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MONDAY ECONOMIC REPORT



Fed's Preferred Measure of Inflation Moderated Further in December

By Chad Moutray – January 30, 2023

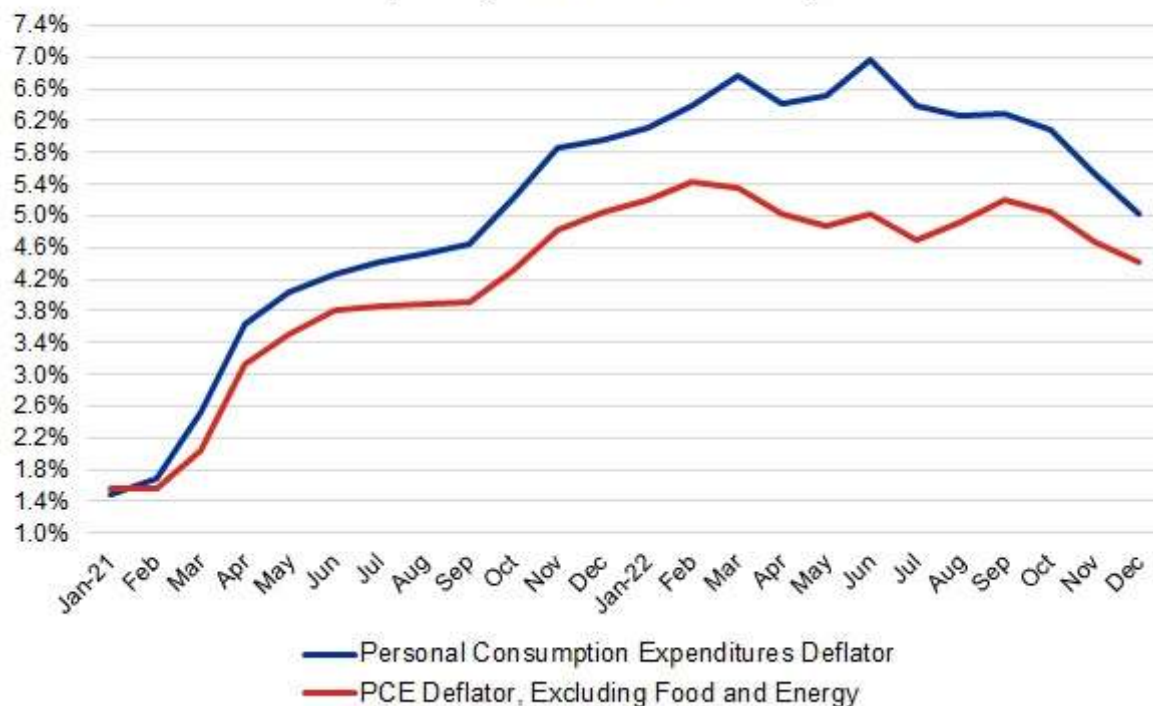
The Weekly Toplines

- The [personal consumption expenditures deflator](#) inched up 0.1% in December. Overall, the PCE deflator has risen 5.0% over the past 12 months, the slowest pace of inflation since September 2021, albeit at a still-elevated rate. Excluding food and energy, core PCE inflation was 4.4% year-over-year in December, a 14-month low.
- With pricing pressures moderating, the Federal Open Market Committee is likely to step down to 25 basis points for the federal funds rate increase at both the Jan. 31 – Feb. 1 (this week) and March 21–22 meetings before hitting the pause button.
- The U.S. economy [grew](#) 2.9% at the annual rate in the fourth quarter, expanding on the 3.2% growth in the third quarter. Strength in inventory spending, service-sector spending, net exports and government spending were bright spots in the fourth quarter, with the housing market providing a sizable drag on growth. Goods consumption rebounded somewhat, providing a positive contribution to real GDP growth for the first time in 2022.
- Despite solid growth in the second half of 2022, there continued to be significant downside risks in the economic outlook, with the risk of a recession elevated. With that said, the current forecast is for 1.3% growth in real GDP in 2023, slowing from 2.1% growth in 2022.
- [New orders for durable goods](#) jumped 5.6% to a record \$286.9 billion in December, buoyed by significant gains in aircraft and parts orders, which can be highly volatile from month to month. Excluding transportation equipment, new durable goods orders edged down 0.1%. Overall, while new durable goods orders excluding transportation soared 6.7% in the first half of 2022, sales fell 0.6% in the second half, with slowing global growth and an uncertain outlook dampening activity.

