US Daily: Updating Our Growth Impulses and GDP Forecast (Briggs)

- We see two main challenges to medium-term growth. First, fiscal support is set to step down significantly through the end of next year. Second, consumer services spending will need to recover quickly to offset a decline in goods spending as it normalizes from its current elevated level.
- After updating our estimates of the key growth impulses that drive our consumption forecast—reopening, fiscal stimulus, pent-up savings, and wealth effects—and incorporating a longer-lasting virus drag on virus-sensitive consumer services spending, we now expect a more delayed recovery in consumer spending. This pattern, combined with our expectation that semiconductor supply likely won't improve until 2022H1 and inventory restocking will therefore be delayed until next year, argues for a less front-loaded recovery from here than we had expected.
- We have therefore cut our growth forecast for 2021Q4 to 4.5% (vs. 5.0% previously) and revised our growth forecast for 2022Q1-Q4 to 4.5%/4%/3%/1.75% (vs. 5.0%/4.5%/3.5%/1.5%). These changes imply a downgrade to 2021 GDP growth to 5.6% on an annual basis (vs. 5.7%) and 5.2% on a Q4/Q4 basis (vs. 5.3%), and a downgrade in 2022 growth to 4.0% on an annual basis (vs. 4.4%) and 3.3% on a Q4/Q4 basis (vs. 3.6%). These changes are mostly offset by upgrades to our growth forecast in 2023 and 2024, however.
- Following Friday's employment situation report, we have left our unemployment rate forecast unchanged. We continue to expect that the unemployment rate will fall to 4.2% by end-2021 and 3.5% by end-2022.

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Updating Our Growth Impulses and GDP Forecast

We see two main challenges to medium-term growth. First, fiscal support is set to step down significantly through the end of the year. Although we maintain a positive outlook for household income because a recovering labor market and firm wage growth—particularly among low-wage workers—should keep income above its pre-pandemic trend through end-2022, the decline in transfer income will likely cause a pullback in spending for some households.

Second, consumers' service spending will need to recover quickly to offset a decline in goods spending as the latter normalizes from its current elevated level. This will likely prove challenging while COVID cases remain elevated, since many people still feel at least somewhat uncomfortable engaging in many activities that were routine prior to the pandemic (left chart, Exhibit 1). Furthermore, for activities like going to a movie theater, many individuals don't anticipate resuming normal spending patterns for at least another 6 months, suggesting a full normalization in economic activity may take some time (right chart, Exhibit 1).

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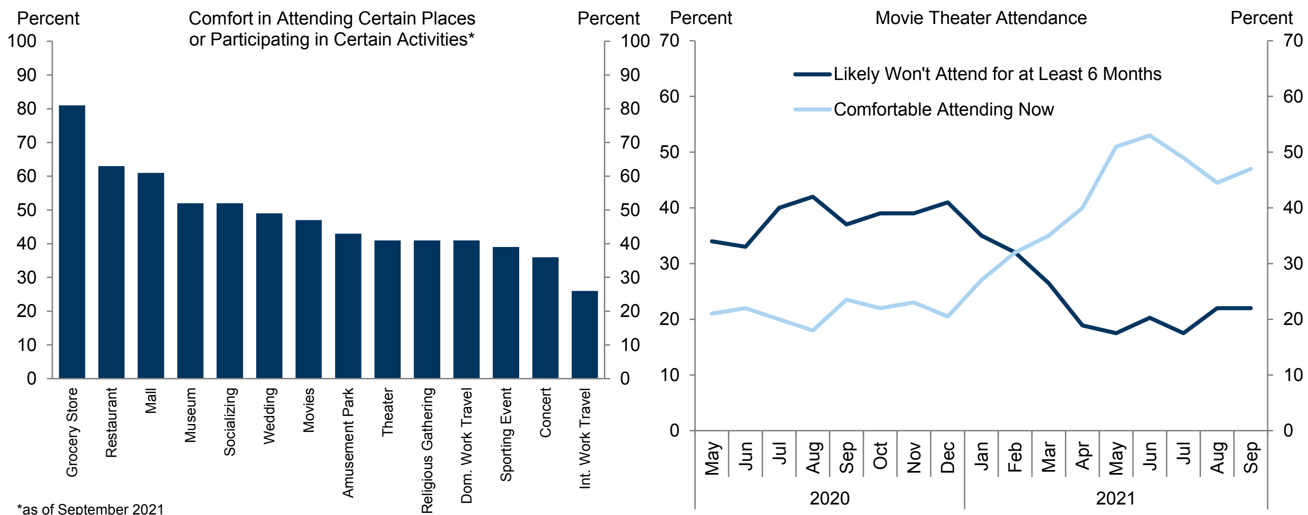
Exhibit 1: Many People Remain Uncomfortable Resuming Normal Service Spending



