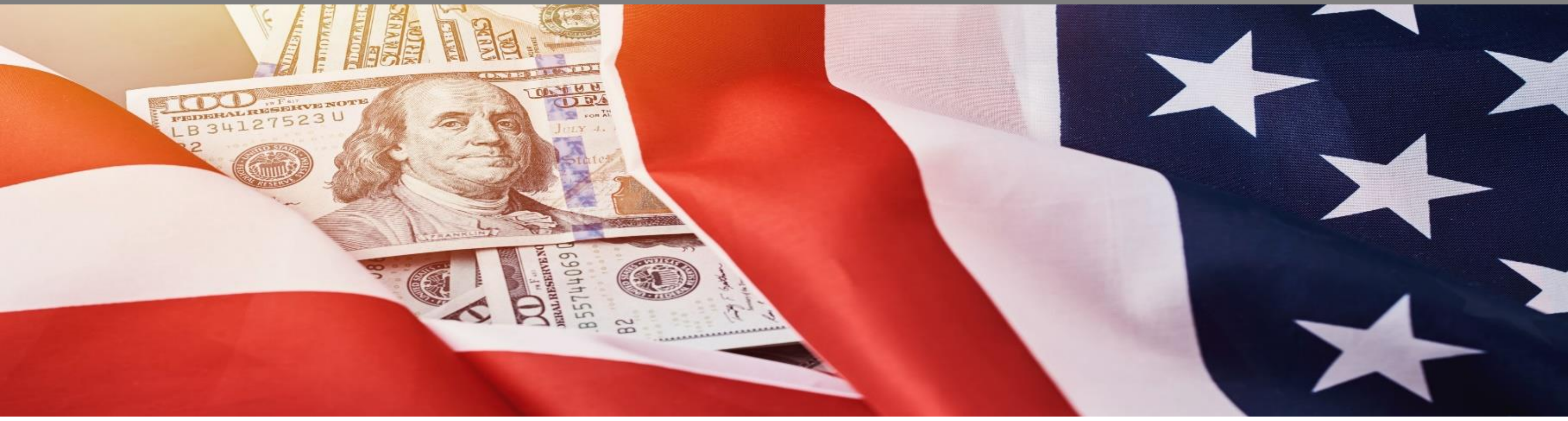
BEA 東亞銀行

Economic Research

February 2023

Market Monitor – United States

The Slowing Pace of Rate Hikes



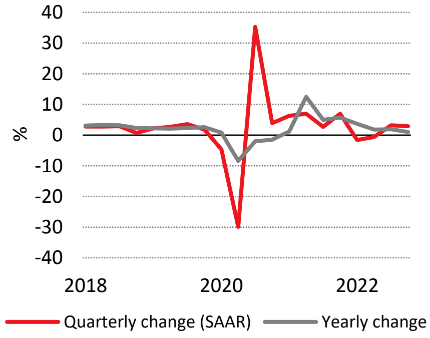
- US GDP expanded at an annualized rate of 2.9% QoQ in Q4 2022 and 2.1% YoY for the whole year of 2022, chiefly supported by a moderate growth in consumer spending and an improvement in net exports.
- The Fed raised the fed funds rate by another 25 bps to 4.5%-4.75% at its latest meeting, but the rate hike cycle is yet to be over as inflation is expected to exceed its policy target for some time.
- The US job market remains tight at the beginning of 2023, with nonfarm payroll adding 517,000 jobs in January. The unemployment rate further dropped to a 54 year low of 3.4%.

US economy remained resilient in 2022 despite rapid rate hikes

The US economy recorded solid growth in 2022 despite aggressive rate hikes. US GDP expanded at an annual rate of 2.9% quarter-on-quarter (QoQ) in Q4 2022, only slightly lower than the 3.2% growth in the previous quarter. The Q4 2022 growth was mainly driven by a moderate expansion in personal consumption, positive contribution from net exports and inventory investments. However, the rapid interest rate hike in 2022 negatively impacted the housing sector, as residential investment dropped by an annualized rate of 26.7% QoQ in Q4 2022 after dropping 27.1% QoQ in Q3 2022. On a year-on-year (YoY) basis, US GDP slowed gradually from 3.7% in Q1 to 1.8%, 1.9% and 1.0% from Q2 to Q4, respectively, and grew 2.1% for the whole year of 2022.

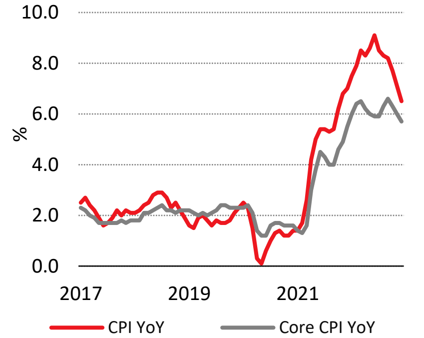
Meanwhile, the YoY increase in headline consumer price index (CPI) further decelerated to 6.5% in December 2022 from 7.1% in November, mainly due to a drop in energy prices. The growth of core CPI also decelerated by 0.3 percentage points from the previous month to 5.7% YoY in December 2022, mainly due to the continued easing in the price of core goods. However, the rise in core services and shelter costs remains high at 7.0% YoY and 7.5% YoY, respectively, in December. The stickiness of core services and shelter costs indicates that overall inflation will remain well above the 2% policy target for some time.

