Daiwa Capital Markets

U.S. Economic Comment

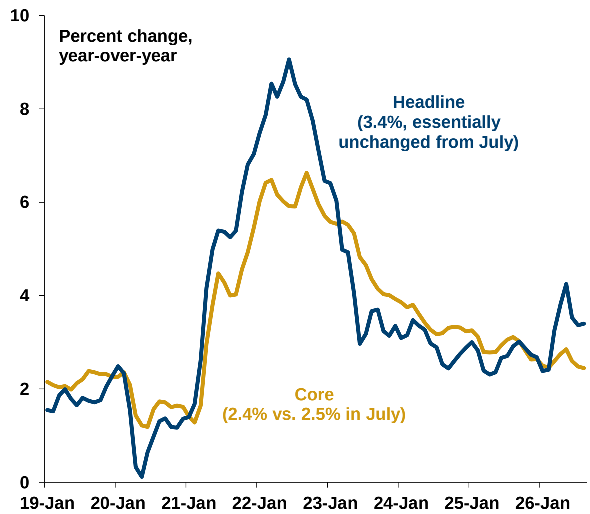
- FOMC preview: firm underlying inflation paves the way for a hike next week
- Summary of Economic Projections: expect modest changes to inflation and rates outlooks

Lawrence Werther
lawrence.werther@us.daiwacm.com
+1-212-612-6393
Brendan Stuart
brendan.stuart@us.daiwacm.com
+1-212-612-6172

A September "Risk Management" Hike?

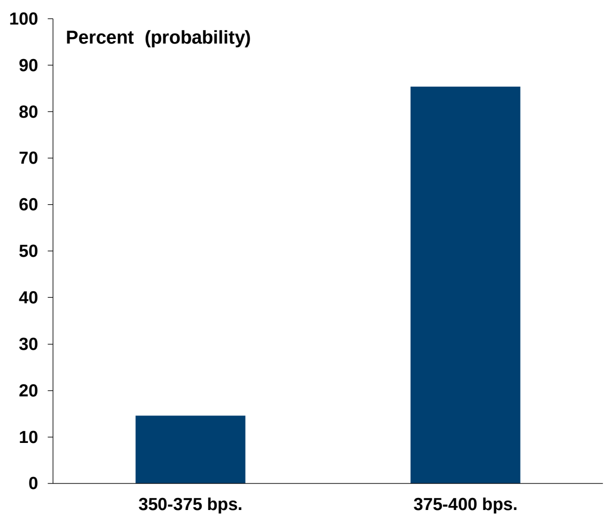
After the results from last week's Employment Situation report ratified Chairman Warsh's assessment at the Jackson Hole Economic Policy Symposium that current labor market conditions "are consistent with full employment " -- recall that job growth in August accelerated to 162,000 from a trailing three-month average of approximately 38,000 and the unemployment rate remained at a subdued 4.1 percent – we viewed the August CPI print as the key factor determining the outcome of next week's FOMC meeting. At the time, we hypothesized that an increase in the core CPI rounding to 0.2 percent, the likely outcome anticipated by the vast majority of participants in the Bloomberg economist survey, would be enough to sway the majority of the FOMC to maintain a watch-and-wait approach aligned with further discerning the underlying trend in prices, whereas an outcome above that could spur action by the Committee. Ultimately, the latter was realized, with the headline CPI advancing 0.4 percent (+0.396 percent with less rounding), matching expectations, and the core rounding up to 0.3 percent (+0.290 percent). Moreover, the latest shifts were consistent with year-over-year increases of 3.397 percent for the headline index and 2.446 percent for the core measure (versus advances of 3.365 percent and 2.478 percent, respectively in July; chart, below left). In essence, the data failed to illustrate a further stirring in inflationary pressures while also emphasizing the current sideways trend above 2 percent. Thus, in light of the lack of progress toward target, the market-implied probability of a hike of 25 basis points next week shifted from slightly less than 60 percent last Friday to almost 87 percent currently (chart, below right).

