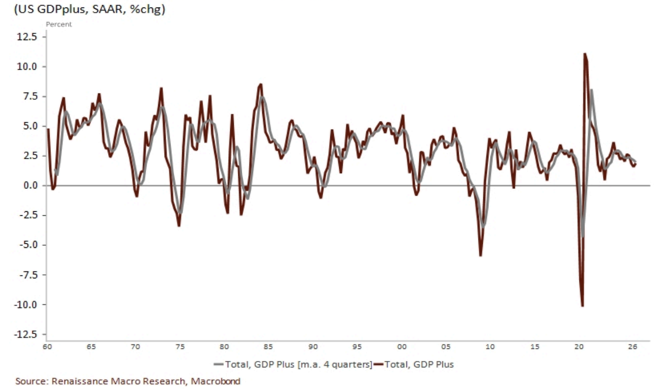
Monday Monetary Thoughts

Call it stagflation-lite

Q2 was the high-water mark for growth

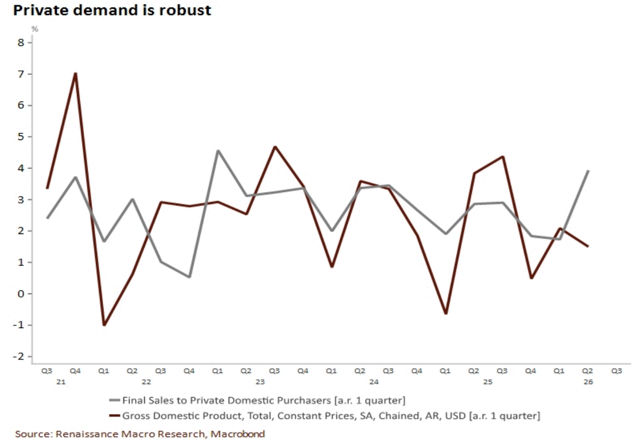
Underlying growth appears to be about two percent. That's the message when taking an average of expenditure side and income side growth. The Philadelphia Fed's GDPplus measure aims to do precisely this. In Q2, the measure ran 1.9 percent and the trend over the last year has cooled. The economy is not booming, nor is it materially slowing down.

GDPplus says growth is cooling but not stalling
(US GDPplus, SAAR, %chg)



Turning to GDP, private domestic demand was strong in Q2, climbing 3.9 percent SAAR. Roughly 2.5ppt of this growth came from the consumers' spending with the remainder coming from business fixed investment. It's difficult to see either continuing, and I'd anticipate slower real growth in the coming quarters.

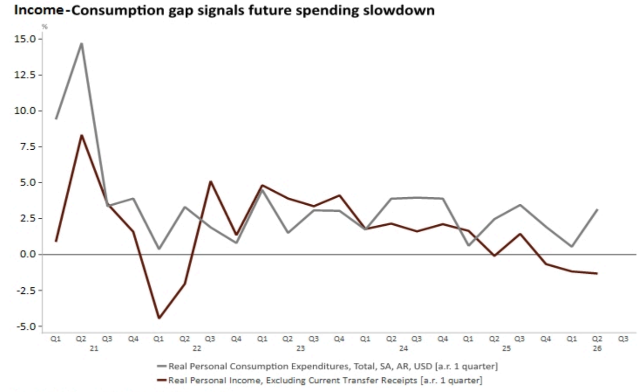
Private demand is robust



Expect slower growth

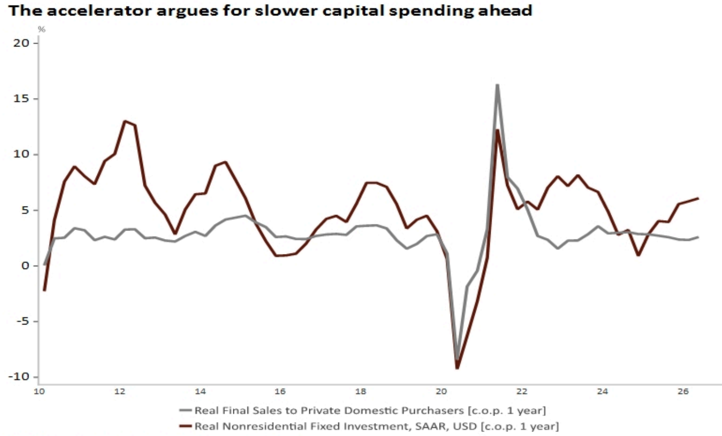
Real consumers' spending advanced 3.2 percent in Q2, the fastest pace in three quarters. This comes even as real disposable incomes fell over the quarter, indicating an ongoing drawdown in the household saving rate. There is a limit to how long this can keep up. Faced with an initial energy shock, households treat the shock as temporary, drawing down saving to keep consumption going. The longer the shock persists, the more likely consumers see the shock as permanent.

