PCE Inflation, total and portion attributable to specific factors

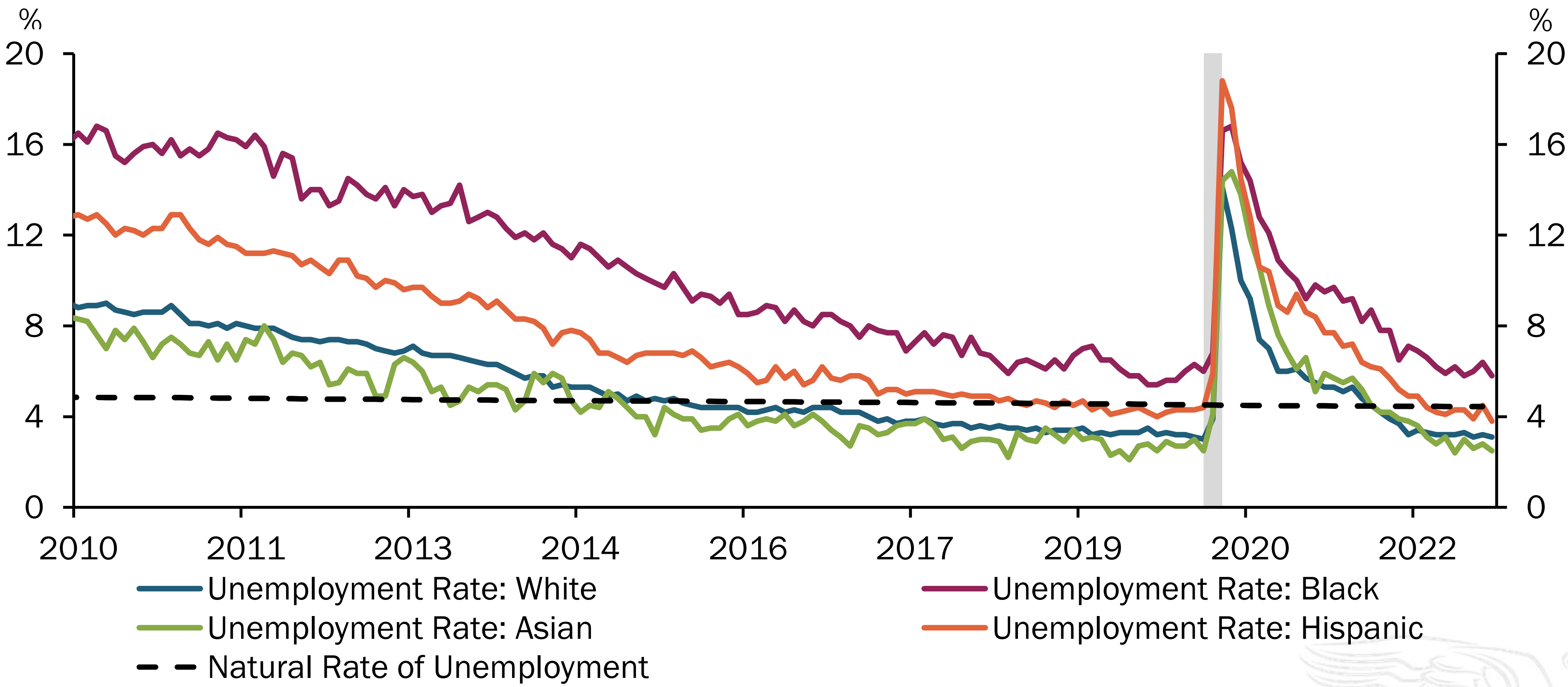
Indicators of demand and supply imbalances

