

October 18, 2021

Inflation remains high, but it may be stabilizing

Inflation appears to be the topic *du jour* for nearly everyone today, as price gains continue to be surprisingly strong. This is unlikely to subside in the near term given the continued pressures from supply chain disruptions and labor market dynamics (although we still expect inflation to partially subside next year). The impact from rising prices can be seen in other economic data, with small business optimism and consumer sentiment edging lower and consumers being forced to spend more with higher food and energy costs (among other things), boosting retail sales.

Inflation is hot, but much is owed to Covid-related interruptions

The consumer price index (CPI) rose by 0.4 percent for September, bringing the year-over-year measure up to 5.4 percent. The core reading (which removes the volatile food and energy components) rose by a more modest 0.2 percent and kept the year-over-year metric at 4.0 percent. The details did little to settle the debate between the transitory and persistent camps. The shelter category, which accounts for over 30 percent of the headline CPI and about 40 percent of the core reading, rose by 0.5 percent. This category has been increasing steadily on the back of sharply rising home price gains (while this is not a 1:1 translation, rising home prices should eventually filter into the CPI components that reflect housing costs). Shelter tends to be one of the more persistent categories, which suggests that some inflation pressures may be present for a while.

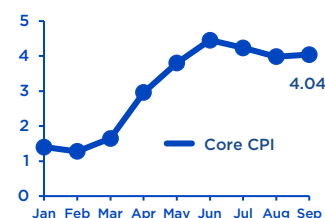
On the other hand, categories such as used car prices, airfares, and lodging away from home all declined. These groups were some of the driving forces for higher inflation earlier this year and are expected to continue to provide some downside pressure in the months ahead. Ultimately, it will take time to resolve the supply chain issues which will give us greater insight as to the level of long-term price pressures. This is likely to be an important determinant when the Federal Open Market Committee (FOMC) decides that raising short-term interest rates will be appropriate. The more persistent these price gains are, the sooner a change in rates will come. We still expect the initial rate hike to come sometime in 2023, but the risk is that a hike will come sooner rather than later, at least for now.

Retail sales jump despite consumer sentiment concerns

Small business optimism edged lower to 99.1 for September on the back of declines in plans to hire and those who expect a better economy. Labor market constraints are weighing on the outlook. Consumers continued to be worried in the early part of October with the University of Michigan consumer sentiment survey declining further. Near-term inflation fears are prevalent, but this hasn't been enough to hold back actual spending, at least for now. Retail sales grew by a solid 0.7 percent for September with the control group up by 0.8 percent. The report showed broad spending gains across most categories, but the largest came from spending on goods. Some of the money spent by consumers can be tied back to higher inflation, particularly in the cost of food and gasoline.

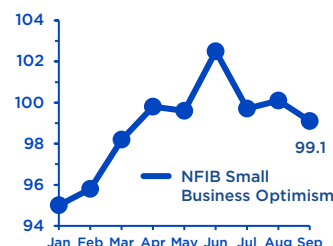
While sentiment shows a concern by consumers about the outlook, it has yet to put a dent in their willingness to spend. Some price increases and supply shortages (such as computer chips which are crimping auto sales) are causing buyers to shift where they spend, but they haven't led to the drop that analysts would expect if darker times were ahead for the economy. This positive retail sales report comes as Covid cases are decelerating in the U.S., which should also be a positive moving forward.

The core CPI held steady, but the risks aren't over



Consumer price increases continue to be strong and there are growing concerns that above-trend price gains may linger longer than expected previously.

Small business optimism edged lower



Inflation and hiring continue to weigh heavily on small businesses owners and their outlook for the economy. But business activity remains solid.

Source: Haver Analytics

The Week Ahead

Here's what we are watching this week

Industrial production



Industrial production should rise further

After strong growth for much of the year, the industrial production (IP) index grew by six percent in August from a year earlier. While the ISM manufacturing index still showed solid growth in production for September, it was somewhat weaker than in the prior month, likely due to supply chain problems and a lack of workers. But a relatively warm month could mean more growth in utility output. Additionally, higher energy prices should mean that production increased here, too. In total, we project growth of 0.3 percent for IP in September, a solid gain but slower than in the past four months.

