UNITED STATES

ONE FINAL RISE

The US economy continues to grow and create jobs, albeit at a gradually slower pace, and the Federal Reserve has not quite finished with rate hikes. We continue to anticipate a recession, from Q3 2023 until Q1 2024, under the effect of monetary tightening. Having opted for the status quo in June on the back of inflation continuing to fall and in order to take time to assess the effects of the monetary tightening implemented to date, the Fed is expected to make a final 25 bps increase in July, bringing the Fed funds range to 5.25-5.50%.

After being artificially supported by the positive contribution of inventory changes in Q4 2022 (+0.4 percentage points on +0.6% q/q of growth), US growth was, conversely, artificially lowered by their negative contribution in Q1 2023 (-0.5 pp on +0.5%). While the contribution of net exports was slightly positive, the contribution of final domestic demand was significant (+0.9 pp), thanks in particular to household consumption (contribution of +0.7 pp). Household consumption did not experience a single negative quarter, despite the inflationary shock, unlike the eurozone, where household consumption had already fallen twice, in Q4 2022 and Q1 2023.

In Q2, according to the Federal Reserve Bank of Atlanta GDPNow estimate, US growth would reach +0.5% q/q (non-annualised rate), a figure slightly higher than our forecast (+0.4% q/q). This positive print is likely to be fuelled by a more favourable contribution in inventories. There is little doubt that we will see a further drop in residential investment (this would be the 9th fall in a row); our attention will focus on how negative the change will be (bigger than in Q1?). The resilience of household consumption and non-residential investment will also be closely scrutinised. In particular, it will be interesting to see whether investment in structures posts a further quarter of strong growth, following on from Q4 2022 and Q1 2023 (around +4% q/q each quarter[1]), a renewed momentum attributed to the Inflation Reduction Act.

According to our scenario, Q2 would mark the last quarter of growth before the economy enters a recession from Q3 onwards, under the effect of monetary tightening. For the time being however, the economy is showing few warning signs of such a scenario, apart from the marked drop in the Conference Board Leading Economic Index (LEI, -8.4% in May, 6-month change annualised rate, with a diffusion index of 40). This decrease is due to the negative contribution of the "new orders" component of the manufacturing ISM, the credit indicator, consumer expectations and the inversion of the yield curve.

The turbulence and concerns raised by the SVB episode in March, including fears about a hard landing for the economy, have subsided: according to the latest SLOOS (Senior Loan Officer Opinion Survey on Bank Lending Practices), the tightening of lending standards has continued, but in line with previous developments. This tightening of credit conditions is more of a «squeeze» (with risk discrimination) than a more worrisome «crunch».

The ongoing deterioration of the labour market, which remains gradual, is also continuing to put the LEI recession signal into perspective. And while the main confidence surveys (ISM business confidence and consumer surveys) were negative on balance in May[2] , we should not be overly concerned for the moment. However, in terms of small businesses (NFIB survey) and CEOs (Conference Board quarterly survey), morale is very low. And according to the Federal Reserve Bank of Philadelphia Anxious Index, the probability of a decline in real GDP in the following quarter has been relatively high since the beginning of the year (around 45%).

1 Contributing approximately 0.1 percentage points to growth each quarter.
2 See EcoPulse June 2023.

GROWTH & INFLATION

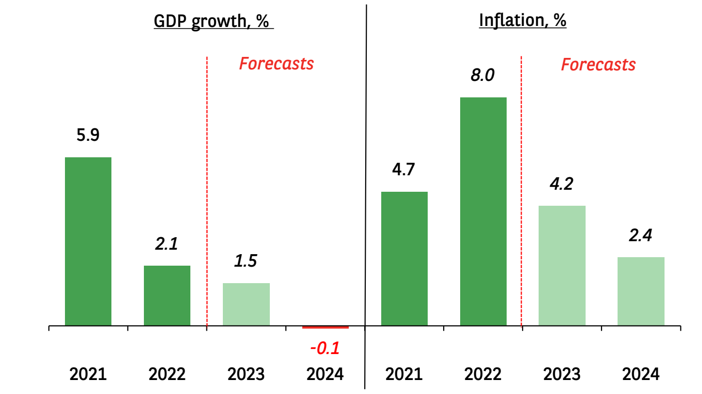

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

In June, the Fed opted, as expected, for the status quo, interrupting a series of 10 rate hikes, which had begun in March 2022, totalling 500 bps. For the Fed, it is a matter of taking the time to assess the effects of the significant monetary tightening implemented to date. Tougher lending conditions are also contributing to the Fed's monetary policy tightening. Inflation figures for May were encouraging (down -0.9 pp to 4% y/y for the headline rate - the lowest since April 2021 and the start of the inflation surge - with a drop of -0.2 pp to 5.3% y/y for core inflation). Disinflation is also about to become significant enough for real interest rates to return to positive territory, strengthening the restrictive nature of monetary policy. However, we believe this status quo by the Fed will not mark the end of the interest rate hike cycle, given the still high level of inflation and the resilience, at this stage, of the economic situation: we expect a final 25 bps increase in July, bringing the Fed funds range to 5.25-5.50%.

In our scenario, the quarter when the Fed ends its monetary tightening will coincide with the start of the recession. The latter is expected to be short and shallow (from Q3 2023 to Q1 2024 with a cumulative drop in GDP of 0.7%), as the decline in inflation, the resilience of the labour market and the favourable momentum of investment in structures will act as cushions. In annual average terms, US growth should stand at 1.5% in 2023, and should be slightly negative in 2024 (-0.1%), due to the negative carry-over at the beginning of the year (-0.4%) and a recovery which should remain restrained by the still restrictive nature of monetary policy, despite first rate cuts in the spring.

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