STATE STREET GLOBAL ADVISORS

November 10, 2023
Commentary

Weekly Economic Perspectives

Contents

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The Economy

Central banks dominate the otherwise quiet data week via both words and action.

US

Unemployment claims have behaved erratically enough over the course of the year and have been revised substantially enough that any dramatic declarations about their direction of travel are unwise at this point. However, they have moved meaningfully higher in recent week and given that this ascent is corroborated by the reported increase in the unemployment rate, the message appears to be one of slow but steady labor market erosion. Continuing unemployment claims increased by 22k to 1.834 million, the highest since mid-April. The four-week moving average touched 1.789, the highest since mid-May.

Figure 1: US Continuing Unemployment Claims Near Cycle Highs

Sources: SSGA Economics, DOL, Macrobond

The preliminary November reading on the **University of Michigan consumer sentiment index** was a little perplexing as it showed a sizable jump in inflation expectations that seems at odds with recent market data. However, given that the exact opposite dynamic occurred in September (inflation expectations eased just as gasoline prices were surging), we suspect this is more of a lag issue than an outright disconnect. As such, we would expect to see the inflation expectation numbers moderate anew. For now, though, the short term (1-year) inflation expectations ticked up two tenths to a seven-month high of 4.4%. Long term (5-10 years) expectations jumped two tenths to 3.2%, the highest level since March 2011. This bears close watching, although we are not unduly alarmed at this moment given the series has shown considerable volatility over the past year. Given that the overall index is highly sensitive to inflation perceptions, it is not surprising that the headline index plunged 3.4 points to a six-month low of 60.4. The deterioration was concentrated in the expectations component, though current situation assessments also darkened.

Given the high cost of credit, consumers are becoming more discerning about its deployment. After an unusual and very large decline in overall **consumer credit** in September—driven by student loan prepayments—credit expanded by a modest $9.1 billion in October, lowering the growth rate to a two and a half year low of 3.4%.

Canada

The **minutes** of the Bank of Canada's (BoC) October 25 meeting hinted that policy rates may remain high for longer as the Bank left rates at a 22 year high on a "strong consensus". However, "some members felt that it was more likely than not that the policy rate would need to increase further." The debate is set to continue as "they agreed to revisit the need for a higher policy rate at future decisions with the benefit of more information." BoC senior deputy governor Carolyn Rogers also echoed the 'higher for longer' narrative this message this week in a speech.

Lending conditions for households including (mortgages and non-mortgage lending), which were the tightest in Q1 have eased significantly in Q3, as shown in the BoC's **Senior Loan Officer Survey**. The mortgage lending conditions index (balance of opinion) eased to -5.5% from 0.39% in Q2 and a massive 35.62% in Q1. Both, price and non-price measures have eased; however, it is not the case for business lending, which tightened to 13.20% from 7.60% in Q2.

However, the house sector's outlook has not improved in our thinking. An estimated 2.2 million Canadians will face an 'interest rate shock' when renewing their mortgages in the next two years, according to the bi-annual report from the Canada Mortgage and Housing Corporation (CMHC). The CMHC noted that more than 290,000 mortgages were renewed for a higher interest rate in 2023 and the share of mortgages in arrears in Q2 recorded a notable annual increase. However, mortgage delinquency rate in Canada is currently at 0.15%, near its historic lows. Separately, CMHC's Mortgage Consumer Survey showed that mortgage transactions in the past 18 months decreased 36%, compared to the same period in 2022. A staggering 74% mortgage consumers are either impacted already or expect to be impacted by higher interest rates. The report also showed that 'just' 55% respondents believed that their home value would appreciate in the next year, a sharp drop from 84% last year.