US GDP



Source: Bloomberg

US Inflation



Source: Bloomberg

In the start of 2023, the US job market remains tight with nonfarm payroll adding 517,000 jobs in January and upward revisions for both November and December of 2022. The unemployment rate further dropped to a 54-year low of 3.4% in January 2023 from 3.5% in December 2022. However, the YoY increase in average hourly earnings eased to 4.4% in January 2023 from an upwardly revised 4.8% in December 2022 and clearly slowed when compared to the 5.9% in March 2022.

The pace of rate hikes was reduced to 25 bps, as expected, but the rate hike cycle is yet to be over

The Fed slowed its pace of rate hikes to 25 bps as expected, raising the fed fund funds rate to 4.50%-4.75% in its February meeting, but signalled that more rate hikes are ahead. At the press conference, Chairman Powell said that they had already raised rates by 4.5 percentage points, and are deliberating a couple more rate hikes to reach a level they consider to be appropriately restrictive. This means that the Committee is still upholding the December's dot plot projections, which indicates two more possible 25-bp hikes in March and May respectively, raising the fed funds rate target range to 5.00%-5.25%. Chairman Powell pushed back against possible rate cuts in 2023, and believes that the fed funds rate needs to be restrictive for some time.

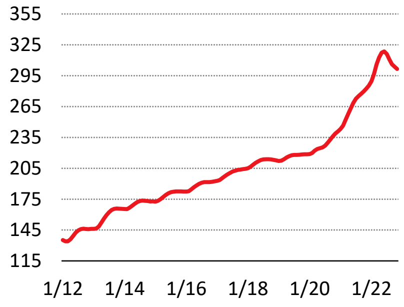
The US economy is expected to stay modest in 2023, given an elevated inflation and tight monetary policy stance, etc. With the aggressive rate hikes by the Fed, the interest rate sensitive housing market recorded a notable slowdown. The S&P 20-city Composite Home Price Index fell for five consecutive months, declining by 0.5% month-on-month (MoM) in November 2022 after falling 0.5% MoM in October. Although the Fed envisaged a pause in rate hikes when inflation shows a clear downward trend toward its policy target, the interest rate is expected to stay elevated for the rest of 2023. Besides, global economic growth is set to slow further in 2023 according to the latest IMF forecast. Global GDP is forecasted to see 2.9% growth in 2023, down from 3.4% in 2022. In addition, the recent layoffs announced by large US corporations have spread beyond the technology sector, with Goldman Sachs, Fedex and McDonald's announcing layoff plans in January 2023. Finally, the debt ceiling could be another important issue which could hit US economic performance in 2023. With US consumer and investment performance expected to stay soft in 2023, US GDP growth is expected to slow further to 0.5%, when compared to 2.1% in 2022.

Benchmark equity indices rebound in January 2023

US equity markets rebound in the beginning of 2023, with investors optimistically expect the near end of the interest rate hike cycle and companies reporting better than expected earnings for Q4 2022. Major stock market indices posted gains in January 2023. As of the 31st January 2023, the Dow Jones Industrial Average, S&P 500 and Nasdaq rose by 2.8%, 6.2% and 10.7%, respectively when compared with the end of December 2022. Meanwhile, the benchmark 10-year treasury yield closed at 3.511% at the end of January 2023, 37 basis points lower than the previous month.

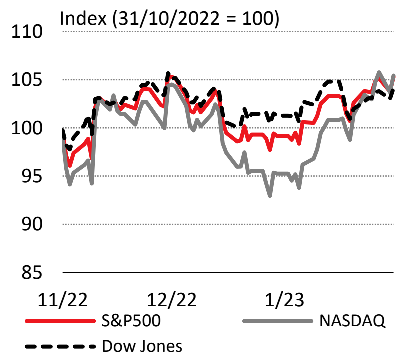
The US dollar also weakened as investors begin pricing in the end of the rate hike cycle. As of the 31st January 2023, the dollar index stood at 102.10, about 4.4% lower than the level at the end of 2022.

S&P/Case-Shiller 20-City Composite Home Price Index



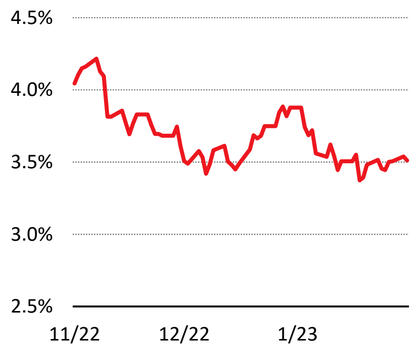
Source: Bloomberg

US Equity Indices



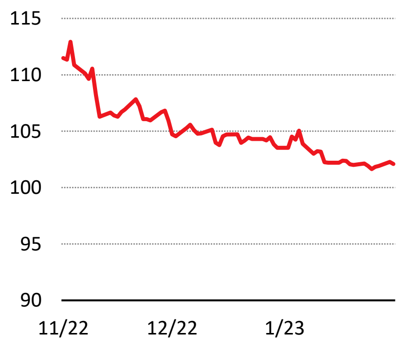
Source: Bloomberg, data as of 31/1/2023

US 10-year Treasury Yield



Source: Bloomberg, data as of 31/1/2023

Dollar Index



Source: Bloomberg, data as of 31/1/2023

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