

Contributors

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Chart 1

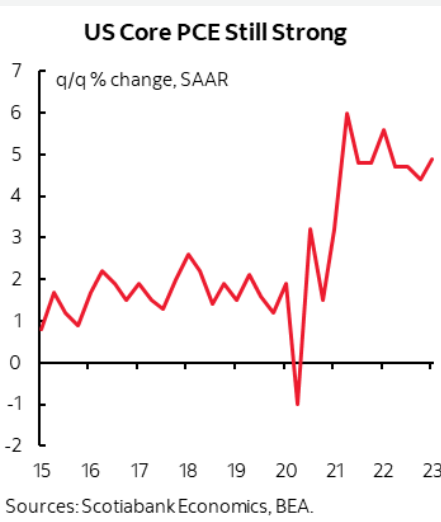
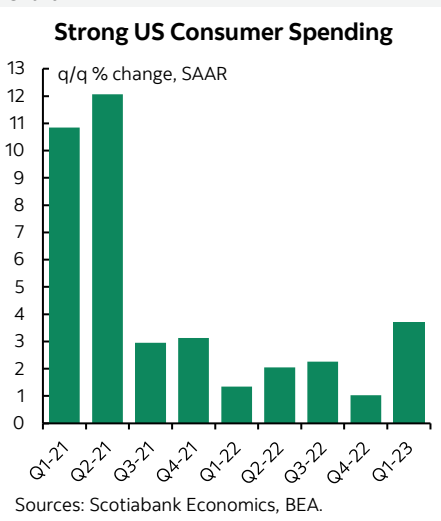


Chart 2



Strong US Consumers Continue to Drive Hot Inflation, Cementing a Fed Hike Next Week

- **Treasuries sell off...**
- **...in reaction to hotter than expected core PCE inflation**
- **A 25bps hike next week is a done deal with markets pricing part of another**
- **US GDP disappointed...**
- **...but not for the surmised reasons...**
- **...as US consumer spending was very strong...**
- **...with good reasons for continued consumer resilience**
- **US inventory positions remain healthy**
- **US initial jobless claims dip, remain range bound**

US GDP Q1 / core PCE, q/q % SAAR:

Actual: 1.1 / 4.9
 Scotia: 2.0 / 4.7
 Consensus: 1.9 / 4.7
 Prior: 2.6 / 4.4

Core inflation surprised higher and dominated GDP in terms of market attention as the yield on the 2-year Treasury climbed by 9bps and pricing for next Wednesday’s FOMC meeting inched closer to a full quarter point and terminal rate pricing moved up 3–4bps to price part of another quarter point hike at the June meeting. The S&P is shaking it off with a gain of 0.8% so far this morning as earnings and the consumer’s resilience are mattering more. GDP did indeed surprise lower, but not at all for the reasons that were the subject of much speculation over the last couple of days or so.

Core PCE inflation landed at 4.9% q/q at a seasonally adjusted and annualized pace in Q1. That is the strongest gain since 2022Q1 and maintains persistent pressure at elevated heights (chart 1). That gain exceeded consensus expectations for a 4.7% rise and picked up the pace from 4.4% in Q4. Why this happened is not clear but will be informed by tomorrow’s breakdown of the monthly figures when we’ll get March core PCE and possible revisions to prior months. Either my estimate for March core PCE of 0.3% m/m is too low and/or there were positive revisions to prior months because in the absence of such possibilities we should have gotten 4.7% q/q SAAR.

Headline US GDP growth slipped to 1.1% q/q SAAR but I wouldn’t get all twisted out of shape over it and for two broad reasons.

The first caution always applies to the first estimate for US GDP. It’s a guess in the absence of more complete data. There can be large revisions—up or down—in the second and third swings at the figures that incorporate more complete data sources especially on services.

