PROSPECTS FOR THE US ECONOMY IN 2025

I was originally going to write an article on the prospects for the global economy but because the research needed to accomplish this would mean delaying the article beyond the 25th I decided to limit it to the USA, particularly now that Wall Street has had a reality check.

The Dow Jones Index representing 30 of the largest US corporations with a combined market cap of over $42 trillion has had the longest losing streak – 11 sessions up to Wednesday – since 1974. However before we get carried away, the total fall is just 6% from its peak. The catalyst for the Wednesday fall was the outlook for further FED rate cuts in 2025 which was reduced from 4 to only 2 cuts because of sticky inflation. The stock markets had banked on sustained falls in interest rates to fuel the boom in share prices.

The other fuel of course is the A.I. boom. Here too a reality check is emerging. In a previous post I wrote about the difficulties besetting scaling up. That is making these parasitic mimics more capable and responsive by increasing their capacity to consume more data. Now a much more worrying development has emerged with the latest iterations. They are becoming more uncontrollable, not so much developing a mind of their own or human traits such as deception, but simply more difficult to manage. They are failing to follow changes to their instructions, instead they are processing their original instructions while avoiding any re-directions or modifications. This inflexibility will become more important when vendors release the next big thing, agentic systems where systems compute independently or unsupervised after they are set specific tasks. Whereas hallucinating was obvious, this misdirection is obscured requiring labour time to uncover them then correct them, making them untrustworthy if not unviable. The usual silicon valley hype is beginning to lose its allure.

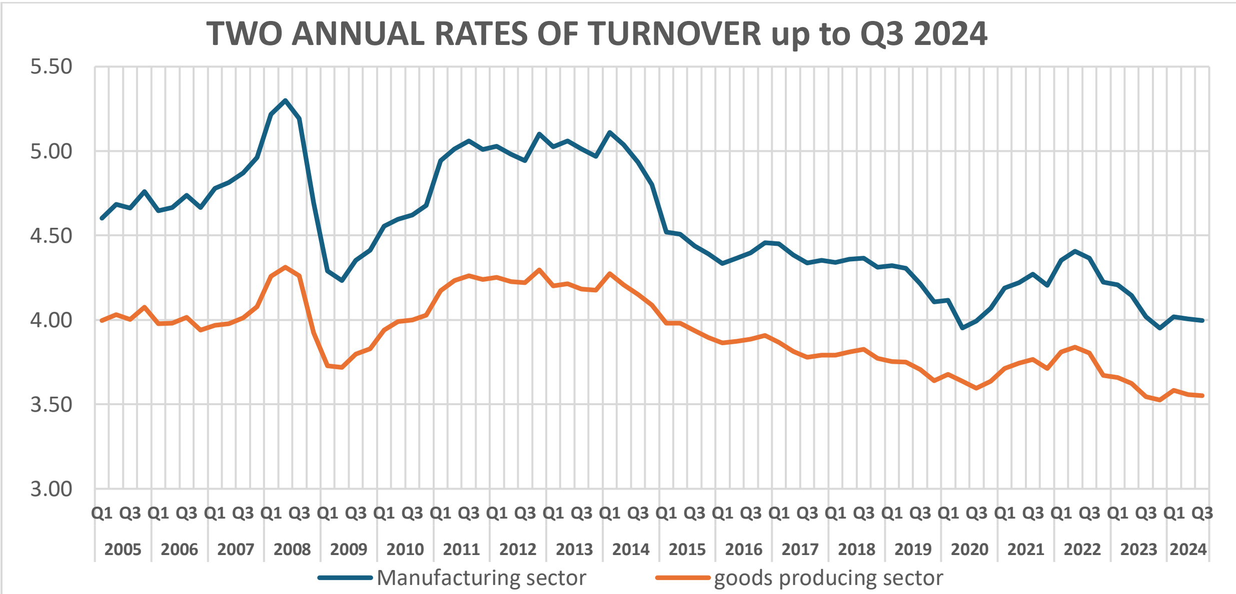
The final headwind is caused by the growing recognition that not only are these systems merely mimics, parasitic on human creativity, but that this creativity has been largely pirated from sources protected by Intellectual Property rights, that is from journalists, artists, writers, actors and so on. This issue was highlighted by the recent death of an OPENAI whistleblower Suchir Balaji who claimed he could no longer work for the company because it was stealing the works of independent creators for its own benefit. In time, the rising frequency of copyright lawsuits could de-dollarize many of these LLM companies.

Thus the A.I. hype is beginning to deflate. It was formerly based on the cultivated illusion of infinite potential, but now it appears it has only limited potential. And if this is the case then who needs all these Nvidia chips in the hope of this or that breakthrough as Microsoft has discovered. As a result Nvidia's share price is in correction territory down 12% from its peak having lost close to $400 billion in market cap. This is not to disparage the family of LLMs especially the bespoke *enterprise models* trained on the data arising from specific corporate sectors. In time the focus will shift from the vendors of these systems such as Google and OPENAI to the companies actually employing these systems by un-employing their workers.

The rate of turnover.

