MORNING BRIEFING
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Switching Planets: Investors Now From Venus, Analysts From Mars

Check out the accompanying chart collection.

Executive Summary: We've been making the case that the latest bear market might have bottomed on June 16. So far, so good. ... Just a few weeks back, industry analysts' earnings estimates suggested they were oblivious to investors' recession fears, and we quipped that the former was from Venus, the latter from Mars. Now it's investors interpreting news with a rosy bias as analysts shave their estimates. … The stock market now appears to be discounting investors' recent hopes of peak inflation, peak Fed hawkishness, and a mild recession. … Also: We examine Powell's suggestion that monetary policy is nearly restrictive. … And: The Bond Vigilantes are from Venus now too.

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Strategy I: Trading Places. Since our June 24 *QuickTakes*, we've been making the case that the bear market in the S&P 500 might have ended on June 16, when it was down 23.6% to 3666 from its record high of 4796 on January 3. We wrote: "[S]entiment indicators were so bearish that they were bullish. … On a fundamental basis, we've noted that commodity prices are showing signs of peaking, suggesting that inflation may be doing the same. Bond market indicators have also turned more bullish recently. For now, we see the 3666 level as a possible bear-market bottom."

So far, so good. The S&P 500 is up 12.6% since June 16 through Friday's close (*Fig. 1*). It is down only 13.9% from its record high. So far, it has remained in bear-market territory—i.e., with a decline of 20% or more—for only 21 calendar days of the 207 days since its record high. If June 16 marked the bottom, then the index bottomed 164 days into the latest bear market (*Fig. 2*). Let's have a closer look at the recent happy developments:

(1) *Different planets.* Here is the performance derby of the 11 sectors of the S&P 500 since June 16 through Friday's close and during the bear market from January 3 through June 16 (sorted by the former): Consumer Discretionary (21.8%, -36.4%), Information Technology (17.2, -30.2), Real Estate (14.8, -24.9), Utilities (13.7, -8.3), S&P 500 (12.6, -23.6), Industrials (11.8, -18.6), Health Care (10.7, -14.4), Financials (9.6, -22.4), Consumer

Staples (8.2, -11.2), Communication Services (6.4, -32.7), Materials (4.7, -16.5), and Energy (1.8, 35.0). (See *Table 1* and *Table 2*.)

That's quite a reversal of fortune among the 11 sectors of the S&P 500. Similarly, industry analysts and investors seem to have traded places. During the bear market, Joe and I maintained that industry analysts were from Venus, while investors were from Mars. The former didn't seem to have a care in the world and kept raising their estimates for the revenues and earnings of the S&P 500 companies for 2022 and 2023. At the same time, investors, fearing a recession caused by the Fed's tightening of monetary policy to fight inflation, slashed the valuation multiples they were willing to pay for what they deemed to be the delusional earnings estimates provided by the analysts.

(2) *Analysts from Mars.* In the past couple of weeks, we've observed that analysts may finally have started to shave their estimates to reflect the mild recession that occurred during the first half of this year, with real GDP falling modestly during Q1 and Q2 (*Fig. 3*). S&P 500 forward earnings—i.e., the time-weighted average of analysts' consensus earnings estimates for this year and next year—rose 7.5% since the start of this year to a record high during the week of July 7 as the analysts raised their 2022 and 2023 estimates. They've been cutting their annual estimates for the past five weeks through the July 21 week, so forward earnings has flattened around $239 per share.

(3) *Investors from Venus.* Meanwhile, since June 16, investors seem to have concluded that they might have been too bearish about the outlook for both Fed policy and earnings. The S&P 500's forward P/E, which started the year at 21.4, bottomed at 15.3 on June 16 and was back up to 17.2 on Friday (*Fig. 4*).

Previously, we had observed that the June 16 low coincided with the peak of the S&P GSCI commodity price index on June 8 and the peak of the 10-year Treasury bond yield on June 14, at 3.48%. After June's worse-than-expected CPI came out on July 13, we observed that the market had held up well compared to the dive it took when May's number was released on June 10. That suggested to us that the market was starting to discount the possibility that June's CPI might have marked peak inflation, as we discussed in our July 12 *QuickTakes* titled "Will June's CPI Inflation Rate Be the Peak?"

(4) *Feshbach on the market.* I checked in with my friend Joe Feshbach on his latest market call. We seem to be on the same planet lately. In his opinion: "Sentiment indicators proved reliable once again. Nasdaq breadth was a bit shaky Friday so that could lead to temporary profit-taking. However, the put/call ratios I monitor showed skepticism on the rally which

should be a nice clue that the market will work its way higher after any pullback."