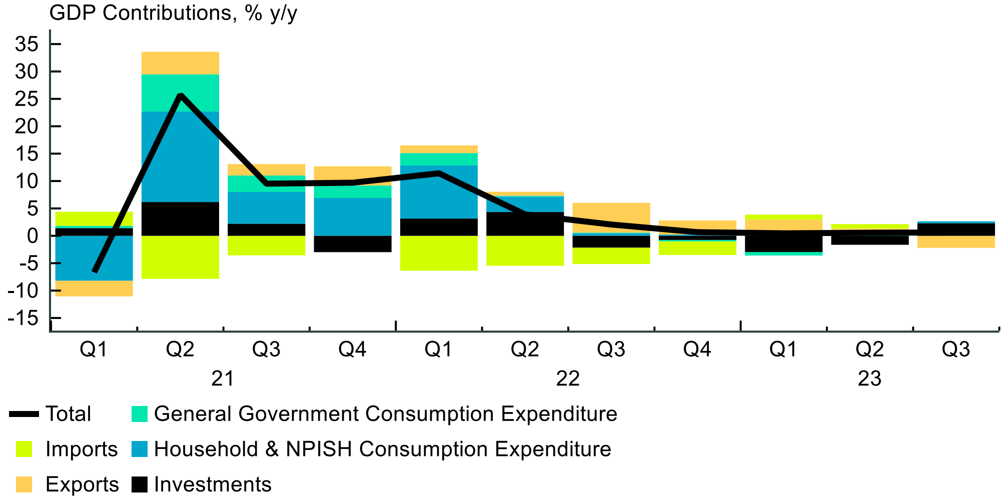
Figure 2: Mortgage Lending Conditions Ease In Canada

Sources: SSGA Economics, BoC, Macrobond
Updated as of 11/12/2023

UK

This week's headline **GDP** release showed virtually no growth in Q3, in line with Bank of England (BoE) expectations, and slightly better than the consensus of 0.1 contraction. However, the details were quite disappointing with significant declines in both private consumption and business investment. As the impact of interest rate hikes continued to grow, household consumption fell 0.4% q/q, following an increase of 0.5% in previous quarter. Meanwhile, weakness in housing market led to the fourth consecutive decline in residential investment (1.7% q/q). Business investment also contracted 4.2% q/q and government spending dropped by 0.5% q/q. The declines were offset by growth in net trade and inventories. Exports rose 0.5% q/q, following in a decrease of 0.9% in Q2 while imports fell 0.8% q/q. As interest rate hikes continue to weigh on private consumption and business investment, we continue to expect further weakening in GDP in Q4 and through the first half of 2024.

Figure 3: UK Economy Is Sliding Into A Recession



Sources: SSGA Economics, ONS, Macrobond
Updated as of 11/12/2023

Eurozone

The ***eurozone* services PMI** retreated 0.9 percentage points to a 32-month low of 47.8 in October, a third consecutive decline. New business volumes continued to contract sharply with new exports falling at the fastest pace over two-and-a-half years. Employment also slowed significantly. Costs increased but selling price inflation eased to the lowest since May 2021. German services fell back to contraction territory, down from September's 50.3 to 48.2 in October.

***German* industrial production** (including construction) contracted larger-than-expected at 1.4% m/m in September, equivalent to 2.1% q/q decline, and brought output to the lowest level since August 2020. The fall was driven by sharp declines in vehicles, pharmaceuticals, electrical equipment and energy.

