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TPWC Market and Economic Update

The Markets

Our dear old favorite index, the S&P 500 Stock Index (SPX), turned in an above-average week, rising 0.96% to close at 3007.39. That puts it still 20 points below where it was about six weeks ago, but on an improving trend after the Chinese government announced a suspension of tariffs on at least some pork and soybean imports in response to President Trump's short-term deferral of tariff increases from the current 25% to 30% on some goods. The week's close puts the SPX up 3.53% from a year ago.

The big market news was a 40.2 basis point rise in the yield of the 10-year U.S. Treasury note to 1.898%, again apparently on the potential for a breakthrough in the trade war. With the 90-day T-bill at 1.961%, the yield curve remains inverted and thereby still forecasting a recession, just not so strongly. West Texas Intermediate crude oil headed in the other direction, declining 3.33% for the week, closing at $54.86.

The Economy

The Commerce Department released its first estimate of what happened in the U.S. economy during the month of August. The good news was that vehicle purchases jumped 1.8% from July in response to lower interest rates and vehicle price cuts as the new model year draws near. Vehicle purchases were the driver in raising retail sales by 0.4% for the month. That was the good news. The other side of the story is that except for consumer vehicle purchases, consumer spending on retail purchases was the same as it was in July.

Looking back at the trailing numbers, retail sales are up a whopping 4.1% from a year ago, demonstrating how much of the last year's GDP growth was driven by consumer spending. Almost exclusively based on consumer spending growth, the U.S. GDP grew at an annualized rate of 3.1% in the first quarter and at a 2% rate in the second. Considering that the jump in vehicle sales is very unlikely to continue, the underlying zero growth in other retail sales for the month caused the consensus for third-quarter GDP growth to be reduced to about 1.8%.

Unemployment remained at 3.7% for August although the creation of new job openings slowed. Overall, the economy continues to function at something approaching its full capacity. In another area where the headline number was different from the underlying "core" figures, the consumer price index (CPI), a widely followed inflation measure, rose only 0.1% in August. The backside to that report was that core consumer prices rose 0.3%, or 3.6% on an annualized basis for the last three months. That report put the rise in core consumer prices up 2.4% from a year ago, but on a trend that seems to indicate higher inflation may be in store for the months to come. Another supporting indicator, real hourly earnings, increased 0.4% in August, a 4.8% annualized rate. For the trailing 12 months, wages were up only 1.5%, so average real wages, probably the main driver of inflation, is accelerating.

The Chairman of the Chicago Federal Reserve Bank and a voting member of the Federal Reserve Board stated in a speech that the sustainable U.S. GDP growth rate was 1.75%. He cited a critical labor shortage, immigration restrictions, and trade policy uncertainty as the limiting factors on U.S. Growth. Separately, the Federal Reserve issued a prediction that 2019 GDP growth would be approximately 2.1% with lower growth forecast for 2020 and 2021.

The National Federation of Independent Businesses announced that 34.4% of its members reported that difficulty in finding qualified workers was limiting growth. That number is a new record with the previous record being 33% during the year 2000, just before the recession that began in 2001. In 2007, just before the Great Recession, the number stood at 27. That abnormally high percentage of businesses reporting difficulty in finding qualified workers is another indicator that the economy is running at or very near to its maximum capacity.

In an oddly contrasting data set, the number of retail stores closing or filing for bankruptcy in the first six months of 2019 has exceeded the number for all of 2018. Anecdotal reports suggest that the labor shortage, excessive debt, expansion that anticipated continuing retail sales growth, and the growth of online shopping were the culprits.

The bottom line is that the economy continues to drive forward at or near-maximum capacity but the growth rate is slowing and weaker businesses are beginning to show signs of stress.

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