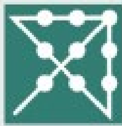

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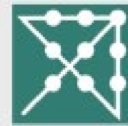

MORNING BRIEFING
May 15, 2023

Disintermediation, Disinflation & Dystopia

Check out the accompanying chart collection.

Executive Summary: The Fed sought to allay fears of bank runs when it provided backstop funds to banks. Consider the fears allayed—so far, at least. The disintermediation threat hasn't descended; it hasn't wrought a credit crunch, a recession, or widespread economic destruction. Now if fears aren't stoked by further talk of bank runs, maybe, just maybe, the threat will go away. … Also: The high-inflation saga's loose ends all seem to be resolving now in a Hollywood-style happy ending. … And: The latest episode of the debt ceiling drama playing out in Washington is ably narrated by Capital Alpha's Jim Lucier. … Lastly: Dr. Ed reviews "Beef" (+ +).

YRI Weekly Webcast. Join Dr. Ed's live webcast with Q&A on Mondays at 11 a.m. EST. You will receive an email with the link one hour before showtime. Replays of the weekly webcasts are available *here*.

Disintermediation: A Quiet Place. "*A Quiet Place*" is a 2018 science fiction horror film. The plot focuses on the Abbott family, which struggles to survive in a post-apocalyptic world inhabited by blind extraterrestrial creatures with an acute sense of hearing. The Abbotts must avoid making any noise or risk sure death. They communicate by sign language.

Fed officials are hoping that they've succeeded in quieting any noise about deposit runs in the banking system. To contain the banking crisis that erupted during the week of March 10, the Fed introduced the *Bank Term Funding Program* (BTFP) on March 12. It was designed to supplement the traditional discount window as a source of liquidity to the banking system through March 11, 2024:

"The BTFP offers loans of up to one year in length to banks, savings associations, credit unions, and other eligible depository institutions pledging any collateral eligible for purchase by the Federal Reserve Banks in open market operations, such as U.S. Treasuries, U.S. agency securities, and U.S. agency mortgage-backed securities. These assets will be valued at par. The BTFP will be an additional source of liquidity against high-quality securities, eliminating an institution's need to quickly sell those securities in times of stress."

The March 12 *press release* stated that the BTFP "will make available additional funding to

eligible depository institutions to help assure banks have the ability to meet the needs of all their depositors." The Fed can't insure all deposits. That would require an act of Congress authorizing the FDIC to raise the current insured deposit limit of $250,000. So instead, the Fed has assured depositors that their banks are safe because they have access to plenty of liquidity.

So far, so good:

(1) *The Fed's total loans to the banking system* jumped from only $15.1 billion on March 8 to peak at $357.9 billion on March 29. The figure was down slightly to $309.0 billion on May 10 (*Fig. 1* and *Fig. 2*). Primary credit (a.k.a. discount window borrowing) plunged from a peak of $117.0 billion on March 22 to just $4.6 billion on May 10. Other credit extensions to support the FDIC's efforts to restructure the three failed banks (so far) rose to $214.4 billion.

(2) *Deposit outflows* so far haven't suggested a run as much as a walk. From March 8 through May 3, deposits are down $449.2 billion (*Fig. 3*). Some of that drop was offset by a $219.8 billion decline in securities held by the banks and a $508.2 billion increase in their borrowing. These figures undoubtedly were skewed by the three failed banks.

(3) *The volume of loans* being made is the key indicator of whether the banking crisis to date turns into an apocalyptic credit crunch. Again, so far, so good: From March 8 through May 3, loans are up $24.7 billion (*Fig. 4*). Both residential real estate and consumer loans rose to new record highs on May 3. Commercial & industrial loans and commercial real estate loans rose to record highs just before the banking crisis started. They've edged down since then but remain near their record highs.

(4) *Bottom line: "Shhhh!"* So let's not have any more talk about deposit runs. Let's keep very quiet about this matter so as not to provoke a killer credit crunch and a recession. We may signal but not verbalize "Shhhh!" by putting our index fingers in front of our lips.