Labor market conditions are historically tight



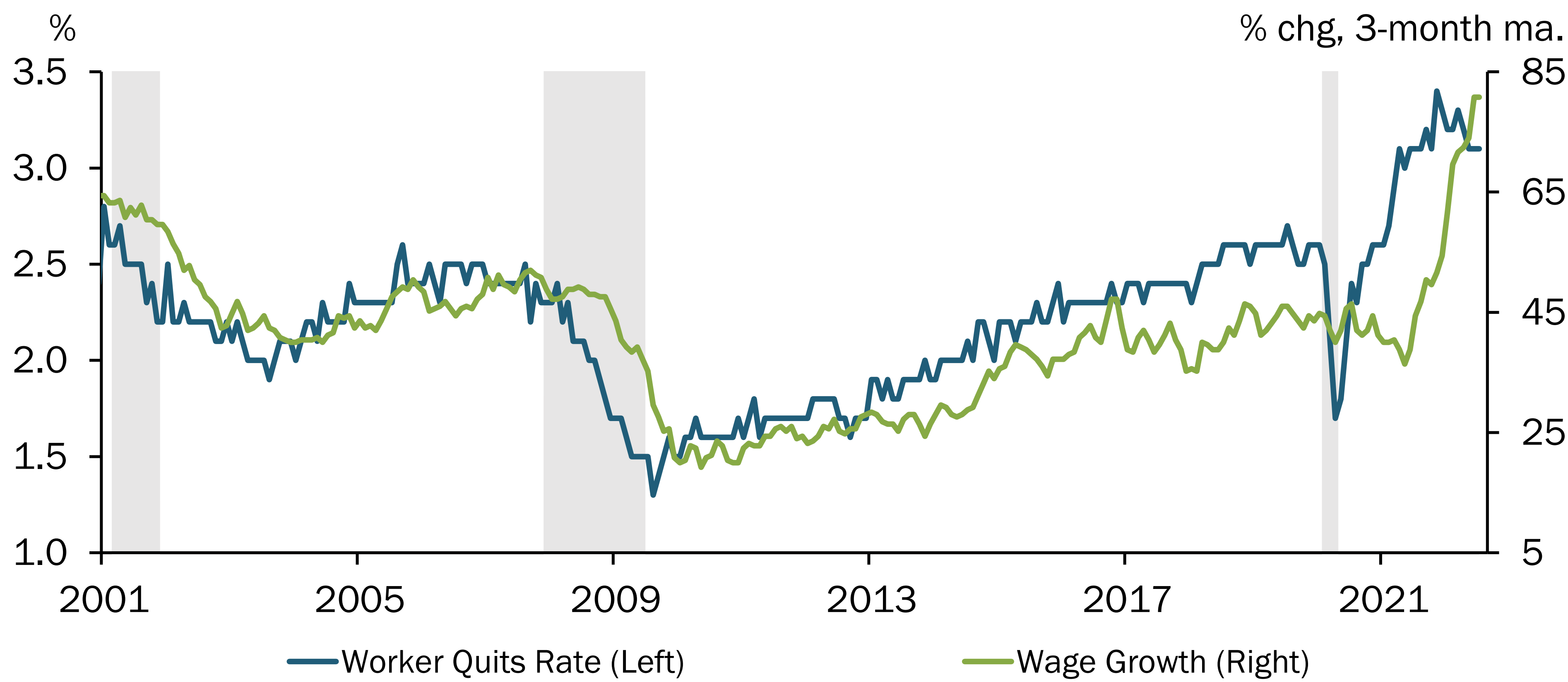
Sources: KCFRB

Unemployment rates are at or below pre-pandemic lows



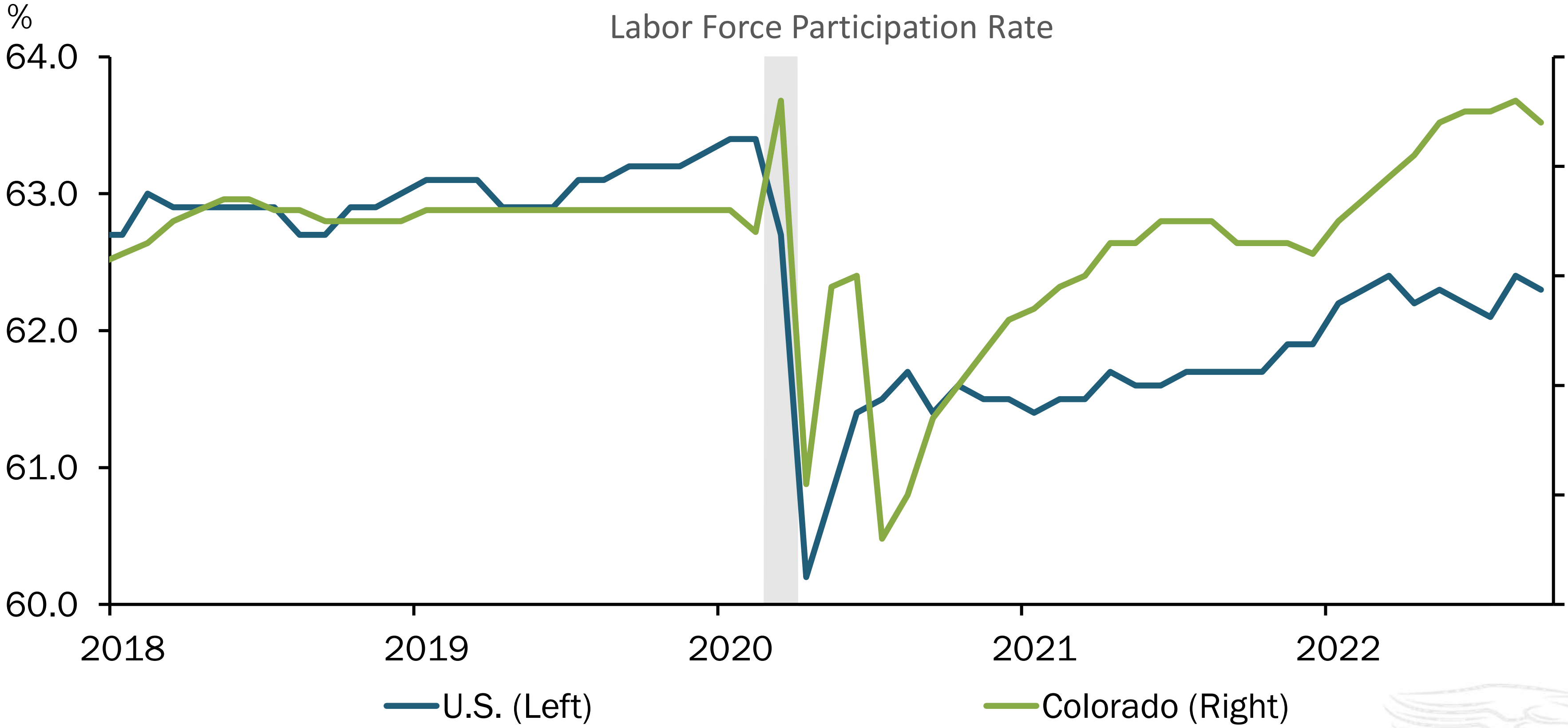
Source: BLS, Haver Analytics
Note: Grey bars indicate recession shading

Workers left their jobs at elevated rates over the past 18 months, further tightening the labor market and driving broad-based wage growth



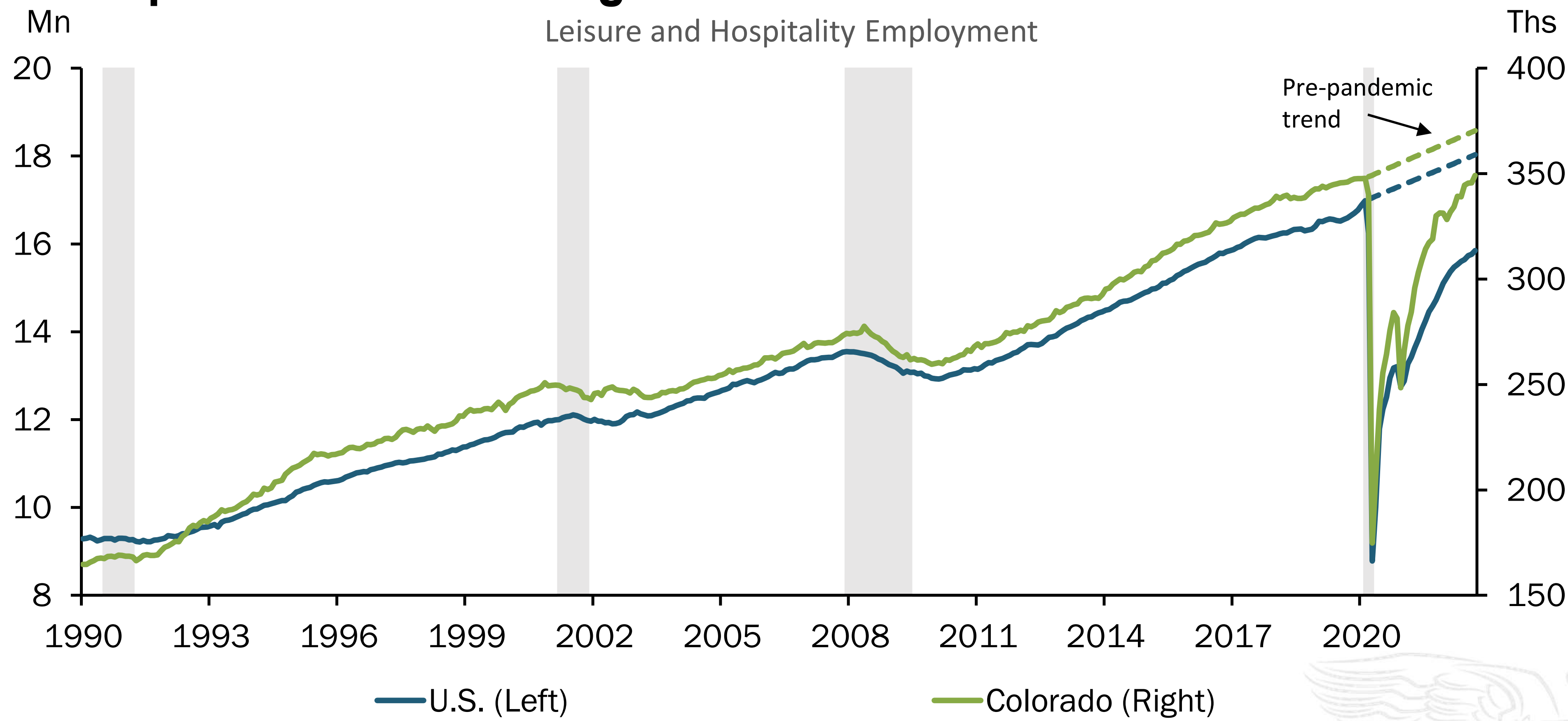
Source: BLS, Haver Analytics
Note: Grey bars indicate recession shading

