MORNING BRIEFING
January 30, 2023

ABCs of GDP & PCED

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Executive Summary: The global financial markets are reflecting expectations for an improved global economy, and the US stock market is siding with the optimists on the US economic outlook, us among them: We continue to see greater odds of a soft landing (60%) than a hard one (40%). … Recent GDP and inflation data support our soft-landing scenario. Q4 GDP was strong, but a look under the hood suggests it was boosted by unintended inventories and Q1 GDP might be tempered by inventory liquidation. The past three months of PCED inflation data highlights reassuring downward progress, especially in goods inflation. … And: Dr. Ed reviews "Argentina 1985" (+ + +).

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Strategy: Betting on Global Growth. While many economists and strategists have been fretting about a 2023 global recession led by economic downturns in the US, Europe, and China, stock investors started the new year by snapping up cheap stocks around the world. Traders in the commodity pits have been going long metals futures contracts. The dollar has weakened as the outlook for the global economy has improved. In other words, financial markets are anticipating a brighter outlook for 2023 compared to 2022. We are siding with the markets.

The consensus outlook seems to have turned more optimistic for Europe and China in recent weeks. On the other hand, the outlook for the US remains hotly debated. Nevertheless, the US stock market has been siding with the optimists since the S&P 500 bottomed on October 12 of last year. Consider the following developments in the US and global financial markets:

(1) *S&P 500.* The S&P 500 tried and failed to rise above its 200-day moving average three times during the bear market from January 3 to October 12, 2022 (*Fig. 1*). These attempts were followed by new bear market lows. The rally since the October 12 low of 3577.03 on the S&P 500 saw another failed attempt to take out the 200-day moving average during late November. However, the index found support around 3800 late last year and early this year

and rose above its 200-day moving average in recent days, closing at 4070.56 on Friday.

Leading the charge during January have been some of the S&P 500's most cyclical sectors: Communication Services (14.8%), Consumer Discretionary (14.5), Information Technology (9.8), Real Estate (9.2), Materials (7.3), S&P 500 6.0), Financials (5.8), Energy (4.2), Industrials (2.9), Consumer Staples (-2.2), Utilities (-2.3), and Health Care (-2.4) (*Fig. 2* and *Table 1*).

The leadership of cyclicals is even more striking since the October 12 bear market low: Materials (21.8%), Financials (19.8), Real Estate (19.0), Information Technology (16.8), S&P 500 (13.8), Energy (13.7), Communication Services (13.6), Utilities (12.1), Health Care (8.9), Consumer Staples (8.1), and Consumer Discretionary (4.9) (*Table 2*).

As we previously observed, the rally since October 12 has been associated with improving breadth, as more and more stocks have participated. Since then, here is the performance derby of some of the major US stock market indexes: S&P 500 Equal Weighted Total Return (18.1%), S&P 500 Equal Weighted (17.4), S&P 400 (16.3), S&P 500 Transportation (14.7), S&P 500 Total Return (14.4), and S&P 500 (13.8) (*Fig. 3*). Furthermore, the NYSE advance/decline line seems to be breaking out of its downward consolidation that started in early 2021 (*Fig. 4*).

What about earnings? Industry analysts have been trimming their estimates for S&P 500 operating earnings per share (*Fig. 5*). Here are the y/y quarterly growth rates they are projecting as of the January 19 week: Q1 (-2.5%), Q2 (-3.5), Q3 (3.5), and Q4 (10.4). However, their annual earnings-per-share expectations for 2023 (at $227, up from $219 in 2022) and 2024 (at $252) remain consistent with our soft-landing economic outlook (*Fig. 6*). By the way, the percent of S&P 500 companies with positive three-month percent changes in forward revenues and forward earnings rebounded to 66.1% and 56.5% during the January 27 week, up from recent low readings of 50.6% and 44.4% during the December 30 week (*Fig. 7* and *Fig. 8*).

In conclusion, we believe that the rally since October 12 is the Real McCoy—the start of a new bull market instead of just a rally within a bear market. That assessment is consistent with our optimistic outlook for the global economy as well as our view that a soft landing is more likely than a hard landing for the US economy.

Although we are feeling more optimistic, we are sticking with our 60% subjective probability of a soft landing and 40% of a hard landing. Let's see whether Fed Chair Jerome Powell insists on depressing us all yet again on Wednesday during his press conference.

