ECONOMIC PREVIEW

Week of July 4, 2022

Indicator/Action Economics Survey:	Last Actual:	Regions' View:
Fed Funds Rate: Target Range Midpoint *(After the July 26-27 FOMC meeting):* Target Range Mid-point: 2.125 to 2.375 percent Median Target Range Mid-point: 2.375 percent	Range: 1.50% to 1.75% Midpoint: 1.625%	Last week's release of the third estimate of Q1 GDP showed real GDP contracted at an annualized rate of 1.6 percent. While that may not seem like much of a change from the second estimate showing a 1.5 percent contraction, the details beneath the headline number paint a different picture of the economy and cast a cloud over the Q2 data. Growth in real consumer spending was revised considerably lower, with a sharp downgrade in services spending. This in part reflects a large downward revision to spending on health care services, which accounts for over one-quarter of services spending. Much of this spending does not reflect out-of-pocket expenditures by consumers, but is nonetheless booked as consumer spending, so services spending entered Q2 on a lower trajectory than had previously been thought to be the case. One reason this matters is growth in services spending has been expected to take up the slack from fading consumer spending on goods, which was also revised lower in the third estimate of Q1 GDP. Q2 growth in real consumer spending is shaping up to be even slower than the 1.8 percent annualized growth seen in Q1. In part, this reflects less favorable path of income than implied in the earlier estimates of Q1 GDP; the third estimate showed real disposable (after-tax) personal income fell in Q1, thanks in part to tax payments being revised higher. To be sure, consumers continue to sit on notably high deposit balances, but between elevated inflation and softer income trends, these balances won't last as long as had been thought. The third estimate of Q1 GDP also showed a larger build in nonfarm business inventories than had previously been reported. While this meant inventories were less of a drag on Q1 GDP than had previously been reported, it sets them up to be a significant drag on Q2 GDP – in the calculation of the annualized quarterly change in GDP, it is the change in the change in inventories that matters. The inventory build in Q2 is tracking to come in below that seen in Q1, even more so after the upward revision to the Q1 data, to the point that inventories could deduct up to two percentage points off the quarterly change in real GDP in Q2. With slower growth in consumer spending, the drag from inventories could easily be enough to result in a second straight contraction in real GDP, but keep in mind that the trade deficit will be much narrower than was the case in Q1, when trade deducted 3.23 percentage points off the quarterly change in real GDP. But, even if real GDP contracted again in Q2, that would not mean the economy has slipped into recession. Two consecutive quarterly declines in real GDP is how a recession is often defined in media accounts, but that is not the threshold used by the National Bureau of Economic Research (NBER), the unofficial arbiter of turns in the business cycle, which defines a recession as "a significant decline in economic activity that is spread across the economy and lasts more than a few months." By that standard, the economy is just not there, which of course doesn't mean it can't or won't get there, particularly with the FOMC intent on "doing a job" on demand as a roundabout way of dampening inflation pressures. While the June employment report (see Page 2) is the highlight of this week's slate of data releases, Wednesday will bring the release of the Job Openings and Labor Turnover Survey (JOLTS) for May. Though lagging the nonfarm employment data by a month, the May JOLTS data will be worth watching for signs that labor demand is easing. While a decline in job openings in the May survey will no doubt trigger a wave of dour headlines, the reality is that labor supply is still no match for labor demand. After all, the April data showed 11.4 million open jobs, or, almost two open jobs for each unemployed person, and the number of open jobs has been running roughly 4.5 million above pre-pandemic levels, which at the time were showing labor demand running well ahead of labor supply. To be sure, that differential will narrow as the economy slows, but we're a long way from the labor market being balanced. Wednesday also brings the release of the minutes of the June FOMC meeting, which may shed some light on how the Committee is thinking about the tradeoff between a slowing economy and the quest to bring inflation down, and the nature of the debate around the pivot from a 50-basis point funds rate hike to a 75-basis point hike.
May Factory Orders Tuesday, 7/5 Range: 0.3 to 1.5 percent Median: 0.5 percent	Apr = +0.3%	Up by 1.2 percent.

