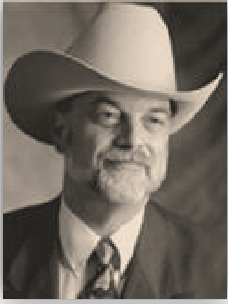

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TPWC Market and Economic Update

The Markets

Our deal old S&P 500 Stock Index (SPX) plowed ahead another week, rising 0.95% to close at 5137.08. It is now up 7.7% so far this year and over 29% from a year ago. Looking back three years, one can get an interesting perspective on such things. The SPX is up 32.73% from that point, meaning it gained almost all the gains accumulated over the last three years in the last twelve months. Take out the gains from the past year and it is only up 3.7% over a two-year period. Markets work that way. It takes a great deal of patience and tolerance for poor and even negative performance to reap the long-term benefits of investing. Our other followed market indicator, the CRSP US Mid-Cap Value index, rose 1.14% for the week to 2574.14 and is only up 6.6% from a year ago. Here is where patience is now required as the rest of the market creeps along slowly, in contrast to the "Significant 6" (previously "Magnificent 7") that are providing most of the growth in the SPX.

Over on the other side of the market, where the U.S. Treasury yield curve is the dominating factor, the benchmark 10-year U.S. Treasury note ended the U.S. market week yielding 4.19% while the one-month T-bill held at 5.54% and the other end of the curve, the 30-year Treasury bond was paying 4.33%. As has been the case, the 10-year Treasury was the lowest point in the curve as said curve remained strongly inverted. West Texas Intermediate crude oil continued its slow, but seemingly relentless climb, ending the U.S. market week at $79.76, up 4.2% from last week.

The Economy

Traders waited with bated breath this week for the Bureau of Economic Analysis (BEA) to release January's Personal Consumption Expenditures (PCE) index price reading, with their usual focus on the Federal Reserve Board's possible reaction to the PCE, the Fed's preferred inflation gauge. The PCE was well behaved, coming in very much as forecast, and was up 0.3% for January, but perhaps more importantly, only rose 2.4% from a year ago. Meanwhile though, personal income in current dollars rose a full 1%, while disposable income was up 0.3% for the month. Interestingly, expenditures were up 0.7%, suggesting that the American consumer may be borrowing more to spend more. Once more, *goods*, meaning items bought rather than services paid for, *declined* about 0.5% in price while the cost of *services* rose 3.9% over the past year. That should come as no surprise to anyone who has tried to get something repaired or other services. The price of buying something has come down while the price of getting someone to do something has risen.

One of the larger questions that people rightfully ask is how the Consumer Price Index (CPI), produced by the Bureau of Labor Statistics in the Labor Department, which comes out earlier in the month, can be one number but then the later release of the PCE from the BEA in the Commerce Department comes out lower. The difference is classic and says a lot about statistics. The CPI is based on a weighted average price change of a list of goods and services with the weighting based on where people *say* they are spending their money. The PCE, on the other hand, comes from a weighted list of goods and services with the weighting based on where consumers *actually* spent their money. Consumers consistently remember spending more money on things that have risen in price, leading to a higher average for the CPI. The PCE data takes longer to gather because businesses must compile what they have sold during the month and report that information to the Commerce Department. The reality is that consumers tend to spend more on things that are declining in price, so the PCE almost always comes in lower than the CPI. A prime example is that

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very consistently, the amount consumers spend on alcohol is significantly higher than what they report spending. The reverse is true of spending on shelter. Consumers consistently report spending almost twice as much on shelter as they do.

Another key element in our economy at present is why the U.S. is booming when most of the rest of the world is gazing at actual or potential recessions. The prime difference boils down to something called "worker productivity." In the U.S. labor participation remains below where it was prior to the pandemic while in much of Europe, labor participation is up even as their growth stagnates or retreats. Data lags in this area, but in the four years beginning with 2019, real output per hour in the U.S. non-farm workforce rose 6.4% while employment only increased 4% and hours worked fell 1.3%. That results in a production growth of 9.2% and an output per worker rising at 5%, all adjusted for inflation. Where did all that come from? It appears that the ability to shift workers into more productive slots as needed may be the key, as well as technological changes. The contrast between work-rules dominated workplaces where unions dominate and demand that people only be required to work at the task they were hired for and the more free-market workplaces where employees may be moved to where they are needed may be the key ingredient. Workers appear to have been moving out of areas where robots and digital technology are taking over and into areas that require thought and flexibility.

Until next week, we remain at your service, providing fiduciary advice, portfolio management, and planning to our clients, and sole employers.

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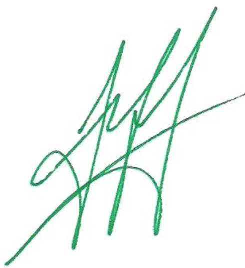

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