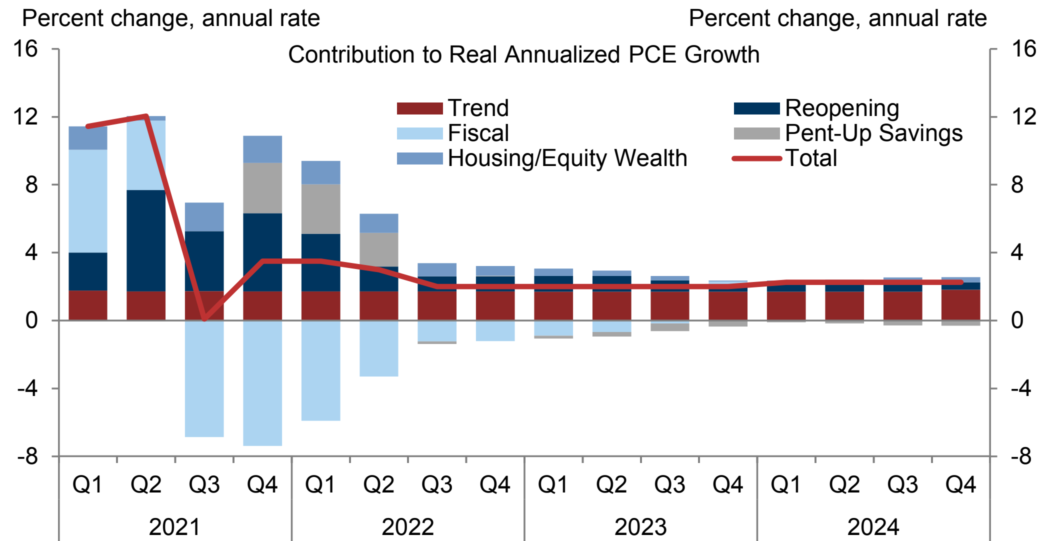
Source: Morning Consult, Goldman Sachs Global Investment Research

In addition to the near-term virus drag, we also expect that spending on some services and nondurables will remain persistently below its pre-pandemic trend, particularly if a shift to remote work results in some workers spending less overall. To estimate the impact on spending, we rely on a rich academic literature that finds spending declines by round 5% at retirement because workers stop paying for things like lunch and instead spend time preparing food at home.[1] Assuming a similar increase in home production from remote working, a 10pp increase in remote work, and a 60% employment-to-population ratio implies a permanent 0.3% reduction in overall PCE due to the shift to remote working.

[1] Mark Aguiar and Erik Hurst. "Consumption versus expenditure." Journal of Political Economy 113.5 (2005): 919-948.

In Exhibit 2 we use our prior methodology to decompose our consumption forecast across the various growth impulses—reopening, fiscal stimulus, pent-up savings, and wealth effects—that drive our outlook, as well as trend growth. We continue to expect that the fiscal impulse will remain very negative for the next several quarters as the spending contribution from pandemic-related fiscal transfer fades, but that other impulses will more than offset this drag.

