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| Current Forecast | | | | | |
|---|---|---|---|---|---|
| | 2023 | 2024 Est | 2025 Est | 2026 Est | 2027 Est |
| GDP Growth | 3.1% | 2.3% | 2.0% | 1.9% | 1.1% |
| Change in Consumer Prices | 3.3% | 2.6% | 2.7% | 2.7% | 4.3% |
| Fed Funds Target Rate | 5.50% | 4.50% | 3.75% | 3.75% | 5.00% |
| 5-Year Treasury Yield | 3.85% | 4.15% | 4.25% | 4.25% | 5.00% |
| 10-Year Treasury Yield | 3.84% | 4.25% | 4.75% | 4.88% | 5.00% |
| S&P 500 EPS | $218 | $241 | $264 | $287 | $304 |

Longer-term inflation will likely be higher than what prevailed before the pandemic but close to the FRB's 2% target. The Federal Reserve Bureau (FRB) will cut the (Federal Funds Rate) FFR by 0.25% at every other meeting until it achieves neutrality (3.75%). Security National Bank's investment services team expects the 10-year Treasury to end 2025 at 4.75%. Fiscal pressures will eventually lead to higher long-term rates. We expect earnings for the S&P 500 to post modest growth for the rest of this economic cycle. We see de minimis recession risk before 2027 as growth will likely be around its non-inflationary potential of 1.8% to 2.0%. We are penciling in an inflation wave in 2027.

| Last Month's Rates and Total Returns | | | | |
|---|---|---|---|---|
| November 30, 2024 | Value | One Month | Year to Date | 1 Year |
| Fed Funds Target (Upper) | 4.75% | -25 bp | -75 bp | -75 bp |
| 3-Month Treasury Yield | 4.49% | -5 bp | -86 bp | -90 bp |
| 2-Year Treasury Yield | 4.15% | -1 bp | -10 bp | -56 bp |
| 5-Year Treasury Yield | 4.06% | -9 bp | +21 bp | -22 bp |
| 10-Year Treasury Yield | 4.17% | -11 bp | +29 bp | -19 bp |
| Mortgage News 30-Year | 6.88% | -21 bp | +21 bp | -27 bp |
| S&P SuperComposite 1500 | 1,365 | 6.16% | 27.52% | 33.87% |
| S&P 500 Index | 6,047 | 5.87% | 28.07% | 33.89% |
| S&P 500 Equal Weight Index | 7,576 | 6.42% | 20.56% | 28.83% |
| S&P Midcap 400 | 3,364 | 8.81% | 22.67% | 33.36% |
| S&P SmallCap 600 | 1,539 | 10.94% | 18.09% | 33.20% |
| S&P 500 Growth | 4,063 | 5.94% | 34.94% | 39.94% |
| S&P 500 Value | 2,027 | 5.78% | 20.48% | 27.14% |
| World ex-US, USD | 337 | -0.91% | 7.63% | 13.03% |
| Wilshire Liquid Alts | 197 | 1.42% | 8.62% | 9.05% |
| BB U.S. Aggregate | 92 | 1.06% | 2.93% | 6.88% |
| Crude Oil – WTI Near Term | $68 | -1.82% | -5.09% | -10.48% |
| Gold – Near Term | $2,657 | -2.97% | 28.83% | 30.37% |
| U.S. Dollar Index | 106 | 1.69% | 4.35% | 2.16% |

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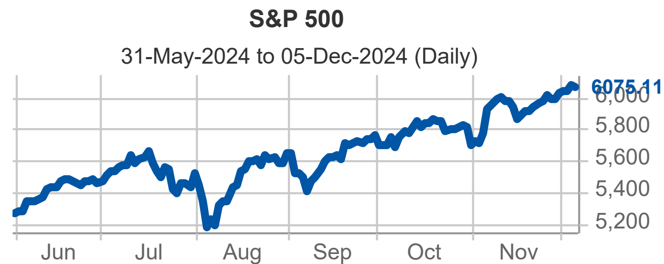
Security National Bank's investment services team within its private client services division authors economic forecasts that provides our investment committee and the bank's funds management committee with background assumptions for use in investment decisions. We are pleased to share our economic outlook with you. Please be advised that our crystal ball is just as clouded as other prognosticators and that all forecasters have poor track records. We base our projections on what we think monetary and fiscal policymakers *will* do, not what they *should* do. At the end of this report, you will find commonly used abbreviations and terms for your reference.

**Stock Market**

The Trump-led Republican sweep triggered a risk-on trade following the election as investors rotated into cyclical market areas. In addition, the Federal Reserve also did its part to keep economic momentum moving forward with an additional 25 basis point interest rate reduction at its November 7th meeting.




Smaller stocks significantly outperformed large stocks, and the consumer discretionary and financial services sectors trounced the materials and healthcare sectors. Longer-dated bonds outperformed shorter-duration bonds. Once again, November lived up to its reputation as the best-performing month. Over the last ten years, the S&P 1500 has only had one down November (2021), averaging a 4.3% return.

The S&P 1500 Index, our benchmark, returned 6.2% for the month and is up 27.5% YTD. The S&P 500 returned 5.9% for the month and is up 28.1% YTD. The equal-weighted S&P 500 Index returned 6.4% and is up 20.6% YTD. Strategas Research Partners recently highlighted that the YTD return for the S&P 500 Index represents the 9th-best YTD return in history. Meanwhile, small-capitalization stocks rose an outstanding 10.9% for November and are up 18.1% YTD. Mid-capitalization stocks also posted a strong showing during November, rising by 8.8% for the month and are up 22.7% on a YTD basis.

For November, consumer discretionary was the top-performing sector Exchange Traded Fund (ETF), up 12.9%, followed by financial services, up 10.5%. Healthcare was the worst-performing sector ETF, up 0.4%, followed by materials, up 1.5%. YTD, the financial services sector was the best-performing sector, up 38.1%, while the healthcare sector lagged, up 9.3%.

While investors have cheered the strong market returns posted thus far during 2024, perhaps the only downside of the current investing landscape is that valuations are elevated relative to historical averages. At the end of November, the S&P 500 was trading at 22.2x forward earnings, compared to an average of 16.6x since 1996. Thus, future market gains will likely depend more on earnings growth than multiple expansions.

