Daiwa Capital Markets

U.S. Economic Comment

- PCE price index: in line with expectations; sticky in upper 2's although not an impediment to near-term rate cut narrative
- Views from the FOMC: Waller strongly endorses a September cut
- Q3 GDP update: consumer spending adjusted higher on July data; net exports poised to be drag on growth

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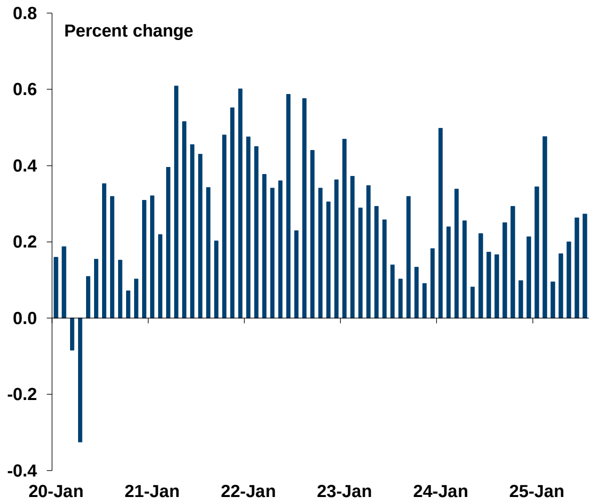
July Inflation -- More of the Same

With expectations for the July reading for the price index for personal consumption expenditures dialed in ahead of today's release on account of previously published data on the CPI and PPI, the results appeared as something of an afterthought. The headline price index rose 0.2 percent and the core 0.3 percent (chart, below left), consistent with year-over-year advances of 2.6 percent for the headline and 2.9 percent for the core. The advance in the headline was only marginally faster than that for June (+2.596 percent versus +2.565 percent), although the year-over-year pace for the core index was approximately 0.1 percentage point faster than that in the prior month. At best, the latest results suggest a sideways move in consumer prices with still-scant evidence of meaningful pressure from tariffs. In light of the current static state, and views held by seemingly many at the Fed that tariffs will have only a passing impact on inflation, officials have already signaled that the near-term path of the federal funds rate is lower – with the next change likely to occur at the September 16-17 FOMC meeting.

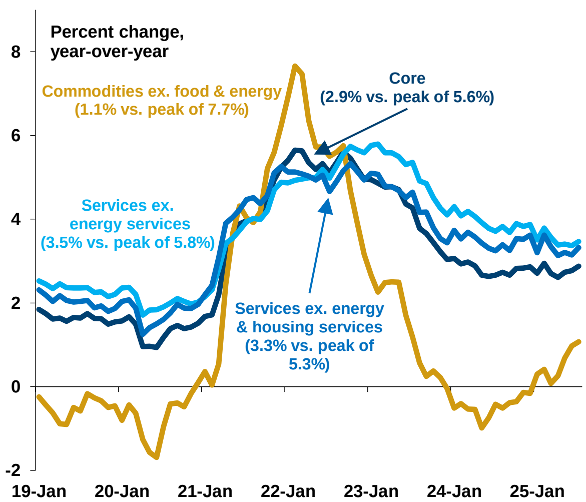
Interestingly, core goods prices were again well behaved in July despite ongoing concern about the impacts of import duties on consumer prices. Indeed, while the year-over-year change core goods rose 0.1 percentage point to 1.1 percent – the fastest increase since July 2023 and a clear signal that disinflation in goods prices has ended – the component was unchanged month-over-month (chart, below right). As in other recent months, hints of tariff-related price increases were present (e.g., prices of tools jumped 1.2 percent, the fourth consecutive brisk advance), but changes in other areas remained subdued (e.g., new motor vehicle prices rounded up to no change after back-to-back declines and are up only 0.5 percent year-over-year). Moreover, we suspect that softening consumer demand will further constrain firms' abilities to push higher costs onto consumers, a consideration that likely underpins policymakers' apparent confidence that second-round inflationary effects from tariffs carry a reasonably low probability of being realized.

