MARC Board of Directors
October 25, 2022

U.S. and KC Economic Forecast

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KC RISING
OUR SHARED VISION FOR REGIONAL PROSPERITY

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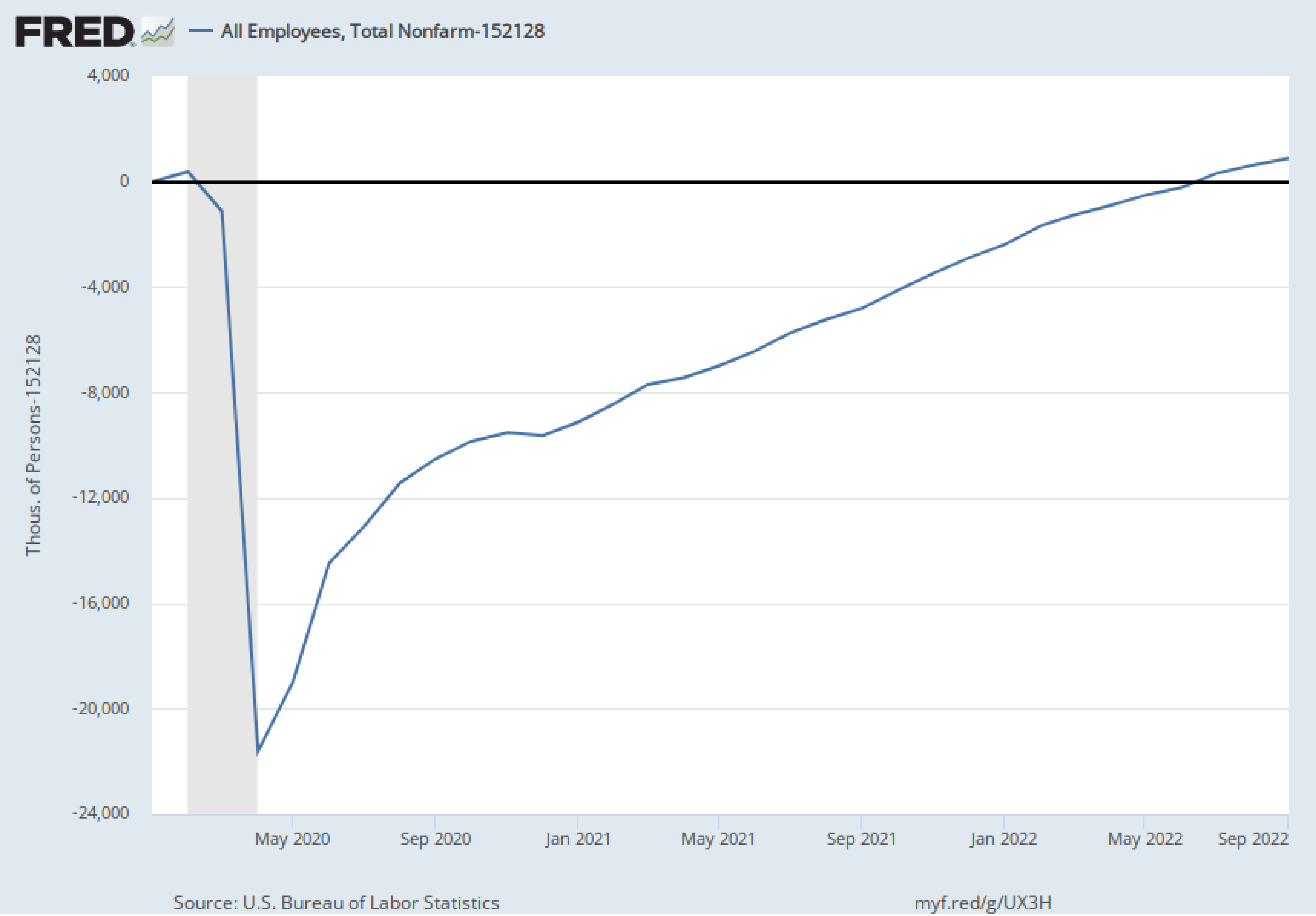
U.S. Economic Situation and Forecast

Photo by NASA on Unsplash

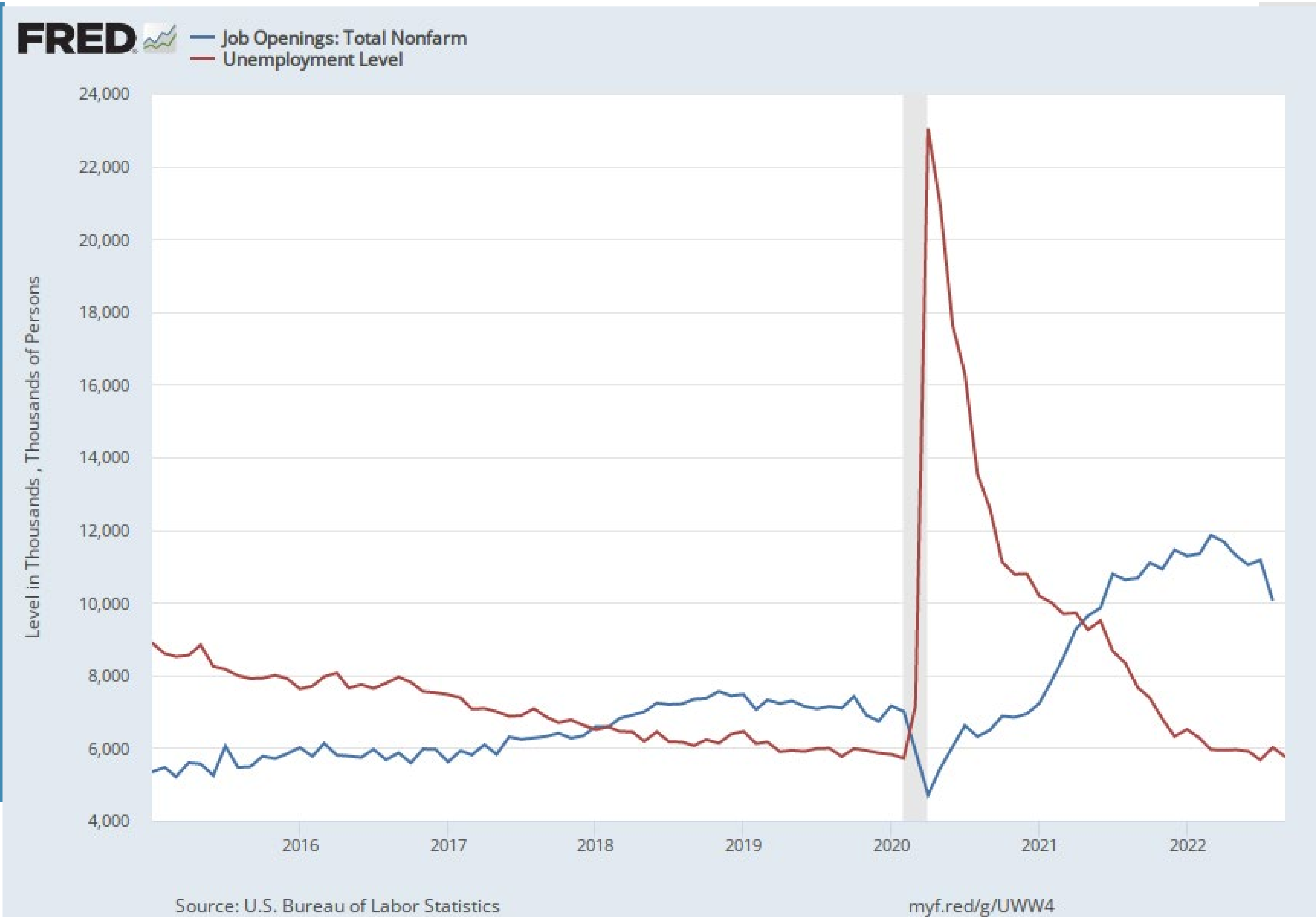
U.S. jobs reached their pre-pandemic peak in August 2022. Monthly payroll employment has slowed from 537,000 in July to 263,000 in September. This is still more than twice as much as the working age population grows each month, and so reflects an economy pulling more people into the labor force.



Source: BLS

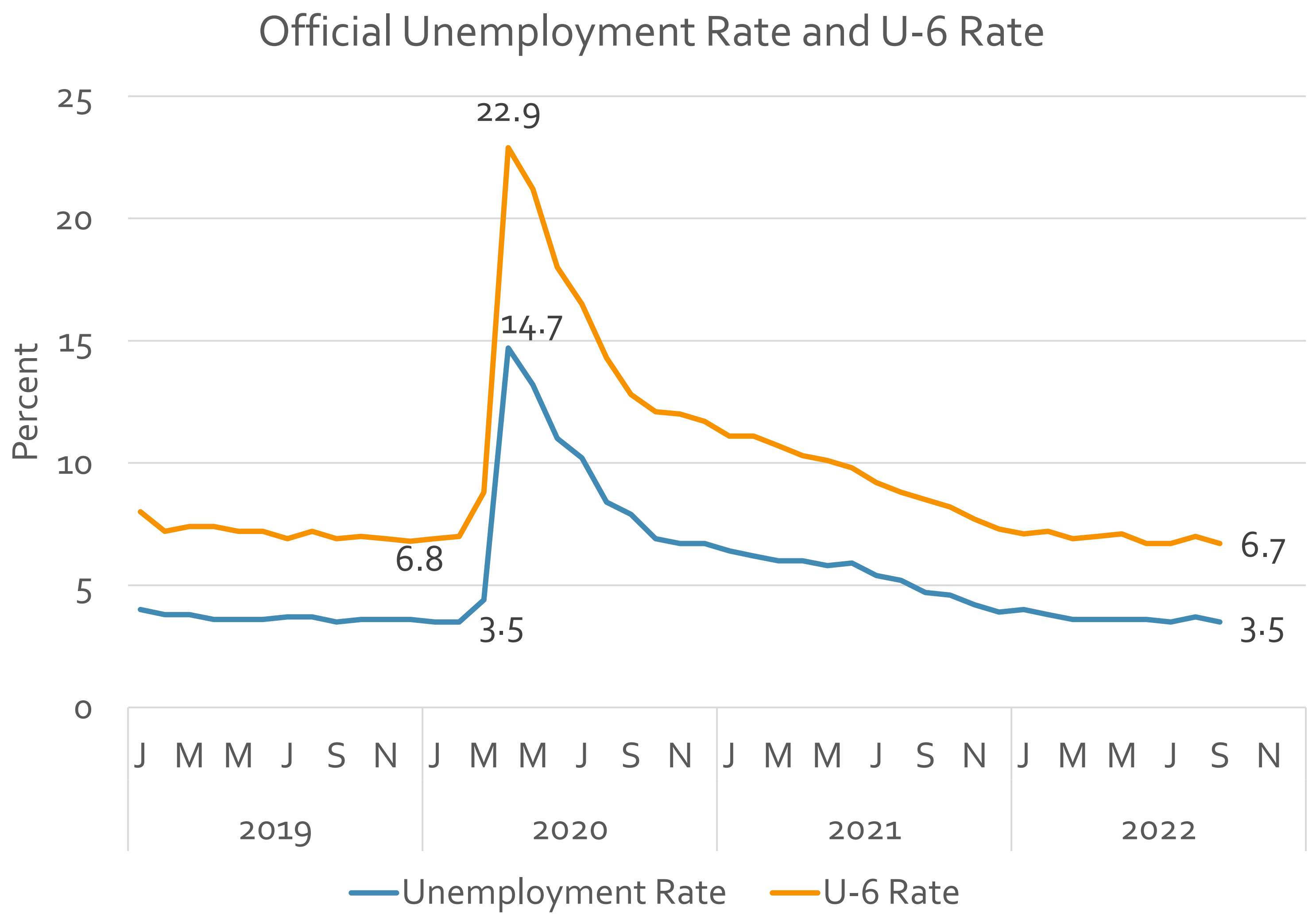
U.S. Job Postings vs. Unemployed Persons, 2015-2022

Further evidence that the job market is cooling comes from recent declines in the numbers of job postings. Nonetheless, there are 1.6 jobs for every unemployed person in the country, indicative of a job market that is still extremely tight.



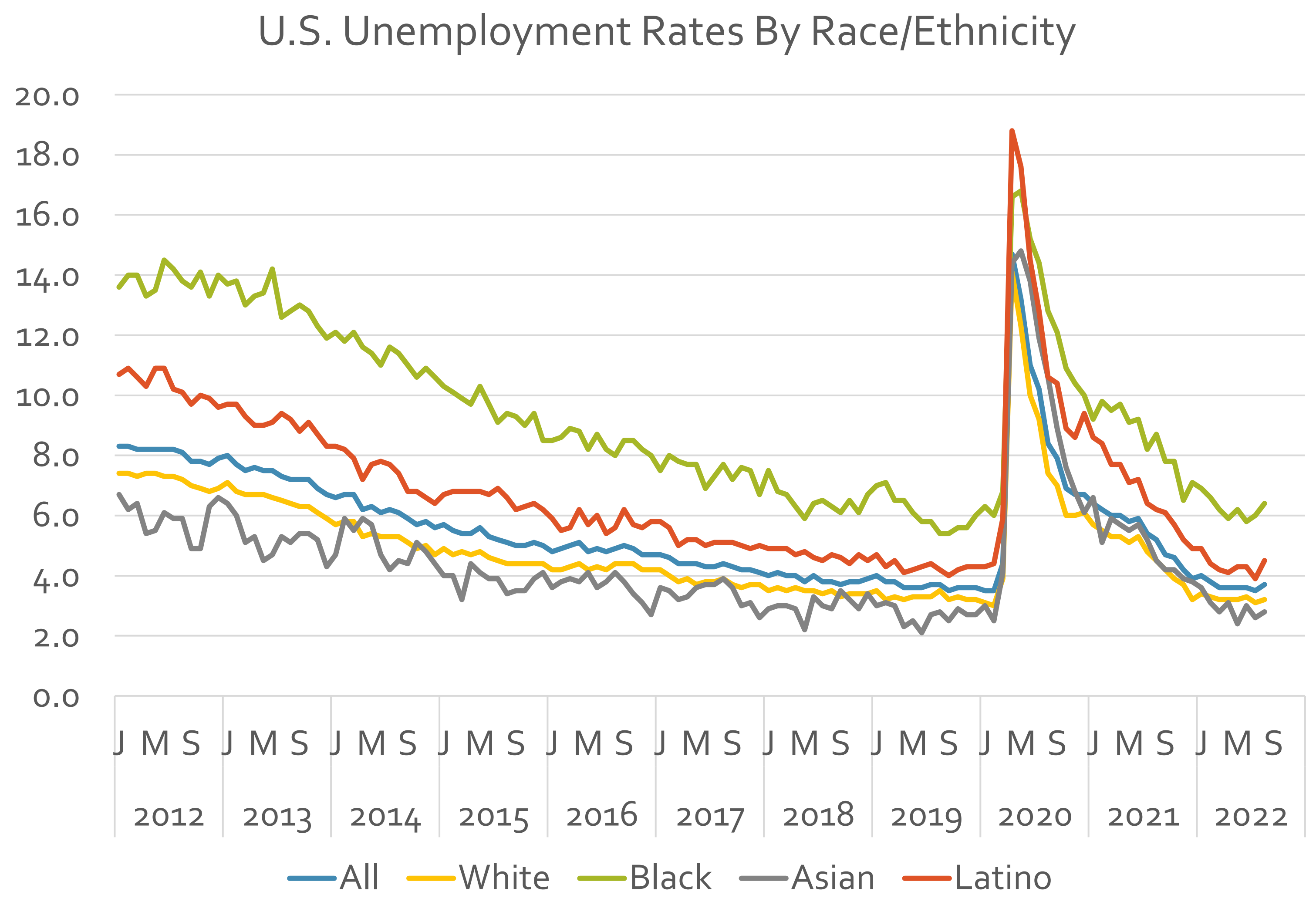
Source: EMSI

The official unemployment rate at its pre-recession low, while the broader measure of labor underutilization, the U-6 rate that includes discouraged workers and part-time workers who want to work full-time, is 0.1% *below* its pre-pandemic level.



