U.S. Economic Comment

- August employment: continued improvement in supply-demand imbalances
- Supplementary labor market data: supporting evidence of softening conditions
- Inflation update: two percent not yet assured

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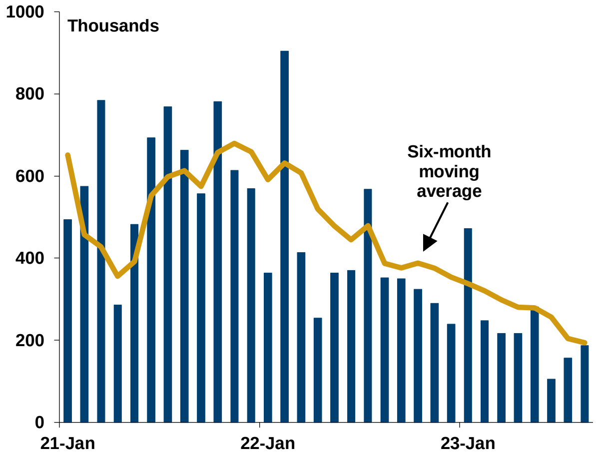
August Employment

The increase of 187k in nonfarm payrolls in August was firmer than the expectation for a gain of 170k, and the print would have been stronger (approximately 240k) but for two special factors. First, the bankruptcy at Yellow contributed importantly to a decline of 37k in trucking transportation. Second, the ongoing Hollywood actors' strike led to a drop of 17k in the motion picture industry. Revisions of -110k in the prior two months softened the tone of the report to a degree, but average payroll growth of 194k in the past 6 months (inclusive of the special factors and revisions) is still solid from a longer-term perspective (chart, below left). For comparison, job growth in 2019 averaged 163k per month – a performance lauded by Fed officials at the time. However, payroll growth has slowed markedly from the 399k average monthly gain in 2022 and the 360k average in January/February 2023. The effects of restrictive monetary policy have started to diffuse through the economy with effects leading to gradual moderation in payroll growth.

That moderation may also be influencing wages somewhat, as average hourly earnings increased 0.2 percent in August versus an average of 0.36 percent in the previous 12 months (chart, below right). The change equated to a year-over-year increase of 4.3 percent, below the recent high of 5.9 percent in March of last year but viewed as still inconsistent with a return to two-percent inflation. Moreover, recent demands by large unions (Teamsters representing UPS, the United Autoworkers, and others) suggest that wage pressures could intensify as workers seek to recover lost purchasing power after the recent bout of inflation.

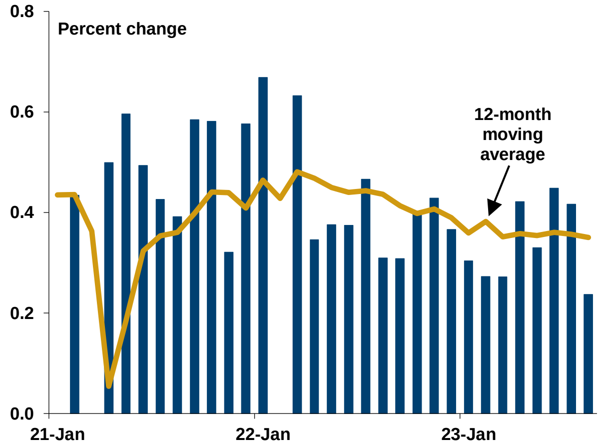
We were more encouraged by developments in the Household Survey data, as they suggest that supply and demand in the labor market are coming into better balance. The unemployment rate increased by 0.3 percentage point to 3.8 percent (chart, next page, left). The rate is still exceedingly low by historical standards and could be viewed as consistent with a fully employed economy, thus indicating progress. Critical to the latest shift was a surge of 736k in the size of the labor force, among the largest increases of the past few years (chart, next page, right). The move signaled a meaningful injection of new supply that could help contribute to slowing wage growth. We would also highlight, although less enthusiastically, the increase of 514k unemployed persons, the largest since COVID-related distortions in 2020. This metric indicates softening demand while supply is picking up.

