BEA東亞銀行

Economic Research

May 2023

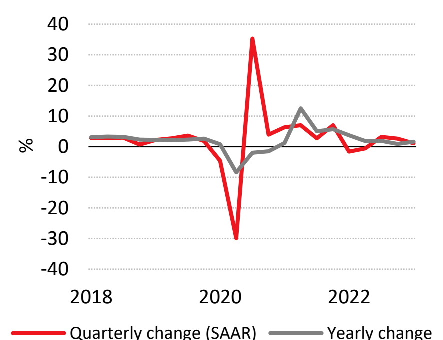
Market Monitor – United States

Moderate Growth in Q1 2023 But Downside Risks Remain

- The US economy expanded moderately in Q1 2023, with a 1.1% annualized QoQ GDP growth.
- Headline inflation continued to ease, but core inflation remained sticky, with headline and core consumer price indices (CPI) rising by 5.0% and 5.6% YoY in March respectively.
- The Fed raised the fed funds rate target range by 25 (basis points) bps to 5.00%-5.25% at its May meeting and signalled that the US is near the end of the rate hike cycle.

US economic growth moderated in Q1 2023 and core CPI remained firm in March

The US economy expanded moderately in Q1 2023 due to the drag caused by the changes in inventories. GDP grew at an annualized rate of 1.1% quarter-on-quarter (QoQ) in Q1 2023, down from the 2.6% QoQ growth in the previous quarter. The slower headline growth in Q1 2023 was mainly driven by the negative contribution from the change in private inventories and a slight decline in fixed investment, while personal consumption expenditure still posted solid growth with net exports making a small contribution. Private consumption expenditures and exports posted annualized QoQ growth of 3.7% and 4.8% in Q1 2023 respectively, up from 1.0% and -3.7% in the previous quarter, however, fixed investment recorded an annualized QoQ decline of 0.4%, with residential investment declining by 4.2%, both up from -3.8% and -25.1% in the previous quarter respectively. Changes in private inventories contributed to the largest negative drag, subtracting 2.3 percentage points (ppts) from the annualized GDP growth in Q1 2023. On a year-on-year (YoY) terms, US real GDP accelerated slightly from 0.9% in Q4 2022 to 1.6% in Q1 2023, indicating that the moderate expansionary trend continues.



Source: Bloomberg

US job market eased slowly amid tightened monetary environment and banking sector concerns. The US employment market remained solid, though easing slowly since the Fed's tightening cycle began. In April, nonfarm payroll added 253,000, up from the downwardly revised 165,000 in March but gradually slowing from the 6-month average

of 290,000. The unemployment rate edged down by 0.1 ppt from March to a multi-decade low of 3.4% in April. The YoY increase of average hourly wage edged up by 0.1 ppt from March to 4.4% in April, though it was down 1.4 ppts from the same month last year. Nevertheless, the Fed is expected to stay cautious, with a relatively tight job market and wage growth remains higher than consistent with the 2% inflation target.

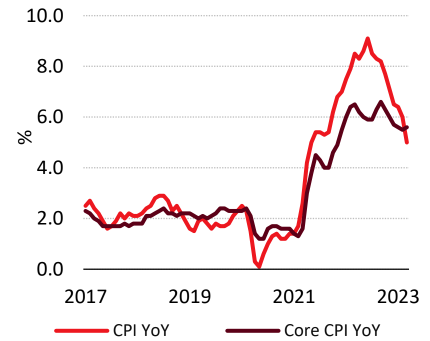
Driven by a decline in energy prices, the headline CPI dropped by 1.0 ppt to 5.0% YoY in March. Despite a lower headline CPI, core inflation stayed firm and edged up again from 5.5% YoY in February to 5.6% in March, as core services and shelter costs stayed elevated, with the former edging down from 7.3% YoY in February to 7.1% in March, while shelter costs accelerated slightly to 8.2% YoY in March from 8.1% in February. With the solid employment market and still robust wage growth, core inflation is expected to only gradually moderate in the months ahead, taking time for it to return to the Federal Reserve's (Fed) policy target. Amid the high inflation and interest rate environment, the University of Michigan Consumer Sentiment Index remained subdued and inched up by only 1.5 points from March to 63.5 in April. The 1-year inflation expectations bounced by 1.0 ppt to 4.6%, while the 5-year expectation slightly edged up by 0.1 ppt to 3.0% in April.

