Economy in Focus
May 26, 2021

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The Economic Outlook

Strong Economic Growth, Rising Inflation, and Supply Challenges

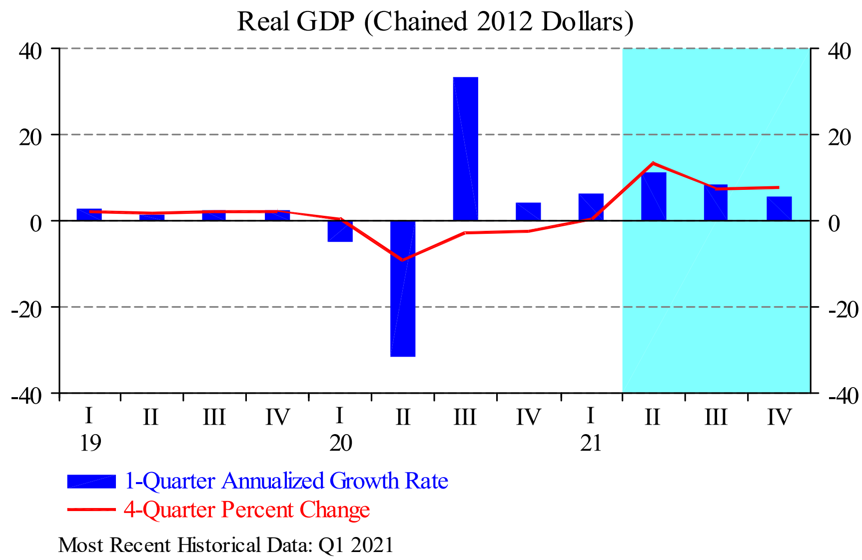
After a strong overall start to the year at 6.4% annualized growth in the first quarter, the economic recovery is expected to strengthen further in the second and third quarters. The successful vaccine program in the United States is expected to bring economic activity close to pre-COVID-19 levels in the coming months, especially in the areas of the service economy most negatively impacted by the pandemic. Massive monetary and fiscal stimulus will further raise levels of aggregate demand in the economy, supporting growth in virtually all areas. Consumer spending on services is expected to show the greatest degree of improvement, but business capital investment, international trade, inventory building, and government spending are also likely to exhibit especially high overall economic growth. Residential investment is expected to grow strongly overall in 2021, although housing may encounter inflationary headwinds. The global economy is generally recovering from COVID-19 related reductions in economic activity, promoting a synchronous global recovery. The overall national forecast for growth in real GDP is 7.2% in 2021, sufficiently high to exceed the -3.5% decline in 2020. Despite disappointing national employment growth in April, employment is expected to resume brisk growth for much of 2021, bringing the unemployment rate down to 4.5% by year-end.

While the year will be one characterized primarily by economic recovery, inflation is also expected to rise at rates that have become unfamiliar in recent years.

- Broad-based inflationary pressures have emerged that will likely result in annual inflation growth of 3.5% in 2021, well above 1.25% in 2020, and the highest since 2008 if the forecast is accurate. Numerous supply challenges and bottlenecks have emerged in restarting the economy including shortages of labor and material inputs. The worldwide shortage of semi-conductors is constraining to the production of vehicles and other modern products that require computer technology. Many of these challenges will be met by private sector adjustments in production and demand in the coming months. Therefore, overall inflation is expected to decline next year, making much of the current inflation temporary or “transitory” in the parlance of Federal Reserve policy makers. However, the current expansion of aggregate demand relative to constrained aggregate supply is historically high in magnitude, raising long-term inflation risks.
- The Federal Reserve will likely be cautious to not raise the Fed Funds rate target in 2021 so as not to forestall labor market recovery.
- However, the Federal Reserve is expected to begin to taper their asset purchases from the current $120 billion per month pace beginning in the fourth quarter.
- The Federal Reserve is also forecasted to begin to raise the Fed Funds rate target in the second quarter of 2022, ahead of current market and policy maker projections.

Central bank bond purchases are downward forces on government bond yields, thereby posing a constraint on long-term interest rate increases this year. However, with economic growth, inflation and deficit financing rising, the low 10-year Treasury yield is forecasted to climb to 2.00% by year-end, returning gradually to levels prior to the COVID-19 crisis. Interest rates and inflation are likely to push higher in 2022 if highly accommodative monetary and fiscal policies become permanent. The massive American Jobs Plan (AJP) and American Families Plan (AFP) are not incorporated into the forecast as they have not yet been approved into law. The dollar may also encounter downward pressure concurrent with a widening trade deficit and higher inflation. (For the full forecast, please see the Summary Forecast Table at the end of this report.)

Real GDP Forecasted to Grow Strongly 2021



Huntington Private Bank Leading Indicators Point to Continued Strong Economic Recovery

Our 11 leading indicators of the national economy are pointing to continued Economic Recovery and Expansion in the coming 12 to 18 months period. We rate recent data for each indicator as predicting Expansion, Contraction, or Neutral. The tally in May strongly favors Expansion, with 8 indicators pointing towards Expansion, 2 indicators with Neutral ratings, and one indicator pointing to Contraction. We review recent performance in the following:

1. **Unemployment Insurance: Initial Claims: Expansion**

Declining unemployment insurance claims are strongly predictive of economic growth and improving labor market conditions. While initial unemployment claims have been stubbornly high during the economic recovery that began last year, initial unemployment claims returned to a declining trend during the spring, upgrading a Neutral rating during the first quarter into an Expansion rating.

