U.S. Economic Comment

- Inflation: continued deceleration in November
- Insights on Q4: solid consumer spending; neutral influence from equipment spending
- The housing market: still in a slump

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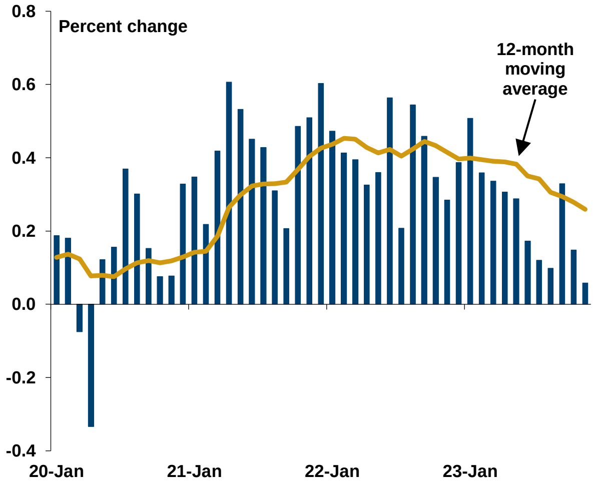
PCE Price Index: On Track for Two Percent

The November reading on the price index for personal consumption expenditures ratified assessments by Fed officials that continued realignment of pandemic-related supply and demand imbalances and constraints on demand exerted by restrictive monetary policy are having a meaningful impact on inflation. The headline PCE price index dipped 0.1 percent (+2.6 percent year-over-year versus 2.9 percent in October), with a drop of 2.7 percent (-6.0 percent year-over-year) in the energy component and a dip of 0.1 percent (+1.8 percent year-over-year) in the food component offsetting a modest increase in the core (+0.1 percent; +3.2 percent year-over-year, down from 3.4 percent in October).

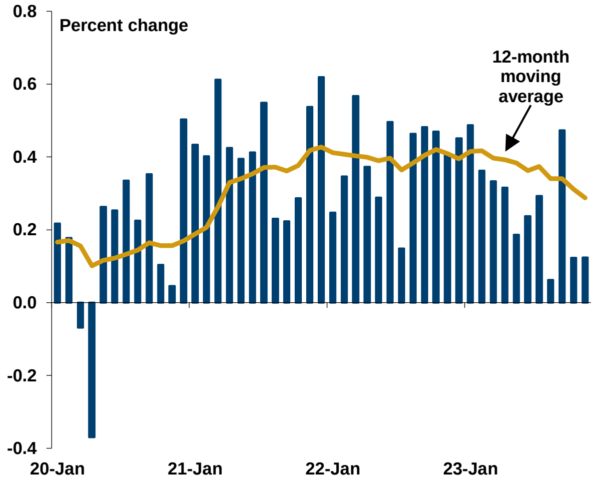
Critically, core inflation is falling back toward target, registering increases of 0.2 percent or less in five of the past six months (chart, below left). Annualized three-month and six-month growth rates of 2.2 percent and 1.9 percent, respectively, suggest that core inflation has made up substantial ground in returning to target. Service inflation excluding energy and housing services, a subset of the broader PCE index monitored closely by Fed officials, has shown similar progress. The index rose 0.1 percent (+3.5 percent year-over-year) in November, the third modest increase in the past four months (chart, below right). Annualized three-month and six-month advances of 2.9 percent and 2.7 percent, respectively, in this area also signify more sustainable inflation. Fed officials may be waiting to declare victory on inflation, but the November PCE data offer additional evidence of a durable return to two percent.

