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USA ECONOMIC REVIEW

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USA ECONOMIC REVIEW

Global Recovery Hit by Huge Supply Shock

The recovery from the COVID-19 pandemic is being harmed by a possibly massive global supply shock, which could slow growth and raise inflation. The Ukraine conflict and economic sanctions against Russia have jeopardized world energy supplies. Sanctions do not appear likely to be lifted anytime soon. Russia contributes around 10% of the world's energy, including 17% of natural gas and 12% of oil. The increase in oil and gas prices will increase industry expenses and diminish real incomes for consumers. Europe might face complete energy shortages and rationing if Russia's supply is cut off abruptly. Increased energy prices are unavoidable.

Forecasts Cut on Energy Shocks, Rate Hikes

Rating Agencies have lowered global GDP growth predictions for 2022 by 0.7 percentage points to 3.5%, 1.5% points to 3.0% for the eurozone, and 0.2 percentage points to 3.5% for the US. This reflects the pressure from increasing energy costs and a faster-than-expected pace of US interest rate rises. The prediction for global growth in 2023 downward by 0.2 percentage points to 2.8%.

EU's Reliance on Russian Energy Exposed

Russia supplied a quarter of primary energy consumption in the eurozone in 2019. This figure corresponds to OPEC's share of global primary energy production in 1973. Eurozone inflation will average 5% in 2022 due to the increase in European gas costs.

Fed Cannot Help Support Growth this Time

Prior to the Ukraine invasion, the Fed shifted to a hawkish stance and began hiking rates in March. We anticipate that the Fed Funds rate will reach 2% by the end of 2022 and 3% by the end of 2023. Additionally, the ECB indicated an early end to asset purchases in 3Q22, and we now anticipate the ECB raising the main refinancing operations rate by 25bp in 1Q23. By contrast, the People's Bank of China is easing, with inflation remaining low. Additional interest rate and RRR reductions, as well as significant fiscal easing, are expected. However, with consumption and property markets remaining subdued, we forecast growth of only 4.8%, well below the official target. Inflationary pressures and supply shocks might have a significantly greater negative impact on global GDP growth if they result in much more aggressive Fed tightening, push oil prices to USD150 per barrel (bbl), and trigger major European energy restrictions. We explain the consequences in a negative case.

Forecast Highlights

The global economy expanded swiftly at 5.9% in 2021, but the outlook has deteriorated as inflationary pressures have intensified and Russia's invasion of Ukraine and subsequent sanctions have disrupted global energy markets. We now forecast global growth to moderate to 3.5% in 2022, down from 4.2% in December's Global Economic Outlook for 2021. (GEO). Additionally, we reduced our global growth prediction for 2023 by 0.2 percentage points to 2.8%, reflecting the lagged effect of this year's faster-than-expected monetary policy tightening. These predictions for global GDP growth are higher than historical norms, owing to persistent post-pandemic recovery dynamics and strong near-term demand momentum in the United States. However, there are risks to our baseline forecasts, and later in the study, we sketch out a downside scenario in which inflation pressures culminate in a significant growth shock.

Additionally, the global growth prediction for 2023 was lowered by 0.2 percentage points to 2.8%, reflecting the lagged effect of this year's faster-than-expected monetary policy tightening. These predictions for global GDP growth are higher than historical norms, owing to persistent post-pandemic recovery dynamics and strong near-term demand momentum in the United States. However, there are risks to our baseline forecasts, and later in the study, we sketch out a downside scenario in which inflation pressures culminate in a significant growth shock.

Global Recovery on Track Pre-Invasion

The global economic recovery was on pace before to Russia's invasion of Ukraine. China's GDP growth outperformed our forecasts in 4Q21, while historical data adjustments resulted in the eurozone and UK annual growth outturns for 2021 exceeding our December GEO predictions by 0.3pp and 0.6pp, respectively. India's recovery accelerated to 8.1% in 2021 (calendar year). The rise of Omicron cases at the turn of the year had a relatively slight and transient effect on activity in the United States, the United Kingdom, and the eurozone.

