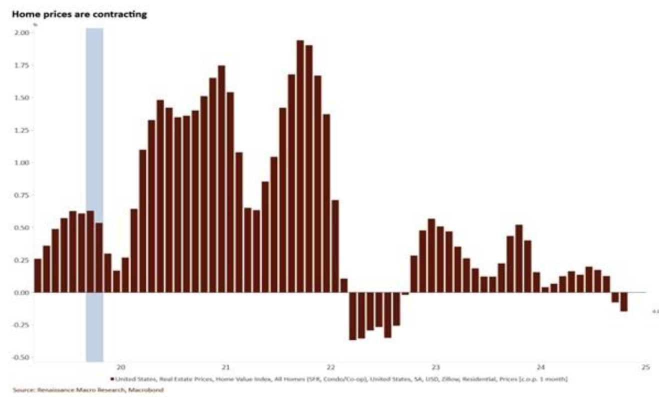
Dutta's Monetary Thoughts

Factories hit the skids

Neil Dutta

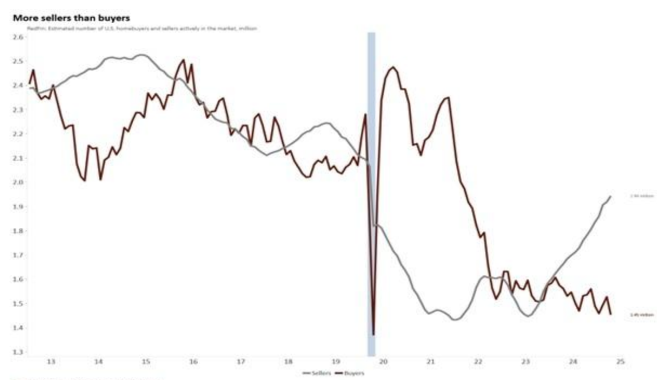
Home prices and labor cooling together

Households are likely to feel worse about their financial positions in the months ahead. Home prices are declining as housing inventories climb, and labor market conditions cool down. This is a bad combination especially considering the Fed's wait and see approach. Put differently, the Fed continues to tolerate a worsening of households' budget constraint.

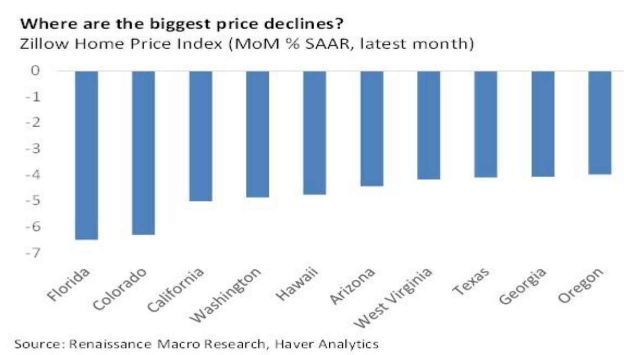


More sellers than buyers in housing

As [Redfin recently reported](), "there are an estimated 1.9 million home sellers in the U.S. housing market and an estimated 1.5 million homebuyers. In other words, there are 33.7% more sellers than buyers (or 490,041 more, to be exact). At no other point in records dating back to 2013 have sellers outnumbered buyers by this large of a number or percentage." Obviously, if there are more sellers than sales, inventories will rise, and prices will fall.

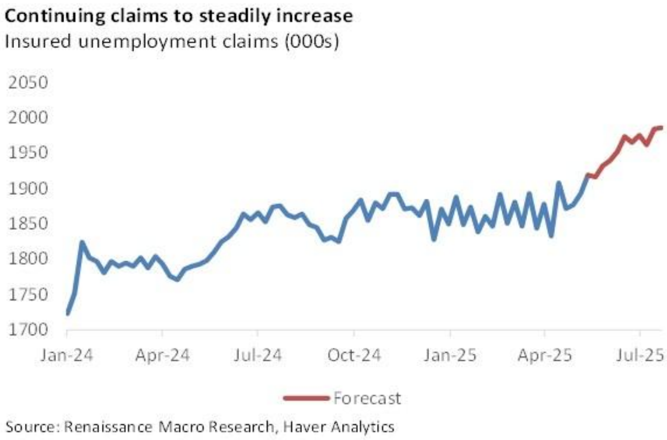


Across the country, the states seeing the biggest declines in prices now are the ones that made the strongest contribution to construction over the last number of years. Where are prices falling most rapidly? Florida, California, Arizona, and Texas, among others. Thus, with prices declining in the places housing has been getting built, it stands to reason that construction is likely to decline going forward. Indeed, the ten states with the steepest price declines represent about half the construction in the US.

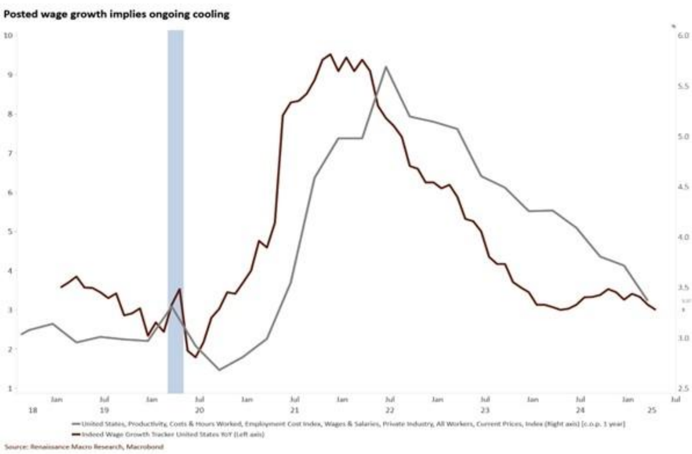


Labor market is slacking

Meanwhile, the labor markets are continuing to cool off. There are several data-points that have captured our attention even if the most obvious – nonfarm payrolls – has yet to crack. Here are the indicators we have been following.

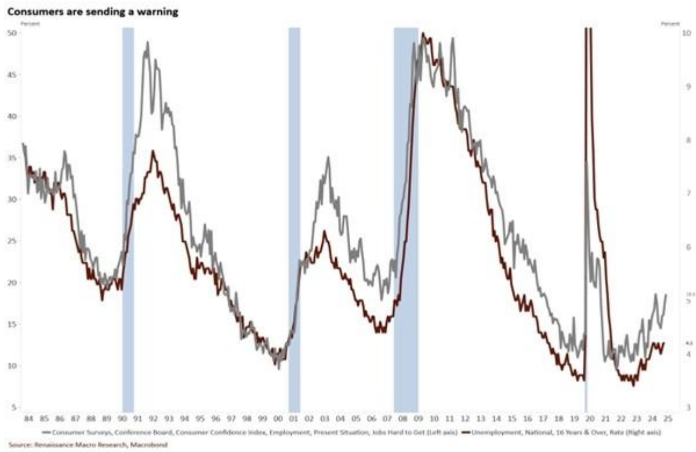


- Continuing unemployment claims have been rising roughly four to five percent against last year consistently for the last 12 months. Perhaps there is a residual seasonality issue at work. Still, if we push this forward, it means continuing claims will be close to two million by the end of July.



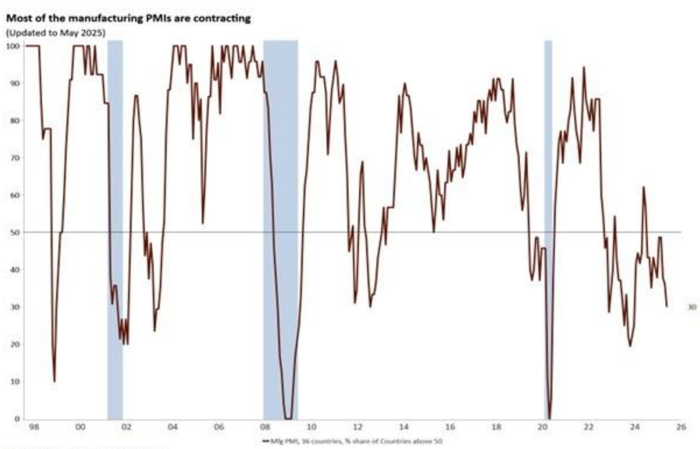
- The increasing slack in the labor market has put downward pressure on posted wage growth. The latest data from Indeed show posted wage growth rising just three percent against last year; this tends to move ahead of more widely followed metrics like the Employment Cost Index.

- Cyclical parts of the labor market – goods-producing industries and cyclical services – have been cooling more rapidly than acyclical parts of the labor market such as healthcare and education. This would not be happening if underlying growth was strong.



- Consumers are telling us labor market conditions are getting worse with more noting that "jobs hard to get." Historically, this measure tends to have a strong contemporaneous relationship with the unemployment rate.

