<u>The Outlook: Feb. 28, 2023</u>

Main Street, looking ahead: from the top down <u>and</u> the bottom up.

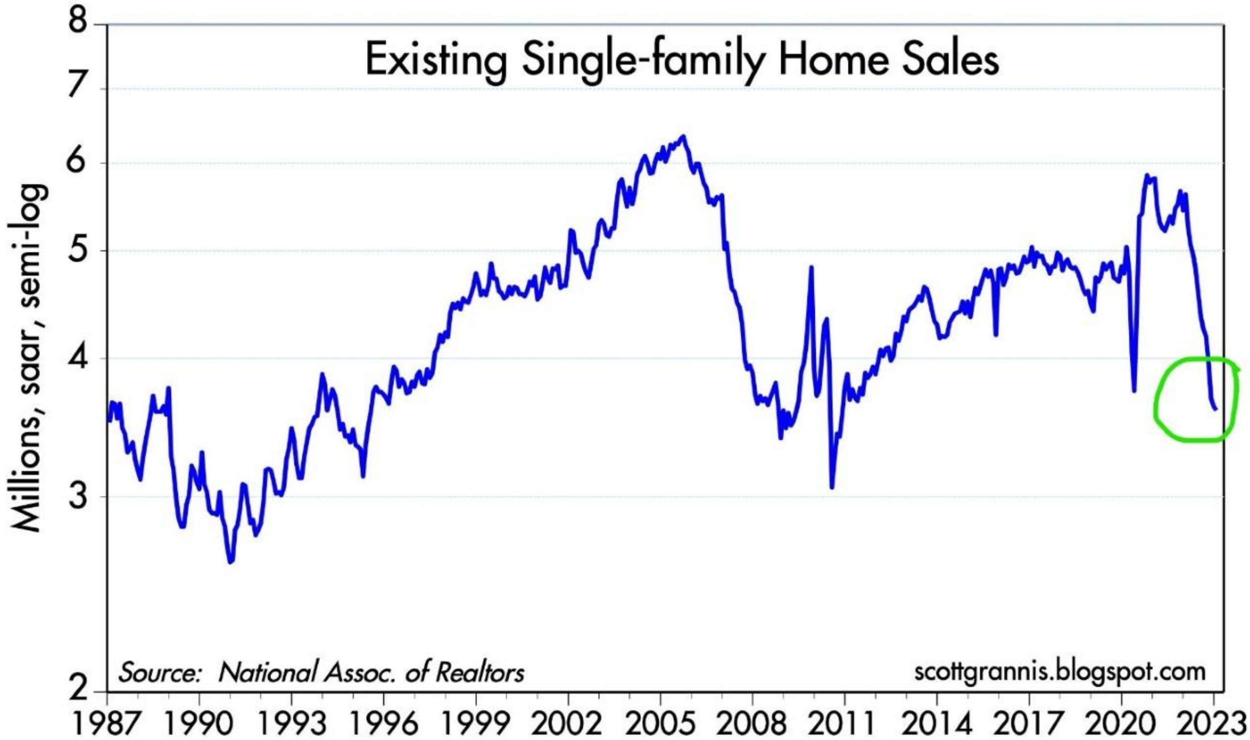
A great question for those of us in the investment world (and every other world) is: "Shall we look at things from the top down . . . or from the bottom up?" Shall we prize the view from the mountaintop, so to speak, focusing on grand economic events and trends . . . or do we think the view from the humblest blocks on Main Street matters more, where we can see what real people and companies are doing as they try to cope with those "grand events"?

