Weekly Update of U.S. Economy

Junko Nishioka
Chief Economist
Sumitomo Mitsui Banking Corporation

(212) 224-4568
junko_nishioka@smbcgroup.com

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Conditions Not Recessionary but Show Signs of Economic Slowdown

The Uptick in Business Costs Should Be Short-Lived

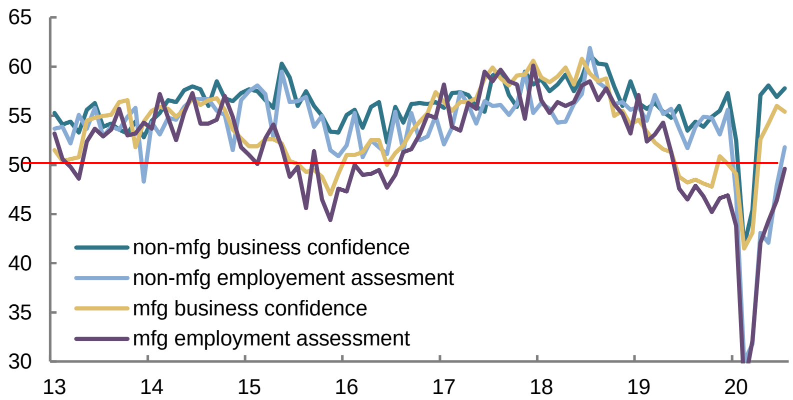
- The Institute for Supply Management (ISM) services index rose 0.9 points to 57.8 in September, signaling growth for the fourth consecutive month. However, the business confidence data shouldn't be taken at face value, and the economy still has a long way to go before it fully recovers from the COVID-19-led recession.
- The trade deficit widened to the largest figure since 2006 as the U.S. imported a record amount of consumer goods ahead of the holiday shopping season while sluggish global demand slowed the recovery pace of exports.
- Job openings and hires changed little in August, indicating that a rapid recovery of the labor market from the bottom in April has tapered off. The expiration of fiscal support seems to have limited the scope for retaining and rehiring of employees.
- Even an agreement between House Speaker Nancy Pelosi and Treasury Secretary Steven Mnuchin would be a major step towards fiscal stimulus in the near term, though that is unlikely to draw support from enough Senate Republicans to pass the Senate before the election.
- The delayed approval of the Phase Four fiscal package would prompt the Federal Reserve Board and market participants to revise downward their economic forecast as the consensus economic view had largely incorporated the positive impact of fiscal measures during the October-December quarter.
- We forecast the U.S. GDP to considerably slow its pace of recovery in October-December of this year to 2.1% on a quarter-over-quarter annualized basis following a rapid recovery in July-September.
- Due to supply constraints, as observed in slower deliveries in the ISM data, and the difficulties in labor force retention, the economy will likely face upward pressure on costs. The September Consumer Price Index (CPI), due out next week, is one of the key data points in closely measuring how much corporations are passing their costs onto output prices. However, we believe that sluggish final demand in the economy will ultimately dominate as a factor to dampen corporate pricing power and the economy will likely face downward pressure on inflation in the long run.

