**MORNING BRIEFING**
**January 19, 2023**

## Health Care, Going Global & ChatGPT

*Check out the accompanying chart collection.*

**Executive Summary:** The S&P 500 Health Care sector sheltered investors from the ravages of last year's bear market, but it's been underperforming since the market began to recover in mid-October. Jackie examines why other sectors might be more alluring now and why investors are looking past meager 2023 growth prospects for select health care companies active in M&A. … Also: Why have global stocks begun outperforming US stocks? Fears not materializing in Europe and China are part of the picture, US economic uncertainty and middling earnings growth prospects are another. … And: In a world where AI programs can write like humans, what could go wrong? Plenty.

**Health Care: Looking for the Right Rx.** Over the past year, the S&P 500 Health Care sector lived up to its defensive reputation and gained 0.5% even as the S&P 500 lost 14.4%. No matter how much the Fed raises interest rates, people still get sick, need to visit the doctor, and buy medicine. But since the S&P 500 began to rally after bottoming on October 12, the Health Care sector has begun to underperform other sectors. It may continue to do so if this rally has legs and investors are lured instead to sectors that have underperformed over the past year, offer faster earnings growth prospects, or both.

The performance derby for the S&P 500 and its 11 sectors on a y/y basis through Tuesday's close shows that the Health Care sector has provided excellent shelter for investors as the market fell: Energy (40.5%), Utilities (2.7), Health Care (0.5), Consumer Staples (-2.9), Industrials (-4.0), Materials (-6.3), Financials (-12.2), S&P 500 (-14.4), Real Estate (-17.8), Information Technology (-21.4), Consumer Discretionary (-29.6), and Communication Services (-34.9) (*Table 1*).

Since the S&P 500 bottomed in October, however, the Health Care sector has lagged the broader market. Here's the S&P 500 performance derby from October 12 through Tuesday's close: Materials (21.1), Industrials (19.9), Financials (18.6), Real Estate (16.7), Utilities (15.9), Energy (12.2), Information Technology (12.0), S&P 500 (11.6), Consumer Staples (10.8), Health Care (10.6), Communication Services (5.9), and Consumer Discretionary (-0.8) (*Table 2*).

Analysts expect a 3.5% decline in earnings for the Health Care sector this year, below the 2.8% gain that's forecast for the S&P 500 and below those of most sectors: Consumer

Discretionary (28.3%), Industrials (13.4), Financials (12.9), Utilities (7.5), Communication Services (5.8), Consumer Staples (3.2), S&P 500 (2.8), Information Technology (0.2), Health Care (-3.5), Materials (-11.5), Energy (-14.5), and Real Estate (-14.8).

Here's a look at some of the headwinds and tailwinds affecting health care companies, including patent expirations, wage pressures, and litigation settlements:

(1) *M&A saves the day.* Investors may be looking past drug patent expirations and betting that drug companies have the financial wherewithal to buy and develop smaller companies' drugs to fill the void. That would explain why the S&P 500 Pharmaceuticals industry's stock price index has risen 9.9% from the market's October 12 low through Tuesday's close, even though analysts' consensus forecasts have the industry's earnings falling 6.0% this year and rising just 4.7% in 2024 (*Fig. 1*). Likewise, the S&P 500 Biotechnology industry's stock price index has jumped 13.2% since October 12 even though its earnings are forecast to drop 14.9% this year and rise only 2.4% in 2024 (*Fig. 2*).

Consider AbbVie, a member of the S&P 500 Biotechnology index. It lost patent protection on Humira—a drug that treats rheumatoid arthritis and Crohn's disease, among other ailments, and that kicked in more than a third of the company's sales last year. AbbVie has been making small acquisitions, most recently in October when it purchased DJS Antibodies. DJS develops antibody medicines that target disease-causing proteins. That followed AbbVie's purchase last spring of Syndesi Therapeutics, which makes drugs that improve cognitive function, including one to treat Alzheimer's. Investors clearly approve: AbbVie's shares have rallied 8.0% since October 12 even though analysts see its earnings per share falling from $13.83 in 2022 to $11.81 this year.

Likewise, Pfizer's earnings per share is forecast to drop from $6.48 in 2022 to $4.69 this year, but its stock has rallied 9.9% since the market's October's low. Patent expirations are expected to reduce the company's revenue by $17 billion by the decade's end, but management plans to replace this revenue through internal drug development and acquisitions. Pfizer purchased Biohaven and its migraine drugs for $11.6 billion in May 2022 and Global Blood Therapeutics, a sickle cell disease drug maker, for $5.4 billion in October.