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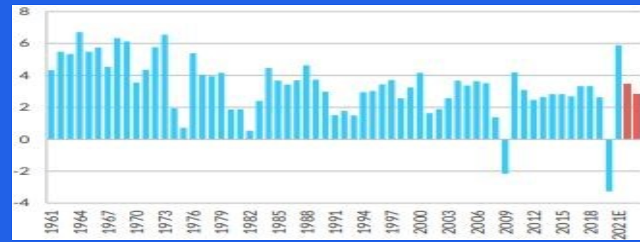


Impact of Russia's Economic Isolation

At the end of February, when Russian armed forces invaded Ukraine, the outlook shifted dramatically. This provoked a rapid, strong, and coordinated response from the US, EU, and UK, among others, aimed at isolating the Russian economy financially. No economy of Russia's size and significance has ever faced such severe sanctions. The Russian economy is the 11th largest in the world, with a GDP of USD1.6 trillion in 2021 (just under 2% of global GDP) and more than USD800 billion in international trade flows (imports plus exports). While much has been made of the fall in global bank exposure to Russia over the last decade, Russia's gross foreign liabilities - which include FDI, portfolio equities and debt, and bank loans – exceeded USD1.2 trillion in September 2021. In terms of potential global economic consequences, 'disconnecting' an economy of this size from the global banking system bears no relation to prior sanctions put on North Korea or Venezuela.

For several economies in eastern Europe, the impending serious recession in Russia will be a big shock to export demand, but exports to Russia account for a tiny proportion of overall exports and GDP in the majority of major economies. Rather than that, the greatest impact is due to Russia's enormous share of world oil and gas production and commerce. Russia produces 13% of the world's oil, 11% of the world's oil exports, and roughly 17% of the world's gas. It is by far the greatest gas exporter in the world, accounting for over a quarter of global exports. Global energy markets are being disrupted by the rising danger of a large section of these energy supplies becoming unavailable.

The United States, the United Kingdom, and Canada have already opted to restrict or phase out Russian oil imports, and while Germany and the EU have so far resisted, political pressure to do so is rising. Additionally, there have been rumours of' 'elf-sanctioning,' in which possible buyers have been unable to deal for political or reputational reasons, commensurate with the Russian oil barrels' increasing price discount to global benchmarks. According to press reports, funding for Russian oil commerce is also becoming more difficult. Russia has also threatened to restrict gas exports in retaliation.

The US economy has largely remained unaffected by the spike in Omicron cases around the turn of the year. GDP growth in 4Q21 was consistent with the December GEO, at 1.7% quarter on quarter (qoq) (7.0% annualised), and monthly data indicate that momentum will continue to be high in early 2022. Consumer expenditure indicators quickly recovered from a modest dip in December, while non-farm payrolls increased by an average of 580,000 in January and February. Although direct trade with Russia is limited, the spike in global oil prices is escalating what was already a serious inflation problem.

US merchandise exports to Russia and Ukraine amount for barely 0.4% of total US exports and 1% of total imports. In 2021, the US was a tiny net exporter of oil and petroleum products, and wholesale gas prices in the US have not risen as sharply as in Europe. However, the surge in global oil prices in the aftermath of Russia's invasion and subsequent sanctions is exacerbating the spike in headline inflation, which reached a 40-year high of 7.9% yoy in February.

Inflation in the United States was initially fuelled by a surge in core consumer goods prices. While it is expected that commodities bottlenecks will reduce, there is little concrete evidence of this occurring thus far. Meanwhile, inflation in the services sector continues to accelerate, reaching a 30-year high of 4.4% in February. While some of this reflects the transportation sector's reopening characteristics, the primary cause was the acceleration of house rentals. The expansion of inflation to services is a result of labour market tightening and wage growth.

GROSS DOMESTIC PRODUCT

According to the Bureau of Economic Analysis, B.E.A.) "Third" estimate, real gross domestic product (GDP) increased at an annual rate of 6.9% in the fourth quarter of 2021. Real GDP increased by 2.3% in the third quarter. The GDP estimate released today is based on more complete source data than were available for the "second" estimate in February. In the second estimate, the increase in real GDP was 7.0%. Notably, "The downward revision primarily reflected downward revisions to personal consumption expenditures (PCE) and exports that were partly offset by an upward revision to private inventory investment," as noted by Bureau of Economic Analysis.

