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Economic Update

OCTOBER 2024

Commentary

What a difference a month can make in the markets! A little more than a month ago, many were pointing to an impending recession and an extremely aggressive Fed rate cutting cycle. After a slew of better-than-expected economic reports, the market is now worried about a possible re-acceleration of the economy rather than a recession.

The main impetus of the changing mindset was the much stronger-than-expected labor report that was released in early October. Coming into that report, the trend had been decreasing job gains (along with revisions lower from previous months) and an increasing unemployment rate. The October data showed just the opposite. Job growth was almost double the consensus and reached its highest pace since March. The unemployment rate dropped back to June's level of 4.1%. In addition, wage inflation ticked back up.

Later in the month, the retail sales data showed that consumer spending remains strong. The data from that report that feeds into the gross domestic product (GDP) calculation (called "control-group sales") surged by more than twice the level expected and gained by the most in three months. Control group sales ended the third quarter at a 6.4% annualized pace. As long as consumer spending remains elevated, the economy will avoid a recession.

Despite the improved economic data, we believe that the odds of a re-acceleration of the economy remain relatively low. Labor market data is extremely volatile with a high margin of error, so it's important not to make too much out of one data point. The overall trend continues to show a labor market that has weakened from the beginning of the year. Consumer spending has held up well, but there are signs of consumer stress. Credit card delinquencies are at multi-year highs, and consumer sentiment remains subdued.

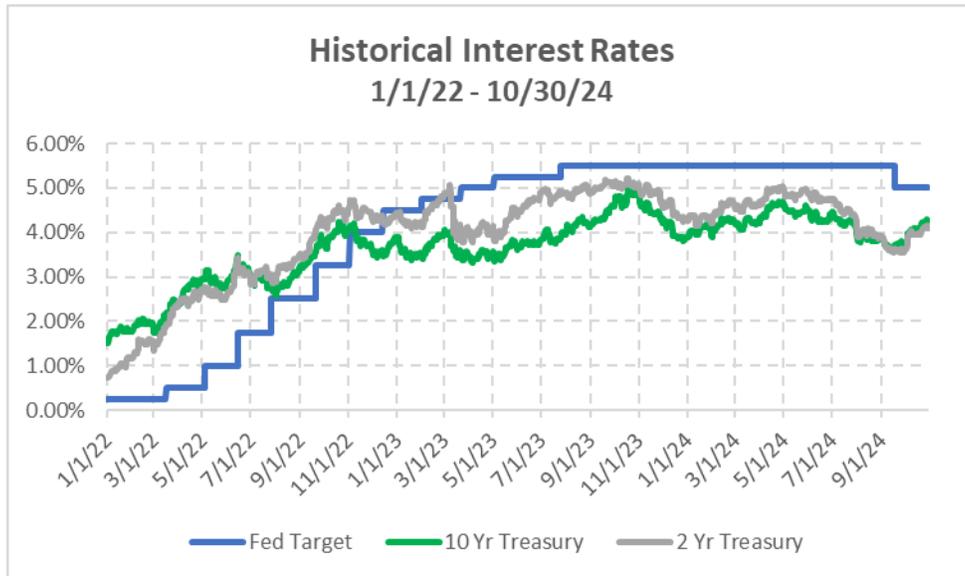
Turning to the election, which is now less than a week away, the betting markets point to a close race, but increased odds of a Trump victory (along with a good chance of a Republican sweep of Congress). Regardless of the ultimate winner, we expect the majority of the tax cuts, which are due to expire in 2025, to be extended. In addition, the proposals from both presidential candidates point to a continuation of elevated federal government deficits. For fiscal policy, control of Congress matters just as much as control of the White House. Congress has less control in areas related to tariffs and immigration. Therefore, the winner of the presidential election will have wider latitude to make immediate policy changes in those areas.

THIS MONTH

- COMMENTARY
- FIXED INCOME OUTLOOK
- LABOR READINGS
- INFLATION READINGS
- CONSUMER READINGS

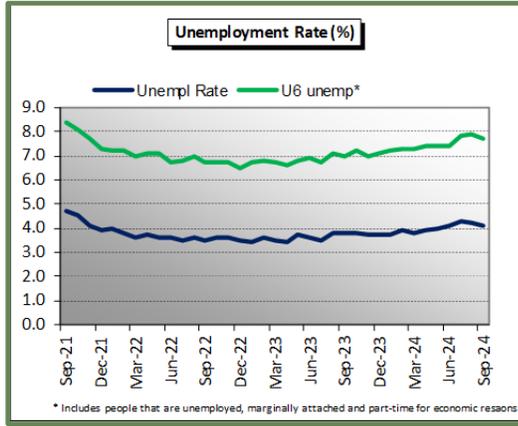
Fixed Income Outlook

Treasury bond yields moved significantly higher during October on the back of much stronger-than-expected labor market and consumer spending data. The medium to long end of the curve shifted up by approximately 50 basis points. Market pricing is now aligned with the Fed’s latest projections, which has a 25 basis point cut at each of the next two meetings this year and a rate of 3.50% at the end of 2025. We believe there is a higher risk of a recession than a re-acceleration of the economy and therefore view the recent backup in yields as a good opportunity to add duration.



