STATE STREET GLOBAL ADVISORS

May 17, 2024
Commentary

Weekly Economic Perspectives

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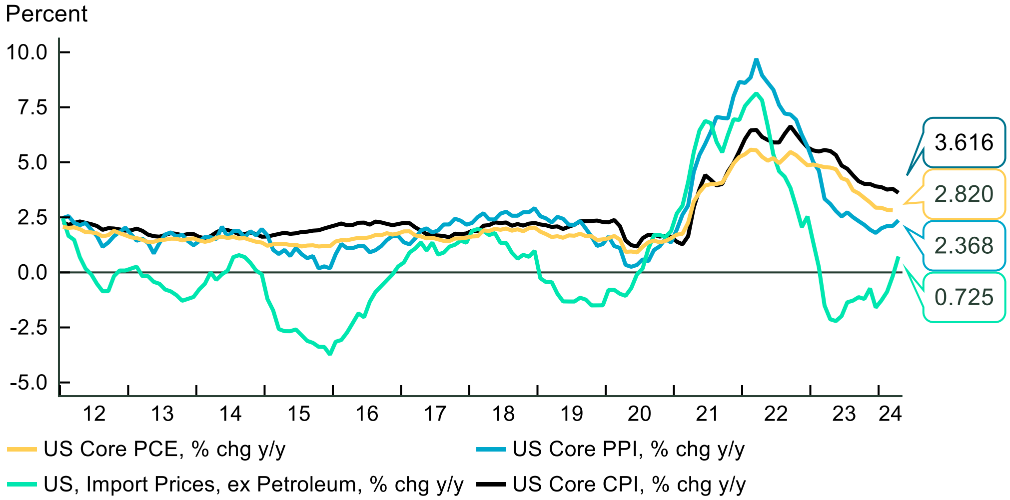
The Economy

US inflation improves but demand indicators soften.

US

Following three months of upside surprises, the April **consumer price inflation** data brought a bit of much needed relief. Both overall and core prices (excluding food and energy) increased 0.3% m/m, a tenth less than in March. For headline, this was marginally below consensus expectations. The headline inflation rate eased a tenth to 3.4% y/y and the core inflation rate eased two tenths to 3.6% y/y.

Figure 1: US Core Inflation Metrics



Sources: Macrobond, SSGA Economics, BLS
Updated as of 5/19/2024

Food prices were flat, with food at home actually down 0.2% m/m while food away from home rose 0.3% m/m. Energy prices rose 1.1% m/m, driven by a 2.8% jump in gasoline prices. Goods prices rose 0.2%, although core goods prices declined 0.1% thanks to lower car prices. Indeed, there was a 0.4% decline in new vehicle prices and a 1.4% drop in used car prices. The latter reflects lower auction prices, but with sizable pullbacks in three of the past four months, the run of declines may pause next month. Service prices increased 0.4% m/m, the least since December, largely due to a 0.7% drop in energy services. This, too, is a delayed reflection of lower natural gas prices: last month we commented that it was surprising we did not see any relief in this CPI component, but it arrived in April with a 2.9% m/m decline. Shelter costs increased 0.4% m/m, and OER (owners' equivalent rent) did the same. Airline fares declined 0.8% but medical care increased 0.4%. Nothing in this report was particularly striking and the near-term road remains bumpy given persistent pressures in car insurance and repair costs, as well as slow moderation in rent inflation. Still, in the context of further evidence of consumer demand and labor market cooling, this report keeps the possibility of a late July Fed rate cut alive.

Indeed, most of this week's data was on the soft side. Last month, we expressed surprise at the strength in March **retail sales** and were especially puzzled by the surge on online sales. The latest update validated that sentiment, as sales were flat in April and there were downward revisions to both March and February data.

Notably, online sales declined 1.2% m/m in April, and were the worst performing category during the month. The best performing categories were gasoline stations (+3.1% m/m), clothing (+1.6%) and electronics (1.5%). Control sales (excluding food services, building materials, autos dealers and gas stations) declined 0.3% m/m.

The housing data softened broadly. **Homebuilders' sentiment** retreated six points to a four-month low of 45 in May, with softness across components. April **housing starts** improved a little but from a downwardly revised March print and look fairly soft. **Housing permits** declined 3.0% to the lowest level since December 2022.

The industrial sector data also disappointed. **Industrial production** was flat in April and the March increase was revised down sharply. Meanwhile, both the **Empire** and the **Philly Fed manufacturing surveys** missed expectations, with soft new orders.

