Nationwide Economics

Weekly Economic Review & Outlook

April 11, 2022

Quantitative tightening to ramp up quickly

The minutes from the most recent (March) Federal Open Market Committee (FOMC) meeting were released last week. The details indicated that policymakers are keen to lower inflation by reversing expansionary policy at a rapid pace by both increasing policy interest rates (perhaps at a faster pace than financial markets expect) and starting to reduce the size of the Fed's balance sheet. In addition to the minutes, the ISM services index showed continued solid expansion while echoing the ISM manufacturing survey with prices remaining elevated. But the Manheim used vehicle value index fell sharply for a second consecutive month.

Balance sheet reduction to start soon

In the press conference following the March FOMC meeting, Fed Chair Jerome Powell mentioned that the group was close to finalizing what the reduction of the Fed's balance sheet will look like. Last week we received more details about what exactly the committee thinks is an appropriate pace to paring it back. Following the framework that was established back in 2017, the FOMC discussed allowing the balance sheet to run off by as much as $60 billion per month for Treasury securities and $35 billion per month for agency mortgage-backed securities (MBS).

While the minutes didn't state when the runoff would begin, it is likely to be fully up to speed within two to three months. The actual announcement is likely to come at the next FOMC meeting in early May. Early estimates following the minutes release last week showed that there may be trouble hitting the cap for MBS securities. One of the main drivers of this is that mortgage rates have been jumping, reducing the flow of refinancing activity which would typically cause more redemptions inside the MBS pools. So, if the Fed intends to hit these caps on a regular basis, this could mean that asset sales would be required to hit the target — perhaps adding to volatility in the mortgage market.

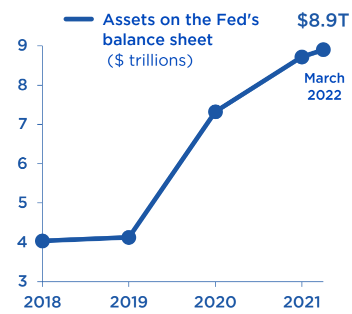
In addition, the FOMC minutes indicated that 'many' participants would have favored a 50-basis point rate increase in March had it not been for the uncertainty generated by the Russian invasion of Ukraine. While there is still plenty of uncertainty around that war, the odds of a 50-basis point rate hike at the May (and perhaps June) meeting have increased sharply.

The ISM services index was solid

The ISM services index moved higher for March as new orders and production bounced back. The employment component moved back above 50, the expansion/contraction level. But the prices paid index moved back to a very high level, suggesting that there are still supply chain issues that are impacting input costs. In addition to supply chain concerns, industry commentary suggested that while demand remains high, there is still trouble with hiring enough workers to meet those orders.

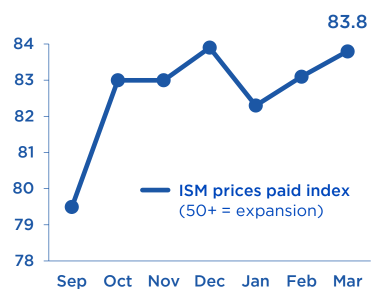
But there was also some good news on inflation last week. The Manheim used vehicle value index — which has a high correlation with used car prices in the CPI — fell sharply for a second consecutive month for March. While previous gains mean that prices over the past year are still up by 25 percent, they were up by nearly 50 percent just a few months ago. With used cars having a relative importance of 4.2 percent in the CPI, this may be the start of a slowing in inflation.

The Fed's balance sheet runoff should start soon



The Fed's balance sheet has expanded to record levels but it should start to be reduced soon.

The ISM services prices paid index rose again



The rise of Covid cases in China and the Russian invasion of Ukraine are helping to keep prices elevated.

Source: Haver Analytics

Contributors: Dan Hadden, Financial Markets Economist | Daniel Vielhaber, Economist

The Week Ahead

Here's what we are watching this week:

Consumer price index — Apr 12

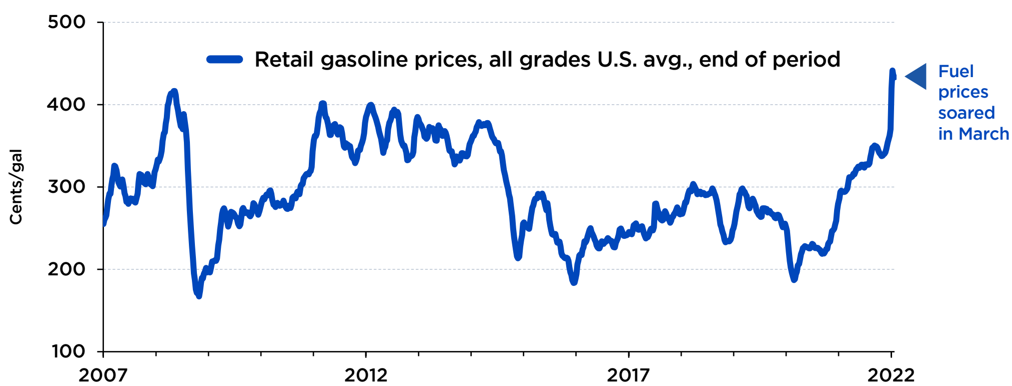
Consumer prices likely surged for March, led by food and energy

