Daiwa Capital Markets

U.S. Economic Comment

- June employment: firm headline offset by large downward revisions; unemployment rate ticks higher
- Wage growth: ongoing moderation

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June Employment

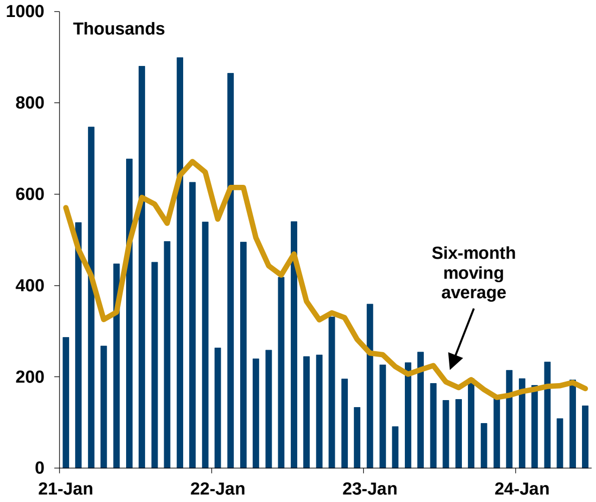
The summary section of the Federal Reserve's semi-annual Monetary Policy Report released earlier today (which comes ahead of Chair Powell's semi-annual Congressional testimony next week) offered a succinct assessment of current conditions in the labor market, although it did not take into account today's employment report: "The balance between labor demand and supply appears similar to that in the period immediately before the pandemic, when the labor market was relatively tight but not overheated." Broadly speaking, the labor market is moderating in response to restrictive monetary policy with conditions aligning to support solid payroll gains and wage growth more consistent with two percent inflation over time. That said, we viewed the employment results for June as offering additional evidence of this softening, and while not immediately problematic, we did observe pockets of weakness in the latest report.

On face, the payroll data for June were firm, with the print of 206,000 exceeding the Bloomberg median expectation of growth of 190,000. Importantly, however, the latest results were joined by downward revisions of 111,000 to results in the prior two months. In one sense, the revisions were inconsequential. Payroll growth in the first half of 2024 averaged 222,000, behind the 289,000 pace in 23-H1 (when the labor market was still hot) but just ahead of the 213,000 average in the second half of last year and still far exceeded average job growth of 166,000 in the aforementioned pre-pandemic period (2019). Even so, we were struck by the size of the latest revisions, and we would direct readers to two instances in the June FOMC minutes (released Wednesday) when Fed staff and FOMC members cast some doubt on the underlying strength of the labor market. Specifically, the Staff Review of the Economic Situation from the Minutes noted, "The recently released fourth-quarter data from the Quarterly Census of Employment and Wages suggested that while the strong reported rate of payroll increases last year may have been overstated, job gains were still solid." Additionally, "several" FOMC members "suggested that the establishment survey may have overstated actual job gains." The excerpts were fairly benign, but if the assessments of labor market conditions therein do correct, they imply that the current stance of monetary policy may be too restrictive and therefore may generate a slowdown in the labor market beyond what is desirable. Moreover, if these revisions were to materialize, it would potentially give credence to the argument for a policy pivot sooner rather than later (particularly in light of recent moderation in inflation).

Beyond concerns stemming from today's revisions and views offered in the June FOMC Minutes, we also would highlight compositional elements of the latest data that bear close watching. Notably, private sector payroll growth in Q2 has softened, twice falling below the average of 179,000 in the six months ended March – 136,000 in the latest month and 108,000 in April (chart, next page, left). Additionally, downward revisions to payrolls in April and May were concentrated in the private sector (86,000 of 111,000) and the distribution of job growth was fairly narrow. Regarding industry breakdown, the healthcare and social assistance area, which is broadly immune to cyclical influences and is driven by requirements of caring for an aging population, recorded an increase of 82,400 in June – a reading essentially in line with the trailing six-month average of 83,200 and accounting for more than 60 percent of private sector job growth. For comparison, average monthly growth in 2019 of 45,000 was approximately 30 percent of private-sector job growth. Other cyclical areas made more substantial contributions to job gains.