Income-Consumption gap signals future spending slowdown



Of course, in the immediate term, there are more obvious headwinds. There is a waning fiscal impulse as tax refunds have now become a thing of the past. Prime-Day, World Cup, and America 250 create the potential for a consumption hangover; activity pulled into the present at the expense of future months.

The accelerator argues for slower capital spending ahead



Source: Renaissance Macro Research, Macrobond

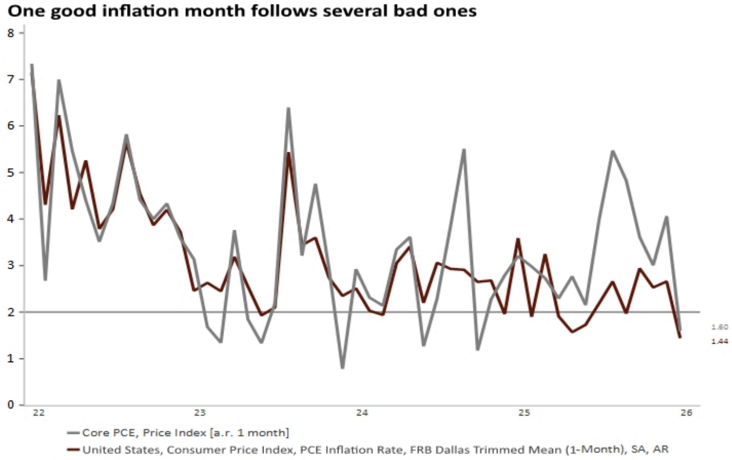
Nonresidential business fixed investment likely has hit a bit of an inflection point too. Investment spending tends to follow an accelerator effect. That is, as growth perks up, investment tends to rise somewhat faster. Between tighter credit conditions for important tech firms and the fact that stocks have been moving sideways for the last three months, I'd argue for some easing of the accelerator mechanism. It certainly feels that capital spending is less about spending out of free cash flow and more about taking on additional debt, creating some vulnerability to higher rates. Thus, at the margin, I'd argue that investment spending cools off somewhat from here.

That said, the slowdown in consumers' spending will be more important than any cooling we're likely to see in business investment.

June the low point for inflation

While Q2 was the high-water mark for growth, I suspect that June was the low-point for underlying consumer price inflation. After several months of above-target inflation, June saw core PCE rise just 1.6 percent SAAR. Median and trimmed-mean PCE also ran below target. That said, I would not get too carried away for a few reasons.

One good inflation month follows several bad ones



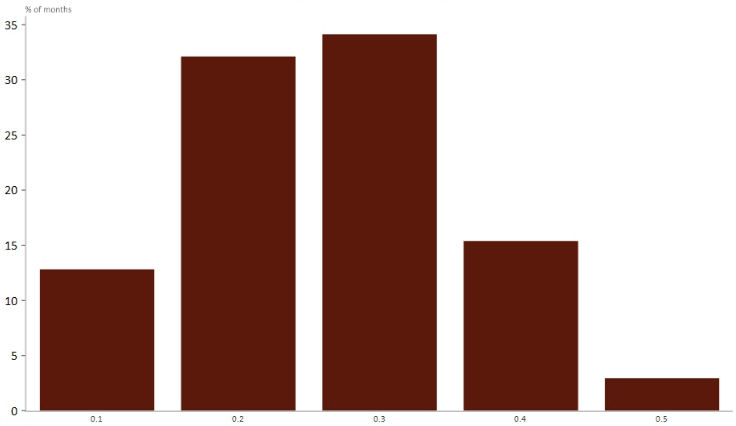
Source: Renaissance Macro Research, Macrobond

- First, one month of good news comes on the heels of several months of bad news. Even with the better June figure, core inflation has run nearly twice the Fed's target over the first half of 2026.

- Second, the likelihood of stringing out a series of benign inflation prints is low. For starters, since 2023, core PCE has come in at or below 0.2 percent roughly 35 percent of the time. Seeing this happen three months in a row, the odds decline to less than five percent.

Most core PCE prints cluster between 0.15% and 0.35% m/m

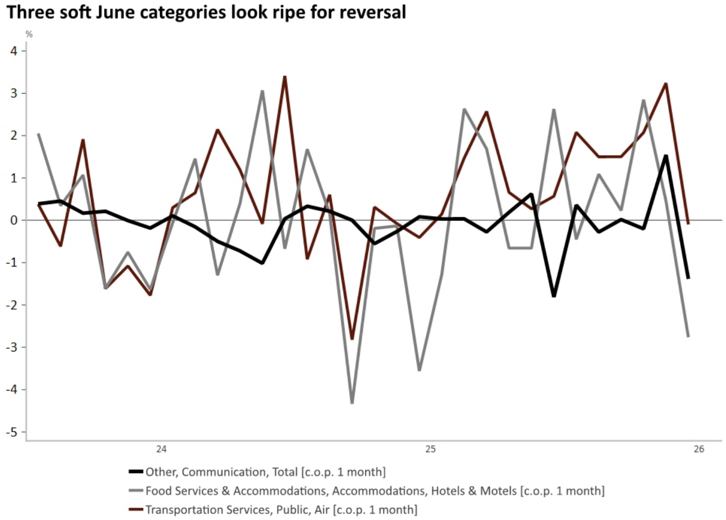
(Distribution of Core PCE m/m %, (Jan-2023 onwards, bin midpoint, 0.1 width))



Source: Renaissance Macro Research, Macrobond

- Third, a few areas seem ripe for reversing in the months ahead. Three that come to mind: communication services, airfares (oil pass-through), and hotels & motels. In short, the odds favor a pick-up in inflation in July.

