National Economic Estimating Conference
Executive Summary
December 18, 2023

The National Economic Estimating Conference met on December 18, 2023, and adopted the control forecast. Relative to the July 2023 forecast, multiyear data revisions made the interpretation of recent actuals challenging, with significantly higher levels coming into the beginning of the forecast period for several key variables. To ameliorate these discontinuities, much of the conference discussion focused on changes in growth rates between the two forecasts. In this respect, the growth rates for many variables showed improvement in the current year (FY 2023-24), a somewhat surprising result in an environment of persistent inflation and tight financial conditions. Nevertheless, future growth rates for the key metrics generally exhibit mixed results with some coming in lower and others little changed.

Overall, S&P Global considers some weakening of economic conditions necessary to bring down the still unacceptably high levels of inflation to the Federal Reserve's objective of 2% within an acceptable timeframe. In their view, this requires a period of below trend growth, referred to as a growth recession, to cool off the economy and reduce wage pressures on inflation. In addition, global uncertainties related to the oil market, the war in Ukraine, and now a war in the Middle East continue to affect the US economy.

Expectations for the Real Expenditures grouping are important to the state's largest revenue source, the Sales Tax. Relative to the prior forecast, the December forecast mostly has stronger growth rates in the 2023-24 fiscal year, but only four of the 13 metrics in this grouping show continued improvement into FY 2024-25. The other nine have weaker growth rates than previously expected in the second year—or, in the case of fixed residential investment, is weaker in both years. Real GDP, real consumer spending, government spending and inventory investment all follow this pattern.

As an example, real GDP grew a weaker than forecast 1.6% for the full 2022-23 fiscal year. Growth for the current year (FY 2023-24) improves to 2.5% and then declines to 1.1% in FY 2024-25. At the end of the forecast horizon, annual growth settles in close to S&P's estimate of potential GDP (1.6% to 1.7%); however, this is slightly lower than expected in July and overall sluggish relative to historical performance. In this regard, the FY 2018-19 rate was 2.3% and a long-term growth rate of 2.2% was expected prior to the pandemic.

Similarly, real consumer spending surged by 5.5% in FY 2021-22 and stepped back to 1.7% in FY 2022-23. This year, spending accelerates to 2.3%, but then shifts down to 1.3% in FY 2024-25 as consumers try to maintain their standard of living in a continuing high-cost environment. Only in the second half of the forecast does growth increase to the 2% range, with rates comparable to the pre-pandemic history. Note that this aggregated number does not speak to composition. According to S&P Global data, in FY 2023-24, real personal consumption expenditures (PCE) on motor vehicles & parts, is expected to increase 0.7%, while real PCE on services is expected to increase 2.2%.

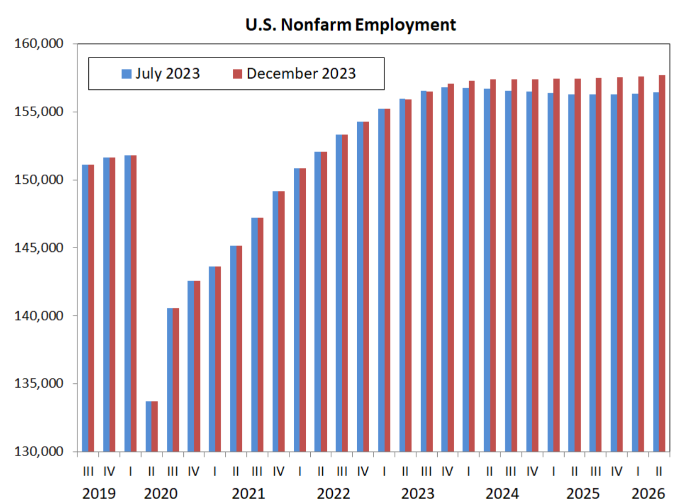
On the other hand, the Components of Income grouping has more varied outcomes that align better with the seesawing transfer payments and labor market disruptions during and after the pandemic. The headline metric for this grouping is personal income. According to an analysis by S&P

Global, the income support provided by federal pandemic relief measures averaged $2.7 trillion at an annual rate over the first half of 2021, dropped to $0.7 trillion in the fourth quarter, and shrank to near zero in 2023. As a result, personal income stayed strongly positive in FY 2019-20 and grew by 9.0% over the prior year in FY 2020-21. In tandem with the loss of these relief programs, personal income growth only notched 3.3% in FY 2021-22, but accelerated to 5.0% in FY 2022-23 as wages played catch-up with inflation in a tight labor market. Personal income has anticipated growth for this year (4.8%) that is unchanged from the expectations in the summer, but higher growth for next year (5.3%). Thereafter, growth remains solidly above 4%, mostly falling below—albeit near to—the prior forecast. Other than FY 2025-26, this is lower than the 4.6% long-term growth expected pre-pandemic.

