Daiwa Capital Markets

U.S. Economic Comment

- U.S. households: strong or strained financially?
- Federal budget: half-year review
- Q1 GDP preview: probably soft, but not deeply troubling

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The U.S. Consumer

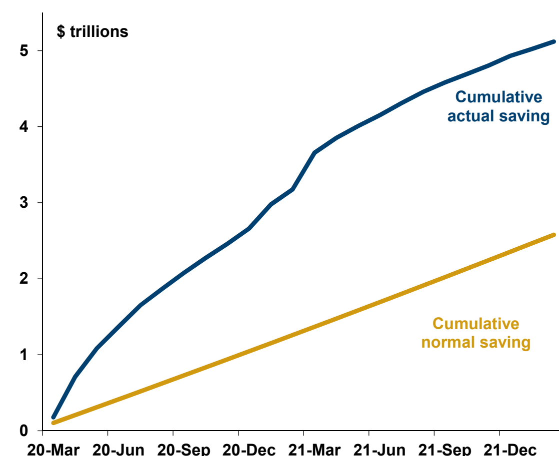
Most forecasts of the U.S. economy this year envision solid support from consumers, fueled by a firm labor market and healthy financial positions. Individuals have accumulated a pool of savings well above where it might have been in the absence of the pandemic (chart, left: the gap between actual cumulative saving and the pre-Covid trend totals $2.5 trillion, more than 10 percent of GDP). This jump in savings, along with sharp advances in home prices and equity values, has bolstered the net worth of many households. Most individuals, it would seem, are on solid financial ground.

However, the latest report on consumer credit raised questions, as the series published by the Federal Reserve Board surged in February, with revolving debt (primarily credit card balances) accounting for much of the increase. The jump triggered media reports speculating that rapid inflation was straining household budgets and forcing individuals to rely on credit-card debt.

We have no doubt that rapidly rising prices will generate enlarged credit card bills, but we believe it is far too early to suggest that a meaningful share of the household sector is now financially stressed. We would first note that many individuals used revolving debt judiciously during the worst of the pandemic. Indeed, aggregate credit card debt fell noticeably in most of 2020 and early 2021 and is still below pre-Covid levels despite surges in recent months (chart, right).

Moreover, we saw scant evident of stress before the onset of Covid. Delinquency rates on consumer debt moved to historic lows in the previous expansion, and they fell further in the current recovery, as many individuals apparently used their federal support to strengthen their financial positions. Low delinquency rates are understandable given the environment of the past decade or so, as rock-bottom interest rates and firm incomes have pushed debt servicing burdens to levels far below previous readings (chart, next page).

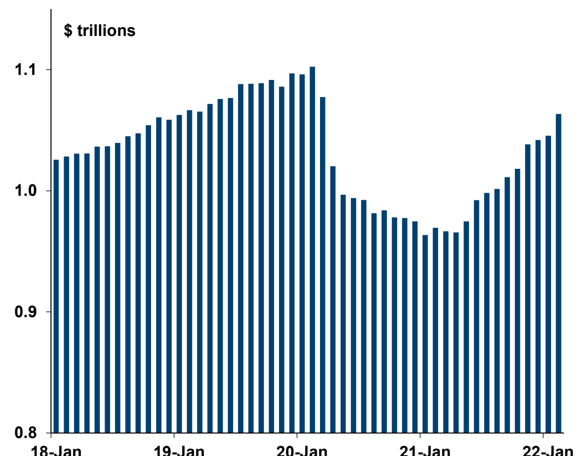
Personal Saving*



** Cumulative normal saving assumes that disposable personal income continued to grow at the 2018-19 pace and that the saving rate held steady at 7.5 percent.*

