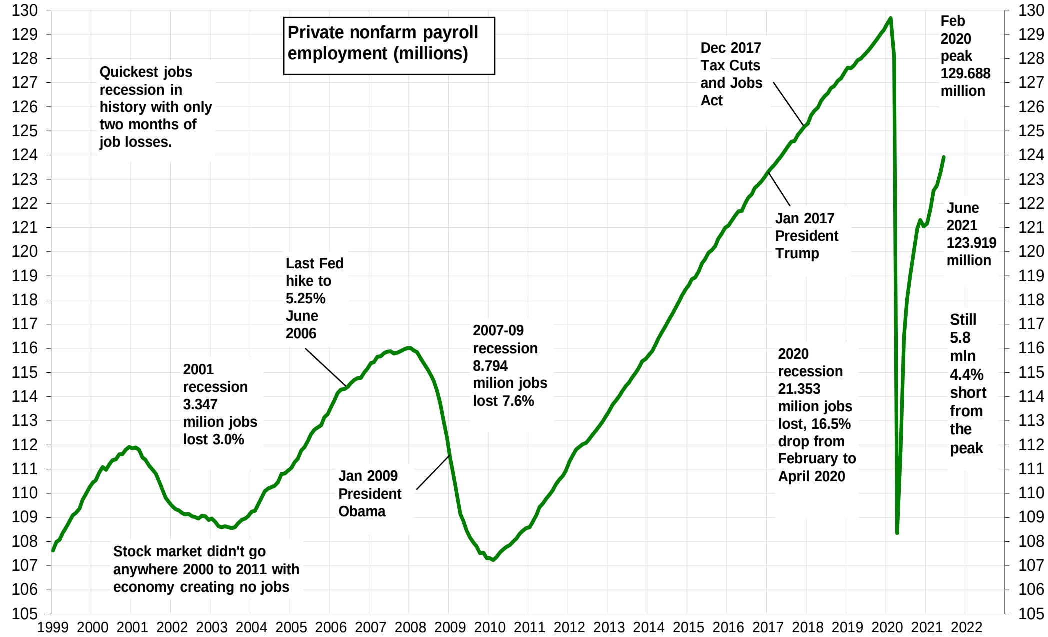
Financial Markets This Week

Christopher S. Rupkey, CFA
Chief Economist
crupkey@fwdbonds.com

2 JULY 2021

MONSTER JOBS REPORT



Biggest jobs gain this year in June. The record 9.3 million job openings at the end of April didn't lie. Nearly one million jobs were gained in June meaning the economic outlook for the second half of 2021 is rock solid. Join the conversation. Heck, drop your cell phone, turn off the social media, and do something. Get to work. Your country needs you. Join the labor market, it's red hot.

Payroll employment rose 850K in June and has averaged monthly gains of 542K in 2021. 22.362 million jobs lost in March/April 2020, and now 15.598 million have been hired back with 6.764 million left to go. Manufacturing jobs are still down 481K from February 2020 before the pandemic, retail jobs down 303K or 1.9%, local government education down 414K, and leisure and hospitality down 2.2 million or 12.9%.

Monthly changes (000s)	Jun	May	Apr	Mar	Feb
Payroll employment	850	583	269	785	536
Private jobs	662	516	226	724	622
Leisure/Hospitality jobs	343	306	328	227	413
Unemployment rate %	5.9	5.8	6.1	6.0	6.2
Not in labor force (mln)	100.253	100.275	100.115	100.445	100.708
... and Want A Job (mln)	6.428	6.600	6.647	6.850	6.933
Average hourly earnings	$30.40	$30.30	$30.17	$29.97	$30.00
MTM % Chg	0.3	0.4	0.7	-0.1	0.3
YOY % Chg	3.6	1.9	0.3	4.3	5.2

The biggest gain in nonfarm payroll jobs this year is good news, but if you pull back the curtain there are signs that the economy is overheating as the reopening demand following the pandemic is stronger and more powerful than companies expected. For one thing, labor isn't cheap and the inflation we have seen won't be as temporary as some Fed officials believe because now wages are moving up sharply. We have never experienced an economy where there are still nearly 7 million out of work and yet wages for those on the job are soaring. Average hourly earnings are up 3.6% the last year to $30.98 in June which is over $63,000 a year assuming you work 8 hours a day. Leisure and hospitality worker wages are up 7.1% the last year which is a sure sign hotels can't find any workers. The other lower-pay worker category is retail, and their wages are up 6.2% the last year.

