WEEKLY COMMENTARY

Does Credit Still Pose Risks to the US Economy?

By Francis Généreux, Principal Economist

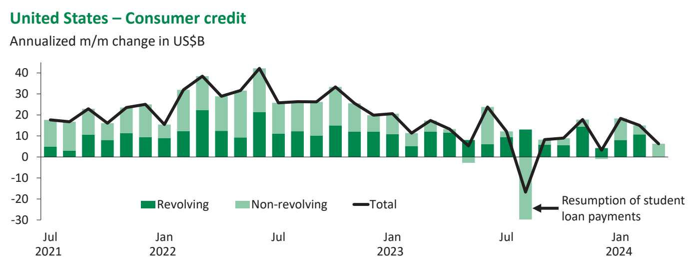
Real GDP growth slowed in the first quarter of 2024, compared to the rapid expansion seen in the second half of 2023. The US economy is nevertheless still booming, as reflected by buoyant domestic demand, which climbed by an annualized 2.8% in the first quarter. This was partly due to quarterly growth in real spending on services, which was the strongest it's been since 2014 (except for upticks due to the end of lockdowns). Even April hiring, which was down slightly from previous months, isn't that much of a concern.

A number of factors explain the resilience of domestic demand and household consumption. One is rising salaries. The wealth effect—amplified by soaring stock indexes, higher interest income and rising home prices—has also boosted consumer spending. The substantial surplus savings consumers built up during the pandemic also allowed them to keep spending. But researchers at the San Francisco Fed believe pandemic-era savings have now been spent, leaving households with less of a cushion against economic uncertainty. They point out that "consumers could use debt—such as credit cards and personal loans—to further support their current spending habits, although the current elevated interest rate environment means that the cost of using credit is higher than in the decade preceding the pandemic recession."

Of course, credit could prove useful for consumers who want to spend more than they currently earn. The last few days have seen the release of fresh data on changes in consumer credit, as well as attitudes to credit on the part of financial institutions, households and businesses.

First, compared to 2022, consumer credit growth has significantly cooled since the fall of 2023 (graph 1). That's no surprise, as that's generally what happens when interest rates go up. Until February, the slowdown was most obvious in term loans. However, the monthly gain in revolving credit (cards and lines of credit) was particularly low in March. It remains to be seen whether this recent soft patch is just a passing phase or the sign of a lasting trend toward weaker growth.

Graph 1
Consumer Credit Has Cooled



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A key factor in how the credit market develops over the coming months will obviously be the interest rate trajectory. The recent lack of progress on inflation should prompt caution among Federal Reserve (Fed) officials at their next few meetings. The upcoming elections will likely limit what the Fed can do, since it probably won't want to pivot on interest rates in the midst of the election campaign unless it's absolutely necessary. We therefore don't expect the central bank to begin monetary easing until November. Higher-for-longer rates should keep a lid on credit in the US, and possibly here in Canada as well, even though the Bank of Canada will likely start cutting rates soon.

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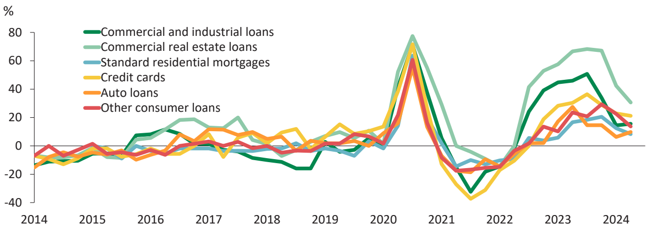
NOTE TO READERS: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.

Obviously, interest rate movements are key, but the willingness of financial institutions to extend credit is nevertheless an important factor. Once again, this week we got new information to chew on with the publication of the Fed's quarterly Senior Loan Officer Opinion Survey.

