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Economic Indicators December 2021

By Kim W. Suchy

Late last year, the economy came grinding to a halt, then picked up early this year only to get stuck in the mud once again as supply shortages and labor disruptions reared their ugly heads. This is not just a domestic problem, the global economy is experiencing its own set of consequences.

Grocery stores have some limited items, ports are jammed waiting for goods to be moved and car manufacturers have halted production in spots due to chip shortages. Meanwhile prices are escalating on many goods and services and many increases are north of 10%. While we have heard over the last several months that the Fed has professed that this fast-paced inflation is transitory, the reality of what we now pay at the pump, at the stores and restaurants is forcing us to think otherwise. When we are *forced* to think otherwise, bad things can happen; especially when prices continue to escalate at the pace we experiencing and supply/production slows.

Consider production cutbacks from global car manufacturer Toyota who has cut recent production by more than a third from 2020 levels as shortages stalled its production process — as well as the firms that move their autos and trucks around the globe. Also consider the likes of Nike shoes which had to scale back output because migrant workers had to return home due to C19 concerns. Further, China, is confronting virus outbreaks and responding with targeted lockdowns. Its factory prices are rising at a 10% annual rate, the fastest in 30 years according to Bloomberg Economics.

So, production slowdowns coupled with rising prices places the Fed and Central Bankers across the globe with the possibility of dealing with stagflation. Let's call this, stagflation-light, as the last time the Fed dealt with this was back in the 70's when inflation ran hot, the economy slowed and the combined Fed & Treasury missteps were so entrenched that it took a few years to bail out of the storm. As we often hear, this time is different...or could be different. The Central Bankers know the causes of inflation and supply disruption. They also have a bit of a head start in staving off the root causes. Should supply chains disruptions free up and product delivered to ultimate

consumers sooner rather than later, the global economies should be able to circumvent surging prices and production slowdowns.

However, now we have another new concern to add to the mix, the Omicron variant. At the time of this writing, Fed Chair Powell warned Omicron would cause new supply-chain disruptions…this coupled with new travel restrictions in South Africa and Europe has sent the markets lower and has created a renewed fear of GDP slowdowns.

Fed Chair Powell in his testimony before Congress has been asked repeatedly to do what he can to ward off inflationary pressures yet in order to do so may require much more restrictive monetary practices; one's that may stabilize prices but impede employment growth or production. Powell certainly has the issues in the crosshairs, it's just a matter of what to shoot at first, and when.

There seems to be more we don't know than know at this stage, but concerns about supply chain issues are valid given fear of the new variant is already restricting travel. The most important unknown is vaccine viability against the new strain, not just whether vaccines prevent it, but also whether vaccines reduce symptoms.

Here is your look at developments in the global marketplace.

Positive Developments:

- The Federal Reserve Board reports that industrial production increased 1.6% in October after disruptions from Hurricane Ida and factories rushed to boost output to meet strong demand. The gains were broad-based, with every major category contributing to the rebound, easily beating the consensus expected gain of 0.9%.

- In China, Singles' Day 2021 was a reaffirmation of the promise of China e-commerce and the stocks of the main players (Alibaba and JD.com) rose immediately after the results came out on 11/13/21. Chinese consumers have an insatiable appetite for product. According to Alibaba Group Holdings, Alibaba and JD.com logged $139B of sales across their platforms on China's Singles Day shopping event, setting a new record.

- The Commerce Department reported that retail sales surged 1.7% in Oct. and have surged 14.8% yoy. This number is somewhat inflated by a 46.8% increase in gasoline prices, but the CPI has risen 6.2% (including gasoline sales) in the last year, so a 14.8% rise in retail sales is impressive, and bodes well for the holiday shopping season. Note, sales at online retailers surged 4% in October and electronics & appliance sales rose an impressive 3.8%. Restaurant and bar sales were flat in Oct., but they have risen 29.3% in the past 12 months.

- The Dept. of Labor reported that new claims for unemployment were essentially unchanged in the latest week, coming in at 268K, compared to a revised 269K in the previous week. Continuing unemployment claims were much more encouraging, coming in at 2.08M in the latest week, down significantly from a revised 2.21M the previous week.