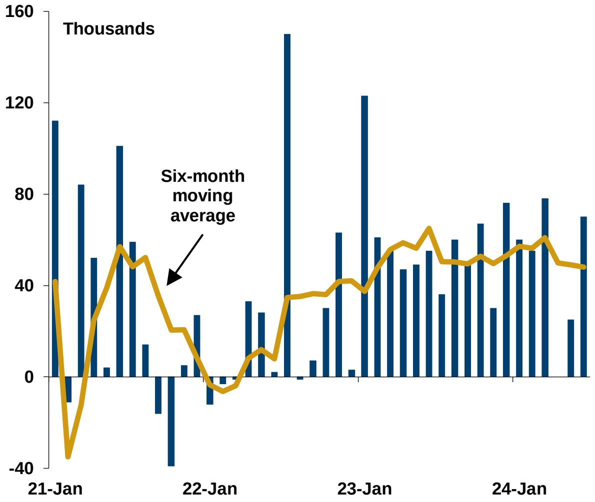
We also are monitoring with interest government-sector job growth, specifically at the state and local levels; on the point, we suspect that ongoing firm hiring has been supported by previously unspent COVID-related funding from the federal government, a source of support that has exerted a counter-cyclical influence and at some point soon may be exhausted. In the latest month, total government payrolls grew by 70,000 (versus a trailing six-month average of 49,000; chart, next page, right), of which 65,000 were hires by state and local governments. For comparison, total government hiring in 2019 averaged 18,000 per month. Again, should government-related hiring normalize, total payroll growth could ease rapidly.

Change in Private Payrolls



Source: Bureau of Labor Statistics via Haver Analytics

Change in Government Payrolls

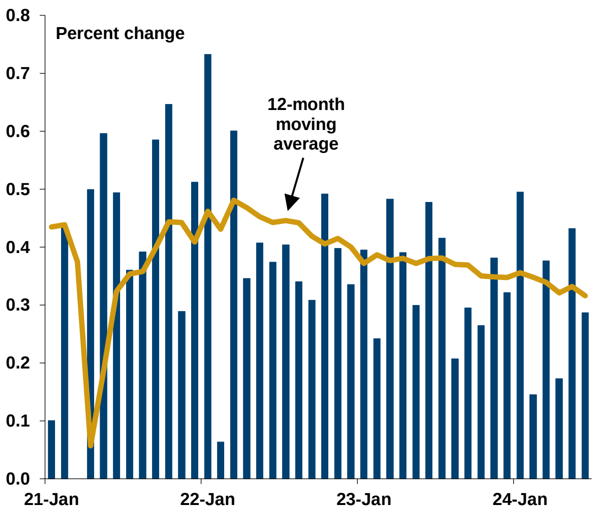


Source: Bureau of Labor Statistics via Haver Analytics

Wage Growth

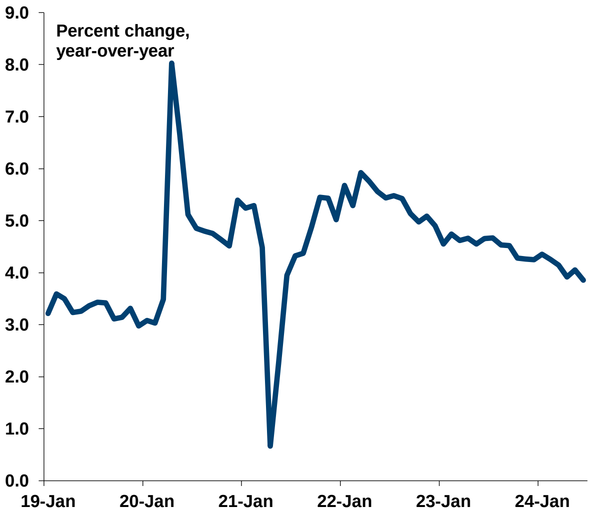
While we do have some concerns about the underlying strength of the labor market, wage growth at least appears to be moderating in an orderly manner, although it is still somewhat faster than that consistent with a sustainable return to two percent inflation. Monthly growth in average hourly earnings in June of 0.3 percent – a reading matching the trailing 12-month average – translated to year-over-year growth of 3.9 percent, 0.2 percentage point slower than the May change (charts, below). The latest year-over-year change, while above the approximately 3.0 percent growth we view as consistent with the Fed's inflation mandate (inflation target plus trend productivity growth of around 1.0 percent), it is well below the recent high of 5.9 percent in March 2022 (a clean reading illustrating unsustainable wage growth generated by tight labor market conditions) and 2020 high of 8.0 percent (which was likely distorted by pandemic-related disruptions). With supply and demand in the labor market coming into better balance, ongoing moderation appears likely. Should labor market conditions soften more rapidly than anticipated, then the deceleration in wage growth would follow suit.