- Orders for core capital goods—a proxy for capital spending in the U.S. economy—declined 0.2% in December. Nonetheless, core capital goods orders grew 5.2% year-over-year and were not far from the record high in August.
- Manufacturing activity contracted for the third straight month, according to the [S&P Global Flash U.S. Manufacturing PMI](#). Hiring turned negative for the first time since July 2020, but respondents felt cautiously optimistic about production over the next six months.
- Manufacturing activity continued to contract in the [Kansas City](#) and [Richmond](#) Federal Reserve Bank districts in January, mirroring other regional surveys.
- [Personal spending](#) declined for the second straight month, including sizable decreases for durable and nondurable goods. Despite some weakening at year's end, personal spending has risen 7.4% over the past 12 months.
- Personal income increased 0.2% in December. Wages and salaries rose 0.3%, but with manufacturing wages and salaries declining 0.6%. Over the past 12 months, total wages and salaries have increased 5.3%, with manufacturing wages and salaries rising 3.8% year-over-year.
- The personal saving rate increased from 2.9% in November to 3.4% in December, the highest since May. While the saving rate remains low, the uptick in the last few months of the year suggests that Americans were holding onto more of their incomes.
- The [Index of Consumer Sentiment](#) rose to 64.9 in January, a nine-month high, according to the University of Michigan and Thomson Reuters. Overall, while Americans remain uncertain about geopolitical events, the economy and inflation, it is encouraging to see consumer confidence trend in the right direction, even as sentiment remains lower than preferred.

Year-Over-Year Percentage Changes in the PCE Deflator

(January 2021 – December 2022)



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, Jan. 23
Conference Board Leading Indicators

Tuesday, Jan. 24
Richmond Fed Manufacturing Survey
S&P Global Flash U.S. Manufacturing PMI
State Employment Report

This Week's Indicators:

Monday, Jan. 30
Dallas Fed Manufacturing Survey

Tuesday, Jan. 31
Conference Board Consumer Confidence
Employment Cost Index

Wednesday, Feb. 1
ADP National Employment Report

Wednesday, Jan. 25
Business Employment Dynamics

Thursday, Jan. 26
Durable Goods Orders and Shipments
Gross Domestic Product
International Trade in Goods (Preliminary)
Kansas City Fed Manufacturing Survey
New Home Sales
Weekly Initial Unemployment Claims

Friday, Jan. 27
Personal Consumption Expenditures
Deflator
Personal Income and Spending
University of Michigan Consumer Sentiment
(Revision)

Construction Spending
FOMC Monetary Policy Statement
ISM® Manufacturing Purchasing Managers' Index®
Job Openings and Labor Turnover Survey

Thursday, Feb. 2
Factory Orders and Shipments
Productivity and Costs
Weekly Initial Unemployment Claims

Friday, Feb. 3
BLS National Employment Report

A Message from Husch Blackwell



What Risks Can Manufacturers Expect in 2023?

As international commerce evolves, Husch Blackwell's team of legal thought leaders is providing insight into what manufacturers can expect in 2023. Download our [Legal](#)

[Insights for Manufacturing report](#) to explore how the legal and regulatory framework is evolving to address manufacturing's large generational shifts. Topics include:

- Supply chain risk and reshoring;
- Cybersecurity and data protection;
- Heightened regulatory and enforcement risk;
- Product safety and associated liability; and
- Increased unionization and skilled labor scarcity.

The choices made during this era of transition will be crucial for U.S. manufacturers. Download our [Legal Insights for Manufacturing report](#) to learn more.

Deeper Dive

- **[Business Employment Dynamics](#):** Manufacturing experienced a net increase of 3,000 jobs in the second quarter of 2022, slowing materially from the gain of 130,000 in the first quarter. Manufacturers saw gross job gains of 464,000 in the second quarter, with 414,000 from expanding establishments and 50,000 from new establishments. At the same time, gross job losses totaled 461,000 in the second quarter, with 374,000 from contracting establishments and 87,000 from closing establishments.

In addition, the Bureau of Labor Statistics [reported](#) the formation of 7,000 manufacturing start-ups in the second quarter of 2022, the same pace as in the first quarter. The [start-up rate](#) represented 2.1% of all establishments in the sector. Those new establishments (or “births”) employed 30,000 workers in the second quarter, up from 27,000 in the previous quarter. Overall, manufacturing start-up rates rose sharply in 2021 but have cooled since then, albeit at levels that remain elevated relative to pre-pandemic paces, including for employment.

