MORNING BRIEFING
January 26, 2022

The Monetary Policy Cycle

Check out the accompanying chart collection.

(1) More on Panic Attack #73. (2) How is this taper tantrum different than the previous three? (3) From cooing doves to squawking hawks. (4) Tracking the Fed's monetary policy cycle. (5) Bond yields rise during tightenings, fall during easings. (6) Yield-curve spread usually widens late during tightenings; this time, it's been narrowing before tightening has even started. (7) Stocks have rallied before and early during tightenings. (8) The P/E tends to rise and fall as the federal funds rate falls and rises. (9) A déjà vu of 2000 all over again? (10) S&P 500 forward revenues, earnings, and margins all at record highs. (11) Tracking Covid around the world. (12) Learning to live with the pathogen.

Strategy: Stocks & the Monetary Policy Cycle. Joe and I included the current market selloff in our *list of panic attacks* in Monday's *Morning Briefing*. It is #73 since the start of the bull market in 2009. In our opinion, it started on January 5 when the Fed released the minutes of the December 14-15 FOMC meeting. The minutes turned out to be more hawkish than investors expected, as Melissa and I discussed yesterday. So in our list, we are identifying the triggering event as a "taper tantrum."

As we've observed recently, the current taper tantrum is different than the previous three when inflation was low and the Fed could respond to the tantrums by backing off. Fed officials did that simply by stopping their hawkish talk and cooing like doves. Those pivots immediately calmed the stock market.

This time, Fed officials can't coo. They have to continue to squawk like hawks and act like hawks. The FOMC meeting that started yesterday will end today. At 2:00 p.m., the Fed will issue the committee's statement, and at 2:30 p.m., Fed Chair Jerome Powell will conduct his usual post-meeting press conference. It is widely expected that the Fed will signal a rate hike that will follow the March 15-16 meeting, i.e., after the Fed has terminated its QE4ever bond buying program. It is also expected that Powell will provide more details on the Fed's plan to allow its balance sheet to shrink as securities mature.

For context, let's have a look at the history of the monetary policy cycle since 1954:

(1) *Treasury bond yield.* Starting in 1954, the monetary policy cycle is determined by when

the Fed tightens by raising the federal funds rate and eases by lowering the federal funds rate (*Fig. 1*). In the past, the 10-year US Treasury bond yield consistently rose during periods of tightening and fell during periods of easing (*Fig. 2*).

This time, the yield bottomed at a record low of 0.52% on August 4, 2020. It rose over 1.00% in early 2021 and has been hovering around 1.50% since then. It was 1.78% yesterday. That's widely perceived to be unusually low given that the CPI inflation rate jumped over 2.00% during March 2021 and ended the year at 7.00% (*Fig. 3*). The monetary policy cycle suggests that the bond yield will start moving higher once the Fed actually starts to raise the federal funds rate. We are predicting that the yield will rise to 2.50% by the end of this year.

(2) *Yield curve.* The yield curve, defined as the spread between the bond yield and the federal funds rate, tends to narrow during tightening periods and turn negative at the end of such periods (*Fig. 4*). In the past, inverted yield curves have had an uncanny ability to anticipate financial crises that triggered widespread credit crunches and recessions (*Fig. 5*).

During periods of monetary easing, the yield-curve spread tends to widen. That's what it has been doing since the two-month recession of 2020. Then again, the spread between the 10-year and 2-year Treasury yields has been narrowing since early April (*Fig. 6*). That suggests that the bond market may already be anticipating that once the FOMC actually starts to hike the federal funds rate, the committee won't have to raise much before causing the sort of problems that cause the Fed to ease and push bond yields down!

(3) *Stocks.* In the past, the S&P 500 has tended to rally during periods of monetary tightening until investors anticipated an imminent recession (*Fig. 7*). That makes sense since the S&P 500 is one of the 10 components of the Index of Leading Economic Indicators, which tends to turn down about three months before recessions, on average (*Fig. 8*).

(4) *S&P 500 valuation.* Joe and I have compiled a data series for the P/E of the S&P 500 that uses trailing earnings from 1960 to 1978 and forward earnings from then on (*Fig. 9*). ("Forward earnings" is the time-weighted average of analysts' consensus earnings estimates for this year and next, which we calculate since it more precisely approximates the earnings prospects investors base decisions upon.) This combined series shows that the P/E tends to fall during tightening periods and to rise during easing periods.

