



# 2024 outlook: Fed WINS in '24, but at what cost?

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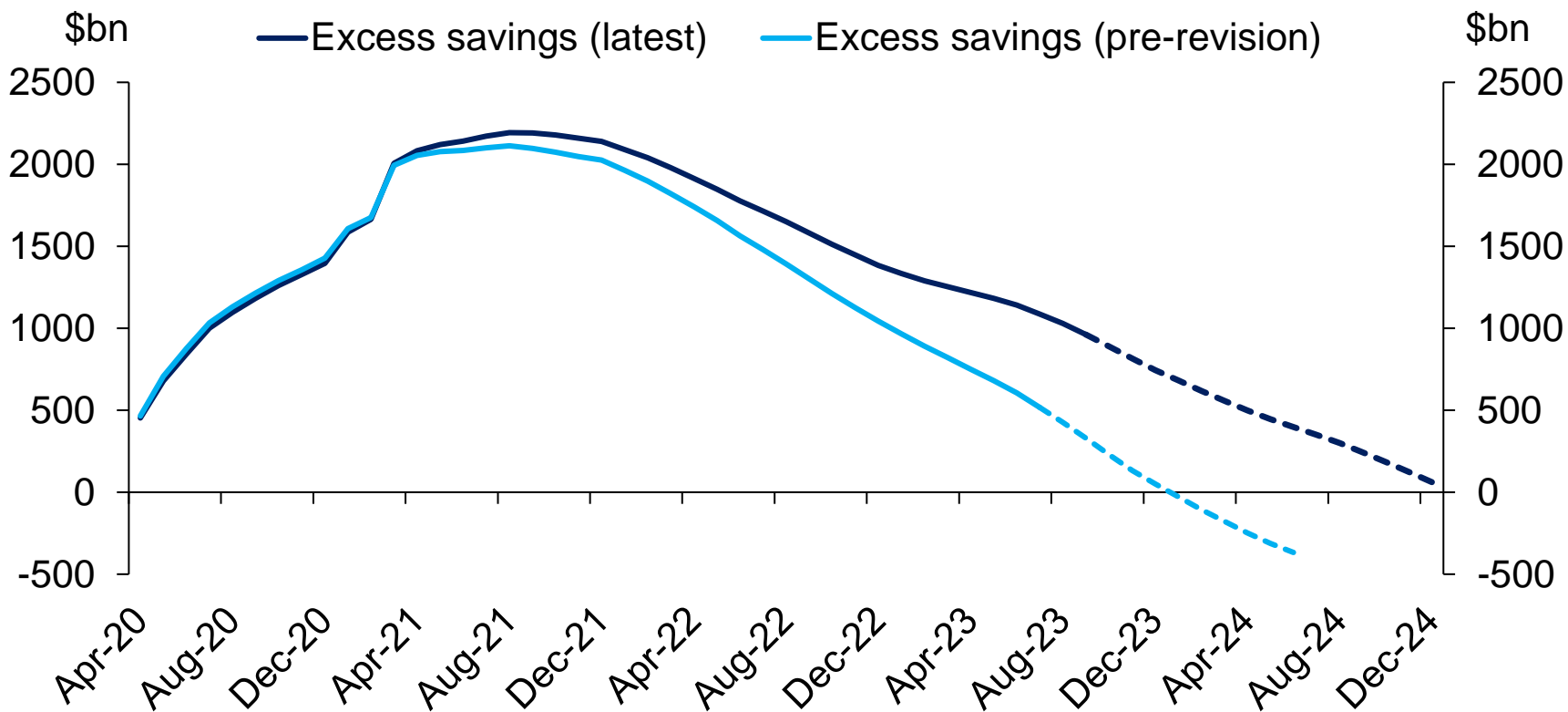


# 2023 in review: Why the economy outperformed



# Household accumulated excess savings revised higher but falling

## Household accumulated excess savings

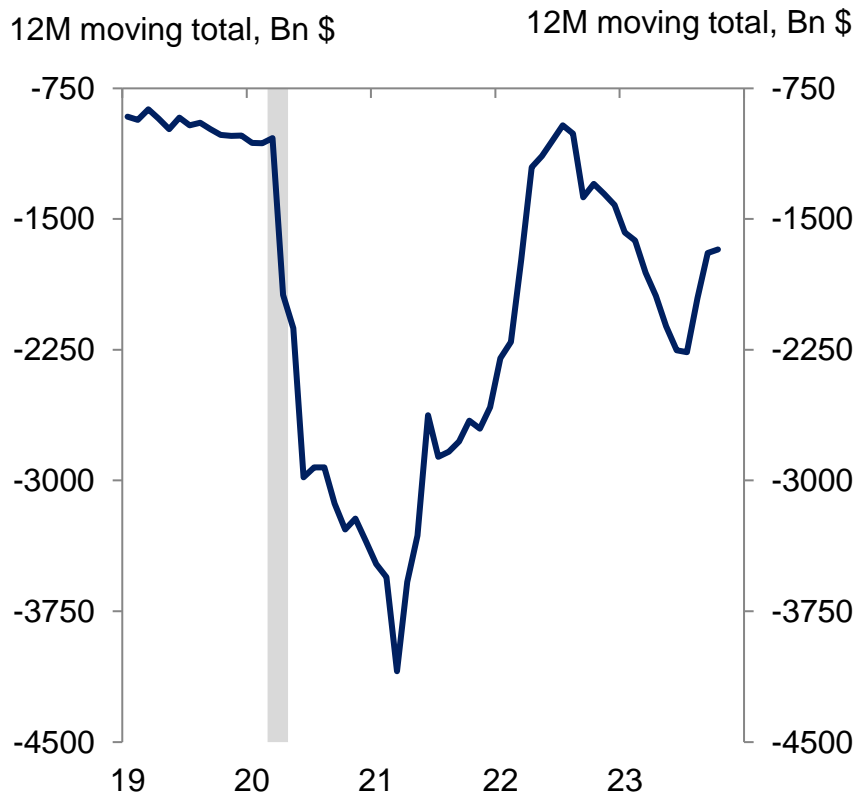


Source: BEA, Haver Analytics, Deutsche Bank

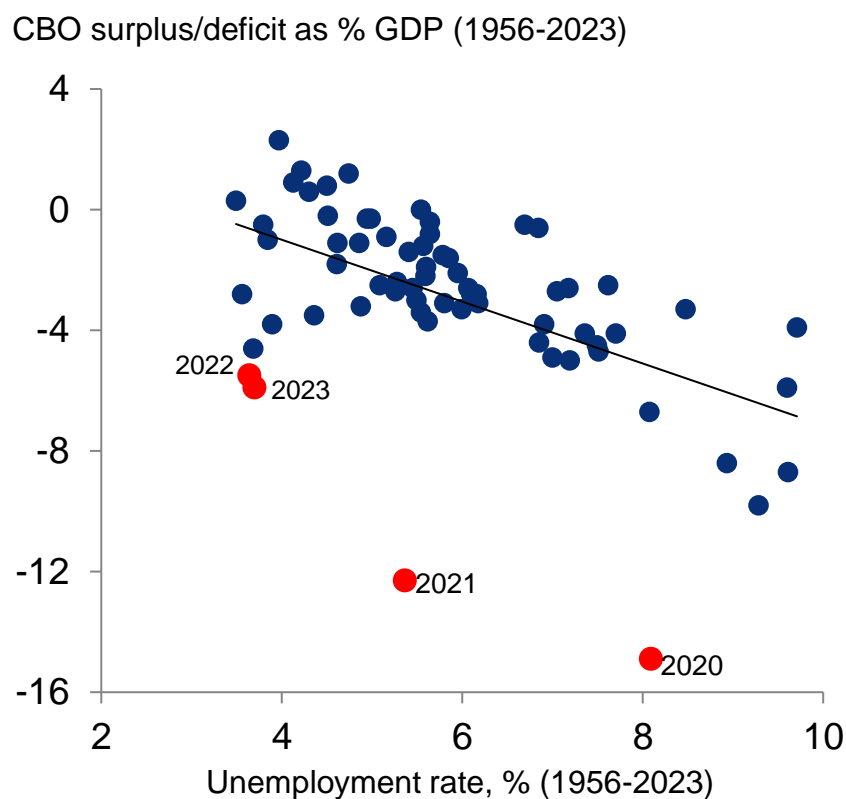


# Fiscal policy provided support in 2023

## Federal budget deficit



## Unemployment versus budget deficit

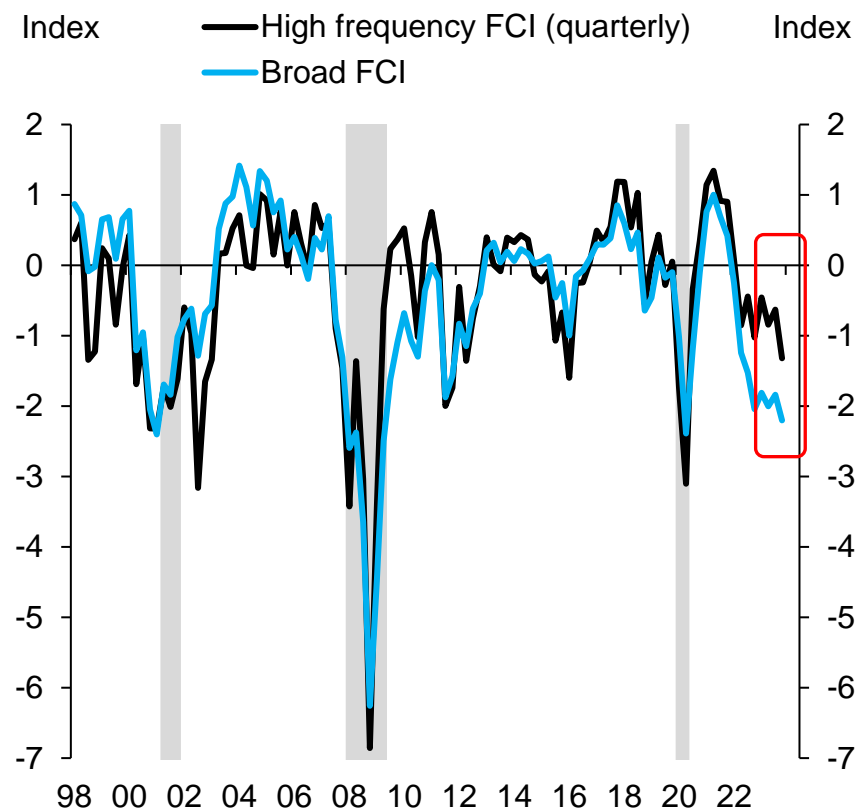


Source: Treasury, BLS, CBO, Haver Analytics, Deutsche Bank

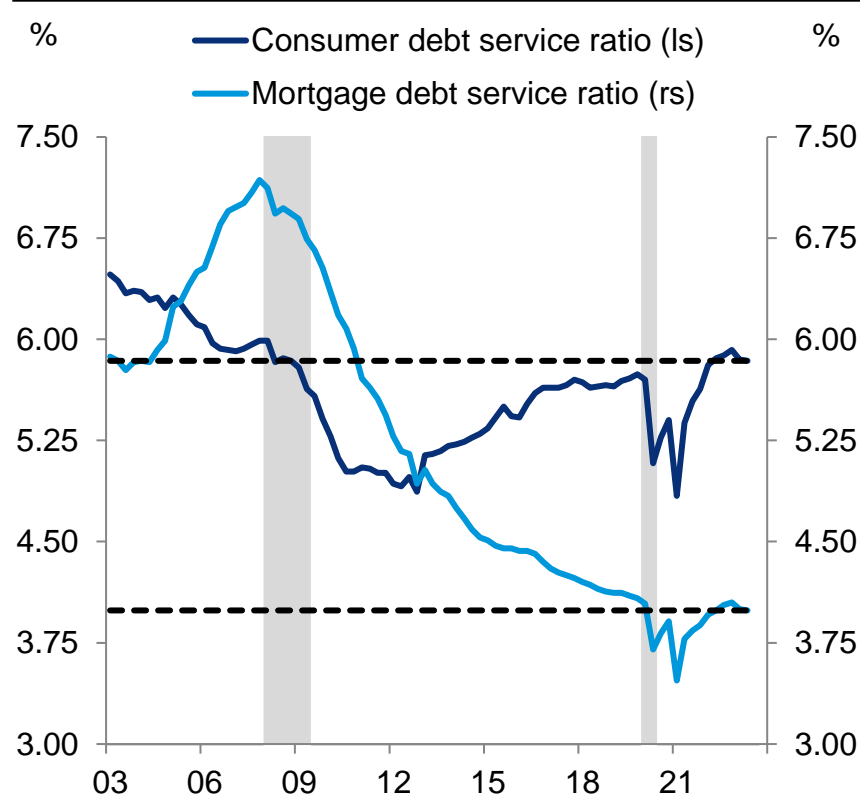


# Monetary policy traction was muted with asset-price based FCI not tightening and locked in rates

## FCIs



## Debt service ratios

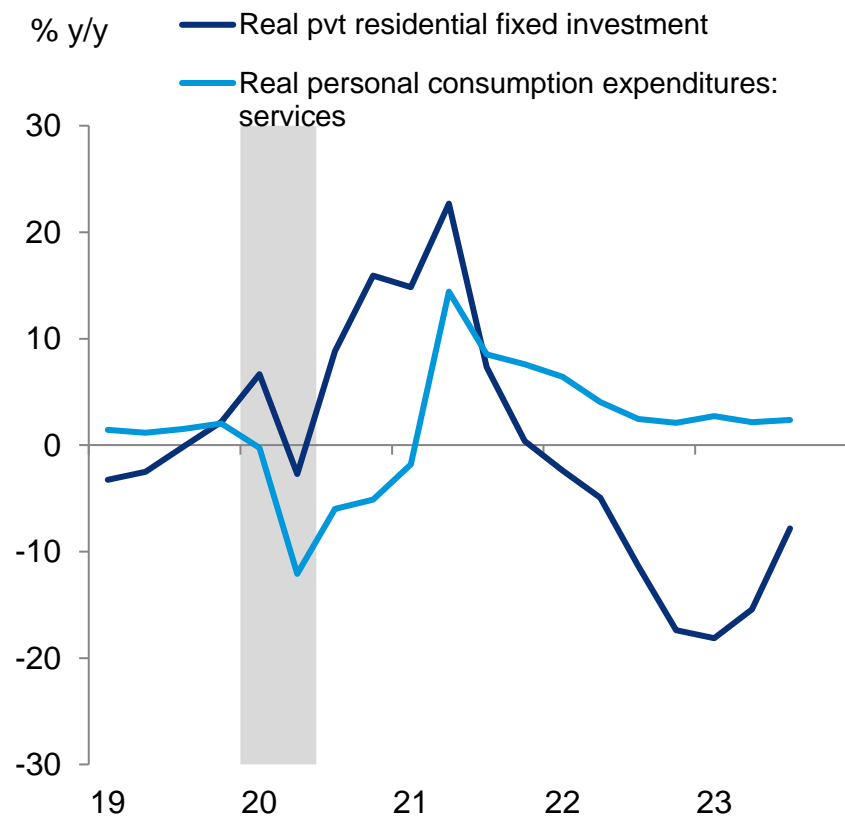


Source: FRB, Haver Analytics, Deutsche Bank

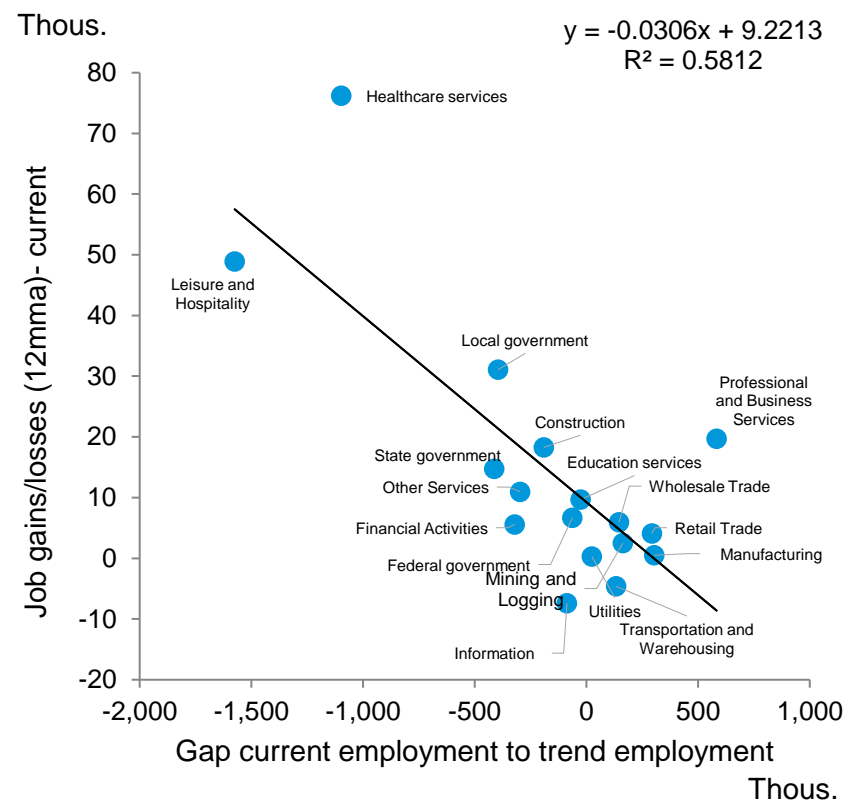


# An asynchronous cycle: consumer sturdy as housing plunged, pent-up demand in some sectors

## Residential investment and services consumption



## Jobs gap vs. pre-covid compared to job momentum



Source: BEA, BLS, Haver Analytics, Deutsche Bank



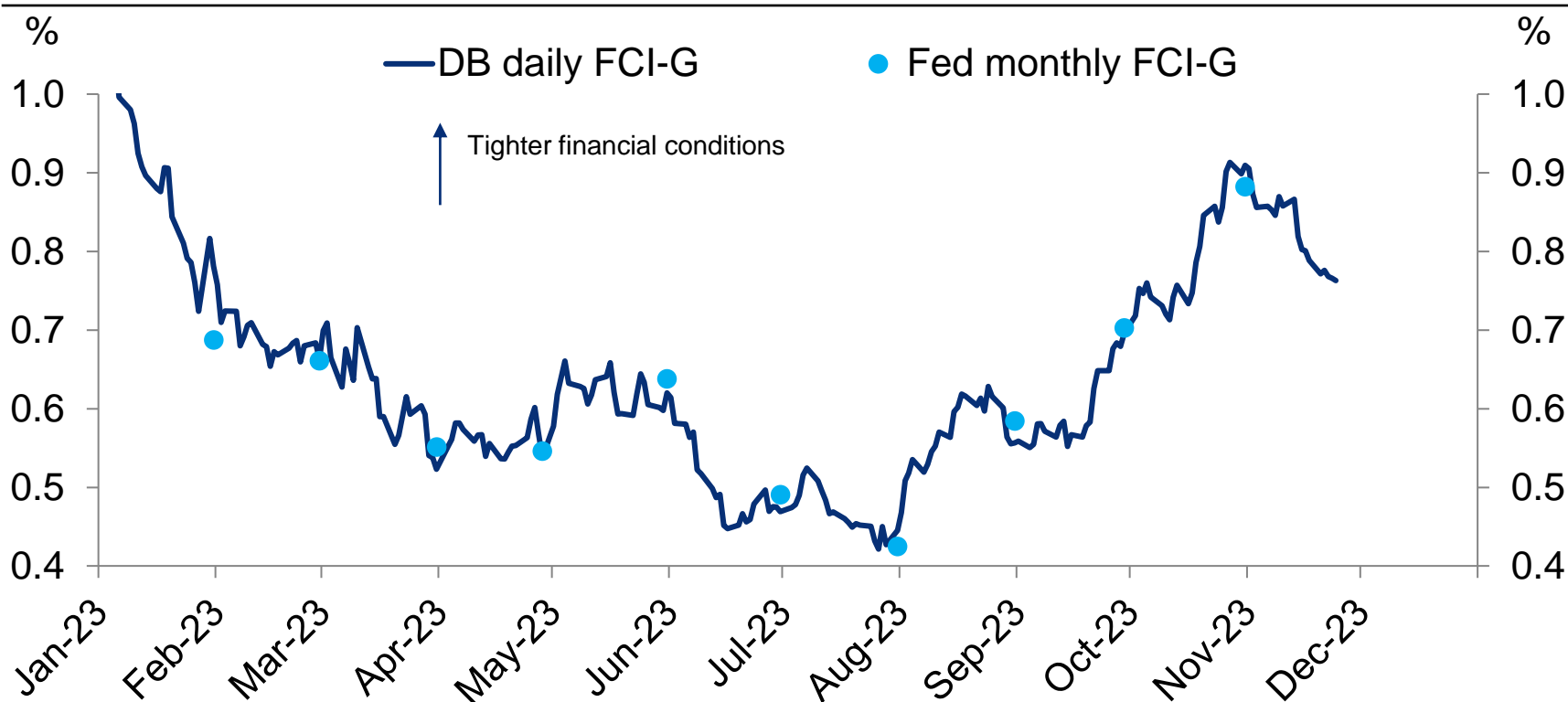
# The continued case for a mild recession





