STATE STREET GLOBAL ADVISORS

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Commentary

Weekly Economic Perspectives

Contents

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The Economy

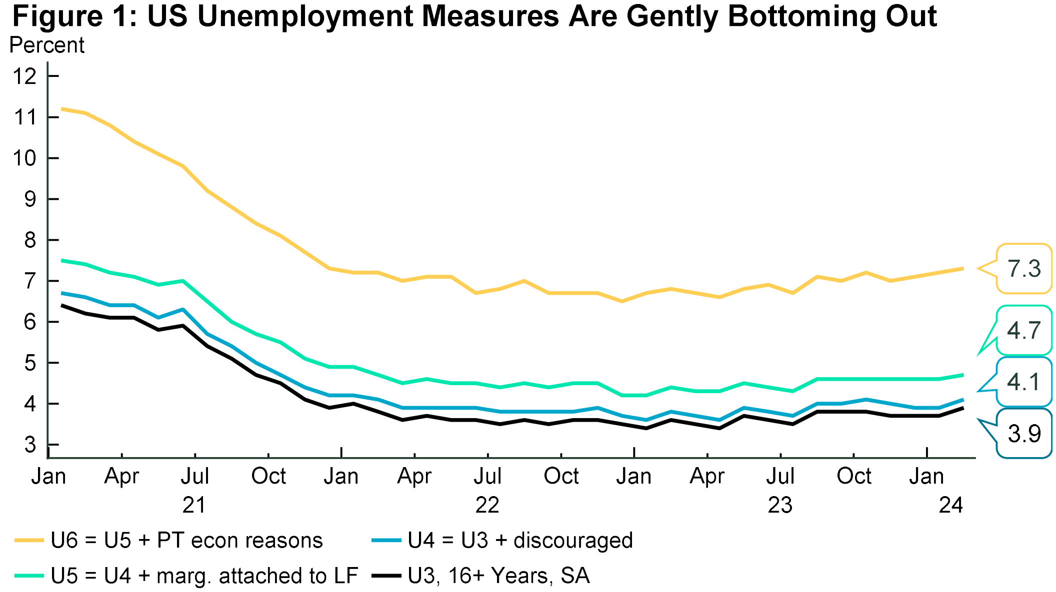
Markets lack conviction on timing for rate cuts as volatile data extends uncertainty.

US

The deterioration in US macro data quality has crossed from pestering nuisance into genuine problem territory; the **payrolls report** is but a high-profile example of a much larger problem. The economy added a better-than-expected 275k jobs in February, but this was accompanied by a record downward revision of 167k to the prior two months. As a result, the initial 353k jobs we thought were added in January, turned out to have been only 229k. To be sure, even the downwardly revised figure is still remarkably high, but the problem is that we are lurching from big revision to big revision (January's revision was a record high) and amid all the data noise we risk losing track of the true signal and underlying trend.

To us, the trend remains one of gentle labor market erosion as excess labor demand has largely faded and wage pressures ease. Indeed, the household report—which has been painting a less upbeat picture than the establishment report for some months—showed a further increase in the number of unemployed and a two-tenth rise in the **unemployment rate** to 3.9%. The underemployment rate—a broad measure of labor market slack that includes discouraged workers, those marginally attached to the labor force, and those working part time for economic reasons even though they would prefer full-time work—ticked up a tenth to 7.3%; it had bottomed at 6.5% in December 2022. The labor force participation rate was unchanged.

Figure 1: US Unemployment Measures Are Gently Bottoming Out



Sources: Macrobond, SSGA Economics, BLS
Updated as of 3/11/2024

Wage pressures eased markedly, with average hourly earnings (AHE) up just 0.1% m/m after January's downwardly revised 0.5% m/m gain. We argued last month that the big rise in AHE then was largely due to a weather-related compositional skew that would reverse; the latest update supports that interpretation. Overall AHE wage inflation eased a tenth to 4.3% y/y while AHE inflation for production and nonsupervisory employees eased two tenths to 4.5% y/y. The upside in this report was the improvement in hours worked. The average workweek increased by 18 minutes, retracing half of January's decline, and overtime extended. In combination with higher employment, this lifted aggregate hours (a measure of total labor effort in the economy) by 0.4%, unwinding January's decline, and boding well for wage and salary income growth in February.

