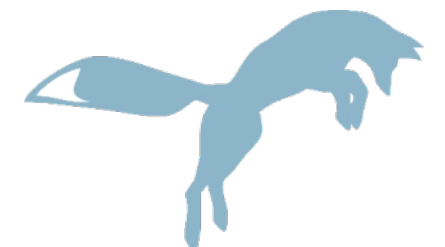



U.S. Economic Outlook

Kate Watkins, Ph.D.
President & Chief Economist
Bright Fox Analytics

**NCSL Spring 2024
Budget Working Group**
Seattle, Washington
June 6, 2024

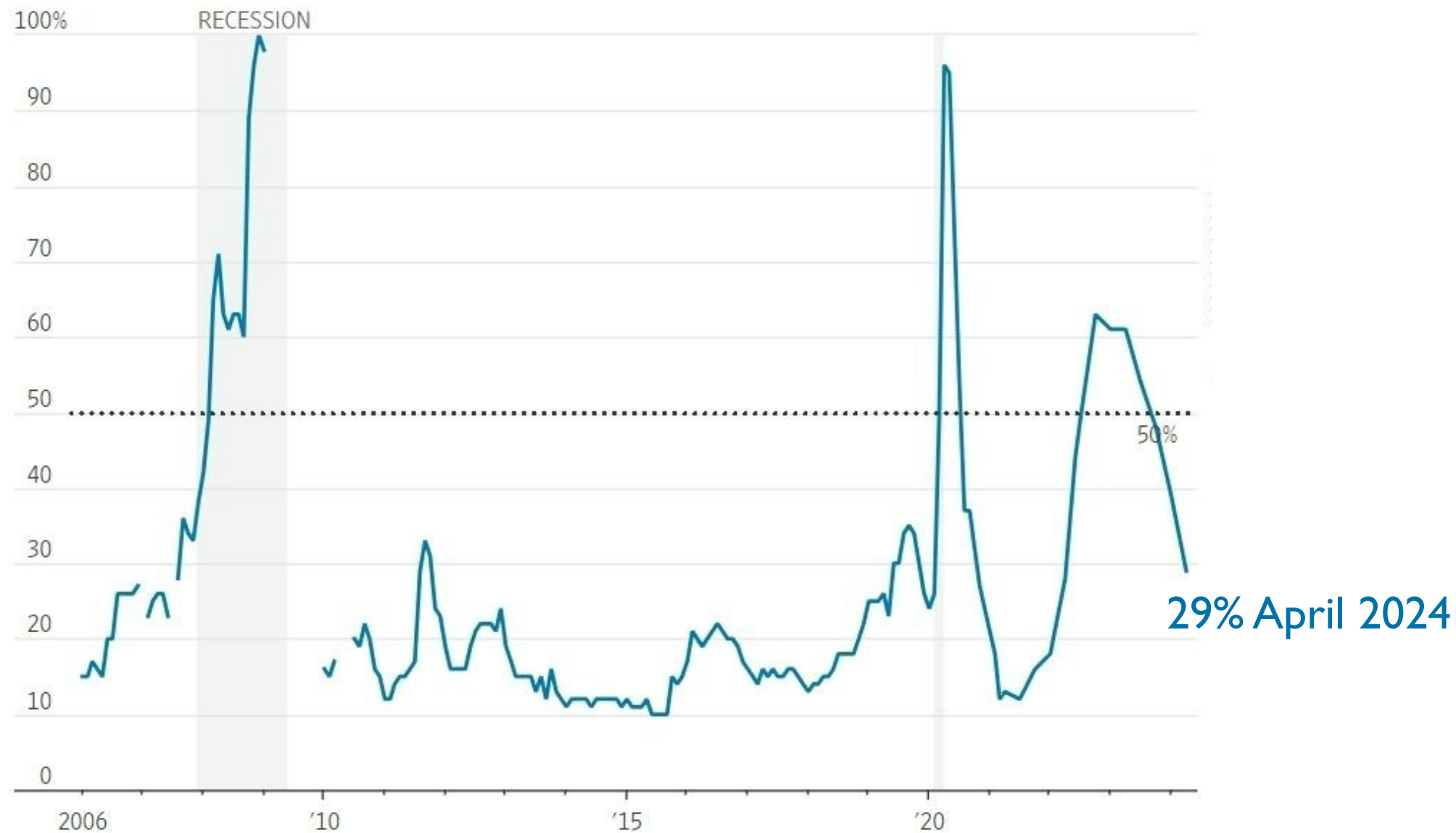


Presentation Overview

- Why aren't we in a recession yet?
 - Economic outlook
 - Household income & wages
 - Business income
 - Consumer spending
 - Housing & commercial real estate
 - Risks to the outlook
- Income, sales, and property taxes
- 

The economy continues to surprise...to the upside

Economists' Recession Expectations Probability Within the Next 12 Months



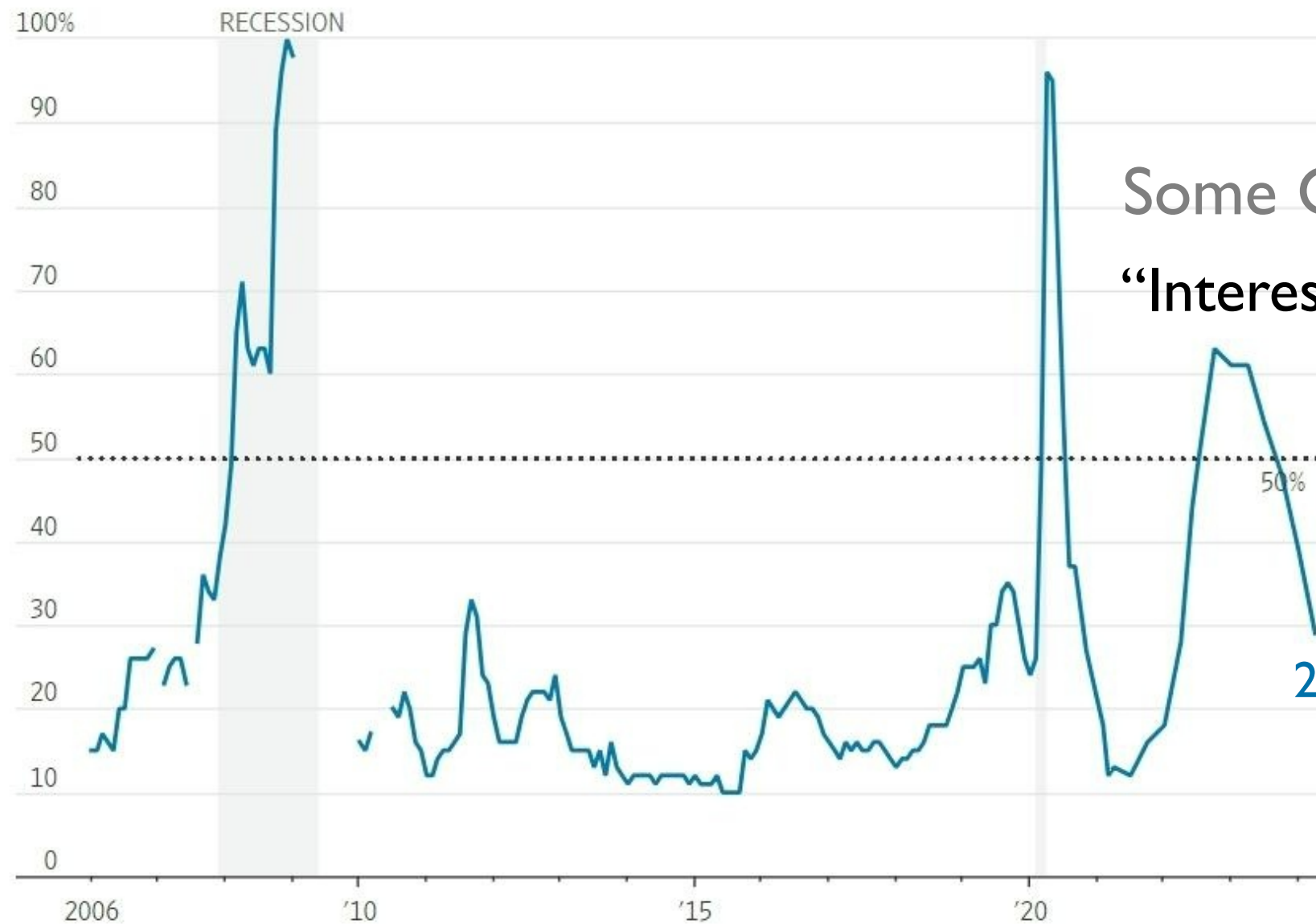
Source: Sam Goldfarb & Anthony DeBarros. "‘Envy of the World’—U.S. Economy Expected to Keep Powering Higher." April 14, 2024.

Available at: <https://www.wsj.com/economy/central-banking/economy-forecast-lower-recession-chances-1f24174b>

Note: Wall Street Journal survey of 69 economists. Average of economists' answers. Gaps indicate questions not asked or data unavailable.

Stories economists tell

Economists' Recession Expectations Probability Within the Next 12 Months



Some Common Narratives Among Economists

“Interest rate hikes will lead to recession”

“Consumers surprisingly resilient”

“A soft landing is in sight”

“Immigration boosted growth”

29% April 2024

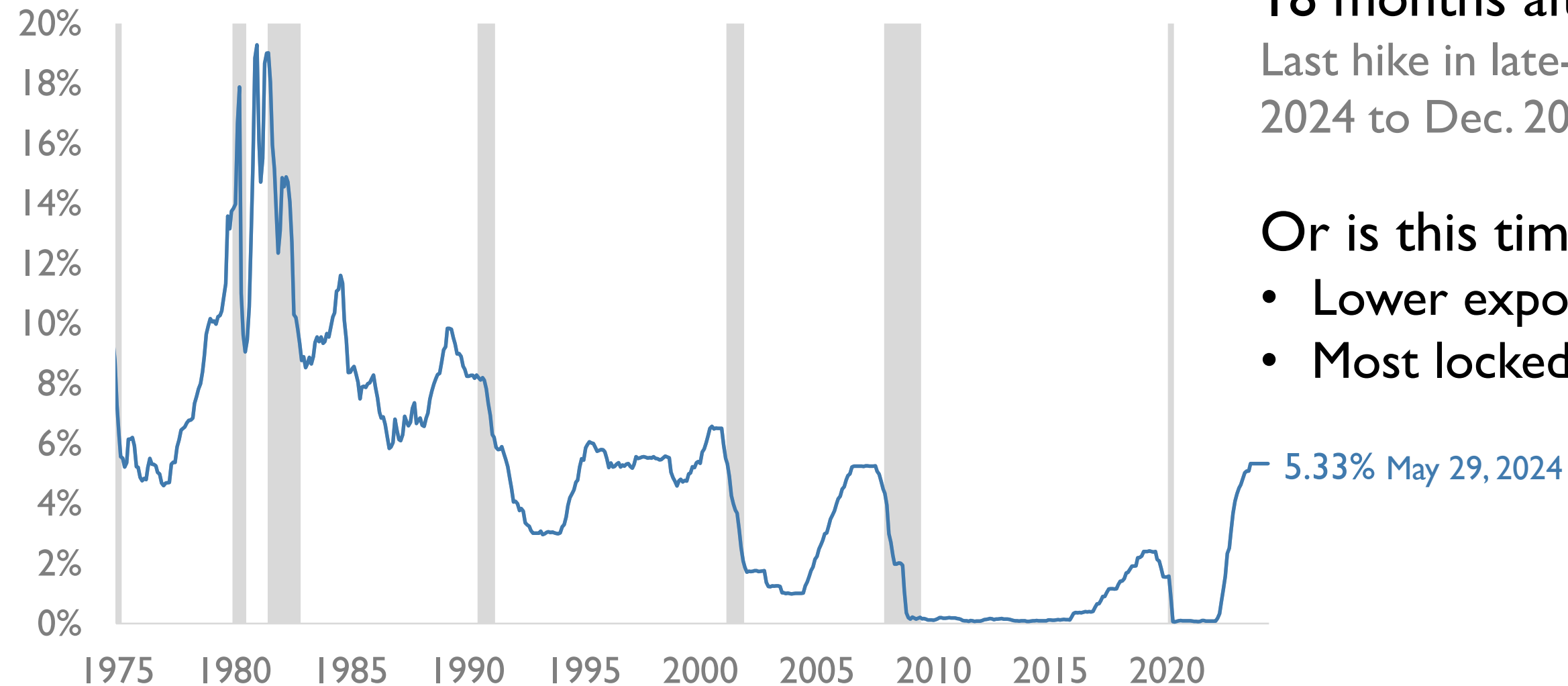
Source: Sam Goldfarb & Anthony DeBarros. “‘Envy of the World’—U.S. Economy Expected to Keep Powering Higher.” April 14, 2024.

Available at: <https://www.wsj.com/economy/central-banking/economy-forecast-lower-recession-chances-lf24174b>

Note: Wall Street Journal survey of 69 economists. Average of economists' answers. Gaps indicate questions not asked or data unavailable.

Monetary policy & recession risk

Effective Federal Funds Rate



Recessions historically hit 9 to 18 months after the last hike

Last hike in late-July 2023...March 2024 to Dec. 2024 recession start?

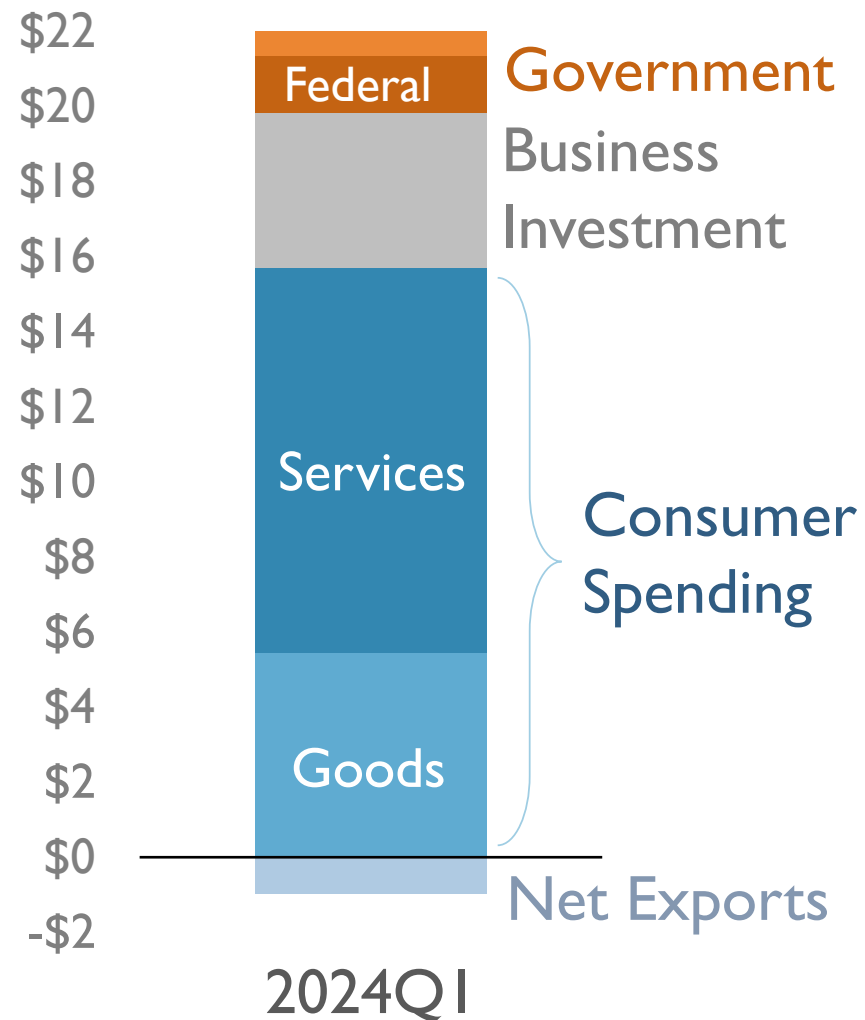
Or is this time different?

- Lower exposure to rates
- Most locked in at low rates

What's driving U.S. economic activity?

