STATE STREET GLOBAL ADVISORS

April 5, 2024
Commentary

Weekly Economic Perspectives

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Spotlight on Next Week
US headline inflation to tick higher but core measure should ease. The ECB and the BoC to hold rates. Wage growth may have eased in Japan. Aussie consumer sentiment to improve.

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The Economy

The theme of macro resilience continues to support markets.

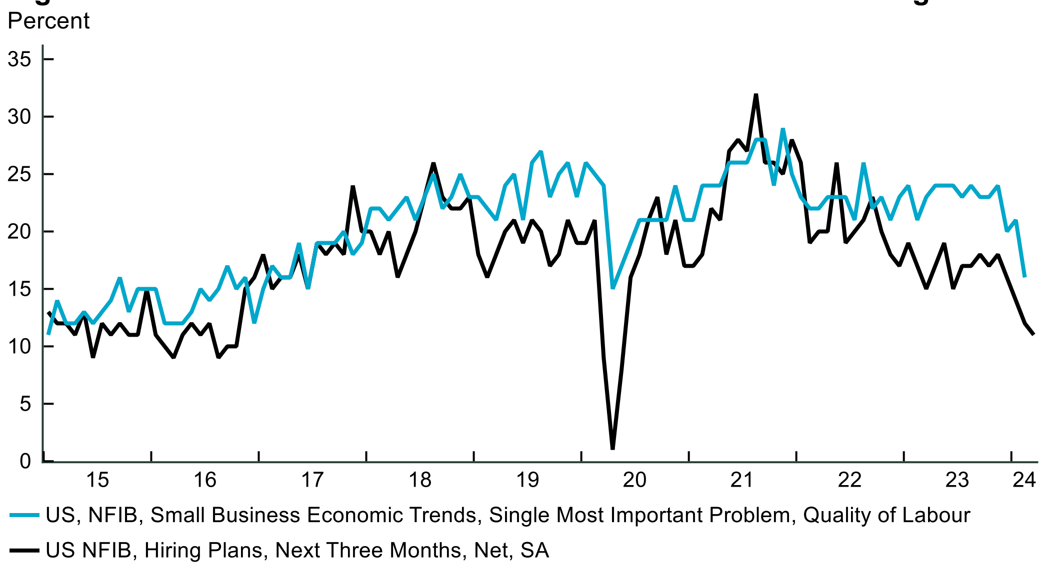
US

The US economy continues to generate jobs at a seemingly relentless pace as **payrolls** grew by a much better than expected 303k in March. The upside surprise was notable, yet in line with the labor market's repeated outperformance of expectations in recent months. What was not in line with recent trends was that this report was not accompanied by a downside revision to prior months; rather, there was a small upward revision. This "broke the pattern" of revisions that had prevailed over the past year+, namely one large positive revision followed by three large negative ones. It remains to be seen if revisions become more random going forward (as they should be), but this makes this report even stronger than we anticipated.

There was nothing in the industry distribution that really stood out. Compositionally, this was very similar to the February report, with reasonably broad job gains across industries and the government continuing to play a big role. Private payrolls grew 232k and the government added 71k. Healthcare and leisure/hospitality accounted for about two thirds of the 190k private service sector jobs created in March. In the household survey, employment increased by 498k, and unemployment declined by 29k, raising the labor force by 469k and lifting the participation rate by two tenths to 62.7%. The **unemployment rate** dipped a tenth to 3.8% but the underemployment rate was steady at 7.3%.

After a compositional-driven surge in January and a corrective relapse in February, **wage growth** returned to more typical levels. Total average hourly earnings (AHE) grew 0.3% m/m, in line with the 2023 average. AHE for production and non-supervisory employees grew just 0.2% m/m, the lowest since August 2023 and, before that, January 2021. Both measures of wage inflation moderated further to 4.1% y/y and 4.2% y/y, respectively. Both mark the lowest levels since June 2021.

