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THE SHRINKING CONSUMER RUNWAY

IT'S HARD FOR THE FED TO GET A SOFT LANDING WHEN THE BULK OF THE ECONOMY IS RUNNING OUT OF RUNWAY

- Why the consumer is key to watch vis-à-vis the economy;
- What recent GDP revisions tell us about consumer spending;
- How consumers' balance sheets tell the real story of what's ahead;
- The biggest issue facing consumers and investors for the next 15 years;
- How you should react to key consumer signposts;
- And more!

Near the end of September, it was announced that the BEA, the agency that analyzes and produces GDP data, had revised down the Q1 GDP numbers for 2020, 2021 and 2022. The culprit? Consumer spending.

Reuters reported, “In 2022, GDP contracted at a 2.0% rate in the first quarter, revised down from the previously reported 1.6% pace. Consumer spending, now estimated to have been flat instead of growing at a 1.3% rate as previously reported, accounted for the downgrade.”

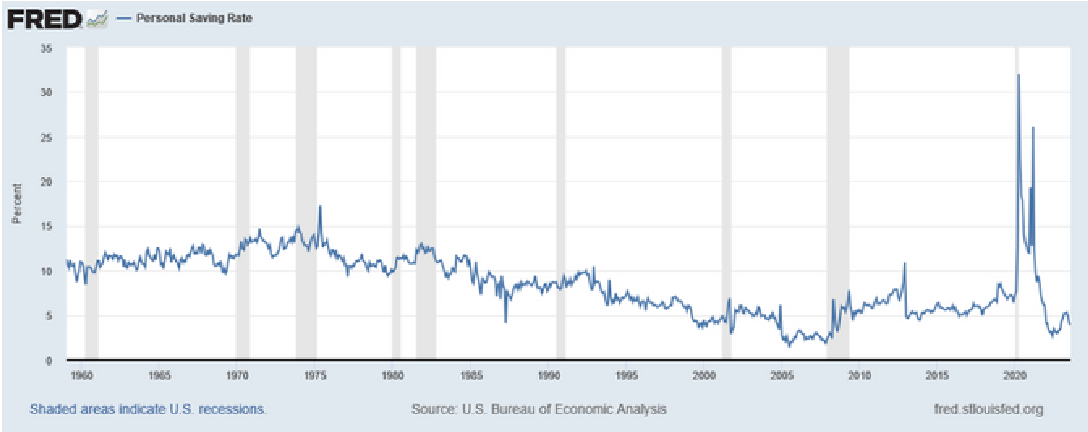
Even with robust government spending propping up the GDP, the consumer is an incredibly important piece of the economy, typically accounting for nearly 70% of the economy overall.

American consumers have been carrying the economy on their backs to their own detriment. Now, we are hearing the consumer may not have been as strong as we thought. And with the consumer’s runway getting shorter, it makes it much more challenging for the Fed to engineer their hoped-for soft landing.

With a soft landing looking less likely, it’s a critical time to think about hedges like gold and silver—more on that below.

While the broader economic numbers may still be in positive territory (unless, of course, they get downward revisions, too), the balance sheets of individuals aren’t looking so hot.

On the personal savings side, the personal saving rate is currently at 3.9% (as of August 2023 data), a rate materially lower than historical averages.



U.S. Bureau of Economic Analysis, Personal Saving Rate [PSAVERT], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/PSAVERT, September 30, 2023.

On the debt side of the balance sheet, the situation is looking even more grim.

As of the end of Q2 2023, household debt was at an all-time high of $17.1 trillion. This includes credit card debt, which had passed a record of $1 trillion, as well as records across auto and student loan debt as well.

Delinquencies in credit card debt and auto loans have also reached levels that haven't been seen in more than a decade (3.8% and 3.6%, respectively). At current interest rates (for the last week of September, the APR for Forbes' tracked credit card interest rates was more than 28%!), delinquencies are likely to continue.

Throw on top that the student loan pause has been lifted and repayments are due beginning this month, and the consumer will continue to be squeezed.

Stimulus has run out, reality is setting in and the runway is getting shorter and shorter.

Jamie Dimon, head of JPMorgan Chase, has been warning about the consumer and the economic trajectory.

S&P Global Ratings agrees. In a recent report, they said, "excess household savings have been largely depleted, student-loan payments restart next month, and there's been a surge in subprime auto loan and credit card delinquencies, especially among lower-income (and younger) Americans."

Of course, part of what has given the consumer confidence has been the robust labor market. Workers have felt secure in their jobs, or at least being able to find a new one, which gives them the confidence to continue to spend (even if that is beyond their means).

And, recent union labor negotiations have produced pay raises in certain sectors.

However, union labor is a small percentage of the overall worker base.

On the job openings front, the most recent JOLTS (Job Openings and Labor Turnover Survey) data maintained the previous month's lower rate of workers quitting. More consternation about jobs (real or perceived) could cause the consumer to pull back. But the likelihood is that personal balance sheets, particularly the liabilities side, will crack first.

Let’s not forget another potential consumer headwind: energy prices. Consumers have been facing higher prices at the pump, eating into more of their income and creating less confidence about the economy. Should we get a cold winter, whether domestically, in Europe, or both, that could fuel a further rise in energy costs (pun intended) and quell consumer demand in other areas.

Given the economic backdrop, it’s hard to see how the consumer gets a soft landing when their runway is getting shorter and shorter—it looks like they are in position to overshoot the runway altogether.

Even consumer stock analysts are starting to sound the alarm on this situation. Morgan Stanley strategist Michael Wilson warned that household spending levels are not likely to be able to be sustained. It was reported by Fortune that he wrote about the deteriorating performance in consumer discretionary stocks, saying, “This price action is picking up on slowing consumer spend, student loan payments resuming, rising delinquencies in certain household cohorts, higher gas prices and weakening data in the housing sector.”

The position of the consumer doesn’t necessarily mean we get a full technical recession (given government spending) or a steep drop in inflation (given the need to finance the US debt and deficits and other issues) as it normally would, but it does mean that a shallow recession is probably the base case, with stagflation being the next likely probability. Possibilities including a deeper recession or higher inflation are also not off the table.

The biggest issue facing both investors and consumers though is that the next 15 years will be nothing like the last 15 years. This is an underappreciated view. The last 15 years were an anomaly, and given the backdrop of the US’s financial position and shifts in the geopolitical landscape, we must appreciate it as it is and not think of it as a baseline or a benchmark.

So, what should you do?

Personally, continue to manage your budget appropriately and cut back where you can in your discretionary spending. Beef up your emergency funds if you don’t have a robust runway of your own and make sure you are earning an appropriate yield on any cash via money market instruments.

From a portfolio perspective, I would consider the recent pullback in pricing of gold and silver as an immediate buying opportunity to help round out hedges for the mid-to-long term.

If you haven't had an opportunity to hedge and diversify your portfolio, or perhaps you haven't hedged enough, give my friends at Goldline a call at 800-319-9533 to help you. Their knowledgeable Account Executives can assist in helping you navigate what might be ahead by using precious metals as a potential hedge, along with any other diversification and hedging strategies that might be appropriate for you.

Consumers have been flying high on stimulus, good jobs, and a decade and a half of massive market manipulation by the Fed. But the consumers' planes are running low on gas (which is also getting more expensive) and the runway is getting shorter. While a soft landing is unlikely, let's hope there's not a crash landing.

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