Visa Business and Economic Insights

U.S. Economic Outlook

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Softer Q3 economic data clouds the outlook

Last month, we downgraded our outlook for Q3 GDP growth as incoming economic data, combined with our timely indicator of consumer spending (the Spending Momentum Index), was pointing toward softness. Given the changes made a month ago, our outlook has only been modestly downgraded this month as incoming data has supported our case for 0.4 percent (annualized) growth for Q3. We attribute the downshift in consumer spending and, by extension, GDP growth to two key factors–a surge in the Delta variant and higher consumer prices eroding the purchasing power of consumers.

While it is still early, we see things improving a bit in Q4. For starters, new COVID case counts and hospitalizations have been falling since mid-September, which should help lift consumer spending on services. Inflation pressures, however, are likely to persist through the end of the year and will continue to keep a lid on overall consumer spending growth. Even with the more modest pace of growth through the end of this year, we still expect the Federal Reserve to begin tapering its purchases of assets next month. Beyond the Fed, we continue to be focused on developments on Capital Hill and the possibility of more gridlock around funding the government and lifting the nation's debt limit beyond the current deadline of December 3rd.

With our revisions to the outlook this month, we now see GDP growth expanding 5.3 percent this year, 3.2 percent next year and moderating closer to its long-run average at 2.6 percent in 2023.

Highlights

Growth hits an air pocket in Q3

Tapering is still on track for November

Watch for more D.C. drama next month

Fig. 1 Real gross domestic product (GDP) (SA, CAGR and YoY* percent change)

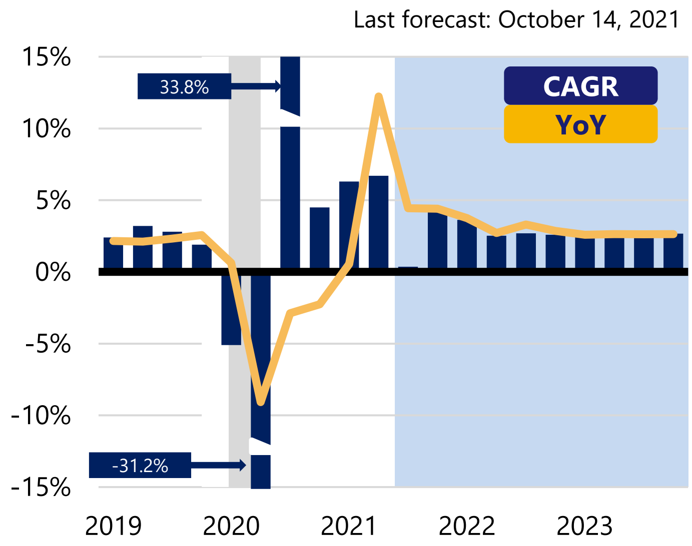
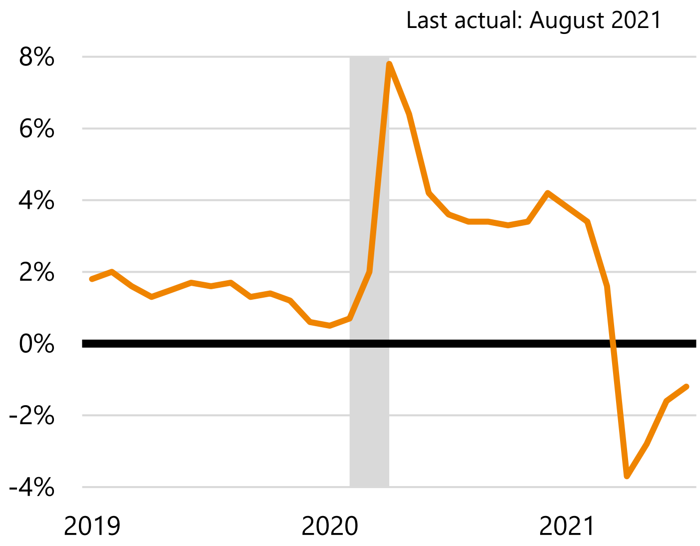


Fig. 2 Real (inflation-adjusted) average hourly earnings (SA, YoY percent change)



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

Softer Q3 economic data clouds the outlook (cont.)

'You're going to need a bigger boat'

Delta variant case counts peaked toward the middle of the month, which seem to have adversely affected consumer confidence and spending on services.[1] Beyond the COVID impact, global supply chain issues have resulted in goods shortages. Backlogs at West Coast ports due, in part, to labor shortages is forcing some retailers to secure their own ships in order to safeguard their supply chains ahead of the holiday shopping season. The disruptions are also leading to higher prices for consumers. While average hourly earnings have been robust, higher consumer prices have been eroding consumers' real purchasing power (right graph on pg. 1). Inflation-adjusted average hourly earnings contracted for the fifth month in a row in August, and early indications are the reading was negative again in September.[2]

Given these headwinds, we now see real consumer spending rising just 0.7 percent (annualized) in Q3 and then bouncing back to 3.8 percent in Q4. In nominal terms, the higher inflation readings will make spending look stronger. Nominal consumer spending is expected to expand 11.3 and 11.8 percent (YoY), respectively in Q3 and Q4 of this year. Next year, the economy is expected to return closer to its long-run average and thus nominal consumer spending is expected to rise 5.9 percent (YoY) after expanding 11.7 percent this year.

