THE ECONOMIC OUTLOOK GROUP

475 Wall Street
PRINCETON, NEW JERSEY 08540 Tel: (609) 529 -1300
www.EconomicOutlookGroup.com

ECONOMIC TALKING POINTS

Bernard Baumohl
Chief Global Economist

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Current pace of retail sales is unsustainable. But the other big story for 2025 will be manufacturing employment and output.

The question that has bedeviled experts at the Federal Reserve and many private economists the last few years is just how fast can the economy grow before it breaks into an inflationary sweat? Simply put, where is the economy's speed limit?

The long held view of the red zone is once the GDP growth rate accelerates past 1.8% - 2.0%. A sustained period of expansion beyond that range will cause the economy to overheat (in the absence of a major improvement in productivity). Or at least that is the conventional thinking.

Yet, the economy has been racing ahead closer to a 3% clip most of this year, fueled in large part by a resilient consumer. And today the Federal Reserve Bank of Atlanta projected that GDP growth in the final quarter of 2024 could actually exceed 3%!

In addition, the December survey by NAHB showed homebuilder confidence for sales over the next six months leaped to its highest since April 2022!

Now let's toss into this frothy pot the latest news on retail sales, which rose by a better than expected 0.7% in November. Most of the jump went to purchase cars and auto parts as Americans sought to replace autos and trucks that were damaged or lost during hurricanes Helene and Milton. Another contributing factor was a rush to buy EVs before the year is out to lock in the $,7,500 tax credit for such new vehicles and $4,000 for similar used ones. President-elect Trump warned he would end such incentives once he takes office in January. Other storm-related purchases

increased as well and include building material, garden equipment and supplies, as well furniture and home furnishings.

Not surprisingly, inflation pressures picked up in recent months given all this robust activity. Yet traders in the financial markets appear convinced the Fed will ease its grip on the monetary brakes again and cut interest rates another quarter point.

Why do so? Good question. We don't believe it is warranted.

Well, perhaps the Fed is looking past those categories. If we peel off the headline numbers in retail sales and examine some of its components, one can reasonably argue this holiday shopping season may be the last "Hurrah" before consumers pull back in early 2025. Case in point: Americans in November scaled back on dining out. Spending on food services and drinking places dropped 0.4% last month, the first decline since last March and the biggest pull back since January of this year. This shouldn't come as a shock given the record level of household debt and interest rates. Something had to be compromised.

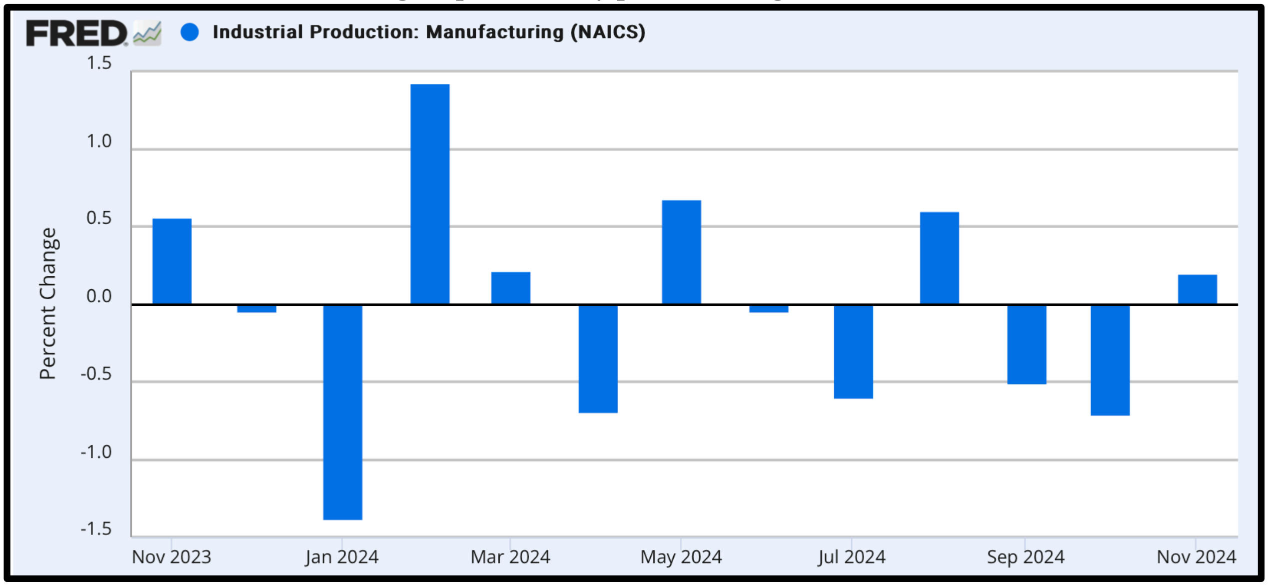
Estimated Change in monthly Sales for Retail and Food Services, by Kind of Business