In addition to patent expirations, some drug companies will face mounting price pressure from the US government. The Health and Human Services Department will publish in September a list of the 10 most popular drugs covered by Medicare, on which it will launch price negotiations under new powers granted by the Inflation Reduction Act. The list will include only drugs that have been on the market for at least seven years without generic competition or 11 years for biological products like vaccines.

Price negotiations will begin in 2025 and go into effect in 2026. It's unknown which drugs will make the list, but here are the most expensive drugs for Medicare Part D (purchased by seniors though pharmacies) in 2020, according to a January 12 CNBC *article*: Bristol-Myers' Eliquis and Revlimid, J&J's Xarelto, Merck's Januvia, Eli Lilly's Trulicity and Jardiance, AbbVie's Imbruvica and Humira, Sanofi's Lantus Solostar, Pfizer's Ibrance, and AstraZeneca's Symbicort. The list will expand in subsequent years.

(2) *Labor woes.* Hospital staffing has improved dramatically from the depths of the Covid pandemic, when traveling nurses were being called in and earning premium pay. But the tight overall labor market continues to empower today's workers to demand higher pay. Monday's *WSJ* carried an *article* about doctors in residency and fellowship programs forming unions faster than usual: Five teaching hospitals faced such activity last year, up from two in 2021 and the normal pace of one per year. Residents are pushing for fewer hours and improved wages, particularly in pricey metropolitan areas.

In addition, more than 7,000 unionized nurses at Montefiore Medical Center and Mount Sinai Hospital in New York City went on strike for three days earlier this month, returning to work after reaching a tentative deal that includes 19%-plus wage increases over three years and enforceable patient-to-nurse ratios. The deal, according to a January 12 *WSJ* *article*, is similar to the new contracts recently agreed to by three other NYC hospitals.

The share prices of HCA Healthcare and Universal Health Services both fell sharply early in 2022 as investors learned that higher-than-expected labor costs were eating into the companies' profits. Both stocks since have bounced back, leaving the S&P 500 Health Care Facilities stock price index up 1.9% y/y through Tuesday's close (*Fig. 3*). Analysts are optimistic that the industry's revenue and earnings will climb by 4.1% and 7.5% this year and 5.7% and 13.3% in 2024 (*Fig. 4* and *Fig. 5*).

(3) *Distributors' stocks on fire.* Shares of the S&P 500 Health Care Distributors industry have had quite the run, soaring 35.7% y/y through Tuesday's close and 14.0% since the market's October 12 low (*Fig. 6*). Cardinal Health and McKesson shares are the standouts, both are up more than 40% y/y. AmerisourceBergen, Cardinal, and McKesson benefitted from entering a $19.5 billion opioid-related lawsuit settlement with most US states early last year, ending some of the uncertainty about their opioid-related liability.

The industry's earnings are expected to rise a respectable 5.4% this year and 12.7% in

2024, and analysts' net earnings revisions have been positive lately (*Fig. 7*). Despite the strong stock price performance last year, the industry's forward P/E of 14.2 is well above its March 23, 2020 low of 8.5 but not far from its recent high in early December of 14.7 (*Fig. 8*).

**Strategy: Time To Go Global?** This year has kicked off with international stocks outperforming US stocks by a large margin. The ratio of the US MSCI stock price index relative to the All Country World ex-US MSCI stock price index, measured in dollars, peaked on October 28 and has fallen 14.1% since then (*Fig. 9*). In local currencies, the ratio peaked just over a year ago, on December 27, 2021, and since has fallen 12.2%. Is this just a short-term reversal, giving US stocks time to breathe before continuing their outperformance, or should investors pack their bags and Go Global? Let's have a closer look:

(1) *The Boogie Man fails to appear.* Recent months have not brought the misfortunes that were widely expected to befall China and Europe. China started providing financial support to its ailing real estate developers, stopped picking on its technology companies by slapping them with new regulations, and lifted its zero-Covid rules. These moves should allow its economy to pick up speed in 2023 after logging only 3% real GDP growth last year. The China MSCI stock price index bottomed on October 31 and has risen 49.1% since then (*Fig. 10*).

