



OXFORD  
ECONOMICS

# MAIN STREET REPORT

Your window into small business health

Q4 2023



## Resilience and consumer confidence spell growth



### Executive summary

North American economic strength is riding on the backs of the resilient U.S. Consumer. For the past two years, the fear of an imminent recession rang in the ears of economists and consumers alike, radiating declining confidence in growth and the ability to prolong spending behaviors consumers grew accustomed to during pandemic recovery. Those fears have been pushed aside as consumers beat holiday spending expectations, upending retailers' anxiety entering the season. This unexpected cash flow helped small businesses pay down their outstanding debt and begin to look seriously at capital expenditures and future growth planning for 2024. Headwinds remain high with inflation exceeding expectations, lenders constraining exposure through underwriting, and a hesitation brought on by market noise. Not to say we are out of the woods. The FOMO felt by small businesses is growing as the anticipation of the start of growth rests in the Federal Reserve's start to quantitative loosening. The longer they wait, the fewer opportunities they may present. The past macroeconomic president suggests the market will slow. What is different in 2024 is that the labor force is still strong, and consumer spending is supporting businesses keeping their doors open.

The U.S. economy is poised to grow but is waiting on the Federal Reserve to signal they are clear to fully engage.

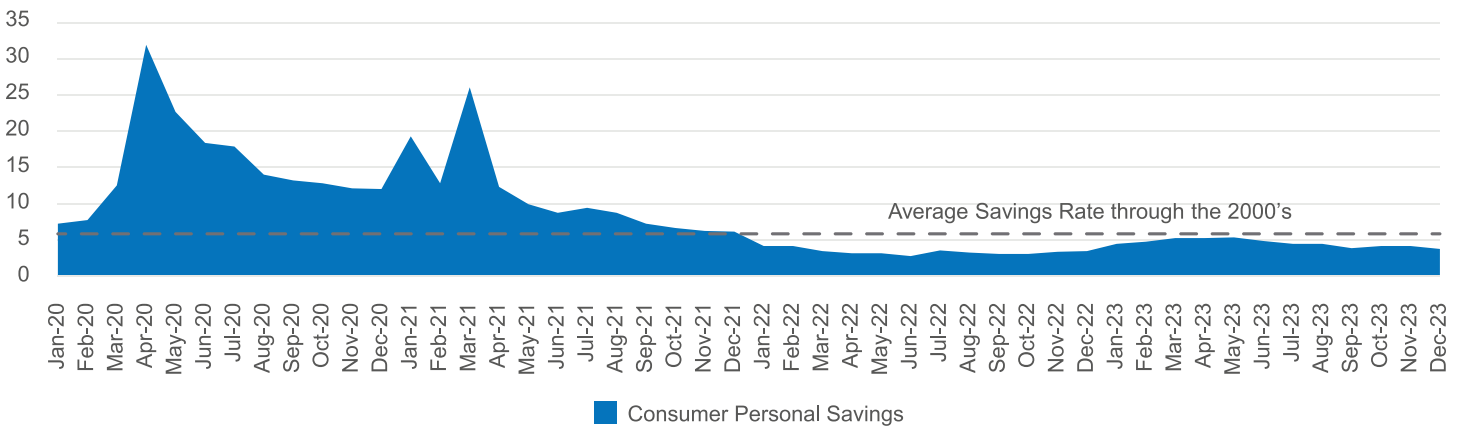
# Macroeconomic overview

The U.S. economy is chugging along, and the economic outlook continues to brighten because of the labor market's resilience, loosening financial conditions, solid household and nonfinancial corporate balance sheets, and continued progress on disinflation. Oxford Economics expects the macroeconomic backdrop for small businesses to remain solid in 2024, with U.S. GDP growth forecast to be 2.3% in 2024, which is close to growth in 2023 and the economy's trend growth rate. The peak drag from tighter monetary policy and more restrictive lending conditions is now behind us, fiscal policy no longer looks set to be such a significant drag, and the outlook for consumer spending is still bright.

The economy expanded at a 3.3% annualized pace in Q4, driven mostly by continued strong consumption growth. Consumers' real disposable incomes are still growing at a decent pace as the job market remains strong, wage growth is elevated, and inflation is declining. The spending strength has also been supported by households reducing their savings, with the personal saving rate close to historic lows.

The low level of saving is one reason to expect consumers — the driving force of the U.S. economy — to slow their spending over the coming years.

