

ECONOMIC UPDATE FOR LFMA

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Presenter introduction

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Nonprofit

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ECONOMIC OUTLOOK

Nonprofits Enter 2023 With Inflation Cooling and Job Market Still Strong

By *Sara Herschander* | JANUARY 23, 2023

Bloomberg

US Edition

Live Now Markets Economics Industries Technology Politics **Wealth** Pursuits Opinion Businessweek Equality Greer

Wealth

Credit Suisse’s Collapse Reveals Some Ugly Truths About Switzerland for Investors

- Nation has long traded on its image as a bastion of certainty
- Law professor says Swiss made to look like a ‘Banana Republic’

Forbes

Sticky Wages, Stickier Inflation

RSM

Our Task: Separate Signal From Noise

SIGNAL



NOISE



Big-picture changes in the U.S. economy

Moving from pre-pandemic financial and real economy conditions to "what comes next"

1995–2020 pre-pandemic and pre-war era	Post-pandemic economy
Insufficient aggregate demand	Insufficient aggregate supply
Excess savings	Liquidity constraint
Hyper-globalization	Dichotomy of globalization Re-globalization/regionalization Industrial policy: Infrastructure buildout and energy transformation Digital globalization intensifies
Low inflation	High inflation
Low interest rates	Higher interest rates
Plentiful labor	Demographic constraints: Less labor

What We Know: The U.S. Economy

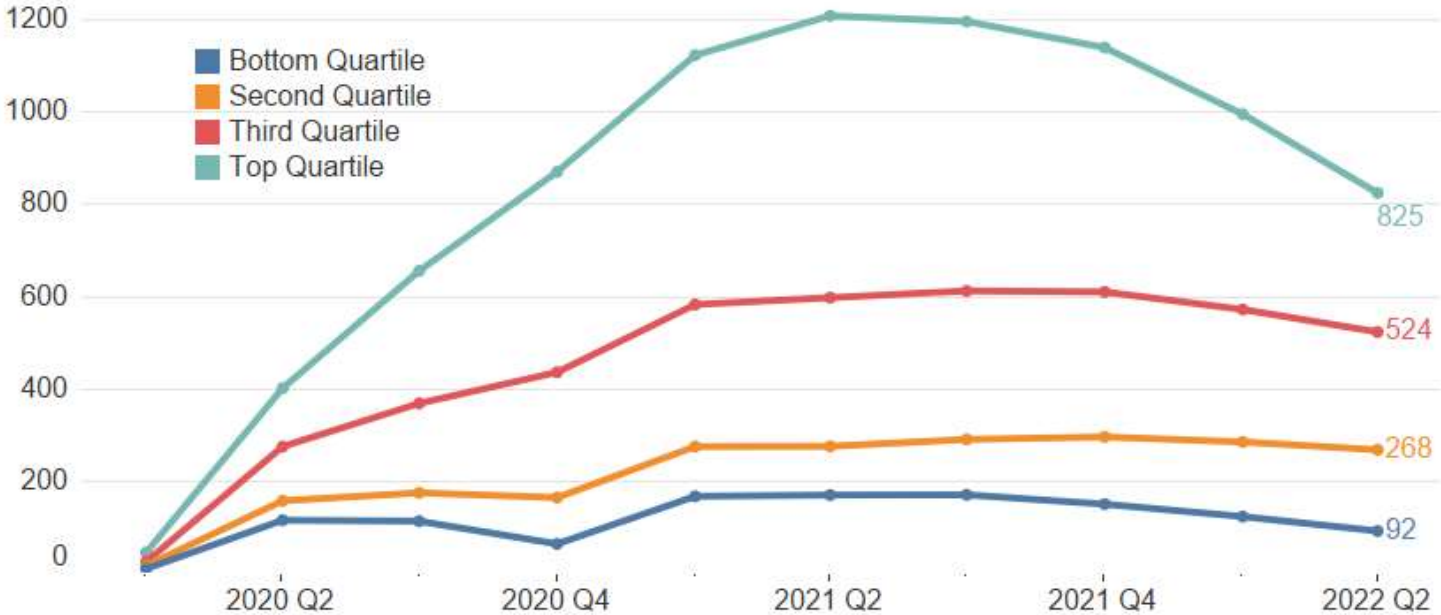
1. Nonprofits and the economy generally were in great financial shape at the end of 2021.
2. Inflation took hold in 2022, lagging from pandemic actions and global shocks.
3. Because of this, the Federal Reserve has taken action to slow the economy, including raising interest rates. This has had many knock-on effects.
4. Nevertheless, many elements of the economy remain strong.