Source: FRED

Despite an economy seemingly running at full capacity, the unemployment rate for Black workers is twice that of White workers, while Latino workers' unemployment rate is about 40% higher. Asian unemployment, at 2.8% is the lowest of all racial groups.

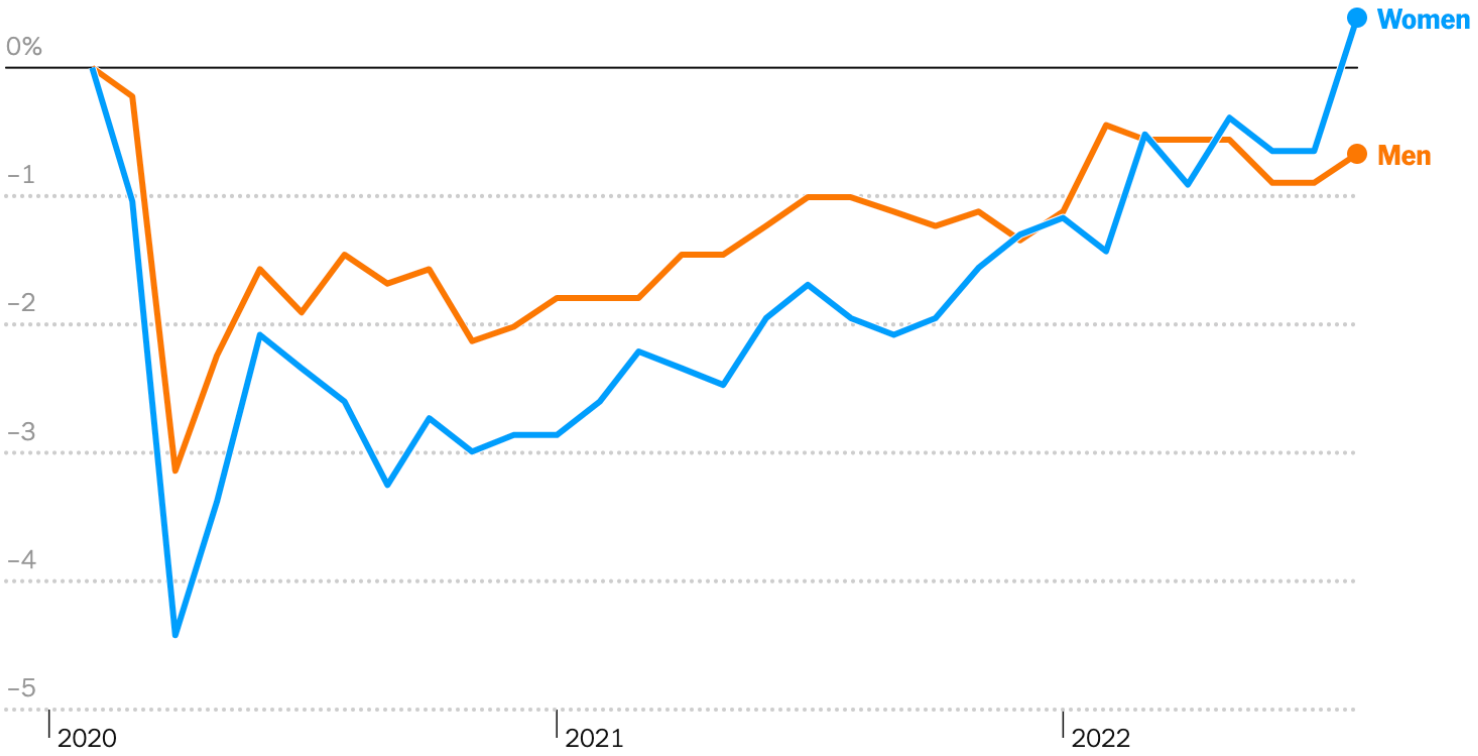


Source: Bureau of Labor Statistics

While women lagged men in returning to the workforce initially due to care issues, both childcare and care of those recovering from COVID, recently they have returned in larger numbers and now exceed pre-pandemic levels. Men are still struggling, however.

Working-age men haven't returned to the labor force as quickly as women

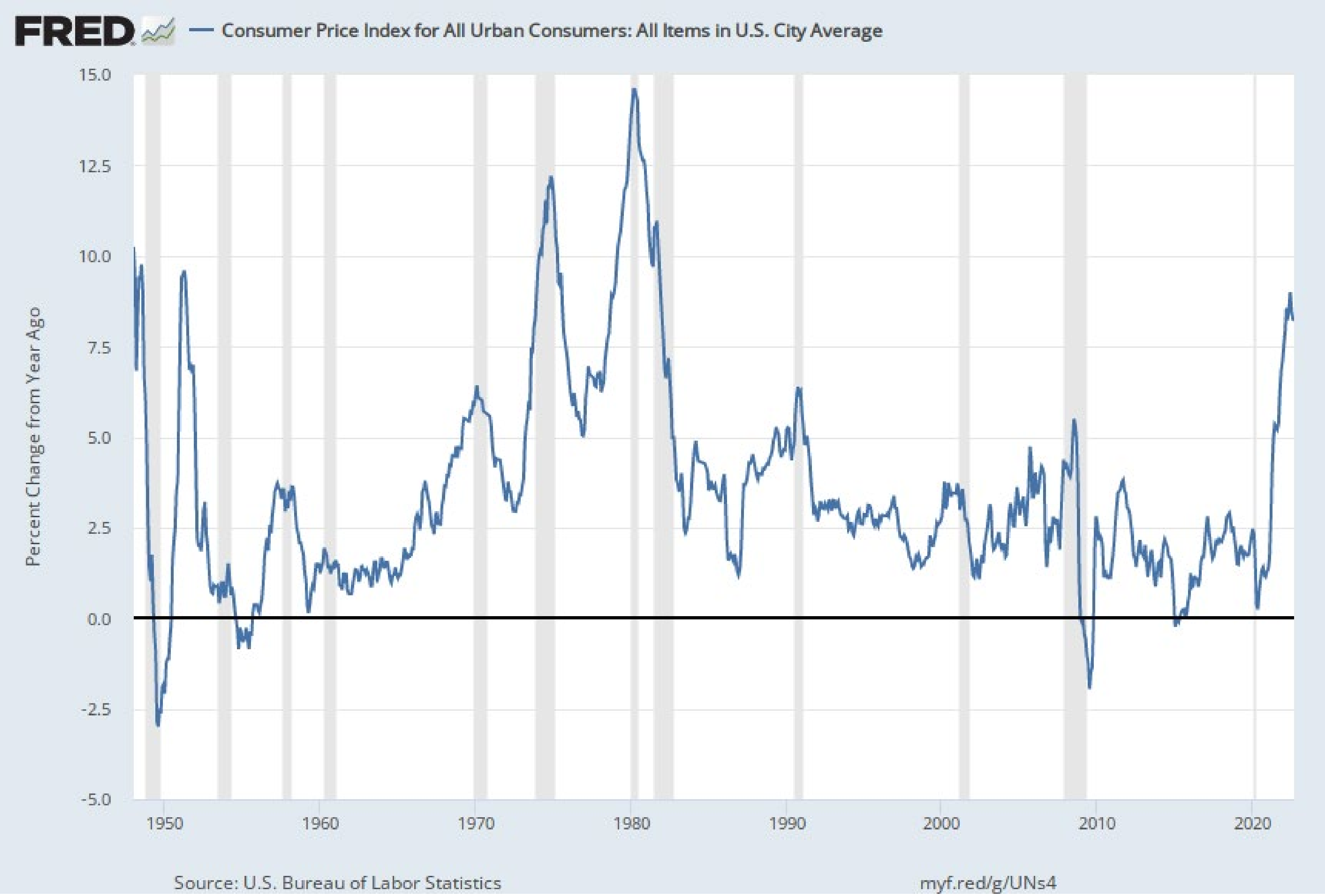
Percent change in labor force participation rate for men and women ages 25-54 since before the pandemic



Data is seasonally adjusted. Labor force participation rate is the share of each group who are in the labor force (employed, unemployed but looking for work or on temporary layoff). • Source: Bureau of Labor Statistics • By Ella Koeze

Source: New York Times, September 13, 2022

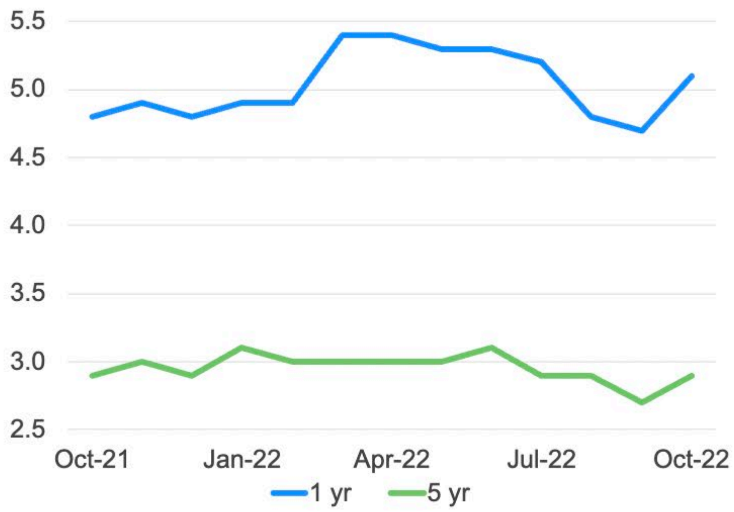
Inflation measured in terms of CPI is at 40 year high due to the combination of pent-up demand meeting supply side shocks. The only good news? It still not close to the peak in the 1980s…

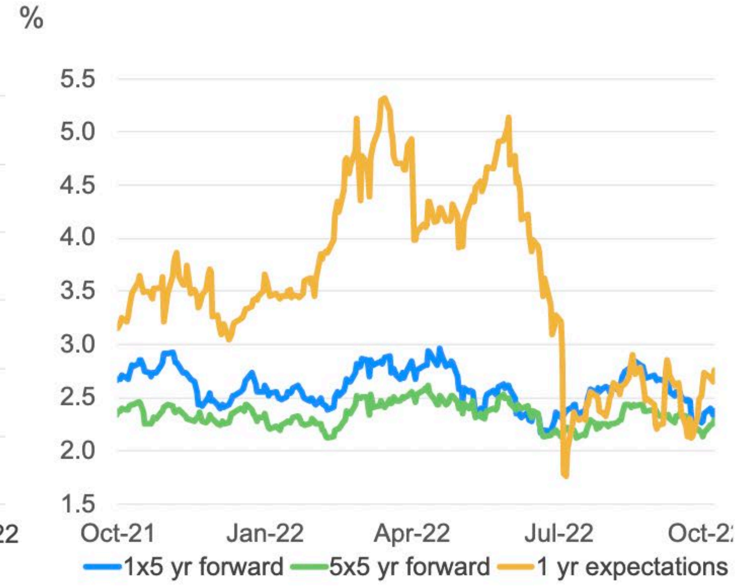


…and inflationary expectations still seem to be well-anchored (though perhaps creeping up).

