<

MONDAY ECONOMIC REPORT

Essential Takes on Leading Economic Indicators

By Chad Moutray, Ph.D., CBE – September 3, 2019 – SHARE

Regional Fed Surveys Show Some Stabilization in Manufacturing Activity

The Weekly Toplines

- After weaker data in previous months, manufacturing surveys from the Dallas and Richmond Federal Reserve Bank districts showed some signs of stabilization in August. Yet, it is clear that activity has decelerated from stronger paces last year. In the Texas release, sample comments continued to note worries about slower global growth, trade policy uncertainties and the difficulties in finding sufficient talent. The outlook for the next six months remained positive for both districts.

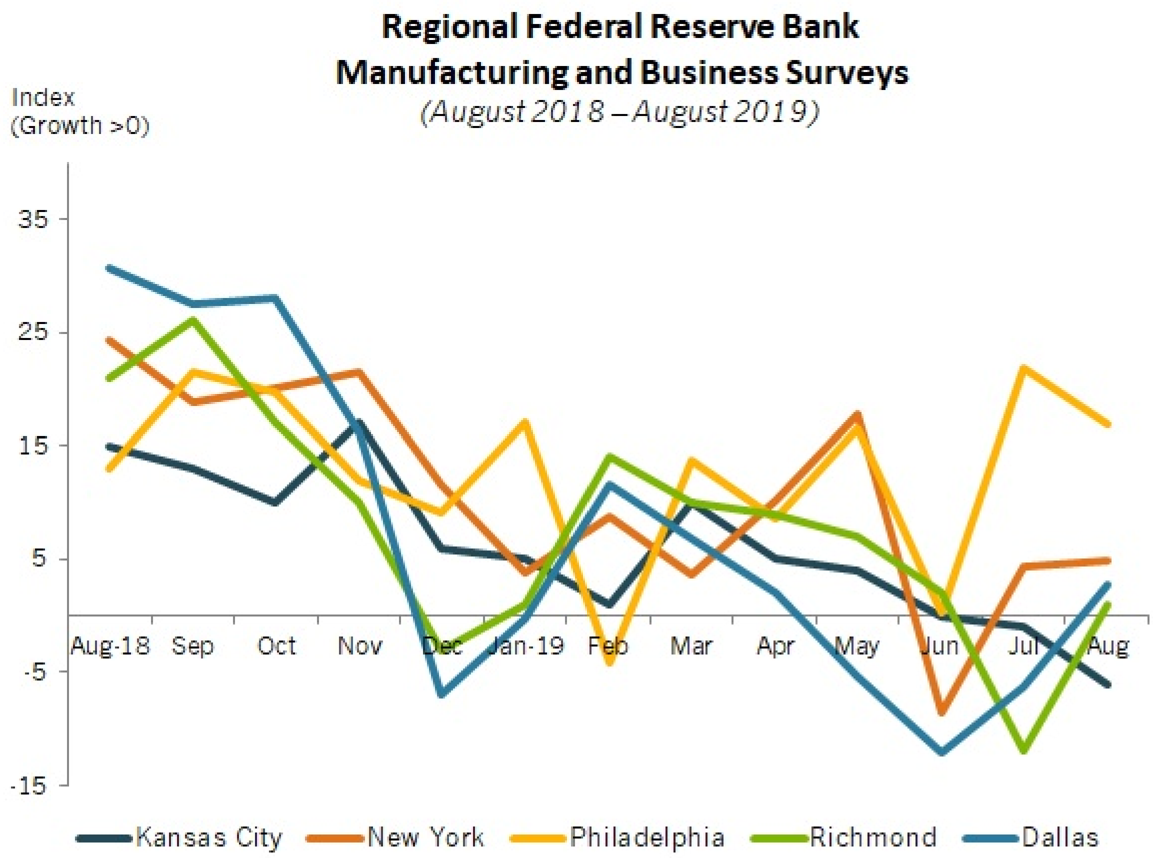
- New durable goods orders increased 2.1 percent in July, but with very large increases for defense and nondefense aircraft orders, which are often highly volatile from month to month. Excluding transportation equipment, new durable goods orders fell 0.4 percent in July. Over the past 12 months, new durable goods orders have risen a very soft 1.0 percent, with a decline of 0.1 percent with transportation equipment excluded.