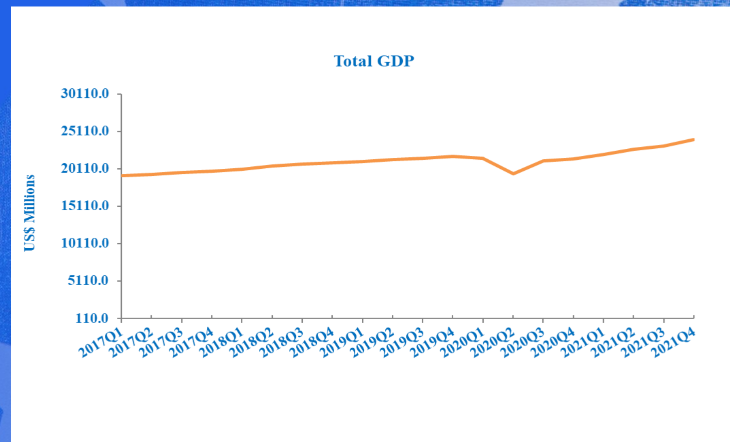
The ongoing economic impact of the COVID-19 pandemic was evident in the increase in fourth-quarter GDP. In some sections of the country, a revival of COVID-19 cases has resulted in increased restrictions and disruptions in the operations of establishments. Payments to businesses in the form of forgivable loans, grants to state and local governments, and social benefits to households also decreased, as provisions of several federal programs expired or tapered off.

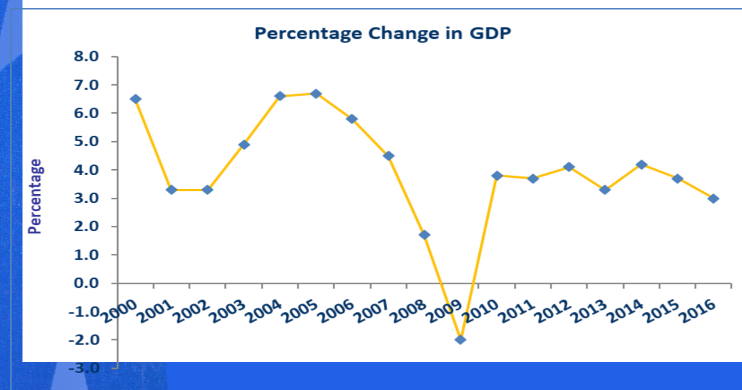
The increase in GDP was led by an increase in private inventory investment, PCE, exports and non-residential fixed investment during the fourth quarter, this was partially offset by a decline in both federal and state and local government spending. Imports increased, which is a factor in calculating GDP.

Private inventory investment increase was due wholesale trade and retail trade industries (led by motor vehicles dealers). The increase in PCE was due to an increase in services, led by health care, financial services, and insurance, and recreation. The increase in exports reflected increases in both goods and services. Notably, "the increase in exports of goods was widespread, and the leading contributors were consumer goods, foods, feeds, as well as beverages industrial supplies and materials. The increase in exports of services was led by travel," according to bea. The increase in non-residential fixed investment was mainly due to a rise in intellectual property products that was partly offset by reductions in structures.

The decrease in federal government spending was mostly due to a decrease in defense spending on intermediate goods and services. Also, the decrease in state and local government spending is as a result of a drop in gross investment (led by new educational structures). The increase in imports was mostly due to an increase in goods (led by non-food and non-automotive consumer goods, as well as capital goods).

In the fourth quarter, current dollar GDP increased 14.5% on an annual basis, or $800.5 billion, to $24.00 trillion. GDP increased by 8.4%, or $461.3 billion, in the third quarter. Furthermore, the price index for gross domestic purchases increased 7% for the fourth quarter, in contrast to a 5.6% increase in the third quarter. The PCE price index increased 6.4%, compared with an increase of 5.3%. Excluding food and energy prices, the PCE price index increased 5.0%, compared with an increase of 4.6%.





