Industry Snapshots

Arrow denotes 12-month moving total/average direction.

RETAIL SALES	Mild Rise
WHOLESALE TRADE	Flat
AUTO PRODUCTION	Mild Rise
MANUFACTURING	Mild Decline
ROTARY RIG	Flat
CAPITAL GOODS	Mild Rise
NONRESIDENTIAL CONSTRUCTION	Steep Rise
RESIDENTIAL CONSTRUCTION	Mild Decline

Steep Rise · *Mild Rise* · *Flat* · *Mild Decline* · *Steep Decline*

Macroeconomic Outlook

US Real Gross Domestic Product in the second quarter came in 2.6% above the prior year. However, while consumer and business-to-business spending trends are above the year-ago level, the economy is slowing.

We anticipate that the headwinds currently facing the economy will eventually prevail. Our expectation is for a mild recession for the overall economy in 2024. Industrial Production will generally decline next year, and we anticipate two quarters of real GDP contraction in 2024 as well. The signs of upcoming decline are varied and widespread. Interest rates, at their highest level in decades, are creating higher borrowing costs, which is contributing to slowing macroeconomic demand. On the consumer side, which makes up more than two-thirds of US Real Gross Domestic Product, finances are weakening. Excess savings, which were built up during the pandemic, have been eroded by general spending and rising prices; consumers are leaning more heavily on debt to fund their spending. While metrics like credit card delinquency rates are rising, they remain well below the levels leading up to the Great Recession, which supports our expectation that the downturn next year will not be a repeat of that period.

> *"We anticipate that the headwinds currently facing the economy will eventually prevail."*

Decline next year will not be felt evenly. Industries which rely more heavily on financing, such as construction machinery or larger capital investments, are likely to pull back more sharply than those industries for which demand is relatively inelastic, such as food or medical. Industries which have government backing, such as defense, semiconductors, infrastructure, and renewable energy, are also likely to fare relatively well during the upcoming downturn.

We are beginning to see green shoots from the housing market. Since this industry leads the macroeconomy by roughly one year, recovery in the residential construction sector bodes well for recovery in the broader economy in late 2024. We continue to monitor this and other leading indicators for signs of recovery and rise in late 2024 and beyond.

Make Your Move

Make sure you know your end markets' sensitivity levels to interest rates. Markets that are more sensitive to interest rates will likely face a greater pullback in demand than less sensitive markets leading up to, and during, the upcoming recession.

Investor Update

The S&P 500 ended July at 4,589, coming in 3.7% below the all-time month-end high of 4,766, which was established at the end of 2021. However, increasing recessionary risks from high interest rates, credit tightening, and associated financial stress suggest potential turmoil later this year.

ITR Economics Long-Term View

2023	2024	2025
SLOWING GROWTH	RECESSION	GROWTH

Leading Indicator Snapshot

	3Q2023	4Q2023	1Q2024
ITR Leading Indicator™	🔴	🔴	🟢
ITR Retail Sales Leading Indicator™	🔴	🔴	🔴
US OECD Leading Indicator	🔴	🟢	🟢
US ISM PMI (Purchasing Managers Index)	🔴	🔴	🔴
US Total Industry Capacity Utilization Rate	🔴	🔴	⚪

🟢 *Denotes that the indicator signals cyclical rise for the economy in the given quarter.*

🔴 *Denotes that the indicator signals cyclical decline for the economy in the given quarter.*

⚪ *N/A*

KEY TAKEAWAYS

- The US Total Industry Capacity Utilization Rate declined further in June. Descent in this leading indicator suggests that the US industrial sector will remain on the back side of the business cycle into at least the beginning of 2024.
- Both the US OECD Leading Indicator and US ISM PMI (Purchasing Managers Index) moved higher. However, numerous economic headwinds suggest that the annual rate-of-change for US Industrial Production is likely to continue declining into 2024.
- Ongoing decline in the ITR Retail Sales Leading Indicator™ suggests that the Retail Sales annual rate-of-change will decline further in the coming quarters.

