BEA 東亞銀行

Economic Research

August 2021

Market Monitor – United States

Solid Growth Amid Persistent Inflationary Pressure

Supply chain constraints continue to prop up consumer prices

Supply chain constraints continue to boost inflation.

Resurgence in Covid-19 cases triggers fears that recovery of US economy may be distorted.

Treasury yields drop as investors seek safe havens.

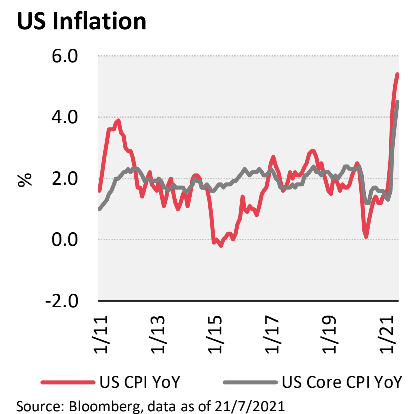
As pandemic-related restrictions continued to ease, the US economy saw solid recovery in the second quarter, with GDP rising at an annualised rate of 6.5% quarter-on-quarter. This was mainly supported by a further rise in consumption, with personal consumption expenditure seeing 11.8% growth during the quarter. Meanwhile, the US labour market showed further improvements in June, with 850,000 jobs added to nonfarm payrolls. The rise in nonfarm payrolls topped market expectations. However, unemployment edged up slightly from 5.8% in May to 5.9% in June, with more people voluntarily leaving their jobs.

Inflationary pressure continues to grow as the economy recovers. Headline CPI rose 5.4% year-on-year in June, the biggest increase since August 2008, following a 5.0% rise in May. Core CPI also climbed 4.5% during the month, the largest rise since November 1991. Continued supply chain constraints like chip shortages contributed to the persistent rise in consumer prices, with a 45.2% surge recorded in used car prices during June.

Despite the continued rise in inflationary pressure, the Federal Reserve (Fed) still held the fed funds rate at 0%-0.25% and maintained the monthly asset purchase programme at its policy meeting in July. Chairman Powell also revealed that the officials had taken the first "deep dive" into how to scale back asset purchases. However, decision on tapering timing had not yet been made at the meeting. Powell also suggested that the Fed still needed to more time to look at the data, especially the employment side, to ensure the right timing for any policy move.

Looking ahead, although the US economy is expected to see continued recovery in the second half of 2021, the spread of the delta variant may pose risks to continued economic recovery. The new variant may challenge the effectiveness of existing vaccines and a further resurgence in cases could trigger a resumption of lockdown measures, resulting in disruption to business activity and consumption.

US Inflation

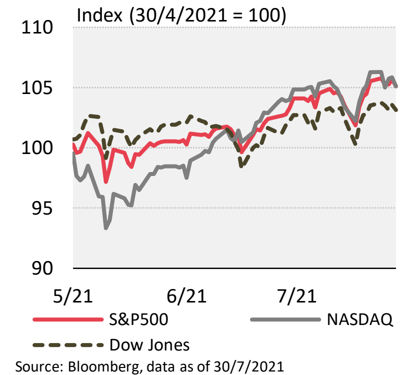


Source: Bloomberg, data as of 21/7/2021

Equity markets see choppy trading amid resurgence of new cases

As of 31st July, the 7-day average of new Covid-19 cases in US was about 78,600, significantly up from less than 12,500 cases at the end of June. Some advanced economies like the UK and Japan also saw a rebound in new cases. Benchmark equity indices dipped as investors worried about the spread of the delta variant and its potential impact on the US and other major economies. On 19th July, the S&P 500 Index was nearly 1% down from the level at the end of June, while the Nasdaq and Dow Jones both dropped 1.6% compared to the end of the previous month. Equity markets later rebounded as investors expected companies to post brighter earnings in the second quarter. As of 30th July, the S&P 500 index had registered a 2.3% gain since the end of June, while the Nasdaq and Dow Jones recorded 1.2% gain and 1.3% gain, respectively, over the same horizon.

US Equity Indices



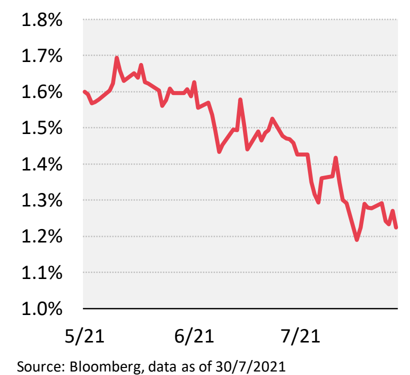
Source: Bloomberg, data as of 30/7/2021

Treasury yields drop as investors become risk-averse

Treasury yields dropped, as investors flocked to safe haven assets amid fears that a resurgence in Covid-19 cases could threaten the US economic recovery. As of 30th July, the 10-year US Treasury yield stood at 1.224%, about 25 basis points lower than the level at the end of June. Nonetheless, as the Fed still underscored that more economic improvement would be required before making any policy shift and market participants reckoned that the interest rates would remain low in the short run, dollar index saw 0.3% drop over the same horizon.

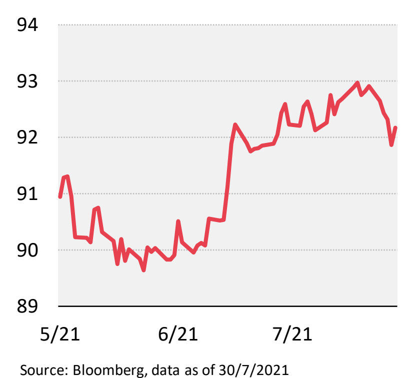
Going forward, the movement of treasury yields and the US dollar will be determined by the risk appetite of investors. If the economy and jobs market continue to improve and inflation expectation persists, the Fed will start to reduce asset purchases. The benchmark 10-year treasury yield may resume its upward trend and the US dollar may strengthen again. Assets that previously benefited from low interest rates and ample liquidity may face the risk of a price correction.

US 10-year Treasury Yield



Source: Bloomberg, data as of 30/7/2021

Dollar index



Source: Bloomberg, data as of 30/7/2021

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