

## Economic Outlook:

New Year, Old Problems:  
Inflation, Policy Risks Remain

*February 2022*



# STIFEL

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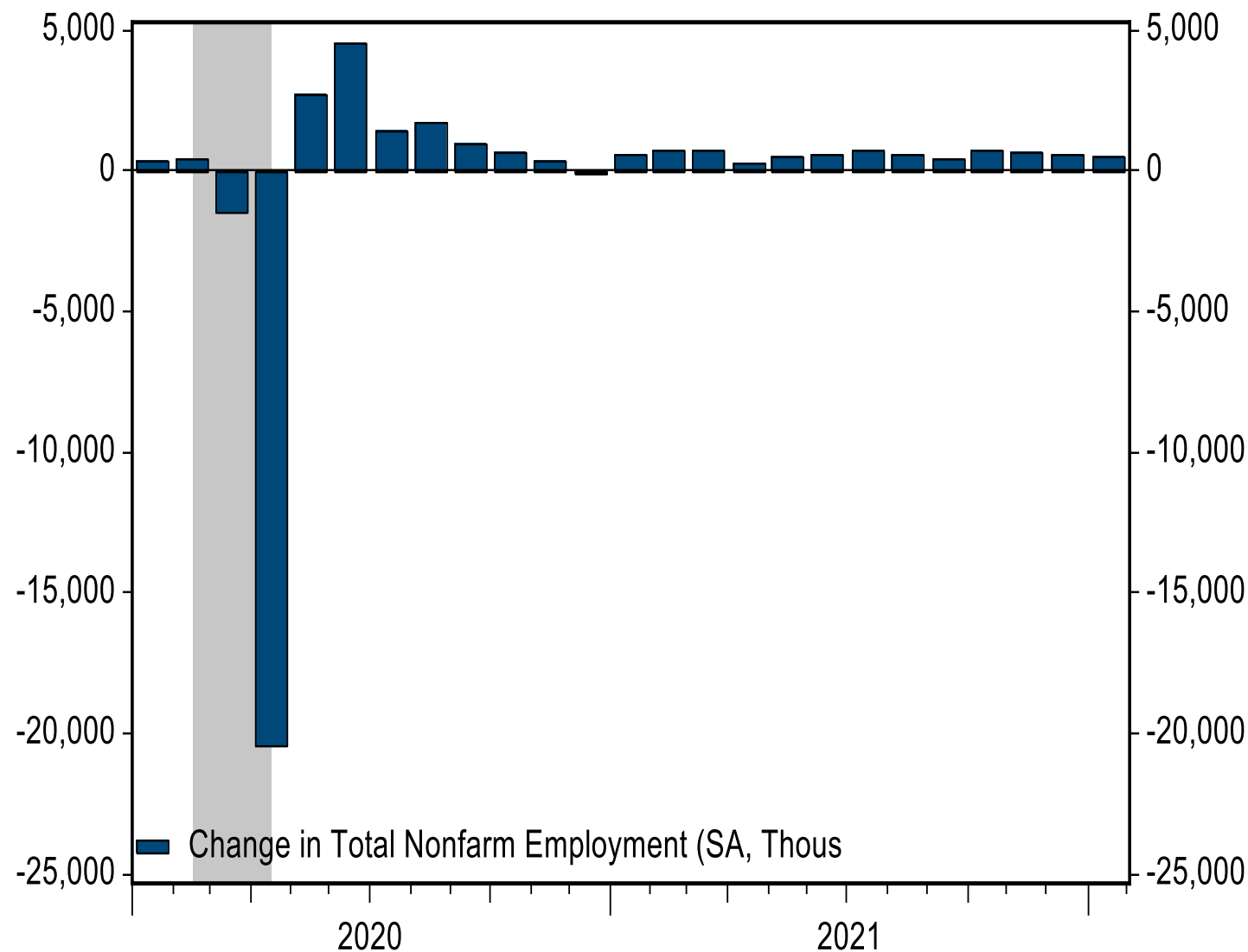
*For Institutional Use Only*

## 467k Payrolls Added in January

Nonfarm payrolls fell 1.5M in March and 20.5M in April of 2020, the largest monthly decline on record

Nonfarm payrolls rose **467k** in January 2022, the weakest pace of job creation since September 2021

For the full year, payrolls rose 6.7M, a record high, but following a 9.3M drop in 2020, the largest decline on record, and more than the combined decline in 2008 and 2009



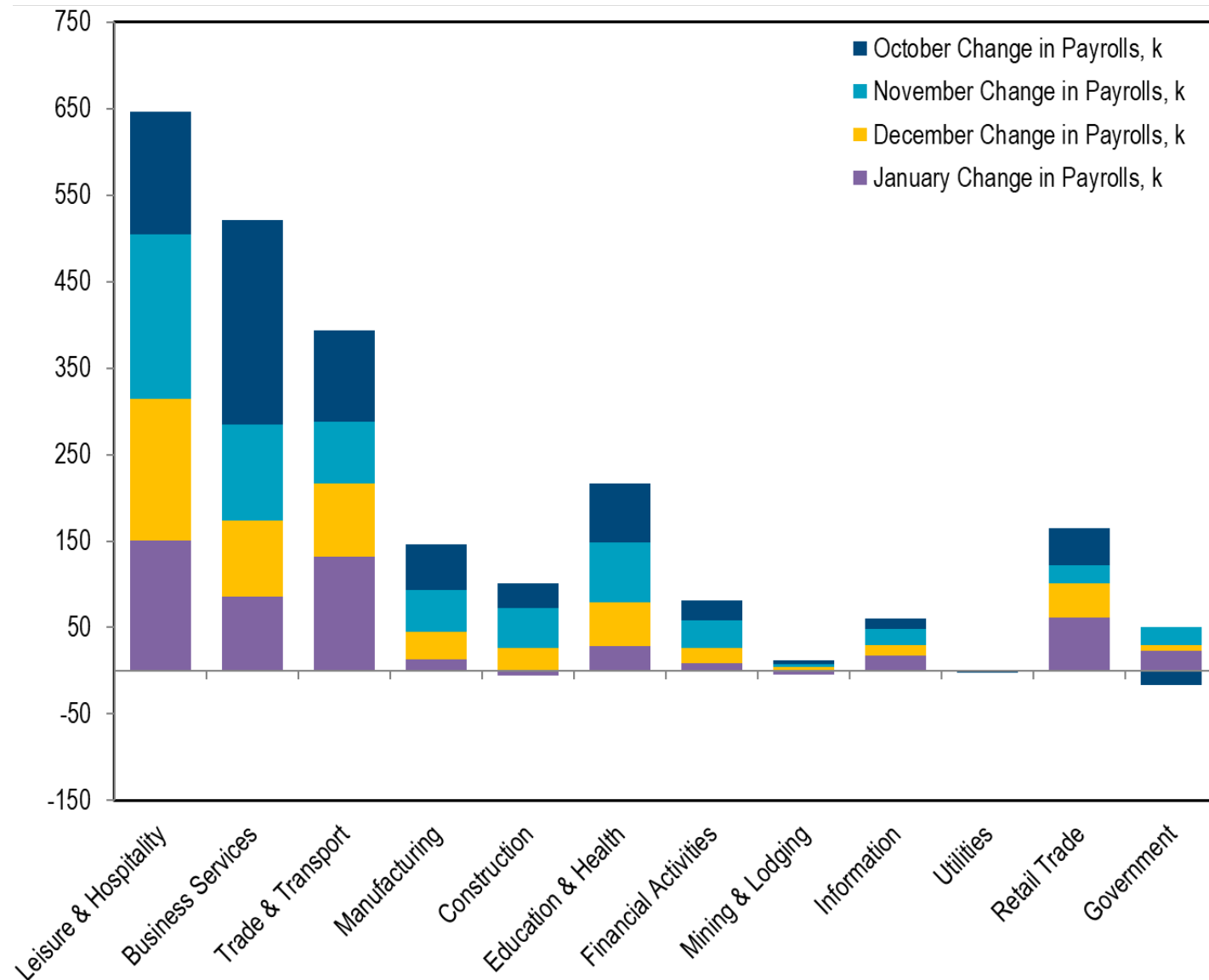
Source: Bureau of Labor Statistics/Haver Analytic

## Payrolls by Category

Leisure & hospitality led the gain in payrolls in January with **151k**

Business services payrolls rose **86k**, trade and transport rose **132k**, and retail trade rose **61k**

On the weaker side, construction payrolls fell **5k** in January



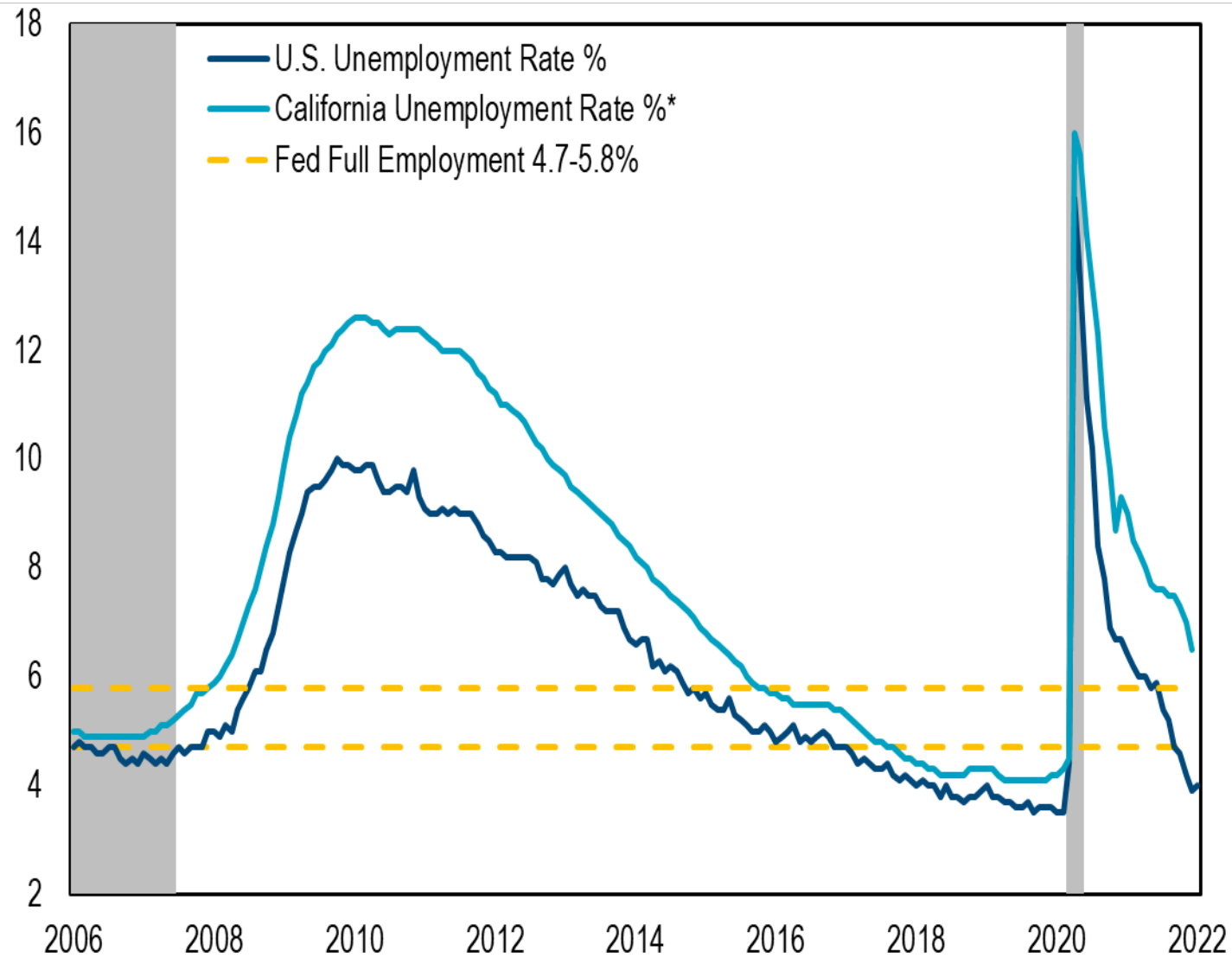
Source: Haver Analytics/Bloomberg

## 4.0% U.S. Unemployment Rate; 6.5% California Unemployment Rate

The U.S. unemployment rate ticked up from 3.9% to **4.0%** in January, a two-month high

The unemployment rate in California dropped from 7.0% to **6.5%** in December 2021, the lowest since March 2020

While still elevated from the 3.5% U.S. jobless rate at the start of 2020, last month's rate stands in stark contrast to a near 15% peak in April 2020



Source: Bureau of Economic Analysis/ Bureau of Labor Statistics

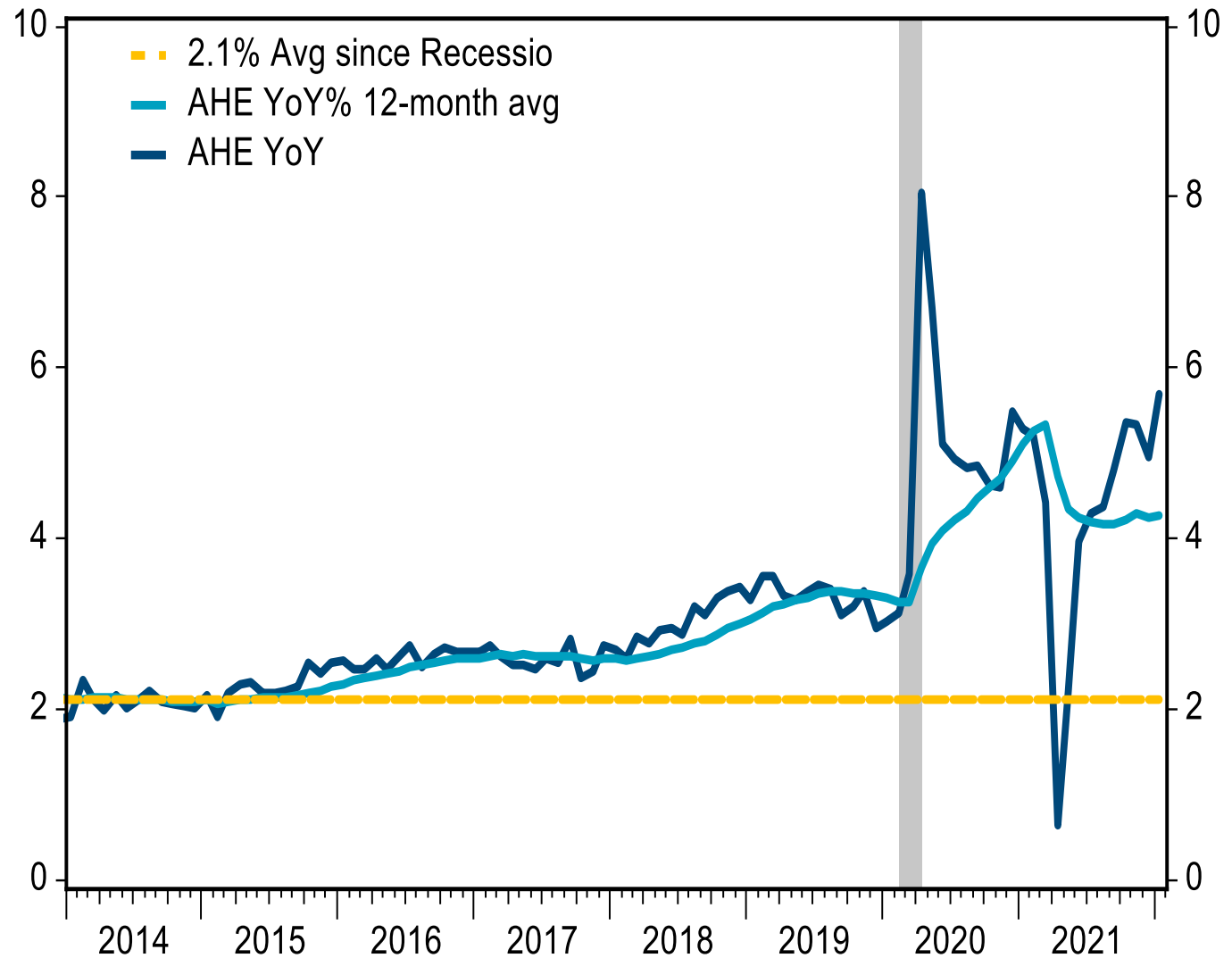
\*Data as of Dec. 2021

## Average Hourly Earnings Accelerate

Average hourly earnings rose **0.7%** in January, following a 0.5% increase in December

Year-over-year, wages rose **5.7%** in January, still below a recent peak of 8.2% in April 2020

Average earnings increased early on during the pandemic as lower-wage workers dropped out of the workforce