UNEMPLOYMENT

In March, total nonfarm payroll employment increased by 431,000. The unemployment rate ticked down by 0.2% to 3.6% which is 6.0 million persons in March 2022. Notably, these measures are little different from their values in February 2020 (3.5% and 5.7 million, respectively), prior to the coronavirus (COVID-19) pandemic. The job growth was spread across various industries, with leading gains in leisure and hospitality, professional and business services, retail trade, and manufacturing.

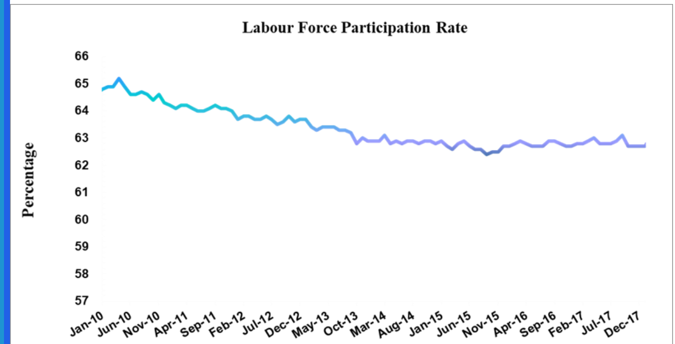
Furthermore, among the major worker groups, the unemployment rates for adult women (3.3%) declined in March. The jobless rates for adult men (3.4%), teenagers (10.0%), Whites (3.2%), Blacks (6.2%), Hispanics (4.2%), and Asians (2.8%) showed little change over the month.

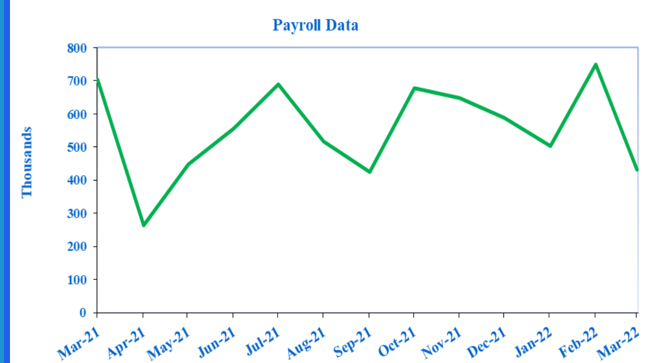
According to the BEA, among the unemployed, the number of permanent job losers declined by 191,000 to 1.4 million persons in March and is little different from its February 2020 level of 1.3 million person. The number of persons on temporary layoff was little changed over the month at 787,000 and has essentially returned to its February 2020 level. Additionally, the long-term unemployed accounted for 23.9% of all unemployed persons in March. In March, the number of long-term unemployed (those jobless for 27 weeks or more) decreased by 274,000 to 1.4 million persons.

Notably, the number of persons on temporary layoff was at 787,000 in March. The number of permanent job losers declined to 1.4 million. The number of persons not in the labor force who currently want a job increased by 382,000 to 5.7 million in March. A total of 1.4 million individuals were slightly attached to the labour force. Of the marginally attached, 373,000 persons were classified as discouraged workers in March.

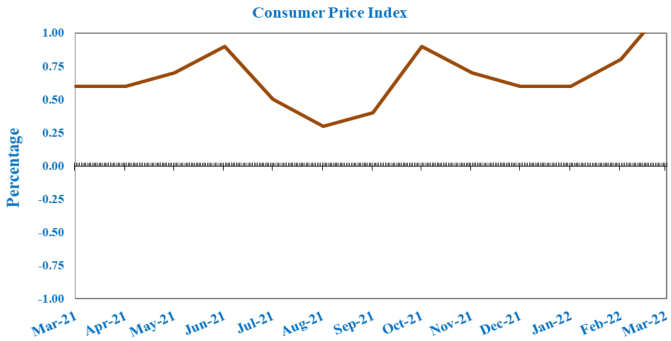
The labour force participation rate for March 2022 stood at 62.4%, while the employment population ratio changed little to 60.1%. Nonetheless, persons employed part-time for economic reasons stood at 4.2 million in March. Based on BLS assessment, “these individuals, who would have preferred full-time employment, were working part time because their hours had been reduced or they were unable to find full-time jobs.”