The second caution is that the details were more constructive than the headline GDP disappointment. The feared disappointment in consumer spending after revisions to retail sales just did not materialize. Indeed, it’s quite the opposite as inflation-adjusted consumer spending grew 3.7% q/q SAAR for the most powerful gain since 2021Q2 (chart 2). That was enough to contribute 2.5 percentage points to the 1.1% rise in GDP on a weighted contributions basis. Goods consumption added 1.5 ppts of that contribution and services added an extra 1%.

Why is the US consumer so strong? I'll repeat past arguments about how much stronger their finances are in this hike cycle than prior ones such as into the GFC. Debt service payments are hovering around record lows as a share of disposable income; they will rise as higher rates pass through revolving and nonrevolving loans, but still remain comfortably low. Americans locked in generational lows in mortgage rates when the nominal 30-year rate fell to 2.9% and was basically free in real terms. The US household debt-to-income ratio is at its lowest in over two decades and their cash horde remains elevated as consumers squirreled away stimulus and supports.

The flipside to consumer resilience in this cycle is that they are better able to take rate hikes and perhaps this means a bias toward continued tightening.

Chart 3 shows the trend in quarterly GDP growth.

Chart 4 shows the weighted contributions by component to Q1 GDP growth. At the top of the list were the two consumption items.

At the bottom of the list is that inventories dragged 2.3 ppts off of headline GDP for the biggest drag effect since 2021Q1. This partly reflects the sheer strength of consumer spending that depleted inventories.

Imports subtracted 0.4 ppts because they increased by 2.9% q/q SAAR in a partial reversal of the prior quarter's decline. This may reflect efforts to restock inventories with imported content. A rise in imports is a drag on GDP growth given that the accounting treats it as a leakage effect out of the economy.

Exports added 0.5 ppts in weighted terms. Government spending added 0.8 ppts especially federal (0.5) but state/local gov'ts added 0.3.

Investment was a fairly neutral contributor and only subtracted -0.1 ppts with generous rounding. Nonresidential investment added 0.1, residential investment subtracted just 0.2.

Chart 5 shows the history of revisions to US GDP growth to buttress the earlier point. Sometimes they are small and sometimes the revisions can be multiple percentage point swings.

Charts 6–14 depict the state of US inventories overall (chart 6) and by retail category across the remaining charts. I don't see reason for alarm across the suite of measures particularly given the greater resilience in household finances during this cycle.

In separate releases, US weekly initial jobless claims dipped a touch to 230k from 246k and seems to be of decent quality with no states estimated (ie: hard submissions). That keeps them range bound at comfortably low levels consistent with ongoing job growth. Pending home sales fell by 5.2% m/m SA in March but was largely ignored by markets in relation to the focus upon inflation.