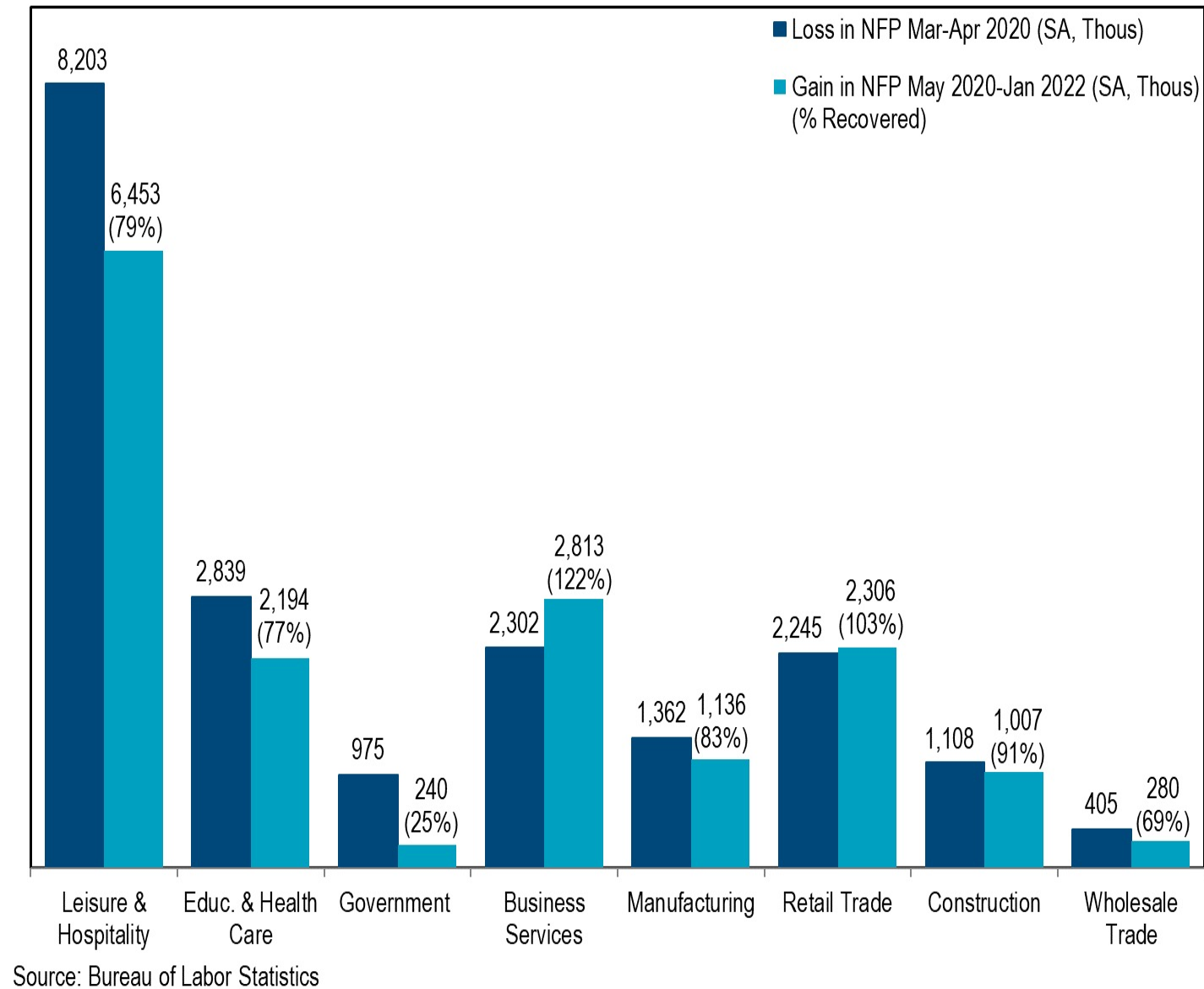
Source: Bureau of Labor Statistics/Haver Analytic

\*Does not include government assistance

## Hardest Hit Industries Recapture Jobs

The leisure and hospitality industry lost over **8M** jobs during the pandemic but has since recaptured more than **6M** or **79%**

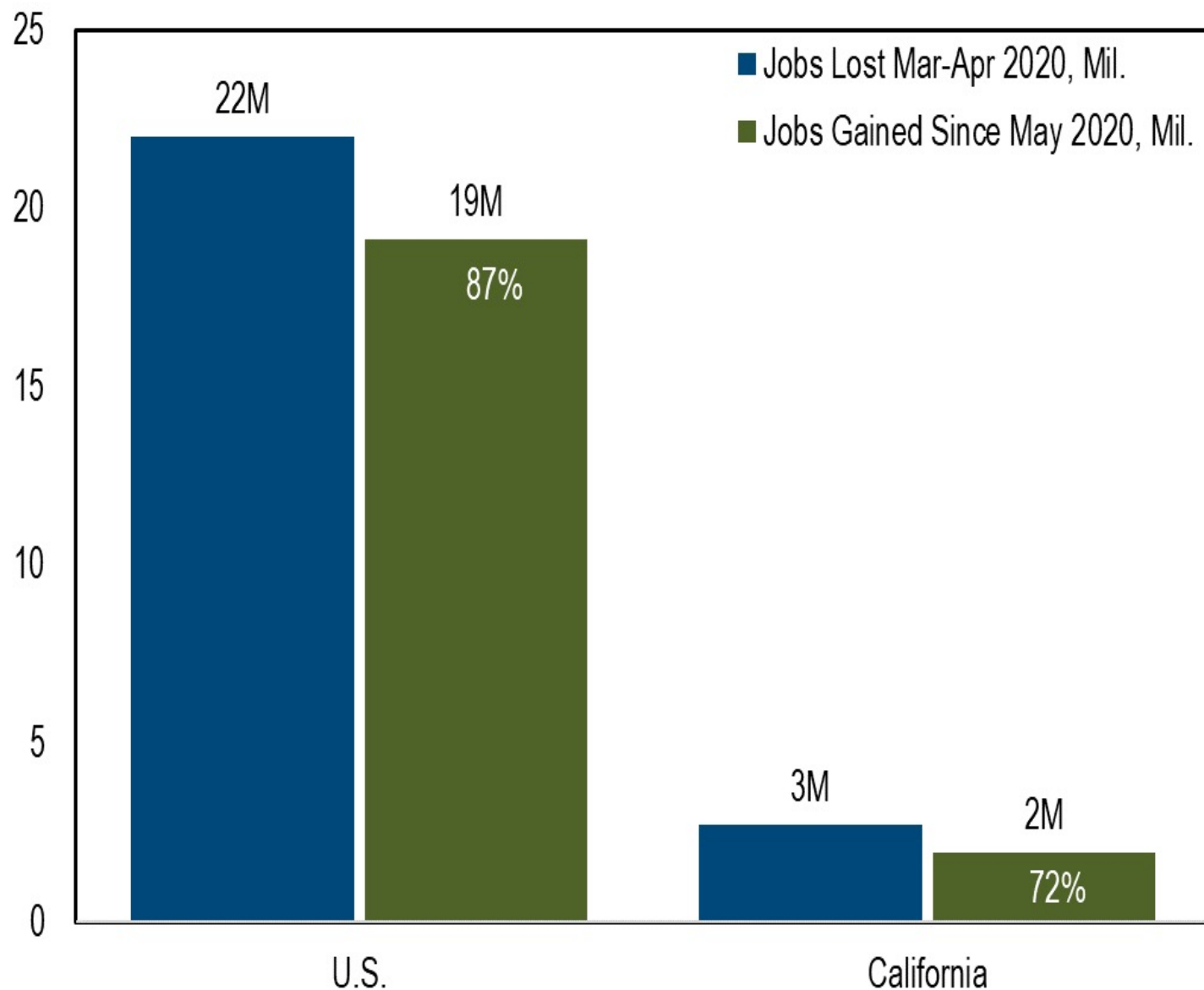
The hardest hit sectors have recaptured roughly 80% of lost jobs



## U.S. and California Still Need to Recapture Jobs

The U.S. lost over **22M** jobs at the onset of the pandemic, but since then about **19M** have come back

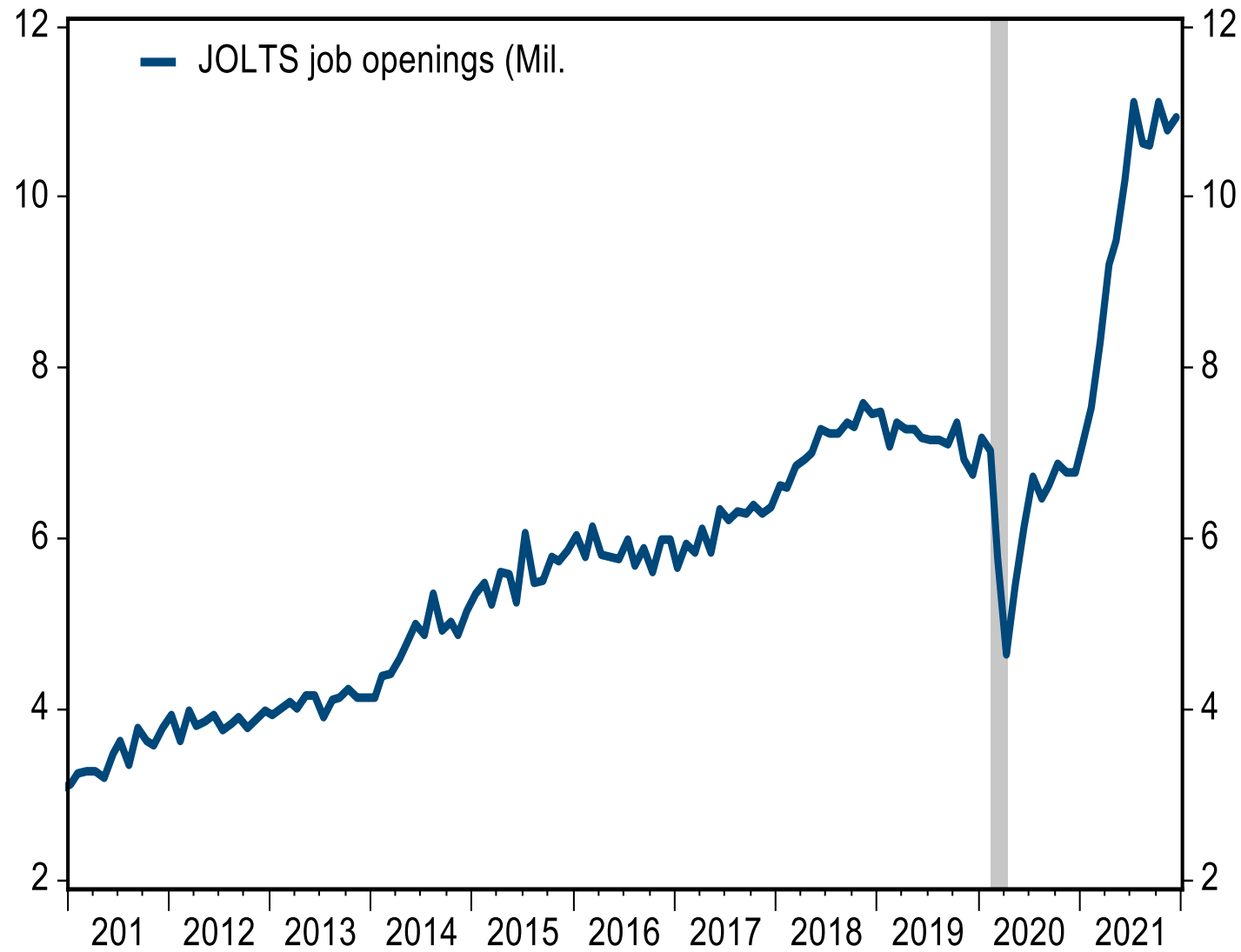
California lost around **3M** jobs at the onset of the pandemic, but 72%, or around **2M** have come back



Source: Bureau of Labor Statistics

## Labor Demand Outpaces Labor Supply

The number of job openings, according to JOLTS – the Job Openings and Labor Turnover Survey – rose from 10.8M to **10.9M** in December, a two-month high and the seventh straight month above 10M, suggesting producers remain desperate for workers to increase output and meet a still-heightened level of demand for goods and services



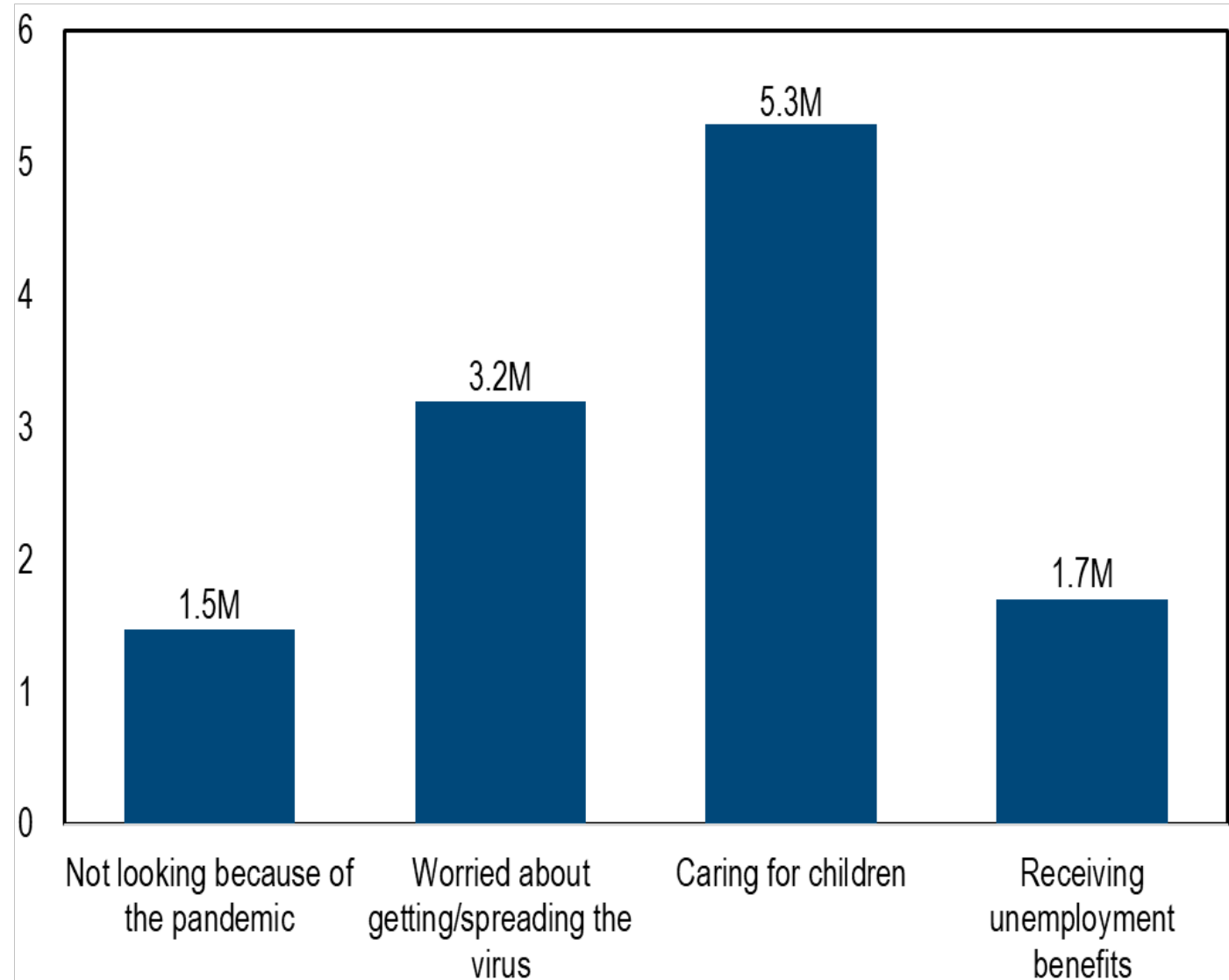
Source: Bureau of Labor Statistics/Haver Analytic



## Where Have All the Workers Gone?

According to the Bureau of Labor Statistics, as of January, **1.5M** Americans report they are prevented from looking for work due to the pandemic with over **3M** reporting they remained sidelined due to *“worries about getting or spreading the virus”*

The Census Bureau reports more than **5M** people are out of work because they were *“caring for children not in school or daycare”*