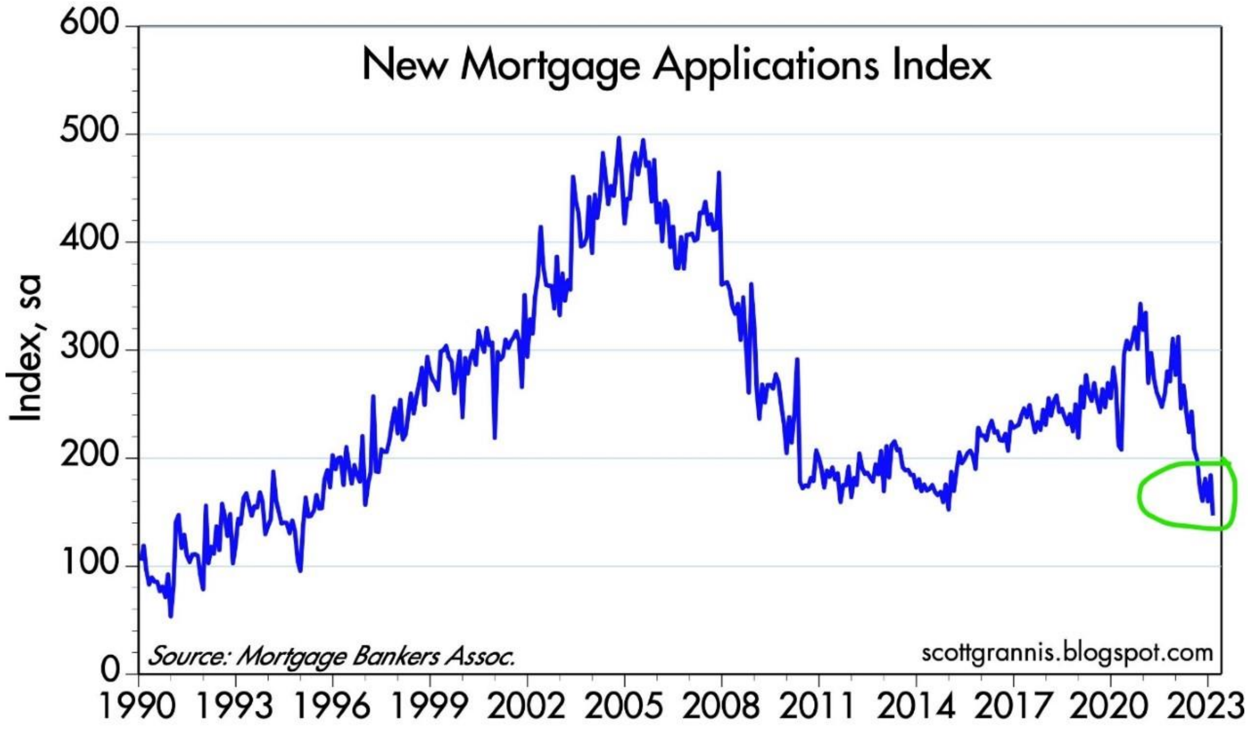
Outlook's answer is never a surprise: "Look at <u>both</u>. See the whole picture, always . . . <u>then</u> come to a judgment."

That principle really matters at this moment. The heart of what's going on these days is that <u>Main Street World is trying to cope with the "grand top-down actions" of central banks around the world</u>: our Fed, the European Central Bank, the Bank of Japan and the Bank of England to name the Big Ones. Main Street is extremely good at coping with problems. "Top-down specialists" (like politicians and central bankers) always underestimate just how well Main Street copes. (Often enough, they comprehend nothing about it.) The Top-Down types are intent, at the moment, on "crushing inflation" by hiking interest rates until Main Street can't cope anymore and shuts up shop in waves, handing pink slips to ordinary Main Street people by the millions. They think that's the only way to kill inflation, essentially because that's what was needed back in 1980 – 82, when inflation spiked to 10-15% and interest rates to 20% before the Monster rolled over and died.

