

Service sector starving for workers

The ISM services index was weaker than expected for June, falling to 60.1 (readings above 50 indicate expansion). While this is still a very strong reading and points to further solid sector growth, the survey data continued to highlight the challenges for service industries from the lack of available workers. New orders remained elevated, but overall business activity dropped despite the widespread reopening of in-person activities and the employment component fell into contraction for the first time since December.

Job openings remained at record levels at the end of May, a bit higher than April at 9.2 million. The largest surge in openings has occurred within the service sector, led by 1.25 million open positions in leisure and hospitality. Given that total recreation and restaurant employment were still down by 18 percent and 12 percent, respectively, in June compared with their pre-pandemic peaks, these businesses have the most need to refill staffs as demand has returned. But the lack of interested workers has cut into capacity while forcing more employers to raise wages for their incoming or current talent.

The theme of labor shortages continued within the advanced jobs data for June from the National Federation of Independent Business. A near-record 56 percent of small businesses reported few or no qualified applicants while nearly half were not able to fill job openings. A record 39 percent of firms raised compensation with more planned increases on the way. The prospect of higher earnings, the fading of special pandemic unemployment benefits, and the eventual return of in-person schooling should prompt more workers to reenter the workplace in coming months. But sector growth could be capped by low labor supply in the meantime, even as consumer demand for services moves higher.

Long-term interest rates continue to fall

After ending the first quarter at a post-COVID peak of 1.74 percent, the 10-year Treasury note yield slid backward during the second quarter to close at 1.44 percent on June 30. This downward trend culminated last week as yields decreased sharply — ending the week at just above 1.35 percent and at one point hitting 1.25 percent in intraday trading on Thursday.

The run-up in long-term rates during February and March was driven primarily by faster growth and inflation expectations as the rapid vaccine rollout pushed forward the reopening of the economy and set into motion the supply crunch currently driving up some prices. As these price disruptions look increasingly transitory, forward inflation expectations have pulled back — helping to lower Treasury yields. Growth projections for the post-pandemic surge, while still very strong, have also eased in recent weeks — especially globally where the COVID delta variant is having the largest impact on consumer activity. Inflation expectations have also slipped a bit, likely pulling yields down some, as well.

But the key to the drop in rates over the past three months is probably a short-term supply-demand imbalance. Despite record federal budget deficits, new issuance of Treasury securities has slowed recently. At the same time, the Fed's QE purchases of Treasury securities has continued unabated — essentially taking up all of the new supply. As new supply increases again in coming months and the Fed at least starts discussing tapering its QE purchases, we expect that yields on longer-term Treasury securities will rise again, although held in check by little prospect of rate hikes by the Fed.

You Need to Know

Week in Review

Service sector growth hit by lack of labor

The ISM services index fell in June but still indicated solid expansion conditions. Small businesses continue to have difficulty finding workers to meet rising consumer demand.

Long-term interest rates pull back further in early July

The 10-year Treasury note yield briefly dropped below 1.30 percent as recent Fed purchases of Treasury notes have about equaled new issuance, with lower inflation and growth expectations having an impact, too.

Week Ahead (Forecasts)

Slower inflation projected for June

The consumer price index (CPI) likely rose by 0.4 percent for June — a smaller increase than over the previous three months but still above the long-term trend.

Retail sales likely up a tad, but held back by a sharp drop in light vehicle sales

The already reported supply-chain caused pullback in light vehicle sales is expected to hold down overall retail sales for June, with a rise of 0.1 percent.


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The Week Ahead

This will be a busy week for economic data with updates for retail sales, the consumer price index (CPI), and industrial production.

Inflation expected to moderate in June, although remaining high

Monthly readings from the consumer price index (CPI) were hotter than expected from March through May as a few price categories saw significant spikes during the fuller reopening of the economy. This — helped by base effects — pushed up the year-over-year figures for the overall and core (excluding energy and food) CPI to the highest rates in at least 13 years. The monthly change in the CPI is projected to moderate for June, increasing by 0.4 percent — still an annualized gain of 4.9 percent. But with an even faster monthly gain a year earlier, the 12-month change in the overall CPI should edge down to 4.8 percent. The core CPI should see a slower increase of 0.3 percent, although this would move up the 12-month trend rate to 3.9 percent.

