Weekly Update of U.S. Economy

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The Door for Another Rate Hike Is Still Open

Higher for Longer and Economy's Soft-Landing Scenario

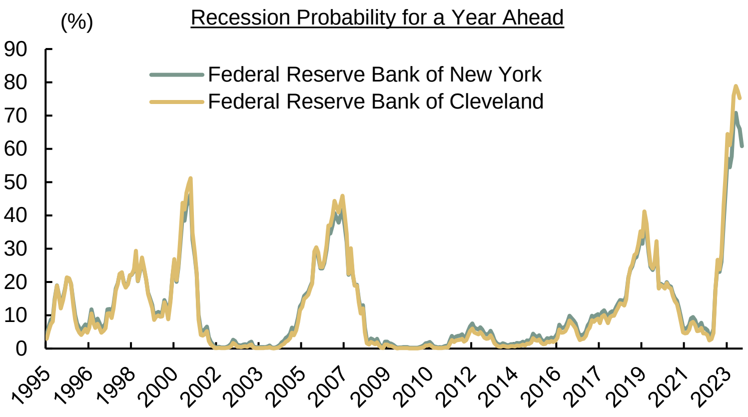
- The Federal Reserve Board (the "Fed") Chair Jerome Powell clearly attributed the solid state of the U.S. economy to the private sector's healthy balance-sheet condition. In fact, recent economic data indicates that the economy maintains resilience despite the tight monetary policy.
- However, it's true that sectors that are sensitive to interest-rate fluctuations, such as the housing market, are under downward pressure. Existing home sales fell for the third consecutive month in August, reversing all the rebound made in the first half of this year. In fact, the downward pressure on the housing market is not only caused by rising interest rates, but also by the lack of inventory, which reduces potential purchasing motivation.
- In terms of whether the U.S. economy can achieve a soft landing going forward, in addition to the trajectory of prices as they converge to the 2% target, the extent to which consumer spending continues to grow is becoming increasingly important.
- Despite the pressure on major auto makers to cut jobs, the number of weekly jobless claims remains low. This is one factor that has encouraged the Fed to prolong its "higher for longer" policy.
- At the Federal Open Market Committee (FOMC) meeting this week, the members unanimously decided to maintain the policy interest rate—the target range for the federal funds rate—at 5.25%-5.50%.
- The quarterly updated economic outlook (the Summary of Economic Projections, or SEP) was clearly revised upwards. The policy statement was even revised upward based on the actual state of the economy. This may have come as a surprise to those who were concerned about when the Fed would start lowering interest rates due to the easing of inflationary pressures and the slowing pace of employment growth as early as 2024.