Change in Nonfarm Payrolls



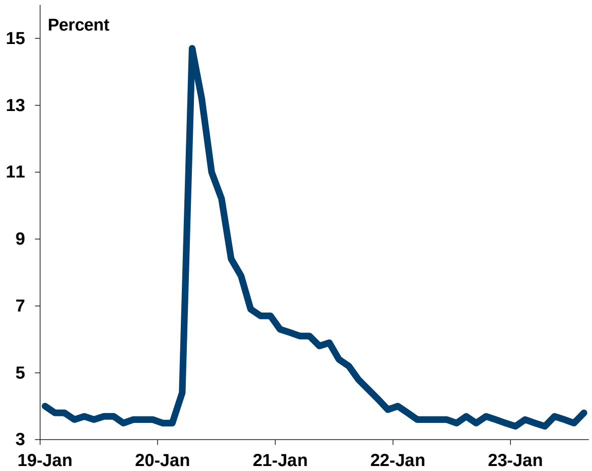
Source: Bureau of Labor Statistics via Haver Analytics

Average Hourly Earnings



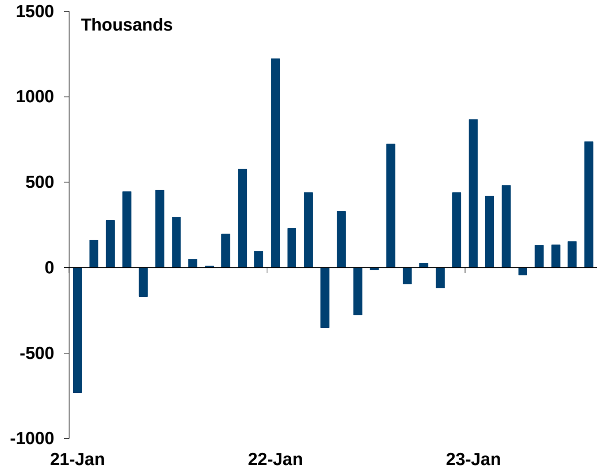
Source: Bureau of Labor Statistics via Haver Analytics

