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provides a personal view on topical economic issues

June 2023 Economic Outlook: Forecasting the Second Half of 2023 and 2024

Key takeaways:

- **Prevedere's economic baseline scenario predicts a mild US recession as measured by overall GDP will still likely develop in the second half of this year.**
- **Inflation is expected to trend toward the Fed's target benchmark rate by year-end 2024, which could provide a path for the Fed to lower rates and help accelerate the economic recovery.**
- **The labor market is currently tight, but the trend is loosening, and the unemployment rate will begin to move mildly higher next year as the impacts of this mild recession are felt. However, the labor imbalance is likely to remain more elevated than during past recessions, which will help fuel the recovery in 2024.**

This June Economic Outlook report dives into the future trajectory of the U.S. economy in 2024.

The upcoming recession is the most forecast in history, and as a result many companies are focusing on what will happen during the recession and are neglecting to plan for recovery that will follow.

At Prevedere, we predict a mild recession beginning in the second half of 2023. But companies need to be prepared for the impacts of economic recovery that is likely to take hold in 2024.

This report discusses the three possible economic scenarios for the recession in 2023, three economic themes that will help drive economic recovery, and how companies' experiences will differ in 2024.

Current Economic Scenarios

Prevedere has calculated three different possible economic scenarios for the next two years.

The **baseline scenario**, which is the most probable path of the US economy, predicts a mild decline in overall GDP to develop in the second half of this year. The recession will be relatively mild. The depth of the decline or the steepness of this recession is likely similar to 2001 and significantly more mild than the 2008/2009 financial crisis.

The most **optimistic scenario** is that the economy will move sideways through the second half of this year and into 2024 with no actual quarter-over-quarter GDP contraction. In this best-case scenario, growth will reaccelerate in 2024.

The most **pessimistic** or worst-case scenario is where we see the recession developing in the second half of this year, but it starts more intense and extends a little longer through the first half of 2024. In this pessimistic scenario, the recession would be more profound and longer as inflation remains more stubborn, and the Fed cannot lower interest rates as quickly as in the baseline scenario. However, even in this most pessimistic scenario, we see economic recovery, as measured by GDP, by late 2024.

Stabilizing Inflation

When considering inflation's impact, economists look at headline CPI, flexible CPI, and sticky CPI. The headline CPI, or total CPI, is most often quoted. Flexible CPI is the things that respond to price very quickly, like energy and gasoline prices, etc. Sticky inflation describes prices that take longer to respond, like shelter or service prices.

Flexible price inflation has been easing in recent months. This is generally a result of lower supply chain backlogs, declining commodity prices, and transportation bottlenecks dissipating.

However, sticky price inflation remains elevated, although it is starting to turn over and move in the right direction. The impending contraction in consumer spending is likely to help with some of the more sticky components of inflation, like services inflation. As consumers start to pull back and thus lower demand for some of these services, we might see the inflation rate decrease at a more favorable pace.

Headline inflation is expected to continue moving downward toward the Federal Reserve's goal.

Likely, inflation will not reach the Fed's target goal in 2023 or 2024, but it is trending in the right direction.

Overall, the decreasing inflation rate will be a good sign for economic recovery in 2024.

Lower Interest Rates

The Federal Reserve has been increasing interest rates since March of 2022 to combat rampant inflationary pressures. The effects of higher interest rates increase the cost of borrowing and thus curb aggregate demand in the economy as it becomes more expensive to obtain financing and credit. Yet, these effects are lagged.

Feeling the full effect of changing interest rates on overall economic activity is delayed. In fact, the U.S. economy has yet to experience the full extent of the increases that the Fed has already put in place.

On the flip side, when the Fed does start to lower interest rates early next year, while this will help further the recovery, consumers will feel the extent of these decreases or the majority of the upside of the lower interest rates in 2025. The expectation is that with inflation trending in the right direction, the Fed will be able to reduce interest rates again next year.

Decreased interest rates will help spur more robust economic growth in 2025. The most robust part of the economic recovery could happen in the early portion of 2025, fueled by stabilized inflation, lower interest rates, and a strong labor market.

Resilient Labor Market

The current tightness in the labor market will shift to being a positive driver of the economic recovery in 2024, once inflation has eased. Currently, the labor market is very tight. All organizations have felt a significant imbalance between labor supply and labor demand. The number of unemployed persons per job opening is less than 0.5, meaning there are two job openings for every unemployed person in the labor market.

