Capital Markets Strategy

Essential inCights for the C-Suite

“Soft Landing” for the US Consumer

Recent Trends in Sentiment, Spending, Savings & Wages

JUL 2024


"Man is born free,
and everywhere he is in chains."
First and most acclaimed line in "The Social Contract"
by philosopher Jean-Jacques Rousseau (1712-1778)

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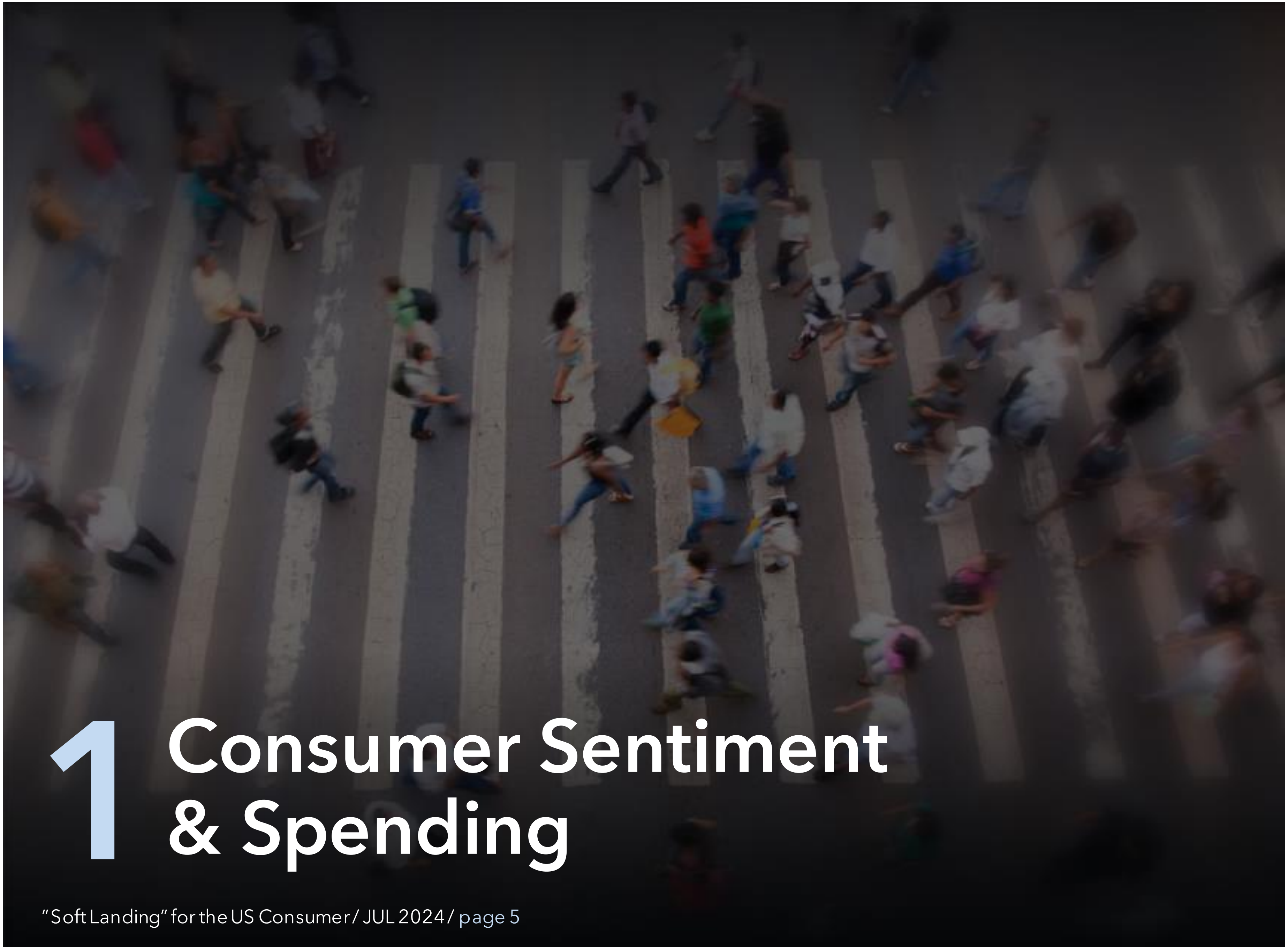
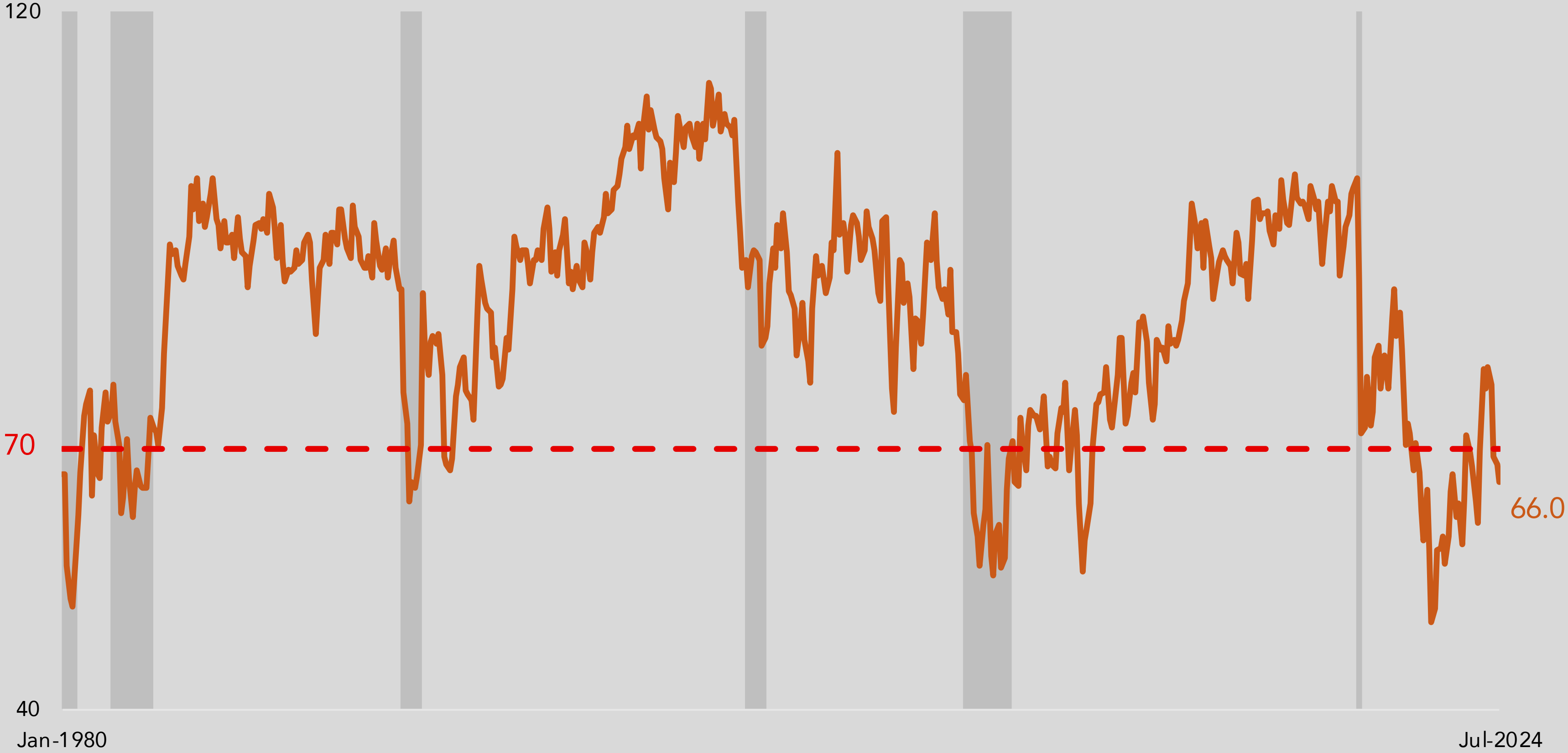


1 Consumer Sentiment & Spending

Consumer Confidence Subdued

Prior to 2008, declining consumer confidence was a strong indicator of high recession risk. Specifically, the University of Michigan consumer confidence index typically dipped below 70 during recessions. However, post 2008, the relationship between consumer confidence and recessions has declined. More recently, softer labor markets, higher gas prices and elevated interest rates have weighed on sentiment while consumer spending has remained resilient.

University of Michigan consumer sentiment

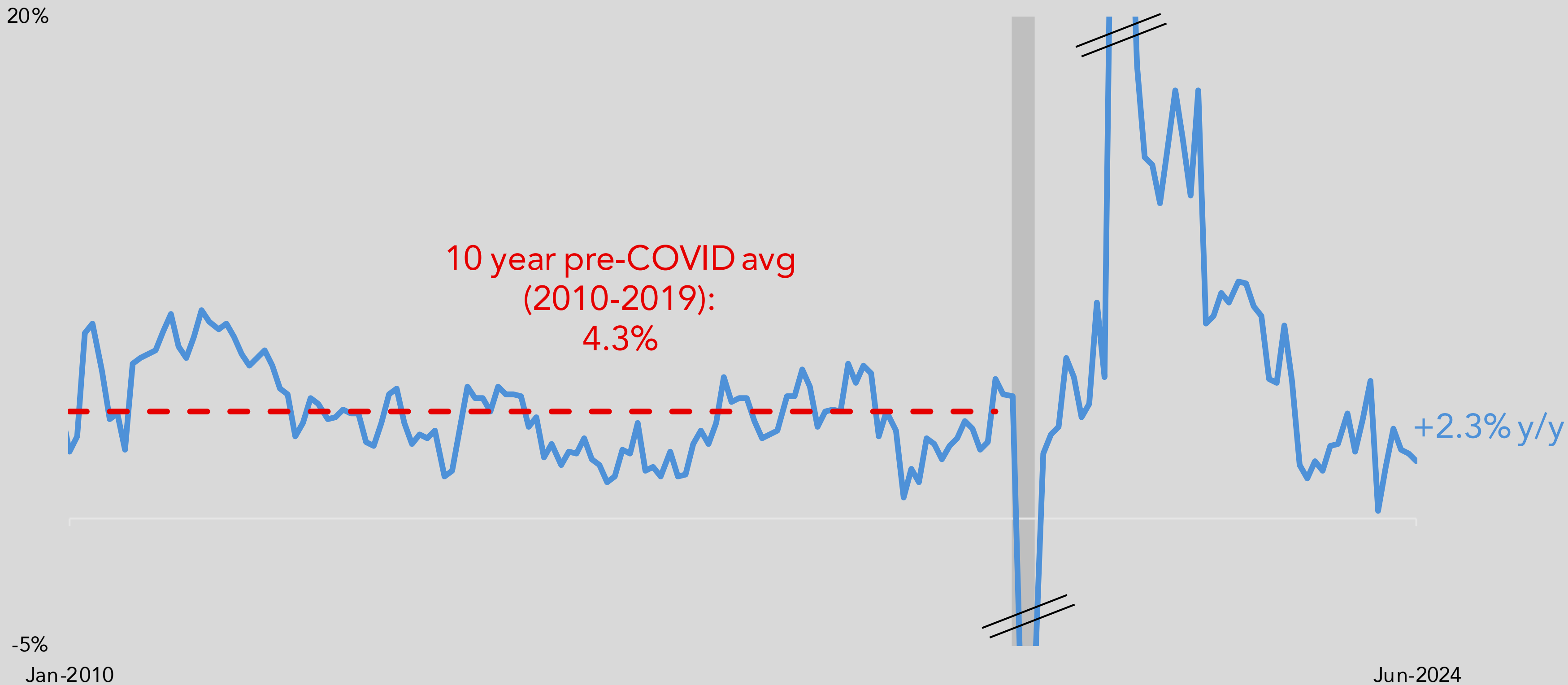


Source: (1) Bloomberg. Data as of July 12, 2024. Oxford Economics "US: Subdued consumer sentiment not reflected in the spending data" (July 12, 2024).

"Soft Landing" in Consumer Spending

The recent normalization in consumer spending growth from the COVID-era reflects a "cooling" in US economic growth rather than a contraction. While lower income households are bearing the brunt of a cooling labor market and "sticky" inflation, US consumer spending is more dependent on middle and upper income households. Though the June retail sales data was softer at a headline level, the underlying data points to continued resilience in most sectors and roughly 2% annualized consumer spending in Q2.

US retail sales y/y

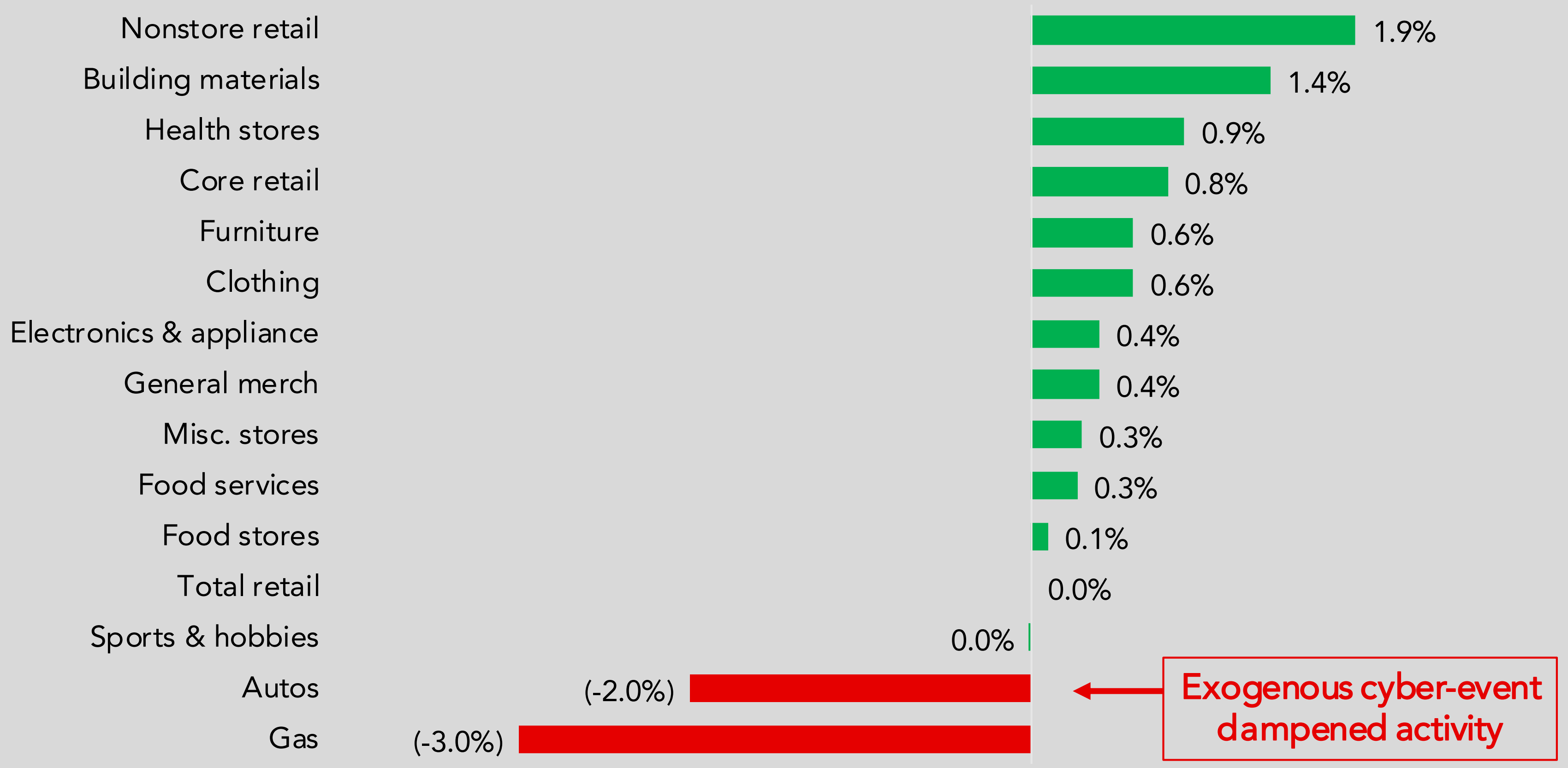


Source: (1) Bloomberg. Data as of July 16, 2024. FRED. Real retail sales are adjusted for inflation. Capital Economics "US Retail Sales (Sep.), Real consumption growth muted as higher rates bite)."