# Even though they have loosened since the November meeting, financial conditions remain tighter

## DB's daily Fed FCI

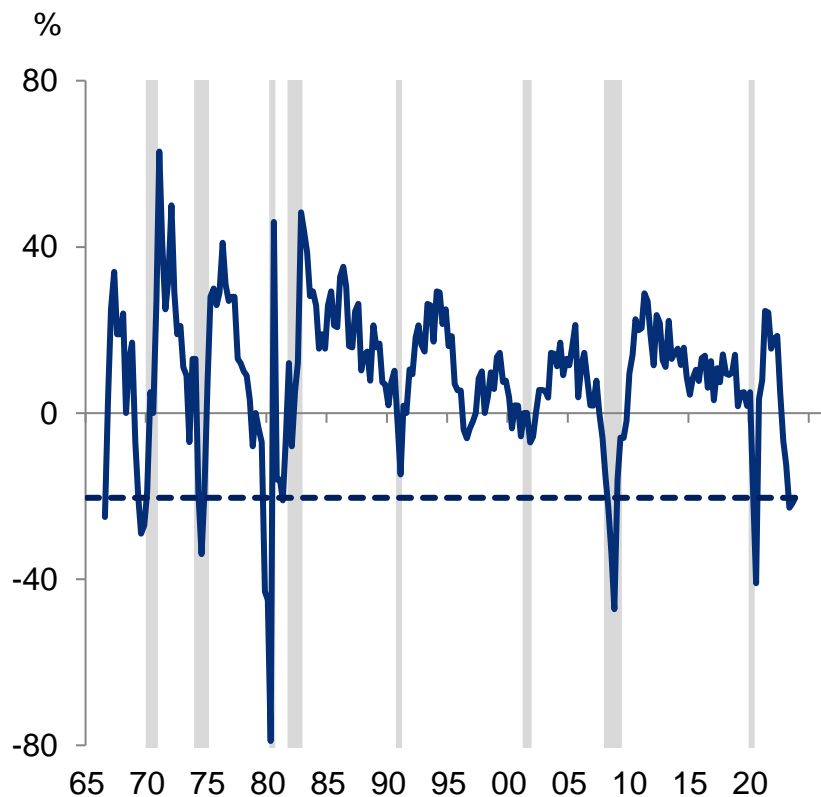


Source: FRB, Haver Analytics, Deutsche Bank

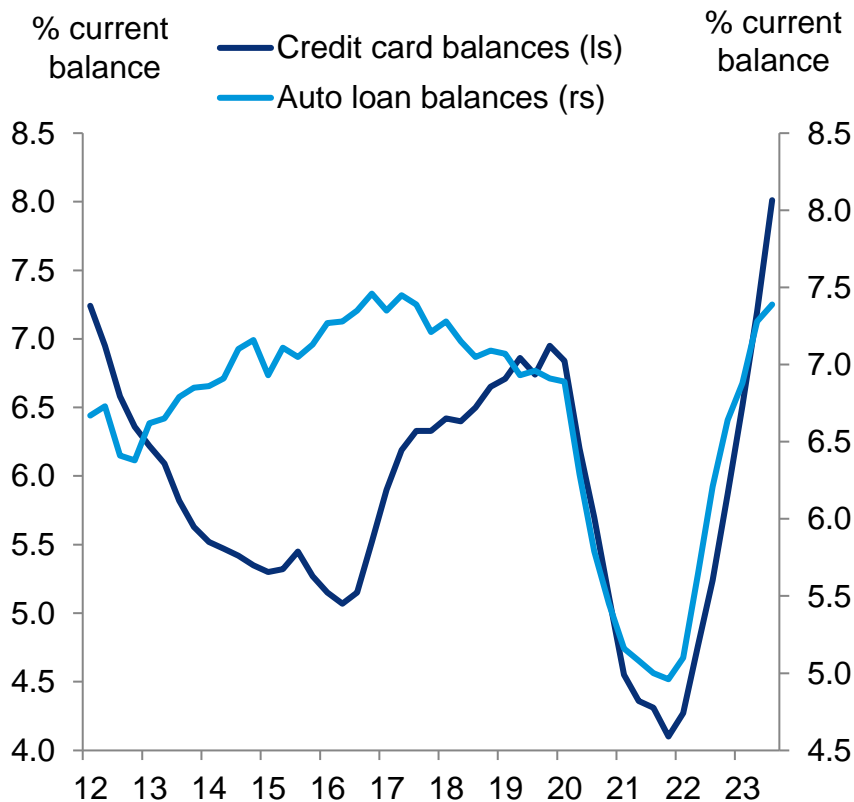


# Bank lending conditions are very tight, including for consumers, with delinquency rates on the rise

## Banks' willingness to lend to consumers



## Newly-delinquent loan balances



Source: FRB, FRBNY Consumer Credit Panel/ Equifax, Haver Analytics, Deutsche Bank

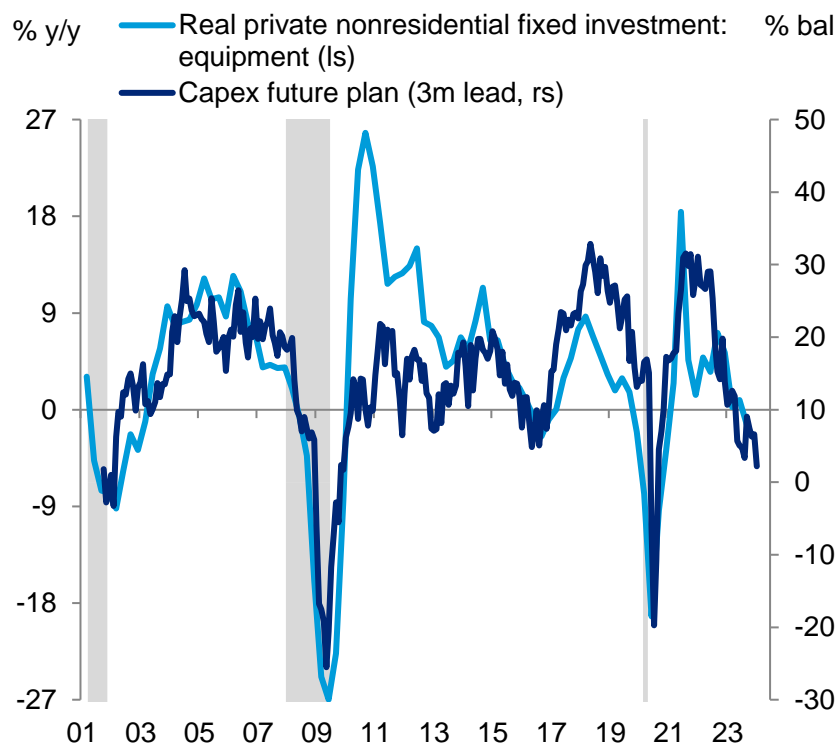


# Leading indicators for capex signal a slowdown is coming

## SLOOS versus equipment spending



## Firm capex versus equipment spending



Note: Capex future plan is an average from the regional Fed surveys. Source: FRB, BEA, Regional Fed Surveys, Haver Analytics, Deutsche Bank

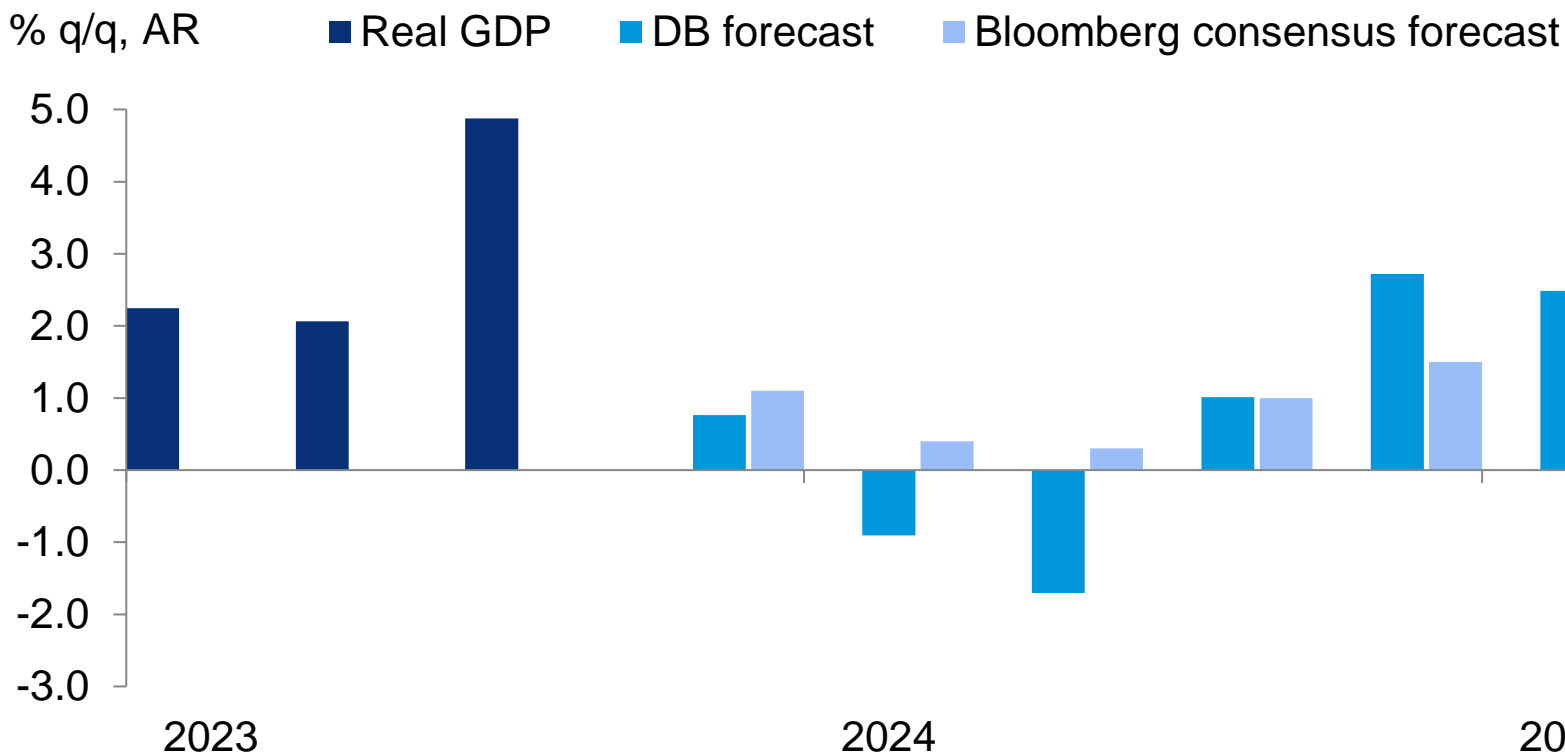


# Growth: An H1 soft patch



# DB growth forecast below consensus in H1 2024, above consensus end-24/early-25

## US growth forecast versus consensus

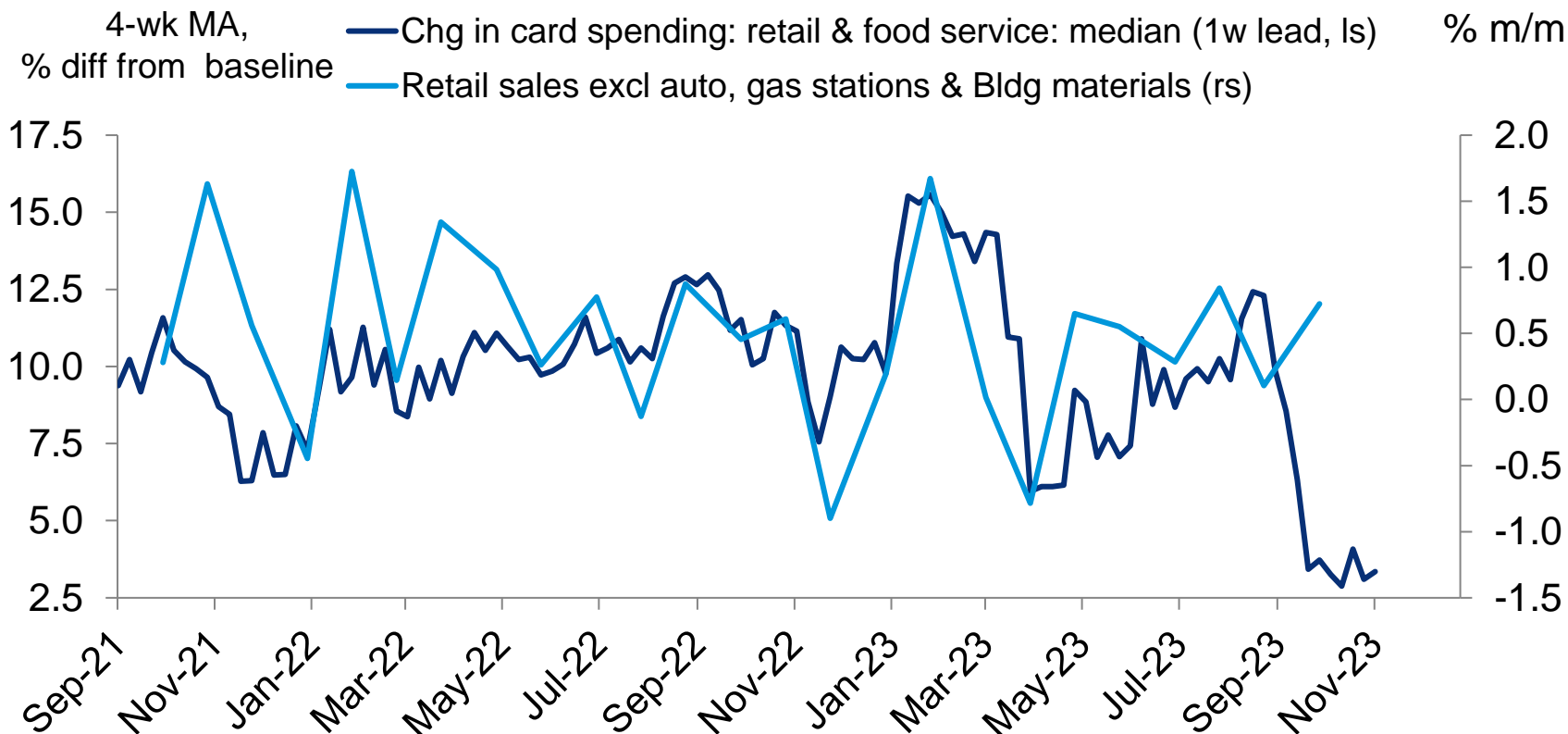


Note: Bloomberg consensus is as of November 22, 2023. Source: BEA, Haver Analytics, Bloomberg Finance LP, Deutsche Bank



