AgCountry Farm Credit Services
Q1 2022 ECONOMIC REVIEW
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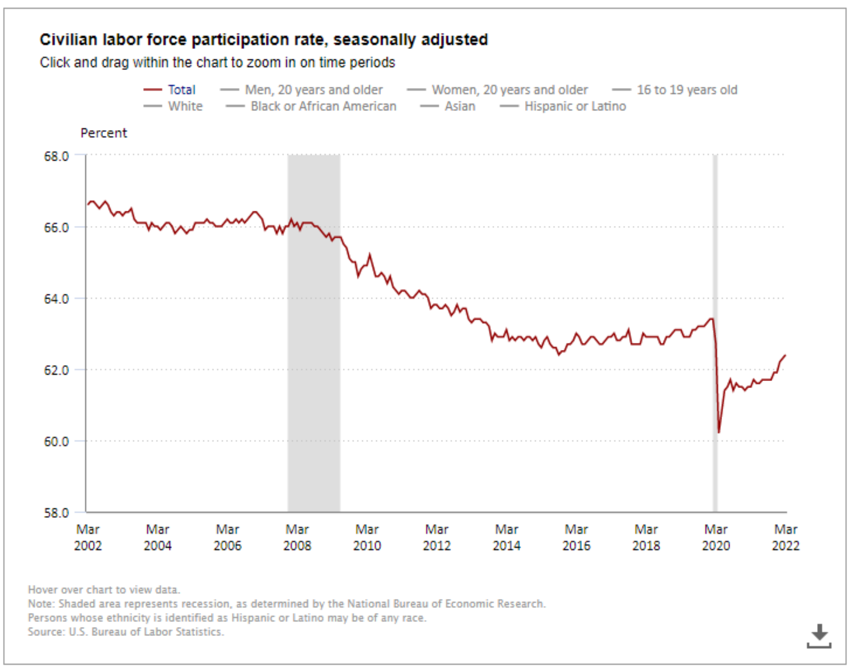
The nation's economic condition continued to improve during the first quarter of 2022, attributable to fiscal stimulus as well as continued positive economic activity. The number of administered vaccines has continued to increase with 77% of the US population having at least one dose and 65% fully vaccinated (CDC). Additionally, the Russian invasion into Ukraine has created uncertainty in the financial markets, supply chain concerns in a number of key industries and caused prices to spike for a number of commodities, including oil, natural gas and wheat creating a new set of economic concerns and inflationary pressure.

<u>Federal Reserve FOMC Statement March 16, 2022:</u>

"The invasion of Ukraine by Russia is causing tremendous human and economic hardship. The implications for the U.S. economy are highly uncertain, but in the near term the invasion and related events are likely to create additional upward pressure on inflation and weigh on economic activity."

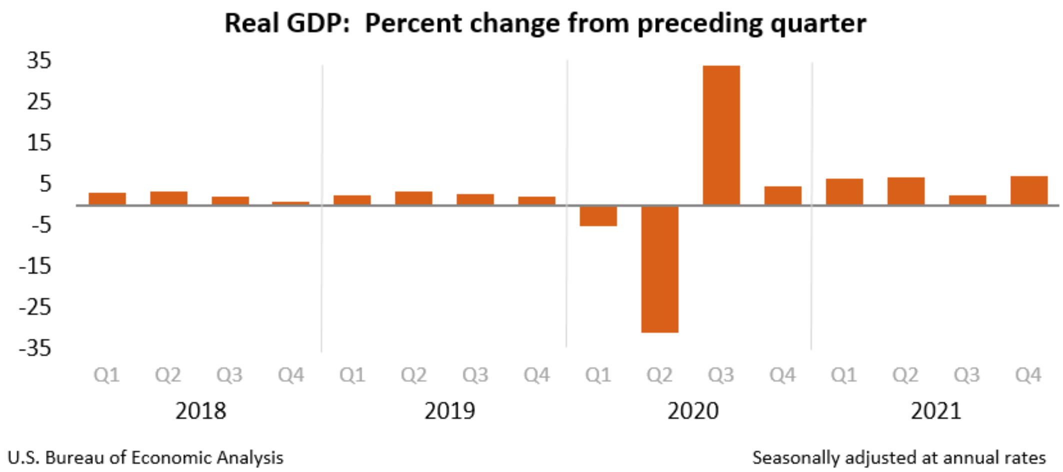
EMPLOYMENT:

Total nonfarm employment rose by 431,000 in March, the unemployment rate declined to 3.6%, and the number of unemployed decreased by 318,000 to 6.0 million. Prior to the COVID-19 pandemic (February 2020), the unemployment rate was 3.5%, and 5.7 million were unemployed. The labor force participation rate changed slightly to 62.4% in March but still remains lower than 63.4% witnessed in February 2020. Moody's anticipates that full employment, defined as 3.5% unemployment rate and 62.5% labor force participation rate, will be achieved in 2022.