Core PCE Price Index



Source: Bureau of Economic Analysis via Haver Analytics

PCE Price Index: Core Services Ex. Housing*

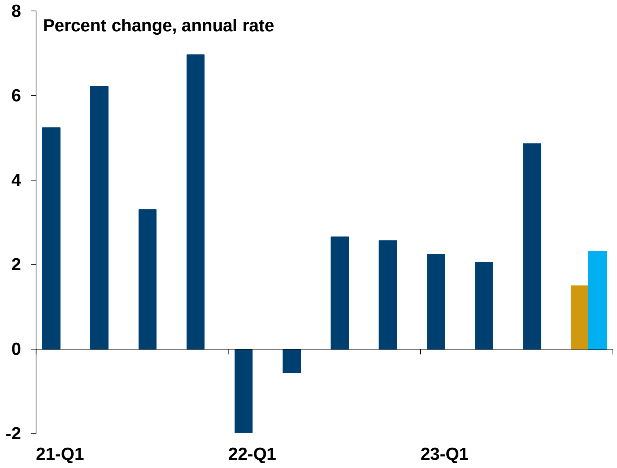


** Service pricing excluding energy and housing services.*
Source: Bureau of Economic Analysis via Haver Analytics

Insights into Q4 GDP

The inflation data grabbed attention this morning, but other information in the pre-holiday data dump offered good insight into Q4 GDP, which our calculations suggest is on track for annualized growth of approximately 1.5 percent while the Atlanta Fed's GDPNow model raises the possibility of an even firmer 2.3 percent (chart, next page, left). Our less aggressive estimate, if realized, would translate to Q4/Q4 growth of 2.7 percent in 2023, a robust performance despite aggressive action by the Federal Reserve.

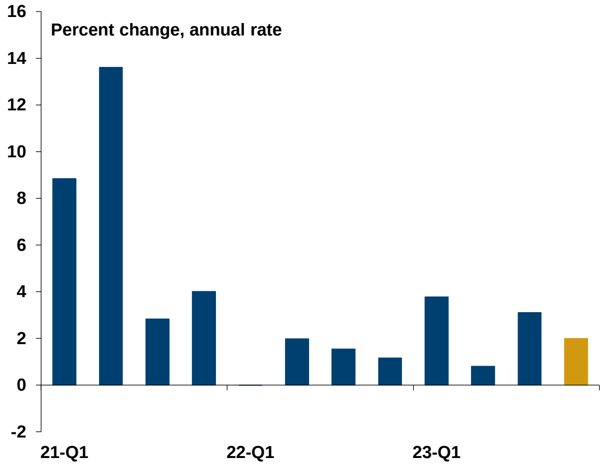
GDP Growth*



** The gold and light blue bars are forecasts of 1.5% and 2.3%, respectively, for 2023-Q4 from DCMA and the Federal Reserve Bank of Atlanta's GDPNow model.*

Sources: Bureau of Economic Analysis via Haver Analytics; Federal Reserve Bank of Atlanta; Daiwa Capital Markets America

Real Consumer Spending Growth*



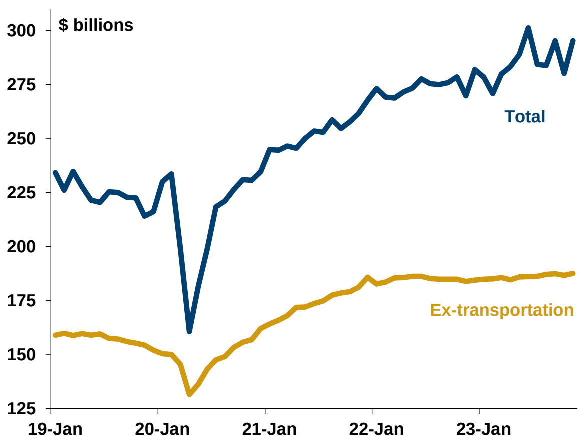
** The gold bar is a forecast of 2.0% for 2023-Q4.*

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

A key driver of growth is growth in Q4 thus far is the resilient U.S. consumer. Consumer spending growth for Q3 was a bit less impressive than initially thought (+3.1 percent, released with yesterday's 3rd estimate of Q3 GDP, versus 3.6 percent previously reported), but data for Q4 currently imply growth of about 2.0 percent—about one percentage point faster than our initial assumption of growth of 1.0 percent (chart, above, right). Real outlays increased only modestly in October (+0.1 percent), but today's report on Personal Income and Consumption from the Commerce Department showed that growth in November was stronger (+0.3 percent). If real spending were to rise only modestly in December, say 0.1 percent, growth for the quarter would exceed 2.0 percent, a solid performance in almost any circumstance.

