Macro Pulse™

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Soft Patch or Mount Everest of Weakening Conditions?

In April, the word "du jour" for describing unwelcome economic developments was "transitory." Rising prices, slow employment growth, essentially anything other than the housing slowdown – all were deemed transitory. In May, the preferred descriptor changed to "soft patch." Much like the "green shoots" of 2009, "soft patch" seemed to pop up virtually everywhere. Even the *Financial Times* couldn't resist and wrote "Mr. Bernanke's comments suggest he expects a 'soft patch' rather than a more serious slowdown in the recovery." Michael Pento, senior economist at Euro Pacific Capital, did a brilliant send-up of the term when titling his May 31 blog post "Soft Patch or Quicksand?" Actually, Pento was clever a couple of times in May, as he also turned the phrase "Mount Everest of weakening economic data" to describe the current situation.

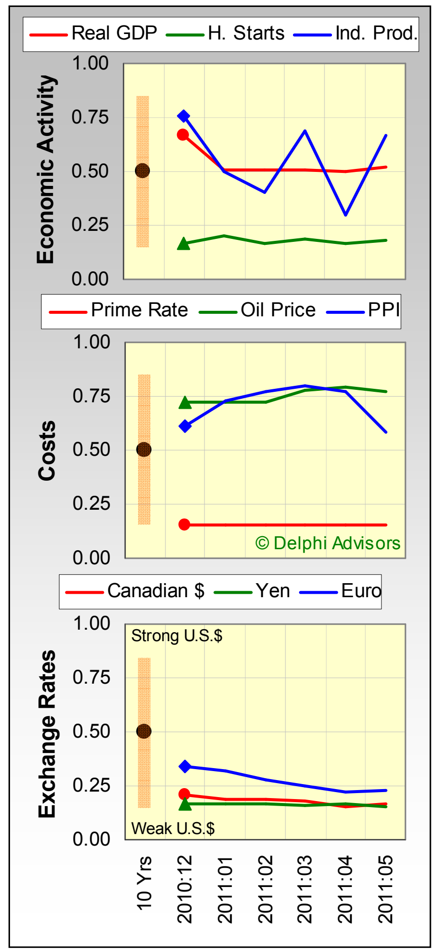
One of the most obvious pieces of data contributing to that Mount Everest of data was the May employment report showing the creation of only 54,000 non-farm jobs, and an increase in the unemployment rate to 9.1 percent. After taking into account downward revisions that erased 39,000 jobs from the March and April employment estimates, the May report added only 15,000 jobs on net.

The employment situation and rising prices are making consumers more pessimistic. The median year-ahead inflation expectation of consumers surveyed by the University of Michigan was 4.1 percent in May. However, the median expectation for increases in family income was nearly zero. In other words, consumers do not expect their incomes to keep up with inflation.

Manufacturing, the belle of the recovery so far, may also be faltering. The fall-off in new orders for non-defense capital goods excluding aircraft, which are a leading indicator for business investment in equipment, was especially troubling. The poor news on durable goods followed reports of a drop in U.S. industrial production in April and other related metrics.

The most recent residential housing figures were also largely negative. For example, the S&P/Case-Shiller 20-city home price index retreated below the low seen in April 2009, confirming a double-dip in home prices across much of the nation. Also, April's new home sales remained barely above the all-time low set in February, and permits fell; lastly, pending home sales retreated to a 7-month low.

Perhaps the current situation will ultimately turn out to be a soft patch, but then again anyone who has operated heavy machinery knows just how easy it is to bury the equipment up to the axles. Unfortunately, with the political parties playing "chicken" over the U.S. debt ceiling, no Treasury buyers apparently willing to take over when the Fed wraps up QE2 at month's end, and oil showing no real signs of becoming cheaper, the economy could also find itself "up to the axles."



Previous six month's behavior of macroeconomic variables indexed relative to their historical 10-year min, max and average (lower and upper ends of the orange bars, and black dots, respectively)

This report is a compilation of articles posted on our website (http://delphiadvisorsmacropulse.blogspot.com/); those articles relate recent economic developments to the U.S. forest products sector in much greater detail. They also provide context for our complete, 24-month forecast, which is contained in the *Economic Outlook* newsletter available through Forest2Market (http://www.forest2market.com/f2m/us/products/outlook). ■