North American Building Material Distribution Association

Trends ▪ Education ▪ Leadership ▪ Networking

Published Quarterly by ITR Economics™ for NBMDA and NAFCD Members **ITR Advisor / Volume 9 / March 2022**

Industry Snapshots

Arrow denotes 12-month moving total/average direction.

RETAIL SALES	Steep Rise
WHOLESALE TRADE	Steep Rise
AUTO PRODUCTION	Steep Decline
MANUFACTURING	Mild Rise
ROTARY RIG	Mild Rise
CAPITAL GOODS	Steep Rise
NONRESIDENTIAL CONSTRUCTION	Mild Rise
RESIDENTIAL CONSTRUCTION	Steep Rise

Steep Rise · *Mild Rise* · *Flat* · *Mild Decline* · *Steep Decline*

Macroeconomic Outlook

Please note: At ITR Economics, we confine our analysis to the economic impact of events. That does not mean we assign primacy to the economics, and it does not diminish our personal anguish over the pain, suffering, and loss of life resulting from Russia's invasion of Ukraine.

As the first quarter of 2022 nears a close, uncertainty has gripped both US and world economies. International conflict in Ukraine is contributing to high inflation figures as many businesses begin to contend with slowing growth in orders and sales. US Real GDP is already in Phase C, Slowing Growth, and we anticipate many other macroeconomic segments – including US Industrial Production, US Total Retail Sales, and US Nondefense Capital Goods New Orders – will follow suit imminently.

High gasoline prices, a result of high oil prices, have been one of the largest consumer impacts of the current inflationary trend. While daily oil prices have retreated from peak levels of over $120 per barrel, prices remain above $100 as of this writing. This has translated to gasoline prices averaging more than $4 a gallon. Thus far, consumers have been willing to shoulder the burden of rising prices. They have been able to tap into savings built up over the course of the pandemic, and low debt-to-income ratios suggest they have the ability to take on more debt. In addition, the Federal Reserve has begun taking steps to attempt to rein in inflation. It has raised the Federal Funds Rate by 0.25 percentage points, and it has signaled further interest rate rise is ahead. We anticipate quarterly inflation will peak around the middle of this year; disinflation – i.e., slowing inflation – will be the trend for the second half of 2022 and into 2023.

> *"International conflict in Ukraine is contributing to high inflation figures as many businesses begin to contend with slowing growth in orders and sales."*

The relative plateau exhibited by US Single-Unit Housing Starts in recent months is an early manifestation of slowing economic growth. Housing Starts reflect the financial position and confidence of consumers, as a home is a sizeable investment that incorporates both up-front costs that require savings and, for the overall purchase, borrowing costs. Trends in US Personal Savings Rates and US Conventional 30-year Mortgage Rates suggest residential construction will move along the back side of the business cycle into the second half of this year. The national housing shortage will contribute to subsequent residential construction growth. If consumers pare back spending in response to high inflation, construction growth may suffer.

In periods of higher uncertainty, it is essential to lead your business with confidence. Economic fundamentals are strong for growth into at least 2023. While it is important to stay abreast of current trends, keep your focus on the longer-term vision for your business. Let the knowledge of ongoing growth ahead color your capital investments, hiring decisions, and strategic plans.

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Make Your Move

Ensure you have a mix of products or services aimed at a more price-conscious consumer who may focus more on necessities than discretionary items on the back side of the business cycle.

Investor Update

The S&P 500 weakened further in February, as was anticipated based on prior leading indicator signals. The 3.1% decline from month-end January to month-end February was only slightly steeper than normal; the low-side-of normal occurrence for that time frame is -2.9%. That is noteworthy because there was sufficient time in late February after the Ukraine invasion began for a more dramatic decline to occur. Early March included, the market has held up well from our vantage. We seem to be experiencing essentially normal correction activity.

