U.S. Economic Comment

- Employment: strong payroll growth in September, albeit with caveats
- Labor market data keep open the prospect of a hike at the Oct/Nov FOMC meeting
- Wages: hints of moderation

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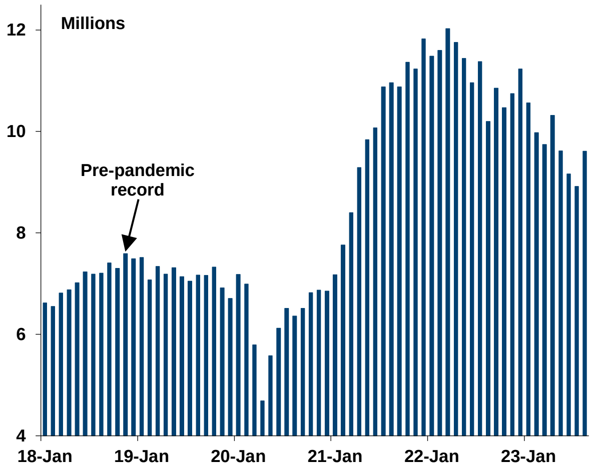
September Employment

Expectations for payroll growth in September were mixed heading into Friday's employment report. On the one hand, the Job Openings and Labor Turnover survey released on Tuesday indicated that demand for labor picked up after falling in six of the previous seven months. Openings were below the record of 12.0 million in March 2022, but at 9.6 million in August they remained well above the pre-COVID high of 7.6 million in November 2018 (chart, left). In addition, layoffs appeared contained, as initial claims rose by only 2k to 207,000 in the final week of September. The average of 210,000 for last month was 24,000 below the August average and a bit below levels that prevailed before the onset of pandemic-related shutdowns. Alternatively, arguments could be made for a soft report. Payroll growth had previously averaged 150,000 per month in the three months ended August, and a low-side reading of 89,000 private-sector jobs added in September reported on Wednesday in the ADP National Employment Report raised the possibility of sluggish payroll growth reported in the official statistics. Ultimately, the earlier data signaling firm labor market activity were ratified, as payroll growth in September smashed expectations (+336,000 versus the Bloomberg consensus estimate of +170,000) and results in the prior two months were revised higher by a combined 119,000 (chart, right).

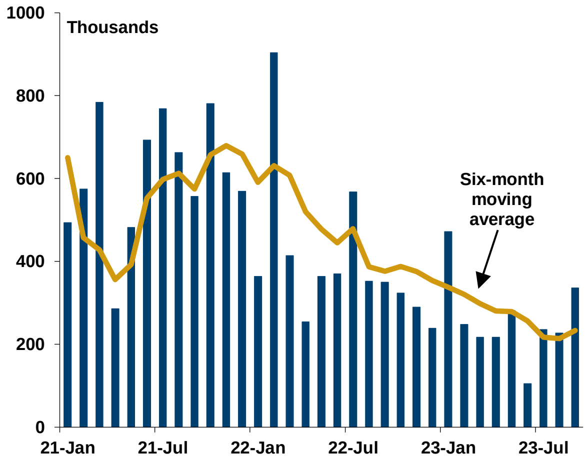
Although the aggregate results on payroll employment were strong, we viewed several elements of the data as suggesting that the near-term burst is unsustainable over a more prolonged period. In the private sector, we were struck by job growth of 96,000 in the leisure and hospitality area out of 263,000 total jobs, the sharpest increase since a jump of 99,000 in January 2023 (chart, next page, top right). Establishments in this category hired aggressively amid chronic labor shortfalls as life returned to normal post-COVID. However, hiring had slowed steadily from average monthly increases of 206,000 in 2021 to 88,000 last year and 44,000 through August. Moreover, 60,700 of the jobs in the leisure and hospitality area were added by bars and restaurants – below the high of the year of 81,500 in January but well above the average of 22,000 in the February-to-August period. Thus, the results strike us as either random volatility amid a decelerating trend, or unsustainable over the coming months. Concerning the sustainability of the positions added, we view dining out as a discretionary activity that is often curtailed if budgets are strained. Should the economy slow entering 2024, which is our baseline view, many of these positions would be rapidly eliminated.