Housing starts



Modest decline expected for housing starts

Housing starts were solid for August but still held back by significant supply constraints and high construction costs, as well as a labor shortages. It's likely that homebuilders would like to build more houses to capitalize on strong housing demand and low supply but are simply close to capacity at the current pace. Multifamily starts could drop a bit after reaching their fastest pace since before the pandemic and second fastest since 1987, but we believe total starts in September reflected an effort to continue to push capacity. We project a slight step down to an annualized pace of 1.61 million units for September housing starts.

Existing home sales



Existing home sales expected to rise

As with housing starts, existing home sales have been solid but could be stronger if not for limitations on the supply side. The inventory of existing homes for sale continues to hover marginally above the all-time low recorded in March which has held sales to a lower level than strong housing demand would suggest. Pending home sales jumped for August, however, which likely led to a rise in existing home sales for September — when many of those sales would have been finalized. We project a rise in the annualized pace of existing home sales for September to 6.15 million units.



Source: National Association of Realtors/Haver Analytics

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)	4,471	1.84%	20.40%	30.27%
S&P 400 (Mid)	2,748	2.18%	20.28%	38.97%
S&P 600 (Small)	1,364	0.41%	23.01%	48.52%
S&P 500 (High Quality)	50	1.51%	20.78%	28.23%
Russell 1000	4,831	2.01%	19.77%	30.85%
Russell 2000	5,631	1.47%	15.57%	39.62%
Dow Jones	35,295	1.58%	16.98%	26.23%
NASDAQ	14,897	2.18%	16.18%	28.03%
MSCI EAFE	2,325	2.42%	10.91%	27.65%
MSCI EM	1,284	2.13%	1.46%	17.27%

*represents total return

S&P Metrics	LTM P/E	NTM P/E	LTM EPS Growth	NTM EPS Growth
Current	23.23	20.72	31.87	16.35
Prior Month	23.68	20.93	26.85	18.94
Prior Year	24.34	21.98	-13.04	15.73

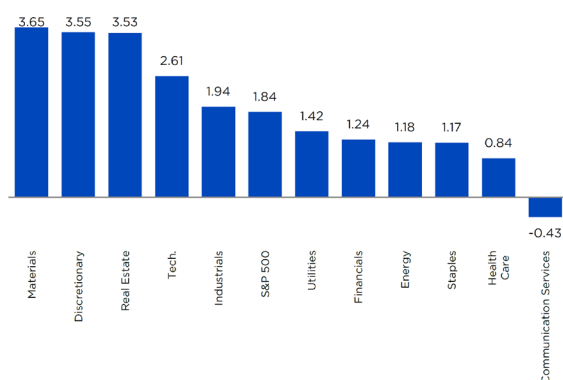
Fixed Income	Last	Returns		
		1 Week	YTD	1 Year
U.S. Aggregate	1.65%	0.33%	-1.72%	-1.09%
U.S. Inv Grade	2.24%	0.71%	-1.33%	0.99%
U.S. High Yield	4.76%	0.15%	4.35%	9.62%
TIPS	1.28%	0.65%	4.52%	6.13%

Rates	Last	Change		
		1 Week	YTD	1 Year
6M T-Bill	0.06%	-0.01	-0.03	-0.06
2 Yr Treasury	0.41%	0.09	0.28	0.27
5 Yr Treasury	1.13%	0.08	0.77	0.81
10 Yr Treasury	1.59%	-0.02	0.66	0.85
30 Yr Treasury	2.05%	-0.11	0.4	0.53

