

## US data flow backs the case for 75bp

It has been a volatile week for interest rate expectations ahead of the July 27th FOMC meeting, but the final sets of data showing reasonable retail sales yet falling inflation expectations, lower import price inflation and the second consecutive fall in manufacturing suggests a 75bp hike is the most likely outcome



Final economic data sets indicate the Fed is likely to hike rates by 75bp on July 27

### Inflation fears show signs of easing

There has been growing speculation over a possible 100bp hike from the Fed later this month following the 9.1% inflation print and the Bank of Canada opting for a surprise 100bp hike. However, we have had quite an array of US numbers this morning, which fit with the notion that a 75bp hike is the most likely outcome of the July 27th FOMC meeting.

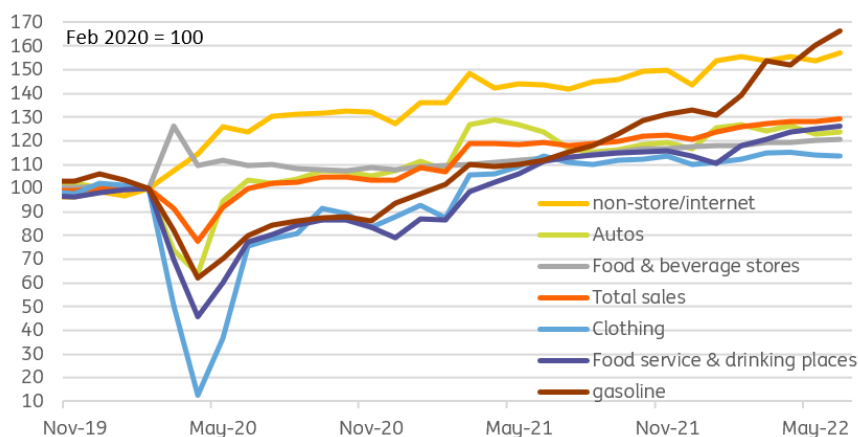
The University of Michigan sentiment index is not always as closely followed as other indicators, but the surprise jump in its inflation expectations series last month was seen as the catalyst for the Federal Reserve to opt for a 75bp hike at the June FOMC meeting. Up until that point 50bp was the Fed's forward guidance, but soon after the number was published journalists received a call to say momentum was shifting.

Today's report shows both the year ahead and 5-10Y inflation expectations headed lower in July, the former to 5.2% from 5.3% and the latter to 2.8% from 3.1% (consensus 5.3% and 3% respectively). These are important developments as they suggest households are looking through the current period of inflation and have confidence that it will head lower with lower gasoline

prices the likely instigator. If this holds then the risk of second-round inflation via higher wages will wane, meaning the Fed will have less work to do.

With regards to inflation, June import price inflation numbers were a lot softer than expected, coming in at 0.2%MoM/10.7%YoY versus 0.7%/11.4% expected. More evidence that dollar strength is acting as a brake on inflation by reducing some pipeline price pressures.

## Retail sales by component



Source: Macrobond, ING

## Still spending for now

Consumer confidence did improve marginally, but remains at incredibly weak levels as recession fears mount. Nonetheless, US retail sales still managed to rise 1% month-on-month in June at the headline level (consensus 0.9%) and there was a 0.2 percentage point upward revision to May's growth rate to -0.1% MoM from -0.3%. Gasoline was the key area of strength, rising 3.6% on higher prices, but there were also decent increases in furniture (1.4%) and non-store retail (2.2%) while eating and drinking out increased 1%.

The core "control" figure which excludes the volatile food, gasoline, autos and building materials rose 0.8% MoM versus the 0.3% consensus, but there were a net 0.3pp downward revisions to May's growth rate. So on balance the retail sales report is a little bit better than expected, especially given evidence from some of the credit card providers that suggested sales were not looking great.

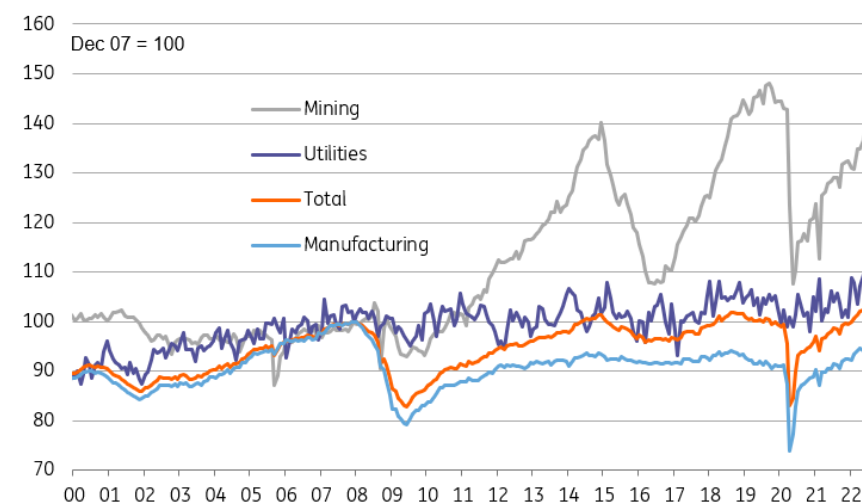
It's important to remember that this is a dollar value figure so higher prices are boosting the number. Adjusted for inflation "real" growth will be close to zero overall in June. However, it is important to remember that consumer spending is much broader than retail sales alone. Households are spending more on leisure and hospitality as spending reorientates back towards services and away from goods. This still has a long way to go with retail sales set to underperform broader spending trends over coming quarter – we look for it to drop back from the current 48% of total consumer spending and move towards pre-pandemic levels of 43% of total spending.

For now though households appear to be willing to run down some of the savings accumulated through the pandemic and we look for real consumer spending to rise 0.2% MoM in June leaving 3Q annualized consumer spending that will form part of the GDP report up 1.2% annualized. If correct this will be the weakest figure since the 33.4% plunge in 2Q 2020.

## Manufacturing softness intensifies

Meanwhile industrial production was disappointing. Output fell 0.2% in June (consensus +0.1%) while May's figure was revised down a tenth to 0.1% MoM. Surprisingly it was manufacturing that was the weak point, falling 0.5% MoM for the second consecutive month (autos down 1.5%, machinery down 1.1%). Utilities fell 1.4%, which is weather driven while mining rose 1.7%.

## Industrial production components



Source: Macrobond, ING

## 75bp on July 27th

Markets had been getting close to pricing in a full 100bp hike from the Federal Reserve on July 27, but comments from two of the most notable hawks yesterday (James Bullard and Chris Waller) had seen doubts emerge. While all options were on the table, they indicated they wanted to see strong numbers between now and July 27th to convince them that 75bp wasn't the better option at this stage. Today's numbers on balance don't appear to be strong enough to make that case and if they can't be convinced then it is unlikely that many others on the FOMC will be. Housing data is on the schedule for next week, but rising mortgage rates and falling mortgage applications suggest the numbers won't be strong enough to alter the story. We still favour a 75bp move on July 27th with 50bp hikes in September and November and a final 25bp move in December.

### Author

**James Knightley**

Chief International Economist, US

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial

instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit [www.ing.com](http://www.ing.com).