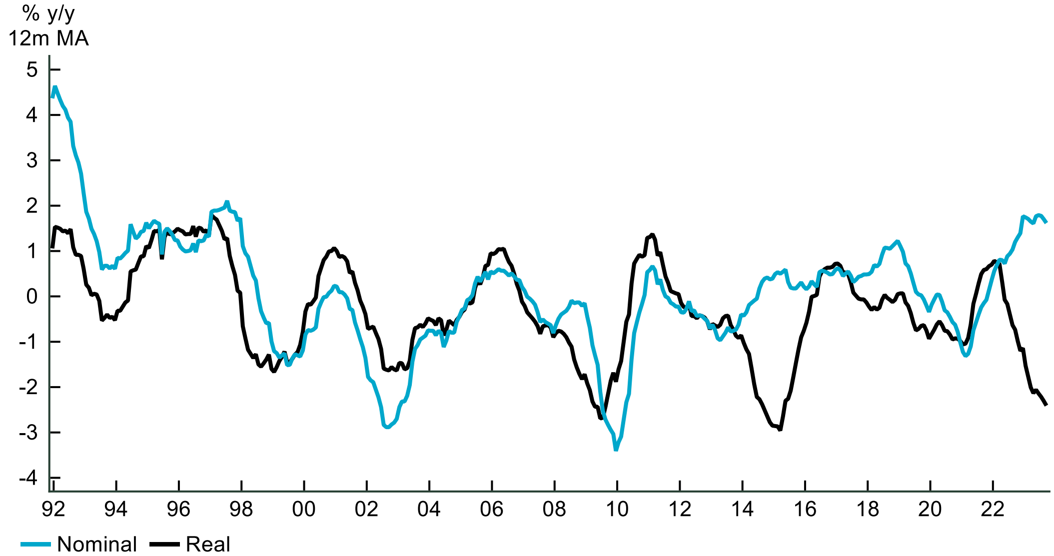
Final reading of ***German* inflation** showed that it decelerated 0.7 percentage points to 3.8% in October as expected. This is also the lowest rate since August 2021, reflecting the decline in energy prices. Core inflation rate (excluding food and energy) inched down three-tenths to 4.3%. Food prices were up 6.1% y/y in the month, contributing largely to the inflation.

***Italian* retail sales** fell for the second month by 0.3% m/m in September, bucking market expectation of a 0.1% increase. The fall was caused by declines in both food (-0.2%) and non-food sales (-0.5%). In annual terms, retail sales rose 1.3% in September compared to 2.4% in previous month.

Japan

Higher wages seem increasingly likely in Japan in the year ahead. UA Zensen, the country's largest trade union, announced its plans to ask for a 6% wage hike during the *shunto* negotiations next week; this comes after the trade confederation Rengo announced its plans for asking a 5% wage hike. Separately, **nominal wages** grew 1.2% m/m as expected in September. Bonus payments dropped 6.4% and dragged the overall wage growth; however, scheduled wages that account for 70% of overall wages grew three-tenths higher than in August at 1.5%. However, real wages declined for the eighteenth month.

Figure 4: Japanese Wages In Perspective



Sources: SSGA Economics, MHLW, Macrobond
Updated as of 11/12/2023

Reflecting this, in the Summary of Opinions of the **Bank of Japan** (BoJ) during last week's meeting, a member opined that "next year's base pay negotiations will exceed what was agreed this year;" and "it seems that achievement of the price stability target is coming into sight." The most encouraging comment this week however came from **Governor Ueda**, who said that the Bank could end easy monetary policy if they foresee real wages turning positive (not actually turning positive). As of September, they declined 2.4% y/y; however, if the momentum in wages sustains and inflation eases, this becomes a possibility in Q1 2024, when we expect the Bank to end negative interest rate policy.

Furthermore, real consumption as measured by the BoJ's **Consumption Activity Index** declined 1.0% m/m, after they increased 0.2% in August. Durable goods consumption declined 2.4% and non-durables by 1.6%. Nonetheless, owing to July and August increases, we expect the national accounts-based consumption to rise 0.5% q/q annualized, in Q3. However, imports could have declined strongly while, gross fixed capital formation could be reverting down from 2022 highs as well. All this mean that **GDP** could more or less be unchanged from Q2, after a strong 4.8% q/q annualized showing in Q2. Our pick is for a +0.1% q/q, annualized in Q3.

Australia

As widely expected, the **Reserve Bank of Australia** (RBA) hiked the cash rate by 25 bps this week to 4.35%. The Bank featured an upgraded inflation outlook, too. The Statement of Monetary Policy (SoMP) noted that the Bank considered leaving the cash rate at 4.10% but hiked due to a stronger outlook on inflation.

