

The US Economy & Financial Markets in 10 Slides

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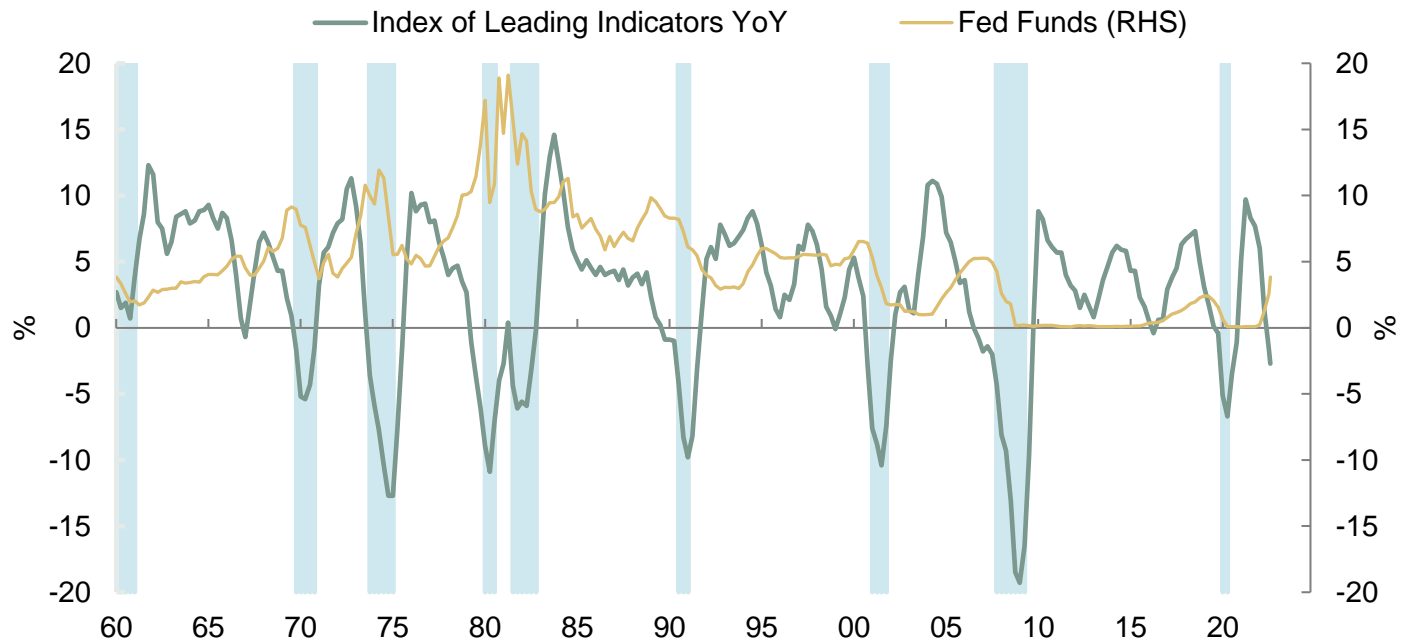