Disinflation: It's a Wonderful Life. Will the latest inflation story have a happy ending, as did "*It's A Wonderful Life*," the 1946 Christmas classic starring Jimmy Stewart and Donna Reed?

Financial markets anticipated an unhappy ending during the first 10 months of last year. Over that period, bond investors (like Fed officials) realized that they were behind the inflation curve. The 10-year Treasury yield rose from 1.63% at the start of 2022 to peak at 4.25% on October 24 (*Fig. 5*). That happened as the CPI inflation rate soared from a

lockdown low of 0.1% y/y on May 2020 to peak at 9.1% on June 2022.

It has fallen every single month since then to 4.9% in April of this year. The bond yield has remained below its October 24 peak, falling to 3.46% at the end of last week. If disinflation continues at this pace, the CPI inflation rate could be down to 3.0%-4.0% in time for Christmas. That's our wonderful life forecast.

Stock investors seem to be coming around to this happy outlook as well. The forward P/E of the S&P 500 plunged from 21.5 on January 3, 2022. It bottomed at 15.1 on October 12 last year. It was back up to 18.0 on Friday (*Fig. 6*).

Let's review a few of the happy-ending inflation indicators:

(1) *Disinflation correlations.* Services account for 61.5% of the CPI. So it isn't surprising that the CPI inflation rate on a y/y basis is highly correlated with the ISM Services prices paid index pushed ahead by three months (*Fig. 7*). The actual latter series fell from a peak of 84.5 during December 2021 to 59.6 during April 2023. That implies that the CPI inflation rate is on track to fall to 3.0% by July!

But it's a little hard to believe that will happen since rent isn't reflected in the ISM measure but is a major component of the CPI. Rent inflation seems to be peaking only now and might take a while to fall back down to its pre-pandemic pace. Christmas occurs in December, not July, but maybe it will start early this year for investors.

Christmas might come in September if we can rely on the correlation between the CPI inflation rate and the percent of small business owners planning to raise their average selling prices their average selling prices, pushed ahead by five months (*Fig. 8*). The actual latter series peaked at a record 54% during November 2021 and fell to 21% in April 2023. That suggests that the CPI inflation rate could fall to 3.0% by September. Ho! Ho! Ho!

(2) *PPI and CPI for personal consumption*. While the CPI was still up 4.9% through April, the PPI for personal consumption was up only 2.7% y/y through April, little changed from March's 26-month low of 2.5%, and down dramatically from last year's peak of 10.4% during March 2022 (*Fig. 9*). The PPI does not include rent either.

(3) *Rent.* The CPI measures of rent inflation remained elevated during April, with primary residence at 8.8% and owners' equivalent rent at 8.1% (*Fig. 10*). However, the three-month annualized rates for both fell to 7.3% and 6.9%, suggesting that both have peaked.

(4) *Food & energy.* Clearly peaking is the CPI foods index (*Fig. 11*). The y/y rate was 7.7% through April, but the three-month annualized rate was down to 1.7%. The CPI energy index peaked at 41.6% y/y during June 2022. It was down to -5.1% in April.

(5) *Core services inflation excluding housing.* Fed officials are particularly concerned about the stickiness of the core services PCED ex-housing costs inflation rate (*Fig. 12*). It has been stuck around 4%-5% for the past 11 months through March. The comparable series for the CPI is for services excluding energy and shelter. It peaked at 6.7% during September 2022 and fell to 5.0% through April.

Dystopia: On the Beach. "*On the Beach*" is a 1959 post-apocalyptic science fiction drama film starring Gregory Peck, Ava Gardner, Fred Astaire, and Anthony Perkins. It is based on Nevil Shute's 1957 novel with the same name depicting the aftermath of a nuclear war. Today, our fearless political leaders in Washington may be on the brink of a disaster of their own making if they don't come an agreement soon on raising the debt limit.

