U.S. Economic Comment

- Payrolls: moderating trend, but still firm
- Wage growth: inconsistent with two-percent inflation

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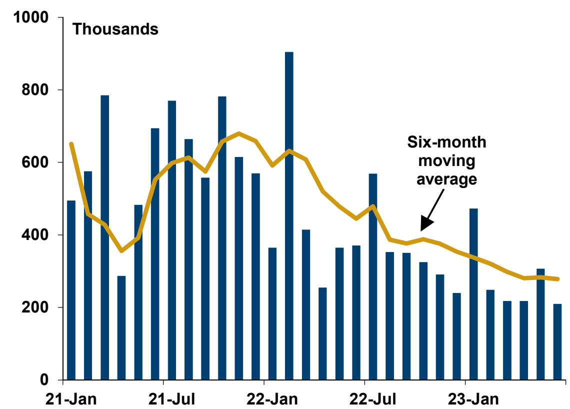
June Employment

We suspect that market participants were poised on Friday for an upside surprise on nonfarm payrolls. The National Employment Report published jointly by the ADP Research Institute and the Stanford Digital Economy Lab triggered downside volatility in the equity market and higher Treasury rates on Thursday with its June release indicating private-sector job growth of 497,000 versus a more conservative consensus estimate of 225,000. Prospects for additional policy tightening beyond that indicated in the Fed's latest dot plot (median of 5.625 percent for year-end 2023) appeared to be a possibility to address resurgent job growth. Fears subsided on Friday with a payroll print of 209,000 (+149,000 private-sector growth) and downward revisions to past months' data totaling 110,000 (chart, left). However, we would argue that while the June payroll print failed to match lofty expectations after ADP and lagged by a wide margin the average of 283,000 in the prior six months, it was still firm by longer-term standards and likely to trigger additional action by the FOMC. Even after the payroll miss, market participants also seem to share this view. The implied probability of a 25-basis-point rate hike at the July 25-26 meeting as calculated by futures prices currently exceeds 90 percent (chart, right).

Payrolls

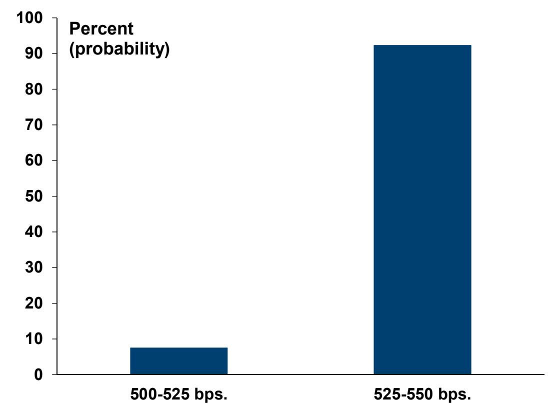
Digging into the payroll data revealed some interesting shifts by industry but lacked any evidence of a broad slowdown in hiring. On the soft side, temporary help services cut jobs for the sixth time in the past eight months (-13,000 in June). Trimming temporary workers often precedes broader layoffs, but we have not seen significant evidence of this thus far in the current cycle. Hiring slowed in other areas. The leisure and hospitality industry, for example, added "only" 21,000 workers in June after similar additions in the prior two months. The soft results contrasted to average growth of 67,000 in Q1 and 88,000 last year, which suggests the industry has "right-sized" employment levels after cuts during COVID-related shutdowns. This industry, however, appears unlikely to cut payrolls in the near future given the resurgence of dining out, travel, etc. On a firmer note, the healthcare industry added at a brisk clip (+65,000, matching the average in the prior six months). In addition, the cyclically sensitive construction industry offered further evidence of a rebound, adding 23,000 jobs for the second consecutive month – a move that has coincided with firmer building activity. In all, dynamics tilt favorably amid some top-line slowing in job growth.