What are Fed officials going to do? The bond market rally is betting today's report is not good enough to halt the emergency Fed stimulus, but we have inflation, now we have wage inflation, and yet somehow the unemployment rate remains stuck at 5.9%. The Fed's leadership is waiting for the labor market to show more improvement from the 6.7% unemployment rate when they met in December 2020. We aren't sure the improvement to 5.9% seen to date will be enough for them. It is doubtful that the Federal Reserve's "substantial further progress" requirement before tapering their $120 billion monthy QE purchases has been met yet.

Payroll jobs fall from February 2020 peak as recession began

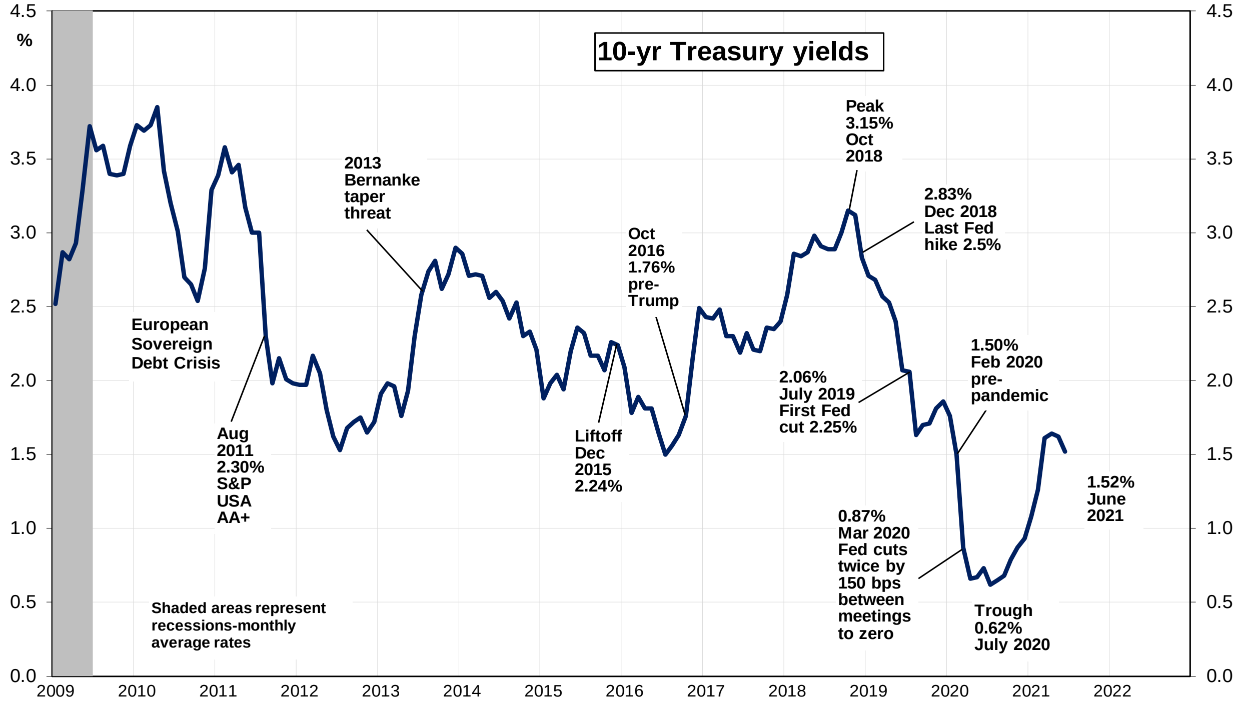
Data in thousands	Jun 21	May 21	Apr 21	16 months Feb 20 Jun 21	Jun 2021	Feb 2020
Nonfarm Payroll Employment	850	583	269	-6,764	145,759	152,523
Total Private (ex-Govt)	662	516	226	-5,769	123,919	129,688
Goods-producing	20	19	-41	-779	20,358	21,137
Mining	10	4	4	-56	585	641
Manufacturing	15	39	-35	-481	12,318	12,799
Motor Vehicles & parts	-12	23	-42	-113	873	986
Construction	-7	-22	-9	-238	7,410	7,648
Private Service-providing	642	497	267	-4,990	103,561	108,551
Trade, transportation, utilities	99	63	-70	-598	27,278	27,876
Retail stores	67	27	-22	-303	15,306	15,610
General Merchandise	25	-2	-7	89	3,088	2,999
Food & Beverage stores	-13	-7	-52	14	3,089	3,075