US Consumer Spending: Composition of Savings

Cumulative excess savings since Q1-2020 by income quartile

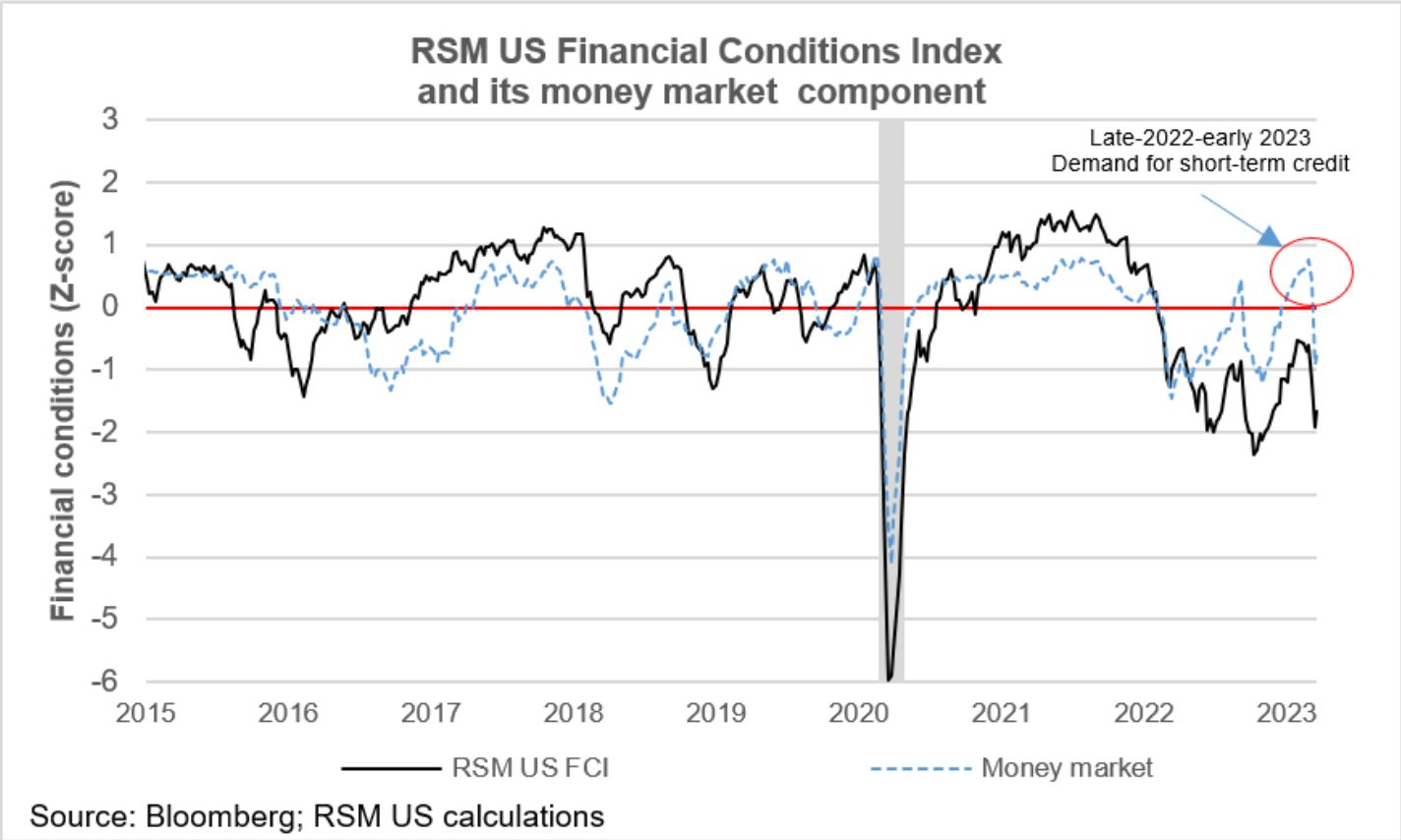
Billion \$



Source: BEA, Federal Reserve, RSM US