Change in Nonfarm Payrolls



Sources: Bureau of Labor Statistics via Haver Analytics

Target Rate Probability for July FOMC Meeting



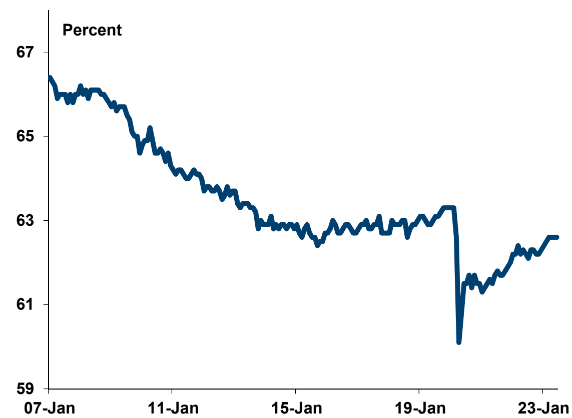
Source: CME Group, FedWatch Tool

The Household Survey & Wages

The unemployment rate, which eased by 0.1 percentage point to 3.6 percent in June stood as a stark reminder of tight labor market conditions. It is still almost one half percentage point below the long-run view of Fed officials of 4.0 percent, which could be considered the full-employment unemployment rate. Either the supply of workers needs to increase further, or demand for workers needs to cool more than it has already.

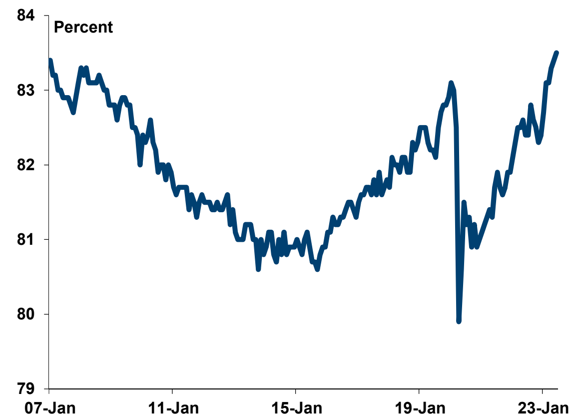
We are not particularly optimistic regarding additional help from the supply side. The labor-force participation rate has stalled at 62.6 percent for the third consecutive month after increasing in the second half of last year and early 2023. It remains below pre-COVID levels (chart, left). The prime-age participation rate (the rate for individuals aged 25-54) has continued to rise after eclipsing pre-COVID levels, including an uptick to 83.4 percent in June, but additional assistance from this group to offset retirements or other withdrawals appears limited given recent elevated readings (chart, right). Thus, Fed officials may have to do more to control labor demand.

Labor Force Participation Rate



Sources: Bureau of Labor Statistics via Haver Analytics

Prime-Age Labor Force Participation Rate*

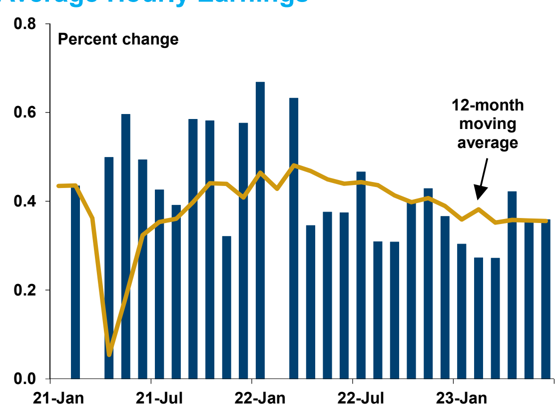


** Labor force participants aged 25 to 54.as a share of the civilian non-institutional population aged 25 to 54.*

Source: Bureau of Labor Statistics via Haver Analytics

The ongoing imbalance is evident in brisk wage growth, which increased 0.4 percent in June, a reading little changed from the underlying average (chart). The shift translated to year-over-year growth of 4.4 percent, down from the cycle high of 5.9 percent in March 2022 but little changed from other recent observations. Wage growth would need to moderate to something closer to three percent (target inflation plus a modest trend increase in productivity) to be consistent with stable prices over time. Moreover, other measures of wages (Atlanta Fed Wage Tracker, Employment Cost Index) suggest that wage pressure may be more acute than suggested average earnings.