Other data this week confirmed the gentle trend of erosion. **Job openings** dipped slightly in January, although they remain elevated relative to pre-Covid norms. However, both the hire rate and the quits rate have now dipped below levels prevailing in 2018-19, suggesting a little more softness than openings alone imply.

Unemployment claims remain very low historically but they, too, are in the early stages of a gentle uptrend. This is more visible in the continuing claims data, which rose to just over 1.9 million in the latest week. The more stable 4-week moving average reached 1.888 million, the highest level since December 2021.

After two big moves (down in December and up in January) the **non-manufacturing ISM index** posted a more modest 0.8-point retreat in February, settling at 52.6. The slightly softer than anticipated print masked some important areas of strength, however. The business activity metric (the old headline) touched a five-month high of 57.2, and new orders hit a six-month high of 56.1. Employment dipped back into contraction with a 2.5-point decline to 48.00. and the prices paid metric eased 5.4 points to 58.6. All in all, a mixed report, but far from weak.

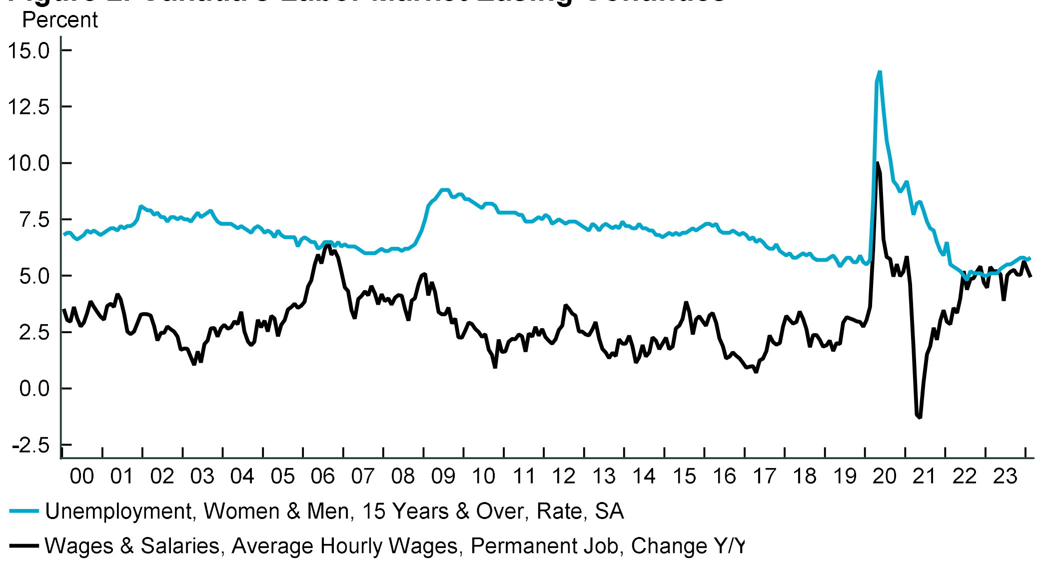
Consumer credit has exhibited considerable volatility in recent months. Having surged by a massive $28.3 billion in November, it was almost flat in January and rose by $19.5 billion in February. The increase was fairly evenly split between revolving and non-revolving credit. The latter aligns with the marked improvement in auto sales during the month. Overall consumer credit is only up 2.5% y/y as high interest rates weighs on credit demand.