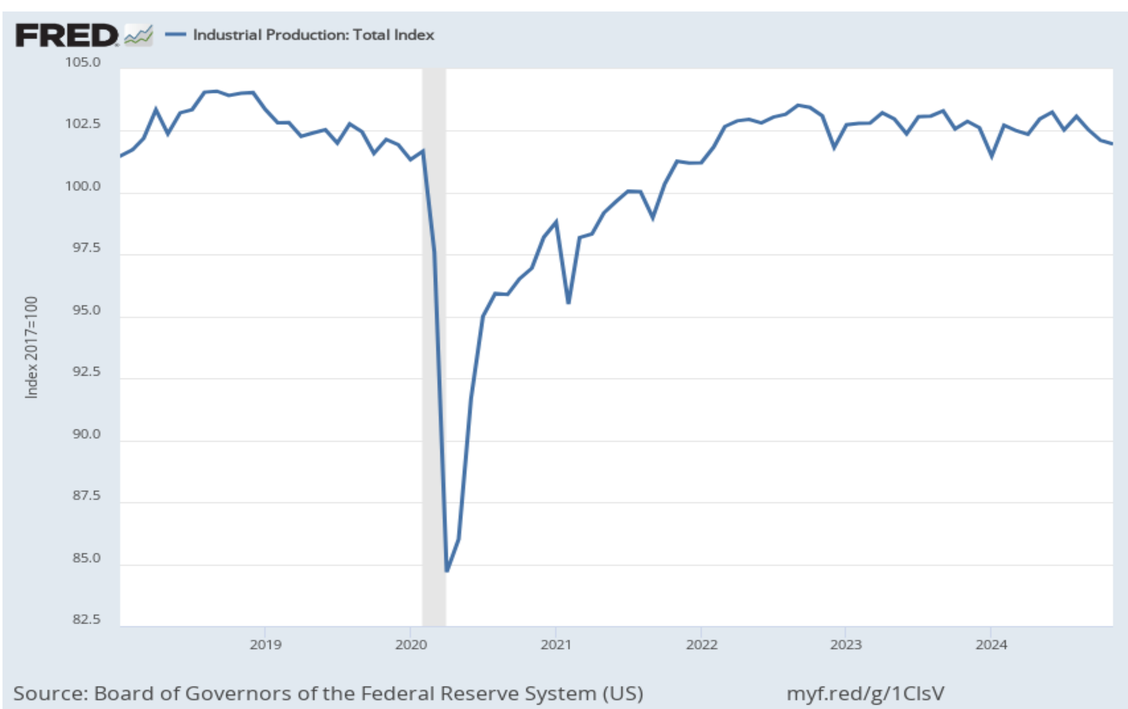
This week the BEA released GDP-by-Industry data for the third quarter enabling me to extend the annual rate of turnovers. These can be seen in the graphs that follow. All the rates remain depressed and in a trough. I will go on to explain that part of the reason lies in profit gouging which has inflated the prices of final sales or GVA relative to intermediate input prices. (However, this is not the case in Graph 1.) This has the effect of slowing down circulation because the equation is sensitive to the relation between the price of final sales and the price of total sales, or GVA vs G.O., where G.O. stands for Gross Output. Nevertheless this effect is minor and cannot explain away the slump in turnovers which is not consistent with a resilient economy.

Graph 1.



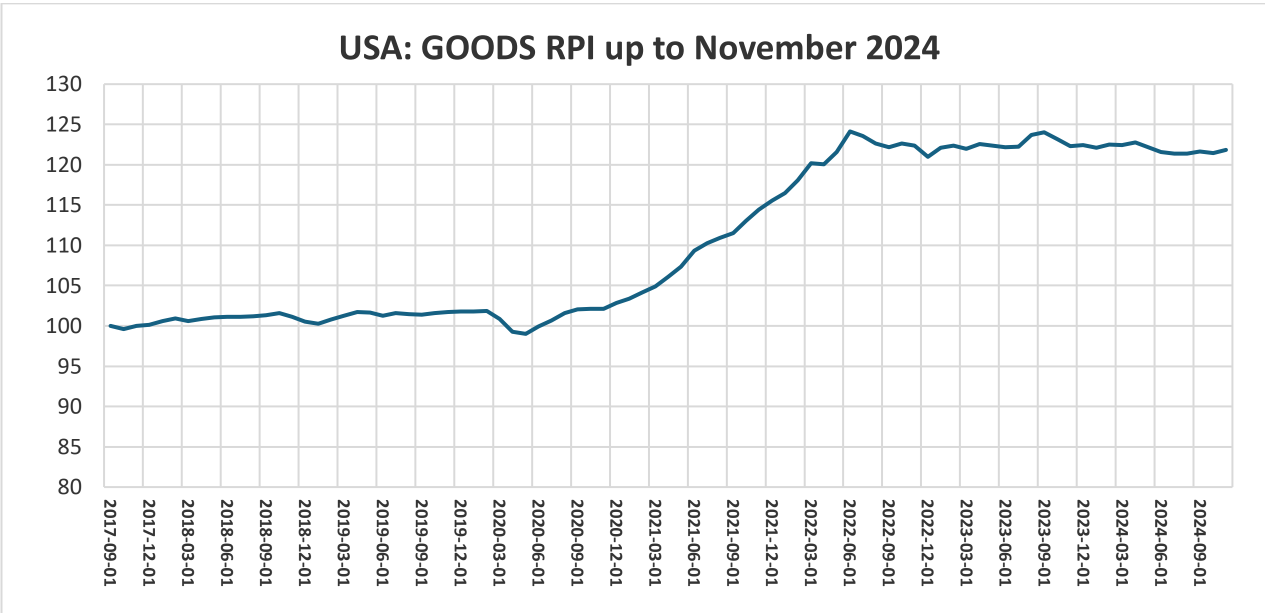
These depressed rates of turnover are consistent with industrial production in the doldrums. Industrial production, despite the Biden Administration's support for reshoring is down 3% from its pre-pandemic peak, down 2% from its post-pandemic peak, and it is down year on year. In addition imports once adjusted for inflation are no higher than the pre-pandemic average of $259 billion vs $258 billion today.

Graph 2.



