

## US Watch

## December employment: Simmering not boiling

**Gradual cooling in hiring**

The December employment report continued to show a gradual cooling in the labor market that is more consistent with a soft landing than a recession. Nonfarm payroll employment beat expectations with a 216k increase (consensus: 175k). However, there were net downward revisions of 71k to the prior two months continuing a trend seen throughout the year. As a result, the three-month average change in nonfarm payrolls declined from 221k in September to 165k in December. Moreover, the three-month average change for private payrolls fell to 115k in December from 153k in September. In other words, the pace of job growth is cooling.

**Government and healthcare**

Growth in payroll employment continues to be narrowly driven. Of the 216k increase, over half were in the government and healthcare sectors. These two sectors have accounted for close to 60% of 2023 job growth. They are also acyclical, and we think both could continue to drive employment over the coming months. Healthcare employment is supported by the structural aging of the US population and is still 4.3% below its pre-pandemic trend. Meanwhile, government employment is 2.4% below its pre-pandemic trend and state and local education is still below its pre-pandemic level.

**Bimodal services**

More generally, services employment and private employment was again driven by high-touch services—leisure and hospitality, education and health, and other services. These three sectors added 117 jobs in December, while low-touch services (services less high-touch) cut 20k jobs. This is the fifth consecutive month that low-touch services shed jobs, underscoring the narrowness of job growth seen in 2023. In short, there are pockets of weakness but that is being overwhelmed by the strength in a few sectors.

**Income growth supports slowing but positive spending**

Importantly for the consumer outlook, growth in wage income was solid in December as the aggregate payrolls index increased by 0.3% m/m. This is despite average weekly hours declining a tenth to 34.3 from 34.4, as strong payroll growth and a better-than-expected 0.4% m/m increase in average hourly earnings boosted payrolls. Taking a step back, aggregate payrolls rose by 4.5% annualized in 4Q, which likely helps explain the ongoing strength of the consumer.

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Macro  
United States

**US Economics**  
BofAS

**Michael Gapen**  
US Economist  
BofAS  
+1 646 855 3270  
[michael.gapen@bofa.com](mailto:michael.gapen@bofa.com)

**Stephen Juneau**  
US Economist  
BofAS  
+1 202 442 7429  
[stephen.juneau@bofa.com](mailto:stephen.juneau@bofa.com)

**US Rates Research**  
BofAS

**Meghan Swiber, CFA**  
Rates Strategist  
BofAS  
+1 646 743 7020  
[meghan.swiber@bofa.com](mailto:meghan.swiber@bofa.com)

**G10 FX Strategy**  
MLI (UK)

**Howard Du, CFA**  
G10 FX Strategist  
BofAS  
+1 646 743 7017  
[yuhao.du@bofa.com](mailto:yuhao.du@bofa.com)

[See Team Page for List of Analysts](#)

AHE: Average Hourly Earnings

k: thousand

PCE: personal consumption  
expenditure

saar: seasonally adjusted annual rate

UAW: United Auto Workers

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## A perplexing household report

After a strong November, the household survey was generally weak this month. Household employment, which we focus less on given its smaller sample compared to the establishment data, fell by 683k in December, more than reversing last month's increase. Moreover, the count of those not in the labor force rose by 845k, while unemployed only increased by 6k. Therefore, most of the drop in employment represented workers leaving the labor force. As a result, the labor force participation rate fell by three-tenths to 62.5%.

By age group the decline in the labor force participation rate was broad-based with the participation rate down for 16–24 (-0.4ppt), 25–54 (-0.1ppt), and 55+ (-0.4ppt). The decline in participation rate for those aged 25–54 bears watching as strong participation among this group has helped improve the balance between labor demand and supply. Over the last six months, participation of those 25–54 is down 0.3ppt, driven entirely by a seven-tenth decline in female participation. We'll be watching this trend closely to see if it continues as it could change the way we think about the balance in the labor market.

