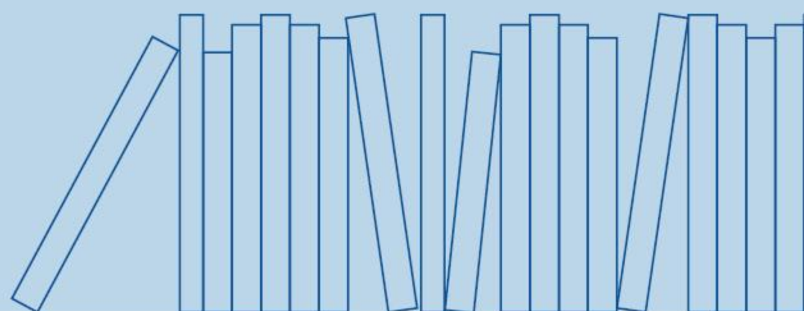
Economic Commission for Latin America and the Caribbean

ECLAC OFFICE IN WASHINGTON, D.C.

U.S. Economic Outlook

Quarterly developments



Washington, D.C., 6 july 2018

This document was prepared by Helvia Velloso, Economic Affairs Officer, under the supervision of Inés Bustillo, Director, ECLAC Washington Office.

The views expressed in this document, which has been reproduced without formal editing, are those of the authors and do not necessarily reflect the views of the Organization.

United Nations Publication
LC/WAS/TS.2018/5
Copyright © United Nations, July 2018. All rights reserved
Printed at United Nations

Contents

Highlights 5
Overview 7
I. Quarterly Developments 11
 A. GDP Growth 12
 B. Industrial production 14
 C. Labor market 15
 D. Inflation 17
 E. Monetary policy 19
 F. Financial conditions 20
 G. External sector 21
II. Recent U.S. trends and Latin American and Caribbean 23
III. Looking ahead 25

Highlights

- In the first quarter of 2018, the U.S. economy grew at an annualized rate of 2%, a slower pace than previously thought. The revised figure is the slowest pace in a year, but growth is expected to rebound in the current quarter.

- Growth was held back by the slowdown in consumer spending, which grew only 0.9% in the first quarter, after a 4% growth in the fourth quarter of last year.

- U.S. employers added 1,287,000 jobs during the first half of 2018. Unemployment rate was at 4% at the end of June.

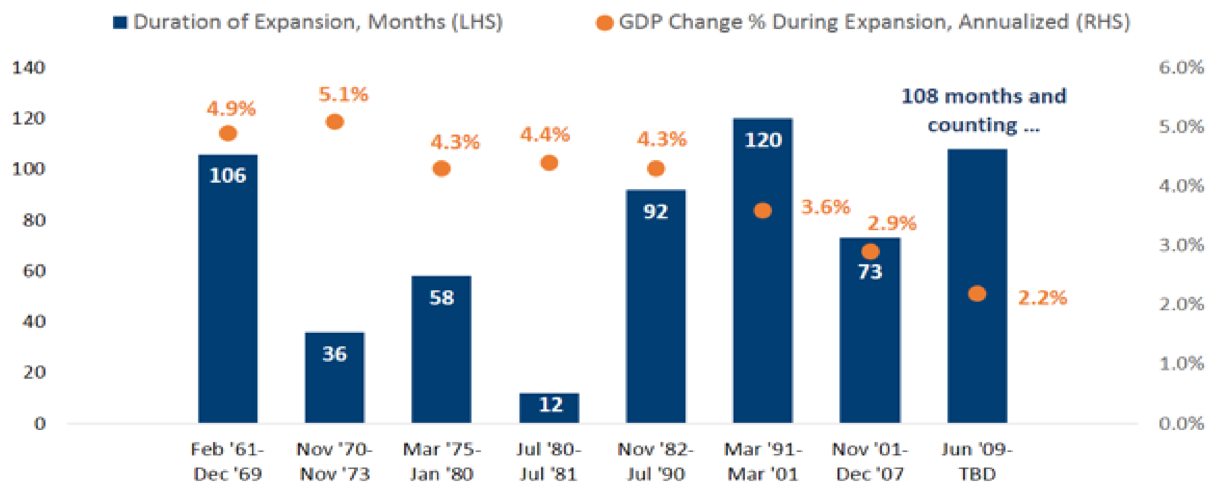
- Compared with its pace before the 2008 recession, productivity growth is disappointingly slow. On a year-ago basis, unit labor costs were up 1.1% in the first quarter while productivity increased 1.3%, indicating acceleration in wages that nevertheless falls short of prerecession rates.
- Over the last 12 months, the all items Consumer Price Index rose 2.8% before seasonal adjustment, continuing its upward trend since the beginning of the year. The core CPI was up 2.2% on the year.
- In May, the trade deficit in goods was smaller-than-expected, raising estimates of second-quarter U.S, growth. The trade deficit narrowed 3.7% in May from the prior month, as exports climbed 2.1% and imports rose a modest 0.2%.

- The Federal Open Market Committee (FOMC) raised interest rates by a quarter point two times in the first half of 2018 – in March and in June – and signaled that two more increases were on the way in the second half of the year, as Fed officials expressed confidence on the strength of the U.S. economy.

Overview

The U.S. economic expansion is nine years old and is about to enter its tenth year. June marked the 108th month of growth for the U.S. economy. It is now the second longest expansion on record and in one more year the current economic expansion may become the longest on record.[1] However, growth has been unusually shallow (chart 1). Some 59% of private-sector economists surveyed by the Wall Street Journal in May forecast that the expansion is most likely to end in 2020, as the Federal Reserve raises interest rates to cool off an overheating economy.

CHART 1:
THE CURRENT U.S. EXPANSION: LONG IN DURATION, SHALLOW IN MAGNITUDE

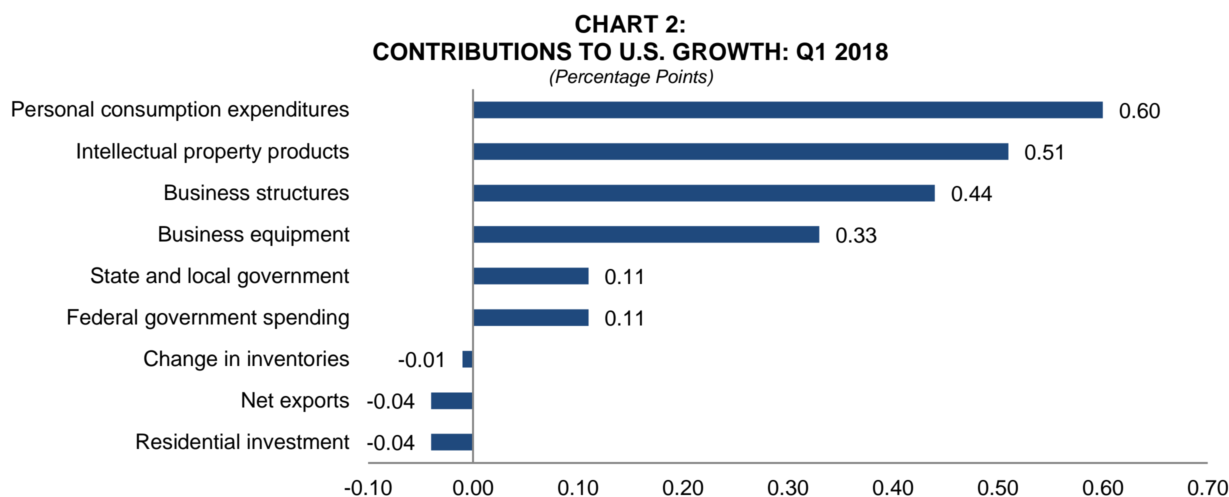


Source: Calamos Investments using data from U.S. Bureau of Economic Analysis. Billions of Chained 2009 dollars, quarterly GDP. https://seekingalpha.com/article/4184486-clock-ticking-u-s-economic-expansion

[1] The economic expansion that began in July 2009 is already the second-longest growth run in U.S. history, linger than the expansion in the 1960s; only the expansion of the 1990s is longer.

