January 2025

Monthly Market Update

Economic headlines

Federal Reserve (Fed) eases monetary policy.

The Fed cut interest rates by 25 basis points in its December meeting, bringing the current range to 4.5%-4.75%. While inflation has slowed, it remains above the Fed's 2% target. Federal funds futures and the Federal Reserve Board both suggest the Fed will cut rates by an additional 50 basis points in 2025.

Fed shifts monetary policy.

Fed Chair Jerome Powel indicated that rather than establishing a predetermined set of rate cuts, the Fed will wait for economic data to weaken and/or inflation to slow before acting. Current rates are considered neutral; neither restrictive nor accommodative. The Fed's dual goals of bringing down inflation and keeping the unemployment rate low are thought to be in balance at this time.

President Trump's election creates uncertainty.

Pro-growth changes such as tax cuts, reduced regulations and initiatives to improve government efficiency may be offset by higher tariffs and policies that reduce immigrant labor. While forecasters generally see these effects evening out in the medium- to long-run (beyond 2-3 years), there is disagreement as to their short-term impact on Gross Domestic Product (GDP) and inflation.

Consumer spending drives economic growth.

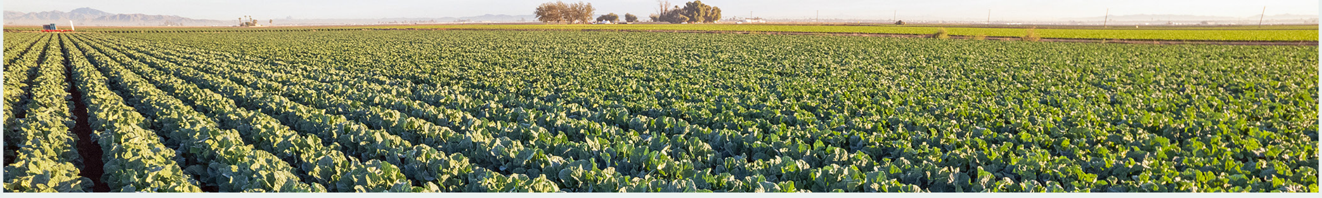
Real GDP exceeded expectations and grew by about 2.7% for the second half of the year, due to strong consumer spending in Q3. The unemployment rate remains relatively low, and nonfarm payrolls increased by nearly one million despite three catastrophic hurricanes and multiple labor strikes. Strong consumer spending was in part due to rising equity markets, which helped to support consumer confidence and offset the impacts from inflation and higher interest rates.

Positive investor sentiment drives gains in equities.

Investors remain optimistic about future growth despite persistently elevated interest rates, softening employment and other concerns. The major indexes have established several new record highs over the last few months. As of Jan. 9, the S&P 500 Index is up about 23% year over year (see chart below). Some investors worry growth may have occurred too quickly, and values may be excessive.

S&P 500 Index

Source: Nasdaq.



Industry updates

General sentiment – *The squeeze continues.*

The agricultural economy continues to face challenges, with tight profit margins expected to persist for many commodities into 2025. While production costs are anticipated to decrease or stabilize throughout the next year, they will still be the fourth highest on record (following 2022, 2023 and 2024). These high costs, combined with forecasted decade-low commodity prices, will continue to pressure producers' profitability. More than half of farmers expect that financial conditions for the agricultural sector will worsen over the next year. (Exceptions include the cattle and dairy industries which are benefitting from lower feed costs.) Good risk management strategies will be important to producers' bottom lines in 2025.

In the short-term producers expect the profitability squeeze to continue. However, many remain optimistic about the five-year outlook, with more than 50% expecting a return to more profitable times for agriculture.

Crop inputs – *Oil prices are holding steady, while cargo is being frontloaded.*

Energy prices end the year flat, but dynamics are complex.

Oil prices closed the year where they started, at $71 per barrel. Relatively stable prices over the last several months obscure complex market dynamics. Bearish economic sentiment in China, a robust U.S. dollar, increased production from the Americas (U.S., Canada, Guyana and Argentina) and Nigeria, along with lower projected trade due to the application of tariffs by the Trump Administration will likely continue to weigh on prices in 2025. Further, Trump is signaling his desire to end conflicts in Ukraine and the Middle East, which would reduce risk premiums and potentially add supply. These factors may be counterbalanced by continued production cuts by Organization of Petroleum Exporting Countries (OPEC+) members, economic growth spurred by lower interest rates, increased sanctions on Venezuela and Iran, and rising demand from India and other Southeast Asian countries. The Biden Administration imposed sanctions on Russian oil exports on Jan. 10. While this led to a jump in prices, it is unclear if the Trump Administration will support this policy. Forecasts suggest a supply glut of about 1.2 million barrels per day in 2025.

Transportation costs are mixed.

Shipping rates are mixed. In December, average bulk vessel prices fell notably due to lower Chinese demand, excess vessel capacity and the normalization of Panama Canal crossings. (Crossings fell drastically in 2023 due to severe drought.) Bulk vessel rates for grains and seed oils declined slightly but remained more stable compared to average bulk prices. Container shipping rates from Asia to the U.S. have increased as shippers frontload cargo ahead of Trump's inauguration and China's Lunar New Year. However, rates for vessels departing from West Coast ports to Asia remain relatively flat. West Coast trucking rates increased moderately in December, likely due to increased cargo volume as shippers frontload orders. Generally low energy prices are helping to keep transportation rates down.

Fertilizer prices remain stable.