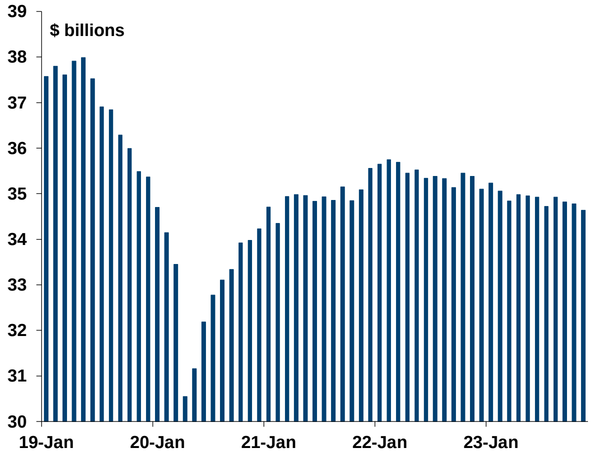
Today's report on durable goods for November, while less impressive than the data on consumer spending, suggested stabilizing equipment spending amid an uncertain outlook into 2024. Headline orders continued to show marked volatility on account of uneven civilian aircraft orders, jumping 5.4 percent after a drop of 5.1 percent in October. However, averaging through the noise shows a flat trend. Orders excluding transportation rose 0.5 percent, augmenting an upward tilt to the series in place since the summer (chart, below left). The subdued bookings pipeline has translated to restrained equipment spending recently, with real activity declining in three of the past four quarters (including an annualized drop of 4.4 percent in Q3). Nominal shipments of nondefense capital goods excluding aircraft declined 0.1 percent in November, and by a larger amount after adjusting for inflation (-0.4 percent).

New Orders for Durable Goods



Source: U.S. Census Bureau via Haver Analytics

New Shipments for Durable Goods*



** Nominal shipments of nondefense capital goods excluding aircraft adjusted by the private capital equipment component of the producer price index.*

Sources: Bureau of Labor Statistics, U.S. Census Bureau via Haver Analytics; Daiwa Capital Markets America

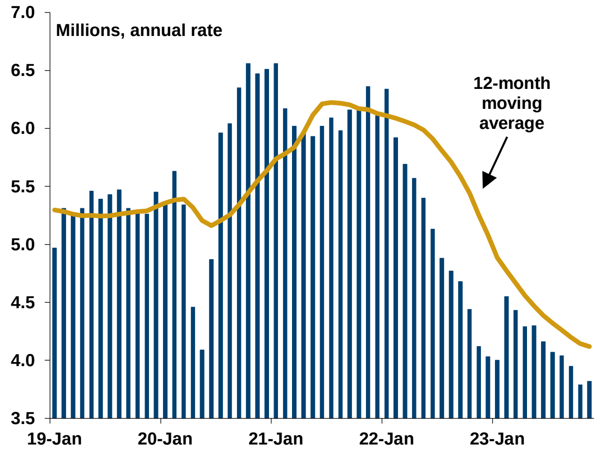
However, the average of real shipments for October/November was little changed from the Q3 average, suggesting a flat performance for Q4 – unimpressive, but a neutral influence on growth versus our initial assumption of a drag in Q4.

Scant Evidence of a Revival in Housing

The recent easing in mortgage interest rates has stirred some chatter about a potential pickup in the housing market, an area of the economy that has experienced a sharp slowdown amid Fed tightening. However, while rates have fallen by over 100 basis points from recent highs in October (7.79 percent for a 30-year loan on October 26 versus 6.49 percent on December 21 according to the Freddie Mac Mortgage Market Survey), formidable challenges to recovery remain. Bank lending standards have tightened significantly in the past year, and new loans could be further curtailed amid an uptick in delinquencies. Moreover, potential homebuyers, already managing strained budgets, face challenging affordability conditions amid still-elevated (although lower) financing costs and high prices.

