Goldman Sachs | Economics Research

30 May 2022 | 1:10AM EDT

US Economics Analyst

Private-Sector Growth: Down but Not Out (Hill/Abecasis)

- Worrying news in corporate earnings calls and downside surprises in the May survey data have led some investors to worry that a recession is arriving ahead of schedule. We review the latest signals and fundamental drivers of the growth outlook across four dimensions: momentum, consumer demand, business activity, and the labor market.
- **Growth Momentum:** Realized growth had already slowed by the winter, with domestic demand, gross domestic income, and our CAI together suggesting a pace of 2-3%—down from +5.6% on average during 2021. The +1.5% preliminary May CAI reading suggests that growth has slowed further but nonetheless remains positive.
- **Consumer demand:** Alternative data indicate consumer weakness in May that is not yet visible in the official data—perhaps in response to tighter financial conditions and higher consumer prices. This sequential weakness appears more pronounced for retail goods, consistent with a reopening-related demand shift back toward services. Services spending remains 5% below trend because of virus-sensitive categories like spectator events and travel, and coupled with very healthy household balance sheets and moderating headline inflation, we expect the early-summer lull in consumption growth will prove short-lived.
- **Business activity:** Despite declining business confidence and high-profile earnings misses from retail and tech bellwethers, we find that business activity is outperforming sentiment. The much-maligned Q1 earnings season was actually better than expected overall, with S&P EPS growth 6pp above consensus on the back of 17% year-on-year revenue growth. And equity analyst forecasts for revenue and capex actually *improved* following the financial results and conference calls of the S&P 1500 firms that have reported. Relatedly, while the shipments, orders, and business activity measures of the May business surveys declined, they still indicate a solid pace of growth.
- **Labor market:** Employment indicators also indicate deceleration rather than contraction. The employment measures in the April and May business surveys generally outperformed the headline and activity components. And while jobless claims and layoff announcements have increased, both moves so far look like normalization from the abnormally depressed levels of 2021. Job openings also moderated somewhat in late spring but remain 40-60% above 2019 levels,

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depending on the measure.

- These facts suggest a growing disconnect between perceptions of the economy and actual business activity. Relatedly, a May survey of CEOs found that a majority now expect a recession. However, the same survey indicated that nearly two thirds of CEOs nonetheless plan to expand their workforce.
- While our growth forecast has long been below consensus, we believe fears of declining economic activity this year will prove overblown unless new negative shocks materialize. We continue to forecast slower but not recessionary growth, with a trade-related rebound to +2.8% in Q2 followed by +1.6% average growth over the following four quarters (qoq ar).

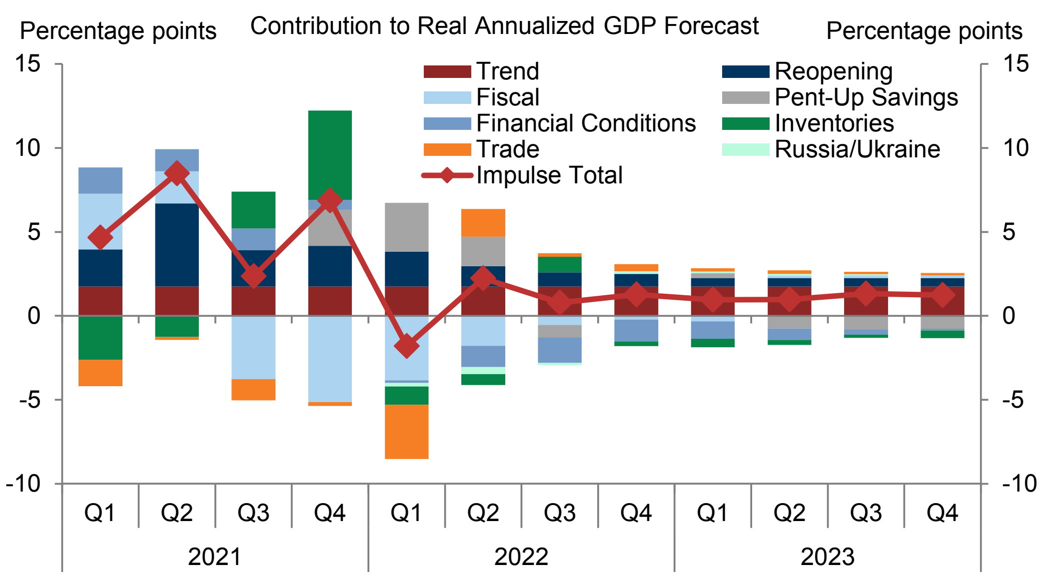
Private-Sector Growth: Down but Not Out

Last fall, we argued that tighter fiscal and monetary policy would cause growth to slow to a near-potential pace by late 2022. We subsequently downgraded the growth outlook further in response to the Russia-Ukraine War and again after the further tightening in financial conditions during the spring. While our growth forecast has long been below consensus, worrying news in recent corporate earnings calls and downside surprises in the May survey data have led some investors to go further and express concern that a recession might be arriving ahead of schedule. We assess these concerns by revisiting the near-term growth outlook across four dimensions: momentum, consumer demand, business activity, and the labor market.

Temperature Check

Our estimates of the various growth impulses affecting the US economy argue for 1-1.5% GDP growth in 2022 and 2023, as shown in Exhibit 1. These impulses include drags from tighter financial conditions and reduced fiscal support, as well as a waning boost from reopening and the sun-setting effects of pent-up savings on consumption growth.

