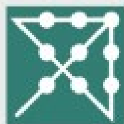
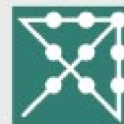
 Yardeni Research 

MORNING BRIEFING
March 21, 2022

A Very Brief History of the Rise & Fall of Modern Monetary Theory

Check out the accompanying chart collection.

Executive Summary: Now that the Fed is tightening, US monetary policy is no longer bullish for stocks; the "Fed Put" is dead. Replacing it: the "CFO Put," i.e., the market-buoying activities of corporate CFOs. But the tug-of-war between bearish and bullish forces may not be won decisively by either side in coming months; we see a volatile sideways-trading S&P 500. … Yield-curve inversion fears are misplaced. Inversion doesn't cause a financial crisis/credit crunch/recession scenario but predicts one. And more convincing predictors are flashing no-recession signals—including the Fed's lack of inflation-fighting gusto. … Also: Policymakers implemented Modern Monetary Theory during the pandemic, revealing the folly of the theory.

YRI Monday Webcast. Join Dr. Ed's live Q&A webinar on Mondays at 11 a.m. EST. You will receive an email with the link to the webinar one hour before showtime. Dr. Ed's presentation lasts about 15 minutes with another 15 minutes for Q&A. Replays of the Monday webinars are available *here*. You can view a replay of Dr. Ed's recent one-hour webcast on "Predicting Inflation" *here*.

Strategy I: The CFO Put. The Fed Put is probably dead now that inflation is raging and the Fed is in tightening mode. However, it has been replaced by the CFO Put. Corporations have lots of cash on their balance sheets, which they've raised over the past two years at record-low interest rates (*Fig. 1*). They are also generating a record amount of cash flow (*Fig. 2*). Consider the following:

(1) *Buybacks and dividends.* Last year, the CFOs of the S&P 500 companies repurchased a record $881.7 billion of their shares (*Fig. 3*). Some of that reflected purchases to offset the dilution of per-share results stemming from new shares issued through stock compensation plans, while some of the buybacks boosted earnings per share. The CFOs at the S&P 500 companies paid out a record $511.4 billion in dividends last year (*Fig. 4*). Lots of those payouts to investors were probably reinvested in the stock market.

(2) *M&A activity.* The CFOs have plenty of cash for mergers and acquisitions (M&A). Last year, global M&A activity shattered all-time records, comfortably erasing the high-water mark that was set nearly 15 years ago. Overall deal volumes in the US nearly doubled to $2.61 trillion in 2021, according to Dealogic. Dealmaking in Europe jumped 47% to $1.26

trillion, while that in the Asia Pacific region rose 37% to $1.27 trillion. M&A activity is likely to slow this year as interest rates continue to rise.

(3) *CFO Put.* Notwithstanding this slowdown, M&A, along with buybacks and dividends, should remain a significant source of support for stock market bulls. A bullish case built on these factors is what I mean by the "CFO Put." In the tug-of-war between the bulls and the bears this year, higher-for-longer inflation and Fed tightening of monetary policy will be pulling for the bears. No longer is the Fed Put viable now that the Fed has begun to tighten. The Fed Put is dead; long live the CFO Put!

(4) *Tug-of-war*. The outcome of this tug-of-war may continue to be a volatile range for the S&P 500 around the current 4400, plus or minus 400, for the next several months (*Fig. 5*). Our good friend and technical guru Joe Feshbach told us on Friday evening that he sees more of the same trading range for the stock market:

"The good news is the Nasdaq broke to new lows then reversed, suggesting a short-term low has been achieved. The S&P 500 did not make new lows; therefore, we only had three good days of put/call readings. I would've liked to have seen five great readings or at least one. The best strategy short term is to buy weakness and sell after a few days of strength."

Strategy II: The Yield-Curve Recession Question. In the past, inverted yield curves didn't cause recessions. Rather, they anticipated that if the Fed continued to raise the federal funds rate, tighter monetary policy would probably cause a financial crisis, which would lead to a widespread credit crunch, which would cause a recession (*Fig. 6*). So the federal funds rate rose above the 10-year Treasury bond yield just before recessions as investors anticipated those events. Melissa and I discussed this process in our April 2019 *Topical Study* titled "The Yield Curve: What Is It Really Predicting?"