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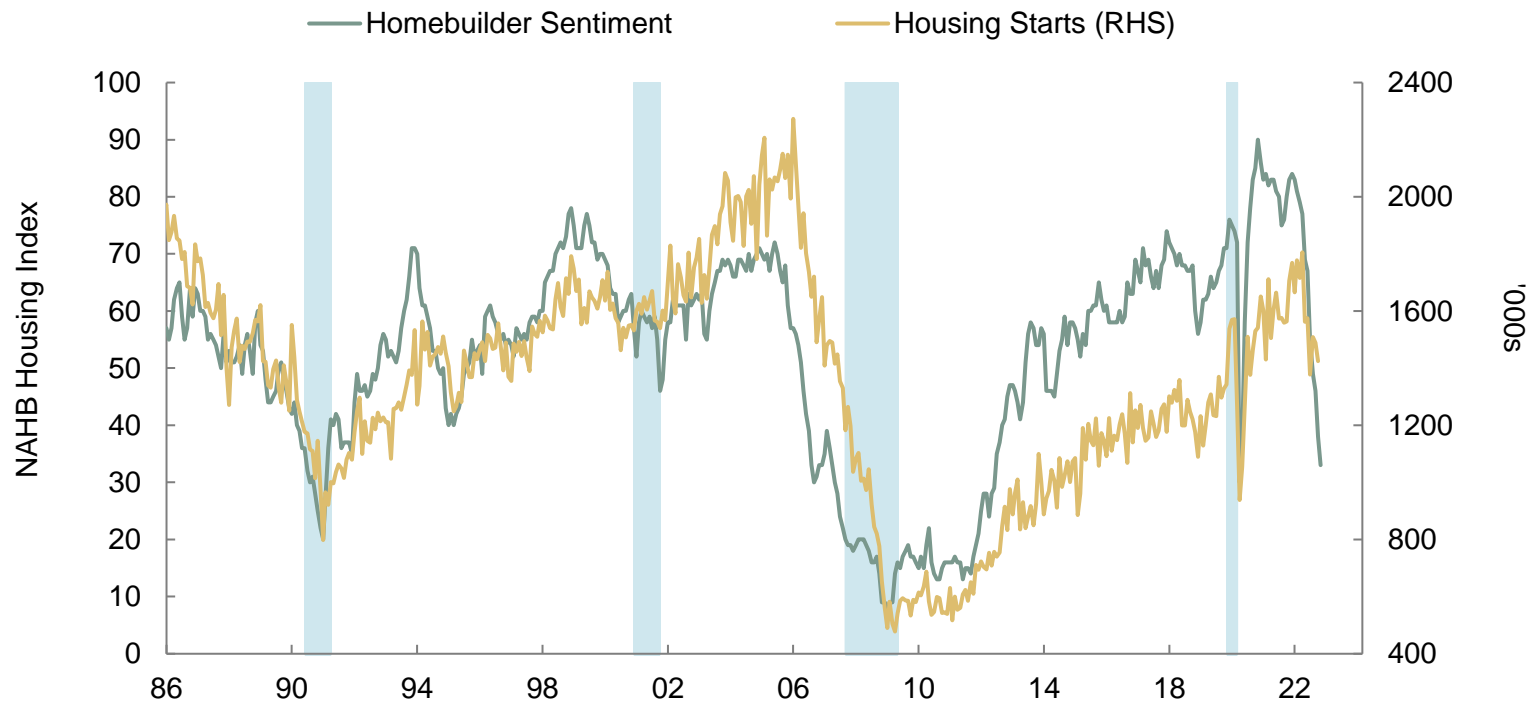
Tightening Into A Slowdown