Exhibit 1: Fundamentals Argue for 1-1.5% Growth in 2022 and 2023

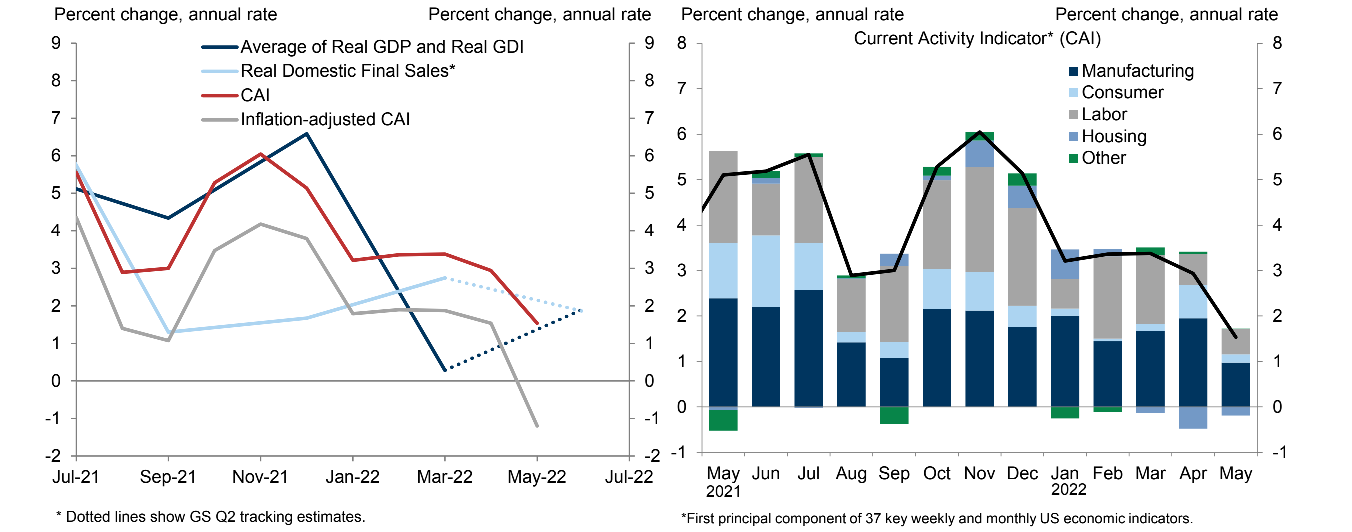


Source: Department of Commerce, Goldman Sachs Global Investment Research

As shown in Exhibit 2, realized growth had already slowed to a 2-3% pace during the winter and early spring, in part reflecting declines in interest-rate-sensitive sectors like housing and durable goods. While we expect GDP growth to rebound from the foreign trade-led weakness in Q1, our preliminary May Current Activity Indicator (CAI) stands at +1.5% annualized (vs. +3.3% on average in Q1).[1]

[1] Additionally, our version of the CAI that adjusts for nominal bias in business surveys now stands at -1.0% annualized (vs. +1.7% on average in Q1), and we expect real domestic final sales growth to decelerate from +2.7% annualized in Q1 to +1.9% in Q2.

Exhibit 2: Underlying Growth Already Slowed to 2-3% During the Winter and Early Spring, Helped by a Slowdown in Interest-Sensitive Sectors Like Housing



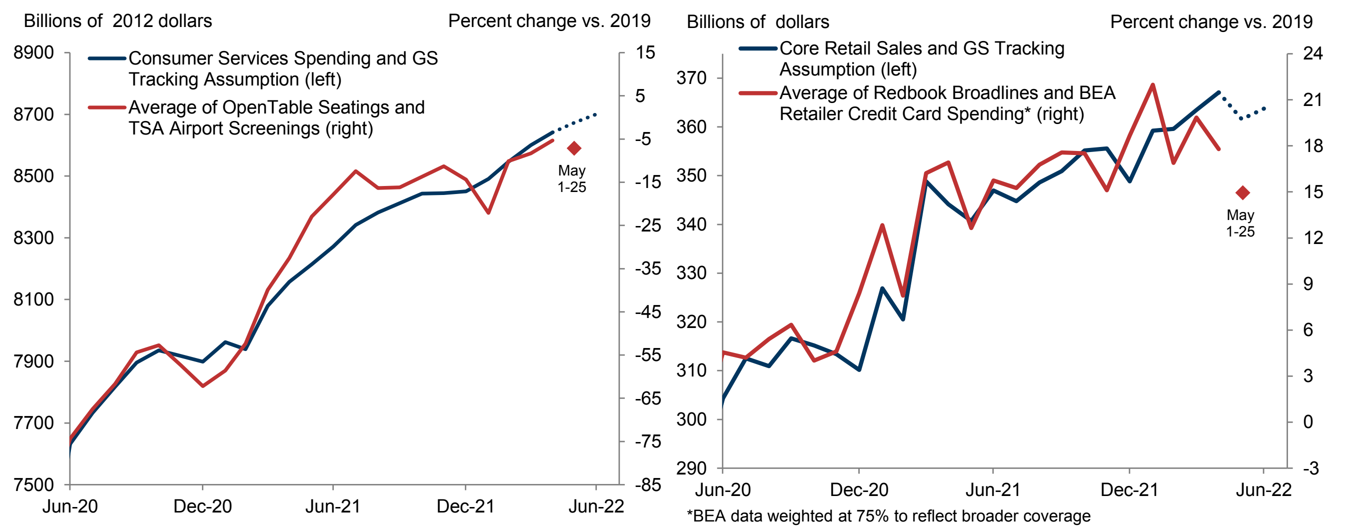
Source: Department of Commerce, Goldman Sachs Global Investment Research

Taken together, the activity data reported so far this year indicate a slowing but still positive trend in GDP growth, at roughly 2-3% during the winter and closer to 1-2.5% so far in Q2.