Average Hourly Earnings



Source: Bureau of Labor Statistics via Haver Analytics

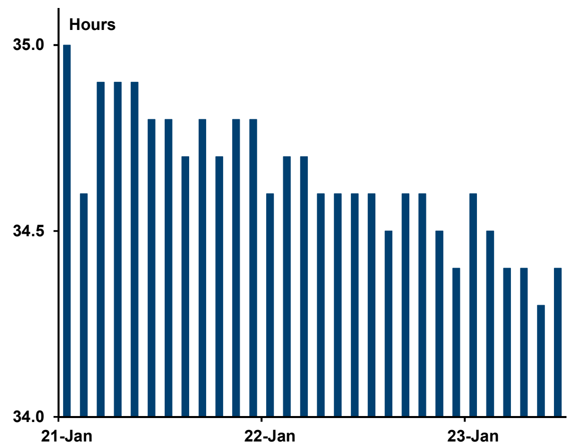
An Addendum on the Workweek

While data on the length of the workweek often takes a backseat to other data on employment day, we pay close attention to this metric as it is a key variable that can influence output. Putting aside considerations regarding productivity growth, firms can boost output by increasing the amount of employees, employee hours, or both. The average workweek increased 0.1 hour in June to 34.4 hours, but it remained in the low end of the recent range (chart, next page, left). The pickup, combined with the increase in payrolls, led to a jump of 0.4

percent in the aggregate hours index after a net decline in the prior four months (chart, right). For the second quarter, aggregate hours increased 0.1 percent, annual rate, versus 2.4 percent in Q1.

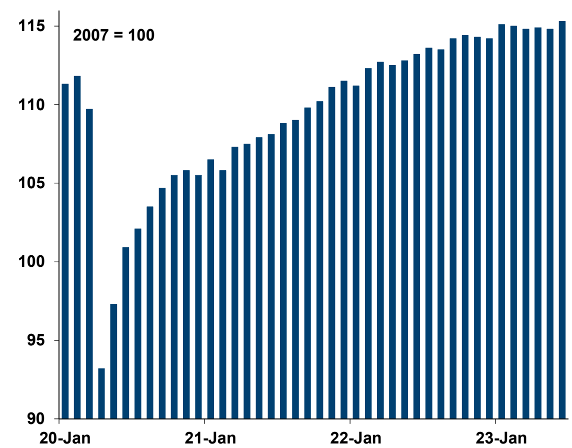
We hesitate to draw broad conclusions from top-line data on the workweek and aggregate hours, but we suspect that firms are tinkering with production runs and scaling back hours to a degree to maintain headcount. Firms have struggled to fill positions for much of the current expansion, and they don't want to get caught unprepared when the economy accelerates again (as occurred in many cases in the immediate period following the post-pandemic reopening of the economy). Thus, so-called labor-hoarding could be another contributory factor to tight labor-market conditions.

Average Weekly Hours



Sources: Bureau of Labor Statistics via Haver Analytics

Aggregate Weekly Hours Index*



** Total private industries.*

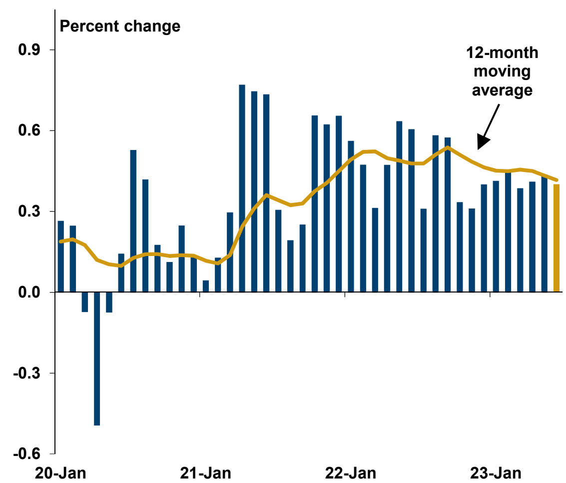
Source: Bureau of Labor Statistics via Haver Analytics