Interest rates rising

Even with September's softer than expected employment report, we expect the Federal Reserve to begin tapering its purchases of both Treasuries and mortgage-backed securities in November, which should continue through the middle of next year. Our view is that the November tapering has been priced into current Treasury yields (interest rates) and thus we expect only gradual upward pressure on long-term interest rates. We see the 10-year U.S. Treasury rate ending the year at 1.60 percent. Short-term Treasury markets have been rattled by the debt ceiling drama in D.C. over the past few weeks. While the four-week Treasury bill has come back down from a high of 0.10 percent after the debt ceiling deal was announced, the two-month T-bill has now climbed higher, pricing in the uncertainty over getting another deal by December 3rd when the current debt limit deal expires.

Risks to the outlook

The biggest risks to the outlook remain the ongoing supply chain issues. If confidence falls further or consumers are unable to spend due to out-of-stock items, the softness in real spending may persist into early next year. On the policy front, the showdown over funding the government and lifting the debt limit could lead to greater financial market volatility and, by extension, dent consumer confidence. On the upside, Congress could come to an agreement and thus end up boosting government investment next year.

	Actual		Forecast						Actual	Forecast		
	2021				2022				2020	2021	2022	2023
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
Gross Domestic Product (CAGR)	6.3	6.7	0.4	4.4	3.6	2.5	2.7	2.6	-3.4	5.3	3.2	2.6
Personal Consumption	11.4	12.0	0.7	3.8	2.3	2.5	2.4	2.4	-3.8	7.8	3.0	2.4
Business Fixed Investment	12.9	9.2	1.6	5.4	5.5	5.5	6.2	6.2	-5.3	7.5	5.3	6.1
Equipment	14.1	12.1	-11.0	3.5	4.1	4.3	4.7	4.6	-8.3	11.8	2.6	4.9
Intellectual Property Products	15.6	12.5	10.1	9.1	8.3	7.7	8.7	8.8	2.8	10.2	8.9	8.1
Structures	5.4	-3.0	0.7	1.5	2.3	3.0	3.7	4.0	-12.5	-6.9	2.0	4.1
Residential Construction	13.3	-11.7	-3.1	-3.7	1.3	2.0	2.3	2.4	6.8	9.5	-0.8	2.2
Government Purchases	4.2	-2.0	2.4	2.5	1.9	2.0	1.8	1.5	2.5	1.0	1.8	1.8
Net Exports Contribution to Growth (%)	-1.6	-0.2	-0.6	-0.4	-0.5	-0.6	-0.4	-0.4	-0.3	-1.7	-0.5	-0.4
Inventory Change Contribution to Growth (%)	-2.6	-1.3	2.4	1.0	1.3	0.1	0.1	0.0	-0.5	-0.2	0.8	0.1
Nominal Personal Consumption (YoY % Chg.)	3.9	20.7	11.3	11.8	8.9	5.5	5.0	4.3	-2.6	11.7	5.9	4.0
Nominal Personal Income	16.1	1.1	4.7	6.5	-5.1	1.6	1.5	1.7	6.5	7.0	-0.2	4.0
Retail Sales Ex-Autos	11.6	28.5	15.4	16.7	8.5	3.4	3.2	2.9	0.3	17.8	4.4	3.4
Consumer Price Index	1.9	4.8	5.3	5.8	5.2	3.3	2.3	2.1	1.2	4.5	3.2	1.9
Federal Funds Rate (Upper Bound)	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.88
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.54	3.25	3.25	3.88
10-Year Treasury Yield	1.74	1.45	1.52	1.60	1.68	1.78	1.98	2.18	0.89	1.58	1.91	2.46

Forecast as of: October 14, 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.

Footnotes

[1] Conference Board and Bureau of Economic Analysis, U.S. Department of Commerce
[2] Bureau of Labor Statistics, U.S. Department of Labor

Accessibility Notes

Fig. 1
GDP CAGR ranges from 2.4% in Mar-2019, to a low of -31.2% in Jun-2020, a high of 33.8% in Sep-2020, and the latest reading of .4% in Sep-2021, with the GDP CAGR forecast to finish 2021 at 4.4%, 2022 at 2.6% and 2023 at 2.7%. YoY GDP growth ranges from 2.2% in Mar-2019 to a low of -9.1% in Jun-2020, a high of 12.2% in Jun-2021, and the latest reading of 4.4% in Sep-2021, with YoY GDP growth forecast to finish 2021 at 4.4%, 2022 at 2.9%, and 2023 at 2.6%.

Fig. 2
A line chart showing growth ranging from 1.8% in Jan-2019 to a high of 7.8% in Apr-2020, a low of -3.7% in Apr-2021 and the latest reading of -1.2% in Jul-2021.

For more information

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