Our good friend Jim Lucier and his colleagues at *Capital Alpha Partners* do an outstanding and brave job of watching Washington for investors. The following is Jim's May 11 take on the outlook for the debt ceiling negotiations:

(1) *Bueller, Bueller …* Investors seem surprisingly relaxed about the Treasury Department's projected June 1 X-date. But members of Congress are focused on a different deadline: How to get out of town for Memorial Day. The Senate is set to leave on May 19, the House on May 25. Neither comes back until June 6. That means that if there is to be a short-term extension of the debt ceiling deadline, as we expect, both houses need to approve it before they leave. Only then will members be free to go on vacation.

It's the Senate's turn to move first. One reason House Speaker Kevin McCarthy (R-CA) seems to say (for now) that the House won't approve a short-term extension is that House members are still in a resting phase following their close vote to pass the House debt limit package on April 26. We think the House will be surprisingly ready to act once the Senate takes its turn. As we have noted previously (see May 3: *When the Dust Settles*), action, pause, and reaction is basically the way that Congress works.

The Big Four congressional leaders met with President Joe Biden on May 10. One House Republican reportedly called the meeting "a total waste of time." We're delighted because that was the optimal outcome. The meeting had to happen, but there was no particular need

for anything to be accomplished by it. Things could have gone much worse. It might have devolved into a shouting match. Even worse, Biden could have taken the opportunity to lecture House Republicans, as President Obama did in 2011. It's in the President's interest not to hector the Republicans, causing them to dig in their heels against a deal, as we think House Republicans will allow a deal to pass the House with Democratic votes. But it needs to be the right deal.

Staff is meeting on Capitol Hill to begin negotiations. This is great, in our opinion. What they're talking about, no one knows. It could be a spending agreement, as Democrats want; or a spending agreement linked to increasing the debt limit, as Republicans prefer. The key thing is that they are talking, and they are talking about a spending agreement. The genie is out of the bottle.

(2) *Back to the future.* The Big Four will meet again at the White House on Friday, May 12. If there's a framework agreement by then, so much the better. It would be a skeletal agreement at best, with perhaps three elements: base year (fiscal 2022 or fiscal 2023), growth factor (perhaps 1%), and some additional bell or whistle. A framework agreement would make voting on an extension easier—as, indeed, an extension will be necessary because working out the additional details could take weeks or months. (Note: The May meeting 12 was postponed to this week amid constructive comments from both sides about "progress" being made. Jim is encouraged by this and thinks we could see a framework agreement that is more comprehensive than the bare-bones deal he outlines here.)

As we have written previously (see May 2: *Take a Chill Pill*), we could see an extension of 30, 60, or 90 days; but in our view, 30 or 60 days will not be enough, and 90 won't work because the end of that period lands on Labor Day Weekend. So we think a longer 120-day extension to September 30 (or several short extensions to that date) is possible. But what matters more to us than the length of the extension is that once talking starts, the gangs break loose. This would be a literal gang on the Senate side and an organized caucus such as the Problem Solvers on the House side.

Senate Majority Leader Charles Schumer (D-NY) has been able to keep the Senate Democrats united in the position that no talks are needed; a clean debt limit increase is the only option. But once there is a deal in the making, it is going to be harder and harder for Schumer to keep his members out of it.

Collective Washington, us included, is shocked that McCarthy managed to get a debt limit package through the House. He got it through on a tight vote and with dubious expedients,

but no one expected him to get it done at all, let alone in April, and to emerge with his political standing intact if not enhanced. The White House and Senate Democrats had not planned for this; they're still processing the information and deciding what to do in response. The Hive Mind is buzzing for a while.

But there's more information requiring processing, which may not yet be fully factored in on the Senate side. That information came to us as a second shock last week. After some initial doubt, even after the House passed the Limit, Save and Grow Act (H.R. 2811), we have concluded that McCarthy is secure in his position as speaker—at least more secure than we'd expected. We think that short of some extreme tail-risk event, McCarthy is likely to retain his position as speaker until the end of this Congress. We are hearing this from more and more Republican sources on the Hill.

