FEDERAL RESERVE BANK OF BOSTON™

The

President's Report *to the* Board *of* Directors

July 13, 2021

CURRENT ECONOMIC DEVELOPMENTS - July 13, 2021

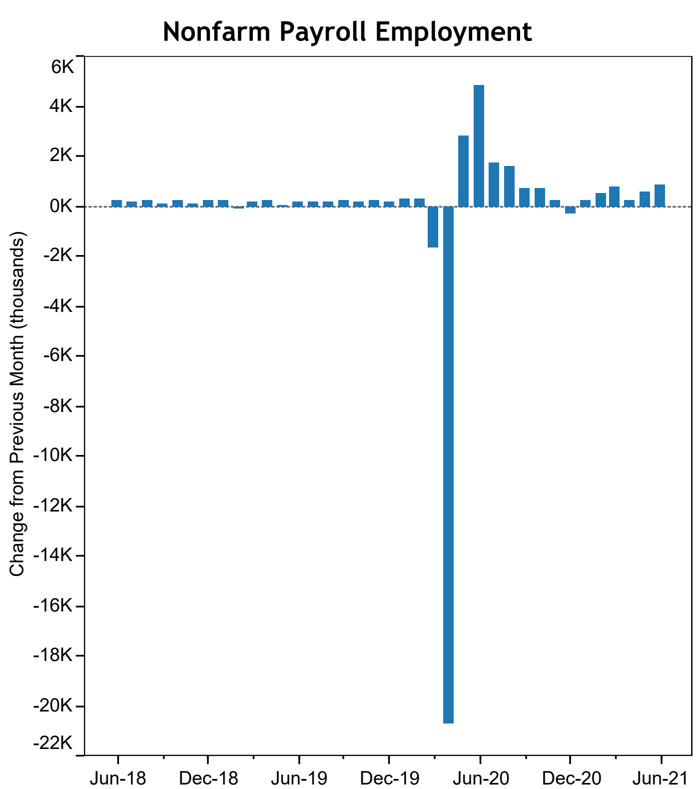
Data released since your last Director's meeting suggest improving economic and public health conditions will support continued strong growth through the second half of the year. With nearly 60% of the adult population having been vaccinated and coronavirus cases remaining low, consumers seem increasingly comfortable resuming normal activity. Downside risks remain from supply chain issues, worker shortages, and increasing price pressures - however, each of these headwinds are expected to moderate over the months ahead.

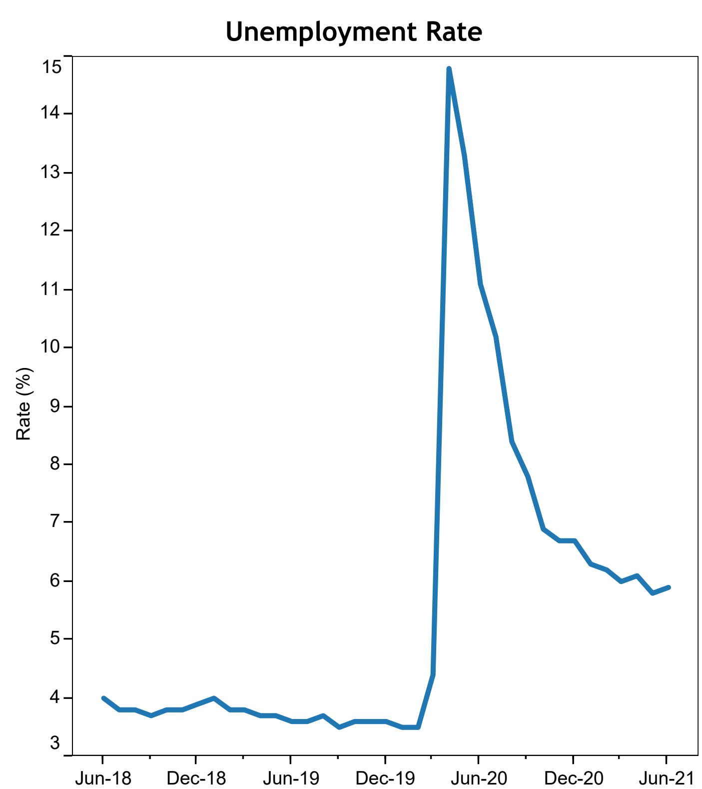
The June employment report showed that nonfarm payrolls rose by 850,000 jobs as the prior two months of data were revised higher, on net. However, a decline in civilian employment in the Household Survey caused the unemployment rate to tick up from 5.8% to 5.9%. Initial claims for unemployment insurance were little changed last week, but with extended benefits expiring in many states and employers struggling to fill positions, claims are likely to decline in the coming weeks. Consumer attitudes improved in June. However, while the consumer confidence index has attained a near-full recovery, the sentiment index remains below its pre-pandemic levels. Retail sales, real disposable income, and real consumption all posted declines in May data while June data for lightweight vehicle sales also softened.

Indicators of housing market activity remained elevated but have generally been slowing in recent months. New and existing home sales both declined further in May, as did building permits. Housing starts did rebound a bit in May but might reverse course in the coming months due to the recent declines in permits. Industrial production grew more than expected in May but remained below pre-pandemic levels. Orders for durable goods as well as orders of nondefense capital goods excluding aircraft continued as signs of strength and grew on a monthly and year-over-year basis. The ISM activity indices remained elevated in June though declined due largely to decreases in the employment components. Regional surveys from the Federal Reserve were mixed but also remained at elevated levels as well as in expansionary territory.

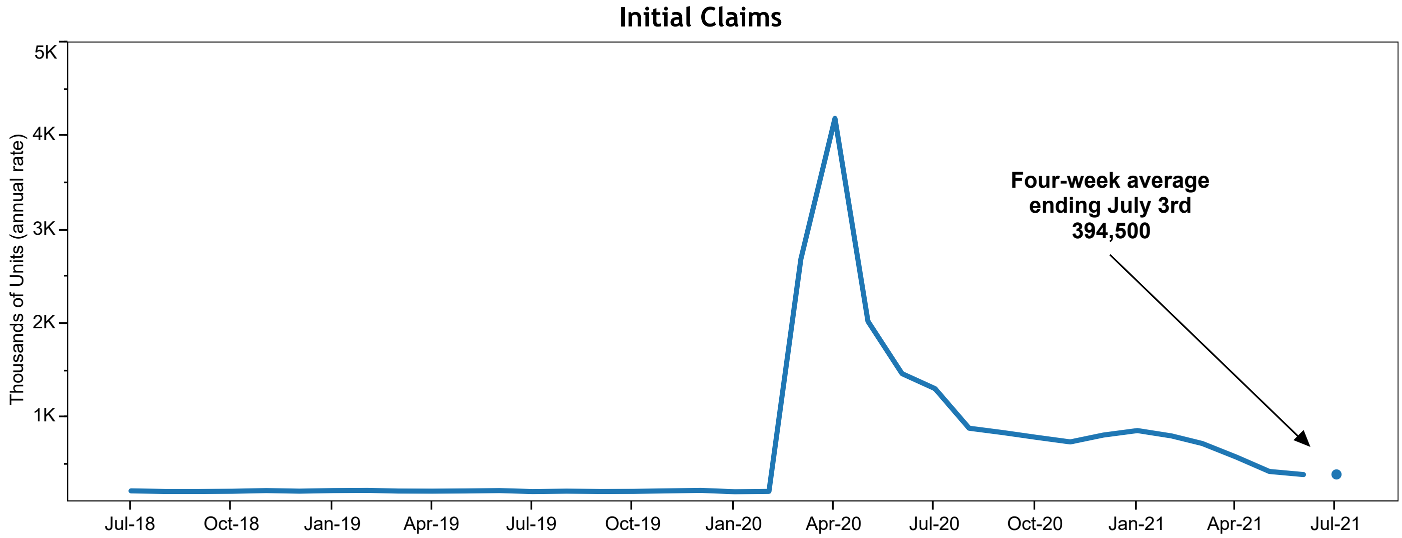
Inflation measures continued to accelerate in June, with both the total and core CPI growing at their fastest 12-month rates in 13 years. The gains were driven largely by higher costs for new and used vehicles, along with food and gasoline. PCE inflation also accelerated in May, with June data due at the end of the month. On average, oil prices have continued their steady rise, hovering close to $75 per barrel in recent daily data.

