



Kristina Hooper
Chief Global Market Strategist

The world is opening up in many places, and I have had the good fortune of more travel and interaction with clients. One of the questions I get is about which metrics I like to follow most closely. I have a very long list, but below are a few that I think are particularly relevant right now.

Metrics to watch in April

Chinese economic indicators. China's economy has come under pressure recently as a result of COVID lockdowns around the country. That is reflected in the most recent Purchasing Managers Index (PMI) survey data. China's manufacturing PMI for March clocked in at 49.5 – which is technically contraction territory – down from 50.2 in February.¹ Similarly, the services PMI for March clocked in at 48.4 compared with 51.2 in February.¹ I continue to believe this weakness should be very short-lived and I expect to see a reacceleration in economic growth in the back half of 2022 as lockdowns subside with the recently announced change in COVID policy to “zero-COVID at a societal level” and monetary and fiscal stimulus support the economy. We will want to follow the PMIs closely, including the sub-indexes, which can provide additional color on economic activity, as well as economic data.

European economic data. Europe is at the epicenter of the Russia-Ukraine crisis, and the eurozone economy is clearly at an increasing risk of recession, in my view. We are already seeing weakness in economic sentiment, which could easily translate into a decline in economic activity. The euro area Economic Sentiment Indicator reflects this worsening sentiment. It dropped 5.4 points in March, largely due to a substantial drop in consumer confidence.² So we will want to follow European economic data, especially consumer spending since that appears to be an area of real weakness. In addition, the Economic Uncertainty Indicator rose abruptly in March (up 10.7 points to 25.8).² Typically when economic uncertainty goes up, capital spending decreases. And so, we will want to follow these sentiment indicators and business investment closely.

Geopolitical developments related to energy production. Obviously, the prices of oil and natural gas are front and center in the minds of economists and strategists right now because they're having such an impact on the global economy. While many fear oil prices will rise above \$150 per barrel, I think it's important to note that historically, oil prices have rarely lasted above \$100 per barrel for very long. High prices tend to have a way of reducing demand and increasing supply.

One way to increase supply is through geopolitical negotiations, and so we will want to follow such developments closely. While geopolitical developments could push energy prices up — for example, if the European Union (EU) makes the decision to no longer

purchase Russian energy or if Russia refuses to sell to the EU — they can also cause them to fall by increasing supply. We could see countries like the US focus less on the environmental impact of fossil fuels in the short run and allow greater energy production. The US and European countries could ease sanctions on countries such as Iran and Venezuela in order to increase the supply of energy. And we have already seen the US announce plans to dramatically increase the release of oil from the country's strategic petroleum reserves.

Supply chain disruptions. Supply chain disruptions have a significant impact on supply and also can contribute to inflationary pressures. Disruptions were starting to improve in some parts of the global supply chain until Russia's invasion of Ukraine. Exacerbating supply chain issues is the most recent wave of COVID, which is causing lockdowns in China. Recently, the New York Fed created a Global Supply Chain Pressure Index. Its most recent reading, for February, shows easing in global supply chain pressures since December 2021. However, I anticipate the March reading will show a worsening situation, reflecting the invasion of Ukraine and the COVID-related lockdowns.

This is a helpful metric to get a sense of how much disruption is occurring in supply chains – which of course has implications for inflation. That said, this is a “big picture” assessment of the global supply chain, incorporating transportation costs from sources such as the Baltic Dry Index as well as delivery times and backlogs pulled from PMI surveys of major interconnected economies (China, the euro area, Japan, Taiwan, South Korea, the United Kingdom, and the United States). There are also country-specific assessments for those major interconnected economies. There are limitations to these indices, as they do not give us a sense of specific stresses. (As such, we also need to track key inputs such as semiconductors.)

Shipping container prices. In addition to supply chain disruptions, I think it's important to pay close attention to shipping container prices. They reflect a variety of factors including labor costs (and labor scarcity) as well as oil prices. And they can play a significant role in inflationary pressures, as higher transportation costs can often be added to the prices that consumers pay for goods. I follow the Freightose Baltic Index: Global Container Freight Index and the World Container Index as well as container costs for specific shipping routes. The good news is that container prices have eased since peaking several months ago, although they remain much higher than they were before the pandemic.³

US consumer sentiment on “big ticket item” buying conditions. The University of Michigan surveys consumers monthly on whether they believe it is a good time or a bad time to buy major household durables and vehicles (two separate survey questions). In recent months, we have seen the index plummet, with an increasing number of consumers saying it is a bad time to buy such items. This could be a positive in terms of reducing inflationary pressures; it means that households are postponing major purchases unless necessary. Keep in mind that typically consumers in inflationary environments have purchased goods sooner because they expect prices to rise in the future. A reduction in demand may help alleviate inflationary pressures.

US inflation expectations. The Federal Reserve wants to ensure that longer-term inflation expectations remain “well anchored.” Of course, the Fed follows different measures of inflation expectations, from market-based to survey-based – and there are a variety of surveys, from economists to business leaders to consumers. However, I continue to believe that what the Fed cares about most is consumers’ inflation expectations since they are such an important part of the US economy. And so, following the NY Fed Survey of Consumers and University of Michigan Survey of Consumers inflation expectations – especially longer-term expectations – may be very helpful. As of now, Michigan consumer expectations for inflation five years ahead remain elevated but appear relatively well anchored, but that could change as time passes and inflation remains high.

