NATIXIS INVESTMENT MANAGERS | SOLUTIONS

MACRO COMMENTARY | October 2024

PORTFOLIO ANALYSIS & CONSULTING

Charts and Smarts®

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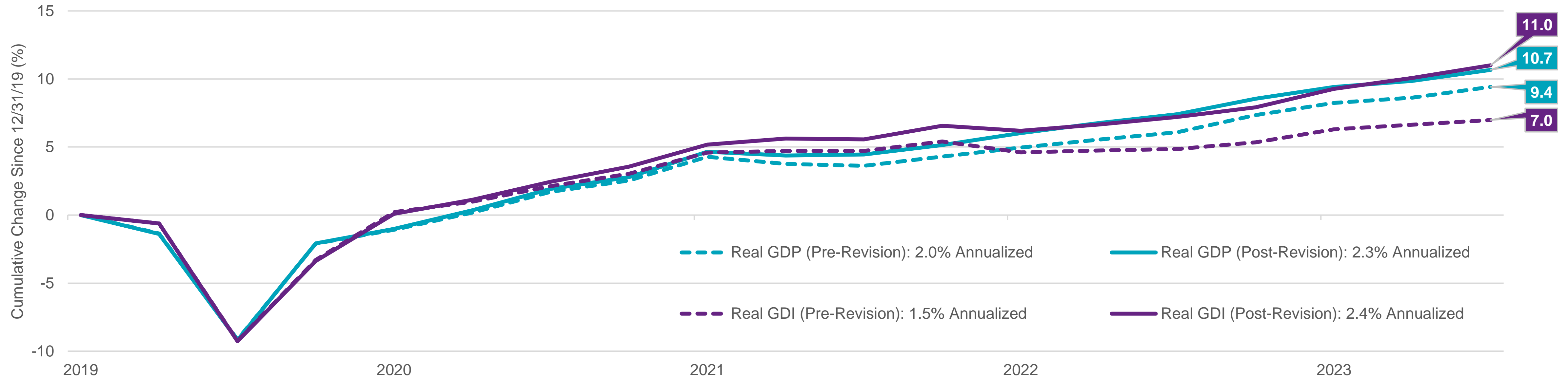
Beautiful

Real Gross Domestic Product (GDP) vs Gross Domestic Income (GDI) (12/31/19–6/30/24)



While one bear narrative after another has crumbled in the face of stable and resilient growth over the past year and a half, there's one argument that has managed to just barely survive. Until now that is. Since the early stage of the post-pandemic recovery, an unusual dynamic has emerged within the national accounts. Measuring the size of any economy, let alone one as large and complex as the US economy, is an enormous undertaking. While many economic laypeople are familiar with gross domestic product (GDP) as a measure of economic activity, there are, in fact, more ways to accomplish the same goal. Whereas GDP measures the value of final goods and services produced within the economy, gross domestic income (GDI) measures the costs incurred and incomes earned in the production of GDP. In other words, GDP measures output, and GDI measures the income associated with that output. In theory, the two should be roughly equivalent, although differences in source data can lead to deviations over time. While the Bureau of Economic Analysis (BEA), the agency tasked with constructing both measures, considers GDP a more reliable measure as it relies on timelier and more expansive input data, that hasn't stopped the bears from pointing out the widening gap between the two measures and leaning on the less optimistic picture of the economy painted by the GDI data. Through Q2 2024, GDI suggested the US economy had grown at an annualized clip of just 1.5% since the end of 2019 as compared to the 2% pace implied by GDP, resulting in a cumulative gap of almost 2.5%. Fortunately, each year the BEA releases revisions to the national accounts as more reliable data becomes available, and with the latest batch of revisions not only has that gap completely disappeared, with GDI now measuring above GDP, but both GDP and GDI were revised up meaningfully to boot. The post-pandemic recovery has been even stronger than we had previously thought. Time to flip back to the no landing script.

Source: Portfolio Analysis & Consulting, Bloomberg.

