WBA
WISCONSIN ECONOMIC
REPORT
A compilation of sector forecasts from industry experts.

Wisconsin Bankers Association

Bankers are Prepared for Challenges

By Rose Oswald Poels, WBA President and CEO

Wisconsin banks are well positioned to help their customers and communities navigate through 2023, which is expected to be a more challenging year economically. With interest rates rising dramatically throughout last year, banks' profitability has increased to a net interest margin of 3.19% in the third quarter of 2022.

All categories of lending have seen increases both on a quarter-over-quarter basis, as well as year over year. Residential loan demand continued to grow at a steady pace, up 5.25% from the prior quarter, and 10.23% from the prior year, despite rising interest rates, due in part to a decline from a high in home prices. Commercial lending saw ongoing strong demand year over year with an increase of 10.04%, although the third quarter grew at a slower pace of 2.25% from the prior quarter, signaling business owners' concerns around inflation, a potential recession, and uncertainty heading into the midterm elections. Finally, farm loans increased 5.80% quarter over quarter and 6.79% year over year, representing a consistent pace of borrowing in light of higher input costs such as fuel and fertilizer.

Also demonstrated in the 2022 third quarter numbers is the strong financial health of Wisconsin bank borrowers. Credit quality remains very strong with loans and leases 90 or more days past due continuing their downward trend, remaining at historic lows. Noncurrent loans compared to total loans is now at .40% — which is essentially negligible. Borrowers are keeping on top of their monthly loan payments, even through this inflationary period. Consumers are tapping into their savings to offset higher food and energy prices, and to pay down debt. The pace of deposit growth at Wisconsin's banks has slowed, where total deposits grew only 1.45% from the prior quarter, and just 3.83% year over year.

On a national level, economic data is consistent with the themes seen from the banking industry's data. Real personal consumption expenditures, which account for about 70 percent of real GDP, continued to expand during the first half of 2022, albeit at a slow pace. Other important economic indicators, such as payrolls, industrial production, and manufacturing activity, also slowly expanded in the first half of the year, while real retail sales and real personal income were mostly flat.

Looking ahead, bankers are in a unique position given their insight into the financial well-being of their individual and business customers to share thoughts as to what 2023 could bring. WBA conducted an end-of-year survey between November 15–30 with 71 bank CEOs responding to our Economic Conditions Survey. While there are some bright spots in the survey results, bankers are concerned about a looming recession.

Three quarters of respondents rated Wisconsin's current economic health as "excellent" or "good." This continues a trend from the mid-year 2022 survey, when 71% of survey respondents gave "excellent" or "good" ratings. None of the Wisconsin bank CEOs who completed the most recent survey foresee major economic improvement in the first half of 2023 — 28% predict that the economy will stay the same and 72% predict it will weaken in the next six months. Given the likelihood of a recession in 2023, bankers are understandably concerned about borrowers' continued ability to repay loans, and the effect ongoing rising rates will have on slowing economic growth even further.

Among the economic bright spots cited by CEOs in the survey were high employment, continued spending by consumers, the housing market, and business growth — particularly in manufacturing, agriculture, and service/tourism.

High inflation and the Federal Reserve's response to it are certainly concerns heading into 2023. The Federal Reserve's tightening has been aggressive throughout 2022, and while it is expected that the Federal Reserve will continue to raise rates in 2023 to combat inflation, it likely will do so in smaller increments than what was seen last year. More time needs to be given to let the effect of these rate hikes work their way through the system before another major increase occurs.

Despite concerns looming about a recession, Wisconsin consumers and business owners will be able to continue to rely on their banks as a source of trusted financial partnership and a safe place to deposit their money.

Founded in 1892, WBA is the state's largest financial industry trade association, representing more than 200 commercial banks and savings institutions, their branches, and over 30,000 employees. The Association represents banks of all sizes in Wisconsin, and nearly 98 percent of banks in the state are WBA members.