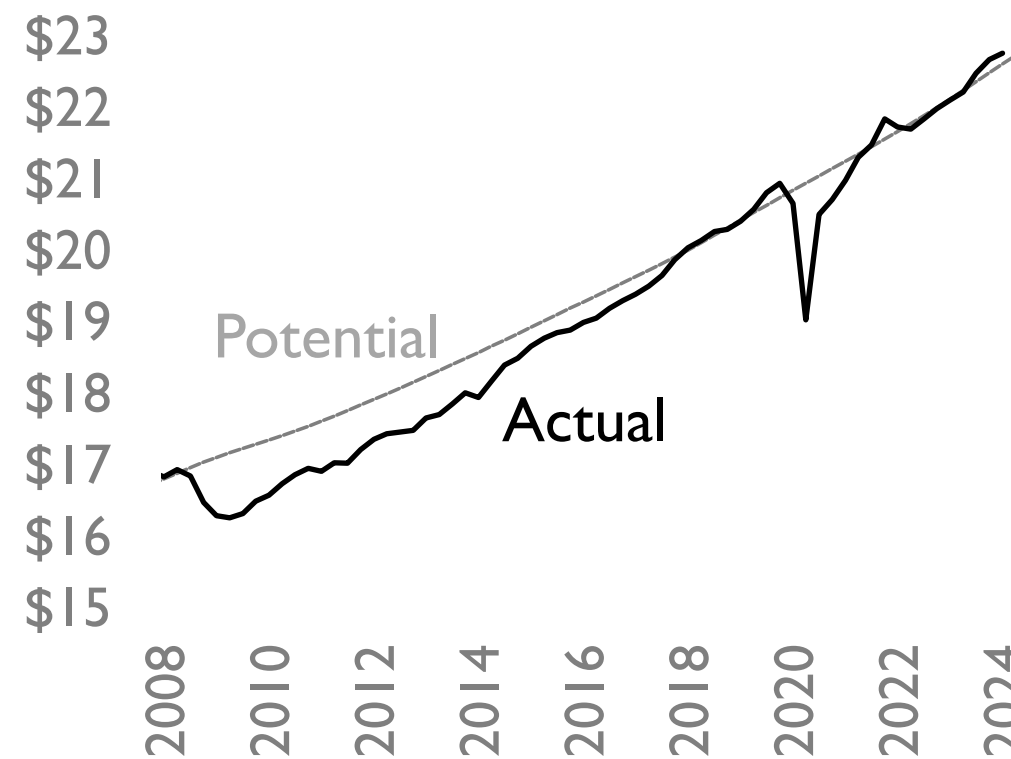
Real Gross Domestic Product (GDP)

Trillions



Real GDP

Trillions



Major Components

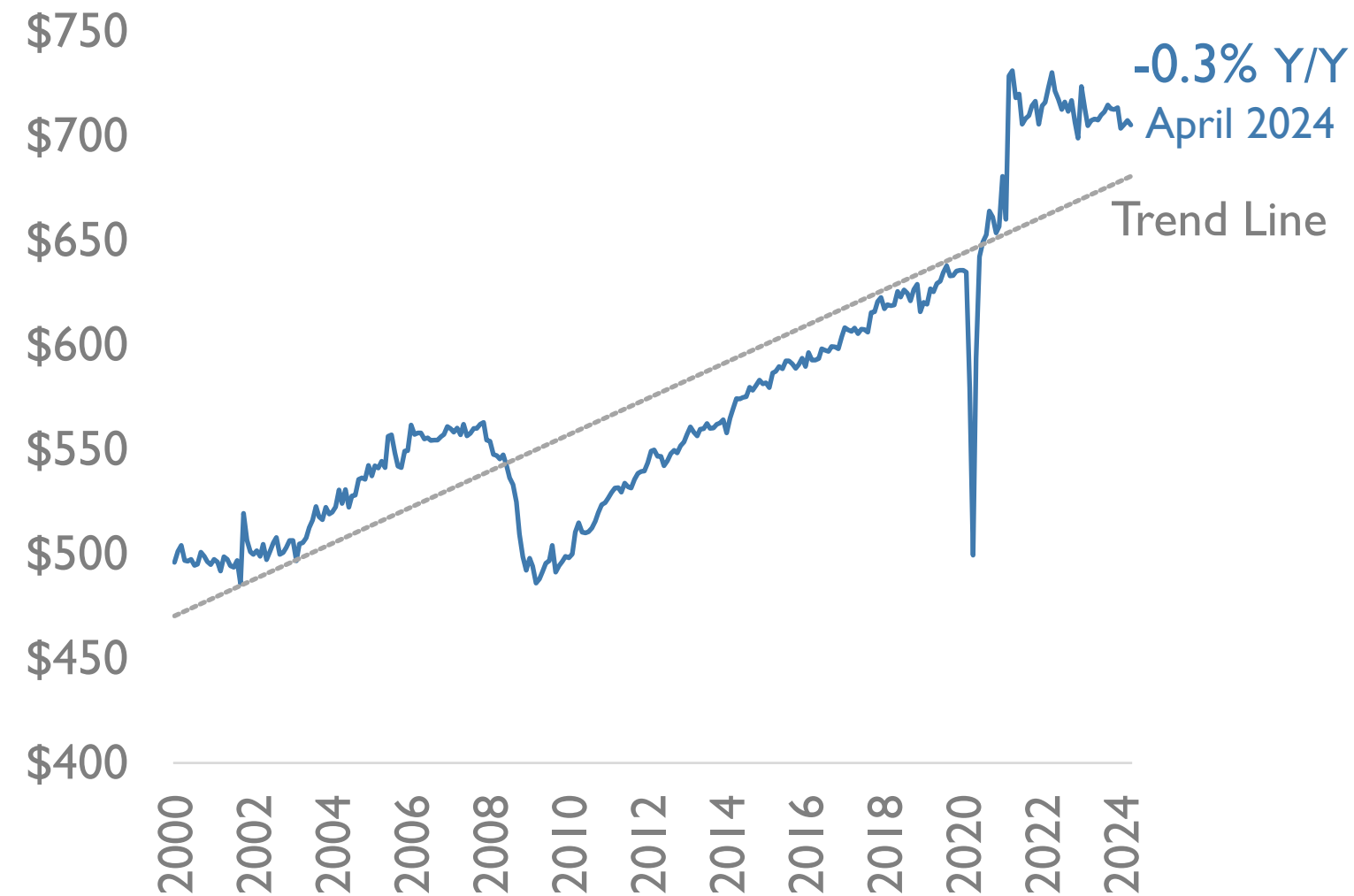


Source: U.S. Bureau of Economic Analysis (real GDP) & U.S. Congressional Budget Office (potential GDP).
Data shown as seasonally adjusted annualized rates. Data through 2024Q1.

Inflation-adjusted retail sales flat, reverting to trend; pandemic savings exhausted

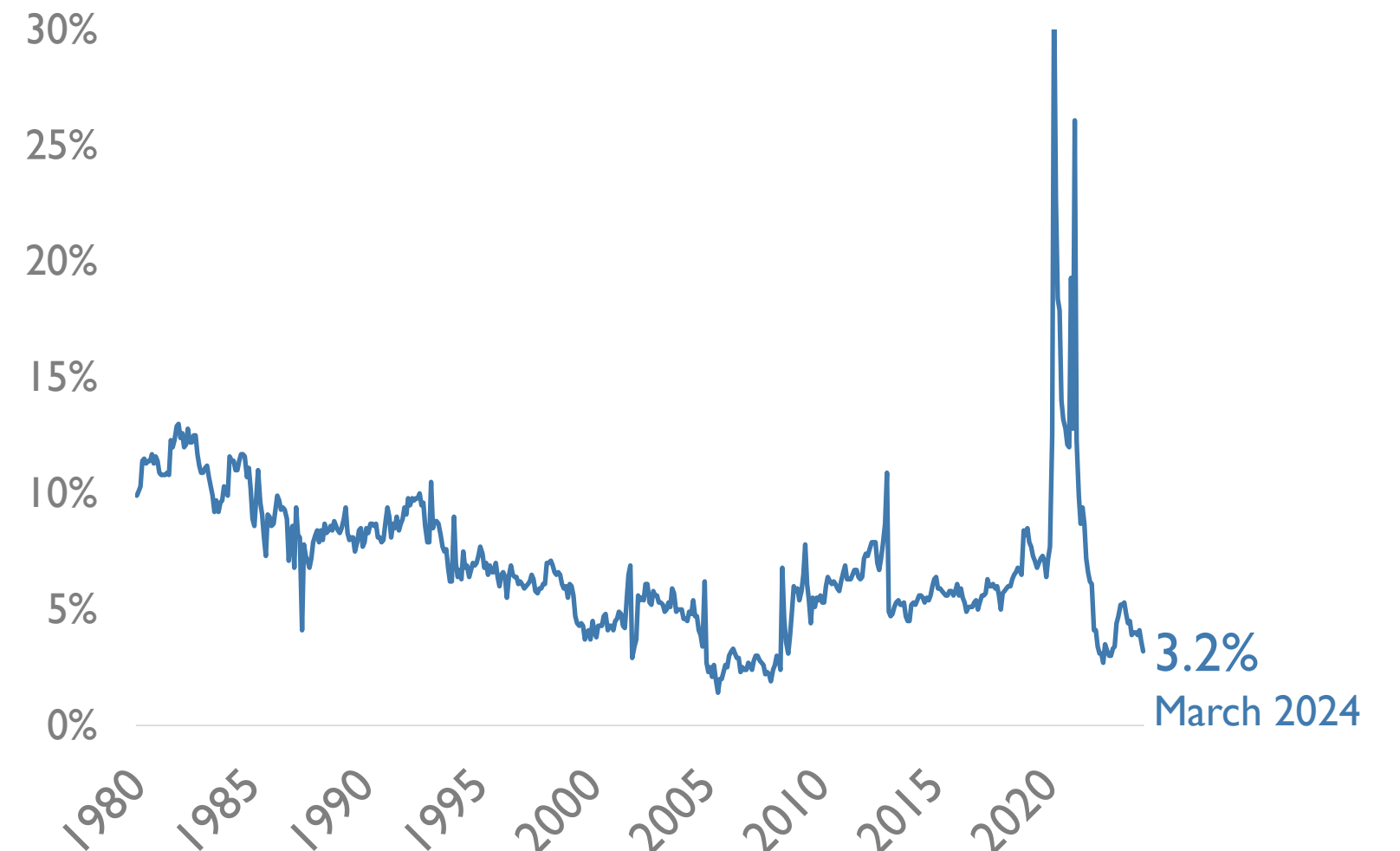
U.S. Real Retail Trade & Food Services

Billions of 2024 Dollars



U.S. Personal Savings Rate

Ratio of Savings to Disposable Personal Income



Source: U.S. Census Bureau, U.S. Bureau of Economic Analysis, and Federal Reserve Board of Governors. Data are seasonally adjusted.

Most consumers are spending less

VISA Spending Momentum Index

Billions of 2024 Dollars



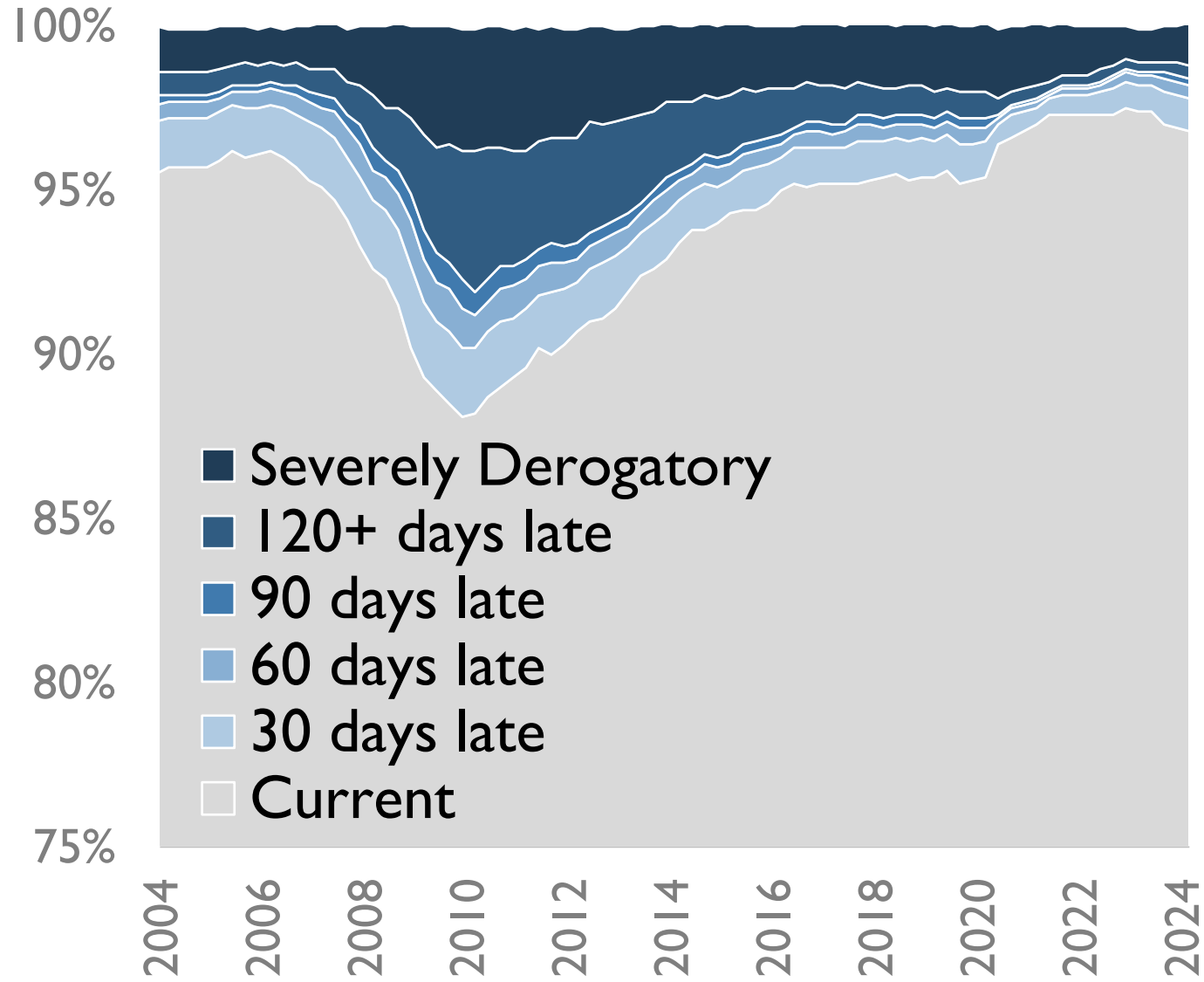
About the VISA SMI

Measures changes in spending across consumers, not aggregate spending levels

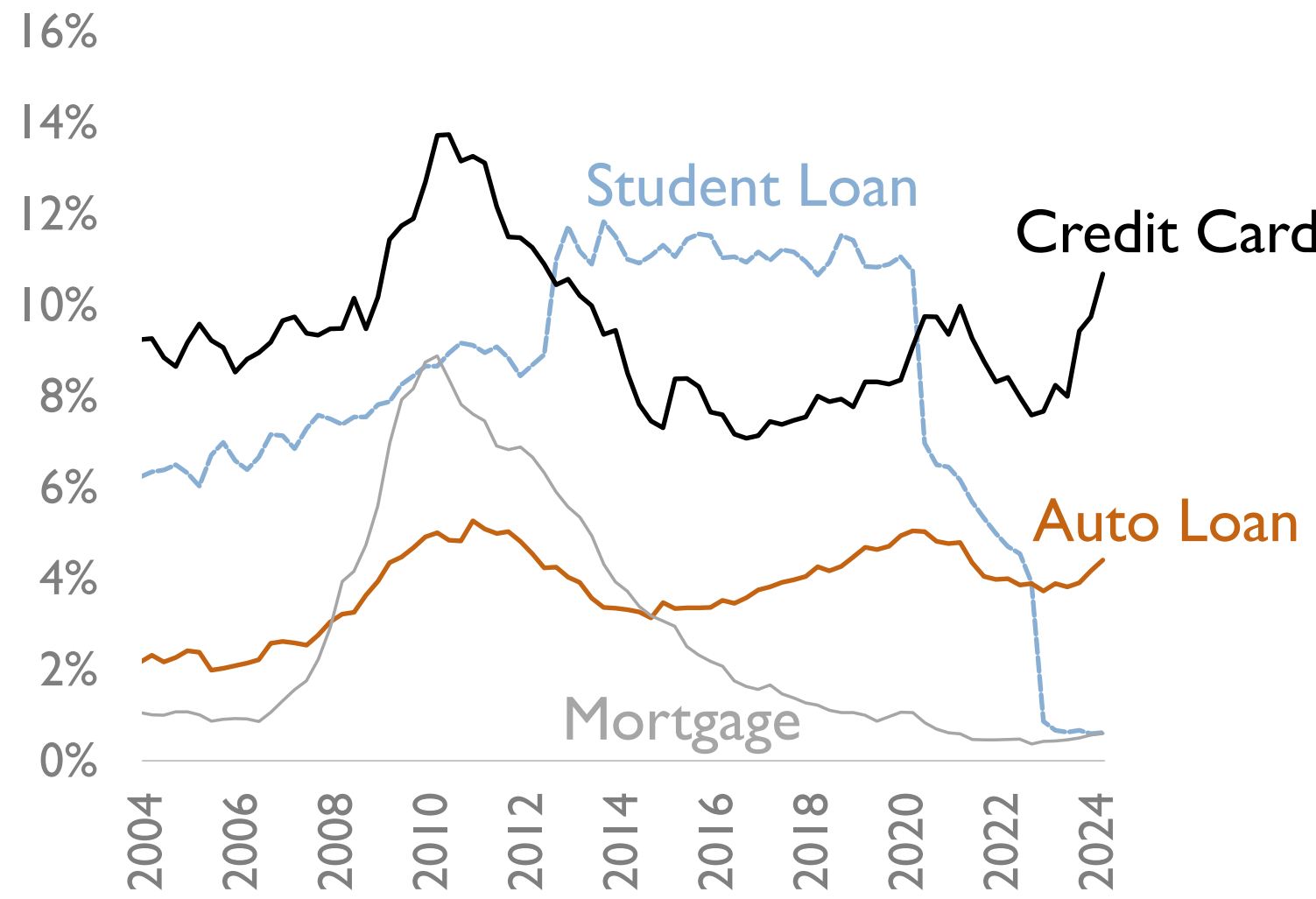
Captures all spending, including digital and services purchases

