

Domestic Growth Momentum Weakening and Risk of Foreign Shocks Is Elevated; Recession Is Essentially a Coin Toss Over the Next Year and a Half

The outlook worsened further over the last month. The University of Michigan’s Consumer Sentiment Indicator and expectations of small business owners in the National Federation of Independent Business’s monthly survey have both fallen to record lows—and a survey of community bank CEOs conducted by the American Bankers Association shows more than nine in 10 expect a recession over the next 1-2 years. CPI inflation jumped more than expected to a new 40-year high in June as national gas prices soared above \$5 per gallon, and the yield curve—the differential between the yields on two-year Treasury notes and ten-year notes—turned negative, a sign that financial markets, like consumers, small business owners, and community bankers, see rising risk of a recession ahead.

All is not lost. Wealthier consumers are still catching up on spending on travel, dining out, and entertainment that they skipped in 2020 and 2021, which is fueling continued growth of the service sector, which employs four in five private workers. While pockets of the economy are starting to see job losses, including big box retail, tech, mortgage finance, and parts of manufacturing, labor demand remains extremely high, and laid-off workers are finding new jobs much faster than in a conventional downturn. Strong labor demand is also helping lower- and middle-income households supplement incomes by taking on additional shifts or jobs. After a surge to record highs in June, gasoline prices are coming back down, and futures prices of other energy, metals, and food commodities fell over the second quarter as well. That should help slow inflation in the second half of 2022.

Even so, downside risk to the economy continues to rise. With growth momentum weakening, one more negative shock would be enough to push the U.S. into a recession. And risks of such a shock from abroad are high. The Russia-Ukraine war could cause a European energy crisis in the winter heating season; China’s lockdowns and housing market correction could weaken foreign economies even more. Comerica’s July outlook assumes these foreign shocks do not become big enough to tip the U.S. into a recession, but that risk—rather than the muddle-through described by our forecast—is roughly a coin toss.

Following June’s worse-than-expected CPI inflation of 9.1% (!) and better-than-expected payroll job growth of 372,000 (!!), the Fed will make another big interest rate hike at its July 27 interest rate decision. At their last decision, Chair Powell said the July meeting would probably be a choice between a half percentage point hike and a three quarters of a percent hike. But data out since Chair Powell spoke make the July decision more likely to be between a three quarters of a percent hike, which is Comerica’s forecast, or a hike of a full percentage point. Comerica forecasts another percentage point of federal funds rate hikes by year-end 2022, and unchanged rates in 2023. Financial markets are pricing in the possibility of interest rate cuts next year, another sign of recession fears.

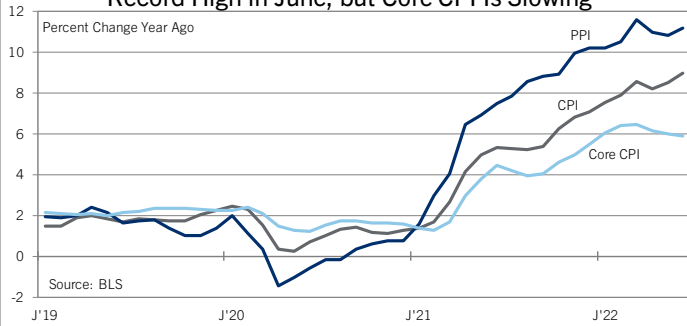
U.S. Economic Outlook, Summary

| <i>a = actual f = forecast</i> | 1Q'22a | 2Q'22p | 3Q'22f | 4Q'22f | 1Q'23f | 2Q'23f | 3Q'23f | 2021a | 2022f | 2023f | 2024f |
|--|--------|--------|--------|--------|--------|--------|--------|-------|-------|-------|-------|
| Real GDP (Percent Change Annualized) | -1.6 | 3.3 | 1.1 | 1.5 | 1.3 | 1.0 | 1.2 | 5.7 | 2.4 | 1.4 | 1.4 |
| CPI (Percent Change Year-over-Year) | 8.0 | 8.7 | 8.8 | 8.0 | 6.5 | 4.4 | 3.1 | 4.7 | 8.4 | 4.1 | 1.2 |
| Payroll Jobs (Average Monthly Diff., Ths.) | 573 | 375 | 250 | 225 | 200 | 175 | 150 | 514 | 356 | 166 | 150 |
| Unemployment Rate (Percent) | 3.8 | 3.6 | 3.6 | 3.7 | 3.7 | 3.7 | 3.7 | 5.4 | 3.7 | 3.7 | 3.8 |
| Federal Funds Rate (Effective) | 0.12 | 0.77 | 2.33 | 3.04 | 3.38 | 3.38 | 3.38 | 0.08 | 1.57 | 3.38 | 2.96 |
| 10-Yr. Treasury Rate | 1.94 | 2.93 | 3.04 | 2.90 | 2.78 | 2.63 | 2.60 | 1.44 | 2.70 | 2.64 | 2.53 |