Fertilizer prices are expected to remain relatively stable into 2025. USDA anticipates a 1.4% increase in corn plantings, which would boost nitrogen demand. However, rising production rates in the U.S. and abroad should offset the increased demand. Phosphorus affordability remains a challenge due to a reduction in supply from Chinese export controls, and countervailing duties placed on imports from Morocco and Russia. Potash is the most affordable of the main fertilizer ingredients due to an abundance of Canadian, Russian and Belarus supply in both U.S. and global markets. Some analysts worry that escalating conflict in the Middle East could extend to neighboring countries, potentially disrupting major fertilizer shipping routes like the Persian Gulf and the Strait of Hormuz. Urea prices have dropped 9% over the past year, influenced by declines in ammonia prices, its source material, and lower demand. Many farmers took a cautious approach to urea purchases, anticipating further price drops and reducing overall demand.

Almonds and pistachios – *Almond industry may be turning a corner.*

The almond industry may be turning a corner. Prices have increased and appear to be holding at near break-even levels. Anecdotal reports suggest the crop will come in closer to 2.7 billion pounds opposed to the 2.8 billion forecasted. Lower supply should continue to support prices. India's demand for inshell almonds increased in December. Year-to-date exports to India remain notably below the five-year average, suggesting increased buying could continue as the marketing season progresses. There are emerging reports of pest damage leading to browning and reduced yields in Kern County, but the full extent is not yet known.

Pistachio prices continue to hold flat and anecdotal reports suggest the crop is slightly smaller than forecasted. Shipments to retailers are down year over year, likely the result of a smaller crop rather than weak markets.

Apples – *Sentiment weakens on larger than expected crop.*

While the season started off on a cautiously optimistic note, sentiment has since weakened due to the larger than expected crop compressing returns. Organic, some club varieties and Honeycrisp apples are the exception, with the latter positively impacted from a crop size roughly half of last year's. There are increasing reports of orchards coming up for sale and/or being taken out of production throughout Washington. Many of these are older and/or low production, though it's also occurring among those with main varieties such as Fuji and Gala. Demand for orchards has softened, and those with long-term inefficiencies and out-of-date varietals are experiencing the largest change in values. Multiple years of weak markets has also impacted succession planning, with younger/older generations hesitant to take/pass on unprofitable operations. While conditions are challenging, they have improved from last season and shipments to retailers are strong.

Pear prices are holding strong due to the very short, good quality crop and producers with sufficient supply, located primarily in Southern growing regions.

Cattle – *Increasing prices and less beef predicted for 2025.*

Reflecting on 2024, cattle inventories continued to decline despite expectations that many producers might retain cattle and focus on rebuilding. Total 2024 beef production are forecasted to show an increase of 0.3% year over year, as opposed to initial estimates of a 3%-4% reduction. Beef production was bolstered by higher-than-expected slaughter rates and larger carcass weights. In 2024, carcasses averaged nearly 20 lbs heavier than the previous year. Despite ongoing concerns about reduced demand, retail beef prices increased by 3.5% year over year.

The ban on importing live cattle from Mexico into the U.S. due to New World Screwworm (NWS) remains ongoing as the two countries work to set up quarantine procedures. Highlighting the extent of the impact, USDA lowered their quarterly 2025 beef production forecast into Q4 2025. When cattle prices in the Southern Plains increased more than $15 per cwt during the month of December, the USDA also responded by increasing their 2025 cattle price forecast.

Beef production for 2025 is forecasted at 25.6 billion pounds, down 5% from the previous year. Cattle prices are forecasted to modestly increase, while domestic beef consumption is expected to decrease by 3.5% largely due to less beef production and higher prices.

Dairy – *2025 looks to be a more favorable year for dairies.*

Dairies are entering 2025 in a much stronger position than they were a year ago, and all indications point to much stronger returns for dairies in the coming year. Feed is inexpensive and readily available. Western dairy feed costs dropped by more than 20% in 2024, with hay prices at their lowest levels in the past four years. Despite downward pressure on milk prices throughout 2024 Q4, cheese and butter prices have steadied since December, with milk prices likely to follow suit. Notwithstanding lower milk prices during Q4, margins for the period are still expected to be the highest in the last decade for most producers. Dairy margins for Q1 of 2025 are projected to be in the profitable given stronger milk prices and low feed costs.

Highly Pathogenic Avian Influenza (HPAI) continued to slow national milk production. Since November, more than 700 California herds have been infected, leading to a record 9.2% year-over-year drop in the state's November milk production. California's December milk production numbers will likely show an even sharper decline. In response, the Governor of California declared a state of emergency to provide funding and resources to combat the spread. In AgWest's territory, HPAI has been detected in California, Idaho, and Nevada so far and it is likely to spread to other states in 2025, causing temporary drops in milk production. To identify HPIA cases faster and limit spread of the virus, USDA has mandated bulk testing of milk supplies starting Dec. 16, 2024. USDA has created Financial Assistance Programs to help offset the cost of testing and milk losses.

Forest products – *Industry remains challenged by housing market.*

Lumber prices ended the year up 9%, though they generally remain at break-even levels. Housing starts ended the year slightly down at 1.3 million units, driven by declines in the multi-family sector. Apartment construction is slowing due to persistently elevated interest rates, economic uncertainty and flat rent growth. Markets appear increasingly oversupplied, and this suggests multi-family construction has limited upside potential in 2025. Single-family home starts are likely to remain flat until the spring when the weather improves.

Log prices were generally flat across the Northwest, while those in Southern Oregon appear to be on an upswing due to lower log supply. Snow depth is building across the Cascades, suggesting loggers will slow cut levels and/or focus on lower elevation sites. An amendment to the Northwest Forest Plan, governing federally-managed lands, was proposed mid-November and is intended to reduce wildfire risk. The amendment proposes four alternative ways forward, three of which would, to varying degrees, increase harvest levels on public lands. It remains unclear how likely this amendment is to pass.

