

# WEEKLY

## Economic Commentary

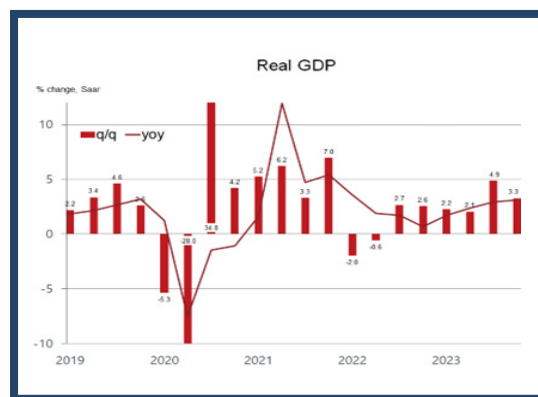
JANUARY 26, 2024



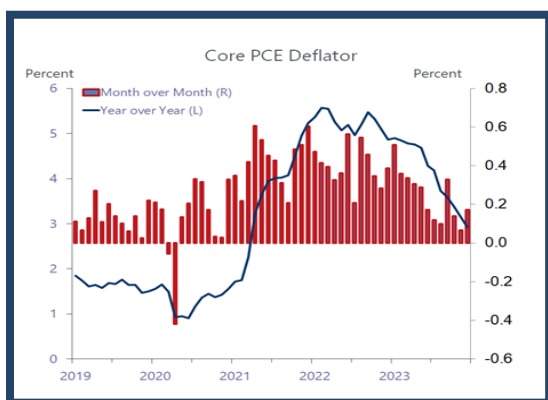
**Millennium**  
CORPORATE CREDIT UNION

**Like the Energizer Bunny, the U.S. economy just won't quit.** Never mind the widespread forecast early last year that the nation would be in the grips of a recession by now. As the curtain descended on 2023, Americans were not even experiencing a growth recession, so-called for an economy that slogs ahead at a below trend pace, which is generally estimated at a tad under 2 percent. According to the latest government data, the economy blasted through that threshold, expanding at a 3.3 percent annual rate in the fourth quarter. What's more, the main growth driver, consumer spending, ended the period with more momentum than it started. On average for the year, real GDP increased 2.5 percent, faster than the 1.9 percent in 2022. Importantly, the engine revved up as the year progressed, jumping from a 2.1 percent growth rate over the first half to 4.1 percent over the second.

True, the fourth quarter pace slowed from the outsized 4.9 percent growth rate staged in the third quarter. That's partly due to the 46-day auto strike that depressed auto output for a big chunk of the period and sliced 0.8 percent from GDP. If not for the assembly line stoppage, the fourth quarter's growth would have been 4.0 percent, still slower than the third quarter, but more than double the economy's potential growth rate. Unsurprisingly, traders are scaling back their bets of a March rate cut, with less than 50 percent now expecting the Fed to pull the trigger that early, according to the CME tracking tool. Given the central bank's deep aversion to easing policy prematurely, the risk of keeping rates elevated too long given the economy's muscular performance is greatly diminished.



We expected a later starting date before the latest batch of reports were released, and incoming data strengthens the case for more patience. That said, it would be a mistake to underestimate the case for a rate cut sooner rather than later. Just as the economy is running hotter than expected, the inflation embers have turned from smoldering to simmering and are poised to evaporate if current trends continue. The Fed's preferred inflation gauges – the PCE deflators – fell further in the closing months of the year. Over the last 3 and 6-months, both the overall and core deflators, are running at or below the Fed's 2% percent target and the year-over-year core rate dipped below 3% in December for the first time since March 2021.



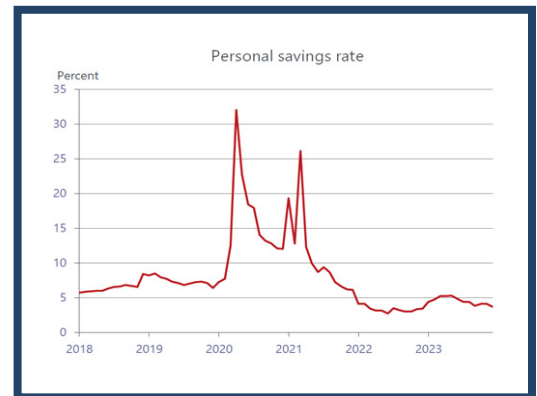
As this disinflationary trend continues, the pressure on the Fed to start cutting rates will intensify, as real rates, adjusted for inflation, would otherwise increase. That's already been happening since last July as the Fed has kept its policy rate unchanged amid the steady decline in inflation. Some believe the Fed risks waiting too long to follow inflation on the way down, but the economy's resilience so far has diluted that argument. What's more, a major contribution to the inflation retreat has come from the strong rebound in the supply of workers and products, as the acute shortages and supply chain disruptions linked to the health crisis have healed. But the contribution from expanding supply has just about run its course, and the Fed believes that more help will be needed from the demand side to keep inflation on a declining path.

