

# Dutta's Monetary Thoughts

This bear is hibernating for the summer

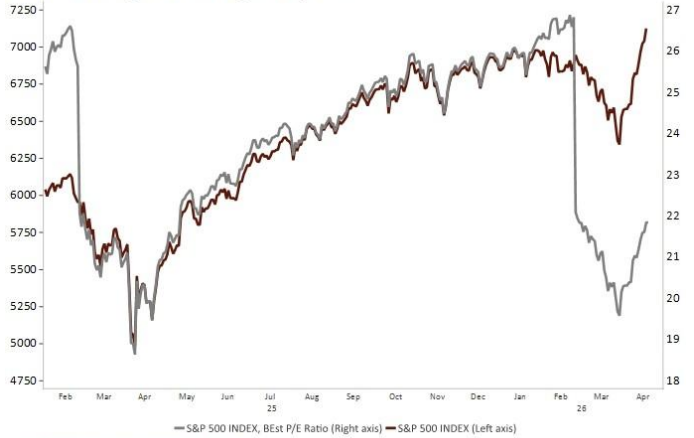
Neil Dutta

## What's changed and what hasn't?

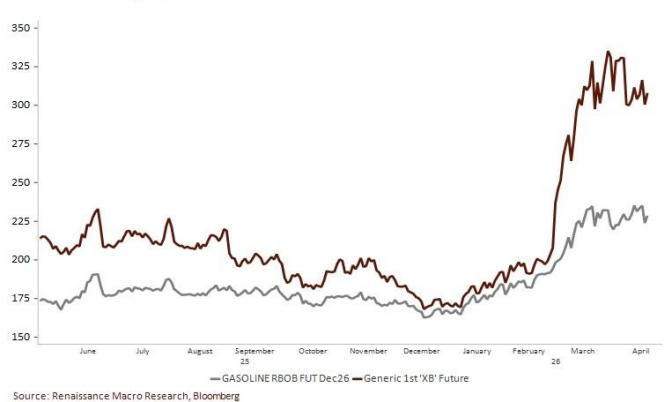
Financial markets are learning to live with higher oil prices. There is still plenty of back and forth and negotiating in public. The Strait of Hormuz still looks closed. My general sense is that the bias for stocks is to move up in the absence of bad news. Multiples will drop when there is bad news and earnings tend to move up over time unless you expect recession. That's broadly what I think the markets are discounting.

For households, I think conditions have improved, but we will still see some lasting damage. Wholesale gasoline prices have eased to \$300, consistent with retail gasoline of roughly \$4.10 per gallon. Futures for wholesale gasoline have eased to \$224, which implies retail gasoline prices slide to roughly \$3.35 per gallon. The US consumes roughly ~137 billion gallons of gasoline per year. At \$0.52/ gallon, that to roughly a \$70 billion annual drag on consumer spending — or 0.3-0.4ppt of disposable income. This is about the midpoint of most estimates on tax refunds.

Markets learning to live with higher oil prices

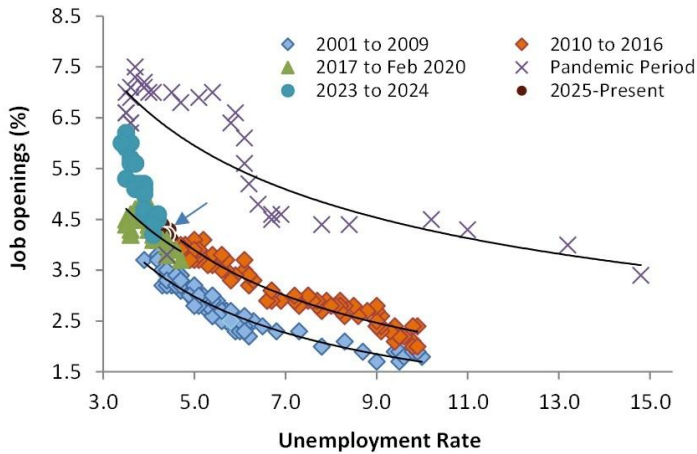


Gasoline futures point to retail relief ahead



**No movement along the curve for a year**

Beveridge Curve

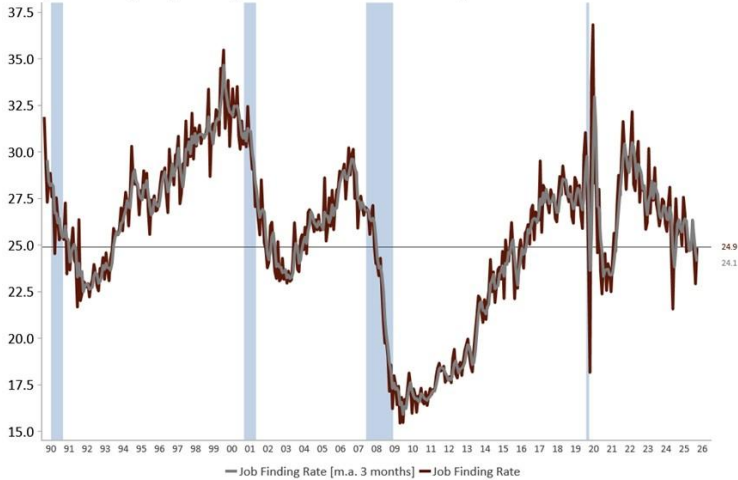


Source: Renaissance Macro Research, Haver Analytics

**Labor market: Stable**

At the margin, I feel somewhat more sanguine on the labor market; conditions seem stable. Indeed, the labor market has been operating along the same part of the Beveridge Curve for a while now. For much of the last two years or so, I have been operating under the assumption that unemployment could rise without an increase in layoffs because job finding rates would slide. Difficulty with job finding would push up unemployment in the same way water draining out of a tub more slowly leads to higher levels of water in the tub, all else equal.

**Can job finding keep sliding without recession at this point?**



Source: Renaissance Macro Research, Macrobond

The good news is that it is difficult to see why the job finding rate gets much worse than it is right now. As our nearby figure shows, job finding rates are about as weak as they were in the early 1990s, early 2000s, and 2008. We're operating close to recession-like conditions as it is; so, we'll likely need to see much weaker growth for job finding to get even worse than it is now. This means the rise in unemployment at this point will have to come from an increase in layoffs. There is no indication that layoffs are climbing. Initial unemployment claims remain low.