The action in the stock market since January 5 suggests that investors are rerating the

forward P/E of the S&P 500 in anticipation of the tightening of monetary policy over the rest of this year. The pattern is reminiscent of what occurred during the Tech Wreck when the forward P/E crashed from a peak of 25.4 during the week of March 24, 2000 to 14.5 during the week of October 4, 2002 (*Fig. 10*). That happened even though the Fed was easing during most of that period. The big difference this time is that the earnings outlook is much brighter, especially for technology stocks.

(5) *S&P 500 earnings.* The good news for investors is that while they were rerating the forward P/E of the S&P 500 to the downside, forward earnings continued rising to record highs during the January 20 week (*Fig. 11*). That happened as forward revenues and the forward profit margin also rose to record highs.

(6) *Blue Angels.* Our Blue Angels framework displays the picture of the stock market's puzzle pieces (*Fig. 12*). The S&P 500 experienced a P/E-led meltup from 12.9 on March 23, 2020 to a high of 23.2 on September 2, 2021. It's been mostly an earnings-led meltup since the spring of 2020. Now it's a meltdown in the P/E to 19.6 on January 24 combined with the ongoing meltup in earnings!

(7) *Earnings and the federal funds rate.* By the way, there is a decent correlation between the y/y growth rate of S&P 500 forward earnings and the y/y change in the federal funds rate (*Fig. 13*). There was a closer fit between the cycles of the two prior to the Great Financial Crisis. The correlation could make a comeback if the federal funds rate rises to 1.00% by year-end 2022 and 2.00% by year-end 2023. That's what we expect currently, but we also expect to amend this forecast along the way.

Virus I: Covid's Leaps & Bounds. Just two months after the hyper-contagious Omicron variant of Covid-19 was first reported in South Africa, case counts have surged and then moderated around the world. But some regions where Covid has been allowed to run wild—either unintentionally or intentionally to promote herd immunity—are now reporting rebounding infections; India and Brazil are examples. Is herd immunity nothing but a pipe dream?

Last week, Jackie and I examined the lengths to which China has gone to enforce its zero-Covid policy—including shutting down factories, which could seriously disrupt global supply chains and boost prices further. Below, Melissa and I discuss Taiwan's zero Covid policy, which also has come at a price. Extreme social interventions such as China's and Taiwan's seemed to work to vanquish Covid in those regions, but is that a sustainable approach?

On a hopeful note, might human coexistence with Covid become no big deal if future mutations of the virus are decreasingly severe, as Omicron proved to be? It seems logical to think that viruses would tend to become more transmissible yet less severe as they mutate (because the inclination of a virus is to replicate and stay alive!). But scientists argue whether that will turn out to be the case with Covid.

If infections with mostly nonexistent to mild symptoms become commonplace, especially with the help of vaccinations that prevent severe disease, might counting cases become moot? Already, case counts seem borderline irrelevant when anecdotal examples abound of asymptomatic infections that came to light only from routine Covid testing in workplaces or health care facilities.

In any event, we will stop counting the rate of infection when everyone else does. For now, let's have a look at the latest Covid counts:

(1) *US.* The number of new Covid cases in the US hit a record-high 917,154 on January 19, using the 10-day moving average (*Fig. 14*). New cases may have peaked, as they since have continued to subside. Meanwhile, the number of Covid hospital patients, which lags infections, rose to a new record high of 150,217 on January 21, also using a 10-day moving average. However, the pace of hospitalizations has not nearly kept up with the pace of inflections.

(2) *Europe.* The sum of new cases in France, Germany, Italy, Spain, and the UK rose to a record of 907,189 on January 24, on a 10-day basis (*Fig. 15*). The number of hospital patients in just France, Italy, and the UK rose to 64,635 on January 21 (*Fig. 16*). But it has not yet reached a new record.

(3) *India and Brazil.* India's first wave occurred in summer 2020 (*Fig. 17*). The country's second wave was a nightmare during the spring of last year. The number of new cases crested at 382,588 on May 10, based on the 10-day moving average. But then it plunged to a remarkably low level under 10,000 during December. Now, India is entering its third wave. According to early *reports*, the cases popping up in this wave have been mild, *owing* to high rates of prior infection and vaccination.

Brazil seemed finally to be coming out of one long wave of pandemic misery during H2-2021. But now, Brazil's case count is back up again too.

