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Goldman Sachs Cuts GDP Forecast, Warns of Economic Hit From Bank Rout

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Goldman Sachs Group (GSG) slashed its U.S. GDP forecast and warned of an economic hit from recent bank failures.

The investment bank raised its estimate of the odds of an American recession on March 15, to 35 percent over the next 12 months due to increased concern over the economic impact of stress in the banking sector.

GSG warned of a cascade of effects throughout the economy in the aftermath of the collapse of Silicon Valley Bank and Signature Bank last week, the second- and third-largest bank failures in the U.S. history, respectively, only behind the collapse of Washington Mutual in 2008 during the during the financial crisis.

Economists led by Goldman's chief economist, Jan Hatzius, raised GSG's predictions of a slump from its previous estimate of 25 percent after the collapse of SVB.

However, the new estimate is still below the 60 percent average, according to economists surveyed by Bloomberg.

GSG's U.S. economic growth indicators still remain positive, with its business growth measures averaging at 52 in February, just above the 50-point line of negative activity, wrote Hatzius.

Hatzius cut Goldman's 2023 GDP forecast by 0.3 percent, and is now looking at full-year GDP growth of 1.2 percent.

"The macroeconomic impact of a pullback in lending will remain highly uncertain until the extent of the stress on the banking system becomes clear," said Hatzius.

Federal Regulators Try to Reassure Banking Sector

Federal regulators have been taking action this week to prevent a banking crisis and mass layoffs in the tech sector in the wake of the banking crisis which left many startups without access to their assets.

Goldman's real-time estimate on jobs data showed that the layoff rate rose to 1.2 percent, which is still historically low, while the gap between workers and available jobs declined to above the 2 million mark that economists said is needed to "rebalance the labor market."

Meanwhile, a joint statement from Treasury Secretary Janet Yellen, Federal Reserve chairman Jerome Powell, and FDIC chairman Martin Gruenberg on March 12 promised depositors that they would have access to all of their assets stored at the failed banks, after fears that the legal $250,000 insurance cap would prevent that.

No losses will be borne by the taxpayer, and any losses to the Deposit Insurance Fund to fully pay off uninsured depositors will be recouped by a special assessment on banks, they explained.

The Fed also made available additional funding to eligible lenders to help assure that they can meet depositor needs and prevent future bank runs.

More Bad News in Switzerland Adds to Fears of Pending Financial Crisis

The current banking crisis has also encouraged swaps traders to bring forward expectations for a reduction in interest rates by the Fed.

Borrowing rate hikes have led to a sudden shift in the bond markets, which is partially being blamed for causing SVB and Signature to fail.

Investors' worries about systemic financial stress on the banking sector have further escalated after the stock of Credit Suisse Group AG fell 30 percent on March 15, hitting a new low.

This came after its largest shareholder, Saudi National Bank, declined to provide further financial support, owing to regulatory issues, forcing Credit Suisse to try and reestablish confidence, albeit with little results.

Switzerland's second-biggest bank reported that fourth-quarter customer outflows rose to more than $120 billion.

Hatzius said that the constant news of negative headlines in the banking industry could cause a slow down in lending and thus weaken economic growth.

"U.S. policymakers have taken aggressive steps to shore up the financial system, but concerns about stress at some banks persist," Hatzius said.

"Ongoing pressure could cause smaller banks to become more conservative about lending in order to preserve liquidity in case they need to meet depositor withdrawals, and a tightening in lending standards could weigh on aggregate demand," he added.