While labor supply remains constrained nationally



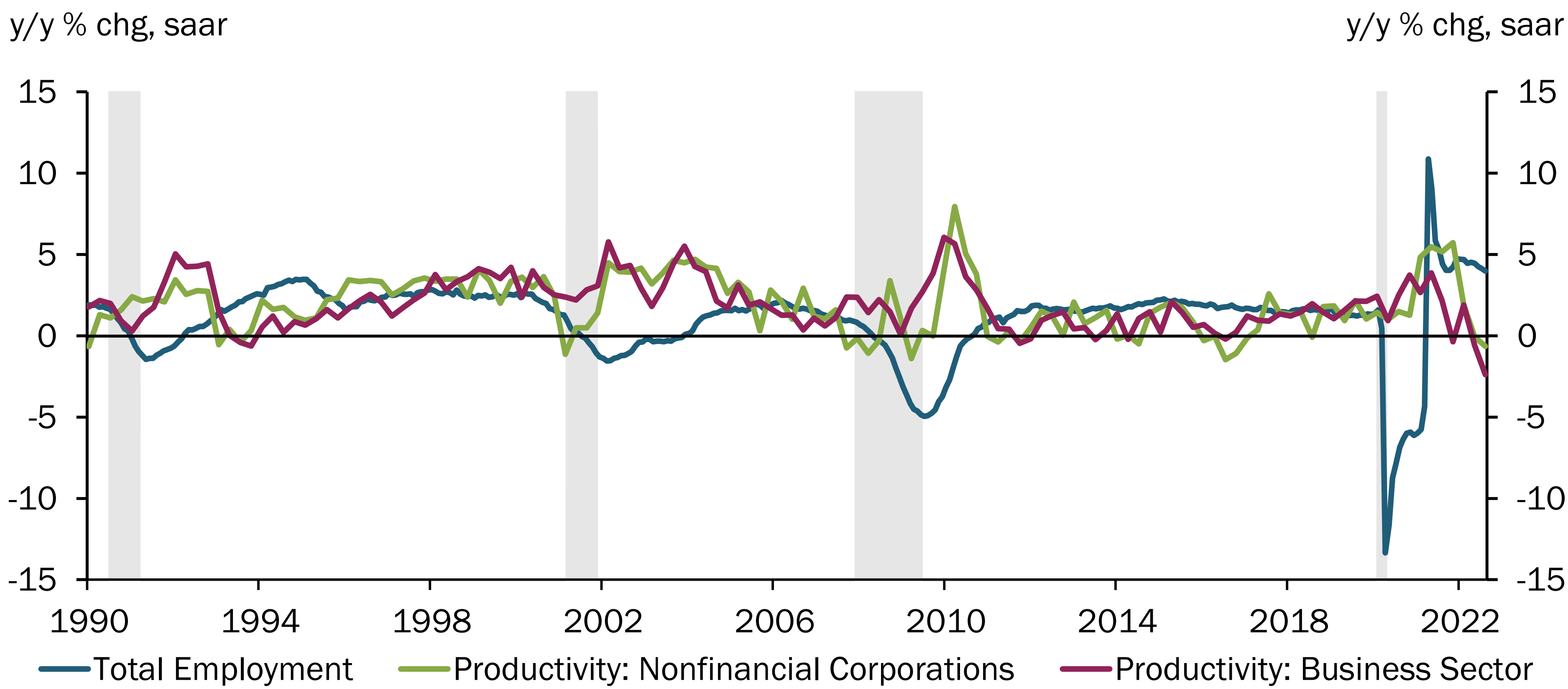
Source: BLS, Haver Analytics
Note: Grey bars indicate recession shading

Employment shortfalls in leisure and hospitality remain acute, adding to cost pressures in that segment of the service sector



Source: BLS, Haver Analytics
Note: Grey bars indicate recession shading

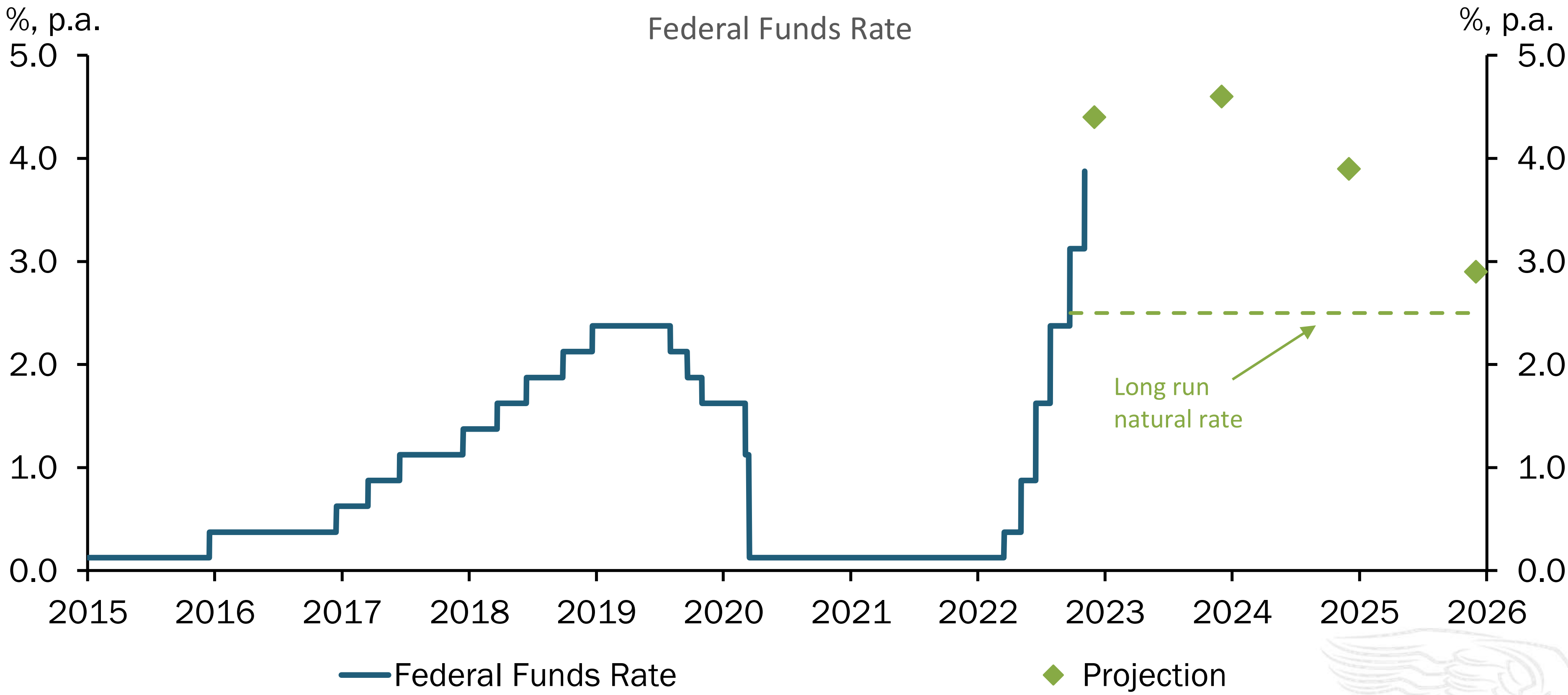
Dismal labor productivity has exacerbated supply constraints, but productivity tends to be subdued during periods of rapid job growth



Sources: BLS/ Haver Analytics

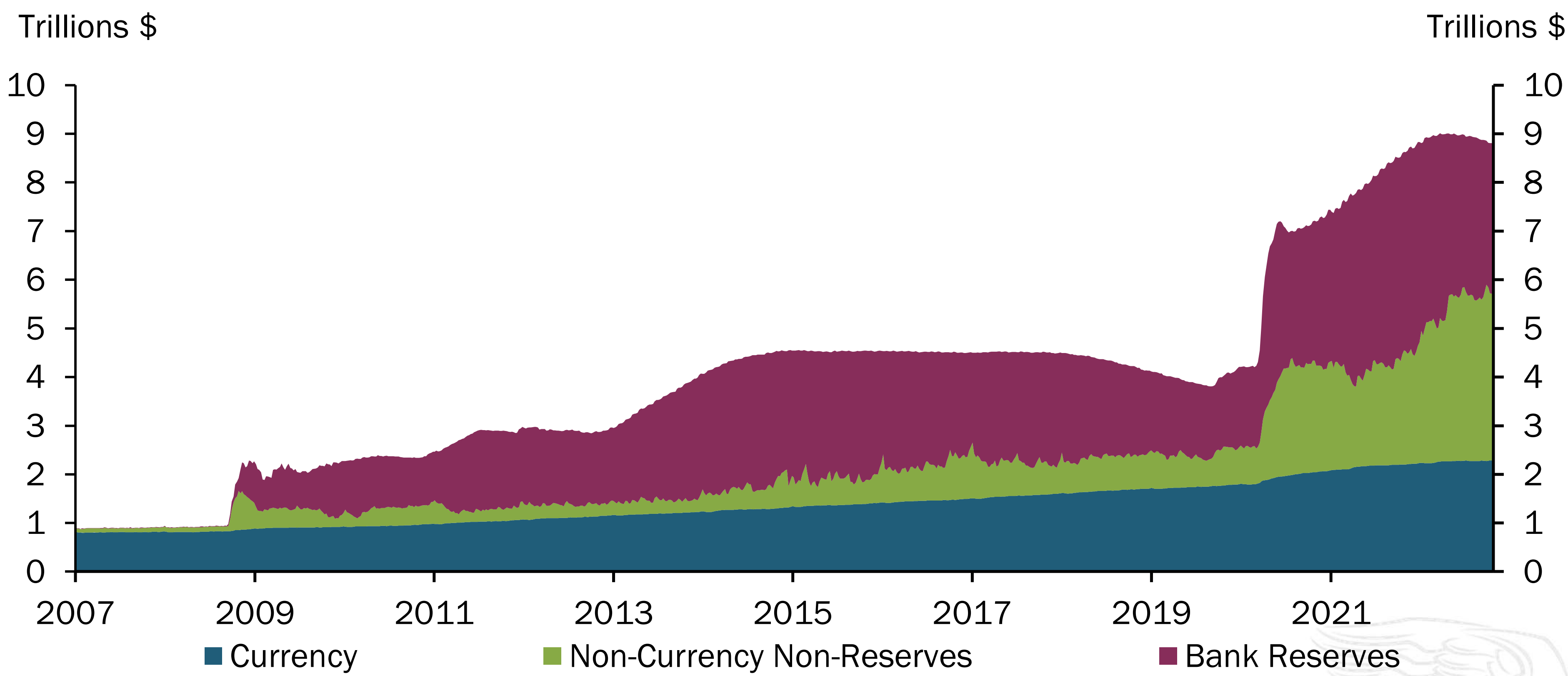
Monetary policy adjustments transmission to the real economy