Fed Hints at Neutral Rate While Showing Hawkish View on Economy

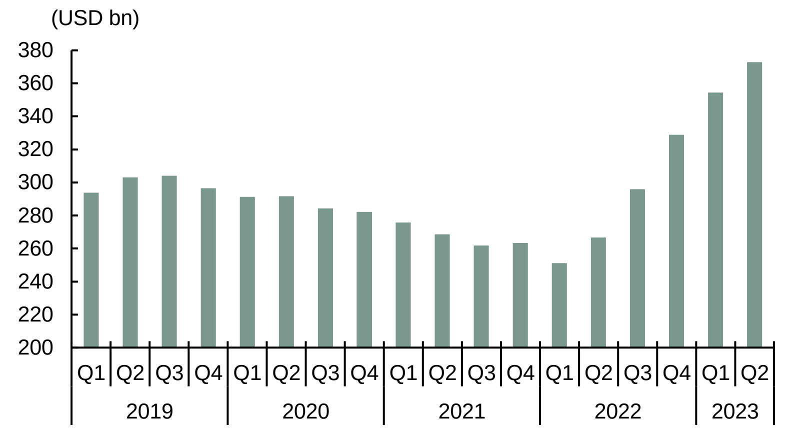
- The core Personal Consumption Expenditures deflator was revised downward from 3.9% in 2023 to 3.7%, but remained unchanged at 2.6% in 2024, and slightly revised upward to 2.3% in 2025 from the previous 2.2%. Importantly, this implies that Fed officials expect to see a stable return to the 2% target only after the second half of 2025.
- Meanwhile, there are growing concerns that a resurgence in crude oil prices will be a factor in delaying the return of the inflation rate to the 2% target. Crude oil prices increased to a near 10-month high this week on a tighter supply outlook and optimism of the Organization of the Petroleum Exporting Countries (OPEC) over the resilience of energy demand in global economies.
- At present, it is hard to believe that the overall inflation rate will continue to accelerate again due to the rise in oil prices alone. Rather, given the strong elasticity of consumption to increases in gasoline prices, we should think that rising resource prices will have a negative effect on the U.S. economy, which relies on personal consumption.
- The action of the Fed is still data-dependent. When considering how realistic it is to raise interest rates again for this year, we need to examine where the current actual policy interest rate is relative to the interest-rate level that is considered neutral from the perspective of the economy and prices. If even a rate hike of more than 5% is not enough to reach the neutral level, further rate hikes will become more realistic. On the other hand, if the current interest rate has already significantly exceeded the estimated neutral rate, then Chair Powell's bullish comments can be interpreted as nothing more than an announcement aimed at calming inflation expectations, implying there will be no more interest-rate hikes this year.
- At the post-meeting press conference, Chair Powell made brief comments about the neutral interest rate. This is evidence that banks are beginning to gain confidence that the policy interest rate has achieved the terminal level.

The Door for Another Rate Hike Is Still Open (continued)

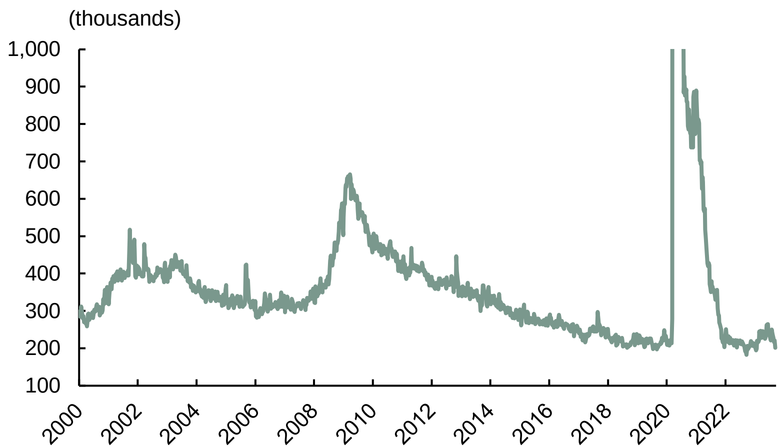
There is growing divergence between the Fed and market participants on expectations for a recession.



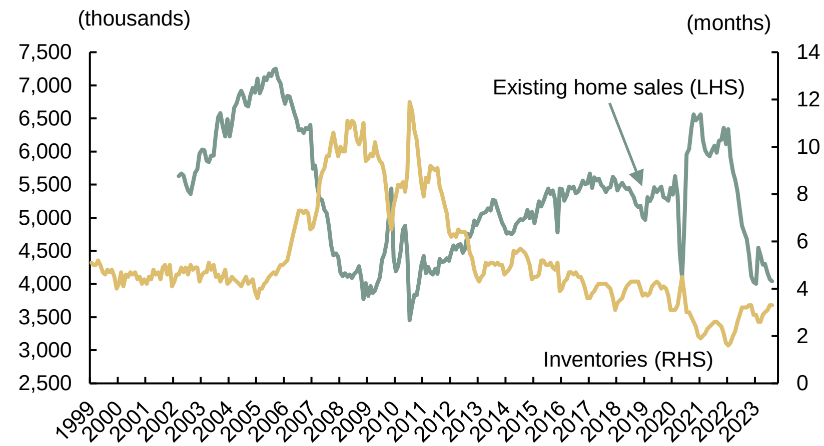
The U.S. corporate sector's interest payments have been increasing at a rapid pace.