Core PCE Price Index



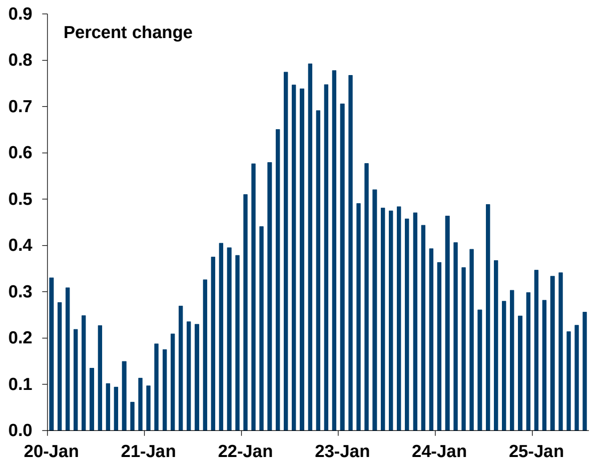
Source: Bureau of Economic Analysis via Haver Analytics

Decomposition of Core PCE



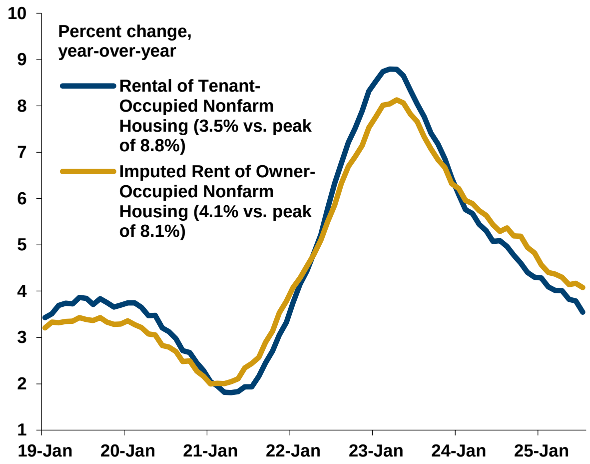
Source: Bureau of Economic Analysis via Haver Analytics

PCE Price Index: Primary Rent



Source: Bureau of Economic Analysis via Haver Analytics

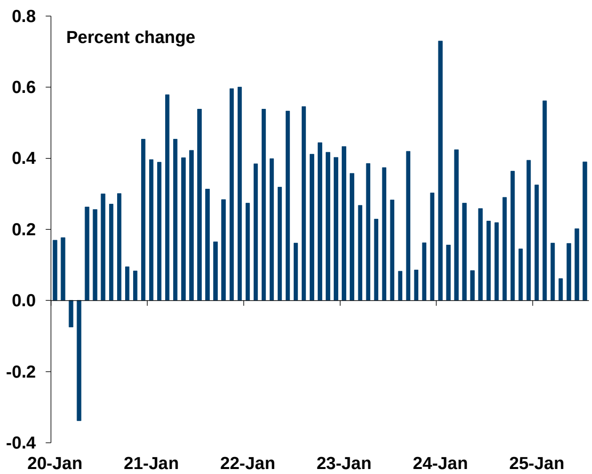
PCE Inflation: Shelter



Source: Bureau of Economic Analysis via Haver Analytics

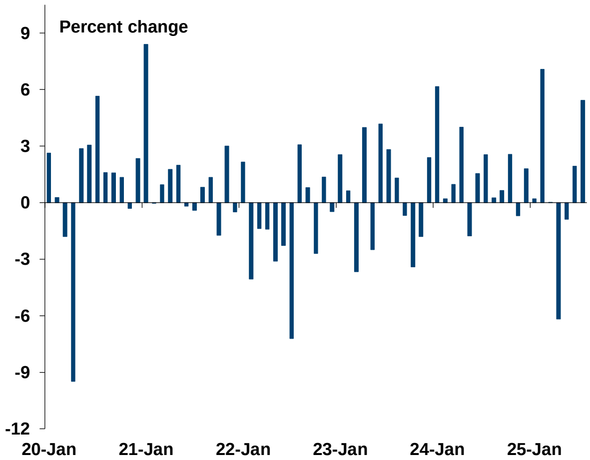
Price pressure was instead concentrated in core services, although here, too, several components showed favorable results and other upside moves that are unlikely to be sustained for a prolonged period. Turning first to highly favorable developments, housing related components either matched or moved closer to pre-pandemic trends (charts, above). Both the rental of tenant-occupied housing and imputed rent of owner-occupied nonfarm housing components rounded up to 0.3 percent – continuing to record increases in the 0.2 to 0.4 percent range since last September. Correspondingly, the year-over-year advance in rents eased to 3.5 percent from 3.8 percent in June and is now aligned with the pre-pandemic performance (which corresponded with the prior period of subdued inflation), and the increase in imputed rents moderated by 0.1 percentage point to 4.1 percent – still elevated but easing toward the previous trend. Contrastingly, core services excluding housing services rose 0.4 percent, the fastest monthly increase since February, with year-year-over-year pace increasing to 3.3 percent from 3.2 percent in the prior month. Notable in this area were several components that registered large – and possibly unsustainable – surges. Namely, portfolio management fees surged 5.4 percent after an increase of 1.9 percent in the prior month and the costs of attending spectator sporting events rose 1.9 percent. The strength in the former category reflected higher returns generated by the ongoing rally in equities and that in the latter occurred after three consecutive drops, including a monthly plunge of 12.2 percent this past April. Other areas suggested softening demand for discretionary outlays, including a decrease of 1.3 percent in the costs of hotel/motel stays after a drop of 3.6 percent in June and a modest increase (0.3 percent) in airfares after back-to-back declines. In our view, caution is still warranted as inflation is not back to 2 percent, but we have become increasingly convinced that tariff-related price pressure will be short-lived and that the re-achievement of the inflation target can be realized even amid further easing in monetary policy.