- The Index of Leading Economic Indicators is down nearly 3% over the last 12 months. In the past, the Fed never has raised interest rates when the index was declining. Recession ahead?



Hard Landing For Housing

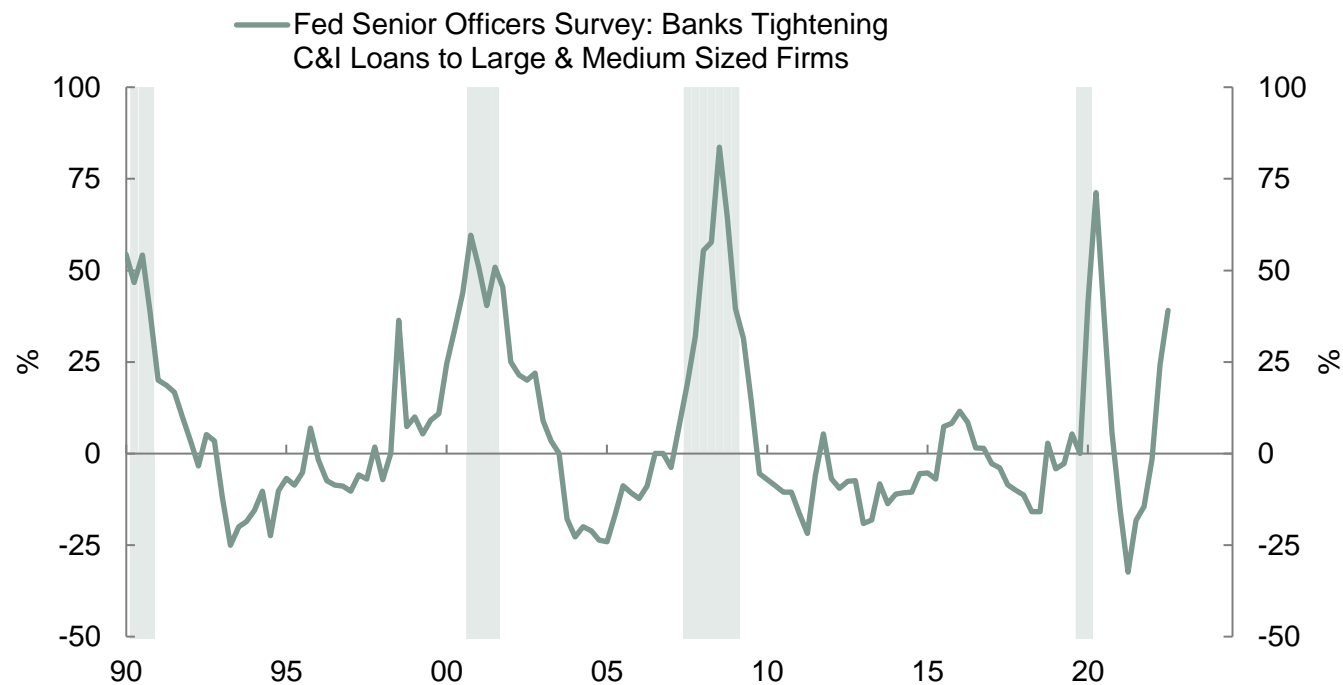
- Homebuilder sentiment has plunged to its lowest (non-pandemic) reading since the GFC. Over the past year, sentiment is down 50 points, the largest 12 month drop record. This points to sharply low housing starts and construction activity going forward.



Source: National Association of Home Builder, US Census Bureau, Bloomberg, Federal Reserve, SMBC Nikko

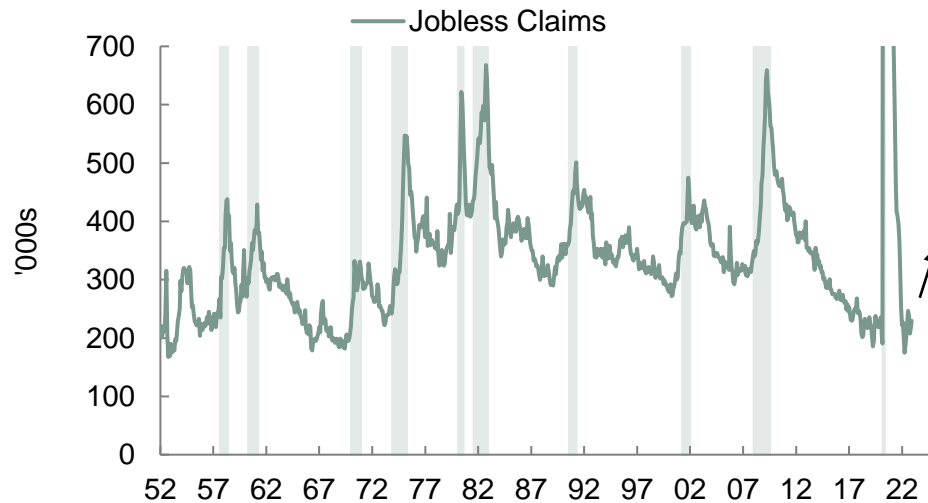
Rapid Tightening In Lending Standards

- Loan officers are quickly tightening standards on highly cyclical commercial and industrial loans. With ISM manufacturing slightly below 50, has a factory sector recession just begun?