The Federal Reserve is moving interest rates further into a restrictive stance of monetary policy to restore price stability



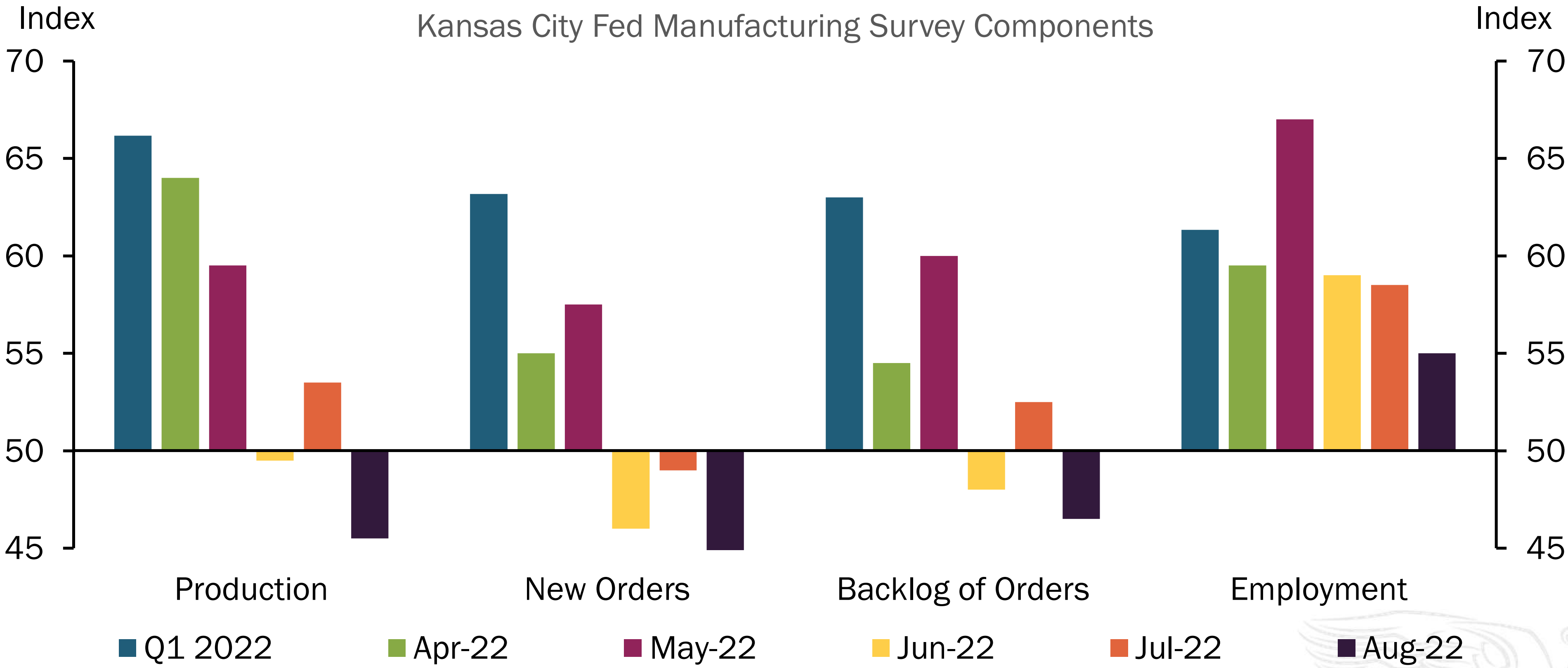
Sources: Federal Reserve Board, Summary of Economic Projections, Haver Analytics

The Federal Reserve is reducing the size of its balance sheet



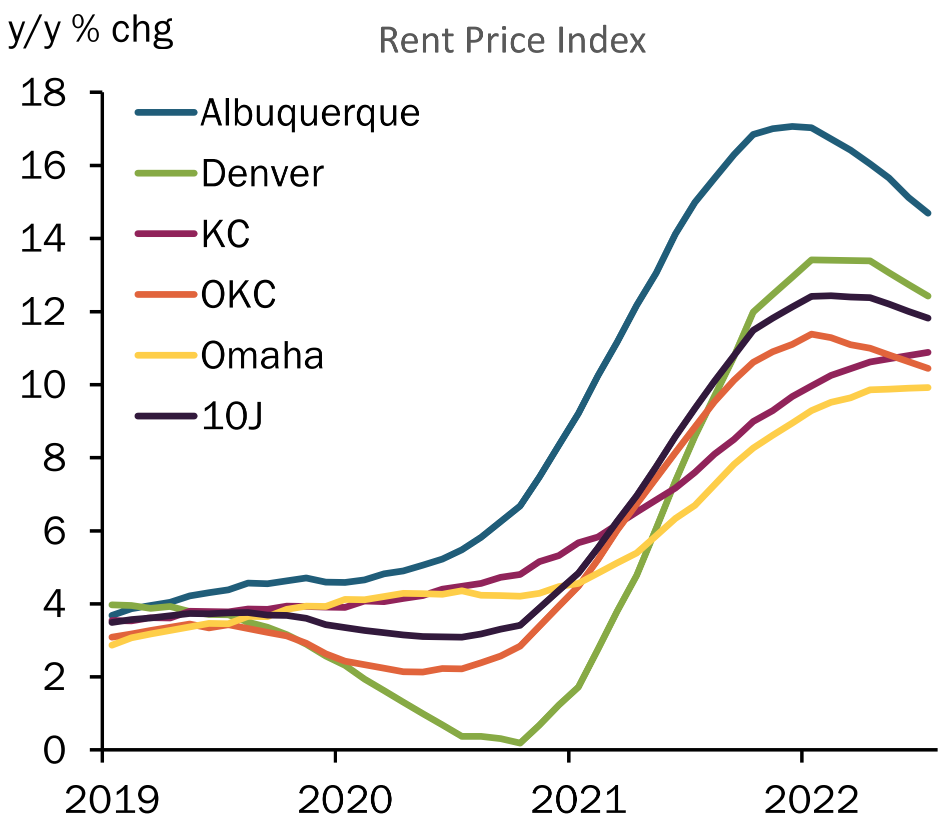
Sources: Federal Reserve Board, Haver Analytics