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**International Stock Returns**

Last month, international stocks rose by 0.1% in local currencies but fell by 0.91% when translated into U.S. dollars. The US dollar rose by 1.7% as global investors flocked to the U.S. to take advantage of higher U.S. interest rates and as a hedge against possible tariffs.

Stocks in China fell by 4.2% in local currency as stimulus measures continue to disappoint investors and possible tariffs add to uncertainties. Performance was mixed within North America, with Canadian stocks advancing by approximately 6% for the month, while markets in Mexico struggled, declining by approximately 3% during November.

**Fixed Income Returns**

U.S. interest rates fell across the curve, with longer-term interest rates falling slightly more than close in rates. Longer-duration fixed-income products outperformed. The 20+ year Treasury ETF returned 2.0%, while the 1-3 Year Treasury ETF returned 0.3%. YTD, interest rates are mixed, short-term rates are lower, and long-term rates are higher. The 1-3 Year Treasury ETF returned 3.7% on a YTD basis, while the long-term treasury ETF has declined by 1.8% thus far during 2024. We remain cautious and will continue to keep our duration short.

**Focus on the Long View**

Over the last thirty years, the U.S. experienced a terrorist attack, presidential impeachments, a global financial crisis, a pandemic, bouts of inflation, and multiple bear markets. Stock market returns as measured by the S&P 1500 have shown consistency over the longer term. We list the longer-term returns for the broad stock and bond markets each month. This table reminds us to focus on the long term.

| | Five Years | Ten Years | Twenty Years | Thirty Years |
|---|---|---|---|---|
| Stocks | 15.5% | 13.1% | 10.7% | 11.1% |
| Bonds | -0.1% | 1.5% | 3.1% | 4.6% |

Over the last 30 years, the economy has experienced only 13 (11%) quarters of contraction, with five of these during the Great Financial Crisis (GFC). The extended periods of economic growth have resulted in above-average stock market returns and below-average fixed-income returns. Unless the economic paradigm changes, stocks should outperform fixed income. Because of today's high valuations, stock returns may not be as generous. Considering our country's dismal fiscal position, we remain cautious about bond returns.

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**Interest Rate Policy**

As expected, the FOMC cut the FFR by 0.25% on November 7, bringing the cumulative cuts to 0.75%. The FFR currently stands at 4.50% to 4.75%. The post-meeting statement was minimally changed. The debate has shifted to the pace of further cuts and the terminal level for this easing cycle.

| Meeting Date | Futures Market 11/06/2024 | SNB Forecast |
|---|---|---|
| December 18 | 4.50% | 4.50% |
| January 29 | 4.50% | 4.50% |
| March 19 | 4.25% | 4.25% |
| May 7 | 4.25% | 4.25% |
| June 18 | 4.00% | 4.00% |
| July 30 | 4.00% | 4.00% |
| September 17 | 4.00% | 3.75% |
| October 29 | 4.00% | 3.75% |
| December 10 | 4.00% | 3.75% |

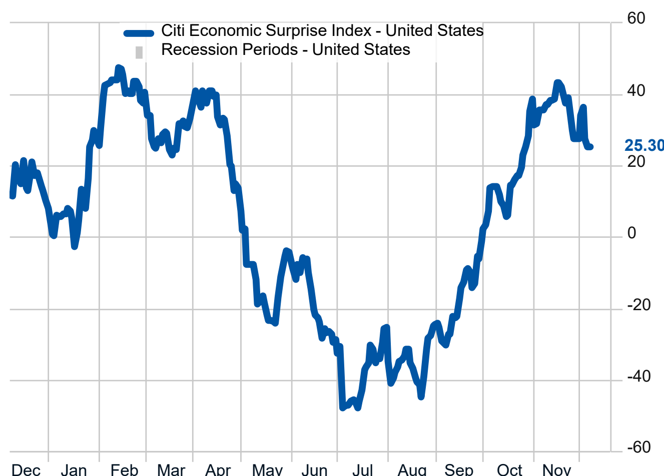
We expect the FOMC to cut the FFR by 0.25% at its next meeting on December 18. The futures market implies an 87% probability of a 0.25% cut and a 13% chance of no cut.

The pace of further rate cuts will likely slow down to one cut for every other meeting. We currently forecast the terminal rate to be 3.75%, while the futures market puts it at 4.00%. The terminal rate will shift with each economic report.

At the New York Times' DealBook Summit from December 4, FRB Chair Jerome Powell stated that the FOMC could "afford to be a little more cautious," "the economy is strong," and "the labor market is "better and downside risks are less." He also added growth has been "definitely better" than expected, and inflation has come in "a little higher." Investors interpreted his speech as supporting a cut in December followed by a slower pace of future cuts.

**Recent Economic Reports**

The chart at the right shows that economic reports were better than expected from mid-August through early November. Since then, reports have either met expectations or been slightly disappointing. The Citi Economic Surprise Index compares economic reports with expectations. When the line falls, actual results are less favorable than expectations. This is our favorite graph; it summarizes many economic reports into an easily understood graph.




Interest rates fell modestly as the risk of an overheating economy lessened. Equities rose as the likelihood of a "Goldie Locks" economy increased.

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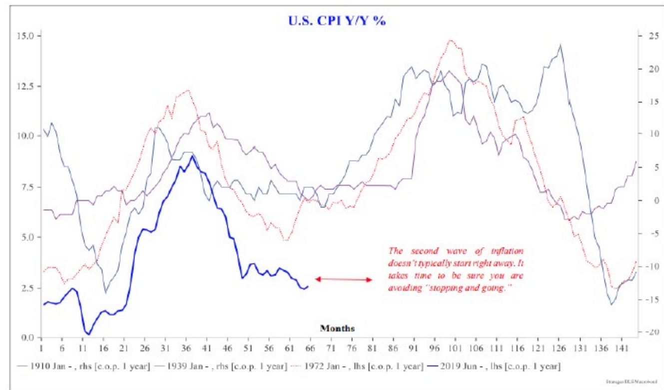
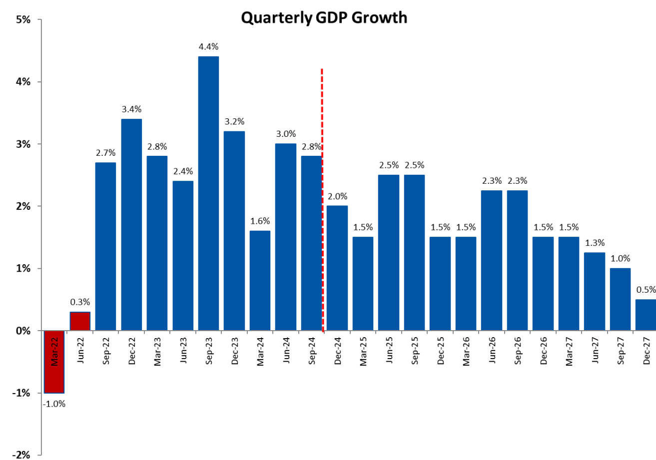
**Economic Growth**

This month, we expanded our forecast to include 2027. We did that not because we had any insight into what the world would look like beyond tomorrow. Instead, our goal was to introduce the idea of inflation waves. Our friends at Strategas Securities provided this graph. A second inflation wave often follows an initial inflationary episode. While the economy's course is not set in stone, we remain vigilant to the prospect of a second inflationary wave. For modeling purposes, we have it starting in early 2027.