Rising From A Low Level

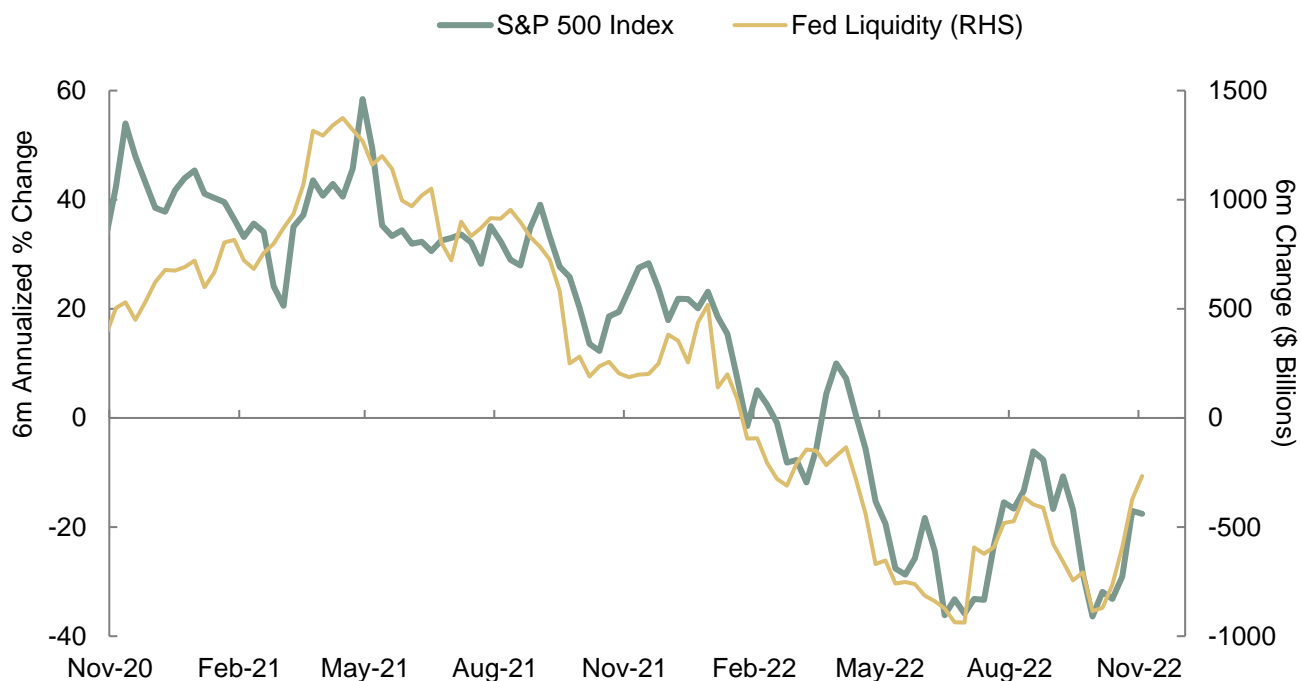
- **Jobless claims are leading indicator of the labor market. Claims averaged 320k during the onset of previous recessions but we found the percentage increase from their cyclical low is even more important. The upshot is that the labor market can weaken sharply.**



Date	Claims at Recession Onset	% Change From Trough
Sep-52	207	23.2
Sep-54	235	15.2
Apr-59	294	20.5
Apr-66	221	23.5
Feb-73	255	14.9
Sep-78	413	27.5
Mar-81	438	7.4
Jan-89	367	26.6
Mar-00	388	42.6
Feb-06	380	30.1
Average >	320k	23%

