***Summary***

Economic data for the week included the Fed signaling upcoming rate hikes, a stronger-than-expected GDP growth report for Q4, and robust housing data, but a weaker durable goods report.

U.S. equity markets ended mixed to higher in a volatile trading week, with large cap stocks outperforming small caps. Foreign stocks generally were negative, in keeping with a stronger dollar. Bonds fell back broadly along with higher interest rates following a hawkish Federal Reserve. Commodities gained, mostly in the energy sector—particularly due to weather, Ukraine, and market technicals in natural gas.

***Economic Notes***

(0) The late January **FOMC meeting** ended with no change in the fed funds rate, as expected, but the timeline for a March rate hike was essentially solidified, as the tapering of quantitative easing-based bond purchases will end earlier in that month. Chair Powell's news conference after the meeting noted the increasing balance between different factors, such as the improving economy and employment markets, but also inflation and uncertainty and less balanced effects of Covid on some sectors and groups more than others. Noting two-sided risks now more than ever during the past few years, Powell noted that the Fed needs to remain 'humble and nimble'. That said, there is 'broad support on the committee' that conditions have strengthened, and could be appropriate for tightening, which would include even the more dovish members of the committee that had argued in favor of easy policy for some time (holding out mostly for full employment reasons).

A set of principles was laid out, noting a structure for monetary tightening, leaving more certainty about what tools are to be used when. As expected, interest rates were reinforced as the primary tool. Only once rate hikes have been underway would a reduction in the size of the immense balance sheet start to occur. These leaves a lot of leeway, but also points to the fine-tuning of maturing asset reinvestments being the next step, as opposed to asset sales, at least for now.

(+) The advance reading of U.S. **GDP** for Q4 2021 showed a 6.9% increase, beating expectations of 5.5%. The largest contributions originated from inventories (representing 4.9% of the total GDP result, but a common wildcard from quarter-to-quarter) and personal consumption in services (up 3.3%, and 2.3% of the total GDP number). On the downside, government spending fell back (-3%) as did structures investment (-11%). The GDP price index rose at a 6.9% annualized rate for Q4, above forecast, led by gains in fixed investments. The core PCE price index rose at an annualized rate of 4.9% in Q4, which generally met expectations.

Assessments of Q1-2022 GDP have already begun, with the Atlanta GDPNow coming out with an initial low estimate of 0.1%, with the range of blue chip forecasts falling between 2% and 5% (with an average of 3.5%). The negative effects of omicron here are apparent, with still-high demand held back by supply issues. GDP later in the year is expected to drift closer to the 2.0-2.5% secular average.

(0) **Personal income** for December rose 0.3%, short of the 0.5% forecast, led by a sharp rise in wage/salary income of 0.7%. **Personal spending** fell by -0.6%, in line with expectations, and led by far weaker consumption for durable goods, while service spending has started to pick back up again. Accordingly, the personal savings rate rose by 0.7% to 7.9%. On a year-over-year basis, income gained 7% (the strongest calendar year in the past 15), while spending grew by over 13%. The PCE price index rose 0.5% on both a headline and core level in December, just above expectations. This brought the trailing 12-month PCE gain to 5.8% and 4.9% on a headline and core level, respectively. Income has been marked by the fading of fiscal stimulus and rise in wages more recently, with spending held back by the inability to fulfill orders in some cases.

(-) **Durable goods orders** for December reversed course by falling back by -0.9%, a bit further than the -0.6% forecast, noting that the prior month results were generally revised higher. Due to aircraft being a decliner for the period, removing transportation, goods rose 0.4%, beating consensus by a tenth of a percent. Core capital goods orders were unchanged, while core capital goods shipments gained 1.3% for the month. For both of the primary durable goods series, orders were up 12-13% from levels a year ago. In fact, the headline orders are now up over 15% from the Feb. 2020 pre-Covid reporting levels.

(+) The **S&P/Case-Shiller home price index** rose 1.2% in November, beating expectations of 0.9%. All 20 cities in the index experienced gains, led by 2% rises in Seattle, Miami, and Tampa. The year-over-year price change decelerated a bit, by -0.2% to a still-robust 18.3%.

(+) The **FHFA house price index**, a broader survey, rose a similar 1.1% in November, matching the prior month and beating expectations by a tenth of a percent. All nine national regions saw gains, led by 2% in South Atlantic (MD through FL) and East South Central (KY/TN/MS/AL). The year-over-year national index growth rate ticked up a tenth to 17.6%. As with the Case-Shiller index, this remains near an all-time high for the series.

(+) **New home sales** rose a sharp 11.9% in December to a seasonally-adjusted annualized rate of 811k homes, a tick higher than the prior month's pace with revisions, and beating the median forecast of 2.2%. The months' supply of new homes fell by -0.6 to 6.0, with sales beating the smaller rise in inventories. (However, inventory growth has been dominated by the category of 'homes not started' and 'under construction', which are less helpful in the near-term to alleviate home price pressures.) Regionally, the South and Midwest saw gains in the 30-60k range, while the units fell in the Northeast slightly. Sales remain down -14% over the past year, although the median sales price rose by over 3% to $377,700, while the average price rose 14% over the last 12 months to $457,300.

(-) **Pending home sales** for December, on the other hand, fell by -3.8%, disappointing relative to market expectations of only a -0.4% drop. Sales fell in every region, with the -10% drop in the West leading the way, and lesser declines elsewhere. This measure tends to correlate to existing home sales in coming months to some extent.