This does not mean that McCarthy could accept just any bill from the Senate side, but we think that any bipartisan bill that gets 60 Senate votes (including nine Republicans) and the support of more than half the House Republican Conference is a bill that McCarthy could get through the House.

(3) *We've seen this movie before.* Since such a bill would need up to 51 Democratic votes on the Senate side, we don't see House Democrats voting against it *en masse*. As a result, we think the debt limit drama this year will look more like a movie we've seen before. Last week (*May 2*), we wrote about "Ferris Bueller's Day Off." This week, we're reminded of another 1980s teen classic, "Back to the Future."

If those who see a quick deal coming are correct, then Hallelujah. A framework deal by this weekend or soon would be great too. We think 2023 ultimately will play out like 2011, except that the final product will be less ambitious, its construction ramshackle by comparison, and its effectiveness more doubtful. Though we see the debt ceiling lift happening by September 30, we think that appropriations could take until Christmas to work out, or longer, as they often do. Then we'd worry about a greater risk than usual of long-term continuing resolutions in place of one or several appropriations bills.

There's still significant risk of failure, but that risk seems to be diminishing over time, as the financial markets may be telling us already.

Movie. "Beef" (+ +) (*link*) is a Netflix mini-series about the many potential adverse consequences of getting into a road-rage beef with another driver. In this case, the altercating male and female drivers have lots of homegrown frustrations that inflame their

anger on the road. In other words, they have much in common. Needless to say, their hostile incident only worsens their personal woes. The moral of the story is: Deal with your rage at home. Don't take it on the road. If you do, you run the risk of instigating a fight with someone as nuts as you are. This series is reminiscent of "Falling Down" (1993), another road-rage movie starring Michael Douglas.

Calendars

US: **Mon:** Empire State Manufacturing Index -3.7; TIC Net Long-Term Transactions; Barkin; Bostic; Cook; Kashkari. **Tues:** Retail Sales Total, Core, Control Group 0.7%/0.4%/0.3; Industrial & Manufacturing Production -0.1%/0.1%; Capacity Utilization 79.7%; Business Inventories 0.1%; Housing Market Index 45; API Weekly Crude Oil Inventories; IEA Monthly Report; Williams; Barr; Bostic; Mester. (Bloomberg estimates)

Global: **Mon:** Eurozone Industrial Production -2.5%m/m/0.9%y/y; Eurozone Reserve Assets; Germany WPI; Spain Consumer Confidence 78.9; Japan Machine Tool Orders; China Retail Sales 20.1%y/y; China Industrial Production 10.1%y/y; China Fixed Investment 5.2%y/y; China Unemployment Rate; China FDI; Australia Westpac Consumer Sentiment -1.7%; China NBS Press Conference; RBA Meeting Minutes; European Union Economic Forecasts; Eurogroup Meetings; Nagel; Pill. **Tues:** Eurozone GDP 1.3%y/y; Germany Employment; Eurozone Trade Balance; Germany ZEW Economic Sentiment -5.5; Italy CPI 0.8%m/m/8.8%y/y; UK Average Earnings Including & Excluding Bonus 5.8%/6.8%l UK Employment Change 3m/3m 160k & Unemployment Rate 3.8%; UK Labor Productivity; Canada CPI 0.4%m/m/4.4%y/y; Japan GDP 0.1%q/q/0,7%y/y; China Manufacturing Sales 0.7%; Lagarde; Tuominen. (Bloomberg estimates)