2. **Treasury Yield Curve: Expansion**

The Treasury yield curve is the plot of U.S. Treasury interest rates against the length of maturity on the X axis. A positive sloping Treasury yield curve is predictive of economic expansion, whereas a negative slope is predictive of recession. The current yield curve continues to have a strong upward slope.

3. **Interest rate spreads of High Yield Corporate bonds over U.S. Treasury bonds: Expansion**

The interest rate spread between High Yield Corporate bonds and U.S. Treasury bonds widens during periods of economic stress, as markets require higher interest rates to compensate for increased risk of default. Corporate spreads over Treasuries have generally been low by long-term historical standards in the year-to-date. Highly accommodative Federal Reserve monetary policies during the economic recovery, including the Federal Reserve's bond buying programs, have helped to maintain a low cost of credit to businesses, reflected by historically narrow quality interest rate spreads.

4. **Real GDP Growth Q4 to Q4: Expansion**

Real GDP declined sharply in the second quarter of 2020 but has been rising strongly since that time in an elongated V-pattern. In the first quarter of this year, real GDP rose at a 6.4% annualized rate and was 0.4% above real GDP in the first quarter of 2020. Annual real GDP growth is expected to expand sharply in the second and third quarters as the recovery widens to include COVID-19 impacted sectors of the economy.

5. **Annual National Income Corporate Profits Before Taxes: Expansion**

Along with real GDP, economy-wide corporate profits have made a strong recovery from the COVID-19 downturn. Strong Corporate profits support high levels of business expansion, capital investment, and payroll expansion.

6. **Non-Farm Proprietor's Income Growth (Small Business): Expansion**

Non-Farm Proprietor's Income reflects the general financial health and capacity of small businesses, which are leading growth engines in the U.S. Economy. Nonfarm Proprietor's income grew 1.6% YoY in Q1. The small business sector has been significantly supported by PPP and should benefit significantly from the easing of the health crisis in the coming months. Rating raised to Expansion from Neutral in January on strengthening small business income growth.

7. **Real Personal Income Growth Excluding Current Transfer Receipts: Contraction**

Real Personal Income Growth excluding transfer receipts is a direct measure of the economy's capability to generate real income independent of many transfer policies. The measure was down -0.8% Year-on-Year in the first quarter. Although nominal incomes net of transfers is expected to rise in the second quarter, rising inflation is likely to put downward pressure on real incomes, especially as the economy encounters supply constraints during reengagement in 2021. Rating lowered from Neutral in January to Contraction on rising inflation.

8. New Private Housing Units Authorized: Expansion

New Private Housing Units reflect plans for household expansion in the economy, reflecting the momentum of economic growth as well as housing markets overall. Total Permits for New Private Housing units was at 1759K in Q1 for the highest level since the second quarter of 2006.

9. Close-end Consumer Loans Delinquency rate (non-mortgage): Neutral

Overall consumer credit repayment performance has been mixed. Overall Consumer closed-end delinquency rate has been above 2.0% and rising prior to recessions. Most recent rates as of December were 2.39% for accounts and 1.96% for balances, with both stabilizing during quarter (source: ABA). FFIEC Bank Consumer Delinquency & Charge-off rates have been at historically low levels though modestly up in Q4 over Q3. High government support helping to maintain liquidity and solvency for many consumers.

10. University of Michigan Consumer Expectations Index: Expansion

A Conference Board leading index, the University of Michigan Consumer Expectations Index projects economic activity in the upcoming 6 months. Expectations have been volatile, but on an upward trend, resulting in a rating increase from Neutral to Expansion. Consumer Expectations declined between April and May on consumer expectations of rising inflation. If consumer expectations decline further in May, then the Expansion indicator will be downgraded.

11. Demand for Commercial and Industrial Loans from the Senior Loan Officer Survey: Neutral

Demand for loans is mixed but on an improving trend. Net Demand in Q1 was modestly negative at -6.1 for Mid-to-Large Firms (Annual Sales greater than $50 million), and modestly positive at +2.9 for Small Firms (Annual Sales greater than $50 million). (Source: Federal Reserve)

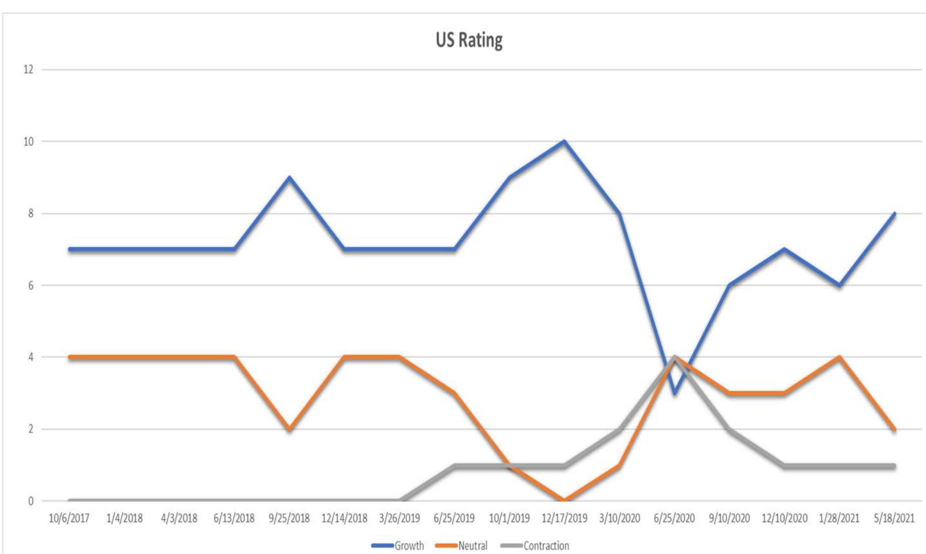
TOTAL United States Economy

Overall Economic Indicators are supportive of the Economic Expansion Forecast for 2021. Financial, GDP, Profits, and Housing indicators are strong. Labor market indicators have improved. The major negative development in April and May was rising inflation. Inflation is slowing consumer real incomes growth before transfers, thereby slowing baseline consumer purchasing power.