Mother Nature was kind enough to bestow a warm winter on Europe, which should leave enough natural gas for Europeans to heat their homes and run their businesses through this winter. That was not a given after Russia sharply reduced natural gas deliveries last summer. The price of natural gas spiked to €339 MWh during August 2022 before recently dropping back down to €60 MWh (*Fig. 11*). The Europe MSCI stock price index bottomed on September 29 and since has rallied 19.6% in local currency; in dollars, it bottomed on September 27 and has rallied by 31.7% (*Fig. 12*).

(2) *US recession fears strike.* Meanwhile, the US Federal Reserve has been more aggressive in tightening monetary policy than was expected as recently as last summer, which has left most economists expecting a US recession sometime soon (though we do not fall into that camp). Rising interest rates and a Covid hangover has burst the MegaCap-8 stocks' bubble and dragged down the S&P 500. The US MSCI stock price index peaked on December 27, 2021 and has fallen 18.0% through Tuesday's close (*Fig. 13*).

Exacerbating these trends is the US dollar, which after climbing higher since May 2021 has suddenly reversed course and fallen 7.6% since its peak on October 19, 2022 (*Fig. 14*).

(3) *Looking abroad for earnings growth.* US MSCI earnings is expected to grow by 3.2% this year, landing the US in the middle of the pack in terms of countries' 2023 earnings growth prospects. Topping the list is Sri Lanka (55.2%) and in last place is the Czech Republic (-38.5). Notable are the strong earnings expected for India (21.3), China (14.4), and Mexico (9.1) and the weak earnings growth expected for Latin American countries like Brazil (-18.0), Chile (-14.0), and Colombia (0.1). (Data isn't provided for Argentina and Russia.)

European countries are expected to post mixed earnings growth in 2023, with Portugal (20.8), the Netherlands (20.6), and Switzerland (17.9) posting strong earnings growth and Denmark (-22.7), Austria (-12.7), and Norway (-12.3) the weakest.

Here are the 2023 earnings growth estimates for the following regions: Emerging Markets Asia (2.4%), US (3.2), World (2.1), World ex-US (1.1), EMU (0.9), Emerging Markets (0.6), Europe (0.3), and Emerging Markets Latin America (-12.9) (*Fig. 15*).

(4) *Multiples dropping around the world.* The US MSCI forward P/E has contracted sharply over the past two years. It peaked at 23.3 in January 2021 and since has fallen to 17.7. That brings the index's forward P/E back to the midpoint of its 25.2-9.5 range since the start of the century. Other countries have experienced multiple contraction as well. The forward P/E on the All Country World ex-US MSCI index has fallen to 12.4 from a recent peak of 17.1 in February 2021 (*Fig. 16*).

**Disruptive Technologies: Thinking About ChatGPT.** There's no doubt about it: ChatGPT has writing chops. Some of the samples we read may have lacked creative flourishes, but they certainly looked like writing that could have been produced by a human. Earlier this week, Microsoft, an investor in ChatGPT's creator OpenAI, announced plans to incorporate artificial intelligence into all of Microsoft's existing products and give companies access to OpenAI tools so that they can create applications using AI.

We tried to get on the OpenAI *website* to test it for ourselves numerous times yesterday. But the site was at capacity and asked us to try back later. We certainly will. But until then, here are some of the things that ChatGPT is reportedly good and not good at doing:

(1) *It's fast.* ChatGPT has absorbed large volumes of data from the Internet written by humans. It can turn around an article or email much faster than its human counterpart.

(2) *It's good.* ChatGPT was asked to write 50 abstracts about medical research papers published in various industry publications, a January 12 *article* in *Nature* reported. A

plagiarism checker didn't flag any plagiarism in any of the AI-generated abstracts.

An AI-output detector was able to identify 66% of the ChatGPT-written abstracts as penned by AI. Humans reading the abstracts didn't fare much better. They identified only 68% of the AI-generated abstracts correctly, misidentifying the other 32% as human, and they got 86% of the human-generated abstracts right, missing the other 14%. In other words, ChatGPT is pretty darn good.

(3) *It's not current.* ChatGPT isn't connected to the Internet, and it has limited knowledge about things that occurred after 2021. This likely will be fixed overtime.

(4) *It publishes errors with authority.* Users report that ChatGPT sometimes produces incorrect answers, but it does so in a sentence or paragraph that's still well written. As a result, readers say it can be tricky to flag when ChatGPT has made a mistake, especially if the reader isn't knowledgeable about the subject.

