Louisiana Corporate Credit Union
ECONOMIC & FINANCIAL DIGEST
3500 N. Causeway, Suite 1510 • Metairie, Louisiana 70002 • (800) 421-7030 • www.lacorp.com
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No Time For Complacency

The economy isn't in or flirting with a recession, but that hasn't stopped many from sounding the recessionary alarm. That's not surprising. Heightened uncertainty goes hand in hand with fears of the unknown, and those fears can cause changes in behavior. It's quite possible to talk ourselves into a recession, just as expecting higher inflation can be a self-fulfilling prophecy. It's the job of the Federal Reserve to bring clarity and calm to the discussion so that it can identify and respond to underlying forces rather than subjective influences that it cannot control. Simply put, it needs to separate the noise from the signal when formulating rate-setting decisions.

Unfortunately, that's easier said than done. It's hard to remember another time when the public's mood was as different from its actions as is the case now. The economy is still doing relatively well. The job market is holding up and real incomes are rising, keeping a solid foundation under consumption. Meanwhile, some key inflation measures turned softer in February, reversing a scary jump that occurred in January. The combination of sustained growth and cooling, but still high, inflation reinforces the Fed's decision to keep rates where they are.

But if you look at how people feel, the picture turns considerably darker. Household sentiment is plunging,and inflationary expectations are surging. Investors too are turning skittish, stoking market volatility and pricing in higher odds that the Fed will need to cut rates more times than it currently plans this year to stave off a recession. Gyrating stock prices pose more of a threat to the economy than in the past for a number of reasons, so the trend needs close watching. Importantly, the drumbeat of tariff headlines continues to roil markets and underpin the heightened uncertainty that is rattling households and businesses. Economists have been frantically revising forecasts of growth and inflation in response to erratic tariff and other fiscal policy announcements, but no one is confident about how this will end. One thing is clear: the uncertain policy environment has significantly broadened the range of possible outcomes, with both recession and higher inflation on the radar. Against this noisy backdrop, the search for clarity will not be easy, raising the odds of a policy mistake that could send the economy down the wrong path.

Wealth Effect Cuts Both Ways

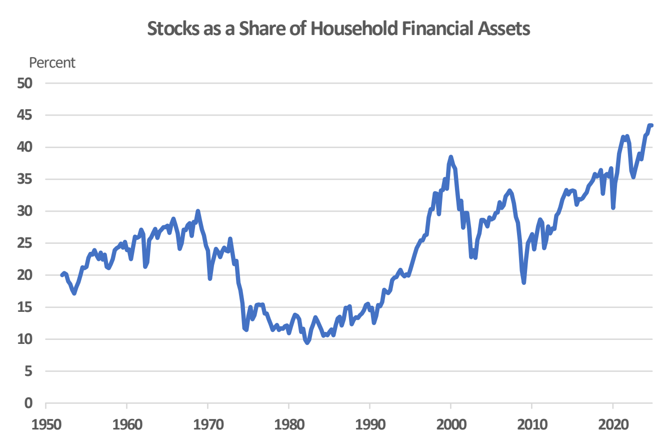
There is a time-honored adage that says the stock market is not the economy. Nor has it been a reliable predictor of economic trends. As noted economist Paul Samuelson famously quipped many years ago, "the stock market has forecasted nine of the past five recessions." Of course, when he made that remark in 1966 stocks were not broadly held nor were they a big part of household wealth. Hence, while people may have conflated trends in stock prices with the economy's performance, most were not deeply affected on a personal level.

That's not the case now. Stock portfolios account for a record share of household financial assets, about double the share of the 1960s. And while price appreciation has contributed importantly to the increase, a broader swath of households now participates in the stock market. largely through 401(K)s and other retirement plans. Unsurprisingly, the influence of the stock market has grown accordingly. When people feel wealthier, they save less and spend more – and vice versa. The positive wealth effect had a meaningful impact sustaining consumption last year, even as growth in jobs and wages slowed.

Hence, just as appreciating stock portfolios in recent years boosted spending more than would be indicated by income growth, just the opposite is likely should stock losses erode the financial wealth of households. Despite the modest correction in February and early March, however, investors retain a formidable cushion from the gains built up in recent years, so the near-term spending outlook is still positive. But the growing importance of risky stocks as an asset holding of households makes the economy more vulnerable to a bear market, particularly amid cooling job and income growth.

Stagflation Fears

One of the biggest fears among investors as well as policy makers is that the economy is flirting with a case of stagflation. There is no definitive measure of this condition, which is broadly thought to exist when the economy is growing below its potential



and inflation is exceeding a certain target, currently 2 percent, for a sustained period of time. Sustainability is the key qualifier because both sides of the lever can move outside of those parameters for brief periods, such as when an external shock like an oil or health crises hits – or, more relevant now, higher tariffs on imported goods.

