Breakout Briefings
Our Worldview in Charts

May 2024

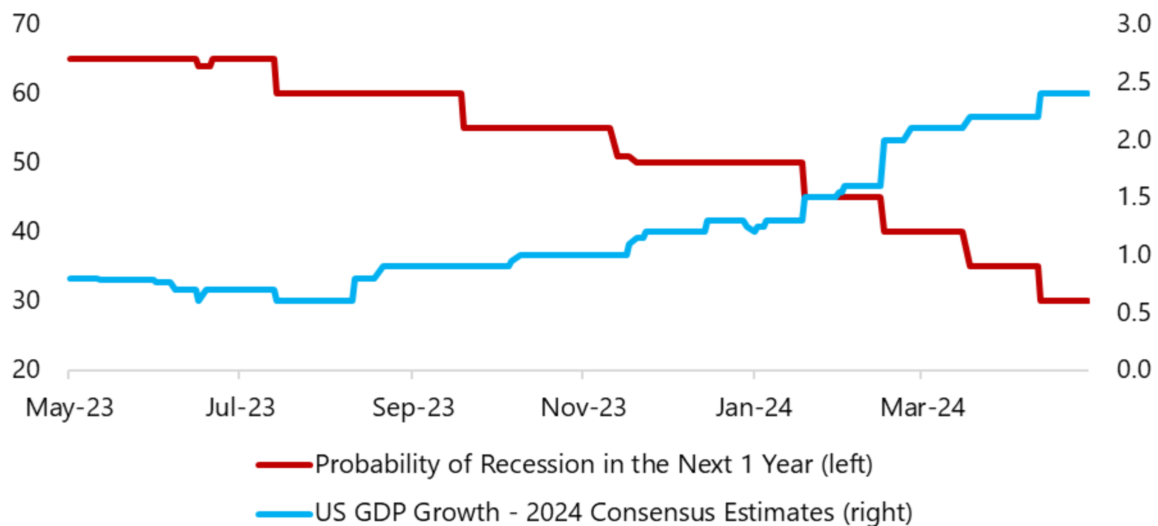
The Secret of American Resilience

Last month, the United States reported sequential GDP growth at 1.6 percent, hitting that pace or higher for the seventh quarter and confirming the remarkable story of America's economic resilience. Near universal expectations that Fed rate hikes would trigger a recession have evaporated. The question is why, and the answer has enormous consequences for global financial markets. The most overlooked reason in our view is not some special American dynamism; it is unusually generous government stimulus—which is not sustainable.

What Recession?

Over the last year, as the US economy continued to grow at an unexpectedly high pace, the Bloomberg Consensus forecast for 2024 went from dour to delighted; the average prediction for GDP growth quadrupled from 0.8 percent to 2.5 percent, and the expected probability of a recession declined from more than 60 percent to just 35 percent now (Chart 1).

Chart 1. US GDP Growth Estimates and Probability of Recession (Percent)



Source: Bloomberg, Breakout Capital Calculations. Note: All estimates are based on Bloomberg Consensus Forecasts

The Exceptional US Deficit

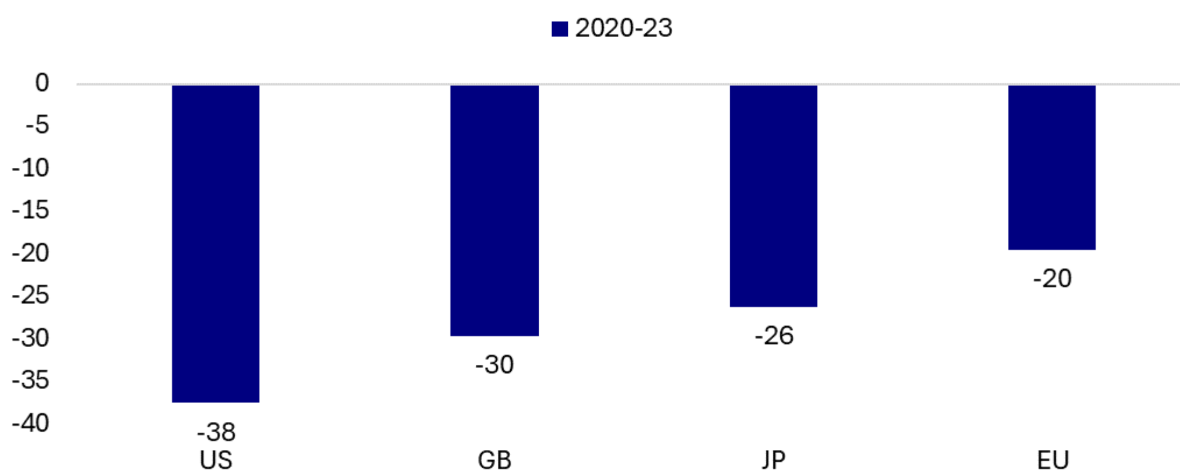
This was, in fact, the first time since 1970 that the consensus forecast had put the probability of a recession above 50 percent. Yet the downturn never came, suggesting that the conventional models are even more off the mark than usual, in these unusual post-pandemic conditions. What really stands out about the United States is that, far more than other developed countries, it kept stimulating its economy well after the recession of 2020 was over.