The decrease in the labor force also combined with the small increase in unemployment left the unemployment rate unchanged at 3.7%. Meanwhile, the duration of unemployed workers for 15 weeks or more did increase, mostly reversing the prior month's decline. The series has increased over the last six months suggesting that spells of unemployment are becoming longer. In our view, this is consistent with the data from JOLTS on the hiring rate and with the recent upward trend in continuing claims.

Last the updated seasonal factors and revisions to the household survey did little to change the narrative. The unemployment rate was little changed in 2023.

## Implications for the Fed

In terms of implications for the Fed, our view heading into the report was that a number broadly in line with consensus would not change the narrative or move market pricing of cuts much. We think the signal, on net, is consistent with this view. We think the overall tone of the report - despite the beat in headline payrolls - is supportive of the Fed's view that the labor market is coming into better balance.

At the private sector level, nearly all the gains in employment come from two sectors - leisure and hospitality and education and health - whereas growth in employment outside of these sectors has ground to a halt. Over the past six months, the change in private payrolls has averaged 134k, with 127k coming from these two sectors. It remains an open question as to how long the "catch-up effect" in high-touch services will continue and where employment growth will be when it fades. In addition, and despite the beat in average hourly earnings, slower hiring rates and a softer average work week mean slower growth in labor market income. While in line with our view that labor markets will remain healthy enough to keep consumers spending and the economy out of recession, the signal from labor markets seems to be one of a cooling economy.

We retain our view that the combination of activity data and inflation data will support the start of a gradual easing cycle in March. Our forecast for quarterly 25bp cuts in 2024 and 100bp for the year. We believe the Fed is invested in achieving a soft landing and is more balanced in its reaction function than it was before, taking on board the signal that the economy can grow at a modest pace while inflation continues to decelerate. If so, then appropriate policy could call for an early start to policy normalization, but also a gradual pace of normalization.

## Rates and FX: market reaction

The initial reaction from rates market sees the payroll report as modestly paring back the probability of early and swift Fed cuts. However, the weaker than expected ISM data reversed some of this reaction. Rates market now prices cuts in '24 of 143bps vs 135bps pre data and March is now priced closer to 72% probability for a 25bp cut vs 65% pre data. The selloff on non-farm payrolls (NFP) followed by the weaker ISM may

have encouraged investors to "buy the dip" as rates are still prone to rally as the Fed delivers on cuts. We hold our neutral duration stance after the significant rally on the Fed's pivot. However, we see near-term US rate risks as being skewed to the downside informed by risks to Fed outlook, historical patterns after the last Fed hike, and market pricing vs forwards.

The USD has sold off quite aggressively in December after the dovish FOMC. While we hold a medium-term bearish USD view, last month's selloff was faster than our expectation (see Global Macro Year Ahead: 19 November 2023). Into 2024, the USD has rallied back for 4 out of the past 5 sessions. We believe the combination of short USD profit-taking and a more balanced Fed minutes this week has been driving the pullback in the USD. Today's headline NFP surprise and higher than expected wage data should keep the USD supported for the time being. That being said, the 200d SMA at 103.43 for the DXY index should also serve as a strong resistance and the price action of the day became more balanced after the negative surprise from ISM Services Employment. For USD bears to re-engage with the lower USD view, we would pay attention to the US CPI data next week. Consensus forecast currently expects a moderate 0.2% MoM print for both headline and core CPI. A CPI release in-line with current consensus could lead to some renewed interest to short the USD again, in our view.