The FRB will respond to higher inflation by raising interest rates and slowing the economy. Until then, inflation, as measured by the CPI, should run around 2.7%—about where it is now. Real economic growth will run from 1.5% to 2.5%.




We do not know if the next inflationary wave will hit in 2027, 2026, or 2030. However, we believe the odds of a second inflationary wave are higher than most investors realize. There is enough uncertainty to keep us from going all-in on the inflation trade. It will color, not dominate, our investment decisions.

The economy will do well before the dreaded inflationary wave hits. To incorporate the momentum we continue to see, we raised our forecasted growth rate for 2025 by 0.5%. Groth trail off in 2027 is in response to higher interest rates brought on by the inflationary wave. If the wave were delayed or canceled, 2% growth would be expected.

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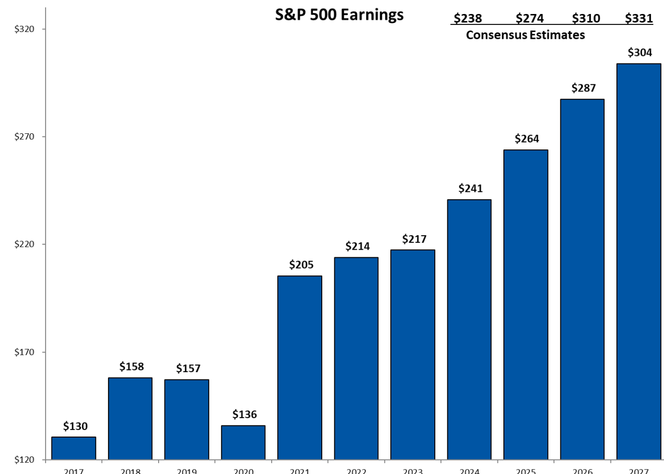
**Stock Earnings Forecast**




We raised our 2025 EPS estimate by $12 to incorporate the better economic outlook. Our forecast remains substantially below the consensus. This year, the profit margin for the S&P 500 will be 12.0%. Consensus numbers for next year call for a 13.0% profit margin. Either revenue needs to grow faster than consensus, or earnings estimates need to come down.

The optimism surrounding profitability is probably the most fraught area around valuations. If profit margins do not continue to climb, today's high P/E ratio is not justified. The S&P 500 trades 23 times our 2025 earnings (2025 P/E) and 22 times consensus. Over the last ten years, it has traded at a median P/E of 17.7 times forward earnings. Our fair value multiple remains at 20.0. Unless interest rates fall below 4%, the market's multiple will unlikely expand from here and will likely contract. This implies that earnings growth and dividends will drive stock market returns. A five percent annual total return over the next several years seems reasonable.

If you have questions or comments about this Outlook, don't hesitate to contact our Security National Bank Private Client Services team.

Damian Howard, CFA
SVP, Director of Investment Services

Clinton Rushing, CFA
VP, Senior Investment Officer

Lauren Mozur
Investment Officer

Please see the obligatory disclosures at the bottom of each page and at the end of this report.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Since 1977, the Federal Reserve has operated under a mandate from Congress to "promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates"—commonly called the Federal Reserve's "dual mandate." For this reason, we always start our economic review with employment followed by inflation.

**Employment**

Please remember that the labor market is a lagging indicator. Job losses typically occur after the economy enters a recession.

Total nonfarm payrolls rose by 227,000 in November compared to expectations of 200,000 positions added. The previous two months' payrolls were revised up by a combined 56,000. This month likely contained some catch-up from October's hurricane- and strike-impacted report. However, the catch-up and revisions were not as large as some market participants expected. The probability of a 0.25% FFR cut on December 18 rose from 71% just before the report to 87% today.

Private sector jobs rose by 194,000 in November compared to expectations of 200,000 positions added. October's private sector estimate was revised up by 26,000. The three-month moving average rose to 138,000 from 85,700 the previous month. Employment rose in health care, leisure and hospitality, and professional service. Wage growth fell to 0.37% from 0.42% the previous month. The three-month average (TMA) of 4.5% for wage growth is above the FRB's target of 3.5%. The aggregate payrolls index rose 0.8% M/M and is up 5.1% Y.Y.

We begin our employment review by examining the JOLTs (Jobs Openings and Labor Turnover) report published by the Bureau of Labor (BLS). This gives us an idea of how big a cushion the economy has before employment is impacted. Generally, companies will first cut open positions before employees.

| JOLTS Report | | | | |
|---|---|---|---|---|
| | Most Recent | Previous Month | Previous Year | Long-Run |
| Open Positions | 7,744,000 | 7,372,000 | 8,685,000 | |
| Open/Unemployed | 1.1X | 1.1X | 1.4X | 0.9X |
| | | | | |
| Open Rate * | 4.8% | 4.6% | 5.4% | 4.4% |
| Hire Rate * | 3.6% | 3.9% | 4.1% | 4.1% |
| Lay-Off Rate * | 1.1% | 1.3% | 1.2% | 1.4% |
| Quit Rate * | 2.3% | 2.2% | 2.6% | 2.4% |

* Private Sector

The October JOLTS report was better than expected. The BLS reported 7.7 million open positions versus the consensus of 7.4 million. Open positions grew by 367,000, led by professional and business services (209,000) and restaurant and hotel (162,000) sectors. State and local government open positions grew by 32,000. The wholesale trade sector reported 37,000 fewer open positions.

