Financial Markets This Week

12 JULY 2024

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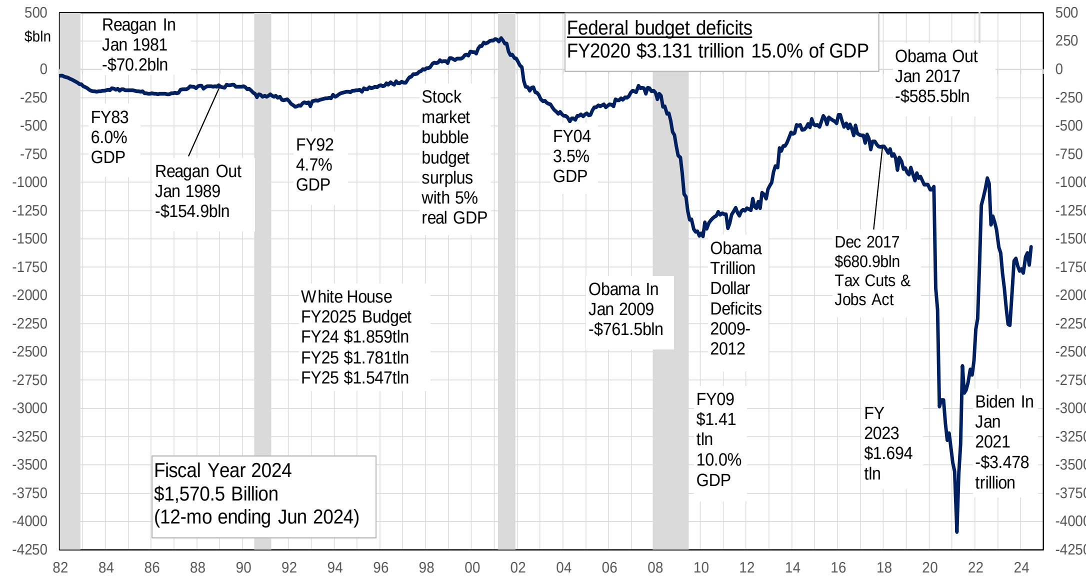
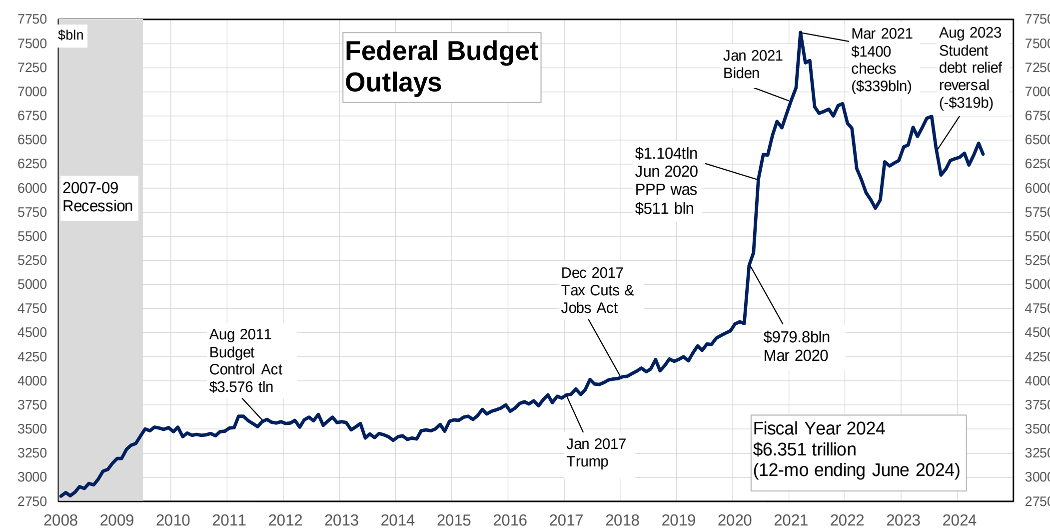
TOO MUCH GOVT SPENDING