ITR Economics Long-Term View

2022	2023	2024
SLOWING GROWTH	SLOWING GROWTH	GROWTH

Leading Indicator Snapshot

	2Q2022	3Q2022	4Q2022
ITR Leading Indicator™	🔴	🔴	⚪
ITR Retail Sales Leading Indicator™	🟢	🟢	🟢
US OECD Leading Indicator	🔴	🔴	⚪
US ISM PMI (Purchasing Managers Index)	🔴	🔴	🔴
US Total Industry Capacity Utilization Rate	🔴	🟢	⚪

🟢 *Denotes that the indicator signals cyclical rise for the economy in the given quarter.*

🔴 *Denotes that the indicator signals cyclical decline for the economy in the given quarter.*

⚪ *N/A*

KEY TAKEAWAYS

- The majority of leading indicators suggest imminent slowing growth for US Industrial Production.
- The system of leading indicators also suggests that this upcoming period of slowing growth will persist into at least the second half of 2022; some of the individual indicators portend slowing growth into at least 2023.
- ITR Economics™ is monitoring the conflict in Ukraine, as political events can cause disruptions to the fundamentals that typically drive the US economy.

onDemand

Industry Analysis

RETAIL SALES

- Annual Retail Sales totaled $7.6 trillion in February, up 20.9% from the year-ago level
- Both Retail Sales and inflation-adjusted Retail Sales are rising at fastest-ever rates, which suggests consumers are absorbing price increases
- Retail Sales will grow at a slower pace in 2022

WHOLESALE TRADE

- Annual US Total Wholesale Trade, up 24.0% in January from the year-ago level, is rising at the fastest pace in the history of the dataset
- Rise in Wholesale Trade is due to both increasing volume and rising price levels
- This year's growth rates will generally be below those of 2021 as economic activity cools

AUTO PRODUCTION

- Amid supply constraints, annual North America Light Vehicle Production declined in January to be virtually even with the year-ago level
- Demand for vehicles remains strong, though buyers may become more price-conscious in this current inflationary environment
- Geopolitical conflict poses a risk to the availability of materials such as neon and palladium; this is a threat to future Production

MANUFACTURING

- Annual US Total Manufacturing in February was 7.9% above the year-ago level
- ITR Checking Points™ signal that Manufacturing and the majority of its components will transition to slowing growth in the near term
- Production will grow throughout 2022, but at a slower pace than in 2021

ROTARY RIG

- The US Rotary Rig Count in the three months through February averaged 605 units, up 64.2% from the same period one year ago
- Due to geopolitical conflict, oil prices have risen in recent weeks; this is likely to incentivize more exploration in the near term
- With prices so elevated, producers are more likely to revisit previously unprofitable basins

CAPITAL GOODS NEW ORDERS

- Annual US Nondefense Capital Goods New Orders (excluding aircraft) were up 15.1% from the year-ago level
- Key commodity prices are running higher than expected due to the Russian invasion of Ukraine; this will put upward pressure on dollar-denominated New Orders in the near term
- Plan for a slower rate of growth this year than in the latter half of 2021

TOTAL NONRESIDENTIAL CONSTRUCTION

- Annual US Total Nonresidential Construction spending through January was 2.0% below the year-ago level
- Due to price increases, select Nonresidential sectors appear to be on the rise, but adjusting for inflation in most of these cases reveals that actual activity is down
- Rising prices, higher interest rates, and labor market tightness will be pain points for the industry this year

TOTAL RESIDENTIAL CONSTRUCTION

- US Total Residential Construction in the 12 months through January was 22.2% above the year-ago level
- Recent rise in mortgage rates is unlikely to derail the market this year; low inventory levels suggest Construction will still rise in 2022
- Rising materials prices and labor shortages will remain pain points throughout the year