Canada

Housing market activity moderated in April. **Housing starts** trended lower, with the seasonally adjusted annualized rate of housing starts down 1.0% m/m to a still-solid level of 240.2k. The six-month moving average of starts was also down 2.2% m/m at 238.6k. The decline was driven by lower multi-unit starts in Vancouver and decrease in both multi-unit and single-detached starts in Toronto. High interest rates and construction costs might lead housing starts to trend lower in the next few months.

There was also a minor dip in sales in April as high interest rates continued to affect demand. **Existing home sales** were down 1.7% m/m in April, following a modest rise of 0.5% m/m in the previous month. This left the current existing home sales 11% below their pre-pandemic level. Meanwhile, new listings were up 2.8% m/m, leading the sales-to-new listings dropping to 53.4%, closer to the historical norms of 55%.

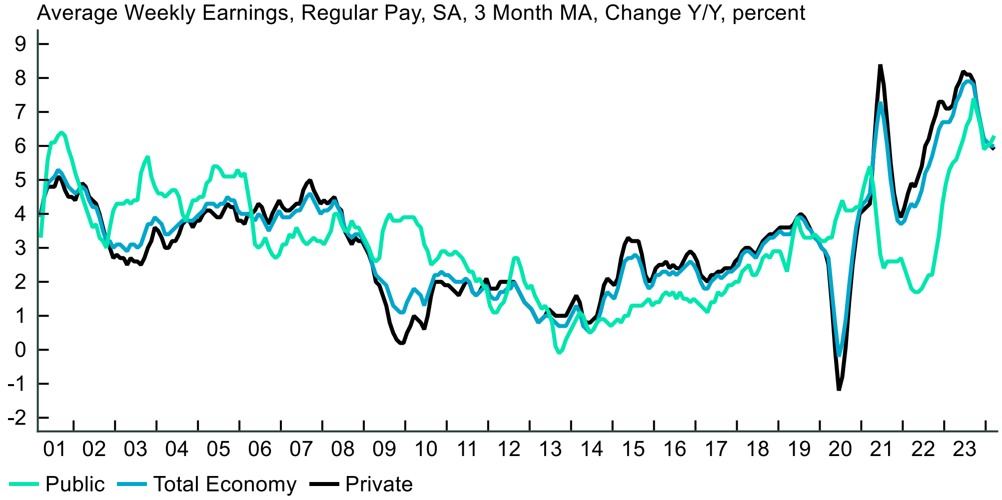
Building permits were down 11.7% in March, largely above market expectations of a 4.3% contraction. The decline was driven led by lower construction intentions in the non-residential component (-16.7%) and residential sector (-8.3%).

UK

The latest labor data revealed further easing in the job market albeit at a marginal pace. The unemployment rate for the three months to March inched up one tenth to 4.3%, with the usual caveat that there is "increased volatility of LFS estimates". This was in line with market and BoE expectations. Labor demand continued easing as headline vacancies in the three months to February fell for the 22nd consecutive period to 898k.

Headline wage pressure came in above consensus but that was due to strong public sector earnings growth. The **growth in average total pay** (including bonuses) for the three months to January inched up one tenth to 5.7% y/y, bucking market expectation of a decrease to 5.5%. The **growth in regular pay** (excluding bonuses) remained unchanged at 6.0% y/y, compared to market expectation of a decline to 5.9% y/y. Meanwhile, private sector wage growth edged down one tenth to 5.9% y/y. Given the latest labor market data were quite mixed, next week CPI figures will likely be the most influential upcoming data release in determining whether the BoE will go for a rate cut in June.

Figure 2: UK Private Sector Wage Growth Continued Slowing Down



Sources: Macrobond, SSGA Economics, ONS
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Eurozone

Not much new data was reported in the eurozone this week, with updated information largely confirming earlier releases for Q1 GDP growth (+0.3% q/q) and April inflation (+2.4% y/y). Among the new releases were the French ILO unemployment rate (steady at 7.3%) and the ***German* Zew Index of investor confidence**, which continues its steady recovery and now stands at its highest since right before the Ukraine invasion. Data remain supportive of a June ECB cut.