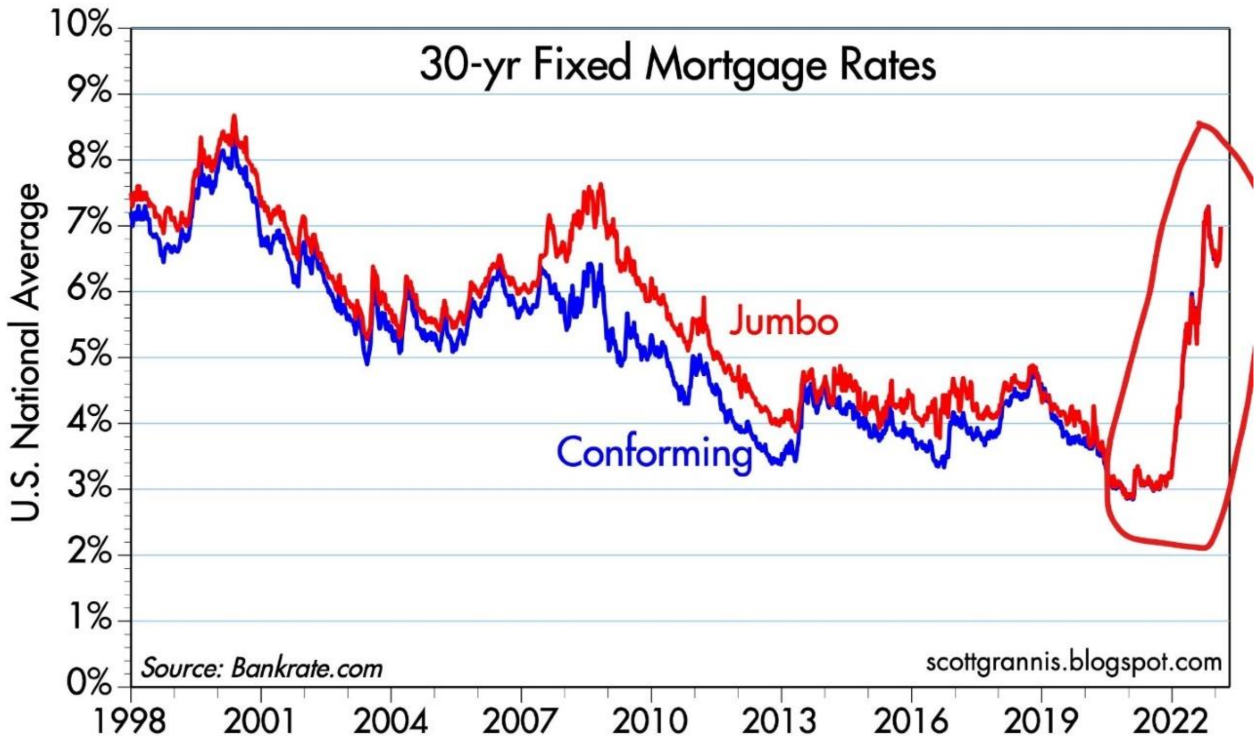
Amazingly, the Inflation Monster never came back to life after dying in the early 80's. Oh, it growled off-stage a few times, but that's where it stayed: off the world stage, never a real problem . . . until now. So the world's eminent Top-Downers think nothing's changed: the only way to kill the Monster is to half-kill Main Street with interest rates high enough to cripple.

And there is some crippling going on for sure . . . right alongside Main Street's usual waves of coping. Let's look at a few pictures, from the invaluable Scott Grannis among others.