## U.S. Consumer savings rate

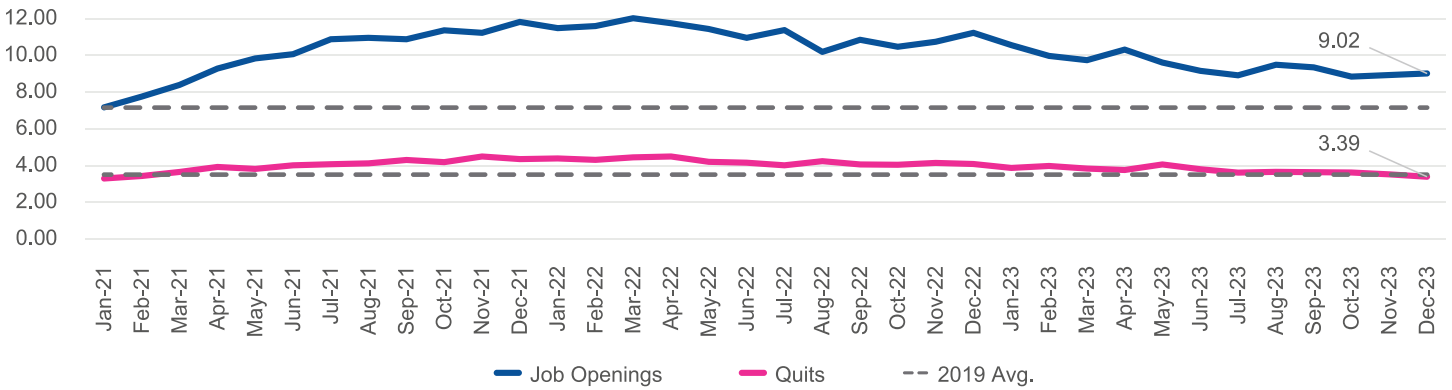


Source: U.S. Bureau of Economic Analysis

According to an analysis by Oxford Economics, the spending down of excess savings left over from the pandemic has now largely run its course. Those funds have now largely been spent, or the cash has been invested elsewhere.

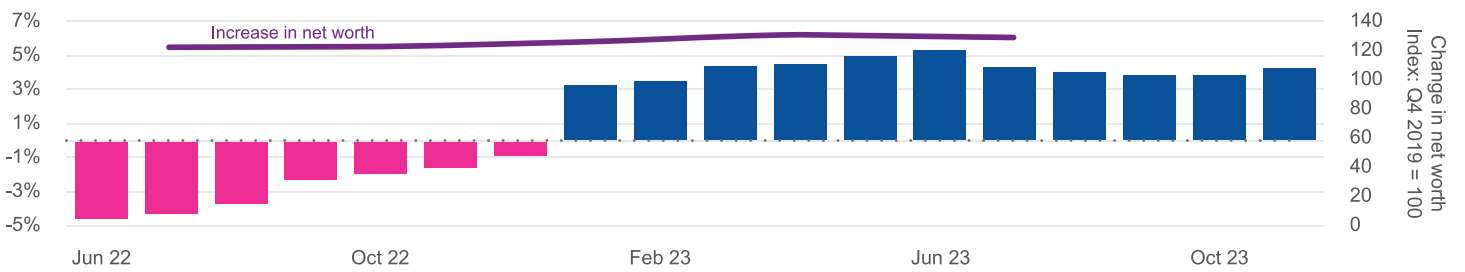
However, there does not appear to be a greater risk that consumers tighten their purse strings significantly. Consumer spending will be supported by wealth effects, strong job growth, solid growth in real disposable income, and past declines in gasoline prices.

## U.S. Labor market cooling



Source: U.S. Bureau of Economic Analysis

## Disposable income

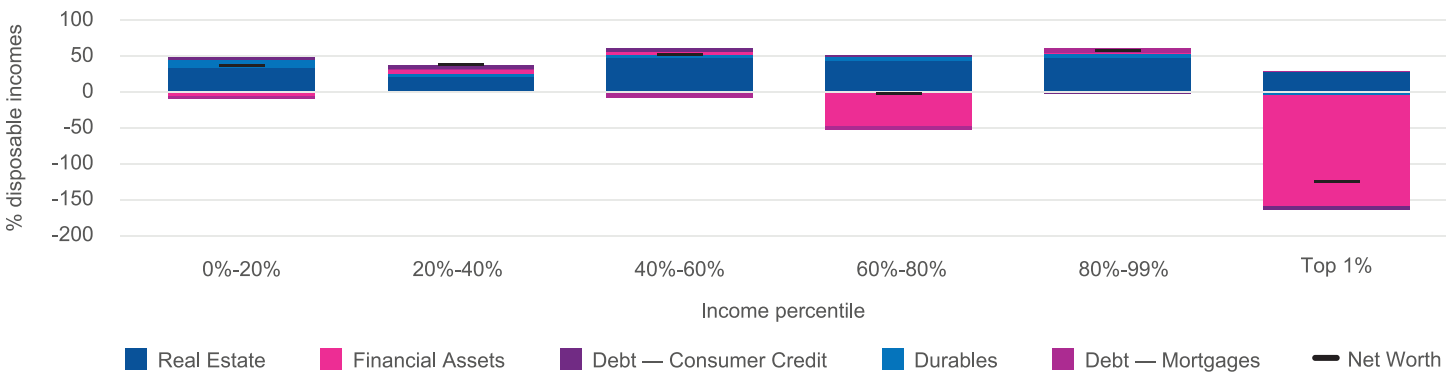


Source: U.S. Census Bureau

## Fuel and energy prices

Households came into the pandemic with solid balance sheets and low levels of debt, and the burden of servicing that debt has remained low because much of it is financed at fixed interest rates. Moreover, the surge in house prices since the beginning of the pandemic has lifted household's net worth significantly, and those gains have been shared by Americans at every income level, not just those at the top. That will help limit the rise in consumer delinquencies, which Experian data show rose slower in the fourth quarter.