US Retail Sales Exceed Expectations

Headline retail sales were unchanged in June, exceeding consensus expectations for a (-0.3%) contraction. The underlying data suggests that the US consumer is still strong, though taking a slightly more cautious approach toward spending. Nearly every category of retail sales increased in June with the exception of gas and autos where a cyber-attack caused widespread software outages for dealers.

US retail sales by category, m/m

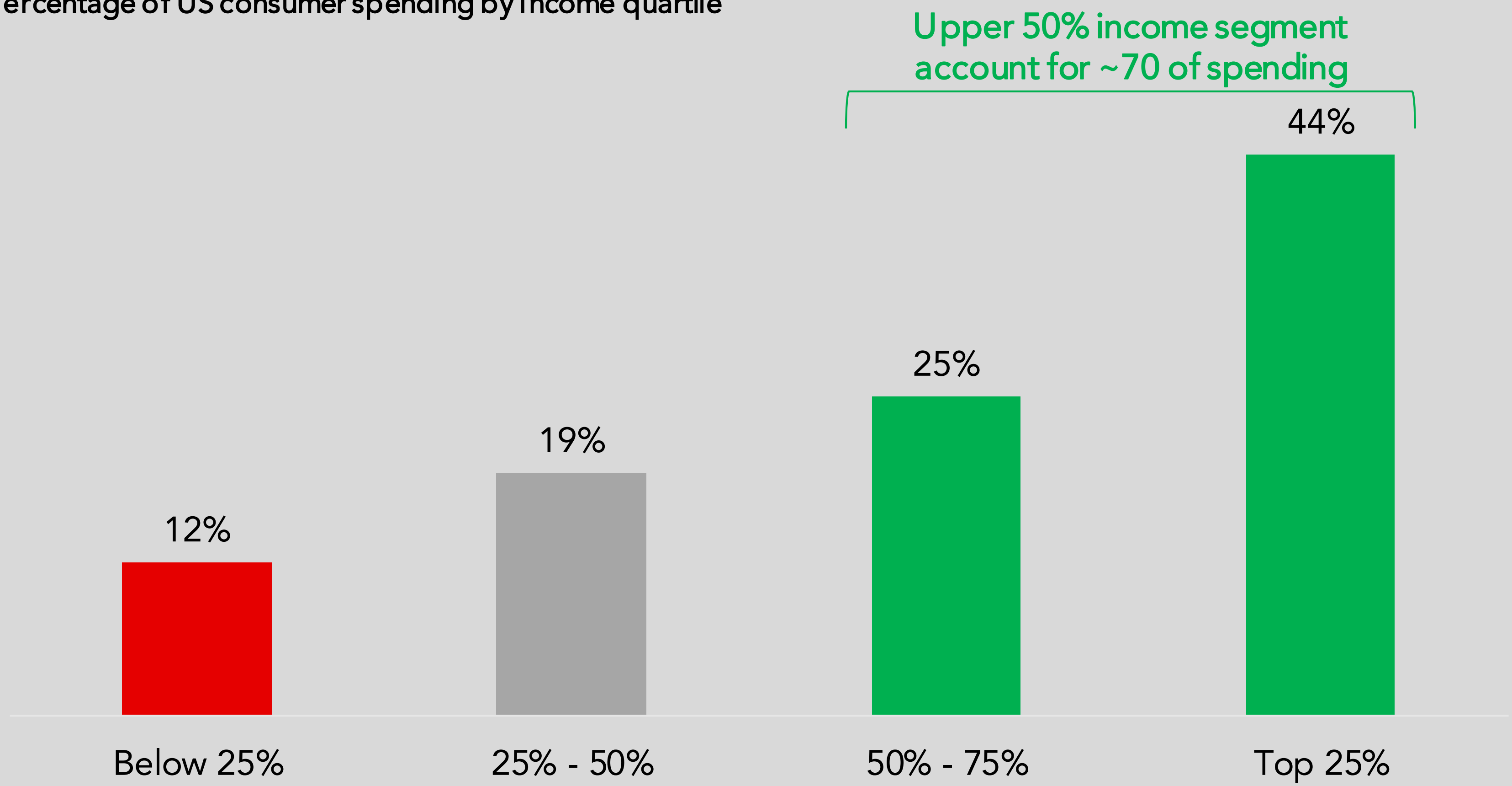


Source: (1) Bloomberg. US Census. Data as of July 17, 2024. Core retail sales excluded motor vehicles & parts and gasoline.

Higher Income Households Drive Consumption

Households in the bottom quartile of earnings account for just 12% of overall US consumer spending while the upper 50% account for ~70% of US consumption. While slower consumption from lower-income households may challenge specific retailers, the impact to broader economic growth should be contained.

Percentage of US consumer spending by income quartile



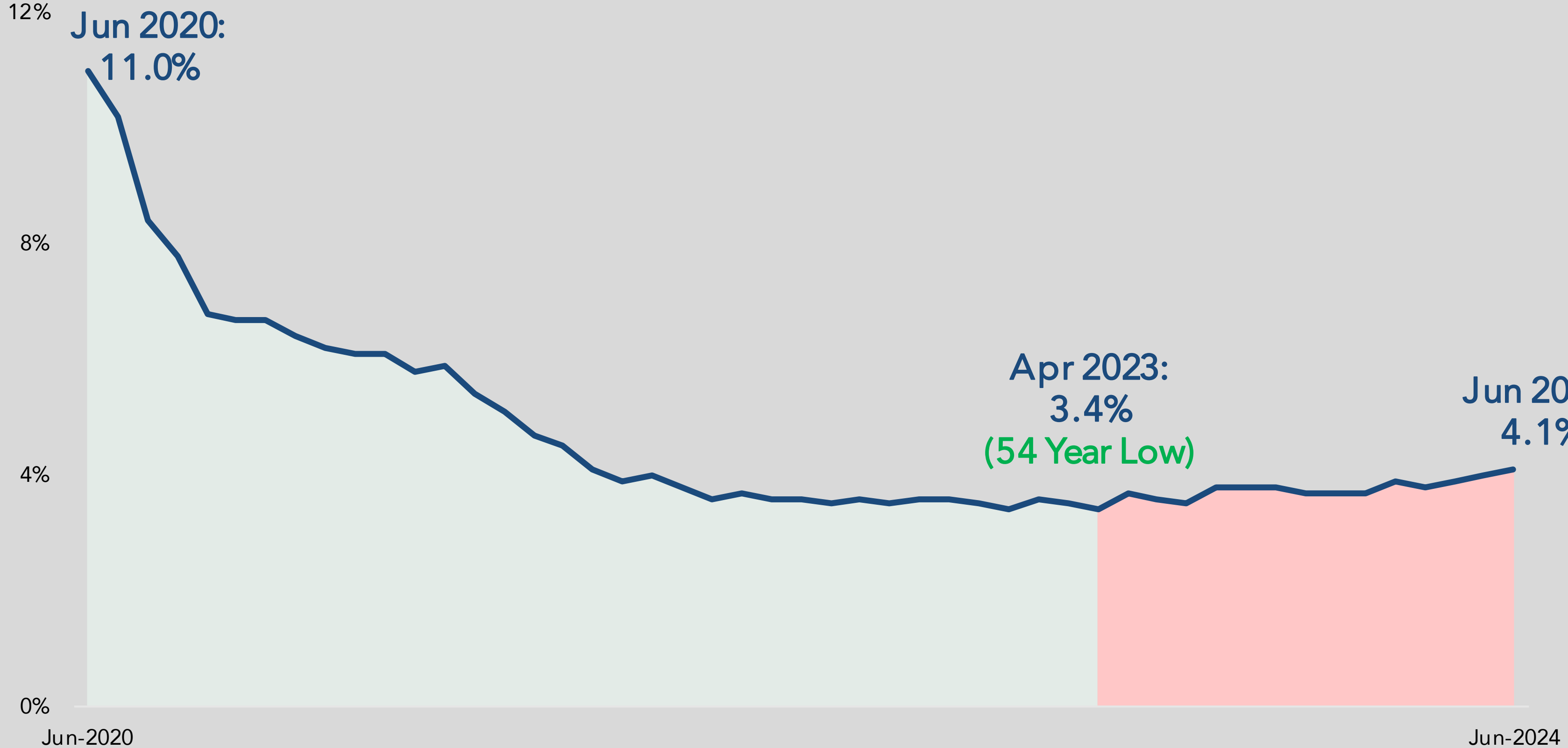
Source: (1) Oxford Economics "US: Low-income consumers feeling the slowing economy" (May 31, 2024).

2 Labor Markets & Wage Growth

US Unemployment Rate Rising

US unemployment edged slightly higher from 4.0% to 4.1% in June. While still low by historic standards, the unemployment rate has been rising steadily for 14 months, since hitting a cyclical and 54 year low of 3.4% in April 2023. The June employment report itself was also "soft" with downward revisions to job growth in the prior two months, the slowest wage growth in three years and an uptick in unemployment.

US unemployment rate

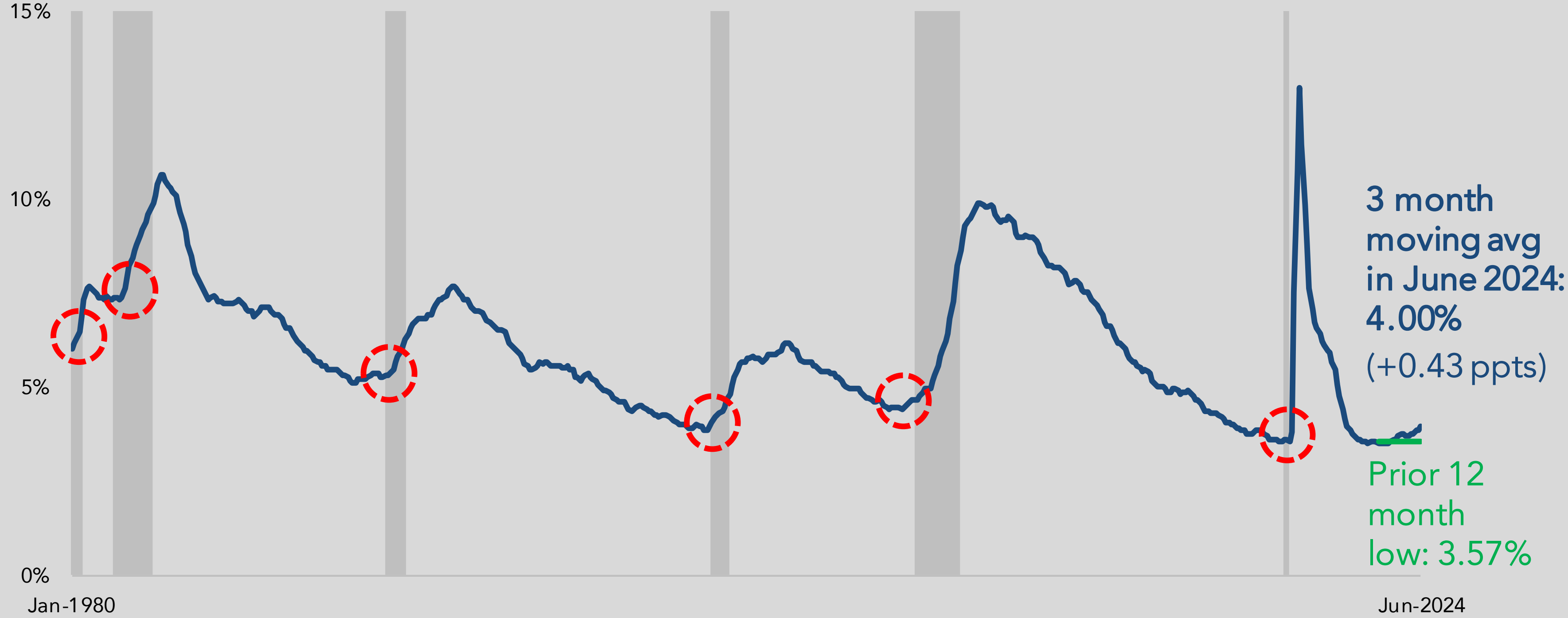


Source: (1) Bloomberg. Data as of July 8, 2024.

