The Recession Has Been Called Off, For Now

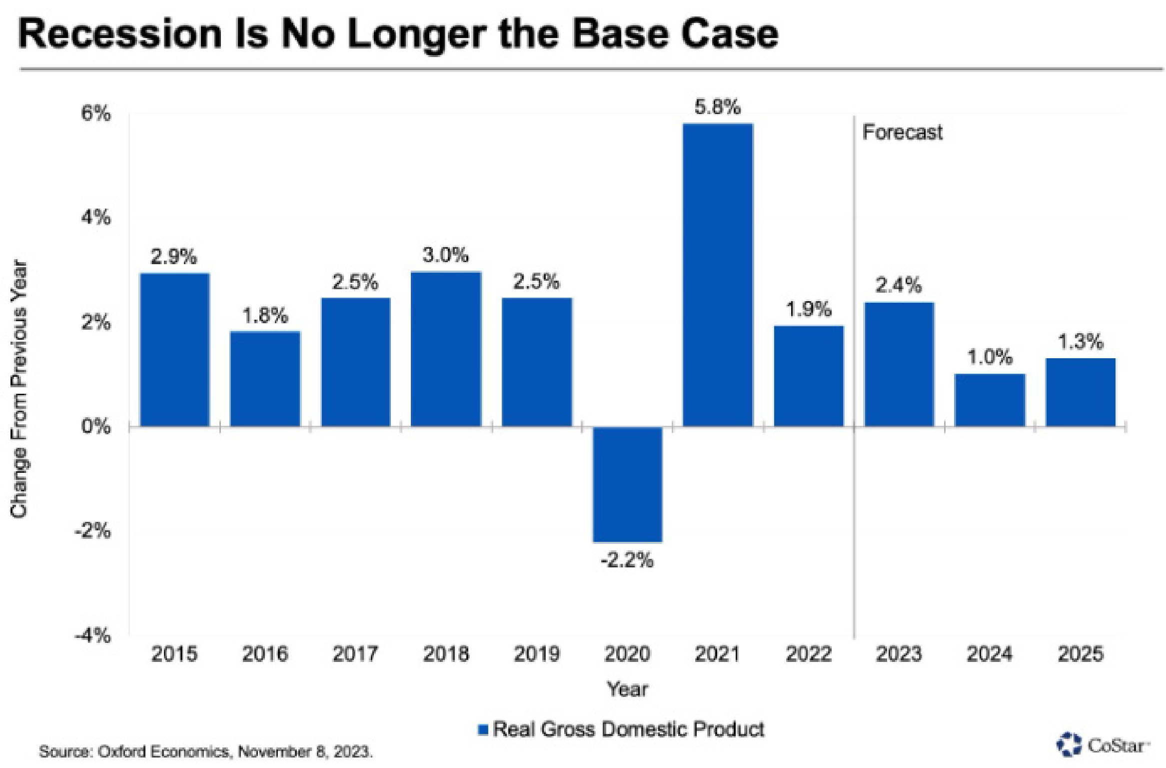
Economic Forecasts Turn Slightly Positive for 2024

By Christine Cooper and Rafael De Anda

While the commercial real estate sector encountered multiple headwinds in 2023, including a capital markets seizure and a drop in tenant demand, the U.S. economy has managed to avoid an outright recession.

Market watchers over the past year have pushed their negative forecasts further into the future, as consumer spending carried the economy quarter after quarter. Underlying data showed that much of the growth in spending was being fueled by a rundown of excess savings and by leaning on credit cards and personal loans, suggesting that a recession was more likely than not.

But heading into 2024, more economists are backing off their pessimistic forecasts and now see the Federal Reserve successfully steering the economy into a soft landing.



One of the most recent shops to change its tune was Oxford Economics (OE), which provides the macroeconomic assumptions that are used in the CoStar's commercial real estate property forecast models.

In its November forecast update, the firm notes it now expects the economy to "stagnate rather than contract" next year. Stagnation is a period of slow, below-trend economic growth and relatively high unemployment. In this scenario, real gross domestic product is projected to grow by 1% in 2024, with the first and second quarters seeing no growth at all. Job losses are mild, but the unemployment rate ends 2024 at 4.5%.

Several recent economic developments have helped move OE's forecasts into positive territory. For example, retail sales have continued to grow, albeit more slowly, and if the trajectory holds it would make a contraction in personal consumption expenditures (a key driver of economic growth) in the fourth quarter unlikely. The resumption of student loan payments and tax payments, paired with higher interest rates and slower income growth, have had a smaller impact on consumers than OE had predicted, although the firm still expects these factors to slow economic growth next year.

The term "rolling recession" has been bandied about to explain why some sectors of the economy are faring better than others, suggesting that those that are doing well, such as leisure and hospitality, are just at different stages of the business cycle than those that are faltering. For example, troubles in the real estate market have slowed construction activity in both residential and nonresidential structures, and factory activity has been in contraction for 13 consecutive months.