This stimulus has supported economic growth, as well as consumer, housing, and other asset prices. In the years since the start of the pandemic, rising deficits amounted to a cumulative 40 percent of GDP in the United States, twice the average in Europe, and a third higher than in the United Kingdom

Note: Rockefeller Capital Management does not have any investment or trading authority over the positions held by Breakout Capital and its clients.

(Chart 2). Forward estimates based on Bloomberg consensus data suggest that deficits in the United States are expected to remain significantly higher than its peers.

Chart 2: Cumulative Fiscal Deficit to GDP (Percent)

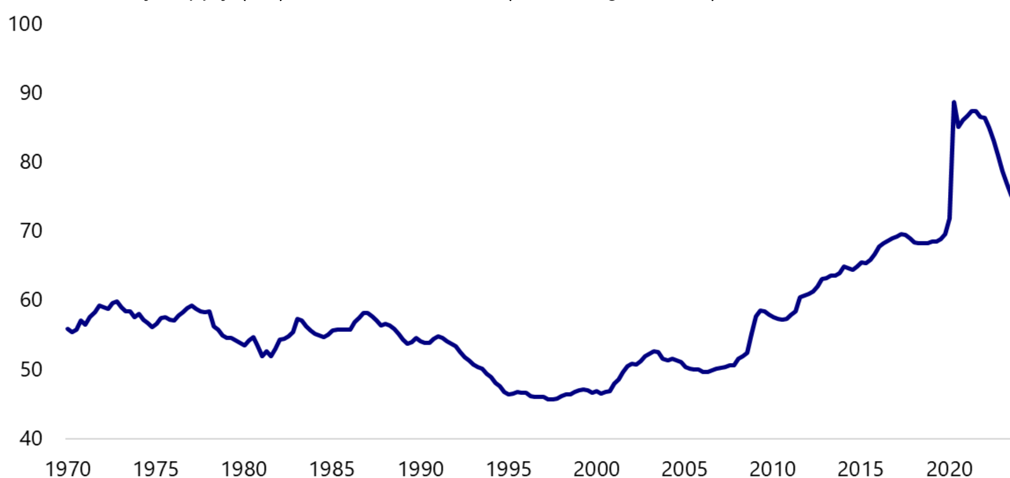


Source: National Sources, Bloomberg Estimates, Breakout Capital Calculations

Monetary Overhang

Another way to track the “legacy stimulus” still coursing through the US economy is through M2, the broad measure of money supply that includes cash held in money market accounts and bank deposits, as well as other forms of savings. In the United States, this measure increased during the pandemic by almost 20 percentage points to 90 percent of nominal GDP (Chart 3). Despite the recent moderation, it remains 5 percentage points higher than pre-pandemic levels in the United States, while it has normalized for most other developed economies including the Euro Area, the United Kingdom, and the Nordic countries.

Chart 3. Money Supply (M2) in the United States (Percentage of GDP)



Source: Haver Analytics Breakout Capital Calculations.

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When Liquidity Drowns Out Rates

This liquidity hangover has countered Fed interest rate hikes and helps explain the current behavior of asset prices. Corporate earnings are up, on strong GDP growth, but prices for stocks — not to mention bitcoin, gold and much else — have been rising even faster. This combination — higher stock valuations despite higher rates — is extremely rare. US stock market valuations have risen from 18.1x at the start of the tightening cycle to around 21.2x – an increase of almost 20 percent. This compares with an average decline of almost 15 percent over the previous 12 tightening cycles, going back to the 1950s (Chart 4).