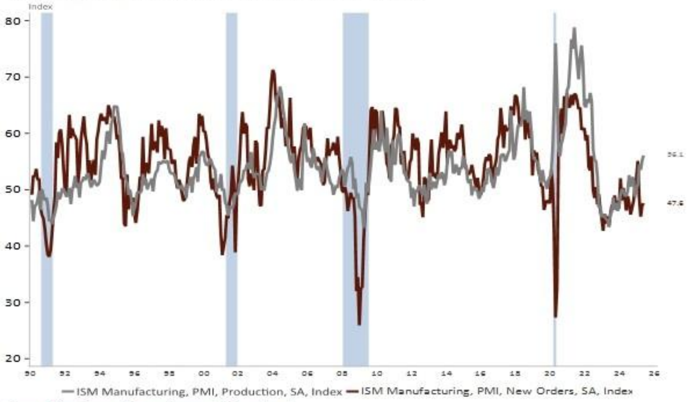
As our nearby figure shows, it is unusual to see home prices declining and continuing claims rising at the same time. However, this is exactly where the US economy is right now. The main asset on the household balance sheet – their home – is deflating while the primary source of cash flow – the jobs market – is seeing increasing slack. Cuts last year have not really changed this dynamic. Indeed, it has gotten worse since the 100bp decline in the federal funds rate. Not good



Sluggish factories

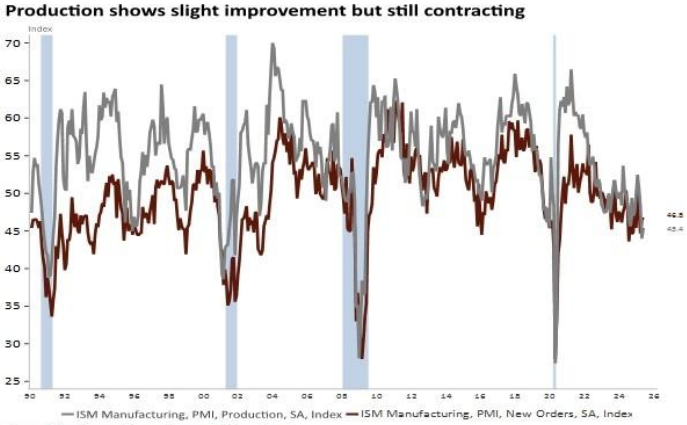
Manufacturing activity continues to deteriorate globally. By our count, just 31 percent of the manufacturing PMIs released are in expansion territory, the lowest since December 2023. The weakness is centered in Asia with South Korea, Vietnam, Taiwan and Japan all running below breakeven. China's Caixin Manufacturing PMI is released later tonight though the official PMI stood below 50 in May. In Europe, we see more of the same: conditions in the core – France and Germany – remain softer than the periphery – Spain and Greece. Stepping back, manufacturing is highly tradeable, and a trade war threatens to upend global supply chains in several critical sectors; that will take time to sort out.

Tariff-driven re-routing impacts delivery times



Source: Renaissance Macro Research, Macrobond

Production shows slight improvement but still contracting



Source: Renaissance Macro Research, Macrobond

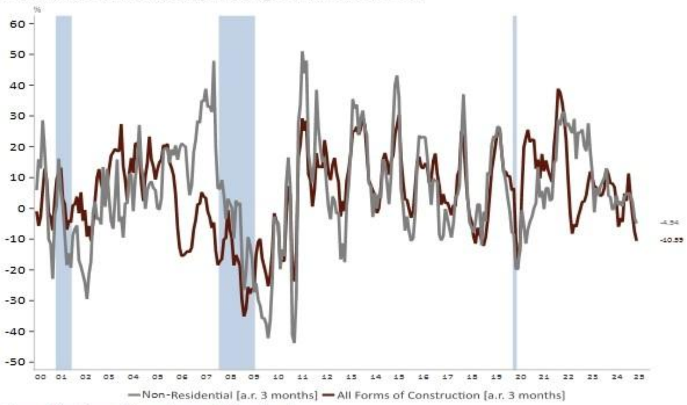
Putting the ISM in PessimISM

- The ISM Manufacturing PMI unexpectedly slid 0.2pts to 48.5 in May. The only metric really holding up ISM was supplier deliveries, which rose to 56.1, the highest since June 2022. Normally, lengthening delivery times are seen as a source of upward demand pressure; factories have so much trouble keeping up with demand that it takes longer to move products out of factories. However, I'd take the rise in delivery times as a reflection of the challenges factories face as supply chains are re-routed due to tariffs.

- The May ISM data paints a mixed picture of the manufacturing sector, with some signs of stabilization alongside persistent weakness, particularly in exports. While overall demand remains sluggish, the new orders index ticked up slightly to 47.6 in May, from 47.2 in April. However, export orders tumbled further, falling to 40.1 from 43.1 in April, highlighting continued challenges for manufacturers reliant on international trade. This decline in export orders is notable, especially considering the ongoing weakness in the broad dollar exchange rate. Meanwhile, the production index also saw a slight rebound, rising to 45.4 from April's low of 44.0. While this improvement is welcome, the index remains at a depressed level. This slight uptick in production is mirrored by a similarly small rise in the employment index, which edged up to 46.8 from 46.5.

- Looking through respondent commentary, it is no surprise that tariffs and the related economic certainty remain front and center on the minds of purchasing managers. Government spending cuts also got a shout. Interestingly, despite the noise around tariffs, the prices index dipped to 69.4 in May, down 0.4 percentage points from April's 69.8.

Private construction spending continues to fall



Source: Renaissance Macro Research, Macrobond

Construction spending continues to contract

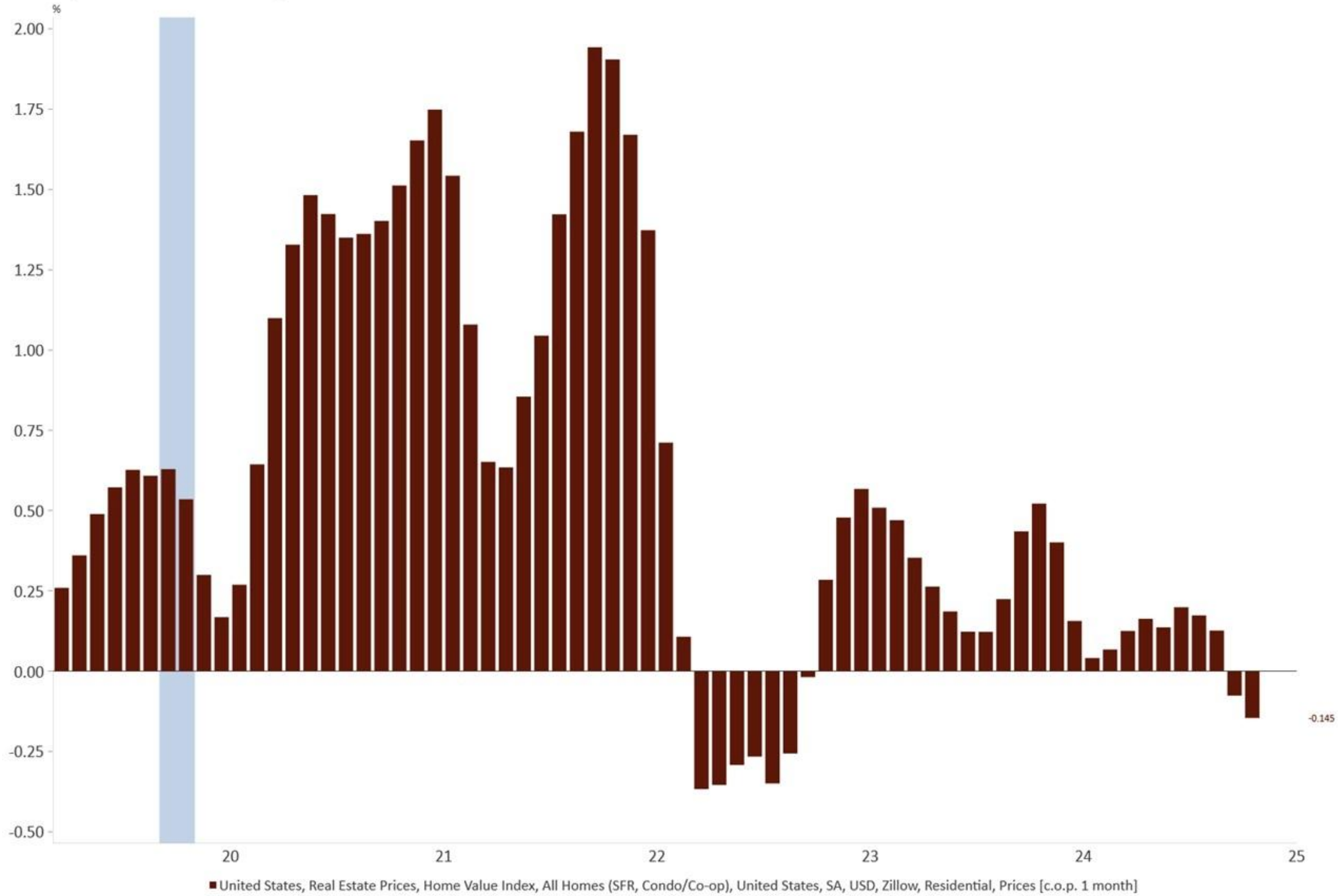
- In April, total construction spending declined 0.4% following a 0.8% decline in March. Private construction spending slid 0.7%, the third consecutive decline; over this three-month period, private construction spending has declined 10.6% annualized. Non-residential private construction has dropped roughly 5% at an annual rate over the last three months as gains from data-centers and manufacturing structures have flattened out. With private construction spending declining, I have a tough time seeing why construction payrolls continue to hold up.

