March 17, 2025

Monday Monetary Thoughts

When in doubt, do nothing

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Fed does not want to be the story

The Fed does not want to be the story this week. It's rare, but my view on the Fed this week is more political than economic though I think both ways end up in the same place.

If the Fed is hawkish, markets will probably weaken further; as a result, they'll take some of the heat off the White House for the recent selloff in equity markets. If they are dovish, they may well encourage the administration to dial up the heat even more. Thus, it's best to say nothing. The Fed is in watching the data, and "well positioned to wait for greater clarity" as Powell has noted recently.

The economic data leads me to a similar place too.

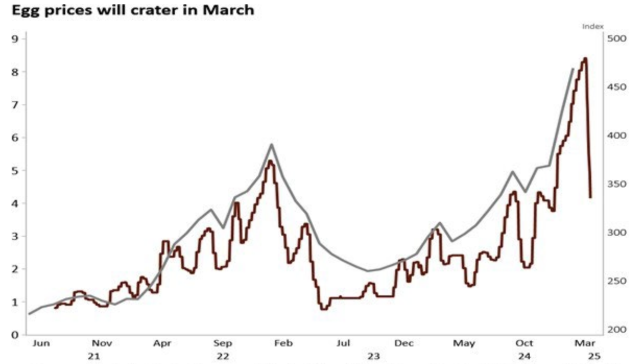
Growth is slowing, but there is no smoking gun just yet. Conditions are slowing, but so far, it has been in a linear fashion. Inflation progress has been bumpy. Inflation expectations have jumped, but consumer views on the labor market have cratered. Thus, it is fair to say that the Fed is facing pressure on both sides of its mandate

I expect a modest downward revision to GDP, perhaps taking growth to potential. Most current-quarter tracking estimates are running below 2.0 percent. I also expect a 0.1ppt increase in the core inflation estimate. Currently, I am tracking 2.7 percent for core PCE year-on-year. I'm skeptical the Fed bakes in much for tariffs just yet – they can express that frustration through the risk assessments. At any rate, under our scenario, it would make sense to simply leave the federal funds rate projection unchanged at 3.9 percent.

There are reasons to see consumer price indices moderate

In the short-run, over the next couple of months, there are a few reasons to expect consumer prices to moderate. Let's run down the list.

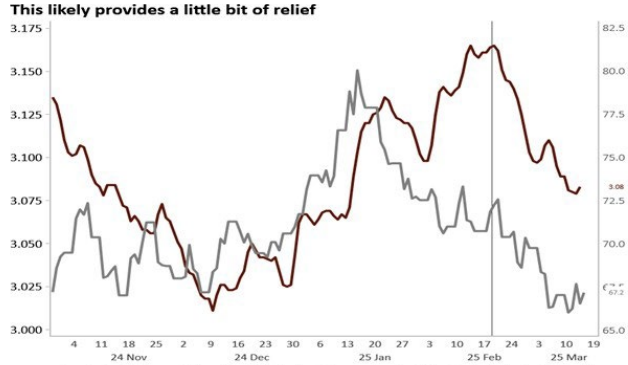
Egg prices will crater in March



—Consumer Price Index, Food at Home, Eggs, SA, Index (Right axis) [lead 1 month] —Eggs US (USD/Dozen) (Left axis)
Source: Renaissance Macro Research, Macrobond

- Egg prices have collapsed. In the last week, egg prices have declined nearly 40 percent. By itself, this would cut monthly headline CPI inflation by 0.1ppt.

