Nationwide Economics
Weekly Economic Review & Outlook
June 21, 2021

Supply-side constraints are having an impact

Retail sales declined by 1.3 percent for May as topline spending was again weaker than expected. But there were significant upward revisions to March and April that point to a stronger trend pace of expenditures – and perhaps to upward revisions for the May data, as well. A pickup in spending at restaurants and clothing stores was likely influenced by the fuller reopening of in-person activities across the country. Despite May's decease, retail sales were still up by more than 28 percent over the past year and have far surpassed pre-COVID levels on the back of the successive stimulus payments this year.

There are signs, however, that rising prices and supply shortages are leading to reduced sales in some sectors. The previously reported drop in unit auto sales weighed heavily on total sales — sales ex-autos showed a smaller 0.7 percent decline. Rising prices and lack of availability likely played a role in sharp sales drops for furniture, appliances, and building materials during May. But as supply chains heal over the course of the year, these supply side impacts should wane – although the downside impacts are likely to linger for the next few months.

New home construction is being hit by the supply crunch as housing starts for May were little changed from the originally reported April figure (although up by 3.6 percent due to downward revisions for April). A lack of buildable lots, labor shortages, and rising costs (especially for lumber) have squeezed many builders this year. The NAHB Housing Market Index, while still elevated, fell to its lowest level since last August as builders noted waning homebuyer traffic and were less confident about single-family sales over the next six months.

The outlook for home construction over the remainder of the year depends upon both demand and supply factors. On the demand side, if job gains continue to be strong and mortgage rates remain low (even if rising some), then new home sales should move higher — incenting builders to increase construction. On the supply side, if the number of buildable lots increases and construction cost gains moderate, then builders will be able to start more units. Lumber prices, while still high, have already dropped considerably from their all-time peaks of about a month ago. In the aggregate, we still expect starts and new sales to move higher as the strong demand metrics should win out.

The Fed pushes forward its tightening timeline

While there was no change in monetary policy at the June FOMC meeting, the median projection of FOMC participants for the federal funds rate now shows two rate hikes for 2023 (up from none in March's projections). There remains a wide dispersion within the 2023 federal funds rate forecasts with five of the 18 participants still not expecting a rate move until 2024. Still, the rapid acceleration in growth and inflation so far in 2021 may have shifted the thinking on how long near zero rates will be needed to boost to recovery.

In the near term, there was no intention made to reduce the amount of monthly asset purchases made by the Fed. Chair Powell noted during his press conference that any move to taper these purchases would be announced well in advance, suggesting that this policy move remains at least a few meetings away. We expect that the current pace of purchases could be maintained into 2022, but a tapering of MBS purchases may occur sooner, given the hot housing market.

You Need to Know

Week in Review

Retail spending weaker for May

Total sales fell modestly for May, helped by supply constraints that have limited new light vehicle production. But upward revisions to prior months suggest that the trend in spending remains solid.

No policy move in June, but the Fed shifts forward its tightening timeline

The median federal funds rate forecast from FOMC participants sees two rate hikes in 2023 for the first time as the Fed projects a stronger recovery. And it is finally talking about talking about tapering.

Week Ahead (Forecasts)

Weaker new and existing home sales expected for May

Reflecting continued supply limitations and rising prices, both new and existing sales are projected to decline modestly for May – although still at elevated levels.

Another rise in core inflation projected

The year-over-year change in the core PCE price index should increase to 3.4 percent for May, but this is likely the near-term peak for inflation readings.

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The Week Ahead

This week's economic news focuses on housing market data from May as well as the latest on income/spending and the Fed's preferred inflation measure, the core PCE price index.

Existing home sales expected to drop

While strong compared with most of the past fifteen years, existing home sales for April were weaker than recent months. Housing demand remains strong as mortgage rates continue to be historically low and workers adjust their locations to reflect increased work-from-home options. On the other hand, the market has not seen the rise in homes for sale expected as the pandemic winds down; the supply of existing homes for sale is hovering around its all-time low and continues to limit potential sales. Taken together – and given the already announced drop in pending home sales – we project a modest drop for May existing home sales to an annualized pace of 5.72 million units. As in April, this is strong from a historical perspective, but continues to be held back by a severe lack of supply.

