

# QUEST Economic Update | September 2023

Near-term economic growth forecasts higher; inflation worries resurfacing; additional rate hike likely later this year



Ernst & Young LLP's Quantitative Economics and Statistics (QUEST) group's Economic Update summarizes the latest US economic trends and significant global developments.

Current as of 9/26/2023

Forecasts for near-term economic growth have risen, along with renewed concerns over inflation. Nevertheless, forecasts generally expect a significant economic slowdown and loosening of labor markets, albeit without an economic contraction.

US economic growth may have accelerated in the third quarter following solid 2.0% and 2.1% increases in real GDP (annualized), respectively, in the first and second quarters. The Atlanta Fed's GDPNow forecast expects the US economy to expand by 4.9% in the third quarter. The Federal Reserve September economic projections broadly signaled a stronger economy in both 2023 and 2024 as compared to its June projections.

Overall inflation as measured by the Consumer Price Index has ticked up over the past three months. Labor markets remain tight. Although the August unemployment rate increased to 3.8% from 3.5% in July, it remains near historic lows and well below the roughly 4.5% rate most economists view as consistent with full employment. Job gains have slowed in recent months, but weekly unemployment claims remain below pre-pandemic levels. Job openings have fallen from their highs in early 2022 but remain well above unemployment.

Notwithstanding the economy's resilience, most economic forecasts see economic growth weakening significantly over the next several quarters with possible recession-like conditions. Many forecasts see the unemployment rate rising to 4.5% to 5.0% in 2024, but without an economic contraction – a soft landing. While the Federal Reserve left interest rates unchanged at their September 19-20 meeting as they continue to assess how the fastest increase in interest rates since the early 1980s impacts the economy, they indicated there may be one additional rate increase later this year. Market expectations are for rates to remain constant through mid-2024 and then begin to decline.

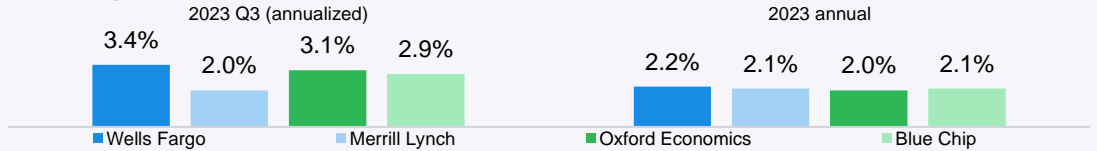
## OVERALL US ECONOMY

The economic picture appears to have improved with the Federal Reserve lifting its projections for GDP growth to 2.1% for 2023 and 1.5% for 2024. While many forecasts see economic growth slowing in 2024, the consensus is for a soft landing rather than an economic contraction.

### US GDP growth forecast

**Roughly 2.9%** growth expected for 2023 Q3 (annualized)

**Roughly 2.1%** growth expected for 2023



## LABOR MARKETS

Labor markets remain tight. The August unemployment rate was 3.8%, above the 3.5% rate in July, but still at a historically low level. Job gains have slowed, but unemployment claims remain below pre-pandemic levels.

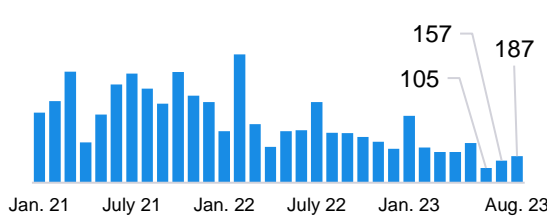
**606k** job gain on average in 2021

**399k** job gain on average in 2022

**236k** job gain on average in 2023

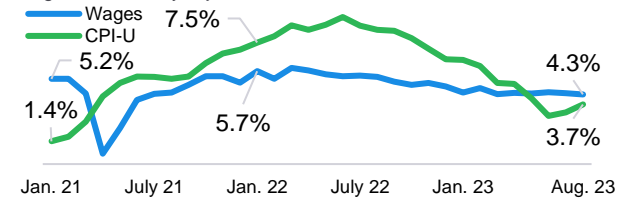
### Nonfarm payroll employment

Month-over-month change (in thousands), seasonally adjusted



### Hourly wages and CPI-U

Change from a year earlier, CPI - not seasonally adjusted, Wages - seasonally adjusted

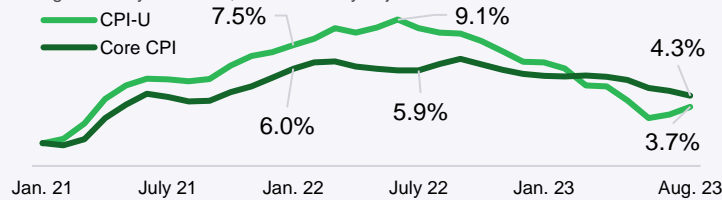


## INFLATION / INTEREST RATES

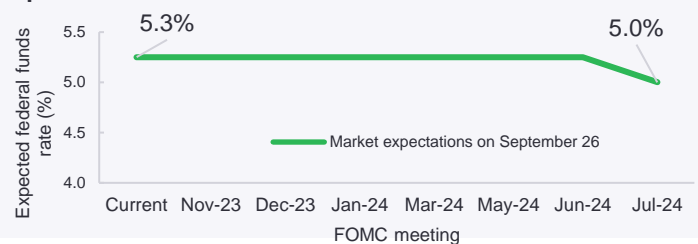
Overall inflation as measured by the CPI has increased for the past three consecutive months rising by 3.7% in August, 3.2% in July and 3.0% in June. The strong economy and renewal of inflationary pressures caused the Federal Reserve to indicate at its September 19-20 meeting that it would likely raise rates one additional time this year.

