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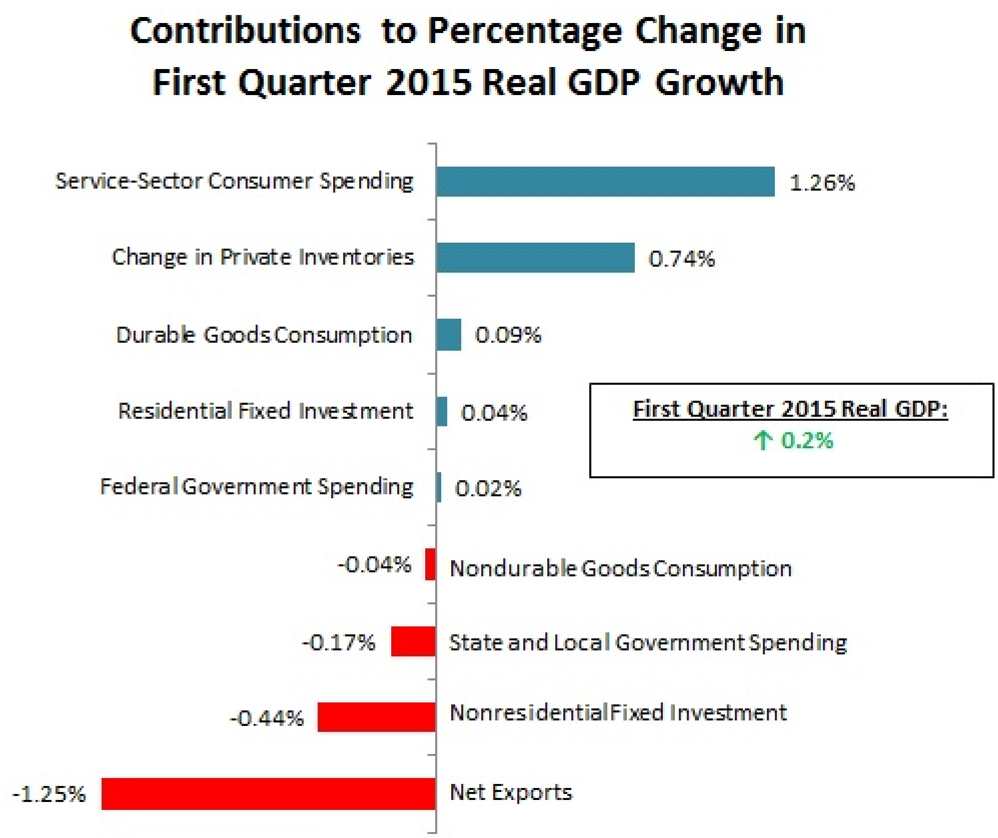

The U.S. economy stagnated in the first quarter, with real GDP growing by just 0.2 percent. This compares to a consensus estimate of 1.1 percent, and it was lower than the 5.0 percent and 2.2 percent growth rates observed in the third and fourth quarters of 2014, respectively. As one might expect from a data point that is just shy of zero, the underlying contributions to growth were mixed. Net exports and government spending were drags on activity in the first quarter, particularly with headwinds from a stronger dollar. Consumer spending on goods and nonresidential fixed investment were also weak, with the latter experiencing sharp declines stemming from the energy market and its supply chain. The bright spots—to the extent that you could call them that—were service-sector spending and a rebound in inventories.

The latest Institute for Supply Management also reflects much of this softness. The manufacturing Purchasing Managers' Index (PMI) was unchanged in April at 51.5, and it has generally trended lower since measuring 57.9 six months ago. Also, employment shifted negative for the first time in nearly two years. Still, there were signs of cautious optimism in the report, with new orders, exports and production growth moving somewhat higher.

Meanwhile, surveys from the Dallas and Richmond Federal Reserve Banks both indicated contracting activity levels in April. The Texas economy continues to grapple with the ramifications of lower crude oil prices. For instance, nearly 28 percent of the Dallas Federal Reserve's respondents said conditions had worsened in April. Nonetheless, both regional surveys provided a more upbeat assessment about the coming months. Along those lines, construction spending was up 2.8 percent in March, increasing to an all-time high for the second straight month, suggesting that manufacturing leaders have enough confidence in their outlook to warrant additional construction investment.

