4th Quarter 2024

Data as of October 1, 2024

Nationwide Market Insights℠

Our perspective on the market and economic forces influencing investment planning and retirement

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Nationwide Market Insights℠

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Executive Summary

Markets have been on a wild ride recently as investors recalibrate their expectations in a normalizing economy and amid greater recession concerns. We think the economy remains relatively solid and continue to forecast a soft landing. However, we should be vigilant for downside risks since the labor market is moderating and some consumers are overextended. We think risk assets will hold their ground as investors try to decide whether a soft landing or a hard landing is in store.

A cooler economy should lead inflation to ease, but there could be bumps along the way to the Federal Reserve's two percent objective. Fed policymakers embarked on their long-awaited easing cycle last month with a large 50 basis point rate cut. With inflation no longer posing a major threat and risks to employment rising, we anticipate a string of rate cuts over the coming months.

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Financial Markets

Highlights

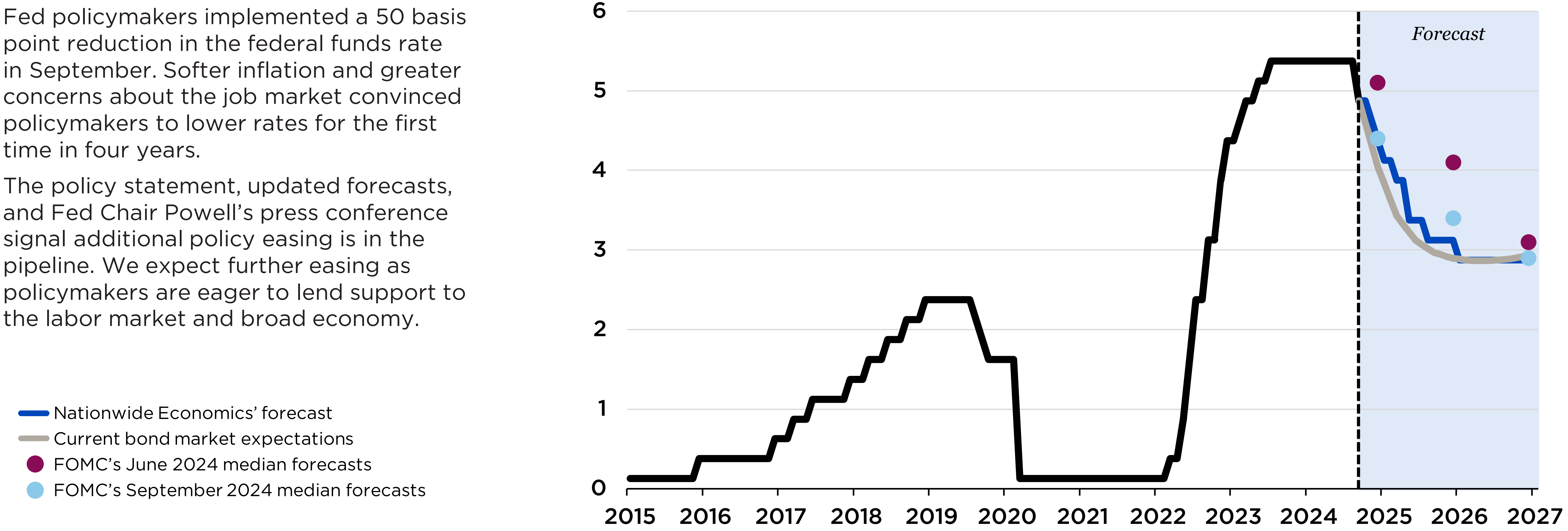
Fed cuts rates and more easing is ahead

Fed policymakers implemented a 50 basis point reduction in the federal funds rate in September. Softer inflation and greater concerns about the job market convinced policymakers to lower rates for the first time in four years.

The policy statement, updated forecasts, and Fed Chair Powell's press conference signal additional policy easing is in the pipeline. We expect further easing as policymakers are eager to lend support to the labor market and broad economy.

Federal funds rate

Percent



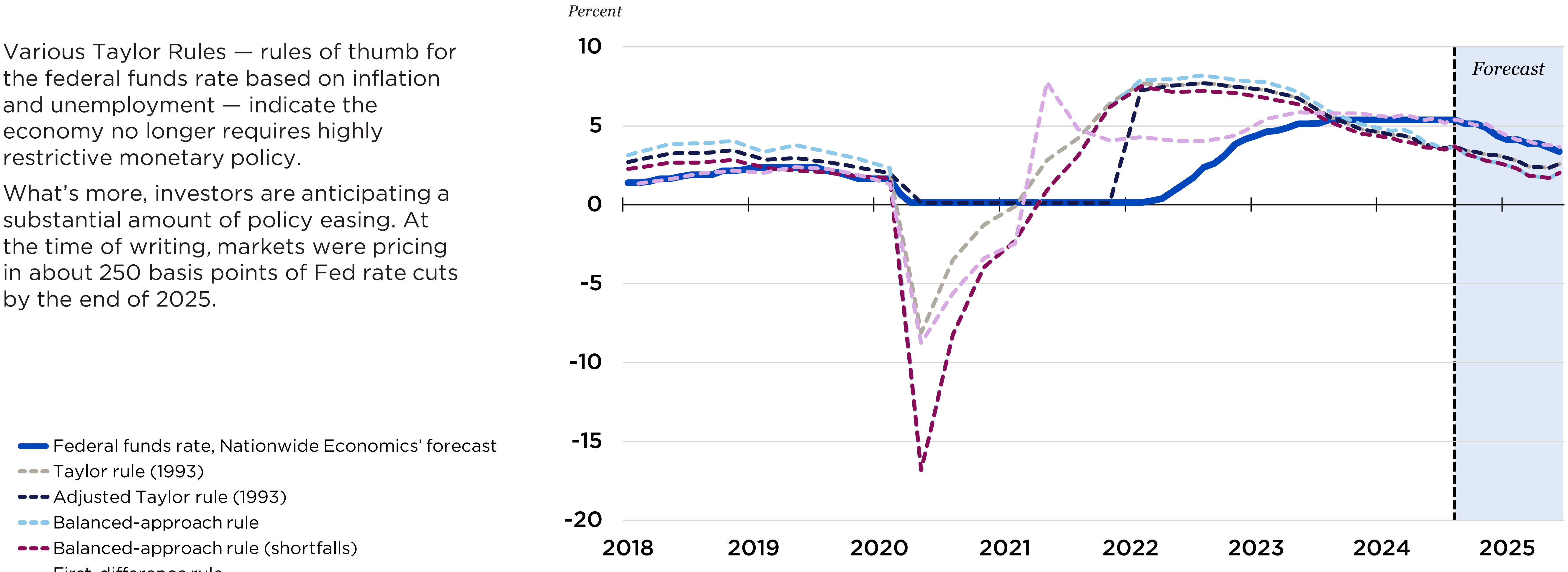
Source: Federal Reserve, Bloomberg, CME, SOFR Futures Data, Nationwide Economics

Taylor Rules suggest Fed is at risk of falling behind the curve

Various Taylor Rules — rules of thumb for the federal funds rate based on inflation and unemployment — indicate the economy no longer requires highly restrictive monetary policy.

What's more, investors are anticipating a substantial amount of policy easing. At the time of writing, markets were pricing in about 250 basis points of Fed rate cuts by the end of 2025.

Historical federal funds rate prescriptions from simple policy rules



Note: Future estimates calculated using Nationwide Economics' baseline forecast

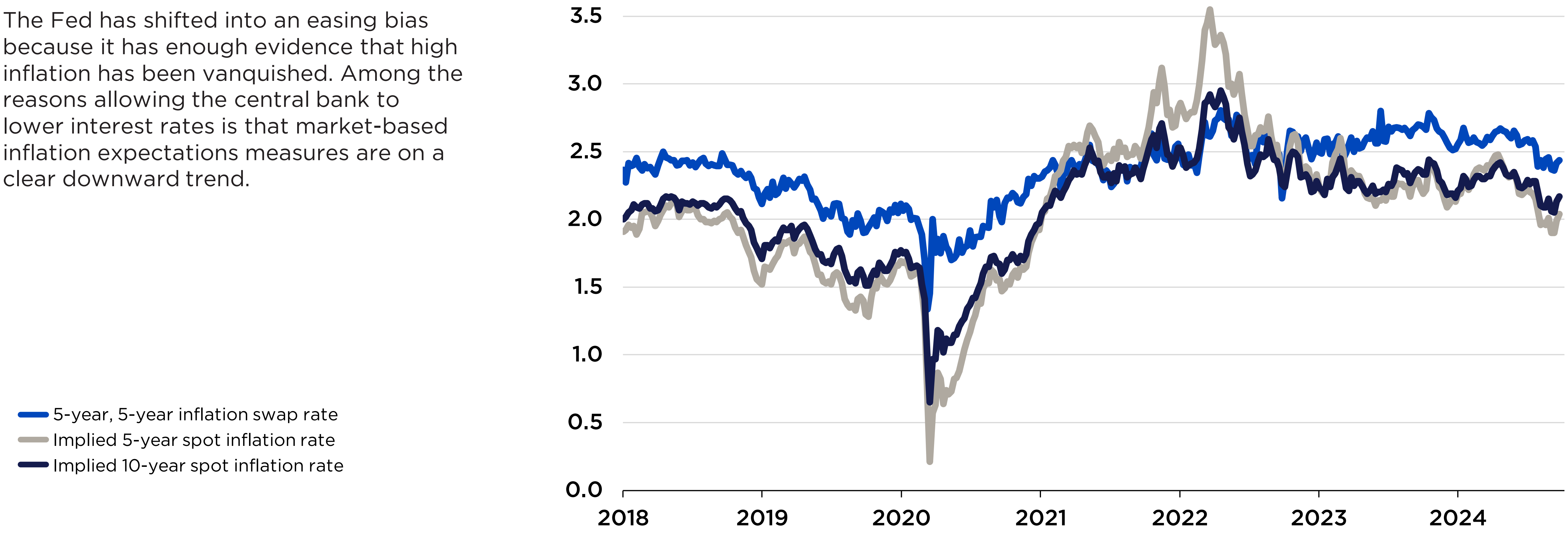
Source: Federal Reserve Bank of New York; Survey of Primary Dealers; Federal Reserve Bank of St. Louis, Federal Reserve Economic Data, DFEDTARL and DFEDTARU; Federal Reserve Board staff estimates, Nationwide Economics

Inflation expectations are easing

The Fed has shifted into an easing bias because it has enough evidence that high inflation has been vanquished. Among the reasons allowing the central bank to lower interest rates is that market-based inflation expectations measures are on a clear downward trend.

Market-based measures of inflation expectations

Percent



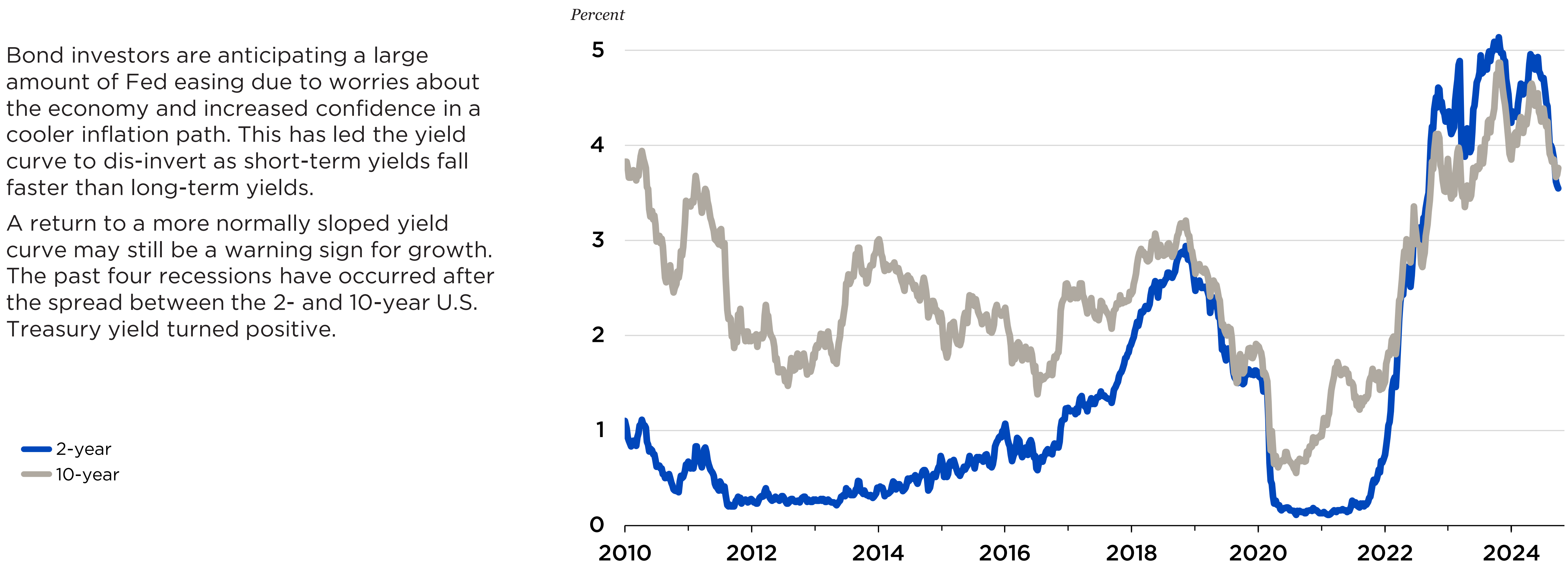
Source: Federal Reserve, Bloomberg, Haver Analytics, Nationwide Economics

Treasury yield curve dis-inverts

Bond investors are anticipating a large amount of Fed easing due to worries about the economy and increased confidence in a cooler inflation path. This has led the yield curve to dis-invert as short-term yields fall faster than long-term yields.

A return to a more normally sloped yield curve may still be a warning sign for growth. The past four recessions have occurred after the spread between the 2- and 10-year U.S. Treasury yield turned positive.