# Card spending data have softened recently

## BEA card data versus retail control



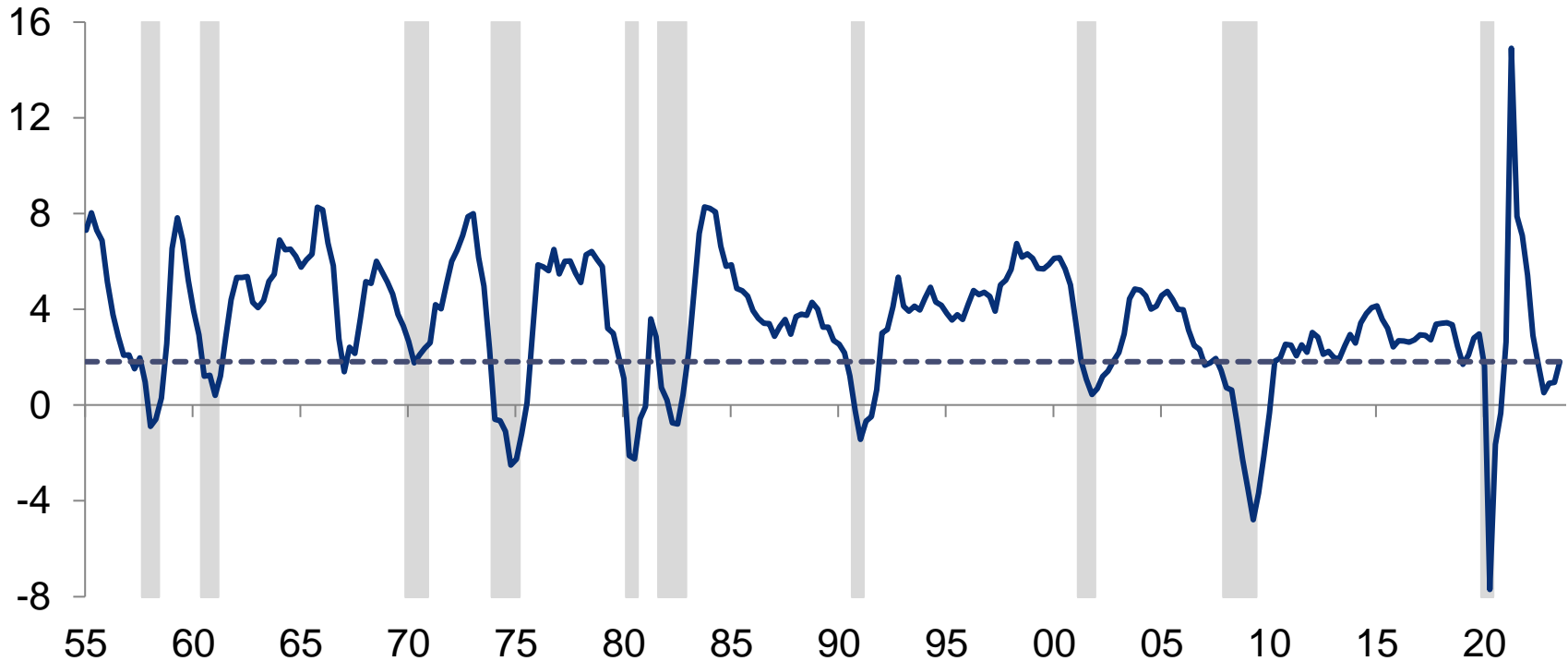
Source: BEA, Census, Haver Analytics, Deutsche Bank



# Domestic private demand excluding autos and transport equipment is weak

## Domestic private demand excluding autos and transportation equipment

y/y % chg

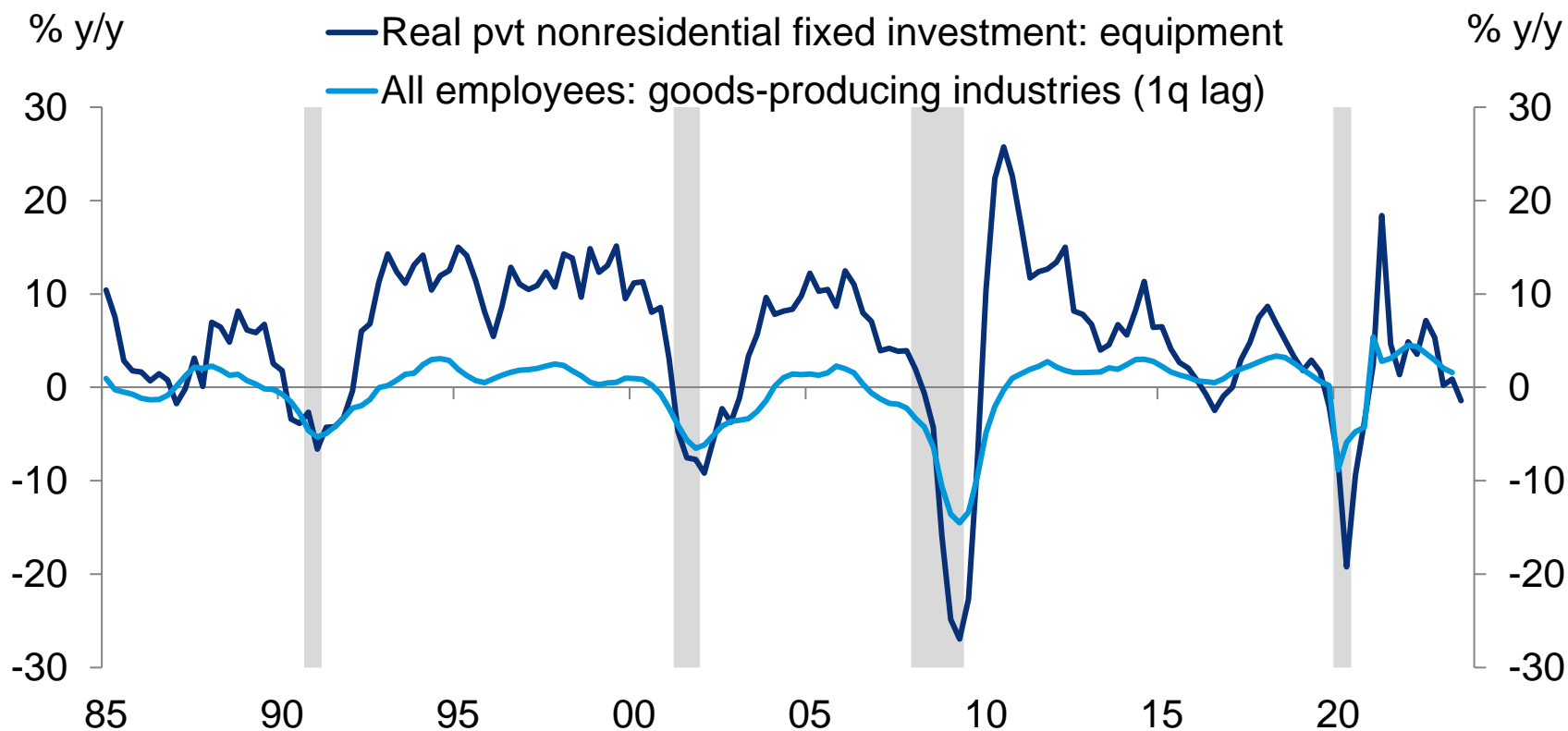


Source: BEA, Haver Analytics, Deutsche Bank



# Downturn in equipment spending tends to lead to weaker payrolls

## Capex spending versus payrolls



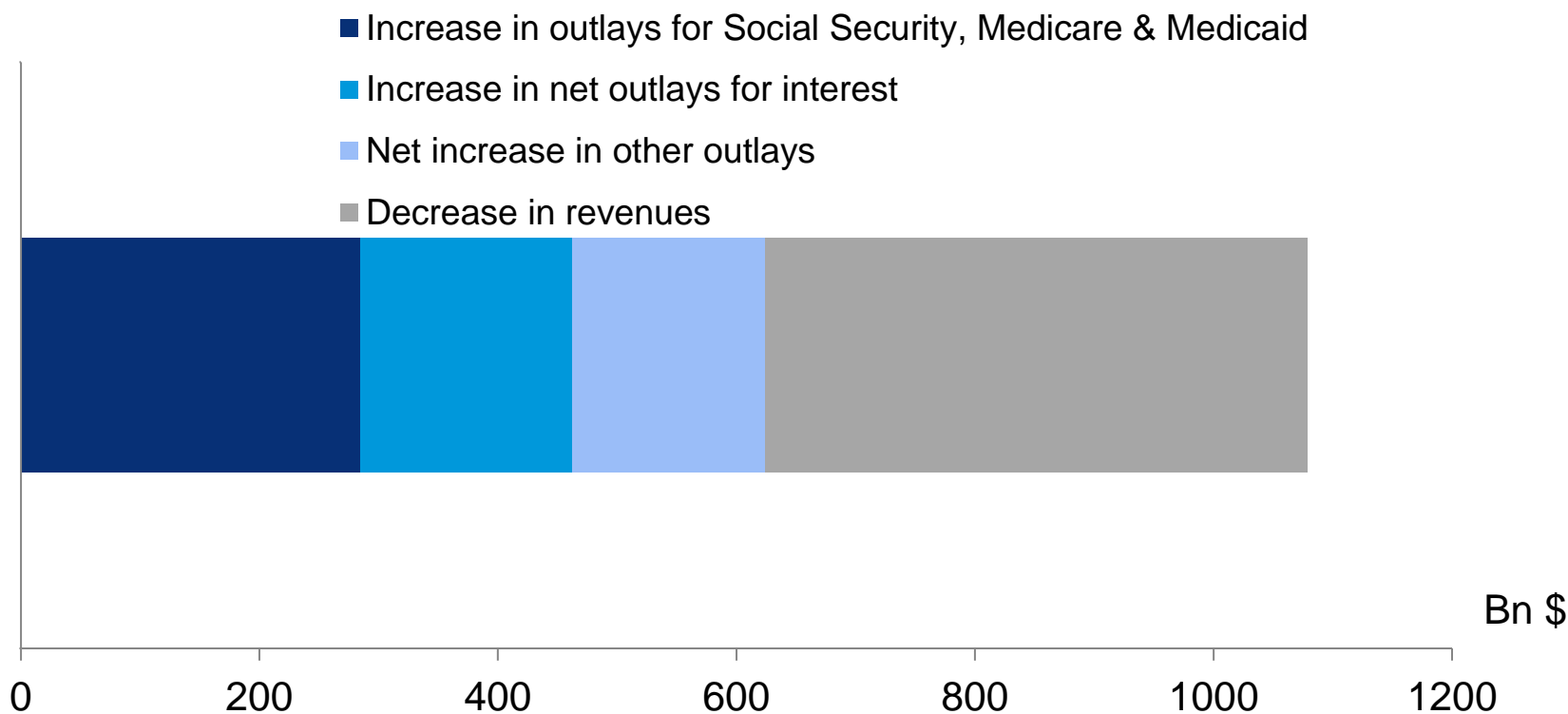
Source: BEA, BLS, Haver Analytics, Deutsche Bank





# The deficit widened more than expected in 2023 mostly on revenue shortfalls

## Contributions to the \$1.1trn widening of the federal deficit in FY 2023



Source: CBO, Deutsche Bank



# Breaking down the deficit components and our expectations

Fiscal Year (FY)	CBO May 2023 Estimate of FRA			2023 Actual*	DB Forecast
	2023	2024	2025		2024
Revenues (\$ bn)	4,815	4,847	4,974	4,439*	4,830
Outlays (\$ bn)					
Mandatory	3,975	3,824	4,022		3,940
Discretionary	1,712	1,781	1,833		1,775
Net interest	663	744	769	659*	805
Total	6,350	6,349	6,624	6,467**	6,521
<b>Deficit (\$ bn)</b>	<b>-1,535</b>	<b>-1,501</b>	<b>-1,649</b>	<b>-2,028**</b>	<b>-1,691</b>

\*September Monthly Treasury Statement

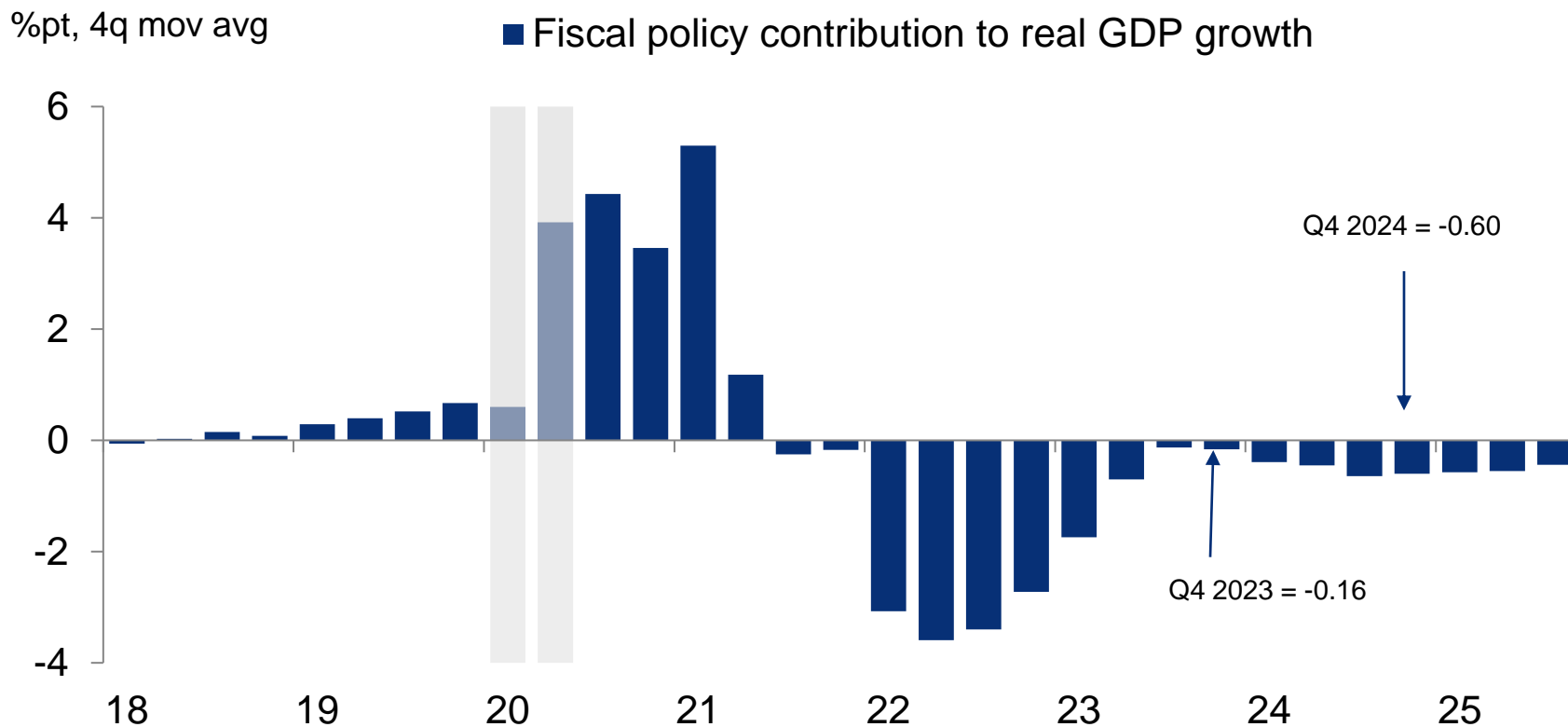
\*\*September Monthly Treasury statement excluding \$333bn student debt cancellation

Source: BEA, BLS, Haver Analytics, Deutsche Bank



# Fiscal impulse is expected to be modestly negative in 2024

## Hutchins Center fiscal impulse



Source: Hutchins Center, BEA, Haver Analytics, Deutsche Bank



# Labor market: Soft landing now, mild recession later?



# Labor market has shown considerable progress coming into better balance

## Measures of labor market slack

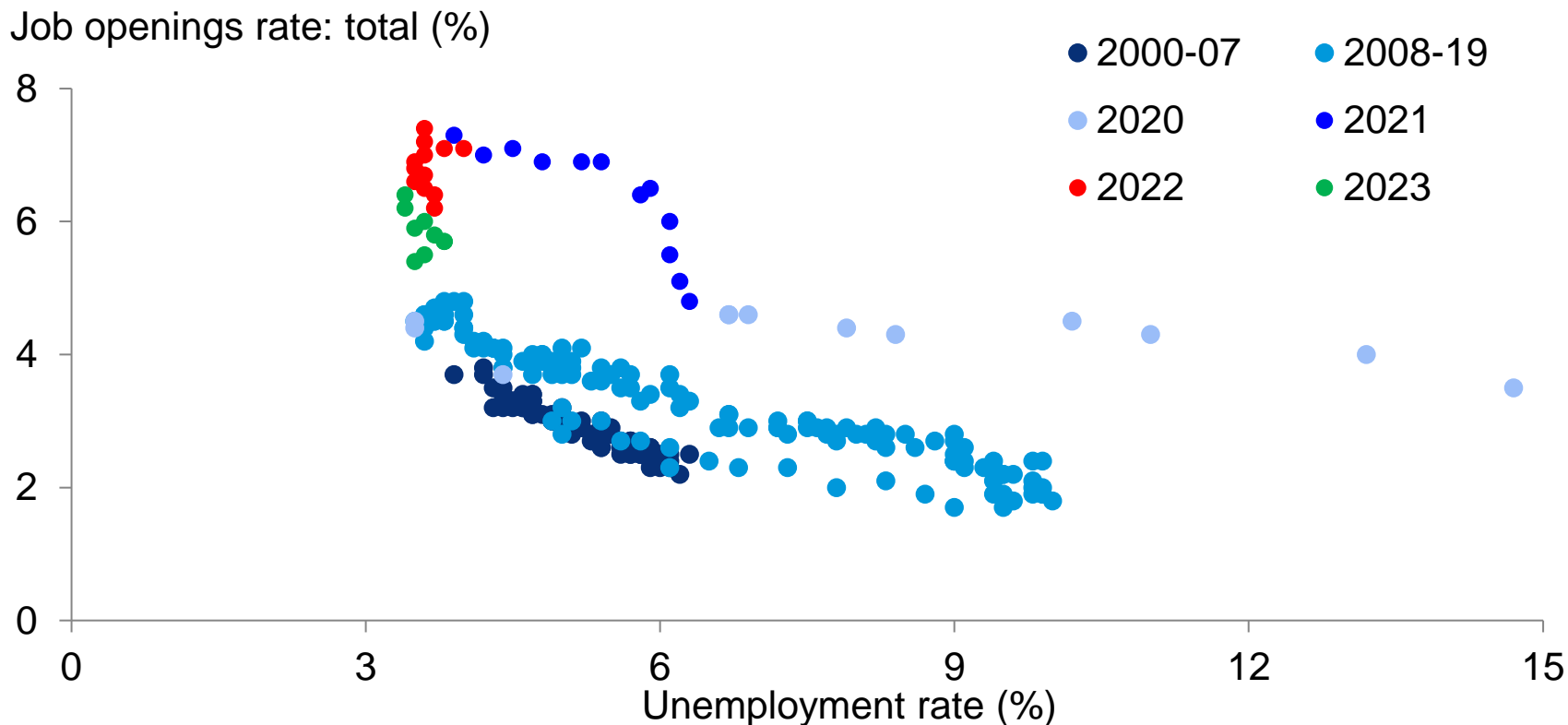


Note: Data show Z-scores translated to fit with directionality of the unemployment rate, i.e., higher=looser, lower=tighter. Source : BLS, Haver Analytics, Deutsche Bank