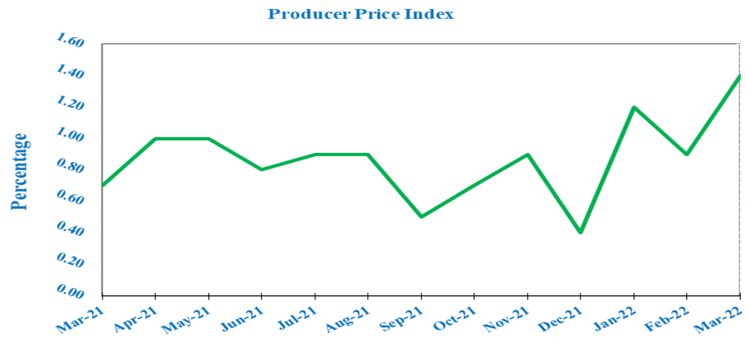
Total nonfarm payroll employment rose by 431,000 in March but is down by 1.6 million, or 1%, from pre-pandemic level in February 2020. Job growth averaged 562,000 per month in the first quarter of 2022. In the pass month professional and business services added 102,000 jobs in March 2022. Employment in leisure and hospitality continued to trend up in March (+112,000). Retail trade added 49,000 over the month. Additionally, employment in social assistance added 25,000 and construction added 19,000. Other sectors such as health care (+8,000), Financial activities (+16,000), and Manufacturing (+38,000) added to total employment. While employment in transportation and warehousing reduced by 1000 also, there was little changed shown in mining, wholesale trade, information, other services, and government.





Labour Force in Thousands	Jan-Mar	Apr-Jun	Jul-Sep	Oct - Dec
Year	Q1	Q2	Q3	Q4
2017	437,406	439,138	440,693	442,035
2018	444,015	446,253	447,645	448,865
2019	450,572	452,192	453,246	454,715
2020	455,638	401,328	421,393	427,388
2021	431,175	435,533	440,619	445,897
2022	451,163	-	-	-





CONSUMER PRICE INDEX

The Consumer Price Index for All Urban Consumers (CPI-U) rose 1.2% for March 2022, on a seasonally adjusted basis, according to U.S. Bureau of Labour Statistics (BLS) after a 0.8% increase in February. The all-items index rose 8.5% before seasonal adjustment over the last year to an index level of 287.504 (1982-84=100).

The all-items less food and energy index climbed 0.3% in March 2022 compared to January 2022 0.5% increase. Notably, "The shelter index was by far the biggest factor in the increase, with a broad set of indexes also contributing, including those for recreation, household furnishings and operations, medical care, and motor vehicle insurance." The all-items less food and energy index increased 6.5% over last 12 months with virtually all of its major component indexes rising over the span.

The index shelter accounts for nearly two thirds of the all-items less food and energy monthly increase, it rose by 0.5% in March. The rent index increased 0.4% in March, as did the owners' equivalent rent index, while there was a 3.3% increase in lodging away from home. The index for household furnishings and operations also continued to rise month over month by 1%. The index for motor vehicle insurance rose 0.7% and the index for personal care rose 0.5%. Other indexes such as airline fares (+10.7%), recreation (+0.2%) and apparel (+0.6%). While the medical care index increased 0.5% due to a 0.5% rise in physicians' services, 0.4% in hospital and offset by a 0.2% decline in prescription. Furthermore, the index for new vehicles increased 0.2% in March, while used cars and trucks fell 3.8% and communication declined 0.5%.

The index for food rose 1.0% in March, after a 0.1% increase in February. The index for food at home increased 1.5%, while the index for food away from home rose 0.3% in March. Over the last 12 months, the index for food at home and food away from home increased 10% and 6.9%, respectively.

Furthermore, Under the index for food at home, all six major store food group indexes increased in March, fruits and vegetables (+1.5%), meats, poultry, fish and eggs (+1.0%), cereals and bakery products (+1.5%), dairy and related products (+1.2) and non -alcoholic beverages (+1.2).

The food away from home 0.3% increase was mainly due to the index for full-service meals which rose 0.7% in contrast to the index for limited-service meals which declined 0.2%, its first decrease since October 2018.