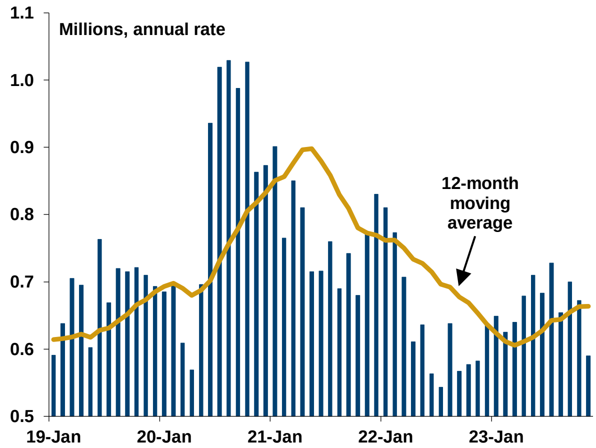
Data on existing and new home sales in November, both released this week, illustrate how difficult conditions for buyers continue to translate to soft sales activity and how a return to a vigorous market is still a ways away. While sales of existing homes this week rose 0.8 percent to 3.82 million, annual rate, the pickup followed four consecutive declines and the pace of activity remains in the vicinity of the record low of 3.45 million in July 2010 (chart, below left). Inventories of existing homes available for sale remain critically tight in many markets, supporting high prices, as many current owners are unwilling to list homes and face the prospect of taking out a new mortgage financed well above the likely below-four-percent rates on their current loans. Sales in the new home market, in contrast, are closer to pre-pandemic norms. However, they have fallen for two consecutive months, including a drop of 12.2 percent in November to 0.590 million, annual rate (chart, below right). Moreover, the builder sentiment index constructed by the National Association of Home Builders and Wells Fargo, suggests that the industry participants assess that the market faces significant challenges. The measure fell to 34 in November from 40 before picking up to 37 in December. For context, readings above 50 indicate favorable views on the market by home builders.

Existing Home Sales



Source: National Association of Realtors via Haver Analytics

New Home Sales



Source: U.S. Census Bureau via Haver Analytics

While conditions are undoubtedly poor, we would highlight two reasons for hope. First, much of the recent decline in mortgage rates occurred in December, and additional easing could be in store as the Fed approaches a pivot to easier monetary policy (which we anticipate beginning in June with a cut of 25 basis points in the federal funds rate). The decline, realized and expected, could pull more potential buyers into the market. Secondly, the inventory situation in the new home portion of the market is radically different than that for existing homes. Builder inventories are heavy, as illustrated by the months' supply of home available for sale of 9.2 (up from 7.9 in October; chart). The current inventory position of builders, elevated from a long-term perspective, could lead to a more favorable pricing environment in the new home market. This too raises the possibility of some recovery in sales at some point in 2024.

Note to readers:

The next U.S. economic comment will be published on January 5, 2024. We wish you a happy holiday season and a healthy New Year!

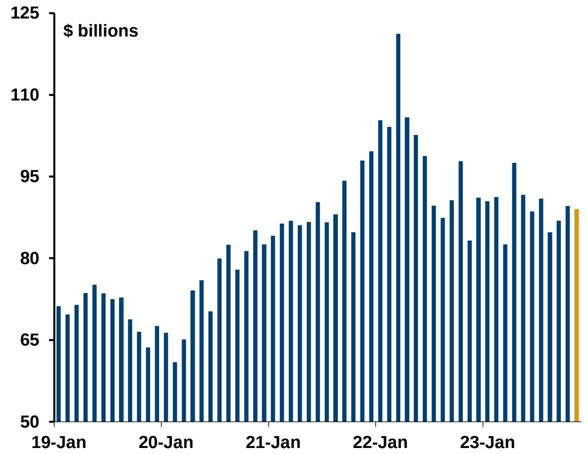
The Week Ahead

U.S. International Trade in Goods (November) (Thursday)

Forecast: -$89.0 Billion ($0.6 Bn. Narrower Deficit)

Lower prices of petroleum products could depress the values of both exports and imports of industrial supplies in November. Outside of the industrial supplies area, exports of consumer goods ex. autos could bounce higher after an aberrant plunge of 9.0 percent in October, as could auto exports which fell 5.8 percent. The projected rebounds in November raise the possibility of a modest narrowing in the monthly trade deficit in goods after a widening of $2.7 billion in the previous month (chart).