## U.S.: Change in net worth by income level Q4 2019 to Q3 2023



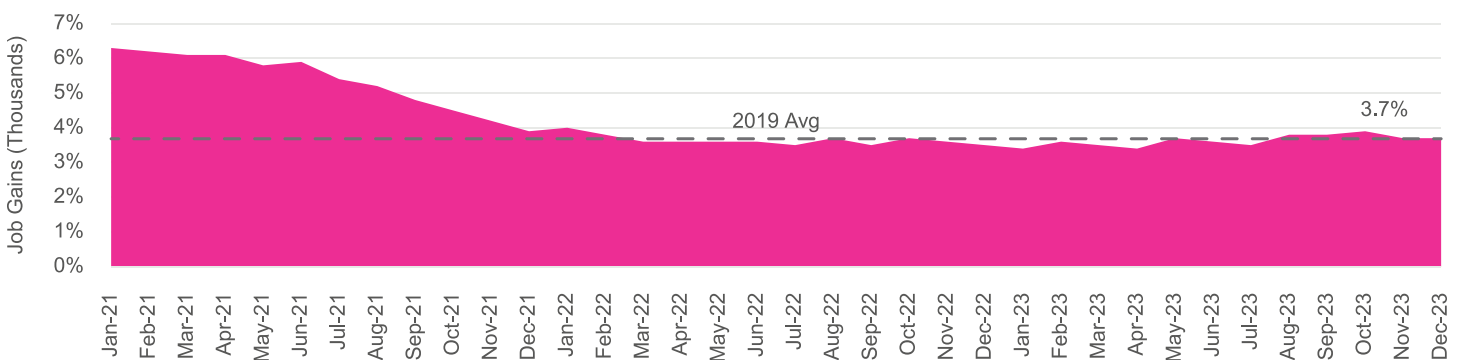
Source: Oxford Economics/Haver Analytics

Continued solid growth in consumer spending is the foundation for a brighter outlook for small businesses' sales and earnings. Other parts of the economy still need to hold up, but prospects appear better than they did three months ago. Higher borrowing costs and tighter credit availability still weigh directly on firms' investment plans, but Oxford Economics believes the peak drag is now behind us. In addition, there is the prospect of the bipartisan tax package working its way through Congress, which would extend business tax breaks and could boost the prospects for investment this year.

Oxford Economics anticipates that the improved economic backdrop and the shift towards easier financing conditions will keep the rise in corporate delinquencies muted and limit the normalization of bankruptcies over the coming year, in line with the latest trends shown by Experian data.

We expect the labor market conditions to ease but remain solid. We expect net job growth to slow and the unemployment rate to drift higher to just over 4% in 2024 from its current rate of 3.7%.

## Unemployment rate



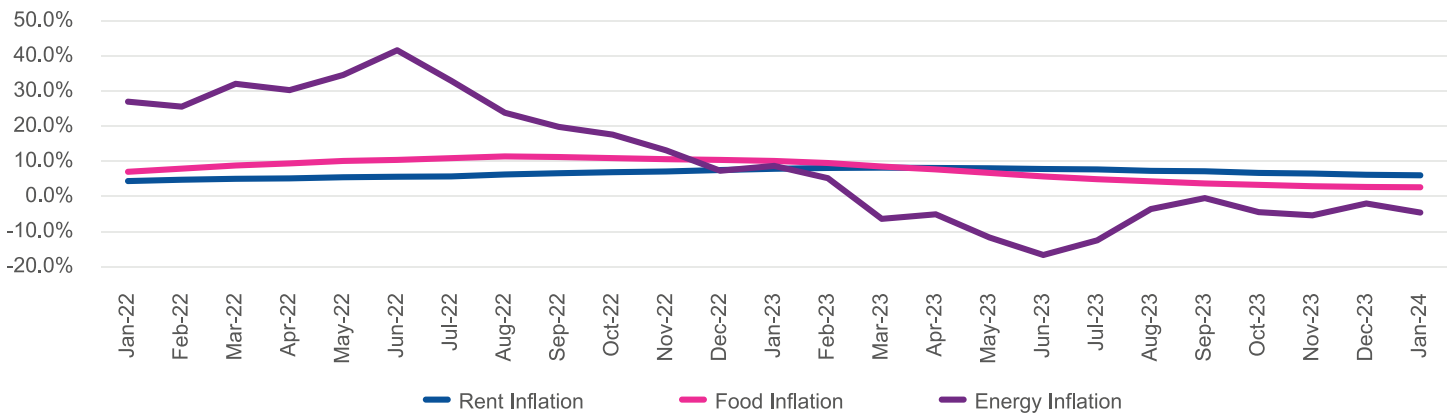
Source: U.S. Bureau of Economic Analysis

