Indiana Economic Forecast Update

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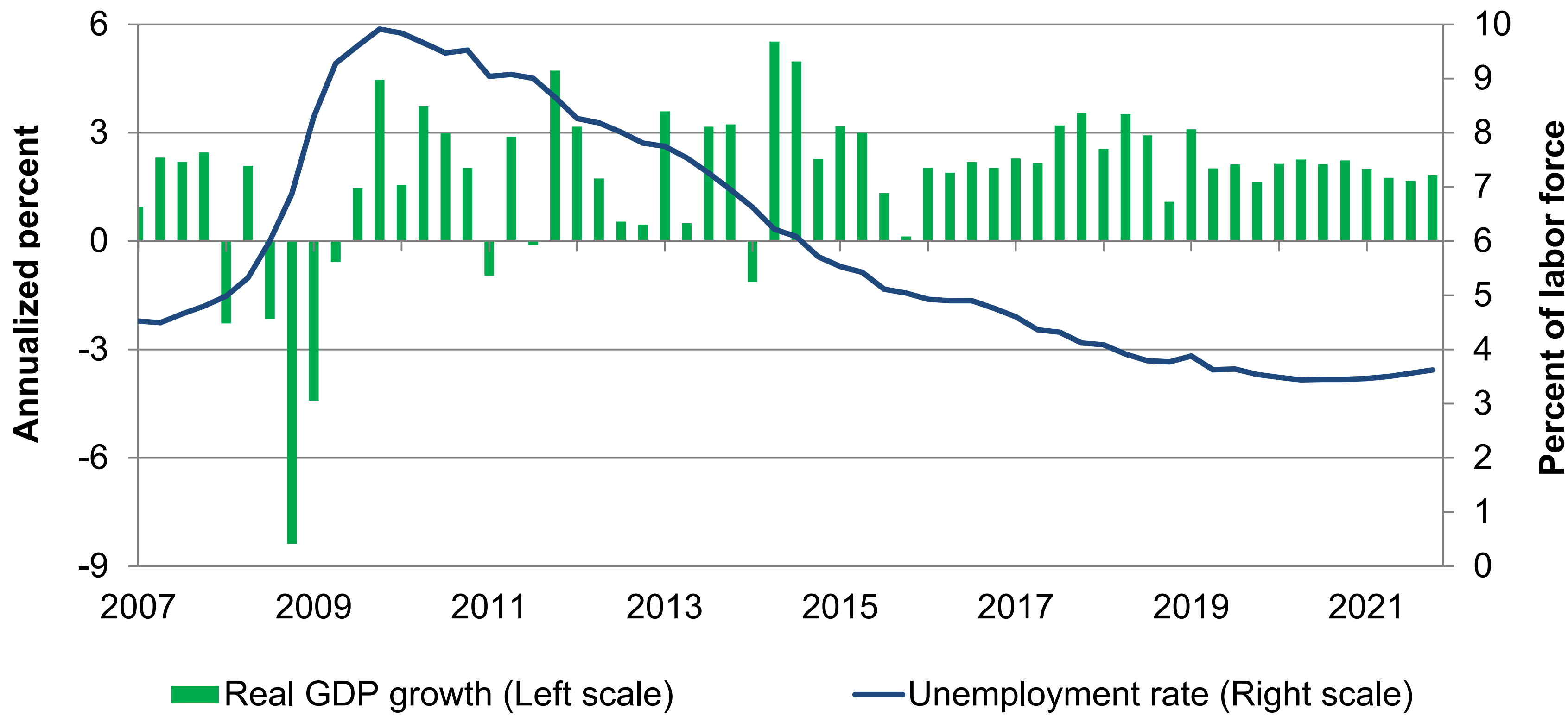
December 20, 2019

US economic growth settles near a 2% trend

- Real GDP grew at annual rates of 2.0% in the second quarter and 2.1% in the third quarter of 2019.
- Consumer spending is leading the US expansion, supported by solid gains in employment, real wages, and household wealth.
- Capital spending has decelerated in response to trade policy uncertainty, weak oil and gas prices, and the halt in deliveries of Boeing's 737 MAX aircraft.
- Diminishing fiscal stimulus, labor-supply constraints, a reversal of monetary easing, a deceleration in household wealth, and lagged effects of tariff increases will contribute to a slowdown in real GDP growth after 2020.
- Core inflation will rise slightly above 2% in response to pressures from import tariffs and a tight labor market.
- Growth in early 2020 will be boosted by special factors—a post-strike rebound in auto production at GM, a recovery in Boeing's production, and government spending for the decennial census.

The US economic expansion will continue, with the unemployment rate reaching a low of 3.4% in 2020

