Daiwa Capital Markets

U.S. Economic Comment

- The U.S. labor market: a few cracks; no meaningful breakage
- Inflation: a new metric to guide Fed decisions

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A Tight Labor Market Despite a Slow Economy

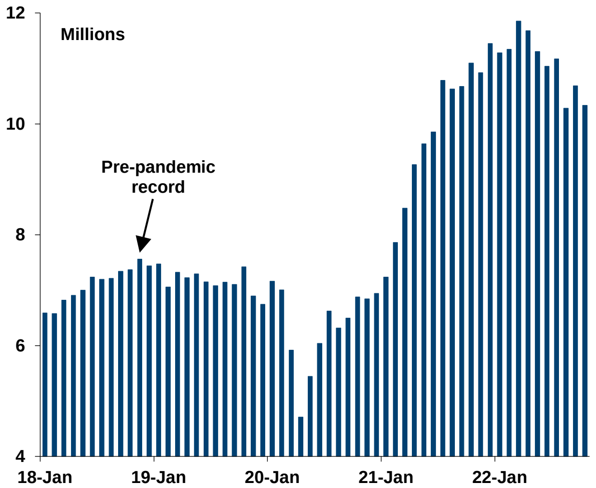
Fed Chair Jerome Powell provided an unusually clear statement this week on his policy intentions, noting that the pace of tightening would soon slow. At the same time, he emphasized that the Federal Open Market Committee would continue to raise interest rates and that the Committee would likely maintain a restrictive stance for a lengthy period.

A slower pace of tightening seems warranted based on recent data, which suggest the economy is beginning to slow. Although the October report on consumer spending was strong (real growth of 0.5 percent in October), other figures released this week point to negative contributions to growth from net exports and inventory investment. In addition, figures on construction and pending home sales indicate that the housing market remains decidedly weak. Finally, a sub-50 reading on the ISM index points to softening in the manufacturing sector. All told, GDP growth of more than one percent in Q4 seems like a reach.

Slow economic growth, though, will not deter the Fed from tightening. To the contrary, officials want to achieve slow growth in order to reduce the supply-demand imbalance in the labor market and to reduce inflation. Fed decisions will be driven largely by developments in the labor market rather than the growth of GDP, and recent statistics show that the labor market remains tight.

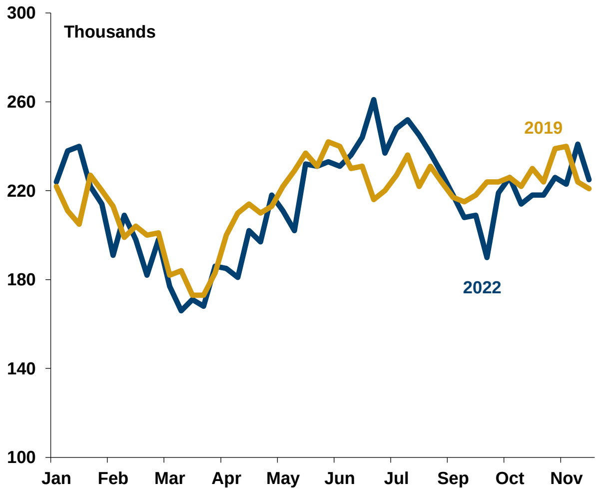
Continued job growth at a healthy clip suggests that the Fed will be pressing on with rate increases. The payroll gain of 263,000 in November lagged the average of 444,000 in the first half of the year, but it was still strong by historical standards. In addition, other recent employment statistics suggest that job growth will remain firm. Job openings, although off from the record high of 11.9 million in March, remain at a stratospheric level relative to historical standards (chart, left; 10.3 million in October versus a pre-pandemic record of 7.6 million).