Average Hourly Earnings



Source: Bureau of Labor Statistics via Haver Analytics

Average Hourly Earnings

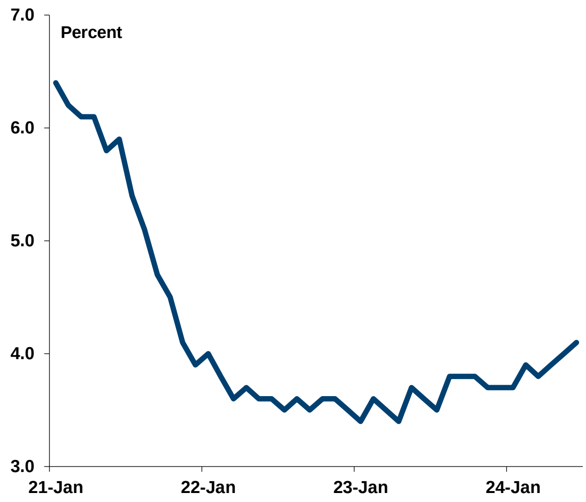


Source: Bureau of Labor Statistics via Haver Analytics

The Unemployment Rate and Ancillary Labor Market Data.

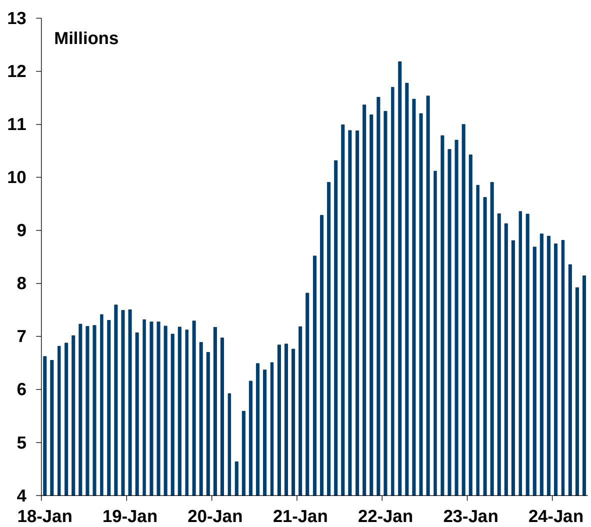
A final labor market related passage from the June FOMC minutes caught our attention, especially in light of the recent upward drift in the unemployment rate (+0.3 percentage point in Q2 to 4.1 percent, including a pickup of 0.1 percentage point in June; chart, right): "Several participants specifically emphasized that with the labor market normalizing, a further weakening of demand may now generate a larger unemployment response than in the recent past when lower demand for labor was felt relatively more through fewer job openings." Previously Fed officials had broadly argued that declines in demand would unfold as reduced job vacancies, which largely transpired as openings fell from a record 12.2 million in March 2022 to 7.9 million in April before rising to 8.1 million in May (reported in the JOLTS data on Tuesday; chart, below left). Now, as openings have leveled closer to pre-pandemic levels, unemployment claims (and the jobless rate) have moved higher. Initial claims for unemployment insurance held in the low-200k range from the fall of 2023 through April (which either matched or fell below the 2019 average of 218,000), but they have deteriorated more recently, including the latest weekly reading of 238,000 (off marginally from the recent high of 243,000 in the week ended June 8; chart, below right). Correspondingly, continued unemployment claims have risen for nine consecutive weeks from a recent low of 1.768 million in late April to 1.858 million as of June 22. Again, the shifts don't necessarily portend a rapid further increase in the unemployment rate and broader deterioration in the labor market, but they do underscore the point that, "with the risks to the Committee's dual-mandate goals having now come into better balance, labor market conditions would need careful monitoring." (For further reading on the referenced reports, please see: "Monetary Policy Report," Federal Reserve Board, July 5, 2024. https://www.federalreserve.gov/monetarypolicy/files/20240705_mprfullreport.pdf; "Minutes of the Federal Open Market Committee, June 11-12, 2024" Federal Reserve Board, July 3, 2024. https://www.federalreserve.gov/monetarypolicy/fomcminutes20240612.htm)

