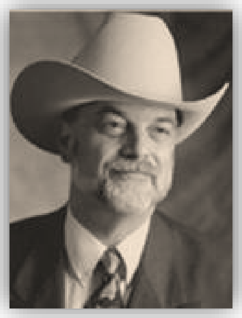

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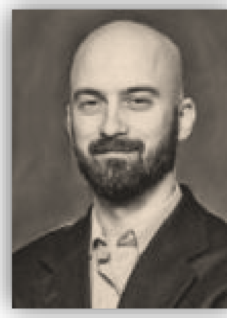

October 21, 2022

TPWC Market and Economic Update

The Markets

The S&P 500 Stock Index (SPX) bobbed up and down with vigor all week as various bits of news and rumor swept through the media but seemed repelled like a scalded cat from falling below the 3650 level. Then, on Friday, as the October options expiry date hit, instead of plunging, as it has every other month this year on that magical date, it soared! Something fundamental has changed. The SPX closed at 3752.75, up a very healthy 4.74% for the week. That rise still leaves it down 21.26% this year and 17.43% lower than it was a year ago, but up over 19% from three years ago and 68% from where it was in March of 2020. Meanwhile, the CRSP Mid-Cap Value Index rose 3.34% to 2188.36 leaving it down 15.74% this year and about 14% from last October. We hate to jinx this rally, but we get the feeling that we may have glimpsed the bottom last week.

The yields on Treasury securities were perhaps even more interesting, at least for market and economics geeks like us. The 10-year note yield soared from last week's just over 4% to 4.3% by midday on Friday, but then it fell back to close at 4.23%. That was not a surprise, but what happened to the 2-year note was. The yield (interest rate) for notes maturing two-years hence, *fell* from last week's 4.66% to 4.49% and, as a result, the yield curve became less inverted, and thereby is now predicting a less-severe recession may arrive sometime in 2023. West Texas Intermediate crude oil (WTI) joined the stock market in wobbling all week but wound up pretty much where it started at $85.90 per barrel, up 0.36%.

The Economy

As has been the habit of market and media pundits for pretty much all year, the focus for the week was on inflation and a lot of guessing about what the Federal Reserve Board is going to do to fight it. Speeches by voting members of the Board are forming into a relatively clear picture that has short-term interest rates going up another 0.75% next month, but with much smaller increases or even a pause in rate hikes following that. Those comments were credited with the shifts we are seeing in the bond market and the stock market rise.

In the real economy things continued to happen and be measured, and some of them suggest the U.S. economic expansion may be moderating. September's retail spending report showed spending was flat for the month. So far this year, retail spending rose 8.2% through August, about the same as inflation, so a non-rise in retail suggests that demand may be moderating.

At the wholesale level, the prices of goods are disinflating but that fall in prices for things we buy was more than offset by the increase in services prices. Historically, goods prices lead services prices either going up or down. If the pattern we have seen over the past two months continues, inflation may be a thing of the past in six months to a year. The other good news buried in the Labor Department's reports is that wages are following price raises rather than leading them. If wages are following, the dreaded, "wage-price inflation spiral" is not a factor.

U.S. banks are reporting that credit card spending is not decreasing. They are also reporting that while consumer cash holdings are slightly below their peak, they are still considerably higher than before the pandemic. More, the banks are reporting rising earnings, higher than Wall Street expected, and are seeing no evidence of loan payment deterioration. So far, 70% of third quarter earnings reports by publicly traded U.S. companies have come in significantly higher than expected; another indicator that any possible recession is not showing up in the real world. Then came the news from the Federal Reserve that industrial production in the United States rose 0.6% in September after rising 0.4% in August. Those are not numbers that suggest the U.S. is sliding into a recession, rather, they are what we would normally expect early in an economic expansion.

Even as the U.S. economy continues to roar ahead, it is good to keep in mind that much of the rest of the world appears to be experiencing some very real economic stress. Natural gas shortages in Europe are already constraining industry, inflation is near or at the double-digit level, and surveys suggest that there is a near-universal expectation of a soon and possibly severe recession. China's massive real estate market looks like it has not imploded only because the government is propping it up. There may be oceans between us and them, but we are not an island economically. Economic decline in Europe and China may have an economic effect here.

Until next week, we remain focused on doing an ever-better job of managing your portfolios toward your individual needs and providing the best fiduciary advice and service known to mankind!

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