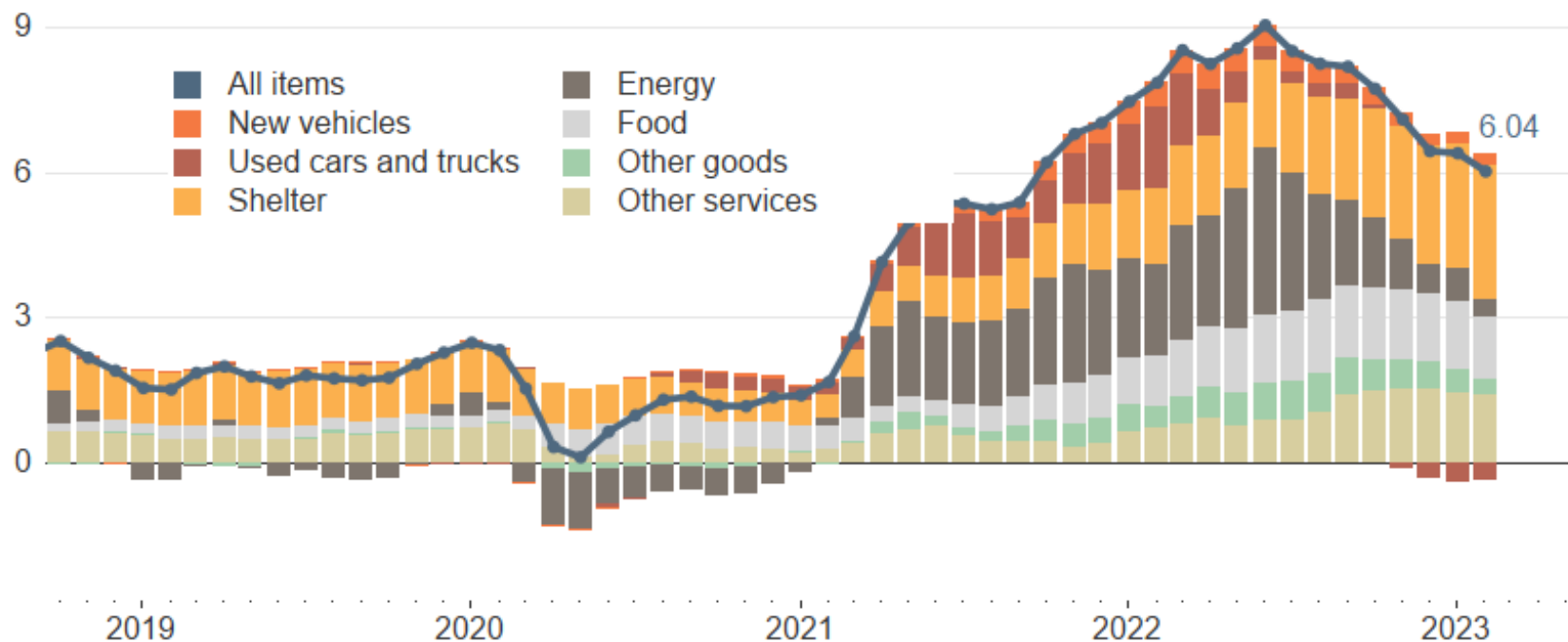


RSM Financial Conditions Index



Year-over-year CPI changes

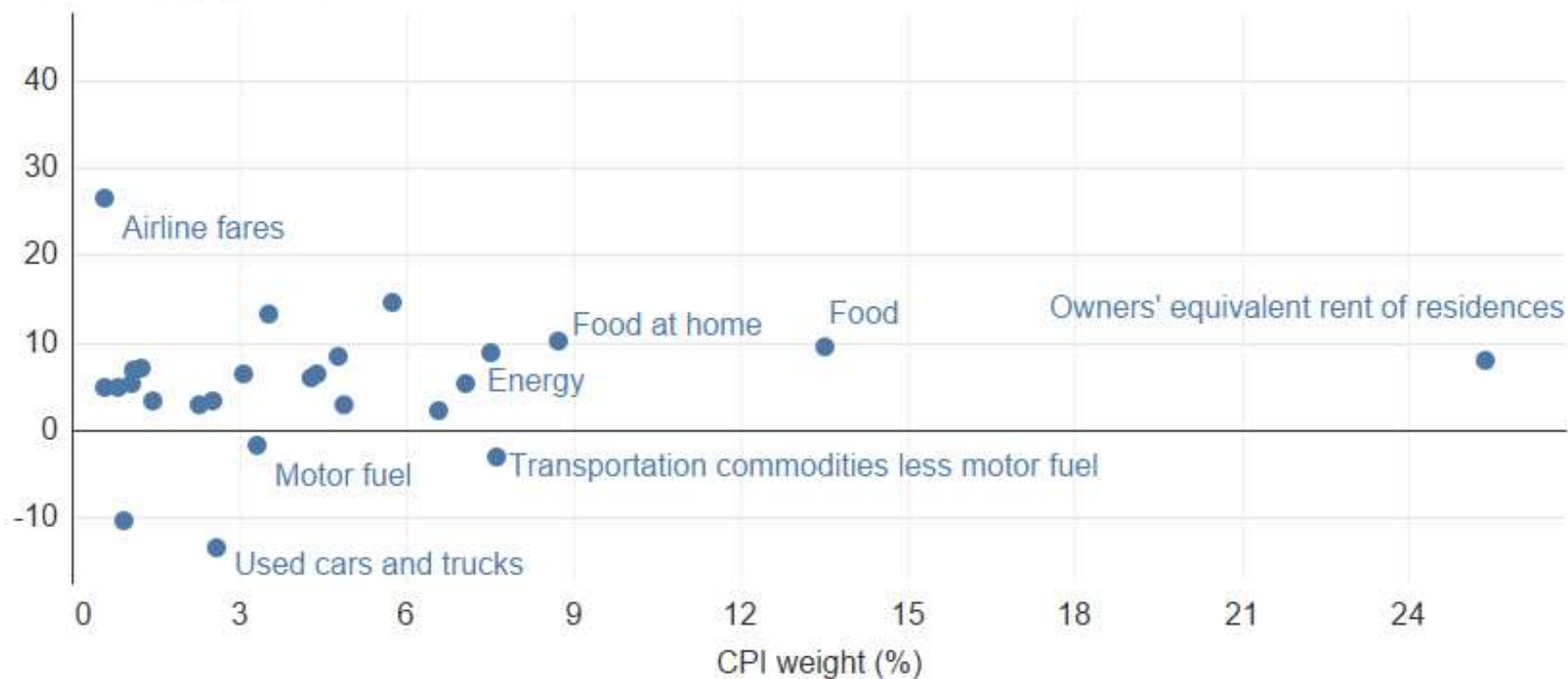
With main component percentage contribution; seasonally adjusted