CNET uses AI to generate articles about basic financial subjects, like compound interest, and until recently it used the human-sounding byline "CNET Money Staff." Only after clicking on the byline would a reader learn that the article was AI generated. A few articles contained errors highlighted in a January 17 *article* in Futurism. CNET published an article confirming that it used AI to generate about 75 articles that were subject to review by a human editor. Future bot-written articles will carry the byline "CNET Money" and disclose: "This article was assisted by an AI engine and reviewed, fact-checked and edited by our editorial staff." AI-generated mistakes that slip by the human fact-checkers will be publicly corrected.

Two old sayings come to mind. "Mom always said not to believe everything you hear." It's always important to know the source of information, and ChatGPT would be wise to provide the sources used to create its essays so the accuracy can be verified.

The second saying comes from Jackie's high school computer teacher: "Junk in, junk out." In other words, computers' output is only as good as the programs they're fed. The same goes for ChatGPT essays. Now that AI has made creating content fast and cheap, evaluating what we read online has grown even trickier.

## Calendars

**US: Thurs:** Housing Starts & Building Permits 1.359mu/1.370mu; Philadelphia Fed Manufacturing Index -11; Initial & Continuous Jobless Claims 214k/1.66m; Crude Oil Inventories & Natural Gas Storage; Williams; Brainard. **Fri:** Existing Home Sales -5.4%; US Baker-Hughes Rig Count; Waller; Harker. (Bloomberg estimates)

**Global: Thurs:** Eurozone Current Account; ECB Publishes Account of Monetary Meeting; Schnabel; Lagarde. **Fri:** Germany PPI -1.2%m/m/20.8%y/y; UK Headline & Core Retail Sales 0.5%m/m/-4.1%y/y & 0.4%m/m/-4.4%y/y; China New Loans; Lagarde; Nagel; Elderson. (Bloomberg estimates)

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## Strategy Indicators

**Stock Market Sentiment Indicators** (*link*): The Bull-Bear Ratio climbed for the second week this week to 1.57—the highest since mid-August 2022—after falling the prior three weeks from 1.37 to 1.08. *Bullish sentiment* jumped to its highest reading since the start of 2022, outnumbering bears for the ninth consecutive week, climbing from 36.6% to 46.5% the past two weeks. Meanwhile, *bearish sentiment* retreated for the second week to 29.6%, the lowest since mid-September and far below the 44.1% reading in early October last year. The *correction count* slipped for the second week to 23.9%, after climbing steadily from 24.3% in early December to 29.6% during the January 3 week, remaining well below its late September peak of 40.3%. Turning to the AAII Sentiment Survey (as of January 12), pessimism about the short-term direction of the stock market dropped to its lowest level in 10 weeks, with neutral sentiment also heading lower, while optimism rebounded. The *percentage expecting stock prices to rise* over the next six months rebounded 3.5ppts to 24.0% after falling 6.0ppts (to 20.5% from 26.5% the prior week). It remained below its historical average of 37.5% for the 54th consecutive week, and was at an unusually low level the seventh successive week. The *percentage expecting stocks to fall* over the next six months fell for the third week from 52.3% to 39.9% (only its second time below 40% since September 2022), with pessimism remaining above its historical average of 31.0% for 57 of the past 60 weeks. The *percentage expecting stock prices will stay essentially unchanged* over the next six months fell 1.5ppts to 36.0%, after soaring 11.6ppts (to 37.5% from 25.9%) the prior week—the highest percentage since the March 31, 2022 week's 40.6%. It was above its historical average of 31.5% for the second straight week.