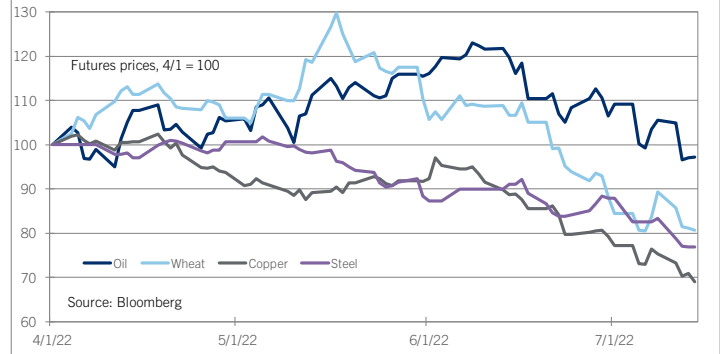
a = actual f = forecast

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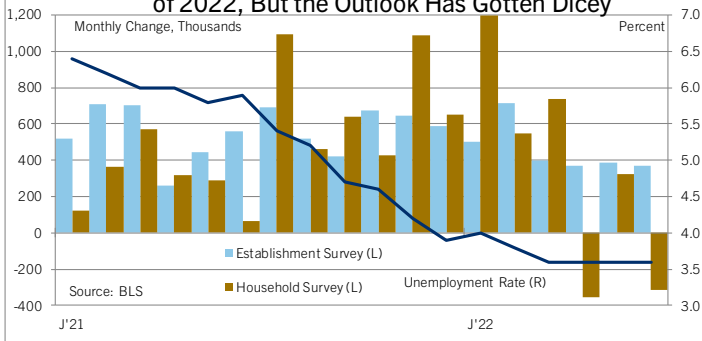
Gas and Diesel Prices Pushed Inflation to a New Record High in June, but Core CPI Is Slowing



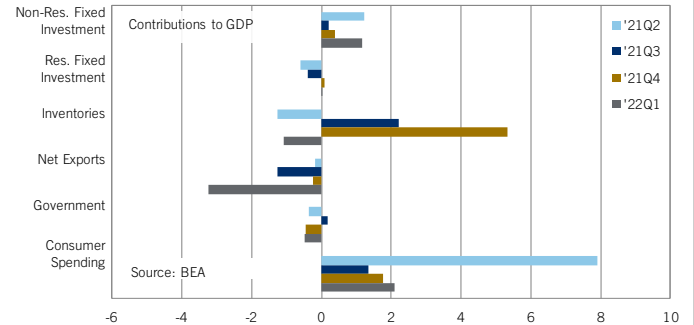
Commodity Prices Are Falling, Inflation Will Slow



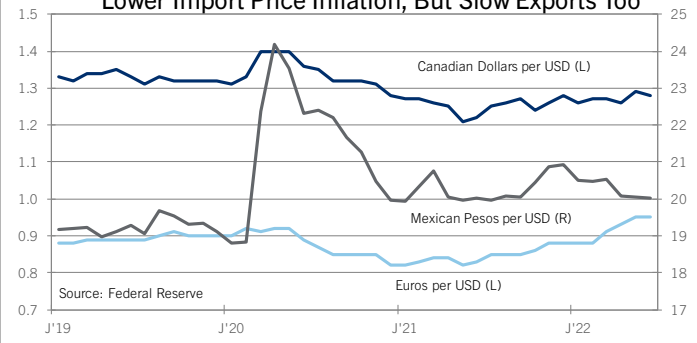
Labor Market Data Say No Recession in the First Half of 2022, But the Outlook Has Gotten Dicy