Source: BLS, RSM US

Year-over-year CPI changes

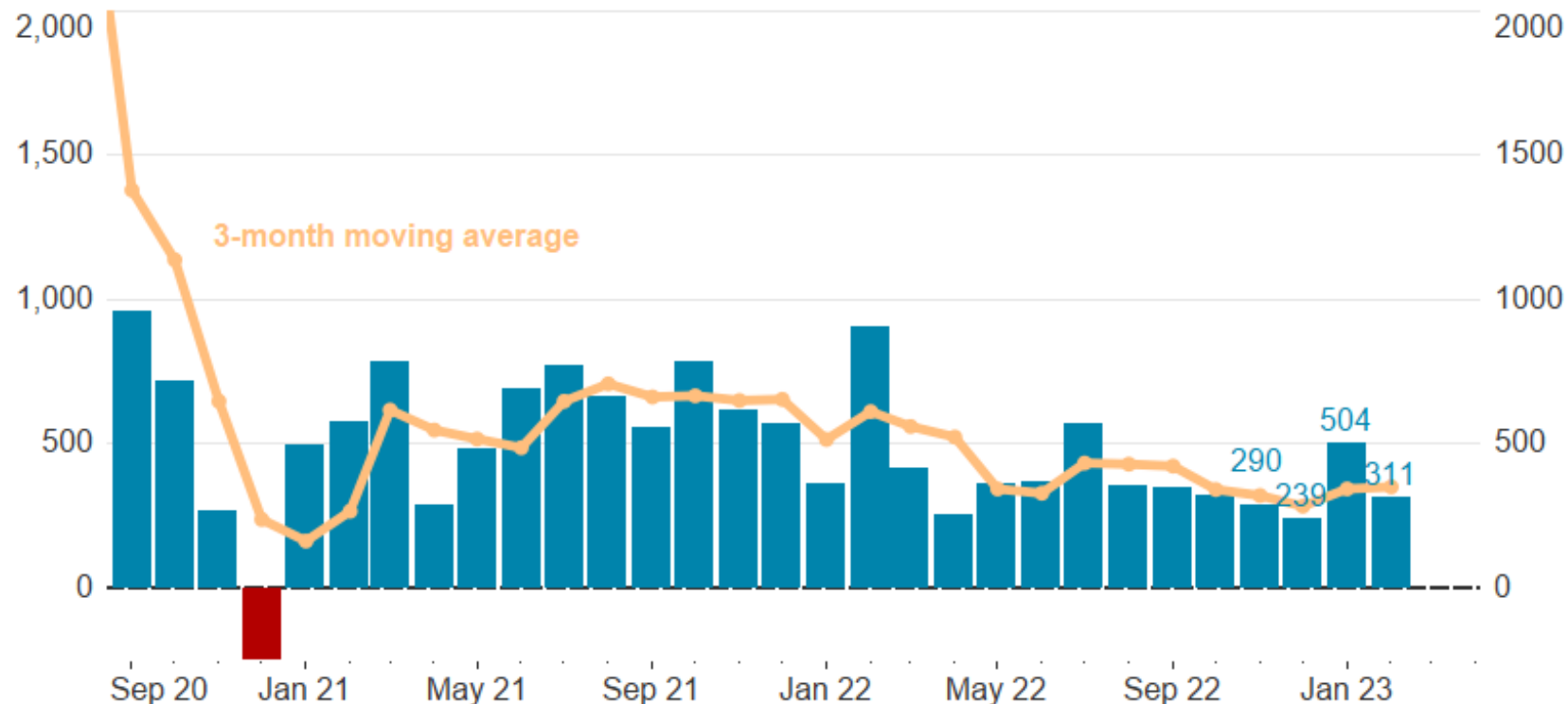
% YoY change, NSA



Source: BLS, RSM US

Change in nonfarm payrolls

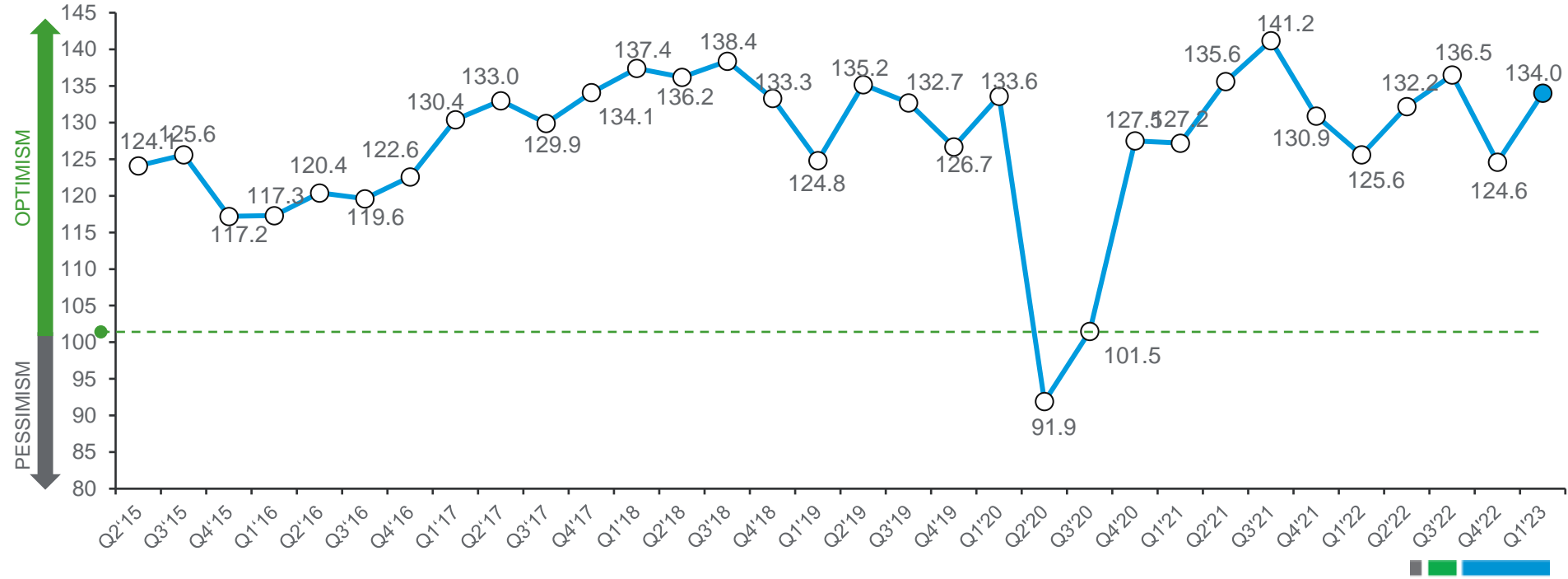
Monthly job gains, in thousands



Source: Bloomberg, BLS, RSM US

The RSM US Middle Market Business Index in Q1'23 is statistically more optimistic when compared with Q4'22

MIDDLE MARKET BUSINESS INDEX
(Seasonally Adjusted)



Further MMBI optimism

Business is improving in the middle market ...

53%

of respondents reported an increase in gross revenues, up from 42% in the final quarter of last year.

49%

of participants reported an increase in net earnings.

