

Greater Kansas City Chamber of Commerce Economic Forecast Breakfast December 8, 2022

U.S. and KC Economic Forecast

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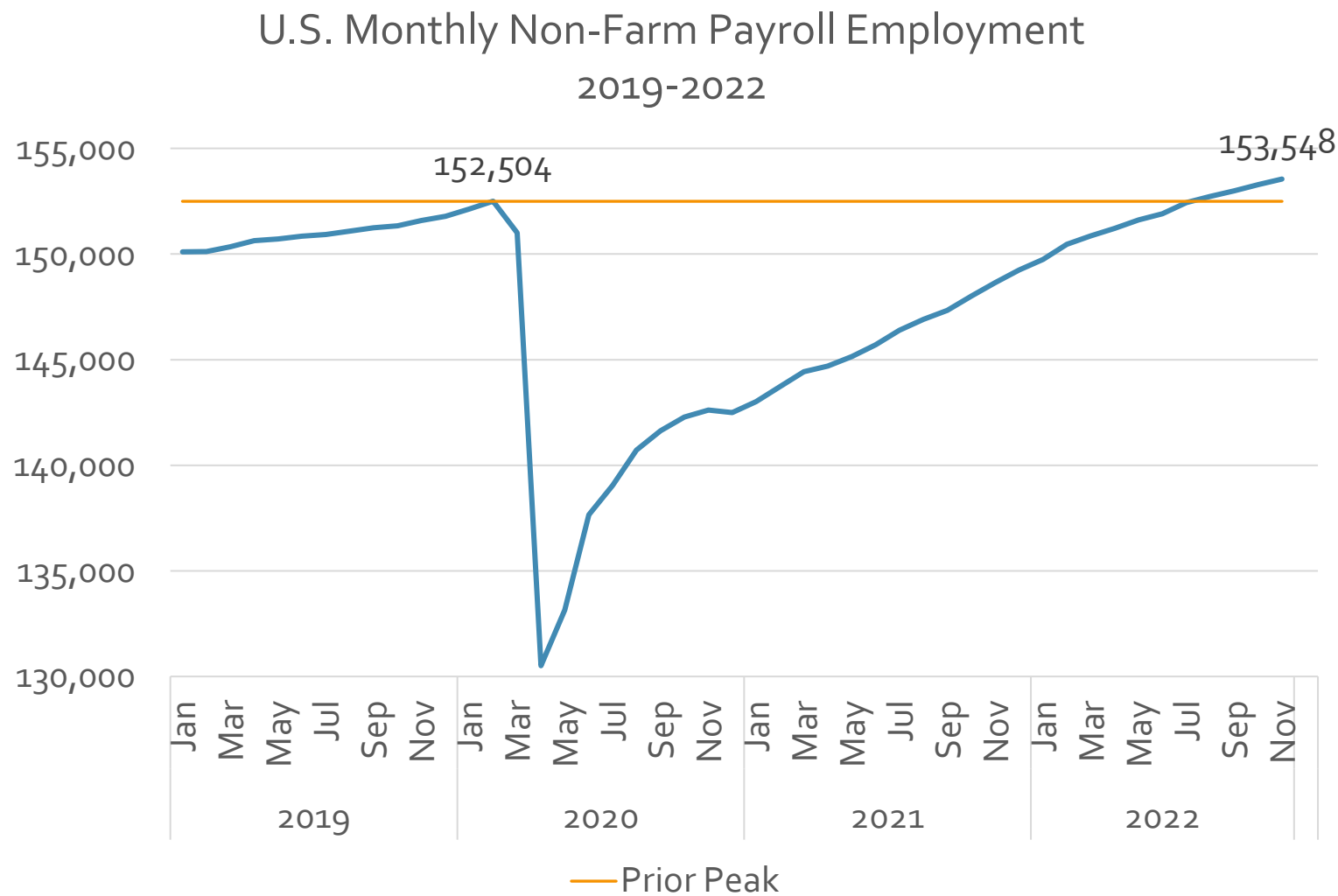
U.S. Economic Situation and Forecast



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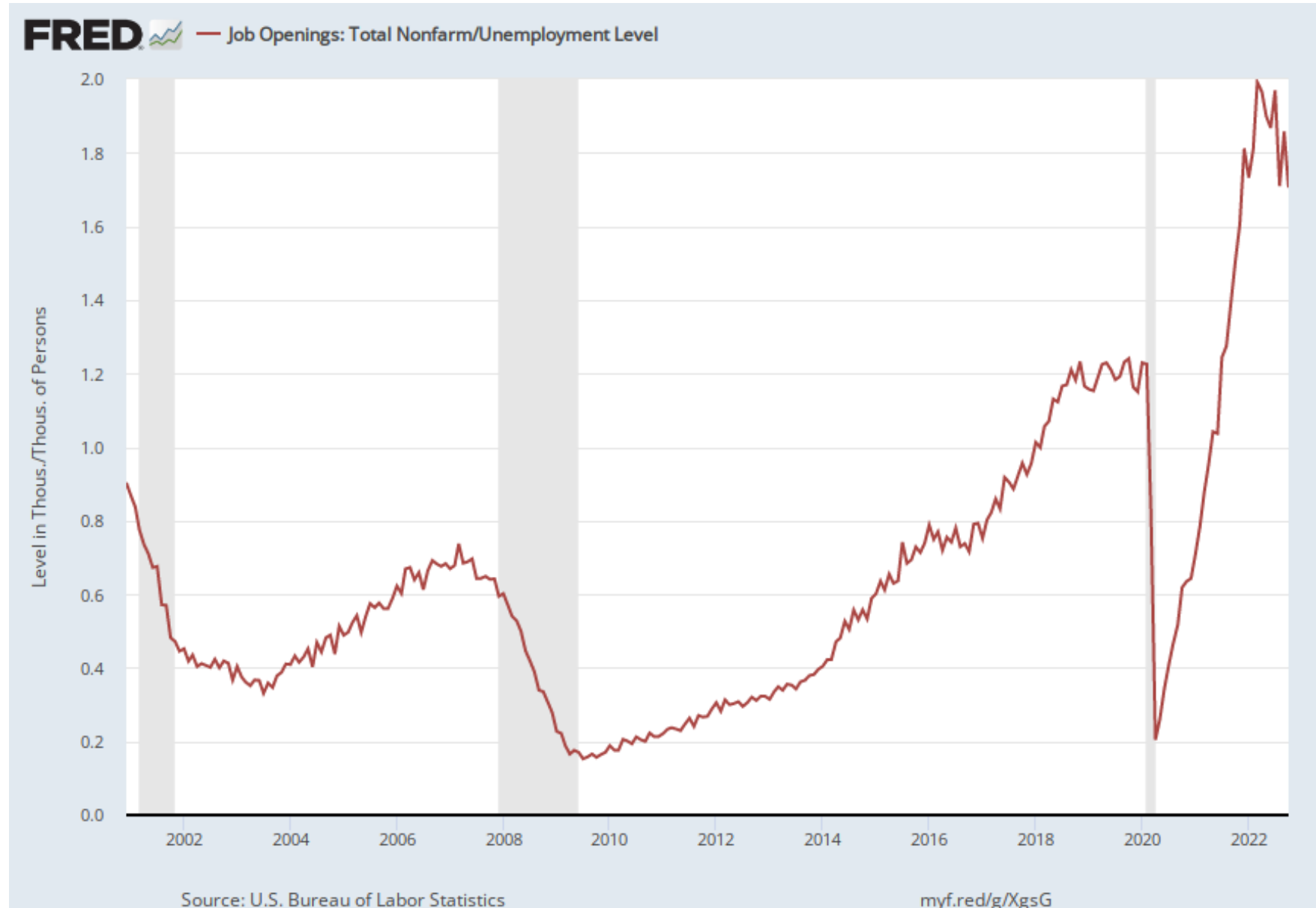
U.S. jobs reached their pre-pandemic peak in August 2022. Monthly payroll employment has slowed from 537,000 in July to 263,000 in November. This is still more than twice as much as the working age population grows each month, and so reflects an economy pulling more people into the labor force.

Source: BLS



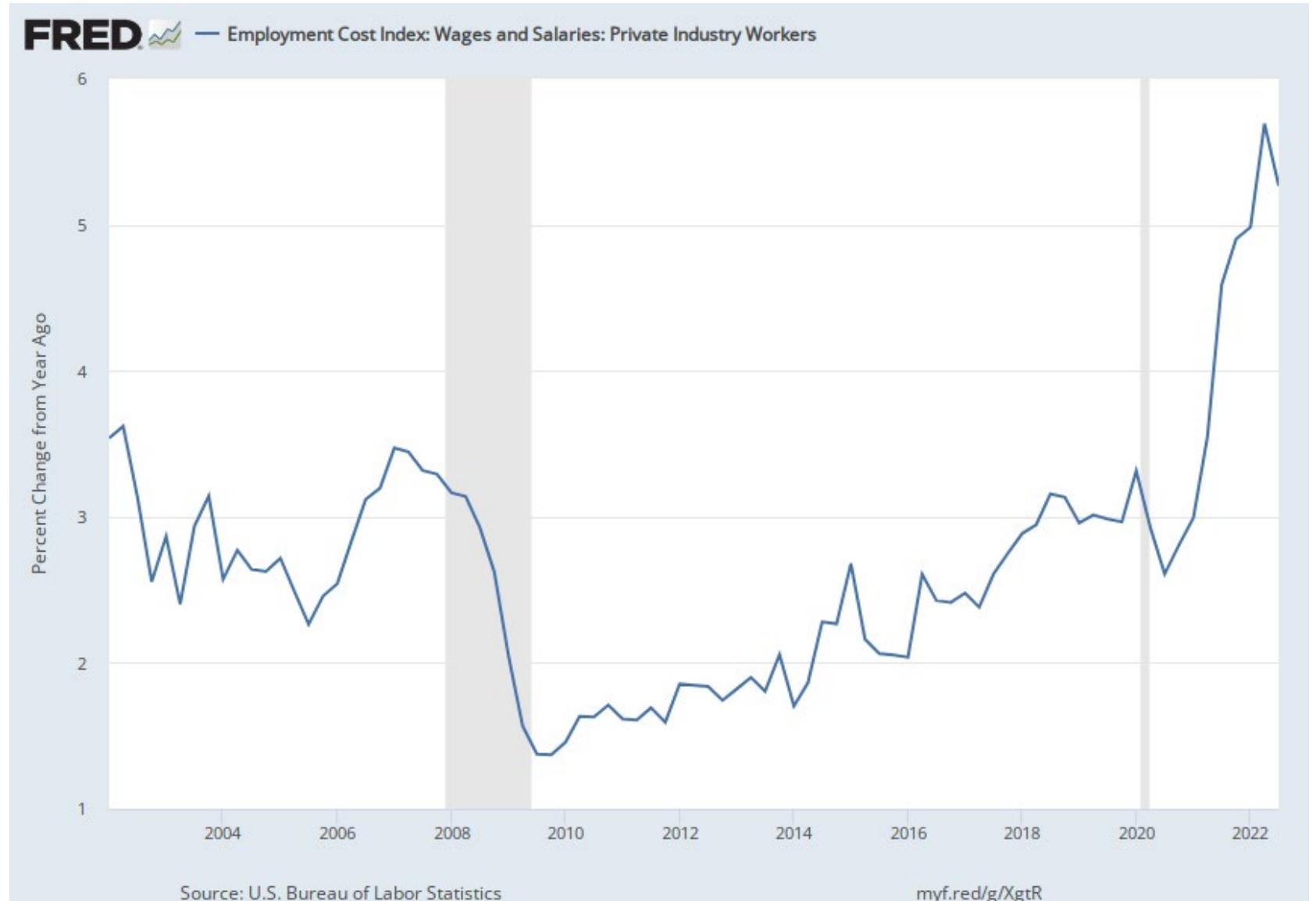
U.S. Job Openings Per Unemployed Persons, 2001-2022

Further evidence that the job market is cooling comes from recent declines in the numbers of job openings. Yet, there are still 1.7 jobs for every unemployed person in the country, indicating a job market that is much tighter than it was pre-pandemic.



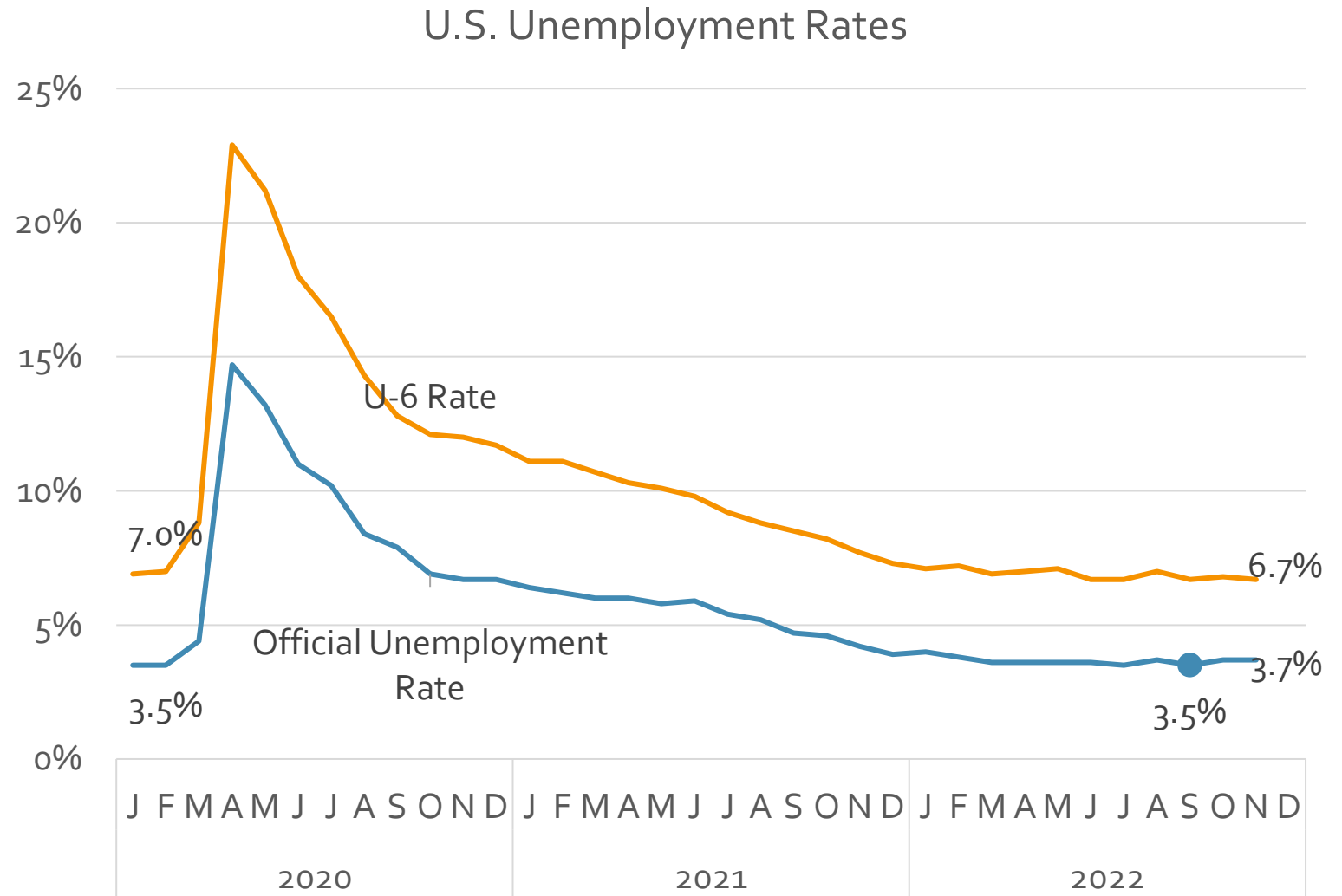


As a result, while the rate of wage increases may have come off their peak, at 5.3 percent over the past year they are still well above pre-pandemic norms



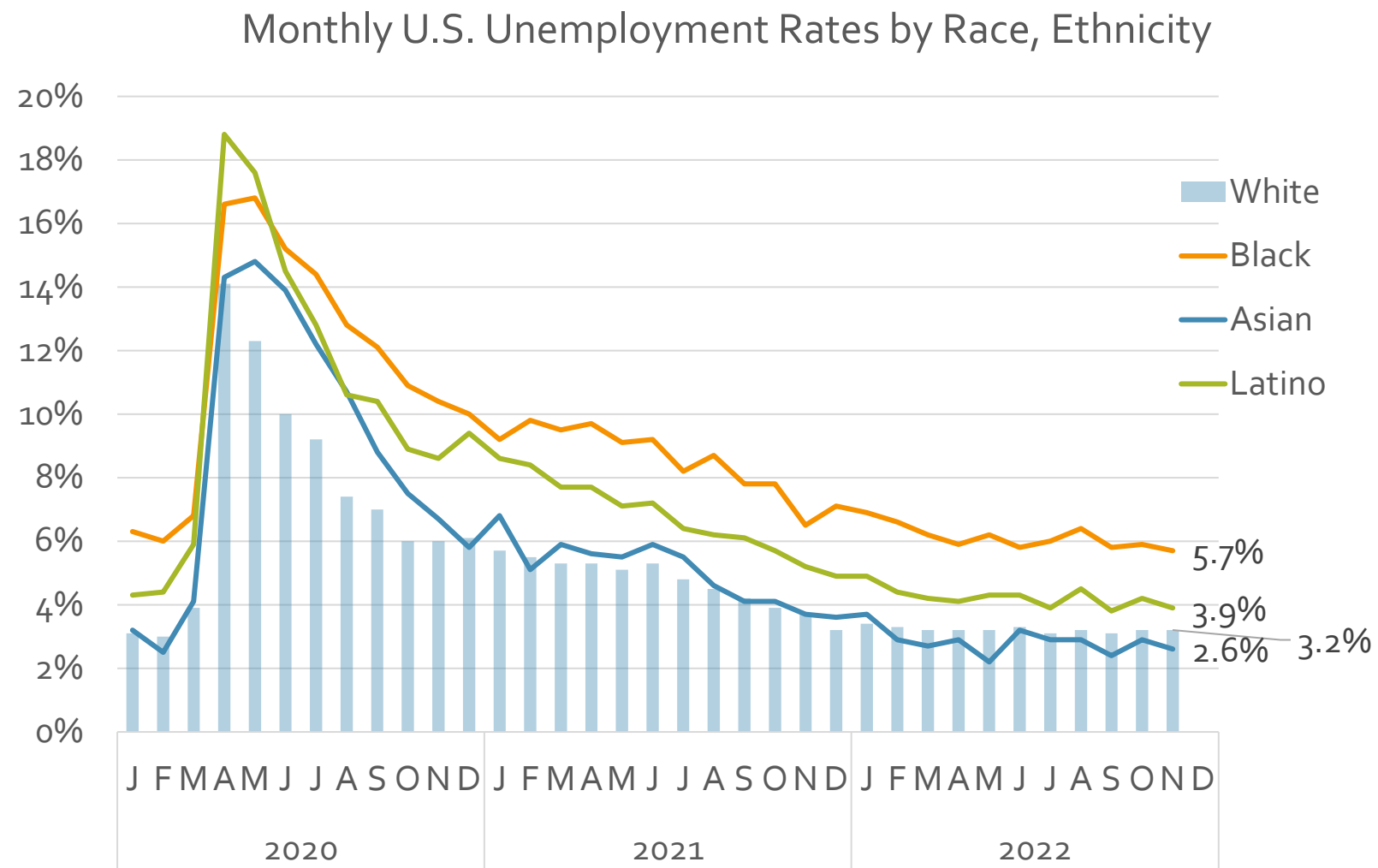
The official unemployment rate has come off its post-pandemic lows, but just barely at 3.7 percent. Meanwhile, the rate that includes discouraged workers and part-time workers who want a full-time job is 0.3% *below* its pre-pandemic low.

Source: FRED



Despite an economy seemingly running at full capacity, the unemployment rate for Black workers is 80% higher than that of White workers, while Latino workers' unemployment rate is about 20% higher. Asian unemployment, at 2.6% is the lowest of all racial groups.