The Week Ahead

CPI (June) (Wednesday)
Forecast: 0.3% Headline; 0.4% Core

Available quotes suggest the costs of energy commodities increased modestly in June, while prices of energy services could provide a partial offset with a sixth consecutive month of declines. The energy index, on balance, is still well above its pre-COVID level, but it has fallen 17 percent since its peak in June 2022. The food index also has surged in the current expansion, advancing almost 23 percent since February 2022, but the trend has flattened in recent months. Costs of restaurant meals are still advancing at a brisk clip (0.5 percent per month in the past six months), but costs of meals at home only rose 0.2 percent per month over that span (inclusive of an average decline of 0.1 percent per month in the three months ended May). In the core component, goods prices have moderated since a spike during the pandemic and early stages of the current expansion, but they are showing signs of stirring (average increase of 0.6 percent in the past two months versus an average decline of 0.05 percent in the six months ended March). Prices of services excluding energy have remained under pressure (average advance of 0.5 percent in the past 6 months). With core goods prices having possibly bottomed, and with costs of housing services slowing only modestly, another brisk increase in the core is possible in June (charts).

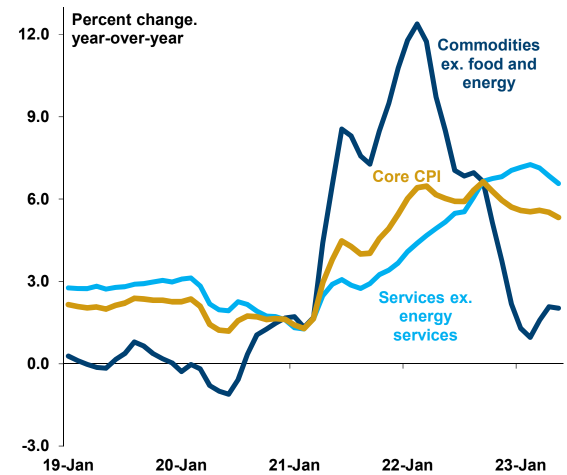
Core CPI*



** The gold bar is a forecast for June 2023.*

Sources: Bureau of Labor Statistics *via Haver Analytics*; Daiwa Capital Markets America

Core CPI, Year-Over-Year

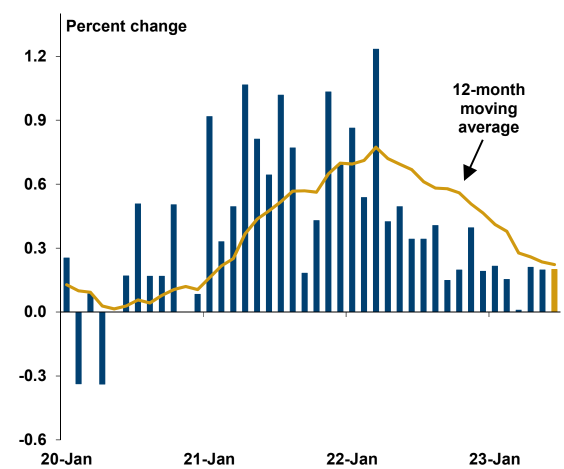


Source: Bureau of Labor Statistics via Haver Analytics

PPI (June) (Thursday)
Forecast: 0.2% Headline; 0.2% Excluding Food & Energy

Data from wholesale energy markets suggest that energy prices rose modestly during the June survey period. Food prices at the producer level often move erratically, but they have fallen in five of the past six months (average decline of 1.0 percent over that span inclusive of a pickup of 0.3 percent in March). Prices excluding food and energy could post a moderate advance (chart, right). Core goods prices have increased 0.2 percent per month in the past six months, while service prices have averaged 0.1 percent. The trend in construction costs has slowed, with an average increase of 0.3 percent per month in the past six months versus 1.5 percent in the six months ended November 2022.