... and prospects remain strong ...

57%

expect an increase in both gross revenues and net earnings through the middle of the year.

... while the view of the overall economy is positive.

47%

said that the economy had improved, up from only 28%.

41%

expect it to improve over the next six months.



What We Expect: The U.S. Economy

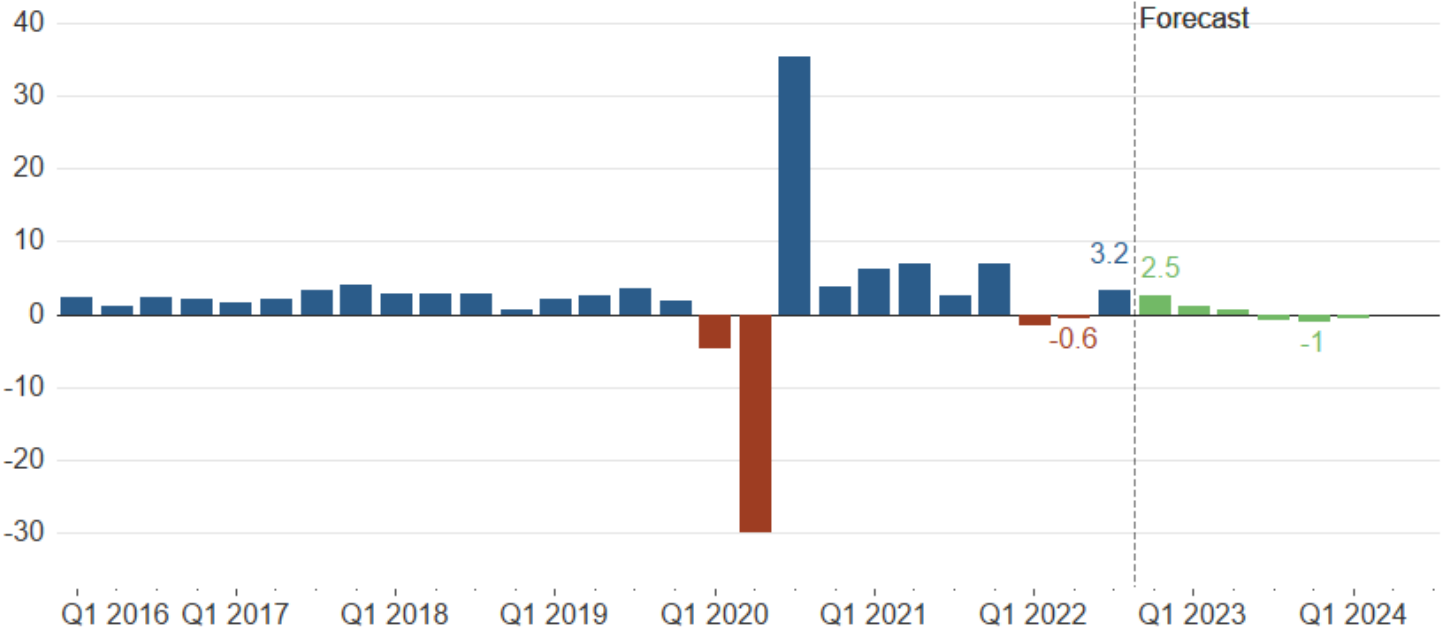
1. The U.S. economy will enter into recession in the latter half of this year.
2. Interest rates will increase slightly, then hold at that level.
3. Unemployment will rise, but not catastrophically.
4. The world will never be the same.



