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HaMMR Digest

Stay current with economic and mortgage market trends.

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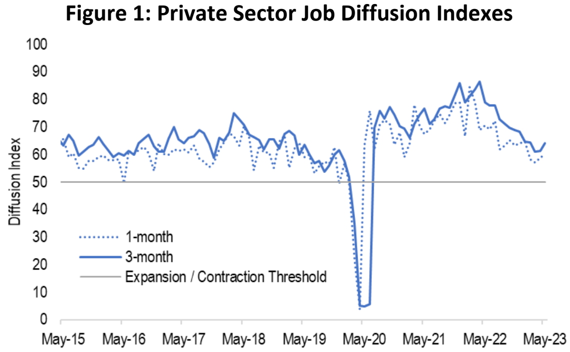
Weekly Wrap — Cross Currents

- Job growth came in strong again with a 339k monthly gain in May on top of upward revisions to prior months.
- Underlying labor market details, however, still show normalization is underway.
- The Fed will likely pause in June, but the door remains wide open for a July hike.

Incoming data keep surprising mostly to the upside with the labor market taking center stage this week. Headline job growth handily beat consensus expectations for a record 14th time in a row, rising 339k m/m (cons. 195k) on top of an upward revision of 93k to the prior two months combined. Aggregate labor income for total private and non-manager private payrolls grew a healthy 3.8% and 6.4%, respectively, on a three-month annualized basis while the breadth of job gains, as measured by the one-month diffusion index, rose for the second month in a row to 60.2, a four-month high (Figure 1). The prime age (i.e., 25-54-year-old) labor force participation rate hit another 21-year high, rising to 83.4%, while the job openings-to-unemployed ratio rose to 1.8 in April from 1.6 in March.

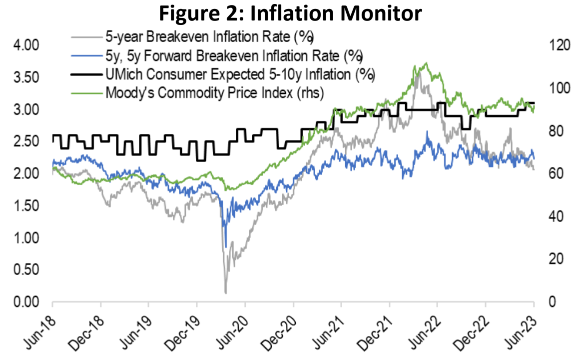
The picture, though, is not so clear. The unemployment rate ticked higher by 26bps to 3.65% (cons. 3.5%) as unemployment rose by 440k m/m, the largest monthly increase since April 2020. Labor force flows into employment are falling, further supported by the steady decline in both hires and quits rates in recent months while the duration of unemployment has tracked higher. Household perceptions of labor market conditions, as proxied by the Conference Board's labor market differential measuring the difference between households' perception that jobs are "plentiful" vs. "hard to get," declined from its lofty level of 38% over the prior three months to 31% in May, a 25-month low.

Figure 1: Private Sector Job Diffusion Indexes



Source: Bureau of Labor Statistics, Arch MI

Figure 2: Inflation Monitor



Sources: Moody's, University of Michigan, Federal Reserve Board, Arch MI

Although the labor market is not as hot as six months ago, it is still supporting incomes and in turn the outlook for consumer spending and housing. Real personal spending rose 0.5% m/m in April (cons. 0.3%) with growth shared across services and goods. New home sales surprised to the upside again in April, rising 4.4% m/m (cons. 3.3%) to a seasonally adjusted annual rate (saar) of 683k, adding to evidence that the new home sales market has found a bottom. Goods producers are still struggling with a plethora of Purchasing Managers' Indexes (PMI) pointing to slumping near-term activity. The ISM Manufacturing PMI fell to 46.9 in May (cons. 47.0) from 47.1 in April. Production rose on the month despite new orders, backlogs and inventories declining as producers were content keeping operations lean in an uncertain environment, a theme echoed in Fed regional and S&P PMI surveys. However, construction spending grew at a robust 1.2% m/m in April (cons. 0.2%) with private non-residential investment activity bolstered by ongoing manufacturing investment while residential spending rose 0.4% m/m, the largest increase since last May.

In total, the data flow for the prior two weeks does not solidify the green light for the Fed to raise rates at their June meeting. Despite still-hot realized consumer inflation, expectations remain well-anchored (Figure 2) and recent Fed commentary strongly suggest that risk management supersedes an "insurance" hike with markets pricing in a roughly 30% chance the Fed hikes next week and a 75% chance they hike in July. It would be unprecedented for the Fed to pause for a month then resume hiking after such a rapid pace of tightening, but life has been unprecedented since the pandemic and we do not rule out one more hike if inflation does not cool as expected.