University of Michigan Survey

Bond Market

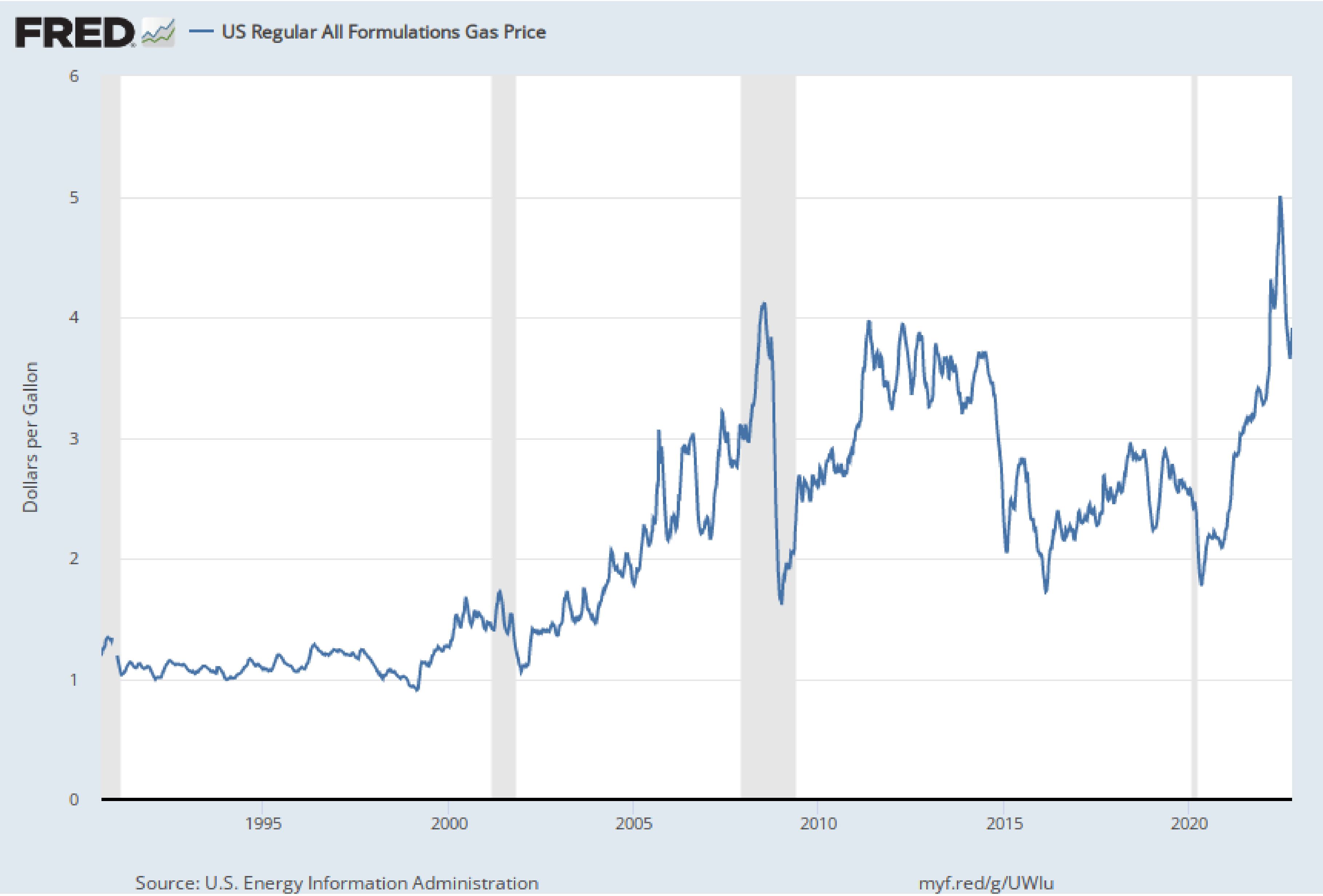




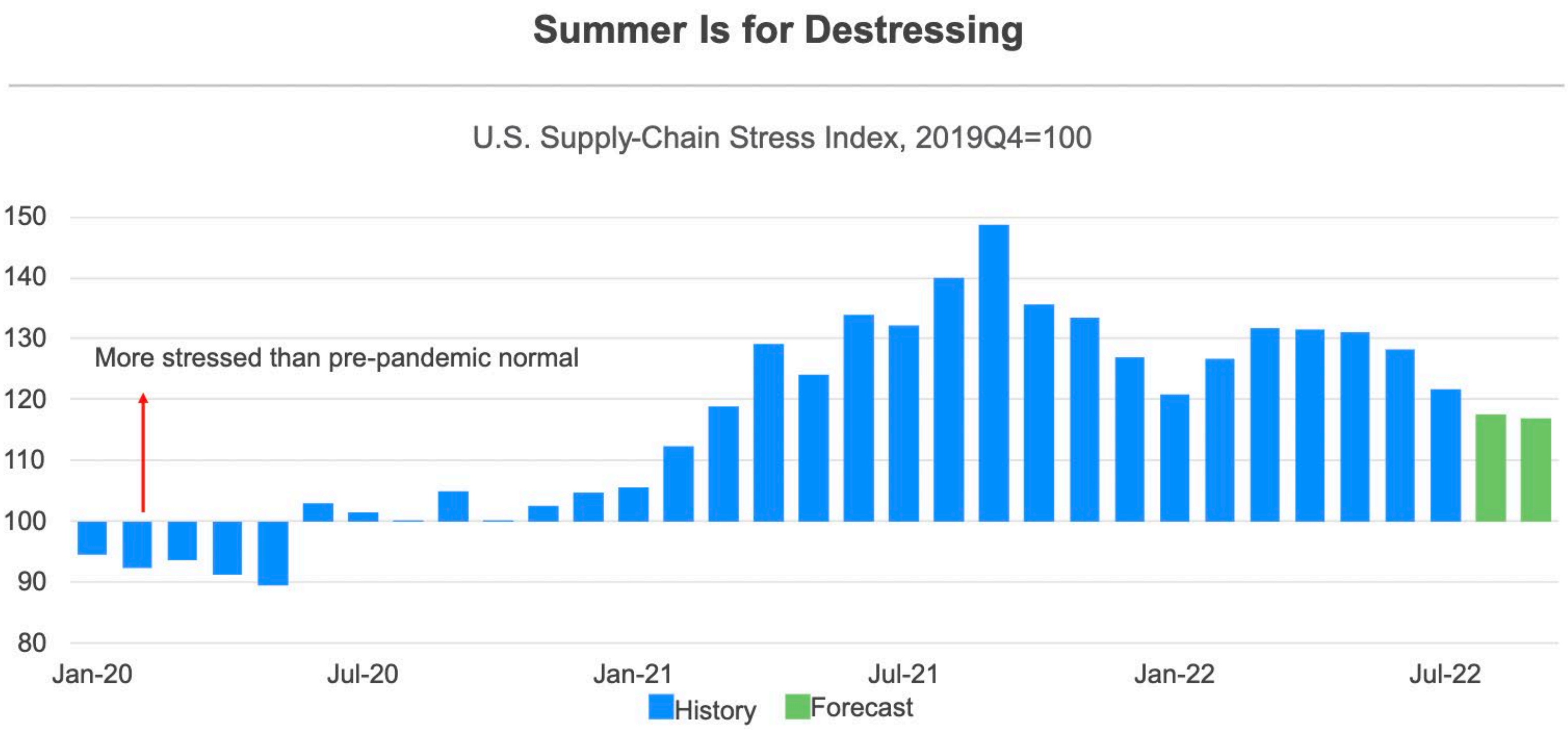
Sources: Univ. of Michigan, ICE, Moody's Analytics

https://www.economy.com/economicview/analysis/390839

Average gasoline prices are well off their peaks, but still about $1 more than pre-pandemic. Still, they are roughly at the average of the 2012-2014 period when the economy was significantly weaker.

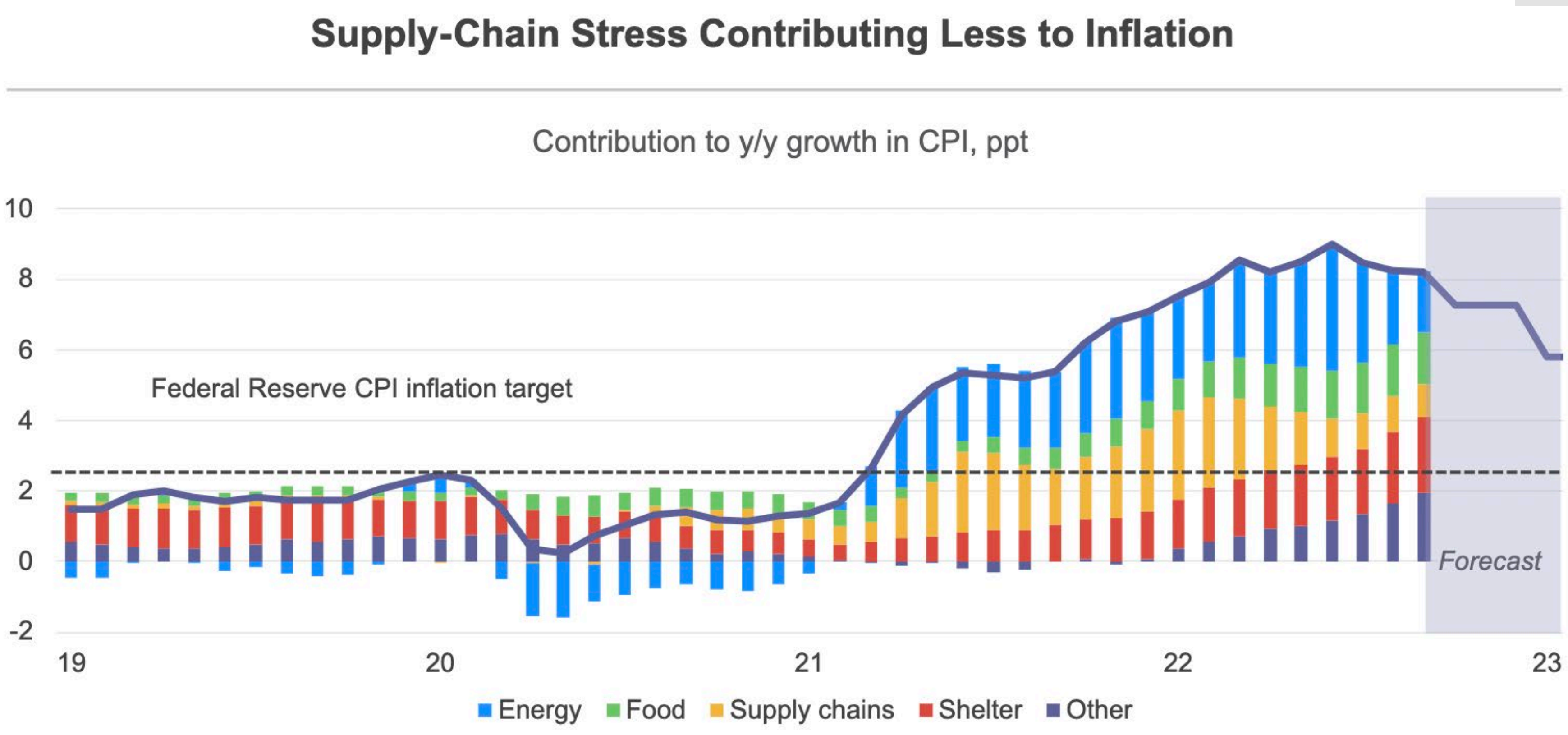


Supply bottlenecks appear to be generally moderating, though they are still elevated the pace of reduction has not been sufficient to relieve inflationary pressures.



Source: Moody's Analytics

As a result, supply chain pressures and energy prices are contributing less to inflation. Rather, the price rises of the last year have now fed into services where prices are "sticky" – medical care, education, recreation and rent – and these are accounting for a larger share of current price hikes.



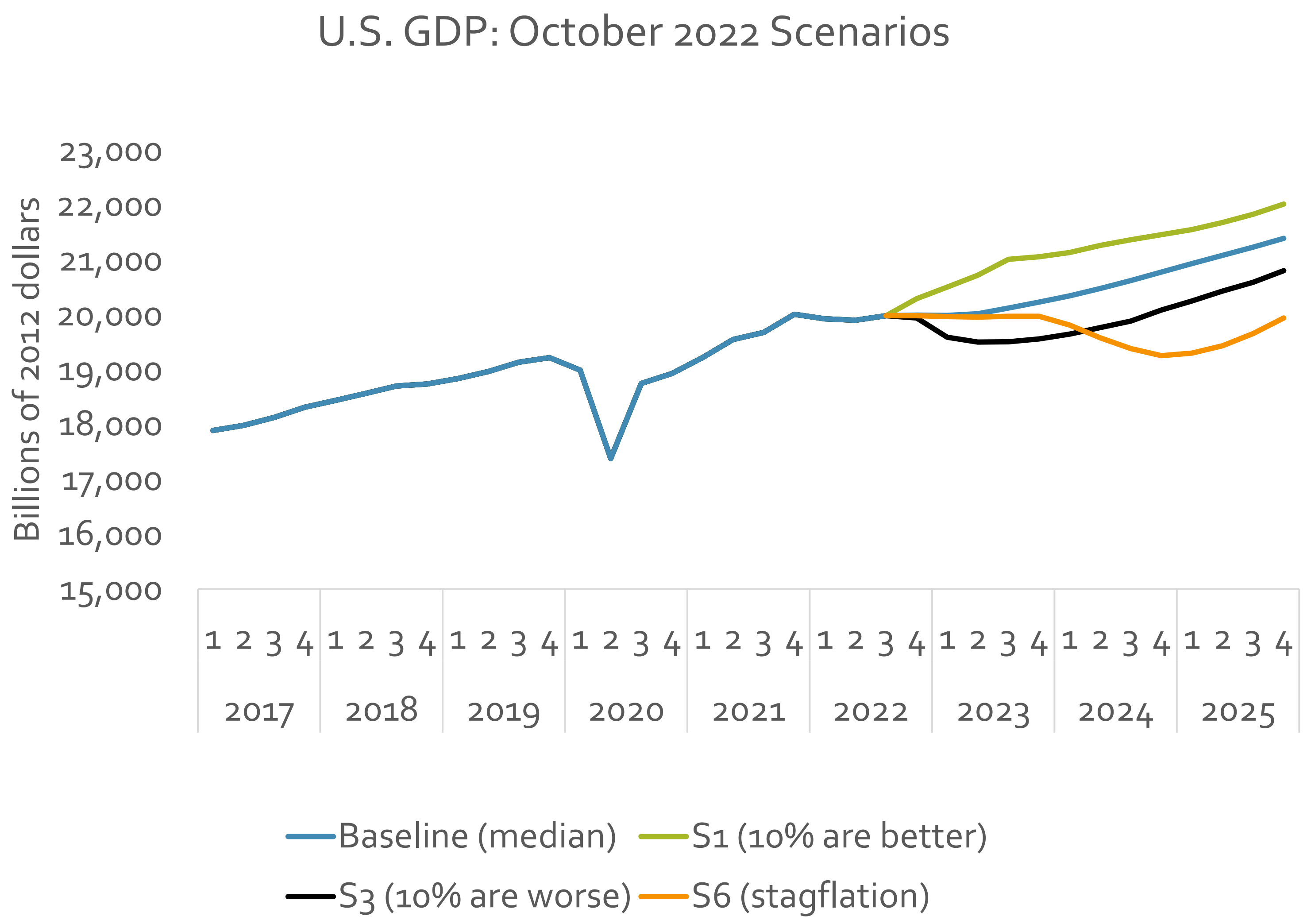
Sources: BLS, Moody's Analytics

Moody's Analytics:

October 2022 Assumptions for Baseline Forecast

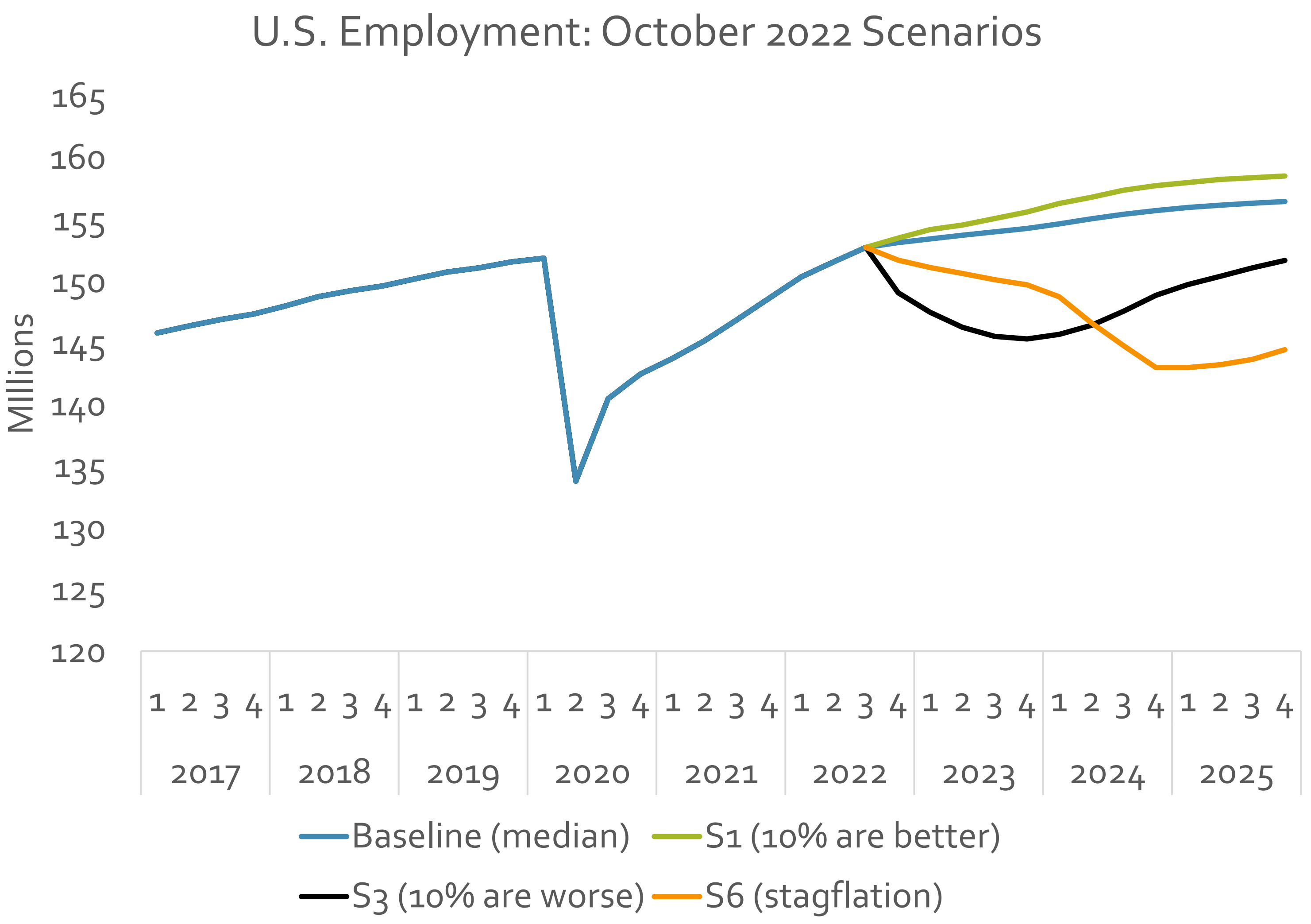
- The Fed will increase the funds rate another 75 basis points at the November meeting of the Federal Open Market Committee, 50 basis points at the December meeting, and 25 basis points at the meeting in late January. It is expected to peak at between 4.5% and 4.75% next year – nearly twice the level of the currently estimated "neutral" rate of 2.5%.
- We assume the Russian invasion of Ukraine won't expand beyond Ukraine.
- Oil supply will be down between 2 and 3 million barrels per day compared to pre-pandemic causing oil prices to stabilize near $100 a barrel. It won't be until mid-2023 that they gradually begin to trend down toward their equilibrium price of about $70.
- We assume the economy is currently at or near full employment - a 3.5% unemployment rate, a 62.5% labor force participation rate, and a prime-age employment-to-population ratio of at least 80%.
- The mid-term elections are likely to result in divided government and political gridlock, with no new fiscal policy initiatives likely to be undertaken.
- There are no widespread lockdowns due to a new COVID variant.