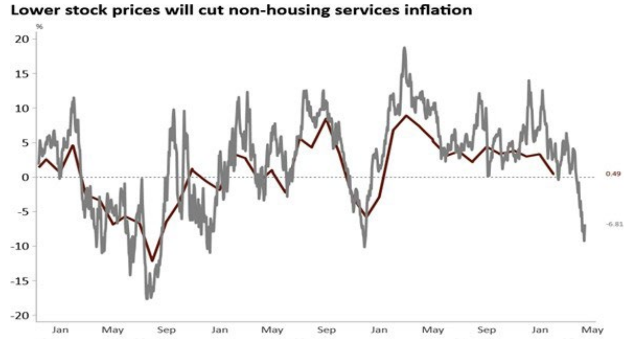
This likely provides a little bit of relief



—Generic 1st 'CL' Future (Right axis) —Daily National Average Gasoline Prices Regular Unleaded (Left axis)
Source: Renaissance Macro Research, Macrobond

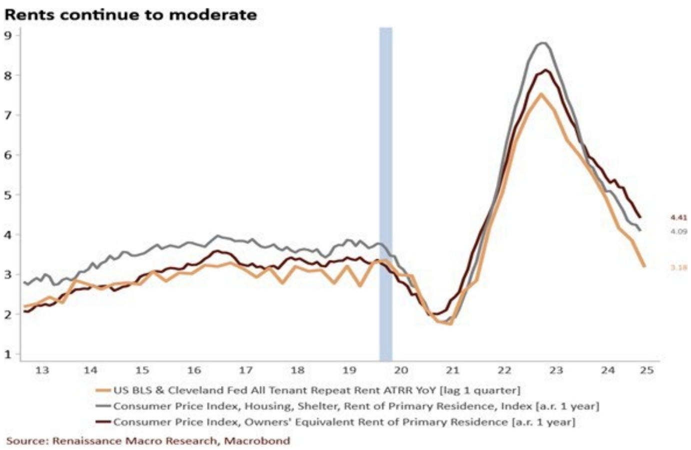
- Gas prices continue to moderate. Retail pump prices are down roughly 40 cents per gallon compared to last year and off about ten cents since mid-February

Lower stock prices will cut non-housing services inflation

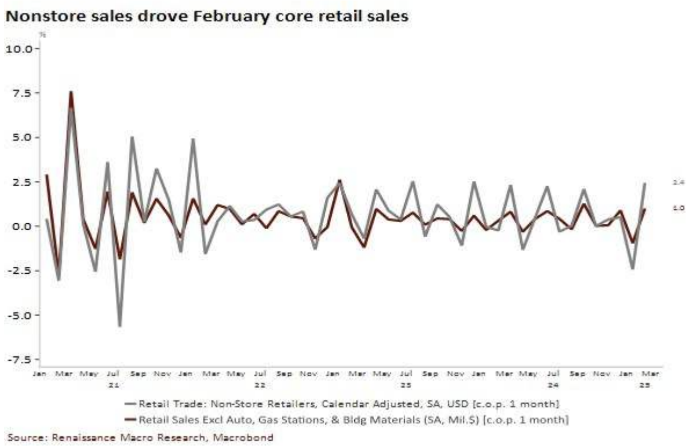


—S&P 500 INDEX [c.o.p. 13 weeks, lag 1 month]
—PCEPI, Portfolio Management & Investment Advice, SA, Index [c.o.p. 3 months]
Source: Renaissance Macro Research, Macrobond

- Lower stock prices will be a catalyst to declines in portfolio management PCEPI. Over the last three months, the S&P500 has dropped about 7 percent. Doing the math, we estimate a 0.1ppt cut to core PCE.

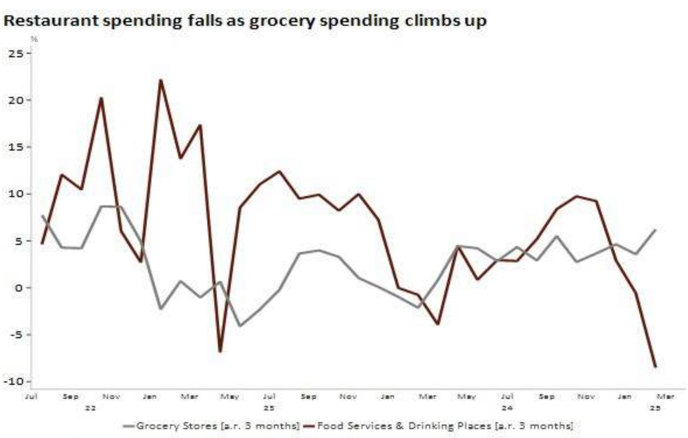


- Housing rental inflation will continue to moderate. The BLS All Tenant Repeat Rent Index stands at 3.18% year-over-year. This measure is not revised much and tends to have a short-lead on OER and primary rents



