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MARKET
UPDATE
2024 Q3

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The opinions expressed in this article are Mr. Hanson's own and do not necessarily reflect the position of all advisors at Ankerstar Wealth.

3Q 2024 Market (and Real Estate) Update:

What I wrote last quarter on both the economy and real estate market remains largely intact for this third quarter (see Joel Market Update 2024Q2) with the following minor updates:

- It now looks like the Federal Reserve may not cut interest rates this year or if they do, at most 1-2 cuts. Inflation remains sticky due largely to rising auto insurance premiums and shelter (housing). This has delayed the rebound in bond portfolios; however, I expect bonds (think longer term maturities) to perform well in 2025 as rate cuts accelerate
- The market continues to be led by large tech firms (e.g., Nvidia, Apple, Amazon) and has not broadened out with strength to other sectors (yet!) as I expected. The U.S. economy looks to continue to remain strong (no recession in sight with rising wages, strong productivity, and inflation trending lower) so the market will broaden as interest rate cuts become a reality. I still believe small cap stocks with positive earnings are set to outperform going forward 12 months.

Moving on … mentioned in the last quarterly update was the long-term concern of our rising U.S. debt to Gross Domestic Product (GDP – the value of total final output of goods and services produced by the U.S. in a certain period of time) so I'd like to provide my thoughts on this topic and what variables could potentially minimize the impact. For simplification, following are key bullet points:

- 2024 U.S. GDP estimated to be $28.2 trillion
- Current U.S. debt held by the public is $27.6 trillion
- 2024 U.S. tax revenues estimated to be $5.1 trillion
- 2024 U.S. spending estimated to be $6.5 trillion … 5.7% of GDP more than revenues (adding to debt)
- 14% of U.S. GDP spent on entitlements (e.g., Medicare, Social Security)
- 7% of U.S. GDP spent on other federal programs (defense, R&D, education, highways, etc.)
- 2% of U.S. GDP spent on paying interest on our debt … and growing, especially with higher interest rates
- Public national debt on course to balloon … 2024 it will be 98% of our nation's entire GDP; estimated to rise to 110% of GDP by 2030 and 140% by 2040 and a massive 180% of GDP by 2050 (and interest on the debt will be the largest single federal expenditure)

So, what to make of these numbers? It is estimated that public national debt levels approaching 180% of GDP could have major negative impacts to our equity and bond markets. Why? As risk of government default increases, bond interest rates will rise to account for the higher risk which only exacerbates the cost of debt. The economy will weaken due to reduced government spending available for productive purposes such as direct spending on infrastructure or indirectly by increasing the money supply to fuel consumption and business investment (i.e., the stock market). Bottom line: Congress will need to take corrective action within the next 20 years or risk a potential fiscal crisis. What are their options?

1) Print more money to pay off debt. Probably the least palatable option as this would cause massive inflation and reduced confidence in the dollar, the world's reserve currency

2) Raise taxes or tax cuts to spur income (and arguably, generate more taxes) … both tools have been used in the past and history shows that revenues remain in the 16-18% of GDP range

3) Cut spending. Politicians are loath to reduce entitlements or discretionary spending (think reelection risk). By spending 24% of GDP with revenue only 17% of GDP, our deficit spending at this pace (with interest expense increasing exponentially) is untenable

While our continued deficit spending will most certainly have long term negative consequences, there are two economic variables that could blunt the spending impact by growing our GDP at a faster rate:

3) How fast the workforce expands (either through more births than deaths, increasing lifespans and/or increased immigration, both legal and illegal)

2) How quickly worker productivity grows (more output per worker)

Workforce growth is about 0.5% per year but has been slowing for a long time now. By the end of the decade, it's likely to fall to 0.4% per year. By 2045, about 0.2% per year, which includes immigration. This trend is not favorable for long term growth of our economy.
On the other hand, worker productivity has a better outlook. Output per worker has risen by 1.5% annually over the past 15 years. Recently, it has been a bit higher, likely due to remote work (less in person meetings). Pushing worker productivity up is key to long run GDP growth. History shows that education of the workforce was key to boosting productivity, however, it now appears technological progress appears to be the more important factor. Artificial intelligence has the potential to be the catalyst for major worker efficiency gains across many jobs and sectors. Coupled with the trend of more remote work, worker productivity increases are forecast to improve substantially.

The bottom line: our nation's rising debt is a major long-term concern; however, fiscal stability and continued prosperity can be maintained if we grow the economy's GDP 3 plus percent per year on average and thus the rising debt to GDP percentage can be slowed significantly. This in turn will be music to the ears of the stock market.

In summary, I wanted to shed some light on the long-term issue of our nation's debt levels (Congress will need to take corrective action soon!) but also show that for the near future, our economy is on solid ground for continued prosperity! Please reach out to me anytime at joel@ankerstarwealth.com if you have any questions on this commentary or any other question. The Ankerstar Wealth team remains committed to helping you "Maximize Life by Maximizing Wealth"!