Source: Bureau of Labor Statistics

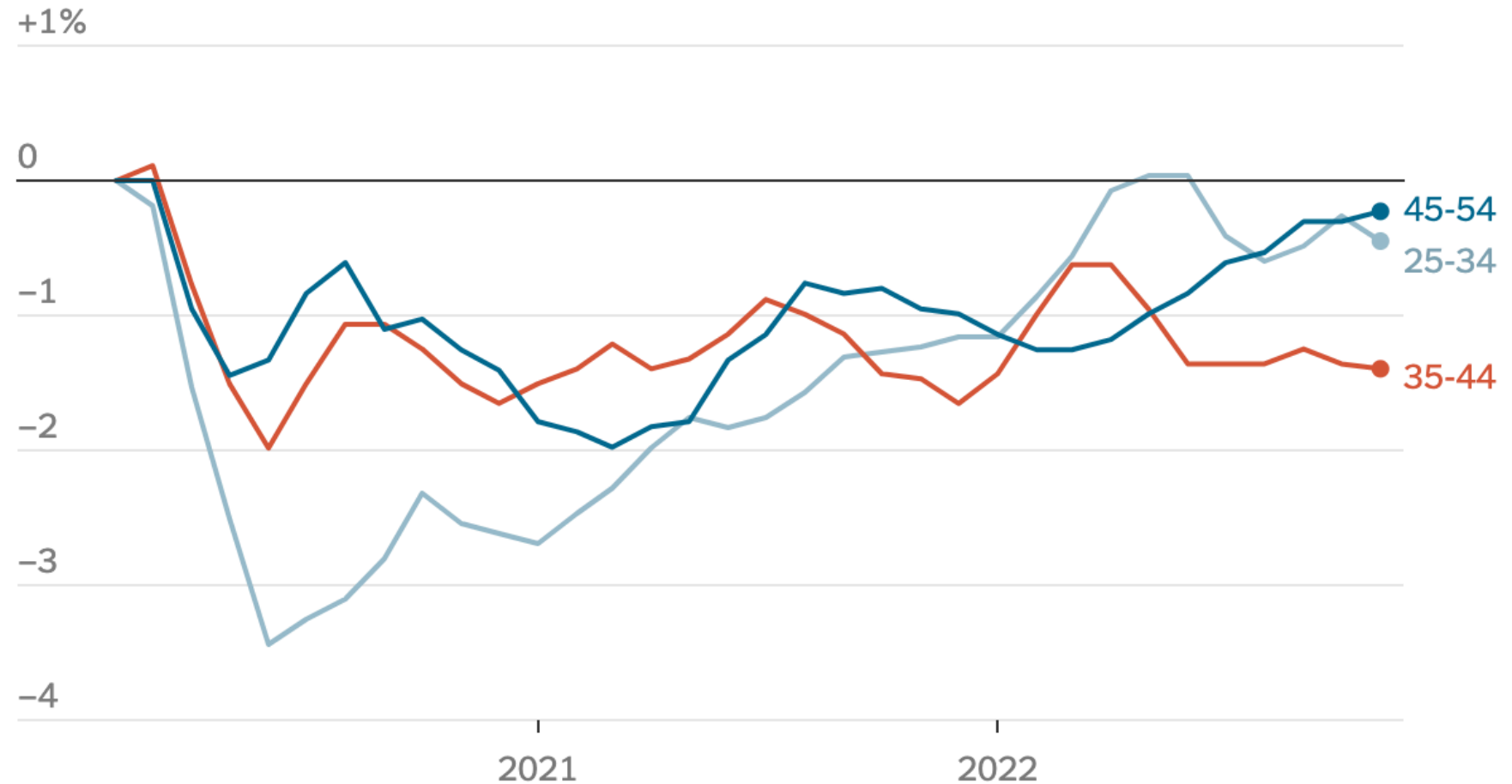




How the male labor force shifted during the pandemic

Men ages 35-44 are working or looking for work at a notably lower rate than before the pandemic.

Change in male participation rate since Feb. 2020 by age group



Note: Three-month rolling average of seasonally adjusted data • Source: Bureau of Labor Statistics • By The New York Times

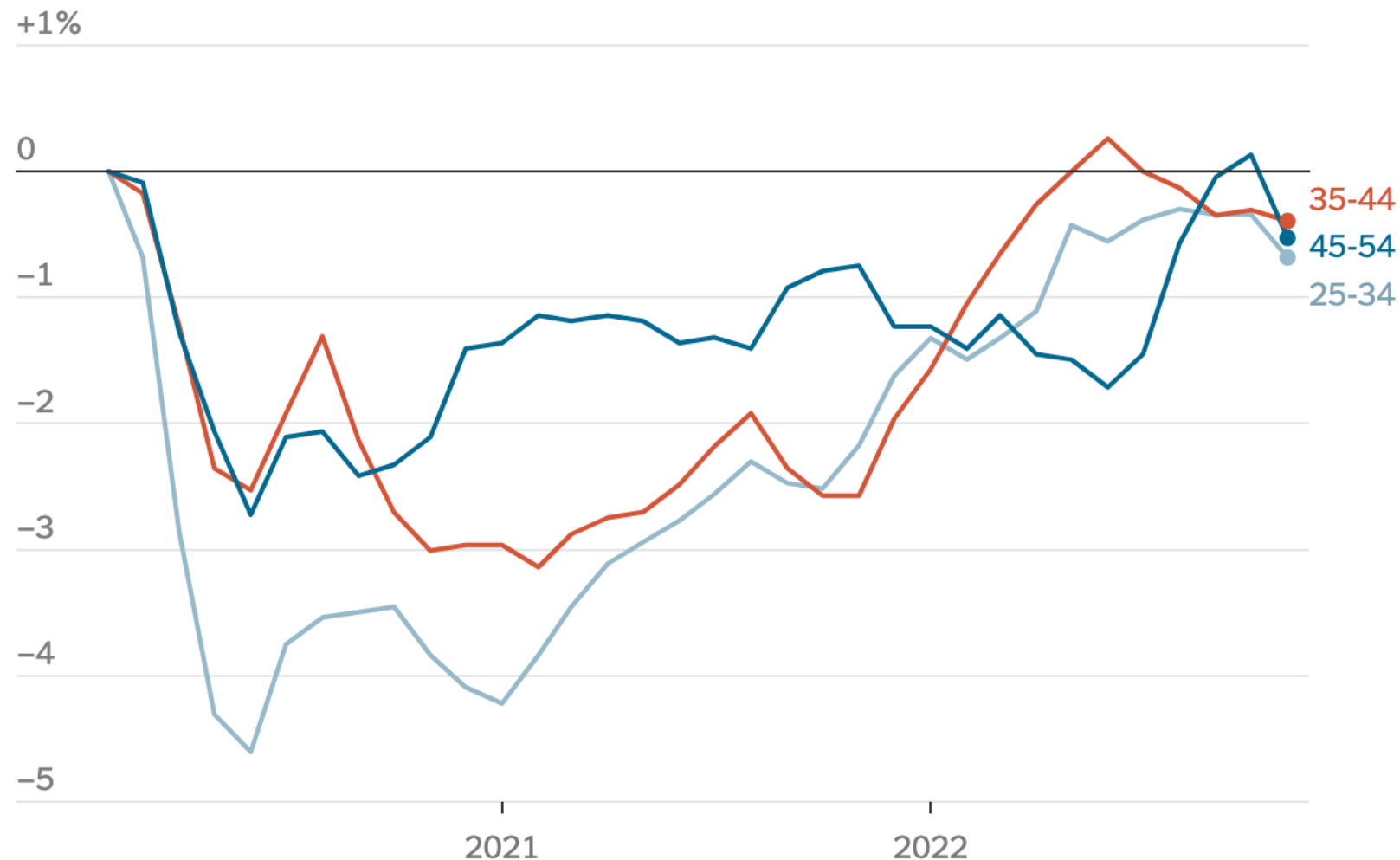
Similarly, despite high labor demand, middle-aged men (35-44) have been reluctant to return to the labor force. Reasons why this demographic group is lagging are not clear.

By contrast, most women in their prime working ages (25-54) have returned to the labor force at rates similar to before the pandemic

How the female labor force shifted during the pandemic

Women ages 35-44 are working or looking for work at similar rates relative to before the pandemic.

Change in female participation rate since Feb. 2020 by age group



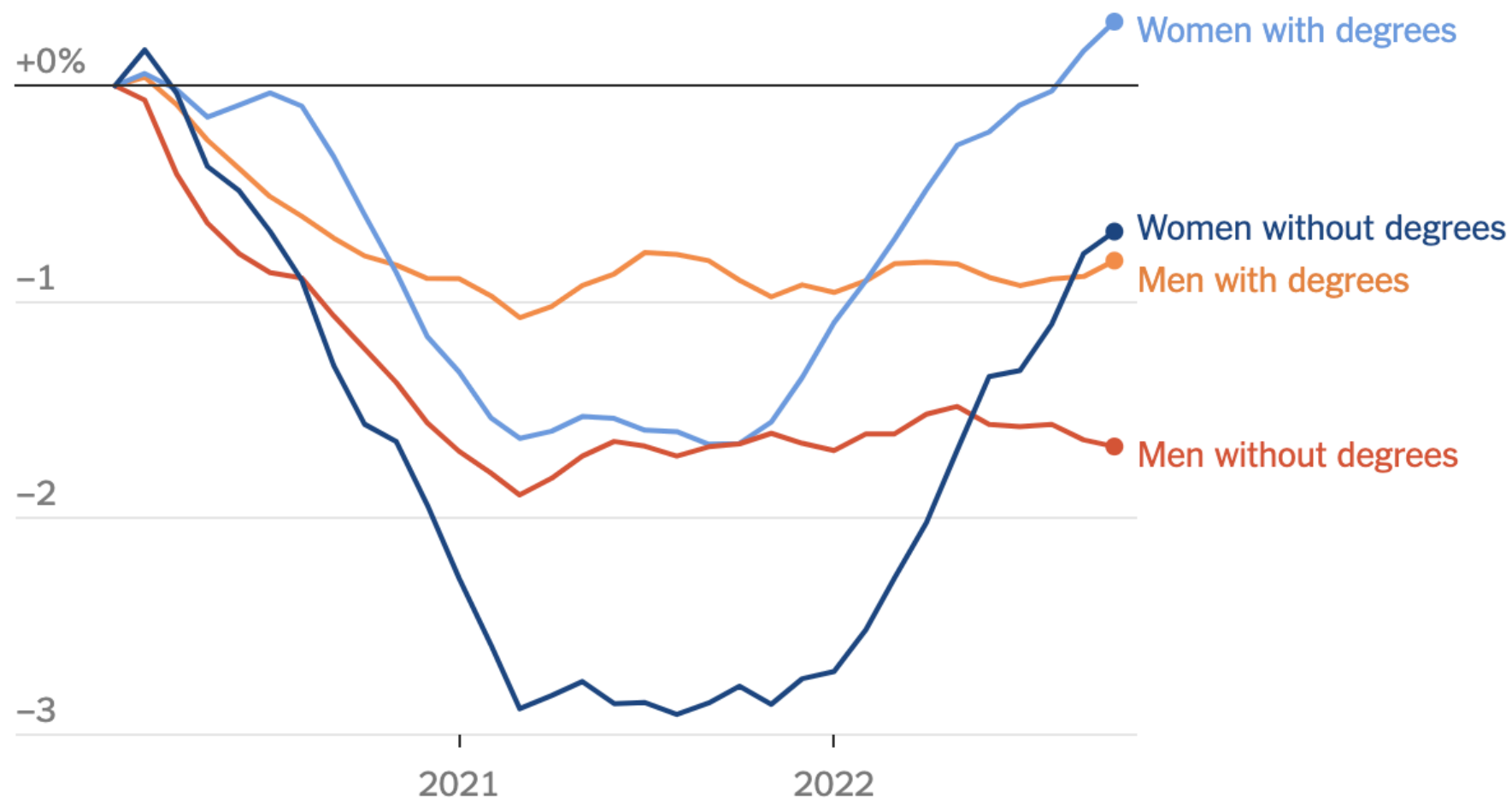
Note: Three-month rolling average of seasonally adjusted data • Source: Bureau of Labor Statistics • By The New York Times



An education gap

People without a four-year college degree have returned to the labor force more slowly than others in the same age group.

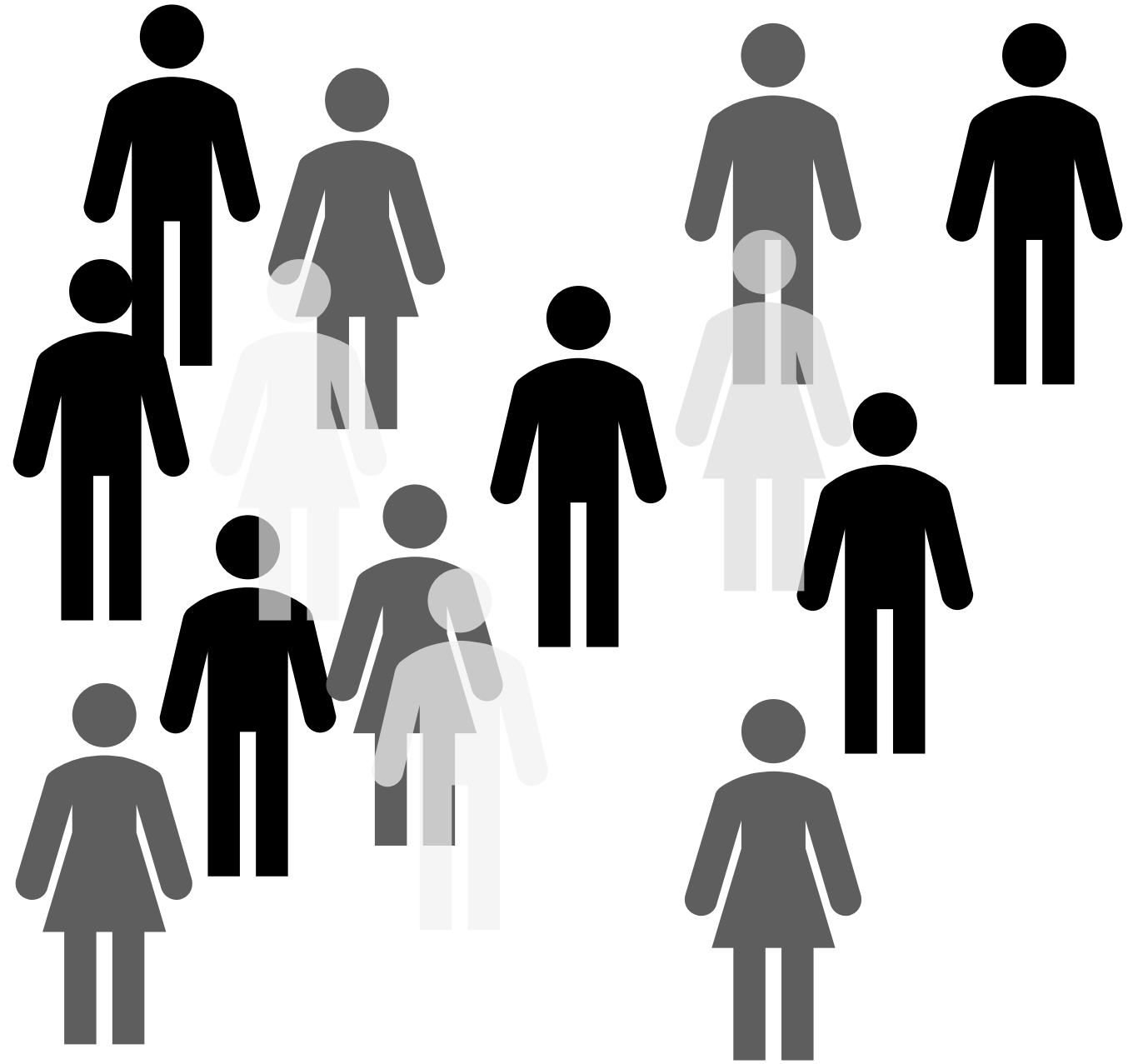
Change in participation rate for people ages 35-44



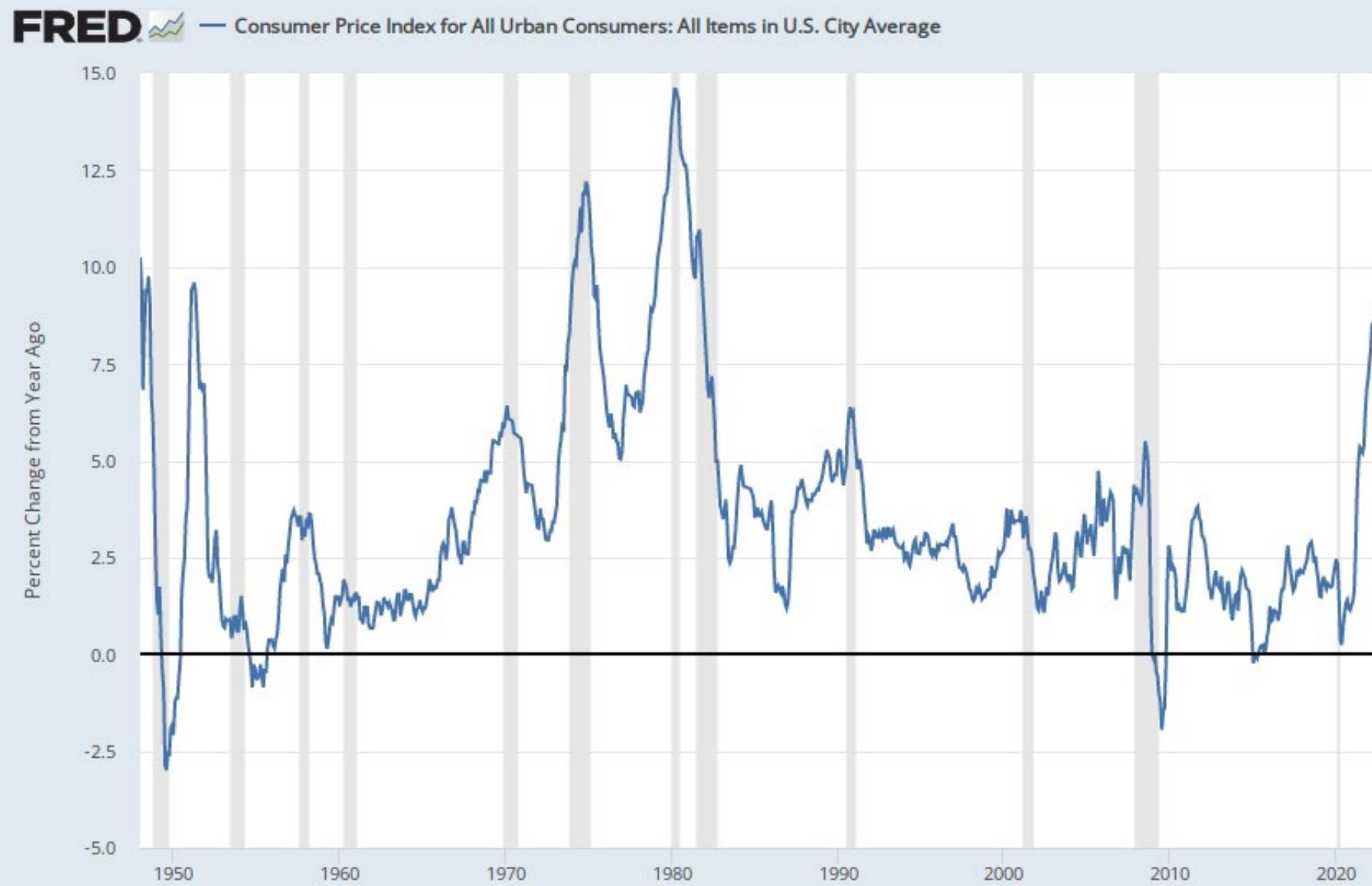
Note: 12-month rolling average, not seasonally adjusted • Source: Current Population Survey via IPUMS • By The New York Times

Regardless of gender, education level appears to have a significant impact on a person's ability to return to the workforce. But only women with a four-year degree have returned at rates that match their pre-pandemic levels.

So we have this paradox – exceptionally high labor demand, rising wages, yet it is insufficient to fully employ all groups. What will it take for these missing workers to rejoin the labor force?



High labor demand but limited supply is one key factor fueling inflation. CPI is at 40 year high due to the combination of pent-up demand meeting supply side shocks and limitations. The only good news? It still not close to the peak in the 1980s...