PCE Price Index: Core Services Ex. Housing



Source: Bureau of Economic Analysis via Haver Analytics

PCE Price Index: Portfolio Management



Source: Bureau of Economic Analysis via Haver Analytics

Another Voice Favoring Lower Rates

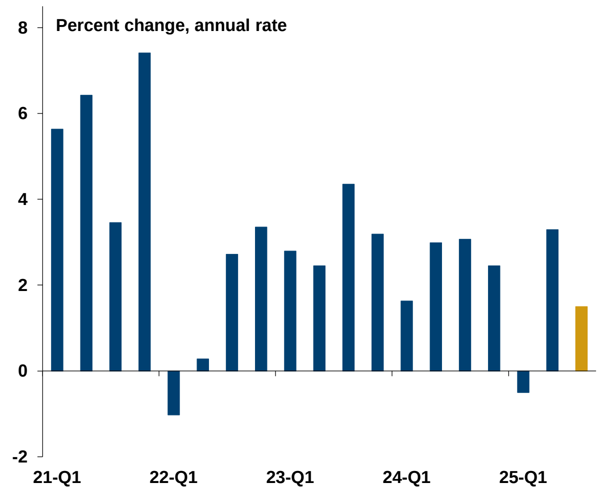
After dissenting at the July FOMC meeting in preference of a rate cut of 25 basis points, Governor Waller followed Chair Powell's dovish speech at Jackson Hole (Aug. 22) with remarks yesterday evening reiterating his case for easier monetary policy by shifting away from what he views as a "moderately restrictive" stance: "I think there is a growing consensus that monetary policy needs to be more accommodative, and even some recognition that it would have been wise to begin this process in July… as I stand here today, I anticipate additional cuts over the next three to six months, and the pace of rate cuts will be driven by the incoming data."

Underlying his assessment is a view suggesting that the balance of risks is shifting, with cuts warranted to support the labor market. On the point, he articulated the belief that risks to the labor market "are continuing to build," and that "labor demand may be on the edge of a sharp decline." Additionally, he pointed to slowing private-sector job growth, accompanied by recent downward revisions, and an increase in unemployment among cyclically sensitive groups (teens and young adults) as further evidence of this underlying softening. At the same time, he appeared relatively sanguine on inflation. He expressed the view that the costs of tariffs would be distributed in equal parts among exporters, importers, and consumers and he noted that "most forecasts" call for "monthly tariff effects dissipating by early 2026." Moreover, he noted that inflation expectations remain contained, which will curtail risks for more persistent inflationary effects, and concluded that "monetary policy should look through the tariff effects on inflation." Again, although Waller is one voice among many, we do suspect that his comments, along with those of Chair Powell, indicate a shift in consensus that makes a cut of 25 basis points in September an essentially foregone conclusion, while keeping the door ajar to further easing at upcoming meetings. (For more the entirety of his prepared remarks, see: Waller, Christopher J. "Let's Get On with It," Federal Reserve Board, August 28, 2025. https://www.federalreserve.gov/newsevents/speech/waller20250828a.htm)

Q3 GDP Tracking Update

Moving beyond the inflation statistics, we also took note of several data that help inform on view on Q3 GDP growth, which led us to revise higher our tracking estimate from 1.2 percent last week to 1.5 percent (chart, below left). In the plus column, nominal consumer spending of 0.5 percent published in the July Personal Income and Outlays report translated to a real (inflation adjusted) gain of 0.3 percent, a firm result given depressed consumer confidence and hints of hesitation in discretionary areas of spending. With that said, even if real consumer outlay growth were to ease to 0.1 percent per month in August and September, results for the quarter would exceed by a small margin those in the prior quarter – far from a robust performance but still supportive enough to keep the economy on a growth track (chart, below right).