Strategy II: The Fed Is From Outer Space. In addition to discounting peak inflation, the market seems to have discounted peak Fed hawkishness last week on Wednesday afternoon during Fed Chair Jerome Powell's *press conference* right after the FOMC voted to hike the federal funds rate by 75bps to a range of 2.25%-2.50%. Consider the following:
(1) *Neutral debate.* In his brief prepared remarks, Powell started out saying: "My colleagues and I are strongly committed to bringing inflation back down, and we are moving expeditiously to do so. … It is essential that we bring inflation down to our 2% goal if we are to have a sustained period of strong labor market conditions that benefit all." He reiterated that the Fed remains on course to "significantly reducing the size of our balance sheet."

Then, in his unscripted remarks, he responded to a reporter asking "how far into restrictive territory rates may need to go?" He said, "[W]e've been saying we would move expeditiously to get to the range of neutral. And I think we've done that now. We're at 2.25 to 2.50, and that's right in the range of what we think is neutral." Apparently, his suggestions that the Fed is on the borderline of restrictive territory and therefore closer to being done tightening were all it took to move more investors from Mars to Venus.

On Friday, former Treasury Secretary Lawrence Summers *accused* Powell of coming from outer space. He said that the Fed is engaging in "wishful thinking" similar to the Fed's delusion last year that inflation would be transitory. He accused Powell of saying things "that, to be blunt, were analytically indefensible." He added, "There is no conceivable way that a 2.5% interest rate, in an economy inflating like this, is anywhere near neutral." Former Federal Reserve Bank of New York President William Dudley said on Wednesday that, given the level of uncertainty, "I'd be a bit more skeptical" in saying policymakers had reached neutral.

(2) *Safe passage.* Investors were also delighted to hear Powell say, "We're not trying to have a recession. And we don't think we have to. We think there's a path for us to be able to bring inflation down while sustaining a strong labor market ... along with—in all likelihood—some softening in labor market conditions. So … that's what we're trying to achieve, and we continue to think that there's a path to that."

However, he reiterated that "restoring price stability is just something that we have to do. There isn't an option to fail to do that." Investors clearly chose to cherry-pick Powell's dovish comments and ignore his hawkish ones, now that they are on Venus.

(3) *No more guidance.* Apparently, investors were also happy that Powell said that the Fed's decisions going forward will be totally data dependent, and the Fed will no longer provide forward guidance (until further notice): "In terms of September, we're going to watch the data and the evolving outlook very carefully. … I'm not really going to provide any specific guidance about what that might be. But I mentioned that we might do another unusually large rate increase, but that's not a decision that we've made at all."
Again, investors chose to interpret that as leading to a happy potential outcome, namely, that the data will show weakening economic activity and peaking inflation, thus bringing the Fed's monetary policy tightening cycle to an end sooner rather than later.

(4) *Playbook from Venus.* Powell did offer a bit of guidance. He said, "And I think you can still think of the destination as broadly in line with the June SEP. Because it's only six weeks old."

"SEP" stands for the "Summary of Economic Projections," which shows the consensus forecasts of the FOMC participants for the federal funds rate, the unemployment rate, real GDP, headline PCED inflation, and core PCED inflation. Back in June, they expected the federal funds rate would be raised to 3.40% by the end of this year and 3.80% by the end of next year. (See our *FOMC Economic Projections*.)

According to the SEP, that's restrictive enough to bring inflation down but without causing a recession. More specifically, real GDP is expected to grow 1.7% this year and next year, with the unemployment rising to only 3.9% next year. The PCED inflation rate is expected to fall from 5.2% this year to 2.6% in 2023 and 2.2% in 2024.

On Venus, there are only happy endings.

Credit: The Bond Vigilantes Are From Venus Too. Joining stock investors on Venus are the Bond Vigilantes. Consider the following:

(1) *Bullish indicators.* As noted above, the US Treasury bond yield peaked this year (so far) at 3.49% on June 14, falling to 2.67% on Friday. That's surprising given that inflation remains so high. But we aren't surprised. As we've pointed out before, the bond yield closely tracks the copper/gold price ratio and the Citigroup Economic Surprise Index (*Fig. 5* and *Fig. 6*). Both remain bullish for the bond market, with the copper/gold price ratio signaling that the yield should be closer to 2.00%.

(2) *The dollar, QT2 & the yield curve.* As we noted in last Tuesday's *Morning Briefing*, the

strong dollar combined with the Fed's intention to proceed with QT2 may be equivalent to a hike in the federal funds rate of at least 100bps. The Fed's critics seem to overlook this important point. A 2.50% federal funds rate in fact may be at the neutral rate under the circumstances!