CPI: Headline & Core



Source: Bureau of Labor Statistics via Haver Analytics

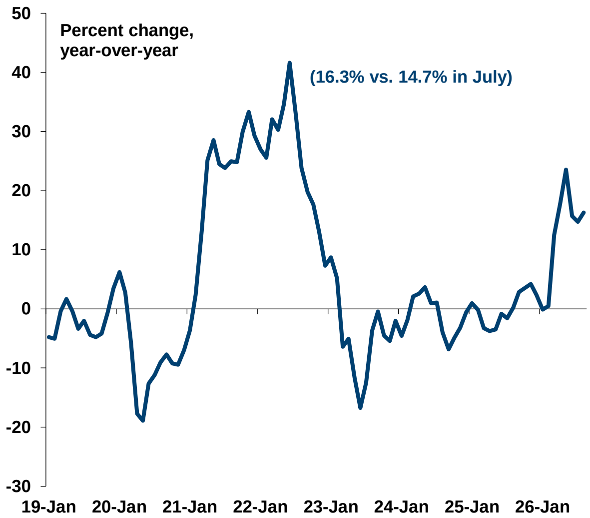
Federal Funds Target Rate Probabilities*



** The implied target range for the federal funds rate at the conclusion of the September meeting based on futures pricing data as of September 11, 2026.*
Source: CME Group, FedWatch tool

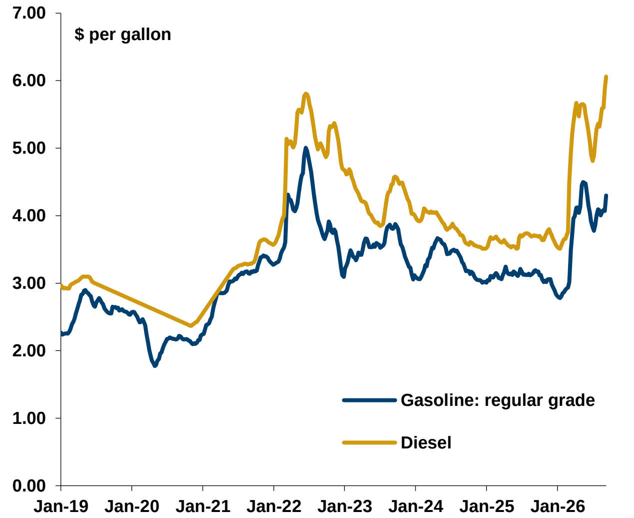
Even in acknowledging the pronounced shift in the likelihood of action next week, we hesitate to conclude that the now-expected move is necessarily a harbinger of further hikes beyond fine-tuning of 25 to 50 basis points (i.e., a limited series of adjustments designed to hedge against elevated inflation risks). Of late, much of the risk surrounding inflation and its trajectory stems from the ongoing conflict in the Middle East and its pronounced impact on energy prices. On the point, the energy component of the CPI rose 2.1 percent today (+16.3 percent year-over-year; chart, below left), exclusively reflecting a jump in energy commodities after cooling in the prior two months. Perhaps more important than movements in the CPI, however, have been the sustained upward trajectory in fuel prices illustrated in the chart below to the right. At $4.30 (as of 9/10), the average retail price of regular grade gasoline is up over 52 percent year-to-date, while the cost of diesel at $6.06 has surged more than 71 percent. Prices could level off here, which would suggest a moderation in price growth, but the substantial price-level change thus far in 2026 raises the possibility of second-round effects reverberating through the economy (e.g., higher costs of transportation and logistics services). Thus far, we view those impacts since the start of the conflict in late February as mostly contained, but risks nonetheless remain elevated until the situation is resolved. In light of that fact, we are inclined to view any change of course at upcoming FOMC meetings as more so aligned with sound risk management practices rather than a concession to hawks that the real policy rate is insufficient to return inflation to target. Indeed, should the conflict end fairly soon and energy prices retreat, any longer-term effect would indeed prove limited and – dare we say – transient.

