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ECLAC Office in Washington, D.C.

United States economic outlook

Third quarter of 2023

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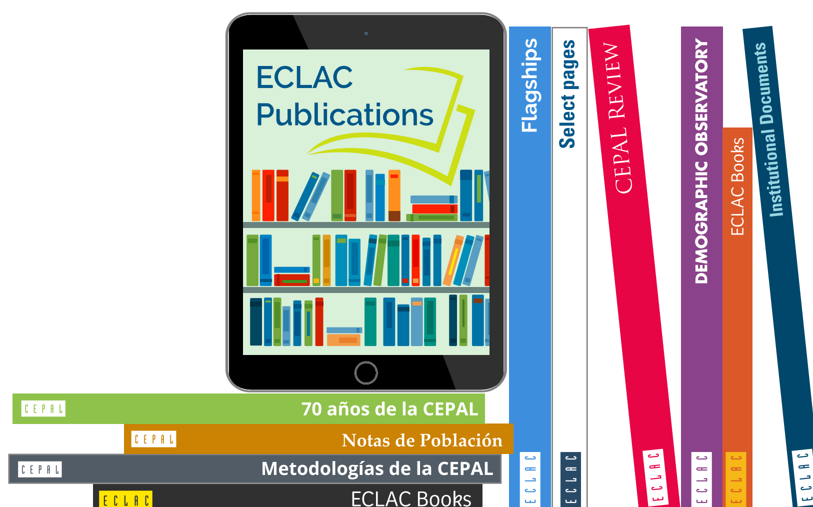

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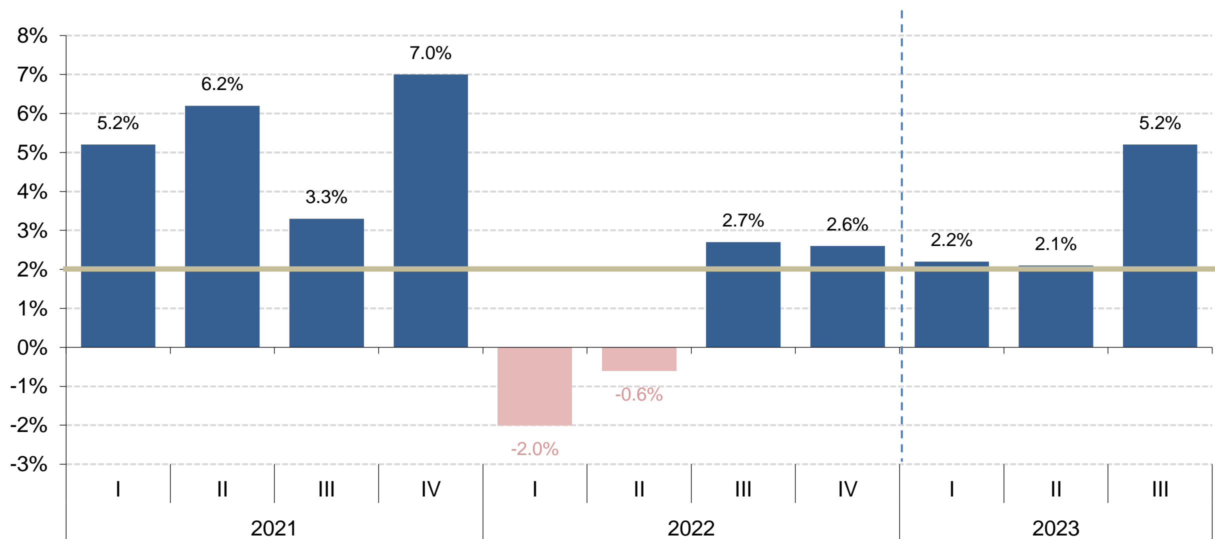
Highlights

- The United States Gross Domestic Product (GDP) rose 5.2% in the third quarter of 2023, the fastest pace in nearly two years. Consumer spending was the main driver of economic growth in the quarter, followed by accumulation of private inventories.
- The labor market has continued to show strength. An average of 232,000 new jobs were created per month and 2.6 million new jobs were added from January to November 2023, while the unemployment rate was at 3.7% at the end of November. Despite resilience in the labor market, it is showing signs of cooling, with job openings decreasing and quits now at the same level they were before the pandemic.
- Inflation has continued to moderate. It slowed to 3.1% in November 2023 from 6.5% in December 2022. Core inflation, which excludes volatile energy and food categories, declined to 4% in November, the lowest level in two years, from 5.7% in December 2022.
- The Federal Reserve raised interest rates four times this year, with quarter-point increases in January, March, May, and July 2023, but has left its policy rate unchanged since then at 5.25% to 5.50%, the highest level since 2001.
- Despite the interest rate hikes over the last year and in the first semester of 2023, the United States economy —supported by a strong job market, with an unemployment rate that remains historically low, and retreating inflation— remains resilient, contributing to rising optimism that the United States economy is approaching a soft landing.
- However, uncertainty is high, and risks of a hard landing remain. The recent pace of growth may be hard to sustain, as high interest rates eventually take a toll on U.S. consumers and businesses, and inventory accumulation and consumer spending start to moderate. Nonetheless, the underlying trend year-to-date has been of a resilient U.S. consumer, supported by a strong labor market and receding inflation.

Overview

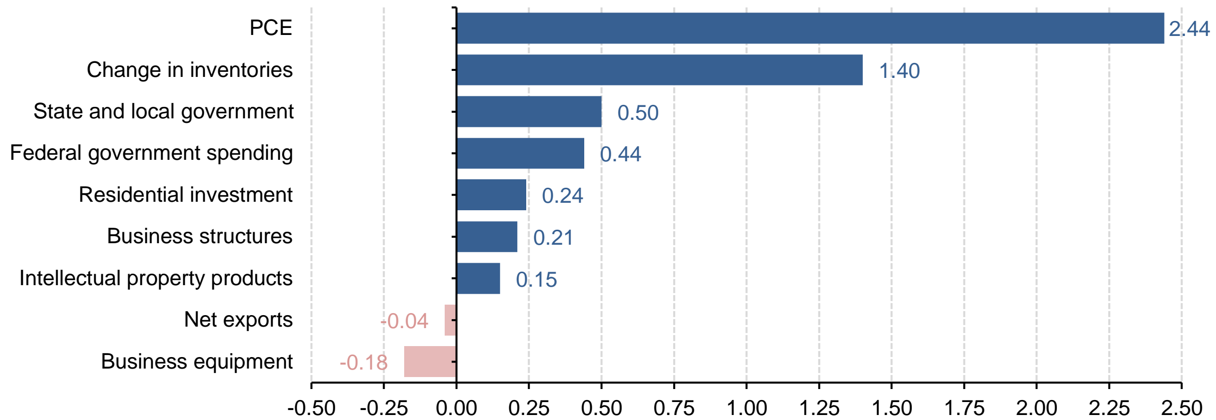
The United States Gross Domestic Product (GDP) rose 5.2% in the third quarter of 2023, the fastest quarterly pace since the fourth quarter of 2021. The third quarter of 2023 was the fifth consecutive quarter of growth above the economy's potential, estimated at 2% (figure 1). Consumer spending was the main driver of the GDP increase in the third quarter of 2023, contributing 2.44% to growth in the quarter (figure 2).

Figure 1
United States real Gross Domestic Product quarterly growth rate: first quarter of 2021—third quarter of 2023
(Percentage, not seasonally adjusted)



Source: United States Bureau of Economic Analysis, U.S. Department of Commerce.

Figure 2
Contributions to percent change in real GDP, third quarter of 2023
(Percentage points, seasonally adjusted at annual rates)

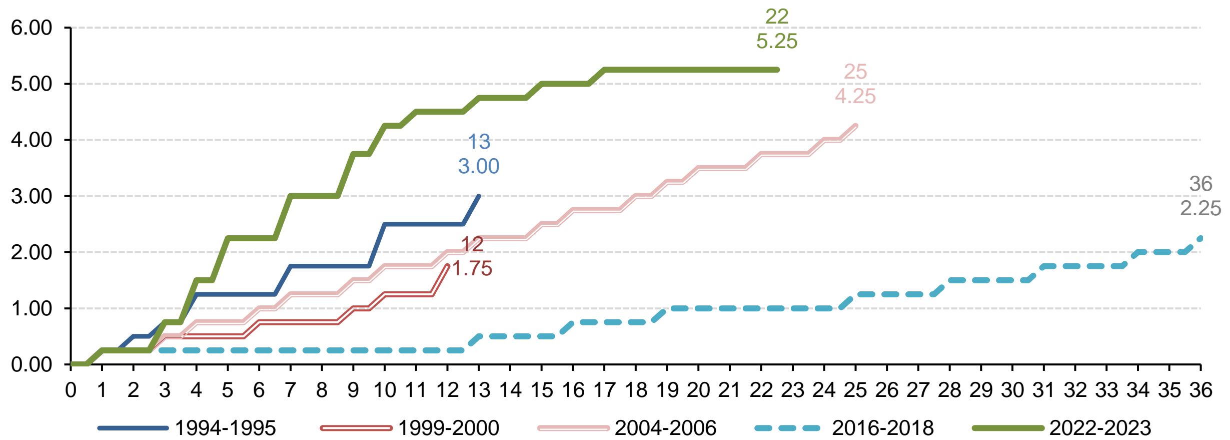


Source: ECLAC Washington Office based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.
PCE: Personal Consumption Expenditures.

The inflation rate has been retreating and moving in a more positive direction. The consumer-price index rose 3.1% in November from a year earlier, a slight slowdown from 3.2% in October, according to the Bureau of Labor Statistics. Core prices, which strip out volatile food and energy components, rose 4% in November from a year earlier, the same as October. The November inflation numbers bolster Federal Reserve officials' view that interest rates should remain at current levels during the spring of next year. Investors are currently betting the central bank will begin cutting rates as soon as next spring, but Fed Chair Jerome Powell earlier this month said it was too soon "to speculate on when policy might ease." However, Fed officials' projections, released after the central bank's last meeting of 2023 on 12-13 December, suggest three interest rate cuts for 2024. In their projections, officials see the federal-funds rate target ending 2024 between 4.5% and 4.75%, 0.75% lower than the current rate, and half-point lower than projected in September.

The Federal Reserve has kept interest rates unchanged since July, after raising them four times in the first seven months of the year —there were quarter-point interest rate increases in January, March, May and July 2023. In its last meeting of the year in December, the Fed left its policy rate unchanged at 5.25% to 5.50%, a 22-year high. The current tightening cycle, which started in March 2022, is the United States's third longest cycle, and with the fastest pace of increases (figure 3).