Transportation/warehousing	11	21	-55	-94	5,730	5,823
Truck transport	6	-3	2	-38	1,487	1,525
Air transportation	8	7	6	-83	434	517
Couriers/messengers	-24	1	-61	117	1,000	883
Warehousing and storage	14	5	-1	101	1,428	1,328
Utilities	0	-1	0	-8	539	547
Information	14	28	11	-178	2,736	2,914
Financial	-1	-3	17	-75	8,800	8,875
Insurance	0	-3	-8	12	2,868	2,856
Real Estate	0	4	14	-100	2,262	2,362
Commercial Banking	-4	-9	-2	-61	1,340	1,400
Securities/investments	2	4	6	24	990	966
Professional/business	72	36	-79	-633	20,836	21,469
Temp help services	33	-7	-122	-279	2,666	2,945
Management of companies	-1	-9	2	-92	2,333	2,425
Architectural/engineering	3	2	12	9	1,556	1,546
Computer systems/services	0	3	8	3	2,242	2,239
Legal services	6	2	2	-27	1,138	1,165
Accounting/bookkeeping	3	17	15	28	1,056	1,028
Education and health	59	59	23	-1,028	23,537	24,565
Hospitals	-6	-2	-3	-102	5,135	5,238
Educational services	39	39	-10	-255	3,524	3,779
Leisure and hospitality	343	306	328	-2,181	14,734	16,915
Hotel/motels	75	33	58	-452	1,653	2,105
Eating & drinking places	194	201	168	-1,270	11,038	12,308
Government	188	67	43	-995	21,840	22,835
Federal ex-Post Office	-2	4	-1	19	2,279	2,260
State government	69	47	10	-210	5,093	5,303
State Govt Education	75	52	10	-168	2,428	2,596
Local government	124	30	30	-798	13,871	14,669
Local Govt Education	155	50	22	-414	7,616	8,030