Job Openings



Source: Bureau of Labor Statistics via Haver Analytics

Change in Nonfarm Payrolls



Source: Bureau of Labor Statistics via Haver Analytics

We also view with some skepticism the staying power of hiring by state and local governments. These two areas added a combined 67,000 positions in September after increases of 39,000 in August and 81,000 in July (chart, middle right). The recent data show a marked increase from the average of 23,000 per month in 2022 and 44,000 per month in the first half of 2023. Such a brisk increase in hiring seems counterintuitive amid concerns about a potential economic slowdown stemming from recent monetary policy action. The more likely explanation, we suspect, is that previously unspent aid to states from pandemic-related federal legislation is only now being deployed. If this is the case, the burst in hiring should ebb as the funds are depleted. Moreover, cyclical influences (slowing tax revenues amid easing in economic activity) could again take hold.

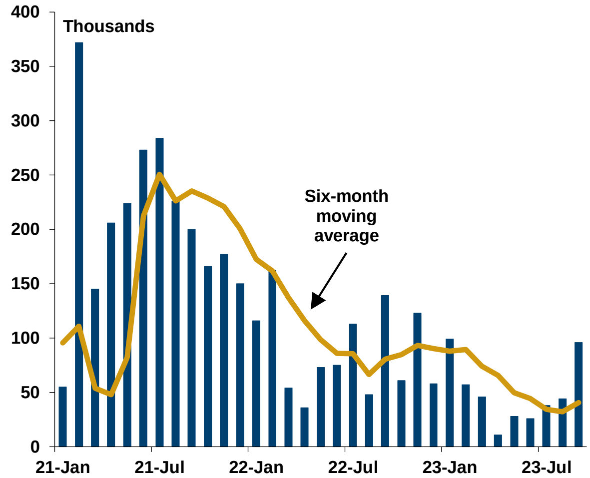
Data Dependence & the Upcoming FOMC Meeting

Based on our read of the payroll data, we suspect that job gains in September overstated the underlying strength of the labor market. However, the increase taken in context with other employment-related indicators is likely too robust for Fed officials to ignore. Thus, barring a low-side surprise on the CPI next Thursday (perhaps a 0.1 percent print for core), we view the odds as slightly favoring a 25-basis-point hike at the upcoming FOMC meeting. Fed officials have noted in recent remarks that supply and demand in the labor market have come into better balance, although the recalibration process is ongoing. We view the latest round of data as a partial setback to this narrative. Demand for labor remains high, and the latest reading on the unemployment rate (3.8 percent; unchanged from that in August) indicates what could be considered a fully employed economy. Moreover, a plateau in the prime-age labor force participation rate in recent months implies that there is little additional labor supply on the sidelines (chart, bottom right). If Fed officials want the labor market to cool further, additional policy restraint beyond what is currently in the pipeline may be required.

Average Hourly Earnings: Hope for the Doves?

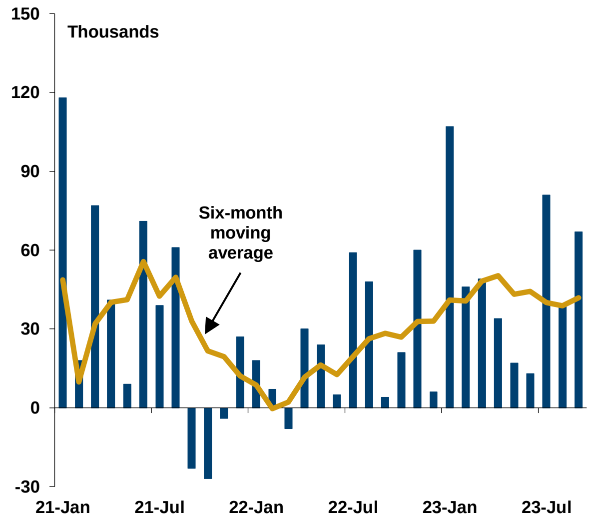
Average hourly earnings rose 0.2 percent for the second consecutive month, suggesting a potential easing in wage growth despite brisk hiring intensifying otherwise tight labor market conditions (chart, next page, left). The moderate advance led to a year-over-year increase of 4.2 percent, down one tick from the August reading and well below the recent high of 5.9 percent in March 2022 (chart, next page, right).