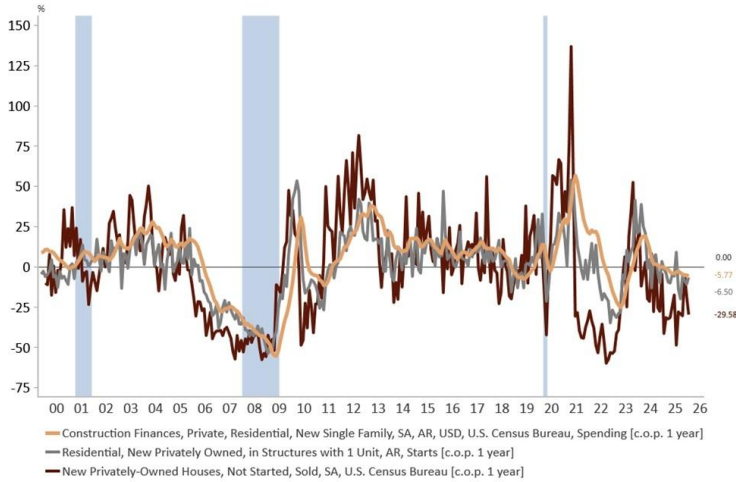
The bad news is that there is not much evidence labor demand has perked up nor is there much evidence that labor incomes are accelerating. Indeed, the balance of risks shows an ongoing slowing in wage growth on the horizon.

**Wage growth indicators signal a steady cooling in labor markets**



I pay especially close attention to Indeed’s Wage Growth Tracker; this measure maps the changes in wages & salaries advertised in job postings on Indeed, controlling for job titles. Wage growth in open positions ought to lead overall wage growth. Next, I follow the HPW Labor Market Tightness Index, which is a weighted average of the quits rate and job vacancies per job seeker. The Employment Cost Index tends to follow both measures.

**Single-family construction to keep sliding**

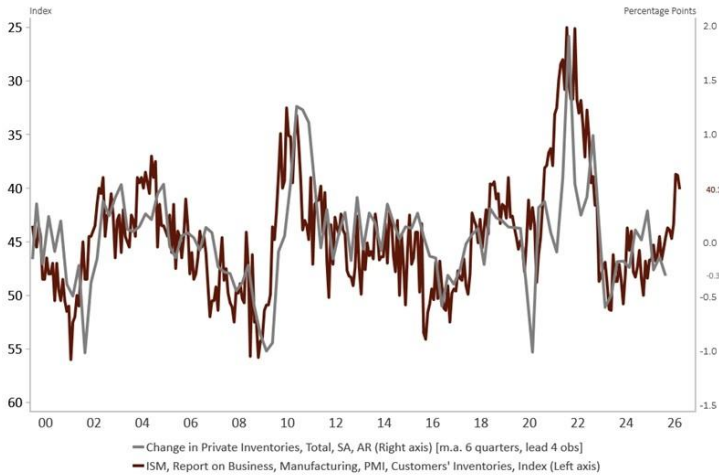


**Push and pull in cyclical areas**

Cyclical areas of the US economy are moving in different directions with manufacturing appearing to pick up with ongoing weakness in housing.

Let’s start with housing first. Residential investment is a function of three factors: (1) home sales, (2) construction, and (3) renovation spending. The good news is that conditions can’t really get much worse in the resale market. The bad news is that construction and home renovation spending is likely to soften. With new home sales weak, there is not much in the pipeline for singlefamily starts and with completions running above starts, assume continued declines in units under construction. On net, expect residential investment to continue cutting US GDP growth into Q3.

**Inventories to be rebuilt**



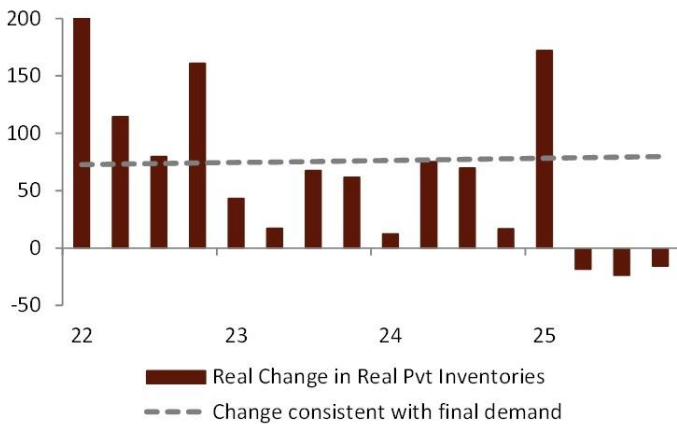
Source: Renaissance Macro Research, Macrobond

**Factories improving**

Manufacturing, on the other hand, is showing marked improvement. Inventories have cut US GDP by an average of 0.6ppt per quarter for the last six quarters. Inventories tend to be a small part of GDP, but account for a large chunk of the cyclical swings in activity. At any rate, as our nearby figure shows, manufacturing purchasing managers have generally said their level of inventories is too low rather than too high. As inventories restock, we should see some pick-up in factory activity.

**Room for inventories to add to GDP**

billions of chained 2009 dollars, annual rate



Source: Renaissance Macro Research, Haver Analytics

If the economy grows at 2.5 percent, its pace since 2023, inventories would need to rise by roughly \$80 billion per year to keep pace with overall sales. Inventories have been running well below this level in recent quarters. Thus, there is reasonable scope for inventories to lift GDP growth in the quarters ahead.

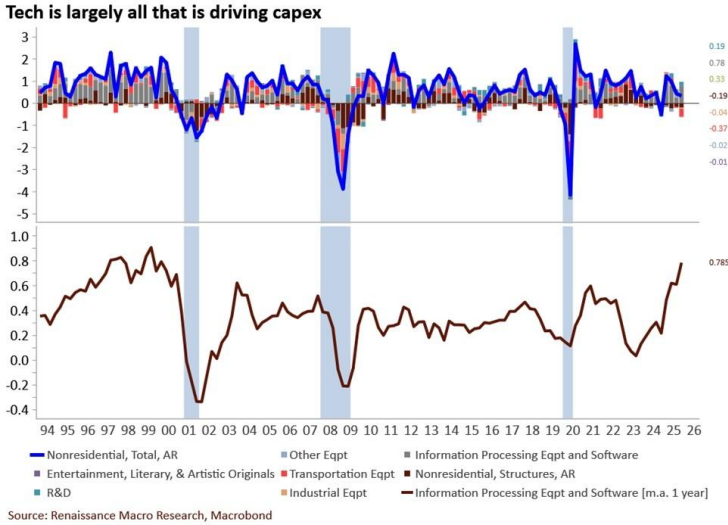
Regional manufacturing surveys have shown sharp improvement in April, but I assume these surveys overstate the magnitude of the rebound quite a bit. After all, manufacturing production is up less than one percent over the last year. The degree of improvement in surveys relative to hard-data might reflect that conditions have been depressed for a while; a modest bounce feels that much better. Either way, for manufacturing up is up.