A similar levitation act is visible in the US housing market; despite higher mortgage rates, prices have risen steadily and faster than in other developed nations.

Chart 4: US Tightening Cycles, S&P 500 Valuations since 1954

	Fed Funds Rate		S&P 500 P/E		
Tightening Cycle	Start	End	Start	End	Expansion/ Contraction
Nov 1954 - Oct 1957	0.83%	3.50%	12.3x	3.5x	-8.8x
August 1958 - November 1959	1.53%	4.00%	16.5x	16.8x	0.3x
April 1961 - November 1966	1.49%	5.76%	21.4x	14.6x	-6.8x
October 1967 - August 1969	3.88%	9.19%	18.0x	16.0x	-2.0x
February 1972 - July 1974	3.30%	12.92%	18.2x	8.9x	-9.3x
April 1977 - June 1981	4.73%	19.10%	9.7x	8.8x	-0.9x
February 1983 - August 1984	8.51%	11.64%	11.8x	10.0x	-1.8x
March 1988 - May 1989	6.58%	9.81%	14.3x	12.5x	-1.8x
January 1994 - April 1995	3.05%	6.05%	16.6x	14.1x	-2.5x
June 1999 - July 2000	4.76%	6.54%	25.2x	23.4x	-1.8x
June 2004 - November 2006	1.03%	5.25%	16.8x	15.0x	-1.8x
February 2017 - February 2019	0.66%	2.40%	18.2x	16.8x	-1.4x
April 2022 - current	0.33%	5.33%	18.1x	21.2x	3.0x

Source: Bloomberg, Factset, Shillerdata.com, Breakout Capital Calculations. Note: Tightening cycles start at the month end prior to the first meaningful month rise in Fed Funds Effective Rate, and at the peak month-end Fed Funds Effective Rate. Price-to-forward earnings is used for the full available history, prior to which price to trailing earnings is used.

The Wealth Effect

Market commentary is fixated on estimates of “excess savings,” and how they are boosting US consumer spending. We believe an equally if not more important role is played by those high stock and housing prices, inspiring consumers through the “wealth effect.” Since 2020, the total net worth of US households has risen by nearly $40tn to $157tn, driven by home and stock prices (Chart 5).

This also helps explain another unusual aspect of current US conditions—the confluence of persistent consumer price inflation and high asset prices—and why these conditions are unlikely to last. The United States simply cannot keep running a deficit near 6 percent of GDP, or six times the median level in Western Europe—not when inflation in both consumer goods and asset prices is forcing the Fed to keep rates high. It’s hard to know when the sugar rush of legacy stimulus will wear off, but when it does, expect American resilience to fade with it—and more balance to return to global markets.

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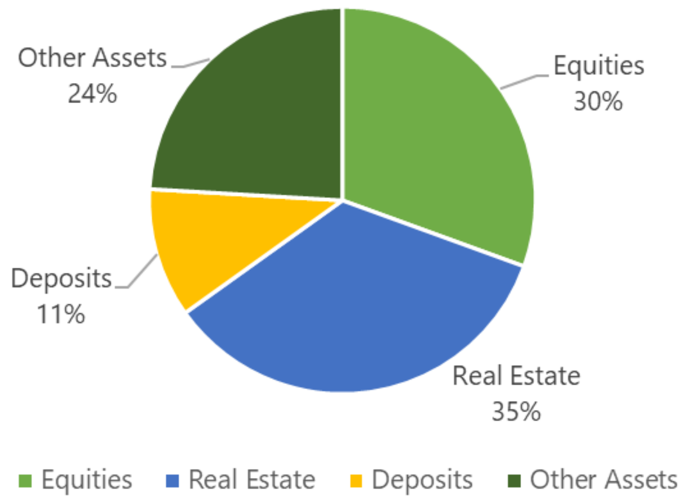
Chart 5. Drivers of the Nearly $40 Trillion Increase in US Household Assets (USD Trillions)



Source: Federal Reserve, Breakout Capital Calculations. The chart plots the change in US household assets from 2019 end to 2023 end

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