Data review: Consumers cut back on discretionary

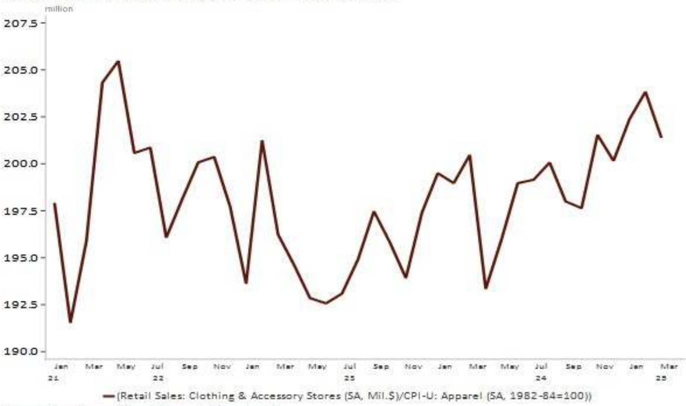
In February, retail sales missed estimates, climbing 0.2% following a 1.2% decline in January, revised down 0.3ppt. The consensus miss from month-to-month was largely about online retail. In January, e-commerce sales declined 2.4% and in February, online sales rose 2.4%. As a result, core retail sales jumped 1.0% after falling 1.0% the month prior. Ex-online, core retail sales & food service has declined for two consecutive months! All told, we're tracking just 1.1% annualized growth in PCE in Q1.



Consumers are cutting back on their discretionary purchases.

Over the last three months, restaurant sales have collapsed 8.5% at an annual rate, the weakest pace since early 2022. During this three-month period, sales at grocery stores have advanced 6.2% at an annual rate, the fastest three-month clip since November 2022. When households spend more dining out relative to dining in, it is a sign of optimism; when the opposite is true, I'd be more concerned.

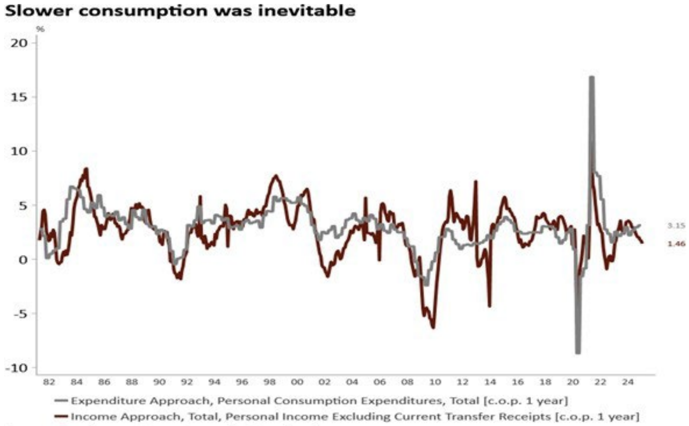
Declining real apparel purchases as prices rise



Source: Renaissance Macro Research, Macrobond

Clothing and accessory store sales fell 0.6% following a 0.7% drop in January. Importantly, this comes as apparel CPI rose in February. Thus, consumers are cutting back on their real purchases of clothes. That consumers are this price sensitive should make apparel retailers a bit more circumspect about passing on higher costs to consumers.