This time, the Fed started the latest monetary policy tightening cycle on Wednesday with a measly 25bps hike in the federal funds rate, yet investors already are fretting that the yield curve is on the verge of inverting and signaling an imminent recession. Melissa and I would be inclined to agree if the Fed seemed truly committed to bringing inflation down this time. In the past, the Fed achieved that by tightening until the resulting credit crunch caused a recession, which always brought inflation down (*Fig. 7*). The Fed shows no signs that it's ready to do that anytime soon.

Besides, the "official" yield-curve spread between the 10-year yield and the federal funds rate actually has been widening since the end of the lockdown recession in early 2020. Last

week, it was 183bps, up from -55bps when the pandemic hit (*Fig. 8*). No recession signaled there. Furthermore, this spread is one of the 10 components of the Index of Leading Indicators (LEI), which rose 0.3% m/m during February remaining in recent record-high territory (*Fig. 9*). The LEI isn't signaling recession either.

Nevertheless, investors looking for a recession signal are focusing on the yield curve spread between the 10-year and 2-year Treasuries (*Fig. 10*). It has narrowed from last year's peak of 156bps during the April 2 week to just 24bps during the March 18 week of this year. We are hard pressed to see an imminent financial crisis resulting from the Fed's rate hike. Perhaps one will result from the Russian debt crisis, but we doubt that it would cause a credit crunch in the US.

MMT: Too Good To Be True. Until 2020, Modern Monetary Theory (MMT) was an offbeat school of thought that was embraced by progressive economists prior to the pandemic. It posits that any government can spend with abandon to create full employment and widespread prosperity as long as it prints its own currency. The inevitable inflationary consequence of doing so explains why mainstream economists, including even Keynesians like Harvard economist Larry Summers, mostly have rejected it. MMT's zealots countered that higher taxes could be targeted to cool inflation if necessary.

Now that the inflation genie is out of the bottle, what does the MMT playbook suggest we do about it? First, let's review how the rise of MMT led to its fall:

(1) *Pandemic's policy pandemonium.* Timing is everything, and the pandemic overnight converted MMT from a fringe idea to the raison d'être behind massive fiscal spending financed with record-high federal government deficits and with huge purchases of government securities and mortgage-backed bonds by the Fed. Why worry about inflationary consequences when the pandemic might cause a depression?

In fact, it was government-imposed lockdowns that nearly caused a depression. But policymakers won't let a good crisis go to waste (hat tip to Obama presidential adviser Rahm Emanuel, who voiced that cynical advice)—even if their policies have caused the crisis. That's because the government is here to help (hat tip to former President Ronald Reagan, who called those words the most terrifying in the English language).

From February 2020 (just before the pandemic) through February 2022, the US Treasury's marketable debt held by the public soared $6.1 trillion to a record-high $20.9 trillion (*Fig. 11*). Over this same period, the Fed's holdings of US Treasury securities increased $3.3

trillion to a then record $5.7 trillion (*Fig. 12*). The Fed also purchased $1.3 trillion in mortgage-backed securities and federal agency debt over this same period.

As a result of all these purchases by the Fed, M2 soared along with total deposits at commercial banks by $6.4 trillion to $21.8 trillion and by $4.7 trillion to $18.1 trillion from February 2020 through January 2022 (*Fig. 13*). Bank loan demand was weak because credit conditions were extremely easy in the capital markets thanks to the Fed's contribution to implementing MMT. So the banks joined the Fed in piling into Treasuries and mortgage-backed securities (*Fig. 14*).

What I call "T-Fed" (the coordinated activity of the Treasury and the Fed) followed the MMT playbook to a tee, flooding the financial markets with liquidity.

(2) *Rearing its ugly head.* MMT worked for a short while; it did stimulate a remarkable V-shaped recovery in the economy (*Fig. 15*). However, the rebound in the labor market was slower than Fed officials expected, probably because the federal government's fiscal stimulus programs included very generous unemployment supplements to the benefits provided by the states through early September 2021. As a result, the Fed continued to step on the monetary accelerator through early March 2022, even though the number of job openings started to exceed the number of unemployed workers during May 2021 (*Fig. 16*).

