

## Softer US services growth favours further Fed rate cuts

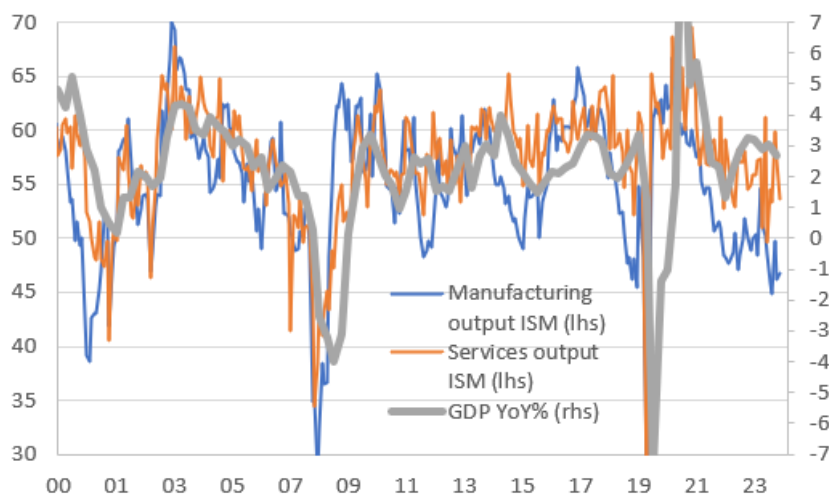
Commentary from Fed officials has leaned dovish over the past week, suggesting subdued data will give them greater confidence to cut rates at a third consecutive meeting on 18 December. This week's ISM reports have ticked that box and a soft jobs number on Friday would likely seal the deal even if next week's inflation data remains sticky



The November reading of the US ISM services index is quite a bit weaker than predicted. The headline balance dropped to 52.1 from 56.0 versus a consensus forecast of 55.7. This is the weakest reading for three months, but at least it remains above the break-even 50 reading. Business activity declined 3.5 points to 53.7 while new orders fell 3.7 points, also to 53.7. This is a disappointing outcome with the ISM attributing the softening to "election ramifications and tariffs... with cautionary outlooks related to the potential impact on respondents' specific industries".

On balance it is supportive of the rate cut narrative at the December FOMC meeting and suggests a cooling in economic growth in the fourth quarter, especially with the manufacturing ISM index remaining in contraction (sub 50) territory. The chart below shows the relationship between the output series for the services and manufacturing ISM reports versus GDP growth.

## ISM business surveys' output components versus GDP growth



Source: Macrobond

The employment component dropped to 51.5 from 53.0 while the prices paid component was little changed at 58.2. The relationship with non-farm payrolls and the ISM employment components has broken down in recent years and so we don't expect this outcome to seriously shift the consensus for Friday's jobs report. Remember that 53.0 is historically consistent with decent increases in employment, yet we know the outcome last month was for private payrolls to fall 28k. Likewise the private ADP series released earlier (146k versus the 150k consensus) is in our view a poor guide for non-farm payrolls. As such the current consensus of 215k looks about right to us. But remember that we will get 44k or so formerly striking workers returning and roughly 65k employees returning that were not included last month due to Hurricane Milton effects. Therefore the "true" payrolls expectation of actual jobs growth is  $215k - 44k - 65k = 106k$ .

The Fed commentary this week has generally leaned dovish and if we do get a jobs report indicating roughly 100k of net job creation and the unemployment rate ticks up to 4.2%, as we expect, then a 25bp rate cut on 18 December looks probable.

### Author

**James Knightley**

Chief International Economist

[james.knightley@ing.com](mailto:james.knightley@ing.com)

### Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit <http://www.ing.com>.