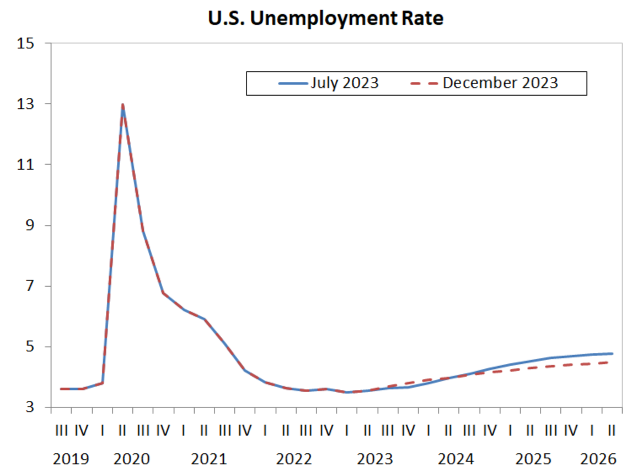
Nonetheless, this is only part of the income story. Real disposable income swung from growth of 4.7% and 6.2% during the pandemic fiscal years 2019-20 and 2020-21 to a contraction of -4.8% in FY 2021-22 as government income support retreated and inflation took off. While turning positive, it only inched up 0.9% in FY 2022-23. Growth peaks at 3.3% in the current fiscal year and drops only slightly to 3.2% in FY 2024-25 before receding to an above 2% rate thereafter. The single largest driver of personal income—wages and salaries—is expected to see moderating growth in the future after recording near record-high growth in FY 2021-22 of 9.7% (the record was 12.8% in FY 1978-79). This year will likely see 5.5% growth, before a retreat to approximately 4.0% over the rest of the forecast period.

In FY 2022-23, households reduced their saving rate to a level (4.1%) last seen at the onset of the Great Recession as they battled the effects of high inflation for the second year. This year, saving will continue near this low level (4.3%). Some households have even turned to the use of credit for additional income support. According to the Federal Reserve Bank of New York's *Quarterly Report on Household Debt and Credit*, total household debt increased by 1.3% to $17.29 trillion in the third quarter of the 2023 calendar year. Credit card balances were among the items experiencing significant jumps in that quarter. In the longer run, S&P Global expects the saving rate to settle around 8%, higher than the pre-pandemic 7.3% seen in FY 2018-19 and markedly higher than the prior forecast.

The Employment and Output grouping is really a composite of metrics for several diverse economic markets. Turning first to the labor market, nonfarm employment grew by 3.3% in FY 2022-23 and is projected to advance a stronger than expected 1.5% in the current fiscal year. After that, growth all but flatlines for the following three years (0.2%, 0.1% and 0.2%, respectively) as businesses finally become reluctant to hire and invest in the face of uncertain economic conditions, high interest rates, and rising labor costs. Employment growth then settles to rates of 0.3% to 0.5%, resulting in approximately the same number of jobs as expected pre-pandemic for that period and similar to the prior forecast. Underlying this result is a Labor Force Participation Rate that declines an average of -0.3% each year as the population continues to age.



Relative to the July forecast, unemployment rate expectations are unchanged for the short term and shift only slightly over the next six years. In this regard, the unemployment rate had improved as expected to 3.5% in FY 2022-23, well below the full-employment unemployment rate and a sign of an unsustainably tight labor market. For the current year, both the old and new forecasts have the rate creeping up to 3.8% before finally shifting above 4.0% in response to higher interest rates and slowing economic activity. The rate gradually increases to 4.5% in FY 2026-27 and then slowly retreats to 4.3% throughout the second half of the forecast. S&P Global uses this rate as the full-employment unemployment rate.



In line with the Federal Reserve's first actions to use tight monetary policy to curb inflation in late FY 2021-22, the national housing market is now in its third fiscal year of turmoil. Following single-digit declines in FY 2021-22 and double-digit declines in FY 2022-23, the new forecast embeds yet another year of double-digit declines for existing home sales in FY 2023-24, with even deeper losses than previously predicted. While existing home sales resume growth in FY 2024-25, the market splits with condominiums and cooperatives growing more weakly than previously expected and single-family home sales growing more strongly.

Lagging behind existing home sales in their response to increasing interest rates, housing starts did not turn negative on a fiscal year basis until 2022-23 when starts declined by 14.1%. As relatively high interest rates continue to undermine housing activity, starts remain in a slump with back-to-back declines of 4.5% in FY 2023-24 and 1.3% in FY 2024-25. Starts stay below 1.4 million units annually in FY 2023-24 and thereafter, facing near-term headwinds from doubled mortgage rates and high construction costs. Similar to existing home sales, multi-family starts fare slightly worse.

Several other metrics are noteworthy. Corporate profits is one of the few areas where the outlook has unambiguously weakened throughout the forecast. Book profits edged up only 0.9% in FY 2022-23, while economic profits grew by 5.3%. The forecast for both metrics is markedly softer in FY 2023-24 and FY 2024-25, with economic profits turning negative. This latter variable is particularly important to understanding the path corporate income tax receipts will likely follow. With the exception of two isolated years, the expected growth rates are all lower.

Finally, the price of Brent crude oil will retreat to below $85 per barrel in FY 2023-24 from the $113.3/ barrel seen in the second quarter of 2022 at the onset of the war in Ukraine. Prices will not stay at this low level for long. The new forecast shows that the price per barrel moves close to $100 towards the end of the period. While this end-level is above pre-pandemic forecasts, it is below the July forecast. Significantly, the emerging threat to gas prices from disturbances in the Red Sea have yet to be included in the forecast.