Summary Table
Huntington Private Bank Leading Economic Indicators
May 2021

Leading Indicator	Rating
Unemployment Insurance: Initial Claims: Expansion	Expansion
Treasury Yield Curve	Expansion
Quality Interest Rate Spreads	Expansion
Real GDP Growth	Expansion
National Income Corporate Profits Pre-Tax Growth	Expansion
Non-farm Proprietor's Income Growth	Expansion
Real Personal Income Growth Excluding Current Transfer Receipts	Contraction
New Private Housing Units Authorized	Expansion
Close-end Consumer Loans Delinquency rate (non-mortgage)	Neutral
University of Michigan Consumer Expectations Index	Expansion
Demand for Commercial and Industrial Loans from the Senior Loan Officer Survey	Neutral
Total United States Economy	Expansion

Huntington Private Bank Leading Indicator Rating History
Improving Overall Trends in Expected National Economic Growth

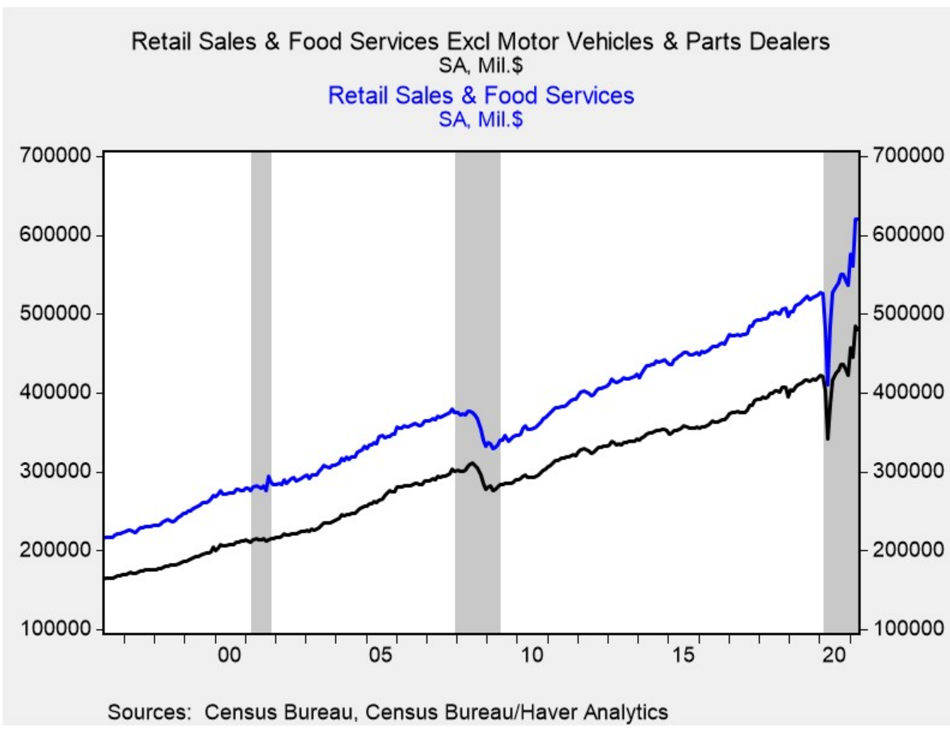


Second Quarter Economic Update: Strong Economic Growth, Constraints to Supply, and Increased Inflation

The United States economy is in a period of strong economic growth, but with rising inflation and considerable supply bottlenecks. We spotlight key areas of the economy through the following charts on key economic developments.

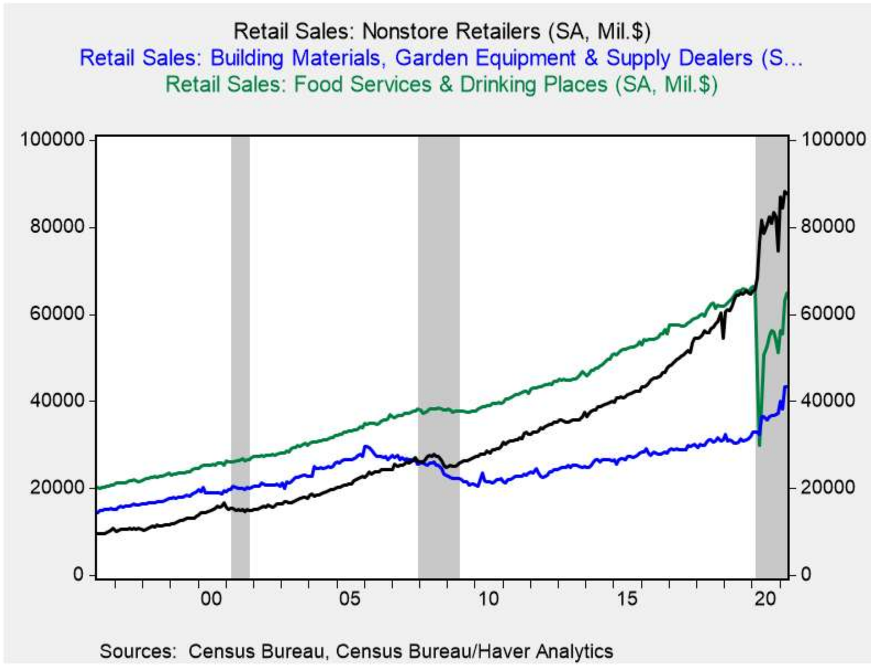
- Total retail sales in April were only 0.02% higher than they were in March, but March levels were already at record highs. Retail sales excluding motor vehicles and parts dealers were down -0.8% month-to-month but following a record high month. Annual comparisons to the COVID-19 closure months of March and April 2020 are extremely positive. Total retail sales were up 51.2% in April. Retail sales excluding motor vehicles and parts dealers were up 40.6%.

