

Global economic roundup: US jobs, European manufacturing, and Chinese confidence



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US jobs

The August jobs report showed that the US economy is slowing, but it's still in very good condition.

European manufacturing

Manufacturing new orders in the eurozone fell to one of the lower levels on record in August.

Chinese confidence

As China's post-pandemic economic reopening falters, stimulus could help boost confidence.

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In many parts of the world, school is back in session and summer is unofficially over. For those who spent the last few days or weeks at the beach, the Eminem lyric "Snap back to reality" might feel particularly appropriate today. Snapping back to reality means it's time for a quick catch up on relevant news and recent data. I also believe snapping back to reality means recognizing that a "soft landing," even for the US economy, is unlikely given the "long and variable lags" of monetary policy. File this week's update under the theme "Bumpy landing – bumpy takeoff."

- Many developed economies are in the midst of a bumpy landing as central banks try to tame inflation without starting a recession. So far, the US is experiencing less turbulence than the eurozone and the UK, but I don't expect even the US economy to get away with a truly soft landing.
- At the same time, China is experiencing a very bumpy takeoff as it tries to boost economic growth following years of pandemic-related restrictions.

Let's review some of the most recent data.

Bumpy landing: US

The August US jobs report¹ showed an economy that is slowing but still in very good condition. Job creation was solid, although the number of jobs created in the previous two months was revised down by 110,000. Unemployment edged up to 3.8%. Most importantly, in my opinion, wage growth eased. Average hourly earnings rose 0.2% for the month and 4.3% year over year.

Wage growth is a powerful factor in overall inflation, and it's heartening to see it getting closer to pre-pandemic levels. Wage growth will likely continue to moderate given that job openings continue to fall. US job openings, which peaked in March 2022 at 12 million, fell to 8.8 million in July.² This was the first time job openings were below 9 million since March 2021.²

The US economy has thus far been relatively unscathed by aggressive tightening on the part of the Federal Reserve (Fed), but we know credit conditions have tightened significantly, so I anticipate there will be more damage. For example, one upscale furniture manufacturer in the US recently announced it was going out of business, largely because it was unable to secure financing. I suspect more will follow.

Bumpier landing: Eurozone

Purchasing Managers' Indexes (PMI) for August³ showed a eurozone economy that is under more pressure than that of the US. The S&P Global HCOB composite euro-zone PMI for August was 46.7, close to its weakest level in nearly three years, which indicates a rapid decline. Services PMI fell to 47.9 from 50.9 in July, putting it into contraction territory for the first time this year. Most concerning were the new orders sub-indexes for both services and manufacturing. They both declined, with manufacturing new orders faring worse. Germany is under particular pressure, with the overall decline in activity in Germany the strongest since June 2009 with the exception of the pandemic.

The silver lining is that an increasingly negative impact to the eurozone economy, especially if it comes with moderating inflation, may mean an earlier end to rate hikes by the European Central Bank (ECB). Recent inflation-related metrics are helping that case. August core inflation slowed, and consumer inflation expectations remain relatively well-anchored, with one-year ahead expectations remaining at 3.4% and three-year ahead expectations nudging up slightly to 2.4%.⁴

Also bumpy: UK

The UK economy has also been negatively impacted by rate hikes, as evidenced in its most recent PMI surveys.⁵ The S&P Global/CIPS Purchasing Managers' Index (PMI) for the UK manufacturing sector fell to 48.6 from 50.8 in July. And its services sector PMI dropped to 49.5 in August from 51.5 in July. The services sector reading is at a seven-month low, while the manufacturing reading is at the lowest level since May 2020.

This is problematic given that the Bank of England (BOE) is poised to remain hawkish beyond when the Fed and even the ECB are expected to end rate hikes, which could cause more damage to the UK economy. However, that could change, especially if recent rapid declines in inflation continue. And so it will be important to see the extent to which a cooling UK economy translates into cooling inflation in the near term, which could then translate into a less hawkish BOE.

Bumpy takeoff: China

In China, the post-pandemic reopening has been disappointing. The lagged effects of monetary policy have played a role here too, as rate hikes in the US and Europe have weighed on global demand for goods. This has impacted China's manufacturing sector and contributed to the uneven recovery.

