

# Volatility, Not Recession

July 29, 2022

There is likely to be a lot of noise about “technical recession” as the real economy contracted for the second quarter in a row. Q2 GDP fell by an annualized 0.9% q/q after having contracted by an annualized 1.6% in Q1.<sup>1</sup> However, a lot of what we are seeing is an inventory story related to supply-chain disruptions. Final sales of domestic product (GDP less private inventories) were up 1.1% after contracting 1.2% in the previous quarter and real consumer spending continued to grow.<sup>2</sup>

## The consumer is still spending

Consumers continue to shift from goods to service spending with the contribution from goods spending subtracting 1.1pp from GDP while increased spending on services adding 1.8pp to GDP. However, even here there are oddities lingering from COVID – consumer spending on food and beverages for off premises consumption subtracted 0.7pp from GDP while spending on food services and accommodation contributed 0.6pp to GDP. Consumers are still straining to maintain a level of post-COVID activity even in the face of higher prices.

## Rate Hikes Begin To Have an Impact on Investment

Housing investment has begun to show the impact of Fed rate hikes with residential investment subtracting 0.7pp from GDP this quarter.<sup>3</sup>

## Recession?

Not yet, in our view. Even with two quarters of negative growth it is our view that the labor market remains too strong for this to be self-sustaining and the inventory contribution to GDP over time should net to zero. However, ongoing volatility related to supply-chain disruptions, consumer spending shifts and geopolitical events seems likely to remain in place for some time. We continue to expect a recession in 2023 that should see an increase in unemployment and a related decline in consumption as well as a shift in Fed’s policy stance.

## Endnotes

<sup>1</sup> Bureau of Economic Analysis

<sup>2</sup> *ibid*

<sup>3</sup> Bureau of Economic Analysis and MIM

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