OBSERVATIONS

- Producer prices rose +1.0% month-over-month (MoM) in January from December, and +9.7% on a year-over-year (YoY) basis. Excluding food, energy, and trade, producer prices rose +0.9% MoM, while having risen +6.9% YoY — slightly below December's record high +7.0% YoY reading.[1]
- Japan's economy resumed growth in Q4 2021, achieving +1.3% growth from Q3 2021 and marking the fastest quarterly growth rate for the island nation since Q4 2020.[1]
- U.S. retail sales rose by +3.8% in January from December, nearly doubling expectations. Compared to the same month a year ago (Jan-2021), retail sales were up +13.0%. These strong retail sales gains reflect both the rise in inflation over the past year as well as continued spending by the U.S. consumer.[2]
- U.S. industrial production increased by a healthy 1.4% in January over December, and it is now +4.1% higher than January-2021. Capacity utilization also increased in January to 77.6%, which is 1.9 percentage points below long-run average (1972-2021) of 79.5%.[3]
- Unlike in the U.S. and Europe, Chinese inflation remains muted and registered just +1.5% year-over-year (YoY). Meanwhile producer prices, which spiked in China last year, eased modestly in January to +9.1% YoY.[4]
- Jobless claims rose to 248k during the most recent week, while the four-week moving average stands at 243k. New claims have, generally, remained below 250k per week since mid-November 2021.[1]
- As Europe continues to see natural gas supplies from Russia diminish, the U.S. has emerged as the primary beneficiary. The U.S. passed Qatar as the largest exporter of liquified natural gas (LNG) during December while supplying nearly half of the total LNG delivered to Europe last month.[5]

EXPECTATIONS

- The Russia-Ukraine crisis seems to be inching towards a conclusion of sorts. The White House warned late last week that a Russian invasion could come at any time. Whereas the joint Russian-Belarussian military exercises concluded on 20-February and no Russian invasion has yet materialized.[6] The likelihood of a Russian invasion still seems a 50-50 proposition, but unless the invasion begins soon the prospect is likely to diminish as the costs of keeping nearly 20% of their military deployed to the border mount every day.

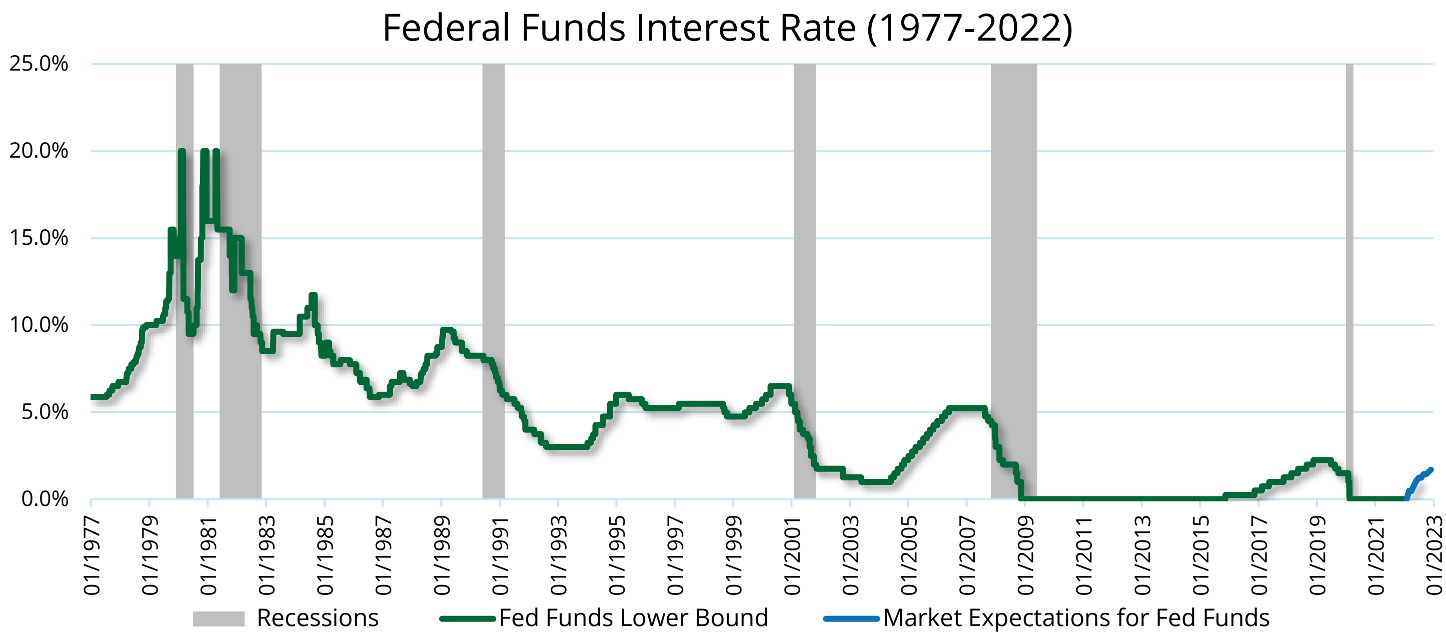
ONE MORE THOUGHT[7]: *Too much too soon?*