It has been more difficult to gauge consumer sentiment in light of recent slowness in the economy, with varied news out last week. As noted above, goods spending was essentially flat in the first quarter, suggesting a high degree of caution. Personal spending figures echoed this finding; however, they also observed an increase of 0.4 percent in March, suggesting a bit of a rebound from softness during the prior months. The savings rate declined to 5.3 percent, but it continues to be higher than a few months ago, with the rate being 4.4 percent as recently as November. Likewise, consumer confidence has eased in the early months of this year after peaking at the end of 2014. The April data, however, were mixed, with the University of Michigan's measure rebounding a little but the Conference Board's report showing confidence pulling back once again.

If there was any silver lining to this negative news, it is the belief in financial markets that slower growth will postpone the Federal Reserve's push for higher interest rates. For its part, the Federal Open Market Committee went out of its way in its latest statement to suggest that the recent slowdown was due to "transitory factors," thereby keeping a possible June rate increase on the table. At the same time, the Federal Reserve will likely be looking for stronger economic data before beginning to normalize policies, making a September (or later) rate increase more probable. This perception has already impacted exchange rates, with the euro rising from a low of $1.0524 on March 13 to Friday's close of $1.1218. However, even with some slight weakening in the dollar in recent days, it has appreciated 18.1 percent against the euro since the end of June 2014.

This week, the highlights will be on international trade and employment. On Tuesday, we will get the latest figures on the U.S. trade deficit, including manufactured goods exports, which have struggled of late on weaknesses abroad and a stronger U.S. dollar. At the end of the week, the Bureau of Labor Statistics will release April jobs numbers, which we hope will reflect a bit of a rebound after softer hiring in February and March. Other reports out this week include the most recent data points for consumer credit, factory orders and productivity.

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Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

This Week's Indicators:

Monday, April 27
Dallas Fed Manufacturing Survey

Tuesday, April 28
Conference Board Consumer Confidence
Richmond Fed Manufacturing Survey

Wednesday, April 29
Business Employment Dynamics
FOMC Monetary Policy Statement
Gross Domestic Product (First Quarter 2015)

Thursday, April 30
Employment Cost Index
Personal Income and Spending

Friday, May 1
Construction Spending
ISM Purchasing Managers' Index
University of Michigan Consumer Sentiment (Revision)

Monday, May 4
Factory Orders and Shipments

Tuesday, May 5
International Trade Report

Wednesday, May 6
ADP National Employment Report
Productivity and Costs

Thursday, May 7
Consumer Credit

Friday, May 8
BLS National Employment Report

Summaries for Last Week`s Economic Indicators

Business Employment Dynamics

The Bureau of Labor Statistics reported that net employment growth slowed in the third quarter of 2014, according to the latest Business Employment Dynamics (BED) data. Manufacturers had gross job gains of 404,000 in the third quarter, with 365,000 from expanding establishments and 39,000 from new establishments. At the same time, there were gross job losses of 389,000 workers in the quarter, with 349,000 from contracting establishments and 40,000 from closing establishments. Therefore, there was a net employment change of 15,000 for the manufacturing sector in the third quarter, down from 72,000 in the second quarter. Still, net hiring among manufacturers has now been positive for seven consecutive months, averaging roughly 28,500 per quarter over that time frame.

The BED database continues to reflect reduced startup rates for new manufacturing establishments over the longer term. There were 5,000 new manufacturing establishments in the third quarter of 2014, unchanged from the prior quarter. Nonetheless, this was down from the essentially 8,000 per month pace in 1994. In addition, the rate of employees per startup in manufacturing has also declined, down from an average of 97,250 employees from new establishments in 1994 to 22,000 in the third quarter of 2014.

To be fair, similar findings can be seen in other industries, with reduced entrepreneurship rates and smaller workforces per new startup. Policymakers and researchers have searched for reasons to explain this phenomenon. I testified on this issue last fall before the House Small Business Subcommittee on Contracting and Workforce.

