Summary

Economic data for the week included U.S. GDP coming in for Q4 at a stronger pace than expected, in addition to positive reports for durable goods orders, new home sales, and consumer sentiment.

Global stocks rose last week, with the U.S. leading the way, upon rising hopes for the economy achieving a soft landing and inflation easing. Bonds were little changed on the week. Commodities were mixed, with both crude oil and natural gas prices falling due to higher supply pressures.

Economic Notes

(+) The first edition of Q4 2022 U.S. **GDP** came in at 2.9%, just below the Q3 pace of 3.2%, and above consensus estimates calling for 2.6%. For the 2022 full year, GDP rose 2.1%, in keeping with longer-term trend, but well below the recovery pace of 5.9% in 2021. For Q4 specifically, contributors included strength in inventories (contributing 1.5%, half of the overall growth figure), consumer spending, government spending, and nonresidential fixed investment. These were offset by declines in residential fixed investment (homebuilding largely, pulling -1.3% off of the gross growth number) and net exports. The overall result was far less impressive when the more cyclical items were removed, such as inventories, which are prone to reversal from more extreme readings from one quarter to the next. The GDP price index rose at an annualized rate of 3.5% in Q4, and 6.3% for the whole calendar year—the more recent deceleration being good news.

The Atlanta Fed's GDPNow initial measure for Q1 2023 shows a far lower estimate of 0.7%. This consists of expected positive growth from consumer spending and nonresidential fixed investment, while homebuilding and inventories are expected to drag on growth. While positive on net, this is certainly slower than Q4, and offers far less cushion from zero—reiterating recession risks.

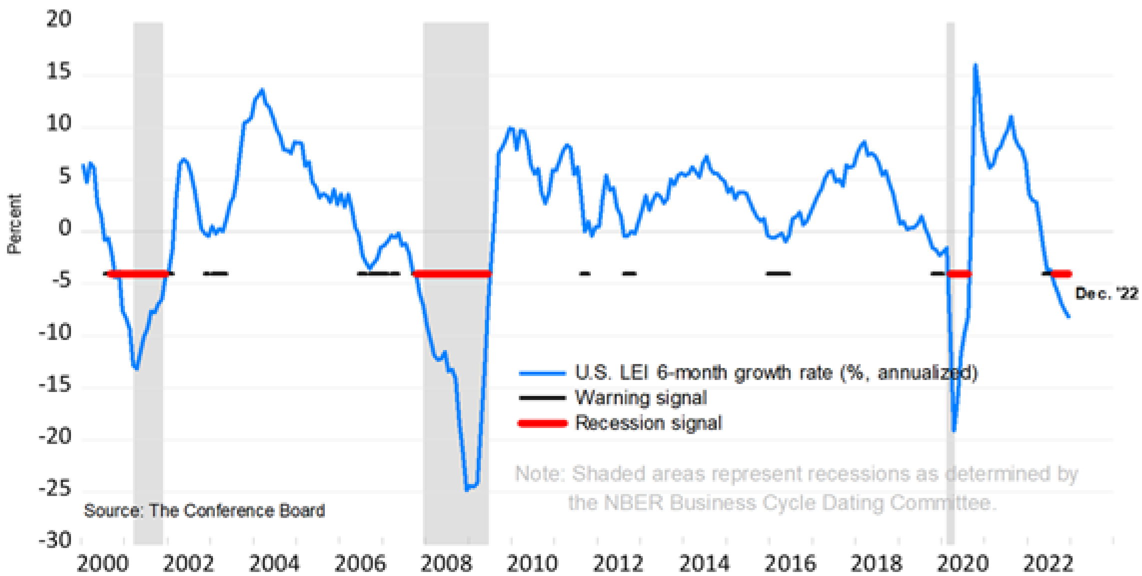
(0) **Personal income** for December rose by 0.2%, while **personal spending** fell -0.2%—both matching expectations. The latter coincided with waning stimulus payments, notably in CA, and caused the personal saving rate to tick up to 3.4%. Economists have been watching the waning effect on government transfer payments during the pandemic, as consumers either hoarded cash or spent on goods in the initial year, with spending moving toward services in the next round. Those resources seem to be running dry, with some expectations this may create incentive for employment, helping close current dislocations. PCE inflation rose by a rounded 0.1% and 0.3%, for headline and core, which brought the trailing 12-month inflation figures to 5.0% and 4.4%—obviously well above the Fed's target, but heading in the right direction.