The Fed hiked another 25 bps despite persistent uncertainties in regional banking issues

As inflationary pressures stay elevated, the Fed raised its policy rates by 25 basis points (bps) at its May policy meeting, bringing the target range of the fed funds rate to 5.00%-5.25%. There were a couple of dovish changes to the policy statement in May, such as dropping the March statement's reference "to attain a stance of monetary policy that is sufficiently restrictive", and replacing March statement's data dependent language from "in determining the extent of future increases in the target range" to "in determining the extent to which additional policy firming may be appropriate". These indicated that the explicit policy tightening bias in the previous statement was softened. Chairman Powell further said a few times that the policy rate is tight and that the real rates are meaningfully above the neutral rates. However, Chairman Powell also said that future decisions would be made on a "meeting-by-meeting basis" and that the Committee was "prepared to do more if greater monetary policy restraint is warranted." Overall, the message from the May meeting signalled that the US is near the end of the rate hike cycle, but a rate cut in 2023 is not expected with inflation remaining far higher than the Fed's policy target and the labour market remaining tight.

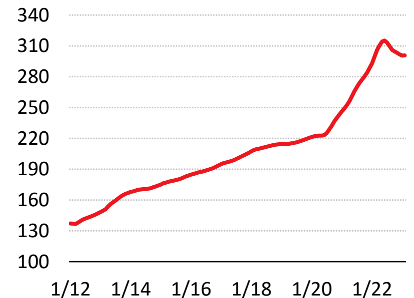
Looking ahead, the impact from the rapidly tightening monetary policy is expected to surface gradually, which could have repercussion on the US financial markets and economy. Given that the US interest rate has cumulatively risen by 500 basis points in roughly more than a year time, the rapidly tightened credit conditions would not only affect the financial soundness of regional banks but could also affect the refinancing and value of US properties ahead. The YoY increase of the S&P/Case-Shiller 20-City Composite Home Price Index narrowed significantly to 0.4% in February from the 2.6% in January, although recording a slight 0.1% MoM rise after 7 consecutive months' decline. If the US property markets, including commercial real estate, correct abruptly, the consumption and business sentiment will no doubt be seriously impacted. Coupled with the debt ceiling deadlock, the outlook of US economy and its financial markets remains highly uncertain.

US Inflation



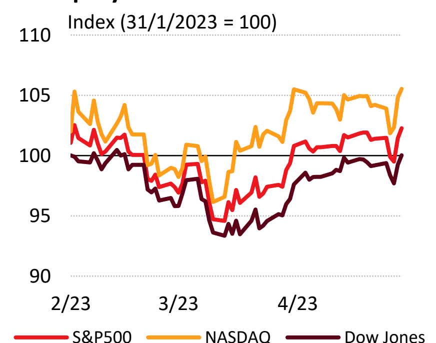
Source: Bloomberg

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



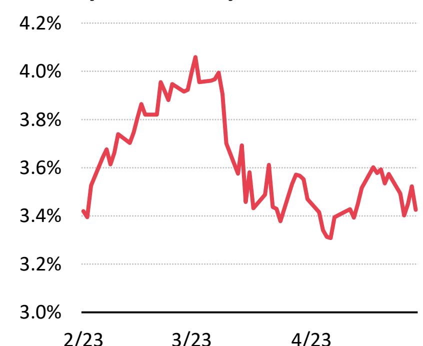
Source: Bloomberg

US Equity Indices



Source: Bloomberg, data as of 30/4/2023

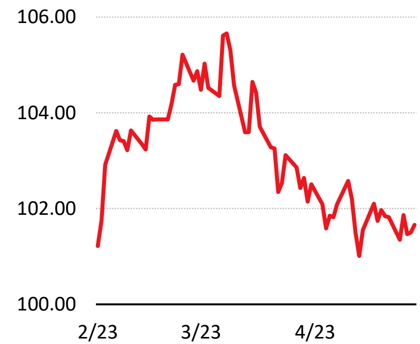
US 10-year Treasury Yield



Source: Bloomberg, data as of 28/4/2023

US stock markets saw stable performance, while the dollar slightly weakened

In April, US benchmark equity indices saw stable performance, with expectation that the US rate hike cycle is close to the end and some companies reporting better-than-expected earnings. As of the end of April, the S&P 500 Index and Dow Jones Industrial Average rose by 1.5% and 2.5% respectively, when compared to the end of March. Meanwhile, Nasdaq was little changed over the same horizon. As market participants remained somewhat cautious, the 10-year treasury yield closed at 3.425% at end-April, down 5 basis points from the previous month. Meanwhile, the US dollar slightly weakened, driven by the easing safe haven demand and expectations that the Fed's rate hike cycle could end soon, with the dollar index closing at 101.659, down about 0.8% from the level at end-March.



Source: Bloomberg, data as of 28/4/2023

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