Hay – *Hay prices stabilize in 2024 amid high inventory levels.*

In 2024, hay prices fell by more than 20% from the previous year with the average national hay price at $159 per ton. Prices are expected to remain low in 2025 due to high on-farm inventory levels and challenging demand. On-farm hay stocks in the West reached 10.4 million tons on Dec. 1, 2024. While this reflects a 6.2% year-over-year decrease, there is enough hay on hand for livestock producers to replenish feed inventories. Slow markets and mild winter conditions have reduced the demand for feed-quality hay in the West.

Dairies are slowly purchasing hay, which is competing with lower-priced feed alternatives like silage and almond husks. Improved milk prices should allow dairies to move away from purchasing hay strictly on an as-needed basis and feel more confident in making purchases as required. However, a smaller national herd (both cattle and dairy) will further reduce domestic hay demand. International demand has been sluggish. Despite expectations of increased sales in the winter, China hasn't boosted its hay purchases, likely due to governmental policies aimed at reducing their national dairy herd. Furthermore, a strong U.S. dollar has hindered export sales from other key international buyers.

As 2025 begins, drought and water availability are major concerns for hay growers. More than 48% of alfalfa acres are in drought, with weather forecasting models predicting drier conditions in the Southwest over the next few weeks. Persistent drought could impact hay production. A short hay supply could rally hay prices.

Lemons and oranges – *Prices are down for both navel oranges and lemons.*

Navel prices have stabilized following a sharp drop in December and are on average 17% below last year's levels. The crop's small size profile is leading to high prices for large fruit and low prices for smaller fruit. Global juice supply is down significantly due to Brazil's short crop. While juice prices increased significantly in response, low returns continue to challenge growers. USDA's January production estimate suggests flat year-over-year supply for navels and a 10% year-over-year decline in Valencias. USDA also reports orange acreage and production in Chile and South Africa, the largest foreign suppliers to the U.S., will rise in 2025.

Lemon harvest is picking up in the Central Valley where recent rains have led to an increase in fruit size. Fruit sizes remain smaller in the southern growing region. Prices are down slightly from last season and fell 3%-9% in December across small to medium sizes. Imports have wrapped up for the season. USDA reports acreage and production will increase in Chile in 2025, the largest foreign supplier to the U.S., and decrease in Argentina, the second largest supplier to the U.S.

Potatoes – *Producers face limited planting options with falling commodity prices.*

In 2024, potato acreage and open market prices in the Northwest decreased due to fewer contracted acres and excess potato supply. Potato processors continue to post lower earnings citing weak restaurant traffic and growing global supply imbalances. Given stress in the processing sector and continued excess potato supplies, contracted acres are likely to decline in 2025.

Despite challenging conditions, potatoes remain a contender for 2025 planting decisions. Prices for many rotation crops fell by 15%-25% in 2024, so producers have few viable alternatives.

Profitability will be a challenge in 2025. The prospect of lower input costs will likely not be enough to offset lower commodity prices.

Wheat – *Challenges persist in 2025.*

In 2025, wheat growers' profitability will largely depend on effectively managing production costs and implementing risk management and diligent grain marketing strategies. With wheat prices projected at $5.80 per bushel for the 2025-26 crop, most producers are expected to operate below or near break-even levels. USDA forecasts minimal relief for production costs, with 2025 wheat costs estimated at $386.14 per acre, just $2.02 per acre less than in 2024. This reduction is insufficient to counterbalance the significant drop in wheat prices in 2024 when winter and spring wheat prices dropped an average of $1.20 per bushel. Producers are forecasted to plant 46 million acres, 3.6 million fewer than the previous year.

Despite an overall pessimistic outlook, shifts in the global wheat supply could support higher prices. Both the European Union and Russia are expected to have lower production in 2025. Russia is also reducing their export quota by two-thirds, effective from mid-February through June, to balance their domestic needs with production. Despite a strong dollar, U.S. wheat exports for the 2024-25 crop are expected to increase by 20% year-over-year from the 50-year low reached in 2023-24, primarily due to lower exports from competitors. If the U.S. dollar weakens, U.S. wheat exports could see an even greater increase.

In late December, Congress passed the American Relief Act of 2025, which will provide $9.8 billion in relief payments to 20 crops. This one-time payment to producers is based on 100% of planted acres and 50% of prevented planting acres for the 2024 crop year, aiming to mitigate some of the losses incurred. It is estimated that producers will receive the following assistance payments per acre: $31.80 for wheat, $21.76 for barley, $26.76 for canola, $19.32 for lentils, $16.16 for dry peas, $17.48 for flaxseed, $21.77 for small chickpeas, $24.16 for large chickpeas, and $11.42 for mustard seed.

Payments are expected to be distributed to growers sometime in the spring of 2025, with a cap of $250,000 for producers who derive more than 75% of their income from farming.