Canada

The **Bank of Canada (BoC)** left its overnight rate unchanged at 5.0% while continuing its policy of quantitative tightening. The bank highlighted evidence of weaker economic momentum as "final domestic demand contracted with a large decline in business investment". The bank also stated that "employment continues to grow more slowly than the population, and there are now some signs that wage pressures may be easing". Meanwhile, the BoC continues to expect "inflation to remain close to 3% during the first half of this year before gradually easing" and is still concerned about inflation risks. That said, the BoC will continue to sit on the sidelines for the next few months while maintaining its cautious rhetoric.

The labor market showed further signs of easing in February. Employment rose by 41k in the month, following a similar rise in January (+37k). The increase was mainly driven by gains in full-time jobs (+71k) while part-time employment fell by 30k. Given rapid labor force growth, the unemployment rate inched up a tenth to 5.8%. Wage growth slowed by four tenths to 4.9% y/y but remains elevated.

Figure 2. Canada's Labor Market Easing Continues



Sources: Macrobond, SSGA Economics, StatCan
Updated as of 3/11/2024

Building permits rose by 13.5% in January, well above consensus of 4.5% increase. Residential permits increased 12.6%, mainly due to strong rebound in multi-unit construction intentions. Non-residential permits was up by 14.8%, with commercial rose 34.5% to the highest monthly level since April 2023.

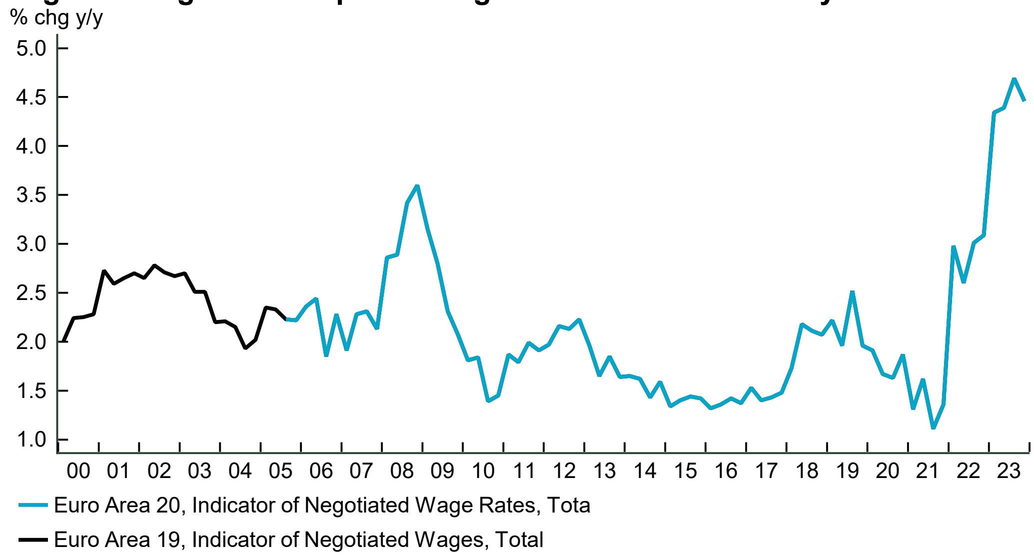
UK

The services sector experienced another strong expansion in February, with business expectations at their highest since February 2022. The final reading of **services PMI** registered 53.8, slightly lower than 54.3 in previous month and the earlier flash estimate of 54.3. New orders rose solidly, driven by rising business and consumer spending. Job creation rose modestly but at the fastest pace since July 2023. Meanwhile, strong wage pressures and higher shipping costs led to strongest rate of input price inflation since September 2023 and robust increase in average prices charged.

