Economic data tracker – Cooler labor trends support Fed hold

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Week 35 – September 1, 2023

Trend watch and what's new this week

First, our hearts are with those dealing with the aftermath of Hurricane Idalia, which barreled through the southeast. It has only just begun to ripple through the activity-based data (slides 5 and 6). For instance, dining reservations plunged in Florida (-24% compared to 2022 levels), South Carolina (-37%), Georgia (-17%), and North Carolina (-15%). Idalia will continue to cycle through the data first as evacuations but then as clean up and repair efforts ramp up over the coming weeks.

Job growth cooled in August, unemployment rate jumped

U.S. payrolls in August added 187,000 jobs, just ahead of the consensus expectations of 170,000. Two of the major industry groups – information and mining & logging – slashed payrolls during August (slide 7). Also, the unemployment rate jumped to 3.8% in August. That's up 0.4 percentage points from the cycle low of 3.4%. More importantly, it is just shy of an increase of 0.5 percentage points, which is widely regarded as a recession flag.

That was coupled with sizable downward revisions to the prior two months, knocking the six-month average down to 194,000 from 222,500 (slide 8). It was accompanied by further signs of cooling, including a dramatic cooling of wage gains (slide 9). These are corroborated by other labor figures, such as the stepdown in job openings and the quit rate, and a spike in job cut announcements. The lone outlier is weekly jobless claims, which haven't budged.

Supplementary labor data mixed, but above prior levels

On slide 10, the number of job openings dropped 3.7% in July to 8.8 million, the 11th decline in the past 16 months. Hiring fell 2.8% to 5.8 million. Openings and hiring remain above pre-pandemic levels. Meanwhile, the so-called quit rate – officially known as the percentage of employees voluntarily quitting – slipped to 2.3% from 2.6% in May, and down from the cycle peak of 3% in 2022. It is now in-line with the pre-pandemic level.

The Fed's favorite gauge showed inflation remains sticky

On slide 11, the Fed's favorite inflation gauge—the price index of core personal consumption expenditures (core PCE)—rose 0.2% in July and increased 4.2% from a year ago. It's moving in the right direction and is down from its March '22 high of 5.4%. Ultimately, inflation remains uncomfortably high and well above the Fed's 2% target, and likely contributes to the case for the Fed to pause but not stop rate hikes.

Revisions to business inventories lower 2Q growth

On slide 12, real GDP growth in the second quarter was revised downward to 2.1% on an annualized basis from the initially reported 2.4% pace. The biggest contributor in the second quarter was consumer spending followed by business spending. However, there were downward revisions to business inventories, business spending, and net exports.

Economic commentary – Our take and the bottom line

Our take

On its face, August was another solid jobs report – marked by job growth above the long-term average, an unemployment rate significantly below 5%, and wage growth still well-above the pre-pandemic trend. But within the broader context of the past few years, it showed a deceleration almost across the board.

Additionally, the revisions were significant; most notably, June's job growth was lowered to 105,000, which is essentially stall speed. That's barely enough to keep such a large economy afloat and the unemployment rate stable. A 100,000 per month is the economic equivalent of the Mendoza line, a baseball term for when a major league player is typically sent down to the minors or released for having such a poor batting average. Furthermore, it's a danger zone for job growth, whereby outright job losses have often happened historically after crossing below 100,000.

These cooling trends were corroborated by other labor figures, such as the stepdown in job openings and the quit rate, and a spike in job cut announcements. In fact, the decline in the quit rate signals that the so-called "Great Resignation" appears to be over. The lone outlier is weekly jobless claims, which haven't budged.

As we mentioned last month, a so-called soft landing of the U.S. economy does appear possible. Yet, it also undercuts the soft-landing thesis – that the economy is resilient enough to avoid a recession, especially with the jump in the unemployment rate and headline job growth dipping near the Mendoza line. Naturally, some might say, "yes, June job growth slowed but it reaccelerated in July and August." To which our reply is – July and August haven't been revised yet. Lest we forget, June was quite literally cut in half to 105,000 from the originally reported 209,000. Again, most recessions initially look like a soft landing with very few exceptions (like 2020). The economic data cools and conditions look fairly stable until they don't.

It would be unprecedented to avoid a recession with weakening leading indicators, higher interest rates, and tighter financial and credit conditions. Many of the leading indicators are pointing downward and have been for more than a year. Moreover, most of the incoming economic data has been decelerating, not strengthening. That said, we don't anticipate a sudden collapse in economic activity and don't view the economy as overly weak. Regardless, it's certainly not as strong as many of the soft-landing bulls are projecting.

Ultimately, we believe labor market conditions have cooled enough to allow the Fed to continue holding rates steady in September, letting them assess the overall economy. While it's clearly cooler than the blistering pace of 2021 and 2022, inflation remains well above anyone's comfort level. At the very least, the Fed will need to maintain rates, though it's still possible additional rate hikes will be needed to curb inflation if price trends don't cooperate.