- **[Conference Board Leading Indicators](#):** The Leading Economic Index decreased 1.0% in December, falling for the 10th straight month. Over the past six months, the LEI has declined 4.2%, suggesting weaker growth over the coming months as firms grapple with an uncertain economic outlook. The release notes that these data are consistent with a higher risk of recession in the near term. Nonetheless, the Coincident Economic Index edged up 0.1% in December, with 1.4% growth over the past six months.
- **[Durable Goods Orders and Shipments](#):** New orders for durable goods jumped 5.6% from \$271.6 billion in November to a record \$286.9 billion in December. With that said,

significant gains occurred in defense and nondefense aircraft and parts orders, which can be highly volatile from month to month. Excluding transportation equipment, new durable goods orders edged down 0.1% from \$179.0 billion to \$178.8 billion. Overall, while new durable goods orders excluding transportation soared 6.7% in the first half of 2022, sales fell 0.6% in the second half, with slowing global growth and an uncertain outlook dampening activity. Over the past 12 months, new durable goods orders rose 11.9%, or a more modest 2.1% year-over-year with transportation equipment excluded.

In December, the underlying data were mixed. In addition to aircraft, durable goods sectors with increased new orders included electrical equipment, appliances and components (up 1.9%), motor vehicles and parts (up 0.7%), other durable goods (up 0.7%) and fabricated metal products (up 0.3%). In contrast, demand declined for machinery (down 1.7%), computers and electronic products (down 0.6%) and primary metals (down 0.3%).

Orders for core capital goods (or nondefense capital goods excluding aircraft)—a proxy for capital spending in the U.S. economy—declined 0.2% from \$75.0 billion in November to \$74.9 billion in December. Nonetheless, core capital goods orders grew 5.2% year-over-year and were not far from the record high in August (\$75.4 billion).

Meanwhile, durable goods shipments increased 0.5% from \$276.3 billion in November to a record \$277.7 billion in December. Excluding transportation equipment, shipments of durable goods edged down 0.1% from \$184.0 billion to \$183.9 billion. On a year-over-year basis, durable goods shipments have risen 8.5% since December 2021, or 4.2% excluding transportation equipment. In addition, core capital goods shipments declined 0.4% from \$75.0 billion to \$74.7 billion, with 7.6% growth over the past 12 months and activity that remains just shy of October's record (\$75.2 billion).

- **Gross Domestic Product (Fourth Quarter):** The U.S. economy grew 2.9% at the annual rate in the fourth quarter, expanding on the 3.2% growth in the third quarter. Strength in inventory spending, service-sector spending, net exports and government spending were bright spots in the fourth quarter, with the housing market providing a sizable drag on growth. Goods consumption rebounded somewhat, providing a positive contribution to real GDP growth for the first time in 2022.

Despite solid growth in the second half of 2022, there continued to be significant downside risks in the economic outlook, with the risk of a recession elevated. With that said, the current forecast is for 1.3% growth in real GDP in 2023.

Breaking down the various components of real GDP growth:

- **Private consumption expenditures:** Consumer spending on goods rose 1.1% at the annual rate in the fourth quarter, the first positive reading in one year, with durable and nondurable goods spending up 0.5% and 1.5%, respectively. At the same time, service-sector spending increased 2.6% in the fourth quarter, slowing from 3.7% in the third quarter. Personal consumption expenditures added 1.42 percentage points to headline real GDP growth in the fourth quarter, with goods and service-sector spending adding 0.26 and 1.16 percentage points to topline growth, respectively.
- **Gross private fixed investment:** Nonresidential fixed investment inched up 0.7% at the annual rate in the fourth quarter, easing from 6.2% in the third quarter. Spending on structures rebounded, rising ever so slightly after declines in the previous six quarters, and intellectual property products were once again a bright spot, which should benefit productivity growth moving forward. Yet, equipment spending fell for the second time in the past three quarters, and residential investment remained solidly negative, plummeting 26.7% at the annual rate in the fourth quarter. Overall, nonresidential fixed investment added just 0.09 percentage points to headline growth in the fourth quarter, with residential spending subtracting 1.29 percentage points.

Meanwhile, inventory investment contributed 1.46 percentage points to real GDP growth in the fourth quarter, ending two straight quarters of sharp declines.

- **Net exports:** Net exports provided 0.56 percentage points to headline growth in the fourth quarter. Yet, goods exports fell 7.0% at the annual rate in the fourth quarter, with goods imports dropping 5.6%. The decline in goods imports was enough to contribute 0.72 percentage points to topline growth, offsetting the 0.58 percentage-point drag from goods exports. Service-sector trade contributed a net 0.42 percentage points as well.
 - **Government spending:** Federal government expenditures rose 6.2% at the annual rate in the fourth quarter, with state and local government spending up 2.3%. Government spending added 0.64 percentage points to real GDP growth in the fourth quarter.
- **International Trade in Goods (Preliminary):** The U.S. goods trade deficit rose from \$82.93 billion in November to \$90.27 billion in December, according to preliminary figures. The higher goods trade deficit for the month was the result of reduced goods exports (down from \$169.41 billion to \$166.78 billion) that corresponded with an increase in goods imports (up from \$252.34 billion to \$257.05 billion). Final data, which will include the service-sector trade surplus, will be released Feb. 7.