Retail Sales at Record Levels



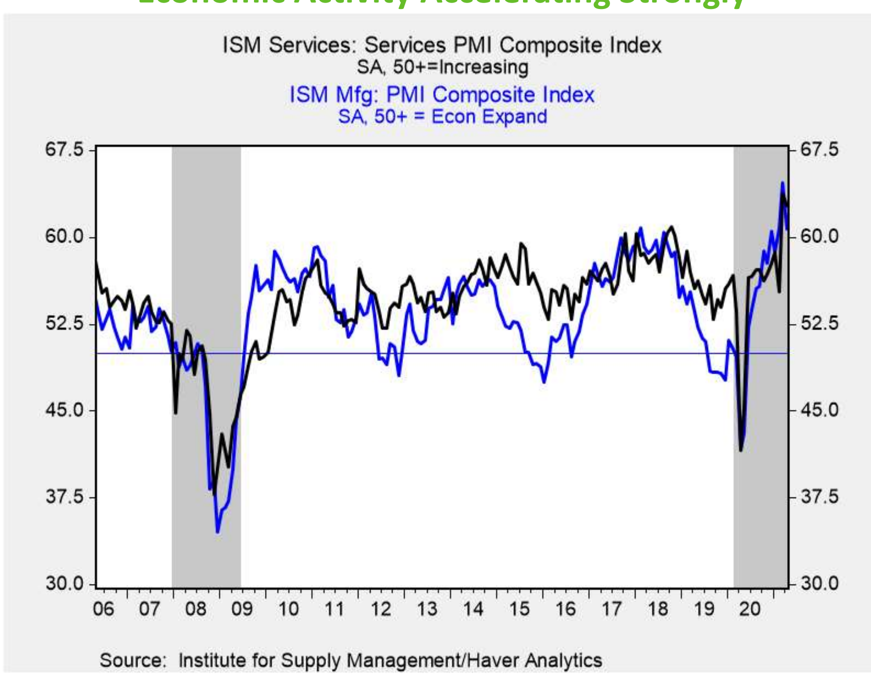
- Retail sales have risen sharply in areas that were negatively impacted by the COVID-19 closures and downturn. From April 2020 to April 2021, retail sales surged 116.8% at Food Services and Drinking Places, 104.5% at Motor Vehicle and Parts dealers, 170.1% at Furniture, Home Furnishings, Electronics & Appliance dealers, 155.0% at Sporting Goods, Hobby, Book & Music stores, and 727.8% at Clothing and Accessory stores. In addition to strong growth in retail establishments negatively impacted by COVID-19, retail sales also remained strong in retail sectors that benefited from COVID-19 related mobility reductions. Retail sales rose annually by 14.5% for Non-store Retailers, and by 33.8% for Building Materials, Garden Equipment, and Supply Dealers.

Retail Spending Growth is Broad-based, including Restaurants and Drinking Places and other Retail Sectors negatively impacted by COVID-19



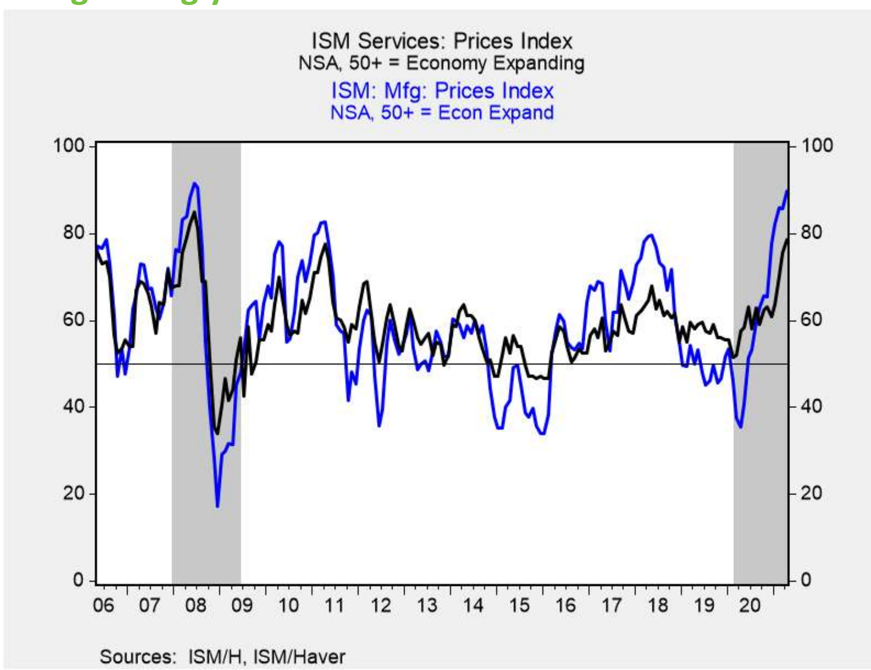
- Economic indicators point to very strong economic growth. According to the Institute for Supply Management, combined economic activity in Manufacturing and Services was at a record high in March, followed by the second highest level in April. (Records go back to July 1997.) In contrast to much of 2020 when Manufacturing outperformed the Services sector, the current acceleration in economic activity is in both Services and Manufacturing areas of the economy.