Eurozone

The March **ECB meeting** did not create any waves. All three policy interest rates were left unchanged, with the main refinancing rate, the marginal lending facility rate, and the deposit facility rate remaining at 4.50%, 4.75% and 4.00%, respectively. There were some noticeable changes to the staff macroeconomic forecasts but these essentially only brought the latest ECB projections in line with our forecasts from mid-December so they do not force any reassessment on our part. Specifically, 2024 real GDP growth was lowered two tenths to 0.6% (we are still comfortable with our 0.7% projection) and headline 2024 inflation was lowered from 2.7% to 2.3% (we are still comfortable with our 2.4% projection). The parameters around balance sheet policy are evolving as already announced. APP (asset purchase program) balances are already declining as reinvestments have stopped. PEPP (pandemic emergency purchase program) reinvestments will slow by €7.5 billion a month during the second half of the year before ending altogether at the end of the year. Although economic activity is and is expected to remain tepid for some time, the ECB remains concerned about pipeline wage inflation, and rightly so (Figure 3). This is why we never anticipated more than 100 basis points worth of rate cuts from the ECB this year even when market sentiment had shifted more dovish than that. June still looks like a good time for the easing cycle to begin.

Figure 3: Significant Pipeline Wage Pressures Are A Worry For The ECB



Sources: Macrobond, SSGA Economics, ECB
Updated as of 3/11/2024

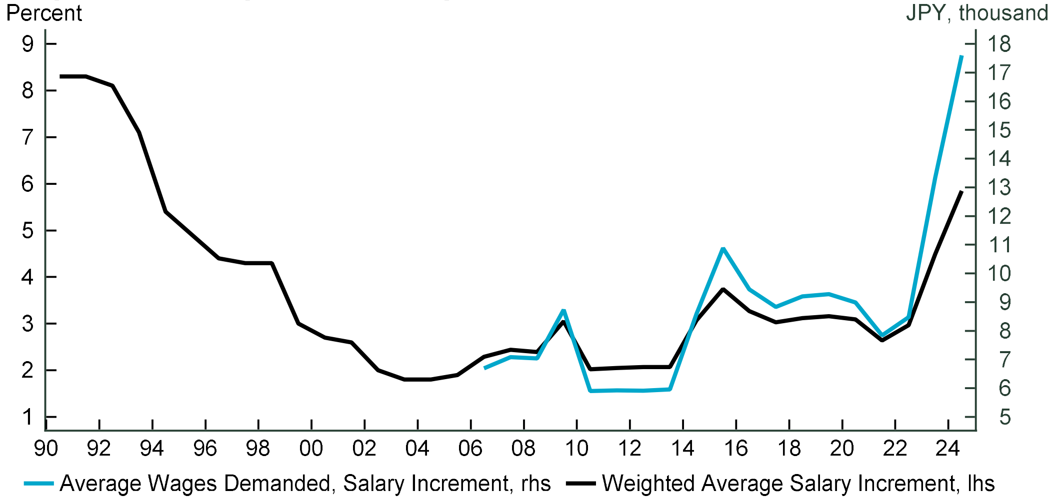
Japan

Japan's largest labor union, Rengo, officially demanded an average hike of 5.85%, way above market expectations and the highest in 30 years! This has taken the weighted average increment demanded to 17,606 yen. We expect an average raise of 5% among large firms, to be announced in the next week. Resultingly, **we now see a higher chance the Bank of Japan (BoJ) will adjust its policy in March**.

Nominal cash earnings rose 2.0% y/y in December, an acceleration from an upwardly revised 1.8% in November. However, a 16.2% jump in special wages (bonuses, etc.) has caused this, otherwise on a constant sample basis, the growth remained at a healthy 2.0%. Most importantly, real wages declined meagerly by 0.6%, much below the 2.1% decline in November, in line with our thinking highlighted recently in this blog piece.

Household spending meanwhile declined 6.3% y/y in January (or declined by 2.1% m/m), the biggest decline since February 2021. However, this does not necessarily reflect the trend in consumption as auto related spending dragged the overall data due to the Noto peninsular earthquake.