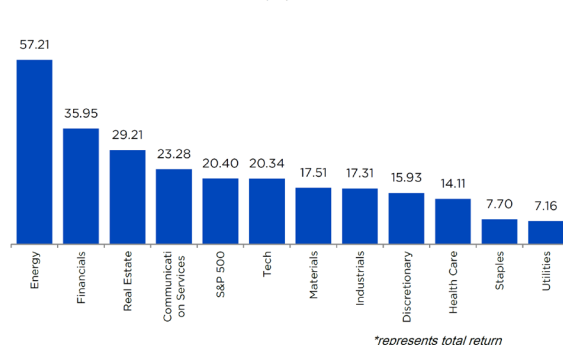
Spreads	Last	Change (Abs %)		
		1 Week	YTD	1 Year
AAA Rated	0.46	-0.02	-0.09	-0.25
BBB Rated	1.13	-0.01	-0.19	-0.59
High Yield	3.12	-0.08	-0.74	-1.89
10 to 2 yr Treasury	1.18	0.00	0.38	0.58

Commodities/FX	Last	Returns (Currencies in \$ strength)		
		1 Week	YTD	1 Year
Gold	1767.20	0.62%	-6.65%	-7.15%
Bitcoin	61455.23	14.05%	111.74%	434.74%
WTI Oil	82.28	3.43%	70.18%	101.47%
EUR/USD	1.16055	-0.27%	5.15%	0.80%
USD/JPY	114.07	1.81%	10.48%	8.34%

S&P Sector Returns — Week (%)

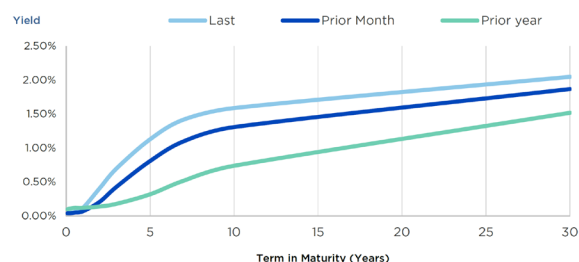


S&P Sector Returns — YTD (%)*



*represents total return

U.S. Yield Curve



Russell Style Returns — Week

	Value	Core	Growth
Large	1.4	2.0	2.6
Mid	1.7	2.3	3.4
Small	1.0	1.5	1.9

Russell Style Returns — YTD

	Value	Core	Growth
Large	20.7	19.8	18.9
Mid	23.5	20.1	14.0
Small	27.2	15.6	5.1

Additional Economic Indicators

Previous Week's Indicators

	Period	Actual	Previous
NFIB small business optimism index	Sept.	99.1	100.1
JOLTS job openings	Aug.	10.4 M	11.1 M
Consumer price index (m/m)	Sept.	0.4%	0.3%
CPI (y/y)	Sept.	5.4%	5.3%
Core CPI (m/m)	Sept.	0.2%	0.1%
Core CPI (y/y)	Sept.	4.0%	4.0%
Initial jobless claims	Week ending Oct. 9	293,000	329,000
Producer price index	Sept.	0.5%	0.7%
PPI ex food and energy	Sept.	0.6%	0.6%
Retail sales	Sept.	0.7%	0.9%
Retail sales ex autos	Sept.	0.8%	2.0%
Import prices	Sept.	0.4%	-0.3%
NY Fed Empire State manufacturing index	Oct.	19.8	34.4
Consumer sentiment	Oct.	71.4	72.8

This Week's Indicators

	Release Date	Period	Forecast*	Previous
Industrial production	Mon.	Sept.	0.3%	0.4%
Capacity utilization	Mon.	Sept.	76.6%	76.4%
NAHB housing market index	Mon.	Oct.	77	76
Housing starts	Tues.	Sept.	1.61 M	1.62 M
Building permits	Tues.	Sept.	1.70 M	1.72 M
Initial jobless claims	Thurs.	Week ending Oct. 16	287,000	293,000
Philadelphia Fed manufacturing index	Thurs.	Oct.	33.6	30.7
Existing home sales	Thurs.	Sept.	6.15 M	5.88 M
Index of leading economic indicators	Thurs.	Sept.	0.4%	0.9%
Markit flash manufacturing index	Fri.	Oct.	60.9	60.7
Markit flash services index	Fri.	Oct.	55.9	54.9

* Nationwide Economics Forecast



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