Unfortunately, it didn't take very long for inflation to rear its ugly head, which it hadn't done since the Great Inflation of the 1970s. The government's stimulus programs boosted consumer incomes and spending, especially on goods. The resulting demand shock overwhelmed supplies from domestic production and imports.

The CPI inflation rate, on a year-over-year basis, rose above the Fed's official 2.0% target during March 2021—one year after fiscal and monetary policymakers embraced MMT as the best way to put the economy on life support—to 7.9% during February 2022 (*Fig. 17*). Leading the way higher was the durable goods component of the CPI, which was up by a record 18.7% y/y through February 2022 (*Fig. 18*).

Widespread labor shortages boosted wage inflation. The Atlanta Fed's wage growth tracker rose from 3.7% during February 2020 to 5.8% during February 2022 (*Fig. 19*). A wage-price spiral was developing (*Fig. 20*).

Even if consumer durable goods inflation moderates in coming months, rent inflation is bound to move higher. That's because the median existing home price rose 33.4% over the

24 months through February 2022 (*Fig. 21*). Lots of first-time would-be homebuyers have been priced out of the housing market and now have no choice but to rent. As a result, demand for rental units has surged, which has caused rent inflation on new leases to soar. That's already showing up in the rent component of the CPI and will continue to do so over the coming 12-24 months (*Fig. 22*). In other words, the wage-price spiral has turned into a wage-price-rent spiral.

(3) *Professor Kelton's MMT in theory and practice.* The February 7, 2022 issue of *The New York Times* ran a *story* on Professor Stephanie Kelton, one of MMT's biggest proponents. She literally wrote the *book* on the subject in June 2020. It is titled *The Deficit Myth: Modern Monetary Theory and the Birth of the People's Economy*. The title says it all: Government deficits are the best way to help people who need help. She declared victory in March 2020, tweeting, "It took a virus to kill the deficit myth." That was her "mission accomplished" moment.

Kelton was all for the first two rounds of major fiscal stimulus in 2020, which included hundreds of billions of dollars in economic relief checks sent by the Treasury to millions of Americans. She also supported the third round in early 2021, downplaying the inflation concerns of Larry Summers.

In a July 16, 2021 Bloomberg *interview*, Kelton sided with Fed Chair Jerome Powell, who called the surge in consumer prices "transitory." She stated that "by and large" it's a sign of "growing pains of an economy that's emerging from a pandemic and reopening." Now that inflation is raging, Kelton and other proponents of MMT claim that inflation is a good problem to have if the alternative is an anemic recovery.

(4) *Bernanke's helicopter money.* MMT isn't modern, isn't monetary, and isn't a theory. It's a fancy name for "helicopter money." This term was first coined by Milton Friedman in 1969, when he mused that a central bank could always revive a weak economy by dropping money from a helicopter.

The term gained currency after then-Fed Governor Ben Bernanke referenced it in his famous 2002 preventing-deflation speech, earning him the nickname "Helicopter Ben." He explained: "A money-financed tax cut is essentially equivalent to Milton Friedman's famous 'helicopter drop' of money."

Bernanke hasn't been very vocal about his initial enthusiasm and subsequent disappointment (if any) with Washington's helicopter drop. On the other hand, Powell clearly

thought it was a fringe theory before the pandemic. In his February 26, 2019 congressional testimony on monetary policy, he disparaged MMT, rejecting the idea that the Fed would ever help combat the impact of spiraling fiscal deficits by keeping interest rates low. A year later, on March 3, 2020 after an emergency meeting of the FOMC, Powell reasserted, “So, in terms of fiscal policy, again, [that’s] not our role. We have a full plate with monetary policy. [It’s] [n]ot our role to give advice to the fiscal policymakers.”

(5) *Jerome Powell’s pivot.* What a difference a pandemic makes. Powell embraced MMT 20 days later, on Monday, March 23, 2020, when the Fed implemented an open-ended program of buying Treasury, mortgage-backed securities, and Agency debt. By the end of that week, on Friday, March 27, Congress had passed the first of several rounds of massive fiscal stimulus. That was the week that MMT triumphed as T-Fed worked to support the economy and financial markets.