Conference Board Consumer Confidence

The Conference Board reported that consumer sentiment pulled back again in April. The Consumer Confidence Index has been quite volatile over the past few months. After jumping from 93.1 in December to 103.8 in January (its highest level since August 2007), the index has measured 98.8 in February, 101.4 in March and 95.2 in April. Despite the back-and-forth swings each month, the index measuring current conditions has edged lower for three consecutive months, down from 113.9 in January to 106.8 in April. This figure continues to reflect progress in overall attitudes over the longer term; yet, it mirrors recent softness in a number of economic data points.

These responses often hinge on opinions about employment and income, and this is the case here, too. The percentage of respondents feeling that jobs were plentiful dropped from 21.0 percent to 19.1 percent, with those sensing that jobs were hard to get edging up from 25.5 percent to 26.4 percent. Likewise, the percentage of respondents expecting their incomes to decrease rose from 9.7 percent to 11.2 percent, the highest level in six months. On the other hand, the percentage anticipating higher incomes declined slightly from 18.8 percent to 18.3 percent, which remains better than the 16.4 percent who said the same thing in February.

Looking at buying plans, respondents were less likely to purchase an appliance (down from 49.6 percent to 46.8 percent) or automobile (down from 12.7 percent to 10.8 percent). Yet, they were also somewhat more likely to purchase a home (up from 4.8 percent to 5.2 percent). Home-buying intentions remain soft, however, down from 6.5 percent in November.

Construction Spending

The Census Bureau reported that manufacturing construction increased 2.8 percent in March, rising to an annualized $69.81 billion. This was the second consecutive month in which this figure reached an all-time high, surpassing last month's $67.93 billion. As such, construction activity has fully recovered from the recession, when spending plummeted to a low of $29.74 billion in January 2011. Across the past year, manufacturing construction has jumped significantly, up from $46.33 billion in March 2014, or an increase of 50.7 percent. This sharp increase suggests that manufacturing leaders have enough confidence in their outlook to warrant additional construction investment, which is encouraging.

At the same time, the overall report was less positive. Total construction spending declined 0.6 percent, with decreases in residential (down 1.6 percent) and public-sector (down 1.5 percent) spending. Dollars devoted to residential spending have declined 2.3 percent year-over-year, and public construction projects have edged down 0.3 percent since March 2014.

In contrast, private, nonresidential construction (up 1.0 percent) was a bright spot. Beyond manufacturing, other nonresidential business segments with more spending in March included communications (up 12.0 percent), lodging (up 5.7 percent), transportation (up 3.3 percent) and office (up 2.9 percent) industry projects. Religious (down 5.2 percent), amusement and recreation (down 3.4 percent), commercial (down 2.7 percent), power (down 0.9 percent) and educational (down 0.5 percent) projects saw spending declines for the month.

Dallas Fed Manufacturing Survey

The Dallas Federal Reserve Bank reported that manufacturing activity contracted in Texas for the fourth straight month. The composite index of general business conditions rose from -17.4 in March to -16.0 in April, suggesting a slightly slower pace of decline for the month. Yet, manufacturers in the district are struggling with lower crude oil prices and a stronger U.S. dollar. Each was mentioned several times in the sample comments, providing a double whammy to the Texas economy. Nearly 28 percent of manufacturing respondents to the survey suggested that conditions had worsened in April, versus 11.7 percent indicating some improvement.

The April data reflected a broad set of weaknesses in the market. A number of indicators continued to contract, even with some easing for the month in a few key measures. These included new orders (up from -16.1 to -14.0), production (up from -5.2 to -4.7) and shipments (up from -8.7 to -5.6). Capacity utilization saw a larger decrease for the month (down from -6.4 to -10.4).

Still, it was not all bad news. Raw material costs (down from -9.4 to -11.2) were lower, and manufacturers continue to invest in their businesses. Hiring (up from -1.8 to 1.8) and capital expenditures (up from 0.0 to

3.3) both returned to being a net positive in April. This suggests that leaders in the sector remain mostly upbeat in their outlook for the future, warranting additional workers and increased investments.

Indeed, roughly 45 percent of respondents predict higher new orders over the next six months, with 41.2 percent expecting increased production. Moreover, 26.1 percent anticipate adding to their workforce, and 21.6 percent expect to grow their capital expenditures in the coming months. However, many of the forward-looking indices decelerated in April—a reflection of the headwinds noted above in the current economic environment. The percentage of respondents indicating a worsening of expected business conditions rose from 16.1 percent in March to 23.0 percent in April. As such, to the extent that manufacturers are net optimists overall, the report makes it clear there is a lot of anxiousness in such sentiments.