A combination of strong consumer demand, pandemic-related supply chain issues, and soaring food/energy prices have lifted trend growth in the consumer price index (CPI) to its highest level since early 1982. While supply chain issues were still present, the big story for March's CPI release should be yet another spike in energy prices, this time due mostly to Russia's invasion of Ukraine. Also, the invasion has driven up food prices due to Russia and Ukraine's roles in global grain and/or seed oil trade. All told, we project growth in the CPI of 1.1 percent for March, and growth in the core rate (the overall index less food and energy) of 0.5 percent. This would raise the 12-month trend rates to 8.4 percent and 6.7 percent, respectively.

Retail sales — Apr 14

...and rising prices probably boosted retail sales

Growth in retail sales was likely solid for March in part due to rising prices. Travelers paid far more at the pump with the monthly average price of retail gasoline up by over 70 cents per gallon, while spending at both grocery stores and restaurants was probably up due to rising food prices (and much lower Covid infections in the case of restaurants). Additionally, while vehicle unit sales were down a little in March, it's likely that rising prices resulted in growth in retail sales for vehicles. We project growth in overall retail sales of 0.6 percent for March, and of 0.4 percent when excluding autos.



Sources: Energy Information Administration/Haver Analytics

Industrial production — Apr 15

Growth expected for industrial production (IP)

Industrial production continues to face the headwind of limited semiconductor availability, which is preventing increased production of automobiles (and other manufactured goods). But the Markit manufacturing PMI, which has a high correlation with manufacturing IP, climbed to the highest level in six months for March, suggesting growth in manufacturing activity. Utilities output, which declined for February after a colder-than-normal January, was likely more neutral for March. Mining output probably rose modestly in response to higher crude oil prices. In total, we project growth in IP of 0.4 percent for March.

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Weekly Market Snapshot

Provided by IMG Business and Product Development – Data Analytics Team

Equity	Last	Returns 1 Week	YTD*	1 Year *
S&P 500 (Large)	4,488	-1.24%	-5.46%	11.08%
S&P 400 (Mid)	2,617	-3.41%	-7.56%	-0.23%
S&P 600 (Small)	1,273	-4.37%	-8.87%	-3.20%
S&P 500 (High Quality)	50	-0.88%	-6.61%	10.26%
Russell 1000	4,752	-1.53%	-6.21%	8.50%
Russell 2000	4,957	-4.60%	-10.88%	-10.11%
Dow Jones	34,721	-0.23%	-3.94%	5.58%
NASDAQ	13,711	-3.85%	-12.19%	-0.20%
MSCI EAFE	2,140	-1.36%	-7.51%	-2.67%
MSCI EM	1,128	-1.52%	-8.02%	-13.91%

* represents total return

S&P Metrics	LTN P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	20.62	19.17	37.42	9.74
Prior Month	20.52	18.14	40.39	8.70
Prior Year	26.07	22.37	-1.05	23.24

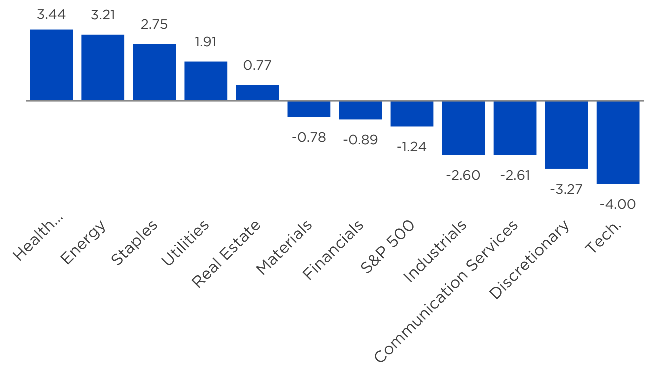
Fixed Income	Last	Returns 1 Week	YTD	1 Year
U.S. Aggregate	3.23%	-1.82%	-7.89%	-6.69%
U.S. Inv Grade	3.92%	-2.36%	-9.96%	-7.55%
U.S. High Yield	6.53%	-1.34%	-6.25%	-2.85%
TIPS	2.88%	-1.26%	-4.69%	2.17%