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Wisconsin Hospital Association

COVID Continues Stress on Health Care

By Eric Borgerding, WHA President and CEO

Nearly three years after COVID-19 upended the health care system, hospitals continue adjusting to what are clearly longer-lasting, if not permanent, impacts of the pandemic. At the same time, Wisconsin hospitals and health systems, 95% of which are nonprofit, continue providing a variety of services and filling social and public health gaps across the state, but ongoing strains on resources, finances, and workforce are posing unprecedented challenges to fulfilling these missions.

> According to the American Hospital Association, hospitals' use of contract temporary labor increased 132% for full-time and 131% for part-time staff last year.

Well-documented burnout caused job vacancy rates to increase in 13 of 17 Wisconsin hospital professions in 2021, by double digits in seven of those. Higher vacancies have forced hospitals to increasingly rely on very costly temporary staffing. According to the American Hospital Association, hospitals' use of contract temporary labor increased 132% for full-time and 131% for part-time staff last year.

As reported in our 2022 Workforce Report, citizens over the age of 55 make up 28% of the country's population but account for 57% of health care spending — trends mirrored here. As health care needs increase with the aging population, demand for Wisconsin's health care workforce will also increase while its supply is expected to diminish. An aging population also means more health care is covered by Medicare, which reimburses Wisconsin hospitals at 23% below what it costs to provide care. Medicare now comprises nearly 50% of Wisconsin hospitals' "payer mix" and is growing.

The CDC estimates that 41% of U.S. adults either delayed or avoided non-COVID medical care during the early stages of the pandemic. Patient volumes have rebounded since their COVID-induced plunge in 2020, but many of those patients are sicker, more resource- and cost-intensive with longer, often unreimbursed, lengths of stay.

Hospitals are not immune to the impacts of historic inflation, which has caused sharp spikes in labor, drugs, and medical supplies costs. Wisconsin hospitals have experienced a $580 million annual increase in labor costs and $1.6 billion annual increase in supply costs since 2019. We reported in October that supplies and services remain the largest expenses for Wisconsin hospitals, up 14.7% since 2019. The ability to simply recoup these costs by raising prices has essentially disappeared, yet health insurance premiums continue rising. According to a recant *Kaiser* analysis, in the past year, the CPI for hospital services rose 3.4%, compared to 7.7% for all good and services and a whopping 20.6% for health insurance.

> Wisconsin hospitals have experienced a $580 million annual increase in labor costs and $1.6 million annual increase in supply costs since 2019.

> Responsible stewardship has helped Wisconsin hospitals manage through the pandemic, but its lingering damage is posing serious and ongoing challenges.

Soaring inflation coupled with diminished resources caused drastic declines in Wisconsin hospital and health system operating margins in the first half of 2022, falling to 0.4%. Total margins dropped well into the red at -11.9%.

Despite these new realities, Wisconsin's hospitals remain committed to delivering quality care for everyone, while still subsidizing negative margin services (hospice, home health, behavioral health, long term care, others) that would not otherwise exist in many communities. Responsible stewardship has helped Wisconsin hospitals manage through the pandemic, but its lingering damage is posing serious and ongoing challenges.

Established in 1920, Wisconsin Hospital Association (WHA) advocates on behalf of its 140-plus member hospitals and health systems to enable the delivery of high-quality, high-value care across Wisconsin. Visit WHA at wha.org.

Construction Business Group

Building for the Future — 2023 Construction Industry Forecast

By Robb Kahl, CBG Executive Director

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Economic forecasts are a bit like New Year's resolutions — hopeful optimism for future success in areas that one struggled with in the past. For the construction industry, the hope is that 2023 will bring an increase in owner confidence to invest in construction projects, lower interest rates to make project financing possible, leveling of material prices and availability to minimize bid price increases and material delays, and an ample supply of employees, willing and able to work building Wisconsin.

In 2022, U.S. total construction starts rose 11% (through September) with increases in all major sectors: private residential 13%, private nonresidential 11%, and public sector, including transportation, 7%. The Architectural Billing Index for September reflects that architectural billings are up slightly over 2021, a good sign of new projects to come, and the Dodge Momentum Index is up over 25% from October 2021. Manufacturing, water supply, and commercial construction saw the largest increases in 2022 with power, office, and transportation at levels lower than or equal to 2021. As historical trends demonstrate, growth in the different construction segments can vary widely each year. In 2023, federal funding is anticipated to spur growth in some markets that were down this past year.

