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The U.S. Economic Outlook for 2020–2022
Executive Summary: August 2020

Could Have Been Worse

The collapse of global GDP amidst the COVID-19 pandemic in the second quarter of 2020 was unprecedented. Yet, the pace of domestic contraction, 9.5 percent relative to the first quarter (32.9 percent pace at an annual rate), was far from the worst globally. The euro area economy shrunk by 12.1 percent relative to 2020Q1, including an 18.5 percent contraction in Spain. The United Kingdom fared even worse, contracting by 20.4 percent.

Consumption of services, which usually holds up during recessions, accounted for 22.9 percentage points of the 32.9 percent pace of domestic output contraction. The drop in consumer spending on healthcare alone lowered annualized GDP growth by about 10 percentage points. Apart from spending on gasoline, consumption of goods held up well, thanks to more than $500 billion in direct personal income support via stimulus checks and vastly expanded unemployment benefits. Business investment accounted for a further 9.4 percentage points of the contraction, with a large drag from inventory draws.

The Shortest Recession?

After losing an unprecedented 20.8 million jobs in April, total nonfarm payrolls have exceeded expectations, adding back 9.3 million jobs total over May, June, and July. Hiring in the leisure and hospitality sectors, which were amongst the hardest hit sectors in the spring, accounted for about one-third of the seasonally adjusted payroll employment gains in July.

The unemployment rate jumped to 14.7 percent in April but has since declined to 10.2 percent in July. Likewise, the index for industrial production bottomed in April, 16.5 percent lower than its February reading. By July, industrial output had regained half of those losses, registering an 8.2 percent decline relative to February.

The 1980 recession is currently the shortest on record, at six months. Should our forecast of continued expansion hold up, the 2020 recession will set a new record.

High Impact, High Uncertainty Assumptions

The course of the pandemic, public policy responses, and people's attitudes toward both are all of first-order importance for this forecast. We must make strong assumptions to produce our forecast, but our confidence in them is not very high.

It appears that getting COVID-19 triggers a lasting immune system response that is very likely to reduce the severity and infectiousness to others upon a potential reinfection. Hence, we expect the pandemic to end once enough people acquire a significant immune response either through infection or an effective vaccine.

In areas with over 20 percent blood antibody prevalence and only moderate restrictions on behavior, we observe a lack of case resurgence. Based on national case dynamics, we think the U.S. may be halfway through the acute phase of the pandemic, after which more modest restrictions would likely be sufficient to hold the spread in check. Until then, new local infection spikes are possible. Still, we expect mitigation policies to remain moderate, which by this stage of the pandemic appears to be largely sufficient to keep the healthcare load manageable.

The vaccine pipeline looks promising. We hope for a wide distribution of a vaccine by mid-2021.

Is the Fed Done?

This spring, the Federal Reserve went big, cutting interest rates to zero, dramatically increasing the size of its balance sheet, backstopping a broad range of markets, and even facilitating direct loans to small and medium-sized businesses and nonprofits. By now, however, it appears that we should not expect further unconventional policies. It seems that the Fed has cooled on the idea of yield curve control, and negative interest rates were never seriously considered. We expect that *the target range for the federal funds rate will remain unchanged in 2020–22, at 0 to 25 basis points. The forward policy guidance on when rates will lift off the floor is likely to be enhanced with outcome- and calendar-based triggers.*

Congress Running Low on Urgency

Within weeks of the COVID-19 pandemic hitting the United States, Congress acted decisively to mitigate the adverse effects of the crisis. Almost three months since the passage of the last bill, the urgency seems to have left Washington, DC, despite a clear need for additional support. Negotiations have stalled, with the parties at least a trillion dollars apart on the size of the next package. We nonetheless still expect a deal, along with a continuing resolution to fund the government. We believe Congress will send another round of stimulus checks and keep more than half of the expired $600-a-week boost to unemployment benefits in place through 2020.