Great speech from Governor Waller on the outlook

- In a recent speech, Governor Waller addressed the impact of tariffs on inflation and inflation expectations. Key excerpt for me, “Given labor market conditions, it seems hard to believe that the high inflation expectations we are seeing in consumer surveys will lead to large nominal wage increases and a secondround burst of inflation.” I think that is spot on. Workers are not in a position of leverage in the labor market right now.

- Unlike others, Waller sounds like someone that has a coherent intellectual view for monetary policy. When thinking about who to nominate in Powell’s stead, President Trump give current Governor Waller serious consideration!

Home prices are contracting



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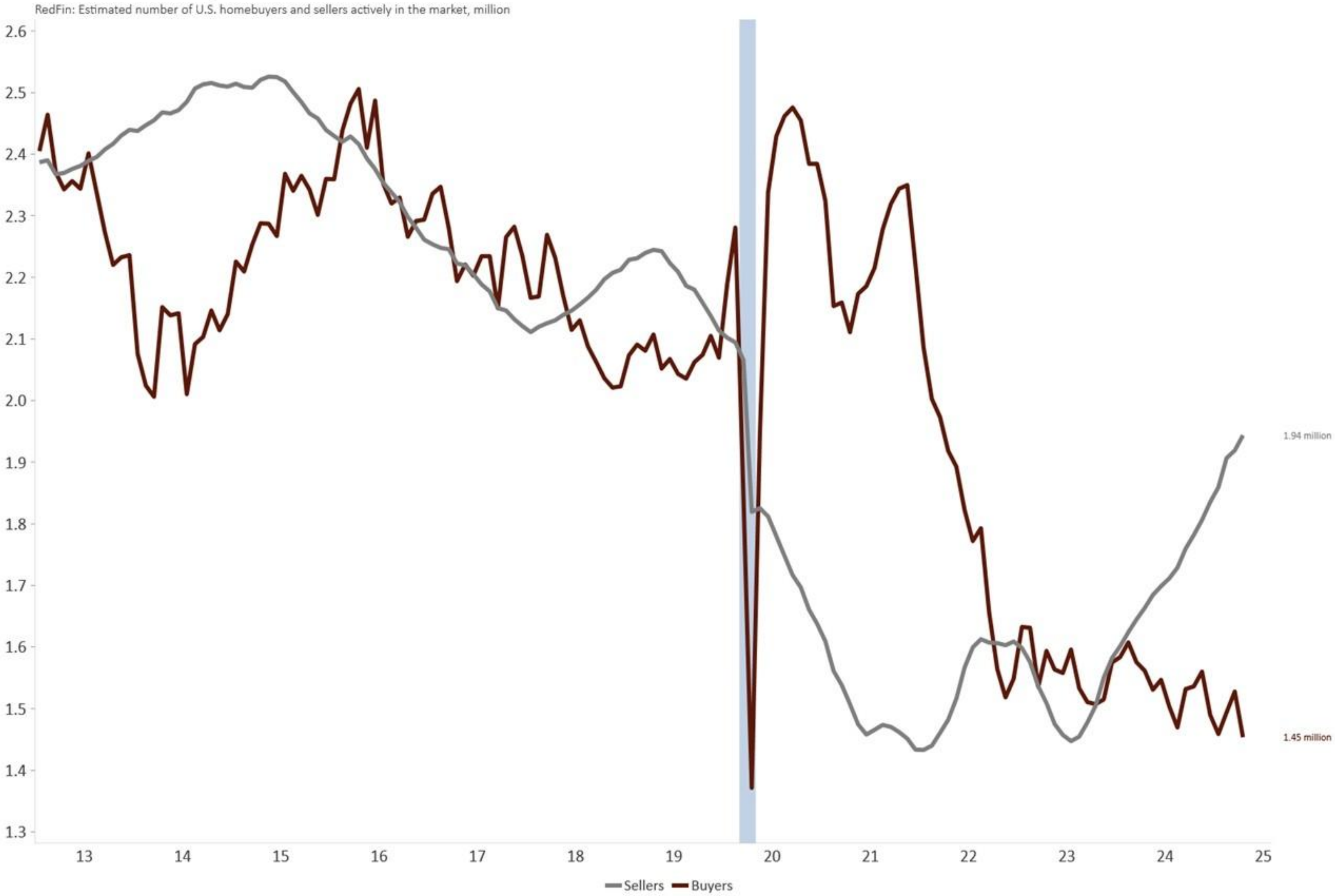
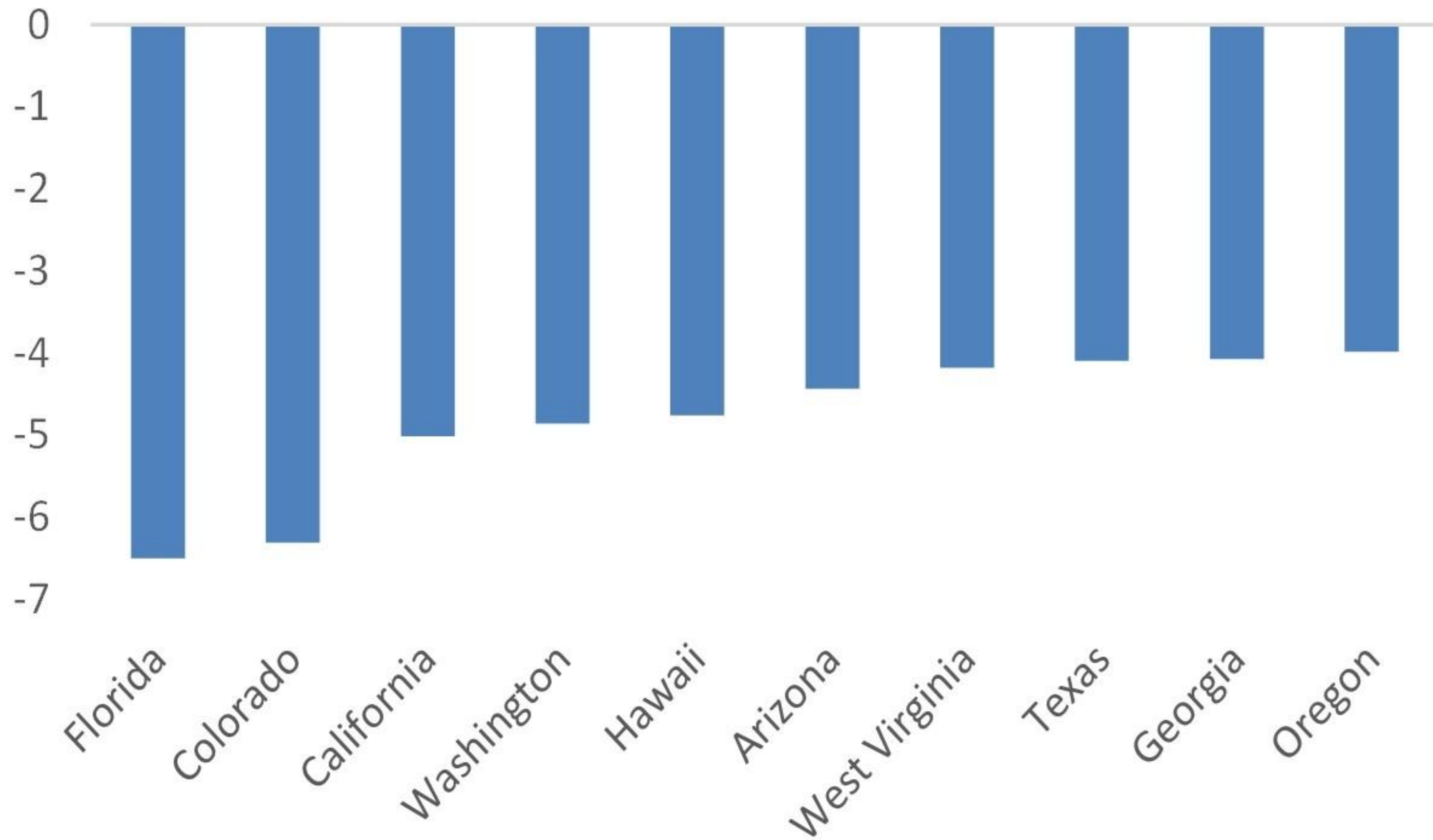
More sellers than buyers