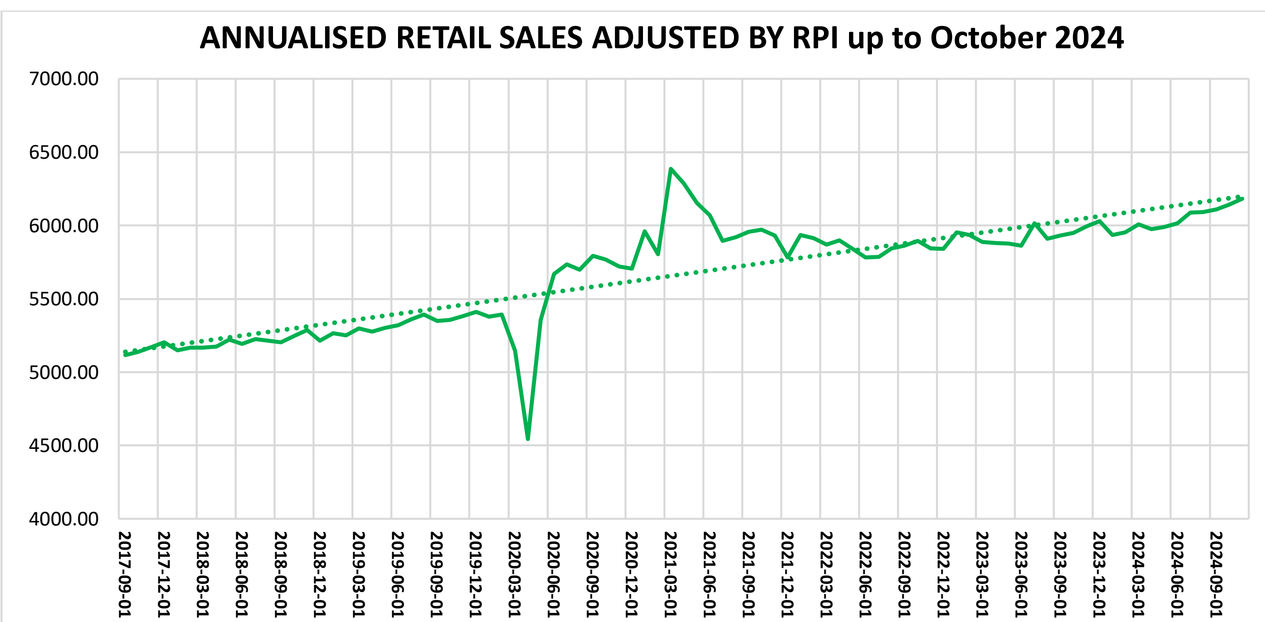
Next let us turn to the retail sector. This important sector which lies at the heart of personal consumption and is equal to around a third of adjusted GDP. According to official date, It has shown a slight improvement so far in H2 2024. Graph 3 is the Retail Price Index, which I construct using FRED Tables CUSR0000SAN and CUSR0000SAD. Despite a slight uptick in November, goods prices are essentially flat to falling.

Graph 3.



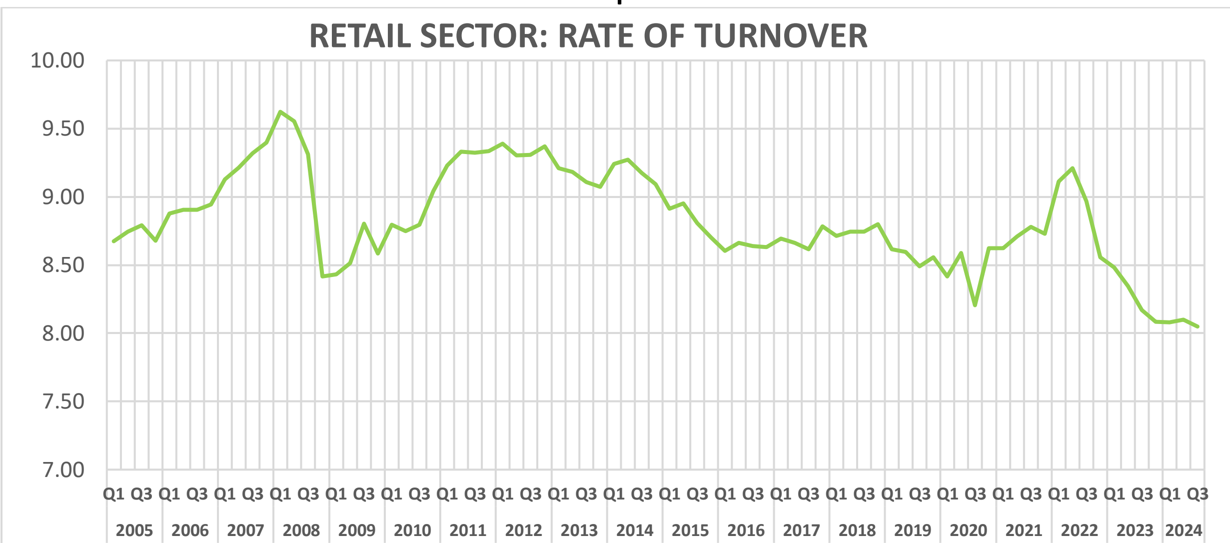
As a result of the mild deflation in prices, the volume of retail sales according to the official data once more, is on the rise since mid-year. Even accepting the data, the recent pickup could be front end buying as consumers worry about Trump tariffs and the withdrawal of EV subsidies.

Graph 4.



Certainly the rate of turnover for the retail sector does not support robust retail sales. Normally such an event is accompanied by rising turnover as demand accelerates sales, but this is not the case. Only one of them can be correct, either Graph 4 or Graph 5. Turnover in retail continues to slump to levels not seen since the start of the series. It is down 12.5% from its Covid Funded 2022 peak and down nearly half a percent from the trough in 2009 following the financial crash.

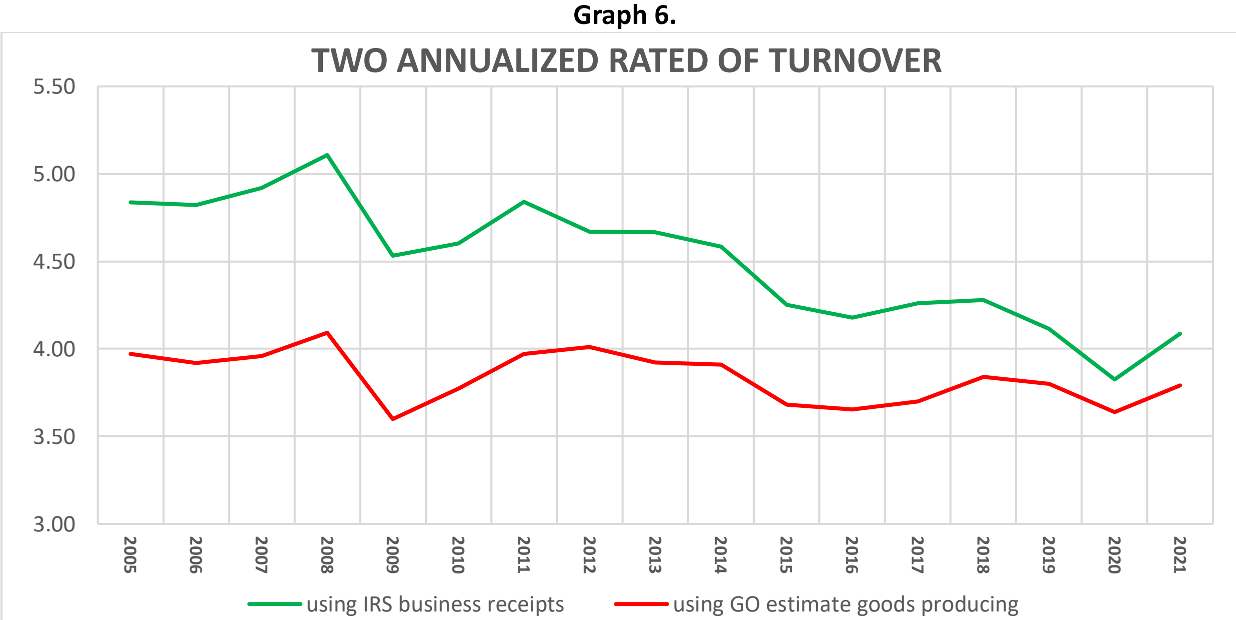
Graph 5.



