Economic Research

September 2022

Market Monitor – United States

Inflation Eases Slightly in July

Headline inflation eases slightly in July as energy prices decelerate

Real GDP growth in Q2 was revised slightly upward to an annualised rate of -0.6%, up from -0.9% previously, driven by an upwardly revised growth in consumer spending. The overall message from Q2 GDP remained little changed however, with two consecutive quarters of negative growth and real domestic final sales remaining weak, dragged down by inventories and lower residential and structural investment.

Inflationary pressure moderated slightly in July, driven mainly by decelerating energy prices. The headline consumer price index (CPI) eased somewhat from the four-decade high of 9.1% year-on-year (YoY) growth in June to 8.5% in July, while the core CPI, which excludes food and energy prices, stayed unchanged at 5.9% YoY in July. On a month-to-month basis, headline inflation was 0.0% in July, down from 1.3% in June, while core inflation was 0.3%, down from 0.7% in June.

Among the price components, energy prices slowed by a rather significant 8.7 percentage points to 32.9% in July. There was no let-up in food inflation, with prices rising 10.9% YoY in July, up 0.5 percentage point from June. Moreover, we are also seeing a significant shift in inflationary pressure from core goods prices to core services prices. For example, used vehicle prices decelerated from 7.1% YoY in June to 6.6% in July, while new vehicle prices decelerated from 11.4% to 10.4%. At the same time, shelter costs continued to accelerate from 5.6% YoY in June to 5.7% in July, while transport costs rose from 8.8% to 9.2%. This trend is expected to continue into Q4 2022, with prices for core services rising more quickly than for core goods. Given the slow deceleration, inflation is unlikely to return to the target set by the Federal Reserve (Fed) anytime soon.

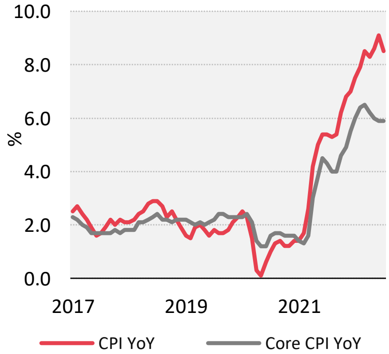
As the rise in energy prices continues to decelerate, consumers are beginning to lower their short-term inflation expectations, which resulted in a further slight rebound in consumer confidence in August. The University of Michigan Consumer Sentiment Index rose to 58.2 in August, up from 51.5 in July, while the one-year inflation expectation fell to 4.8% in August, down by 0.4 percentage point from July and reaching the lowest since

Inflation eases slightly from a four-decade high, with headline CPI YoY growth of 8.5% in July.

Labour market remains tight, with 315,000 jobs added to nonfarm payrolls in August, despite the unemployment edging up by 0.2 percentage point month on month to 3.7%.

Cautious lift in consumer sentiment.

US Inflation



Source: Bloomberg, data as of 15/8/2022

December 2021. At the same time, the five-year inflation expectation stayed at 2.9% in August.

US employment market remains active, but the unemployment rate edged up by 0.2 percentage point to 3.7% in August, mainly reflecting more people returning the labour force. The labour participation rate also rose 0.3 percentage point to 62.4% in August. The number of newly added nonfarm payroll moderated to 315,000 in August, its June and July figures also revised down by 105,000 and 2,000 to 293,000 and 526,000 respectively. In the first eight months of 2022, the monthly increase of nonfarm payroll averaged 438,000, lower than average of 562,000 in 2021, indicating the employment market has recorded some initial slowdown from a rather tight level, while average hourly earnings continued to see solid growth of 5.2% in August.

The minutes of the Federal Open Market Committee's (FOMC) July meeting revealed that officials still saw the need for ongoing rate hikes, despite slower spending and production amid the normalisation of monetary policy. While officials discussed a potential slowdown in rate hikes, they believe that it would be appropriate to raise the rate further to a restrictive level and maintain it there for some time to ensure that inflation is firmly on the path back to 2%. As the Fed has not yet finished its tightening of monetary policy, overall growth momentum – including consumer spending and business investment – is likely to slow down further in the months ahead.