Consumption Growth: Soft in May, Not Going Away

Alternative data indicate a slowdown in consumer spending in May—perhaps in response to tighter financial conditions and higher consumer prices. As shown in Exhibit 3, the sequential weakness appears more pronounced for retail goods, consistent with a reopening-related demand shift back toward services.

Exhibit 3: Consumer Spending Likely Slowed in May, Particularly for Discretionary Goods Categories

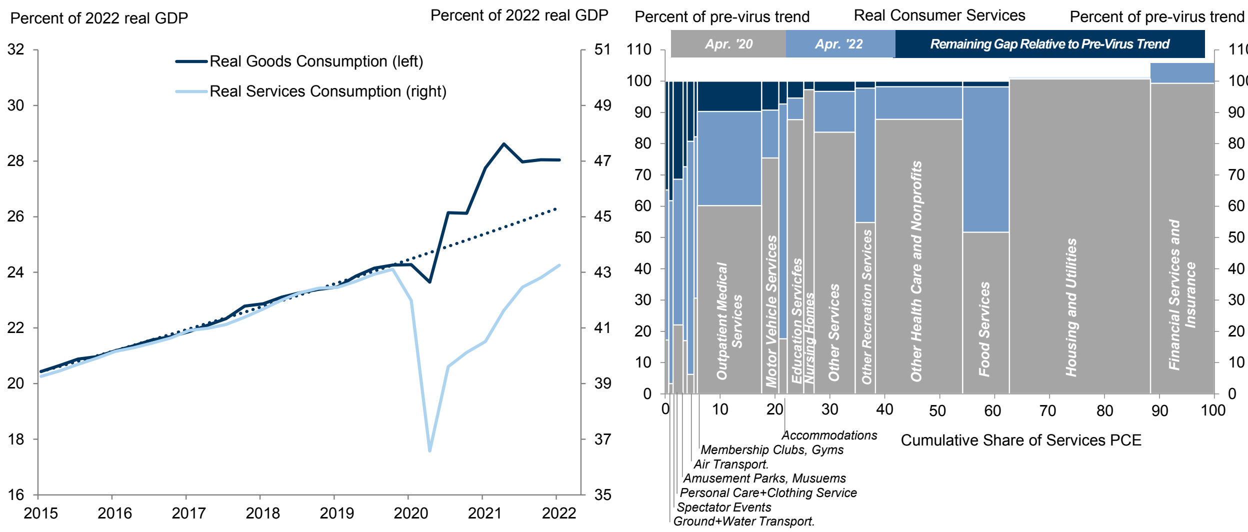


Source: Department of Commerce, OpenTable, Transportation Security Administration (TSA), Census Bureau, Goldman Sachs Global Investment Research

Weaker consumer sentiment and the mounting drag from financial conditions suggests some of this weakness could persist into June, and our +2.7% tracking estimate for annualized real consumption growth in Q2 assumes an outright decline in May that only partially reverses in June.[2]

Looking beyond the early-summer spending weakness, we continue to expect a rebound in services consumption in the second half of the year. Real services spending remains roughly 5% below its pre-pandemic trend—mostly due to continued weakness in virus-sensitive categories like medical, recreation, and travel (see Exhibit 4). These categories should continue to recover as covid concerns ease.

Exhibit 4: Consumer Spending Likely Slowed in May, Particularly for Discretionary Goods Categories

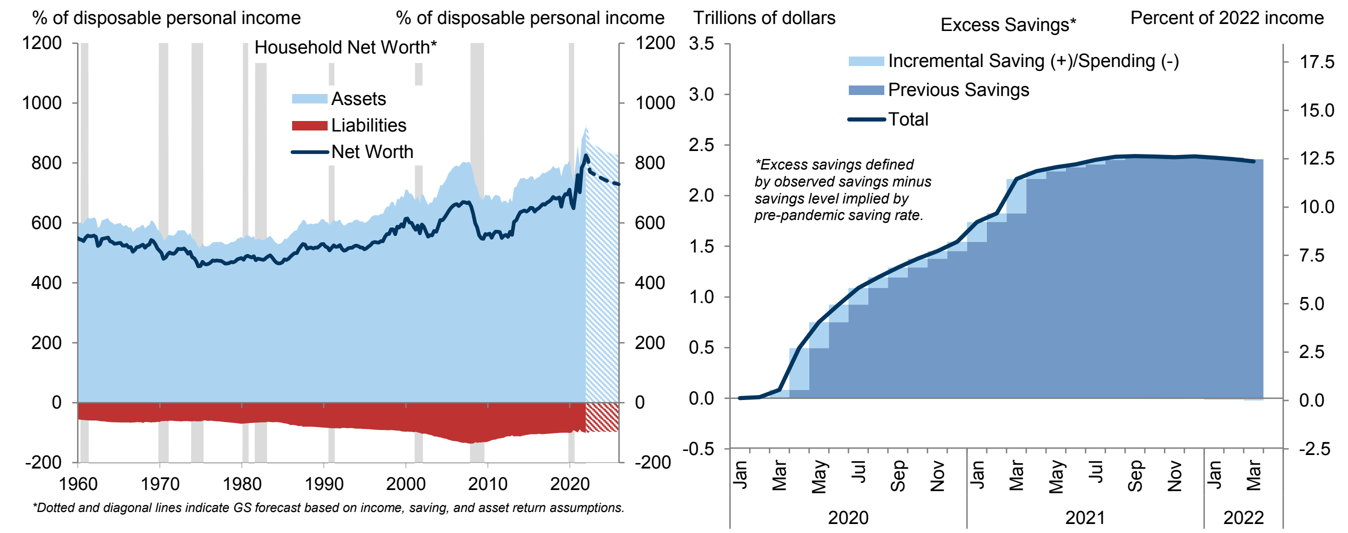


Source: Department of Commerce, Goldman Sachs Global Investment Research

Additionally, household balance sheets are very healthy, suggesting that consumers can supplement their spending by drawing down pent-up savings accumulated during the pandemic. As shown in Exhibit 5, household net worth as a share of personal income remains near all-time highs even after taking into account the recent asset price declines, and we estimate that excess savings accumulated during the pandemic stand at roughly 12.5% of annual income. This has allowed consumers to support spending by lowering their saving rates, which declined to 4.4% in April.