PPI Ex. Food & Energy*



** The gold bar is a forecast for June 2023.*

Sources: Bureau of Labor Statistics via Haver Analytics; Daiwa Capital Markets America

Federal Budget (June) (Thursday)
Forecast: $175.0 Billion Deficit

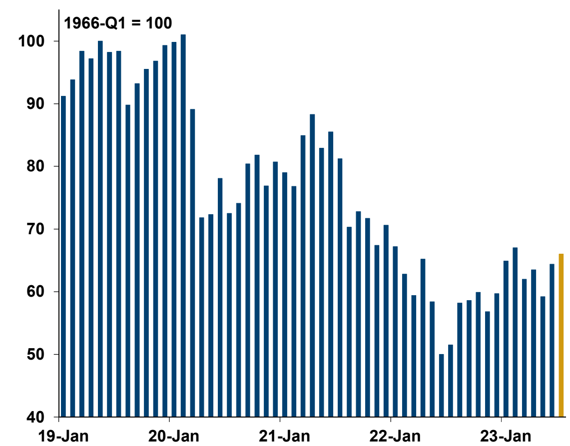
The federal government experienced marked deterioration in its budget position thus far in FY2023, with revenues dropping 11.3 percent and outlays jumping 9.4 percent versus the first eight months of FY2022. Available data suggest that the situation is unlikely to improve in June, with outlays down almost 10 percent year-over-year. If the forecast is realized, the deficit for the first nine months of FY2023 would total in excess of $1.3 trillion (versus a deficit of $515 billion in the same period in FY2022).

Consumer Sentiment (July) (Friday)
Forecast: 66.0 (+2.5%)

While the job market remains favorable, which all else equal would boost confidence, ongoing brisk inflation has strained household budgets for much of the current expansion. Thus, while sentiment improved in the first half of 2023 versus the closing months of last year (an average of 63.5 thus far in 2023 versus 58.8 in 2022-Q4), we do not anticipate sentiment in July to break out of the range in place for the past year and one-half (chart, left).

Although the effects of recent inflation have damaged the consumer psyche, survey respondents anticipate inflation to decelerate in coming months and remain contained in the longer run. The year-ahead inflation gauge fell to 3.3 percent in June, the lowest reading since early 2021, while the longer-term measure remained within its recent range (chart, right). Next week's report will provide an important update on these measures, which are watched closely by Fed officials.

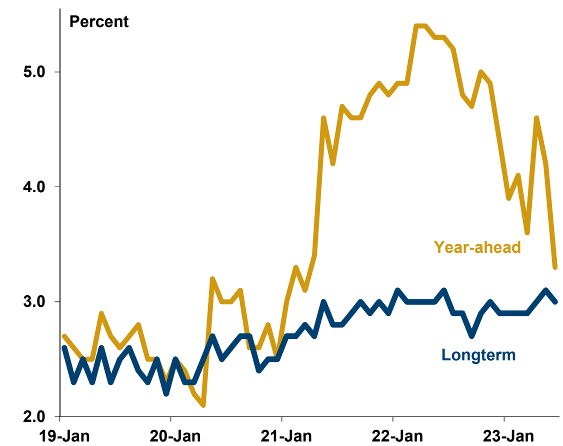
Consumer Sentiment*



** The gold bar is a forecast for July 2023.*

Sources: University of Michigan via Haver Analytics; Daiwa Capital Markets America