What stands out the most is that financial institutions haven't relaxed their credit conditions for most types of loans to individuals or businesses. But there's a smaller share of institutions that keep tightening their conditions (graph 2). Institutions continue to see weak demand for credit (graph 3),

Graph 2
Financial Institutions Keep Tightening Credit Conditions, but Not As Much as Last Year
United States – Net share of financial institutions that are tightening loan conditions*



The graph doesn't show all loan types, particularly mortgages.
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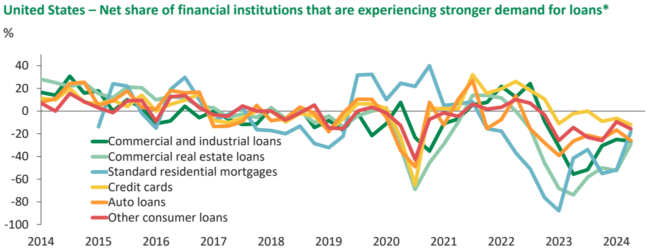
which is to be expected as long as market interest rates remain high. At least the situation isn't getting worse.
That said, there are still quite a few risks. Late payments on

Graph 3
Demand for Loans Is Still Slowing, but Not As Much as in 2023

United States – Net share of financial institutions that are experiencing stronger demand for loans*



The graph doesn't show all loan types, particularly mortgages.
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credit cards and—to a lesser extent—car loans are mounting. The situation seems relatively under control for late payments on student loans and mortgages, while personal bankruptcies are currently at a historic low in the United States. A faltering job market and persistently higher unemployment could nevertheless worsen the situation.

Although this isn't our baseline scenario, sticky or even rising inflation that would force the Fed to start hiking rates again also poses major risk. This would drive market and retail rates back up. Until now, the economy has shown surprising resilience in the face of high rates. But a further tightening of financial conditions could be the straw that breaks the camel's back and triggers the downturn that the United States has managed to avoid. This could disrupt a soft landing.

These factors suggest that the credit trajectory isn't cause for major concern, at least for now. However, as long as interest rates stay relatively high, risks remain for the US economy.

What to Watch For

UNITED STATES

WEDNESDAY May 15 - 8:30	
April	**m/m**
Consensus	0.4%
Desjardins	0.4%
March	**0.4%**

Consumer Price Index (April) – Inflation numbers were disappointing once again in March. The annual change in the consumer price index (CPI) rose from 3.2% to 3.5%, reaching its highest level since September 2023. Although the increase was partially attributable to a base effect, recent price fluctuations also played a major role, particularly in services excluding food, energy and shelter, one of the measures the Federal Reserve monitors closely. We expect the month-over-month change for April to be 0.4%, as it was in March. Energy prices will likely contribute positively, especially since gas prices pushed higher last month. We expect food prices to edge up by a modest 0.1%. Core CPI is expected to rise 0.3%, which would be a slight improvement over the three consecutive monthly gains of 0.4% recorded in January, February and March. We still expect to see a significant discrepancy between goods and services prices. Total annual inflation will likely decrease from 3.5% to 3.4%, with core inflation ticking down from 3.8% to 3.7%.

WEDNESDAY May 15 - 8:30	
April	**m/m**
Consensus	0.4%
Desjardins	0.7%
March	**0.7%**

Retail sales (April) – Retail sales were up 0.7% in March, and while this was a pretty good showing, it wasn't as impressive as the 1.0% improvement recorded the month prior. We expect that retail sales rose another 0.7% in April. Total sales were likely bolstered by motor vehicle sales and stronger gas station sales. Preliminary card transaction data is fairly positive for the other sectors, especially for furniture stores, building materials stores and restaurants.

THURSDAY May 16 - 8:30	
April	**ann. rate**
Consensus	1,435,000
Desjardins	1,425,000
March	**1,321,000**

New housing starts (April) – Housing starts are back to being volatile. After falling 12.2% in January, activity surged 12.7% in February before plummeting 14.7% in March. This was the steepest drop since February 2015, if we exclude the first few months of the pandemic. At just 1,321,000 annualized units, the March rate was the lowest since August 2023. However, we think the April numbers will already show an upturn. Housing starts should align more closely with the rate of building permits issued, which averaged 1,493,000 units in the first three months of 2024. This is supported by the fact that the number of people employed in residential construction increased in April. Another positive sign is that builder confidence has improved since the end of 2023.

THURSDAY May 16 - 8:30	
April	**m/m**
Consensus	0.2%
Desjardins	-0.2%
March	**0.4%**

Industrial production (April) – Industrial production recorded two consecutive increases of 0.4% in February and March. But the drivers behind this growth were very different from one month to the other. Energy production was very weak in February, but it partially rebounded in March. Meanwhile, manufacturing growth was much stronger in February than in the month that followed. Manufacturing output may have dipped in April, as suggested by the reduction in hours worked and the decline in the ISM index. We also expect that mining activity slowed while energy production increased slightly. Total industrial production likely dipped 0.2%.

