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# MONDAY ECONOMIC REPORT

Essential Takes on Leading Economic Indicators

By Chad Moutray, Ph.D., CBE – August 5, 2019 – SHARE

## The Federal Reserve Cuts Interest Rates for the First Time Since 2008

### The Weekly Toplines

- As widely expected, the Federal Open Market Committee voted to reduce the federal funds rate by 25 basis points after its July 30–31 meeting, marking the first cut in interest rates since the financial crisis in 2008. The Federal Reserve said it was taking this action to help keep the economic expansion going—an "insurance policy" against slower growth. There are also expectations that the Federal Reserve might do another cut in rates at its next meeting. In addition, the Federal Reserve will stop reducing the size of its balance sheet.

- Despite the FOMC's action, participants continued to cite strength in the labor market and in consumer spending. Yet, the cut in short-term rates was spurred by softening manufacturing activity, weak business fixed investment, continuing uncertainties in the economic outlook (including from trade) and core inflation that was below the Federal Reserve's target of 2 percent.

- Financial markets were rattled at the end of last week by President Donald Trump's announcement of new tariffs on Chinese goods on September 1. This could raise prices for more consumer goods and darken the outlook, particularly as it relates to business spending. For his part, NAM President and CEO Jay Timmons once again urged the administration and Chinese officials to reach an agreement quickly.

- The ISM® Manufacturing Purchasing Managers' Index® expanded at the slowest pace since August 2016 in July, down from 51.7 in June to 51.2 in July, largely on softer production and employment growth and declining exports. While the manufacturing sector has now expanded for 35 straight months, there has been notable slippage in activity and the outlook since then. At the same time, the Dallas Federal Reserve Bank noted declining sentiment for the third straight month despite still-expanding new orders and production and a relatively upbeat outlook.

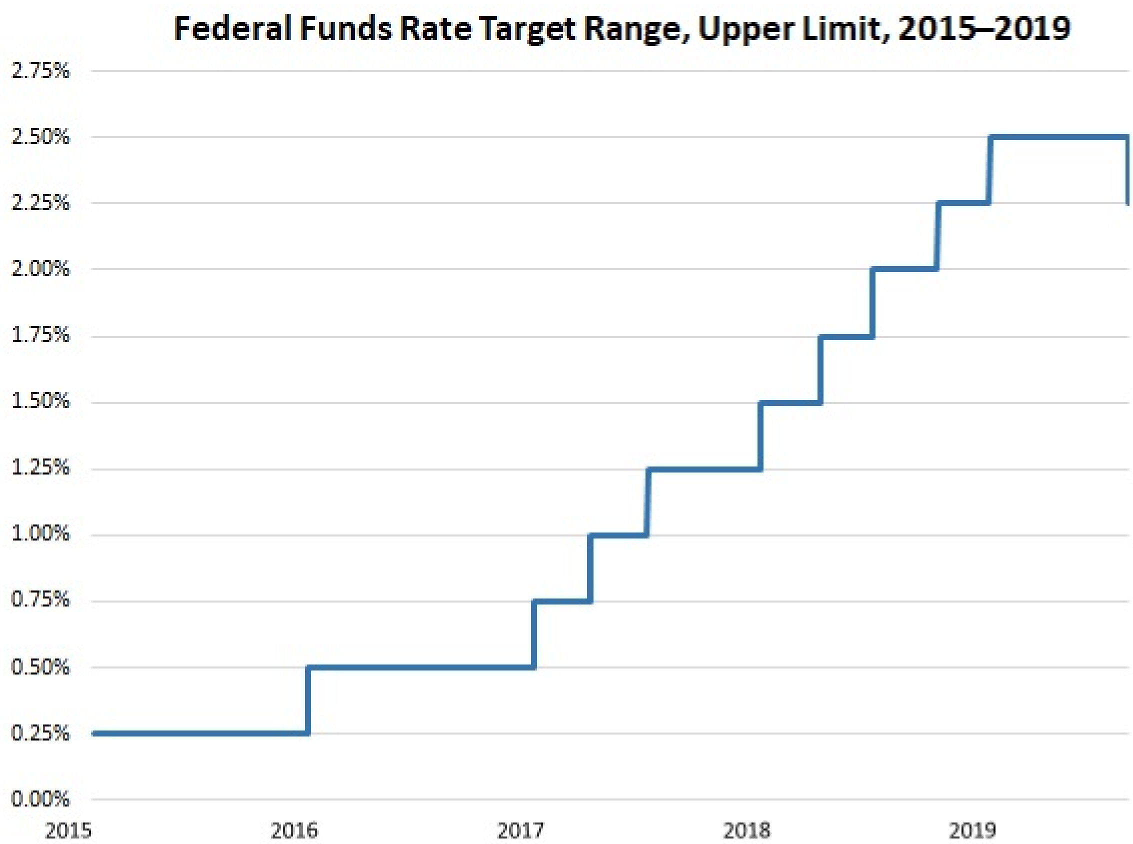
- After falling in April and May, new orders for manufactured goods rebounded in June, but continued to highlight weaknesses in the sector. New factory orders have fallen 1.2 percent since June 2018, edging down 0.1 percent with transportation equipment excluded. More positively, core capital goods spending has risen a modest 1.5 percent year-over-year.