Goods exports fell \$2.63 billion in December, with reduced exports for industrial supplies (down \$3.40 billion) and consumer goods (down \$346 million). However, increased exports for the month in foods, feeds and beverages (up \$682 million) and automotive vehicles (up \$306 million) partially offset those declines.

Meanwhile, goods imports increased \$4.71 billion in December, with strength in consumer goods (up \$3.97 billion) and automotive vehicles (up \$3.03 billion). Imports of industrial supplies declined \$2.57 billion in December.

- **[Kansas City Fed Manufacturing Survey](#)**: Manufacturing activity contracted for the fourth straight month in the Kansas City Federal Reserve Bank's district, but with the composite index improving from -4 in December to -1 in January. Activity declined for new orders, production, exports and the average employee workweek. At the same time, slight expansions occurred for both shipments and hiring, and raw material costs accelerated somewhat.

Manufacturers in the district continued to predict relatively sluggish growth over the next six months, with the forward-looking composite index easing from 6 to 3. Respondents expected employment growth to remain solid, with modest increases seen for capital expenditures. Manufacturers predicted input costs to be elevated over the next six months, albeit with the slowest rate of growth since July 2020.

- **[New Home Sales](#)**: New single-family home sales increased for the third straight month, rising 2.3% from 602,000 units at the annual rate in November to 616,000 units in December, boosted by strength in the Midwest and South. Despite some progress, homebuyers continue to cite affordability as a concern, which has impacted the housing market negatively. Over the past 12 months, single-family home sales have fallen 26.6% year-over-year.

There were 9.0 months of supply for new single-family homes in December, down from 9.2 months in November. The median sales price pulled back for the second consecutive month from a record of \$491,300 in October to \$459,000 in November and \$442,100 in December. The median sales price has increased 7.8% year-over-year from \$410,000 in December 2021.

- **[Personal Consumption Expenditures Deflator](#)**: The PCE deflator inched up 0.1% in December, the same pace as in November. Energy costs fell for the fifth time in the past six months, dropping 5.1% in December. At the same time, food prices rose 0.2% for the month, the weakest growth rate since March 2021. Excluding food and energy prices, the PCE deflator increased 0.3% in December, up from 0.2% in November.

Overall, the PCE deflator has risen 5.0% over the past 12 months, down from 5.5% year-over-year in November and the slowest pace of inflation since September 2021, albeit at a still-elevated rate. Excluding food and energy, core PCE inflation was 4.4% year-over-year in December, a 14-month low.

The PCE deflator is the preferred measure of inflation for the Federal Reserve, and with pricing pressures remaining well above desired rates, the Federal Open Market Committee will continue to tighten monetary policy as it seeks to tackle inflationary pressures in the U.S. economy. Yet, pricing pressures are moderating, and as a result, the FOMC is likely to step down to 25 basis points for the federal funds rate increase at both the Jan. 31 – Feb. 1 and March 21–22 meetings before hitting the pause button. As always, this will hinge on upcoming inflation and employment data.

- **[Personal Income and Spending](#):** Personal consumption expenditures declined for the second straight month, falling 0.2% in December after edging down 0.1% in November. Spending on durable and nondurable goods decreased 1.9% and 1.4% in December, respectively. Service-sector spending rose 0.5% for the month. Despite some weakening at year's end, personal spending has risen 7.4% over the past 12 months, with goods and service-sector purchasing up 4.7% and 8.7% since December 2021, respectively.

Meanwhile, personal income increased 0.2% in December, easing slightly from 0.3% in November. Wages and salaries rose 0.3% for the month, but with manufacturing wages and salaries declining 0.6% from \$1,051.5 billion in November to \$1,045.1 billion in December. Over the past 12 months, total wages and salaries have increased 5.3%, with manufacturing wages and salaries rising 3.8% year-over-year.

With income growth outpacing spending, the personal saving rate increased from 2.9% in November to 3.4% in December, the highest since May. While the saving rate remains low, the uptick in the last few months of the year suggests that Americans were holding onto more of their incomes.