New home sales also likely down for May

As with existing homes, new home sales for April were strong in absolute terms, but weaker than they could have been if they weren't limited by the supply side of the market. Housing demand remains strong and interest in new homes continues to benefit from the lack of existing homes for sale, pushing potential homebuyers into the market for new homes. Given supply constraints, home builders can't provide all the new homes that buyers want – leading to many builders not accepting home sale contracts in the near term. Sales likely dropped for May to an annualized pace of 841,000 units, with median prices of homes sold up strongly again.

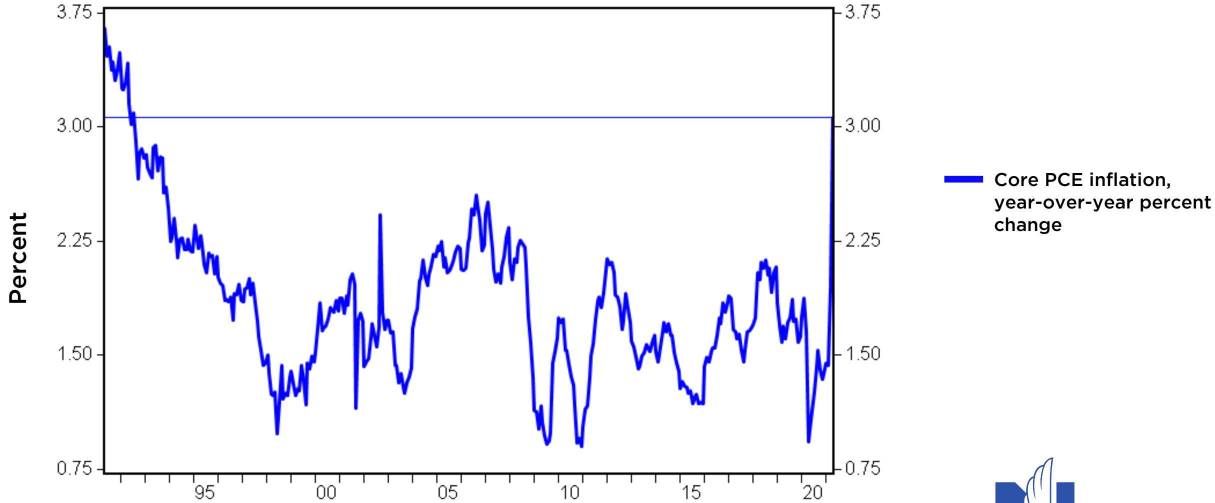
Income and inflation gains expected for May

Despite the drop in retail sales (mainly goods) for May, overall personal consumption expenditures (PCE) were likely boosted by the surge in services as restrictions on in-person activities have been mostly lifted. We project an increase of 0.8 percent for the month. Personal income is also projected to rise by 0.8 percent as wage gains have accelerated while job growth was strong over the month.

Core consumer inflation continued to climb sharply for May according to the consumer price index (CPI), and we expect that the core PCE price index saw a jump, as well. We project a strong 0.5 percent gain in core PCE inflation for May. This would bring the 12-month trend rate to 3.4 percent, which would be the fastest pace in nearly 30 years – although this could be the peak for year/year inflation readings.

Worth Watching

Core PCE inflation surpassed three percent for the first time since 1992 for April.



Sources: Bureau of Economic Analysis/Haver Analytics

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Weekly Market Snapshot

Equity	Last	Returns 1 Week	YTD*	1 Year*
S&P 500 (Large)	4,166	-1.87%	11.71%	35.87%
S&P 400 (Mid)	2,612	-5.06%	13.87%	47.68%
S&P 600 (Small)	1,331	-4.67%	19.51%	62.54%
S&P 500 (High Quality)	47	-1.26%	11.81%	33.83%
Russell 1000	4,513	-1.82%	11.43%	38.09%
Russell 2000	5,561	-4.17%	13.78%	58.51%
Dow Jones	33,290	-3.40%	9.79%	30.25%
NASDAQ	14,030	-0.26%	9.21%	42.14%
MSCI EAFE	2,309	-2.40%	9.24%	31.65%
MSCI EM	1,361	-1.44%	6.36%	40.01%

*represents total return

S&P Metrics	LTM P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	24.47	20.40	11.68	25.65
Prior Month	25.15	21.05	5.88	25.43
Prior Year	21.02	21.87	-9.33	2.11

