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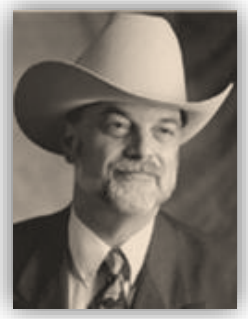

Jeffrey W McClure CFP®

PO Box 1029 / 918 N. Main Street
Salado, TX 76571

TPWC

Jacob A McClure CIMA®

(254) 947-1111
(800) 914-7526

Serving Investors Since 1982

www.tpwc.com

jeff@tpwc.com

jake@tpwc.com

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TPWC Market and Economic Update

The Markets

The S&P 500 Stock Index (SPX) drifted back below the 4000 level on Monday, Dec. 5, but then seemed to find a comfortable bottom around 3934 and, after testing it several times, closed out the week ending on Dec. 9 at 3934.38, down 3.37% for the week. That slide left it about 17.5% lower than it was when 2022 started, but still up about 9.8% from mid-October, up 76% from March of 2020, and up about 28.5% from three years ago. The other equity index we follow, the CRSP US Mid-Cap Value index declined 2.97% to close at 2379.56. It is now down 8.38% this year and 6.72% from a year ago.

The benchmark 10-Year U.S. Treasury Note's yield climbed 2.14%, causing bond prices to fall in step with the stock market and ended the week at 3.585%. For those of you who are following the score card on this, the Treasury yield curve remains solidly inverted, with the one-year note yielding 4.72%. The price for a barrel of West Texas Intermediate Crude fell almost $9 per barrel to $71.45, presaging good news at the gas pump as the national average price for a gallon of regular gasoline dropped to $3.32 per gallon, about 36% lower than it was in June of this year.

The Economy

The financial media remained stuck in "forecast the Fed" mode, reporting what in other times would be good economic news as bad, and bad economic news as good. The prevailing thought process appears to be that any good news suggesting that the U.S. economy is churning along nicely will cause the Federal Reserve to increase rates further than it would otherwise and thereby make a recession both more likely and more severe. Of course, when one boils that down to the underlying logic (or illogic), it means that reports of healthy growth, job creation, and profits are indicators of a looming recession. If you find that does not make a great deal of sense, we are with you.

We did get a good indicator of what is happening beneath the surface of the economy and driving inflation as the Bureau of Labor Statistics (BLS) produced its Producer Price Indexes report for November. The one-year increase in wholesale prices came in at 7.4%, which sounds bad, but the core index, less food, fuel, and services was 4.9%, far better than the double digit increases we saw earlier in the year. Better yet, the one month change in prices from October to November was only 0.3%. That still amounts to an annualized increase of about 4%, which is double the Fed's target of 2%, but digging down deeper reveals that disinflation may already be underway. It was what economists call "goods" that led the way into inflation as supply chains buckled around the world and in this report, the core goods inflation this month is only 0.1%, an annualized rate of only about 1.21%.

The BLS also reported on Productivity and Costs for the third quarter in its second revision, and in that report was some excellent news. Labor productivity increased at an annual rate 0.8% for the quarter, rather than the 0.3% posted in the first estimate. In the manufacturing sector, productivity increased at an amazing annual rate of 5.8%. Since wage increases are considered in this report, that means although wages may be rising at a 5% rate, manufacturing production per hour is rising 5.8% faster than that! There are only three basic elements to the growth in a national economy, the number of workers working, the productivity of those workers, and the willingness of customers to purchase the goods and services they provide. People are certainly showing they are willing to buy, and productivity is rising, so the problem continues to be an insufficient number of workers, particularly in the services area.

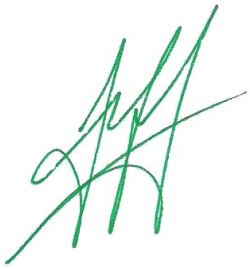
Unfortunately, since a lot more workers are unlikely to show up soon, the Fed needs to cause us to stop being so willing to spend money, particularly on services.

Commercial real estate continued to take hits as big-city office buildings, particularly in New York City, are unable to fill vacancies. Publicly traded real estate funds have fallen, some by as much as half, and many non-traded "alternative" real estate investment funds have ceased to allow investor withdrawals. One office security company put the average weekday occupancy of office space in New York at about 50%. As leases expire, many tenants are not renewing. This looks more and more like a sea change in the economy as the work-from-home ethic becomes more established.

As a last, but encouraging piece of news, Goldman Sachs economists published their opinion that the United States would narrowly avoid recession and that PCE inflation (the one the Fed follows) should decline to about 3% by the end of 2023 with only a half percent rise in unemployment. We certainly hope they are right.

Not much has changed in the bottom line. The U.S. economy continues to charge along running a bit hotter than is healthy for the long-term and inflation is still too high, but is coming down, while the rest of the world is probably in or entering a recession. We remain optimistic despite some likely bumpy times in the next few months.

Until next week, we remain your faithful, fiduciary, servants, working hard every day to do a better job of serving you, our clients, and our sole employers.



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M.S. Personal Financial Planning

Jacob A. McClure, CIMA®