

US economy expands 3%

The strong growth figure should keep the Fed on track for a December hike but its inflation, not growth, that is still the big headache for policymakers



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The US economy is continuing to motor along at a fair pace. That's according to the first third-quarter growth estimate which has come in better than expected at 3%.

Straight away though, it's worth saying that much of this can be put down to a sizable inventory rebuild. That lifted growth by 0.7ppt and of course doesn't tell us an awful lot about the underlying economic trend, a task also complicated by the effect of the recent hurricanes.

But does any of this matter for the Fed? For a long time now, policymakers have seemed pretty comfortable about growth. Instead, inflation is still the far bigger conundrum

That said, it's clear the US economy enjoyed another quarter of solid consumer spending,

supported by the tight labour market. Business spending was also strong, backing-up what we've seen in recent business surveys (many of which are now at 10+ year highs).

But does any of this matter for the Fed? Well, for a long time now, policymakers have seemed pretty comfortable about growth. Instead, with core PCE having fallen back significantly over recent months, inflation is still a far bigger conundrum. The core view on the committee is still that much of the recent dip is down to temporary factors, and with pipeline pressures building given higher commodity prices and the weaker dollar, we also suspect inflation will recover over the next few months.

But until it does, markets will remain sceptical – although inflation is not the only reason why markets are wary of the Fed's rate hike ambitions. The Fed Chair saga, which looks set to reach its finale next week, is still a big uncertainty. Lingering concerns about another debt-ceiling showdown in December right around the time of the Fed's meeting, are also a risk. Until these hurdles are crossed markets will most likely continue to take the Fed dots with a certain pinch of salt.

Even with these headwinds though, we still think the Fed is on course to hike again in December and twice more in 2018

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