2-year and 10-year U.S. Treasury yields



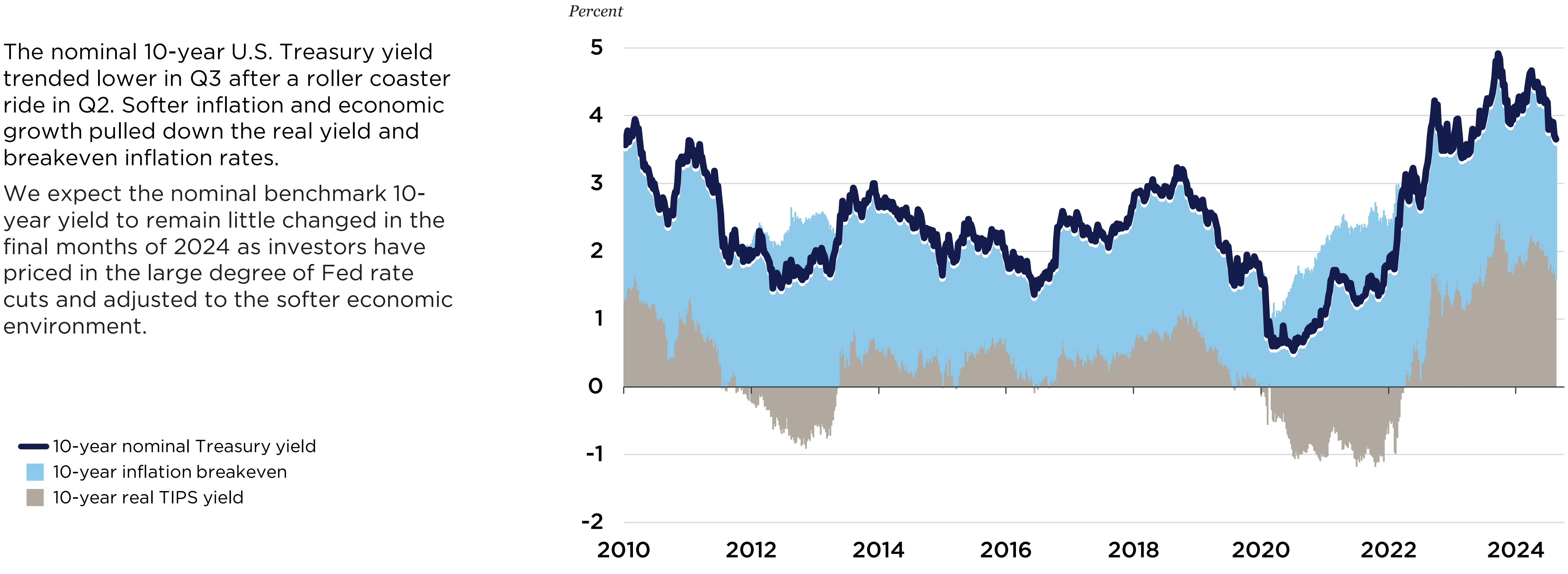
Source: Bloomberg, Nationwide Economics

Buoyant growth keeps real rates elevated

The nominal 10-year U.S. Treasury yield trended lower in Q3 after a roller coaster ride in Q2. Softer inflation and economic growth pulled down the real yield and breakeven inflation rates.

We expect the nominal benchmark 10-year yield to remain little changed in the final months of 2024 as investors have priced in the large degree of Fed rate cuts and adjusted to the softer economic environment.

Breakdown of the 10-year U.S. Treasury yield



Source: Bloomberg, Nationwide Economics

How markets move after Fed rate cuts

The historical performance of key financial market benchmarks in the wake of Fed rate cuts offers a guide of how investors may respond to the current easing cycle. Equities and the U.S. dollar tend to respond positively while the spread between the federal funds rate and 10-year U.S. Treasury yield often widens.

Economic soft landing

Changes in financial market indicators after Federal Reserve begins easing cycle

Percent (S&P 500® Index & Broad Trade-Weighted U.S. Dollar Index); Basis points (10-year Treasury - Federal Funds Rate spread)

	3-month change			6-month change			12-month change		
	S&P 500® Index	10-year Treasury - Federal Funds Rate spread	Broad Trade-Weighted U.S. Dollar Index	S&P 500® Index	10-year Treasury - Federal Funds Rate spread	Broad Trade-Weighted U.S. Dollar Index	S&P 500® Index	10-year Treasury - Federal Funds Rate spread	Broad Trade-Weighted U.S. Dollar Index
Oct 1984	1.1	203.5	4.2	10.4	166.0	7.6	12.5	76.0	3.7
Jun 1989	9.5	58.0	3.2	8.6	77.3	2.7	13.9	167.3	7.4
Jul 1995	5.1	1.0	3.6	11.3	-11.0	6.7	18.7	151.0	9.4
Jan 2001	-17.9	80.0	4.0	-8.4	252.0	4.1	-13.5	427.0	4.6
Sep 2007	-4.3	14.0	-2.3	-12.4	148.0	-7.1	-20.6	179.0	-1.0
Jul 2019	1.9	17.0	0.4	8.2	-1.0	0.2	9.8	53.0	1.5

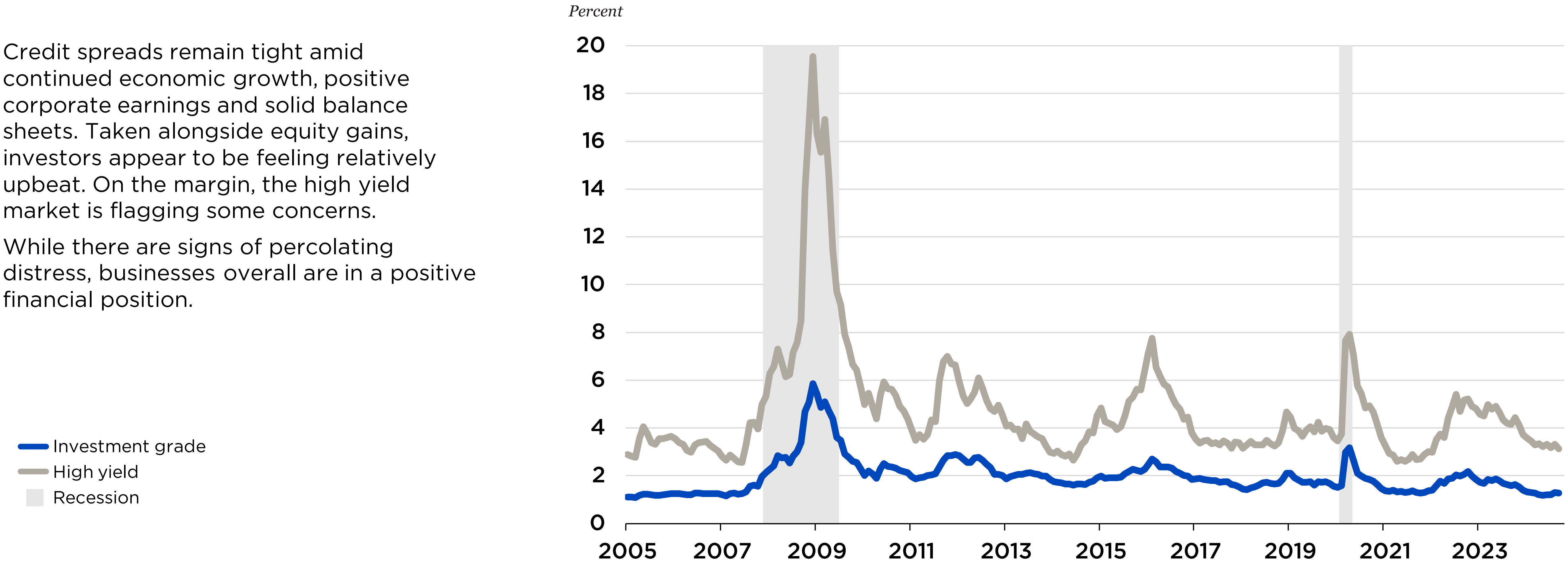
Source: Federal Reserve Board, Haver Analytics, Bloomberg, Nationwide Economics

Corporate bond spreads aren't flagging big worries

Credit spreads remain tight amid continued economic growth, positive corporate earnings and solid balance sheets. Taken alongside equity gains, investors appear to be feeling relatively upbeat. On the margin, the high yield market is flagging some concerns.

While there are signs of percolating distress, businesses overall are in a positive financial position.

Investment-grade and high-yield option adjusted spreads



Source: Federal Reserve Board, ICE/Bank of America Merrill Lynch, Haver Analytics, Nationwide Economics

Which fixed-income asset classes are gaining or losing in 2024?

Investors maintain a healthy appetite for risk despite worries about the economy. High yield continued to outperform other major asset classes through the end of Q3, posting the highest year-to-date return. On the other end of the spectrum, Municipals and Treasuries are underperforming.

Yearly changes by asset class

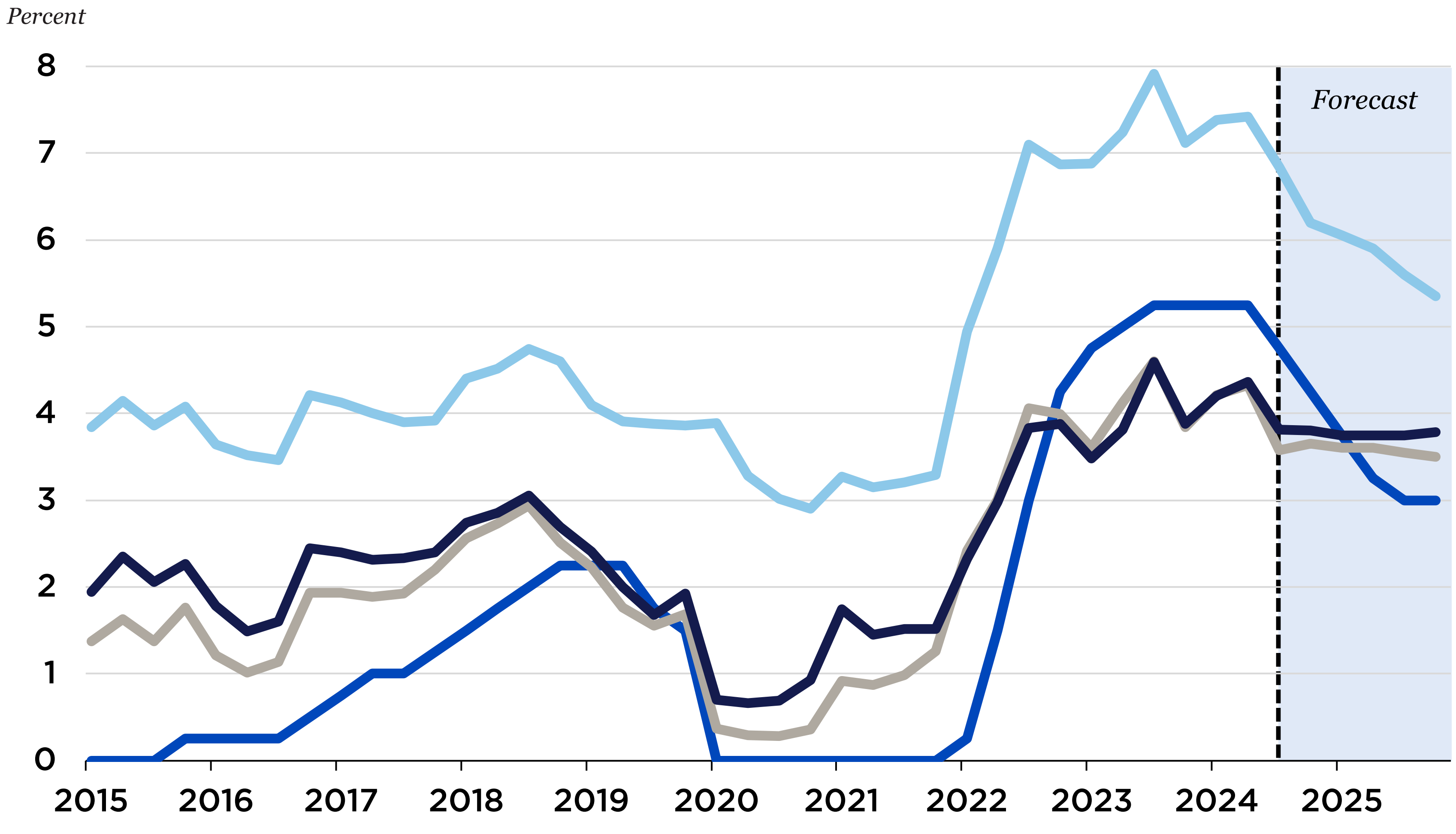
2015	2016	2017	2018	2019	2020	2021	2022	2023	2024 YTD
Municipals 3.3%	HY Corporate 17.1%	HY Corporate 7.5%	Agencies 1.3%	IG Corporate 14.5%	TIPS 11.2%	TIPS 6.1%	Agencies -7.9%	HY Corporate 13.4%	HY Corporate 6.3%
MBS 1.5%	IG Corporate 6.1%	IG Corporate 6.4%	Municipals 1.3%	HY Corporate 14.3%	Treasuries 10.6%	HY Corporate 5.3%	Municipals -8.5%	IG Corporate 8.5%	IG Corporate 3.5%
Agencies 1.0%	TIPS 4.8%	Municipals 5.4%	MBS 1.0%	Treasuries 8.9%	IG Corporate 9.9%	Municipals 1.5%	MBS -11.8%	Municipals 6.4%	TIPS 3.3%
Treasuries 0.9%	Bloomberg Agg 2.6%	Bloomberg Agg 3.5%	Bloomberg Agg 0.0%	TIPS 8.8%	Bloomberg Agg 7.5%	IG Corporate -1.0%	HY Corporate -11.9%	Bloomberg Agg 5.5%	Agencies 3.3%
Bloomberg Agg 0.5%	MBS 1.7%	TIPS 3.3%	Treasuries 0.0%	Bloomberg Agg 8.7%	HY Corporate 7.1%	MBS -1.0%	TIPS -12.6%	Agencies 5.1%	MBS 3.3%
IG Corporate -0.7%	Agencies 1.4%	MBS 2.5%	TIPS -1.5%	Municipals 7.5%	Agencies 5.5%	Agencies -1.3%	Bloomberg Agg -13.0%	MBS 5.0%	Bloomberg Agg 3.1%
TIPS -1.7%	Municipals 0.2%	Treasuries 2.1%	HY Corporate -2.1%	MBS 6.4%	Municipals 5.2%	Bloomberg Agg -1.5%	IG Corporate -15.8%	TIPS 3.8%	Treasuries 2.2%
HY Corporate -4.5%	Treasuries -0.2%	Agencies 2.1%	IG Corporate -2.5%	Agencies 5.9%	MBS 3.9%	Treasuries -3.6%	Treasuries -16.3%	Treasuries 3.2%	Municipals 1.3%

Note: IG corporate represents investment grade corporate debt; HY corporate represents high yield corporate debt
Source: Bloomberg, Nationwide Economics

Lower interest rates are ahead

We expect short- and medium-term interest rates to decline over the coming quarters as the economy cools off, inflation moderates, and the Federal Reserve unwinds its restrictive monetary policy. Mortgage rates should follow suit.

Nationwide Economics' interest rate forecasts



Note: September 2024 forecast vintage
Source: Haver Analytics, Nationwide Economics

Equities persevere

The S&P 500® Index remains on an encouraging track, though it has lost some upward momentum recently as investors adjust to the reality of a normalized economy amid rising concerns the soft landing could turn into a recession.

Large cap tech stocks continue to be the driving force of equities' buoyancy. It remains to be seen how much longer this theme can run.

