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MONDAY ECONOMIC REPORT

Manufacturing Wages and Salaries Rose a Record 4.9% Year-Over-Year in Q1

By Chad Moutray – May 2, 2022

The Weekly Toplines

- Private manufacturing wages and salaries jumped 1.5% in the first quarter. That increase translated into 4.9% growth over the past 12 months, the fastest pace in the history of the data series, which dates to the beginning of 2001.
- The U.S. economy shrank 1.4% at the annual rate in the first quarter, contracting for the first time since the second quarter of 2020. However, the data suggest some underlying strength in the U.S. economy that might not be obvious in the headline number.
- If one were to only include personal consumption expenditures and fixed investment, for instance, real GDP growth would have been 3.1% at the annual rate in the first quarter. The continued reopening of the economy and pent-up demand, especially in the service sector, remain encouraging. Yet, other factors—including government spending, inventories and net exports—were simply enough to outweigh those positives.
- Overall, the current forecast is for 3.0% growth in real GDP in 2022, suggesting that the economy should rebound in the coming quarters but also reflecting a reduced outlook for growth stemming from the Russian invasion of Ukraine and higher inflation. There also continues to be downside risks in the outlook with notable uncertainties related to the situation in Ukraine and attempts to slow pricing pressures.
- The personal consumption expenditures deflator rose 0.9% in March, the fastest monthly gain since January 2021. Food and energy prices increased 1.4% and 11.8%, respectively. Excluding food and energy prices, the PCE deflator increased 0.3% in March, the same pace as in February.

- Overall, the PCE deflator has risen 6.6% year-over-year, the greatest increase since January 1982. Core inflation has increased 5.2% over the past 12 months, pulling back from 5.3% growth in February, which was the strongest pace of inflation since April 1983.

- These data will put continued pressure on the Federal Reserve to tackle inflation. The Federal Open Market Committee is likely to increase the federal funds rate by 50 basis points at this week’s meeting, building on the 25 basis-point hike at its March 15–16 meeting. Another 25 or 50 basis-point increase is anticipated at the June 14–15 meeting. The Federal Reserve will also start reducing its balance sheet, with an announcement likely coming at this week’s meeting, as well.

- New orders for durable goods rose 0.8% March, but defense and nondefense aircraft and parts sales, which can be highly volatile from month to month, both decreased sharply. Motor vehicles and parts orders rebounded, up 5.0% in March. Excluding transportation equipment, new durable goods orders increased 1.1% to a record $191.3 billion in March.

- Core capital goods (or nondefense capital goods excluding aircraft)—a proxy for capital spendthiring in the U.S. economy—rose 1.0% from $80.0 billion in February to a record $80.8 billion in March, with 10.2% growth year-over-year.