Figure 1: US Small Businesses Labor Needs Seem To Be Waning



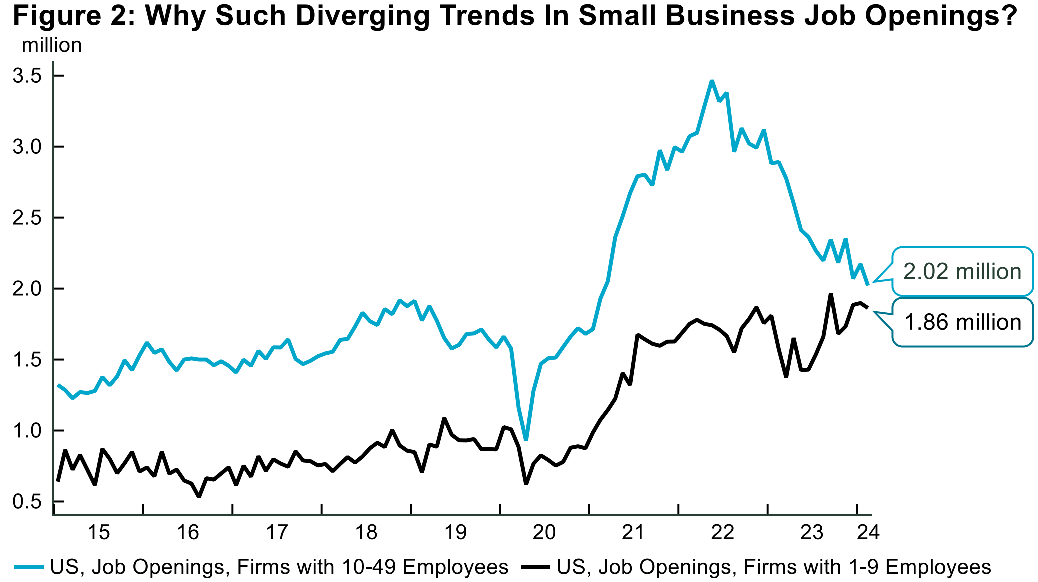
Sources: Macrobond, SSGA Economics, NFIB
Updated as of 4/5/2024

The fact that wage disinflation continues despite the robust pace of job creation we've seen lately underscores the idea that competition for workers has eased considerably. The dynamic is well aligned with signals from the NFIB survey showing that hiring intentions and the share of small businesses saying that the inability to find quality labor is their biggest problem have eased dramatically (Figure 1, page 1). It is less well aligned with still elevated job openings (more on that below), so the various labor market data sets continue to send contradictory messages. **Aggregate hours** jumped 0.5% m/m; in conjunction with pay increases, implying a solid month for labor income.

The **Jobs Opening and Labor Turnover Survey (JOLTS)** data has long told a story of a gently normalizing labor market, though one in which labor demand continues to exceed labor supply. There were 8.756 million open positions in February, little changed from January. This is down markedly from over 12 million in March 2022, but still about 1.5 million above 2019 levels. At the same time, 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.

Once we move beyond the headlines, the data is replete with contradictions. We have long highlighted how steady declines in openings at larger firms (50+ employees) contrast with persistently elevated openings at sub-50 employees firms. But there is a growing divergence even within the sub-50 employee universe, with openings at firms with 1-9 employees hovering near record highs while openings at firms with 10-49 employees are almost back to pre-Covid levels. One struggles to find an adequate explanation for such contrasting behavior at similarly sized firms. Even if small firms may have shrunk further in recent years, perhaps falling below the 10-person threshold and boosting openings in the 1-9 segment, it is unlikely that this can explain the difference, especially since the 10-49 bucket should then also benefit from some entrants from the tier immediately above it.

Figure 2: Why Such Diverging Trends In Small Business Job Openings?



Sources: Macrobond, SSGA Economics, BLS
Updated as of 4/5/2024

This is not the only blatant oddity. We are also struck by the renewed upturn in healthcare and social assistance job openings, as well as huge volatility in the financial activities segment.