Source: Renaissance Macro Research, Macrobond

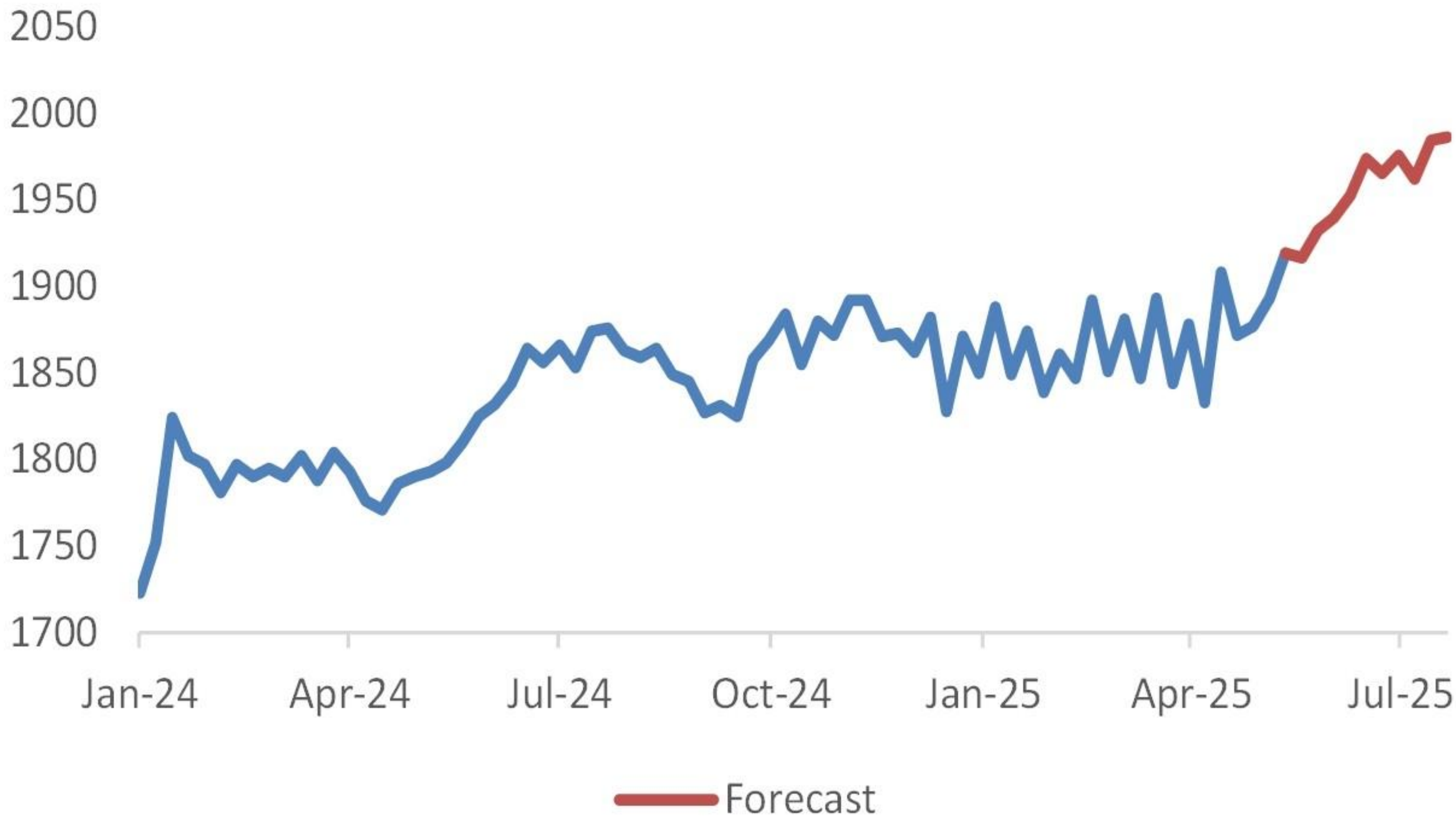
Where are the biggest price declines?
Zillow Home Price Index (MoM % SAAR, latest month)



Source: Renaissance Macro Research, Haver Analytics

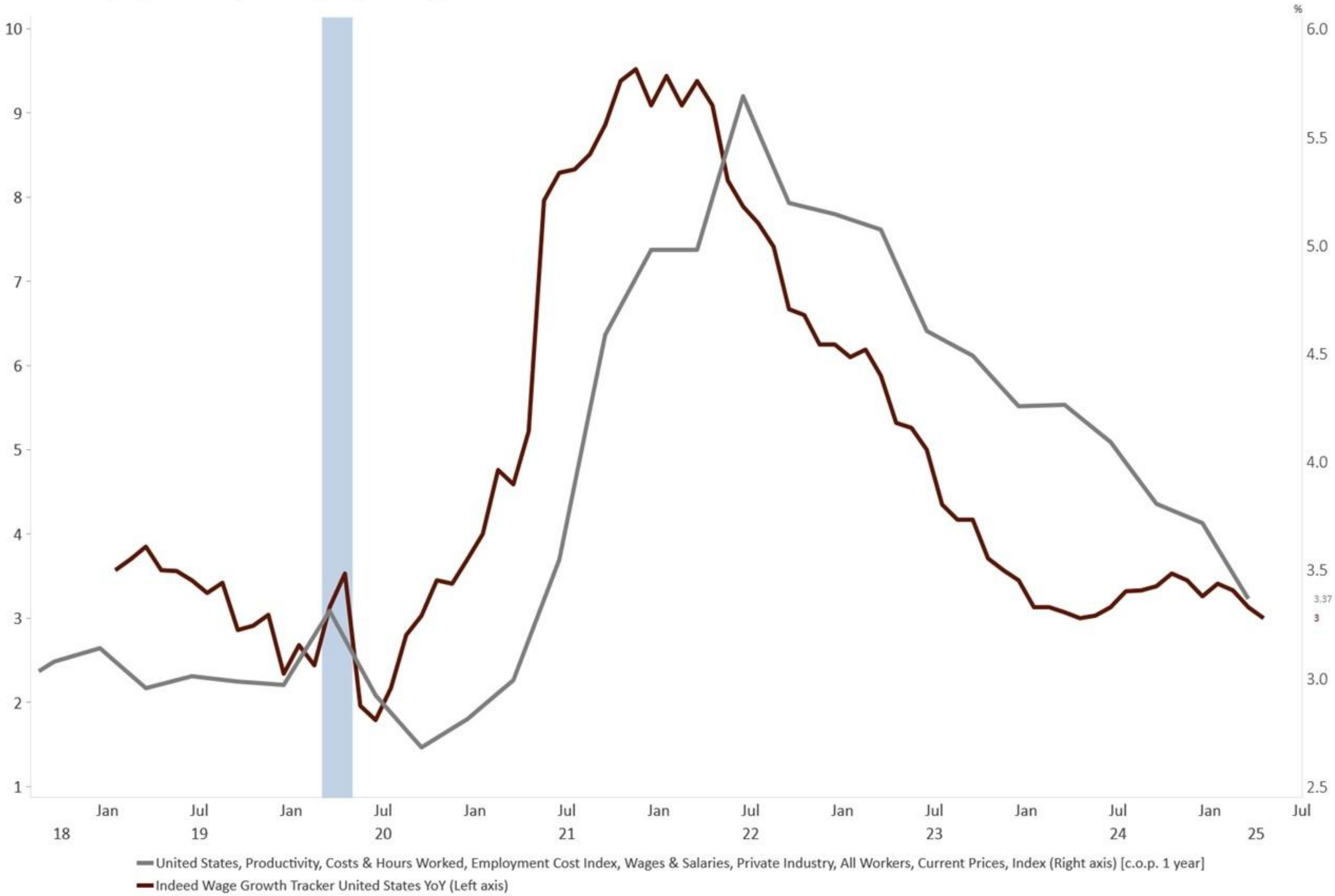
Continuing claims to steadily increase

Insured unemployment claims (000s)



