Nationwide Economics
Weekly Economic Review & Outlook
July 19, 2021

Inflation surges again but softer gains likely ahead

The consumer price index (CPI) jumped again for June, rising by 0.9 percent for the fastest monthly gain in 13 years. Consumer inflation has now spiked by 5.4 percent over the past year — the second fastest rate in the past 30 years. The CPI rose by more than 2.3 percent during the second quarter, the second hottest three-month period for price gains since 1982. Core prices also climbed by a sharp 0.9 percent for June — pushing up the 12-month change in that key metric to the fastest pace in nearly 30 years at 4.5 percent.

Higher food and energy costs added to inflationary pressures for the month, but much of the increase was again caused by lingering COVID impacts. Several categories (including apparel, airline fares, and hotel costs) are still below their pre-pandemic levels and continue to see outsized gains as prices reset in response to the surge in consumer demand. The shortage of microchips has caused production cutbacks and driven up costs for new cars and appliances, as well as an unprecedented 45 percent annual spike in used car and truck prices. After excluding outliers, the Cleveland Fed's trimmed-mean CPI showed a 0.5 percent increase for June and a more modest 2.9 percent change over the past year (although trending upward).

The price spikes from the transition out of the pandemic likely played out during the second quarter and should fade soon. We expect monthly CPI readings to be slower over the rest of 2021, although annual comparisons will remain elevated until a year from now when the recent monthly increases roll off the calculations. But not all the higher costs will be transitory, keeping annual inflation near 2.5 percent in coming years compared with the sub-2.0 percent pre-COVID trend. Moreover, elevated retail prices for consumers could extend for some time within some areas that have jumped this year.

Solid retail spending in June

Retail sales climbed by 0.6 percent for June, a solid increase given the drag from a sharp drop in unit auto sales. Core retail sales (excluding auto, building supply, and gasoline sales) showed a stronger 1.1 percent gain — the fastest increase for this measure in a non-stimulus month since last September. Lifted by the government payment surges from January and March, the year-over-year gain in retail sales remained very strong at 17.6 percent.

Service sector sales continued to get a boost from increased traffic after a fuller reopening of the economy. Spending was up sharply at restaurants, clothing stores, and general merchandise retailers as consumers have flocked back to in-person shopping. Rising inflation also likely contributed as higher prices increased the dollar value of sales. Online expenditures have slowed as the pandemic has ebbed but remain a source of growth for many retailers.

Growth in retail sales decelerated in the second quarter, largely the expected after effects of the first quarter's stimulus-induced surge. Still, we expect that the economy expanded strongly over the period, likely near an 8.0 percent annualized pace. Given the strong growth in the first half of 2021, the level of real GDP likely surpassed its pre-COVID peak during the second quarter — signaling an end of the recovery and the start of the next expansion.

You Need to Know

Week in Review

▲ **Consumer inflation still hot for June**

The CPI jumped again for June to complete the fastest quarter for price gains in 40 years. COVID impacts continue to drive outsized increases in a few areas and are masking a more modest underlying trend for inflation.

▲ **Service sector retailers see further recovery for June**

Retail sales rose by 0.6 percent for June as strong sales on in-person activities offset a sharp decline in unit auto sales.

Week Ahead (Forecasts)

▼ **A small decline expected for June housing starts**

While the overall pace of housing starts should be strong, they were likely still held back by high input costs, lack of workers, and a low supply of available lots.

▲ **Existing home sales should see a small increase**

Strong demand factors likely supported a faster pace of existing home sales for June, despite a very low supply of homes for sale.

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The Week Ahead

This week's economic data are heavy on housing and include updates on the NAHB housing market index, housing starts and permits, existing home sales, and the Conference Board's index of leading economic indicators.

Little change expected for housing starts

Housing starts rose a touch for May but remained below the 14-year high seen in March and are currently being held back by several factors. While housing demand remains high, builders are dealing with high input costs and a low supply of available lots on which to build. Additionally, as with much of the economy, construction is experiencing a labor shortage, likely causing builders to limit the contracts they accept in order to prevent overpromising the number of houses they can build. We project a small decline in starts to an annualized pace of 1.51 million units. While lower than in six of the past seven months, this pace would still be stronger than in most of the last 15 years.