FRIDAY May 17 - 8:30	
April	**m/m**
Consensus	-0.3%
Desjardins	-0.3%
March	**-0.3%**

Leading indicator (April) – Although the leading indicator finally broke its 23-month streak of declines by posting a 0.2% improvement in February, the celebration was short-lived. By March, the leading indicator had already pulled back 0.3%. We expect a similar result for the month of April, with the key detractors being consumer confidence, the ISM index and interest rate spreads.

CANADA

WEDNESDAY May 15 - 8:15	
April	**ann. rate**
Consensus	240,000
Desjardins	236,000
March	**242,200**

Housing starts (April) – We anticipate a further retreat in housing starts for April, likely falling to 236k from about 242k in the previous month. The market is facing multiple headwinds, including high borrowing costs and a shortage of skilled labour. Homebuilder sentiment also continues to be gloomy in both the single- and multi-family housing markets—unsurprising, given recent news reports of construction projects being paused or cancelled. We expect housing starts in 2024 to lag well behind last year's performance.

WEDNESDAY May 15 - 9:00

April	m/m
Consensus	n/a
Desjardins	-1.2%
March	**0.5%**

Existing home sales (April) – We're projecting a 1.2% decline in national home sales for April. Early figures from local real estate boards indicated small declines in month-over-month sales in Toronto and Calgary, while Vancouver sales have edged slightly higher since March. In contrast, sales in Edmonton were up sharply from the previous month, with purchases still well above pre-pandemic levels there and in Calgary. New listings have outpaced sales in both Toronto and Vancouver, a trend we'll continue to monitor closely. The declining sales-to-new-listings ratio suggests that we might see price pressures easing soon.

OVERSEAS

WEDNESDAY May 15 - 19:50

Q1 2024	q/q
Consensus	-0.4%
Q4 2023	**0.1%**

Japan: Real GDP (first quarter) – The Japanese economy didn't show much vim and vigour in the second half of 2023. After falling 0.8% on a non-annualized basis in the summer of 2022, Japan's real GDP regained a mere 0.1% over the fall. We'd be surprised if it managed to push higher in the first three months of 2024, with a decline seeming more plausible. Retail sales stayed flat during the quarter, while industrial production, housing starts and real exports fell.

THURSDAY May 16 - 22:00

China: Industrial production and retail sales (April) – The Chinese economy performed relatively well in the first quarter of 2024, with real GDP growing 5.3% year-over-year (1.6% non-annualized quarter-over-quarter change). We'll be watching industrial production and retail sales data for initial indications on how well the country's economy is faring in the second quarter. China's PMI indexes improved in April, suggesting solid growth. This would be good news for retail sales, which fell short of expectations in March by increasing just 3.1% over the same month in the previous year.