US GDP: Economy Still Expanding

U.S. real GDP growth

Quarter-over-quarter %, seasonally adjusted annualized rate

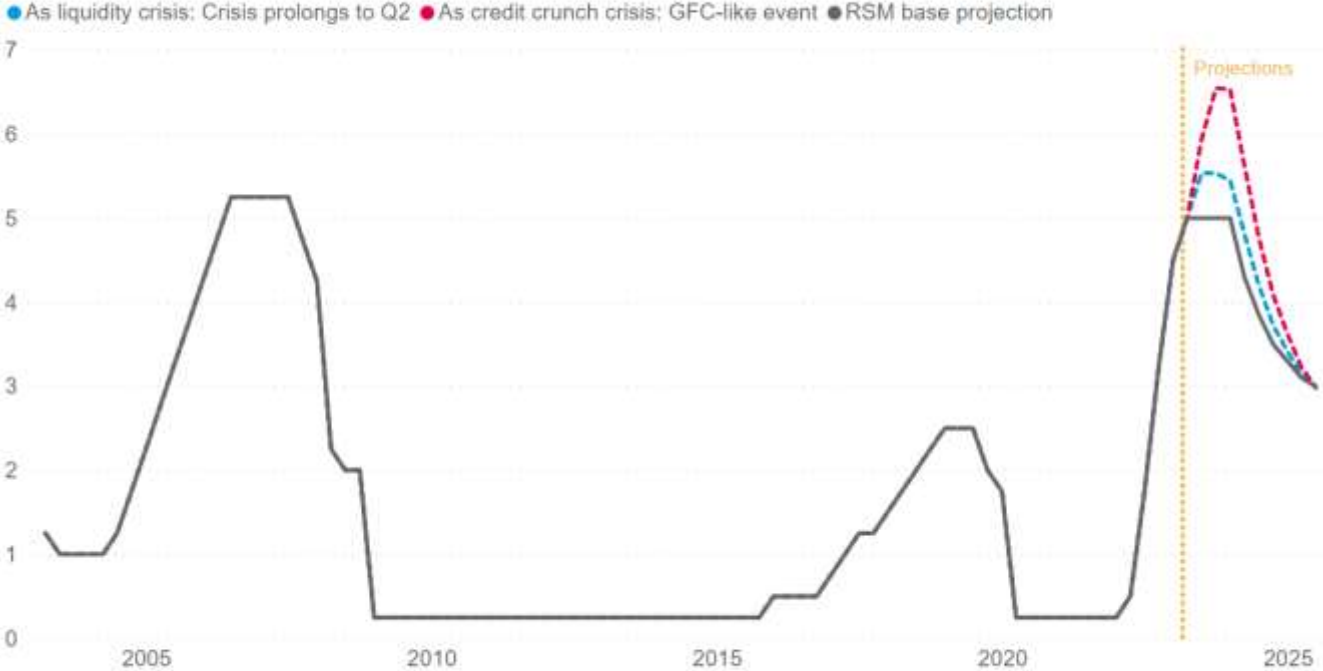


Source: Bureau of Economic Analysis, RSM US



Scenarios: Interest Rates and Inflation

How high rates would have to rise to achieve the same inflation impact



Source: Federal Reserve, RSM US

Scenarios: Unemployment and Inflation

Our base case: How much unemployment must rise

Unit = percentage

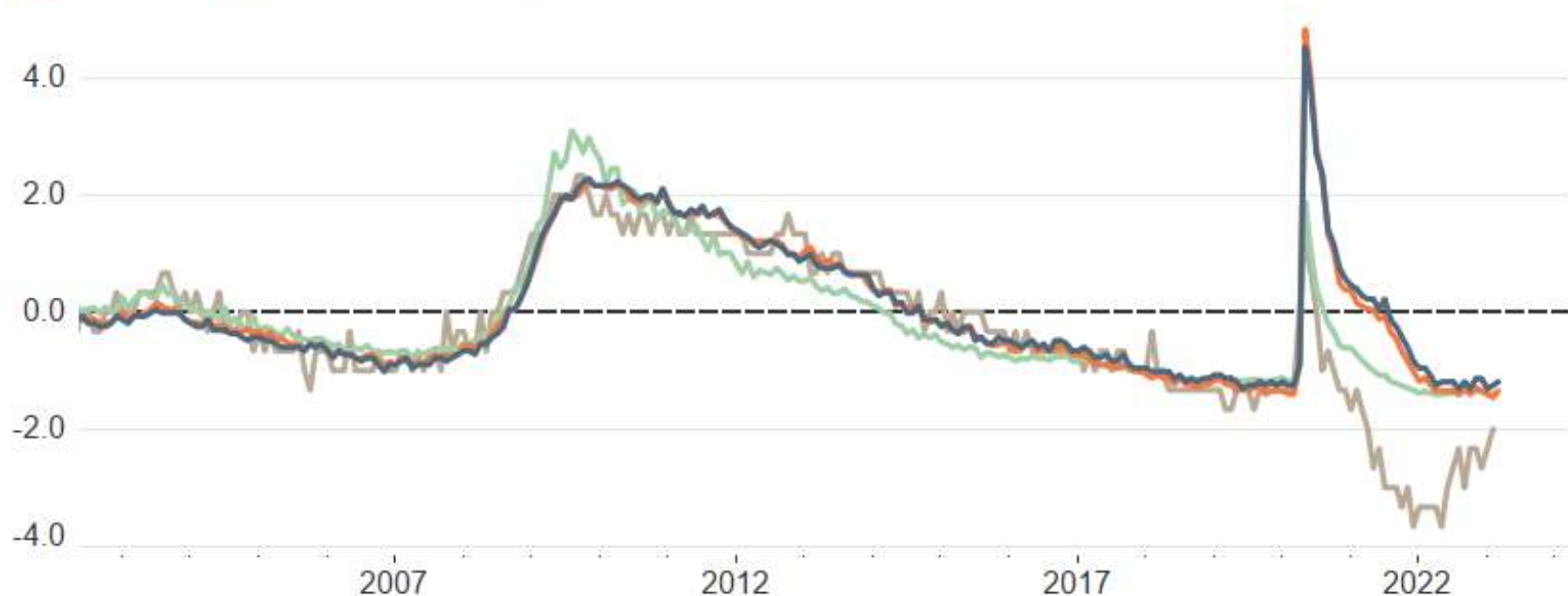


Source: BLS, CBO, RSM US

Measures of labor market tightness

Calculated using z-score based on mean and standard deviation from 2001 to 2019

- Unemployment rate (prime-age)
- Unemployed per job opening
- Unemployment rate (U-3)
- Reverse quit rate