Exhibit 2: PCE Growth Should Remain Positive Despite a Sizable Fiscal Drag



Source: Goldman Sachs Global Investment Research

In Exhibit 3 we estimate the overall impulse to GDP by adding up our consumption impulses, our forecast for international trade, and the GDP contributions from our revised forecast for inventory restocking, which now assumes that semiconductor supply will not improve until 2022H1 and inventory restocking will therefore be delayed. These estimates imply a moderate acceleration in growth in the near term, but a deceleration back to near trend by end-2022.

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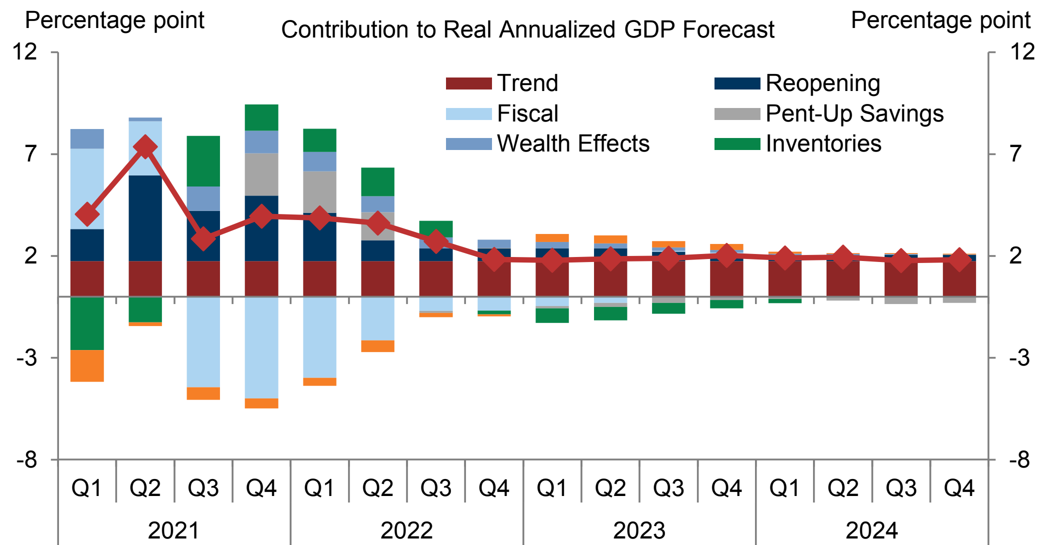
Exhibit 3: Our Growth Impulses Imply an Acceleration in the Near-Term, but a Deceleration by End-2022



Source: Goldman Sachs Global Investment Research

We are currently tracking 2021Q3 GDP growth at 3.25%, although inventories and foreign trade remain important sources of uncertainty. Based on our findings above, we have cut our growth forecast for 2021Q4 to 4.5% (vs. 5.0% previously) and revised our growth forecast for 2022Q1-Q4 to 4.5%/4%/3%/1.75% (vs. 5.0%/4.5%/3.5%/1.5%). These changes imply a downgrade in 2021 GDP growth to 5.6% on an annual basis (vs. 5.7%) and 5.2% on a Q4/Q4 basis (vs. 5.3%) and a downgrade in 2022 growth to 4.0% on an annual basis (vs. 4.4%) and 3.3% on a Q4/Q4 basis (vs. 3.6%). These changes are mostly offset by upgrades to our growth forecast in 2023 and 2024, however.

Following Friday's employment situation report, we have left our unemployment rate forecast unchanged, reflecting that the slower than expected recovery in employment has been thus far offset by a slower than expected recovery in labor force participation. We continue to expect that the unemployment rate will fall to 4.2% by end-2021 and 3.5% by end-2022.

Joseph Briggs

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We, Jan Hatzius, Alec Phillips, David Mericle, Spencer Hill, CFA, Joseph Briggs and Ronnie Walker, 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.

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