Summary

Economic data for the week was mixed, including disappointments in retail sales and industrial production. Consumer and producer inflation both came in higher than expected, while housing data was mixed, with fewer starts but stronger builder sentiment.

Global equities saw gains last week, despite mixed economic data. Bonds fell back as interest rates ticked higher along with higher-than-expected inflation data. Commodities were little changed, with crude oil prices only slightly higher.

Economic Notes

(-) **Retail sales** fell by -0.8% in January, which disappointed relative to the -0.2% median forecast, and reversed some gains from the prior month. Removing the more volatile products (gasoline, autos, and building materials, all of which saw declines), core retail sales fell a less dramatic -0.4%. Despite winter weather having a likely negative impact on headline sales, non-store/online retail fell nearly a percent as well, while restaurant sales rose nearly a percent. Furniture and department stores also saw gains in the month. Relative to a year ago, headline retail sales are up 0.6%, which falls into the negative when adjusted for inflation. The recent trend points to decreased consumer activity, with excess household savings finally running down, seen by rising credit balances. The magnitude of this decline in coming months remains to be seen.

(+) The **Philadelphia Fed manufacturing index** improved a strong 15.8 points back to expansionary territory, at 5.2, exceeding the expected contractionary -8.6. The composition was mixed, with new orders rising in the double-digits but remaining in contraction, while shipments rose back into expansion, as did the assessment of business conditions six months out. Employment fell nearly -10 points further into contraction.

(+) The **Empire manufacturing index** rose an even more dramatic 41.3 points to a just-under neutral level of -2.4, relative to the -12.5 expected. The composition here was stronger, with new orders rising over 43 points, but staying in contraction, while employment rose but stayed just under neutral. Shipments also gained strongly, tipping into expansion, while prices paid also reaccelerated higher to further expansion. There are thought to be some seasonal adjustment factors involved, due to the wild swings in this particular index relative to others over the past few years, potentially taking away from its usefulness.

(-/0) **Industrial production** in January fell by -0.1%, in contrast to a slight increase of 0.2% expected. Within the report, manufacturing production fell -0.5%, with only minimal declines in areas like auto production, while high-tech equipment production rose a percent—likely due to recent incentives for onshoring of tech manufacturing. Utilities saw a gain of nearly 6%, related to winter heating needs, while mining activity (including energy drilling) fell by over -2%. **Capacity utilization** came in at 78.5%, down -0.2% from the prior month and below expectations for a slight increase.

(-/0) The **Consumer Price Index** for January rose 0.3% on a headline level, and picked up to 0.4% on a core level, ex-food and energy. This was despite a -1% drop in energy prices during the month, including -3% in energy commodities (including gasoline), while food prices rose nearly a half-percent. On the core side, as a significant chunk of the overall index, shelter costs remained strong. This is even more the case on the side of owners' equivalent rent, which has diverged from normal rent due to higher home prices, creating some measurement distortions. Other areas of strength included transportation, medical services, and lodging; on the deflationary side were used car prices, which fell -3%. Some economists note a degree of 'January effect,' with year-end adjustments in prices (notably in areas like medical services and car insurance), similar to what occurs with worker salaries. This negates some of the single-month strength, but remains an upward price factor nonetheless.

Year-over-year, headline CPI decelerated from 3.4% to 3.1%, while core CPI came in unchanged at 3.9%. Energy commodity prices fell by -7% over the year, driving the headline part of the index, while core remains stickier than hoped. These 3-4% readings continue to disappoint markets, although they represent significant improvement compared to peak inflation of over 9% at one point during mid-2022. Part of this is due to the Fed's self-imposed target of 2%, considered an arbitrary 'sweet spot' of 'just enough' inflation that coincides with trend economic growth, albeit not 'too much.' Historically, over the past century over which CPI has been measured, 3% has been the average rate, with the low inflation of the past few decades an anomaly. This recent strength likely pushes out the Fed's timeframe for this year's rate cuts, which has disappointed markets.

(-) The **Producer Price Index** for January rose 0.3% on a headline level, and 0.5% for core, subtracting food and energy—each was above the expected 0.1% increase. It appeared that routine annual price increases here, too, played a role in the monthly results unique to January, including in areas like medical care. Year-over-year, PPI rose 0.9% and 2.0% on a headline and core level, respectively, which is far more tempered. This included the continued split between services prices rising just over 2% and goods prices falling by nearly -2% (affected by a drop in energy prices as well). This also reflects the divergent growth levels in the two parts of the broader economy.

