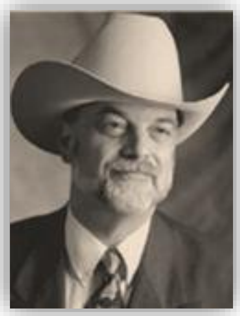

THE PERSONAL WEALTH COACH®

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TPWC Market and Economic Update

The Markets

The S&P 500 Stock Index (SPX) gave another hopeful hop for the week ending on July 22 by rising 2.55% to 3961.63. That close puts the Index up 8.04% from its low of 3666.77 on 6/16, but still down 17.35% from its top in early January. From one year ago it is down 16.88%, but up about 28% from three years ago. Such is the nature of U.S. equity markets over our history. There are ups and downs, but, particularly in the post-World War II stock market, even in the short term down periods, if one looks back a few years there is a clear gain. It is certainly an open question as to whether June 16 will be seen as the bottom of this bear market. There is historical support for seeing that date as the bottom but there are other precedents that suggest at least one more down leg is needed before the final turn. The other equity index we follow, the CRSP Mid-Cap Value Index, closed at 2312.19, up 2.53% for the week and down just under 11% from its top in January. It remains down 4.26% from a year earlier.

The yield on the 10-year U.S. Treasury note continued its downward slide, dropping another 5.6% to 2.761% as the collective wisdom of the bond market participants was that high inflation is indeed a passing thing and both it and interest rates will not rise as much over the next decade as was thought earlier. With the 2-year note at 2.920%, the critical 2 year to 10-year part of the Treasury yield curve remains slightly inverted. That mild inversion is an element in the growing consensus that there is now a 50% chance of a mild recession sometime in the next 18 months or so. Like interest rates, the price of West Texas Intermediate crude oil (WTI) inched downward, slipping 2.7% to $94.92 per barrel. The national average gasoline price for regular followed suit as it declined to $4.41 from over $5.00 a month ago according to the American Automobile Association. Here in Central Texas, the average price at the pump had come down to a delightful $3.84.

The Economy

The focus of the week's economic news remained on inflation, interest rates, and whether the Federal Reserve would plunge the U.S. economy into a recession in its attempts to dampen demand and thereby reduce inflation. There is no shortage of opinion on those subjects, but there are some things that are supported by the facts.

While we hate to use this phrase, it is different this time. The last time we had high inflation, back in the 1980s, the reason for the rise in prices was excess demand. Simply put, a large portion of the U.S. population was getting large wage increases without increasing output. At the same time, the industries supplying the things that were being bought were almost exclusively here in the U.S. and neither output nor productivity were rising. Two things cured the inflation contagion, one in the short-term and the other in the long-term. Short-term, a dramatic increase in interest rates crushed demand. Longer-term, moving industrial production to low-cost areas in Asia increased supply and forced a reduction in prices.

This time around, as the pandemic set in, we had a recession and unemployment surged. It now appears that the three sets of stimulus checks did a fair job of replacing the lost consumer spending power, but consumers suddenly shifted to buying goods rather than services. The pandemic simultaneously caused a supply shortage of those goods from sources in Asia. The other major factor, which is credited with much of the inflation surge this year, was Russia's invasion of Ukraine. As it happened, just as European and U.S. consumers broke free from the pandemic restraints with a surge of new spending, the invasion abruptly reduced the supply of petroleum, grain, and fertilizer. The combination of consumers coming out to spend, Russia's oil being embargoed, and a resurgent pandemic in China created a sharp conflict between supply and demand. It is classic economics that a surge in demand meeting a restriction in supply will create a rise in prices.

It is important to note that were this inflation episode to have been caused by the government stimulus bills enacted here in the U.S., inflation would be much higher here than elsewhere. At present, consumer spending here in the U.S. is about what it was projected to be before the pandemic. Europe, where there were no stimulus bills, is seeing as high or higher inflation as the United States. The problem facing the Federal Reserve is that decreasing demand here at home does nothing to address the global supply shortage. Fortunately, the Fed is aware of these issues, and we can reasonably hope to see the cure not be more painful than the disease.

Meanwhile all the economic indicators are suggesting that U.S. economic growth is moderating but still strong. Employment continues to rise at an historically high rate, unemployment is near a record low, and debt levels are falling.

Until next week we remain focused on what we do, serving our clients with the excellent service, good investment and financial advice, and fiduciary investment management.

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