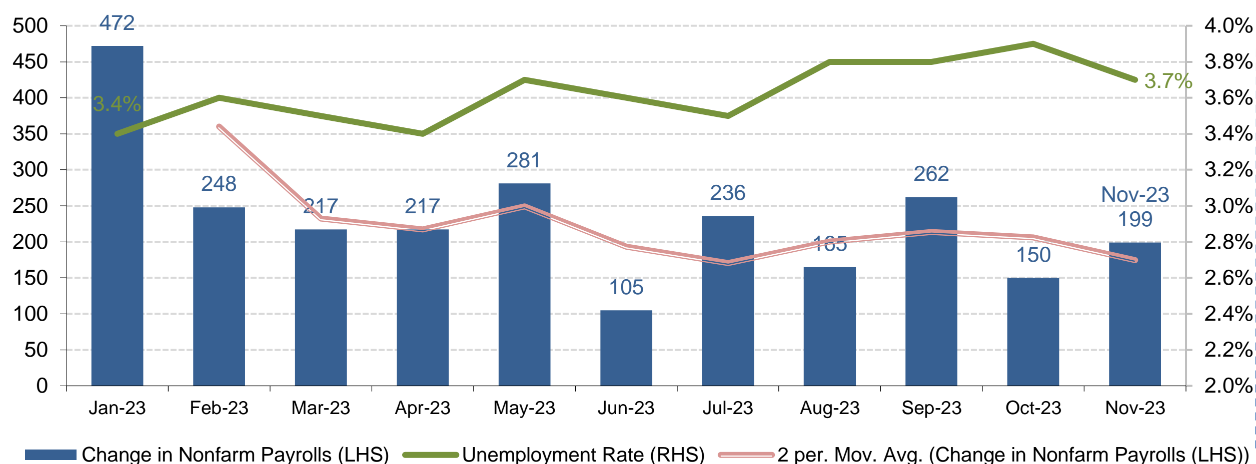
Figure 3
United States Federal Reserve tightening cycles 1994—2023
(Percentage)



Source: ECLAC Washington Office, based on data from the United States Federal Reserve.

The labor market remains strong but has started to cool down, which has been the ultimate goal of the current monetary tightening cycle. According to the Bureau of Labor Statistics, in the last business day of October 2023 there were still 8.7 million job openings in the United States, but down from a peak of 12 million in March 2022. Businesses are hanging on to their workers and not resorting to layoffs but have cut some openings. A moderation in quit rates —which are now at the same level as before the pandemic— has also been observed, consistent with the Fed's plan. An average of 232,000 new jobs were created per month and 2.6 million new jobs were added from January to November 2023, while the unemployment rate went up from a record low of 3.4% in January to 3.7% in November 2023 (figure4).

Figure 4
Monthly job creation and unemployment, January—November 2023
(Annual job growth in thousands (left axis); Percentage (right axis))



Source: ECLAC Washington Office based on data from the United States Bureau of Labor Statistics.

Given the resilience of the U.S. economy in face of the rapid increases in interest rates over the last year and in the first semester of 2023, optimism that the United States economy is approaching a soft landing —the notion that the Federal Reserve will be able to slow the economy and reduce inflation without causing a recession— is on the rise. A soft landing would be unusual, since in the past 80 years the Federal Reserve has never managed to bring inflation down substantially without sparking a recession.

The U.S. economy is projected to grow 1.5% on average in the fourth quarter and 0.7% in the first quarter of 2024, according to market forecasts (table 1). On an annual basis, average market projections point to growth of 2.4% in 2023 and of 1.1% in 2024, inflation at 4.1% in 2023 and 2.6% in 2024, unemployment rate at 3.7% in 2023 and 4.3% in 2024, and the federal funds rate at 5.3% in 2023 and 4.4% in 2024, with most projections made in November and December 2023 (table 2).

Despite the resilient economic outlook, risks of a hard landing remain. The downside risks to growth include the possibility that interest rates remain higher for longer, even penciling in interest rate cuts next year, which could eventually negatively impact consumer and business spending. Following Fed officials own projections, a 4.6% interest rate a year from now, adjusted for 2.4% inflation, still leaves a relatively high real rate of 2.2%, which is above the 0.5% "neutral" rate that Fed officials have considered consistent with stable growth and inflation.[1]

[1] The "neutral" rate is the interest rate level that the Federal Reserve believes is consistent with a balanced economy in the long run. At the September 2023 Federal Open Market Committee (FOMC) meeting, the median projection for the long-run real neutral rate was 0.5%, but five of 17 participating members suggested they believe the rate (the nominal rate minus the Fed's 2 % inflation target) is now 1% or higher. See Brookings, "What is the neutral rate of interest?" by Sam Boocker, Michael Ng, and David Wessel, 3 October 2023 [online] https://www.brookings.edu/articles/the-hutchins-center-explains-the-neutral-rate-of-interest/.

Fiscal concerns are another risk to the outlook. In November, Moody's revised the outlook on the U.S. Government's credit ratings to negative, saying that downside risks to the country's fiscal strength have increased. Given higher interest rates and the lack of effective measures to reduce public spending or increase revenues, the agency said it expects fiscal deficits to remain large.

There are upside risks to the outlook as well. Policy tightening may never take a major toll on individuals and businesses, consumer spending may remain resilient if inflation continues its downward trend, and an increase in productivity could be supportive of growth. U.S. labor productivity increased 5.2% annualized in the third quarter according to the Bureau of Labor Statistics, exceeding consensus forecasts.

Table 1
Quarterly forecasts for United States economic growth in 2023 and early 2024
(Percentage change)

	Q4 2023 (qoq)	Q1 2024 (qoq)	Date of Forecast
What Markets Say			
Bank of America/Merrill Lynch	1.5%	1.5%	Dec-23
Capital Economics	0.5%	0.2%	Dec-23
JPMorgan	2.0%	1.3%	Dec-23
Moody's Economy.com	0.8%	1.1%	Nov-23
Mortgage Bankers Association	0.8%	-0.4%	Nov-23
National Association of Realtors	1.6%	1.7%	Oct-23
National Bank of Canada	1.5%	-0.7%	Nov-23
TD Bank Financial Group	3.7%	0.9%	Sep-23
Wells Fargo/Wachovia	0.7%	0.9%	Nov-23
Forecasts average	**1.5%**	**0.7%**	

Source: ECLAC Washington Office, based on market sources.

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Table 2
Annual forecasts for United States economic growth, 2023 and 2024
(Percentage change)

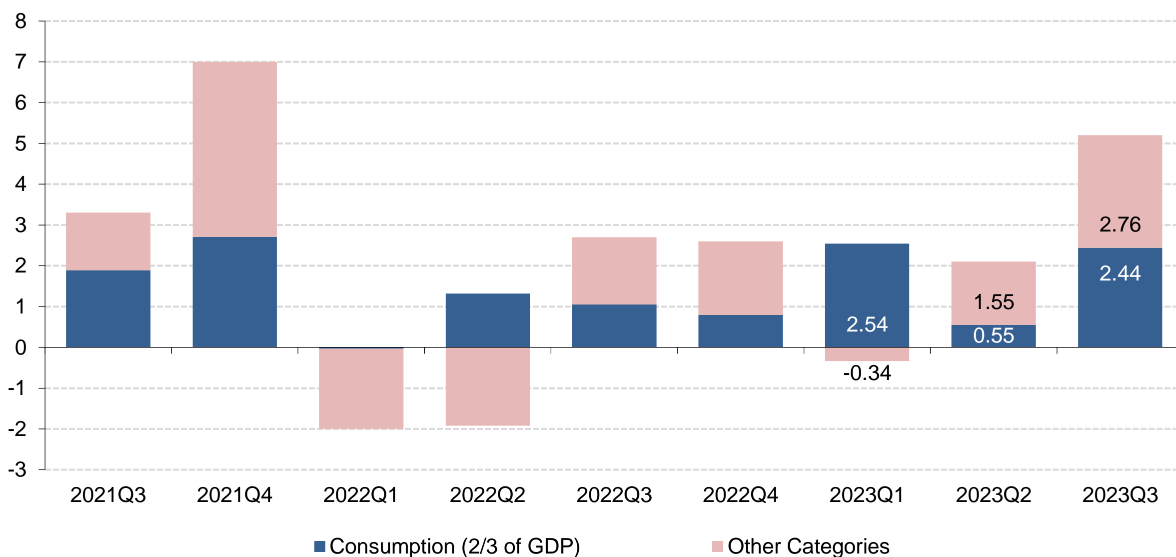
	Real GDP (% change, y/y)		Inflation (% change, y/y)		Unemployment Rate (%)		FED Funds Rate (%)		
	2023	**2024**	**2023**	**2024**	**2023**	**2024**	**2023**	**2024**	**Date of Forecast**
A. What Government Agencies Say									
FED[1]	2.6%	1.4%	2.8%	2.4%	3.8%	4.1%	5.4%	4.6%	*Dec-23*
CBO	1.5%	1.0%	4.2%	2.6%	3.7%	4.5%	5.0%	5.0%	*Jun-23*
OMB[2]	0.4%	1.8%	3.3%	2.5%	3.8%	4.4%	*na*	*na*	*Jun-23*
B. What Markets Say									
Bank of America/Merrill Lynch	2.5%	1.4%	4.1%	2.9%	3.7%	4.2%	5.4%	4.6%	*Dec-23*
Capital Economics	2.4%	1.3%	4.1%	2.3%	3.7%	4.4%	5.4%	3.4%	*Dec-23*
JPMorgan	2.5%	1.6%	4.1%	2.4%	3.6%	4.2%	5.5%	4.5%	*Dec-23*
Moody's Economy.com[3]	2.4%	1.7%	4.2%	2.8%	3.7%	4.0%	5.0%	5.1%	*Nov-23*
Mortgage Bankers Association	2.5%	0.4%	3.2%	2.4%	3.7%	4.6%	5.4%	4.6%	*Nov-23*
National Association of Realtors[3]	2.1%	1.5%	4.3%	2.7%	3.7%	4.1%	5.1%	4.7%	*Oct-23*
National Bank of Canada	2.4%	0.3%	4.2%	2.8%	3.7%	4.6%	5.5%	4.8%	*Nov-23*
TD Bank Financial Group	2.3%	1.3%	4.2%	2.7%	3.6%	4.2%	5.5%	4.0%	*Sep-23*
The Economist Intelligence Unit[4]	2.4%	0.9%	4.1%	2.6%	3.7%	4.4%	*na*	*na*	*Nov-23*
Wells Fargo/Wachovia[3]	2.4%	0.8%	4.2%	2.5%	3.7%	4.2%	5.3%	4.2%	*Nov-23*
Market Average	***2.4%***	***1.1%***	***4.1%***	***2.6%***	***3.7%***	***4.3%***	***5.3%***	***4.4%***	
C. What International Organizations Say									
United Nations DESA (Baseline)	1.1%	1.0%	*na*	*na*	*na*	*na*	*na*	*na*	*May-23*
World Bank	1.1%	0.8%	*na*	*na*	*na*	*na*	*na*	*na*	*Jun-23*
OECD	2.2%	1.3%	3.8%	2.6%	*na*	*na*	*na*	*na*	*Sep-23*
IMF	2.1%	1.5%	*na*	*na*	*na*	*na*	*na*	*na*	*Oct-23*

Source: ECLAC Washington Office based on official and market sources.
Note: FED: Federal Reserve; CBO: Congressional Budget Office; OMB: Office of Management and Budget (U.S. Administration's forecasts).
[1] Projections of change in real GDP and inflation (measure used is PCE inflation, the FED's preferred measure) are percent changes from the fourth quarter of the previous year to the fourth quarter of the year indicated. [2] Projections are for real, chained (2012) dollars GDP, fourth quarter-over-fourth quarter; CPI: fourth quarter-over-fourth quarter; unemployment rate: annual. [3] Moody's, the National Association of Realtors, and Wells Fargo/Wachovia forecast the Fed funds rate as an annual average, not end-period [3] CPI: average; Fed Funds Rate: end-period.