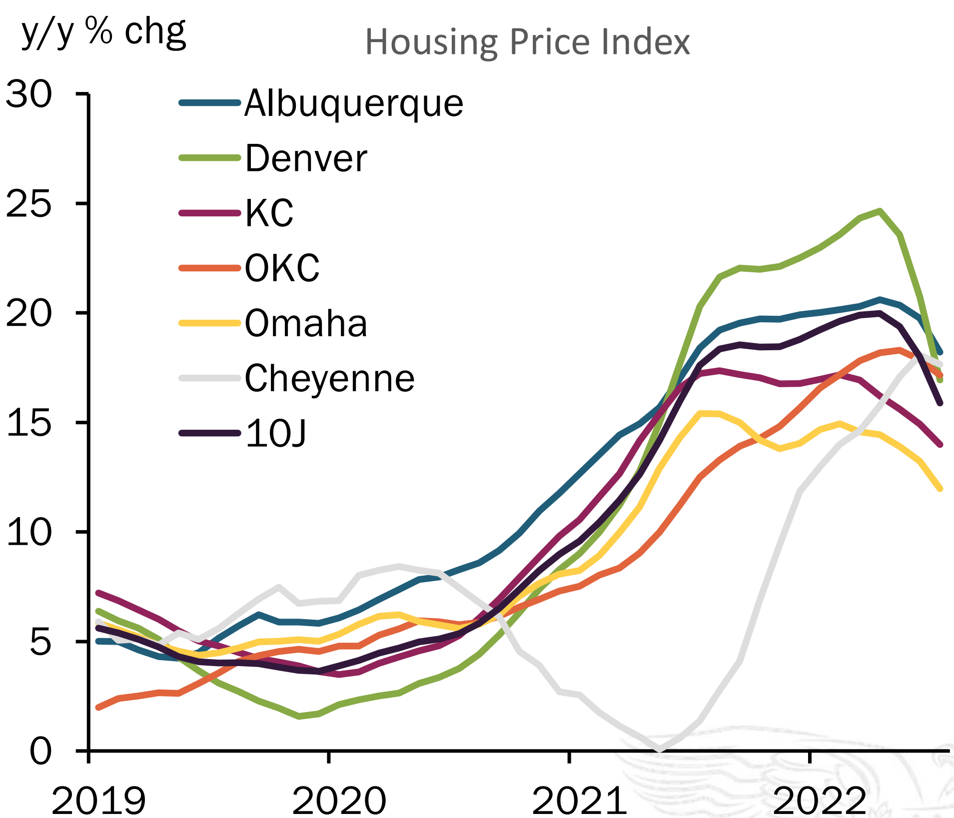
Measures of production across the region point to declining activity, while job growth and labor demand remain healthy



Sources: KC Fed Manufacturing Survey
Note: An index level above 50 indicates the level of activity is increasing.

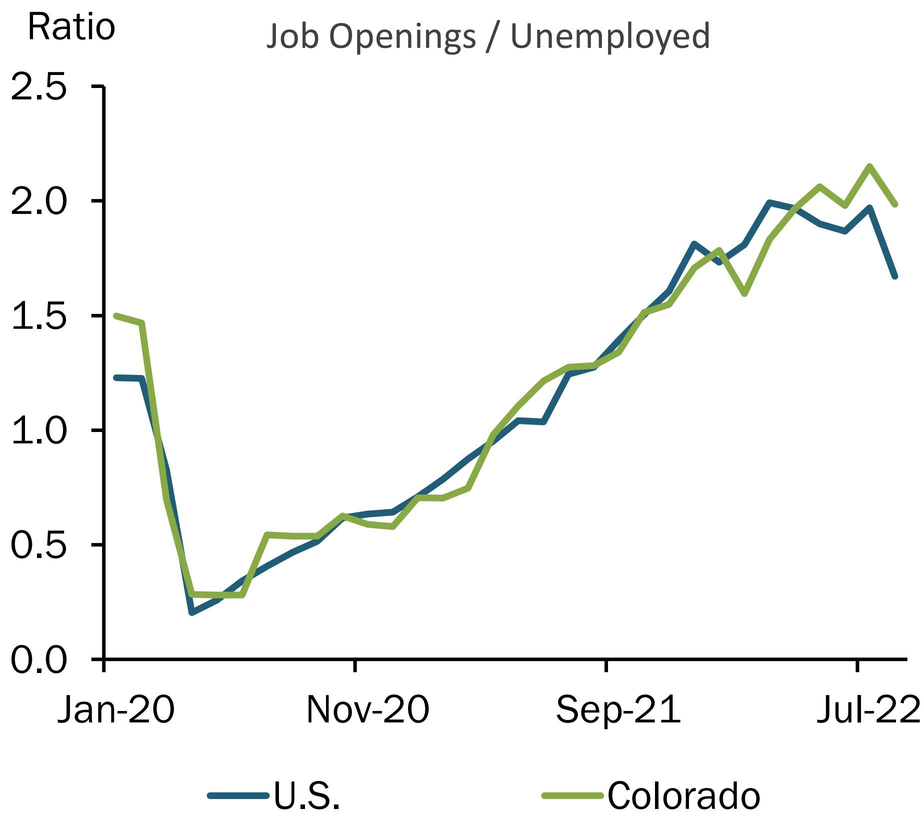
The housing market is cooling as the numbers of existing homes sold and the number of new homes constructed are falling