Bottom line

A shallow recession remains our base case as dramatically higher interest rates and tighter credit conditions ratchet up stress on consumers and businesses going forward. This now includes restarting student loan payments later this year as a result of the recent federal debt deal. We also believe that the Fed will keep interest rates higher for longer. Yet, a recession isn't inevitable and the timing remains fluid.

Econ-at-a-Glance

	Economic indicator	Trend	Last	Next – consensus	Comments
Overall	Gross domestic product (GDP)	▲	2Q P: 2.1%	2Q F: 2.1%	Missed the consensus of 2.4%. The biggest detractors were downward revisions to business inventories, business spending, and net exports. Government and consumer spending were revised up.
Jobs	Unemployment rate[x]	▲	Aug: 3.8%	Sep: N/A	Jumped to the highest level since February ’22.
	Monthly jobs (nonfarm)	▲	Aug: 187K	Sep: N/A	Just ahead of the consensus (170,000), but was coupled with sizable downward revisions to the prior two months, knocking the six-month average down to 194,000 from 222,500.
	Weekly jobless claims[+]	▲	8/26: 228K	9/2: 234K	Dropped 4.0% WoW, which was the sixth decline in eight weeks.
	Nonfarm productivity	⇆	2Q A: 3.7%	2Q F: 3.4%	It was the fastest productivity increase in 11 quarters, dating back to 3Q20, while unit labor costs cooled to 1.6% from 3.3% in 1Q23.
Interest rates	Federal funds rate	▼	5.25% – 5.50%	9/20: 5.25% – 5.50%	Given weakening data and cooler wages, markets now expect a pause in September, but less clarity for the rest of 2023.
	10-year U.S. Treasury yield	▼	4.16%‡	Flat	Big rate swings in the past two weeks, being pushed around by inflation and jobs data, while investors price in “higher for longer” from the Fed. We expect more volatility.
	10-year AAA GO muni yield	▼	2.87%‡	Flat	Ticked lower WoW but still near the highest level since November ’22.
	30-year fixed mortgage rate	▼	7.53%‡	Flat/down	It slipped modestly WoW but remains near the highest level since October ’00. Higher rates hurt housing affordability.
Inflation	Consumer prices (CPI)[x]	▼	Jul: 0.2%	Aug: 0.5%	The YoY pace ticked higher to 3.2% but is down from 5.0% in March.
	Core CPI	▼	Jul: 0.2%	Aug: 0.2%	Up 4.7% YoY, cooling for the fourth consecutive month.
	Producer prices (PPI)	⇆	Jul: 0.3%	Aug: 0.4%	The YoY pace jumped 0.8% after dropping to 0.2% in June.
	Core PPI	⇆	Jul: 0.3%	Aug: 0.2%	Rose at its fastest pace in 8 months as services reaccelerated.

▲Good ▼ Bad ⇆ Neutral [+]Leading indicator [x]Lagging indicator ‡Intraday quote Bloomberg consensus shown

Econ-at-a-Glance

	Economic indicator	Trend	Last	Next – consensus	Comments
Housing	Existing home sales	▼	Jul: 4.07M	Aug: N/A	Dropped 2.2% in July and down for the 17th time in 18 months.
	New home sales	▲	Jul: 714K	Aug: N/A	Jumped 4.4% MoM, while price rose 4.8% to $436,700.
	New housing starts	⇆	Jul: 1.452M	Aug: N/A	Rebounded 3.9% MoM, as single-family starts surged 6.7%.
	New permits⁺	⇆	Jul: 1.443M	Aug: N/A	Edged up 0.1% MoM, while single-family permits rose 0.6%.
Business	Durable goods orders⁺	▲	Jul P: -5.2%	Jul F: -5.2%	Aircraft orders declined after a massive 71% spike in June. Core capital goods orders (ex-air & defense) edged up 0.1% MoM.
	ISM Manufacturing Index	▼	Aug: 47.0	Sep: N/A	Activity contracted for the 10th month in a row. Employment contracted for the third-straight month.
	ISM Services Index	▲	Jul: 52.7	Aug: 52.5	Expanded for the sixth month in a row after briefly contracting in December. The prices paid component rose to a three-month high.
	Business inventories^X	▲	Jun: 0.0%	Jul: 0.1%	Flat in each of the past two months (May and June).
Consumer	Personal income	▲	Jul: 0.2%	Aug: N/A	Missed the consensus and matched the smallest rise in 9 months.
	Personal spending	▲	Jul: 0.8%	Aug: N/A	Better than expected and June was revised upward.
	Retail & food sales	▲	Jul: 0.7%	Aug: 0.2%	It just hit a fresh all-time high, surpassing the January ’23 level.
	Consumer sentiment	▲	Aug F: 69.5	Sep P: 69.8	Edged lower after hitting a 21-month high in July, while one-year inflation expectations rose to 3.5%, a three-month high.