The **manufacturing ISM** came in a bit stronger than expected in March, while the **non-manufacturing ISM** was a little weaker than expected. Neither should be made too much of. Rather, we see both confirming trends already in place: a gentle bottoming out of manufacturing activity following more than a year of contraction, and a gentle downtrend in non-manufacturing activity as consumer demand normalizes after the initial re-opening burst higher. The manufacturing ISM rose 2.5 points to 50.3—the first expansionary reading since late 2022—as production jumped. However, that jump in production follows a weak reading the month before, so we doubt that the underlying improvement was quite as robust. Indeed, employment continued to contract, and pricing metrics were steady. On the non-manufacturing side, the headline index retreated 1.2 points to 51.4, but this was only a three-month low. At odds with this was the further uptick in the business activity metric, which improved incrementally to 57.4. Employment contracted again, however. The price metric drew most attention as it dipped to a four-year low of 53.4, but we would caution against reading too much into this. Instead, this pullback should probably be best seen as a pullback following the January surge in the price metric. If, as we suspect, there is an element of start-of-year price hikes reflected in this data, that showed up in January, faded in February, and disappeared by March. Still, perhaps an encouraging signal for the next inflation report.

Canada

The labor market lost momentum in March. The **unemployment rate** rose more than expected to 6.1%, up from 5.7% in February. This is also the highest level since January 2022. There was little change in employment in March (-2.2k) with part-time jobs down by 1.6k. Wage growth inched up a tenth to 5.0% y/y.

UK

Manufacturing returned to growth in March, with modest increases in new orders and output. Final readings of **manufacturing PMI index** posted 50.3 in March, above flash estimate of 49.9 and up from 47.5 in previous month. Employment and purchasing activity continued to decline but the rates of contraction slowed sharply. Business sentiment hit an 11-month high.

The service sector expansion slowed in March. The final reading of **the services PMI inde**x inched down by 0.7 percentage points to 53.1. Employment increased marginally during the period. Input prices continued to accelerate while prices charged by service providers rose at the slowest pace since September 2023.

The effect of high interest rates on the housing market continues to fade. **Mortgage approvals** increased to a 17-month high of 60,4k in February. Net approvals for remortgaging also rose from 30,9k to 37,7k. The amount of net lending secured by dwellings increased to £1.5 billion, compared to £1.1 billion of net repayments in January. Meanwhile, the **Nationwide house price index** edged down 0.2% m/m in March, bucking expectations of an increase of 0.3% m/m. Nevertheless, in annual terms, the growth rate rose to 1.6% y/y, up from 1.2% y/y in February.

Figure 3: UK House Prices Rising Again

Sources: Macrobond, SSGA Economics, Nationwide
Updated as of 4/5/2024

Eurozone

Eurozone manufacturing continued to contract, with regional **manufacturing PMI** falling from 46.5 in February to a three-month low of 46.1 in March, driven by movements in suppliers' delivery times and stocks of purchases. Meanwhile, the decline in new orders and output further eased and delivery times improved markedly. Italy and Spain manufacturing indices picked up during the period while Germany and France's underperformance continued.

The **eurozone services PMI** increased more than expected by 1.3 percentage points to 9-month high of 51.5 in March, marking the second consecutive expansion. New business resumed growth for the first time in nine months. Employment slowed but remained above its survey average. Input cost inflation fell to an 8-month low although the pace of increase remained steep. Similarly, output charges rose at their slowest pace since last November. Germany services PMI index registered at 50.1, up from 48.3 in February.

Japan

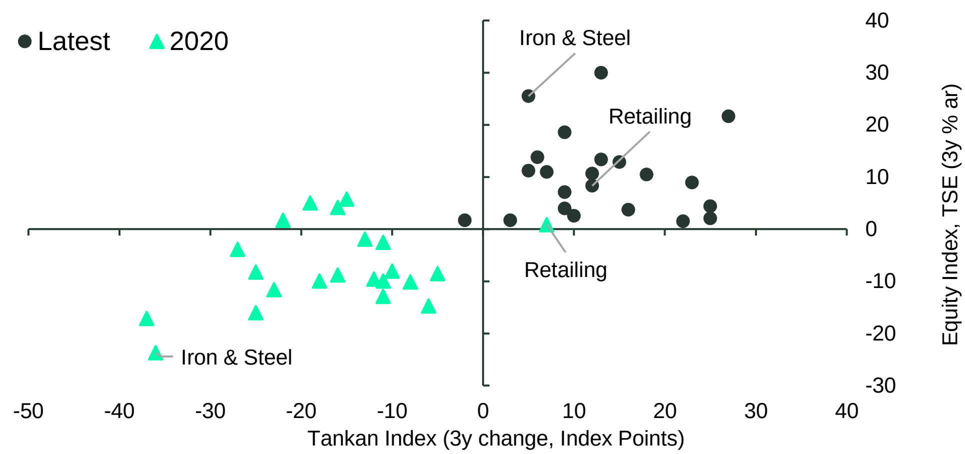
Our latest outlook on the BoJ and investment implications can be found here.