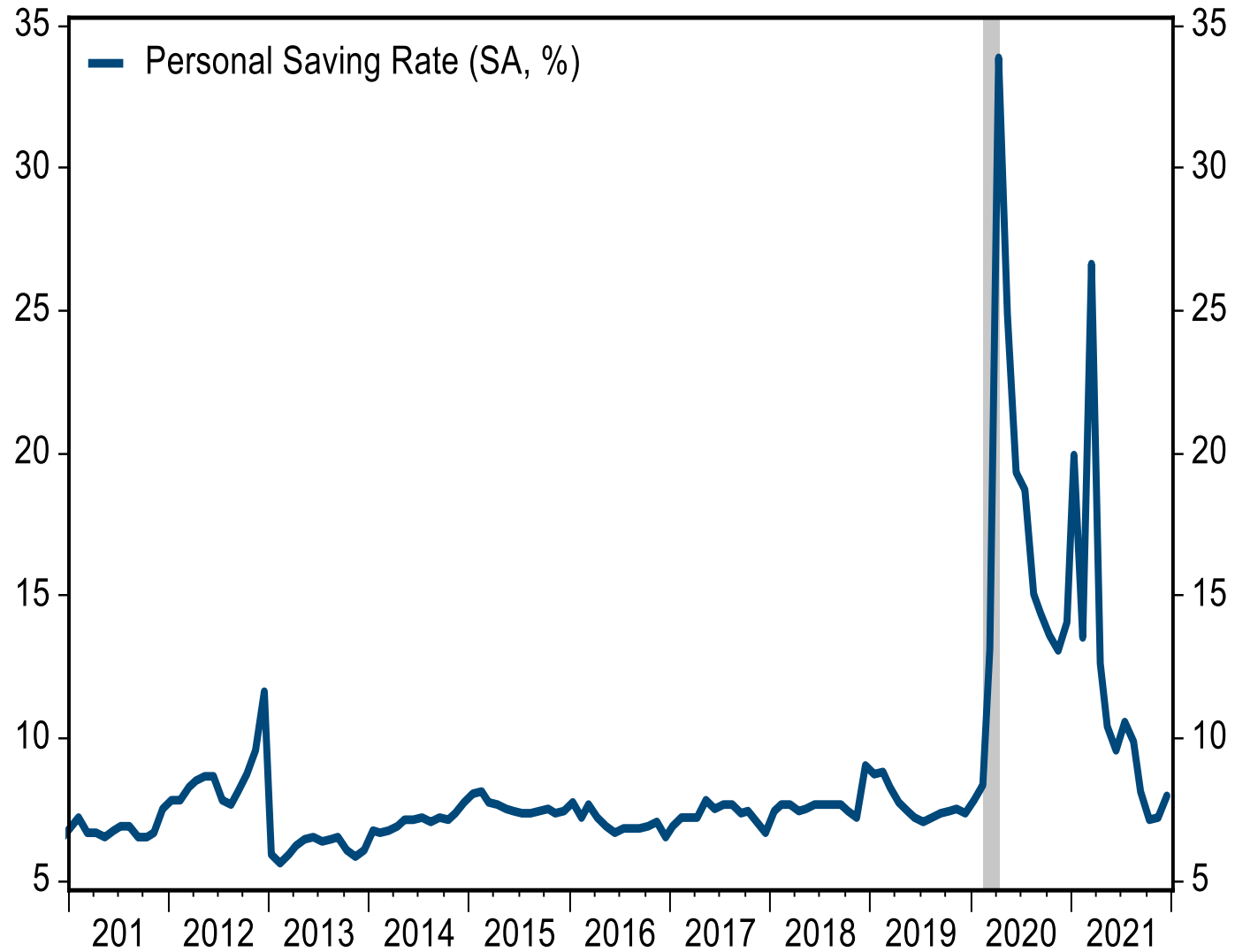


Source: Bureau of Labor Statistics

## Trillions in Accumulated Savings

The U.S. consumer remains solid with **\$1.4T** in savings and a savings rate of **7.9%** as of December

Additional savings, higher wages and additional federal spending will help supplement the consumer and mitigate the fiscal cliff resulting from an end of pandemic stimulus



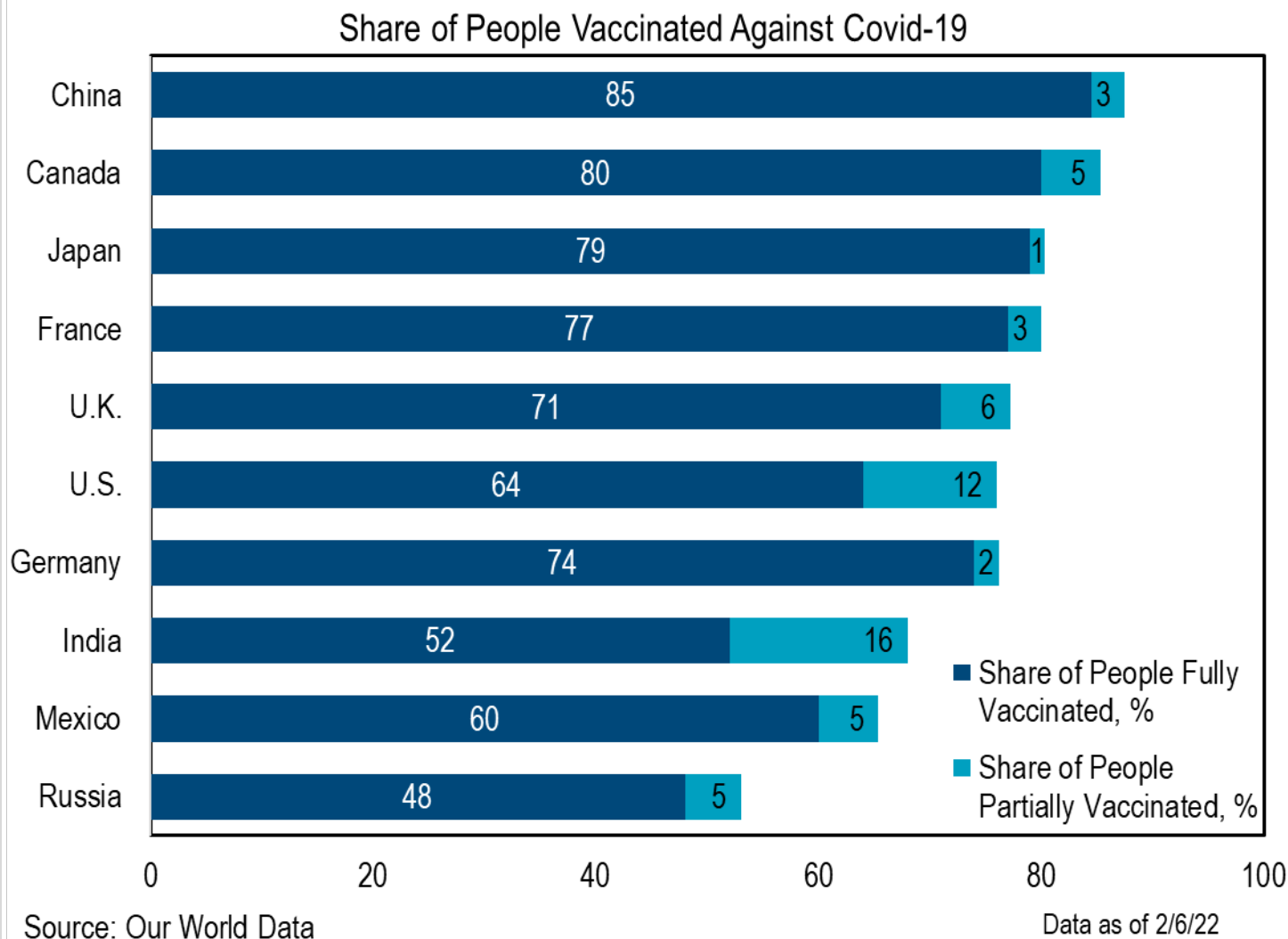
Source: Bureau of Economic Analysis/Haver Analytic

## Pace of Vaccinations Slows

The pace of vaccinations in the U.S. has slowed from 3M a day in the spring to around 425k a day

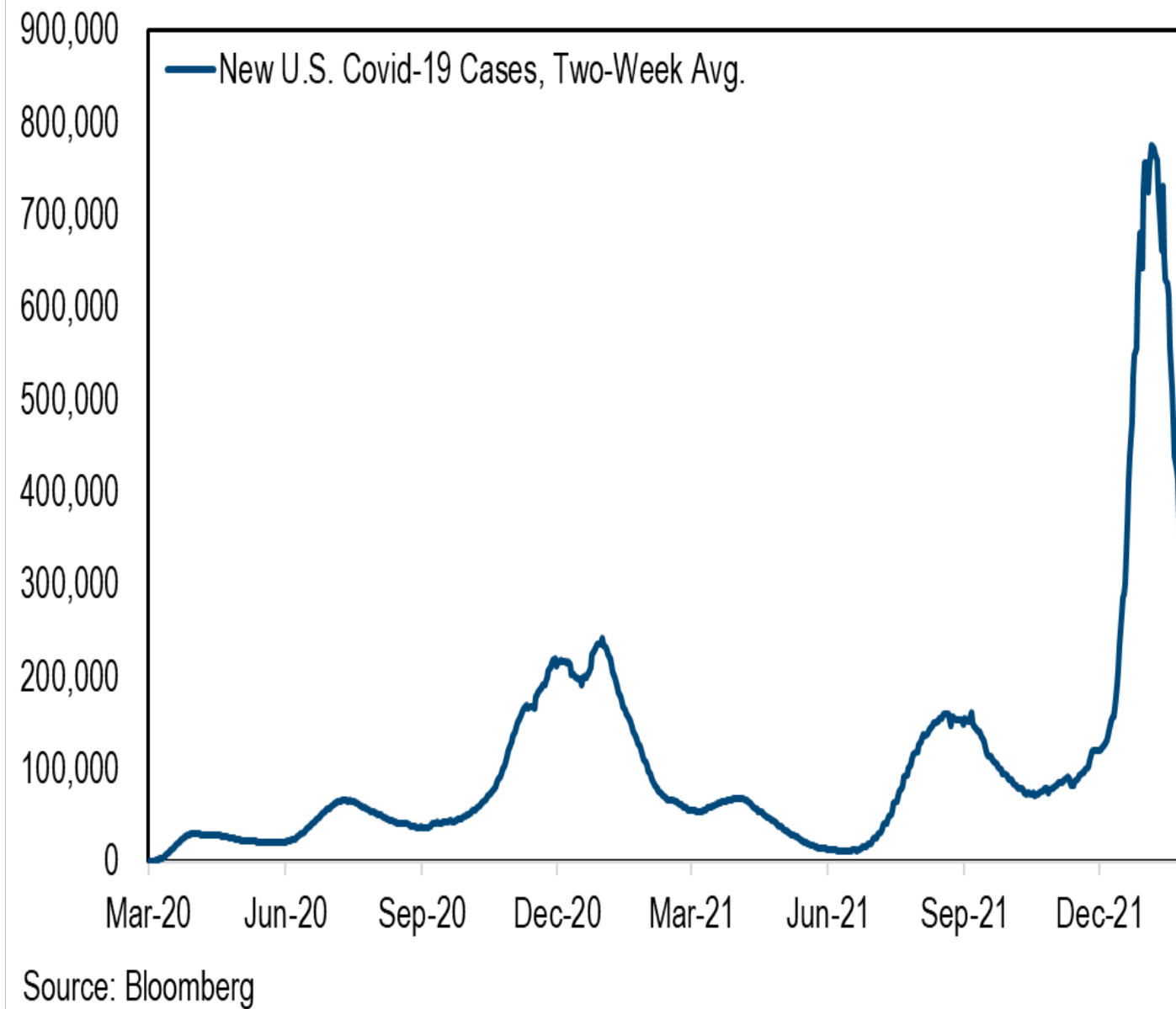
According to the CDC, **76%** of the American population has been partially vaccinated, **64%** fully vaccinated and **43%** saturated with additional booster shots

By contrast, Canada, France, and Germany are all up over 70% fully vaccinated, where as countries like India, Mexico, and Russia are down around 60%



## Covid-19 Case Numbers Trending Down

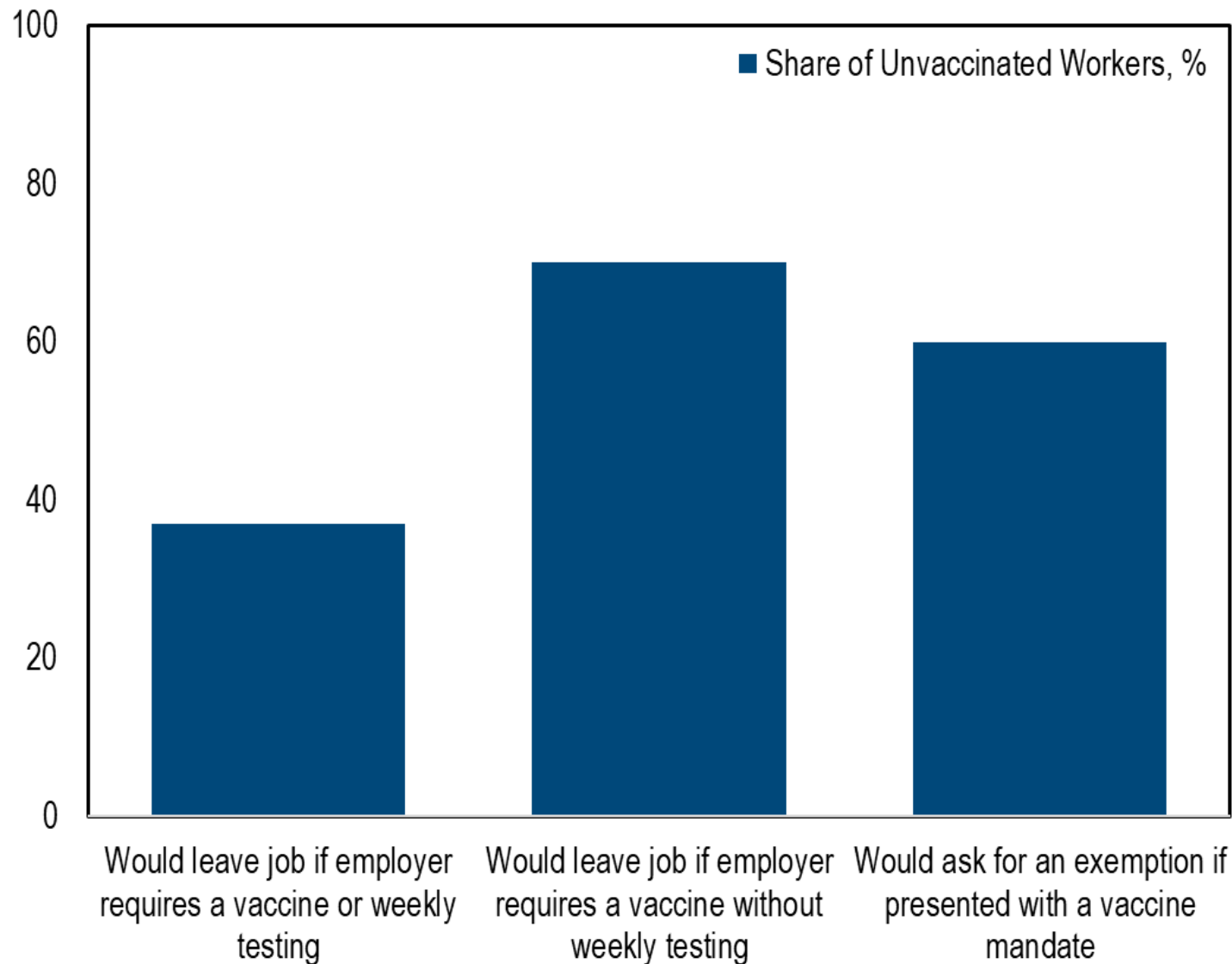
Covid-19 cases reached record highs driven by the highly contagious Omicron variant with the U.S. averaging over **200k** new cases a day



## Covid-19 Vaccine Mandate

More than a third (37%) of unvaccinated workers (roughly **13M** of adults overall) say they would leave their job if their employer required them to get a vaccine or get tested weekly, a share that rises to seven in ten unvaccinated workers (roughly **23M** of all adults) if weekly testing is not an option

Six in ten workers (roughly **20M** of all adults) say they would ask for an exemption if presented with such a mandate



Source: Kaiser Family Foundation

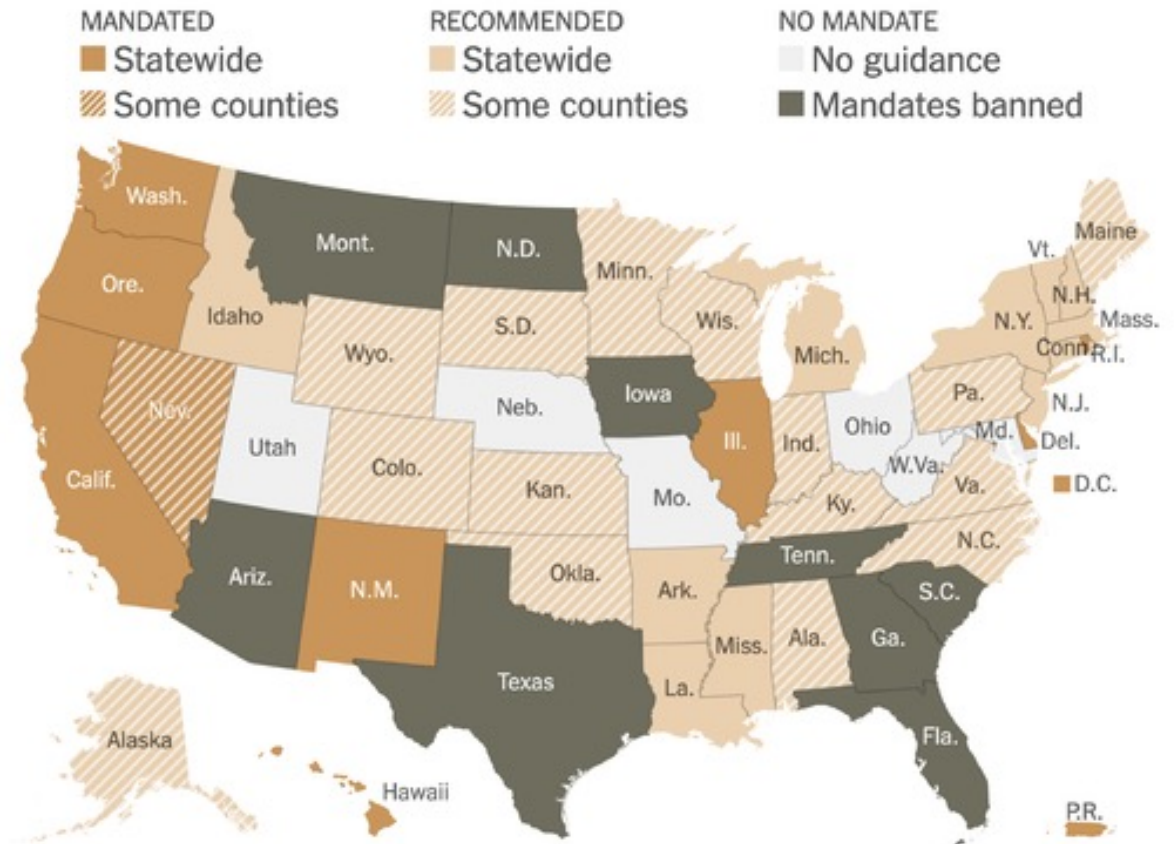
## COVID-19 Safety Protocols by State

As of February 10, **8** states and Washington, D.C. have mask requirements in place, but many of the mandates will be lifted in the upcoming days and weeks