Recent Data Releases

Key economic and housing data releases over the last week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
5/23/23	S&P Global US Services PMI	May P	**55.1**	52.5	53.6	index, sa
5/23/23	S&P Global US Composite PMI	May P	**54.5**	53.0	53.4	index, sa
5/23/23	New Home Sales	Apr	**683**	665	656	k, saar
5/23/23	New Home Sales m/m	Apr	**4.1%**	-2.6%	4.0%	sa
5/25/23	GDP Annualized q/q	1Q S	**1.3%**	1.1%	1.1%	saar
5/25/23	Personal Consumption q/q	1Q S	**3.8%**	3.7%	3.7%	saar
5/25/23	Core PCE Inflation q/q	1Q S	**5.0%**	4.9%	4.9%	saar
5/25/23	Pending Home Sales m/m	Apr	**0.0%**	1.0%	-5.2%	sa
5/25/23	Pending Home Sales y/y	Apr	**-22.6%**	-20.1%	-23.3%	nsa
5/26/23	Durable Goods Orders	Apr P	**1.1%**	-1.0%	3.3%	m/m, sa
5/26/23	Personal Income	Apr	**0.4%**	0.4%	0.3%	m/m, sa
5/26/23	Personal Spending	Apr	**0.8%**	0.5%	0.1%	m/m, sa
5/26/23	Real Personal Spending	Apr	**0.5%**	0.3%	0.0%	m/m, sa
5/26/23	PCE Inflation m/m	Apr	**0.4%**	0.3%	0.1%	sa
5/26/23	PCE Inflation y/y	Apr	**4.4%**	4.3%	4.2%	nsa
5/26/23	PCE Core Inflation (ex Food and Energy) m/m	Apr	**0.4%**	0.3%	0.3%	sa
5/26/23	PCE Core Inflation (ex Food and Energy) y/y	Apr	**4.7%**	4.6%	4.6%	nsa
5/26/23	U. of Mich. Sentiment	May F	**59.2**	58.0	57.7	index, nsa
5/26/23	U. of Mich. 1 Yr Inflation	May F	**4.2%**	4.5%	4.5%	nsa
5/26/23	U. of Mich. 5-10 Yr Inflation	May F	**3.1%**	3.1%	3.2%	nsa
5/30/23	FHFA House Price Index m/m	Mar	**0.6%**	0.2%	0.7%	sa
5/30/23	S&P CoreLogic CS 20-City m/m SA	Mar	**0.5%**	0.0%	-0.1%	sa
5/30/23	S&P CoreLogic CS 20-City y/y NSA	Mar	**-1.2%**	-1.6%	0.4%	nsa
5/30/23	Conf. Board Consumer Confidence	May	**102.3**	99.0	103.7	index, sa
5/31/23	MBA Mortgage Applications	5/26/23	**-3.7%**	--	-4.6%	w/w, sa
5/31/23	JOLTS Job Openings	Apr	**10.1**	9.4	9.7	m, sa
6/1/23	ADP Employment	May	**278**	170	291	k, m/m, sa
6/1/23	Nonfarm Productivity	1Q F	**-2.1%**	-2.4%	-2.7%	q/q, saar
6/1/23	Unit Labor Costs	1Q F	**4.2%**	6.0%	6.3%	q/q, saar
6/1/23	Initial Jobless Claims	5/27/23	**232**	235	230	k, sa
6/1/23	Continuing Claims	5/20/23	**1,795**	1,800	1,789	k, sa
6/1/23	S&P Global US Manufacturing PMI	May F	**48.4**	48.5	48.5	index, sa
6/1/23	ISM Manufacturing	May	**46.9**	47.0	47.1	index, sa
6/1/23	ISM Prices Paid	May	**44.2**	52.3	53.2	index, nsa
6/1/23	Wards Total Vehicle Sales	May	**15.1**	15.3	15.9	m, saar
6/2/23	Nonfarm Payrolls	May	**339**	195	294	k, m/m, sa
6/2/23	Private Payrolls	May	**283**	168	253	k, m/m, sa
6/2/23	Unemployment Rate	May	**3.7%**	3.5%	3.4%	sa
6/2/23	Average Hourly Earnings m/m	May	**0.3%**	0.3%	0.4%	sa
6/2/23	Average Hourly Earnings y/y	May	**4.3%**	4.4%	4.4%	nsa
6/2/23	Average Weekly Hours All Employees	May	**34.3**	34.4	34.4	sa
6/2/23	Labor Force Participation Rate	May	**62.6%**	62.6%	62.6%	sa

Sources: Bloomberg Consensus Survey of Economists, Arch MI

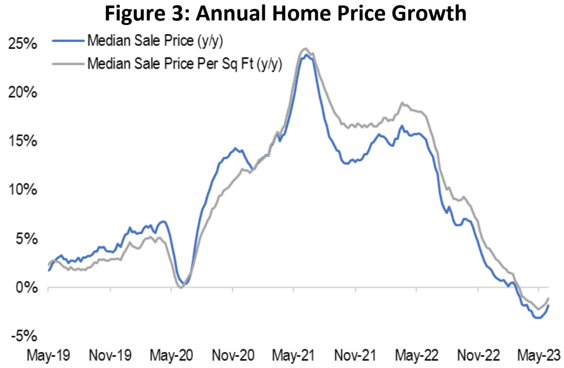
Green = beat expectations; **Red** = worse than expectations; (compared vs. prior if no consensus estimates available)

HOUSING MARKET TRANSITIONING TO A NEW PHASE

The housing market has transitioned from its tightest state in history in 2021, when demand far exceeded supply to a softening market in 2022 as demand fell in response to affordability constraints caused by rapidly rising home prices and mortgage rates surging from below 3% to above 7%. Now the housing market is transitioning into a new phase in 2023 where the remaining pool of buyers who are able to afford a home with mortgage rates above 6% still exceeds the available supply. As we have mentioned previously, the persistent market tightness has been driven by a lack of existing homeowners listing their homes for sale and a surge in the number of listed homes being pulled off the market. Had new listings and delisted homes followed the typical pre-COVID-19 seasonal pattern in 2023, the housing market would be approaching a relative balance similar to that which prevailed at the onset of the pandemic. Instead, the months' supply of homes for sale remained nearly 30% below the typical pre-COVID-19 level for this time of year and prices have responded by rising at a double-digit annualized pace over the past quarter. We do not expect that price momentum to be sustained over the summer as the recent surge in mortgage rates back toward 7% has cooled demand. On net, we expect mortgage rates to trend back toward the low-6% range by year-end and a stabilization in demand at a lower than pre-COVID-19 level to modestly lift home prices in 2023. Despite that national narrative, we expect home-price declines to persist over 2023 for the most overvalued markets (predominantly located in the western half of the U.S.) while more balanced markets in the Midwest and East record modest price growth.