Change in Leisure & Hospitality Payrolls



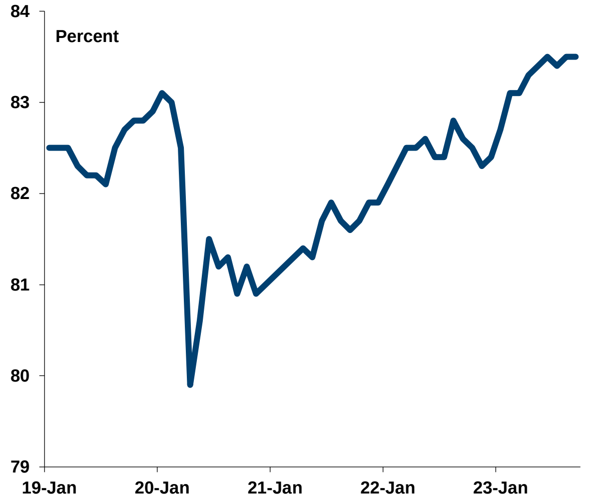
Source: Bureau of Labor Statistics via Haver Analytics

Change in State & Local Government Payrolls



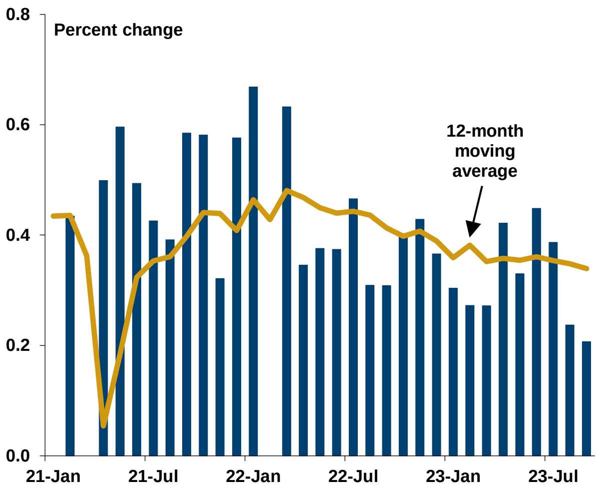
Source: Bureau of Labor Statistics via Haver Analytics

Prime-Age Labor Force Participation Rate*



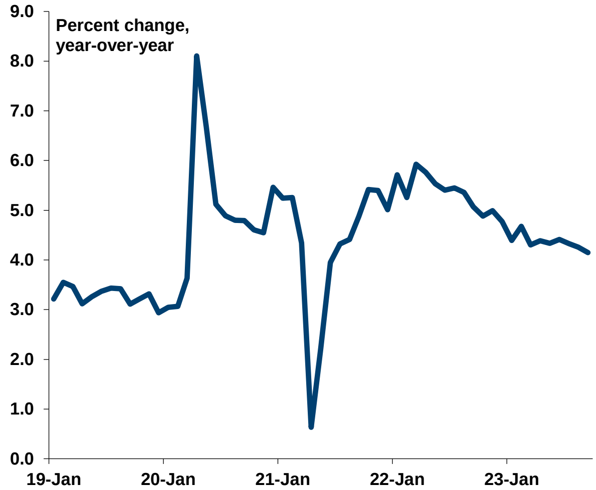
** Labor force participants aged 25 to 54 as a share of the civilian non-institutional population aged 25 to 54.*
Source: Bureau of Labor Statistics via Haver Analytics