I. Quarterly developments

In the first three quarters of 2023, the U.S. economy showed steadfast resilience, with consumer spending being a substantial driver. In the first quarter, consumer spending contribution to GDP growth stood at 2.54%, moderating to a 0.55% contribution in the second quarter, and rebounding to 2.44% in the third. Other categories also rebounded from a negative contribution in the first quarter to a 2.76% contribution in the third (figure 5).

Figure 5
Contributions to percent change in real GDP growth, third quarter 2021—third quarter 2023
(Percentage points, seasonally adjusted at annual rates)

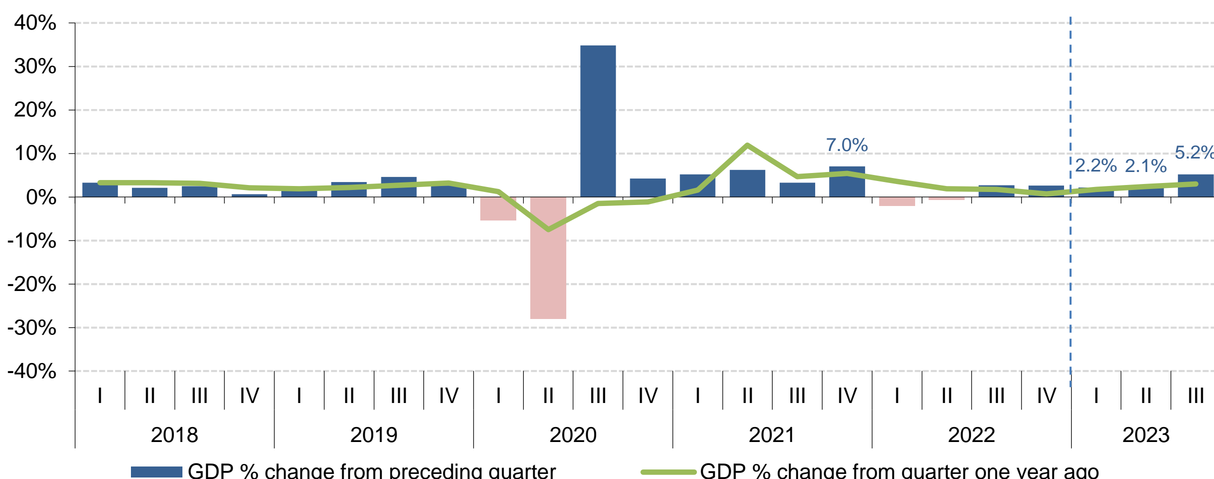


Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.
Note: Contributions to growth are measured at seasonally adjusted annual rates.

A. Quarterly GDP Growth

Real gross domestic product (GDP) increased at an annual rate of 5.2% in the third quarter of 2023 according to the Bureau of Economic Analysis's second GDP estimate released on 29 November 2023, significantly outpacing the 2.1% increase of the second quarter (figure 6). This is the fifth consecutive quarter of growth and the fastest quarterly growth rate since the fourth quarter of 2021.

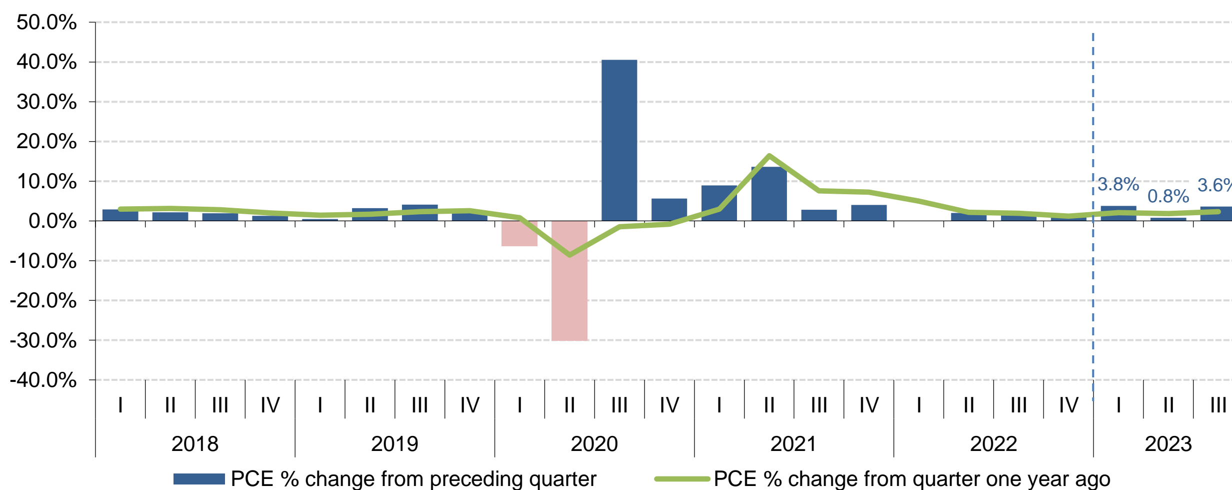
Figure 6
United States real GDP quarterly growth, first quarter 2018—third quarter 2023
(Percentage points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic analysis, U.S. Department of Commerce.

The increase in real GDP in the third quarter of 2023 reflected increases in personal consumption expenditures (PCE), private inventory investment, exports, state and local government spending, federal government spending, and residential and non-residential fixed investment. Imports, which are a subtraction in the calculation of GDP, increased, leading trade to be a slight drag on growth in the third quarter. PCE, the most important source of growth in the third quarter, increased 3.6%, a surge from the 0.8% increase in the second quarter (figure 7).

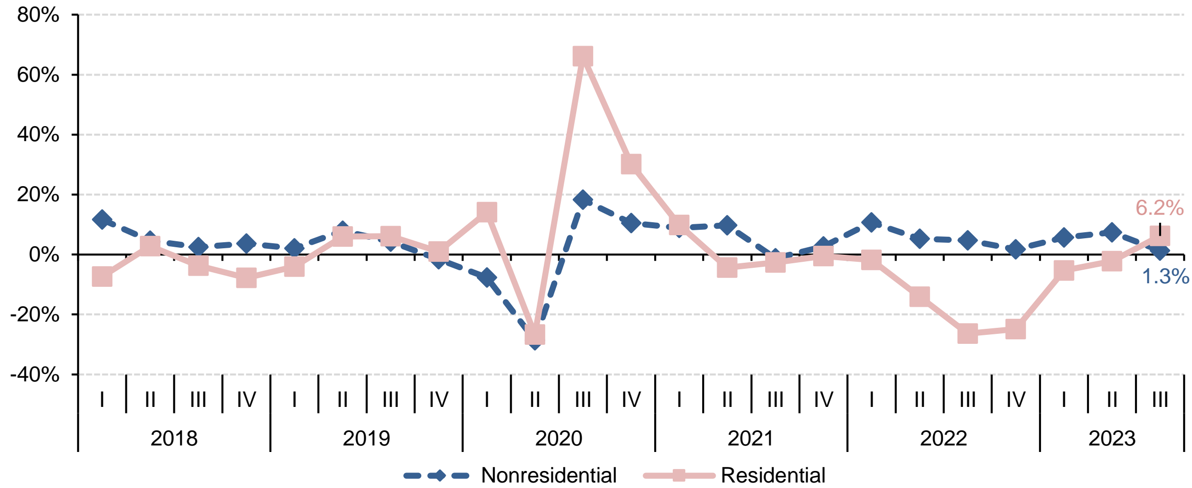
Figure 7
United States personal consumption expenditure growth, first quarter 2018—third quarter 2023
(Percentage points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

Fixed investment, which includes residential and nonresidential investment, increased 2.4% in the third quarter, less than in the first (3.1%) and second (5.2%) quarters. Residential investment increased at an annual rate of 6.2%, the first quarterly increase after nine consecutive quarters of decline. Non-residential investment grew 1.3%, following increases of 5.7% and 7.4% in the first and second quarters, respectively (figure 8).

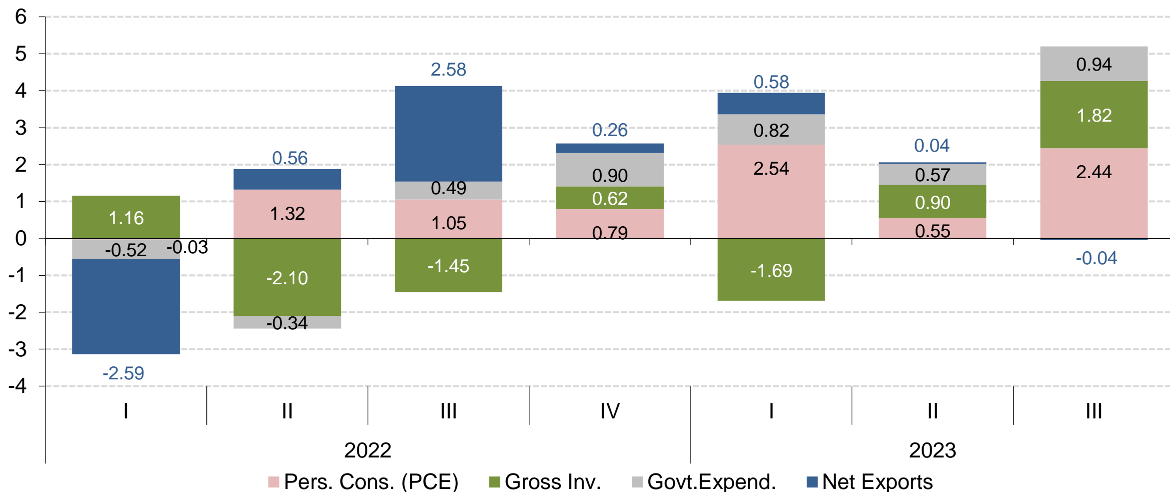
Figure 8
United States fixed investment growth, first quarter 2018—third quarter 2023
(Percentage points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

Nonresidential fixed investment made its smallest contribution to growth in two years, but residential investment made its first contribution to growth since the start of 2021. Nonresidential investment contributed 0.18%, while residential investment added 0.24%. Fixed investment thus added 0.42% to growth in the third quarter. Private wholesale inventory accumulation added 1.40%, the second largest positive contribution to growth in the third quarter. Overall, gross private domestic investment added 1.82% to third quarter growth (0.42% from fixed investment plus 1.40% from change in private inventories) (figure 9).

Figure 9
Contributions to U.S. real GDP growth, first quarter 2022—third quarter 2023
(Percentage points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.
Note: Contributions to growth are measured at seasonally adjusted annual rates.

Government spending increased 5.5% in the third quarter, following increases of 4.8% and 3.3% in the first and second quarters, respectively. It added 0.94% to the third quarter growth.