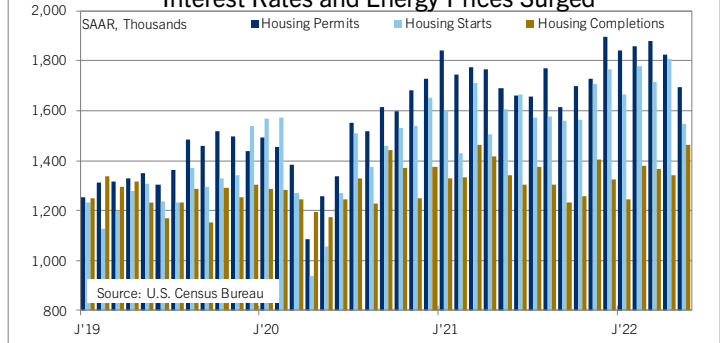
GDP Growth Probably Turned Positive in the 2nd Quarter as Trade and Inventory Headwinds Faded



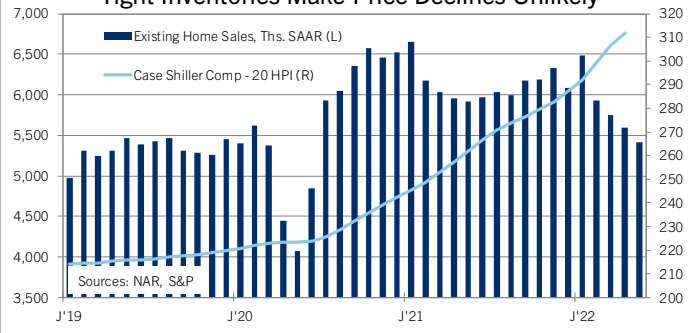
Dollar at a Multi-Decade High Against the Euro Will Lower Import Price Inflation, But Slow Exports Too



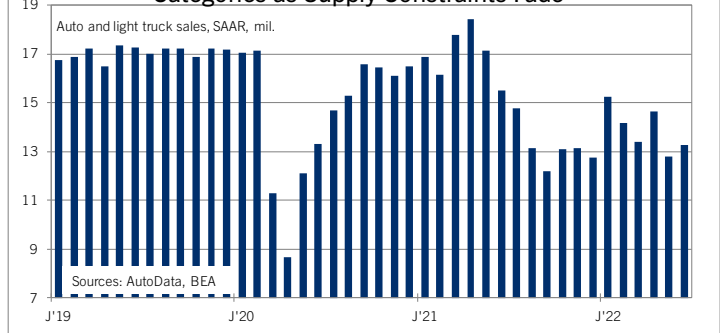
Housing Activity Slowed Sharply in the Spring as Interest Rates and Energy Prices Surged



Housing Sales Will be Slower Going Forward, But Tight Inventories Make Price Declines Unlikely



Auto Sales Will Outperform Other Durable Goods Categories as Supply Constraints Fade