Delaware & Rhode Island, for example, will end their indoor mask mandate on Feb. 11, but keep the mandate for schools until March

To date, **29** states that had orders broadly requiring residents to wear masks in public have lifted them

### Statewide Mask and Face Covering Mandates

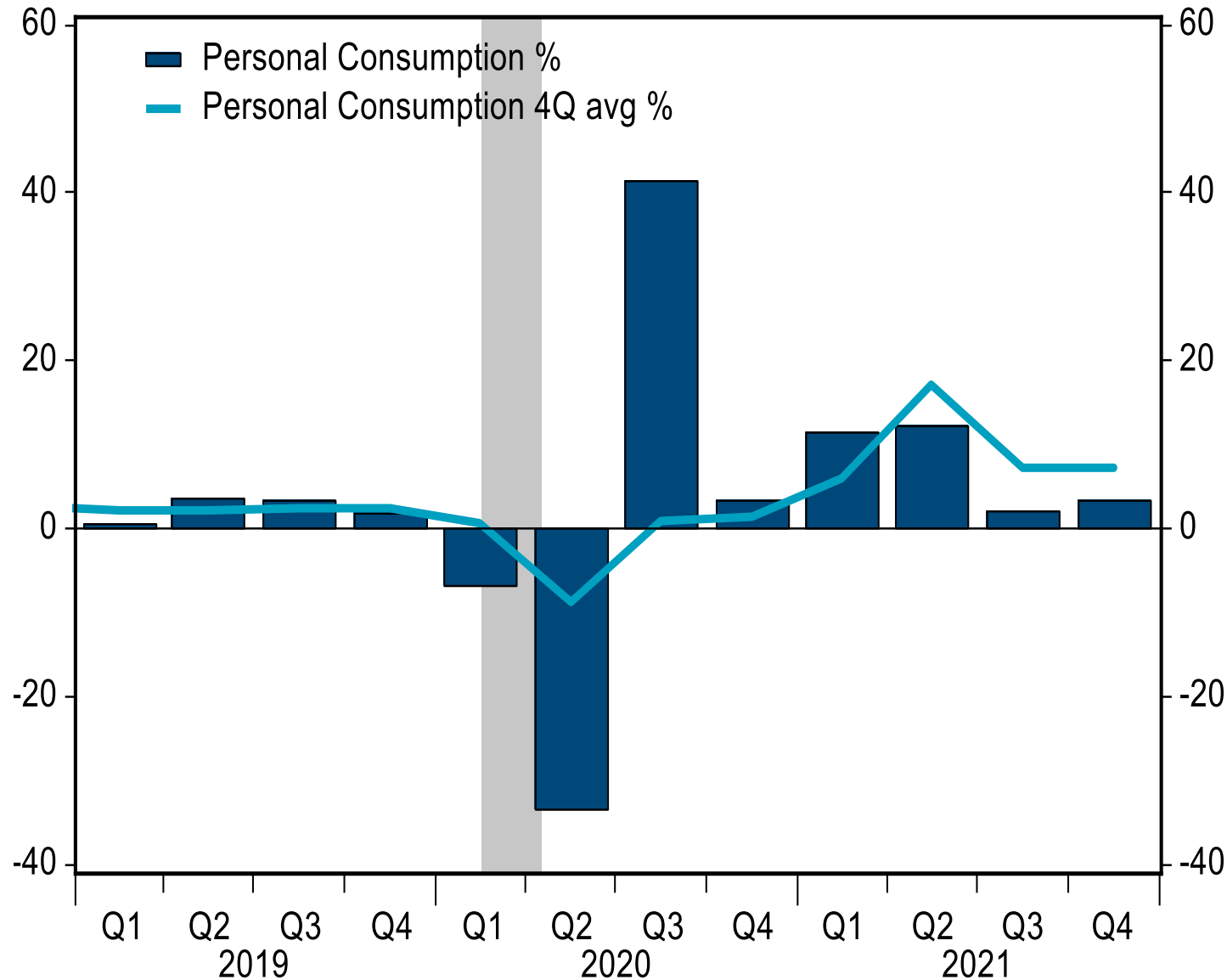


Source: New York Times, Data as of 2/10/2022

## Stimulus Support to Consumption Wanes

Personal consumption expenditures rose **3.3%** in Q4, up from the 2.0% pace the quarter prior, but down from the 12% pace in Q2

On a four-quarter average basis, consumption remained at 7.2%, down from the record 17.1% pace in Q2



Source: Bureau of Economic Analysis/Haver Analytic

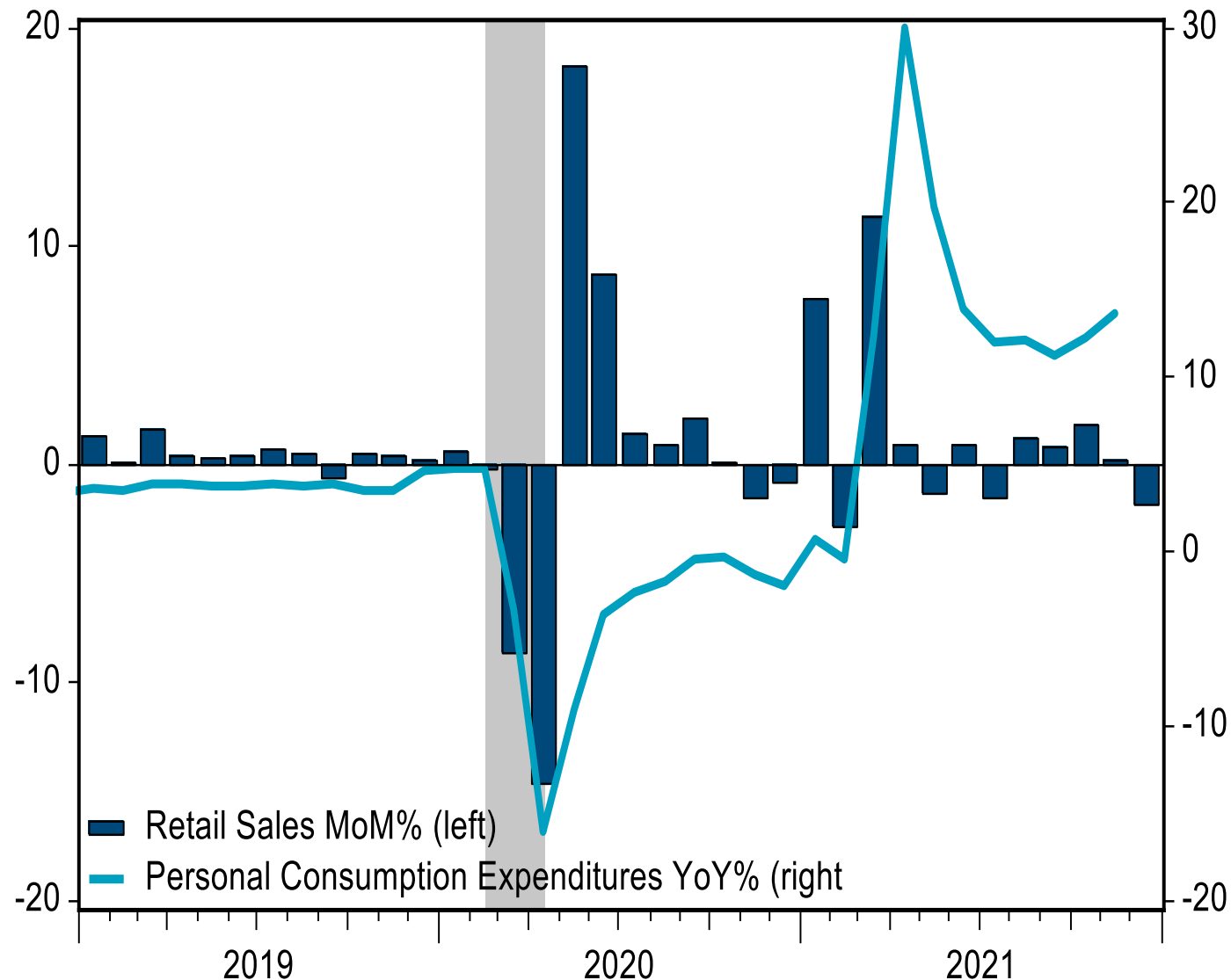
## Retail Sales Decline in December

Retail sales fell 8.2% in March and 14.7% in April 2020

Sales fell **1.9%** in December, following a 0.2% increase in November, and further below the 18.3% peak in May 2020

Over the past six months, sales have averaged 0.1%

Year-over-year, retail sales rose **17%** in December, following an 18.2% gain in November



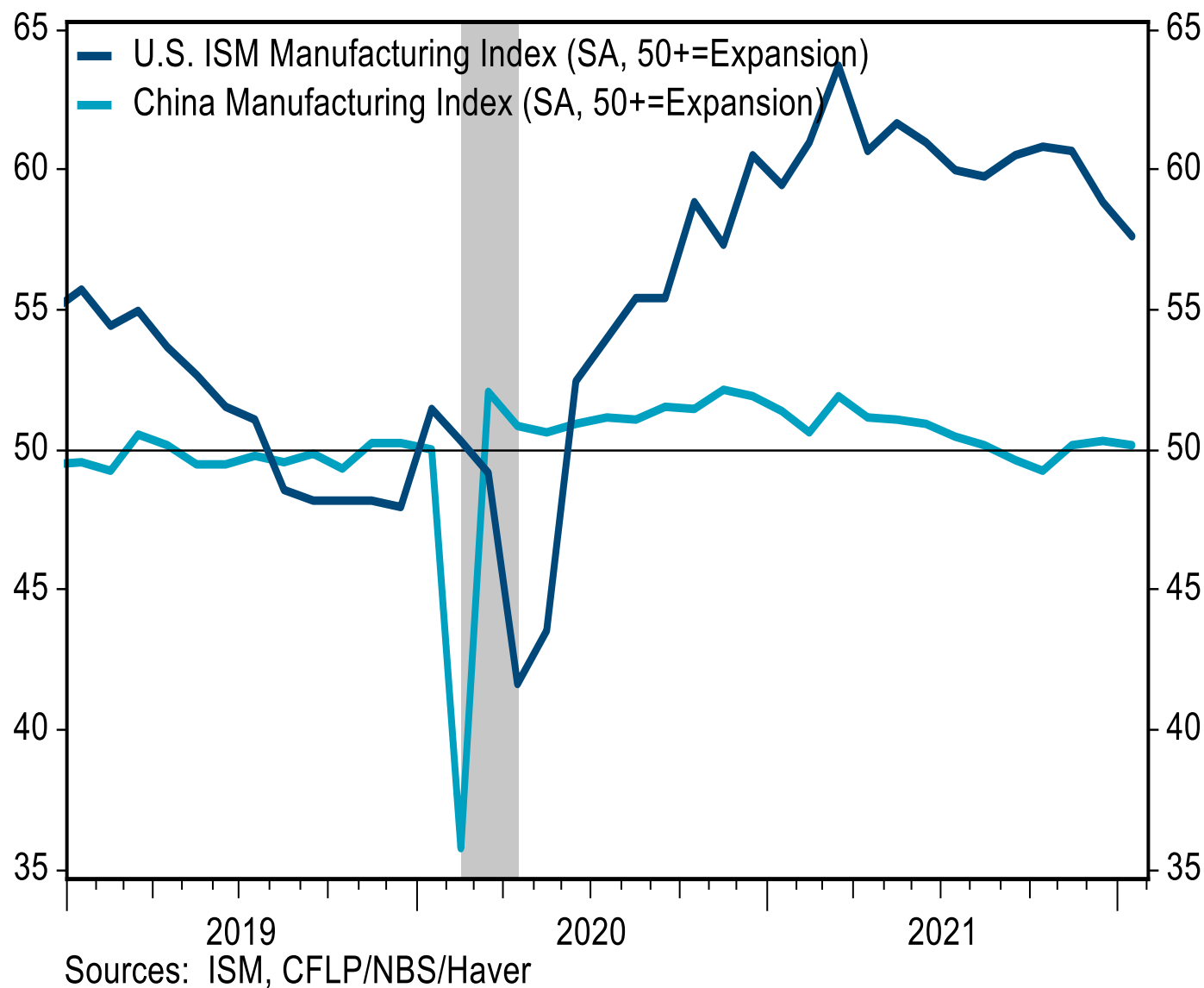
Sources: Census Bureau/Haver Analytics, Bureau of Economic Analysis



## Manufacturing Activity Solid

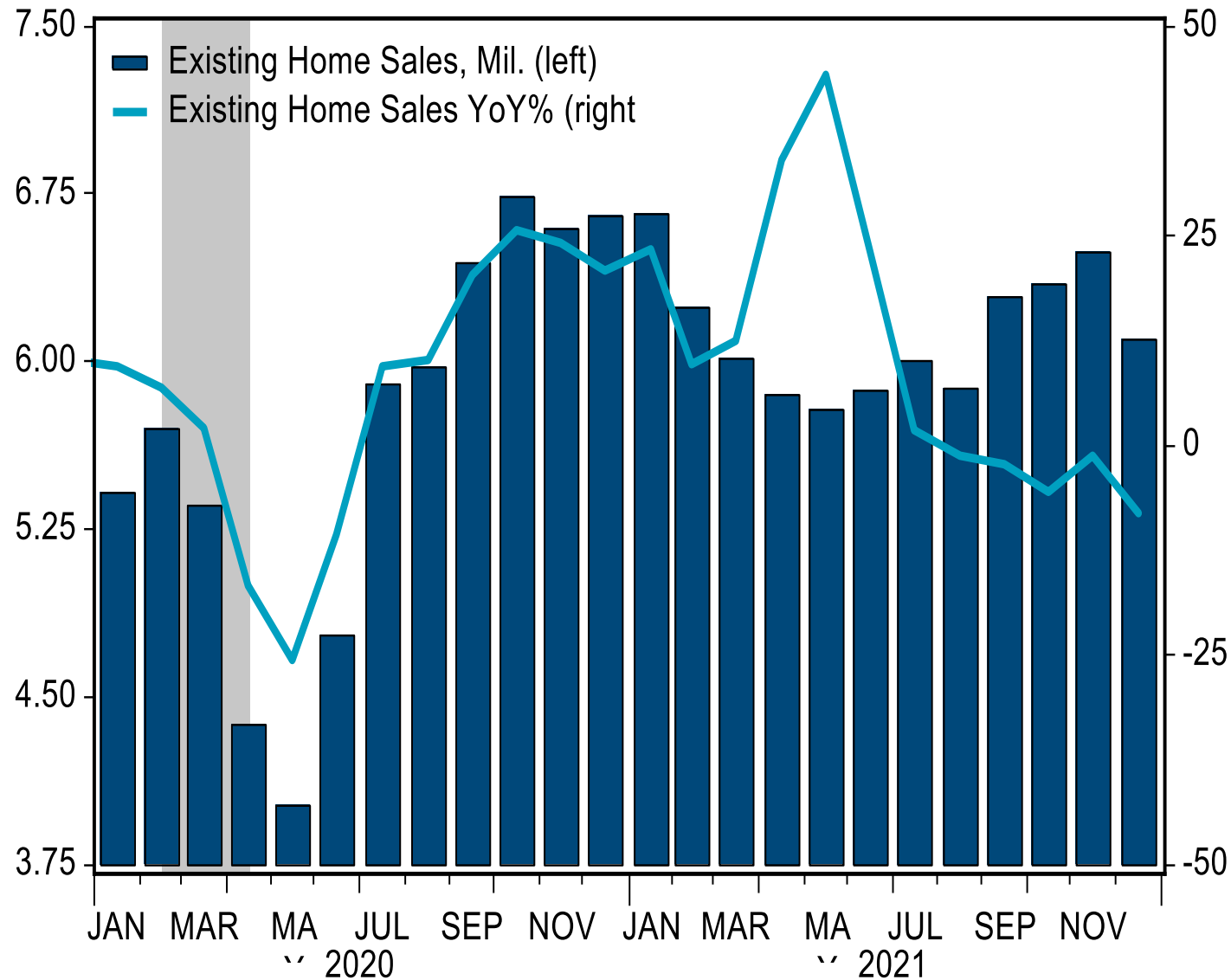
The ISM manufacturing Index dropped from 50.3 in February 2020 to a low of 41.7 in April 2020, but has since rebounded to **57.6** as of January, albeit the lowest reading since November 2020

