February 2021

Trends Report

ITR Economics

Executive Summary

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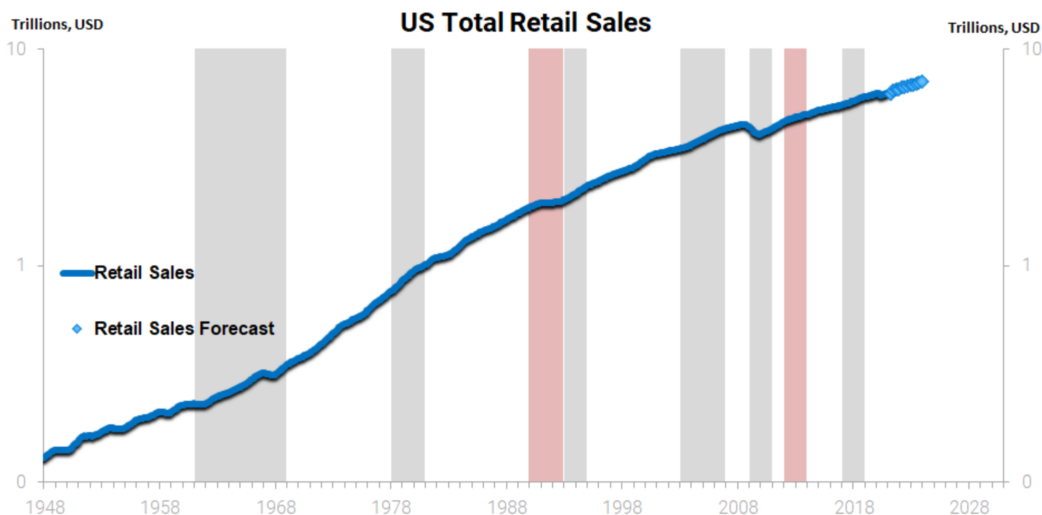
Recovery, Politics, and Inflation: What You Need to Know

ECONOMIC OVERVIEW

The economy is progressing in its recovery. The data reported out over the last month did not hold any negative surprises. The trends are moving as anticipated, which in many cases means ongoing rise. The ascent in Capital Goods New Orders turned significantly higher in the rates-of-change. The New Orders tally for the last three months is 13.6% above the same three months in 2019. The New Orders 3MMT is at record levels and, by this tally, recovery from COVID is complete. Consumers are happy, and businesses are buying capital equipment. Signals from the leading indicators and other variables affirm that additional rise awaits in 2021. You don't want to be on the lagging edge of this trend if your markets are tied to these trends. It could cost you in terms of price, availability, and opportunity. Of course, there are sectors of the economy that are lagging the recovery in GDP, retail sales, single-unit housing, etc. Sectors within nonresidential construction, travel, lodging, and entertainment will likely not catch on to the rising trend until late 2021 or during 2022.

THE ALIGNED GOVERNMENT IN WASHINGTON

The fact that we have one political party controlling the executive and legislative branches of the federal government is not cause for us to change our outlook for 2021-2024. The post-WWII record of retail sales (retail sales ultimately drive the economy) is depicted by the blue line on the chart below. The grey-shaded areas show the times when either the Democrats or the Republicans controlled both the Oval Office and Congress. There is no discernible, predictable ramification on retail sales from the alignments. What this tells us is that we do not need to fear retail sales altering away from the current recovery trend because of the politics, either by accelerating away or falling below trend. Individuals may feel one way or the other, but the macroeconomic trend, which reflects the opportunities within the economy, stays the course.



The chart also shows two periods shaded in red. Those are the two most recent times individual income taxes went up. We included this view because there is concern that the aligned politics of the government means an increased probability of higher taxes. That may be the case; however, the last two instances occurred under President George H.W. Bush and President Barack Obama, and neither had an aligned Congress to work with. Note that the period of change in taxes had no demonstrable impact on the retail sales trend under Obama. The retail sales trend leveled off under the Bush administration, but we had forecasted that was going to occur a year before it actually did and before "Read my lips – no new taxes!" became a thing. Will some microeconomic retail sales trend shifts occur? Potentially yes. Do we have to be concerned about a retail-sales induced recession because of a tax increase? The record suggests we don't. That does not mean we are proponents of higher taxes or think that tax cuts are some sort of elixir for the economy. The analysis simply means that we can effectively plan for our business's future regardless of the tax climate in most cases by focusing on the business cycle, not the political cycle.