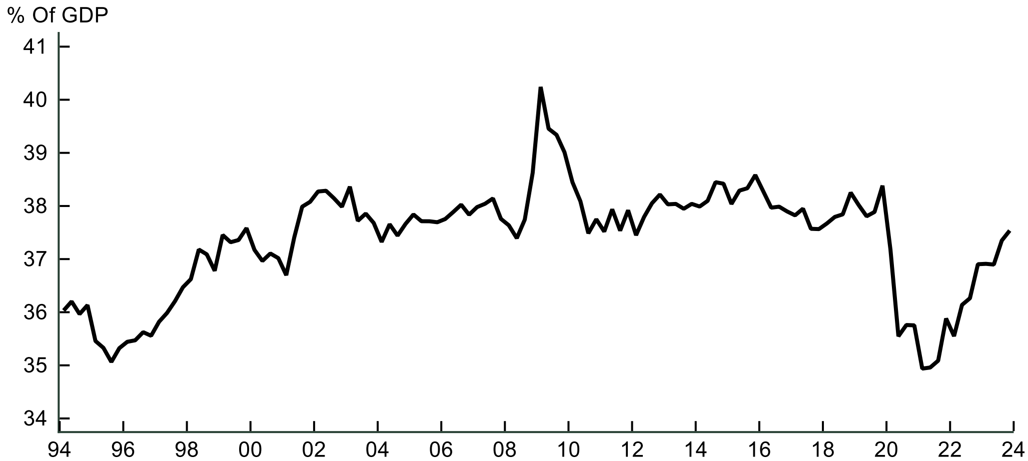
Japan

Q1 GDP contracted 0.5% q/q, a tenth more than we expected, putting the annualized rate of decline at 2.0%. Private consumption contracted for the fourth quarter, down 0.7% q/q. Durable goods consumption declined 12.2% q/q and detracted two percentage points from growth. This was just as bad as during the peak of pandemic (-12.3%) and was driven largely by a temporary shutdown at automakers earlier in the quarter.

However, there are three critical areas that still could add some growth impulse: spending from inbound tourists ("direct purchases in the domestic market by non-residents"), intellectual property rights (IPR), and services. Tourism has boomed since Covid on the weak yen, but we think that it will remain the same even when the yen appreciates 10-15% towards its fair value. Furthermore, remittances from IPR (and computer software) have also been robust. Take together, their share in GDP has risen from 34.5% in Q1 2021 to 37.5% as of Q1 2024 and has yet to reach its pre-pandemic level (figure 2).

Figure 3: Japan's GDP Recovery On Track

Share Of Spending Related To Services, IPR & Tourism In GDP



Sources: SSGA Economics, CAO, Macrobond
Updated as of 5/19/2024

The temporary factors this quarter also affected capex, which declined 0.8% q/q after expanding 1.8% in the last quarter. Private housing investment also declined. Exports dropped 5.0%, largely due to the suspension of auto production which resulted in net exports dragging growth.

Real compensation of employees declined sequentially by 0.4% and for the overall fiscal year, it declined 1.8% y/y, more than the 1.2% in FY 2023. Looking ahead, we expect that the higher *shunto* wage hike this year will lift compensation as well as private demand. Still, we see downside risks to our GDP forecast of 1.0% this year, as we now see GDP rising just by 0.5%.

The key risk still is the yen. This is because its weakness could once again reaccelerate inflation and stall the expected improvements in real compensation as well as private demand. For this reason, we still expect the Bank of Japan (BoJ) to hike their policy rate this year and also the next.

The BoJ this week reduced their planned purchases of 5-10y JGBs by 50 billion yen to 425 billion yen. Although this is just 3.3% of the 6 trillion yen average monthly purchases, it is a step in the right direction. We still expect the BoJ to hike to a terminal policy rate of 0.75% before December 2025.

As for the next week, we expect April CPI may have eased considerably, but remain above the 2% CPI target.

Australia

Interesting dynamics remain in play in Aussie markets as it added 38.5k jobs in April, more than expected (SSGA 20.0k, consensus 23.7k). However, full-time (FT) employment declined 6.1k, and the entire lifting was due to the 44.6k rise in part-time (PT) employment. The **labor market** is characterized a cyclical FT employment and counter-cyclical PT employment. Hence, it is more important to observe FT employment, which is cooling quite well. The unemployment rate rose 0.2 ppts to 4.1%, as the participation rate rose to 66.7%.

Meanwhile, the growth in the **Wage Price Index (WPI)** eased 11 bps and rose 4.1% y/y, in line with our expectations of peaked wage growth. Compositionally, the decline was largely caused by a softer rise in public sector wages (0.46% q/q) but private wages too eased (0.81%).

