US economic outlook October 2024

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The US economy is gently decelerating from a very robust pace of growth due increased private sector prudence, but Fed easing should buffer the slowdown

Outlook

Recent economic data confirms the US economy remains on solid footing ahead of the general elections. Upward revisions to income growth and historically robust productivity growth remain the key pillars to the US economic outperformance while selective consumer prudence in the face of high prices continues to drive disinflation. What appears to be unfolding before our eyes is a soft-landing scenario only the most optimistic dream of. With hurricanes and strikes likely to inject volatility in economic data in coming weeks, Fed officials will likely revert to policy gradualism following an "catch-up" rate cut of 50 basis points (bps) in September.

Looking ahead, we foresee consumers and businesses still spending but doing so more prudently amid still-elevated costs and rates. We continue to expect a bifurcated consumer spending outlook with lower-income households with larger debt burdens exercising more spending restraint while families at the higher end of the income spectrum still spending, albeit with more discretion. We foresee real GDP growth averaging 2.7% in 2024 and easing to 1.9% in 2025 but note the unusually elevated level of uncertainty dependent on the election outcome.

Slower but resilient labor trends

An above-trend 254k payroll gain in September and a decline in the unemployment rate to 4.1% indicate labor market conditions remain generally healthy, characterized by slower labor supply absorption rather than broad-based layoffs. We expect business leaders will continue to curb wage growth, hire with caution and proceed with strategic layoffs to contain costs heading into 2025. We foresee the unemployment rate rising further toward 4.4% by year-end and reaching 4.5% in 2025.

Polarized and prudent consumers

The stronger-than-expected September retail sales report capped a quarter of solid growth for consumer spending and confirmed that households are spending more prudently but not retrenching, thanks to resilient personal income momentum. On average, household finances remain healthy even if increased polarization is evident. Lower-income and younger families are gradually more constrained by elevated debt financing costs and rising delinquencies while older generations and higher-income households have more fixed-rate debt and therefore are less burdened by elevated debt servicing costs. We foresee gradually cooling consumer

spending growth from 2.6% in 2024 to 2.0% in 2025 as slower employment growth weighs on income trends and prices and rates remain generally elevated.

Continued disinflation

While Consumer Price Index (CPI) inflation eased less than expected in September, the combination of selective consumer spending, increased pricing sensitivity, reduced markups, moderating wage growth and cooling rent inflation should continue to drive a healthy disinflationary impulse heading into 2025. We foresee headline CPI inflation closing the year around 2.4% and core CPI inflation just below 3.0% in December, but we note the risk from rising tensions in the Middle East pressuring oil prices and pushing up shipping and transportation costs.

Gradual easing cycle

The Federal Open Market Committee (FOMC) voted to cut the federal funds rate by 50bps to 4.75%–5.00% at the September meeting. Given broad-based uncertainty as to the degree of policy restrictiveness and the level of the neutral rate of interest, most policymakers will likely favor reactionary policy gradualism as their modus operandi. While the cacophony of Fed speeches has given conflicting signals as to the Fed's reaction function — with the most hawkish policymakers even hinting at a pause in November — Fed Chair Jerome Powell has stressed that policy gradualism will prevail through year-end. We remain of the view that the Fed will cut interest rates by 25bps at every meeting through June of next year. This would translate into 50bps of additional rate cuts by year-end and another 100bps in H1 2025 putting the fed funds rate at 3.4% in June 2025.

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