Nonfarm payroll employment added 850,000 jobs in June and revisions to April and May data resulted in a net increase of 15,000 more jobs than were previously reported. The June increases were driven by gains in the leisure, hospitality, and public and private education sectors. Unexpectedly, the unemployment rate ticked up from 5.8% to 5.9%, reflecting a decline in civilian employment (in the Household Survey) as the labor force participation rate remained flat.

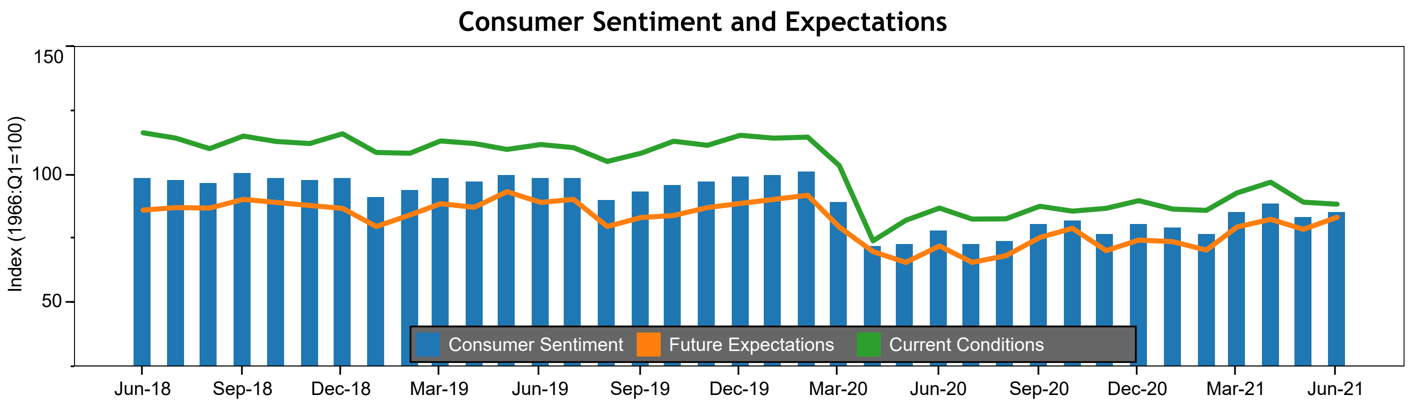


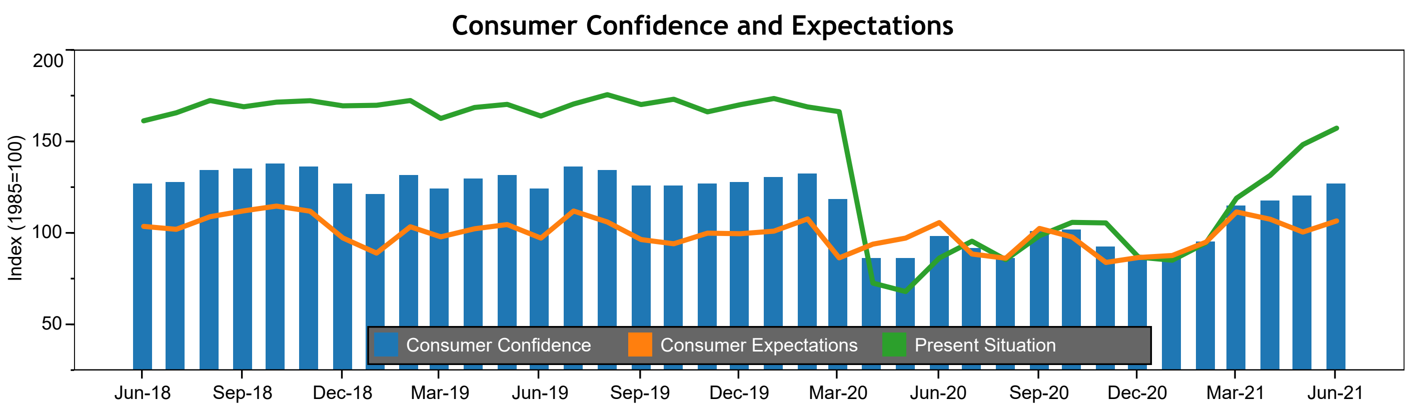


Initial claims for unemployment insurance rose by 2,000 to 373,000 last week and the four-week moving average was essentially unchanged at 394,500. Nearly half of US states have opted-out of extended federal benefits programs associated with pandemic relief – claims are likely to decline in the months ahead.



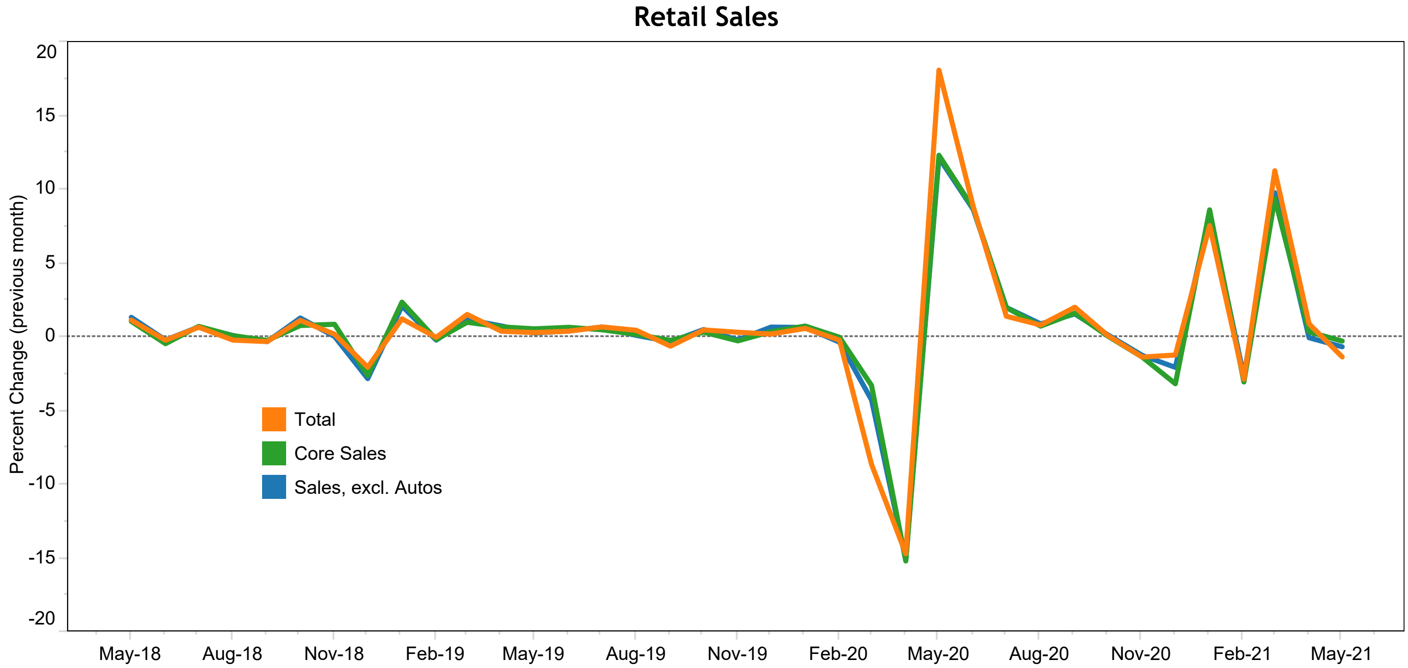
The consumer confidence index rose to 127.3 in June and May's reading was revised further upward. The latest reading was just short of the index's 2019 average - suggesting the recovery in consumer confidence is nearly complete. In June, both the present situation and the expectations subcomponents improved – to 157.7 and 107.0, respectively. The consumer sentiment index rose to 85.5 in June, improving from May and registering the second-highest reading since the start of the pandemic. However, unlike the confidence index, sentiment remains well-below its pre-pandemic levels. The current conditions subcomponent fell from the previous month to 88.6 while the expectations subcomponent rose to 83.5.