Equity markets see increased volatility in August, amid higher bond yields and a stronger US dollar

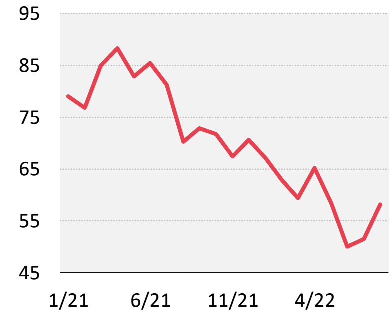
US equity markets registered significant gains in the first half of August, as US companies reported better-than-expected earnings, inflationary pressure showed initial signs of peaking, and the markets were beginning to price in a slower pace of rate hike ahead. However, as investors faced renewed worries over more aggressive tightening by the Fed towards the end of August, after the hawkish remarks by Fed Chair Jerome Powell at Jackson Hole Economic Symposium, the downward pressure of stock market indices intensified. As of 31st August, the S&P 500 Index had dropped by 4.2% since the end of July, and the Nasdaq by 4.6%. The Dow Jones Industrial Average was down by 4.1% over the same horizon.

In the bond market, the benchmark 10-year treasury yield edged higher as market fears of a severe economic downturn had been allayed to some extent and the Fed was expected to continue raising interest rate aggressively. As of 31st August, the 10-year treasury yield stood at 3.195%, about 54 basis points higher than at the end of July.

In the foreign exchange market, the US dollar saw volatile movement in August, with the dollar index once falling by 0.8% from the end of July and the CPI figure weaker than expected. Nonetheless, the dollar regained momentum after the release of the FOMC minutes and as worries over the global economic outlook intensified. The dollar index rose above 109 at one point as demand for safe haven assets increased. As of 31st August, the dollar index stood at 108.7, about 2.6% higher than at the end of July.

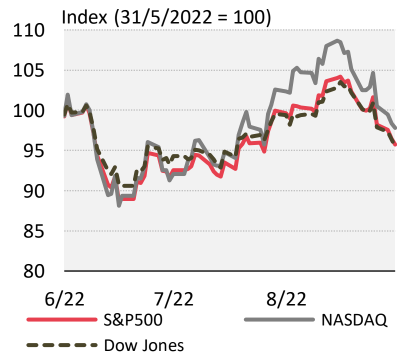
Looking ahead, the US financial markets may see increased volatility as investors' risk appetite evolves in response to the US economic outlook, expected monetary policy, geopolitics, and other factors.

University of Michigan Consumer Sentiment Index



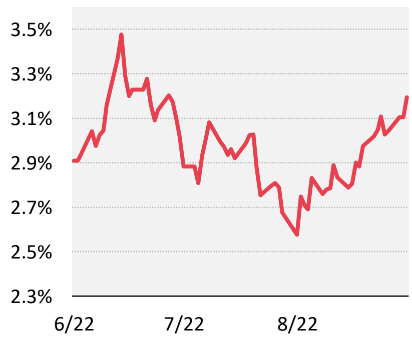
Source: Bloomberg, data as of 31/8/2022

US Equity Indices



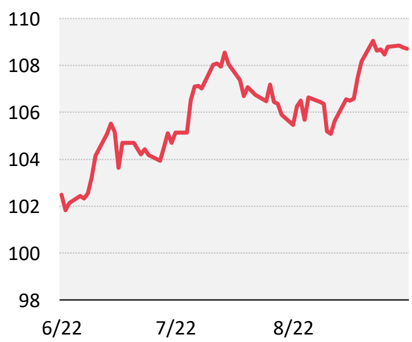
Source: Bloomberg, data as of 31/8/2022

US 10-year Treasury Yield



Source: Bloomberg, data as of 31/8/2022

Dollar Index



Source: Bloomberg, data as of 31/8/2022

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