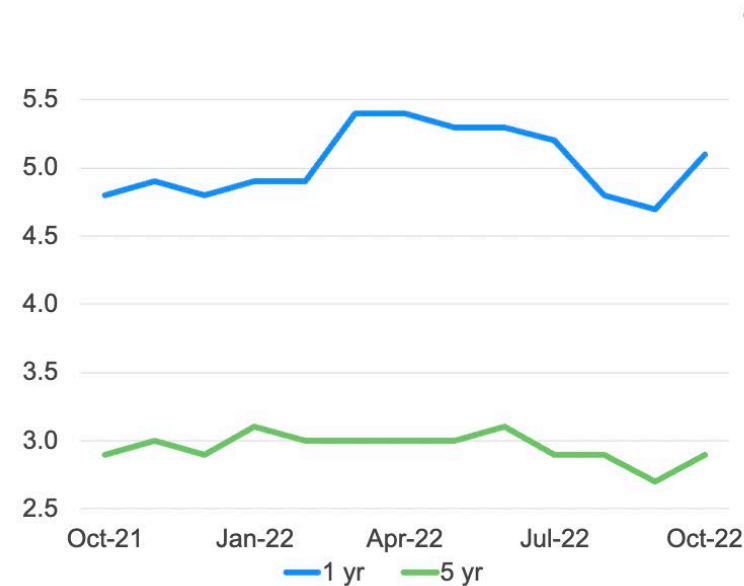


Source: U.S. Bureau of Labor Statistics

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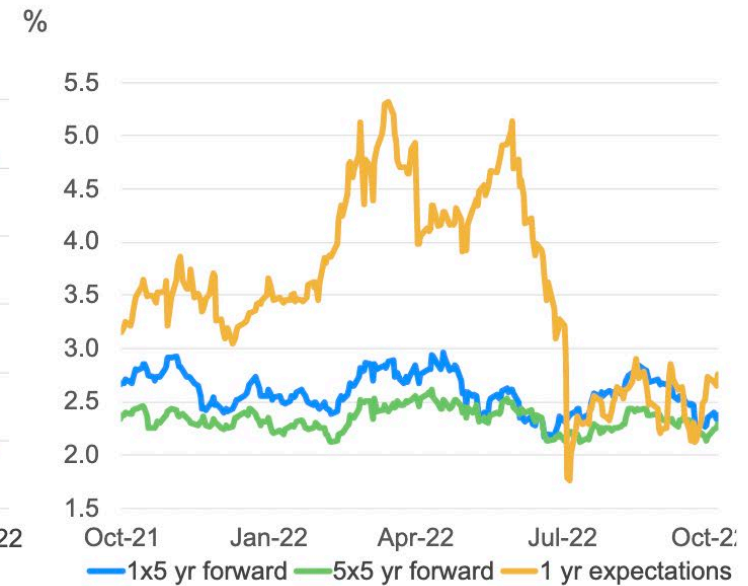
...and inflationary expectations still seem to be well-anchored (though perhaps creeping up).

University of Michigan Survey

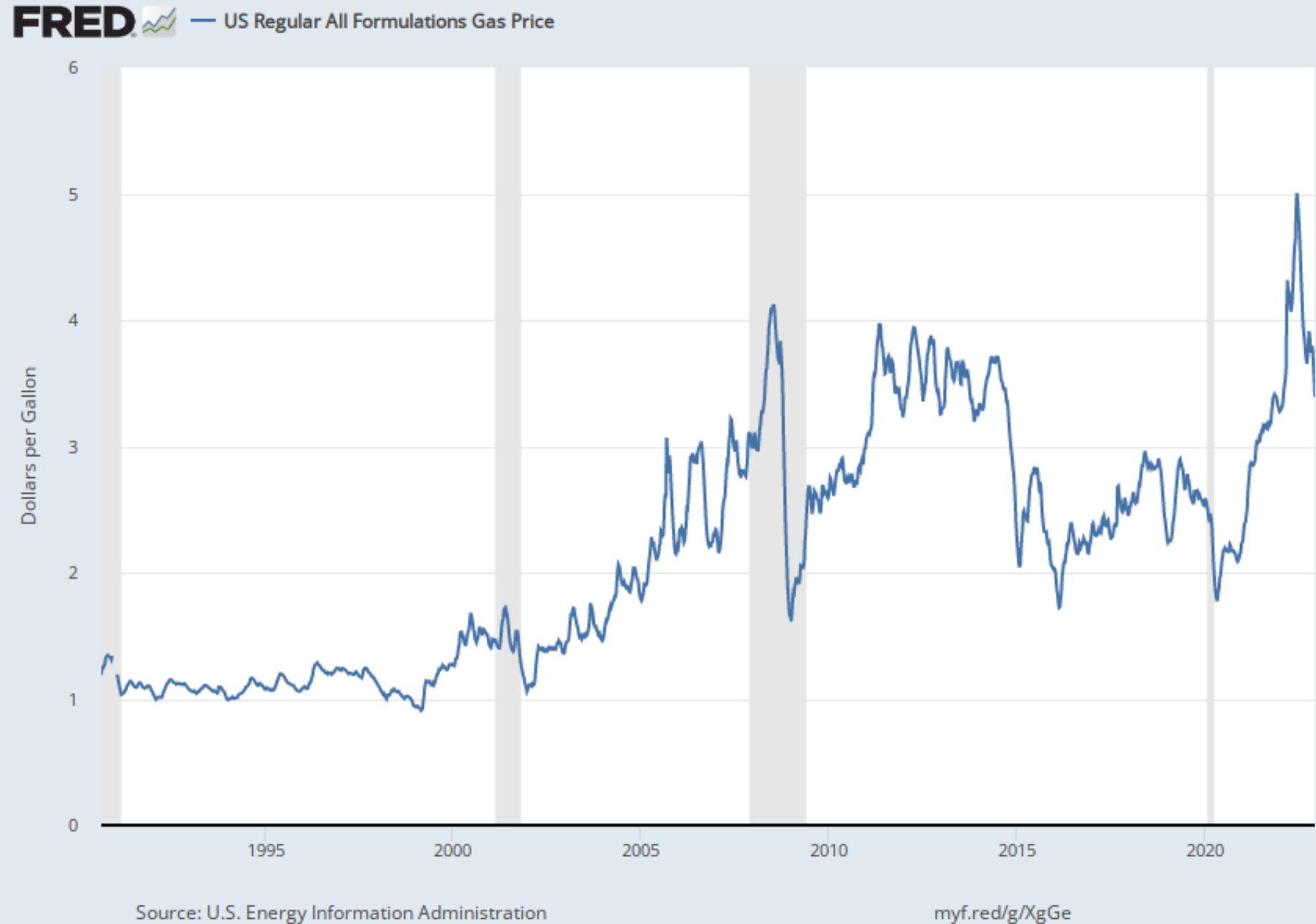


Sources: Univ. of Michigan, ICE, Moody's Analytics

Bond Market

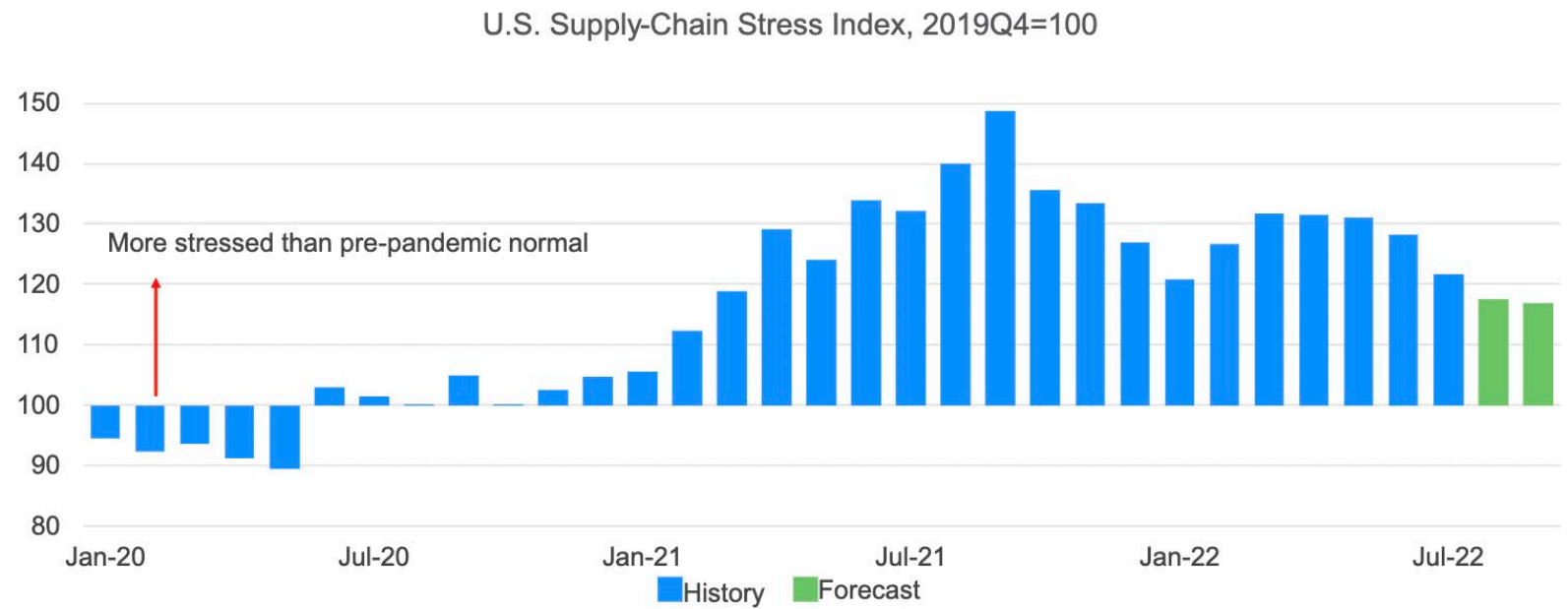


After briefly touching \$5/gallon in early summer, U.S. average gasoline prices have come down to \$3.39 a gallon. This puts them at the level experienced between 2011 and 2013, though still about \$1 more than pre-pandemic.



Supply bottlenecks appear to be generally moderating, though they are still elevated.

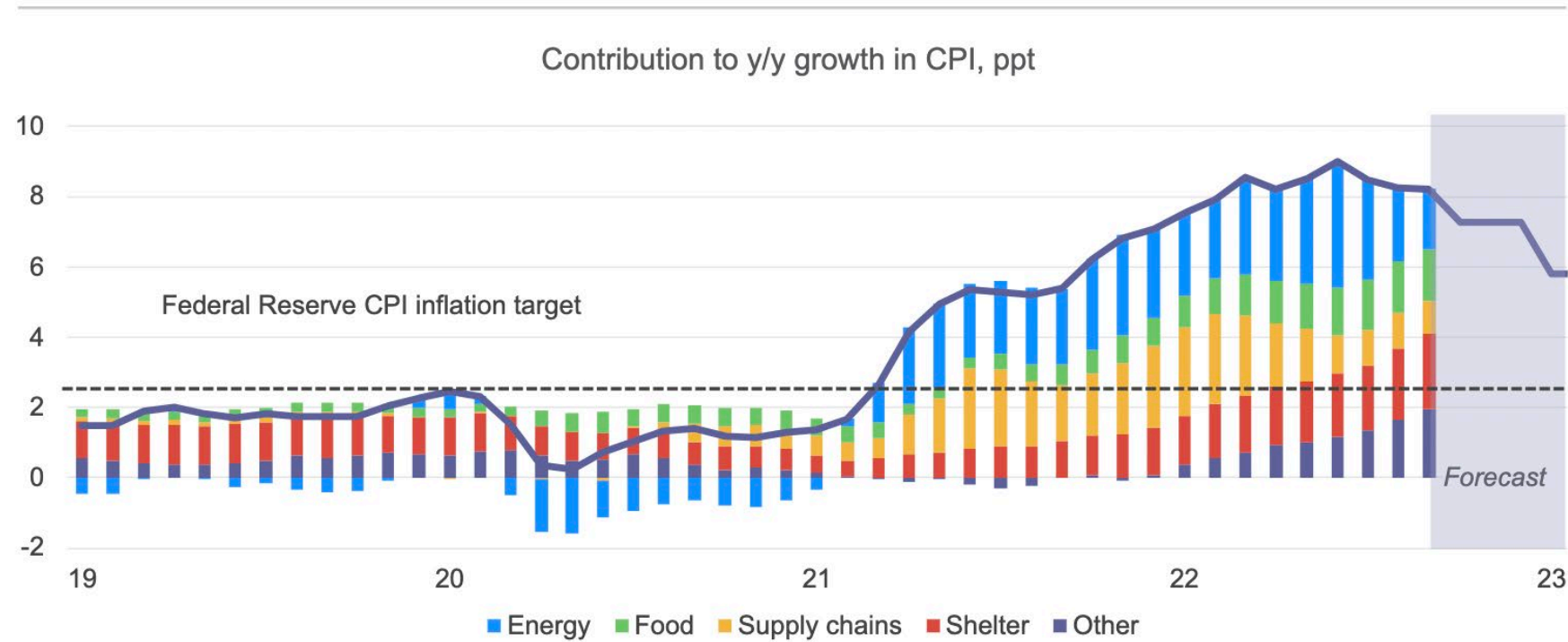
Summer Is for Destressing



Source: Moody's Analytics

As a result, supply chain pressures and energy prices are contributing less to inflation. Instead, 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.

Supply-Chain Stress Contributing Less to Inflation



Sources: BLS, Moody's Analytics

Moody's Analytics:

November 2022 Assumptions for Baseline Forecast

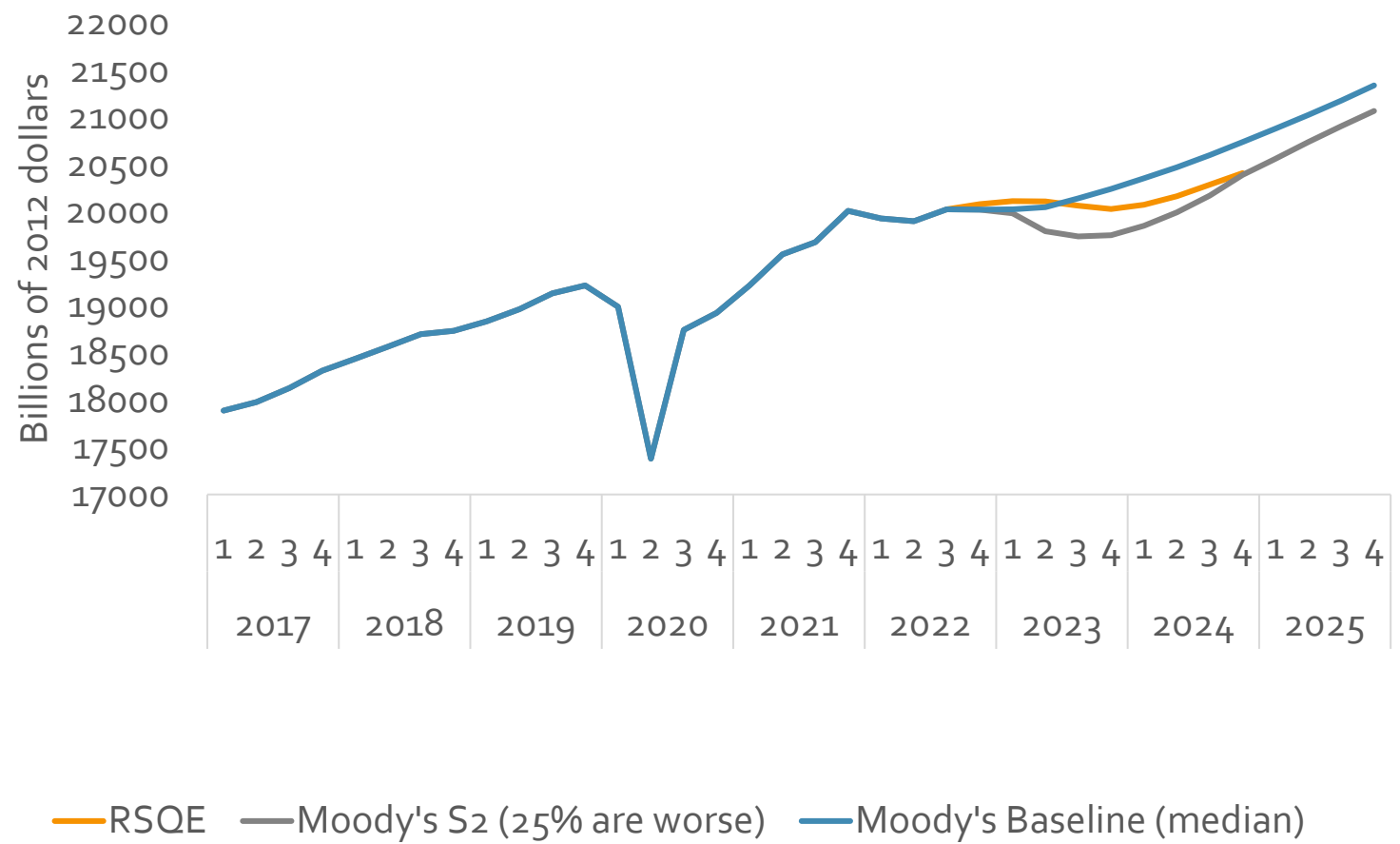
- The Fed will increase the funds rate another 75 basis points at the November meeting of the Federal Open Market Committee, 50 basis points at the December meeting, and 25 basis points at the meeting in late January. It is expected to peak at between 4.5% and 4.75% next year – nearly twice the level of the currently estimated “neutral” rate of 2.5%.
- Russia's war with Ukraine won't expand into other countries.
- 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%.
- There are no widespread lockdowns due to a new COVID variant.



Moody's believes a soft-landing – where the economy slows but does not decline – is still possible. This is its baseline forecast, which it gives a 50/50 chance of occurring. RSQE instead shows a mild recession beginning in the last half of 2023. Given the numerous ways in which something unexpected could happen, the RSQE forecast seems more likely.

Source: Moody's Analytics

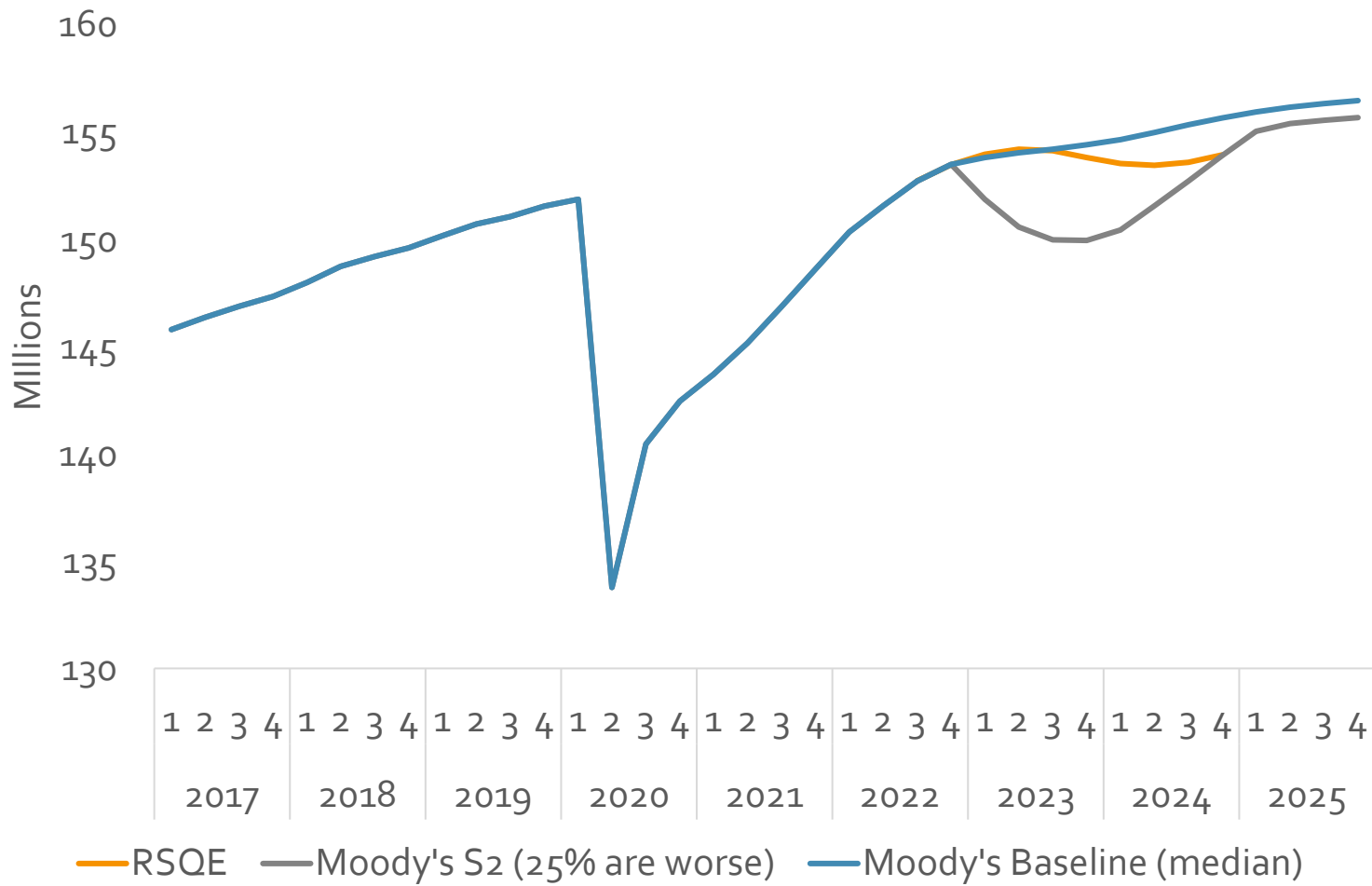
U.S. GDP: November 2022 Scenarios





Moody's show flat employment growth, while RSQE shows a dip in employment beginning in the second half of 2023, resulting in a net loss of 680,000 jobs, peak to trough. A recession more average than mild – as shown in Moody's S2 scenario – could lead to a loss of 3.5 million jobs .