Three soft June categories look ripe for reversal



Source: Renaissance Macro Research, Macrobond

There are good reasons to anticipate a cooling in inflation over time given the weak growth in wages and salaries and ongoing slowing in housing rents; however, inflation remains above target and is likely to remain that way under most plausible scenarios beyond a time that's satisfied by the word "soon."

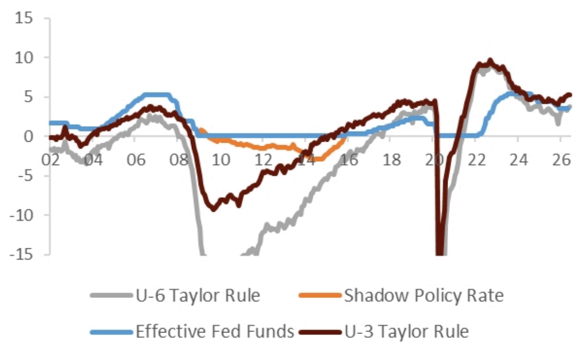
The loneliest job in DC

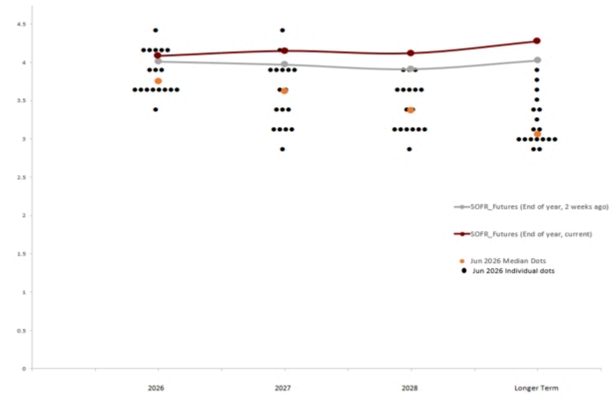
This brings me to the Fed. The market assumes that Kevin Warsh is in control of this FOMC; hence the movement in the front-end following the last rates decision. Warsh went a bit beyond simply standing pat in July. At any rate, my assumption is that his performance last week has not exactly endeared him to his colleagues inside the Eccles building. None of these people believe jawboning is a substitute for rate hikes. Dissents will only mount with the Chair increasingly isolated from the rest of the committee.

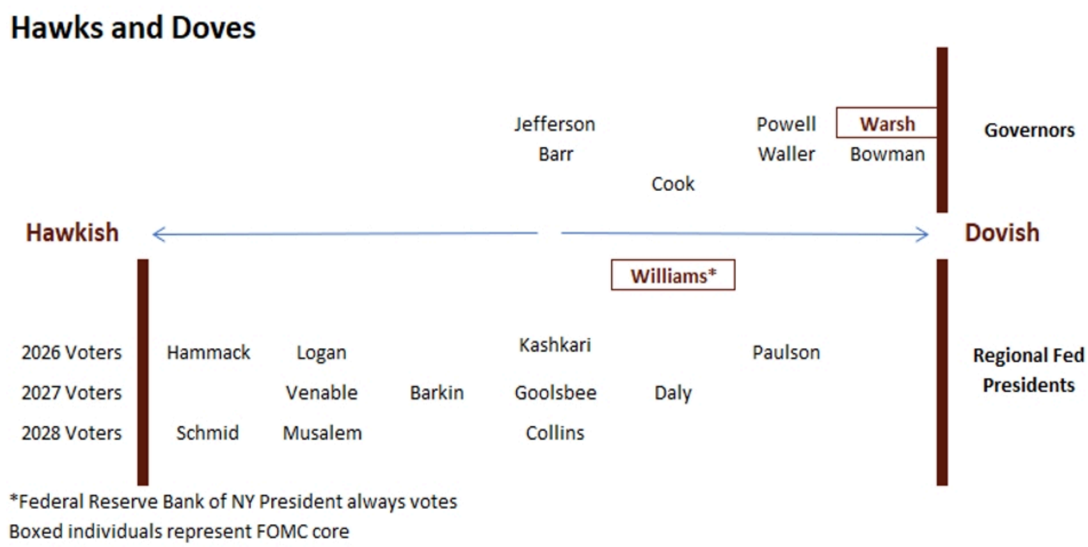
Play defense

Our outlook has important implications for capital markets. The slowing in growth implies that investors should curb risk appetite and take more defensive positions. In broad terms this means moving away from riskier asset classes like credit and equities. At a more micro level, our Fed call argues for a flatter Treasury yield curve. The Fed can't talk loudly and carry a stick forever. Eventually, they'll need to move the policy rate this year as the cooling of risk appetite takes some pressure off the long end.