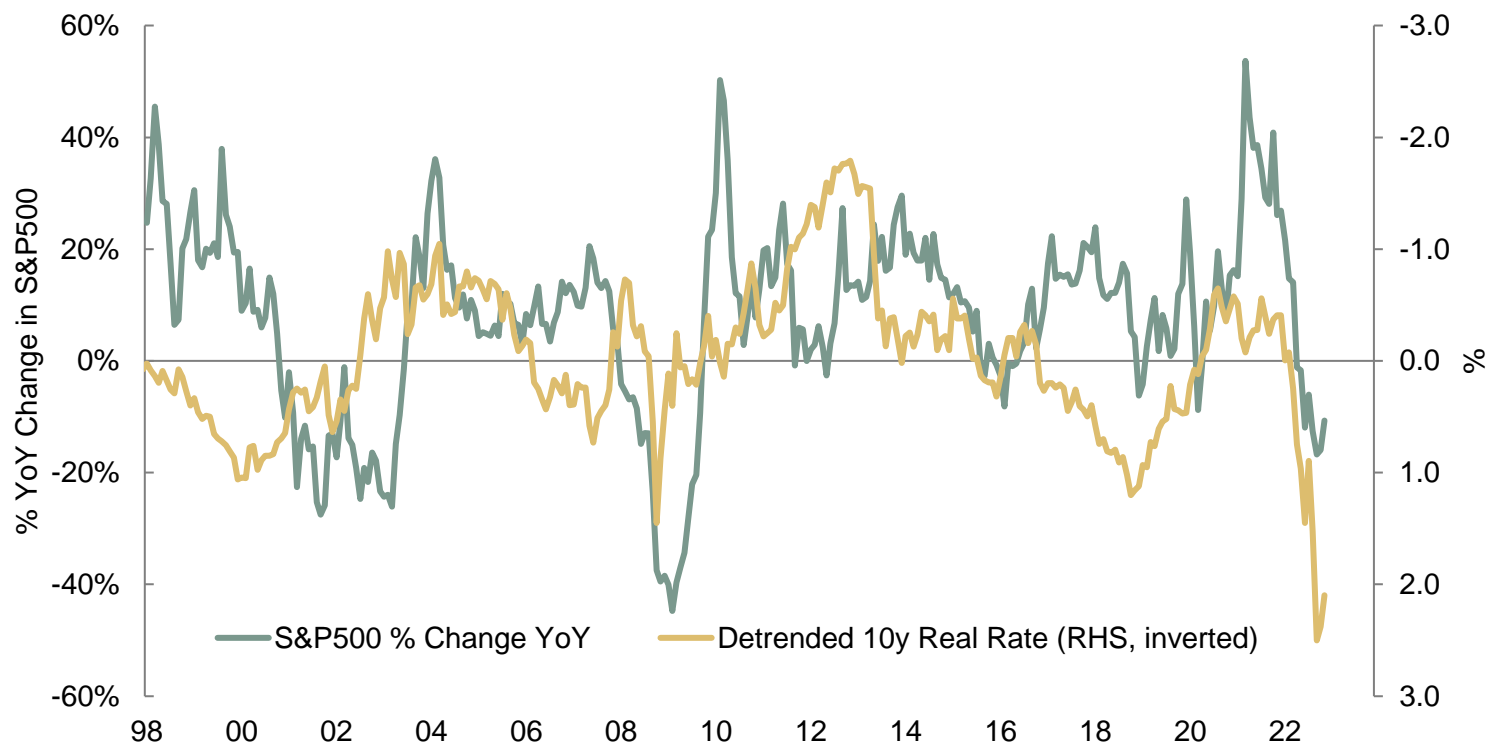
Fellow Travelers: Stocks & Liquidity

- Over the last two years, the correlation between the change in stock prices and Fed liquidity is nearly 0.95. The persistence of quantitative tightening will remain a headwind to equity market recovery in addition to currently high real interest rates (next slide).