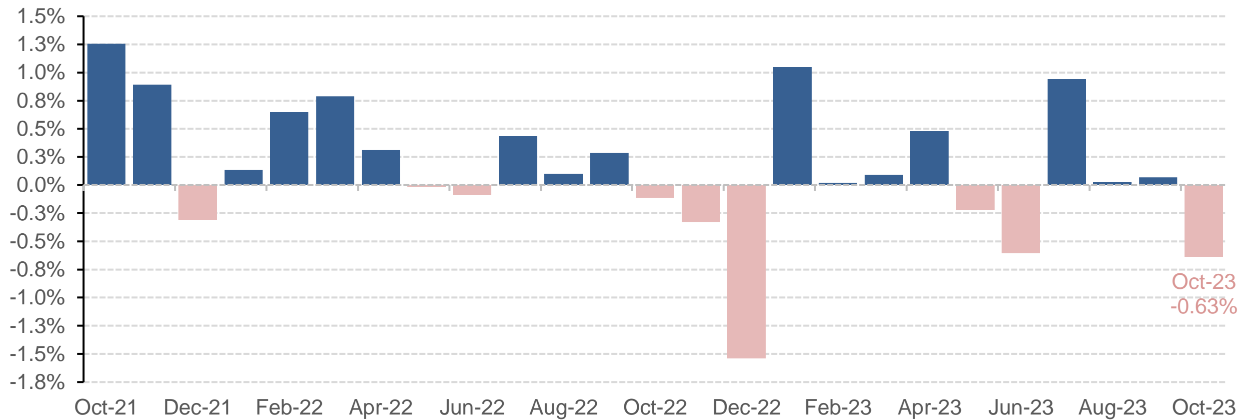
Exports increased 6.0% in the third quarter, following a decline of 9.3% in the second. Exports of goods and services increased by 7.7% and 2.7%, respectively. Imports, a subtraction to growth, increased 5.2%, reflecting increases in both goods and services (6.0% and 1.9%, respectively). Overall, net exports subtracted 0.04% from growth.

The United States economy's recent performance has consistently exceeded the expectations of those who anticipated a recession by now, and the strong growth reported for the third quarter has reiterated this trend.

B. Industrial production

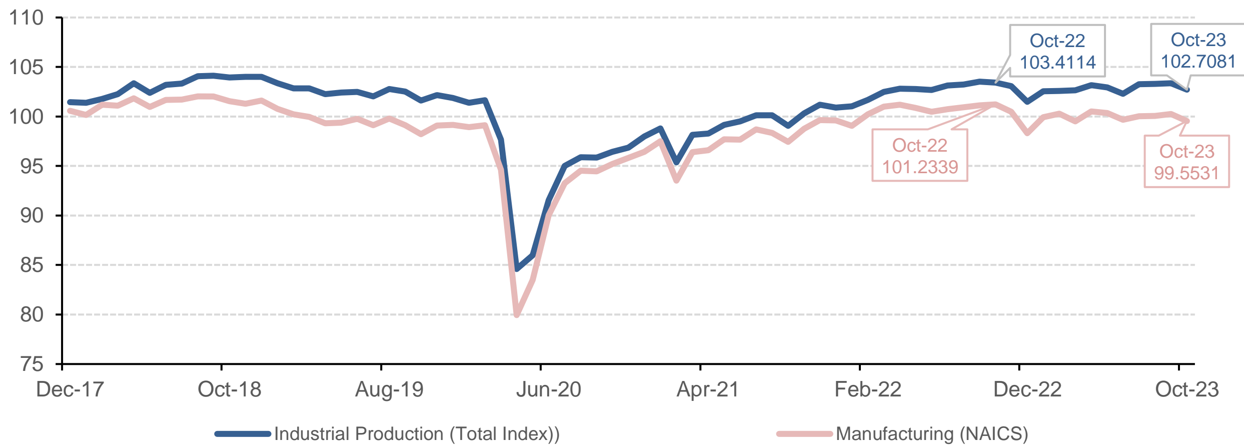
U.S. industrial production data were weaker than anticipated in October 2023. Total industrial production contracted 0.6% in October and was 0.7% lower than a year ago, signaling that the long and lagged effects of monetary policy may be gradually being felt at the more interest-rate-sensitive sectors of the economy (figures 10 and 11).

Figure 10
United States industrial production and manufacturing output, October 2021—October 2023
(Index 2017=100, Monthly, Seasonally Adjusted; Monthly Percent Change;)



Source: ECLAC Washington Office, based on data from the U.S. Federal Reserve and the Federal Reserve of St. Louis (FRED).

Figure 11
United States industrial production and manufacturing output, December 2017—October 2023
(Index 2017=100, Monthly, Seasonally Adjusted)



Source: ECLAC Washington Office, based on data from the U.S. Federal Reserve and the Federal Reserve of St. Louis (FRED).

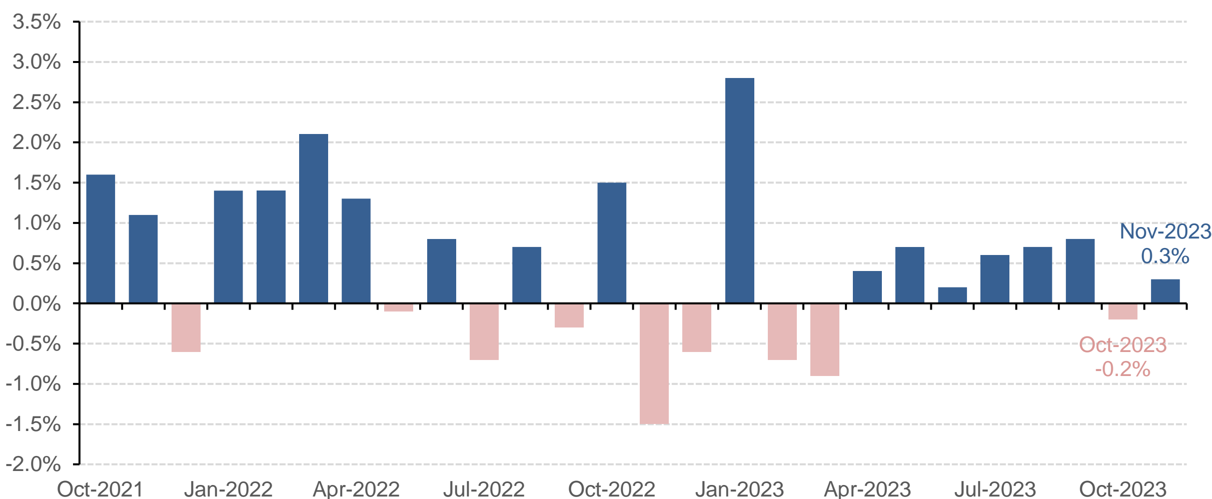
Manufacturing output contracted by 0.7% after a 0.2% increase in September and is 1.7% lower than at the same time last year (figure 11), as the effects of the Federal Reserve's interest rate hikes hit more sensitive goods industries. Capacity utilization for manufacturing contracted from 77.8% to 77.2%.

C. Retail sales

Retail sales, which include spending at stores, restaurants, dealerships and online, rose a seasonally adjusted 0.3% in November from the month before, the Commerce Department said on 14 December. That was a rebound from October's downwardly revised 0.2% decline and a surprise to economists who had expected sales to fall again last month. Excluding gasoline and auto sales, retail spending rose 0.6% last month from October, after increasing just 0.1% the prior month, suggesting U.S. consumer s[pending remains robust. Overall sales rose 4.1% in November from a year earlier, outpacing cooling inflation.

The resilience of retail sales throughout 2023, despite occasional fluctuations, mirrors broader economic patterns. Consumers' willingness to spend, particularly online and at food service establishments, continues to support retail figures. This is against a backdrop of fluctuating gasoline prices, which, while contributing to retail strength in certain months, also underline persistent inflationary pressures. Solid consumer spending, coupled with easing inflation and low unemployment, point to an economy heading toward a soft landing.

Figure 12
United States total retail sales, October 2021—October 2023
(Seasonally adjusted, Month to month percentage change)



Source: ECLAC Washington Office, based on data from Advance Monthly Sales for Retail and Food Services, U.S. Census Bureau.

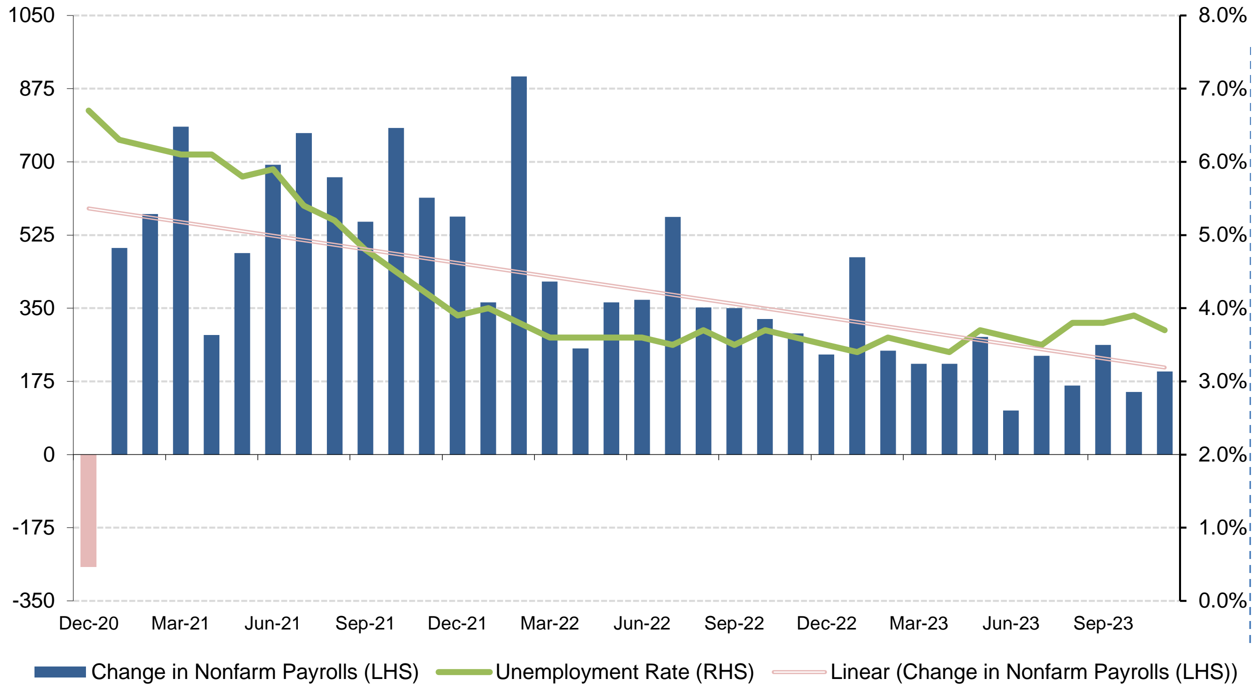
D. Labor market

Hiring has remained robust throughout 2023.The U.S. economy added 2.6 million jobs from January to November 2023 on a seasonally adjusted basis, averaging 232,000 jobs per month. November 2023 was the 35th consecutive monthly gain, even as policymakers take significant steps to cool the economy and ease inflation, but employment creation is trending lower (see linear trend in figure 13).

