July 31, 2025

Dutta’s Economic Daily

AI > Consumer for now

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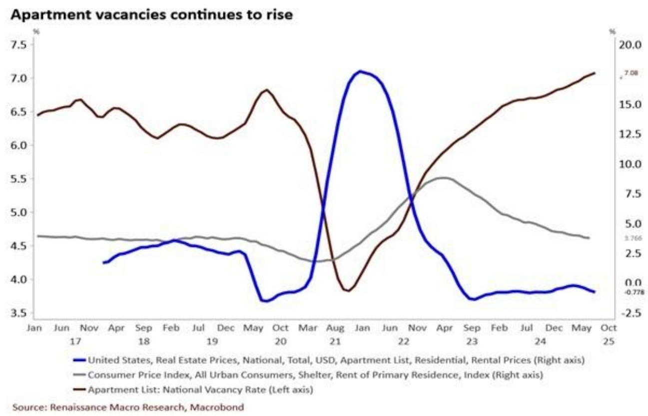
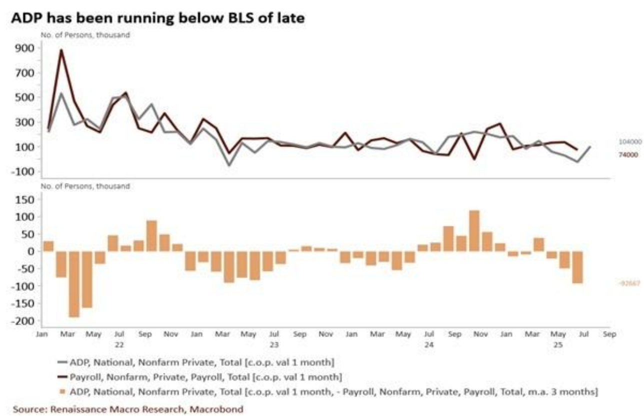
Vacancies climbing

- According to ApartmentList, multi-family vacancies continue to rise in July. To wit, “Our national vacancy index – which measures the average vacancy rate of stabilized properties in our marketplace – ticked up this month and now stands at 7.1 percent. This represents an all-time high for this data series, which goes back to the start of 2017.” Not surprisingly, the ongoing increase in vacancies has kept a lid on rent growth, which has declined 0.8 percent against the same month last year. The drop in rents in the ApartmentList is notable as it leads the more widely measure of CPI housing rental inflation.

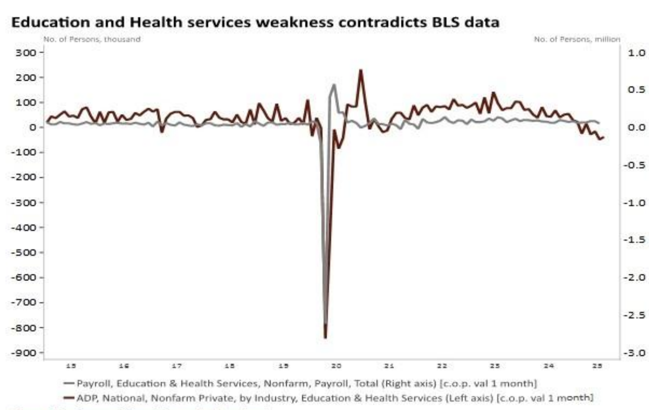


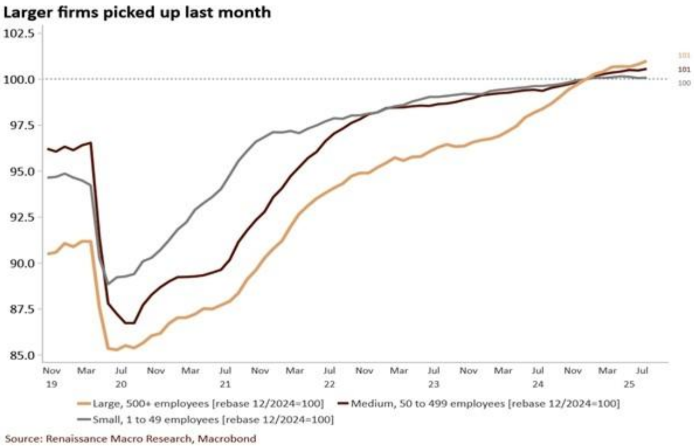
ADP: Disconnect is about education & health

- According to the latest ADP employment report, private payrolls advanced 104,000 in July following a contraction of 23,000 in June. This was slightly ahead of consensus expectations; however, I would not change any views around Friday’s employment data. The bigger story is that over the last three months, private payrolls have averaged gains of just 37,000 per month. That’s somewhat below the growth in the labor force even accounting for weaker immigration.



- An important source of the disconnect between ADP and BLS is in education & health services. In ADP, this industry fell another 38,000 in July, the fifth decline in six months. By contrast, the BLS has the industry adding roughly 75,000 per month on average over the last three months. That’s about a 100,000 swing.