Fixed Income	Last	Returns 1 Week	YTD	1 Year
U.S. Aggregate	1.52%	0.11%	-1.60%	-0.11%
U.S. Inv Grade	2.09%	0.58%	-1.22%	3.59%
U.S. High Yield	4.71%	-0.07%	2.96%	12.80%
TIPS	1.09%	-0.36%	1.00%	6.27%

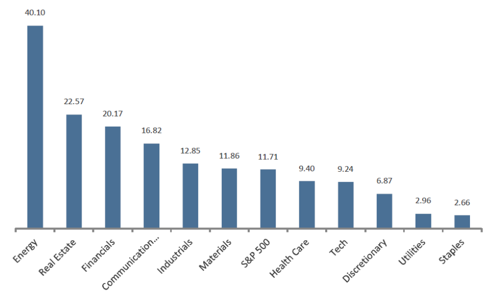
Rates	Last	Change 1 Week	YTD	1 Year
6M T-Bill	0.06%	0.02	-0.03	-0.11
2 Yr Treasury	0.26%	0.10	0.13	0.07
5 Yr Treasury	0.89%	0.13	0.53	0.55
10 Yr Treasury	1.45%	-0.02	0.52	0.74
30 Yr Treasury	2.01%	-0.14	0.36	0.54

Spreads	Last	Change (Abs %) 1 Week	YTD	1 Year
AAA Rated	0.45	-0.02	-0.10	-0.30
BBB Rated	1.1	-0.03	-0.22	-0.96
High Yield	3.18	-0.03	-0.68	-2.83
10 to 2 yr Treasury	1.19	0.00	0.39	0.67

Commodities/FX	Last	Returns (Currencies in $ strength) 1 Week	YTD	1 Year
Gold	1767.90	-5.83%	-6.61%	2.50%
Bitcoin	35785.22	-4.12%	23.30%	280.61%
WTI Oil	71.64	0.90%	48.17%	84.69%
EUR/USD	1.1856	2.10%	3.10%	-5.67%
USD/JPY	110.24	0.43%	6.78%	3.25%

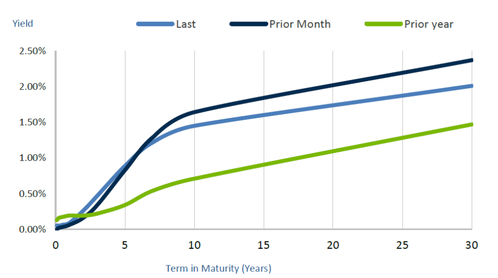
S&P Sector Returns — Week (%)

S&P Sector Returns — YTD (%)*



*represents total return

U.S. Yield Curve



Russell Style Returns — Week

	Value	Core	Growth
Large	-4.1	-1.8	0.5
Mid	-4.7	-3.0	0.3
Small	-5.5	-4.2	-2.7

Russell Style Returns — YTD

	Value	Core	Growth
Large	13.9	11.4	9.2
Mid	16.0	12.5	6.4
Small	23.8	13.8	4.5

Sources: IMG Business and Product Development -Data Analytics Team; FactSet

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Previous Week's Indicators

	Period	Actual	Previous
Retail sales	May	-1.3%	0.9%
Retail sales ex autos	May	-0.7%	0.0%
Producer price index	May	0.8%	0.6%
NY Fed Empire State manufacturing index	June	17.4	24.3
Industrial production	May	0.8%	0.1%
Capacity utilization	May	75.2	74.6%
NAHB Housing Market Index	June	81	83
Housing starts	May	1.57 M	1.52 M
Building permits	May	1.68 M	1.73 M
Initial jobless claims	Week ending June 12	412,000	375,000
Philadelphia Fed manufacturing index	June	30.7	31.5
Index of leading economic indicators	May	1.3%	1.3%

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Existing home sales	Tues.	May	5.72 M	5.85 M
New home sales	Wed.	May	841,000	863,000
Initial jobless claims	Thurs.	Week ending June 19	370,000	412,000
Durable goods orders	Thurs.	May	1.5%	-1.3%
Real GDP (revision)	Thurs.	Q1 2021	6.3%	6.4%
Kansas City manufacturing survey	Thurs.	May	24	26
Personal income	Fri.	May	0.8%	-13.1%
Consumer spending	Fri.	May	0.8%	0.5%
Core PCE price index	Fri.	May	0.5%	0.7%

* *Nationwide Economics Forecast*

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