For businesses, this is likely to be close to a Goldilocks scenario — labor market conditions will remain solid enough not to undermine overall economic demand. Still, it will help ease the perennial labor shortages of the past few years, making workers easier to find for those expanding businesses. Looser labor market conditions are still feeding through to cooler wage growth, reducing pressures on firms' cost bases.

Inflation has been easing faster than expected over the past few months, helped by lower prices for goods and slowing wage growth, contributing to weaker inflation in the services sector.



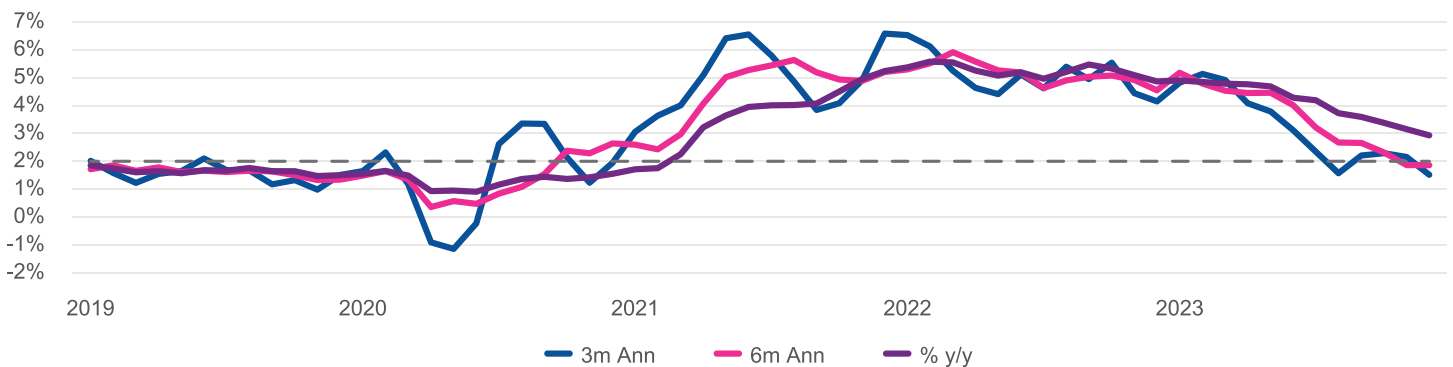
## Tangible Inflation trends



Source: Bureau of Labor Statistics

Oxford Economics forecasts that inflation will fall close to the Fed's 2% inflation target later before the end of 2024 as rental inflation cools and wage growth falls to rates more consistent with 2% inflation.

## U.S.: Core PCE deflator



Source: Oxford Economics/Haver Analytics

The Fed will not wait until inflation has fallen to its target before cutting interest rates. Still, Oxford Economics expects the coming rate-cutting cycle to be gradual by historical standards. The backdrop of a resilient economy and the fact that the Fed is approaching the inflation target from above rather than below adds to the case for caution. Oxford Economics expects the first rate cut to come in May, with rate cuts following at one per quarter.

The risks to the outlook appear balanced. On the upside, inflation could decline more rapidly, and the Fed could begin easing sooner, which Oxford Economics expects would trigger a faster turnaround in growth prospects in the second half of the year, as activity in rate-sensitive sectors of the economy like autos, business equipment, and residential investment improve.

On the downside, the economy's resilience could trigger a revival in inflationary pressures, which cause the Fed to keep interest rates higher for longer. That would increase the economic risks from the financial sector, mainly commercial real estate, which could spill back to weaker demand in the rest of the economy.