(2) *All Country World MSCI.* Our TINAC hypothesis—i.e., that foreign investors remained tethered to US markets given their rationale that "there is no alternative country" with as much investment appeal—mostly worked well during the pandemic up until the point in late 2022 when it didn't. During that period, global investors perceived the US as a safe haven in an increasingly unsettled geopolitical environment. The dollar soared until it peaked at a record high on October 19, 2022 (*Fig. 9*).

Around that time, investors turned more optimistic about both Europe's prospects and China's outlook. Europe succeeded in replacing Russian natural gas with other sources as winter approached and turned out to be a mild one. On December 7, China's government abruptly *scrapped* its zero-Covid policy.

The ratio of the US MSCI to the All Country World ex-US MSCI (in dollars) peaked at a record high on October 28, 2022 (*Fig. 10*). Here is the performance derby of the major MSCI stock price indexes (in dollars) since October 12 of last year through Friday's close: Italy (42.5%), Germany (41.6), China (38.6), EMU (38.5), Europe (31.4), UK (26.3), Emerging Markets Asia (25.5), All Country World ex-US (25.3), Emerging Markets (21.5), Japan (20.3), All Country World (18.1), US (13.7), and Emerging Markets Latin America (7.8) (*Table 3*).

As investors turned more optimistic on the global economic outlook, they scrambled to purchase overseas stocks because they've been cheaper than US stocks. Here are the forward P/Es of the major MSCI stock price indexes during the January 19 week: US (17.6), EMU (12.5), Japan (12.2), Emerging Markets (12.1), and the UK (10.5) (*Fig. 11*).

(3) *Commodity prices and currencies.* Most commodity prices are quoted in dollars. So there tends to be an inverse correlation between the dollar and commodity prices (*Fig. 12*). When the global economy is doing well, the dollar tends to weaken and commodity prices tend to strengthen, which is what has been happening since late last year. Particularly strong has been the metals component of the CRB raw industrials spot price index, which includes copper scrap, lead scrap, steel scrap, tin, and zinc (*Fig. 13*).

The euro and the yen rebounded smartly since late last year as financial markets started to discount the end of the Fed's monetary tightening cycle but assumed that the European Central Bank and the Bank of Japan must do more tightening ahead.

US Economy I: Slicing & Dicing GDP. Friday's GDP report for Q4-2022 is also consistent with a soft-landing forecast. The 2.9% (saar) increase was widely reported to be a strong number following Q3's 3.2%. Both are more consistent with a no-landing scenario. However, as we observed in our January 26 *QuickTakes*, while real GDP was up 2.9%, real final sales of domestic product rose only 1.4% (*Fig. 14*).

In other words, inventory investment accounted for a bit more than half of the increase in real GDP during Q4. In the GDP accounts, inflation-adjusted retail inventories excluding autos fell for the second quarter in a row as the industry cut prices to reduce the big pile of unintended inventory accumulation during the previous three quarters (*Fig. 15*). As retailers scrambled to reduce their inventories, manufacturing and wholesale inventories piled up during Q4. During Q1-2023, we expect to see inventory liquidation among manufacturers and wholesalers, offset by some rebuilding of inventories by retailers.

Now let's briefly examine the other major components of real GDP:

(1) *Consumer spending.* Personal consumption expenditures rose 2.1% during Q4. They were up 2.8% during 2022, led by a 4.5% increase in services. Goods consumption fell 0.4% last year after jumping 12.2% during 2021 (*Fig. 16*).

Hard landers are warning that pandemic-related excess saving allowed consumers to spending more last year as evidenced by the drop in the personal saving rate from 12.0% in 2021 to 3.4% in 2022 (*Fig. 17*). That's true, but we expect that real disposable income will continue to get a boost from employment gains and rising real wages this year (*Fig. 18*).

(2) *Residential investment.* Single-family housing activity was a big drag on real GDP last year. It might be less so this year. Mortgage rates and home prices have been coming down, and there is lots of pent-up demand for housing.

Residential investment fell 26.7% (saar) during Q4 following a 27.1% drop in Q3. For all of 2022, it was down 10.7%. Leading the way down during 2022 compared to 2021 was a 38.5% drop in single-family construction (*Fig. 19*). Multi-family residential investment held up well last year and should do so this year.