Job Openings



Source: Bureau of Labor Statistics via Haver Analytics

Initial Claims for Unemployment Insurance



Source: U.S. Department of Labor via Haver Analytics

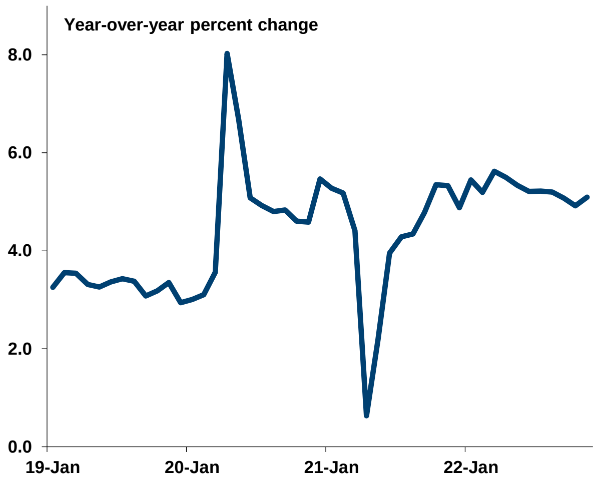
With businesses having difficulty in finding workers, layoffs have been limited thus far and could remain restrained in the months ahead. Despite numerous announcements of payroll cuts, initial claims for unemployment insurance have barely moved this year, bouncing within a range similar to that before the onset of Covid (chart; prior page, right). Similarly, we were struck by job growth of 20,000 in the construction industry in November. With the housing industry essentially in recession, we saw the potential for job cuts in this sector, but builders continued to add workers. Construction firms trimmed their average workweeks because of slower activity, but they added employees.

Average hourly earnings, which jumped 0.6 percent in November, perhaps represent the most telling signal that labor markets remain tight. The latest increase left year-over-year growth at 5.1 percent, not meaningfully below the recent high of 5.6 percent in March (chart, left). Some commentators have noted the deceleration in the past several months as a hint that labor market tightness is beginning to ease, but we view the downward drift as insignificant.

Moreover, we suspect that individuals will continue to negotiate aggressively for wage increases, partly to restore real compensation that has been eroded by inflation and partly because of a perceived bargaining advantage. The job-assessment measure in the Conference Board survey of consumers shows that individuals sense that the labor market is tight and that sizeable wage increases are obtainable. The net assessment of job availability in this survey (share indicating that jobs are plentiful less the share saying that jobs are hard to get) is off the recent high, but still far above historical norms (chart, right).

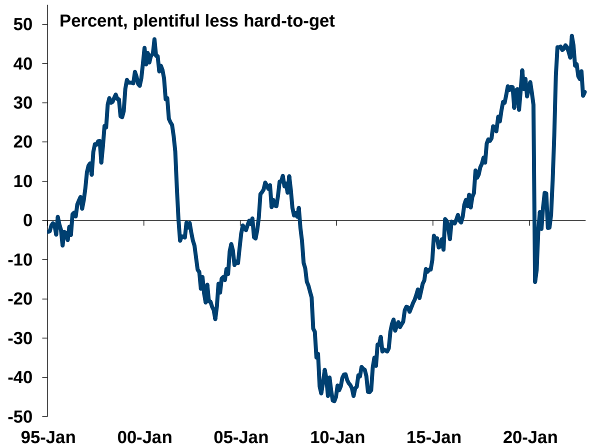
Chair Powell argued this week in his speech at the Brookings Institution that brisk wage growth driven by tight labor markets represented the most notable inflation risk next year. Given recent statistics on the labor market, this view seems to be on the mark.

Average Hourly Earnings



Sources: Bureau of Labor Statistics via Haver Analytics

Labor Market Assessment*



** The share of respondents to the Conference Board's consumer confidence survey indicating that jobs are plentiful less the share reporting that jobs are hard to get.*

Source: The Conference Board Board via Haver Analytics

Inflation Risks

Chair Powell is focusing on the labor market because he sees other inflation risks as diminishing. He noted that supply-chain difficulties should continue to lessen and that rents on new leases suggest that pressure in this hot sector will begin to ease next year. Rapid wage growth, though, could continue to fuel inflation.

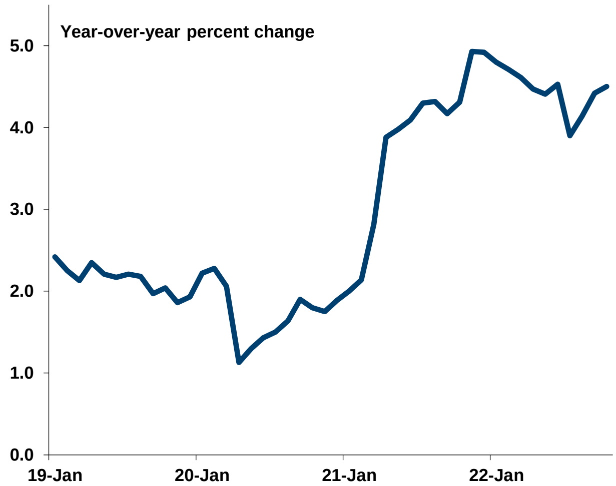
Mr. Powell noted that wage pressure would be especially important in service-producing sectors, where labor is the dominant input and wages are the most significant cost. The Fed Chair introduced a new measure intended to track prices in the wage-sensitive sectors. Specifically, Mr. Powell focused on the price index for core personal consumptions expenditures of services excluding housing. That is, the measure is based on the Fed's preferred inflation gauge (the PCE price index), but it excludes the prices of all goods, energy services (i.e. charges for electricity and natural gas), and housing costs (i.e. rents).