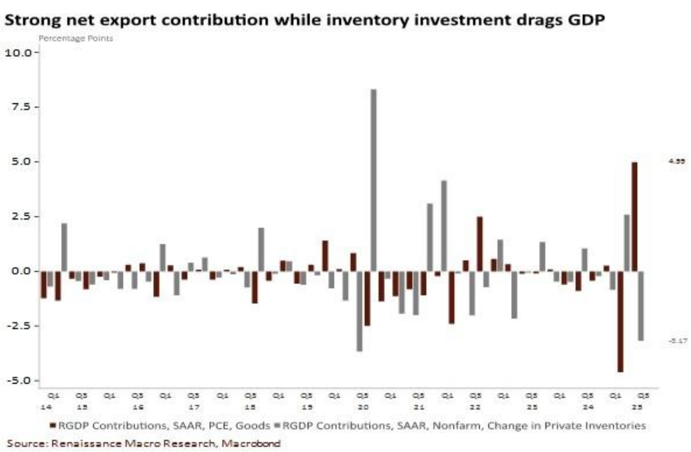




• By industry size, small firms continue to struggle. For firms with under 50 employees, payroll growth has declined 0.3 percent at an annual rate over the last three months. By contrast, large firms with at least 500 employees have seen payrolls rise at a 1.2 percent annual rate over this period

Q2 GDP was soft under the hood

- In Q2, real GDP advanced 3.0 percent following a 0.5 percent annualized decline in Q1. As we will show, there is quite a bit of noise due to imports. Average out the first two quarters and real GDP expanded 1.2 percent SAAR in H1. That's below the Fed's estimate of longer-run potential.

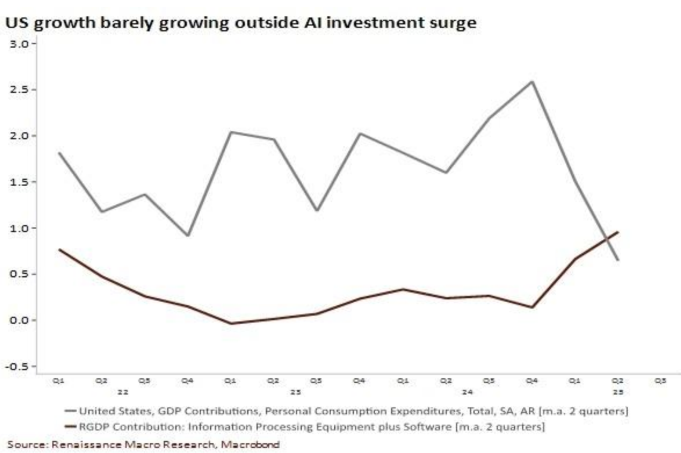


- With imports imploding in Q2, net exports added 5ppt to GDP growth. Inventory investment is the mirror image of the narrower trade deficit, cutting GDP by 3.2ppts. Removing these components, real final sales to domestic purchasers rose just 1.1 percent SAAR, the weakest since Q3 2022. Underlying growth momentum has clearly slowed and domestic demand tends to provide more useful information about where economic conditions are headed than GDP itself.

Looking through the details, three things stood out to me.

- First, real consumers' spending added 0.98ppt to GDP, but 0.35ppt of that was health care services, an acyclical category. Averaging out the first half, consumption excluding health care added just 0.3ppt to GDP growth. That is not good. It is difficult to articulate a bullish thesis for the consumer right now. First, wage growth continues to cool alongside a slowing jobs market. Second, home prices are slowing, and homes are the main asset on the household balance sheet. Third, tariffs are a consumption tax, the point will be to slow consumers' spending down. Fourth, AI investment is putting pressure on the US electrical grid, driving up the utility bills for households, another shock to disposable income.