Credit card and auto loan delinquencies on the rise

U.S. Household Debt Delinquency Status
Percent of Total Debt



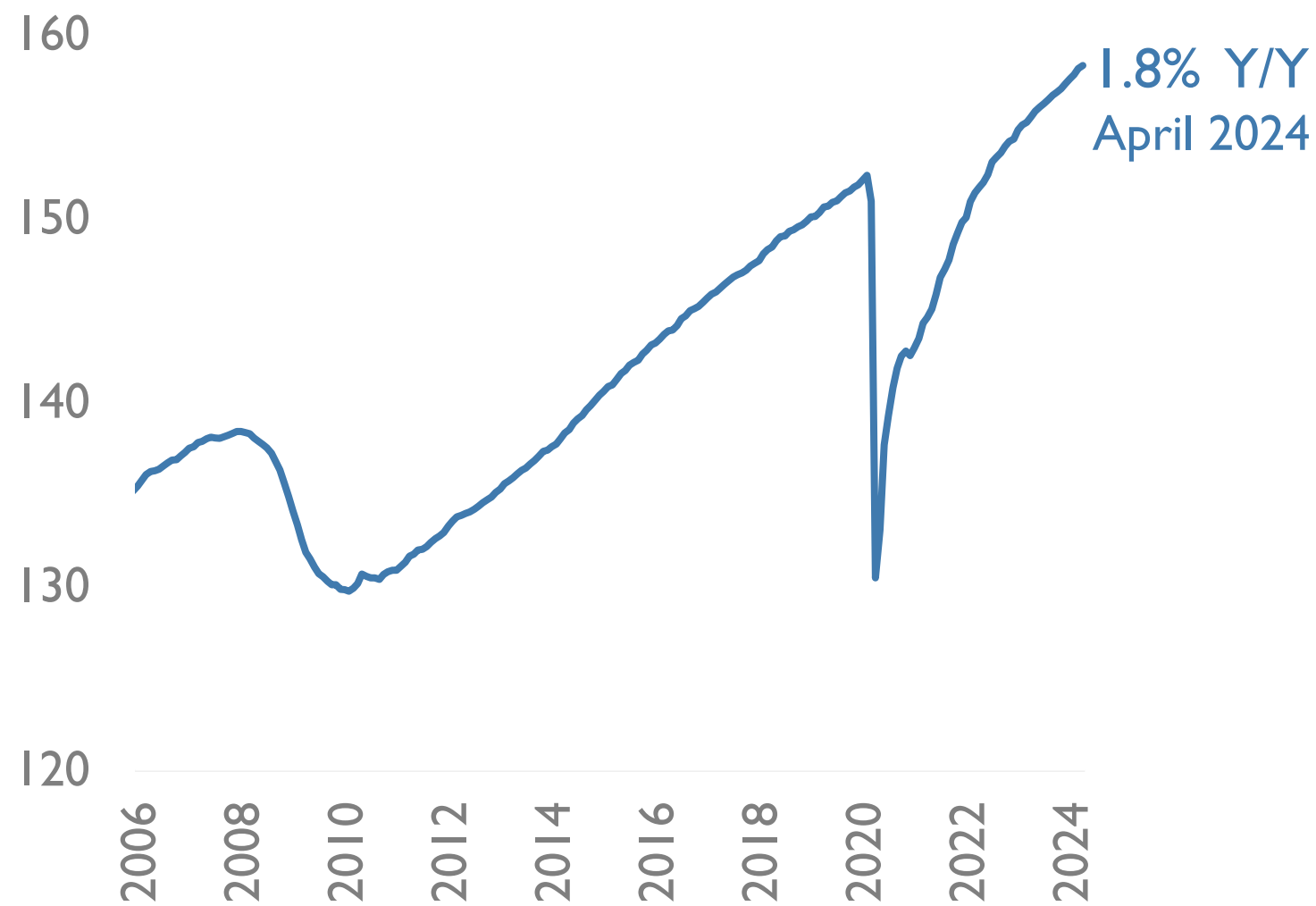
Percent of Balance 90+ Days Delinquent
Trillions



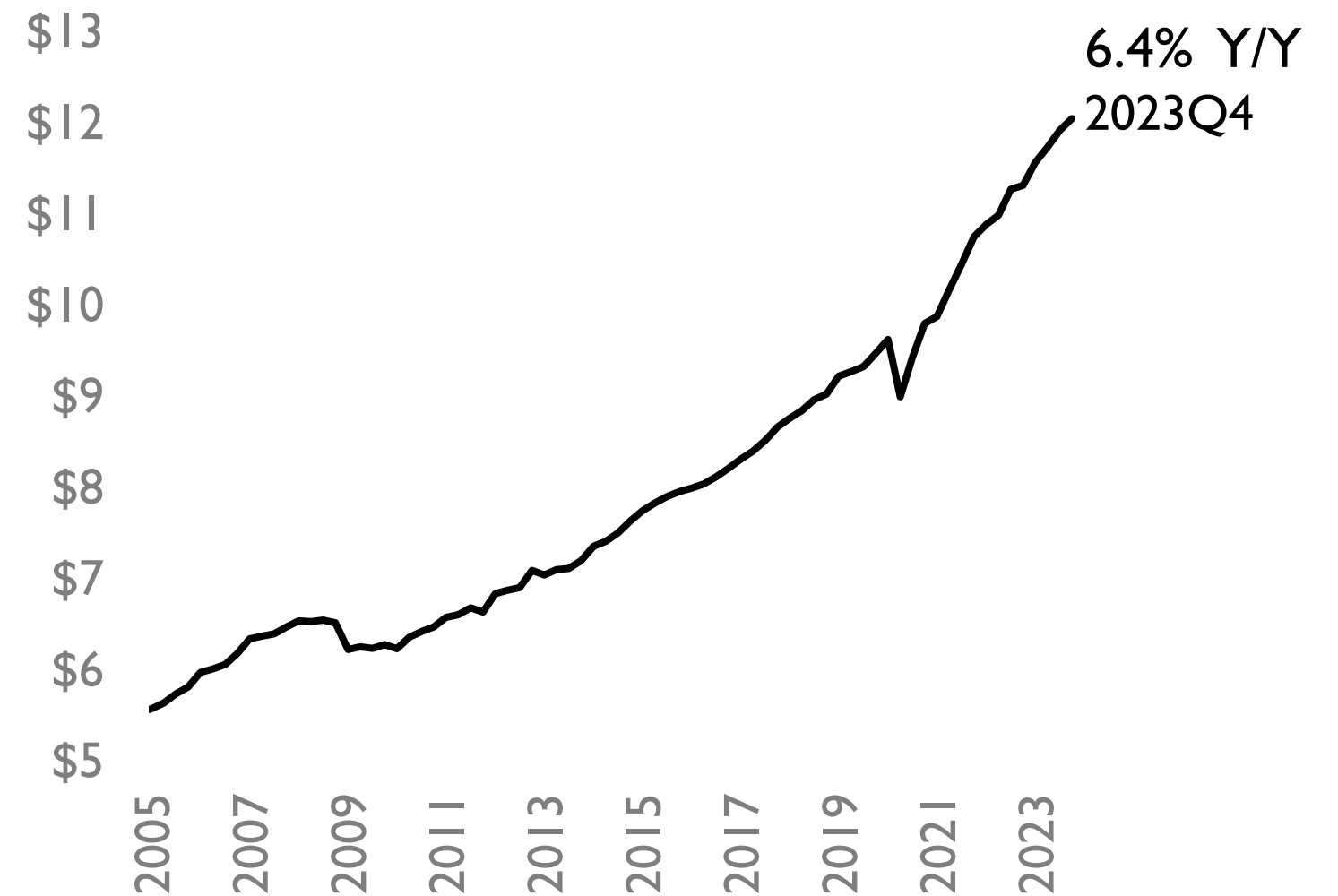
Source: Source: Federal Reserve Bank of New York / Equifax.

Ongoing jobs and real wage growth supporting consumer activity

U.S. Nonfarm Employment
Millions of Jobs



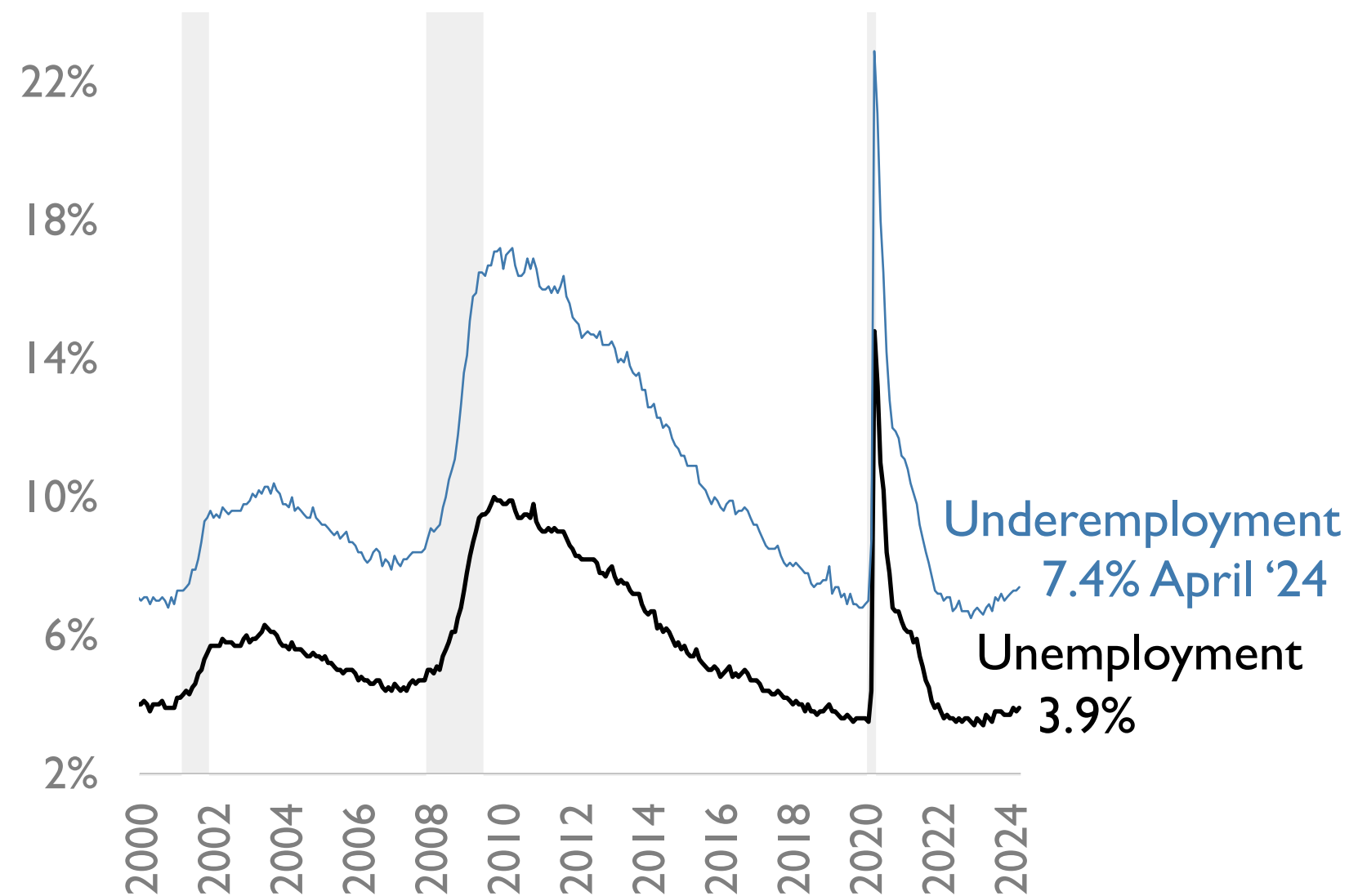
U.S. Employee Compensation
Trillions, Annualized