(-) **Housing starts** fell -14.8% in January to a seasonally-adjusted annualized rate of 1.331 mil. units, disappointing relative to the expected no change. However, the prior month's growth was revised higher. The decline was focused in the multi-family segment (down -36%, a lot, even for that volatile series), while single-family starts fell nearly -5%—with both likely related to colder and wetter weather in certain regions. The Midwest and Northeast saw the most severe declines of -20% to -30%, which pointed to weather as a potential cause. Over the past year, overall starts are down by -1%, but split dramatically between a -37% drop in multi-family and 22% rise in single-family starts. **Building permits** fell -1.5%, underwhelming compared to the expected 1.3% increase. These were led by a drop in multi-family, while single-family permits rose. The path of multi-family/apartment building continues to decline, offset by the construction of needed single-family homes.

(+) The **NAHB housing market index** rose 4 points in February to 48, a few points better than the expected 46. This continued a string of improvements, following a prior string of negativity. All key categories saw similar levels of increase—current sales, future sales, and prospective buyer traffic. The West and Northeast experienced the strongest gains in the neighborhood of 7-9 points, with only the Northeast showing positive (above 50) sentiment.

(0) The preliminary **Univ. of Michigan index of consumer sentiment** for February rose by 0.6 of a point to 79.6, just below the 80.0 expected. Regardless, this was the strongest reading in nearly three years. Assessments of the current economic environment ticked down a bit but were offset by a rise in future expectations. Inflation expectations for the coming 1 year ticked up a tenth of a percent to 3.0%, versus no expected change, while those for the next 5-10 years were unchanged at 2.9%. Anecdotally, it appeared that labor market strength and continuing deceleration in inflation had helped the mood.

(0) **Initial jobless claims** for the Feb. 10 ending week fell by -8k to 212k, below the 220k forecast. On the other hand, continuing claims for the Feb. 3 week rose by 30k to 1.895 mil., above the 1.880 mil. expected. Claims were mixed by state, with increases on the coasts, which could be weather related, but overall, no dramatic change here.

Market Notes

Period ending 2/16/2024	1 Week %	YTD %
DJIA	0.02	2.76
S&P 500	-0.35	5.15
NASDAQ	-1.31	5.18
Russell 2000	1.17	0.40
MSCI-EAFE	1.47	1.04
MSCI-EM	2.11	-0.65
Bloomberg U.S. Aggregate	-0.55	-2.01

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
2/9/2024	5.44	4.48	4.14	4.17	4.37
2/16/2024	5.44	4.64	4.29	4.30	4.45

U.S. stocks started decently but ran into the wall of CPI inflation on Tuesday morning, which showed less improvement than expected. However, weaker retail sales helped the slowing growth narrative, as the timing and depth of interest rate cuts have been the primary concerns of markets over the past several weeks. While there were a variety of factors related to the new year, stickier prices could cause the Fed to delay the implementation of rate cuts further into the year.

By sector, energy and materials earned gains of over 2% last week, while technology fell back by over -2%. Real estate was little changed, despite the higher interest rates over the week. Small cap stocks also outperformed large caps, with cheaper valuations there finally seeing more media coverage.

Foreign stocks outperformed U.S. stocks for the week, with gains in the U.K. and Japan outperforming minimal change in Europe. In contrast to the U.S., inflation showed better signs of easing, with the U.K. having fallen into recession in Q4 and the Bank of England poised to cut rates. In Japan, while corporate earnings have come in decently, economic growth has been somewhat weaker than expected, hovering around recession levels for Q4 as well. Chinese markets were closed for the Lunar New Year holiday, but U.S.-traded ETF assets traded higher.

Bonds were held back last week by rising interest rates—again related to the stronger inflation data, which pushes out the expected Fed easing regime. U.S. government and investment-grade corporates declined to similar degrees, while floating rate bank loans earned a small gain. Foreign bonds were generally down, along with a stronger dollar.

Commodities were little changed in total, with gains in industrial metals offset by a decline in agriculture. Crude oil prices rose 2% last week to $78/barrel, as still-high U.S. and OPEC+ production has offset any risk premium from conflict in the Middle East, coupled with slower demand. Natural gas prices declined -10% along with less severe winter weather.

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, 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.

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