This measure is off the high registered late last year, but net progress in the past year-and-one-half has been limited. One would be hard pressed to describe the trend as downward, and the rate of growth (4.5 percent year-over-year) is more than double the Fed's inflation target.

We have recreated Chair Powell's gauge to allow tracking for October and beyond (he had data only through September, but included a staff estimate for October). The Commerce Department published the PCE price index for October the day after Chair Powell's speech, and the new measure was not quite as favorable as the traditional core index (0.3 percent for the new index versus 0.2 percent for the PCE index excluding food and energy).

The median PCE price index published by the Cleveland Fed also rose by 0.3 percent in October. The differential between the median gauge and the traditional core measure indicated that sizeable declines in a limited number of items were restraining the traditional core index. Prices of used motor vehicles had such an influence with a decline of 2.4 percent. Prices of watches and jewelry and photographic equipment also posted declines in excess of two percent.

PCE Price Index: Core Services Ex. Housing Services*



** An observation for October 2022 was calculated by Daiwa Capital Markets America.*

Sources: Powell, J.H., (2022, November 30). Inflation and the Labor Market. Retrieved from: https://www.federalreserve.gov/newsevents/speech/powell20221130a.htm; Daiwa Capital Markets America

Daiwa Capital Markets

Review

Week of Nov. 28, 2022	Actual	Consensus	Comments
Consumer Confidence (November)	**100.2 (-2.0%)**	**100.0 (-2.4%)**	The November reading on consumer confidence was above the recent low of 95.3 in July, but it is off sharply from the cyclical peak of 128.9 in June 2021. Despite talk of recession and announcements of job cuts, views on the labor market remained favorable. The net assessment of job availability (the share indicating that jobs were plentiful less the share indicating that jobs were hard to get) totaled 32.8%, down from the record of 47.1% in March, but very much in the upper end of the historical range.
Revised GDP (2022-Q3)	**2.9% (+0.3 Pct. Pt. Revision)**	**2.8% (+0.2 Pct. Pt. Revision)**	An upward adjustment to consumer spending contributed importantly to the revision to GDP growth in Q3 (growth of 1.7% versus 1.4% first reported), as did business fixed investment (a less-negative performance in outlays for new structures), government spending, and net exports. Inventory investment provided a partial offset, subtracting 1.0 percentage points from growth rather than 0.7 percentage point in the preliminary tally. The report included the first estimate of corporate profits for Q3. Earnings fell slightly from the elevated reading in Q2, but the dip did little damage to the firm trend in the current expansion.
U.S. International Trade in Goods (October)	**-$99.0 Billion ($7.1 Billion Wider Deficit)**	**-$90.6 Billion ($1.3 Billion Narrower Deficit)**	Both sides of the trade ledger contributed to the widening in the trade deficit in October, as exports fell 2.6% and imports rose 0.9%. While the picture could change with results for November and December, the October results suggest a negative contribution from net exports to GDP growth in Q4 of approximately ¾ percentage point. Such a drag would offset the small net positive contribution in the first three quarters of the year and leave net exports as an approximately neutral influence on economic growth for the year.
Job Openings (October)	**10.334 Million (-353k)**	**10.250 Million (-467k)**	Job openings in the U.S. fell by 353,000 (3.3%) in October to 10.334 million from a downwardly revised level in September (10.687 million versus 10.717 million first published; -0.3%). Openings have fallen by more than 1.5 million from the record of 11.855 million in March, suggesting some softening in the demand side of the labor market, but they are still almost 37% higher than the pre-pandemic record of 7.558 million in November 2018.
Personal Income, Consumption, Core Prices (October)	**0.7%, 0.8%, 0.2%**	**0.4%, 0.8%, 0.3%**	The firm advance in personal income in October in part reflected a jump in transfer payments, fueled by one-time refundable tax credits issued by state governments. Wages rose moderately (0.5%), and investment income was strong (1.0%). Consumers spent actively in October, as growth of 0.8% in nominal outlays translated to a gain of 0.5% in real terms. The strong results set the stage for solid growth of consumer spending in Q4, possibly in excess of 3.0%. The increase in the core price index trailed the average of 0.4% in the prior 12 months. The restraint in the core component was influenced by lower prices of goods that had surged during the pandemic or early stages of the recovery (used vehicles, furniture, appliances). However, some pressure points were still evident in the core index (rents, airfares, hotel fees).