Transportation, manufacturing, and energy projects are forecasted to be strong in 2023 due in part to three major investments made at the national level. The Infrastructure Investment and Jobs Act (IIJA) signed in November 2021 authorized an additional $550 billion above baseline infrastructure spending to fund the interconnected transportation network and supports expansion of broadband, bridge repair, and clean energy transmission and power upgrades. The Chips+ Act funds investment in domestic manufacturing of semiconductors. The Inflation Reduction Act of 2022 includes a major expansion of tax credits (and direct payments to municipalities, non-profits, and tribes) for investment in projects that increase energy efficiency and reduce carbon emissions.

Despite the ongoing concerns about a housing shortage, particularly for accessible housing, it is forecasted that both multi-family and single-family housing will fall for at least the first half of 2023 due to rising interest rates. The post-pandemic shift from retail to e-commerce and office work to employee preference for hybrid work leaves ongoing uncertainty in the retail and office sectors but leads to increased demand for e-commerce/distribution and decentralized office locations.

The availability and cost of building materials in 2022 was particularly challenging for contractors as they strived to keep bid price increases at a minimum. Between April 2020 and September 2022, steel increased 91%, plastic construction products 56%, and copper and brass mill shapes 54%. While these increases in construction inputs are remarkably high, the good news is that the prices have been rapidly falling since Q1 of 2022, giving optimism to contractors and owners alike. While material costs and supply chain challenges increased between April 2020 and April 2022, they are stabilizing; unlike the challenge of finding workers. Wisconsin, like the rest of the Midwestern states, has close to no population growth, making worker shortages once again the #1 challenge for construction, and every other industry.

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Wisconsin's construction industry contributes not only to the quality of life we enjoy but is an important stimulator for the economy. Every $1 spent within the construction industry produces an economic impact of $1.81. Every $1 million spent within the construction industry generates 12 jobs on average (7 within construction and 5 in other sectors) and over $690,000 in wages. We look to 2023 with optimism and are prepared to work with other industry leaders as we Build Wisconsin Together.

The Construction Business Group promotes and protects the construction industry. We ensure fair contracting laws are followed on public construction projects. We work cooperatively with contractors, employees and public entities by educating them on fair contracting laws, monitoring projects for fair contracting compliance, and identifying and helping to resolve compliance issues.

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Wisconsin Farm Bureau Federation

Wisconsin Farmers Continue to be Cautiously Optimistic

By Kevin Krentz, WFBF President

It's often said, you have to be an optimist to be a farmer. While there is a lot to be thankful for as we head into 2023, there are also a lot of concerns lingering for Wisconsin farmers who experienced a year of great turmoil and change. But alas, it's time to look ahead to a new year.

The past year brought a war in Ukraine, severe drought pockets in the western portion of the U.S., intense market volatility, as well as inflation that we haven't experienced in 40 years. These have drastically complicated the commodity markets in the U.S.

At the farmgate, we have seen increased prices for the commodities we produce, but like other industries, we also experienced increased costs for everything from tractor parts to seed and fertilizer. In general, there is optimism for 2023 because of the global demand for products, but there also is skepticism among farmers.

Farmers are good at controlling what we can control. Many farmers use forward contracts on both production and purchased inputs or protect their margins through insurance or hedging. Through good management, we also need to nurture our crops and care for our livestock. Balancing business needs is a major focus and seems to get more complicated by the year.

According to the U.S. Bureau of Labor Statistics, the current annual inflation rate for the U.S. for the 12 months ending October 2022 stands at 7.7%. Generations of farmers have not experienced rates at this level. Add to that the supply chain challenges that have affected equipment purchases and building expansions, and we have some large stress points within the agricultural community.

Higher interest costs and current land prices also make it challenging for beginning farmers to enter the industry, which will continue the trend of consolidation.

