

Getting some answers from the US consumer puzzle

The US growth story remains driven by consumer resilience. High income households are in a great financial position, but those on lower incomes are feeling intensifying stress. How these competing stories play out will be key to the growth outlook for the rest of the year and the prospect of Federal Reserve interest rate cuts



How long can the spending strength of the top 20% of Americans offset everyone else?

It's all about the high-earning consumer

The remarkable resilience of the US economy to high interest rates and tight credit conditions has to be admired. But now we're starting to see signs of softening. Business surveys have weakened notably, consumer confidence is moderating, and first-quarter GDP growth was weaker than

expected, although that was mainly due to a negative contribution from inventories and net trade.

Nonetheless, inflation continues to run too hot. With three consecutive 0.4% month-on-month core CPI prints from the start of the year, the Fed is in no mood to cut interest rates imminently. The reason for the strength of the US economy remains the consumer, who accounts for 70% of GDP. The top 20% of households by income spend roughly the same dollar amount as the bottom 60%. By definition, those at the top have good incomes and probably own their own home, either outright or with a low fixed-rate mortgage. They have exposure to rising property and stock prices and have their savings in money market funds making 4-5%, so high interest rates actually benefit these households.

The question hanging in the air is how long the spending strength of the top 20% can continue to offset intensifying stresses for everyone else.

Savings are being sharply depleted

There are four ways to finance consumer spending: through income, savings (either saving less each month or running down the stock of savings), borrowing or selling assets. Real household disposable income is flat-lining and hasn't been the prime driver of consumer strength for well over a year; wage growth has slowed and inflation is eating into spending power. Instead, it is households in aggregate which have fully run down the excess savings built up during the pandemic which are keeping the momentum going.

The San Francisco Fed estimates that during Covid, excess savings maxed out at \$2.1tn in August 2021. They now stand at a negative \$72bn. We know wealthier households have continued to build savings, so this suggests that lower-income households have not only exhausted those pandemic-era savings but are likely eating into pre-existing savings, too.

Credit card spending isn't particularly sustainable

That leaves credit as the primary source for many households to be able to increase spending. But with credit card borrowing costs at all time highs and car loans at 20+ year highs, this is hardly sustainable. Indeed, delinquency rates on consumer loans are rising sharply, and Philly Fed data suggests more than 10% of households are only making the minimum payment on their credit cards as of the last quarter of last year.

If business surveys, such as the ISM employment series and the NFIB hiring intentions survey, are correct and job losses become a reality, it is difficult to see consumers as the driving force of economic growth in the second half of 2024 as they have been over the past few years. Intensifying weakness in lower-income household spending power runs the risk of offsetting what we see in those higher-income brackets.

Such an outcome will help dampen inflation pressures and, if we see the unemployment rate start to rise, both the Fed's and the market appetite for interest rate cuts will intensify. We continue to look for three interest rate cuts this year, starting at the September FOMC meeting.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user’s investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.