Restating turnover.

In my previous article on the US economy I commented that I had found a source for Gross Output in the Tax Tables prepared by the [Internal Revenue Service](). Gross Output is not found in NIPA Table 1.14 which is why I have to estimate it. The IRS report is Titled: *Corporation Income Tax Returns Complete Report.* Then I used *Business Receipts* found in the first Table: *Table 1. Number of Returns, Selected Receipts, Cost of Goods Sold, Net Income…* Here is the turnover for the period covered by the reports.

Graph 6.

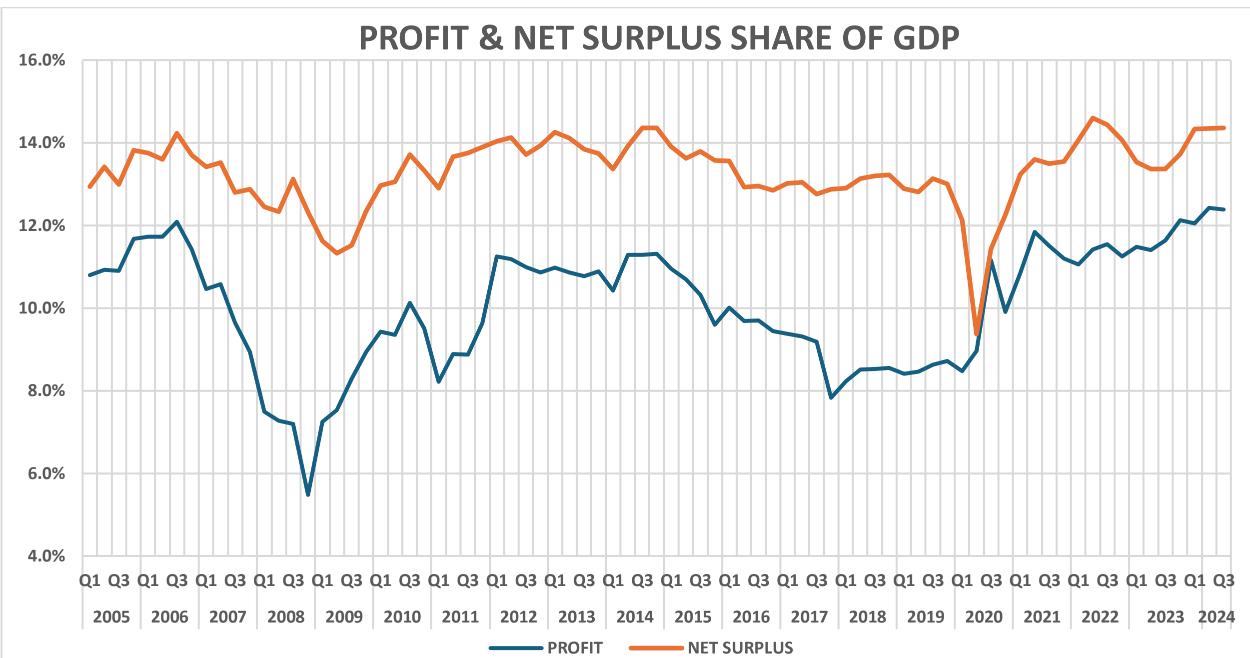


First an explanatory note. The IRS data covers the whole corporate sector. I have taken this into account when preparing the goods sector estimate of Gross Output. We observe that the variation is greatest in the period leading up to the *Financial Crash*. This speaks to business receipts in the financial sector being inflated by the bubble at the time. Thereafter as conditions normalize after the *Crash* the two rates of turnover converge. The key question of course is this: what is the effect on the all important rate of profit due to its effect on circulating capital. My best estimate is around 0.25% latterly in the rate of profit. Statistically this is too small to revise any conclusions or observations.

The effect of profit on turnover.

Many analysts have pointed out that the share of GDP consumed by profits is at an all-time high, well at least since the 1950s. It is. But equally important, the net surplus which is often neglected is not so extraordinary, as can be seen in the graph below. While the Net Surplus is on par with the previous peak in 2014, profits are up 10%. As profit is a component of the net surplus, its comparative rise needs to be explained. The reason for the divergence, as I have pointed out before, is the net interest paid by non-financial corporations which has been reduced by the infusion of Covid Funds, a legacy which continues to endure, allowing corporation to earn additional interest on their resulting cash hoards. Focusing on profits, the non-financial corporate rate of profit is currently the highest it has been since the 1950s.

Graph 7.

