

# Weekly Update of U.S. Economy

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# The End of Policy Tightening Is Not Yet in Sight

## FOMC Review

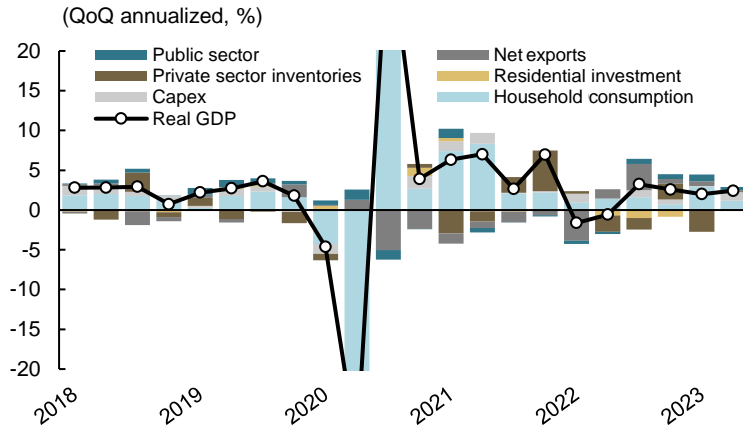
- On July 26, the Federal Open Market Committee (FOMC) unanimously decided to increase the policy interest rate—the target range for the federal funds rate—from 5.00%-5.25% to 5.25%-5.50%. Being accompanied by an augmented level of quantitative tightening, allowing redemption of securities held at a faster pace in September of last year, the Federal Reserve's (the "Fed") stance on overall monetary policy remained tight.
- The main focus of this week's meeting was to what extent the FOMC would show a willingness to raise interest rates further at the next and subsequent meetings. Given that there were no conspicuous downward revisions to the economic assessment, and that phrases such as "the Committee remains highly attentive to inflation risks" remained, there seems a fair chance that the Fed will continue its rate hikes.
- Compared to the Fed chair's remark last month that "at least two rate hikes would be appropriate this year," these comments sounded like a somewhat more conservative statement about the possibility of further interest-rate hikes. However, it rather implies the Fed's intention to wait and see the cumulative impact of its monetary tightening on business activities. In addition, the period until the next FOMC meeting in September is relatively long, with two months' worth of employment statistics and price indicators to be released, and from August 24 to 26, officials from major central banks and academics will discuss policies when they meet at the Jackson Hole Economic Policy Symposium.
- If the inflation indicators for the next two months display a steady slowdown, even if the policy interest rate remains unchanged at 5.25%-5.50%, the real interest rate (nominal policy interest rate – inflation rate) will rise and monetary policy will be tightened further. In the meantime, if Fed officials gain confidence that the slowdown in inflation is not temporary and that upside risks to prices have eased, the Fed will make a formal statement about it and decide how long it will continue to tighten policy. The current situation is still one step short of that scenario.

## The Economy Appears to Remain Within Range of a Soft Landing

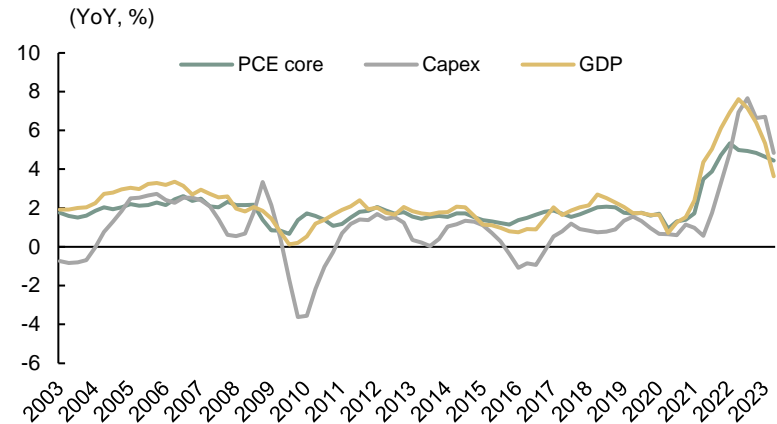
- The real GDP growth rate for the April-June quarter of this year, which was announced the day after the FOMC meeting, was 2.4% on an annual basis from the previous quarter, slightly accelerating from 2.0% in the January-March quarter. Since the period after the economy temporarily sank into consecutive negative growth during late 2022 and early 2023 due to supply constraints, the economy has maintained a growth trend that exceeds the potential growth rate despite the ongoing policy tightening. A limited impact of tight monetary policy on final demand would give the Fed a rationale for continuing its tightening policy for the long term.
- The real interest rate—the federal funds rate minus the personal consumption expenditures (PCE) deflator—is increasing at a rapid pace since it rose into positive territory. While the burden of interest rates is expected to weigh heavily on corporate activity, the private sector has not expanded its leverage over the past few years. The low sensitivity to interest-rate rises on the part of corporate investment, consumer durable goods consumption and housing investment will make it harder for Fed officials to decide when they should consider tapering their tight policy.
- Corporate bond refinancings will increase, with high yield bonds accounting for nearly half, according to an analysis by Standard and Poor's. However, until that stage is reached, the Fed has time to confirm whether the accumulation of tightening policies to date will curb economic activity and further solidify the declining trend in prices.
- Real disposable income for individuals grew 2.5% during April-June, continuing steady growth after the sharp increase in January-March (+8.5%). Personal consumption is growing within the range of disposable income, and the savings rate rose slightly to 4.4% from 4.3% in the previous quarter. There is no noticeable heating up in consumption, and it seems unlikely that the cumulative effect of monetary tightening will suddenly force a significant contraction. Although it depends on future developments in asset prices, we believe that the economy is still within range of a soft landing.