U.S. Employment: November 2022 Scenarios

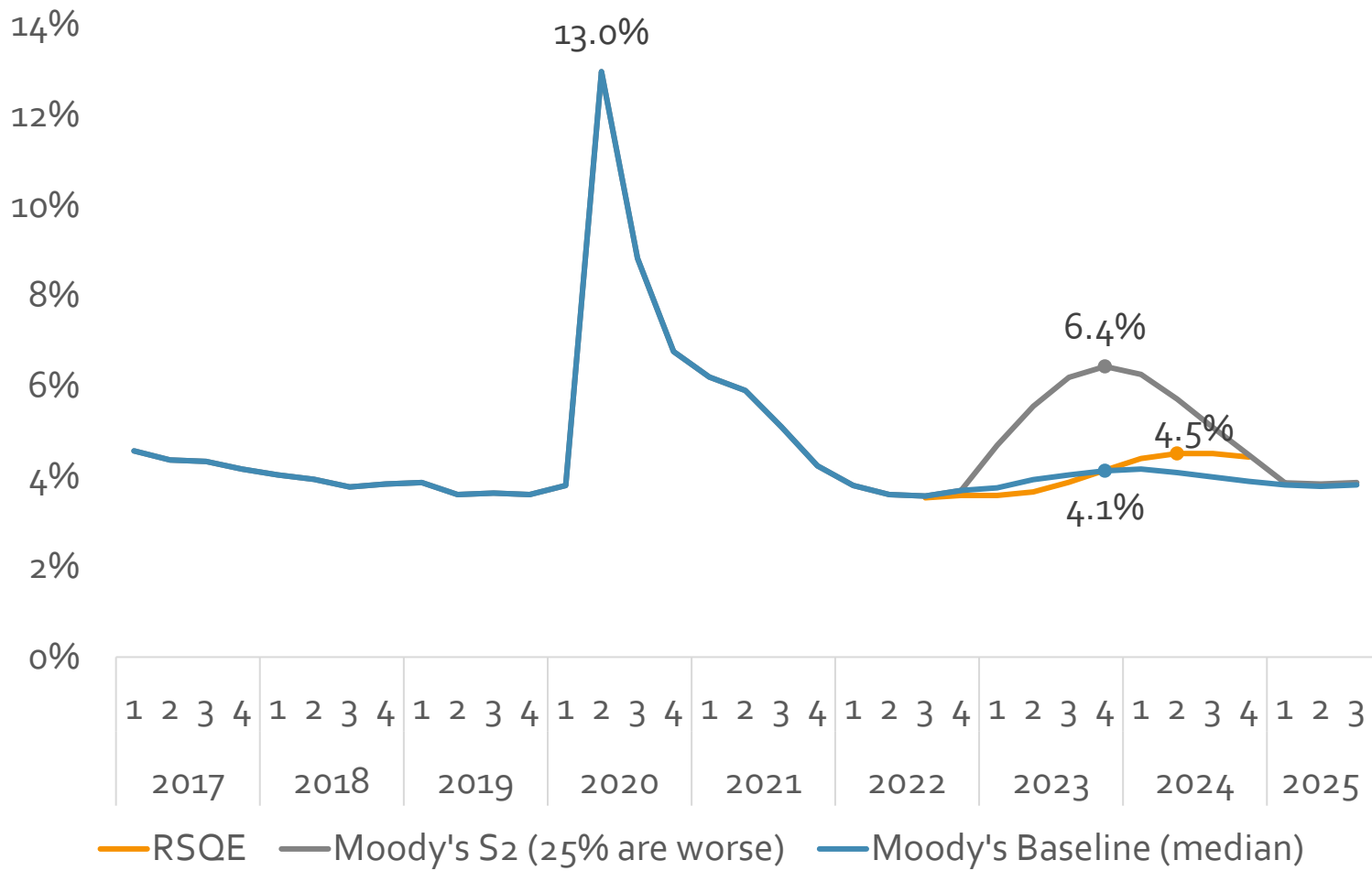


Source: Moody's Analytics

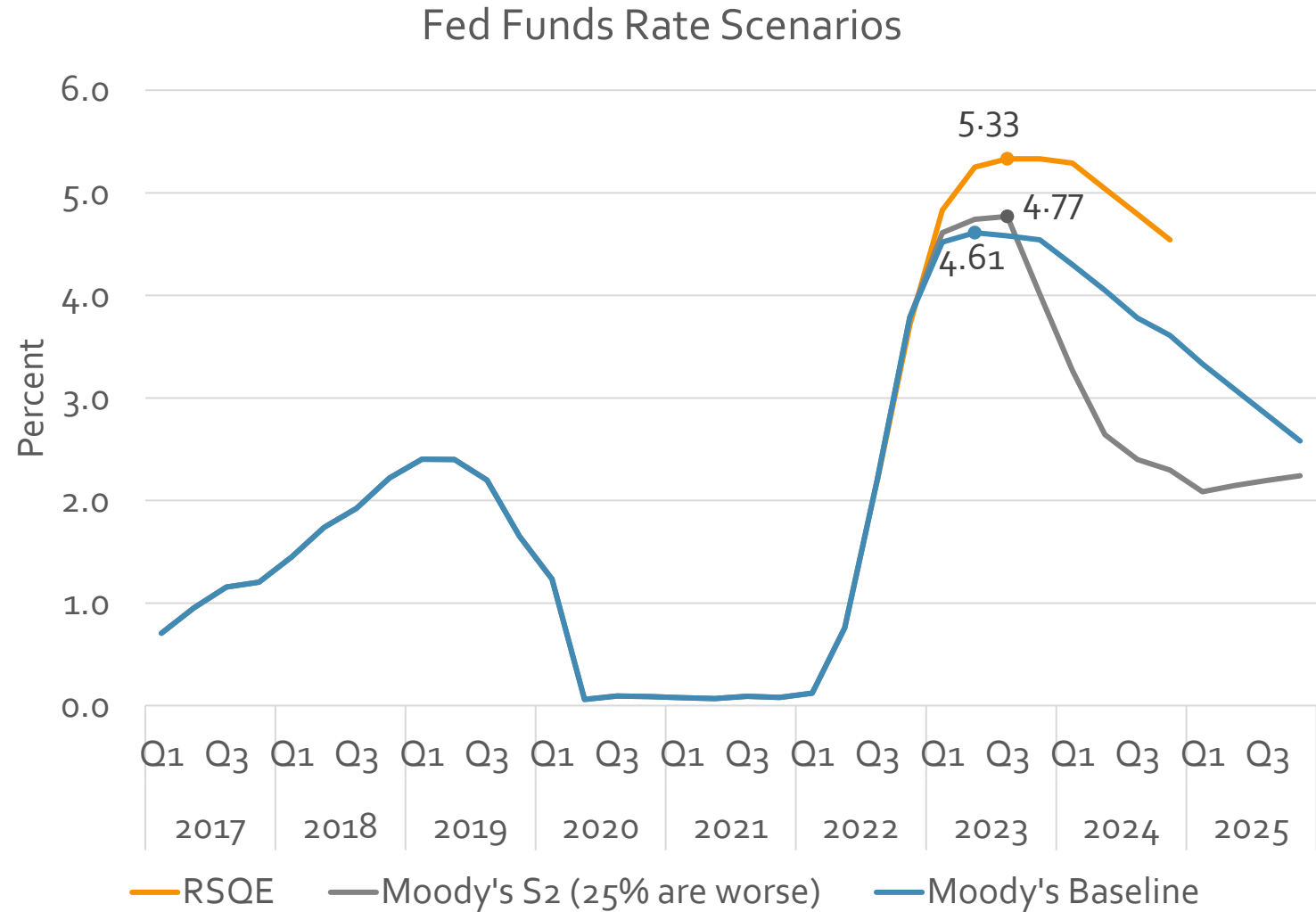


Moody's baseline forecast expects unemployment to rise 1/2 a percentage point to 4.2%. RSQE expects it to rise slightly more, to 4.5%. If the recession turns into one closer to average, this could push the unemployment rate to 6.4%.

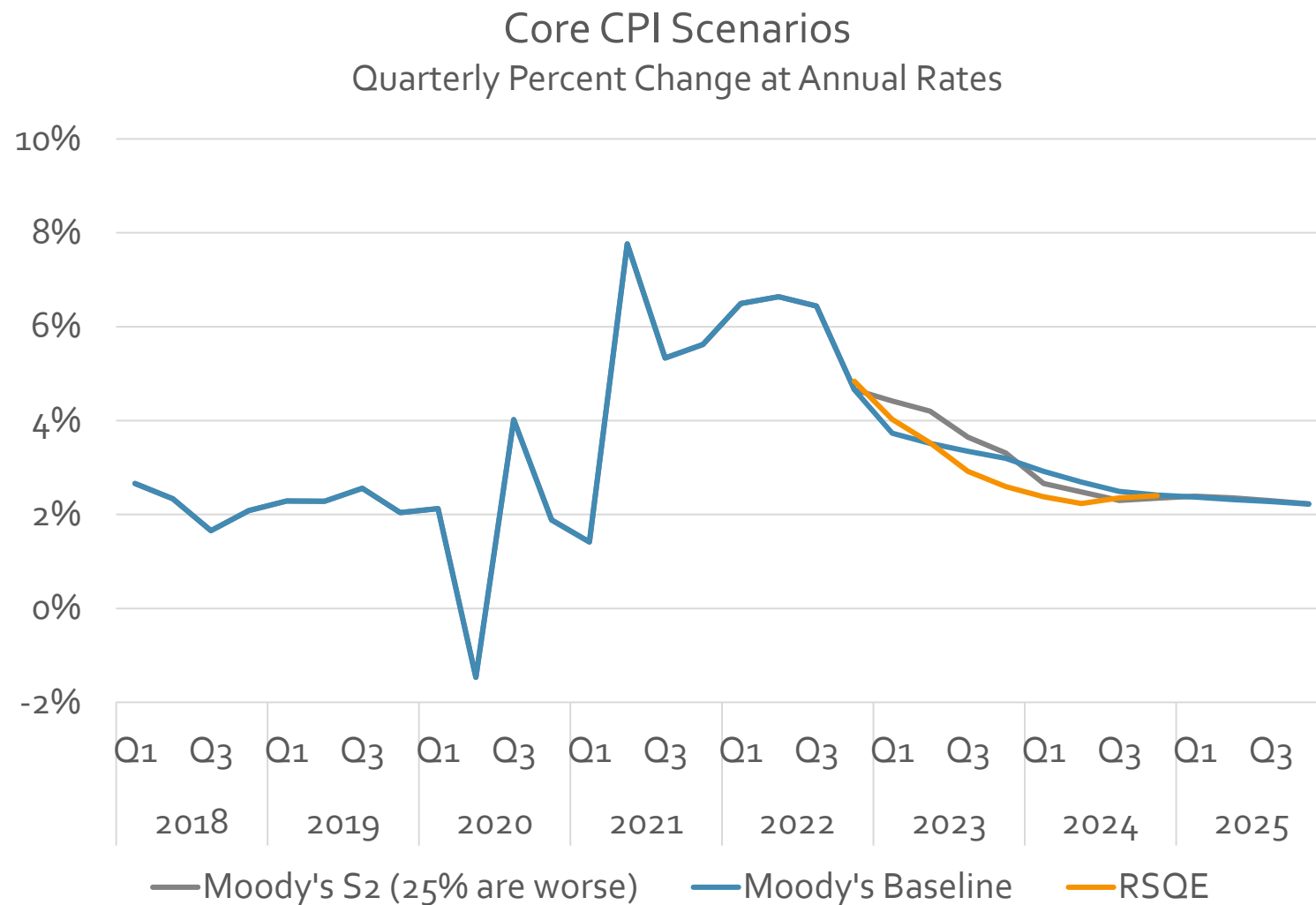
U.S. Unemployment Rate: November 2022 Scenarios



The Fed is likely to start reducing its pace of interest rate increases beginning in December. Moody's believes there will be a 1/2-point increase at that meeting, followed by a 1/4-point increase at the next, peaking at about 4.6%. RSQE thinks the Fed will need to be more aggressive, with the Fed Funds rate rising to between 5 1/4 and 5 1/2 by third quarter in the last half of 2023 and remaining there for a year.



All forecasts expect a sharp reduction in inflation. Because RSQE's forecast keeps the Fed Funds rate higher for longer, it achieves a slightly faster reduction in core inflation (abstracting from volatile food and energy prices) and achieves the Fed's target by first quarter 2024. Moody's anticipates it will take until 3rd quarter.

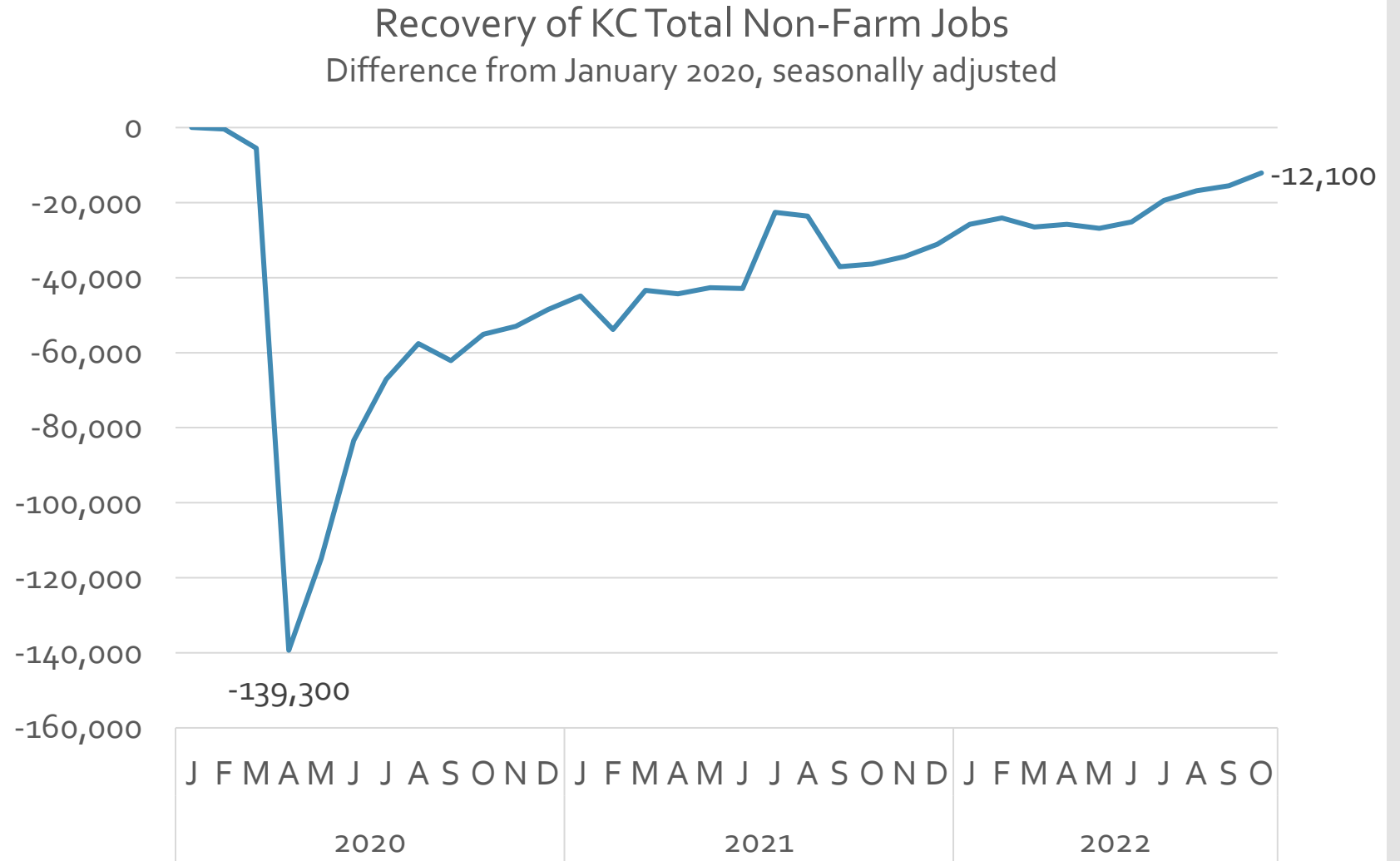


KC Economy – Current Situation



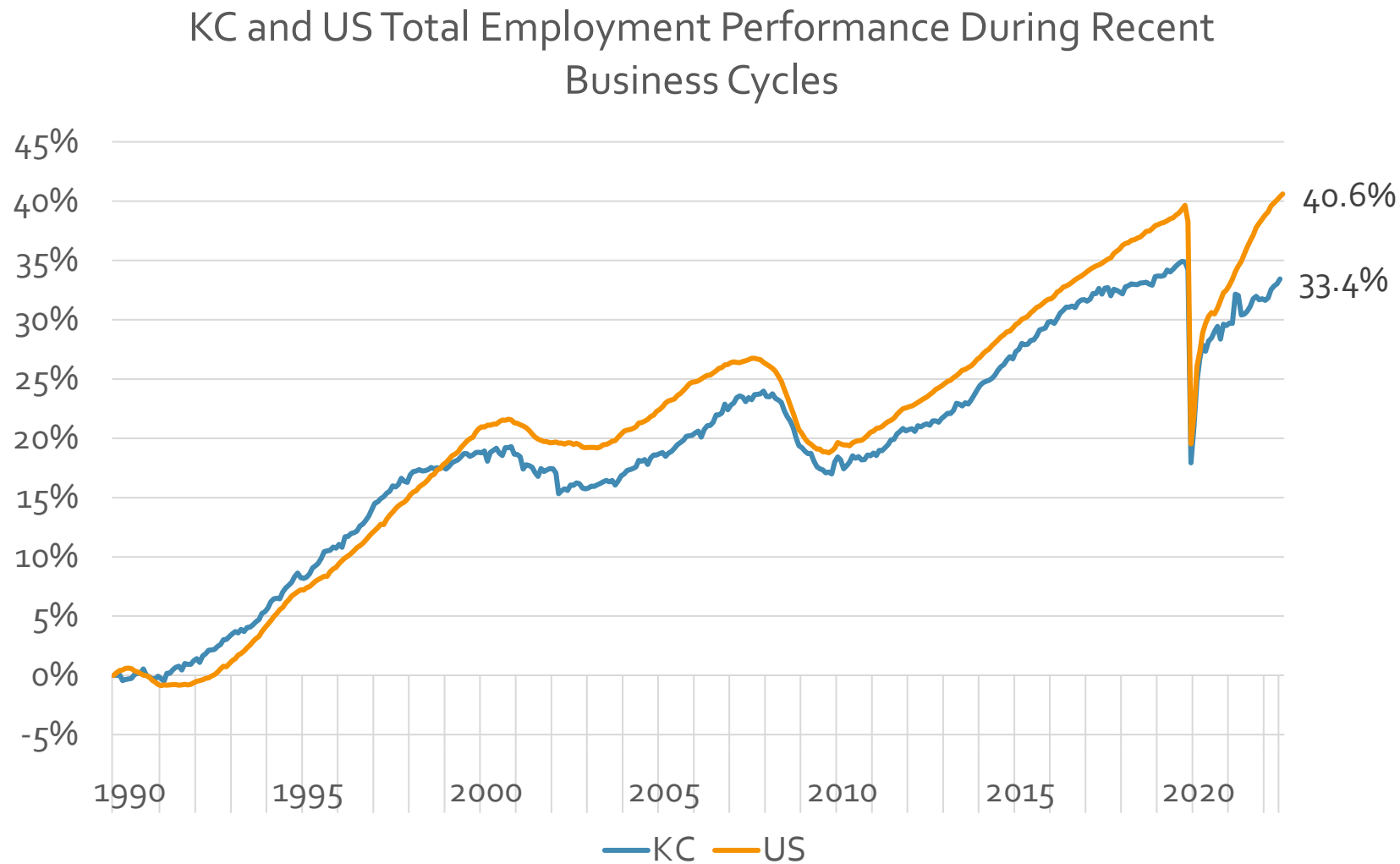
Photo by [Jake Fagan](#) on [Unsplash](#)

The trajectory of KC's employment recovery is much shallower than the nation's. We've only recovered 91% of our lost jobs while the U.S. has recovered all of them.