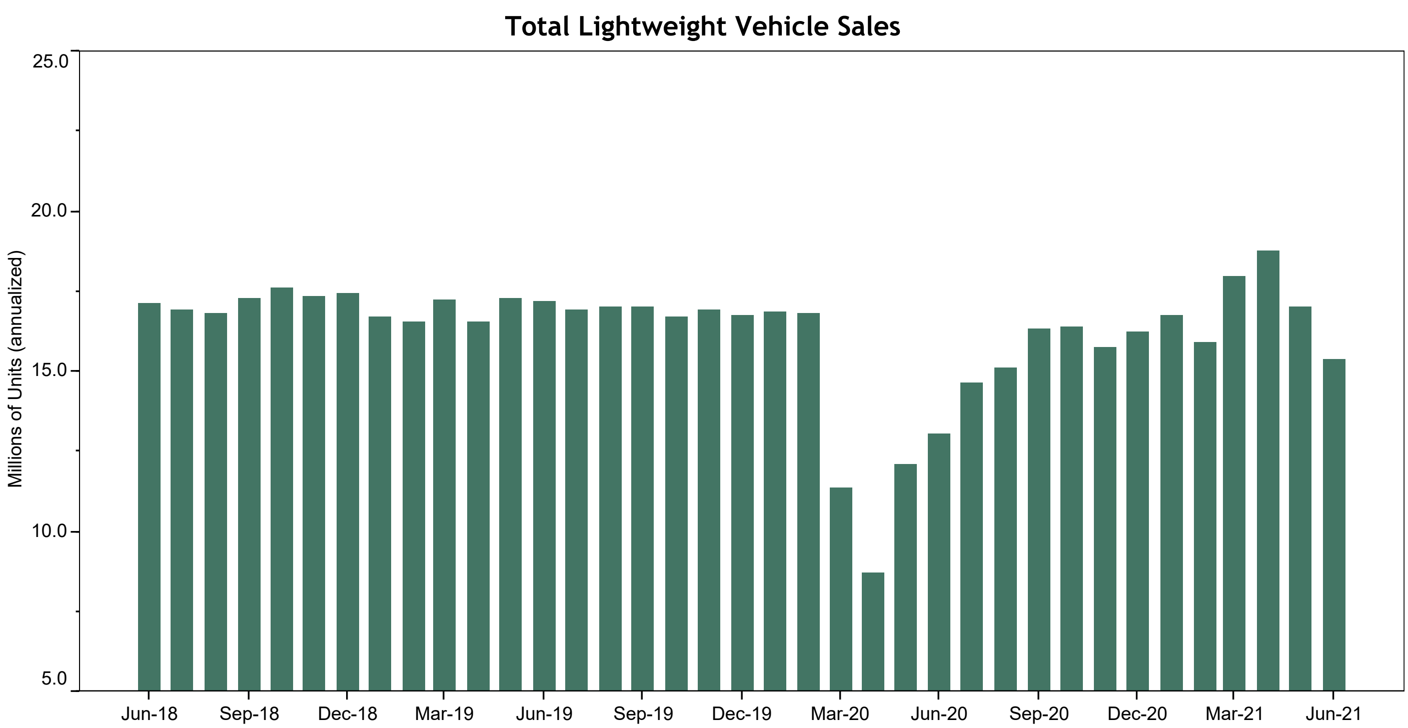


Source: University of Michigan (sentiment) and The Conference Board (confidence) / Haver Analytics.

Total retail sales declined by 1.3% in May after both March and April's numbers were revised upward. Core sales dipped 0.3% while sales excluding autos fell 0.7%. June sales data are due out Friday morning and markets anticipate an additional decline in total sales.



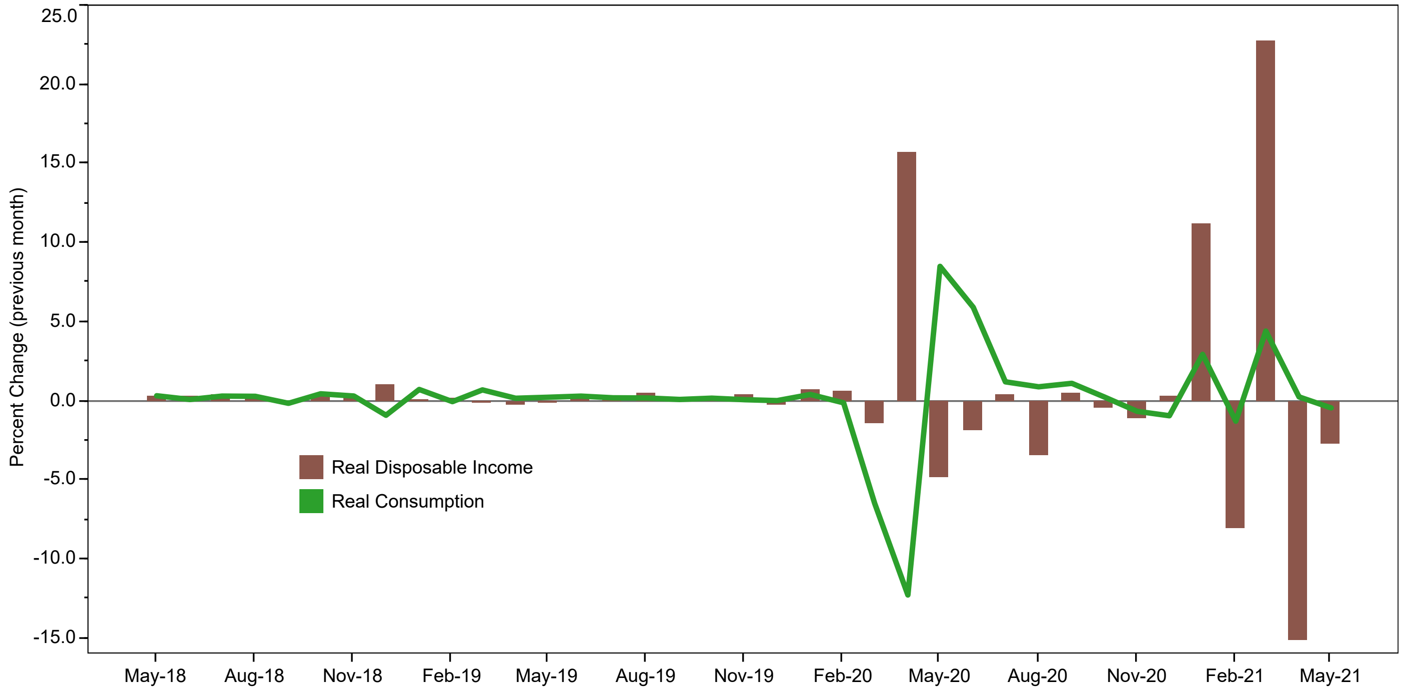
Sales of lightweight vehicles decelerated in June, falling to a 15.4 million-unit annual rate from the previous month's rate of 17.0 million. The continuing semiconductor shortage combined with high demand in recent months has left inventories quite sparse – a turn that is now weighing on sales.