Monetary metrics

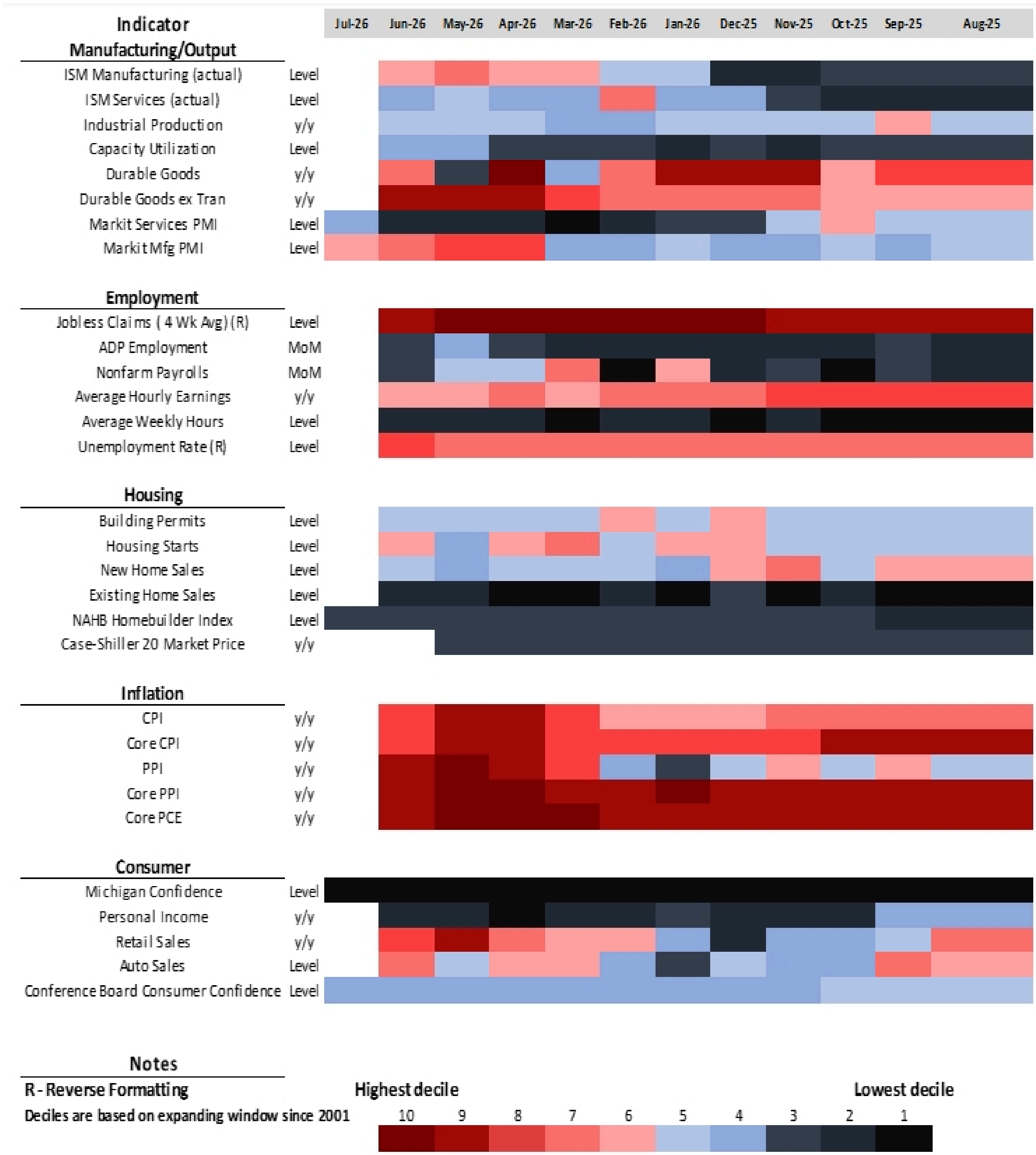




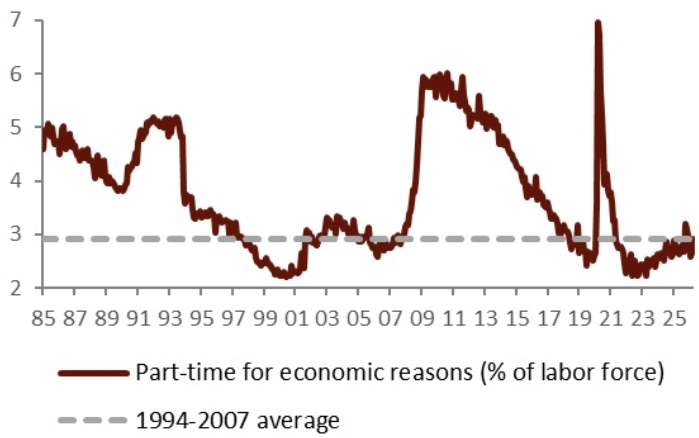


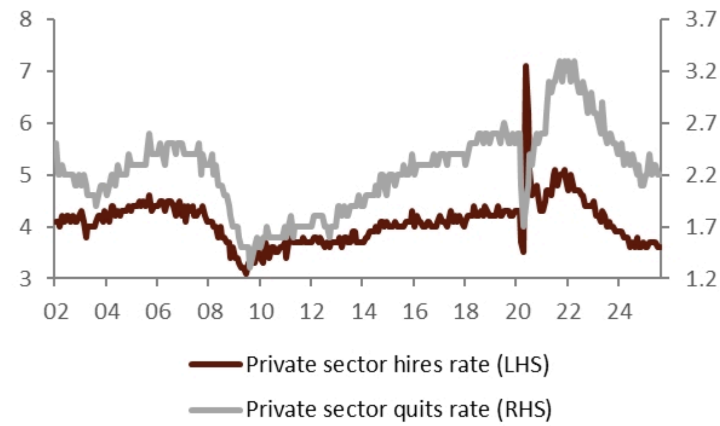
FOMC Forecasts	Median				Central Tendency			
	2026	2027	2028	Longer run	2026	2027	2028	Longer run
Change in real GDP	2.2	2.3	2.2	2	2.0–2.3	2.0–2.4	2.0–2.3	1.8–2.0
March projection	2.4	2.3	2.1	2	2.2–2.5	2.0–2.4	2.0–2.3	1.8–2.0
Unemployment rate	4.3	4.3	4.2	4.2	4.3–4.4	4.2–4.5	4.1–4.3	4.0–4.3
March projection	4.4	4.3	4.2	4.2	4.3–4.5	4.2–4.4	4.0–4.4	4.0–4.3
PCE inflation	3.6	2.3	2	2	3.5–3.7	2.2–2.5	2.0–2.1	2
March projection	2.7	2.2	2	2	2.6–3.1	2.0–2.3	2	2
Core PCE inflation4	3.3	2.5	2.1		3.2–3.5	2.3–2.6	2.0–2.2	
March projection	2.7	2.2	2		2.5–2.8	2.0–2.4	2	
Projected policy path								
Fed funds rate	3.8	3.6	3.4	3.1	3.6–4.1	3.1–3.9	3.1–3.6	3.0–3.5
March projection	3.4	3.1	3.1	3.1	3.1–3.6	2.9–3.6	2.9–3.6	2.9–3.5