- The U.S. economy grew 2.0 percent at the annual rate in the second quarter, off slightly from the previous estimate of 2.1 percent growth and down from 3.1 percent growth in the first quarter. Consumer and government spending buoyed growth for the quarter, but drags from business spending and net exports counterbalanced this somewhat. Nonresidential fixed investment fell 0.6 percent in the second quarter, the first decline since the first quarter of 2016.

- Moving forward, I estimate 1.9 percent growth at the annual rate in the third quarter, with 2.3 percent growth for 2019. The outlook is for 1.8 percent growth in 2020, but with strong cases for both upside and downside risks to that figure, at least for now.

- According to the Conference Board, consumer confidence slipped marginally in August, with the headline index down from 135.8 to 135.1, but mostly sustained the strong reading from July. Indeed, consumers felt more upbeat about current economic conditions, with that measure rising to the best reading since November 2000 on strong labor market and income assessments.

- In contrast, the Index of Consumer Sentiment fell from 98.4 in July to 89.8 in August, according to the University of Michigan and Thomson Reuters. This was well below the preliminary estimate of 92.1 and the weakest reading since October 2016, largely on a sharply reduced outlook due to increased trade policy uncertainties and volatility in financial markets.
- Nonetheless, personal spending jumped 0.6 percent in July, the best reading since April. This suggests that the consumer continues to spend at a solid pace, helping to prop up the economy. Personal consumption expenditures have risen 4.1 percent year-over-year, a decent pace even as it inched down from more robust year-over-year rates last year. The saving rate also reflected the acceleration in spending, falling to 7.7 percent, the lowest rate since November.
- The core PCE deflator rose 0.2 percent in July, with a gain of 1.6 percent year-over-year. That is down from 2.1 percent year-over-year in July 2018. This measure has remained below the Federal Reserve’s stated goal of 2 percent core inflation for seven consecutive months, or in every month so far in 2019.
- 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. The Federal Open Market Committee is likely to reduce short-term interest rates at the Sept. 17–18 meeting, following the 25-basis-point reduction made at the July 30–31 meeting.



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, August 26
Chicago Fed National Activity Index
Dallas Fed Manufacturing Survey
Durable Goods Orders and Shipments

Tuesday, August 27
Conference Board Consumer Confidence
Richmond Fed Manufacturing Survey

Wednesday, August 28
None

Thursday, August 29
Gross Domestic Product (Revision)
International Trade in Goods (Preliminary)

Friday, August 30
Personal Consumption Expenditures

This Week's Indicators:

Monday, September 2
LABOR DAY HOLIDAY

Tuesday, September 3
Construction Spending
ISM® Manufacturing Purchasing Managers' Index®

Wednesday, September 4
International Trade Report

Thursday, September 5
ADP National Employment Report
Factory Orders and Shipments
Productivity and Costs (Revision)

Friday, September 6
BLS National Employment Report

Deflator
Personal Income and Spending
University of Michigan Consumer Sentiment (Revision)

Deeper Dive

- **Chicago Fed National Activity Index:** The Chicago Federal Reserve Bank reported that the National Activity Index weakened once again, with the headline index dropping from 0.03 in June to -0.36 in July. It was the seventh negative reading in the past eight months, with index readings below zero consistent with an economy that is operating below the historical trend. Manufacturing challenges have contributed to this weakness, with the sector anxious about slowing growth globally and ongoing trade uncertainties. In July, industrial production fell 0.2 percent, with output in the manufacturing sector off 0.4 percent. This subtracted 0.25 points from the NAI for the month.

- **Conference Board Consumer Confidence:** Consumer sentiment slipped marginally in August, with the headline index down from 135.8 to 135.1, but mostly sustained the strong reading from July. Indeed, consumers felt more upbeat about current economic conditions, with that measure rising to the best reading since November 2000. This was partially offset by some slight slippage in expectations in the outlook, but that figure was also solid overall.

  In the latest data, the percentage of respondents suggesting that business conditions were "good" increased from 39.9 percent to 42.0 percent, whereas those noting conditions were "bad" declined from 11.2 percent to 9.8 percent. The labor market variables also remained quite healthy. The percentage of Americans feeling that jobs were "plentiful" increased from 45.6 percent to 51.2 percent, with those responding that jobs were "hard to get" dropping from 12.5 percent to 11.8 percent.