The **Commonwealth Budget for FY 2025** implied a near-term improvement in public finances. They have good support from strong commodity prices, which were assumed rather conservatively. The budget forecasts a surplus of A$ 9.3 bn or 0.3% of GDP, just a touch below that of the last fiscal. The forecast calls for deficits in the next three years due to a net government spending of A$ 24.4 bn. Aussie households, burdened by high prices get A$ 300 bn worth energy rebates which cost A$ 3.5 bn. They come along with the long-awaited income tax cuts and measures that improve aged care and lower pharmaceutical prices. Government net debt is forecasted to rise to 21.8% of GDP by FY 2027, as Australia remains way ahead of its global peers on debt metrics.

Week in Review (May 13 – May 17)

Country	Release (Date, format)	Consensus	Actual	Last	Comments
Monday, May 13					
CA	Building Permits (Mar, m/m)	-4.3%	-11.7%	8.9% (↓)	Disappointing.
JN	PPI (Apr, y/y)	0.8%	0.9%	0.9% (↑)	Good.
AU	NAB Business Confidence (Apr)	na	1.0	1.0	Could improve only through rate cuts.
Tuesday, May 14					
US	NFIB Small Business Optimism (Apr)	88.2	89.7	88.5	Mixed details.
US	PPI Final Demand (Apr, y/y)	2.2%	2.2%	1.8% (↓)	In line.
UK	ILO Unemployment Rate (Mar, 3m)	4.3%	4.3%	4.2%	In line with expectations.
UK	Average Weekly Earnings (Mar, y/y, 3m)	5.5%	5.7%	5.7% (↑)	Public sector wage pressure rose.
GE	CPI (Apr, y/y, final)	2.2% (p)	2.2%		
GE	ZEW Survey Expectations (May)	46.4	47.1	42.9	Improvement continues.
AU	Wage Price Index (Q1, y/y)	4.2%	4,1%	4.2%	As expected, but good.
Wednesday, May 15					
US	CPI (Apr, y/y)	3.4%	3.4%	3.5%	Incrementally better.
US	Retail Sales Advance (Apr, m/m)	0.4%	0.0%	0.6% (↓)	Miss augmented by downward revision.
US	Empire Manufacturing (May)	-10.0	-15.6	-14.3	Mixed.
US	NAHB Housing Market Index (May)	51.0	45.0	51.0	Higher mortgage rates undermine demand.
US	Business Inventories (Mar, m/m)	-0.1%	-00.1%	0.3% (↓)	Modest.
CA	Housing Starts (Apr, thous)	240.0	240.2	242.3 (↑)	Trending lower.
CA	Manufacturing Sales (Mar, m/m)	-2.8%	-2.1%	0.9% (↑)	Better than expected.
CA	Existing Home Sales (Apr, m/m)	na	-1.7%	0.5%	Soft.
EC	GDP (Q1, q/q, prelim, sa)	3.0%(p)	0.3%	-0.1%	Modest recovery has begun.
EC	Industrial Production (Mar, m/m, sa)	0.4%	0.6%	1.0% (↑)	Putting in a bottom, but still very weak.
FR	CPI (Apr, y/y, final)	2.2% (p)			
JN	GDP (Q1, q/q, sa, prelim)	-0.3%	-0.4%	0.0% (↑)	Temporary factors but should improve in Q2.
JN	Industrial Production (Mar, m/m, final)	3.8% (p)	-3.1%	-6.8%	Improving.
JN	Capacity Utilization (Mar, m/m)	na	1.3%	-0.5%	Great!
AU	Unemployment Rate (Apr)	3.9%	4.1%	3.8%	Labor market is cooling very well.
AU	Employment Change (Apr, thous)	23.7	38.5	-5.9 (↑)	Surge in part time jobs.
Thursday, May 16					
US	Initial Jobless Claims (May 11, thous)	220	222	232 (↑)	Very low.
US	Continuing Claims (May 04, thous)	1,780	1,794	1,781 (↓)	Very low.
US	Housing Starts (Apr, thous)	1,420	1,360	1,287 (↓)	Rather soft.
US	Philadelphia Fed Business Outlook (May)	8.0	4.5	15.5	Mixed details.
US	Building Permits (Apr, thous)	1,480	1,440	1,485 (↑)	Soft.
US	Import Price Index (Apr, y/y)	0.4%	1.1%	0.4%	Highest since December 2022.
US	Industrial Production (Apr, m/m)	0.1%	0.0%	0.3% (↓)	Manufacturing declined 0.3% m/m.
Friday, May 17					
US	Leading Index (Apr)	-0.3%	-0.6%	-0.3%	Large decline.
EC	CPI (Apr, y/y, final)	2.4%	2.4%	2.4%	As already reported.
FR	ILO Mainland Unemployment Rate (Q1)	7.3%	7.3%	7.3%	Steady.

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

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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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