

# U.S. Economic Outlook

August 12, 2021

## Sitting on the dock of the bay...<sup>1</sup>

Since last month's update, we learned that the economy expanded 6.5 percent (annualized) in the second quarter.<sup>2</sup> Initial data on Q3 has also been promising to-date, with 943,000 jobs added in July and average hourly earnings rising 4 percent year-over-year (YoY).<sup>3</sup> The July Visa Spending Momentum Index (SMI) provided our first look at consumer spending for the quarter, which also pointed towards continued robust consumer spending activity.<sup>4</sup> There are some challenges, however, that may begin to limit consumer spending in the coming months. Namely, the ongoing global supply chain disruptions. Auto sales slid for three months in a row now,<sup>2</sup> not for lack of demand, but rather a global auto chip shortage that is preventing some car makers from keeping vehicles in stock. The surge in U.S. domestic demand has also created challenges for key U.S. ports trying to keep up with demand. Several U.S. ports remain backlogged and are struggling to get the plethora of container ships unloaded ('sitting on the dock of the bay'...). These are just two examples of the challenges associated with trying to service the robust rebound in U.S. consumer spending. Retail inventories as of May were down to less than 1.1 months of supply left.<sup>5</sup> There are some signs that things are easing but it will likely take a couple of quarters for global supply chains to catch-up. We estimate that real GDP growth will expand 5.4 percent (annualized) in Q3, with a whopping 2.7 percentage points coming from inventory rebuilding.

GDP growth in this month's outlook is expected to rise 5.9 percent YoY this year before downshifting to 3.5 percent in 2022.

### Highlights

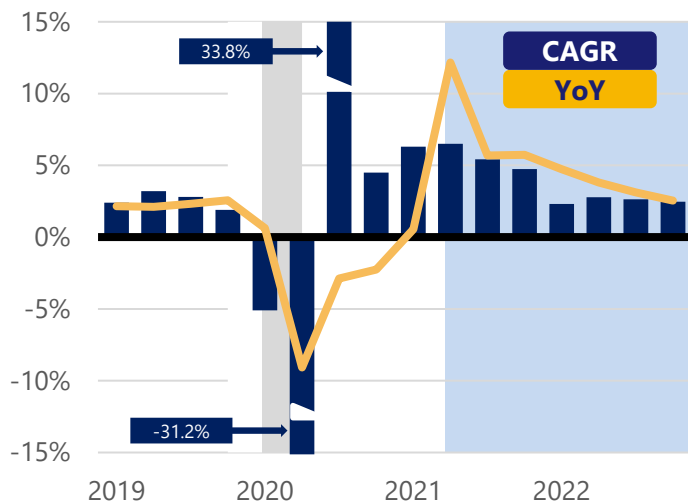
**Spending activity off to a strong start**

**Supply chain issues continue**

**Watch out for the fiscal cliff this fall**

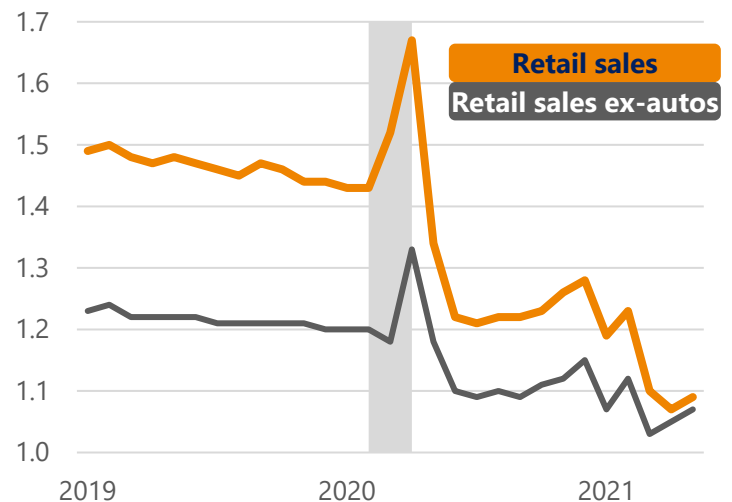
### Real gross domestic product (GDP) (SA, CAGR and YoY\* percent change)

Last forecast: August 12, 2021



### Inventory-to-retail sales ratio shows tight supply (SA, months supply)

Last actual: May 2021



\*Seasonally adjusted (SA), compound annualized growth rate (CAGR), year-over-year (YoY). Sources: Visa Business and Economic Insights, U.S. Department of Commerce.

## Sitting on the dock of the bay... (cont.)

### No signs of Delta impacting confidence

Another emerging concern is the surge in the Delta variant. So far, there has not been much impact on consumer confidence. Conference Board's July consumer confidence reading increased, with consumers more optimistic about both current and future economic conditions.<sup>6</sup> The elevated confidence readings for July are consistent with the Visa SMI, which rose 0.7 points month-over-month. We will be watching the August reading of both measures closely as some metro areas have opted for mask mandates and other restrictions to contain the spread of the virus.

