Nationwide®
is on your side

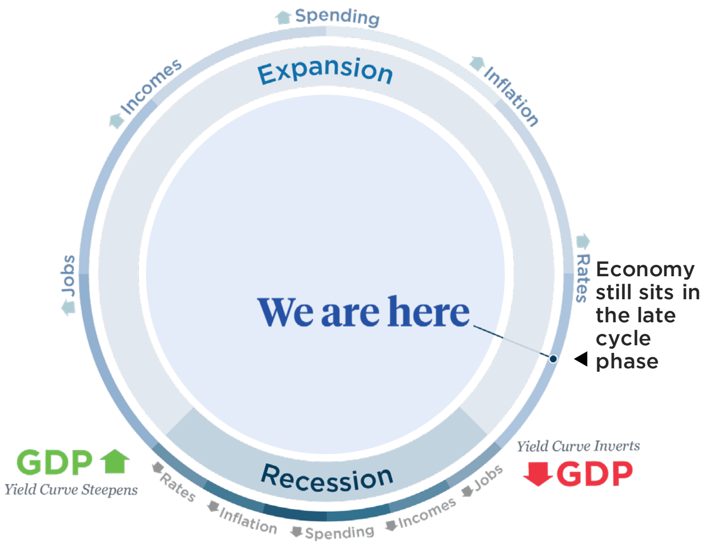
Economic & Financial Markets Monthly Review | July 2024

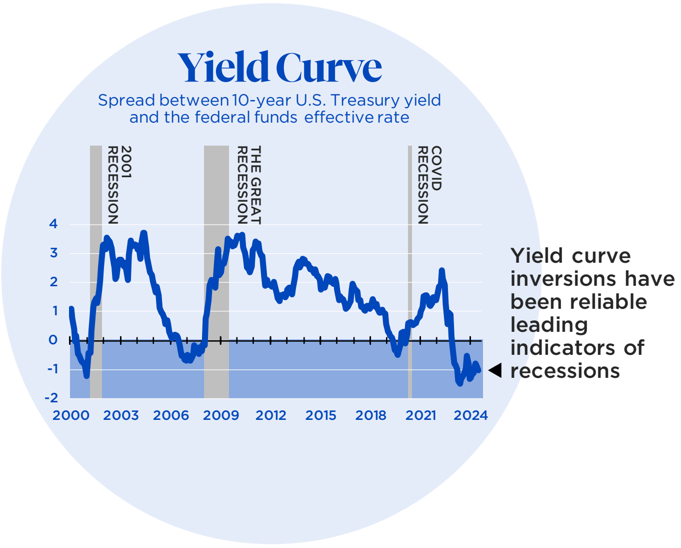
# Cooler winds for the economy at mid-year

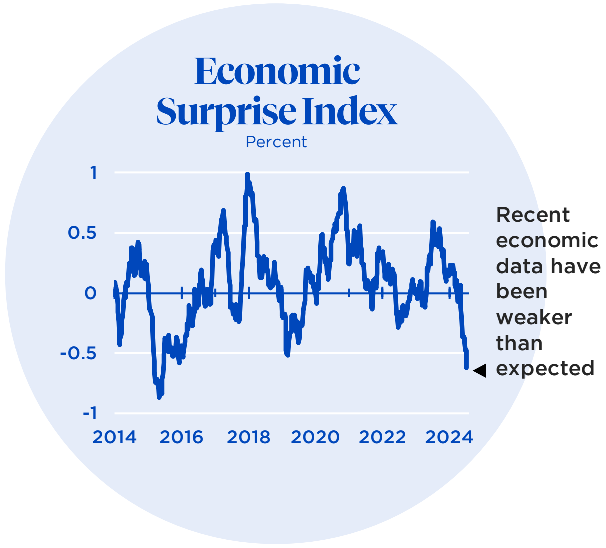
## Economic Overview

# Where is the economy now?

Economic activity downshifted by mid-year with elevated interest rates and inflation fatigue weighing on spending behavior by consumers and businesses. But growth should remain positive, albeit likely running below trend through the end of the year. The less frothy economic data provide more reason for the Fed to start lowering interest rates in the second half of 2024.




## Where we are this month

### Soft landing still most likely

The U.S. economy should post more modest growth in the second half of 2024 as interest rate and inflation headwinds build for consumers.

### Yield curve inversion widens

The spread between the 10-year Treasury rate and the fed funds rate was at its widest point of the year in June as long-term rates moved lower.

### Data take a downward turn

Bloomberg's U.S. Economic Surprise Index has dropped to the lowest reading since 2015 as recent economic readings undershoot consensus estimates.

## What does this mean

**Soft landing still most likely**

- We foresee higher odds of a soft landing than a recession in the year ahead, especially if the Fed starts to reduce the pressure from high interest rates before year end.
- But recession risks still loom on the horizon for 2025 and beyond, led by concerns that the Fed will maintain restrictive monetary policy for an extended period or if consumers experience an unexpected price/income shock.