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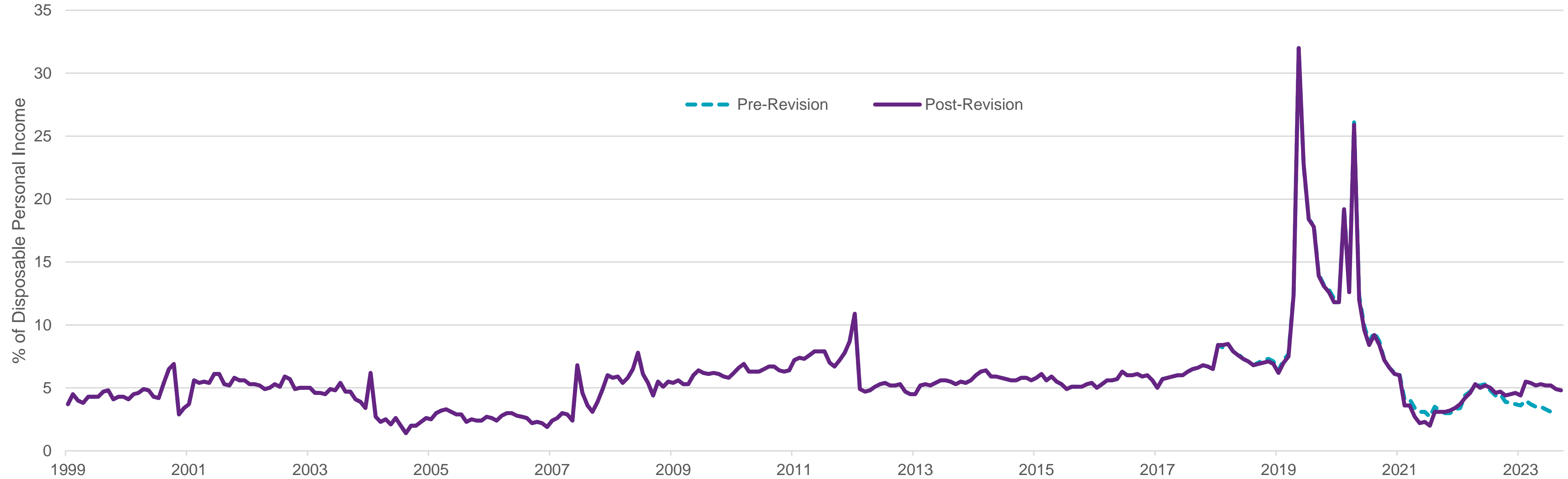
Disarm

Personal Saving Rate (12/31/16–8/31/24)



As a part of those same annual revisions to the National Economic Accounts, estimates of personal income and spending are updated to reflect more complete and detailed data than was previously available, including annual Census surveys, federal budget data, and tax return data, among other sources. Given the large upside revisions to GDI, it shouldn't come as much of a surprise that personal income estimates were revised materially higher as well. Personal income was revised up nearly $800 billion, while personal outlays and taxes were revised higher just over $300 billion. The result: a materially higher level of personal saving than previously estimated. With calls of a cracking consumer only growing louder as the focus has shifted to the continued easing in the labor market, the low saving rate has been a key pillar in the bearish calls around the consumption and growth outlook. But post-revision, the saving rate now sits at 4.9% versus the prior estimate of just 2.9%, placing it at the lower end of the elevated pre-pandemic range that was characterized by a protracted balance sheet repair cycle. All told, these revisions speak to an economy that has been meaningfully stronger than previously thought and is likely to prove more resilient given continued buffers from healthy employment, income growth, and savings. It's been a tough year to be an economic bear.

Source: Portfolio Analysis & Consulting, Bloomberg.

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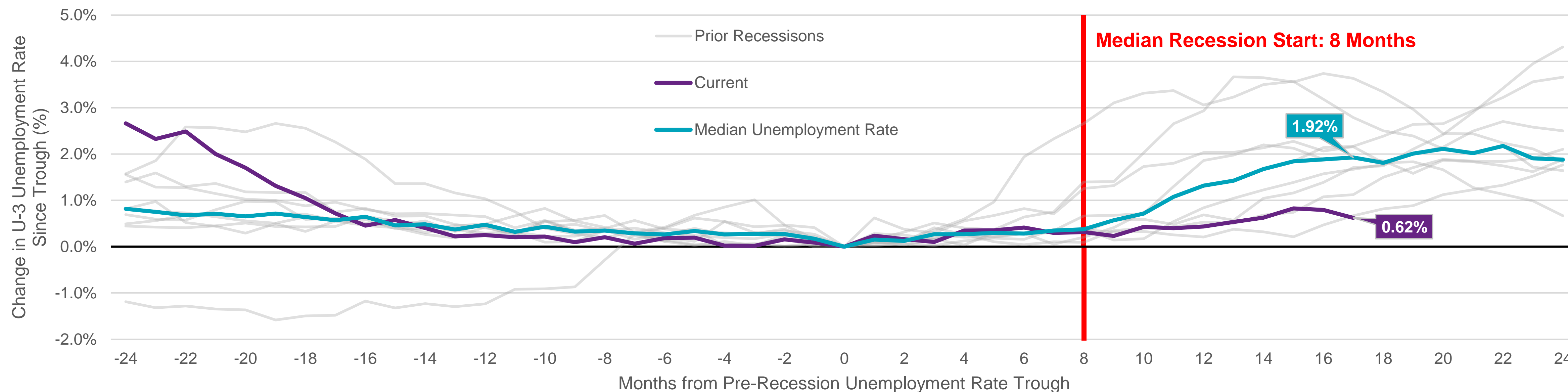
1979

