Morning Market Tidbits

March cut still in play

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Economics
United States

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In focus

In our recent report, US Watch: December employment: Simmering not boiling, we reviewed the December employment print. 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. Services employment and private employment were again narrowly driven by high-touch services—leisure and hospitality, education and health, and other services. Importantly for the consumer outlook, growth in wage income was solid in December as the aggregate payrolls index increased by 0.3% m/m.

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. 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%. The decrease in the labor force also combined with the small increase in unemployment left the unemployment rate unchanged at 3.7%.

On net, this supports our view that the labor market is coming into better balance, and income growth continues to support spending. We retain our view that the Fed will begin a gradual easing cycle starting with a 25bp cut in March.

Additionally, in our report, CPI Inflation Watch: December US CPI Inflation preview: A soft 0.3% m/m print, we published our forecast for the upcoming CPI print. For the December CPI report, we forecast that headline and core CPI rose by 0.3% m/m. On a y/y basis, headline should print at 3.3% and core at 3.9%. The headline NSA index should print at 306.634.

Within core, we expect core goods and core services to continue to paint two different pictures. On the one hand, we look for core goods prices to decline for a seventh consecutive month (-0.2% m/m), owing in part to a decline in used cars and trucks. On the other hand, we expect core services prices to increase at 0.4% m/m or 5.0% annualized over the last three months, owing in large part to sticky rents. Excluding rent and owners' equivalent rent (OER), we expect that core services prices rose by a still elevated 0.3% m/m compared to 0.4% m/m in November. In short, services inflation likely remained sticky-high in December.

A CPI report in line with our forecast would continue to signal ongoing progress towards the Fed's 2% target. Therefore, in our view, it would keep the Fed on track for a 25bp cut in March. A soft 0.3 m/m is unlikely to move current Fed pricing much, if at all.

Importantly, the translation of the CPI data to the Fed's preferred measure of inflation, PCE, will be what matters most to the markets and Fed policy. In the last six months there has been a larger divergence in monthly measures of inflation, owing largely to different weights. Therefore, any knee-jerk market reaction to the CPI report could be reversed depending on what the detailed numbers mean for PCE inflation.

CPI: Consumer Price Index

FOMC: Federal Open Market Committee

k: thousand

SEP: Summary of Economic Projections

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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
Establishment survey						
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%
Household survey						
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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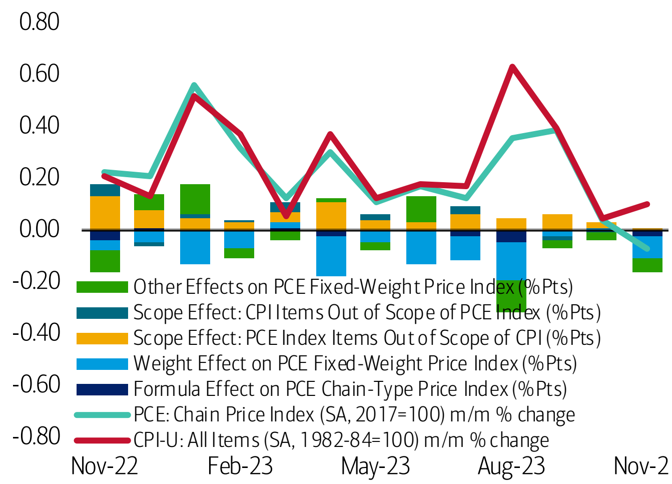
Exhibit 1: Factors that explain the Wedge between % m/m changes in Headline CPI and PCE inflation (ppt)
In the last six months, there has been a larger divergence in monthly measures of inflation, owing largely to different weights and other effects, which include seasonal adjustment differences



Source: Bureau of Economic Analysis, Haver Analytics

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Market action

The Asian equity markets that we cover closed negative overnight. Looking at individual markets, we note that the Hang Seng, the Shanghai Composite, the Indian Sensex, and the Korean Kospi fell 1.9%, 1.4%, 0.9%, and 0.4%, respectively, while the Nikkei was closed.

As of 7:00 am ET, aggregate European stocks are down 0.2%, and S& P500 futures are down 0.1%. In the bond markets, 10-year Treasury yields came in flat at 4.04%, and German Bund yields increased 3bp to 2.19%. The dollar index is up $0.10 to $102.51. West Texas Intermediate (WTI) crude oil prices are $2.03 lower at $71.78/barrel, and gold prices are at $2020.11/ounce.