Average Hourly Earnings

June 2021

3.6%	$30.40	Total private
2.6	$44.61	Utilities
2.3	$44.53	Information
5.9	$40.10	Financial jobs
3.6	$36.49	Professional/business
0.2	$35.00	Mining logging
3.9	$32.86	Construction
4.0	$31.19	Manufacturing durables
3.6	$29.54	Education and health
6.2	$21.92	Retail trade
7.1	$18.23	Hotels/restaurants

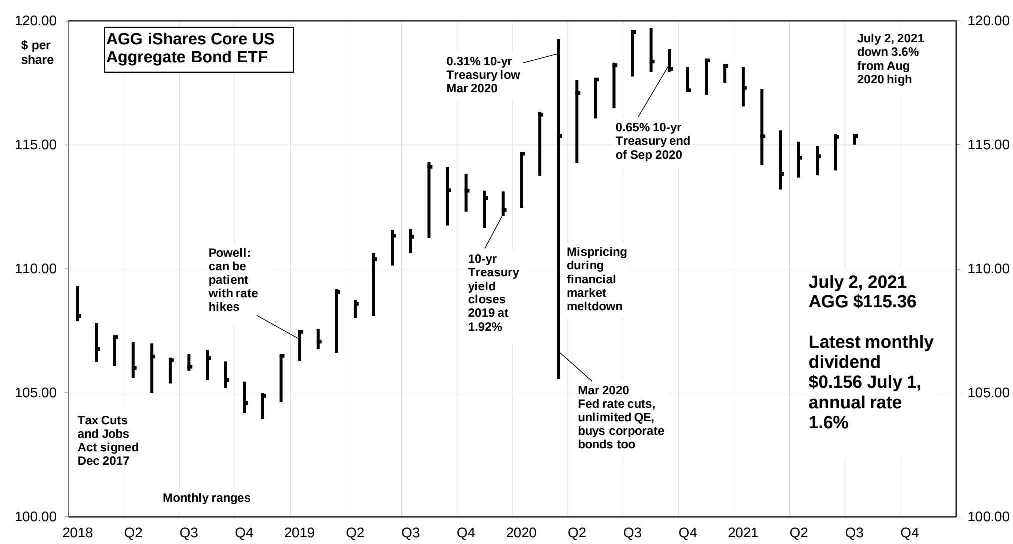
INTEREST RATES



The bond market is in narrow-range rally mode since the 1.78% yield peak on March 30th which we guess fits the story of the economy moving beyond peak-growth if you like fairy tales. Little bond reaction to the 850K jobs number Friday with the early 2pm ET holiday close. The stock market rally continues on and on with the story of economic recovery or any other story that fits with the uptrend. Quarter-end buying, day after quarter-end buying. The latest story is the first two weeks of July are historically the best of the year for price gains. On Friday, S&P 500 up 15.9% YTD, 10-yr yields 1.44%.

Checkup on the 40-fixed income side of the 60/40 stocks/bonds portfolio

The 60s side of the 60/40 model investment portfolio is doing so well that many won't care about what bonds are doing but we will update the chart we have on it this week. The latest AGG dividend which has been sinking is 1.6% versus 1.3% for the S&P 500 ETF. Back in October 2018 when the Fed nearly had rates up to 2.5%, the dividend yield was 2.9%, although there has been principal appreciation of 9.3% since then: even if most investors in the 40-side won't be sellers.



FEDERAL RESERVE POLICY

Selected Fed assets and liabilities Fed H.4.1 statistical release billions, Wednesday data	30-Jun	23-Jun	16-Jun	9-Jun	March 11 2020** pre-Covid
Factors adding reserves					
U.S. Treasury securities	5183.385	5163.445	5153.771	5129.891	2523.031
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347
Mortgage-backed securities (MBS)	2319.637	2354.155	2328.124	2244.270	1371.846
Repurchase agreements	0.000	0.000	0.000	0.000	242.375
Primary credit (Discount Window)	0.477	0.461	0.584	0.502	0.011
MMLF	0.000	0.000	0.000	0.000	
PDCF	0.000	0.000	0.000	0.000	
Commerical Paper Funding Facility	8.554	8.554	8.554	8.554	
Paycheck Protection Facility	90.626	87.129	86.591	87.069	
Corporate Credit Facility (CCF)	25.902	25.863	25.844	25.896	
Municipal Liquidity Facility	10.740	10.738	10.736	10.734	
Main Street Lending Program	30.547	30.538	30.529	30.576	
Term Asset-Backed Facility (TALF II)	4.689	4.762	4.762	4.762	
Central bank liquidity swaps	0.568	0.483	0.500	0.516	0.058
Federal Reserve Assets	8126.9	8151.2	8113.5	8001.6	4360.0
3-month Libor %	0.15	0.15	0.12	0.12	0.77
Factors draining reserves					
Currency in circulation	2183.581	2179.557	2178.952	2180.167	1818.957
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	851.929	733.877	765.114	673.555	372.337
Treasury credit facilities contribution	40.278	50.278	50.278	50.278	
Reverse repurchases w/others	991.939	813.650	520.942	502.904	1.325
Reserve Balances (Net Liquidity)	3511.630	3765.713	3905.735	3916.725	1779.990
Treasuries within 15 days	79.125	80.188	79.372	50.731	21.427
Treasuries 16 to 90 days	267.131	299.927	292.109	327.810	221.961
Treasuries 91 days to 1 year	678.379	647.609	656.183	643.991	378.403
Treasuries over 1-yr to 5 years	1995.709	1983.709	1982.040	1978.648	915.101
Treasuries over 5-yrs to 10 years	950.972	947.593	943.249	933.934	327.906
Treasuries over 10-years	1212.068	1204.418	1200.819	1194.777	658.232