(3) *Capital spending.* Nonresidential investment rose 3.6% last year, led by an 8.7% increase in intellectual property (with software, R&D, and creative originals all rising to record highs) and a 4.3% increase in equipment, while structures fell 7.4% (*Fig. 20*).

Industrial equipment was led higher by transportation equipment. Industrial and high-tech equipment edged down but remained near recent record highs. Technology continued to account for about 50% of current-dollar capital spending. (*Fig. 21*). The weakness in structures last year was in commercial, health care, power, and communications (*Fig. 22*). Manufacturing structures held up well and may be heading higher.

(4) *Trade.* The trade deficit narrowed a bit during Q4, providing a slight boost to real GDP (*Fig. 23*). The pandemic has had a wild impact on this deficit. It widened to a record high during Q1 as imported merchandise ordered during 2021 flooded into the country after getting stuck out at sea for several months, mostly as a result of port congestion. It's unlikely to continue to narrow as it did during the last three quarters of 2022.

(5) *Government.* Spending by the federal, state, and local governments started to boost real GDP during H2-2022 (*Fig. 24*). They are all likely to continue to do so in 2023 as spending on public infrastructure takes off.

US Economy II: Slicing & Dicing PCED. Fed officials tend to focus on the y/y PCED measure of inflation rate on a y/y basis. They should also have a look at inflation on a three-month basis to assess whether the latest data are pointing to transitory or persistent inflation. Consider the following:

(1) The inflation news in the Q4-2022 GDP release was good: The price index for gross domestic purchases rose 3.2% (saar) versus 4.8% during Q3. The headline consumption deflator increased 3.2% versus 4.3%, while the core rate rose 3.8%, down from 4.7%.

(2) In early 2022, we predicted that the headline PCED inflation rate would decline from 6%-7% during H1-2022 to 4%-5% during H2-2022 to 3%-4% in 2023. So far, so good (*Fig. 25*). It fell from a peak of 7% during June of last year to 5% by the end of the year.

(3) We like to compare the y/y inflation rate to the three-month annualized rate to see whether inflationary pressures are rising or falling in the short run. Over the three months through December, the headline PCED inflation rate was 2.1% versus 5.0% y/y, while the core rate was up 2.9% versus 4.4% (*Fig. 26*).

Here are the comparable comparisons for food (4.1%, 11.2%), energy (-16.8, 6.9), durable goods (-3.8, 2.7), and nondurable goods excluding food and energy (1.4, 3.3) (*Fig. 27*).

(4) While goods inflation is turning out to be relatively transitory after all, services inflation

remains persistent. Rent inflation as measured in the PCED shows no sign of peaking, rising to 8.3% y/y for tenants during December (*Fig. 28*). The three-month rate was 9.1%, but it may be starting to moderate, reflecting the fact that inflation in new rental leases dropped sharply during H2-2022.

Movie. “Argentina 1985” (+ + +) (*link*) is an excellent docudrama about the prosecution of the military leaders who led the bloody military junta that terrorized Argentina during the early 1980s. It is based on the true story of Julio Strassera, Luis Moreno Ocampo, and their young legal team of unlikely prosecutors. In his closing statement, Strassera said, “I wish to waive any claim to originality in closing this indictment. I wish to use a phrase that is not my own, because it already belongs to all the Argentine people. Your Honors: *Nunca más!*”

Calendars

US: Mon: Dallas Fed Manufacturing Index; Loan Officer Survey. **Tues:** Consumer Confidence 109.0; Employment Cost Index 1.1%; S&P/CS HPI Composite 20 cities -0.5%m/m/6.9%y/y; Chicago PMI 44.9; API Weekly Crude Oil Stock. (Bloomberg estimates)

Global: Mon: Eurozone Business & Consumer Survey 97.0; Germany GDP 0.0%q/q/0.8%y/y; Spain CPI 4.9% y/y; Japan Unemployment Rate & Jobs/Application Ratio 2.5%/1.36; Japan Retail Sales 3.0% y/y; Japan Industrial Production; China M-PMI & NM-PMI 49.7/52.0. **Tues:** Eurozone GDP -0.1%q/q/2.2%y/y; Germany CPI 1.0%m/m/9.2%y/y; Germany Import Prices -2.2%m/m/11.6%y/y; Germany Retail Sales 0.4%; Germany Unemployment Rate 5.5%; France GDP 0.1% q/q; France CPI 0.5% m/m; Italy GDP -0.1%q/q/2.0%y/y Italy Unemployment Rate 7.8%; Japan Household Confidence 30.6; Canada GDP 0.1%m/m/3.5%y/y; China Caixin M-PMI 48.9; ECB Bank Lending Survey. (Bloomberg estimates)