Labor shortages easing in many industries, employers gaining leverage

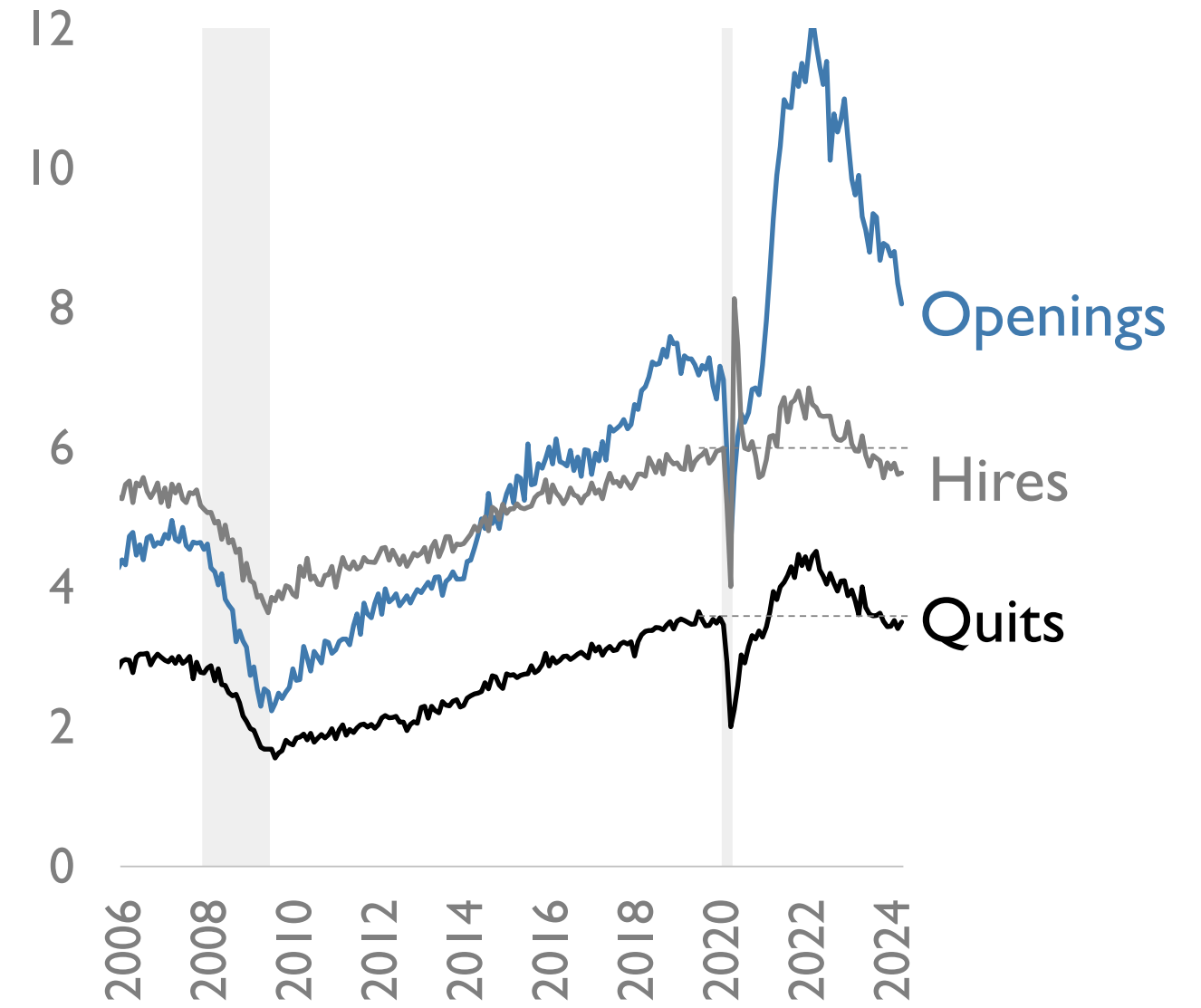
Unemployment Rates

Share of the Labor Force



U.S. Job Turnover

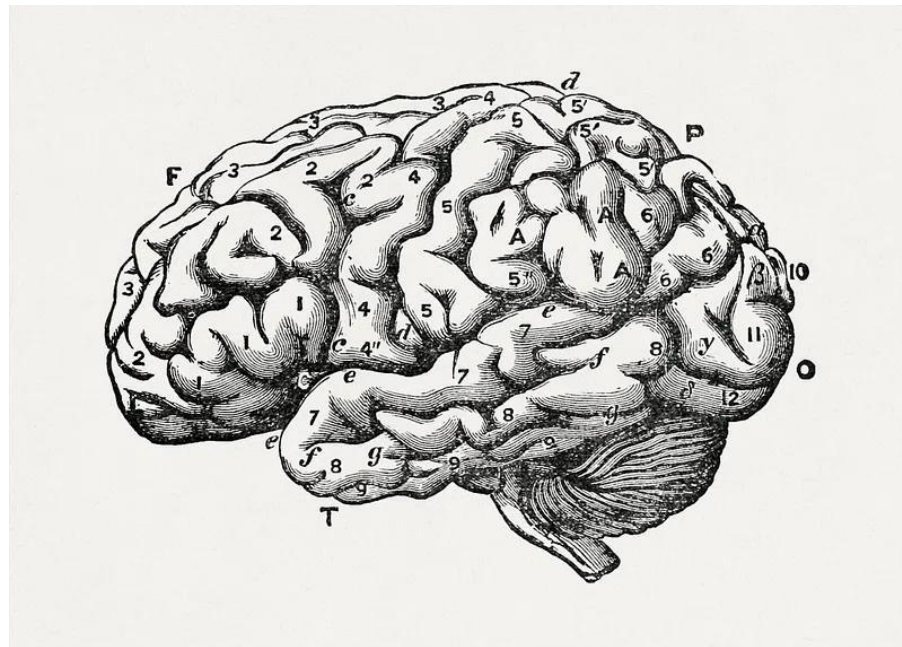
Millions



How does media consumption impact consumer activity?

Bounded Rationality

(Herbert Simon 1982)



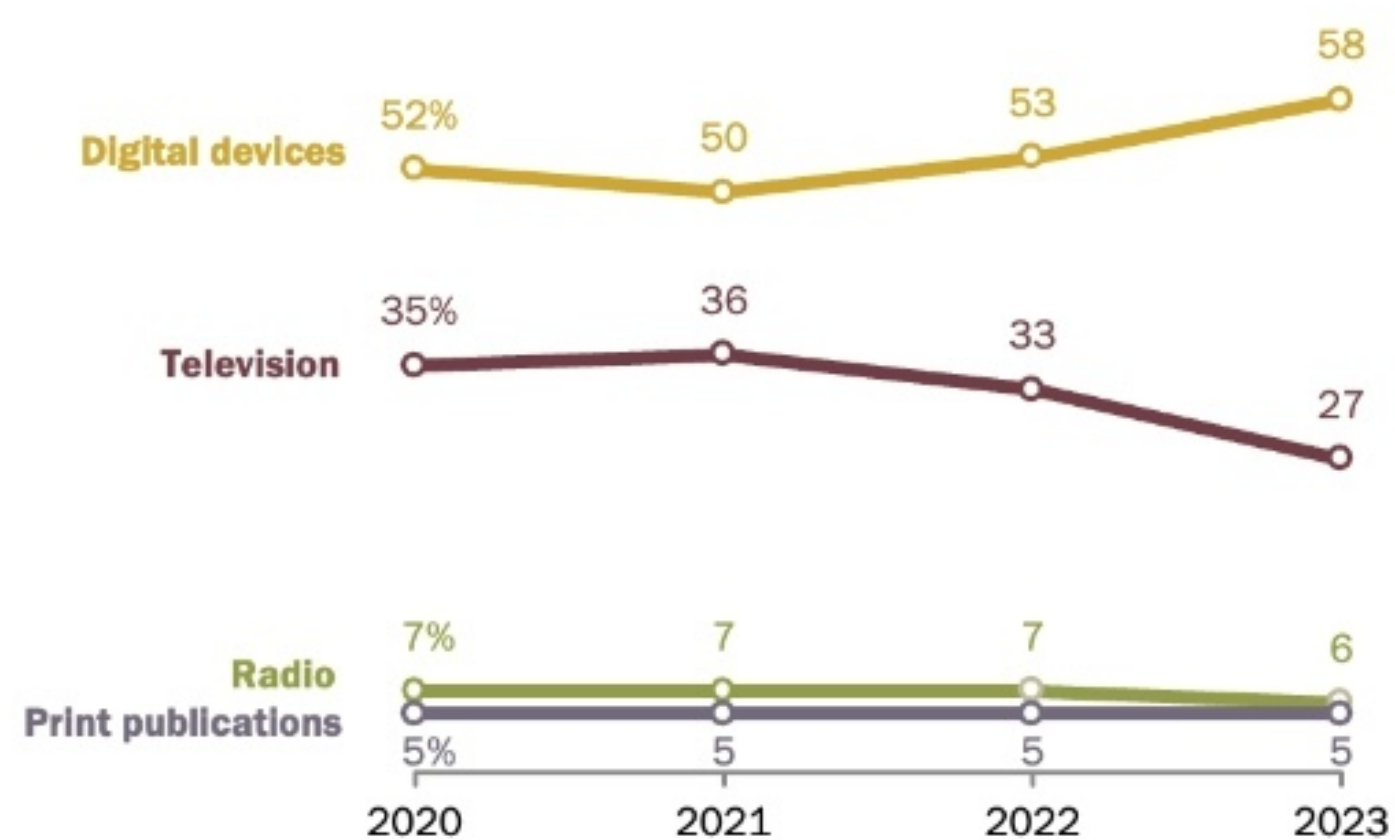
Economic decisions are a function of:

- Time limitations
- Cognitive ability
- Relevant information

Changes in information flows

News platform preferences

% of U.S. adults who prefer ____ for getting news



Digital devices gaining market share

Traditional news continues downward trend

Source: Survey of U.S. adults conducted Sept. 25-Oct. 1, 2023.

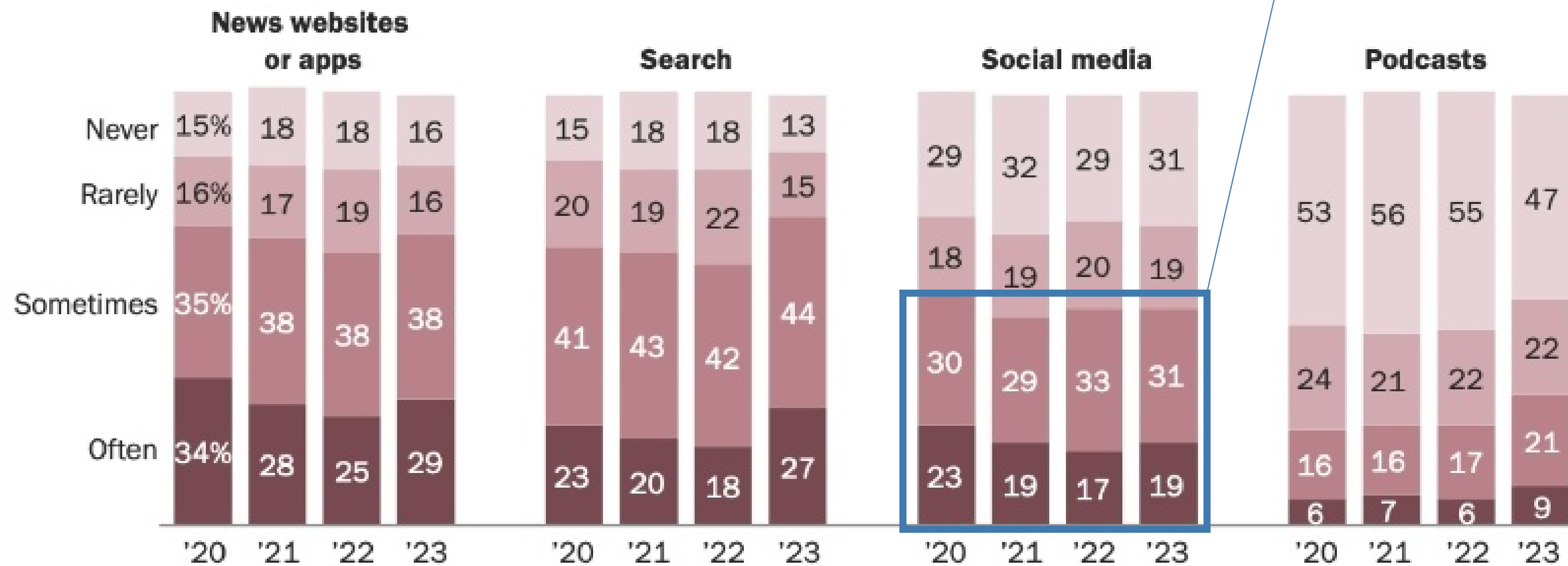
PEW RESEARCH CENTER

Changes in information flows

News consumption across digital platforms

% of U.S. adults who ___ get news from ...

50% of respondents sometimes or often rely on social media for news



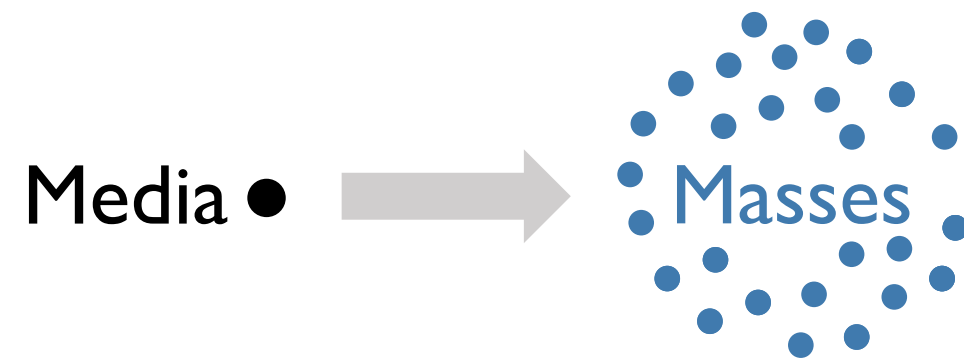
Note: Figures may not add up to 100% due to rounding. Respondents who do not have internet access at home did not receive these questions; they are included with those who said "Never," along with those who say they do not get news from digital devices.

Source: Survey of U.S. adults conducted Sept. 25-Oct. 1, 2023.

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Changes in information flows

Traditional Media



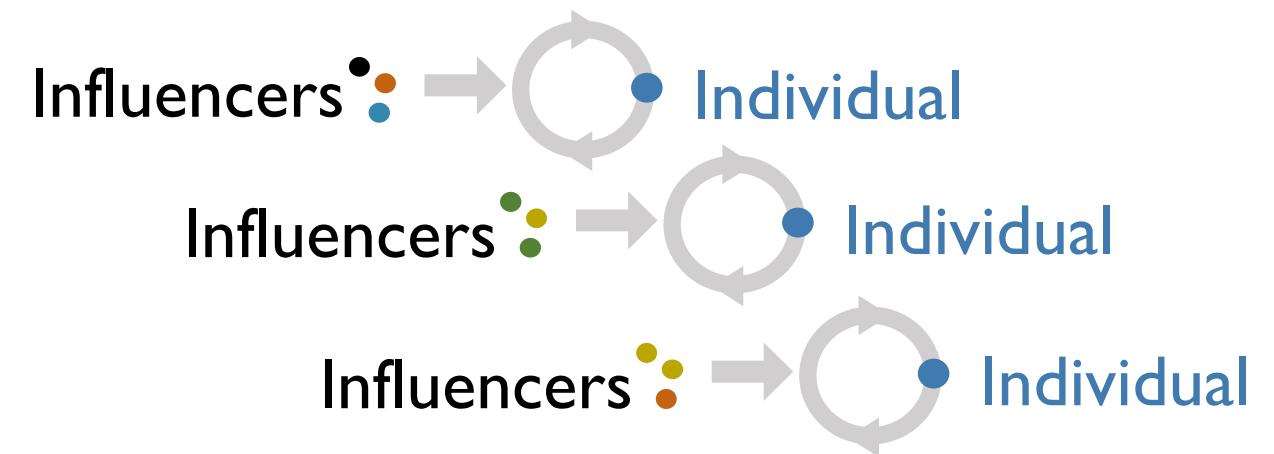
Structure of information diffusion

One-to-many broadcast

Economic information flows

Many individuals getting the same economic information

Social Media



Algorithm-curated many-to-one distribution

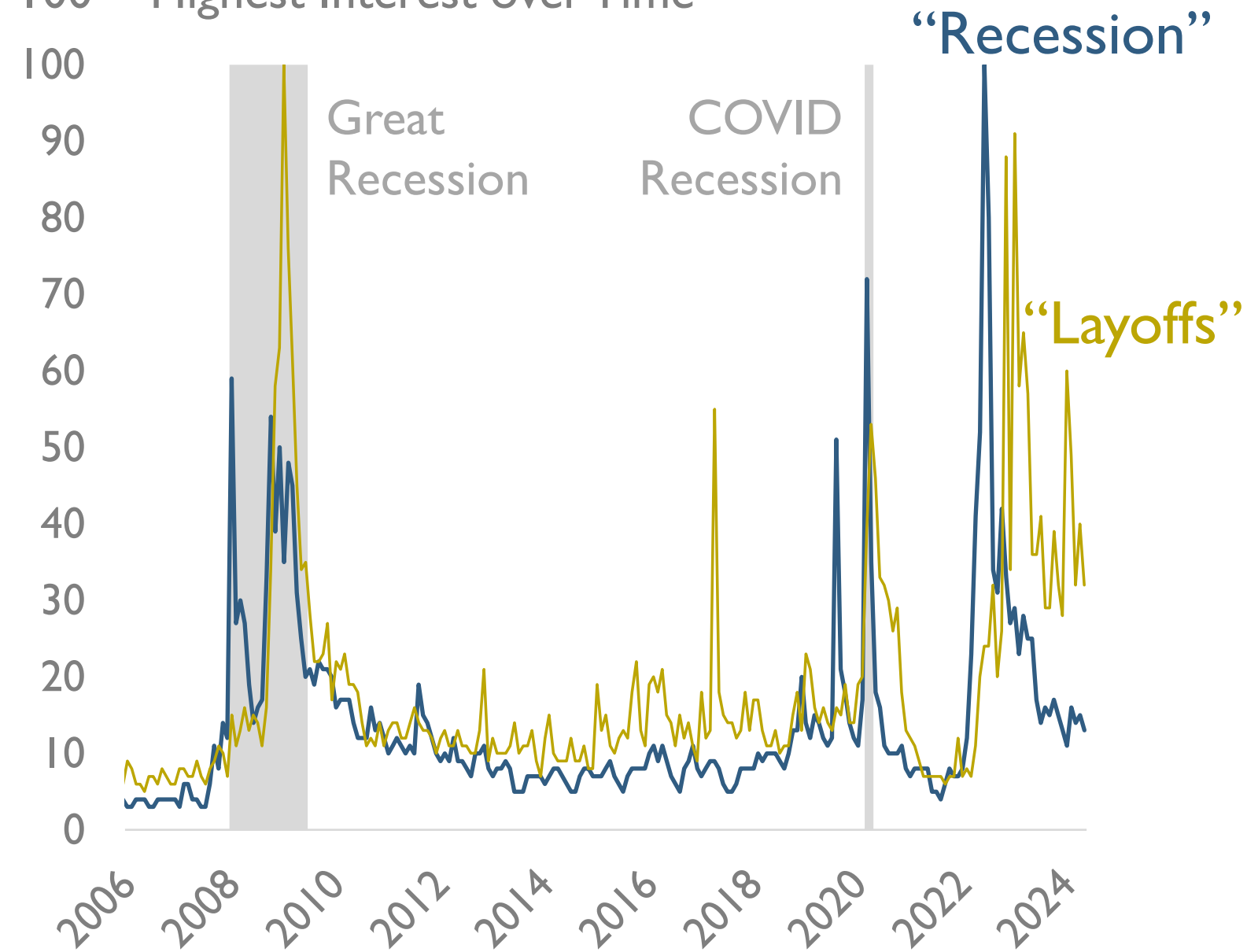
Inconsistent consumption of inconsistent economic information