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

Consumer Credit: Revolving Credit



Source: Federal Reserve Board via Haver Analytics

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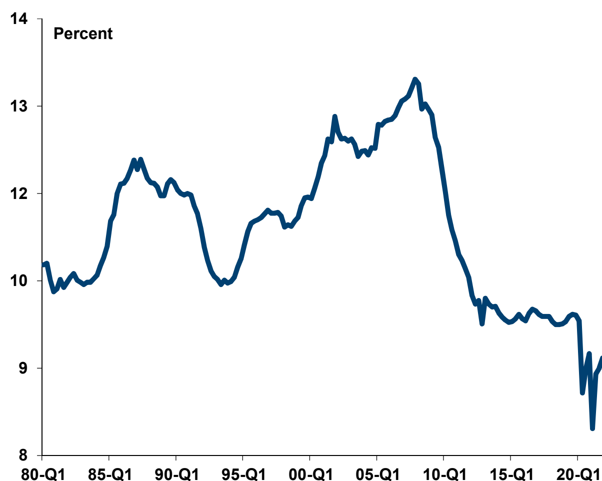
Active consumer spending also suggests that individuals are not under severe financial pressure. The upcoming report on GDP for the first quarter (April 28) is likely to show growth of real consumer spending in excess of three percent (annual rate).

Federal Budget FY2022-H1

The federal government completed the first half of fiscal year 2022 in March, and its taxing and spending provisions generated a budget deficit of $668 billion, down dramatically from the shortfall of $1,706 billion in the same period last year. A marked improvement is hardly surprising, as the deficit in FY2021 was boosted by efforts to provide support to individuals, businesses, and state & local governments during the pandemic. Still, results were better than we suspected, with the deficit narrower than the average shortfall of $717 billion in the first halves of fiscal 2019 and 2020.

Household Debt Service Ratio*



** Household debt service payments as a share of disposable personal income.*
Source: Federal Reserve Board via Haver Analytics

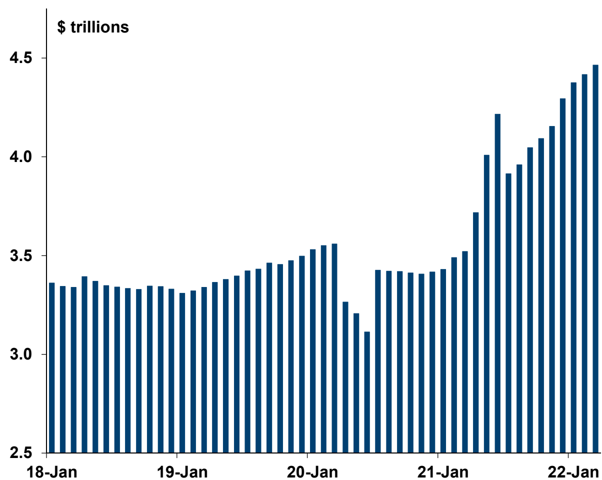
The federal government typically registers approximately three-quarters of its annual budget deficit in the first half of the fiscal year (final settlements of tax obligations for individuals and corporations in the prior calendar year occur in the second half of the government's fiscal year, fueling revenues and containing the deficit). If that pattern were to be maintained this year, the fiscal year deficit for 2022 would total less than $900 billion, narrower than the projection of $1,153 billion made by the Congressional Budget Office in July 2021.

Both sides of the ledger contributed to the improvement in the budget, as federal outlays fell 18.2 percent from the same period last year while revenues jumped 24.5 percent. The drop in outlays was to be expected because of fading pandemic-related support. Despite the decline, spending still had a firm tone. The first half of the fiscal year included some elements of Covid programs, and thus outlays were still a bit above the pre-virus trend and slightly larger as a share of GDP than the long-run average (an estimated 23.1 percent in the first half versus an average of 21.2 percent in the 10-years before the onset of Covid).

We view recent revenue developments as the most notable aspect of the budget results so far this fiscal year, as strong growth has pushed receipts well above the pre-pandemic trend and has generated a hefty reading when measured as a share of GDP (17.5 percent versus an average of 16.4 percent in the 10 years before the onset of Covid).

Some of the revenue gain could be viewed as the result of Covid or other special factors. For example, employers were allowed to delay the payment of their share of payroll taxes during the worst of the pandemic, and those taxes are now flowing into the Treasury. Similarly, state governments are now replenishing their balances in unemployment insurance trust funds. A drop in

Federal Revenues*



** 12-month moving totals.*
Source: U.S. Treasury Department via Haver Analytics

tax refunds has helped to boost net receipts, probably because of processing delays at the Internal Revenue Service.

