Industry Snapshots

Arrow denotes 12-month moving total/average direction.

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

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

Macroeconomic Outlook

Trends in the economy continue to vary by market, but on the whole, we anticipate that slowing growth will characterize US Real GDP for the remainder of 2024, with a relatively similar pace of growth projected for 2025. For our clients who follow the industrial side of the economy, expect some industrial sector weakness for the next two to three quarters before growth picks up more noticeably in the back half of 2025.

With inflation easing to 2.5% in August – a significant drop from inflation's mid-2022 peak of 9.1% – and slowing growth in the labor market, the Federal Reserve elected to cut short term interest rates by 50 basis points at its latest meeting. More accommodative monetary policy will eventually benefit interest-rate-sensitive sectors, such as construction and manufacturing.

The easing in inflation – the rate of rise in prices – helps but does not fundamentally change the financial picture of some households. Many businesses are reporting that consumers are increasingly resistant to paying higher prices. Those who do not own stocks or their home are more likely to feel the economic pain of high price levels, as they are paying higher rents and not reaping the benefits of either the strong stock market or rising home equity.

Growth in US Total Retail Sales will be somewhat muted in the near term, a combined result of abating inflation, as the Retail Sales dataset is measured in dollars, and a more prudent consumer budgeting carefully or seeking cheaper alternatives. Inflation-adjusted US Personal Savings has settled into a plateau after a period of decline, a signal that consumers are adjusting their spending habits. High borrowing costs pose a stumbling block, but the interest rate cut from the Federal Reserve will provide some relief. Relief will be lagged, as it can take time for rate cuts to work their way through to consumers. Some buyers may stay on the sidelines and await further cuts.

> *"Many businesses are reporting that consumers are increasingly resistant to paying higher prices."*

Annual US Single-Unit Housing Starts have begun to decline on an annual basis. We recently revised our outlook for Starts downward given decline in the ITR Single-Family Housing Leading Indicator™. Starts are unlikely to crater given still pent-up demand for homes amid tight supply. Expect a near-term dip in Starts before rise returns in mid-2025. While Starts are a bellwether for the macroeconomy, this brief falter in Starts is more likely a sign of weakness rather than a sign of recession for the macroeconomy.

General rise – albeit sluggish rise – in the leading indicators signals cautious optimism. Take advantage of near-term softness to prepare for more robust growth in the years ahead. Think about what you will not have time to do when the economy is firing on all cylinders. Train your staff, develop new products or services, or consider entering a new market altogether.

Make Your Move

It is important to keep in mind that the S&P 500 is a weighted index and is heavily skewed toward larger firms, particularly tech firms. These firms account for an outsized portion of the strength we have seen in the past couple of years. Take this into consideration as you think about portfolio diversification.

Investor Update

The S&P 500 shrugged off the weakness exhibited from the second half of July into early August weakness, ending August just below record-high territory. An emerging trend is milder ascent in the S&P 500 and relative outperformance in more traditional, less tech-focused sectors. We are keeping a close eye on the technology sector, which is in a defined 3/12 declining trend despite general strength but will likely benefit from interest rate cuts.

ITR Economics Long-Term View

2024	2025	2026
RETAIL GROWTH; INDUSTRIAL FLAT	GROWTH	GROWTH

Leading Indicator Snapshot

	4Q2024	1Q2025	2Q2025
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

- Leading indicators are predominantly flashing green, but the strength is more muted than robust, with some leading indicators edging lower in recent months.
- The US ISM PMI (Purchasing Managers Index) monthly rate-of-change is now below zero, which could portend weakness in the industrial sector for 2025 if taken alone. Our analysis suggests this is likely to be a blip within an overall rising trend, but if that analysis proves to be incorrect, it would be a downside threat to our 2025 forecast for mild industrial sector growth.
- Recovery in the ITR Leading Indicator™ has been somewhat muted in recent months, indicating that firms should plan for a sluggish upturn – rather than breakneck rise – for industrial sector activity in 2025.

Industry Analysis

RETAIL SALES

- US Total Retail Sales in the 12 months through August were 3.2% above the year-ago level
- Real personal incomes are rising at a below-average pace, leading some consumers to seek lower-cost items as high interest rates and prices cut into budgets, particularly for those on the lower end of the income spectrum
- Mild rise will characterize retail spending for the remainder of the year and into early next year

WHOLESALE TRADE

- US Total Wholesale Trade in the 12 months through July was 1.1% above the year-ago level and is accelerating in growth
- Know your market's inventory situation; e.g., machinery shows declining sales-to-inventory ratios for big ticket items as ratios move upward for others like hardware, plumbing and heating equipment, chemicals, and electrical equipment
- Expect mild Wholesale Trade growth in the coming quarters