**S&P 500 Earnings, Revenues, Valuation & Margins** (*link*): The S&P 500's forward profit margin remained steady last week at a 20-month low of 12.6%. That's down 0.8ppts from its record high of 13.4% achieved intermittently from March to June. Since the end of April 2020, it has exceeded its prior record high of 12.4% in September 2018. It's now up 2.3pts from 10.3% during April 2020, which was the lowest level since August 2013. Forward revenues was flat w/w at 0.2% below its record high in mid-October. Forward earnings fell 0.2% w/w and is 4.4% below its record high in mid-June. Both had been steadily making new highs from the beginning of March 2021 to mid-June; prior to that, they peaked just before Covid-19 in February 2020. The consensus expectation for forward revenues growth was unchanged w/w at a 30-month low of 2.7%. That's down from a record high of 9.6% growth at the end of May 2021 and compares to 0.2% forward revenues growth during April 2020, which was the lowest reading since June 2009. Forward earnings growth dropped 0.2ppt w/w to 4.3%, but remains above its 30-month low of 4.0% the week before that. 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. During 2022, analysts' revisions to their forecasts for 2022 revenues outpaced their revisions for 2022 earnings, so the imputed 2022 profit margin estimate that we calculate from those forecasts fell 0.8ppt to 12.4% (unchanged w/w). They expect revenues to rise 11.5% (up 0.1ppt w/w) in 2022 and 2.4% in 2023 (unchanged w/w) compared to the 16.5% gain reported in 2021. They expect earnings gains of 7.5% in 2022 (down 0.1ppt w/w) and 2.8% in 2023 (down 0.2ppt w/w) compared to an earnings gain of 50.5% in 2021. Analysts expect the profit margin to drop 0.5ppt y/y to 12.4% in 2022 (unchanged w/w) compared to 12.9% in 2021 and to improve 0.1ppt y/y to 12.5% in 2023 (unchanged w/w). The S&P 500's weekly reading of its forward P/E rose 0.5pt w/w to a four-week high of 17.4. That's up from a 30-month low of 15.3 in mid-October and is down from a four-month high of 18.2 in mid-August. It also 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 rose 0.07pt w/w to a four-week high of 2.20, up from a 31-month low of 1.98 in mid-October. That's down from a four-month high of 2.38 in mid-August and also compares to a record high of 2.88 at the end of 2021 and a 49-month low of 1.65 in March 2020.

**S&P 500 Sectors Earnings, Revenues, Valuation & Margins** (*link*): Looking at the 11 S&P 500 sectors, last week saw consensus forward revenues rise for five sectors and forward earnings rise for three sectors. The forward profit margin rose w/w for four sectors: Consumer Staples, Industrials, Real Estate, and Utilities. Nearly all of the sectors are below recent record highs in their forward revenues, earnings, and profit margins. Consumer Staples, Financials, and Health Care are the only sectors with forward revenues at a record high this week. Consumer Staples has forward earnings at a record high this week. Forward earnings for Financials, Industrials, and Utilities still remains close to their recent record highs, but Energy's is quickly giving up its gains since its record high in October. Since mid-August, all sectors have seen forward profit margins retreat from their record highs. Those of Industrials and Tech remain close to their post-pandemic highs, and Energy's is now down 0.7ppt from its 12.8% record high in late November. Only three sectors posted a higher profit margin y/y during 2020: Consumer Staples, Tech, and Utilities; during 2021, all of the sectors but Utilities posted a y/y improvement. Energy and Industrials are the only two sectors expected to see margins improve y/y for full-year 2022, followed by these five sectors in 2023: Communication Services, Consumer Discretionary, Financials, Industrials, and Utilities. Here's how they rank based on their current forward profit margin forecasts along with their record highs: Information Technology (24.0%, unchanged w/w from a 20-month low and down from its 25.4% record high in early June), Financials (17.9, down 0.1ppt w/w and down from its 19.8 record high in August 2021), Real Estate (17.4, up 0.1ppt w/w and down from its 19.2 record high in 2016), Communication Services (14.1, unchanged w/w and down from its 17.0 record high in October 2021), Utilities (13.8, unchanged w/w and down from its 14.8 record high in April 2021), Energy (12.1, down 0.2ppt w/w and down from its 12.8 record high in November), S&P 500 (12.6, unchanged w/w at a 20-month low and down from its record high of 13.4 achieved intermittently from March to June), Materials (11.4, down 0.1pt w/w to a 22-month low and down from its 13.6 record high in June), Health Care (10.1, unchanged w/w at a 30-month low and down from its 11.5 record high in March), Industrials (10.1, unchanged w/w and down from its 10.5 record high in December 2019), Consumer Discretionary (7.3, unchanged w/w at a 32-month low and down from its 8.3 record high in 2018), and Consumer Staples (7.1, unchanged w/w at a 56-month low and down from its 7.7 record high in June 2020).