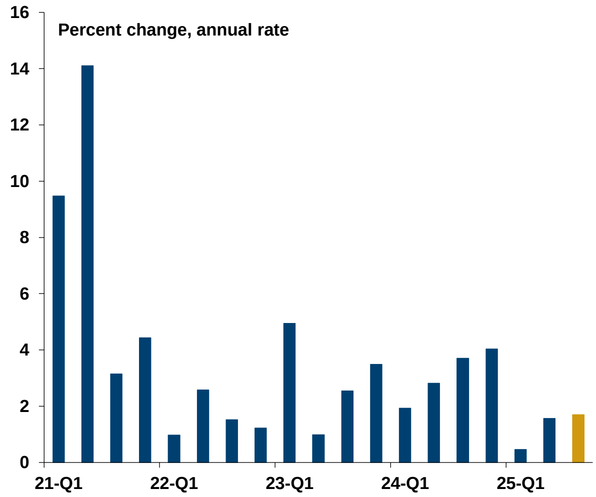
GDP Growth*



** The gold bar is a forecast for 2025-Q3.*

Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

Real Consumer Spending Growth*

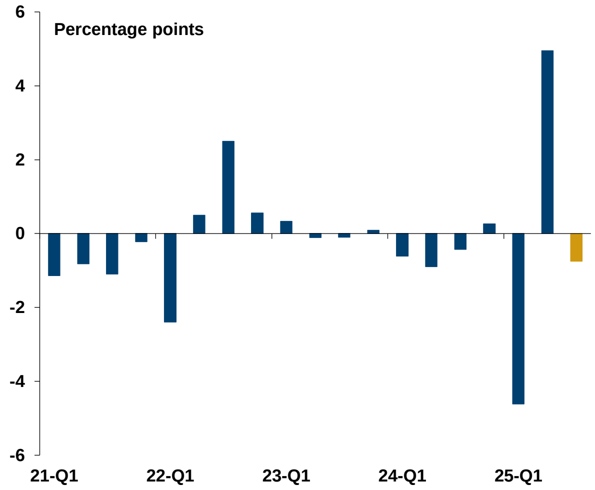


** The gold bar is a forecast for 2025-Q3.*

Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

On the negative side, international trade data for July released in the Census Bureau's Advance Economic Indicators release indicated that the trade deficit in goods widened by $18.7 billion to $103.6 billion, far exceeding the Bloomberg survey median projection of -$90.2 billion. The deficit, which reflected a dip of 0.1 percent in U.S. exports of goods that was eclipsed by a surge of 7.1 percent in imports, was markedly wider than the -$89.0 billion average in Q2 and thus suggested a drag from net exports on growth (which we currently project to be approximately 0.75 percentage point; chart, right). Part of the firm reading on imports reflected an advance of 4.8 percent in capital goods, but the industrial supplies category also surged 25.4 percent. We could infer that part of the increase was driven by gold repatriation, and will therefore not affect net exports, but relying only on the data in hand leads us to anticipate another swing in net exports in Q3 on account of the Trump administration's trade policy.

Net Exports of Goods & Services*



** Contribution to real percentage change in GDP. The gold bar is a forecast for 2025-Q3.*

Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

The Week Ahead

ISM Manufacturing (August) (Tuesday)
Forecast: 48.5% (+0.5 Pct. Pt.)

Economic uncertainty fueled by a still-evolving tariff policy coupled with a restrictive stance of monetary policy has created a difficult environment for manufacturing businesses, with the factory sector as a whole remaining stuck in neutral. On the point, firms surveyed in the ISM report have noted difficulty in forecasting what they will ultimately pay in duties, increased costs of raw materials, and uncertainty surrounding sourcing strategies. Thus, the ISM manufacturing index appears poised to stay in contractionary territory for the sixth consecutive month (and 32nd in the past 34).

