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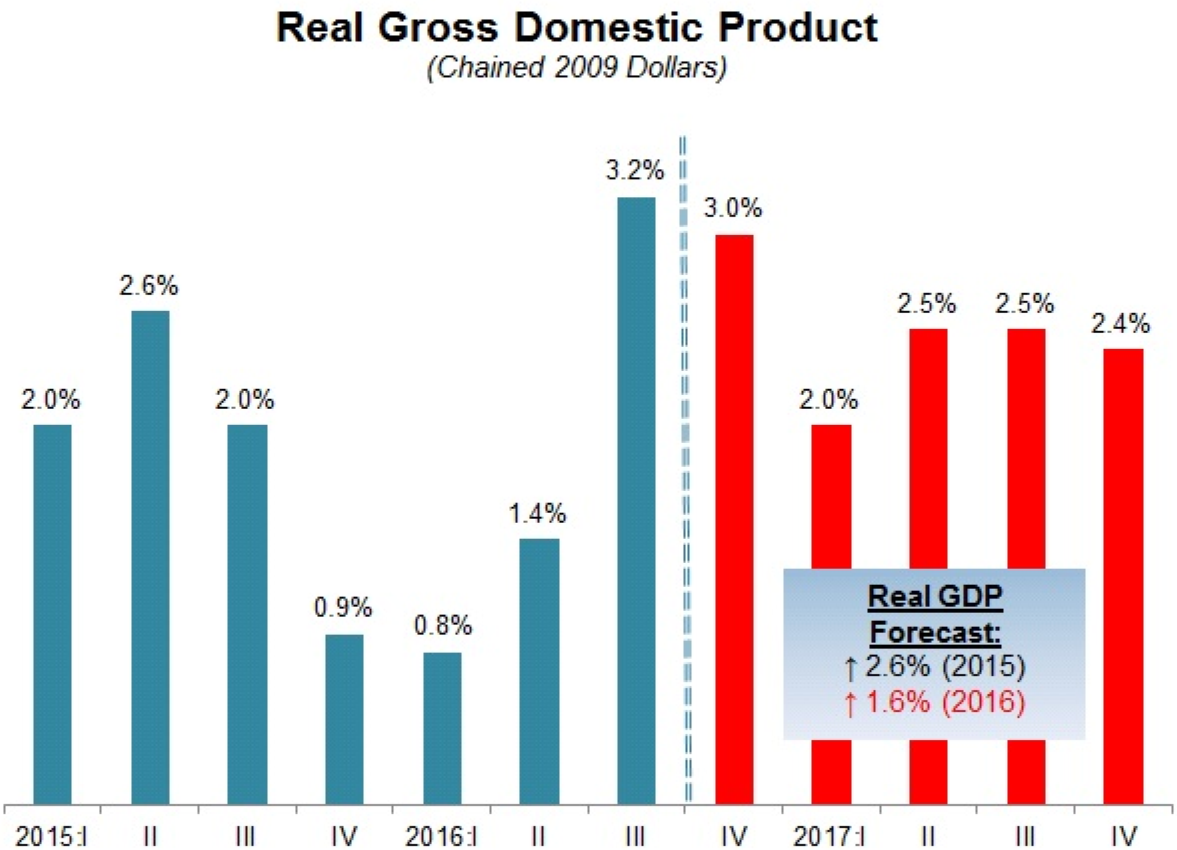
Monday Economic Report

December 5, 2016



We have seen a steady stream of good economic numbers in the past few weeks, and the data that came out last week was no exception. First and foremost, strong consumer spending helped push real GDP growth higher, to a revised 3.2 percent in the third quarter. Original estimates set the growth at 2.9 percent, with both figures marking the fastest quarterly growth rate in two years. Overall, this report was good news. With the U.S. economy expanding by only 1.1 percent at the annual rate in the first half of 2016, the third quarter numbers were entirely welcome, especially for consumer spending and net exports. Business investment remains a concern, but will hopefully recover moving forward with improvement confidence. In the end, real GDP will grow by 1.6 percent in 2016, but I expect stronger activity next year, with the current forecast being 2.5 percent growth.