Personalized echo-chamber

Perceptions of the economy disconnected from reality

Google Search Interest

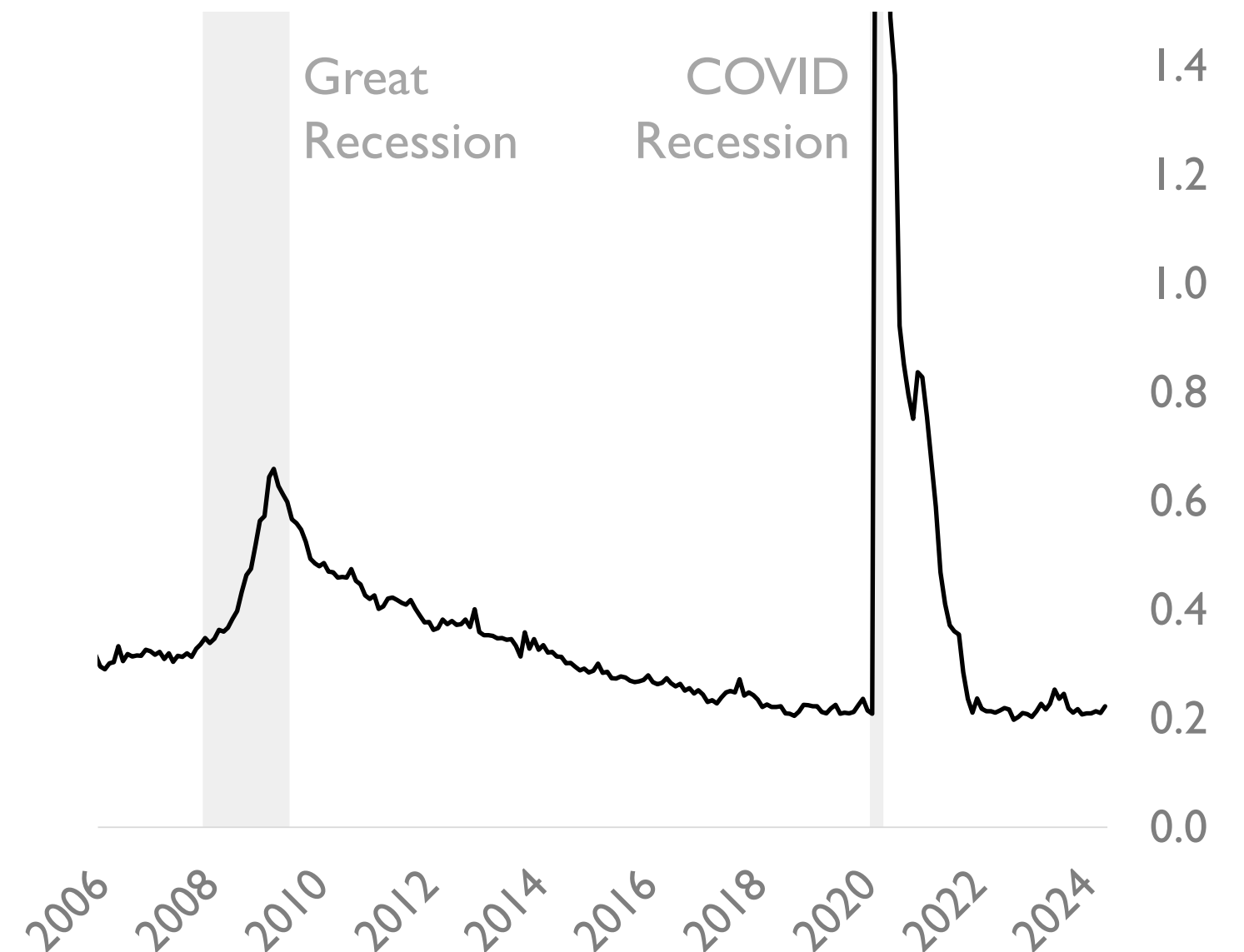
100 = Highest Interest over Time



Source: Google Trends. Based on United States search results; search of all categories of information sources.

U.S. Initial Unemployment Insurance Claims

Millions



Source: U.S. Department of Labor. Data are seasonally adjusted and through May 2024.

CONSUMER OUTLOOK SUMMARY

Expect a more cautious and conscientious consumer

- Post-pandemic “YOLO” spending easing
- Household stimulus payments exhausted
- Consumers shifting to lower-cost alternatives
- Consumer debt, delinquencies low but rising

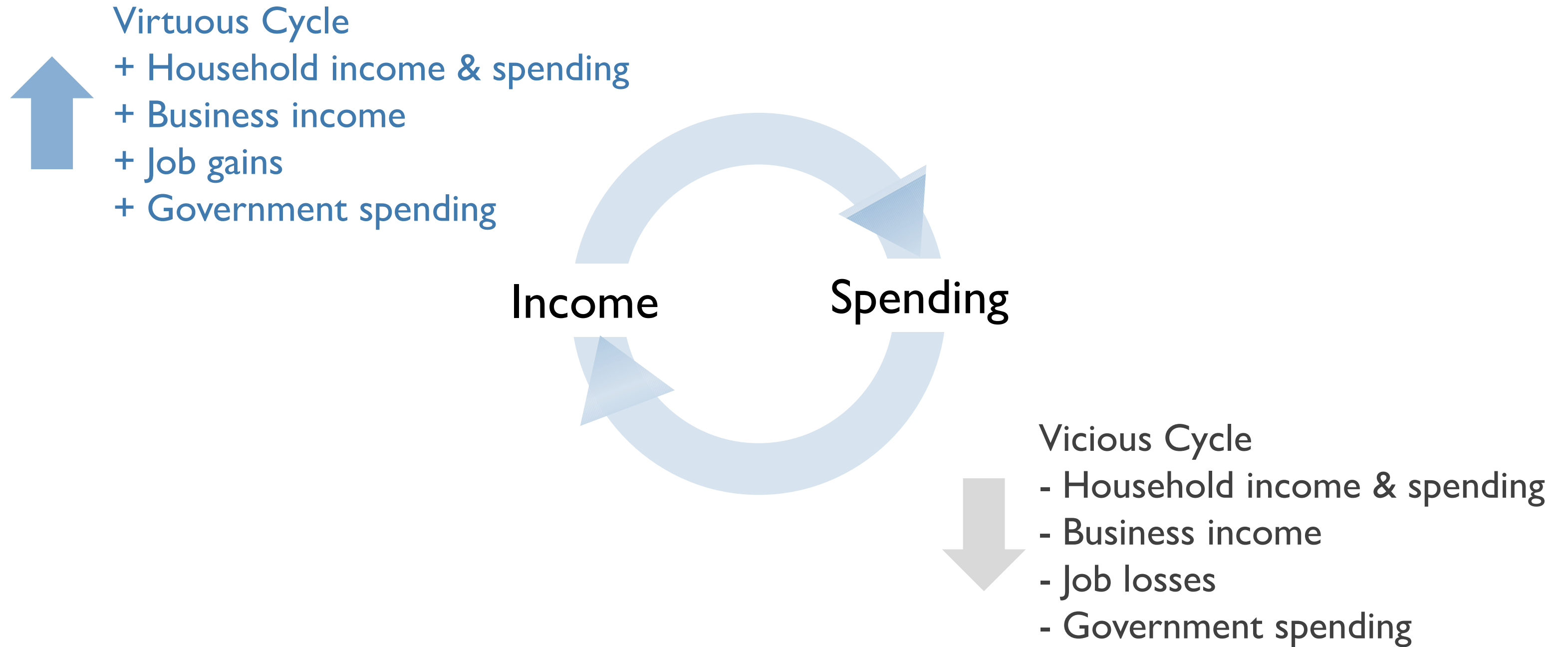
Sustaining Growth

- Real wage growth
- Savvy savers
- Strong equity markets

Slowing Growth

- End of pandemic stimulus
- Slower jobs growth
- Higher interest rates for longer
- Households without savings, investments, or low-mortgage homes pinched

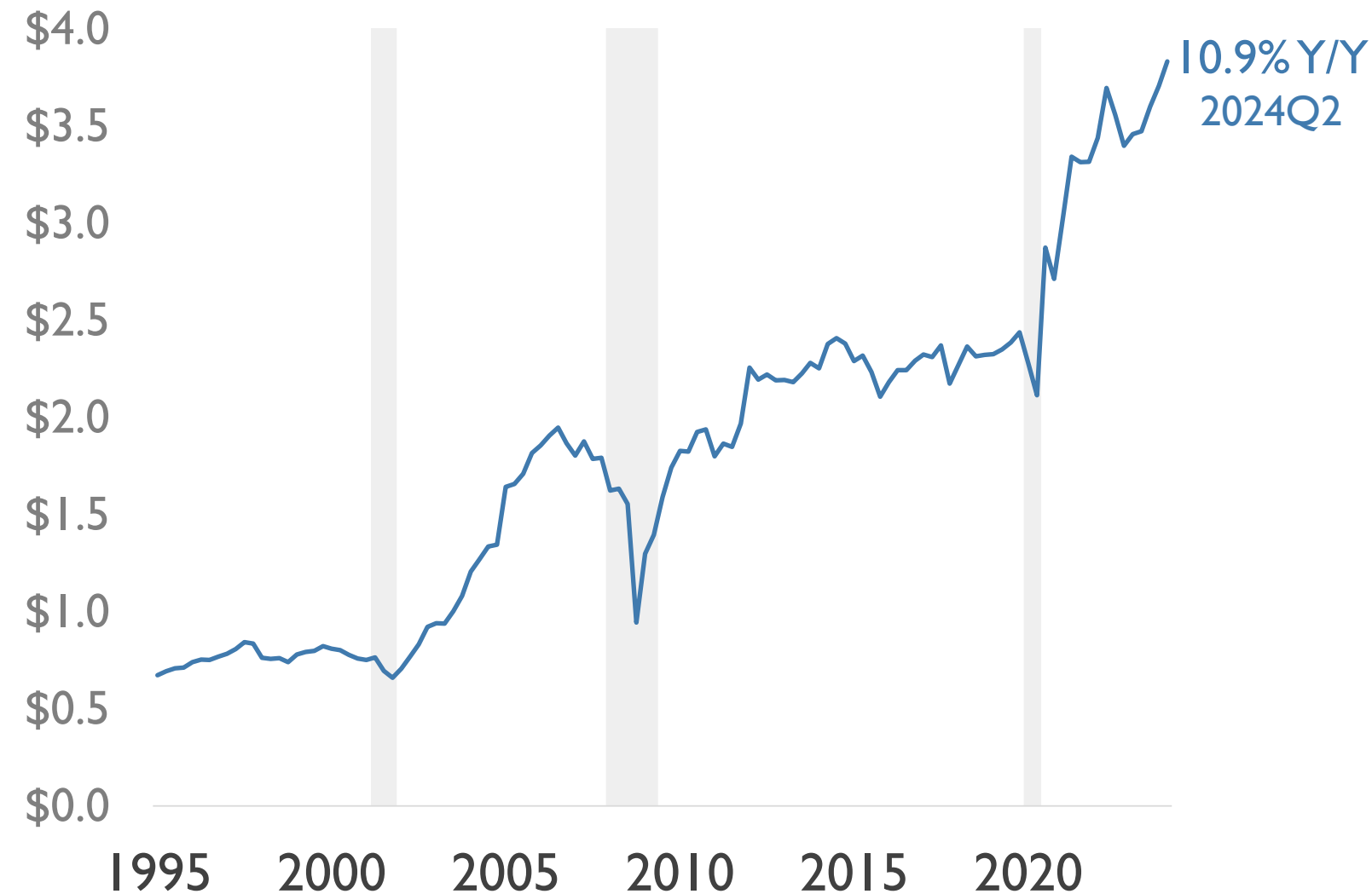
Interconnected economy



What's next for corporate income taxes?

U.S. Corporate Profits Before Tax

Trillions



Slowing Growth

- Consumer spending slowing
- Higher interest rate environment
- Some industries struggling

Sustaining Growth

- Input prices & labor shortages easing
- Consumer spending still growing
- Federal stimulus (IIJA, CHIPS, IRA)
- AI, automation providing labor savings

Source: U.S. Bureau of Economic Analysis. Seasonally adjusted annual rates.
Corporate profit amounts are without inventory valuation or capital consumption adjustments.

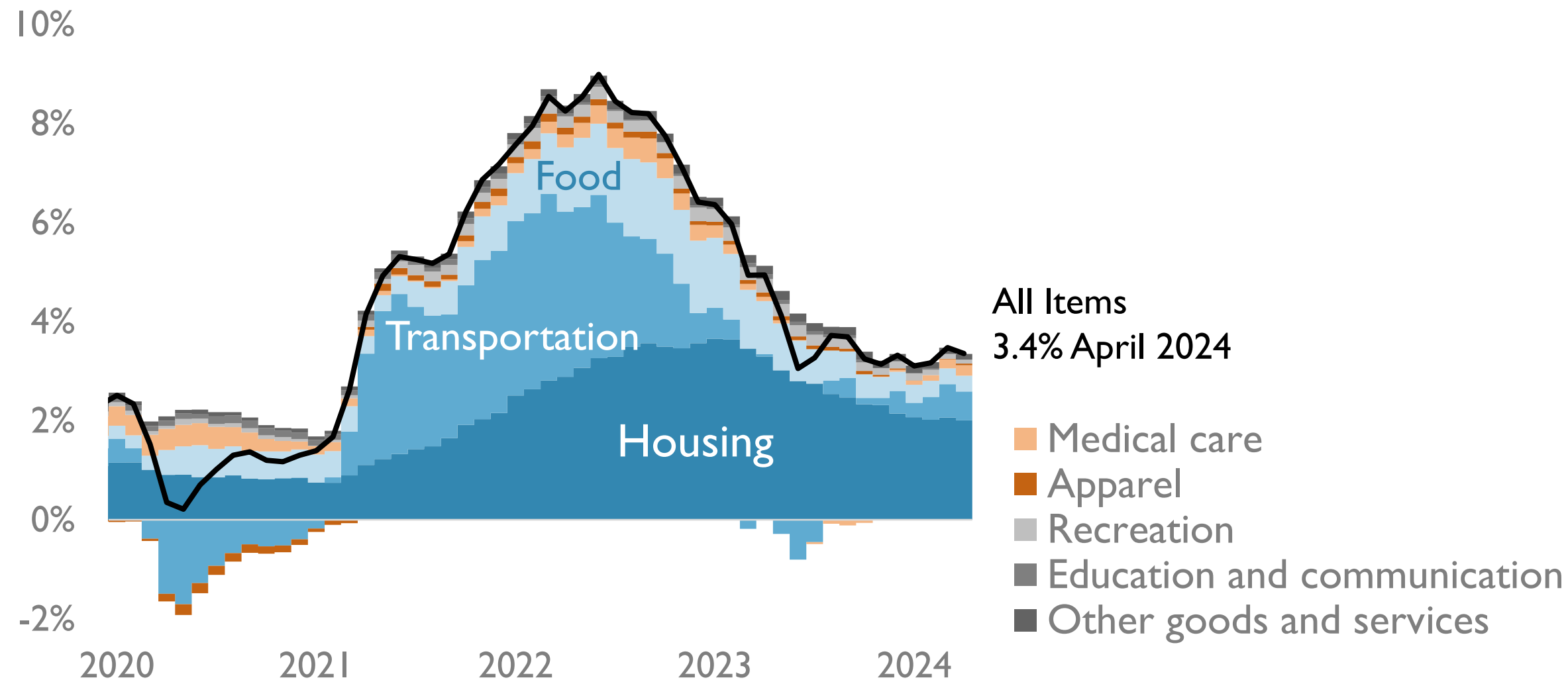
Federal spending continues to prop up growth