Virus II: The Curious Case of Taiwan's Zero Covid. Taiwan is often credited with having

cracked the code on keeping Covid-19 outbreaks low while going about life as normal. Indeed, the nation has largely avoided significant lockdowns yet has reported just 18,041 cases to date out of a population of 23.5 million, reported Reuters on January 20. The country's largest outbreak, during H2-2021, saw thousands infected with the original variant; but case counts eventually were brought back to zero, observed *The Guardian* on January 22.

Other countries with zero Covid-19 policies, such as China, have managed to obtain that status temporarily via authoritarian-type mass lockdowns and mobility-control measures. Taiwan has taken a different but still life-disrupting approach. The question is: How long can Taiwan keep its extreme measures up without greatly impeding its global businesses and domestic tourism?

Without further ado, here are the elements of Taiwan's approach to keeping Covid at bay:

(1) *Extreme border control.* Strict border control and impeccable contact tracing have allowed Taiwan's inhabitants to roam the island fairly freely while the pandemic raged elsewhere. In other words, the entire Island could be considered to have been in lockdown from the rest of the world. Even today, Taiwan continues to be open for essential travel only while tourism remains banned. In 2019, more than 29 million international arrivals entered Taiwan. In 2020, the figure dropped to 3.9 million. Through October of last year, just 335,000, reported *The Guardian* on November 8, 2021.

(2) *Quarantines, testing, masking.* Quarantining and testing are strongly enforced for essential travelers. Negative PCR Covid-19 tests are required from all visitors, who must quarantine for 14 days at a government-approved hotel. Residents are permitted to quarantine at home if they can prove they live alone, reports *Traveling Lifestyle*.

(3) *Some social restrictions.* Taiwan immediately clamps down on measures at the borders after identifying small numbers of cases. On January 22, Taiwan's Central Epidemic Command Center (CECC) reported 82 domestic cases, including 63 mostly migrant workers found ill in one cluster at the Taoyuan factory, noted *The Guardian*. To tackle the small recent rise in Omicron cases, the Ministry of Labor restricted the mobility of migrant workers and imposed mass-testing requirements on employers of 50 or more migrant workers. Taiwan also has a compliant public on its side.

(4) *Vaccinations are popular.* Taiwan mandates full vaccination for entry into entertainment venues such as night clubs and bars, Reuters reported. More than 70% of people in Taiwan

have received two vaccine doses. Starting this week, visits to hospitalized patients or people in long-term residential care facilities will be *banned* unless for emergency.

(5) *Waiting to coexist.* During the H2-2021 outbreak in the capital city, masks were required to be worn indoors and violators fined. Schools and local councils also were closed for several weeks. At that time, the island had one of the lowest vaccination rates in the world at less than 1% of the population, *reported* CNN.

In September 2021, CECC told *The Guardian* that it isn't targeting zero Covid-19 but is heading toward it. "The current goal is to achieve Covid-19 zero, but Taiwan must also be prepared to coexist with Covid-19," the health minister told parliament.

In October 2021, a special adviser to the CECC, said: "We must wait until the virus becomes mild and the human immune system can adjust before it can start coexisting with the virus." *The Guardian* reported that he seemed to suggest that could take about three years.

Virus III: Learning To Live with Covid. One of Israel's leading immunologists, Professor Ehud Qimron, head of the Department of Microbiology and Immunology at Tel Aviv University, recently wrote an open *letter* sharply criticizing the Israeli and global management of the pandemic. Here's what he had to say and what we say in response:

(1) *Control is too costly.* "Two years late, you finally realize that a respiratory virus cannot be defeated and that any such attempt is doomed to fail. … You refused to admit that the infection comes in waves that fade by themselves, despite years of observations and scientific knowledge. … You refused to admit that mass testing is ineffective. … You refused to admit that recovery is more protective than a vaccine. … You insisted on ignoring the fact that the disease is dozens of times more dangerous for risk groups and older adults. … You refused to adopt the 'Barrington Declaration', signed by more than 60,000 scientists and medical professionals."

The professor concluded: "When you compare the destructive policies you are pursuing with the sane policies of some other countries—you can clearly see that the destruction you have caused has only added victims beyond the vulnerable to the virus. The economy you ruined, the unemployed you caused, and the children whose education you destroyed—they are the surplus victims as a result of your own actions only."

(2) *But vaccines do work.* To the professor's point about vaccines being less protective than

recovery, we observe that vaccines do appear to be effective against Covid hospitalization. US Centers for Disease Control and Prevention (CDC) reported this week that booster doses were 90% effective at keeping people out of the hospital after they had become infected with the Omicron variant. Doses were 82% effective at preventing emergency department and urgent care visits.