**March 11, 2020 start of coronavirus lockdown of country

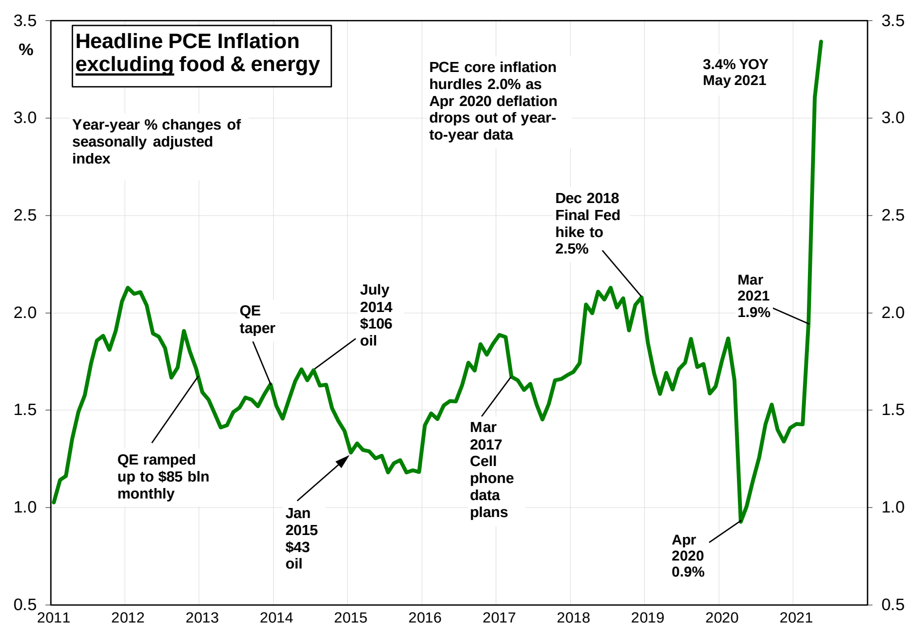
MMLF: Money Market Mutual Fund Liquidity Facility: loans secured by assets bought by banks from money market funds

PDCF: Primary Dealer Credit Facility: o/n and term funding with maturities to 90 days

CCF: Corporate credit facility: Primary market (PMCCF) and Secondary Market (SMCCF)

The Fed meets on July 27-28, 2021 to consider its monetary policy. It doesn't seem appropriate to keep adding money to the banking system if the economy creates 850K new payroll jobs in June, the uptick in the unemployment rate from 5.8 to 5.9 percent notwithstanding. In the old days, it was hard for the Fed to agree to even bring the unemployment rate into the picture as a goal of monetary policy. It was just inflation. The thinking at the time a labor market indicator was added was that the Fed funds rate should be brought back up completely to normal levels (normal in 2012 was 4.25%) by the time the unemployment rate was back down at full employment levels (full employment unemployment was 5.6% in 2012).

That was then and this is now, where it sounds like Fed Chair Powell doesn't want to lift interest rates from zero until unemployment gets back down to the 3.5% best economy in fifty years unemployment rate in early 2020 before the pandemic crashed the markets and the economy. The normal Fed funds rate is 2.5%, but Fed liftoff won't start until the unemployment rate gets to 3.5%. That may take a while if the Fed counts the labor force dropouts in this recession. It was unique in this recession for there to be so many dropouts. Those not in the labor force totaled 95.180 million in February 2020 and are 100.253 million in June 2021, an increase of 5.073 million. If we add these to the unemployment count, June's 5.9% unemployment rate is 8.8% or even farther away from the Fed's goal. By the way, this labor force dropouts count won't be as meaningful fairly shortly because the number of dropouts grows naturally if you will with the growing U.S. population which is about 330 million today. In other words, the dropouts won't ever return to 95.180 million again.