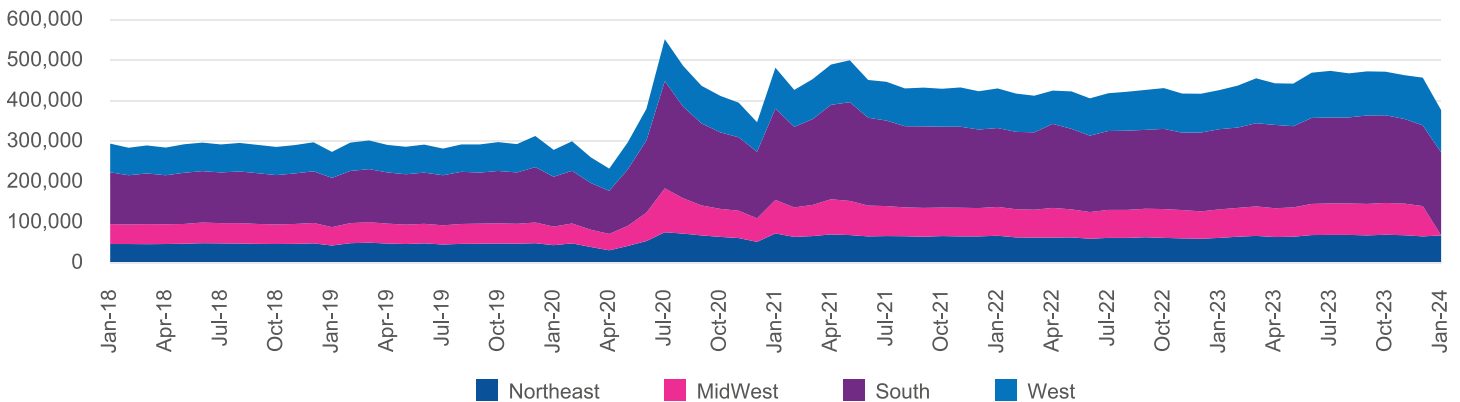
Geopolitical risks, including disruption in global shipping lanes, appear limited for now but could loom larger if conflicts were to broaden and disrupt global energy supplies or cause broader disruption.



## U.S. Business

The entrepreneurial spark that powers innovation in the U.S. has not slowed. New business applications continue to outpace pre-pandemic levels. They are building the foundation of businesses preparing to expand as the country comes out of a period of self-induced quantitative tightening activity by the Federal Reserve.

### Small business starts



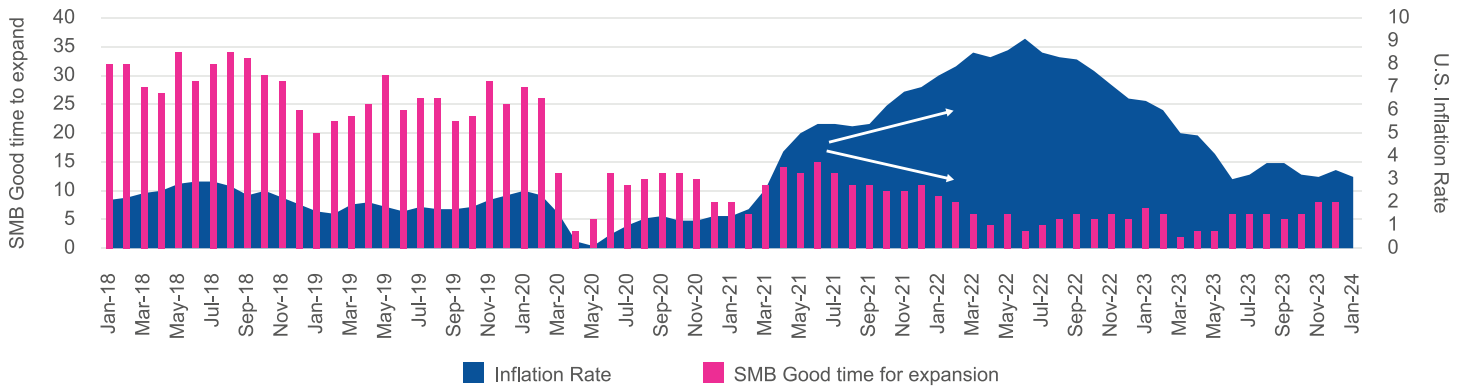
Source: U.S. Census Bureau

Small businesses are vital to the U.S. economy, serving as a wellspring of innovation, employment, and economic resilience. These small enterprises employ 47.1% of the private workforce, as per the Small Business Administration (SBA), underscoring their critical role in U.S. job creation. They contribute 44%, a substantial portion, of the U.S. Gross Domestic Product (GDP). Beyond economic metrics, small businesses are pivotal in fostering diversity. They provide opportunities for all segments of society, including minorities and women, to innovate and thrive. Following the pandemic, the resilience of small businesses has been notable, with improved survival rates indicating their adaptability and importance in economic recovery. The survival rate of small businesses varies over time, but recent data provides a clear picture. According to the U.S. Bureau of Labor Statistics, the survival rates for establishments indicate that about 80% survive the first year, 70% survive the second year, about 60% survive the third year, and around 50% make it through the fifth year. These rates gradually decline, highlighting small businesses' challenges in maintaining longevity. The survival and growth of small businesses are crucial for sustaining the American economy's vibrancy, highlighting the need for continued support and recognition of their value.

The number of business applications was down across most regions in January 2024 after closing the year strong in December, above 400k a month. Small businesses struggle to grow in an environment with high funding rates, anxious investors, and tightening lending standards.