Gross domestic product expanded at a seasonally and inflation-adjusted annual rate of 2% in the first quarter of 2018, according to the Commerce Department's third and final estimate released at the end of June. First-quarter GDP was initially reported at 2.3%, but was revised down in subsequent months (to 2.2% and to 2% in April and May, respectively). Business investment (including intellectual property products, structures and equipment) was the main driver of growth (contributing 1.28% to growth in the first quarter), followed by consumer spending (which contributed 0.60% to growth), while inventories, net exports and residential investment were a drag (chart 2). Investment outside the housing market was stronger than earlier thought, growing by the fastest pace in about three years.

CHART 2:
CONTRIBUTIONS TO U.S. GROWTH: Q1 2018
(Percentage Points)



Source: Bureau of Economic Analysis, U.S. Department of Commerce

First-quarter growth figures have repeatedly disappointed in recent years, prompting economists to warn that seasonal-adjustment problems may be causing distortions. The Commerce Department has said it is working to address the issue. Analysts suggest that growth has picked up in the second quarter[2] and quarterly forecasts for the rest of the year show growth around 3% (table 1), with the balance of risks to the forecast on the upside. Economists think growth will remain robust throughout 2018, supported by the historically low unemployment rate and the effects of fiscal stimulus.

TABLE 1:
QUARTERLY FORECASTS FOR U.S. ECONOMIC GROWTH

	Q2 2018 (qoq)	Q3 2018 (qoq)	Q4 2018 (qoq)	Date of Forecast
What Markets Say				
Bank of America/Merrill Lynch	3.2%	3.6%	3.1%	Jun-18
J.P. Morgan	4.0%	2.5%	2.5%	Jun-18
Moody's Economy.com	3.7%	3.4%	3.3%	Jun-18
Mortgage Bankers Association	4.1%	2.7%	2.6%	Jun-18
National Association of Realtors	2.8%	2.7%	3.0%	Jun-18
National Bank of Canada	3.2%	3.1%	2.4%	Jun-18
TD Bank Financial Group	4.3%	2.7%	3.0%	Jun-18
Wells Fargo/Wachovia	4.2%	3.1%	3.0%	Jun-18
Forecasts average	***3.7%***	***3.0%***	***2.9%***	

Source: ECLAC Washington Office, based on several market sources.

[2] The Commerce Department will release second-quarter growth data at the end of July, along with comprehensive revisions of historical data. Economists are raising their estimates of second-quarter U.S. growth after government figures showing a smaller-than-expected trade deficit for May were released on June 27.

In Mid-June, The FOMC meeting was perceived by market participants as more hawkish than previously anticipated. The committee unanimously voted to raise the fed funds target rate by 25 basis points, to a range of 1.70-2.00%. Moreover, the Fed's median 2018 and 2019 rate projections increased relative to the March FOMC projected path, to 2.4% and 3.1%, respectively – implying four hikes in total for 2018, three for 2019, and one for 2020, versus three, three, and two hikes, respectively, as of the March meeting. The description of the economy was also upgraded, as were staff forecasts for growth and inflation in 2018.

The U.S. economy grew 2.3% in 2017, and growth is now expected to accelerate to close to 3% this year, according to forecasters (table 2). U.S. consumer price inflation was 2.1% last year, but according to market projections, the CPI is expected to increase at a 2.5% rate on average in 2018.

Although forecasters do not envision a recession beginning within the next year, there are reasons for caution. The labor market is at full strength, asset prices are frothy, monetary policy is tightening, and rising trade tensions have increased anxiety among investors, who worry that profits and equity performance may have already peaked. U.S. companies are facing more challenges now than when they announced their first-quarter earnings results. Much of the concern early this year was centered on threats to profit margins from rising commodity costs, led by oil, and wage pressure. Now trade tensions and a rising dollar have been added to their concerns.

In addition, in what is becoming a big topic in Wall Street, the widely watched "yield curve" is getting close to predicting a recession, something it has done before with surprising accuracy. The yield curve is the difference between interest rates on short-term U.S. government bonds (two-year Treasury notes) and long-term government bonds (10-year Treasury notes). When an economy seems to be in good health, the rate on long-term bonds is higher than on short-term ones. Lately, however, even as the economy is showing strength, long-term bond yields have been slow to rise, suggesting traders are concerned about long-term growth. At the same time, the Fed has been raising short-term rates, so the yield curve has been "flattening." If the curve keeps moving in this direction, eventually long-term interest rates will fall below short-term rates. On July 3, the gap between 2 and 10-year Treasury yields reached its lowest level in more than ten years, dipping below 30 basis points for the first time since August 2007, as trade tensions continue to bolster U.S. government bond prices.

The yield curve helps determine some crucial decisions to the health of the economy. A flattening curve makes bank lending less profitable, and if the flow of lending is curtailed, economic activity will be impacted. However, some see the yield curve today as a less reliable indicator than in the past, because of central banks' bond purchasing in recent years, arguing that central banks, rather than the markets, have had a bigger influence on both the long-term and short-term rates.

TABLE 2:
ANNUAL FORECASTS FOR U.S. ECONOMIC GROWTH

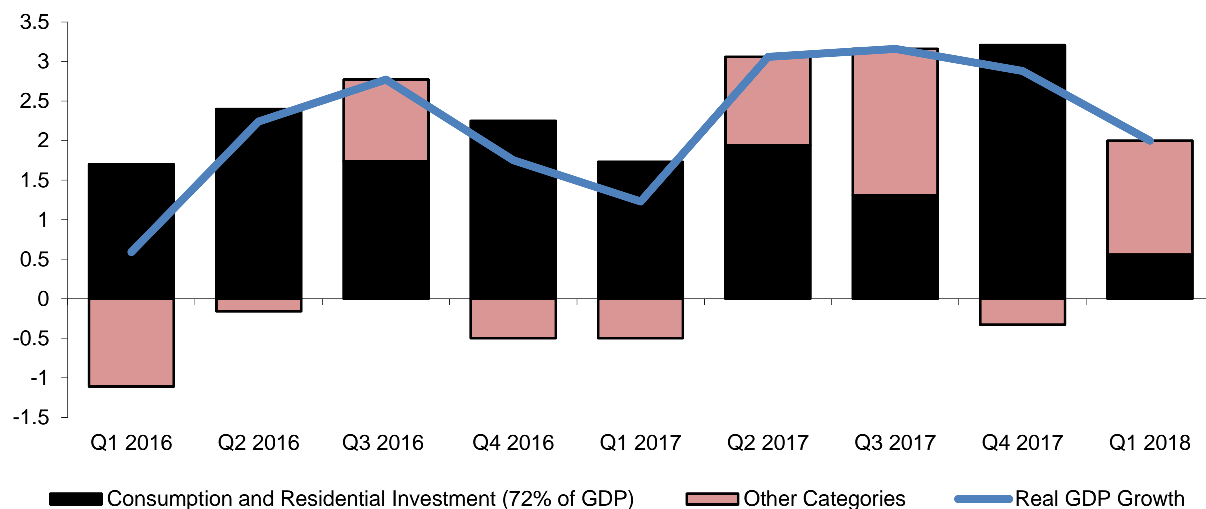
	Real GDP (% change, y/y)		CPI (% change, y/y)		Unemployment Rate (%)		FED Funds Rate (%)		
	2018	**2019**	**2018**	**2019**	**2018**	**2019**	**2018**	**2019**	**Date of Forecast**
A. What Government Agencies Say									
FED*	2.8%	2.4%	2.1%	2.1%	3.6%	3.5%	2.4%	3.1%	*Jun-18*
CBO	3.0%	2.9%	2.2%	2.2%	3.8%	3.3%	1.9%	3.1%	*Apr-18*
OMB	3.1%	3.2%	1.9%	2.0%	3.9%	3.7%	*na*	*na*	*Feb-18*
B. What Markets Say									
Bank of America/Merrill Lynch	2.9%	2.4%	2.5%	2.2%	3.8%	3.3%	2.38%	*3.13%*	*Jun-18*
JPMorgan	2.9%	*na*	2.6%	*na*	3.8%	*na*	2.50%	*na*	*Jun-18*
Moody's Economy.com	3.0%	2.6%	2.7%	2.5%	3.8%	3.3%	1.90%	3.40%	*Jun-18*
Mortgage Bankers Association	2.9%	2.3%	2.5%	2.3%	3.8%	3.6%	2.38%	3.13%	*Jun-18*
National Association of Realtors	2.6%	2.7%	3.1%	2.7%	4.0%	4.0%	1.80%	2.60%	*Jun-18*
National Bank of Canada	2.8%	2.3%	2.5%	2.3%	3.9%	3.6%	2.25%	3.00%	*Jun-18*
TD Bank Financial Group	3.0%	2.8%	2.5%	2.1%	3.8%	3.6%	2.50%	3.25%	*Jun-18*
The Economist Intelligence Unit	2.7%	2.5%	2.4%	2.4%	3.9%	3.7%	*2.10%*	*3.10%*	*Jun-18*
Wells Fargo/Wachovia	3.0%	2.8%	2.1%	2.3%	3.9%	3.6%	2.13%	2.75%	*Jun-18*
Market Average	***2.9%***	***2.6%***	***2.5%***	***2.4%***	***3.9%***	***3.6%***	***2.2%***	***3.0%***	
C. What International Organizations Say									
United Nations DESA (Baseline)	2.5%	2.3%	*2.1%*	*2.1%*	*4.0%*	*3.7%*	*na*	*na*	*Dec-17/May-18*
World Bank	2.7%	2.5%	*na*	*na*	*na*	*na*	*na*	*na*	*Jun-18*
OECD	2.9%	2.8%	2.2%	2.2%	3.9%	3.6%	*na*	*na*	*May-18*
IMF*	2.9%	2.7%	2.5%	2.4%	3.9%	3.5%	*na*	*na*	*Apr-18*