▲Good ▼ Bad ⇆ Neutral ⁺Leading indicator ^{X}Lagging indicator ‡Intraday quote Bloomberg consensus shown

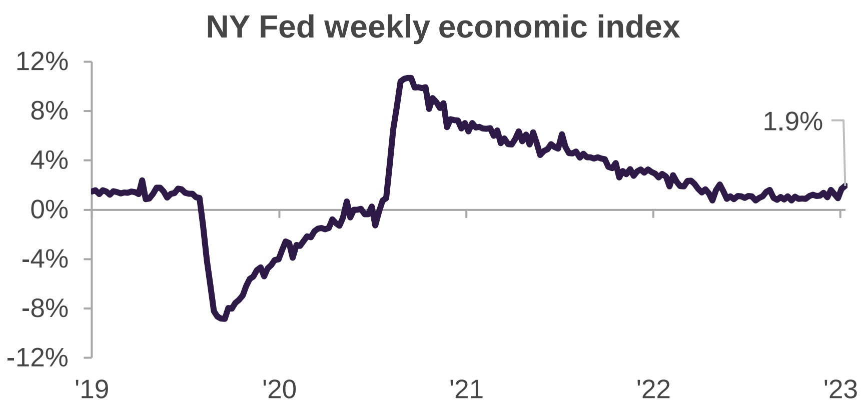
U.S. activity-based data matrix

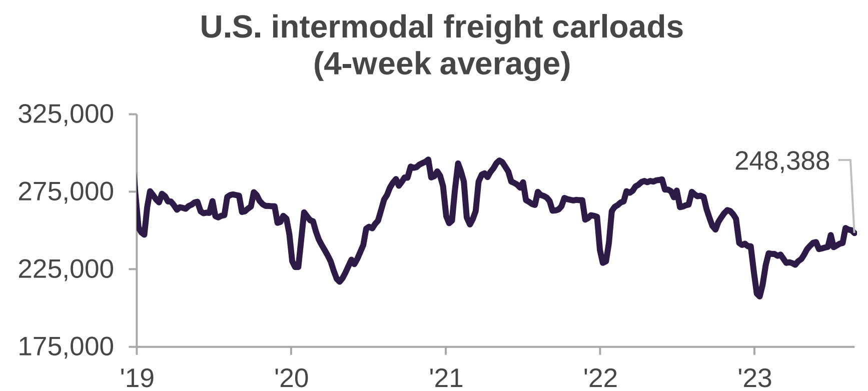
Indicator	Relative trend	What we're watching
Back to office	⇆	Held steady at 47.2 for a second straight week (pre-pandemic indexed to 100). Top cities were Houston (61), Austin (58), and Dallas (54); bottom were San Jose (39) and Philadelphia (40). The trend is steadily improving and is now about half of pre-pandemic levels, which is a modest positive for overall growth.
TSA air passenger throughput	▲	Weekly counts dropped 4.1% WoW, down for a 7th straight week, to 15.9 million. It is up 2.5% from the same week in August '19 and 9.5% above August '22. Year to date is up 0.1% compared to the same period in 2019.
OpenTable restaurant bookings	⇆	Dipped to -6.0% from -4.7% last week (compared to 2022 levels). Top positive states were led by Nebraska (+10%) and Missouri (+6%); bottom were Florida (-24%), South Carolina (-37%), Georgia (-17%), and North Carolina (-15%) due to Hurricane Idalia. Top cities were Kansas City and Minneapolis (both +29%); bottom were Tampa (-69%), Orlando (-25%), and Boca Raton (-19%).
Hotel occupancy	▲	Fell to 65.0%, the fifth straight WoW decline. The average daily rate fell WoW to $150.47, up 2.0% from the same week in '22, and revenue per available room also fell WoW to $106.89, up 2.0% from Aug. '22.
Freight (rail/truck/ship)	▼	Rail traffic fell 1.3% WoW and dropped 2.8% MoM in August and traffic is -11% YoY. Container traffic in July rose 3.5% at 5 of the top U.S. ports (LB, SAV, SEATAC, HOU, CHS), but is -18% YoY. The Cass Freight Index fell 1.2% in July, the 9th decline in 11 months.
Staffing index	⇆	Slipped to 101.0 from 101.9 in the prior week, which was the highest level since February. The '19 average was 94.2. The pre-pandemic all-time high was 105.8, set in Dec. '14. The cycle low was 59.6, set in April '20.
Apartment rental prices	▲	Rent index increased 0.5% MoM in July and rose 3.6% YoY, which is below the annual average of 5.7% since 2015. The rental growth rate clearly peaked during the second half of 2021.