In short, I'd argue the economy is holding together, but growth is nothing especially exciting with pockets of improvement offset by weakness elsewhere.

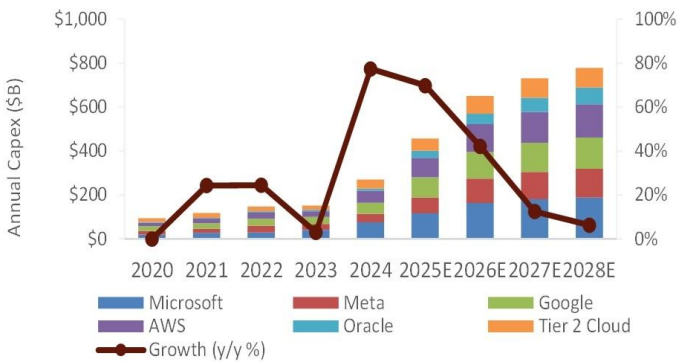
**The downside risk scenario**

To the extent there are meaningful risks, I can see them brewing later this year into 2027. There are three things I am thinking about.

- The US economy is well supported by continued nonresidential business equipment spending thanks to information processing equipment and software. Much of this is driven by an unprecedented AI-related infrastructure buildout.

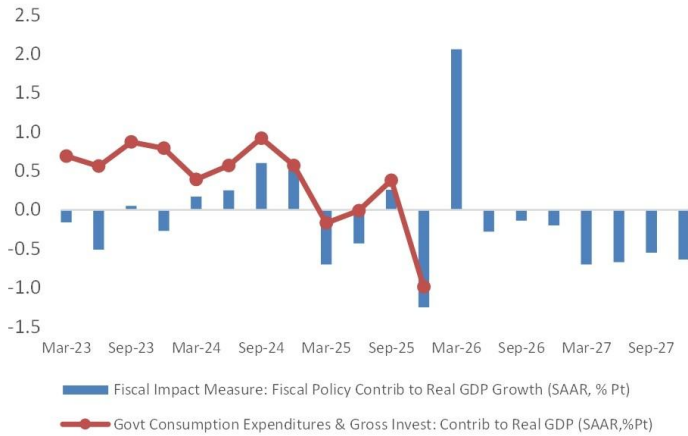


**Hyperscaler capex growth rolls over sharply after 2025**



- Total hyperscaler capex — Microsoft, Meta, Google, AWS, Oracle, and Tier 2 cloud — is projected to reach roughly \$651 billion in 2026, up 42% from roughly \$457 billion in 2025 (itself up 70% from 2024). But the rate of growth is poised to decelerate sharply: consensus estimates show capex rising to roughly \$732 billion in 2027, implying growth slows to about 12%. By 2028, growth slows further to 6%, and by 2029-30 capex growth essentially flatlines near zero before turning slightly negative. Capital spending intentions remain solid across surveys for now, but the deceleration in the growth rate of this spending — from 70% to 42% to 12% to 6% over three years — is worth watching as a potential headwind for equipment investment and GDP growth into next year.

**From tailwind to headwind, especially next year**  
(QoQ % SAAR)



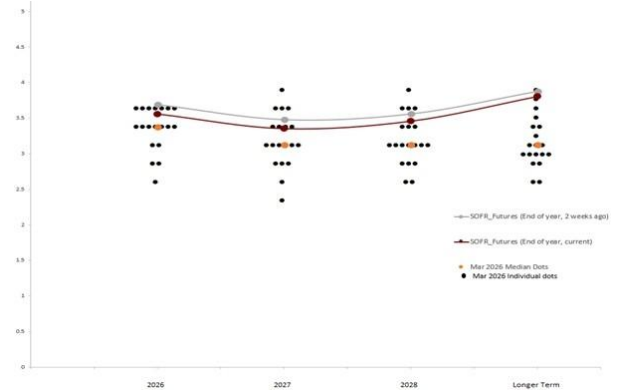
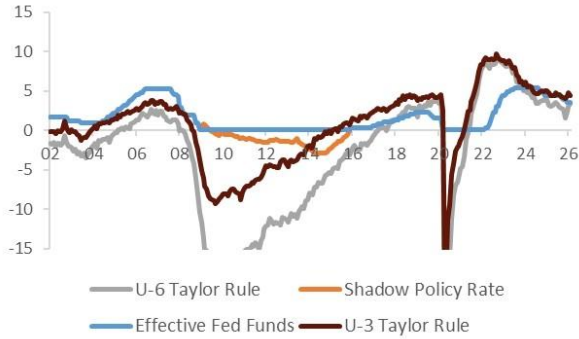
Source: Renaissance Macro Research, Haver Analytics

- Fiscal policy will transition from tailwind to headwind by the end of the year. According to Brookings, fiscal policy is poised to cut US GDP growth by an average of 0.2ppt for the rest of the year with the drag poised to climb sharply in 2027 – 0.6ppt drag on average per quarter.

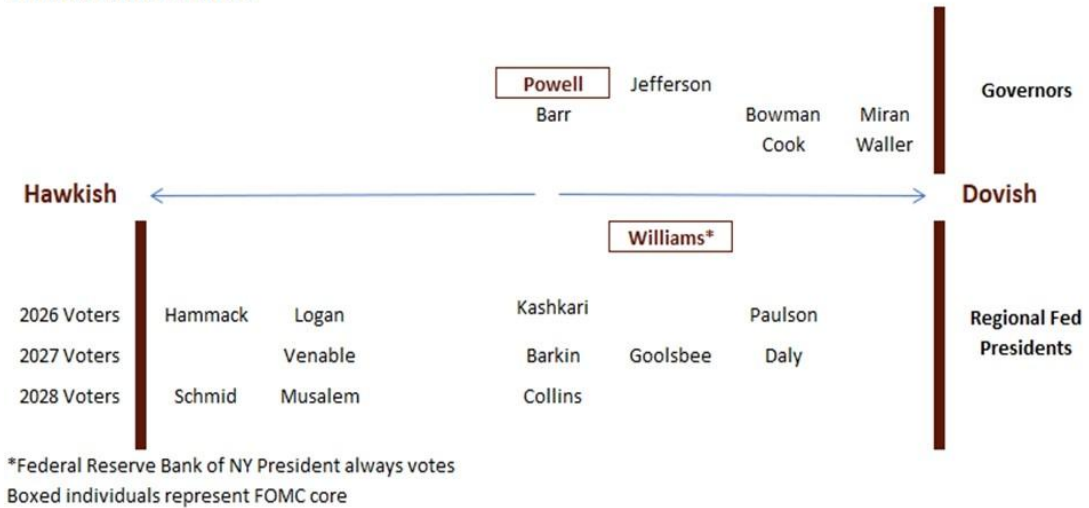
- Lastly, what if the Fed hasn't done much as fiscal policy is tightening? Given the concerns around inflation, there is some risk of the Fed not doing anything even with nominal wage growth cooling over the summer. That represents passive tightening.