Unemployment Rate



Source: Bureau of Labor Statistics via Haver Analytics

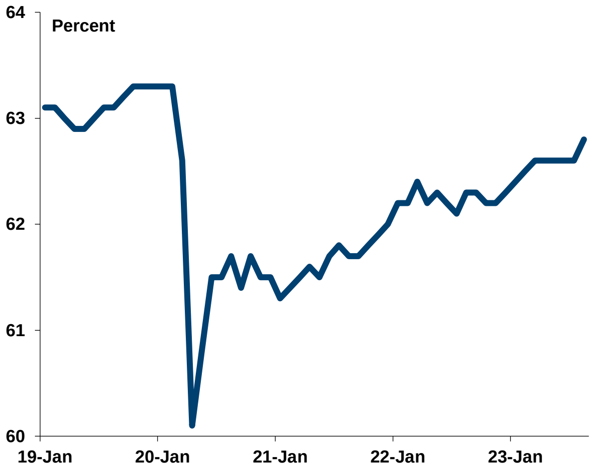
Change in the Labor Force



Source: Bureau of Labor Statistics via Haver Analytics

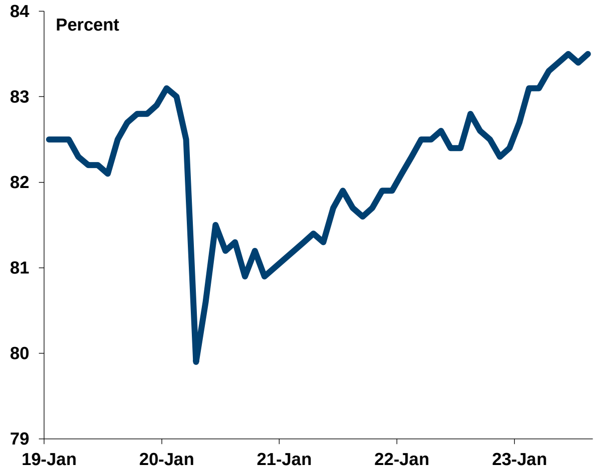
To provide a different view on the positive aspects of the data, the jump in the labor force pushed the participation rate 0.2 percentage point higher to 62.8 percent – the highest of the current expansion. Prime-age participation returned to the high of the current expansion as well (83.5 percent) and exceeded pre-pandemic levels (charts, below).

Labor Force Participation Rate



Source: Bureau of Labor Statistics via Haver Analytics

Prime-Age Labor Force Participation Rate*



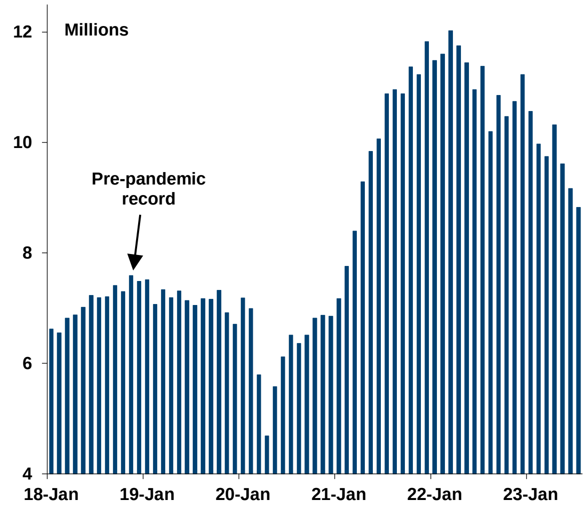
** Labor force participants aged 25 to 54 as a share of the civilian non-institutional population aged 25 to 54.*
Source: Bureau of Labor Statistics via Haver Analytics

Other Labor Market Data

Additional data on the labor market released earlier this week support the view that underlying labor market conditions are easing. The Job Openings and Labor Turnover Survey (JOLTS) for July, which was released on Tuesday, indicated that job openings, a key measure of labor demand, fell by 338k to 8.827 million. Moreover, the shift occurred from a downwardly revised reading in June (9.165 million versus 9.582 million), which suggests that the labor market could be cooling more rapidly than previously believed. Openings remain above the pre-pandemic peak of 7.594 million in November 2018, but they have now fallen by 3.2 million from the peak of 12.027 million in March 2022, with about three quarters of the slippage occurring this year (chart, next page, left). There are now approximately 1.5 job openings per unemployed individual, down from 2.0 in March 2022.

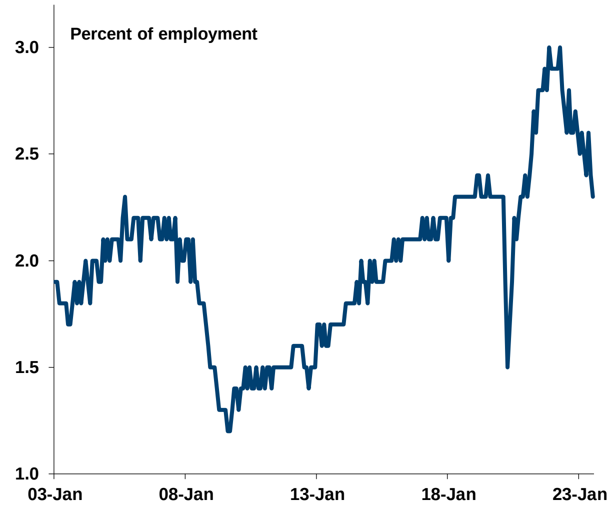
Workers appear to perceive the shift in underlying conditions, as indicated by data in the JOLTS and Conference Board's confidence survey for August. Quits (from the JOLTS), which indicate a worker's willingness to leave a current position for a new opportunity, ebb and flow depending on the strength of the labor market. They fell by 253k to 3.549 million in July. As a share of employment, quits dropped to 2.3 percent, well off the recent high of 3.0 percent in April 2022, indicating that more workers are voluntarily remaining in current positions (chart, below right). Similarly, the job appraisal measure in the Conference Board's survey caught the attention of market participants. The share of survey respondents indicating that jobs were plentiful fell to 40.3 percent from 43.7 percent, while the share reporting that jobs were hard-to-get rose to 14.1 percent from 11.3 percent. The net reading (plentiful less hard-to-get) was the lowest since the spring of 2021.