If incoming data is any indication, that help is not yet forthcoming, bolstering the case for the Fed to be a bit

more patient before pulling the rate-cutting trigger. Consumers, the economy's main growth driver, continue to keep their wallets wide open. Personal consumption increased a sturdy 2.8 percent in the fourth quarter, only slightly slower than the 3.1 percent advance in the third. But again, momentum is key. After starting the period on the sidelines, consumers stepped up their purchases in November and December, ending the quarter with a flourish. That trajectory is just the opposite of the pattern seen in the third quarter, when spending was front-loaded.

Hence, consumers handily weathered the steep rise in real rates last year, and the strong momentum heading into 2024 indicates that they still have firepower to sustain spending at a sturdy pace for a while. It's important to remember that the Fed's policy rate is not the only influence on consumer behavior. Even as it kept its rate unchanged since July, investors had an idea of where it was heading and jumped the gun, pricing lowered rate expectations into the bond market that sent long-term yields sharply lower from October through December. Just how much that buoyed the economy in the fourth quarter is hard to quantify, but the housing sector undoubtedly benefited from lower mortgage rates. The 30-year rate tumbled from 7.79 percent in October to 6.61 percent at year-end, which spurred a rebound in new home sales in December as well as a jump in pending sales for existing homes.

But the scaled back bets of an early rate cut have found their way into the bond market, where yields have backed up by around 25 basis point since the beginning of the year. The Fed probably welcomes that back-up, as the easing of financial conditions late last year – paced by the wealth-boosting rallies in both the stock and bond markets – buoys demand and runs counter to the Fed's inflation-fighting efforts. Historically, there is a strong correlation between household wealth and savings, with more of the former correlated with less of the latter. Unsurprisingly, the personal savings rate fell in the fourth quarter, resting at a near historical low of 3.7 percent in December. While it is true that the vast majority of stocks are held by wealthier individuals who have a high savings propensity, the broader population is getting ever-more invested in the stock market. According to the latest Federal Reserve survey of consumer finances, a record 58 percent of the population owned stocks in 2022, up from 53 percent in 2019, the last time the survey was taken.



We suspect the Fed will need more evidence that demand is easing before undertaking the first rate cut, as the risk of a hard landing given the economy's momentum is quite low. A \$23 trillion economic behemoth does not reverse course on the dime. That said, the signs of a softening demand are present, and should become more visible in coming months. Household spending and savings decisions are affected by wealth changes, but the trend in income and employment is far more impactful. Both are slowing and should continue to do so as 2024 progresses. Indeed, the setback in the savings rate in December had less to do with the wealth boost to spending than the setback in real disposable income, which eked out a slim 0.1 percent increase following a 0.5 percent gain in November. The good news is that inflation is falling faster than incomes, providing heft to household purchasing power. But as job growth slows, as we expect, so too will wage growth; and as job insecurity rises amid the swirl of global, political and policy uncertainties, households will decide to shore up precautionary savings, resulting in a gradual slowing of consumer spending.

## KEY FINANCIAL INDICATORS

INTEREST RATES	January 26	Week Ago	Month Ago	Year Ago
3-month Treasury bill	5.35%	5.36%	5.36%	4.67%
6-month Treasury bill	5.22	5.23	5.27	4.84
2-year Treasury note	4.34	4.38	4.25	4.20
5-year Treasury note	4.03	4.05	3.85	3.61
10-year Treasury note	4.14	4.13	3.88	3.51
30-year Treasury bond	4.37	4.33	4.04	3.62
30-year fixed mortgage rate	6.69	6.60	6.61	6.13
15-year fixed mortgage rate	5.96	5.76	5.93	5.17
<b>STOCK MARKET</b>				
Dow Jones Industrial Index	38109.43	37863.80	37689.50	33978.08
S&P 500	4891.00	4839.81	4769.80	4070.56
NASDAQ	15310.97	14972.76	14992.97	11140.43
<b>COMMODITIES</b>				
Gold (\$ per troy ounce)	2018.20	2031.80	2071.80	1927.60
Oil (\$ per barrel) - Crude Futures (WTI)	78.20	73.71	71.30	79.38

## KEY ECONOMIC INDICATORS

	Latest Month/Quarter	Previous Month/Quarter	Two-Months/ Quarters Ago	Average-Past 6 Months or Quarters
New Home Sales (December) - 000s	664	615	676	673
Durable Goods Orders (December) - % change	5.5	-5.5	4.0	0.5
Real GDP (Q4) - % change, Saar	3.3	4.9	2.1	2.9

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