Average Hourly Earnings



Source: Bureau of Labor Statistics via Haver Analytics

Average Hourly Earnings



Source: Bureau of Labor Statistics via Haver Analytics

While the near-term slowing could be viewed as sufficient evidence to argue for a pause in rate hikes, possibly indicating that current labor markets are aligned to allow for a gradual slowing in wage pressure or even suggesting that underlying demand is softer than implied by current data, we remain skeptical. We readily acknowledge that year-over-year shifts can obscure near-term progress, but we would emphasize that wage growth is still at least 100 basis points faster than what is viewed as consistent with the two-percent inflation target (approximately 3.0 percent; inflation target plus trend productivity growth). Additionally, month-to-month shifts can be volatile, and they may be influenced by compositional shifts in hiring rather than actual wage changes (i.e. an increase in jobs at a particular point in the wage spectrum – low-paying leisure and hospitality jobs, for instance – rather than actual acceleration or deceleration in wage rates). Moreover, we view recent anecdotal evidence as favoring workers in wage negotiations. Employees of UPS secured large pay increases after tense negotiations, and UAW-affiliated autoworkers may do the same in the coming weeks. In addition, Bank of America recently announced pay increases for low-tier workers, as did Amazon for transportation and warehousing employees. We view the leverage of unions in negotiations and voluntary wage increases by large employers as evidence of continued tightness in labor markets.

Thankfully, the Employment Cost Index, which we view as a better measure of wage trends, will be released on the first day of the upcoming FOMC meeting. This metric, a fixed-weight measure, is immune to compositional shifts in the workforce and more accurately tracts labor costs for the same jobs over time. This measure showed year-over-year compensation growth of 4.5 percent in Q2, down from a recent high of 5.1 percent in 2022-Q2; wage growth came in at 4.6 percent year-over-year, also slower than 5.2 percent in Q2 of last year. Q3 results for this metric will provide needed clarity to FOMC participants ahead of their decision.

The Week Ahead

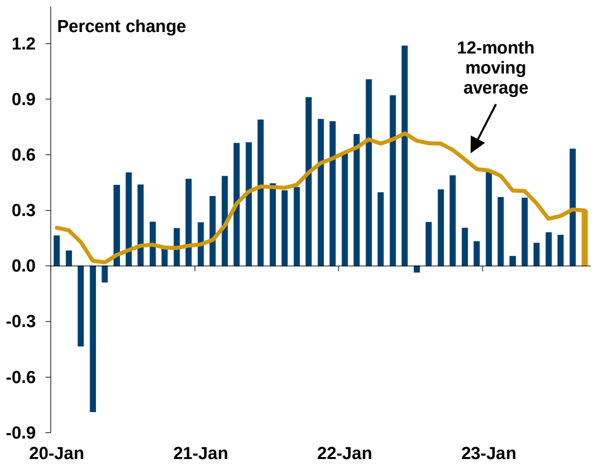
PPI (September) (Wednesday)
Forecast: Forecast: 0.2% Final Demand, 0.2% Ex. Food & Energy

Available data suggest that energy prices at the producer level rose moderately during the September survey period. Food prices at the producer level are often volatile, although they have declined in seven of the past nine months, including a drop of 0.5 percent in August. Core goods prices have increased 0.1 percent per month, on average, in the past six months; service prices have advanced at a slightly faster pace – 0.2 percent. Construction costs have averaged monthly declines of 0.2 percent per month in the past six months.

CPI (September) (Thursday)
Forecast: 0.3% Total, 0.3% Core

Gasoline prices were little changed during the September survey period, but the energy component could increase after seasonal adjustment (although by much less than the surge of 5.6 percent in August). In addition, the increase in food prices is likely to be closer to the 0.2 percent average increase in 2023 thus far than the 0.8 percent per month average in 2022. The core component could increase 0.3 percent for the second consecutive month after back-to-back advances of less than 0.2 percent in June and July (chart, right). While airline fares could ease after a jump of 4.9 percent in August, costs of owner-occupied housing and rents are still advancing at a brisk clip (0.4 percent and 0.5 percent, respectively, in August), as are insurance costs. Moreover, hotel/motel fees face upside risks after a cumulative drop of 7.7 percent in the past five months.