Job Openings



Source: Bureau of Labor Statistics via Haver Analytics

Quit Rate



Source: Bureau of Labor Statistics via Haver Analytics

July Inflation: Still Too Fast

The July reading on the price index for personal consumption expenditures (PCE) released on Thursday with the Bureau of Economic Analysis's Personal Income and Outlays Report likely strengthened the case for a pause in rate hikes at the September 19-20 FOMC meeting, although we viewed it as still insufficient to convince us that inflation is on a trajectory back to two percent. We have already seen instances in this cycle where inflation has slowed and then reaccelerated or when new pressure points have emerged as others have receded. Thus, we maintain the view that officials will hike the target range for the federal funds rate to a range of 5.50 to 5.75 percent, but we anticipate the move occurring at the October 31-November 1 meeting rather than in September, thereby allowing policymakers to review a broad array of additional data that may provide critical insight into economic developments. And, after reaching the terminal rate, we do not anticipate a pivot occurring until 2024-Q2, followed by a restrictive stance for an extended period thereafter.

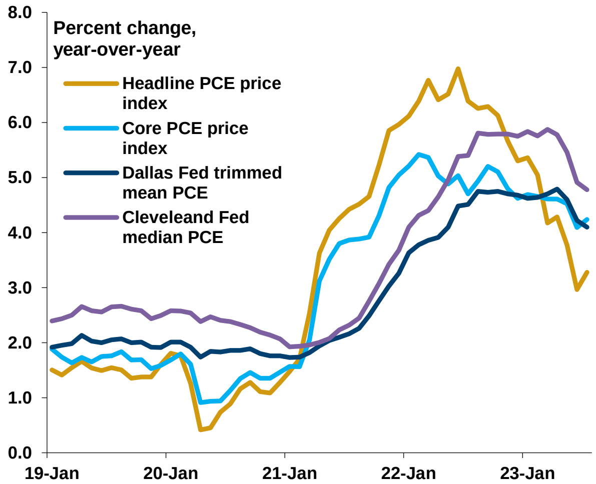
In one sense, inflation-related developments can be viewed favorably. The headline price index rose 0.2 percent for the second consecutive month after an increase of only 0.1 percent in May, with both food and energy prices continuing to moderate after coming under significant pressure earlier in the expansion Moreover, the core index has increased 0.2 percent per month in the past two months. Headline inflation rose 3.3 percent, year-over-year, but it is well below the recent peak of 7.0 percent in June 2022; core inflation also rose 0.1 percentage point to 4.2 percent, but it too has decelerated from 5.4 percent in February 2022 (chart, below left). Within the core component, we have finally seen hints of easing in vehicle prices (-1.3 percent in July), and continued discounting in the prices of other core goods – the costs of TVs fell 1.4 percent, the fifth large decline in the past six months, and appliance prices (-0.5 percent) dropped for the sixth month in the past seven.

