U.S. Economic Outlook

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Lower rates on the horizon

To cut or not to cut (rates)? That is the question members of the Federal Open Market Committee (FOMC) will be debating later this month. Economic data is mixed, with coincident economic data such as employment growth showing continued strength while more forward-looking data such as business sentiment indices showing signs of softness. Furthermore, inflation readings have been below the Fed's expectations, something it hopes a rate cut could help correct. The FOMC will likely cut rates twice this year, trying to nudge inflation closer to its 2 percent target and offset the slowdown in U.S. manufacturing. With ongoing trade tensions feeding global economic softness, it's doubtful that Fed policy will be successful in boosting inflation and business demand.

One of the big modifications to the forecast this month is a downward revision to business investment over the entire forecast horizon. Ongoing uncertainty related to trade policy along with more modest global economic growth will likely keep business investment restrained for the near future. Businesses are expected to remain cautious at this late stage of the business cycle. Consumer spending, however, should remain relatively stronger following a soft first quarter as job gains and wage growth help to support further spending activity.

Key Takeaways

Expect two rate cuts from the Fed this year

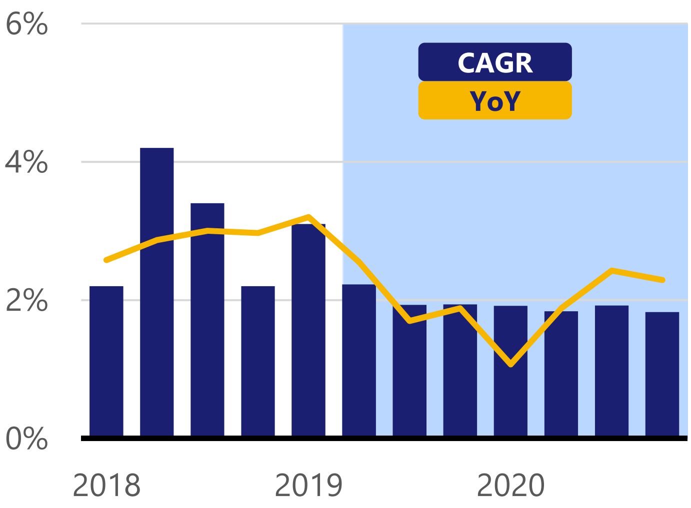
Business investment likely to remain soft

Consumer spending is still holding up

Credit availability concerns remain

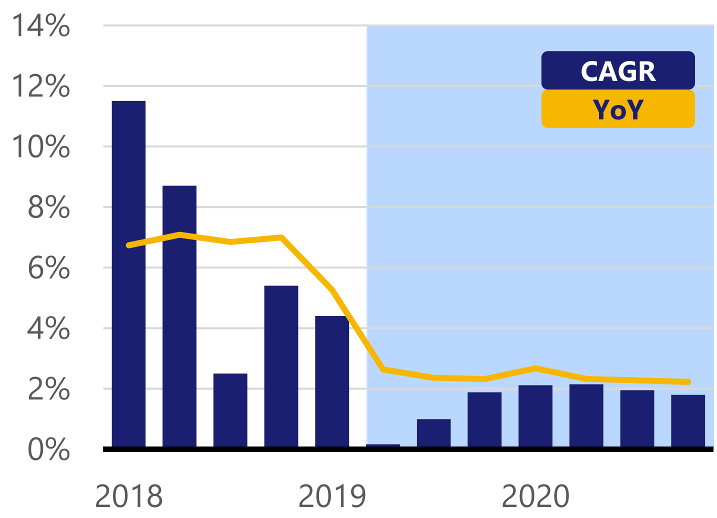
Real gross domestic product (SA, CAGR and YoY percent change)

Last forecast: July 2019



Real business fixed investment (SA, CAGR and YoY percent change)

Last actual: July 2019



Source: Visa Business and Economic Insights and U.S. Department of Commerce

Lower rates on the horizon (cont.)

Consumer spending bounces back in Q2

Consumer spending appears to have bounced back in Q2 to around 3.7 percent on an annualized basis. June's blockbuster jobs report showing 224,000 jobs added for the month suggested that momentum behind consumer spending is likely to continue. That said, there are signs that consumers are growing weary of future economic conditions. Consumer confidence slid in June to the lowest level since September 2017, with consumer expectations of future economic conditions falling back to levels not seen since January of this year during the government shutdown and equity market sell-off. While a one-month slide is not concerning, it comes as manufacturing activity remains particularly soft, suggesting a more modest pace of consumer spending is likely in the second half of the year.