Civilian Unemployment Rate



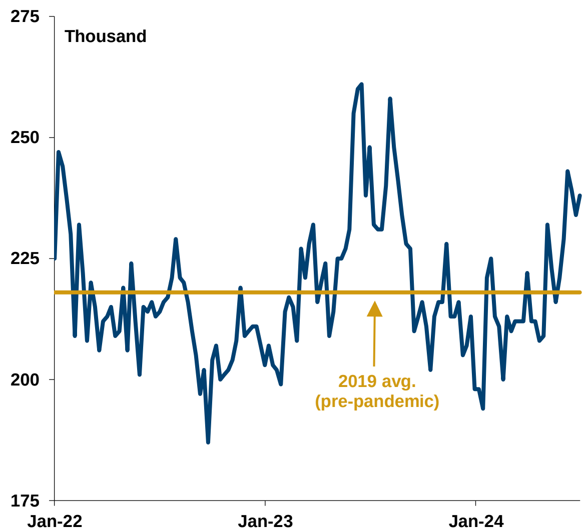
Source: Bureau of Labor Statistics via Haver Analytics

Job Openings



Source: Bureau of Labor Statistics via Haver Analytics

Initial Claims for Unemployment Insurance



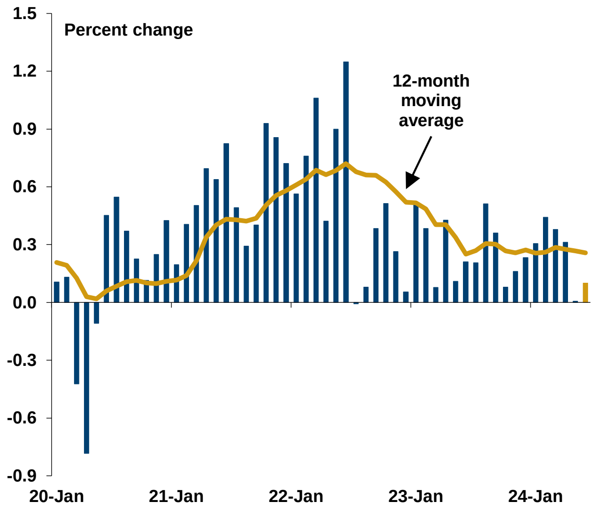
Source: U.S. Department of Labor via Haver Analytics

The Week Ahead

CPI (June) (Thursday)
Forecast: 0.1% Headline, 0.2% Core

Available quotes on the prices of energy commodities for June raise the possibility of a second consecutive sizable decline in the energy component of the CPI. Additionally, increases in the food component appear to be slowing further in 2024 from a moderate pace of gains in the prior year (average monthly advance of 0.1 percent per month in 2024 thus far versus 0.2 percent in 2023). In the core component, prices of goods remain contained (average monthly decline of 0.1 percent in the past 12 months), although core service prices are still inconsistent with two percent inflation (+0.4 percent, on average, in the past 12 months). Part of the pressure in core services reflects ongoing firm increases in rents and owners' equivalent rent of residences, but advances excluding housing also have been brisk (+0.4 percent per month, on average, in the past 12 months, although this area declined modestly in May: -0.04 percent, rounding up to no change).