Source: Bureau of Economic Analysis / Haver Analytics.

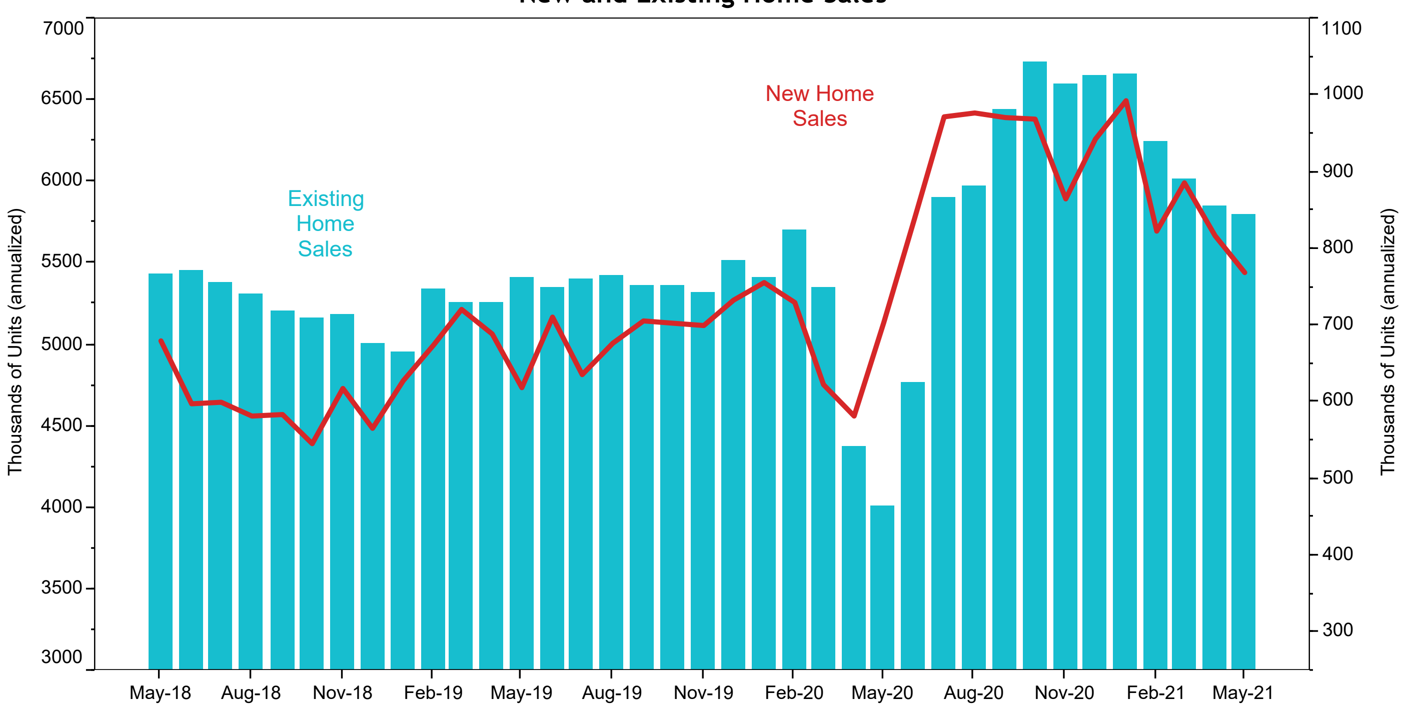
After April's 15.1% decline from the highs seen in March, real disposable income decreased 2.8% in May. Real consumption decreased 0.4% in May but was revised higher in the two previous months.

Real DPI and Consumption



Despite remaining at elevated levels, sales of new and existing homes decreased in May. New home sales fell 5.9% from the month prior to an annual rate of 769,000. Existing home sales registered the fourth consecutive month of declines, falling 0.9% to an annual rate of 5.80 million units in May.

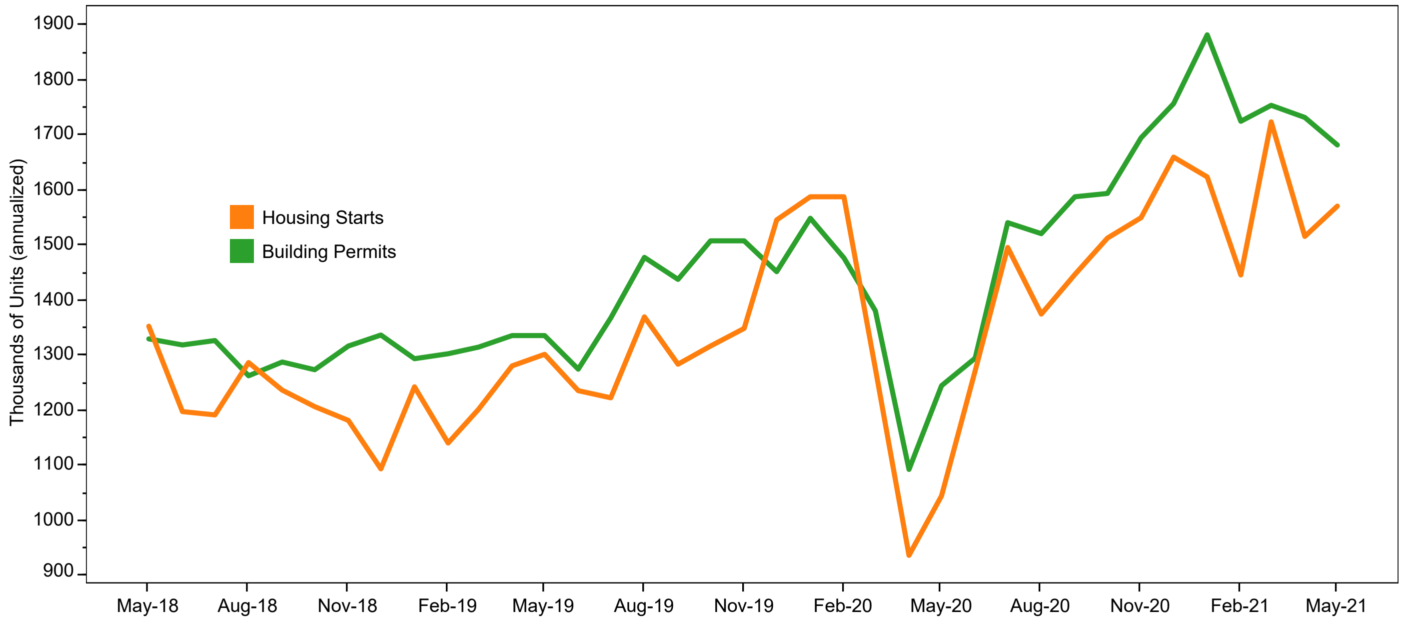
New and Existing Home Sales



Source: National Association of Realtors (existing home sales) and U.S. Census Bureau (new homes sales) / Haver Analytics.