This view is corroborated by the inversion of the yield curve. The yield spread between the 10-year and 2-year US Treasury notes turned negative on July 6 and was down to -22bps on Friday (*Fig. 7*). That certainly is signaling that bond investors believe that interest rates are already high enough to weaken economic growth and bring inflation down.

The 2-year yield—which tends to be an indicator of the market's expectations for the federal funds rate over the next 12 months—peaked this year at 3.45% on June 14 (*Fig. 8*). It was down to 2.89% on Friday. It currently implies "one and done," i.e., that one more federal funds rate hike of 50bps to a range of 2.75%-3.00% in September should be the end of the Fed's rate hiking.

That may seem absurdly low to the Fed's critics, but they've been ignoring the restrictive impact of the strong dollar and QT2. Fed officials undoubtedly have run their econometric model to determine the equivalence of these restrictive developments to the magnitude of a rate hike. They should share that information with the public.

(3) *Flow of funds.* The rally in the bond market has been especially impressive given that bond mutual funds experienced net withdrawals of $83.2 billion over the past 12 months through June (*Fig. 9*). That may be a good contrary indicator given that investors piled into these funds at a record 12-month pace of $766 billion during April 2021, the worst possible time to be buying bonds as it turned out.

Previously, we observed that net capital inflows into the US from abroad added up to $1.3 trillion over the 12 months through May (*Fig. 10*). Over that same period, private foreigners' net purchases of US bonds was $796.8 billion (*Fig. 11*). On the other hand, foreign investors sold $162.4 billion in US equities, on balance, over this same period.

(4) *TINAC.* The above suggests that global investors have concluded that the US represents a safe haven for their money in a world that's going mad. Their mantra is "there is no alternative country" (TINAC). That explains why the dollar has been so strong since the start of this year, as they've been buying lots of US bonds. Now they may also be buying US stocks. If not, their bond purchases certainly have helped to lower the bond yield here, which seems to be providing support for valuation multiples in the stock market.

Inflation: Hopefully Peaking. So is inflation peaking or not? There are mounting signs that it is peaking, but not enough of them to be certain. It didn't peak in June, as the headline PCED inflation rate rose to 6.8%, the highest since January 1982 (*Fig. 12*). The core inflation rate was 4.8%. We are still predicting that the headline rate will moderate to 4%-5% during H2. We should see it get closer to this range when July's PCED is released on August 26 for the following reasons:

(1) *Food & energy.* Agricultural commodity prices dropped during July, suggesting some moderation in food inflation, which was 11.2% y/y during June in the PCED (*Fig. 13*). The same can be said about energy inflation, with the exception of natural gas prices, which moved higher in July. The energy component of the PCED was up a whopping 43.5% y/y during June.

(2) *Core inflation.* The three-month annualized inflation rates for both durable and nondurable goods (excluding food and energy) moderated significantly through June (*Fig. 14*). Retailers have been forced to liquidate their bulging inventories by slashing their prices. We also expect to see further weakness in the prices of household furniture and appliances as a result of the housing recession (*Fig. 15*).

Debbie and I anticipated that some of the progress likely to be made in durable and nondurable goods inflation will be offset by the rent components of the PCED services sector. Sure enough, rent of primary residence and owners' equivalent rent are rising at faster rates, of 5.8% and 5.4% y/y through June (*Fig. 16*). The comparable three-month annualized rates are even higher at 7.9% and 7.1%.

(3) *Employment costs.* In his presser, Fed Chair Powell said that among the more important inflation indicators is the Employment Cost Index (ECI). It came out on Friday, and it showed no signs of peaking. The ECI inflation rate continued to move higher during Q2 with a gain of 5.5% y/y, led by a 5.7% increase in wages and salaries, while benefits rose 5.3% (*Fig. 17*).

The wage-price-rent spiral was still spiraling through June.