One measure that mimics stagflation is the so-called Misery Index, which combines the increase in the consumer price index with the unemployment rate, a proxy for growth. The most extreme cases occurred in the 1970s and early 1980s, when periods of high unemployment and inflation sent monetary policy into a frenzy of extreme rate changes, pushing them up to crush inflation and then down to resuscitate growth, setting the stage for a rapid-fire series of recessions that cured neither. That unstable era reflected the Fed's difficult task of achieving its dual mandate of maximum employment and price stability when those goals are moving in opposite directions.

The question is, at what point does the combination of unemployment and inflation meet the condition of stagflation, which effectively leads to a Hobson's choice for the Fed: either raise rates to curb inflation – and risk a recession – or lower them to prevent rising unemployment – and risk more inflation. Unfortunately, there is no widely accepted number, as it changes over time. But many believe that stagflation is reached when inflation is running 1 percent above the Fed's target, currently 2 percent, and unemployment rises 1 percent above the level consistent with full employment, currently estimated at 4.3 percent. That would put the threshold at 8.3 percent – 1.4 percent above the current 6.9 percent. That's about where it was a year ago, as the rise in the unemployment rate has just about offset the decline in inflation.

No Hurry to Cut Rates

At its latest policy meeting on March 19-20, the Fed increased its year-end forecast for both inflation and unemployment, but not enough to reach the point of stagflation. Importantly, neither trend is expected to persist, as both inflation and unemployment is projected to decline next year. However, inflation is expected to decline more, closing in on the 2 percent target, which opens the door for two more rate cuts the Fed intends to make this year to keep the economy on a growth trajectory.

We agree that there is no hurry to cut rates, as the current and projected unemployment rate remains near historically low levels and well below the level seen in past recessions. And with inflation still above the 2 percent target, and projected to move higher this year, the Fed unsurprisingly feels comfortable keeping its policy rate steady at a modestly restrictive level. At this juncture, the Fed sees the risk of higher inflation greater than the risk of a recession. Importantly, for the first time in his press conference, Fed Chair Powell acknowledged that announced and prospective tariffs underpin the higher inflation forecast this year.

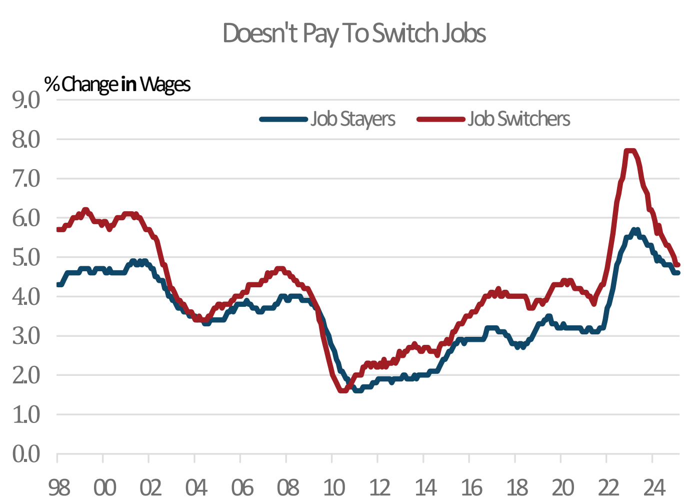
But a key element in the Fed's outlook – and that of many private economists – is that the inflationary impact of tariffs is temporary, resulting in a one-time increase in the price level. Unless tariffs are imposed over and over again, the rate of price increases – i.e. the inflation rate – should resume its decline next year and reach the 2 percent target by 2027. That makes sense on paper, but there is one caveat that could prevent it from happening. If the tariff-induced increase in the price level stokes a sustained increase in inflationary expectations, a feedback loop would be set in motion that leads to a sustained increase in inflation. It's far too early to know if inflationary expectations have become unanchored, as the latest surge revealed in the University of Michigan survey is only for one month and has not been validated by other indicators, including market-based measures in the bond market.

Risks Could Shift

Firm judgements about what the administration will do on the tariff front is difficult to make, as President Trump has changed course several times – increasing then rescinding or delaying the timing of levies, adjusting the contents of the goods involved, and moving around the trading partners that would be targeted. So far, the main result of the shape-shifting nature of tariff threats has been a surge in uncertainty and a slide in household and business sentiment. There's been scant evidence of harm to the real economy.

But that could change in a hurry, and there may be more cracks under the hood than appreciated. True, the economy's linchpin, the job market, seems healthy on the surface, generating a solid 150 thousand net new payrolls in February. That's more than enough to keep the unemployment rate low, particularly since reduced immigration and increased deportations are restricting the supply of labor. But employment data is a lagging indicator as the process of recruiting, hiring, and onboarding takes time; hence, payroll growth lags shifts in economic activity.