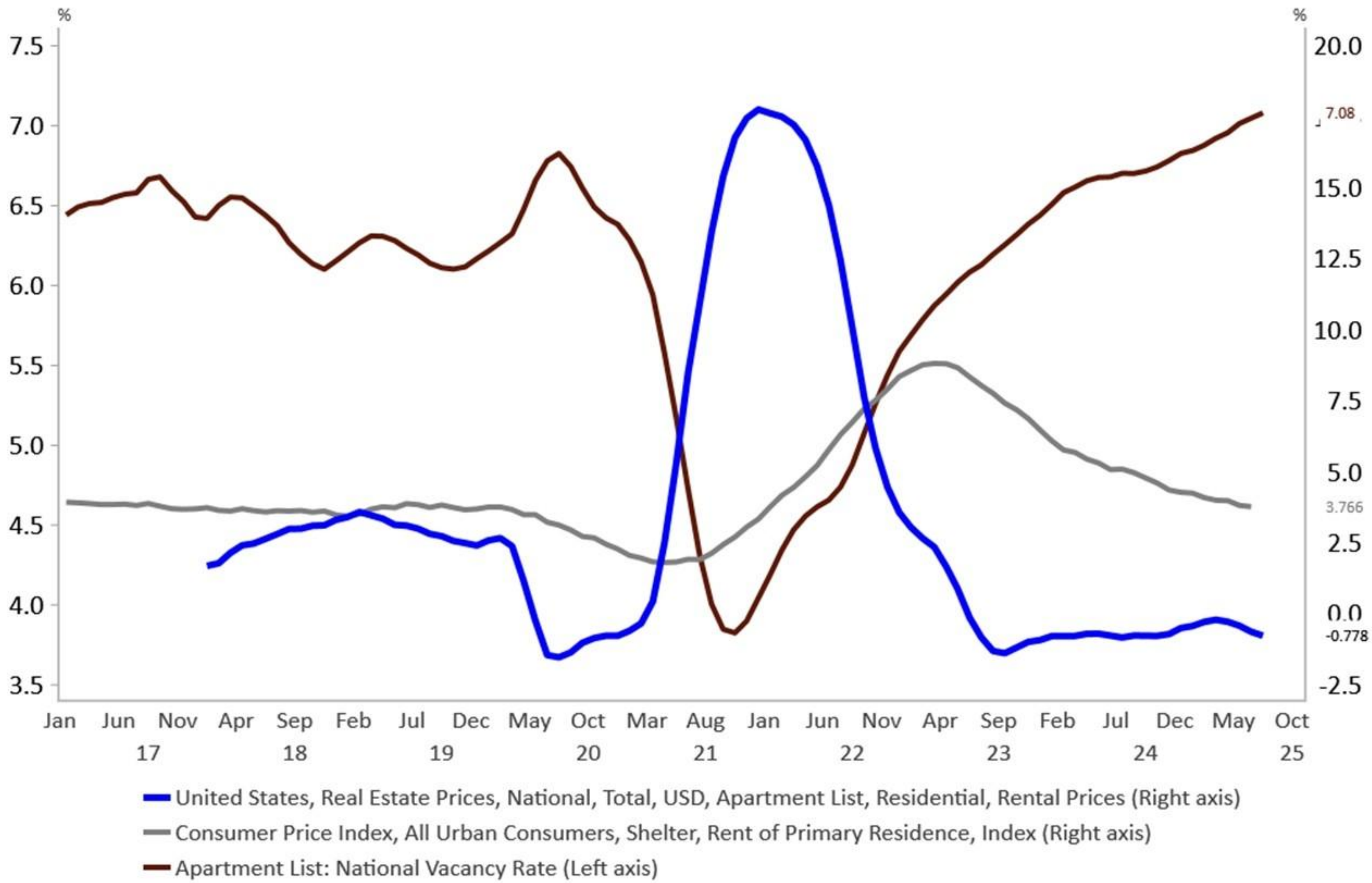
- Second, research and development spending continues to decline. In Q2, real private R&D investment fell 1.7 percent SAAR, the fourth decline in five quarters. It's rare to see R&D investment decline.



- Third, AI related tech continues to provide a tailwind to growth. Software and information processing equipment lifted GDP growth by 0.52ppt in Q2, averaging 1ppt to GDP growth in the first half. Put differently, the US economy is barely growing outside AI.

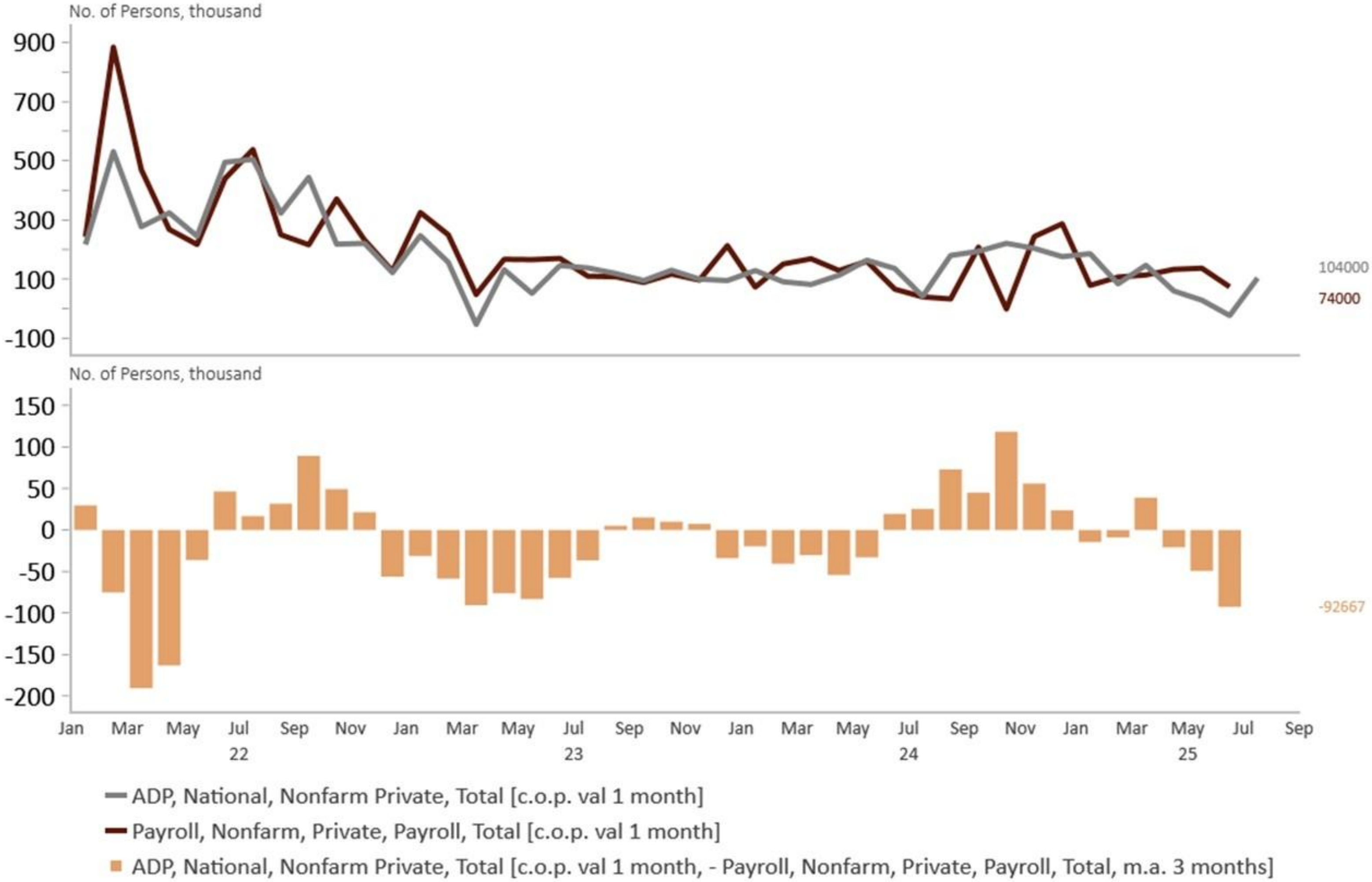
To review, the US economy is on thin ice. Longer-term interest rates have jumped following today's GDP data even though it was not a good report. If all of us are waiting around for a smoking gun in the economic data or evidence of non-linearity to emerge, then it creates the risk of a more abrupt shift in markets later.