Sounding the "Sahm"

June's 4.1% unemployment rate came close to triggering the so-called "Sahm Rule", a signal that has accurately predicted all 12 US recessions since WWII, with only two false positives (1959 and 2003). The "Sahm Rule" was named after former Federal Reserve and Council of Economic Advisors economist Claudia Sahm, who observed in 2019 that US recessions historically "begin" when the 3-month moving average of the national unemployment rate rises by 0.5 percentage points or more relative to its low during the prior 12 months. <u>However, this cycle may be different</u>, with structurally tight post-COVID labor markets, and a 54-year low in unemployment in April 2023, <u>possibly raising the "Sahm Rule" threshold this time.</u>

US unemployment rate, 3 month moving average

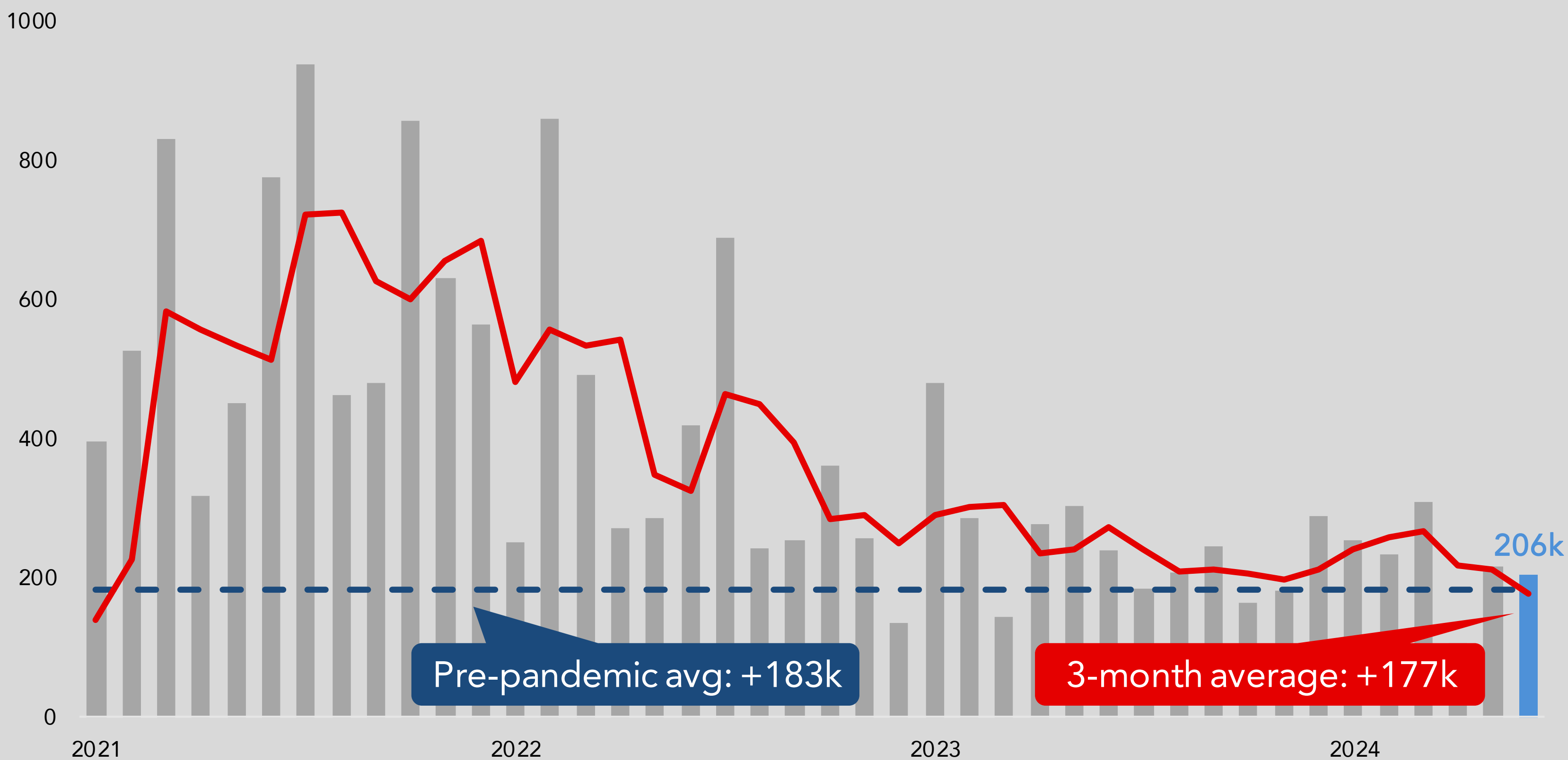


Source: (1) Bloomberg. Data as of July 8, 2024. Prior 12 month low refers to 3 month moving average.

Nonfarm Payrolls Converging with Pre-COVID Average

Nonfarm payrolls have decelerated, suggesting that US labor markets may be rebalancing. June's payroll report exceeded consensus expectations. However, the notable revisions lower to April and May data dragged the 3-month moving average job gain down to 177k, the lowest since January 2021 and below the pre-pandemic average.

US nonfarm payrolls, monthly change, thousands

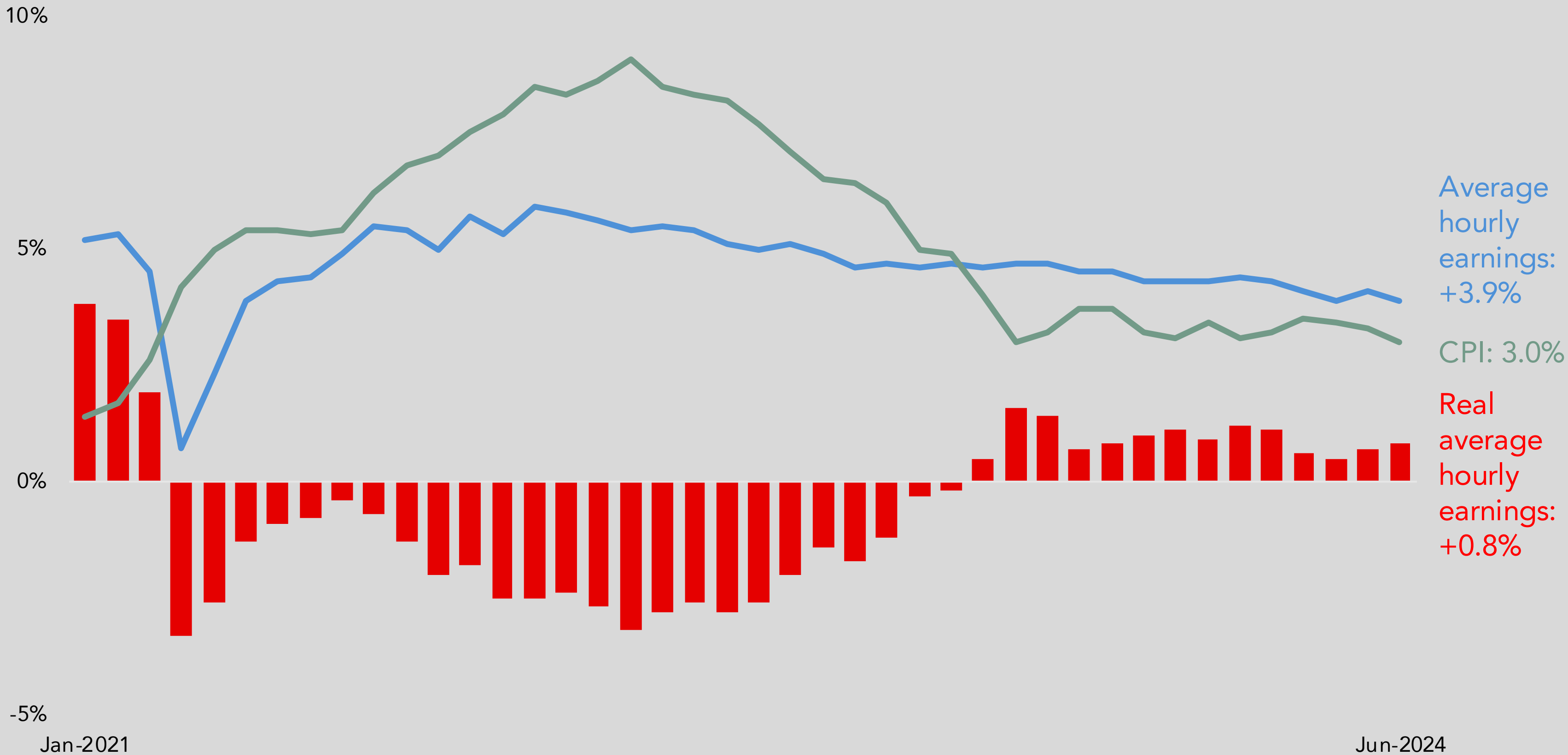


Source: (1) Bloomberg. Data as of July 17, 2024.

Real Wage Growth <1%

Real wage growth turned positive in May 2023 as inflation rapidly decelerated from its 2022 peak. Real disposable incomes and wages, however, are growing below 1% while wage growth has decelerated for lower-income sectors in particular. Lower-income households are also disproportionately impacted by inflation, creating additional challenges for household disposable income.

y/y change in real and nominal earnings and CPI

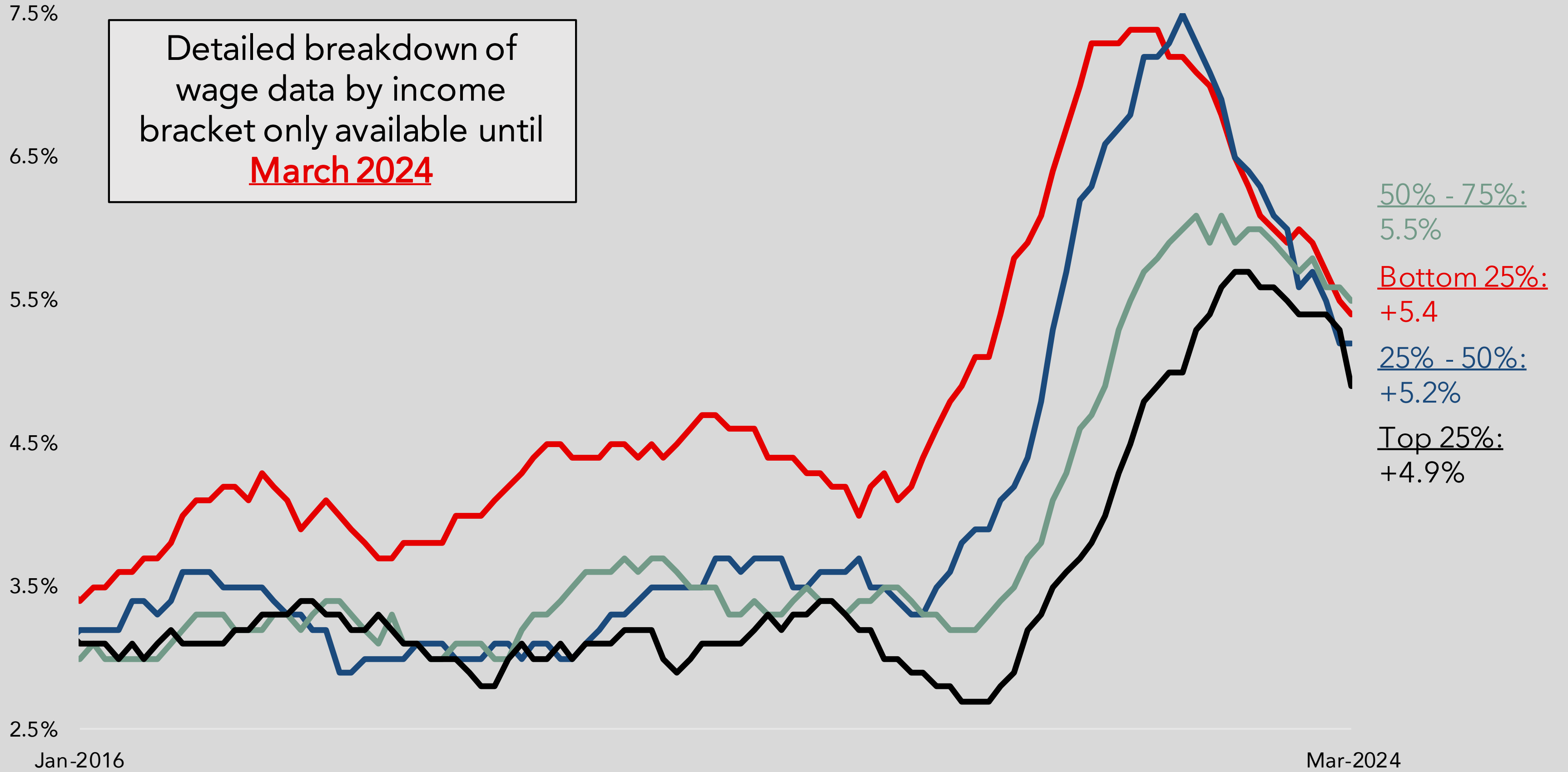


Source: (1) Oxford Economics, "Low-income consumers feeling the slowing economy" (May 31, 2024). Bloomberg. Data as of July 12,2024.

Wage Inflation by Income Bracket

In the early days of the COVID pandemic, lower-wage industries experienced the sharpest labor shortages, thereby driving the largest and most rapid hourly wage increases. In recent months, labor supply-demand dynamics have re-balanced and the wage premium for lower-wage industries has declined.

Hourly wage growth by quartile , 12 month moving avg

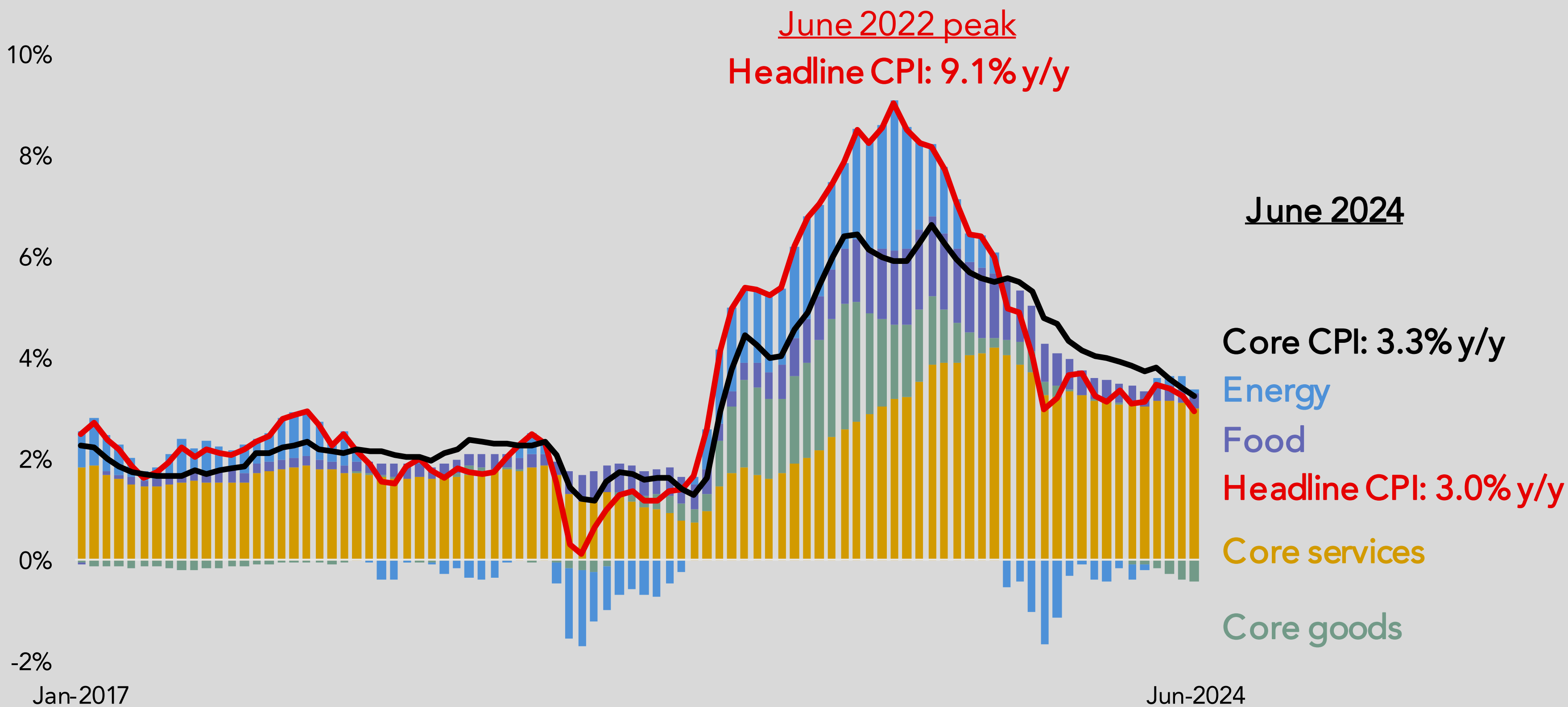


Source: (1) Atlanta Fed Wage Growth Tracker. 12-month moving average of median wage growth, hourly data. Data as of July 12, 2024.