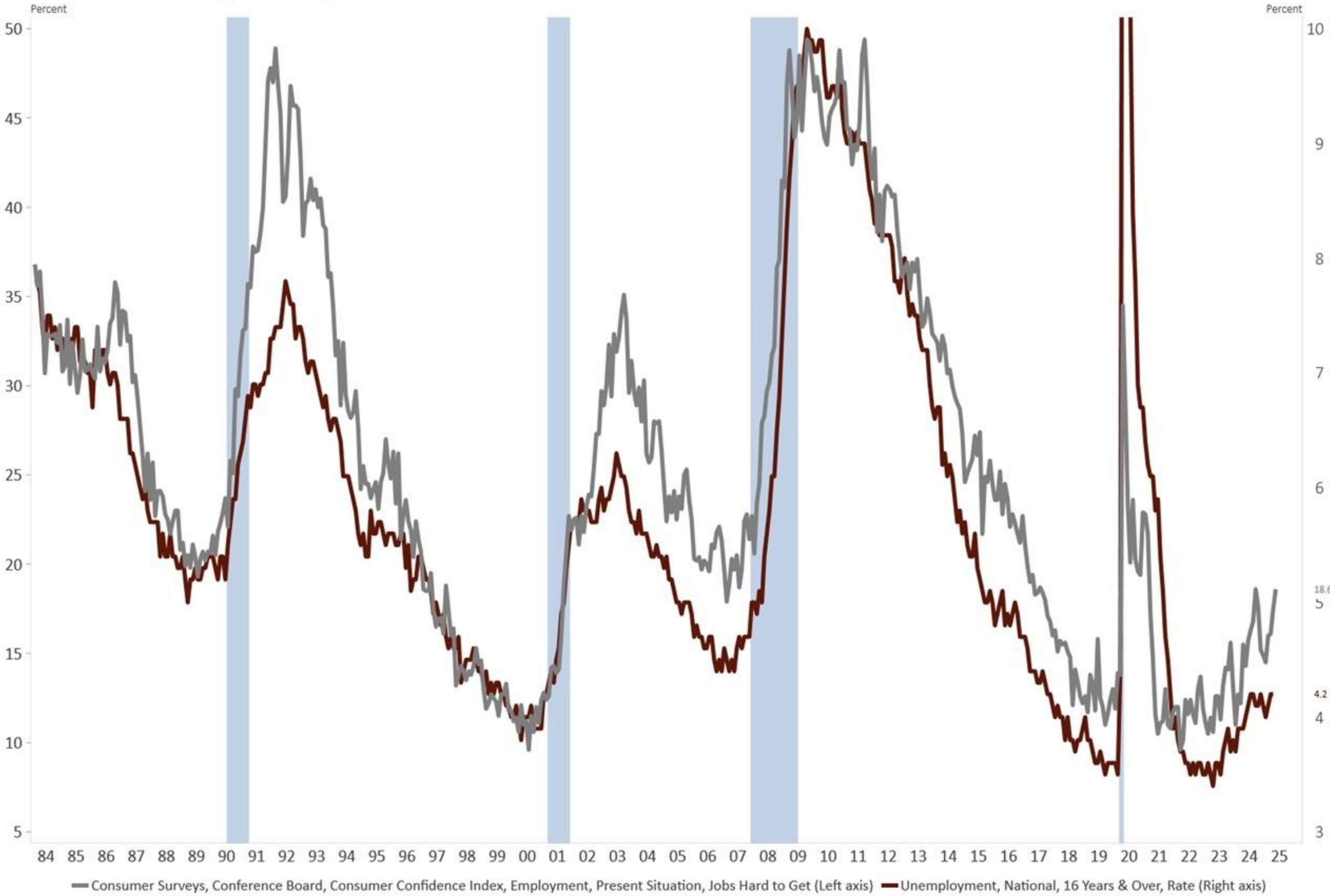
Source: Renaissance Macro Research, Haver Analytics

Posted wage growth implies ongoing cooling



Source: Renaissance Macro Research, Macrobond

Consumers are sending a warning



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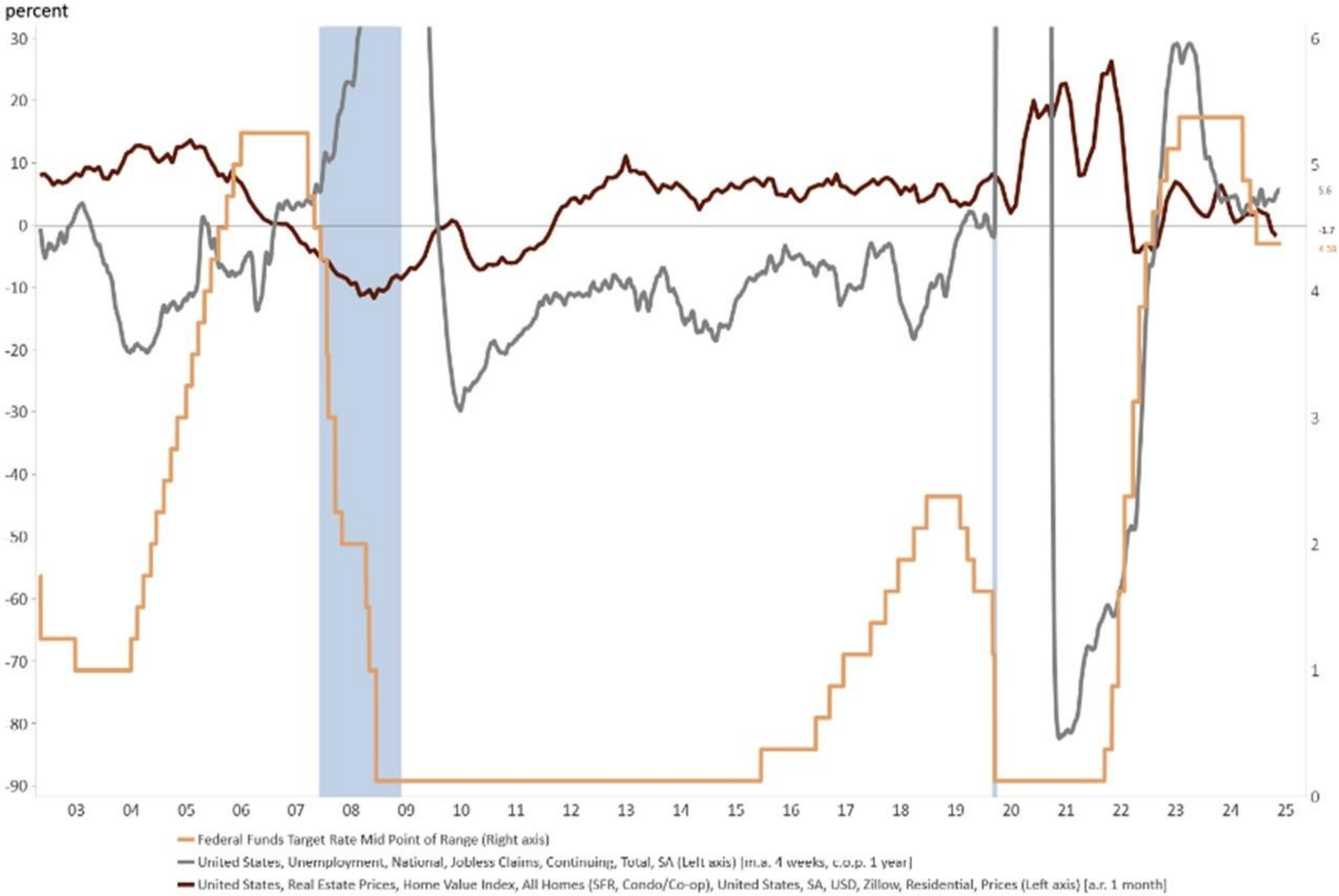
It's usually not good when home prices are down and continuing claims are rising



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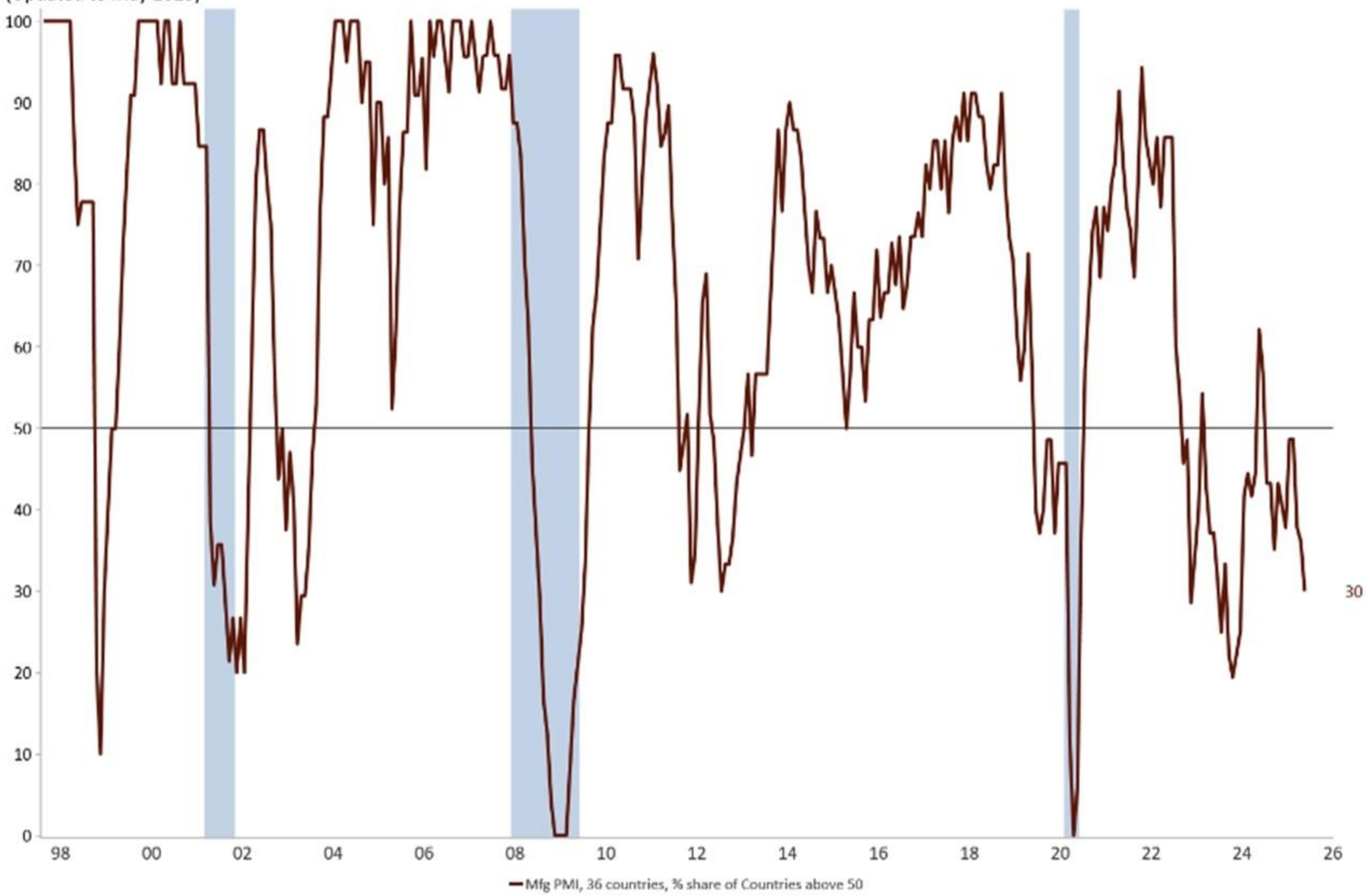
Most of the manufacturing PMIs are contracting