Weekly initial jobless claims declined to 201,000 during the week ended September 16.



August existing home sales continued to decrease for the third consecutive month as a lack of inventories and high mortgage rates discouraged potential buyers.



Sources: Federal Reserve Bank of New York, Federal Reserve Bank of Cleveland, Bureau of Economic Analysis, Bureau of Labor Statistics, National Association of Realtors

SMBC Economy and Rates Forecast

		2022			2023				2024				2021	2022	2023	2024
		Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4				
U.S.	Real GDP (saar)	-0.6	3.2	2.6	2.0	2.1	2.5	1.2	0.6	1.0	1.2	1.7	6.0	2.1	2.1	1.2
	Inflation rate (YoY)	5.0	5.0	4.8	4.7	4.4	4.0	3.6	3.0	2.7	2.6	2.5	3.3	5.0	4.2	2.7
	Jobless rate	3.6	3.6	3.6	3.5	3.6	3.4	3.6	3.9	4.1	4.2	4.3	5.4	3.7	3.7	4.4
Euro area	Real GDP (qoq)	0.8	0.4	-0.1	0.0	0.3	0.2	0.1	0.2	0.3	0.3	0.2	5.3	3.3	0.6	0.9
	Inflation rate (YoY)	8.0	9.3	10.0	8.0	6.2	4.8	3.2	3.1	2.9	2.7	2.5	2.6	8.4	5.6	2.8
	Jobless rate	6.7	6.7	6.7	6.6	6.6	6.6	6.7	6.8	6.8	6.9	6.9	7.7	6.7	6.6	6.9
Japan	Real GDP (saar)	5.6	-1.5	0.2	3.7	6.0	0.9	0.9	0.9	0.9	1.1	0.7	2.3	1.0	1.5	1.0
	Inflation rate (YoY)	2.1	2.7	3.8	3.5	3.2	3.0	2.5	3.0	2.8	2.5	2.1	-0.2	2.3	3.0	2.6
	Jobless rate	2.6	2.5	2.5	2.6	2.5	2.4	2.4	2.3	2.3	2.3	2.3	2.8	2.6	2.4	2.3
China	Real GDP(YoY)	0.4	3.9	2.9	4.5	6.3	4.8	5.5	4.5	5.0	5.1	5.1	8.4	3.0	5.3	4.9
	Inflation rate (YoY)	2.2	2.8	1.8	1.3	0.2	0.0	0.6	1.1	1.5	1.8	2.0	0.8	1.7	0.5	1.6
	Jobless rate	5.8	5.4	5.6	5.5	5.2	5.3	5.2	5.1	5.0	5.0	5.0	5.1	5.1	5.3	5.0

Rates		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
U.S.	FF target range	4.25 ~ 4.50	4.75 ~ 5.00	5.00 ~ 5.25	5.25 ~ 5.50	5.25 ~ 5.50	5.25 ~ 5.50	5.00 ~ 5.25	5.00 ~ 5.25	4.75 ~ 5.00	4.25 ~ 4.50	5.25 ~ 5.50	4.75 ~ 5.00
	2yr UST	3.43	4.03	4.90	5.00	5.00	5.00	4.75	4.75	4.75	3.43	5.00	4.75
	10yr UST	3.87	3.47	3.84	4.50	4.20	4.00	3.90	4.00	4.00	3.87	4.20	4.00
Germany	ECB refi rate	2.50	3.50	4.00	4.25	4.25	4.25	4.25	4.00	3.75	2.50	4.25	3.75
	ECB depo rate	2.00	3.00	3.50	3.75	3.75	3.75	3.75	3.50	3.25	2.00	3.50	3.25
	2yr Schatz	2.50	2.68	3.20	3.20	3.00	2.80	2.50	2.40	2.30	2.50	3.00	2.30
	10yr Bunds	2.20	2.29	2.39	2.30	2.30	2.30	2.20	2.10	2.10	2.20	2.30	2.10
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	0.04	-0.06	-0.07	0.10	0.15	0.20	0.30	0.30	0.30	0.04	0.15	0.30
	10yr JGB	0.42	0.35	0.40	0.65	0.75	0.80	0.90	0.90	0.90	0.42	0.75	0.90
China	Policy rate	2.75	2.75	2.65	2.50	2.40	2.40	2.40	2.40	2.40	2.75	2.40	2.40
	2yr gov bond	2.39	2.41	2.11	2.05	2.05	2.08	2.15	2.25	2.35	2.39	2.05	2.35
	10yr gov bond	2.83	2.85	2.64	2.64	2.45	2.50	2.55	2.60	2.65	2.83	2.45	2.65