Over the last 12 months all six indexes for food at home increase, notably, "the index for meats, poultry, fish, and eggs increased 13.7% over the last year as the index for beef rose 16%. The other major grocery store food group indexes also rose over the past year, with increases ranging from 7% (dairy and related products) to 10.3% (other food at home)," according to the Bureau of Labor Statistics. Furthermore, "the index for full-service meals rose 8% over the last 12 months, and the index for limited-service meals rose 7.2%. The index for food at employee sites and schools, in contrast, declined 30.5% over the past 12 months, reflecting widespread free lunch programs," in relation to the index for food away from home.

The index for energy increased 11% in March, after a 3.5% increase in February. This movement was due to a sharp 18.3% increase the gasoline index. Meanwhile, the index for natural gas increased 0.6% whereas the electricity index increased 2.2% in March.

The energy index rose 32% over the past 12 months with all major energy component indexes increas-

PRODUCER PRICE INDEX

The seasonally adjusted Producer Price Index for final demand gained 1.4% in March 2022, according to the US Bureau of Labor Statistics. Following gains of 0.9% in February and 1.2% in January 2022. Final demand prices increased 11.2% for the 12 months ended March 2022 on an unadjusted basis, the largest increase since 12-month data were first calculated in November 2010.

The increase in the final demand index in March can be attributed to a 2.3% increase in final demand goods prices. Notably, "Over half of the broad-based advance in March can be traced to a 5.7% jump in prices for final demand energy. The indexes for final demand goods less foods and energy and for final demand foods also moved higher, 1.1% and 2.4%, respectively." according to the U.S Bureau.

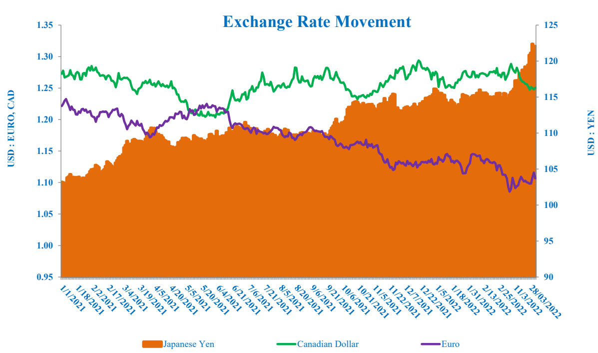
Following a 0.3% increase in February 2022, prices for final demand services increased 0.9% in March 2022. Notably, "Over 40% of the March advance can be traced to a 1.2% rise in margins for final demand trade services. (Trade indexes measure changes in margins received by wholesalers and retailers.)" There was a 5.5% increase for final demand transportation and warehousing services. Prices for final demand services excluding trade, transportation, and warehousing increased by 0.3%.

The final demand foods index rose 2.4% (February 2.1%) and for energy rose 5.7% (February 7.5%). Prices for final demand products, excluding food, energy and trade services increased by 0.9% in March, the largest advance since rising 1.0% in January 2021. For the 12 months ended in March, the index for final demand less foods, energy, and trade services increased 7.0%.

U.S. DOLLAR

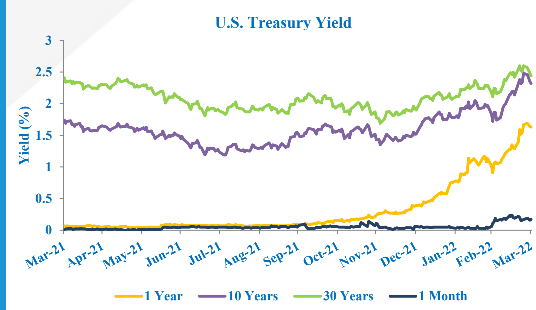
For March 2022, the EUR/USD pair closed at $1.1067 versus $1.1125 at the start of the month, a 0.52% decrease. According to FX empire, this decrease is as a result of "EUR/USD is currently trying to settle below 1.1100, while the U.S. dollar is moving higher against a broad basket of currencies. The U.S. Dollar Index is currently testing the resistance at 97.50. If this test is successful, the U.S. Dollar Index will move towards the next resistance at 97.75, which will be bearish for EUR/USD."