2 We assume real consumption growth of -0.6% in May and +0.3% in June following the 0.7% gain reported for April.

Exhibit 5: Healthy Household Balance Sheets and Pent-Up Savings Are a Major Tailwind



Source: Federal Reserve, Department of Commerce, Goldman Sachs Global Investment Research

Business Activity Outperforming Sentiment

High-profile earnings misses from some retailers and technology companies have contributed to the recent growth fears. However, our equity strategists note that Q1 earnings season as a whole has been better than expected, featuring 11% EPS growth for the S&P 500—6pp above consensus—on the back of 17% revenue growth—including +13% ex-energy. Relatedly, while a May survey of CEOs found a majority now expect a recession, the same survey indicated that nearly two-thirds of CEOs nonetheless plan to expand their workforce.

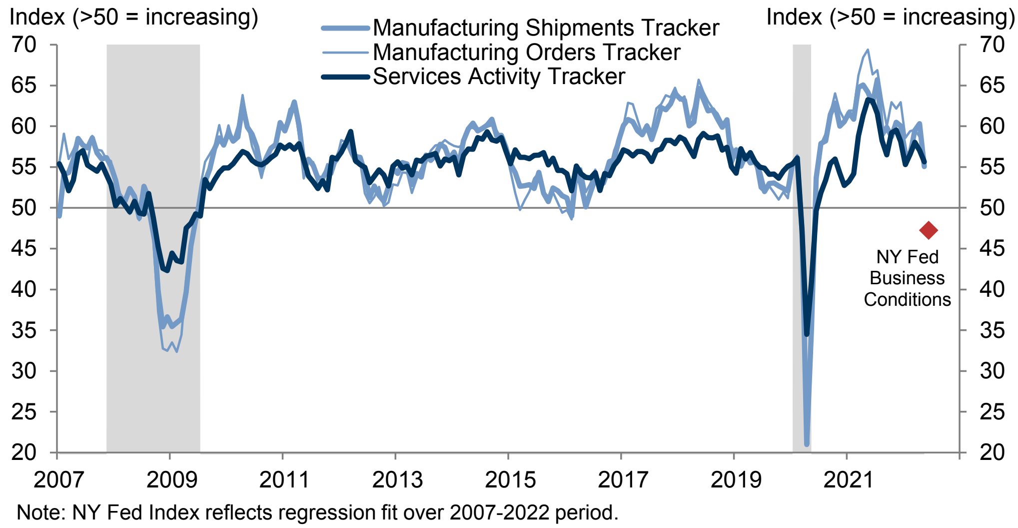
Rather than economic weakness, an alternative explanation for some of the downside earnings surprises is the changing composition of demand amid this year's rapid reopening. Specifically, the transition from goods to services spending poses a revenue headwind and a planning challenge for retailers, and the transition from digital activity to in-person interaction poses revenue and user-growth headwinds for tech firms. On the former, retail bellwethers Walmart and Target actually reported *better-than-expected* revenues[3] despite declining earnings, and the Target management team was emphatic that they were not seeing signs of a consumer slowdown. Their disappointing earnings results instead reflected increased discounting in some stay-at-home categories, as well higher input prices for products and labor.

Are business conditions deteriorating markedly in Q2? Despite the market narrative of declining business activity and sharply lower management confidence, the activity measures of the surveys available for April and May indicate a deceleration rather than a collapse. As shown in Exhibit 6, our survey aggregates for manufacturing shipments and services business activity have declined over the past two months, but both remain handily in expansionary territory (at 55.1 and 55.6 respectively). Nor has the

[3] At +2.0% and +1.8% above consensus, respectively. The increase in discounting resulted from rapid inventory restocking ahead of a surprisingly rapid shift in the composition of consumer demand towards reopening categories like luggage and beauty.

manufacturing orders component—traditionally thought to be a leading indicator—diverged to the downside (tracking at 55.3 in May).

Exhibit 6: Despite a Few Headline Misses, Business Surveys Still Indicate Firm or Solid Growth in May



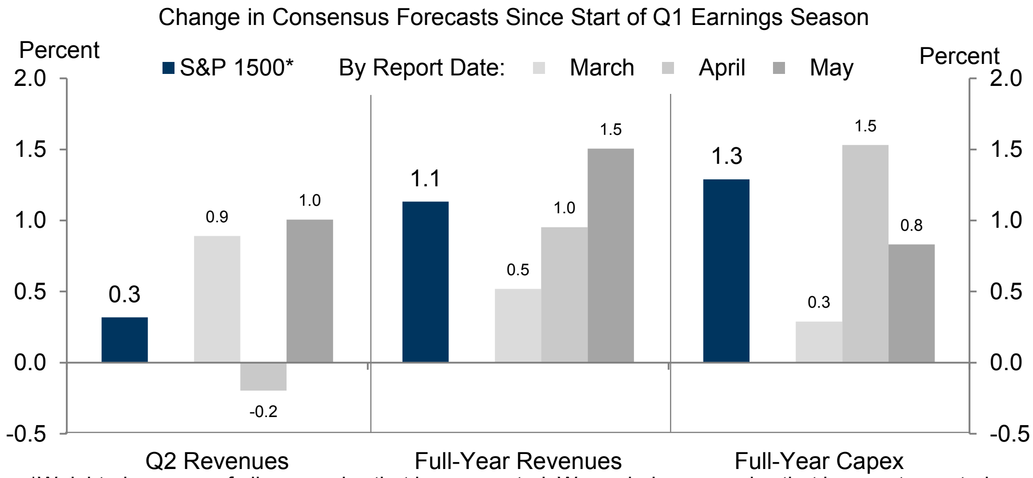
Source: Census Bureau, Federal Reserve, Goldman Sachs Global Investment Research

