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A Canary in Someone Else's Coal Mine?

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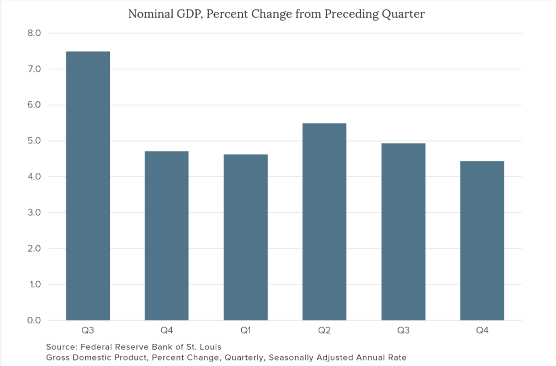
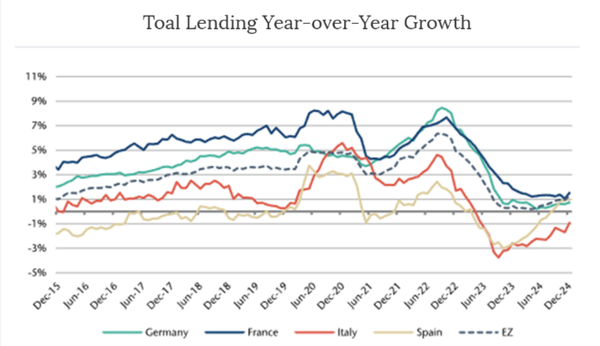
Our recent Perspectives piece pointed out that loan growth has been slowing in the U.S. Currently, loan demand is growing below nominal GDP, meaning our economy is experiencing some deleveraging. This could be a potential precursor of economic weakness and an indication that consumers and businesses are becoming cautious and, as a result, are taking on less debt. Loan demand, and the overall health of the banking system, is often a good real-time indicator of economic activity. Hence our title, implying that slack loan growth is a potential "canary in the coal mine," indicating softening in the economy.

We recently learned preliminary U.S. GDP figures for the fourth quarter of 2024, which indeed revealed a slowdown in economic activity. Real GDP grew at 2.3%, down from 3.1% in the third quarter. That said, this is still a healthy rate of expansion. Certainly it is not flashing any material signs of recession or economic weakness, at least at this point. Furthermore, the U.S. labor market remains robust, and consumer spending continues to support growth, reinforcing our view that the U.S. economy is resilient even in the face of global uncertainty.



Source: Federal Reserve Bank of St. Louis
Gross Domestic Product, Percent Change, Quarterly, Seasonally Adjusted Annual Rate

However, we do note that loan growth in Europe is particularly weak and has taken a step down in the final months of 2024. The chart below illustrates monthly loan demand trends in the major European countries.



Source: Jeffries

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This decline in loan demand could be related to potential U.S. tariffs and their impact on exports. It is also likely being influenced by recent political upheaval in Europe's leading economies, including ongoing government instability in France, uncertainty over Germany's energy policy, and challenges surrounding Italy's fiscal outlook. Additionally, mortgage demand remains low amid still-elevated borrowing costs, further straining European banks. The ECB (European Central Bank) has responded by lowering interest rates several times, most recently in late January. It is now anticipated that European rates will be declining more rapidly than in the U.S. as the ECB is expected to cut rates more aggressively than the Federal Reserve. This signals their concern over stagnation risks and is a result of the backdrop of economic weakness accompanied by the lack of loan demand.

In contrast, while the U.S. has experienced some moderation in loan demand, it is not nearly as severe as what is happening in Europe. U.S. banks remain well-capitalized, and financial conditions have not tightened to the same degree. Additionally, U.S. consumer and business confidence, while moderating, remains more stable relative to Europe, where geopolitical tensions, energy costs, and government dysfunction are exacerbating economic concerns.

This divergence underscores our bias toward U.S. markets and reinforces the concept of *American Exceptionalism*. We continue to believe the U.S. is the best place to invest due to its stronger economic fundamentals, more predictable monetary policy, and greater resilience in the face of global disruptions. This is evidenced by the dramatic outperformance of the U.S. stock market over the past 15 years. We continue to believe in the significance of both *American Exceptionalism* and *Dividend Exceptionalism*, and we will maintain our focus on these two longstanding principles as we make investment decisions on behalf of our clients.