Real GDP and unemployment



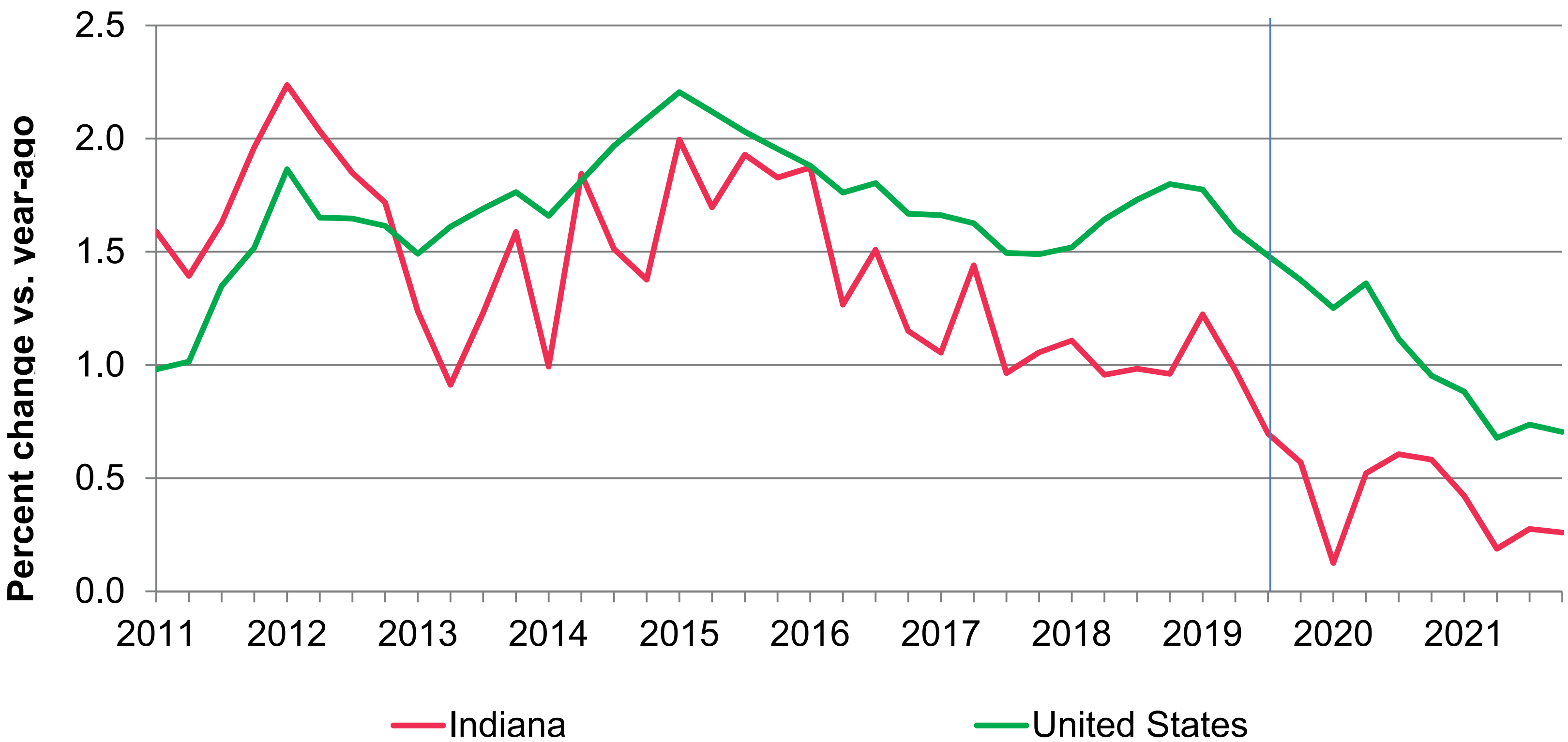
Source: IHS Markit

Changes to December forecast from April

- Recession risk is lower thanks to robust consumer spending, firmness in housing market, and signs of improvement in manufacturing
  - Risks from the global economy have at least moderated
- UAW/GM strike moves the needle on manufacturing activity, but overall impact muted
  - Six-week shutdown affected end of 2019Q3 and start of 2019Q4; GM expected to accelerate production in remainder of 2019 and early 2020 to rebuild inventories
  - Overall impact on economy low, but some suppliers and businesses near affected plants will find it difficult to recoup losses
- Indiana payroll employment lower than expected in 2019, largely in leisure and hospitality, retail, and transportation and warehousing
  - Weakness in leisure and hospitality/retail likely a function of low unemployment; may be offset by more hours worked for employees
  - Manufacturing employment a bit weaker, partly due to GM, but recovers in 2020
  - Transportation affected by slow growth in manufacturing, reduced foreign trade, lack of workers
- Outlook for housing starts somewhat brighter for the U.S. and Indiana
  - Federal Reserve interest rate cuts helped, along with solid income growth and demand from newer households

Employment growth will slow in the state and nationwide as we basically achieve full employment

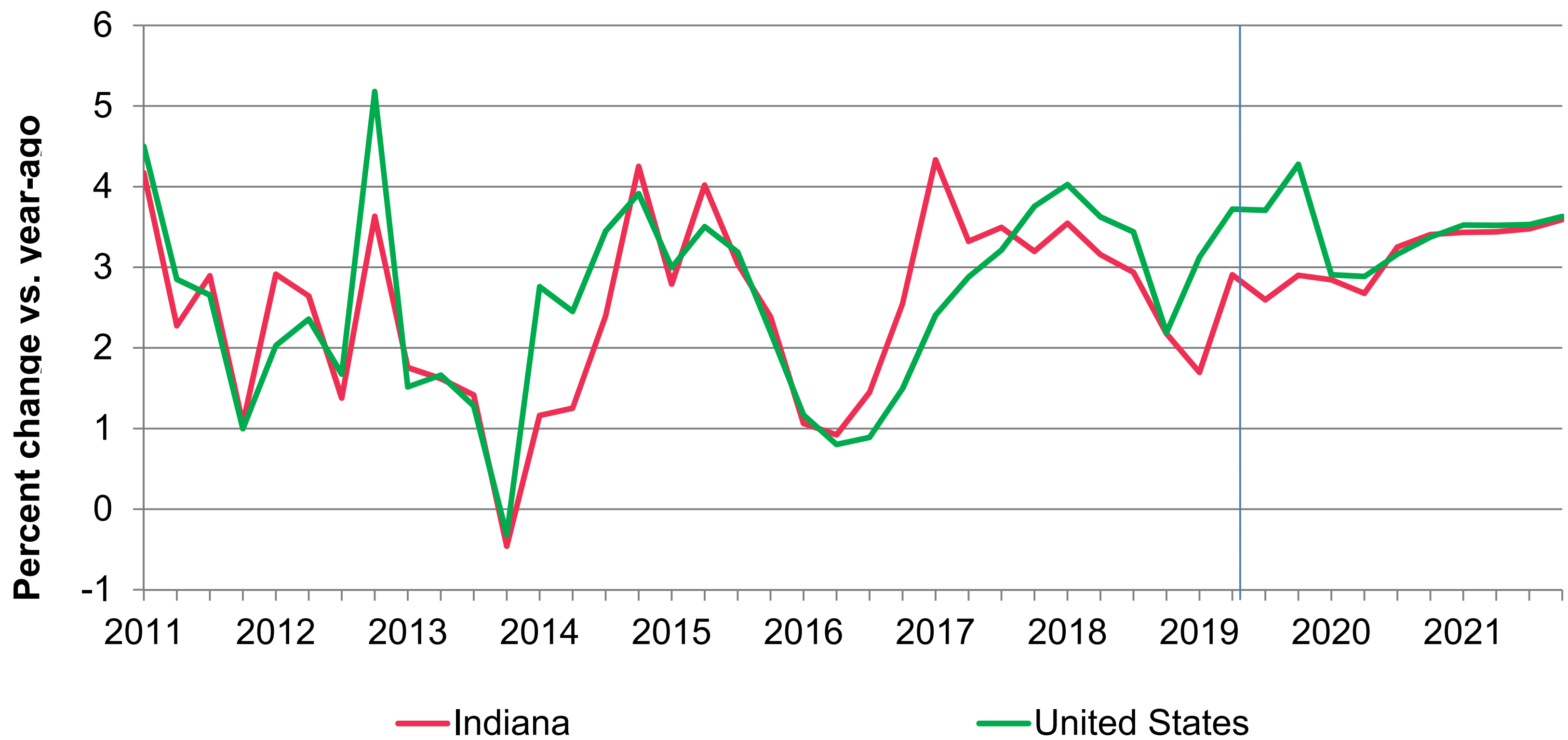
Indiana employment growth vs. United States



