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ECONOMIC TALKING POINTS
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Consumer Spending Beyond the Stimulus Checks

An interesting mix of economic reports was released in the last 24 hours. When viewed together they appear to weaken the argument that the US is headed this year for explosive economic growth, surging inflation and sharply higher yields.

Retail Sales:
Let's begin with the 3% decline in retail sales last month. Household spending plummeted across nearly all categories, with declines most noticeable in autos, furniture, electronics, home improvement, clothing, sporting goods and at restaurants. Even eCommerce sales fell 5.4%. The one category that did show a pop was outlays for gasoline, which rose 3.5%, but that was mostly due to rising gas prices and not greater demand.

The fall in consumer spending last month was to be expected. People in the Midwest and South were confined to their homes due to a devastating snow and ice storm. That deep freeze led to large swatches of power failures, water pipe bursts and causing overall damages estimated to be more than $18 billion.

Now that weather conditions are returning to seasonal norms, Americans should resume shopping. Fueling this next wave of expenditures is the passage of President Biden's $1.9 trillion American Rescue Plan. That legislation provides an additional $1,400 to each qualified American and allows more pent up demand to be unleashed.

But let's take a step back for a moment to get a broader perspective on just how durable this spending really is.

The latest round of payments represents the third major stimulus check people received from the government since March 2020. The first check was for $1,200 and it led to a steep upswing in household spending late in the 2Q 2020. That was followed by a second round of checks in December, this time in the amount of $600. Not surprisingly that also ramped up consumer purchases in January 2021. And there is no doubt the newest stimulus of $1,400 will lead to another jump in retail sales.

The position we're taking is that these spurts in household outlays are being triggered by singular events ––the stimulus checks. We do not yet see the kind of sustained increases in consumer spending that comes from an improvement in economic fundamentals, such as low unemployment and rising wages.

The country is still far from those goals. Employment is down by more than 9 million from the pre-pandemic level. At least 20 million Americans are still collecting some form of unemployment benefits, compared to 2.1 million just 12 months ago.

And in terms of personal income, if we look at wages and salaries (thus excluding the stimulus checks), it is up just 1.1% over the year, while (PCE price) inflation during that time increased by 1.5%. So Americans actually lost purchasing power, though again that was partially made up by the stimulus checks.

But we need to look next what consumers may do beyond this latest check disbursement. There's no question those government payouts have led to more spending and helped boost personal savings to nearly $4 trillion. **However, it is also true that we're going to be transitioning from a period of fiscal stimulus to one of restraint by mid-year, with higher taxes in some form likely to take effect as early as next year.** It's not at all clear how strong consumer spending will be if the labor market remains soft and once those stimulus checks stop arriving. That is one of the reasons we are not yet on board with all those super-bullish economic forecasts for 2021 and 2022.

Treasury TIC data:
A second report in the last 24 hours that should get more attention these days is the government's monthly release on the Treasury International Capital (TIC) system. Given the massive and still growing size of the US budget deficit and national debt, are foreign investors still willing to finance more of these government IOUs? Apparently, yes!

Foreign purchases of US Treasuries in jumped by the most in six months in January! And the two largest foreign investors were Japan, which boosted its holdings that month to $1.27 trillion, the most since last August.

China also couldn't resist the higher US yield and bought another $23 billion, lifting its holdings to $1.09 trillion, the most it has owned in more than 18 months. (Of course, such purchases also help rein in the RMB's appreciation, so it's a double bonus for China!)

Total foreign ownership of US Treasuries in January rose to $7.12 trillion, a 12 month high.

Here's what is noteworthy about these data points. There has been widespread concern that with US GDP racing towards 6% to 10% growth this year, we could see an upward spiral of inflation as well. All that activity would push yields on 10-year treasury notes to 2%, if not higher, this year. But what is often missed in the analysis is the desire of foreign investors (both private and central bankers) to buy US debt now that real returns look so much more attractive relative to the sovereign debt of all other industrial countries.

If we're to assume the US roll out of the vaccine continues to improve and the economy does pick up more speed, foreign demand for Treasuries will continue to increase and that should bid up the price of notes and bonds and keep yields from climbing to a point where it can snuff out US growth. Case in point: When the Treasury auctioned off its latest tranche of 10- year notes. There was still solid foreign demand.

This underlying foreign demand for US debt should therefore keep yields on the benchmark 10 yr hovering between 1.4% and 1.7% this year. And no one would be more grateful for this foreign appetite for US debt than Jerome

Powell, since it obviates the need for him to consider a policy of yield curve control.

Housing Market Index:
The housing market last year turned out to be the best in nearly two decades. We still believe 2021 will produce even stronger sales. But there may be some air pockets along the way.

