Summary

For the holiday-shortened week, economic data included gains in retail sales, consumer sentiment, and homebuilder sentiment, while industrial production was little changed, and several housing metrics weakened.

Equities gained in the U.S. as earnings reports have started, while foreign stocks fell back. Bonds lost ground globally upon higher interest rates and a stronger dollar. Commodities were mixed, with little change in crude oil prices last week.

Economic Notes

(0/+) **Retail sales** rose by 0.6% in December, exceeding the 0.4% rise expected. Headline sales were led by a 1% rise in autos but offset by a -1% decline in gasoline sales, in keeping with lower energy prices. Removing the more volatile components, core/control sales gained 0.8%, well above the 0.2% forecast. With a holiday boost during the month, department store sales rose 3%, followed by gains in non-store/internet, clothing, misc., and sporting goods; on the other hand, furniture, electronics, and health/personal care saw declines. On a year-over-year basis, retail sales rose 5%, which represents a reacceleration higher from the lows of last summer and back into positive results on an after-inflation basis.

(0) **Industrial production** rose 0.1% in December, in contrast to an expected -0.1% decline. Among the primary segments, manufacturing rose by a tenth (led by auto production rising nearly 2% and high-tech equipment up a percent), mining rose nearly 1%, while utilities output fell -1% (the latter largely being weather-dependent, which could well reverse based on frigid January conditions). **Capacity utilization** was unchanged at 78.6%. Over the past year, overall industrial production is up only 1% over the past year, with dispersed results by category. High-tech equipment production was up nearly 20% (with help from the CHIPS Act and related programs), with auto production rising nearly 5%.

(-) The **Empire Manufacturing index** fell by a substantial -29.2 points to a deeper contractionary level of -43.7 in January. In fact, this ended up at the deepest trough in the history of the series, other than the early pandemic days of April 2020. Other components were also sub-par, as new orders fell by -38 points to -49, and shipments fell -25 to -31. Prices paid rose by over 6 points, further into expansion. On the more positive side, employment ticked up by over a point but remained slightly in contraction, and assessments of business conditions six months out rose 7 points to an expansionary 19 level, which bodes well for future sentiment. This has been a volatile series compared to national ISM, which could be related to seasonal adjustments, as are a variety of indicators in recent years.

(0) The **Philadelphia Fed manufacturing index** rose by 2.2 points to a still-contractionary -10.6 level for January, below the -6.5 median forecast. Under the hood, data was stronger, with new orders, shipments, and employment all improving, but remaining in contraction. Prices paid fell back on the month but remained in expansion. On the negative side, assessments of business conditions over the next six months fell by -17 points, falling back in contraction.

(-) **Existing home sales** fell -1.0% in December to a seasonally-adjusted rate of 3.78 mil., below the 0.3% increase expected by consensus. While single-family units fell slightly, the bulk of the change was a -7% drop in multi-family. Regionally, sales in the West rose 8%, while the Midwest and South saw declines. The median sales price reaccelerated by nearly a half-percent to a year-over-year pace of 4.4%, to $382,600 to end the year. For inventory, months' supply fell to 3.2, but remains up from 2.9 in Dec. 2022.

It was noted that sales for 2023 overall sank to their lowest pace in 30 years, falling -6% on a year-over-year basis. In a sense, this isn't surprising, considering the shock in interest rates higher, not only suppressing affordability for new buyers, but also the lack of interest in selling by owners of current low-rate mortgages, lack of inventory generally, and a backlog in builder activity on the new home side. This would be considered a perfect storm of sorts, bucking the trend of usual price declines when rates rise, if supply were able to adjust normally as classic economics would dictate. Per the NAR, the bulk of national sales (44%) are in the $250-500k category, which is related to the growing demand for housing at more affordable price points but also higher averages.

(-) **Housing starts** fell in December by -4.3% to a seasonally-adjusted annualized level of 1.460 mil. units, above the 1.436 mil. expected. Single-family starts represented the whole of the decline, while multi-family units rose. Regionally, only the West saw gains, which were offset by declines elsewhere. Over the trailing 12 months, starts are up 8% overall, with single-family up 16% and multi-family down -8%. This is an acknowledgement of the strong need for new housing stock, especially on the more affordable side, while the strong cyclical apartment building trend has been fading following a stretch of strong activity. **Building permits**, on the other hand, rose 1.9% to a seasonally-adjusted annualized pace of 1.495 mil. On a year-over-year basis, the trend and compositional differences are even more pronounced, with overall permits up 6%, with single family up 33% and multi-family down -24%.