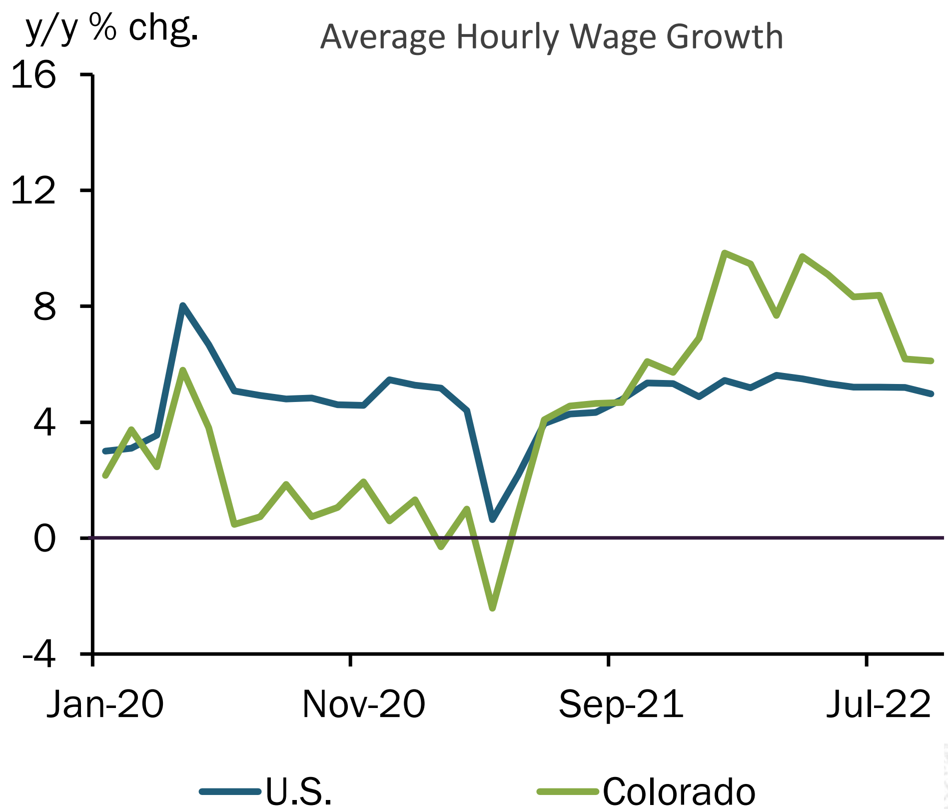




Source: Zillow, Haver Analytics

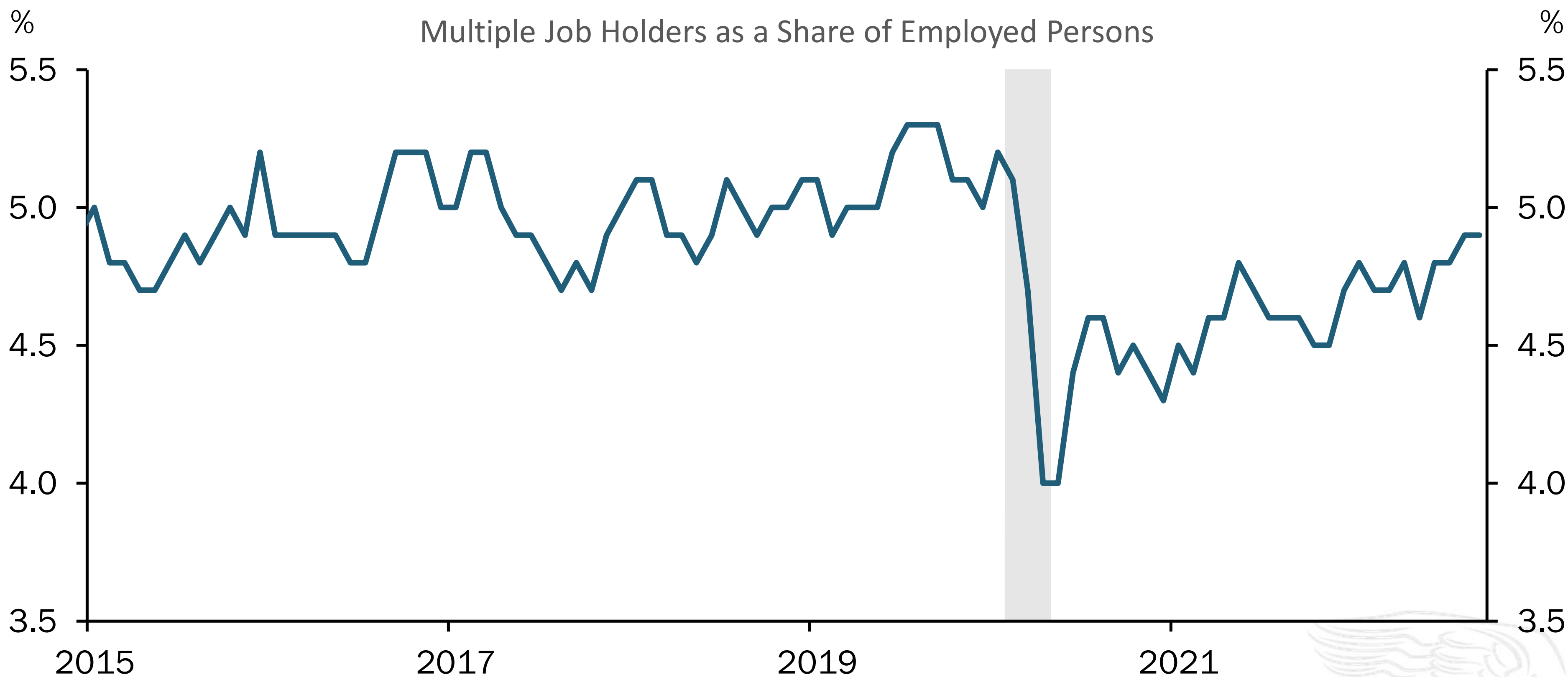
Worker quits rates and job posting rates are starting to soften, but wage growth remains elevated





Source: BLS, Haver Analytics

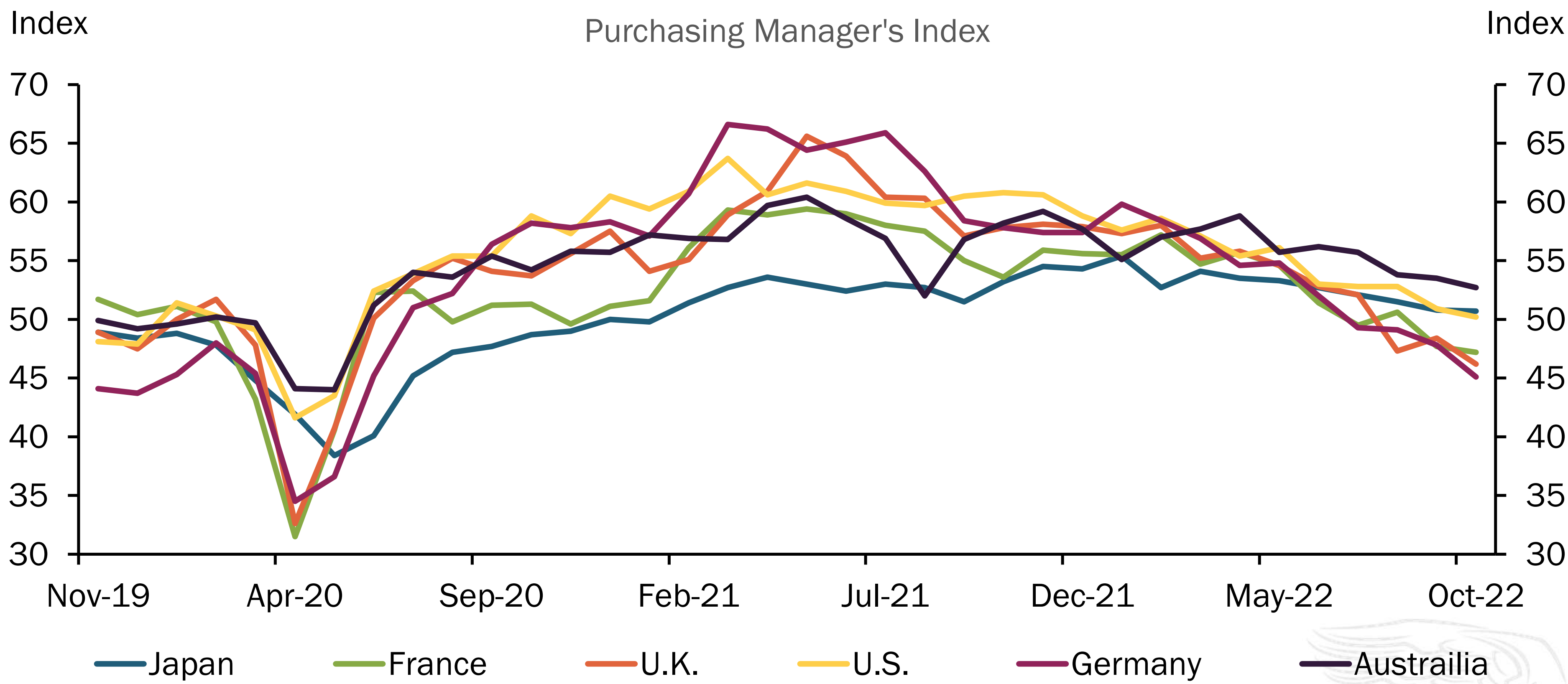
The share of employed individuals with more than one job has increased over the past few months