The unemployment rate reached a historic low of 3.4% —the lowest rate since 1969— in January and April 2003, and was at 3.7% at the end of November, down from October's 3.9% rate, the year's peak. The labor force participation rate was at 62.8% in November and has been at that level since August (with the exception of October, when it went down to 62.7%). This is the highest rate since February 2020 (figure 14). According to

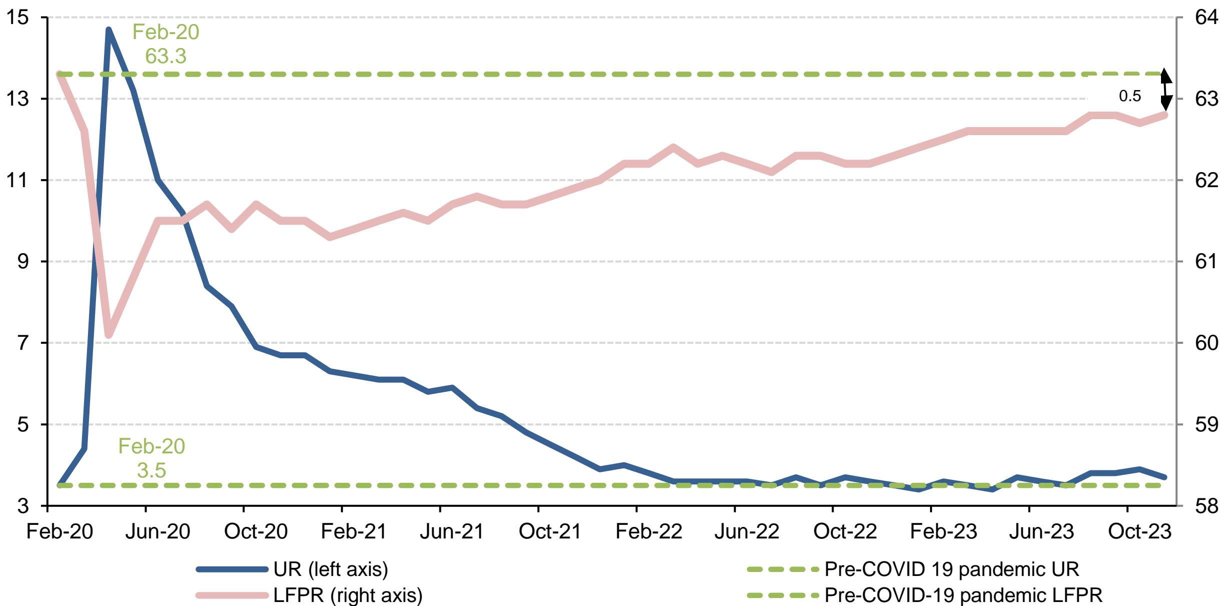
the Bureau of Labor Statistics, despite gradual recovery, the labor force participation rate (LFPR) in November 2023 remained a half percentage point lower than that of February 2020.

Figure 13
United States monthly job creation and unemployment rate, December 2020—November 2023
(Average monthly job growth in thousands (left axis); Percentage (right axis)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

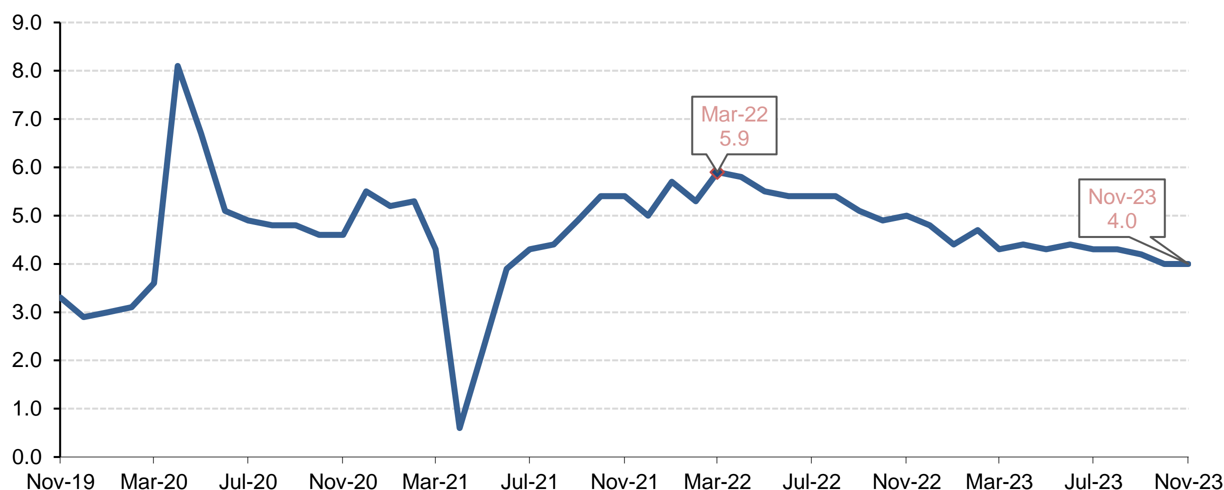
Figure 14
United States labor force participation share, February 2020—November 2023
(Percentage)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics. UR: unemployment rate; LFPR: labor force participation rate.

While the labor-force participation rate has edged up in recent months, wage growth has slowed, both signs of a looser labor market. Hourly earnings were up 4% in November year-on-year, down from a peak of 5.9% in March 2022 (figure 15).

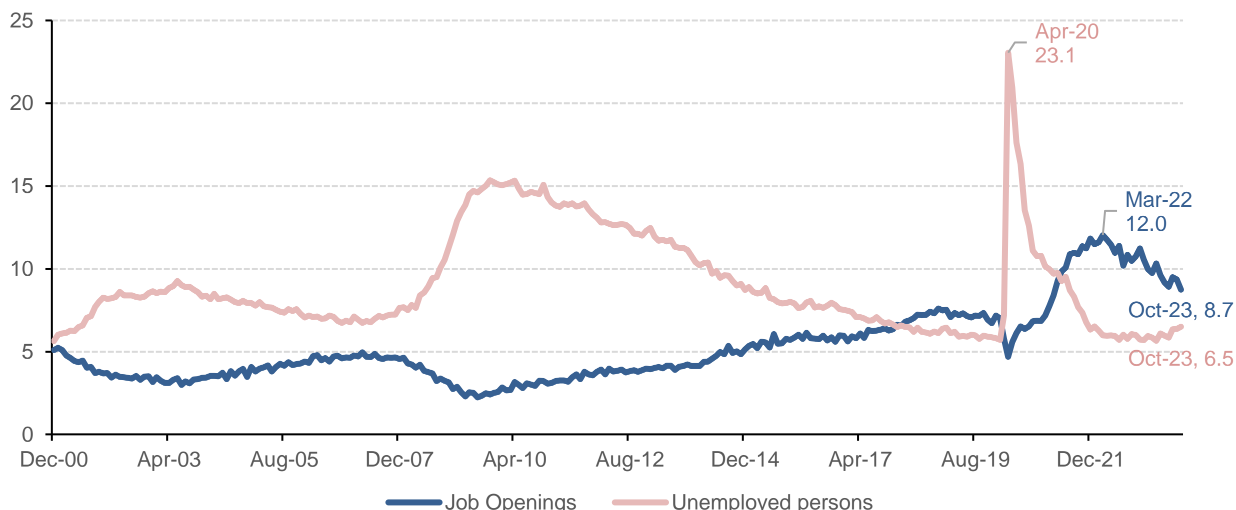
Figure 15
United States average hourly earnings, November 2019—November 2023
(Percentage change from a year ago)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

Despite the resilience in wages and solid job gains so far this year, labor market conditions are easing gradually. According to the latest Job Openings and Labor Turnover Survey (JOLTS) released on 5 December 2023, job openings fell to 8.7 million on the last business day of October, the lowest figure since March 2021. Job openings have been on a downward trajectory since reaching a peak in March 2022, as the Federal Reserve works to cool the labor market. Job openings in October still far outnumbered the 6.5 million unemployed people seeking work, indicating the labor market remained tight (figure 16).

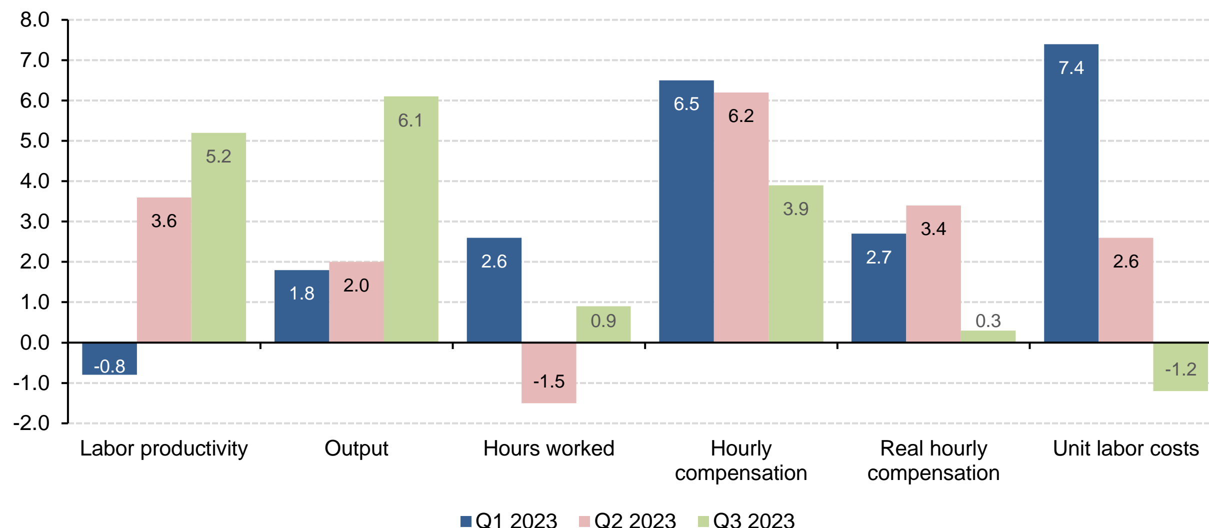
Figure 16
United States job openings vs number of unemployment persons: December 2000—October 2023
(Millions of openings and persons)



Source: ECLAC Washington Office, based on data From FRED Graph Observations, Federal Reserve Bank of St. Louis, Job Openings: Total Nonfarm, Level in Thousands, Monthly, Seasonally Adjusted and Unemployment Level, Thousands of Persons, Monthly, Seasonally Adjusted.

Improved labor productivity gains have contributed to the U.S. economy's resilience. The 5.2% annualized climb in U.S. labor productivity in the third quarter of 2023 exceeded expectations and is the strongest quarterly rate since the early recovery from the COVID-19 pandemic in mid-2020. In the third quarter, output increased 6.1% at an annualized rate while hours worked went up 0.9%. Unit labor costs fell by 1.2% after increasing 2.6% in the second quarter (figure 17). On the inflation front, strong productivity growth means fewer wage increases are passed through to consumer prices. In addition, in the context of the recent above-potential U.S. economic growth, above-trend productivity gains is good news for monetary policy.

Figure 17
United States productivity and costs: first, second and third quarters of 2023
(Percent change from previous quarter at seasonally adjusted annual rates)



Source: U.S. Bureau of Labor Statistics.