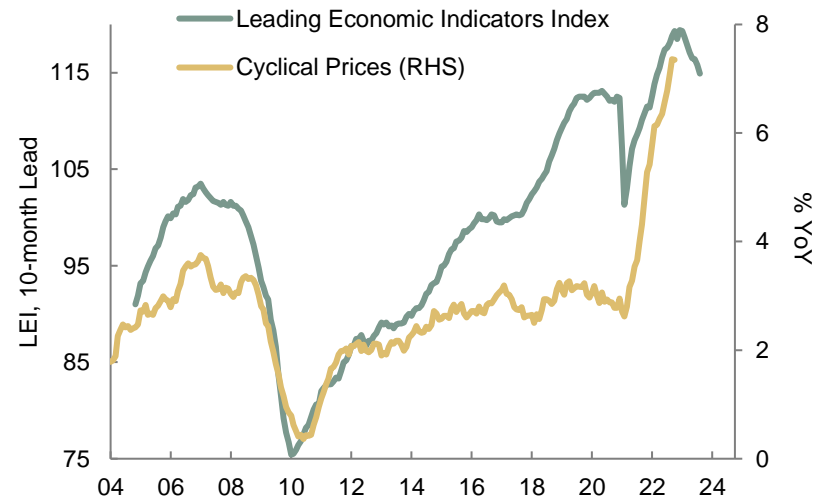
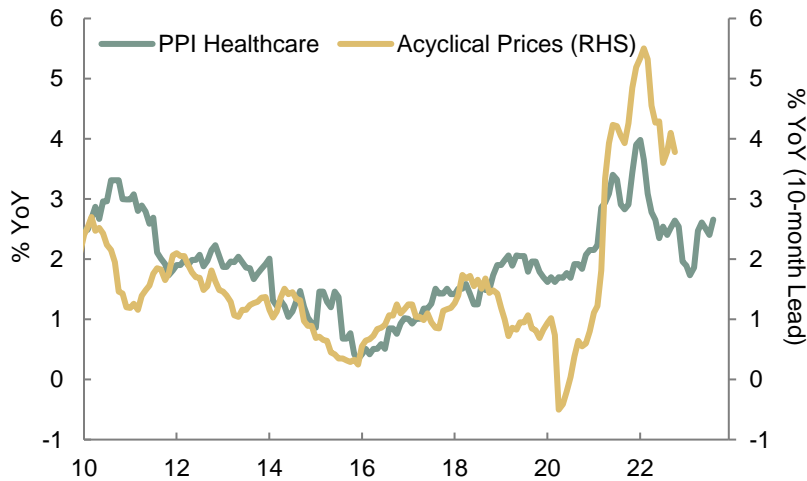
An Elevated Real Rate of Interest

- According to our calculations, the real rate is about 200 basis points (Inverted on chart) higher than its equilibrium level. It is no that wonder financial asset prices are under downward pressure!