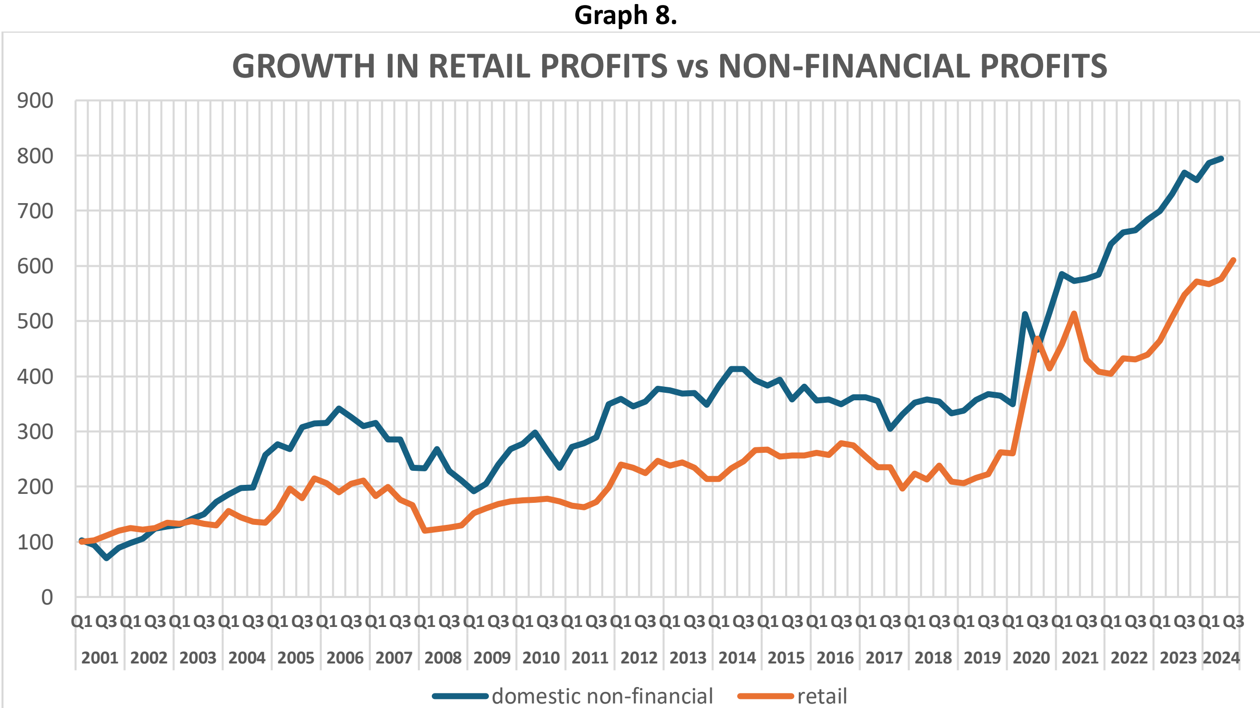


Much of this growth in profits is due to just five corporations according to FactSet: "*It is interesting to note that four of the top five contributors to earnings growth for CY 2024 are "Magnificent 7" companies: NVIDIA, Amazon.com, Alphabet, and Meta Platforms. Overall, analysts expect the "Magnificent 7" companies will report earnings growth of 33% in 2024. On the other hand, analysts predict the other 493 companies will report earnings growth of just over 4% for 2024.*" The bulk of US corporations are unprofitable or marginally profitable. The usurping of profits by the *Frightening Five* does a disservice to the rest of the economy. More to the point, FactSet's overall data for the S&P 500 suggests the official profit data is vastly inflated. Graph 7 may be a product of profit modelling which is outdated.

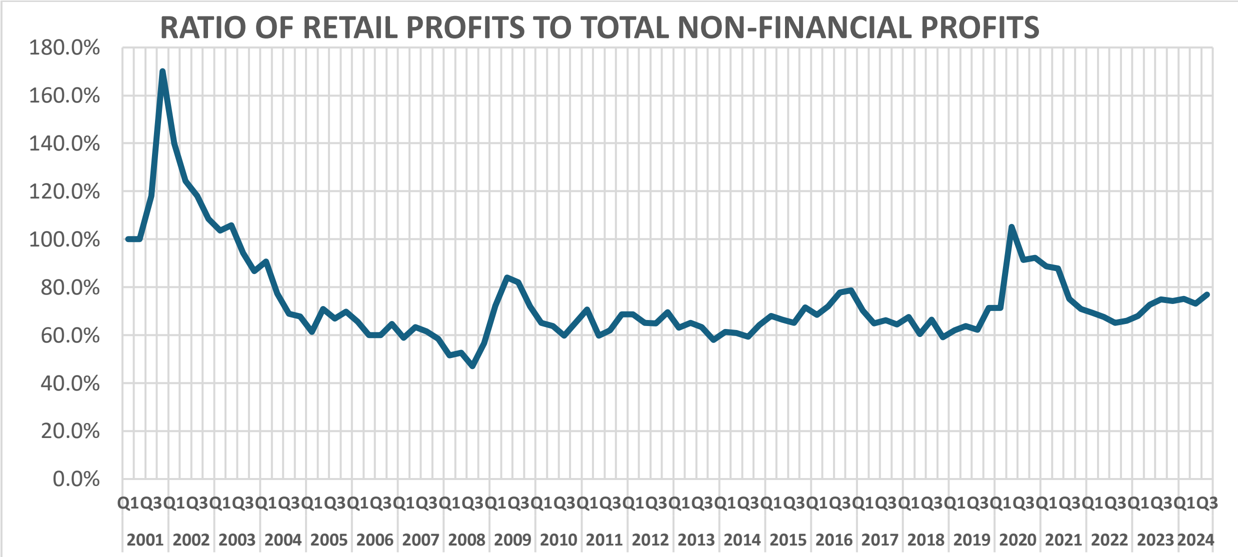
Another way of examining the effect of profit realised in final sales on turnover is to use gross profit. Gross profit or the gross margin is obtained by subtracting the cost of sales (aka inputs) from the sales revenue. If the price of intermediate goods are falling relative to selling out prices, everything else being equal, gross profit will increase. Many corporations release what is called their gross margin made up of their gross profit divided by sales. And in many cases they have been increasing due to the retreat in input prices. All of which would reduce the rate of turnover as measured by the formula. However, as we have seen above, this effect is minimal considering the bulk of the corporations other than the *Frightening Five* have not seem much of an improvement in their profits. (We should also bear in mind the *Frightening Five* have a bigger impact on profits than on revenue or sales because their profit margins are three times higher than average thus they have triple the effect on profits compared to their effect on revenue.)