**Table 1: Summary of jobs data (most recent 6 months)**

Nonfarm payrolls have increased by an average of 193k over the last six months, but 165k over the last three

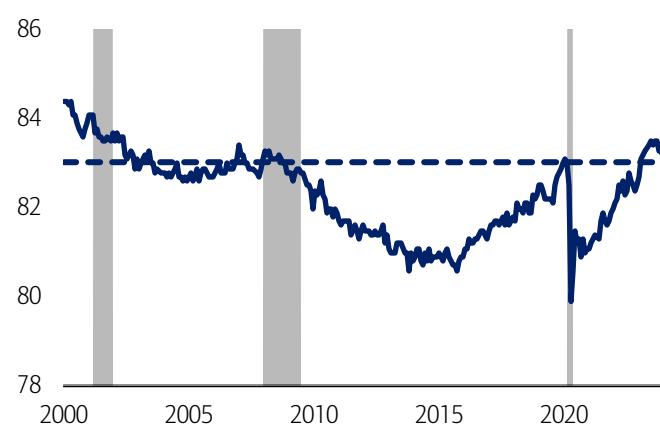
	Dec	Nov	Oct	Sep	Aug	Jul
<b>Establishment survey</b>						
Nonfarm payrolls	216k	173k	105k	262k	165k	236k
Private payrolls	164k	136k	44k	199k	114k	145k
Construction	17k	6k	27k	9k	30k	12k
Manufacturing	6k	26k	-38k	11k	-2k	-2k
Government	52k	37k	61k	63k	51k	91k
Average weekly hours	34.3	34.4	34.3	34.4	34.4	34.3
Avg hrly earnings (mom %)	0.4%	0.4%	0.3%	0.3%	0.3%	0.4%
<b>Household survey</b>						
Unemployment rate	3.7%	3.7%	3.8%	3.8%	3.8%	3.5%
Participation rate	62.5%	62.8%	62.7%	62.8%	62.8%	62.6%
Labor force	-676k	404k	-174k	57k	727k	113k
Household Jobs	-683k	586k	-270k	50k	291k	205k
Employment to pop. ratio	60.1%	60.4%	60.3%	60.4%	60.4%	60.4%

Source: Bureau of Labor Statistics

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**Exhibit 1: Prime age labor force participation rate (% , dotted line = December 2019-February 2020 average)**

The prime age participation rate has declined recently

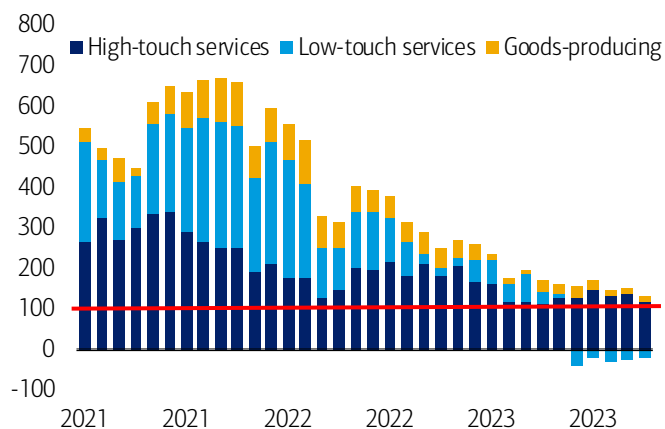


Source: Bureau of Labor Statistics

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**Exhibit 2: Private sector job growth (thousand, seasonally adjusted-sa)**

Job growth has become increasingly narrowly driven

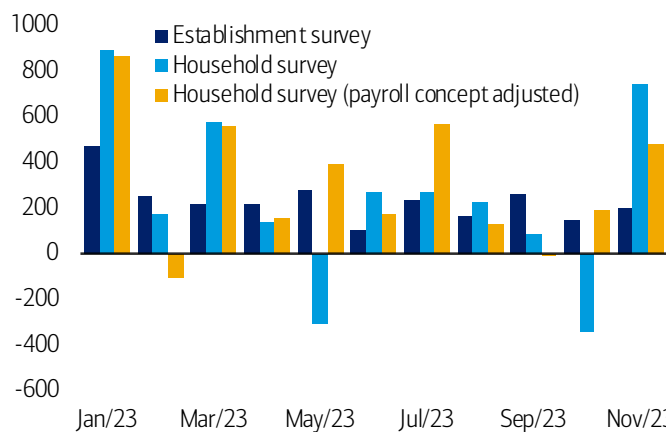


Source: Bureau of Labor Statistics, BofA Global Research

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**Exhibit 3: Establishment and household payroll growth (thousand, sa)**

