February 9, 2024
Commentary

Weekly Economic Perspectives

Contents

Spotlight on Next Week
US retail sales seen down slightly in January. UK unemployment rate to fall. Japan's Q4 GDP to decline sequentially. Aussie employment may have bounced back.

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The Economy

Macro data remain mixed and noisy, but slowdown and disinflation trends in place.

US

The US housing recession is over. Read our special report.

Incoming macro data remains quite noisy so each release should be taken with a grain of salt. For instance, the **non-manufacturing ISM index** rebounded strongly in January, more than retracting the big December decline. The headline rose 2.9 points to 53.4, new orders rose 2.2 to 55.0, and employment surged 6.7 points, though only to 50.5. Export orders and imports both surged, suggesting some degree of revival in external activity; it remains to be seen if this is sustained as similar bursts higher in prior months were not. Unsurprisingly, backlogs increased slightly, and delivery times lengthened. The price metric surged 7.3 points to 64.0, the highest since February 2023. On its own and at face value, this report suggests a notable uptick in service sector activity, but it follow a large decline in December so it may be better to average the two (52.0), which is marginally lower than the average of the previous three months (52.6).

Consumer credit is also exhibiting considerable volatility. Having surged by a massive $23.5 billion in November, overall consumer credit rose a minimal $1.6 billion in December, largely on the back of revolving credit. Given high interest rates, consumers are likely weary of carrying balances. It will be interesting to see if January brings an outright decline.

Meanwhile, anxiously awaited **CPI revisions** turned out to be a non-event, with updated data very closely matching previous estimates and confirming the strong disinflation trend of the last few months. We continue to look for a first Fed rate cut at the May meeting despite the strong January employment report. The start of the cutting cycle is not predicated on labor market weakness but rather on the disinflation trend, and that remains in place.

Canada

The latest **labor market** report was an upside surprise in the headline rather than the details. Following three months of little change, employment increased by 37k, but all the job gains were part-time. Meanwhile, the 0.1 percentage point decline in the unemployment rate (to 5.7%) was driven entirely by a 0.1 percentage point decline in the labor force participation rate (to 65.3%). This, together with possible seasonal adjustment issues with January job reports, does not suggest a strong labor market. Wage growth slowed to 5.3% y/y from 5.7% in the previous month, but remains elevated. As this week's labor report does not show a clear picture of the economy, the BoC is likely to remain on hold until it sees inflation improve.

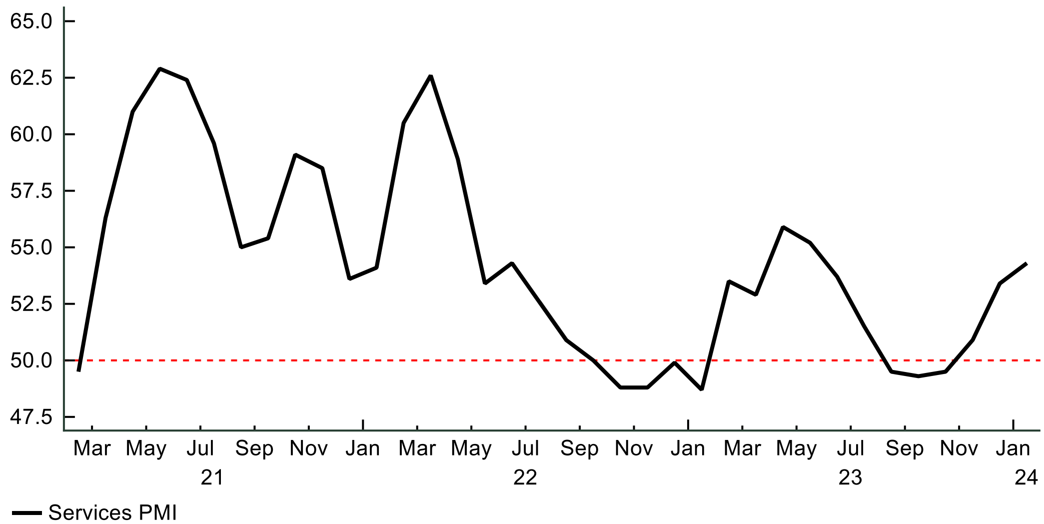
Building permits contracted 14.0% in December to the lowest level since October 2020. Residential permits fell 17.9%, driven by a sharp decline in the multi-unit segment. Non-residential sector permits fell 7.0%, with institutional in Quebec more than offsetting gains in commercial and industrial components across the country.

