UNITED STATES

RETURN TO NORMAL

US inflation seems to have resumed its downward trajectory in Q2 2024, after a Q1 of price acceleration that led the Federal Reserve (Fed) to revise, in June, its expectations for rate cuts for the year (from three to one, in line with our own forecasts). At the same time, economic activity remains strong, although it has lost some of its momentum.

Generally, the US economy has surprised somewhat on the downside in early 2024. This was particularly reflected by the fairly sharp fall in the GDP growth rate to +0.3% q/q in Q1 (compared with expectations of +0.6%), after reaching +0.8% in Q4 2023. This figure can, however, be put into perspective by the negative contributions of changes in inventories (-0.1 pp) and, against a backdrop of rising imports, of foreign trade (-0.2 pp). In addition, the underlying measure of domestic demand (corresponding to the sum of private consumption and fixed investment), which was the driving force behind the surprising momentum of 2023, is up +0.7%, in line with recent levels. Another negative development is the -0.6% q/q fall in corporate profits, resulting from non-financial companies (-4.7%), after three quarters of progress.

Inflation was more of a source of concern than economic activity, with a series of higher than expected figures in Q1 bringing the disinflation trajectory to a halt. However, the figures available for Q2 suggest a return to normal, with two monthly slowdowns in the CPI and its underlying component, taking these to +3.3% (-0.2 pp in two months) and +3.6% y/y (-0.4 pp), respectively. Furthermore, we estimate that inflation will continue its downward trajectory, reaching +2.8% y/y in Q4 2024, before moving further towards the 2% target in 2025. As for GDP growth, we expect a rebound to +0.8% q/q in Q2, still underpinned by household consumption and business investment.

A SOFT LANDING FOR THE LABOUR MARKET?

Non-farm payrolls growth accelerated as a general trend in the first few months of 2024. In May, for example, it stood at +255k as a 6-month moving average, compared with +213k at the end of 2023. These figures indicate a robust level, but far from the levels seen in 2021 (+604k as an annual average) and 2022 (+377k), which corresponded to an exceptional situation of tightness in the post-Covid rebound phase. For the time being, these developments are more akin to a rebalancing than to a genuine deterioration in the labour market likely to provoke an anticipated move by the Fed on interest rates. Although the unemployment rate is rising and close to triggering the signal for recession, its low initial level (3.4% in April 2023) and its current level (4.0%, below the Congressional Budget Office estimate of a neutral level of 4.4%) put this rise into perspective.

By contrast, signs of rebalancing are more pronounced in the JOLTS data on job vacancies and labour turnover. The number of job vacancies, which has clearly been on a downward trend for several quarters, reached its lowest level since February 2021, at 8.05 million in April 2024. Consequently, the ratio of job vacancies to unemployed persons (known as the «v/u ratio»), which is a key measure for the Fed in assessing tightness on the labour market, stood at 1.24 in the same month. This figure, which is at its lowest since June 2021 and corresponds to the pre-pandemic levels of the US economy, provides a measure of the extent of the recovery since the record level of 2.03 seen in March 2022, on the eve of monetary tightening.

A RATE CUT TO ROUND OFF 2024

In addition to the expected unanimous decision to maintain the interest rate target (within a range of +5.25% to +5.5%, as at the 6 previous meetings), the FOMC's monetary policy meeting on 11-12 June saw the publication of the summary of the median economic projections of the committee members. The committee is now indicating a single rate cut (-25 bps) in 2024, compared with three cuts previously, although policymakers are divided (8 members expect one cut, 7 expect two, and 4 expect no change). This is in line with our forecast, since we are also expecting a single rate cut this year, in December. In our view, the likelihood of a rate cut before the last meeting of the year is limited, given the proximity of the presidential election (despite official denials regarding this factor) and because the progress of disinflation or the deterioration of the labour market is not such that easing rates would be inevitable for the Fed.

Moreover, beyond monthly or quarterly developments, the Federal Reserve is constrained by the need to preserve the credibility of its monetary commitments. This prevents it from declaring "mission accomplished" or easing its policy in real terms without a high degree of certainty that inflation will return to its target. Such an approach would contradict its mandate and could ultimately lead to further tightening if this threatens to sustainably disrupt inflation expectations (although these are also influenced by other factors, such as the price of Brent crude). In this respect, it should be pointed out that, although short-term household inflation expectations, as measured by the Conference Board, are less positive (5.4%), there has been no lasting slippage in long-term measures of market expectations. As a result, the 10-year breakeven inflation rate and the 5-year inflation swaps remain between +2.0% and +2.5%.

GROWTH AND INFLATION

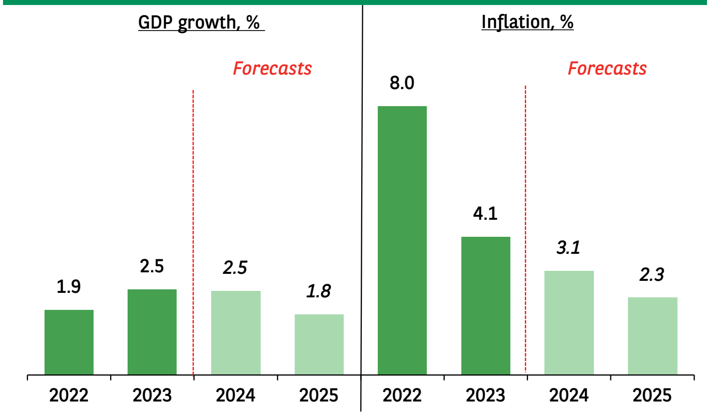

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

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