A Closer Look: The US Economy

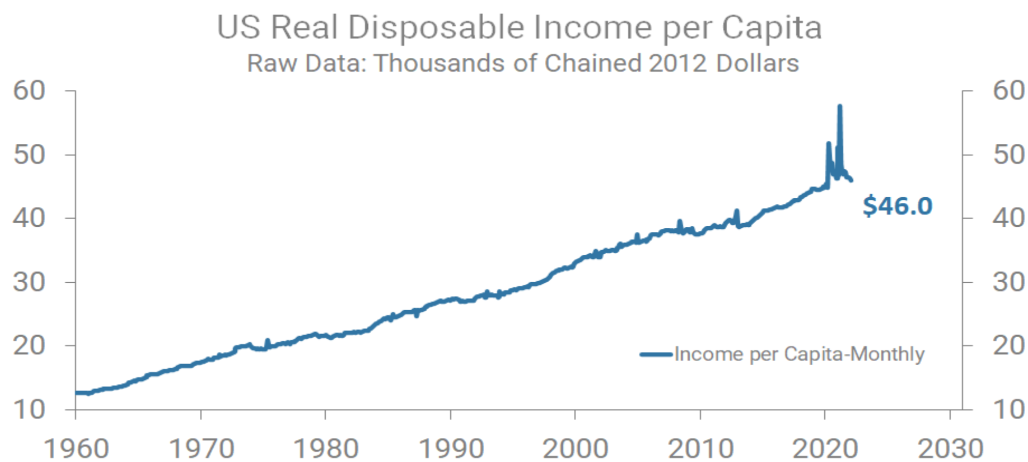
Signs Point to 'Soft Landing' Ahead

BY: LAUREN SAIDEL-BAKER

What you need to know: A resilient consumer will support continued US macroeconomic expansion

The US economy is entering a slowing growth trend but, despite geopolitical conflict, remains poised to avoid a recession. A major component of that strength rests with the US consumer, who drives roughly two-thirds of US GDP.

The tight labor market is contributing to favorable consumer outcomes as more jobseekers are able to find employment, and it is putting upward pressure on wages. This, coupled with the extraordinary pandemic-era government support, suggests that consumer finances are strong in aggregate.



Despite concerns of rising inflation, consumers as a whole have savings and potential borrowings to fall back on. Although they have spent much of their extraordinary stimulus payout, aggregate US Personal Savings levels are still trending around the pre-pandemic high. With regard to borrowing, delinquency rates are low across most debt categories, and low interest rates are making borrowing affordable. US household debt service payments currently account for just 9.2% of disposable personal income – a manageable level for borrowers and well-below the long-term average of 11.1%.

Taken together, these consumer trends have been supporting resurging demand and, in turn, the rapid rebound in economic activity. Relative to the year-ago level, annual US Total Retail Sales are up 19.7% – the highest year-over-year comparison in the history of the dataset. While this pace of growth is not sustainable, especially considering that it was spurred by impacts of stimulus that will not repeat, a contraction in activity is also unlikely, due to the consumer strength outlined above.

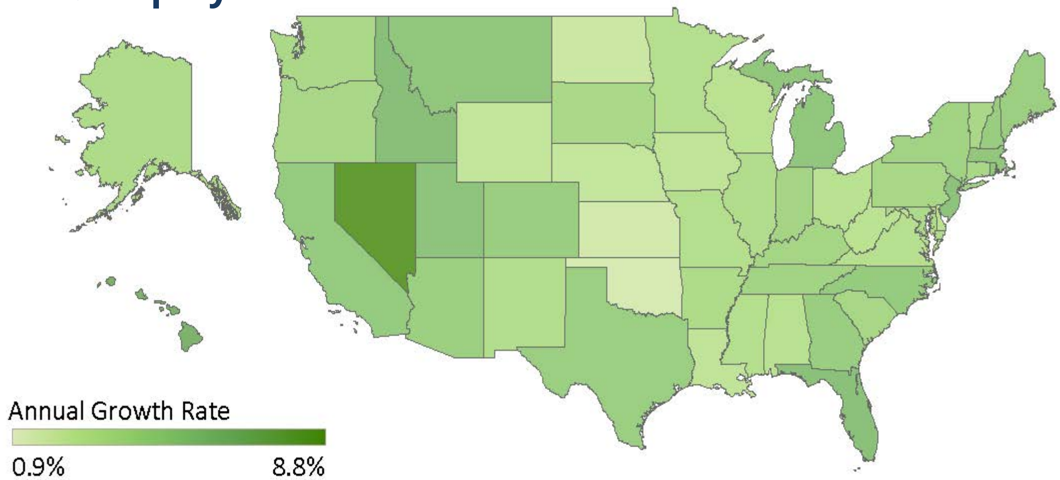
Rather than decline, expect a slower pace of rise in consumer spending, resulting in slower – and more manageable – economic growth ahead. There are several risks to the health of the US consumer, but none significant enough to alter our expectation for a macroeconomic "soft landing" – that is, the avoidance of a recession this cycle.