The National Association of Home Builders reported that its Housing Market Index slipped two points in March, to 82. While any figure above 50 indicates healthy activity, we have detected rising frustration among builders about a confluence of forces that have clouded the outlook. They've already had to deal with the rising cost of lumber as well as other essential building material, the lack of suitable land and a shortage of workers. With home prices edging higher, builders wonder whether the recent rise in mortgage rates will begin to stifle demand for new homes this year and beyond. (Another looming factor is the disruptive technology of 3-D printers to build homes. How will affect standard home construction in the future? These 3D homes are starting to pop up around the country because they are faster to produce and cheaper to make.)

The recent rise in Treasury yields pushed the 30-yr mortgage rate above 3%, highest since last summer. Our latest model indicates that homebuyer interest will begin to wane as rates approach the 4.25% to 5.0% range. But I don't see those rates materializing until 2023 at the earliest.

Industrial Production:
No one should be terribly surprised by the 2.2% decline in industrial production last month. The deep freeze that screamed across major parts of Texas and the Midwest pulverized refineries, electrical utilities and manufacturers. Factory output alone fell 3.1% and mining sank 5.4%.

We expect to a see major bounce back this month in both output and capacity usage, given how lean inventories are on both finished goods and commodities.

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United States

	I 2020	II 2020	III 2020	IV 2020	I 2021	II 2021	III 2021	IV 2021	I 2022	II 2022	III 2022	IV 2022	I 2023	II 2023	III 2023	IV 2023
Real Gross Domestic Product (GDP):																
%	-5.0	--31.4	33.4	4.1	4.2	5.1	5.3	6.1	3.1	6.2	5.5	4.8	2.8	3.8	3.1	2.9
Personal Consumption Expenditures:																
PCE %	-6.9	-33.2	41.0	2.4	4.4	5.2	4.7	6.0	2.4	5.2	4.1	3.9	4.0	4.1	2.8	3.5
Inflation, end of period, year-over-year:																
CPI %	1.5	0.6	1.4	1.4	1.5	2.0	2.5	2.7	2.5	2.5	2.3	2.2	2.5	2.6	2.6	2.7
Unemployment Rate (end of period):																
%	4.4	11.1	7.8	6.7	6.2	6.0	5.9	5.8	5.8	5.8	5.6	5.4	5.4	4.9	4.4	4.1
Non-farm Payrolls, monthly avg. thousand:																
	-303	-4,427	1,322	283	322	385	370	380	270	285	265	240	185	225	235	250
Treasury 10-yr Note Yield % (end of period):																
	0.63	0.65	0.68	0.91	1.47	1.51	1.60	1.70	1.82	2.05	2.00	1.94	1.90	2.05	2.00	2.10
Federal funds rate % (end of period):																
	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.13	0.38	0.88	1.13

GDP Growth - Global Economy

Country	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
US	2.6	1.6	2.2	1.8	2.5	3.1	1.7	2.3	3.0	2.2	-3.5	5.1	5.3	3.2
Eurozone	1.7	1.4	-0.9	-0.2	1.4	2.1	1.9	2.5	1.9	1.2	-6.8	3.3	2.5	2.0
United Kingdom	1.7	0.7	0.3	1.8	2.9	2.2	1.9	1.9	1.3	1.5	-9.9	4.4	4.6	3.1
Japan	4.6	-0.4	1.6	1.5	-0.1	1.1	0.5	2.2	0.3	0.7	-4.8	2.4	2.8	2.2
Canada	3.1	3.1	1.8	2.3	2.9	0.7	1.0	3.2	2.0	1.6	-5.1	5.4	3.4	2.9
India	8.4	8.6	6.7	4.9	7.4	8.0	8.1	7.2	6.8	4.8	-8.2	9.1	6.4	5.7
China	10.5	9.5	7.8	7.7	7.3	6.9	6.7	6.8	6.6	6.1	2.3	6.9	5.7	5.6
Brazil	7.5	2.7	0.9	2.3	0.1	-3.5	-3.5	1.2	1.2	1.1	-4.1	2.9	2.7	2.4
Mexico	5.2	4.0	3.9	1.4	2.3	2.7	2.7	2.4	2.1	-0.1	-8.3	3.3	2.8	2.7
Australia	2.8	2.6	3.6	2.4	2.6	2.5	2.4	2.4	2.7	1.8	-1.1	2.5	3.0	2.7
Russia	4.0	4.3	3.4	1.3	0.6	-2.8	-0.2	1.6	2.5	1.2	-3.1	2.4	3.3	2.0
World	4.2	3.1	2.5	2.6	2.8	2.8	2.6	3.4	3.2	2.9	-4.2	4.4	4.2	3.9