Further, adults ages 65 and older who are not vaccinated against Covid-19 are nearly 50 times more likely to be hospitalized than seniors who have received a full vaccine course and a booster shot, according to CDC data, *reported* Fox on Friday. Recent jumps in pediatric hospitalizations also were *reported* to have been mostly among unvaccinated kids.

Our conclusion: Whether by vaccine, natural immunity, virus mutation, or a combination of the three, Covid is likely to become less and less severe, which will likely lead to less severe restrictions around the world. Whether the draconian means of virus control undertaken by some countries justify the ends they've achieved remains a subject of heated debate.

Calendars

US: Wed: New Home Sales 760k; Goods Trade Balance Advance Estimate -$96.1b; Wholesale Inventories 1.3%; MBA Mortgage Applications; Crude Oil Inventories & Imports; FOMC Interest Rate Decision 0.25%. **Thurs:** Real GDP & GDP Price Index 5.5%/6.0%; Core PCED 4.9%; Durable Goods Orders, Total, Core, and Core Nondefense Capital Goods Orders -0.5%/0.4%/0.4%; Initial & Continuous Jobless Claims 260k/1.65m; Kansas City Fed Manufacturing Index; Pending Home Sales -0.2%; Natural Gas Storage. (Bloomberg estimates)

Global: Wed: France Consumer Confidence 98; BOC Interest Rate Decision 0.25%. **Thurs:** Germany Gfk Consumer Climate -7.8; Spain Unemployment Rate 14.2%. (Bloomberg estimates)

Strategy Indicators

S&P 500 Earnings, Revenues, Valuation & Margins (*link*): The S&P 500's forward profit

margin was steady at a record high of 13.3% last week. Since the end of April 2020, it has exceeded its prior record high of 12.4% in September 2018. It's now up 3.0ppts from 10.3% during April 2020, which was the lowest level since August 2013. Forward revenues and forward earnings per share were also at record highs. They've both been making new highs since the beginning of March 2021 after peaking just before Covid-19 in February 2020. Since the Q2-2021 earnings season came in way better than expected, analysts have been playing catch-up with their lowball estimates from the Covid-19 shutdown period. Prior to this catch-up period, consensus S&P 500 forecasts had been falling at rates paralleling the declines during the 2008-09 financial crisis. Forward revenues growth remained steady w/w at 7.3%, just above its 12-month low of 7.1% in early December. That's down from a record high of 9.6% growth at the end of May 2021 and should continue to move lower as base effects subside. Still, that's up from 0.2% forward revenues growth during April 2020, which was the lowest reading since June 2009. Forward earnings growth fell 0.4ppt to 8.6%. It remains above its 16-month low of 8.2% in early December, but should also continue to move lower due to base effects. That's down from its 23.9% reading at the end of April 2021, which was its highest since June 2010, and up substantially from its record low of -5.6% at the end of April 2020. On a positive note, this year analysts have been raising their consensus forecasts for 2021 and 2022 revenues and earnings growth; the imputed profit margin estimate that we calculate from those forecasts has been rising too. They expect revenues to rise 16.3% in 2021 (up 0.1ppt w/w) and 7.7% (up 0.1ppt w/w) in 2022 compared to the 2.1% decline reported in 2020. They expect earnings gains of 50.6% in 2021 (up 0.5ppt w/w) and 8.6% in 2022 (down 0.3ppt w/w) compared to a 13.4% decline in 2020. Analysts expect the profit margin to rise 3.0ppts y/y in 2021 to 13.1% (unchanged w/w) from 10.1% in 2020 and to improve 0.1ppt y/y to 13.2% in 2022 (unchanged w/w). The S&P 500's weekly reading of its forward P/E fell 0.9pt to a 20-month low of 21.2. That's down from an eight-month high of 21.7 at the end of 2021 and compares to 23.1 in early September 2020, which was the highest level since July 2000 and up from a 77-month low of 14.0 in March 2020. The S&P 500 weekly price-to-sales ratio fell 0.12pt w/w to a 14-week low of 2.70, and is down from a record high of 2.88 at the end of 2021. That's up from its four-month low of 2.69 in mid-October and compares to its prior record high of 2.86 at the end of November and a 49-month low of 1.65 in March 2020.