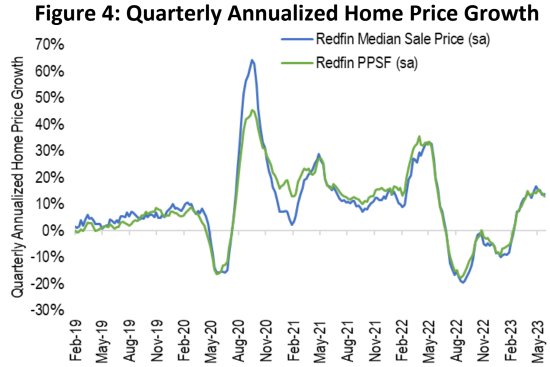
We have mentioned that annual comparisons would remain challenged over the first half of the year, given the vastly different housing markets in the first half of 2022 and the first half of 2023. However, as we approach mid-year, annual comparisons will instead receive a tailwind due to comparisons with the weak second half of 2022. Case in point, per Redfin data for the week ending May 28, despite the -1.1% year-over-year decline in the national median sale price per square foot (Figure 3) — up from -1.7% last week and -2.2% four weeks ago — the pace of price growth over the past quarter translates to a seasonally adjusted 13% annualized rate, a sharp reversal from the -18% annualized decline reached last August (Figure 4). Accordingly, we expect year-over-year home-price growth to rebound over the coming months. Annual growth in the national median sale price per square foot accelerated to -1.1% y/y, all of which represent a drastic slowdown from the 18% annual gain recorded at this time last year.

Figure 3: Annual Home Price Growth



Source: Redfin, Arch MI

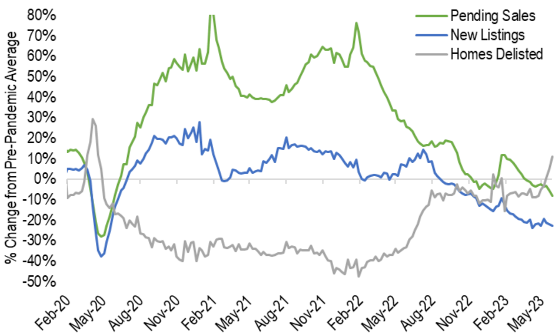
Figure 4: Quarterly Annualized Home Price Growth



Source: Redfin, Arch MI

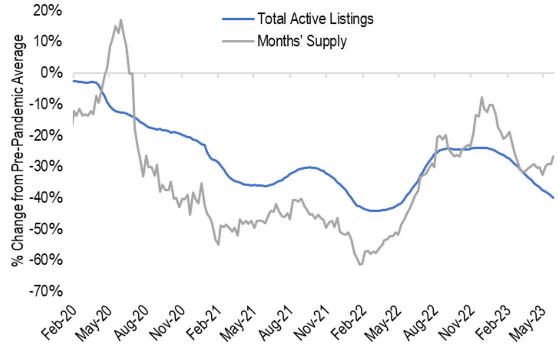
Pending home sales were down roughly -21k y/y (Figure 5), or -27% below the year-ago level. The recent pace of pending sales was -8% below the pre-pandemic average for this time of year but deteriorated slightly from -5% below last week and -3% three weeks ago. Higher mortgage rates have also weighed on potential sellers as new listings declined to -23% below the pre-pandemic average from -23% four weeks ago. Meanwhile, the number of delisted homes rose to 11% above the pre-pandemic average for this time of year from -5% four weeks ago. The decline in new listings and increase in delisted homes offset the cooling pace of sales and pushed the number of active listings down to -40% below the pre-pandemic average and well below last year's peak of -25% (Figure 6). Despite total homes sold being down -25% y/y and -19% below the pre-pandemic average, the national market remains somewhat tight given months' supply is 2.5 months, -27% below the pre-pandemic average for this time of year. The current months' supply is a modest increase from the 1.9 months recorded for the same week in 2022 when the market was incredibly tight.

Figure 5: U.S. Existing Home Sales Market Dynamics



Source: Redfin, Arch MI

Figure 6: U.S. Active Listings & Months' Supply



Source: Redfin, Arch MI

Of the major metros we track (Figure 7), annual home-price growth was weakest in **Austin** (-18%), **Phoenix** (-10%), **Los Angeles** (-8%), **Denver** (-6%) and **Seattle** (-6%). Home-price growth slowed most rapidly compared with a year ago in **Austin** (-41%-pts), **Phoenix** (-35%-pts), **Tampa** (-33%-pts), **Dallas** (-31%-pts) and **Nashville** (-27%-pts). Conversely, annual home-price growth was strongest in **Miami** (4%), **Washington DC** (1%) and **Chicago** (1%). Median days on the market have extended alongside softening market conditions, with many markets exceeding pre-pandemic timelines. Markets with the longest median days on the market relative to the pre-pandemic norm include **Austin** (31 days longer), **Chicago** (20) and **Boston** (8), while some markets like **New York** (-33) and **Tampa** (-11) remained well below pre-pandemic timelines. Markets that have deteriorated the most based on months' supply include **Austin**, **Seattle** and **Portland**, where months' supply climbed to a respective 51%, 1% and -1% relative to their pre-pandemic averages from -18%, -25% and -38% below one year ago. Months' supply remained below pre-pandemic levels in most markets (-27% below nationally), with **Baltimore** (-45%), **San Diego** (-40%), **Atlanta** (-37%), **Riverside** (-30%) and **New York** (-27%) remaining the tightest relative to their pre-pandemic averages.