GROSS DOMESTIC PRODUCT:

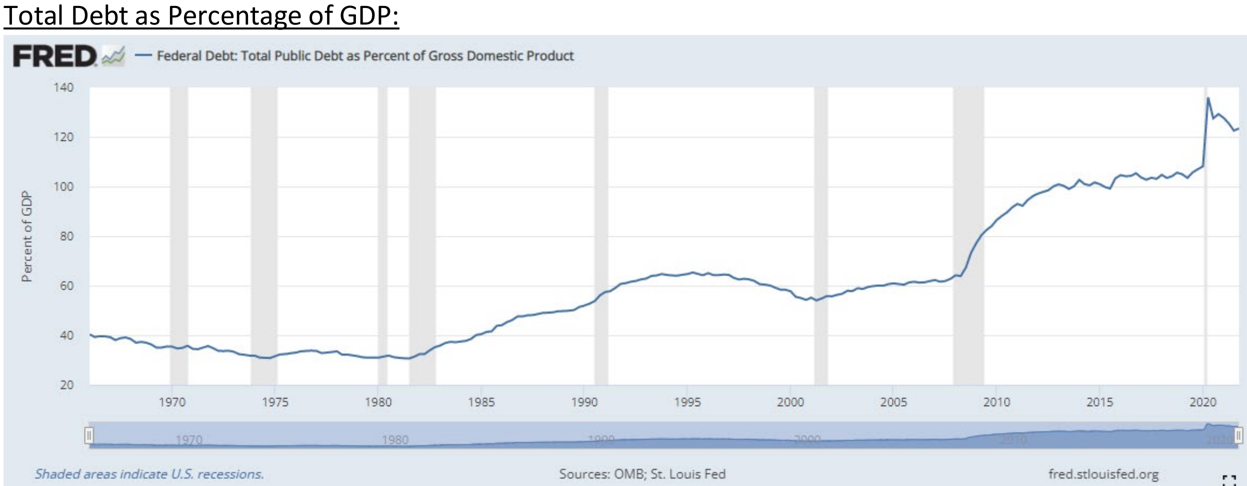
After the sharp decline in Gross Domestic Product (GDP) during the second quarter of 2020, GDP grew throughout 2021. The chart below displays the trend in quarterly GDP growth. GDP increased at an annual rate of 6.9% in the fourth quarter of 2021. Moody's March Baseline has 2022 GDP growth at 3.5%. Moody's also expects GDP growth of 3.1% in 2023 and 3.0% in 2024.



FISCAL POLICY:

Fiscal support since the beginning of the pandemic will ultimately total more than $5 trillion, equivalent to nearly 25% of 2019 GDP and approximately three times the support provided during the global financial crisis. The highly expansionary, deficit-financed discretionary fiscal policy will continue to provide a boost to the economy. Moody's expects lawmakers to pass $600 billion in legislation that the Biden administration has named "Building a Better America." The spending package would mostly center around $330 billion in clean-energy tax credits and $230 billion in federal spending to address climate change. The federal government is expected to post a deficit of over $3 trillion in 2021 and $2 trillion in fiscal 2022. The publicly traded Debt-to-GDP ratio is near 100% and will soon breach the all-time high of 106% reached briefly after World War II.

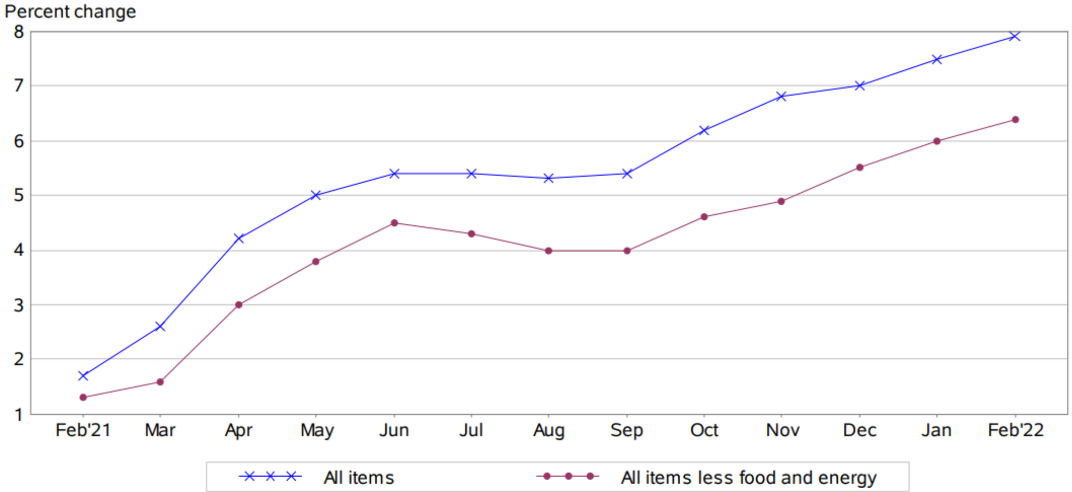
Total Debt as Percentage of GDP:

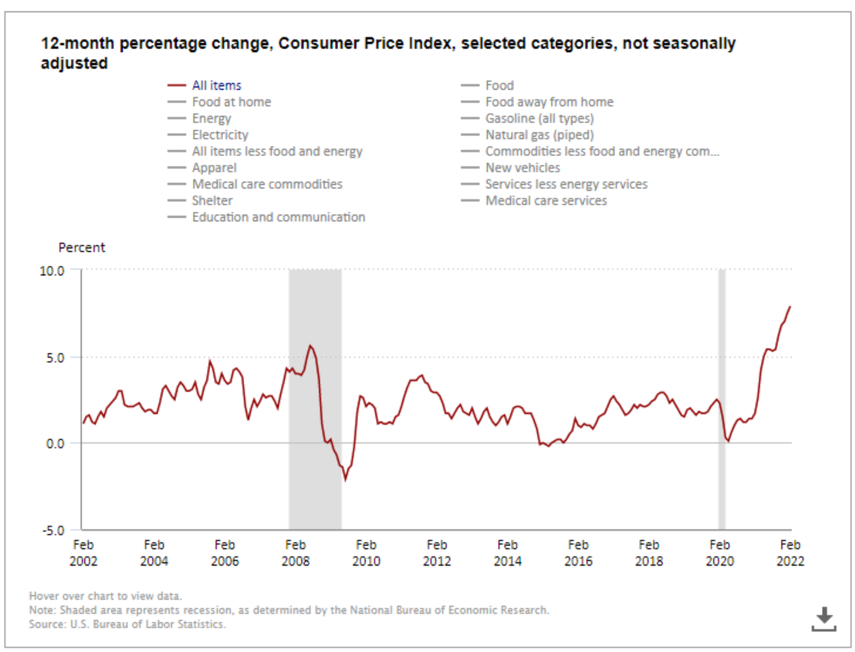


INFLATION:

Consumer prices have increased this year due to the fiscal stimulus resulting in higher personal spending. The all-items index rose 7.9% for the 12 months ending February 2022. Increases for gasoline, shelter and food were the largest contributors to the all-items index increase. The gasoline index increased 6.6% in February and accounted for nearly one-third of the index's increase that month. Moody's March 2022 Baseline forecasts CPI to be 6.9% in the first quarter of 2022 and to decline throughout the year ending at 5.8% for 2022.

Chart 2. 12-month percent change in CPI for All Urban Consumers (CPI-U), not seasonally adjusted, Feb. 2021 - Feb. 2022





The Federal Reserve has shifted its stance on inflation from transitory inflation caused by supply constraints to now both supply and demand imbalances created by the pandemic. Prior to the price increases during the fall of 2021 the FOMC members expected 2021 headline Consumer Price Index (CPI) to be below 4% however 2021 inflation came in higher than expected at 5.5%.

<u>Federal Reserve Chair Pro Tempore Powell Speech "Restoring Price Stability" March 21, 2022:</u>

"It continues to seem likely that hoped-for supply-side healing will come over time as the world ultimately settles into some new normal, but the timing and scope of that relief are highly uncertain. In the meantime, as we set policy, we will be looking to actual progress on these issues and not assuming significant near-term supply-side relief."

<u>MONETARY POLICY:</u>

The Federal Reserve has started normalizing monetary policy and has recently ended their quantitative easing program and began raising interest rates at its March Fed Open Market meeting by increasing the Fed Funds rate by 25 basis points. Moody's anticipates that the Federal Reserve will continue to raise the Federal Funds Rate with four 25 basis point hikes in 2022 and another four in 2023. It is expected that the federal funds rate reaches its long-run rate of 2.5% by the middle of 2024.