Calendars

US: Mon: ISM M-PMI & Price Index 52.0/74.3; Construction Spending 0.2%. **Tues:** Job Openings 11.00m; API Weekly Crude Oil Inventories; Bullard. (Bloomberg estimates)

Global: Mon: Eurozone, Germany, France, Italy, and Spain M-PMIs 49.6/49.2/49.6/49.1/50.2; Eurozone Unemployment Rate 6.6%; Germany Retail Sales 0.2%m/m/-8.0%y/y; UK M-PMI 52.2. **Tues:** Spain Unemployment Rate; Spain Consumer Confidence; UK Nationwide HPI 0.5%; RBA Interest Rate Decision 1.85%; China Caixin NM-PMI. (Bloomberg estimates)

Strategy Indicators

Global Stock Markets Performance (*link*): The US MSCI index rose 4.2% last week as the index moved further away from bear market territory again to end the week at 15.0% below its record high on December 27. The US MSCI ranked seventh of the 48 global stock markets that we follow in a week when 40 countries rose in US dollar terms. The AC World ex-US index rose 1.7% for the week, but remained in a bear market at 20.7% below its June 15, 2021 record high. Most regions rose last week, but EM Latin America was the best performer, with a gain of 7.0%, followed by EMU (2.6%) and EAFE (2.1). BIC (-0.6) was the worst performing region last week, followed by EM Asia (-0.4), EM Eastern Europe (0.0), and EMEA (1.0). Argentina was the best-performing country last week with a gain of 17.8%, followed by Brazil (9.7), Norway (6.7), Colombia (6.2), and Italy (5.3). Among the 22 countries that underperformed the AC World ex-US MSCI last week, Pakistan's 4.3% decline was the worst, followed by China (-3.7), Hungary (-3.0), and Morocco (-2.1). In July, the US MSCI rose 9.2% for its first gain in four months and its biggest since November 2020. The US MSCI ranked 4/48 in July and easily outperformed the 3.2% gain for the AC World ex-US index as 35 of the 48 countries moved higher. Chile was the best performer, with a gain of 12.4%, followed by Sweden (11.3), the Netherlands (10.4), the US (9.2), and India (9.2). The worst-performing countries in July: Pakistan (-17.2), China (-10.0), Morocco (-4.0), Hong Kong (-3.7), and the Czech Republic (-2.4). EAFE was the best-performing region in July with a gain of 4.9%, ahead of EMU (4.6), EMEA (4.3), EM Latin America (4.2), and the AC World ex-US (3.2). BIC (-4.0) was July's worst-performing region, followed by EM Asia (-1.8) and EM Eastern Europe (-1.2). The US MSCI's ytd ranking rose two places w/w to 23/49. The US MSCI's ytd decline of 14.5% is now less than the 17.1% drop for the AC World ex-US. EM Latin America is down 0.1% ytd and is the only region outperforming

the AC World ex-US. The laggards: EM Eastern Europe (-83.9), EMEA (-32.7), EMU (-23.3), BIC (-21.5), EM Asia (-19.6), and EAFE (-17.1). The best country performers so far in 2022: Jordan (24.9), Chile (20.2), Brazil (3.3), Indonesia (0.7), and Portugal (-1.7). Apart from Russia, in which investors have lost 100.0% of their investment this year, here are the worst-performing countries ytd: Sri Lanka (-68.3), Pakistan (-45.2), Hungary (-42.1), Egypt (-39.5), and Poland (-35.4).

S&P 1500/500/400/600 Performance (*link*): All three of these indexes rose for a second straight week and ended the week out of a bear market. LargeCap's latest gain of 4.3% had the index finish at 13.9% below its record high on January 3. MidCap jumped 4.8% to end the week 13.7% below its record high on November 16, while SmallCap rose 4.6% to finish at 15.4% below its November 8 record high. All 33 sectors moved higher for the week, up from 29 sectors rising a week earlier. SmallCap Energy was the best performer with a gain of 18.0%, followed by MidCap Energy (10.7%), LargeCap Energy (10.3), MidCap Materials (7.1), and MidCap Industrials (7.1). SmallCap Consumer Discretionary (0.5) was the biggest underperformer last week, followed by LargeCap Consumer Staples (1.6), SmallCap Consumer Staples (1.7), LargeCap Health Care (2.0), and MidCap Health Care (2.2). During July, LargeCap soared 9.1%, but that was less than the gains for MidCap (10.7) and SmallCap (9.9). All 33 sectors rose in July, up from just one sector rising in June, which was the lowest count since February 2020. July's best performers: LargeCap Consumer Discretionary (18.9), MidCap Energy (16.1), SmallCap Energy (14.1), MidCap Tech (13.7), and MidCap Industrials (13.7). July's biggest laggards: SmallCap Consumer Staples (2.1), SmallCap Utilities (3.0), LargeCap Consumer Staples (3.1), LargeCap Health Care (3.2), and LargeCap Communication Services (3.5). In terms of 2022's ytd performance, LargeCap, with a 13.3% decline, continues to trail SmallCap (-11.5) and MidCap (-11.6). Just five of the 33 sectors are positive so far in 2022, up from three a week earlier. Energy continues to dominate the top performers: SmallCap Energy (42.4), LargeCap Energy (41.6), MidCap Energy (34.5), MidCap Utilities (3.6), and LargeCap Utilities (3.3). The biggest ytd laggards: LargeCap Communication Services (-28.0), SmallCap Consumer Discretionary (-24.4), SmallCap Real Estate (-20.6), LargeCap Consumer Discretionary (-20.4), and MidCap Consumer Discretionary (-19.8).