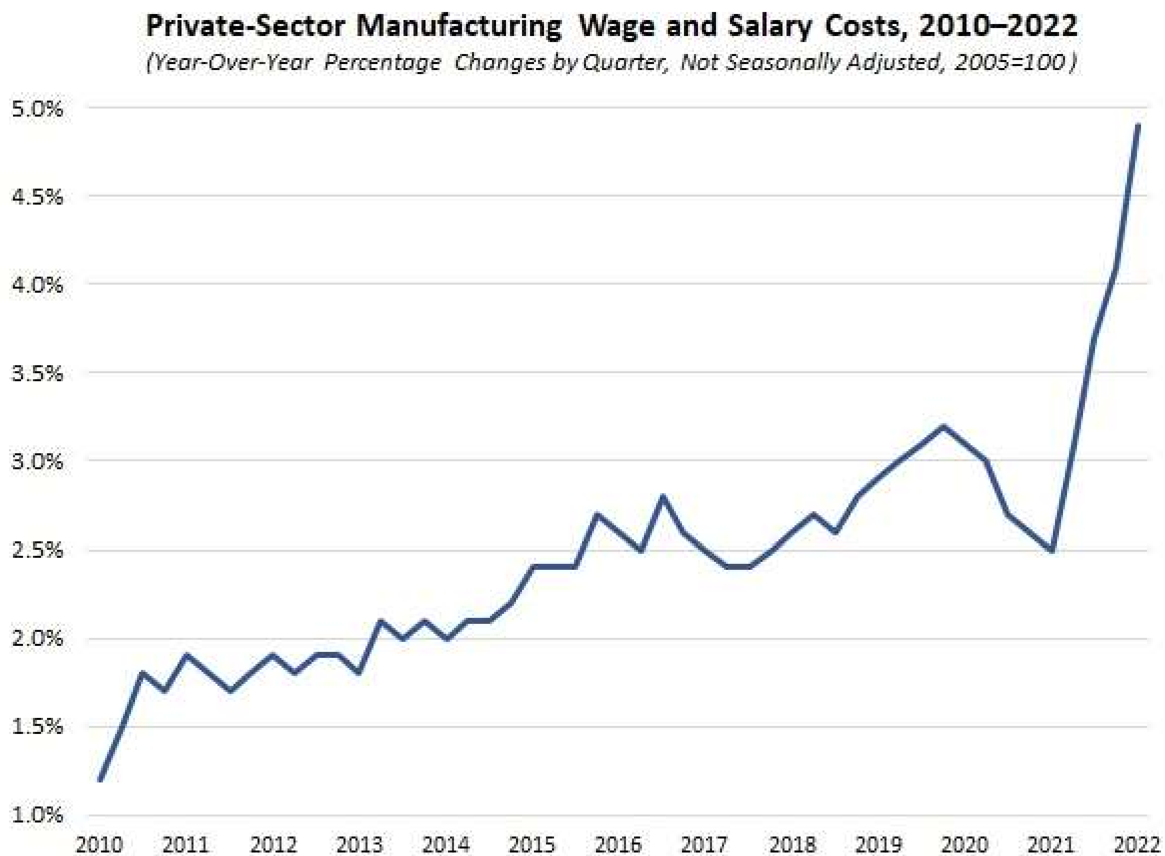
- As with other indicators, these data continue to illustrate the resilience of the manufacturing sector in the face of significant challenges with supply chain bottlenecks, worker shortages, soaring costs and COVID-19.

- The three manufacturing sentiment surveys out last week from the Dallas, Kansas City and Richmond Federal Reserve Banks provided mixed results but with expanding activity in each. Pricing pressures remained elevated, but respondents remained positive in their outlook.

- The U.S. goods trade deficit soared from $106.35 billion in February to a record $125.32 billion in March, according to preliminary figures. These data continued to be skewed by supply chain disruptions, higher petroleum prices and stronger economic growth in the U.S. relative to other markets.

- In March, goods imports jumped from $264.29 billion to $294.63 billion, an all-time high, which outpaced the increase for goods exports, up from $157.95 billion to a record $169.31 billion.

- New single-family home sales tumbled 8.6% from 835,000 units at the annual rate in February to 763,000 units in March, a four-month low. Affordability issues, higher mortgage rates, supply chain problems and workforce shortages continued to challenge the housing market.



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

This Week's Indicators:

Monday, May 2

Monday, April 25
Chicago Fed National Activity Index
Dallas Fed Manufacturing Survey

Tuesday, April 26
Conference Board Consumer Confidence
Durable Goods Orders and Shipments
New Home Sales
Richmond Fed Manufacturing Survey

Wednesday, April 27
Business Employment Dynamics
International Trade in Goods (Preliminary)

Thursday, April 28
Gross Domestic Product
Kansas City Fed Manufacturing Survey
Weekly Initial Unemployment Claims

Friday, April 29
Employment Cost Index
Personal Consumption Expenditures Deflator
Personal Income and Spending
University of Michigan Consumer Sentiment (Revision)

Construction Spending
ISM® Manufacturing Purchasing Managers' Index®

Tuesday, May 3
Factory Orders and Shipments
Job Openings and Labor Turnover Survey

Wednesday, May 4
ADP National Employment Report
FOMC Monetary Policy Statement
International Trade Report

Thursday, May 5
Productivity and Costs
Weekly Initial Unemployment Claims

Friday, May 6
BLS National Employment Report

A Message from Bain & Company

Beyond the Machine: The Industry's Next Act
From investing in automation to retooling for sustainability, machinery and equipment companies have set bold transformation agendas. How will you address the forces at play?