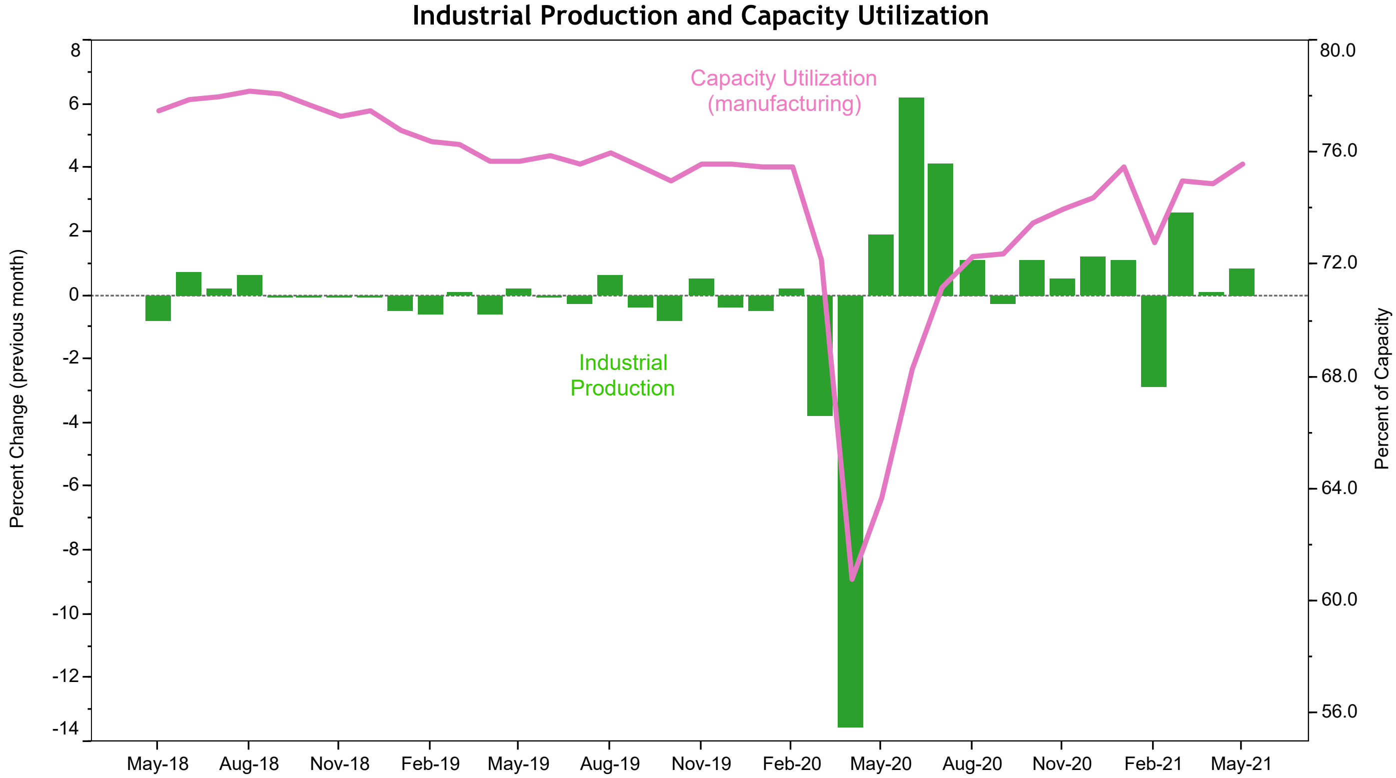
Housing starts rose 3.6% to a 1.57 million annual rate in May, aided by gains in both the single- and multi-family sector. Housing permits registered declines in May – falling 3.0% to an annual rate of 1.68 million units. Both single- and multi-family permits posted decreases. While starts and permits remain elevated, new construction is slowing amid higher input prices and material and labor shortages.

Housing Starts and Building Permits



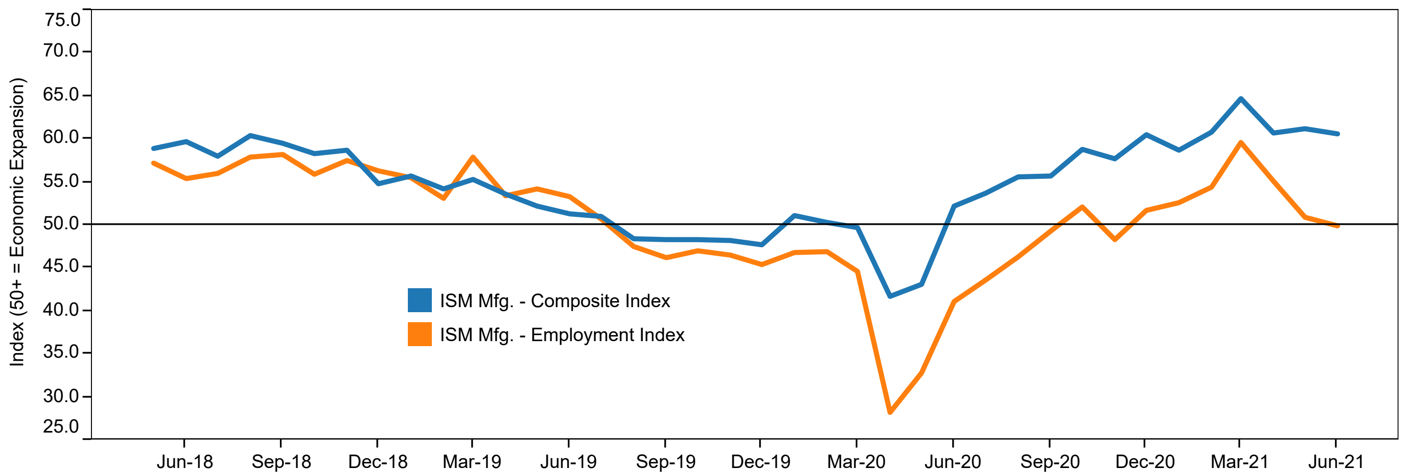
Industrial production grew 0.8% on a monthly basis in May after April's 0.5% gain was revised down to 0.1%. Manufacturing, mining and utilities all posted gains but have not attained their pre-pandemic levels. Output for motor vehicles and parts led the gains in manufacturing output but also remained depressed relative to pre-COVID levels. Capacity utilization in manufacturing rose to 75.6% in May - a reading that is 2.6 percentage points below it's long-run (1972-2020) average. Industrial production data for June are due out Thursday morning.