Source: SMBC

SMBC FX Forecast

		2022	2023				2024				2022	2023	2024
		Q4	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4			
USD/JPY	Range	130.58 ~ 151.95	127.23 ~ 137.91	130.64 ~ 145.07	137.25 ~ 152.00	133.00 ~ 147.00	131.00 ~ 145.00	126.00 ~ 140.00	128.00 ~ 142.00	128.00 ~ 130.00	113.47 ~ 151.95	127.23 ~ 152.00	126.00 ~ 145.00
	End of period	133.00	132.86	144.31	145.00	140.00	138.00	133.00	135.00	135.00	131.12	140.00	135.00
EUR/USD	Range	0.9633 ~ 1.0735	1.0484 ~ 1.1033	1.0635 ~ 1.1095	1.0300 ~ 1.1300	1.0200 ~ 1.1200	1.0100 ~ 1.1100	1.0000 ~ 1.1000	1.0100 ~ 1.1100	1.0100 ~ 1.1100	0.9536 ~ 1.1495	1.0200 ~ 1.1300	1.0000 ~ 1.1100
	End of period	1.0705	1.0839	1.0909	1.0700	1.0600	1.0500	1.0500	1.0600	1.0600	1.0705	1.0600	1.0600
USD/CAD	Range	1.3275 ~ 1.3885	1.3291 ~ 1.3832	1.3151 ~ 1.3642	1.3110 ~ 1.3685	1.3000 ~ 1.4200	1.3000 ~ 1.4200	1.3000 ~ 1.4200	1.2800 ~ 1.4000	1.2700 ~ 1.3800	1.2477 ~ 1.3885	1.3000 ~ 1.4200	1.2700 ~ 1.4200
	End of period	1.3554	1.3516	1.3242	1.3431	1.3600	1.3500	1.3500	1.3400	1.3300	1.3554	1.3600	1.3300
CAD/JPY	Range	96.76 ~ 109.11	95.13 ~ 100.59	97.54 ~ 109.21	105.02 ~ 110.09	97.00 ~ 109.00	96.00 ~ 108.00	92.00 ~ 104.00	94.00 ~ 107.00	94.00 ~ 107.00	89.77 ~ 110.06	95.13 ~ 113.00	92.00 ~ 108.00
	End of period	96.76	98.28	109.04	110.09	103.00	102.20	98.50	100.75	101.50	96.76	97.80	92.48
EUR/JPY	Range	138.81 ~ 148.40	138.19 ~ 145.67	143.12 ~ 157.92	149.00 ~ 163.00	144.00 ~ 158.00	138.00 ~ 152.00	133.00 ~ 147.00	136.00 ~ 150.00	136.00 ~ 150.00	124.40 ~ 148.40	137.39 ~ 163.00	133.00 ~ 152.00
	End of period	140.41	144.01	157.43	155.15	148.40	144.90	139.65	143.10	143.10	140.41	148.40	143.10
Oil price (WTI futures)		82.64	75.99	73.67	80.00	82.00	82.00	76.00	77.00	78.00	98.74	77.92	78.25

Source: SMBC

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