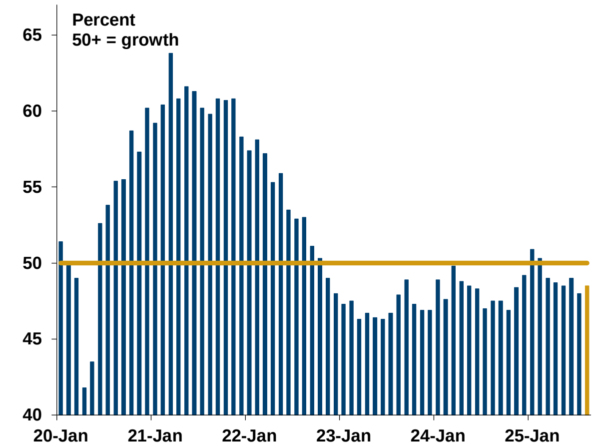
Construction Spending (July) (Tuesday)
Forecast: -0.2%

With housing starts having been rangebound over the past several months, private residential construction is likely to post another disappointing result in July, augmenting the downward trend in place since the spring of last year. Concurrently, while government spending could nudge higher, business-related activity has tilted lower since late 2023 as previous investment tied to federal policies (e.g., Inflation Reduction and CHIPS Acts) continues to peter out. Thus, total construction activity seems likely come in lower for the tenth time in the past eleven months.

Factory Orders (July) (Wednesday)
Forecast: -1.3%

Following a decline of 9.4 percent in the prior month, durable goods orders fell again in July, easing 2.8 percent. Recent shifts in total bookings have typically reflected erratic swings in the often-volatile transportation category, with this area decreasing 9.7 percent (influenced importantly by the 32.7 percent drop in civilian aircraft orders). Excluding transportation, orders have tilted higher on balance over the past twelve months. Preliminary shipments data released with the Advance Report on Durable Goods on August 26 indicate an increase of 0.5 percent for nondurables.

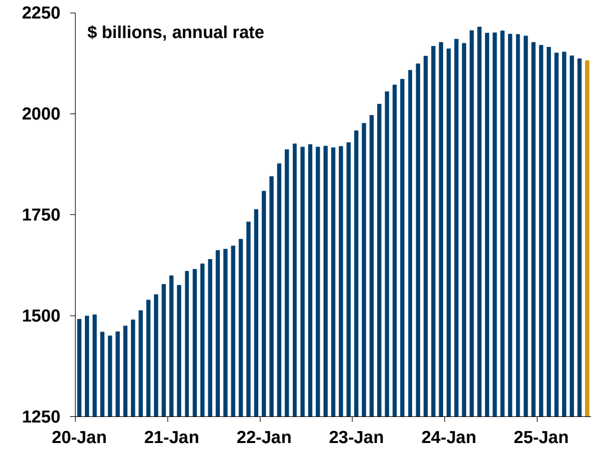
ISM Manufacturing Index*



** The gold bar is a forecast for August 2025.*

Sources: Institute for Supply Management via Haver Analytics; Daiwa Capital Markets America

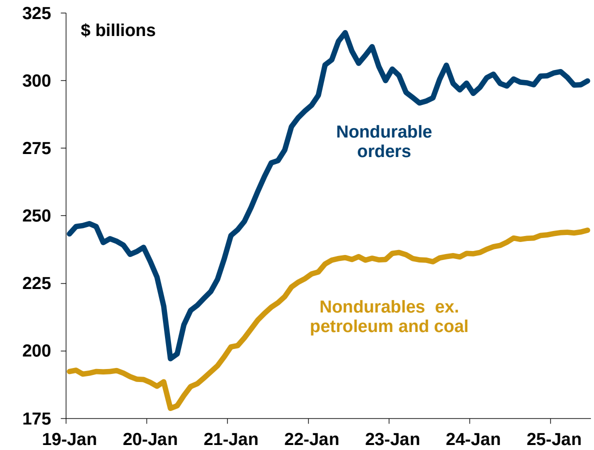
Value of Construction Put in Place*



** The gold bar is a forecast for July 2025.*

Sources: U.S. Census Bureau via Haver Analytics; Daiwa Capital Markets America

New Orders for Nondurable Goods



Source: U.S. Census Bureau via Haver Analytics

Trade Balance (July) (Thursday)
Forecast: -$79.0 Billion ($18.8 Billion Wider Deficit)

The goods deficit widened by $18.7 billion to $103.6 billion in July (Census basis; published August 29), implying similar deterioration for the total trade shortfall. Trade flows had exhibited high volatility on account of tariff front running earlier in the year, with the choppiness continuing in July after signs of normalization in Q2. Thus, the early data for Q3 suggest a negative contribution from net exports to GDP growth in the area of 0.75 percentage point after wide swings in recent quarters (a positive contribution of 4.95 percentage points in Q2 that flowed a drag of 4.61 percentage points in Q1).

