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U.S. Outlook

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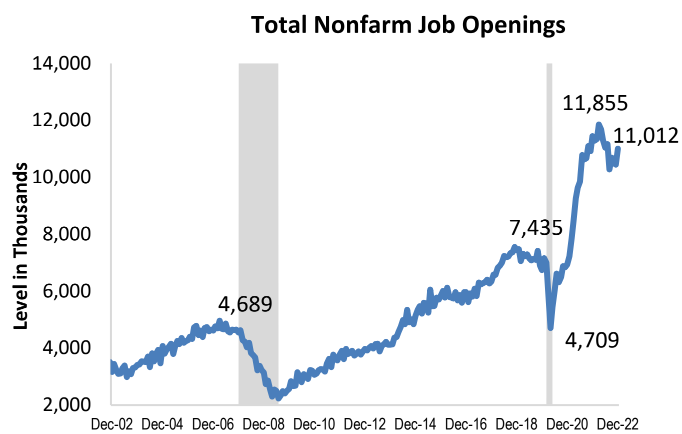
Date	Indicator	For	Estimate	Consensus*	Previous Period
14-Feb-2023	NFIB Small Business Optimism	Jan	91.0	89.8	89.8
14-Feb-2023	CPI MoM	Jan	0.5%	0.5%	-0.1%
14-Feb-2022	CPI Ex Food and Energy MoM	Jan	0.4%	0.4%	0.3%
15-Feb-2023	Empire Manufacturing	Feb	-24.0	-20.0	-32.9
15-Feb-2023	Retail Sales Advance MoM	Jan	1.7%	1.8%	-1.1%
15-Feb-2023	Retail Sales Ex Auto MoM	Jan	0.6%	0.7%	-1.1%
15-Feb-2023	Industrial Production MoM	Jan	0.4%	0.6%	-0.7%
15-Feb-2023	Capacity Utilization	Jan	79.0%	79.1%	78.8%
15-Feb-2023	Business Inventories	Dec	0.3%	0.3%	0.4%
15-Feb-2023	NAHB Housing Market Index	Feb	37	36	35
16-Feb-2023	Building Permits	Jan	1360k	1350k	1337k
16-Feb-2023	Housing Starts	Jan	1370k	1350k	1382k
16-Feb-2023	Initial Jobless Claims	Feb 11	205k	NA	196k
16-Feb-2023	Philadelphia Fed Business Outlook	Feb	-8.0	-7.4	-8.9
16-Feb-2023	PPI Final Demand MoM	Jan	0.4%	0.4%	-0.5%
16-Feb-2023	PPI Ex Food and Energy MoM	Jan	0.3%	0.3%	0.1%
17-Feb-2023	Import Price Index MoM	Jan	-0.1%	-0.2%	0.4%
17-Feb-2023	Leading Index	Jan	-0.4%	-0.3%	-0.8%

Fed's Finally Getting Through To The Bond Market

Jay Powell and the rest of the FOMC must feel like a broken record at this point as the stock and bond markets have largely been tone deaf to the Fed's message on the likely terminal Fed funds rate and how long they are going to have to keep monetary policy in restrictive territory to ensure that they bring inflation down to their 2.0% target. It took a barn burner January Employment Report and a surprisingly strong December JOLTs report to concentrate the minds on Wall Street that traders might want to rethink their expected Fed funds rate path over the next couple of years, especially the prospect for sharp rate cuts starting in the second half of 2023.

Job Openings On The Rebound



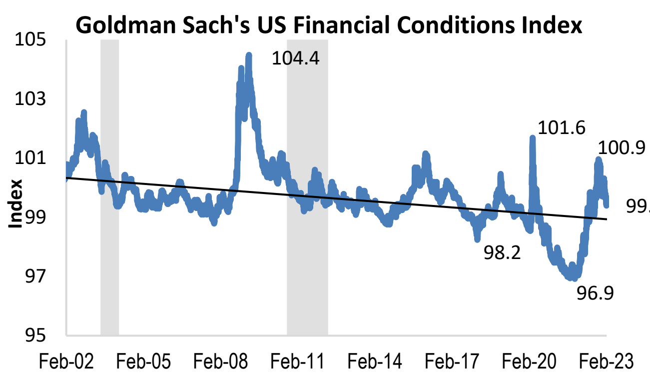
Source: U.S. Bureau of Labor Statistics

Here is why we think Fed Chair Jay Powell and other FOMC members feel the need to push back hard on the market's dovish take on monetary policy.