Source: IHS Markit

Higher productivity and employer competition for workers will bolster wage rates

Indiana wage growth vs. United States

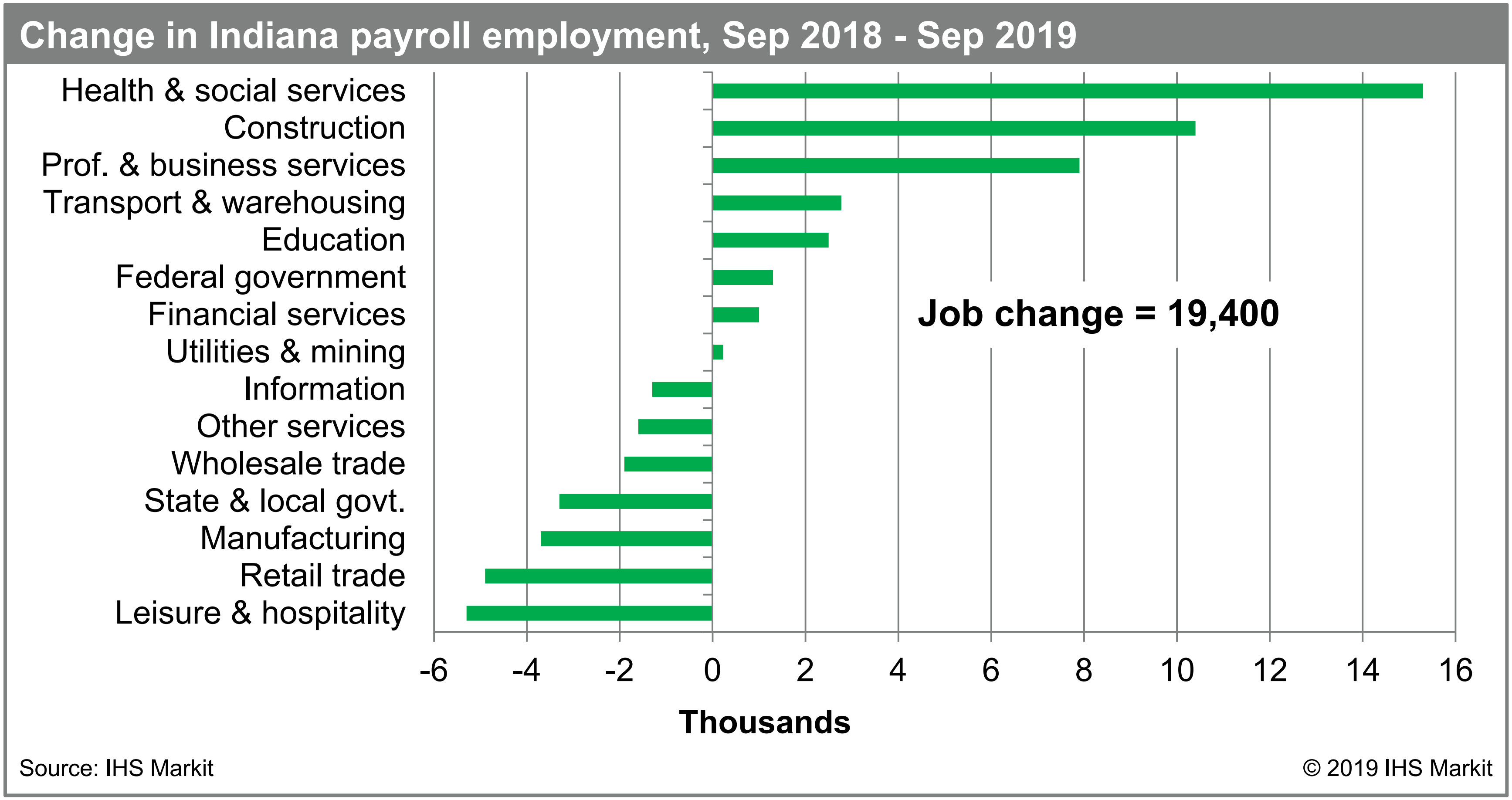


Source: IHS Markit

Key economic indicators for Indiana

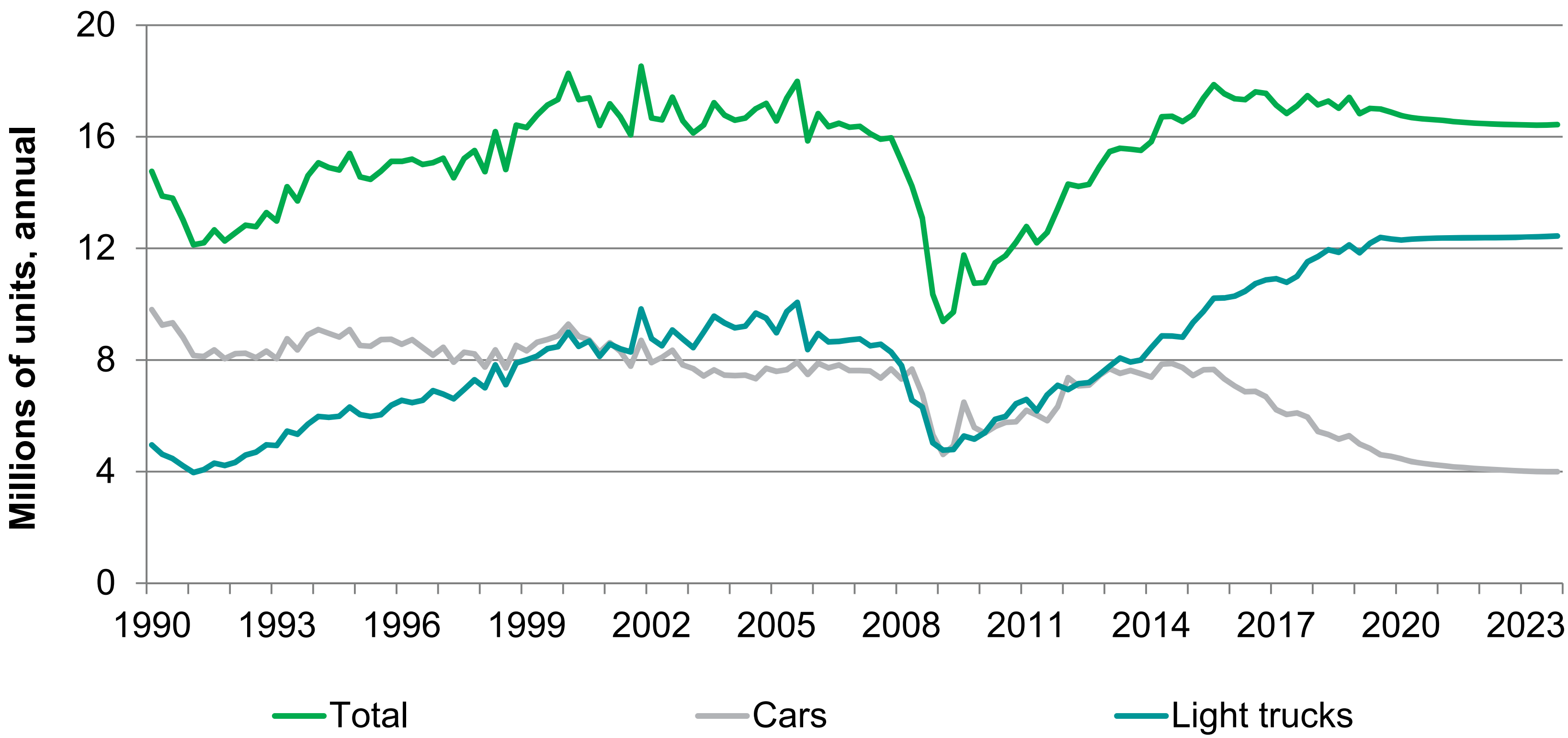
	2018	2019	2020	2021	2022
Units: Percent change					
Payroll employment	1.0	0.9	0.5	0.3	0.1
Unemployment rate (%)	3.4	3.4	3.1	3.2	3.4
Wage income	4.0	3.4	3.5	3.8	3.9
Personal income	4.8	3.8	3.4	3.8	4.0
Real gross state product	2.0	0.6	1.8	1.4	1.2
Personal consumption exp.	4.1	3.7	4.2	4.0	4.0
Housing starts (thousands)	20.6	20.4	21.8	21.2	20.6
Share of multi-family (%)	18.3	16.2	15.5	16.4	16.9