Neutral Developments:

- According to FactSet, it is not unusual for companies to comment on subjects that had, or will have, an impact on their earnings and revenues in a given quarter. Of the SP500 companies, 342 have cited the term "supply chain" during their earnings calls for Q3 which is well above the five-year average of 178. In fact, this is the highest overall number of SP500 companies citing "supply chain" on earnings calls going back to at least 2010. The previous record was 292, which occurred in Q1 2020.

- The Magnificent 8 are the 8 stocks in the SP500 with the highest market capitalizations. They are Alphabet (Google), Amazon, Apple, Meta (Facebook), Microsoft, Netflix, NVIDIA, and Tesla. They are all in the S&P 500 Growth index. According to Yardeni Research, their aggregate market cap has soared from $1.2T at the start of 2013 to a record $12.0T to present. Over this same period, their market-cap share of the SP500 has risen from 8.9% to a record 30.0%. Their forward P/E was about 15 in early 2013. Since mid-2020, it has been volatile around 40. The forward P/Es of the S&P 500 with and without the Mag-8 currently are around 21 and 18. I guess the message here is that disruption in one or more of the Mag 8 could be problematic for the broad-based SP500.

- An interesting divergence is developing. The Census Bureau reported that retail sales hit another all-time high last month while consumer sentiment is at its lowest level in 10 years. There's no question consumers are worried about higher inflation, but that hasn't caused them to reduce spending yet. Demand for goods/services remains incredibly strong and consumers have been very insensitive thus far to rising prices. If and when that changes, we could have a troubling situation; stagflation.

- The C19 situation is changing ever so fast. In Sept., the world was on a strong trajectory to rid itself of C19 due to rising vaccination rates, lower trending caseloads, hospitalization, and mortality rates. Within the past few weeks, however, C19 cases are once again spiking, primarily across Europe, prompting a re-imposition of a national lockdown and mandatory vaccinations in Austria.

- A strong Dollar is a major *headwind* for profit margins of multinational corporations, especially those that generate more than 50% of their revenues from outside the U.S. As the Fed continues taper and rates edge higher, the path of least resistance for the Dollar remains higher. This structural dynamic is also *bullish* for companies where the majority of business is dollar-based or where goods and services are sold within the U.S. especially small and mid-cap companies.

- *Existing* home sales increased 0.8% in October to a 6.3M a/r. Sales are down 5.8% vs. a year ago. The median price of an existing home rose to $354K in October and is up 13.1% vs. a year ago. Average prices are up 8.2% vs. last year according to Census Bureau reports.

- Treasury yields *tend* to track inflation fundamentals. But today, yields are far below the current level of inflation. As you know, bond yields are elevated from the lows of earlier this, but they are still far below where they should be given the current level of inflation.

Negative Developments:

- Zillow estimates that rental costs for new tenants are up 9.2% in the past year and Apartmentlist.com estimates they have risen an even faster 15.8%, easily exceeding typical gains in the 3.0 to 4.0% range.

- Consumer prices continued to accelerate in October, rising at the fastest pace for any month in more than a decade and pushing the 12-mo. increase to 6.2%, the largest since 1990. Inflation is clearly becoming a problem and the Feds claim that it's "transitory" is wearing very this. The Bureau of Labor Statistics reported that energy, food, housing and new cars had monthly increases of 4.8%, 0.9%, 0.7% and 1.4% respectively.

  - Producer prices did not fare any better. In fact, Producer prices continue to rise at the fastest pace in decades, with little sign inflation pressures are going to ease. The producer price index rose 0.6% in October and is up 8.6% in the past year.

  - According to Charlie Bilello Research, here are commodity price increases yoy... Gasoline: +128% WTI Crude: +123% Heating Oil: +122% Brent Crude +113% Coffee: +101% Natural Gas: +81% Cotton: +67% Aluminum: +44% Corn: +43% Copper: +41% Sugar: +33% Wheat: +30% Soybeans: +18% Lumber: +17% Silver: -3% Gold: -6%.