GDP declined slightly in first half of 2022 due to Omicron and inventory reductions. This likely modestly reversed itself in 3rd quarter. But under the baseline forecast, GDP is essentially flat until md-2023 when it is assumed the Fed pauses on increasing interest rates and then begins to reduce them.



Source: Moody’s Analytics

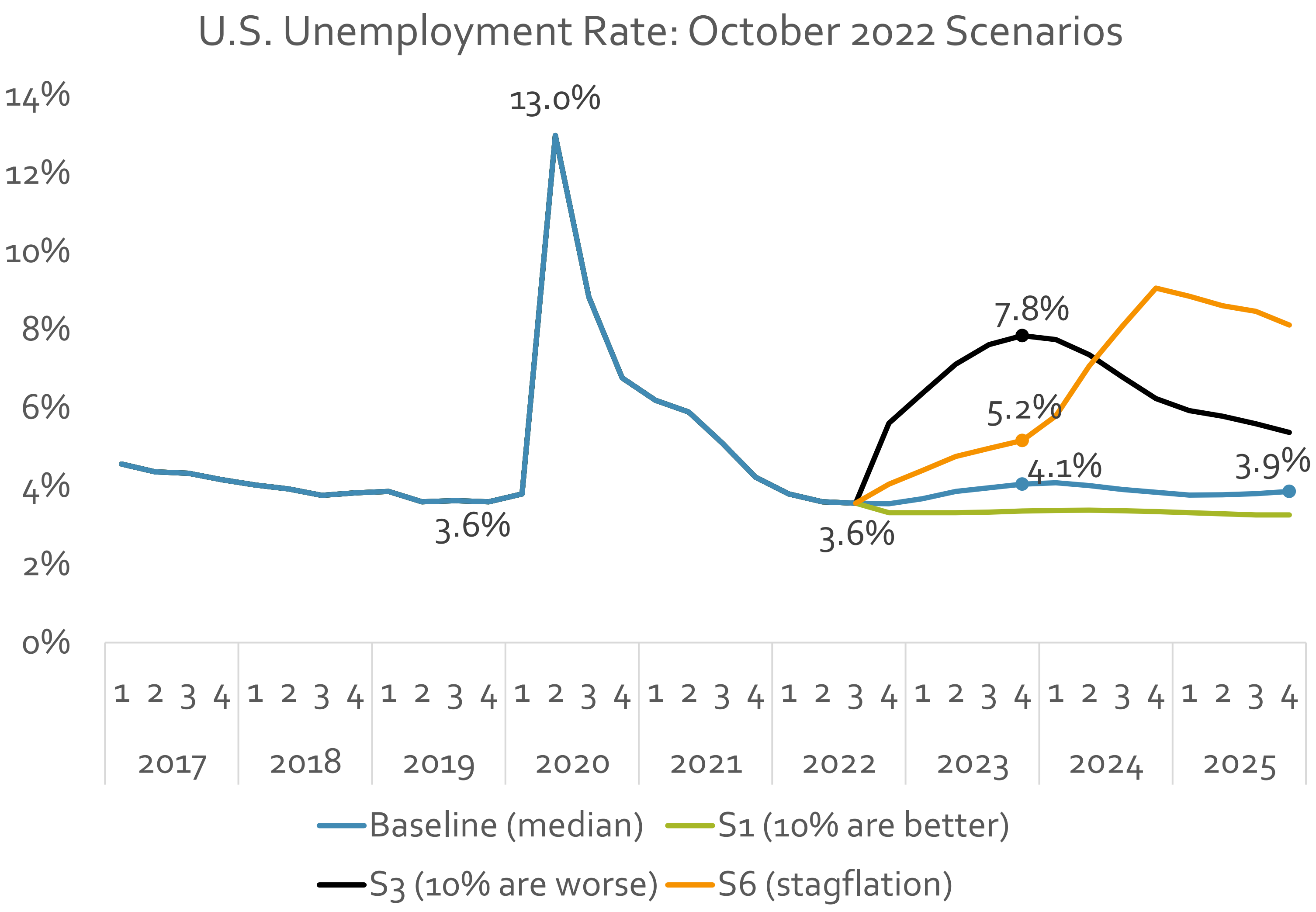
With flat GDP growth, employment should decline due to productivity increases. The baseline forecast shows flattening employment growth instead, reflecting the current momentum still in the labor market. That momentum ends beginning in 4th quarter under the recession and stagflation scenarios.



Source: Moody's Analytics

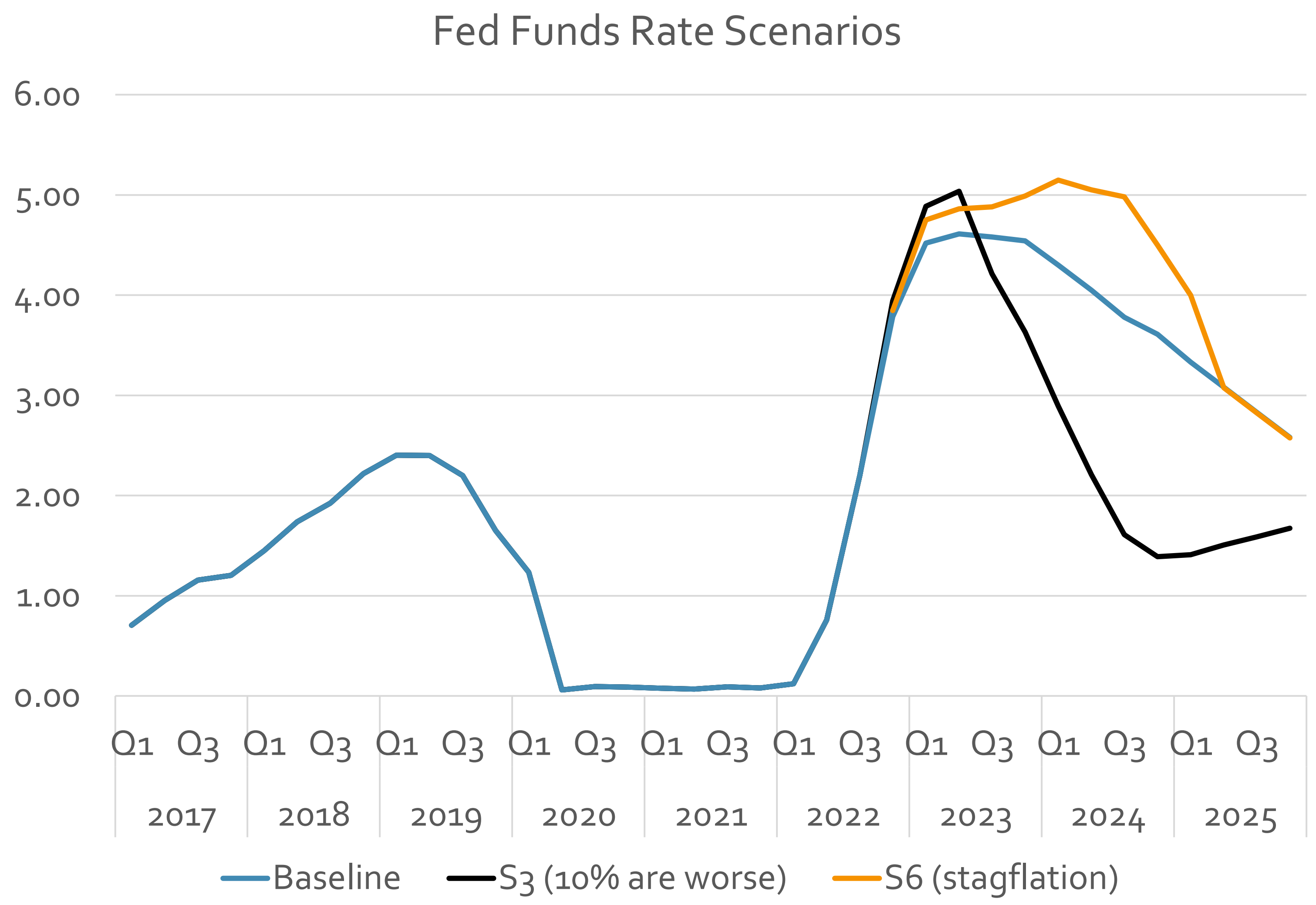
The baseline forecast expects unemployment to barely rise above 4%, while it increases to at least double that rate in both the recession and stagflation scenarios.

In no scenario does the unemployment rate approach what was experienced during the Covid-19 recession.

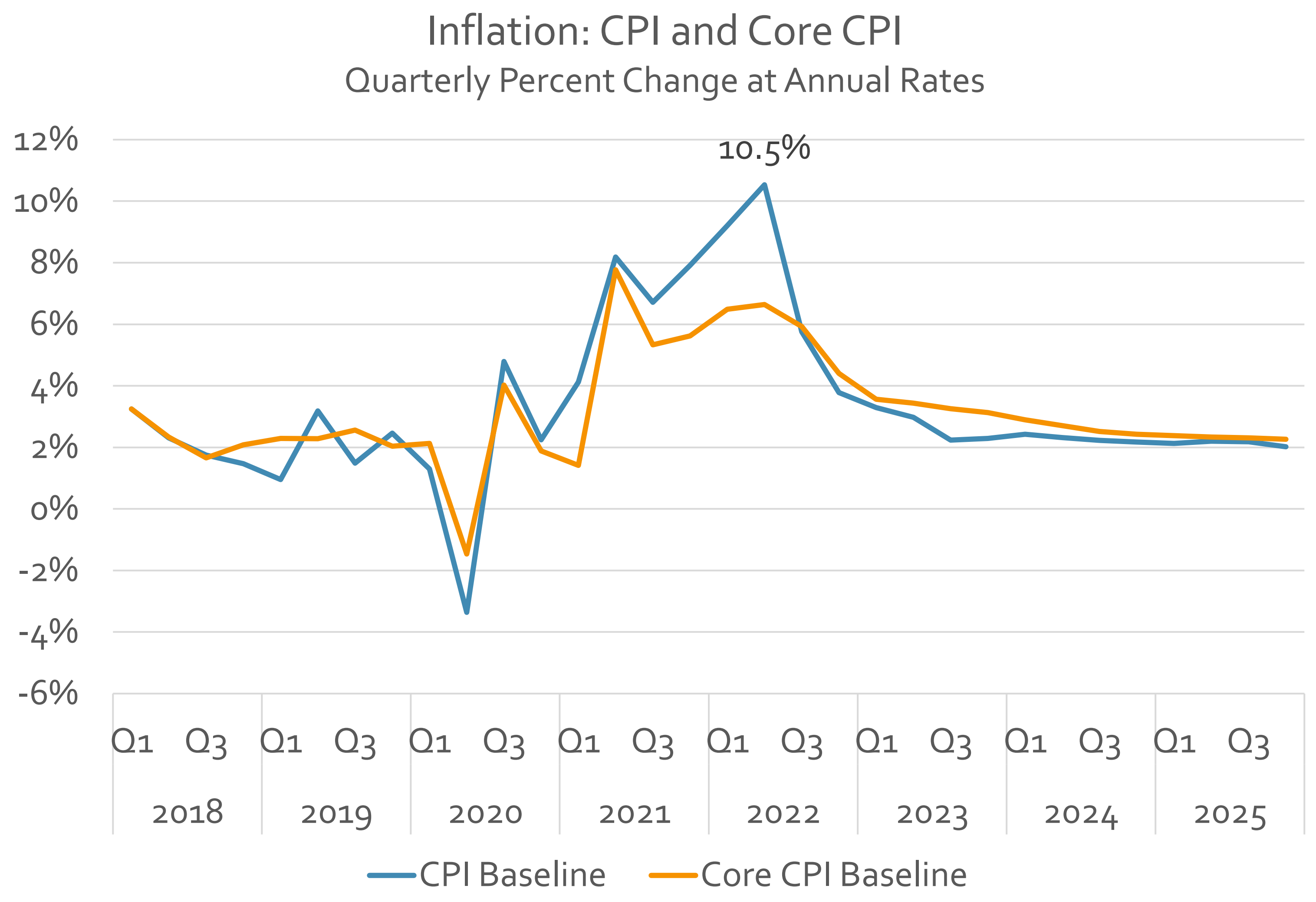


Source: Moody's Analytics

With fiscal policy receding, monetary policy takes center stage as the primary drive of macro-economic outcomes. The Fed's aggressive stance – willing to raise interest rates until observable inflation declines, even though monetary policy acts with a lag of up to a year – is the reason why inflationary expectations remain anchored.