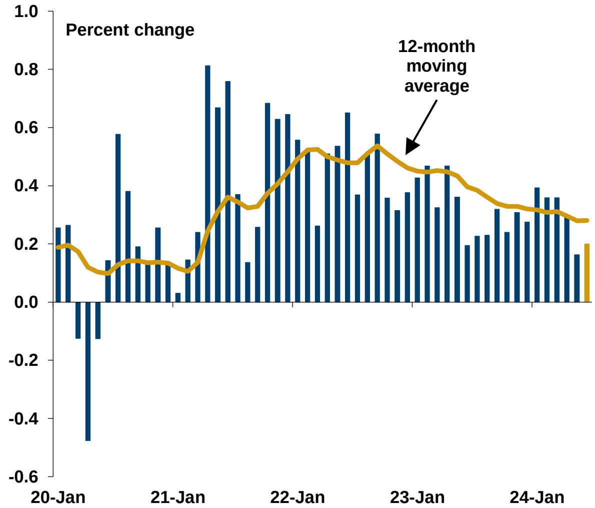
Headline CPI*



** The gold bar is a forecast for June 2024.*

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

Core CPI*



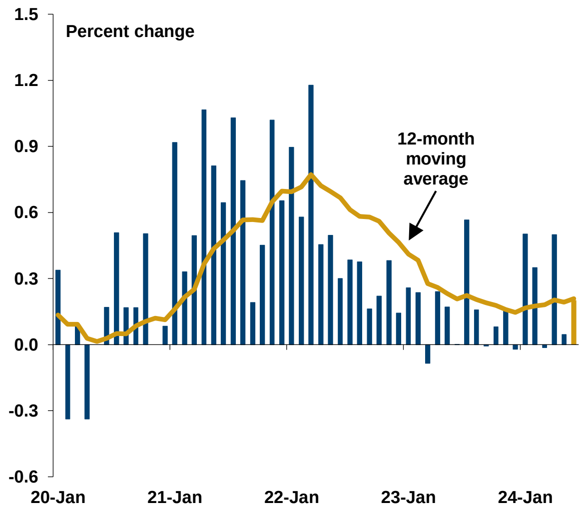
** The gold bar is a forecast for June 2024.*

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

PPI (June) (Friday)
Forecast: 0.1% Final Demand, 0.2% Ex. Food & Energy

Wholesale energy prices could fall for a second consecutive month in June after a prior drop of 4.8 percent. Moreover, food prices are likely to remain on a subdued trajectory amid wide swings (range of -0.6 percent to +1.0 percent in the past 12 months; monthly average of +0.1 percent). Goods prices excluding food and energy have increased 0.1 percent per month, on average, in the past 12 months, while service prices have advanced at a slightly faster pace (+0.2 percent per month). Construction costs have been contained, declining 0.1 percent per month on average over the past year.

PPI Ex. Food & Energy*



** The gold bar is a forecast for June 2024.*

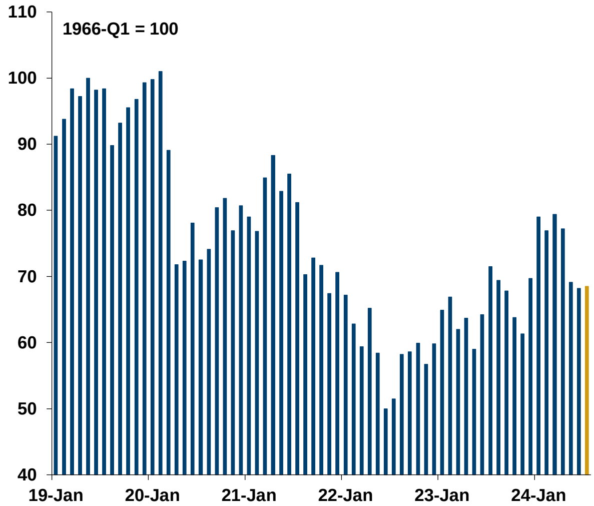
Sources: Bureau of Labor Statistics via Haver Analytics; Daiwa Capital Markets America

Consumer Sentiment (July) (Friday)
Forecast: 68.5 (+0.3 Index Pt. or +0.4%)

Consumer views on inflation appear to be improving, which all else equal could boost sentiment. Still, signs of softening labor market conditions (a recent uptick in unemployment claims) and strained household budgets (increased loan delinquency rates) could provide an offset and leave the University of Michigan sentiment gauge range-bound in early July (chart, below left).

With regard to inflation expectations, the year-ahead measure eased 0.3 percentage point in June to 3.0 percent – a reading in the lower end of the range of the current expansion (chart, below right). Correspondingly, the longer-term measure remained at that level for the third consecutive month; although it is up from recent lows, Fed officials still view longer-term inflation expectations as anchored. We suggest monitoring these measures closely when the early July report is published next week.