- **Dallas Fed Manufacturing Survey:** After three months of contracting levels of activity, manufacturers reported a rebound in August. The composite index increased from -6.3 in July to 2.7 in August, with stronger expansions reported for new orders, production and shipments. Despite that progress, the sample comments continued to note worries about slower global growth, trade policy uncertainties and the difficulties in finding sufficient talent. In special questions, 83.6 percent of manufacturing respondents said their companies were having difficulties finding qualified workers, up from 79.5 percent who said the same thing in May. Along those lines, hiring and capital spending growth slowed in the August data.

  Moving forward, manufacturers in the Texas district remained positive about the next six months, including optimism for increased demand, output, hiring and capital expenditures, albeit with some easing from July's expectations. Pricing pressures are expected to continue moderating, with the forwardlooking index for raw material costs decelerating to the lowest level since February 2016.

- **Durable Goods Orders and Shipments:** New durable goods orders increased 2.1 percent in July, extending the 1.8 percent gain in June. Nonetheless, very large increases occurred in July in defense and nondefense aircraft orders, which are often highly volatile from month to month. Motor vehicle sales rose 0.5 percent for the month, with transportation equipment demand jumping 7.0 percent. Excluding transportation equipment, however, new durable goods orders fell 0.4 percent, with declining sales in July for fabricated metal products, machinery, primary metals and other durable goods. Beyond increased auto sales, there was greater demand for computers and electronic products and electrical equipment, appliances and components.

  Overall, global economic headwinds and trade uncertainties continue to challenge growth in the manufacturing sector. Indeed, new durable goods orders have risen a very soft 1.0 percent over the past 12 months, with a decline of 0.1 percent with transportation equipment excluded. This suggests flat demand year-over-year for the broader measure of durable goods. At the same time, new orders for core capital goods (or nondefense capital goods excluding aircraft)—a proxy for capital spending in the U.S. economy—increased 0.4 percent in July, but on a year-over-year basis, this figure decreased 0.5 percent.

  Meanwhile, durable goods shipments decreased 1.1 percent in July, with a decline of 0.7 percent excluding transportation equipment sales. On a year-over-year basis, durable goods shipments edged down 0.1 percent, with core capital goods shipments up 1.0 percent since July 2018.

- **Gross Domestic Product (Second Quarter Revision):** The U.S. economy grew 2.0 percent at the annual rate in the second quarter, off slightly from the previous estimate of 2.1 percent growth and down from 3.1 percent growth in the first quarter. Consumer and government spending buoyed growth for the quarter, but drags from business spending and net exports counterbalanced this somewhat. Slowing global growth and trade uncertainties were both challenges in the second quarter, with businesses hesitant to increase spending. Along those lines, nonresidential fixed investment fell 0.6 percent in the second quarter, the first decline since the first quarter of 2016.

  Moving forward, I estimate 1.9 percent growth at the annual rate in the third quarter, with 2.3 percent growth for 2019. The outlook is for 1.8 percent growth in 2020, but with strong cases for both upside and downside risks to that figure, at least for now.

  The downward revision stemmed from weaker data than what was estimated in the prior release for exports, government spending, inventories and residential spending. Better personal consumption expenditures figures offset this to some degree. Along those lines, consumer spending grew 4.7 percent at the annual rate, up from the previous estimate of 4.3 percent growth and rebounding from weaknesses in the prior two quarters. Durable and nondurable goods spending jumped 13.0 percent and 6.8 percent in the second quarter, respectively, contributing 1.78 percentage points in total to top-line growth and bouncing back from sluggish consumer spending in the fourth and first quarters. With service-sector spending included, personal consumption expenditures added 3.10 percentage points.

However, weaknesses from business spending and net exports, which combined to subtract 1.83 percentage points from the top line, offset those positive elements. A 9.4 percent decline at the annual rate in spending for structures pulled nonresidential fixed investment lower. Spending on private inventories also provided a drag, subtracting 0.91 percentage points from real GDP growth and ending three quarters of increases. (This could be a positive for third quarter growth if demand picks up, as it could necessitate additional production to restock shelves.) Residential investment fell for the sixth consecutive quarter, down an annualized 2.9 percent in the second quarter.

Meanwhile, goods exports fell 5.6 percent at the annual rate in the second quarter, with goods imports edging up 0.3 percent. This was largely expected given the strong growth in exports in the first quarter, likely reflecting some shifting of activity in light of trade uncertainties. Overall, net exports subtracted 0.72 percentage points from top-line growth.