Existing home sales should climb, but will still be held back by low supply

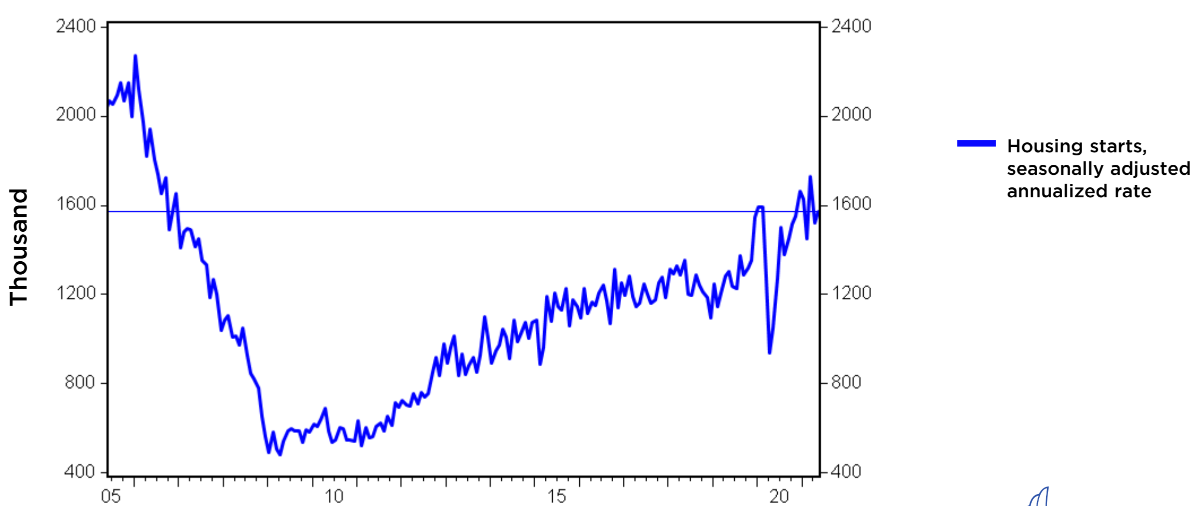
Existing home sales fell slightly for May but remained strong, and based on a rebound in the NAR's pending home sales index we believe that sales climbed for June. Demand factors for housing are healthy, with mortgage rates remaining very low and job gains picking up speed. Demand also likely continues to benefit from the ability of many workers to permanently work from home. Broad-based labor shortages are also pushing wages higher, providing higher income and making it easier to qualify for mortgage loans. Continuing to hold sales back, however, is the still historically low supply of homes for sale and rapidly rising house prices. We project a small climb in sales to an annualized pace of 6.1 million units.

More strong growth likely for the index of leading economic indicators (LEI)

Despite slowing a bit for May, the year-over-year percent growth rate for the LEI was still at its second highest level ever. The annual growth rate almost certainly fell again for June due to base effects, as economic conditions were rapidly improving last June in the early stages of the economic re-opening from COVID restrictions. Still, the monthly gain is expected to be strong for a fourth straight month because of solid growth in manufacturers' new orders, a continued decline in initial jobless claims, and yet more record highs for the S&P 500 index. We project growth in the LEI of 0.9 percent, which would bring the 12-month percent change down to 12.4 percent.

Worth Watching

Despite a need for more homes, housing starts have come down from the recent high.



Sources: Census Bureau/Haver Analytics

Weekly Market Snapshot

Equity	Last	Returns 1 Week	YTD*	1 Year*
S&P 500 (Large)	4,327	-0.96%	16.12%	36.66%
S&P 400 (Mid)	2,617	-3.29%	14.19%	45.03%
S&P 600 (Small)	1,298	-4.55%	16.66%	55.08%
S&P 500 (High Quality)	49	-0.39%	17.35%	35.74%
Russell 1000	4,664	-1.26%	15.27%	38.10%
Russell 2000	5,376	-5.11%	10.07%	48.97%
Dow Jones	34,688	-0.52%	14.45%	32.33%
NASDAQ	14,427	-1.87%	12.34%	38.74%
MSCI EAFE	2,303	-0.46%	9.11%	27.55%
MSCI EM	1,340	1.72%	5.15%	30.85%

**represents total return*

S&P Metrics	LTM P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	24.57	21.23	14.89	22.78
Prior Month	24.88	21.16	9.92	24.13
Prior Year	21.97	22.24	-10.92	5.85