- Manufacturing employment rose by 16,000 workers in July, but job growth has slowed considerably this year. The sector has averaged nearly 8,000 new workers per month so far in 2019 relative to the more robust average of almost 22,000 per month in 2018. Nonetheless, the average hourly earnings for production and nonsupervisory workers has risen 3.3 percent over the past 12 months, even as the average workweek narrowed to the lowest level since January 2014.

- Overall, the U.S. economy added 164,000 workers in July, with job growth also softening so far in 2019. The unemployment rate remained at 3.7 percent, near 50-year lows, and the so-called “real unemployment” rate fell to 7.0 percent, a rate not seen since December 2000.

- Encouragingly, personal income increased strongly, up 0.4 percent in June for the fourth consecutive month. Over the past 12 months, personal income has risen a healthy 4.9 percent, with manufacturing wages and salaries up a robust 5.1 percent since June 2018. Personal spending rose 0.3 percent in June, slowing from a gain of 0.5 percent in May but continuing to be a healthy figure.

- Consumer confidence rebounded, up from 124.3 in June to 135.7 in July, the strongest reading since November, according to the Conference Board. Americans felt more upbeat about both current and future economic conditions, particularly regarding jobs and income. The University of Michigan and Thomson Reuters’ measure of consumer sentiment also inched higher in July, remaining rather elevated “despite ongoing trade uncertainties.”




## Economic Indicators

**Last Week's Indicators:**
(Summaries Appear Below)

**Monday, July 29**
*Dallas Fed Manufacturing Survey*

**Tuesday, July 30**
*Conference Board Consumer Confidence*
*Personal Consumption Expenditures Deflator*
*Personal Income and Spending*

**Wednesday, July 31**
*ADP National Employment Report*
*Employment Cost Index*
*FOMC Monetary Policy Statement*

**Thursday, August 1**
*Construction Spending*
*ISM® Manufacturing Purchasing Managers' Index®*

**This Week's Indicators:**

**Monday, August 5**
*None*

**Tuesday, August 6**
*Job Openings and Labor Turnover Survey*

**Wednesday, August 7**
*Consumer Credit*

**Thursday, August 8**
*None*

**Friday, August 9**
*Producer Price Index*

**Friday, August 2**
*BLS National Employment Report*
*Factory Orders and Shipments*
*International Trade Report*
*University of Michigan Consumer Sentiment (Revised)*

## Deeper Dive

- **ADP National Employment Report:** Manufacturing employment edged up by 1,000 workers in July, increasing for the fourth straight month, according to ADP estimates. With that said, the sector has seen nearly 2,400 additional employees per month since February, which stands in sharp contrast to the more robust roughly 18,200 monthly average over the prior 14 months (January 2018 to February 2019). This shows how much hiring has softened recently due to slowing global growth and trade uncertainties.