Deeper Dive

- **Business Employment Dynamics:** Manufacturing experienced a net increase of 56,000 jobs in the third quarter of 2021, bouncing back from the decline of 29,000 in the second quarter. Manufacturers saw gross job gains of 480,000 in the third quarter of 2021, with 431,000 from expanding establishments and 49,000 from new establishments. At the same time, gross job losses totaled 424,000 in the third quarter, with 366,000 from contracting establishments and 58,000 from closing establishments.

  In addition, the Bureau of Labor Statistics reported the formation of 8,000 manufacturing start-ups in the third quarter of 2021, the strongest figure since the first quarter of 2000. The start-up rate represented 2.2% of all establishments in the sector. Those new establishments (or "births") employed 29,000 workers in the third quarter, up from 27,000 in the previous quarter and the best reading since the second quarter of 2008.

- **Chicago Fed National Activity Index**: The National Activity Index slipped somewhat from 0.54 in February to 0.44 in March but remained solid. The three-month moving average rose from 0.43 to 0.57. Positive index readings suggest that the U.S. economy is growing above trend. As such, the three-month moving average suggests that the national economy continues to expand despite ongoing challenges with supply chain disruptions, workforce shortages, soaring costs and COVID-19.

  Manufacturing production rose 0.9% in March, showing the resilience of the sector and building on the 1.2% gain in February. Indeed, manufacturing capacity utilization jumped to 78.7% in March, the highest reading since December 2007. Overall, manufacturing production has risen 3.9% post-pandemic. With that in mind, production-related indicators added 0.27 to the NAI in March. In addition, employment-related indicators contributed 0.16 to the headline index in March, but personal consumption and housing subtracted 0.04.

- **Conference Board Consumer Confidence**: Consumer confidence ticked down from 107.6 in March to 107.3 in April, according to the Conference Board. Americans remained anxious in their assessments of the current economic environment, likely on inflation concerns and on uncertainties surrounding the Russian invasion of Ukraine, but expectations for future conditions improved somewhat in April. The percentage of respondents suggesting that business conditions were "good" increased from 19.6% to 20.8%, while the percentage feeling that conditions were "bad" inched up from 21.4% to 21.9%. At the same time, the percentage of respondents suggesting jobs were "plentiful" declined from 56.7% to 55.2%, while those saying jobs were "hard to get" increased from 9.6% to 10.6%.

  Regarding the outlook, the percentage of consumers anticipating better business conditions over the next six months declined from 19.0% to 18.1%, while those predicting a worsening of conditions dropped from 24.1% to 21.8%. Meanwhile, the percentage of respondents expecting more jobs in the next six months edged down from 17.6% to 17.4%, while those expecting fewer jobs rose from 18.0% to 18.9%. In addition, 16.5% of consumers predicted higher incomes in the months ahead, up from 15.1%, while the percentage anticipating reduced incomes ticked up from 13.7% to 13.8%.

- **Dallas Fed Manufacturing Survey**: Manufacturing activity decelerated, with the composite index of general business conditions falling from 8.7 in March to 1.1 in April, the slowest pace of growth since July 2020. Despite some slippage in sentiment, the underlying data provided mixed results. Growth in new orders and shipments improved, but production, capacity utilization, employment, hours worked and capital spending each softened somewhat. The increase in wages remained very strong, even as the index pulled back from a record high in March. The sample comments noted challenges with supply chain disruptions, long delivery times, the conflict in Ukraine, workforce shortages and inflation.