Figure 7: Weekly Housing Monitor (as of May 28, 2023)

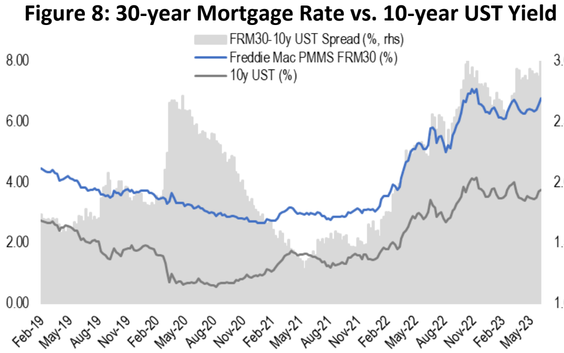
Metro	Median Sale Price Per Square Foot (y/y)		Active Listings with Price Drops		Share of Homes Sold Above List		Average Sale-to-List Ratio		Total Active Listings (y/y)	Median Days on Market vs Pre-COVID		Months' Supply vs Pre-COVID	
	Current	Year Ago	Current	(Δ y/y, ppt)	Current	(Δ y/y, ppt)	Current	(Δ y/y, ppt)		Current	Year Ago	Current	Year Ago
All Redfin Metros	-1%	18%	5%	1%	35%	-20%	100%	-3%	-3%	-13	-23	-27%	-44%
Atlanta	0%	24%	5%	0%	34%	-27%	99%	-3%	5%	-2	-15	-37%	-46%
Austin	-18%	23%	9%	3%	18%	-49%	98%	-7%	49%	31	6	51%	-18%
Baltimore	1%	11%	5%	0%	51%	-6%	102%	-1%	-12%	-10	-15	-45%	-56%
Boston	0%	12%	4%	0%	60%	-15%	103%	-3%	-17%	8	6	-16%	-31%
Chicago	1%	8%	3%	0%	46%	-7%	100%	-1%	-28%	20	21	-10%	-13%
Dallas	-5%	26%	7%	2%	32%	-40%	99%	-7%	17%	-2	-15	-22%	-44%
Denver	-6%	17%	9%	5%	42%	-29%	100%	-5%	5%	0	-2	-3%	-38%
Houston	-2%	21%	7%	1%	22%	-25%	98%	-3%	24%	-6	-21	-21%	-51%
Los Angeles	-8%	15%	3%	0%	50%	-21%	101%	-4%	-20%	-4	-12	-20%	-27%
Miami	4%	25%	3%	1%	16%	-17%	97%	-2%	0%	-6	-20	-24%	-54%
Minneapolis	-2%	11%	5%	1%	51%	-14%	102%	-3%	-9%	-5	-9	-7%	-33%
Nashville	-1%	26%	5%	1%	21%	-34%	99%	-4%	59%	-1	-30	-6%	-53%
New York	-2%	14%	4%	0%	27%	-6%	100%	-1%	-15%	-33	-44	-27%	-41%
Phoenix	-10%	25%	6%	-1%	19%	-37%	98%	-4%	8%	7	-20	-9%	-29%
Portland	-4%	17%	6%	0%	44%	-22%	101%	-4%	-1%	-2	-6	-1%	-38%
Riverside	-5%	21%	4%	-1%	40%	-26%	99%	-3%	-13%	-9	-26	-30%	-38%
San Diego	-4%	22%	4%	-1%	53%	-16%	101%	-3%	-30%	-7	-9	-40%	-40%
Seattle	-6%	18%	6%	-1%	45%	-23%	101%	-6%	-20%	-1	-2	1%	-25%
Tampa	-2%	31%	8%	1%	20%	-32%	98%	-4%	40%	-11	-26	-24%	-52%
Washington DC	1%	11%	4%	0%	51%	-10%	101%	-2%	-15%	5	-4	-19%	-35%

Note: Data reflects 4-week averages; Source: Redfin, Arch MI

MORTGAGE APPLICATION ACTIVITY DECLINED AGAIN AS RATES SURGED

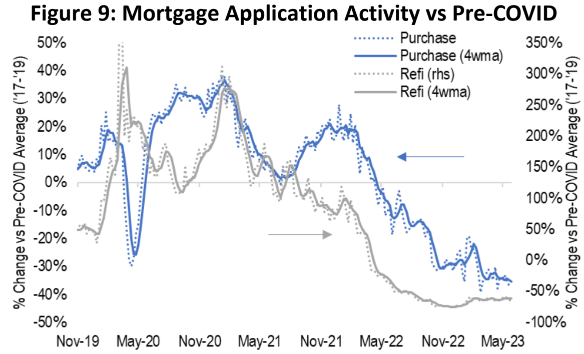
According to the MBA Weekly Applications Survey, the average contract conventional mortgage rate rose 22bps to 6.91% during the week ending May 26 while the FHA contract mortgage rate also rose 29bps to 6.85%, resulting in a 7bps widening of the spread between the FHA and conventional mortgage rate to -0.06%. Freddie Mac's more recent Primary Mortgage Market Survey (PMMS) for the week ending May 31 indicated that the FRM30 jumped 22bps w/w to 6.79% (Figure 8) as 10-year UST yields climbed 4bps to an average of 3.74% over the same period. Accordingly, the spread between the PMMS FRM30 and the 10-year UST widened 18bps to 3.05%, about 135bps wider than its typical non-stressed level prior to the pandemic and the widest spread dating back to 1986. We expect rate volatility and mortgage spreads to remain wide until more clarity is gained around the path of inflation and monetary policy, which is not likely to occur until later this summer.