- **American Rescue Plan Act of 2021 (ARPA)**
 - \$1.9 trillion, including \$350 billion for state and local governments
- **Infrastructure Investment and Jobs Act of 2021 (IIJA)**
 - \$550 billion in new federal spending over 5-year period
- **Inflation Reduction Act of 2022 (IRA)**
 - \$145 billion allocated across many federal programs
 - Companies have announced \$115 billion in clean energy manufacturing investments
- **CHIPS and Science Act of 2022 (CHIPS)**
 - \$53 billion in federal funds investing in domestic manufacturing
 - Companies are investing hundreds of billions on top of these amounts

Consumer inflation has moderated but remains above Fed target

CPI-U Inflation, All U.S. Urban Areas

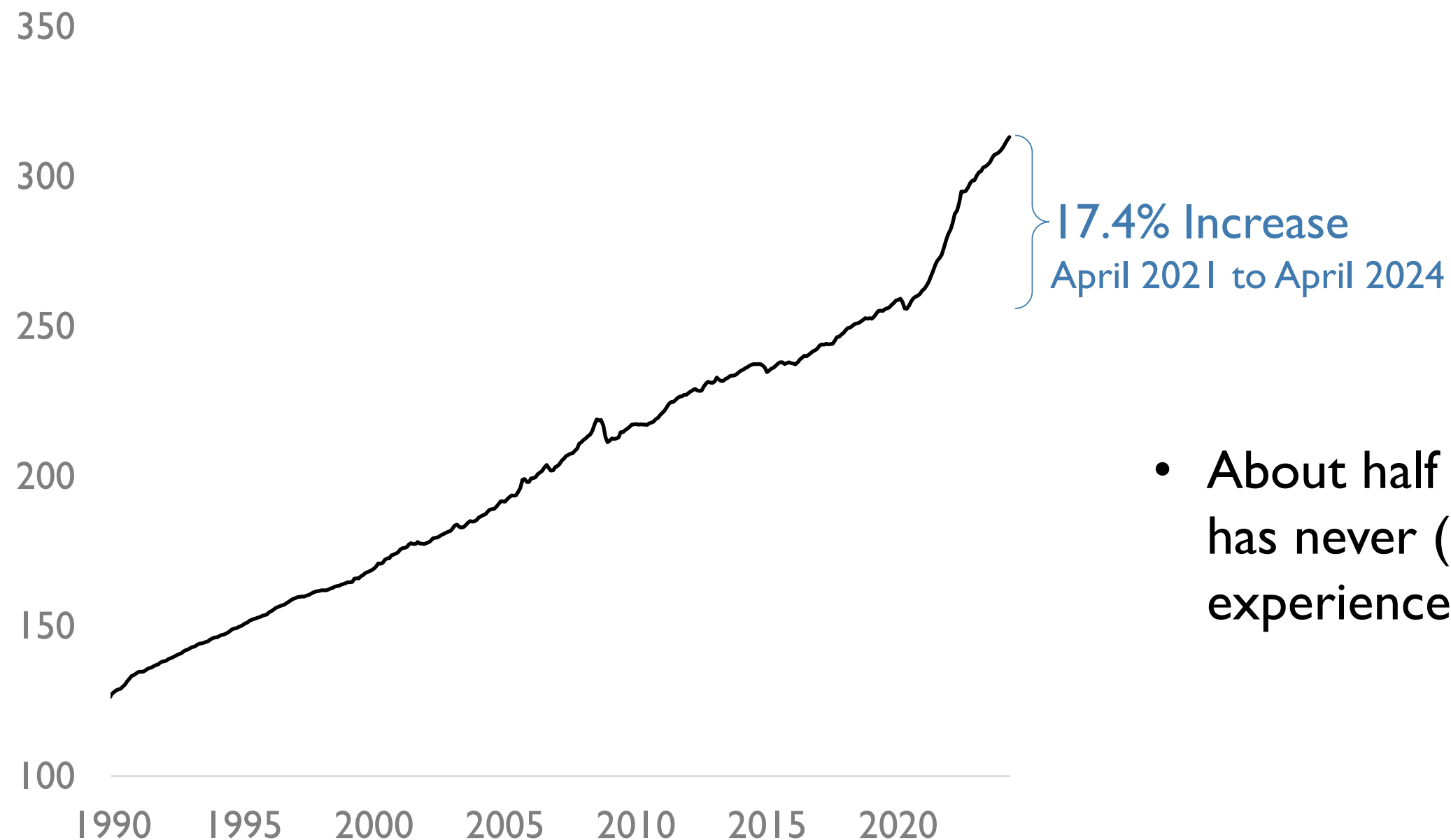
Contribution to Percent Change by Component



Source: Bureau of Labor Statistics with author's calculations using relative weights.

Consumers feeling the weight of price hikes, some much more than others

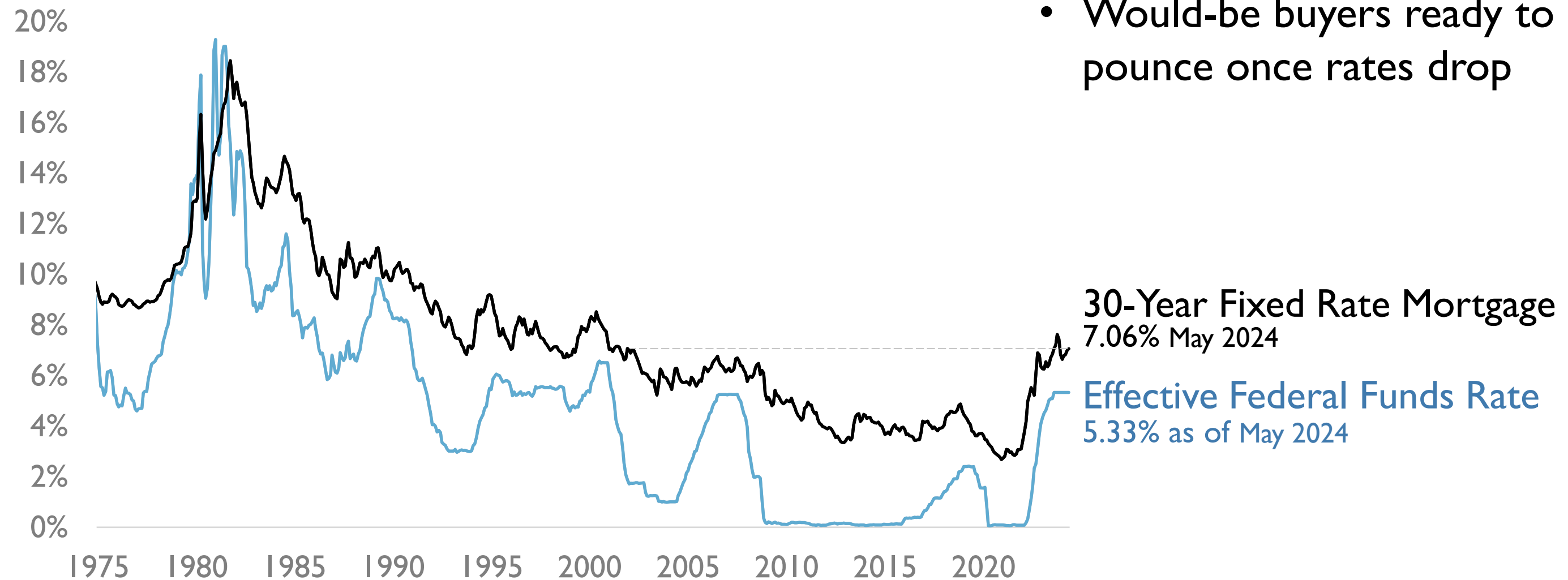
CPI-U Headline Index, All U.S. Urban Areas



- About half of the US population has never (or was too young to) experience inflation like this before

Monetary policy has slowed housing market activity

U.S. Interest Rates

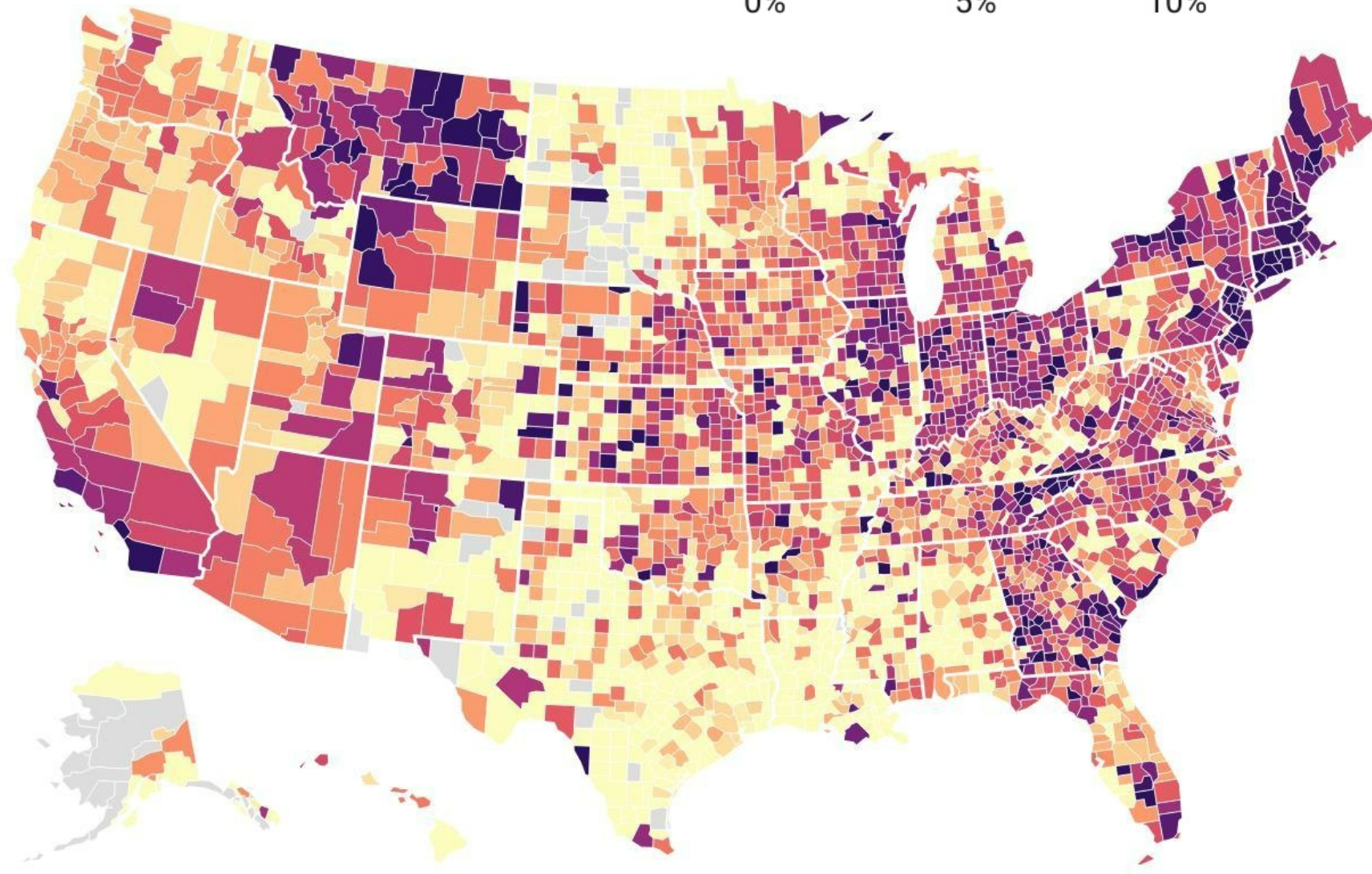
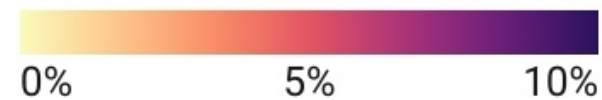


Source: Federal Reserve Board of Governors & Freddie Mac. Average monthly rates.

Home price appreciation varies by region; prices subdued by higher interest rates but still rising in many areas