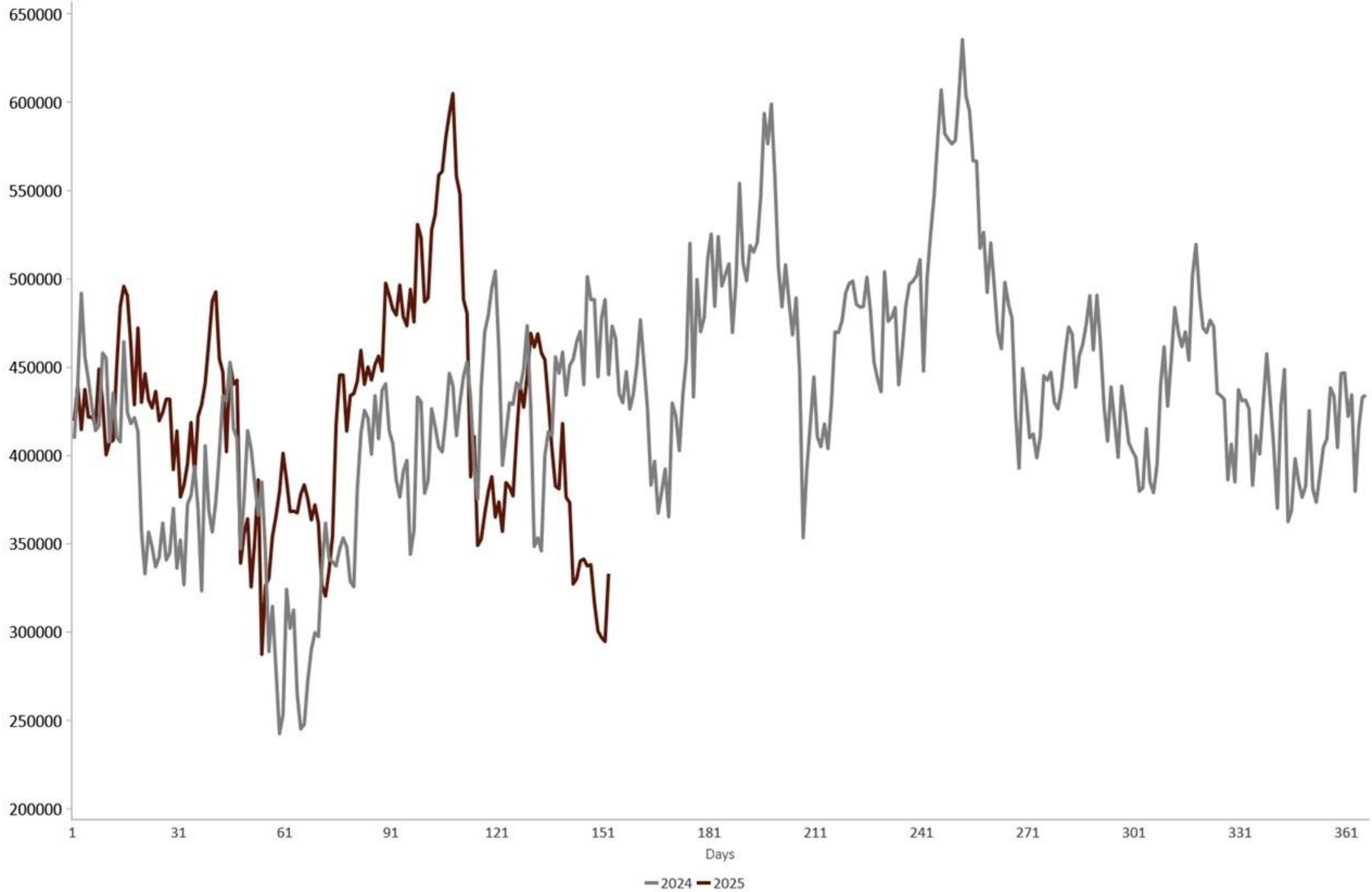
(Updated to May 2025)