Strategy Indicators

Global Stock Markets Performance (*link*): The US MSCI index rose 2.6% w/w and remained out of a bear market for a third week at 16.2% below its record high on December 27, 2021. The US MSCI ranked 12th of the 48 global stock markets that we follow in a week when 32 of the 48 countries rose in US dollar terms. The AC World ex-US index rose for a sixth straight week, but underperformed with a gain of 1.4% w/w as it improved to 14.9%

below its June 15, 2021 record high. EM Latin America was the best regional performer with a gain of 2.2%, followed by EM Eastern Europe (2.1%), EMU (1.5), and EM Asia (1.5). EMEA was the worst performing region last week, albeit with a gain of 0.3%, followed by BIC (1.4) and EAFE (1.4). The Czech Republic was the best-performing country last week, with a gain of 9.4%, followed by Egypt (8.9), Chile (5.6), Korea (4.7), and Singapore (3.6). Among the 27 countries that underperformed the AC World ex-US MSCI last week, Pakistan's 6.4% decline was the biggest, followed by those of Turkey (-4.6), India (-3.6), Morocco (-2.1), and Denmark (-1.8). Looking at 2023's performance so far, the US MSCI is up 6.3% and ranks 29/48 as just six of the 48 countries are down ytd. The AC World ex-US has risen 8.9% ytd, with all regions in positive territory. EMU is the best performer, with a gain of 11.6%, followed by EM Asia (11.0), BIC (10.5), EM Eastern Europe (9.8), and EM Latin America (9.2). The regional laggards so far in 2023: EMEA (2.2) and EAFE (8.5). This year's best ytd country performers: the Czech Republic (9.2), Mexico (17.6), China (17.2), Korea (16.6), and the Netherlands (16.0). Here are the worst-performing countries of the year so far: Pakistan (-14.9), Morocco (-3.9), Turkey (-3.7), India (-2.5), and Norway (-1.8).

S&P 500/400/600 Performance (*link*): All three of these indexes rose for the third time in four weeks. LargeCap gained 2.5% w/w, slightly ahead of the 2.4% and 2.1% gains recorded for MidCap and SmallCap. At the week's end, LargeCap finished at 15.1% below its record high on January 3, 2022, MidCap at 10.0% below its record high on November 16, 2021, and SmallCap at 14.8% below its November 8, 2021 record high. Thirty-one of the 33 LargeCap and SMidCap sectors moved higher for the week, up from nine rising a week earlier. LargeCap Consumer Discretionary was the best performer, with an increase of 6.4%, followed by SmallCap Communication Services (4.5%) and SmallCap Consumer Discretionary (4.4). Among the worst performers for the week were LargeCap Health Care 0.9%, followed by LargeCap Utilities (-0.5) and SmallCap Financials (-0.3). Looking at performances so far in 2023, LargeCap's 6.0% gain is trailing those of SmallCap (7.9) and MidCap (7.8) as 30 of the 33 sectors are higher ytd. The top sector performers in 2023: SmallCap Communication Services (17.6), SmallCap Consumer Discretionary (15.6), LargeCap Communication Services (14.8), LargeCap Consumer Discretionary (14.5), and MidCap Communication Services (12.7). Here are 2023's biggest laggards: LargeCap Health Care (-2.4), LargeCap Utilities (-2.3), LargeCap Consumer Staples (-2.2), MidCap Utilities (0.1), and SmallCap Utilities (0.6).

S&P 500 Sectors and Industries Performance (*link*): Nine of the 11 S&P 500 sectors rose last week, and five outperformed the composite index's 2.5% gain. That compares to a 0.7% decline for the S&P 500 a week earlier, when three sectors rose and four outperformed the index. Consumer Discretionary was the best performer, with a gain of

6.4%, followed by Tech (4.1), Communication Services (3.3), Real Estate (2.8), and Financials (2.5). Health Care was the worst performer, with a decline of 0.9%, followed by Utilities (0.5), Consumer Staples (0.4), Materials (0.7), Energy (0.8), and Industrials (2.1). Looking at 2023's performance so far, the S&P 500 is up 6.0% ytd with five sectors outperforming the index and eight higher for the year. The best ytd performers: Communication Services (14.8), Consumer Discretionary (14.5), Tech (9.8), Real Estate (9.2), and Materials (7.3). These are 2023's worst performers: Health Care (-2.4), Utilities (-2.3), Consumer Staples (-2.2), Industrials (2.9), Energy (.2), and Financials (5.8).