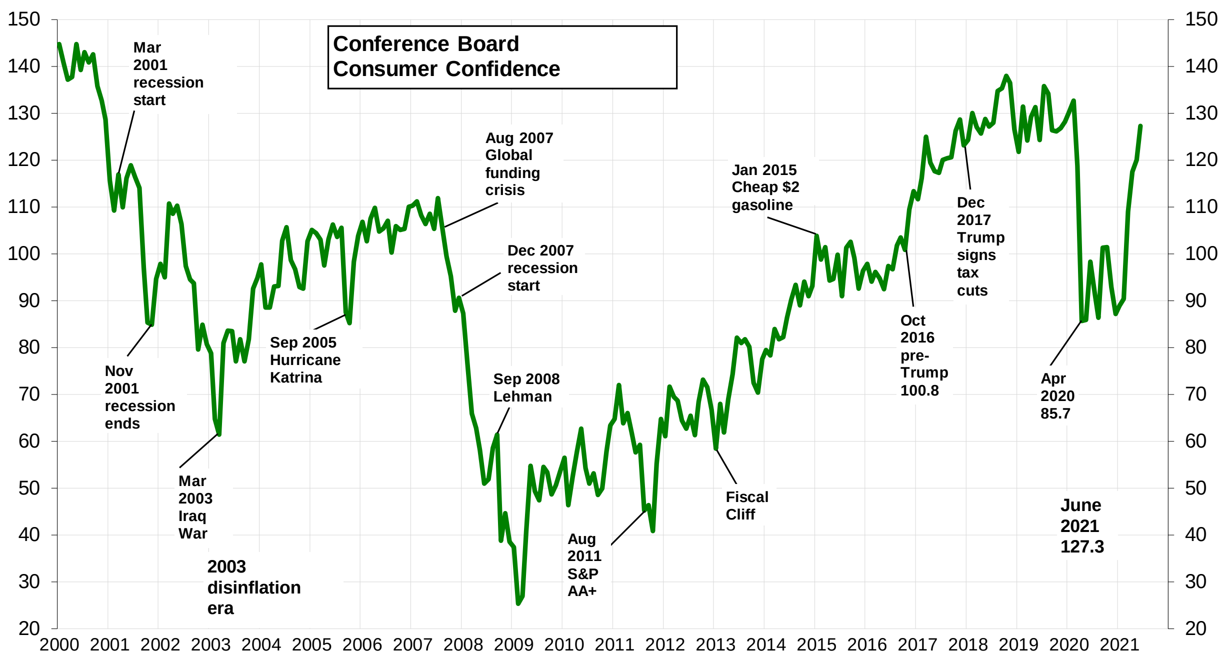
More Fed officials are concerned about inflation, although maybe not enough to start the tapering. Low interest rates help support the economy, but normally just the interest-rate sectors like housing and autos, sectors that don't need the Federal governments help right now. It seems like too much money printing looking at just the Fed's U.S. government securities purchases: $504 billion March 2020, $993 billion in April, $138 billion in May and then $80 billion monthly since then with no sign of when it will be tapered. Under Bernanke, the maximum monthly purchases of Treasuries were $45 billion for a year before tapering. On Thursday before the employment data, St. Louis Fed President Bullard said they needed to begin discussing tapering, and Philly Fed President Harker said tapering this year would be appropriate "sooner rather than later."

OTHER ECONOMIC NEWS

Consumers are back from the pandemic blues (Tuesday)

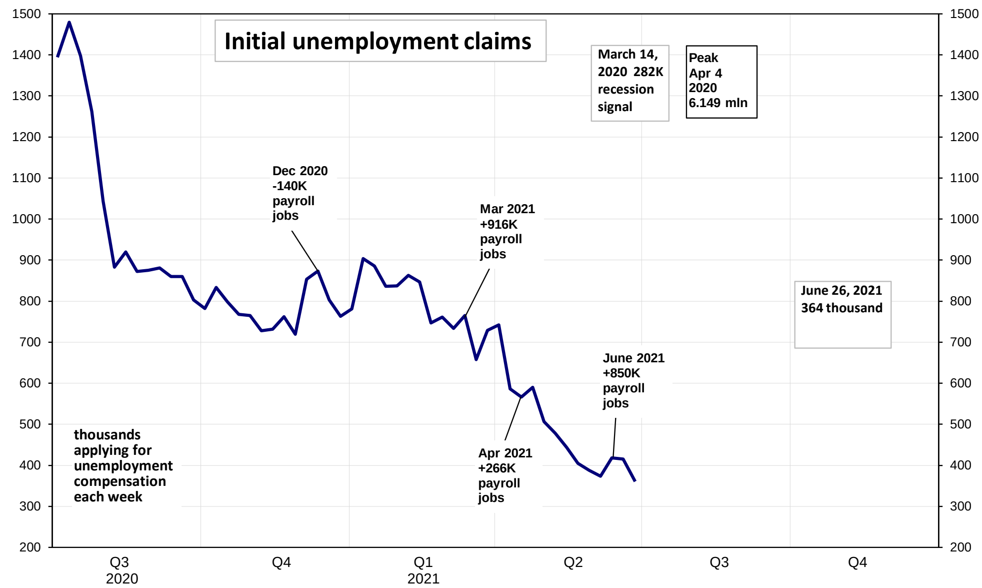
Breaking economy news. The consumer confidence report from the Conference Board is out and you can read it if you pony up the $995 annual subscription or you can wait for the twice a month free consumer sentiment report from the University of Michigan. Consumers are no longer singing the pandemic blues with the confidence index jumping 7.3 points to 127.3 in June which is the happiest reading yet for this measure of how the consumer is doing. Jobs are plentiful with a reading of 54.4 in June up from 48.5 in May which could indicate one million new nonfarm payroll jobs in Friday's report if the consumer is right. Jobs this plentiful sure doesn't look like a recession anymore. Maybe the Federal Reserve is watching the wrong labor market data in thinking the economy still needs the support of $120 billion in monthly bond purchases.