Federal Government spending up 4.5% in first 9 months of FY2024



The June monthly Federal budget deficit was released Thursday which completes the third fiscal (FY) quarter for the year. We have heard that there is too much Federal government spending since graduate school in the 70s, and perhaps it is still true although it hasn't brought the house down yet. Our advice is to let the market tell you if the national debt load around the economy's neck is not sustainable. Ditto for bankrupt Social Security. It is already bankrupt if you want to know where the shortfall from more monthly payments to senior citizens has fallen behind monthly payroll tax collections for years now, and the difference is made up by other Federal income taxes or Treasury borrowing from the bond markets, the biggest, deepest, most liquid markets in the world. Don't wait for 2033 or 2035 or whatever fanciful date the Social Security Trustees put on the bankruptcy date, the national retirement system's sea is awash with red ink right now. The payments/obligations to the nation's elderly are being met in full right now 100 cents on the dollar even though receipts are less than outlays each and every month. Better to stop scaring the public. The idea that



Social Security has some secret holding of cash assets on its books of 4 or 5 trillion dollars that will last into the 2030s is laughable. (Note: our editor did not take this last sentence out.) Congress would have spent that cash long ago, and indeed, they have.

Too much government spending? Federal budget outlays are running $6.351 trillion in the 12 months ending June 2024. We are a little surprised that outlays did not drop back more dramatically after the pandemic emergency spending programs, but perhaps we should not have been given the same thing happened after the 2007-09 recession stimulus spending. Republicans took back the House in November 2010, the Budget Control Act was signed in August 2011, and nondefense discretionary outlays fell modestly for a couple of years 2012-13, but generally the impact is limited because in this case controllable nondefense discretionary outlays were only $647 billion of $3.603 trillion in total Federal government outlays in FY 2011 or 18%. We will see what the next Congress is able to do in January 2025. The bond market says the national debt is sustainable for now otherwise 10-yr Treasury yields would be at 6%.