Nominal Trade Deficit in Goods*



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

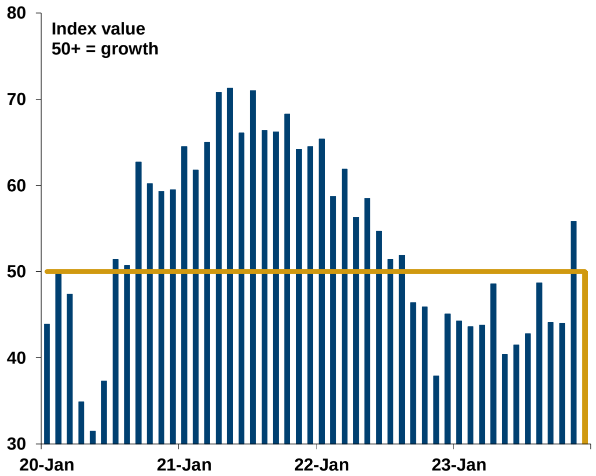
Sources: U.S. Census Bureau via Haver Analytics; Daiwa Capital Markets America

Chicago Purchasing Managers' Index (December) (Friday)

Forecast: Headline 50.0 (-5.8 Index Pts.); Prices 60.0 (+0.1 Index Pt.)

Although many indicators tied to the manufacturing sector (PMIs, regional Fed indexes) are signaling weak activity, the MNI Chicago PMI surged 11.8 index points to 55.8 after sub-50 readings in the 14 months prior. The moves in production (+15.9 index points to 62.4) and new orders (+12.5 index points to 54.7) after averages of 45.8 and 43.1, respectively, in the first 10 months of 2023 raise the distinct possibility of at least partial reversions in December, which would drag the headline lower (but leave it perhaps above the 44.2 average in Jan.-Oct. 2023). Additionally, keep a close eye on the prices measure (not part of the headline composite), which remains elevated, although below readings in the 90's in the second half of 2021 and 80's for much of the first three quarters of 2022 (chart, right).