Looking ahead, manufacturers in the Texas district expressed cautious optimism in their outlook for the next six months. The forward-looking composite measure dropped from 8.2 to 1.8, the lowest reading since May 2020.

- **Durable Goods Orders and Shipments:** New orders for durable goods rose 0.8% from $272.7 billion in February to $275.0 billion in March. This was not far from the record level in January, which was $277.5 billion. Defense and nondefense aircraft and parts sales, which can be highly volatile from month to month, both decreased sharply in March. On the other hand, motor vehicles and parts orders rebounded from recent softness, up 5.0% in March. Excluding transportation equipment, new durable goods orders increased 1.1% from $189.2 billion in February to a record $191.3 billion in March. New orders have jumped 10.2% over the past 12 months, or 8.9% with transportation equipment excluded.

  In addition to motor vehicles and parts, demand increased in March for electrical equipment, appliances and components (up 3.9%), computers and electronic products (up 2.6%), primary metals (up 1.5%), fabricated metal products (up 0.8%), machinery (up 0.7%) and other durable goods (up 0.1%). Core capital goods (or nondefense capital goods excluding aircraft)—a proxy for capital spending in the U.S. economy—rose 1.0% from $80.0 billion in February to a record $80.8 billion in March, with 10.2% growth year-over-year.

  Meanwhile, durable goods shipments increased 1.2% from $270.9 billion in February to a record $274.2 billion in March. On a year-over-year basis, durable goods shipments have risen 10.8% since March 2021, or 11.6% excluding transportation equipment. In addition, core capital goods shipments edged up 0.2% from $79.5 billion to $79.7 billion, an all-time high, with 10.9% growth over the past 12 months.

  As with other indicators, these data continue to illustrate the resilience of the manufacturing sector in the face of significant challenges with supply chain bottlenecks, worker shortages, soaring costs and COVID-19.

- **Employment Cost Index:** Private manufacturing wages and salaries jumped 1.5% in the first quarter, extending the 1.0% growth in the fourth quarter. That increase translated into 4.9% growth over the past 12 months, the fastest pace in the history of the data series, which dates to the beginning of 2001. For all private-sector employees, wages and salaries increased 1.3% in the first quarter, with 5.0% growth year-over-year, the same record pace that was observed in the fourth quarter.

Benefits costs for manufacturing employees rose 2.5% in the first quarter. On a year-over-year basis, benefits have risen 5.0%, a rate not seen since the second quarter of 2011. Overall, total manufacturing compensation rose 1.8% for the first quarter, or 4.9% year-over-year, an all-time high.

- **Gross Domestic Product**: The U.S. economy shrank 1.4% at the annual rate in the first quarter, contracting for the first time since the second quarter of 2020. The decline stemmed from reduced government spending, inventories, net exports and nondurable goods spending, offsetting stronger data for durable goods purchases, service-sector consumer spending and fixed investment. The data reflect negative impacts from supply chain disruptions, the Russian invasion of Ukraine, slower global growth relative to the U.S., the spread of the omicron variant (earlier in the quarter) and inflation.

  Note that these data suggest some underlying strength in the U.S. economy that might not be obvious in the headline number. If one were to only include personal consumption expenditures and fixed investment, for instance, real GDP growth would have been 3.1% at the annual rate in the first quarter. The continued reopening of the economy and pent-up demand, especially in the service sector, remain encouraging. Yet, other factors—including government spending, inventories and net exports—were simply enough to outweigh those positives.

  Overall, the current forecast is for 3.0% growth in real GDP in 2022, suggesting that the economy should rebound in the coming quarters but also reflecting a reduced outlook for growth stemming from the Russian invasion of Ukraine and higher inflation. There also continues to be downside risks in the outlook with notable uncertainties related to the situation in Ukraine and attempts to slow pricing pressures.