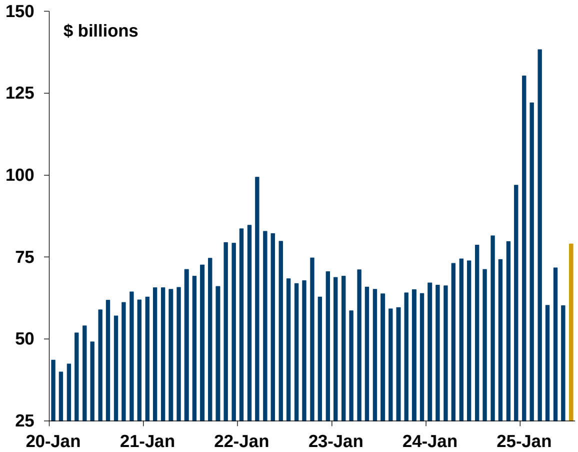
ISM Services (August) (Thursday)
Forecast: 50.5% (+0.4 Pct. Pt.)

Despite prevailing uncertainty stemming from the Trump administration's tariff agenda, service-providing firms appear to be holding up better than their manufacturing counterparts, with the ISM services index likely to hold out in expansion territory for the 13th time in the past 14 months (though at a level only modestly above the critical threshold separating expansion from contraction). In that regard, we could envision this metric remaining sluggish in coming months as slack demand continues to weigh on both business activity and new orders.

Payroll Employment (August) (Friday)
Forecast: 70,000

Labor market conditions have softened noticeably in recent months, with average payroll growth of 35,000 in the past three months lagging the 171,000 monthly pace in 2024-H2 and 111,000 in the first quarter of 2025. Thus, downside risks to labor market conditions appear to have risen noticeably. Moreover, sluggish employment growth raises the possibility of the unemployment rate increasing 0.2 percentage point to 4.4 percent in the latest month after just rounding down to a 0.1 percentage point increase in July. Growth of average hourly earnings could remain close to the trailing twelve-month average of 0.3 percent (associated with a year-over-year increase of 3.7 percent).

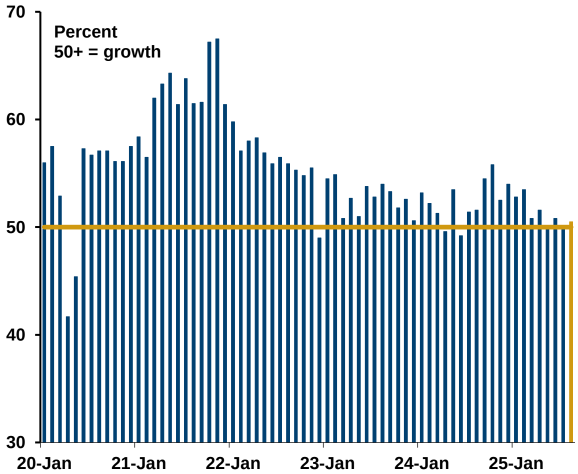
Trade Deficit in Goods & Services*



** The gold bar is a forecast for July 2025.*

Sources: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

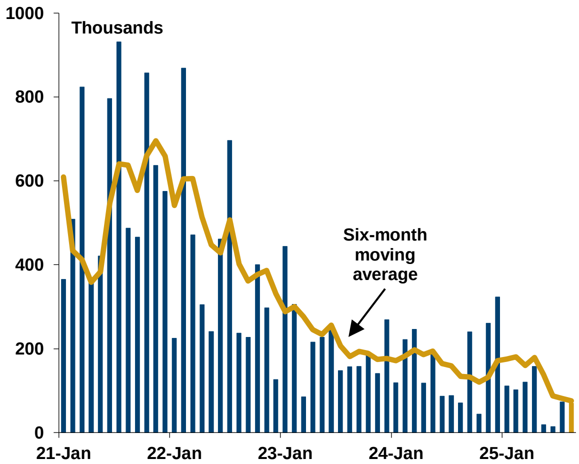
ISM Services Index*



** The gold bar is a forecast for August 2025.*

Sources: Institute for Supply Management via Haver Analytics; Daiwa Capital Markets America

Change in Nonfarm Payrolls*



** The gold bar is a forecast for August 2025.*

Sources: Bureau of Labor Statistics via Haver Analytics; Daiwa Capital Markets America

