UNITED STATES

THE INVISIBLE TIGHTENING

The US economy keeps growing and postponing the occurrence of a recession that is still likely, but not in 2023 and in a circumscribed way. While households' consumption has so far proven resilient to the monetary tightening, the delayed and cumulative effects should eventually impulse a recessionary dynamic. The first fallout is already visible on the real estate market and the labour market has exhibited signs of easing. If rate hikes are probably over, the restrictive stance is not.

US GDP advanced by +0.5% (q/q) in Q2, an important increase enabled by the improvement in nonresidential investment (+1.8% q/q) linked to the implementation of the Inflation Reduction and CHIPS acts. Consumption brought a positive contribution again, despite a slowdown (+0.1pp v. +0.6pp in Q1). If the GDP growth rate should improve in Q3 (+0.9% q/q according to our forecast), we anticipate a sharp slowdown in Q4 (+0.1% q/q) before a slip into recession in H1 2024. The excess savings inherited from the pandemic era and the resilient labour market have contributed to postpone a widely expected recession so far, but the fade of these supporting factors and the cumulative and delayed effect of monetary tightening should eventually hit US growth and induce a contraction of GDP in Q1 (-0.3% q/q) and Q2 (-0.1% q/q) 2024.

The labour market reports some signs of easing of tensions, such as the rebound in the participation rate (62.8% in August) and the slowdown in the pace of non-farm payrolls (+189k between June and August 2023 v. +241k for the three months prior), although the latter was counterbalanced by a surprisingly positive figure in September (336k, the highest since January). We anticipate that the slow puncture will persist, and that the unemployment rate will rise to 4.7% (3.8% currently) before the end of 2024 in the wake of the recession predicted for H1 2024. This could be close to a soft landing: admittedly, the United States would observe a GDP contraction together with a higher unemployment, but on a somewhat contained scale, particularly in view of the magnitude of the monetary tightening that started in March 2022 (+525bps, the steeper since +1005bps in 1980 – 1981 under Paul Volcker's governance).

THE DIRECT EXPOSURE OF REAL ESTATE MARKET TO MONETARY TIGHTENING

Thirty-year fixed mortgage rates are currently trending around 7.3% according to Freddie Mac, the highest since 2001, against 3.5% before the beginning of rate hikes. In addition to the impact on real estate demand, this is constraining the supply of existing homes since potential sellers are unwilling to switch to a higher level of debt service. Therefore, the existing home sales have nearly steadily eroded since February 2022. Their monthly average amounts to 4.23 million since early 2023, against 5.46 million between January and August 2022. In the meantime, housing starts have fallen to a 3-year low in August (1.28 million), mitigated by a significant improvement in building permits (+6.9% m/m).

The 'New' component of the sector is therefore taking advantage from a carryover effect and was improving since November 2022 in 3-month moving average before receding in August (699k in August, -12k monthly). This should translate into the quarterly national accounts and the Atlanta Fed GDPnow is forecasting a growth of residential investment (+1.3% q/q) in Q2), following a 9-quarter streak of contraction. However, this will probably prove insufficient to support the whole real estate sector, notably because of the relative size of the new-homes market compared to existing homes (8.5 times less transactions in average since 2007). Furthermore, the NAR Affordability Index is still trending at standards unseen since the mid-1980s (87.7 in August).

GROWTH & INFLATION

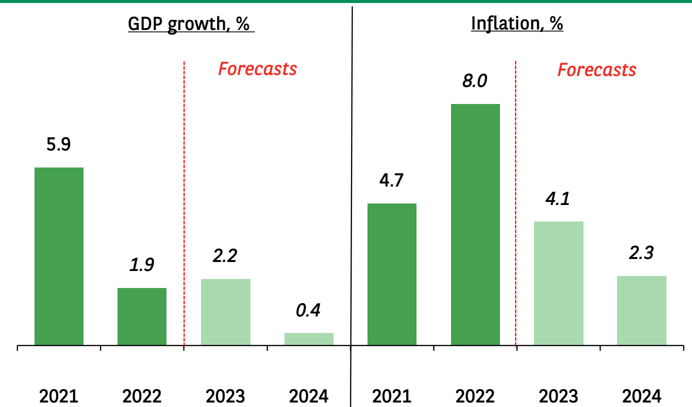

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

HIGHER FOR LONGER

The September FOMC meeting resulted in holding the target at 5.25%-5.50%, following a +25 bps hike in July, and despite the summer increase in inflation (+3.7% y/y for the CPI in August vs. +3.1% in June). The rate decision was disclosed together with the Summary of Economic Projections Q3 update, which views an additional +25 bps by the end of the year, followed by -50 bps in 2024 - implying an upward revision of the expected rate for the end of 2024. Our baseline scenario is unaffected, as we still consider the de jure monetary tightening over, although risks are tilted to the upside. The general stance of the Federal Reserve and Jerome Powell remains hawkish, although the risk management question is increasingly present. It must be highlighted that, with time moving on and inflation moving down, holding the nominal interest rates translates de facto into further tightening.

Finally, there are several points to be monitored over the coming weeks. On the one hand, consumption could suffer from the resumption of student loans repayments starting in October. On the other hand, it is also likely to be constrained by sustainably higher level in oil prices (the Brent price is currently higher than 85 USD), which would undoubtedly exert upward pressures on inflation and could threaten the anchoring of expectations. In addition, a government shutdown is still plausible and would disrupt government action and weigh on federal employees (4M people), while the potential consequences of the UAW strike are uncertain.

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