Rates	Last	Returns 1 Week	YTD	1 Year
6M T-Bill	1.19%	0.10	1	1.15
2 Yr Treasury	2.53%	0.09	1.80	2.39
5 Yr Treasury	2.76%	0.21	1.50	1.91
10 Yr Treasury	2.72%	0.33	1.2	1.08
30 Yr Treasury	2.76%	0.32	0.86	0.44

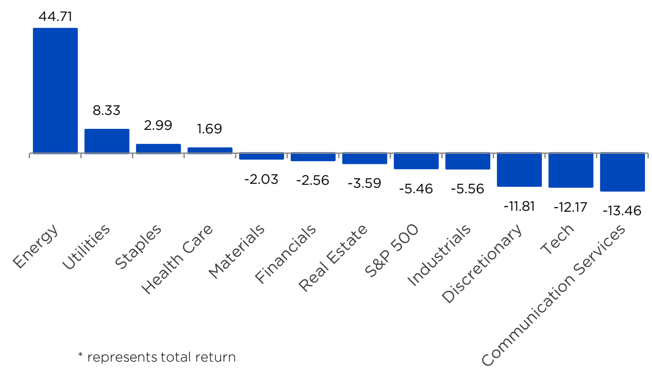
Spreads	Last	Change (Abs %) 1 Week	YTD	1 Year
AAA Rated	0.57	-0.01	0.06	0.11
BBB Rated	1.47	0.00	0.24	0.28
High Yield	3.57	0.17	0.47	0.36
10 to 2 yr Treasury	0.19	0.00	-0.6	-1.31

Commodities/FX	Last	Returns (Currencies in $ strength) 1 Week	YTD	1 Year
Gold	1941.60	1.17%	6.24%	10.52%
Bitcoin	42257.02	-8.72%	-8.91%	-27.13%
WTI Oil	98.26	-1.07%	30.44%	64.84%
EUR/USD	1.08735	1.48%	4.38%	8.61%
USD/JPY	124.41	1.26%	8.03%	13.85%

S&P Sector Returns — Week (%)

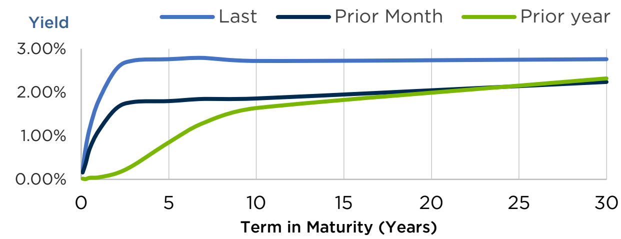


S&P Sector Returns — YTD (%)*



* represents total return

U.S. Yield Curve



Russell Style Returns - Week

	Value	Core	Growth
Large	0.1	-1.5	-3.1
Mid	-1.0	-1.8	-3.3
Small	-4.1	-4.6	-5.1

Russell Style Returns - YTD

	Value	Core	Growth
Large	-0.1	-6.2	-11.6
Mid	-2.3	-6.9	-15.0
Small	-5.6	-10.9	-16.1

Source: FactSet

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Additional Economic Indicators

Previous Week's Indicators

	Period	Actual	Previous
Factory orders	Feb.	-0.5%	1.5%
U.S. trade balance	Feb.	-$89.2 B	-$89.2 B
Markit services PMI	Mar.	58.0	56.5
ISM services PMI	Mar.	58.3	56.5
Initial jobless claims	Week ending Apr. 2	166,000	171,000
Consumer credit	Feb.	$42 B	$8 B

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Small business optimism index	Tues.	Mar.	95.5	95.7
Consumer price index (m/m)	Tues.	Mar.	1.1%	0.8%
CPI (y/y)	Tues.	Mar.	8.4%	7.9%
Core CPI (m/m)	Tues.	Mar.	0.5%	0.5%
Core CPI (y/y)	Tues.	Mar.	6.7%	6.4%
Producer price index	Wed.	Mar.	1.3%	0.8%
Core PPI	Wed.	Mar.	0.3%	0.2%
Initial jobless claims	Thurs.	Week ending Apr. 9	161,000	166,000
Retail sales	Thurs.	Mar.	0.6%	0.3%
Retail sales ex autos	Thurs.	Mar.	0.4%	0.2%
Import prices	Thurs.	Mar.	2.5%	1.4%
Consumer sentiment (preliminary)	Fri.	Apr.	57.2	59.4
Empire St New York Fed manufacturing survey	Fri.	Apr.	-2.5	-11.8
Industrial production	Fri.	Mar.	0.4%	0.5%
Capacity utilization	Fri.	Mar.	77.8%	77.6%

*** Nationwide Economics Forecast**

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