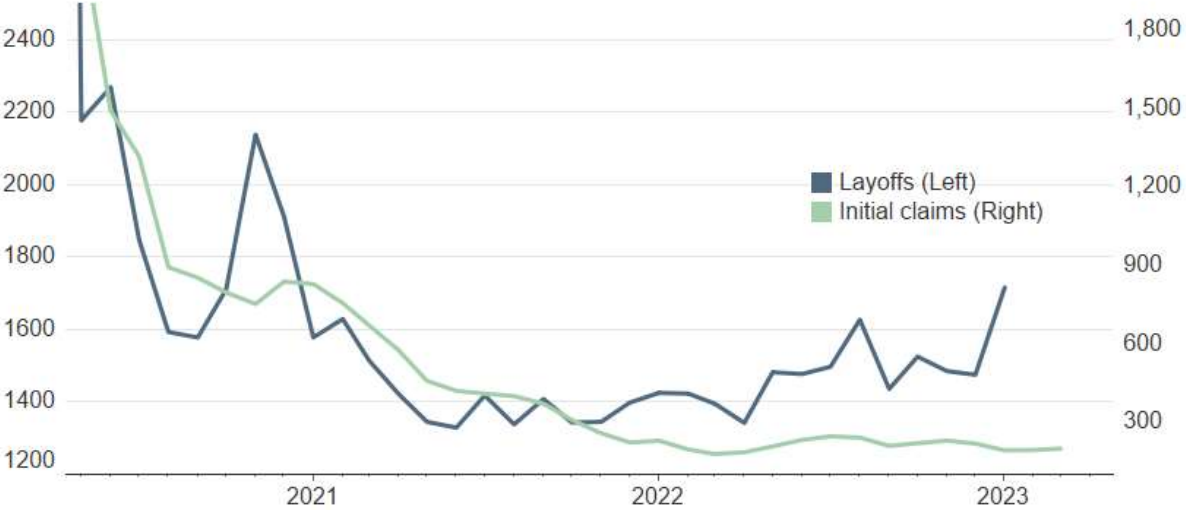
Note: Values below 0 indicate more tightness than neutral. The reverse quit rate is calculated as 1 minus the quit rate.

Source: BLS, RSM US

Layoffs picking up

Initial jobless claims vs. layoffs

In thousands



Source: Labor Department, RSM US

Remote work is here to stay



- What began out of necessity early in the pandemic **has become a preference** among workers.
- Facing a tight labor market, **employers have had little choice** but to accommodate workers' demands for flexibility.
- Larger middle market firms have **handled the transition better**, both from a technological and human resources standpoint.
- Remote work allows businesses to **source talent from a bigger geographical area**.