CPI: Energy



Source: Bureau of Labor Statistics via Haver Analytics

US Gasoline & Diesel Prices*

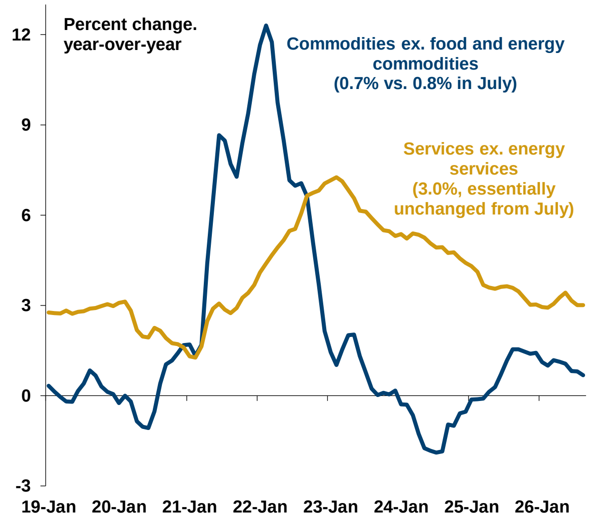


** Weekly end-of-period data except for the latest observations which are daily quotes from September 10, 2026.*

Source: Energy Information Administration via Haver Analytics

Outside of the energy complex, we observed little that meaningfully swayed our view that aggregate inflation could move mostly sideways over the balance of the year before the disinflationary impulse gains steam in the first half of 2027. In that regard, the monthly increase of 0.1 percent in core goods prices, and attendant deceleration in the year-over-year advance to 0.7 percent in August from 0.8 percent previously, suggests that price pressure tied to tariffs continues to ebb (even amid now heightened trade tensions with Canada; chart, right). Further, on the services side, monthly increases in the rent of primary residence and owners' equivalent rent of residences components rounding up to 0.2 percent augmented favorable trends consistent with the pre-pandemic episode. (The year-over-year increase in primary rents slowed to 2.75 percent from 2.86 percent, while that for OER eased to 3.08 percent from 3.23 percent.)

CPI: Core Goods & Core Services



Source: Bureau of Labor Statistics via Haver Analytics

To be sure, there were some areas of concern. The tuition, other school fees, and childcare area rose briskly for the second consecutive month, with the increase of 0.8 percent in August pushing the year-over-year growth rate to 3.4 percent from 2.7 percent previously. Additionally, airfares remained under pressure (likely influenced by both firm demand and higher fuel prices), with the jump of 2.7 percent in August sustaining the year-over-year change at +23.4 percent (elevated but off slightly from +25.5 percent in July). Finally, reflecting ongoing capex demand in the AI space, which is exerting pressure on chips prices, the computers, peripherals, and smart home assistant devices component jumped 3.8 percent month-to-month, the second consecutive increase in excess of three percent, with the year-over-year growth rate surging to +8.4 percent from +3.9 percent. Relatedly, the year-over-year growth rate in the computer software and accessories category (only available on a not seasonally adjusted basis) accelerated to +25.4 percent from +21.2 percent in the prior month.

All told, the hawkish tone of Chairman Warsh's remarks at Jackson Hole likely left little recourse for avoiding a rate hike after today's CPI report. We calculate that the combined results of that report and the PPI suggest an increase of 0.25 percent increase in the core price index for personal consumption expenditures – the Fed's preferred inflation metric – associated with a year-over-year advance of 3.37 percent, functionally similar to the unsatisfactory +3.34 percent pace in July. At the same time, uncertainty stemming from energy prices may recede fairly rapidly with little long-term effect on underlying inflation (which is why central banks often look through moves in commodity prices), and price shifts tied to AI could be at least partially the result of supply-side factors (which monetary policy is ill suited to address). Therefore, we foresee the Fed Chairman, aligned with his preferred method, avoiding guidance affirming that a series of rate hikes is in store – a strategy preferred by policy hawks likely unconvinced about the restrictiveness of the current level of interest rates – in favor of a meeting-by-meeting approach as ongoing attempts are made to better discern underlying trend inflation.