Review Continued

Week of Nov. 28, 2022	Actual	Consensus	Comments
ISM Manufacturing Index (November)	**49.0 (-1.2 Index Pts.)**	**49.7 (-0.5 Index Pt.)**	The ISM manufacturing index fell into contractionary territory in November for the first time since May 2020, when the U.S. was in the midst of Covid-related lockdowns. While the production measure remained in growth territory, the latest reading of 51.5 (-0.8 index pt.) was well-below readings earlier in the year and the robust average of 61.0 in 2021. The new orders and employment components both signaled contraction (falling 2.0 index points to 47.2 and 1.6 index points to 48.4, respectively). Although the supplier deliveries index rose by 0.4 index point, the restrained reading of 47.2 suggested that supply chains have largely normalized. The price index continued its downward trend from the recent high of 87.1 in March (-3.0 index points to 43.0).
Construction Spending (October)	**-0.3%**	**-0.2%**	Private residential construction was a drag on total activity in October, falling for the fifth consecutive month, although the latest decline was light (off 0.3% versus an average of -1.5% in the prior four months). Private nonresidential building fell 0.8%, but the drop represented only a modest offset to solid advances in the prior five months (average increase of 1.5%). Government-related construction rose 0.6%. Federal activity surged in the latest month, but the jump represented only a partial offset to a drop in September. Building by state and local governments rose modestly, but the pickup followed brisk advances in the prior four months.
Payroll Employment (November)	**263,000**	**200,000**	The increase of 263,000 in nonfarm payrolls in November slowed a bit from the average of 272,000 in the prior three months, but firms are still adding jobs at a solid clip despite aggressive tightening by the Fed and slowing economic growth. The unemployment rate was unchanged at 3.7% in November after an increase of 0.2 percentage point in the prior month. While unchanged from the prior reading, the November result carried a soft tone for the second consecutive month, as both employment measured by the household survey and the size of the labor force declined (off 138,000 and 186,000, respectively). Average hourly earnings jumped 0.6% from an upwardly revised reading in the prior month (0.5% versus 0.4%).

Sources: The Conference Board (Consumer Confidence); Bureau of Economic Analysis (Revised GDP, Personal Income, Consumption & Core Price Index); U.S. Census Bureau (U.S. International Trade in Goods, Construction Spending); Institute for Supply Management (ISM Manufacturing Index); Bureau of Labor Statistics (Job Openings, Payroll Employment); Consensus forecasts are from Bloomberg

Preview

Week of Dec. 5, 2022	Projected	Comments
ISM Services Index (November) (Monday)	**53.0 (-1.4 Index Pts.)**	With tight financial conditions filtering through the economy, the services index slipped from a record high of 68.4 last November to 54.4 in October. Recent softening in data and increased expectations of recession next year suggest further easing in November.
Factory Orders (October) (Monday)	**1.0%**	The already published increase of 1.0% in new orders for durable goods appears likely to be joined by a firm advance in the nondurable area, as higher prices could boost the value of petroleum and coal bookings. Orders for other nondurable goods have shown little change in the past three months as soft real flows have offset price effects.
Trade Balance (October) (Tuesday)	**-$80.0 Billion ($6.7 Billion Wider Deficit)**	The widening of $7.1 billion in the goods trade deficit (published November 30) is likely to dominate the report on total international trade for October, although a pickup in the service surplus after a drop in the prior month could provide a modest offset.
Revised Nonfarm Productivity (2022-Q3) (Wednesday)	**0.8% (+0.5 Pct. Pt. Revision)**	An upward revision to the measure of output used in the calculation of nonfarm productivity suggests a positive adjustment in Q3, although productivity growth is likely to remain miniscule relative to the drop in the prior two quarters (average decline of 5.0%). The expected revision to productivity points to a downward adjustment to unit labor costs (2.8% rather than 3.5%), a notable moderation from a surge in the first half of the year (average quarterly advance of 8.7%, annual rate).
PPI (November) (Friday)	**0.1% Total, 0.2% Ex. Food & Energy**	Available quotes suggest that energy prices softened at the producer level in November, and increases in food prices appear to be slowing after a surge in the early months of the year. Easing supply constraints and moderating demand seem to be limiting pressure on prices excluding food and energy, which have averaged increases of 0.2% in the from June through October after an average of 0.7% in the first five months of the year.
Consumer Sentiment (December) (Friday)	**56.0 (-1.4%)**	Increased chatter about a possible recession next year and a recent pickup in layoff announcements are likely to weigh more heavily on consumer moods than the recent decline in gasoline prices, suggesting a another depressed reading on consumer sentiment in early December.