With that said, other areas remain a concern. The increase in primary rents slowed to 0.4 percent from an average of 0.6 percent in the previous six months, and imputed rents of owner-occupied housing rose 0.5 percent (versus 0.6 percent in the prior six months). Fed officials expect additional moderation in shelter costs, but various measures of rents and home prices have again started increasing. Core service prices excluding housing services, which are being monitored closely by Fed officials, jumped 0.5 percent (4.7 percent, year-over-year, up from 4.1 percent in June). This area has shown little evidence of improvement. Large shifts in costs of financial service fees and commissions (+4.3 percent) and spectator sporting events (+5.9 percent), while being somewhat esoteric categories, played a role in the increase, but they were not solely responsible for it.

Data series from various Federal Reserve banks eliminate outlier observations to provide a better sense of underlying inflation. These too do not yet indicate compelling evidence of a broadly-based retreat in inflation. The Trimmed Mean PCE Price Index from the Federal Reserve Bank of Dallas, which eliminates 24 percent of the weighted distribution of price changes from the lower tail of the distribution and 31 percent from the upper tail, recorded year-over-year inflation of 4.1 percent, down slightly from 4.2 percent in June and only 1.2 percentage points below the cycle high of 5.4 percent in February 2022. The Median PCE measure from the Federal Reserve Bank of Cleveland, which observes only the central point of the distribution, showed a slowing in the year-over-year inflation rate (down 0.1 percentage point to 4.8 percent), but the pace was still problematic (chart, below left).

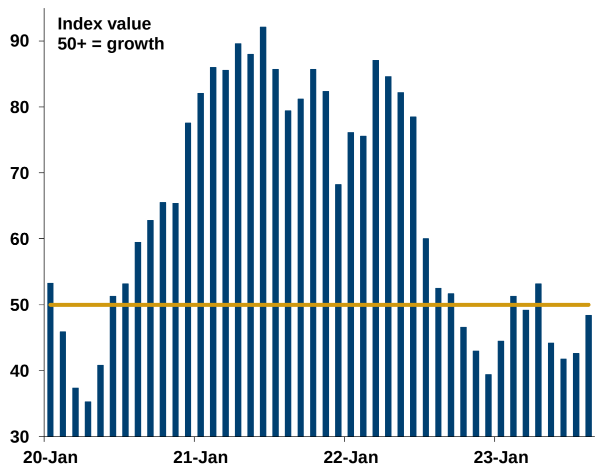
Additional concern may be warranted when monitoring potential new pressure points as well. The price of West Texas intermediate crude oil is up almost 28 percent from the recent low in mid-June, and other commodity prices are showing signs of stirring. These could again contribute to a renewed acceleration in headline inflation. The price index released with today's ISM factory report for August showed that prices were still contracting, but the latest reading of 48.4 was up from the recent low of 39.4 in December of last year and again close to indicating increasing prices (chart, below right). In all, continued vigilance on inflation and a restrictive monetary policy setting are still required by the FOMC to achieve the two-percent price stability mandate.

PCE



Sources: Bureau of Economic Analysis, Federal Reserve Bank of Dallas, and Federal Reserve Bank of Cleveland via Haver Analytics