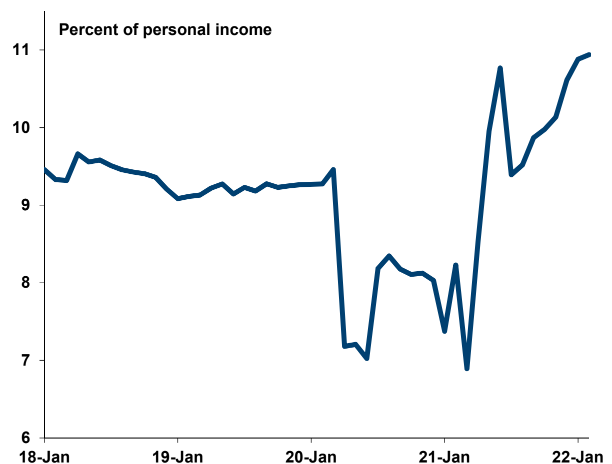
One source of firm revenue growth – remittances from the Federal Reserve -- will undoubtedly begin to slow in the coming months. The start of quantitative tightening will reduce the size of the Fed's interest-earning portfolio, thereby reducing the source of remittances to the Treasury. In addition, the increases in the Fed's target interest rate will lead to larger interest payments on bank reserves held at the central bank.

While special factors have certainly played a role in boosting federal revenues, economic fundamentals also have been important. Hefty collections of excise taxes and customs duties are suggestive of strong economic activity, while robust gains in individual and corporate receipts (up 31.0 percent and 15.6 percent, respectively) provide more definitive evidence of fundamental improvement in the economy and the finances of the federal government.

The increase in individual taxes was interesting in that it occurred despite a meaningful shift in the tax code. A strong economy would represent an obvious source of revenue growth, but other factors had to be in play because the average effective tax rate (individual taxes as a share of personal income) increased noticeably (chart).

One possible explanation for the pickup in effective tax rates is that a disproportionate share of income growth was earned by upper-income individuals, whose high marginal tax rates would pull the average higher. Another possibility is that lower-income individuals have realized much of the gain, which would push them into higher tax brackets, which also would boost the average tax rate. Given the evidence on wage growth by income class (e.g. the Atlanta Fed's wage tracker), gains in the lower portion of the income distribution most likely have been a factor.

Effective Personal Income Tax Rate*



** 12-month moving totals of federal receipts of individual income taxes as a share of personal income (annual rate).*

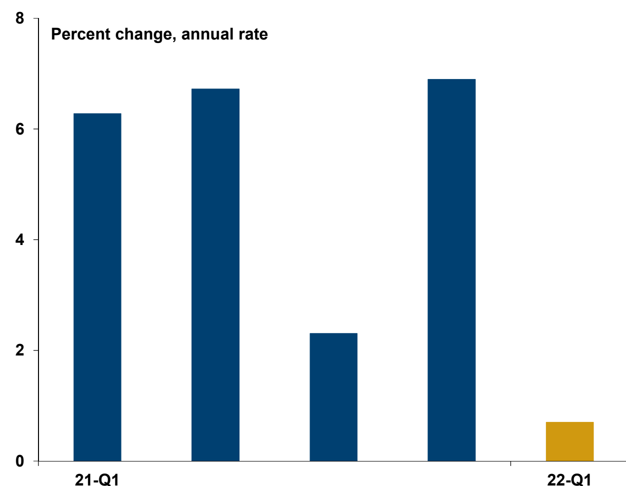
Sources: Bureau of Economic Analysis and U.S. Treasury Department via Haver Analytics; Daiwa Capital Markets America

Q1 GDP: Deceptively Slow

The Commerce Department will publish its first estimate Q1 GDP on April 28, and the results are likely to be soft. We have a projection of 0.7 percent, while the Bloomberg consensus is showing 1.0 percent (annul rates). Observers might be tempted to conclude that the modest advance signals heightened risks of recession. However, we would not draw strong conclusions from this report.

Two components of GDP are likely to stand out on the soft side: inventory investment and net exports. A sizeable negative contribution from inventory investment, probably more than a percentage point, could be viewed as normal

GDP Growth*



** The reading for 2022-Q1 (gold bar) is a forecast.*

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

random volatility in this often-erratic component. After a huge positive contribution in the fourth quarter (adding 5.3 percentage points to growth) some cooling in inventory investment was to be expected. A constraint of a percentage point after the burst in the fourth quarter could be viewed as a mild shift.