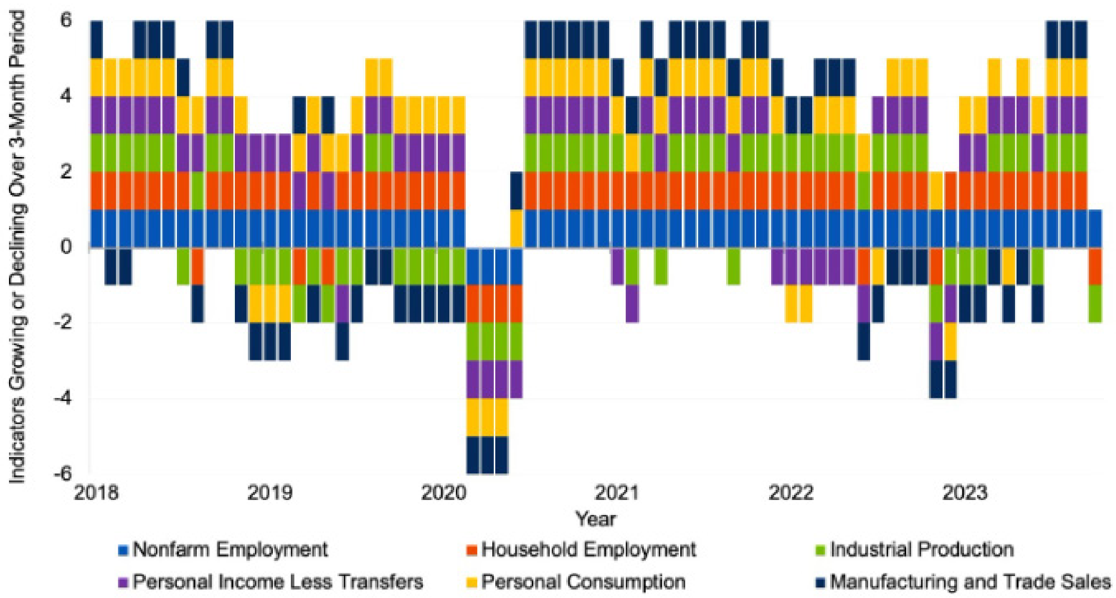
The National Bureau of Economic Research, the nation's foremost arbitrator of when the economy is in recession, follows six economic indicators that taken together encapsulate widespread economic activity rather than just considering a few sectors at a time. These indicators are personal income, personal spending, employment (by two measures), industrial production, and manufacturing and trade sales. No recession is in sight yet when collectively tracking these indicators, although two have contracted in October from three months earlier.

Of course, conditions can change quickly given the monetary tightening that has already occurred which may not have fully played out yet.

The labor market is coming off its frothy high, with the three-month average of job gains on a slowing trend for almost two years. Real disposable income fell in August and September, putting a risk to what has been robust household spending. And while significant progress has been made on the inflation front, core inflation as measured by the consumer price index, rose by 4% in October over the prior year, more than hoped for, which could push the Fed to boost its overnight lending rate yet again, further tightening credit conditions and weighing on business activity and investment.

One reliable recession indicator is the Conference Board's leading economic index, composed of 10 economic indicators. This index has been falling for 19 consecutive months, a sign difficult to ignore. In October, most of the components contributed negatively, including the ISM Index of new orders and the average consumer expectation for business conditions. Interest rate spreads also continue to show a contraction, as the spread between the 10-year Treasury and the 2-year bill has been negative since July 6, 2022.

All Six Recession Indicators Were Positive in September



Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve Board, Census Bureau, September and October, 2023.
Notes: Value of 1 represents growth over three-month period, value of -1 represents decline over three-month period. All monetary values are inflation adjusted.

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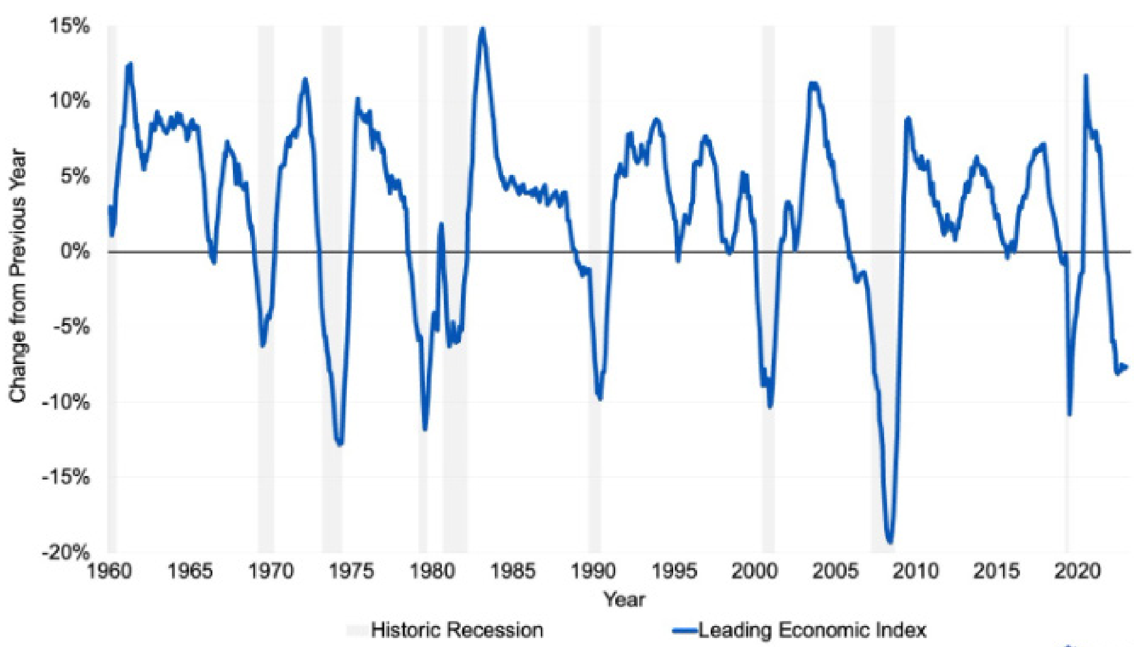
Leading Economic Indicators Are Falling



Source: Conference Board, October 2023

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