(6) *Now what should we do?* MMT deserves credit for the rapid drop in the unemployment rate from a peak of 14.7% during April 2020 to just 3.8% during February 2022. But it also gets the blame for the excessively stimulative combination of fiscal and monetary policies that caused a demand shock that overwhelmed global supply chains, resulting in a shocking increase in the inflation rate to 40-year highs. The good news is that there are more job openings than workers to fill them, resulting in higher wages. The bad news is that price inflation is almost completely eroding the purchasing power of wages.

So MMT gets the credit and the blame for reviving the Philips curve, i.e., the inverse relationship between the unemployment rate and both wage and price inflation.

In her MMT primer, Kelton wrote that if the government wants to boost spending in a targeted area, it may “need to remove some spending power from the rest of us to prevent its own more generous outlays from pushing up prices.” One way to create this room is through higher taxes. Taxes are also a “powerful way for governments to alter the distribution of wealth and income.” Governments can also use taxes “to encourage or discourage certain behaviors.” Those are the words of a true-blue progressive economist.

Of course, conservatives have rejected MMT because they recognize that it provides a blank check for increased government spending and taxation. If the spending causes inflation, then raise taxes, say the progressives. That would be MMT’s prescription for dealing with today’s high rates of inflation.

(7) *Just a bad dream.* In her 2020 book, Kelton wrote: “Like Dorothy and her companions in

The Wizard of Oz, we need to see through the myths and remember once again that we've had the power all along." Kelton was referring to Dorothy's power to go back home to Kansas simply by clicking the heels of her ruby-red slippers three times. Similarly, Kelton believes that the US government has always had the power to run huge budget deficits and should be doing so to cure all our ills.

As a result of the pandemic, her theory took on a life of its own. Governments around the world spent massively on stimulative deficit-financed fiscal policies to offset the recessionary forces unleashed by the pandemic. Central bankers provided ultra-easy monetary policies to allow the resulting deficits to be financed at record-low interest rates. Now inflation is soaring.

Kelton's book leaves no doubt about what MMT is all about: It's an agenda for more big government and higher taxes. Kelton's views must strike many conservatives as unrealistic and utopian. Proponents of free market capitalism might exclaim: "Pay no attention to the professor behind the curtain!" Recall that most of "The Wizard of Oz" was a bad dream Dorothy had after getting hit on the head.

Calendars

US: **Mon:** Chicago Fed National Activity Index; Powell; Daly; Mester. **Tues:** Richmond Fed Manufacturing Index 2; API Weekly Crude Oil Inventories; Williams; Daly; Mester. (Bloomberg estimates)

Global: **Mon:** Germany PPI 1.7%m/m/26.2%y/y; Lagarde; Nagel; Lowe. **Tues:** Eurozone Current Account €24.3b; UK CBI Industrial Trends Orders 16; Japan Leading Index -1.0%; Lagarde; Guindos; Cunliffe; Lane; Panetta. (Bloomberg estimates)

Strategy Indicators

Global Stock Markets Performance (*link*): The US MSCI index registered its best weekly gain since November 2020, soaring 6.4% to 7.5% below its record high on December 27. The index ranked 12th of the 49 global stock markets we follow in a week when 43 of the 49 countries rose in US dollar terms and the AC World ex-US index gained 4.7% to 11.2%

below its June 15, 2021 record high. None of the countries traded at a record high in dollar terms during the week, but Canada came within 0.2% of its January 17 record. EMU was the best-performing region last week, with a gain of 6.8%, followed by EM Eastern Europe (6.1%), EAFE (5.5), and BRIC (4.7)—albeit without the "R," as Russia's market has not priced since March 8. The biggest underperformers, albeit with gains, were EMEA (0.8), EM Asia (3.7), and EM Latin America (4.0). The Netherlands was the best-performing country last week, rising 10.3%, followed by Ireland (9.8), Sweden (9.0), Singapore (7.9), and Austria (7.8). Among the 27 countries that underperformed the AC World ex-US MSCI last week, Sri Lanka dropped 8.9%, followed by Pakistan (-4.4), the Philippines (-1.7), Argentina (-1.5), and Colombia (-0.4). The US MSCI's ytd ranking improved to 27/49 from 31/49 a week earlier, and its 7.0% decline is now less than the 7.2% drop for the AC World ex-US. EM Latin America has risen 17.3% ytd and is the only region outperforming the AC World ex-US. The laggards: EM Eastern Europe (-79.2), EMEA (-26.3), BRIC (-15.2), EMU (-12.0), EM Asia (-9.7), and EAFE (-7.7). The best country performers so far in 2022: Peru (31.8), Chile (24.7), Brazil (22.6), Colombia (20.6), and South Africa (16.6). The worst-performing countries: Russia (-100.0), Sri Lanka (-39.0), Hungary (-21.7), Austria (-20.1), and the Netherlands (-17.4).