Figure 4: Average Shunto Wage Hike Demand In Japan



Sources: Macrobond, SSGA Economics, RENGO
Updated as of 3/11/2024

Inflation in Tokyo rebounded in February, as the headline index jumped 2.6% y/y, after dropping to 1.8% last month. Energy prices declined by just 5.0% y/y, an eleven-month high as the base effects are now waning, as we have been writing for some time. Food prices still remain strong at 4.7%, but down from 8.7% in September/October 2023. This is also reflective in the 1.0% rise in meals eaten outside, down from 8.3% in May 2023. Otherwise, services prices rose 2.0% y/y, the seventh month at or above 2.0%; they rose 3.1% without imputed rents. However, recreational services continued rising in double digits, especially those of package tours remain very strong.

In another positive development, Q4 **capex** rose 16.4% y/y, after a 3.4% rise in Q3. Most notable driver is significantly high investments in ICT equipment (65.8%) and information & communications (39.8%). This strong result will have a significantly positive bearing on next week's Q4 GDP revision, which could potentially swing growth into a strong positive territory. So, the Japanese economy will have escaped a technical recession, but we will know for sure next week.

The BoJ continued to offer constructive guidance to markets on their impending policy normalization. **Governor Ueda** made two critical comments this week:

1. The BoJ will continue buying JGBs whether they end the Yield Curve Control (YCC) or not; so, they may not 'stealth taper' their government bond holdings.

2. After ending negative rates, the BoJ will continue using interest on excess reserves as short-term interest rates; so, the benchmark policy rate will likely remain the same.

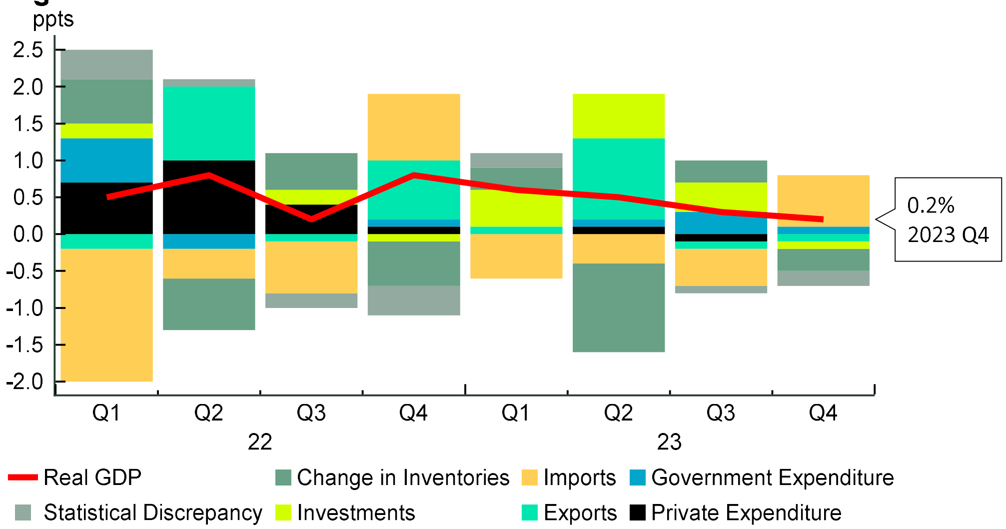
The policy board member Nakagawa said "*it will take until autumn and beyond*", if they wait until smaller firms announce their wage growth rates, so the bank may still make a policy move in the next 60 days, but **we see a higher probability of a policy movement on March 19th, when the BoJ meets this month**.

Australia

Q4 GDP growth slowed to 0.2% q/q, in line with our thinking but below expectation of 0.6%. The difference entirely came from inventories, which shaved 0.3 ppts off of growth. Otherwise, a 3.4% q/q decline in imports was the largest contributor to growth at 0.7 ppts, as we expected. This was especially caused by a 9.0% contraction in travel services imports as Australians travelled less overseas.

