



WEEKLY ECONOMIC COMMENTARY

This Week's Economic Review and Outlook

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Weekly Economic Commentary | Week of January 22, 2018



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BEIGE BOOK: WINDOW ON MAIN STREET

KEY TAKEAWAYS

- Based on our analysis, the Beige Book continues to deliver a positive view of the U.S. economy.
- The Beige Book Barometer rose to +62, consistent with the average of +64 for 2017.
- Weather-related words declined in January, while references to tax reform rose.

BEIGE BOOK SUGGESTS CONTINUED MODERATE ECONOMIC GROWTH

The latest edition of the Federal Reserve's (Fed) Beige Book, released Wednesday, January 17, 2018, continued to deliver a positive view of the U.S. economy. The Beige Book is a qualitative assessment of the domestic economy and each of the 12 Fed districts individually, released once per year, ahead of each Federal Open Market Committee (FOMC) meeting--the next of which is set to take place from January 23-24, 2018. We believe that the Beige Book is best interpreted by measuring how key words change over time. The qualitative inputs for the Beige Book Barometer (BBB) are collected in the weeks prior to January 8, 2018.

SENTIMENT SNAPSHOT

We created our proprietary Beige Book Barometer (BBB) [Figure 1] to evaluate the sentiment behind the entire Beige Book. The BBB is a diffusion index measuring the number of times the word "strong" or its variants appear in the Beige Book less the number of times the word "weak" or its variants appear. When the BBB is declining, it suggests that the economy is deteriorating; when it's advancing, it suggests that the economy is improving.

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BEIGE BOOK BAROMETER CONTINUES TO SUGGEST MODERATE GROWTH

● Number of Times “Strong” (and Variants) Is Mentioned Minus Number of Times “Weak” (and Variants) Is Mentioned



Source: LPL Research, Federal Reserve 01/22/18

In January 2018, the barometer climbed from a November reading of +53 to +62, close to the +64 average for all of 2017. The number of weak words declined, nearly hitting a low of -10 in November 2017, with most of the improvement [Figure 2]; meanwhile, strong words remain well off the peak hit in the middle of 2015. History has been sufficient to indicate steady expansion as long as weak words are low, with a spike in strong words often indicating weakness.

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WEAK WORDS REMAIN NEAR CYCLE LOW

● Strong Words ● Weak Words



Source: LPL Research, Federal Reserve 01/22/18

How They Work: Beige Book and Beige Book Barometer

The Beige Book compiles qualitative observations made by community bankers and business owners about economic (lending conditions, nonresidential construction, prices, tourism, wages) and banking (lending conditions, loan demand, loan quality) conditions in 12 districts (Boston, Kansas City, New York, Philadelphia, etc.). This local color that makes up each Beige Book is compiled by on

rotating basis--the report is much more "Main Street" than "Wall Street" focused. It provides an excellent window into the economy using plain, everyday language. The report is prepared eight times per year, ahead of each of the eight FOMC meetings. 31--February 1, 2017.

The Beige Book Barometer is a diffusion index that measures the number of times the word "strong" or its variations appear; when the Beige Book Barometer is declining, it suggests that the economy is weakening. When the Beige Book Barometer is rising, it suggests that the economy is improving.

HURRICANE IMPACT DECLINING, TAX REFORM GETTING ATTENTION

The United States felt the devastating impact of Hurricane Harvey in late August, and Hurricane Irma in early September. The number of 4 or stronger magnitude hurricanes have made landfall within the country in the same year. The hurricanes remain an important factor in rebuilding provides a small boost to the economy, but the attention given to the economic impact has slowly declined. The word "strong" appeared in the Beige Book 65 times in October, 37 times in November, and 15 times in the most recent version. Meanwhile, "weak" appeared 4 times in the November Beige Book and 23 times in the most recent edition, as Main Street tries to navigate the new tax law.

WATCHING WAGES & INFLATION

Market participants continue to monitor inflation and wages closely, as they gauge not just when, but how far and how long it will last. Each Beige Book provides an economy-wide assessment of wages and prices.

On wages, the January 2018 Beige Book observes:

Most Districts cited on-going labor market tightness and challenges finding qualified workers across skills and sectors. Several Districts noted elevated demand for manufacturing and construction labor. Wages increased at a modest pace.

On price pressures, the January 2018 Beige Book observes:

Most Districts reported modest to moderate price growth since the last report...Reports of pricing pressures were mixed. Several Districts noted increases in manufacturing, construction, or transportation input costs. Firms in some Districts reported modest price increases and there were reports of rising home prices. Retailers in some Districts reported modest price increases and there were reports of rising home prices. Agriculture and energy commodity prices were mixed.

We monitor wage and price pressures via our Inflation Barometer, which is a simple count of the number of times the words "shortage," "widespread," and "rising" appear in the Beige Book. Consistent with the moderate price growth noted in the Beige Book, the Inflation Barometer related to inflation climbed modestly in January to +121, nearly matching the 2017 average of +122 [Figure 3]. The current level is below this level following a brief spike to +136 in July. The current level remains meaningfully above the 2015-2016 average, but the impact on price levels remains modest.

CONCLUSION

The level of the January 2018 Beige Book Barometer has been historically associated with continued economic expansion. The level is near expansion lows, while positive words held steady. The attention given to Hurricanes Harvey and Irma has declined significantly since the impacted regions, while Main Street exhibited an overall positive response to the new tax law. The current level is below this level following a brief spike to +136 in July. The current level remains meaningfully above the 2015-2016 average, but the impact on price levels remains modest.

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