- The conflict in Ukraine is creating uncertainty and volatility in asset prices. However, while rising energy costs are marginally cutting into disposable income, the war is unlikely to significantly alter US consumer spending patterns. Distant conflict captures consumers' attention, but it has less influence on actual buying patterns.

- Inflation erodes purchasing power, and a significant jump in consumer price inflation, could, to the extent that it outpaces wage gains, result in declining "real", inflation-adjusted income – over a long enough period of time to hinder spending. However, we expect disinflation will take hold in the Consumer Price Index (CPI) by the middle of 2022. We will continue to monitor this risk.

- Interest rate increases are likely to be implemented this year and next as part of the Federal Reserve's effort to counter high inflation. Changes in rates will alter borrowing incentives and impact the affordability of mortgages and other forms of debt. But increases will likely be gradual and moderate enough to avoid shocking markets, and this should mitigate the consumer impact. Federal Open Market Committee members project that even in 2024 and the longer run, interest rates will range from 2–3%. While higher than the recent historically low rates, these levels are still quite manageable in the broader economic context.

State-by-State: Employment



- Annual US Private Sector Employment is up 5.3% year-over-year. However, at 2.7% below the March 2020 level, Employment has not yet fully recovered from the pandemic-related shutdowns. Meanwhile, US Total Nonfarm Job Openings are up 59.1% from the year-ago level; this indicates strong demand for labor and suggests that Employment's incomplete recovery is largely attributable to workforce availability issues.
- Employment growth rates for Nevada and Hawaii – up 8.8% and 6.6% year-over-year, respectively – are the strongest in the country. Nevada's particularly strong growth is occurring as an increasing number of people leave California and head to nearby states in search of a more affordable cost of living. In Hawaii, tourism spending has increased significantly from a year ago, alongside the gradual loosening of travel and other restrictions related to COVID-19. As tourism returns to the state, we can expect Employment will continue to rise.
- Employment growth rates for Oklahoma and Kansas – up 1.4% and 1.6%, respectively – are lagging those for the rest of the US.

Reader's Forum

What is going on with interest rates, and how will it impact my business this year?

Sara Aybar, Economist at ITR Economics™, answers:

The Federal Reserve announced in March that it was increasing short-term interest rates by 25 basis points; this the is first rise in interest rates since 2018. This decision stems from mounting concerns over inflation – at 7.9% as of February – and the tight labor market. Despite rising prices and a US Personal Savings Rate that has returned to the pre-pandemic level, consumer demand is relatively strong. Concerned that such demand will fuel further inflation, the Fed is aiming to curb the latter by raising the federal funds rate to 1.9% by the end of 2022. This could be accomplished via any combination of hikes made over the Fed's six remaining meetings this year.

We do not expect these increases to stop the economy from growing. If your business has planned investments for this year, it may be wise to lock in your interest rates now before they are lifted further this year.

Please send questions to:questions@itreconomics.com