Consumer confidence soared in November to its highest level since July 2007, according to the Conference Board, bouncing back from a pre-election lull in the October report. This mirrored a similar post-election rise in sentiment seen in the competing survey from the University of Michigan and Thomson Reuters. This should serve as good news for retailers — and by extension, manufacturers — for the holidays. Indeed, personal spending rose for the second straight month in October, albeit slower than in September, with 4.2 percent growth year-over-year. That suggests that Americans have been more willing to open their pocketbooks in recent months relative to a more-cautious approach seen earlier in the year. At the same time, consumers have benefited from rising personal income, up 0.6 percent in October, its fastest pace of growth since April. Over the past 12 months, personal incomes have risen 3.9 percent, a nine-month high and definite progress from the 3.4 percent pace seen in August.

Meanwhile, the indicators for manufacturing were mixed. On the positive side, the Institute for Supply Management's (ISM) Manufacturing Purchasing Managers' Index (PMI) rebounded once again in November, growing at a five-month high. The composite index rose from 51.9 in October to 53.2 in November, expanding for the third straight month. This is encouraging for a sector that has seen subpar growth over much of the past two years on global headwinds and economic anxieties. Indeed, manufacturing production (up from 54.6 to 56.0) in November expanded at its fastest clip since July 2015, with new orders (up from 52.1 to 53.0) also accelerating slightly. Exports (down from 52.5 to 52.0) and employment (down from 52.9 to 52.3) slowed a little for the month but remained positive, with hiring expanding for only the third time this year so far. In a similar manner, the Dallas Federal Reserve Bank reported that manufacturing activity expanded in November at its fastest rate since July 2014, representing notable improvement after contracting for 22 straight months.

Turning to the labor market, the unemployment rate fell to 4.6 percent, its lowest level since August 2007. At the same time, nonfarm payrolls rose by 178,000, which was on par with the consensus estimate of around 180,000. This should help cement a Federal Reserve rate hike at its upcoming meeting on December 13 and 14. Despite these positives, manufacturers have continued to struggle, as evidenced by the loss of 4,000 workers in November, with 60,000 fewer workers on net year-to-date. Employment in the sector has now declined for four straight months. Moving forward, manufacturing leaders are cautiously optimistic about demand and production for 2017, and we would expect that this increase in activity would lead to additional hiring.

Beyond jobs, manufacturers were also cautious about construction spending in October, with activity pulling back for the second straight month. The value of construction put in place in the sector declined 2.4 percent from September to October. While manufacturing construction has trended higher in the past several years, largely from increased investment in the chemical sector, activity has stalled more recently as manufacturing grapples with sluggish growth and economic and political anxieties. Along those lines, construction activity in the manufacturing sector has pulled sharply lower since achieving the all-time high in September 2015. As with hiring, we would expect construction investment to improve as we move into 2017, especially given strengthening demand and better confidence figures.

Given the economic headwinds seen globally over the past few years, we will be looking for signs of progress on the export front this week. For its part, net exports were a bright spot in the most recent GDP data for the third quarter, making the U.S. trade report from the Census Bureau one of the economic highlights of the week. Other indicators to watch include the most recent figures for consumer confidence, consumer credit, factory orders and shipments, and job openings and labor productivity.

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Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, November 28
Dallas Fed Manufacturing Survey

This Week's Indicators:

Monday, December 5
None

Tuesday, November 29
Conference Board Consumer Confidence
Gross Domestic Product (Revision)

Wednesday, November 30
ADP National Employment Report
Personal Income and Spending

Thursday, December 1
Construction Spending
ISM Manufacturing Purchasing Managers' Index

Friday, December 2
BLS National Employment Report

Tuesday, December 6
Factory Orders and Shipments
International Trade Report
Productivity and Costs (Revision)

Wednesday, December 7
Consumer Credit
Job Openings and Labor Turnover Survey

Thursday, December 8
None

Friday, December 9
University of Michigan Consumer Sentiment

Summaries for Last Week`s Economic Indicators

ADP National Employment Report
ADP reported that manufacturing employment growth remained weak in November, with hiring in the sector down in 9 of the 11 months so far this year. November, there were 10,000 fewer workers on net for manufacturers, which continue to be challenged by global headwinds and economic anxieties. Overall, employment in the sector is down by 46,000 year-to-date, according to ADP. This suggests that manufacturers remain wary about adding to their workforce, particularly with sluggish growth in demand and production. Yet, job openings and sentiment surveys have been more favorable as of late, which could indicate better hiring growth moving forward when manufacturers become less cautious.

