Federal Reserve signals tighter policy ahead amid strong growth and higher inflation

- Unemployment fell to 5.8% in May, the lowest since March 2020 amid easing restrictions and a pickup in hiring.
- The US economy added 559K jobs in May, from an upwardly revised 278K in April, slightly below expectations.
- Wage growth surged to 2% in May due to the base effect from the dip in May 2020 and a tighter labor market.
- Inflation rose to 5% in May, the highest since 2008 on higher commodity prices, supply constraints.
- The Fed kept the policy rate at a range of 0-0.25% but signaled the possibility of two rate hikes by end-2023.
- The USD index rose in June, following the Fed’s hawkish shift, and confirming recovery expectations.

Chart 1: Real GDP growth

GDP grew by an annualized 6.4% in 1Q21, in line with expectations following a 4.3% expansion in 4Q20.

Source: Refinitiv

Chart 2: Unemployment rate

Unemployment fell to 5.8% in May, the lowest since March 2020 (from 6.1% in Apr.) amid easing restrictions and a pickup in hiring.

Source: Refinitiv

Chart 3: Non-farm payrolls (jobs)

The economy added 559K jobs in May, from an upwardly revised 278K in April but below market expectations of 650K.

Source: Refinitiv

Chart 4: Wage growth

Wage growth surged to 2% in May due to the base effect from the dip in May 2020 and a tighter labor market.

Source: Refinitiv
Inflation continued to rise, reaching 5% in May, the highest since 2008 on reopening pressures and year-on-year base effects.

Retail sales growth ex-autos fell to 26% in May from a historical high of 43% in April, and should ease further in coming months.

Chart 5: Consumer price inflation

(\% \text{y/y})

Chart 6: Commercial and industrial loans

(\% \text{y/y})

Chart 7: Retail sales

(\% \text{y/y})

Chart 8: Existing home sales and housing starts

(million units)

Chart 9: Business activity surveys

(index)

Chart 10: US government spending and revenues

(\% \text{y/y} \text{ of } 12 \text{ month cumulative totals})

Inflation continued to rise, reaching 5% in May, the highest since 2008 on reopening pressures and year-on-year base effects.

Core loan growth fell sharply into negative territory at -16% in May, a historical low, due to the exceptionally high base levels of 2020.

Retail sales growth ex-autos fell to 26% in May from a historical high of 43% in April, and should ease further in coming months.

Housing starts rose 3.6% m/m to 1.57 million as low interest rates, recovery optimism continued to fuel real estate demand.

The ISM manufacturing index edged up to 61.2 in May, from 60.7 in April as new orders rose in line with higher demand.

The 12-month fiscal deficit narrowed to $3.3 trillion in May as receipts rose on higher employment and an earlier tax deadline.

Source: Refinitiv

Source: Refinitiv

Source: Refinitiv

Source: Refinitiv
The Fed kept the policy rate unchanged at a range of 0-0.25% but signaled the possibility of two rate hikes by end-2023.

Source: Refinitiv

The US 10-year treasury yield remained low at 1.52% as of June 27, down 8 bps m/m, on continued government purchasing.

Source: Refinitiv

Futures markets probabilities of a rate hike in 2021 have fallen to zero as the Fed asserted that no hike is expected until 2023.

Source: Refinitiv

Federal reserve assets expanded to $8.1 trillion in June, but may begin to flatten off once QE tapering starts (maybe late 2021).

Source: Refinitiv

The S&P500 set a new record high, as vaccine progress and recovery prospects supported bullish sentiment.

Source: Refinitiv

The USD index rose in June, as the Fed shifted its stance, easing inflation concerns and confirming recovery expectations.

Source: Refinitiv
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