Source: BLS, FRED
Note: Grey bars indicate recession shading

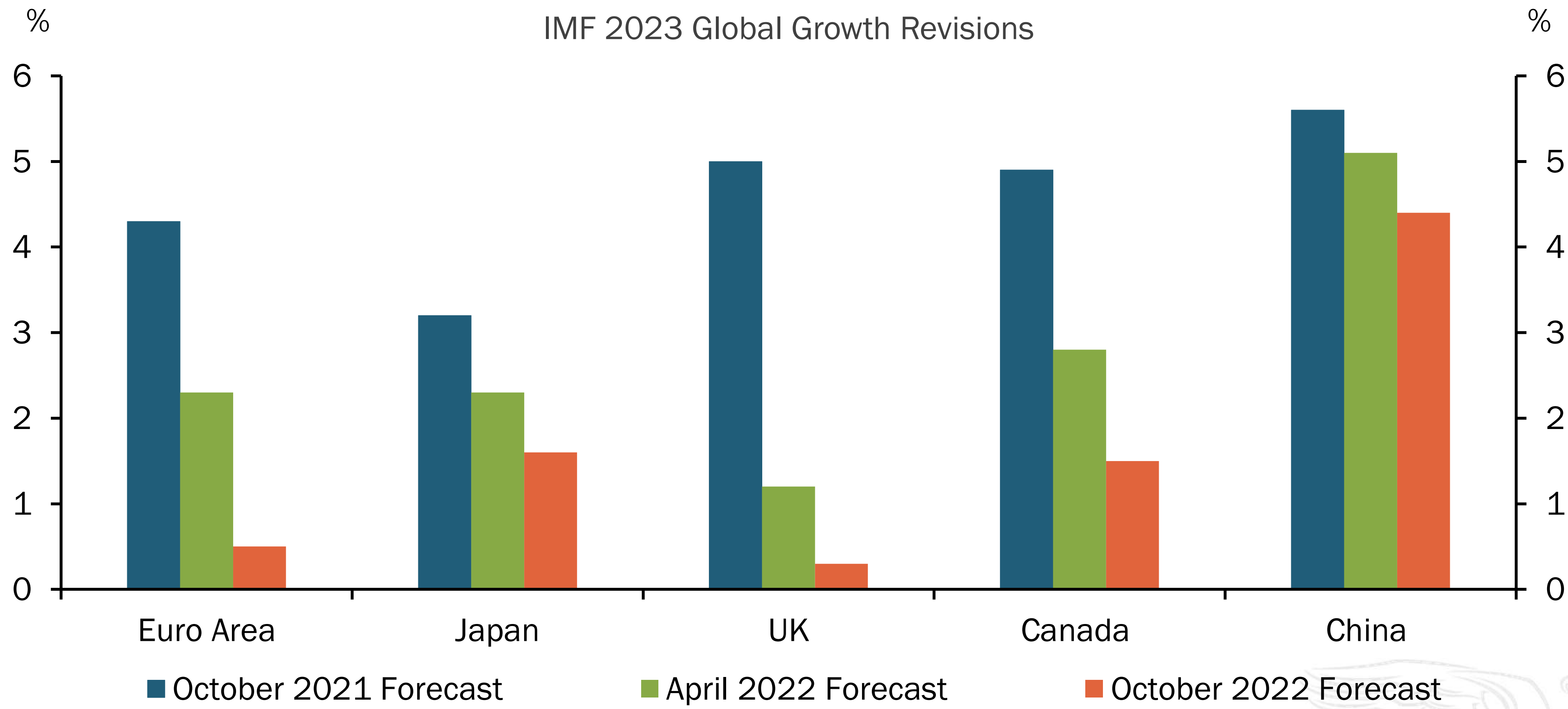
Global risk factors

High energy costs are generating substantial headwinds for global manufacturing activity