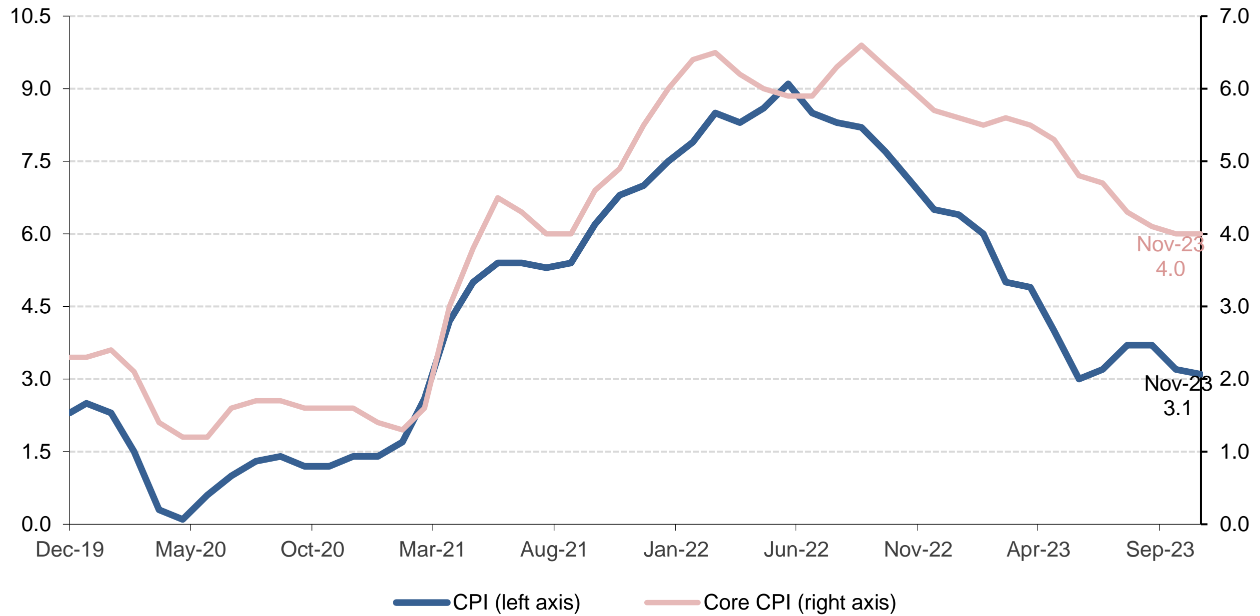
E. Inflation

Building on a trend of moderating price increases since inflation reached a peak of 9.1% in June 2022, the Consumer Price Index for All Urban Consumers (CPI-U) —which measures the costs of everyday goods and services from food to dental care— advanced 3.1% in November 2023 at an annualized rate, down from 3.2% in October, the second lowest headline inflation number since March 2021 (the lowest was a reading of 3% in June). Energy prices were a disinflationary force as gasoline prices declined.

Prices excluding food and energy, the core CPI, rose 4.0% at an annualized rate in November 2023, same as in October, and the smallest 12-month increase in two years (figure 18). Looking forward, it is possible that softer economic growth and a continued normalization in the labor market may contribute to drive a sharper-than-expected fall in core inflation over the next 12 months.

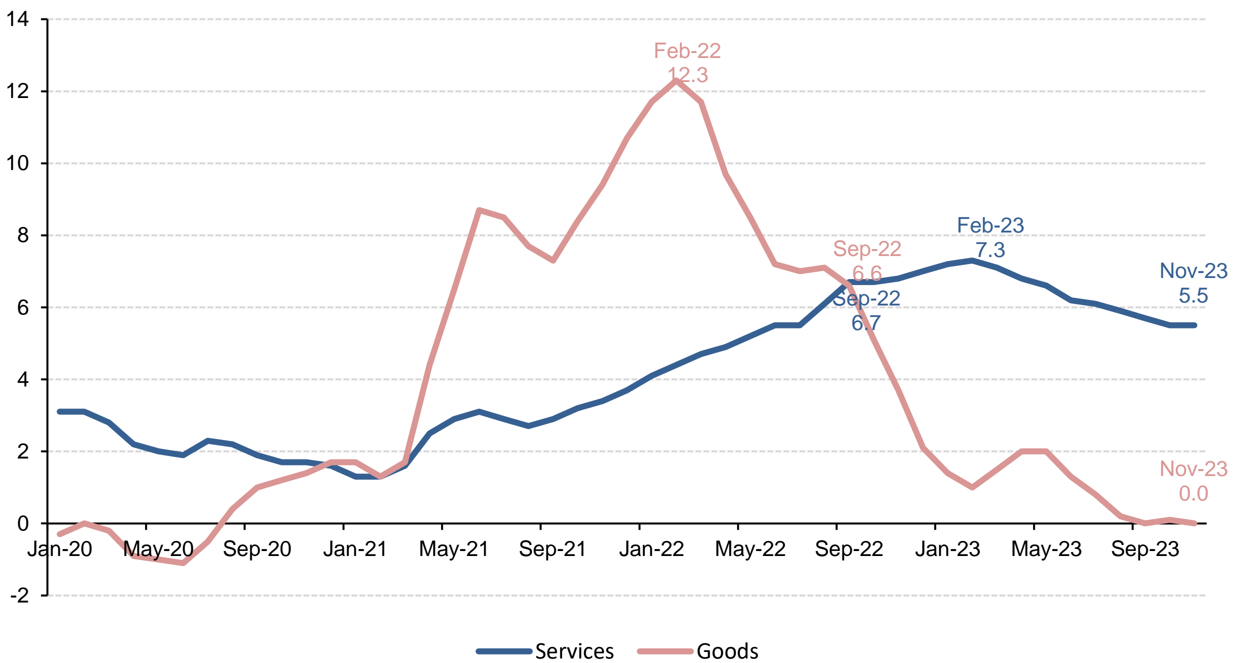
In the twelve months leading up to November 2023, core goods prices registered no increase in November 2023, continuing the downward trend observed since the earlier in the year's peak—a 2% increase in April and May. The overall peak (12.3%) was reached in February 2022. This suggests that the supply chain issues that previously escalated the costs of goods are being mitigated. As of November 2023, the inflation rate for services stood at 5.5% year-over-year, showing a decrease from February's high of 7.3%, yet indicating that cost pressures within the service sector persist (figure 19).

Figure 18
United States domestic prices: monthly evolution, December 2019—November 2023
(CPI-U unadjusted 12 months percent change)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

Figure 19
Core goods and services United States domestic prices: monthly evolution, December 2019—November 2023
(12 months percent change)



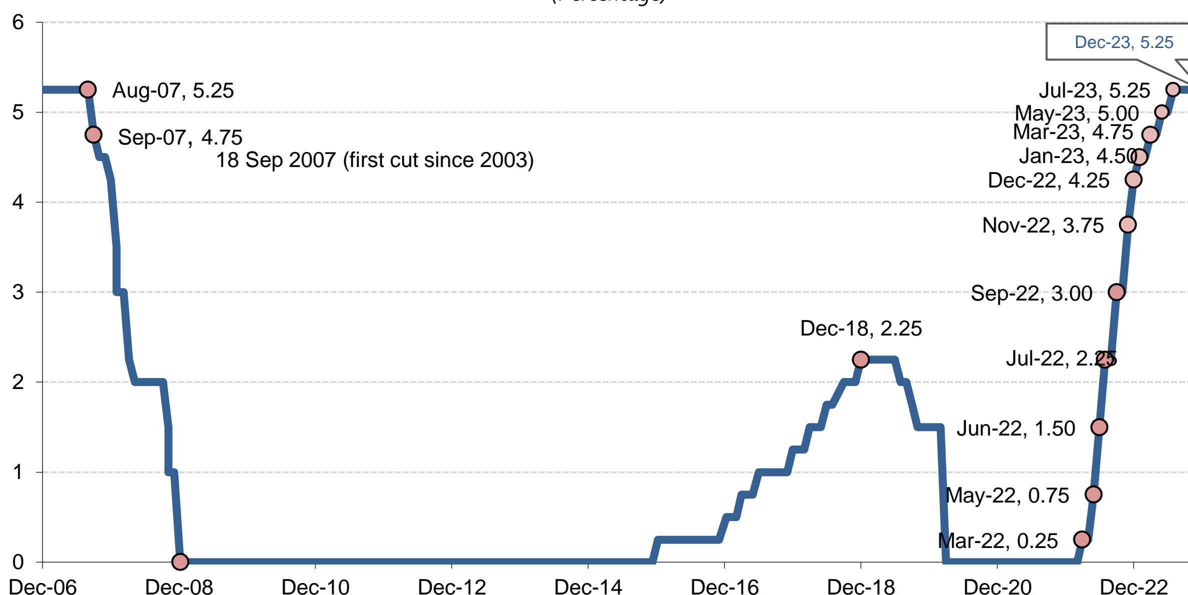
Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

F. Monetary policy

On 13 December 2023, the Federal Reserve held interest rates steady for a third consecutive meeting. This was their final policy decision of 2023. Fed officials signaled inflation had improved more rapidly than anticipated, opening the door to rate cuts next year. Most Fed officials penciled in three interest rate cuts for 2024 in projections released after their two-day meeting.

In an expected move, Fed officials voted unanimously to hold the federal funds rate's target range at 5.25%-5.50%, a 22-year high. As the previous section showed, inflation has trended downward steadily, allowing the committee to step back and evaluate the economy's reaction to its post-pandemic tightening. The Federal Reserve raised interest rates four times in 2023. There were quarter-point interest rate increases in January, March, May and July 2023 (figure 20).

Figure 20
U.S. federal funds target rate, December 2006—December 2023
(Percentage)



Source: ECLAC Washington Office, based on data from the U.S. Federal Reserve. Rates in the chart are the bottom limit of the target range for the federal funds rate.

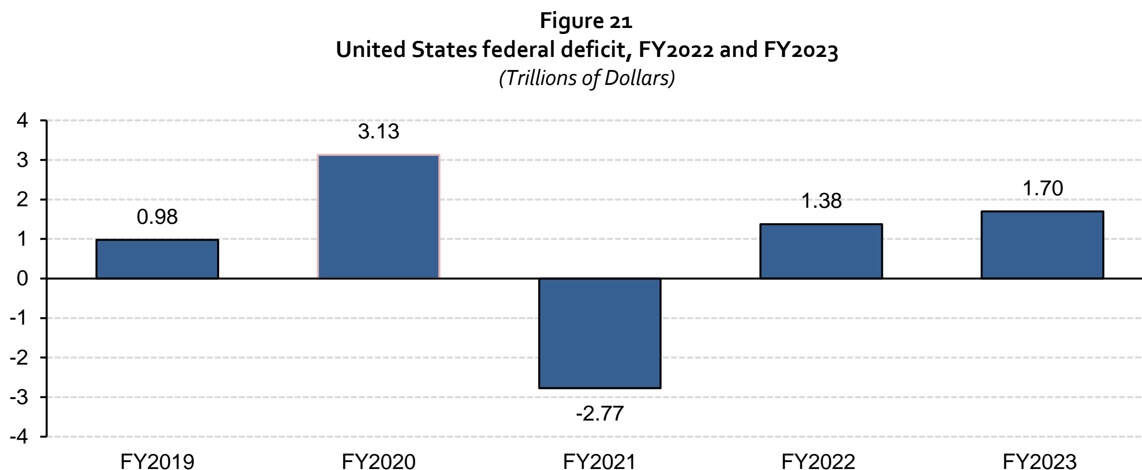
The so-called dot plot —a chart that summarizes the Federal Open Market Committee's (FOMC) outlook for the federal funds rate— showed that most officials expected rates would end next year at 4.5% to 4.75%, suggesting three quarter-point cuts from current levels in 2024. The dot plot showed expectations for rates to fall even lower in 2025, with most officials forecasting rates would end up between 3.5% and 3.75%. Expectations for a steeper pace of rate cuts next year triggered a rally in U.S. stocks and sharp fall in Treasury yields, with the two-year yield recording its biggest daily decline since the collapse of Silicon Valley Bank in March.