- **[Richmond Fed Manufacturing Survey](#):** Manufacturing activity contracted for the sixth time in the past eight months, according to the Richmond Federal Reserve Bank, with the composite index of general business activity down from 1 in December to -11 in January. New orders have not expanded since March 2022, with declines in the latest data seen for shipments, capacity utilization, capital expenditures, hiring and local business conditions. With that said, wage growth remains solid, and raw materials and finished goods inventories continued to expand. Moving forward, manufacturers in the district felt negative in their expectations for new orders, shipments and capacity utilization, but predicted hiring and wage growth to strengthen

somewhat.

Inflationary pressures have continued to moderate, but at elevated levels. Costs for raw materials rose 7.91% in January, with the prices received for goods and services up 6.52%. In addition, respondents anticipated an annualized 3.96% increase in costs six months from now, with the expected prices received rising 3.72%.

- **[S&P Global Flash U.S. Manufacturing PMI](#)**: Manufacturing activity contracted for the third straight month, according to the S&P Global Flash U.S. Manufacturing PMI, but with the headline index improving from 46.2 in December to 46.8 in January. New orders (up from 42.7 to 43.9) continued to decline sharply, albeit up from December's post-pandemic low, with slower declines also reported for output (up from 46.2 to 46.7) and exports (up from 46.7 to 48.1). On the other hand, hiring (down from 50.6 to 49.7) turned negative for the first time since July 2020. The index for future output (up from 62.5 to 68.6) strengthened, signaling increased (cautious) optimism about production over the next six months.

After growing at the slowest pace since July 2020 in December, raw material costs (up from 55.6 to 57.7) accelerated somewhat in January, increasing modestly. The index for supplier delivery times (down from 49.9 to 49.3) pulled back for the second straight month, suggesting slight increases in delivery times despite notable improvements in bottlenecks overall in recent months.

Meanwhile, despite contracting for the seventh straight month, the [S&P Global Flash Eurozone Manufacturing PMI](#) improved from 47.8 in December to 48.8 in January. The rate of decline continued to ease for new orders, exports and output, and employment strengthened. Encouragingly, the index for future output rose to its highest level since before the Russian invasion of Ukraine, signaling hopes for decent (and likely cautious) growth in production over the coming months. In addition, input prices grew modestly, decelerating to the slowest growth rate since October 2020.

In [France](#), manufacturers reported the first expansion in activity since August, with rebounding employment and slower declines in other key measures. At the same time, contractions continued in [Germany](#) and, outside the Eurozone, in the [United Kingdom](#). Manufacturing activity in Great Britain fell sharply, but at a slower rate, while service-sector sentiment plummeted to a two-year low. In Germany, the index for future output was positive for the first time since February 2022.

- **[State Employment Report](#)**: Texas created the most net new manufacturing jobs in December, adding 5,500 workers. Other states with notable employment growth for the month included Ohio (up 4,900), Georgia (up 3,600), Oregon (up 2,400) and

Pennsylvania (up 2,000). Over the past 12 months, Texas (up 49,000) also had the most manufacturing employment growth. Other states with significant year-over-year gains included California (up 35,000), Florida (up 27,400), Pennsylvania (up 25,400), Ohio (up 22,800) and Illinois (up 17,600).

In December, the [U.S. unemployment rate](#) edged down from 3.7% to 3.5%. At 2.2%, Utah had the lowest unemployment rate nationally, followed closely by North Dakota (2.3%), South Dakota (2.3%), Florida (2.5%), Minnesota (2.5%), Nebraska (2.6%) and Vermont (2.6%). At the other end of the spectrum, Nevada had the highest unemployment rate in the country at 5.2%. Other states with elevated rates included Illinois (4.7%), the District of Columbia (4.7%), Oregon (4.5%) and Delaware (4.4%).

- [University of Michigan Consumer Sentiment \(Revision\)](#): The Index of Consumer Sentiment rose from 59.7 in December to 64.9 in January, a nine-month high, according to final data from the University of Michigan and Thomson Reuters. That improved slightly from the previous estimate of 64.6. Assessments of current conditions improved strongly, buoyed by labor market strength and slowing inflation data. Expectations of future conditions also improved in January. Overall, while Americans remain uncertain about geopolitical events, the economy and inflation, it is encouraging to see consumer confidence trend in the right direction, even as sentiment remains lower than preferred.
- [Weekly Initial Unemployment Claims](#): The week ending Jan. 21 saw 186,000 initial unemployment claims, down from 192,000 for the week ending Jan. 14 and the lowest reading since mid-April. In contrast, the week ending Jan. 14 saw 1,675,000 continuing claims, up from 1,655,000 for the week ending Jan. 7. Even with the slight rise in continuing claims, the labor market remained a bright spot in the economy.

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