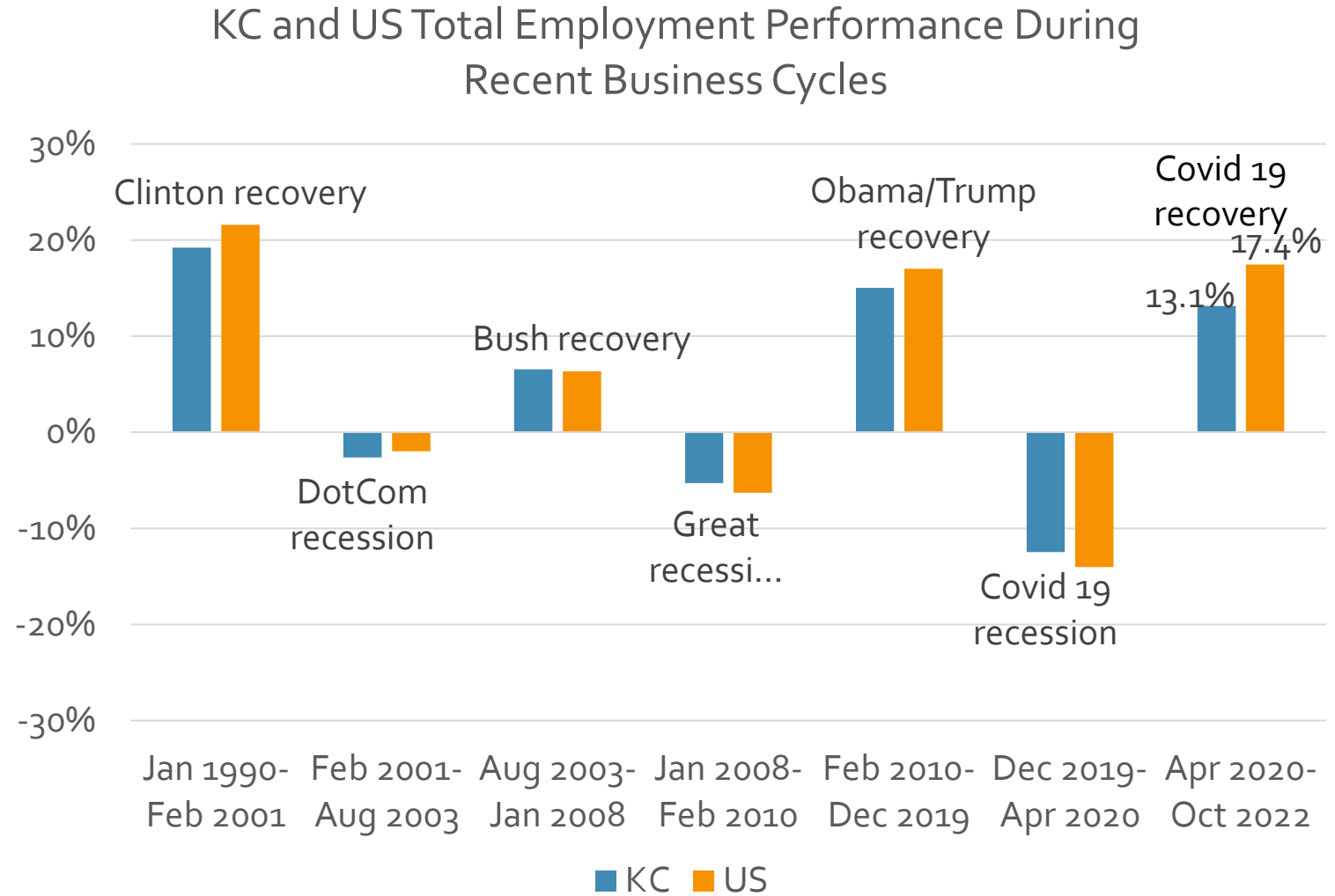


Source: Bureau of Labor Statistics

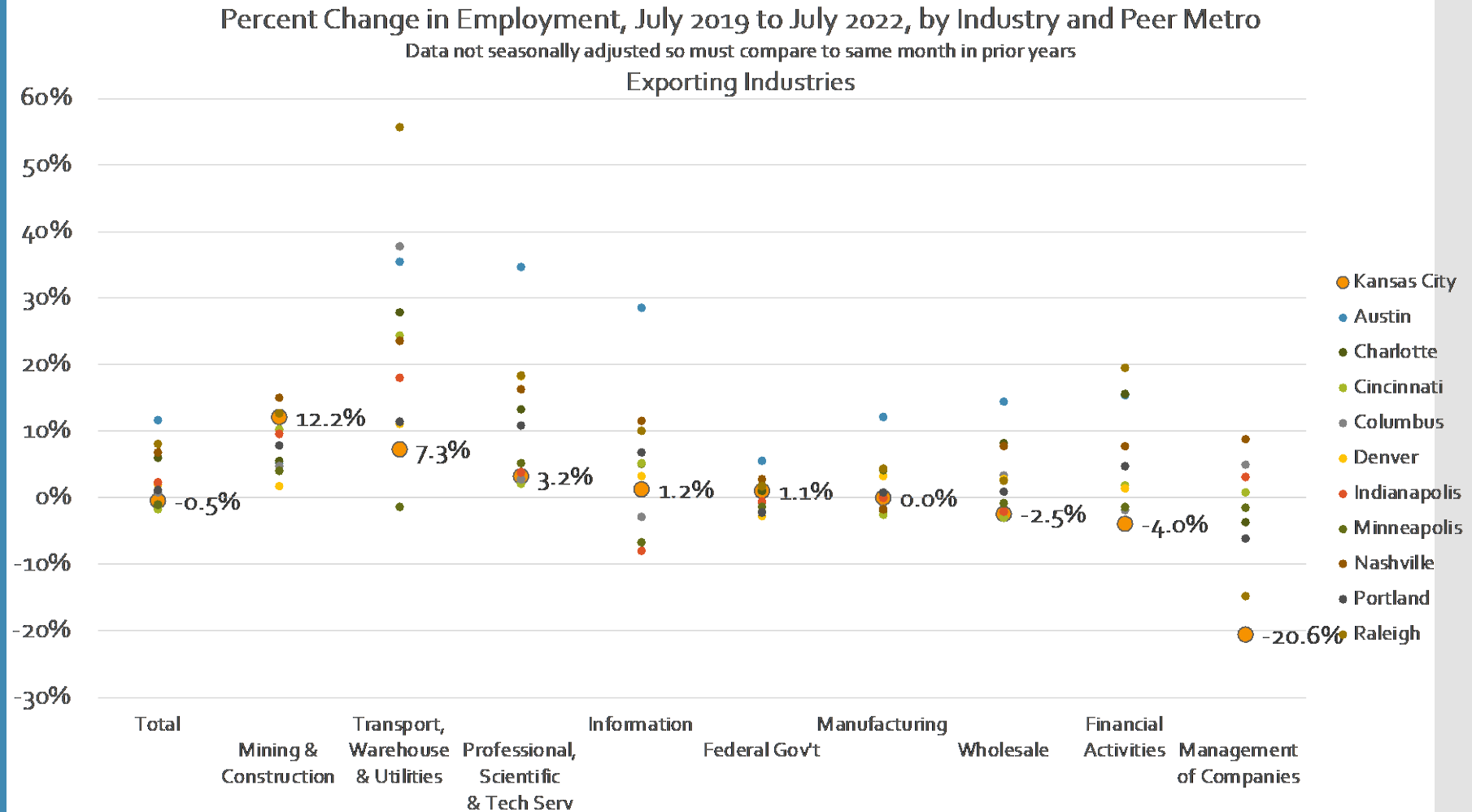
This truism is true, at least in recent business cycles – The KC economy doesn't bust as low but it doesn't boom as high. The problem is, recovery periods last much longer than recessions, so the KC economy is gradually losing ground relative to the nation.



Aggregating the data by business cycle shows this pattern even more clearly. During the recovery from the Covid-19 pandemic, KC's employment growth rate is currently running 4.3% behind the U.S.



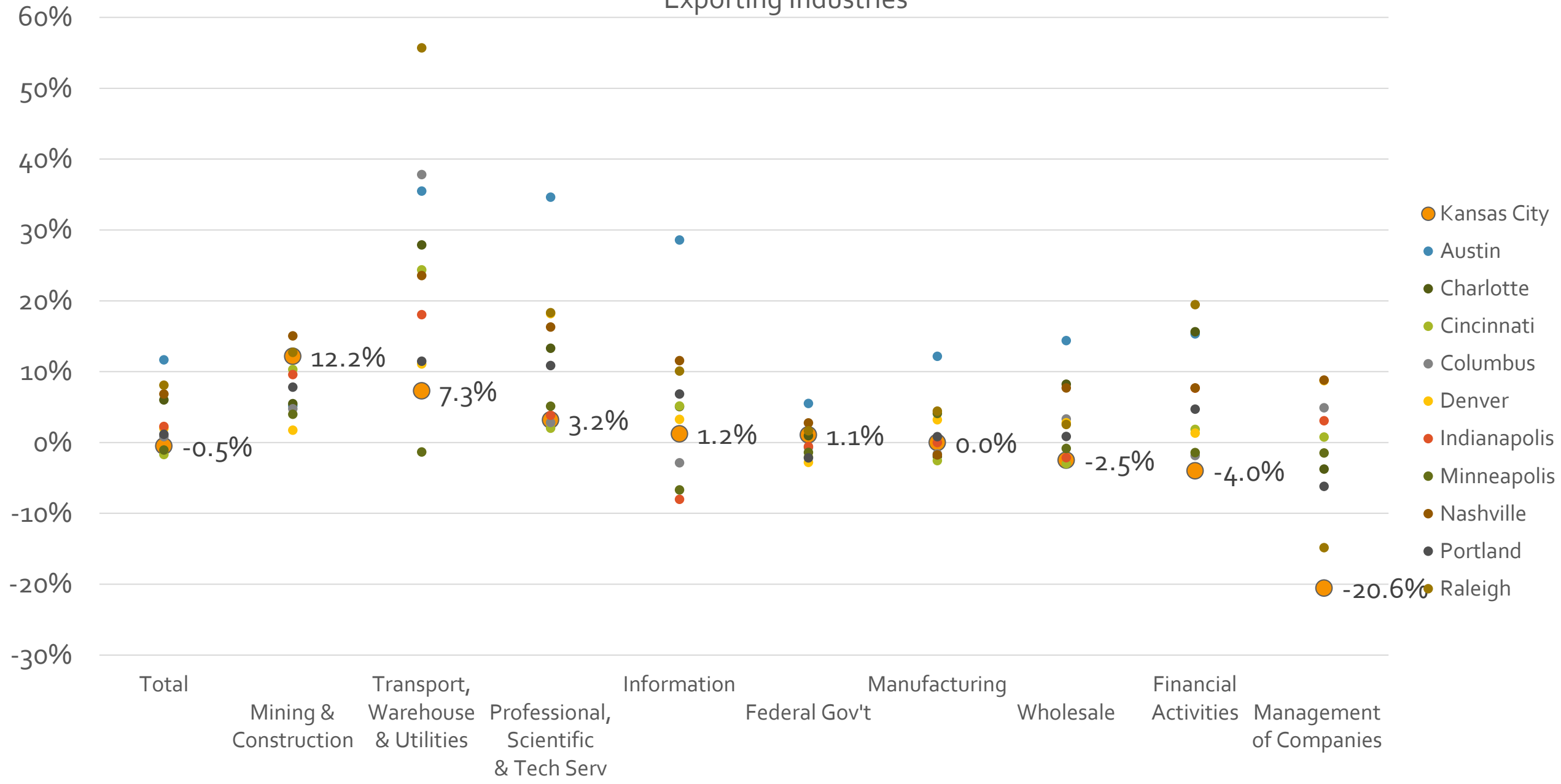
This relative sluggishness affects virtually all of our exporting industries. Only Construction is growing faster than most of metros the KC region benchmarks itself against. Industries that are high performers, like Warehousing and Professional Services, still rank low relative to benchmark metros.



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

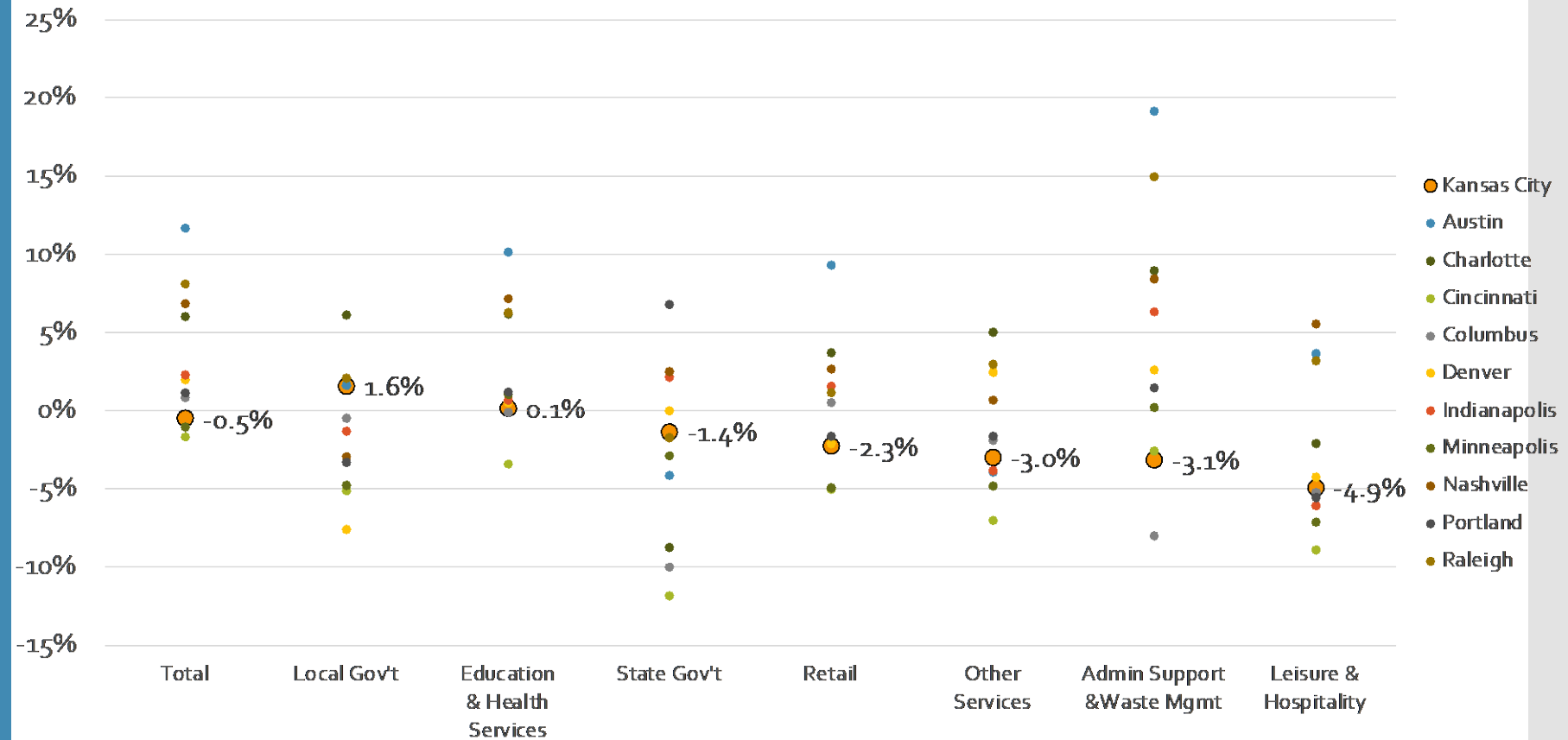


While many of our exporting sectors have recovered their lost jobs, most of our local serving sectors have not. Some – like Retail Trade and Leisure and Hospitality – are among our largest employers. These sectors are struggling nationwide, though, so KC's rank relative to benchmark metros is not as often near the bottom for these sectors.