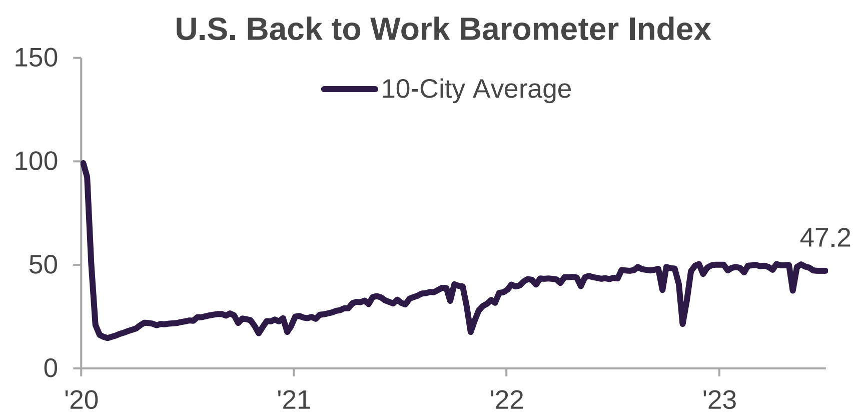
Trend relative to whether it is favorable for economic growth:
▲Positive ▼Negative ⇆Neutral / Mixed

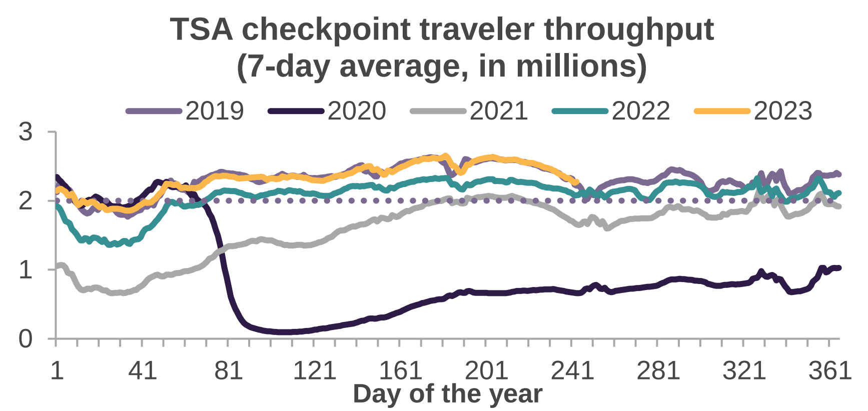
Data source: Truist IAG, Bloomberg, Kastle Back to Work Barometer, Transportation Security Administration, OpenTable, STR/CoStar, American Staffing Association, Zillow. Week-over-week and year-over-year change are abbreviated as WoW and YoY, respectively.

Activity-based trends slipped to start 2023, but firming through late August







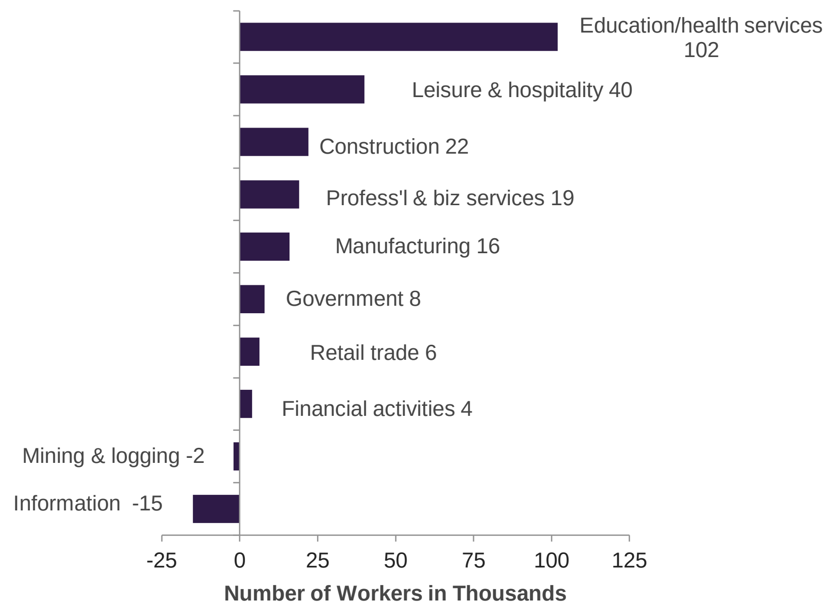


Data source: Truist IAG and the following additional sources respectively: Top left: Bloomberg, NY Federal Reserve Weekly Economic Index through August 26, 2023. Top right: (U.S. intermodal freight carloads) Bloomberg, Association of American Railroads Intermodal Trailers U.S. Freight Carloads, 4-week average through August 25. Bottom left: Bloomberg, Kastle Systems averaged weekly through August 23. Bottom right: Bloomberg, Transportation Security Administration (TSA) 7-day average through August 31.