The Summary of Economic Projections and Committee Statement

At the conclusion of next week's FOMC meeting the Committee will release alongside its statement a new Summary of Economic Projections, which will also include an initial round of forecasts for 2029. Aligned with his approach in June, we expect that Chairman Warsh will avoid submitting projections. Even so, the forecasts, in our view, will remain useful in gauging the potential reaction functions of various policymakers. For September, we anticipate only modest changes to the latest SEP vis-à-vis that in June save for the inclusion of 2029 projections (table). Growth forecasts in the low 2's are reasonable given the performance of the economy in 2026 thus far, and extrapolating that trend is not unreasonable at this juncture. The unemployment rate may be nudged lowed in the near-term, possibly to 4.2 percent in 2026 and 2027, although we would not view any wiggles as signaling a change in the prevailing narrative on the labor market. Projections for inflation and the target range for the federal funds rate could prove a bit trickier, at least for 2026. We again expect that inflation forecasts will be close to those in June, although we could envision the median expectation for the federal funds rate showing a full rate hike, or possibly two, rather than the 3.75 percent median previously. With that said, we still suspect that at least a large minority of policymakers remain unconvinced about the need for more than modest increases in the policy rate.

Economic Projections of the FOMC, June 2026*

	2026	2027	2028	Longer Run
Change in Real GDP	2.2	2.3	2.2	2.0
Unemployment Rate	4.3	4.3	4.2	4.2
PCE Inflation	3.6	2.3	2.0	2.0
Core PCE Inflation	3.3	2.5	2.1	--
Federal Funds Rate	3.8	3.6	3.4	3.1

** Median projections*
Source: Federal Open Market Committee

For illustrative purposes, we have also included the July FOMC statement (below). Aside from a possible increase in the target range in the federal funds rate, and perhaps a shift in dissents, we see only limited prospects for a change in language. Recent statements were made deliberately terse, and we fully expect that the FOMC will maintain this new paradigm aligned with Chairman Warsh's vision.

July 29, 2026 FOMC Statement

The Federal Open Market Committee approved the following statement for release by a 9 – 3 vote:

The Committee decided to maintain the target range for the federal funds rate at 3-1/2 to 3-3/4 percent, in support of the Federal Reserve's dual mandate. The Committee is continuing its policy of maintaining ample reserves in the banking system.

Economic activity is expanding at a solid pace despite elevated uncertainty that owes, in part, to the conflict in the Middle East. Productivity growth and capital investment are strong. Job gains have kept pace with the workforce, and the unemployment rate has changed little.

Inflation remains elevated relative to the Committee's 2 percent goal, in part reflecting supply shocks that have driven price increases in certain sectors, including energy. The Committee will deliver price stability.

Voting against the monetary policy action were Beth M. Hammack, Neel Kashkari, and Lorie K. Logan, who preferred to raise the target range for the federal funds rate by 1/4 percentage point at this meeting.

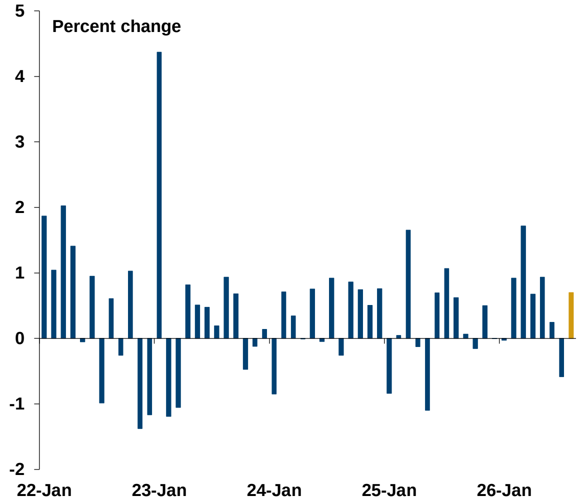
Source: Federal Open Market Committee

The Week Ahead

Retail Sales (August) (Wednesday)
Forecast: +0.7% total, +0.6% ex. autos, +0.4% ex. autos & gas

An increase in automotive sales in August points to improvement for the motor vehicle and parts component of retail sales. Moreover, with higher prices at the pump, the gasoline component could also provide a boost to the anticipated increase in total activity. While transactions excluding autos and gasoline contracted in July – likely reflecting a cooldown after consumers pulled forward purchases in June to take advantage of Amazon Prime Day and other competing sales -- we expect a rebound in August closer to the average monthly read of +0.6 percent in 26-H1.