S&P 500 Sectors and Industries Performance (*link*): All 11 S&P 500 sectors rose last week and six outperformed the composite index's 4.3% gain. That compares to a 2.5% gain for the S&P 500 a week earlier, when eight sectors rose and seven outperformed the index. Energy was the top performer with a gain of 10.3%, followed by Utilities (6.5%), Industrials (5.7), Consumer Discretionary (5.5), Tech (5.1), and Real Estate (4.9). The worst performers, albeit with gains: Consumer Staples (1.6), Health Care (2.0), Communication

Services (2.5), Financials (2.9), and Materials (4.1). After tumbling 8.4% in June, the S&P 500 soared 9.1% in July for its best monthly performance since November 2020 and its best July since 1939. All 11 sectors moved higher during July and four outperformed the broader index. That compares to all 11 falling and six beating the S&P 500's 8.4% decline in June. The leading sectors in July: Consumer Discretionary (18.9), Tech (13.5), Energy (9.6), and Industrials (9.5). July's laggards, albeit with gains: Consumer Staples (3.1), Health Care (3.2), Communication Services (3.5), Utilities (5.4), Materials (6.1), Financials (7.0), and Real Estate (8.5). The S&P 500 is down 13.3% so far in 2022 with five sectors ahead of the index and just two in positive territory. The best performers in 2022 to date: Energy (41.6), Utilities (3.3), Consumer Staples (-3.9), Health Care (-6.2), and Industrials (-9.7). The ytd laggards: Communication Services (-28.0), Consumer Discretionary (-20.4), Tech (-17.4), Real Estate (-14.6), Financials (-13.8), and Materials (-13.7).

S&P 500 Technical Indicators (*link*): The S&P 500 jumped 4.3% last week and improved relative to its 50-day moving average (50-dma) and its 200-day moving average (200-dma). The index closed above its 50-dma for a second straight week after 14 weeks below, but closed below its 200-dma for the 23rd time in 25 weeks. It had been above its 200-dma for 81 straight weeks through early February. The S&P 500's 50-dma moved higher for the first time in 16 weeks as the index improved to a 15-month high of 5.4% above its rising 50-dma from 1.2% above its falling 50-dma a week earlier. That's up from a 27-month low of 11.1% below its falling 50-dma in mid-June. The index had been mostly trading above its 50-dma from late April 2020 to early April 2022; 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 closed Friday at 4.8% below its falling 200-dma, up from 9.0% below a week earlier and from a 26-month low of 17.1% below its falling 200-dma in mid-June. The latest reading is down sharply from 10.8% above its rising 200-dma in early November. That compares to 17.0% above in December 2020, which was the highest since November 2009 and up from the 26.6% below registered during the Great Virus Crisis on March 23, 2020—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. The 200-dma declined for a 14th straight week.

S&P 500 Sectors Technical Indicators (*link*): All 11 S&P 500 sectors traded above their 50-dmas last week for the first time since the end of March. That's up from six a week earlier and an improvement from the two weeks before the end of June when all 11 sectors were below. Health Care was above for a fifth week as Consumer Discretionary, Consumer

Staples, and Tech each marked their third straight week above. Eight of the 11 sectors had a rising 50-dma, up from three a week earlier. Communication Services, Energy, and Materials are the only sectors with a falling 50-dma. Looking at the more stable longer-term 200-dmas, Health Care and Utilities moved back above in the latest week and joined Energy, which was above for a 45th straight week. For perspective, at the depths of the Great Virus Crisis in April 2020, Health Care was the only sector trading above its 200-dma. Four sectors have a rising 200-dma, unchanged from a week earlier. Consumer Staples, Energy, Health Care and Utilities.