S&P 500 Sectors Earnings, Revenues, Valuation & Margins (*link*): Last week saw consensus forward revenues rise for eight of the 11 S&P 500 sectors, forward earnings move higher for six sectors, and the forward profit margin rise for two sectors and fall for two. Nearly all sectors are at or near record highs in their forward revenues, earnings, and profit margin. Energy still has forward revenues and earnings well below record highs, but its profit margin is the highest since November 2008. Financials, Real Estate, and Utilities

have forward earnings at or near record highs, but their forward revenues and margins are lagging. Only three sectors posted a higher profit margin y/y in 2020: Consumer Staples, Tech, and Utilities. For 2021, a y/y improvement is expected for all but Utilities. Four sectors are expected to see margins decline or remain flat y/y in 2022: Communication Services, Financials, Materials, and Real Estate. The forward profit margin was at record highs during 2018 for 8/11 sectors, all but Energy, Health Care, and Real Estate. Here's how they rank based on their current forward profit margin forecasts along with their record highs: Information Technology (25.0%, down from its 25.1% record high in December), Communication Services (16.7, down from its 17.0 record high in October), Real Estate (16.3, down from its 19.2 record high in 2016), Utilities (14.7, down from its 14.8 record high in April), Materials (13.3, down from its 13.4 record high in December), S&P 500 (13.3, a record high this week), Health Care (11.4, a new record high this week), Industrials (10.3, down from its 10.5 record high in December 2019), Consumer Staples (7.6, down from its 7.7 record high in June), Consumer Discretionary (8.0, down from its 8.3 record high in 2018), and Energy (9.2 [13-year high], down from a record-high 11.2 in 2007).

S&P 500 Sectors Forward Revenues and Earnings Recovery from Covid-19 Trough (*link*): The S&P 500's forward revenues and earnings as well as its implied forward profit margin bottomed at cyclical lows on May 28, 2020 after 14 weeks of Covid-19-related declines. Forward revenues and earnings have risen 23.2% and 59.7%, respectively, since then to new record highs. The forward profit margin has risen 3.3ppts to a record high of 13.3%. That exceeds its prior pre-Covid record of 12.4% in late 2018. During the latest week, consensus forward revenues rose for eight of the 11 S&P 500 sectors, forward earnings moved higher for six sectors, and the forward profit margin rose for two sectors and fell for two. Here's how the S&P 500 and its 11 sectors rank by their changes in forward revenues and forward earnings since May 28, 2020: Energy (forward revenues up 43.0%, forward earnings up 2,206.6%), Materials (34.2, 103.1), Information Technology (29.5, 48.8), Industrials (28.1, 79.2), Communication Services (26.0, 57.7), S&P 500 (23.2, 59.7), Financials (21.2, 67.3), Health Care (19.3, 35.5), Consumer Discretionary (18.1, 102.5), Real Estate (14.6, 31.6), Consumer Staples (14.4, 21.2), and Utilities (0.3, 6.0).

S&P 500 Q4 Earnings Season Monitor (*link*): With nearly 14% of S&P 500 companies finished reporting revenues and earnings for Q4-2021, revenues have beat the consensus forecast by 2.5% and earnings by 6.6%. While these surprises are above the long-term trend, the earnings surprise is the weakest since Q1-2020. At the same point during the Q3 season, revenues were 2.2% above forecast and earnings beat by 14.3%. For the 68 companies that have reported Q4 earnings through mid-day Tuesday, the aggregate y/y revenue and earnings growth rates have slowed considerably from their readings during Q2

and Q3. The small sample of Q4 reporters so far collectively has a y/y revenue gain of 12.5% and an earnings gain of 26.5%. Just 78% of the Q4 reporters so far has reported a positive earnings surprise, below the 81% that has beaten revenues forecasts. Furthermore, fewer companies have reported positive y/y earnings growth in Q4 (78%) than positive y/y revenue growth (90). These figures will change markedly as more Q4-2021 results are reported in the coming weeks, but the early read on earnings is disappointing compared to the previous six quarters. We expect the y/y growth rates to continue easing in Q4 compared to Q2 and Q3. We also think the revenue and earnings surprises will moderate q/q as well due to missed deliveries, higher costs, and increased company guidance ahead of the earnings season.