The China Manufacturing PMI fell from 50.3 to **50.1** in January, down from a near-term peak of 52.0 in March 2020



## Elevated Demand for Housing

Existing home sales dropped 4.6% in December to a **6.18m** unit pace, however, up more than 50% since the May 2020 low

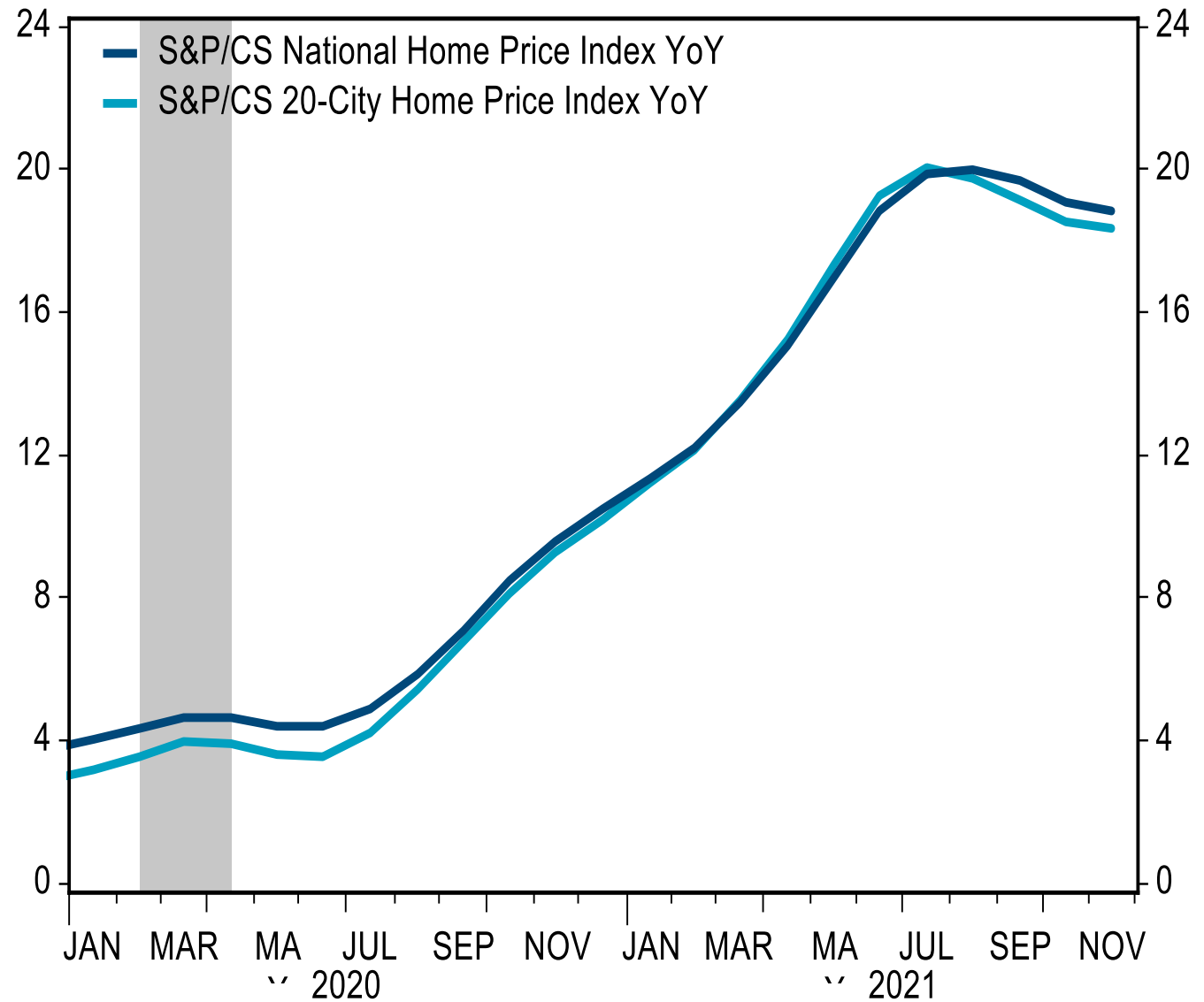


Source: National Association of Realtors/Haver Analytic

## U.S. Home Prices on the Rise

Year-over-year, the 20-city home price index rose **18.3%** in November, down from the record 20.0% increase reported in July

Nationally, home prices rose **18.8%** on an annual basis in November, down from a 20% increase in August, the largest gain in the history of the index dating back to 1987



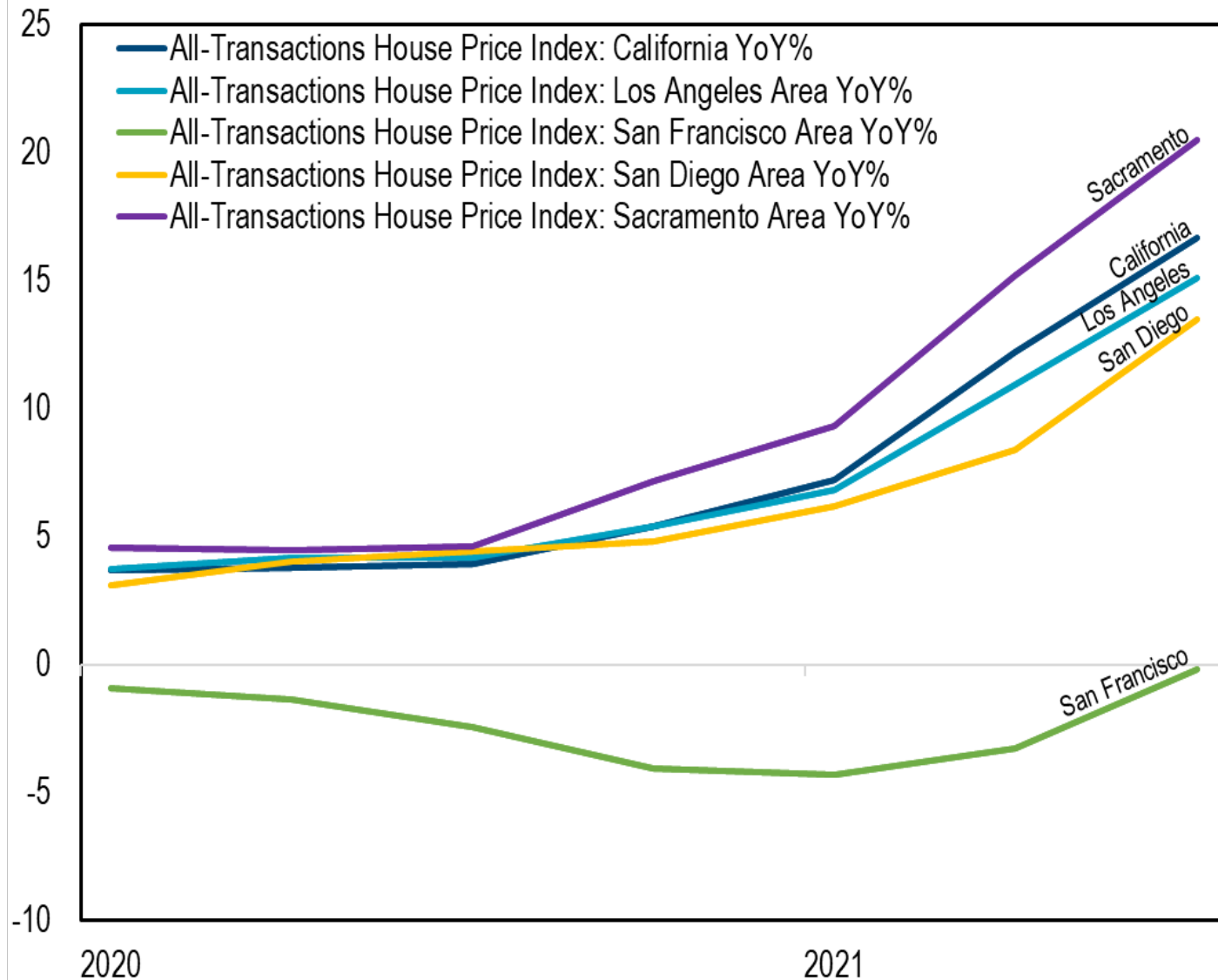
Source: Standard & Poor's/Haver Analytic

## California Home Prices on the Rise

House prices in California are up **16.7%** in Q3 2021, the highest since 2006

In the Los Angeles area, house prices are up **15.1%** as of Q3 2021, while house prices in the Sacramento are **20.5%** more expensive

On the other hand, house prices in the San Francisco area are up **2.1%** in Q3 2021 after more than two year of negative readings

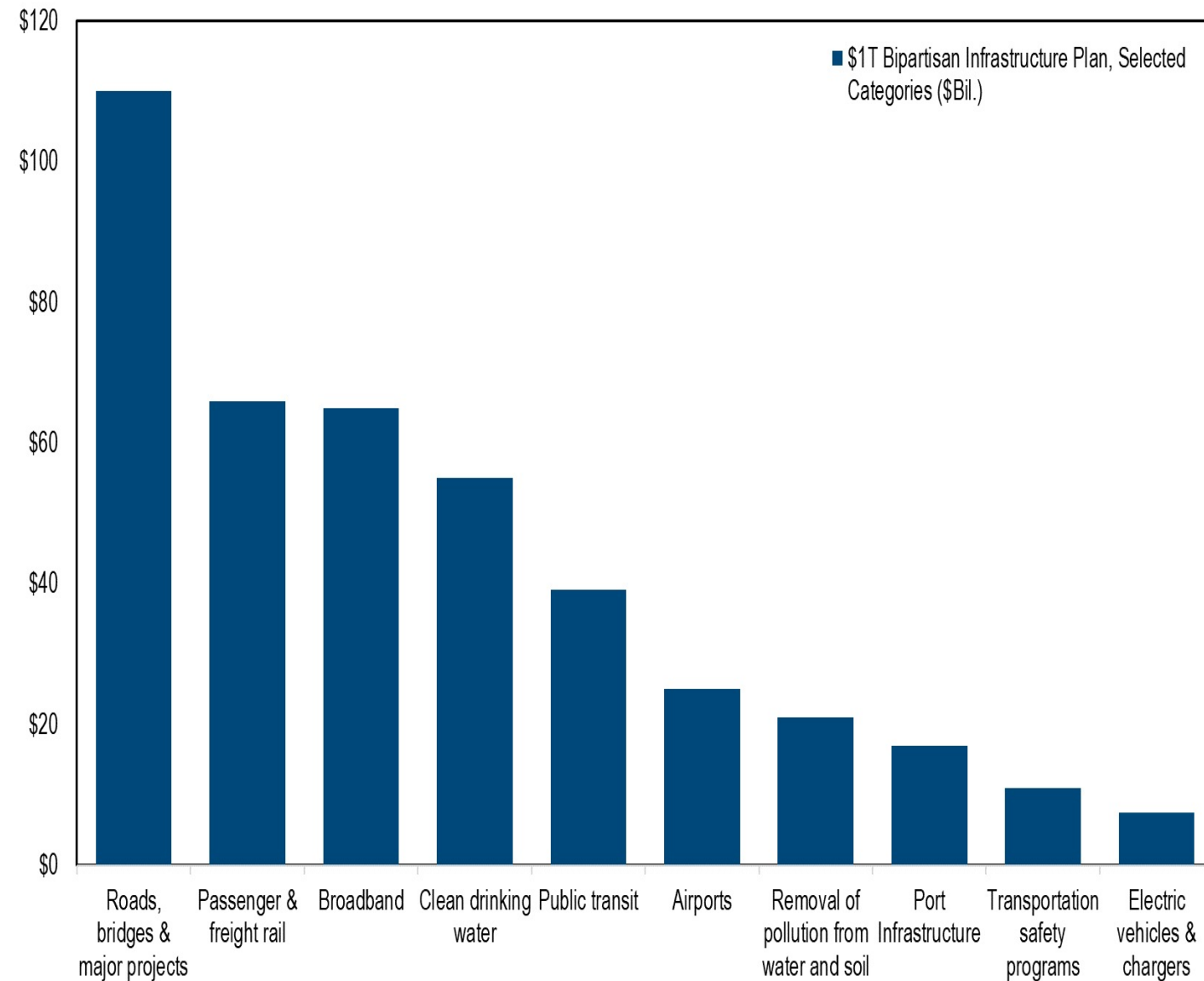


Source: FRED

## \$1.2T Infrastructure Plan

After months of negotiations and a standoff between progressive and moderate Democrats, the **\$1.2T** package of road, broadband, and other "hard" infrastructure improvements passed the U.S. House of Representatives on November 6 with a 228-to-206 vote

Key items include:  
\$110B for roads & bridges  
\$66B for passenger & freight rail  
\$55B for clean drinking water



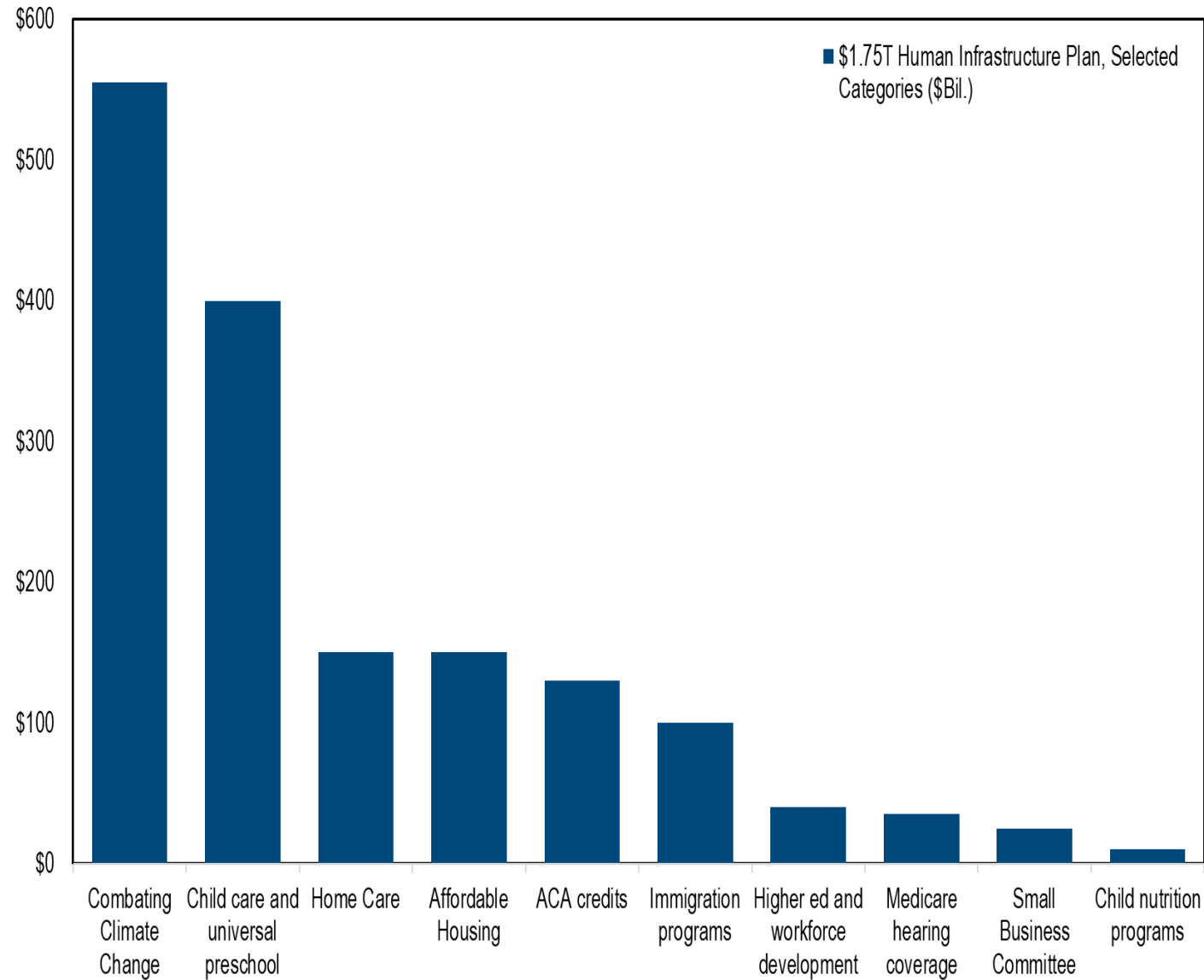
Source: Reuters/NPR

## \$1.75T Human Infrastructure Plan

The White House rolled out a revamped framework that aims to expand the nation's social safety net and combat climate change

The cost of the package has been reduced down from its original \$3.5T price tag to **\$1.75T** over a decade

Key items include:  
\$550B to combat climate change  
\$400B for child care & universal pre-K  
\$150B for home care & \$150B for affordable housing programs