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| | 1Q'22a | 2Q'22p | 3Q'22f | 4Q'22f | 1Q'23f | 2Q'23f | 3Q'23f | 2021a | 2022f | 2023f | 2024f |
|--|-------------|-------------|--------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Output | | | | | | | | | | | |
| Nominal GDP (Billions \$) | 24387 | 25012 | 25457 | 25839 | 26142 | 26389 | 26622 | 22996 | 25174 | 26508 | 27353 |
| Percent Change Annualized | 6.6 | 10.7 | 7.3 | 6.1 | 4.8 | 3.8 | 3.6 | 10.1 | 9.5 | 5.3 | 3.2 |
| Real GDP (Chained 2012 Billions \$) | 19728 | 19889 | 19945 | 20022 | 20088 | 20141 | 20198 | 19427 | 19896 | 20179 | 20470 |
| Percent Change Annualized | -1.6 | 3.3 | 1.1 | 1.5 | 1.3 | 1.0 | 1.2 | 5.7 | 2.4 | 1.4 | 1.4 |
| Pers. Consumption Expenditures | 13881 | 13918 | 13926 | 13932 | 13957 | 13981 | 13988 | 13625 | 13914 | 13985 | 14187 |
| Percent Change Annualized | 1.8 | 1.1 | 0.2 | 0.2 | 0.7 | 0.7 | 0.2 | 7.9 | 2.1 | 0.5 | 1.4 |
| Nonresidential Fixed Investment | 2975 | 3014 | 3022 | 3013 | 3008 | 3000 | 2990 | 2868 | 3006 | 2991 | 2943 |
| Percent Change Annualized | 10.0 | 5.2 | 1.1 | -1.2 | -0.7 | -1.0 | -1.4 | 7.4 | 4.8 | -0.5 | -1.6 |
| Residential Investment | 699 | 712 | 691 | 686 | 677 | 666 | 652 | 708 | 697 | 661 | 643 |
| Percent Change Annualized | 0.4 | 7.8 | -11.1 | -3.3 | -5.0 | -6.4 | -7.9 | 9.2 | -1.5 | -5.2 | -2.6 |
| Change in Private Inventories | 188 | 100 | 0 | -20 | -10 | -40 | -40 | -33 | 67 | -23 | -9 |
| Net Exports | -1545 | -1409 | -1259 | -1176 | -1147 | -1083 | -1023 | -1284 | -1347 | -1060 | -972 |
| Government Expenditures | 3334 | 3360 | 3374 | 3395 | 3412 | 3425 | 3440 | 3376 | 3366 | 3433 | 3486 |
| Percent Change Annualized | -2.9 | 3.1 | 1.6 | 2.6 | 1.9 | 1.6 | 1.7 | 0.5 | -0.3 | 2.0 | 1.5 |
| Industrial Prod. Index (2007=100) | 103.4 | 105.2 | 105.3 | 105.1 | 104.6 | 104.2 | 103.7 | 100.1 | 104.7 | 103.9 | 102.8 |
| Percent Change Annualized | 7.0 | 7.0 | 0.4 | -0.8 | -1.6 | -1.8 | -1.9 | 5.5 | 4.6 | -0.8 | -1.0 |
| Capacity Utilization (Percent) | 77.5 | 78.4 | 78.4 | 77.9 | 77.3 | 76.6 | 75.9 | 75.4 | 78.1 | 76.2 | 74.2 |
| Prices | | | | | | | | | | | |
| CPI (1982-84=100) | 284.6 | 292.0 | 297.2 | 300.7 | 303.0 | 304.9 | 306.5 | 271.0 | 293.6 | 305.6 | 309.1 |
| Percent Change Annualized | 9.2 | 10.8 | 7.3 | 4.7 | 3.2 | 2.5 | 2.2 | 4.7 | 8.4 | 4.1 | 1.2 |
| PCE Price Index (2012=100) | 120.1 | 123.0 | 125.4 | 126.8 | 127.8 | 128.5 | 129.2 | 115.5 | 123.8 | 128.8 | 130.0 |
| Percent Change Annualized | 7.1 | 10.1 | 7.9 | 4.7 | 3.0 | 2.4 | 2.1 | 3.9 | 7.2 | 4.0 | 0.9 |
| GDP Price Index (2012=100) | 123.7 | 126.0 | 127.9 | 129.3 | 130.4 | 131.3 | 132.1 | 118.5 | 126.7 | 131.6 | 133.9 |
| Percent Change Annualized | 8.2 | 7.4 | 6.2 | 4.6 | 3.4 | 2.8 | 2.4 | 4.2 | 6.9 | 3.9 | 1.7 |
| PPI, Final Demand (Nov. 2009=100) | 135.2 | 138.7 | 141.7 | 144.1 | 146.1 | 147.9 | 149.4 | 126.7 | 139.9 | 148.5 | 152.3 |
| Percent Change Annualized | 13.1 | 10.8 | 8.9 | 7.0 | 5.7 | 4.9 | 4.1 | 3.9 | 8.2 | 4.9 | 2.6 |
| Crude Oil, WTI (\$/barrel) | 94.3 | 108.4 | 110.0 | 110.0 | 95.0 | 90.0 | 87.0 | 67.6 | 105.7 | 89.3 | 80.0 |