Net, net, consumer confidence is rebounding quickly as the economy's reopening collides with the summer vacation season sending consumer sentiment soaring to levels not seen since the pandemic struck over a year ago. Their happiness knows no bounds for now. There is still a question mark about the economic outlook once the stay-at-home economy gets back to work and the consumer shift of their purchases from store-bought goods to services is completed. A lot of the conditions that support the ebullience of consumers is going away as there will be no more $1400 checks from the Federal government, no more $300 extra weekly jobless benefits and no more Federal Reserve QE stimulus that supports a roaring stock market. Stay tuned. Story developing.



America is back to work (Thursday)

Breaking economy news. Jobless claims fell to 364 thousand in the June 26 week which is a decline of 51 thousand from the prior week. Back below 400 thousand is a milestone which shows jobs are more available and the output gap is smaller than we ordinarily see following a typical economic recession which is good for employment but bad for inflation. Good news today for the economy and the only mystery is why is the bond market rallying and yields falling on this labor market news. If the labor market is healing, then the Federal Reserve is getting closer to the date when it can scale back its monthly $120 billion QE purchases. If the market is afraid of another taper tantrum the bond market isn't showing it. The only other mystery is why the Department of Labor says 14.659 million were receiving unemployment benefits checks in the June 12 week while the Bureau of Labor Statistics says the number of unemployed in June is just 9.316 million. Other than massive mismeasurement or outright fraud, we aren't sure what to think.

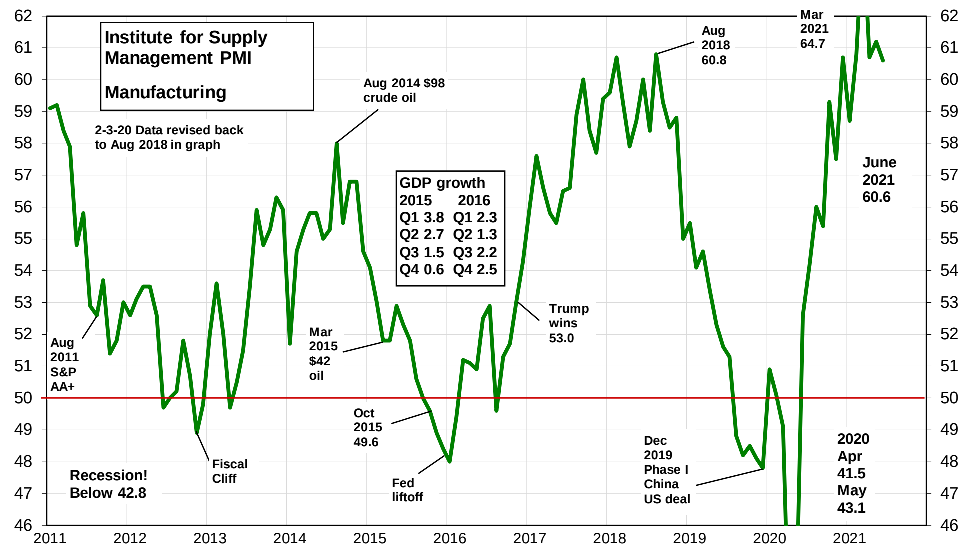


Net, net, there's more opportunity than ever before in this labor market recovery from the pandemic where the number of filings for jobless benefits is falling because the work is out there if you want it. If you are available, companies want you badly and we are already seeing this as employers are having to sweeten job offers with perks and cash. America's back to work and an important milestone was reached where new claims are back below the 400 thousand barrier after a hiccup at the start of June. Summer is always the strongest season for hiring each year and this year is no exception with layoffs at a new low since the pandemic recession started over a year ago. Claims were slightly higher early in June around the survey period for payroll jobs, and we hope that does not bode poorly for tomorrow's all-important monthly payroll employment report. The market is counting on a 700K payroll jobs number tomorrow. Bet on it.