Swings in sentiment and market prices often produce volatility in some of the more subjective survey questions, including the "general business conditions" diffusion index from the New York Fed that declined sharply in May (red dot in the same exhibit). These facts suggest a growing disconnect between perceptions of the economy and actual business conditions—which in theory could resolve in either direction.

To gauge whether businesses are observing actual demand weakness or changing their own spending behavior, we review the revenue and capex forecasts for S&P 1500 companies, specifically those that have reported Q1.[4] Our goal was to gauge the degree to which fundamentals are deteriorating or expected to deteriorate in Q2 and 2022. But as shown in Exhibit 7, analyst forecasts for both revenues and capex have *improved* on net (+0.3% for Q2 revenues, +1.1% for full-year revenues, and +1.3% for full-year capex; all on a weighted basis). In contrast, revenue per share estimates generally fell during the early innings of the last two recessions, trending down throughout most of 2008 and declining almost continually from March through June 2020.

4 During their post-earnings conference calls, reporting firms provide quantitative or qualitative guidance on business activity and their expectations for the subsequent quarter.

Exhibit 7: Corporate Outlooks Are Improving—Even Among Companies Reporting in May



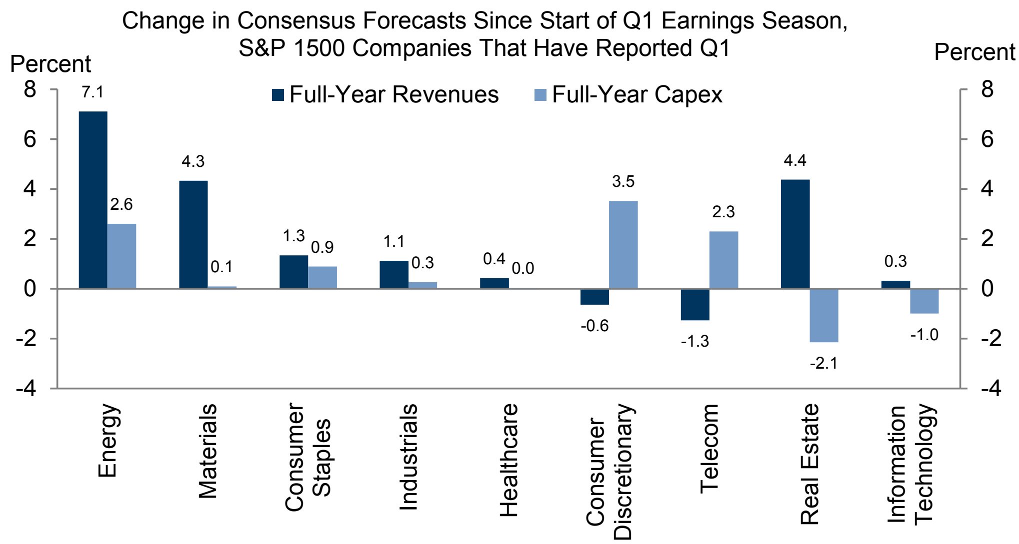
*Weighted average of all companies that have reported. We exclude companies that have not reported because their management teams have not yet provided updated guidance to the equity analysts in consensus.

Source: Company data, Goldman Sachs Global Investment Research

Furthermore, revenue guidance has arguably been more upbeat for the late-reporters, whose management teams have a more timely view of business activity. As shown by the grey columns of the same exhibit, despite sequentially weaker survey and sentiment data in May, revenue upgrades have on net been the largest for the subset of companies that reported in that month (as opposed to in March or April).

Exhibit 8 decomposes the industry breakdown of these forecast revisions and indicates fairly broad-based improvement. Notable laggards include the revenue outlook for consumer discretionary and telecom and the capex outlook for real estate and information technology—all of which could in part reflect the rapid reopening of the economy and related shifts in the composition of demand, as discussed previously.

Exhibit 8: Pockets of Weakness? Revenue Outlook Softening for Consumer Discretionary and Telecom; Real Estate and Tech Reining in Capex Budgets