The open rate is the number of open jobs divided by the total (filled and unfilled). FRB research suggests that unemployment significantly increases once the open rate falls below 4.5%. The rate increased to 4.8% in September. This measure gives job openings room to ease before unemployment rises.


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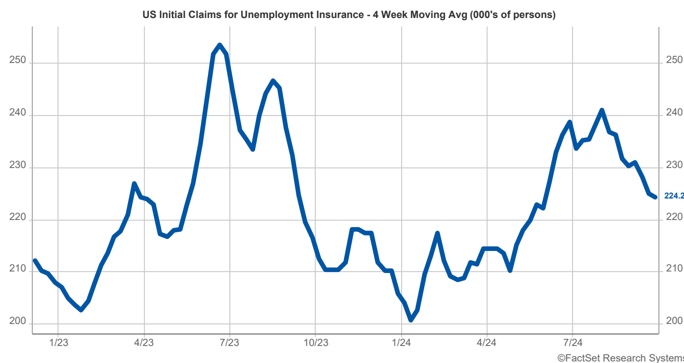
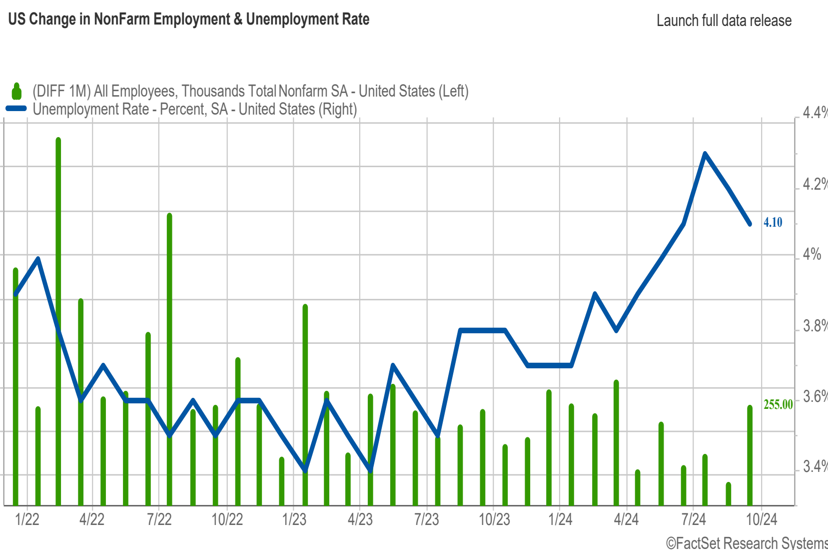
Both the hire rate and the layoff rate are below the long-term average. This indicates that employers are retaining their talent (low layoff rate) but are unable to or unwilling to expand payrolls (low hire rate). This points to a slow labor market turnover. It is expensive to hire and train new workers. A low-turnover labor market should be more productive, which will help increase labor productivity. We expect the recent improvement in labor productivity may be partially impacted by lower labor turnover.

The quit ratio ticked up slightly but remains below pre-pandemic levels. An elevated quit rate is associated with higher wage growth, as employees usually switch jobs for higher pay. The ratio tends to lead to compensation costs by nine months. The lower quit rate should lead to lower wage growth.

Initial jobless claims for the week ending November 29, 2024, were 224,000, bringing the four-week average to 218,250. Continuing claims fell by 13,000 M/M to 1,871,000. While up from their January lows, initial claims are below the two recent peaks and would need to rise above 300,000 before unemployment increases dramatically. The continued modest level of jobless claims supports the view of a slowing but healthy labor market.




According to the Establishment survey, the economy added 227,000 jobs and 194,000 in the private sector. The consensus was for 200,000 and 200,000 new jobs. Payrolls for the previous two months were revised higher by 56,000. The unemployment rate rose slightly to 4.2% as the number of unemployed persons rose by 161,000. On a Y/Y basis, the number of unemployed people rose by 883,000. The participation rate fell by 0.1% to 62.5%. Hourly earnings rose by 0.4%, above the consensus estimate of 0.3%.




Job gains were concentrated in health care (54,000 jobs added) and government (33,000 jobs added). Manufacturing rebounded by adding 22,000 jobs, partially offsetting the previous five months' 96,000 decline.

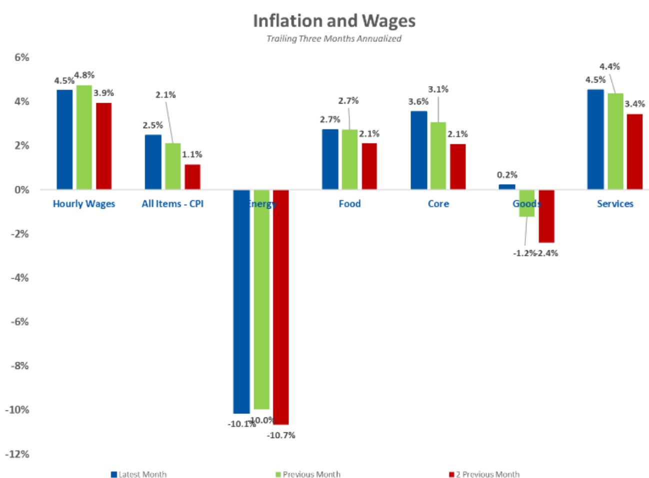
The unemployment rate rose by 0.1% to 4.2% as the number of officially unemployed persons increased by 161,000 to 7.1 million. The unemployment rate for the 25-year-old and older cohort rose by 0.1% to

3.5%. The broader U-6 unemployment rate rose by 0.1% to 7.8%. The participation rate fell by 0.1% to 62.5%. The employment-to-population decreased by 0.2% to 59.8%.

Last month's average hourly earnings (wages) rose by $0.13 per hour to $35.61, up 0.4% and above the consensus estimate of 0.3%. Average hourly earnings are up $1.38 per hour or 4.0% Y/Y. Over the last three months, average hourly earnings grew at a 4.5% pace, decreasing from the 4.8% pace the previous month. The FRB wants wage growth to stay below 3.5% for an extended period. While wage growth is above the FRB's target, it will not cause the FRB to deviate from its rate-cutting path. The average workweek rose by 0.1 hours to 34.3. Average weekly earnings rose by $8.00 (0.4%) from the previous month. Average weekly earnings are up $43.91 (3.7%) year over year.