AUTO PRODUCTION

- Annual North America Light Vehicle Production is edging lower off a tentative April 2024 peak but remained 3.3% above the year-ago level as of July
- Quarterly Production has dipped below year-ago levels, signaling further downward pressure for annual Production in the coming quarters
- The recent interest rate cut from the Federal Reserve will likely inject some energy into auto demand and keep recession for Production mild

MANUFACTURING

- Annual US Total Manufacturing Production in August was 0.3% below the year-ago level
- Still-high borrowing costs pose a risk to Production recovery
- The US Manufacturing Capacity Utilization Rate declined 0.9 percentage points from August 2023 to August 2024, pointing toward continued softness in Production in at least in the near term

ROTARY RIG

- The average US Rotary Rig Count in the three months through August fell to 587 rigs, 12.3% below the same period last year
- Declining domestic oil inventories signal that a near-term Rotary Rig Count recovery is probable
- Conflict overseas could also bolster the Rotary Rig Count as domestic producers rise to meet demand should there be a supply shortfall

CAPITAL GOODS NEW ORDERS

- Annual US Nondefense Capital Goods New Orders (excluding aircraft) are trending relatively flat, up 0.7% compared to one year ago
- General flatness rather than outright decline in business-to-business spending can be attributed to generally elevated Producer Prices, as the New Orders dataset is dollar-denominated
- Annual US Defense Capital Goods New Orders have ticked up strongly in recent months but are still 4.0% below the year-ago level

TOTAL NONRESIDENTIAL CONSTRUCTION

- US Total Nonresidential Construction in the 12 months through July was 11.5% above the year-ago level; growth is slowing
- The recent interest rate cuts by the Federal Reserve will have a lagged positive impact on Construction, as projects take time to develop
- Be prepared for further Construction softening, as contractor backlog for commercial, industrial, and heavy highway/infrastructure markets is down 6.8% year over year

TOTAL RESIDENTIAL CONSTRUCTION

- Annual US Total Residential Construction in July was 5.0% above the year-ago level and is accelerating in growth
- Affordability is weighing on single-family housing, leading to a tentative decline in US Single-Unit Housing Starts
- US Multi-Unit Housing Starts are in a tentative recovery trend

A Closer Look: The US Economy

A Deep Dive Into Consumer Prices

CAROLINE DUNSBY

What you need to know: While inflation is lower, consumer spending patterns may still be impacted from previous high inflation

Inflation, as measured by the change in Consumer Prices, eased to 2.5% in August – in other words, Consumer Prices this August were 2.5% above Prices in August last year. Monthly consumer inflation has not been this low since early 2021, and this is a stark contrast to the 9.1% peak in June 2022, the most robust inflation in over 40 years. If inflation is lower, why do things still feel expensive? And what implications does that have for businesses and the economy at large?

Inflation Has Eased, but Price Levels Are Elevated

While a year-over-year inflation metric is a favorite of economists because of its consistency for comparisons, we realize that, while shopping, consumers are not always comparing prices to exactly 12 months ago. Inflation was relatively low in the decade preceding the pandemic but really ramped up starting in 2021. Often now you will hear consumers referring to how much cheaper things were before the pandemic, and rightfully so. As of August, Consumer Prices are up 22.5% from December 2019, or an average annualized inflation rate of 4.4%, more than double the Fed's 2% mandate. So, while since mid-2022 we have seen disinflation – price levels still rising, just at a less robust clip – the cumulative impact of high price levels may linger.

Important Day-to-Day Consumer Prices

It is important to remember that the Consumer Price Index is a very broad measure. If you dig deeper into the costs of goods and services that go into this overall measure, you will find that some prices have gone up less than overall Consumer Prices, and others have increased more.

Take gasoline costs, for example. From December 2019 to August 2024, gasoline prices are up 37.6%, and this is after they have fallen considerably from 2022 highs. Naturally, this is a big hit on some consumers that rely on a lot of driving, potentially causing them to re-budget their incomes or dig into some savings.

Food costs also come up often. Grocery prices are up 26.7% from December 2019 to August 2024, marginally above overall Consumer Prices. However, this varies by what you are eating and where you are buying your food. US Food Away From Home Prices, typically applicable to restaurants, are up 28.6% over the same period, the extra likely due to pressure on wages. In terms of groceries, bread prices are up 43.1% over that period, due in part to high wheat prices stemming from the war in Ukraine. Conversely, vegetable prices are up just 13.1%, much closer to what we would expect over that period if inflation had stayed around the Fed's typical goal of 2%.

Housing Costs

Experiences with housing costs vary greatly based on the consumer's ownership status and location. The Federal Housing Finance Agency's US Home Price Index increased by 57.2% from December 2019 to June 2024. Those who owned homes heading into the pandemic were, in many cases, able to lock in historically low mortgage rates.