I wouldn't press too hard on the bear case right this second, but I think there are a few things I'd be thinking about as the summer progresses. This bear is going into hibernation for the spring and summer.

**Monetary metrics**

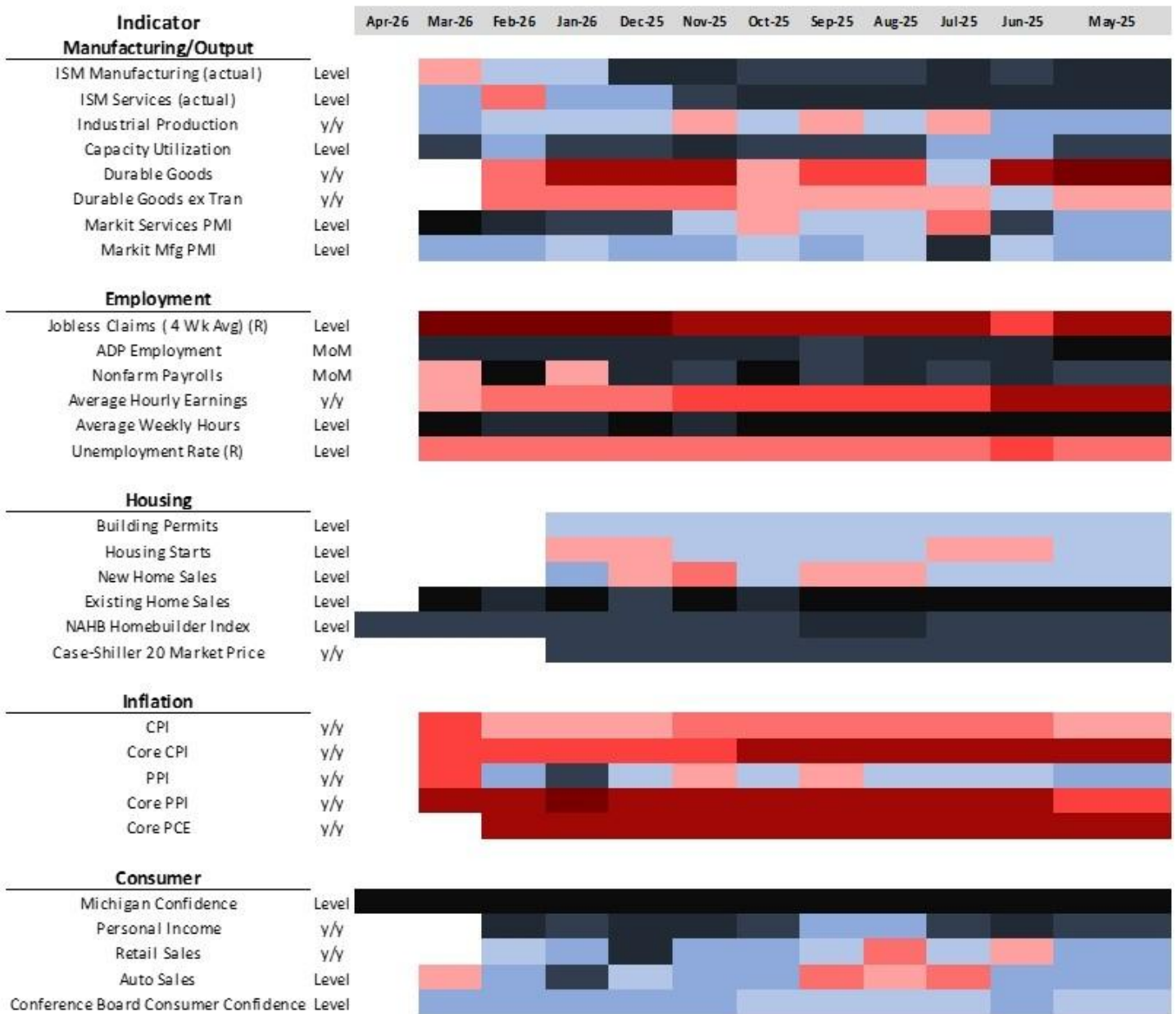


**Hawks and Doves**



FOMC Forecasts	Median				Central Tendency			
	2026	2027	2028	Longer run	2026	2027	2028	Longer run
<b>Change in real GDP</b>	2.4	2.3	2.1	2.0	2.2–2.5	2.0–2.4	2.0–2.3	1.8–2.0
December projection	2.3	2.0	1.9	1.8	2.1–2.5	1.9–2.3	1.8–2.1	1.8–2.0
<b>Unemployment rate</b>	4.4	4.3	4.2	4.2	4.3–4.5	4.2–4.4	4.0–4.4	4.0–4.3
December projection	4.4	4.2	4.2	4.2	4.3–4.4	4.2–4.3	4.0–4.3	4.0–4.3
<b>PCE inflation</b>	2.7	2.2	2.0	2.0	2.6–3.1	2.0–2.3	2.0	2.0
December projection	2.4	2.1	2.0	2.0	2.3–2.5	2.0–2.2	2.0	2.0
<b>Core PCE inflation</b>	2.7	2.2	2.0	2.0	2.5–2.8	2.0–2.4	2.0	2.0
December projection	2.5	2.1	2.0	2.0	2.4–2.6	2.0–2.2	2.0	2.0
<b>Projected policy path</b>								
<b>Fed funds rate</b>	3.4	3.1	3.1	3.1	3.1–3.6	2.9–3.6	2.9–3.6	2.9–3.5
December projection	3.4	3.1	3.1	3.0	2.9–3.6	2.9–3.6	2.8–3.6	2.8–3.5

