

Special Commentary — July 19, 2024

Despite the Heat, the Animal Spirits are Cooling Off

Summary

- Our Animal Spirits Index (ASI) fell in June to 0.53 from 0.88 in May but has remained positive in all six months of 2024.
- Most components were subtractive in June, with the only strength tied to indicators reflecting the stock market.
- Though a positive reading, it sits below the year-to-date average of 0.75 and is the lowest index value seen since November of last year, reflecting the recent deceleration seen in the U.S economy.

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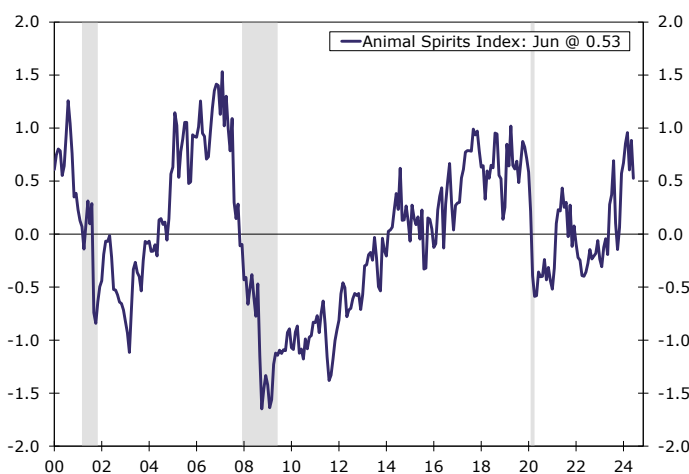
Stormy Spirits Ahead?

Our Animal Spirits Index (ASI) fell in June to 0.53 from 0.88 in May but has remained positive in all six months of 2024 ([chart](#)). Previous reports detail the index's methodology, but on a basic level, an index value above zero indicates optimism and a value below zero suggests pessimism.¹ Though June's reading remains positive, it sits below the year-to-date average of 0.75 and is the lowest index value seen since November of last year.

The ASI consists of five indicators: the S&P 500 Index, the Conference Board's Consumer Confidence Index, the yield curve (the spread between the 10-year and three-month Treasury yields), the VIX Index and the Economic Policy Uncertainty Index. The policy uncertainty and VIX indices inversely affect the ASI. In other words, a rise in uncertainty or volatility decreases the index, while a fall increases the index, all else equal.

Most components were subtractive in June, with the only strength tied to the indicators reflecting the stock market. The S&P 500 Index reached another record high, and rose roughly 183 points over the month. Year-to-date, the index is up 13% and has contributed positively to the ASI for five out of the six months of 2024. Stock market volatility remained roughly the same from May to June, falling slightly to 12.44 from 12.92 previously. In the bond market, the yield spread on the 10-year and 3-month Treasuries widened to -94 bps from -77 bps in May. The yield curve has been inverted since November 2022 and continues to weigh heavily on the ASI.

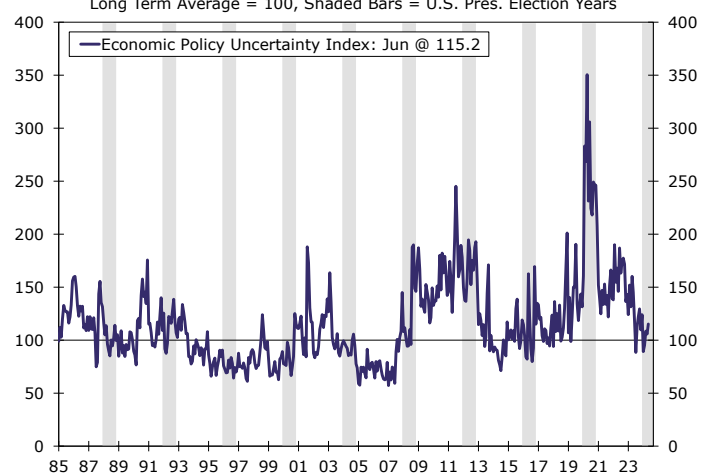
Animal Spirits Index



Source: Wells Fargo Economics

U.S. Economic Policy Uncertainty Index

Long Term Average = 100, Shaded Bars = U.S. Pres. Election Years



Source: Baker, Bloom & Davis and Wells Fargo Economics

The Consumer Confidence Index fell slightly in June to 100.4 from 101.3 in May. However, it is down roughly 10% from the start of 2024 and has decreased in all but one month of this year. As we wrote in a recent [special report](#), in past presidential election years, the Consumer Confidence Index tends to come in a bit soft in the months before an election. This creates scope for the index to continue to weigh on animal spirits through the end of this year. Also poised to contribute negatively to the ASI this election year is the Economic Policy Uncertainty Index. The index rose over nine points to 115 in June and has remained above the long-term average of 100 for most of this year. As seen in the [chart](#) above, the Economic Policy Uncertainty Index has historically risen ahead of presidential elections, leaving opportunity for the index to increase further as November approaches.

The ASI has remained in positive territory for eight consecutive months but has been trending downward since reaching a post-pandemic high in March. This aligns with the recent deceleration in the U.S. economy. As outlined in our latest [U.S. Economic Outlook](#), real GDP rose only 1.4% in the first quarter of this year after growing at an annualized rate of 3.4% in Q4-2023. Payroll growth has also slowed in recent months, and the unemployment rate has trended higher. We look for the FOMC to cut the fed funds rate by 25 bps at its September 18 meeting, followed by another 25 bps rate cut at its December meeting and an additional 100 bps of easing in 2025. Until then, softening economic activity and increased political uncertainty may create volatility for the ASI in the near future.

Endnote

1 – Please see [The Roar of the Animal Spirits: A New Index](#) and [Finding Neverland: What Drives Animal Spirits?](#) (January 2018). ([Return](#))

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