Not only have labor market conditions tightened further in recent months with the unemployment rate hitting a new 54-year low of 3.4% in January, but job openings have also been creeping higher since August 2022 and absolutely popped back above 11.0 million openings in December. The Federal Reserve and most private sector macroeconomists believe we need to get the U.S. unemployment rate well above 4.0% for a prolonged period of time to truly vanquish inflation for good. So on that front the 450 basis points of Fed rate hikes so far don't even put the Federal Reserve on the scoreboard in cooling down labor market conditions to a sustainable pace.

Even more troubling for the Fed's battle to stanch inflation has been the significant loosening in financial conditions since October. The Goldman Sachs Financial Conditions Index has noticeably eased since October 2022.

Financial Conditions Have Been Loosening Since October

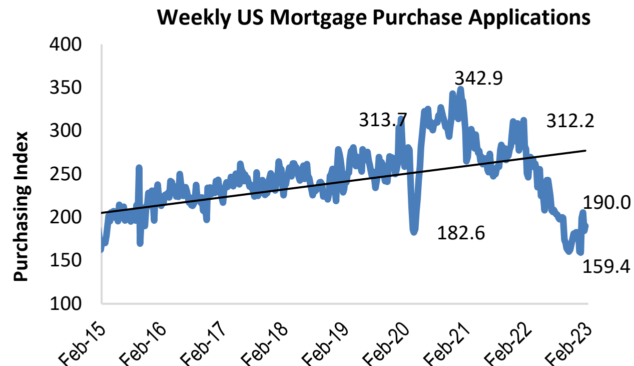


Source: Bloomberg

Long-term Treasury yields, mortgage rates, and high-yield credit spreads have all dropped sharply over the last several months. This has helped trigger a sizable stock market rally since the beginning of the year and bolstered confidence in the "soft landing" scenario for the U.S. economy.

Rising stock prices, resilient labor demand, and rising nominal wages are bolstering investor and consumer confidence, household wealth, and even increasing demand for home purchases. According to the Mortgage Bankers Association, home purchase applications increased 19.2% in January as 30-year mortgage rates plunged around a percentage point from 7.2% in October to just 6.2% at the beginning of February.

Housing Demand Comes Back To Life



Source: Mortgage Bankers Association

Homebuilder stocks and lumber prices both confirmed the stabilization in housing demand in January. We are forecasting a noticeable bounce in the NAHB Housing Market Index for February with a rebound in January housing starts and permits too when the data get released next week. Jay Powell noted in his post FOMC press conference last week that the Fed needs to see "financial conditions that reflect the policy restraint put in place." That's Fed speak for "we need to see tighter financial conditions".

Fed funds futures are finally catching on that the Fed still has a lot of work cut out for it to achieve their inflation goal, and the path to 2.0% inflation might not be a smooth one. As of February 10th, Fed funds futures were pricing in a terminal Fed funds rate of 5.17%, implying two more quarter point rate hikes before a pause with a year-end expected rate of 4.89%. This is far closer to our own forecast and the forecast coming from the FOMC median than the market was on February 1st after Powell's last FOMC press conference. On the 1st, the market expected the Fed funds rate to peak at only 4.89% and end the year at 4.4%. So the peak Fed funds rate in the market today is 28 basis points higher than it was right after the February FOMC meeting, while the year-end Fed funds rate is now 49 basis points higher than it was then. The two year Treasury yield has jumped 39 basis points since Feb 1st to 4.50%. These dramatic interest rate moves on the short-end of the yield curve are a large step in the right direction, the market has begun to listen, but rates still have a ways to go to reflect current conditions. A Fed rate cut in 2023 is still a long shot and robust economic data for January give it even less of a chance.