Like many other industries, another issue farmers and agribusinesses face is a severe lack of employees. The BLS also reports that Wisconsin's October unemployment rate was at 3.3%. Labor shortages will continue to drive innovation and automation as farms find ways to become more efficient with limited workers. Once politics settle, a focus on immigration reform will be revisited.

Our state's farmers not only supply locally but are a large part of the global food supply.

Farm Bureau has long advocated for reducing trade barriers globally and will continue to do so. The current geopolitical environment will continue to change our trade maps moving forward, but U.S. farmers can compete with other global food producers when presented with barrier-free trade.

On the consumer front, food prices are constantly a focus and talking point. Some of the higher costs at the farm level are being passed to customers at the grocery stores. This is driving the demand for certain products and consumers wanting to know where and how their food is grown and raised.

Within the consumer conversation, we are continuously evaluating our practices when it comes to conservation. However, in order to be sustainable, we cannot regulate farms out of business. Farmers must be able to afford to adapt to the ever-changing government regulations and industry requirements while being able to try new things that might better our resources. Wisconsin farmers are some of the most progressive at this throughout the country. We have made great progress and will continue to lead innovation.

> "Wisconsin agriculture consists of 64,100 farms on 14.2 million acres and annually contributes $104.8 billion to our state's economy."

Wisconsin agriculture consists of 64,100 farms on 14.2 million acres and annually contributes $104.8 billion to our state's economy. Much of which is spent within the state's rural communities.

Wisconsin Farm Bureau has advocated for farmers for more than 102 years and as farming continues to adapt to feed the world, Farm Bureau will continue to adapt to support our farmers.

Every year, through our grassroots process, Farm Bureau voting members at the county level bring forth policy that guides our organization at the local, state, and national levels on issues affecting our members. There is no shortage of topics to be discussed for our farmers.

As a new year and political cycle begin, you can expect many of these topics to be discussed.

There is optimism for the new year because, by nature, farmers are hopeful people. We will see what the truth holds in the next 12 months as 2023 unfolds.

Wisconsin Farm Bureau Federation is the state's largest general farm organization, representing farms of all sizes, commodities and, management styles. There are more 46,000 members that belong to WFBF. Voting Farm Bureau members annually set the policy the organization follows, and are involved in local, state, and national affairs, making it a true grassroots organization.

Wisconsin Manufacturers & Commerce

The New Malaise

By Kurt R. Bauer, WMC President and CEO

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2022 felt a lot like the **Carter** years of the late 1970s. That period was marked by runaway inflation, spiking interest rates, high crime, energy insecurity, and the Cold War. Add to the mix a lingering governmental legitimacy crisis caused by Watergate, and the blow to both our national psyche and international prestige caused by the Iranian hostage crisis (and the failure of the Desert One rescue mission).

All of the above created a widespread belief that America was in decline.

I see a lot of parallels to what happened then and what is happening now. For example:

- Inflation is the highest it has been since the 1970s;
- Interest rates are rising;
- Crime is rampant in big cities;
- The cost of energy is way up and its reliability is in question;
- We face a new Cold War with not only Russia, but with China as well;
- Distrust in government and other institutions is way up; and
- We saw an incredibly chaotic U.S. withdrawal from Afghanistan.

The difference between 40 years ago and now is that many of the problems we face today are self-inflicted by wrongheaded policies. When President Carter gave his "malaise speech" in 1979, the U.S. didn't have the technology to affordably extract oil and gas from the vast deposits of shale found in North America, which meant we were at the mercy of the Organization of the Petroleum Exporting Countries (OPEC).

Hydraulic fracturing changed all that and as a result, the U.S. was a net exporter of oil and gas in 2019 and 2020. But, not today because the **Biden** Administration's energy policy is to rapidly (I would argue recklessly) transition away from fossil fuels by thwarting the investment, exploration, extraction, refinement, and transportation of domestically produced coal, oil, and natural gas. As a result, energy prices are rising, which drives inflation because energy is the common ingredient in everything that is made, grown, and transported. That is why energy is often referred to as the master resource. Without reliable and affordable energy, countries cannot prosper. The U.S. is no exception.