S&P 1500/500/400/600 Performance (*link*): All three of these indexes soared last week. LargeCap was the best performer with a gain of 6.2%, ahead of MidCap (5.3%) and SmallCap (4.2). LargeCap is now 7.0% below its record high on January 3. MidCap ended the week 7.0% below its record high on November 16, and SmallCap improved to 8.7% below its November 8 record high. Twenty-nine of the 33 sectors rose last week, up from four rising a week earlier. LargeCap Consumer Discretionary was the best performer for the week with a gain of 9.3%, followed by MidCap Tech (8.0%), LargeCap Tech (7.9), SmallCap Consumer Discretionary (7.7), and MidCap Consumer Discretionary (7.5). SmallCap and LargeCap Energy were the biggest underperformers last week with declines of 3.6%, followed by SmallCap Utilities (-1.0), MidCap Energy (-0.4), and LargeCap Utilities (0.5). In terms of 2022's ytd performance, all three indexes are down ytd. SmallCap is down 4.5% ytd, less than the declines for MidCap (-4.8) and LargeCap (-6.4). Just five of the 33 sectors are positive so far in 2022. Energy continues to dominate the top performers: SmallCap Energy (33.5), LargeCap Energy (32.4), MidCap Energy (23.9), MidCap Materials (5.5), and SmallCap Materials (0.3). The biggest ytd laggards: LargeCap Communication Services (-13.1), MidCap Consumer Discretionary (-11.0), LargeCap Tech (-10.9), LargeCap Consumer Discretionary (-10.8), and SmallCap Consumer Discretionary (-10.0).

S&P 500 Sectors and Industries Performance (*link*): Ten of the 11 S&P 500 sectors rose last week and four outperformed the composite index's 6.2% rise. That compares to a 2.9%

decline for the S&P 500 a week earlier, when just one sector rose and eight outperformed the index. Consumer Discretionary was the top performer with a gain of 9.3%, ahead of Tech (7.9%), Financials (7.1), and Health Care (6.2). The worst performers: Energy (-3.6), Utilities (0.5), Real Estate (2.7), Consumer Staples (3.8), Industrials (5.0), Materials (5.2), and Communication Services (5.8). The S&P 500 is down 6.4% so far in 2022, with one sector in positive territory and seven ahead of the index. The best performers in 2022 to date: Energy (32.4), Financials (-0.5), Utilities (-1.7), Health Care (-3.1), Industrials (-3.1), Consumer Staples (-3.9), and Materials (-5.4). The ytd laggards: Communication Services (-13.1), Tech (-10.9), Consumer Discretionary (-10.8), and Real Estate (-9.3).

S&P 500 Technical Indicators (*link*): The S&P 500 rose 6.2% last week and improved relative to its 50-day moving average (50-dma) and 200-day moving average (200-dma) for the first time in three weeks. The index closed above its 50-dma for the first time in 11 weeks, but was below its 200-dma for the eighth time in nine weeks. It had been above its 200-dma for 81 straight weeks through early February. The S&P 500's 50-dma moved lower for a tenth week, as the index improved to 0.9% above its falling 50-dma from 5.8% below its falling 50-dma a week earlier. It remains above its 23-month low of 7.5% below its 50-dma in late February. That compares to a 27-week high of 4.9% in early November and its prior 11-month low of 2.0% below in early October. The index had been mostly trading above its 50-dma since late April 2020; in June 2020, it was 11.7% above, which was the highest since its record high of 14.0% in May 2009. That compares to 27.7% below on March 23, 2020—its lowest reading since it was 29.7% below on Black Monday, October 19, 1987. The price index improved to 0.4% below its falling 200-dma from 6.1% below its falling 200-dma a week earlier. That's up from a 23-month low of 6.8% last Monday and is down sharply from 10.8% above in early November. That also compares to 17.0% above in December 2020, which was the highest since November 2009 and up from the 26.6% below registered on March 23—the lowest reading since March 2009. At its worst levels of the Great Financial Crisis, the S&P 500 index was 25.5% below its 50-dma on October 10, 2008 and 39.6% below its 200-dma on November 11, 2008.