First Post-COVID M/M Inflation Decline

US headline and core CPI eased more than expected in June, following a soft May inflation print. Headline inflation decelerated to 3.0% y/y, down from 3.3% y/y in May, while the monthly measure decreased (-0.1%), the first decline since the onset of the pandemic. Though US disinflationary forces have gained momentum, "sticky" services inflation has disproportionately impacted lower income household spending.

Breakdown of CPI by components

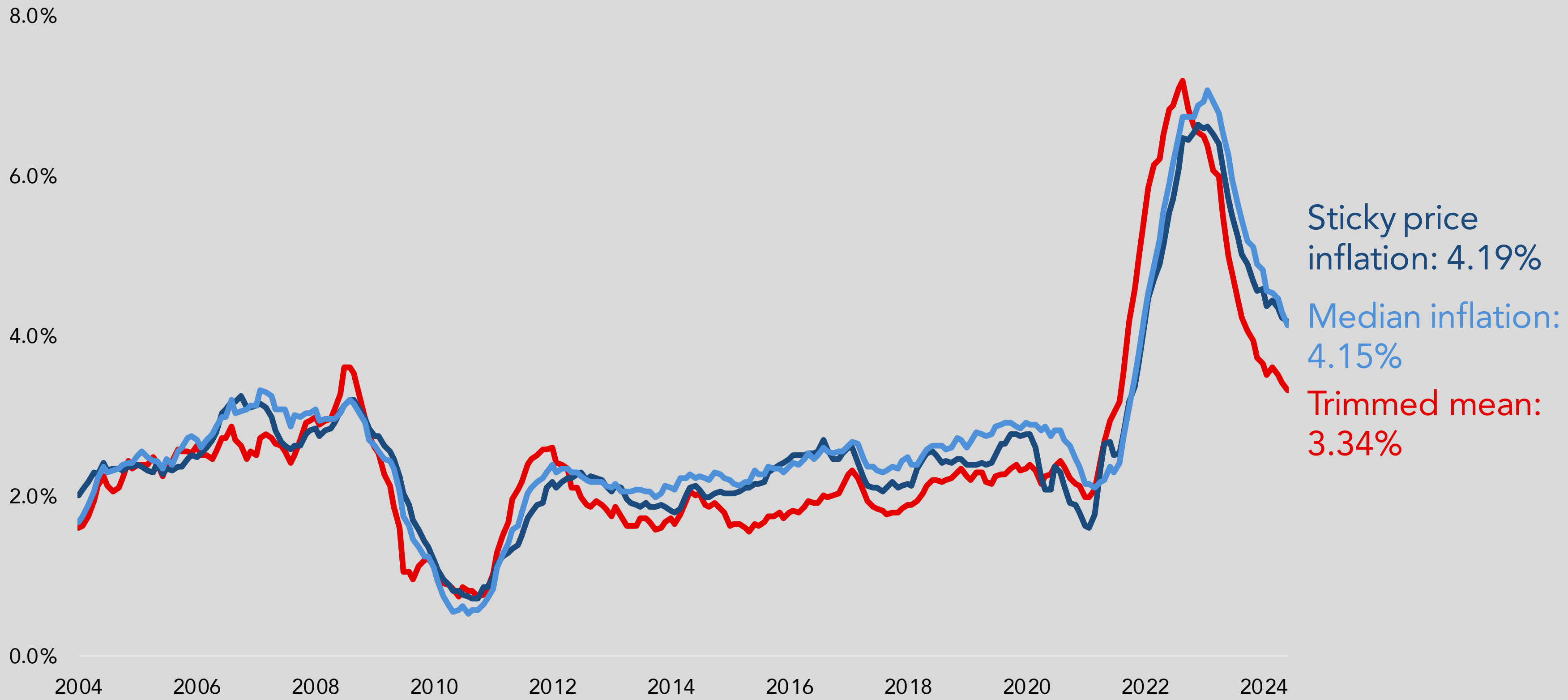


Source: (1) Bloomberg. Data as of July 17, 2024.

Steady US Disinflation Pace Underway

A series of "sticky" US inflation reports in Q1 entailed a mix of "seasonality" and "noise" that masked an underlying disinflation trend that is clearly underway. Three important benchmark measures of inflation, the Cleveland Fed's trimmed mean measure (which excludes the most significant outliers in either direction), the Atlanta Fed's sticky price index, and the Cleveland Fed's median CPI index, are all coming down.

US inflation measures, y/y

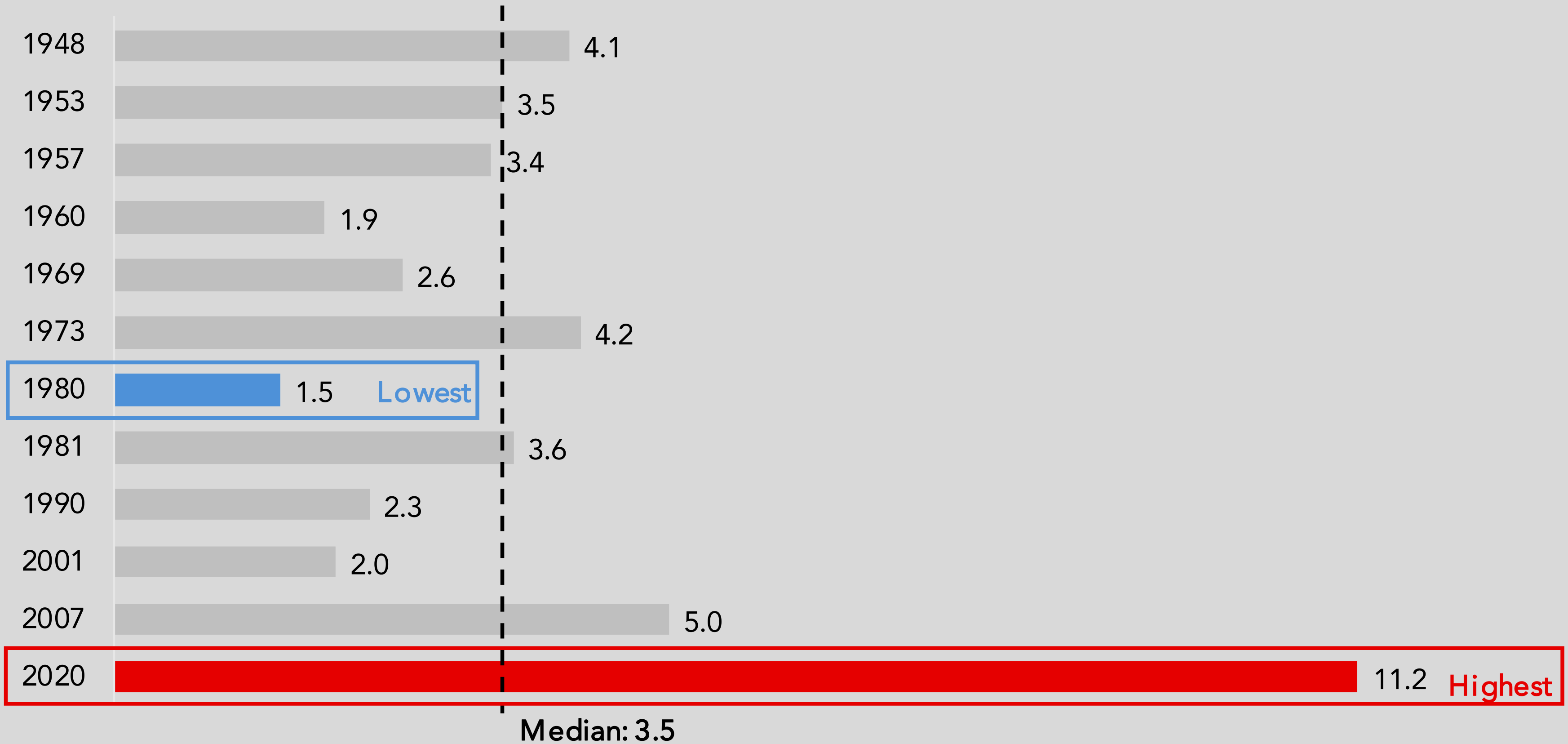


Source: (1) Bloomberg, "Cuts Are in the Air After Inflation Surprise" (John Authers). Data as of July 12, 2024.

Labor Markets Provide Buffer for Recession Timing

The unemployment rate has risen in every one of the 12 US recessions since WWII. Historically, unemployment has increased by approximately 0.4% from its trough to the "start of the recession," and an average of 3.5% from trough "to peak" during and after the recession. Additionally, in every post-WWII US recession the unemployment rate has risen to above 6.0% at its peak.

Change in unemployment rate, from trough to peak, during and after recession



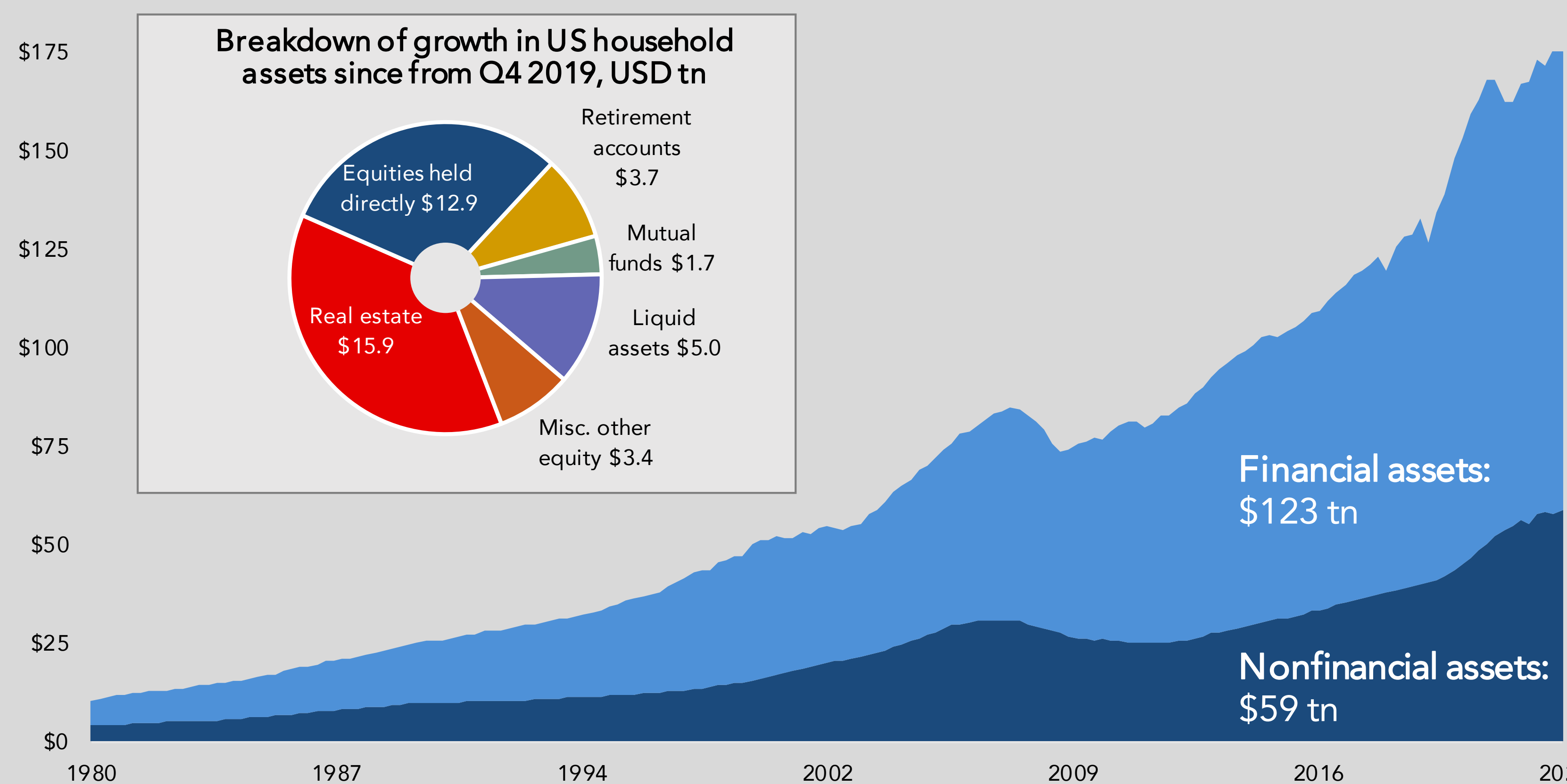
Source: (1) Bureau of Labor Statistics. Bloomberg.

3 Consumer Assets & Liabilities

Equities, Real Estate Drive $40 Tn Household Balance Sheet Increase

Total US household balance sheets increased over $40 trillion since the end of Q4 2019. The combined increase in equity holdings and real estate values have accounted for over two-thirds of the increase in US consumer balance sheet assets since the COVID crisis began.