S&P 500 Technical Indicators (*link*): The S&P 500 improved last week relative to its 50-day moving average (50-dma) and 200-day moving average (200-dma). The index was above its 50-dma and 200-dma for a third week, but has only been above its 200-dma four times in the past 36 weeks. It had been above its 200-dma for 81 straight weeks through early February. The S&P 500's 50-dma moved higher as the index improved to a seven-week high of 1.0% above its now-rising 50-dma from 1.0% above its falling 50-dma a week earlier. That compares to a four-month low of 10.6% below at the end of September, a 23-month high of 8.7% above the index's rising 50-dma in early August, and 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 a 12-month high of 3.4% above its falling 200-dma, up from 0.7% above a week earlier. That's well above its 26-month low of 17.1% below its falling 200-dma in mid-June and down sharply from 10.8% above its rising 200-dma in November 2021. 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 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 fell for a 38th straight week, but its pace of decline has slowed since October, when it was falling at its fastest rate since July 2009.

S&P 500 Sectors Technical Indicators (*link*): Eight of the 11 S&P 500 sectors are trading above their 50-dmas, up from seven above a week earlier. The three sectors still trading below their 50-dma: Consumer Staples, Health Care, and Utilities. Nine sectors have a rising 50-dma now, up sharply from five a week earlier. The two with their 50-dmas still falling: Consumer Staples and Health Care. Looking at the more stable longer-term 200-dmas, Communication Services, Real Estate, and Tech turned positive w/w, leaving these three sectors still below that measure: Consumer Discretionary, Consumer Staples, and Utilities. However, just three sectors trade above their 200-dma. The rising 200-dma club has three members now, as Energy welcomed Financials and Industrials in the latest week.

US Economic Indicators

GDP (*link*): Real GDP expanded 2.9% (saar) during Q4 after rising 3.2% during Q3, which followed declines of 0.6% and 1.6% the prior two quarters. Consumer spending and inventory investment accounted for much of the increase. *Real consumer spending* increased 2.1% (saar), averaging quarterly gains of 1.9% during 2001. Real consumer goods consumption posted its first gain in four quarters, climbing 1.1% (saar), led by a 1.5% gain in nondurable goods consumption; durable goods spending ticked up only 0.5%. Services consumption continued to set new record highs, advancing 2.6% (saar) last quarter. Meanwhile, *real gross private domestic investment* increased 1.4% (saar) after contracting 9.6% and 14.1% the prior two quarters, as real inventory investment increased sharply to $129.9 billion (saar) from $38.7 billion during Q3. *Nonresidential investment* inched up by 0.7% (saar), following a 6.2% jump during Q3, while residential investment continued to contract at a double-digit rate, falling 26.7% last quarter. Within nonresidential investment, intellectual property products (5.3%, saar) continued to record impressive gains, while equipment (-3.7) fell last quarter and structures (0.4) stabilized after plummeting the prior six quarters. Meanwhile, *real net exports of goods & services* narrowed for the fourth straight quarter, as imports dropped 4.6% and exports fell 1.3%. (Imports are a subtraction in the calculation of GDP, so imports contributed positively.)

Contributions to GDP Growth (*link*): Inventory investment and consumer spending were the biggest positive contributors to real GDP during Q4, adding 1.46ppts and 1.42ppts, respectively, while residential investment (-1.29) was a big drag once again. The biggest contribution in *consumer spending* was services consumption (1.16ppts), followed by nondurable (0.22) and durable (0.04) goods consumption, respectively. Trade contributed 0.56ppt to Q4 real GDP, with imports (0.71) contributing positively and exports (-0.15) negatively. Government spending (0.64) added to real GDP growth for the second consecutive quarter after contributing negatively the first half of the year, with both federal (0.39) and state & local government (0.25) spending in the plus column. Nonresidential fixed investment added 0.09ppt to real GDP, as a positive contribution from intellectual property products (0.28) more than offset the negative contribution from equipment (-0.20) spending; structures contributed only 0.01ppt.