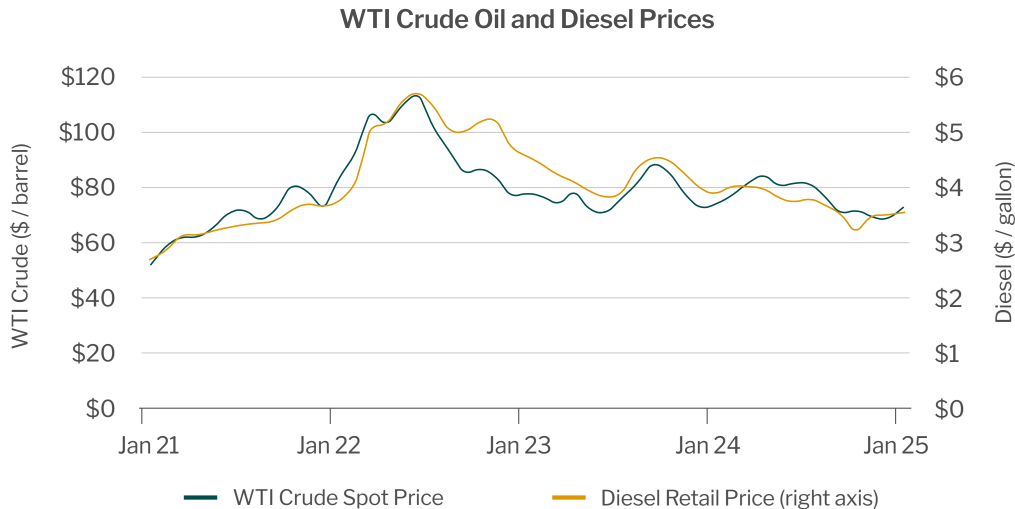
Wine and wine grapes – *Wine sales may be nearing a bottom.*

Recent data supports that wine sales are on track to have declined again in 2024, but the rate of change has slowed. Some think the industry may be nearing a bottom with markets returning to near normal conditions following the pandemic's off-premise and Direct-to-Consumer sales boom. Despite some optimism, wine inventory levels remain elevated and demand down. It will likely take another three to five years for the industry to balance supply with demand. The lower value wine market continues to be the most challenged, but there are reports of wineries achieving success in the $40 / bottle range as well as the premium and ultra-premium categories. There has also been some success in accessing non-traditional markets such as airlines.

This harvest season saw generally good quality fruit, average yields in Oregon and Washington and very low yields in California. Oregon observed a bump in winery visits in December; however, the general trend seems to be weakening across the region due to decreasing discretionary income and lower rates of alcohol consumption. In California and Washington, there are numerous reports of growers considering or actively removing acres and/or utilizing minimal inputs. Reducing inputs could have longer term implications for productivity and/or costs. The number of wineries for sale in California and Oregon has increased. While values have held relatively constant, transaction levels are flat to down.

Data and trends

This section presents select economic indicators to help producers gauge the direction of their business. These metrics reflect current market dynamics and their potential impact on operations. Come back each month to stay informed and adapt swiftly to the ever-changing economic landscape.

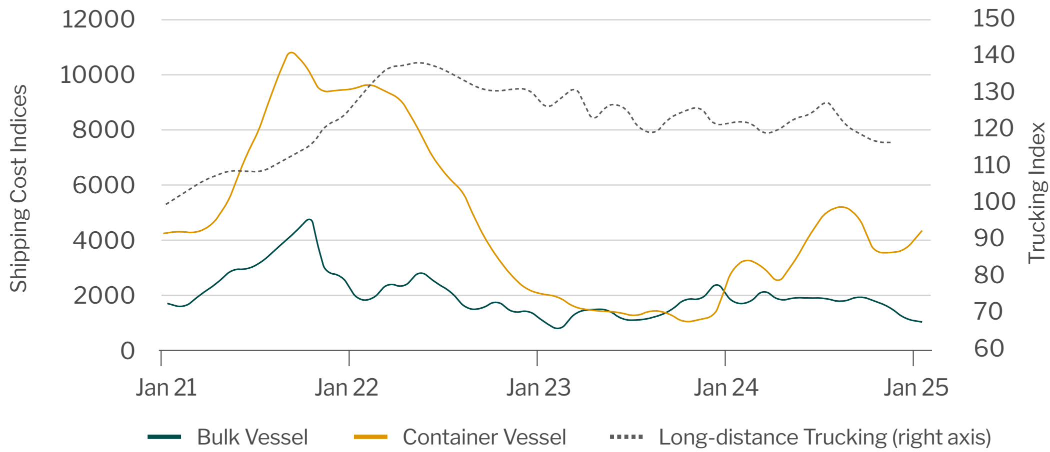


Source: U.S. Energy Information Agency.

Observation: Oil prices increased mid-January as markets anticipated disruptions from U.S. sanctions on Russia, which target their oil and gas revenues. This was coupled with higher demand due to cold weather in the Midwest and Europe. Despite these factors, supply and demand conditions seem relatively balanced.

About this indicator: The West Texas Intermediate (WTI) crude oil price is a benchmark for oil pricing and influences the cost of fuels like diesel, which is essential for running farm equipment and transporting goods.

Transportation Price Indices



Source: Bloomberg. Freightos. U.S. Bureau of Labor Statistics.

Observation: Container shipping costs rose as buyers frontloaded cargo ahead of Trump's inauguration and China's Lunar New Year. West Coast trucking rates also increased moderately due to this frontloading. Meanwhile, bulk vessel prices dropped significantly due to lower Chinese demand, excess vessel capacity and the stabilization of Panama Canal crossings.

About this indicator: The long-haul trucking index measures the changes in trucking freight rates over time. The Baltic Dry Index measures the average global cost of shipping bulk materials, including grains, sugar, metals, and others. The container index measures the average global cost of shipping containers. Shipping prices vary by route and carrier size based on market dynamics and may move independently from global averages (i.e., the cost to ship goods from the West Coast to Asia could remain flat even if global rates are increasing).