Consumer Inflation Expectations



Source: University of Michigan via Haver Analytics

Daiwa Capital Markets

Economic Indicators

July 2023

Monday 3

CONSTRUCTION

Mar	0.6%
Apr	0.4%
May	0.9%

ISM MFG. INDEX

	Index	Prices
Apr	47.1	53.2
May	46.9	44.2
June	46.0	41.8

Tuesday 4

INDEPENDENCE DAY

Wednesday 5

FACTORY ORDERS

Mar	0.6%
Apr	0.3%
May	0.3%

FOMC MINUTES

VEHICLE SALES

Apr	16.1 million
May	15.1 million
June	15.7 million

Thursday 6

UNEMPLOYMENT CLAIMS

	Initial	Continuing
	(millions)	
June 10	0.264	1.761
June 17	0.265	1.733
June 24	0.236	1.720
July 1	0.248	N/A

ADP EMPLOYMENT

	Private Payrolls
Apr	291,000
May	267,000
June	497,000

TRADE BALANCE

Mar	-$60.6 billion
Apr	-$74.4 billion
May	-$69.0 billion

JOLTS DATA

	Openings (000)	Quit Rate
Mar	9.745	2.5%
Apr	10,320	2.4%
May	9,824	2.6%

ISM SERVICES INDEX

	Index	Prices
Apr	51.9	59.6
May	50.3	56.2
June	53.9	54.1

Friday 7

EMPLOYMENT REPORT

	Payrolls	Un. Rate
Apr	217,000	3.4%
May	306,000	3.7%
June	209,000	3.6%

Monday 10

WHOLESALE TRADE (10:00)

	Inventories	Sales
Mar	-0.2%	-2.7%
Apr	-0.3%	0.2%
May	**-0.1%**	**0.3%**

CONSUMER CREDIT (3:00)

Mar	$22.8 billion
Apr	$23.0 billion
May	--

Tuesday 11

NFIB SMALL BUSINESS OPTIMISM INDEX (6:00)

Apr	89.0
May	89.4
June	--

Wednesday 12

CPI (8:30)

	Total	Core
Apr	0.4%	0.4%
May	0.1%	0.4%
June	**0.3%**	**0.4%**

BEIGE BOOK (2:00)

May 2023 Beige Book: "Economic activity was little changed overall in April and early May. Four Districts reported sma increases in activity, six no change, and two slight to moderate declines."

Thursday 13

UNEMP. CLAIMS (8:30)

PPI (8:30)

	Final Demand	Ex. Food & Energy
Apr	0.2%	0.2%
May	-0.3%	0.2%
June	**0.2%**	**0.2%**

FEDERAL BUDGET (2:00)

	2023	2022
Apr	$176.2B	$308.2B
May	-$240.3B	-$66.2B
June	**-$175.0B**	-$88.8B

Friday 14

IMPORT/EXPORT PRICES (8:30)

	Non-Petrol Imports	Nonagri. Exports
Apr	-0.2%	-0.1%
May	-0.2%	-1.8%
June	--	--

CONSUMER SENTIMENT (10:00)

May	59.2
June	64.4
July	**66.0**

Monday 17

EMPIRE MFG

Tuesday 18

RETAIL SALES

IP & CAP-U

BUSINESS INVENTORIES

NAHB HOUSING INDEX

TIC FLOWS

Wednesday 19

HOUSING STARTS

Thursday 20

UNEMP. CLAIMS

PHILLY FED INDEX

EXISTING HOME SALES

LEADING INDICATORS

Friday 21

Monday 24

CHICAGO FED NATIONAL ACTIVITY INDEX

Tuesday 25

FHFA HOUSE PRICE INDEX

S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX

CONSUMER CONFIDENCE

FOMC MEETING (FIRST DAY)

Wednesday 26

NEW HOME SALES

FOMC DECISION

Thursday 27

UNEMP. CLAIMS

Q2 GDP

ADVANCE INVENTORIES

DURABLE GOODS ORDERS

INTERNATIONAL TRADE IN GOODS

PENDING HOME SALES

Friday 28

PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX

EMPLOYMENT COST INDEX

REVISED CONSUMER SENTIMENT

Forecasts in bold.