Source: ECLAC Washington Office based on official and market sources.
Note: FED: Federal Reserve; CBO: Congressional Budget Office; OMB: Office of Management and Budget (U.S. Administration's forecasts).
*Forecast for PCE inflation.

I. Quarterly Developments

U.S growth slowed in the first quarter of 2018, but first-quarter growth figures have repeatedly disappointed in recent years, prompting warnings that seasonal-adjustment problems may be causing distortions. The contribution of the core of the U.S. economy – consumption and residential investment – lowered considerably in the first three months of 2018, held back by the slowdown in consumer spending, which contributed only 0.6% to growth compared to a contribution of 2.75% in the fourth quarter of 2017, while residential investment subtracted -0.04% from first-quarter growth (chart 3). On the positive side, however, business investment was a driver of economic growth, contributing 1.28%.

CHART 3:
CONTRIBUTIONS TO U.S. REAL GDP GROWTH
(Percentage Points)

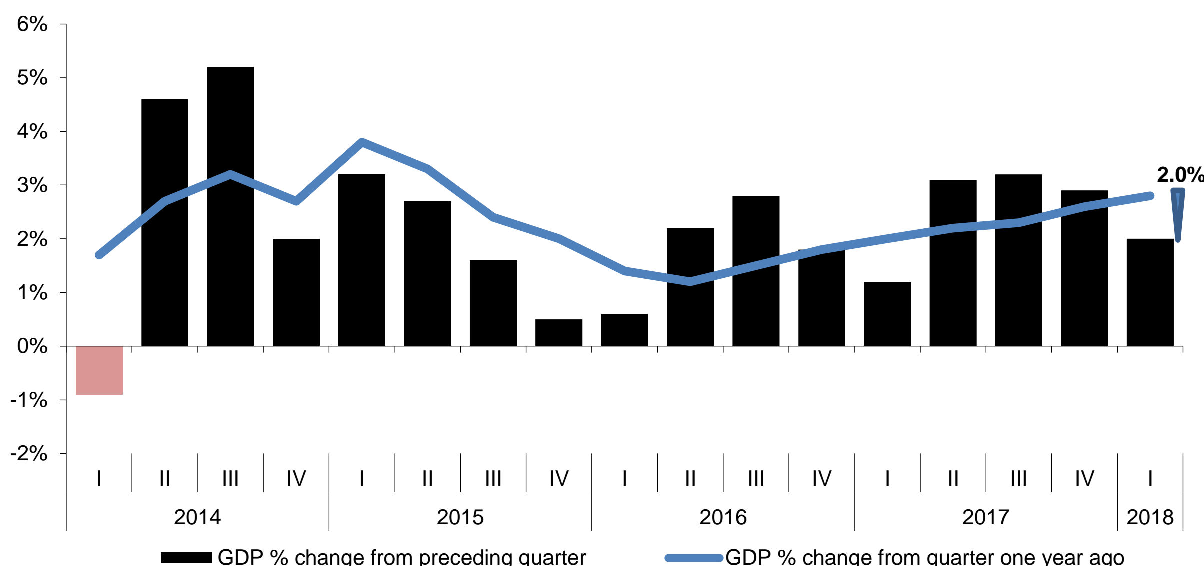


Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.
Note: Contributions to growth are measured at seasonally adjusted annual rates.

A. GDP Growth

According to the third estimate released by the U.S. Department of Commerce on 28 June 2018, the U.S. economy grew at an annual rate of 2% in the first quarter, following an increase of 2.9% in the previous quarter. It has followed a similar pattern to recent years, with a sharp slowdown early in the year. This was the slowest quarterly pace in a year (chart 4). Growth is expected to rebound in the second quarter, despite growing trade tensions. According to the Commerce Department, the deceleration in real GDP growth in the first-quarter reflected decelerations in personal consumption expenditure, exports, state and local government spending, federal government spending, and a downturn in residential fixed investment. These movements were partly offset by a smaller decrease in private inventory investment and a larger increase in nonresidential fixed investment. Imports, which are a subtraction in the calculation of GDP, decelerated.

CHART 4:
U.S. REAL GDP: QUARTERLY GROWTH
(Percentage Points)

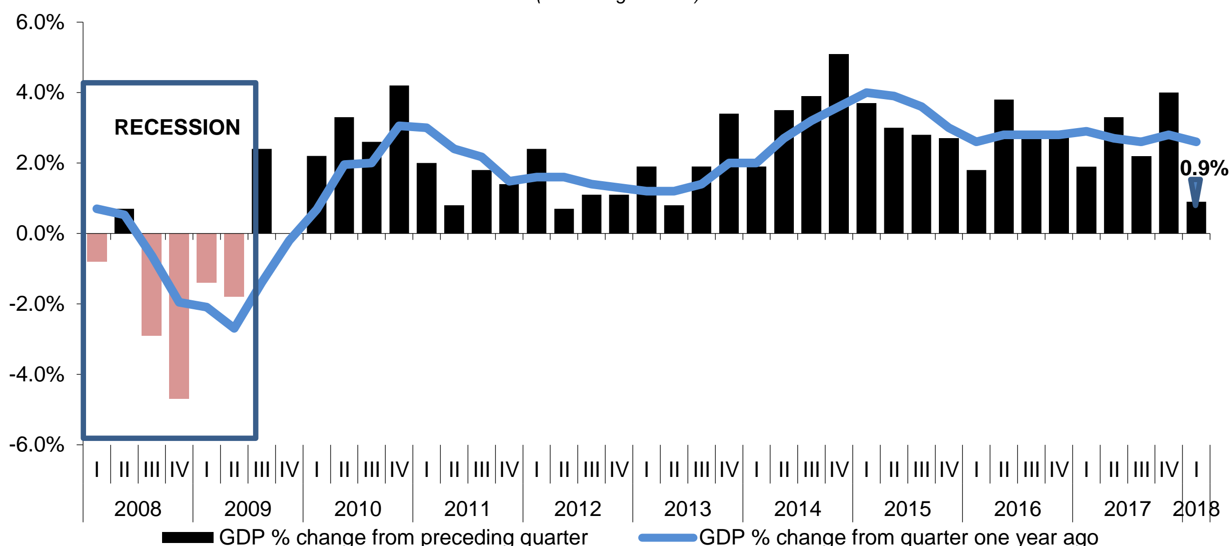


Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

The largest component of GDP, real personal consumption expenditures, grew only 0.9% in the first quarter, after increasing of 4% in the fourth quarter of 2017 (chart 5). Consumer spending was a modest driver of growth, contributing 0.60% to growth. This was sharply down from the 2.75% contribution in the fourth quarter. Consumers spent less on services than previously thought, with health-care purchases by nonprofits and spending on finance and insurance services weaker than had been previously reported.