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INFLATION AND THE LONGER-TERM OUTLOOK

ITR Economics' thinking about the economic outlook during the 2030s is predicated on four primary trends. The prospects for each of these trends being problematic for the US economy (indeed the global economy) are largely unchanged, although COVID-19 and its attendant ramifications have, in some instances, magnified these causal factors. The four causal trends from our perspective are:

- Demographics
- Health Care Costs
- Inflation
- US National Debt

There is an understandable tendency to assume that some combination of the increase in government debt and monetary stimulus, both of which are significant in size and scope, will lead to inflation, with all of its attendant ills. If significant inflation were to occur in the near term, it could pull in the projected 2029 major business cycle high. However, we are not anticipating the kind of inflation that would cause interest-rate rise to problematic levels in the near term, especially in regard to the CPI-indicated inflation rate. When inflation gets high, it systemically distorts macroeconomic behavior; however, it does not appear likely to occur soon enough that we need to change the timeline.

It takes more time than many people realize to create the macroeconomic distorting kind of inflation folks seem to be worried about. We don't expect to see the broad-based inflation pressures really start to build until 2024 or later.

The historical record shows an economy doesn't go from essentially nonexistent inflationary pressures to broad-based inflation in a matter of quarters or even a year. This is especially likely to be true when the factors driving the velocity of money remain in the "off" position and asset price bubbles develop in lieu of the broader CPI-type inflation. What is happening in the single-family home real estate market and in stock prices is apparently where most of the near-term "monetary pressure" is evident. It is more likely that a diminishing role for monetary policy as a stimulus policy tool in the intermediate years and an increased propensity for spending by the federal government will set the stage for more of the systemic inflation issues that will tie in with the 2029 high.

Running a business in the "in-between" of higher CPI inflation being out in the intermediate-term future but with rising input prices in this cycle means leaders are going to be put to the test to grow EBITDA along with the top line. Investing in efficiencies, differentiation, economic moats, strategic acquisitions, and continuous training of our labor inputs become crucial to our bottom lines through at least the next three to four years.

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US Computers & Electronics New Orders

Billions of Dollars, NSA

HIGHLIGHTS

- The New Orders 12MMT was up 4.8% for 2020
- We expect Phase B, Accelerating Growth, to extend into late 2021
- Rising consumer demand bodes well for New Orders

FORECAST

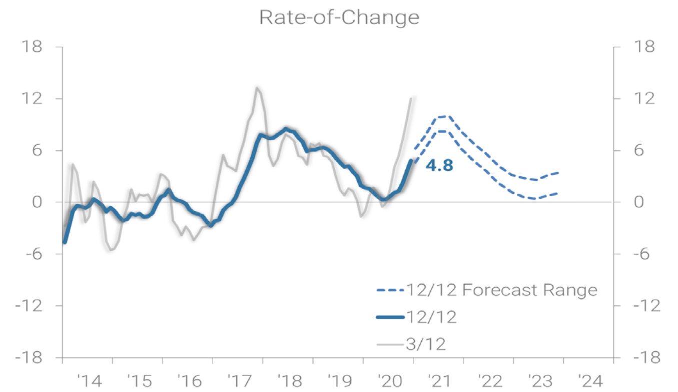
	12/12	12MMT
2021:	7.2%	$319.3
2022:	2.2%	$326.4
2023:	2.3%	$333.9

OVERVIEW

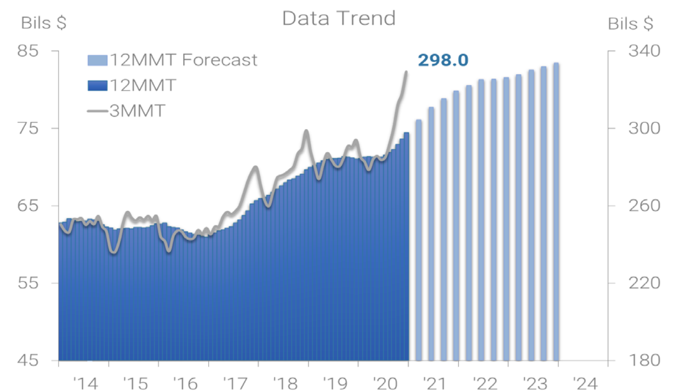
Annual US Computers and Electronics New Orders totaled $298.0 billion in 2020, up 4.8% from the 2019 level. The third-quarter-to-fourth-quarter increase was the strongest in 15 years, and the quarterly growth rate was at 12.0%. These are positive signals for further New Orders rise in at least the near term. We expect the New Orders 12MMT to rise through at least the next three years, though the pace of rise will slow between late 2021 and mid-2023.

Annual US Single-Unit Housing Starts were up 11.6% for 2020. Low mortgage rates and low for-sale inventories are boosting demand for new housing construction. Consumers who are moving into new homes tend to spend more on home goods ranging from furniture to electronics. Coupled with a growing remote workforce, this will likely boost demand for computers and electronics this year.

RATE-OF-CHANGE



DATA TREND



LINKS

Ask an Analyst

Data Methodology

ITR MANAGEMENT OBJECTIVE

New Orders are accelerating. However, avoid straight-line projections, as the rate of growth will be slowing by late 2021.

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