ECONOMIC AND INDUSTRY FORECAST FOR 2023

DOOR AND ACCESS DEALERS SHOULD PREPARE FOR TURBULENCE

By Phillip M. Perry

After two years of frenetic activity fueled by a post-pandemic recovery, door and access dealers should expect a tougher operating environment in 2023. Growing headwinds include rising inflation, higher interest rates, a softening housing market, continuing supply chain disruptions, declining capital investments, and escalating costs for wages and energy.

"2023 is likely to be a challenging year for retailers," said Scott Hoyt, senior director of consumer economics for Moody's Analytics. "We are projecting growth of only 2.8%, well below the sector's historic 4.3% average."

Dismal numbers

The forecast represents a significant decline from the 8.3% increase expected for 2022. The recent trend is well below 2021's 17.5% increase.

"Of the many factors weighing on growth, the biggest will be a slowdown in inflation, since retail activity is measured in nominal terms," said Hoyt. Moody's Analytics forecasts that by the end of 2023 inflation will have declined from its recent 8% pace to 2% according to the Federal Reserve.

Price increases aren't the cure-all

Inflation can be a double-edged sword. It helps raise merchandise prices while simultaneously dampening shopper behavior. As a result, businesses will be hurt by a decline in inflation over the coming 12 months, and rising prices have not been the remedy they hoped for in 2022.

In addition, shopper psychology remains as unsettled as it was a year ago. "It's hard to get a handle on consumer confidence right now," said Hoyt. "If you ask people about their finances and they think about the stock market or gasoline prices compared to a year ago, they're really depressed. If you ask them about the labor market and their job situation, they're feeling pretty good."

Company profits will take a hit

Other factors that will weigh on retail activity in 2023 include the loss of helpful economic initiatives. "Government stimulus packages, ultra-low interest rates, and strong money supply creation had been helping to compel business activity until mid-2022," said Anirban Basu, chairman and CEO of Sage Policy Group. "All those fundamentals have been inverted."

According to Bernard Yaros Jr. of Moody's Analytics, the Real Gross Domestic Product (GDP) is expected to increase by 0.7% in 2023. "The projection for 2022 is 1.7%. Both figures represent much slower activity than the 5.9% increase of 2021." GDP, the total of a nation's goods and services, is the most commonly accepted measure of economic growth. "Real" GDP adjusts for inflation.

The slowdown in the overall economy should have a depressing effect on corporate profits. Moody's Analytics projects corporate projects to increase at a 5.2% clip in 2023, which is a decline from the 7.9% figure anticipated for 2022. Both estimates are much lower than the 25% increase of 2021.

Healthy employment

Reports from the field support the analysis of economists. "In the first half of 2022, many of our member companies were still experiencing high demand," said Tom Palisin of The Manufacturers' Association in York, Pa. "But as the year progressed, there was a significant slowdown caused by the labor shortage, inflationary issues, and global events."

The good news is that strong employment conditions is helping to alleviate the negative impact of the economy. Moody's Analytics predicts an unemployment rate of 4.1% by the end of 2023. Many economists label a rate between 3.5% and 4.5% the "sweet spot" that balances the risks of wage escalation and economic recession.

Wages remain high

High employment levels tend to spark wage increases and more retail spending. "Wage rates, as measured by the Employment Cost Index (ECI), remain very high by the standards of the last couple of decades," said Hoyt.

A healthy 3.7% increase is expected in 2023, reflecting the strong growth of a tight labor market. "While we've had growth over 3% for the last three years, prior to 2020 the last time we had growth in the ECI of over 3% was 2007." On the flipside, higher wages increase operating costs, which can dampen profits.

Worker shortage woes

"Employers will be very focused on labor availability in 2023," said Yaros. When will the available workforce grow? According to experts, not anytime soon. "The labor market's going to be tight for years to come," said Bill Conerly, principal at Conerly Consulting. "The decade from 2020 to 2030 is expected to have the lowest growth of working age population since the Civil War. One reason is the retirement of the Baby Boomers; another is the low rate of immigration over the last few years."

Palisin agreed that a labor shortage is going to be a long-term condition, and said his members are making moves to lessen the effect. "Employers are trying to be creative in the way they keep and retain workers, not only by offering higher salary rates but also by extending benefits and encouraging work flexibility. They are also investing more in automation for labor-intensive tasks."

Interest rate effect

Another major factor affecting profits is a rise in interest rates — the Federal Reserve's favorite tool for fighting inflation. When interest rates increase, door and access businesses (and their net revenues) are directly affected.

"The purpose of increasing interest rates is to drive down demand," said Palisin. "Too many of our companies have lines of credit that rely on floating interest rates. Rising rates will take a hit to the bottom line as companies decide whether to utilize those lines of credit to support their cash flow and investments."