As we look ahead to the second half of this year, we expect to see a larger divergence between real (inflation-adjusted) and nominal consumer spending. Real spending is expected to rise 8.1 percent (YoY) in Q3 while nominal spending will likely be closer to 12.6 percent. The gap is explained by the higher inflation readings expected over the quarter, in part, due to the ongoing supply chain issues. While the robust pace of earnings is welcome news, the inflation factor is becoming a concern. June marked the third month in a row with a decline in real average hourly earnings, which suggests that the higher prices are eroding the purchasing power of consumers.<sup>3</sup> The residual effects of the stimulus programs are likely leading consumers to look past the higher prices for now.

### Inflation: transitory or just plain expensive?

Economists are debating whether the elevated inflation readings are "transitory" or if the price pressures will be short-lived and thus less of a concern to the Fed trying to decide when to hike interest rates. Meanwhile, consumers are seeing higher prices in several areas, including at the pump and grocery store. The headline Consumer Price Index (CPI) was up 5.4 percent in June.<sup>3</sup> Among the categories leading the way were used car prices, up 45.2 percent YoY, and airfares, up 24.6 percent.<sup>3</sup> The auto price pressures should begin to ease once supply chains catch-up and airfares should stabilize once the airlines are able to bring more capacity back online, but both will take time. We see the CPI remaining elevated through Q1 of next year before YoY price growth begins to moderate in the latter half of 2022.

### Risks to the outlook

Among the risks creeping into the economic outlook this month is the approaching fiscal cliff this fall. Congress will need to enact a funding bill to avoid a government shutdown and lift the nation's borrowing limit to prevent a default on the debt. In addition, housing affordability is an ongoing concern as home prices continue to surge higher in many areas. On the upside, the Biden Administration extended deferred student loan payments until January 31, which could lift Q4-2021 consumer spending.

	Actual				Forecast				Actual		Forecast	
	2020				2021				2019	2020	2021	2022
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Gross Domestic Product (CAGR)	-5.1	-31.2	33.8	4.5	6.3	6.5	5.4	4.7	2.3	-3.4	5.9	3.5
Personal Consumption	-6.9	-33.4	41.4	3.4	11.4	11.8	5.8	3.3	2.2	-3.8	8.4	3.6
Business Fixed Investment	-8.1	-30.3	18.7	12.5	12.9	8.0	8.8	5.8	4.3	-5.3	8.3	5.5
Equipment	-21.3	-36.2	55.9	26.4	14.1	13.0	4.0	3.5	3.3	-8.3	14.2	4.6
Intellectual Property Products	3.8	-10.6	8.1	10.2	15.6	10.7	9.5	10.0	7.2	2.8	9.8	6.8
Structures	-0.9	-46.8	-15.3	-8.2	5.4	-7.0	0.6	1.9	2.0	-12.5	-7.6	2.6
Residential Construction	20.4	-30.7	59.9	34.4	13.3	-9.8	0.4	1.9	-0.9	6.8	10.8	1.2
Government Purchases	3.7	3.9	-2.1	-0.5	4.2	-1.5	2.2	3.1	2.2	2.5	1.1	1.8
Net Exports Contribution to Growth (%)	-0.1	1.5	-3.3	-1.7	-1.6	-0.4	-0.4	-0.4	-0.2	-0.3	-1.8	-0.5
Inventory Change Contribution to Growth (%)	-0.5	-4.0	6.8	1.1	-2.6	-1.1	2.7	1.3	0.1	-0.5	-0.1	0.6
Nominal Personal Consumption (YoY % Chg.)	2.0	-9.6	-1.6	-1.3	3.9	20.7	12.6	12.6	3.7	-2.6	12.2	6.3
Nominal Personal Income	3.3	10.9	7.1	4.8	16.1	1.0	3.6	5.2	4.1	6.5	6.3	-1.0
Retail Sales Ex-Autos	2.6	-7.6	3.3	2.8	11.6	27.9	15.0	15.5	3.4	0.3	17.2	3.4
Consumer Price Index	2.1	0.4	1.2	1.2	1.9	4.8	5.3	5.5	1.8	1.2	4.4	3.0
Federal Funds Rate (Upper Bound)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	2.19	0.25	0.25	0.25
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	5.28	3.54	3.25	3.25
10-Year Treasury Yield	0.70	0.66	0.69	0.93	1.74	1.45	1.27	1.31	2.14	0.89	1.44	1.51

Forecast as of: August 12, 2021

Interest rates presented are end of quarter rates

Note: Annual numbers represent year-over-year percent changes and annual averages

Sources: Visa Business and Economic Insights analysis of data from the U.S. Department of Commerce, U.S. Department of Labor and Federal Reserve.

## Notes

<sup>1</sup> Otis Redding

<sup>2</sup> Bureau of Economic Analysis, U.S. Department of Commerce

<sup>3</sup> Bureau of Labor Statistics, U.S. Department of Labor

<sup>4</sup> Visa Business and Economic Insights

<sup>5</sup> U.S. Census Bureau, U.S. Department of Commerce

<sup>6</sup> Conference Board.

## Forward Looking Statements

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