GDP growth forecast to be fastest since 1984

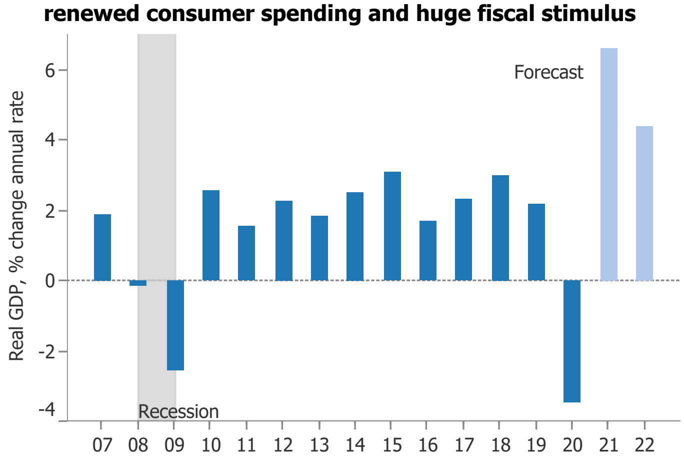
• **Real GDP plunged in the second quarter of 2020 but rebounded by 9 percent in the second half of last year.** The economy has proven much more resilient than expected. The Blue Chip consensus now projects that GDP will grow 6.6 percent this year with the most optimistic panel members forecasting growth of 7.3 percent. In addition to headway against the virus – 80 percent of the population is expected to be vaccinated by October of this year – real activity will be bolstered by unprecedented fiscal stimulus and continued support from the monetary authorities. See figure 1.

• **Federal government debt increased from $5 trillion in new fiscal stimulus programs enacted over the past year.** This is expected to push federal debt to about 110 percent of GDP by 2023. At present, low interest rates make the national debt more affordable. But the mounting debt burden could put upward pressure on long-term interest rates as lenders demand compensation for the increased credit risk. This would result in lower saving, reduced investment, and slower economic activity. See figure 2.

• **Rapid economic growth and base year effects will cause inflation to jump in the first half of this year.** Energy and transportation services prices plunged from January to May of last year and temporary supply bottlenecks are currently constraining production. However, slack in the economy will prevent breakaway inflation from developing. In the past half century, inflation has never experienced a sustained pick up unless the economy had been running above full capacity for an extended period. See figure 3.

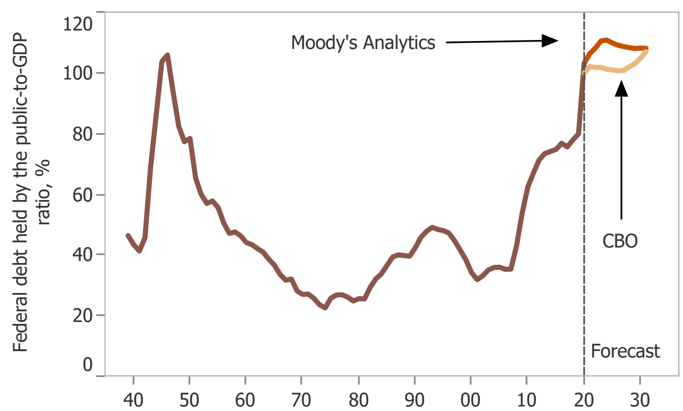
• **Monetary policy will remain accommodative.** The Federal Reserve is expected to keep short-term rates near zero through 2022, but market-determined long-term rates are forecast to climb steadily reflecting vigorous economic growth and expectations of higher inflation. The Blue Chip consensus foresees the 10-year Treasury yield increasing to a range of 1.8-2.5 percent by the end of 2022. The central bank's stated goal is to encourage a rise in inflation to somewhat above its long-term target of 2 percent and maintain it there for a significant period before tightening policy. See figure 4.

Figure 1: Real GDP growth is expected to rise sharply on renewed consumer spending and huge fiscal stimulus



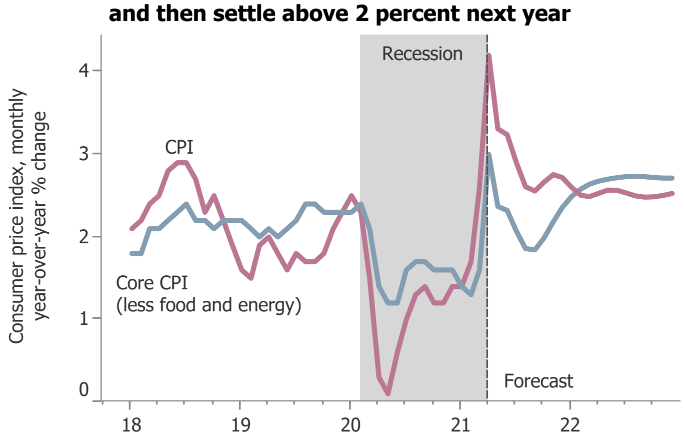
Sources: BEA, Blue Chip Concensus Indicators (May 2021)

Figure 2: Rising federal debt raises long-term concerns, but low interest rates make the debt more affordable



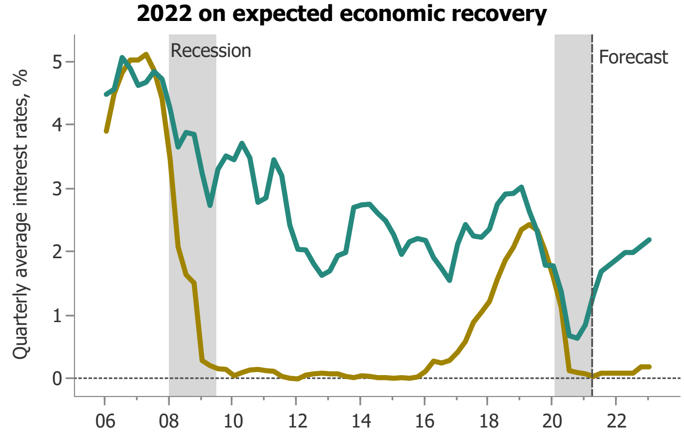
Sources: U.S. Treasury, CBO (February 2021), Moody's Analytics (baseline forecast May 2021)

Figure 3: Inflation to move temporarily higher and then settle above 2 percent next year



Sources: BLS (data through April 2021), Moody's Analytics (baseline forecast May 2021)

Figure 4: Yield curve forecast to steepen through 2022 on expected economic recovery



Sources: Federal Reserve (data through 1Q:2021); Blue Chip Consensus Indicators (May 2021)