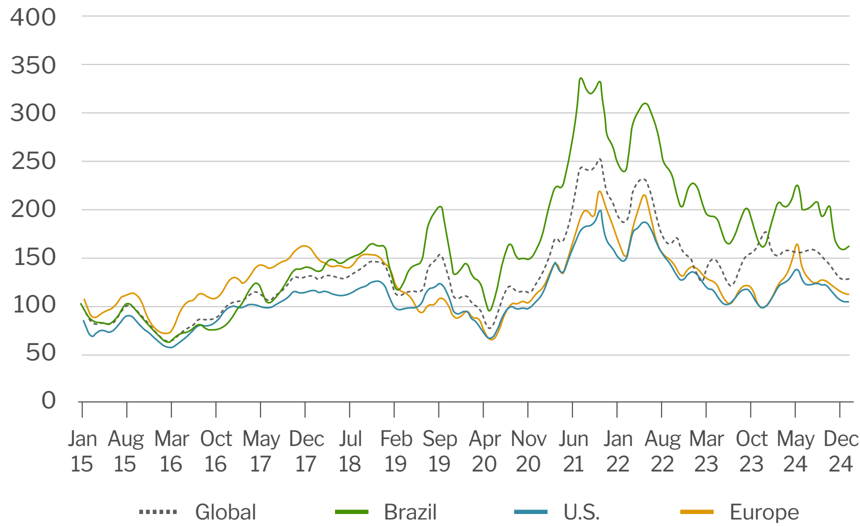
DXY Index

Source: Bloomberg.

Observation: The dollar has climbed to two-year highs, driven by stronger-than-expected employment data in early January and the general perception that President Trump's reelection is positive for the U.S. economy.

About this indicator: The DXY index measures the strength of the U.S. dollar against a basket of foreign currencies. The strength of the U.S. dollar impacts the competitiveness of agriculture producers in foreign markets. As the dollar strengthens, U.S. producers & exports become less competitive, and vice versa.

Grain and Oilseed Freight Indices



Source: International Grains Council.

Observation: Shipping costs for grains and oilseeds have declined the last several months, which should benefit West Coast producers. Costs associated with U.S. and Europe grains track closely, while those from Brazil are notably more expensive.

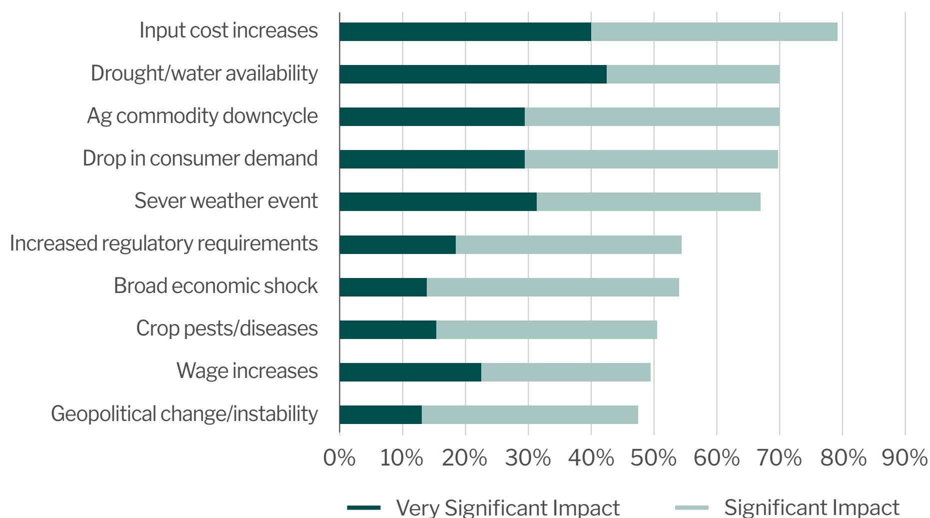
About this indicator: The International Grains Council produces the Grain and Oilseed Freight Index to better inform the global agriculture economy on bulk shipping costs. While the Baltic Dry Index is the typical indicator used when tracking bulk shipping rates (see transportation chart above), this index isolates the costs for shipping grains and oilseeds.

Spotlight

AgWest AgTrends Survey: *Key customer insights for the next 18 months*

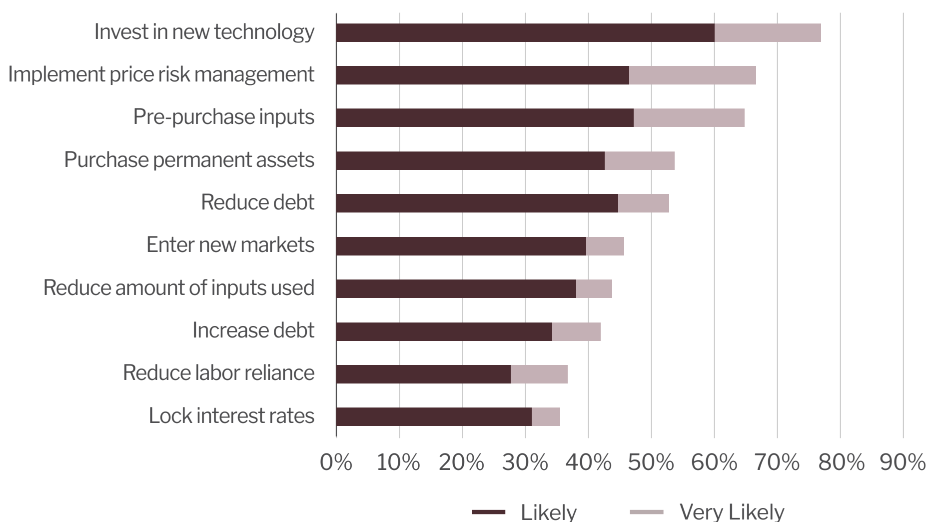
As the new year begins, it's crucial to examine the trends that are likely to influence the agricultural landscape. This article explores opportunities and threats ag producers anticipate over the next 18 months. These findings are from AgWest's AgTrends Survey, completed by 460 AgWest customers this fall.