# Most of the progress driven by declining demand, though unemployment has started to rise

## Beveridge curve (unemployment rate versus job openings)

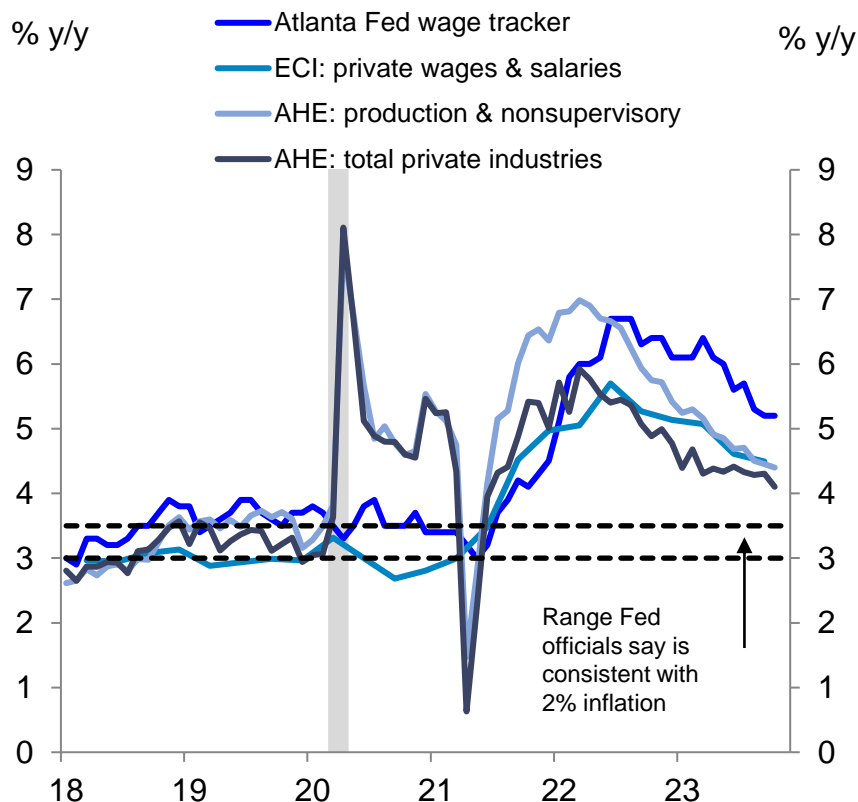


Source: BLS, Haver Analytics, Deutsche Bank

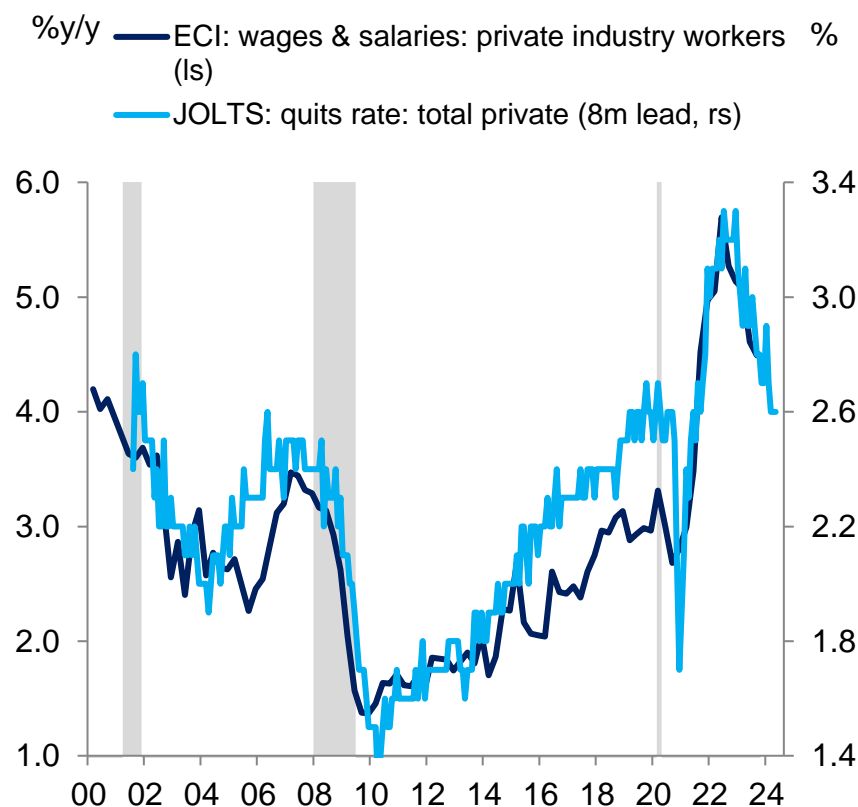


# Wage growth still elevated but leading indicators are compelling that it should normalize ahead

## Wage growth



## Quits rate leading wage growth

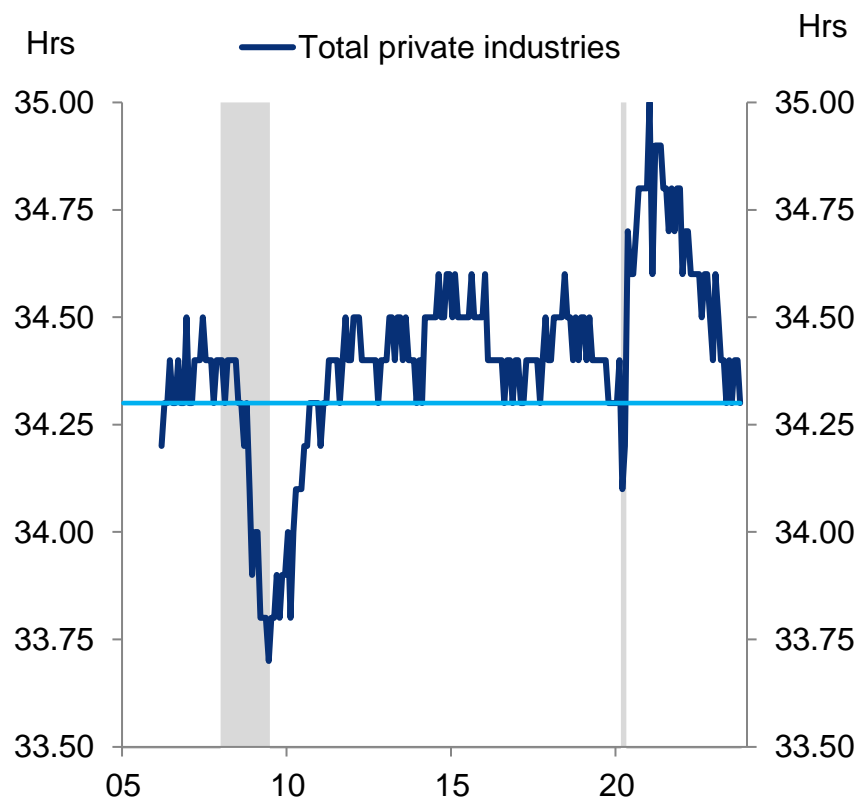


Source: BLS, FRB Atlanta, Haver Analytics, Deutsche Bank

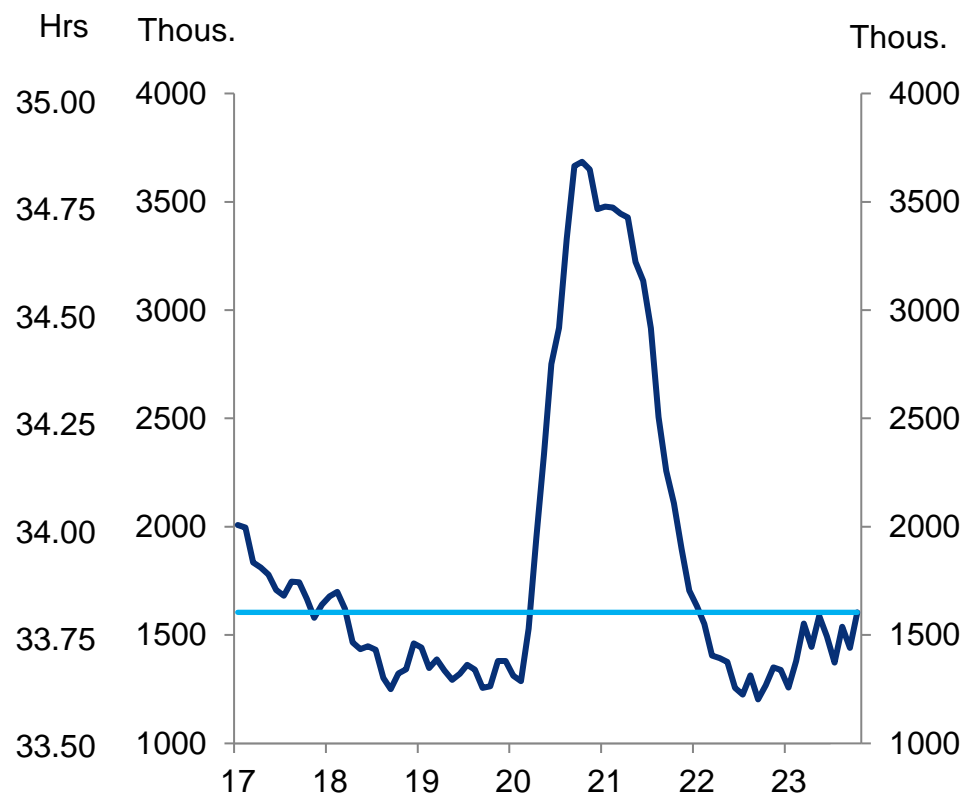


# Data are consistent with a softening labor market: declining workweek, rising permanent job losers

## Average weekly hours



## Permanent job losers



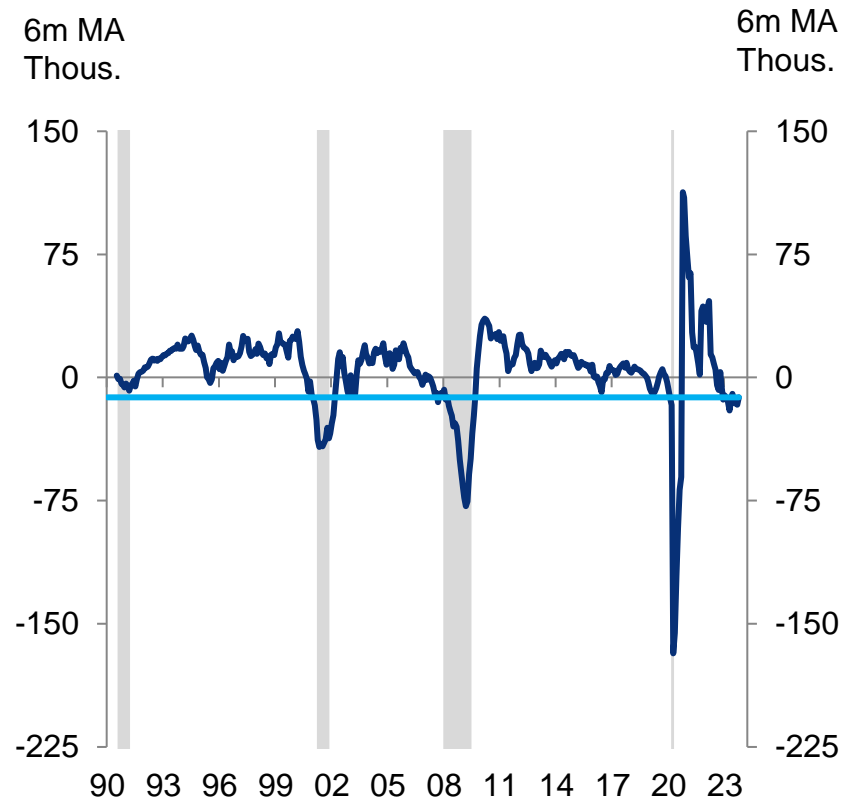
Source: BLS, Haver Analytics, Deutsche Bank