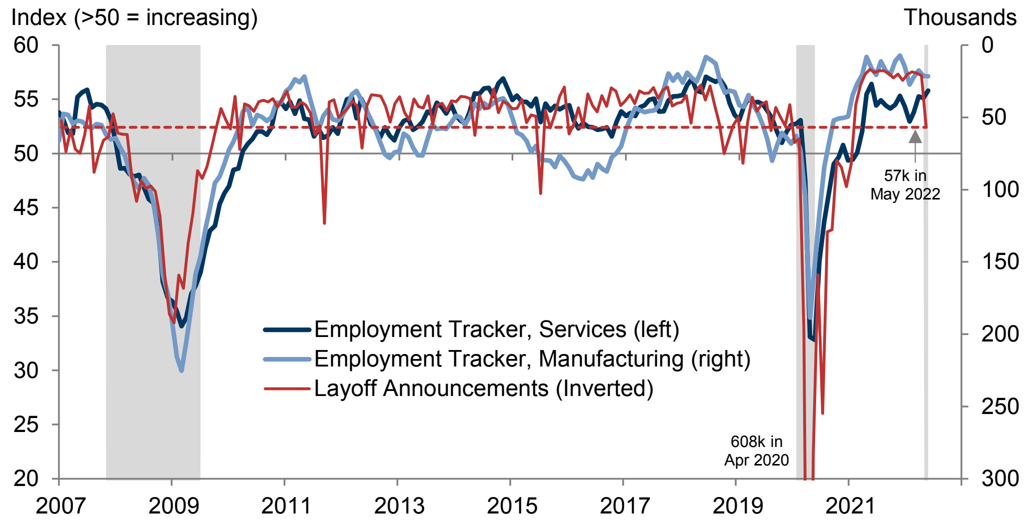


Source: Bloomberg, Goldman Sachs Global Investment Research

Job Growth to Slow but Remain Positive

Broadly speaking, labor market indicators also indicate a deceleration rather than a contraction. As shown in the blue lines of Exhibit 9, the employment components of the monthly business surveys were relatively resilient in April and May, particularly for services (dark blue line; again, perhaps related to the reopening). And while layoff activity is clearly on the rise (red line, inverted), so far it appears to mark a normalization from the abnormally depressed levels of 2021. Initial jobless claims tell a similar story. While they have rebounded to 207k on average over the last four weeks from 178k on average in March, they remain below the 218k average of 2019 and well below the 312k average in the 2010s.

Exhibit 9: The Labor Market Is Cooling, But Not at a Concerning Pace

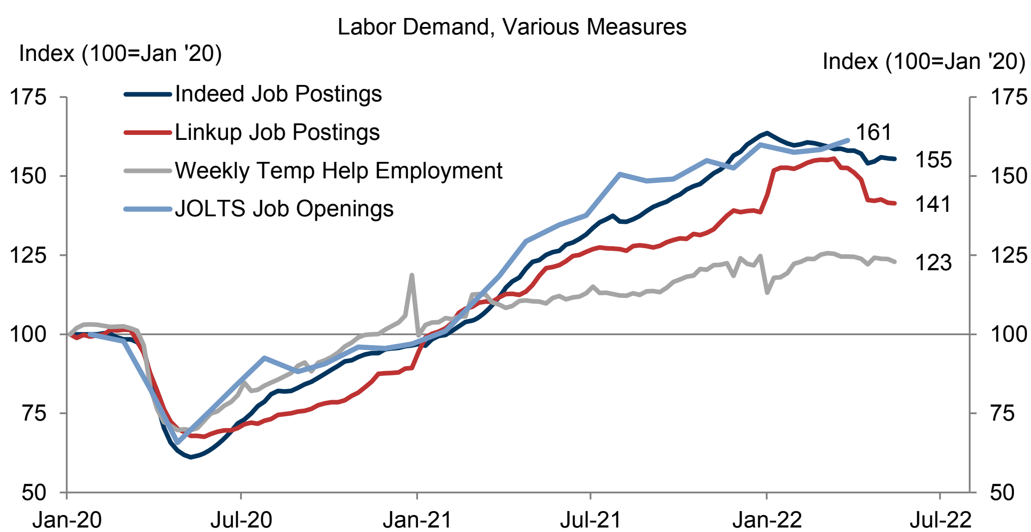


May 2022 layoff announcements nowcasted from XN data

Source: Challenger Gray & Christmas, Goldman Sachs Global Investment Research

Job openings also appear to be moderating somewhat, but again hardly to concerning levels. Exhibit 10 plots four measures of labor demand, all of which continue to indicate a large shortage of workers relative to pre-pandemic. We also believe most of the elevated level of job postings reflects genuinely strong labor demand, because two-thirds of job listings were posted or re-posted in the last 90 days, and because we estimate duplicate job listings related to remote work can only explain 3pp of the increase since 2019.

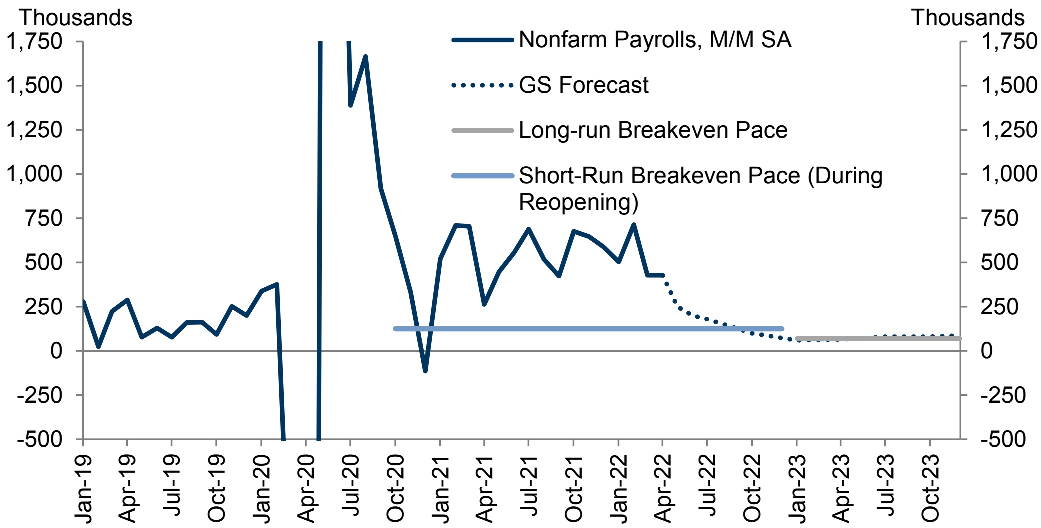
Exhibit 10: Millions of Jobs Remain Unfilled, Even After the Recent Pullback in Postings



Source: Indeed, Linkup, Department of Labor, Goldman Sachs Global Investment Research

Exhibit 11 plots the monthly pace of job gains as well as our forecasted path in 2022 and 2023. The pullback in labor demand from an unprecedented to a high level, coupled with continued labor supply constraints, argue for a further slowing in job growth in the spring and early summer: We forecast a 210k average pace in the next three reports.