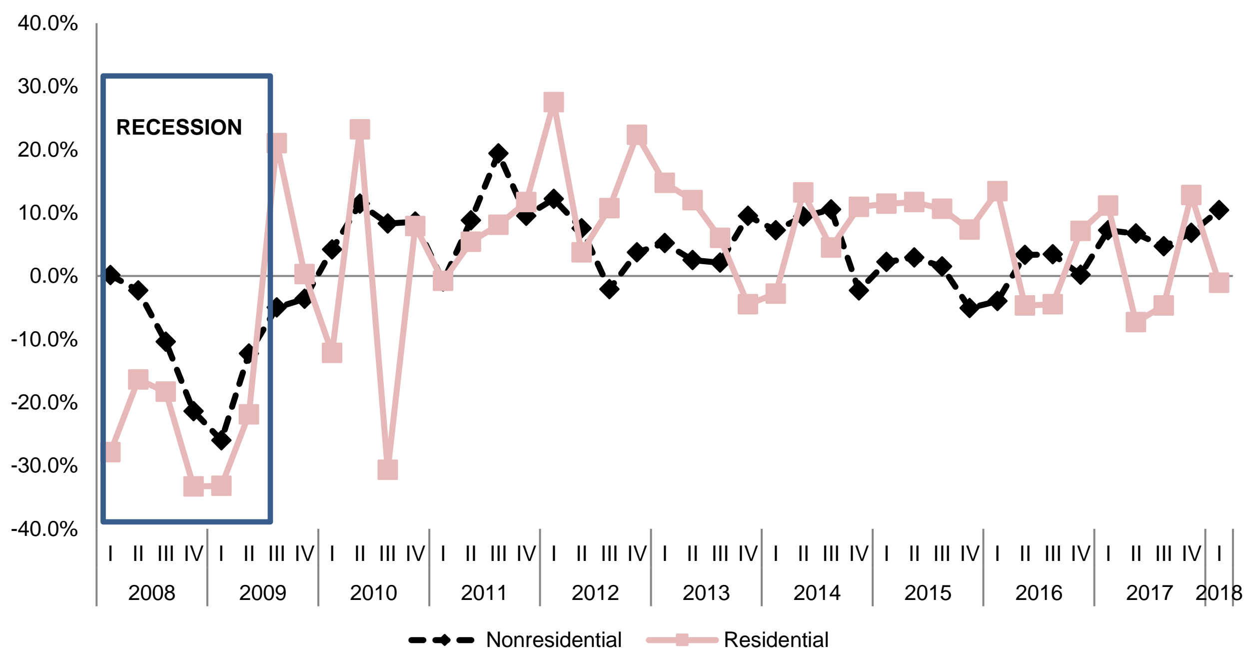
Fixed investment was the largest contributor, adding 1.2% to growth in the first quarter, led by intellectual property and equipment investment. Fixed investment was the main driver of growth in the first quarter. The change in private inventories subtracted 0.01% from the first quarter change in real GDP, after subtracting 0.53% from growth in the previous quarter. Overall, gross private domestic investment increased at a 7.5% annual rate in the first quarter, adding 1.22% to first-quarter GDP growth (with 1.23% due to business fixed investment – 1.28% from nonresidential and -0.04% from residential – and -0.01% due to inventories).

CHART 5:
PERSONAL CONSUMPTION EXPENDITURE: QUARTERLY GROWTH
(Percentage Points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

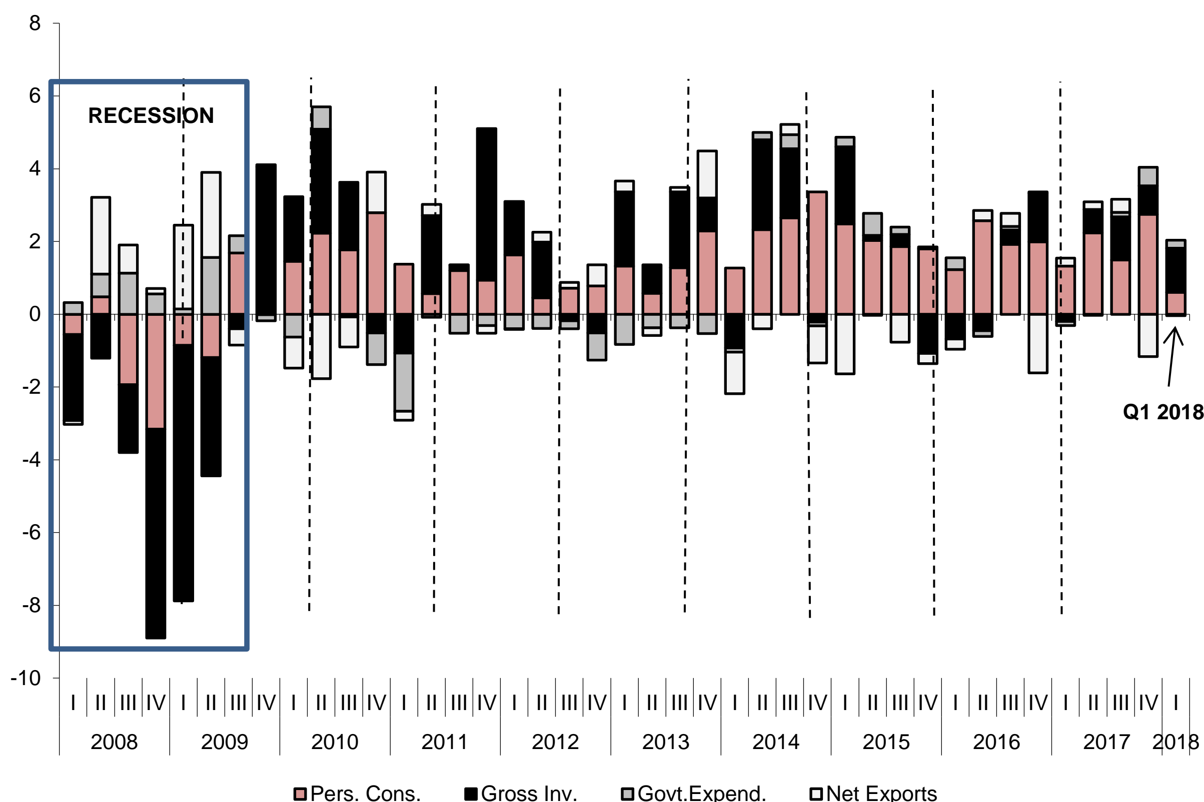
CHART 6:
GROSS PRIVATE DOMESTIC INVESTMENT: QUARTERLY GROWTH
(Percentage Points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.

Overall, government spending increased 1.3% and added 0.22% to growth in the first quarter. State and local government spending increased 1% and federal outlays increased 1.7% in the first quarter (national defense spending increased 1.8%, while nondefense spending increased 1.6%). Finally, net exports subtracted 0.04% from growth in the first quarter. Exports increased 3.6% and imports 3.2%, adding 0.44% to and subtracting 0.48% from first-quarter growth, respectively (chart 6).

CHART 6:
CONTRIBUTIONS TO REAL GDP GROWTH
(Percentage Points)



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Department of Commerce.
Note: Contributions to growth are measured at seasonally adjusted annual rates.

In summary, the third estimate of GDP growth in the first quarter was revised down, but according to several closely watched models that track economic output it seems that the U.S. economy has picked up steam in the second quarter. Despite the moderation in first-quarter growth, the U.S. expansion enjoyed its ninth birthday in June. The U.S. expansion has been remarkably stable in recent years. With the economy seemingly at full employment and monetary policy expected to tighten further, the expansion is likely entering its later stages.

B. Industrial production

Industrial production decreased 0.1% in May, marking the first decline since January. On the positive side, the change for April was revised up to 0.9% from the 0.7% previously reported (table 3). Overall, industrial production stands 3.5% higher over that of a year earlier. Manufacturing output decreased 0.7% and was the main reason for the weak top line, but the change for April was revised higher. Manufacturing production was up 1.7% on a year-ago basis. Mining output advanced 1.6%, whereas utilities output rose 0.4%. Capacity utilization edged 0.1 percentage point lower.

The ISM manufacturing index unexpectedly gained 1.5 points to 60.2 in June, driven by a surge in the index of supplier deliveries (from 62 to 68.2), likely reflecting firms' efforts to front-load production

ahead of the imposition of tariffs. Historically an ISM index above 60 is difficult to sustain, and supply constraints are an issue. It is increasingly likely that the trade tensions will escalate, adding to the sector's economic costs. Another reason why economic costs could increase is that these tariffs are on top of the expanded steel and aluminum tariffs, which are only beginning to affect costs through the supply chain.