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June ISM Non-Manufacturing Index Range: 52.5 to 56.5 percent Median: 54.0 percent	Wednesday, 7/6	May = 55.9%	Down to 53.4 percent. We expect the ISM's index to show continued expansion in the broad services sector, but at a slower pace than in recent months. Particular areas in which growth has likely slowed sharply include retail trade, transportation and warehousing, real estate, and information services. Recall that the ISM's survey of the manufacturing sector showed new orders declined in June, so this will be a key metric to watch in the services survey. Our forecast anticipates the new orders index in the services survey remained above 50.0 percent in June, but just barely, and we won't be surprised if it actually dipped below. Other components to watch are prices paid for non-labor inputs and supplier delivery times; if demand is indeed slowing to a meaningful degree, that will be reflected in these components in the months ahead.
May Trade Balance Range: -$86.0 to -$83.4 billion Median: -$84.9 billion	Thursday, 7/7	Apr = -$87.1 billion	Narrowing to -$84.4 billion. March saw the largest trade deficit on record, which went a long way toward trade being a huge drag on Q1 GDP, deducting 3.23 percentage points from the quarterly change in real GDP. If our forecast of the May data is on or close to the mark, that would set the stage for a much smaller trade deficit to make a meaningful contribution to Q2 GDP, offsetting much of the drag from a smaller inventory build. As we've noted on several occasions, the trade data have been notably volatile since the onset of the pandemic, and while sharp swings in measured imports and exports can have outsized impacts on the GDP data, they actually tell us little about the underlying health of the U.S. economy.
June Nonfarm Employment Range: 180,000 to 400,000 jobs Median: 273,000 jobs	Friday, 7/8	May = +390,000 jobs	Up by 202,000 jobs, with private sector payrolls up by 178,000 jobs and public sector payrolls up by 24,000 jobs. Right off the bat, seasonal adjustment poses a high hurdle for the June employment data, as June is typically a month in which not seasonally adjusted payrolls rise sharply. That is particularly true in sectors such as retail trade, construction, and leisure and hospitality services. As such, smaller than normal gains in not seasonally adjusted employment in these areas will be treated harshly in the seasonally adjusted data, which we anticipate will prove to be the case. There are ample signs that retail trade and construction have slowed, and firms in leisure and hospitality services have for some time been frustrated by an inability to fill open positions. At the same time, hiring in information services is set to slow, while the ISM Manufacturing Index points to a pronounced slowdown in hiring in the factory sector in the BLS data. We look for the pace of job growth to slow further in the months ahead as the broader economy does the same.
June Manufacturing Employment Range: 10,000 to 40,000 jobs Median: 25,000 jobs	Friday, 7/8	May = +18,000 jobs	Up by 13,000 jobs.
June Average Weekly Hours Range: 34.6 to 34.6 hours Median: 34.6 hours	Friday, 7/8	May = 34.6 hours	Unchanged at 34.6 hours. Cuts in hours worked would be a clear sign of pronounced weakening in the demand for labor, as firms will adjust hours as a first step in altering total labor input as final demand shifts. Though not incorporated into the measure of hours worked in the establishment survey, the May household survey showed an increase in the number of people working part-time due to slack business conditions which, if sustained, would point to a rising unemployment rate. At the same time, small changes in hours worked have a substantial impact on growth in aggregate labor earnings and, in turn, growth in personal income. So, though not typically a main focal point of the monthly employment reports, average weekly hours clearly merit closer attention in the months ahead.
June Average Hourly Earnings Range: 0.2 to 0.4 percent Median: 0.3 percent	Friday, 7/8	May = +0.3%	Up by 0.4 percent, which would translate into a year-on-year increase of 5.1 percent. Our calls on job growth, hours worked, and hourly earnings would yield a 0.5 percent increase in aggregate private sector wage and salary earnings, leaving them up 9.5 percent year-on-year.
June Unemployment Rate Range: 3.5 to 3.7 percent Median: 3.6 percent	Friday, 7/8	May = 3.6%	Down to 3.5 percent. While we expect a further increase in labor force participation, we think job growth will be sufficient to push the jobless rate down. That said, the participation rate remains well below pre-pandemic norms, which will act as a check on any increases in the unemployment rate should the demand for labor diminish as the broader economy slows.

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