Beware of further slowdowns in business investment

The ISM Manufacturing Index, a key gauge of sentiment in the sector, continued to slide in June to 51.7, the lowest reading since October of 2016. Industrial production as of May is only up 0.7 percent since last year—disappointing for an economy growing between 2.5-3.0 percent. While there have been adverse effects on the sector due to U.S. trade policy and global growth concerns, these issues may mask a more concerning underlying trend: that businesses have become less optimistic about the prospects for U.S. economic growth. With rate cuts from the Federal Reserve on the horizon, business investment will be closely watched for signs of a rebound. Will this business cycle be prolonged further, or are businesses preparing for a slower growth environment?

Key risks to the outlook

Since the last FOMC meeting, where clear signals emerged that rate cuts may be needed, the yield curve (which measures the difference between short and long-term interest rates) became more inverted. Historically, such significant inversions have led to a drying up of credit as lending became less profitable. Thus, one reason to believe that the rate cuts from the Fed may not be as effective this time around is this inverted yield curve environment. The continued inversion may slow lending activity rather than boost it, even with a rate cut.

U.S. Economic Forecast

	Actual				Forecast				Actual		Forecast	
	2018				2019							
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	2017	2018	2019	2020
Gross Domestic Product (CAGR)	2.2	4.2	3.4	2.2	3.1	2.2	1.9	1.9	2.2	2.9	2.6	1.9
Personal Consumption	0.5	3.8	3.5	2.5	0.9	3.7	2.4	2.3	2.5	2.6	2.5	2.4
Business Fixed Investment	11.5	8.7	2.5	5.4	4.4	0.2	1.0	1.9	5.3	6.9	3.2	1.8
Equipment	8.5	4.6	3.4	6.6	-1.0	-1.6	-0.5	1.1	6.1	7.4	1.4	0.9
Intellectual Property Products	14.1	10.5	5.6	10.7	12.0	5.5	5.0	4.8	4.6	7.5	8.3	4.5
Structures	13.9	14.5	-3.4	-3.9	4.3	-5.8	-2.5	-1.5	4.6	5.0	-0.8	-1.2
Residential Construction	-3.4	-1.3	-3.6	-4.7	-2.0	0.0	1.5	2.2	3.3	-0.3	-1.6	1.7
Government Purchases	1.5	2.5	2.6	-0.4	2.8	4.3	2.6	2.3	-0.1	1.5	2.4	2.2
Net Exports Contribution to Growth (%)	0.0	1.2	-2.0	-0.1	0.9	-0.5	-0.3	-0.3	-0.3	-0.2	-0.1	-0.3
Inventory Change Contribution to Growth (%)	0.3	-1.2	2.3	0.1	0.6	-0.9	-0.1	-0.1	0.0	0.1	0.2	-0.1
Nominal Personal Consumption (YoY % Chg.)	4.3	4.9	5.2	4.5	4.1	4.2	4.1	4.0	4.3	4.7	4.1	4.2
Nominal Personal Income	4.3	4.5	4.5	4.3	3.8	4.1	4.4	4.6	4.4	4.4	4.2	4.2
Retail Sales Ex-Autos	5.3	6.3	6.4	3.9	3.0	3.2	3.2	4.4	5.0	5.5	3.5	4.1
Consumer Price Index	2.2	2.7	2.6	2.2	1.6	1.8	1.9	2.3	2.1	2.4	1.9	1.8
Federal Funds Rate (Upper Bound)	1.75	2.00	2.25	2.50	2.50	2.50	2.00	2.00	1.25	2.13	2.25	2.00
Prime Rate	4.75	5.00	5.25	5.50	5.50	5.50	5.00	5.00	4.10	4.90	5.25	5.00
10-Year Treasury Yield	2.74	2.85	3.05	2.69	2.41	2.00	2.10	2.13	2.33	2.91	2.16	2.24

Forecast as of: July 11, 2019

Interst rates presented are end of quarter rates

Note: Annual numbers represent year-over-year percent changes and annual averages

Sources: Visa Business and Economic Insights, U.S. Department of Commerce, U.S. Department of Labor and Federal Reserve Board

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