Durable Goods Orders & Shipments (*link*): Durable goods orders in December blew past forecasts, soaring to a new cyclical high, increasing at more than double consensus expectations. Billings rebounded 5.6% (vs 2.5% estimate) following a 1.7% drop in November, and excluding defense orders were up 6.3%. Last month's increase in total durable goods orders was led by a 16.8% jump in transportation orders (mostly aircraft); excluding transportation orders, the headline measure slipped 0.1%. Meanwhile, core *capital goods orders* (a proxy for future business investment) has been moving sideways since reaching a record high last August, ticking down 0.2% last month after no change in November—but was just 0.7% below the August level. *Nondefense capital goods shipments excluding aircraft* (used in calculating GDP) contracted for the second month since reaching a record high in October, slipping 0.4% in December and 0.6% during the two months through December.

Regional M-PMIs (*link*): Four Fed districts (New York, Philadelphia, Kansas City, and Richmond) now have reported on *manufacturing activity* for January. Collectively, they show that activity contracted for the sixth successive month to a 32-month low of –13.5 (from -7.0 in December). Activity in the New York (to -32.9 from -11.2) area deteriorated sharply, while Richmond's (-11.0 from 1.0) swung from positive to negative; those declines were partly offset by a narrowing of declines in the Philadelphia (-8.9 from -13.7) and Kansas City (-1.0 from -4.0) areas, with the latter looking about to swing positive. *New orders* (-18.5 from -11.2) fell for the ninth month, sliding at its fastest pace since spring 2020, with billings in the New York (-31.1 from -3.6) and Richmond (-24.0 from -4.0) regions plunging, while both the Philadelphia (-10.9 from -22.3) and Kansas City (-8.0 from -15.0) measures fell at half of December's pace. *Employment* (3.7 from 5.0) gains slowed for the third successive month, from 10.4 in October, as hirings in the Philadelphia (10.9 from -0.9) region swung from negative to positive, while the Richmond (-3.0 from 3.0) region saw a swing from positive to negative, New York hirings (2.8 from 14.0) slowed to a near standstill, and Kansas City's was unchanged at 4.0. T*urning to prices*, the prices-paid and -received measures for the New York, Philadelphia, and Kansas City regions 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. Looking at *prices-paid* indexes, the New York measure is decelerating again after a brief acceleration, easing to 33.0 this month—its lowest since November 2020—and down sharply from its record-high 86.4 last April, while Richmond's (79.1 from 90.8) is down sharply from its record high of 150.1 last May. Philadelphia's has been on a decelerating trend since reaching its cyclical high of 83.6 in November 2021 (which wasn't far from its record high of 91.1 in the 1970s), easing to a 29-month low of 24.5 this month. Kansas City's (20.0 from 18.0) ticked up, but it's down sharply from its record-high 84.0 in October 2021 *Prices-received* indexes were mixed: New York's prices-received measure eased to 18.8, the lowest since January 2021, after a brief blip up; it was at a record high of 56.1 last March, while Richmond's (65.2 from 76.3) continued to slow from its record-high 103.1 last June. The Philadelphia measure edged up from 28.1 (which was the lowest since March 2021) to 29.9 this month, down from its record high of 65.8 in November 2021. Kansas City's (16.0 to 15.0) also ticked up, but was down sharply from its record high of 60.0 during August 2021.

New Home Sales (*link*): New home sales (counted at the signing of a contract) recorded its third straight increase in December as mortgage rates continued to fall, an encouraging sign. Sales jumped 2.3% last month and 12.0% during the three months ending December to 616,000 units (saar). Of the 616,000 *homes sold* in October, only 199,000 were completed, while 154,000 were not yet started and 263,000 units were under construction. Meanwhile, there were 461,000 *units for sale* last month, with only 71,000 units completed and 99,000 not yet started; 291,000 were under construction. At the current sales pace, it would take 9.0 months to run through the supply of new homes, down from 9.2 months in November; it was at 10.1 months last September—which was the highest since April 2009.