Source: Forecasts provided by Daiwa Capital Markets America

Economic Indicators

November / December2022

Monday	Tuesday	Wednesday	Thursday	Friday
28	29	30	1	2
	FHFA HOME PRICE INDEX July -0.6% Aug -0.7% Sep 0.1% **S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX** July -0.8% Aug -1.3% Sep -1.2% **CONFERENCE BOARD CONSUMER CONFIDENCE** Sep 107.8 Oct 102.2 Nov 100.2	**ADP EMPLOYMENT REPORT** Private Payrolls Sep 192,000 Oct 239,000 Nov 127,000 **REVISED GDP** GDP / Chained Price 22-Q2 -0.6% 9.0% 22-Q3(a) 2.6% 4.1% 22-Q3(p) 2.9% 4.3% **INTERNATIONAL TRADE IN GOODS** Aug -$85.8 billion Sep -$91.9 billion Oct -$99.0 billion **ADVANCE INVENTORIES** Wholesale / Retail Aug 1.4% 1.4% Sep 0.6% -0.1% Oct 0.8% -0.2% **JOLTS DATA** Openings (000) / Quit Rate Aug 10,280 2.7% Sep 10,687 2.7% Oct 10,334 2.6% **MNI CHICAGO BUSINESS BAROMETER** **PENDING HOME SALES** **BEIGE BOOK**	**UNEMP. CLAIMS** Initial / Continuing (millions) Nov 5 0.226 1.498 Nov 12 0.223 1.551 Nov 19 0.241 1.608 Nov 26 0.225 N/A **PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** Inc. / Cons. / Core Aug 0.3% 0.7% 0.5% Sep 0.4% 0.6% 0.5% Oct 0.7% 0.8% 0.2% **ISM MFG. INDEX** Index / Prices Sep 50.9 51.7 Oct 50.2 46.6 Nov 49.0 43.0 **CONSTRUCTION** Aug -1.1% Sep 0.1% Oct -0.3% **VEHICLE SALES** Sep 13.6 million Oct 15.1 million Nov 14.1 million	**EMPLOYMENT REPORT** Payrolls / Un. Rate Sep 269,000 3.5% Oct 284,000 3.7% Nov 263,000 3.7%
5	6	7	8	9
ISM SERVICES INDEX (10:00) Index / Prices Sep 56.7 68.7 Oct 54.4 70.7 **Nov 53.0 68.0** **FACTORY ORDERS (10:00)** Aug 0.2% Sep 0.2% **Oct 1.0%**	**TRADE BALANCE (8:30)** Aug -$65.7 billion Sep -$73.3 billion **Oct -$80.0 billion**	**REVISED PRODUCTIVITY & COSTS (8:30)** Productivity / Unit Labor Costs 22-Q2 -4.1% 8.9% 22-Q3(p) 0.3% 3.5% **22-Q3(r) 0.8% 2.7%** **CONSUMER CREDIT (3:00)** Aug $30.2 billion Sep $25.0 billion Oct --	**UNEMP. CLAIMS (8:30)**	**PPI (8:30)** Final Demand / Ex. Food & Energy Sep 0.2% 0.2% Oct 0.2% 0.0% **Nov 0.1% 0.2%** **CONSUMER SENTIMENT (10:00)** Oct 59.9 Nov 56.8 **Dec 56.0** **WHOLESALE TRADE (10:00)** Inventories / Sales Aug 1.4% 0.0% Sep 0.6% 0.4% **Oct 0.8% 0.3%**
12	13	14	15	16
FEDERAL BUDGET	**NFIB SMALL BUSINESS OPTIMISM IINDEX** **CPI** **FOMC (1ST DAY)**	**IMPORT/EXPORT PRICES** **FOMC DECISION**	**UNEMP. CLAIMS** **RETAIL SALES** **EMPIRE MFG. INDEX** **PHILY FED MFG. INDEX** **INDUSTRIAL PROD.** **BUSINESS INVENTORIES** **TIC FLOWS**	
19	20	21	22	23
NAHB HOUSING INDEX	**HOUSING STARTS**	**CURRENT ACCOUNT** **EXISTING HOME SALES** **CONSUMER CONFIDENCE**	**UNEMP. CLAIMS** **REVISED GDP** **CHI. FED NATIONAL ACTIVITY INDEX** **LEADING ECONOMIC INDICATORS**	**PERSONAL INCOME, CONSUMPTION, PRICES** **DURABLE GOODS ORDERS** **NEW HOME SALES** **CONSUMER SENTIMENT**

