ECONOMIC PREVIEW

Week of May 1, 2023

Indicator/Action Economics Survey:	Last Actual:	Regions' View:
Fed Funds Rate: Target Range Midpoint *(After the May 2-3 FOMC meeting):* Target Range Mid-point: 4.875 to 5.125 percent Median Target Range Mid-point: 5.125 percent	Range: 4.75% to 5.00% Midpoint: 4.875%	This week shapes up as one of the most action-packed weeks we can remember. Okay, sure, "action-packed" is a relative term, and our definition may differ oh so slightly from, say, John Wick's definition, but just humor us. In addition to a crowded data docket capped off by the April employment report (see Page 2), the FOMC meets this week. The recent data have shown flagging growth coupled with persistent core inflation, and we think the latter will win out in terms of the FOMC's decision on the Fed funds rate, with the Committee going ahead with another twenty-five basis point hike at this week's meeting. While the Committee could signal that a pause in rate hikes may be in order after this week's meeting, they will also retain a bias toward further hikes until there are signs of a more pronounced deceleration in core inflation, particularly core services inflation, than has been see thus far. Chair Powell will likely stress this point in his post-meeting press conference and also push back firmly against the notion that the FOMC will be cutting the funds rate this year. Though unlikely to keep them from going ahead with another funds rate hike at this week's meeting, recent stress in the banking system will certainly be fresh on the minds of Committee members. As if on cue, Monday brings the release of the latest quarterly *Senior Loan Officer Opinion Survey on Bank Lending Practices* (SLOOS), which will cover how lending standards and loan demand changed over the course of Q1. While we've always monitored the SLOOS data for insights into changes in credit flows that could in turn impact the paths of consumer and business spending, the Fed's survey has for the most part tended to fly under the radar, becoming more visible only during times of financial/economic stress. Needless to say, this is one of those times. To that point, while there has been considerable discussion of lending standards since the March bank failures, many seem not to have noticed that the SLOOS indicated lending standards were being raised, across commercial and consumer spaces and loan demand was fading over the final three quarters of 2022. Moreover, the final 2022 survey, conducted in December, indicated lending officers anticipated further tightening in lending standards and further declines in loan demand over the course of 2023. So, while the Q1 survey will surely show further tightening in lending standards, the meaningful question will be how much of that would have taken place anyway and how much will be in response to stresses in the banking system, a question which, unfortunately, the survey is unlikely to answer. Also of interest to FOMC members this week will be Tuesday's release of the March JOLTS data. Though the March data should show a further decline in job vacancies, the more relevant metric will be the quits rate, which remains easily above pre-pandemic norms. This will matter to the FOMC as job changers typically score larger pay increases, so the FOMC will see the quits rate as an indicator of wage pressures.
April ISM Manufacturing Index Monday, 5/1 Range: 45.6 to 48.7 percent Median: 46.8 percent	Mar = 46.3%	Down to 45.9 percent. As will be the case with much of the data for the month of April, the bar for the ISM Manufacturing Index is set quite high by tough seasonal adjustment. To that point, the April seasonal factors for the sub-indexes for new orders and production are toughest of any month during the year, reflecting the typical spring bounce in activity. That the ISM's gauge has shown the factory sector to be in contraction in each of the past five months suggests any spring bounce this year won't be all that springy, and if we're correct on this point any such shortfall will be treated harshly by seasonal adjustment. At the same time, steadily quickening supplier delivery times, in part reflecting increasing slack across the factory sector, have been a drag on the headline index, and we suspect that will again be the case with the April data. There are some upside risks to our forecast, such as the regional Fed surveys suggesting modest improvement in manufacturing sector activity in April. Also, the number of industry groups reporting growth has risen in each of the past two months, though from a notably low base as only two of the eighteen industry groups reported growth in January. Indeed, with seasonal adjustment likely to cloud the signal in the April data, the number of industry groups reporting growth, particularly growth in new orders, will be more meaningful to us than the headline index. Finally, after having sent strong disinflationary signals over the prior several months, the prices paid index (a gauge of input costs) reversed course in February and didn't move much in March. Should the April survey show continued stability, that will put a dent in our premise that core goods price disinflation, if not outright deflation, would act as a moderating force on overall inflation this year.