There are indicators that give a sense of early changes in the labor market. Keep in mind that job growth itself is not the sole influence on spending behavior of workers.Job security is just as important. If workers sense that job opportunities elsewhere are dwindling or,worse,expect layoffs to increase, they could well pull in their horns. Both seem to be happening. Surveys reveal that households expect the job market to deteriorate later this year and that is encouraging them to stay put rather the quit and gamble they will find something better. Fed data show that the quit rate has fallen to the lowest level in a decade at the end of last year. What's more, companies are not aggressively competing for workers, as the pay difference between job stayers and switchers has collapsed to the lowest level since 2010. This caution may lift once policy uncertainty linked to tariffs clears up. If it continues, the Fed will be shifting its priority from inflation to preventing a recession sooner rather than later.



KEY ECONOMIC AND FINANCIAL INDICATORS

Financial Indicators *

	February	January	December	November	October	September	August	12-Month Range High	12-Month Range Low
Prime Rate	7.50	7.50	7.65	7.81	8.00	8.30	8.50	8.50	7.50
3-Month Treasury Bill Rate	4.22	4.21	4.27	4.42	4.51	4.72	5.20	5.25	4.21
5-Year Treasury Note Rate	4.28	4.43	4.25	4.23	3.91	3.50	4.16	4.56	3.50
10-Year Treasury Note Rate	4.45	4.63	4.39	4.36	4.10	3.72	4.25	4.63	3.72
30-Year Treasury Bond Rate	4.68	4.85	4.58	4.54	4.38	4.04	4.46	4.85	4.04
Tax-Exempt Bond Yield	4.18	4.19	4.04	4.14	3.96	3.83	3.87	4.19	3.54
Corporate Bond Yield (AAA)	5.32	5.46	5.20	5.14	4.95	4.68	5.12	5.46	4.68
Conventional 30-Year Mortgage Rate	6.84	6.96	6.72	6.81	6.43	6.18	6.85	7.06	6.18
Dow Jones Industrial average	44209	43524	43656	43717	42494	41491	40086	44209	38401
S&P 500 Index	6039	5980	6011	5930	5792	5621	5538	6039	5112
Dividend Yield (S&P)	1.24	1.26	1.24	1.23	1.28	1.31	1.31	1.39	1.23
P/E Ratio (S&P)	25.5	27.2	26.5	27.0	26.0	26.3	25.7	27.2	24.1
Dollar Exchange Rate (vs. Major Currencies)	128.1	129.0	127.8	126.5	123.8	122.1	123.7	129.0	121.0

* Monthly Averages

Economic Indicators

	February	January	December	November	October	September	August	12-Month Range High	12-Month Range Low
Housing Starts (Thousands of Units)	1501	1350	1526	1305	1344	1355	1379	1526	1262
New Home Sales (Thousands of Units)		657	734	679	623	726	691	736	623
New Home Prices (Thousands of Dollars)		446	415	396	426	421	406	446	396
Retail Sales (% Change Year Ago)	3.1	3.9	4.4	4.0	3.0	2.0	2.0	4.40	2
Industrial Production (% Change Year Ago)	1.4	1.9	0.5	-0.8	-0.3	-0.7	-0.1	1.9	-0.8
Operating Rate (% of Capacity)	78.2	77.7	77.6	76.8	77.1	77.4	77.9	78.2	76.8
Inventory Sales Ratio (Months)		1.37	1.35	1.37	1.37	1.37	1.38	1.38	1.35
Real Gross Domestic Product (Annual % Change)			2.3			3.1		3.2	1.6
Unemployment Rate (Percent)	4.1	4.0	4.1	4.2	4.1	4.1	4.2	4.3	3.8
Payroll Employment (Change in Thousands)	151	125	323	261	44	240	71	323	44
Hourly Earnings (% Change Year Ago)	4.0	4.0	4.0	4.2	4.1	3.9	4.0	4.2	3.6
Personal Income (% Change Year Ago)		4.6	5.4	5.1	5.2	4.8	5.0	5.9	4.6
Savings Rate (Percent of Disposable Income)		4.6	3.5	3.8	4.0	3.8	4.2	5.4	3.5
Consumer Credit (Change in Blns. Of Dollars)		18.1	-100.0	-14.0	10.2	3.0	4.3	23.7	-100.0
Consumer Prices (% Change Year Ago)	2.8	3.0	2.9	2.7	2.6	2.4	2.5	3.5	2.4
CPI Less Food & Energy (% Change Year Ago)	3.1	3.3	3.2	3.3	3.3	3.3	3.2	3.8	3.1
Wholesale Prices (% Change Year Ago)	3.2	3.7	3.4	2.9	2.7	2.1	2.1	3.7	2.0

Louisiana Corporate Credit Union

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Fourth Quarter 2024 - By the Numbers

$5.9 billion	Total credit union issuance outstandings.
1,598	Number of credit unions that have issuance agreements in place, prepared to issue share certs, should the need arise.
441	Number of credit unions that currently have custodial share certificate issuance balances through SimpliCD.
$100 million	Largest issuance in a single transaction to date.

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