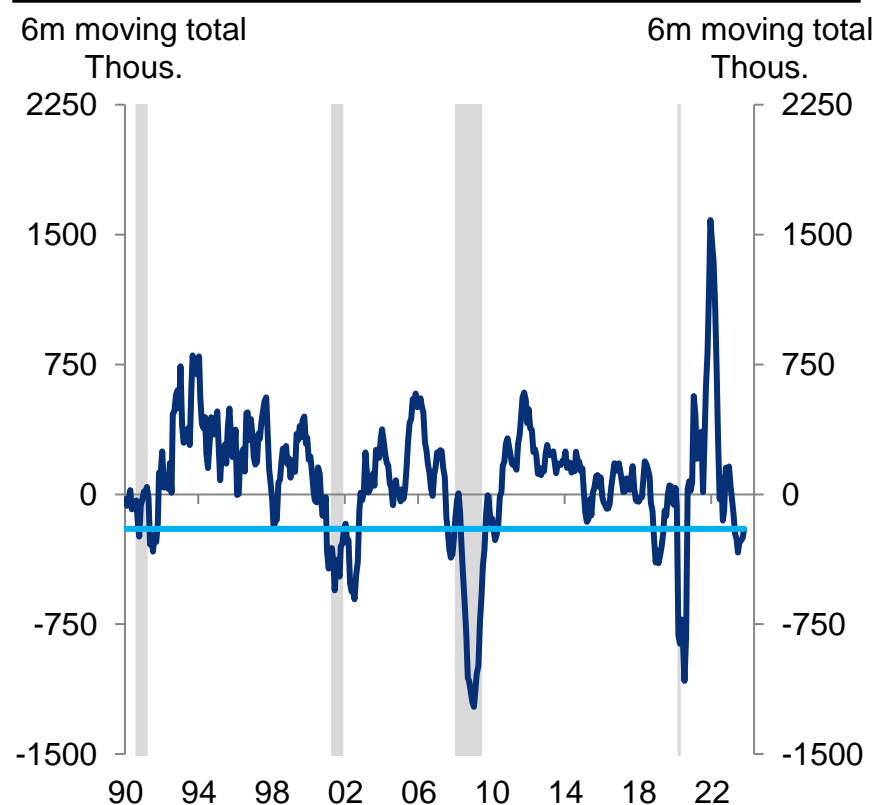


# And temp help workers are being shed amidst consistent downward revisions to private payrolls

## Temporary help workers



## Revisions to private payrolls

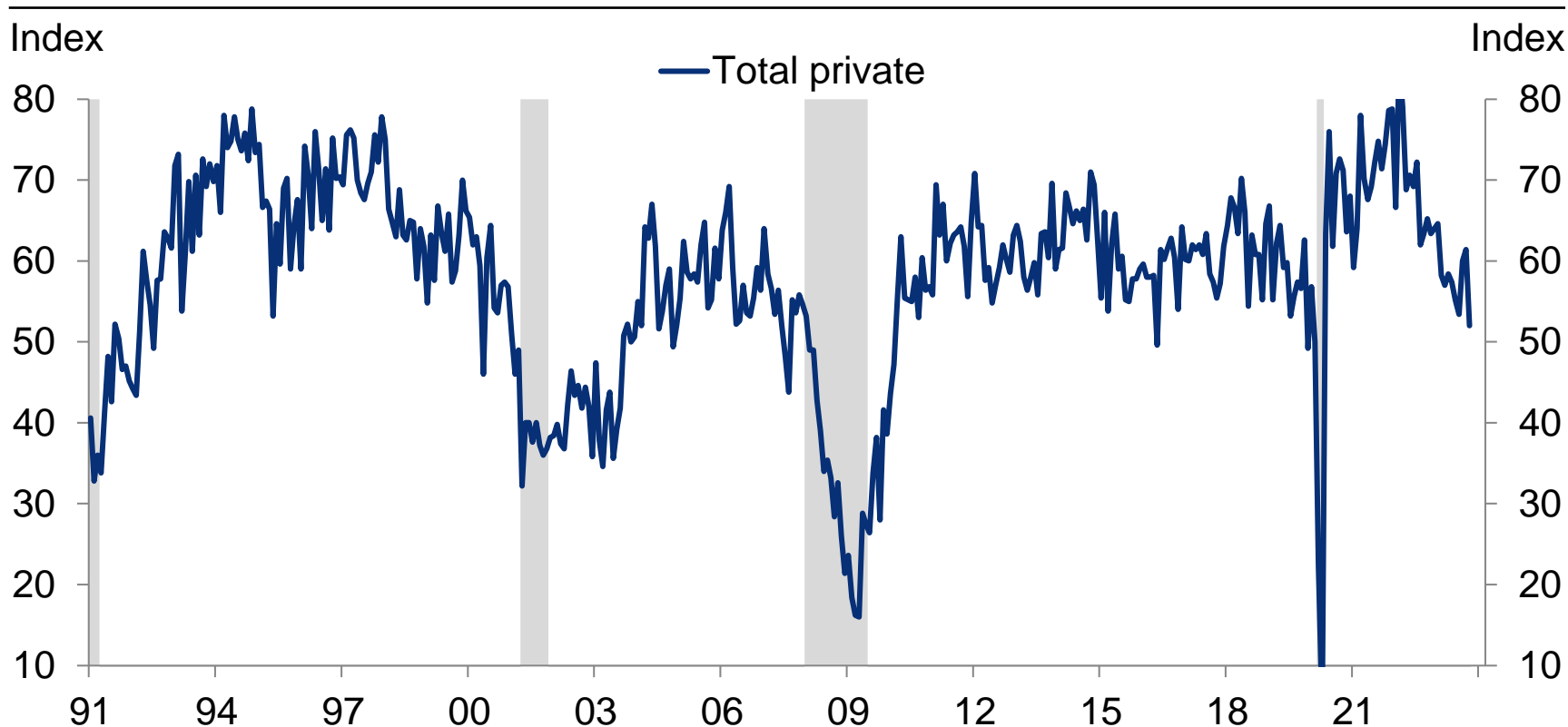


Source: BLS, Action Economics, Haver Analytics, Deutsche Bank



# The diffusion index has slipped noticeably as job gains have narrowed across industries

## Payrolls diffusion index

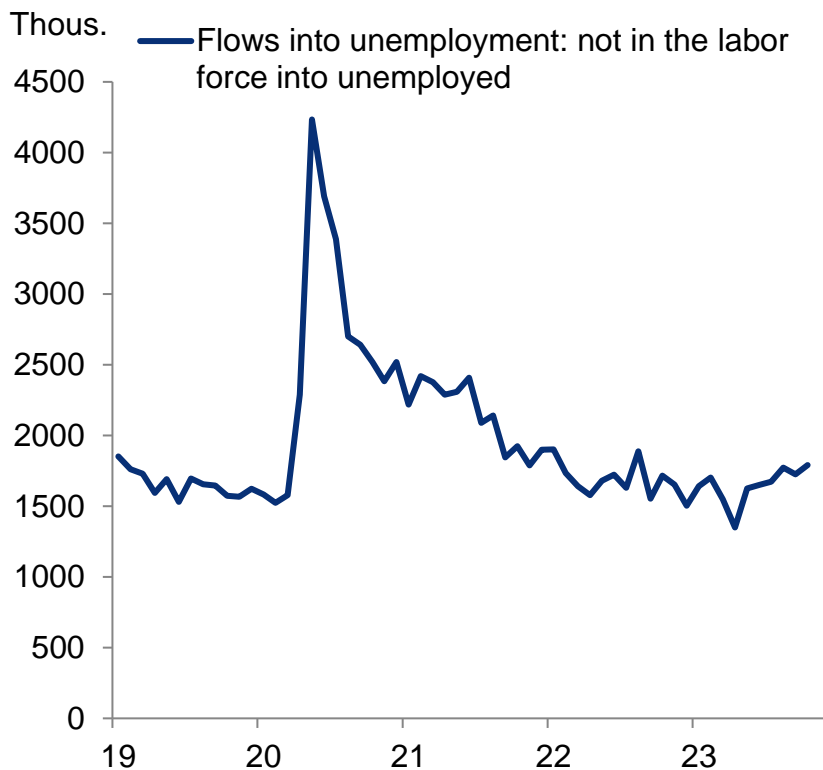


Source: BLS, Haver Analytics, Deutsche Bank

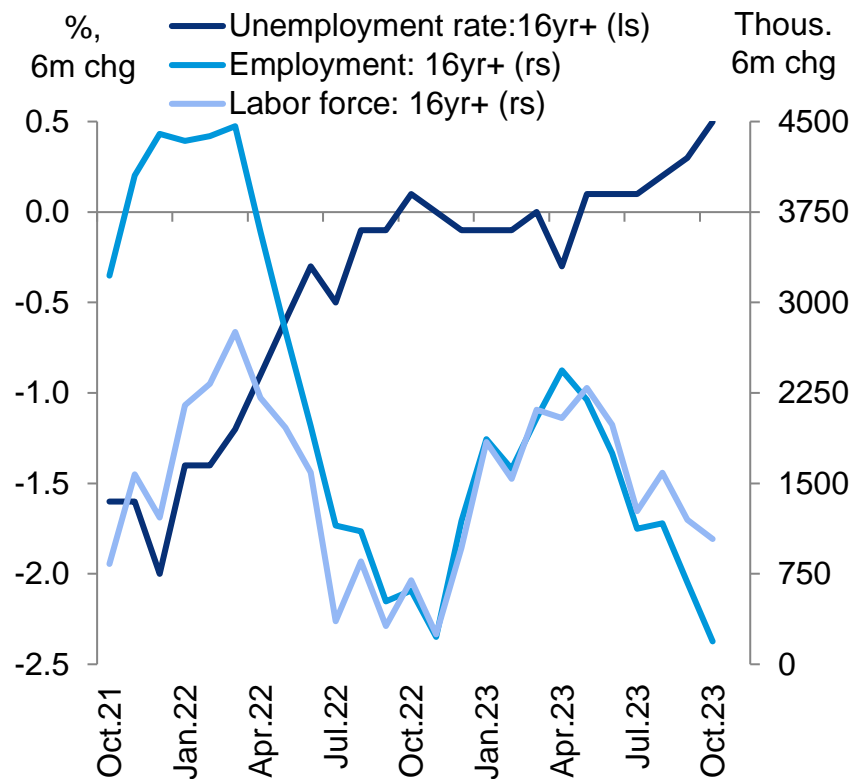


# Labor supply has improved but recent rise in unemployment driven by softening HH employment

## Flows into unemployment



## Household survey data

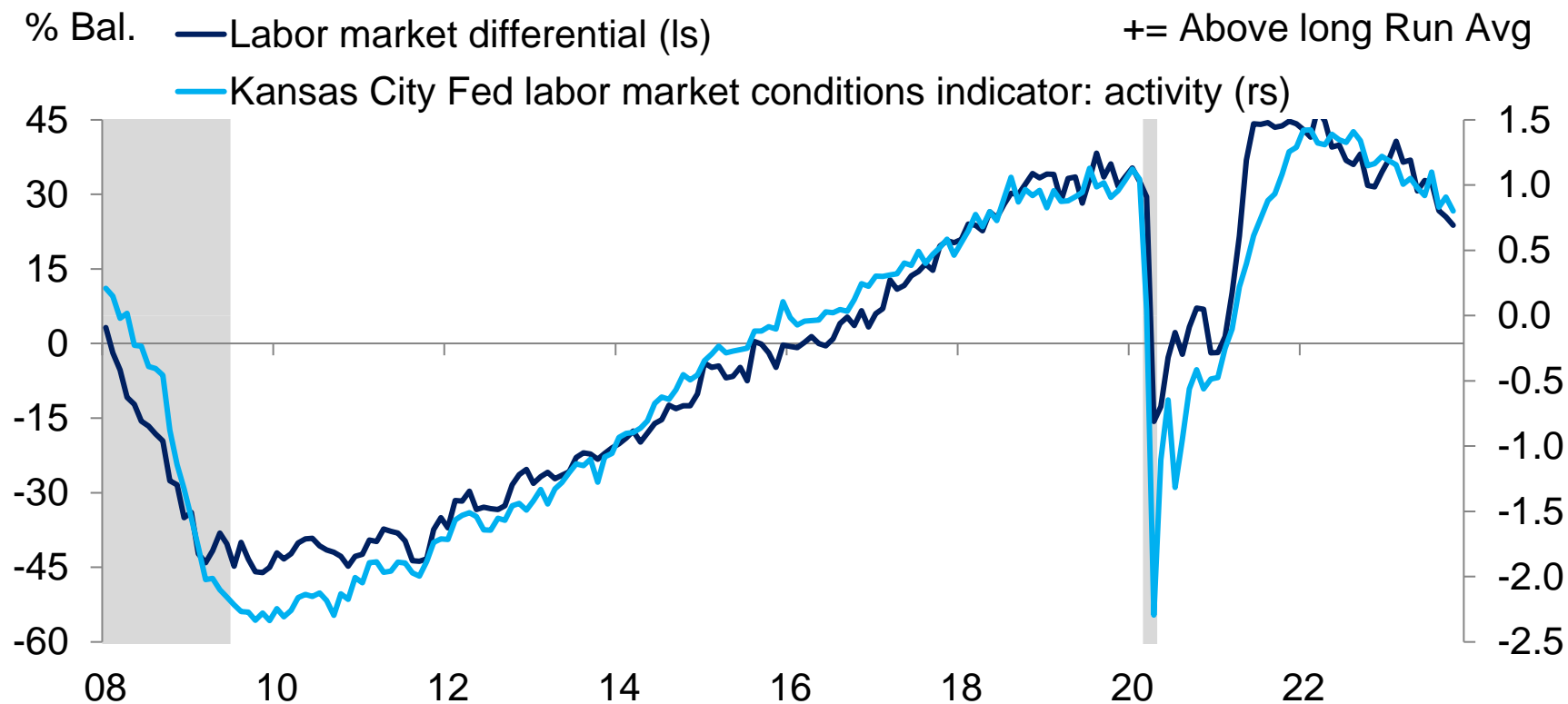


Source: BLS, Haver Analytics, Deutsche Bank



# Broad measures of the labor market have weakened below 2019 levels

## Conference Board labor market differential vs. KC Fed LMCI

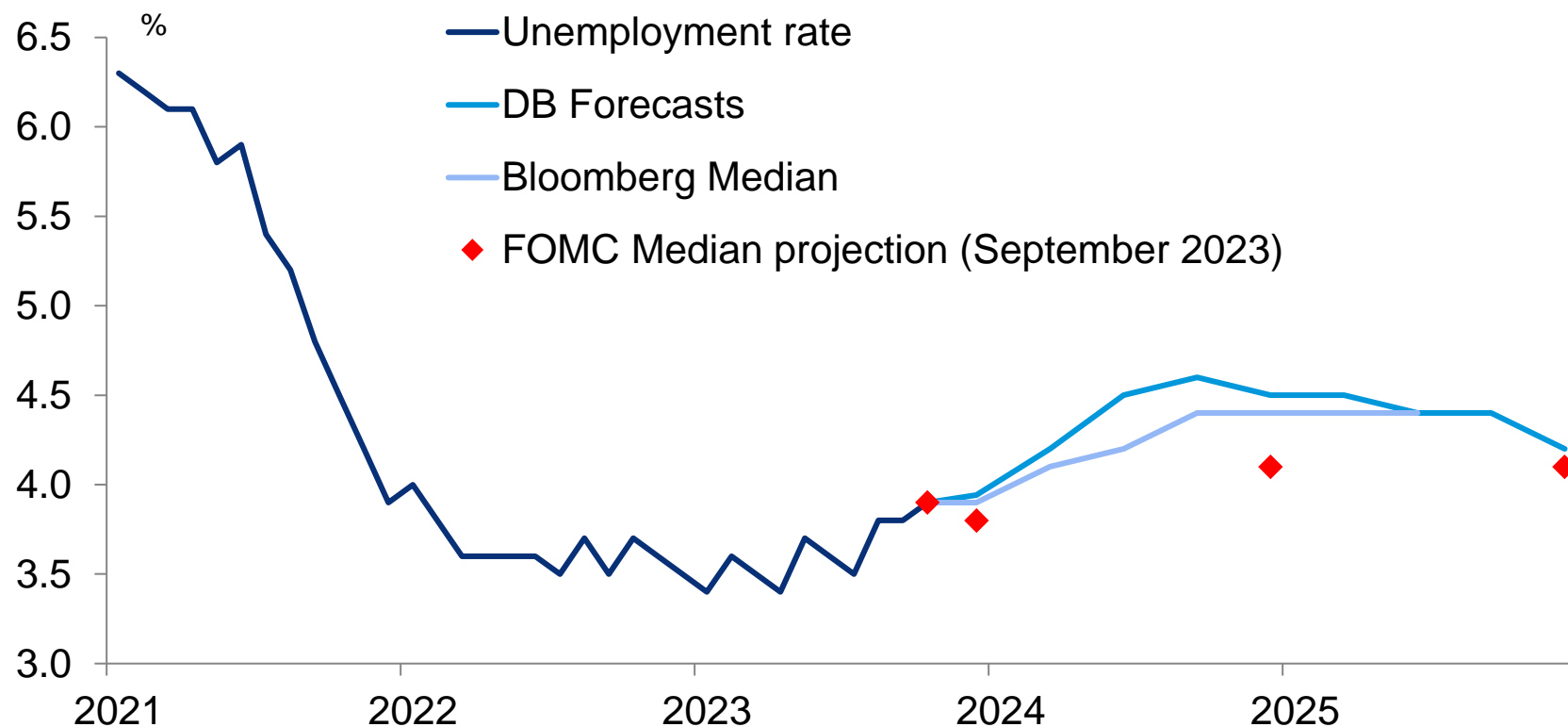


Source: Conference Board, FRBKC, Haver Analytics, Deutsche Bank



# DB unemployment rate forecast modestly above consensus and Fed

## Unemployment rate



Note: Bloomberg consensus is as of November 22, 2023.