Health care, construction have added the most net new jobs over the past year



US light-vehicle sales have peaked; light trucks will continue to outsell cars

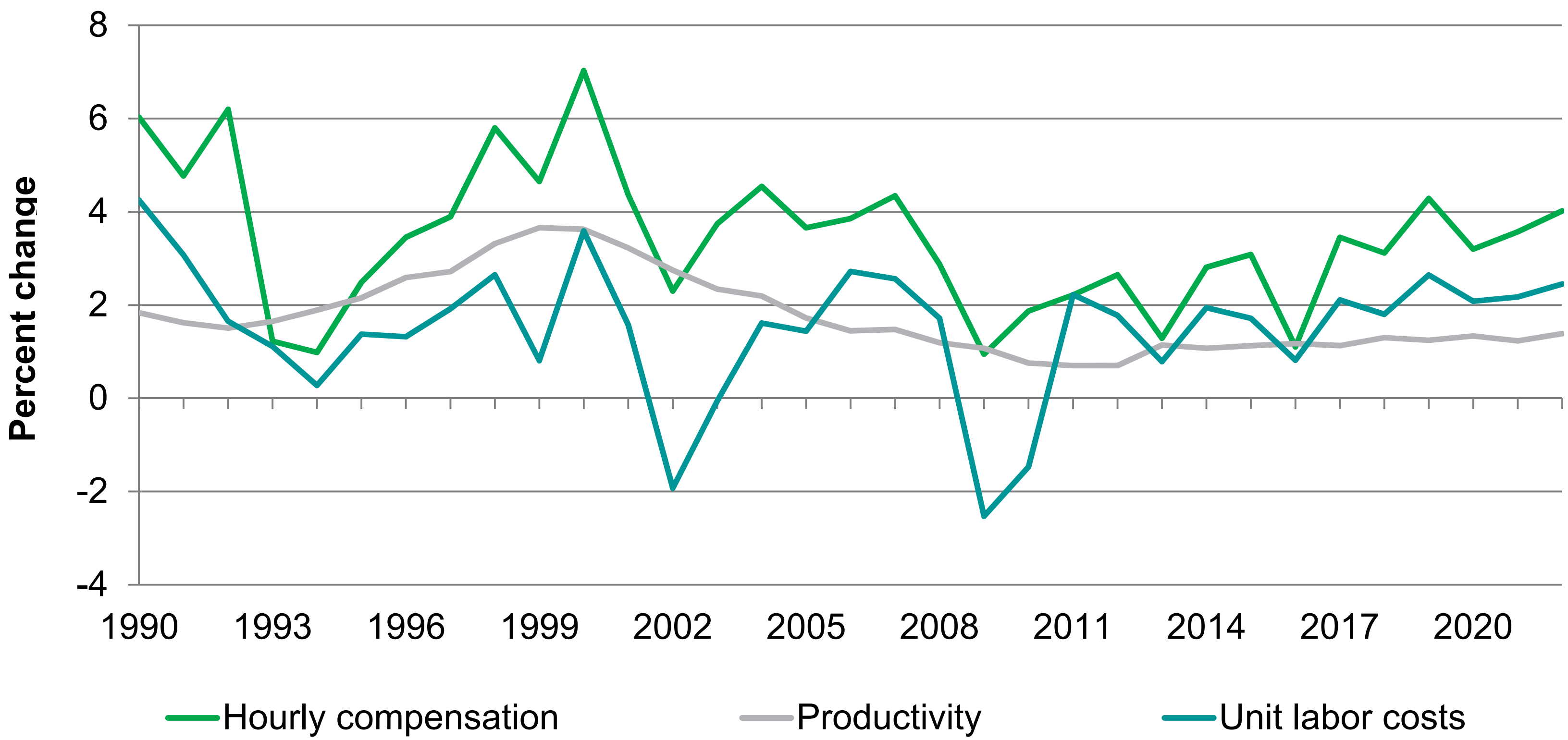
Light-vehicle sales



Source: IHS Markit

Gradual rise in productivity will provide support for higher wages

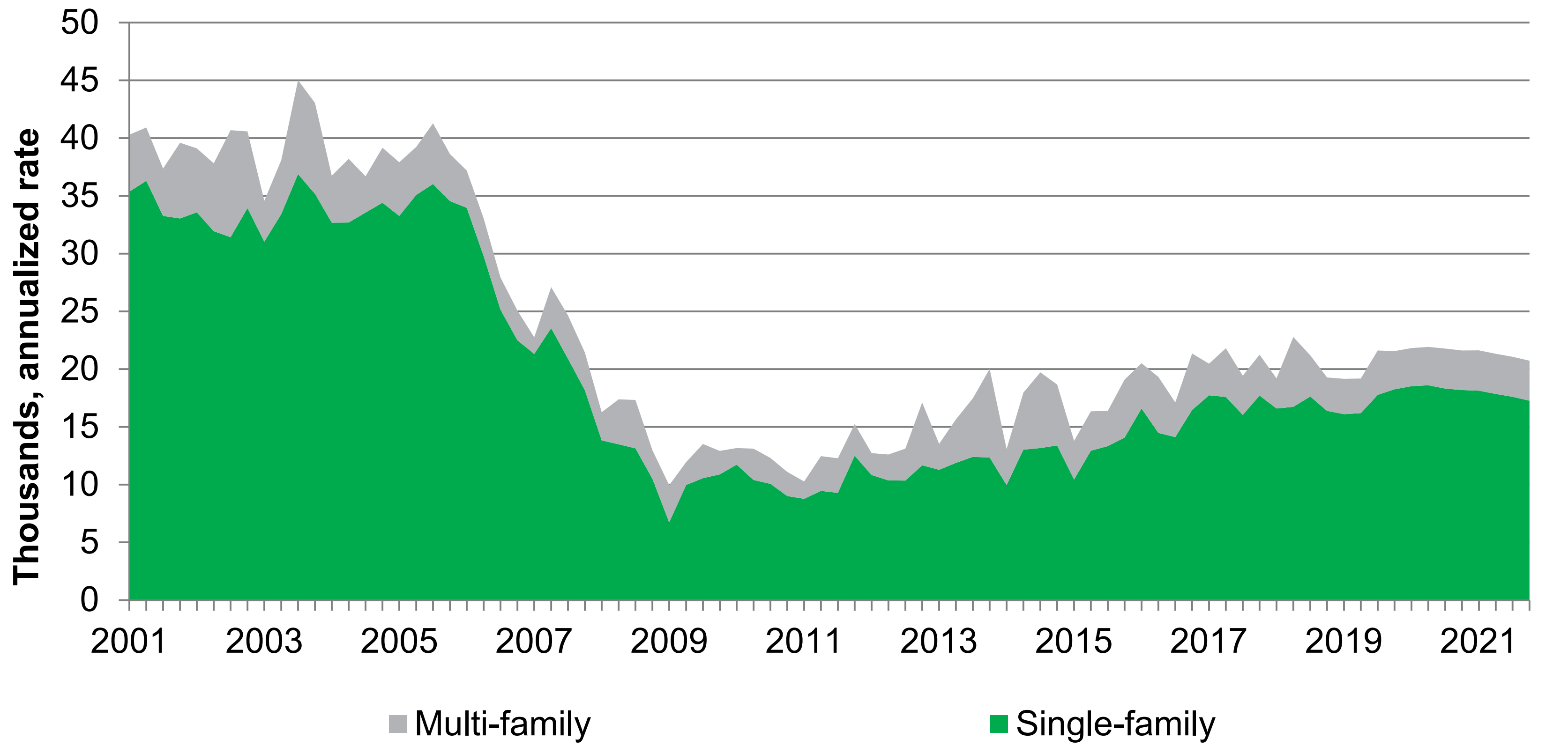
U.S. labor market indicators, private nonfarm sector



Source: IHS Markit

Lower interest rates sparked some gains in home building, but expectations remain rather modest

Indiana housing starts



Source: IHS Markit

Evolution of short-term Indiana forecast

	U.S. GDP		Indiana employment		Indiana income	
Forecast date	**2018**	**2019**	**2018**	**2019**	**2018**	**2019**
Dec 2017	2.6	2.3	1.2	1.0	4.2	4.8
Apr 2018	2.7	2.9	1.3	1.6	4.2	5.2
Dec 2018	2.9	2.6	0.9	1.2	4.3	4.5
Apr 2019	2.9	2.4	1.0	1.4	3.7	4.2
Dec 2019	2.9	2.3	1.0	0.9	4.8	3.8

Units: Percent change

Source: IHS Markit

Bottom line for Indiana

- Economic growth remains steady in Indiana, with many sectors chipping in
  - Solid income growth is supporting consumer spending, which is boosting most service sectors
  - Professional, scientific, and technical (including high-tech) businesses thriving in many areas
  - Health care services, including senior care, face increasing demand
- Growth in manufacturing employment will turn modestly negative over the next few years
  - Output growth slowing (but still positive); in some cases, this easing is occurring in industries that saw big increases in demand in recent years, such as semi trucks
  - Light trucks, SUVs should continue to sell briskly, thanks partly to steady fuel prices
- The outlook for homebuilding, a critical contributor to economic growth, is improving
  - Federal Reserve easing of interest rates a big factor
  - Housing affordability is a factor in economic competitiveness with other states
- Continued growth in the labor force, both in terms of quantity and quality, remains key to maintaining economic growth
  - Retention of “locals”, graduates of in-state universities, and immigration all have a role to play

US macro outlook – additional information

US economic growth by sector

Real GDP and its components

Percent change	2018	2019	2020	2021
Real GDP	2.9	2.3	2.1	2.0
Consumption	3.0	2.6	2.8	2.6
Residential investment	-1.5	-1.6	1.3	-1.0
Business fixed investment	6.4	2.2	1.7	3.2
Federal government	2.9	3.3	3.3	0.3
State & local government	1.0	1.6	1.1	1.2
Exports	3.0	-0.3	1.4	3.2
Imports	4.4	1.3	2.5	5.3