Source: Renaissance Macro Research, Macrobond

Ship counts from China down

Container Ship Tonnage (TEU) - Departures from China to the United States



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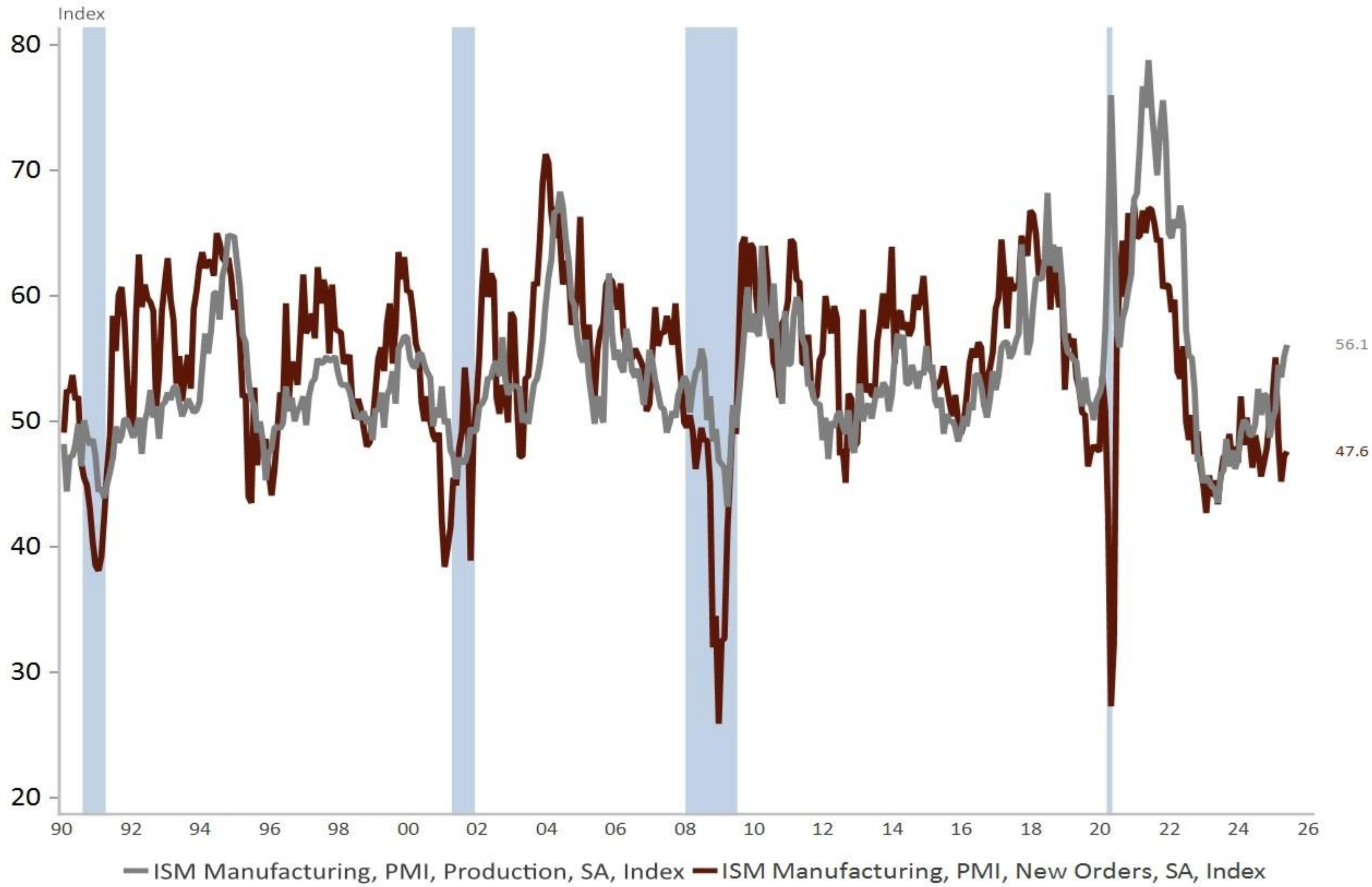
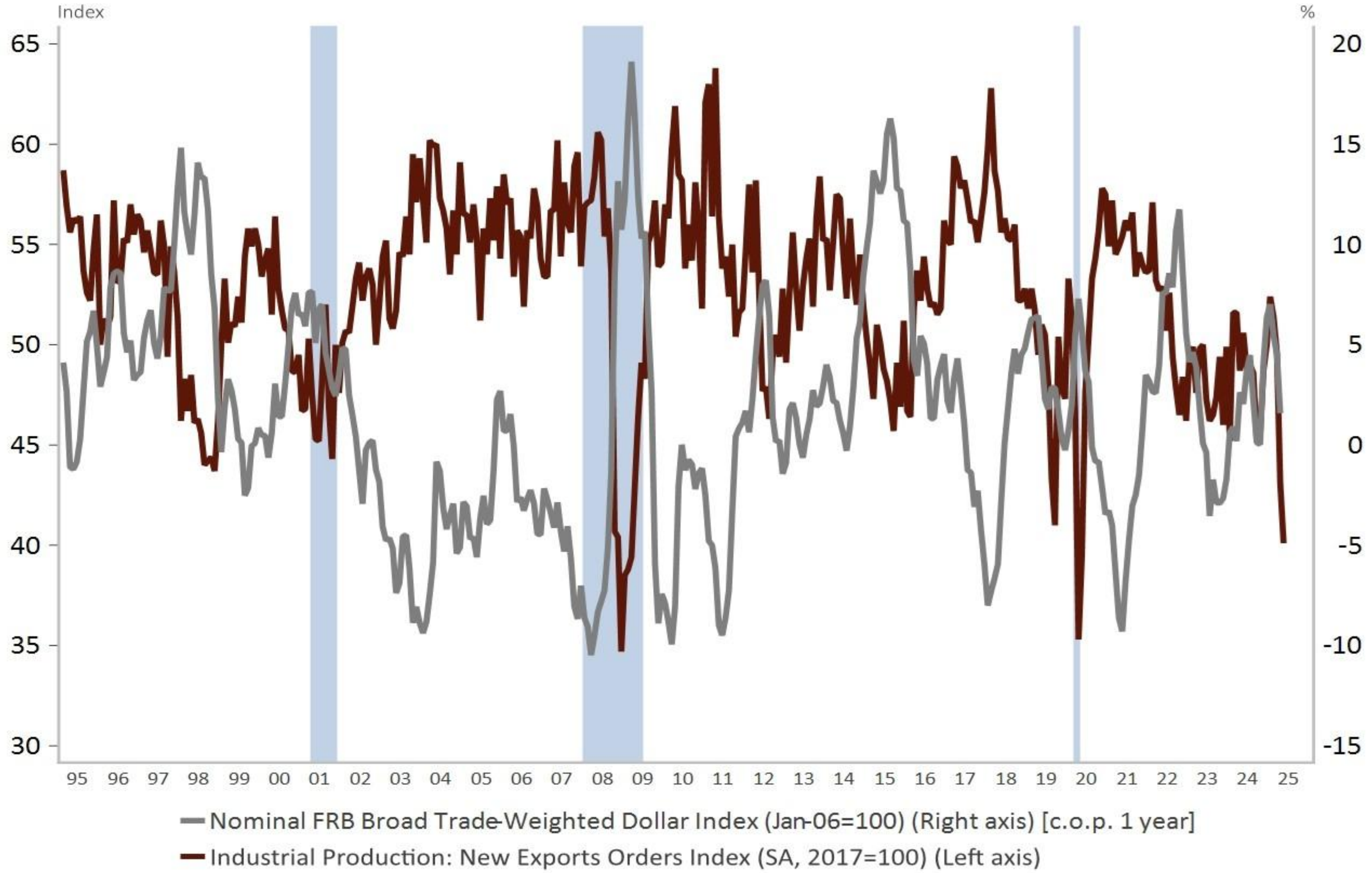


Source: Renaissance Macro Research, Macrobond

Weak dollar fails to boost export orders



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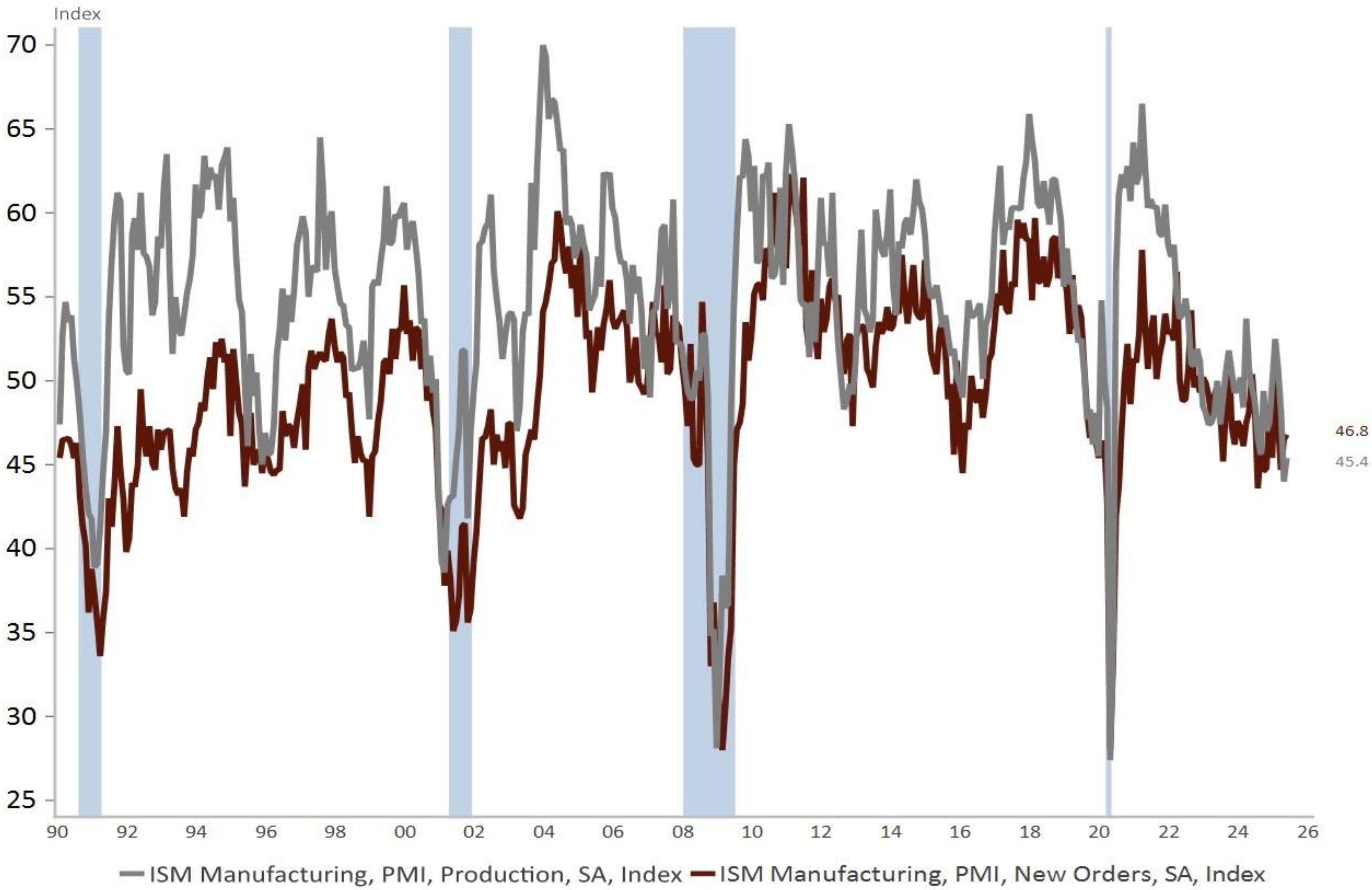