ISM Manufacturing: Prices Index



Source: Institute for Supply Management via Haver Analytics

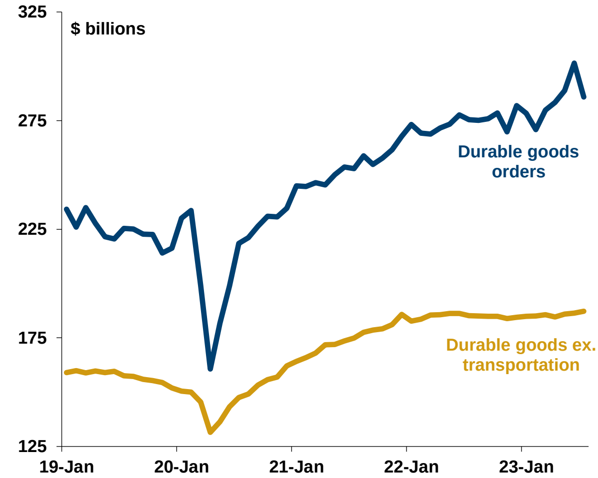
Daiwa Capital Markets

The Week Ahead

Factory Orders (July) (Tuesday)
Forecast: -2.0%

The soft headline performance for durable goods orders in July reported on August 24 most likely will carry over to Tuesday's report on total factory bookings. However, note that the plunge of 5.2 percent in durable goods orders after four consecutive monthly increases was mostly the result of a drop of 14.3 percent in transportation bookings (which reflected a drop 39.5 percent in combined civilian and defense-related aircraft bookings after recent high-side volatility). Durable bookings excluding transportation rose 0.5 percent in July, the third consecutive increase, tilting higher after a sluggish performance since the summer of 2022. Nondurable bookings could increase, with higher prices boosting petroleum-related orders.

Factory Orders



Source: U.S. Census Bureau via Haver Analytics

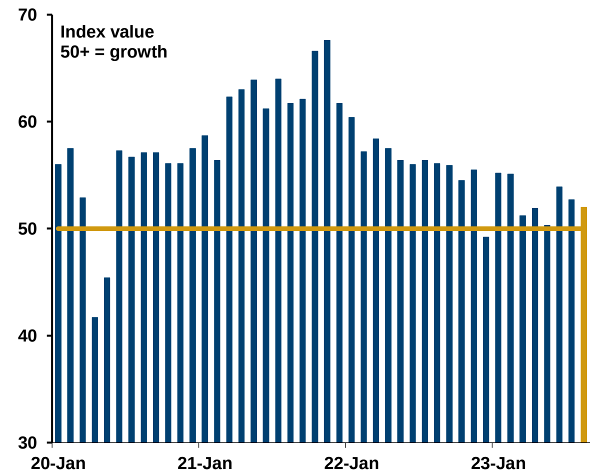
Trade Balance (July) (Wednesday)
Forecast: -$68.0 Billion ($2.5 Billion Wider Deficit)

The widening of $2.3 billion in the goods deficit published August 30 is likely to translate to similar deterioration in the total trade deficit in July. In addition, the service surplus could ease for the second consecutive month after a jump of $1.1 billion in May.

ISM Services Index (August) (Wednesday)
Forecast: 52.0 (-0.7 Index Pt.)

Although the economy faces challenges from restrictive monetary policy, the service sector has proved resilient and continued on a growth trajectory. That growth trend likely remained intact in August, although easing in business activity from an elevated reading of 57.1 could nudge the headline index lower. Keep an eye on the prices index, which registered a reading of 56.8 in July. Rather than raw materials, wages factor importantly into the costs of service firms, and underlying wage growth in the 4.0 to 4.5 percent range could exert upward pressure on this measure.

ISM Services Index



** The gold bar is a forecast for August 2023.*
Sources: Institute for Supply Management via Haver Analytics; Daiwa Capital Markets America

Revised Nonfarm Productivity (23-Q2) (Thursday)
Forecast: 3.2% (-0.5 Pct. Pt. Revision)

A downward revision to the output measure that feeds through to the calculation of productivity points to a downward adjustment of the previously reported brisk productivity growth in Q2. However, anticipated growth in excess of 3.0 percent is still an encouraging development after a contraction of 1.6 percent in productivity in 2022. Unit labor costs also could be revised higher (1.8 percent expected versus 1.6 percent preliminary estimate), reflecting both slower productivity and an upward revision to compensation per hour.