Meanwhile, nonfarm payroll employment rose by 216,000 in November, its fastest monthly pace since June and well above the consensus estimate of 165,000. The year-to-date average is currently 176,000, down from the 2015 pace of 209,000 per month. In November, goods-producing employment mostly declined, largely due to manufacturing (down 10,000) and mining (down 1,000), but construction hiring edged up by 2,000 for the month. In the service-providing sectors, the largest gains were in trade, transportation and utilities (up 69,000), professional and business services (up 68,000), education and health services (up 43,000) and leisure and hospitality (up 38,000). Small and medium-sized businesses (e.g., those with less than 500 employees) accounted for more than 58.3 percent of all net new workers in November.

BLS National Employment Report
We have seen a steady stream of good economic numbers in the past few weeks, including the latest jobs numbers. First and foremost, the unemployment rate fell to 4.6 percent, its lowest level since August 2007. At the same time, nonfarm payrolls rose by 178,000, which was on par with the consensus estimate of around 180,000. Overall, this mirrors healthier figures for consumer spending and improved business sentiment in recent data, which show that the U.S. economy has strengthened. This should help cement a Federal Reserve rate hike at its upcoming meeting on December 13 and 14.

Despite these positives, manufacturers have continued to struggle, as evidenced by the loss of 4,000 workers in November, with 60,000 fewer workers on net year-to-date. It was the fourth straight monthly decline for employment in the sector. Moving forward, manufacturing leaders are cautiously optimistic about demand and production for 2017, and we would expect this increase in activity to lead to additional hiring.

Digging further into the November data, nondurable goods firms added 2,000 workers on net for the month, but this was offset by a decline of 4,000 workers among durable goods manufacturers. The largest declines were seen in the machinery (down 3,900), plastics and rubber products (down 2,200), printing and related support activities (down 2,100), fabricated metal products (down 1,600) and transportation equipment (down 1,300). The latter was off despite an increase of 1,200 workers for motor vehicles and parts. Other areas with higher employment in November included miscellaneous nondurable goods manufacturing (up 3,600), food manufacturing (up 1,600), chemicals (up 1,000) and computer and electronic products (up 900).

Average weekly earnings in manufacturing edged lower, down from $1,075.08 in October to $1,063.31 in November. On a year-over-year basis, average weekly earnings have increased from $1,038.66 in November 2015, up 2.4 percent for the 12-month period. Average weekly hours were also off, declining from 40.8 hours to 40.6 hours, with average overtime hours unchanged at 3.3 hours.

Conference Board Consumer Confidence

Consumer confidence soared in November to its highest level since July 2007, according to the Conference Board, bouncing back from a pre-election lull in the October report. The Consumer Confidence Index jumped from 100.8 in October to 107.1 in November. This mirrored a similar post-election rise in sentiment seen in the competing survey from the University of Michigan and Thomson Reuters. More importantly, it represented a significant improvement in Americans' assessments of the economy since May's dismal 92.4 reading. The underlying data noted progress in the public's perceptions about both current (up from 123.1 to 130.1) and future (up from 86.0 to 91.7) conditions. The measure for the present economic environment also reached its loftiest level since July 2007, with the expectations index climbing to a 17-year high. As noted in the press release, this report should serve as good news for retailers — and by extension, manufacturers — for the holidays.

Reflecting this optimism among consumers, 29.2 percent of those responding said that business conditions were currently "good," up from 26.5 percent in the prior survey. In addition, the percentage feeling that conditions were "bad" declined from 17.3 percent to 14.8 percent. Along those lines, the percentage of respondents saying that jobs were "plentiful" improved from 25.3 percent to 26.9 percent, with those feeling that jobs were "hard to get" unchanged at 21.7 percent. Meanwhile, the percentage expecting their incomes to decrease dropped from 10.2 percent to 9.0 percent. This corresponded to a marginal gain in respondents anticipating higher incomes, up from 17.4 percent to 17.5 percent.