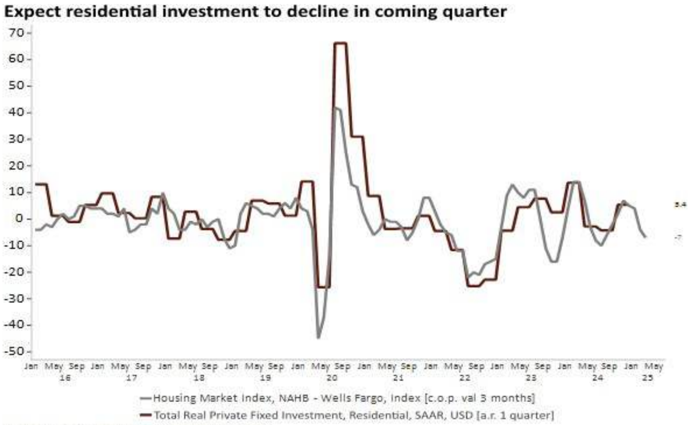
Slower consumption was inevitable



Source: Renaissance Macro Research, Macrobond

Stepping back, the bigger story is that real incomes have slowed, running about half the pace of consumers' spending over the last year. This implies that even if the saving rate stabilizes, we should expect consumption to slowdown. Given the drop in equity prices and cooling off in housing, household net worth is weakening – there is every reason for households to want to save more in this environment

Expect residential investment to decline in coming quarter

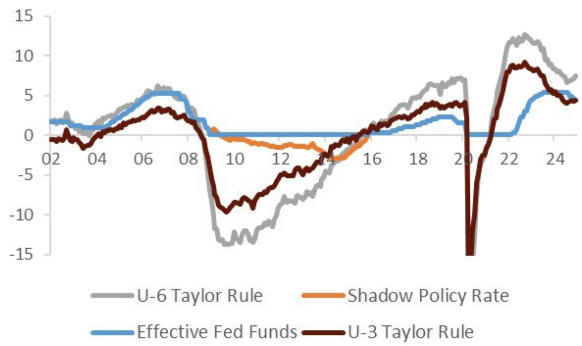


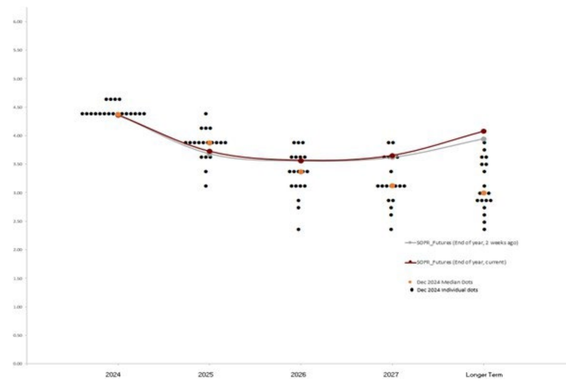
Source: Renaissance Macro Research, Macrobond

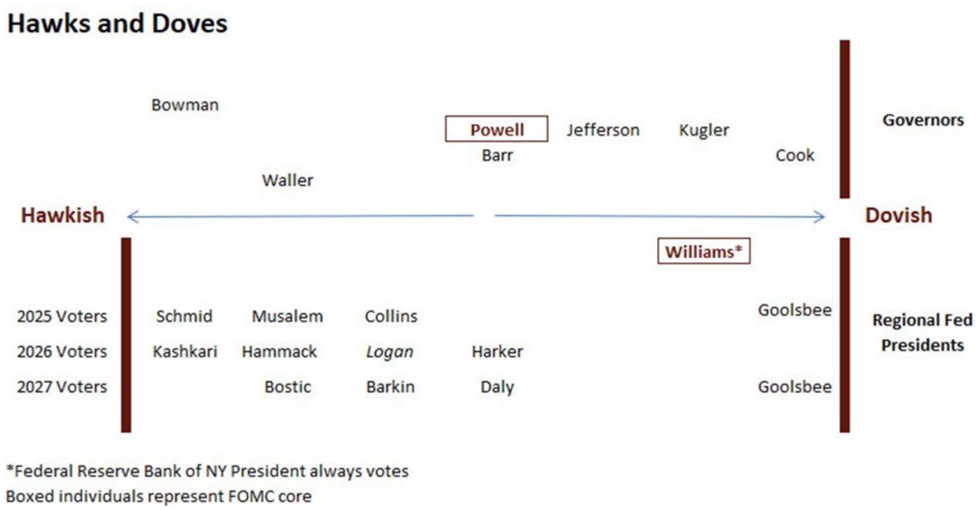
Housing to cut GDP in H1

The NAHB Housing Market Index tumbled 3pts to 39 in March, the lowest level since August and the second consecutive monthly decline. Present sales slid to 43, the lowest since December 2023. Buyer traffic dipped as well though future sales expectations remained stable at 47. The drop in the NAHB data suggest a decline in private residential fixed investment in the coming quarter. Housing market conditions will remain weak until we see lower interest rates. Mortgage rates are stuck between 6.5 to 7.0 percent at a time when incomes are slowing. The math remains challenging for prospective buyers.