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March Construction Spending Monday, 5/1 Range: -0.3 to 0.4 percent Median: 0.1 percent	Feb = -0.1%	Up by 0.4 percent.
March Factory Orders Tuesday, 5/2 Range: -0.4 to 2.0 percent Median: 1.3 percent	Feb = -0.7%	Up by 0.7 percent. While durable goods orders rose by over three percent in March, that was largely a function of a spike in aircraft orders, both civilian and defense, while core capital goods orders, to us the single most important line item in the entire report, fell by 0.4 percent. We look for orders for nondurable goods orders to have declined sharply, further watering down the increase in durable goods orders.
April ISM Non-Manufacturing Index Wednesday, 5/3 Range: 49.8 to 53.5 percent Median: 51.8 percent	Feb = 51.2%	Down to 49.8 percent. As with their survey of the manufacturing sector, the ISM's April survey of the broader services sector faces some tough seasonal adjustment hurdles. For the indexes of business activity, new orders, and employment, the April seasonal factors are exceptionally tough, and rather than the usual spring bounce in activity many industry groups, such as construction, finance, real estate, and transportation/warehousing, could have faced a challenging month, with any such weakness punished by seasonal adjustment. If we're correct on this point, that will make interpreting the survey results a bit tricky, or at least much more difficult than will be implied by the wave of "look what the credit crunch is doing to the economy" headlines that would surely follow. It could be that, seasonal adjustment issues aside, our forecast is too dour, particularly given that in the March survey thirteen of the eighteen industry groups reported growth. Still, at the very least, we expect the April survey to show further slowing in the pace of expansion in the services sector.
March Trade Balance Thursday, 5/4 Range: -$72.0 to -$61.2 billion Median: -$63.5 billion	Feb = -$70.5 billion	Narrowing to -$62.6 billion.
Q1 Nonfarm Labor Productivity Thursday, 5/4 Range: -2.8 to 0.8 percent Median: -1.8 percent SAAR	Q4 = +1.7% SAAR	Down at an annualized rate of 2.5 percent. From the Q1 GDP data, we know that real output in the nonfarm business sector rose at an annualized rate of just 0.16 percent in Q1. At the same time, however, aggregate nonfarm hours worked grew at an annualized rate of 2.5 percent, with modest growth in aggregate hours worked amongst the self-employed. The net result should be a sizable decline in labor productivity and a corresponding spike in unit labor costs (see below) that would add to inflationary worries and weigh on corporate profit margins. But, even if our below-consensus is on or near the mark, the lines from productivity to inflation and profit margins won't be all that straight, as what was a modest draw in inventories weighed on measured Q1 output growth. Though we've been wary of reading too much into the quarterly productivity data since the onset of the pandemic, our sense is that the underlying trend rate of productivity growth remains much too low.
Q1 Unit Labor Costs Thursday, 5/4 Range: 3.0 to 6.9 percent Median: 5.4 percent SAAR	Q4 = +3.2% SAAR	Up at an annualized rate of 6.4 percent, which is the flip side of the decline in labor productivity our forecast anticipates. It may be more useful to focus on growth in hourly labor compensation, which figures into the calculation of unit labor costs and which we expect to show that growth in labor costs decelerated further in Q1.
April Nonfarm Employment Friday, 5/5 Range: 125,000 to 265,000 jobs Median: 180,000 jobs	Mar = +236,000 jobs	Up by 146,000 jobs, with private sector payrolls up by 123,000 jobs and public sector payrolls up by 23,000 jobs. This is another report we expect will be impacted by tough seasonal adjustment. To that point, in any given year April is typically the month with the largest increase in not seasonally adjusted employment as economic activity perks up after the winter lull. What was atypically mild weather this winter, however, meant payrolls in areas such as construction and leisure and hospitality services held up better than normal, meaning less of a bounce in the spring. Indeed, some of these effects were visible in the March data, and we expect the April data to show even more pronounced seasonal adjustment effects. At the same time, a loss of momentum in growth will likely weigh on payrolls in information services, finance, and business services, which is of far more relevance than any seasonal adjustment issues that may arise. Though the pace of job growth is slowing, it has remained notably broad based, making the one-month hiring diffusion index a key metric to watch in the April data. While the labor market is clearly cooling, job growth remains more than sufficient to keep a lid on the unemployment rate, at least for now.

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April Manufacturing Employment Friday, 5/5 Range: -10,000 to 10,000 jobs Median: 0 jobs	Mar = -1,000 jobs	<u>Down</u> by 8,000 jobs.
April Average Weekly Hours Friday, 5/5 Range: 34.4 to 34.5 hours Median: 34.4 hours	Mar = 34.4 hours	<u>Unchanged</u> at 34.4 hours. There is some downside risk to our forecast, particularly if payrolls amongst the goods producing industries (construction, manufacturing, mining/natural resources) decline as we expect will be the case, as these are all industry groups with well above-average workweeks. An often underappreciated point is the extent to which firms can, and do, use hours worked as a lever with which to manage total labor input. We think that to be particularly relevant during this cycle, in that firms will likely be much less likely to let workers go if faced with what they perceive will be a brief and mild downturn given how hard it has been for them to find and retain labor over recent years. A look at past cycles shows there is still considerable room for firms to cut hours worked on top of the two-tenths of an hour reduction seen over the past few months. If that doesn't seem like a big deal, recall that each one-tenth of an hour change in the average length of the workweek is equivalent to over 300,000 jobs in terms of total labor input. It is also worth noting that in addition to total labor input, hours worked is a lever with which firms can manage growth in total labor costs, a point often lost in the almost singular focus on average hourly earnings. In our note on Q1 labor productivity, we pointed out that aggregate private sector hours worked rose at an annual rate of 2.5 percent in Q1. If that seems inconsistent with us noting here that the average length of the workweek has been declining, all of the growth in aggregate hours in Q1 came from an outsized increase in January, with aggregate private sector hours worked having declined in both February and March. Perhaps more than any other single metric, this illustrates our point about the economy having lost momentum over the course of Q1.
April Average Hourly Earnings Friday, 5/5 Range: 0.2 to 0.4 percent Median: 0.3 percent	Mar = +0.3%	<u>Up</u> by 0.2 percent, for a year-on-year increase of 4.1 percent. Our calls on job growth, hours worked, and hourly earnings would yield a 0.3 percent increase in aggregate private sector wage and salary earnings, leaving them up 6.4 percent year-on-year.
April Unemployment Rate Friday, 5/5 Range: 3.4 to 3.6 percent Median: 3.6 percent	Mar = 3.5%	<u>Unchanged</u> at 3.5 percent. April can be a weird month in terms of the household survey data, with it not uncommon to see reported declines in both the labor force and household employment in the seasonally adjusted data. Perhaps a more interesting metric to watch for comes from the data on labor force flows, which track month-to-month changes in labor force status. Over the past several months, the number of people who have transitioned from not in the labor force to employed has been notably elevated, which is consistent with the increases in participation and is a sign of how tight labor market conditions have been. Though this series can be volatile, we use the three-month moving average as an indicator of labor market slack and will be interested to see what the April data show.

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