Source: IHS Markit

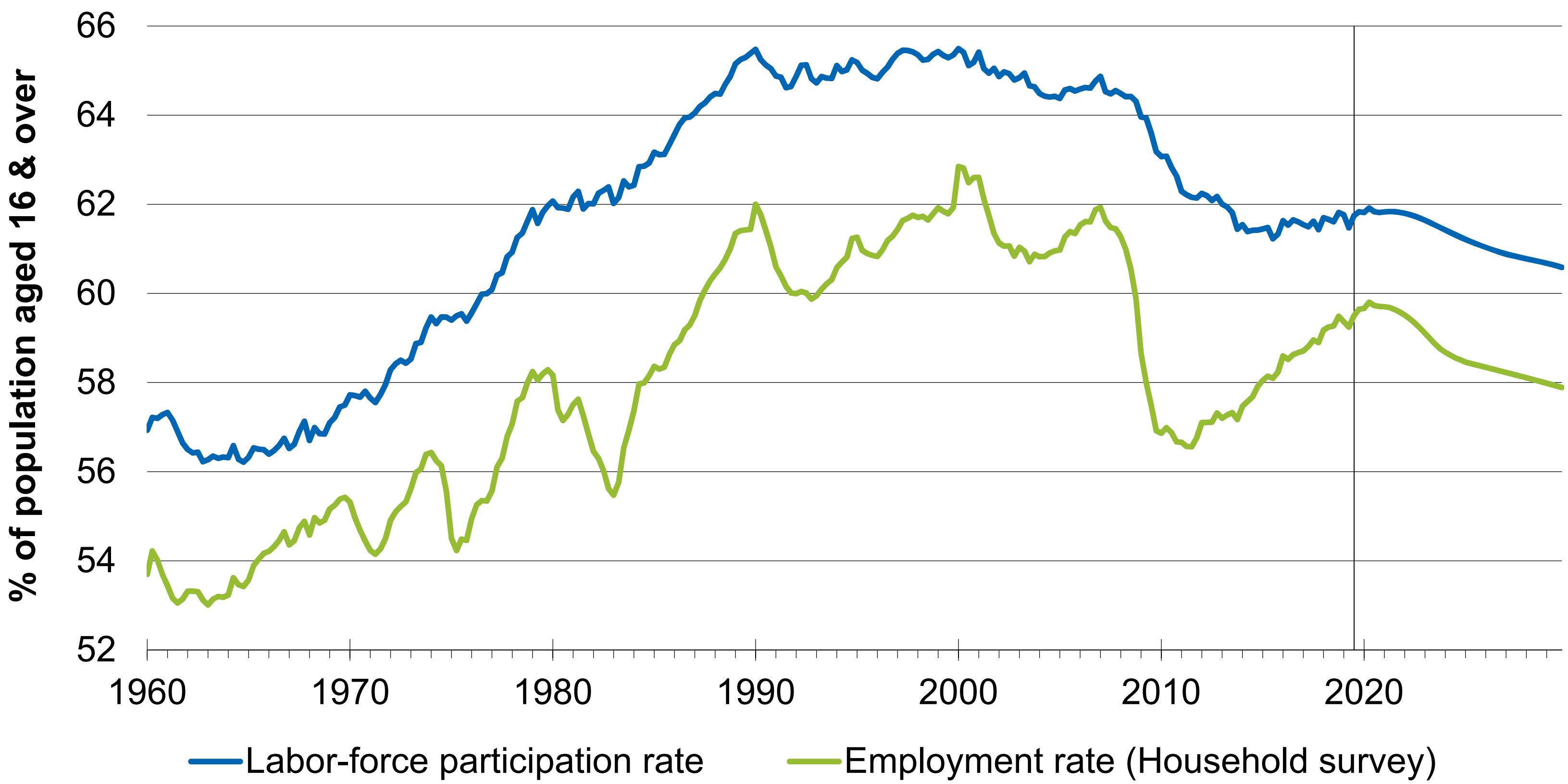
Other key US indicators

Key indicators				
Percent change	**2018**	**2019**	**2020**	**2021**
Industrial production	3.9	0.9	0.5	1.3
Payroll employment	1.7	1.6	1.2	0.8
Light-vehicle sales (Million units)	17.2	16.9	16.7	16.5
Housing starts (Million units)	1.25	1.26	1.29	1.28
Consumer Price Index	2.4	1.8	1.8	1.8
Core CPI	2.1	2.2	2.3	2.2
Brent crude oil price ($/barrel)	71	64	57	52
Federal funds rate (%)	1.8	2.2	1.6	2.0
10-year Treasury yield (%)	16.0	2.1	2.1	2.7

Source: IHS Markit

With baby boomers retiring, labor-force participation and employment rates will trend downward after 2020

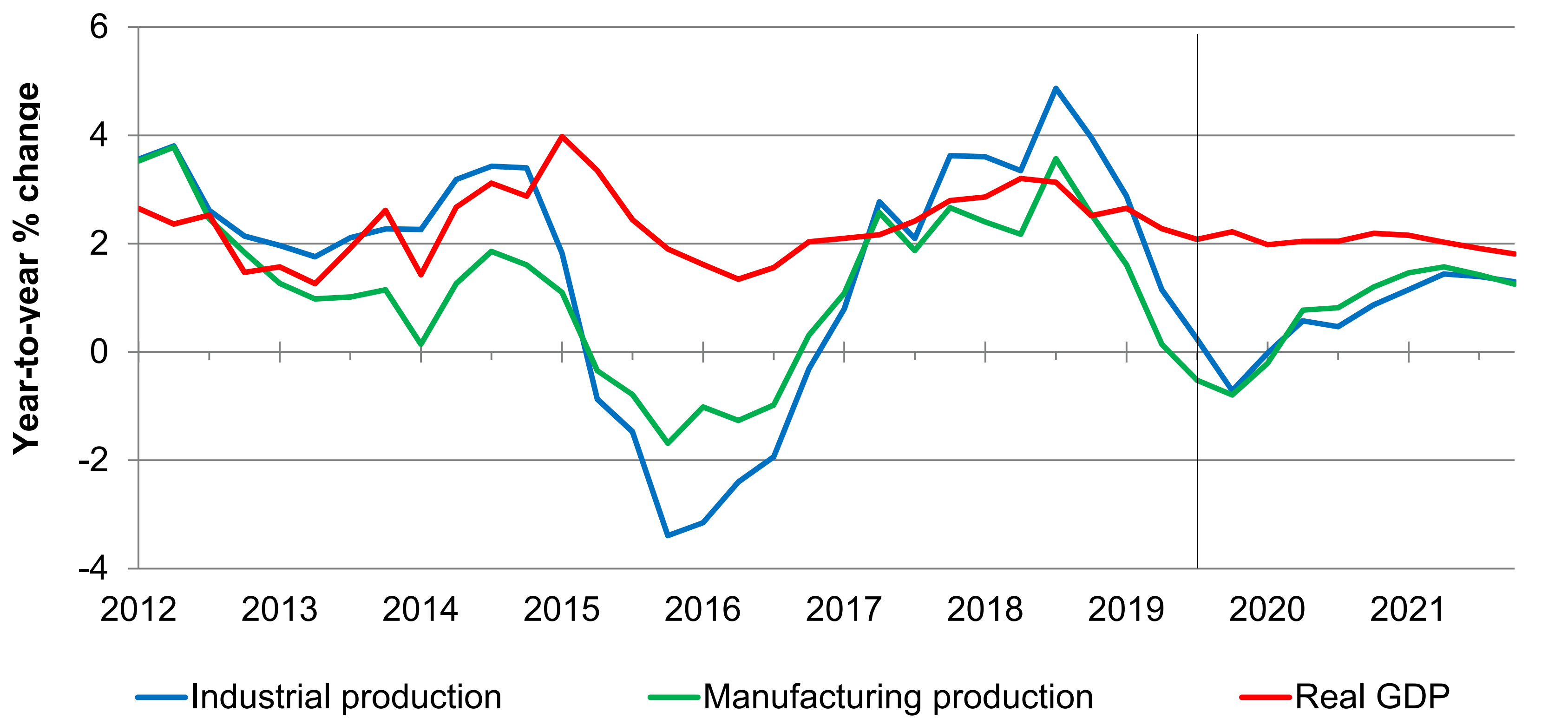
Labor-force participation and employment rates