We can now turn back to retail and evaluate its profit profile and its subsequent effect on turnover. Though retail profits have soared, they have done so at a rate below that of the non-financial sector inflated by the *Frightening Five*. As Graph 9 which follows shows, as a ratio of total non-financial profits, the retail sector ratio while higher is not higher to the degree that it explains most of the slowdown in retail turnover. If we factor in the following: between Q4 2019 and Q2 2022, the peak of profit gouging, turnover rose from 8.56 to 9.21 despite retail profits soaring by two thirds. Part of this was due to soaring input prices as well. Between Q2 2022 and Q3 2024 profits rose by only 19% and yet turnover has plunged from 9.21 to only 8.05. We can therefore conclude that retail sales are not as 'resilient' as officially reported which is in line with anecdotal observations such as credit and debit card usage which has been underwhelming falling short of expectations. This is in line with retail sales in Texas one of the more buoyant states. Finally, the Census Bureau's high frequency data also show flat sales. And given the ructions on Wall Street they will be even more underwhelming in the future.

Graph 8.



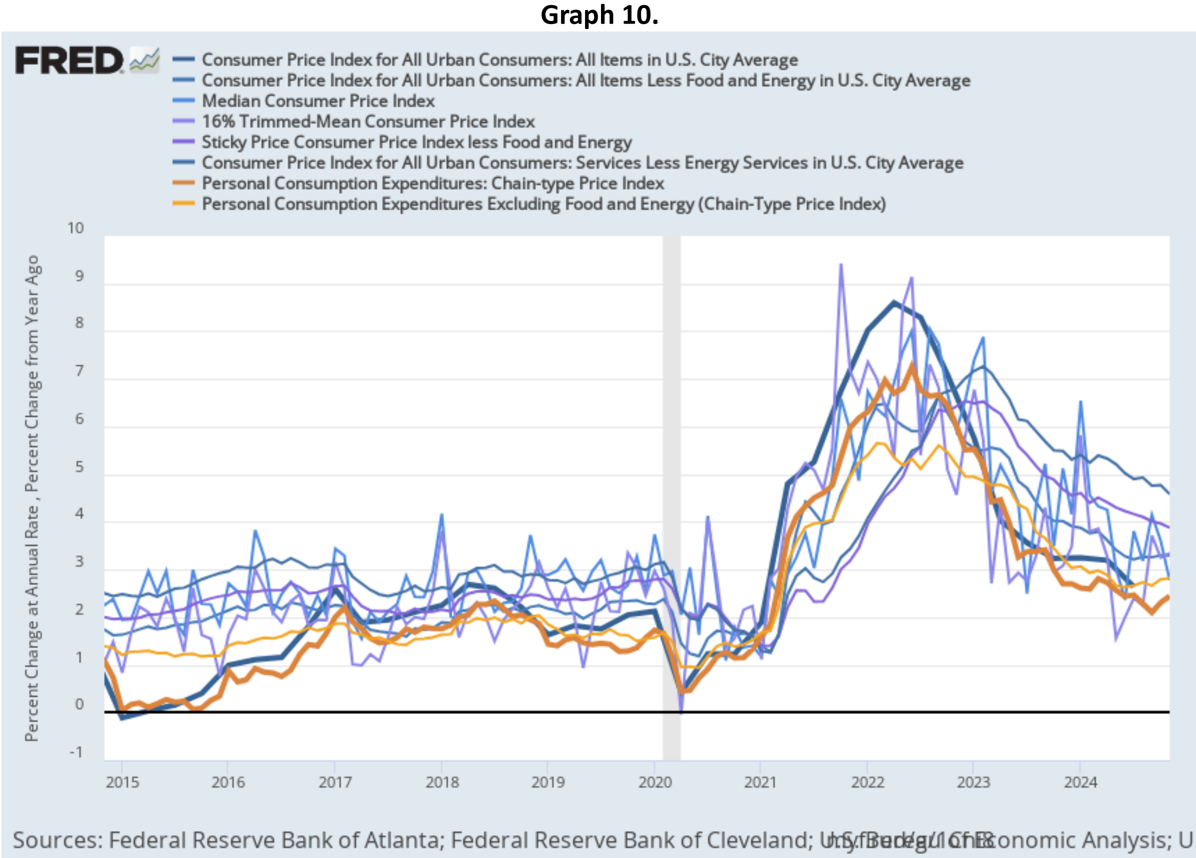
Graph 9.



The importance of deflators.

This graph below shows a whole series of deflators, or if you like, Inflation Indexes. They come in all shapes, sizes and colours. But which is the most accurate when measured both statistically and in terms of their impact on consumers.

Graph 10.



The Cleveland FED median CPI considers its CPI index to be the most accurate because it is less affected by price changes at the extremes. In Q3 it registered an increase of 3.9% vs the regular Consumer Price Index of 2.7% and the PCE Index of 2.6%. The gap was even bigger when using the BEA deflator for PCE (Personal Consumption Expenditures) which was only 2.3%. Let us assume the Cleveland FED is correct and that its median CPI is the most accurate measure of consumer inflation. How does this affect GDP growth? Given that PCEs represent roughly 70% of GDP, the effect of the difference in the deflators would be 3.9% - 2.3% x .7 = 1.12%. On this basis GDP would be only 2% not 3.1% as estimated by the BEA. Interestingly enough this coincides with Gross Domestic Income or GDI which only grew by 2.1%. At the moment economists are at a loss to explain the unusual and enduring gap between GDP and GDI.

The problem is not so much the nominal growth in GDP estimated by the BEA to be 5.3% which is not dissimilar to the nominal rise in the Gross Output (total sales) of private companies which in turn correlates to the revenue of S&P companies, in contrast to the profit data, which does not. The real problem is inflation adjusted real or volume growth. Thus the real figure of 3.1% is obtained by deducting a deflator of only 2.2% from the nominal figure of 5.3%. It is the issue of the deflator that is of concern.