The headline & trimmed-mean CPI metrics are expected to rise by 4.5% (+0.4 ppts & +0.6 ppts, respectively) in December 2023. For December 2024, both CPI metrics are now expected to rise 3.5% (+0.2 ppts) and 3.3% (+0.2 ppts) respectively. More importantly, the Bank now forecasts inflation returning to their target in December 2025 (2.9%). Growth was upgraded too, to 1.6% y/y (+0.50 ppts) by the end of 2023 and to 2.0% (+0.4 ppts) in 2024. The GDP growth forecasts reflect upgrades to investments and exports, and not consumption. Finally, the unemployment rate will rise to 4.3% (-0.2 ppts) by the end of 2025, underscoring a strong labor market.

The liaison program highlighted the developing softness in the economy; specifically, it noted that the employment intentions have eased while the forward expectations on wage growth have also been easing.

The upgraded inflation forecasts raise the bar for further hikes, but the debate on the necessity of further hikes will continue. However, we maintain our terminal rate at 4.50%. Rate cuts are still an exceptionally long way off at the moment. Next week, we expect the Wage Price Index to print 4.0% y/y and employment should grow by about 10k, while full-time employment continues to cool in line with the developments we have been highlighting.

Week in Review (Nov 06 – Nov 10)

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, Nov 06					
EC	Services PMI (Oct, final)	47.8 (p)	47.8	48.7	Confirms initial release.
EC	Composite PMI (Oct, final)	46.5 (p)	46.5	47.2	Confirms initial release.
GE	Factory Orders (Sep, m/m)	-1.5%	0.2%	1.9% (↓)	Soft.
GE	Services PMI (Oct, final)	48.0 (p)	48.2	50.3	Soft.
JN	Labor Cash earnings (Sep, y/y)	1.2%	1.2%	0.8% (↓)	Outlook for 2024 is improving a lot.
Tuesday, Nov 07					
US	Consumer Credit (Sep, $, bn)	9.50	9.06	-15.79 (↓)	Growth slowing given high cost of credit.
GE	Industrial Production (Sep, m/m)	-0.1%	-1.4%	-0.1% (↑)	Weak.
AU	RBA Cash Rate Target	4.35%	4.35%	4.10%	Higher CPI & GDP forecasts mark upside risks.
Wednesday, Nov 08					
CA	Building Permits (Sep, m/m)	-1.2%	-6.5%	4.3% (↑)	Disappointing.
GE	CPI (Oct, y/y, final)	3.8% (p)	3.8%	4.5%	In line with expectations.
IT	Retail Sales (Sep, m/m)	0.1%	-0.3%	-0.4%	Weak.
Thursday, Nov 09					
US	Initial Jobless Claims (Nov 04, thous)	218	217	220 (↑)	Low but gently rising.
US	Continuing Claims (Oct 28, thous)	1,820	1,834	1,812 (↓)	Highest since mid-April.
FR	Wages (Q3, q/q, prelim)	na	0.5%	1.0%	Decelerating.
Friday, Nov 10					
US	U. of Mich. Sentiment (Nov, prelim)	63.7	60.4	63.8	Inflation expectations surprisingly rose.
UK	Industrial Production (Sep, m/m)	0.0%	0.0%	-0.5% (↑)	Weak.
UK	GDP (Q3, q/q, prelim)	-0.1%	0.0%	0.2%	Concerning.
IT	Industrial Production (Sep, m/m)	-0.2%	0.0%	0.3% (↑)	Weak.

Source: for data, Bloomberg®; for commentary, SSGA Economics.

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* Pensions & Investments Research Center, as of December 31, 2022.

† This figure is presented as of June 30, 2023, and includes approximately $63 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated. Please note all AUM is unaudited.

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