(0) **Durable goods orders** for December rose a sharp 5.6%, reversing a decline the prior month and beating expectations of 2.5%, including upward revisions for prior months. However, removing transportation, the orders declined by -0.1%, just a tenth better than expected. The obvious difference was a 16.7% gain in transportation equipment, containing a 116% rise in non-defense aircraft/parts. This tends to be less predictable as a monthly series due to inconsistent and lumpy orders. However, capital goods orders generally rose 16%. For the full year, all durable orders rose 11%, and 6% on an ex-transportation basis. Removing the more sporadic defense and aircraft orders, core orders have flattened more recently, in keeping with other weaker manufacturing data.

(+) **New home sales** for December rose 2.3% to a seasonally-adjusted annualized rate of 616k, just above expectations calling for 612k, along with a downward revision for Nov. This resulted in a year-over-year decline of -26% (the largest calendar year drop since the financial crisis). The median sales price fell by -3.7% in the month to $442,100, while still up 7.8% over the trailing 12 months. Inventory came in at 9.0 months' supply, due to more rapid sales, down -0.2 from last month but up from 5.6 a year ago.

(+) **Pending home sales** rose by 2.5% in December, relative to an expected -1.0% drop, in addition to an upward revision for the prior month. This represented the first gain in seven months, so was taken positively, and tends to bode well for future existing home sales in the next several months. Looking backward, the pending sales index remains down -34% from a year ago.

(-) The Conference Board **Index of Leading Economic Indicators** for December fell by -1.0%, similar to the decline the prior month, and continuing to point to high recession odds. Weakness came from most segments, including labor, manufacturing, housing, and financial indicators. The measure is down -4.2% for the latter half of 2022, a steeper decline than the -1.9% drop in the first half of the year, with financial and non-financial components falling at roughly equivalent rates. However, the coincident and lagging indicators rose by 0.1% and 0.3% in December, respectively. While this index of course contains information we already know, the most useful part is the historical correlation of the mix of ten inputs with the economic cycle and recession periods.



(+) The final **Univ. of Michigan index of consumer sentiment** for Jan. rose by 0.3 of a point to 64.9, above expectations for no change from the early report (which had gained almost 5 points from the prior month). The total figure consisted of assessments of current conditions declining a bit, offset by an improvement in expectations for the future. Inflation expectations for the coming 1 year fell by a tenth to 3.9%, as did those for the next 5-10 years to 2.9%. However, as commentary noted, inflation uncertainty continues to weigh on respondents, as do the rising chances of an economic downturn by two-thirds of the group. This reiterates current anticipation for a recession by both businesses and consumers being among the highest in recent decades.

(0) **Initial jobless claims** for the Jan. 21 ending week fell -6k to 186k, below the 205k consensus forecast. Continuing claims for the Jan. 14 week rose by 20k to 1.675 mil, above the 1.658 mil. expected. These changes remain small on net, and are likely still influenced by year-end seasonal effects. However, they haven't shown much deterioration.