<u>Federal Funds Rate Probabilities:</u>

FedWatch Tool

Target Rate: Current | Compare | Probabilities
Historical: Historical | Downloads | Prior Hikes
Dot Plot: Chart | Table

FED FUND FUTURES

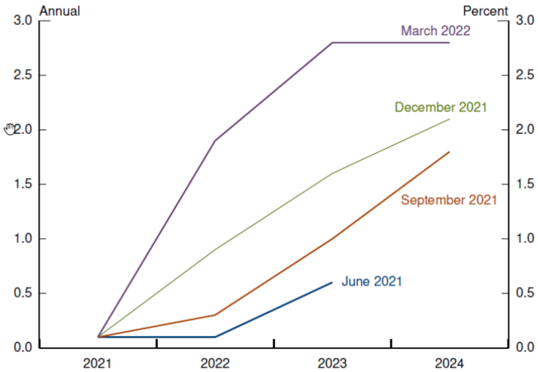
ZQJ2	ZQK2	ZQM2	ZQN2	ZQQ2	ZQU2	ZQV2	ZQX2	ZQZ2	ZQF3	ZQG3	ZQH3	ZQJ3
99.6588	99.2575	98.9775	98.7125	98.3625	98.2475	97.9925	97.7175	97.5725	97.4575	97.2700	97.1675	97.0650

MEETING PROBABILITIES

MEETING DATE	50-75	75-100	100-125	125-150	150-175	175-200	200-225	225-250	250-275	275-300	300-325	325-350	350-375	375-400	400-425	425-450
5/4/2022	22.3%	77.7%	0.0%	0.0%	0.0%											
6/15/2022	0.0%	0.0%	16.2%	62.7%	21.1%	0.0%	0.0%	0.0%	0.0%	0.0%						
7/27/2022	0.0%	0.0%	0.0%	5.4%	31.6%	48.9%	14.1%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	
9/21/2022	0.0%	0.0%	0.0%	0.0%	3.3%	21.6%	42.3%	27.3%	5.4%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%
11/2/2022	0.0%	0.0%	0.0%	0.0%	0.0%	2.9%	19.1%	39.5%	29.4%	8.4%	0.7%	0.0%	0.0%	0.0%	0.0%	0.0%
12/14/2022	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	2.6%	17.5%	37.5%	30.4%	10.4%	1.5%	0.1%	0.0%	0.0%	0.0%
2/1/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.6%	6.3%	22.5%	35.7%	25.4%	8.2%	1.1%	0.1%	0.0%	0.0%
3/15/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.1%	1.2%	7.8%	23.7%	34.8%	23.8%	7.5%	1.0%	0.0%	0.0%
5/3/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.6%	4.4%	15.6%	29.1%	29.4%	15.9%	4.4%	0.6%	0.0%
6/14/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.3%	2.7%	10.4%	22.9%	29.3%	22.1%	9.7%	2.3%	0.3%
7/26/2023	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%	0.3%	2.1%	8.6%	19.9%	27.8%	23.8%	12.6%	4.1%	0.8%

The chart above provides a complete view of the current market (Chicago Mercantile Exchange) probabilities across all scheduled FOMC meetings and possible Federal Funds rate outcomes. The chart below shows how members of the FOMC have changed their viewpoint Federal Funds Rate increases. As the economy continues to rebound and inflation concerns increase the committee has responded with a higher projected rate path. Investors are expecting the Fed to move more aggressively than Moody's was projecting in their early March Baseline given more recent economic news and concerns with the Russian Ukraine war.

Figure 5. FOMC participants project a higher federal funds rate path



Note: Figure reports the median expectation of FOMC participants for the federal funds rate at the end of the year indicated.
Source: Summary of Economic Projections, available on the Board's website at https://www.federalreserve.gov/monetarypolicy/fomccalendars.htm.

<u>FOMC March 16th Statement:</u>

"The Committee seeks to achieve maximum employment and inflation at the rate of 2 percent over the longer run. With appropriate firming in the stance of monetary policy, the Committee expects inflation to return to its 2 percent objective and the labor market to remain strong. In support of these goals, the Committee decided to raise the target range for the federal funds rate to 1/4 to 1/2 percent and anticipates that ongoing increases in the target range will be appropriate. In addition, the Committee expects to begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities at a coming meeting."

<u>US 10-Year Treasury Yield:</u>

- The closely watched 10-year treasury yield has increased to over 2% during the first quarter of 2022. The 10-year serves as a barometer for the economy and is watched closely by investors. Moody's expects the 10-year treasury yield to steadily increase over the next few years, reaching its estimated long-run equilibrium of 3.75% by mid-decade.

<u>CONCLUSION:</u>

The economy continues to rebound from the disruptions caused by the COVID-19 pandemic and is now faced with new inflation headwinds as well as disruption from the Russian/Ukraine conflict. The question is now that we are nearing full unemployment, and inflation is above previous expectations, how quickly will FOMC increase the Federal Funds Rate to keep inflation in check while still allowing the economy to grow?

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Economic Review

SOURCES:

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2. https://covid.cdc.gov/covid-data-tracker/#cases_totalcases
3. https://covid.cdc.gov/covid-data-tracker/#vaccinations_vacc-total-admin-rate-total
4. https://www.bls.gov/news.release/empsit.nr0.htm
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