Economic Activity Accelerating Strongly

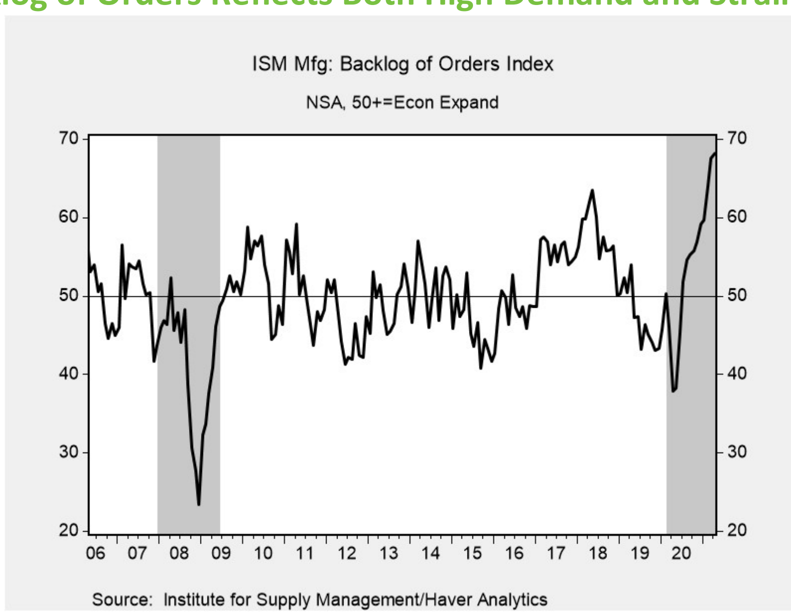


- Price pressures are rising as historically high aggregate demand encounters constrained aggregate supply. Economic activity is rising at record speeds, but supply bottlenecks and depleted inventories are forcing prices significantly higher as well. West coast port clogs, depleted retail inventories, shortages of semi-conductors and other critical components for vehicle production, spiking commodity prices, and general labor shortages are constraining supply in the economy during a period of extraordinarily high aggregate demand. Other recent shocks to supply include significant utility shutdowns during the severe winter in Texas, a cyberattack on a major oil pipeline, and a traffic jam of barges on the busy Mississippi caused by a crack in a major bridge.

Prices Paid Rising Strongly as Bottlenecks and Low inventories create headwinds

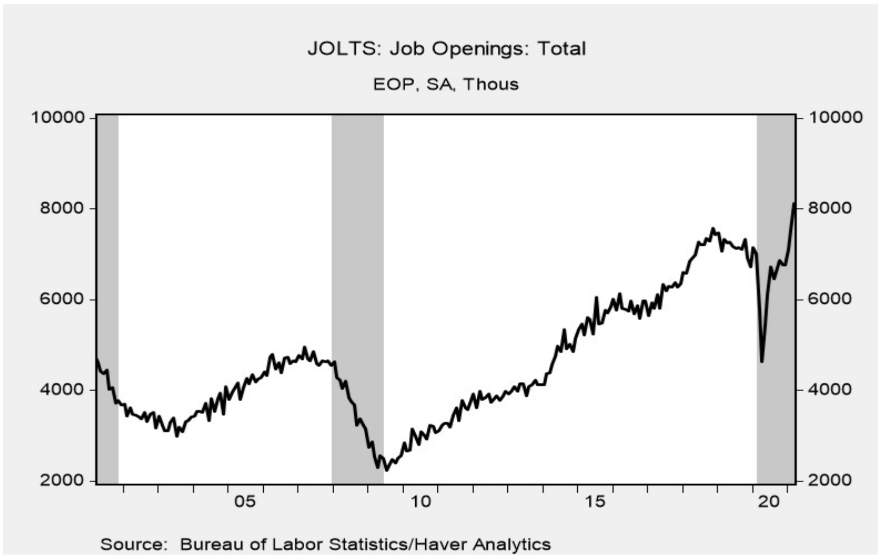


Rising Backlog of Orders Reflects Both High Demand and Strains on Supply



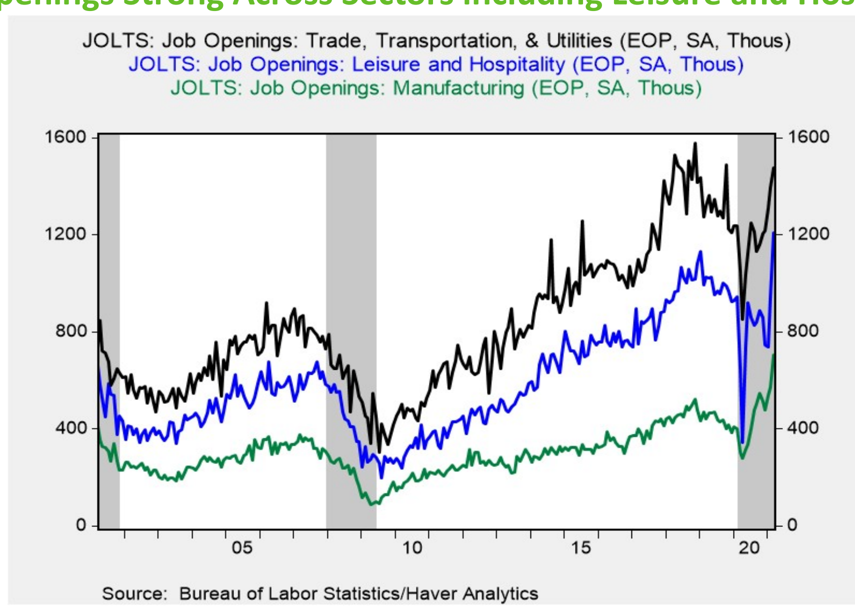
- Job Openings rose to a record high in March, just one year after COVID-19 shut down many parts of the economy. Total Private and Government job openings rose to record highs.