On the other side of the coin, this rise in prices in tandem with currently high mortgage rates makes buying much more difficult. For urban consumers, rent has increased about 25.4% since the end of 2019, marginally more than overall US Consumer Prices. However, this will vary drastically by region, as some will have felt their rents increase by much more than others.

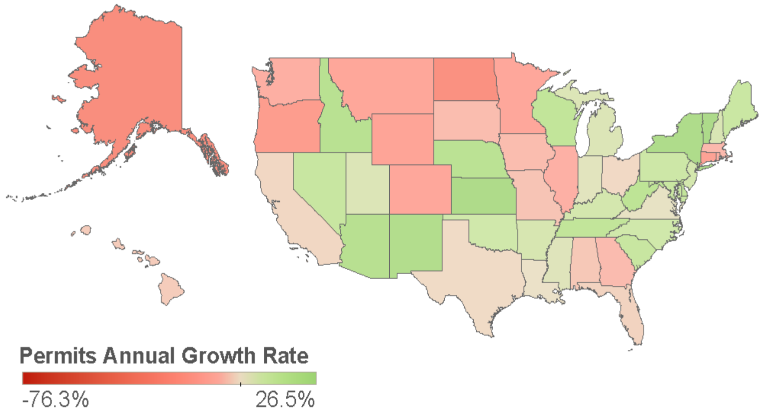
Takeaways for Your Business

Yes, lower inflation is good for consumers, but this may not mean that consumer spending patterns will exactly mirror pre-pandemic trends. There are many variables impacting consumers' willingness to spend. Some consumers are better positioned to absorb cumulative price increases, such as those who locked in low mortgage rates, saw a higher than median increase in real wages, had exposure to the stock market before the pandemic, or live in an area with lower rise in rents. Generally speaking, such consumers are those who today have higher income or net worth. Meanwhile, it is typically lower-to-middle-income consumers facing tight budgets due to increased price levels.

If your business is consumer facing, look at the relative prices of your product mix. Some large consumer-facing businesses, such as Walgreens and PepsiCo, are reporting that consumers are looking for lower-cost alternative goods. Consumers may also choose to forgo or postpone purchases of discretionary or big-ticket items, as evidenced by lower prices for vehicles. Price increases may be harder to pass along on discretionary items.

We expect inflation to reach a trough around the middle of 2025. The next period of higher inflation, though lower than the levels seen in much of 2021 and 2022, will be painful for those who do not prepare for it; price levels will be compounding on top of the heights they reached during the pandemic period. Ensure you are well positioned for a more inflationary environment in the second half of 2025 and beyond. For example, utilize lower interest rates ahead of that time to invest in efficiencies that will reduce your reliance on labor costs.

State-by-State: Permits



- US Housing Unit Building Permits in the 12 months through July were 1.5% above the year-ago level; however, the year-over-year ascent may be brief given that the most recent three months of Permits are running 2.4% below the same three months one year earlier, a negative ITR Checking Point™.
- Permitting trends are geographically mixed, with significant variation between neighboring states; every region has a state at double-digit growth rates and a state with a negative growth rate.
- Generally speaking, states with a lower cost of living are outperforming adjacent states with a higher cost of living – for example, Nevada and Arizona permits are rising while California permits contract, and Vermont, New Hampshire, and Maine permits are rising while Massachusetts permits contract.
- We expect the housing market to contract in the near term given affordability constraints, but we expect that decline will be relatively short and give way to rise next year as rate cuts and a limited housing supply support growth.

Readers' Forum

Why was the recent jobs report revised, and what does it mean for the economy?

Haley Sienkiewicz, Economist at ITR Economics™, answers:

The Bureau of Labor Statistics (BLS) reviews employment data periodically, which is benchmarked once a year. Data adjustments are generally par for the course for economic data, as data sources aim to incorporate the most up-to-date information in data releases.

The recent revision by the BLS was to March 2024 employment data, and reflected a downward adjustment; there were 818,000 fewer workers employed in March 2024 than initially reported, signaling a somewhat weaker jobs market than previously thought for that time period. This reduction of 818,000 jobs amounts to a downward revision of 0.5%, which is above the historical average for revision metrics. It is also important to point out that this data revision is preliminary and will not be finalized until February 2025. Since the revision is to March data, remember that it tells us what has already happened, not necessarily what is happening right now.

Regardless of how the revision shakes out, looking at the labor market to figure out where the economy is headed is akin to using your rearview mirror to drive a car. To see where the economy is going, look to a system of leading indicators, which suggest that we are likely to see similar growth rates – or slightly higher growth rates – for most core segments of the economy in 2025.

Please send questions to: questions@itreconomics.com