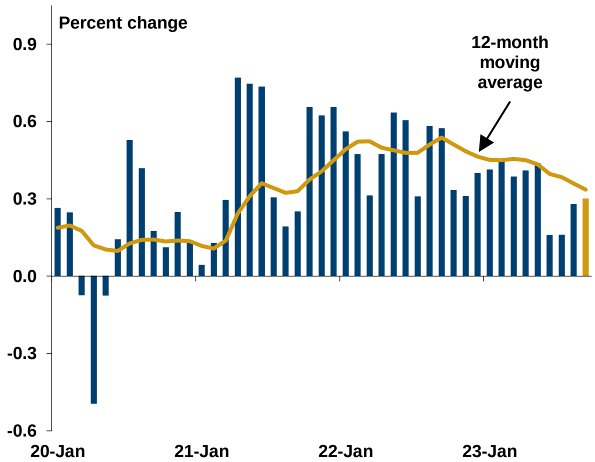
Headline CPI*



** The gold bar is a forecast for September 2023.*

Sources: Bureau of Labor Statistics via Haver Analytics; Daiwa Capital Markets America

Core CPI*



** The gold bar is a forecast for September 2023.*

Sources: Bureau of Labor Statistics via Haver Analytics; Daiwa Capital Markets America

Federal Budget (September) (Thursday)
Forecast: $150.0 Billion Deficit

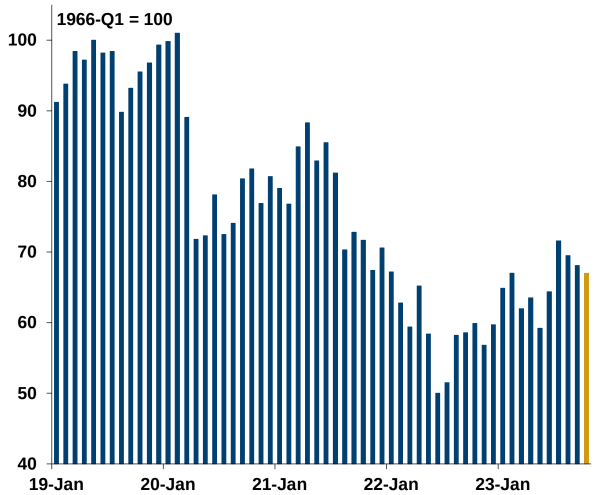
The release of September budget results by the U.S. Treasury Department will provide insight on the fiscal position of the federal government for the entirety of FY2023. Results thus far are not encouraging, as revenues have fallen almost 10 percent year-to-date while outlays have increased by a bit less than three percent. The brisk spending and softening revenue flows have contributed to a deficit of $1.52 trillion in the first 11 months of the fiscal year, a result that already eclipsed the full-year deficit of $1.38 trillion for FY2022. The anticipated deficit for September would push the shortfall for the full 12 months of FY2023 to $1.67 trillion. Please note that budget results for the final month of the fiscal year are often delayed from the anticipated release date.

Consumer Sentiment (October) (Friday)
Forecast: 67.0 (-1.1 Index Points or 1.6%)

Higher borrowing costs amid a surge in interest rates and gasoline prices approaching $4.00 per gallon could weigh on attitudes in early October (chart, left).

Keep an eye on the year-ahead and long-term inflation expectations measures published with the Michigan report. Year-ahead inflation expectations fell 0.3 percentage point to 3.2 percent in September, the lowest reading since the spring of 2021, while long-term expectations eased 0.2 percentage point to 2.8 percent (chart, right).

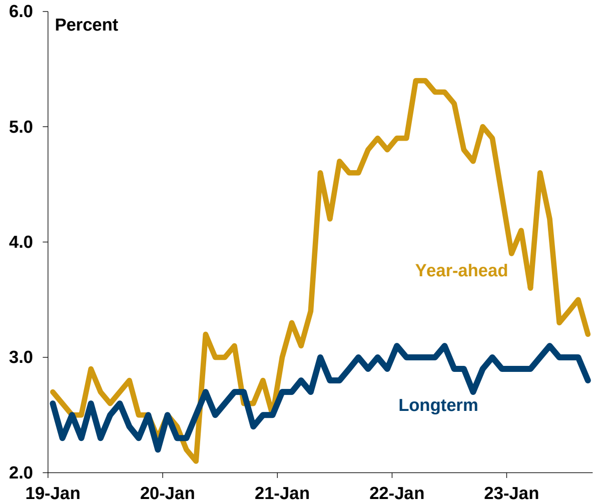
Consumer Sentiment*



** The gold bar is a forecast for October 2023.*

Sources: University of Michigan via Haver Analytics; Daiwa Capital Markets America