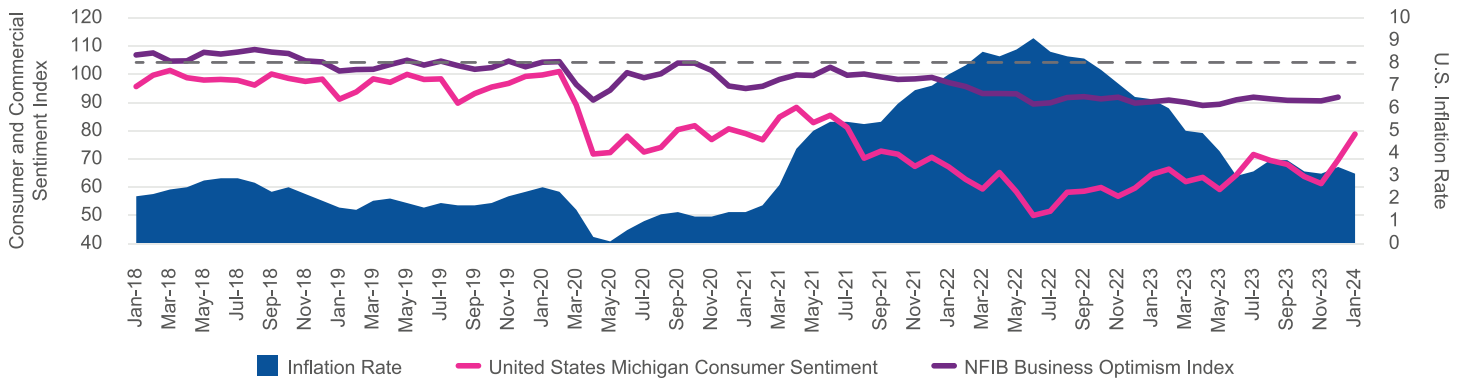
## Outlook for expansion: Percent next three months — “Good time to expand” (Seasonally adjusted)



Source: NFIB and U.S. Bureau of Labor Statistics

The consumer is leading sentiment as they see their behavior of spending through adversity, driving steady cashflows for businesses. Small business sentiment will be a fast follower as they see resilient consumer spending support growth even if funds are priced higher than expectations.

## Consumer and commercial sentiment overlayed by inflation



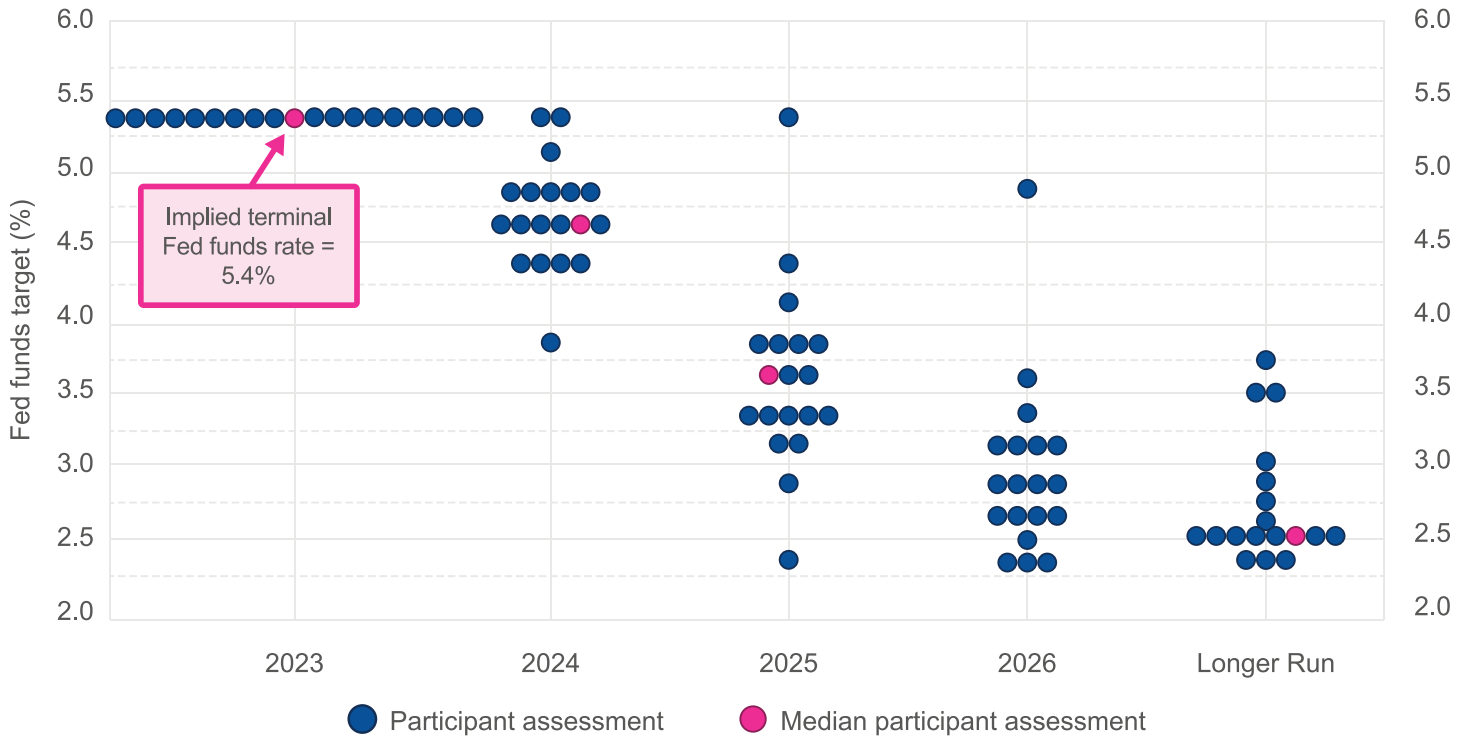
Source: National Federation of Independent Business, University of Michigan, U.S. Bureau of Labor Statistics