Job Opening Rise to New Record High in March



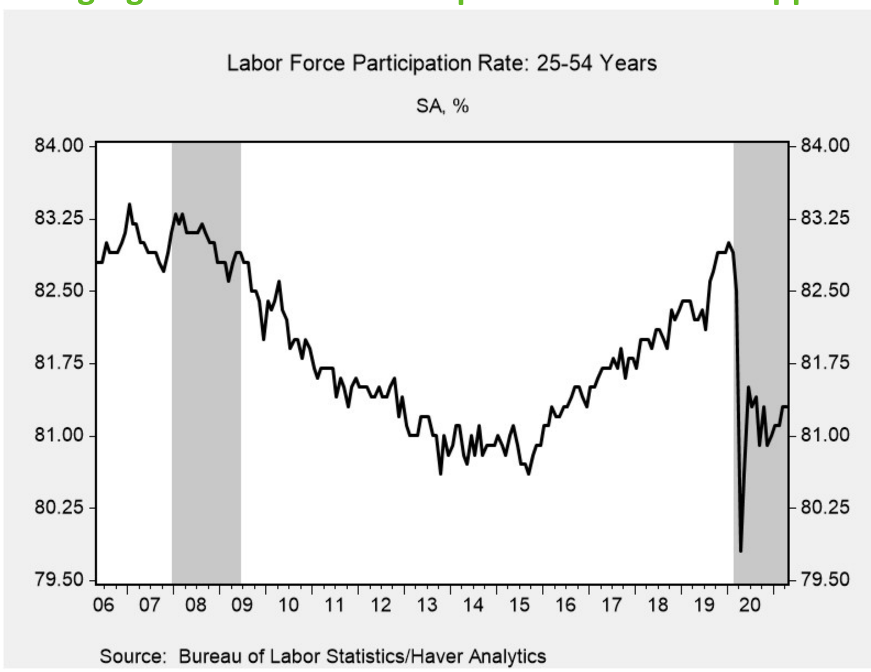
- Job Openings were broad-based across major sectors of the economy, including Leisure and Hospitality, the hardest hit sector of employment losses resulting from the COVID-19 shock and closures. Leisure & Hospitality Job Openings joined Manufacturing Job Openings to reach record highs. Job Openings in Leisure & Hospitality rose to 1,209,000 in March, 30.8% above the average annual job openings of 924,000 in 2019, the full year before the COVID-19 downturn. Job openings in Manufacturing were 706,000 in March – 83.4% above the average annual job openings in 2019. Education and Health had their second highest job openings on record at 1,425,000 in March, following record high job openings of 1,592,000 in February.

Job Openings Strong Across Sectors including Leisure and Hospitality



- The Labor Force Participation Rate of Prime Working Age Workers (25 – 54 years of age) has not shown signs of recovery even as Job Openings (JOLTS) have climbed to record levels. At 81.3% in April and 81.2% in the first quarter, the Prime Working Age Participation Rate was significantly below the 83.0% pre-COVID-19 peak participation rate in January 2020. The continuation of low participation during a period of plentiful jobs may indicate serious structural challenges in labor markets if payroll growth remains subpar in the coming months, as it did in April when employment grew 266,000 instead of the one million anticipated by consensus economic forecasts.

Prime Working Age Labor Force Participation Remains Disappointingly Low

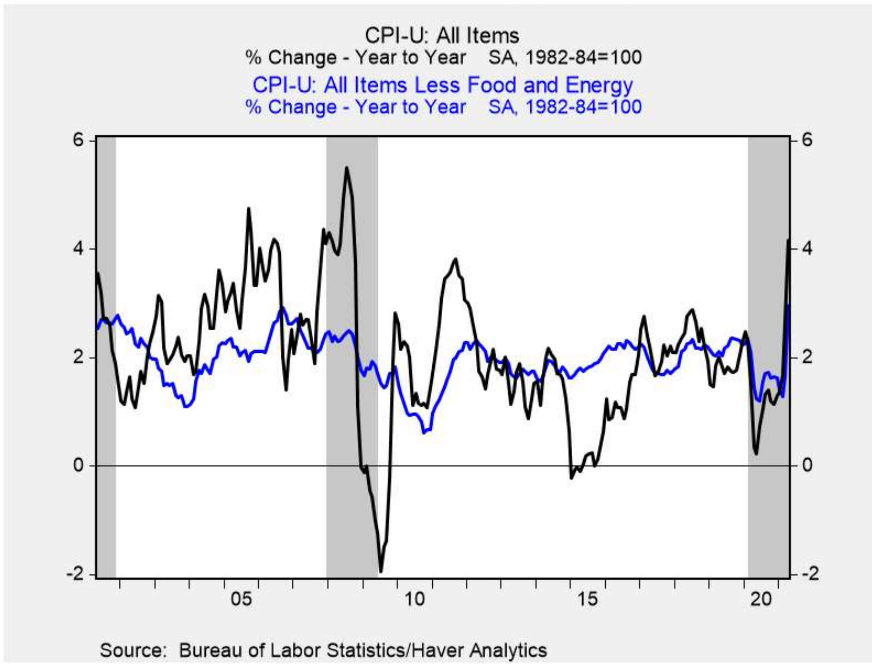


Supply disruptions, inventory shortages, and labor shortages have contributed extensively to recent price pressures. Many of these disruptions will likely prove "transitory" or temporary, but they are significant in the near term. For example, the shortage of semiconductors has already had far reaching impacts on vehicle markets as production of new vehicles will likely slow. An anticipated shortage of new vehicles has already lifted vehicle prices generally, including a 10% rise in used car prices in April.