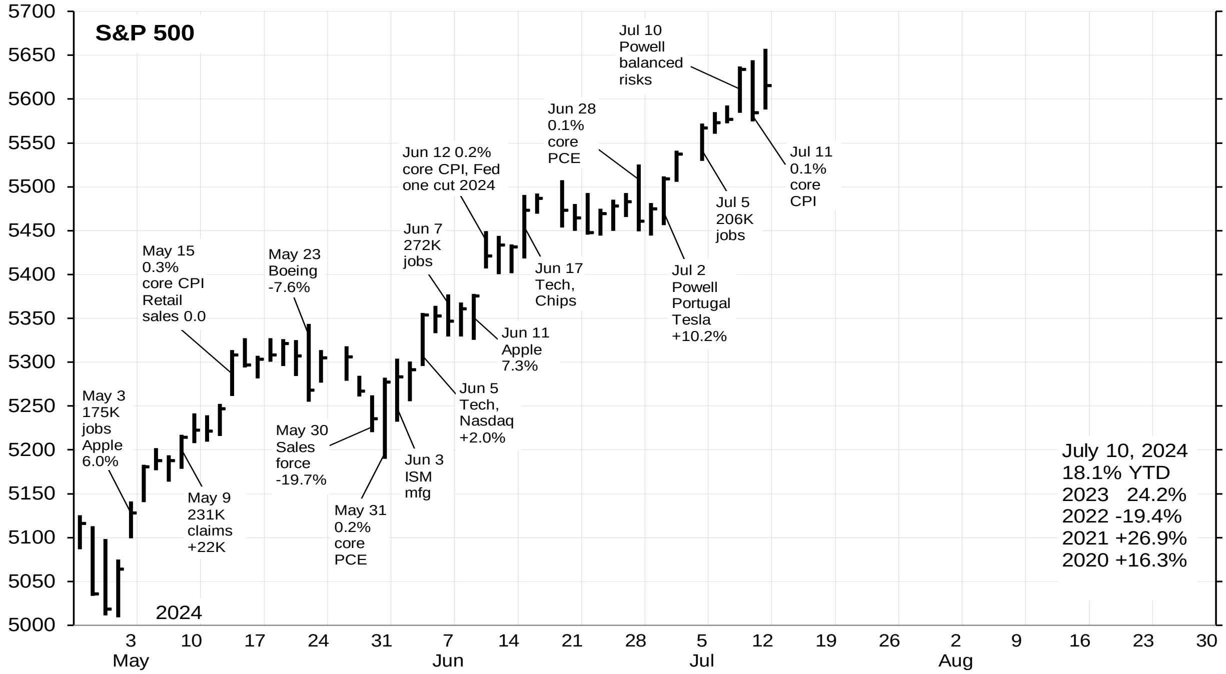
Federal Government Spending ($bln) Where to cut?	3 Qtrs FY24 Q4 23-Q2 24	3 Qtrs FY23 Q4 22-Q2 23	Fiscal Year Changes	Fiscal Year % chg	Full Year FY 2023
TOTAL BUDGET OUTLAYS	5,022.456	4,805.518	216.938	4.5	6,134.432
Legislative	4.985	4.910	0.075	1.5	6.515
Judicial	6.931	6.689	0.242	3.6	8.995
Agriculture	159.939	182.525	-22.586	-12.4	228.887
Commodity Credit Corporation	6.420	6.889	-0.469	-6.8	7.318
Food Stamps	79.715	106.174	-26.459	-24.9	134.634
Child Nutrition	26.447	25.013	1.434	5.7	29.235
Commerce	10.259	8.968	1.291	14.4	12.045
Defense	608.570	576.406	32.164	5.6	775.872
Military Personnel	148.446	141.496	6.950	4.9	183.898
Operation Maintenance	238.766	231.624	7.142	3.1	317.563
Procurement	112.153	106.200	5.953	5.6	141.749
Research Development	99.142	87.598	11.544	13.2	121.954
Military Construction	8.922	7.825	1.097	14.0	10.344
Education	202.496	172.294	30.202	17.5	-41.108
Office of Federal Student Aid	121.830	93.583	28.247	30.2	188.369
Energy	36.740	24.728	12.012	48.6	34.423
Health Human Services	1257.589	1293.190	-35.601	-2.8	1708.521
Medicare	761.433	768.992	-7.559	-1.0	1024.288
Medicaid States Grants	459.861	471.404	-11.543	-2.4	615.772
Homeland Security	65.701	68.015	-2.314	-3.4	89.032
Housing Urban Development	35.894	40.204	-4.310	-10.7	55.194
Interior	12.599	11.063	1.536	13.9	15.865
Justice	32.170	33.939	-1.769	-5.2	44.327
Labor	39.216	73.038	-33.822	-46.3	87.530
State Unemployment Benefits	27.153	22.170	4.983	22.5	30.181
State	24.638	22.557	2.081	9.2	32.997
Transportation	79.192	76.313	2.879	3.8	109.786
FAA	16.926	17.956	-1.030	-5.7	23.824
Federal Highway Admin.	40.671	35.252	5.419	15.4	54.018
Treasury	1040.231	875.953	164.278	18.8	1106.950
IRS	183.566	215.640	-32.074	-14.9	254.964
Premium Tax Credit	75.481	57.030	18.451	32.4	82.597
Earned Income Credit	58.861	54.214	4.647	8.6	55.468
Child Tax Credit	25.567	27.919	-2.352	--	28.768
Interest on Public Debt	867.746	652.403	215.343	33.0	879.307
Veterans Affairs	235.283	219.519	15.764	7.2	301.026
Corps of Engineers	8.130	6.747	1.383	20.5	7.806
Other Defense Civil Programs	46.848	51.147	-4.299	-8.4	68.928
Environmental Protection	9.573	7.799	1.774	22.7	12.586
Exec. Office of President	0.461	0.390	0.071	18.2	0.543
International Assistance	22.824	30.320	-7.496	-24.7	36.050
NASA	18.708	18.416	0.292	1.6	25.319
National Science Foundation	6.369	6.068	0.301	5.0	8.951
Personnel Management	94.350	91.851	2.499	2.7	122.508
Small Business Admin.	32.554	25.339	7.215	28.5	26.072
Social Security Admin.	1132.130	1053.054	79.076	7.5	1416.328
Retirement Benefits	963.151	884.369	78.782	8.9	1192.149
Federal Disability Payments	114.946	111.607	3.339	3.0	149.667
Other Independent Agencies	76.993	76.550	0.443	--	134.262