Treasury Financing

July 2023

Monday	Tuesday	Wednesday	Thursday	Friday
3	4	5	6	7
AUCTION RESULTS: 13-week bills 5.230% 3.00 26-week bills 5.260% 3.02 42-day CMBs 5.170% 2.73 **ANNOUNCE:** $70 billion 4-week bills for auction on July 6 $60 billion 8-week bills for auction on July 6 $46 billion 17-week bills for auction on July 5	**INDEPENDENCE DAY**	**AUCTION RESULTS:** Rate Cover 17-week bills 5.250% 3.31 **SETTLE:** $70 billion 4-week bills $60 billion 8-week bills $46 billion 17-week bills	**AUCTION RESULTS:** Rate Cover 4-week bills 5.150% 2.54 8-week bills 5.200% 2.88 **ANNOUNCE:** $123 billion 13-,26-week bills for auction on July 10 $38 billion 52-week bills for auction on July 11 $40 billion 3-year notes for auction on July 11 $32 billion 10-year notes for auction on July 12 $18 billion 30-year bonds for auction on July 13 $50 billion 42-day CMBs for auction on July 11 **SETTLE:** $123 billion 13-,26-week bills $50 billion 42-day CMBs	
10	11	12	13	14
AUCTION: $123 billion 13-,26-week bills	**AUCTION:** $38 billion 52-week bills $40 billion 3-year notes $50 billion 42-day CMBs **ANNOUNCE:** $70 billion* 4-week bills for auction on July 13 $60 billion* 8-week bills for auction on July 13 $46 billion* 17-week bills for auction on July 12 **SETTLE:** $70 billion 4-week bills $60 billion 8-week bills $46 billion 17-week bills	**AUCTION:** $46 billion* 17-week bills $32 billion 10-year notes	**AUCTION:** $70 billion* 4-week bills $60 billion* 8-week bills $18 billion 30-year bonds **ANNOUNCE:** $123 billion* 13-,26-week bills for auction on July 17 $12 billion* 20-year bonds for auction on July 19 $17 billion* 10-year TIPS for auction on July 20 **SETTLE:** $123 billion 13-,26-week bills $38 billion 52-week bills $50 billion 42-day CMBs	
17	18	19	20	21
AUCTION: $123 billion* 13-,26-week bills **SETTLE:** $40 billion 3-year notes $32 billion 10-year notes $18 billion 30-year bonds	**ANNOUNCE:** $70 billion* 4-week bills for auction on July 20 $60 billion* 8-week bills for auction on July 20 $46 billion* 17-week bills for auction on July 19 **SETTLE:** $70 billion* 4-week bills $60 billion* 8-week bills $46 billion* 17-week bills	**AUCTION:** $46 billion* 17-week bills $12 billion* 20-year bonds	**AUCTION:** $70 billion* 4-week bills $60 billion* 8-week bills $17 billion* 10-year TIPS **ANNOUNCE:** $123 billion* 13-,26-week bills for auction on July 24 $42 billion* 2-year notes for auction on July 24 $43 billion* 5-year notes for auction on July 25 $35 billion* 7-year notes for auction on July 27 $24 billion* 2-year FRNs for auction on July 26 **SETTLE:** $123 billion* 13-,26-week bills	
24	25	26	27	28
AUCTION: $123 billion* 13-,26-week bills $42 billion* 2-year notes	**AUCTION:** $43 billion* 5-year notes **ANNOUNCE:** $70 billion* 4-week bills for auction on July 27 $60 billion* 8-week bills for auction on July 27 $46 billion* 17-week bills for auction on July 26 **SETTLE:** $70 billion* 4-week bills $60 billion* 8-week bills $46 billion* 17-week bills	**AUCTION:** $46 billion* 17-week bills $24 billion* 2-year FRNs	**AUCTION:** $70 billion* 4-week bills $60 billion* 8-week bills $35 billion* 7-year notes **ANNOUNCE:** $123 billion* 13-,26-week bills for auction on July 31 **SETTLE:** $123 billion* 13-,26-week bills	

**Estimate*