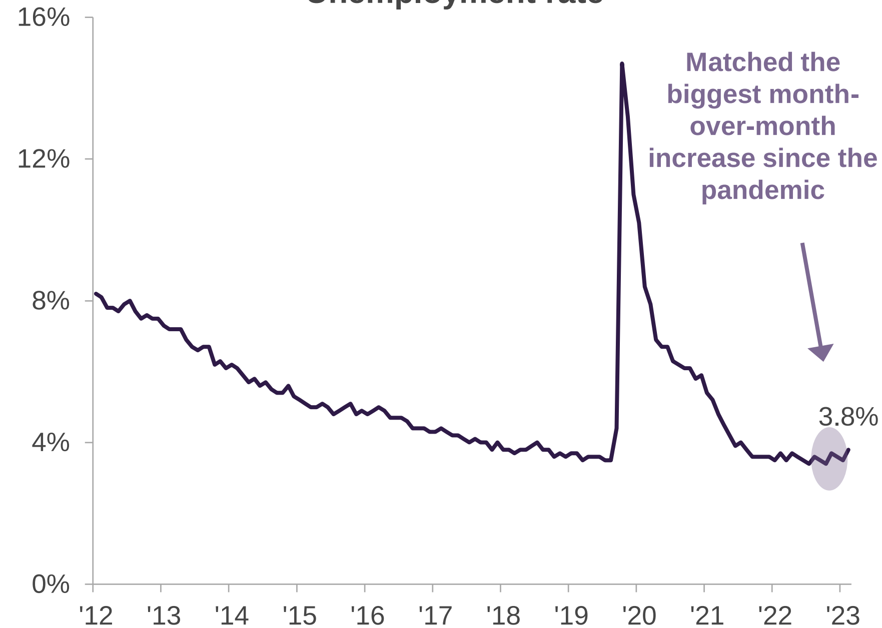
Job growth remained solid in August, but clearly cooling

U.S. payrolls in August added 187,000 jobs, just ahead of the consensus expectations of 170,000. Two of the major industry groups – information and mining & logging – slashed payrolls during August. Also, the unemployment rate jumped to 3.8% in August. That's up 0.4 percentage points from the cycle low of 3.4%. More importantly, it is just shy of an increase of 0.5 percentage points, which is widely regarded as a recession flag.

Monthly change by major industry group (in thousands)



Unemployment rate



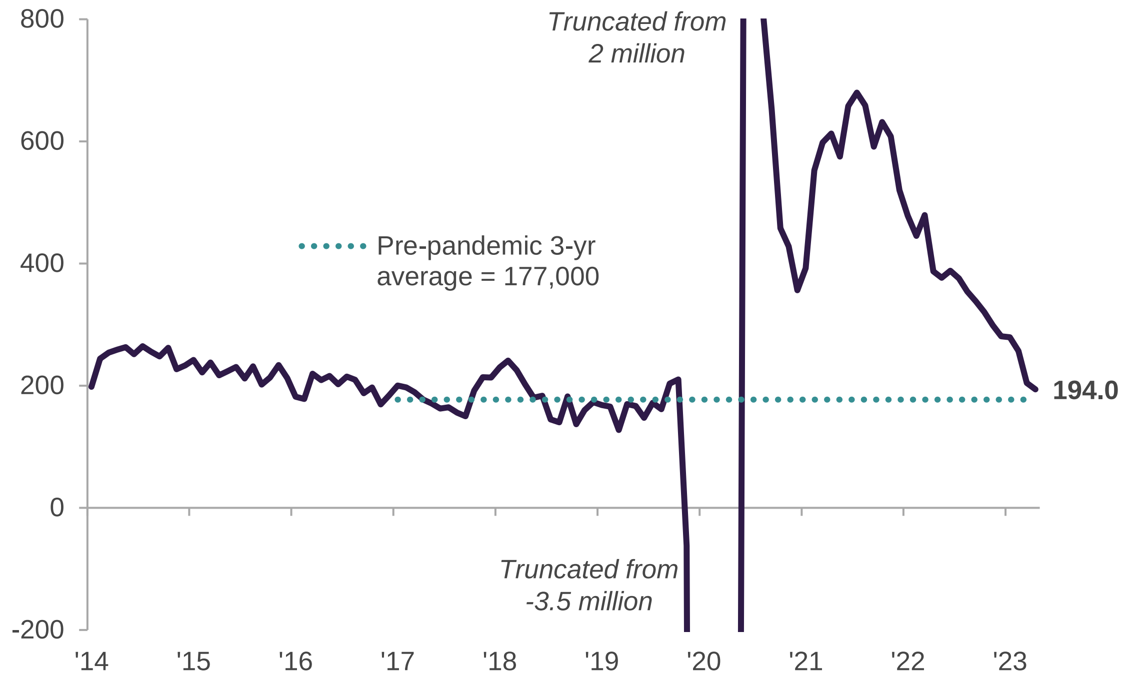
Data source: Truist IAG, Bloomberg, Bureau of Labor Statistics. Monthly data through August 2023.

Employment has cooled to the prior trend

While job growth has declined compared to very strong 2021 and 2022 results, the U.S. has created 194,000 new jobs on average for the past six months. That's a lot closer to the pre-pandemic 3-year average of 177,000.

At the very least, the Fed will probably need to maintain rates, though it's still possible additional rate hikes will be needed to curb inflation if price trends don't cooperate.