US Economic Indicators

GDP (*link*): Real GDP fell for the second consecutive quarter, contracting 0.9% (saar) last quarter following a 1.6% drop during Q1. Gross private domestic investment—which includes nonresidential investment, residential investment, and the change in inventories—plummeted 13.5% (saar) during Q2, as the change in inventory investment slowed considerably to $81.6 billion (saar) from $188.5 billion during Q1, while residential investment plunged 14.0%. (Real final sales, which excludes inventory investment, expanded 1.1%.) Meanwhile, real nonresidential expenditures (-0.1%, saar) were flat last quarter following a double-digit gain during Q1, as a 9.2% (saar) increase in spending on intellectual property products last quarter was offset by declines in spending on structures (-11.7) and equipment (-2.7). Real government spending was also a drag on growth, contracting 1.9% (saar)—with both federal (-3.2) and state & local government (-1.2) expenditures contracting. Meanwhile, real consumer spending increased 1.0% (saar), the weakest showing since the Q2-2020 contraction during the pandemic, as real spending on services expanded 4.1% (saar), more than offsetting the 4.4% drop in goods consumption—with spending on both nondurable (-5.5) and durable (-2.6) goods in the red. Trade was a positive, with the real net exports deficit narrowing from $1.54 trillion during Q1 to $1.47 trillion during Q2 as exports expanded 18.0% while imports rose 3.1% (an increase in imports is a subtraction from GDP in calculations).

Contributions to GDP Growth (*link*): Real Inventory was the biggest negative contributor to real GDP during Q2, while trade was the biggest positive contributor. Inventory investment subtracted 2.01ppts from Q2 real GDP—virtually all nonfarm (-1.96). Also dragging growth lower last quarter was real residential investment (-0.71) and government spending (-0.33)—with both federal (-0.20) and state & local (-0.13) governments contributing to the decline. Meanwhile, trade (+1.43) gave a boost to Q2 growth, driven by

exports (+1.92), which more than offset the negative contribution from imports (-0.49). Consumer spending (+0.70) also added to growth, but it was a mixed bag, with spending on services (+1.78) more than offsetting the negative contribution from goods spending (-1.08) and nondurable goods (-0.85) consumption accounting for most of the drop. Meanwhile, real nonresidential investment (-0.01) was neutral, with structures (-0.32) and equipment (-0.16) spending subtracting from growth while spending on intellectual property products (+0.47) contributed positively to growth.

Personal Consumption Deflator (*link*): June's PCED advanced 1.0%, the largest one-month gain since September 2005, while core prices rose 0.6%, double the average 0.3% increase the first five months of this year. The yearly headline rate climbed to 6.8% in June, its highest reading since January 1982; it was at 4.0% a year ago. The yearly core rate ticked up to 4.8% after easing from 5.3% in February (highest since spring 1983) to 4.7% in May. On a three-month annualized basis, the core rate heated up to 5.1%, surpassing June's yearly rate of 4.8%. Prices for durable goods rose 4.2% (saar) over the three months through June, accelerating from 1.0% and -1.1% the prior two months, while core nondurable goods prices rose 0.8% (saar) during the three months ending June, up from -0.1 in May. Meanwhile, services prices ex energy accelerated for the third month, to 5.4% during the three months through June from 4.0% during March and February. The three-month annual rates for both consumer durable (4.2% & 6.1%) and consumer core nondurable (0.8 & 3.0) goods were below their yearly rates, while the core services price (5.4 & 4.5) was above. *PCED components for which three-month rates lag yearly rates:* household appliances (-8.8 & 7.8), sports & recreational vehicles (-2.5 & 2.3), lodging away from home (-1.4 & 10.7), prescription drugs (0.0 & 2.4), clothing & footwear (2.8 & 5.0), furniture & home furnishings (3.6 & 11.0), recreation services (4.8 & 5.1), professional & other services (6.4 & 7.2), tobacco (7.3 & 7.9), new motor vehicles (10.9 & 11.6), motor vehicles & parts (11.0 & 13.1), and gasoline & other energy products (36.7 & 61.6). *PCED components for which three-month rates exceed yearly rates:* airfares (56.4 & 29.8), transportation services (24.5 & 11.5), food & nonalcoholic beverages purchased for off-premise consumption (14.7 from 12.7), personal care products (6.4 & 4.2), tenant rent (7.9 & 5.8), owner-occupied rent (7.1 & 5.4), alcoholic beverages purchased for off-premise consumptions (4.3 & 3.0), education services (3.3 & 2.2), video audio & information processing (1.0 & -1.4), hospitals (4.8 & 3.5), education services (3.3 & 2.2), and car & truck rental (1.2 & -9.5). *PCED components with comparable three-month and yearly rates:* food services & accommodations (6.7 & 6.7), used motor vehicles (4.1 & 4.2), and physician services (0.5 & 0.3).