Consumer Inflation Expectations



Source: University of Michigan via Haver Analytics

Daiwa Capital Markets

Economic Indicators

October 2023

Monday	Tuesday	Wednesday	Thursday	Friday
2	3	4	5	6
ISM MFG. INDEX Index Prices July 46.4 42.6 Aug 47.6 48.4 Sep 49.0 43.8 **CONSTRUCTION** June 0.5% July 0.9% Aug 0.5%	**JOLTS DATA** Openings (000) Quit Rate June 9,165 2.4% July 8,920 2.3% Aug 9,610 2.3% **VEHICLE SALES** July 15.9 million Aug 15.3 million Sep 15.7 million	**ADP EMPLOYMENT** Private Payrolls July 312,000 Aug 180,000 Sep 89,000 **ISM SERVICES INDEX** Index Prices July 52.7 56.8 Aug 54.5 58.9 Sep 53.6 58.9 **FACTORY ORDERS** June 2.3% July -2.1% Aug 1.2%	**UNEMPLOYMENT CLAIMS** Initial Continuing (millions) Sep 9 0.221 1.658 Sep 16 0.202 1.665 Sep 23 0.205 1.664 Sep 30 0.207 N/A **TRADE BALANCE** June -$63.7 billion July -$64.7 billion Aug -$58.3 billion	**EMPLOYMENT REPORT** Payrolls Un. Rate July 236,000 3.5% Aug 227,000 3.8% Sep 336,000 3.8% **CONSUMER CREDIT** June $13.8 billion July $11.0 billion Aug -$15.6 billion
9	10	11	12	13
COLUMBUS DAY	**NFIB SMALL BUSINESS OPTIMISM INDEX (6:00)** July 91.9 Aug 91.3 Sep -- **WHOLESALE TRADE (10:00)** Inventories Sales June -0.7% -0.8% July -0.2% 0.8% Aug -0.1% 0.2%	**PPI (8:30)** Final Demand Ex. Food & Energy July 0.4% 0.4% Aug 0.7% 0.2% **Sep 0.2% 0.2%** **FOMC MINUTES (2:00)**	**UNEMP. CLAIMS (8:30)** **CPI (8:30)** Total Core July 0.2% 0.2% Aug 0.6% 0.3% **Sep 0.3% 0.3%** **FEDERAL BUDGET (2:00)** 2023 2022 July -$220.8B -$211.1B Aug $89.3B -$219.6B **Sep -$150.0B** -$429.8B	**IMPORT/EXPORT PRICES (8:30)** Non-Petrol Imports Nonagri. Exports July 0.0% 0.6% Aug 0.0% 1.7% Sep -- -- **CONSUMER SENTIMENT (10:00)** Aug 69.5 Sep 68.1 **Oct 67.0**
16	17	18	19	20
EMPIRE MFG	**RETAIL SALES** **IP & CAP-U** **NAHB HOUSING INDEX** **BUSINESS INVENTORIES** **TIC FLOWS**	**HOUSING STARTS** **BEIGE BOOK**	**UNEMP. CLAIMS** **PHILLY FED INDEX** **EXISTING HOME SALES** **LEADING INDICATORS**	
23	24	25	26	27
CHICAGO FED NATIONAL ACTIVITY INDEX		**NEW HOME SALES**	**UNEMP. CLAIMS** **GDP** **DURABLE GOODS ORDERS** **INTERNATIONAL TRADE IN GOODS** **ADVANCE INVENTORIES** **PENDING HOME SALES**	**PERSONAL INCOME, CONSUMPTION, AND CORE PRICE INDEX** **REVISED CONSUMER SENTIMENT**

Forecasts in bold.