Services activity⁶ has been better, although it has come under pressure as well. The Caixin China Services PMI fell to 51.8 in August from 54.1 in July. That's still in expansion territory, but it's the lowest level we've seen in eight months. However, unlike we've seen in the eurozone, the new orders sub-index is suggesting there could be improvement ahead.

One issue that has been problematic for China is the property sector. However, the situation appears poised to improve. Policymakers in China have recently announced some measures that will support the property sector, including easing lending rules for first-time buyers; these include lowering mortgage rates and easing the down payment

ratio. In addition, it was announced on Sept. 5 that major property developer Country Garden was able to avoid default. Country Garden honored its US bond coupon payments just before the grace period was to end.

Ultimately, this is a confidence game. Chinese policymakers need to provide enough stimulus to boost confidence. Measures such as last week's significant cut in the tax on securities transactions and the measures to support the property sector could potentially help build that confidence, in my opinion, but more is needed.

A bumpy road: Markets

Uncertainty over monetary policy has contributed to significant swings in the 10-year US Treasury yield, which had a substantial impact on the performance of the S&P 500 Index in August.

The S&P 500 Index was down for August overall, but it finished well above its lows as a late-month fall in the 10-year US Treasury yield took some pressure off stocks. That fall in the 10-year yield was prompted by data suggesting that inflation is moderating, which increased expectations the Fed would end its hiking cycle.

At the end of the day, policy matters for markets, just as it does for economies. Once there is clarity that the Fed rate hike cycle has ended, I expect that could not only be positive for risk assets but it could result in a weakening US dollar, which in turn could be particularly positive for emerging market equities.

Also helping is that emerging market central banks have already begun to ease. It's not just China cutting rates; Brazil and Chile have as well, and there are expectations that Mexico and even Taiwan and Korea could soon follow. As more targeted policy is rolled out to support China's economy, I believe that will be positive for Chinese equities.

This is a time to follow monetary and fiscal policy closely, including the Sept. 6 meeting of the Bank of Canada, which has been something of a first mover when it comes to monetary policy. Changes are in the air, and that can lead to investment opportunities.

Notes

¹Source for all US jobs data: US Bureau of Labor Statistics, as of Sept. 1, 2023

²Source: Job Openings and Labor Turnover Survey, US Bureau of Labor Statistics, as of Aug. 29, 2023

³Source for eurozone PMI data: S&P Global as of Sept. 5, 2023

⁴Source: European Central Bank, as of Sept. 5, 2023

⁵Source for UK PMI data: S&P Global/CIPS, as of Sept. 1, 2023, and Sept. 5, 2023

⁶Source for China PMI data: S&P Global/Caixin Media, as of Sept. 5, 2023

Important information

Past performance is not a guarantee of future results.

This does not constitute a recommendation of any investment strategy or product for a particular investor. Investors should consult a financial professional before making any investment decisions.

All investing involves risk, including the risk of loss.

In general, stock values fluctuate, sometimes widely, in response to activities specific to the company as well as general market, economic and political conditions.

The risks of investing in securities of foreign issuers, including emerging market issuers, can include fluctuations in foreign currencies, political and economic instability, and foreign taxation issues.

Investments in companies located or operating in Greater China are subject to the following risks: nationalization, expropriation, or confiscation of property, difficulty in obtaining and/or enforcing judgments, alteration or discontinuation of economic reforms, military conflicts, and China's dependency on the economies of other Asian countries, many of which are developing countries.

The Eurozone (also known as the euro area or euroland) is an economic and monetary union of 18 European Union member states that have adopted the euro (€) as their common currency.

Purchasing Managers' Indexes are based on monthly surveys of companies worldwide, and gauge business conditions within the manufacturing and services sectors.

The HCOB Eurozone Composite PMI® is compiled by S&P Global from responses to questionnaires sent to survey panels of manufacturers in Germany, France, Italy, Spain, the Netherlands, Austria, Ireland and Greece, and of service providers in Germany, France, Italy, Spain and Ireland, totalling around 5,000 private sector companies.

The S&P Global/CIPS UK Purchasing Managers' Index is compiled from survey data collected from supply chain managers in the UK and hundreds of companies each month in manufacturing, services and construction sectors.

The Caixin China General Services PMI is based on data compiled from monthly replies to questionnaires sent to purchasing executives in over 400 companies.

Tightening monetary policy includes actions by a central bank to curb inflation.

The opinions referenced above are those of the author as of September 5, 2023. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.