Different measures of employment growth



Source: Bureau of Labor Statistics, BofA Global Research

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**Table 2: Monthly payroll growth heatmap (m/m change, 000s sa)**

Job growth has been driven by a narrow group of industries

Dec-23 nfp share	Component	Dec-23	Nov-23	Oct-23	Sep-23	Aug-23	Jul-23	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23
100%	<b>Total nonfarm</b>	<b>216</b>	<b>173</b>	<b>105</b>	<b>262</b>	<b>165</b>	<b>236</b>	<b>105</b>	<b>281</b>	<b>217</b>	<b>217</b>	<b>248</b>	<b>472</b>
85%	<b>Total private</b>	<b>164</b>	<b>136</b>	<b>44</b>	<b>199</b>	<b>114</b>	<b>145</b>	<b>86</b>	<b>255</b>	<b>179</b>	<b>157</b>	<b>193</b>	<b>353</b>
14%	Goods-producing	22	30	-12	21	28	12	32	24	25	-19	18	41
0%	Mining and logging	-1	-2	-1	1	0	2	-1	3	5	2	1	4
5%	Construction	17	6	27	9	30	12	29	25	11	-9	14	26
8%	Manufacturing	6	26	-38	11	-2	-2	4	-4	9	-12	3	11
5%	Durable goods	8	34	-37	10	0	12	17	3	13	-5	1	0
3%	Nondurable goods	-2	-8	-1	1	-2	-14	-13	-7	-4	-7	2	11
72%	Service-providing	142	106	56	178	86	133	54	231	154	176	175	312
18%	Trade, transportation, and utilities	0	-25	-2	31	-28	20	-48	48	-17	3	36	61
4%	Wholesale trade	6	5	8	16	3	15	-7	8	-2	4	7	9
10%	Retail trade	17	-24	17	2	-6	13	-23	21	-2	-19	48	22
4%	Transportation and warehousing	-23	-5	-28	12	-27	-7	-19	19	-15	16	-18	32
0%	Utilities	0	0	2	2	2	-2	1	1	2	2	-1	-2
2%	Information	14	15	-12	-6	-22	-19	-10	-4	3	3	-8	-23
6%	Financial activities	2	1	-8	0	1	15	2	13	27	-5	0	-1
15%	Professional and business services	13	-19	-26	-17	8	-29	-1	45	48	45	21	44
16%	Education and health services	74	109	84	86	105	104	79	88	77	70	64	111
11%	Leisure and hospitality	40	12	25	76	8	38	26	28	11	46	57	99
4%	Other services	-1	13	-5	8	14	4	6	13	5	14	5	21

Source: Bureau of Labor Statistics. nfp = non-farm payrolls.

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**Table 3: Monthly average hourly earnings heatmap (% m/m)**

Wage inflation was strong in December (+0.4% m/m)