Industrial Production and Capacity Utilization

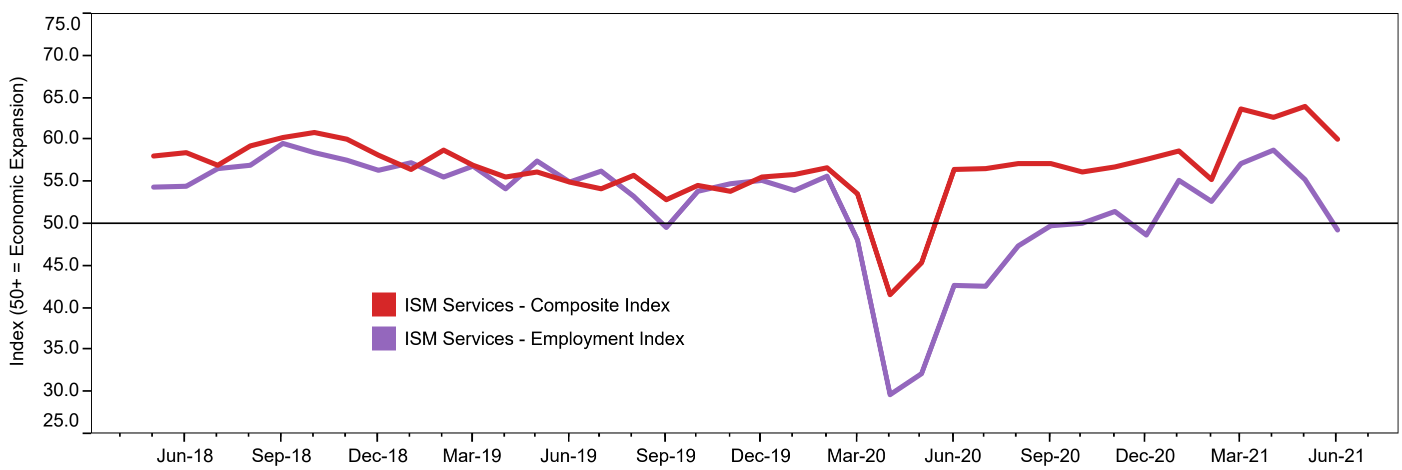


The ISM manufacturing index, despite remaining at elevated levels, slipped in June, falling to 60.6 from the previous month's reading of 61.2. While this number represents healthy expansion in manufacturing, it is the index's lowest level since January 2021. The employment component of the index fell to 49.9, signaling contraction for the first time since November 2020. The ISM services index saw similar movement as the composite index fell from 64.0 in May to 60.1 in June. The employment component also indicated contraction and did so for the first time since December 2020. Regional surveys from the Federal Reserve were mixed but all remained at elevated levels as well as in expansionary territory.

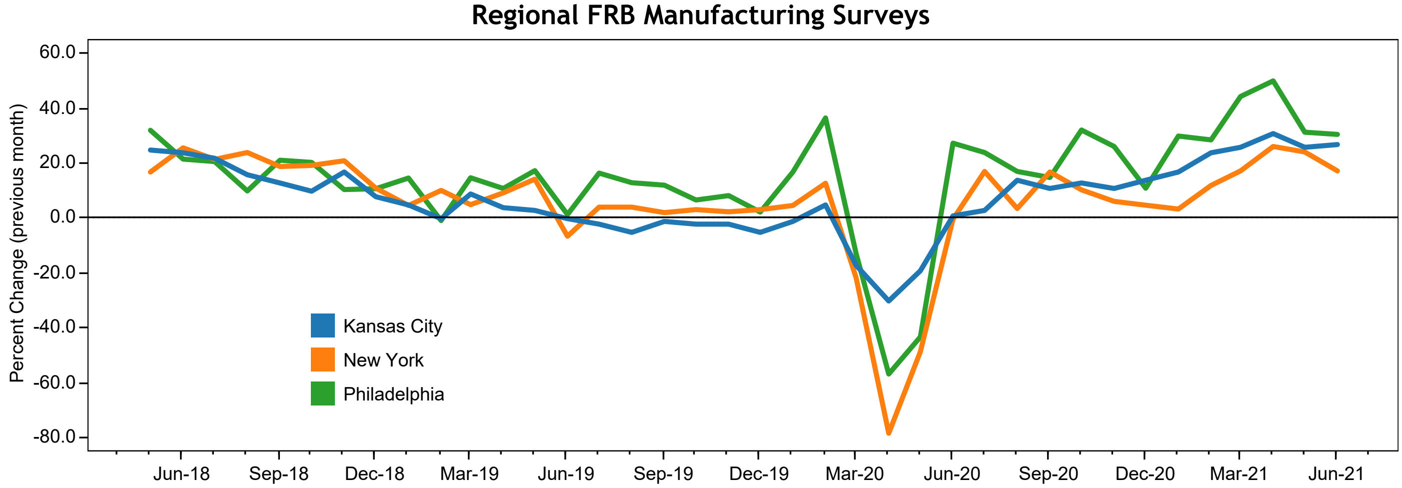
ISM Manufacturing Indices



ISM Services Indices



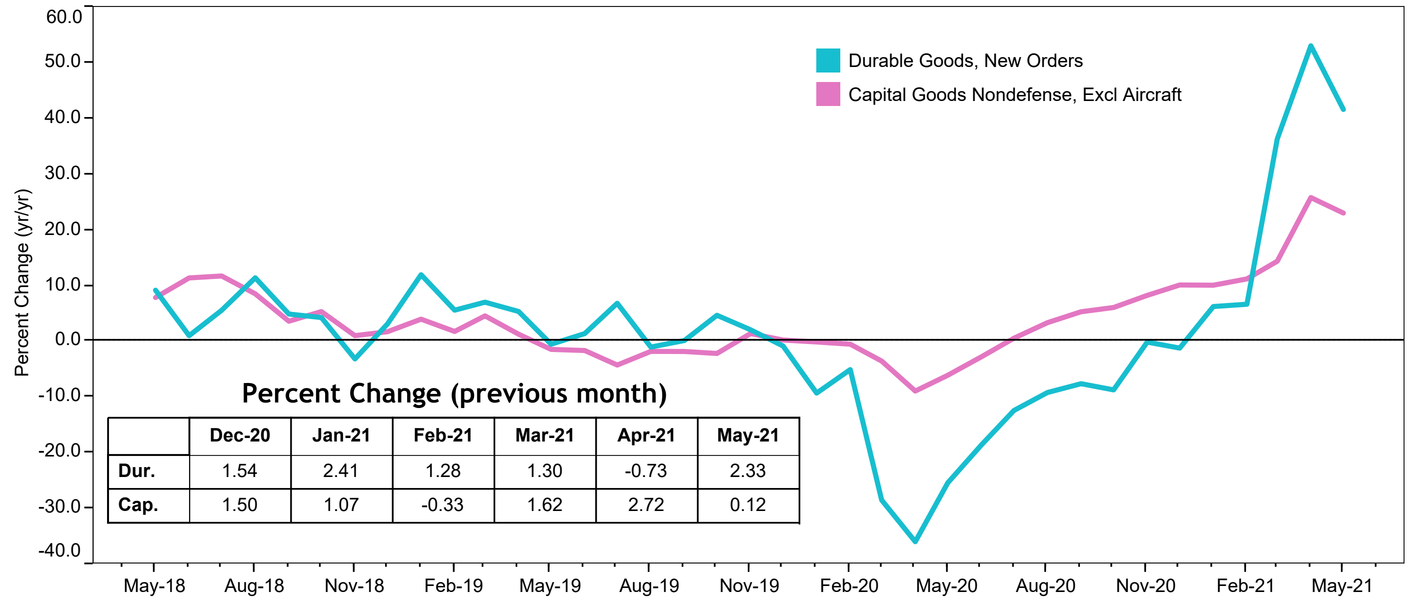
Regional FRB Manufacturing Surveys



Source: Institute of Supply Management / FRB Regional Banks: New York, Philadelphia, Kansas City / Haver Analytics.

