

Consumers Come Back Down to Earth

While recent cracks in consumer spending bear monitoring, consumers (and the fixed income sectors they help propel) are still well positioned.

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Key takeaways

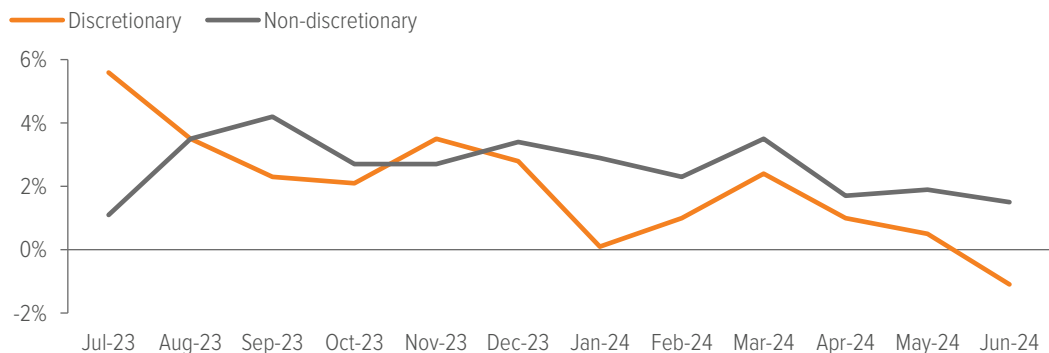
- While spending is slowing from elevated post-Covid levels, headlines suggesting a broad slowdown in U.S. consumer spending are exaggerated—historically strong labor markets, elevated real income and increased wealth from asset appreciation should continue to support consumers.
- Broadly speaking, we believe consumer spending in aggregate will continue to propel economic growth.
- However, selectivity in this environment is key as pockets of weakness are emerging—we favor investments tied to higher-income consumers and consumer staples, and are underweight investments tied to lower-income consumers and discretionary spending.

Resilient consumers have been the backbone of the current economic expansion

U.S. consumers play a crucial role in driving economic growth, historically contributing more than 60% to the country’s GDP.¹ In the wake of the Covid shutdown, consumer spending has soared. At this stage of the market cycle, any shifts in consumer behavior can have significant implications for the overall economy. Understanding the current state of U.S. consumers is vital for investors looking to gauge future economic performance and the fixed income markets influenced by consumer spending.

Exhibit 1: Discretionary spending is slowing as consumers prioritize savings and staples

Year-over-year percentage change



As of 06/30/24. Source: J.P. Morgan.

¹ Source: CEIC. From March 1947 to June 2024.

Yes, some consumer trends are showing cracks

Some signals point to a consumer slowdown, with less discretionary spending and more focus on discounts:

- Auto companies are increasingly offering incentives to stimulate purchases, signaling a potential softening in consumer demand for vehicles.
- Discount airlines are experiencing growth at the expense of legacy carriers, suggesting that consumers are prioritizing cost savings in travel expenses.
- Sales of big-ticket discretionary items are weakening, reflecting a cautious approach by consumers towards non-essential spending.

But consumers still have plenty of things going in their favor

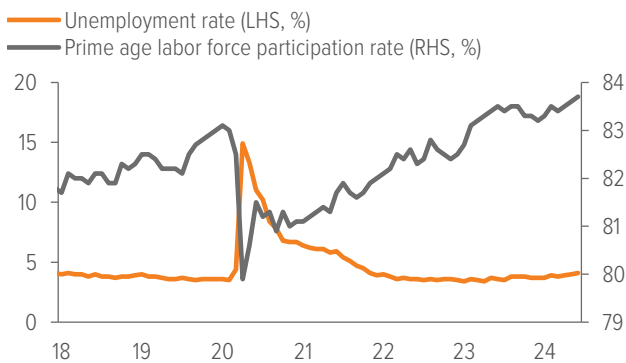
Consumers have several tailwinds at their back. Despite recent disappointing jobs data, unemployment remains low by historical standards.

Meanwhile, household balance sheets remain on sound footing, as rising stock prices and home price appreciation have increased household net worth (Exhibit 2). Furthermore, the cumulative impact of recent wage growth has led to historically high levels of income, which makes current debt levels very manageable (Exhibit 3).