S&P 500 Sectors Technical Indicators (*link*): Among the 11 S&P 500 sectors, four were the only ones to trade above their 50-dmas last week: Communication Services, Consumer Staples, Financials, and Tech. That's a huge improvement from a week earlier when Energy and Utilities were the only sectors above their 50-dma. However, Energy and Health Care are the only sectors with a rising 50-dma, as Health Care turned higher in the latest week. Looking at the more stable longer-term 200-dmas, Communication Services, Consumer Discretionary, and Tech were the only sectors below that measure last week as six sectors moved back above. For perspective, back in April 2020, just one sector (Health Care) was

trading above its 200-dma. Eight sectors have a rising 200-dma, up from six a week earlier as Consumer Discretionary and Financials turned up in the latest week. The three remaining members of the declining 200-dma club include Communication Services, Industrials, and Materials.

US Economic Indicators

Leading Indicators (*link*): Leading indicators edged higher in February, partially reversing January's decline, though Ataman Ozyildirim, senior director of economic research at The Conference Board, notes: "The latest results do not reflect the full impact of the Russian invasion of Ukraine, which could lower the trajectory for the US LEI and signal slower-than-anticipated economic growth in the first half of the year. The global economic impact of the war on supply chains and soaring energy, food, and metals prices—coupled with rising interest rates, existing labor shortages, and high inflation—all pose headwinds to US economic growth. While the Omicron wave and its economic impact waned in recent months, the potential for new COVID-19 variants remains." Leading indicators edged up 0.3% last month following a 0.5% decline in January—which was only its second decline since April 2020 and the first since February 2021. The LEI ended 2021 at a record high. Seven of the 10 components of the LEI rose in February, while three fell. The interest-rate spread (+0.23ppt) was the biggest positive contributor to the LEI, followed by the average workweek (+0.17), jobless claims (+0.14), and the ISM orders index (+0.13), while the leading credit index (+0.06), real core capital goods orders (+0.02), and real consumer goods orders (+0.01) were more modest contributors. Meanwhile, consumer expectations (-0.14) and stock prices (-0.13) were the biggest drags on the LEI, with building permits (-0.06) a distant third. Given all the uncertainties, the Conference Board revised its growth projection for the US economy down to 3.0% for 2022—still well above its pre-pandemic growth rate, which averaged 2.0%.

Coincident Indicators (*link*): The Coincident Economic Index (CEI) climbed to yet another record high in February, advancing for the fourth time in five months, by 0.4% m/m and 1.5% over the period, after showing no growth during August and September. All four components of the CEI contributed positively in February: 1) Employment (+0.15ppt) in February posted its strongest monthly gain since July, as the Covid-19 Omicron variant faded, with total payroll employment soaring 678,000 (vs 400,000 expected). Monthly increases for both January and December were revised higher, for a net gain of 92,000. 2) Industrial production (+0.10ppt). increased 0.5% during February to within a fraction of a

new record high, with manufacturing output posting an impressive 1.1% increase during the month. 3) Real personal income less transfer payments (+0.07) increased 0.2% in February; even though this was the first increase since the measure reached a record high in October, the advance brought it to within a few ticks of a new record high. 4) Real manufacturing & trade sales (+0.05) advanced for the fifth time in six months, up 0.3% in February and 0.8% over the period. It's within 1.5% of March 2021's record high.