Japan's macro environment in rapidly evolving rapidly; Bank of Japan (BoJ) Governor Kazuo Ueda in an interview with Asahi Shimbun noted that the results of the high *shunto* negotiations will lift actual wages and subsequently reflect in higher inflation through autumn this year. While this is largely in line with our outlook, we were pleasantly surprised with the governor's conviction, as he said the likelihood of achieving the 2% inflation target will **increase rapidly**. Noteworthy that Governor Ueda admitted downside risks to growth in Q1, which was why we maintained our 2024 growth forecast of 1.0%. He also said that if the yen continues to weaken and impact the wage-price cycle, it **would be a reason to respond with monetary policy**. We sense that the BoJ will adjust its policy tools to contain excess moves in the yen. This has a direct impact from pushback against rate cut expectations in the US. The BoJ's communications are shifting gears into hawkishness, so we see upside risks to our BoJ outlook.

The BoJ's **Consumption Activity Index** rose 0.6% m/m after a downwardly revised -0.1% January. Nondurable goods consumption rose strongly at 2.3% m/m and was offset by a decline of 0.6% in durable goods. This data highlights that consumption remained weak in the first two months of 2024. However, much like the BoJ, we expect a recovery in the later part of the year. We are also encouraged with the **Composite Leading Indicator** hitting an 18-month high of 112.9 in February.

Business sentiment in the services sector climbed to a 33-year high in Q1, as reflected in the Q1 Tankan survey, in line with our expectation that services will support the next leg in inflation and growth in Japan. The business conditions index at large non-manufacturers rose two points to 34.0. Information services performed the best among all sectors, consistent with a large rise in software investments recorded in the MoF's capital expenditures data for Q4 2023. Furthermore, sentiment in the real estate and accommodations sectors also remained robust. Otherwise, the Manufacturing DI worsened two points to eleven, as the auto sector declined notably due to temporary disruptions earlier in the year. Nonetheless, there is a notable improvement in industry-wise sentiment, as well as their corresponding performance in the equity market in the last 3 years.

Figure 4: Tankan vs Equity Performance



Note: The data matches sentiment in the Tankan survey with the TSE's industry wise indices. Few names are not exactly the same,so they were matched individually

Source: SSGA Economics, BoJ, TSE, Macrobond

Finally, the Bank of Japan's (BoJ) estimated **output gap** closed out in Q4 2023, indicating that the economy is now at its potential for the first time in 15 quarters, in line with our long-standing forecasts. The output gap stood at 0.02%, an improvement from last quarter's -0.37%.

Australia

For the first time in two years, the **Reserve Bank of Australia (RBA)** did not discuss a rate hike at their last meeting, according to the March meeting minutes. Forward guidance also softened, as risks 'had become a little more even' and as underlying inflation 'continued to moderate'. We still expect the first rate cut from the RBA either in August (70%) or September (30%).

The RBA changed its monetary policy framework by endorsing an 'ample reserves' system in which the supply for reserves will move in line with the demand from the financial system, as opposed to the 'scarce' or the (current) 'excess' reserves system. This system will allow the bank to decrease its bond holdings by more (even though QT remains passive for now) and correct any shortage in liquidity by increasing repo operations. So, the composition of its balance sheet will change eventually while the size stabilizes due to QT. Currently, the BoE, ECB and Riksbank have similar frameworks in place. The full details are yet to be announced by the RBA.