S&P 500® Index: Market cap versus equal-weighted

Index, 12/30/22 = 100

Note: The results shown represent past performance; past performance does not guarantee future results
Source: Bloomberg, Nationwide Economics

What worked in 2023 works in 2024

Last year's investment winners continue to work in 2024. Equities are outperforming other major asset classes. Further, U.S. equities have outperformed their global peers. Commodities and bonds are lagging, as they did in 2023.

Annual equity returns

Percent

Note: The results shown represent past performance; past performance does not guarantee future results
Source: Bloomberg, Nationwide Economics

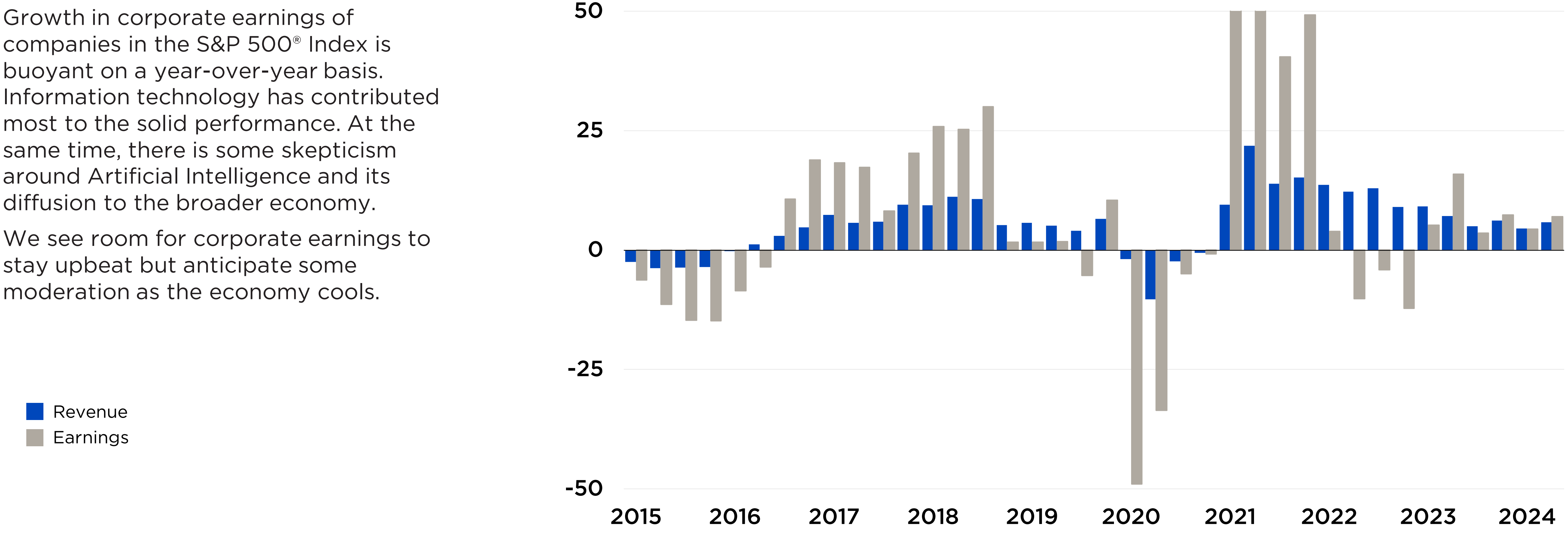
Positive trends for U.S. corporations

Growth in corporate earnings of companies in the S&P 500® Index is buoyant on a year-over-year basis. Information technology has contributed most to the solid performance. At the same time, there is some skepticism around Artificial Intelligence and its diffusion to the broader economy.

We see room for corporate earnings to stay upbeat but anticipate some moderation as the economy cools.

S&P 500® Index: revenue and earnings growth

Year-over-year percent change



Note: The results shown represent past performance; past performance does not guarantee future results
Source: Standard & Poor's, Nationwide Economics

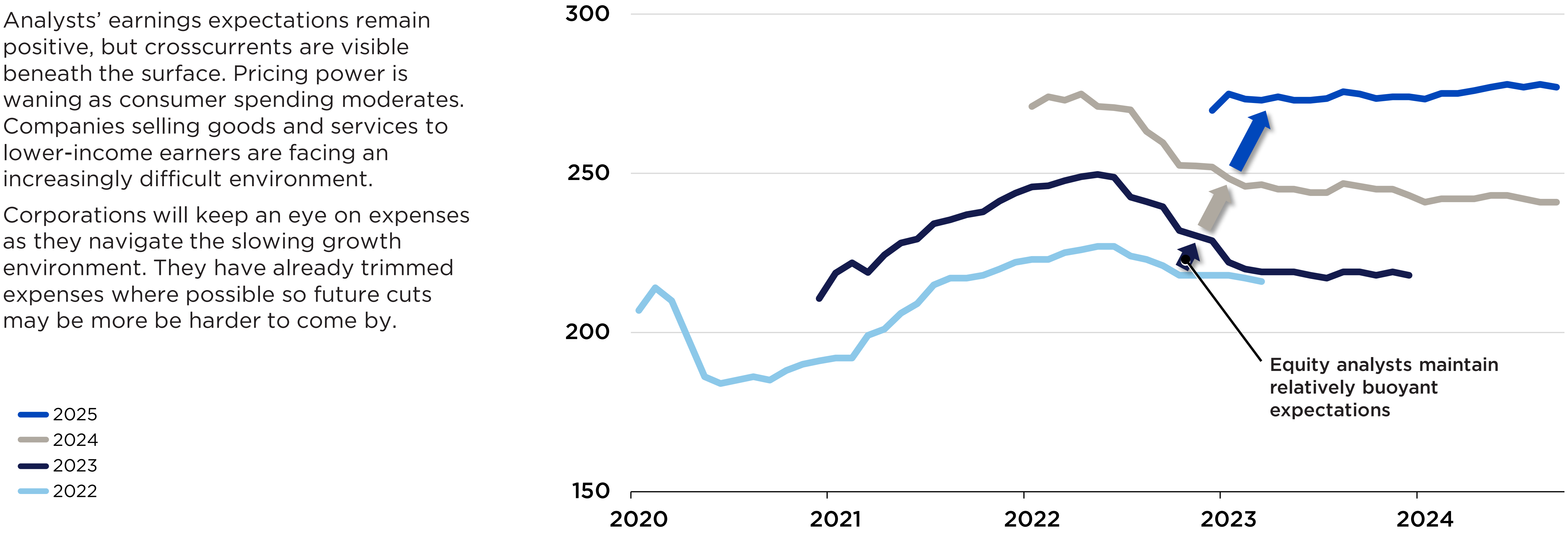
Earnings expectations are being revised higher

Analysts' earnings expectations remain positive, but crosscurrents are visible beneath the surface. Pricing power is waning as consumer spending moderates. Companies selling goods and services to lower-income earners are facing an increasingly difficult environment.

Corporations will keep an eye on expenses as they navigate the slowing growth environment. They have already trimmed expenses where possible so future cuts may be more be harder to come by.

Earnings evolution: S&P 500® Index

Dollar earnings per share

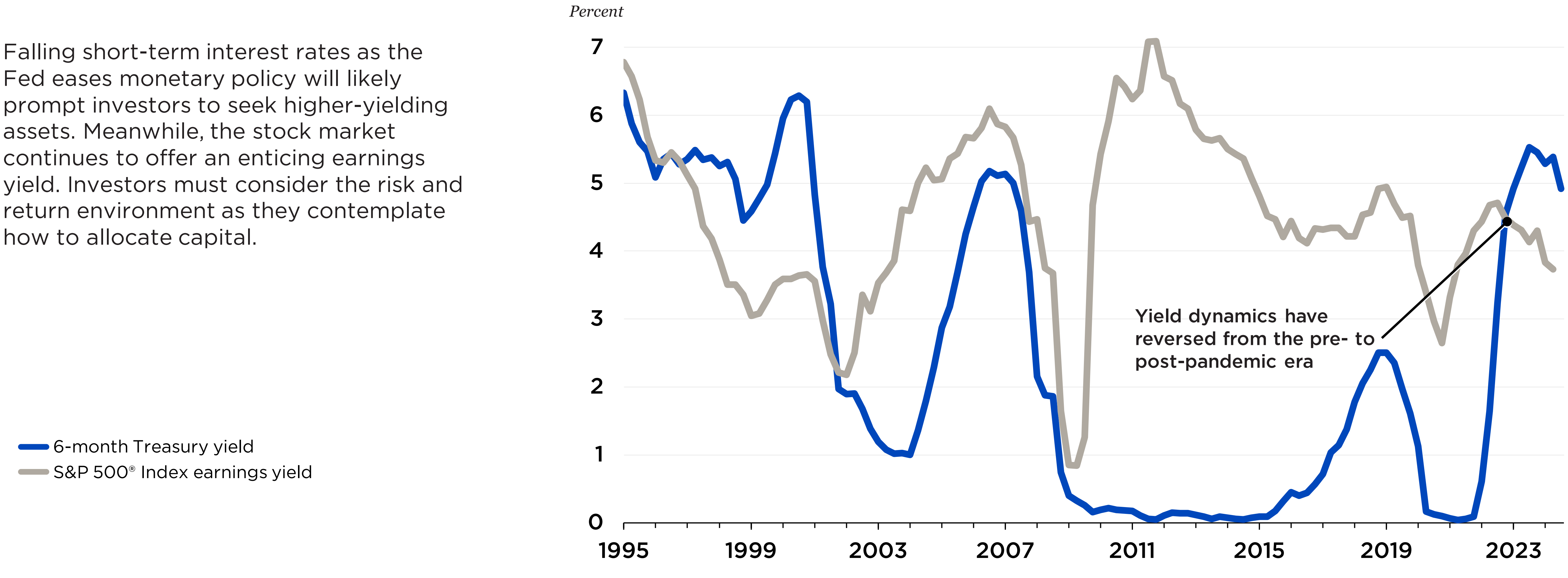


Source: FactSet, Nationwide Economics

High rates give investors options

Falling short-term interest rates as the Fed eases monetary policy will likely prompt investors to seek higher-yielding assets. Meanwhile, the stock market continues to offer an enticing earnings yield. Investors must consider the risk and return environment as they contemplate how to allocate capital.

6-month Treasury yield and S&P 500® Index earnings yield



Source: Standard & Poor's and Bloomberg, Nationwide Economics

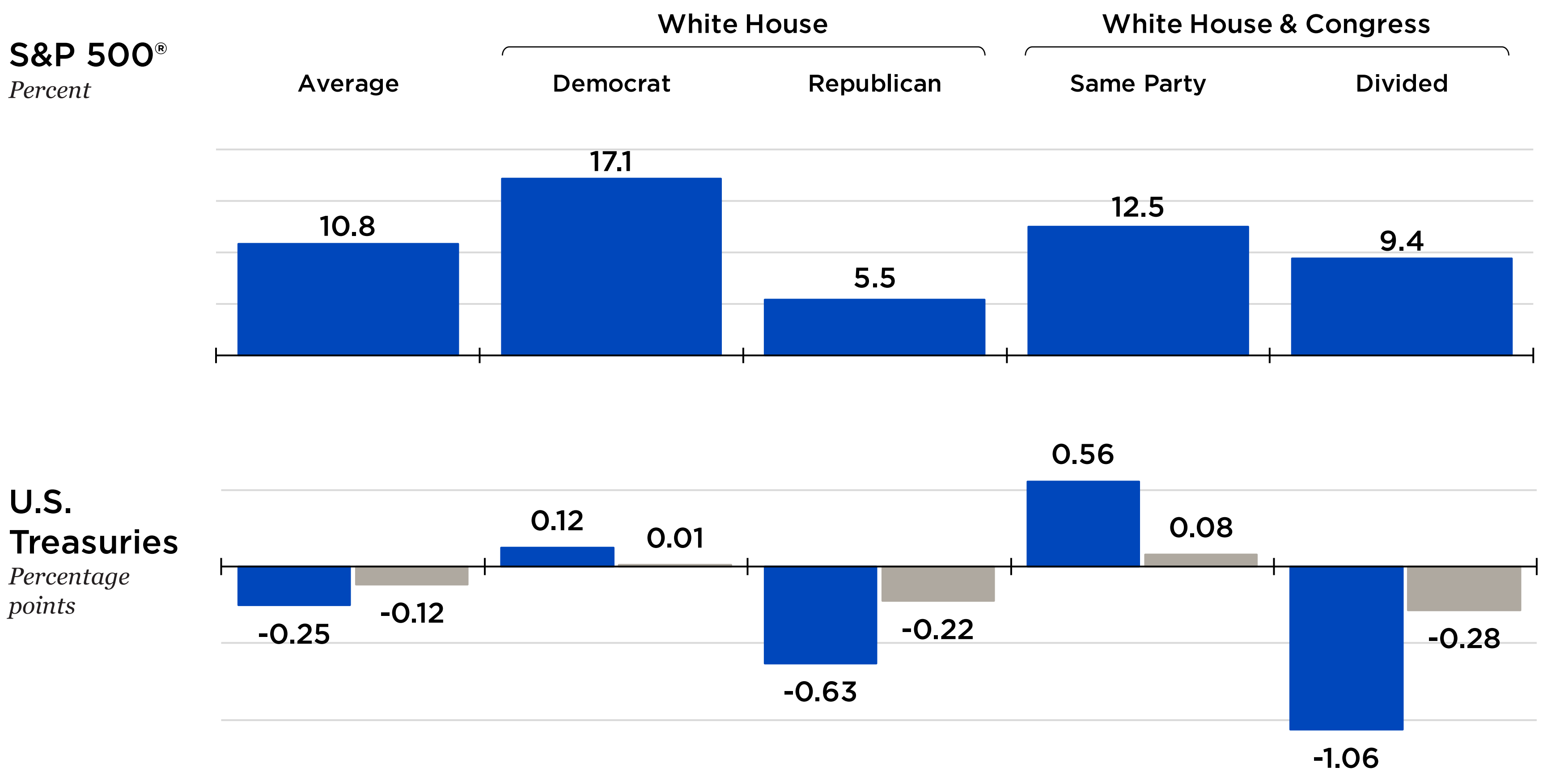
The election is on investors’ minds

The upcoming U.S. presidential election is a key source of uncertainty. History shows the S&P 500® increases more with a Democrat in the White House versus a Republican. Gains are tempered if the party in the White House does not have control of Congress.

On the fixed income front, the U.S. Treasury curve tends to bull steepen one year after a Republican wins the White House. The curve tends to be little changed if a Democrat wins.