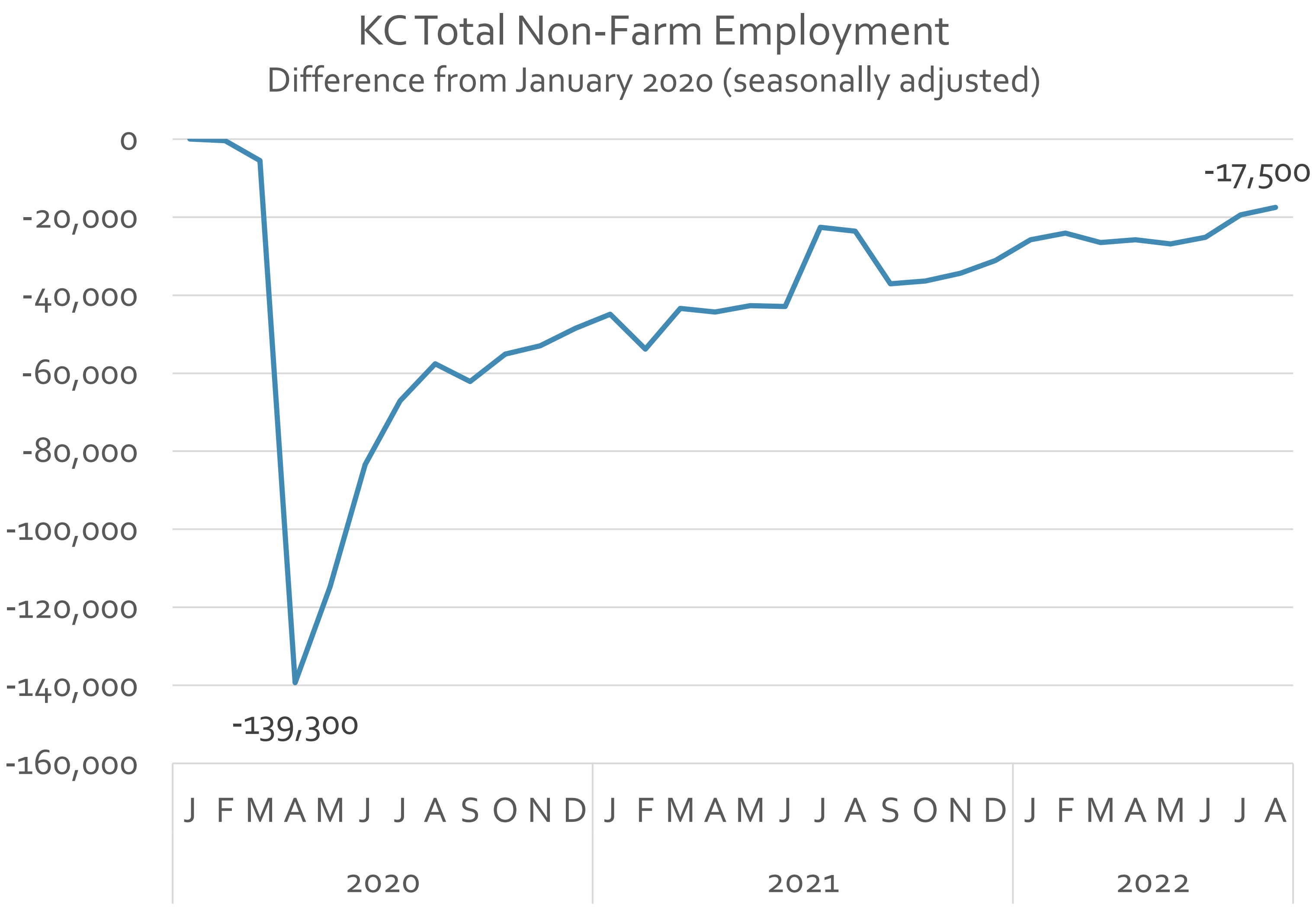
Quarterly topline inflation is expected to peak at 10.5% in 2nd quarter 2022 and fall to under 4% by the end of the year. It should reach the Fed's target by 3rd quarter 2023. Core inflation is stickier and won't be in range of the Fed's target until the end of 2024.



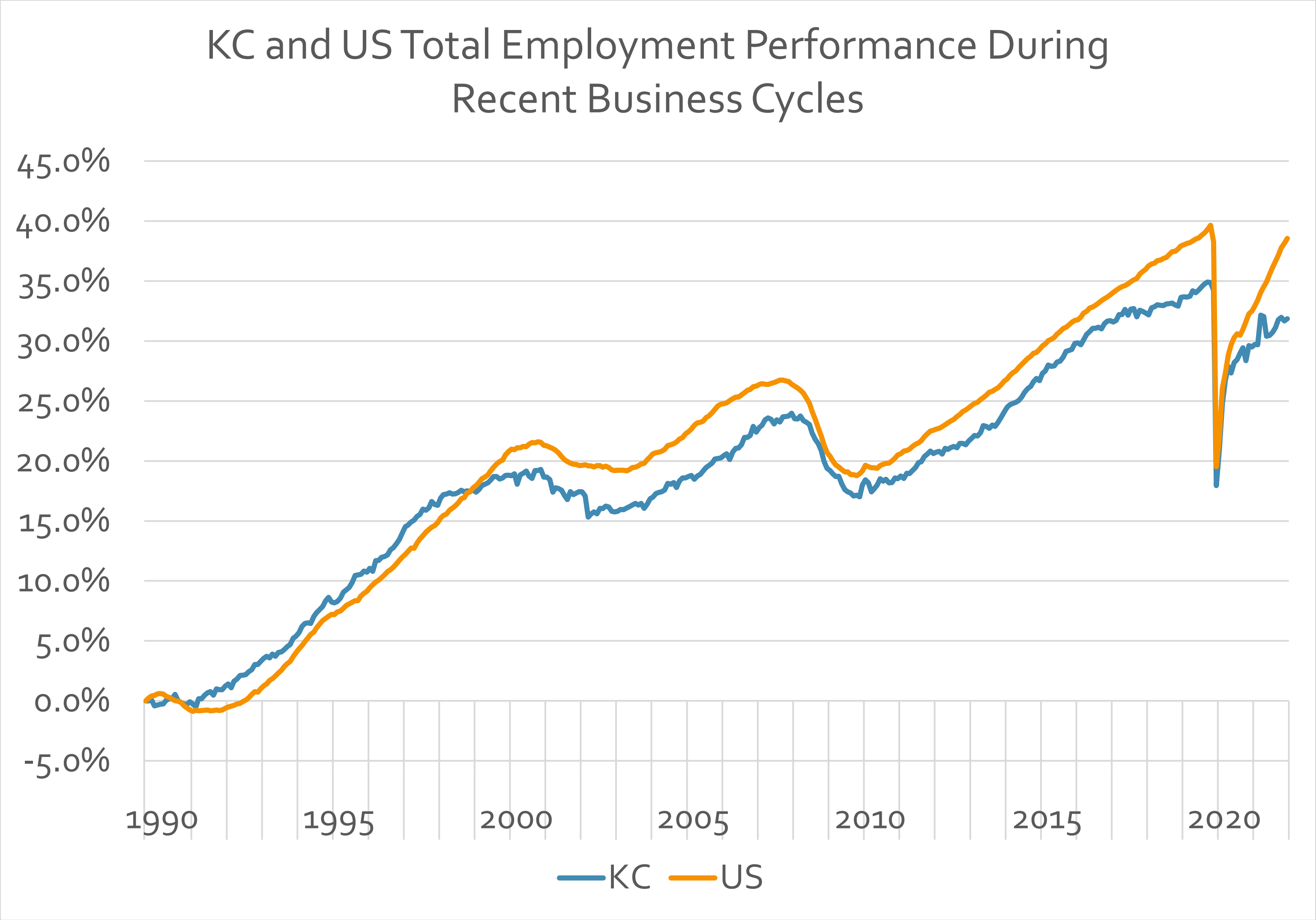
KC Economy – Current Situation

Photo by Jake Fagan on Unsplash

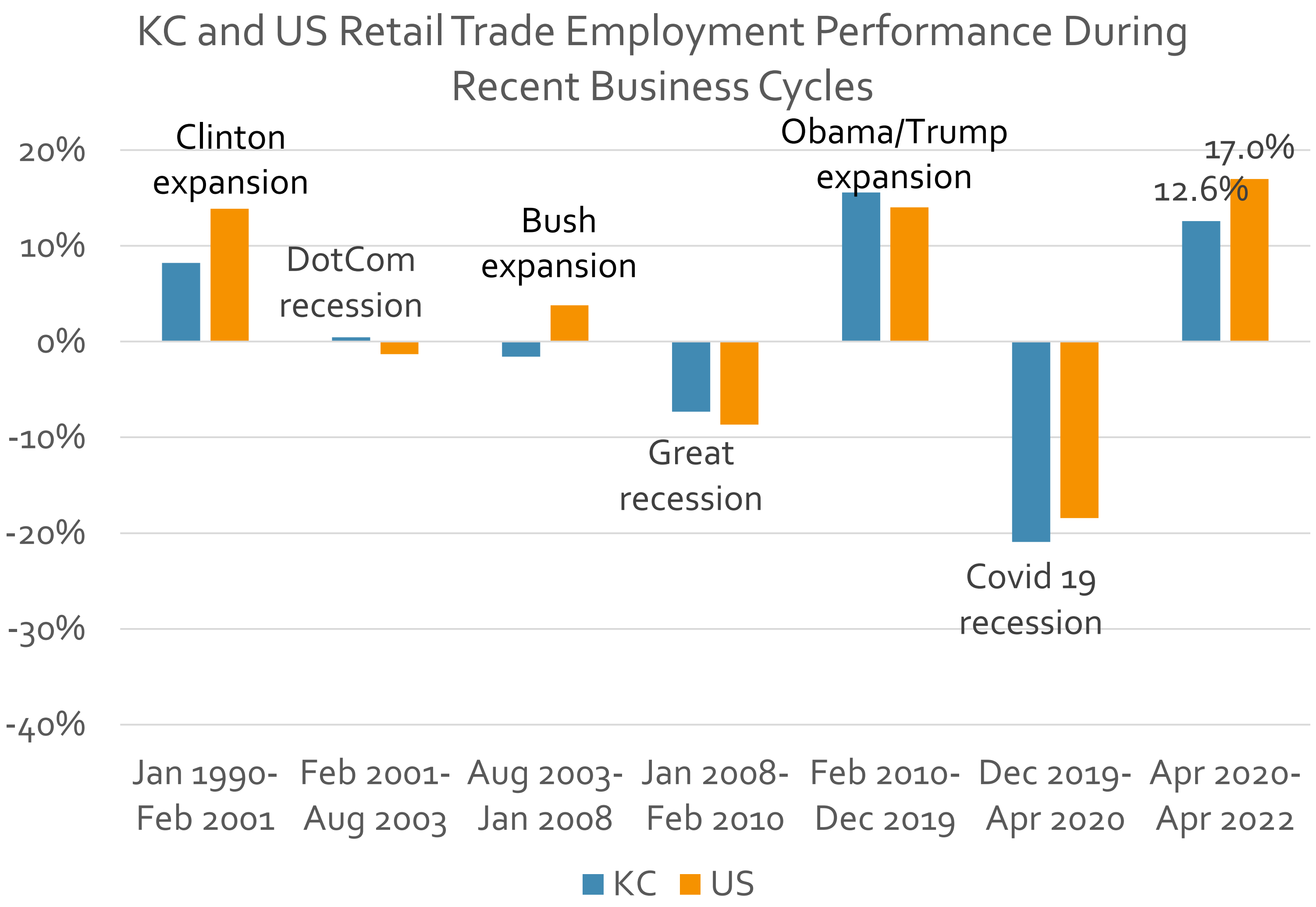
The trajectory of KC's employment recovery is much shallower than the nation's. We've only recovered 87.5% of our lost jobs while the U.S. has recovered all of them and then some.