- **International Trade in Goods (Preliminary):** In advance statistics, the goods trade deficit declined from $74.16 billion in June to $72.34 billion in July, narrowing for the second straight month. Goods exports rose by $889 million, led by increases for automotive vehicles, capital goods and consumer goods but partially offset by reduced activity for industrial supplies and foods, feeds and beverages. At the same time, goods imports decreased by $932 million, pulled lower by weaknesses in capital goods. Final data will be released Sept. 4, which will also include the service-sector trade surplus.

- **Personal Consumption Expenditures Deflator:** The PCE deflator rose 0.2 percent in July, up from 0.1 percent in both May and June. Increased energy costs, up 1.4 percent in July, helped to lift the headline figure, with food costs off 0.1 percent in both of the past two months. The core PCE deflator, which excludes food and energy prices, increased 0.2 percent in July for the second consecutive month. Over the past 12 months, the PCE deflator has risen 1.4 percent, up from 1.3 percent in June but down from 2.5 percent year-over-year in July 2018. Core inflation has also decelerated, down from 2.1 percent year-over-year in July 2018 to 1.6 percent in the latest data. This measure has remained below the Federal Reserve's stated goal of 2 percent core inflation for seven consecutive months, or in every month so far in 2019.

  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. This includes the 25-basis-point cut in short-term rates made at the July 30–31 meeting, but also the likely federal funds rate reduction that could be made at its next meeting Sept. 17–18.

- **Personal Income and Spending:** Personal consumption expenditures jumped 0.6 percent in July, up from 0.3 percent in June and the best reading since April. This suggests that the consumer continues to spend at a solid pace, helping to prop up the economy. Durable and nondurable goods spending increased 0.6 percent and 1.1 percent, respectively, for the month. Moreover, personal spending has risen 4.1 percent year-over-year, a decent pace even as it inched down from more robust year-over-year rates last year.

  At the same time, personal income edged up 0.1 percent in July, slowing from a gain of 0.5 percent in June. Over the past 12 months, personal income has risen 4.6 percent, easing somewhat from the 5.0 percent year-over-year pace in June. In addition, manufacturing wages and salaries inched down from $918.5 billion in June to $917.0 billion in July. Even with some easing, that would indicate a healthy 4.0 percent growth rate since July 2018, which was $881.4 billion.

  With spending soaring but income slowing, the saving rate dropped from 8.0 percent in June to 7.7 percent in July, the lowest rate since November. This is consistent with the acceleration of consumer spending in recent months, which is encouraging.

- **Richmond Fed Manufacturing Survey:** Manufacturing activity stabilized in August after declining in July at the fastest pace since January 2013. The composite index of general business activity rose from -12 in July to 1 in August, with improving activity for new orders, shipments and the average workweek. Capital spending accelerated slightly in August, but hiring remained negative for the second straight month. Moving forward, manufacturers in the district remained mostly optimistic about the next six months, albeit with some easing in the growth expected for sales, shipments, capacity utilization, capital spending and employment. Manufacturers continue to anticipate wages expanding at a solid pace, with firms once again noting an inability to find sufficient talent.

  Raw material costs pulled back in the latest survey, up 2.69 percent at the annual rate in August after jumping 3.04 percent in July. Manufacturers also predict some slowing in price growth, with respondents expecting an annualized 2.28 percent increase six months from now, down from 2.50 percent and 2.33 percent in the prior two surveys, respectively.

- **University of Michigan Consumer Sentiment:** The Index of Consumer Sentiment fell from 98.4 in July to 89.8 in August, according to the University of Michigan and Thomson Reuters. This was well below the preliminary estimate of 92.1 and the weakest reading since October 2016. Americans felt less upbeat about both current and future economic conditions, but especially in the outlook. Consumers expressed anxiousness on increased trade policy uncertainties and volatility in financial markets.

Take Action

If you have not already done so, please take a moment to complete the latest NAM Manufacturers' Outlook Survey. This 29-question survey will help us gauge how manufacturing sentiment has changed since the second quarter survey. The current survey includes special questions on trade uncertainties, infrastructure, immigration, tax reform and new technology implementation. To complete the survey, click here. Responses are due by Tuesday, Sept. 3, at 5:00 p.m. EDT. As always, all responses are anonymous.

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