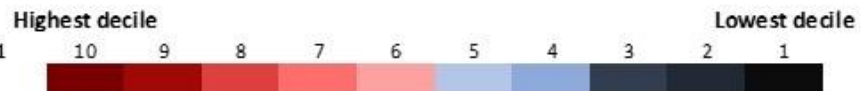
**High frequency data heat-map**



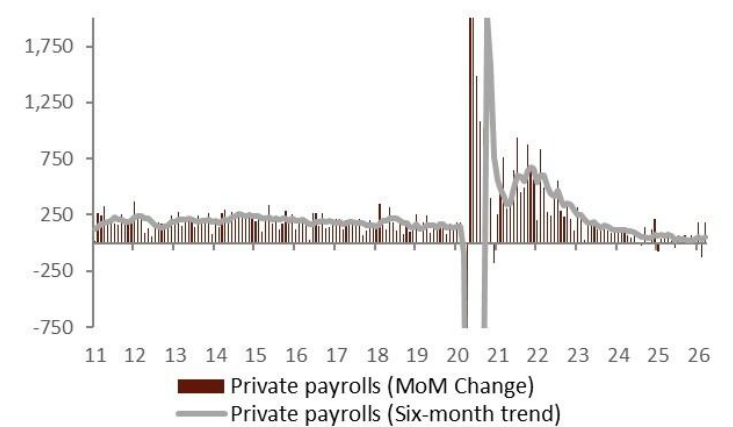
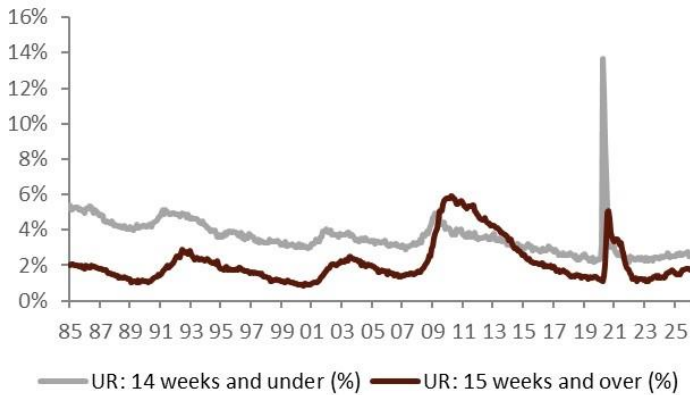
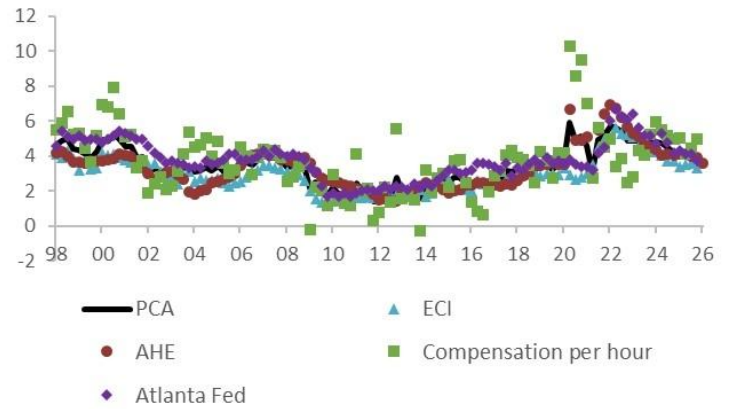
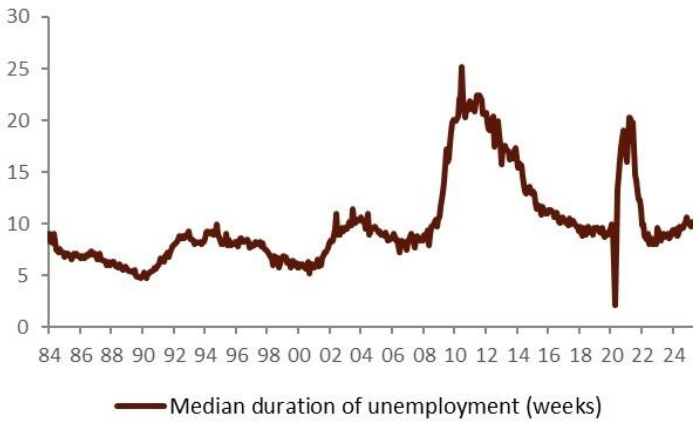
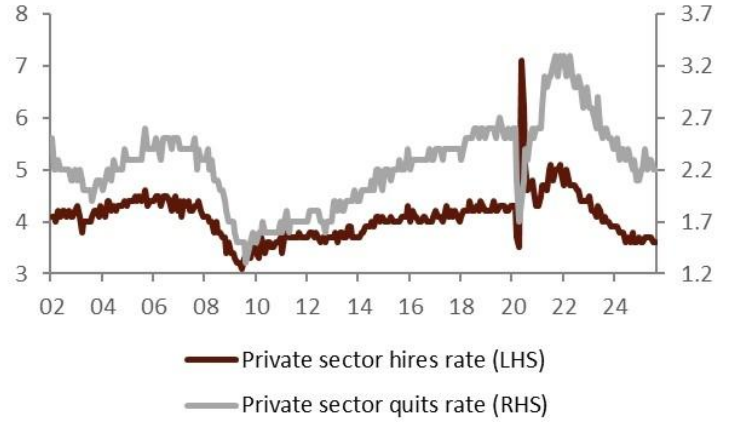
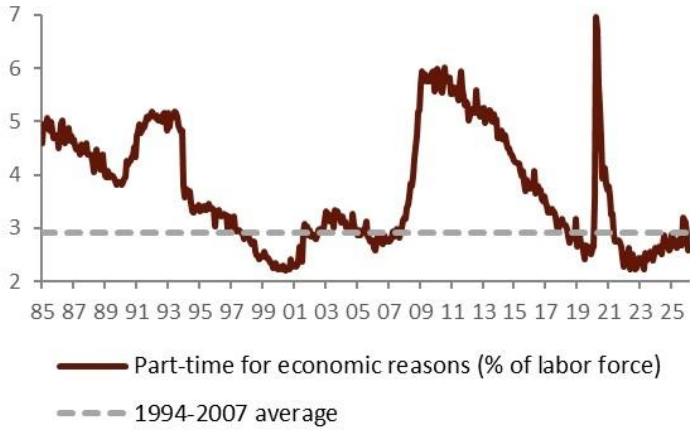
**Notes**