Economic Indicators

August/September 2025

Monday 25

CHICAGO FED NATIONAL ACTIVITY INDEX

	Monthly	3-Mo. Avg.
May	-0.18	-0.14
June	-0.18	-0.26
July	-0.19	-0.18

NEW HOME SALES

May	0.630 million
June	0.656 million
July	0.652 million

Tuesday 26

DURABLE GOODS ORDERS

May	16.5%
June	-9.4%
July	-2.8%

FHFA HOME PRICE INDEX

Apr	-0.3%
May	-0.1%
June	-0.2%

S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX

Apr	-0.4%
May	-0.3%
June	-0.3%

CONFERENCE BOARD CONSUMER CONFIDENCE

June	95.2
July	98.7
Aug	97.4

Wednesday 27

Thursday 28

UNEMPLOYMENT CLAIMS

	Initial	Continuing
	(millions)	
Aug 2	0.227	1.942
Aug 9	0.224	1.961
Aug 16	0.234	1.954
Aug 23	0.229	N/A

GDP

	GDP	Chained Price
25-Q1	-0.5%	3.8%
25-Q2(a)	3.0%	2.0%
25-Q2(p)	3.3%	2.0%

PENDING HOME SALES

May	1.8%
June	-0.8%
July	-0.4%

Friday 29

PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX

	Inc.	Cons.	Core
May	-0.4%	0.0%	0.2%
June	0.3%	0.4%	0.3%
July	0.4%	0.5%	0.3%

INTERNATIONAL TRADE IN GOODS

May	-$96.2 billion
June	-$84.9 billion
July	-$103.6 billion

ADVANCE INVENTORIES

	Wholesale	Retail
May	-0.3%	0.2%
June	0.1%	0.2%
July	0.2%	0.2%

MNI CHICAGO BUSINESS BAROMETER

June	40.4
July	47.1
Aug	41.5

REVISED CONSUMER SENTIMENT

July	61.7
Aug(p)	58.6
Aug(r)	58.2

Monday 1

LABOR DAY

Tuesday 2

ISM MFG. INDEX (10:00)

	Index	Prices
June	49.0	69.7
July	48.0	64.8
Aug	**48.5**	**65.0**

CONSTRUCTION (10:00)

May	-0.4%
June	-0.4%
July	**-0.2%**

Wednesday 3

FACTORY ORDERS (10:00)

May	8.3%
June	-4.8%
July	**-1.3%**

JOLTS DATA (10:00)

	Openings (000)	Quit Rate
May	7,712	2.0%
June	7,437	2.0%
July	--	--

BEIGE BOOK (2:00)

July 2025:
"Economic activity increased slightly from late May through early July. Five Districts reported slight or modest gains, five had flat activity, and the remaining tw Districts noted modest declines i activity."

VEHICLE SALES

June	15.3 million
July	16.4 million
Aug	**16.0 million**

Thursday 4

ADP EMPLOYMENT (8:15)

	Private Payrolls
June	-23,000
July	104,000
Aug	--

UNEMP. CLAIMS (8:30)

TRADE BALANCE (8:30)

May	-$71.7 billion
June	-$60.2 billion
July	**-$79.0 billion**

PRODUCTIVITY & COSTS (8:30)

	Productivity	Unit Labor Costs
25-Q1	-1.8%	6.9%
25-Q2(p)	2.4%	1.6%
25-Q2(r)	**3.0%**	**1.5%**

ISM SERVICES INDEX (10:00)

	Index	Prices
June	50.8	67.5
July	50.1	69.9
Aug	**50.5**	**69.5**

Friday 5

EMPLOYMENT REPORT (8:30)

	Payrolls	Un. Rate
June	14,000	4.1%
July	73,000	4.2%
Aug	**70,000**	**4.4%**

Monday 8

CONSUMER CREDIT

Tuesday 9

NFIB SMALL BUSINESS OPTIMISM INDEX

Wednesday 10

PPI

WHOLESALE TRADE

Thursday 11

UNEMP. CLAIMS

CPI

FEDERAL BUDGET

Friday 12

CONSUMER SENTIMENT

Monday 15

EMPIRE MFG

Tuesday 16

RETAIL SALES

IMPORT/EXPORT PRICES

IP & CAP-U

NAHB HOUSING INDEX

BUSINESS INVENTORIES

FOMC MEETING (FIRST DAY)

Wednesday 17

HOUSING STARTS

FOMC RATE DECISION

Thursday 18

UNEMP. CLAIMS

PHILLY FED INDEX

LEADING INDICATORS

TIC FLOWS

Friday 19

Forecasts in bold. (a) = advance (1st estimate of GDP), (p) = preliminary (2nd estimate of GDP), (r) = revised