In a statement, the central bank described the conditions under which it would consider "any additional policy firming that may be appropriate to return inflation to 2 per cent over time" — softer language that suggests the central bank may not see a further need to raise rates again. At the press conference following the decision, Federal Reserve Chair Jerome Powell said the inclusion of the word "any" reflected a view that the policy rate was "likely at or near its peak for this tightening cycle." He also added that while officials "do not view it as likely to be appropriate to raise interest rates further, neither do they want to take the possibility off the table".

G. Fiscal policy

The United States federal deficit increased by 23% in the 2023 fiscal year (FY) compared with FY 2022. The cumulative deficit came to US$ 1.7 trillion, up US$ 320 billion from fiscal 2022 (figure 21).

Figure 21
United States federal deficit, FY2022 and FY2023
(Trillions of Dollars)



Source: ECLAC Washington Office, based on data from the U.S. Treasury Departments and FRED Graph Observations, Federal Reserve Bank of St. Louis.

Moody's Investors Service on 10 November 2023 announced it was revising the outlook on the U.S. government's ratings to negative, while affirming the long-term issuer and senior unsecured ratings at Aaa. A key driver to the outlook change was Moody's assessment that downside risks to the country's fiscal strength have increased "and may no longer be fully offset by the sovereign's unique credit strengths." Given higher interest rates and without effective measures to reduce government spending or increase revenues, the agency said it expects fiscal deficits will remain very large and debt affordability would be significantly weakened. The rise in Treasury bond yields has increased pre-existing pressure on debt affordability, Moody's added. The agency expects interest payments relative to revenue to rise to around 26% in 2033 from 9.7% in 2022. Additionally, Moody's said it sees interest payments relative to GDP will rise to around 4.5% in 2033, from 1.9% in 2022. In affirming the country's rating, Moody's said the United States' "formidable credit strengths continue to preserve the sovereign's rating, in particular exceptional economic strength, high institutional and governance strength, and the unique and central roles of the U.S. dollar and Treasury bond market in the global financial system." [2]

H. Financial conditions

Despite monetary policy tightening, United States stocks have performed well in 2023 year-to-date (as of 12 December 2023), with the largest gains in tech stocks, from cloud computing to generative AI. The S&P 500 index gained 21%, the Dow Jones Industrial Average 10%, and the NASDAQ composite 40%. Stocks have been gaining since October, as investors bet that the Federal Reserve's monetary policy tightening cycle has peaked (figure 22). On 12 December, the Chicago Board Options Exchange Volatility Index (VIX) —a primary gauge of stock market volatility— reached a new yearly low, approaching levels last seen in January 2020, pointing to market optimism. During much of the year market participants were cautious, concerned about a slowdown in growth and even a recession, but economic resilience and the retreat in inflation has led them to rethink this strategy.

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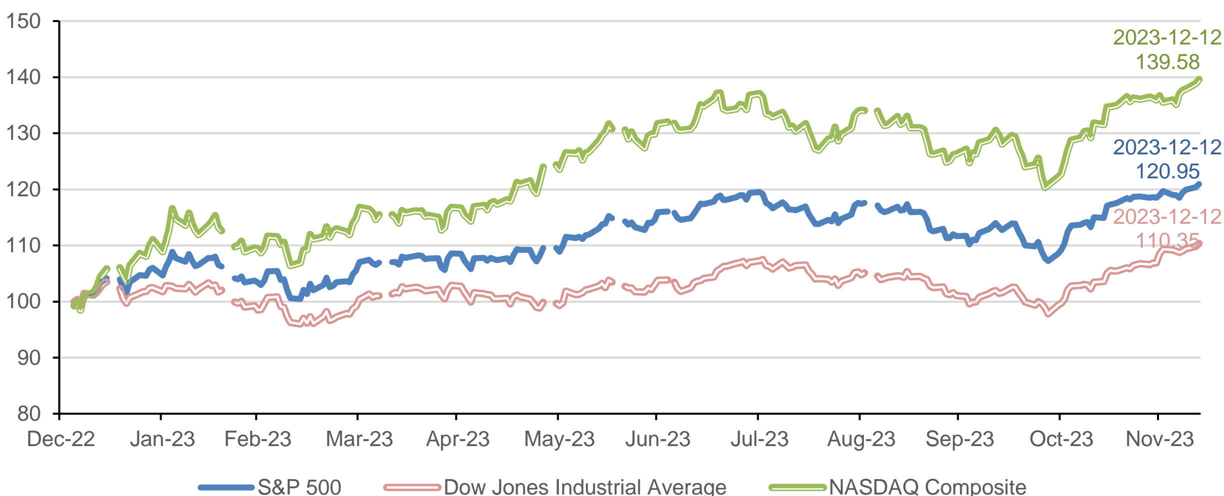
[2] Moody's Rating Action, "Moody's changes outlook on United States' ratings to negative, affirms Aaa ratings" 10 November 2023 [online] https://ratings.moodys.com/ratings-news/411110.

Figure 22
U.S. stock market indices, 30 December 2022—12 December 2023
(Daily, not seasonally adjusted; 30 December 2022=100)

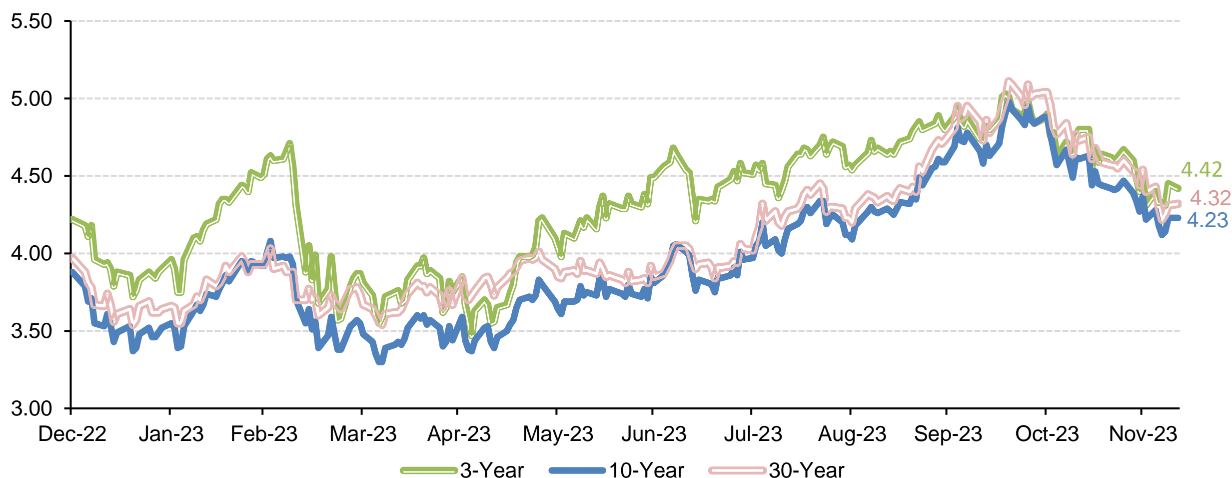


Source: ECLAC Washington Office, based on data from the Federal Reserve of St. Louis (FRED).

In the U.S. Treasury market, the 3-year, 10-year and 30-year Treasury yields were at 4.42%, 4.23% and 4.32%, respectively, on 11 December 2023 (figure 23). Government bond yields, which have stirred much of the recent volatility, declined after breaching 5% for the first time in 16 years in October.

According to Morning Star MarketWatch, a "5% 10-year rate is regarded by investors as a significant milestone for a number of reasons. One is that it generally makes government debt more appealing when compared to stocks, as traders and investors factor in a higher cost of doing business by companies and discount the value of their future earnings."[3] With Treasury yields declining since their peak in October, investors are growing more bullish about stocks.

Figure 23
U.S. Treasury security yields, 30 December 2022—12 December 2023
(Constant maturities; daily yields)



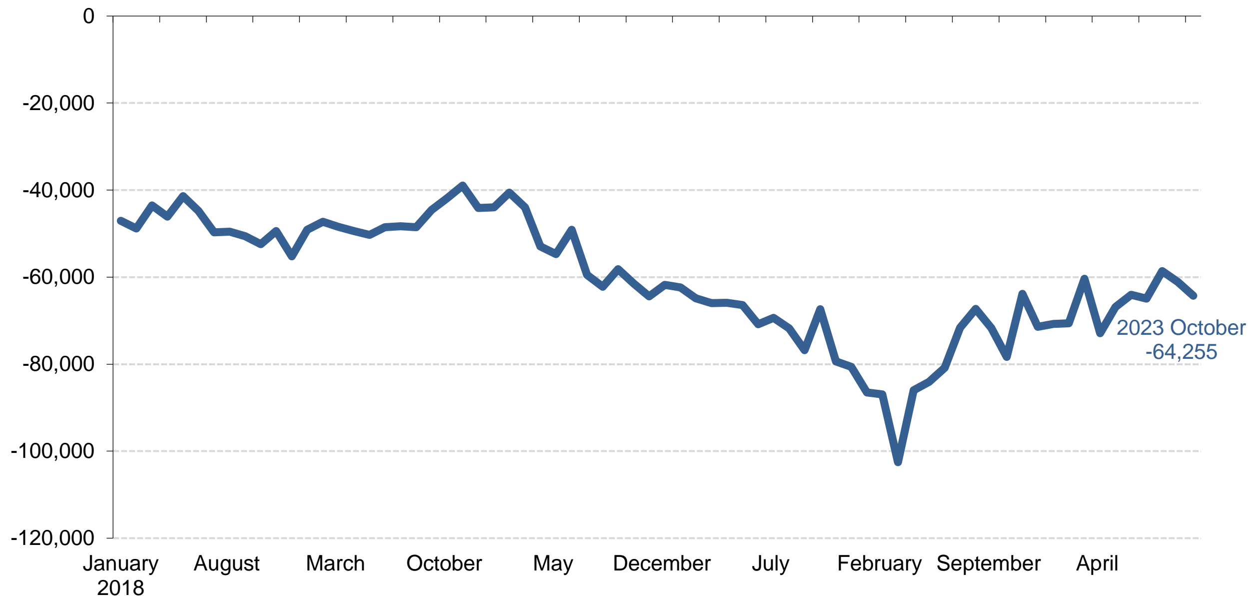
Source: ECLAC Washington Office, based on data from the Federal Reserve of St. Louis (FRED).