**R - Reverse Formatting**

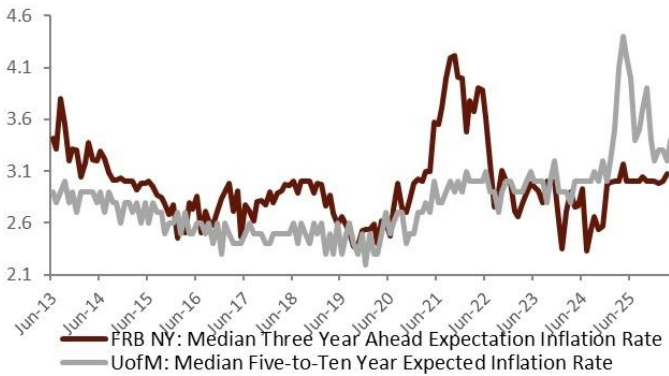
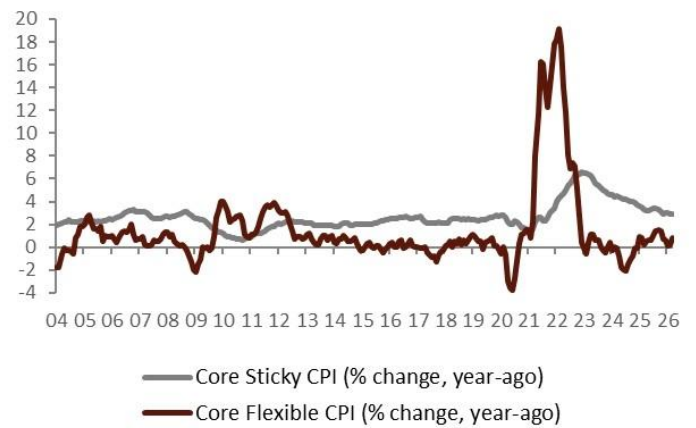
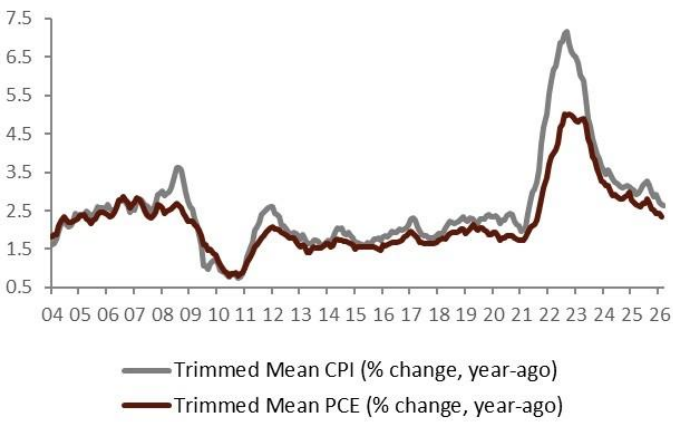
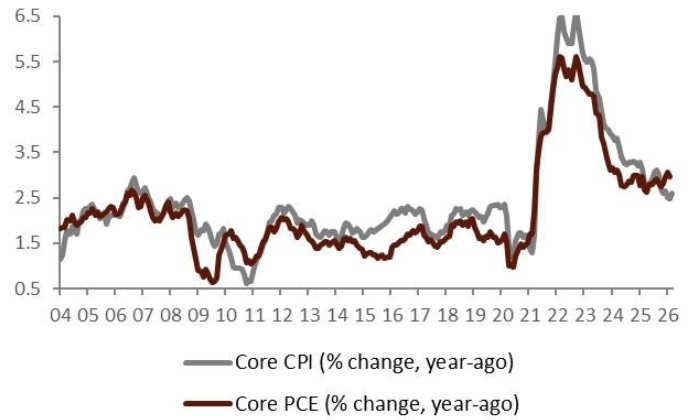
Deciles are based on expanding window since 2001