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

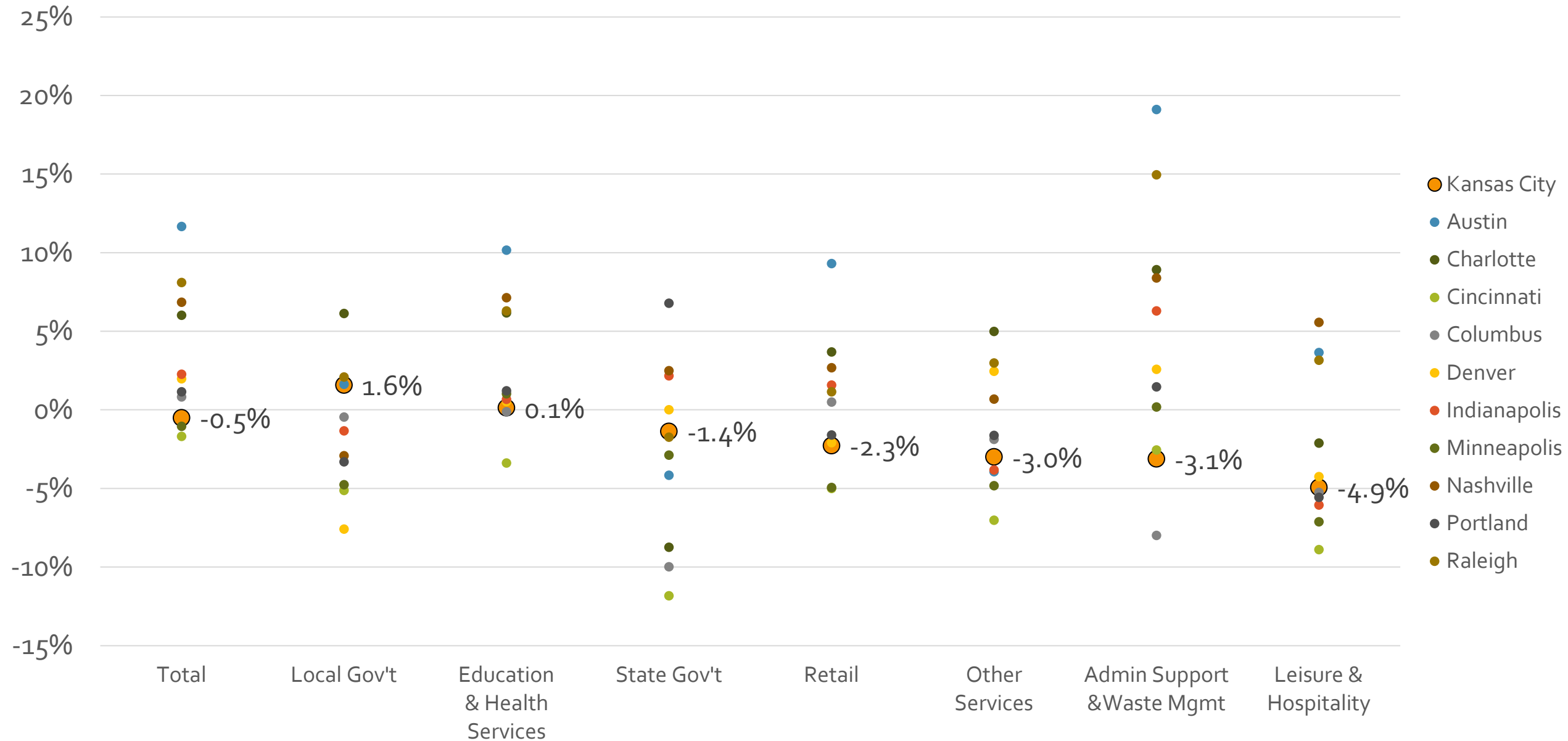
Local-Serving Industries



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

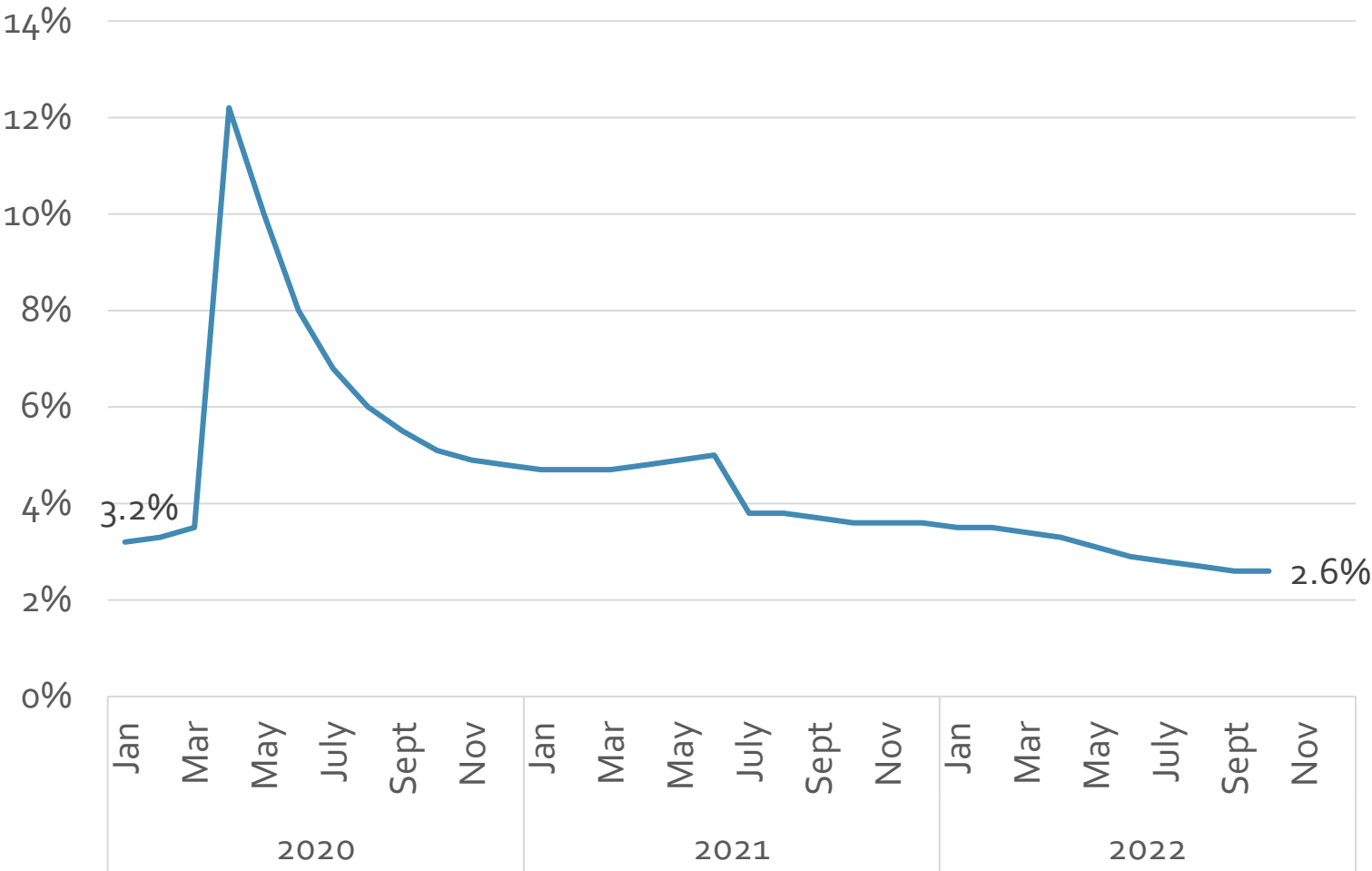
Local-Serving Industries





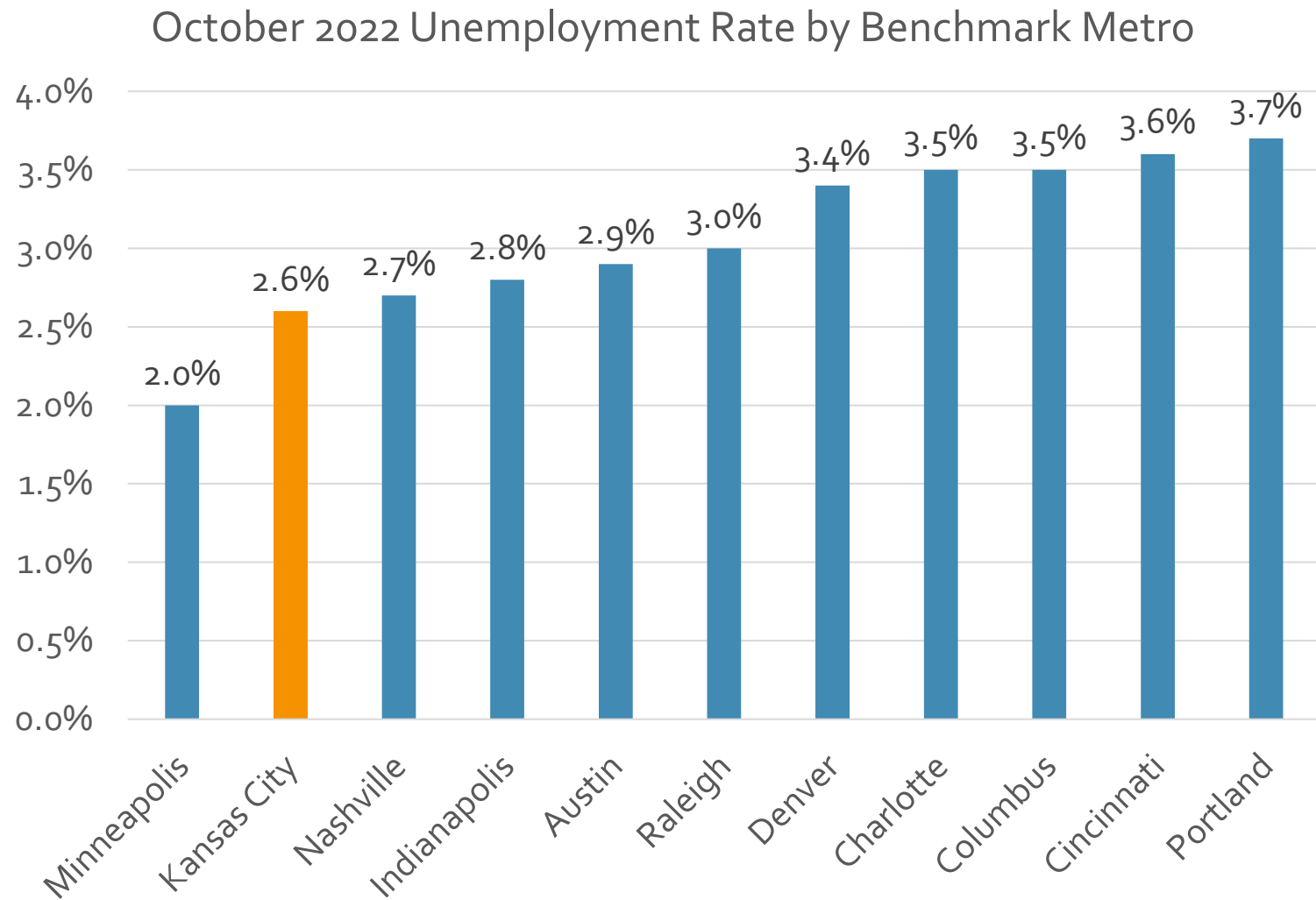
Yet, despite slow employment growth, our unemployment rate is 0.6% below its pre-pandemic low. This suggest labor supply issues may be biting here more than elsewhere.

Kansas City Unemployment Rate

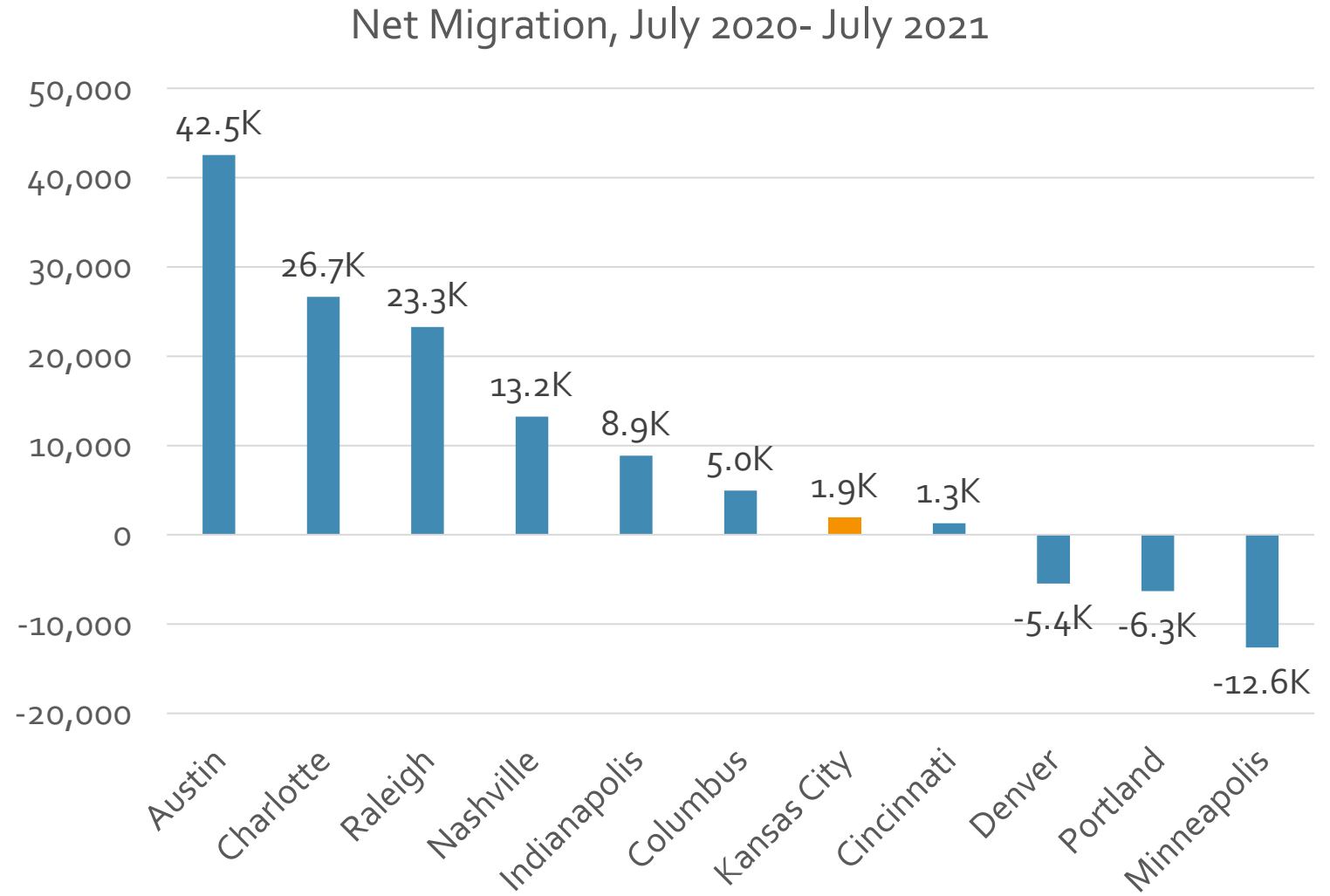


Source: BLS LAUS series

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.



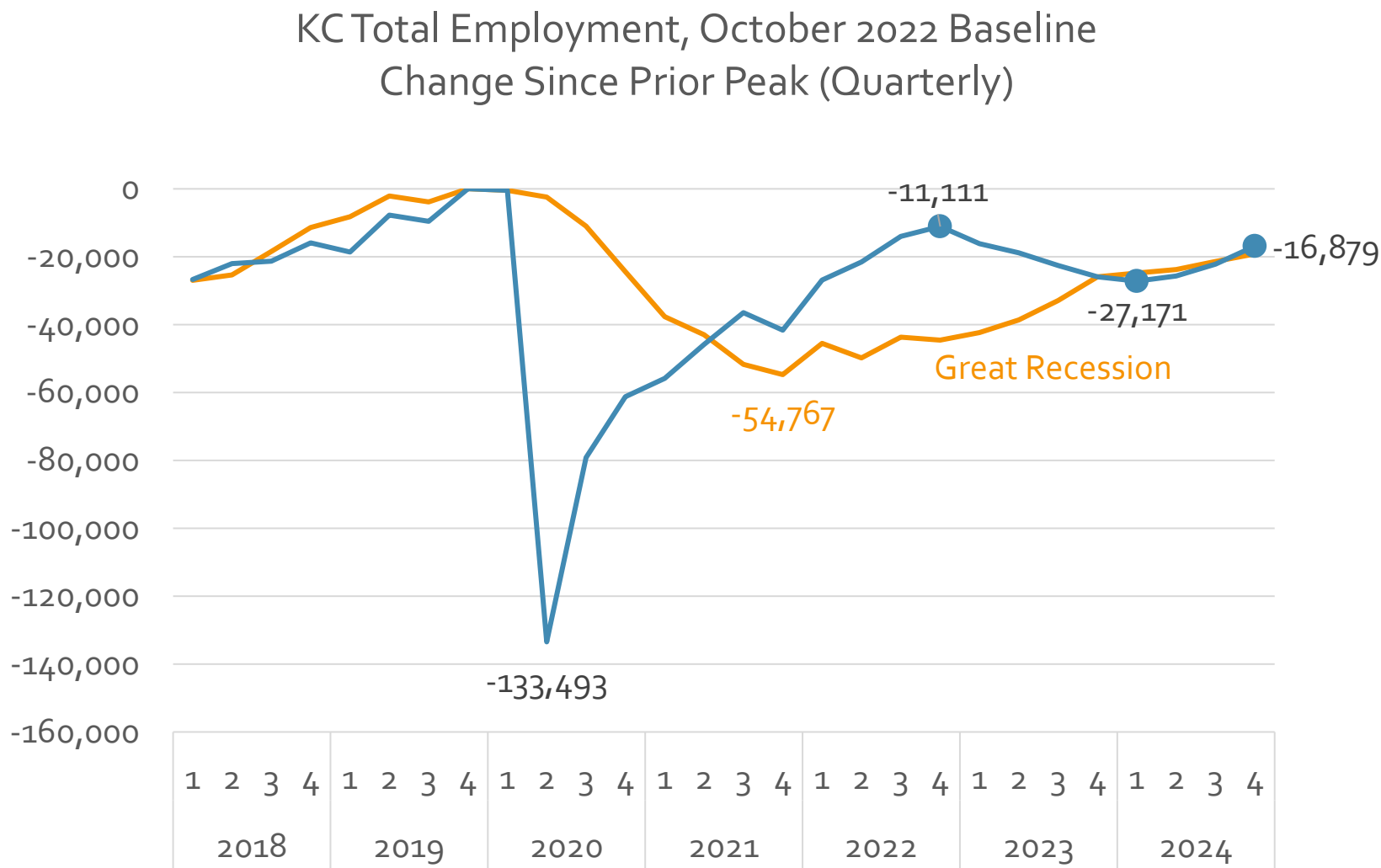
KC Economy – Forecast



Photo by [Jake Fagan](#) on [Unsplash](#)

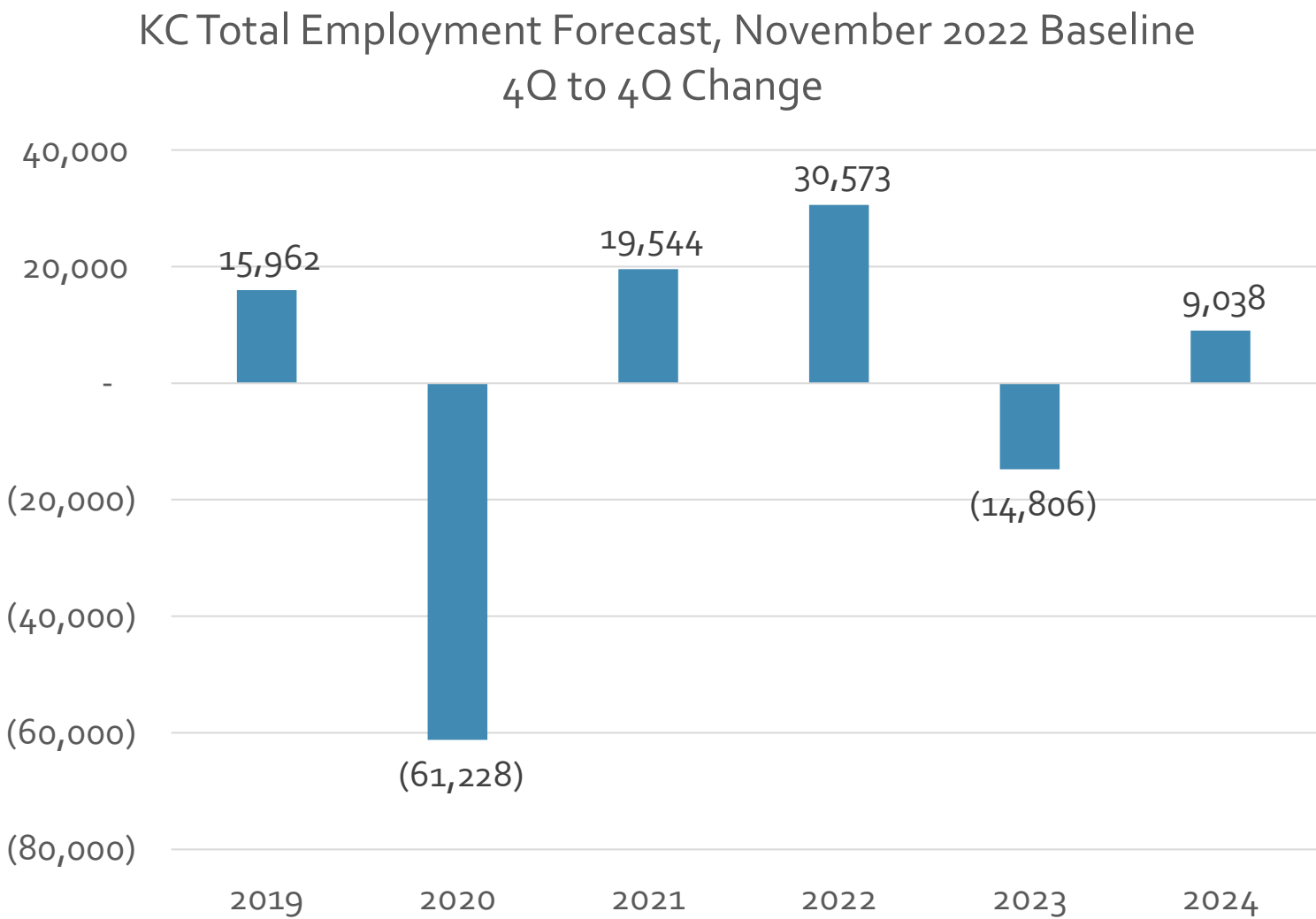


Based on the RSQE forecast, KC won't quite fully recover the jobs lost during the pandemic before they begin to fall again under the weight of a second recession. This one will be much milder, with a net loss of about 16,000 jobs peak to trough over the course of about 1 year beginning in 1Q 2023.