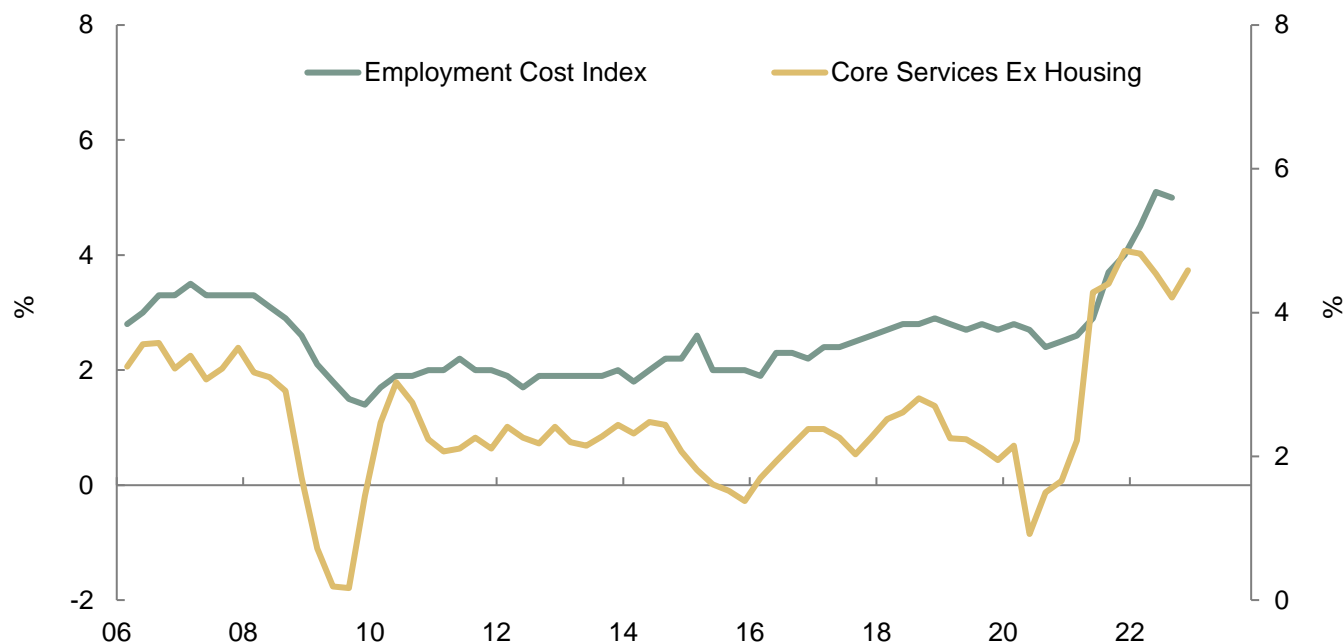
Past The Peak

- The core PCE deflator can be split down into two components: acyclical and cyclical inflation. Slowing healthcare prices point to slower acyclical inflation while the sharp drop in the Index of Leading Economic Indicators points to an imminent slowing in cyclical inflation.



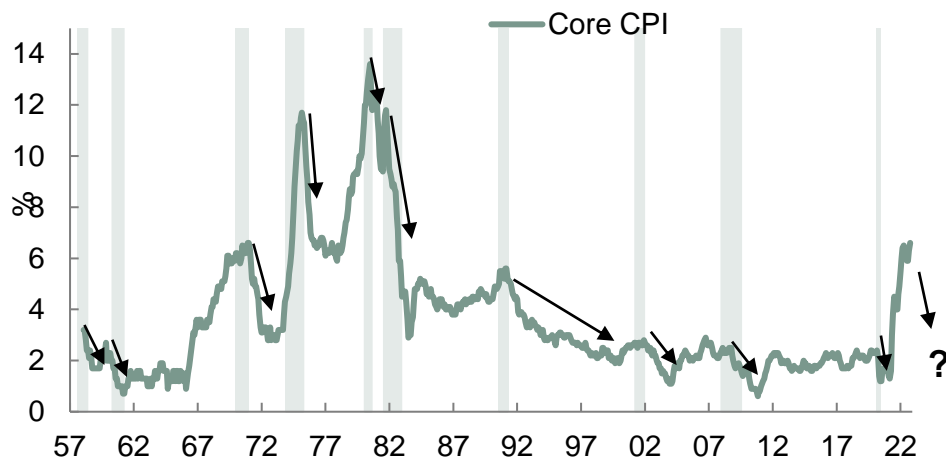
Chair Powell Says...

- The price of core PCE services excluding housing (shown below) is “the most important category for understanding the evolution of core inflation” according to Powell. So far, these prices are sticky but that could change when unemployment rises, thus forcing wages down.