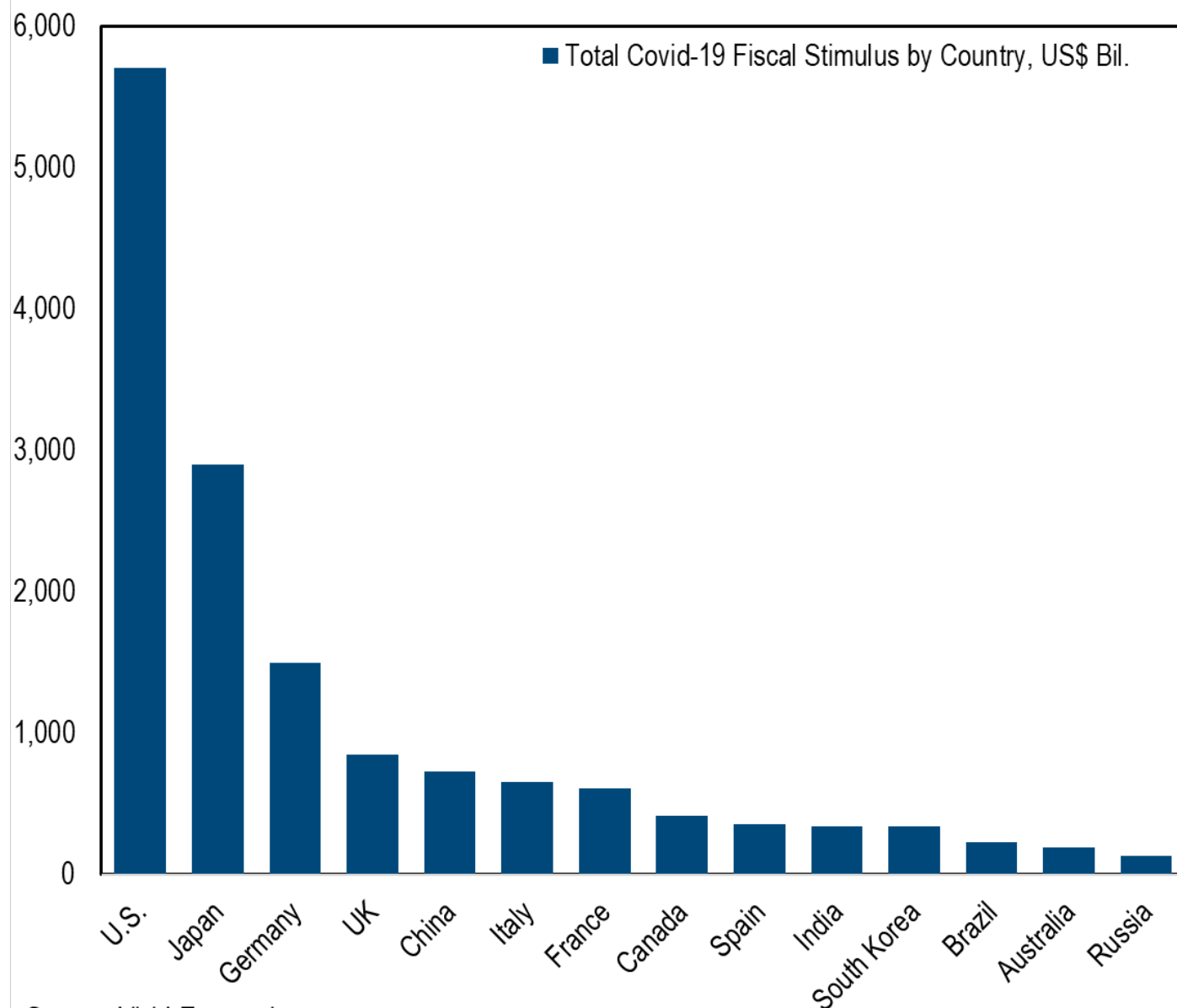
Source: CBS

## Global Covid-19 Spending

The U.S. has spent nearly **\$6T** in Covid relief, and Japan has spent nearly \$3T

By contrast, Australia and Russia have spent \$190B and \$129B, respectively

On a per capita basis, however, the U.S. has spent around \$17k, while Japan has spent around \$23k and Germany has spent around \$18k



Source: Vivid Economics

## Fed to Conclude Taper in March

The Fed doubled the pace of asset reductions at its December FOMC meeting from a monthly reduction of \$15B – \$5B in MBS and \$10B UST to \$30B a month – \$10B for MBS and \$20B for UST beginning in January

Reductions started in November at the \$15 billion pace, meaning the Fed's asset purchase program could be concluded by March 2022 rather than in June had the \$15B pace been maintained

At that point, the Committee will presumably move on to the second phase of its policy adjustment, liftoff

### Federal Reserve Potential Taper Outline:

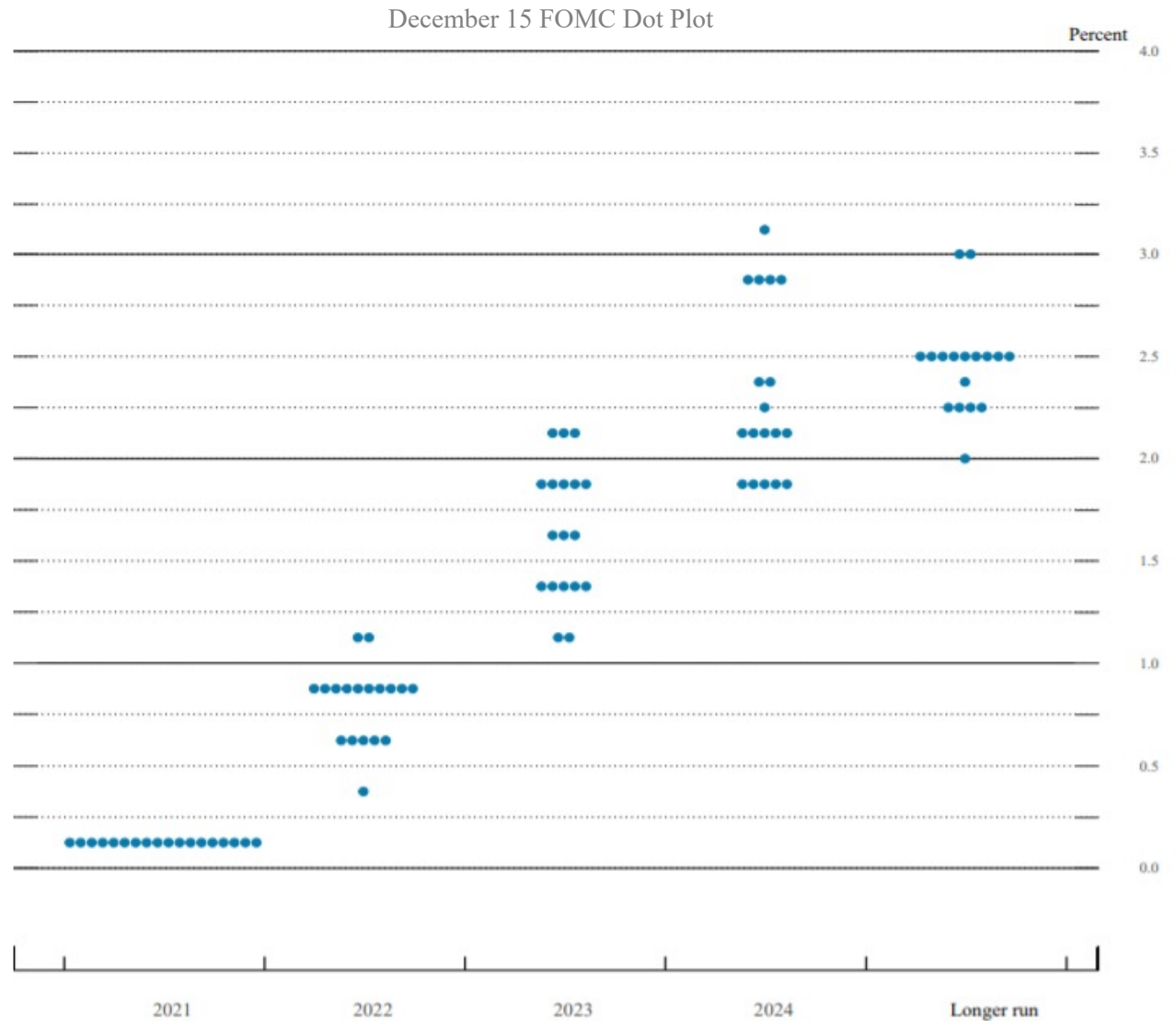
	Monthly Purchases of UST (Bil. \$)	Monthly Purchases of MBS (Bil. \$)
Oct-21	\$80	\$40
Nov-21	\$70	\$35
Dec-21	\$60	\$30
Jan-22	\$40	\$20
Feb-22	\$20	\$10
Mar-22	\$0	\$0

Source: Federal Reserve Board/Stifel



## Fed December Dot Plot

According to the December FOMC dot plot, the majority of Committee members expect three rate hikes this year with five members forecasting two hikes and two members forecasting four hikes



Source: Federal Reserve Board

## Global Central Bank Policy

16 central banks across the world are set to hike rate this year, or have already hiked rates, while 5 are forecasted to keep rates unchanged

The People's Bank of China as well as the Bank of Russia, however, are forecasted to cut rates this year

Central Bank	Keep Rates Unchanged in 2022	Hike Rates in 2022	Cut Rates in 2022
U.S. Federal Reserve		X	
European Central Bank	X		
Bank of Japan	X		
Bank of England		X	
Bank of Canada		X	
People's Bank of China			X

Source: Bloomberg

## Fed Acknowledges Persistent Inflation

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*“Supply and demand imbalances related to the pandemic and the reopening of the economy have continued to contribute to elevated levels of inflation.”*

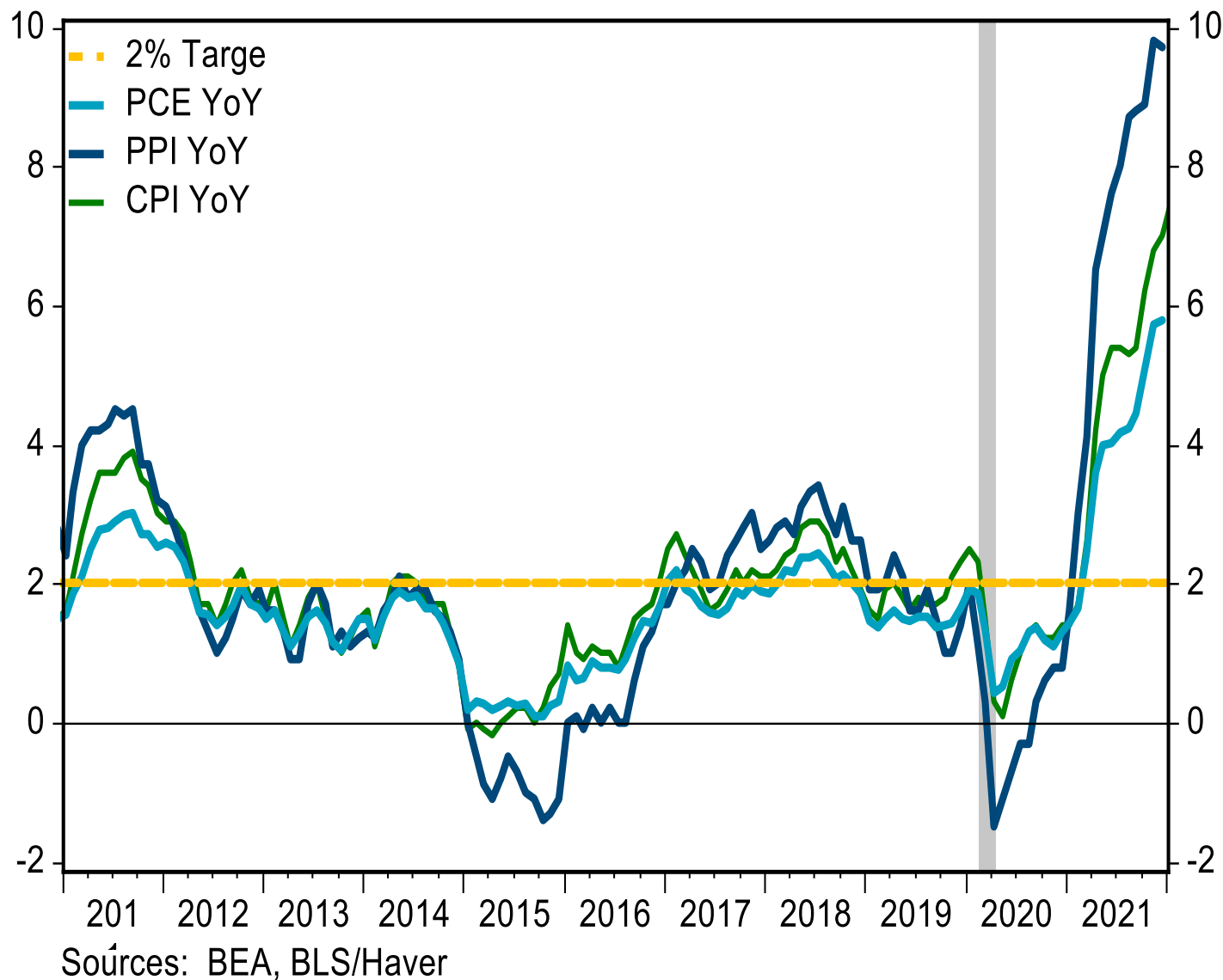
-January 26 FOMC Statement

## ***“Persistent”* Rise in Inflation**

The PCE rose **0.4%** in Dec. and rose **5.8%** YoY, the most since June 1982. The core PCE rose **0.5%** in Dec. and rose **4.9%** YoY, the most since 1983. Inflation had fallen short of the Fed’s 2% target for nearly a decade

Inflation averaged 1.3% from 2015-2020, allowing a potential for inflation to run near 3% for the next five without exceeding a longer-term average of 2%

However, in 2021 alone, inflation averaged 3.7%



## Inflation by Category

The cost of gasoline continues to rise, up **40%** over the past 12 months, with other housing materials such as lumber and heating equipment up **35%** and **22%** over the past 12 months, respectively

The cost of animal feed and certain foods has also increased with animal feeds up **9%**, eggs up **13%**, and pork prices up **14%** from a year ago in January



Gasoline: **40.0% YoY**



Used Cars & Trucks: **40.5% YoY**



Asphalt: **69.5% YoY**



Prepared Paint: **15.6% YoY**



Hardwood Lumber: **34.9% YoY**



Heating Equip.: **21.6% YoY**



Animal Feeds: **9.2% YoY**



Pork: **14.1% YoY**



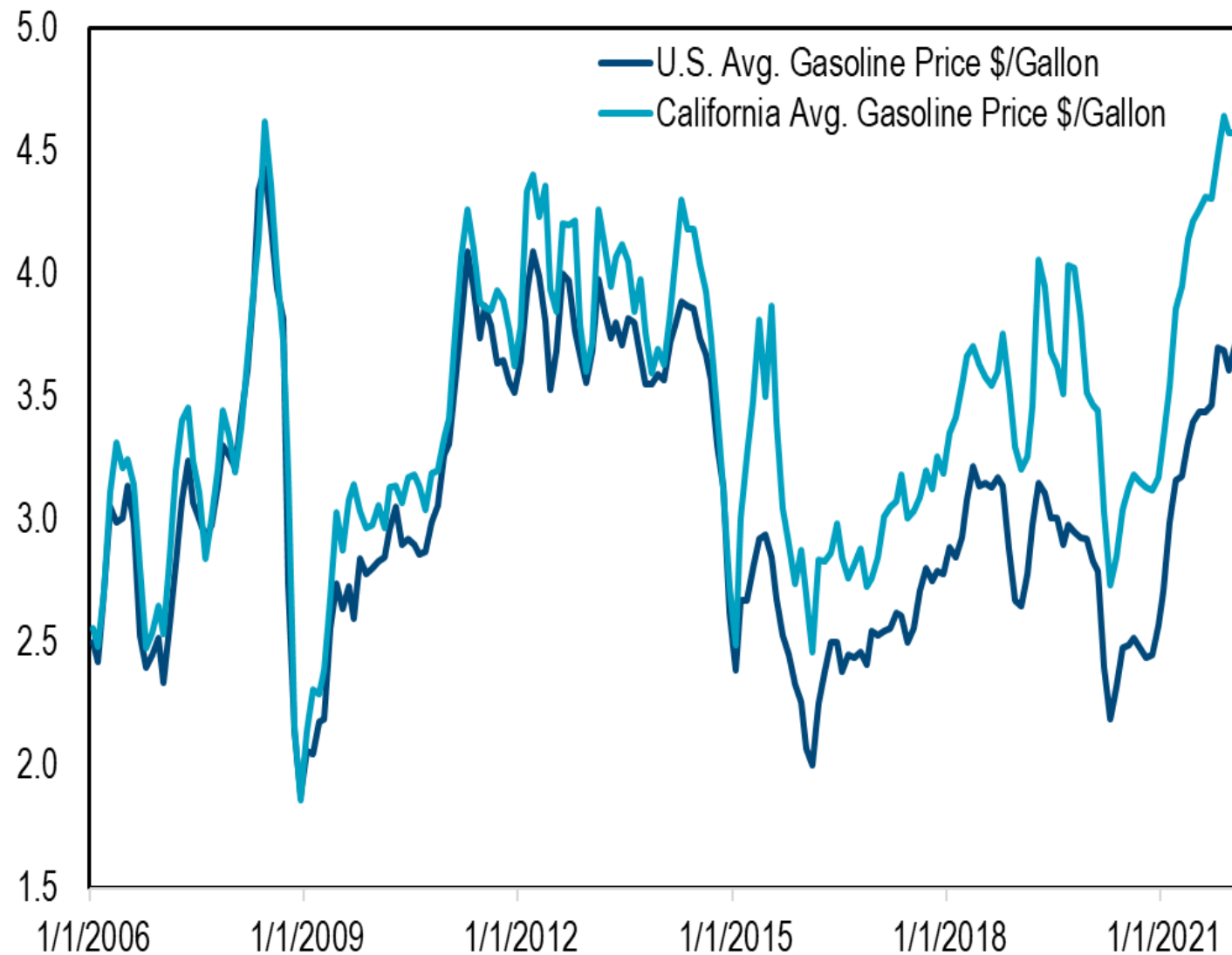
Eggs: **13.1% YoY**

Source: Haver Analytics

## Gas Prices on the Rise

Gas prices are on the rise across the country with the national average at **\$3.71** a gallon as of January, up 37% from this time last year and up 55% from a recent low of \$2.40 in March 2020