Key Economic and Interest Rate Forecasts

	History				Forecast								Yr/Yr % chg or Annual Avg.			
Economic Data	**2022.1**	**2022.2**	**2022.3**	**2022.4**	**2023.1**	**2023.2**	**2023.3**	**2023.4**	**2024.1**	**2024.2**	**2024.3**	**2024.4**	**2021**	**2022**	**2023**	**2024**
Real GDP*	-1.6	-0.6	3.2	2.9	-0.8	-2.5	0.2	1.4	1.8	1.4	1.6	1.8	5.9	2.1	0.3	1.2
Personal Consumption Expenditures*	1.3	2.0	2.3	2.1	0.8	-0.5	0.5	1.2	1.4	1.4	1.7	2.0	8.3	2.8	1.0	1.2
Non-residential Fixed Investment*	7.9	0.1	6.2	0.7	3.0	-5.3	-1.0	-0.7	0.9	1.0	1.1	1.2	6.4	3.6	0.4	0.0
Private Housing Starts (000s units)	1,720	1,647	1,450	1,403	1,385	1320	1300	1280	1274	1320	1355	1390	1,605	1,555	1321	1335
Vehicle Sales (mill. Units, annualized)	14.1	13.3	13.3	14.1	14.0	12.6	12.8	13.0	13.3	13.8	14.0	14.1	15.0	13.7	13.1	13.8
Industrial Production*	4.7	5.0	1.8	-1.7	-2.2	-3.0	-0.8	0.5	1.3	1.2	1.8	1.9	4.9	3.9	-1.0	0.7
Nonfarm Payroll Employment (mil.)	150.8	152.0	153.3	154.3	155.3	154.7	154.3	154.3	154.4	154.8	155.1	155.4	146.3	152.6	154.6	154.9
Unemployment rate	3.8	3.6	3.6	3.6	3.5	4.0	4.4	4.7	4.8	4.7	4.7	4.6	5.4	3.7	4.2	4.7
Consumer Price Index* (percent)	9.2	10.5	5.7	3.1	3.7	3.1	3.0	2.5	2.4	2.3	2.2	2.2	4.7	8.0	4.0	2.5
"Core" CPI* (percent)	6.5	6.6	6.4	4.4	4.2	3.9	3.5	3.0	2.4	2.3	2.2	2.1	3.6	6.1	4.4	2.7
PPI (finished goods)* (percent)	6.5	6.6	6.4	4.4	4.1	3.9	3.5	3.0	2.4	2.3	2.2	2.1	8.9	13.5	3.0	2.0
Trade Weighted Dollar (Fed AFE)	108.5	113.7	119.0	120.0	115.0	113.3	112.4	111.8	111.8	111.9	112.1	112.3	104.6	115.3	113.1	112.0
Crude Oil Prices -WTI ($ per barrel)	91	104	89	83	79	77	74	73	72	71	70	70	67	92	76	71

*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

	History				Forecast								Annual Average			
Financial Data	**2022.1**	**2022.2**	**2022.3**	**2022.4**	**2023.1**	**2023.2**	**2023.3**	**2023.4**	**2024.1**	**2024.2**	**2024.3**	**2024.4**	**2021**	**2022**	**2023**	**2024**
S & P 500	4,464	4,106	3,980	3,852									3,218	4,273		
Dow Jones Industrial Average	34,679	32,688	31,774	32,490									26,891	34,055		
Federal Funds Rate (effective)	0.21	0.96	2.63	3.64	4.63	5.04	5.13	5.13	5.04	4.79	4.54	4.29	0.09	1.86	4.98	4.67
Treasury-3 Month Bills (yield)	0.31	1.10	2.75	4.19	4.70	4.99	5.05	5.04	4.99	4.74	4.49	4.24	0.04	2.09	4.95	4.62
Treasury-2 Year Notes (yield)	1.46	2.72	3.38	4.39	4.28	4.67	4.82	4.83	4.81	4.66	4.56	4.37	0.26	2.99	4.65	4.60
Treasury-5 Year Notes (yield)	1.83	2.96	3.23	4.00	3.68	4.19	4.40	4.45	4.49	4.44	4.34	4.19	0.84	3.00	4.18	4.37
Treasury-10 Year Notes (yield)	1.95	2.93	3.10	3.83	3.58	4.09	4.30	4.34	4.39	4.33	4.24	4.11	1.45	2.95	4.08	4.27
Treasury-30 Year Notes (yield)	2.26	3.06	3.26	3.90	3.68	4.19	4.40	4.44	4.49	4.43	4.34	4.21	2.06	3.12	4.18	4.37
Prime Rate	3.33	4.08	5.75	6.82	7.75	8.16	8.25	8.25	8.16	7.91	7.66	7.41	3.25	4.99	8.10	7.79
SOFR Overnight Rate	0.09	0.69	2.15	3.60	4.48	4.92	5.03	5.03	4.94	4.69	4.44	4.19	0.04	1.63	4.87	4.57
SOFR 3-Mo. CME	0.34	1.32	2.84	4.24	4.68	5.10	5.19	5.19	5.10	4.86	4.61	4.36	0.05	2.19	5.04	4.73
Libor 3-Mo. U.S. Dollar	0.53	1.54	3.00	4.51	4.83	5.17	5.26	5.26	5.22	4.96	4.71	4.46	0.16	2.39	5.13	4.84
Mortgage-30 Year (yield)	3.82	5.27	5.62	6.63	6.18	6.74	6.97	7.04	7.06	6.98	6.84	6.61	2.96	5.33	6.73	6.87
BAA Corporate (yield)	3.97	5.02	5.35	5.98	5.43	6.04	6.40	6.49	6.54	6.58	6.54	6.46	3.39	5.08	6.09	6.53

Source: Bank of the West Economics, Bloomberg, Federal Reserve