US household balance sheet assets, USD tn



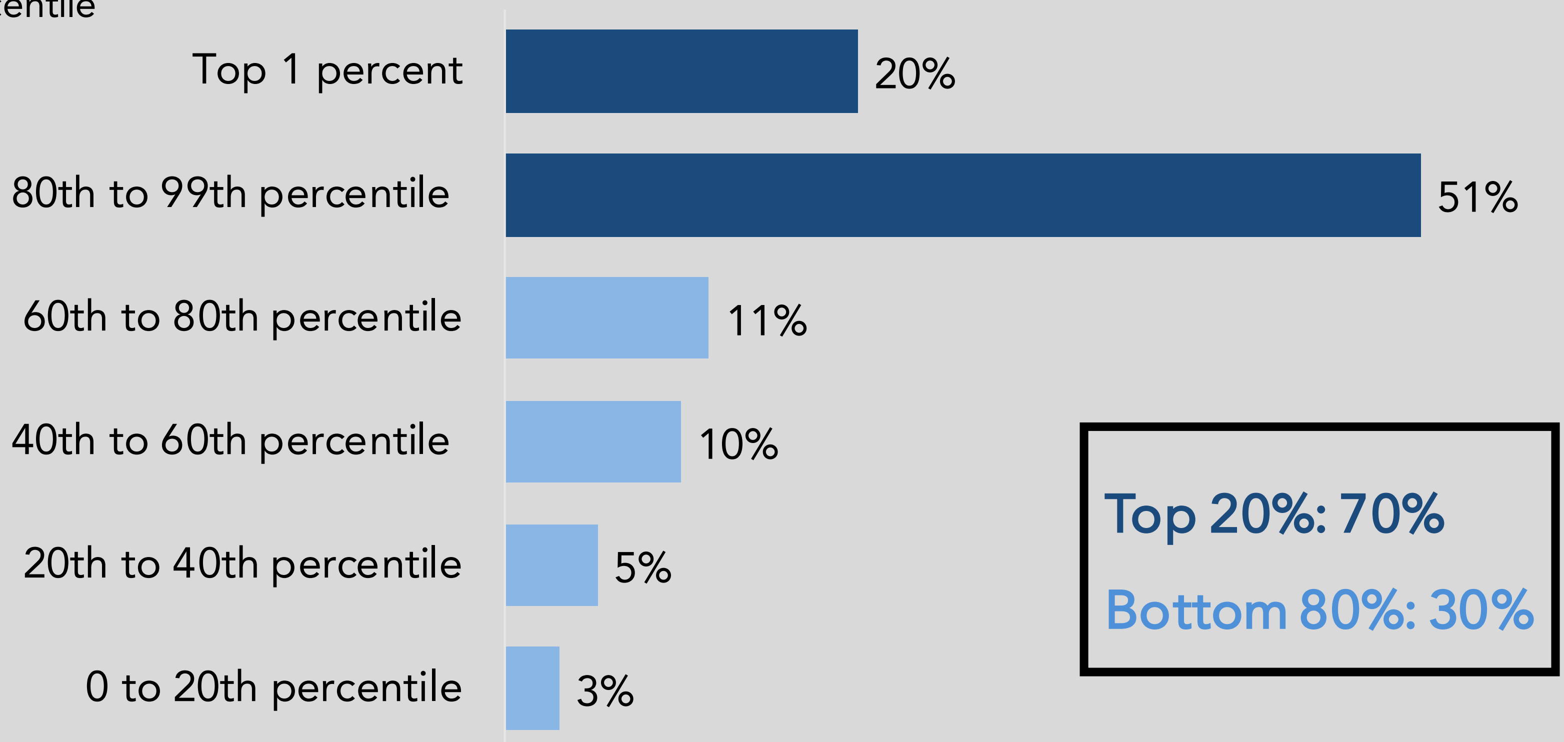
Source: (1) Federal Reserve. Financial Accounts of the US, Household balance sheets. Data through Q1 2024. (2) Oxford Economics. Data as of Q1 2024.

Wealth Gains Disproportionately Accumulated to Top 20%

Over 70% of total wealth gains since Q4 2019 accumulated to those in the top 20% income bracket, who spend more heavily on services. While "excess savings" during the crisis period were robust, they were not evenly distributed and have largely been spent.

US household wealth gains since Q4 2019

Share of cumulative household net worth change during the pandemic by percentile

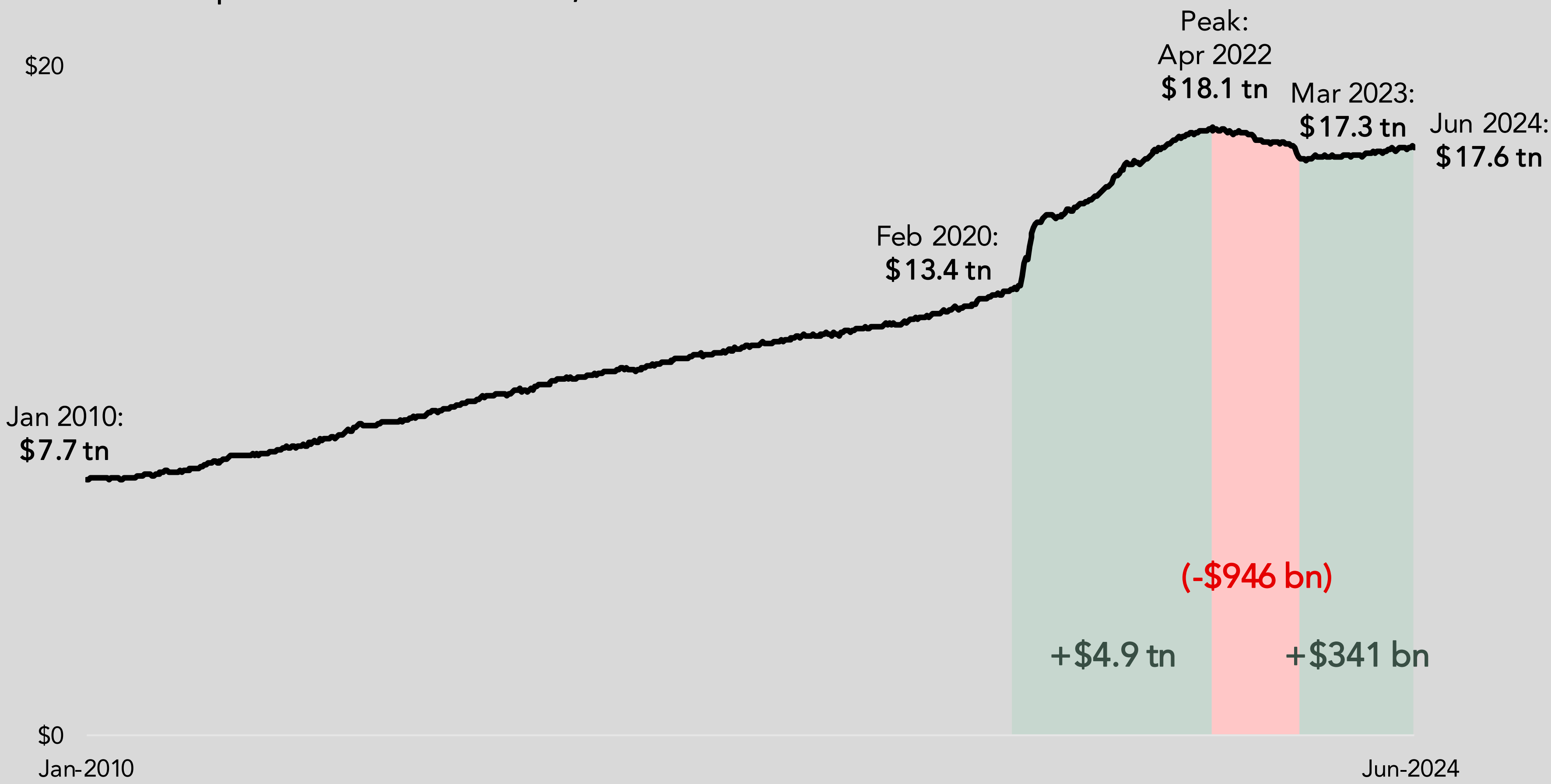


Source: (1) Oxford Economics, "US Excess Savings Offer Cushion to Only Some Households". Data through Q1 2024.

US Consumer Deposits Still Elevated

After a sharp decline during the US regional bank crisis of early 2023, US consumer deposits into commercial banks have increased once again. Deposits are more than $340 bn higher today vs. just over a year ago.

US consumer deposits into commercial banks, USD tn

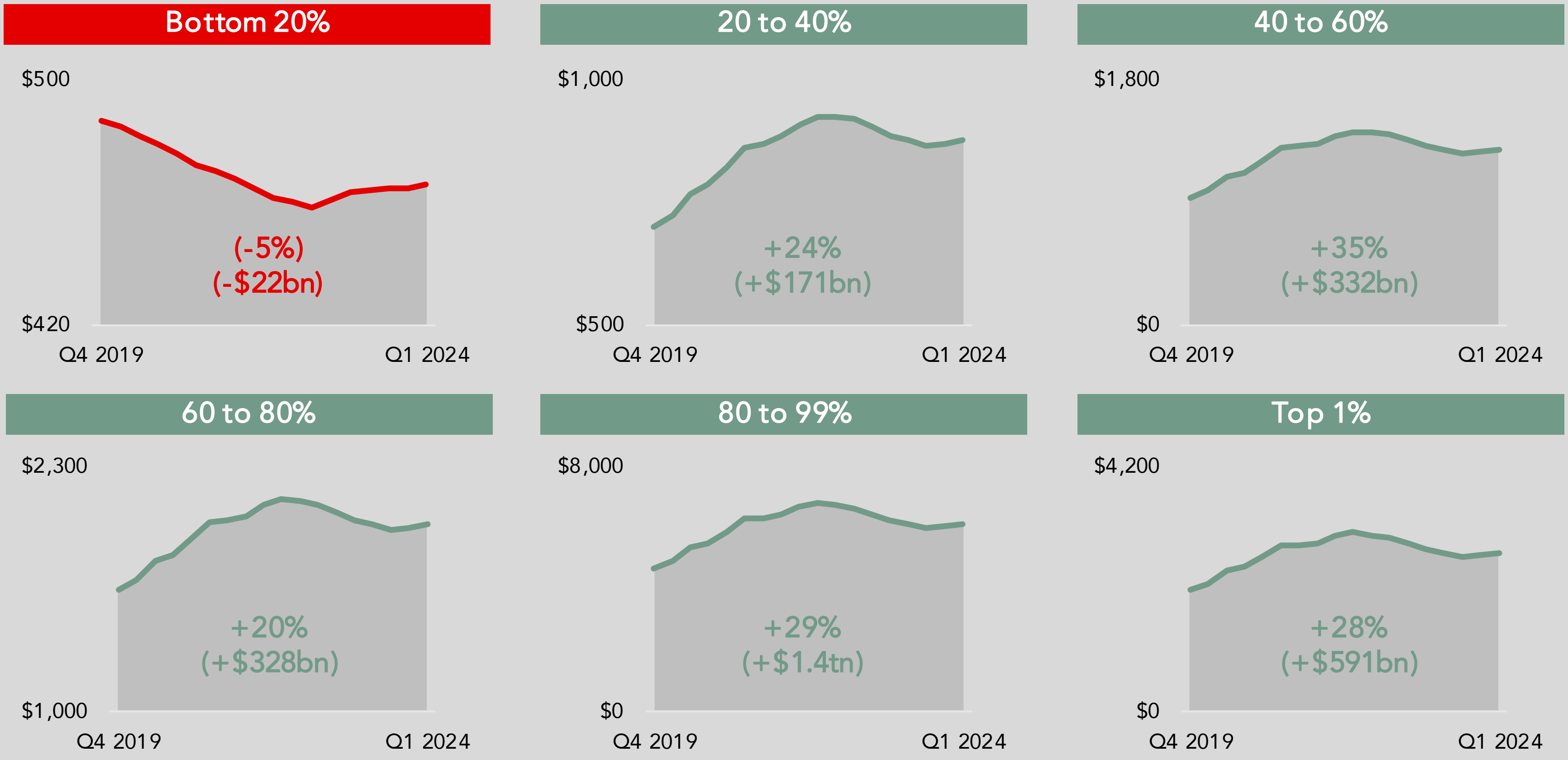


Source: (1) FRED. Deposits for all commercial banks, weekly Wednesday level. Data as of July 12, 2024.

Strength of US Consumer Varies by Income Bracket

US bank deposits have risen since the COVID crisis across every income bracket except the lowest 20%. Against a backdrop of high inflation, the lowest income group has experienced liquid dis-savings while higher income groups grew deposits by 20 – 30% on average.

Bank deposits, by income bracket, USD bn

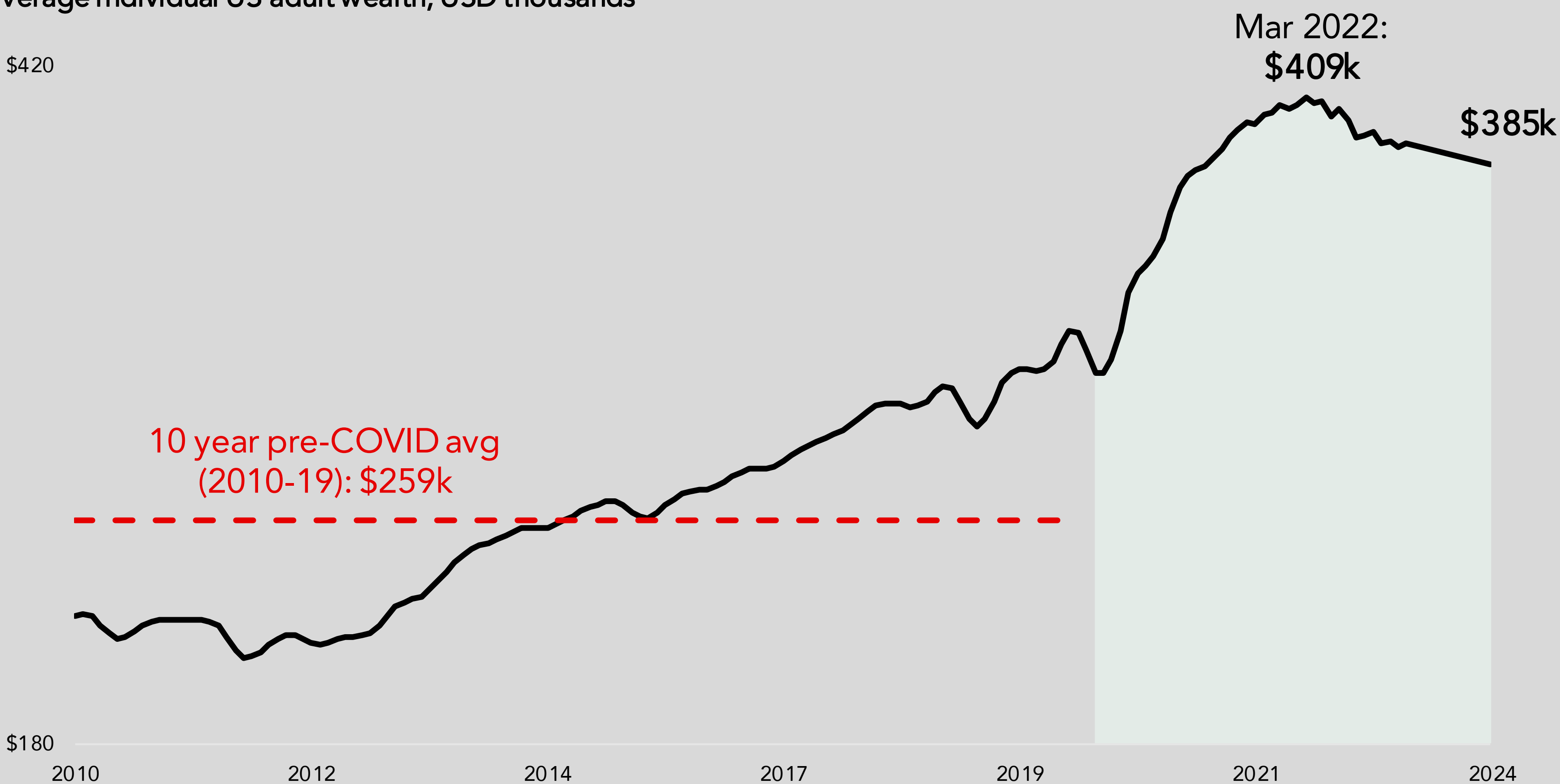


Source: (1-6) Federal Reserve. Distributional Financial Accounts. Data as of July 12, 2024.