Although the labor market is currently tight, it is starting to trend toward loosening. The unemployment rate will begin to increase as the impacts of this recession are felt, but it will be mild relative to historical recessions. Through 2025, the unemployment rates are expected to range from 3.74 to 4.5. These rates represent low levels of unemployment in an economic slowdown because of the current tightness in the labor market that will remain.

Since many businesses have struggled to find the right talent over the last few years to fill their open jobs, they will be hesitant to let go of labor during this downturn in fear of having to repeat filling that role again. As a result, we expect fewer jobs to be lost during this recession than traditionally seen during other economic downturns.

Low job loss numbers will lead to an opportunity for a quicker recovery. The economy will be ready to recover in 2024 due to fewer job losses combined with stabilized inflation and lower interest rates.

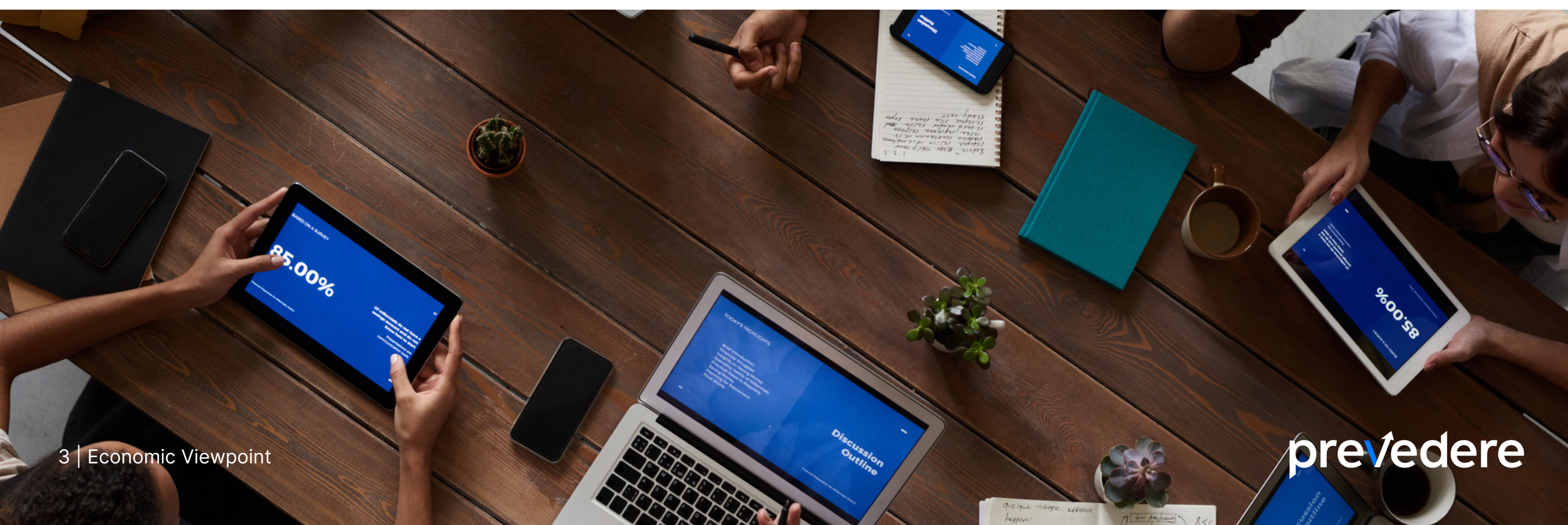
Questions for Businesses to Consider While Planning for 2024

Executives need to understand where they fall in this business cycle. Even though we know a recession is coming, adequately preparing for this downturn means that your organization can identify which external themes directly impact your group.

Here are some economist-led questions to consider while planning for economic recovery:

- Are you an industry that will feel the downturn early?
- Are you already starting to feel a downturn?
- Given who your customer is, will you feel the impacts of a recession later on?
- Will this recession help drive your sales because you are a counter-cyclical business?
- Can you proactively take advantage of recovery?
- When is the timing of when your business will recover?
- How will your core consumer and unique business drivers play into recovery opportunities?

Businesses must be able to directly quantify the impact that this economic downturn will likely have on their organization. Utilizing these specific leading indicators will allow you to pinpoint and predict future business performance. Even though this recession is extensively discussed, that doesn't translate to knowing how the downturn will impact your business. Successful organizations must identify, quantify, and predict how these external themes of recession and recovery will affect their business over the next two years.