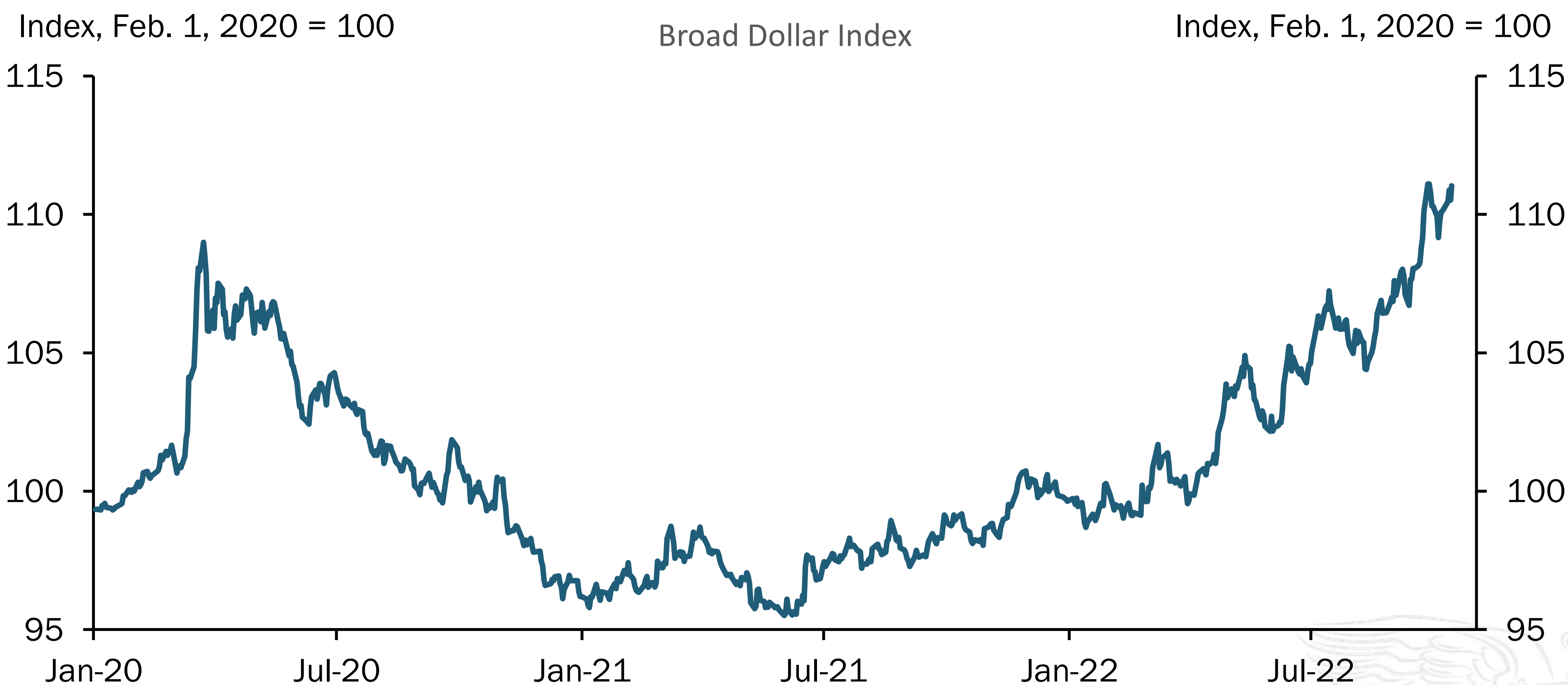
Sources: S&P Global, Bloomberg

Global growth projections continue to deteriorate



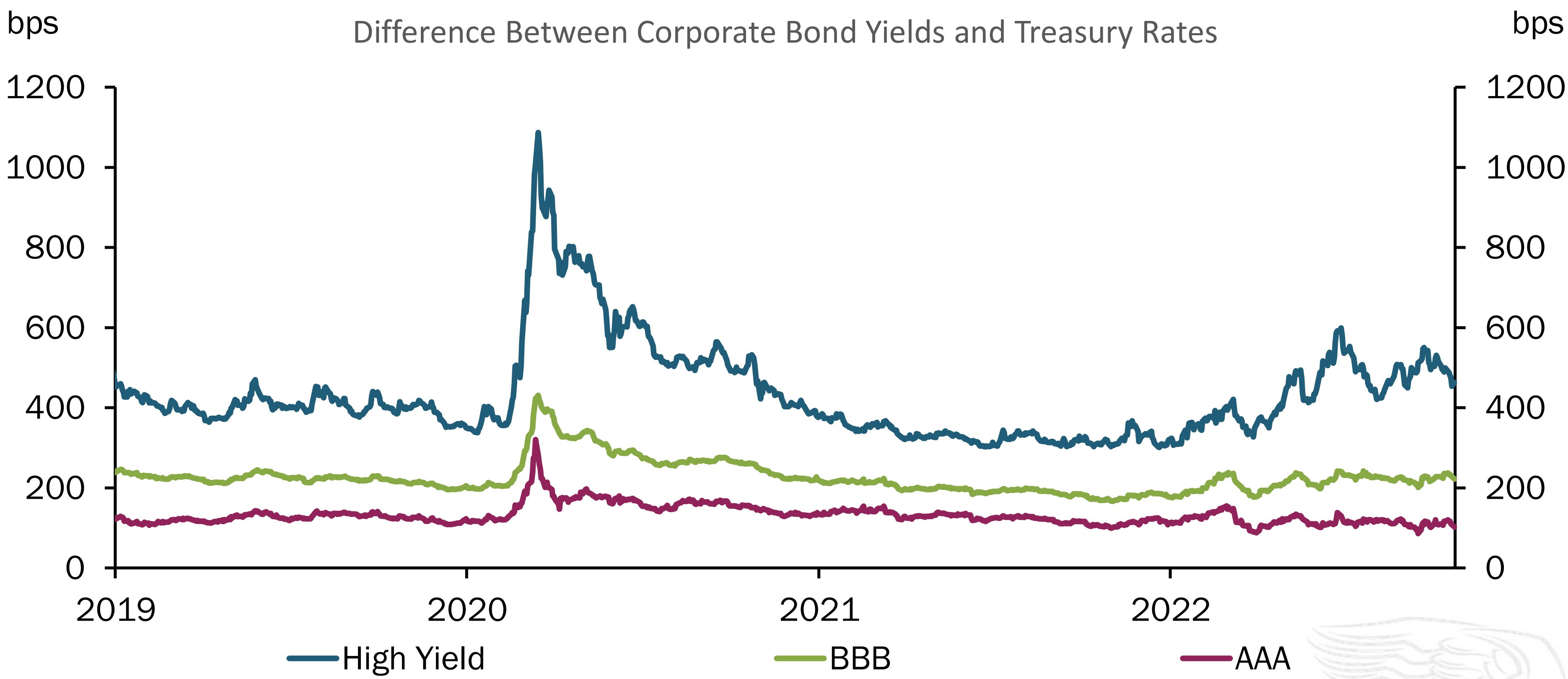
Sources: IMF WEO

Global currencies have weakened against the dollar, further tightening financial conditions



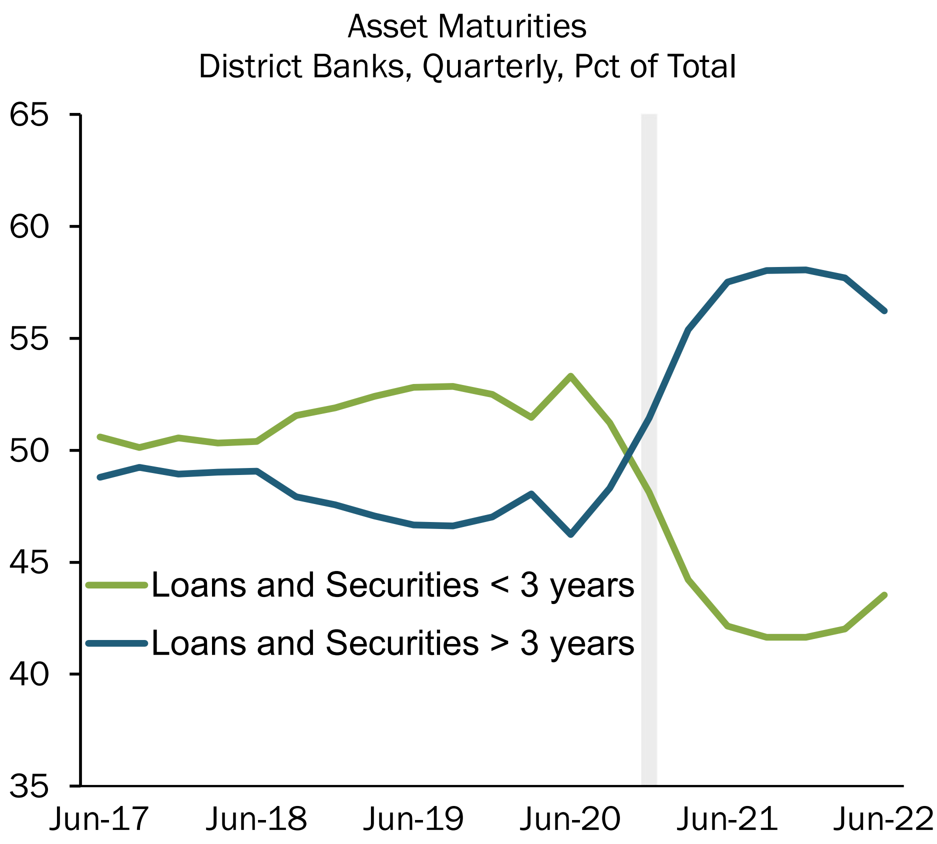
Sources: Federal Reserve Board

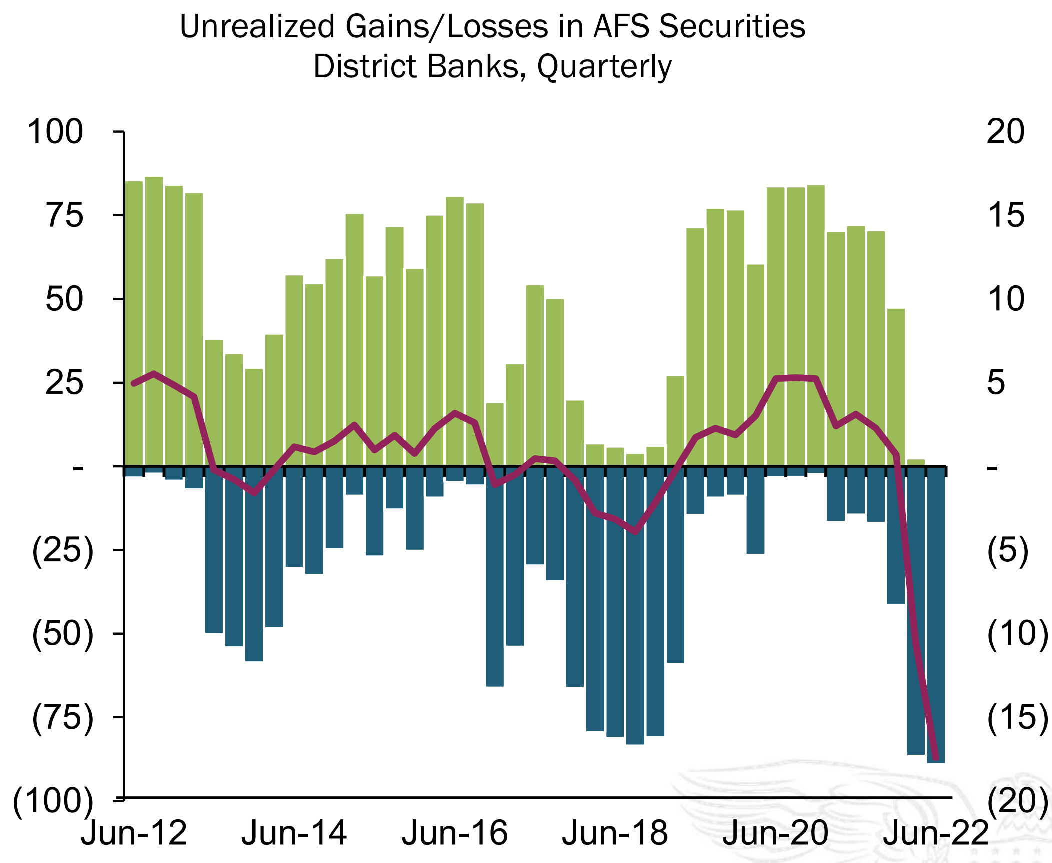
As economic conditions are beginning to change, financial markets are repricing credit risks



Sources: FRED

Prior to tightening of monetary policy, bank had extended the duration of assets on their balance sheets





Sources: Source: Reports of Condition and Income

Looking ahead

- Uncertainty about the near- and medium-term outlooks remains elevated
- Wage growth will likely remain elevated even as labor market conditions have become less tight
- Contacts across the region are reporting varied actions to ‘right-size’ their business.
  - businesses in some sectors have started to reduce their employment to align with cooling demand
- The Federal Reserve has stated that a sustained stance of restrictive policy is likely to be appropriate to restore price stability

https://www.KansasCityFed.org/Speeches