US GDP (Q4 2024 – first estimate)

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Strategy realized

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Goldilocks economy to end 2024

- Real GDP grew a robust 2.3% annualized in Q4 2024, following an impressive 3.1% expansion in Q3. For the full year, GDP rose 2.5%, surpassing even the most optimistic forecasts from late 2023.
- Real final sales rose 3.2% while inventories subtracted a substantial 0.9 percentage point (ppt) from GDP growth. Consumer spending once again drove the gain with an impressive and broad-based 4.2% advance — the strongest since Q1 2023. Business investment contracted 2.2% led by a significant plunge in equipment investment while residential investment rebounded 5.3%. Net trade was neutral for GDP growth with exports and (surprisingly) imports contracting in sync. Government spending 2.5% with federal outlays modestly outpacing state and local spending.
- What are the main takeaways?
  - Domestic demand remained strong through 2024, with final sales to private domestic purchasers rising 3.0% year over year (y/y) in Q4.
  - Despite a "bump in the road" in Q4, inflation is still converging toward the Federal Reserve's 2% target with minimal economic disruption.
  - The Fed opted to hold rates steady in January but remains open to further policy easing if inflation convincingly and sustainably eases. We believe a March rate cut remains on the table.
  - Policy changes in regulation, immigration, trade and taxes are unlikely to impact the economy until the second half of 2025, but rising policy uncertainty could create financial market pressures and private sector stress despite the pro-business vibes.
- While economic momentum entering 2025 remained strong, the economy is expected to gently ease toward its 2%-trend pace in the coming quarters. Consumers will continue to spend, but at a more moderate clip as they continue to adjust to a higher price and interest rate environment. Cooler final demand growth means that businesses will continue to strategically manage their workforce while focusing on productivity enhancements to offset lingering cost pressures.
- Importantly, the outlook is clouded by heightened policy uncertainty. We anticipate a full extension of the Tax Cuts and Jobs Act, a reduction in net immigration from 1.1m pre-pandemic to 900,000 per year, and an increase in the effective tariff rate of 3% to 4% (roughly a third of the proposed 10% blanket tariffs). We foresee the economy growing 2.2% in 2025 and 1.7% in 2026.

In the details:

Growth in real final sales to domestic purchasers (which excludes the net international trade components) rose 3.1% quarter over quarter in Q4 while real final sales to private domestic purchasers (also excluding government spending) grew 3.2%. On a year-over-year basis, real GDP growth cooled 0.2ppt to a still-robust 2.5% y/y pace while growth in real final sales to private domestic purchasers eased 0.1ppt to 3% y/y.

On the inflation front, price pressures firmed slightly in Q4 Q3 with headline inflation rising a tick to 2.4% y/y and core personal consumption expenditures (PCE) inflation rising 0.1ppt to 2.8% y/y. Despite the bump in the road, both measures are at their lowest level since Q1 2021 and within striking distance of the Fed's 2% target. We foresee headline and core PCE inflation cooling to 2.2% and 2.3%, respectively, in Q4 2025.

Consumer spending grew an impressive 4.2% in Q4 — its strongest gain since Q1 2023 — following an impressive 3.7% surge in Q3. Spending on durable goods led the gains, up 12.1% (the strongest since Q1 2023) driven by autos, recreational goods and vehicles, and furnishings and household equipment. Outlays on nondurables grew a strong 3.8% on robust spending on clothing and groceries, despite a pullback on gas.

Spending on services advanced a solid 3.1% on broad-based gains. Households spent freely on health care, financial services and transportation, and they didn't shy away from spending at restaurants, hotels and other recreational activities.

Household finances remain healthy even if increased polarization is evident. Looking ahead, moderating employment gains and income momentum point to softening outlays growth, especially for lower- to median-income families who are disproportionally affected by higher prices and interest rates along with higher debt burdens and reduced savings buffers. We project that consumer spending will grow around 2.3% in 2025 after an expected 3.2% advance in 2024.

Residential investment rebounded 5.3% in Q4 following a 4.3% contraction in Q3. Still, investment remains down 13% from its 2021 Q1 peak. While the worst of the housing sector correction is behind us, historically low affordability made worse by the recent rebound in mortgage rates and cooler income growth will cap residential investment growth in the coming quarters. Construction activity is still likely to benefit from an undersupplied housing market, but labor constraints from reduced immigration could restrain activity and pressure costs.

Business investment fell 2.2% in Q4, its first decline since 2021 Q3. Equipment investment was the main culprit, plunging 7.8% on a severe pullback in computers and peripheral equipment investment, down 48.4%. Investment in transportation equipment also fell sharply, down 14% while investment in industrial equipment only rose 1.2%.

Spending on structure also contributed to the decline in business investment, falling 1.1% in the quarter. The 4.2% rise in power and communications structures (driven in part by data centers) was more than offset by a decline in investment in commercial and health care structures and mining structures.

Intellectual property investment rose a moderate 2.6% in Q4 despite strong growth in software investment (+32.8%) — likely indicating some initial growth tailwinds from investment in generative AI. Investment in research and development rose a modest 1.7% while entertainment investment eased 0.9%.

Government spending grew a more moderate 2.5% following 5.1% growth in Q3. Federal outlays rose 3.2% amid slower federal defense outlays and a modest pickup in nondefense spending. Spending growth at the state and local level eased to a 2.0% annualized pace following a 2.9% advance in Q3.

Net international trade was neutral to GDP growth in Q4, as exports fell by 0.8% driven lower by a 5% decline in goods exports, and imports also fell 0.8% on the back of a 4% decline in goods imports, which was offset by a 12.8% surge in services imports. Looking ahead, we anticipate cooler imports as domestic activity slows and moderate export momentum as global activity remains subdued.

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