UK

The services sector expanded for the third consecutive month in January. The final reading of services registered 54.3, up from 53.4 in the previous month and above the earlier flash estimate of 53.8. With stronger business and consumer spending, output growth sped up to its fastest for eight months. Rebound in new orders also led to fastest rate of job creation since July 2023. Cost inflation softened but average prices charged rose robustly due to elevated wage pressures.

Figure 1: Robust Growth In UK Services Activity

% Balance / Diffusion Index



Sources: SSGA Economics, S&P Global
Updated as of 2/9/2024

Eurozone

There was little new data released in the region this week, with service PMIs tracking preliminary data closely and inflation doing the same.

Italian data releases point to some building softness in an economy that has relatively outperformed in 2023. ***Italian*** **consumer sentiment** has been relatively buoyant for much of last year, but took and big step down in December and failed to improve much in January. At 96.4, it marked the second lowest reading since October 2022, when inflation was much higher. Perhaps not surprisingly, retail sales dipped 0.1% in December to settle just 0.3% higher than in December 2022.

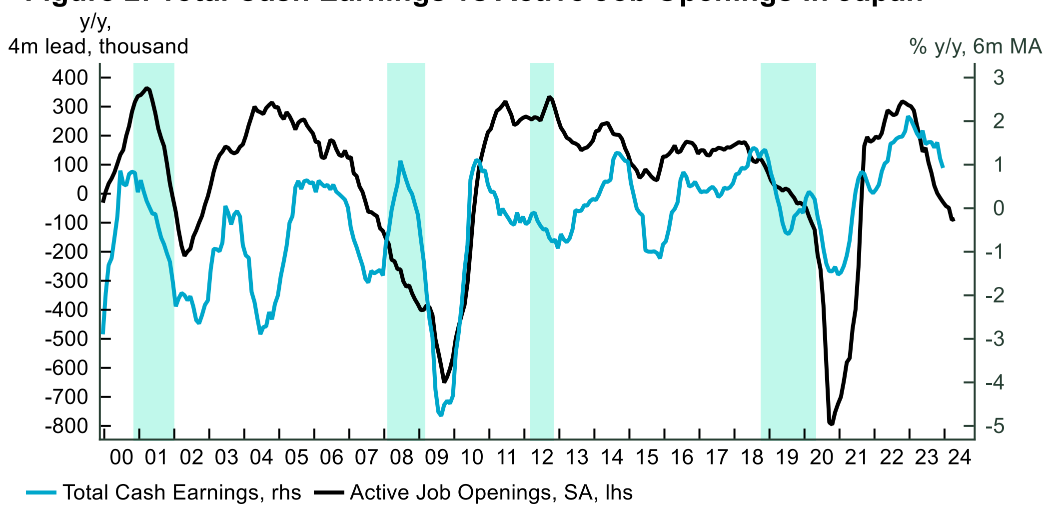
Italian **industrial production** rose 1.1% m/m in December, but this follows persistent weakness over the course of the year and still left output 2.1% lower than in December 2022. For 2023 as a whole, industrial production declined 2.5%.

Japan

Confidence is rising every week at the **Bank of Japan (BoJ)** for its first rate hike in 17 years. Governor Ueda this week reiterated in front of the parliament that even if the bank ends negative interest rates, "*accommodative financial conditions will continue*". Another speech from Deputy Governor Uchida said that "*it is hard to* *imagine a path in which it would then keep raising the interest rate rapidly.*" These comments echo our long-standing view that the BoJ will increase interest rates only twice in 10 bps moves to a terminal of 0.1% this year. Officials however did not comment on how they would perceive a possible negative GDP print next week.