Apartment vacancies continues to rise



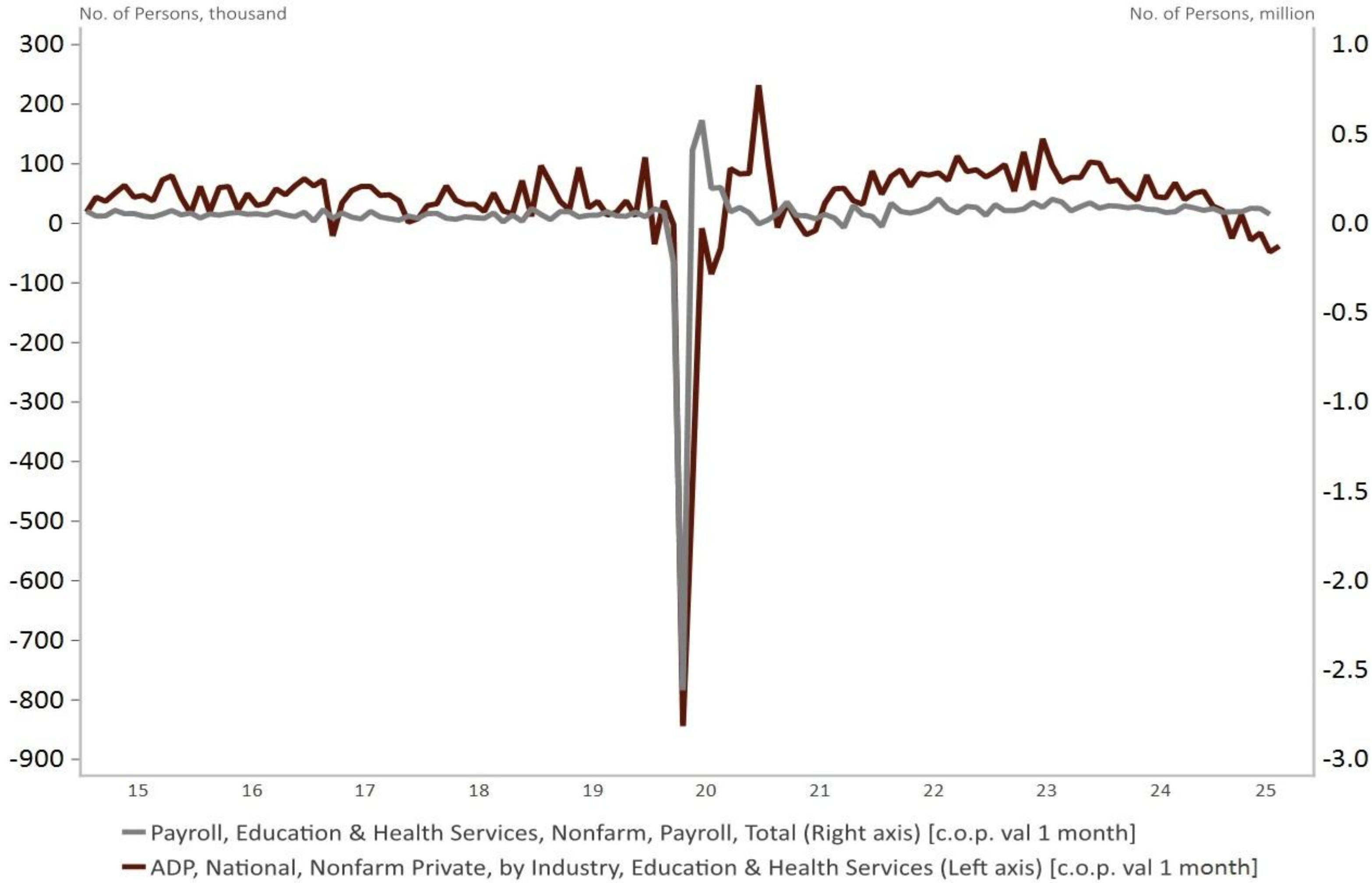
Source: Renaissance Macro Research, Macrobond