Source: IHS Markit

US industrial production will rise after a mini-recession

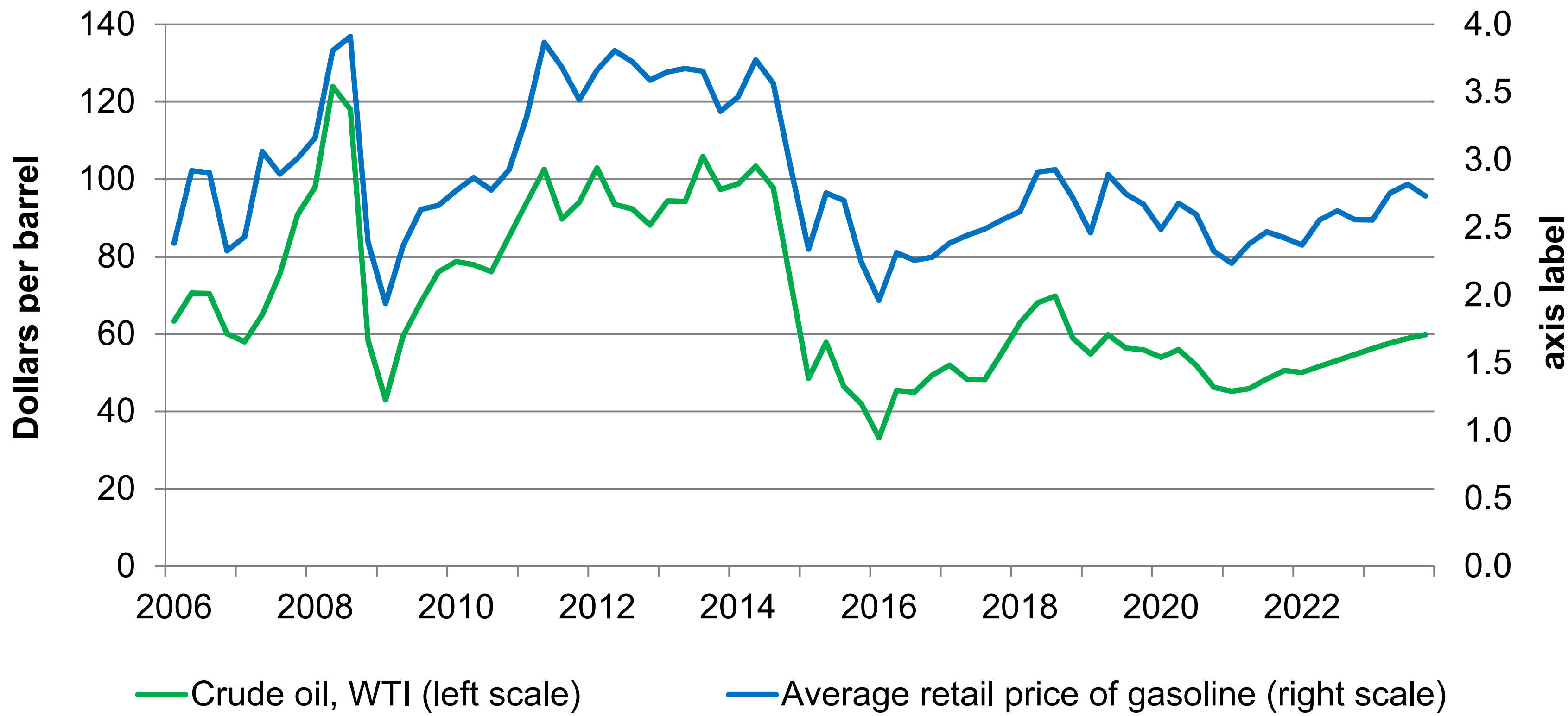
Industrial production and real GDP



Source: IHS Markit

Gasoline prices moving gradually higher – domestic production reduces risk of oil price surge