(0) The Conference Board **index of consumer confidence** for January fell by -1.4 points to 113.8, but beat consensus expectations of 111.2. Assessments of present conditions rose by over 3 points, while expectations for the future fell by nearly -5 points. The labor differential, measuring the job-finding ease, ticked down a fraction of a point, but remained at levels hovering around all-time highs. In recent weeks/months, the offsetting conditions of Covid omicron variant uncertainty, a recovery in employment, but high inflation, leave consumers likely somewhat uncertain about 2022 to some degree.

(0) **Initial jobless claims** for the Jan. 22 ending week rose by 30k to 260k, but still below the 265k expected by consensus estimate. **Continuing claims** for the Jan. 15 week rose by 51k to 1.675 mil., above the median forecast of 1.653 mil. Initial claims rose more dramatically in CA (23k), while they fell by 4-5k in NJ, PA, and NY.

***Market Notes***

| Period ending 1/28/2022 | 1 Week (%) | YTD (%) |
|---|---|---|
| DJIA | 1.34 | -4.36 |
| S&P 500 | 0.79 | -6.93 |
| NASDAQ | 0.02 | -11.96 |
| Russell 2000 | -0.97 | -12.30 |
| MSCI-EAFE | -3.61 | -5.73 |
| MSCI-EM | -4.26 | -3.28 |
| Bloomberg U.S. Aggregate | -0.36 | -2.13 |

| U.S. Treasury Yields | 3 Mo. | 2 Yr. | 5 Yr. | 10 Yr. | 30 Yr. |
|---|---|---|---|---|---|
| 12/31/2021 | 0.06 | 0.73 | 1.26 | 1.52 | 1.90 |
| 1/21/2022 | 0.17 | 1.01 | 1.54 | 1.75 | 2.07 |
| 1/28/2022 | 0.19 | 1.15 | 1.61 | 1.78 | 2.07 |

U.S. stocks ended the week mixed to surprisingly higher, despite a see-saw week, and the S&P reaching -10% correction territory briefly, based on a Jan. 3 peak date. Stocks started the week sharply negative, with investors contemplating the potential language and tone from the mid-week FOMC meeting, along with ongoing inflation and slowing growth woes. In fact, it was reported Monday was the largest trading day in history for U.S. stocks, with 40% of that volume based on ETFs. At this rate, January 2022 will end up as the most negative market month since March 2020—given that it's been almost two years, we were about due for a correction, according to many strategist opinions. The Russell 2000 index of small cap stocks remain down almost -20% from November highs, near more extreme bear market territory. Interestingly, S&P implied volatility (VIX) had been fairly benign before ticking up to around 40, albeit just briefly—a region characteristic of corrections of the past decade. Trading of ETFs as a percentage of overall equity trading volume has ramped up to nearly a third, compared to last year's average of 25% (per Blackrock data).

By sector, energy stocks gained 5% on the back of higher crude oil prices, with both technology and financials each also faring positively—surprisingly, to some extent—due to each being the anchors of their respective 'growth' and 'value' style groups. Industrials, utilities, and consumer discretionary stocks lagged, with returns below -1% each. Real estate was down only minimally.

Foreign stocks were held back by a nearly-2% rally in the U.S. dollar last week, likely exacerbated by hawkish Federal Reserve language (higher interest rates tend to be bullish for a currency relative to peers, all else equal). While shares in the U.K. gained, Europe and Japan declined. Stocks in the emerging markets fell back as well, led by weakness in China and Korea, due to concerns over ongoing Asian economic slowing, while Russian stocks gained with energy prices and some optimism about resolution with Ukraine.

U.S. bonds lost ground for the week across the board, with interest rates at the middle of the yield curve ticking higher, along with the more hawkish Fed language. Corporates from investment-grade to high yield and bank loans also fared negatively, as spreads widened. Most notably, the 2-year treasury note rose about 15 bp in yield during Chair Powell's press conference, which was more open to tighter policy at a faster rate than markets expected beforehand. As implied by its maturity, the 2-year is somewhat of a proxy for the fed funds rate two years out. The 10-year yield vacillated, but ended higher, with the next significant technical level around 2.00%. Foreign bonds all fared negatively, in keeping with the much stronger dollar. The Bank of Canada surprised some by not raising rates last week, due to omicron concerns, but are likely to align with the Fed with hikes in a few months.

We've seen some comments from larger Wall Street firms about moving some fixed income back to treasuries (which were dramatically underweighted in some cases). This is interesting, not surprising, but also a reflection of the reactionary nature often seen in equity market drawdowns. Owning treasury bonds hasn't been a place to earn a fortune over the last few years (with the 10-year yield still well below 2%), but they have acted as one of the few portfolio building blocks that zig when equities zag. The time to buy insurance is before the house catches fire.

Commodities rose by several percent, with gains in energy and agriculture offsetting declines in industrial and previous metals. The price of crude oil rose by 2% to just under $87/barrel, while natural gas prices spiked by over 20%—the latter due to colder expected weather and a late week event with traded gas futures. The build-up of Russian troops at the Ukrainian border has fueled some of the oil move higher, although natural gas prices tend to be more regional. Europe sources roughly half of its natural gas needs from Russia, complicating their involvement politically or militarily, with prices already high.

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, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, 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.

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