Dec-23 nfp share	Component	Dec-23	Nov-23	Oct-23	Sep-23	Aug-23	Jul-23	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23
85%	<b>Total private</b>	<b>0.44%</b>	<b>0.35%</b>	<b>0.27%</b>	<b>0.27%</b>	<b>0.27%</b>	<b>0.39%</b>	<b>0.45%</b>	<b>0.33%</b>	<b>0.42%</b>	<b>0.27%</b>	<b>0.27%</b>	<b>0.30%</b>
14%	Goods-producing	0.35%	0.58%	0.35%	0.44%	0.12%	0.71%	0.56%	0.45%	0.48%	0.54%	0.21%	0.51%
0%	Mining and logging	0.54%	0.00%	-0.21%	1.23%	0.10%	0.50%	-0.16%	0.79%	1.23%	0.46%	0.38%	0.90%
5%	Construction	0.11%	0.54%	0.43%	0.24%	0.25%	0.85%	0.25%	0.42%	0.33%	0.42%	0.42%	0.25%
8%	Manufacturing	0.48%	0.61%	0.27%	0.52%	0.00%	0.62%	0.81%	0.41%	0.50%	0.63%	0.03%	0.64%
5%	Durable goods	0.66%	0.61%	0.52%	0.56%	0.03%	0.65%	0.56%	0.54%	0.42%	0.66%	0.06%	0.67%
3%	Nondurable goods	0.03%	0.60%	-0.10%	0.43%	0.00%	0.44%	1.22%	0.14%	0.62%	0.58%	-0.03%	0.59%
72%	Service-providing	0.47%	0.32%	0.24%	0.21%	0.30%	0.33%	0.39%	0.33%	0.39%	0.24%	0.27%	0.24%
18%	Trade, transportation, and utilities	0.58%	0.31%	-0.07%	0.38%	0.31%	0.17%	0.49%	0.10%	0.59%	0.17%	0.81%	0.53%
4%	Wholesale trade	0.11%	0.38%	-0.57%	0.22%	0.43%	0.08%	0.85%	-0.08%	0.55%	0.11%	0.36%	1.03%
10%	Retail trade	0.83%	0.33%	0.00%	0.25%	0.25%	0.17%	0.25%	0.00%	0.29%	-0.04%	1.06%	0.30%
4%	Transportation and warehousing	0.57%	0.24%	0.48%	0.61%	0.31%	0.24%	0.59%	0.31%	0.87%	0.42%	0.78%	0.35%
0%	Utilities	-1.17%	0.48%	0.24%	0.26%	-0.62%	0.56%	0.46%	0.49%	0.30%	0.76%	0.20%	0.78%
2%	Information	0.84%	0.84%	0.68%	0.06%	0.37%	0.10%	-0.21%	1.05%	-0.89%	0.31%	0.34%	0.02%
6%	Financial activities	0.36%	0.41%	0.07%	0.48%	0.80%	0.65%	0.77%	0.75%	-0.07%	0.38%	0.09%	0.21%
15%	Professional and business services	0.51%	0.46%	0.44%	0.22%	0.07%	0.57%	0.32%	0.22%	0.48%	0.45%	0.23%	0.38%
16%	Education and health services	0.30%	0.06%	0.24%	0.21%	0.27%	0.30%	0.34%	0.18%	0.31%	0.06%	-0.21%	0.37%
11%	Leisure and hospitality	0.37%	0.51%	0.56%	0.05%	0.24%	0.09%	0.33%	0.48%	0.53%	0.67%	0.05%	0.00%
4%	Other services	0.59%	0.13%	0.50%	0.20%	0.84%	0.20%	0.30%	0.41%	0.85%	-0.81%	0.17%	0.44%

Source: Bureau of Labor Statistics. nfp = non-farm payrolls.

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**Table 4: Annual average hourly earnings heatmap (% y/y)**