Market changes one year after U.S. presidential election

Data includes every presential election since 1972; sample for 2—year U.S. Treasury yield calculation excludes the 1972 election



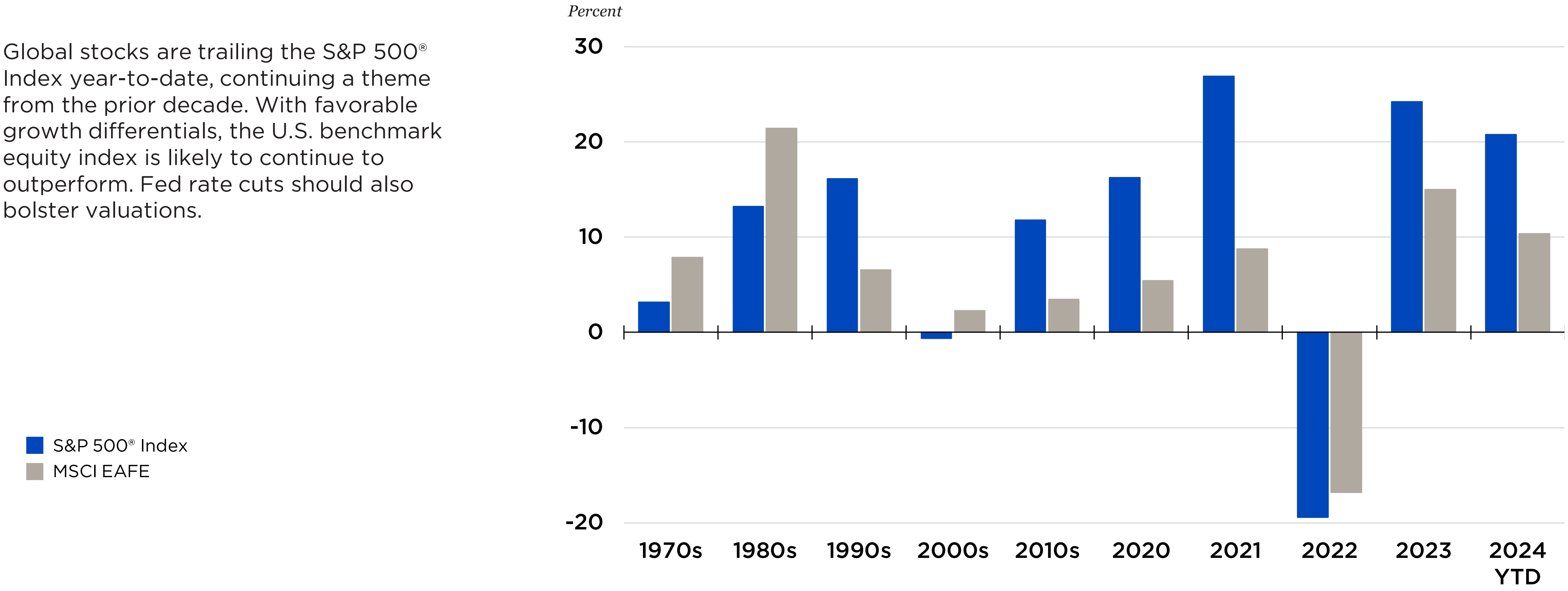
2-year Treasury yield
10-year Treasury yield

Source: Haver Analytics, Nationwide Economics

U.S. equities outpace their global counterparts

Global stocks are trailing the S&P 500® Index year-to-date, continuing a theme from the prior decade. With favorable growth differentials, the U.S. benchmark equity index is likely to continue to outperform. Fed rate cuts should also bolster valuations.

Annualized changes in the S&P 500® Index and the MSCI EAFE Index



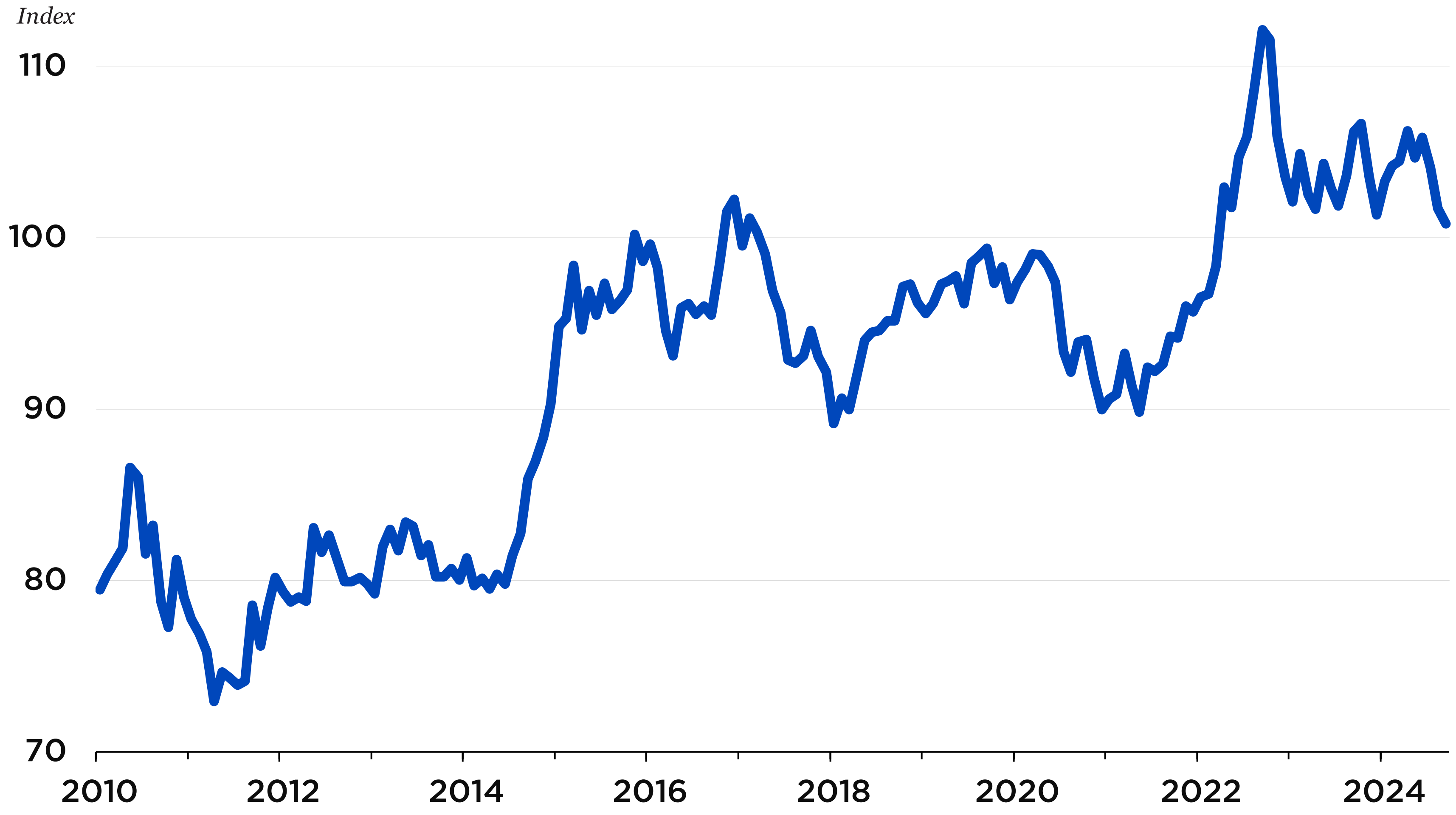
Note: The results shown represent past performance; past performance does not guarantee future results
Source: Bloomberg

A mildly weaker greenback

The dollar has lost some ground, but favorable interest rate and growth differentials and elevated geopolitical risks will support the U.S. currency's value.

The U.S. dollar's position as the world's reserve currency and its pivotal role in global financial markets will support the currency's value. Meanwhile, the federal government's debt burden poses a meaningful downside risk in the long term.

The trade-weighted U.S. dollar index



Source: ICE, Bloomberg, Nationwide Economics

Downward trending commodity prices

The benchmark CRB commodity price index has fallen about 3.5 percent since peaking in April as commodity costs have declined in aggregate.

Crude oil prices have garnered plenty of headlines, but the decline isn't limited to hydrocarbons. The prices of metals and agricultural goods have also fallen.

CRB Spot commodity price index

Index; 1967 = 100

Source: Commodity Research Bureau, Haver Analytics, Nationwide Economics

U.S. Economy

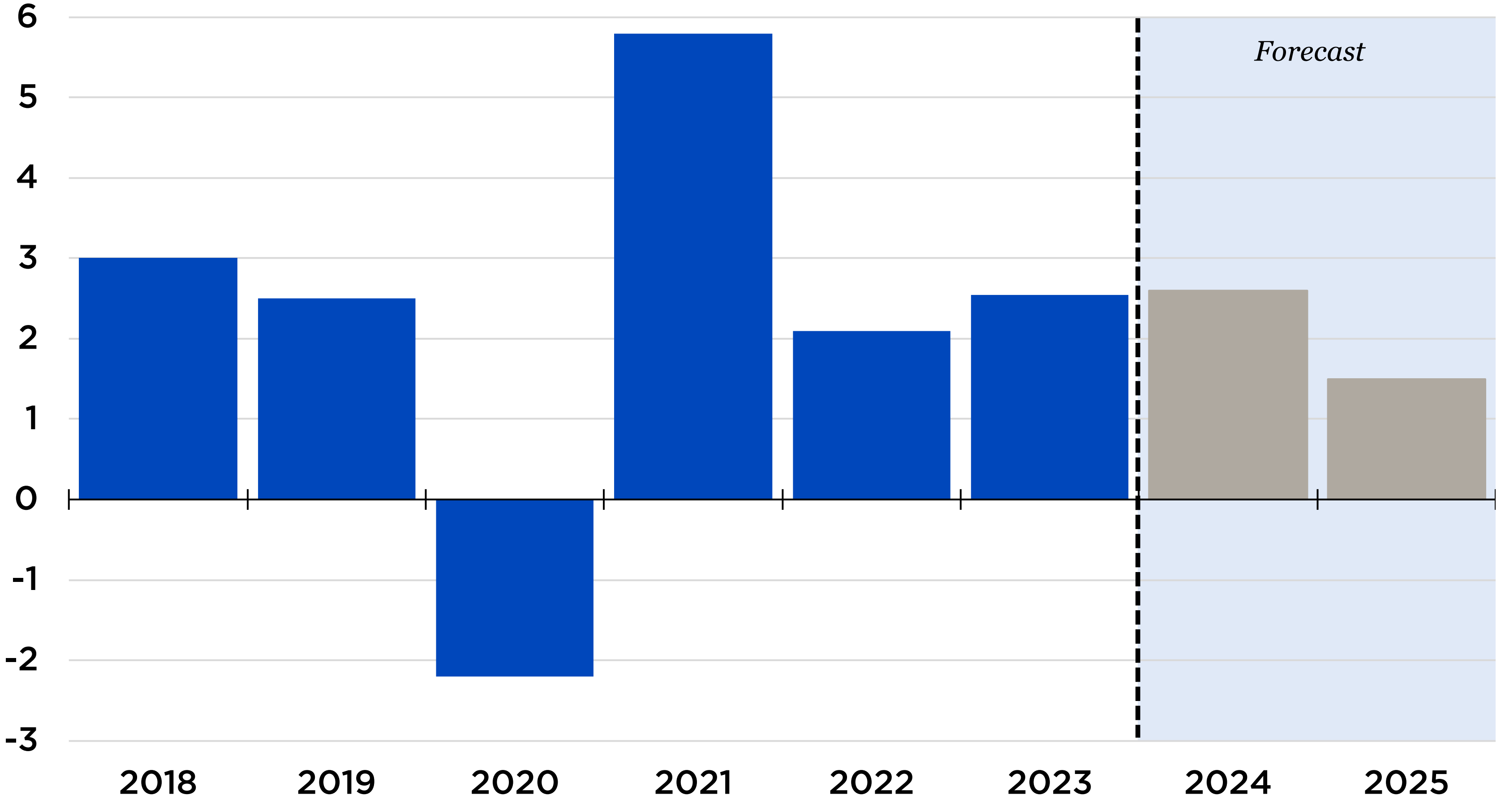
Highlights

Cooling economic growth

The data depict a moderating economic expansion, with few of the typical signs normally seen at the start of recessions. We anticipate a tempered GDP advance through the rest of 2024 and a moderate gain in 2025. Rising signs of stress in certain consumer and business segments indicate that risks to growth are tilted to the downside.

GDP growth – historical and forecast

Percent, annual average



Source: Bureau of Economic Analysis, Haver Analytics, Nationwide Economics

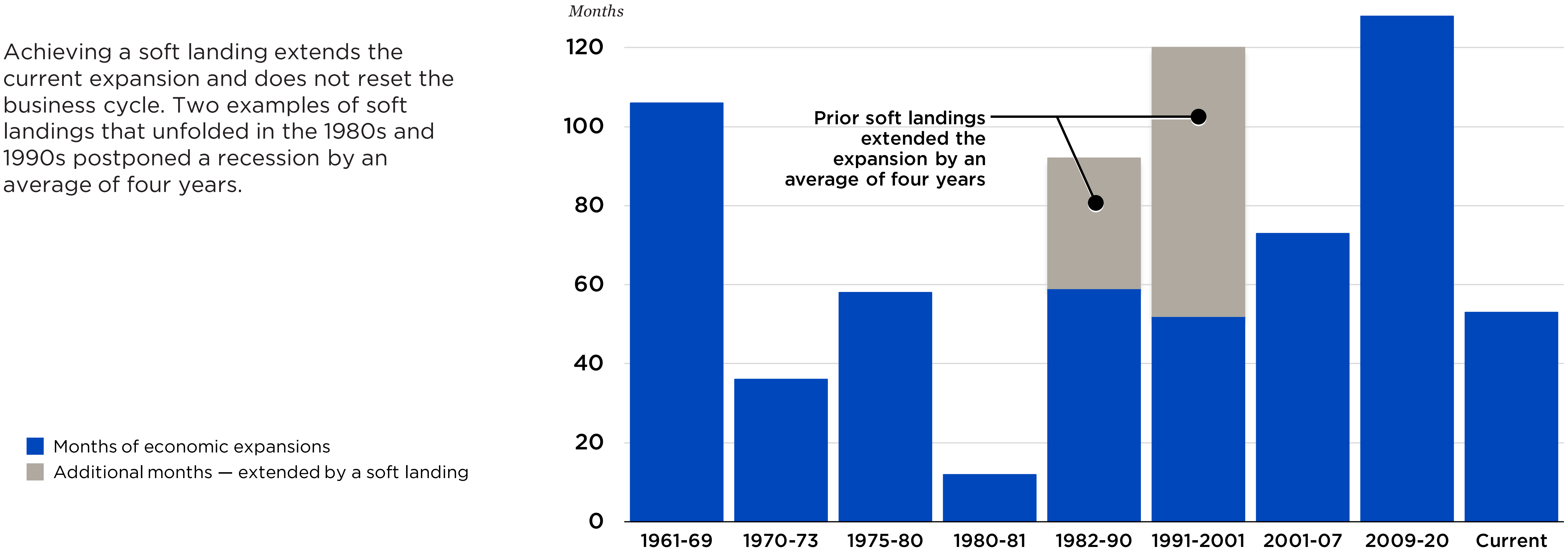
Where are we in the business cycle?