**Yield curve inversion widens**

- As the market awaits Fed easing, the yield curve inversion remains entrenched with long-term interest rates dropping in anticipation of lower policy rates in coming years. Portions of the yield curve could remain inverted over 2025 with the Fed on course to ease rates more gradually than usual.
- The fully inverted yield curve suggests that recession odds remain higher than normal, although a downturn could be delayed for some time by a soft landing.

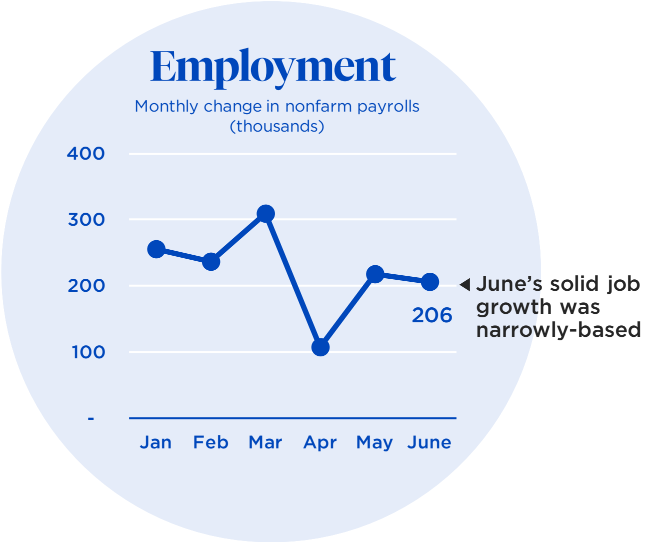
**Data take a downward turn**

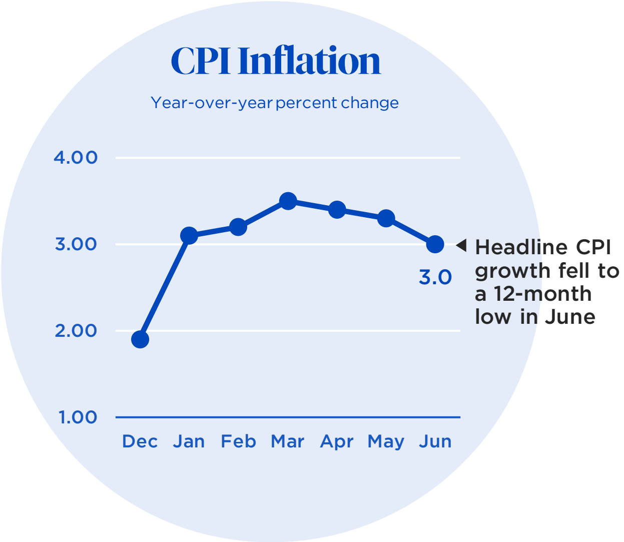
- The weaker shift in the data is another sign that the economy is likely to expand at a below-trend rate in the second half of 2024 as consumers and businesses tighten their belts.
- The cooler trend in activity is welcomed by Fed officials following a hotter start to 2024 than expected. If conditions ease further over the summer, this should keep the FOMC on track for an initial rate cut at its September policy meeting.

# Economic Review

# First half ends with slower job gains, services demand

Headline employment gains were still solid in June but were heavily concentrated in only a couple sectors as hiring has slowed in many areas. Additionally, the unemployment rate climbed for a third straight month and annual wage growth slowed to a three-year low. A weakening employment situation resulted in weaker demand for services at the close of the first half — likely a precursor to slower economic growth in the second half of 2024.





## Where we are this month

## What does this mean

### Momentum slows in the labor market

Headline nonfarm payrolls advanced at a healthy clip of 206,000 in June, while the unemployment rate climbed to 4.1 percent — the highest level since November 2021.

- Three-fourths of the headline gain in payrolls were confined to health care and social assistance and government sectors. Furthermore, large downward revisions to the prior two months provide a clear indication of slowing demand in the labor market.
- Annual wage growth advanced at a pace of 3.9 percent in June. Although it remains above a pace consistent with two percent inflation, it is the slowest annual rate in more than three years.

### Another good inflation reading in June

The overall CPI fell 0.1 percent in June while the core rate rose at a modest 0.1 percent pace, continuing the recent run of positive inflation data.

- The 3-month annualized rate for overall CPI inflation dropped to 1.1 percent and core CPI fell to 2.8 percent on the same basis. Both are indications that inflationary momentum is firmly headed in the right direction in mid-2024.
- Supercore inflation (core services less rents) was flat for a second straight month. There is still work to do to bring the 12-month change down, but services inflation has cooled considerably in recent months.