Producers expect to face several significant challenges over this period. The top five threats identified by AgWest producers include rising input costs, drought, agricultural commodity downturns, declining consumer demand and severe weather events.



Source: AgWest AgTrends Survey.

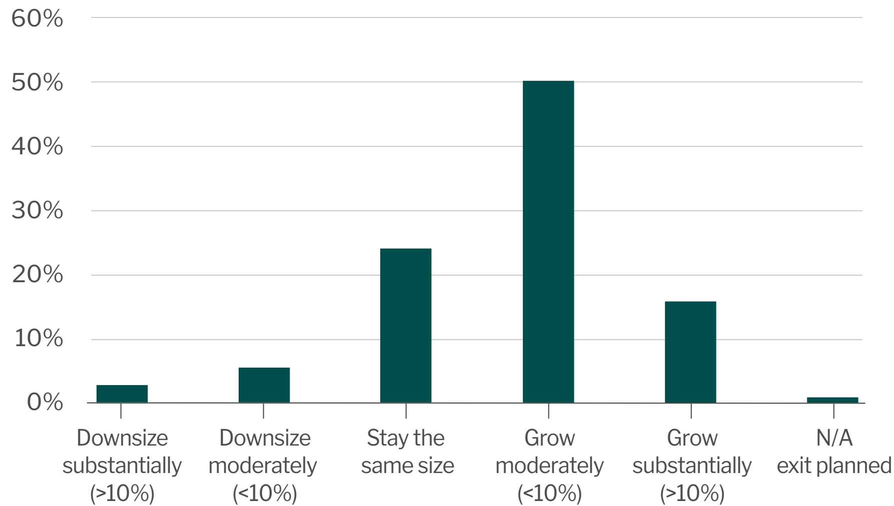
To address these issues, many producers plan to enhance operational efficiency, reduce costs by pre-purchasing inputs and lowering debts, and diversify their operations. Notably, 68% plan to invest in new technology and 59% are considering implementing price risk management strategies such as hedging and crop insurance.



Source: AgWest AgTrends Survey.

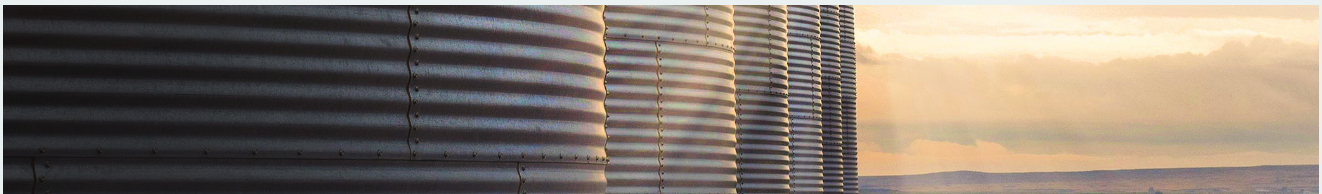
The agricultural sector is poised to adapt and innovate in response to evolving market dynamics with several growth opportunities ahead for producers. Nearly half of respondents are likely to enter new markets, focusing on niche markets, exports, and direct-to-consumer channels. Consumer trends like local sourcing, trendy foods and beverages, and organic products are viewed as potential growth avenues.

In the long term, over two-thirds plan to expand their operations within the next five years. Nearly half of producers expect modest growth in their business. In the next decade, 50% of producers aim to transition their businesses to the next generation.



Source: AgWest AgTrends Survey.

The next 18 months will undoubtedly be a period of significant change for the agricultural industry. By staying informed and proactive, producers can navigate these challenges and take advantage of opportunities that lie ahead.



Quarterly Economic Update

Executive Summary

The U.S. economy continues to expand at a moderate pace despite employment showing signs of cooling and inflation remaining above the Federal Reserve's target. President elect, Donald Trump, is preparing to assume the political reigns of the federal government, which is adding a layer of uncertainty to the economic landscape. Other concerns for the outlook remain in play, including rising federal deficits, weakness in the commercial real estate sector, elevated geopolitical risk, weak global growth and the accumulated impact of high consumer inflation over the last four years. Despite all this uncertainty, in 2024 the equity markets performed better than expected with the major indexes establishing several new highs and the S&P 500 index gaining over 23%. Some investors worry growth may have occurred too quickly, and values may be excessive, but traders and investors are pushing equities higher as 2025 gets underway.

Economic Drivers

Federal Reserve (Fed) eases monetary policy.

The Federal Open Market Committee (FOMC) cut policy rates by 100 basis points in 2024 and while inflation has slowed, it remains above the Committee's 2% target. Meanwhile, labor market conditions have cooled and unemployment has increased moderately. Fed officials view the risks of rising unemployment and higher inflation as roughly balanced. The December rate cut of 25 basis points reduced the federal funds target rate range to 4.25%-4.50%.

Fed shifts monetary policy.

Fed Chair Jerome Powell indicated monetary policy has moved into a new phase given policy rates are at/near neutral levels, or are neither restrictive nor accommodative. Rather than establishing a predetermined set of rate cuts, the Fed will now wait for economic data to weaken and/or inflation to further slow before acting. Indications of strengthening data in either category could keep the Fed sidelined for an extended time. Looking forward:

- Federal funds futures suggest the Fed will cut rates by an additional 50 basis points in 2025, which matches projections by Federal Reserve Board members and staff. Futures indicate the next rate cut could occur as early as May, with an additional rate cut in the fourth quarter. These projections continuously change based on market conditions and economic data.
- The latest economic projections for growth, employment and inflation by Federal Reserve Board members and staff lead them to expect the funds rate to decline to 3.25% by 2027, consisting of 50 basis point reductions in 2025 and 2026, and 25 basis points in 2027.