The 2020–22 Outlook: Checkmark Recovery

Real GDP growth returns at a 20.9 percent annualized rate in 2020Q3 as consumer spending begins to recover. After the initial reopening, growth moderates to 8.2 percent in 2020Q4, resulting in an annual GDP decline of 4.9 percent. About 58 percent of the output loss in 2020H1 is recovered by 2020Q4, but it takes until mid-2022 to reach the pre-pandemic output level.

As the mortgage forbearance and moratoria on foreclosures and evictions expire while unemployment remains elevated, we expect the housing market to sour in 2021, despite low mortgage rates. A full housing recovery is delayed until 2022, when declining unemployment helps reinvigorate new home construction.

Light vehicle sales cratered during the spring but recovered to a 14.5-million-unit annual pace in July. However, very low inventories, domestic capacity constraints, and disrupted imports will likely limit a further rebound this year, with 2020 sales projected to total 13.8 million. Driven by rising light truck sales, total light vehicle sales recover to 15.0 and 16.1 million units in 2021 and 2022, respectively.

Low Inflation and Persistent Unemployment

The 2020 average payroll job count falls by 8.8 million, reflecting only a partial rebound after the March-April collapse that wiped out a total of 22.2 million jobs. In 2021, about 3.0 million payroll jobs come back, helped by restaurants and other hard-hit industries returning to normal operations. Job gains slow in 2022, adding 2.8 million jobs. Government employment loses 700,000 jobs in 2020 and continues to bleed employees in 2021–22, reflecting lingering fiscal stress. The unemployment rate peaked at 13.0 percent in 2020Q2, but quickly retreats to average 9.2 percent for 2020. It continues to inch down to average about 8 percent in 2021 and 7 percent in 2022.

While the pandemic has reduced both aggregate demand and aggregate supply, we think that the demand effects will dominate over the course of this forecast. The core CPI declined considerably this spring but recovered partially in recent months. For the year as a whole, we expect core CPI inflation to average 1.2 percent. It stays low in 2021, before rising to 1.7 percent in 2022. All-item CPI inflation falls more than the core this year and then recovers more vigorously, driven largely by movements in oil prices.

	Actual	**RSQE Forecast**		
	2019	2020	2021	2022
GDP (billions of current $)	21433.2	20547.3	21471.0	22326.6
Real GDP (billions of 2012 $)	19091.7	18165.5	18826.2	19286.5
% change: year-over-year	2.2	-4.9	3.6	2.4
% change: 4th-qtr-to-4th-qtr	2.3	-4.4	3.6	2.0
Nonfarm payroll employment (millions)	150.9	142.1	145.1	147.9
Civilian unemployment rate (%)	3.7	9.2	8.1	6.9
Capacity utilization, total industry (%)	77.8	71.5	75.7	78.3
Inflation (private nonfarm GDP deflator, % change)	1.8	0.8	0.8	1.5
Inflation (CPI-U, % change)	1.8	0.7	1.2	1.8
Inflation (core CPI, % change)	2.2	1.2	1.0	1.7
Light vehicle sales (millions)	17.0	13.8	15.0	16.1
Private housing starts (thousands)	1295.3	1180.8	1082.4	1195.8
3-month Treasury bill rate (%)	2.1	0.4	0.1	0.1
10-year Treasury note rate (%)	2.1	0.8	0.8	1.0
Conventional mortgage rate (%)	3.9	3.1	2.8	3.0
Real disposable income (billions of chained 2012 $)	14882.8	15916.9	15117.9	15333.6
% change	2.2	6.9	-5.0	1.4
Corporate profits after tax (billions of current $)	1938.6	1793.6	2023.5	2157.9
Value of U.S. $ (FRB broad index), % appreciation	4.6	2.9	-1.6	-0.1
Current account balance (NIPA basis, billions of current $)	-502.8	-477.5	-530.3	-635.0
Federal surplus (FY, NIPA basis, billions of current $)	-1023.3	-3317.8	-2285.9	-1563.6