Orders for durable goods rose for the 12th time in the last 13 months, showing an increase of 2.3% in May - more than offsetting April's 0.7% decline. The increase was driven mainly by orders for civilian aircraft that more than offset effects from supply chain issues and worker shortages. Orders of nondefense capital goods excluding aircraft rose 0.1% in May after a 2.7% increase in April. Despite being somewhat distorted by the pandemic's lows last year, year-over-year orders remained elevated.

Durable Goods Orders

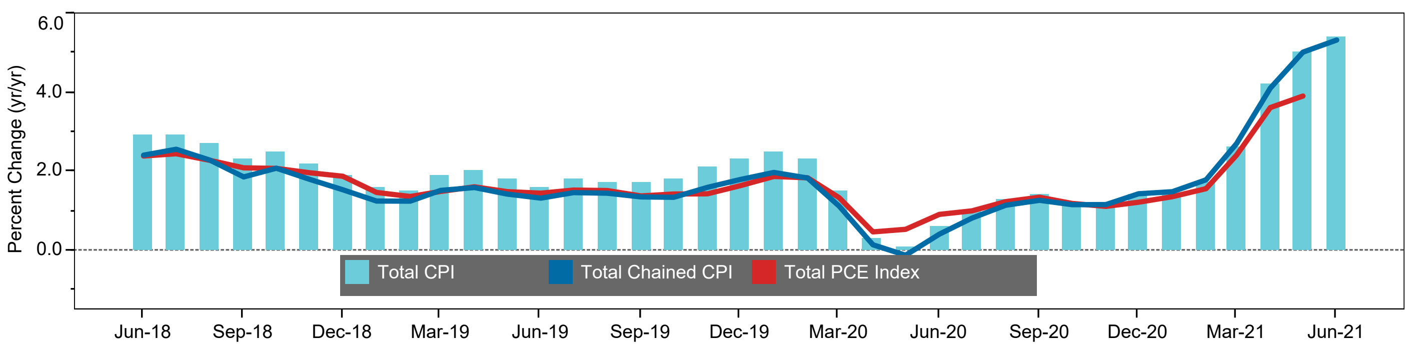


Percent Change (previous month)

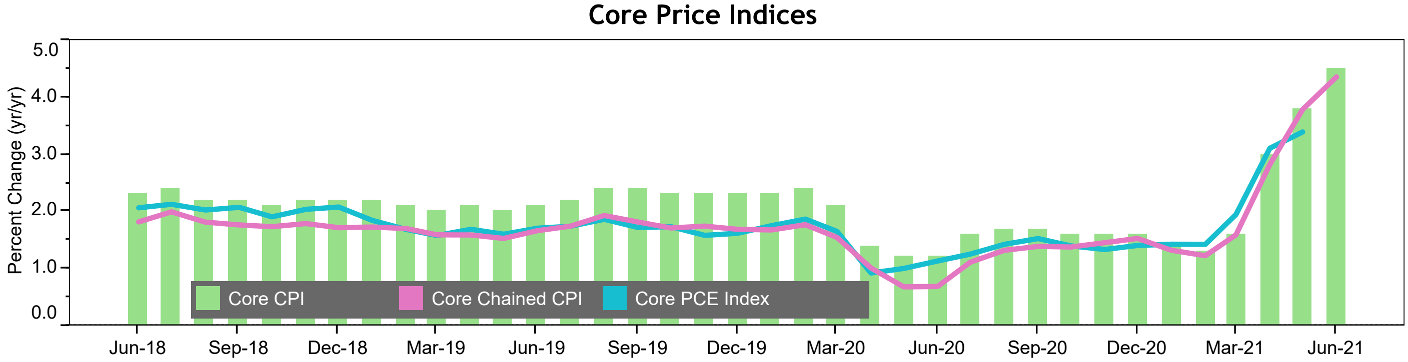
	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21
Dur.	1.54	2.41	1.28	1.30	-0.73	2.33
Cap.	1.50	1.07	-0.33	1.62	2.72	0.12

Consumer prices as measured by the CPI rose sharply in June as both total and core prices rose nine-tenths from May. On a year-over-year basis, total CPI jumped 5.4% as core CPI increased 4.5%. These are the highest annual rates in 13 years. In May, as measured by the PCE index, both total and core prices increased 0.4% and 0.5%, respectively. On a year-over-year basis, total PCE rose 3.9% while core prices rose 3.4%.