Industry Analysis

RETAIL SALES

- Annual US Total Retail Sales totaled $8.2 billion in July, 5.2% above the year-ago level
- Prior inflation has negatively impacted consumers' purchasing power; when adjusted for inflation, accumulated savings are declining
- Some decline in annual Retail Sales in 2024 is likely

WHOLESALE TRADE

- US Total Wholesale Trade in the 12 months through June was up 3.5% from the same period one year ago
- Particularly in the case of durable goods, distributors are seeing growing excess inventories
- Wholesale Trade of Nondurable Goods may be more insulated from decline in 2024 than Durable Goods, given the nondiscretionary nature of some nondurable markets such as food

AUTO PRODUCTION

- Annual North America Light Vehicle Production through June was up 14.8% from last year
- Inventories are increasing as demand slows
- High borrowing costs will hinder some consumer demand for large, financed purchases; Production decline is likely in 2024

MANUFACTURING

- Annual US Total Manufacturing Production is mildly declining
- Annual Total Manufacturing New Orders have ticked down mildly in recent months, signaling further decline for Production is likely
- Elevated interest rates will continue to hamper the manufacturing sector into 2024

ROTARY RIG

- The US Rotary Rig Count was 11.1% below the year-ago level in July
- Tightening credit conditions will put downside pressure on the Rig Count
- Demand for oil and gas will decline amid upcoming macroeconomic weakness, putting further downside pressure on the Rig Count

CAPITAL GOODS NEW ORDERS

- Annual US Nondefense Capital Goods New Orders (excluding aircraft) were 3.7% above the year-ago level in June
- Unfilled orders trends signal elevated but plateauing backlogs; the loosening supply chain will allow businesses to fill orders more quickly
- Risk of order cancellation is higher on the back side of the business cycle

TOTAL NONRESIDENTIAL CONSTRUCTION

- Annual US Total Nonresidential Construction totaled a record $996.4 billion in June, up 14.5% from last year
- Downward movement in corporate profits suggests Construction will transition to a slowing growth trend in the near term
- Declining prices will put downside pressure on dollar-denominated Construction

TOTAL RESIDENTIAL CONSTRUCTION

- Annual US Total Residential Construction in June dropped below year-ago levels for the first time since before the pandemic
- Decline is stemming from single-family construction
- In June, annual US Private Single-Family Residential Construction was 13.6% below the year-ago level, while annual Private Multi-Family Residential Construction rose to 13.7% above the year-ago level

A Closer Look: The US Economy

Interest Rates, Yield Curves, and Downgrades, Oh My!

LAUREN SAIDEL-BAKER

What you need to know: "Noise" is likely to increase as the political season picks up. Do not equate headlines with economic fundamentals

Far from the quiet summer ideal, full of out-of-office messages and calm markets, July and August of this year have been a time of attention-grabbing headlines. Both consumers and businesses are becoming more cautious amid high inflation, still-rising interest rates, and several lackluster data releases. However, the alarmist headlines should not signal concern for business leaders who have been planning for a mild recession in 2024. These developments, while unpleasant, are typically associated with the back side of the business cycle.

GOVERNMENT FISCAL POLICY LEADS TO RATINGS DOWNGRADE, BUT THIS IS NO SURPRISE

In early August, Fitch Ratings downgraded the US long-term credit rating from the highest-possible AAA rating to AA+, citing the country's mounting debt burden and lack of political will to address the deficit. This downgrade follows fellow rating agency S&P's downgrade of the US in 2011 for similar reasons. Almost at the same time, the US Department of the Treasury increased its borrowing estimate for the current fiscal quarter to over $1 trillion. In tandem, these factors will likely affect near-term US Treasury yields in a way that could be read as spooking investors.

While these concerns are valid, they relate to the longer-term outlook rather than the immediate future. As such, we do not expect a significant impact on the 2024 recession. The mounting US government debt load is a key factor in our long-held outlook for a depression around 2030.

Instead, we will be tracking the ongoing yield curve inversion as a gauge of near-term market sentiment. ITR Economics' preferred comparison – the 10-year to 3-month yield – remains inverted as of this writing. If the yield curve does not normalize by late this year or early next year, this market signal may portend a longer or steeper recession in 2024 than currently forecast. Higher debt issuance and credit ratings downgrades will temporarily affect yields but are not a harbinger of steeper-than-anticipated recession.

