3Q24 Economic Summary

Volatility reigned during the third quarter as investors were faced with mixed economic data, increased geopolitical unrest, U.S. election uncertainty, and a "recalibration" of Fed policy. Equity markets sold off sharply after a weaker-than-expected July jobs report, but quickly reversed course and ended the quarter near all-time highs as investors gained confidence that the Fed was committed to supporting growth through policy action. Bond markets also delivered positive returns during the quarter as yields fell across the curve. After being inverted since mid-2022, 2-year yields fell below 10-year yields in September, resulting in a positive sloping yield curve and reflecting market expectations for future rate cuts.

Despite a soft start, the U.S. economy expanded at a robust pace during the third quarter, producing 3Q24 GDP growth of 2.8%. Concerns about the demise of the U.S. consumer continued to be overstated as personal consumption came in strong. Retail sales were up as consumers made back-to-school purchases and got a jump on holiday shopping. In addition, spending on services rebounded as upper-income Americans continued to frequent bars and restaurants and pay for experiences like concerts and travel. Although election uncertainty made some firms hesitant to spend, business investment increased during the quarter. Purchases of machinery were up and investment in computers and software jumped, highlighting the boom in artificial intelligence. Government spending was another contributor to growth as outlays on defense surged. Detractors to GDP included declines in net exports and inventories. Residential investment also contracted during the quarter as home buyers remained sidelined by high mortgage rates and prices.

Labor market data was mixed during the quarter. After softer-than-expected job growth in July and August raised recessionary fears, September hiring rebounded, posting the largest monthly increase since March. Service jobs remained the primary driver of growth as increased hiring in leisure and hospitality, healthcare and government helped to offset declines in manufacturing jobs. After a surprise jump to 4.3% in July, the unemployment rate came down in September, ending the quarter at 4.1%. Although job openings and quit rates declined, demand for workers was healthy and layoffs remained low. Average hourly earnings also increased during the quarter, which boosted consumer confidence and bolstered consumption.

The quarter's solid GDP growth was accompanied by an ease in price pressures. Core PCE, the Fed's favored inflation gauge, declined to 2.2% quarter-over-quarter from 2.8% in 2Q24. Declining goods prices remained the primary driver of the moderation in inflation, but a slowing in the pace of price increases was also evident across a broad range of services, including shelter costs. While the overall trend was positive, inflation did start to tick back up at the end of the quarter as increased consumption resulted in higher prices for groceries, goods and services in September.

Softer labor market data and moderating price pressures during the first two months of the quarter prompted the Fed to begin easing monetary policy at the September FOMC meeting. The Fed opted to go big with its first rate cut since 2020, slashing the fed funds rate 50 basis points to a target range of 4.75%-5.00%. The Committee cited weakening labor market trends and confidence that inflation was on a sustainable path to 2% as reasons for the larger than typical move. The July jump in the unemployment rate sounded alarm bells at the Fed with officials concerned that the labor market may be cooling more rapidly than desired. Participants saw the balance of risks shifting, noting that the downside risks to employment had increased while the upside risks to inflation had diminished. As a result, a recalibration to a more neutral stance of monetary policy was warranted. In his post-meeting press conference Chair Powell emphasized that the move was not an indication of an impending economic downturn but rather a sign of the Fed's commitment to not get behind the curve in supporting a strong labor market. He warned investors not to assume that this was the new pace for rate cuts going forward, stating that policymakers will go carefully, accessing the degree of restrictiveness meeting by meeting. The 50 basis point move was not a unanimous decision. Fed Governor Bowman voted against the action, preferring to cut 25 basis points instead. She voiced concerns that the larger cut could hinder the Fed's progress on inflation by unnecessarily stoking demand.

In conjunction with the ease, the Fed moved its September dot plot projection for the fed funds rate lower, reflecting a faster pace of rate cuts than previously expected. The Fed is now forecasting an additional 50 basis points of cuts in 2024 followed by 100 basis points of cuts in 2025. Markets rallied on the news, believing that the aggressive start to the easing cycle increased the likelihood that the Fed can deliver a soft landing. However, the path forward for the Fed will not be easy. Reducing policy restraint too late or too little could risk weakening economic activity and employment, but easing too soon or too fast could stall or reverse the progress made on inflation. It is a delicate balance and one the Fed must maintain in order to achieve its dual mandate of price stability and maximum employment.

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