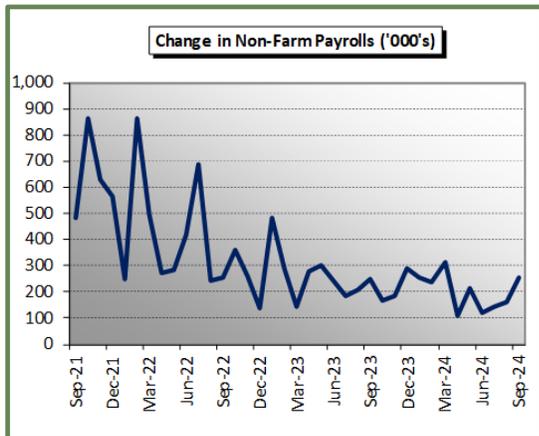
Labor Readings

(Data source: Bloomberg)



Unemployment Rate Declines Again

The unemployment rate in September declined for the second consecutive month. The rate was expected to remain unchanged at 4.2% but declined to 4.1%. The underlying details of the report were strong. The labor force expanded, and the number of employed increased significantly.

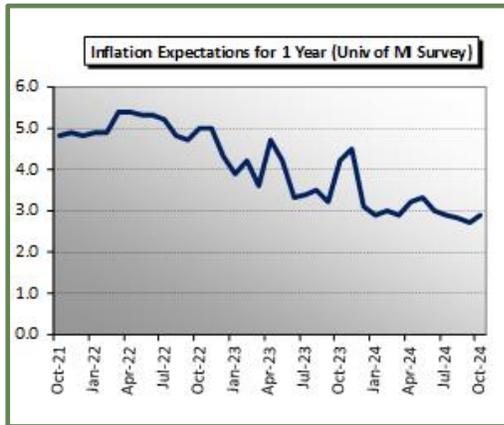


Payroll Growth Much Stronger than Expected

Payrolls expanded by 254,000 jobs in September versus an expected gain of 150,000. In addition, the prior two months were revised upwards, which broke a trend of negative revisions. Despite the upside surprise, the breadth of job gains remains relatively weak.

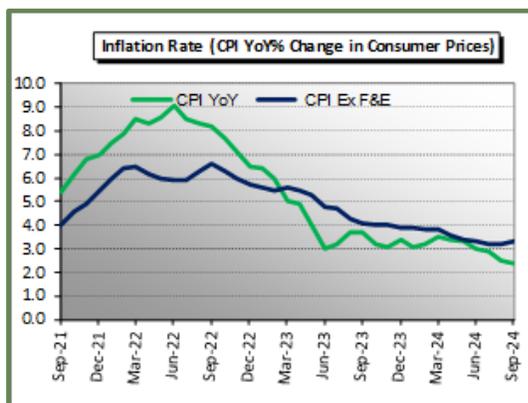
Inflation Readings

(Data source: Bloomberg)



Inflation Expectations Tick Up

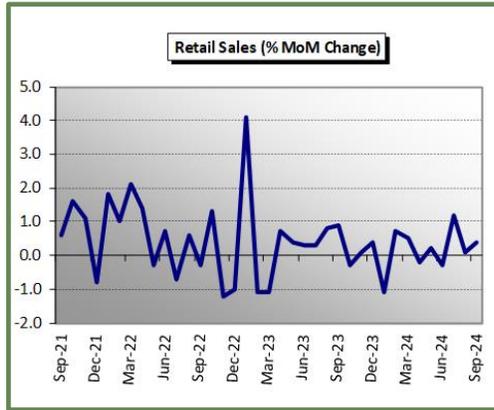
Consumers' inflation expectations for the next year increased for the first time in five months in October. Consumers expect prices to climb by 2.9% compared to 2.7% for the previous month. Consumers expect inflation to gain more than their income in the next year, dropping their perception of their financial situation to the lowest level since 2022.



Consumer Inflation Rises More than Expected

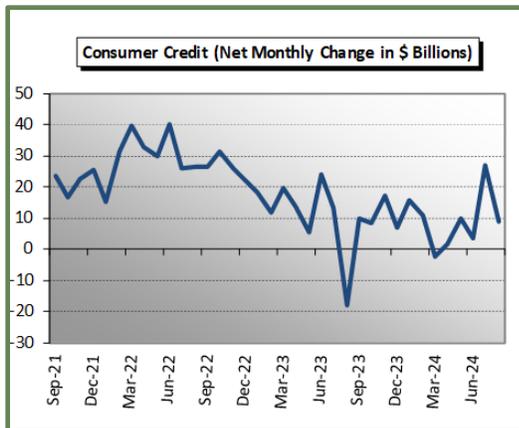
Consumer inflation in September rose slightly more than expectations. The year-over-year change in core inflation experienced its first gain in 17 months. Grocery prices increased by the most since the start of the year. Shelter prices eased from the pace of the prior month, but car insurance, medical care and airfares saw strong price increases.

Consumer Readings
(Data source: Bloomberg)



Retail Sales Show Consumer Strength

Retail sales in September were higher than expected. The gains were broad-based, as 10 of the 13 categories saw increases. Control-group sales, which feed into the GDP calculation, increased by a 6.4% annualized pace in the third quarter, the largest increase since early 2023.



Consumer Borrowing Pace Recedes

Consumer borrowing in August increased at a slower pace than the previous month and lower than expectations. Credit card balances experienced their largest decline since March 2021.