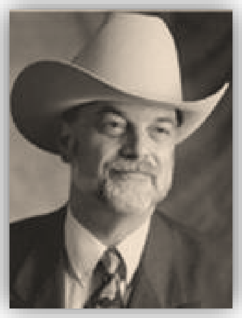

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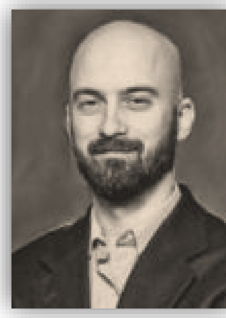

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TPWC Market and Economic Update

The Markets

It was a rough week in the stock market. The S&P 500 Stock Index (SPX) fell 4.77% to close at 3873.33. That left it down about 19.2% from its high back in January, up 5.63% from its low point in June, and down 12.62% from this time last year. Looking longer term, as we do, the SPX is now up 35.27% from this time back in 2019, before the pandemic, and perhaps more impressively, up over 73% from where it was in March 2020, only about two and a half years ago. The stated reason for the fall this week was that the trailing one-year CPI inflation number came in only slightly lower than it did last month. More on that below. Our other followed stock index, the CRSP Mid-Cap Value Index, dropped 4.88% for the week to 2294.29 and is now down 11.66% from its high in January and 5.97% from a year ago.

The benchmark 10-year U.S. Treasury note yield rose an impressive 4.3% to 3.455% for the week. With the 2-year yield standing at 3.85%, the 2–10-year yield curve is again decidedly negative. The yield curve beyond 10-years remains resolutely positive causing the yield curve indicator to be a mixed signal. West Texas Intermediate crude oil (WTI) prices were stable, falling about 1% for the week, to $85.27 per barrel. Markets are behaving oddly, note that bonds, the supposedly reliable alternative to stocks, are down about as much this year as stocks with the Bloomberg Aggregate Bond Index down about 15%, and even gold, widely hailed as a hedge against inflation, is down over 18% from its high in March.

The Economy

The gorilla in the markets this week was clearly the U.S. Bureau of Labor Statistics (BLS) announcement that their Consumer Price Index (CPI-U) was up 8.3% from a year ago with even the core CPI, where food and energy are not counted, up 6.3%. That report was widely quoted as the reason for the stock market decline with the underlying argument being that with inflation that high, the Federal Reserve was almost certainly going to raise interest rates too far and strangle the economy. Even a short glance at the actual report, rather than the headlines, seems to us to tell a different story. For starters, the one-year rate was lower than last month. Then, there was the, to us glaring, issue that the monthly inflation rate for July was 0% and for August was a mere 0.1%. Yes, for both months, energy fell 7.6% and then 10.1%, but the inflation wave was led by energy as petroleum costs soared following Russia's invasion of Ukraine and it took a few months to filter through to prices in general. Almost everything we use in our economy has an energy cost component, so it is reasonable to see the price of just about everything go up a couple of months after the price of oil rises as it did from about $75 per barrel last fall to $120 in June. With the price of oil down about 40% from its high, we are not surprised to see an end to month-to-month high inflation. Yes, given the labor shortages and wages rising at an annualized rate of about 5% for the past six months, we expect the Federal Reserve to kick rates up to the 3% or even 4% range, but it is also clear that the underlying cause of this inflation spike, the cost of fuel, has ceased to be a factor.

Another issue that worried the markets this week was another Labor Department news release where good news is bad news. New jobless claims for the week ending on Sep. 10 were only 213,000. If we take out the seasonal adjustment, the nominal claims were just under 156,000 compared with almost 266,000 a year ago. Employers are simply not laying off very many workers and that suggests a very strong economy. Unfortunately, with the unemployment rate at only 3.7%, there was a fear that the Fed will feel free to really put the pressure on the economy to slow things down.

Then came another report, this time from the Commerce Department, that retail spending rose 0.3% in August, an annualized rate of 3.6%. Retail sales are the biggest factor in our GDP, so, again, there was evidence of a hot-running economy. To confuse things even more, the Producer Price Index for final demand, a measure of wholesale prices, *dropped* 0.1% for the month with the price of goods falling 1.2% and the price of services up 0.4%. Giving weight to that report was the news, again from the BLS, that the price of imports to the U.S. fell 1%. Monthly import prices have been falling since April of this year. Those numbers are important because price increases in imports, like that of petroleum, have led the domestic inflation numbers consistently.

The more we look at the total picture, the more it looks like the inflation spike we have seen was just that, and not the entrenched long-term inflation monster we had to fight in the early 1980s. We are hoping that if there is no monster to fight the Fed will not need to take severe action and we will have the soft landing to which Chairman Powell has referred, as the economy cools a bit but doesn't stall out.

Until next week, as always, we remain hard at work individually designing, monitoring, and researching fiduciary investment portfolios for you, our clients and our sole employers, as well as striving to provide the best investment advice and service humanly possible.

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