Federal Reserve Projections

Indicator	2024	2025	2026	2027
Real GDP growth	2.50%	2.10%	2.00%	1.90%
Unemployment rate	4.20%	4.30%	4.30%	4.30%
Core PCE inflation	2.80%	2.50%	2.20%	2.00%
Federal funds rate	4.50%	4.00%	3.50%	3.25%

Data as of January 9, 2025 – Source: Federal Reserve Board.

President Trump's election creates uncertainty.

Pro-growth changes such as tax cuts, reduced regulations and initiatives to improve government efficiency may be offset by higher tariffs and policies that reduce immigrant labor. While forecasters generally see these effects evening out in the long run, there is disagreement as to its short-term impact on Gross Domestic Product (GDP) and inflation. Other factors like lower expected energy costs may help offset the inflationary impact of tariffs. While the economic implications of a Trump presidency are unclear, it will take time to implement various initiatives and programs.

Consumer spending drives economic growth .

Real GDP exceeded expectations and grew by about 2.7% for the second half of the year, largely due to strong consumer spending in Q3. The unemployment rate remains relatively low, and nonfarm payrolls increased by nearly one million despite three catastrophic hurricanes and multiple labor strikes. Strong consumer spending was in part due to rising equity markets, which helped to support consumer confidence and offset the impacts from inflation and higher interest rates.

Positive investor sentiment drives gains in equity markets.

Investors remain optimistic about future growth despite persistently elevated interest rates, softening employment and other concerns. The major indexes have established several new record highs over the last few months. As of Jan. 11, the S&P 500 index is up about 23% year-over-year. Some investors worry growth may have occurred too quickly, and values may be excessive.

Economic and geopolitical headwinds present risk

There are several risks to economic projections, including:

- Rising prices and debt loads are leading to financial stress, particularly among low wage earners, and this may eventually slow consumer spending. Delinquencies for consumer credit cards and auto loans are trending higher.
- Rising federal debt levels have the potential to increase inflation and treasury yields, weaken the U.S. dollar and reduce the capacity of the U.S. government to respond to an economic crisis and war. The debt to GDP ratio is now at about 124% and continuing to grow. Congress is unlikely to respond until a crisis arises or it creates significant hardship on the American people.

- Conflicts in the Middle East and Ukraine are disrupting global trade flows and dampening economic growth, and an escalation of either would worsen conditions. President Trump appears committed to ending both wars.
- The threat of labor strikes is rising, which leads to disrupted economic activity as businesses adjust their strategies and/or hold off on investments.
- Collaboration among Russia, China, India and Brazil (among other smaller countries) is increasing, which could weaken the U.S. dollar over time.
- There are reports China is working to spur economic growth via monetary and fiscal policy actions. This may result in higher raw material prices, provided their efforts are effective.

Economic data and trends

Interest rates

U.S. Treasury yields have increased 75-100 basis points following the Fed's 50 basis point rate cut in September and guidance that more would be coming, actions that led market participants to worry policymakers may be losing some of their diligence on fighting inflation. Market fears remain given subsequent rate cuts in November and December. Fed Chair Powell's Dec. 18, 2024 post-FOMC meeting comments related to slowing the pace of rate cuts seemed to ease market worries for a time, but recent employment data is reigniting fears that monetary policy may be too accommodative. The market seems to be comfortable with the current level of policy rates given their outlook for growth, employment and inflation. Look for yields to remain elevated until there is a shift in economic conditions. Adjustment to fiscal policy could impact the outlook for yields.

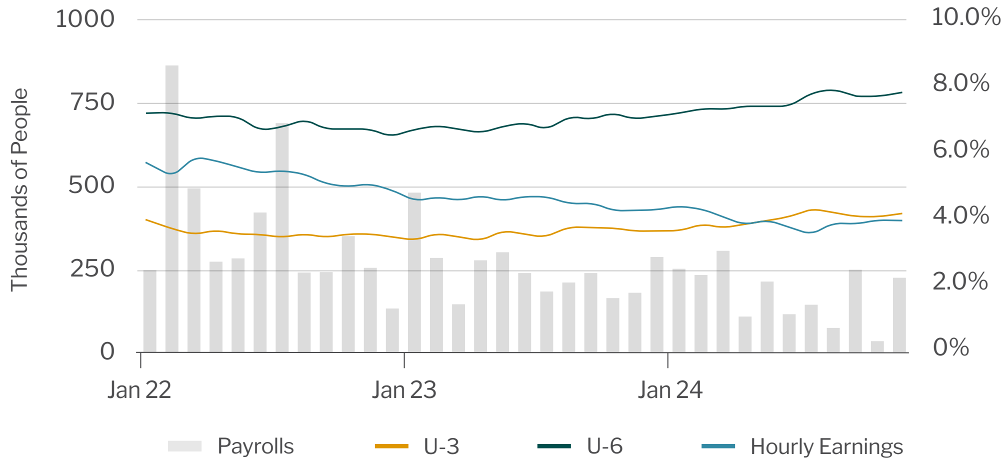
Data as of January 9, 2025 – Source: U.S. Department of the Treasury.

Employment

Nonfarm payrolls had a rough August and October due to Hurricanes Beryl, Helene and Milton. There were both strikes and threats of strike in 2024, which led to increases in real wages for union workers by about 6%. The national U-3 unemployment rate is expected to finish the year at 4.2% with monthly nonfarm payrolls growing by an average of around of 180,000. The U-6 unemployment rate, a broader measure that includes marginally attached and discouraged workers, is expected to end 2024 at 7.8%.