Change in Unemployment Rate (1/31/48–9/30/24)



The lone bright spot for the bears in 2024 has been the rising unemployment rate, which as recently as July looked to be following the classic non-linear path typically seen during previous recessionary environments. But a closer look at unemployment dynamics through this cycle shows some stark differences. When looking at the typical evolution of the unemployment rate during the past nine recessions, excluding the pandemic recession, the current cycle looks very much unlike the rest. We are now 17 months removed from the cycle low in the unemployment rate of 3.4% reached in April 2023. Historically, the economy has entered recession eight months after the trough in the unemployment rate after a 40-basis-point median rise in the unemployment rate, which quickly accelerated to a 1.1% rise just three months later. By 17 months, the median unemployment rate had risen nearly 2% from the pre-recession lows. While it's been a widely held view that the labor market is weakening, there's been little in the way of a substantive explanation from labor market bears as to why the unemployment rate will continue to rise meaningfully, other than to simply claim that historically that's what always happens. "The unemployment rate never rises a little and then stops, it always continues to move higher;" or so the narrative goes. But that appears to be exactly what is playing out today. The unemployment rate has indeed risen 82 basis points from its cycle trough, but has since retraced 20 basis over the past 2 months as a broad range of measures continue to show strong and resilient growth. As we've stated time and again, this cycle is very different from previous ones. Indeed, there's a risk that this could simply be an unusual recession that is taking longer to manifest. But increasingly, it appears that the cooling we've witnessed in labor markets over the past year and a half is a function of continued post-pandemic normalization and not more pernicious deterioration.

Source: Portfolio Analysis & Consulting, Bloomberg. Median unemployment rate is derived from pre-recession unemployment rate troughs in 1953, 1957, 1960, 1969, 1979, 1980, 1989, 2000, and 2007.

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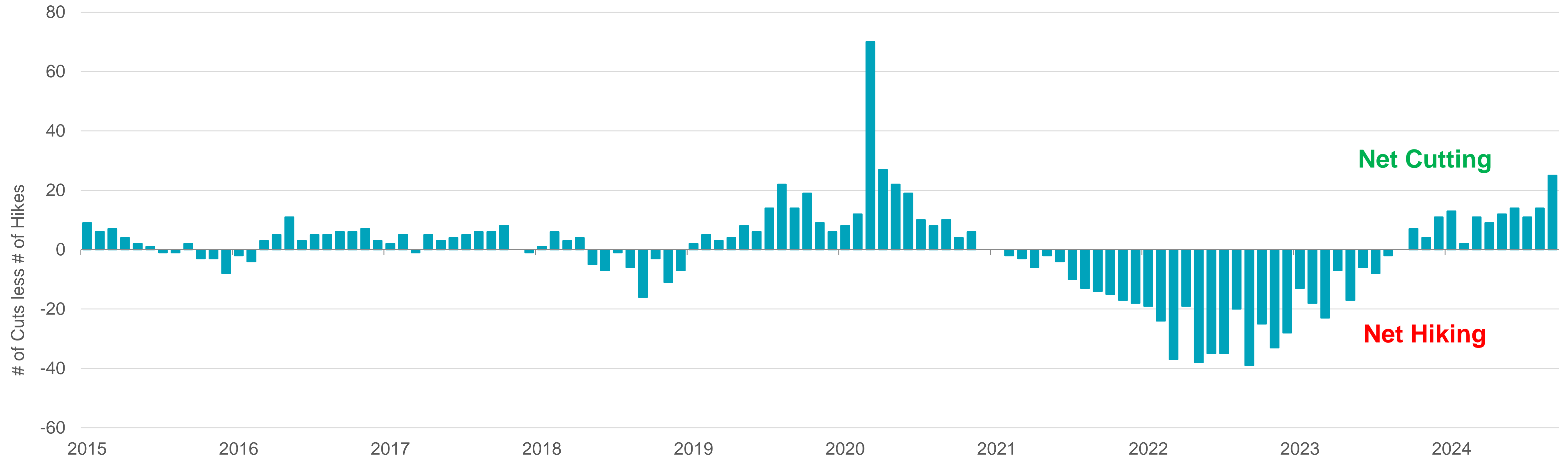
Take Me Down

