CLOSE TO INFLATION PEAK?

Following a second contraction in its GDP in Q2, the outlook for the US economy is at least uncertain. Inflationary pressures are showing signs of easing, but the pace of disinflation could be longer than expected. While consumer confidence recently paused its downward trend and in fact recovered slightly in August, business surveys show a sharp decline in sentiment, particularly in the manufacturing sector. The Federal Reserve has continued the rapid rise in its fed funds rates, which are now at restrictive levels.

GDP fell again in Q2 (-0.9% on an annualised quarterly basis after -1.4% in Q1), mainly due to the drop in private investment and a smaller inventory. Based on our forecasts, the mechanistic upturn in growth in Q3 may continue over several quarters, but at a relatively slow pace. On the inflation side, several indicators suggest a potential slowdown in inflation from mid-2022 (fall in the energy and input prices, slowdown in the price of goods, fewer tensions on the labour market) but there is still a significant amount of uncertainty. And even if this fall in inflation materialises in the coming months, which is the most likely scenario, it is likely to stay above the 2% target until 2024. Having propelled its key rates into restrictive territory (3.00% - 3.25%) with a rise of 75 basis points in September, the Fed is expected to continue its restrictive policy until the end of the year.

Inflation, as measured by the Consumer Price Index (CPI), stood at 8.3% y/y in August, a very high level but down compared to July (8.5% y/y). This reduction is mainly the result of the recent drop in the price of crude oil, partly offset by the sharp increase in food prices. And while total inflation fell, core inflation rose sharply from 0.4 percentage points to 6.3 per cent, raising fears that the inflation peak has not yet been reached.

In fact, inflationary pressures are continuing with the rebalancing of consumer choices from goods to services (cf. figure 2). Due to the health restrictions during the Covid crisis, many consumers had shifted a part of their consumption of services towards goods. This atypical increase in the demand for goods, particularly at the start of the post-Covid recovery, had contributed significantly to the rise in the price of durable goods. However, this rise has slowed significantly since the start of the year (from 11.5% y/y in January to 5.6% y/y in July), with consumption shifting back towards services. The demand for services has returned to its pre-Covid levels but not yet its trend, suggesting that demand could continue to increase.

The rise in property prices has also contributed significantly to the increase in consumer prices (2.1 points year-on-year in August), in particular via the rise in property prices in the cost of home-owner properties. And property prices are still expected to rise in the coming months, despite rising interest rates and signs of a market slowdown. Moreover, inflation in healthcare services, which made a significant contribution to the rebound in core inflation in August, could continue, mainly as a result of salary increases for healthcare workers.

Between the slowdown in the economy and the continued high inflation, a recent divergence has appeared between householder and business sentiment. Consumer confidence in fact improved during August, according to surveys by the Conference Board and the University of Michigan. The perception by households of their personal financial situation even recovered for the second consecutive month, thanks in particular to the positive performance of the labour market. Despite a slight increase in the unemployment rate (+0.2 points in August, to 3.7%), the labour market remains solid, which is supportive of the purchasing power of Americans and mitigates the impact of the rise in the cost of living. Total nonfarm payroll employment is slowing down but remains significant (+315k m/m in August), particularly in the business services, healthcare and retail sectors.

GROWTH & INFLATION

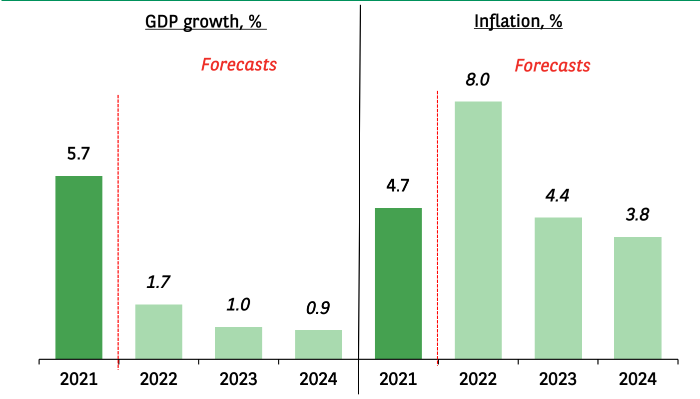

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

US: SERVICES & FOOD INFLATION RISES AS GOODS & ENERGY INFLATION EASES

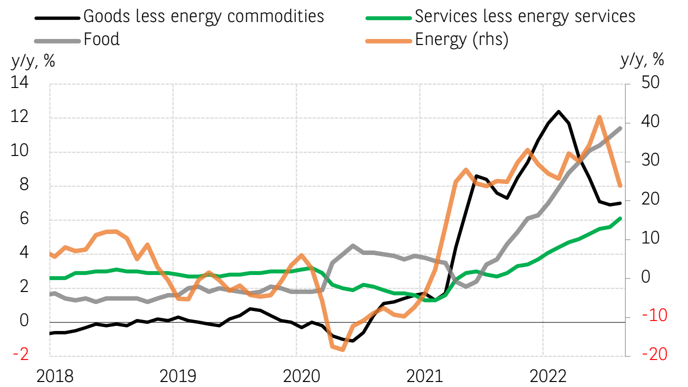

CHART 2 SOURCE: BLS, BNP PARIBAS

On the corporate side, the latest surveys of the business climate have not reflected this slightly improved outlook among households. The Philadelphia Federal Reserve's survey showed a marked slowdown in manufacturing activity (-16.1 points in September) as did the New York Federal Reserve's survey (-11.9 points in September). Nevertheless, the Empire State Manufacturing Survey also indicates that companies are anticipating an upturn in economic activity in the coming months. Specifically, businesses could benefit from the measures in the Inflation Reduction Act, which was passed in August and which is intended to accelerate energy transition in the US economy.

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