Data review

Factory Orders

Factory orders increased by 2.6% m/m in November after a revised up -3.4% print in October. This was slightly more than consensus expectations of a 2.4% print. This is owed mainly to a ~15% m/m rise in transportation equipment manufacturing, especially the 80% rise in non-defense aircrafts and parts. Hence, excluding transportation, factory orders rose by a more modest 0.1% m/m. Durable goods orders excluding transportation also posted a more modest flat print of 0.4%, a tenth lower from the preliminary. Meanwhile, capital goods excluding defense and aircraft (core capital goods) orders that feed into our GDP tracking remained unchanged at 0.8% m/m in the final print. Factory shipments came in at 0.5% m/m. This was on the back of a 1.0% rise in durable goods shipments and a flat print for non-durable goods.

ISM Services

ISM services dropped to 50.6 in December, below consensus expectations at 52.5. Looking at the details, we note that new orders were down to 52.8 from 55.5, while prices paid also fell to 57.4 from 58.3. Meanwhile, employment was noticeably down to 43.3 from 50.7, but given the solid payrolls data today, we would not be too concerned with the numbers, especially given that it is a diffusion index and the strength in payrolls is narrowly driven.

Payrolls

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. Services employment and private employment was again narrowly driven by high-touch services—leisure and hospitality, education and health, and other services. Importantly for the consumer outlook, growth in wage income was solid in December as the aggregate payrolls index increased by 0.3% m/m. 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. 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%. The decrease in the labor force also combined with the small increase in unemployment left the unemployment rate unchanged at 3.7%. We think that the overall tone of the report is consistent with a Fed cut in March.

US GDP Tracking

Exhibit 2: BofA US GDP tracking estimate (% q/q saar)

Our 4Q GDP tracking estimate Is up to 1.2% q/q saar after a stronger-than-expected December vehide sales and payrolls print

Date	Data release	GDP	Final Sales	PCE	Res. Inv.	Struct	Equip	IPP	Gov.	Exports	Imports	Net exports (level)	CIPI (level)
12/12/23	CPI	1.0	1.8	**1.8**	-1.9	2.0	1.0	2.5	2.2	8.7	6.2	-933.6	20.4
12/14/23	PPI, Retail Sales, Business Inventories	**1.1**	**1.9**	**2.0**	**-1.8**	**2.1**	1.0	2.5	2.2	8.7	6.2	-933.6	**13.4**
12/15/23	Industrial Production	**1.1**	**1.8**	**1.9**	-1.8	**1.8**	**1.2**	2.5	2.2	8.7	6.2	-933.6	13.4
12/20/23	Housing Starts and Permits, Existing Home Sales	**1.2**	1.8	1.9	**0.0**	1.8	1.2	2.5	2.2	8.7	6.2	-933.6	13.4
12/21/23	GDP (T) 3Q	**1.1**	**1.7**	1.9	0.0	1.8	1.2	2.5	2.2	8.7	6.2	-933.6	**18.0**
12/22/23	PCE, Durable Goods Orders, New Home Sales	**1.1**	**1.7**	**1.7**	**-0.5**	1.8	**1.9**	2.5	2.2	8.7	6.2	-933.6	**31.3**
12/28/23	Advance Goods Trade Balance, Retail & Wholesale Inventories	**0.9**	**1.5**	1.7	-0.5	1.8	1.9	2.5	2.2	**1.7**	**3.2**	**-947.1**	**23.7**
12/2/24	Construction Spending	0.9	1.5	1.7	**-1.2**	**3.3**	1.9	2.5	**2.6**	1.7	3.2	-947.1	23.7
12/4/24	Vehicle Sales	**1.1**	**2.1**	**2.0**	-1.2	3.3	**2.6**	2.5	2.6	1.7	3.2	-947.1	23.7
12/5/24	Payrolls, Factory Orders	**1.2**	2.1	2.0	**-0.2**	3.3	**2.8**	2.5	**2.3**	1.7	3.2	-947.1	**26.0**
	GDP tracking	1.2	2.1	2.0	-0.2	3.3	2.8	2.5	2.3	1.7	3.2	-947.1	26.0
	Contribution to GDP growth (pp)			1.3	0.0	0.1	0.1	0.1	0.4			-0.2	-0.7
	BofA official GDP forecast	1.5	2.0	2.5	1.0	1.0	2.0	2.5	2.0	3.0	2.0	-929.0	38.0

Source: BofA Global Research. Our GDP tracking estimate reflects the mechanical aggregation of incoming data that directly informs the BEA's GDP calculations. The process is distinct from our official published GDP forecast. Boldface cells indicate where data have implications for tracking estimates. Saar = seasonally adjusted annual rate.

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Overseas Data

Germany

Factory orders showed a very weak 0.3% bounce back in November, after the chunky 3.7% mom contraction in October. Excluding bulk orders, the index is down 0.6% mom. Our Europe economists have cut Germany's growth forecasts from 0.3% for next year to -0.1%, reflecting tighter fiscal policy–going forward, more weakness in Germany data is likely.

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