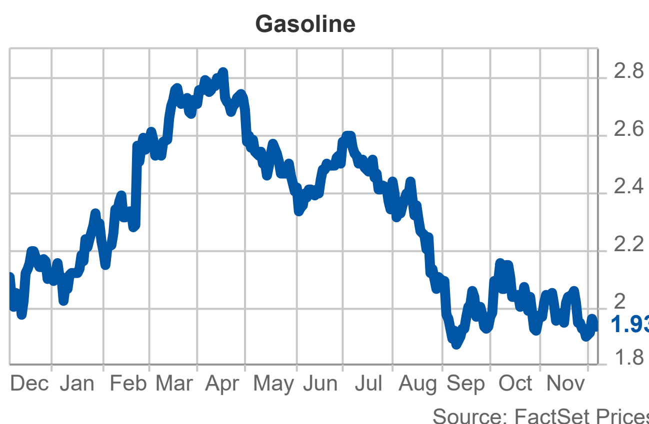
**Inflation**

The next CPI report will be released on December 11, a week before the next FOMC meeting. Thus, the committee will have one additional CPI report when setting monetary policy.




The FRB aims to achieve 2.0% long-term inflation, as measured by the core Personal Consumption Expenditures (PCE) Price Index. Due to differences in various weightings, PCE measures tend to be 0.3% below the more common Consumer Price Index (CPI). The FRB believes it has made substantial progress in achieving that goal. The most recent report put the core PCE at 2.8% Y/Y, slightly higher than the 2.7% Y/Y reported the previous month.
The Trailing Three-Month Annualized (TMA) Core PCE was also 2.8%, down from a peak of 5.7% (Feb 2022). Inflation is not yet at the FRB's target but not too far above. It is appropriate for the FRB to lower interest rates to reflect progress on inflation.

The Consumer Price Index (CPI) rose 0.2% in October and 2.5% (TMA). Core prices rose 0.3% and 3.6% TMA. All items, less food, energy, and shelter (super core), rose by 0.2% and 2.7% TMA.

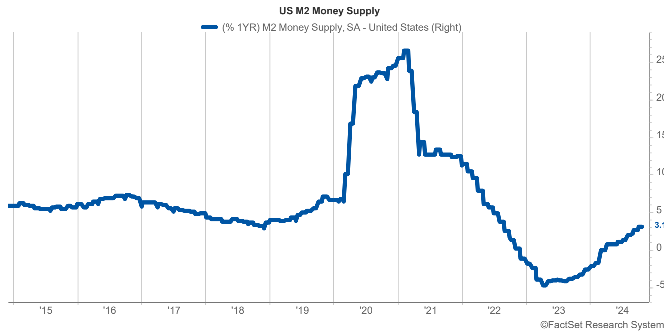



Food prices were up 0.2% M/M and 2.7% TMA. Energy prices fell 0.2% M/M and 10.1% TMA. Wholesale gasoline prices are down 7.1% YTD and 30% from their April highs. The AAA national average gas price is down 6% from a year ago and 7% for Nebraska. Barring further geopolitical tensions, energy should remain a source of deflation.

Goods prices rose 0.1% M/M and 0.2% TMA. Used vehicle prices rose 2.7% for the month and 8.4% TMA. Hurricane Helene is estimated to have damaged up to 138,000 vehicles across six states. These vehicles

will most likely be replaced with used cars from other areas. The demand for replacement cars may keep goods prices up for a few months. The Manheim Used Vehicle Value Index is up 5.1% from its June low. New vehicle demand was not as impacted by the hurricanes. New vehicle prices were down 0.1% M/M but up 0.6% on a TMA basis.

Service inflation runs hot at 0.4% M/M and 4.5% TMA. Owners' Equivalent Rent (OER) was up 0.4% M/M and 5.0% TMA. OER remains significantly above other rent measures. Eventually, this measure will reflect reality. We have given up forecasting when this measure will reflect market-based measures.




Milton Friedman, American Nobel Prize winning economist and statistician, famously said: "Inflation is always and everywhere a monetary phenomenon, in the sense that it is and can be produced only by a more rapid increase in the quantity of money than in output." Much of 2022's and 2023's inflation was caused by the rapid growth of the monetary supply in 2020 and early 2021. At its peak growth, the money supply grew at over 27% Y/Y. The money supply increased faster than output for three years, leading to inflation. The FRB slammed on the brakes in 2022. From March 2022 to March 2023, the money supply contracted 3.7%, or $0.8 trillion. Since March 2023, the money supply has grown by 2.1%. It is now growing at a 3.1% Y/Y pace. This is insufficient for a growing economy. The money supply should grow about 6% Y/Y to promote stable, low inflationary growth. We should point it out. There are very few Friedman acolytes at the FRB.

Because inflation statistics are lagging indicators, economists use forward-looking inflation expectations. The breakeven inflation rate implies what market participants expect inflation to be in the next five years, on average. The 5-year break-even inflation rate peaked at 3.6% in March 2022. Inflation expectations have fallen to the current 2.4%. For now, expectations are where we would expect them to be.

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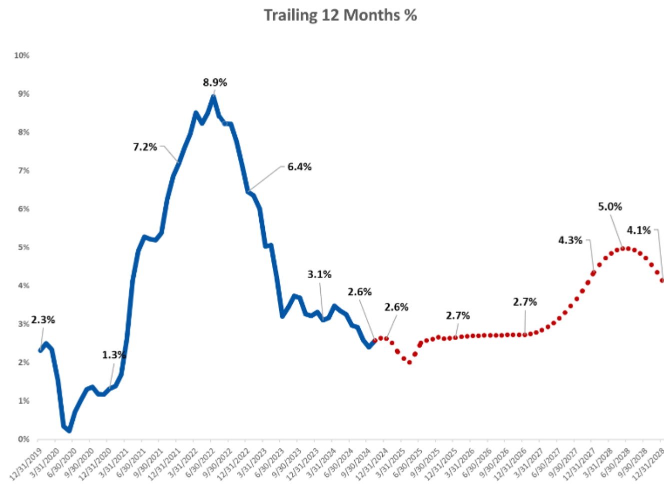
Inflation tends to run through the economy in waves. We are incorporating a second wave of inflation beginning in 2027 and cresting in mid-2028. Until the next wave arrives, CPI inflation should hover around 2.7%, which is where it is today.