Annual wage growth rose by 4.1% y/y in December

Dec-23 nfp share	Component	Dec-23	Nov-23	Oct-23	Sep-23	Aug-23	Jul-23	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23
85%	Total private	4.10%	4.02%	4.10%	4.24%	4.29%	4.33%	4.41%	4.34%	4.38%	4.30%	4.68%	4.39%
14%	Goods-producing	5.41%	5.39%	5.23%	5.35%	5.28%	5.35%	5.06%	4.70%	4.59%	4.65%	4.58%	4.33%
0%	Mining and logging	5.92%	5.90%	6.51%	6.53%	5.49%	5.01%	5.71%	6.91%	7.12%	4.78%	4.39%	4.67%
5%	Construction	4.61%	5.00%	4.96%	5.11%	5.27%	5.41%	4.85%	5.01%	5.18%	5.42%	5.50%	5.31%
8%	Manufacturing	5.66%	5.38%	5.11%	5.26%	5.05%	5.19%	5.02%	4.24%	3.92%	4.05%	3.94%	3.56%
5%	Durable goods	6.10%	5.34%	4.92%	4.85%	4.66%	4.88%	4.50%	3.88%	3.55%	3.82%	3.85%	3.11%
3%	Nondurable goods	4.60%	5.22%	5.22%	5.73%	5.49%	5.38%	5.74%	4.73%	4.55%	4.35%	3.89%	4.34%
72%	Service-providing	3.80%	3.69%	3.80%	3.97%	4.04%	4.09%	4.26%	4.28%	4.33%	4.25%	4.69%	4.44%
18%	Trade, transportation, and utilities	4.46%	4.08%	4.24%	4.80%	4.78%	4.76%	4.92%	4.57%	4.99%	4.45%	4.95%	4.49%
4%	Wholesale trade	3.51%	3.95%	3.91%	5.36%	5.22%	4.98%	5.34%	5.27%	5.11%	4.75%	4.93%	5.07%
10%	Retail trade	3.75%	2.86%	3.62%	4.07%	4.08%	4.00%	4.32%	4.43%	4.66%	3.98%	4.85%	4.26%
4%	Transportation and warehousing	5.93%	5.55%	5.19%	4.77%	4.87%	5.11%	5.13%	3.50%	4.72%	4.23%	4.09%	3.78%
0%	Utilities	2.77%	4.63%	4.03%	4.25%	5.17%	5.60%	4.96%	4.99%	5.75%	5.14%	5.77%	5.19%
2%	Information	3.56%	3.31%	2.01%	1.17%	1.92%	3.42%	3.58%	4.56%	4.25%	5.67%	5.18%	5.78%
6%	Financial activities	5.00%	5.34%	5.09%	4.94%	5.19%	4.66%	4.43%	4.42%	3.77%	4.02%	4.42%	3.99%
15%	Professional and business services	4.45%	4.26%	4.34%	4.38%	4.37%	4.53%	4.51%	4.30%	4.23%	4.44%	4.80%	4.64%
16%	Education and health services	2.46%	2.49%	2.97%	3.33%	3.05%	2.90%	3.33%	3.60%	3.90%	3.88%	4.28%	4.14%
11%	Leisure and hospitality	3.95%	4.42%	4.75%	4.77%	4.88%	5.20%	5.63%	5.81%	5.89%	5.92%	6.67%	7.00%
4%	Other services	3.88%	3.13%	3.84%	3.50%	4.05%	3.36%	3.84%	4.54%	4.30%	3.35%	4.27%	3.73%

Source: Bureau of Labor Statistics. nfp = non-farm payrolls.

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**Table 5: Labor market dashboard**