It's Too Early to Anticipate More Easing

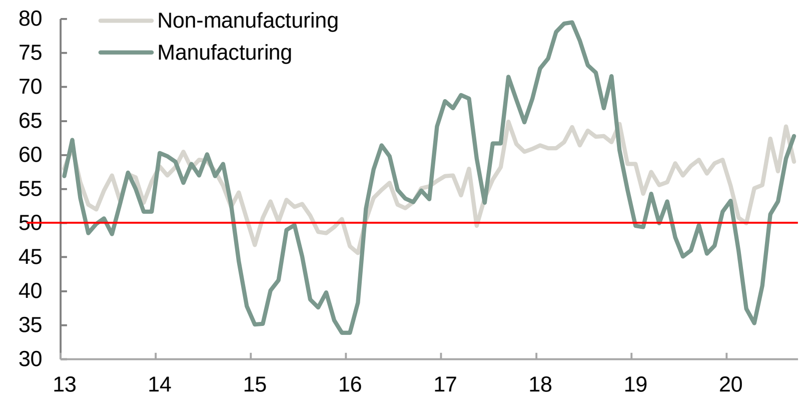
- The minutes of the Federal Open Market Committee (FOMC) meeting held on September 15 and 16 revealed that the enhancement of the forward guidance was made without a firm consensus among the members: while a majority agreed on the maintenance of the current low-interest-rate policy until "inflation had risen to 2 percent and was on track to run moderately in excess of 2 percent for some time", a couple of participants preferred an even stronger policy such that the policy rate would remain "at the ELB until inflation had moved above 2 percent for some time".
- These differences of opinion suggest that a large number of board members might have considerable fears on the possibility of inflation rising at an uncontrollable pace, based on historical experiences like those seen in the 1970s, and would not actively support freely allowing the inflation rate to overshoot the 2% target.
- Another focal point in the minutes is the fact that there is no concrete discussion on quantitative measures to combat downside risks of inflation and the economy. While the board members are not agreed on the degree of the commitment on the average inflation target, it is unlikely that they will reach a consensus on additional asset purchases.
- These developments are also hinted at by the public comments this week provided by board members Charles Evans, president of the Federal Reserve Bank Chicago and Loretta Mester, president of the Federal Reserve Bank of Cleveland, who downplayed the chance of additional asset purchases as a supplemental measure.
- While there has been little progress on the Phase Four fiscal package until now, the board members are likely to downwardly revise their economic forecast for 2020 as the most recent economic forecast had assumed the legislative passage of the package in the near future.

Uptick in Inflation Expectations

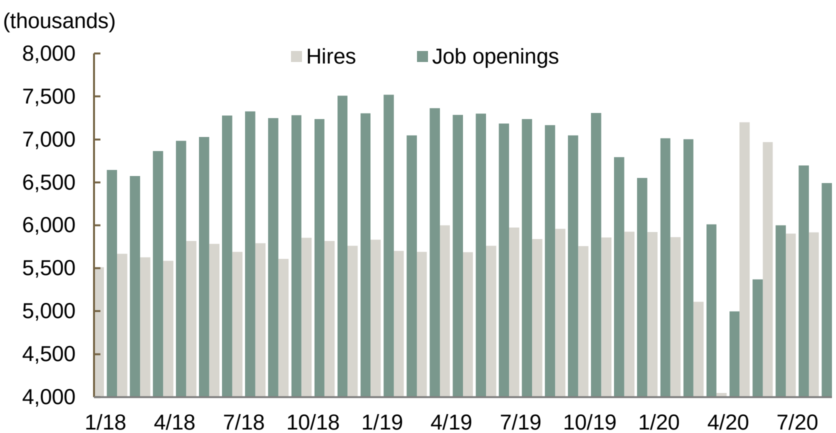
Business confidence in the service sector seems to have tapered off after its recovery from the April bottom. Meanwhile, the employment assessment finally reached the neutral level.



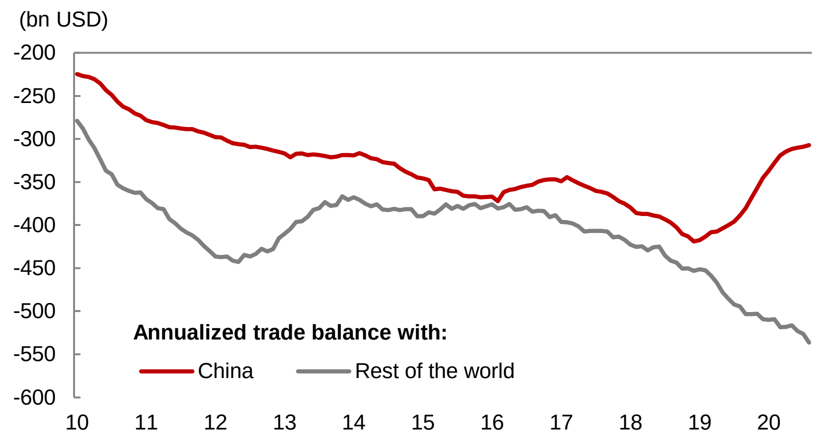
Supply constraints have been raising the price of materials and transaction costs. This may move business managers' price assessments higher but it should be short-lived.