TABLE 3:
U.S INDUSTRIAL PRODUCTION

	Total Industrial Production		**Capacity Utilization Rate**
	Index 2012=100	Percentage Change From Previous Period	Total Industry (%)
2017 Q4	**105.3**	**7.7**	**77.0**
October	104.8	1.5	76.8
November	105.3	0.5	77.1
December	105.8	0.5	77.3
Annual	**103.7**	**1.6**	**76.1**
2018 Q1	**105.9**	**2.4**	**77.2**
January	105.4	-0.3	77.0
February	105.9	0.4	77.2
March	106.4	0.5	77.5
2018 Q2			
April	107.4	0.9	78.1
May	107.3	-0.1	77.9

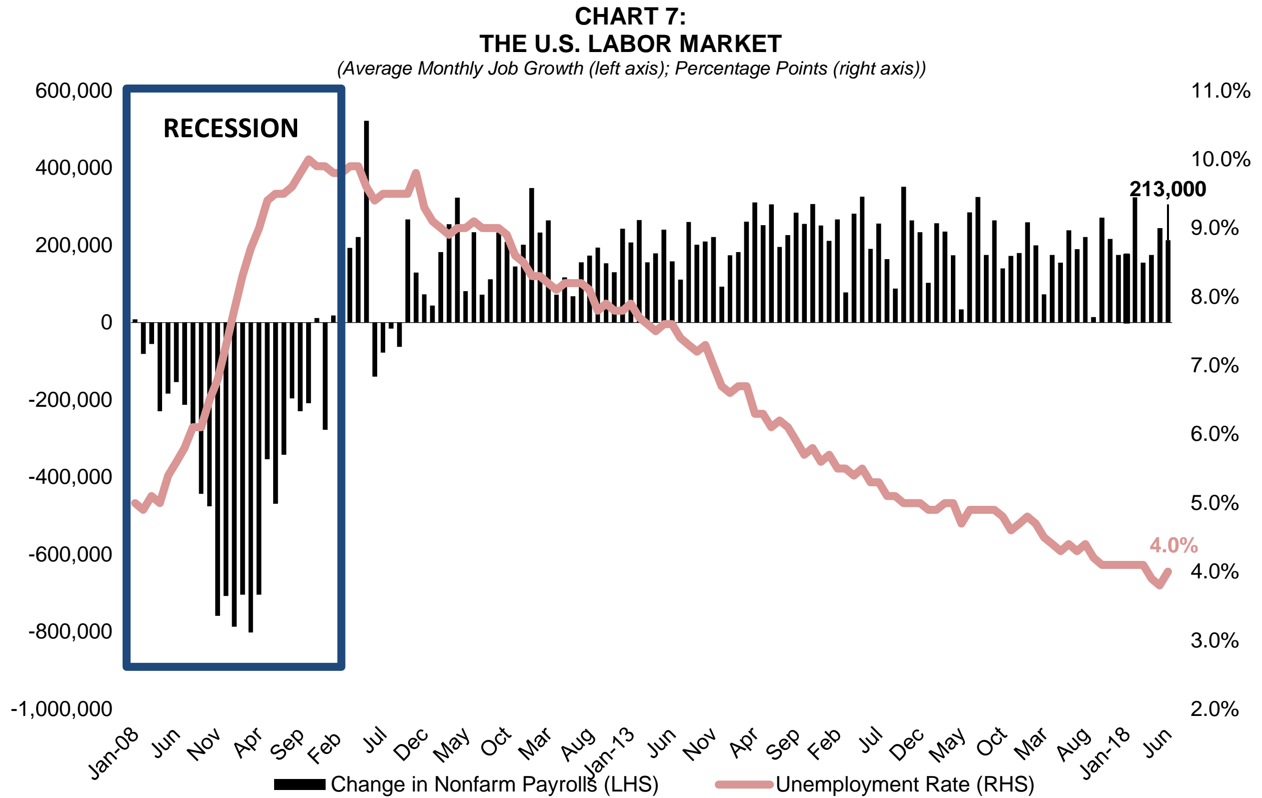
Source: ECLAC Washington Office, based on data from U.S. Federal Reserve, Industrial Production and Capacity Utilization
Note: Quarterly changes are at annual rates. Annual changes are calculated from annual averages.

C. Labor market

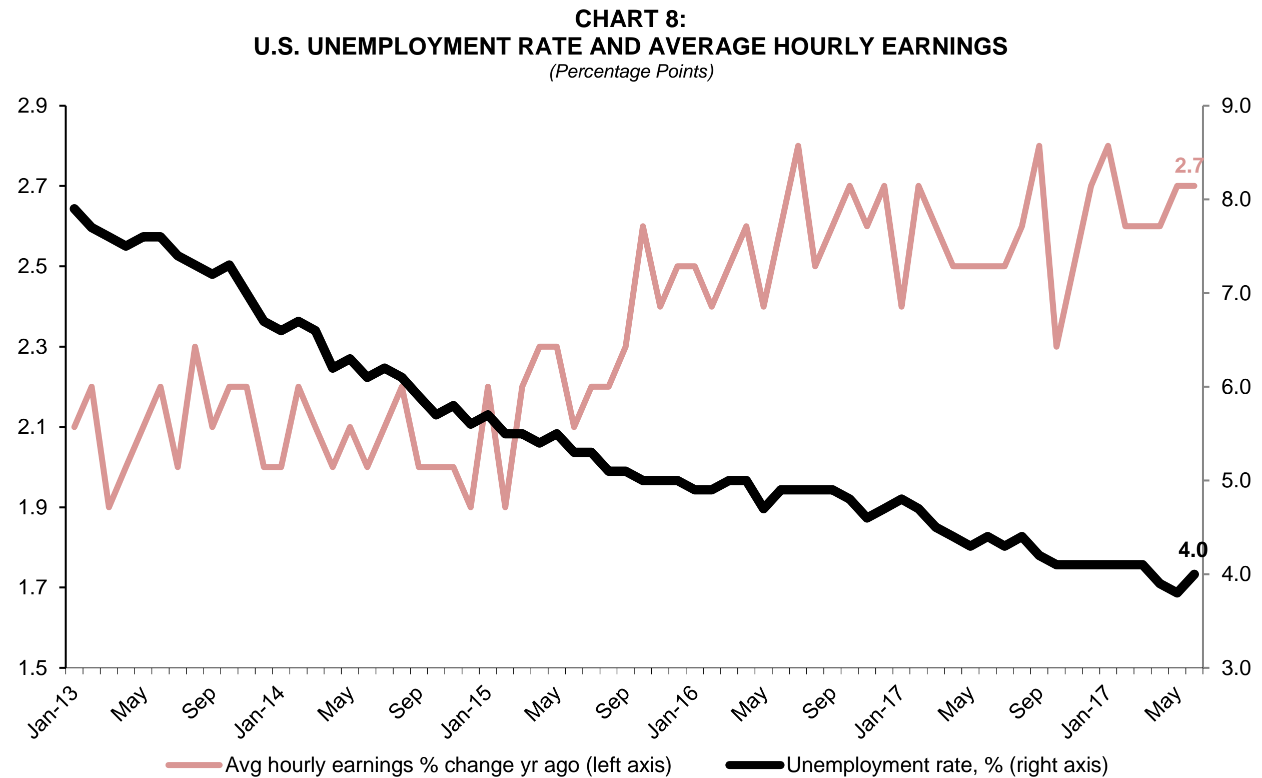
The U.S. economy added 213,000 jobs in June, exceeding expectations. This follows growth of 175,000 and 244,000 in April and May, respectively, both revised upward from 159,000 and 223,000. Trend job growth is solid, averaging 214,500 over the past six months and 197,800 over the past 12 months. The average jobs growth for the first quarter of 2018 was 218,000 a month. The unemployment rate edged higher from an 18-year low of 3.8% to 4% (chart 7), as the labor force participation rate rose by 0.2 percentage point to 62.9%. The rate is up slightly from a recent low of 62.3% in 2015, but still near the smallest share of adults participating since the late 1970s. Average hourly earnings rose 0.3%, up 2.7% on a year-ago basis in May, and 0.19% in June, slightly weaker than expected. As a result, over the year gains were unchanged at 2.7%. (chart 8).