Provided the economy continues to expand at 2.5%-3.0% during 2025, look for a limited increase in the unemployment rate while nonfarm payrolls average around 150,000. In contrast, weaker economic growth will likely translate into higher unemployment. Average hourly earnings will likely grow at a rate of 3.7%-4.0% provided consumer demand remains robust and there is limited negative impact from net immigration flows. Weekly jobless claims data remains well within the range of a solid labor market. An increase to 300,000 to 350,000 in weekly claims would signal material weakness in employment with rising unemployment and the possible onset of a recession.

Jobs, Unemployment and Hourly Earnings



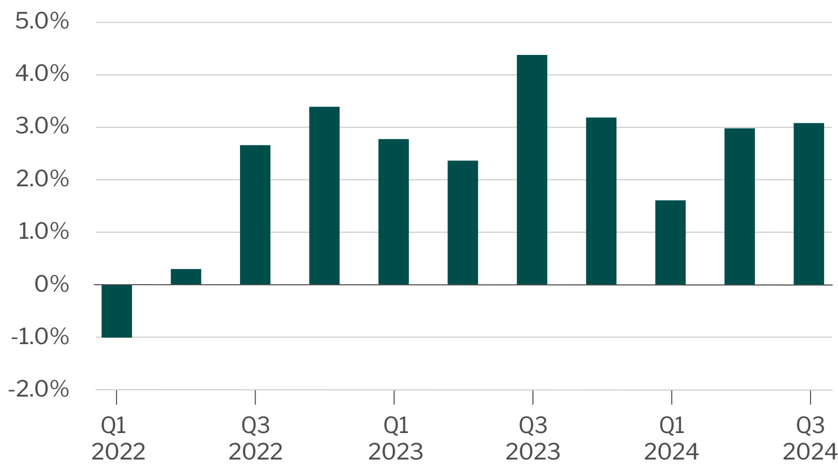
Data as of January 9, 2025 – Source: Bureau of Labor Statistics.

Gross Domestic Product

The third estimate for Q3 2024 GDP came in at 3.1%, which exceeded Q2 2024 GDP of 3.0%. Fed projections indicate 2024 real GDP expanded by 2.5%. Consumer spending drove most of the economic growth, though a boost also came from business spending and government purchases. Housing was a drag on growth for much of the year with the change in inventories being mostly offset by net exports.

The Fed expects GDP to expand by an average of 2.1% for 2025. Expect consumer spending to drive growth with contributions from business spending and government purchases. Higher mortgage rates will restrict any contributions from housing. With energy prices a factor in transportation and manufacturing costs, cheaper energy could also translate into stronger growth and greater competitiveness in foreign markets. The Federal Reserve Bank of Atlanta forecasts Q4 2024 real GDP growth to be around 2.0% and 2.2% for Q1 2025.

Real Gross Domestic Product (GDP)



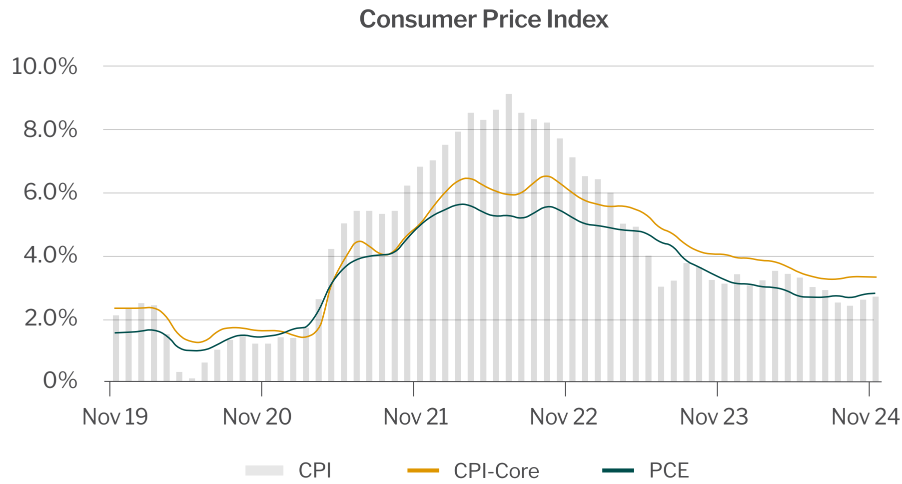
Data as of January 9, 2025 – Source: U.S. Bureau of Economic Analysis.

Inflation

Year over year consumer price inflation was 2.7% in November, up from a low of 2.4% in September and a high of 3.5% in March. Although somewhat choppy, inflation remains on a gradual downward trajectory. Continuing the downward trend may be a challenge depending on many factors discussed above. Over the last four years the CPI is up over 20%, including food and shelter components. Most of the upward pressure on prices is due to increases in the cost of services while commodities inflation has remained muted.

Core-CPI (CPI less food and energy) increased 3.3% year over year for September, October and November. The driver for core inflation continues to be shelter (+4.7%) and transportation services (+7.1%). Motor vehicle insurance costs increased 12.7% for the twelve months ending in November, which is likely a one-off event and is expected to be less of a factor going forward.

Core-Personal Consumption Expenditure (Core-PCE, the Fed's preferred inflation metric), increased 2.8% for twelve months ending November. The Fed's target for core PCE is 2.0%. Further declines in inflation may be challenging as the economy remains resilient. Slowing consumer demand and increasing unemployment could exert downward pressure on inflation metrics.



Source: U.S. Bureau of Labor Statistics. U.S. Bureau of Economic Analysis.