Employment data show a broad-based recovery across demographics

Indicator	Prepandemic avg	Dec-23	Nov-23	Oct-23	Sep-23	Aug-23	Jul-23	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23
<b>Unemployment Rate</b>													
Total	3.6	3.7	3.7	3.8	3.8	3.8	3.5	3.6	3.7	3.4	3.5	3.6	3.4
Prime age (25-54)	3.0	3.3	3.1	3.2	3.2	3.1	3.0	3.1	3.2	3.1	3.0	3.1	3.0
Men	3.5	3.9	4.0	4.1	4.1	4.0	3.7	3.7	3.7	3.5	3.6	3.6	3.6
Women	3.6	3.6	3.4	3.6	3.4	3.5	3.4	3.4	3.6	3.4	3.4	3.5	3.3
White	3.1	3.5	3.3	3.5	3.4	3.4	3.1	3.1	3.3	3.1	3.2	3.2	3.1
Black	6.2	5.2	5.8	5.8	5.7	5.3	5.7	6.0	5.7	4.8	5.1	5.7	5.4
Hispanic	4.3	5.0	4.6	4.8	4.6	4.9	4.4	4.2	4.1	4.4	4.6	5.4	4.7
Asian	2.7	3.1	3.5	3.1	2.9	3.2	2.3	3.1	3.0	2.8	2.8	3.4	2.9
<b>Employment Population Ratio</b>													
Total	61.1	60.1	60.4	60.3	60.4	60.4	60.4	60.3	60.3	60.4	60.4	60.2	60.2
Prime age (25-54)	80.5	80.4	80.7	80.6	80.8	80.8	80.9	80.9	80.7	80.7	80.7	80.5	80.3
Men	66.7	65.5	65.7	65.2	65.5	65.5	65.5	65.6	65.5	65.7	65.8	65.5	65.5
Women	55.8	55.0	55.4	55.5	55.5	55.6	55.5	55.3	55.3	55.4	55.2	55.2	55.2
White	61.3	59.9	60.3	60.1	60.3	60.4	60.3	60.4	60.2	60.3	60.2	60.1	60.2
Black	59.1	60.1	60.0	59.3	59.4	59.4	59.2	58.9	59.6	59.9	60.7	59.7	59.5
Hispanic	64.7	63.4	63.9	63.8	64.1	63.9	64.3	64.4	64.1	63.8	63.7	63.3	63.3
Asian	62.2	61.9	62.7	63.3	63.8	63.5	64.0	63.4	63.1	63.0	63.0	62.9	62.3
<b>Labor force participation rate</b>													
Total	63.3	62.5	62.8	62.7	62.8	62.8	62.6	62.6	62.6	62.6	62.6	62.5	62.4
Prime age (25-54)	83.0	83.2	83.3	83.3	83.5	83.5	83.4	83.5	83.4	83.3	83.2	83.1	82.7
Men	69.1	68.1	68.4	68.0	68.3	68.2	68.0	68.1	68.1	68.0	68.3	68.0	67.9
Women	57.9	57.1	57.4	57.6	57.5	57.6	57.4	57.3	57.3	57.3	57.2	57.2	57.1
White	63.2	62.1	62.3	62.3	62.4	62.5	62.3	62.3	62.3	62.3	62.2	62.1	62.1
Black	63.0	63.4	63.7	63.0	63.0	62.7	62.8	62.7	63.1	62.9	64.0	63.3	62.9
Hispanic	67.6	66.7	66.9	67.0	67.2	67.1	67.3	67.3	66.8	66.8	66.8	66.9	66.4
Asian	63.9	63.9	65.0	65.3	65.7	65.6	65.5	65.4	65.0	64.8	64.8	65.1	64.2
<b>Wage measures</b>													
Employment Cost Index (quarterly, % yoy)	2.7	n.a.	n.a.	n.a.	4.3	n.a.	n.a.	4.5	n.a.	n.a.	4.8	n.a.	n.a.
Atlanta Wage Growth Tracker (% yoy, 12mma)	3.7	n.a.	5.6	5.8	5.8	6.0	6.0	6.1	6.3	6.3	6.4	6.3	6.3
NFIB: % Raising Compensation	33.7	36.0	36.0	36.0	36.0	36.0	38.0	36.0	41.0	40.0	42.0	46.0	46.0
NFIB: % Planning to Raise Compensation	22.3	29.0	30.0	24.0	23.0	26.0	21.0	22.0	22.0	21.0	22.0	23.0	22.0
Conference Board: 6-Month Ahead Income Change	22.3	18.7	17.7	15.6	17.9	18.7	17.8	18.6	18.9	17.3	16.2	14.4	17.4
U of M: 1-Yr Ahead Income Change Expectations (Median)	2.2	2.1	2.2	1.6	1.7	2.4	1.9	1.8	2.3	1.8	1.5	2.4	2.5
NY Fed: 1-Yr Ahead Earnings Growth Expectation	2.5	n.a.	2.7	2.8	3.0	2.9	2.8	3.0	2.8	3.0	3.0	3.0	3.0

Source: Bureau of Labor Statistics

Note: Prepandemic average is the average of each indicator from December 2019-February 2020

BofA GLOBAL RESEARCH

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