What we are doing is unprecedented. In the history of the world, I can't think of another nation that had access within its borders to an incredibly valuable natural resource, but decided not to use it. Instead, the U.S. is begging other nations, including unfriendly and/or autocratic regimes like Venezuela and Saudi Arabia, to sell us the energy we are capable of producing ourselves. Not to mention that the U.S. is dependent on China for the production of much of what goes into or otherwise constitutes "green" energy, like batteries, wind turbines, and solar panels.

Looking ahead, I am not optimistic because if you keep doing what you are doing, you are going to keep getting what you got. According to *Gallup*, 81% of Americans said before last fall's mid-term elections that they were dissatisfied with the direction of the country. Despite that, President Biden's party performed unexpectedly well, which will embolden him to stay the course.

As a result, energy inflation could very well tip the U.S. into a recession in 2023. It will certainly continue to hurt Wisconsin's two signature industries — manufacturing and agriculture — because both consume a lot of energy.

> "Without reliable and affordable energy, countries cannot prosper. The U.S. is no exception."

Oddly, the saving grace may be the workforce shortage. As has been well documented, Wisconsin has a demographically induced labor shortage caused by a combination of several decades of below replacement birthrates and outmigration patterns.

I recently asked an economist from the Federal Reserve Bank of Chicago if there can be a recession without a spike in the jobless rate. The economist smiled wryly and answered with an emphatic no. So even with high inflation, tangled supply chains, and rising interest rates, unemployment in Wisconsin is only 3.3%, up slightly from a record low of 2.8% last spring.

It's a paradox. The labor shortage is keeping many Wisconsin businesses from growing, but it may also help buoy the economy in a downturn.

Founded in 1911, Wisconsin Manufacturers & Commerce (WMC) is the combined state chamber of commerce, state manufacturers' association, and state safety council. With nearly 3,800 members, WMC is Wisconsin's largest business association representing employers of all sizes and from every sector of the economy.

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Wisconsin Grocers Association

It's the Workforce, Duh

By Brandon Scholz, WGA President and CEO

For grocers, it has been an incredible gauntlet from the beginnings of the pandemic in 2022 to the peek over the 2023 precipice.

The challenges created for grocers and their suppliers as the pandemic lodged itself into the daily business operations have only continued to create hurdles for the industry.

As most grocery store shoppers know, not all shelves are full of their favorite products — shoppers have had to deal with substitutes or alternatives.

Throughout all these topsy-turvy, head-spinning challenges, there is one common denominator that bears most of the blame for what drives grocers crazy.

Workforce.

Simply put, there are not enough people available to fill the jobs open today, nor in the years to come. Reports have suggested the workforce population in Wisconsin is flat and likely to decline. *Forward Analytics* notes Wisconsin's youth population has declined 4.3% since 2010 and says a decline in the state's under-18 population will causes economic problems. That same report forecasts that by 2030, the working population will be down by 130,000 people.

Grocers, convenience stores, and retail businesses report there simply is not a pool of people in the workforce that can fill the gaps. And, for those who want to suggest otherwise that all is good because unemployment is low and UI applications are down, that's not necessarily the case.

There are all sorts of reasons why the workforce is running on empty. During the pandemic, people chose not to work; were let go by employers who couldn't keep their doors open; received state and federal assistance to make up for their non-employment status; as well as other factors.

Confounding the employment factor is the regressive impact of inflation that has chewed up most all the incredible and eye-popping increasing in wages and benefits.

Rolling into 2022, with the government giving assurances that the economy was in good shape (inflation not withstanding), the expectations were that people would come back to their jobs, or any job.

Not so. Didn't happen. Not only did people not show up, but the pool of prospective employees was more like a very small pond.

The forecast for 2023 doesn't look much better. You may find grocers taking down a checkout lane and adding a self-checkout stand to help their customers move through the end of their shopping experience.

What's the solution? Wisconsin needs to bring people back to Wisconsin to work here. The question is how.