ADP has been running below BLS of late

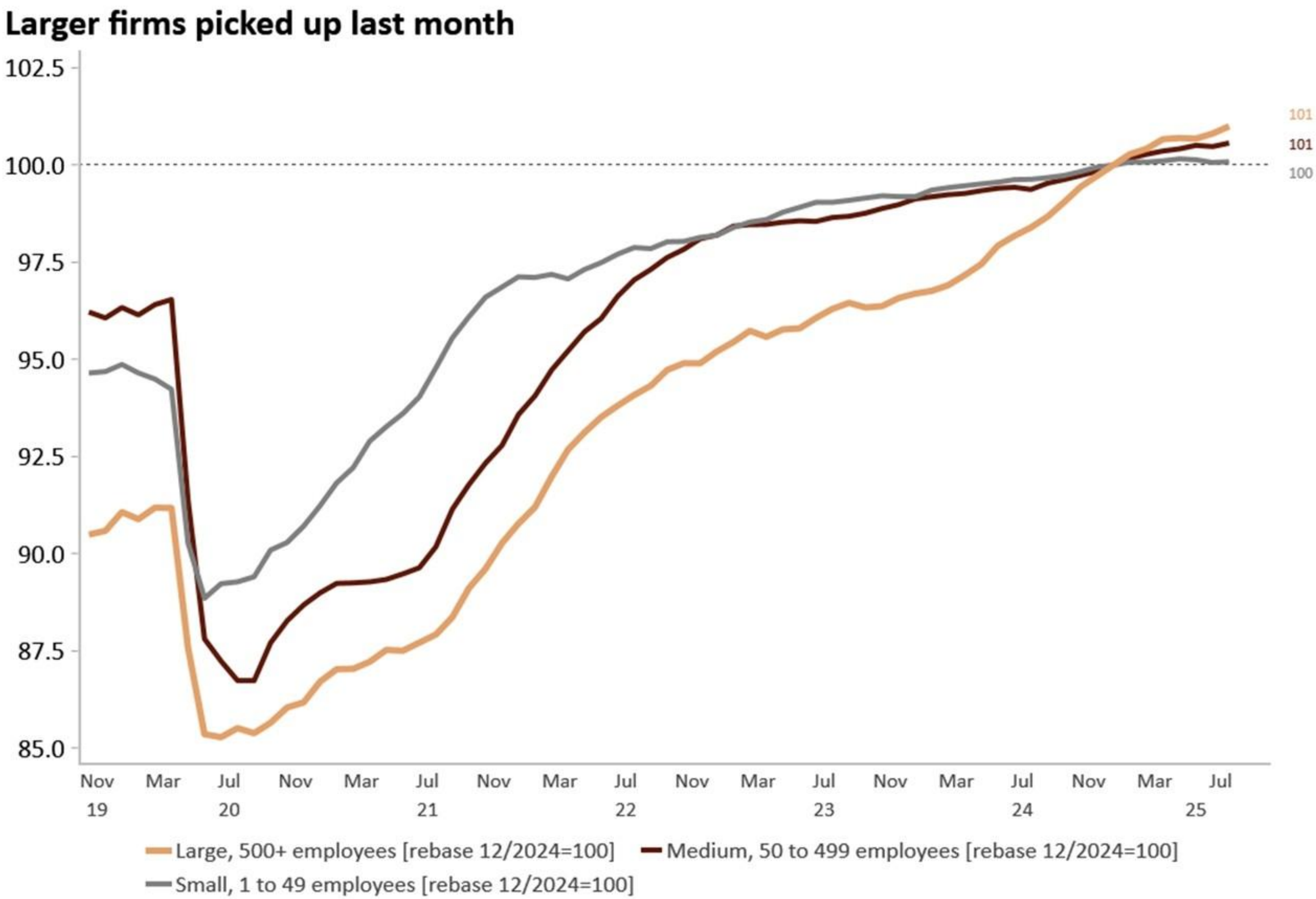


Source: Renaissance Macro Research, Macrobond

Education and Health services weakness contradicts BLS data