Unemployment Benefits Recipients		
6/12/2021	Program	Prior Year
3,208,474	Regular State	17,721,250
10,472	Federal Employees	14,628
6,207	Newly Discharged Veterans	12,591
5,935,630	Pandemic Unemployment Assistance	13,222,961
5,261,991	Pandemic Emergency UC	836,516
154,000	Extended Benefits	2,626
1,267	State Additional Benefits	2,126
81,750	STC/Workshare	305,738
14,659,791	TOTAL	32,118,436

Factory executives remain at peak confidence levels (Thursday)

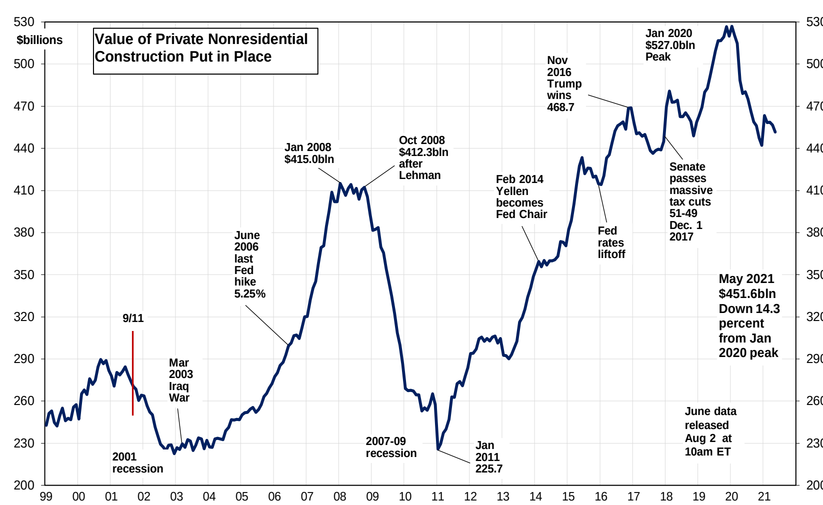
Breaking economy news. The ISM manufacturing index fell to 60.6 in June from 61.2 in May. Any reading above the 60 level indicates that purchasing managers' confidence literally knows no bounds. A 60 reading was last seen way back in 2018 before the China U.S. trade war hurt business confidence enough to throw manufacturing under the bus and into recession even before the pandemic hit the economy hard in February 2020.



Purchasing managers are still more confident than actual production figures from the Federal Reserve even as they cite growing challenges from supply chain constraints to the higher prices they have to pay for materials and for shipping costs. Some even cite labor shortages which we have never heard before this early in the recovery from any recession in modern economic history. Markets will find out tomorrow just how tight the labor market is with the monthly jobs report and if the economy still requires the support of the Federal Reserve that is hellbent on bolstering financial market conditions even if the risk of a housing and stock market bubble grows by the day. The Fed is driving so fast we worry what will happen to the economy if they have to suddenly slam on the brakes.

Net, net, purchasing managers at companies could not be any more confident than they are right now and are turning a blind eye for the moment to the risks posed by price increases for many of the inputs they use to produce goods for the world. Higher prices depress demand, that's a fact, and the higher prices and inflation go, the more likely it is that the U.S. will experience a growth slowdown in the second half of the year.

Also released: Construction data on (Thursday)



Construction is still the weak link. Companies don't need more offices (down 8.3% the last year), lodging is down 23.2% since May 2020, amusement and recreation down 16.6%, and manufacturing and factories down 3.2% the last year. Nonresidential private construction in total fell 1.1% this month and is down 5.8% since May 2020. They revised the data back to 2014 and the amount of construction was revised up sharply over the course of 2019 before the pandemic. From the pre-pandemic record construction level, May activity is down 14.3% where in April, the decline from the pre-pandemic record was just 10.0%. Business investment in new construction subtracted 0.1 percentage points from Q1 2021's 6.4% real GDP.

Analyst Certification

The views expressed in this report accurately reflect the personal views of the research staff at FWDBONDS LLC, the primary analysts responsible for this report, about the subject securities or issuers referred to herein, and no part of such analysts' compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed herein.