# The End of Policy Tightening Is Not Yet in Sight (continued)

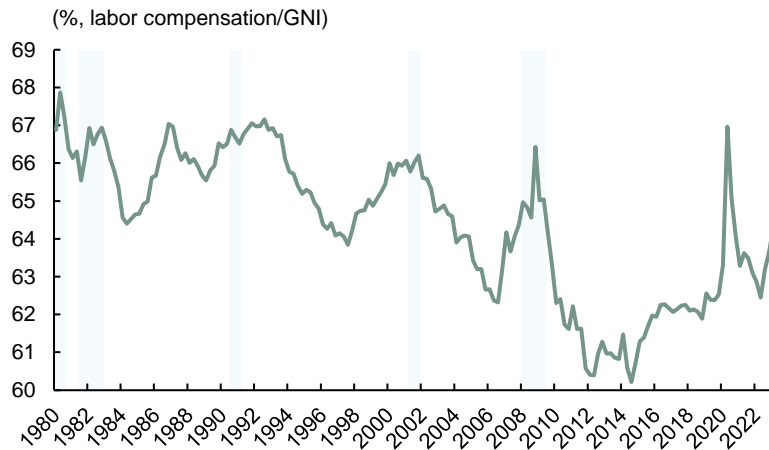
The real GDP rate grew by 2.4% quarter-over-quarter annualized, indicating the limited impact of the rise in real interest rates so far.



The GDP deflator slowed its pace of growth after the peak in 2022.



Employees have been receiving a considerable portion of national income through labor compensation.



The real interest policy rate (federal funds target rate – PCE deflator) is increasing rapidly within positive territory.



Source: Bureau of Economic Analysis

# 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	2.4	-0.8	0.6	0.9	1.4	1.8	2.2	5.9	2.2	1.4	1.0
	Inflation rate (YoY)	5.0	5.0	4.8	4.7	4.4	4.2	3.9	3.2	2.8	2.5	2.2	3.3	5.0	4.4	2.7
	Jobless rate	3.6	3.6	3.6	3.5	3.5	3.7	4.3	4.6	4.7	4.7	4.6	5.4	3.7	3.7	4.7
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	0.4	2.7	1.7	1.0	0.9	0.9	0.8	0.8	0.7	2.3	1.1	1.0	0.9
	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	3.1	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	1.4	1.5	1.6	1.9	2.0	2.0	0.8	1.7	1.1	1.9
	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	4.75	5.00	5.25	5.25	5.00	4.75	4.50	4.25	4.25	5.25	4.25
		~	~	~	~	~	~	~	~	~	~	~	~
	2yr UST	4.50	5.00	5.25	5.50	5.50	5.25	5.00	4.75	4.50	4.50	5.50	4.50
	10yr UST	3.43	4.03	4.90	4.20	4.00	3.80	3.60	3.40	3.20	3.20	4.00	3.20
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	2.55	2.55	2.55	2.55	2.55	2.55	2.75	2.55	2.55
	2yr gov bond	2.40	2.41	2.11	2.16	2.24	2.32	2.39	2.49	2.59	2.40	2.24	2.59
	10yr gov bond	2.83	2.85	2.64	2.64	2.69	2.74	2.79	2.84	2.89	2.83	2.69	2.89

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	127.23	130.64	128.00	125.00	121.00	119.00	116.00	116.00	113.47	125.00	116.00
		~ 151.95	~ 137.91	~ 145.07	~ 147.00	~ 138.00	~ 135.00	~ 133.00	~ 130.00	~ 130.00	~ 151.95	~ 147.00	~ 135.00
	End of period	133.00	132.86	144.31	137.00	133.00	130.00	128.00	126.00	123.00	131.12	133.00	123.00
EUR/USD	Range	0.9633	1.0484	1.0635	1.0300	1.0200	1.0100	1.0000	1.0100	1.0100	0.9536	1.0200	1.0000
		~ 1.0735	~ 1.1033	~ 1.1095	~ 1.1300	~ 1.1200	~ 1.1100	~ 1.1000	~ 1.1100	~ 1.1100	~ 1.1495	~ 1.1300	~ 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	1.3291	1.3151	1.3000	1.3000	1.3000	1.3000	1.2800	1.2700	1.2477	1.3000	1.2700
		~ 1.3885	~ 1.3832	~ 1.3642	~ 1.4200	~ 1.4200	~ 1.4200	~ 1.4200	~ 1.4000	~ 1.3800	~ 1.3885	~ 1.4200	~ 1.4200
	End of period	1.3554	1.3516	1.3242	1.3500	1.3600	1.3500	1.3500	1.3400	1.3300	1.3554	1.3600	1.3300
CAD/JPY	Range	96.76	95.13	97.54	95.00	91.00	90.00	88.00	88.00	85.00	89.77	91.00	85.00
		~ 109.11	~ 100.59	~ 109.21	~ 108.00	~ 103.00	~ 102.00	~ 100.00	~ 100.00	~ 98.00	~ 110.06	~ 109.21	~ 102.00
	End of period	96.76	98.28	109.04	101.48	97.80	96.30	94.81	94.03	92.48	96.76	97.80	92.48
EUR/JPY	Range	138.81	138.19	143.12	144.00	136.00	131.00	128.00	126.00	123.00	124.40	136.00	123.00
		~ 148.40	~ 145.67	~ 157.92	~ 158.00	~ 150.00	~ 145.00	~ 142.00	~ 140.00	~ 137.00	~ 148.40	~ 158.00	~ 145.00
	End of period	140.41	144.01	157.44	146.59	140.98	136.50	134.40	133.56	130.38	140.41	140.98	130.38
Oil price (WTI futures)		82.64	75.99	73.58	75.00	80.00	80.00	75.00	77.00	78.00	98.74	76.37	77.50

Source: SMBC