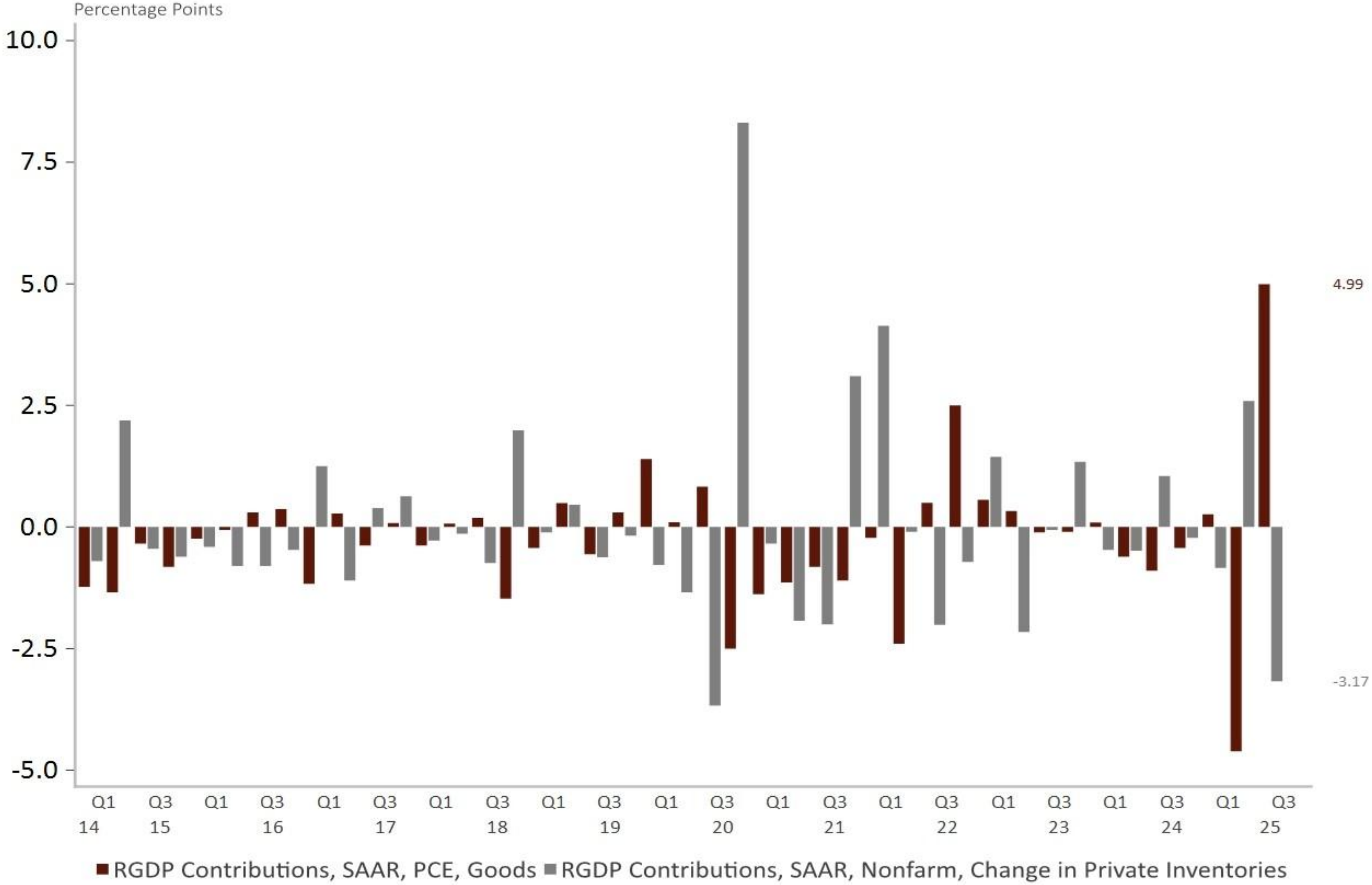


Source: Renaissance Macro Research, Macrobond



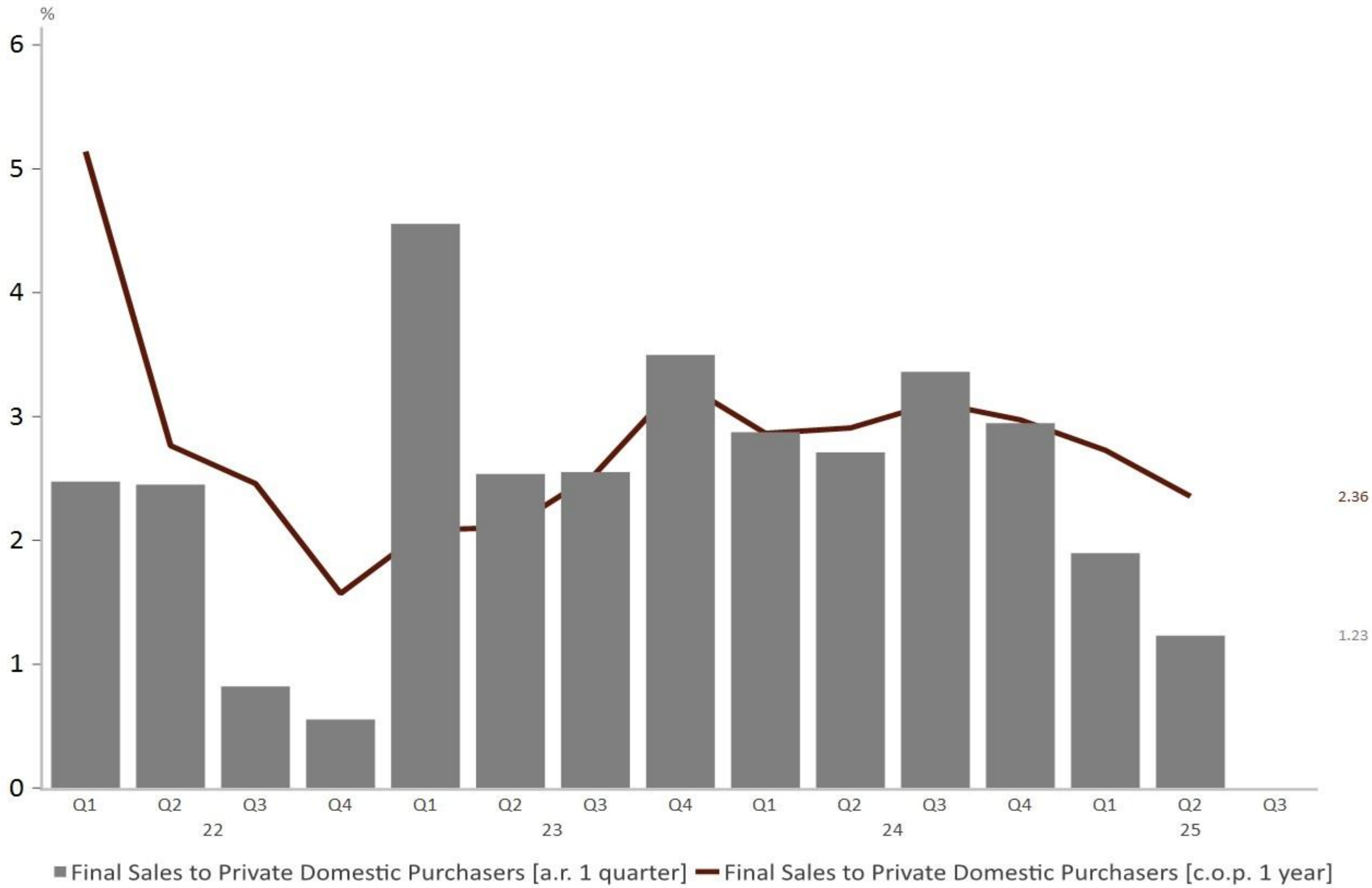
Source: Renaissance Macro Research, Macrobond