Monthly wage growth continued to show differences due to sampling methodologies; **total cash earnings** improved 1.0% y/y in December, while the data from a constant sample remained higher at 2.1% for a third month. The headline is weighed by smaller increases in bonuses. There are high expectations for this year's *shunto* wage negotiations and the boost is much needed right now, as total active job openings—a leading indicator of wages—have been declining.

Figure 2: Total Cash Earnings vs Active Job Openings In Japan



Sources: SSGA Economics, MHLW, Macrobond
Updated as of 2/9/2024

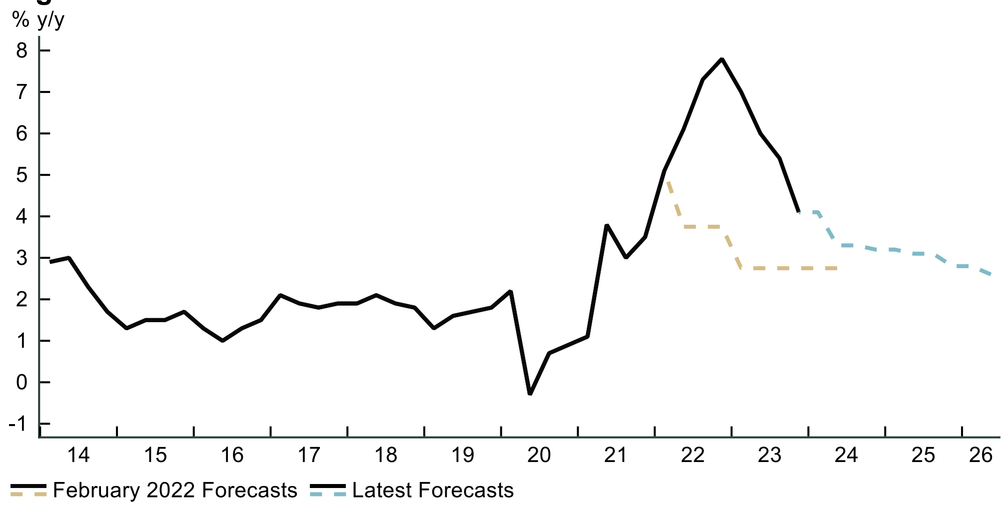
Meanwhile, consumption remains disappointing; the **BoJ Consumption Activity Index** echoed last week's retail sales data and declined by a rather large 1.7% y/y in December. The index correlates with the private consumption in the national accounts by 84% and supports our weak Q4 tracking, which is now consensus. We think the economy lost some (more) momentum in Q4 and forecast a sequential GDP decline of 0.1% q/q. There is a high risk on either side, but the underlying details will highlight feeble consumption and muted exports. Inventories also may have declined, so if the economy grows, it will be either due to higher services exports (tourism) or a faster decline in imports. The higher confidence from the BoJ will be tested next week and if the bank still remains upbeat about their policy maneuver, there is chance of them exiting negative rates or abandoning Yield Curve Control by April. We will know better next week.

Australia

The **Reserve Bank of Australia (RBA)** held its policy as widely expected and retained its tightening bias as "*a further increase in interest rates cannot be ruled out.*" CPI forecasts have been lowered across the horizon, and is now expected to rise 3.3% y/y (down -0.6 ppts from November) in H1 2024 and 3.2% (-0.3) in December 2024. If the ongoing disinflation coincides with slower demand, inflation could decline faster, and an easing cycle may commence. We still expect the first rate cut to happen in August. The current Statement of Monetary Policy's (SoMP) forecasts may not miss the actual CPI as badly as they did during February 2022 (see chart 4), but the downside risk to inflation is more pronounced currently.