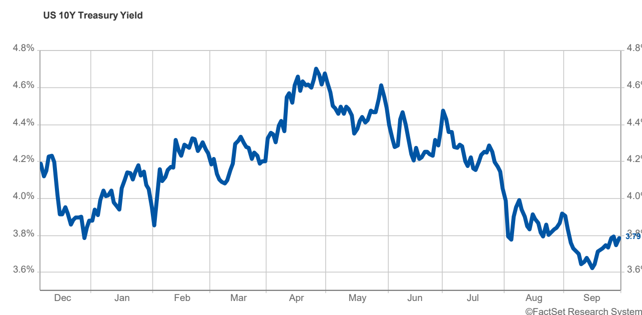
The second wave tends to wreak havoc on bond portfolios. Investors are lulled into the assumption that inflation is dead, lengthening their bond portfolios' duration. Their fixed-income portfolios suffer when the FRB is forced to raise rates.

The graph on the right shows our most recent CPI inflation forecast. We may be early or late in our projections of a pending inflation wave. We know inflation waves tend to come in pairs. We shall see.




## Interest Rates and Credit Markets

Yields moved lower across the curve last month, with the right end of the curve falling a bit more than the left. Fixed-income investors bought into the "Goldie Locks" scenario of modest growth with modest inflation. As outlined below, credit spreads are at record lows, strengthening the "Goldie Locks" fixed income narrative.




The two-year Treasury ended the month at 4.11%, down one basis point, and the 10-year ended at 4.17%, down 11 basis points versus the prior month.

Real rates remain range bond. The real 10-year interest rate has oscillated between 1.5% and 2.0% for the last two years. We view real rates of 2% plus or minus 0.25% as sustainable. We base our long-term ten-year rate (4.75%) on 2.0% real rates plus 2.7% CPI inflation. This is generally higher than most forecasters expect. We increased the 206 and 2027 10-year rate by 0.125% each year to incorporate rate pressure from deficit spending.

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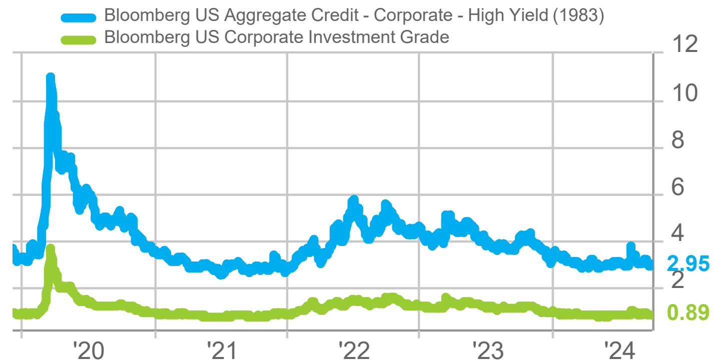
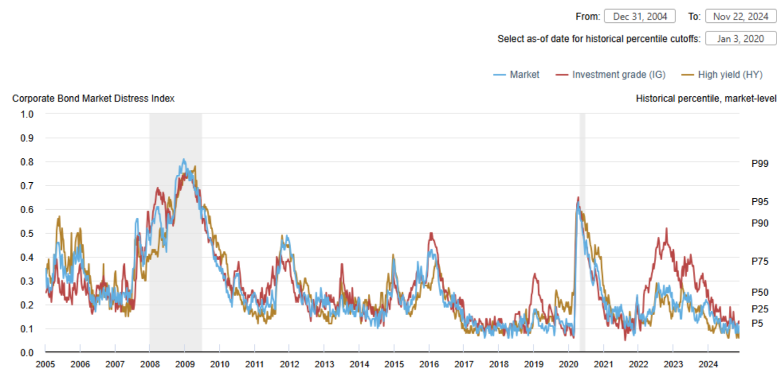
During periods of financial stress, investment grade spreads often widen beyond 2%. During periods of exuberance, they fall below 0.8%. Investment grade spreads ended the month at 0.78%, down six basis points. These spreads discount continued strong economic growth. They are nowhere near signaling a recession or credit stress in large corporate America.




High-yield spreads declined by 17 basis points to 2.66% during the latest month. During periods of economic stress, high-yield spreads often widen to above 8.00%. During periods of exuberance, they fall below 3.5%. We currently classify high-yield spreads as highly exuberant. High-yield credit spreads forecast a "Goldie Locks" economy.

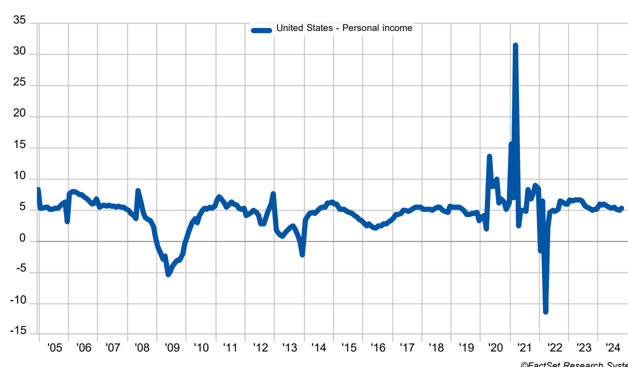
The Federal Reserve Bank of New York calculates the Corporate Bond Market Distress Index (CMDI), a unified measure quantifying joint dislocations in the primary and secondary corporate bond markets. The index incorporates various indicators, including primary market issuance and pricing, secondary market pricing and liquidity conditions, and the relative pricing between traded and nontraded bonds. By this measure, the corporate bond market is functioning at a healthy level. The index is below its historical 5th percentile (least stress) and down from the prior month. Overall, credit remains strong, and defaults are within historical norms.




## The Consumer Sector

The BEA recently updated income and expenditure data covering 1Q2019 to 1Q2024. The BEA substantially increased income estimates, lowering the gap between GDP (expenditures) and GDI (income). As a result, the savings rate is about 2% higher than previously thought.

Personal income rose 0.6% M/M and 4.4% on a Trailing Three-Month Annualized (TMA). Private sector wages and salaries were up 0.5% M/M and 5.8% TMA. Disposable personal income (DPI) was up 0.7% M/M and 4.4% TMA. Wages and other sources of income continue to advance at a modest pace. Consumption rose 0.4% M/M and 4.9% on a TMA.




