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TD Economics

Data Release: Beige Book indicates that June rate hike is likely to proceed

- The Fed Beige Book reported continued economic progress at a modest or moderate pace throughout the country for the period of early-April through late-May, with the exception of the New York district that experienced a flattening out in activity. Optimism amongst business owners narrowed slightly as uncertainty surrounding future policy changes as a source of growth persisted.
- The scarcity of qualified workers continued to lead labor markets tighter, notably for manufacturers and information technology workers. The issue of recruiting and retaining low-skill workers was also emphasized, with many employers expanding their resources devoted to attracting and training workers. Regulatory changes surrounding visa issuance have constrained hiring in some industries including agriculture.
- Wage growth continued at a modest to moderate rate, but employers across several industries where labor shortages are pronounced raised wages substantially in order to attract qualified workers, namely in the manufacturing and IT segments. Although labor markets continued to strengthen, consumer spending was widely reported to be subpar during the period, and the shift to online shopping was noted by retailers as weighing on activity.
- Low inventory levels of residential property continued to lead home prices higher, presenting a challenge for buyers. This has constrained sales activity somewhat as homebuyers are increasingly being priced out. Despite this, these effects should dissipate as the year progresses and wage increases become more robust.
- Commodity prices, namely for lumber and steel, led producers to face higher costs in the construction and manufacturing industries. This is in contrast to the falling prices experienced in the more import-oriented final goods sectors that encompass groceries and apparel. Auto prices also retrenched in some districts as dealers expanded incentives as demand fell from last year's peak levels. Only modest increases in selling prices were seen as the effects of rising input costs have not translated through fully to consumers yet.
- Manufacturing activity continued at a brisk pace, coming off of a strong start to the year. The uncertain trajectory of future government policy was cited again as a cause for some caution in spending, and capital spending plans were largely unchanged from the prior report that indicated declining optimism for future growth as limiting investment in additional capacity.

Key Implications

- With producer prices rising steadily and wage increases being widely reported as labor becomes scarcer, inflation is likely to turn higher in the coming months after a period of subpar readings. This should also bolster consumer spending that was viewed as being soft through the first quarter.
- Although businesses are remaining cautious as the direction of government policy reform remains murky, economic growth overall is expected to at least stabilize above 2% in the coming quarters after the Q1 weakness, paving the way for robust hiring.

- The relatively robust growth outlook, echoed in this Beige Book, isn't likely to dissuade the Fed from proceeding with its June rate hike, provided we see continued labor market strength in this Friday's employment report.

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