  - The inflation issue transcends the globe. TD Economics reports that producer prices in Germany saw the highest yoy increase since 1951 at 18.4% in October. In the UK, CPI jumped to a 10-yr high, up 4.2% yoy in October, potentially pressuring the Bank of England to act at its December meeting.

- A report by the National Association of State Budget Officers said that state spending rose 16% to $2.65T in fiscal 2021. The rise in spending is the highest in almost 35 yrs. States have spent $428B in federal C19 over the past two yrs.

The Markets:

The U.S. equity markets (SP500, Dow and Russell 2000) followed a strong October with a thud and ended the month in negative territory. The bright spot was tech as the NASDAQ ended the month firmly in positive territory. The broader markets have taken on two elements of uncertainty; stagflation and the uncertainties of Omicron. It is still early days for the Omicron variant. All we know with certainty is that it is highly transmissible and hosts a remarkable number of mutations from previous variants. There is not yet any indication that it produces more morbidity or mortality than previous variants, though evidence that this virus is evolving extremely rapidly is concerning and as I always say, "markets dislike uncertainty".

Technology, materials and utilities were bright spots in the market last month while energy, financials and industrials were big disappointments.

U.S. Index	Last Month (% return)	YTD (%)
S&P500	-1.0	21.6
Dow	-4.0	12.7
NASDAQ Comp	1.4	25.2
Russell 2000	-6.4	11.8

On the international front, the markets were generally weak across the board with the exception of the U.K. and China. Step-ups in lockdowns, supply chain and production imbalances were the culprits. Crude oil retreated quite a bit this month as travel and production outlooks weakened.

International Index	Last Month (% return)	YTD (%)
Euro Stoxx 50	-4.9	14.6
Hang Seng	-6.7	-13.9
Germany	-4.4	10.2
Nikkei	-6.2	1.4
FTSE-U.K.	3.0	9.4
China Shanghai Comp.	0.6	2.6
Crude oil	-19.6	36.6

The year 2021 began with the 10-year Treasury Note yield at 0.90%. The 10-year closed November at 1.44%, 12bps lower than the October 2021 close. The 2-year Treasury closed November yielding .53%, 4 bps higher than October's close. The 10/2 spread compressed a bit to 91bps or 16bps tighter than last month. The compression helps explain weakness in financials.

News You Can Use:

Omicron has sparked concern from the international community about the seriousness of the new COVID variant which emerged from South Africa. The variant has a significant number of mutations – 30 on its spike protein (more than double the number carried by Delta) which is the key used by the virus to unlock our body's cells. This leads experts to believe it could be more transmissible and resistant to current vaccines. The US will know in two weeks if existing vaccines are effective and to what degree. The CDC is urging all adults to get a booster shot.

https://www.theguardian.com/world/2021/nov/26/vaccine-resistant-what-scientists-know-new-covid-variant

Last year Amazon reported having 1.3 M people working for the company worldwide, with roughly 950K workers in the US alone. According to recent employment reports, there are

145.8M nonfarm payroll workers out of a total population of 332M. That means that Amazon employs 1 out of 350 Americans, or 1 out of every 153 employed workers. During the holiday period that number goes up even more. Amazon announced it would take on 150K seasonal employees to fulfill the demand for the next few months.

https://www.businessinsider.com/amazon-employees-number-1-of-153-us-workers-head-count-2021-7

#5 ranked Michigan Wolverines beat #2 ranked Ohio State 42-27 on Saturday the 27th, which was the first win since 2011 against the Buckeyes. All eyes were on the Wolverines coach Jim Harbaugh as he had yet to steal a victory from Ohio State in his six years as coach. Harbaugh's pay was slashed last winter because of his lack of success in the rivalry. The college football world was elated for Harbaugh and to see the losing streak end.

https://www.cbssports.com/college-football/gametracker/recap/NCAAF_20211127_OHIOST@MICH/

As always, if I can be of additional guidance, please feel free to call me at 312.485.6847.

Best regards,

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