The US Treasury yield curve. As we are all well aware, the 2-year/10-year US Treasury yield curve inverted last week,⁴ which could be an indicator that markets expect the US economy to worsen. However, other parts of the yield curve appear healthy. We will want to continue to follow the yield curve closely to see if all parts of the yield curve ultimately invert. In particular, I would pay close attention to the 3-month/10-year US Treasury yield curve, as historically some economists have relied on that metric to predict recessions. Moreover, we want to follow yield curves with the understanding that to be predictive, an inversion needs to last a significant period of time – and that inversions have not historically been a reliable sell signal for stocks. Over the past six decades, the median amount of time between the initial inversion of the 2-year/10-year yield curve and the onset of a recession is 18 months.⁵

US employment situation. The March jobs report gave the Fed two reasons to raise rates by 50 basis points in May. First, the report showed strength in job creation. March nonfarm payrolls were strong at 431,000 – and February’s nonfarm payrolls were revised upward to 750,000.⁶ Secondly, average hourly earnings rose 0.4% for the month.⁶

This doesn’t mean that a more aggressive path for rates for the entire year is a done-deal, however. In my view, the biggest risk to the US economy continues to be an overly aggressive Fed that sends the US into recession. I am confident the Fed will try to its best to avoid a recession and engineer a “soft landing” by being data dependent in its actions, which means following the jobs report closely for signs of weakness in coming months. Any significant weakness in employment could be a reason for the Fed to slow down its tightening plans later in the year, so we will want to pay close attention to see if the strength we saw in March persists or reverses. Conversely, if wages were to continue to grow at a fast pace, the Fed could become concerned about the potential for a wage-price spiral (rising wages leading to even higher prices, leading to even higher wages, and so on), which could cause it to get even more aggressive in tightening.

Conclusion

April is Financial Literacy Month in the US, but financial literacy is a critical topic all across the globe. And part of that is understanding what different market and economic reports are telling us as investors. Hopefully, this “short list” can help make sense of this challenging economic environment. However, we must recognize that while these indicators can help inform tactical decisions, they are of little consequence in the longer run. Over the longer run, I believe investors’ focus should be on maintaining portfolios diversified across and within the three major asset classes in order to help meet investment goals.

Notes

¹China National Bureau of Statistics

²European Commission, March 30, 2022

³Freightose Data (Freightose Baltic Index: Global Container Freight Index) and Drewry (World Container Index)

⁴Bloomberg, L.P.

⁵National Bureau of Economic Research; Bloomberg, L.P.; Invesco

⁶US Bureau of Labor Statistics, April 1, 2022

Important information

This does not constitute a recommendation of any investment strategy or product for a particular investor. Investors should consult a financial professional before making any investment decisions.

All investing involves risk, including the risk of loss.

Diversification does not guarantee a profit or eliminate the risk of loss.

In general, stock values fluctuate, sometimes widely, in response to activities specific to the company as well as general market, economic and political conditions.

Investments in companies located or operating in Greater China are subject to the following risks: nationalization, expropriation, or confiscation of property, difficulty in obtaining and/or enforcing judgments, alteration or discontinuation of economic reforms, military conflicts, and China’s dependency on the economies of other Asian countries, many of which are developing countries. The risks of investing in securities of foreign issuers can include fluctuations in foreign currencies, political and economic instability, and foreign taxation issues.

The performance of an investment concentrated in issuers of a certain region or country is expected to be closely tied to conditions within that region and to be more volatile than more geographically diversified investments.

Purchasing Managers Indexes are based on monthly surveys of companies worldwide, and gauge business conditions within the manufacturing and services sectors.

The Economic Sentiment Indicator is a composite indicator made up of five sectoral confidence indicators with different weights: industrial confidence indicator, services confidence indicator, consumer confidence indicator, construction confidence indicator and the retail trade confidence indicator.

The Economic Uncertainty Indicator is a weighted average of the answers of business managers/consumers to a question asking them how difficult it is to make predictions about their future business/financial situation.

The New York Fed’s Global Supply Chain Pressure Index (GSCPI) integrates a number of commonly used metrics with an aim to provide a more comprehensive summary of potential disruptions affecting global supply chains.

The World Container Index, assessed by Drewry, reports actual spot container freight rates for major East-West trade routes. The index consists of eight route-specific indices representing individual shipping routes and a composite index. All indices are reported in USD per 40-foot container.

The Survey of Consumers is a monthly telephone survey conducted by the University of Michigan designed to assess US consumer expectations for the economy and their personal spending.

The Baltic Dry Index provides a benchmark for the price of moving major raw materials by sea.

The Freightose Baltic Index: Global Container Freight Index is based on aggregated and anonymized real-time business data from global freight carriers, freight forwarders, and shippers.

Yield spread is the difference between yields on differing debt instruments, calculated by deducting the yield of one instrument from another.

The yield curve plots interest rates, at a set point in time, of bonds having equal credit quality but differing maturity dates. An inverted yield curve is one in which shorter-term bonds have a higher yield than longer-term bonds of the same credit quality. In a normal yield curve, longer-term bonds have a higher yield.

The opinions referenced above are those of the author as of April 4, 2022. These comments should not be construed as recommendations, but as an illustration of broader themes. Forward-looking statements are not guarantees of future results. They involve risks, uncertainties and assumptions; there can be no assurance that actual results will not differ materially from expectations.