Despite significant inflationary pressures from transitory factors, current inflationary pressures go beyond temporary supply disturbances and are beginning to impact real sectors of the economy. Inflationary pressures are broad-based and building in the Consumer Price Index (+4.15% Year-to-Year in April), the Producer Price Index (+6.2% Year-to-Year in April), GDP (4.1% annualized rate in the first quarter), and most commodities (CRB Index up 50% Year-to-Year in April). During the first quarter, double digit annualized inflation rates occurred in imports (+13.3%), exports (19.7%), and residential investment (+11.4%). Inflation was also accelerating in government expenditures (+6.2%).

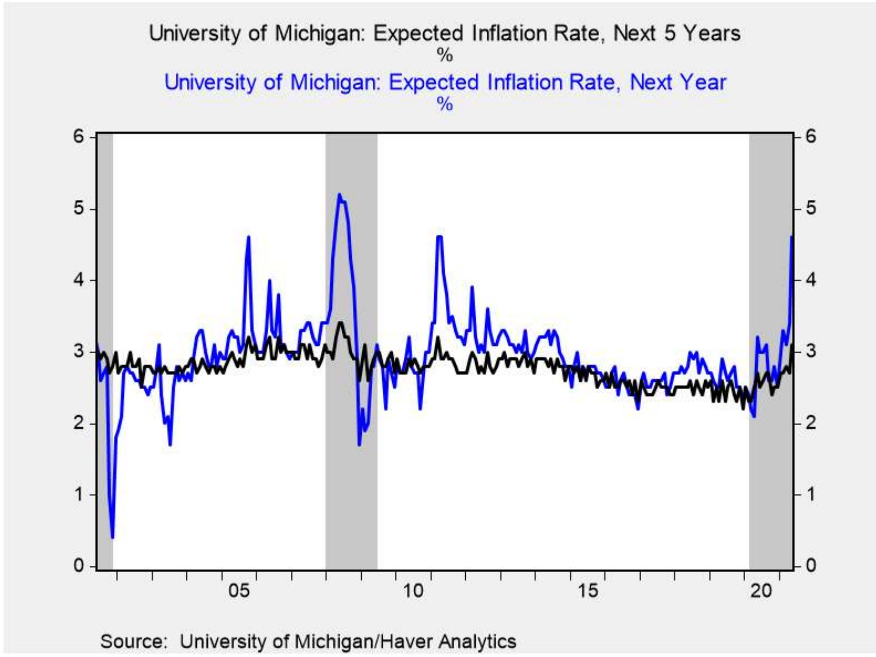
In the coming months, inflation in services will likely accelerate as demand returns to the services sector. Wages will likely rise to encourage workers to return to work as well. Home price growth has been arguably inflationary in the last year (please see the following concerning median home prices) and could ultimately boost rents. Inflation will likely decline from current levels as supply bottlenecks are resolved, but the breadth and extent of current inflationary increases will likely raise long-term inflation risks from the benign levels of the last decade.

Inflation Rises Sharply in April



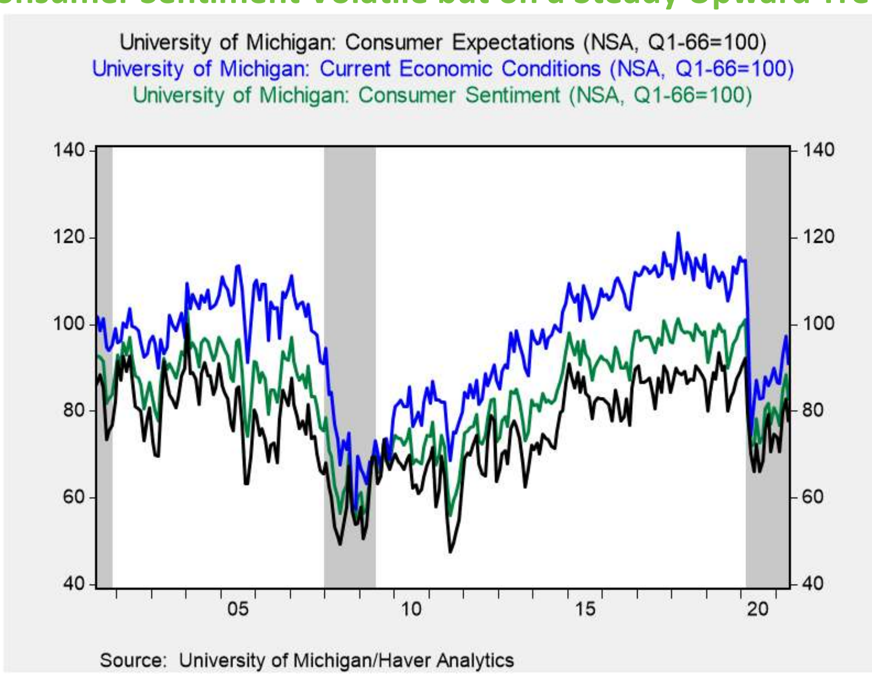
- Consumers expect higher inflation. Consumer expectations of inflation in May rose to 4.6% in the next year, up from 3.4% in April and 2.7% overall in 2020. Their expectations are right in line with recent actual inflation. In the next 5 years, consumers expect inflation to rise 3.1% per year, up from 2.7% in April and 2.5% overall in 2020. Expectations of inflation are an important aspect of many Federal Reserve models of inflation and viewed as a source of future inflation.