The fundamental economic backdrop remains encouraging even as the data flash warning signs. We believe the economy is late-cycle and envision gradually softening growth dynamics into early 2025.

Soft landing doesn't mean the start of a new expansion

Achieving a soft landing extends the current expansion and does not reset the business cycle. Two examples of soft landings that unfolded in the 1980s and 1990s postponed a recession by an average of four years.

Length of economic expansions



NBER, Haver Analytics, Nationwide Economics

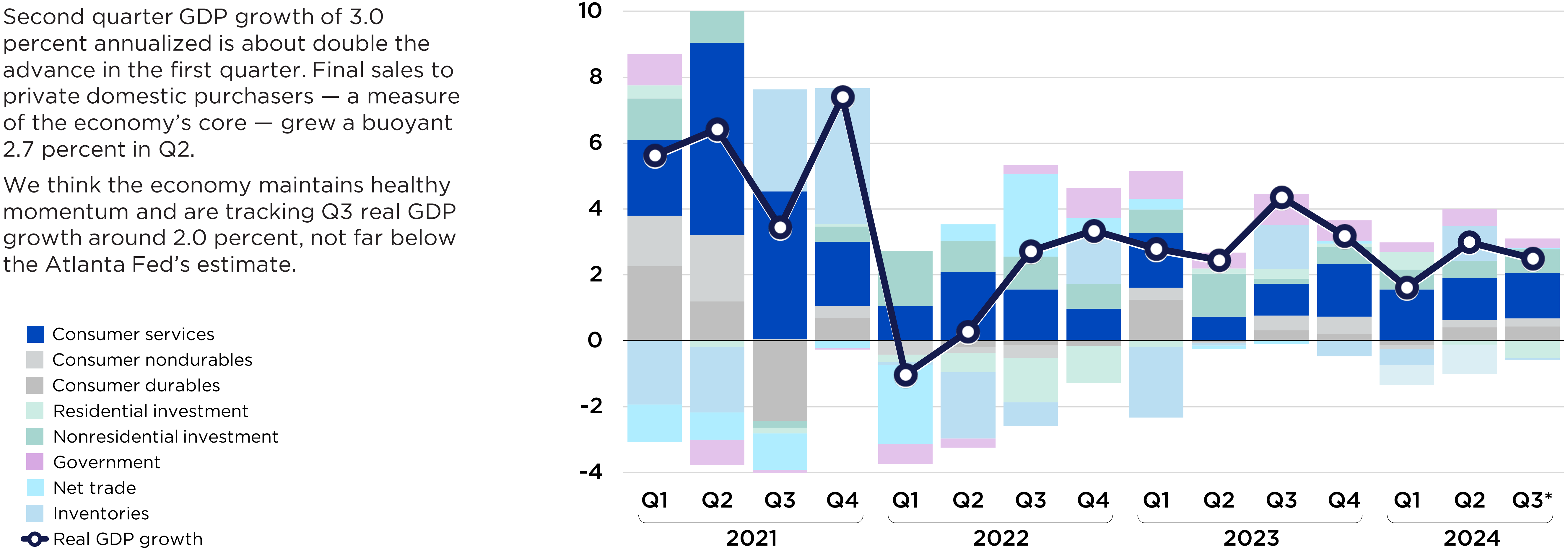
Economy continues to grow

Second quarter GDP growth of 3.0 percent annualized is about double the advance in the first quarter. Final sales to private domestic purchasers — a measure of the economy's core — grew a buoyant 2.7 percent in Q2.

We think the economy maintains healthy momentum and are tracking Q3 real GDP growth around 2.0 percent, not far below the Atlanta Fed's estimate.

Contribution to real GDP growth

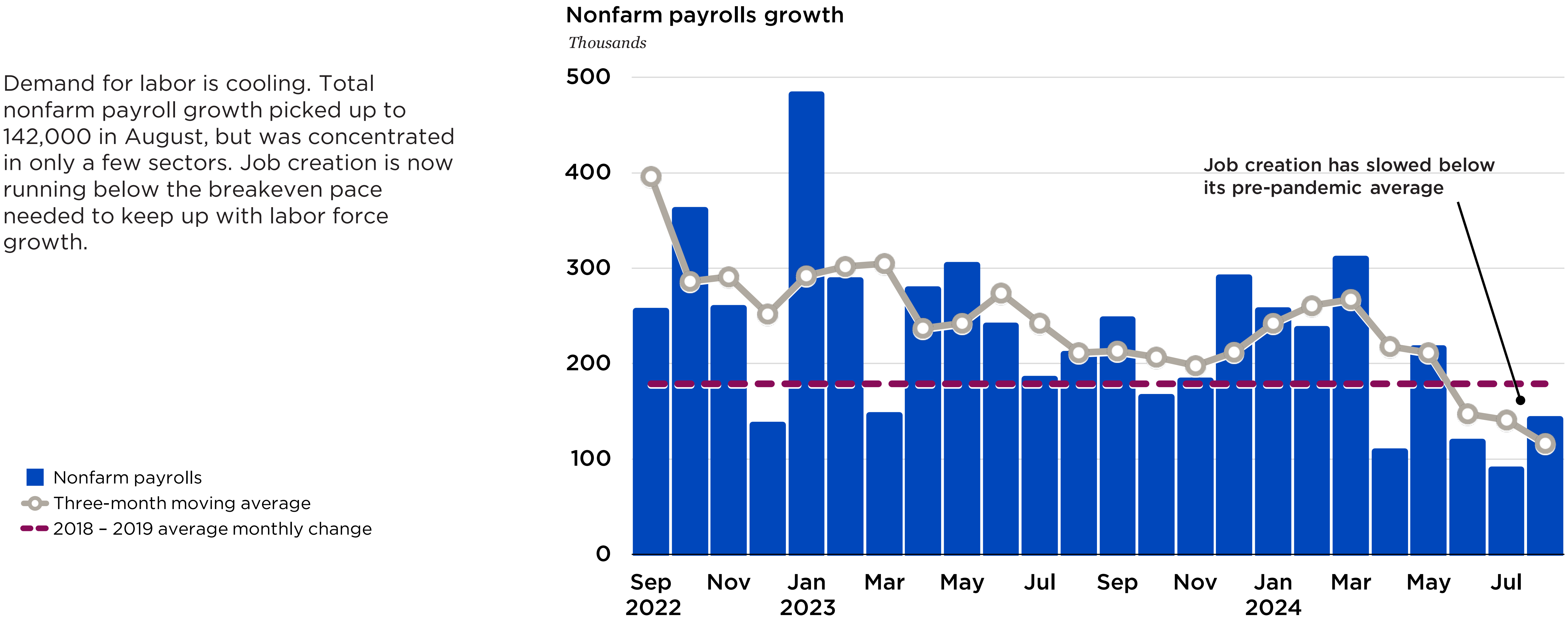
SAAR, percent



*Note: *Represents Federal Reserve Bank of Atlanta's GDP estimate*
Source: Bureau of Economic Analysis, Haver Analytics, Federal Reserve Bank of Atlanta, Nationwide Economics

Downshifting jobs machine

Demand for labor is cooling. Total nonfarm payroll growth picked up to 142,000 in August, but was concentrated in only a few sectors. Job creation is now running below the breakeven pace needed to keep up with labor force growth.



Source: Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

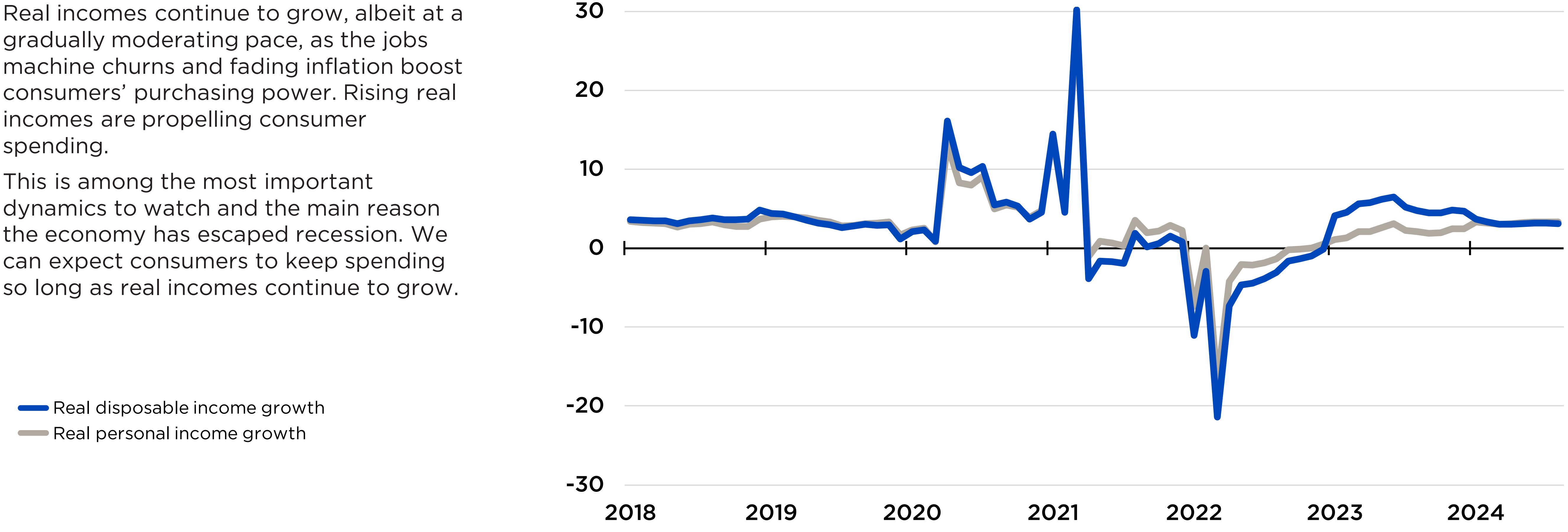
Positive real income trends support outlays

Real incomes continue to grow, albeit at a gradually moderating pace, as the jobs machine churns and fading inflation boost consumers' purchasing power. Rising real incomes are propelling consumer spending.

This is among the most important dynamics to watch and the main reason the economy has escaped recession. We can expect consumers to keep spending so long as real incomes continue to grow.