This view was echoed by Governor Michele Bullock during her testimony before the Australian parliament later in the week: *"if consumption slows more quickly than expected, it could be an opportunity to cut rates."* Furthermore, the start of the easing cycle does not necessarily require inflation to be within 2-3% target band by the year end.

Figure 3: RBA's CPI Forecasts From The SoMPs



Sources: SSGA Economics, ABS, RBA, Macrobond
Updated as of 2/9/2024

Economic growth forecasts have also been revised down; the RBA now expects GDP to grow 1.3% (-0.5 ppts) in H1 2024 and 1.8% (-0.2 ppts) in H2. All these put emphasis on the labor market, which the RBA noted to 'ease gradually', but, opposed to our view of cooling rapidly now. The unemployment rate is now forecasted to rise to 4.3% by December 2024, below our expectations of 4.5%.

Retail volumes in Q4 rose 0.3% q/q, somewhat more than expectations of 0.1%, due to better retail prices. The ABS noted that consumers "*took advantage of discounting for discretionary items like furniture and electronic goods.*" Household goods rose 2.3% q/q and offset declines in clothing (-1.6%) and cafes (-2.1%).

Next week, the January labor market data will continue highlighting seasonality issues. Nonetheless, the economy may have added 15k jobs (total employment, seasonally adjusted), below the consensus expectations.

Week in Review (Feb 05 – Feb 09)

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, Feb 05					
US	ISM Services Index (Jan)	52.0	53.4	50.5 (↓)	Upside surprise, unwinds December's drop/
UK	Services PMI (Jan, final)	53.8 (p)	54.3	53.4	Good.
EC	Composite PMI (Jan, final)	47.9 (p)	47.9	47.6	Soft.
EC	Services PMI (Jan, final)	48.4 (p)	48.4	48.8	Soft.
GE	Services PMI (Jan, final)	47.6 (p)	47.7	49.3	Soft.
JN	Labor Cash Earnings (Dec, y/y)	1.4%	1.0%	0.7% (↑)	Better growth on constant sample basis.
AU	RBA Cash Rate Target (Feb)	4.35%	4.35%	4.35%	Hawkish hold.
AU	Real Retail Sales (Q4, q/q)	0.1%	0.3%	-0.1% (↓)	Lower prices in Q4 boosted volumes.
Tuesday, Feb 06					
CA	Building Permits (Dec, m/m)	2.0%	-14.0%	-3.9%	Worrying.
GE	Factory Orders (Dec, m/m)	-0.2%	8.9%	0.0% (↓)	Welcome bounce, but still very weak.
IT	Consumer Confidence Index (Jan)	na	96.4	95.8	Notable step down in December-January.
Wednesday, Feb 07					
US	Trade Balance (Dec, $ bn)	-62.0	-62.2	-63.2	Improving in real terms also.
US	Consumer Credit (Dec, $ bn)	16.00	1.56	23.48 (↓)	Follows massive November's surge.
GE	Industrial Production (Dec, m/m)	-0.5%	-1.6%	-0.2% (↑)	Dismal.
IT	Retail Sales (Dec, m/m)	na	-0.1%	0.3% (↓)	Soft. Up only 2.2% y/y.
JN	Leading Index CI (Dec, prelim)	109.3	110.0	108.1 (↑)	Good.
Thursday, Feb 08					
US	Initial Jobless Claims (Feb 03, thous)	220	218	224	Still very low.
US	Continuing Claims (Jan 27, thous)	1,878	1,871	1,898	Still very low.
Friday, Feb 09					
CA	Unemployment Rate (Jan)	5.9%	5.7%	5.8%	Driven by weaker labor participation.
GE	CPI (Jan, y/y, final)	2.9% (p)	2.9%	3.7%	As already reported.
FR	Wages (Q4, q/q, prelim)	na	0.3%	0.5%	Easing somewhat.
IT	Industrial Production (Dec, m/m)	0.9%	1.1%	-1.5%	Down 2.1% y/y.

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

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

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