Construction Spending

The Census Bureau reported that private manufacturing construction spending remained cautious in October, pulling back for the second straight month. The value of construction put in place in the sector declined from $75.19 billion in September to $73.37 billion in October, down 2.4 percent for the month. While manufacturing construction has trended higher in the past several years, largely from increased investment in the chemical sector, activity has stalled more recently as the sector grapples with sluggish growth and economic and political anxieties. Along those lines, construction activity in the manufacturing sector has pulled sharply lower since achieving the all-time high of $82.15 billion in September 2015.

As a whole, private nonresidential construction spending dipped 2.1 percent in October, but with year-over-year growth of 4.7 percent. This report showed increased construction spending in the transportation (up 5.1 percent) and communication (up 3.7 percent) sectors, but decreases in most other segments. Outside of manufacturing, the largest declines in October were seen in the religious (down 10.6 percent), power (down 4.3 percent), educational (down 3.4 percent), health care (down 3.3 percent), lodging (down 2.1 percent) and office (down 2.0 percent) sectors.

Meanwhile, private residential construction spending increased 1.6 percent in October, with 4.7 percent growth over the past 12 months. For the month, both single-family and multifamily construction activity rose by 2.8 percent. Yet, the year-over-year growth stemmed from the multifamily segment, up 11.4 percent since October 2015, with single-family construction down 1.6 percent over that time frame. Public construction spending also increased 2.8 percent in October, but with a 0.6 percent decrease year-over-year.

Dallas Fed Manufacturing Survey

Respondents to the Dallas Federal Reserve Bank's Manufacturing Survey said that manufacturing activity expanded in November at its fastest rate since July 2014. The composite index of general business conditions increased from -1.5 in October to 10.2 in November, representing notable improvement after contracting for 22 straight months. A fair share of this gain likely stemmed from a post-election boost in optimism. As one survey respondent said, "There is a great deal of optimism from our customers that the new pro-growth and lower-tax focus by the incoming administration will be a positive change from the past eight years." Indeed, indices for production (up from 6.7 to 8.8), capacity utilization (up from 0.8 to 3.6), employment (up from 0.2 to 4.5) and hours worked (up from -1.8 to 2.5) all ticked up in November, which was encouraging.

With that said, the data show lingering concerns — proof that the manufacturing sector is not completely out of the woods yet. For instance, new orders (up from -3.5 to -1.4) remained in contraction territory despite stabilizing a little. The new orders index has been negative in 9 of the 11 months so far in 2016, suggesting some persistent caution in demand. Shipments (down from 1.9 to -1.9) also fell in November, and capital expenditures (down from 8.7 to 2.0) eased. On the positive side, investment activity expanded for the third consecutive month.

Moving forward, manufacturing leaders were mostly positive about the next six months. The forward-looking measure jumped from 4.8 to 31.6, to nearly a six-year high. More than half of respondents see new orders, production, shipments and capacity utilization rising in the months ahead. At the same time, 37.1 percent and 37.3 percent anticipate greater capital spending and hiring, respectively, over the next six months.

Gross Domestic Product (Revision)

The Bureau of Economic Analysis reported that strong consumer spending helped push real GDP growth higher, to a revised 3.2 percent in the third quarter. Original estimates set the growth at 2.9 percent, with both figures marking the fastest quarterly growth rate in two years. Overall, this report was good news. With the U.S. economy expanding by only 1.1 percent at the annual rate in the first half of 2016, the third quarter numbers were entirely welcome, especially for consumer spending and net exports. Business investment remains a concern, but, hopefully, will recover with improved confidence. In the end, real GDP will grow by 1.6 percent in 2016, but I expect stronger activity next year, with the current forecast being 2.5 percent growth.

Personal consumption expenditures added 1.89 percentage points to headline growth in this latest report, up from 1.47 percent in the prior release. Consumer spending on goods increased 3.4 percent at the annual rate in the third quarter, boosted by strength in durable goods purchases, including motor vehicles. Service sector consumption also improved with this revision, with Americans increasing their spending on services modestly in the third quarter, up 2.5 percent. Yet, nondurable goods spending continued to be a slight drag on growth.