California, meanwhile, has the highest gasoline prices in the nation, up over \$4 and 37% over the last 12 months and up a whopping 67% from a recent low in April 2020



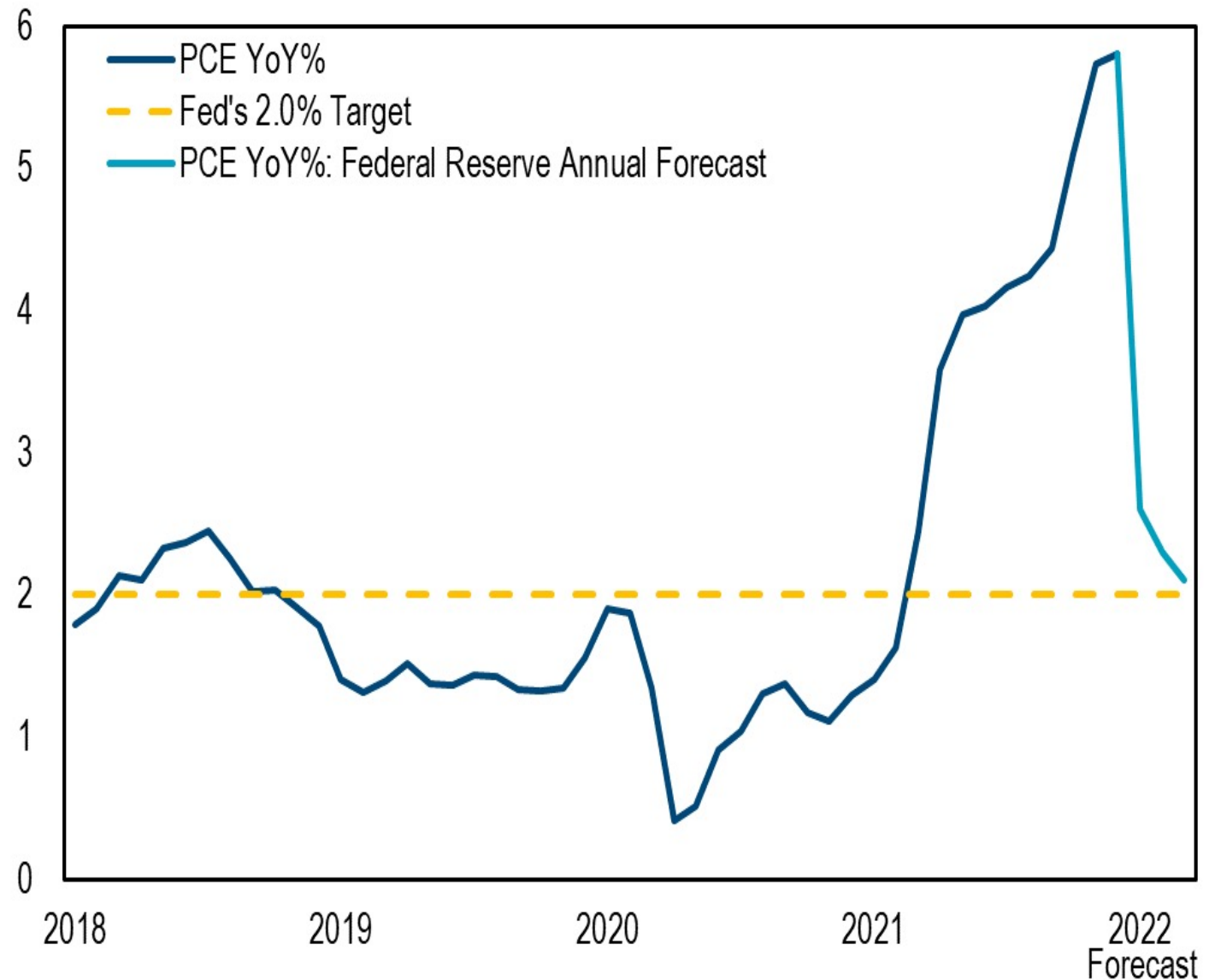
Source: AAA/Department of Energy/ Bloomberg



## Fed Expects Inflation to Moderate “Soon”

Inflation is likely to remain above the Fed’s 2% target for some time

The Fed forecasts a **2.6%** rise in the PCE in 2022, a **2.3%** gain in 2023, and a **2.1%** increase in 2024



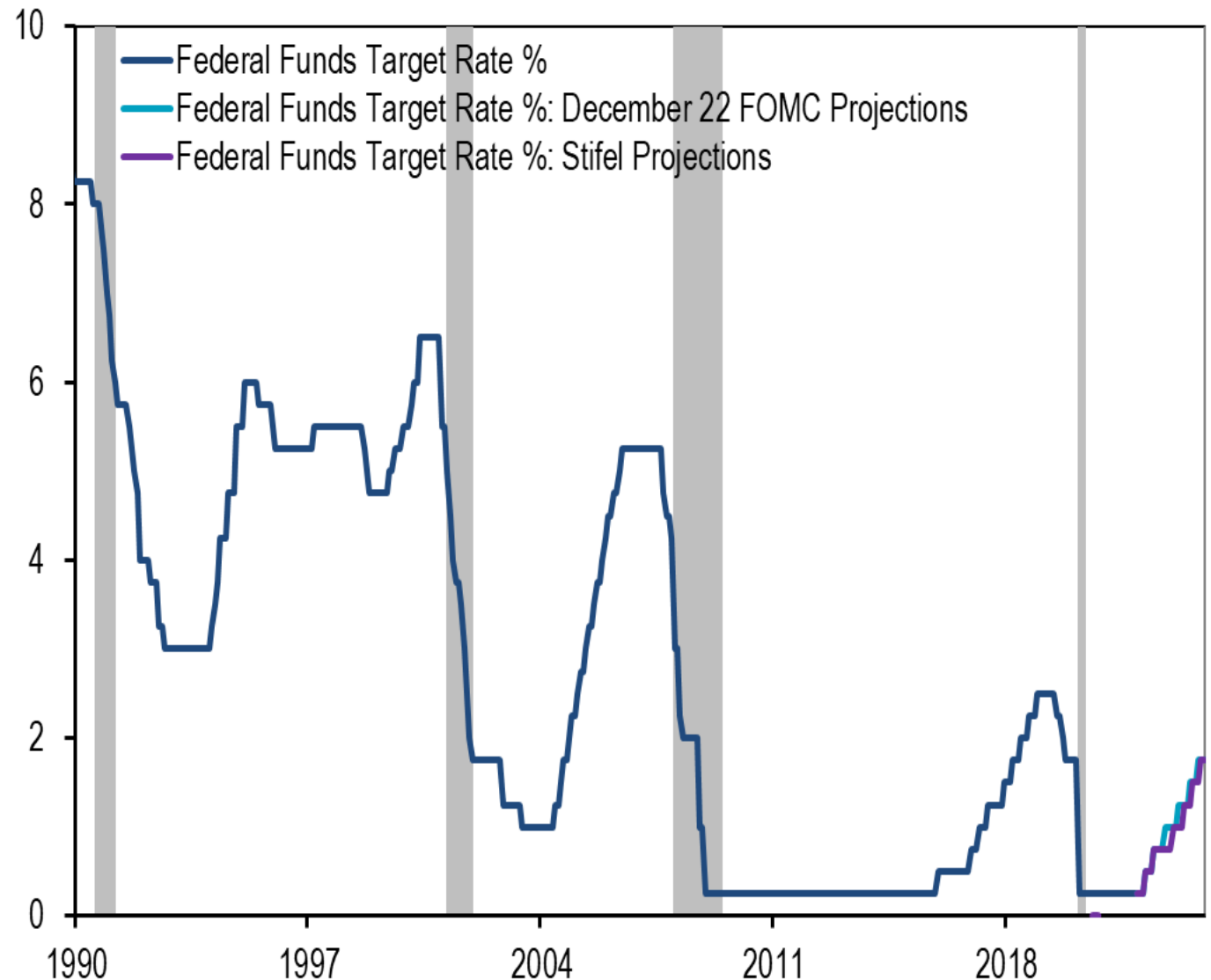
Source: Bureau of Economic Analysis/ Bureau of Labor Statistics/ Federal Reserve

## Fed Projects Rising Rates “Soon”

*“With inflation well above 2 percent and a strong labor market, the Committee expects it will soon be appropriate to raise the target range for the federal funds rate.”*

-Jan. 26 FOMC Statement

The latest December Summary of Economic Projections (SEP) predicts the federal funds rate will rise to 0.9% in 2022, up from the 0.3% expectation in September, and to 1.6% in 2023, up from 1.0% in the September SEP



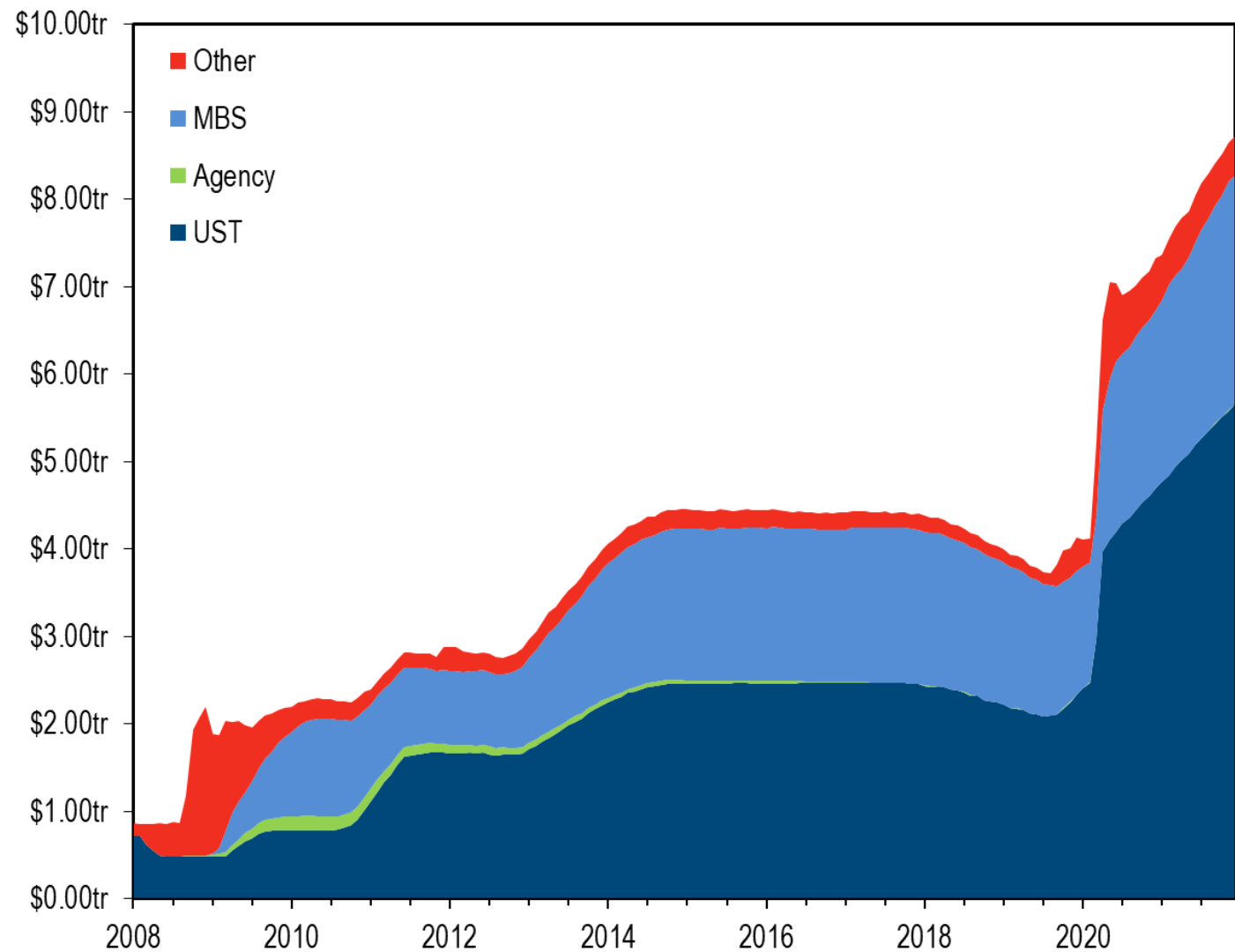
Source: Federal Reserve Board/Bloomberg



## Fed Balance Sheet Tops \$8.5T

During the 2007-2008 Financial Crisis and subsequent recession, the Federal Reserve's balance sheet increased significantly from \$870B in August 2007 to \$4.5T in early 2015, including \$1.7T in MBS and \$1.7T in UST purchases

Since the start of the coronavirus pandemic, the Fed's balance sheet has increased from \$4.2T in February 2020 to **\$8.8T** as of January 2022, with holdings of MBS growing more than \$1.2T and UST purchases rising \$3.3T



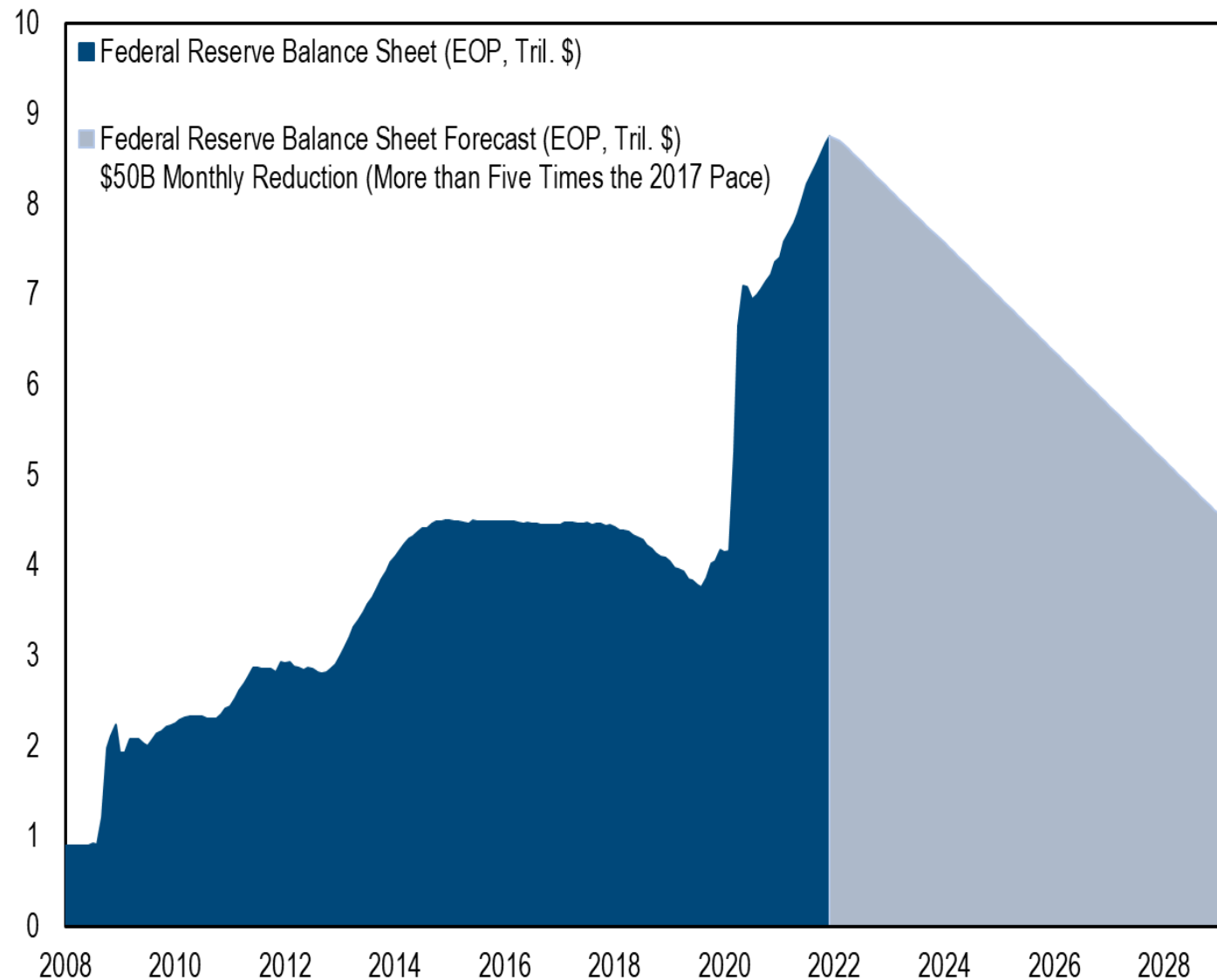
\*Other includes discount window lending; lending to other institutions; assets of limited liability companies (LLCs) that have been consolidated onto the Federal Reserve's balance sheet, and foreign currency holdings associated with reciprocal currency arrangements with other central banks (foreign central bank liquidity swaps).