Economic Indicators

Week of May 13 to 17, 2024

Date	Time	Indicator	Period	Consensus	Desjardins	Previous reading
UNITED STATES						
MONDAY 13	9:00	Speech by Federal Reserve Bank of Cleveland President L. Mester				
TUESDAY 14	8:30	Producer price index				
		Total (m/m)	April	0.3%	0.2%	0.2%
		Excluding food and energy (m/m)	April	0.2%	0.2%	0.2%
	10:00	Speech by Federal Reserve Chair J. Powell				
WEDNESDAY 15	8:30	Consumer price index				
		Total (m/m)	April	0.4%	0.4%	0.4%
		Excluding food and energy (m/m)	April	0.3%	0.3%	0.4%
		Total (y/y)	April	3.4%	3.4%	3.5%
		Excluding food and energy (y/y)	April	3.6%	3.7%	3.8%
	8:30	Empire State Manufacturing Index	May	-10.3	-5.0	-14.3
	8:30	Retail sales				
		Total (m/m)	April	0.4%	0.7%	0.7%
		Excluding automobiles (m/m)	April	0.2%	0.7%	1.1%
	10:00	NAHB housing market index	May	51	n/a	51
	10:00	Business inventories (m/m)	March	0.0%	-0.1%	0.4%
	16:00	Net foreign securities purchases (US$B)	March	n/a	n/a	71.5
THURSDAY 16	8:30	Initial unemployment claims	May 6–10	219,000	219,000	231,000
	8:30	Philadelphia Fed index	April	7.8	5.0	15.5
	8:30	Housing starts (ann. rate)	April	1,435,000	1,425,000	1,321,000
	8:30	Building permits (ann. rate)	April	1,490,000	1,475,000	1,467,000
	8:30	Export prices (m/m)	April	0.2%	0.3%	0.3%
	8:30	Import prices (m/m)	April	0.2%	0.3%	0.4%
	9:15	Industrial production (m/m)	April	0.2%	-0.2%	0.4%
	9:15	Production capacity utilization rate	April	78.4%	78.1%	78.4%
	12:00	Speech by Federal Reserve Bank of Cleveland President L. Mester				
FRIDAY 17	10:00	Leading indicator (m/m)	April	-0.3%	-0.3%	-0.3%
CANADA						
MONDAY 13	8:30	Building permits (m/m)	March	-5.0%	-3.5%	9.3 %
TUESDAY 14	8:30	Wholesale sales (m/m)	March	-1.3%	-1.0%	0.0%
WEDNESDAY 15	8:15	Housing starts (ann. rate)	April	240,000	236,000	242,200
	8:30	Manufacturing sales (m/m)	March	-2.8%	-1.0%	0.7 %
	9:00	Existing home sales (m/m)	April	n/a	-1.2%	0.5 %
THURSDAY 16	---	---				
FRIDAY 17	8:30	International securities transactions ($B)	March	n/a	n/a	-8.78

NOTE: Each week, Desjardins Economic Studies takes part in the Bloomberg survey for Canada and the United States. Approximately 15 economists are consulted for the Canadian survey and a hundred or so for the United States. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Following the quarter, the abbreviations f, s and t correspond to first estimate, second estimate and third estimate respectively. Times shown are Eastern Daylight Time (GMT - 4 hours). Desjardins Economic Studies forecast.

Economic Indicators

Week of May 13 to 17, 2024

Country	Time	Indicator	Period	Consensus m/m (q/q)	Consensus y/y	Previous reading m/m (q/q)	Previous reading y/y
OVERSEAS							
MONDAY 13							
Germany	---	Compte courant (G€)	March	n/a		29.8	
Japan	19:50	Producer price index	April	0.3%	0.8%	0.2%	0.8%
TUESDAY 14							
United Kingdom	2:00	ILO unemployment rate	March	4.3%		4.2%	
Germany	2:00	Consumer price index – final	April	0.5%	2.2%	0.5%	2.2%
Germany	5:00	ZEW Current Conditions Survey	May	-76.3		-79.2	
Germany	5:00	ZEW Expectations Survey	May	45.8		42.9	
WEDNESDAY 15							
France	2:45	Consumer price index – final	April	0.5%	2.2%	0.5%	2.2%
Eurozone	5:00	Net change in employment – preliminary	Q1	n/a	n/a	0.3%	1.2%
Eurozone	5:00	Real GDP – preliminary	Q1	0.3%	0.4%	0.3%	0.4%
Eurozone	5:00	Industrial production	March	0.2%	-2.3%	0.8%	-6.4%
Japan	19:50	Real GDP – preliminary	Q1	-0.4%		0.1%	
THURSDAY 16							
Japan	0:30	Industrial production – final	March	n/a	n/a	3.8%	-6.7%
Italy	5:00	Trade balance (€M)	March	n/a		6,034	
China	22:00	Retail sales	April		3.7%		3.1%
China	22:00	Industrial production	April		5.5%		4.5%
FRIDAY 17							
France	1:30	ILO unemployment rate	Q1	7.5%		7.5%	
Eurozone	5:00	Consumer price index – final	April	0.6%	2.4%	0.6%	2.4%

NOTE: Unlike release times for US and Canadian economic data, release times for overseas economic data are approximate. Publication dates are provided for information only. The abbreviations m/m, q/q and y/y correspond to month-over-month, quarter-over-quarter and year-over-year change respectively. Times shown are Eastern Daylight Time (GMT - 4 hours).