Consumers Beginning to Become Concerned about Inflation as Expectations Rise



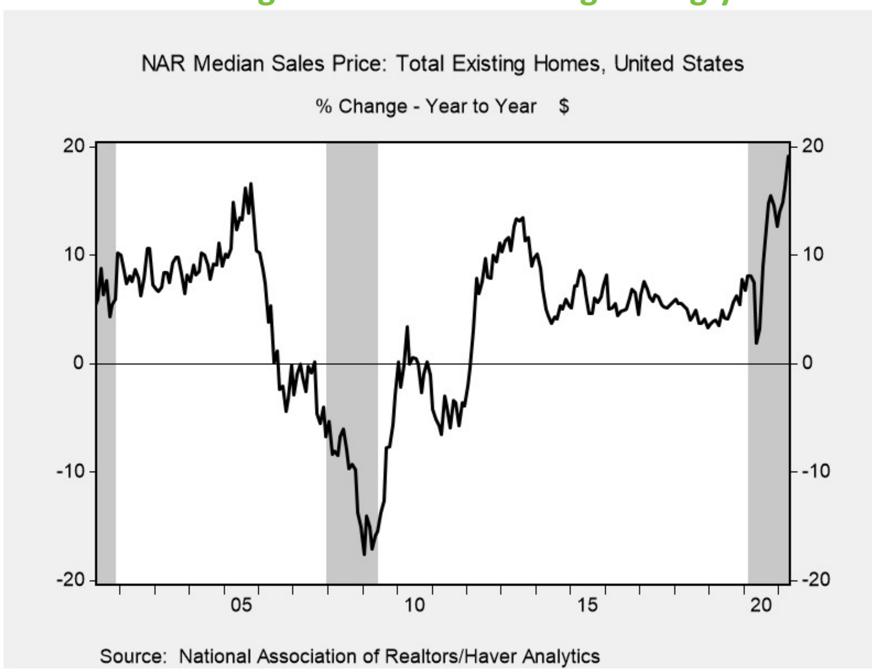
- Consumer Sentiment lost some ground on rising inflation concerns in May after very strong increases in March and April, but the overall upward trends are sustained in Consumer Expectations, Consumer views of their Current Economic Conditions, and in overall Consumer Sentiment. The ground is steep to the pre-COVID-19 level, but the consumer continues to move in a positive direction that will likely be significantly reenforced with increased normalization of activities in the coming months. With job openings plentiful, those that desire employment should also be able to find it.

Consumer Sentiment Volatile but on a Steady Upward Trend



- The NAR median Sales Price of Existing homes rose to $341,600 in April for an increase of 19.1% in one year. Regardless of measure, home prices are rising strongly across the nation. The S&P CoreLogic Case-Shiller 20-city House Price Index rose 13. 3% year-to-year in March for the strongest annual growth in home prices in the 20 largest metropolitan areas since December 2013. Low inventory and high demand are driving a boom in housing markets. While strong housing markets lift consumer wealth, and well-being, they also may be exhibiting nascent signs of inflationary pressures entering housing markets. Annual median home price increases have topped those during the infamous housing boom years of the first decade of the new millennium as evident in the chart below.

Housing Market Prices Rising Strongly



Forecast Summary Table

Key Economic Indicators

May 26, 2021

	2018	2019	2020	2021*
Total Real GDP Annual Growth Rates 2012 Chained Dollars	2.9%	2.3%	-3.5%	7.2%
Consumption	3.0%	2.6%	-3.9%	8.1%
Non-Residential Fixed Investment	6.4%	2.1%	-4.0%	7.9%
Residential Fixed Investment	-1.5%	-1.5%	6.1%	15.5%
Exports	3.0%	0.0%	-13.0%	5.1%
Imports	4.4%	1.0%	-9.3%	12.3%
Government Purchases	1.7%	2.3%	1.1%	5.8%
Change in Private Inventories (Billions 2012 Chained Dollars)	$48.1	$67.0	$-77.4	$13.6
Trade-Weighted Dollar Index (Jan. 2006 = 100) Year-End Source: Federal Reserve	115.6	114.7	111.56	109.0
Nominal GDP Current dollars	5.4%	4.1%	-2.3%	10.8%
Consumer Price Index for Urban Consumers (CPI-U) – Average Annual Rate	2.4%	1.8%	1.25%	3.5%
Federal Funds Rate Target Year-end range	2.25% to 2.50%	1.50% to 1.75%	0.00% to 0.25%	0.00% to 0.25%
10-year Treasury Note Year-end interest rate yield	2.69%	1.92%	0.93%	2.0%
National Income Pre-tax Corporate Profits Average annual growth rate	6.1%	0.3%	-1.2%	12.0%
Net New Average Monthly Non-Farm Payrolls (Thousands of Workers)	193K	178K	-785K	+621K
Unemployment Rate – Year End	3.9%	3.5%	6.7%	4.5%

- Data Sources: Haver Analytics, Federal Reserve, Factset Inc., and other sources noted in text.

* Forecasts: Huntington Investment Management of the Private Bank, Division of Huntington National Bank

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