Revisions show that productivity growth in the first quarter was not as strong as previously believed. Nonfarm labor productivity was revised down from 0.7% to 0.4%. The lower productivity comes as hours were revised up and output was revised down (table 4, chart 9). On a year-ago basis, unit labor costs were up 1.1% in the first quarter while productivity increased 1.3%, indicating acceleration in wages that nevertheless falls short of prerecession rates.

Volatility in productivity from quarter to quarter and even year to year makes identification of underlying trends difficult. Nevertheless, Moody's Analytics has suggested that two general trends are relatively clear. Compared with its pace before the recession, productivity growth is disappointingly slow. This trend has significant consequences for long-term well-being and wage growth, as how much output an economy produces for the given level of inputs is crucial for economic growth. The second trend is that productivity has improved from the worst point in the recession.



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.



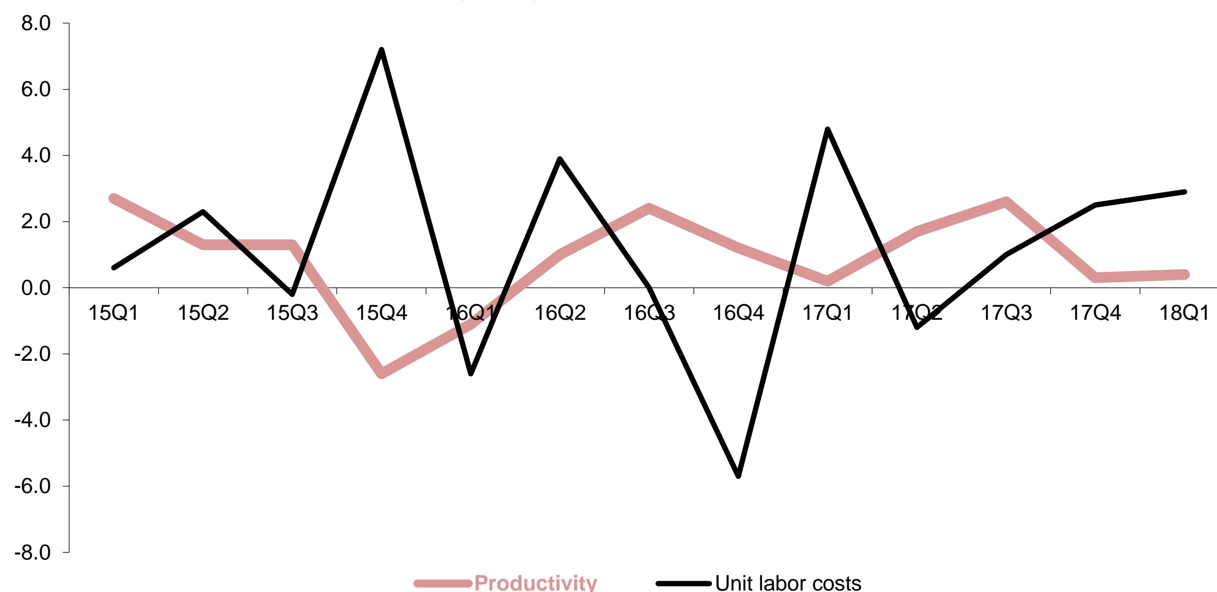
Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

TABLE 4:
U.S. PRODUCTIVITY AND COSTS
Revised first quarter 2018 annual averages
(Seasonally adjusted annual rates)

Sector	Labor productivity	Output	Hours worked	Hourly compensation	Real hourly compensation	Unit labor costs
		Percent change from preceding quarter				
Nonfarm business	0.4	2.7	2.3	3.3	-0.2	2.9
Business	0.7	2.6	1.8	3.9	0.4	3.1
Manufacturing	-1.2	1.7	2.9	3.9	0.4	5.2
Durable	-0.8	3.3	4.2	5.8	2.2	6.7
Nondurable	-0.9	0.0	0.9	0.0	-3.4	0.9

Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

CHART 9:
U.S. NONFARM BUSINESS SECTOR: PRODUCTIVITY VS UNIT LABOR COSTS
(Percentage Change from Previous Quarter at Annual Rates)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

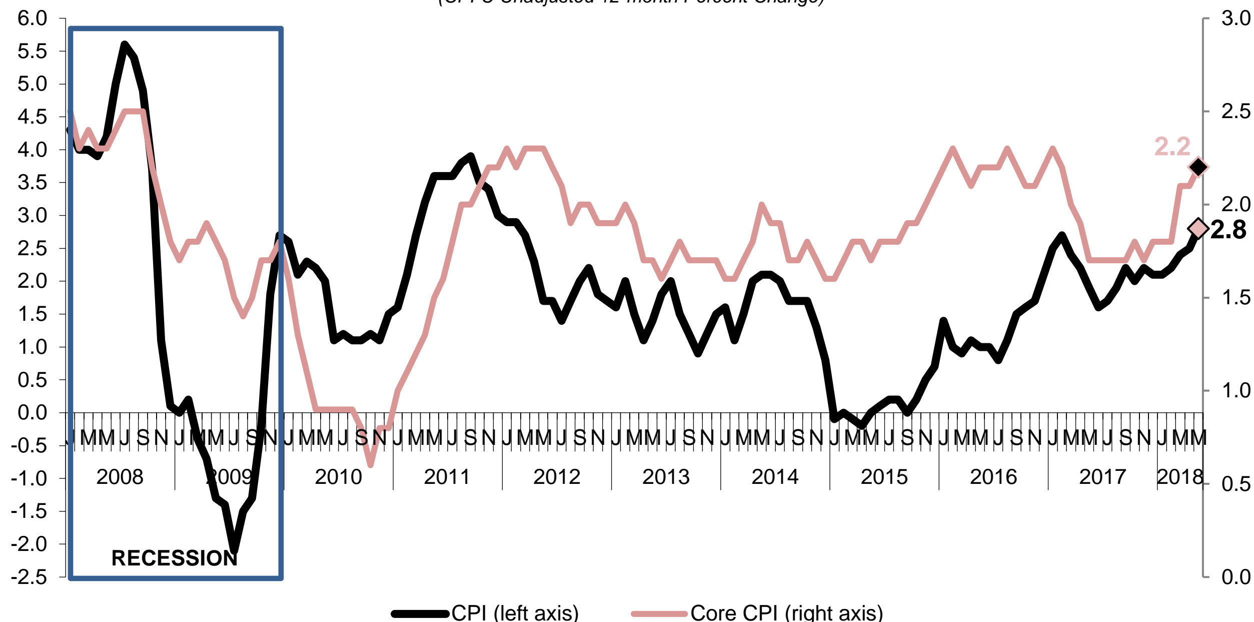
D. Inflation

In May, the Consumer Price Index for All Urban Consumers (CPI-U) increased 0.2% on a seasonally adjusted basis, after posting a 0.2% gain in April. The CPI for energy were up 0.9% in May, led by the gasoline index, which increased 1.7%, more than offsetting declines in some of the other energy component indexes. Food prices were unchanged. Over the last 12 months, the all items index rose 2.8% before seasonal adjustment, continuing its upward trend since the beginning of the year. The index for all items less food and energy rose 2.2% for the 12 months ending May (chart 10).

