

US Macroeconomics

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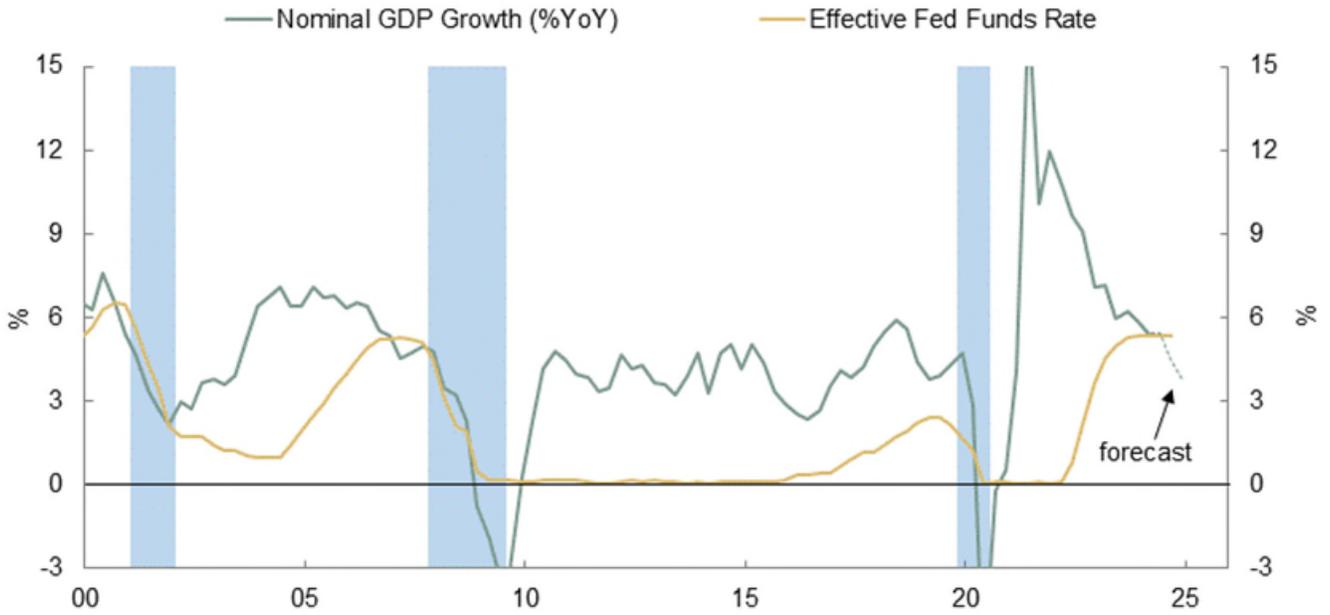
Q2 GDP Report Preview and Outlook

Q2 Preview: Next Thursday, the Bureau of Economic Analysis (BEA) releases its Q2 GDP report (July 25). Although the economy continues to slow from unsustainable post-pandemic highs, **key US growth metrics continued to increase at a healthy pace in Q2. We are forecasting 1.8% QoQar for real GDP growth and 2.0% for real PCE. We also see some upside risk to these figures considering the degree to which inflation relaxed in the second quarter** (CPI printed at 0.0% MoM and -0.1% for May and June respectively).

Although mostly in line with the consensus of economists at the time of this writing, the most notable departure comes from our below-consensus +2.4% QoQar / 2.6% YoY GDP Deflator forecast. **Softer than expected Q2 inflation implies higher real growth** (all else being equal). **Data related to consumer spending suggests a sturdy PCE print.** Quarterly retail sales grew at 2.2% annualized pace, while the *retail control* component (a direct input into PCE data) increased 3.3%. We expect real government spending to increase 1.8%, adding 30 basis points to GDP. However, we expect this to slow to near 1% YoY by yearend 2025 (down noticeably from Q1 2024's 3.9% YoY pace). Equipment investment was driven by solid quarterly growth in durable goods (+5.7% forecasted) and industrial production (+4.2%). Our full forecast table is included below.

H2 2024 Outlook: Although nominal GDP growth was roughly equal to the Fed funds rate in Q2, **the continued slowdown in inflation combined with sluggish productivity growth suggests to us that nominal GDP growth is likely to fall below the cost of borrowing in the second half of the year** (H2). This is a milestone that typically occurs in and around recessions, as illustrated on page 2. As a consequence of this H2 dynamic, system-wide leverage could increase as interest expense outpaces income growth. This is a dynamic that would explain the Fed's eagerness to cut even in the face of low unemployment and still above target inflation.

SMBC US GDP Forecasts (QoQar)	Q2 2024
GDP	1.8
PCE	2.0
Structures Investment	-1.3
Equipment Investment	5.1
Intellectual Property Products	4.3
Residential Investment	-3.0
Inventories*	48.1
Net Exports	9.3
Government	1.8



Source: BEA, Federal Reserve, Haver, SMBC Nikko

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