Personal Income & Consumption (*link*): Both personal income and spending rose more

than expected in June, though both were boosted by higher prices. Personal consumption expenditures jumped 1.1% in June, but barely budged when adjusted for inflation, ticking up only 0.1%. Real goods consumption was little changed in June, up 0.1%, after falling three of the prior four months by 2.4%—with nondurable goods consumption sliding for the fifth consecutive month, by 0.4% in June and 2.6% over the period. Real durable goods spending climbed 0.9% after a 3.2% loss and a 1.5% gain the prior two months. Meanwhile, real services consumption continues to set new record highs, climbing 0.1% in June and 1.9% ytd—not posting a decline since February 2021. Turning to income, nominal personal income rose 0.6% while real personal income contracted 0.3%—posting its third decline this year. Versus a year ago, the former is up 5.7% while the latter is down 1.0%. Meanwhile, nominal wages & salaries continued its record-setting pattern, increasing for the 25th month since bottoming in April 2020; it was up 0.5% m/m and 30.0% over the period. In real terms, wages and salaries dropped 0.5% this month, its second decline this year, with the measure also posting two months of gains and two months of no growth—and is flat ytd. The yearly rate slowed to 3.3% from 6.1% in February; it was less than half last June's 7.4% pace.

Consumer Sentiment Index (*link*): Consumer sentiment in July barely budged from June's record low, as most components of the index barely budged, though buying conditions for durables improved as supply constraints eased. "The one-year economic outlook fell to its lowest reading since 2009," said Surveys of Consumers Director Joanne Hsu. "At the same time, concerns over global factors eased somewhat. The Consumer Sentiment Index (CSI) ticked up to 51.5 in July after sliding five of the prior six months—from 70.6 in December to a new record low of 50.0 in June. Expectations plummeted 21.0 points ytd—from 68.3 in December to 47.3 in July—the lowest reading since spring 1980. Meanwhile, the present situation component increased for the second time this year, climbing 4.3 points in July to 58.1, after dropping 20.4 points the first half of this year to 53.8—a record low for the series going back to the early 1950s. The expected inflation rate ticked down to 5.2% in July from 5.3% in May and June and a recent high of 5.4% in both March and April. It was at 2.5% at the end of 2020. The five-year rate eased to 2.9% from a recent high of 3.1% in June and January.

Employment Cost Index (*link*): Compensation for private industry workers is increasing at a rapid rate, though adjusting for inflation workers' compensation is falling. Compensation continued to accelerate during Q2, rising 5.5% y/y—the highest since mid-1984—from a recent low of 2.4% during Q3-2020, with the yearly increase in wages & salaries up 3.0ppts (to 5.7% from 2.7% y/y) and benefits up 3.3ppts (5.3 from 2.0) over the comparable period. In real terms, however, compensation is down 3.3% y/y, with wages & salaries and benefits falling 3.3% and 3.5%, respectively. Focusing on nominal wages & salaries, service-

providing firms boosted wages by 5.9% y/y, while goods-producing wages were up 4.7%. Here's a list of yearly increases in wages & salaries by industry from highest to lowest: leisure & hospitality (8.2% y/y), retail trade (7.8), wholesale trade (6.9), health care & social assistance (6.0), professional & business services (5.4), manufacturing (4.9), education services (4.7), financial activities (4.6), construction (4.4), transportation & warehousing (4.3), information services (4.3), and utilities (3.4).

Regional M-PMIs (*link*): Five Fed districts (New York, Philadelphia, Dallas, Richmond, and Kansas City) now have reported on manufacturing activity for July and show the manufacturing sector is in contractionary territory for the third month, though the reading is just below the breakeven point. The composite index improved a bit, ticking up to -2.2 after falling the prior three months from 15.1 in April to -3.8 in June. Regionally, it was a mixed bag. Activity in the New York (to 11.1 from -1.2) region swung from negative to positive this month, while Kansas City's (13.0 from 12.0) held steady—not showing negative growth since the height of the pandemic. Meanwhile, the Richmond (0.0 from -9.0) region returned to the break-even level after contracting for two months, while activity in both the Philadelphia (-12.3 from -3.3) and Dallas (-22.6 from -17.7) factories dropped further into contractionary territory. July orders (-8.0 from -8.5) contracted at roughly the same pace as June orders, which was the first negative reading since May 2020. Billings in the Philadelphia (to -24.8 from -12.4) region contracted at double June's rate, while Dallas' (-9.2 from -7.3) were slightly more negative, and Kansas City's (-2.0 from -8.0) less negative. Meanwhile, orders growth in the Richmond (-10.0 from -20.0) area fell at half June's pace, while New York's (6.2 from 5.3) held at a steady pace. Employment (16.1 from 19.3) slowed a bit but continued its strong readings, with a solid pace of hirings by factories in the Philadelphia (19.4 from 28.1), New York (18.0 from 19.0), Dallas (17.9 from 15.2), and Kansas City (17.0 from 18.0) regions; in Richmond (8.0 from 16.0), hirings mirrored orders growth in falling at half June's pace.