The most closely watched measure by the Federal Reserve – the Personal Consumption Expenditure (PCE) core price index– increased at an annualized 1.6% in the first quarter. In May, the core PCE advanced at 2% (chart 11). Year-over-year growth in the core PCE deflator was 0.3 percentage point

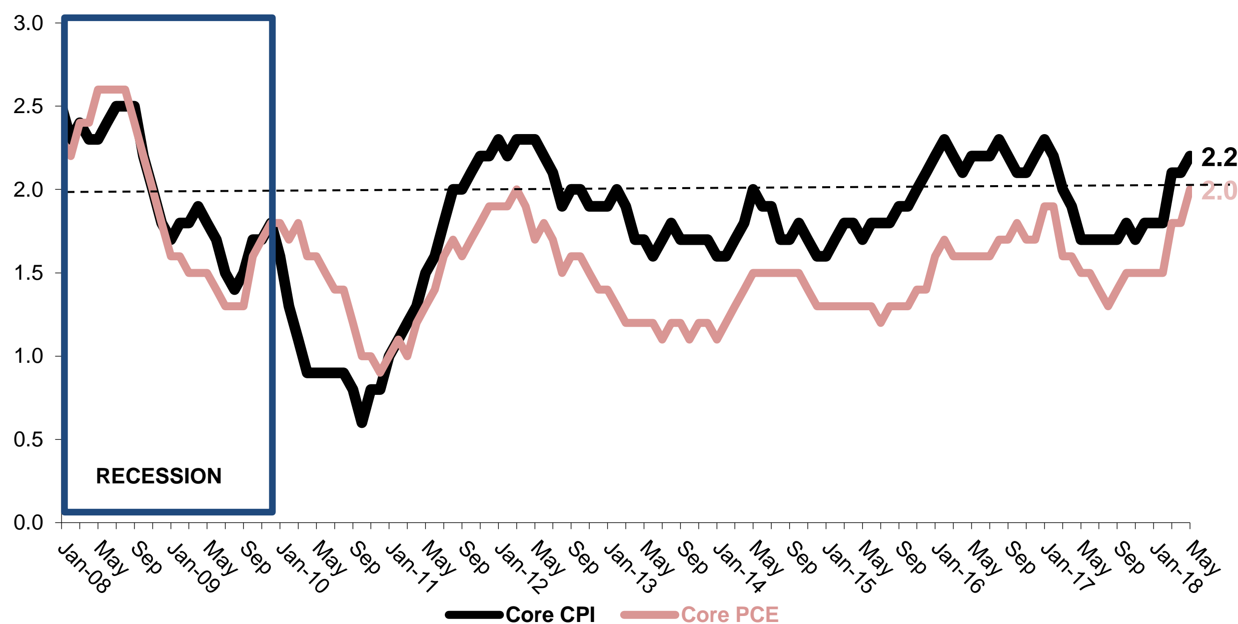
below the core CPI, less than its historical average of 0.5 percentage point, according to Moody's. Growth in the core PCE deflator has clearly accelerated, as it was up 1.5% on a year-ago basis in May 2017.

CHART 10:
U.S. DOMESTIC PRICES: MONTHLY EVOLUTION
(CPI-U Unadjusted 12-month Percent Change)



Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics.

CHART 11:
U.S. CORE CONSUMER PRICE INDICES
(Year-over-year Percentage Change)



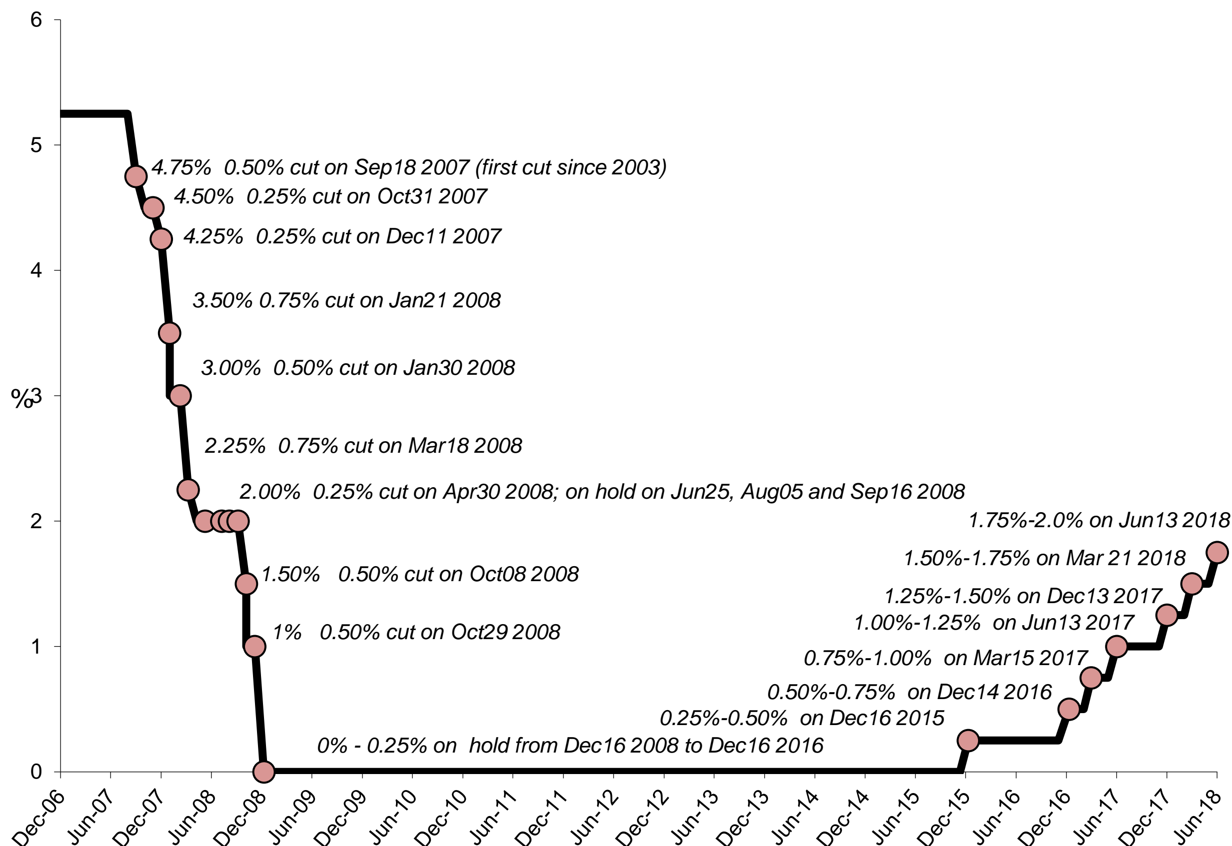
Source: ECLAC Washington Office, based on data from the U.S. Bureau of Labor Statistics (BLS), Department of Labor and the Bureau of Economic Analysis (BEA), U.S. Department of Commerce.

PCE, which is published by the U.S. Commerce Department’s Bureau of Economic Analysis, is derived from retail-sales data collected in business surveys, and in this data, medical care tends to carry the greatest weight. The CPI, on the other hand, is derived from consumer purchases reported in household surveys. Typically, consumers report spending more on shelter than anything else, giving that category more weight in the CPI. Since shelter costs have been rising, the core CPI has been been increasing faster than the core PCE.

E. Monetary policy

The Federal Open Market Committee (FOMC) raised the target range for the fed funds rate in March and June (chart 12). In June, the Committee raised the target rate to a range of 1.75%-2% and dropped the forward guidance from its post-meeting statement. Gone is “the federal funds rate is likely to remain, for some time, below levels that are expected to prevail in the longer run.” Monetary policy continues to be characterized as “accommodative,” even after June's hike, and the outlook still calls for “further gradual increases” in the funds rate. The statement also no longer describes inflation expectations being low. In addition, the central tendency forecast showed a lower unemployment rate this year and a total of four rate hikes. The longer-run projection for unemployment remained at 4.5% while the central tendency forecast for the actual unemployment rate is expected to be 3.5% through 2020. There was also a technical adjustment to the interest paid on excess reserves.

CHART 12:
U.S. FEDERAL FUNDS TARGET RATE
(Percentage)



Source: ECLAC Washington Office, based on data from the U.S. Federal Reserve.

The new Summary of Economic Projections showed modest changes to GDP growth this year, now showing a 2.8% gain, compared with 2.7% in March. The central tendency for where the unemployment rate will average in the fourth quarter of this year fell from 3.8% in the March projections to 3.6%. The central tendency forecast for the unemployment rate in 2019 and 2020 were reduced by 0.1 percentage point. The central tendency for where the headline PCE inflation and the core PCE inflation will average this year increased from 1.9% in March to 2.1% and 2.0%, respectively.

F. Financial conditions

Wall Street's optimism over strong earnings growth for U.S. companies in the first quarter has been replaced by anxiety that profits have already peaked. Companies are facing more challenges now, including trade tensions and a rising dollar.

In the first quarter of 2018, the Dow Jones Industrial Average, the S&P 500, and NASDAQ gained 0.15%, 1.44%, and 6.12%, respectively. In the first five months of the year they gained 0.11%, 1.39% and 6.53%, respectively (table 5). U.S. Treasury security yields gained more, especially short-term maturities. The difference between the short-term and longer-term yields are thus compressing, meaning the yield curve has been "flattening," which has previously been a strong predictor of recessions. In the first five months of 2018, 3-year Treasury yields gained 35.71%, while 10-year and 30-year Treasury yields gained 24.17% and 13%, respectively.