Figure 8: 30-year Mortgage Rate vs. 10-year UST Yield



Sources: Freddie Mac Primary Mortgage Market Survey, Federal Reserve Board, Arch MI

Figure 9: Mortgage Application Activity vs Pre-COVID



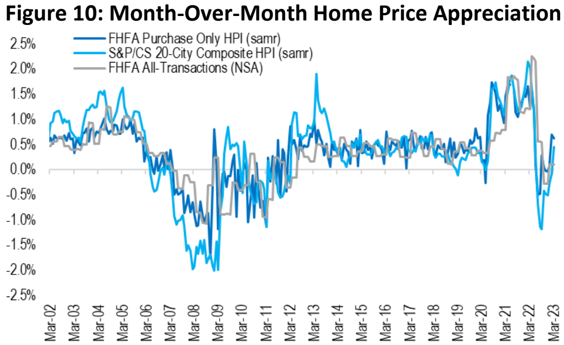
Sources: Mortgage Bankers Association, Arch MI

The MBA Weekly Applications Survey for the week ending May 26 declined -3.7% w/w, leaving the index down -36% year-over-year and down -49% compared with pre-pandemic levels (i.e., the average of the same week in 2017, 2018 and 2019). The weekly decline was driven primarily by a -6.9% decline in refinancing applications, which remained down -45% y/y and -65% below the pre-pandemic level (Figure 9). Purchase applications declined -2.5% w/w and were down -31% y/y and -37% relative to pre-pandemic levels.

HOME PRICES FOUND A BOTTOM IN 1Q23 BUT WHERE TO FROM HERE?

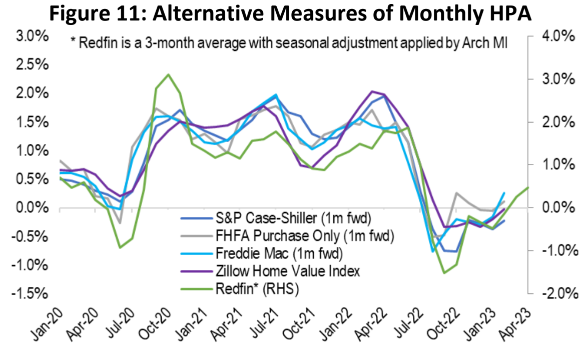
Repeat-sales home price index (HPI) growth improved in March. The FHFA Purchase Only (PO) HPI rose a robust 0.6% m/m (cons. 0.2%) on a seasonally adjusted basis, the third consecutive increase despite a slight deceleration from the 0.7% gain in February (Figure 10). The S&P/Case-Shiller 20-City Composite Home Price Index rose 0.5% (cons. 0.0%) in March, the first monthly increase since June. Fifteen metropolitan areas within the 20-city composite recorded monthly gains, an improvement from 8 in February, 5 in January and none in December. Price declines were most severe in Seattle (-0.9%), Las Vegas (-0.4%) and Cleveland (-0.2%). Other more real-time measures of home-price appreciation (HPA) had already shown a similar improvement in the monthly trend (Figure 11). Based on data from Redfin, monthly HPA continued to trend higher in April and May. While these improvements should be reflected in subsequent releases of the repeat-sales HPIs, the recent upward trend in mortgage rates toward 7% will likely dampen price momentum over the summer.

Figure 10: Month-Over-Month Home Price Appreciation



Sources: S&P, FHFA, Arch MI

Figure 11: Alternative Measures of Monthly HPA



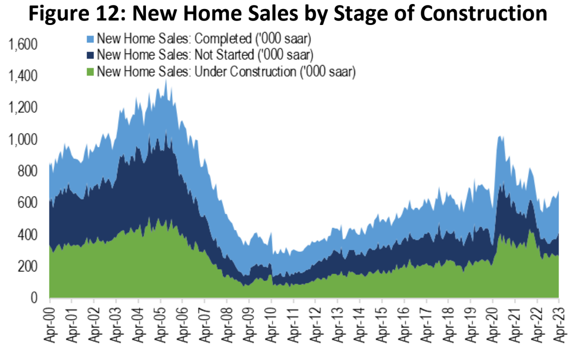
Sources: S&P, FHFA, Freddie Mac, Optimal Blue, Redfin, Zillow, Arch MI

It is important to note that during times of market volatility, there can be divergences between the FHFA and S&P/Case-Shiller HPIs. Index compositional differences do play a factor where the FHFA index is compiled based on conforming, conventional loans purchased and securitized by the GSEs (data included in the index are based on loan origination data) while the S&P/Case-Shiller index captures more transactions and uses a different weighting that places greater emphasis on regions with higher home values. The S&P/Case-Shiller index is a three-month average of closed sales, implying that closed sales for the most recent January–March period could include contracts signed as far back as December.

NEW HOME SALES KEEP SURPRISING TO THE UPSIDE

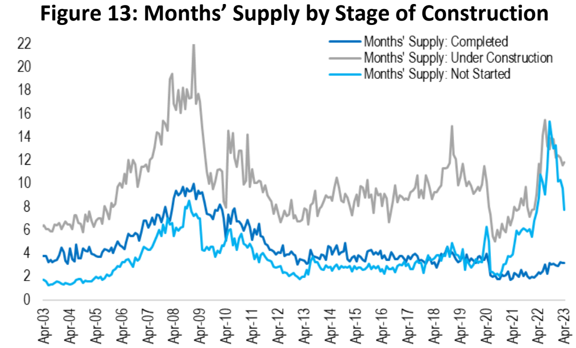
Data from the U.S. Census Bureau showed new home sales climbed for the seventh time in the last eight months through April, rising 4.1% m/m (cons. 3.3%) to a seasonally adjusted annual rate of 683k (cons. 663k) from 656k in March (revised down from 683k). With the multi-month upward trend, new home sales are up 11.8% y/y and 5% above the pre-pandemic pace of sales (Figure 12). Notably, new home sales have been rising since September, albeit on a choppy path, while existing home sales have remained more depressed. Recent commentary from public home builders indicate that demand has steadily improved this year, which confirms the recent improvement in the National Association of Home Builders (NAHB) sentiment index. Additionally, the use of incentives by builders to move product has likely played a factor in bolstering new home sales, which leaves existing home sellers at a relative disadvantage. Accordingly, new home sales comprised 13% of the total home sales market over the past three months, up from 11% at the onset of the pandemic.