**Labor market indicators**

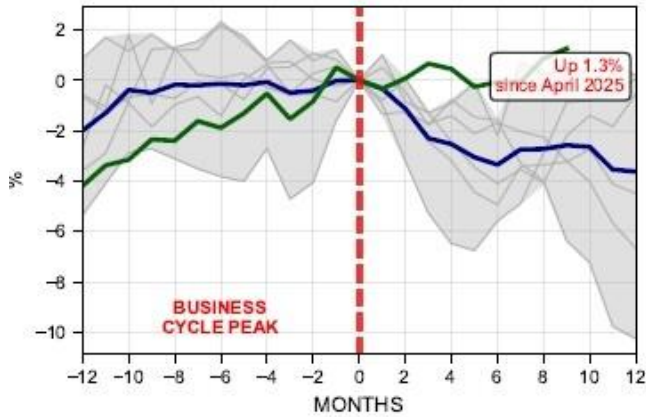


**Inflation indicators**

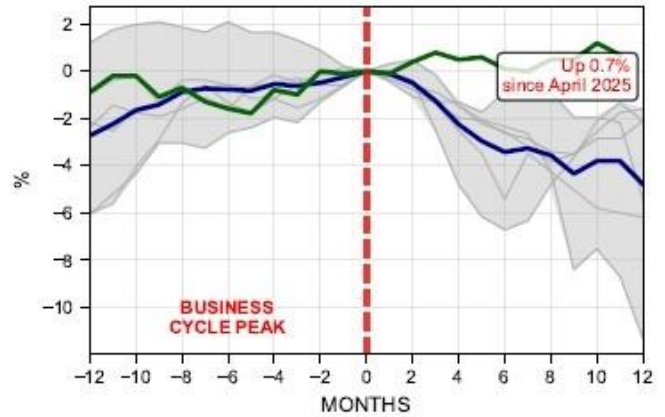


## NBER RECESSION INDICATORS DASHBOARD

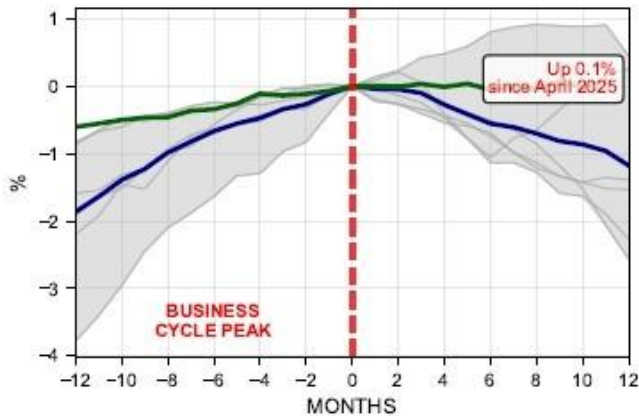
**REAL SALES: MANUFACTURING AND TRADE INDUSTRIES**



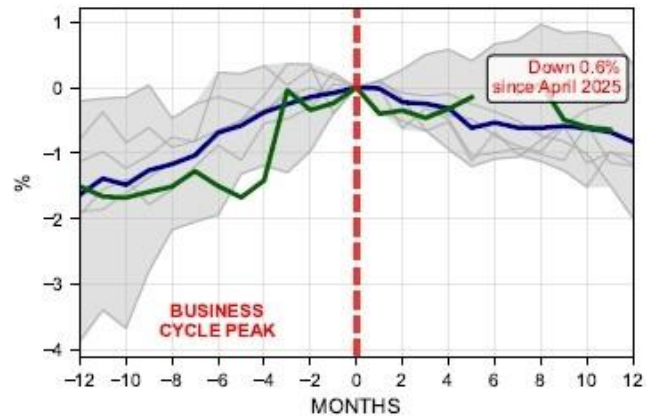
**INDUSTRIAL PRODUCTION**



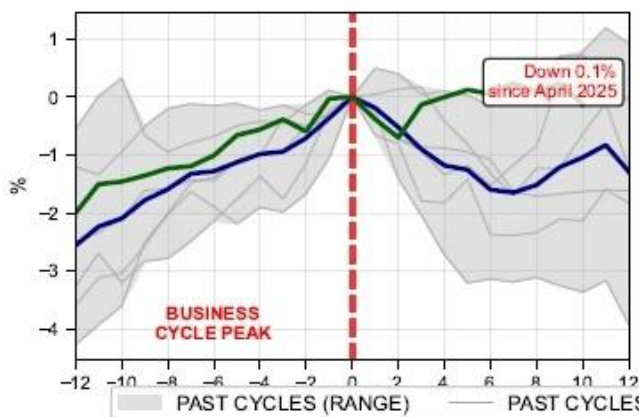
**US NONFARM PAYROLLS**



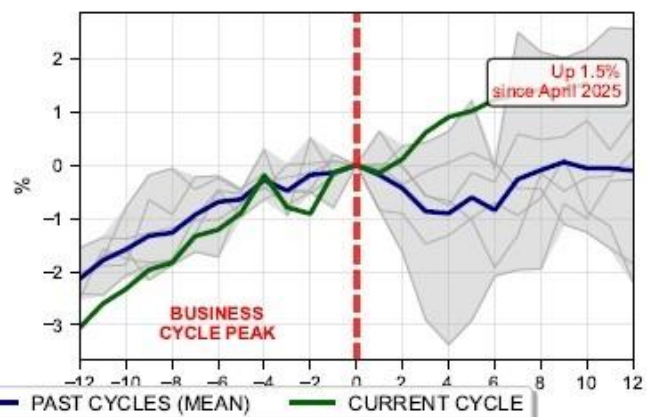
**CIVILIAN EMPLOYMENT**



**REAL PERSONAL INCOME MINUS CURRENT TRANSFER RECEIPTS**



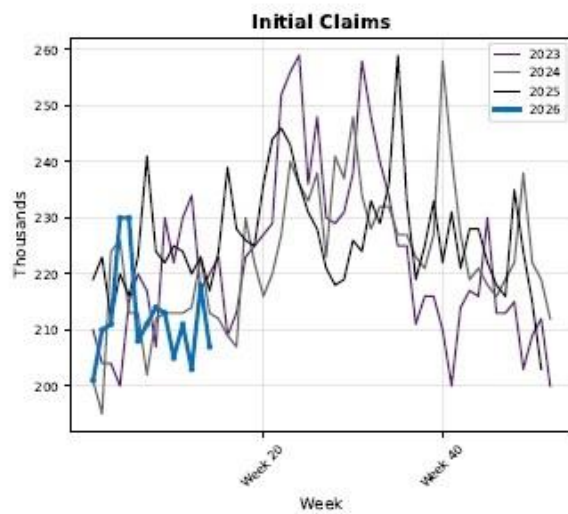
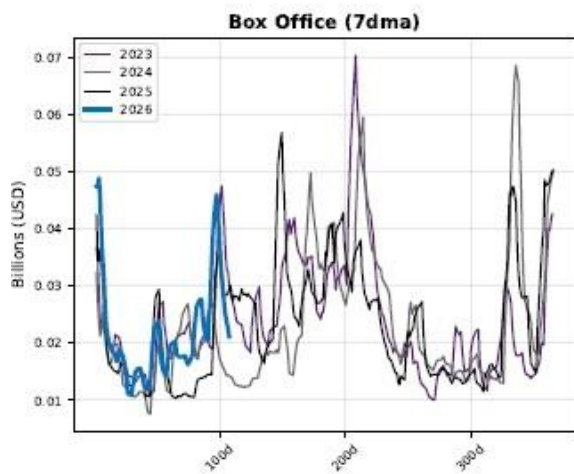
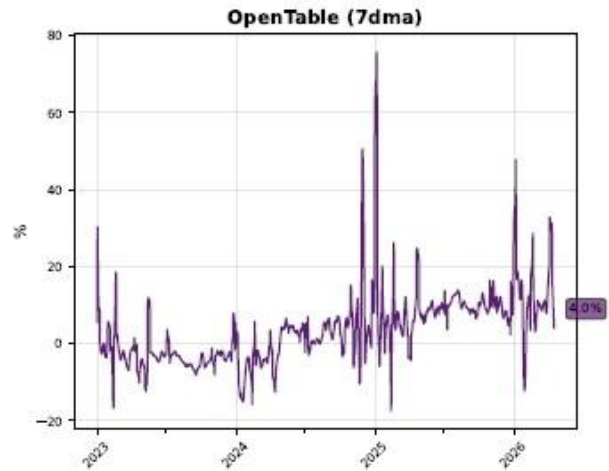
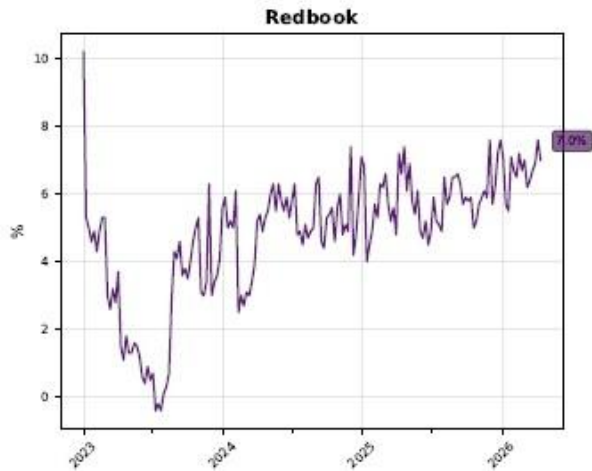
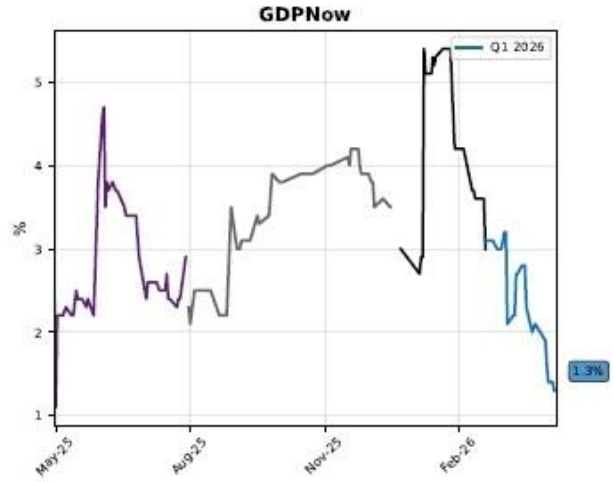
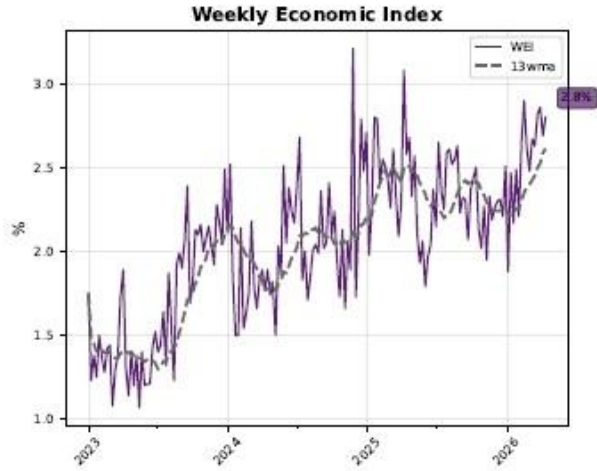
**REAL PCE**