Exhibit 11: We Forecast Payroll Growth to Continue to Slow This Year, Falling Through the Breakeven Pace Required to Stabilize the Jobless Rate



Source: Department of Labor, Goldman Sachs Global Investment Research

Additionally, if GDP growth indeed falls to a potential-like pace in the second half of the year, payroll growth is likely to approach or fall below the breakeven pace consistent with a stable unemployment rate. We estimate this breakeven pace of nonfarm payrolls is roughly 125k/month in the short-run due to rebounding labor force participation and is roughly 75k/month over the medium-term (see light blue and grey lines, respectively).

Although we expect momentum in job gains will push the unemployment rate to a low of 3.4% at some point during the summer, we forecast that the unemployment rate will subsequently rise back to 3.5% at end-2022, and rise further to 3.7% at end-2023.

We remain optimistic that a recession and related sharp rise in the unemployment rate can be avoided, and the measured slowdown we are observing in job openings, consumer spending, and broader growth momentum are so far consistent with this outcome. Coupled with the upbeat revenue and capex guidance from management teams, we believe fears of declining economic activity this year will prove overblown unless new negative shocks materialize. We continue to forecast slower but not recessionary growth, with a trade-related rebound to +2.8% in Q2 followed by +1.6% average growth over the following four quarters (qoq ar).

Spencer Hill

Manuel Abecasis

The US Economic and Financial Outlook

THE US ECONOMIC AND FINANCIAL OUTLOOK
(% change on previous period, annualized, except where noted)

	2020	2021	2022 (f)	2023 (f)	2024 (f)	2025 (f)	2022 Q1	2022 Q2	2022 Q3	2022 Q4	2023 Q1	2023 Q2	2023 Q3	2023 Q4
OUTPUT AND SPENDING														
Real GDP	-3.4	5.7	2.5	1.6	1.8	1.9	-1.5	2.8	2.3	1.5	1.3	1.5	1.5	1.8
Real GDP (annual=Q4/Q4, quarterly=yoy)	-2.3	5.5	1.3	1.5	1.9	1.9	3.5	2.6	2.6	1.3	2.0	1.6	1.4	1.5
Consumer Expenditures	-3.8	7.9	3.0	1.5	1.7	1.9	3.1	2.7	1.6	1.5	1.3	1.5	1.4	1.5
Residential Fixed Investment	6.8	9.2	-4.7	-1.2	2.0	2.0	0.4	-13.7	-5.0	-3.0	1.0	2.0	2.0	2.0
Business Fixed Investment	-5.3	7.4	4.2	2.5	3.5	3.6	9.2	1.8	1.3	2.0	2.8	3.0	3.2	3.4
Structures	-12.5	-8.0	-5.2	-0.8	2.4	3.0	-3.6	-7.8	-4.0	0.0	0.0	0.0	1.0	2.0
Equipment	-8.3	13.1	3.6	1.1	2.8	3.0	13.2	-1.1	-2.0	0.0	2.0	2.5	2.5	2.5
Intellectual Property Products	2.8	10.0	9.6	5.6	4.7	4.5	11.6	10.0	7.5	5.0	5.0	5.0	5.0	5.0
Federal Government	5.0	0.6	-4.4	-1.6	-0.1	0.0	-6.0	-3.0	-3.0	-3.0	-1.0	-1.0	0.0	0.0
State & Local Government	0.9	0.4	0.5	1.0	1.0	1.0	-0.6	0.9	1.0	1.0	1.0	1.0	1.0	1.0
Net Exports ($bn, '12)	-943	-1,284	-1,421	-1,330	-1,320	-1,339	-1,544	-1,406	-1,377	-1,355	-1,345	-1,334	-1,325	-1,317
Inventory Investment ($bn, '12)	-42	-33	133	104	63	60	150	103	140	140	125	110	100	80
Industrial Production, Mfg.	-6.6	6.2	3.6	0.8	1.3	1.6	4.9	2.3	1.3	0.2	0.3	0.8	1.2	1.1
HOUSING MARKET														
Housing Starts (units, thous)	1,395	1,605	1,692	1,720	--	--	1,724	1,687	1,658	1,699	1,719	1,765	1,703	1,692
New Home Sales (units, thous)	831	769	800	888	887	887	777	782	803	836	859	903	901	891
Existing Home Sales (units, thous)	5,638	6,127	5,672	5,640	5,751	5,863	6,057	5,561	5,499	5,571	5,598	5,626	5,654	5,682
Case-Shiller Home Prices (%yoy)*	9.5	18.8	9.0	2.7	3.5	3.8	12.5	11.3	10.1	9.0	--	--	--	--
INFLATION (% ch, yr/yr)														
Consumer Price Index (CPI)**	1.3	7.1	6.2	2.8	2.6	2.4	8.0	7.9	8.0	6.6	5.1	3.9	2.9	2.8
Core CPI **	1.6	5.5	4.8	2.7	2.6	2.5	6.3	5.7	5.7	5.1	4.2	3.5	2.9	2.7
Core PCE** †	1.5	4.9	3.9	2.4	2.3	2.2	5.2	4.7	4.6	4.1	3.6	3.2	2.7	2.5
LABOR MARKET														
Unemployment Rate (%)^	6.7	3.9	3.5	3.7	3.7	3.7	3.6	3.5	3.4	3.5	3.6	3.6	3.7	3.7
U6 Underemployment Rate (%)^	11.7	7.3	6.6	6.7	6.7	6.5	6.9	6.6	6.5	6.6	6.7	6.7	6.7	6.7
Payrolls (thous, monthly rate)	-774	562	270	74	83	60	549	293	153	87	62	70	80	83
Employment-Population Ratio (%)^	57.4	59.5	60.3	60.2	60.1	59.9	60.1	60.2	60.3	60.3	60.3	60.2	60.2	60.2
Labor Force Participation Rate (%)^	61.5	61.9	62.6	62.5	62.4	62.2	62.4	62.4	62.5	62.6	62.5	62.5	62.5	62.5
Average Hourly Earnings (%yoy)	4.9	4.2	5.0	4.2	3.8	3.5	5.4	5.3	4.9	4.5	4.3	4.2	4.1	4.0
GOVERNMENT FINANCE														
Federal Budget (FY, $bn)	-3,129	-2,772	-1,050	-1,100	-1,150	-1,300	--	--	--	--	--	--	--	--
FINANCIAL INDICATORS														
FF Target Range (Bottom-Top, %)^	0-0.25	0-0.25	2.5-2.75	3-3.25	3-3.25	3-3.25	0.25-0.5	1.25-1.5	2-2.25	2.5-2.75	2.75-3	3-3.25	3-3.25	3-3.25
10-Year Treasury Note^	0.93	1.52	3.30	3.15	3.15	3.15	2.32	3.20	3.25	3.30	3.20	3.15	3.15	3.15
Euro (€/$)^	1.22	1.13	1.11	1.20	1.25	1.25	1.11	1.06	1.07	1.11	1.13	1.15	1.18	1.20
Yen ($/¥)^	103	115	125	115	107	107	121	127	125	125	122	120	117	115