  Meanwhile, total nonfarm private employment rose by 156,000 in July, improving from 112,000 in June. The largest gains occurred in professional and business services (up 44,000), education and health services (up 37,000), leisure and hospitality (up 26,000), construction (up 15,000) and financial activities (up 11,000). Using the time frames discussed above, private sector payroll growth has averaged just more than 145,000 over the past five months, slowing from almost 222,000 per month over the previous 14 months.

  In addition, the smallest companies with fewer than 20 employees have experienced declining employment for three consecutive months, down by 18,000 in July. Medium and large businesses with 50 employees or more generated 92.9 percent of the net job creation in July.

- **BLS National Employment Report:** Manufacturing employment rose by 16,000 workers in July, extending the gain of 12,000 in June. The data for the prior two months were revised lower, subtracting a total of 6,000 from May and June job growth in the sector. In July, job growth was buoyed by additional hiring from chemicals, computer and electronic products, furniture and related products and motor vehicles and parts, among others. In contrast, sectors with declining employment in July included machinery, printing and related support activities and primary metals.

  Despite the solid employment increases in the latest report, it is clear that manufacturing job growth has slowed considerably this year versus last, with the sector averaging nearly 8,000 new workers per month so far in 2019 relative to the more robust average of almost 22,000 per month in 2018. This mirrors other data, including production and sentiment data, which show manufacturing activity slowing as a result of weaker global growth and ongoing trade uncertainties.

With that said, there were 12,864,000 employees in manufacturing in July, the most since November 2008. In addition, firms continue to cite difficulty in obtaining talent as a top concern, with record-high levels of job openings.

In the larger economy, nonfarm payrolls increased by 164,000 in July, which was mostly in line with expectations but down from a revised 193,000 in June. Much like the manufacturing data, nonfarm payrolls have slowed year to date, down from an average of 223,250 jobs created in 2018 to just more than 165,000 per month through the first seven months of 2019. Meanwhile, the unemployment rate remained at 3.7 percent, near 50-year lows, and the so-called "real unemployment" rate fell to 7.0 percent, a rate not seen since December 2000.

Beyond hiring, the average workweek of production and nonsupervisory workers slowed to 41.5 hours in July, the lowest level since January 2014. Nonetheless, the average hourly earnings for production and nonsupervisory workers rose to $22.16 in July, up from $21.46 per hour in July 2018 and up 3.3 percent year-over-year.

- **Conference Board Consumer Confidence:** Consumer sentiment rebounded, up from 124.3 in June to 135.7 in July, the strongest reading since November. Americans felt more upbeat about both current and future economic conditions, with strength in expectations for labor market and income growth. In the latest data, the percentage of respondents suggesting that business conditions were "good" increased from 37.5 percent to 40.1 percent, but those noting that conditions were "bad" rose slightly from 10.6 percent to 11.2 percent. Moreover, the percentage of Americans feeling that jobs were "plentiful" increased from 44.0 percent to 46.2 percent, with those responding that jobs were "hard to get" dropping from 15.8 percent to 12.8 percent.

- **Construction Spending:** Private manufacturing construction spending rose 0.9 percent in the latest data, up from $70.28 billion at the annual rate in May to $70.91 billion in June. While this is down from March's pace ($72.26 billion), which was the strongest since December 2016, construction activity has shown a lot of progress across the past 12 months, with spending among manufacturers up a solid 10.5 percent since June 2018. Despite recent improvements, however, private manufacturing construction activity remains below the all-time high of $82.1 billion in May 2015.

  Meanwhile, total construction spending fell for the second straight month, down 1.3 percent in June. Private residential and nonresidential spending decreased 0.5 percent and 0.3 percent, respectively. Over the past 12 months, private nonresidential construction activity edged down 0.4 percent, with private residential construction decreasing by a sizable 8.1 percent. In addition, public sector construction dropped 3.7 percent in June, but with 6.1 percent growth year-over-year.