The Federal Reserve is tasked with two objectives, known as its dual mandate, of achieving not only price stability but also maximum sustainable unemployment. Recent data continues to validate the market's views that unemployment objective has been met while inflation data continues to surprise to the upside. As a result, Federal Reserve officials have spent considerable time in recent weeks, if not months, preparing markets for an eventual withdrawal of its bond buying program as well as interest rate hikes. Expectations for rate hikes in 2022 have climbed from three 0.25% hikes (as of 1-Jan-2022), to nearly seven 0.25% hikes (as of 17-Feb-2022, see **Chart of the Week**). The significant shift in expectations is in part based on the incoming inflation data as well as an evolving view that the Fed is behind the curve in this regard. Short term bond markets have similarly responded, with the 3-

[1] *Bloomberg LP*
[2] *https://www.census.gov/retail/marts/www/marts_current.pdf*
[3] *https://www.federalreserve.gov/releases/g17/Current/default.htm*
[4] *Credit Suisse Economics "China Data: Both headline and PPI inflation continued to fall" 16-Feb-2022*
[5] *https://www.wsj.com/articles/europes-energy-crisis-pays-off-for-u-s-natural-gas-sellers-global-traders-11645099204?mod=markets_lead_pos5*
[6] *https://www.wsj.com/articles/ukraine-troops-told-to-exercise-restraint-to-avoid-provoking-russian-invasion-11645185631?mod=hp_lead_pos1*
[7] *Bloomberg LP, Clearstead, data as of 17-Feb*

Month U.S. Treasury bill yield moving from 0.1% at year end to 0.4%. Meanwhile the 2-Yr U.S. Treasury yield has risen from 0.7% to 1.5% over that same period — begging the question is the market moving too far too soon? Markets appear to be in extrapolation mode, particularly related to recent inflation. Our view continues to center around the likelihood that inflation is in a peaking process with a lower trajectory likely for the second half of 2022 (as always, we continue to test our baseline views). Importantly, the Fed is likely to maintain its data dependent path, acting in accordance with the data that come in. That in of itself is likely to lead to either; the Fed being behind the curve or the Fed being correct about its general stance that while inflation is high, many aspects are transitory and are likely to fade in time (yes, they have been wrong with respect to timing of transitory). Combining these points together we have generally concluded that the markets expectations for six to seven 0.25% rate hikes are likely too much too soon. Markets are betting on policy not directing them. Most importantly, markets appear to be <u>betting on the path of rate hikes, not the end point of rate hikes</u>. For investors, we continue to think best to brace for additional volatility in both equity and bond markets as both digest the Fed's new policy.

CHART OF THE WEEK



Source: Clearstead, Bloomberg LP, as of 14-Feb-22, Market expectations based on Federal Funds futures

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