Retail Sales*



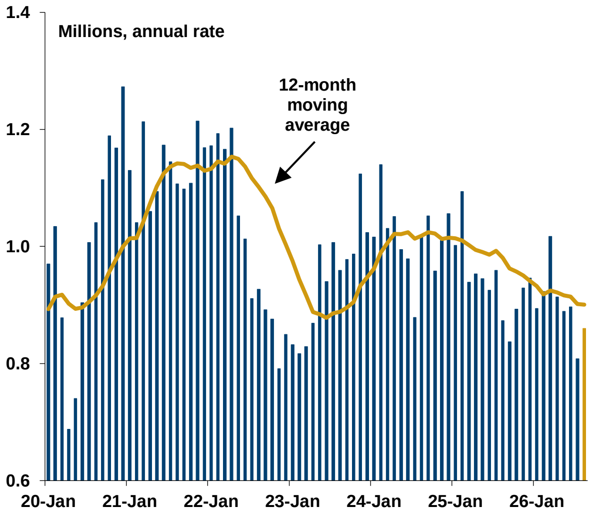
** The gold bar is a forecast for August 2026.*

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

Housing Starts (August) (Thursday)
Forecast: 1.300 million (+4.9%)

Elevated inventories of unsold new homes suggest that builders will continue to exercise caution in initiating new single-family projects in August. That said, following a 9.9 percent decline to 0.808 million units, annual rate, in the prior month (the lowest observed since November 2022), we could envision an increase pushing this series closer to the middle of the recent range – a notion supported by July's 2.5 percent increase in permit issuance. Concurrently, multi-family starts, typically the more volatile of the two components, could post a reading close to the trailing 12-month average of 0.439 million units.

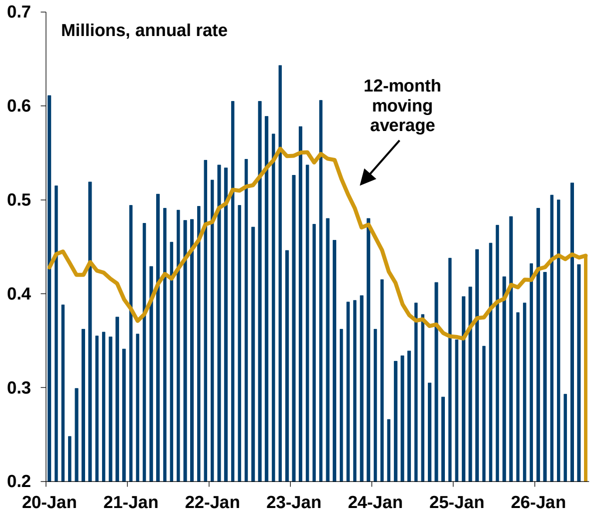
Single-Family Housing Starts*



** The gold bar is a forecast for August 2026.*

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

Multi-Family Housing Starts*



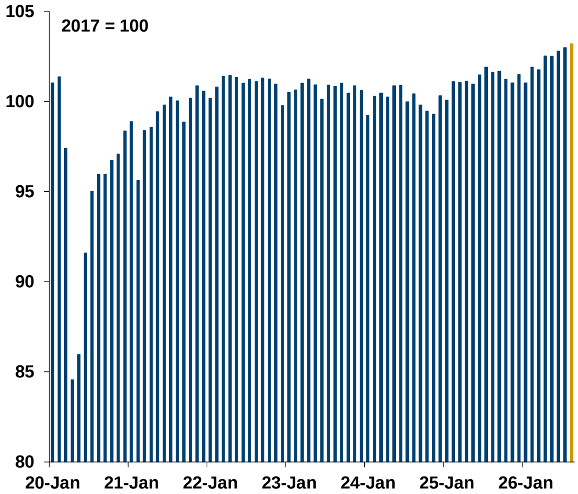
** The gold bar is a forecast for August 2026.*

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

Industrial Production (August) (Friday)
Forecast: +0.2%

An increase in factory headcounts and the maintenance of worktimes in the upper end of the recent range suggest an advance in the manufacturing component of industrial production for the seventh time in the past eight months, a result which would augment the ongoing upward drift in this series since early 2025 (recall that January's shift rounded down to no change: +0.012 percent). Moreover, mining activity could also perform favorably – a notion supported by modest increases in the rotary rig count and payrolls. The utility component often reflects swings in weather rather than economic fundamentals, with above-average temperatures potentially pointing to an uptick in the latest month. That said, keep in mind that this area can show marked volatility on a month-to-month basis.