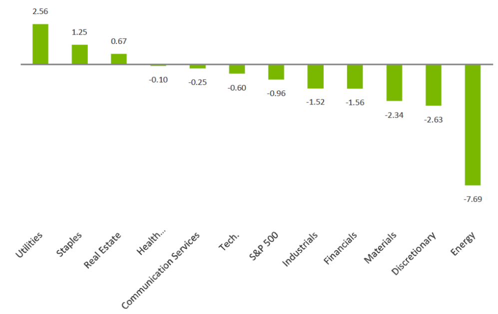
Fixed Income	Last	Returns 1 Week	YTD	1 Year
U.S. Aggregate	1.44%	0.24%	-0.94%	-0.48%
U.S. Inv Grade	2.04%	0.31%	-0.51%	2.33%
U.S. High Yield	4.62%	-0.15%	3.88%	13.26%
TIPS	1.00%	0.85%	3.10%	6.89%

Rates	Last	Change 1 Week	YTD	1 Year
6M T-Bill	0.05%	0.00	-0.04	-0.08
2 Yr Treasury	0.25%	0.02	0.12	0.09
5 Yr Treasury	0.79%	0.00	0.43	0.51
10 Yr Treasury	1.31%	-0.06	0.38	0.69
30 Yr Treasury	1.93%	-0.06	0.28	0.62

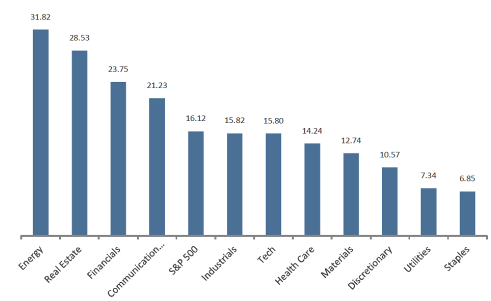
Spreads	Last	Change (Abs %) 1 Week	YTD	1 Year
AAA Rated	0.48	0.00	-0.07	-0.23
BBB Rated	1.14	0.00	-0.18	-0.80
High Yield	3.18	0.11	-0.68	-2.58
10 to 2 yr Treasury	1.06	0.00	0.26	0.6

Commodities/FX	Last	Returns (Currencies in $ strength) 1 Week	YTD	1 Year
Gold	1814.50	0.25%	-4.15%	0.88%
Bitcoin	31389.67	-7.35%	8.15%	243.62%
WTI Oil	71.45	-4.17%	47.78%	75.38%
EUR/USD	1.1809	0.47%	3.49%	-3.30%
USD/JPY	110.11	-0.03%	6.64%	2.79%

S&P Sector Returns — Week (%)

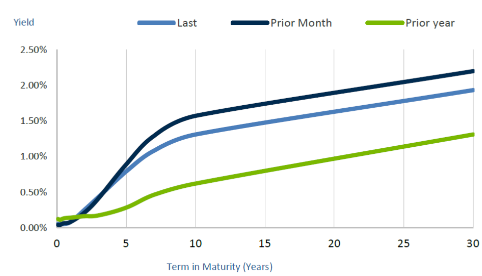


S&P Sector Returns — YTD (%)*



**represents total return*

U.S. Yield Curve



Russell Style Returns — Week

	Value	Core	Growth
Large	-1.4	-1.3	-1.1
Mid	-2.5	-2.8	-3.4
Small	-4.3	-5.1	-5.9

Russell Style Returns — YTD

	Value	Core	Growth
Large	16.2	15.3	14.4
Mid	17.4	13.8	7.4
Small	19.4	10.1	1.4

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

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Previous Week's Indicators

	Period	Actual	Previous
Consumer price index (CPI)	June	102.5	99.6
Core CPI	June	0.9%	0.7%
Producer price index	June	1.0%	0.8%
Initial jobless claims	Week ending July 10	360,000	386,000
Import price index	June	1.0%	1.4%
Empire state index (FRB NY)	July	43.0	17.4
Philadelphia Fed index	July	21.9	30.7
Industrial production	June	0.4%	0.7%
Capacity utilization	June	75.4%	75.1
Retail sales	June	0.6%	-1.7%
Retail sales ex-autos	June	1.3%	-0.9%

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Housing market index	Mon.	July	80	81
Housing starts	Tues.	June	1.51 M	1.57 M
Building permits	Tues.	June	1.63 M	1.68 M
Initial jobless claims	Thurs.	Week ending July 17	345,000	360,000
Existing home sales	Thurs	June	6.10 M	5.80 M
Index of leading economic indicators	Thurs.	June	0.9%	1.3%
Kansas City Fed manufacturing survey index	Thurs.	July	22	27
Markit flash manufacturing index	Fri.	July	61.6	62.1
Markit flash services index	Fri.	July	65.3	64.6

* *Nationwide Economics Forecast*

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