Job openings and hires changed little in August, suggesting that the rapid recovery of the labor market took a pause.



The trade deficit ex-China has widened as the U.S. accelerated its pace of consumer goods imports while the pace of exports slowed.



Sources: Bureau of Labor Statistics, Institute for Supply Management, Bureau of Economic Analysis

SMBC Economy and Rates Forecast

		2019			2020				2021				2018	2019	2020	2021
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
U.S.	Real GDP (saar)	2.0	2.1	2.1	-5.0	-31.4	33.6	2.1	4.6	3.3	2.5	2.5	2.9	2.3	-3.6	3.9
	Inflation rate (YoY)	1.6	1.7	1.6	1.7	1.0	1.5	1.6	1.6	2.0	1.8	1.8	1.9	1.6	1.5	1.8
	Jobless rate	3.6	3.6	3.5	3.8	13.0	8.8	7.6	7.2	6.9	6.7	6.5	3.9	3.7	8.3	6.8
Euro area	Real GDP (qoq)	0.2	0.3	0.0	-3.6	-11.8	8.2	2.0	1.2	1.0	0.8	0.6	1.9	1.3	-8.1	4.8
	Inflation rate (YoY)	1.3	0.9	0.9	1.1	0.2	0.0	0.2	0.4	1.0	1.1	1.2	1.9	1.2	0.4	0.9
	Jobless rate	7.6	7.5	7.4	7.2	7.8	8.2	8.8	9.0	9.0	8.9	8.8	8.2	7.6	8.0	8.9
Japan	Real GDP (saar)	1.6	0.2	-7.0	-2.5	-28.1	15.6	8.8	3.2	2.6	2.2	0.9	0.3	0.7	-5.4	2.9
	Inflation rate (YoY)	0.8	0.5	0.2	0.6	-0.1	-0.2	-0.7	-0.4	0.3	0.3	0.2	0.8	0.7	0.1	0.2
	Jobless rate	2.4	2.3	2.3	2.4	2.8	3.0	3.2	3.2	3.2	3.1	3.0	2.4	2.4	2.8	3.1
China	Real GDP(YoY)	6.2	6.0	6.0	-6.8	3.2	5.3	5.6	19.4	7.8	5.8	5.6	6.7	6.1	2.2	8.9
	Inflation rate (YoY)	2.6	2.9	4.3	5.0	2.7	2.4	2.2	2.0	2.2	2.3	2.4	2.1	2.9	3.5	2.2
	Jobless rate	5.0	5.2	5.1	5.9	5.9	5.6	5.5	5.5	5.4	5.4	5.4	4.9	5.2	5.7	5.4

