OBSERVATIONS

- Markets traded higher last week as investors cheered the better than expected inflation data. The S&P 500 gained +2.9% and small caps gained +4.0%, while the yield on a 10-year Treasury fell -13 basis points to end the week at 4.63%.[1]
- Producer prices came in better than expected in December despite the headline PPI index climbing to 3.3% year-over-year (YoY) last month from November's 3.0% YoY level. Core-PPI, which excludes food and energy also came in lower than expected and was unchanged at 3.5% YoY in December from November's level.[1]
- Consumer inflation as measured by the CPI also came in better than expected despite increasing to 2.9% YoY in December from November's 2.7% YoY level. Core-CPI fell to 3.2% YoY in December, which was a touch lower from November's 3.3% YoY figure.[1]
- Retail sales came in slightly weaker than expected in December—+0.4% month-over-month (MoM) versus expectations for +0.6% MoM—but both October and November's retails sales were revised higher.[1]
- Meanwhile, the Fed's Beige Book—a qualitative assessment of the economic conditions by Fed district—showed that consumer spending generally moved up moderately in November and December, "with most Districts reporting strong holiday sales that exceeded expectations."[1]
- New housing starts surged in December increasing +15.8% MoM to 1.499 million units (annualized rate), but new home building permits fell -0.7% MoM to 1.483 million units (annualized rate). For the full year a total of 1.364 million homes started construction, which was -3.9% less new home starts than in 2023.[1]
- Industrial production increased +0.9% MoM in December and November's industrial production was revised higher, while capacity utilization climbed to 77.6% in December from November's 77% level.[1]
- Initial unemployment claims have started out the year continuing the trend from 2024. Initial claims remained low at 217k last week, which was a slight (+14k) increase from the week prior.[1]

EXPECTATIONS

- Q4 earnings season kicked-off last week with large US banks making bumper profits. JPMorgan delivered a record full year profit. Meanwhile, Goldman Sach, Bank of America, and Morgan Stanley saw Q4 profits double from the previous quarter, and Citigroup and Wells Fargo also beat earnings estimates in Q4.[2]
- As various measures of core inflation ticked modestly lower, expectations for Fed rate cuts adjusted last week. Prior to last week's inflation data, markets had not been pricing in a full -25 basis point Fed rate cut until Sep-2025, but by the end of the week markets had priced in this cut by Jul-2025 and raised the probability of a second rate cut in 2025 from about 20% to 40%.[1]

ONE MORE THOUGHT: Small Business Optimism Surges Post Election[1]

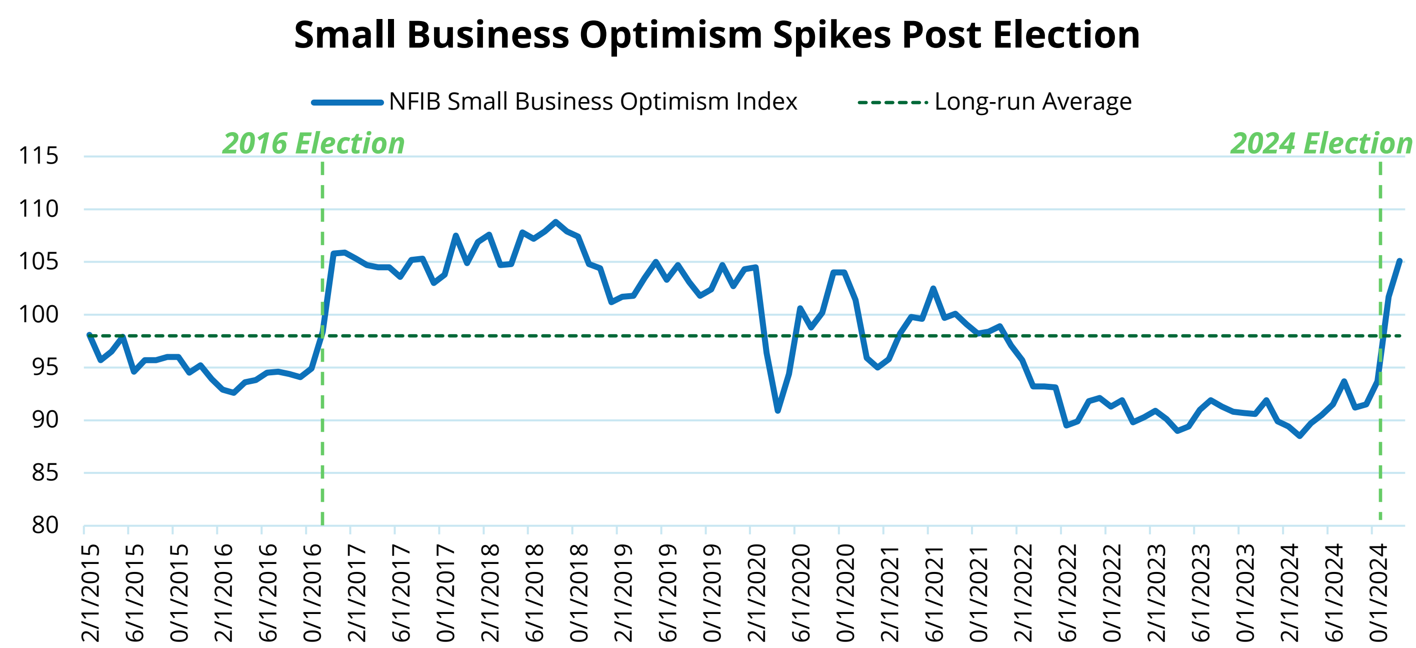
The election of Trump last November on a largely pro-growth, pro-business agenda has spurred a surge in small business optimism. Small businesses seem to be energized by the notion of potentially lower taxes, a push for further deregulation, and rising expectations of a stronger economy in 2025, which has caused small business optimism to rise to pre-pandemic levels. In fact, the net share of small business owners expecting the economy to improve rose 16 points from November to a net 52% (seasonally adjusted) in December—the highest reading on this measure since the fourth quarter of 1983. Additionally, the share of small business owners believing it is a good time to expand their business rose six points to 20%, seasonally adjusted. This is the highest reading since

[1] *Bloomberg LP, 1/17/2025*

[2] *https://www.wsj.com/business/earnings/jpmorgan-chase-earnings-report-4q-2024-jpm-835747eb?mod=earnings_more_article_pos5*

February 2020. Similarly, the net share of small businesses expecting higher real sales volumes rose eight points to a net 22% (seasonally adjusted), the highest reading since January 2020. Hiring plans for small businesses also increased in December. A similar surge in small business optimism also occurred during the 2016 election of Trump. Indeed, Trump's 2016 victory caused the NFIB Small Business Optimism Index to move from well below its 50-year average of 98 to well above its long-run average. Some of this move in the index may be related to the fact that small business owners as a group may lean more Republican than Democrat. But the fact that small business optimism remained above its long-run average throughout Trump's first term—with the brief exception during the early 2020 Covid lockdowns—suggests that the policies pursued by Trump's first administration were largely supportive of the US economy and small businesses overall—see Chart of the Week. Positive small business optimism largely remained in place through the 2020 election and Biden's first year in office but began to decline in 2022 when inflation began to rise steeply, and it became increasingly difficult to hire workers. There remains some uncertainty over both the details and the impact of some of Trump's economic policies in his second term including immigration and tariffs, but so far, the small business community sees the glass as half full and are looking forward to better days to come in 2025.

CHART OF THE WEEK



Source: Clearstead, NFIB, Bloomberg LP 1/17/2025

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