Employment Cost Index

The Bureau of Labor Statistics reported that manufacturing compensation costs rose 0.7 percent in the first quarter, up from a 0.6 percent gain in the fourth quarter. Wages and salaries in the sector were up 0.6 percent in the first quarter, and benefits increased 0.8 percent. Manufacturing workers earned 2.4 percent since the first quarter of 2014, essentially the same year-over-year pace as observed in the fourth quarter. Each was the fastest pace since the second quarter of 2011.

Overall, the employment cost index for private-sector workers also increased 0.7 percent in the first quarter, with wages and salaries up 0.7 percent and benefits up 0.6 percent. Wages and salaries have risen 2.5 percent year-over-year, and benefits have grown 2.7 percent over that time frame. The Bureau of Labor Statistics does not break out various benefit costs, including health insurance, in its quarterly releases.

Gross Domestic Product (First Quarter 2015)

For weeks, I have spoken about a number of economic headwinds that have negatively impacted manufacturing activity. These challenges have included weaknesses abroad, a strong U.S. dollar, lower crude oil prices, residual impacts from the West Coast ports slowdown, bad weather in some regions of the country and a still-cautious consumer. Indeed, the latest real GDP data show that the U.S. economy stagnated in the first quarter, up just 0.2 percent at the annual rate. This compares to a consensus estimate of 1.1 percent, and it was lower than the 5.0 percent and 2.2 percent growth rates observed in the third and fourth quarters of 2014, respectively.

As one might expect from a data point that is just shy of zero, the underlying contributions to growth were quite mixed. Consumer and business spending had been bright spots over the past three quarters, and in this report, those two components added 1.65 percentage points to the headline number. Yet, this was primarily due to increased spending on consumer services, particularly for housing and utilities as well as health care, and to a rebound in inventory spending. In contrast to these strengths, consumer spending on goods was up only 0.2 percent. Businesses also spent dramatically less on nonresidential structures, with equipment spending slowing to a crawl. Much of this could stem from reduced investments due to current energy prices. In total, nonresidential fixed investment fell 3.4 percent, its first quarterly decline in four years, led by a whopping 23.1 percent decrease in structure spending.

The larger drags on real GDP growth, however, came from net exports and government spending. With softer global growth and an accelerated dollar, it has been harder for manufacturers in the United States to increase demand overseas. Goods exports fell 13.3 percent in the first quarter, with goods imports edging up 0.9 percent. As a whole, the net export of goods and services subtracted 1.25 percentage points from the final real GDP number. Net exports have been a drain on growth in four of the past five quarters.

Government spending subtracted 0.15 percentage points from growth. Federal defense and state and local government spending fell 0.7 percent and 1.5 percent, respectively, in the first quarter.

ISM Purchasing Managers' Index

The Institute for Supply Management's manufacturing PMI was unchanged at 51.5 in April. On the positive side, manufacturing activity has continued to expand modestly; yet, the data reflect softness in the market over the past few months. Six months ago, for instance, the PMI value was 57.9, and this headline number has trended lower since then. Demand and output have shifted into a lower gear on challenges from a stronger U.S. dollar, reduced crude oil prices, residual impacts from the West Coast ports slowdown and other factors. These headwinds were top-of-mind for survey respondents in this report.

At the same time, manufacturers have expressed some cautious optimism about the coming months, and this report also indicates a slight rebound in new orders (up from 51.8 to 53.5) and production (up from 53.8 to 56.0). These figures remain lower than their averages in the second half of 2014, which were 61.4 and 61.6, respectively. Nonetheless, it suggests some upward movement, with decent expansions for both. We hope this is a sign of better data moving forward. Along those lines, export orders (up from 47.5 to 51.5) returned to net growth in April, which was encouraging.

One discouraging development was the weakened hiring picture. The employment index (down from 50.0 to 48.3) contracted for the first time since May 2013. In some ways, this mirrors the slower hiring pace seen in the past two national releases, after experiencing average manufacturing job growth of roughly 15,500 per month over the past 15 months. Employment is a lagged indicator, however, and I would expect this index to return to modest growth in the coming months.