PAST CYCLES (RANGE)
  PAST CYCLES
  PAST CYCLES (MEAN)
  CURRENT CYCLE

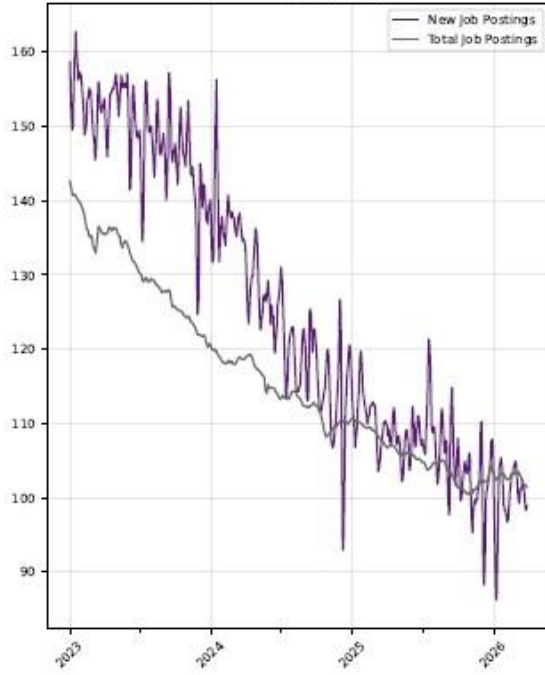
Past 7 cycles excluding Covid-19 period

## High Frequency Economic Dashboard

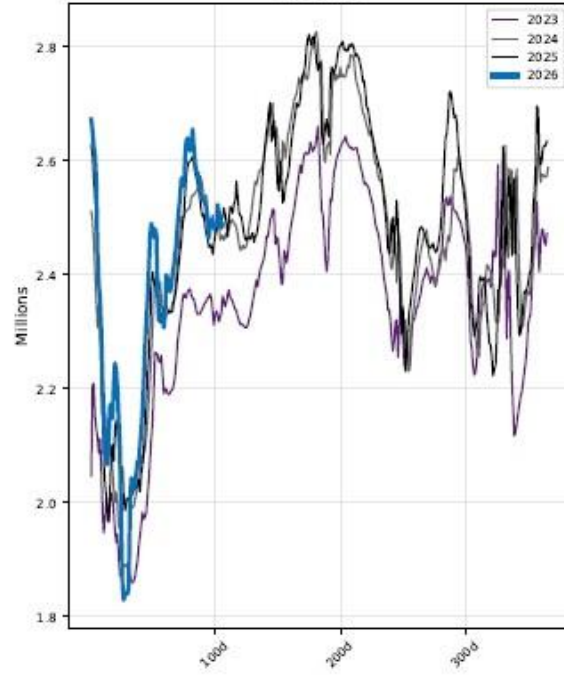


## High Frequency Economic Dashboard

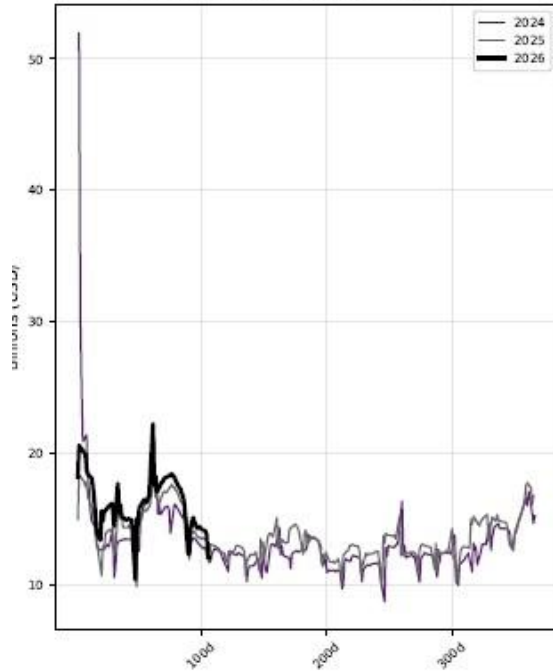
**Indeed Job Postings**



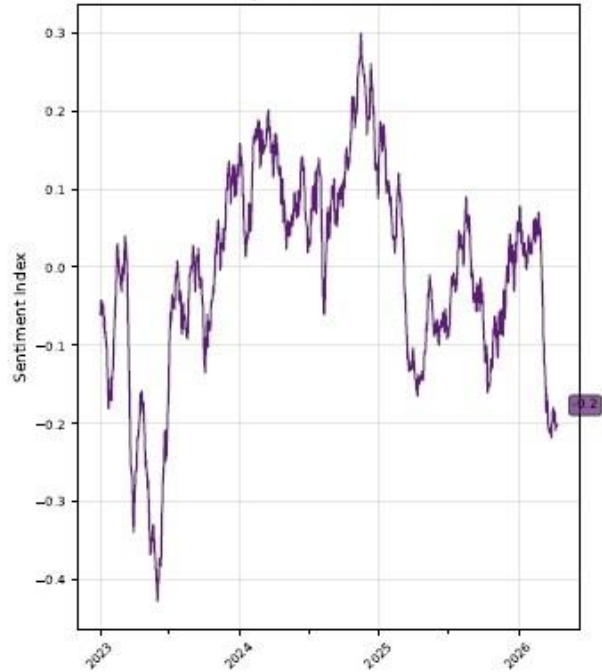
**Air Travel**



**Withheld Income Taxes (10dma)**



**Daily News Sentiment**



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