Strong net export contribution while inventory investment drags GDP



Source: Renaissance Macro Research, Macrobond

Private demand show weakest growth since 2022



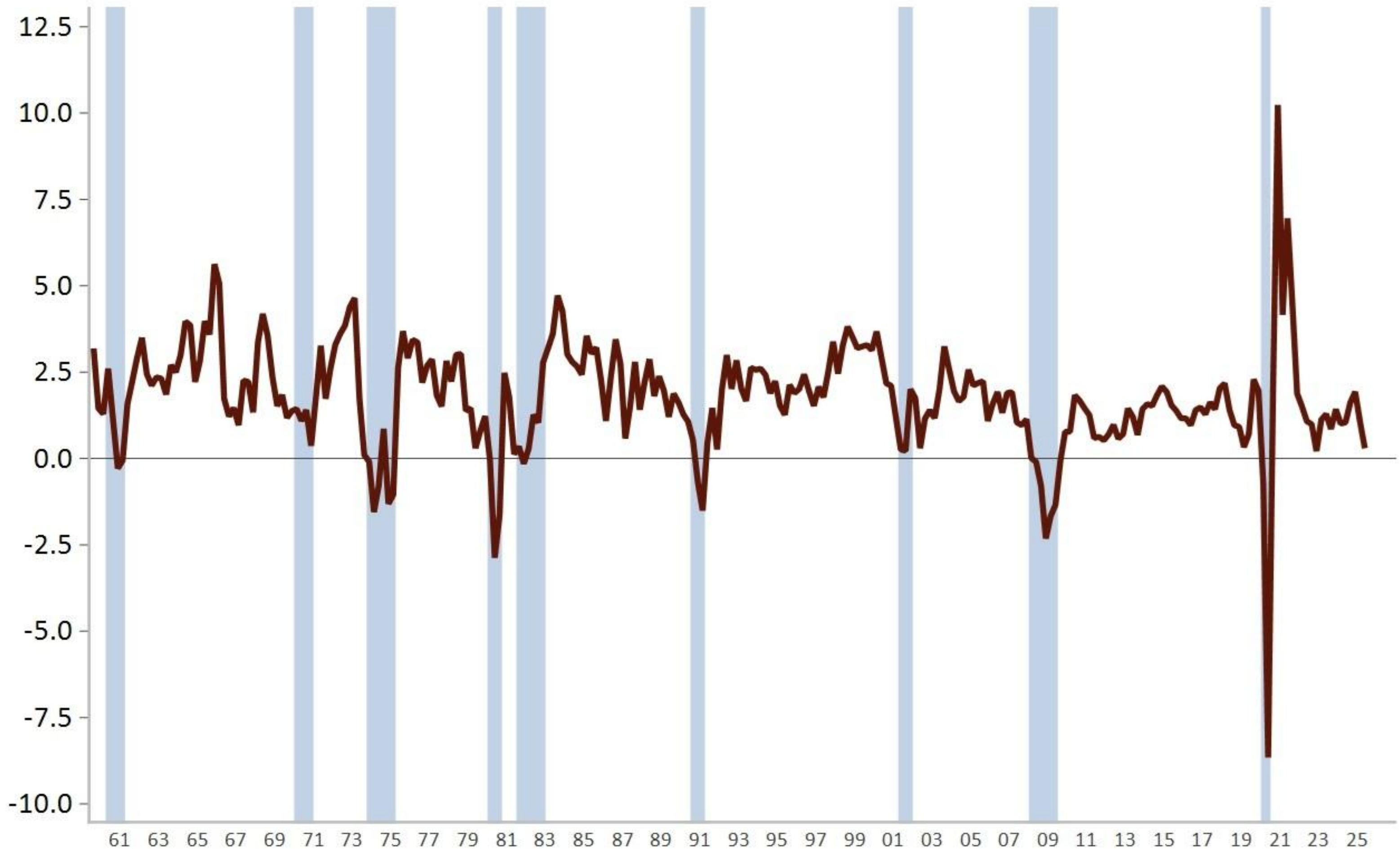
Source: Renaissance Macro Research, Macrobond