Inflation Symmetry

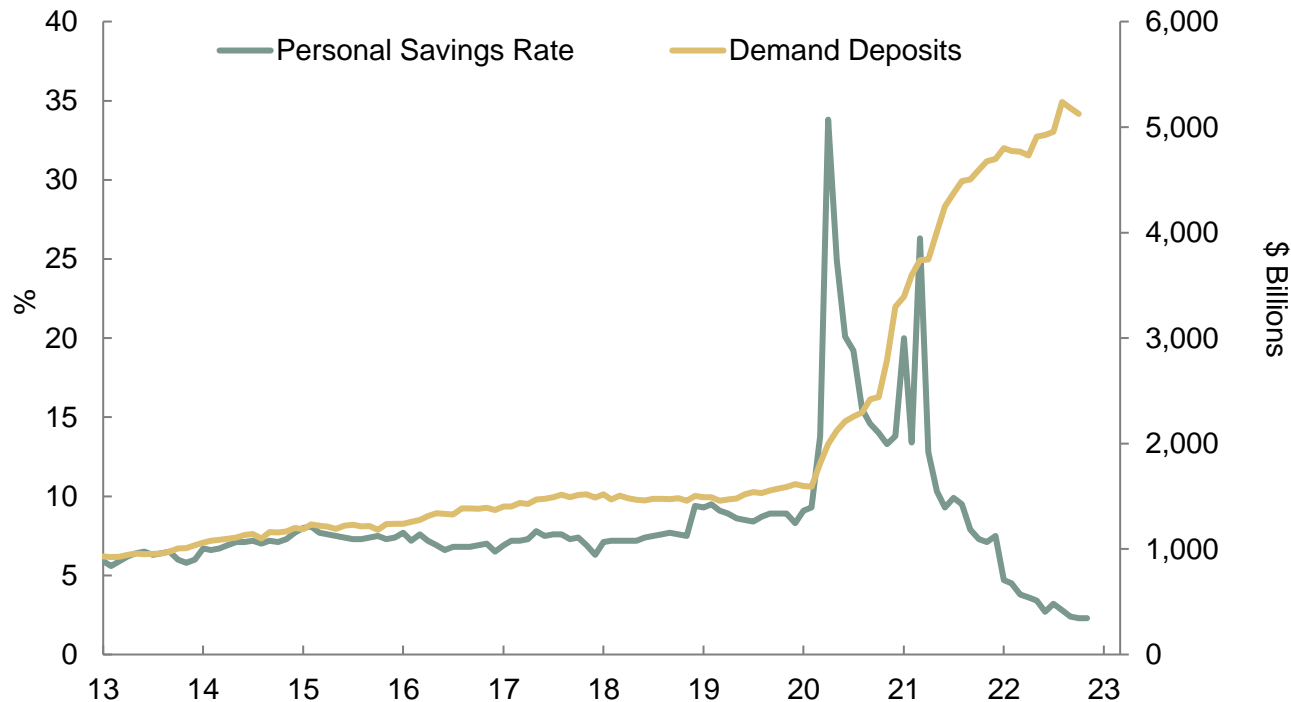
- Inflation has risen sharply but now appears to be reversing course. Historically the deceleration in prices has been the mirror image (i.e., symmetrical) of the acceleration in prices. This is evident from the accompanying table showing the slopes of the inflation upswing and downswing.



Inflation Upswing	Slope	Inflation Downwing	Slope
Sep 1940 to May 1942	0.35	May 1942 to May 1944	-0.47
Feb 1946 - Mar 1947	1.61	Mar 1947 to Apr 1949	-0.66
Jul 1949 - Feb 1951	0.58	Feb 1951 to Oct 1954	-0.21
May 1967 - Dec 1969	0.12	Dec 1969 - Jun 1972	-0.12
Jun 1972 to Dec 1974	0.37	Dec 1974 to Nov 1976	-0.31
Nov 1976 to Mar 1980	0.22	Mar 1980 to Jun 1983	-0.31
Jun 1986 to Sep 1990	0.07	Sep 1990 to Jan 1992	-0.25
Aug 2007 to Jul 2008	0.22	Jul 2008 to Dec 2008	-1.19
May 2020 to Jun 2022	0.38	Jun 2022 to ?	?
Average 1940-2008	0.44	Average 1940-2008	-0.44

Two Competing Factors

- The savings rate is close to an all-time low but accumulated savings are still high at a few trillion above their pre-covid level. Which factor will determine the future household behavior?



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