  Here are the breakdowns of real GDP growth by the various components:
  - Personal consumption expenditures: Consumer spending rose 2.7% at the annual rate in the first quarter, buoyed by 4.1% and 4.3% growth in durable goods and service-sector spending. Nondurable goods purchases declined 2.5%, however, ending four quarters of growth. Real spending on gasoline and other energy goods provided the largest drag on purchases for nondurable goods, but purchases of apparel and food and beverages were also lower. Overall, personal spending added 1.83 percentage points to real GDP growth for the quarter—almost all of which came from services.
  - Gross private fixed investment: Nonresidential fixed investment jumped 9.2% at the annual rate in the first quarter, the strongest pace since the second quarter of last year, led by spending on equipment (up 15.3%) and intellectual property products (up 8.1%). Spending on structures declined for the fourth straight quarter, down 0.9%. At the same time, residential spending increased 2.1%. In

total, fixed investment contributed 1.27 percentage points to headline growth. Yet, businesses spent less on inventories, subtracting 0.84 percentage points from GDP for the quarter. As a result, gross private fixed investment only added 0.43 percentage points to top-line growth.

  - Net exports: With the U.S. economy faring better than other markets, net exports were the largest factor in pulling real GDP growth lower, subtracting 3.20 percentage points from headline growth. Goods exports fell 9.6% at the annual rate in the first quarter, but goods imports soared 20.5%.
  - Government spending: With fiscal stimulus waning, federal government spending has been a drag on real GDP growth for four consecutive quarters. Federal government spending declined 5.9% at the annual rate in the first quarter, with state and local government spending down 0.8%. In total, government spending subtracted 0.48 percentage points from real GDP growth in the latest data.

- **International Trade in Goods (Preliminary):** The U.S. goods trade deficit soared from $106.35 billion in February to a record $125.32 billion in March, according to preliminary figures. These data continued to be skewed by supply chain disruptions, higher petroleum prices and stronger economic growth in the U.S. relative to other markets. In March, goods imports jumped from $264.29 billion to $294.63 billion, an all-time high, which outpaced the increase for goods exports, up from $157.95 billion to a record $169.31 billion.

  Goods exports increased across the board, rising by $11.36 billion and led by strength in industrial supplies (up $7.35 billion) and automotive vehicles (up $1.02 billion), among other categories. Meanwhile, goods imports skyrocketed by $30.34 billion in March, with very sizable gains for consumer goods (up $9.91 billion), industrial supplies (up $9.76 billion), capital goods (up $5.30 billion), automotive vehicles (up $3.53 billion) and foods, feeds and beverages (up $1.03 billion). Final data, which will also include the service-sector trade surplus, will be released May 4.

- **Kansas City Fed Manufacturing Survey:** Manufacturing in the Kansas City Federal Reserve Bank’s district continued to expand solidly, albeit with the composite index of general business activity declining from an all-time high of 37 in March to 25 in April. New orders, exports, production, shipments and the average employee workweek eased in April, but employment strengthened a bit. The index for prices paid increased from 81 to 83, not far from the record rate in May 2021 (88). In their comments, manufacturers cited supply chain disruptions, soaring costs, workforce difficulties, the Ukrainian war and COVID-19 lockdowns in China as significant challenges.

Nonetheless, manufacturers in the district remained optimistic about growth over the next six months, even with the forward-looking composite index decreasing from a record 41 to 34. Pricing pressures are expected to remain highly elevated and near all-time highs.

- **New Home Sales**: New single-family home sales tumbled 8.6% from 835,000 units at the annual rate in February to 763,000 units in March, a four-month low, with sales lower in every region of the country. Overall, affordability issues, higher mortgage rates, supply chain problems and workforce shortages continued to challenge the housing market. Indeed, single-family home sales have fallen 12.6% over the past 12 months, down from 873,000 units in March 2021.

  The supply of new single-family homes for sale on the market jumped from 5.6 months in February to 6.4 months in March, the highest since August. The median sales price for new homes was $436,700 in March, a new record and up 21.4% year-over-year from $359,600 one year ago.