### Demand for services declined in June

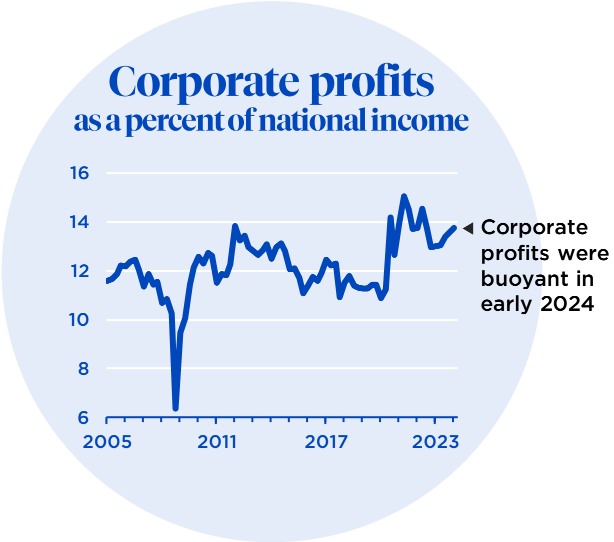
The new orders component of the ISM services survey fell into contraction territory in June (i.e., below 50) for only the second time since the Covid recession.

- June's relatively sharp decline in the new orders index could be a one-month blip but, from a broader perspective, it aligns with a downward trend in new orders back to January 2023.
- The fall in the business activity index was even sharper and pushed the reading into contraction territory. In combination with declining new orders, the latest survey and the underlying trends suggest weaker demand for services going forward.

# Investors remain upbeat overall

Risk assets stayed buoyant in June amid a relatively solid economic backdrop, but interest rates trended lower as the data signal slower growth and inflation. We expect financial markets to remain on a positive track in the latter half of 2024, with equities holding onto gains and borrowing costs falling slowly as the economy settles into a slower track. There should be enough progress on inflation to allow the Fed to start easing monetary policy in September.






## Where we are this month

### Equities extend their gains

Signs of a moderating economy did not sour investors' attitudes as the S&P 500 rose more than three percent last month and is up a robust 17 percent year-to-date.

### Interest rates ease

The 10-year Treasury yield built on its early summer declines, falling another 17 basis points in June. Despite the retreat in rates, borrowing costs remain elevated.

### Profits stay buoyant

Corporate earnings performance was positive at the headline level in Q1, providing fundamental support to the equity market.

## What does this mean

**Equities**

- In a sign of changing tides, stock performance was disparate as the major sectors were split roughly evenly between gains and losses. The fundamental backdrop remained encouraging as the economy continued to expand, financial conditions were loose, and equity analysts hold onto optimistic views.
- The equity market is overvalued by traditional valuation metrics but high hopes surrounding generative AI, a benign environment, approaching Fed cuts are keeping investors upbeat.

**Interest rates**

- A cooling economy has helped to ease interest rate pressures. The 2-year Treasury yield, which is sensitive to Fed policy, ended June roughly 30 basis points lower than at the start of the month.
- Interest rates will remain vulnerable to swings in the economic data and the Fed's messaging on monetary policy. Stubborn inflation and concerns over the federal government's fiscal trajectory lend upside risks to our interest rate forecasts.

**Profits**

- Striking a similar tone as the recent economic data, the earnings performance was mixed beneath the topline as some sectors recorded losses while others registered gains. According to S&P, energy was the top performer in the first quarter from the EPS perspective while industrials lagged their peers.
- We think corporate profits will come under greater pressure in the second half of 2024 as pricing power diminishes and costs pressures remain elevated.

# Outlook

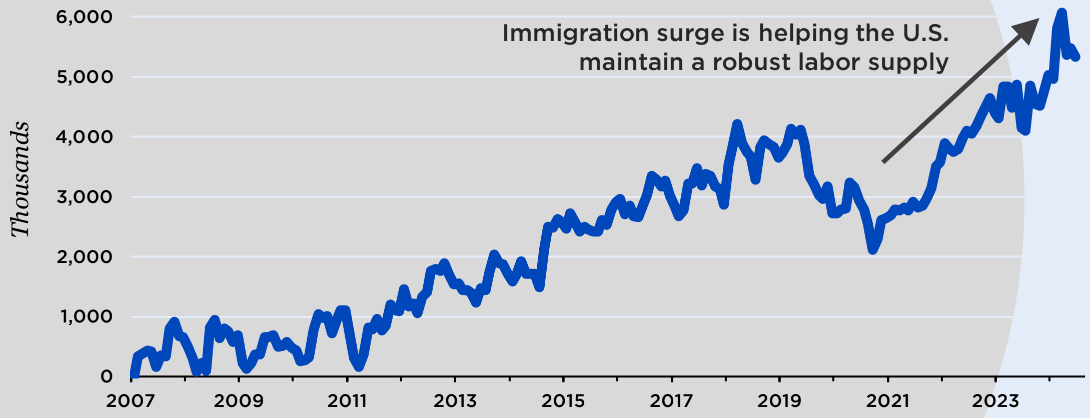
# Climbing unemployment rate is not yet a recession signal

While job growth has remained solid, the unemployment rate has climbed for three consecutive months — rising in June to the highest level since November 2021 at 4.1 percent. This has set off some alarm bells for the economy with the benchmark unemployment reading now 0.7 percentage points above its cycle low.

