TD Economics

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Data Release: U.S. services sector momentum rebounds in April

- After falling 2.4 points in March, the Institute for Supply Management's (ISM) non-manufacturing index rose 2.3 points to 57.5 in April – a print well above market consensus which called for only a modest rise to 55.8. The monthly rebound brings the index back near the highest level since late-2015.

- Gains were broad-based with most sub-indicators recording an improvement on the month. Among the most notable, were gains in new orders (up 4.3 points to 63.2) and new export orders (up 3 points to 65.5) – with both at the highest levels since prior to the Great Recession.

- Business activity (up 3.5 points to 62.4) and prices paid (up 4.1 points to 57.6) also recorded notable improvements – the latter having pulled-back in the prior two months.

- Among the remaining indicators, imports and inventory sentiment fell on the month, but the main soft spot in the report was arguably a slight deterioration in the employment sub-index which eased 0.2 points to 51.4 – the lowest point since mid-2016 – after having fallen 3.6 points in the month prior.

- Comments from survey contacts remained largely positive. Nearly all non-manufacturing industries surveyed reported growth in April, with agriculture, forestry, fishing & hunting being the only exception.

Key Implications

- Contrary to its manufacturing equivalent, which deteriorated for the second consecutive month, the ISM nonmanufacturing index accelerated markedly in April. The monthly improvement is encouraging as the gains were broad-based, comments from survey respondents remained largely positive, and the headline print remained well within expansionary territory.

- That said, in the context of a recent divergence between ‘hard' and ‘soft' survey-based data, there are two important elements worth highlighting in today's report. First is the downtick in the employment sub-index which may point to some softness in this Friday's payrolls report. The rebound in second quarter growth is expected to come as a result of a normalization in consumer spending, which hinges on a supportive labor market. A subpar payrolls print, along with a seemingly diminished appetite for durables goods as per April's soft vehicle sales print, could pare back expectations as to the size of the rebound.

- Today's improvement in the prices sub-index, coming after two consecutive monthly declines is a very welcome development that may signal a break for softening price pressures. We expect the recent softness in price trends to be temporary. But should it persist, it could delay the Fed's interest hiking cycle.

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