Daiwa Capital Markets

Treasury Financing

August/September 2025

Monday	Tuesday	Wednesday	Thursday	Friday
25	26	27	28	29
AUCTION RESULTS: Rate Cover 13-week bills 4.100% 3.07 26-week bills 3.915% 3.36	**AUCTION RESULTS:** Rate Cover 6-week bills 4.210% 2.93 2-yr notes 3.641% 2.69 **ANNOUNCE:** $65 billion 17-week bills for auction on Aug 27 $100 billion 4-week bills for auction on Aug 28 $85 billion 8-week bills for auction on Aug 28 **SETTLE:** $65 billion 17-week bills $100 billion 4-week bills $85 billion 8-week bills	**AUCTION RESULTS:** Rate Cover 17-week bills 4.020% 3.00 5-yr notes 3.724% 2.36 Margin Cover 2-yr FRNs 0.195% 3.22	**AUCTION RESULTS:** Rate Cover 4-week bills 4.245% 2.68 8-week bills 4.145% 2.92 7-yr notes 3.925% 2.49 **ANNOUNCE:** $155 billion 13-,26-week bills for auction on Sep 2 $85 billion 6-week bills for auction on Sep 2 $50 billion 52-week bills for auction on Sep 2 **SETTLE:** $155 billion 13-,26-week bills $85 billion 6-week bills	**SETTLE:** $8 billion 30-year TIPS $28 billion 2-year FRNs
1	2	3	4	5
LABOR DAY	**AUCTION:** $155 billion 13-,26-week bills $85 billion 6-week bills $50 billion 52-week bills **ANNOUNCE:** $65 billion* 17-week bills for auction on Sep 3 $100 billion* 4-week bills for auction on Sep 4 $85 billion* 8-week bills for auction on Sep 4 **SETTLE:** $65 billion 17-week bills $100 billion 4-week bills $85 billion 8-week bills $16 billion 20-year bonds $69 billion 2-year notes $70 billion 5-year notes $44 billion 7-year notes	**AUCTION:** $65 billion* 17-week bills	**AUCTION:** $100 billion* 4-week bills $85 billion* 8-week bills **ANNOUNCE:** $155 billion* 13-,26-week bills for auction on Sep 8 $85 billion* 6-week bills for auction on Sep 9 $58 billion* 3-year notes for auction on Sep 9 $39 billion* 10-year notes for auction on Sep 10 $22 billion* 30-year bonds for auction on Sep 11 **SETTLE:** $155 billion 13-,26-week bills $85 billion 6-week bills $50 billion 52-week bills	
8	9	10	11	12
AUCTION: $155 billion* 13-,26-week bills	**AUCTION:** $85 billion* 6-week bills $58 billion* 3-year notes **ANNOUNCE:** $65 billion* 17-week bills for auction on Sep 10 $100 billion* 4-week bills for auction on Sep 11 $85 billion* 8-week bills for auction on Sep 11 **SETTLE:** $65 billion* 17-week bills $100 billion* 4-week bills $85 billion* 8-week bills	**AUCTION:** $65 billion* 17-week bills $39 billion* 10-year notes	**AUCTION:** $100 billion* 4-week bills $85 billion* 8-week bills $22 billion* 30-year bonds **ANNOUNCE:** $155 billion* 13-,26-week bills for auction on Sep 15 $85 billion* 6-week bills for auction on Sep 16 $13 billion* 20-year bonds for auction on Sep 16 $19 billion* 10-year TIPS for auction on Sep 18 **SETTLE:** $155 billion* 13-,26-week bills $85 billion* 6-week bills	
15	16	17	18	19
AUCTION: $155 billion* 13-,26-week bills **SETTLE:** $58 billion* 3-year notes $39 billion* 10-year notes $22 billion* 30-year bonds	**AUCTION:** $85 billion* 6-week bills $13 billion* 20-year bonds **ANNOUNCE:** $65 billion* 17-week bills for auction on Sep 17 $100 billion* 4-week bills for auction on Sep 18 $85 billion* 8-week bills for auction on Sep 18 **SETTLE:** $65 billion* 17-week bills $100 billion* 4-week bills $85 billion* 8-week bills	**AUCTION:** $65 billion* 17-week bills	**AUCTION:** $100 billion* 4-week bills $85 billion* 8-week bills $19 billion* 10-year TIPS **ANNOUNCE:** $155 billion* 13-,26-week bills for auction on Sep 22 $85 billion* 6-week bills for auction on Sep 23 $69 billion* 2-year notes for auction on Sep 23 $70 billion* 5-year notes for auction on Sep 24 $44 billion* 7-year notes for auction on Sep 25 $28 billion* 2-year FRNs for auction on Sep 24	**SETTLE:** $155 billion* 13-,26-week bills $85 billion* 6-week bills

*Estimate