Retailers will feel consumers’ budget-minded shopping trends as they downsize brands into more affordable products and may spend less each time they visit the store. Companies like Target and Walmart are betting consumers are spending less per trip but making more frequent trips. Holiday shopping in 2023 highlighted a consumer’s willingness to spend even as cash flow ran lean and savings declined. Utilization rates are increasing across all income segments as consumers leverage more. The debt levels are manageable, and consumers and small business owners are managing. The increase in utilization places more customers at risk of dropping out of the most advantageous offer tiers as their credit risk increases when utilization crosses 33% for unsecured debt. Lenders are watching this trend carefully and building alternative products to keep falling consumers engaged and profitable.

The Federal Reserve will evaluate the right time to lower the federal funds rate and begin allowing the economy to accelerate growth.



## December 2023 FOMC participants' assessment of the appropriate Fed funds target rate at the end of 2023, 2024, 2025, 2026 and in the longer run

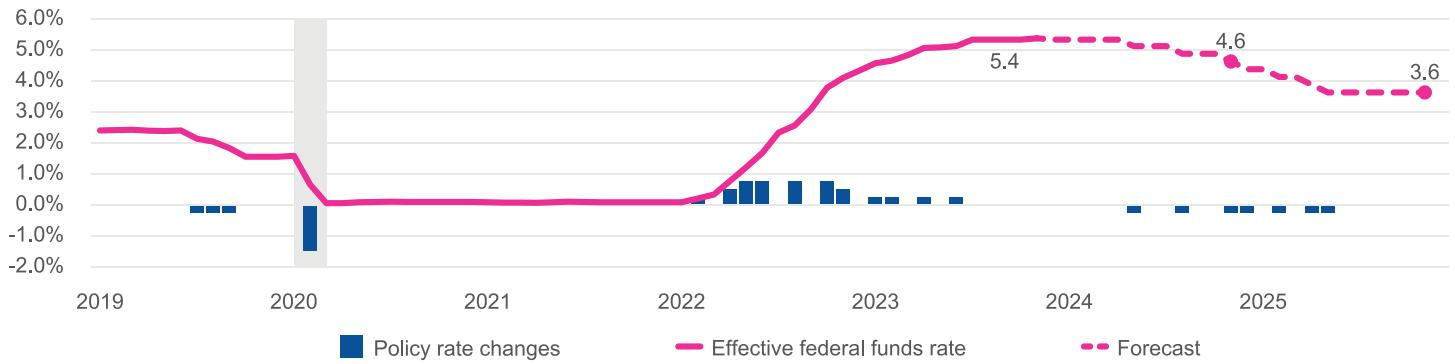


Source: Federal Reserve, Summary of Economic Projections (SEP), December 13, 2023, [realeconomy.rsmus.com](https://real.economy.rsmus.com)

More are leaning towards a rate reduction later in mid-summer.

The market has been building anticipation for rate cuts in the first quarter, however; there is an outside risk of delayed cuts and even the possibility of a rate increase if the economy reheats too quickly. This risk is low because all indicators point to the counter.