Net exports marked another bright spot in the third quarter, contributing 0.87 percent to real GDP, up slightly from 0.83 percent in the advance estimate. It remained the largest contribution for net exports since the fourth quarter of 2013. In the third quarter, goods exports jumped an annualized 14.2 percent, with goods imports edging up 0.7 percent. This was notable, especially given the challenges many manufacturers have had in growing export sales in light of dollar and global headwinds. On a year-over-year basis, goods exports have risen 2.6 percent.

Meanwhile, business spending remained weaker than desired, mirroring recent cautiousness seen in other economic indicators. Nonresidential fixed investment increased marginally, up just 0.1 percent at the annual rate in the third quarter. Spending on structures rebounded strongly (up 10.1 percent), but investments in equipment (down 4.8 percent) contracted for the fourth straight quarter. At the same time, residential investment declined for the second consecutive quarter, down 4.4 percent. In total, fixed investment contracted 0.9 percent in the third quarter, subtracting 0.15 percentage points from headline GDP growth. On the positive side, business inventory spending picked up, adding 0.49 percentage points. That followed five straight quarters where inventory spending was a drag on real GDP activity.

ISM Manufacturing Purchasing Managers' Index

The Institute for Supply Management's (ISM) Manufacturing Purchasing Managers' Index (PMI) rebounded once again in November, growing at a five-month high. The composite index rose from 51.9 in October to 53.2 in November, expanding for the third straight month. This is encouraging for a sector that has seen subpar growth over much of the past two years on global headwinds and economic anxieties. Indeed, manufacturing production (up from 54.6 to 56.0) in November expanded at its fastest clip since July 2015, with new orders (up from 52.1 to 53.0) also accelerating slightly. Exports (down from 52.5 to 52.0) and employment (down from 52.9 to 52.3) slowed a little for the month but remained positive, with hiring expanding for only the third time this year so far.

Overall, manufacturers appear to be more upbeat in their assessments of the economy and about demand. The sample comments tend to echo this. One computer and electronic products leader reported, "Strong manufacturing numbers in anticipation of strong year-end bookings." Other comments also mirrored that positive trend, describing activity as "steady," "consistent" or "good."

Meanwhile, inventories (up from 47.5 to 49.0) contracted for the 17th consecutive month, albeit with some easing in this release. The silver lining is that this could provide a stimulative effect for growth in the coming months, as manufacturers will need to increase production to meet additional demand, with stockpiles quite low. In addition, input prices (unchanged at 54.5) continued to expand modestly but have slowed from mid-year, when the raw material prices index stood at 63.5 in June.

Personal Income and Spending

According to the Bureau of Economic Analysis, personal incomes rose 0.6 percent in October, its fastest monthly pace of growth since April. On a year-over-year basis, personal incomes have increased 3.9 percent, a nine-month high and definite progress from the 3.4 percent pace seen in August. At the same time, total manufacturing wages and salaries increased from $834.4 billion in September to $840.6 billion in October. Overall, manufacturing wages and salaries have trended in the right direction, up from the $780.0 billion and $806.7 billion averages of 2014 and 2015, respectively.

Meanwhile, personal spending increased 0.3 percent in October, rising for the second straight month but slowing from the 0.7 percent gain observed in September. Durable and nondurable goods purchases rose 1.0 percent and 1.4 percent, respectively, for the month. This included decent growth in spending for food and beverages purchased for the home, motor vehicles and parts, and recreational goods and vehicles. In general, Americans have been more willing to open their pocketbooks in recent months relative to a more-cautious approach seen earlier in the year. Along those lines, personal consumption expenditures grew 4.2 percent year-over-year in October, up from 2.9 percent in March, hitting its quickest pace since January 2015.

Still, with eased spending for the month, the personal savings rate ticked back up from 5.7 percent in September to 6.0 percent in October. That is consistent with the year-to-date average through October.

In other news, the personal consumption expenditure (PCE) deflator increased 0.2 percent in October, the same pace as seen in both August and September. Higher energy costs were enough to outpace stagnant food costs. Core inflation, which excludes food and energy, inched up 0.1 percent in October. While pricing pressures remain minimal for now, they are also picking up. The PCE increased 1.4 percent year-over-year in October, up from 0.8 percent in June. Core inflation has risen 1.7 percent this year, matching the rate seen in the past two months.

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