Chart 3

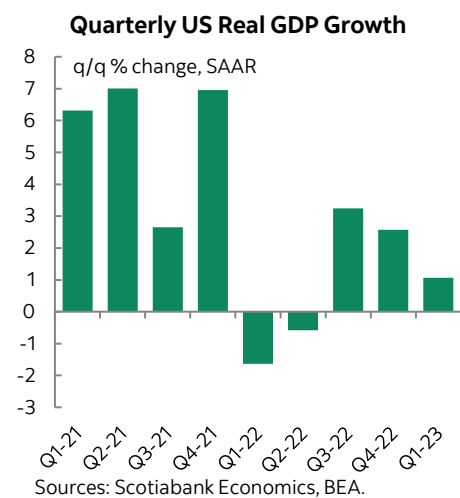


Chart 4

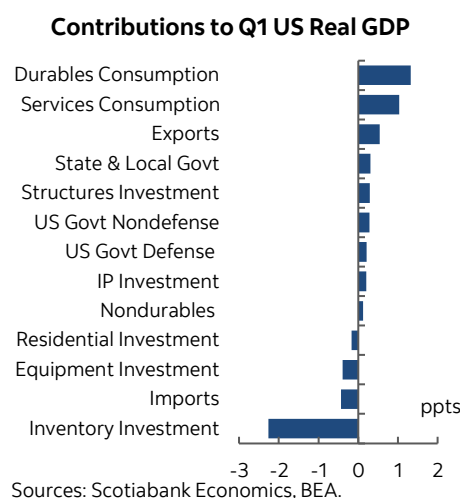


Chart 5

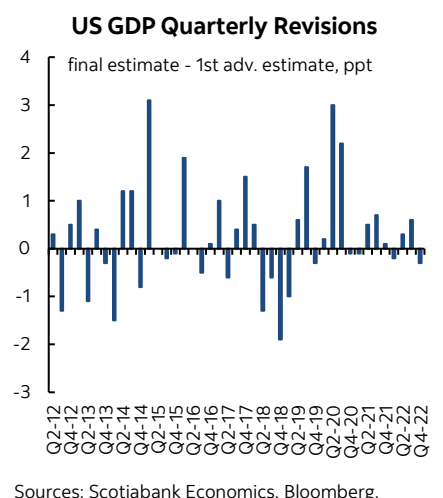
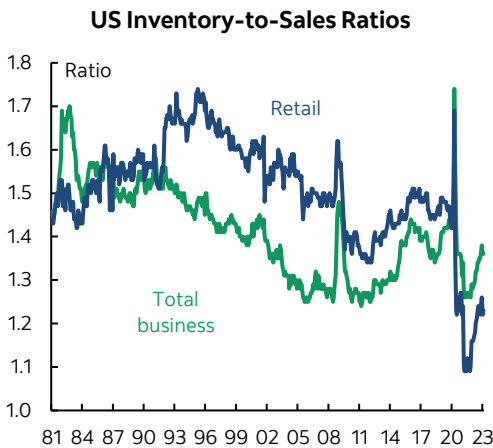
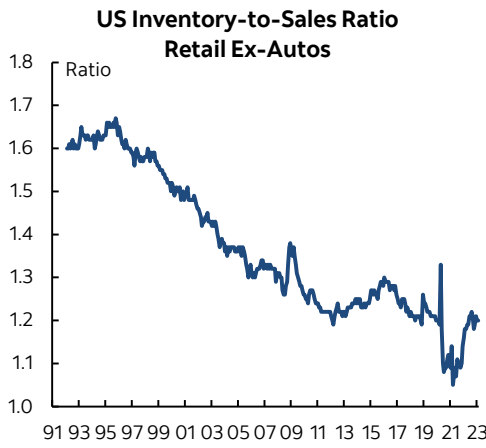


Chart 6



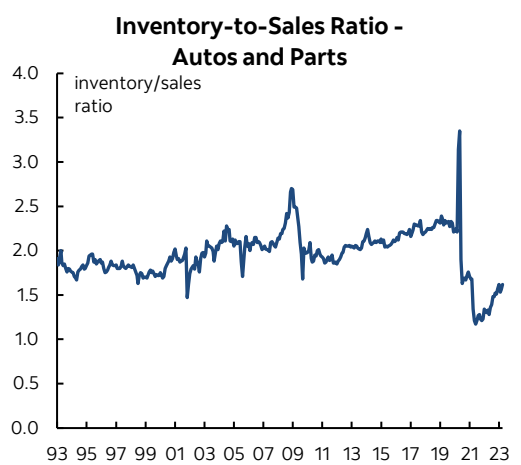
Sources: Scotiabank Economics, US Census Bureau.

Chart 7



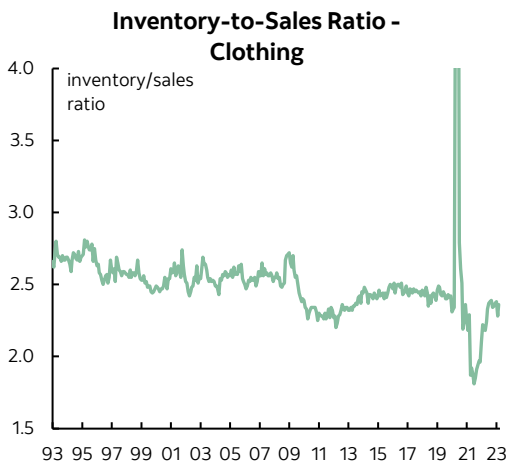
Sources: Scotiabank Economics, US Census Bureau.