Crude oil and gasoline prices

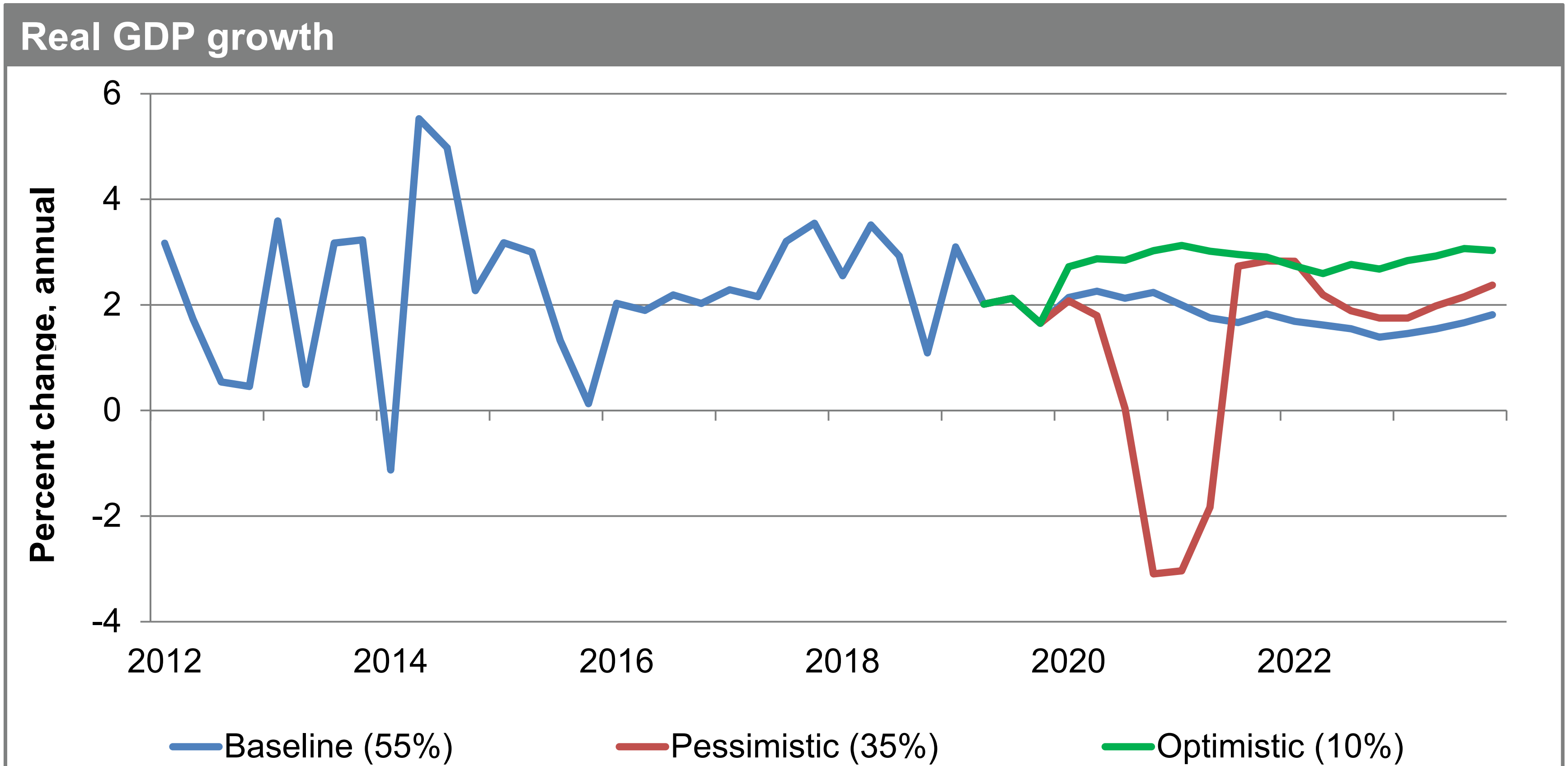


Source: IHS Markit

Risks to national forecast mostly on the downside

- Forecast risks are weighted more to the downside (35% vs. 10%)
  - > This is already the longest "recovery" on record
  - > Global economic growth slowing, especially in developed countries
  - > Policy uncertainty abounds, related to current and threatened tariffs, border closures, immigration policy, health care policy, Brexit impacts, etc.
  - > With Federal Reserve policy still accommodative and Federal budget deficit widening, not much room to respond to a downturn with added stimulus
  - > Low unemployment rates have not led to wage-fueled inflation, but still could
  - > Our current pessimistic scenario features a mild recession
- On the upside, possible surprises include:
  - > Higher productivity growth, perhaps spurred by investments in business equipment, would allow wages to rise without triggering consumer inflation
  - > Homebuilding could (finally) move higher in response to demand, aided by recent decline in mortgage interest rates and demand from millennials
  - > Global economic growth could be higher than expected, spurring export demand

Real GDP growth in alternative scenarios – downside scenario features mild recession late 2020 into 2021



Source: IHS Markit

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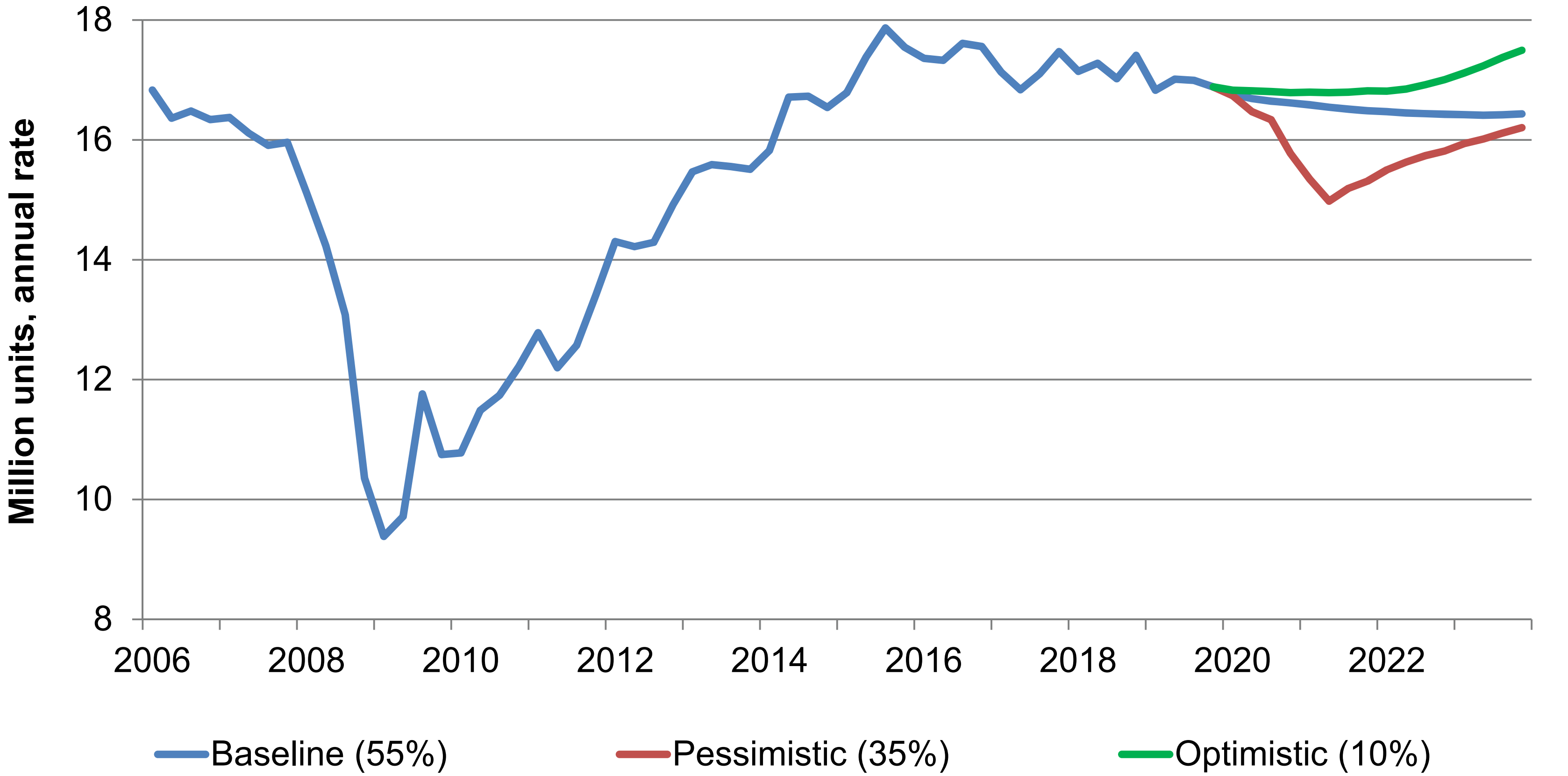
Light-vehicle sales in alternative scenarios

Light-vehicle sales



Source: IHS Markit

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