Net exports will probably subtract more than two percentage points from GDP growth, and this constraint is more of an issue than that from inventory investment. A decline in exports suggests that slow growth abroad is having an influence on U.S. economic activity. Strong imports could be viewed as an indication of brisk domestic demand, but that demand is fueling foreign activity rather than domestic production. Thus, we would not downplay the negative contribution from net exports, but we are hopeful that the constraint in Q1 will be larger than the norm. It will certainly be larger than the average drag of 0.9 percentage point in the first seven quarters of the current expansion.

Review

Week of April 18, 2022	Actual	Consensus	Comments
Housing Starts (March)	**1.793 Million (+0.3%)**	**1.740 Million (-1.6%)**	All of the increase in housing starts in March was driven by a jump in multi-family activity, which advanced 4.6% to 593,000 units (annual rate) -- the best reading of the current expansion, and only slightly below the high of 597,000 in the prior expansion. The flurry of activity in the multi-family sector suggests that builders are sensing a shift in preferences toward apartment living amid a plunge in affordability of single-family homes. Single-family starts slipped 1.7% to 1.200 million. New construction has moved sideways in the past four months, and it is off last year's high of 1.222 million in November, but it still compares favorably to the longer-run performance in single-family starts (although it is below the unusually high levels during the boom period in the early-to-mid 2000s).
Existing Home Sales (March)	**5.77 Million (-2.7%)**	**5.77 Million (-4.1%)**	March brought the second consecutive monthly decline in sales of existing homes and the third in the past four months, with the combination of elevated prices and higher mortgage rates cooling demand. However, while activity is slowing, it is not collapsing, as sales in March remained respectable by historical standards (still above all observations in the previous expansion). An increase of 11.8% in the number of homes for sale, along with the slower sales pace, nudged the months' supply of homes to 2.0 months, up from the record low of 1.6 in January but still notably lean by historical standards.
Leading Indicators (March)	**0.3%**	**0.3%**	Positive contributions from interest rate spreads, initial claims for unemployment insurance, and the leading credit index offset a sizable negative contribution from consumer expectations in March, which led to the 21st advance in the past 23 months in the index of leading economic indicators. The latest reading is 5.9% above the high in the previous expansion (July 2019).

Sources: U.S. Census Bureau (Housing Starts); National Association of Realtors (Existing Home Sales); The Conference Board (Leading Indicators); Consensus forecasts are from Bloomberg

Preview

Week of April 25, 2022	Projected	Comments
Durable Goods Orders (March) (Tuesday)	**0.8%**	A rebound in commercial aircraft bookings could boost total durable goods orders in March, but order flows in other key industries have leveled off recently, suggesting only a modest change excluding transportation.
Conference Board Consumer Confidence (April) (Tuesday)	**105.0 (-2.1%)**	Elevated prices of gasoline and groceries are likely weighing heavily on the minds of consumers, which is likely to push the Conference Board's measure of attitudes lower in April.
New Home Sales (March) (Tuesday)	**0.750 Million (-2.8%)**	Elevated prices and higher mortgage interest rates in March likely dampened sales of new homes for the third consecutive month. The expected reading in March would be in the low end of the range of the current expansion (and notably below the recent high of 993,000 in January 2021), although it would be at the top of the range of the previous expansion and considered firm from a longer-term perspective.
U.S. International Trade in Goods (March) (Wednesday)	**-$105.0 Billion ($1.3 Billion Narrower Deficit)**	Slowing global growth offers little hope that exports will break out of their recent sideways trend, but a cooling in imports after a strong run could lead to a modest narrowing in the goods trade deficit.
GDP (22-Q1) (Thursday)	**0.7%**	Consumer spending, business fixed investment, and residential construction advanced moderately in Q1, but negative contributions from inventory investment (after a massive 5.3 percentage point contribution in Q4) and net exports are likely to offset most of the growth elsewhere.
Employment Cost Index (22-Q1) (Friday)	**1.0%**	Pay packages offered to attract new workers and concessions made to current employees to offset rapid inflation likely led to another jump in compensation costs in Q1 (the third consecutive increases of 1.0% or more).
Personal Income, Consumption, Core PCE Price Index (March) (Friday)	**0.3%, 0.5%, 0.3%**	Wages and salaries grew moderately in March, and investment income could contribute to growth as well. On the outlay side, a decline in new vehicle sales suggests light spending on durable items, but gains in key categories in the retail sales report suggest a pickup in outlays for nondurable items, although much of the change probably reflects higher prices rather than an increase in real activity. The March reading on the core CPI suggests a more moderate increase in the core PCE price index after an average gain of 0.5% in the past five months.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