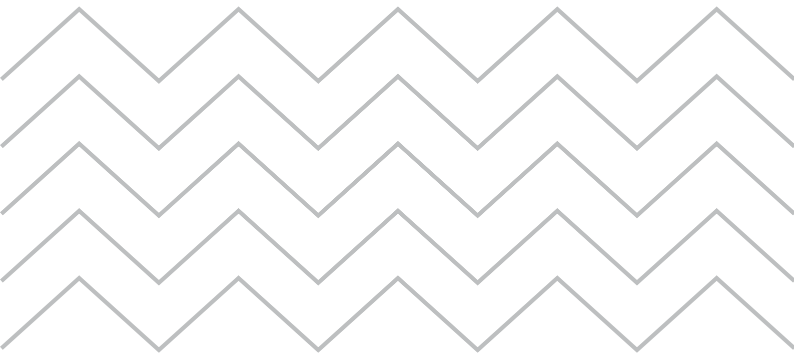
Conclusion

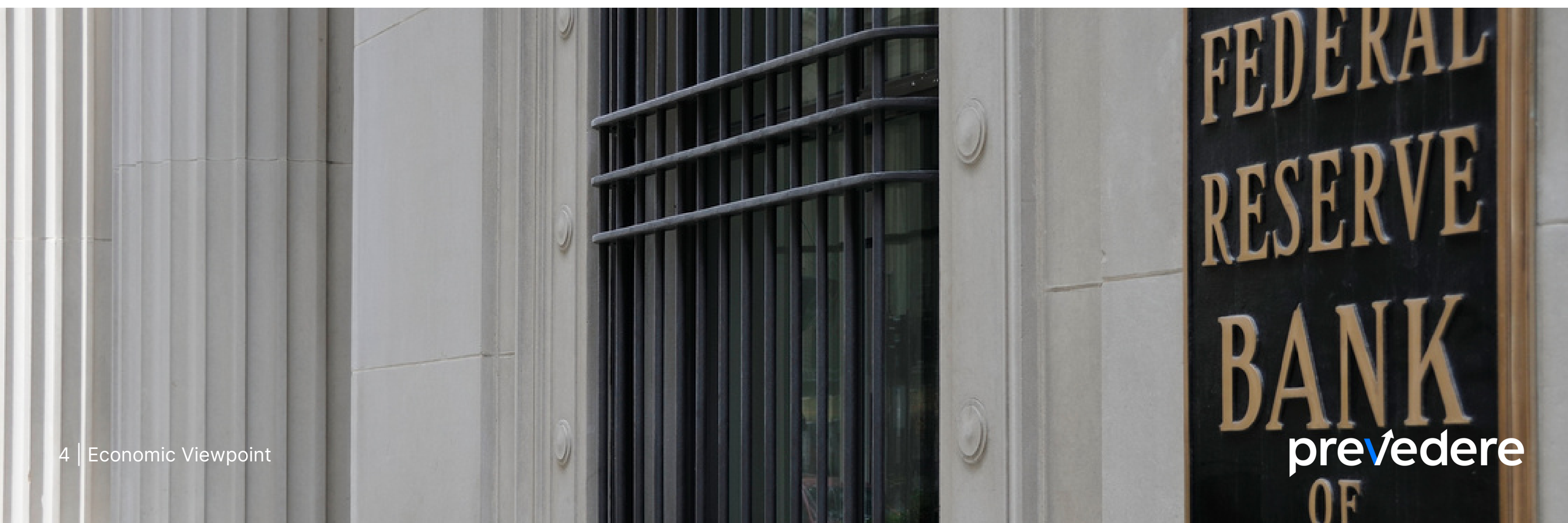
Three main factors will likely spark this resurgence in growth next year: stabilizing inflation, lower interest rates, and the resilient labor market.

We expect inflation to continue trending meaningfully toward the Fed's target rate. Stabilizing inflation indicates that the Fed has accomplished its goal of cooling the demand side inflationary pressures by the contraction and aggregate demand in the overall economy.

The easing inflationary pressures will help drive the 2024 recovery, which coincides with lower interest rates. With inflation trending in the right direction, the Fed will have the flexibility to lower interest rates next year to help spur economic growth into 2025.

Finally, the continuous resiliency and the tightness in the labor market will help aid the economic recovery. The unemployment rate will increase slightly during this downturn, but remain relatively low compared to previous recessions. Therefore, fewer jobs will be lost during the downturn, which will help the recovery gain a solid footing relatively quickly in 2024.





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