We continue to see reduced prices for raw materials (up from 39.0 to 40.5), albeit declining at a slower pace in April than in March. Lower energy costs have put downward pressure on inflation.

Personal Income and Spending

The Bureau of Economic Analysis reported that personal spending rose 0.4 percent in March. As such, consumer spending accelerated from February's 0.2 percent gain and declines in December and January. From a manufacturing perspective, both durable and nondurable goods spending was higher in March, up 1.8 percent and 0.6 percent, respectively. While this is encouraging, particularly if it is the beginning of a rebound, the data also show just how weak consumer spending on goods has been in the first quarter, down 2.2 percent from the fourth quarter. Indeed, the year-over-year pace of personal spending growth has fallen from 4.3 percent in October to 3.0 percent in March. The good news is that this still represents a modest pace of growth.

Meanwhile, personal income growth was flat in March, up just 0.04 percent. The same was true for manufacturing, with total wages and salaries in the sector unchanged at $790.6 billion for the month. The longer-term trend has been more promising, with manufacturing wages and salaries totaling $747.6 billion and $777.2 billion on average in 2013 and 2014, respectively.

With higher spending for the month, the savings rate declined from 5.7 percent in February to 5.3 percent in March. Nonetheless, this continues to be higher than a few months ago, with the savings rate being 4.4 percent as recently as November.

In other news, the personal consumption expenditure (PCE) deflator rose 0.2 percent in March, increasing for the second straight month. This mirrored some recovery in prices for energy goods and services, which increased 1.1 percent and 1.5 percent in February and March, respectively. Still, even with these gains, energy prices remain 18.5 percent lower than a year ago. On a year-over-year basis, the PCE deflator was up just 0.3 percent, with core inflation, which excludes food and energy prices, up 1.3 percent. Each suggests that pricing pressures continue to be minimal for now.

Richmond Fed Manufacturing Survey

The Richmond Federal Reserve Bank reported that manufacturing activity remained soft in April, contracting for the second straight month. If there was a silver lining, it was that several key indicators declined by less in this report. The composite index of general business conditions improved from -8 in March to -3 in April. Along those lines, declines eased for a number of indices, including new orders (up from -13 to -6), shipments (up from -13 to -6) and capacity utilization (up from -7 to -4). New orders decreased for the third consecutive month, reflecting weaker demand.

There was better news on the labor market front. The pace of hiring accelerated slightly (up from 6 to 7), and the average workweek widened (up from -4 to 4). Wages were also higher (up from 8 to 9). These indicators suggest that manufacturers are still willing to increase their employment levels despite current economic headwinds.

Indeed, business leaders in the region continue to be mostly upbeat in their assessments of the next six months, which is likely helping to drive a need for a bigger workforce. The forward-looking measures were mixed but reflect stronger expansions over the next six months, such as for new orders (down from 35 to 32), shipments (up from 37 to 38), employment (down from 23 to 15) and capital expenditures (down from 32 to 26).

Meanwhile, inflationary pressures remain minimal, largely on reduced energy costs. Manufacturers in the region reported that prices paid for raw materials grew 0.69 percent at the annual rate in April, up from 0.62 percent in March. This pace was down sharply from the 2.22 percent rate in October. Looking ahead six months, respondents anticipate raw material prices to increase 1.22 percent at the annual rate, down from last month's 1.53 percent pace.

University of Michigan Consumer Sentiment (Revision)

Consumer confidence improved somewhat in April, according to final figures from the University of Michigan and Thomson Reuters. The headline index in the Surveys of Consumers increased from 93.0 in March to 95.9 in April, with the final number unrevised from its preliminary estimate made two weeks ago. This latest report reversed the easing in sentiment seen in February and March. Even with better data in April, Americans remain less confident today than in January, when the 98.1 reading was the highest level since January 2004.

The data reflect improved assessments for the current (up from 105.0 to 107.0) and forward-looking (up from 85.3 to 88.8) measures. The current conditions index has now exceeded 100 for six straight months. This is encouraging, and we hope a sign that recent weaknesses in the data will be short lived.

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Questions or comments?

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