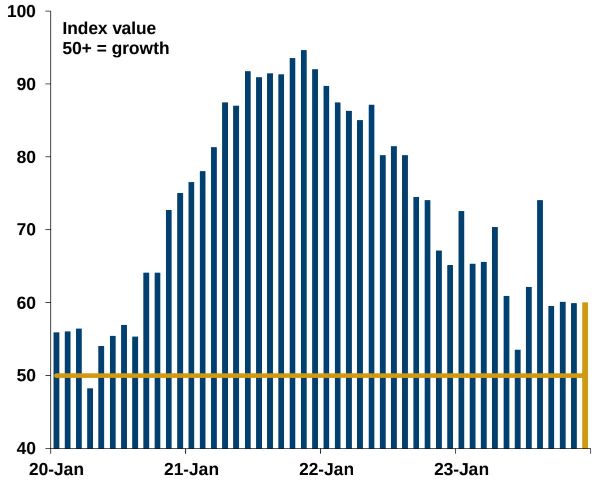
MNI Chicago PMI: Headline Index*



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

Sources: MNI Market News via Haver Analytics; Daiwa Capital Markets America

MNI Chicago PMI: Prices Index*



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

Sources: MNI Market News via Haver Analytics; Daiwa Capital Markets America

Economic Indicators

December 2023 / January 2024

Monday	Tuesday	Wednesday	Thursday	Friday
18	19	20	21	22
NAHB HOUSING INDEX Oct 40 Nov 34 Dec 37	**HOUSING STARTS** Sep 1.356 million Oct 1.359 million Nov 1.560 million **TIC FLOWS** Long-Term / Total Aug $92.6B $161.4B Sep $0.9B -$64.8B Oct $3.3B -$83.8B	**CURRENT ACCOUNT** 23-Q1 -$214.5 bill. 23-Q2 -$216.8 bill. 23-Q3 -$200.3 bill. **EXISTING HOME SALES** Sep 3.950 million Oct 3.790 million Nov 3.820 million **CONFERENCE BOARD CONSUMER CONFIDENCE** Oct 99.1 Nov 101.0 Dec 110.7	**UNEMPLOYMENT CLAIMS** Initial / Continuing (millions) Nov 25 0.219 1.856 Dec 2 0.221 1.866 Dec 9 0.203 1.865 Dec 16 0.205 N/A **REVISED GDP** GDP / Chained Price 23-Q2 2.1% 1.7% 23-Q3 (p) 5.2% 3.6% 23-Q3 (r) 4.9% 3.3% **PHILADELPHIA FED MFG BUSINESS OUTLOOK** Oct -9.0 Nov -5.9 Dec -10.5 **LEADING INDICATORS** Sep -0.8 Oct -1.0% Nov -0.5%	**PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** Inc. / Cons. / Core Sep 0.3% 0.8% 0.3% Oct 0.3% 0.1% 0.1% Nov 0.4% 0.2% 0.1% **DURABLE GOODS ORDERS** Sep 4.0% Oct -5.1% Nov 5.4% **NEW HOME SALES** Sep 0.700 million Oct 0.672 million Nov 0.590 million **REVISED CONSUMER SENTIMENT** Nov 61.3 Dec (p) 69.4 Dec (r) 69.7

Monday	Tuesday	Wednesday	Thursday	Friday
25	26	27	28	29
CHRISTMAS	**CHICAGO FED NATIONAL ACTIVITY INDEX (8:30)** Monthly / 3-Mo. Avg. Sep -0.02 0.00 Oct -0.49 -0.22 Nov -- -- **FHFA HOME PRICE INDEX (9:00)** Aug 0.7% Sep 0.6% Oct -- **S&P CORELOGIC CASE-SHILLER 20-CITY HOME PRICE INDEX (9:00)** Aug 0.8% Sep 0.7% Oct --		**UNEMP. CLAIMS (8:30)** **INTERNATIONAL TRADE IN GOODS (8:30)** Sep -$86.8 billion Oct -$89.6 billion **Nov -$89.0 billion** **ADVANCE INVENTORIES (8:30)** Wholesale / Retail Sep 0.0% 0.4% Oct -0.4% -0.1% Nov -- -- **PENDING HOME SALES (10:00)** Sep 1.0% Oct -1.5% Nov --	**MNI CHICAGO BUSINESS BAROMETER (9:45)** Index / Prices Oct 44.0 60.1 Nov 55.8 59.9 **Dec 50.0 60.0**

Monday	Tuesday	Wednesday	Thursday	Friday
1	2	3	4	5
NEW YEAR'S DAY	**CONSTRUCTION**	**ISM MFG. INDEX** **JOLTS DATA** **FOMC MINUTES** **VEHICLE SALES**	**UNEMP. CLAIMS** **ADP EMPLOYMENT**	**EMPLOYMENT REPORT** **ISM SERVICES INDEX** **FACTORY ORDERS**

Monday	Tuesday	Wednesday	Thursday	Friday
8	9	10	11	12
CONSUMER CREDIT	**NFIB SMALL BUSINESS OPTIMISM INDEX** **TRADE BALANCE**	**WHOLESALE TRADE**	**UNEMP. CLAIMS** **CPI** **FEDERAL BUDGET**	**PPI**