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WHAT RESPONDENTS ARE SAYING

- "There is continued softening of demand in the commercial vehicle market, primarily related to higher prices and economic uncertainty. The impact of ever-changing trade policies of the current administration has wreaked havoc on suppliers' ability to react and remain profitable. Vehicle manufacturers have already rolled price increases into their products to protect their bottom lines but have not been as cooperative with their supply bases. This has resulted in a high occurrence of suppliers falling into financial distress." [Transportation Equipment]
- "Tariffs, avian influenza and broader commodity markets continue to impact business conditions. The volatility of all three makes business planning and overall conditions challenging." [Food, Beverage & Tobacco Products]
- "Government spending cuts or delays, as well as tariffs, are raising hell with businesses. No one is willing to take on inventory risk." [Computer & Electronic Products]
- "Most suppliers are passing through tariffs at full value to us. The position being communicated is that the supplier considers it a tax, and taxes always get passed through to the customer. Very few are absorbing any portion of the tariffs." [Chemical Products]
- "Tariff uncertainty is impacting new international orders. Tariffs are also the main reason our Asia customers are requesting delayed shipments." [Fabricated Metal Products]
- "There is continued uncertainty regarding market reaction to the recently imposed tariffs and resulting actions by other countries. The rare earth restrictions being imposed are of high concern in the near term." [Machinery]
- "The administration's tariffs alone have created supply chain disruptions rivaling that of COVID-19." [Electrical Equipment, Appliances & Components]
- "We have entered the waiting portion of the wait and see, it seems. Business activity is slower and smaller this month. Chaos does not bode well for anyone, especially when it impacts pricing." [Primary Metals]
- "Tariff whiplash continues while the easing of tariff rates between the U.S. and China in May was welcome news, the question is what happens in 90 days. We are doing extensive work to make contingency plans, which is hugely distracting from strategic work, plus it is also very hard to know what plans we should actually implement. The 10-percent tariff on other countries is impactful as well, and it is unclear if/when deals will be made." [Miscellaneous Manufacturing]
- "Uncertainty due to the recent tariffs continue to weigh on profitability and service. An unresolved (trade deal with) China will result in empty shelves at retail for many do-it-yourself and professional goods." [Paper Products]

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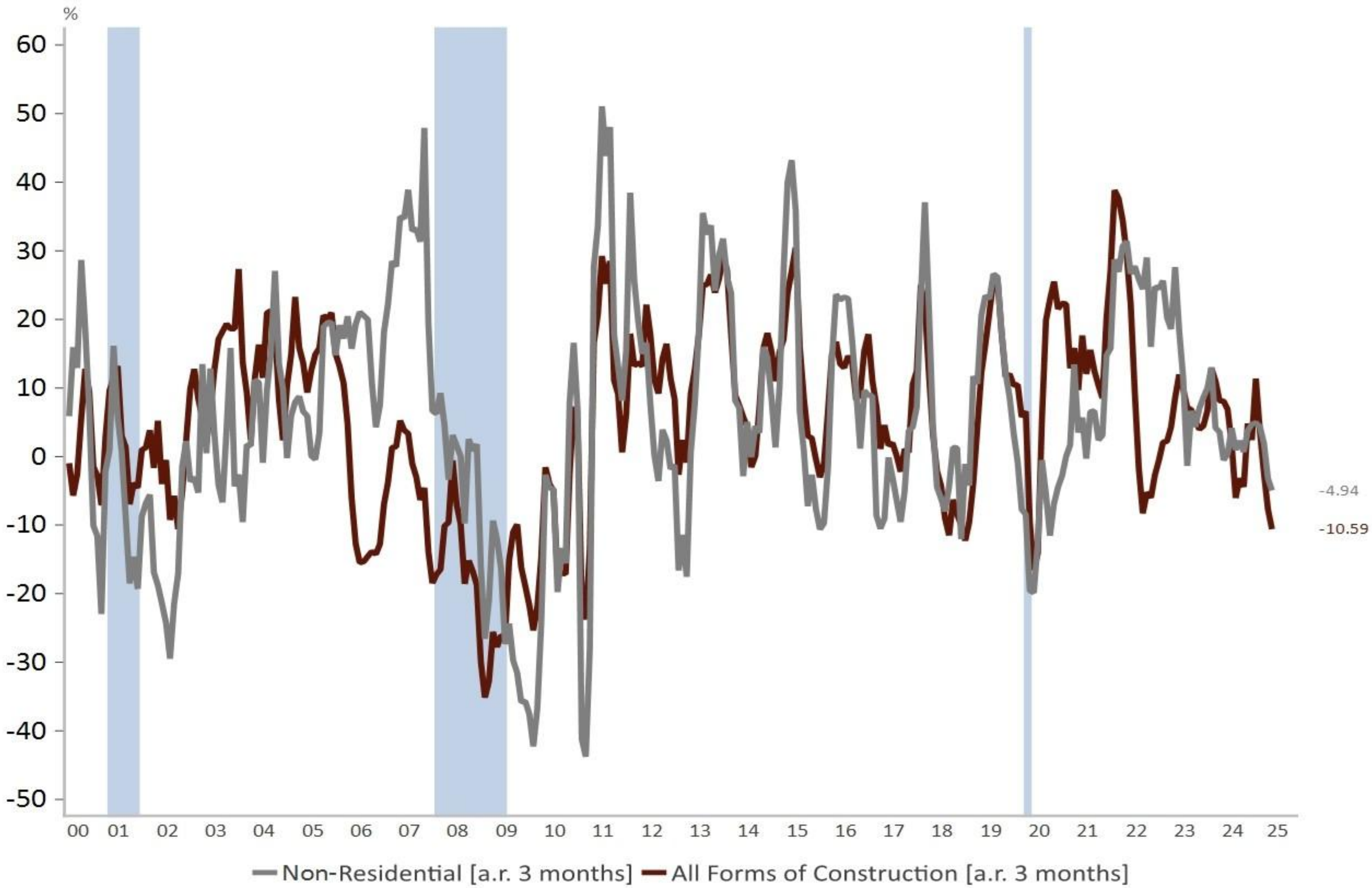

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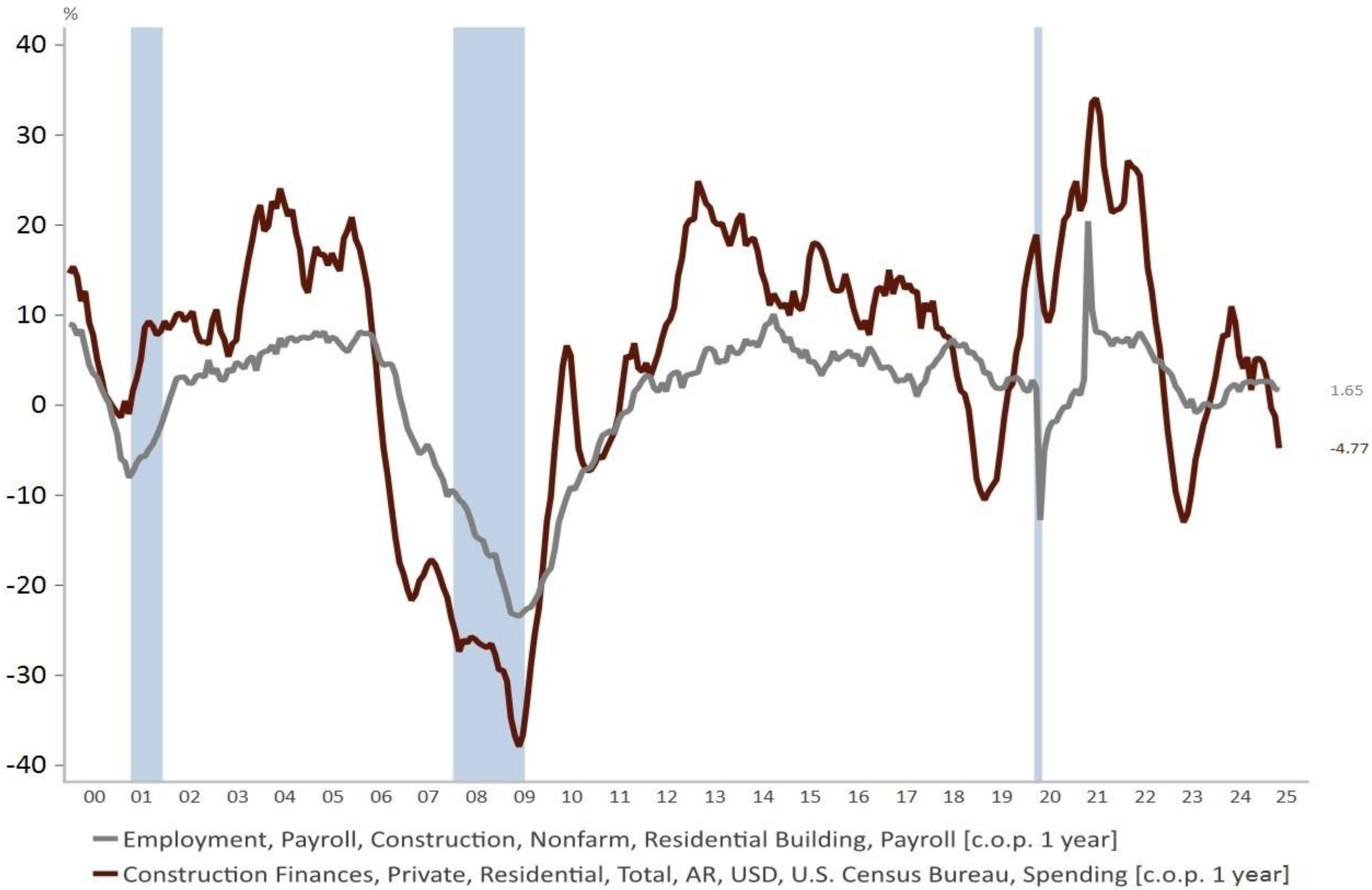
Construction employment weakness expected



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