| Labor Markets | | | | | | | | | | | |
| Payroll Jobs (Average Monthly Diff., Ths.) | 573 | 375 | 250 | 225 | 200 | 175 | 150 | 514 | 356 | 166 | 150 |
| Unemployment Rate (Percent) | 3.8 | 3.6 | 3.6 | 3.7 | 3.7 | 3.7 | 3.7 | 5.4 | 3.7 | 3.7 | 3.8 |
| Average Weekly Hours | 34.6 | 34.5 | 34.5 | 34.4 | 34.4 | 34.4 | 34.4 | 34.8 | 34.5 | 34.4 | 34.3 |
| Population (Millions) | 333.6 | 334.1 | 334.7 | 335.3 | 335.9 | 336.4 | 337.0 | 332.1 | 334.4 | 336.7 | 339.0 |
| Percent Change Annualized | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 | 0.7 |
| Personal Income | | | | | | | | | | | |
| Average Hourly Earnings (\$) | 31.64 | 31.80 | 32.09 | 32.44 | 32.77 | 32.98 | 33.25 | 30.60 | 31.99 | 33.14 | 34.30 |
| Percent Change Annualized | 5.2 | 2.1 | 3.7 | 4.5 | 4.1 | 2.6 | 3.4 | 4.2 | 4.6 | 3.6 | 3.5 |
| Real Disp. Income (2012 Billions \$) | 15152 | 15067 | 15032 | 15161 | 15328 | 15466 | 15647 | 16032 | 15103 | 15571 | 16167 |
| Percent Change Annualized | -7.8 | -2.2 | -0.9 | 3.5 | 4.5 | 3.7 | 4.7 | 2.3 | -5.8 | 3.1 | 3.8 |
| Personal Saving Rate (Percent) | 5.6 | 5.3 | 5.4 | 5.6 | 5.8 | 6.0 | 6.1 | 12.1 | 5.5 | 6.0 | 6.5 |
| Housing | | | | | | | | | | | |
| Housing Starts (Ths., Ann. Rate) | 1720 | 1604 | 1579 | 1587 | 1589 | 1573 | 1564 | 1605 | 1623 | 1572 | 1582 |
| Exst. SF Home Sales (Ths., Ann Rate) | 5380 | 4905 | 5016 | 5062 | 5093 | 5113 | 5154 | 5418 | 5091 | 5133 | 5245 |
| New SF Home Sales (Ths., Ann Rate) | 779 | 681 | 706 | 710 | 714 | 721 | 721 | 769 | 719 | 719 | 729 |
| Case/Shiller HPI (Jan. 2000=100) | 290.6 | 303.8 | 314.3 | 321.3 | 326.0 | 329.2 | 331.9 | 260.1 | 307.5 | 330.3 | 337.8 |
| Year/Year Percent Change | 20.0 | 19.3 | 17.8 | 16.2 | 12.2 | 8.4 | 5.6 | 17.1 | 18.2 | 7.4 | 2.3 |
| Consumer | | | | | | | | | | | |
| Consumer Confidence® (Conference Board) | 108.1 | 103.5 | 97.0 | 97.3 | 98.5 | 100.4 | 105.1 | 112.7 | 101.5 | 103.0 | 116.8 |
| Car and Light Truck Sales (Millions) | 14.3 | 13.3 | 14.4 | 16.0 | 17.0 | 17.7 | 18.3 | 15.1 | 14.5 | 17.9 | 19.2 |
| Interest Rates (Percent) | | | | | | | | | | | |
| Federal Funds Rate (Effective) | 0.12 | 0.77 | 2.33 | 3.04 | 3.38 | 3.38 | 3.38 | 0.08 | 1.57 | 3.38 | 2.96 |
| Prime Rate | 3.29 | 3.94 | 5.45 | 6.16 | 6.50 | 6.50 | 6.50 | 3.25 | 4.71 | 6.50 | 6.08 |
| 1-Month LIBOR | 0.22 | 1.01 | 2.51 | 3.21 | 3.53 | 3.53 | 3.54 | 0.10 | 1.74 | 3.53 | 3.12 |
| 3-Month LIBOR | 0.51 | 1.53 | 2.85 | 3.43 | 3.55 | 3.49 | 3.49 | 0.16 | 2.08 | 3.50 | 3.02 |
| 1-Yr. Treasury Rate | 0.96 | 2.20 | 3.05 | 3.29 | 3.34 | 3.28 | 3.21 | 0.10 | 2.38 | 3.22 | 2.57 |
| 5-Yr. Treasury Rate | 1.82 | 2.95 | 3.08 | 3.04 | 2.94 | 2.79 | 2.70 | 0.86 | 2.72 | 2.77 | 2.40 |
| 10-Yr. Treasury Rate | 1.94 | 2.93 | 3.04 | 2.90 | 2.78 | 2.63 | 2.60 | 1.44 | 2.70 | 2.64 | 2.53 |
| 30-Yr. Fixed Rate Mortgage | 3.79 | 5.24 | 5.89 | 5.95 | 5.65 | 5.24 | 4.88 | 2.96 | 5.22 | 5.10 | 4.62 |

a = actual p = preliminary f = forecast

July 11, 2022

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