Central Bank Policy Actions: Cuts Less Hikes (1/31/15–9/30/24)



While all eyes have been on Powell and the expected policy path for the Fed as it recalibrates policy back to neutral, the bigger picture is one of a synchronized easing cycle from global central banks. With the launch of the US easing cycle at the September meeting, the Fed is simply joining the ranks of a growing contingent of global central banks that are, themselves, recalibrating policy back from restrictive territory as the global inflationary era continues to fade into the past. September saw a net total of 25 cuts of various size from global central banks, marking the largest single month of rate cuts since April 2020. While the Fed is one of the few central banks with an explicit dual mandate, as inflation risks continue to be skewed to the downside, not just within the US but on a global scale as well, global central banks have plenty of cover to shift from fighting elevated inflation to defending against deflation by supporting growth. 2022-itis may be still running rampant as we've started to once again hear chatter of a no landing in the US, but the direction of travel of global monetary policy is clear. Put a global synchronized easing cycle together with still healthy labor markets and a resilient domestic growth backdrop, and it's hard not to come to a constructive outlook for the US economy and risk assets alike.

Source: Portfolio Analysis & Consulting, Bloomberg.

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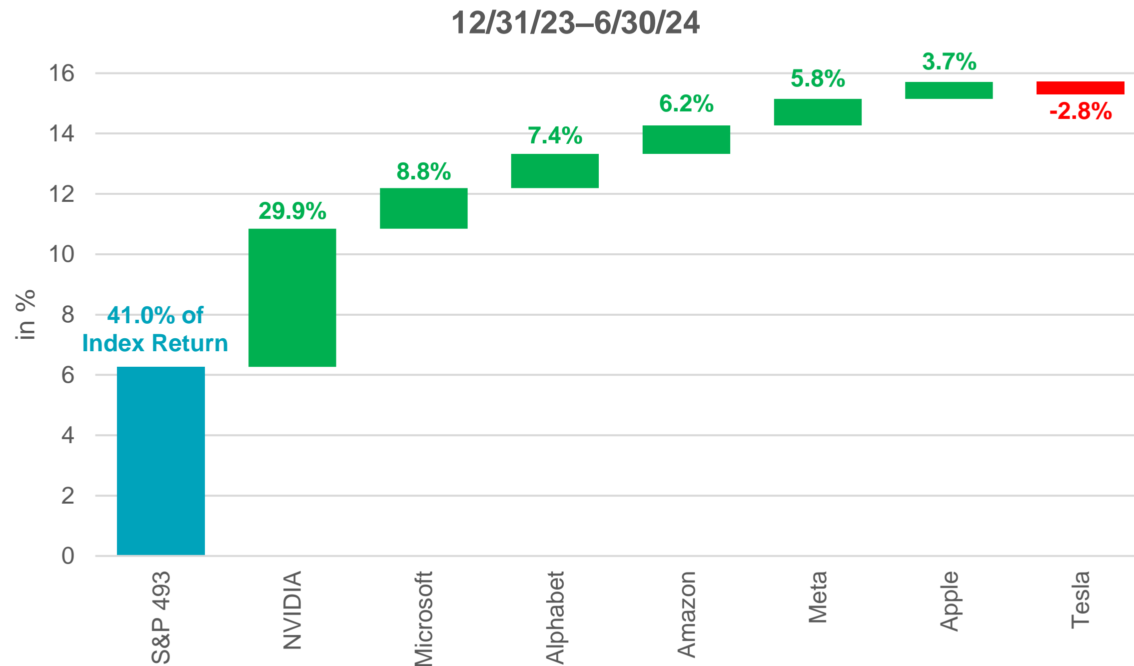
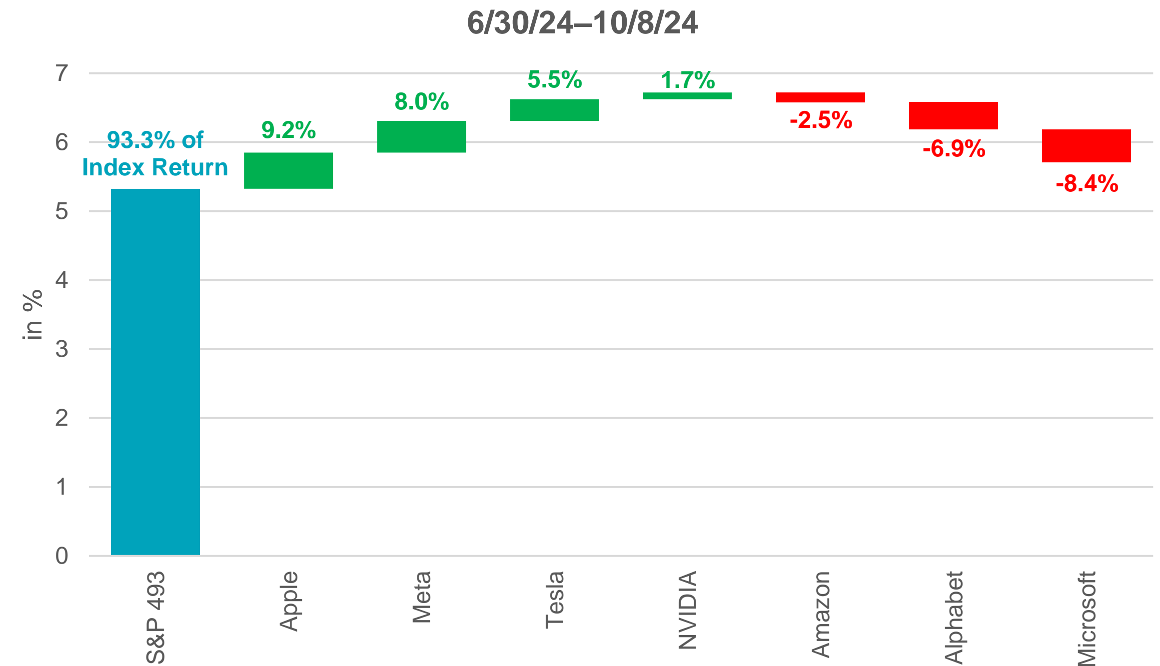
Bye June

S&P 500® Return Contributions