- **Dallas Fed Manufacturing Survey:** While manufacturing new orders and production continued to expand modestly in July, the composite index remained negative for the third straight month, albeit up from -12.1 in June to -6.3 in July. The sample comments suggest slowing global growth and trade uncertainties mainly caused this weakness. The good news was that many of the underlying measures improved slightly in July, including stronger employment and capital spending data, but firms continued to cite difficulties in finding talent. In addition, manufacturers in the Texas district remained positive about the next six months, with an expectation that new orders, production, shipments and employment will pick up moving forward.

- **Employment Cost Index:** Private manufacturing wages and salaries rose 0.7 percent in the second quarter, extending the 0.8 percent gain in the first quarter. That translated into 3.0 percent growth over the past 12 months, the fastest year-over-year pace of growth in 17 years. For all private-sector employees, wages and salaries rose 0.6 percent in the second quarter, with 3.0 percent growth year-over-year as well.

  Benefits costs for manufacturing employees increased 0.5 percent in the second quarter, slowing from a gain of 0.9 percent in the first quarter. On a year-over-year basis, benefits have risen a modest 1.0 percent. As a result, total manufacturing compensation increased 0.6 percent for the quarter, or 2.3 percent year-over-year.

- **Factory Orders and Shipments:** After falling in April and May, new orders for manufactured goods rebounded in June, up 0.6 percent. There was a very large increase in nondefense aircraft orders in June related to the Paris Air Show, but those figures are highly volatile from month to month. Motor vehicle sales rose 1.0 percent for the month. Excluding transportation equipment, factory orders edged up 0.1 percent in June after being unchanged in May, with durable goods demand up 1.9 percent but with sales of nondurable goods down 0.5 percent. Overall, the data continue to highlight weaknesses in the manufacturing sector across the past 12 months, with factory orders down 1.2 percent since June 2018. Excluding transportation equipment, factory orders inched down 0.1 percent year-over-year.

  Nonetheless, new orders for core capital goods (or nondefense capital goods excluding aircraft)—a proxy for capital spending in the U.S. economy—increased 1.5 percent in June, the best monthly reading in 11 months. On a year-over-year basis, core capital goods orders also rose 1.5 percent.

  Meanwhile, shipments increased 0.4 percent in June, improving from the 0.1 percent gain in May. Excluding transportation, factory shipments declined 0.2 percent for the month. Since June 2018, manufactured goods shipments have increased 1.0 percent, with core capital goods shipments up a modest 3.1 percent year-over-year to an all-time high ($70.2 billion).

- **FOMC Monetary Policy Statement:** As widely expected, the Federal Open Market Committee voted to reduce the federal funds rate by 25 basis points after its July 30–31 meeting, marking the first cut in interest rates since the financial crisis in 2008. The Federal Reserve said it was taking this action to help support a "sustained expansion of economic activity, strong labor market conditions and inflation near the Committee's symmetric 2 percent objective." In addition, the FOMC had pursued a path of gradually reducing the size of the Federal Reserve's balance sheet each month, and it voted to stop doing so. The balance sheet reduction strategy, however, has decreased the Federal Reserve's total assets from nearly $4.5 trillion to around $3.8 trillion across the past two years.

Despite the FOMC's action, participants continued to cite strength in the labor market and in consumer spending. Perhaps with that in mind, Boston Federal Reserve Bank President Eric Rosengren and Kansas City Federal Reserve Bank President Esther L. George both dissented, voting to keep rates unchanged. Those voting for the action, however, noted softening manufacturing activity, weak business fixed investment, continuing uncertainties in the economic outlook (including from trade) and core inflation that was below the Federal Reserve's target of 2 percent.

In essence, participants approved a decrease in short-term rates as an "insurance policy"—as it has been described by many analysts—against continued softening in the economic outlook. It is hoped that this reduction will help to stimulate growth, which has softened notably year to date. Moving forward, the FOMC will monitor incoming data to determine if it needs to further cut rates at either its September 17–18 or October 29–30 meetings.