Otherwise, consumption treaded water at 0.1% q/q and has not contributed to growth. Spending on food rose (0.9%) the most since Q1 2023 while spending on vehicles (-3.6%), hotels & cafes (-2.8%), and clothing (-2.5% q/q) declined. Higher interest rates are cooling aggregate demand. Furthermore, the household savings rate rose to 3.2% from 1.9% in Q3, far better than the Reserve Bank of Australia (RBA) forecast of 0.9% for December 2024. Capital spending declined 0.2% q/q, as declines in residential construction and in plant and equipment was balanced by non-dwelling construction and intellectual property rights.

Figure 5: Contributions to Australia's GDP Growth



Sources: SSGA Economics, ABS, Macrobond

On the income side, profits earned by non-financial firms rebounded 2.9% q/q on higher commodity prices, while compensation of employees rose 1.4%. Importantly, labor productivity rose 0.5% for a second successive quarter as nominal unit labor costs growth eased to 1.3%.

Week in Review (Mar 04 – Mar 08)

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, Mar 04					
No major releases					
Tuesday, Mar 05					
US	Factory Orders (Jan)	-2.9%	-3.6%	-0.3% (↓)	Weighed down by aircraft orders.
US	Durable Goods Orders (Jan, final)	-6.1%	-6.2%	-6.1%	Weighed down by aircraft orders.
US	ISM Services Index (Feb)	53.0	52.6	53.4	Mixed details.
UK	S&P Global UK Services PMI (Feb, final)	54.3	53.8	54.3	OK.
EC	HCOB Services PMI (Feb, final)	50.0	50.2	50.0	Soft, but at least not contracting.
GE	HCOB Services PMI (Feb, final)	48.2	48.3	48.2	Weak.
FR	Industrial Production (Jan, m/m)	-0.1%	-1.1%	0.4% (↓)	Soft.
IT	GDP (Q4, q/q, final)	0.2%	0.2%	0.2%	As already reported.
AU	GDP (Q4, q/q, sa)	0.2%	0.2%	0.2%	Aggregate demand slowed, great for the RBA.
Wednesday, Mar 06					
US	JOLTS Job Openings (Jan, thous)	8,850	8,863	8,889 (↓)	In uneven downtrend.
CA	Bank of Canada Rate Decision	5.00%	5.00%	5.00%	On hold.
JN	Labor Cash Earnings (Jan, y/y)	1.2%	2.0%	0.8% (↓)	Solid wage momentum, even in *shunto.*
Thursday, Mar 07					
US	Trade Balance (Jan, $bn)	-63.5	-67.4	-64.2 (↓)	Worsening again?
US	Nonfarm Productivity (Q4, final)	3.1%	3.2%	3.2%	Helps offset some nominal wage growth.
US	Initial Jobless Claims (02-Mar, thous)	217	217	217 (↑)	Still very low.
US	Continuing Claims (24 -Feb, thous)	1,880	1,906	1,898	In gentle uptrend.
US	Consumer Credit (Jan, $bn)	10.00	19.49	0.92 (↓)	Up a modest 2.5% y/y.
CA	Building Permits (Jan, m/m)	4.5%	13.5%	-14.0%	Strong.
EC	ECB Main Refinancing Rate	4.50%	4.50%	4.50%	On hold for a while longer.
GE	Factory Orders (Jan, m/m)	-6.0%	-11.3%	12.0% (↑)	Weak.
Friday, Mar 08					
US	Change in Nonfarm Payrolls (Feb, thous)	200	275	229 (↓)	Record downward revision.
US	Unemployment Rate (Feb)	3.7%	3.9%	3.7%	Has bottomed.
CA	Unemployment Rate (Feb)	5.8%	5.8%	5.7%	In line with expectations.
EC	GDP (Q4, q/q, sa, final)	0.0%	0.0%	0.0%	As previously reported.
GE	Industrial Production (Jan, m/m, sa)	0.6%	1.0%	-2.0% (↓)	Still weak.
JN	Leading Index CI (Jan, prelim)	109.7	109.9	110.5 (↑)	Great result.

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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Marketing Communication

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