### CPI-U and core CPI

Change from a year earlier, not seasonally adjusted



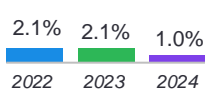
### Expected federal funds rate over 2023 and 2024



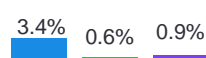
## GLOBAL GROWTH

Forecasts, while generally still suggesting slowing global economic growth in 2023, have improved over the past few months. China's economy is facing renewed challenges seen by slowing growth and high debt in its real estate sector.

### United States



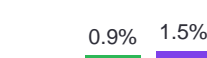
### Euro Area



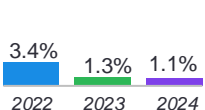
### China



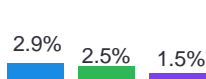
### Russia



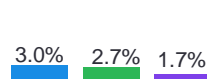
### Canada



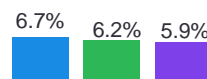
### Brazil



### Mexico



### India



## Upcoming economic data releases

- ▶ GDP for the Q2 of 2023 (third estimate), September 28
- ▶ Job openings for August, October 3
- ▶ Employment situation for September, October 6
- ▶ Consumer Price Index for September, October 12
- ▶ Housing starts for September, October 18
- ▶ Interest rates, Federal Open Markets Committee (FOMC) meeting, October 31 – November 1
- ▶ Productivity for Q3, November 2

## Overall US economy

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The US economy was on solid footing during the first half of 2023 and economic growth may have accelerated during the third quarter. The Federal Reserve Bank of Atlanta's GDPNow forecast projects real annualized GDP growth of 4.9% for the third quarter (as of September 19). GDP grew at 2.0% during the first quarter and 2.1% during the second quarter. Other signs of resilience include a historically low unemployment rate, low weekly unemployment claims, and the fifth straight month of higher retail sales.

The strength of the US economy appears to be driving an uptick, and possibly resurgence, of inflation. The overall CPI has increased for the past three months. The Federal Reserve recently released an update to its June economic projections that broadly signaled a stronger economy in both 2023 and 2024 (i.e., higher real GDP growth and a lower unemployment rate). Its projections for inflation were only slightly changed in 2023 and 2024. The Federal Reserve's dot plot suggested one additional 25-basis point rate increase in 2023 and a slower reduction in rates going forward. The updated projections are consistent

## Labor market

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US labor markets remain tight. The August unemployment rate rose to 3.8% from 3.5% in July, but remains close to historic lows well below the roughly 4.5% rate at which the economy's resources are fully employed.

The economy added 187,000 jobs in August, up from the 157,000 gains in July. Job gains averaged 257,000 over the first six months of 2023 and 399,000 during 2022. Weekly UI claims remain below pre-pandemic levels. Job openings have been generally falling since their high in early 2022 but remain well above unemployment.

The labor force participation rate rose to 62.8% in August after remaining

## Inflation

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Inflationary pressures appear to be resurfacing with some measures increasing or others signaling a continuation of elevated levels that could remain persistently higher than the Federal Reserve's 2% target. Higher inflation for longer may prompt additional rate hikes by the Federal Reserve.

The overall CPI rose by 3.7% (y/y) in August, following its 3.2% increase in July and 3.0% increase in June. The monthly August CPI rose 0.6%, following its 0.2% increase in July and June. The core CPI rose by 4.3% (y/y) in August, as compared to a 4.7% increase in July. The monthly core CPI rose by 0.3% in August, as compared to 0.2 in July. The recent rise in gas prices accounted for over half of the August increase in the overall CPI. Shelter prices have risen for 40 consecutive months. The Federal Reserve Bank of Cleveland's inflation nowcast forecasts the September CPI to increase by 3.7%.

## Global growth

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The global economy is expected to slow during the rest of 2023, with growth in the 1.5% to 2.5% range. Economic growth is expected to slow in the United States, the United Kingdom and the Eurozone. That said, recent forecasts are somewhat more optimistic than a few months ago, although recession or recession-like risks remain in the United States, United Kingdom and Eurozone.

with the "higher for longer" view that has been emerging in response to the strong US economy and uptick in some of the inflation numbers over the past several months.

There are, however, some signs of economic softness. Housing starts fell by 11.3% in August, likely in response to higher mortgage rates, and Conference Board's Consumer Confidence Index fell in August to 106.1 from 114.0 in July. In addition, the Conference Board's Leading Economic Index has fallen in every month since January. While economic growth is expected to slow in the coming quarters, the consensus forecast is for a soft landing.

at 62.6% for five consecutive months. The August underemployment rate, which averaged 8.7% from 2015 through 2019, rose to 7.1% from 6.7% in July. Average hourly earnings were up in August by 4.3% from a year ago, a pace above the rise in consumer prices, signifying an increase in real wages but possibly raising concerns about future inflation.

Despite the current tightness of the labor markets, many forecasters see the unemployment rate rising to the 4.5% to 5.0% range over the next year. Many economic forecasts suggest that the Federal Reserve's higher interest rates will begin to take hold and slow the economy in late 2023 and the beginning of 2024.

The personal consumption expenditure (PCE) price index, the preferred inflation measure of the Federal Reserve, increased by 0.2% in July, the same as in June, and by 3.3% over the past 12 months, up from the 3.0% increase reported in June. The core-PCE price index increased by 0.2% in July, the same as in June, and by 4.2% over the past 12 months, up from the 4.1% increase reported in June.

The strength of the US economy and resurfacing of inflationary pressures had the FOMC indicate one additional rate hike this year in its dot-plot release following its September 19-20 meeting. Market expectations are for rates to remain constant through mid-2024 and then begin to decline.

Although China showed significant strength coming out of its COVID lockdowns, its economy now appears to be experiencing headwinds due to difficulties in its real estate sector, high debt levels and weaker than expected consumer demand.

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ED None

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