Economic Research
03/08/2016

United States

Economic growth stays subdued in July but solid job gains continue

- **PMI surveys point to ongoing 1% annualised GDP growth in Q3**
- **Employment rising at rate of 160k per month in July**
- **Mix of weak growth and solid hiring bodes ill for productivity**

Those looking for signs of the US economy moving up a gear in the third quarter will be disappointed by the PMI readings for July.

The final seasonally adjusted Markit US Composite PMI™ Output Index posted 51.8 in July, up slightly from the earlier 'flash' figure (51.5).

The final reading was above that seen in June (51.2) and signalled the fastest expansion of private sector output since April. However, the latest growth rate was still much weaker than the average since the survey began in late-2009.

As such, the surveys are indicating that the pace of economic growth has held at around 1% at the start of the third quarter, largely unchanged on the signals sent by PMIs for the first and second quarters of 2016.

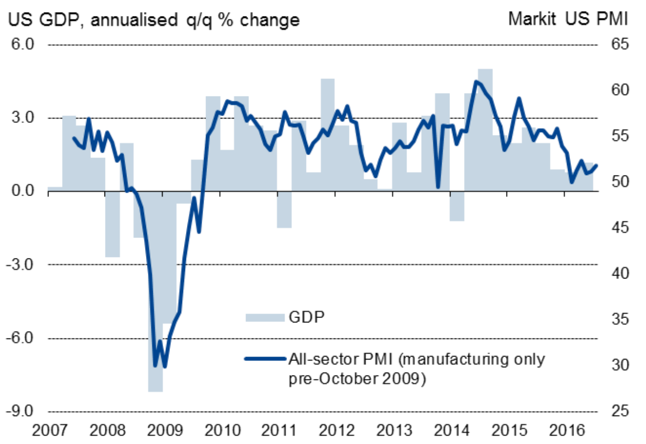
Beating the consensus

The latest PMI should be taken seriously as the surveys have markedly outperformed the consensus this year in predicting GDP. Over the first half of the year, GDP numbers have come in well below consensus expectations, but for both quarters the PMI surveys provided an accurate advance guide to actual GDP growth rates.

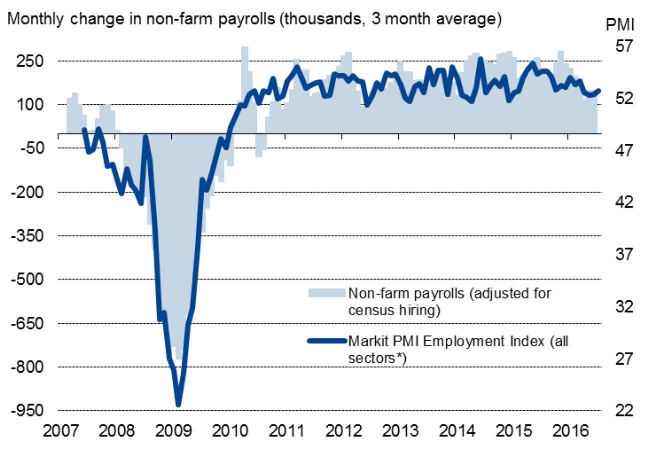
Back in February the surveys were signalling a near-stalling of first quarter GDP, upgraded to a signal of 0.7% once the March PMI became available. The current official estimate of first quarter growth is 0.8%. Note that right up until mid-April, the consensus was for 2% first quarter GDP growth.

More recently, throughout the second quarter, the PMIs were correctly indicating that growth was showing no significant signs of a widely-anticipated rebound from this further quarter weakness, pointing to growth of around 1%. The initial official estimate of second quarter growth is just 1.2%, disappointing market expectations of a 2.6% rise.

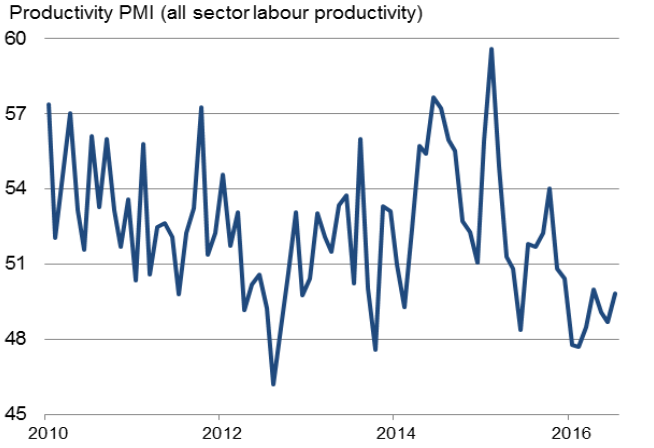
Economic growth and the PMI



Employment and the PMI



Productivity growth implied by the PMI



Sources: IHS Markit, Eurostat.

Solid payroll growth

Once again, there was better news on hiring, with the overall rate of job creation edging up in July to the highest since January.

As with GDP, the surveys provide an accurate advance guide to the underlying trend in official data, exhibiting a close correlation with non-farm payroll numbers (especially once the high volatility of the official data is smoothed out).

A simple regression-based model suggests that the July surveys are broadly consistent with non-farm payrolls rising by 160,000 July.

Hiring is holding up in part because of signs that the soft patch that the economy has gone through may prove temporary. Inflows of new business across the economy rose at the fastest rate seen so far this year in July, and backlogs of work were pushed higher for the first time since last October as a result.

Business confidence about the outlook is also improving, rising in the service sector to the highest since January.

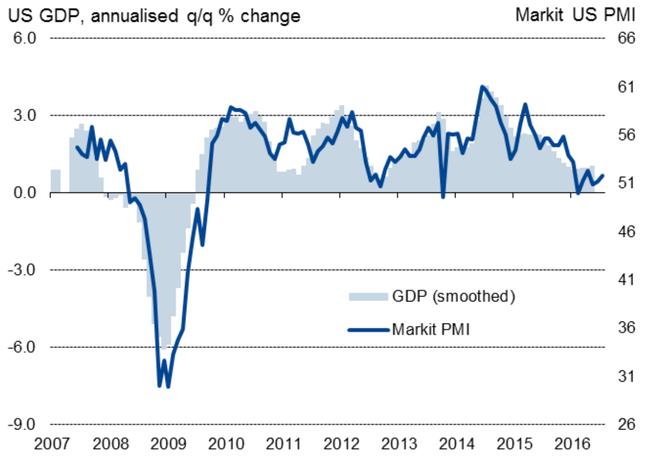
Productivity hit

The downside of such solid employment growth at a time when the economy is expanding at a lacklustre pace is of course the impact on productivity. A quick comparison of the PMI output and employment trends across both manufacturing and services indicates that output per head has been falling in each month so far this year with the exception of a stagnation seen in April. That represents the worst period of productivity seen since this side of the global financial crisis.

2016 rate hike still on the table

These survey results add to the sense that policy makers will be encouraged by the resilience of the labour market in particular, but will want to see signs of stronger economic growth before hiking interest rates again. Another rate hike by the end of the year therefore still looks a strong possibility, though with odds of the timing of that hike skewed heavily towards December.

PMI v smoothed GDP*



* smoothing uses a centered moving average.
Sources: IHS Markit, Eurostat.

Chris Williamson

Chief Economist, Markit
Tel: +44 207 260 2329
Email: chris.williamson@ihsmarkit.com

Click here for more PMI and economic commentary.
For further information, please visit www.markit.com