US Middle Class Wealth Still Elevated

Middle class Americans (those in the 50th to 90th wealth percentile) are the primary engine of the US economy and account for roughly half of US consumer expenditure. Although average wealth for middle class Americans peaked in March 2022, it remains well above the pre-COVID average.

Average individual US adult wealth, USD thousands

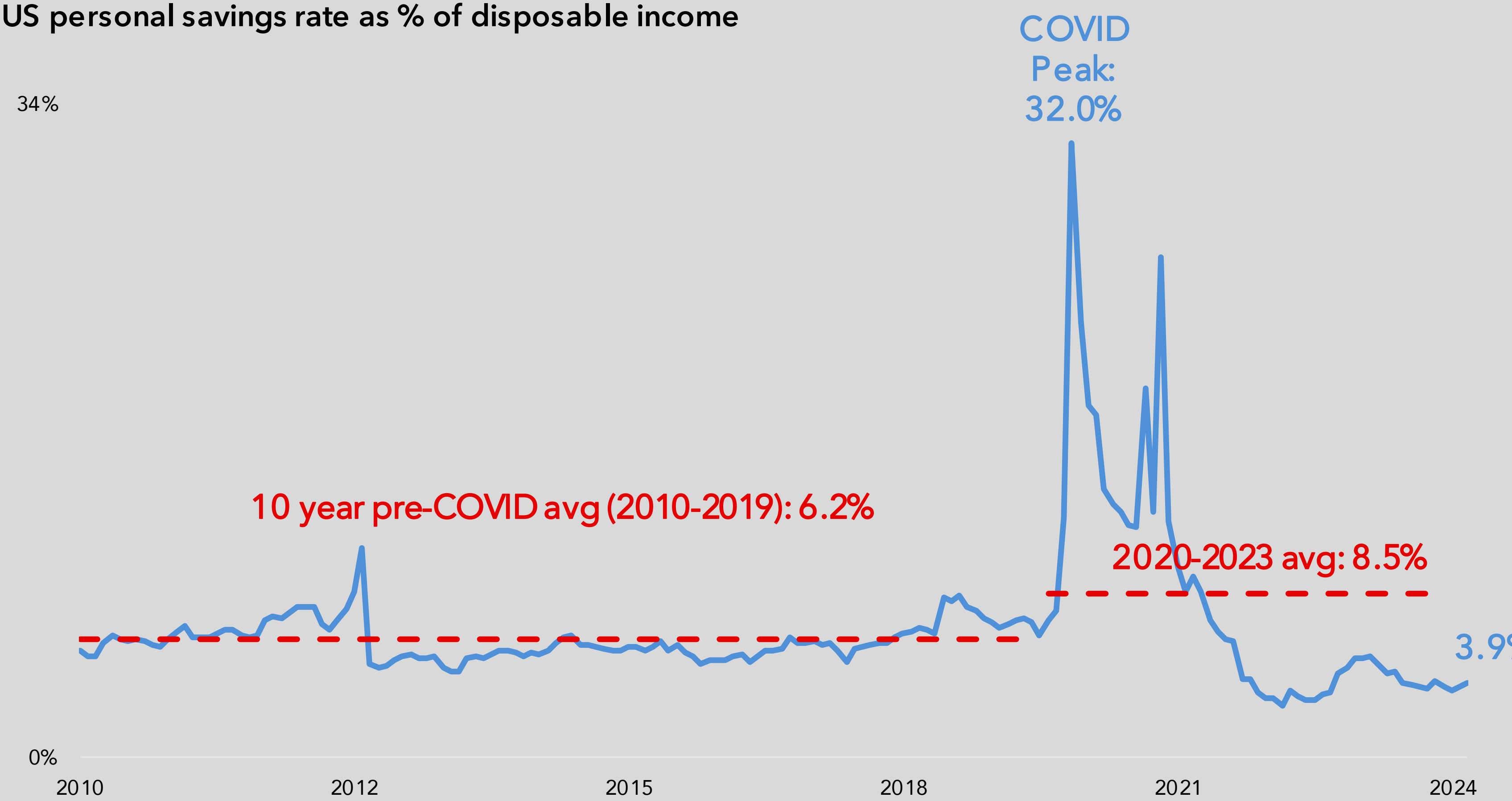


Source: (1) Real Inequality. University of California Berkeley. Average real income in March 2023 dollars for adults aged 20+. 2024 data is estimate as of July 17, 2024.

Savings Rate Below Pre-COVID Levels

The personal savings rate has declined to a 16 month low and stands well below its pre-COVID decade average. Against a backdrop of prolonged elevated inflation, households have dipped into savings and relied more heavily on credit cards to finance spending.

US personal savings rate as % of disposable income

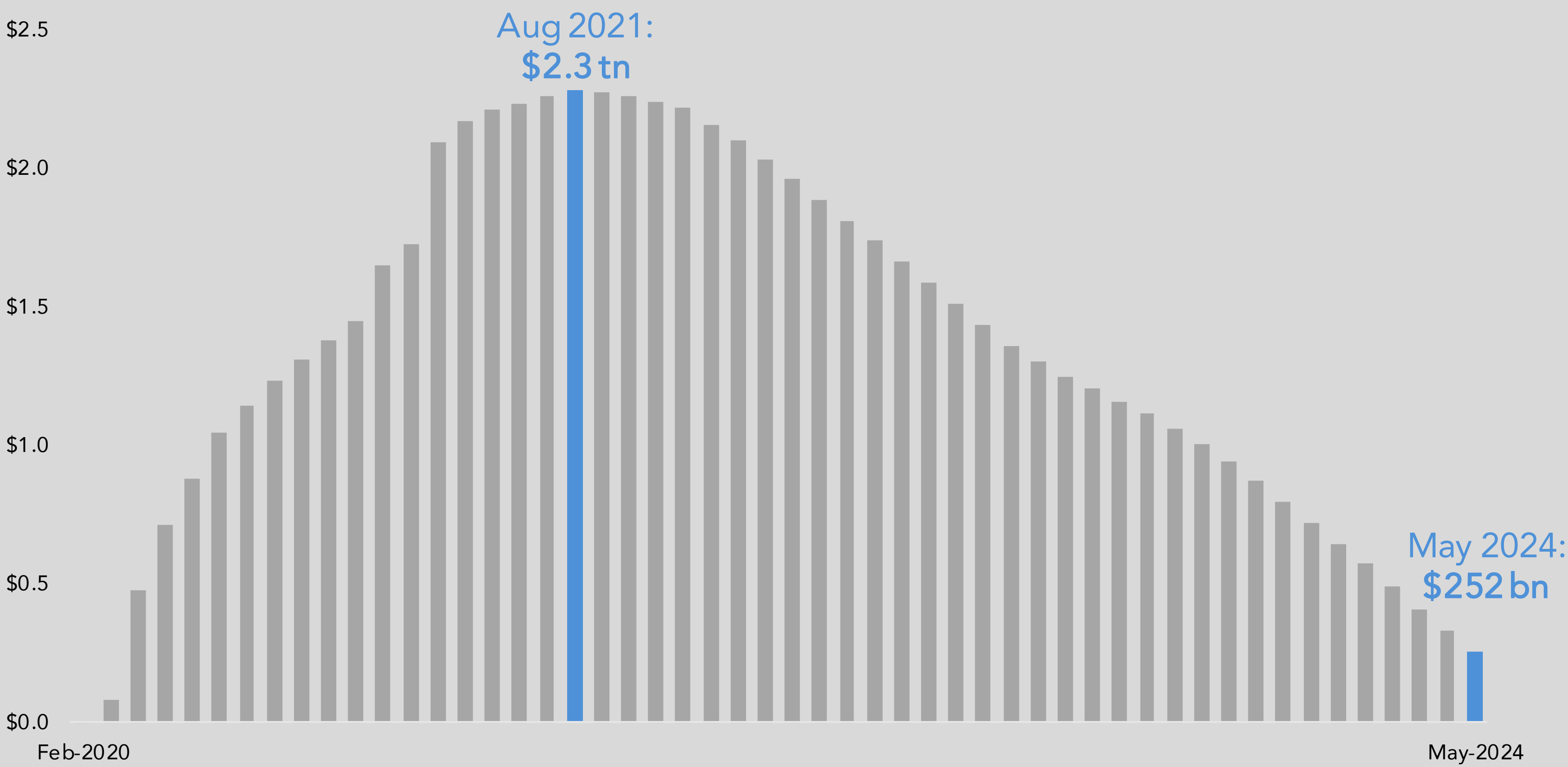


Source: (1) Bloomberg. Data as of July 17, 2024.

“Excess Savings” Depleted

COVID-era “excess savings” peaked over $2 trillion in 2021 and have steadily declined ever since. Though difficult to measure, roughly $250 bn of excess savings remains today on US consumer balance sheets. Over half of this remaining savings is held by the top quartile of US households.

US households’ excess savings, USD tn

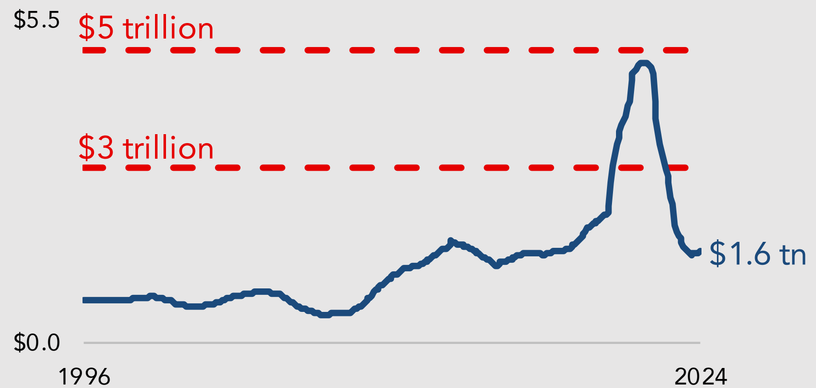


Source: (1) Oxford Economics (Vanden Houten). Excess savings based on Fed approach and Oxford Economics calculations.

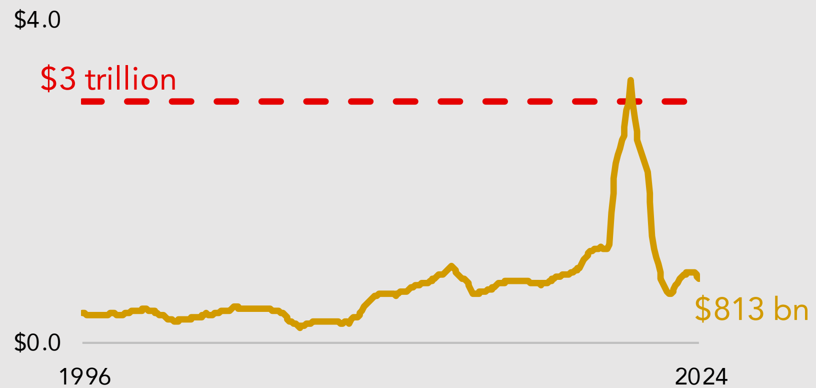
Excess US Savings Largely Spent

COVID-era excess savings have either been spent or "converted" to wealth by the highest income consumers. US consumers in the lowest income bracket have turned to credit cards to fill the gap between lower savings rates and higher prices.