Economic Indicators

August/September 2023

Monday	Tuesday	Wednesday	Thursday	Friday
28	29	30	31	1
	FHFA HOME PRICE INDEX Apr 0.8% May 0.7% June 0.3% **S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX** Apr 0.9% May 1.0% June 0.9% **JOLTS DATA** Openings (000) / Quit Rate May 9,616 2.6% June 9,165 2.4% July 8,827 2.3% **CONFERENCE BOARD CONSUMER CONFIDENCE** June 110.1 July 114.0 Aug 106.1	**ADP EMPLOYMENT** Private Payrolls June 455,000 July 312,000 Aug 177,000 **REVISED GDP** GDP / Chained Price 23-Q1 2.0% 4.1% 23-Q2 (a) 2.4% 2.2% 23-Q2 (p) 2.1% 2.0% **INTERNATIONAL TRADE IN GOODS** May -$91.6 billion June -$88.8 billion July -$91.2 billion **ADVANCE INVENTORIES** Wholesale / Retail May -0.4% 0.6% June -0.7% 0.5% July -0.1% 0.3% **PENDING HOME SALES** May -2.5% June 0.4% July 0.9%	**UNEMPLOYMENT CLAIMS** Initial / Continuing (millions) Aug 5 0.250 1.711 Aug 12 0.240 1.697 Aug 19 0.232 1.725 Aug 26 0.228 N/A **PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** Inc. / Cons. / Core May 0.4% 0.2% 0.3% June 0.3% 0.6% 0.2% July 0.2% 0.8% 0.2% **MNI CHICAGO BUSINESS BAROMETER** Index / Prices June 41.5 53.5 July 42.8 62.1 Aug 48.7 74.0	**EMPLOYMENT REPORT** Payrolls / Un. Rate June 105,000 3.6% July 157,000 3.5% Aug 187,000 3.8% **ISM MFG. INDEX** Index / Prices June 46.0 41.8 July 46.4 42.6 Aug 47.6 48.4 **CONSTRUCTION** May 2.0% June 0.6% July 0.7% **VEHICLE SALES** June 15.7 million July 15.7 million Aug 15.0 million
4	5	6	7	8
LABOR DAY	**FACTORY ORDERS (10:00)** May 0.4% June 2.2% **July -2.0%**	**TRADE BALANCE (8:30)** May -$68.3 billion June -$65.5 billion **July -$68.0 billion** **ISM SERVICES INDEX (10:00)** Index / Prices June 53.9 54.1 July 52.7 56.8 **Aug 52.0 57.0** **BEIGE BOOK (2:00)** **June 2023:** "Overall economic activity increased slightly since late May. Five Districts reported slight or modest growth, five noted no change, and two reported slight and modest declines."	**UNEMP. CLAIMS (8:30)** **REVISED PRODUCTIVITY & COSTS (8:30)** Productivity / Unit Labor Costs 23-Q1 -1.2% 3.3% 23-Q2 (p) 3.7% 1.6% **23-Q2 (r) 3.2% 1.8%**	**WHOLESALE TRADE (10:00)** Inventories / Sales May -0.4% -0.5% June -0.7% -0.7% **July -0.1% -0.5%** **CONSUMER CREDIT (3:00)** May $9.5 billion June $17.8 billion July --
11	12	13	14	15
	NFIB SMALL BUSINESS OPTIMISM INDEX	**CPI** **FEDERAL BUDGET**	**UNEMP. CLAIMS** **PPI** **RETAIL SALES** **BUSINESS INVENTORIES**	**EMPIRE MFG** **IMPORT/EXPORT PRICES** **IP & CAP-U** **CONSUMER SENTIMENT**
18	19	20	21	22
NAHB HOUSING INDEX **TIC FLOWS**	**HOUSING STARTS** **FOMC MEETING (FIRST DAY)**	**FOMC DECISION**	**UNEMP. CLAIMS** **CURRENT ACCOUNT** **PHILLY FED INDEX** **EXISTING HOME SALES** **LEADING INDICATORS**	