NAICS code	Kind of Business	Percent Change[1]					
		Nov. 2024 Advance from --		Oct. 2024 Preliminary from --		Sep. 2024 through Nov. 2024 from --	
		Oct. 2024 (p)	Nov. 2023 (r)	Sep. 2024 (r)	Oct. 2023 (r)	Jun. 2024 through Aug. 2024	Sep. 2023 through Nov. 2023
	Retail & food services, total	**0.7**	**3.8**	**0.5**	**2.9**	**1.8**	**2.9**
	Total (excl. motor vehicle & parts)	0.2	3.2	0.2	2.7	1.3	2.8
	Total (excl. gasoline stations)	0.7	4.4	0.5	3.8	2.0	3.8
	Total (excl. motor vehicle & parts & gasoline stations)	0.2	3.9	0.2	3.8	1.6	3.9
	Retail	0.9	4.1	0.4	2.7	1.7	2.9
441	**Motor vehicle & parts dealers**	**2.6**	**6.5**	**1.8**	**3.7**	**3.9**	**3.5**
4411, 4412	Auto & other motor veh. dealers	2.8	7.0	2.0	4.1	4.3	3.7
442	**Furniture & home furn. stores**	**0.3**	**0.7**	**-0.7**	**2.6**	**1.1**	**1.5**
443	**Electronics & appliance stores**	**0.3**	**1.2**	**2.4**	**-2.2**	**-2.8**	**-2.0**
444	**Building material & garden eq. & supplies dealers**	**0.4**	**4.1**	**0.8**	**3.2**	**2.3**	**3.1**
445	**Food & beverage stores**	**-0.2**	**1.8**	**-0.1**	**2.2**	**0.7**	**2.1**
4451	Grocery stores	-0.2	1.7	-0.1	2.2	0.7	2.1
446	**Health & personal care stores**	**0.0**	**1.8**	**-1.1**	**1.5**	**2.2**	**2.9**
447	**Gasoline stations**	**0.1**	**-3.9**	**0.1**	**-7.3**	**-1.7**	**-7.4**
448	**Clothing & clothing accessories stores**	**-0.2**	**2.2**	**0.4**	**3.6**	**0.5**	**2.9**
451	**Sporting goods, hobby, musical instrument, & book stores**	**0.9**	**-1.4**	**-0.6**	**-2.5**	**1.2**	**-1.9**
452	**General merchandise stores**	**-0.1**	**3.1**	**0.0**	**3.0**	**0.8**	**3.0**
4521	Department stores	-0.6	1.4	-0.1	0.0	-0.6	0.0
453	**Miscellaneous store retailers**	**-3.5**	**0.8**	**-0.8**	**4.7**	**0.8**	**4.3**
454	**Nonstore retailers**	**1.8**	**9.8**	**0.1**	**6.9**	**2.7**	**8.0**
722	**Food services & drinking places**	**-0.4**	**1.9**	**0.9**	**4.2**	**1.9**	**3.2**

Another data point out today was November's industrial production, which slipped 0.1%, its third consecutive monthly slide. Much of that decline was due to the steep downturn in mining activity and utilities. But there was a mild 0.2% pop in manufacturing output in November, only the second increase in six months! These

factories had to ratchet up their production at some point simply to satisfy the strong demand for goods this holiday season.

Manufacturing output, monthly percent change



The big story really is what happens next. Output and employment in manufacturing will take on much greater significance in 2025 in light of the policies planned under Trump 2.0.

How will the arsenal of tariffs that Trump wants to impose impact the US factories? Will such import taxes, which are mostly meant to protect domestic producers from foreign competition, help propel local production and boost hiring? Or will these tariffs raise the cost of imported raw material and intermediate goods to a point where it cuts into the profits of US manufacturers and forces them to slash other operating expenses, such as through layoffs?

While we do not yet know precisely what configuration these tariffs will take, Trump seems determined to ordain them. Once he does, the spotlight should fall on the manufacturing sector and the resulting fallout.