Figure 12: New Home Sales by Stage of Construction



Sources: Census Bureau, Arch MI

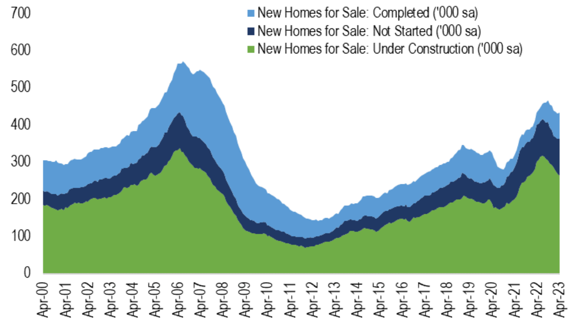
Figure 13: Months' Supply by Stage of Construction



Sources: Census Bureau, Arch MI

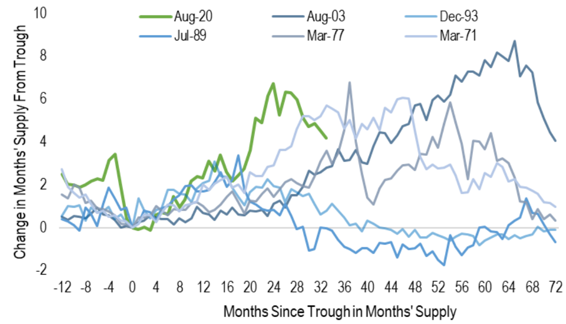
While new home sales continued to trend up, the supply of new homes continued its path to normalization with a mere gain of 0.2% m/m and the first increase in six months. The inventory of new homes for sale in April represented a 7.6 months' supply, down from the cycle peak of 10.1 months back in July and not too far above the historical average of six months. Completed home sales were flat on the month but down -1.5% since December and down -6% from four years ago. The supply of completed, ready-to-occupy inventory was also flat on the month but has been marching higher in recent months, up 6% since December and 106% from one year ago. The rise of completed home inventory reflects a normalization of supply chain constraints rather than a sign of stress given the median time to sell a completed home was just 2.8 months (not seasonally adjusted) in April, down -20% y/y. Additionally, builders continued to prioritize completing units already under construction instead of breaking new ground, which has lifted the months' supply of completed homes to 3.2 months, slightly below where it stood at the onset of the pandemic (Figure 13). The bulk of new home inventory remains skewed toward units not started and under construction, which comprise 84% of the total inventory when combined (Figure 14).

Figure 14: Inventory of New Homes for Sale



Sources: Census Bureau, Arch MI

Figure 15: New Home Months' Supply Cycles



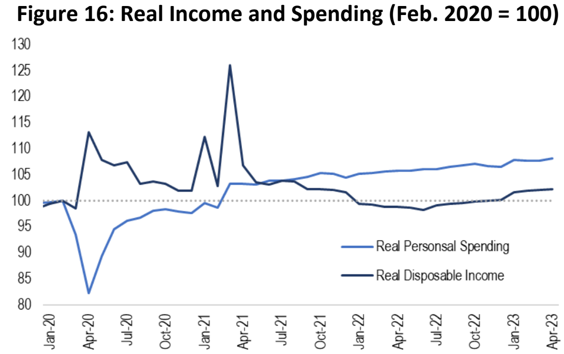
Sources: Census Bureau, Arch MI

Homebuilders have managed through this whiplash-inducing housing cycle much better than during the Global Financial Crisis (GFC). The current cycle for the new home market has been defined by extremes: The pace, magnitude and duration of the slump has been quite unique. The months' supply of new homes surged from a record low of 3.3 months in August 2020 (defined as the peak of the cycle) to a peak of 10.1 months in July 2022 (defined as the trough of the cycle), or an increase of 6.8 months — a deterioration surpassed only by the GFC when months' supply climbed by 8.7 months to a peak of 12.2 months (Figure 15). However, it took over half a decade for the new home sales market to go from its cycle peak in August 2003 to its trough in January 2009, compared with just under two years for the current cycle. Even more impressively, the months' supply of new homes has returned to within shouting distance of its historic average a mere few months after enduring a historic downturn.