Industrial Production*



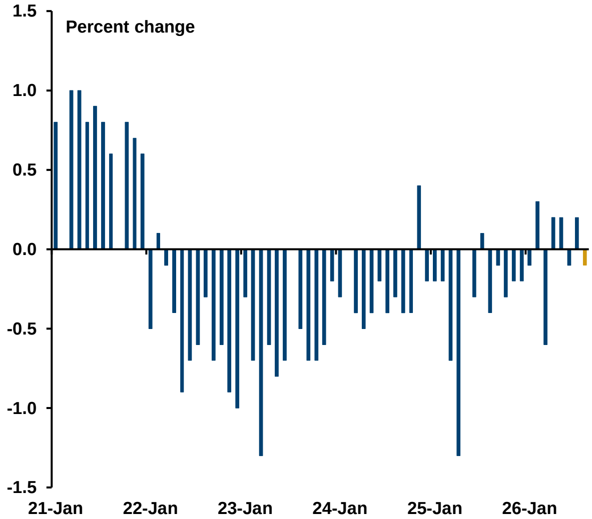
** The gold bar is a forecast for August 2026.*

Sources: Federal Reserve Board via Haver Analytics; Daiwa Capital Markets America

Leading Indicators (August) (Friday)
Forecast: -0.1%

Anticipated positive contributions from higher stock prices and the slope of the yield curve were likely offset by negative consumer expectations and unemployment claims, indicative of the Conference Board's Leading Economic Index decreasing in August for the 46th time in the past 56 months. If the projection is realized, the index will be 18.5 percent below the cycle peak of 121.9 in December 2021. While the easing seen over the past few years would typically be consistent with the economy entering recession, available data still indicate ongoing expansion in the face of heightened uncertainty.

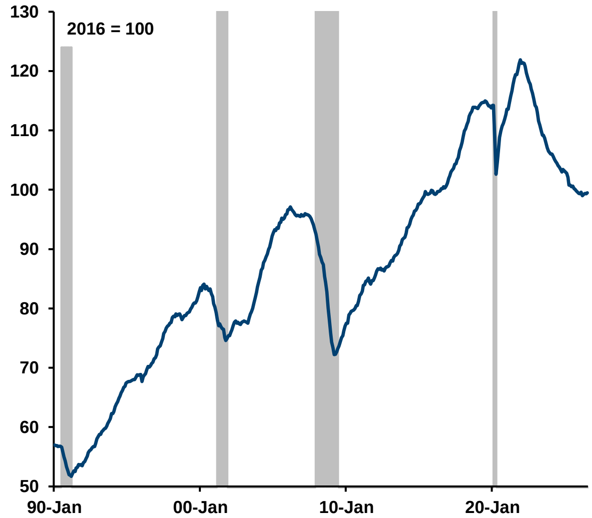
Index of Leading Economic Indicators*



** The gold bar is a forecast for August 2026.*

Sources: The Conference Board via Haver Analytics; Daiwa Capital Markets America

Index of Leading Economic Indicators*



** The shaded areas indicate periods of recession in the United States.*

Sources: The Conference Board, National Bureau of Economic Research via Haver Analytics