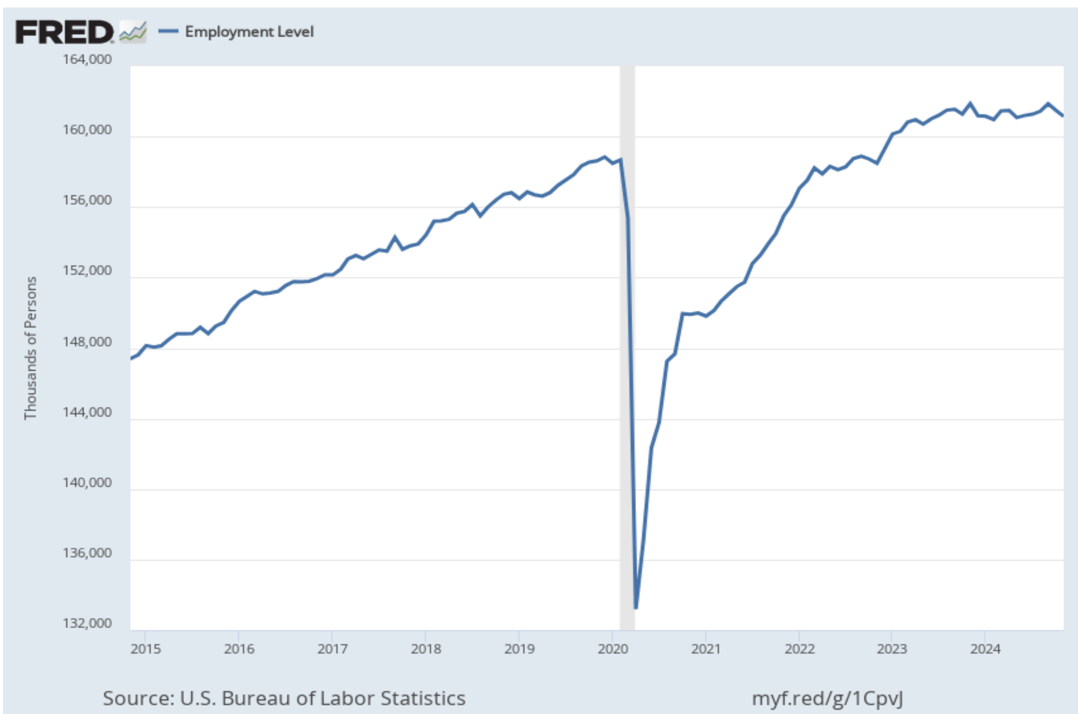
There is one final factor to take into account. If GDP is so strong and if profits in aggregate are so strong, against a background of ongoing price rises, why is the net worth of non-financial corporations plateauing rather then steadily increasing? As I said in the previous article on the US economy, this could be due to the overstatement of profits. According to the official figures found in NIPA Table 1.14, profits grew at more than double the rate yoy compared to S&P 500 profits, which seems highly unlikely given the preponderance of large corporations listed on the Index with their above average rates of profit.

Graph 11.

The other concern are payroll numbers. Last year total job creation was revised down by 30% or 818,000. This year an even bigger downward revision is expected. Although Mish Shedlock is on the right wing of politics his analysis of the labour market in the US in his blog MishTalk is more accurate than most. His estimate for downward revisions for 2024 exceeds that of the actual downward revisions which occurred in 2023.

Another theme is becoming more apparent and prevalent, it is the growing and intensifying hiring freeze taking place amongst private employers. The anecdotal and regional data is more in accordance with the neglected side of the monthly BLS employment report, titled the *Household Survey Report* (Graph 12). The additions to the workforce, other than from unregistered migrant employment, on the *Household Report*, numbered less than 2.5 million from the end of 2019. To put that in perspective, this is only equivalent to the increase during 2024 in the payrolls which appears on the more cited *Establishment Survey* side of the BLS report. I used to pay more attention to the *ADP Employment Report* which used to be closer to the *Household Report* until they wrecked their modelling to align it with the investor focused *Establishment Report*.

Graph 12.



The reason I have spent so much time analysing the current state of the economy is that unless today's estimate is refined and rendered more accurate if not more honest, the outlook for tomorrow is even more unclear.

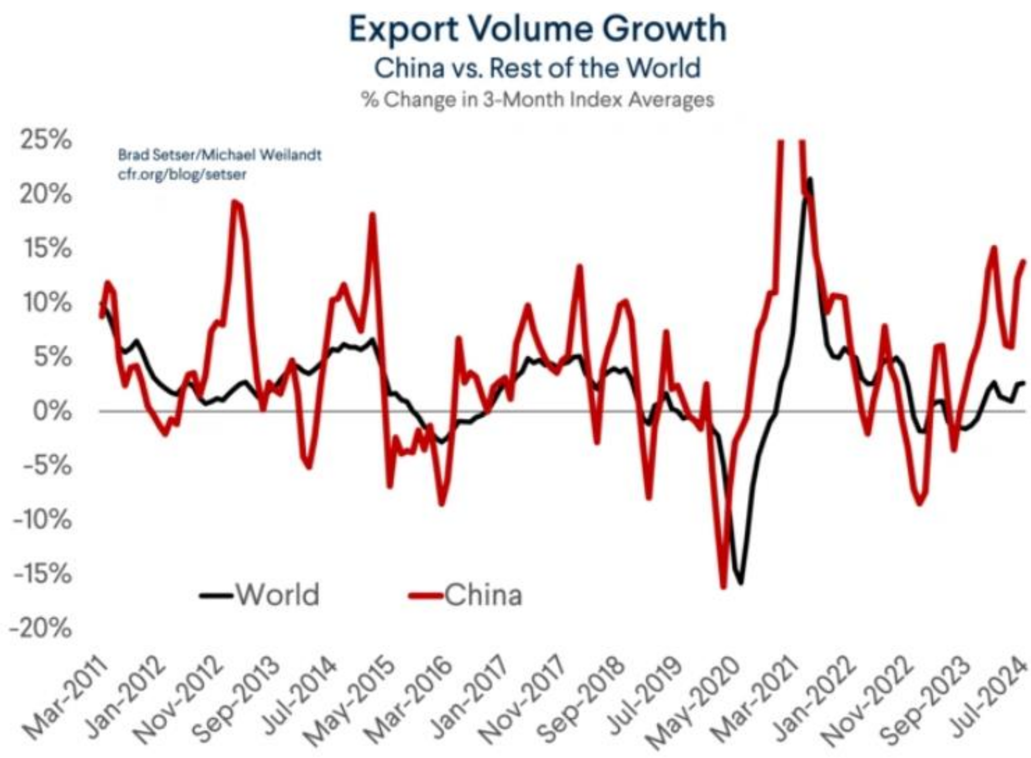
The outlook.

The FED in releasing its decision to cut its lending rate by 0.25% also reduced its estimate of future rate cuts because of sticky inflation and an economy which Powell declared to be in good shape. Indeed GDP growth for the fourth quarter was increased to 3.1%. Coincidentally GDPNOW now also projects a GDP growth rate of 3.1% for the fourth quarter. What could possibly go wrong?