Rates		2019	2020				2021				2019	2020	2021
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
U.S.	FF target range	1.50 ~ 1.75	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	0.00 ~ 0.25	1.50 ~ 1.75	0.00 ~ 0.25	0.00 ~ 0.25
	2yr UST	1.57	0.25	0.15	0.13	0.10	0.10	0.10	0.10	0.10	1.57	0.10	0.10
	10yr UST	1.92	0.67	0.66	0.68	0.60	0.75	0.90	1.20	1.50	1.92	0.60	1.50
Germany	ECB refi rate	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
	ECB depo rate	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
	2yr Schatz	-0.60	-0.69	-0.69	-0.70	-0.70	-0.65	-0.60	-0.60	-0.60	-0.60	-0.70	-0.60
	10yr Bunds	-0.19	-0.47	-0.45	-0.52	-0.55	-0.50	-0.40	-0.30	-0.20	-0.19	-0.55	-0.20
Japan	IOER	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10	-0.10
	2yr JGB	-0.13	-0.14	-0.13	-0.13	-0.10	-0.10	-0.10	-0.10	-0.10	-0.25	-0.10	-0.10
	10yr JGB	-0.11	0.02	0.03	0.02	0.05	0.05	0.05	0.05	0.05	-0.11	0.05	0.05
China	Policy rate	4.15	4.05	3.85	3.85	3.85	3.85	3.85	3.85	3.85	4.15	3.85	3.85
	2yr gov bond	2.46	1.95	2.24	2.76	1.80	1.75	1.75	1.70	1.70	2.46	1.80	1.70
	10yr gov bond	3.14	2.59	2.85	3.13	2.70	2.70	2.65	2.60	2.55	3.14	2.70	2.55

SMBC FX Forecast

		2019	2020				2021				2019	2020	2021
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
USD/JPY	Range	106.48 ~ 109.73	101.19 ~ 112.23	105.99 ~ 109.85	104.00 ~ 107.52	99.00 ~ 112.00	102.00 ~ 112.00	102.00 ~ 115.00	105.00 ~ 115.00	105.00 ~ 115.00	104.46 ~ 112.40	99.00 ~ 112.23	102.00 ~ 115.00
	End of period	108.61	107.54	107.94	105.48	105.00	106.00	108.00	109.00	110.00	108.61	105.00	110.00
EUR/USD	Range	1.0879 ~ 1.1239	1.0688 ~ 1.1495	1.0727 ~ 1.1422	1.1185 ~ 1.2011	1.1300 ~ 1.2500	1.1200 ~ 1.2400	1.1200 ~ 1.2400	1.1300 ~ 1.2500	1.1400 ~ 1.2600	1.0879 ~ 1.1570	1.0636 ~ 1.2500	1.1200 ~ 1.2600
	End of period	1.1213	1.1031	1.1234	1.1721	1.1800	1.1700	1.1700	1.1800	1.1900	1.1213	1.1800	1.1900
USD/CAD	Range	1.2990 ~ 1.3300	1.2965 ~ 1.4511	1.3382 ~ 1.4211	1.2994 ~ 1.3646	1.3000 ~ 1.3800	1.2800 ~ 1.3700	1.2600 ~ 1.3600	1.2600 ~ 1.3600	1.2600 ~ 1.3600	1.2990 ~ 1.3631	1.2965 ~ 1.4511	1.2600 ~ 1.3700
	End of period	1.2990	1.4062	1.3595	1.3319	1.3300	1.3100	1.3000	1.3000	1.3000	1.2990	1.3300	1.3000
CAD/JPY	Range	80.16 ~ 85.00	74.53 ~ 84.55	75.01 ~ 81.64	77.62 ~ 81.58	74.00 ~ 84.00	75.00 ~ 85.00	78.00 ~ 88.00	78.00 ~ 88.00	79.00 ~ 89.00	80.41 ~ 91.10	74.00 ~ 84.00	75.00 ~ 89.00
	End of period	83.63	76.48	79.39	79.23	78.95	80.92	83.00	84.00	84.00	82.30	78.95	84.00
EUR/JPY	Range	117.08 ~ 122.65	116.08 ~ 122.87	114.43 ~ 124.43	120.27 ~ 127.08	119.00 ~ 129.00	120.00 ~ 130.00	122.00 ~ 132.00	124.00 ~ 134.00	126.00 ~ 136.00	115.87 ~ 127.50	114.43 ~ 129.00	120.00 ~ 136.00
	End of period	121.77	118.64	121.24	123.65	123.90	124.02	126.36	128.62	130.90	121.77	123.90	130.90
Oil price (WTI futures)		56.87	20.48	39.62	40.92	42.00	45.00	50.00	52.00	50.00	56.87	42.00	50.00