CONSUMERS OFF TO A GOOD START IN 2Q

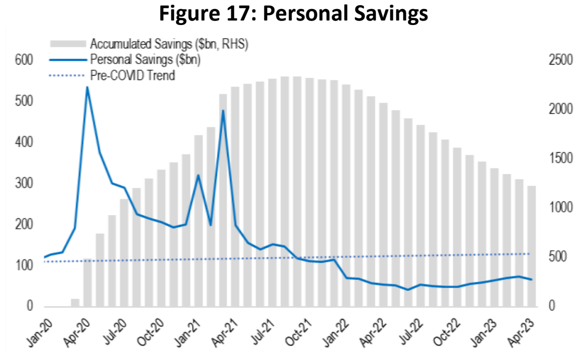
The April personal income and outlay report assuaged concerns that households were "throwing in the towel" as argued by some analysts, given the progressive weakness in spending seen last quarter. April spending was aided by the fact that incomes are starting to at least keep pace with inflation. Nominal personal income rose 0.4% m/m (cons. 0.4%) with steady gains for private wages as the labor market remained tight. Indeed, private wages rose 0.5% m/m and 3.8% on a three-month annualized basis in April, par with the prior three-month average. An additional support to income came from the 1.3% m/m advance in personal interest income — likely a reflection of individuals moving deposits out of the banking system and into higher-yielding money market funds. Meanwhile, nominal disposable income increased 0.4% m/m after a downwardly revised 0.3% gain in March. Nominal spending beat consensus expectations by 30bps, rising 0.8% m/m (cons. 0.5%) with real spending up 0.5% m/m (cons. 0.3%) after a flat reading in March. Real disposable income continued to rise on a three-month annualized basis, up 1.8% in April after an 8.4% gain in March, pushing the absolute level further above where it started the pandemic (Figure 16).

Figure 16: Real Income and Spending (Feb. 2020 = 100)



Sources: BEA, Arch MI

Figure 17: Personal Savings



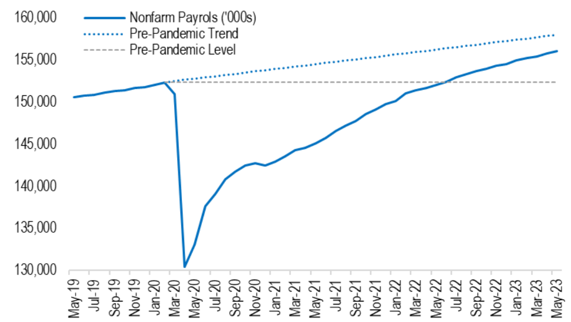
Sources: BEA, Arch MI

With disposable income lagging the pace of spending in April, the savings rate fell 40bps m/m to 4.1% on top of downward revisions to prior months as income was also revised lower. Despite the ongoing strength of the labor market and recovery in real incomes, households are content with dipping into their savings and tapping revolving credit lines to support expenditures. That said, we do see the COVID-19-era savings buffer (Figure 17) being depleted by the end of the year for lower-income households given that the bulk of savings are sitting with higher-income households. With the stock of excess savings trending toward depletion, the outlook for the consumer rests on how long the labor market will remain resilient and how willing consumers will be to tap into credit. We expect the labor market to cool over 2023 and accordingly envision consumer spending downshifting as the year progresses. Higher borrowing costs and tighter credit present downside risks to that already benign outlook. There is some upside risk to our outlook if consumers somehow find the confidence in the face of an economic slowdown to increase borrowing activity, for which they still have capacity given low levels of aggregate outstanding debt relative to incomes.

MAY LABOR MARKET BLOWS THE BARN DOOR OFF?

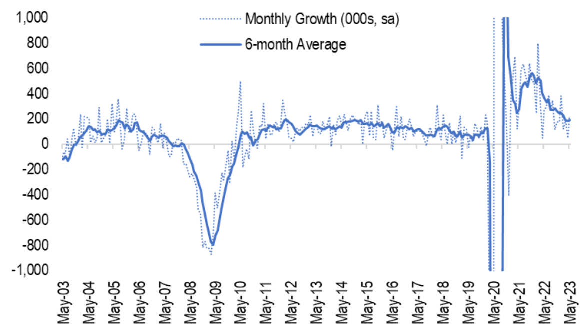
May job growth of 339k (cons. 195k) extended the streak of beating consensus economist forecasts to 14 months and raised the three-month average up to 283k from 253k in April. Through May, the U.S. economy had 3.7 million more jobs than prior to the pandemic (i.e., February 2020) but remained well below the pre-pandemic trend (Figure 18). Some economists have cited a quirk of the employment data known as the "births-deaths" adjustment as artificially inflating the monthly job growth figures. This adjustment is applied by the U.S. Bureau of Labor Statistics to the survey-based estimates of job growth to account for the net effect of businesses opening (births) and going out of business (deaths). The adjustment has averaged a net addition of roughly 110k jobs per month over the past year, which is roughly 20k per month higher than the average pre-COVID-19 adjustment. However, monthly job growth excluding the births-deaths adjustment has averaged 189k over the past six months (Figure 19), which is more than double the pre-COVID-19 pace of roughly 90k.

Figure 18: Nonfarm Payrolls vs Pre-Pandemic Trend & Level



Sources: Bureau of Labor Statistics, Arch MI

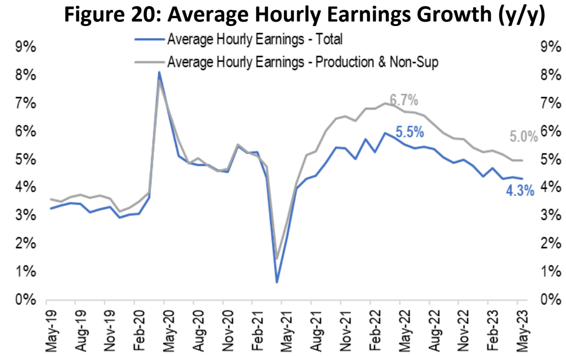
Figure 19: Job Growth Excluding Births-Deaths Adjustment