Well the transition from October to November data is enlightening. Take the FED's [Empire State Business Survey.](#) *"After rising sharply last month, the headline general business conditions index retreated thirty-one points to 0.2."* Note this survey was conducted in the first week of December. The [Philadelphia Business Survey](#) conducted a week later showed the same result: *"The diffusion index for current general activity declined from -5.5 to -16.4 in December, its lowest reading since April 2023."* Talk about a hangover after the Trump party. There were such high hopes until the penny or cent dropped.

There are three Trumpian issues to consider. The first and most important is tariffs. Trump's punitive tariffs against the likes of China and Mexico should be seen not as punishment but as a barometer of the uncompetitive state of the US economy. The fifty to sixty percent proposed tariff is in effect an indicator of the cost price differential between a product produced in the US and in Asia. Only the 100% tariff on Chinese Electric Vehicles seems to have worked so far. The forty-two percent average tariff has not, as can be [seen in this graph](#), because the rising Dollar has helped blunt the effect of tariffs on Chinese imports. In terms of [global exports](#) China's eleven month total this year was up 6.6% on last year in Yuan terms and as [this graph shows,](#) it is much higher in volume terms. Of course volume growth surging ahead of value growth is not good for profit margins.

Graph 13.



Let us assume Trump's tariff wall is more successful than his migrant wall, what then? Well if US producers are sufficiently shielded so that they start building television factories, smartphone factories, EV factories, Battery factories and so forth, it will upset the market. These US produced products will cost consumers 30 to 50% more than their equivalent imports. This expansion of costly manufacturing has not been factored in; all that has been factored in are more expensive imports. But the effect will be more widespread should production increase in the USA itself. What has not been considered is how increasing costly production will generalise the movement in prices upwards, that is to say price effects will move from the margins to the centre of the economy.

Now bear in mind, the previous goods deflation on the back of cheap Asian imports has been the one element supporting standards of living in the USA. Everything else has shot up in price particularly those items which lend themselves to financialisation such as education, healthcare, housing, water and energy. In the end, the only way to measure the cost of things or what is the same thing, standards of living, is to calculate how many hours of work things cost to buy. This has been done in this article. Now considering median wages, at least for men, have stagnated since the 1970s, despite their productivity trebling, the cost of a home in labour hours has gone up 2.3 times since 1972, medical expenses have gone up by half, education has more than doubled, the cost of a car has almost doubled while a vacation has more than doubled. No wonder people voted for Trump and his promise to make their lives great again.

On the one side reshoring will increase employment. On the other side, by raising the value of labour power and therefore cost-prices it will decrease employment. The real problem is that neo-liberalism has completely distorted and deformed US society. The small state ethos shaped by lobbyists and influencers has led to a lack of a skilled workforce amongst other things making reshoring impossible in the near term. The effect is clear to see with the problems besetting the US Navy, which does not have enough skilled shipwrights to service its diminishing fleet never mind add to it. How will they cope with additional factories unless of course LLMs advance to the point where they have factories without workers.

Trump's tariffs will rebound on the world economy already slipping into recession. Trump by putting *America First* believes it will sustain the US economy at the expense of the world economy. This is not new; all US presidents have done so, for example paralysing Japan in the 1980s. But Trump is elevating this to a new level. His assault on the EU is indicative, demanding they buy US energy or face even higher tariffs. I will have more to say about this in my next article on the world economy. Suffice it is to say, the US economy is not an island, and by damaging the world economy, the US will ultimately pay a much higher price than would be the case were their a more collaborative approach. But capitalists do not do collaboration in a crisis, they seek only to offload their pain onto their competitors, especially one which is capable of unseating it, namely China.

The second is Trump's tax cuts amounting to an average of $780 billion p.a. over the next ten years, and of course benefiting the richest layer of taxpayers. Given that the budget deficit in the first two months of this fiscal year has already jumped increasing by an annualised rate of close to a trillion Dollars, this would mean a deficit north of 9%. This would cause the *Debt to GDP* ratio to rise by 4% p.a. which is unsustainable. But don't panic his supporters insist, these cuts will be good for the economy and be offset by higher tariffs. They are peddling fools' gold as the historical data shows the opposite to be the case; reducing the taxes on the rich in an environment of rising inequality is catastrophic for the economy and for services.

The third is the trashing of regulations most of which protect the worker, the environment and the consumer. Some capitalists see regulations as immediate costs, not as protecting their future profits, which they do by keeping workers and the environment fit for purpose. No doubt Musk will excel at slashing protections.. Actually he is already doing this by polluting Texas, California and Florida. Well what does one expect from this environmental poseur and champion of free speech provided it is not extended to his workers trying to unionise against him. No doubt under Musk the cry will go out, water, water everywhere but none fit to drink. Trump and Musk in pursuit of short term profits are fools, if they want to continue to lay golden eggs, then don't shit in the nest. These two charlatans add easy to the word Hypocreasy.

Conclusion.

In the USA long term interest rates are rising, in the rest of the world they are collapsing. In the USA the Dollar continues to strengthen sparking currency crises around the world notably this week in Brazil. In the USA Stock Markets continue to boom in China they are depressed. In the USA the rate of profit is at a peak and in the rest of the world it is troughing.

Does this mean the US economy is asserting itself and will emerge victorious? The answer is no. The US economy is a five card trick or if we add in the two pharma corporations peddling dangerous weight reducing drugs, it is a seven card trick. Below the shimmer caused by the A.I. hype the US economy is in trouble; debt is sloshing all around while Zombie companies stalk the land. LLMs are not a driver for the economy such as the internet which created vast opportunities for investments. All LLMs can do is cull tens of millions of jobs, but in doing so they will disturb what is already a fragile and restless society. Thus before they come to the aid of capitalism, they will first have to convulsively reshape an already brittle society. Time and the class struggle will decide whether they succeed or not.

In the meantime the US will follow the world into recession. Last year the only tongue in cheek prediction I made for 2024 was that as the majority of economists were saying there would be no recession in the USA, one was bound to break out. Once again economists are not predicting a recession in the USA in 2025, but this time there will be one. The world economy is at breaking point and Trump is approaching axe in hand.

Brian Green, 24th December 2024.