Forecasts in bold. (a) = advance, (p) = preliminary, (r) = revised

Treasury Financing

August/September 2023

Monday	Tuesday	Wednesday	Thursday	Friday
28	29	30	31	1
AUCTION RESULTS: Rate / Cover 13-week bills 5.340% 3.04 26-week bills 5.350% 3.17 2-yr notes 5.024% 2.94 5-yr notes 4.400% 2.54	**AUCTION RESULTS:** Rate / Cover 7-yr notes 4.212% 2.66 42-day CMBs 5.290% 2.81 **ANNOUNCE:** $50 billion 17-week bills for auction on Aug 30 $80 billion 4-week bills for auction on Aug 31 $70 billion 8-week bills for auction on Aug 31 **SETTLE:** $50 billion 17-week bills $80 billion 4-week bills $70 billion 8-week bills	**AUCTION RESULTS:** Rate / Cover 17-week bills 5.330% 3.12	**AUCTION RESULTS:** Rate / Cover 4-week bills 5.280% 2.95 8-week bills 5.290% 2.77 **ANNOUNCE:** $131 billion 13-,26-week bills for auction on Sep 5 $42 billion 52-week bills for auction on Sep 5 $60 billion 42-day CMBs for auction on Sep 5 **SETTLE:** $131 billion 13-,26-week bills $16 billion 20-year bonds $8 billion 30-year TIPS $45 billion 2-year notes $46 billion 5-year notes $36 billion 7-year notes $60 billion 42-day CMBs	
4	5	6	7	8
LABOR DAY	**AUCTION:** $131 billion 13-,26-week bills $42 billion 52-week bills $60 billion 42-day CMBs **ANNOUNCE:** $50 billion* 17-week bills for auction on Sep 6 $80 billion* 4-week bills for auction on Sep 7 $70 billion* 8-week bills for auction on Sep 7 **SETTLE:** $50 billion 17-week bills $80 billion 4-week bills $70 billion 8-week bills	**AUCTION:** $50 billion* 17-week bills	**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $131 billion* 13-,26-week bills for auction on Sep 11 $44 billion* 3-year notes for auction on Sep 11 $35 billion* 10-year notes for auction on Sep 12 $20 billion* 30-year bonds for auction on Sep 13 **SETTLE:** $131 billion 13-,26-week bills $42 billion 52-week bills $60 billion 42-day CMBs	
11	12	13	14	15
AUCTION: $131 billion* 13-,26-week bills $44 billion* 3-year notes	**AUCTION:** $35 billion* 10-year notes **ANNOUNCE:** $50 billion* 17-week bills for auction on Sep 13 $80 billion* 4-week bills for auction on Sep 14 $70 billion* 8-week bills for auction on Sep 14 **SETTLE:** $50 billion* 17-week bills $80 billion* 4-week bills $70 billion* 8-week bills	**AUCTION:** $50 billion* 17-week bills $20 billion* 30-year bonds	**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills **ANNOUNCE:** $131 billion* 13-,26-week bills for auction on Sep 18 $13 billion* 20-year bonds for auction on Sep 19 $15 billion* 10-year TIPS for auction on Sep 21 **SETTLE:** $131 billion* 13-,26-week bills	**SETTLE:** $44 billion* 3-year notes $35 billion* 10-year notes $20 billion* 30-year bonds
18	19	20	21	22
AUCTION: $131 billion* 13-,26-week bills	**AUCTION:** $13 billion* 20-year bonds **ANNOUNCE:** $50 billion* 17-week bills for auction on Sep 20 $80 billion* 4-week bills for auction on Sep 21 $70 billion* 8-week bills for auction on Sep 21 **SETTLE:** $50 billion* 17-week bills $80 billion* 4-week bills $70 billion* 8-week bills	**AUCTION:** $50 billion* 17-week bills	**AUCTION:** $80 billion* 4-week bills $70 billion* 8-week bills $15 billion* 10-year TIPS **ANNOUNCE:** $131 billion* 13-,26-week bills for auction on Sep 25 $48 billion* 2-year notes for auction on Sep 26 $49 billion* 5-year notes for auction on Sep 27 $37 billion* 7-year notes for auction on Sep 28 $24 billion* 2-year FRNs for auction on Sep 27 **SETTLE:** $131 billion* 13-,26-week bills	

**Estimate*