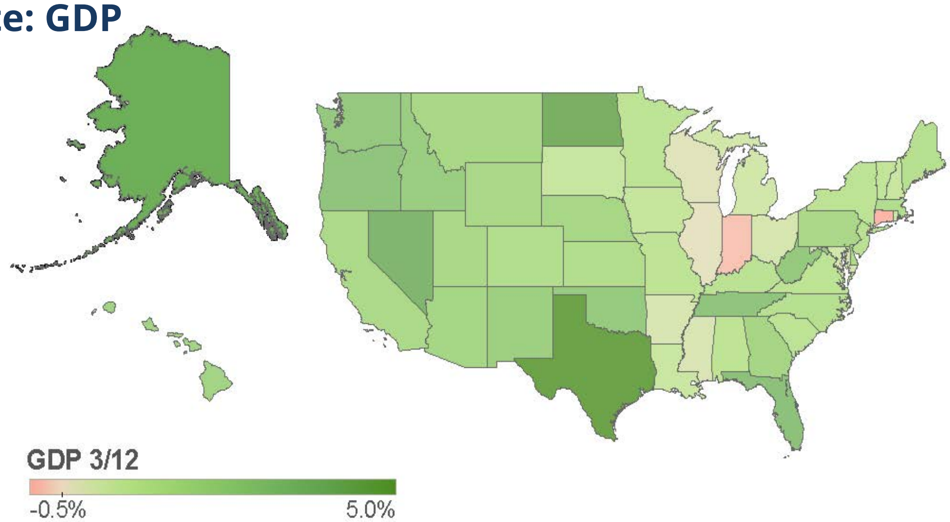
THIS IS NOT WHAT A BANKING CRISIS LOOKS LIKE

In the wake of recent banking sector strife, including the collapse of Silicon Valley Bank, the downgrade to the US credit rating and subsequent downgrades to certain banks made headlines. Yet, the overall financial sector remains resilient, with a commercial and industrial loan charge-off rate of just 0.25%. On the consumer side, auto loan delinquencies are near their five-year low, the credit card delinquency rate of 2.53% is below the pre-COVID 10-year average, and the residential mortgage delinquency rate of 1.74% is the lowest in more than 16 years.

Make no mistake: A downturn is coming. US consumers are becoming more price conscious in the face of high inflation, and businesses are tightening their belts as corporate profits soften. However, the stable base of strong consumer and business finances will provide resiliency at the bottom of the cycle.

The industrial economy will be in Phase D, Recession, by early 2024. As the economy traverses the back side of the business cycle, ominous headlines will mount. It will be increasingly crucial for business leaders to differentiate between "new news" and the reporting of data and events that develop in line with the outlook. You have prepared for the low of the business cycle; now stay the course.

State-by-State: GDP



- US Real Gross Domestic Product (GDP) in the second quarter was 2.6% above the year-ago level.
- Real GDP rose in the first quarter in all but two states: Indiana and Connecticut.
- The West and Southwest regions grew at the fastest pace, with Texas leading all states at 5.0% above the year-ago level.
- States in the Great Lakes and Northeast regions grew at a milder pace; these regions have less favorable demographic trends.

Readers' Forum

What are the key factors that play into ITR's forecast for a 2030s Depression?

Sara Aybar, Economist at ITR Economics™, answers:

US National Debt:

The current US national debt is above $30 trillion. Due to current spending trends, demographics, health care costs, and entitlement programs will lead to a larger debt. Payment on that debt is going to become increasingly difficult as it grows during the next decade.

Demographics:

The baby boomer generation will largely be out of the workforce by the 2030s. Given the generation's size, this shift will put a strain on social programs like Social Security and Medicare. This will amplify the national debt issues and will likely lead to higher taxes on younger generations paying into the programs.

Health Care Costs:

Health care costs are likely to increase for all. With the baby boomer generation reaching higher ages, the number of people needing and receiving health care also increases. This will put additional strain on the health care system and costs.

Entitlements:

At the current rate, there is not going to be enough funding for programs like Social Security, Medicare, and prescription drug assistance.

Inflation:

Federal deficit spending will likely be a common trend as the 2020s continue, with decline in the value of the US dollar a likely consequence. If the US dollar is weakened, we experience higher inflation. Higher inflation will eat into consumers' ability to spend, leading to decreased demand for goods and services.

Please send questions to: questions@itreconomics.com

ITR Economist and Speaker Taylor St. Germain Is the New Host of TrendsTalk

ITR Economist and Speaker Taylor St. Germain has taken over as the official host of TrendsTalk, our popular weekly podcast-style show.

Taylor has many years of expertise consulting for small businesses, trade associations, and Fortune 500 companies across many industries. Taylor's expert insights help hundreds of companies greatly improve their business strategy and planning.

You don't want to miss out on the actionable advice Taylor provides to business leaders each week. Be sure to subscribe to our YouTube channel and follow ITR Economics to catch a new episode of TrendsTalk every Friday!

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