Office of the Comptroller of the Currency

U.S. ECONOMIC SNAPSHOT

July 2022

GDP fell for the second straight quarter; recession risk rising

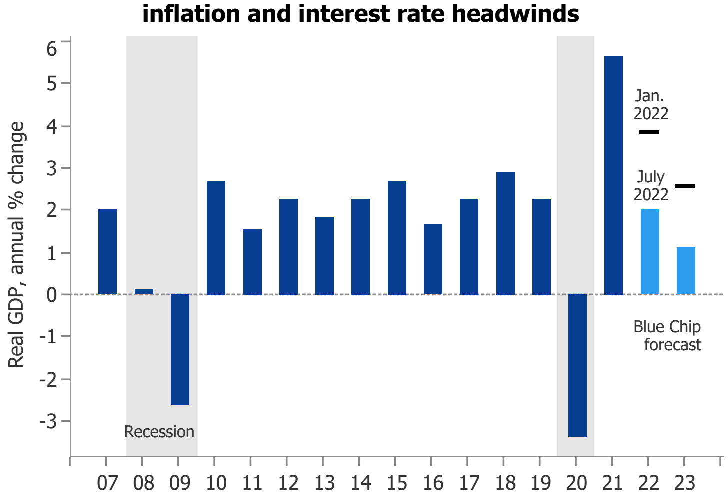
• Real GDP fell by 0.9 percent at an annual rate in 2Q:2022. The decline followed on the heels of a 1.6 percent decrease in the previous quarter as rising interest rates triggered a 14 percent plunge in residential construction and slowed consumer and business spending. A 1.9 percent decrease in government expenditures placed a further drag on activity. Two consecutive quarters of decline in real GDP meets a common definition of recession. But an official verdict is based on a range of indicators, most of which have continued to expand since December. The Blue Chip Consensus (Consensus) forecast for annual real GDP growth has slowed since January, see Figure 1, and the July forecast puts the probabilities of recession at 36 percent for this year and 49 percent in 2023.

• The labor market remains strong, but there are signs it has started to cool. Average job growth in 2022 is slower than the pace of the prior year. See Figure 2. Weekly jobless claims, while still low by historical standards, have risen by 50 percent since early April. But strong hiring in July, which was above expectations, will place pressure on the Fed to keep an aggressive tightening posture.

• Inflation is forecast to slow but will probably remain well above the Fed's target in 2022. See Figure 3. But the outlook is uncertain as economic models are built to forecast business cycles not pandemics. Supply chain problems eased in 2022, but persist and continue to weigh on supply. Although mounting inflation pre-dated the Ukraine crisis, the event has exacerbated price pressures. Stagflation, with high unemployment and inflation for an extended period of time, could also ensue if wages and prices start to accelerate in tandem.

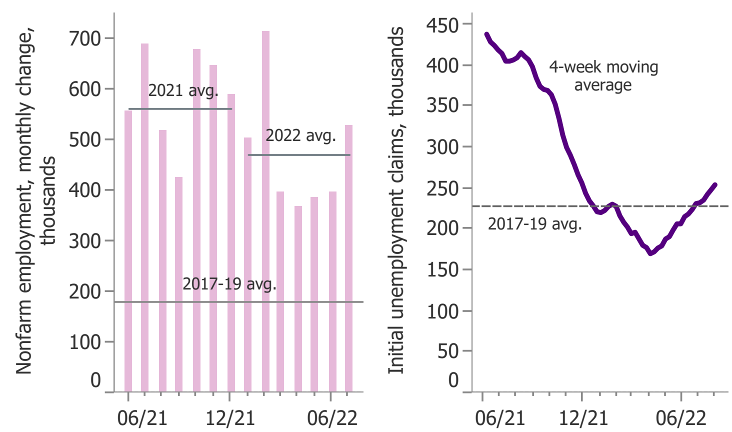
• The Fed's tightening cycle has been aggressive and is expected to continue to prioritize price stability over GDP growth. The 3-month Treasury bill yield is up sharply this year due to tightening monetary policy, with the Consensus expecting it to reach a peak of 3.3 percent by mid-2023. See Figure 4. Though not yet evident in the quarterly averages shown, the 10-year Treasury yield has fallen 82 bps since mid-June on expectations that the economy could weaken further. A flattening yield curve indicates slower growth and a rising risk of recession.

Figure 1: GDP forecast revised downward on inflation and interest rate headwinds



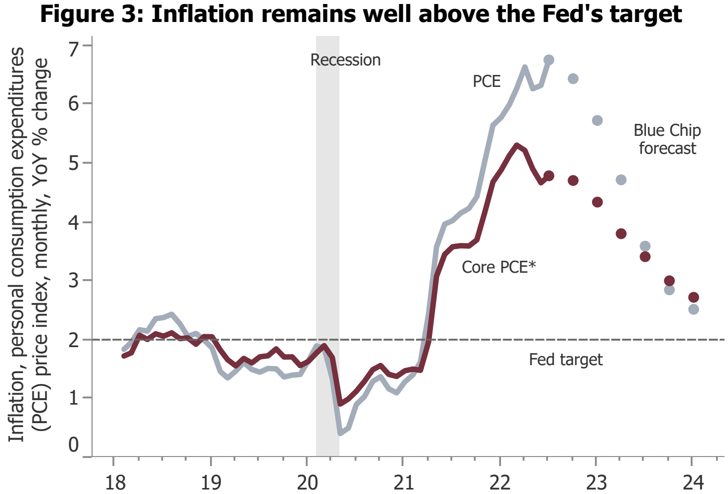
Sources: BEA, Blue Chip Economic Indicators (July 2022)

Figure 2: Job growth remains strong but signs of a softening labor market have emerged



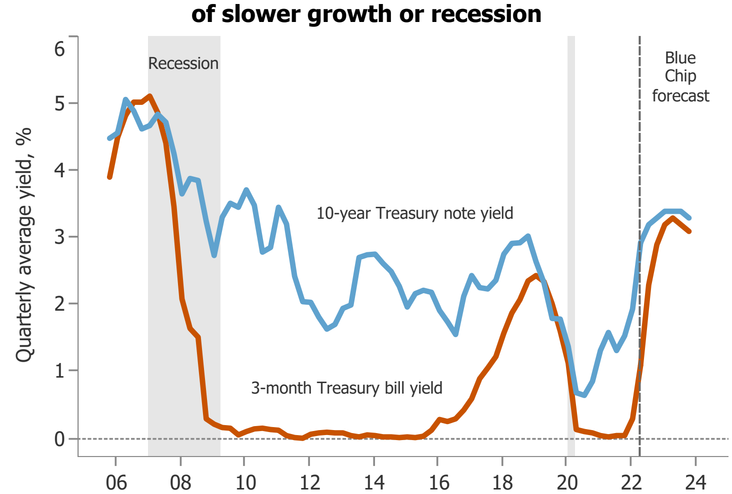
Sources: Bureau of Labor Statistics (July 2022), Depart. of Labor (July 30, 2022)

Figure 3: Inflation remains well above the Fed's target



Sources: BEA (June 2022), Blue Chip Economic Indicators (July 2022)
*excludes food and energy

Figure 4: Yield curve flattening on expectations of slower growth or recession



Sources: Federal Reserve (2Q:2022), Blue Chip Economic Indicators (July 2022)