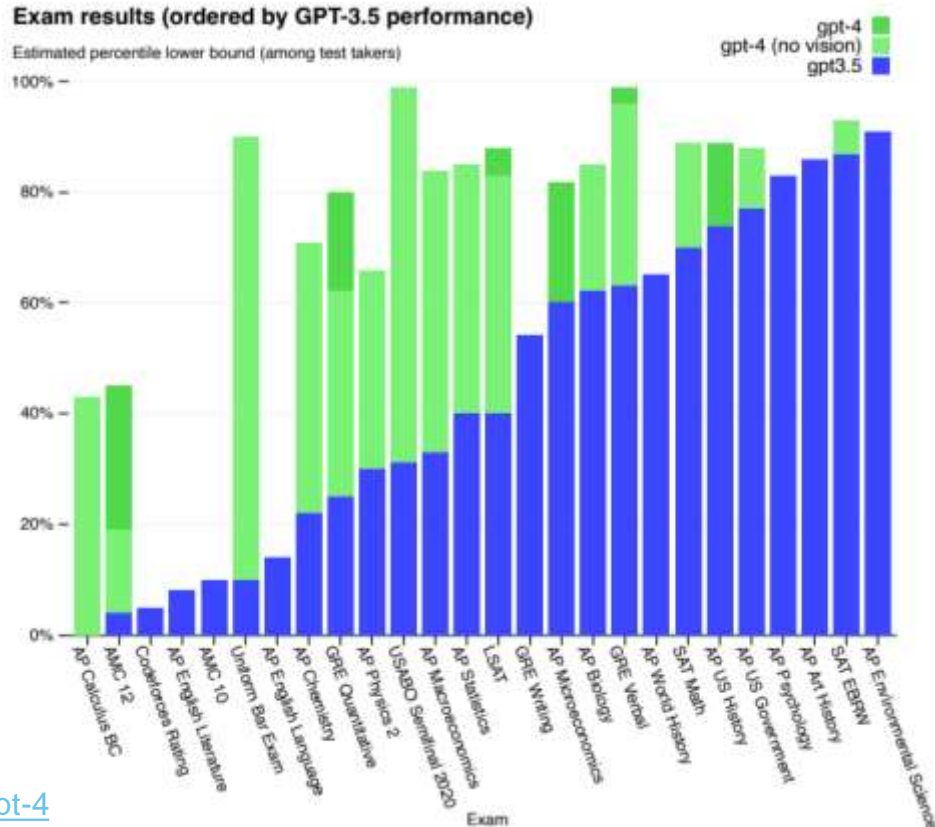
Unleashing the power of artificial intelligence

1. Automation
2. Customer service
3. Personalization
4. Predictive analytics
5. Cost reduction



Source: <https://technologyblog.rsmus.com/data-analytics/unleashing-the-power-of-artificial-intelligence-for-middle-market-businesses-how-openai-can-drive-growth-and-efficiency/>

AI is not the future, it is now

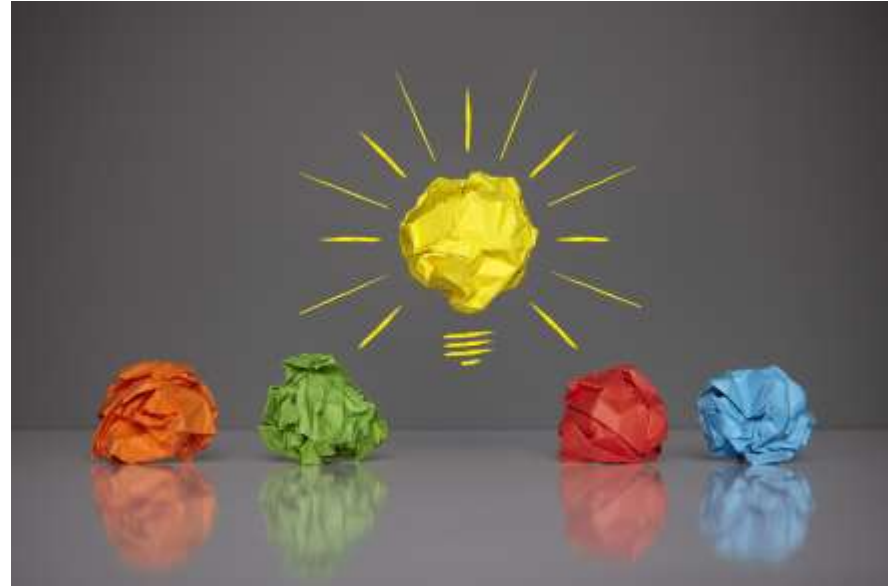


Source: Open AI, *GPT-4 Technical Report*.

<https://openai.com/research/gpt-4>

What This Means for Nonprofits

1. Recession is likely, but not long or deep – continue to invest.
2. Lower income households are hit worst by inflation and unemployment, creating more need and less ability to give.
3. Higher income households remain in solid financial condition, have excess savings.
4. Shrinking endowments and grantmaking portfolios will restrict philanthropy at least through 2024.
5. Labor shortages will persist for nonprofit organizations.





QUESTIONS?

THE POWER OF BEING UNDERSTOOD

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