Regional Prices Paid & Received Measures (*link*): We now have prices-paid and -received data for July from the New York, Philadelphia, Richmond, Dallas, and Kansas City regions, and all are showing a noticeable easing of inflationary pressures. (Note: The New York, Philadelphia, Dallas, and Kansas City 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 fell sharply in July to 64.2 after holding in a volatile flat trend between 80.0 and 88.5 since mid-2021. Regionally, the prices-paid measure in the New York region slowed to 64.3, the lowest since last February, down from April's record-high 86.4, while Philadelphia's gauge eased for the third month to an 18-month low of 52.2 from April's cyclical high of 84.6—which

wasn't far from its record high of 91.1 in the mid-1970s. Dallas saw its prices-paid measure sink to a 20-month low of 38.4 this month, slowing sharply from November's record-high 83.3, while Kansas City's plummeted to 41.0 in July from 71.0 in June and a record high of 88.0 last May. Prices-paid in the Richmond region eased for the second month to 124.9 from May's record-high 150.1. Turning to prices-received, it eased to a 15-month low of 43.2 in July from a recent peak of 60.6 in March. New York's measure slowed for the fourth month in July, from a record-high 56.1 in March to a 16-month low of 31.3, while Philadelphia's is at 30.3, down from November's cyclical high of 62.9. Dallas' eased to a 17-month low of 29.3 from its record-high 50.9 in October, while Kansas City's dropped to 36.0 from April's record-high 57.0. Meanwhile, Richmond's eased to 89.2 from June's record high of 103.1.

Global Economic Indicators

Eurozone Economic Sentiment Indicators (*link*): The Economic Sentiment Indexes (ESI) for the EU and Eurozone continued to plummet in July, with ESIs for both the EU (-4.2 points to 97.6) and Eurozone (-4.5 to 99.0) posting sizeable declines, falling to their lowest levels since January 2021 and February 2021, respectively. The EU's ESI is down 18.6 points since its recent peak of 116.2 in October, while the Eurozone's is 19.0 points lower than its 118.0 peak last July. ESIs dropped in four of the six largest EU economies, with Spain (-5.0 points to 97.1) and Germany (-4.9 to 99.8) taking the biggest hits, followed by Italy (-3.4 to 101.6) and Poland (-3.2 to 92.5). ESIs for France (-0.1 to 102.3) and the Netherlands (+0.2 to 99.3) were stable. For the overall EU at the sector level, consumer confidence remains in a freefall, plunging to a new record low of -27.3 in July, tumbling 23.1 points from last June's -4.2. Meanwhile, services confidence dropped to a 14-month low of 9.8 this month after hovering in a flat trend around 13.4 the first half of the year. Retail trade confidence continues to fall further into negative territory, sliding from its recent peak of 6.3 last August to -5.8 in July—its fifth consecutive month in negative territory—while construction confidence dropped for the sixth time this year, to 0.7, down 7.7 points ytd. Industrial confidence peaked at a record high of 12.9 in December, falling to 2.0 in July.

Eurozone CPI Flash Estimates (*link*): The headline CPI rate for July is expected to accelerate to yet another new record high of 8.9% y/y, up from 8.6% in June and 6.7ppts above last July's 2.2%. The rate was at -0.3% at the end of 2020. Looking at the main components, once again energy is anticipated to record the largest gain, though it is forecast to ease to 39.7% y/y in July after accelerating from 37.5% in April to 42.0% in June;

it was at a record high of 44.3% in March. The rate for food, alcohol & tobacco is forecast to soar to a record-high 9.8% in July, having accelerated steadily from June 2021's 0.5%, while the rate for non-energy industrial goods is expected to pick up to a record-high 4.5%. The services rate is predicted to accelerate 3.7% y/y—the highest since spring 1995. Of the top four Eurozone economies, only Spain (10.8% y/y) is above the Eurozone's expected rate of 8.9%, jumping to a new record high. Meanwhile, rates in Germany (8.5% y/y), Italy (8.4), and France (6.8) were all below the Eurozone's rate of 8.9%—though France's CPI reached a new record high and Italy's was just a tick below June's record 8.5% rate.

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