Economic Indicators

September/October 2026

Monday	Tuesday	Wednesday	Thursday	Friday
7	8	9	10	11
LABOR DAY	**NFIB SMALL BUSINESS OPTIMISM INDEX** June 97.4 July 99.8 Aug 98.7 **CONSUMER CREDIT** May $2.0 billion June $14.6 billion July $18.1 billion		**UNEMPLOYMENT CLAIMS** Initial / Continuing (millions) Aug 15 0.207 1.771 Aug 22 0.204 1.775 Aug 29 0.207 1.774 Sep 5 0.206 N/A **PPI** Final Demand / Ex. Food & Energy June -0.1% 0.4% July 0.1% 0.3% Aug 0.4% 0.2% **EXISTING HOME SALES** June 4.130 million July 4.060 million Aug 3.980 million **WHOLESALE TRADE** Inventories / Sales May 0.3% 3.5% June 0.4% -2.9% July 1.3% 0.8%	**CPI** Total / Core June -0.4% 0.0% July 0.1% 0.2% Aug 0.4% 0.3% **CONSUMER SENTIMENT** July 55.2 Aug 51.7 Sep 47.8 **FEDERAL BUDGET** 2026 / 2025 June -$120.3B $27.0B July -$432.3B -$291.1B Aug -$166.8B -$344.8B
14	15	16	17	18
	EMPIRE MFG (8:30) July 15.6 Aug 20.6 Sep -- **FOMC MEETING (FIRST DAY)**	**RETAIL SALES (8:30)** Total / Ex.Autos June 0.2% -0.2% July -0.6% -0.3% **Aug 0.7% 0.6%** **IMPORT/EXPORT PRICES (8:30)** Non-Petrol Imports / Nonagri. Exports June 0.2% -0.7% July 0.3% -1.5% Aug -- -- **NAHB HOUSING INDEX (10:00)** July 34 Aug 35 Sep -- **BUSINESS INVENTORIES (10:00)** Inventories / Sales May 0.4% 2.1% June 0.1% -1.0% **July 0.8% 0.3%** **FOMC RATE DECISION (2:00)** **TIC FLOWS (4:00)** Long-Term / Total May $231.2B $131.5B June $172.7B $133.5B July -- --	**UNEMP. CLAIMS (8:30)** **HOUSING STARTS (8:30)** June 1.415 million July 1.239 million **Aug 1.300 million** **PHILADELPHIA FED MFG BUSINESS OUTLOOK (8:30)** July 41.4 Aug 47.4 Sep -- **PENDING HOME SALES (10:00)** June -4.8% July -2.3% Aug --	**IP & CAP-U (9:15)** IP / Cap.Util. June 0.3% 76.2% July 0.2% 76.3% **Aug 0.2% 76.3%** **LEADING INDICATORS (10:00)** June -0.1% July 0.2% **Aug -0.1%**
21	22	23	24	25
CHICAGO FED NATIONAL ACTIVITY INDEX			**UNEMP. CLAIMS** **CURRENT ACCOUNT** **NEW HOME SALES**	**DURABLE GOODS ORDERS** **REVISED CONSUMER SENTIMENT**
28	29	30	1	2
	FHFA HOUSE PRICE INDEX **S&P COTALITY CASE-SHILLER 20-CITY HOME PRICE INDEX** **CONFERENCE BOARD CONSUMER CONFIDENCE** **JOLTS DATA**	**ADP EMPLOYMENT** **REVISED Q2 GDP** **PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** **INTERNATIONAL TRADE IN GOODS** **ADVANCE INVENTORIES** **MNI CHICAGO BUSINESS BAROMETER**	**UNEMP. CLAIMS** **ISM MFG. INDEX** **CONSTRUCTION** **VEHICLE SALES**	**EMPLOYMENT REPORT** **FACTORY ORDERS**

Forecasts in bold.