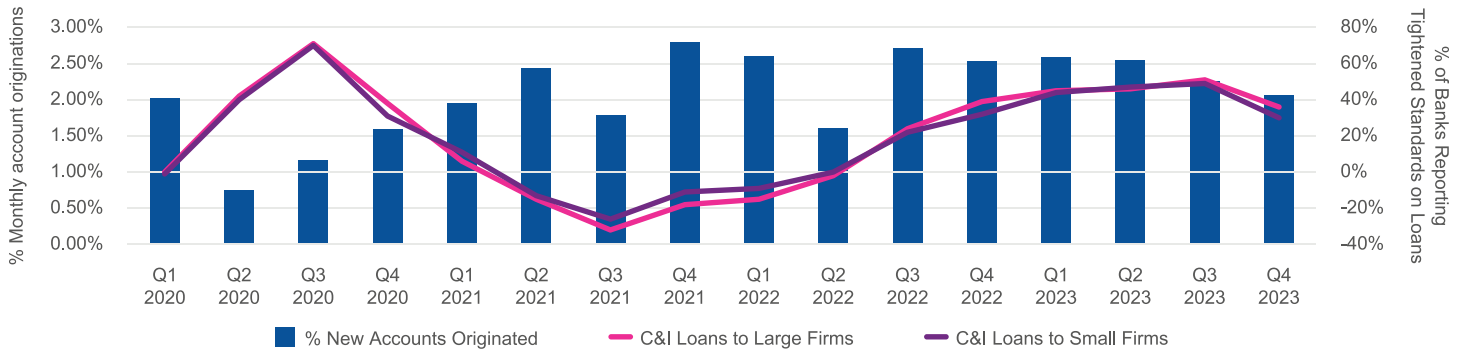
## Fed expectations on rate cuts



Source: Federal Reserve Board of Governors

This will be welcome news to the millions of small businesses that started or grew during high inflation and are now ready to refinance debt acquired by need. Small businesses with 1-4 employees rely on small business commercial credit cards for cheap and available credit. In the third quarter, this type of credit became significantly more expensive as commercial card lenders began raising APRs to limit exposure on current lines, increasing from 5% on average to 29% plus. Owners thought twice about the types of products they used to fill gaps in cash flow as lines of credit and term-style loans with lower rates became more attractive options.

## Commercial card originations overlayed with tightening trend



Source: Experian Commercial Benchmarking

The Federal Reserve will be challenged to make the right call as the U.S. Labor market remains strong, wages rise, and consumers continue to spend. Their target is 2% nominal, but the environment may force the new norm around 3%. The last few points will be the hardest for the Federal Reserve.

Global growth will slow as markets in the E.U. and Asia continue to slow. Conflicts will impact supply chain capacity, impacting goods and energy availability to producers.

## Expectations

In the first quarter of 2024, corporate earnings showed mixed results across various sectors. Companies like Apple and NVIDIA reported solid financial performances, with Apple announcing revenue of \$96.7 billion and NVIDIA experiencing a 19% revenue increase from the previous quarter. On the other hand, alternative segment corporations faced challenges, such as Home Depot, which saw five quarters of revenue decline due to consumers pulling back on home improvement projects as high-interest rates slowed new building activity. The market will see diverse financial outcomes across industry segments, reflecting the complex economic landscape businesses navigated during this period.

In Q4 2023, retail sales showed robust growth, with Amazon reporting a 14% increase to \$170 billion. However, as 2024 began, U.S. retail and food services sales in January dipped by 0.8% from the previous month, signaling a cautious start to the year amidst varying economic conditions.

Closing out 2023 and entering the first quarter of 2024, the logistics and transportation industry experienced mixed performance amid ongoing global economic uncertainties. Innovations like GenAI are reshaping the sector, enhancing supply chain visibility, and improving efficiency. A.I. is anticipated to boost logistics productivity by over 20% by 2035, affecting various aspects like predictive forecasting and smarter inventory management. The industry faces challenges such as a mixed global macroeconomic outlook with lower GDP growth compared to 2023, though real exports are expected to grow. The transportation sector is undergoing significant shifts, including nearshoring efforts and technological advancements in material science and engineering, creating new opportunities and competitive dynamics.

In 2024, the real estate industry faces significant challenges across residential and commercial sectors. Key issues include high-interest rates, a tight labor market, and shifting migration patterns. Commercial real estate is grappling with the uncertainty of office space demand due to hybrid work models, alongside robust performance in multifamily and neighborhood retail but softening in industrial sectors. Labor shortages persist, impacting construction and operational efficiency, while migration trends reshape demand across regions. Additionally, the industry is navigating a complex regulatory landscape, technological evolution, and the need for sustainability compliance. These challenges require strategic realignment and innovation to ensure resilience and growth.

The U.S. economy is strong because of the resiliency of the U.S. Consumer. Consumer balance sheets are stable, and repayment behavior is normalizing for the market. Higher costs, tightening of credit availability, and a cooling job market will place downward pressure on wage growth and limit their purchasing power. Small business confidence is improving, creating upward pressure on businesses' growth and capital spending activities as they transition from survival activities into growth mode.

The Federal Reserve will roll back Federal Funds Rates later in the year, giving consumers and small businesses the green light to invest and grow. Small businesses will refinance prohibitive cost funds and use the savings to expand. The U.S. Economy is pushing past the anxiety of a potential recession and preparing to push off into a season of growth. I will watch the caution flags as they present over the next quarter. The U.S. closed out 2023 strong and is driving to keep the momentum going.





# MAIN STREET REPORT

## About the report

The *Experian/Oxford Economics' Main Street Report* brings deep insight into the overall financial well-being of the small-business landscape, as well as providing commentary around what specific trends mean for credit grantors and the small-business community. Critical factors in the *Main Street Report* include a combination of business credit data (credit balances, delinquency rates, utilization rates, etc.) and macroeconomic information (employment rates, income, retail sales, industrial production, etc.).

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