(+) The January **NAHB housing market index** of homebuilder sentiment rose by 7 points to 44, exceeding the 39 estimate. This was an improvement on recent poor results, but still remained below the 50 level that indicates 'neutral' sentiment. All segments improved, led by future sales expectations up 12 points to a positive 57 level; prospective buyer traffic gained 5 points but remained deeply in negative sentiment territory. The South and West saw the most significant regional gains, with the Northeast the only area with positive building sentiment. It's likely that easing of interest rate financing pressures have helped the situation in recent weeks for several of these housing metrics.

(+) The preliminary Univ. of Michigan **index of consumer sentiment** for January jumped 9.1 points to 78.8, well above the 70.1 level forecast by consensus. This was the strongest single month reading in over two years and continues a string of strong reports. Assessments of both current economic conditions and expectations for the future each rose by similar magnitude. Inflation expectations for the coming year fell -0.2% to 2.9%, while those for the next 5-10 years fell a tenth to 2.8%—both below expectations. Anecdotal commentary reflected the former, that inflation views had improved.

(+) **Initial jobless claims** for the Jan. 13 ending week fell by -16k to 187k, well below the expected rise to 205k, to the lowest level in a year. Continuing claims for the Jan. 6 week declined by -26k to 1.806 mil., in contrast to the forecasted increase to 1.840 mil. It appears that frigid winter weather across a good portion of thin contrast to have contributed to recent results more than other factors, noting the Midwest states leading the drop in claims numbers.

Market Notes

Period ending 1/19/2024	**1 Week %**	**YTD %**
DJIA	0.76	0.55
S&P 500	1.19	1.54
NASDAQ	2.26	2.01
Russell 2000	-0.33	-4.05
MSCI-EAFE	-2.13	-2.52
MSCI-EM	-2.54	-5.13
Bloomberg U.S. Aggregate	-1.10	-1.39

U.S. Treasury Yields	**3 Mo.**	**2 Yr.**	**5 Yr.**	**10 Yr.**	**30 Yr.**
12/31/2023	5.40	4.23	3.84	3.88	4.03
1/12/2024	5.45	4.14	3.84	3.96	4.20
1/19/2024	5.45	4.39	4.08	4.15	4.36

U.S. stocks fell back early in the week as Fed governor Waller's comments and strong retail sales pointed to a path of interest rates remaining higher for longer than the dovish sentiment of late 2023; however, they recovered by week's end to a new record high for the S&P 500. By sector, technology led with a 4% gain, along with strong semiconductor sentiment related to artificial intelligence projects (including Taiwan Semiconductor—granted an emerging markets stock), while energy and utilities each fell back by over -3%. Real estate declined -2% with interest rates rising a bit on the week.

Insofar as earnings for Q4 are concerned, per FactSet, only 10% of firms have reported results so far. At the same time, over 60% have experienced a positive earnings surprise, with a similar number showing a revenue surprise, likely related to very tempered analyst expectations at the moment. The blended earnings growth rate (already reported plus estimates) has deteriorated a bit from an expected near-2% at year-end to now -1.7%. Of course, this remains a moving target being so early in the cycle. Leaders continue to be communications, utilities, and consumer discretionary, with expected earnings growth in the double-digits. Energy and materials bring up the rear, with expectations of -30% and -20%, respectively, on the back of weaker commodities prices, which make their way into company profits with a lag. For the entire S&P, profit margins have been falling from average levels during the past three years, but remain above 10%, which is still an impressive result from a multi-decade perspective.

Foreign stocks, by contrast, fell back with the most modest declines in Europe and Japan offset by over -2% drops in the U.K. and emerging markets. Here, too, it appeared central bank resistance to 'too early' rate cuts damped sentiment (with 'summer' noted by the ECB as more probable than 'spring'), as did higher-than-expected inflation in the U.K. In emerging markets, Chinese stocks suffered the most, down just under -5% in U.S.-dollar terms, due to weaker retail sales and new home prices as the government injects targeted stimulus to boost growth results. Chinese valuations remain among the cheapest in the world, reflecting current negative sentiment.

Bonds fell back last week, with yields rising after expectations for central bank policy rates falling quickly were dashed. Senior loans fared best, with little change for the week. A rise in the value of the U.S. dollar index by nearly a percent punished foreign debt.

Commodities were mixed for the week, with gains in agriculture and declines in industrial and precious metals, while energy was little changed. Crude oil prices rose a fraction of a percent last week to $73/barrel, with little to move the needle other than the International Energy Agency raising expectations for demand growth this year. Natural gas prices dropped nearly -15% (and by a third over the past three months) as recent freezing weather looks to be improving; as one of the most volatile commodities, gas is dramatically affected by such seasonal effects and forecasts this time of year.

Have a good week.

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Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, National Association of Realtors, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, Univ. of Michigan, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post.

Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.