Component Ability to Forecast One-Quarter-Ahead Real GDP/Private NFP Growth

Component (Real)	Predictive Power (Adj. R^2) of GDP	Predictive Power (Adj. R^2) of Priv. NFP
Government	0.01	0.00
Exports	0.01	0.25
Inventories	-0.2	0.26
GDP	0.18	0.66
Final Sales of Domestic Product	0.23	0.65
Imports	0.29	0.50
Fixed Investment	0.29	0.69
Mean Output	0.27	0.66
PCE	0.36	0.58
GDI	0.31	0.60
Final Sales to Domestic Purchasers	0.37	0.64
Final Sales to Private Domestic Purchasers	**0.41**	**0.73**

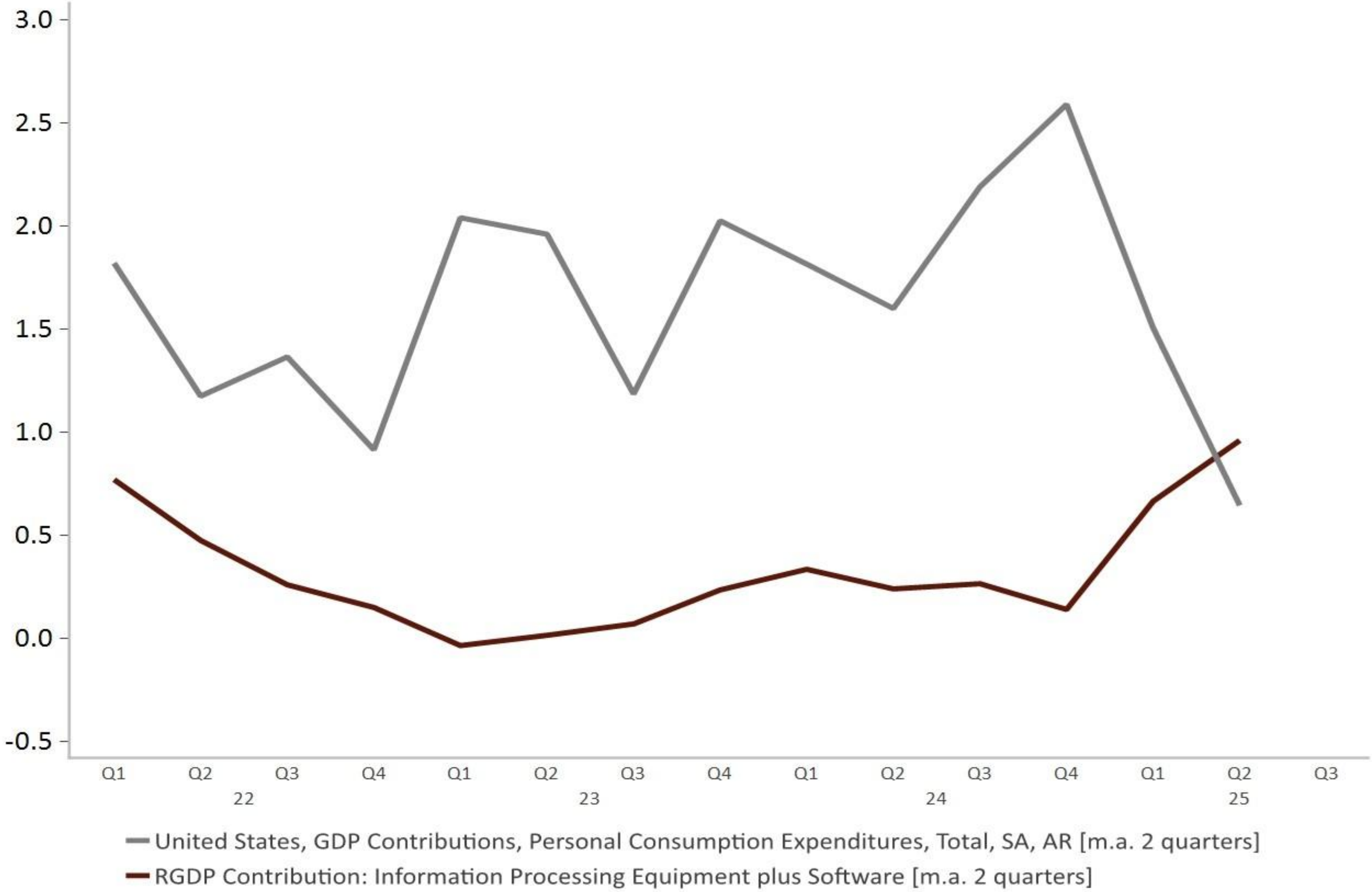
Note: Results are based on regressing 4-lags of the components on GDP/Private NFP using data between 1984-2016.

Consumer spending outside healthcare contributes weakly to first half growth



Source: Renaissance Macro Research, Macrobond

US growth barely growing outside AI investment surge



Source: Renaissance Macro Research, Macrobond