U.S. monthly job growth (Six-month average, in thousands)

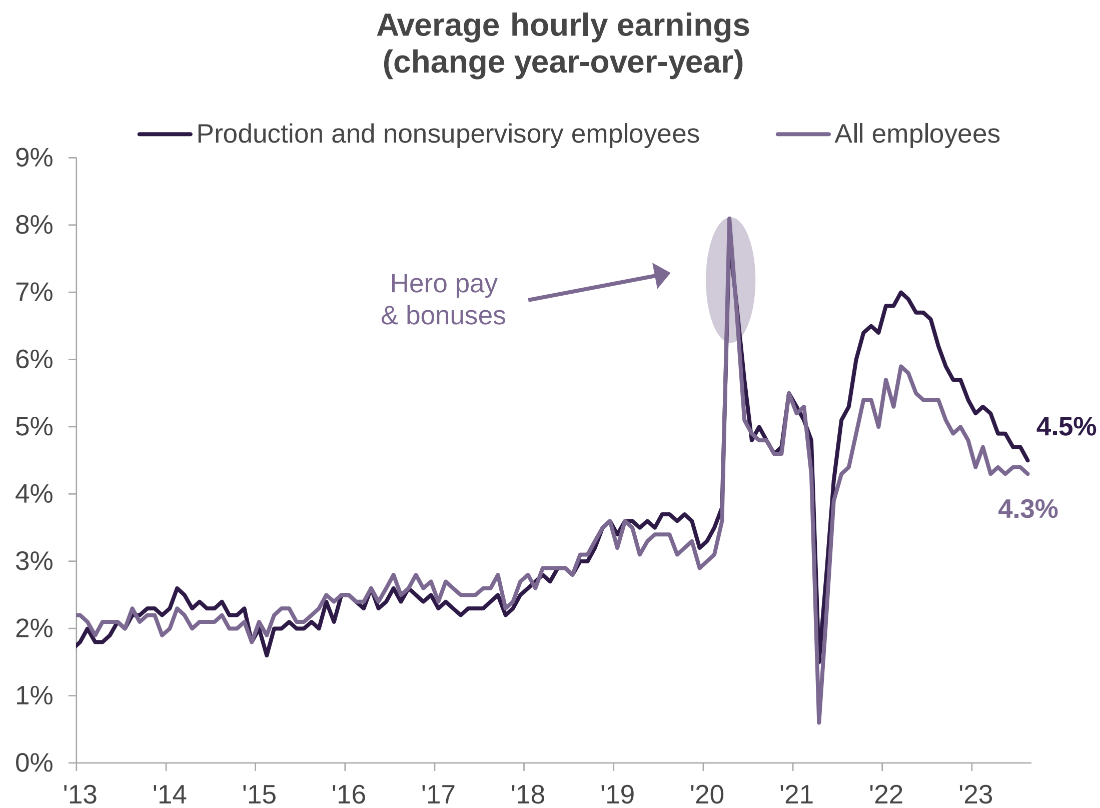


Data source: Truist IAG, Bloomberg, Bureau of Labor Statistics. Monthly data through August 2023

Wages down from their peak, but still running above pre-pandemic levels

Average hourly earnings rose 0.2% month over month in August. That's up 4.3% from a year ago, well-above the pre-pandemic 10-year average of 2.4%, but has dropped from the 2022 peak of 5.9%.

The pace of average hourly earnings for rank & file workers—officially known as production & nonsupervisory employees—also rose 0.2% during August, the smallest gain in 31 months. The annual pace rose 4.5%, well above its pre-pandemic rate of 3.2%. This is important since production & nonsupervisory employees are the bulk of all employees and where most of the dramatic post-pandemic wage gains have been concentrated.

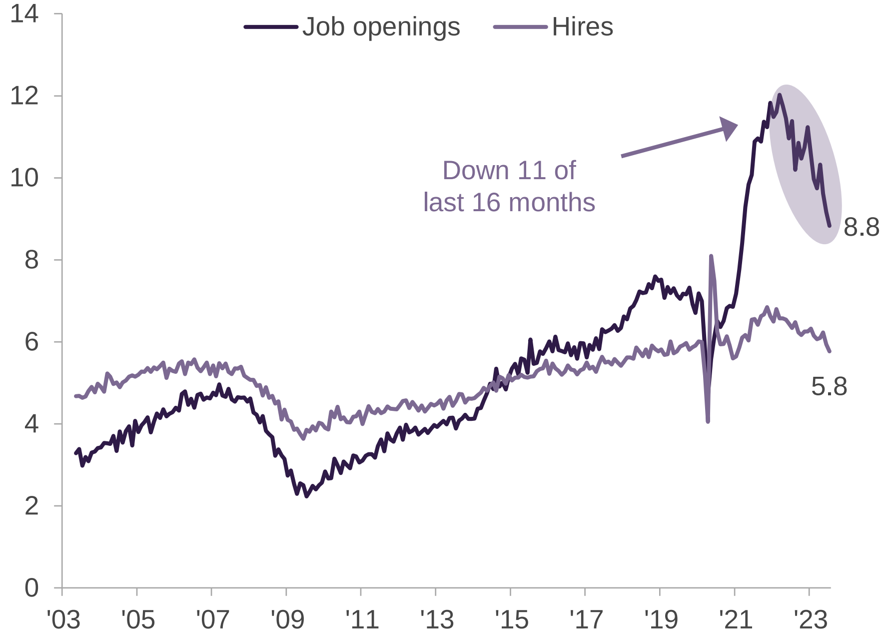


Data source: Truist IAG, Bloomberg, Bureau of Labor Statistics. Monthly data through August 2023.