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

Treasury Financing

November / December 2022

Monday	Tuesday	Wednesday	Thursday	Friday
28	**29**	**30**	**1**	**2**
AUCTION RESULTS: Rate / Cover 13-week bills 4.285% 2.56 26-week bills 4.550% 2.90	**AUCTION RESULTS:** Rate / Cover 52-week bills 4.555% 2.83 **ANNOUNCE:** $45 billion 4-week bills for auction on Dec 1 $45 billion 8-week bills for auction on Dec 1 $33 billion 17-week bills for auction on Nov 30	**AUCTION RESULTS:** Rate / Cover 17-week bills 4.430% 3.10 **SETTLE:** $15 billion 20-year bonds $15 billion 10-year TIPS $42 billion 2-year notes $43 billion 5-year notes $35 billion 7-year notes	**AUCTION RESULTS:** Rate / Cover 4-week bills 3.950% 3.43 8-week bills 4.080% 2.76 **ANNOUNCE:** $99 billion 13-,26-week bills for auction on Dec 5 **SETTLE:** $99 billion 13-,26-week bills $34 billion 52-week bills	
5	**6**	**7**	**8**	**9**
AUCTION: $99 billion 13-,26-week bills	**ANNOUNCE** $45 billion* 4-week bills for auction on Dec 8 $45 billion* 8-week bills for auction on Dec 8 $33 billion* 17-week bills for auction on Dec 7 **SETTLE:** $45 billion 4-week bills $45 billion 8-week bills $33 billion 17-week bills	**AUCTION:** $33 billion* 17-week bills	**AUCTION:** $45 billion* 4-week bills $45 billion* 8-week bills **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on Dec 12 $40 billion* 3-year notes for auction on Dec 12 $32 billion* 10-year notes for auction on Dec 12 $18 billion* 30-year bonds for auction on Dec 13 **SETTLE:** $99 billion 13-,26-week bills	
12	**13**	**14**	**15**	**16**
AUCTION: $99 billion* 13-,26-week bills $40 billion* 3-year notes $32 billion* 10-year notes	**AUCTION:** $18 billion* 30-year bonds **ANNOUNCE:** $45 billion* 4-week bills for auction on Dec 15 $45 billion* 8-week bills for auction on Dec 15 $33 billion* 17-week bills for auction on Dec 14 **SETTLE:** $45 billion* 4-week bills $45 billion* 8-week bills $33 billion* 17-week bills	**AUCTION:** $33 billion* 17-week bills	**AUCTION:** $55 billion* 4-week bills $50 billion* 8-week bills **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on Dec 19 $12 billion* 20-year bonds for auction on Dec 21 $19 billion* 5-year TIPS for auction on Dec 22 **SETTLE:** $99 billion* 13-,26-week bills $40 billion* 3-year notes $32 billion* 10-year notes $18 billion* 30-year bonds	
19	**20**	**21**	**22**	**23**
AUCTION: $99 billion* 13-,26-week bills	**ANNOUNCE:** $45 billion* 4-week bills for auction on Dec 22 $45 billion* 8-week bills for auction on Dec 22 $33 billion* 17-week bills for auction on Dec 21 **SETTLE:** $45 billion* 4-week bills $45 billion* 8-week bills $33 billion* 17-week bills	**AUCTION:** $33 billion* 17-week bills $12 billion* 20-year bonds	**AUCTION:** $55 billion* 4-week bills $50 billion* 8-week bills $19 billion* 5-year TIPS **ANNOUNCE:** $99 billion* 13-,26-week bills for auction on Dec 27 $34 billion* 52-week bills for auction on Dec 27 $42 billion* 2-year notes for auction on Dec 27 $43 billion* 5-year notes for auction on Dec 28 $35 billion* 7-year notes for auction on Dec 29 $22 billion* 2-year FRNs for auction on Dec 28 **SETTLE:** $99 billion* 13-,26-week bills	

**Estimate*