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

Treasury Financing

December 2023 / January 2024

Monday	Tuesday	Wednesday	Thursday	Friday
18	19	20	21	22
AUCTION RESULTS: Rate / Cover 13-week bills 5.260% 2.89 26-week bills 5.130% 3.10	**AUCTION RESULTS:** Rate / Cover 42-day CMBs 5.270% 3.02 **ANNOUNCE:** $56 billion 17-week bills for auction on Dec 20 $80 billion 4-week bills for auction on Dec 21 $80 billion 8-week bills for auction on Dec 21 **SETTLE:** $56 billion 17-week bills $80 billion 4-week bills $80 billion 8-week bills	**AUCTION RESULTS:** Rate / Cover 17-week bills 5.220% 2.99 20-yr bonds 4.213% 2.55	**AUCTION RESULTS:** Rate / Cover 4-week bills 5.265% 2.68 8-week bills 5.270% 2.74 5-yr TIPS 1.710% 2.55 **ANNOUNCE:** $143 billion 13-,26-week bills for auction on Dec 26 $44 billion 52-week bills for auction on Dec 26 $57 billion 2-year notes for auction on Dec 26 $58 billion 5-year notes for auction on Dec 27 $40 billion 7-year notes for auction on Dec 28 $26 billion 2-year FRNs for auction on Dec 27 $70 billion 42-day CMBs for auction on Dec 27 **SETTLE:** $143 billion 13-,26-week bills $70 billion 42-day CMBs	
25	26	27	28	29
CHRISTMAS	**AUCTION:** $143 billion 13-,26-week bills $44 billion 52-week bills $57 billion 2-year notes **ANNOUNCE:** $56 billion* 17-week bills for auction on Dec 27 $80 billion* 4-week bills for auction on Dec 28 $80 billion* 8-week bills for auction on Dec 28 **SETTLE:** $56 billion 17-week bills $80 billion 4-week bills $80 billion 8-week bills	**AUCTION:** $56 billion* 17-week bills $58 billion 5-year notes $26 billion 2-year FRNs $70 billion 42-day CMBs	**AUCTION:** $80 billion* 4-week bills $80 billion* 8-week bills $40 billion 7-year notes **ANNOUNCE:** $143 billion* 13-,26-week bills for auction on Jan 2 **SETTLE:** $143 billion 13-,26-week bills $44 billion 52-week bills $70 billion 42-day CMBs	**SETTLE:** $20 billion 5-year TIPS $26 billion 2-year FRNs
1	2	3	4	5
NEW YEAR'S DAY	**AUCTION:** $143 billion* 13-,26-week bills **ANNOUNCE:** $56 billion* 17-week bills for auction on Jan 3 $80 billion* 4-week bills for auction on Jan 4 $80 billion* 8-week bills for auction on Jan 4 **SETTLE:** $56 billion* 17-week bills $80 billion* 4-week bills $80 billion* 8-week bills $13 billion 20-year bonds $57 billion 2-year notes $58 billion 5-year notes $40 billion 7-year notes	**AUCTION:** $56 billion* 17-week bills	**AUCTION:** $80 billion* 4-week bills $80 billion* 8-week bills **ANNOUNCE:** $143 billion* 13-,26-week bills for auction on Jan 8 $52 billion* 3-year notes for auction on Jan 9 $37 billion* 10-year notes for auction on Jan 10 $21 billion* 30-year bonds for auction on Jan 11 **SETTLE:** $143 billion* 13-,26-week bills	
8	9	10	11	12
AUCTION: $143 billion* 13-,26-week bills	**AUCTION:** $52 billion* 3-year notes **ANNOUNCE:** $56 billion* 17-week bills for auction on Jan 10 $80 billion* 4-week bills for auction on Jan 11 $80 billion* 8-week bills for auction on Jan 11 **SETTLE:** $56 billion* 17-week bills $80 billion* 4-week bills $80 billion* 8-week bills	**AUCTION:** $56 billion* 17-week bills $37 billion* 10-year notes	**AUCTION:** $80 billion* 4-week bills $80 billion* 8-week bills $21 billion* 30-year bonds **ANNOUNCE:** $143 billion* 13-,26-week bills for auction on Jan 16 $13 billion* 20-year bonds for auction on Jan 17 $18 billion* 10-year TIPS for auction on Jan 18 **SETTLE:** $143 billion* 13-,26-week bills	

**Estimate*