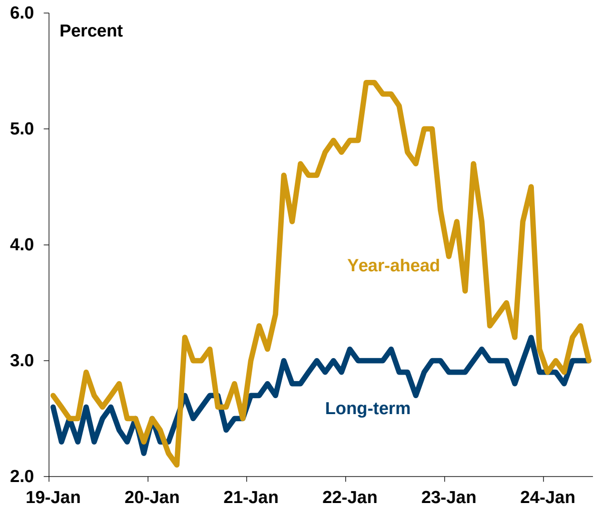
Consumer Sentiment*



** The gold bar is a forecast for July 2024.*

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

Consumer Inflation Expectations



Source: University of Michigan via Haver Analytics

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Economic Indicators

July 2024

Monday	Tuesday	Wednesday	Thursday	Friday
1	2	3	4	5
ISM MFG. INDEX Index Prices Apr 49.2 60.9 May 48.7 57.0 June 48.5 52.1 **CONSTRUCTION** Mar 0.1% Apr 0.3% May -0.1%	**JOLTS DATA** Openings (000) Quit Rate Mar 8,355 2.2% Apr 7,919 2.2% May 8,140 2.2% **VEHICLE SALES** Apr 15.8 million May 15.9 million June 15.3 million	**ADP EMPLOYMENT** Private Payrolls Apr 188,000 May 157,000 June 150,000 **UNEMPLOYMENT CLAIMS** Initial Continuing (millions) June 8 0.243 1.821 June 15 0.239 1.832 June 22 0.234 1.858 June 29 0.238 N/A **TRADE BALANCE** Mar -$68.6 billion Apr -$74.5 billion May -$75.1 billion **ISM SERVICES INDEX** Index Prices Apr 49.4 59.2 May 53.8 58.1 June 48.8 56.3 **FACTORY ORDERS** Mar 0.7% Apr 0.4% May -0.5% **FOMC MINUTES**	***INDEPENDENCE DAY***	**EMPLOYMENT REPORT** Payrolls Un. Rate Apr 108,000 3.9% May 218,000 4.0% June 206,000 4.1%
8	9	10	11	12
CONSUMER CREDIT (3:00) Mar -$1.1 billion Apr $6.4 billion May --	**NFIB SMALL BUSINESS OPTIMISM INDEX (6:00)** Apr 89.7 May 90.5 June -- **POWELL MONETARY POLICY TESTIMONY (SENATE) (10:00)**	**WHOLESALE TRADE (10:00)** Inventories Sales Mar -0.5% -1.3% Apr 0.2% 0.1% **May 0.6% 0.3%** **POWELL MONETARY POLICY TESTIMONY (HOUSE) (10:00)**	**UNEMP. CLAIMS (8:30)** **CPI (8:30)** Total Core Apr 0.3% 0.3% May 0.0% 0.2% **June 0.1% 0.2%** **FEDERAL BUDGET (2:00)** 2024 2023 Apr $209.5B $176.2B May -$347.1B -$240.3B **June -$25.0B** -$227.8B	**PPI (8:30)** Final Demand Ex. Food & Energy Apr 0.5% 0.5% May -0.2% 0.0% **June 0.1% 0.2%** **CONSUMER SENTIMENT (10:00)** May 69.1 June 68.2 **July 68.5**
15	16	17	18	19
EMPIRE MFG	**RETAIL SALES** **IMPORT/EXPORT PRICES** **NAHB HOUSING INDEX** **BUSINESS INVENTORIES**	**HOUSING STARTS** **IP & CAP-U** **BEIGE BOOK**	**UNEMP. CLAIMS** **PHILLY FED INDEX** **LEADING INDICATORS** **TIC FLOWS**	
22	23	24	25	26
CHICAGO FED NATIONAL ACTIVITY INDEX	**EXISTING HOME SALES**	**INTERNATIONAL TRADE IN GOODS** **ADVANCE INVENTORIES** **NEW HOME SALES**	**UNEMP. CLAIMS** **Q2 GDP** **DURABLE GOODS ORDERS**	**PERSONAL INCOME, CONSUMPTION, AND PCE PRICE INDEX** **REVISED CONSUMER SENTIMENT**

Forecasts in bold.