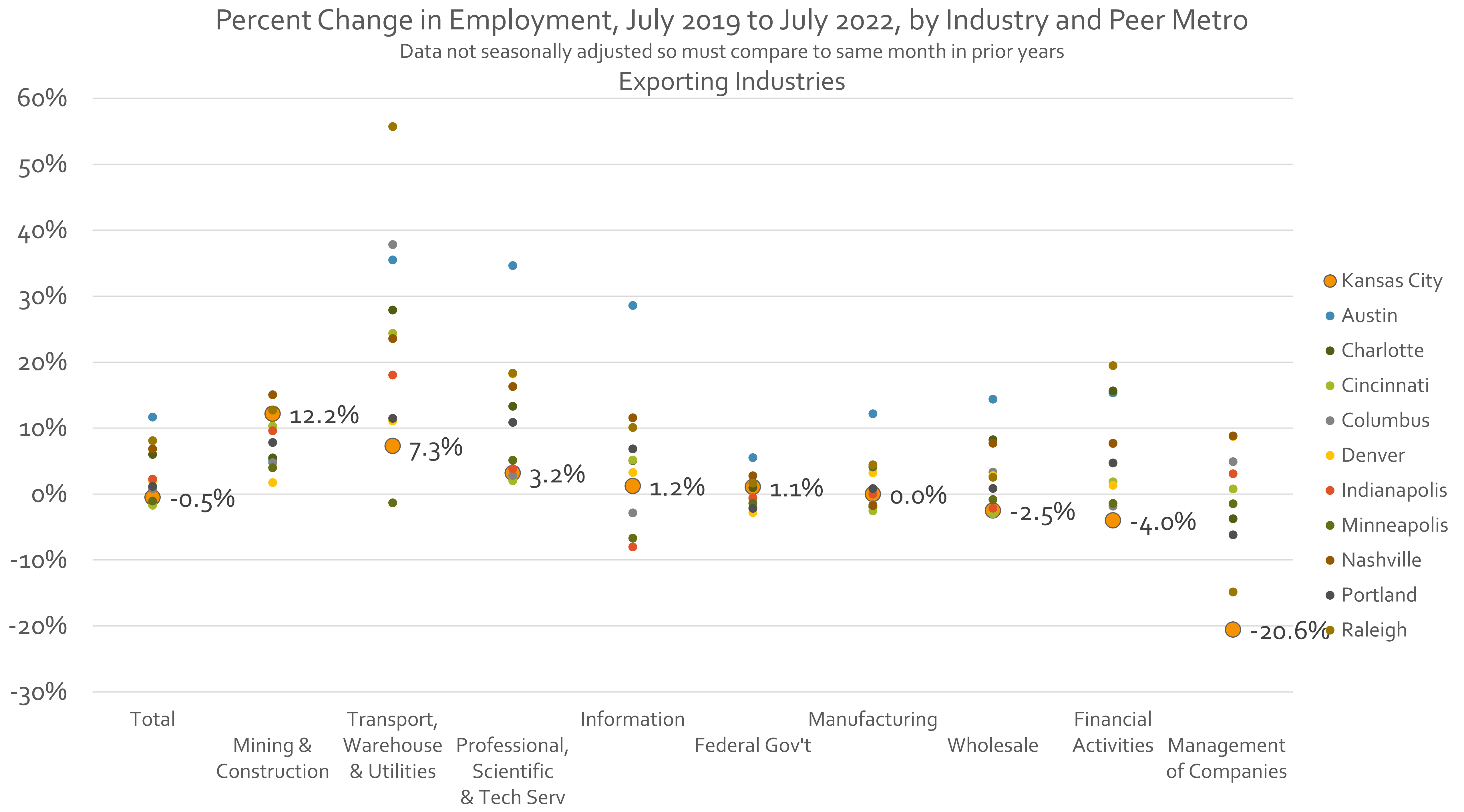


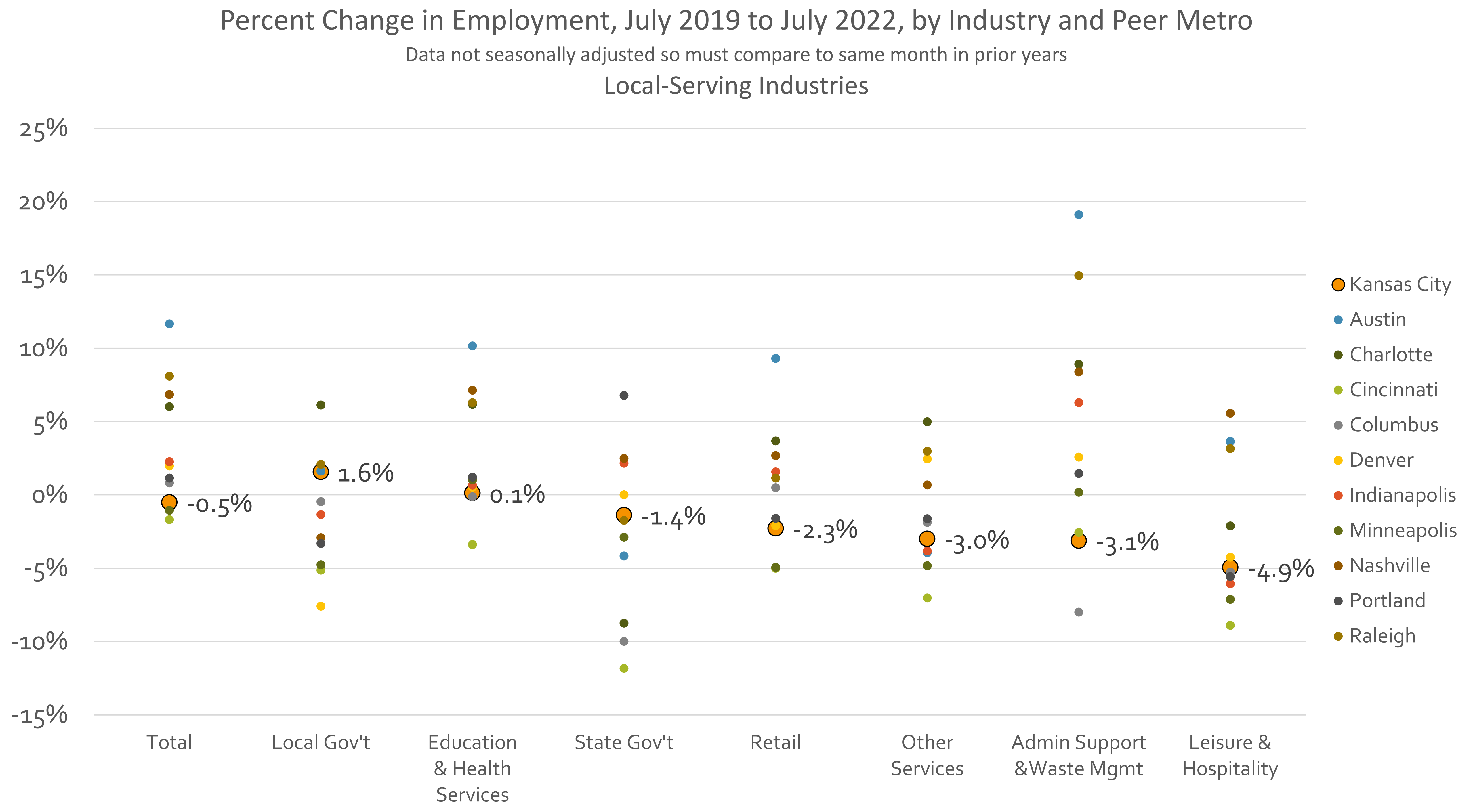
This truism is true, at least in recent business cycles – The KC economy doesn't bust as low but it doesn't boom as high. The problem is, recovery periods last much longer than recessions, so the KC economy is gradually losing ground relative to the nation and peer metros.



Aggregating the data by business cycle shows this pattern even more clearly. KC's growth is currently running 4.4% behind the U.S.

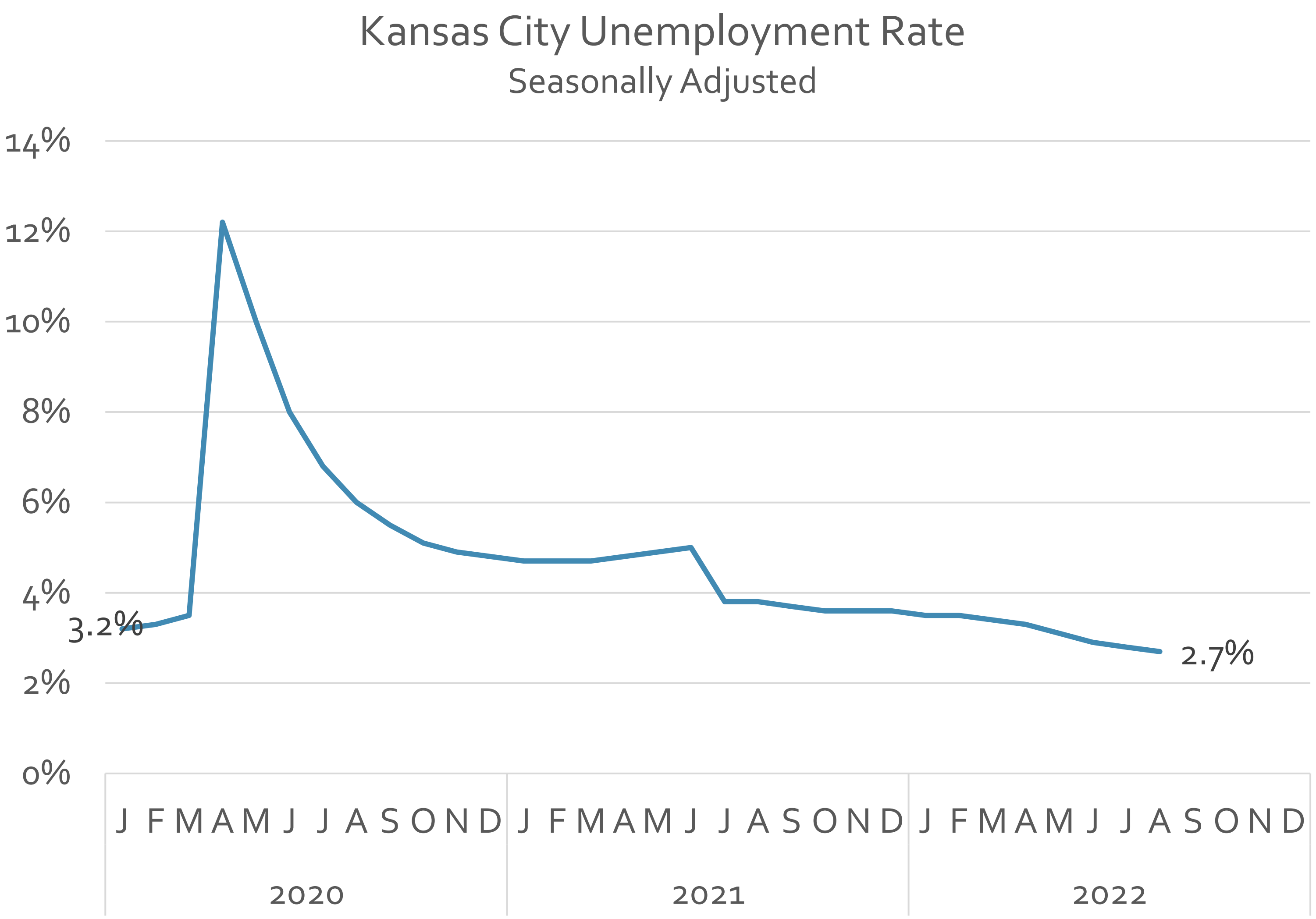



Percent Change in Employment, July 2019 to July 2022, by Industry and Peer Metro
Data not seasonally adjusted so must compare to same month in prior years
Exporting Industries
60%
50%
40%
30%
20%
10%
0%
-10%
-20%
-30%
-0.5%
12.2%
7.3%
3.2%
1.2%
1.1%
0.0%
-2.5%
-4.0%
-20.6%
Total
Mining & Construction
Transport, Warehouse & Utilities
Professional, Scientific & Tech Serv
Information
Federal Gov't
Manufacturing
Wholesale
Financial Activities
Management of Companies
Kansas City
Austin
Charlotte
Cincinnati
Columbus
Denver
Indianapolis
Minneapolis
Nashville
Portland
Raleigh



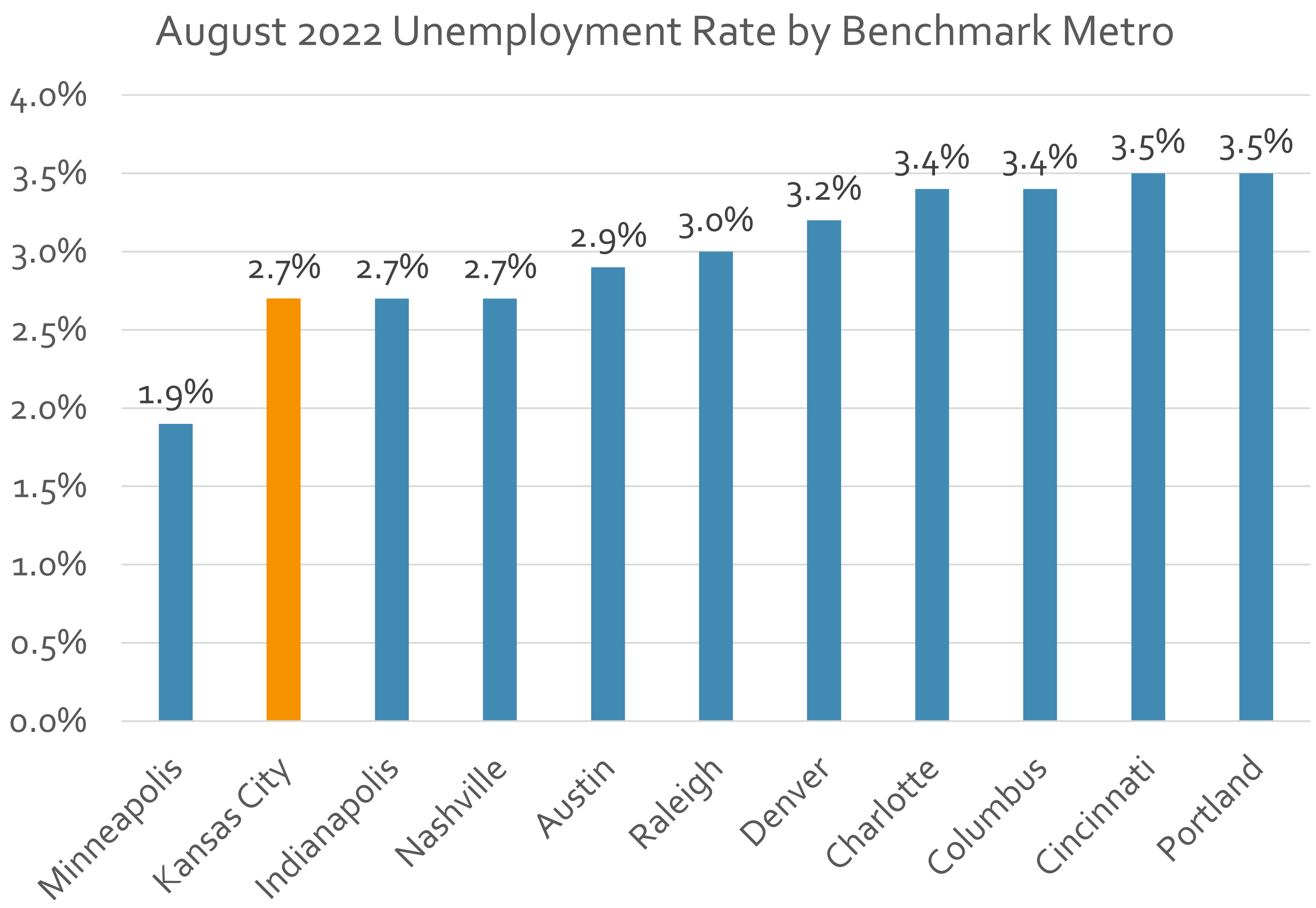
Percent Change in Employment, July 2019 to July 2022, by Industry and Peer Metro
Data not seasonally adjusted so must compare to same month in prior years
Local-Serving Industries
25%
20%
15%
10%
5%
0%
-5%
-10%
-15%
-0.5%
1.6%
0.1%
-1.4%
-2.3%
-3.0%
-3.1%
-4.9%
Total
Local Gov't
Education & Health Services
State Gov't
Retail
Other Services
Admin Support &Waste Mgmt
Leisure & Hospitality
Kansas City
Austin
Charlotte
Cincinnati
Columbus
Denver
Indianapolis
Minneapolis
Nashville
Portland
Raleigh

Yet, despite slow employment growth, our unemployment rate is 0.5% below its pre-pandemic low. This suggest labor supply issues may be biting here more than elsewhere.