Let's target quality of life issues in Wisconsin and focus legislative, employer, and community efforts on several key areas. Good businesses, strong communities, safe streets and less crime, daycare, housing, public transportation, and good schools are key components of attracting new workers to Wisconsin.

These changes will require funding solutions, regulatory relief, and legislative initiatives in local, county, and state governments.

Grocers and their customers are resilient. They've proved it since the pandemic started. It doesn't mean that things are hunky dory, but we're approaching critical mass. Changes must be made to solve our workforce crisis.

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Winsight Grocery Business notes that inflation, technological advances, and the pandemic have influenced grocery shopper habits. It's a common sight to see shoppers using smartphones to look up sales, product information, loyalty apps, and more.

While these changes have become common place for the customer, they are not long-term solutions for the retail world.

It starts with the workforce and quality of life.

The Wisconsin Grocers Association represents nearly 1,000 independent grocers, retail grocery chain stores, warehouses and distributors, convenience stores, food brokers, and suppliers. Wisconsin grocers employ over 50,000 people with more than $1 billion in payroll and generates more than $12 billion in annual sales in Wisconsin resulting in approximately more than $800 million in state sales tax revenue. Visit wisconsingrocers.com.

Wisconsin Technology Council

Recession or No, Wisconsin Tech Sectors Can Move Ahead in 2023

By Tom Still, WTC President

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Call it the "Great Reset." After years of predictably robust growth, technology stocks rebooted in 2022 and disrupted public markets all the way down. The question is whether technology stocks — specifically, Big Tech — will climb back in 2023.

The answer is "probably," but not right away. Both the Nasdaq-100 and the S&P 500 are tech-heavy at the top, and 2022's major value rundowns took place as the tech industry came to grips with too much growth, too fast. Much of that pain may be past. Moreover, tech stocks historically do well in the recovery phase of a recession rather than leading up to one.

> "Wisconsin has yet to adopt a plan for how to place more electric vehicle charging stations. It's currently 43rd out of 50, according to *Governing* magazine."

The Wisconsin economy is increasingly intertwined with what's happening in tech markets. Companies such as *Microsoft*, *Amazon*, *Google*, and *Tesla* all have a presence in the state in one form or another, especially with the advent of remote work. That neighbor who you thought was a stay-at-home mom may well be a software coder.

Whether it brings a full-fledged recession or an economic course correction, the year ahead is a time to seize opportunities to make Wisconsin even more open to tech-based businesses and workers. Some examples:

» Wisconsin should take the next step in seeding the clouds for a private-public "fund of funds." Out-of-state venture capitalists are increasingly finding solid deals in Wisconsin; earlier state pump-priming is working; the research base is here; and a huge state budget reserve should create room for a state investment that levers private dollars. Out-of-state investors will continue to be attracted by strong deals, but also by the state's willingness to show confidence in its own startup expertise.

» Wisconsin is positioned to take advantage of changes in energy and other technologies that can make the world more resilient in the face of climate change. Innovation in solar and wind energy will continue — so long as the grid keeps up with the demand. Storage technologies are a sweet spot; nuclear fission and fusion may help in the long run; some industries see a future in hydrogen energy; and the state is a center for freshwater technology innovation. Can migrating "climate refugees" to fill workforce holes be too far off?

» With better incentives, the state could see an influx of industrial research, data centers (which use a lot of water, by the way), and even video game development. The Columbus, Ohio, region won the *Intel* semiconductor production fight, but there may be more chip-making chances to come.

» There are myriad ways to mess things up, of course. Beating up the healthcare industry over costs alone is a bad strategy in an era when people move for jobs and lifestyle, which includes high-quality health care. Not recognizing the economic value of higher education is a similar mistake. If there's one thing about the Minnesota economy that makes it more attractive to site selectors, it's the significantly higher percentage of people with post-high school degrees. Wisconsin also has yet to adopt a plan for how to place more electric vehicle charging stations. It's currently 43rd out of 50, according to *Governing* magazine. Finally, don't scrimp on the state's research and development future by making it too hard to build academic science and engineering buildings. When Wisconsin delays, its competitors forge ahead.