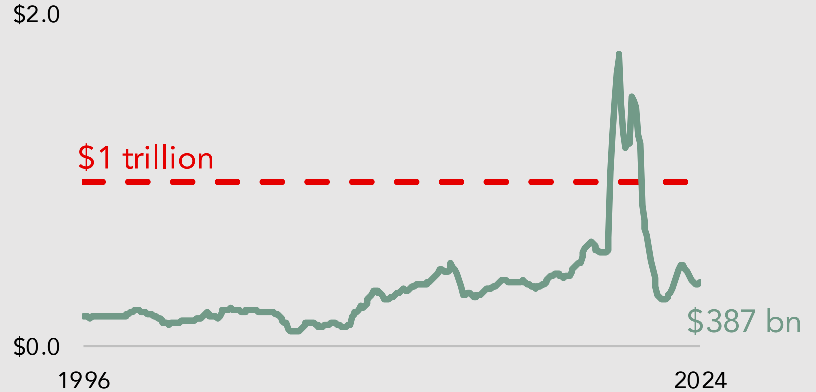
US cumulative savings, trailing 24 months, USD tn



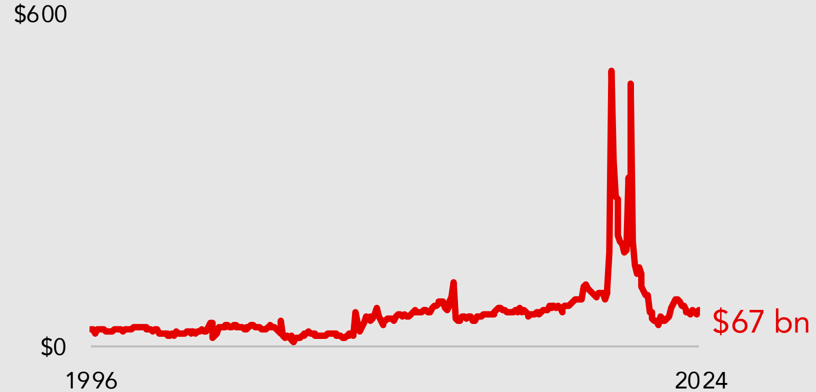
US cumulative savings, trailing 12 months, USD tn



US cumulative savings, trailing 6 months, USD tn



US cumulative savings, monthly, USD bn

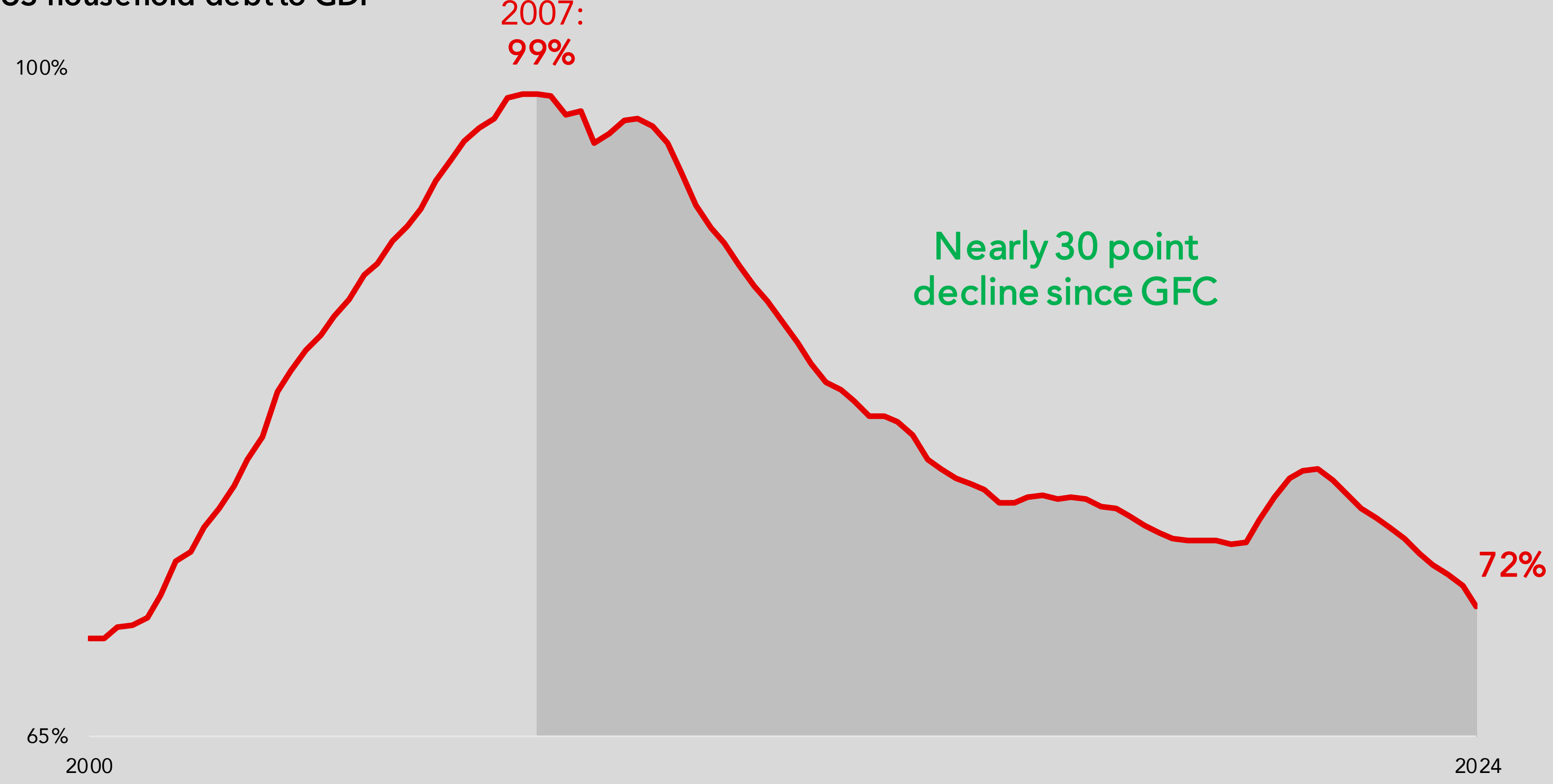


Source: (1-4) CreditSights, "U.S. Consumer Credit and Banks: Narrative Pushback" (July 7, 2022). Bloomberg. Data through May 31, 2024.

Consumer Debt / GDP Well Below GFC Levels

More so than most G20 economies globally, the US consumer has significantly de-levered since the GFC. Today, US consumer debt to GDP stands at 72%, a nearly 30-point decline since the 2007 peak of 99%. While mortgage debt remains the largest sub-category of US debt, auto and student loans have been the fastest growing sub-categories over the last 15 years.

US household debt to GDP

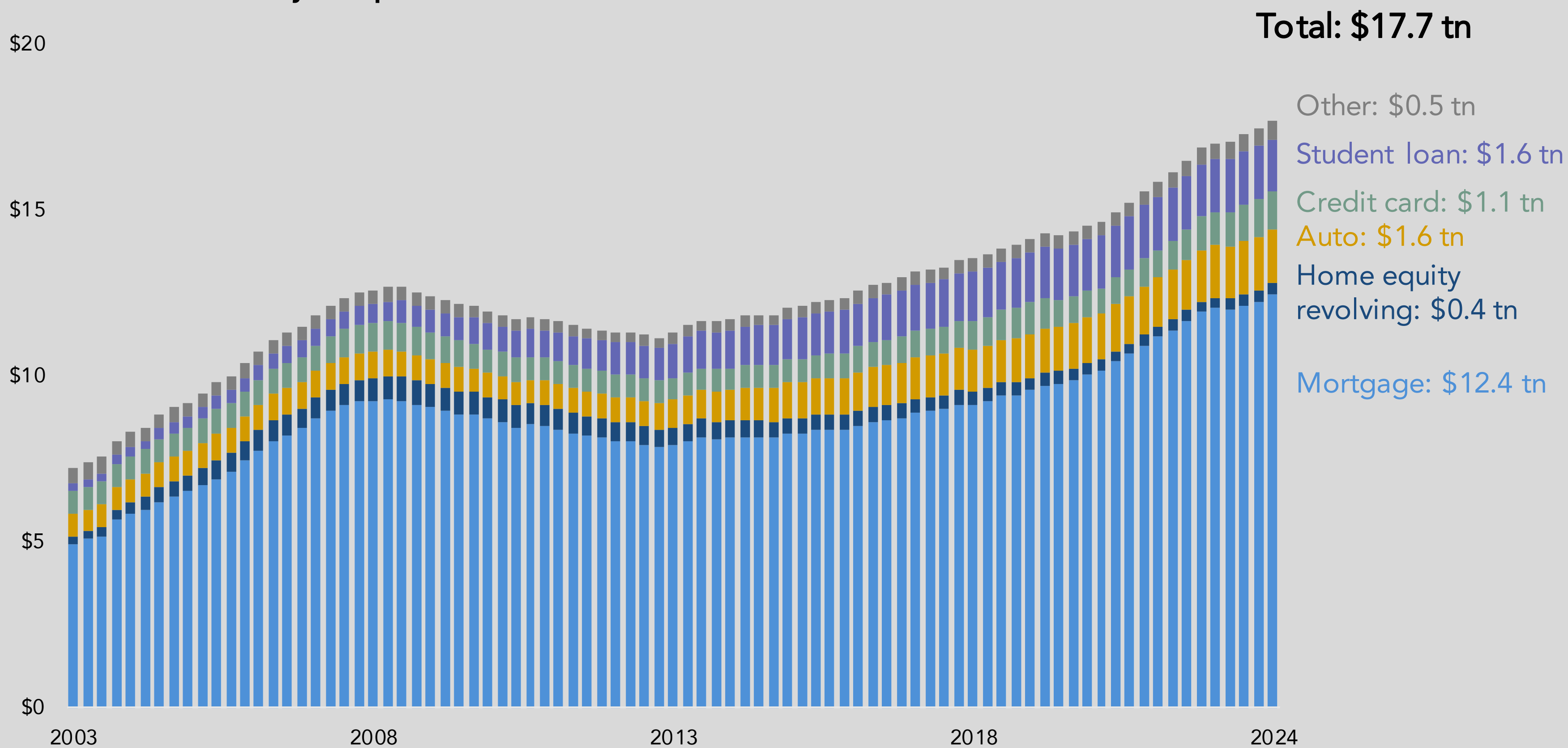


Source: (1) IIF. Data through Q1 2024.

Consumer Debt Largely Fixed Rate

Mortgages represent 70% of the nearly $18 tn of US household debt. Of the $12 tn of outstanding US mortgages, nearly 95% are fixed rate, while nearly 40% were originated or refinanced during the record low 2020-2021 period. While the total amount of household debt has increased since the financial crisis, the percentage of GDP has declined and the composition is more heavily skewed to fixed vs. floating rate.

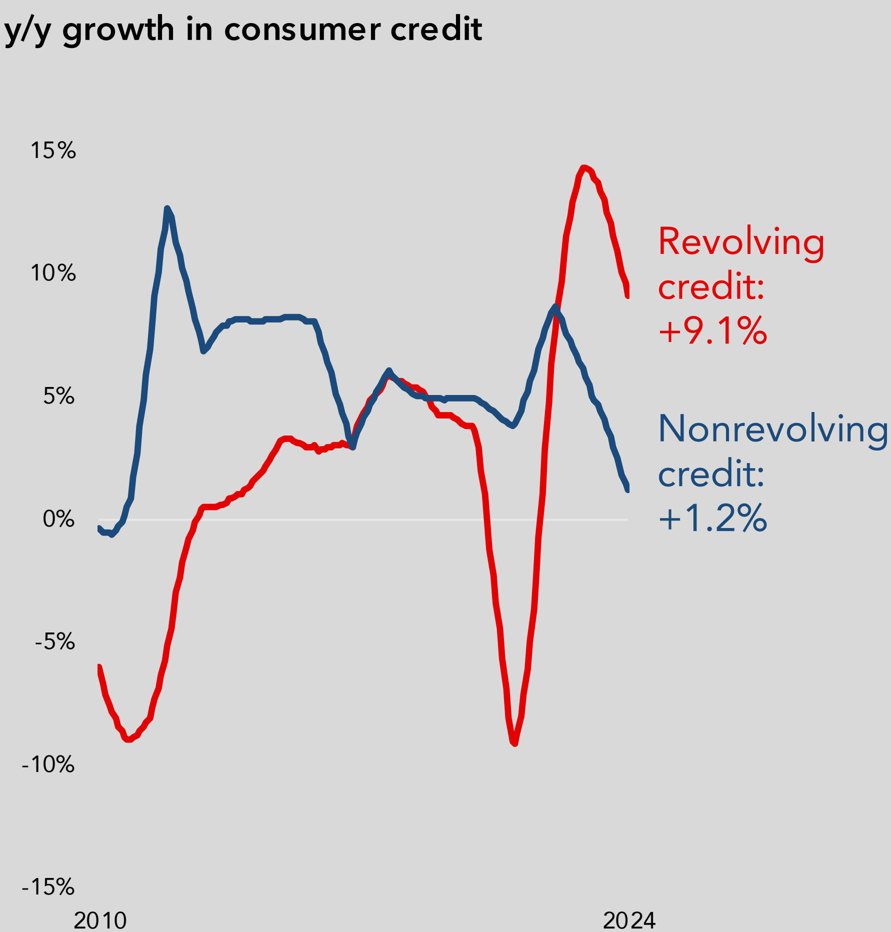
Total debt balance by composition, USD tn

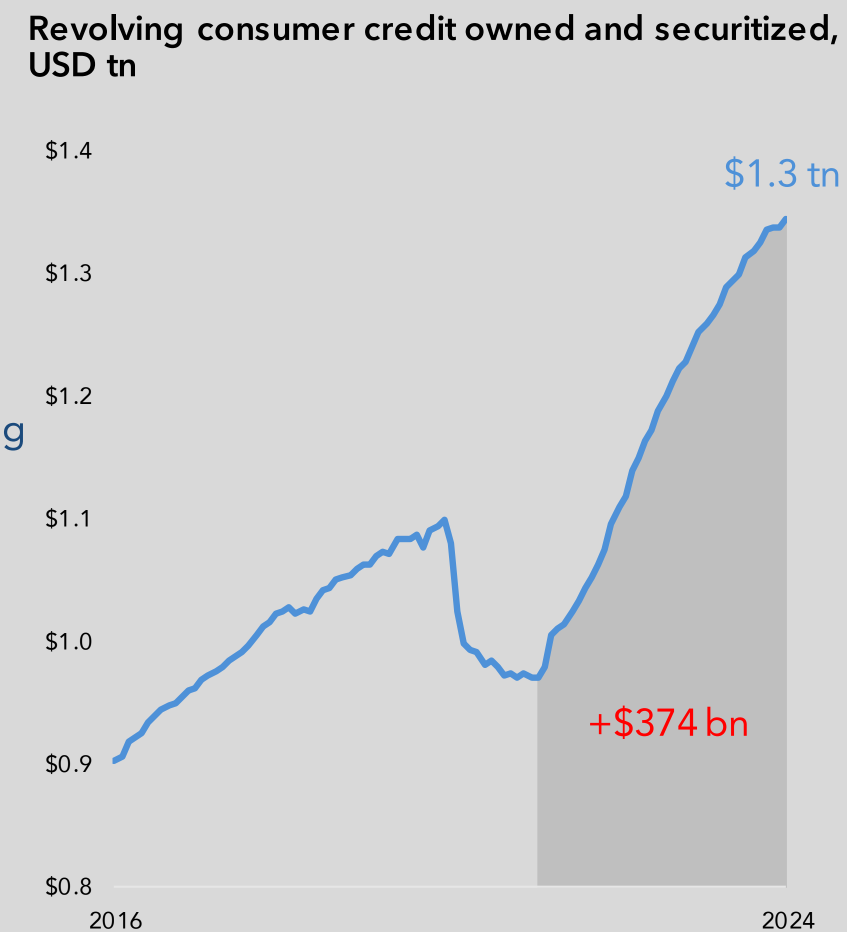


Source: (1) Federal Reserve Bank of NY. Household Debt and Credit Report (Q1 2024). Data as of July 17, 2024.

US Consumer Credit Balances Rising

Revolving consumer credit has increased by over $370 bn to $1.3 trillion from the post-COVID low of $970 bn in 2021.