Separately, **building approvals** declined for a third month in February by 1.9% m/m. Private sector apartment approvals dropped 24.9% and are currently at their lowest level since January 2012. It is quite a risk that approvals and construction is meager in an economy that saw a record surge in demographics. Property prices tracked by Proptrack have risen 6.8% y/y; expensive mortgage rates on expensive properties are weighing on the economy.

Figure 5: Australian Housing Sector

Sources: SSGA Economics, ABS, PropTrack, Macrobond
Updated as of 4/5/2024

Week in Review (Apr 01 –Apr 05)

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, Apr 01					
US	ISM Manufacturing (Mar)	48.3	50.3	47.8	First expansion since late 2022.
JN	Tankan Big Manufacturing Index (Q1)	10.0	11.0	13.0 (↑)	Huge improvement in non-manufacturing.
JN	Services PMI (Mar, final)	54.9 (p)	54.1	52.9	Very good.
Tuesday, Apr 02					
US	Wards Total Vehicle Sales (Mar, mil)	15.85	15.49	15.81	Moving in tight range.
US	Durable Goods Orders (Feb, m/m, final)	1.4% (p)	1.3%	-6.9%	Up 4.5% y/y.
US	Factory Orders (Feb, m/m)	1.0%	1.4%	-3.8% (↓)	Up 1.0% y/y.
US	JOLTS Job Openings (Feb, thous)	8,730	8,756	8,748 (↑)	Lots of contradictions in the data details.
UK	National House PX (Mar, m/m)	0.3%	-0.2%	0.7%	Disappointing.
UK	Manufacturing PMI (Mar, final)	49.9 (p)	50.3	47.5	Good.
UK	Mortgage Approvals (Feb, thous)	56.5	60.4	56.1 (↑)	Good.
EC	Manufacturing PMI (Mar, final)	45.7 (p)	46.1	46.5	Weak.
GE	Manufacturing PMI (Mar, final)	41.6 (p)	41.9	42.5	Weak.
GE	CPI (Mar, y/y, prelim)	2.2%	2.2%	2.5%	In line with expectations.
FR	Manufacturing PMI (Mar, final)	45.8 (p)	46.2	47.1	Weak.
IT	Manufacturing PMI (Mar, final)	48.8 (p)	50.4	48.7	Encouraging!
Wednesday, Apr 03					
US	ISM Services Index (Mar)	52.8	51.4	52.6	Employment contracted again; prices paid eased.
IT	Unemployment Rate (Feb)	7.2%	7.5%	7.3% (↑)	Has it bottomed?
Thursday, Apr 04					
US	Initial Jobless Claims (Mar 30, thous)	214	221	212 (↑)	Still very low.
US	Continuing Claims (Mar 23, thous)	1,810	1,781	1,819	Very low.
UK	Services PMI (Mar, final)	53.4 (p)	53.1	53.8	Expanding but at slower rate.
EC	Services PMI (Mar, final)	51.1 (p)	51.5	50.2	Encouraging!
GE	Services PMI (Mar, final)	49.8 (p)	50.1	48.3	Encouraging!
AU	Building Approvals (Feb, m/m)	3.3%	-1.9%	-2.5% (↓)	Housing market is the biggest concern.
Friday, Apr 05					
US	Change in Nonfarm Payrolls (Mar, thous)	214	303	270(↓)	Another very strong report!
US	Unemployment Rate (Mar)	3.8%	3.8%	3.9%	Participation rate increased.
US	Consumer Credit (Feb, $ bn)	16.40	14.12	17.68	Up just 2.5% y/y.
CA	Unemployment Rate (Mar)	5.9%	6.1%	5.8%	Highest in more than 2 years.
GE	Factory Orders (Feb, m/m)	0.7%	0.2%	-11.4% (↓)	Weak.
FR	Industrial Production (Feb, m/m)	0.4%	0.2%	-1.1%	Downside surprise.
JN	Leading Index CI (Feb, prelim)	111.6	111.8	109.5	Highest in 18 months!

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

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- Build from breadth
- Invest as stewards
- Invent the future

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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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