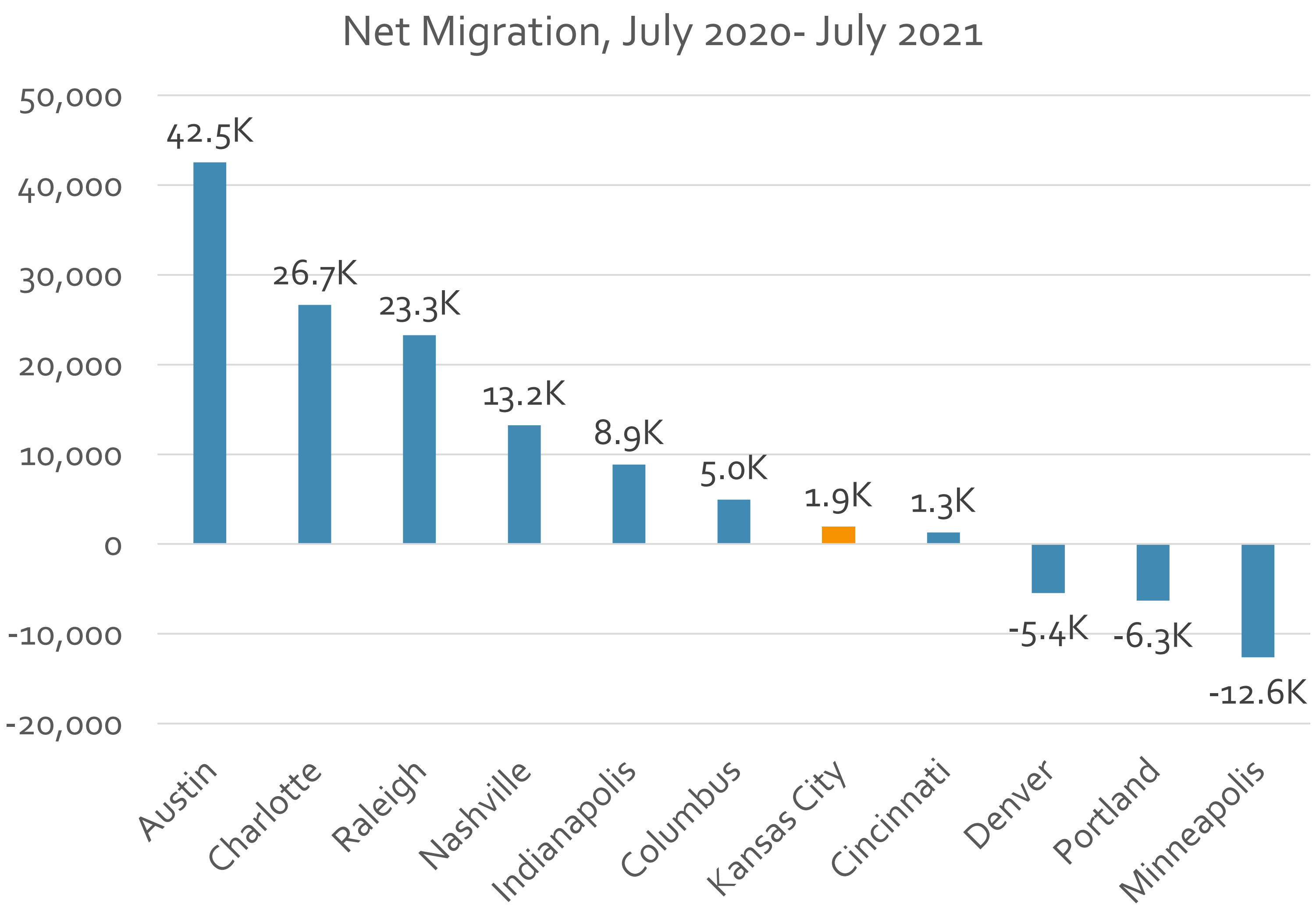


Source: BLS LAUS series

This is given modest support by the fact that KC has the second-lowest unemployment rate among its peers…



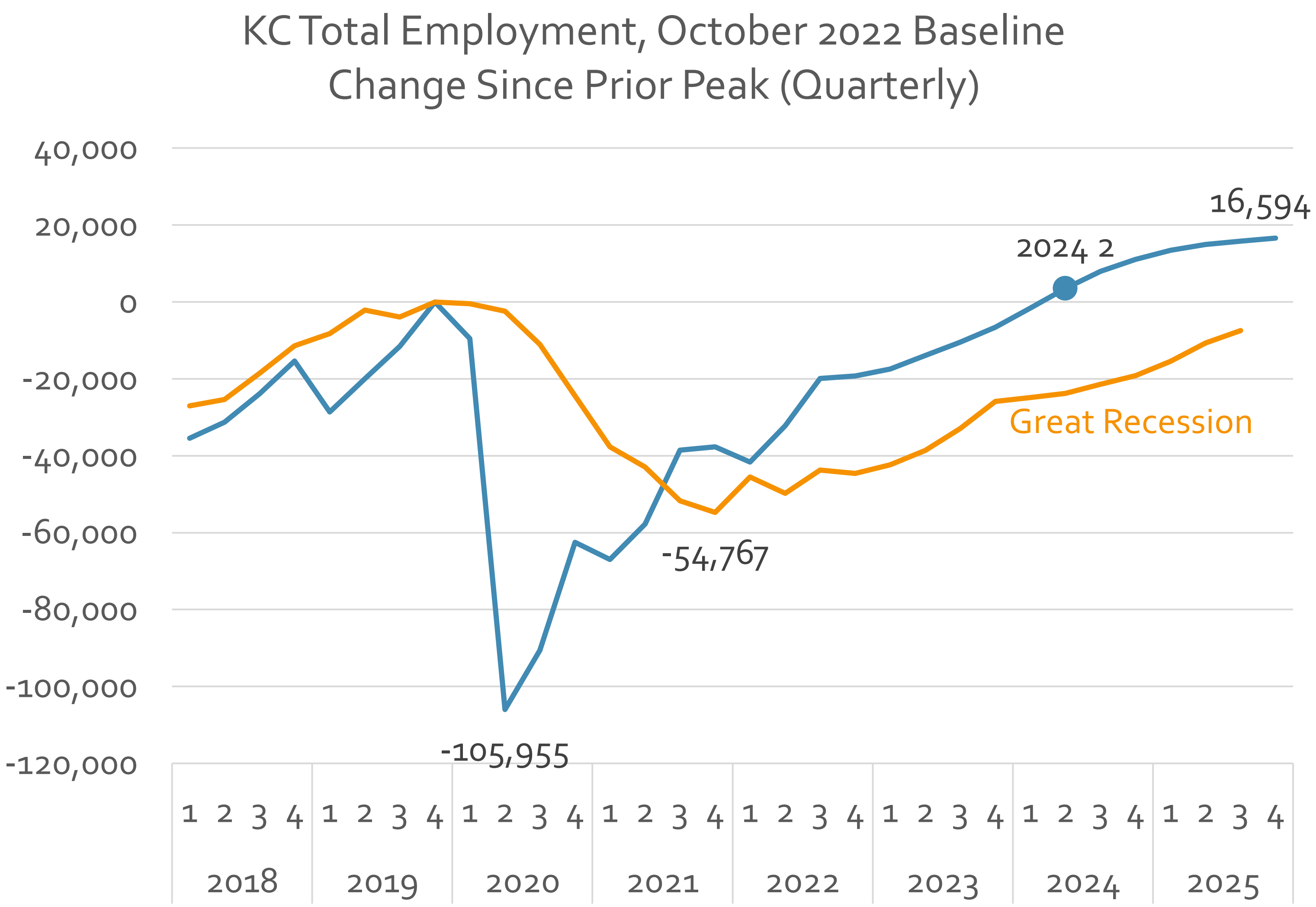
…while also having a relatively low rate of net in-migration.



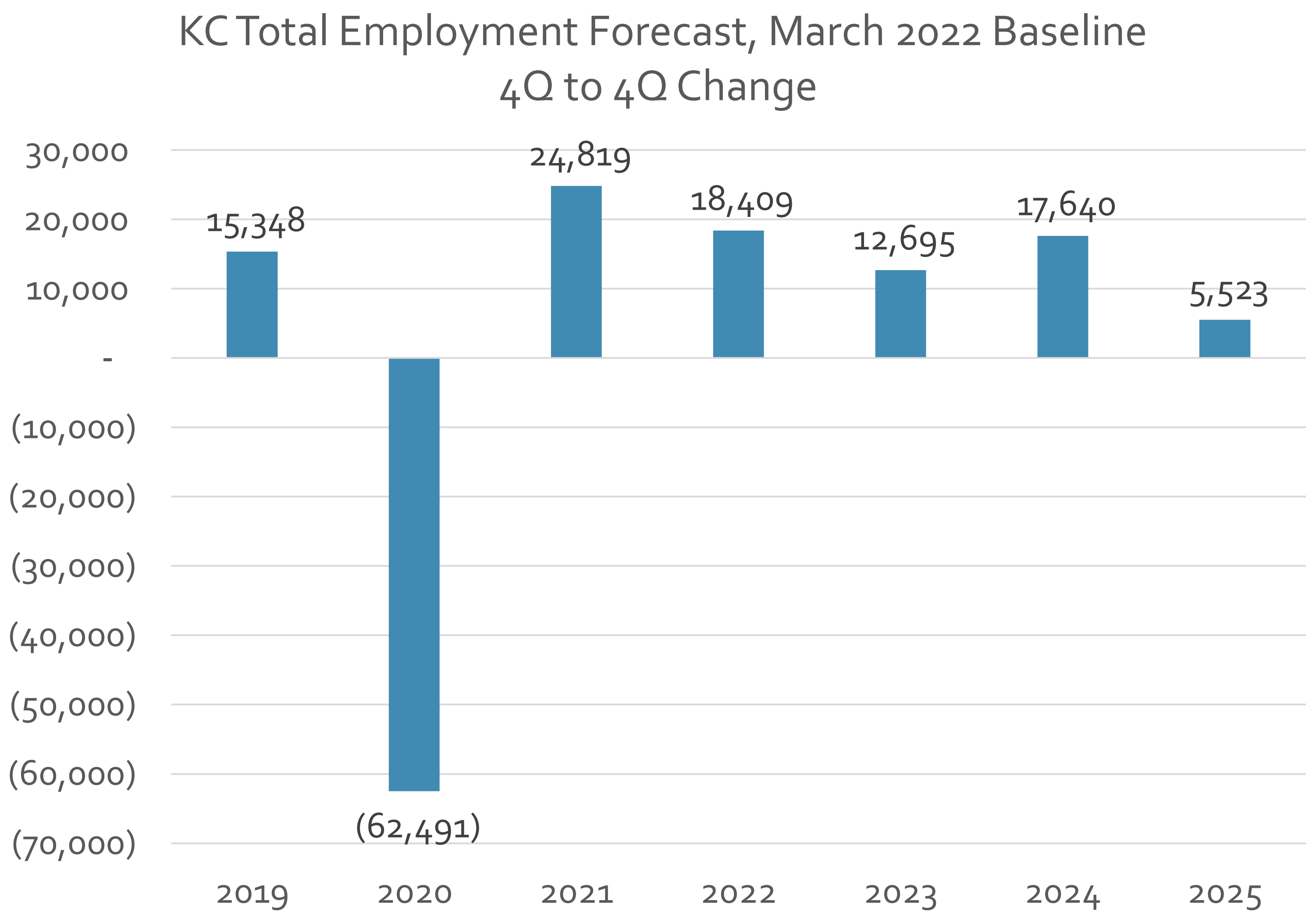
KC Economy – Forecast

Photo by Jake Fagan on Unsplash

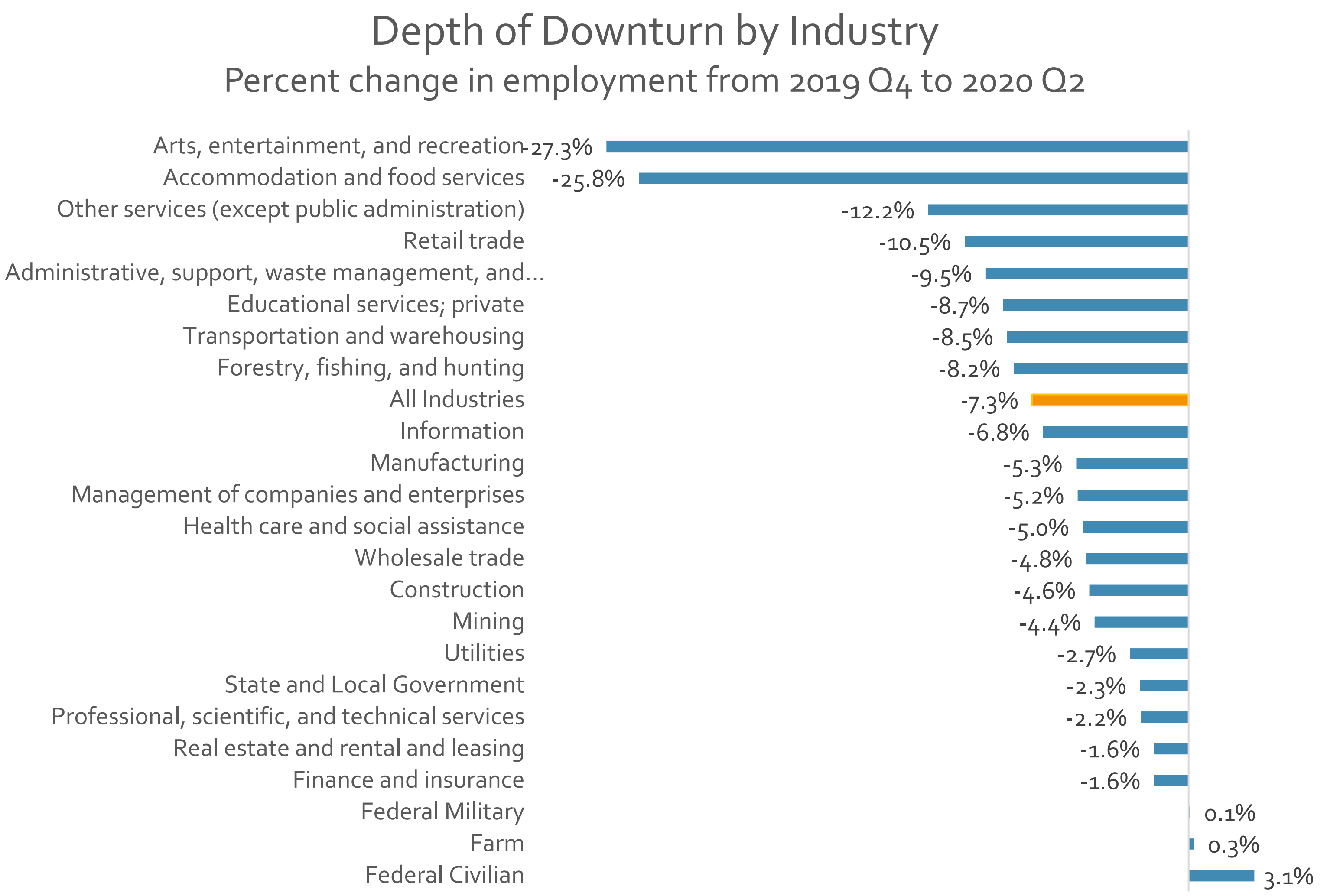
Based on the region's current economic performance relative to the U.S., KC won't exceed its pre-pandemic employment levels until 2nd quarter 2024, nearly 2 years after the nation.