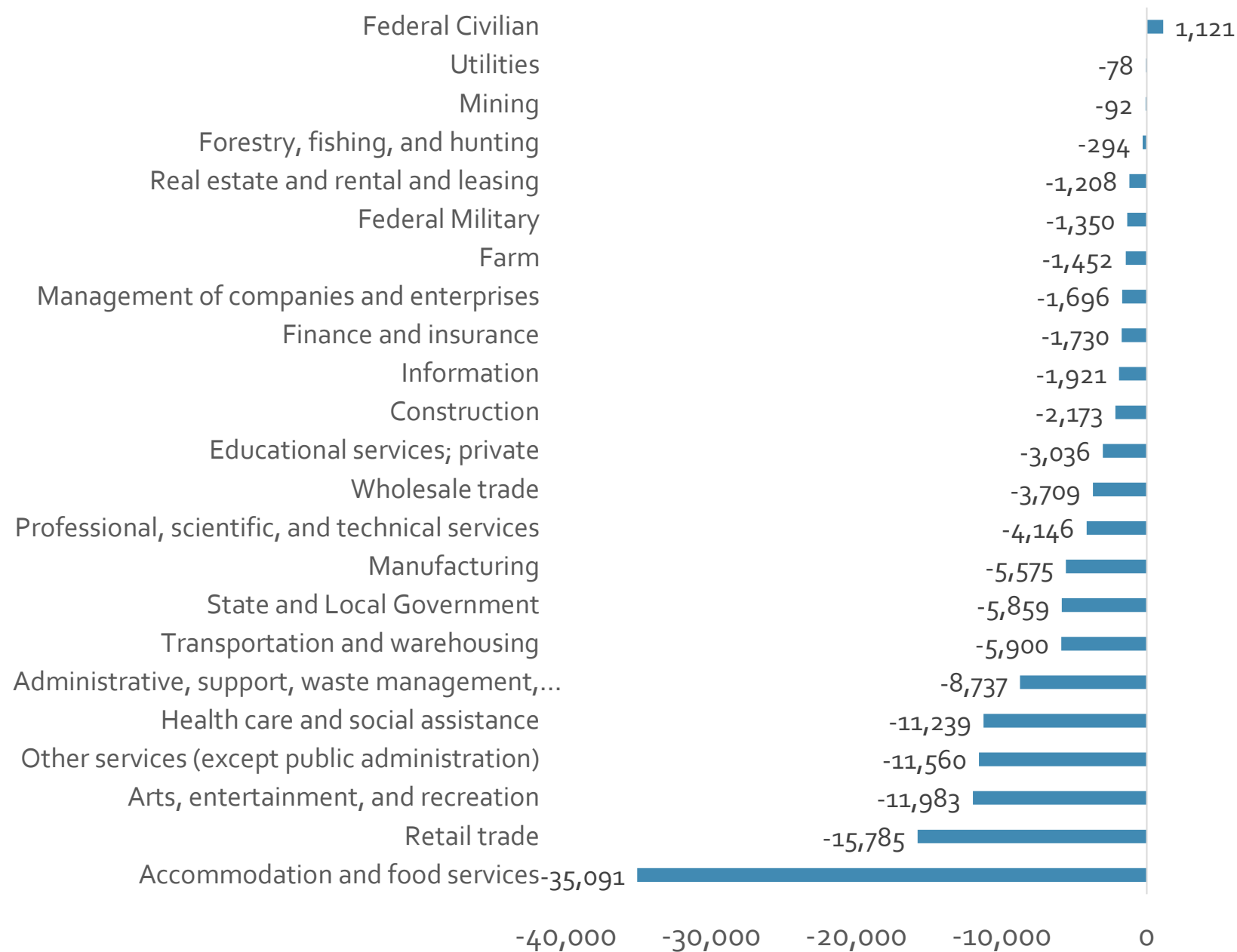
KC's employment growth began to accelerate just before the recession is expected to hit and cause a loss of about 15,000 jobs measured on 4Q-to-4Q basis. The economy begins to rebound after that, though national labor constraints may limit its strength. As a result, KC may not recover all its lost jobs until 2026.



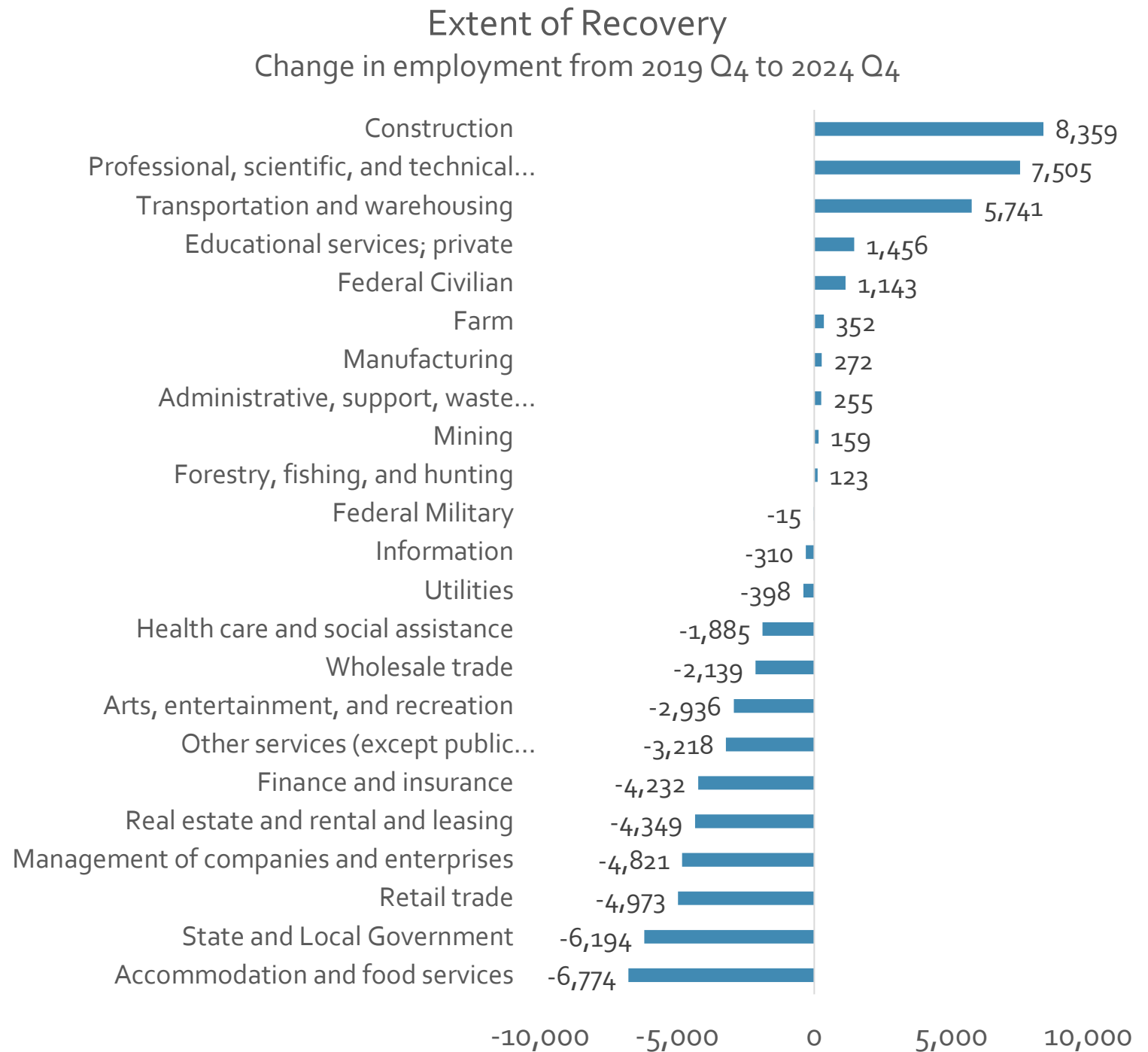
By now, the story here is well known. The lock downs implemented to avoid the worst impacts of Covid-19 hit hard, especially in Accommodation and Food, Retail Trade and Arts and Entertainment. Some sectors the region specializes in proved more resilient during the Covid-19 downturn, such as Finance, Management of Companies, and Professional/Technical Services.

Depth of Downturn by Industry

Change in employment from 2019 Q4 to 2020 Q2

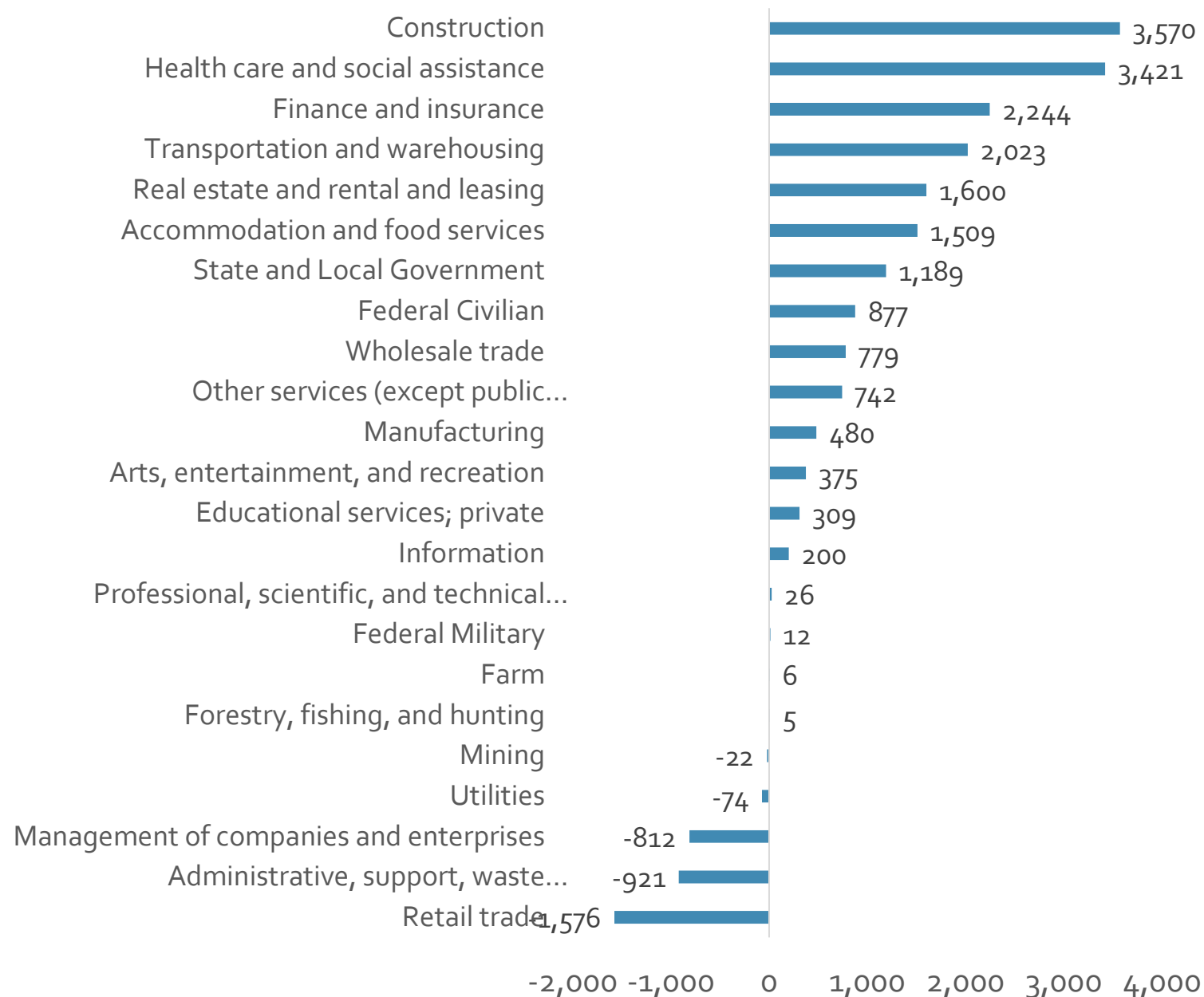


A second recession keeps many industries from fully recovering to pre-pandemic levels. Accommodation and Food, Local Government and Retail Trade are expected to be especially affected. But Construction, Professional Services and Transportation and Warehousing fare relatively well.



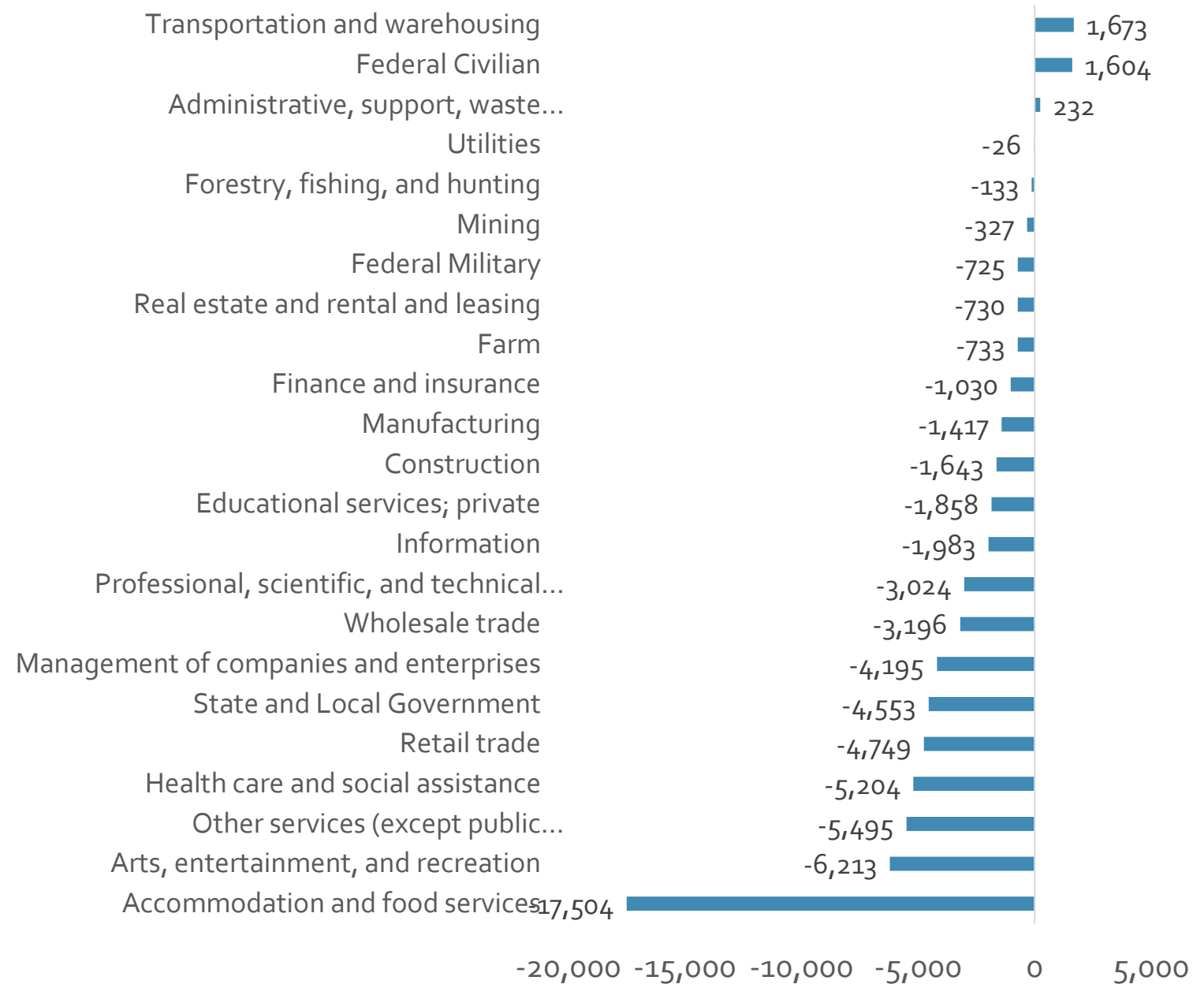
Taking this year by year, the 2018-19 period was the last one we might consider “normal”. Growth in construction and Health Care led the way, while Retail continued to deal with the shift to on-line sales.

KC Employment Change, 2018-19 Fourth-quarter to fourth-quarter



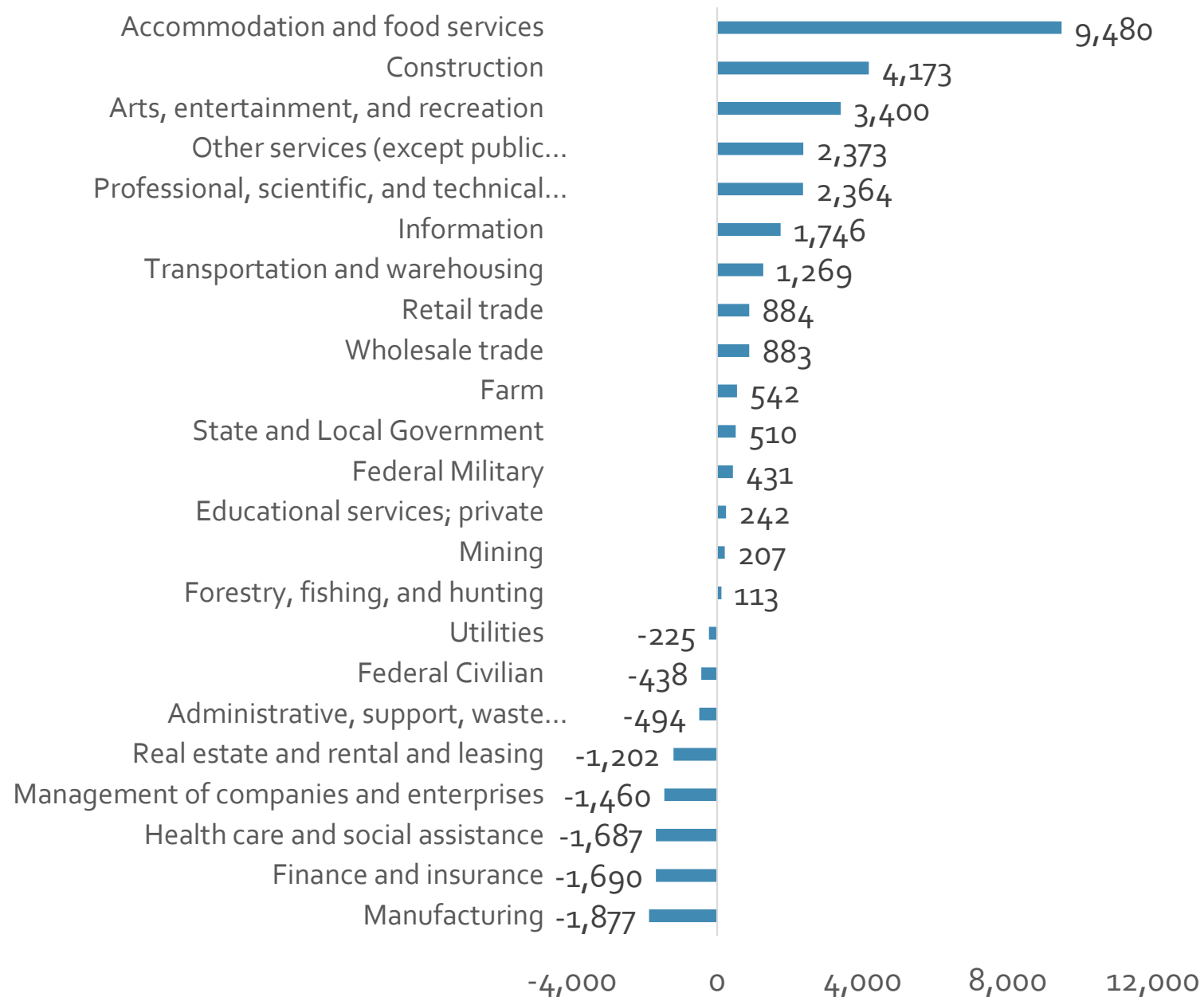
The world turned upside down in 2020 as a result of the Covid-19 pandemic and severe economic dislocations caused by sending all but essential workers home.