Strategy Indicators

Global Stock Markets Performance (*link*): The US MSCI index fell 0.2% last week and moved deeper into a correction at 15.4% below its record high on December 27, 2021. The US MSCI ranked 16th of the 48 global stock markets that we follow in a week when 15 of the 48 countries rose in US dollar terms. The AC World ex-US index fell 0.9% and also remained in a correction, albeit at 16.4% below its June 15, 2021 record high. EM Latin America was the best regional performer with a 2.7% gain, ahead of EMEA (1.5%), EM East Europe (0.1), BIC (-0.7), and EAFE (-0.9). EMU was the worst performing region last

week, with a decline of 1.7%, followed by EM Asia (-1.3). Turkey was the best-performing country last week, with a gain of 11.2%, followed by Argentina (4.3), Chile (4.2), Denmark (4.1), and Brazil (4.0). Among the 27 countries that underperformed the AC World ex-US MSCI last week, South Africa posted the steepest decline, of 6.9%, followed by Peru (-6.5), Pakistan (-5.0), Austria (-3.7), and Belgium (-3.2). Looking at 2023's performance so far, the US MSCI is up 7.5% as its ytd ranking rose three places w/w to 20/48. The AC World ex-US's ytd gain of 6.9% is trailing that of the US again, with 34/48 countries now in positive territory. EM Eastern Europe is the best regional performer ytd, with a gain of 17.2%, followed by EMU (14.1), EAFE (9.4), and EM Latin America (8.7). The regional laggards so far in 2023: BIC (-1.5), EM Asia (1.4), and EMEA (3.1). This year's best ytd country performers: the Czech Republic (41.8), Mexico (25.1), Ireland (22.9), Greece (22.4), and Denmark (18.5). Here are the worst-performing countries of the year so far: Pakistan (-29.9), Colombia (-12.4), Norway (-10.7), Turkey (-10.1), and South Africa (-9.6).

S&P 500/400/600 Performance (*link*): All three of these indexes moved lower for a second straight week. LargeCap dropped 0.3% w/w, less than the declines for MidCap (-1.2) and SmallCap (-1.7). At Friday's close, SmallCap was still in a bear market, while LargeCap and MidCap remained in a correction. LargeCap finished the week at 14.0% below its record high on January 3, 2022, MidCap at 16.4% below its record high on November 16, 2021, and SmallCap at 23.6% below its November 8, 2021 record high. Six of the 33 LargeCap and SMidCap sectors moved higher for the week compared to 11 rising a week earlier. LargeCap Communication Services was the best performer with a gain of 4.3%, ahead of MidCap Consumer Staples (1.3%), MidCap Energy (1.0), SmallCap Tech (0.9), and LargeCap Consumer Discretionary (0.6). Among the worst performers for the week were SmallCap Financials (-4.2), MidCap Communication Services (-3.9), SmallCap Energy (-3.4), MidCap Financials (-2.8), and SmallCap Health Care (-2.5). Looking at performances so far in 2023, LargeCap, with a 7.4% gain, remains well ahead of MidCap (0.1) and SmallCap (-3.3); 19 of the 33 sectors are higher ytd. The top sector performers in 2023: LargeCap Communication Services (26.9), LargeCap Tech (22.3), LargeCap Consumer Discretionary (14.9), SmallCap Consumer Discretionary (8.8), and MidCap Consumer Staples (8.6). Here are 2023's biggest laggards: SmallCap Financials (-23.5), SmallCap Energy (-17.0), MidCap Energy (-15.4), MidCap Financials (-14.4), and LargeCap Energy (-10.2).

S&P 500 Sectors and Industries Performance (*link*): Two of the 11 sectors rose last week, and three outperformed the composite index's 0.3% decline. That compares to a 0.8% decline for the S&P 500 a week earlier, when two sectors rose and six outperformed the index. Communication Services was the best performer, with a gain of 4.3%, followed

by Consumer Discretionary (0.6), and Consumer Staples (0.0). Energy was the worst performer, with a 2.2% decline, followed by Materials (-2.0), Financials (-1.3), Health Care (-1.2), Industrials (-1.2), Real Estate (-1.0), Tech (-0.3), and Utilities (-0.3). Looking at 2023's performance so far, the S&P 500 is up 7.4% ytd, with just three sectors outperforming the index and six higher for the year. The best ytd performers: Communication Services (26.9), Tech (22.3), and Consumer Discretionary (14.9). These are 2023's worst performers: Energy (-10.2), Financials (-7.0), Health Care (-2.9), Utilities (-2.5), Real Estate (0.0), Industrials (0.1), Materials (0.4), and Consumer Staples (3.2).