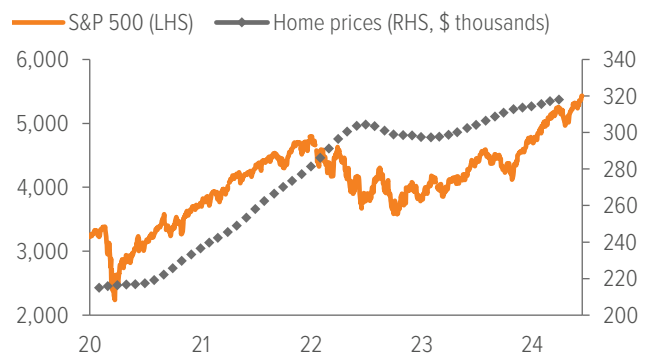
In addition to this supportive macroeconomic backdrop, recent data continue to suggest that consumers are in a position of strength. Real consumer spending ticked up in June (+2.6% year over year; +1.6% 6-month average annualized rate).² Furthermore, according to the Bureau of Economic Analysis, second-quarter GDP growth was recently revised higher amid stronger consumer spending.

Exhibit 2: Tight labor market and increased wealth support consumer spending

Labor market supportive



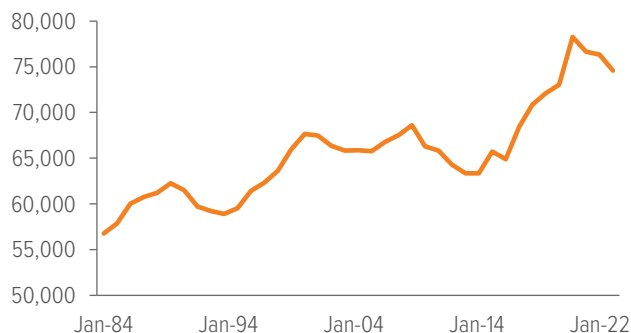
Wealth effect in play



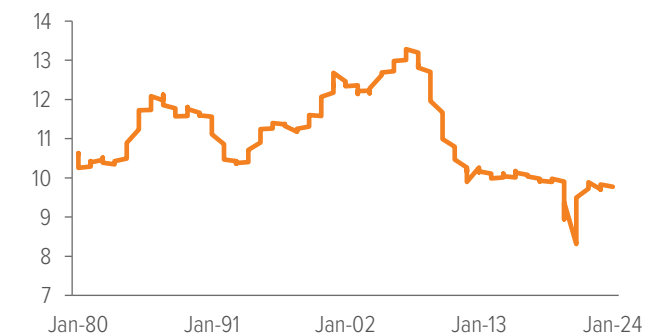
Left panel: As of 06/30/24. Source: U.S. Bureau of Labor Statistics. Right panel: As of 01/01/24. Source: Federal Reserve Bank of St. Louis.

Exhibit 3: Real income remains near all-time highs, and consumer debt is manageable

Real median household income



Debt service as a % of disposable income



Source: Federal Reserve Bank of St. Louis. Real median household income is as of 2022 census (latest available data) and debt service as a % of disposable income is as of January 1, 2024.

²Source: Goldman Sachs' U.S. Consumer Dashboard, August 2024: Resilient Spending Growth (Briggs).

Growing dispersion between high- and low-income consumers

In aggregate, consumers appear well positioned. However, there is a growing divergence between higher-income and lower-income consumer cohorts. For example, lower-income consumers have less of a buffer from the wealth effect, as households in the top 20% of the income distribution accounted for around 68% of total household assets and 71% of net worth as of March 31, 2024.³ This dispersion between consumers is also manifesting in auto loans, where delinquency rates for subprime loans are starting to increase and outpace delinquencies for prime loans.

³Source: Bank of America, "Consumer Checkpoint" Getaways and Giveaways: July 11, 2024.

Fixed income implications

- While any significant cracks in the labor market or consumer incomes would exacerbate the burgeoning slowdown in consumer spending trends, as long as these markets remain strong by historical standards, we believe the outlook for the U.S. consumer is positive.
- As a silver lining for broader risk assets, the backdrop of resilient but slowing economic growth, combined with cooling inflation, gives the Fed more space to cut rates.
- We currently favor investments tied to higher-income consumers, as lower-income borrowers are more likely to feel the strain of stalling economic growth and less likely to benefit from the buffer of higher stock and home prices.
- For corporate bonds, we favor investments that are less tied to discretionary spending and generate more of their revenue through the sales of essential consumer goods.

A note about risk

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