Source: Federal Reserve/Haver Analytics

## Fed Balance Sheet Forecast

In a separate statement released Jan. 26, the Fed said it expects the process of balance-sheet reduction *“will commence after the process of increasing the target range for the federal funds rate has begun.”*

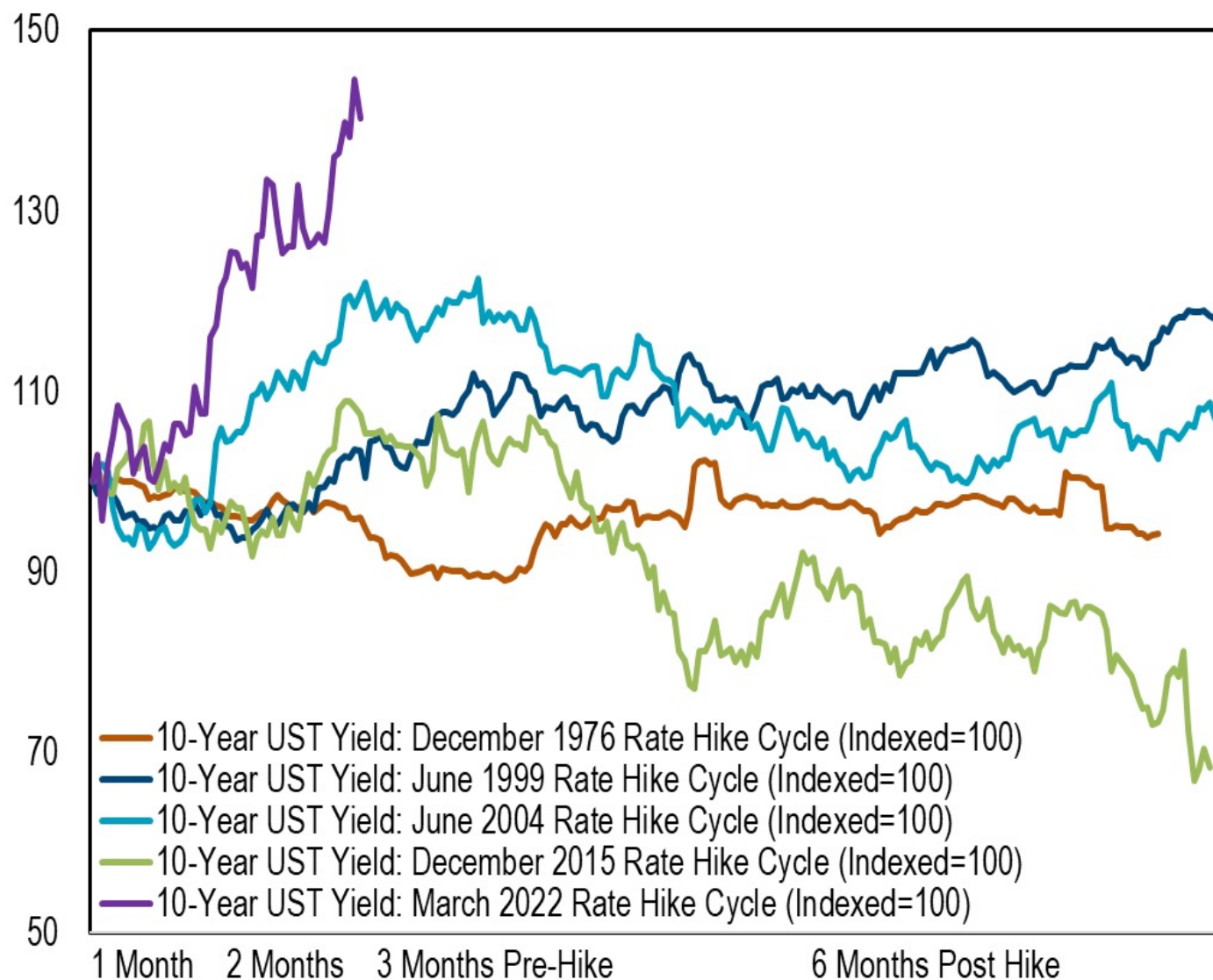
Recall, by contrast, after the taper in 2014, the Fed kept its balance sheet steady for roughly three years before allowing the portfolio to shrink



Source: Federal Reserve Board/Haver Analytics/Stifel

## Market Braces for Three or More Rate Hikes

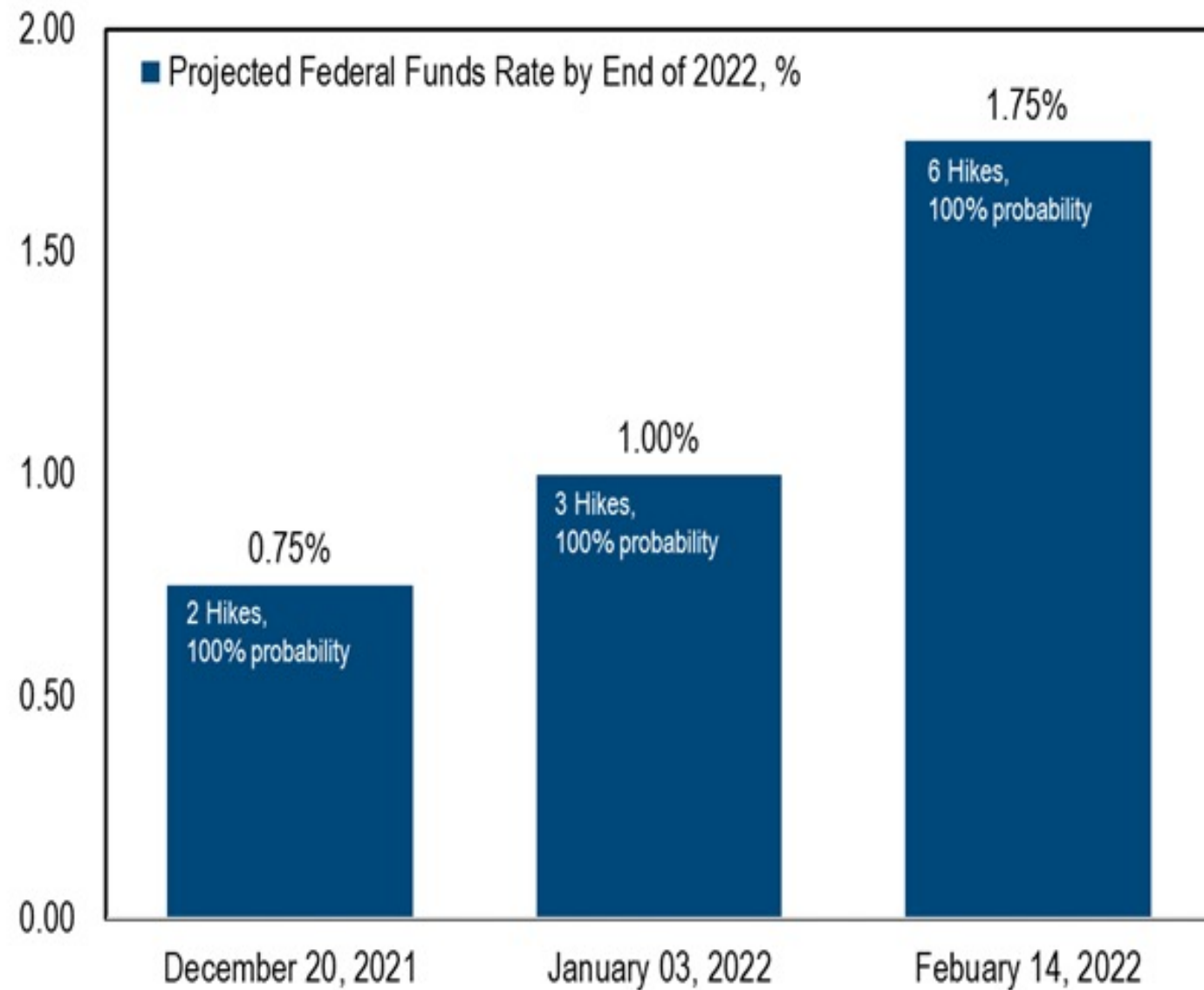
The 10-year has risen 104bps since the start of 2021, and 50bps since the Fed's December FOMC meeting to **1.94%** as of February 11, down slightly from the peak of 2.03% reached earlier on February 11, the highest since 2019



Source: Bloomberg

## Probability of Fed Rate Hikes

The market is currently pricing in a 50bps rate hike in March at 100% probability, up from a less than 50% probability at the start of February



Source: Bloomberg

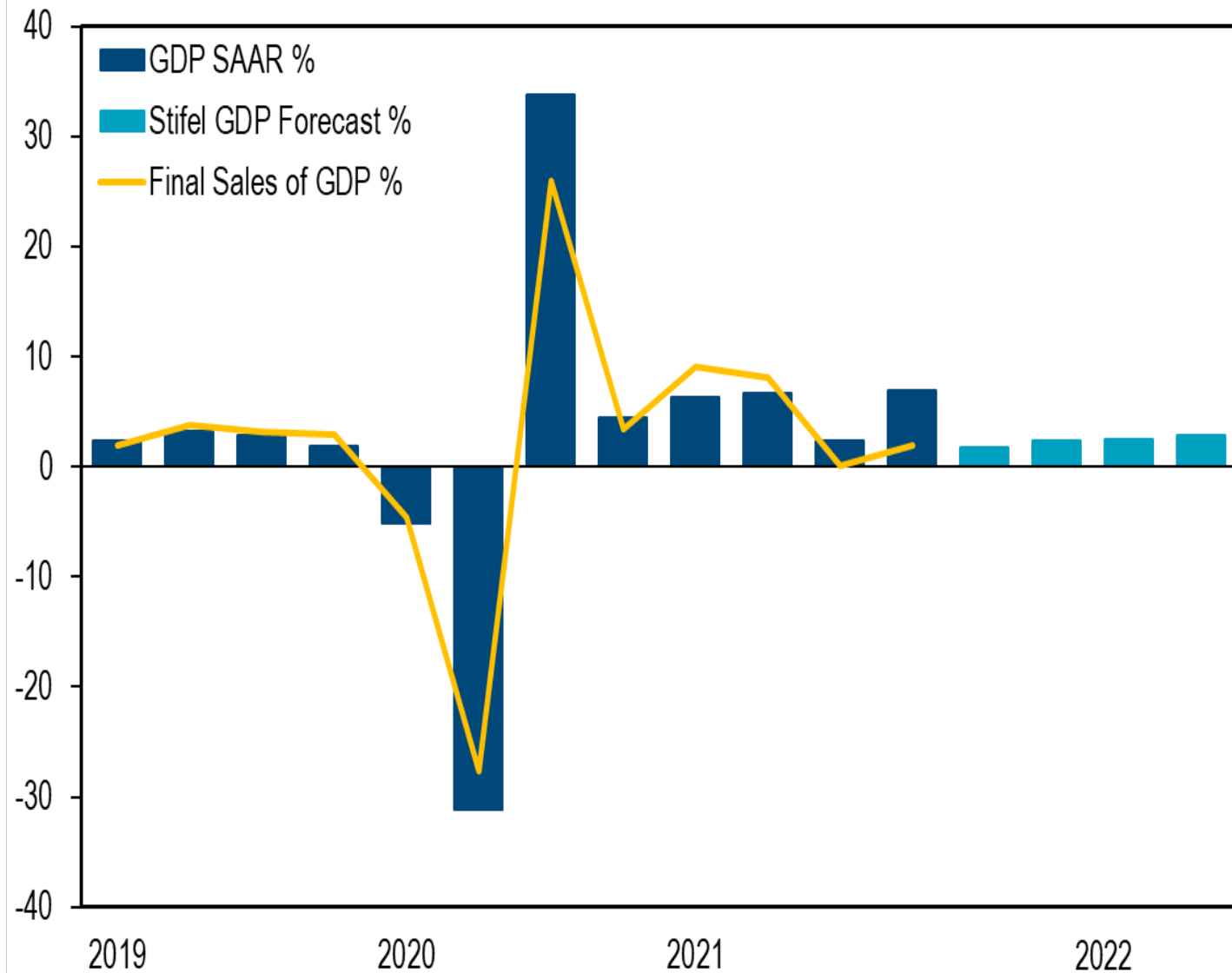
## Growth Reverts to Pre-Pandemic Levels

After a record 31.2% drop in Q2 2020, growth rebounded a record 33.8% in Q3 and rose 4.5% in Q4 2020

GDP rose **6.9%** in Q4 2021, a five-quarter high

Growth is likely to remain restrained throughout 2022

Inventory growth contributed nearly 5% to GDP in Q4



Source: Bloomberg/Stifel

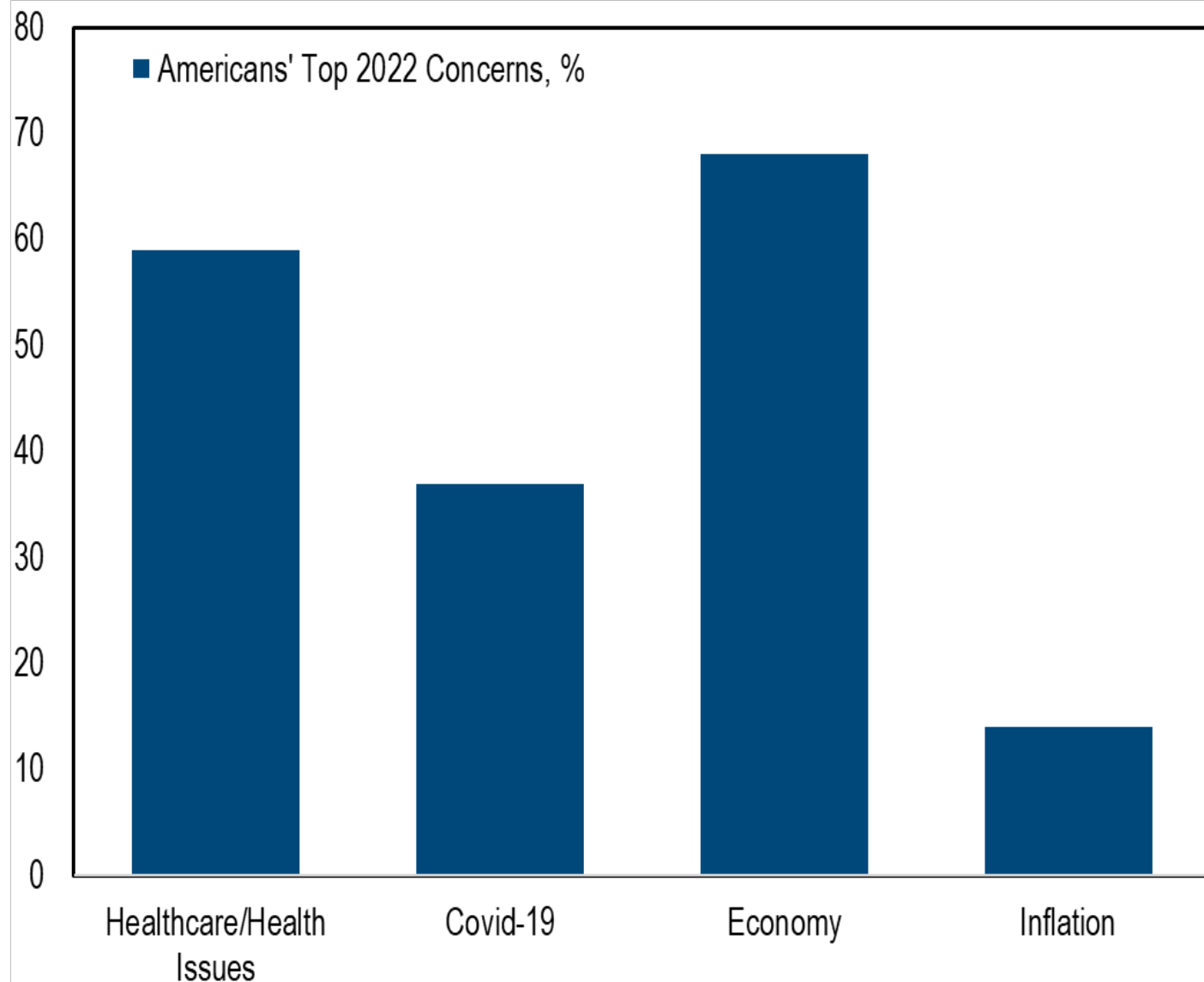
## Americans Fear a Slowing Economy

Just 37% of Americans name the virus as one of their top five priorities for the government to work on in 2022, compared with 53% who said it was a leading priority at the same time a year ago

In terms of healthcare in general, 59% of Americans named it as one of their top priorities

The economy outpaced the pandemic in the open-ended question, with 68% of respondents mentioning it in some way as a top 2022 concern

Mentions of inflation are much higher now: 14% this year, compared with less than 1% last year



Source: The Associated Press-NORC Center for Public Affairs

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