**S&P 500 Sectors & Industries Forward Profit Margin Since Peak** (*link*):
Since the S&P 500's forward profit margin peaked at a record-high 13.4% during the June 9 week, it has fallen 6.4% to 12.6% through the January 12 week. The drop has been paced by four of the 11 sectors, though all but the Energy sector is down since the peak. Here's the sector performance since the June 9 peak: Energy (up 1.7% to 12.1%), Utilities (down 0.5% to 13.8%), Industrials (down 2.6% to 10.1%), Consumer Staples (down 2.7% to 7.1%), Real Estate (down 3.1% to 17.4%), Information Technology (down 5.5% to 24.0%), Financials (down 6.1% to 17.9%), Consumer Discretionary (down 6.5% to 7.3%), S&P 500 (down 6.4% to 12.6%), Health Care (down 8.1% to 10.1%), Communication Services (down 12.6% to 14.1%), and Materials (down 15.8% to 11.4%). These are the best-performing industries since the June 9 peak: Wireless Telecommunication Services (up 53.1% to 10.4%), Oil & Gas Refining & Marketing (up 38.1% to 4.7%), Airlines (up 18.7% to 4.8%),

Oil & Gas Equipment & Services (up 16.8% to 10.7%), and Hotels, Resorts & Cruise Lines (up 14.1% to 11.3%). The worst performing industries since the June 9 peak: Alternative Carriers (down 39.5% to 5.3%), Commodity Chemicals (down 37.9% to 6.4%), Copper (down 36.0% to 12.3%), Home Furnishings (down 33.7% to 5.9%), and Gold (down 32.7% to 12.9%).

## US Economic Indicators

**Retail Sales** (*link*): Retail sales contracted for the second time since reaching a record high in October, falling a larger-than-expected 1.1% in December, following November's 1.0% decline—which was steeper than the 0.6% drop previously reported, as goods prices declined. Of the 13 nominal retail sales *categories*, 10 fell, two rose, and one—food & beverage stores—was flat. Here's a snapshot of the 13 categories' December sales performance versus that of a year ago: building materials & garden equipment & supplies (0.3% m/m & 2.3% y/y), sporting goods & hobby stores (0.1 & 3.9), food & beverage stores (0.0 & 6.9), clothing & accessories stores (-0.3 & 2.9), general merchandise stores (-0.8 & 3.8), food services & drinking places (-0.9 & 12.1), health & personal care stores (-0.9 & 2.8), nonstore retailers (-1.1& 13.7), miscellaneous store retailers (-1.1 & 2.4), electronics & appliance stores (-1.1 & -5.6), motor vehicles & parts (-1.2 & 1.8), furniture & home furnishings (-2.5 & 0.3), and gasoline stations (-4.6 & 5.2).

**Business Sales & Inventories** (*link*): Nominal business sales in November remained stalled around June's record high, while real sales in October climbed back toward its record high at the start of 2022. *Nominal sales* fell 0.8% in November, following a 0.8% rise through the three months ending October, and is within 1.0% of June's record high. Year-to-date sales are up 8.1%. Meanwhile, *real business sales* climbed in October for the fourth successive month, up 0.3%m/m and 2.7% over the period, to within 0.5% of January's record high, following a five-month slide of 3.1%. In the meantime, the real i*nventories-to-sales ratio* remained at 1.46 in October, down from its recent high of 1.48 in June—which was the highest since mid-2020; the nominal ratio in November moved up to a 23-month high of 1.35.

**Industrial Production** (*link*): Output in December slumped for the second month from its record high posted in both September and October. *Headline* production dropped 0.7% in December, following a 0.6% drop in November—which was triple the initial estimate. *Manufacturing* production contracted sharply for the second month, by 1.3% in December and 1.1% in November—which was steeper than the initial 0.6% drop. ISM's manufacturing survey shows activity has been shrinking since November, and Tuesday's manufacturing report by the New York Fed showed a big plunge in activity during January. Meanwhile, *mining* output sank for the second month, by 0.9% m/m and 2.1% over the period, while *utilities* output has spiked the past two months as a cold snap boosted demand for heating. By market group: *business equipment* production contracted for the second month on widespread weakness, slumping 3.7% over the two months through December; leading the contraction were declines of 4.7% and 4.2% for transit and industrial equipment, respectively, while production of information processing & related equipment was 1.5% lower. *Consumer goods* production also fell during the final two months of last year, by 0.7% over the period, led by a 4.4% drop in durable goods output, driven by appliances, furniture, and carpeting (-6.4%) and automotive products (-4.9); consumer nondurable goods rose 1.0% over the final three months of 2022.