KC Employment Change, 2019-20 Fourth-quarter to fourth-quarter



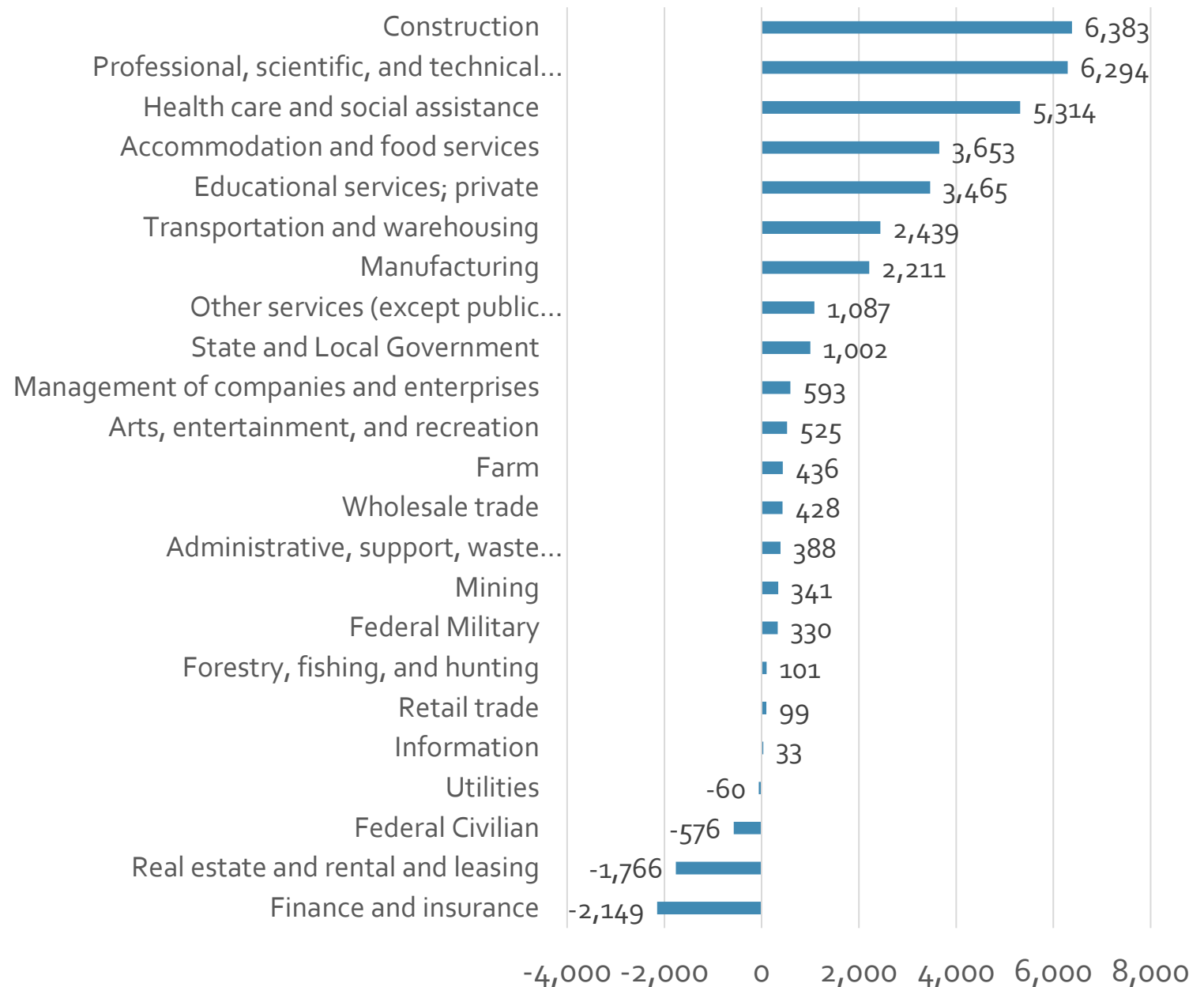
Despite the disruption, the economy began to grow rapidly as a result of several rounds of fiscal stimulus. Some of the sectors hit the hardest – like Accommodation and Food and Arts and Entertainment – also rebounded most strongly over the subsequent year.

KC Employment Change, 2020-21 Fourth-quarter to fourth-quarter



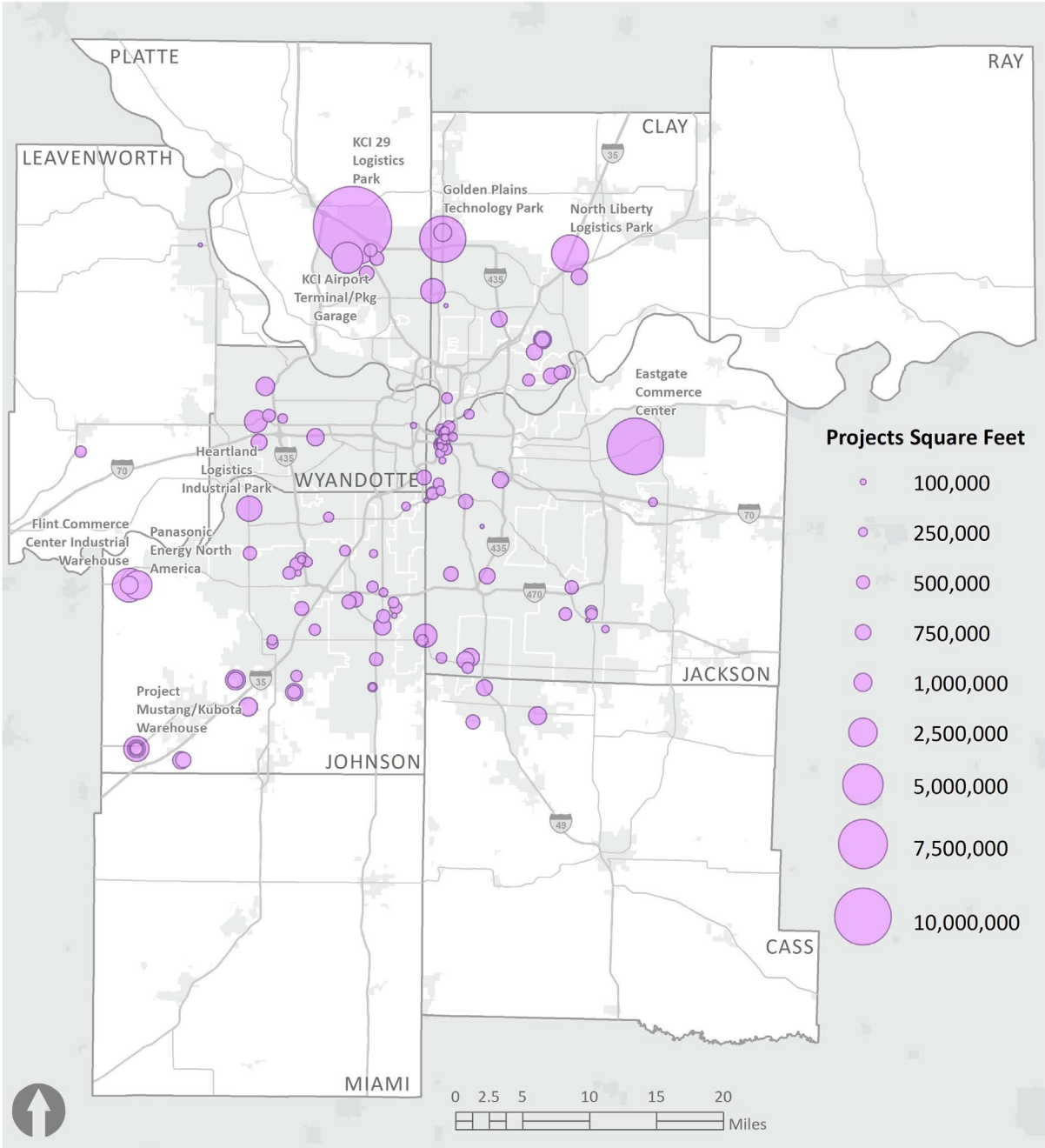
Growth became more widespread in 2022, with Construction, Professional and Technical services, Health Care, and Accommodation and Food leading the way. Finance and Insurance continued to decline. Despite a hot housing market in terms of prices, units sold began to drop this year as interest rates rose.

KC Employment Change, 2021-22 Fourth-quarter to fourth-quarter



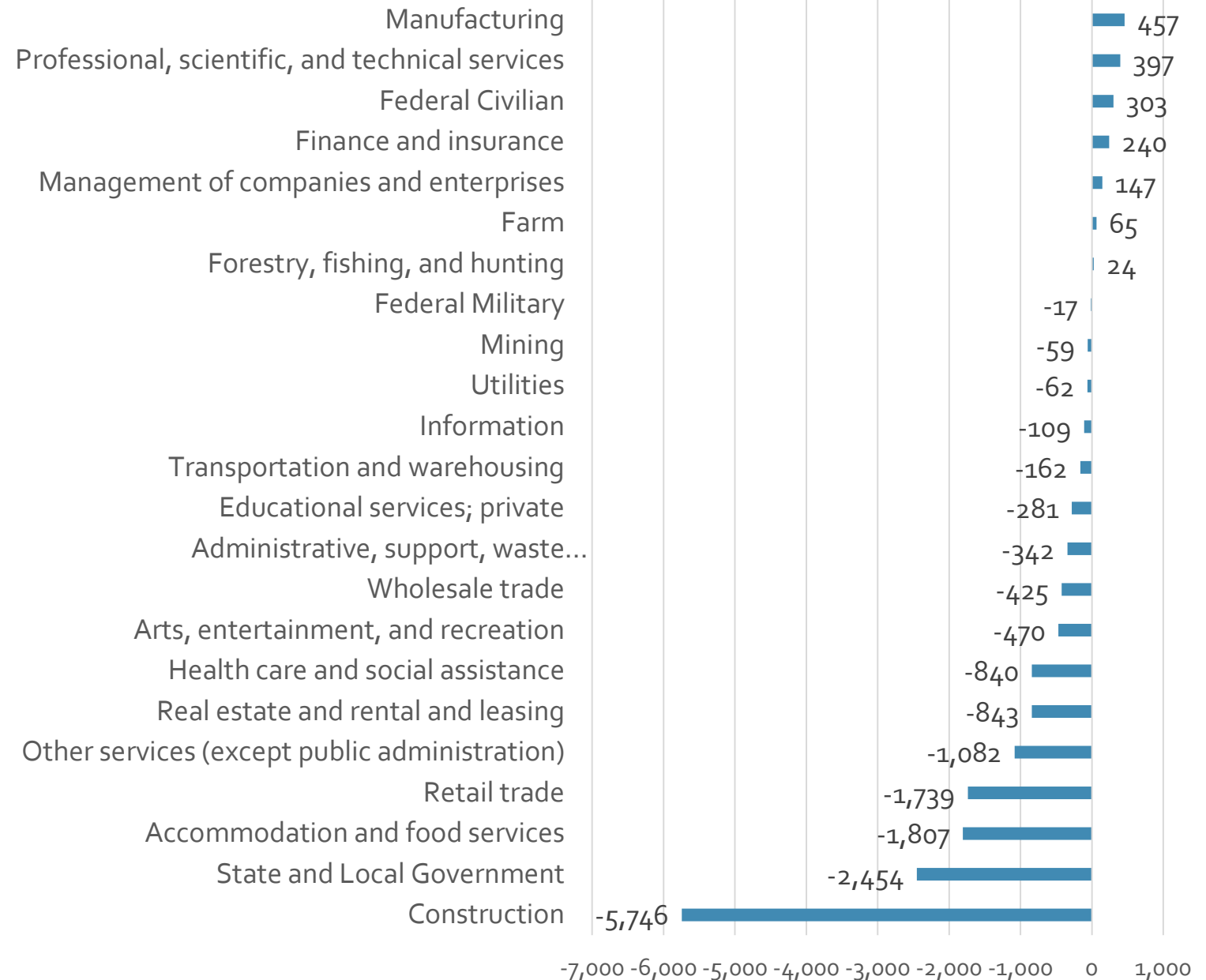
Much of the construction has been concentrated in the industrial and distribution sectors, with most locating near highways along and outside of the I-435 / I-470 Interstate loop.

Largest current and planned construction projects in KC

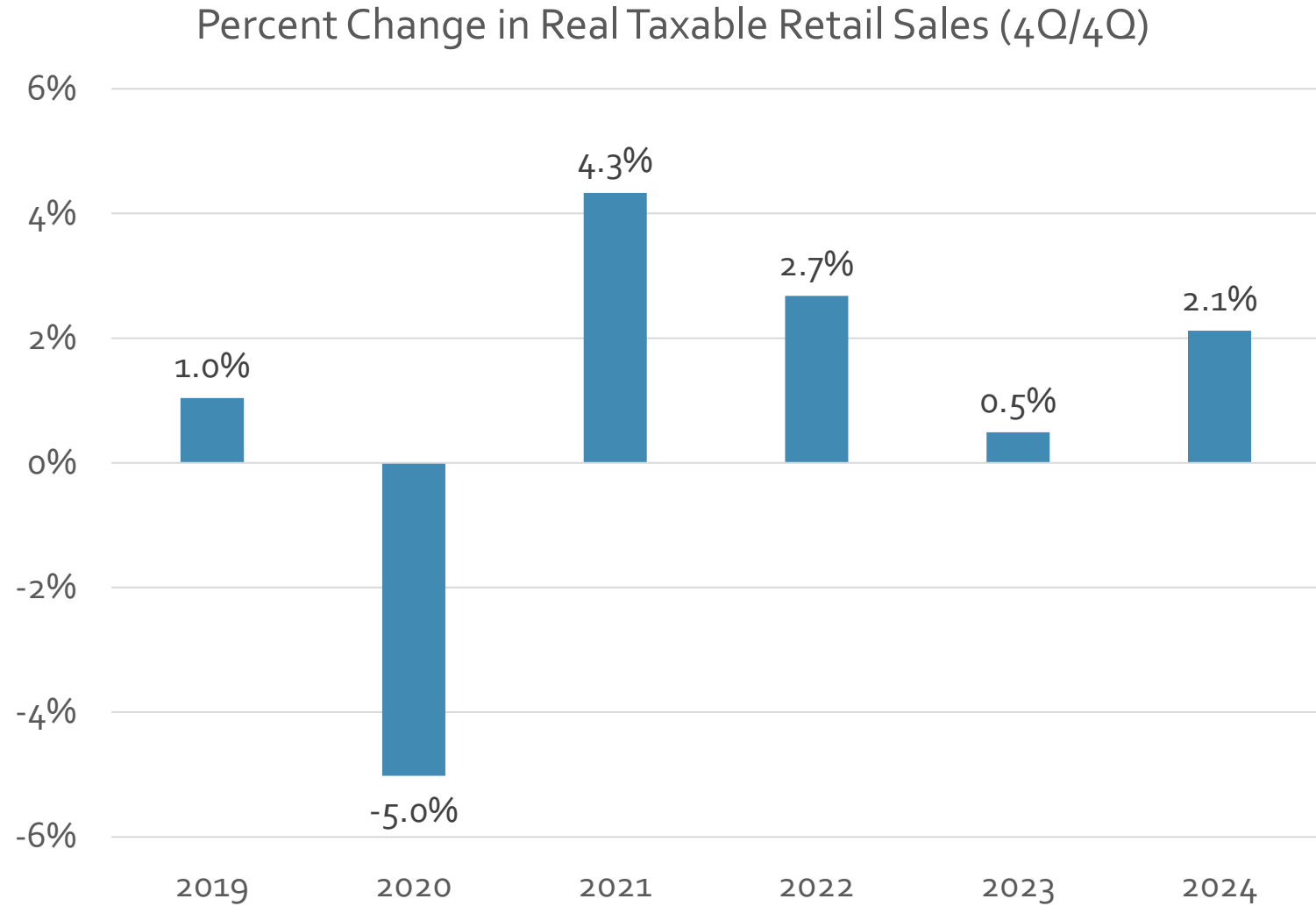


In 2023, the recession hits and takes most sectors with it. Construction employment falls the most in response to high interest rates. As spending growth is reduced, employment in Accommodation and Food and Retail decline significantly and stagnant revenues also hurt local government jobs.

KC Employment Change, 2022-2023 Fourth-quarter to fourth-quarter

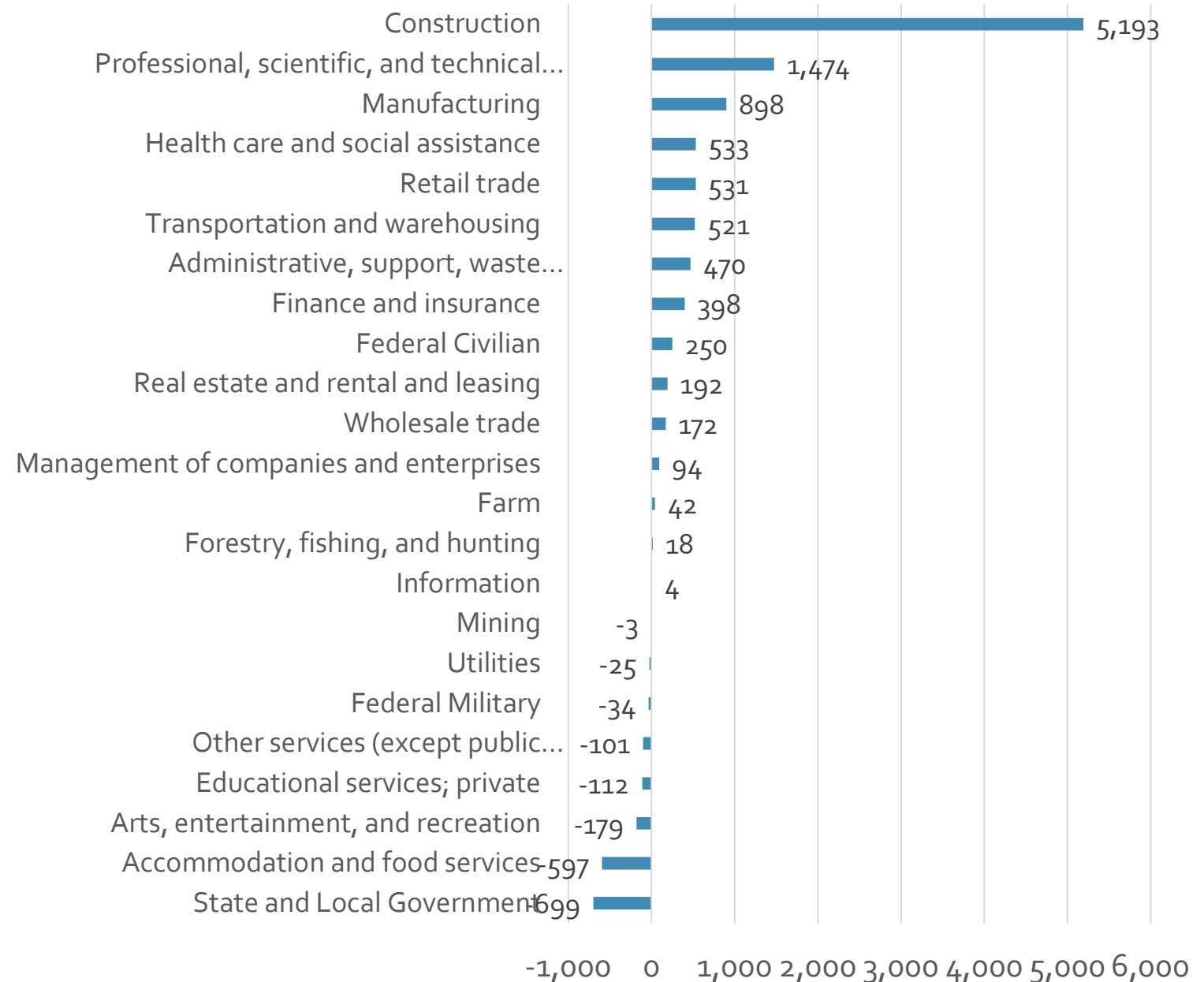


Why the decline in local government? Taxable retail sales follows a similar pattern to total employment, though the sales hold up a bit better than employment, avoiding an outright decline. Still, stagnant revenues in 2023 are likely to restrict local government ability to hire new workers or replace existing ones.



In 2024, the rebound begins. But a mild recession means a mild recovery. Construction is expected to rebound strongly, as is Professional Services. Manufacturing shows strength in response to an improving global economy. But Local Government and Accommodation and Food continue to show lingering after-effects.

KC Employment Change, 2023-2024
Fourth-quarter to fourth-quarter





Summary and Conclusion

- The rapid rise in interest rates has already had an impact on the housing market, raising costs to the point where many consumers can no longer afford to purchase home.
- High interest rates have also added significant cost and instability into investment markets that were already dealing with the confluence of other sources of uncertainty. These include the potential for a “tripledemic,” possible new supply-chain disruptions as China abandons its zero-Covid policy, rising geopolitical tensions created by the war in Ukraine, and increasing economic competition with China.
- With stimulus gone and excess savings dwindling, the consumer is unlikely to be able to plug the gaps in demand these factors are causing.

Summary and Conclusion

- As a result, we are forecasting a mild recession beginning in mid-2023. As it takes hold, inflation should come down. But a full recovery of jobs lost in KC during the pandemic may be postponed until 2026.
- Construction is hardest hit immediately but also is projected to rebound quickly. Manufacturing and Professional/Technical services show significant resiliency during this recession and help to lead the recovery.
- Despite the recession, worker and skill shortages in many occupations are likely to remain as the rate of retirements approaches the rate of new entrants and the rate of immigration remains historically low.
- The region's future economic growth is likely to depend on its ability to upskill its workforce so that it can be more resilient in the face of future disruptions, which appear to be occurring more frequently than in the past.

Summary and Conclusion

Despite experiencing slower growth than national and benchmark markets in the past, today KC is engaged in transformation:

- Attracting new visitors
 - The New KCI
 - 2023 NFL Draft
 - 2026 World Cup
- Growing new industries
 - Panasonic battery plant
 - Life Science Investment
- Creating a new, higher quality of life
 - Streetcar extension
 - Downtown baseball stadium

These investments have the potential to change the region's trajectory and accelerate its progress.

Questions?

Greater Kansas City Chamber of Commerce Economic Forecast Breakfast

December 8, 2022

U.S. and KC Economic Forecast

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