Source: BLS, BEA, Haver Analytics, Deutsche Bank

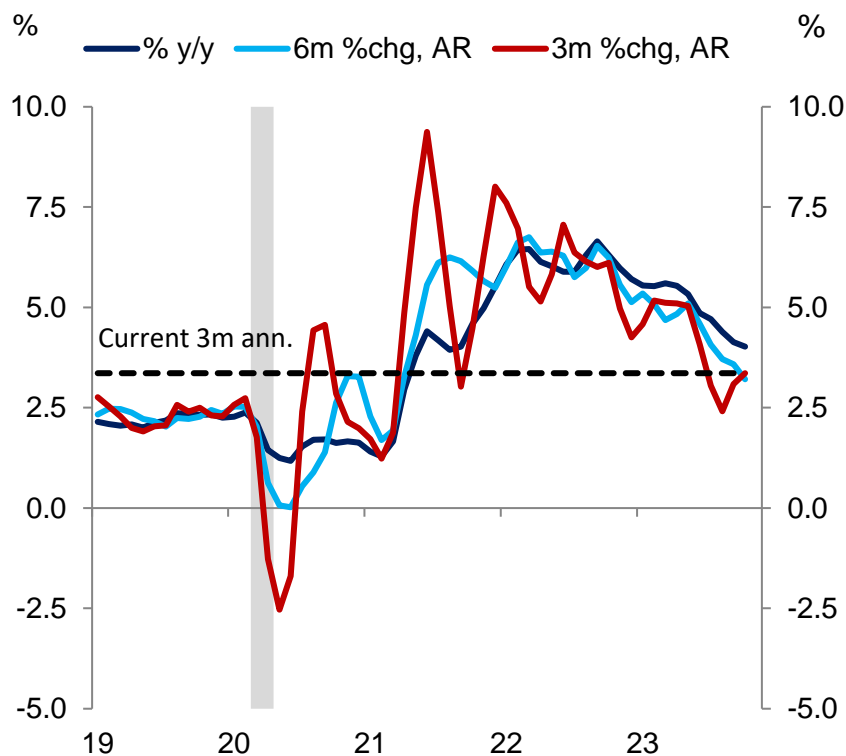


# Inflation: 3% cannot become the new 2%

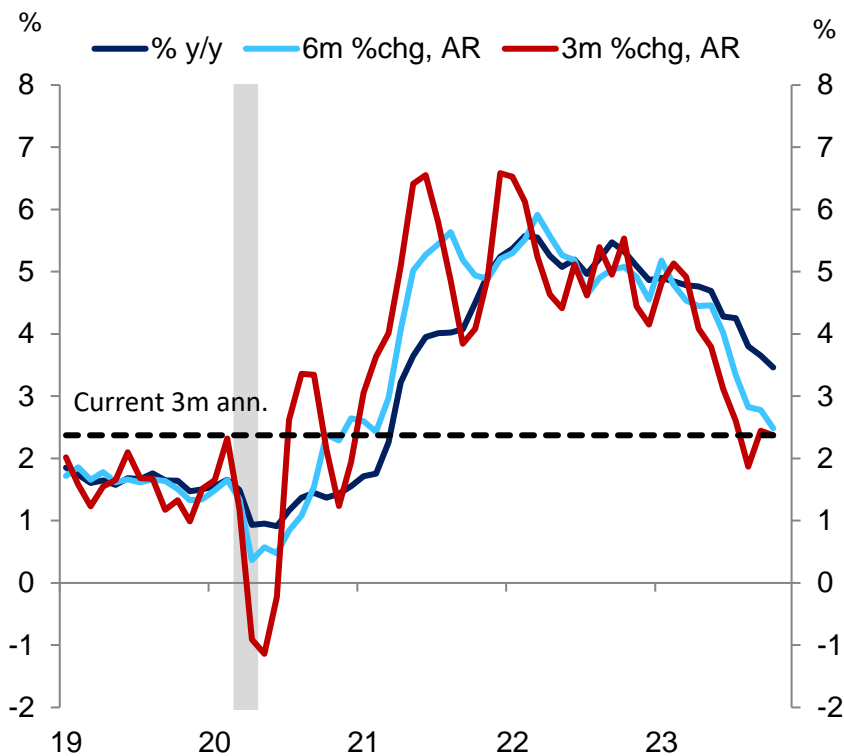


# Core inflation data have shown substantial progress in recent months

## Core CPI



## Core PCE

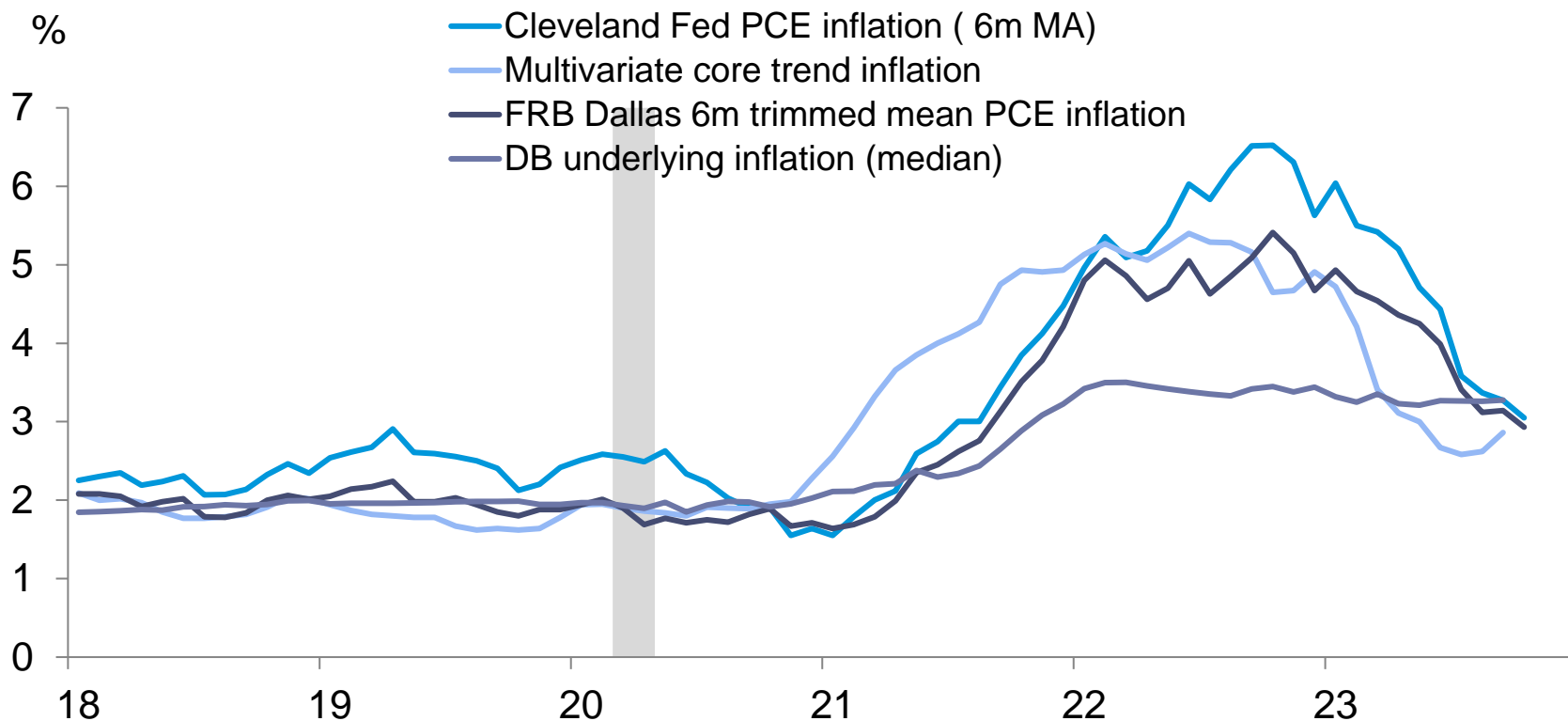


Source: BLS, BEA, Haver Analytics, Deutsche Bank



# There has been some tentative evidence the inflation trend gauges are stabilizing near 3%

## Measures of trend PCE inflation



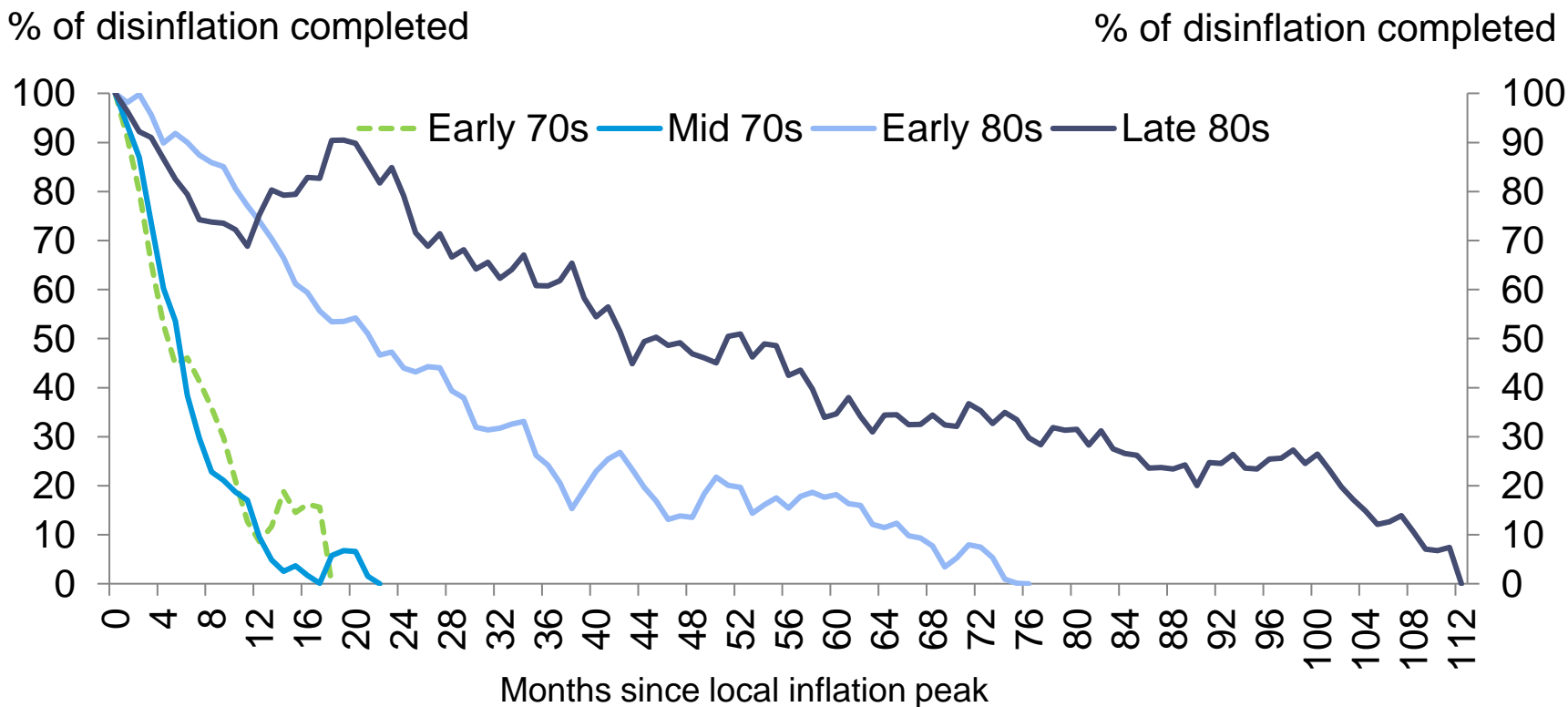
Source: FRB Dallas, FRB Cleveland, FRB New York, Haver Analytics, Deutsche Bank





# The second half of disinflation typically takes longer than the first half

## Historical disinflation episodes

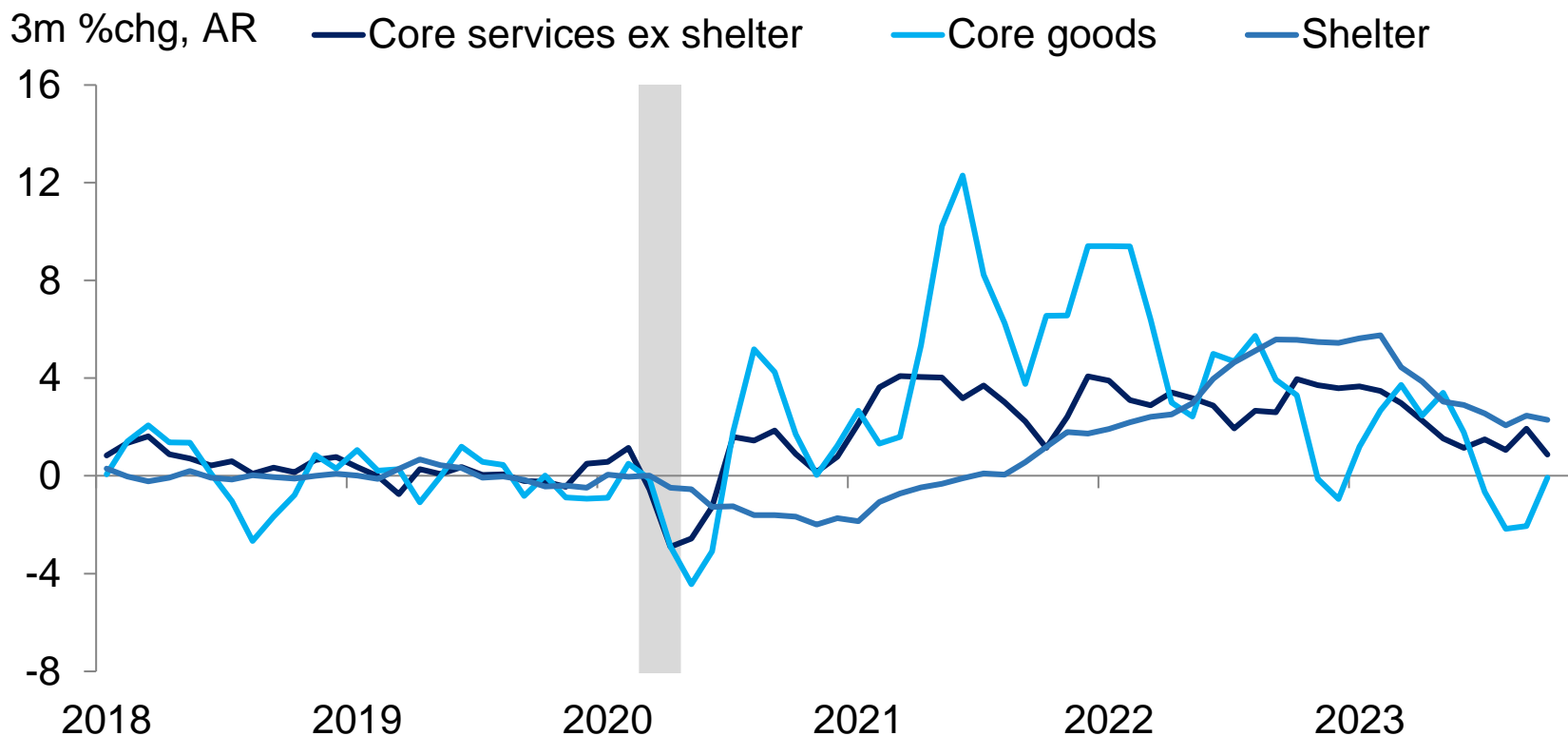


Source: BEA, Haver Analytics, Deutsche Bank



# Core inflation fits with Fed narrative: Core goods “solved”, rents should decline, super core stickier so far

## Core PCE decomposition

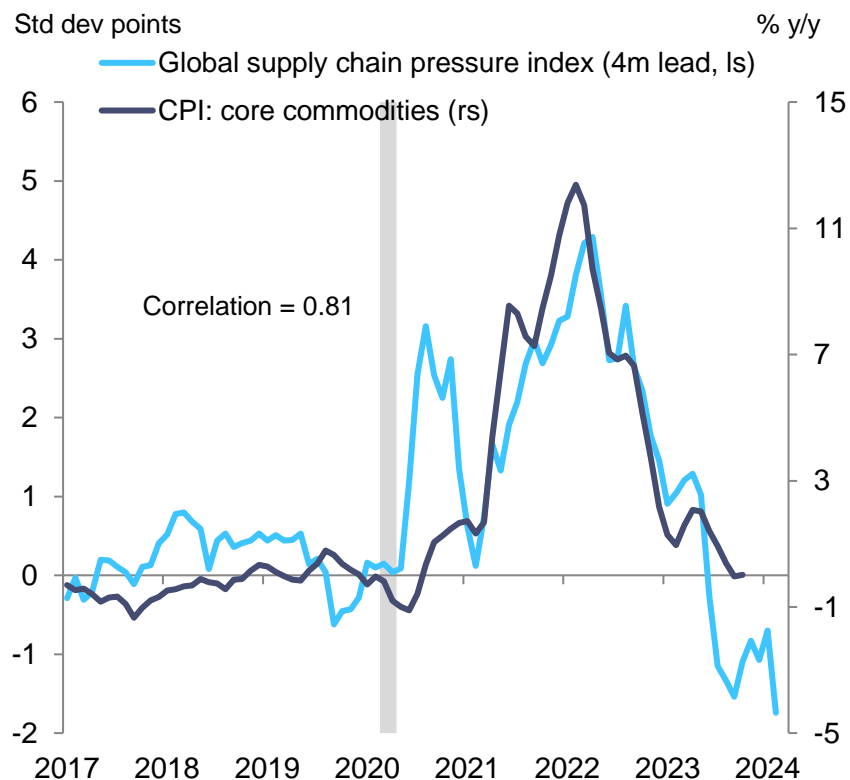


Note: All lines are differences from 2019 averages. Source: BEA, Haver Analytics, Deutsche Bank