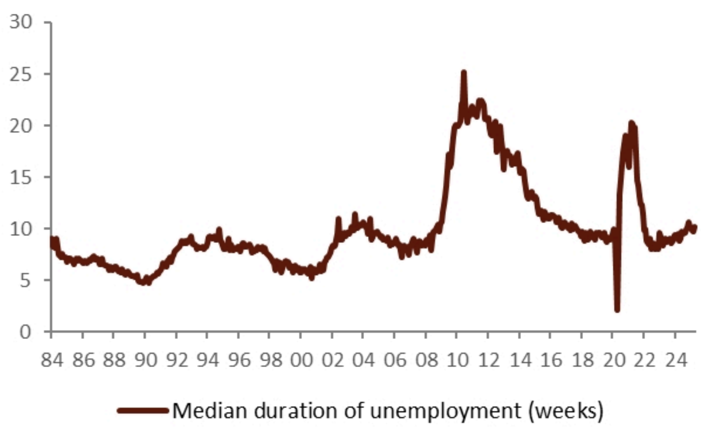
High frequency data heat-map

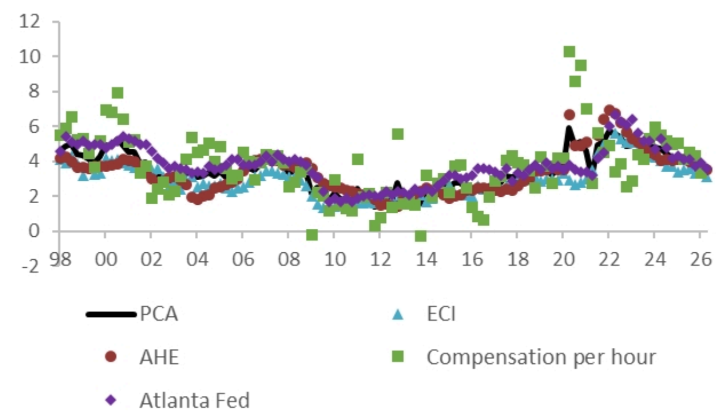


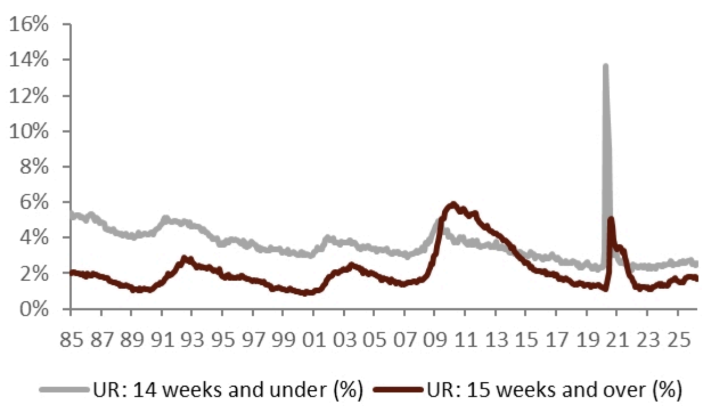
Labor market indicators

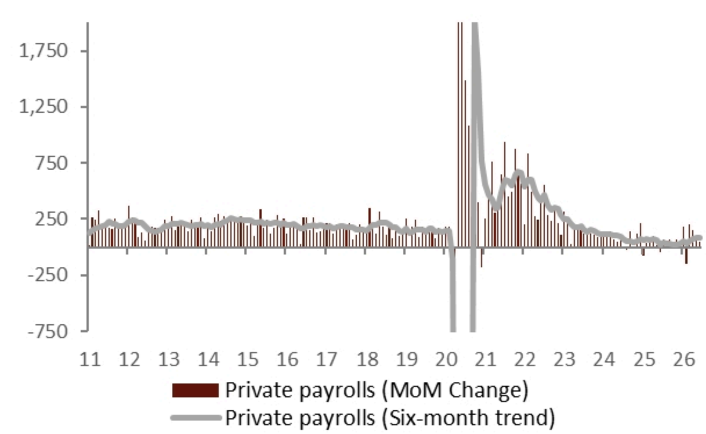




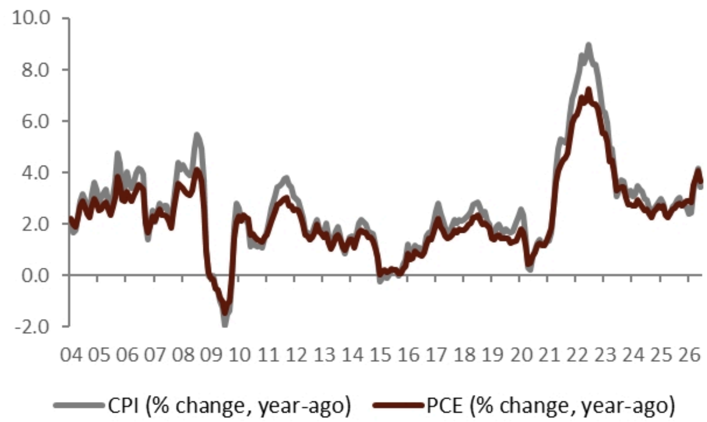


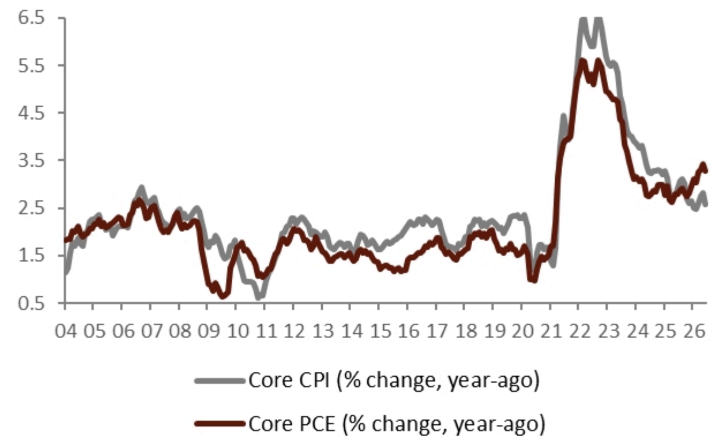


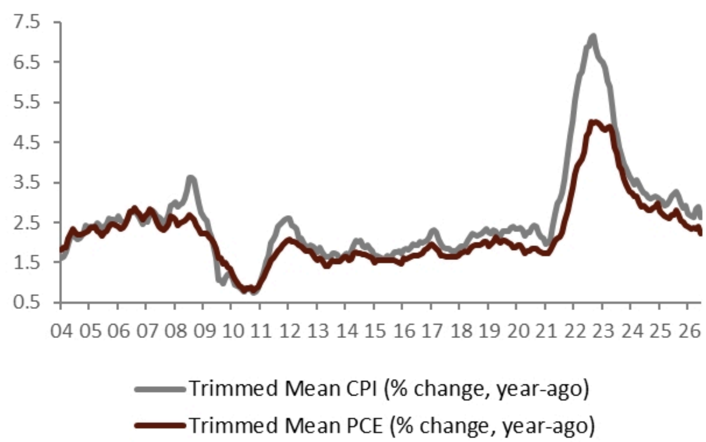


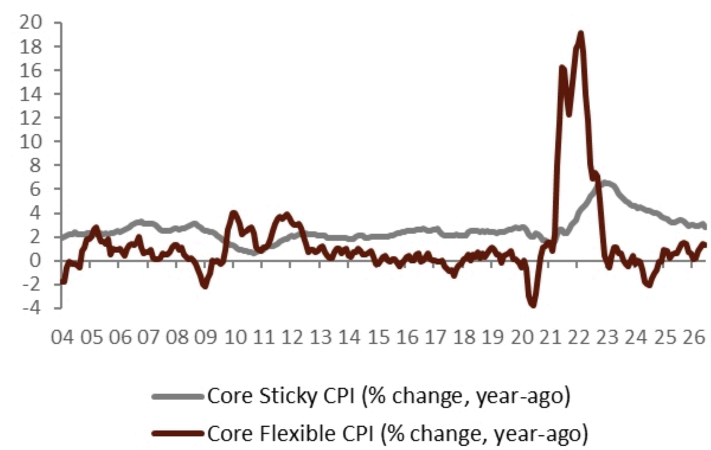


Inflation indicators



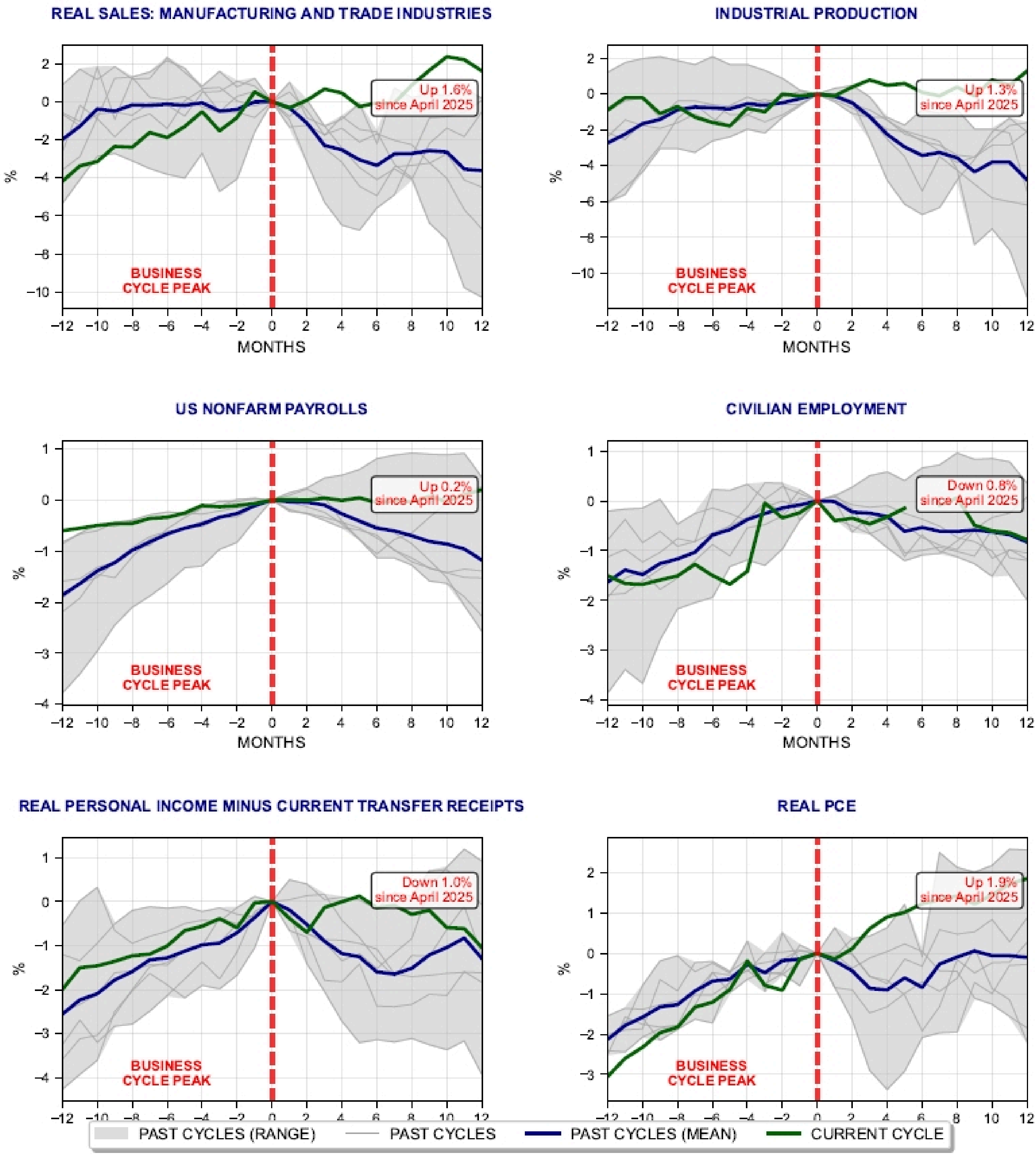






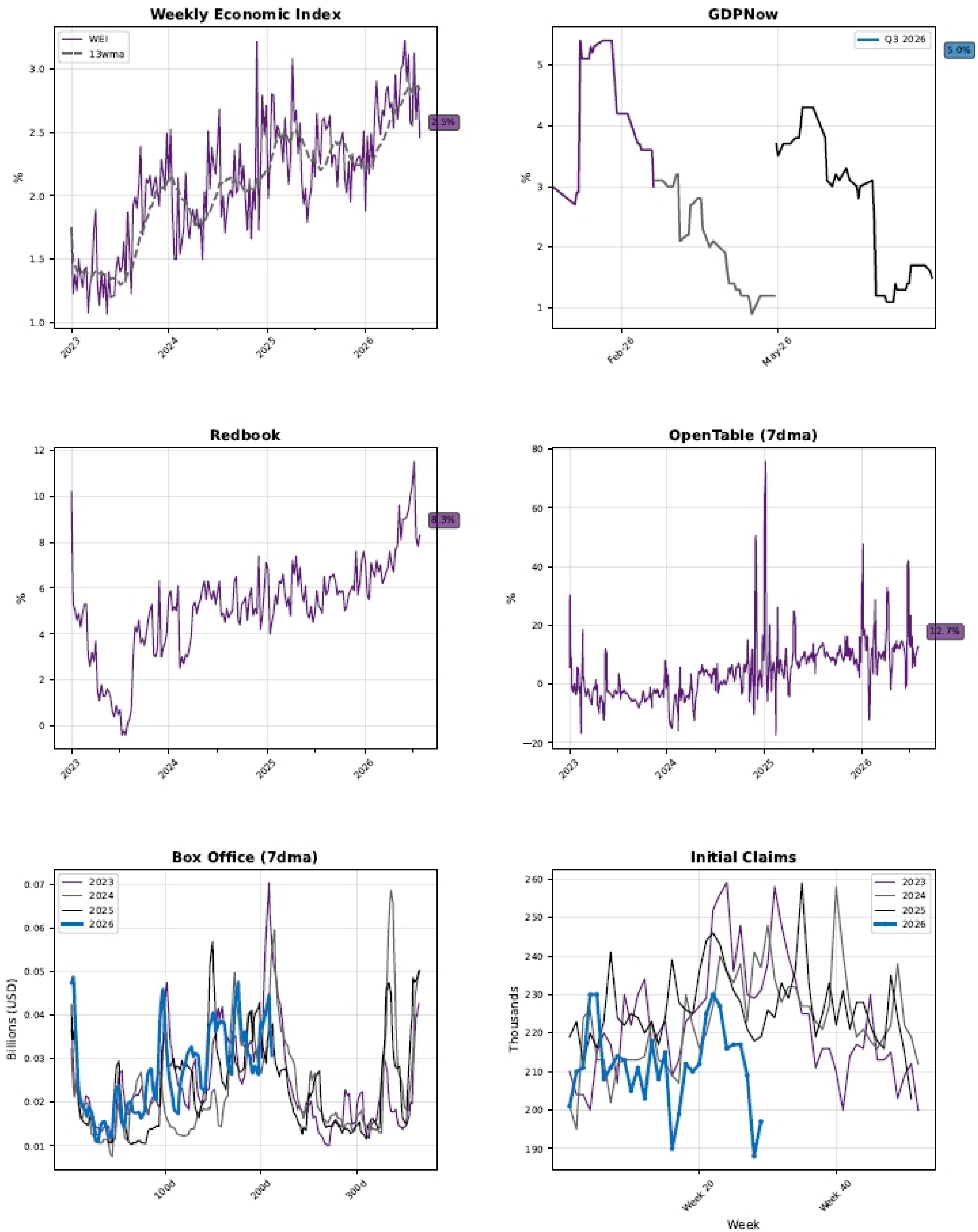
Note: The heatmap shows the distance of each US CPI component's 6-month annualized inflation rate from its historical average. The colour is white when a component's inflation rate is close to its average and is a varying shade of blue (red) when the rate is below (above) the average. Each inflation rate is standardized by subtracting its mean and dividing by its standard deviation, computed over 1996-2019. and We show full Nondurables (which includes food and energy components) alongside Durables, New vehicles, Used cars and trucks, and Apparel; the parent group itself excludes food and energy. Food away from home, Other personal services, and Tenants' & household insurance are published NSA by BLS and seasonally adjusted via X-13ARIMA-SEATS. Values in parentheses are CPI relative importance weights (parts per 100). Sources: BLS via Haver Analytics; RenMac calculations. Last observation: June 2026.

NBER RECESSION INDICATORS DASHBOARD



Past 7 cycles excluding Covid-19 period

High Frequency Economic Dashboard



High Frequency Economic Dashboard