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**LATEST U.S. ECONOMIC OUTLOOK**

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# U.S. Economic Outlook Report: **Spending Power Strong Despite Higher Prices**

***Prevedere Director of Economic Services, Michelle Green, provides a personal view on topical economic issues***

**While there is evidence of improvement in supply-side drivers of inflation, this update focuses on more persistent inflationary pressures and how they may impact the economic recovery this year with a specific emphasis on wage growth.**

## Labor Market Recovery

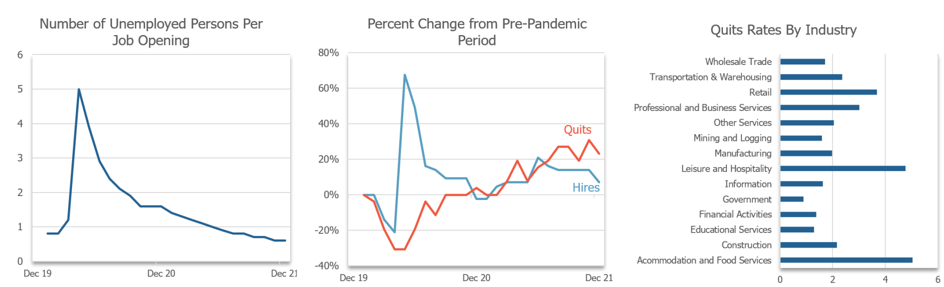
GDP growth in the 4th quarter of 2021 was very strong with Omicron having a slight impact on spending in December. Upcoming data for January is expected to show that the slowdown continued early in the month before rebounding toward the end as the direct threat of Omicron seems to have peaked. Consumer spending is still robust and continues to shift back toward services as consumers gradually return to pre-pandemic routines. Inflation remains a key concern as higher prices eat into consumer wallets, posing a significant risk to spending and therefore economic recovery as a whole.

This particular labor market recovery has been extraordinary. In recent months, everyone's experienced the effects of unexpected business closures, longer wait times, school cancellations, and more - all because there are not enough workers to keep running at full capacity.

The real question at this point is whether this is a frictional imbalance in response to COVID, or whether this is a structural reallocation of labor.

## Has the U.S. Reached Full Employment?

Full employment is typically indicative of a healthy economy that is steadily growing, where anyone who wants a job can get one and where wage growth is moderate, but not steady or putting significant pressures on prices. Once that level is passed, there is a risk that wage pressures build which would put upward pressures on consumer prices as employers seek to pass on higher labor costs to the consumer.




Source: Bureau of Labor Statistics

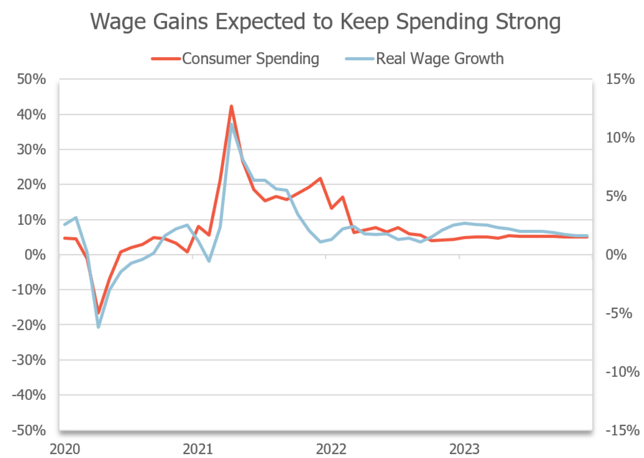
Full employment is the point where the ratio of unemployed persons to available jobs is 1. Prior to the pandemic, the U.S. was already at that point, and perhaps even passing that point. Today, it appears the U.S. is back at that point again.

## Labor Market Exits

Labor market exits are still exceptionally high with January numbers reflecting increased hesitancy of workers. Throughout the pandemic period, exits from the labor market were concentrated heavily in front-line sectors, but there's evidence now that this has spread across a wide range of occupations and industries. The "great resignation" is showing no signs of slowing as workers are reevaluating their employment and demanding a higher premium for work performed.

Reluctance is particularly high from key worker segments, with higher exits among older workers and working parents. In addition to exits, there are fewer new workers entering the labor market from overseas, all of which is reducing the pool of available labor.

## Wage Growth to Support Future Spending


Source: Prevedere

There is absolutely no doubt that wage pressures are growing. Wage growth has been exceptionally strong, even outpacing the highest levels of inflation the U.S. has seen in decades. On one hand, this could mean higher consumer prices are here to stay as employers seek to offset some of these costs, but there are also reasons to be encouraged by these numbers.

It's important to keep in mind that this is no ordinary labor market. In reality, it's unlikely that the U.S. is at a structural level of full employment. As concern over COVID continues to dissipate throughout the coming months and greater mobilization becomes more consistent, many workers are expected to return to the labor force, especially parents and immigrants. This return to the labor force will begin to moderate wage pressures throughout the year and contribute to a slow down in consumer price growth. That said, workers that are currently active in the labor force will benefit from a higher overall level of wages in the long term.

Overall, when thinking about the impact of rising prices, waning government support, and consumer finances in general, there are some positive signs that these wage gains, along with the drawdown of higher savings, will keep spending strong this year and keep the recovery moving forward.

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