Monetary metrics

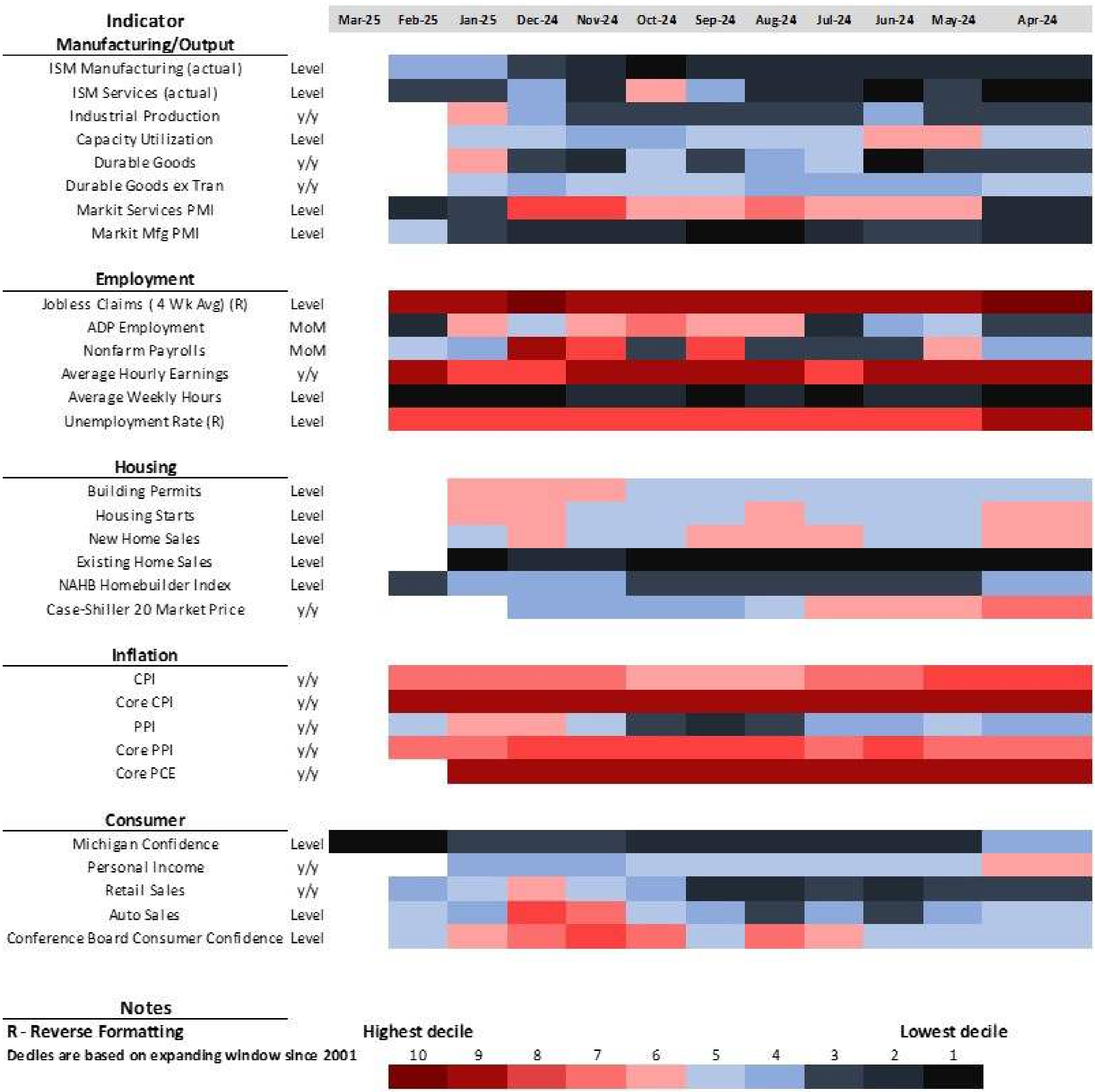




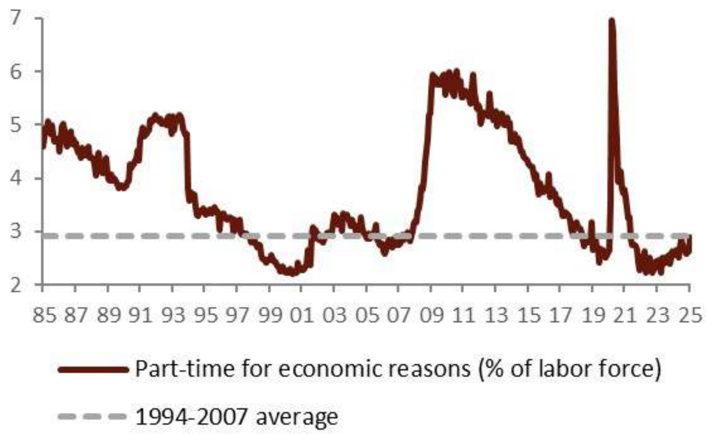


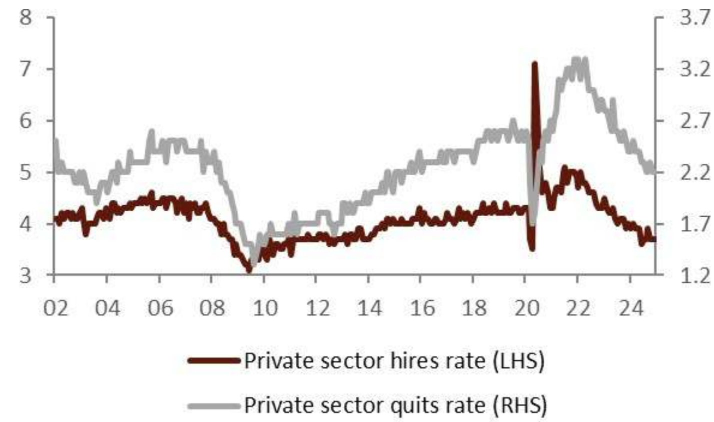
FOMC Forecasts	Median					Central Tendency				
	2024	2025	2026	2027	Longer run	2024	2025	2026	2027	Longer run
Change in real GDP	2.5	2.1	2.0	1.9	1.8	2.4–2.5	1.8–2.2	1.9–2.1	1.8–2.0	1.7–2.0
September projection	2.0	2.0	2.0	2.0	1.8	1.9–2.1	1.8–2.2	1.9–2.3	1.8–2.1	1.7–2.0
Unemployment rate	4.2	4.3	4.3	4.3	4.2	4.2	4.2–4.5	4.1–4.4	4.0–4.4	3.9–4.3
September projection	4.4	4.4	4.3	4.2	4.2	4.3–4.4	4.2–4.5	4.0–4.4	4.0–4.4	3.9–4.3
PCE inflation	2.4	2.5	2.1	2.0	2.0	2.4–2.5	2.3–2.6	2.0–2.2	2.0	2.0
September projection	2.3	2.1	2.0	2.0	2.0	2.2–2.4	2.1–2.2	2.0	2.0	2.0
Core PCE inflation	2.8	2.5	2.2	2.0		2.8–2.9	2.5–2.7	2.0–2.3	2.0	
September projection	2.6	2.2	2.0	2.0		2.6–2.7	2.1–2.3	2.0	2.0	
Projected policy path										
Fed funds rate	4.4	3.9	3.4	3.1	3.0	4.4–4.6	3.6–4.1	3.1–3.6	2.9–3.6	2.8–3.6
September projection	4.4	3.4	2.9	2.9	2.9	4.4–4.6	3.1–3.6	2.6–3.6	2.6–3.6	2.5–3.5