- **Personal Consumption Expenditures Deflator**: The PCE deflator rose 0.9% in March, the fastest monthly gain since January 2021. In March, food and energy prices increased 1.4% and 11.8%, respectively. Excluding food and energy prices, the PCE deflator increased 0.3% in March, the same pace as in February. Overall, the PCE deflator has risen 6.6% year-over-year, the greatest increase since January 1982. Core inflation has increased 5.2% over the past 12 months, pulling back from 5.3% growth in February, which was the strongest pace of inflation since April 1983.

  Rising raw material costs continued to be a major concern for manufacturers, especially with supply chain disruptions, labor market tightness and soaring pent-up demand in the marketplace. The Russian invasion of Ukraine has accelerated those cost pressures. With that said, it is notable that core inflation eased in March, consistent with expectations. The current outlook is for the core PCE deflator to stabilize around 3.5% by year’s end.

  These data will put continued pressure on the Federal Reserve to tackle inflation. The Federal Open Market Committee is likely to increase the federal funds rate by 50 basis points at this week’s meeting, building on the 25 basis-point hike at its March 15–16 meeting. Another 25 or 50 basis-point increase is anticipated at the June 14–15 meeting. The Federal Reserve will also start reducing its balance sheet, with an announcement likely coming at this week’s meeting, as well.

- **Personal Income and Spending**: Personal income rose 0.5% in March, extending the solid 0.7% gain in February. Wages and salaries increased 0.6% for the month, including for manufacturers. More importantly, total wages and salaries in the economy have soared 11.7% over the past 12 months, with manufacturing wages and salaries rising 6.7% year-over-year to $1,018.7 billion in March.

Meanwhile, personal consumption expenditures jumped 1.1% in March, led by increased spending on nondurable goods and services, up 2.5% and 1.1%, respectively. Spending on durable goods fell 1.0% in March, however. Personal spending rose 9.1% year-over-year, with nondurable goods and service-sector spending up 9.9% and 11.1%, respectively, over the past 12 months. Durable goods purchases have declined 1.6% since March 2021.

With spending growth outpacing income, the personal saving rate fell from 6.8% to 6.2%, the lowest since December 2013.

- **Richmond Fed Manufacturing Survey:** Manufacturing activity continued to expand solidly despite numerous challenges, according to the Richmond Federal Reserve Bank. The composite index of general business activity edged up from 13 in March to 14 in April, a four-month high. The underlying data provided mixed results. Shipments, capacity utilization and wages strengthened in April, but new orders, employment and capital expenditures softened somewhat. Supply chain challenges continue to persist, with long vendor lead times and reduced inventories (albeit with slight progress in both). Meanwhile, manufacturers remained positive in their outlook for the next six months. The labor market is predicted to remain very tight, with employment and wage growth expected to increase at elevated rates moving forward.

  Inflation remained a significant challenge. Costs for raw materials soared 11.83% in April, with the prices received for goods and services rising 8.93%. In addition, respondents anticipated an annualized 6.09% increase in costs six months from now, with the expected prices received increasing 5.29%.

- **University of Michigan Consumer Sentiment (Revision):** The Index of Consumer Sentiment jumped from 59.4 in March, the lowest reading since August 2011, to 65.2 in April, according to revised data from the University of Michigan and Thomson Reuters. That was slightly lower than the prior estimate, which was 65.7. The higher April reading stemmed largely from improved economic expectations, likely driven by strong labor market and wage gains. With that said, consumer sentiment remained lower than desired, with Americans continuing to worry about inflation and with lingering uncertainties related to the Russian invasion of Ukraine.

- **Weekly Initial Unemployment Claims:** The week ending April 23 saw 180,000 initial unemployment claims, edging down from 185,000 for the week ending April 16. At the same time, the week ending April 16 saw 1,408,000 continuing claims, inching down from 1,409,000 for the week ending April 9 and the lowest level since the week ending Feb. 7, 1970. Overall, these data continued to reflect a labor market that has improved significantly across the past year.

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