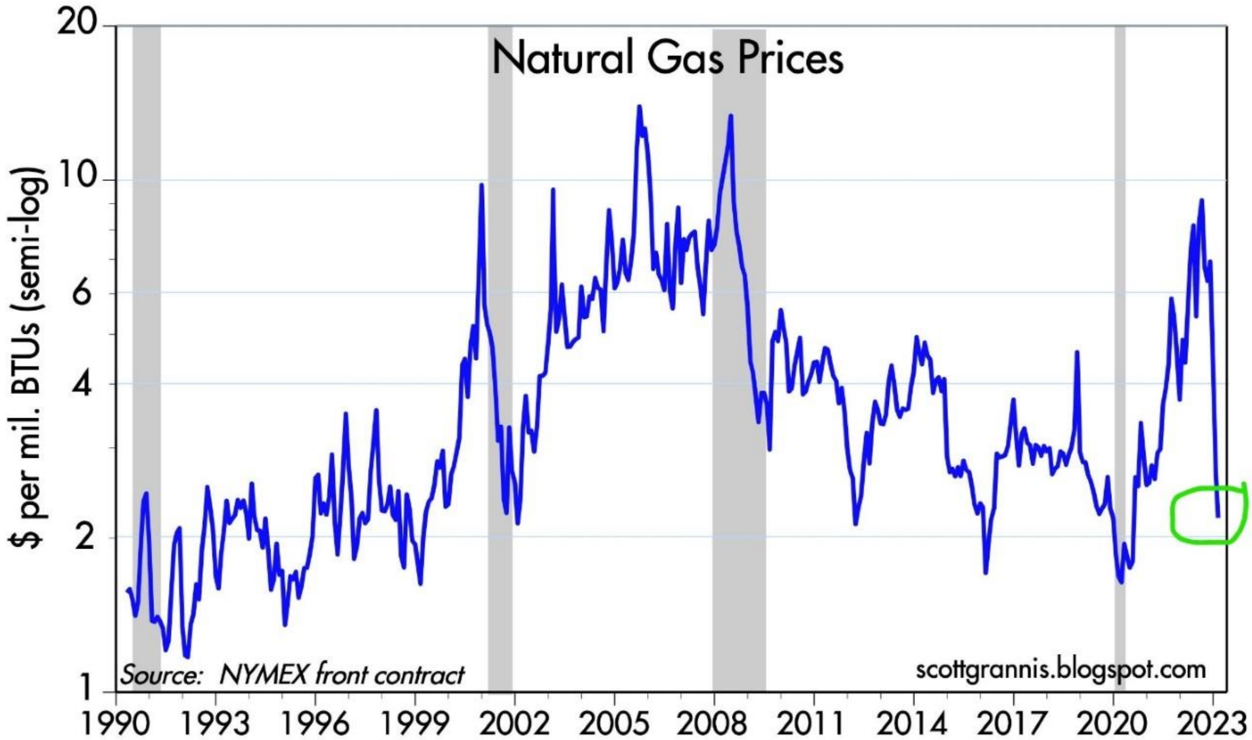


That's a crippled housing market on Main Street, all right. It's not as crippled (yet) as in the Great Financial Calamity of 2008 – 2009, but it's still heading in that direction. Those Top-Down Central Bankers did this (below) . . . and it "worked" if that's the right way to describe a housing industry chopped off at the knees, more or less.