Total Price Indices

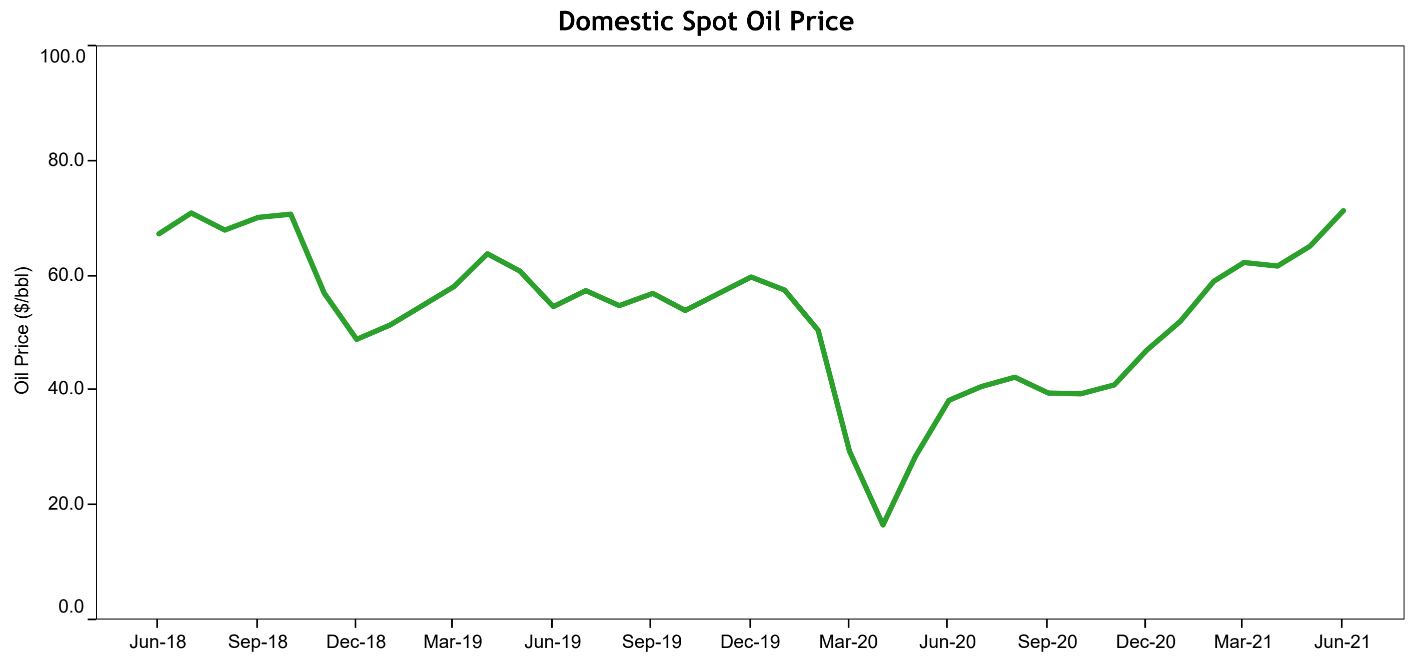


Core Price Indices

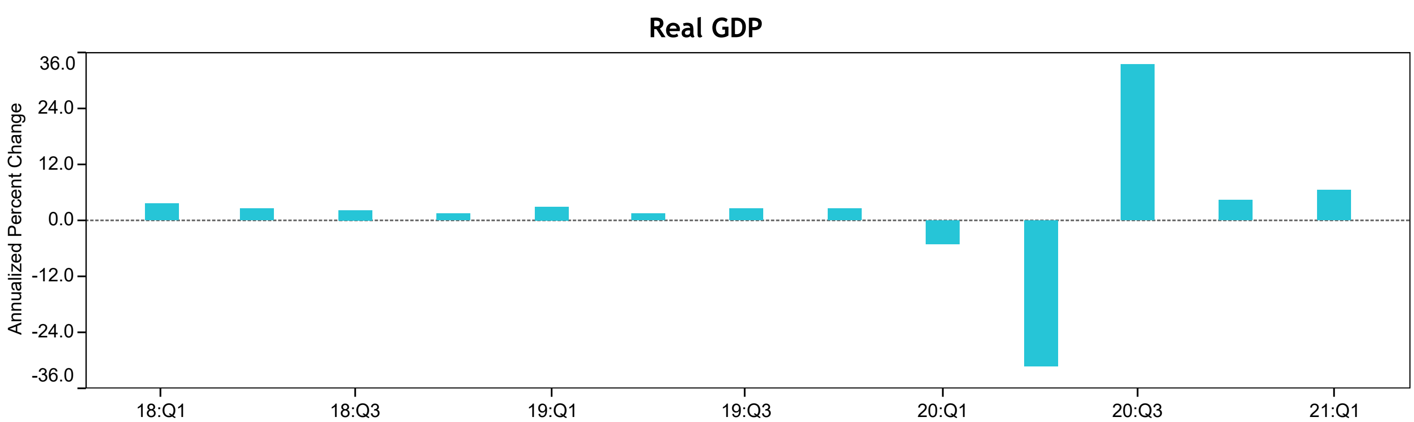


Source: Bureau of Labor Statistics / Bureau of Economic Analysis / Haver Analytics.

On average, oil prices in June rose to their highest monthly average since November 2014 - reaching $71.40 per barrel. Recent daily prices have remained above $70 and closed at $74.10 per barrel on July 12th.



In the third estimate, first-quarter real GDP growth was unrevised from the second estimate of 6.4%. Upward revisions to nonresidential fixed investment, private inventory investment, exports, and PCE were offset by an upward revision to imports.



Revisions to Q1 Real GDP

Description	Second Estimate	Third Estimate
Real GDP	6.4	6.4
Personal Consumption	11.3	11.4
Business Investment	10.8	11.7
Equipment and Software	13.4	15.0
Residential Investment	12.7	13.1
Government	5.8	5.7
Exports	-2.9	-2.1
Imports	6.7	9.5
Final Sales	9.4	9.2

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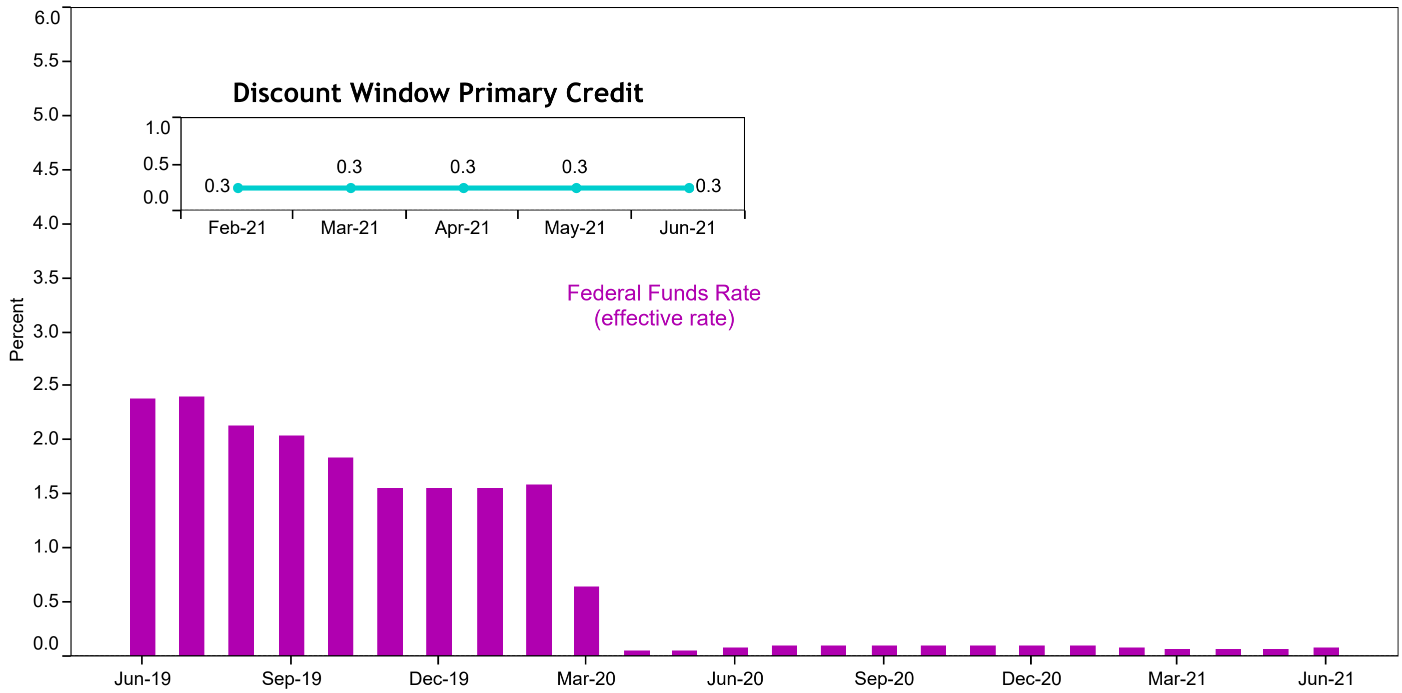
Short-Term Interest Rates



Source: Federal Reserve Board of Governors / Haver Analytics.
Report compiled by Mike Corbett and David J. Brown.