Retail spending to be held back by lower auto sales

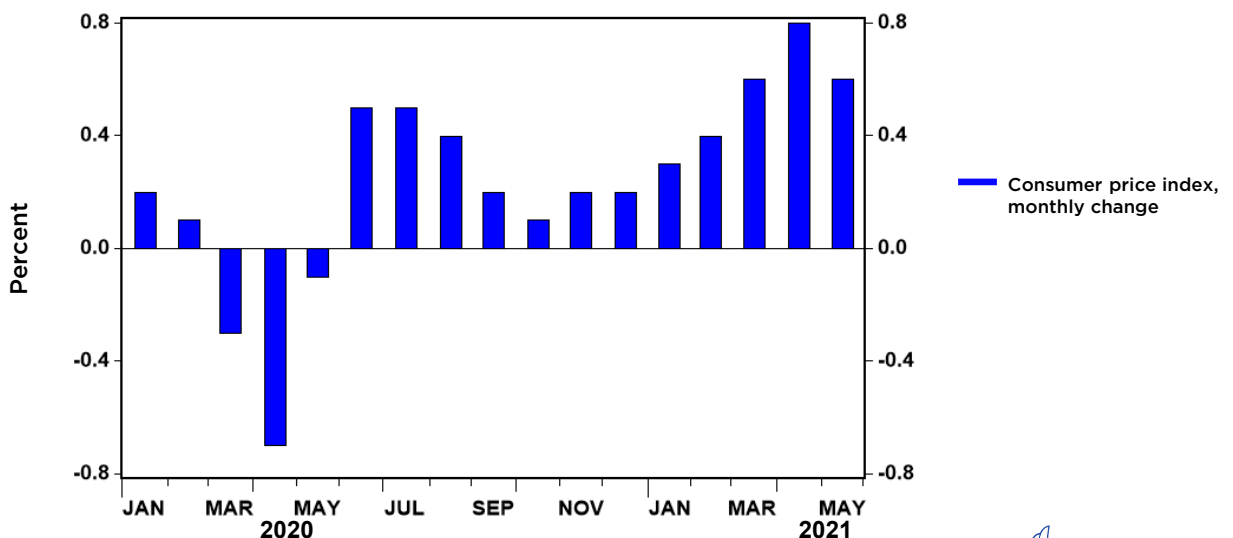
Retail sales dropped for May in a continuation of the post-stimulus lull in spending following March's surge. We expect that the combination of the nearly full return of in-person activities, rising incomes, and faster job gains lifted consumer activity for June. The already reported plunge in auto sales (owing to supply chain issues rather than weaker demand) will likely offset most of the solid spending gains in other categories, resulting in a modest 0.1 percent increase for retail sales. Sales excluding autos are projected to rise by a solid 0.9 percent.

Industrial production likely lifted by higher utilities

While supply chain issues have cut into operations for many manufacturers, the production component of the ISM manufacturing index climbed for June as producers look to satisfy strong market demand for goods. The weather across much of the country was hotter and drier than usual during June and should sharply boost utility output. Taken together, we expect industrial production to rise by a solid 1.0 percent during June with an increase in capacity utilization to 75.9 percent.

Worth Watching

Negative base effects for the CPI will reverse starting in June



Sources: Bureau of Labor Statistics/Haver Analytics

Weekly Market Snapshot

Equity	Last	Returns		
		1 Week	YTD*	1 Year*
S&P 500 (Large)	4,370	0.42%	17.24%	40.79%
S&P 400 (Mid)	2,706	-0.11%	18.07%	56.86%
S&P 600 (Small)	1,360	-0.73%	22.21%	72.16%
S&P 500 (High Quality)	49	0.35%	17.80%	38.60%
Russell 1000	4,724	0.38%	16.74%	42.55%
Russell 2000	5,666	-1.11%	16.00%	64.73%
Dow Jones	34,870	0.25%	15.05%	38.35%
NASDAQ	14,702	0.43%	14.47%	40.39%
MSCI EAFE	2,313	-0.07%	9.61%	31.49%
MSCI EM	1,318	-2.58%	3.37%	24.76%

*represents total return

S&P Metrics	LTM P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	24.89	21.62	13.33	23.06
Prior Month	24.97	21.20	8.99	24.54
Prior Year	21.63	21.97	-10.70	4.96