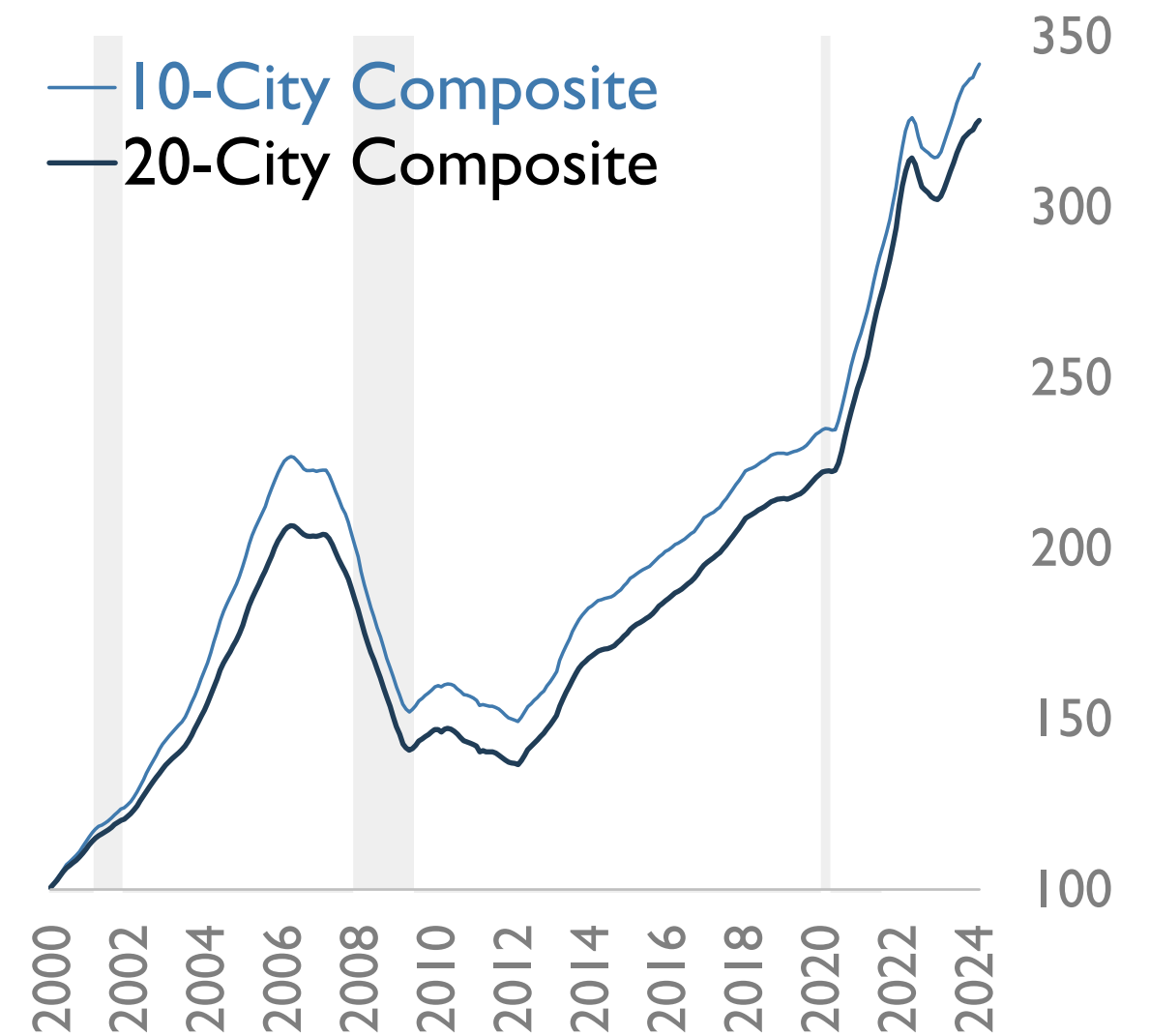
Change in Median Home Price, 2024Q2

Year-over-Year Percent Change



Case-Shiller Home Price Index

— 10-City Composite
— 20-City Composite



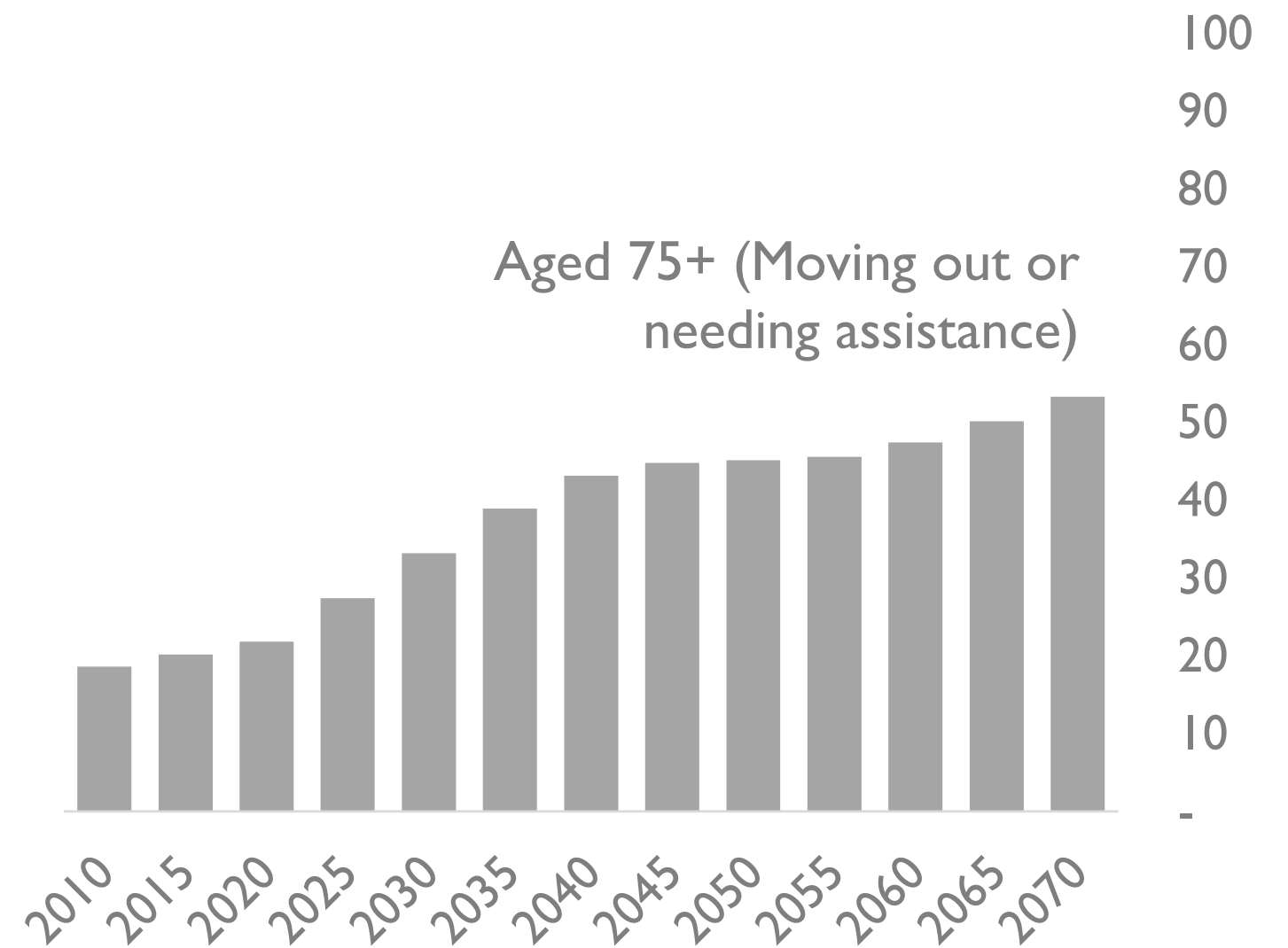
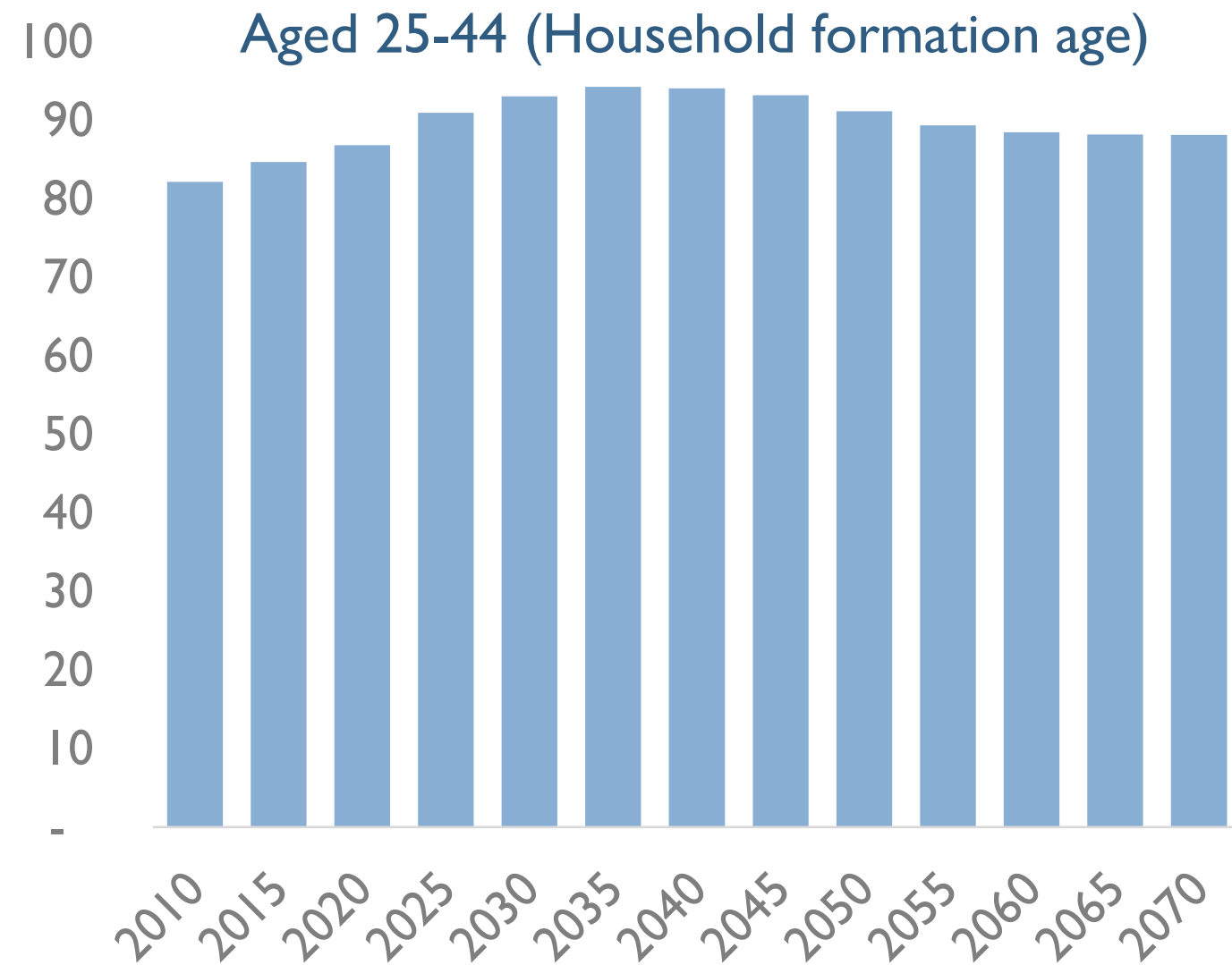
Source: G. Brian Davis, SparkRental Real Estate Blog. Underlying data from Zillow.
*****sparkrental.com/hottest-real-estate-markets/

Source: S&P Dow Jones Indices LLC.
Data are seasonally adjusted and through March 2024.

2025 undersupply, 2030 oversupply? Peak Millennial demand and the Boomer bust to come

Population by Age

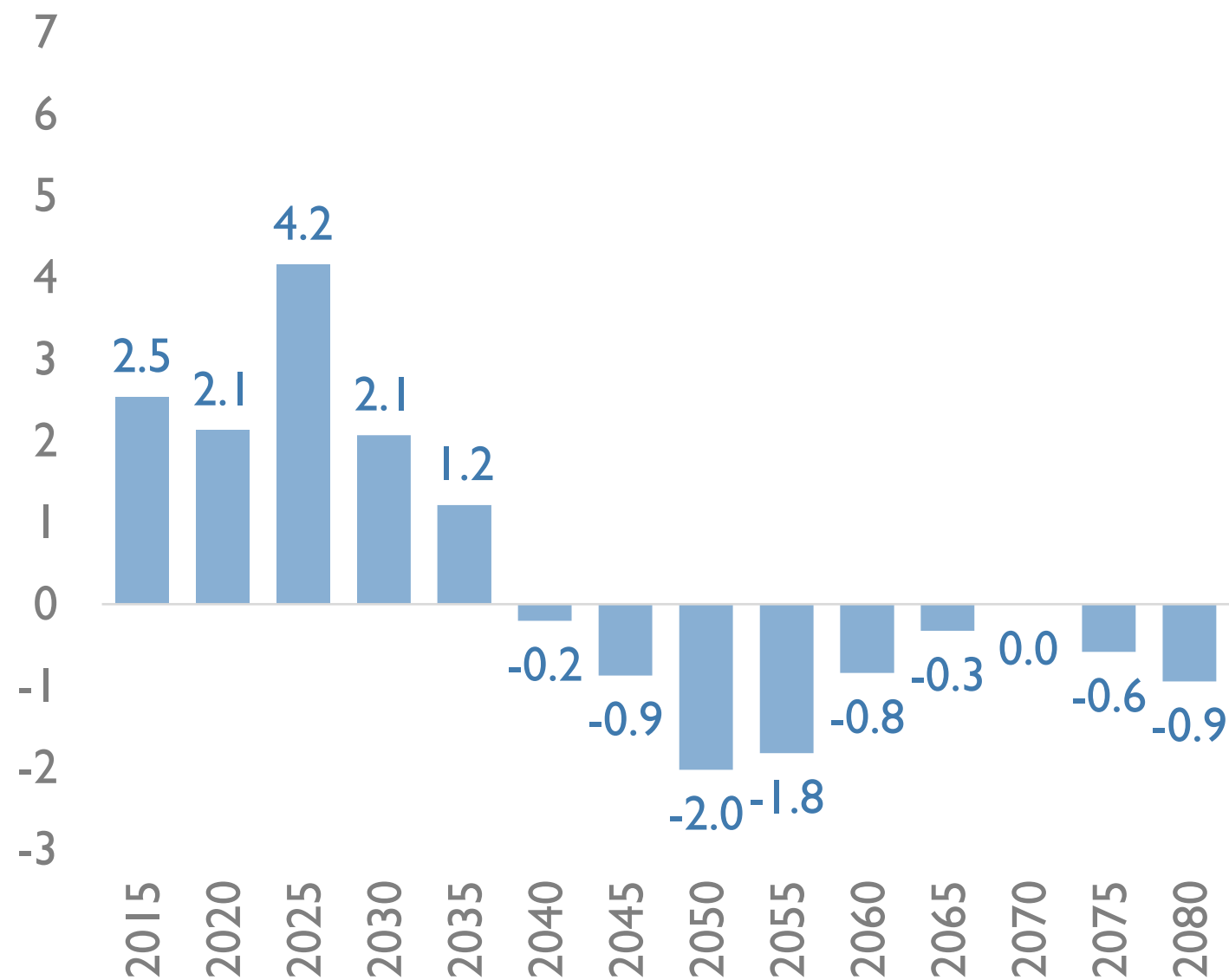
Millions



5-year change in the population...