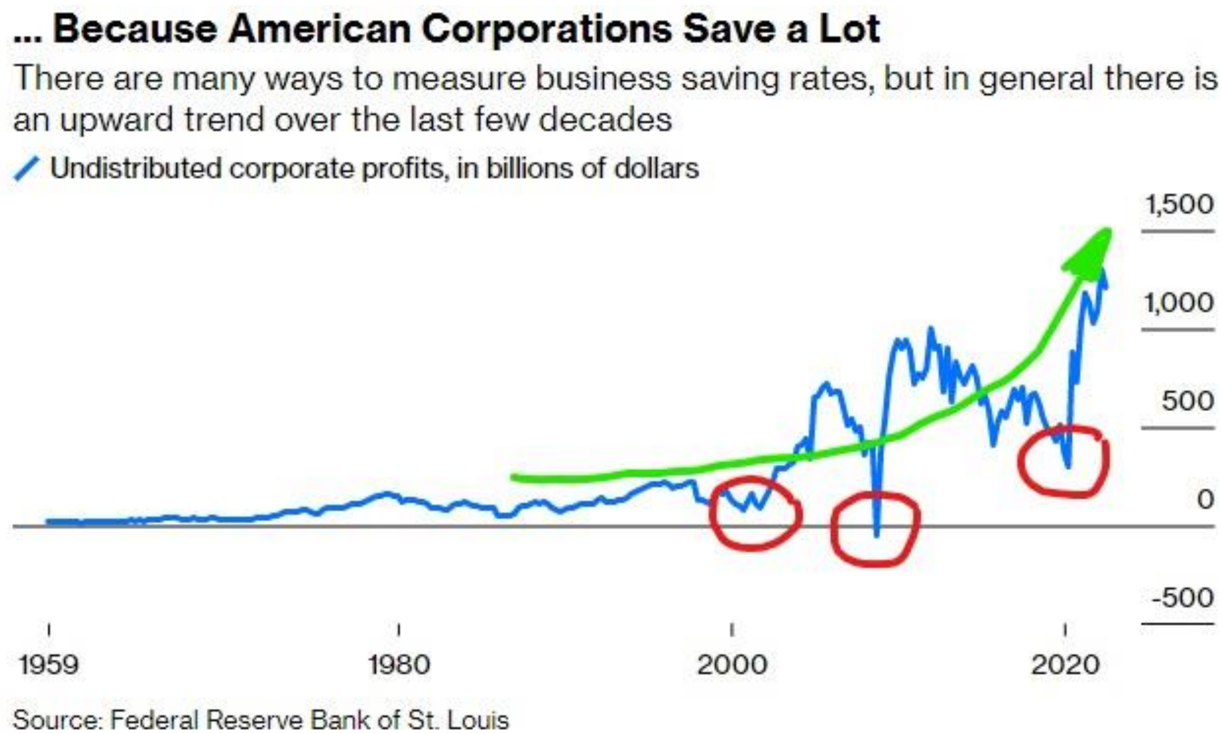


The housing industry works on a few blocks of Main Street . . . but Main Street is vastly bigger than those few blocks. The rest of Main Street has been adapting and coping, week by week and month after month. Some blocks are weaker than others, but none except Housing are crippled yet. Why not?

Well, here are a couple of reasons.



That's an almighty plunge in gas prices in the blink of an eye, economically speaking. Natural gas is factory power all over the world, and a big cost of doing business almost everywhere on Main Street. That green-circled plunge above says, "The cost of power went from "crippling" to "fairly cheap" almost overnight: in Europe, America and much of Asia. Shifting our view to "from the bottom up," uncountable stores, factories and businesses all over Main Street World suddenly found themselves able to keep the doors open and make money, when a few months ago that was looking questionable. Here's another reason Main Street is "coping."



The 3 red circles are the story from the bottom up: 3 "calamities," all frightening . . . and Main Street's completely human reaction: to batten down the financial hatches and shore up their financial muscles so they wouldn't be hurt as badly when the next "red circle" came along. The result? Over 20 years, that swooping-up green arrow: Main Street businesses have a lot more cash on hand than they ever had before.

As we've mentioned once or twice, the more money people have, the less frightened they get by problems—whether they're real problems are the media's daily Nightmares.

Even so, we're still in the same position: Main Street trying to cope, Central Bankers trying to cripple. How's it going to turn out?

At Outlook we're guessing the Central Bankers will go too far. They'll hike rates until more blocks on Main Street seem half-crippled . . . all the while peering through their Coke-bottle spectacles at the stream of passing Inflation reports. That's what Top-Downers do. They almost always "miss the trees for the forest" . . . until they happen to notice that so many trees are sick that the forest has a problem. If we're right, that's not very good for Main Street . . . except that Main Street is so strong it'll merely pause for a bit: not sicken and die, or even get half-crippled. And after the pause it will come roaring back. It always does.

The Central Bankers will go too far . . . but they're going to see something, through those thick glasses, which will eventually make them "pause" themselves.

Of the 52 biggest cities in America, none have seen rents go higher in the past 6 months. Many are already seeing the picture above: falling rents. They are just getting started on the way down, as a river of new rental properties is just beginning to flow into the market. “Rental rates,” remember, drive one-third of the Consumer Price Index. Natural gas costs aren't that big, but they're not trivial either. The same with shipping costs, which have fallen through the floor; and quite a few others.

The Inflation Monster doesn't know it yet, but its big scene is over . . . and it'll be heading off-stage in the not-too-distant future. Main Street just isn't going to be hurt very much by the Top-Downers' near-sighted determination to overdo the rate hikes; and it's going to come roaring back as it always does.

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