Oh, market breadth, one of our favorite topics of discussion. It seems like annually markets have to go through handwringing over narrow participation and the supposed fragility it imparts on the indices. And annually we have to issue reminders that narrow breadth is more the feature than the bug. Sharp narrowing of breadth more often gives way to a bullish broadening as investors get squeezed into exposure and rotate into laggards. And once again, we've seen that dynamic take hold over the third quarter. It wasn't so much that markets were narrow, with the S&P 493 up over 8.5% in just the first six months of the year, but returns were certainly top heavy as the Magnificent 7 drove 59% of the 15.3% total return for the S&P 500 as just 25% of issues in the index outperformed. But as almost $130B in net flows have piled into US equity funds and ETFs since the mid-point of the year, those statistics have flipped dramatically. The long-awaited broadening in market participation has arrived. Since June 30, the S&P 500 has posted a total return of 5.7% with 62% of issues outperforming the index as the S&P 493 has gained 7.5%, while the Magnificent 7 has lagged the broad index, returning just 4.7%. With aggregate equity positioning still fairly light and biased toward the defensive portion of the market, there's plenty of room for a rising tide dynamic to support continued broad participation led by cyclicals and tech as growth remains robust, labor markets stabilize, and global central banks embark along the path of synchronized policy easing.

Source: Portfolio Analysis & Consulting, Bloomberg. Magnificent 7 includes Alphabet, Amazon, Apple, Meta, Microsoft, NVIDIA, and Tesla. S&P 493 represents all other stocks within the S&P 500®. References to specific securities is for informational purposes only and should not be construed as investment advice. **Performance data shown represents past performance and is no guarantee of, and not necessarily indicative of, future results.**

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