Real income growth

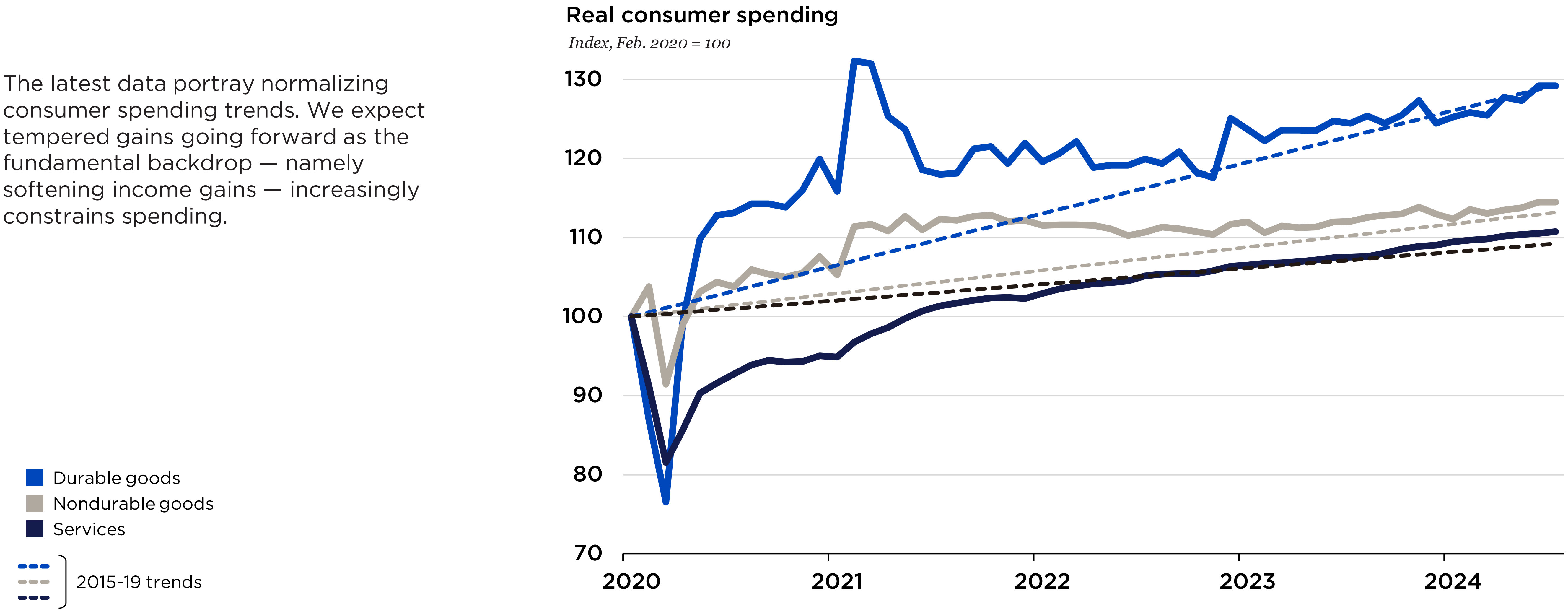
Year-over-year, percent



Source: Bureau of Economic Analysis, Haver Analytics, Nationwide Economics

Consumer spending is holding up

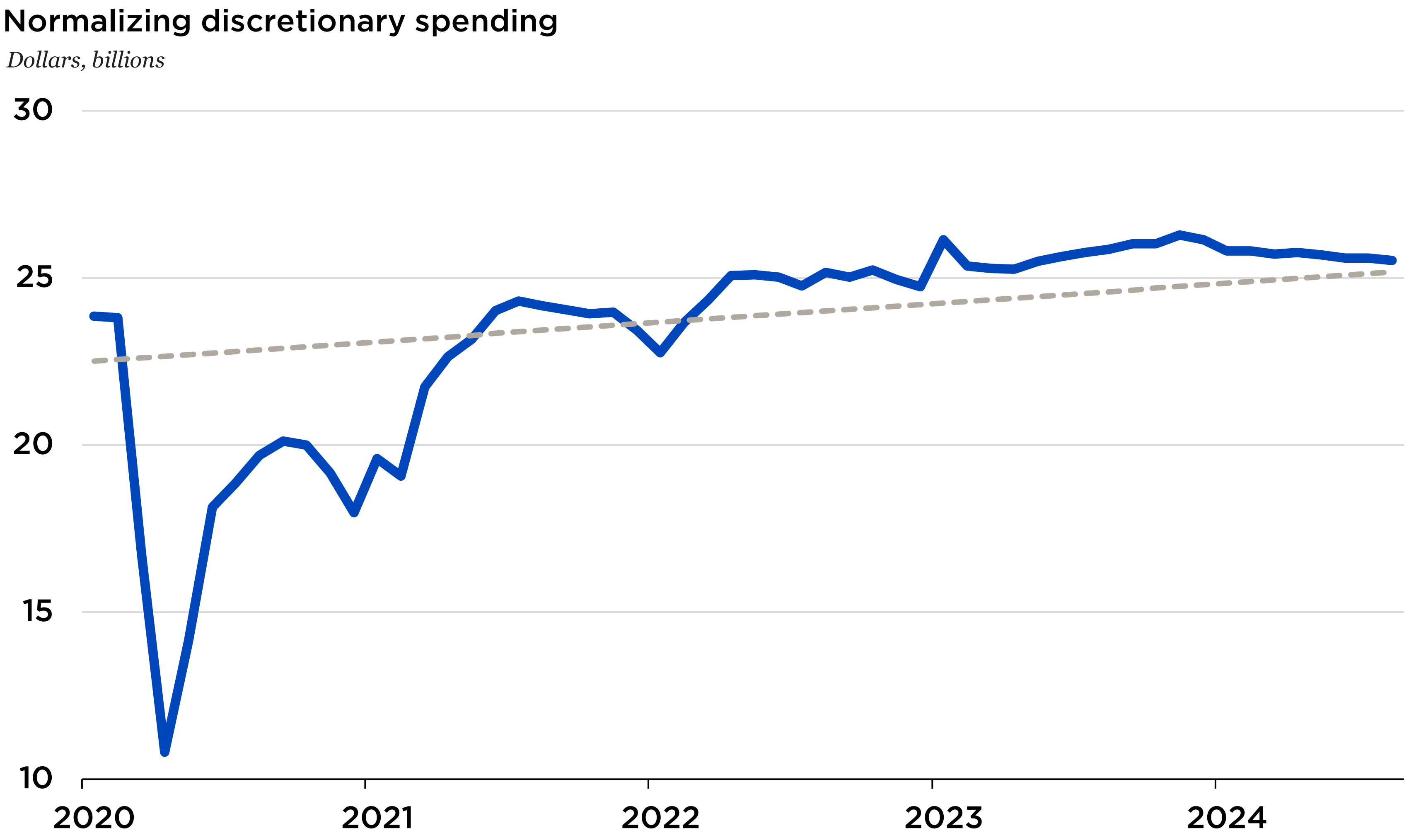
The latest data portray normalizing consumer spending trends. We expect tempered gains going forward as the fundamental backdrop — namely softening income gains — increasingly constrains spending.



Source: Bureau of Economic Analysis, Haver Analytics, Nationwide Economics

Discretionary spending is losing steam

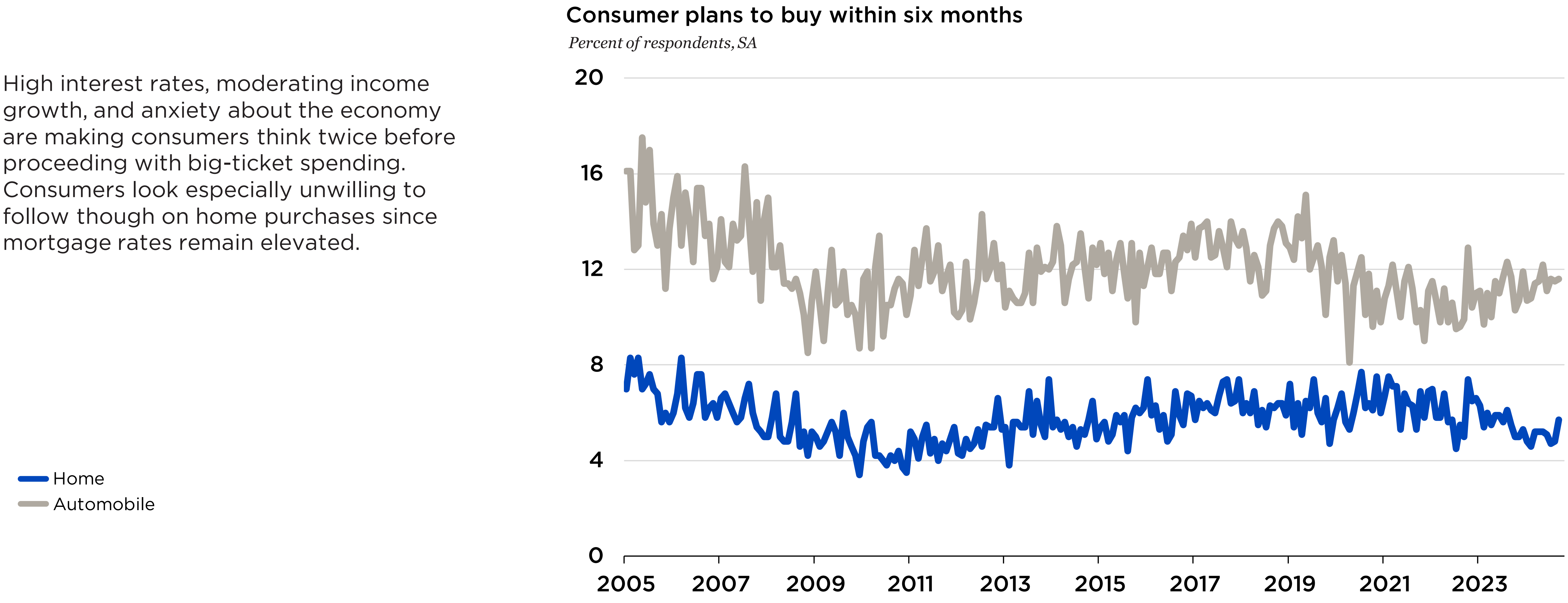
Spending on non-essentials, such as dining out, is reverting to its long-term historical trend. This is a sign that outlays are normalizing after robust revenge spending in the immediate aftermath of the pandemic.



Note: Retail sales deflated with CPI
Source: Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

Big-ticket spending intentions

High interest rates, moderating income growth, and anxiety about the economy are making consumers think twice before proceeding with big-ticket spending. Consumers look especially unwilling to follow though on home purchases since mortgage rates remain elevated.



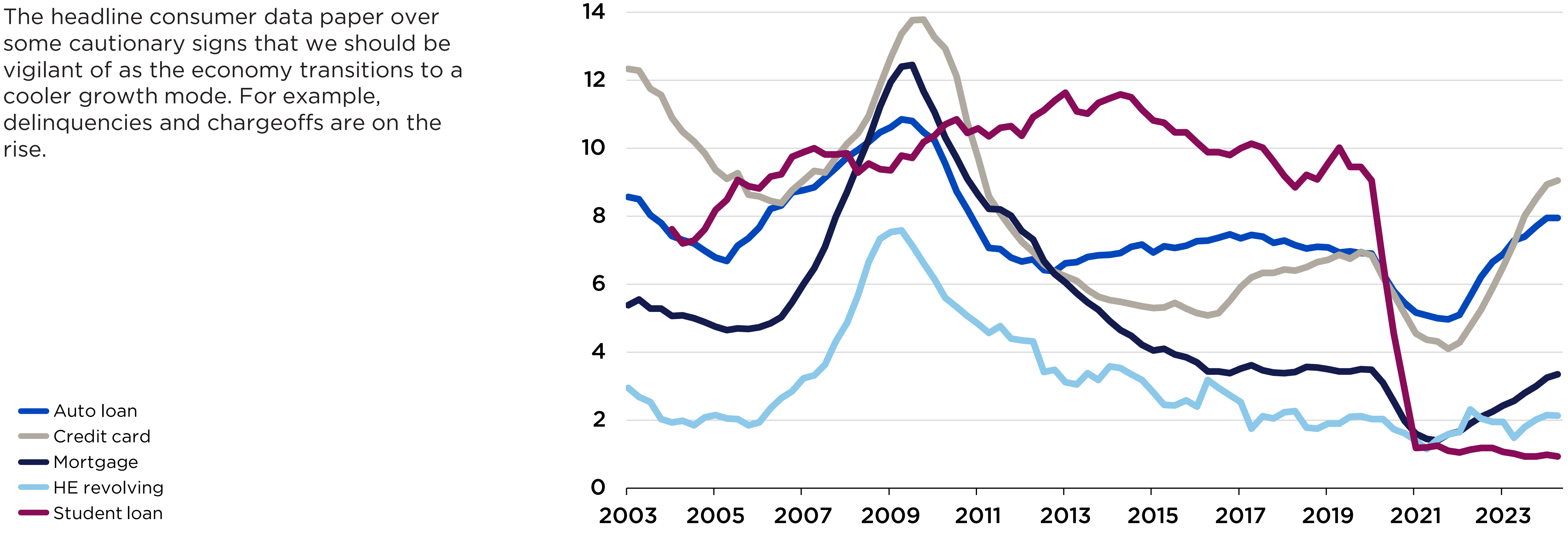
Source: The Conference Board, Haver Analytics, Nationwide Economics

Delinquencies flash warning signs

The headline consumer data paper over some cautionary signs that we should be vigilant of as the economy transitions to a cooler growth mode. For example, delinquencies and chargeoffs are on the rise.

Transition into delinquency (30+) by loan type

Percent of balance



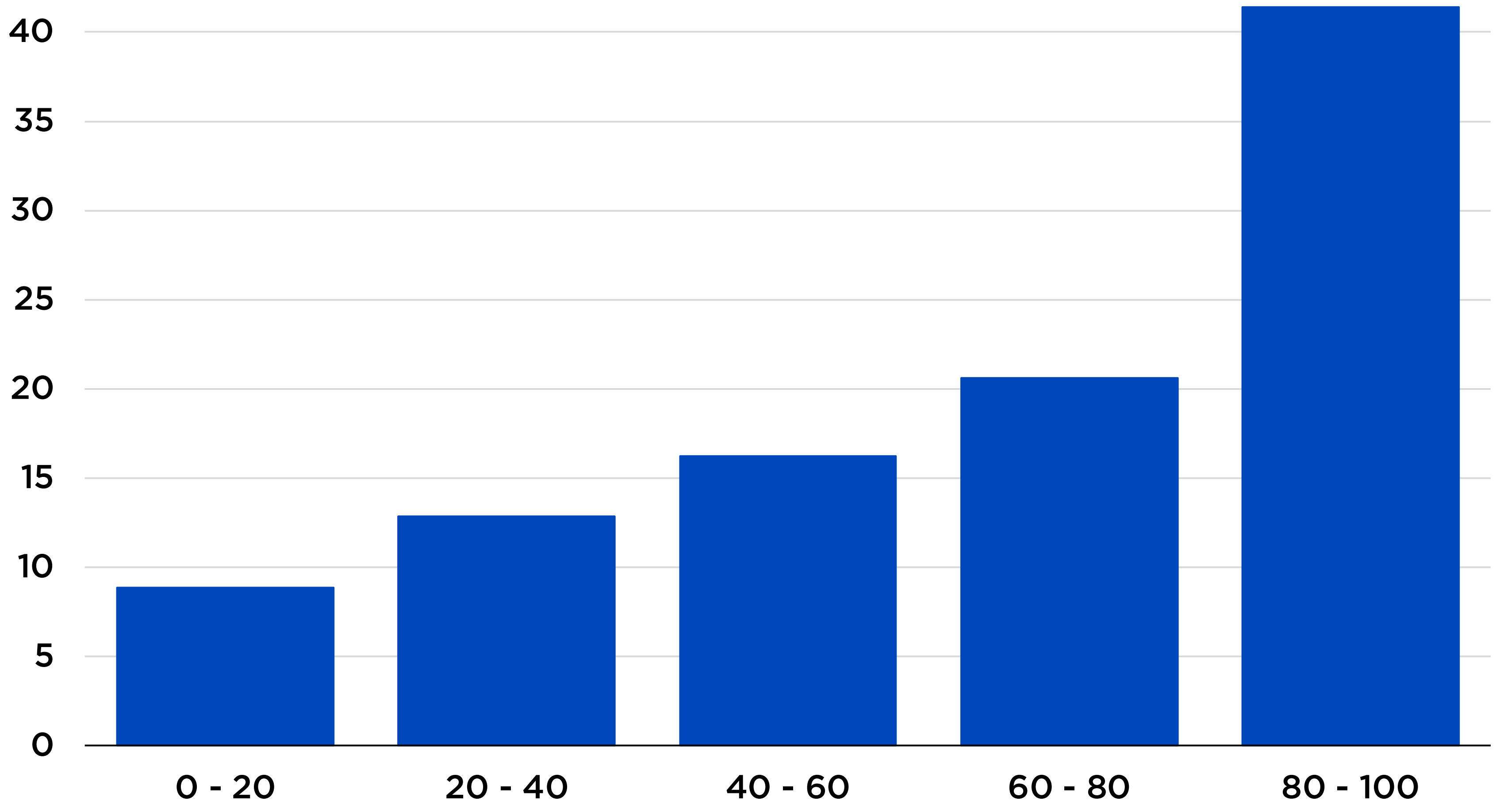
Source: New York Fed Consumer Credit Panel/Equifax

Low-income households are most vulnerable

Consumers at the lower end of the income spectrum will be most vulnerable to moderating income trends. Lower income households do not account for the majority of total consumer spending, but they raise the risks of turbulence as labor demand softens and economic growth slows.

Consumer spending by income quantile

Percent



Source: Bureau of Labor Statistics Consumer Expenditures Survey, Nationwide Economics

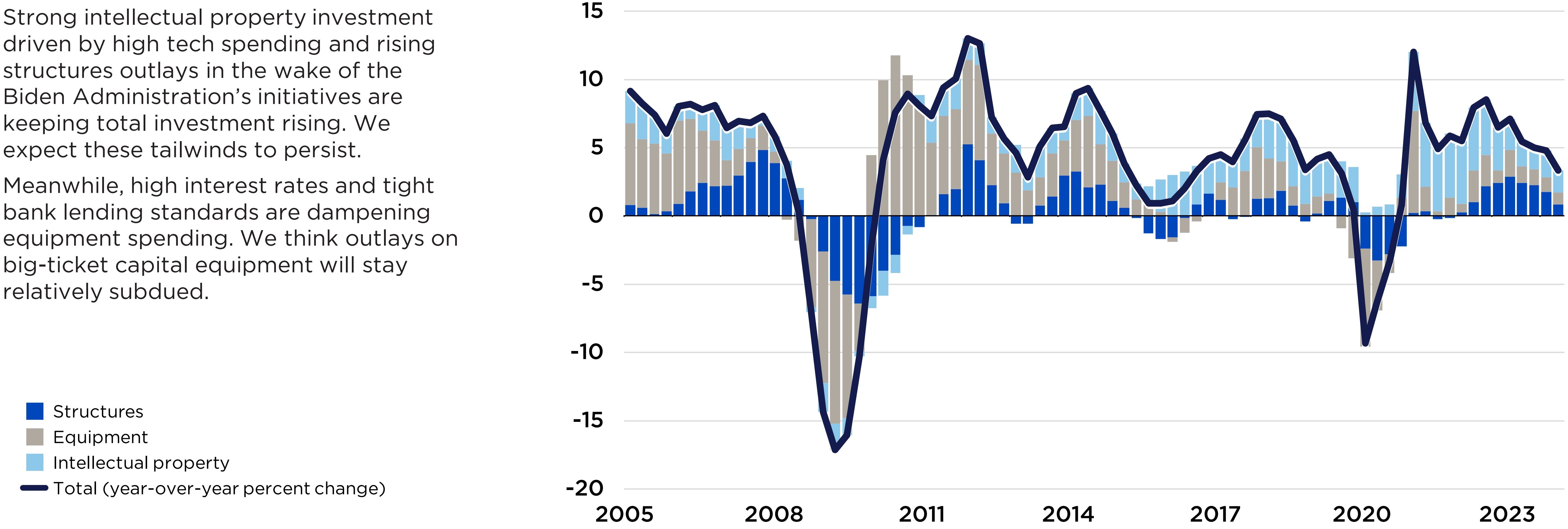
Rising IP and structures spending support business investment

Strong intellectual property investment driven by high tech spending and rising structures outlays in the wake of the Biden Administration's initiatives are keeping total investment rising. We expect these tailwinds to persist.