Looking ahead, "EUR/USD is currently trying to settle below the support at the 20 EMA at 1.1050, while the U.S. dollar is moving higher against a broad basket of currencies. The U.S. Dollar Index has recently managed to get above 98.50 and is moving towards the resistance level at 98.70. In case the U.S. Dollar Index gets to the test of this level, EUR/USD will find itself under more pressure."



U.S. TREASURY YIELD CURVE

The 3-month Treasury bill rate stood at 0.52% up from February's 0.35%. The 5-year rate rose to 2.42% in March 2022 relative to 1.71%, a month earlier. The 10-year rate (also constant maturity) increased to 2.32%, from February's 1.83% and January's 1.79%.



GOVERNMENT DEBT/ DEFICIT

The Congressional Budget Office (CBO) indicated that the federal budget deficit amounted to $667 billion for the first six months of fiscal year 2022.

Furthermore, for the first six months of the fiscal year 2022, CBO estimates receipts to amount to $2,122 billion, $418 billion more than in the similar period in 2021.

However, based on CBO estimates for six months of the fiscal year 2022, outlays are estimated to total $2,788 billion, a $622 billion less relative to the same period last year.

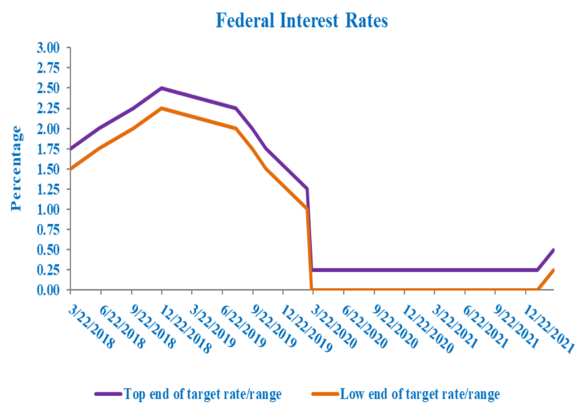
Budget Totals, October-February

Billions of Dollars

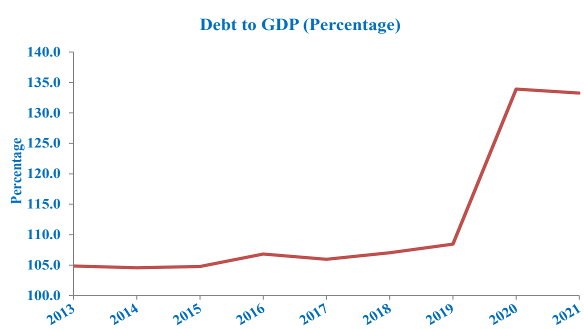
	Actual, FY2021	Preliminary, FY 2022	Estimated Change
Receipts	1,704	2,122	418
Outlays	3,410	2,788	-622
Deficit (-)	-1,706	-666	1,040

FEDERAL RESERVE MINUTES

The Federal Reserve approved a 0.25 percentage point rate hike, the first increase since December 2018. The Federal Reserve believes that indicators of economic activity and employment have continued to strengthen. Job gains have been strong in recent months, and the unemployment rate has declined substantially. However, inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher energy prices, and broader price pressures.



The invasion of Ukraine by Russia is causing tremendous human and economic hardship. The implications for the U.S. economy are highly uncertain, but in the near term the invasion and related events are likely to create additional upward pressure on inflation and weigh on economic activity.



The Federal Reserve cites, “The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With appropriate firming in the stance of monetary policy, the Committee expects inflation to return to its 2 percent objective and the labor market to remain strong.” To support these goals, the Committee decided to raise the target range for the federal funds rate to 1/4 to 1/2 percent and anticipates that ongoing increases in the target range will be appropriate. In addition, the Committee expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities at a coming meeting.

The Board of Governors of the Federal Reserve System voted unanimously to raise the interest rate paid on reserve balances to 0.4 percent, effective March 17, 2022. The Committee will continue to monitor the implications of incoming information for the economic outlook. The Committee would be prepared to adjust the stance of monetary policy as appropriate if risks emerge that could impede the attainment of the Committee’s goals.