Treasury Financing

July 2024

Monday	Tuesday	Wednesday	Thursday	Friday
1	2	3	4	5
AUCTION RESULTS: Rate Cover 13-week bills 5.240% 2.76 26-week bills 5.115% 2.99 **SETTLE:** $13 billion 20-year bonds $69 billion 2-year notes $70 billion 5-year notes $44 billion 7-year notes	**AUCTION RESULTS:** Rate Cover 41 day CMBs 5.270% 3.13 **ANNOUNCE:** $60 billion 17-week bills for auction on July 3 $85 billion 4-week bills for auction on July 3 $80 billion 8-week bills for auction on July 3 **SETTLE:** $60 billion 17-week bills $80 billion 4-week bills $75 billion 8-week bills	**AUCTION RESULTS:** Rate Cover 17-week bills 5.205% 3.15 4-week bills 5.280% 2.81 8-week bills 5.275% 2.76 **ANNOUNCE:** $146 billion 13-,26-week bills for auction on July 8 $46 billion 52-week bills for auction on July 9 $58 billion 3-year notes for auction on July 9 $39 billion 10-year notes for auction on July 10 $22 billion 30-year bonds for auction on July 11 $70 billion 42-day CMBs for auction on July 9	***INDEPENDENCE DAY***	**SETTLE:** $143 billion 13-,26-week bills $65 billion 41-day CMBs
8	9	10	11	12
AUCTION: $146 billion 13-,26-week bills	**AUCTION:** $46 billion 52-week bills $58 billion 3-year notes $70 billion 42-day CMBs **ANNOUNCE:** $60 billion* 17-week bills for auction on July 10 $85 billion* 4-week bills for auction on July 11 $80 billion* 8-week bills for auction on July 11 **SETTLE:** $60 billion 17-week bills $85 billion 4-week bills $80 billion 8-week bills	**AUCTION:** $60 billion* 17-week bills $39 billion 10-year notes	**AUCTION:** $85 billion* 4-week bills $80 billion* 8-week bills $22 billion 30-year bonds **ANNOUNCE:** $146 billion* 13-,26-week bills for auction on July 15 $13 billion* 20-year bonds for auction on July 17 $19 billion* 10-year TIPS for auction on July 18 **SETTLE:** $146 billion 13-,26-week bills $46 billion 52-week bills $70 billion 42-day CMBs	
15	16	17	18	19
AUCTION: $146 billion* 13-,26-week bills **SETTLE:** $58 billion 3-year notes $39 billion 10-year notes $22 billion 30-year bonds	**ANNOUNCE:** $60 billion* 17-week bills for auction on July 17 $85 billion* 4-week bills for auction on July 18 $80 billion* 8-week bills for auction on July 18 **SETTLE:** $60 billion* 17-week bills $85 billion* 4-week bills $80 billion* 8-week bills	**AUCTION:** $60 billion* 17-week bills $13 billion* 20-year bonds	**AUCTION:** $85 billion* 4-week bills $80 billion* 8-week bills $19 billion* 10-year TIPS **ANNOUNCE:** $146 billion* 13-,26-week bills for auction on July 22 $69 billion* 2-year notes for auction on July 23 $70 billion* 5-year notes for auction on July 24 $44 billion* 7-year notes for auction on July 25 $30 billion* 2-year FRNs for auction on July 24 **SETTLE:** $146 billion* 13-,26-week bills	
22	23	24	25	26
AUCTION: $146 billion* 13-,26-week bills	**AUCTION:** $69 billion* 2-year notes **ANNOUNCE:** $60 billion* 17-week bills for auction on July 24 $85 billion* 4-week bills for auction on July 25 $80 billion* 8-week bills for auction on July 25 **SETTLE:** $60 billion* 17-week bills $85 billion* 4-week bills $80 billion* 8-week bills	**AUCTION:** $60 billion* 17-week bills $70 billion* 5-year notes $30 billion* 2-year FRNs	**AUCTION:** $85 billion* 4-week bills $80 billion* 8-week bills $44 billion* 7-year notes **ANNOUNCE:** $146 billion* 13-,26-week bills for auction on July 29 **SETTLE:** $146 billion* 13-,26-week bills	

**Estimate*