The recent rise in the unemployment rate has coincided with a positive labor supply shock led by a surge in immigration. While the native-born working age U.S. population continues to shrink due to retirements from the baby boom generation, broader immigration flows have helped to fill labor supply gaps. The growth in the labor force has also caused unemployment readings to drift higher.

We expect labor demand to weaker further over the second half of 2024 and into 2025, slowing job gains and leading to modest layoffs in some sectors. But the current labor market remains supportive of continued consumer spending and economic growth — just with less of a tailwind than seen in recent years.

## Foreign-born working age population growth




Podcast
**Hear more in our podcast**
PLAY

FIND **NATIONWIDE MARKET INSIGHTS** WHEREEVER YOU LISTEN TO PODCASTS

# Latest Forecast

Data as of July 2024

| | 2023 ACTUAL | 2024 ESTIMATE | 2025 FORECAST | 2026 | 2027 |
|---|---|---|---|---|---|
| REAL GDP | 2.5% | 2.3% | 1.6% | 1.9% | 1.8% |
| UNEMPLOYMENT RATE | 3.6% | 4.0% | 4.3% | 4.0% | 4.0% |
| INFLATION [1] (CPI) | 3.2% | 2.8% | 2.3% | 2.1% | 2.0% |
| TOTAL HOME SALES | 4.75 | 4.78 | 5.10 | 5.95 | 6.15 |
| S&P/CASE-SHILLER HOME PRICE INDEX | 5.5% | 5.0% | 3.3% | 3.2% | 3.0% |
| LIGHT VEHICLE SALES | 15.5 | 15.5 | 15.6 | 16.4 | 16.5 |
| FEDERAL FUNDS RATE [2] | 5.25% | 4.75% | 3.50% | 2.75% | 2.75% |
| 5-YEAR TREASURY NOTE [2] | 3.84% | 4.05% | 3.71% | 3.40% | 3.40% |
| 10-YEAR TREASURY NOTE [2] | 3.88% | 4.15% | 3.80% | 3.80% | 3.80% |
| 30-YEAR FIXED-RATE MORTGAGE [2] | 6.61% | 6.50% | 5.35% | 5.00% | 5.00% |
| MONEY MARKET FUNDS | 5.09% | 5.09% | 3.78% | 2.97% | 2.78% |

[1] Percent change Q4-to-Q4
[2] Year-end

### Cooler energy costs lower inflation path

Consumer inflation should ease further over the second half of 2024, aided by expected lower gasoline and energy prices. Upside risks from services and housing costs remain, which should keep the core CPI elevated despite the lower overall inflation readings.

### Growing confidence in H2 Fed easing

The downshift in economic activity has firmed expectations for Fed monetary policy easing in the second half of the year. Markets are pricing in two rate cuts by year end, with September the likely start for the easing cycle. This aligns with our latest interest rate forecast.

# Contributors

**Kathy Bostjancic**
*SVP & Chief Economist*

**Ben Ayers, MS**
*AVP, Senior Economist*

**Oren Klachkin**
*AVP, Financial Market Economist*

**Daniel Vielhaber, MA**
*Economist*

**Ashleigh Leonard**
*Economics Specialist*

**Brian Kirk**
*Communications Consultant*

# Sources

| Page | | |
|---|---|---|
| **Page 1** | **Where is the economy now?** | |
| | Business Cycle | *Nationwide Economics* |
| | Yield Curve | *Bloomberg; National Bureau of Economic Research* |
| | Economic Surprise Index | *Bloomberg* |
| **2** | **Economic Review** | |
| | Nonfarm payroll gains | *Bureau of Labor Statistics* |
| | Consumer Price Index | *Bureau of Labor Statistics* |
| | ISM Services – New Orders | *Institute for Supply Management* |
| **3** | **Financial Markets Review** | |
| | S&P 500 | *Standard & Poor's* |
| | 10-year Treasury yield | *Federal Reserve Board* |
| | Corp profits as a % of nat'l income | *Bureau of Economic Analysis* |
| **4** | **Outlook** | |
| | Foreign born population growth | *Bureau of Labor Statistics; Nationwide Economics* |
| | Latest Forecast | *Nationwide Economics* |





NFM-11356AO.3