Disposable personal income (DPI) is what consumers have left after paying income and social security taxes. It is what they use to pay for everything else. DPI slightly outgrew purchases Y/Y, causing the savings rate to rise from 4.1% to 4.4%. As mentioned earlier, the BEA substantially increased income estimates. We had previously expressed concern about the low savings rate. While lower than the 7% level that prevailed before the pandemic, it is substantially higher than the 2.9% initially reported. The revised income figures contributed to our increased confidence in next year's GDP growth rate.

| Personal Consumption Expenditures | | | | |
|---|---|---|---|---|
| | M/M | | Y/Y | |
| | Nominal | Real | Nominal | Real |
| Disposable Personal Income | 0.7% | 0.4% | 5.1% | 2.2% |
| | | | | |
| Durable Goods | 0.3% | 0.3% | 2.9% | 4.6% |
| - Motor Vehicles and Parts | 1.0% | 0.1% | 0.9% | 2.3% |
| - Recreational goods and vehicles | 0.3% | 0.8% | 3.9% | 6.0% |
| Non-Durables | -0.2% | -0.1% | 1.6% | 2.2% |
| - Gas and Other Energy | -1.4% | -0.4% | -12.7% | -0.3% |
| Services | 0.5% | 0.2% | 7.0% | 3.0% |
| - Health Care | 0.5% | 0.4% | 8.2% | 5.5% |
| - Food Service & hotels | 0.7% | 0.3% | 4.4% | 1.2% |
| **Total** | **0.4%** | **0.1%** | **5.4%** | **3.0%** |

Personal Consumption Expenditures (PCE) were up 0.4% for the month and 0.1% on a real basis (after subtracting the impact of inflation). Gas and other energy prices fell 1.0% last month. As is typical, consumers took the extra savings and had a bite to eat, did a little bit of traveling, and bought some recreational goods. After all that fun, they went to the doctor and spent what was left on healthcare.

We expect consumption growth to slow the pace of DPI. We are getting close to that.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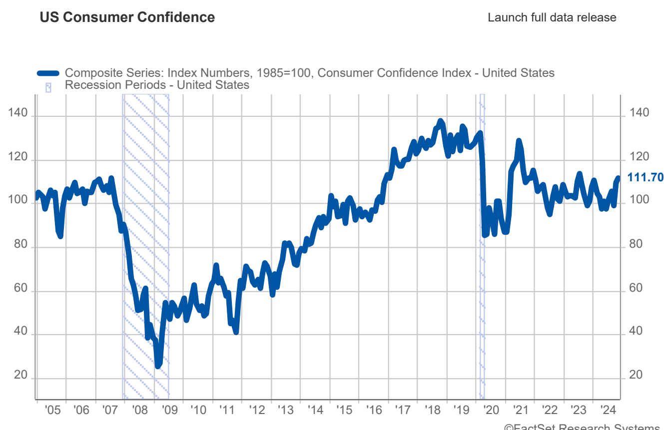
**Confidence**

A clear and decisive election helped boost consumer confidence. In November, the Consumer Confidence Index rose by 2.1 points to 111.7.




The present situation component rose by 4.8 points to 140.9, and the forward-looking expectation component rose by 0.4 points to 92.3. For the expectations component, a reading below the threshold of 80 usually signals a recession ahead.

Lower interest rates, gas prices, higher stock prices, and a clear and decisive election have improved confidence.

"November's increase was mainly driven by more positive consumer assessments of the present situation, particularly regarding the labor market. Compared to October, consumers were also substantially more optimistic about future job availability, which reached its highest level in almost three years. Meanwhile, consumers' expectations about future business conditions were unchanged and they were slightly less positive about future income." said Dana M. Peterson, Chief Economist at The Conference Board.

**Employment Confidence Improved**

The current conditions net employment sub-index (plentiful minus hard to get) rose to 18.2 from 16.5 the previous month. Consumers' outlook for future employment brightened as the net sub-index (more jobs minus fewer jobs) rose to 3.9 from 2.2 the previous month. Consumer confidence reflects the strong labor market.

**Business Confidence Improved**

Consumers' perception of current business conditions also rose as the net sub-index (good minus bad) rose to 6.0 from 5.3 the previous month. Consumers' outlook for future business conditions improved as the net sub-index (better minus worse) rose to 8.3 from 8.1 last month. Consumers' outlook for business conditions brightened modestly.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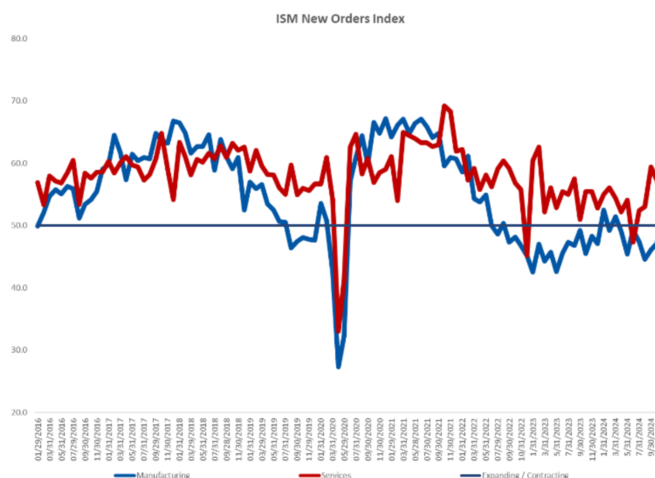
**Inflation Expectations Moderated**
The Conference Board started asking consumers about inflation expectations in 1987. Consumers' expectations for inflation for the next 12 months have remained steady recently. Consumers forecast inflation will be 4.9% in 12 months versus the 5.3% reported the previous month and 7.9% reported in June 2023. This is the first time inflation expectations have been below 5% since March 2020. Inflation expectations are only slightly above the long-term average of 4.8%.

For now, inflation expectations have returned to pre-pandemic levels. This should give the FRB additional cover to continue the easing campaign.

**The Business Sector**
The Institute for Supply Management (ISM) reports monthly on manufacturing and non-manufacturing (service) sector activity. The reports are sentiment-driven and can be influenced by current events. Nonetheless, they do provide real-time clues to what is happening.

The New Orders Index is a leading indicator for the ISM Activities Index and the economy. This chart supports our forecast of a continued shallow manufacturing recession and modest growth for the services industry. The manufacturing new orders index rose above 50 for the first time since March 2024. The service sector index declined slightly but remained elevated, indicating robust growth in new orders. We are curious to see if the improved manufacturing outlook is sustainable.