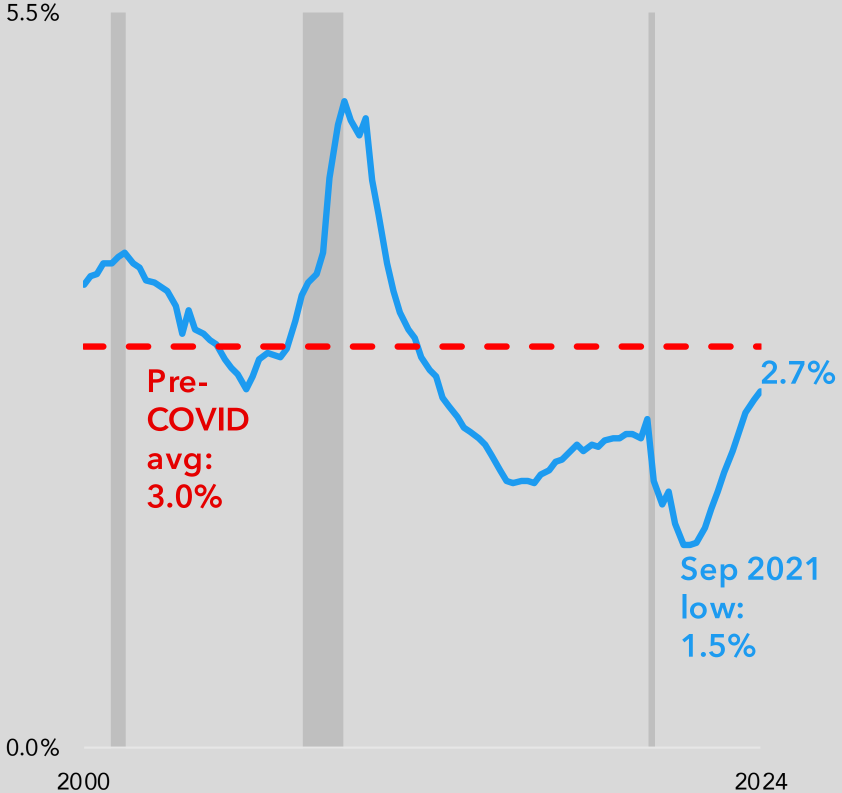


Source: (1-2) Bloomberg. Data as of July 15, 2024. Growth in consumer credit is rolling 12 month average.

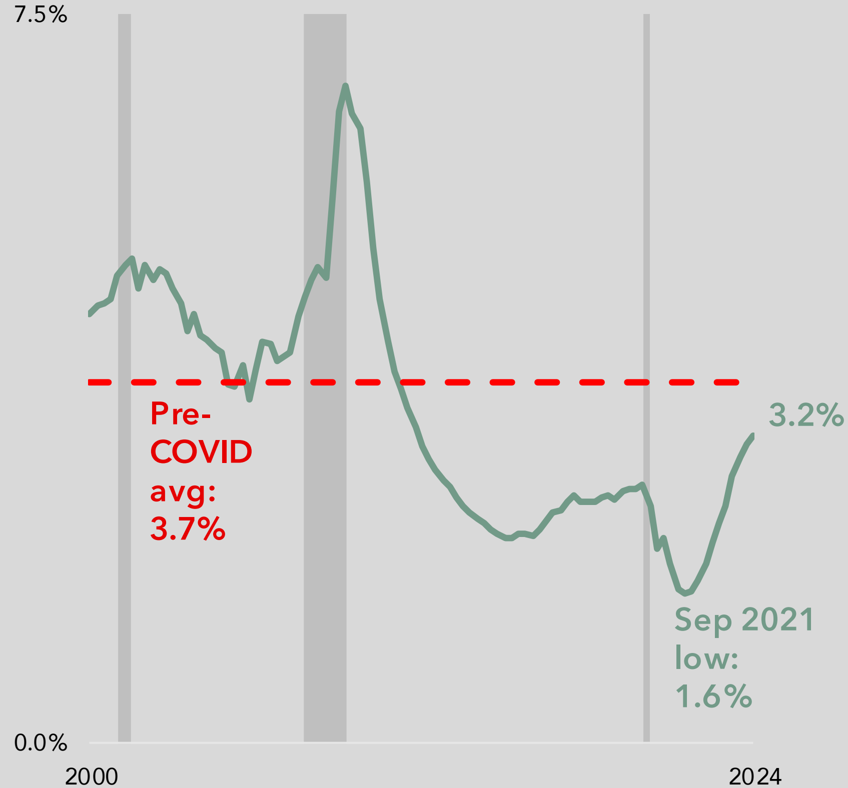
Delinquencies Low But Rising Rapidly

Overall consumer debt remains relatively low and delinquencies are still below 2019 levels, in large part due to the high proportion of fixed rate mortgage debt and pandemic-era student loan relief programs. Growth in credit card debt, however, is outpacing overall consumer spending and delinquency rates are rising rapidly. Credit card delinquencies are particularly high for younger consumers.

US all consumer loan delinquency rates



US credit card delinquency rates

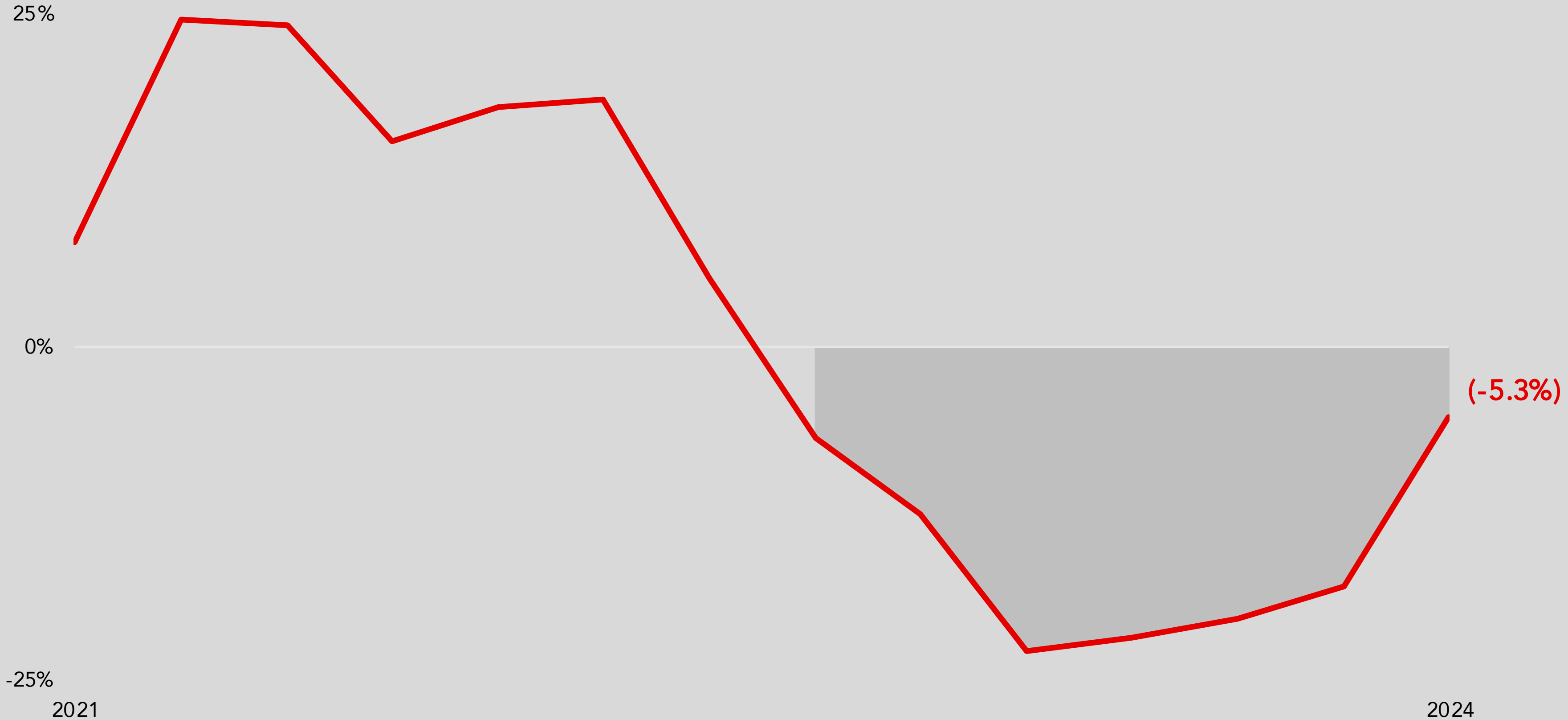


Source: (1-2) Bloomberg. Data as of July 15, 2024. Federal Reserve.

Tighter Access to Credit

The rate of consumer credit growth has declined as consumer access to credit is in restrictive territory. Overall, consumer balance sheets are resilient, though tighter credit availability likely signals a deceleration in future consumer spending.

Net % of banks willingness to make consumer loans



Source: (1) Bloomberg. Data as of July 17, 2024.. Bank willingness to make consumer loans is Net % of domestic responses reporting increased willingness to make consumer install loans.

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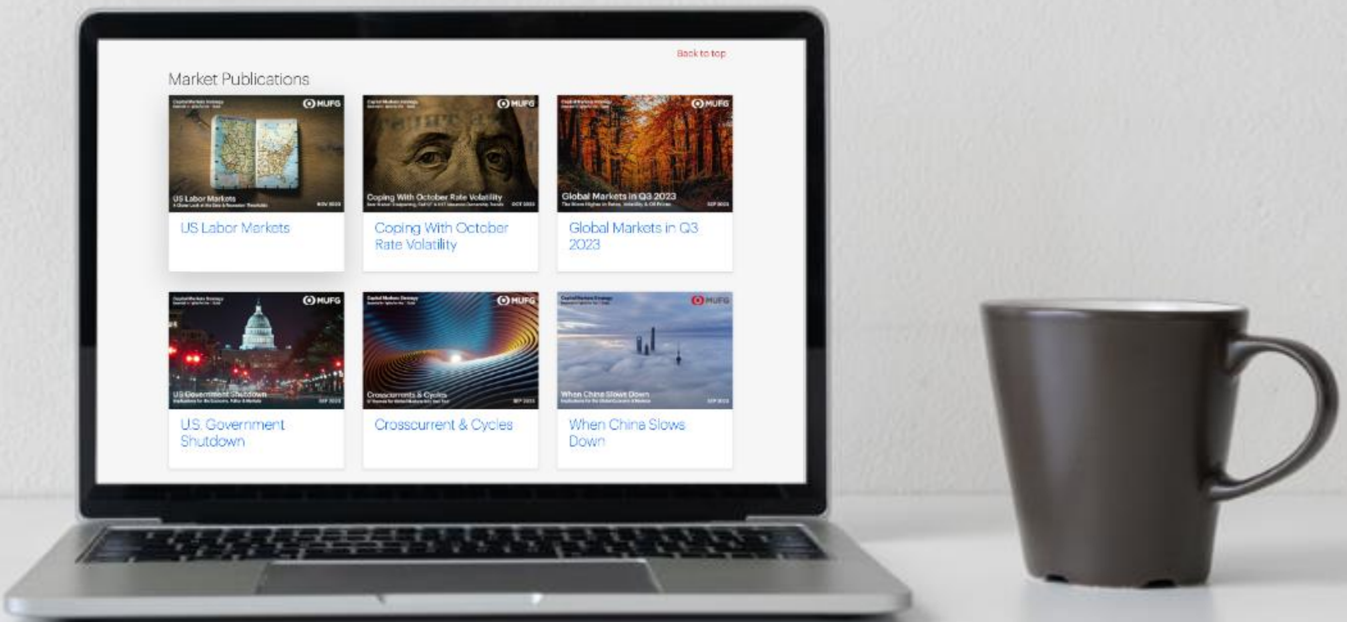

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Tom Joyce is a Managing Director and Capital Markets Strategist within MUFG's global capital markets and investment banking business. Based in New York, Tom heads a team that creates customized analytical content for multi-national S&P 500 companies. His team provides in depth analysis on the impact of economic, political, public policy and regulatory dynamics on the US credit, foreign exchange, rates and commodities markets.

Experience

Tom has nearly 30 years of Investment Banking experience in New York, London, Hong Kong, and San Francisco. Over the last 15 years, Tom created and built the Capital Markets Strategy role, advising corporate C-Suite executives (Boards, CEOs, CFOs, and Treasurers) on the pervasive macro forces driving markets. Tom also presents at dozens of corporate events each year including Board meetings, CEO ExCo sessions, CFO and Treasury off-sites, corporate leadership events and conferences.

Education

Tom's educational background includes a year of study at Oxford University from 1991 - 1992, a Bachelor of Arts in Political Science from Holy Cross College in 1993, and a MBA from Kellogg Business School, Northwestern University in 2000.

Personal

Tom resides in New Canaan, CT with his wife and four sons, where he serves on the Board of Trustees of the New Canaan Library as well as the Holy Cross College President's Council.

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Role

Hailey Orr is a Managing Director in MUFG's Capital Markets Strategy group within the global capital markets and investment banking business. The team provides market based content for corporate clients to assist in strategic decision making. Focus areas include the impact of economic, political, public policy and regulatory dynamics on the US credit, foreign exchange, rates and commodities markets.

Experience

Hailey has over a decade of Wall Street experience, including three years as a Consumer Sector Specialist in Equity Sales and ten years as a Capital Markets Strategist. Hailey is also the co-chair of MUFG's Women's Initiative Network (WIN) has devoted years to participating in and developing Wall Street recruiting programs.

Education

Hailey graduated with honors from the University of Michigan's Ross School of Business with a BBA and a minor in International Studies.

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In March 2020, Crain's New York Business Magazine named Hailey one of the "Rising Stars in Banking and Finance".

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Experience

Stephanie has spent nearly seven years as a Capital Markets Strategist. She is an active member of the University of Michigan recruiting team and is focused on the diversity recruiting effort at MUFG. Stephanie is also a part of MUFG's DEI, Culture & Philanthropy (DCP) Council.

Education

Stephanie graduated with honors from the University of Michigan's Ross School of Business with a BBA .

Personal

Stephanie is actively involved in NYC's iMentor program, mentoring high school students with their journey to college graduation. She also volunteers at Experience Camps, a free summer camp program for grieving children.

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Experience

Angela previously interned at MUFG working in Capital Markets within the Equity Capital Markets and Leveraged Finance divisions. She is also an active member of the Carnegie Mellon University recruiting team.

Education

Angela graduated with honors from Carnegie Mellon University's Tepper School of Business with a BS in Business Administration with an additional major in Statistics and a minor in Media Design. She was a member of Alpha Kappa Psi business fraternity and the Undergraduate Entrepreneurship Association.

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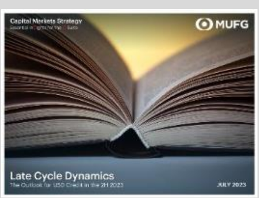

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