Treasury Financing

September/October 2026

Monday	Tuesday	Wednesday	Thursday	Friday
7	8	9	10	11
LABOR DAY	**AUCTION RESULTS:** Rate / Cover 13-week bills 3.800% 2.61 26-week bills 3.890% 2.88 6-week bills 3.740% 2.93 3-yr notes 4.474% 2.72 **ANNOUNCE:** $72 billion 17-week bills for auction on Sep 9 $90 billion 4-week bills for auction on Sep 10 $85 billion 8-week bills for auction on Sep 10 **SETTLE:** $72 billion 17-week bills $90 billion 4-week bills $85 billion 8-week bills	**AUCTION RESULTS:** Rate / Cover 17-week bills 3.895% 2.73 10-yr notes 4.834% 2.71	**AUCTION RESULTS:** Rate / Cover 4-week bills 3.775% 2.81 8-week bills 3.845% 2.82 30-yr bonds 5.308% 2.61 **ANNOUNCE:** $171 billion 13-,26-week bills for auction on Sep 14 $75 billion 6-week bills for auction on Sep 15 $13 billion 20-year bonds for auction on Sep 15 $19 billion 10-year TIPS for auction on Sep 17 **SETTLE:** $171 billion 13-,26-week bills $75 billion 6-week bills	
14	15	16	17	18
AUCTION: $171 billion 13-,26-week bills	**AUCTION:** $75 billion 6-week bills $13 billion 20-year bonds **ANNOUNCE:** $72 billion* 17-week bills for auction on Sep 16 $90 billion* 4-week bills for auction on Sep 17 $85 billion* 8-week bills for auction on Sep 17 **SETTLE:** $72 billion 17-week bills $90 billion 4-week bills $85 billion 8-week bills $58 billion 3-year notes $39 billion 10-year notes $22 billion 30-year bond	**AUCTION:** $72 billion* 17-week bills	**AUCTION:** $90 billion* 4-week bills $85 billion* 8-week bills $19 billion 10-year TIPS **ANNOUNCE:** $171 billion* 13-,26-week bills for auction on Sep 21 $75 billion* 6-week bills for auction on Sep 22 $69 billion* 2-year notes for auction on Sep 22 $70 billion* 5-year notes for auction on Sep 23 $44 billion* 7-year notes for auction on Sep 24 $28 billion* 2-year FRNs for auction on Sep 23	**SETTLE:** $13 billion 20-year bonds **SETTLE:** $171 billion 13-,26-week bills $75 billion 6-week bills
21	22	23	24	25
AUCTION: $171 billion* 13-,26-week bills	**AUCTION:** $75 billion* 6-week bills $69 billion* 2-year notes **ANNOUNCE:** $72 billion* 17-week bills for auction on Sep 23 $90 billion* 4-week bills for auction on Sep 24 $85 billion* 8-week bills for auction on Sep 24 **SETTLE:** $72 billion* 17-week bills $90 billion* 4-week bills $85 billion* 8-week bills	**AUCTION:** $72 billion* 17-week bills $70 billion* 5-year notes $28 billion* 2-year FRNs	**AUCTION:** $90 billion* 4-week bills $85 billion* 8-week bills $44 billion* 7-year notes **ANNOUNCE:** $171 billion* 13-,26-week bills for auction on Sep 28 $75 billion* 6-week bills for auction on Sep 29 $52 billion* 52-week bills for auction on Sep 29 **SETTLE:** $171 billion* 13-,26-week bills $75 billion* 6-week bills	**SETTLE:** $28 billion* 2-year FRNs
28	29	30	1	2
AUCTION: $171 billion* 13-,26-week bills	**AUCTION:** $75 billion* 6-week bills $52 billion* 52-week bills **ANNOUNCE:** $72 billion* 17-week bills for auction on Sep 30 $90 billion* 4-week bills for auction on Oct 1 $85 billion* 8-week bills for auction on Oct 1 **SETTLE:** $72 billion* 17-week bills $90 billion* 4-week bills $85 billion* 8-week bills	**AUCTION:** $72 billion* 17-week bills **SETTLE:** $19 billion 10-year TIPS $69 billion* 2-year notes $70 billion* 5-year notes $44 billion* 7-year notes	**AUCTION:** $90 billion* 4-week bills $85 billion* 8-week bills **ANNOUNCE:** $171 billion* 13-,26-week bills for auction on Oct 5 $75 billion* 6-week bills for auction on Oct 6 $58 billion* 3-year notes for auction on Oct 6 $39 billion* 10-year notes for auction on Oct 7 $22 billion* 30-year bonds for auction on Oct 8 **SETTLE:** $171 billion* 13-,26-week bills $75 billion* 6-week bills $52 billion* 52-week bills	

**Estimate*