Source: Bureau of Labor Statistics, Arch MI

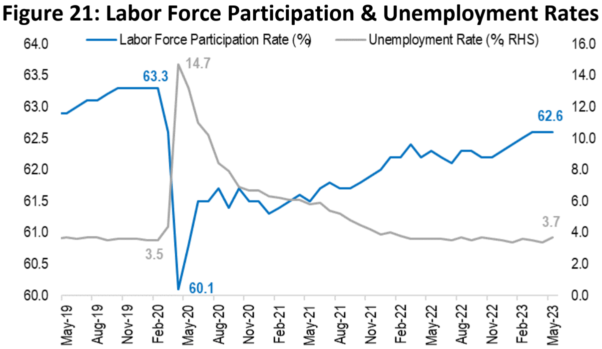
Job gains were led by education and health services (97k), professional and business services (64k) and leisure and hospitality (48k). The breadth of payroll gains improved slightly in May, as reflected by the 1-month diffusion index rising to 60.2 from 58.8. Hourly earnings rose 0.3% m/m (cons. 0.3%) in May and 4.3% y/y (Figure 20) as the unemployment rate rose to 3.65% (cons. 3.5%) amid a 440k m/m increase in the number of unemployed and a steady labor force participation rate of 62.6% (Figure 21). Underlying labor market strength remains despite obvious signs of cooling over the past year, which gives the Fed room to remain vigilant should inflation remain elevated in the months ahead.

Figure 20: Average Hourly Earnings Growth (y/y)



Sources: Bureau of Labor Statistics, Arch MI

Figure 21: Labor Force Participation & Unemployment Rates

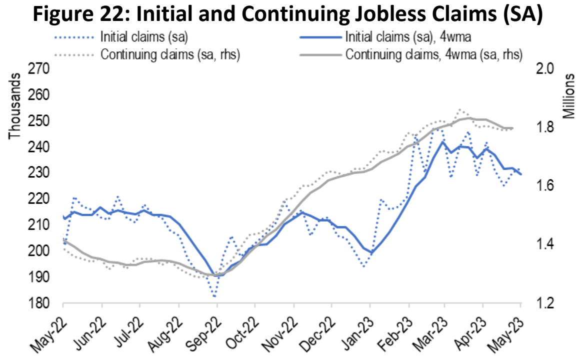


Sources: Bureau of Labor Statistics, Arch MI

JOBLESS CLAIMS SLOWED FURTHER AT THE END OF MAY

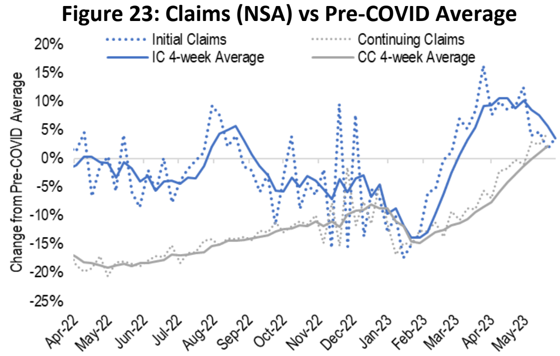
Initial jobless claims rose by 2k to a seasonally adjusted 232k (cons. 235k) during the week ending May 27, moving the four-week average down to 230k from 232k (Figure 22). The non-seasonally adjusted level of initial claims moved up to 4% above its pre-COVID-19 average (i.e., 2018 to 2019) from 2% the week before and up from -17% below in mid-January (Figure 23). Continuing claims for regular state programs (i.e., repeat filers for unemployment insurance) climbed by 6k during the week ending May 20 to a seasonally adjusted 1,795k (cons. 1,800k), moving the four-week average down to 1,798k from 1,799k. Meanwhile, the non-seasonally adjusted level of continuing claims moved up to 4% above its pre-COVID-19 average from 2% the week before and up from -17% below in mid-January. The divergence between the seasonal adjusted data and the non-seasonally adjusted data indicate that some challenges remain with the seasonal adjustment process, even after the most recent update to seasonal factors. Regardless, all indicators suggest the labor market has cooled in 2023 from extremely tight conditions in 2022, but not at an alarming pace through May.

Figure 22: Initial and Continuing Jobless Claims (SA)



Source: U.S. Department of Labor, Arch MI

Figure 23: Claims (NSA) vs Pre-COVID Average



Source: U.S. Department of Labor, Arch MI

The Week Ahead

This week will be light in terms of data releases and unlikely to sway one's view of the economy. After a strong payrolls release, the final May Institute for Supply Management (ISM) and S&P Global US Services PMIs should show the services sector is still expanding, according to the Bloomberg Consensus Survey of Economists. Final April durable goods orders will likely maintain the same theme from the prior few months, mainly that goods production remained weak as firms looked to run leaner operations in the face of elevated economic uncertainty. Jobless claims are expected to tick slightly higher, showcasing a softening labor market but overall to have remained close to historically low levels.

UPCOMING DATA RELEASES

Key economic and housing data releases for the coming week:

Date	Indicator	Period	Actual	Consensus	Previous	Note
6/5/23	S&P Global US Services PMI	May F	--	55.1	55.1	index, sa
6/5/23	S&P Global US Composite PMI	May F	--	54.5	54.5	index, sa
6/5/23	Factory Orders	Apr	--	0.8%	0.4%	m/m, sa
6/5/23	Durable Goods Orders	Apr F	--	1.1%	1.1%	m/m, sa
6/5/23	ISM Services Index	May	--	52.4	51.9	index, nsa
6/7/23	MBA Mortgage Applications	6/2/23	--	--	-3.7%	w/w, sa
6/7/23	Consumer Credit	Apr	--	22.0	26.5	$B, m/m, sa
6/8/23	Initial Jobless Claims	6/3/23	--	237	232	k, sa
6/8/23	Continuing Claims	5/27/23	--	1,802	1,795	k, sa
6/8/23	Wholesale Inventories m/m	Apr F	--	-0.2%	-0.2%	sa

Sources: Bloomberg Consensus Survey of Economists, Arch MI