Industrial Production (*link*): Output in February matched expectations, while manufacturing production posted a noticeable gain after showing little growth in each of the prior two months, with only auto output lagging. Headline production climbed for the fourth time in five months by 0.5% last month and 3.7% over the period—surpassing its pre-Covid level by 2.3% and within a fraction of a new record high. Industrial production was up 7.5% y/y, though the Fed noted that severe winter weather significantly depressed industrial activity last February and said: "A more useful comparison shows that the index has advanced a still-strong 4.2% since January 2021." Manufacturing production rebounded 1.2% in February after a 0.1% uptick in January and a 0.1% downtick in December. Meanwhile, utilities output dropped 2.7% following a weather-related surge during January; mining output was little changed last month. By market group, consumer goods production (-0.4%) ticked down after jumping 2.4% in January to its highest level since 2008, with nondurable consumer goods (-0.1) output holding steady after posting its biggest monthly gain since the early 1950s in January (+2.8). Food & tobacco production hasn't posted a decline in six months, up 0.5% in February and 3.8% over the period, while energy output dropped 2.2% after 9.5% surge in January to its highest level since November 2019. Meanwhile, consumer durable goods output remains in a volatile flat trend. Output of home electronics jumped 2.5% to a new record high, while auto production fell 3.0% in February and 4.1% during the three months through February. Production of business equipment rebounded 1.9% in February after slumping 0.6% the prior two months; February's advance brought the measure to its highest level since December 2019. Within business equipment, production of information processing equipment rebounded 1.8% to a new record high; industrial equipment increased for the fourth month, by a total of 2.9%, to its highest level since the end of 2018; and transit equipment production fell 2.3% y/y, remaining volatile.

Capacity Utilization (*link*): The headline capacity utilization rate in February jumped to its highest percentage since May 2019, with the manufacturing rate the best since September 2018. The capacity utilization rate climbed for the second month from 76.3% in December to 77.6% last month, with the rate 14.2ppts above April 2020's low of 63.4%; it's currently 1.9ppts below its long-run average. The manufacturing rate climbed to 78.0% in February from 77.1% the prior two months—2.5ppts above its pre-pandemic level and only 0.1ppt

below its long-run average. The rate for utilities slumped to 75.7% last month, following a weather-related surge from 70.7% in December to 77.9% in January, while the mining rate was little changed at 78.0%, after jumping from 74.2% in September to a 22-month high of 78.1% in January. Both rates remain well below their long-run averages.

Regional M-PMIs (*link*): Two Fed districts (New York and Philadelphia) have reported on manufacturing activity for March and show the manufacturing sector slowed for the fourth month. The composite index (to 7.8 from 9.6) slumped to a 22-month low this month and was less than a quarter of November's pace, as New York's economy contracted and Philadelphia's grew at nearly double February's pace. New York's composite index (to -11.8 from 3.1) was the weakest since May 2020's -48.5 reading at the height of the pandemic; the March reading was only its second negative one since mid-2020. Growth in the Philadelphia (27.4 from 16.0) region accelerated, though was below last March's 44.5. The new orders (7.3 from 7.8) measure remained stuck around January's 13-month low of 6.5, with New York (-11.2 from 1.4) billings also contracting at the fastest pace since May 2020, while Philadelphia's (25.8 from 14.2) accelerated at a four-month high. Meanwhile, jobs' (26.7 from 27.7) growth continued at a relatively healthy pace, with factory hirings in the Philadelphia (38.9 from 32.3) region accelerating at a record rate and those in New York (14.5 from 23.1) growing at roughly half the pace of recent highs. Turning to prices, the prices-paid measure in the New York region eased for the fourth month, from 83.0 in November to 73.8 in March, while Philadelphia's accelerated from 69.3 in February to 81.0 this month—the highest since mid-1979. New York's (56.1 from 54.1) prices-received index shot up to a new record high in March, while Philadelphia's accelerated for the second month, from 46.4 in January to 54.4 this month, though was below November's 62.9, which was close to its record high of 63.8 in the mid-1970s.