Pending Home Sales (*link*): "This recent low point in home sales activity is likely over," noted Lawrence Yun, NAR's chief economist, though he went on to say, "Mortgage rates are the dominant factor driving home sales, and recent declines in rates are clearly helping to stabilize the market." The *Pending Home Sales Index* (which tracks sales when a contract is signed but the transaction has not yet closed) rose for the first time in seven months, by 2.5% in December, following a six-month slide of 15.2%. *Regionally*, pending home sales rose in two regions and fell in two regions on a monthly basis, but all four contracted on a yearly basis; here's the tally: West (6.4% m/m & -37.5% y/y), South (6.1 & -34.5), Midwest (-0.3 & -30.1), and Northeast (-6.5 & -32.5).

Consumer Sentiment Index (*link*): Consumer sentiment improved for the sixth time in seven months in January, though remained low from a historical perspective. Final data for December show *overall consumer sentiment* rose for the sixth time in seven months, by 5.2 points m/m and 14.9 points over the period, to 64.9, confirming its preliminary reading, with both the present situation and expectations components moving higher. The *present situation component* jumped 9.0 points in January to 68.4—up 14.6 points from its recent low of 53.8 last June—while the *expectations component* rose for the second month, by 2.8 points m/m and 7.1 points over the period, to 62.7. It's up 15.2 points from its recent low of 47.5 last July. Joanne Hsu, director of the survey, warned: "The debt ceiling debate looms ahead and could reverse the gains seen over the last several months; past debt ceiling crises in 2011 and 2013 prompted steep declines in consumer confidence." The *one-year* *expected inflation rate* eased to 3.9% in January (lowest since April 2021), though remains well above its 2.3% to 3.0% range recorded during the two years prior to the pandemic. It peaked at 5.4% last March and April. The *five-year expected inflation rate* was unchanged at 2.9% this month—remaining within the narrow 2.9% to 3.1% range during 17 of the last 18 months—above its 2.2%-2.6% range seen in the two years pre-pandemic. Hsu also cautioned, "Consumers continued to exhibit considerable uncertainty over both long and short-term inflation expectations, indicating the tentative nature of any declines."

Personal Consumption Deflator (*link*): December's PCED rose 0.1%, matching November's gain and easing from October's 0.4%. Meanwhile, core prices rose 0.3%, following gains of 0.2% and 0.3% the previous two months; prices were up 0.5% and 0.6% in September and August, respectively. The yearly headline rate slowed to 5.0%, down from June's 7.0% peak—which was the highest reading since the end of 1981; it was at 6.0% a year ago. The yearly core rate slowed for the third month to 4.4%; it peaked at 5.4% during February and March of last year. On a *three-month annualized* basis, the core rate rose 2.9% (saar) in December, slowing steadily from 5.1% last October. The three-month rate for durable goods contracted 6.8% (saar) in December, down from 5.1% in June, while the three-month rate for core nondurable goods prices ticked up to 1.4% (saar) after slowing from 4.9% in August to 1.2% in November. Meanwhile, services prices ex energy slowed for the second month to 5.0% (saar), over the three-month period, from 6.3% in October, which was the fastest three-month pace since December 2001. The three-month annual rates for consumer durable goods (-6.8%, saar & 1.4% y/y) and consumer core nondurable goods (1.4 & 3.3) were below their yearly rates, while the three-month gain in consumer core services (5.0 & 5.0) matched its yearly rate. *PCED components for which three-month rates lag yearly rates*: gasoline & other energy products (-26.7% & 1.4%), used motor vehicles (-31.0 & -8.8), video audio & information processing (-15.9 & -4.5), furniture & home furnishings (-8.5 & 4.7), prescription drugs (-0.7 & 1.8), clothing & footwear (-0.2 & 3.0), professional & other services (0.0 & 5.6), hospitals (1.5 & 3.0), new motor vehicles (1.5 & 6.0), personal care products (2.8 & 7.9), food & nonalcoholic beverages purchased for off-premise consumption (3.7 from 12.1), tobacco (3.5 & 5.5), motor vehicles & parts (3.2 & 8.7), transportation services (5.9 & 13.2), and airfares (8.8 & 18.8). *PCED components for which three-month rates exceed yearly rates*: lodging away from home (25.7 & 3.2), tenant rent (9.1 & 8.3), recreation services (8.7 & 5.6), owner-occupied rent (8.4 & 7.5), alcoholic beverages purchased for off-premise consumptions (6.7 & 5.5), sports & recreational vehicles (6.5 & 1.2), household appliances (3.9 & -0.2), and physician services (2.6 & 0.2). Meanwhile, the three-month and yearly rates virtually matched for education services (2.4 & 2.5).

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