**Capacity Utilization** (*link*): The *headline* capacity utilization rate moved lower in December for the third month, from 80.1% in September to a 12-month low of 78.8% in December. December's rate was 0.8ppt below its long-run (1972-2021) average. The *manufacturing* utilization rate slumped to a 15-month low of 77.5%—0.7ppt below its long-run average. Meanwhile, the capacity utilization rate for *mining* slipped to 87.7% in December from a recent high of 89.9% in September; it was 1.4ppts above its long-run average. Cold weather boosted the *utilities* rate for the second month to 76.8% in December after dropping to a record low of 71.1% in October, though it remained substantially below its long-run average.

**NAHB Housing Market Index** (*link*): "It appears the low point for builder sentiment in this cycle was registered in December, even as many builders continue to use a variety of incentives, including price reduction to bolster sales," noted Jerry Konter, NAHB's chairman. He went on to say, "The rise in builders' sentiment also means that cycle lows for permits and starts are likely near, and a rebound from home building could be underway later in 2023." *Homebuilders' confidence* rose for the first time in a year, climbing to 35 this month, after plunging 53 points during the 12 months of 2022 to 31—the lowest since mid-2012, excluding its drop to 30 during the height of the pandemic. All three components of the confidence measure improved this month, with the current sales (+4 points to 40) component posting the biggest move up, followed by traffic of prospective home buyers (+3 to 23), and future sales (+2 to 37). Before the pandemic hit, they were at record highs of 96, 77, and 89, respectively, during November 2020.

**Producer Price Index** (*link*): The underlying trend in inflation continued to moderate in December, as final demand PPI posted an unexpected 0.5% drop (versus -0.1% consensus), with the yearly rate sinking to 6.2%, easing steadily from March's record-high

11.7%. Meanwhile, core prices—which excluded food, energy, and trade services—edged up only 0.1%, the smallest monthly gain since November 2020, with the yearly rate easing from a record-high 7.1% in March to a 21-month low of 4.6% in December. *Final demand goods* fell for the first time in four months, sinking 1.6% in December, with the yearly rate easing to a 21-month low of 8.0%, down from June's record high of 17.6%. In the meantime, *final demand services* ticked up only 0.1%, following gains of 0.2% in each of the prior two months, with the yearly rate slowing to a 20-month low of 5.0% after peaking at a record high of 9.4% in March. The PPI for *personal consumption* fell 0.4% in December after gains of 0.1% and 0.6% the prior two months, with the yearly rate easing steadily from March's 10.4% record high, falling to 5.6% by December—the lowest since March 2021. The yearly rate for *personal consumption excluding food & energy* eased to a 19-month low of 4.8%, down from March's record high of 8.1%. Looking at *pipeline prices*, the yearly rate for intermediate goods prices slowed to a 23-month low of 4.7% from a cyclical high of 26.5% during November 2021, while the crude goods rate climbed to 11.7% y/y last month, after slowing dramatically from its recent peak of 50.7% in June to 2.8% by November. It was at 59.0% during April 2021—which was only a tick below its record-high 59.1% in August 1973.

## Global Economic Indicators

**Eurozone CPI** (*link*): December's final estimate for the headline CPI rate matched the flash estimate, showing the CPI slowed for the second month, from a record-high 10.6% in October to 9.2% y/y by year-end. For perspective, the rate was as low as -0.3% at the end of 2020. Looking at the main components, once again *energy* recorded the largest gain, though slowed again in December to 25.5% from 34.9% and 41.5% the prior two months; it was at a record high of 44.3% in March. The rate for *food, alcohol & tobacco* soared to a record-high 13.8% in December—accelerating steadily from June 2021's 0.5%—while the rate for *non-energy industrial goods* reached a new record high of 6.4%. The *services* rate picked up to 4.4% y/y—the highest since the end of 1993. Of the *top four Eurozone economies*, rates for Italy (12.3% y/y) and Germany (9.6) were above the Eurozone's rate of 9.2%, with the former down from its record high of 12.6% during both October and November and the latter down from its record high of 11.6% during October. Meanwhile, rates in Spain (5.5) and France (6.7) were below the Eurozone's 9.2% rate, down from their recent record highs of 10.7% and 7.1%, respectively.

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