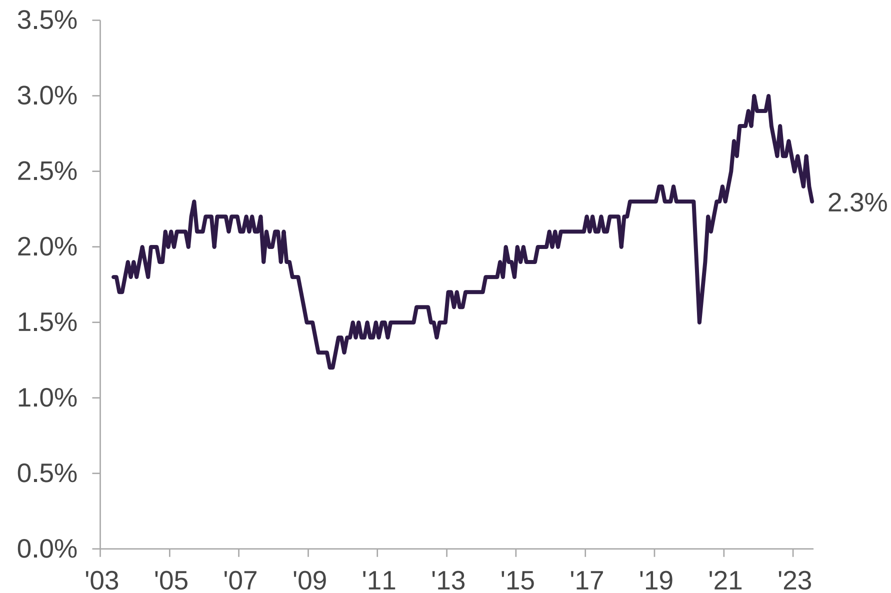
Job openings and hiring drop, while quit rate back down to prior trend

The number of job openings dropped 3.7% in July to 8.8 million, the 11th decline in the past 16 months. Hiring fell 2.8% to 5.8 million. Openings and hiring remain above pre-pandemic levels. Meanwhile, the so-called quit rate – officially known as the percentage of employees voluntarily quitting – slipped to 2.3% from 2.6% in May, and down from the cycle peak of 3% in 2022. It is now in-line with the pre-pandemic level.

U.S. job openings & hires (in millions)



Percentage of employees voluntarily quitting (all industries)



Data source: Truist IAG, Bloomberg, Bureau of Labor Statistics; monthly data through July 2023.

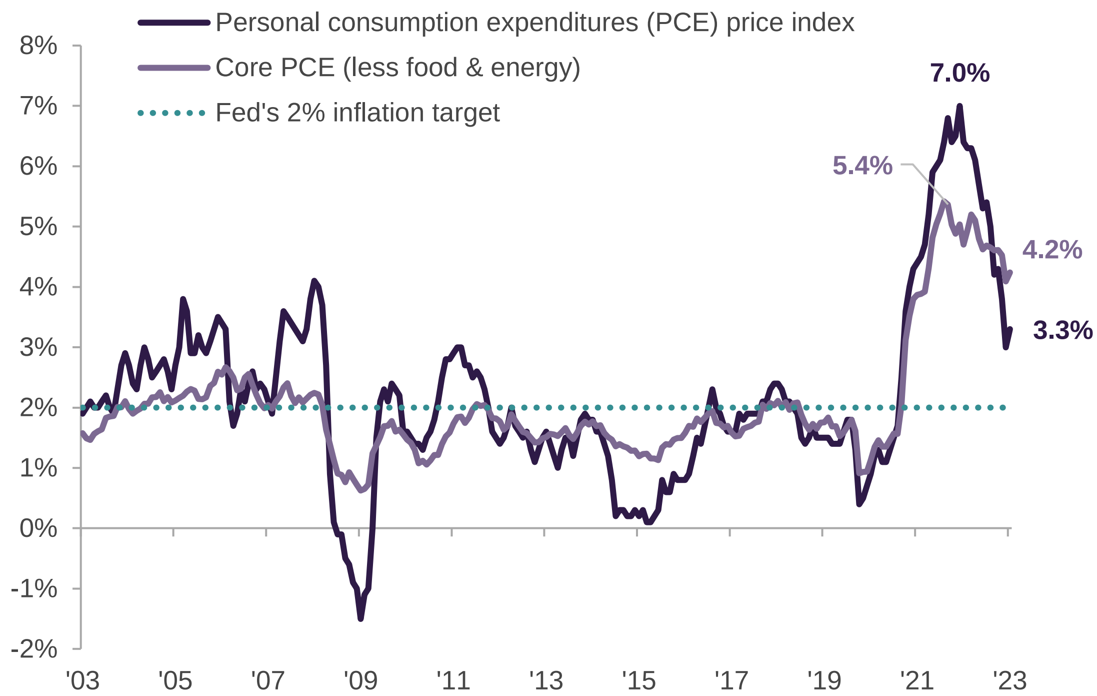
The Fed’s favorite inflation gauge is down from its peak, but still too high – don’t believe the "immaculate deflation" hype

Core PCE is the Fed’s favored inflation gauge. It rose 0.2% in July and increased 4.2% from a year ago. It’s moving in the right direction and is down from its March ’22 high of 5.4%.