* Weighted average of metro-level HPIs for 381 metro cities where the weights are dollar values of housing stock reported in the American Community Survey. Annual numbers are Q4/Q4.
** Annual inflation numbers are December year-on-year values. Quarterly values are Q4/Q4.
† PCE = Personal consumption expenditures. ^ Denotes end of period.
Note: Published figures in bold.
Source: Goldman Sachs Global Investment Research.

Source: Goldman Sachs Global Investment Research

Economic Releases

Date		Time (ET)	Indicator	Estimate GS	Estimate Consensus	Last Report
Tue	May 31	9:00	FHFA House Price Index (March)	n.a.	+2.0%	+2.1%
		9:00	**S&P/Case-Shiller Home Price Index (March)**	**+2.0%**	**+1.90%**	**+2.39%**
		9:45	**Chicago Purchasing Managers' Index (May)**	**53.4**	**55.1**	**56.4**
		10:00	**Consumer Confidence (May)**	**101.3**	**103.9**	**107.3**
		10:30	Dallas Fed Manufacturing Index (May)	n.a.	1.5	1.1
Wed	Jun 01	9:45	S&P Global US Manufacturing PMI (May final)	n.a.	57.5	57.5
		10:00	**Construction Spending (April)**	**+0.3%**	**+0.6%**	**+0.1%**
		10:00	**ISM Manufacturing (May)**	**54.5**	**54.5**	**55.4**
		10:00	JOLTS Job Openings (April)	n.a.	11,400k	11,549k
		17:00	**Lightweight Motor Vehicle Sales (May)**	**13.7M**	**14.30M**	**14.29M**
Thu	Jun 02	**8:15**	**ADP Employment (May)**	**+225k**	**+300k**	**+247k**
		8:30	**Nonfarm Productivity (Q1 final)**	**-7.4%**	**-7.5%**	**-7.5%**
		8:30	**Unit Labor Costs (Q1 final)**	**+12.5%**	**+11.6%**	**+11.6%**
		8:30	**Initial Jobless Claims**	**205k**	**210k**	**210k**
		8:30	Continuing Claims	n.a.	1,333k	1,346k
		10:00	**Factory Orders (April)**	**+0.8%**	**+0.7%**	**+2.2%**
Fri	Jun 03	**8:30**	**Nonfarm Payrolls (May)**	**+275k**	**+325k**	**+428k**
		8:30	**Private Payrolls (May)**	**+250k**	**+303k**	**+406k**
		8:30	**Unemployment Rate (May)**	**3.5%**	**3.5%**	**3.6%**
		8:30	**Average Hourly Earnings (May)**	**+0.4%**	**+0.4%**	**+0.3%**
		8:30	Labor Force Participation (May)	n.a.	62.3%	62.2%
		9:45	S&P Global US Services PMI (May final)	n.a.	53.5	53.5
		10:00	**ISM Services (May)**	**57.0**	**56.5**	**57.1**

Source: Goldman Sachs Global Investment Research

Disclosure Appendix

Reg AC

We, Jan Hatzius, Alec Phillips, David Mericle, Spencer Hill, CFA, Joseph Briggs, Ronnie Walker and Manuel Abecasis, hereby certify that all of the views expressed in this report accurately reflect our personal views, which have not been influenced by considerations of the firm's business or client relationships.

Unless otherwise stated, the individuals listed on the cover page of this report are analysts in Goldman Sachs' Global Investment Research division.

Disclosures

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