U.S. dollar denominated high-yield corporate bond issuance is expected to be lower than in 2017. High-yield spreads have remained stable, despite the significant widening of spreads in the investment grade sector, partly due to relatively low supply of new high-yield bonds. Higher funding costs have made issuers more cautious about increasing their debt. Moreover, more borrowers are favoring the leveraged loan market, which has grown larger than the high-yield bond market.

TABLE 5:

STOCK PRICES Monthly Stock Prices			
2017	**Dow Jones Industrial Average**	**S&P 500**	**Nasdaq**
December	24,545.38	2,664.34	6,889.74
2018			
January	25,804.02	2,789.80	7,279.50
February	24,981.55	2,705.16	7,161.77
March	24,582.17	2,702.77	7,311.51
April	24,304.21	2,653.63	7,084.14
May	24,572.53	2,701.49	7,339.33

U.S. TREASURY SECURITY YIELDS Constant Maturities	Monthly Yields		
2017	**3-year**	**10-year**	**30-year**
December	1.96	2.4	2.77
2018			
January	2.15	2.58	2.88
February	2.36	2.86	3.13
March	2.42	2.84	3.09
April	2.52	2.87	3.07
May	2.66	2.98	3.13

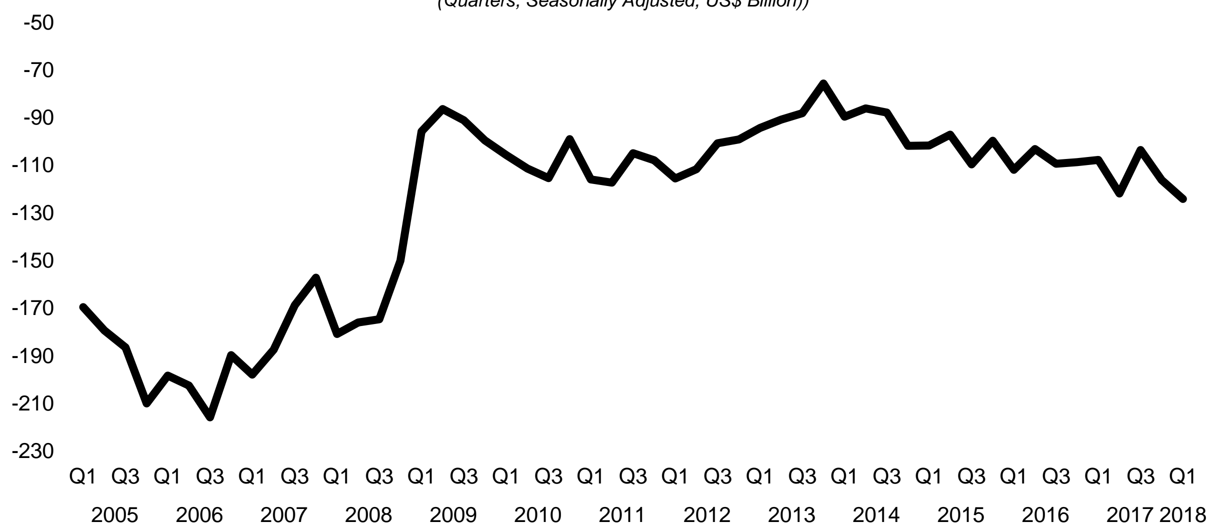
Source: Economic Indicators, U.S. Government

Regarding the banking sector, on June 28 the Federal Reserve Board announced it had completed its review of the capital planning practices of the nation's largest banks and did not object to the capital plans of 34 bank holding companies (out of 35) participating in the Comprehensive Capital Analysis and Review (CCAR). The Fed failed the U.S. unit of Deutsche Bank (for "qualitative reasons"), while three U.S. banks' capital return plans passed with conditions. Stress test scenarios were harsher this year than last. Now in their eighth year, the stress tests are intended to give the public confidence that banks are better prepared for the next crisis.

G. External sector

The U.S. current account deficit, the broadest measure of net exports to the rest of the world because it includes income payments and government transfers in addition to foreign trade, widened to US$ 124.1 billion in the first quarter of 2018, an increase of US$ 8 billion. Although this was a smaller quarterly increase than expected, the deficit was the largest since 2008. The wider deficit was largely the result of an US$ 8.1 billion increase in the goods deficit, the largest component of the current account. As a share of GDP, the current account deficit rose to 2.5% from a revised 2.4% in the prior quarter.

CHART 13:
U.S. BALANCE ON CURRENT ACCOUNT
(Quarters, Seasonally Adjusted, US$ Billion))



Source: ECLAC Washington Office, based on data from the Bureau of Economic Analysis, U.S. Commerce Department.

However, the Commerce Department reported at the end of June that the trade deficit in goods (the largest component of the current account) narrowed 3.7% in May from April, as exports climbed 2.1% and imports rose a more modest 0.2%. The nominal goods deficit has now narrowed for three months in a row, following seven consecutive months of widening. Analysts say that as a result, it seems trade will make a significant contribution to growth in the second quarter.

There remain considerable uncertainties surrounding trade policies, but it is increasingly likely that the trade tensions will escalate, adding to economic costs. Tariffs against imports of solar panels and washing machines were in effect through most of the first quarter, and steel and aluminum tariffs against a limited number of countries came into effect near the end of the quarter. These tariffs may ultimately translate to higher consumer prices and raise the costs of many businesses’ inputs.

II. Recent U.S. trends and Latin American and Caribbean

Despite record debt sales by issuers from Latin America and the Caribbean in the first quarter of 2017, a resurgent dollar alongside rising short-term U.S. interest rates has started to shake investors' confidence in emerging market assets in the second quarter. The U.S. dollar's durable rally and expectations of strong U.S. growth are upending investments across the globe, punishing commodities and emerging markets while attracting more overseas money to the U.S. Because the dollar is the world's main currency, any significant change in its value and outlook can have an important impact on financial markets.

The Federal Reserve raised interest rates two times in the first half of this year, and has signaled that it can raise interest rates two times more in the second half of the year, which would increase pressure on emerging and Latin American and Caribbean (LAC) assets and test the ability of some issuers to repay dollar-denominated debt. Higher U.S. interest rates dim the allure of LAC assets, where investors often take on greater risk in exchange for higher yields and returns. Higher U.S. interest rates together with the unwind of the Fed's balance sheet would support a continuation of the appreciation of the dollar. Withdrawal of dollar liquidity through the Federal Reserve balance sheet unwinding – which is absorbing U.S. dollars, currently at a pace of US$ 20 billion a month – and the ensuing strengthening of the U.S. dollar, are among the main concerns for LAC financial assets in the second half of 2018.

U.S. trade policy is expected to add to the pressure on LAC assets. A fresh round of U.S. tariffs is due to be implemented on July 6, which combined with retaliation measures from U.S. trade partners will likely lead to additional volatility in debt, equity and commodity markets.

III. Looking ahead

The U.S. economy slowed down at the beginning of the year, but since then incoming data has been more positive, and forecasts say growth in the second quarter has picked up significantly. Market projections for real GDP growth in 2018 (made mostly in June), now range from 2.7% to 3% (see table 2). On average, growth in 2018 is expected to expand at an annual pace of 2.9%, what compares to growth of 2.3% in 2017. Market projections for real GDP growth in 2019 currently range from 2.3% to 2.8%. On average, growth in 2019 is expected to expand at an annual pace of 2.6%.

Consensus forecasts put the chance of a U.S. recession in the next two years at about one in three. The Federal Reserve has already raised interest rates two times this year and two more hikes are expected in the second half of the year. It has also started to unwind its balance sheet, tightening monetary policy further.

Regarding future challenges, the Congressional Budget Office has recently released a report indicating that U.S. government debt is on track to hit historically high levels and at its current growth rate will be nearly equal in size to the U.S. economy by 2028. By the end of the year, the ratio of federal debt to GDP will reach 78%, the highest ratio since 1950. The debt is projected to grow to 96% of GDP by 2028, before eventually surpassing the historical high of 106% it reached in 1946.

Comisión Económica para América Latina y el Caribe (CEPAL)
Economic Commission for Latin America and the Caribbean (ECLAC)
www.cepal.org