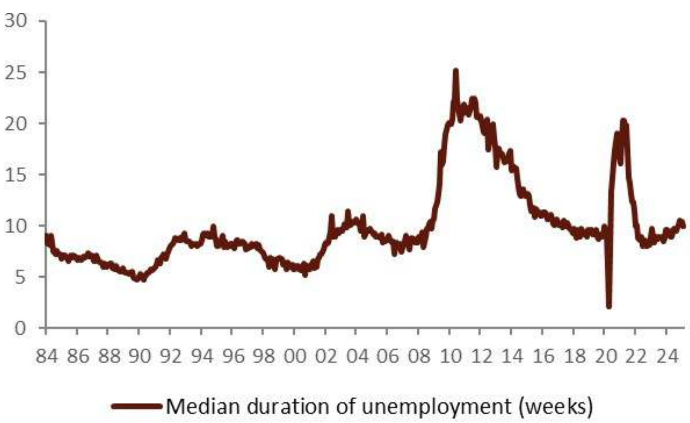
High frequency data heat-map

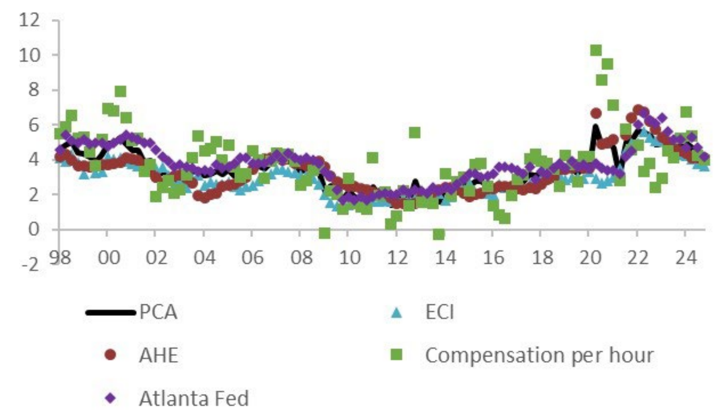


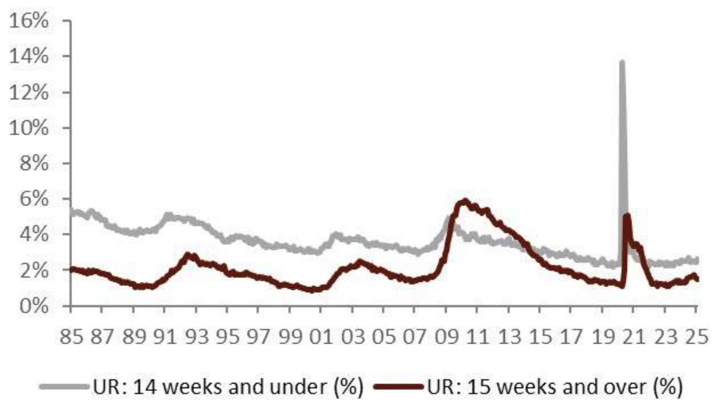
Labor market indicators

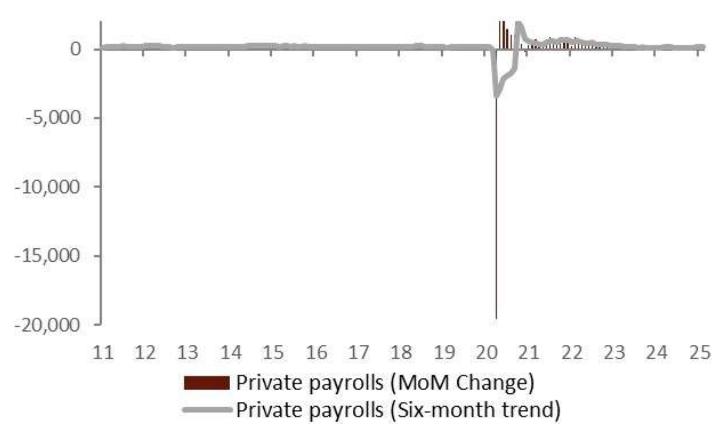












Inflation indicators