More importantly for the Fed, deflation isn’t occurring in the U.S. – let alone an immaculate version some are pinning their rate cut hopes on. For instance, the PCE housing component has cooled from averaging 0.7% in the March ’22 through March ’23 period to 0.5% in the past 5 months, but that's still roughly twice the pre-pandemic 3-year pace of 0.28%.

Ultimately, inflation remains uncomfortably high and well-above the Fed’s 2% target, and likely contributed to the case for the Fed to pause but not stop rate hikes.

Personal consumption expenditures (PCE) year-over-year change



Data source: Truist IAG, Bloomberg, Bureau of Economic Analysis; monthly data through July 2023.

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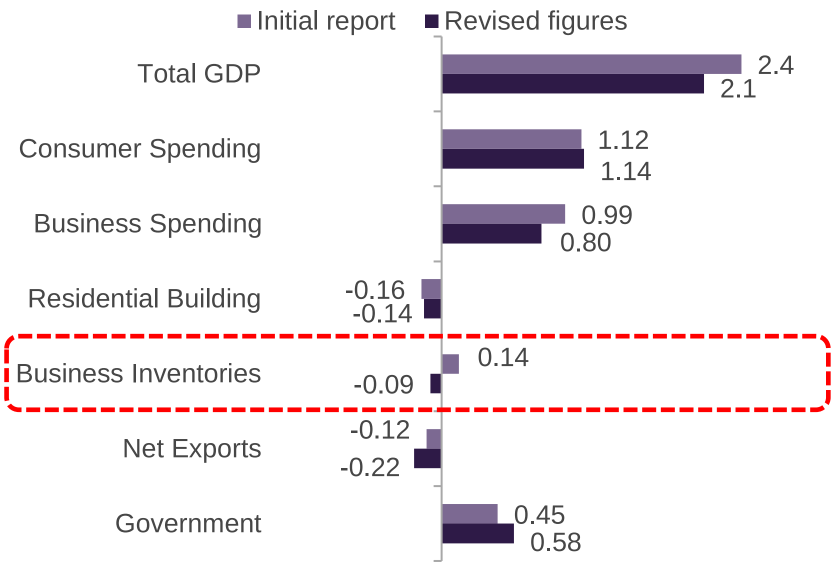
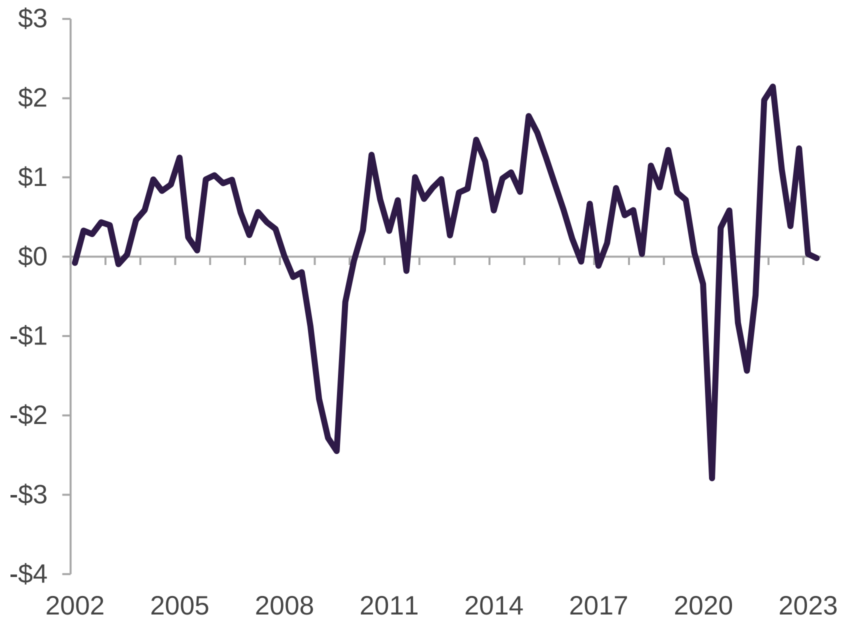
Second quarter U.S. growth revised downward due to swing in inventories

Real GDP rose 2.1% on an annualized basis in the second quarter, revised down from the initially reported 2.4% pace. The biggest contributor in the second quarter was consumer spending followed by business spending. However, there were downward revisions to business inventories, business spending, and net exports.

Contributions to percent change in real gross domestic product (GDP)



Change in business inventories (in $billions)



Data source: Truist IAG, Bureau of Economic Analysis. Left chart figures shown are inflation-adjusted (real) chained (2012) dollars on a seasonally adjusted annual rate.

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