[3] Morning Star MarketWatch, 19 October 2023, https://www.morningstar.com/news/marketwatch/20231019567/why-stock-market-investors-are-fixated-on-5-as-10-year-treasury-yield-nears-key-threshold.

I. External sector

In October 2023, latest data available, the U.S. trade deficit in goods and services grew to US$ 64.3 billion from US$ 61.2 billion in September, according to data released on 6 December 2023 by the Bureau of Economic Analysis, as imports rose and exports declined (figure 24).

Figure 24
United States balance on goods and services trade, January 2016—October 2023
(Millions of dollars, months seasonally adjusted)



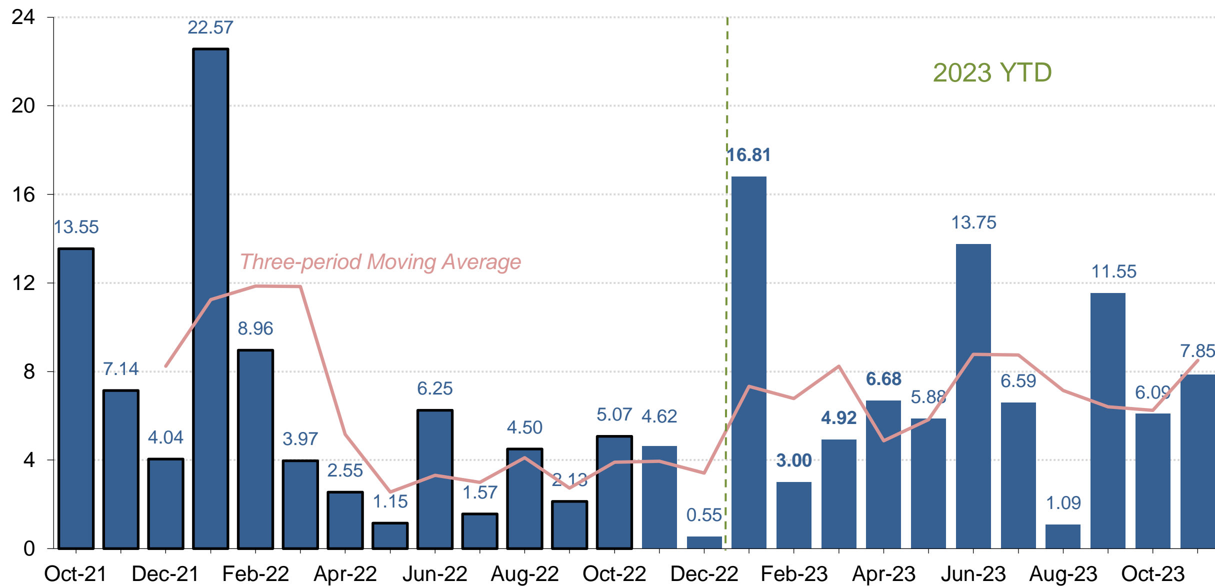
Source: U.S. Census Bureau and the Bureau of Economic Analysis, U.S. Commerce Department.

The rise in the nominal trade deficit in October was driven by a 1.0% month-on-month fall in exports. The United Automobile, Aerospace and Agricultural Implement Workers of America (UAW) strike was a factor, as falling motor vehicle exports accounted for a third of the total decline. With the strike over, this will no longer be a factor in November. The trade deficit is trending smaller this year, but fluctuations in petroleum prices and disruptions due to the autoworker strike have contributed to monthly volatility.

II. Impact on Latin American and Caribbean financial conditions

Latin American and Caribbean (LAC) bond issuers placed US$ 84.2 billion in international bond markets from January to mid-November 2023, with an average coupon that was 1.5% higher than in the same period in 2022. This total was 32% higher than the 2022 annual volume (figure 27). More recently, the region's bond issuances have been supported by speculation that the United States Federal Reserve's interest rate hikes may have peaked.

Figure 25
Monthly LAC international bond issuance, October 2021–15 November 2023
(Billions of dollars)



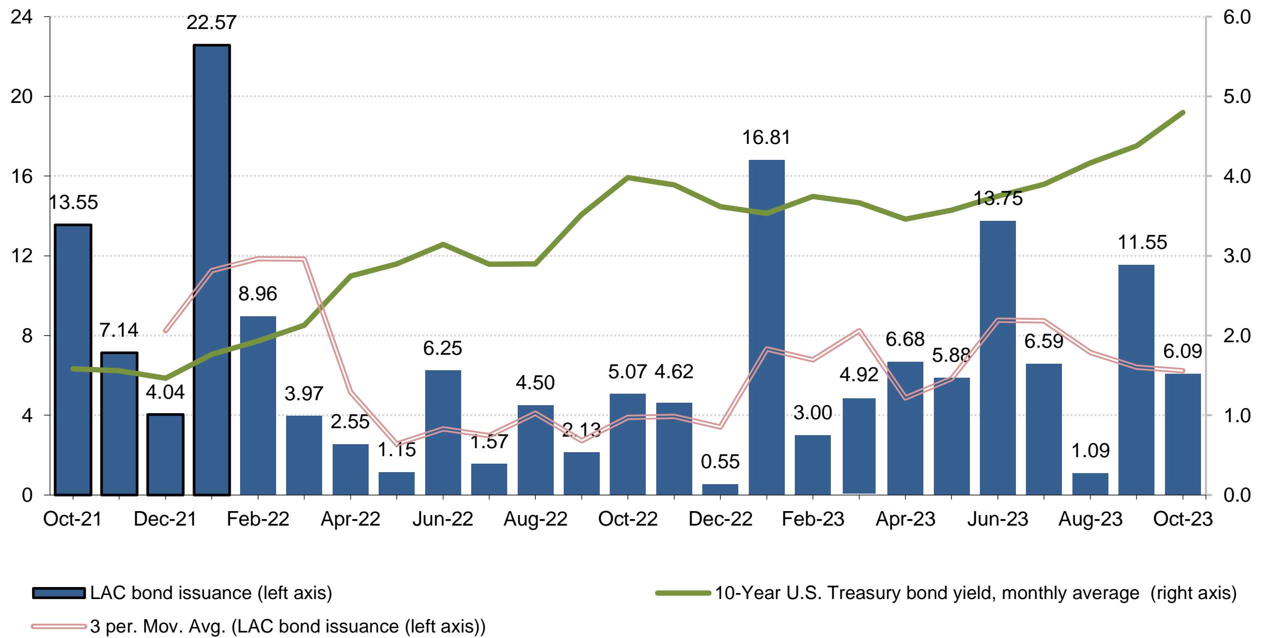
Source: ECLAC, Capital flows to Latin America and the Caribbean: first ten months of 2023 (LC/WAS/TS.2023/8), Santiago, 2023 <online> https://www.cepal.org/en/publications/49048-capital-flows-latin-america-and-caribbean-first-half-2023

Despite a rebound in the region's international bond issuances this year, global financial conditions remain challenging for the region's sovereign and corporate issuers due to higher borrowing costs and tighter lending conditions, adding to their domestic challenges. The Federal Reserve hit pause on its benchmark interest rate increases at its 13-14 June meeting (after hiking it ten times in a row), only to increase it again in July by 25 basis points. Since then, the Fed has kept its benchmark interest rate unchanged at a range of 5.25%-5.50%, the highest level since 2001. In addition, throughout most of September and October, U.S. 10-year Treasury yields climbed towards 5%, perceived by markets as an important threshold (figure 28).

Figure 26

LAC international bond issuance and 10-year U.S. Treasury yield, October 2021–October 2023

(Left axis, billions of dollars; Right axis, percentage)



Source: ECLAC, Capital flows to Latin America and the Caribbean: first ten months of 2023 (LC/WAS/TS.2023/3), Santiago, 2023 <online> https://www.cepal.org/en/publications/68745-capital-flows-latin-america-and-caribbean-first-10-months-2023.

The 10-year Treasury yield serves as a vital economic benchmark. It influences borrowing costs for consumer and businesses and has big implications for the value of emerging market debt securities. When it moves higher, there is an adverse impact on the international bond issuances from Latin America and the Caribbean. In early November, amid growing expectations the Federal Reserve's hiking cycle is coming to an end, a rally in U.S. Treasuries pushed 10-year yields down to their lowest level in five weeks. In response, four sovereign and two corporate issuers from the region came to the international bond market in the first two weeks of November, issuing close to US$ 8 billion of international bonds, a total that was almost 30% higher than the volume for the whole month of October.

III. Looking ahead

In the third quarter, the United States economy grew at the fastest pace in nearly two years. The labor market has remained strong this year —2.6 million jobs were added from January to November 2023 and November marked the 35th consecutive month of job gains— but it is gradually cooling down. The unemployment rate was at 3.7% in November and remains historically low.

Inflation is also gradually decelerating. The economy seems to have overcome supply chain disruptions and the aggressive tightening in monetary policy over the past year and a half has contributed towards reducing excess demand. While inflation started in goods affected by supply chain issues, as supply chain pressures eased, the prices of services rose. According to data from the Bureau of Labor Statistics, for the 12 months ended in November 2023, core service prices were up 5.5% (down from a peak of 7.3% in February 2023) while core goods prices, down from a peak of 12.3% in February 2022, showed no increase.

The Federal Reserve is approaching the end of its monetary tightening cycle. At the press conference following the central bank's final policy decision of 2023 on 13 December, Federal Reserve Chair Jerome Powell said the policy rate was "likely at or near its peak for this tightening cycle." He also added that while officials "do not view it as likely to be appropriate to raise interest rates further, neither do they want to take the possibility off the table".

The December projections released after the meeting show that Fed officials anticipate three rate cuts in 2024, which has an impact on the financing costs for Latin American and Caribbean (LAC) countries. LAC debt issuers that had been waiting for lower borrowing costs have begun to anticipate the end to global interest rate hikes, while accepting that rates may remain higher for longer, and are returning to the international market. The region's cross-border bond market is thus gradually regaining a sense of normalcy.

Optimism for a U.S. soft landing is on the rise. At The Wall Street Journal's CEO Council Summit on 12 December, U.S. Treasury Secretary Janet Yellen said inflation is "meaningfully coming down" and that the U.S. economy is on the path towards a soft landing, meaning that inflation is being tamed without causing a deep economic slowdown.[4] Although acknowledging such an outcome would be rare, she says the data are clearly pointing in that direction.

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[4] The Wall Street Journal, "Yellen Says U.S. Economy on Path to Soft Landing", by Andrew Duehren, 12 December 2023 [online] https://www.wsj.com/economy/central-banking/yellen-says-u-s-economy-on-path-to-soft-landing-21fd2883.

The United States economy expanded by 5.2% in the third quarter of 2023, the fastest pace in nearly two years. Consumer spending was the main driver of economic growth in the quarter, followed by accumulation of private inventories. The third quarter marked the fifth consecutive quarter of growth above the economy's potential. Labour market growth remained solid, with 2.6 million jobs added from January to November 2023, but is easing. Inflation is also gradually slowing. Despite interest rate hikes in 2022 and in the first half of 2023, the United States economy —supported by a strong job market and retreating inflation— remains resilient, fuelling optimism that it is on course for a soft landing.

The *United States economic outlook* reports are published three times a year and follow the main macroeconomic developments of the United States economy and how they could affect financial conditions in Latin America and the Caribbean.

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