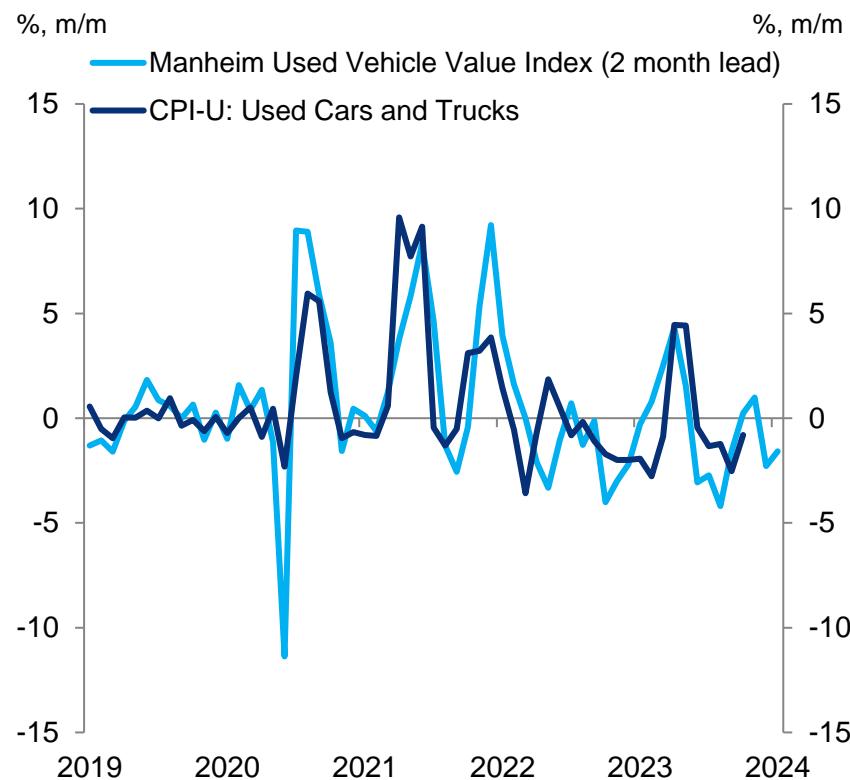


# Fading supply chain pressures suggest core goods inflation should continue to moderate

## Core goods versus supply chains



## Used car prices: Wholesale versus retail

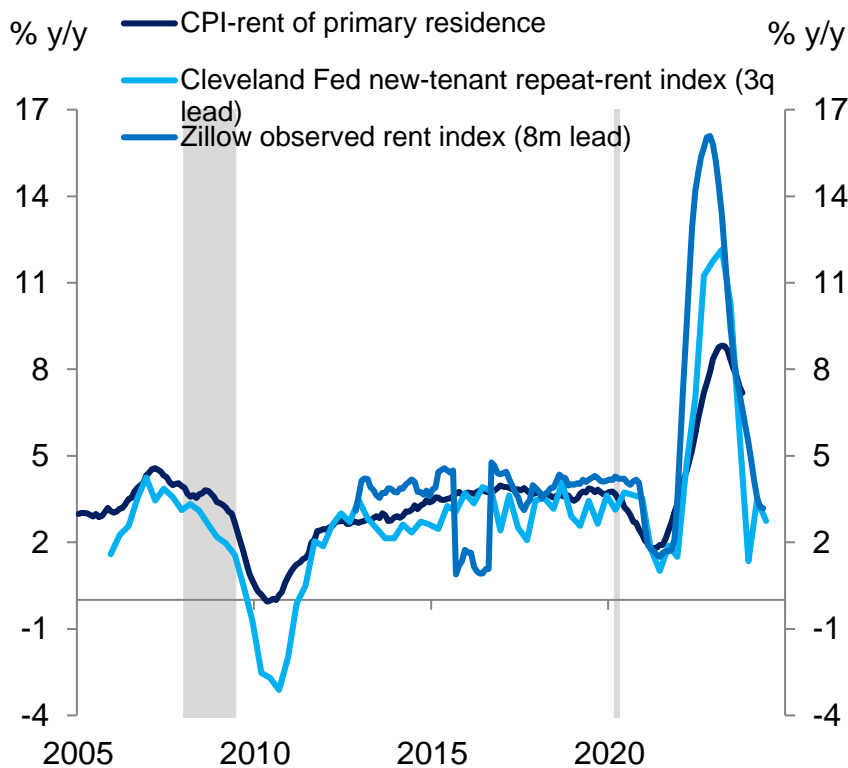


Source: FRB NY LSE, BLS, Manheim, Haver Analytics, Deutsche Bank



# Private estimates of rent suggest they should fall, super core a bit firmer

## Rent inflation



## PCE: Core services ex housing (i.e., super core)

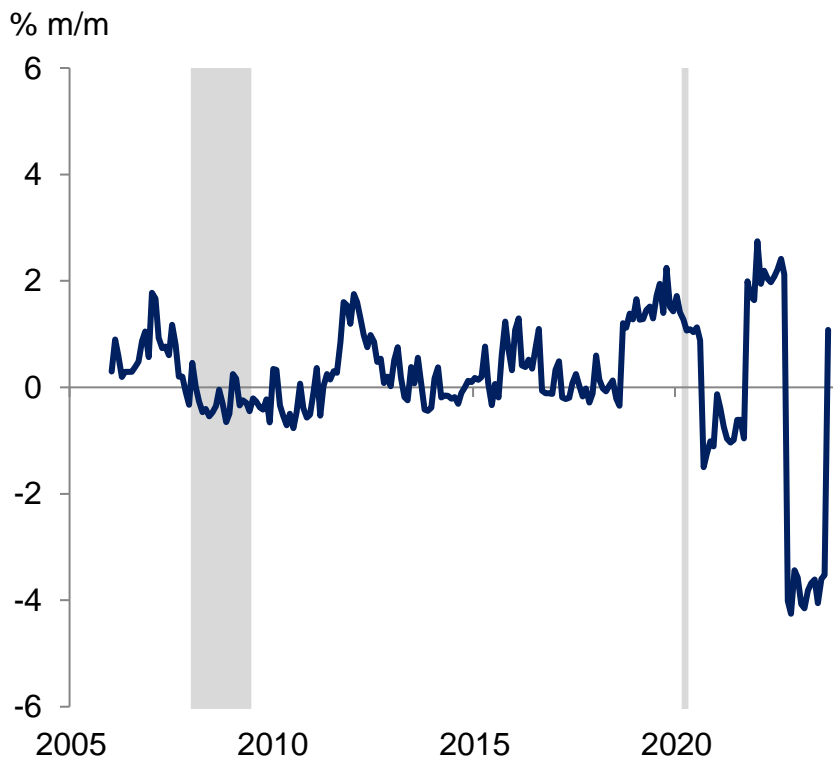


Source: BEA, BLS, Zillow, Haver Analytics, Deutsche Bank

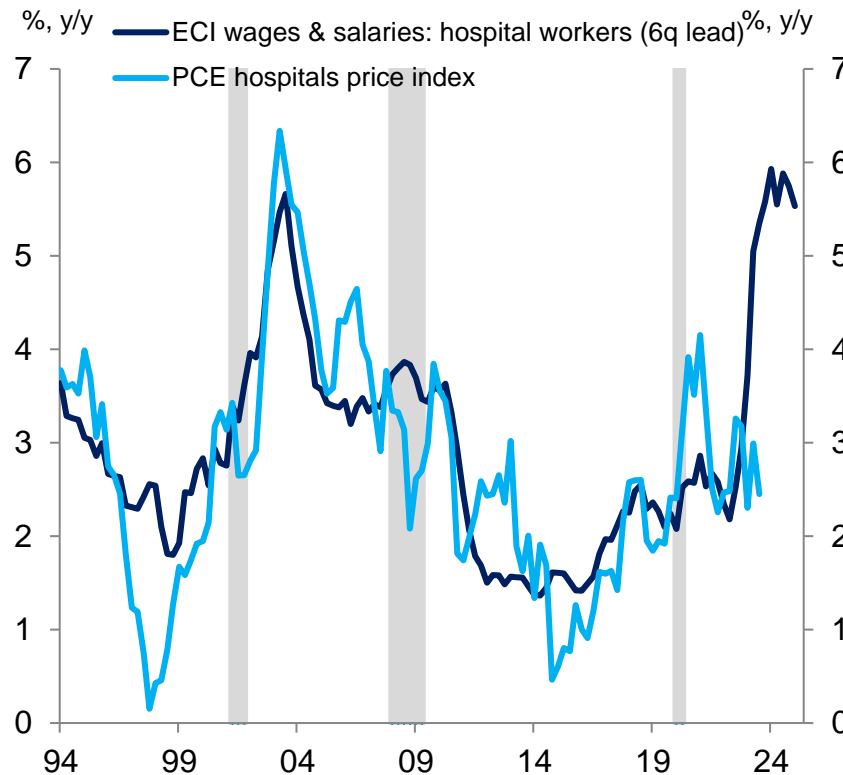


# Health insurance inflation has risen in CPI and has remaining upside in PCE

## CPI health insurance



## PCE health hospital inflation versus ECI

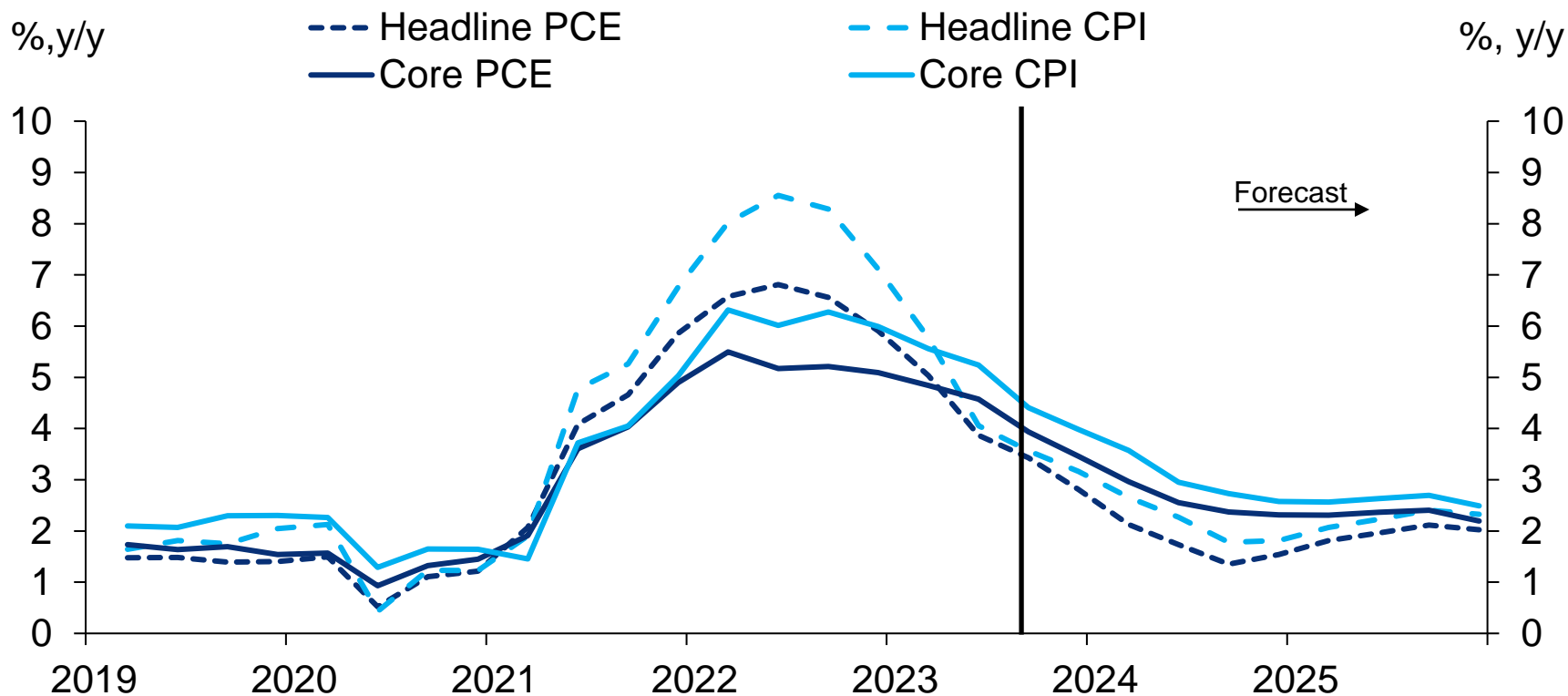


Source: BEA, BLS, Haver Analytics, Deutsche Bank



# We have inflation w/in 30bps of Fed's target in '24, enough to say they have whipped inflation now (WIN)

## DB inflation forecasts



Source: BEA, BLS, Haver Analytics, Deutsche Bank

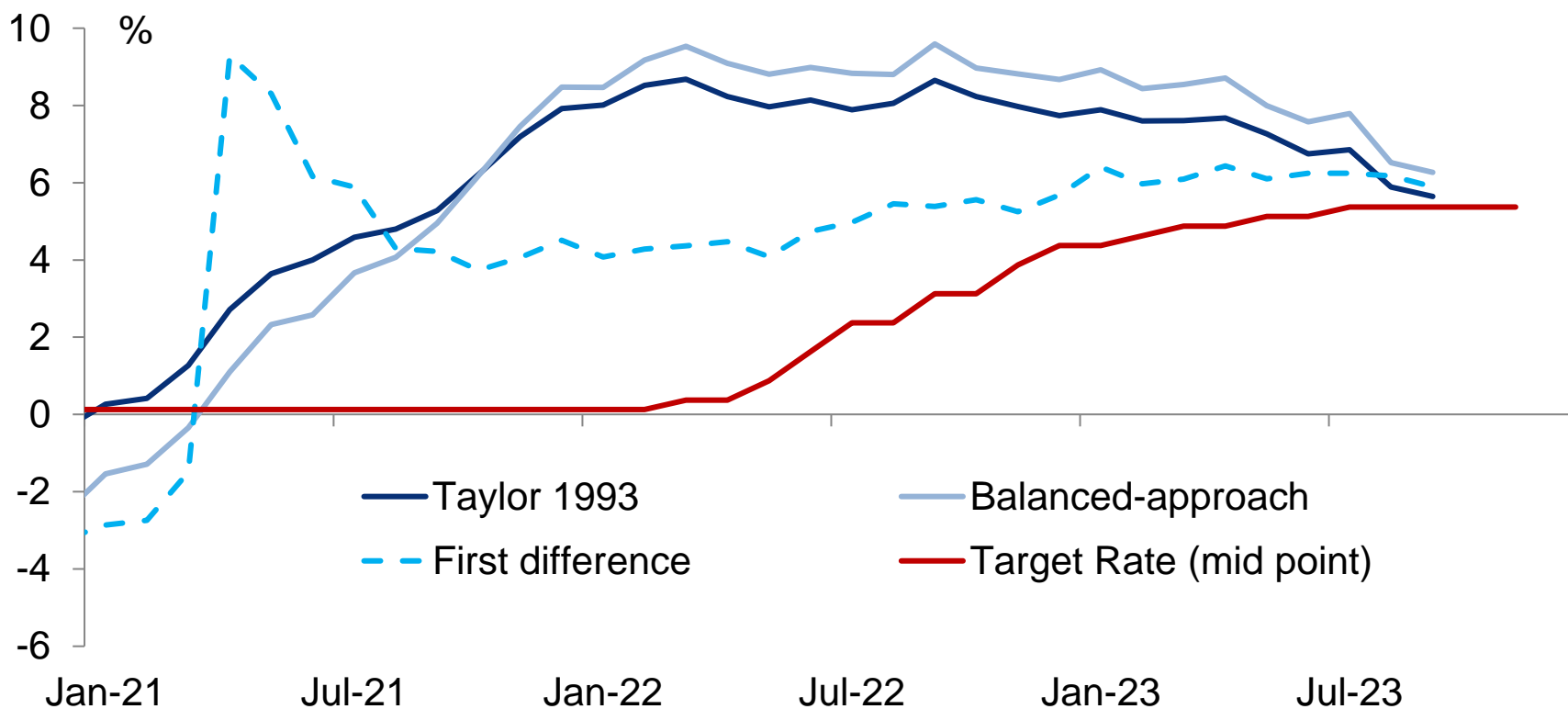


# Fed: High for not so long



# Fed funds rate approaching sufficiently restrictive zone relative to typical policy rules

## Fed funds rate versus policy rules



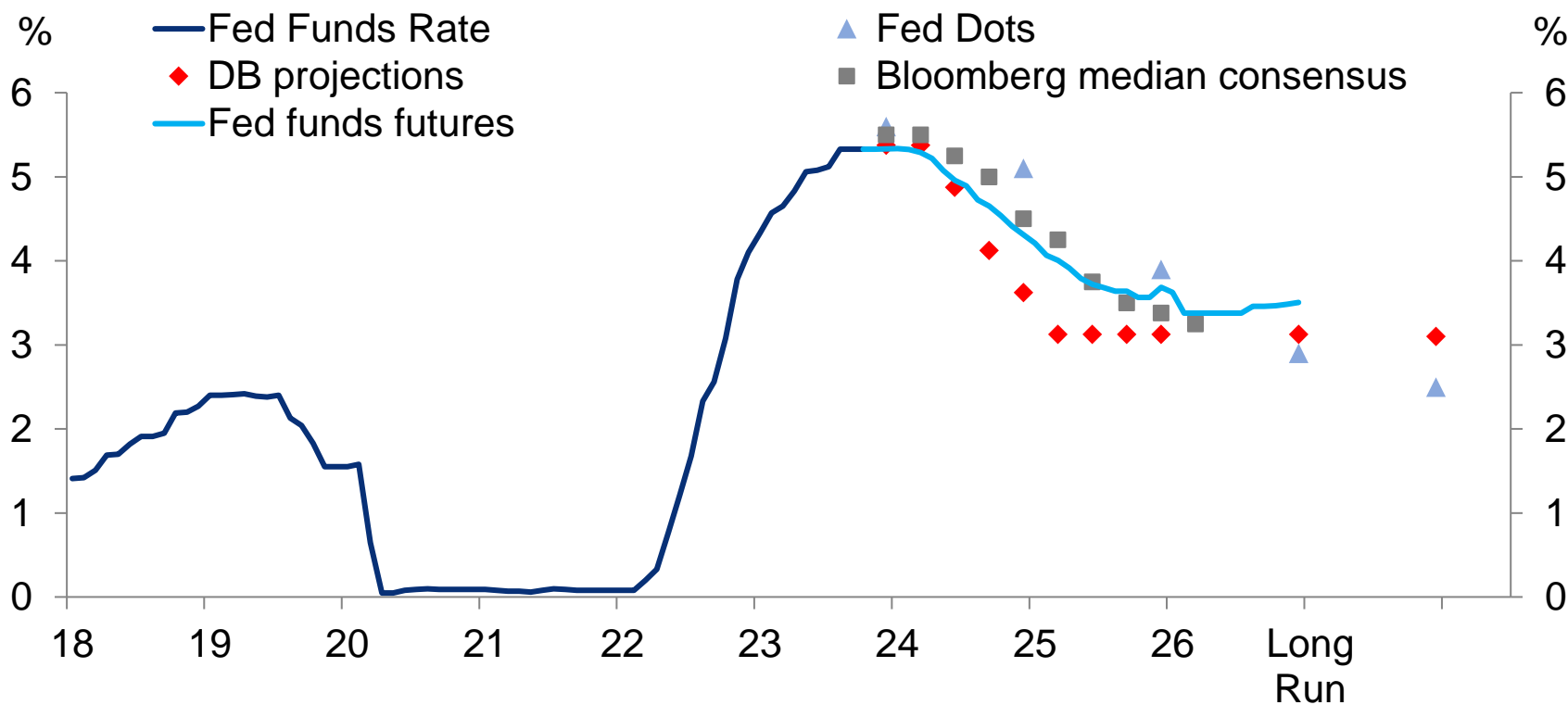
Source: FRB, Haver Analytics, Deutsche Bank





# DB continues to expect more rate cuts in 2024: First cut in June and 175bps total in '24

## Fed funds rate expectations

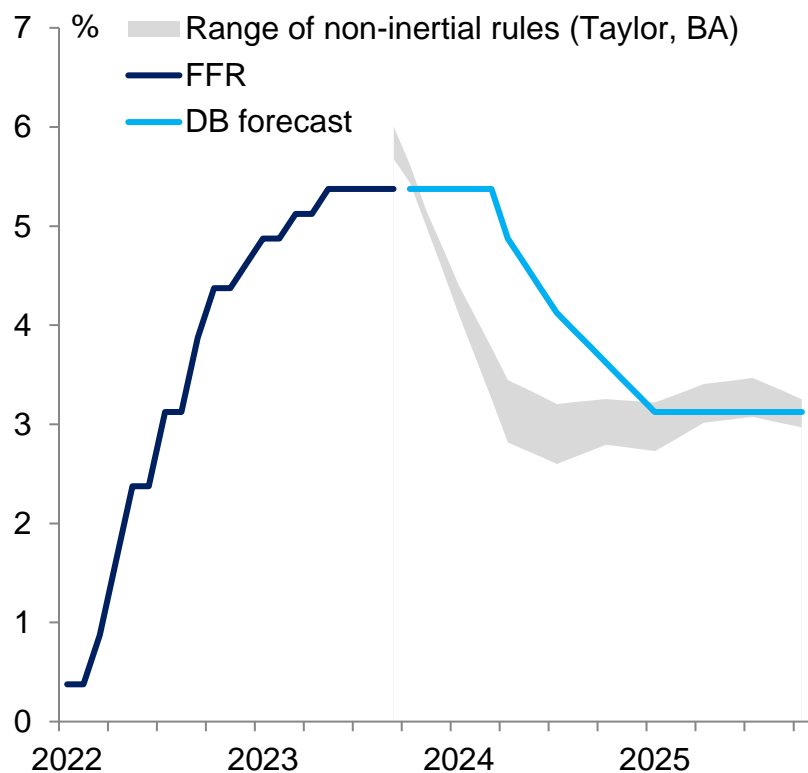


Note: Bloomberg consensus is as of November 27, 2023. : FRB, Bloomberg Finance LP, Haver Analytics, Deutsche Bank

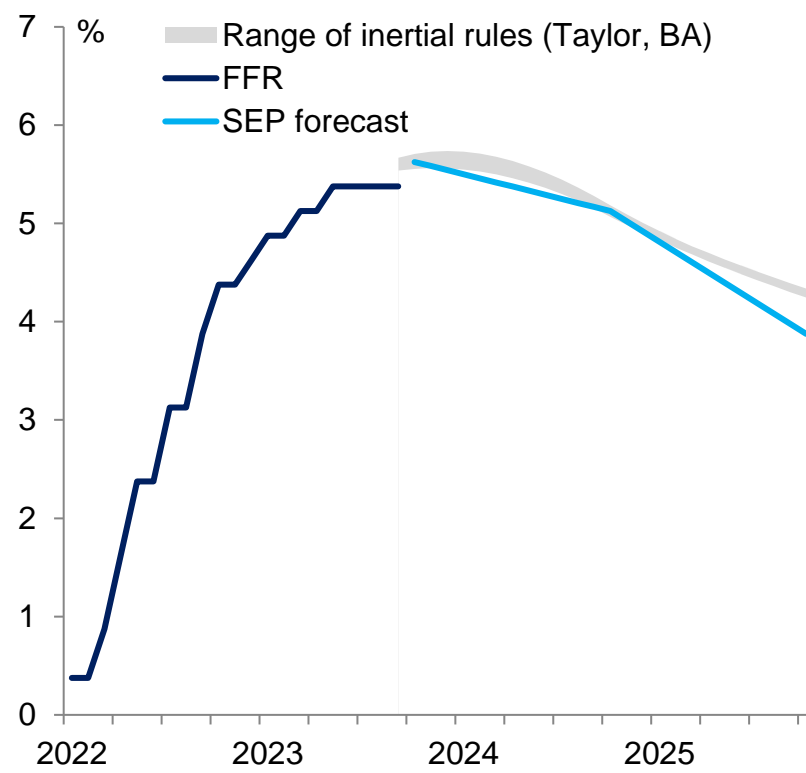


# DB view is less aggressive than (non-inertial) policy rules; Fed view in line with inertial rules

## DB forecast versus policy rules



## Fed's September SEP versus policy rules



Note: We use 1.25% for  $r^*$ , closer to our estimates than the Fed's long-run dot.

Note: We use 1.25% for  $r^*$ , closer to our estimates than the Fed's long-run dot.

Source: FRB, Haver Analytics, Deutsche Bank



# Voters remain on average neutral

<u>Permanent voting members</u>		
Jerome H. Powell, Chair	3	
Phillip N. Jefferson, VC	3	
Michael C. Barr, VC Sup.	2	
Michelle K. Bowman, Gov.	5	
Lisa D. Cook, Governor	2	
Adriana D. Kugler, Governor	3	
Christopher J. Waller, Gov.	4	
John C. Williams, New York	2	
<u>Rotating voting members</u>		
2023 Voters	2024 Voters	2025 Voters
Austan Goolsbee, Chicago	Cleveland Fed President	Austan Goolsbee, Chicago
Lori K. Logan, Dallas	Tom Barkin, Richmond	Susan M. Collins, Boston
Patrick Harker, Philadelphia	Raphael Bostic, Atlanta	St. Louis Fed
Neel Kashkari, Minneapolis	Mary C. Daly, San Francisco	Jeffrey Schmid, Kansas City
<b>Average ranking &gt; 3.0</b>	<b>Average ranking &gt; 3.0</b>	<b>Average ranking &gt; 3.0</b>