Meanwhile, high interest rates and tight bank lending standards are dampening equipment spending. We think outlays on big-ticket capital equipment will stay relatively subdued.

Nonresidential fixed investment

Percentage point contribution to year-over-year growth



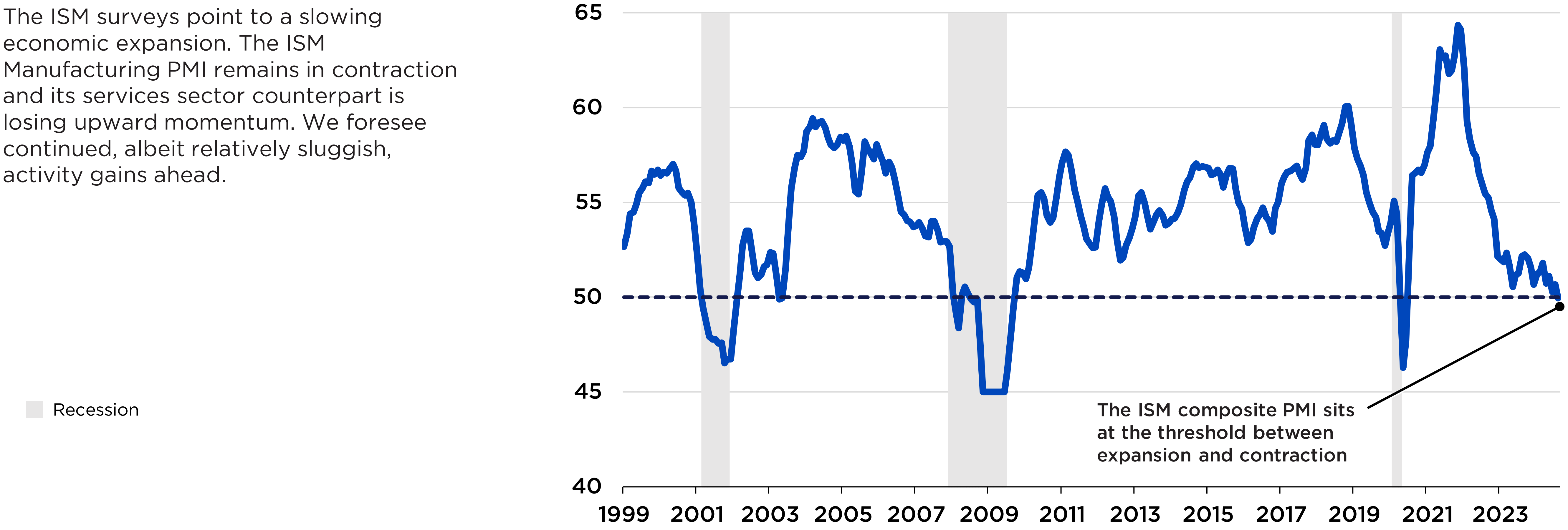
Source: Bureau of Economic Analysis, Haver Analytics, Nationwide Economics

ISMs signal cooler growth

The ISM surveys point to a slowing economic expansion. The ISM Manufacturing PMI remains in contraction and its services sector counterpart is losing upward momentum. We foresee continued, albeit relatively sluggish, activity gains ahead.

Economy-weighted ISM composite PMI

Index; > 50 = expansion



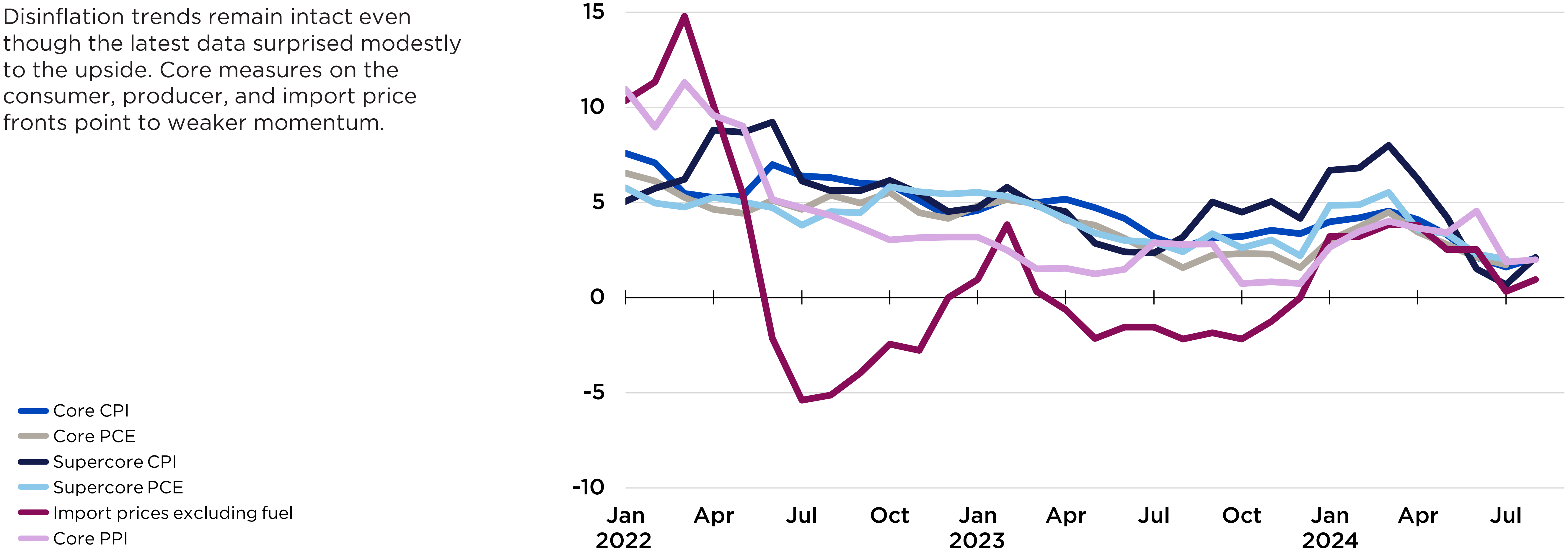
Bureau of Economics Analysis, Institute for Supply Management, Haver Analytics, Nationwide Economics

High inflation appears to be behind us

Disinflation trends remain intact even though the latest data surprised modestly to the upside. Core measures on the consumer, producer, and import price fronts point to weaker momentum.

Broad cooling in core inflation momentum

Three-month annualized growth rate

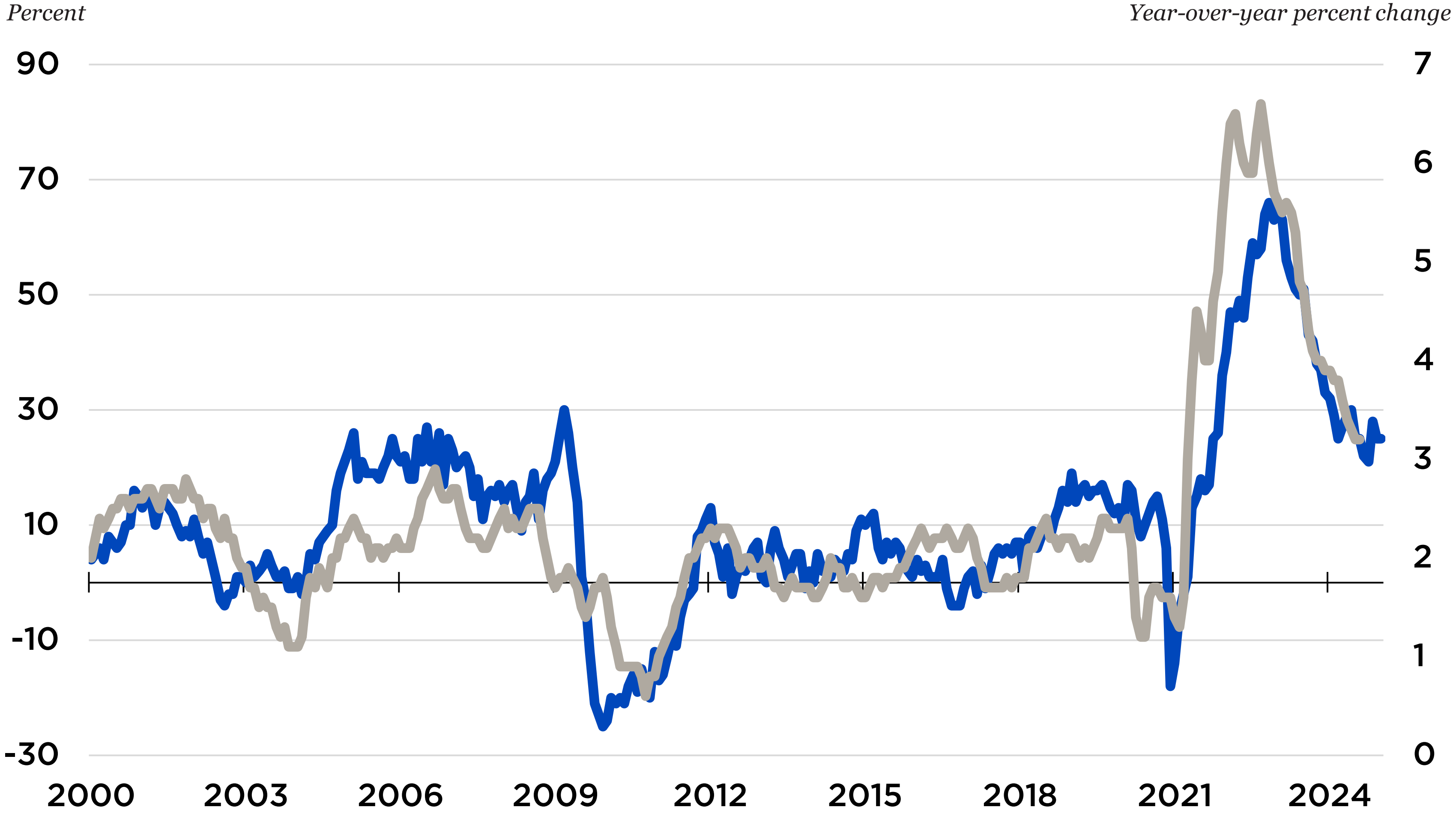


Source: Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

Pricing power is subsiding

U.S. companies are losing pricing power as consumers become more discerning and selective with their purchases, particularly at the lower-end of the income ladder. While this will cap inflation for consumers, it will pose a headwind for U.S. corporations and lead them to try to cut costs to protect margins.

Easing pricing power portends lower inflation



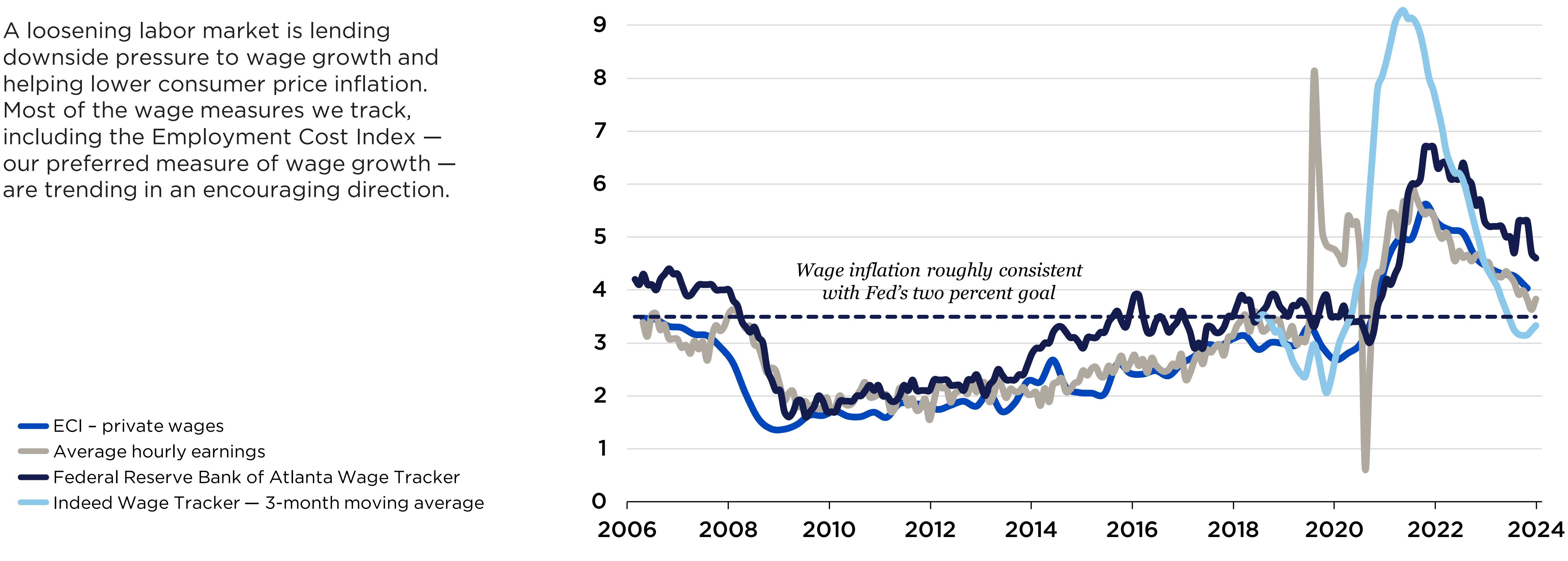
Source: National Federation of Independent Business, Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

Cooling wage growth

A loosening labor market is lending downside pressure to wage growth and helping lower consumer price inflation. Most of the wage measures we track, including the Employment Cost Index — our preferred measure of wage growth — are trending in an encouraging direction.