Lingering supply disruptions

"While supply chain problems have improved, there hasn't been the significant resolution we had hoped for," said Palisin. "Random shortages in materials and deliveries are still plaguing our members, and that's leading to backlogging of orders. Companies just can't get materials or parts."

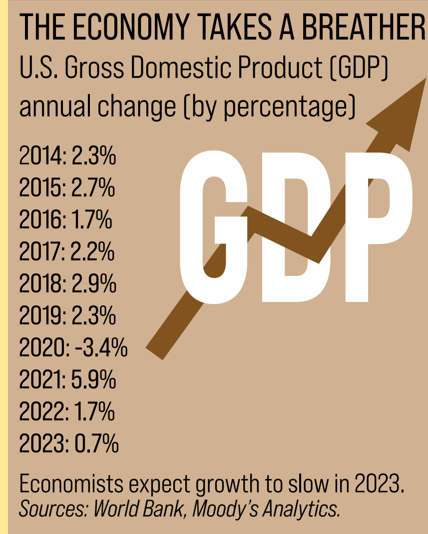
The Russia-Ukraine war has worsened the situation, noted Palisin. "The war has created an energy crunch and a disruption in raw materials from that region that have trickled through the economy to exacerbate supply chain issues." Companies are responding by expanding their sourcing from countries other than China.

Housing headwinds

New home buyers tend to shop, and that sector is also entering a period of correction. "The underlying dynamics of the housing market are changing as lower affordability spurred by higher prices and mortgage rates is weighing on demand," said Yaros.

The rise in home prices is discouraging consumers from signing on the bottom line. Median prices for existing single-family homes are expected to increase 11.5% when 2022 figures are finally tallied. That comes off a strong 18% increase in 2021.

2023 should bring some relief, as house prices are expected to decline by 2.6%. While affordability has sunk to its lowest level since late 2007, the 30-year fixed mortgage rate is nearing its highest level in over a decade, leading to a decline in purchase applications. A decline in new housing starts can only lead to a drop off in garage door sales.



Economists expect growth to slow in 2023.
Sources: World Bank, Moody's Analytics.

Housing starts and garage door sales

Tight housing supply is only adding to upward pricing pressure. The inventory of for-sale homes remains historically low, and new ones will be scarce. "We expect housing starts to fall by 1.8% and 2% in 2022 and 2023, respectively," said Yaros, "compared to a 15.1% increase in 2021."

There's only so much the industry can do to bolster housing supply — one big reason being the aforementioned labor shortage. "The unemployment rate for experienced construction workers is about as low as it's ever been," said Yaros. "Capacity limits have delayed housing completions and contributed to a record number of housing units in the pipeline."

Heads or tails?

"We are faced with a kind of two-sided coin," said Palisin. "The positive side represents strong current orders and a continuing need for more workers, while the negative side represents inflationary pressures and global headwinds."

Which side of the coin will show its face in 2023? Economists advise to keep an eye on the inflation rate, employment trends, and consumer spending. Basu said, "Inflation is the driver of near-and-medium-term economic outlooks." The second vital element is the employment picture. "Employers should watch for any emerging weakness in the labor market."

Finally, what about consumers? "Any softening of spending would point to a looming recession." ■

FORECAST SNAPSHOT

Most important variables affecting business confidence

- **Inflation.** Bumps up retailers' nominal sales but also undermines consumer confidence and spending.
- **Worker scarcity.** Owners are having to pay a lot to get employees, and turnover is high.
- **The post-pandemic shift.** People are spending more on travel, hotels, and restaurants, and less on goods.
- **Rising interest rates.** Higher rates is another depressant on shopper activity.
- **Recession risk.** There's a lot of talk about the high probability that the Federal Reserve won't get this right. A recession is never good for retailers.
- **Supply chain issues.** Delivery disruptions translate into higher costs for merchandise and higher inflation, which eats into real spending and consumer confidence.

Source: Scott Hoyt, senior director of consumer economics for Moody's Analytics.

Will we have a recession?

Phil Perry's article suggests an economic slowdown as the likeliest scenario for 2023. But what are the chances of a recession or an actual decline in business activity?

While Moody's Analytics sets the odds at 50-50, avoiding a recession will require a bit of luck. "The U.S. economy will enter 2023 being vulnerable to anything that might go wrong," said Bernard Yaros Jr. of Moody's Analytics. Risks such as a resurgence of the pandemic in China, a worsening of the Russia-Ukraine war, and another energy supply shock would hurt consumer pocketbooks.

Avoiding a recession will also depend on a couple of things going right, added Yaros. The ebullient labor market will need to cool down at a pace that softens wage increases without sparking economic turmoil.

Most important, the Federal Reserve will need to successfully tame inflation without allowing interest rates to spike the economy. Yaros, however, is optimistic. "We think inflation will steadily slow from more than 8% to a pace that is consistent with the central bank's 2% target by the end of 2023."