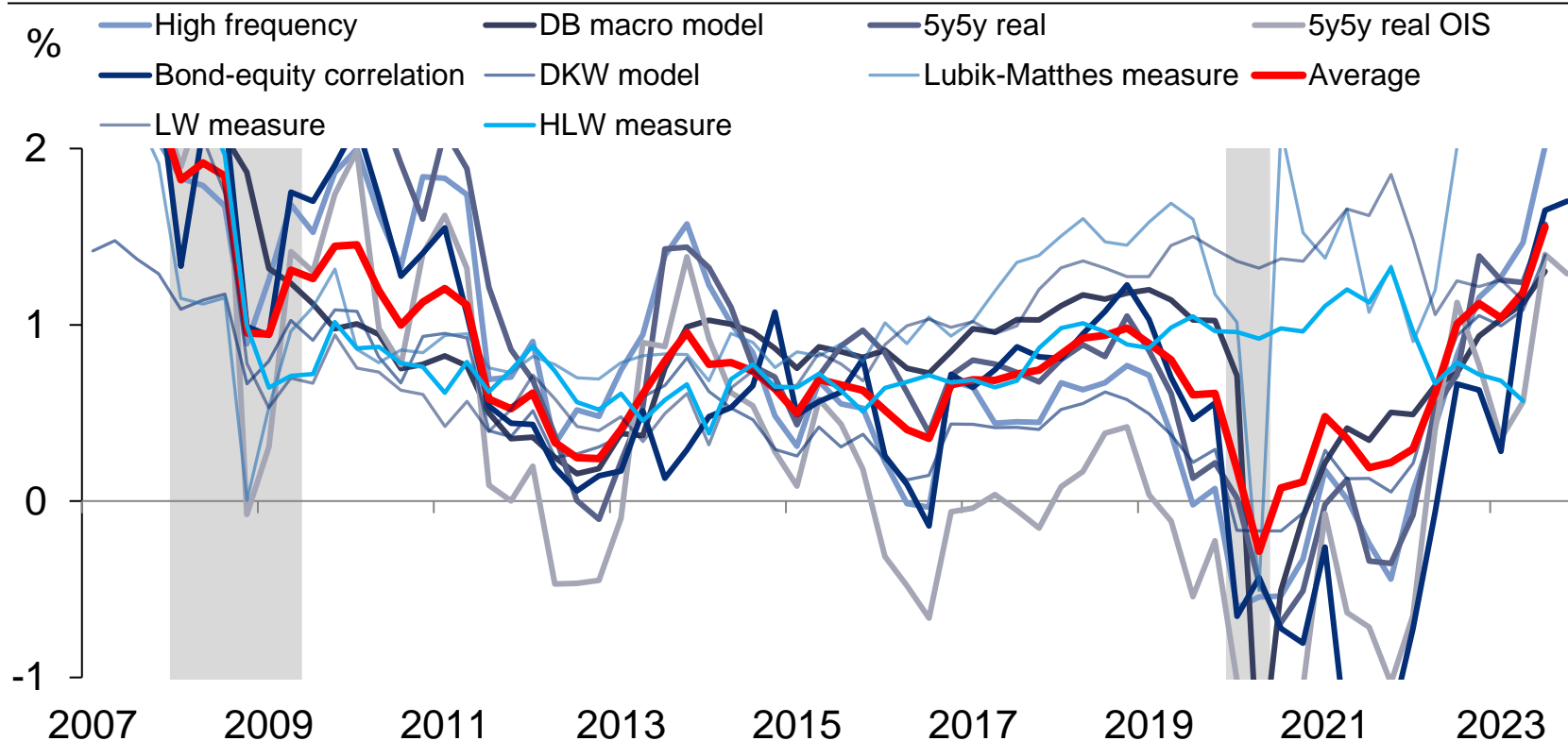
Scores: 1 = Dove, 3 = Neutral, 5 = Hawk

Source: Deutsche Bank



# A variety of measures of r-star have risen materially relative to the pre-pandemic period

## R-star measures

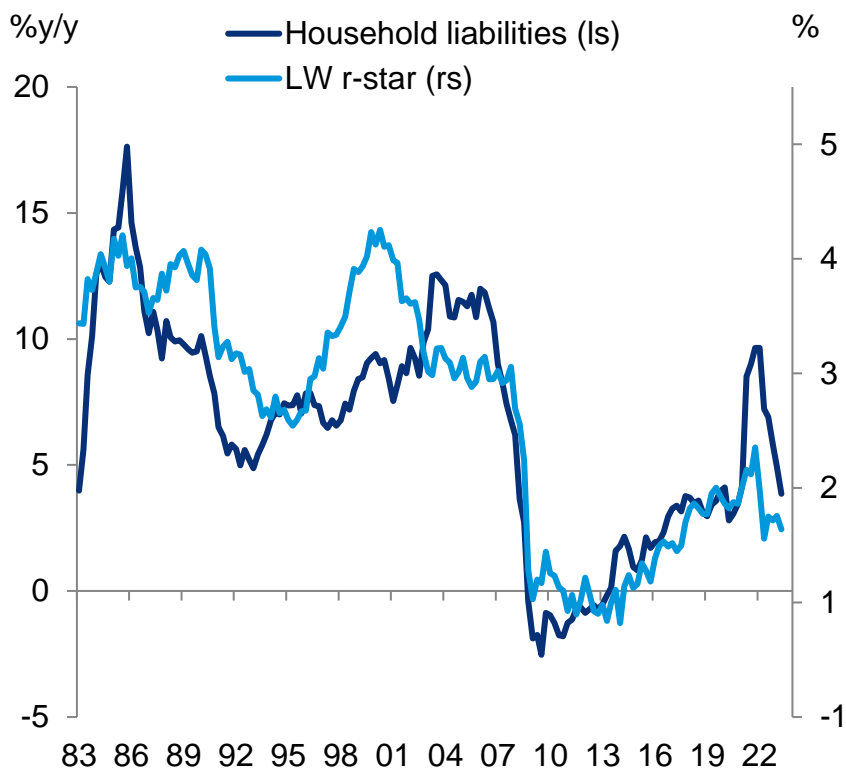


Source: FRBNY, Federal Reserve Board, Federal Reserve Bank of Richmond, Bloomberg Finance LP, Haver Analytics, Deutsche Bank

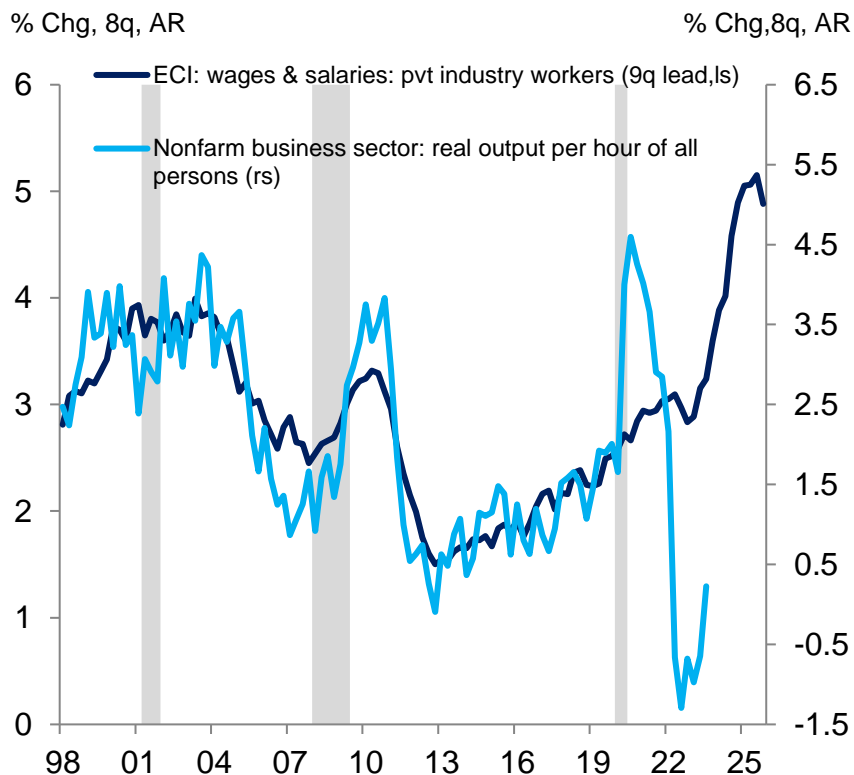


# Factors that depressed r-star changing: no need for household deleveraging and productivity has upside

## R-star versus change in HH liabilities



## Productivity growth versus wages

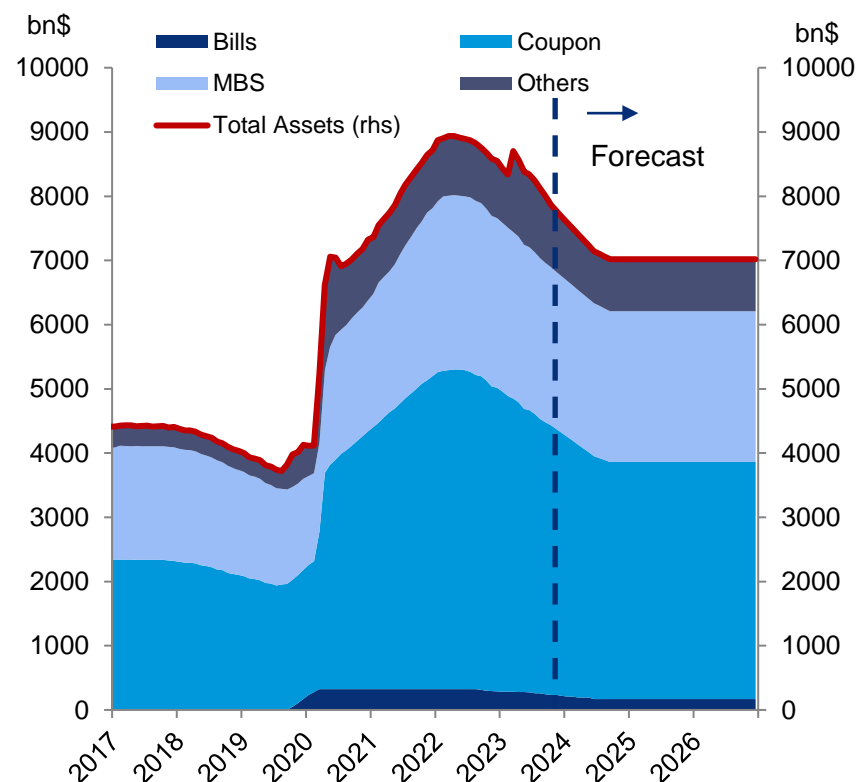


Source: FRB, FRBNY, BLS, Haver Analytics, Deutsche Bank

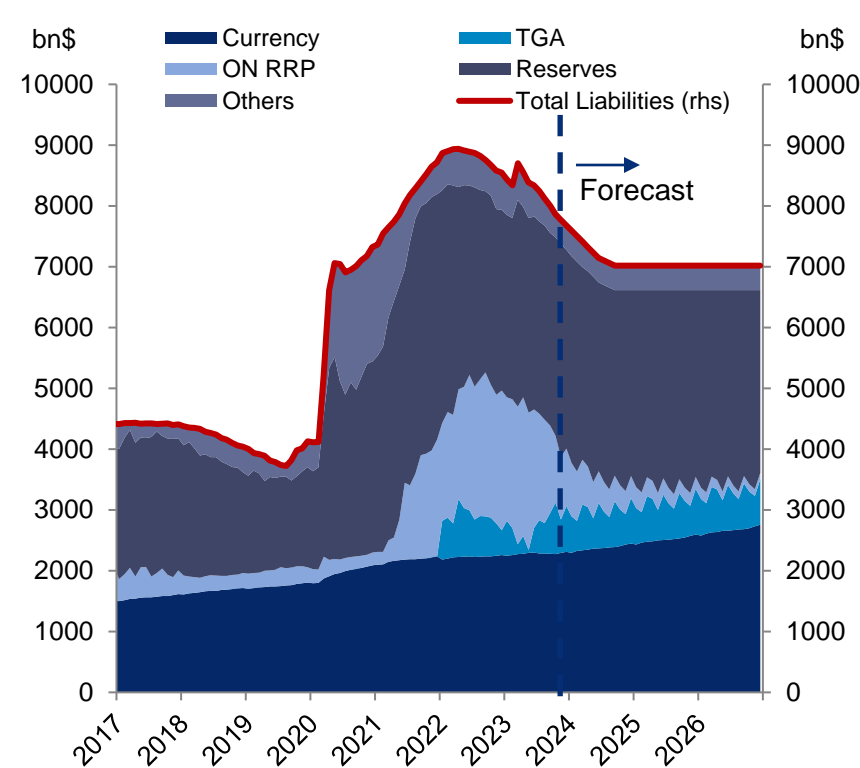


# Fed balance sheet projections: QT to end in Q3 shortly after first rate cut

## Fed assets



## Fed liabilities

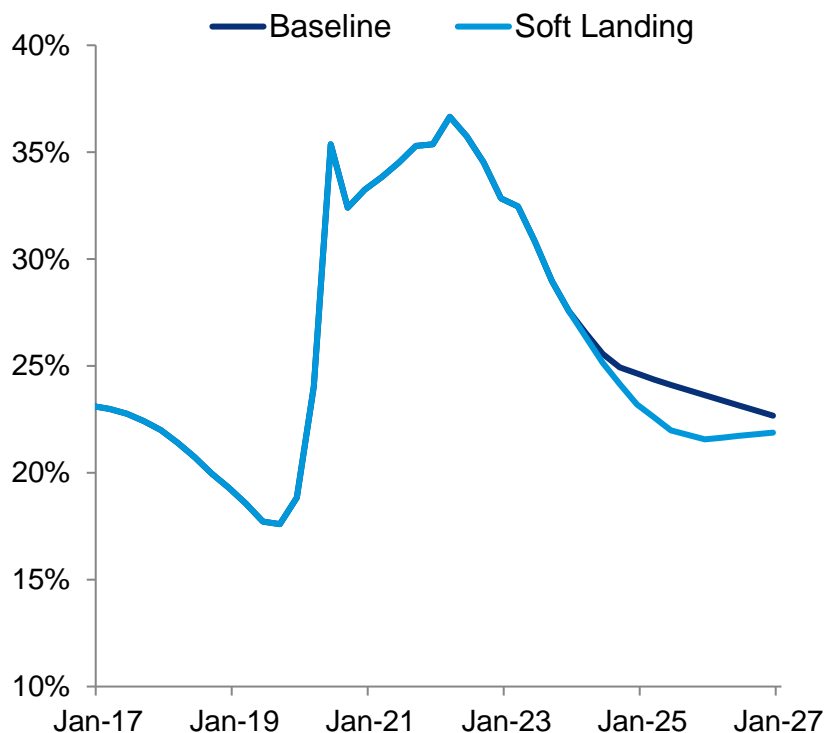


Source: FRB, Haver Analytics, Deutsche Bank

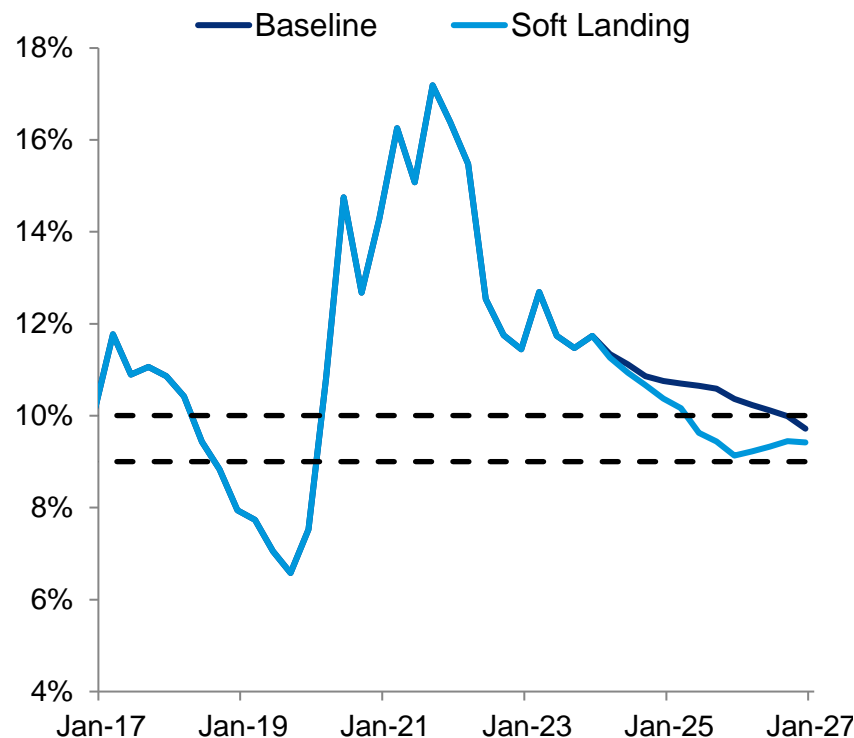


# A soft landing, in which cuts occur just to normalize policy, would mean more QT

Fed assets relative to GDP



Reserve balances relative to GDP



Note: Dashed lines in the right chart represent zone were Fed rules of thumbs have suggested they would slow and stop QT. Source: FRB, Haver Analytics, Deutsche Bank



# DB US Economic Forecast Summary

Economic Activity (% qoq, saar)	2023				2024				2025				2023F	2024F	2025F	2026F
	Q1	Q2	Q3	Q4F	Q1F	Q2F	Q3F	Q4F	Q1F	Q2F	Q3F	Q4F	Q4/Q4	Q4/Q4	Q4/Q4	Q4/Q4
GDP	2.2	2.1	5.2	0.8	-0.9	-1.7	1.0	2.7	2.5	2.0	2.0	2.1	2.5	0.3	2.1	2.0
Private consumption	3.8	0.8	3.6	2.0	-0.5	-1.9	0.6	2.3	2.4	2.3	2.2	2.1	2.5	0.1	2.2	2.3
Investment	-9.0	5.2	10.5	-3.5	-4.4	-1.9	3.0	5.7	5.4	3.4	3.4	4.4	0.5	0.5	4.1	3.3
Nonresidential	5.7	7.4	1.3	0.1	-1.7	-3.1	1.7	4.1	3.6	3.6	3.7	3.7	3.6	0.2	3.6	3.9
Residential	-5.3	-2.2	6.2	-1.1	-1.5	-0.5	2.6	2.7	2.5	2.4	2.6	2.7	-0.7	0.8	2.5	2.5
Gov't consumption	4.8	3.3	5.5	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	3.6	0.9	0.9	0.9
Exports	6.8	-9.3	6.0	2.0	3.0	1.5	3.0	3.6	3.6	3.5	3.6	3.5	1.2	2.8	3.5	3.5
Imports	1.3	-7.6	5.2	2.5	1.2	2.1	2.7	2.9	4.5	4.5	4.5	4.5	0.2	2.2	4.5	4.5
Contribution (pp): Inventories	-2.2	0.0	1.4	-0.4	-0.5	0.1	0.2	0.4	0.4	0.0	0.0	0.2	-0.4	0.0	0.2	0.0
Net trade	0.6	0.0	0.0	-0.2	0.1	-0.2	-0.1	0.0	-0.3	-0.3	-0.3	-0.3	-0.2	0.0	-0.3	-0.3
Unemployment rate, %	3.5	3.6	3.7	3.9	4.2	4.5	4.6	4.5	4.5	4.4	4.4	4.2	3.9	4.5	4.2	4.1
<b>Prices (% yoy)</b>																
CPI	5.8	4.1	3.6	3.2	2.7	2.3	1.8	1.8	2.1	2.2	2.4	2.3	3.2	1.8	2.3	2.5
Core CPI	5.6	5.2	4.4	4.0	3.6	3.0	2.7	2.6	2.6	2.6	2.7	2.5	4.0	2.6	2.5	2.4
PCE	5.0	3.9	3.4	2.8	2.2	1.8	1.4	1.5	1.8	2.0	2.1	2.0	2.8	1.5	2.0	2.1
Core PCE	4.8	4.6	3.9	3.4	2.9	2.5	2.3	2.3	2.3	2.4	2.4	2.2	3.4	2.3	2.2	2.1
Fed Funds	4.875	5.125	5.375	5.375	5.375	4.875	4.125	3.625	3.125	3.125	3.125	3.125	5.375	3.625	3.125	3.125

Source: BEA, BLS, FRB, Deutsche Bank





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# Appendix 1

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