ClearBridge
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U.S. Economic Outlook: Will U.S. Exceptionalism Continue?

2 December 2024

Key Takeaways

- A resilient U.S. economy has stood out against other developed nations in recent years as stronger economic growth and healthier corporate profits have fuelled outsize stock market gains.
- We believe that three of the four key components of exceptional relative U.S. economic growth — the consumer, productivity gains and a solid fiscal impulse — remain intact, while the fourth, growing labour supply, will likely come under pressure, though not enough to derail the expansion in 2025.
- Backed by a green and improving signal for the ClearBridge Recession Risk Dashboard, we are bullish on the U.S. economy in the year ahead and expect GDP growth to deliver an upside surprise relative to current consensus forecasts.

Trump Win, Fed Pivot to Buoy Expansion

The "most anticipated recession ever" never materialised this past year, with the U.S. economy instead achieving a soft landing. The pace of expansion is likely to stay buoyant in 2025 as the economy rides the tailwinds of both a fiscal impulse, courtesy of Donald Trump's election win and a Republican sweep of Congress, and a monetary impulse from the Federal Reserve's pivot to a rate-cutting cycle.

Over the past several years, the U.S. economy's resilience has distinguished it from other developed economies. A key question for investors is whether this trend can continue, as stronger economic gains have translated into healthy corporate profits and outsize stock market gains. Our starting point for such analysis continues to be the ClearBridge Recession Risk Dashboard, our north star when thinking about the health of the U.S. economy. Fortunately, the dashboard's overall signal is currently in green/expansionary territory, and it has been consistently improving over the course of 2024 (Exhibit 1).

We believe there have been four key components of exceptional relative U.S. economic growth over the past few years: the strength of the U.S. consumer, productivity gains, growing labour supply and a solid fiscal impulse. Looking ahead, three of these are likely to remain intact in 2025, while the fourth, growing labour supply, should be less of a benefit, but not so much less that it could derail the U.S. economy.

The U.S. consumer has been a source of strength, initially powered by accumulated savings and generous government transfer payments during the pandemic. As these funds waned, a strong labour market fuelled further upside as wage gains and broad job creation helped boost labour income, the largest single source of spending power for most Americans and closely tied to aggregate consumption trends. These trends appear largely intact as the calendar approaches 2025, with average hourly earnings holding up at a healthy growth rate of 4.0% year over year in October versus 4.3% coming into the year, for example.

Exhibit 1: ClearBridge Recession Risk Dashboard

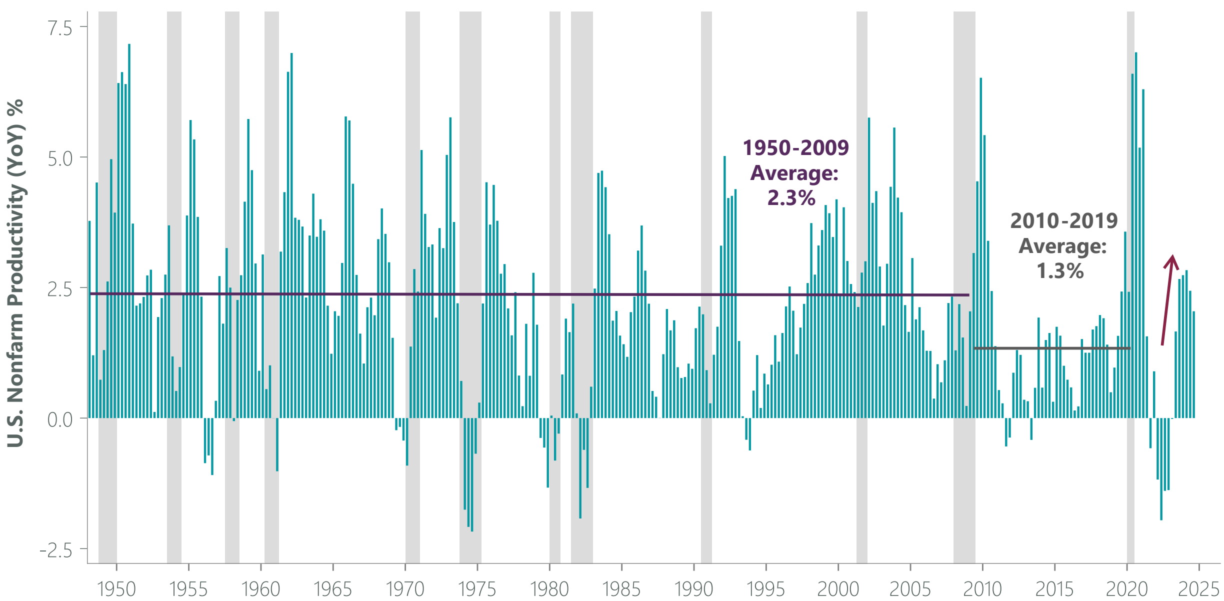
		November 30, 2024	June 30, 2024	March 31, 2024
Consumer	Housing Permits	●	●	●
	Job Sentiment	✖	✖	✖
	Jobless Claims	⬆	●	●
	Retail Sales	●	●	●
	Wage Growth	⬆	⬆	✖
Business Activity	Commodities	⬆	●	●
	ISM New Orders	✖	●	●
	Profit Margins	⬆	⬆	✖
	Truck Shipments	●	●	●
Financial	Credit Spreads	⬆	⬆	●
	Money Supply	●	●	✖
	Yield Curve	✖	✖	✖
	Overall Signal	⬆	⬆	●

⬆ Expansion ● Caution ✖ Recession

Source: ClearBridge Investments.

Sticky wage gains have been a source of concern. Some worry that corporate profit margins will be crimped as businesses have to pay their workers more. We take a different view, however, believing that wages relative to a worker's output (unit labour costs) are actually the key for profit margins. This is an important distinction because productivity gains (a worker's output) have been robust over the past several quarters, returning to levels consistent with the 1950-2009 average as opposed to the post-Global Financial Crisis experience. Looking ahead, we believe productivity will remain healthy given lower levels of job churn; if workers are changing jobs less frequently, these employees are more experienced, typically more tenured and more productive.

Exhibit 2: Productivity is Back



Sources: U.S. Bureau of Labor Statistics (BLS), NBER, and Macrobond.
Data last updated on: 7 November 2024, latest available as of 25 November 2024.
Grey shading represents recessionary periods.

Lower labour churn also means that the pace of hiring should be slower, all else equal. This means that the labour market may look less healthy than it has and raises a risk to continued U.S. exceptionalism if the strong domestic labour market cools. In fact, our primary worry on this front is less about workers staying in their roles longer and more about declining immigration, which has been a source of economic strength in recent years. Already the pace of immigration has slowed since President Biden's executive actions to secure the boarder were issued in June. President-elect Trump is expected to take actions to further slow the pace of immigration into the U.S., which should further cool the pace of job creation and weigh on economic growth at the margin in 2025.

On the positive side, the future Trump administration appears likely to deploy stimulus in the form of individual tax cuts, which should increase the fiscal impulse and help fuel economic growth. Fiscal stimulus has been a strong component of U.S. economic growth in recent years on the back of the Inflation Reduction Act and the CHIPS Act. While the fiscal impulse has begun to wane with little incremental government spending coming on-line, Trump's election and the Republican sweep open the door to using the budget reconciliation process to enact tax cuts, meaning the outlook for the fiscal impulse heading into 2025 should be positive for economic growth.

Putting all this together, we believe the U.S. economy will remain healthy in 2025 with the potential for upside to the 2.0% consensus estimate for GDP growth.

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- 19 years of investment industry experience
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