April / May 2022

Monday	Tuesday	Wednesday	Thursday	Friday
18	19	20	21	22
NAHB HOUSING INDEX Feb 81 Mar 79 Apr 77	**HOUSING STARTS** Jan 1.679 million Feb 1.788 million Mar 1.793 million	**EXISTING HOME SALES** Jan 6.49 million Feb 5.93 million Mar 5.77 million **APRIL BEIGE BOOK** "Economic activity expanded at a moderate pace since mid-February."	**UNEMPLOYMENT CLAIMS** Initial / Continuing (Millions) Mar 26 0.171 1.529 Apr 02 0.168 1.475 Apr 09 0.186 1.417 Apr 16 0.184 N/A **PHILY FED INDEX** Feb 16.0 Mar 27.4 Apr 17.6 **LEADING INDICATORS** Jan -0.4% Feb 0.6% Mar 0.3%	
25	26	27	28	29
CHICAGO FED NATIONAL ACTIVITY INDEX (8:30) Monthly / 3-Mo. Avg. Jan 0.59 0.37 Feb 0.51 0.35 Mar -- --	**DURABLE GOODS ORDERS (8:30)** Jan 1.5% Feb -2.1% **Mar 0.8%** **FHFA HOME PRICE INDEX (9:00)** Dec 1.3% Jan 1.6% Feb -- **S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX (9:00)** SA / NSA Dec 1.4% 1.1% Jan 1.8% 1.4% Feb -- -- **CONFERENCE BOARD CONSUMER CONFIDENCE (10:00)** Feb 105.7 Mar 107.2 **Apr 105.0** **NEW HOME SALES (10:00)** Jan 0.788 million Feb 0.772 million **Mar 0.750 million**	**U.S. INTERNATIONAL TRADE IN GOODS (8:30)** Jan -$107.4 billion Feb -$106.3 billion **Mar -$105.0 billion** **ADVANCE INVENTORIES (8:30)** Wholesale / Retail Jan 1.2% 2.0% Feb 2.5% 1.3% Mar -- -- **PENDING HOME SALES (10:00)** Jan -5.8% Feb -4.1% Mar --	**INITIAL CLAIMS (8:30)** **GDP (8:30)** GDP / Chained Price 21-Q3 2.3% 6.0% 21-Q4 6.9% 7.1% **22-Q1 0.7% 6.5%**	**EMPLOYMENT COST INDEX (8:30)** Comp. / Wages 21-Q3 1.3% 1.5% 21-Q4 1.0% 1.1% **22-Q1 1.0% 1.1%** **PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX (8:30)** Inc. / Cons. / Core Jan 0.1% 2.7% 0.5% Feb 0.5% 0.2% 0.4% **Mar 0.3% 0.5% 0.3%** **MNI CHICAGO BUSINESS BAROMETER INDEX (9:45)** Index / Prices Feb 56.3 86.5 Mar 62.9 85.7 Apr -- -- **REVISED CONSUMER SENTIMENT (10:00)** Feb 62.8 Mar 59.4 Apr(p) 65.7
2	3	4	5	6
ISM MANUFACTURING INDEX **CONSTRUCTION SPEND.**	**FACTORY ORDERS** **JOB OPENINGS & LABOR TURNOVER (JOLTS)** **NEW VEHICLE SALES** **FOMC MEETING**	**ADP EMPLOYMENT REPORT** **TRADE BALANCE** **ISM SERVICES INDEX** **FOMC DECISION**	**INITIAL CLAIMS** **PRODUCTIVITY & COSTS**	**EMPLOYMENT REPORT** **CONSUMER CREDIT**
9	10	11	12	13
WHOLESALE TRADE	**NFIB SMALL BUSINESS OPTIMISM INDEX**	**CPI** **FEDERAL BUDGET**	**INITIAL CLAIMS** **PPI**	**IMPORT/EXPORT PRICES** **CONSUMER SENTIMENT**