As a frame of reference, a reading above 50 indicates expansion; a reading below 50 indicates contraction. Readings approximating 50 indicate the same level of activity.
A Manufacturing PMI above 42.5 generally indicates an expansion of the overall economy.

Activity in the service sector expanded but at a slower pace in November. The Services Index fell 3.9 points to 52.1. The breadth of growth held steady, as fourteen industries reported growth, and one additional industry reported contraction. Comments from the ISM included, "The decrease in the Services PMI® in November was driven by decreases in each of the four directly impacting subindexes (Business Activity, New Orders, Employment and Supplier Deliveries). However, 14 industries reported business activity growth, and 13 indicated new orders expansion; both figures are improvements compared to October. This reinforces the view over the last several months that the services sector has returned to sustained growth. Generally, respondents' comments were neutral to positive, and both positive and negative impacts were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attributed to seasonality. Not surprisingly, election ramifications and tariffs were mentioned often, with cautionary outlooks related to the potential impact on respondents' specific industries."

| Non-Manufacturing Sector | Direction | Rate of Change |
|---|---|---|
| Business Activity / Production | Growing | Slower |
| New Orders | Growing | Slower |
| Backlog of Orders | Contracting | Faster |
| Employment | Growing | Slower |
| Prices Paid | Increasing | Faster |
| Supplier Deliveries | Faster | From Slower |
| Service Sector | Growing | Slower |
| Industries Expanding | 14 | -- |
| Industries Contracting | 3 | +1 |

Employment expanded for the fourth time in five months. The employment index fell by 1.5 points to 51.5. 12.1% of respondents reported reducing employment, while 14.0% reported increasing employment. Employment in the service sector continues to grow at a modest pace.

Prices paid for materials and services rose at a slightly faster pace. Prices have risen for 90 consecutive months. The price component rose by 0.1 points to 58.2. 19.3% of respondents reported higher prices, while 5.6% reported lower prices. Inflationary pressures remain a concern for the service sector.

Activity in the manufacturing sector contracted for the eighth straight month in October but at a slower pace. The manufacturing index rose by 1.9 points to 48.4 points. Growth was sparse as only three industries reported growth, and eleven reported contractions. Comments from the ISM included, "U.S. manufacturing activity contracted again in November but at a slower rate compared to last month. Demand continues to be weak but may be moderating, output declined again, and inputs stayed accommodative."

| Manufacturing Sector | Direction | Rate of Change |
|---|---|---|
| Production | Contracting | Slower |
| New Orders | Growing | From Contracting |
| Backlog of Orders | Contracting | Faster |
| Employment | Contracting | Slower |
| Prices Paid | Increasing | Slower |
| Supplier Deliveries | Faster | From Slowing |
| **Manufacturing Sector** | **Contracting** | **Slower** |
| Industries Expanding | 3 | -2 |
| Industries Contracting | 11 | -- |

Employment contracted at a slower pace in November. The employment index rose by 3.7 points to 48.1. 20.5% of respondents reduced employment, while 14.2% increased employment.

Prices paid for materials and services rose at a modest pace. The Prices Index fell by 4.5 percentage points to 50.3. 11.7% of respondents reported paying lower prices, while 12.2% reported paying higher prices.

Overall, activity in the manufacturing sector continues to decline but at a slower rate. This gives hope that the long but shallow manufacturing recession may be coming to an end.

The Federal Reserve Bank of New York tracks supply chain disruptions with its Global Supply Chain Pressure Index (GSCPI). Supply chain pressures have eased slightly and remain within normal ranges. Global supply chains continue functioning within normal ranges, and any supply chain issues are modest and isolated.


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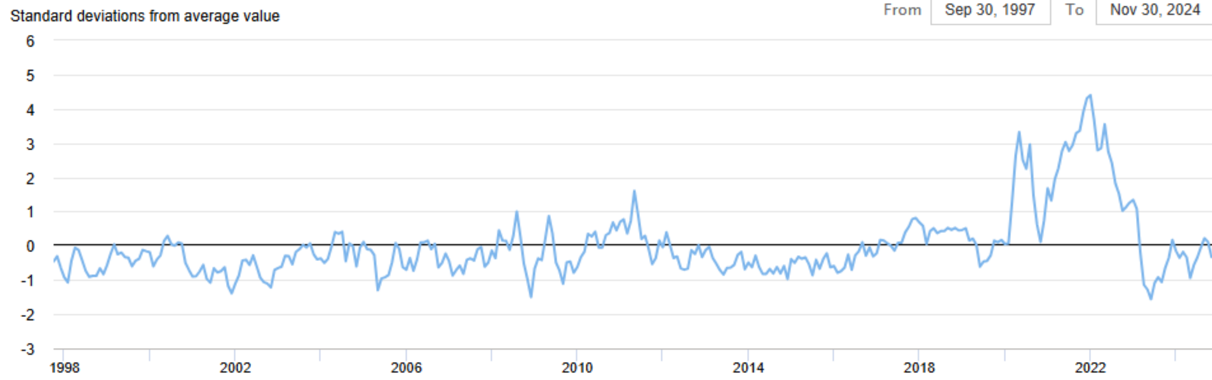


The manufacturing sector continues to experience a modest recession, while the more significant service sector continues to grow steadily. The forward-looking ISM indices point to continued modest economic growth.


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**Abbreviations and Other Terms Used**
This report will use FRB for the Federal Reserve Bank, FOMC for the Federal Open Market Committee, and BLS for the Bureau of Labor Statistics. The FOMC is part of the FRB, which meets eight times yearly to set monetary policy. The primary tool for monetary policy is the Federal Funds Rate (FFR). FFR is the rate set by the FOMC and is the rate at which banks borrow and lend their excess reserves to each other overnight. It forms a floor for short-term interest rates.

We will use the following abbreviations for various governmental agencies.
BEA = U.S. Bureau of Economic Analysis
BLS = U.S. Bureau of Labor Statistics

We will use the terms nominal and real. Nominal values are measured regarding money or things counted in the real world. Retail sales, personal income, expenditures, and corporate earnings are usually reported in nominal dollars. Real values are adjusted for inflation (nominally less inflation). Real values enable comparisons that are not distorted by inflation. GDP numbers are usually reported as real growth.

Other abbreviations are commonly used.
QTD = Quarter-to-date
YTD = Year-to-Date
M/M = Month Over Month
TMA = Trailing Three-Month Annualized
Y/Y = Year Over Year

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