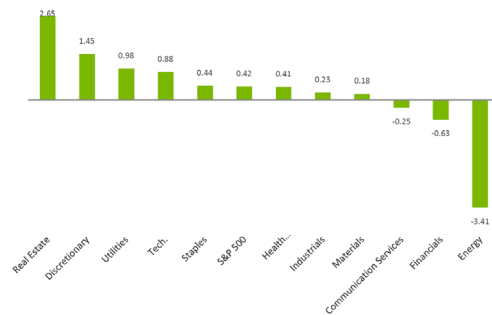
Fixed Income	Last	Returns		
		1 Week	YTD	1 Year
U.S. Aggregate	1.46%	0.31%	-1.18%	-0.56%
U.S. Inv Grade	2.05%	0.29%	-0.82%	2.51%
U.S. High Yield	4.56%	0.20%	4.03%	14.48%
TIPS	1.02%	0.25%	2.23%	6.30%

Rates	Last	Change		
		1 Week	YTD	1 Year
6M T-Bill	0.05%	0.00	-0.04	-0.11
2 Yr Treasury	0.23%	-0.01	0.10	0.07
5 Yr Treasury	0.79%	-0.07	0.43	0.51
10 Yr Treasury	1.37%	-0.07	0.44	0.75
30 Yr Treasury	1.99%	-0.06	0.34	0.67

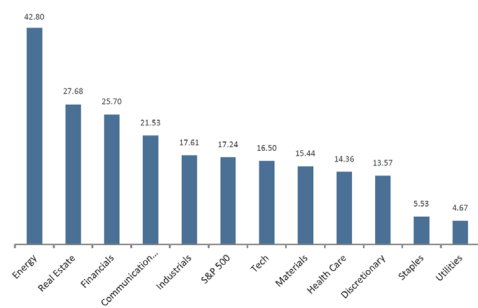
Spreads	Last	Change (Abs %)		
		1 Week	YTD	1 Year
AAA Rated	0.48	0.03	-0.07	-0.25
BBB Rated	1.14	0.03	-0.18	-0.86
High Yield	3.07	0.03	-0.79	-3.07
10 to 2 yr Treasury	1.14	0.00	0.34	0.68

Commodities/FX	Last	Returns (Currencies in \$ strength)		
		1 Week	YTD	1 Year
Gold	1810.00	1.54%	-4.39%	0.60%
Bitcoin	33878.06	0.29%	16.73%	266.94%
WTI Oil	74.63	-0.98%	54.35%	88.27%
EUR/USD	1.18645	-0.18%	3.03%	-5.06%
USD/JPY	110.14	-1.06%	6.68%	2.66%

S&P Sector Returns — Week (%)

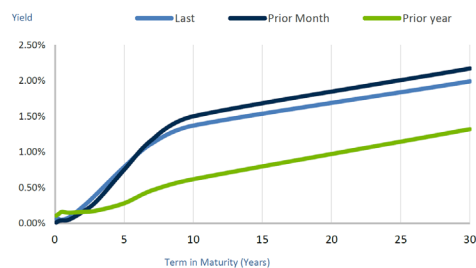


S&P Sector Returns — YTD (%)*



*represents total return

U.S. Yield Curve



Russell Style Returns — Week

	Value	Core	Growth
Large	-0.2	0.4	1.0
Mid	-0.1	0.0	0.2
Small	-1.3	-1.1	-0.9

Russell Style Returns — YTD

	Value	Core	Growth
Large	17.8	16.7	15.7
Mid	20.3	17.1	11.2
Small	24.8	16.0	7.8

Previous Week's Indicators

	Period	Actual	Previous
Markit services PMI	June	64.6	64.8
ISM services index	June	60.1	64.0
Job openings	May	9.2 M	9.2 M
Initial jobless claims	Week ending July 3	373,000	371,000

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Consumer price index (CPI)	Tues.	June	0.4%	0.7%
Core CPI	Tues.	June	0.3%	0.6%
Producer price index	Wed.	June	0.6%	0.8%
Initial jobless claims	Thurs.	Week ending July 10	365,000	373,000
Import price index	Thurs.	June	1.5%	1.1%
Empire state index (FRB NY)	Thurs.	July	21.7	17.4
Philadelphia Fed index	Thurs.	July	29.5	30.7
Industrial production	Thurs.	June	1.0%	0.8%
Capacity utilization	Thurs.	June	75.9%	75.2%
Retail sales	Fri.	June	0.1%	-1.3%
Retail sales ex-autos	Fri.	June	0.9%	-0.7%

* Nationwide Economics Forecast



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