Treasury Financing

October 2023

Monday	Tuesday	Wednesday	Thursday	Friday
2	3	4	5	6
AUCTION RESULTS: Rate Cover 13-week bills 5.345% 2.77 26-week bills 5.340% 2.88 **SETTLE:** $13 billion 20-year bonds $48 billion 2-year notes $49 billion 5-year notes $37 billion 7-year notes	**AUCTION RESULTS:** Rate Cover 52-week bills 5.185% 3.21 42-day CMBs 5.330% 2.46 **ANNOUNCE:** $54 billion 17-week bills for auction on Oct 4 $90 billion 4-week bills for auction on Oct 5 $80 billion 8-week bills for auction on Oct 5 **SETTLE:** $52 billion 17-week bills $85 billion 4-week bills $75 billion 8-week bills	**AUCTION RESULTS:** Rate Cover 17-week bills 5.350% 2.96	**AUCTION RESULTS:** Rate Cover 4-week bills 5.310% 2.95 8-week bills 5.355% 2.46 **ANNOUNCE:** $139 billion 13-,26-week bills for auction on Oct 10 $46 billion 3-year notes for auction on Oct 10 $35 billion 10-year notes for auction on Oct 11 $20 billion 30-year bonds for auction on Oct 12 $70 billion 43-day CMBs for auction on Oct 10 **SETTLE:** $135 billion 13-,26-week bills $44 billion 52-week bills $65 billion 42-day CMBs	
9	10	11	12	13
COLUMBUS DAY	**AUCTION:** $139 billion 13-,26-week bills $46 billion 3-year notes $70 billion 43-day CMBs **ANNOUNCE:** $54 billion* 17-week bills for auction on Oct 11 $90 billion* 4-week bills for auction on Oct 12 $80 billion* 8-week bills for auction on Oct 12 **SETTLE:** $54 billion 17-week bills $90 billion 4-week bills $80 billion 8-week bills	**AUCTION:** $54 billion* 17-week bills $35 billion 10-year notes	**AUCTION:** $90 billion* 4-week bills $80 billion* 8-week bills $20 billion 30-year bonds **ANNOUNCE:** $139 billion* 13-,26-week bills for auction on Oct 16 $13 billion* 20-year bonds for auction on Oct 18 $22 billion* 5-year TIPS for auction on Oct 19 **SETTLE:** $139 billion 13-,26-week bills $70 billion 43-day CMBs	
16	17	18	19	20
AUCTION: $139 billion* 13-,26-week bills **SETTLE:** $46 billion 3-year notes $35 billion 10-year notes $20 billion 30-year bonds	**ANNOUNCE:** $54 billion* 17-week bills for auction on Oct 18 $90 billion* 4-week bills for auction on Oct 19 $80 billion* 8-week bills for auction on Oct 19 **SETTLE:** $54 billion* 17-week bills $90 billion* 4-week bills $80 billion* 8-week bills	**AUCTION:** $54 billion* 17-week bills $13 billion* 20-year bonds	**AUCTION:** $90 billion* 4-week bills $80 billion* 8-week bills $22 billion* 5-year TIPS **ANNOUNCE:** $139 billion* 13-,26-week bills for auction on Oct 23 $51 billion* 2-year notes for auction on Oct 24 $52 billion* 5-year notes for auction on Oct 25 $38 billion* 7-year notes for auction on Oct 26 $26 billion* 2-year FRNs for auction on Oct 25 **SETTLE:** $139 billion* 13-,26-week bills	
23	24	25	26	27
AUCTION: $139 billion* 13-,26-week bills	**AUCTION:** $51 billion* 2-year notes **ANNOUNCE:** $54 billion* 17-week bills for auction on Oct 25 $90 billion* 4-week bills for auction on Oct 26 $80 billion* 8-week bills for auction on Oct 26 **SETTLE:** $54 billion* 17-week bills $90 billion* 4-week bills $80 billion* 8-week bills	**AUCTION:** $54 billion* 17-week bills $52 billion* 5-year notes $26 billion* 2-year FRNs	**AUCTION:** $90 billion* 4-week bills $80 billion* 8-week bills $38 billion* 7-year notes **ANNOUNCE:** $139 billion* 13-,26-week bills for auction on Oct 30 $44 billion* 52-week bills for auction on Oct 31 **SETTLE:** $139 billion* 13-,26-week bills	

*Estimate