Housing Starts & Building Permits (*link*): Housing starts soared in February to its highest level since mid-2006, while building permits declined though remained above a year ago. Housing starts rebounded 6.8% last month (and 22.3% y/y) to 1.769mu (saar), more than reversing January's 5.5% weather-related plunge. Single-family starts climbed 5.6% to 1.215mu (saar), while multi-family starts were 9.3% higher at 554,000 mu—and were up 13.7% and 46.6%, respectively, from a year ago. Meanwhile, building permits sank 1.9% to 1.859mu (saar), though were up 7.7% from a year ago. Single- and multi-family permits were down 0.5% and 4.4% last month to 1.207mu and 652,000 units (saar), but were up 5.4% and 12.2% from last February. While construction is beginning on more new homes, builders are finding it difficult to finish homes already in progress. Housing completions rose 5.9% in February to 1.31mu (saar), though were down 2.8% from a year ago. "Builders are reporting growing concerns that increasing construction costs (up 20% the last 12 months)

and expected higher interest rates connected to tightening monetary policy will price prospective home buyers out of the market," according to Robert Dietz, NAHB's chief economist. Builders' sentiment is deteriorating, with NAHB's HMI dipping for the third month to 79 in March, after climbing steadily from 75 last August to 84 by the end of 2021. It was at a record high of 90 during November 2020. Of the three components of the HMI, future home sales (to 70 from 85) posted the biggest deterioration, losing 15 points, while the remaining two—current sales (86 from 90) and traffic of prospective buyers (67 from 71)—each slumped 4 points. These measures were at record highs of 89, 96, and 77, respectively, during November 2020.

Existing Home Sales (*link*): "Housing affordability continues to be a major challenge, as buyers are getting a double whammy: rising mortgage rates and sustained price increases," said Lawrence Yun, NAR's chief economist. "Monthly payments have risen by 28% from one year ago—which interestingly is not a part of the consumer price index—and the market remains swift with multiple offers still being recorded on most properties." Existing home sales continues its seesaw pattern, dropping 7.2% in February to a six-month low of 6.02mu (saar) after a 6.6% gain and a 3.8% loss the prior two months. Single-family sales sank 7.0% to 5.35mu (saar) after jumping 6.3% and sliding 3.9% the prior two months, with multi-family sales following a similar pattern, dropping 9.5% to 670,000 units, following an 8.8% increase and a 2.9% decrease. Sales fell in all four regions during February, though the South was the sole region with prices above a year ago: South (-5.1%m/m & +3.0%y/y), West (-4.7 & -8.3), Midwest (-11.3 & -1.5), and Northeast (-11.5 & -12.7). Total inventory increased to 870,000 units last month after sinking to a record-low 850,000 units during January, down 15.5% y/y. Unsold inventory was at a 1.7 months' supply in February, up from a record low of 1.6 months in January though down from 2.0 the months' supply last February. The median existing home price was up 15.0% y/y, with prices rising in all regions. Yun notes, "The sharp jump in mortgage rates and increasing inflation is taking a heavy toll on consumer savings. However, I expect the pace of price appreciation to slow as demand cools and as supply improves somewhat due to more home construction."

Global Economic Indicators

Eurozone CPI (*link*): The headline CPI rate accelerated for the eighth month, from 1.9% last June to a record-high 5.9% y/y this February. The rate was at -0.3% at the end of 2020. Looking at the main components, once again energy recorded the largest gain, accelerating for the 14th time in 15 months to a record-high 32.0% y/y, up from -8.3% in November

2020. The rate for food, alcohol & tobacco climbed to 4.2% y/y in February (the highest since October 2008), rising steadily from June 2021's 0.5%, while the rate of non-energy industrial goods increased 3.1%—the highest since early 1990s. The services rate climbed to 2.5% y/y last month after slowing the prior two months from 2.7% in November (the highest since summer 2008) to 2.3% in January. Of the top four Eurozone economies, rates for Spain (7.6% y/y), and Italy (6.2) were above the Eurozone's 5.9% pace, while the rates for Germany (5.5) and France (4.2) were below—with France's the lowest of the Eurozone economies' rates.

Contact us by *email* or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-497-5306
Melissa Tagg, Director of Research Projects & Operations, 516-782-9967
Mali Quintana, Senior Economist, 480-664-1333
Jackie Doherty, Contributing Editor, 917-328-6848
Valerie de la Rue, Director of Institutional Sales, 516-277-2432
Mary Fanslau, Manager of Client Services, 480-664-1333
Sandy Cohan, Senior Editor, 570-228-9102

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