US Economic Indicators

Consumer Confidence (*link*): "Consumer confidence moderated in January, following gains in the final three months of 2021," said Lynn Franco, senior director of economic indicators at The Conference Board. "The Present Situation Index improved, suggesting the economy entered the new year on solid footing. However, expectations about short-term growth prospects weakened pointing to a likely moderation in growth during the first quarter of 2022," she warned. "Looking ahead, both confidence and consumer spending may continue to be challenged by rising prices and the ongoing pandemic." Consumer confidence slumped to 113.8 this month after climbing from 109.8 in September to 115.2 by December, as the expectations component fell to 90.8 this month after rising from 86.7 in September to 95.4 by the end of 2021. The present situation (to 148.2 from 144.8) component, meanwhile, posted its biggest monthly gain in seven months in January after hovering around 145.0 the final four months of 2021. Consumers' appraisal of current business conditions improved in January for the second month, as the percentage saying conditions are good (to 21.1% from 17.9% in November) climbed over the period and the percentage saying conditions are bad (25.6 from 27.3) fell. Consumers' assessment of the labor market was mixed, with those saying jobs are plentiful (55.1 from 55.9) slipping just a bit this month—holding around this percentage since mid-2021—while the percentage saying jobs are hard to get (11.3 from 11.7) also fell slightly, hovering around that percentage the final three months of last year. Meanwhile, the percentage of consumers expecting business conditions to improve (23.8 from 25.4) over the next six months fell in January, while the percentage that expects conditions to worsen (19.0 from 18.6) rose. Consumers were also less optimistic about the short-term labor market outlook, with the percentage expecting jobs to be more available (22.7 from 24.2) moving down and the

percentage expecting fewer jobs (15.7 from 14.7) moving up.

Regional M-PMIs (*link*): Three Fed districts (New York, Philadelphia, and Richmond) have reported on manufacturing activity for January and show the manufacturing sector slowed for the second month, rising at half December's pace this month—as activity in the New York region stalled after 18 months of positive readings. The composite index eased to 10.2 from 21.1 in December and 27.0 in November. Manufacturing activity in the New York (to -0.7 from 31.9) region was slightly negative, while growth in the Richmond (8.0 from 16.0) area was cut in half. In the meantime, growth in the Philadelphia (23.2 from 15.4) region picked up steam in January after being more than halved in December. The new orders (6.3 from 19.3) measure was also impacted by negative growth in the New York (-5.0 from 27.1) and slower growth in the Richmond (6.0 from 17.0) regions this month; new orders growth in the Philadelphia (17.9 from 13.7) area was slightly faster—after slowing appreciably in December from November's 47.4. Meanwhile, jobs growth slowed again in January, to 15.4 from 24.8 and 26.7 the previous two months. Growth eased across all three regions: Philly (26.1 from 33.9), New York (16.1 from 21.4), and Richmond (4.0 from 19.0)—though Philly's held near December's record high.

Regional Prices Paid & Received Measures (*link*): We have prices-paid and -received data for January from the Philadelphia, New York, and Richmond regions, and it's a mixed bag. (Note: The Philadelphia and New York measures are diffusion indexes, while Richmond's measures are average annualized inflation rates—which we multiply by 10 for easier comparison to the other regional measures). The prices-paid measure for Richmond (to 143.2 from 139.8) reached another new record high this month, while Philadelphia's gauge accelerated to 72.5 in January after slowing from 80.0 to 66.1 in December. Meanwhile, New York's measure eased for the second month, from 83.0 in November to 76.7 this month; it was at a record high of 83.5 last May. Richmond's prices-received (112.7 from 82.6) gauge also jumped to a new record this month, while both the New York (to 37.1 from 50.8 in November) and Philadelphia (46.4 from 62.9) prices-received measures slowed for the second successive month—New York's from a record high and Philadelphia's from close to its record high of 63.8 in the mid-1970s.

Global Economic Indicators

Germany Ifo Business Climate Index (*link*): "The German economy is starting the new year with a glimmer of hope," notes Clemens Fuest, Ifo president. Ifo's business climate

index rose for the first time in seven months, climbing to 95.7 as the new year began, after sliding from 101.7 to a 10-month low of 94.8 during the last half of 2021. The expectations component accounted for the move up, rebounding to 95.2 in January, after a six-month drop from 103.2 in June to 92.7 by December. The present situation component, in the meantime, declined for the fifth successive month, from a recent high of 101.6 last August to an eight-month low of 96.1 this month. The manufacturing index (to 19.9 from 17.4) improved this month, with both the present situation (31.9 from 29.5) and expectations (8.4 from 6.1) components moving higher—with the report noting that supply bottlenecks in intermediate products and raw materials have eased a bit. Sentiment in the service sector (7.7 from 4.6) also improved as pessimism disappeared from these companies' expectations (2.2 from -6.3), while sentiment in the construction sector (8.7 from 7.6) got a boost as material shortages eased further.

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