In governmental news, the Republican House leadership resurrected the concept of tax system overhaul—something that has been floating around for decades, but may reach a floor vote this year for the first time. The most recent '**FairTax**' plan would involve replacing all personal and corporate income, estate, gift, and payroll taxes with a national consumption tax (29.8% tax-exclusive), minus an annual 'family consumption allowance' (a type of standard deduction). The most recent national sales tax idea was first rolled out in 1999, was brought up again in 2008, and has received niche support over the years, but hadn't gained enough steam to proceed. Per the Tax Foundation, this would result in a significant reduction in revenue, and would require an extensive shrinking of the budget, which has been one of the primary goals of more conservative House members this year. Proponents of a national sales tax have pointed to the simplicity of the structure, logistics being far easier and less expensive to monitor and administer, as well being able to tap into revenue from the untaxed or black market economy that isn't being captured now through income taxes. Critics have pointed to the proposed abolition of the IRS and replacement of joint administration by state agencies and the Treasury Dept. as cumbersome. Additionally, despite the same rate applied to all purchases (less allowances), sales taxes have been labeled 'regressive' by progressive politicians. This is due to an implied heavier burden on individuals, particularly those in lower-income groups, who tend to spend a greater proportion of income than higher-income households (although the higher-income group tends to purchase more expensive items—so there is some disagreement between economists on the net impact). While chances of passage are low, the introduction of policy like this is often done for either shock value (as in, 'lower the Federal budget or else') or as a starting point for some type of more moderate tax reform and simplification. The U.S. has one of the more complicated Federal tax regimes, bolstered by decades of unique carve-outs and write-offs. Simplification proposals would obviously also have negative implications for the accounting and tax preparation industry.

Market Notes

Period ending 1/27/2023	**1 Week %**	**YTD %**
DJIA	1.81	2.60
S&P 500	2.48	6.11
NASDAQ	4.32	11.07
Russell 2000	2.37	8.58
MSCI-EAFE	1.40	8.55
MSCI-EM	1.44	9.95
Bloomberg U.S. Aggregate	0.09	2.99

U.S. Treasury Yields	**3 Mo.**	**2 Yr.**	**5 Yr.**	**10 Yr.**	**30 Yr.**
12/31/2022	4.42	4.41	3.99	3.88	3.97
1/20/2023	4.72	4.14	3.56	3.48	3.66
1/27/2023	4.73	4.19	3.62	3.52	3.64

U.S. stocks started the week decently, but fell back with negative guidance in technology. However, growth stocks continued to shine, with consumer discretionary (help from Tesla's earnings report/commentary) and technology both up 6% and 4% last week, respectively. Defensives health care and utilities ended slightly negative, to lag the rest of the pack. Real estate rose nearly 3%, despite higher interest rates last week. Overall, conditions point to the increasing possibility of a soft landing, with the economy slowing, but not slowing too fast, coupled with more tempered inflation readings. Eyes will be on the Federal Reserve meeting this coming week.

The S&P 500 continues to close right around the 200-day moving average, which, for technicians, is an important support or resistance point. It's also important because many have been taught that it's important, so can become self-fulfilling. If stock prices can rise and stay above this level, this might perpetuate a more recent bullish view; on the other hand, 2022 featured several attempt to breach that level, each of which failed. Of course, as we know through history, using the 200-day or other moving averages is no magic bullet to profitability, but it tends to be watched closely regardless.

Foreign stocks fared positively on net, but lagged the U.S. ECB members continued a hawkish tone, committing to higher rates in upcoming meetings, despite more economic uncertainty than in the U.S. which remains the wildcard. However, manufacturing/services PMI rose back above 50 into expansion, raising hopes for a potential soft landing in Europe as well. Emerging markets led developed, with gains in Asia piggybacking off of the China reopening. While Chinese markets are on holiday, China ETFs housed elsewhere continue to be traded, and continued to show gains last week.

Bonds and interest rates were little changed last week, with gains of a fraction of a percent in floating rate bank loans leading the way. A stronger dollar held back developed market foreign debt, while emerging market bonds rallied.

Commodities were mixed last week, with agriculture higher and energy down. Crude oil fell over -2% last week to just under $80/barrel, due to higher global supply reports. Further unexpected drops came in natural gas, which was down another -6% last week, with spot prices down about -50% over the last three months, due to warmer than average weather in both the U.S. and Europe which has caused supplies to stay 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, Tax Foundation, 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.