Chart 8



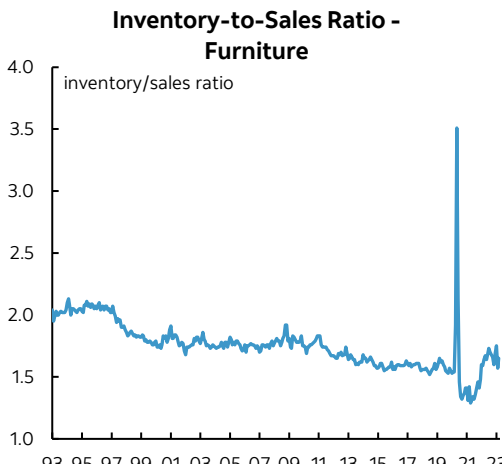
Sources: Scotiabank Economics, Census Bureau.

Chart 9



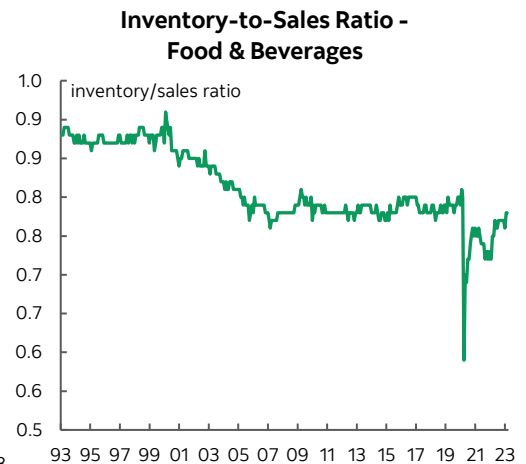
Sources: Scotiabank Economics, Census Bureau.

Chart 10



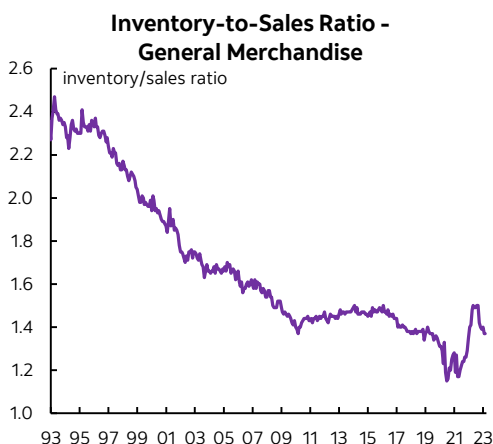
Sources: Scotiabank Economics, Census Bureau.

Chart 11



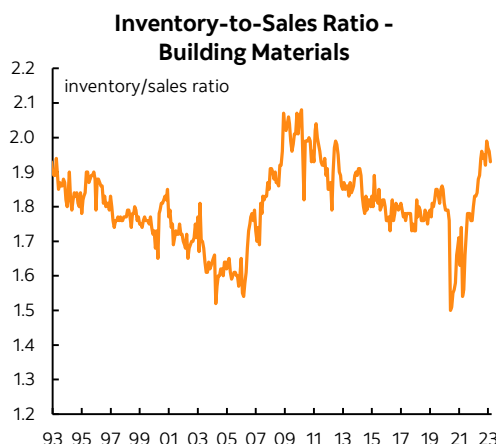
Sources: Scotiabank Economics, Census Bureau.

Chart 12



Sources: Scotiabank Economics, Census Bureau.

Chart 13



Sources: Scotiabank Economics, Census Bureau.

Chart 14



Sources: Scotiabank Economics, Census Bureau.

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