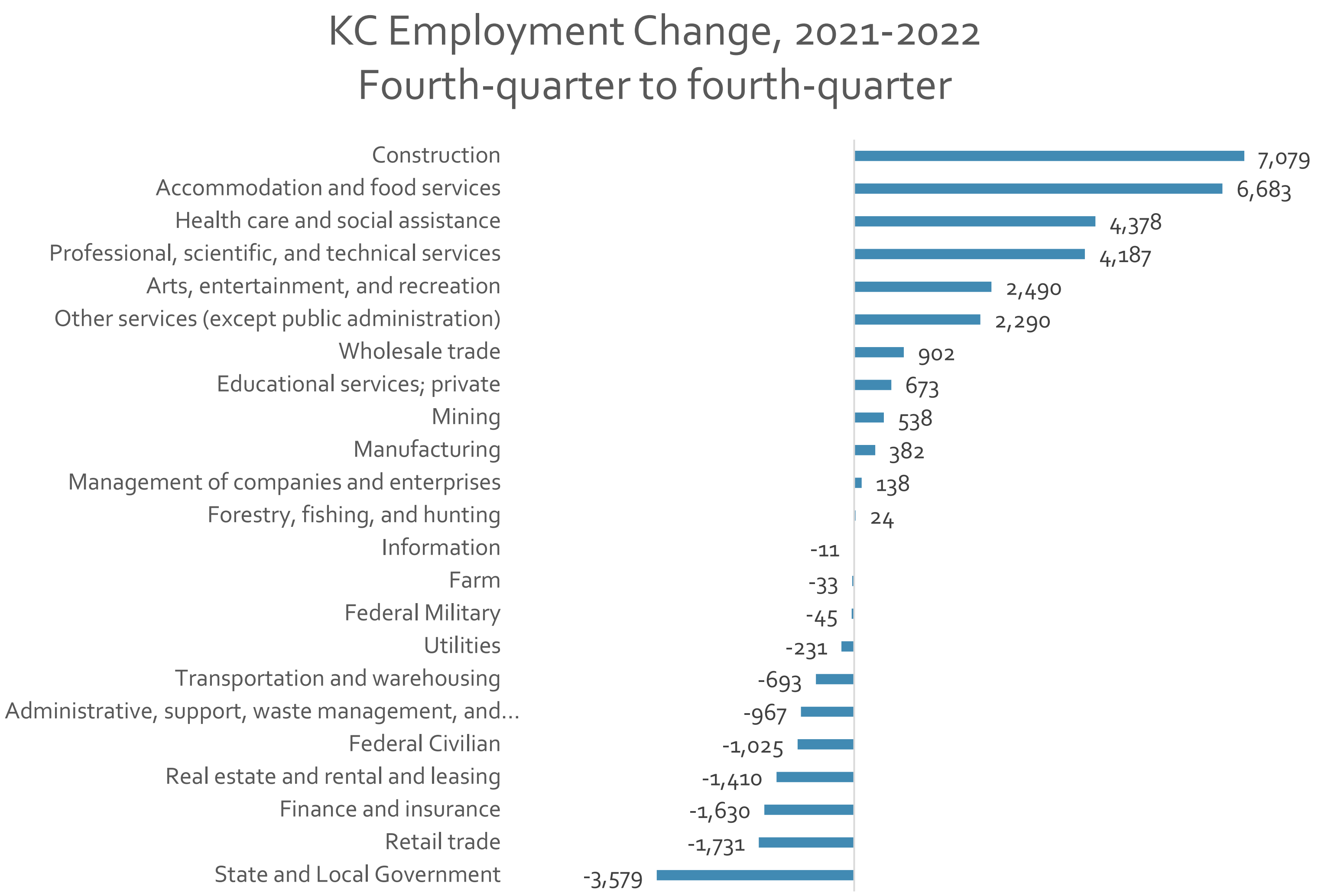
Job growth is expected to decline this year relative to last, and slow down even more next year as the nation skirts a recession. The good news is that KC is typically more resilient than the nation during a downturn. Growth then picks up again in 2024 as interest rates come down. By 2025, though, employment is limited by the growth of the working-age population.



Several sectors the region specializes in proved more resilient in the downturn, such as Finance and Professional/Technical Services.

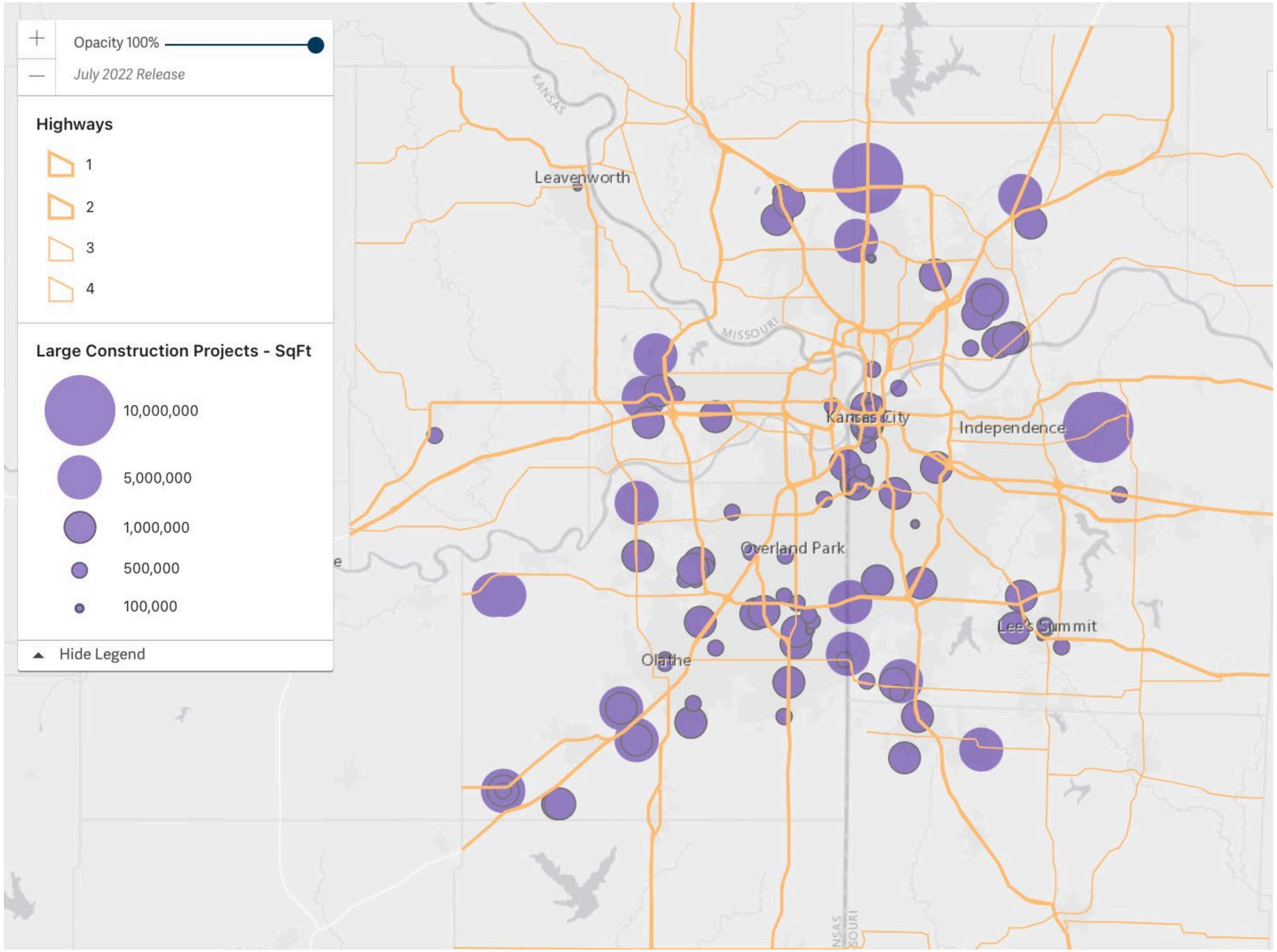


Construction, Accommodation and Food, Health Care, and Professional services led the growth of the regional economy in 2022.

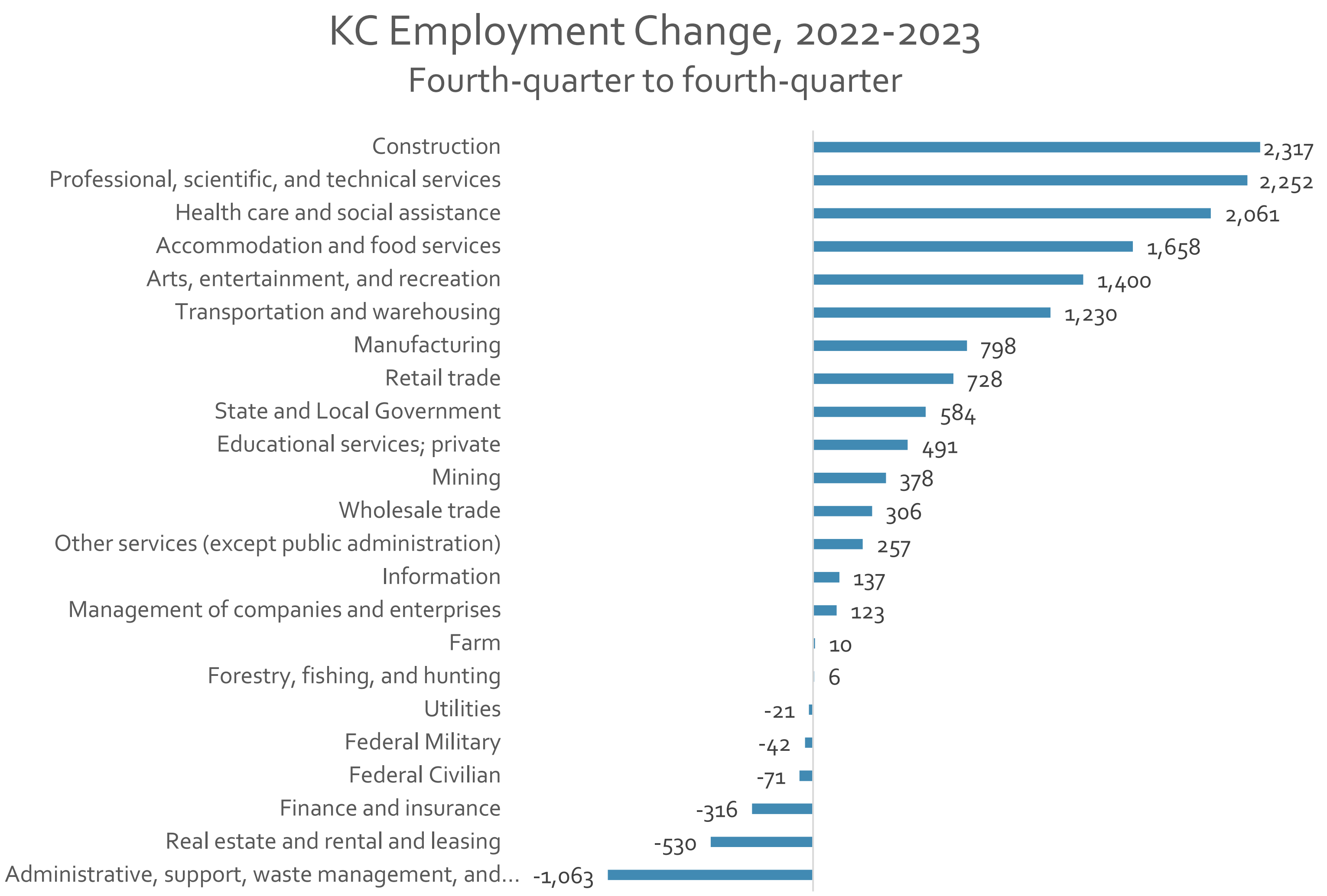


Much of the construction has been concentrated in the industrial and distribution sectors, with most locating near highways along and outside of the I-435 /I-470 Interstate loop.

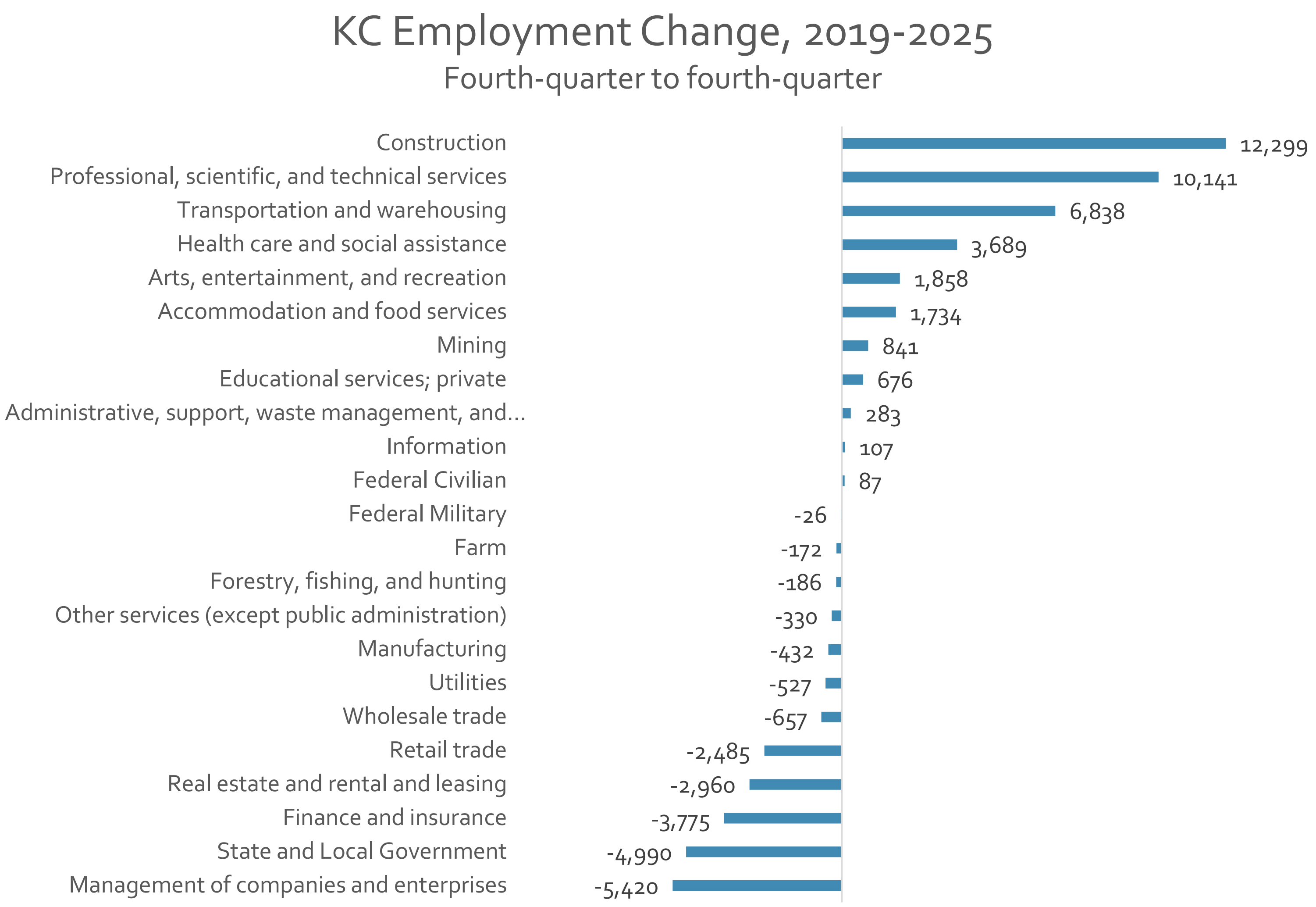
Large Existing and Planned Construction Projects, 2019-2022



Those sectors are expected to be joined by Arts and Entertainment and Transportation and Warehousing in leading regional employment growth in 2023.



Taking the entire pandemic and recovery period into account reveals that Construction, Professional and Scientific Services , Transportation and Warehousing as well as Health Care form the backbone of the region’s economic resilience.



Summary

- Nationally, the economic recovery continues apace, but locally, the KC economy has begun to lag the nation and most of its peers.
- Especially concerning is that this is most true for the sectors the region most specializes most in and most exports to the rest of the country and world.
- At this time, it is not clear why the Kansas City metro's job growth should be slower than it peers, but low labor availability is likely part of the reason. The region has an exceptionally low unemployment rate and also a low net migration rate.
- This means for KC's economy to grow, we must continue to improve our "brand" so we can more easily attract and retain the workers needed.
- But we also must find ways to employ the people who are already here more productively, moving people from lower-paid occupations to the high-demand export-oriented sectors of the economy.
- A workforce strategy IS an economic development strategy.

Questions?

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