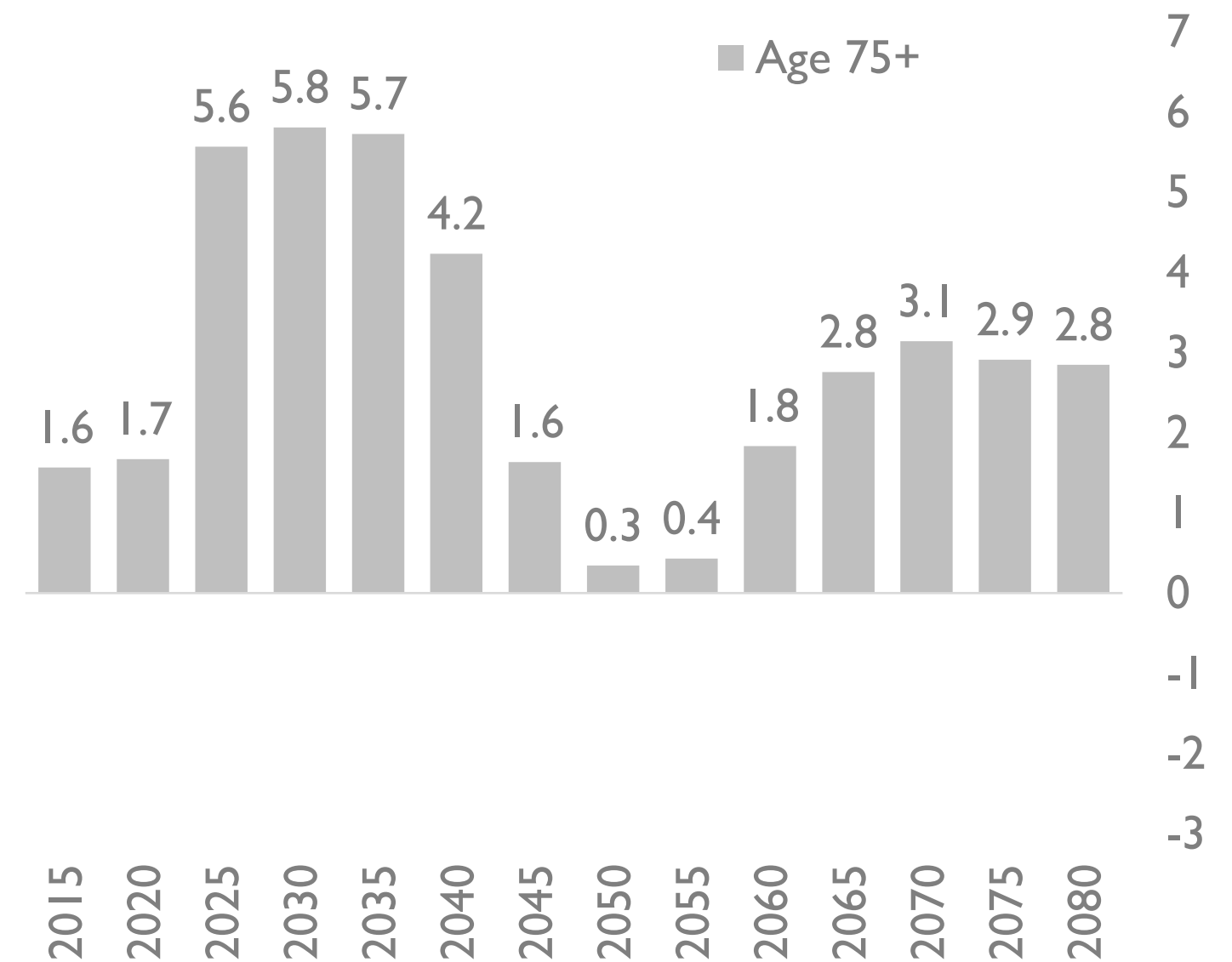
Moving In

Aged 25-44 (Household Formation Age), Millions



Moving Out or Needing Care

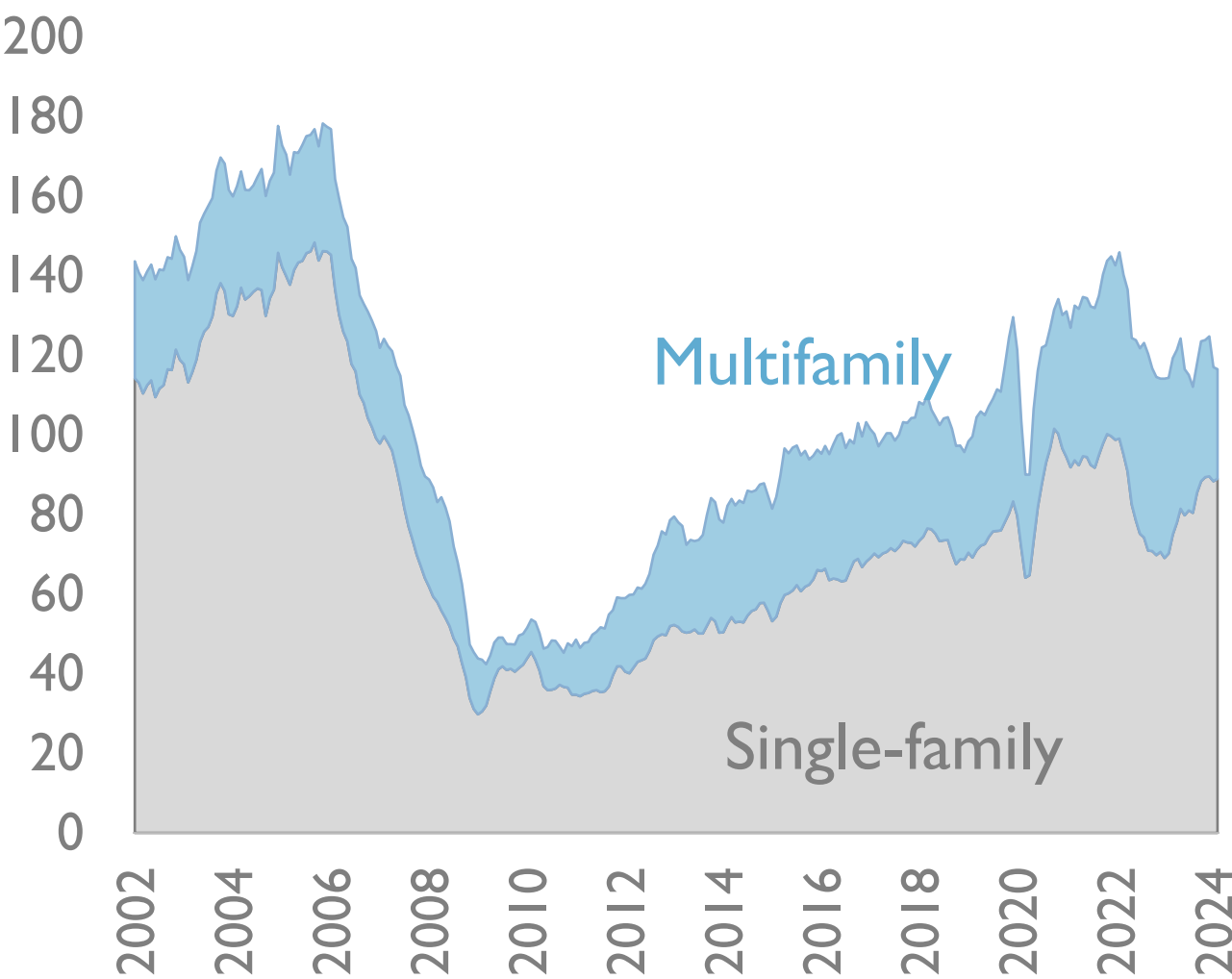
Aged 75+, Millions



Construction activity expected to weaken further on higher interest rates, labor shortages, CRE weakness

Permits for U.S. Housing Units

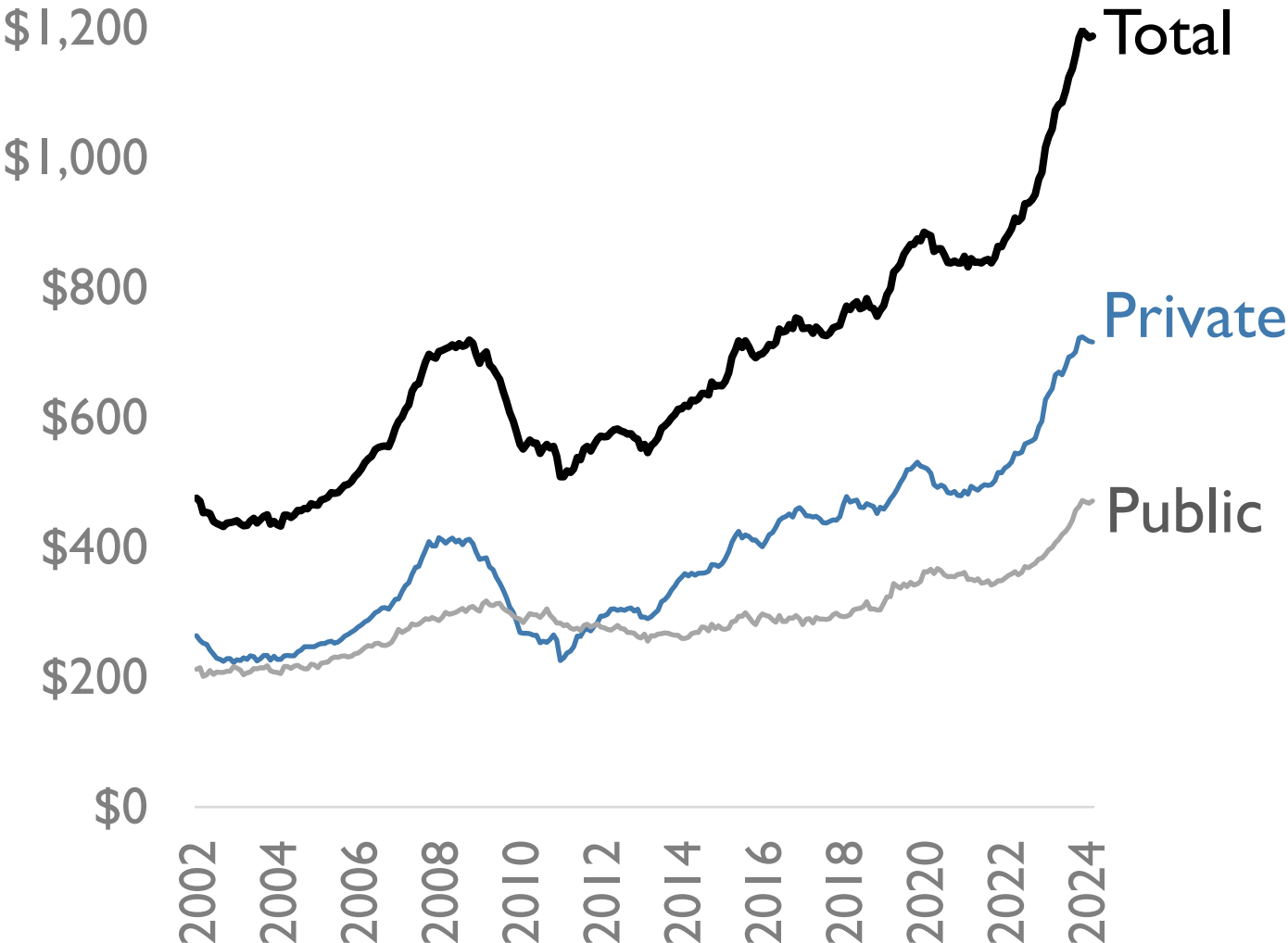
Monthly Permits Issued, 3-Month Moving Average



Source: U.S. Census Bureau. Data are seasonally adjusted and through April 2024.

Nonresidential Construction Spending

Billions



Source: U.S. Census Bureau. Data shown as seasonally adjusted annual rates and are through April 2024.

2024 Economic Outlook Summary

Economic Expectations

- Consumer activity reverting to trend
- Jobs growth will slow further
- Business activity mixed as consumers tighten spending
Federal spending continues to drive momentum in many sectors

State Budget Expectations

- Slow to no real sales tax growth
- More moderate wage withholding growth
- Softening in business income tax revenue; downside risks

2024 Economic Outlook Summary

Economic Expectations

- Inflation around 3%, rising from elevated price levels
- Interest rate cuts will come eventually, but near zero rates are unlikely to return anytime soon
- Home price appreciation subdued by interest rates but Millennial demand waiting in the wings for rate cuts

State Budget Expectations

- Ongoing state expenditure pressures
- Property tax revenue: Subdued growth due to interest rates; regionally-specific trends with slow to no growth in the highest cost areas

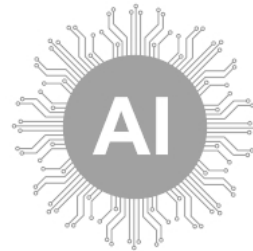
Risks to the outlook: Known uncertainties

Technological Change

How will social media shape a recession?

What does AI mean for the economy?

How will technological change impact state budgets?

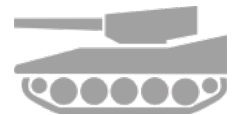


Geopolitical Risk

How could war, terrorism, or cybercrime impact states?

What will protection cost?

What will it mean for immigration?



Climate Change

What costs, crises, or revenue impacts could weather & natural disasters create?



Monetary & Fiscal Policy Risk

What happens if the federal debt gets too big?

Can federal funding remain as big as in the past?

Where will interest rates go next?



Demographics

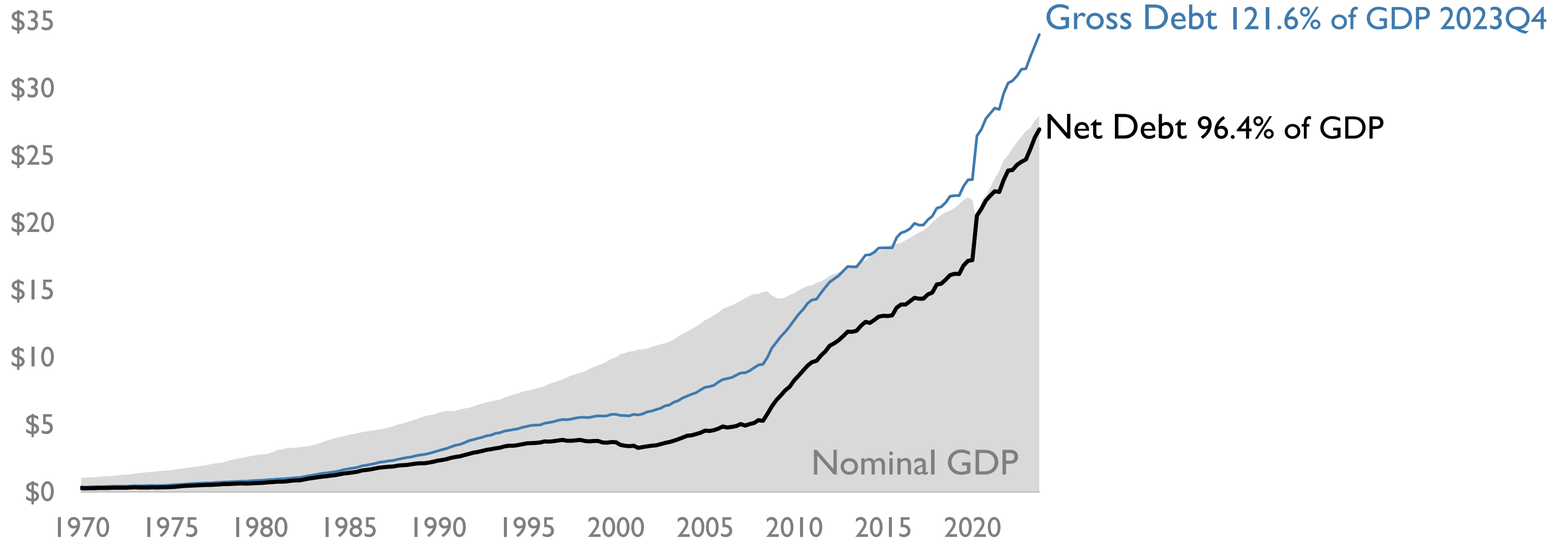
How will aging and lower birth rates impact the economy and state budgets?



What is the future of federal tax policy and spending?

U.S. Federal Debt & GDP

Nominal Amounts, Trillions of Dollars



Source: Office of Management and Budget and U.S. Bureau of Economic Analysis.

*Gross federal debt comprises both debt held by the public and debt issued to various accounts of the federal government, including the major trust funds in the budget (such as those for Social Security). Because the debt issued to those accounts is intragovernmental, it has no direct, immediate impact on the economy. Instead, it represents credits to the various government accounts that can be redeemed as necessary to authorize payments for benefits or other expenses.

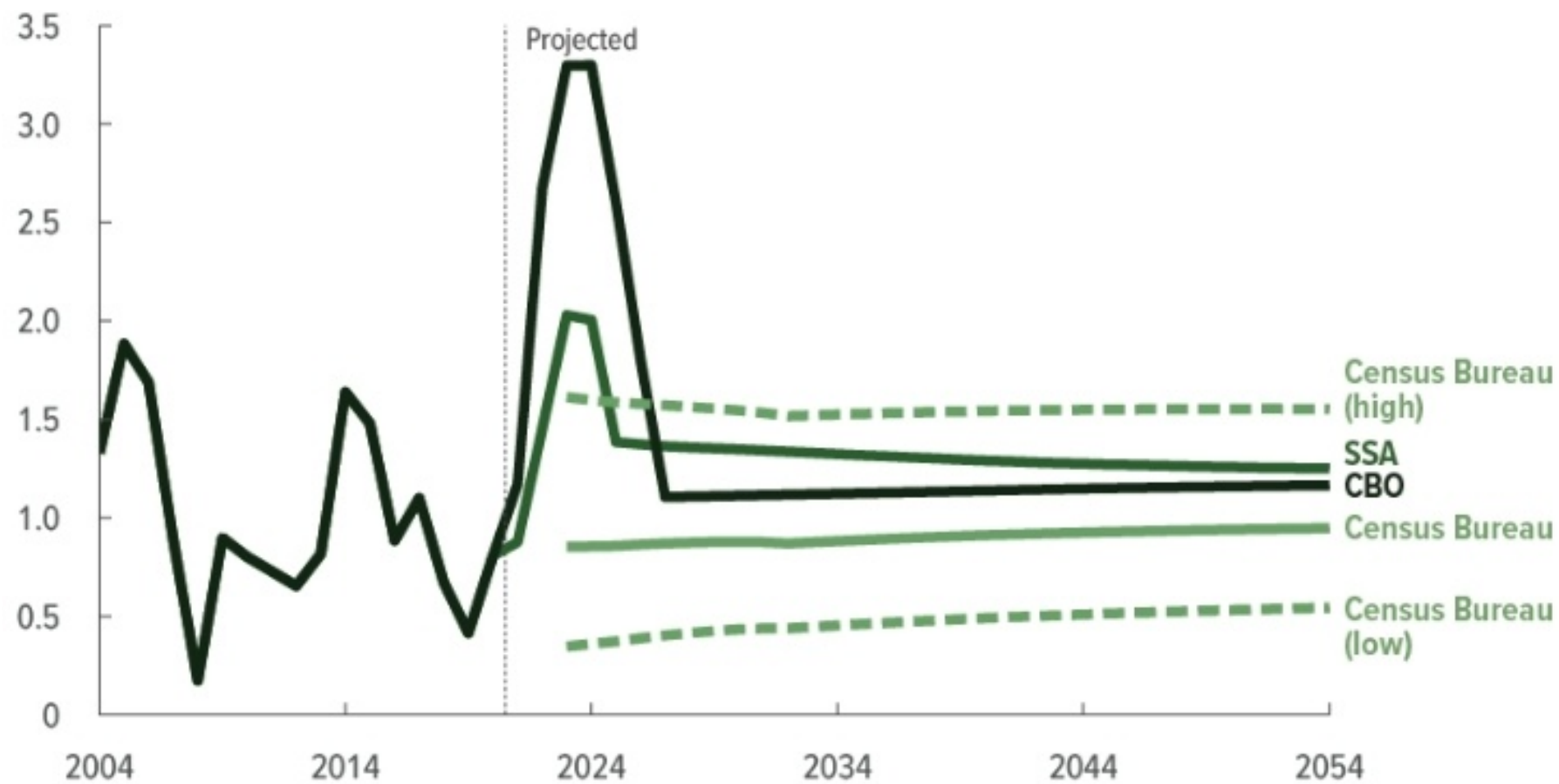
**Net federal debt is limited to debt held by the public.

Geopolitical risk, net migration, migration policy

Figure A-4.

CBO's and Other Agencies' Projections of Net Immigration

Millions of people



- Jobs are people
- More people means more income, consumption, and tax revenue

Questions?

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