S&P 500 Technical Indicators (*link*): The S&P 500 fell 0.3% last week and weakened relative to its 50-day moving average (50-dma) and 200-day moving average (200-dma). The index was above its 50-dma for a seventh week and its 200-dma for an eighth week. It had been above its 200-dma for eight weeks through early March in its longest positive 200-dma streak since it was above for 81 straight weeks through January 2021. The S&P 500 dropped to 1.6% above its rising 50-dma from 2.3% above a week earlier and a 10-week high of 3.4% above the week before that. That also compares to a 20-week low of 3.6% below at the beginning of March, 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 3.9% above its now-falling 200-dma, down from 4.2% above its rising 200-dma a week earlier and a 10-week high of 5.1% above the week before that. That also compares to a nine-week low of 0.3% in early March and a 13-month high of 5.1% above in early February. The S&P 500 is well above its 26-month low of 17.1% below its falling 200-dma in mid-June and compares to 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 50-dma moved higher for an eighth week, but the 200-dma turned down w/w and has risen in just 12 of the past 52 weeks.

S&P 500 Sectors Technical Indicators (*link*): Seven of the 11 S&P 500 sectors are trading above their 50-dmas, unchanged from a week earlier and down from all 11 sectors above the week before that. The four sectors trading below their 50-dma are Energy, Financials,

Industrials, and Materials. Six sectors have a rising 50-dma, unchanged from a week earlier. The five sectors with falling 50-dmas: Energy, Financials, Industrials, Materials, and Real Estate. Looking at the more stable longer-term 200-dmas, the positive club dropped to six members w/w as Materials joined Energy, Financials, Real Estate, and Utilities as the only sectors trading below their 200-dmas. The rising 200-dma club remained steady w/w at seven members; the remaining four, with falling 200-dmas, are: Consumer Discretionary, Financials, Real Estate, and Utilities.

US Economic Indicators

Producer Price Index (*link*): April's *headline PPI* posted its smallest yearly increase since January 2021, advancing a less-than-expected 0.2% last month, following a 0.4% decline in March and no change during February. The yearly rate has been in a freefall since peaking at a record-high 11.7% last March, sinking to a 27-month low of 2.3% this April. *Core prices*—which excludes food, energy, and trade services—edged up 0.2% last month, following gains of 0.1% and 0.2% the prior two months, slowing from January's 0.6% gain; the yearly rate eased to a 25-month low of 3.4%—half of March 2022's record-high 7.1%. *Final demand goods* edged up 0.2% after falling three of the prior four months by 1.6%; gasoline prices' 8.4% rebound from recent months' declines was a major factor. The yearly rate eased further to a 28-month low of 0.8% from last June's record high of 17.6%. *Final demand services* posted its biggest monthly increase in five months in April (0.3%) after posting its first decline since November 2020 in March (-0.1), with the yearly rate ticking up to 3.0% from March's 25-month low of 2.8%; it was at a record high of 9.4% last March. The PPI for *personal consumption* climbed 0.4% in April after falling 0.5% in March and posting no gain in February; that pushed the yearly rate up slightly to 2.7% after easing steadily from last March's 10.4% record high to 2.5% this March—which was the lowest since January 2021. The yearly rate for *personal consumption excluding food & energy* ticked up to 3.4% in April, after easing from a record-high 8.1% last March to a two-year low of 3.1% this March. The core measure rebounded 0.3% in April from a 0.1% decline in March—which was the first monthly decrease since November 2020. Looking at *pipeline prices*, the yearly rate for intermediate goods prices slipped further below zero in April (-3.2% y/y) after dropping below in March for the first time since November 2020 (-1.0); it was at a cyclical high of 26.6% during November 2021. The yearly crude goods rate was in negative territory for the third successive month, falling 19.4% y/y in April, the steepest yearly decline since spring 2020; the rate was at a recent peak of 50.7% last June.