Wage inflation

Year-over-year percent change



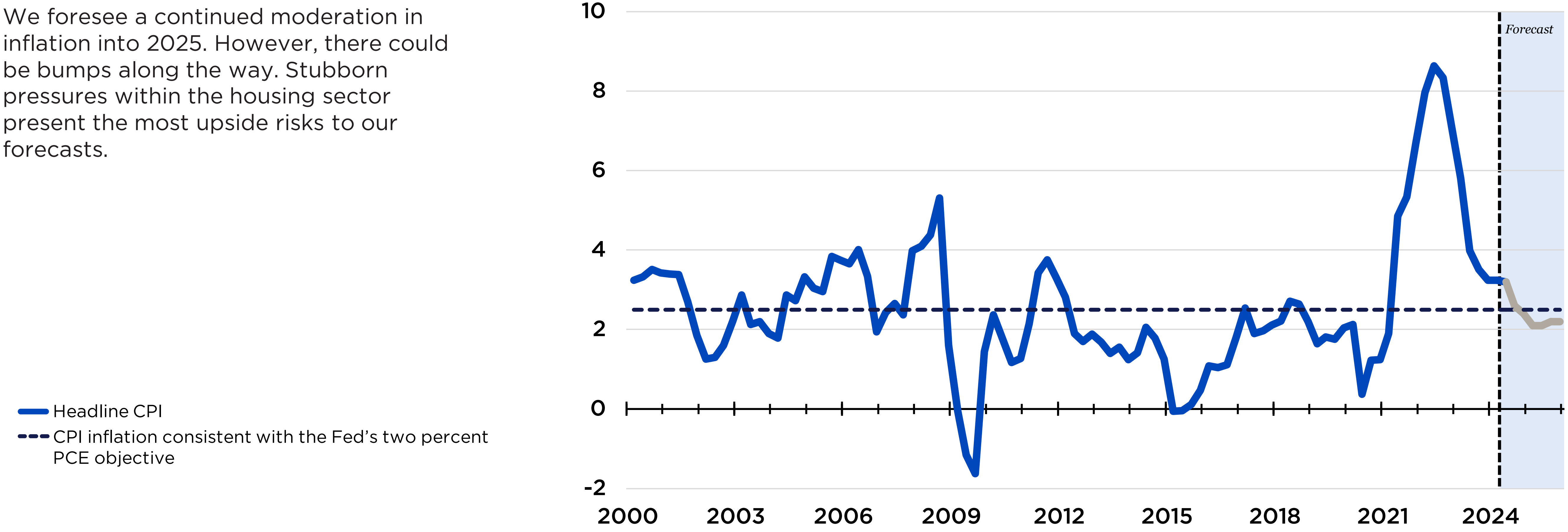
Source: Federal Reserve Bank of Atlanta, Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

Inflation is expected to cool

We foresee a continued moderation in inflation into 2025. However, there could be bumps along the way. Stubborn pressures within the housing sector present the most upside risks to our forecasts.

Headline CPI inflation

Year-over-year percent change

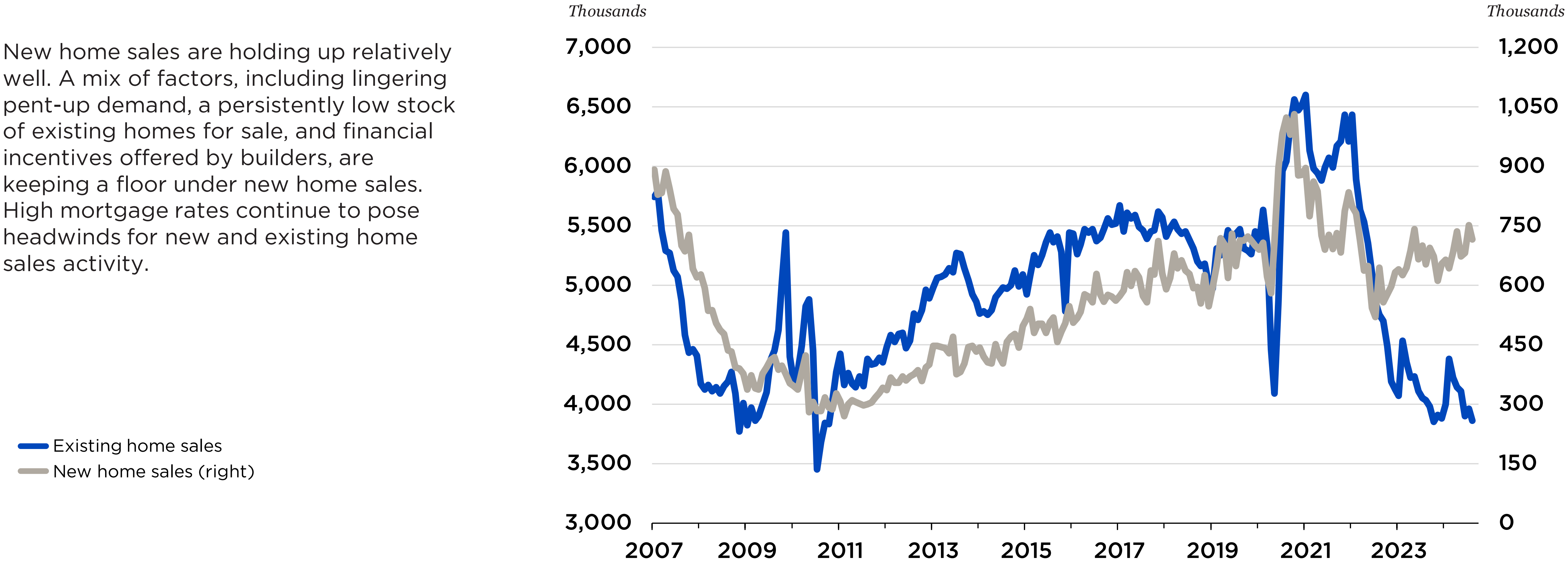


Source: Bureau of Labor Statistics, Haver Analytics, Nationwide Economics

New home sales fare better than existing home sales

New home sales are holding up relatively well. A mix of factors, including lingering pent-up demand, a persistently low stock of existing homes for sale, and financial incentives offered by builders, are keeping a floor under new home sales. High mortgage rates continue to pose headwinds for new and existing home sales activity.

Housing activity

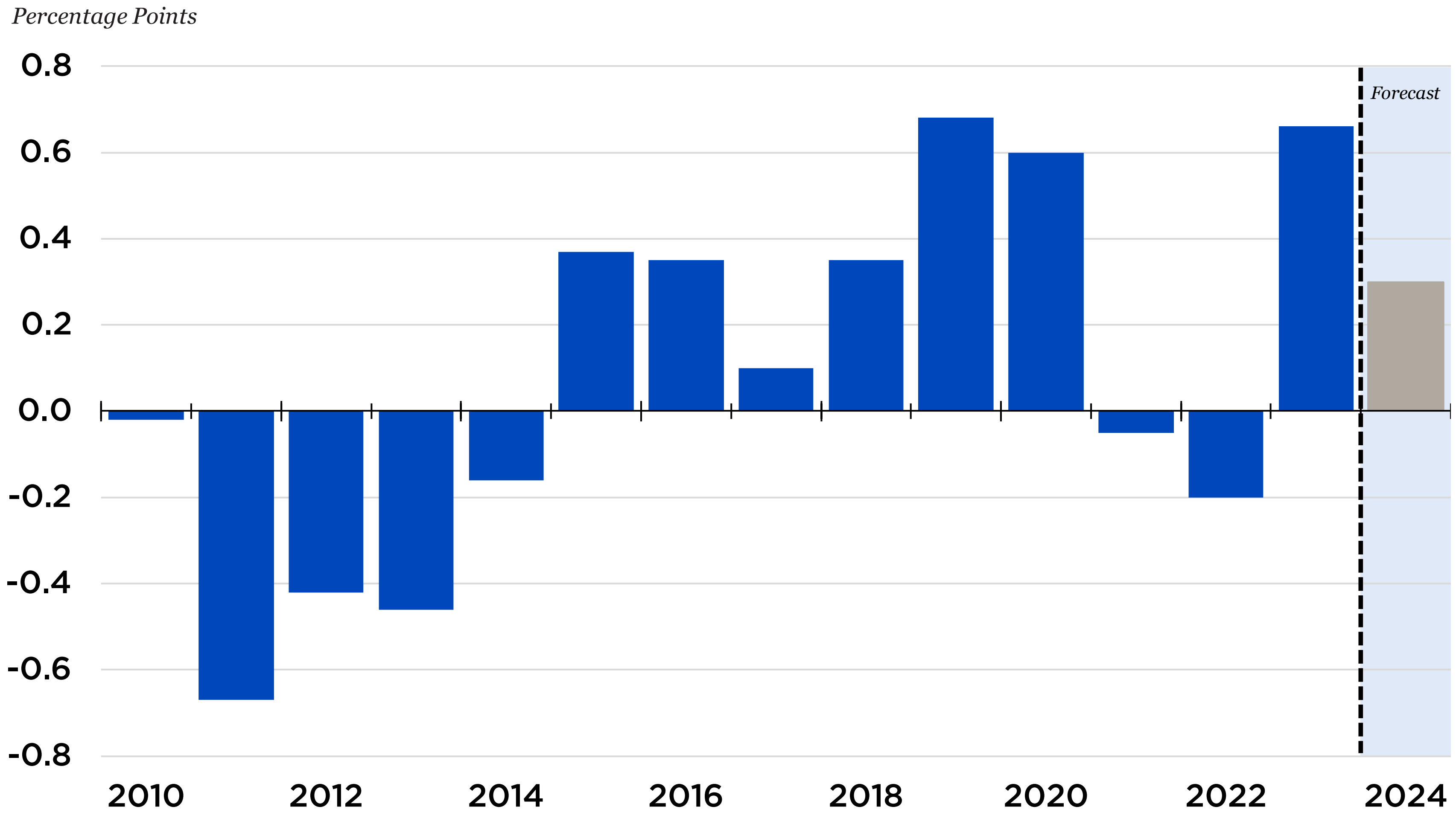


Source: National Association of Realtors, Haver Analytics, Nationwide Economics

Less support from fiscal spending

Total government spending added roughly 0.7 percentage points to GDP growth in 2023. We expect fiscal policy to only mildly boost economic growth in 2024. Whether it is a Republican or Democrat in the White House next year, policymakers are unlikely to curtail spending in 2025.

Contribution of government spending to GDP growth



Source: Bureau of Economic Analysis, Haver Analytics, Nationwide Economics

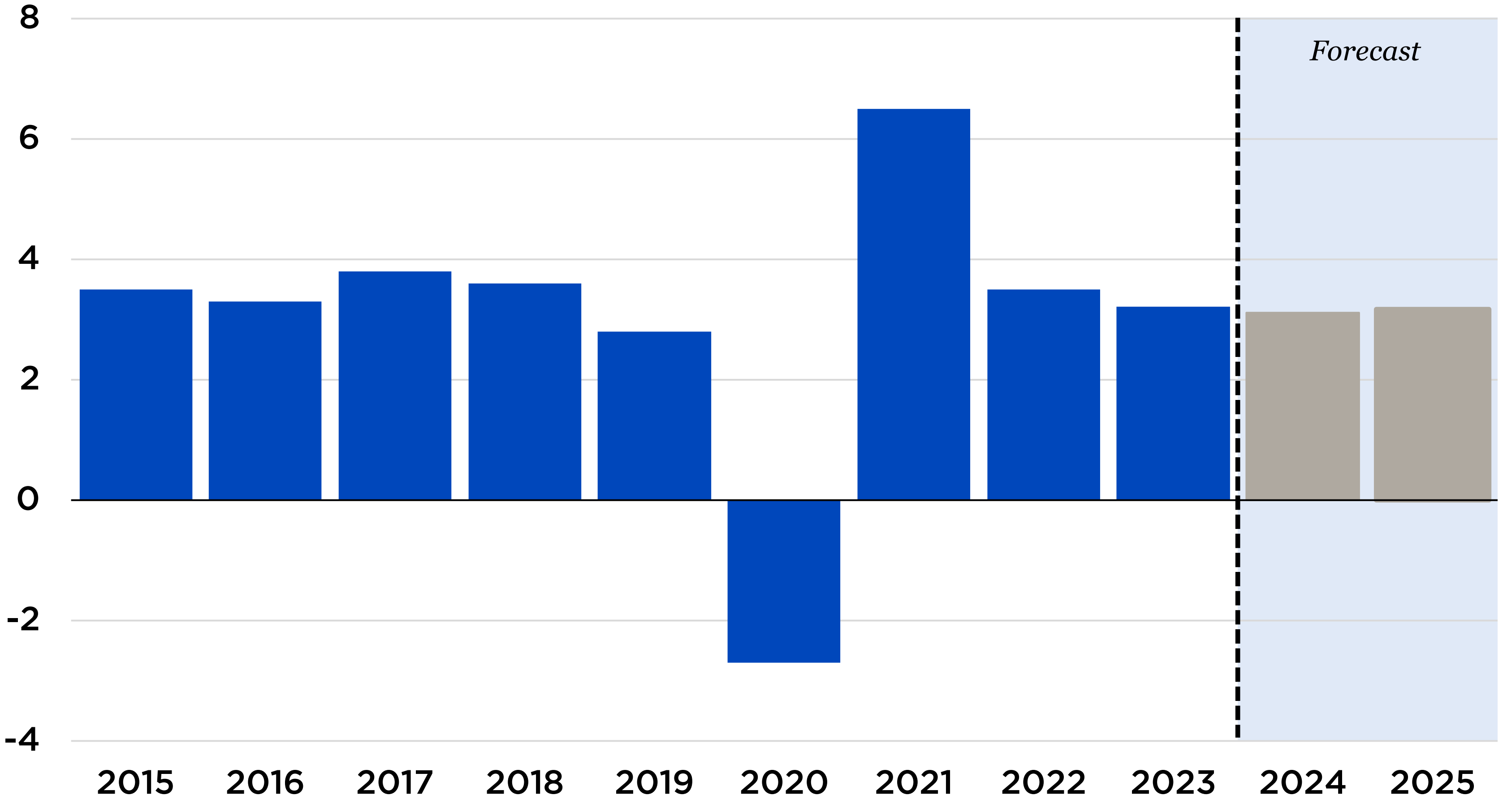
Lackluster global growth

Overseas economic data are painting a relatively grim picture. Global growth will be subpar, with Europe staying soft and China's economy unlikely to expand strongly. A new round of stimulus in China presents some upside risks to our forecast.

At the same time, geopolitical risks remain high amid ongoing conflicts in certain parts of the world and lend downside risks to our outlook.

Global GDP growth

Year-over-year percent change



Note: Forecast includes Nationwide Economics' latest U.S. projections
Source: International Monetary Fund July 2024 World Economic Outlook, Nationwide Economics

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The economic and market forecasts reflect our opinion as of the date of this report and are subject to change without notice. These forecasts show a broad range of possible outcomes. Because they are subject to high levels of uncertainty, they will not reflect actual performance. We obtained certain information from sources deemed reliable, but we do not guarantee its accuracy, completeness or fairness.

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