> "Whether it brings a full-fledged recession or an economic course correction, the year ahead is a time to seize opportunities to make Wisconsin even more open to tech-based businesses and workers."

The Wisconsin Technology Council is the independent, non-partisan science and technology advisor to the governor and the Legislature.

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Wisconsin REALTORS® Association

Housing Market Slows as Demand Cools and Inventory Remains Tight

By Michael Theo, WRA President and CEO
*With insights from **Dave Clark**, economist with Marquette University*

After two straight years of record home sales, the Wisconsin existing home market slowed significantly in 2022. This was a result of both declining demand and continued weak housing supply. Demand slowed in part because the economy weakened slightly in the first half of the year. Specifically, the real (inflation adjusted) GDP fell 1.6% in Q1 of 2022, and it slowed 0.6% in Q2 before rebounding by 2.9% in the third quarter. Still, the labor market remained at full employment which likely presented the National Bureau of Economic Research from classifying the slowdown as an official recession. What really slowed demand was the rapid decline in housing affordability. In October of 2021, a Wisconsin buyer with median family income qualified to buy 201% of the median priced home in the state, assuming a 20% down payment and the remainder financed by a 30-year fixed-rate mortgage at the rates that existed at that time. Just 12 months later, that same buyer would only qualify to purchase 136% of the median priced home. Although median family income was estimated to have grown by 6.2% over that 12-month period, that was offset by a 6.1% increase in the median housing price, and a more than doubling of the 30-year fixed rate mortgage, from 3.07% in October 2021 to 6.90% in October 2022. Weakness on the supply side only exacerbated the problem with total listings in October 2022 down 24% compared to that same month in 2021. Overall, through the first 10 months of 2022, home sales were off their 2021 pace by 11.2%. Even though sales have weakened significantly, this remains a strong sellers' market with just 2.6 months of available supply in October 2022, which is well below the six-month benchmark that signals a balanced housing market.

> "The Fed has indicated that it intends to keep raising short term rates until inflation is under control, even if its actions lead to a recession."

One reason the mortgage rate rose so quickly is because inflationary expectations, which lenders must consider when extending long-term credit to homebuyers, have increased in the past year. That is, inflation is no longer viewed as transitory. As a result, the Fed has taken decisive action to slow the economy and reduce inflation. The Fed's primary tool to slow inflation is to increase the short-term federal funds rate, which is the rate that member banks lend to each other to cover overnight reserve shortfalls. Specifically, the upper limit of the federal funds target range rose from near zero (i.e., 0.25%) at the beginning of 2022 to 4% by early November. The good news is that there has been some slight improvement in headline inflation, which peaked in June 2022 at 9.1% and fell to 7.7% by October. Hopefully that trend continues. Still, inflation remains well above the Fed's target inflation rate of 2% and the Fed has indicated that it intends to keep raising short term rates until inflation is under control, even if its actions lead to recession. Given that the U.S. and Wisconsin labor markets are currently at full employment (i.e., both were under 4% in October), we expect the Fed to continue its upward movement of the federal funds rate. Until inflationary expectations are lowered, mortgage rates will remain elevated and affordability will remain low. This, combined with tight inventories, will constrain the housing market in 2023.

> "Clearly the Fed is committed to controlling inflation, but Congress and the Biden Administration need to avoid exacerbating the inflation problem through irresponsible spending practices."

Nationally, policymakers need to maintain their focus on the inflation problem. Clearly the Fed is committed to controlling inflation, but Congress and the **Biden** Administration need to avoid exacerbating the inflation problem through irresponsible spending practices. While there is little that local policymakers can do to stimulate the demand side of the housing market, they can help set the stage for new construction once the housing sector begins to improve. This includes lowering the regulatory burden and helping to foster growth in training in the building trades.

Founded in 1909, the Wisconsin REALTORS® Association (WRA) is one of the largest trade associations in Wisconsin. It represents and provides services to more than 15,000 members statewide. WRA's goal is to promote the advancement of real estate in Wisconsin and provide cutting-edge tools to help REALTORS® enjoy a successful career and be competitive in their market.