Import Prices (*link*): After falling in eight of the prior nine months, import prices climbed in

April, boosted by the first increase in fuel prices since June 2022. *Total import* prices ticked up 0.4% in April, after plummeting 5.9% during the nine months through March, with the yearly rate in negative territory for the third consecutive month, holding at -4.8%; it peaked at 13.0% last March. *Fuel prices* rebounded 4.5% in April after a nine-month plunge of 37.1%, with the yearly rate edging up to -25.6% y/y in April after plummeting from 130.1% in April 2021 to -28.2% by this March. *Nonpetroleum import prices* fell for the third consecutive month, by a total of 1.1%, after a two-month gain of 1.2%; these prices had dropped 2.2% during the seven months through November. The yearly rate turned negative in March (-1.6% y/y) for the first time since mid-2020 and widened to -2.1% in April; the rate had peaked at 8.1% last March. Here's the yearly rate in import prices for several industries from their recent respective peak rates: industrial supplies, which includes fuels & lubricants (to -17.0% from 55.2%); foods, feeds & beverages (0.2 from 15.7); capital goods (1.1 from 4.2); and consumer goods ex autos (-0.2 from 3.2).

Consumer Sentiment Index (*link*): "While the current incoming macroeconomic data show no sign of recession, consumers' worries about the economy escalated in May alongside the proliferation of negative news about the economy, including the debt crisis standoff," noted Joanne Hsu, director of the survey. *Overall consumer sentiment* fell for the second time in three months, sinking 5.8 points in mid-May and 9.3 points over the period, to a six-month low of 57.7; it was at a 13-month high of 67.0 in February. The *present situation component* also fell for the second time in three months, by 3.7 points m/m and 6.2 points over the period to a five-month low of 64.5. The *expectations component* fell 7.1 points and 11.3 points over those same periods to a 10-month low of 53.4. Turning to inflation, the *one-year expected inflation rate* ticked down to 4.5% in mid-May after climbing from 3.6% (lowest since April 2021) in March to a five-month high of 4.6% in April, remaining well above its 2.3%-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* rose for the second month to 3.2% in mid-May from 2.9% the prior four months, the highest rate since 2011; it had moved in a narrow 2.9%-3.1% range for 20 of the prior 21 months.

Global Economic Indicators

UK GDP (*link*): Real GDP weakened during the final two months of Q1, shrinking 0.3% in March and showing no growth in February following 0.5% growth in January; taken together, the quarter represented only a 0.1% uptick from the previous three-month period. Exceptionally wet weather hit consumer spending in March, with retail and car sales down sharply. In addition, public-sector strikes had an impact on growth during the month. The

service sector contracted 0.5% in March and 0.1% in February, following a 0.8% rebound in January from December's 0.8% shortfall. Service-sector output ticked up only 0.1% during the Q1, matching Q4's gain. *Within services*, the biggest declines in March were recorded in transportation & storage (-1.7%), wholesale and retail trade (-1.4), administrative & support services (-1.3), and accommodations & food services (-0.8). The *construction* sector increased 0.7% in March from the previous three-month period, as the 1.6% drop in activity during January was more than offset by gains of 2.6% and 0.2% during February and March, respectively. *Production* output in March expanded 0.7% after contracting 0.1% and 0.3% the prior two months, eking out only a 0.1% uptick versus the prior three-month span. Manufacturing expanded 0.5% on a rolling three-month basis, rising 0.7% in March, following gains of 0.1% and 0.3% the prior two months.

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