- **International Trade Report:** The U.S. trade deficit edged slightly lower, down from $55.34 billion in May to $55.15 billion in June. In the latest figures, goods imports (down from $216.93 billion to $212.26 billion) fell by more than goods exports (down from $141.03 billion to $137.14 billion). For good exports, the largest declines occurred in automotive vehicles and parts, consumer goods and nonautomotive capital goods. At the same time, all of the major categories declined in June for goods imports, led by sharp reductions for industrial supplies and materials. That was likely the result of decreases in petroleum imports, which fell from $19.35 billion in May to $16.65 billion in June.

  In non-seasonally adjusted data, U.S.-manufactured goods exports totaled $565.23 billion through the first six months of 2019, down 2.78 percent from $581.43 billion for the same period in 2018. This suggests that international demand for U.S.-manufactured goods has weakened in the first half of this year after experiencing better data in both 2017 and 2018.

- **ISM® Manufacturing Purchasing Managers' Index®:** The Institute for Supply Management reported that manufacturing activity expanded at the slowest pace since August 2016 in July. The composite index declined from 51.7 in June to 51.2 in July, largely on softer production and employment growth and declining exports. While the manufacturing sector has now expanded for 35 straight months, activity has decelerated each month so far in 2019 on slowing global growth and trade uncertainties. Indeed, one year ago, manufacturers were reporting solid growth in demand, output and hiring, with notable slippage in activity and the outlook since then. Overall inventories were also negative in July for the second consecutive month. This could necessitate higher production needs if demand strengthened, especially with customer stockpiles remaining very depleted and below ideal levels.

In addition, pricing pressures—a major concern among manufacturers at this time last year—have lessened substantially in recent months. In July, the index for prices dropped from 47.9 to 45.1, declining for the second straight month.

- **Personal Consumption Expenditures Deflator:** The PCE deflator inched up 0.1 percent in June, mirroring the pace in May. Reduced energy costs, down 2.3 percent in June, helped to keep a lid on pricing pressures. At the same time, the core PCE deflator, which excludes food and energy prices, rose 0.2 percent in June for the third straight month. Over the past 12 months, the PCE deflator has risen 1.4 percent, the same rate as in May but down from 2.4 percent year-over-year in June 2018. Core inflation has also decelerated, down from 2.0 percent year-over-year in June 2018 to 1.6 percent in the latest data. This measure remains below the Federal Reserve's stated goal of 2 percent core inflation.

  As such, the pricing data should provide some comfort to the Federal Open Market Committee, as it allows participants the luxury of being more "dovish" in setting monetary policy over the coming months, including at last week's meeting.

- **Personal Income and Spending**: Personal income increased strongly, up 0.4 percent in June for the fourth consecutive month. Over the past 12 months, personal income has risen a healthy 4.9 percent. In addition, manufacturing wages and salaries increased from $914.7 billion in May to $918.7 billion in June. That would indicate a robust 5.1 percent growth rate since June 2018, which was $874.0 billion.

  At the same time, personal consumption expenditures rose 0.3 percent in June, slowing from a gain of 0.5 percent in May but continuing to be a healthy figure. Durable and nondurable goods spending increased 0.4 percent and 0.2 percent, respectively, for the month. Moreover, personal spending has risen 3.9 percent year-over-year, a decent pace even as it inched down from 4.0 percent in the prior report.

  The saving rate edged up from 8.0 percent in May to 8.1 percent in June. Through the first six months of 2019, it has averaged 8.3 percent, up from an average of 7.6 percent in the second half of 2018. This is consistent with the slower pace of spending growth experienced year to date. Still, as the numbers above suggest, consumer spending has been a bright spot in the economy overall, helping to prop up growth.

- **University of Michigan Consumer Sentiment:** The Index of Consumer Sentiment inched up from 98.2 in June to 98.4 in July, according to the University of Michigan and Thomson Reuters. Americans felt slightly less upbeat about current conditions, but the headline index rose on an improved outlook for the coming months. The release added, "Economic confidence has been remarkably stable since the start of 2017, despite ongoing trade uncertainties. The resilience displayed has been primarily due to a renewed sense of personal financial optimism."