Forecasts in Bold. *(p) = preliminary*

Treasury Financing

April / May 2022

Monday	Tuesday	Wednesday	Thursday	Friday
18	19	20	21	22
AUCTION RESULTS: Rate / Cover 13-week bills 0.860% 2.72 26-week bills 1.250% 3.29 **SETTLE:** $46 billion 3-year notes $34 billion 10-year notes $20 billion 30-year bonds	**AUCTION RESULTS:** Rate / Cover 52-week bills 1.870% 3.31 **ANNOUNCE:** $35 billion 4-week bills for auction on April 21 $30 billion 8-week bills for auction on April 21 $30 billion 17-week CMBs for auction on April 20 **SETTLE:** $35 billion 4-week bills $30 billion 8-week bills $30 billion 17-week CMBs	**AUCTION RESULTS:** Rate / Cover 17-week CMB 1.070% 3.82 20-yr bonds 3.095% 2.80	**AUCTION RESULTS:** Rate / Cover 4-week bills 0.500% 3.21 8-week bills 0.625% 3.24 5-year TIPS -0.340% 2.73 **ANNOUNCE:** $96 billion 13-,26-week bills for auction on April 25 $24 billion 2-year FRNs for auction on April 27 $48 billion 2-year notes for auction on April 26 $49 billion 5-year notes for auction on April 27 $44 billion 7-year notes for auction on April 28 **SETTLE:** $105 billion 13-,26-week bills $34 billion 52-week bills	
25	26	27	28	29
AUCTION: $96 billion 13-,26-week bills	**AUCTION:** $48 billion 2-year notes **ANNOUNCE:** $35 billion* 4-week bills for auction on April 28 $30 billion* 8-week bills for auction on April 28 $30 billion* 17-week CMBs for auction on April 27 **SETTLE:** $35 billion 4-week bills $30 billion 8-week bills $30 billion 17-week CMBs	**AUCTION:** $30 billion* 17-week CMBs $24 billion 2-year FRNs $49 billion 5-year notes	**AUCTION:** $35 billion* 4-week bills $30 billion* 8-week bills $44 billion 7-year notes **ANNOUNCE:** $96 billion* 13-,26-week bills for auction on May 2 **SETTLE:** $96 billion 13-,26-week bills	**SETTLE:** $20 billion 5-year TIPS
2	3	4	5	6
AUCTION: $96 billion* 13-,26-week bills **SETTLE:** $16 billion 20-year bonds $24 billion 2-year FRNs $48 billion 2-year notes $49 billion 5-year notes $44 billion 7-year notes	**ANNOUNCE:** $35 billion* 4-week bills for auction on May 5 $30 billion* 8-week bills for auction on May 5 $30 billion* 17-week CMBs for auction on May 4 **SETTLE:** $35 billion* 4-week bills $30 billion* 8-week bills $30 billion* 17-week CMBs	**ANNOUNCE:** $45 billion* 3-year notes for auction on May 10 $36 billion* 10-year notes for auction on May 11 $22 billion* 30-year bonds for auction on May 12 **AUCTION:** $30 billion* 17-week CMBs	**AUCTION:** $35 billion* 4-week bills $30 billion* 8-week bills **ANNOUNCE:** $96 billion* 13-,26-week bills for auction on May 9 **SETTLE:** $96 billion* 13-,26-week bills	
9	10	11	12	13
AUCTION: $96 billion* 13-,26-week bills	**AUCTION:** $45 billion* 3-year notes **ANNOUNCE:** $35 billion* 4-week bills for auction on May 12 $30 billion* 8-week bills for auction on May 12 $30 billion* 17-week CMBs for auction on May 11 **SETTLE:** $35 billion* 4-week bills $30 billion* 8-week bills $30 billion* 17-week CMBs	**AUCTION:** $30 billion* 17-week CMBs $36 billion* 10-year notes	**AUCTION:** $35 billion* 4-week bills $30 billion* 8-week bills $22 billion* 30-year bonds **ANNOUNCE:** $96 billion* 13-,26-week bills for auction on May 16 $34 billion* 52-week bills for auction on May 17 $16 billion* 20-year bonds for auction on May 18 $14 billion* 10-year TIPS for auction on May 19 **SETTLE:** $96 billion* 13-,26-week bills	

*Estimate