Social Security In/Out

$ bln	Receipts	Payments	Red/Black
FY2019	770.282	888.080	-117.798
FY2020	825.307	940.221	-114.914
FY2021	814.034	982.673	-168.639
FY2022	911.191	1,063.897	-152.706
FY2023	1,020.442	1,192.149	-171.707
Feb 24	83.589	107.828	-24.239
Mar 24	92.262	108.621	-16.359
Apr 24	110.173	109.028	1.145
May 24	85.482	109.381	-23.899
Jun 24	119.003	109.928	9.075

** Note: June 2024 Social Security is still "insolvent," prior year adjustments increased the total receipts for this one month (and April 2024 saw self-employment contributions rise).

INTEREST RATES



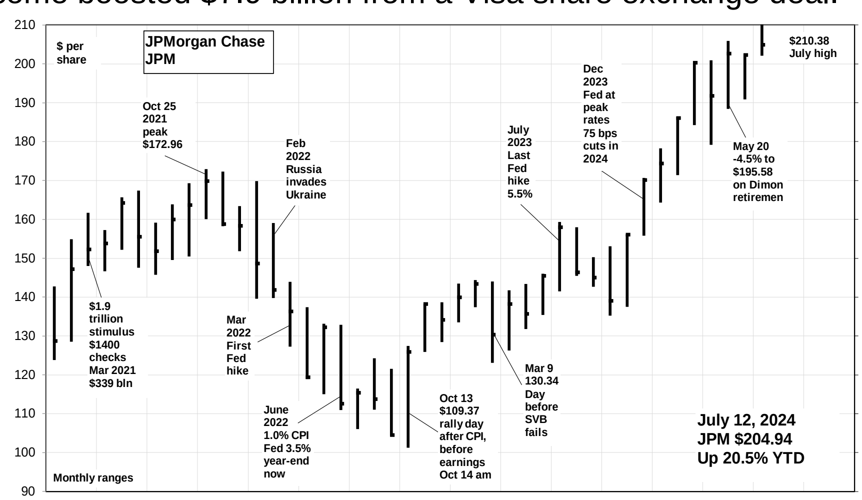
Stocks were higher this week so everyone is happy, although the daily ranges were quite large on the final three days. The S&P 500 inched upward towards the 5,600 level, breaking above that perhaps on the second day of Powell's testimony Wednesday, repeating the theme of balanced risks out there, and they were not just purely fighting inflation with higher rates anymore, although of course they are: higher rates the only way they know to return it to 2.0%. Good inflation data Thursday with immediate selling following the move to new highs; this keeps happening, the recent experience after 0.1% core PCE inflation at the end of June, but it goes back further. The stock rally on Friday was not easily explainable besides saying equities recovered lost ground from Thursday's "tech-related sell-off," and even made a new all-time high briefly. CPI/PPI say 0.0% core PCE inflation on July 26. Stay tuned.

JPMorgan Chase (JPM) up 20.5% YTD

The stock fell 1.2% Friday following the earnings report before the open on Friday, July 12. After the April 12 earnings report the stock fell from $195.43 to as low as $179.20 before recovering. The stock fell 4.5% on May 20 on an earlier possible retirement for Dimon. Earnings press release has Dimon saying geopolitical risks are potentially the most dangerous since WWII. Global investment banking fees wallet share is 9.5% YTD. Net income boosted $7.9 billion from a Visa share exchange deal.

JPM results (billions)

Quarter	Net Income	Provision for Credit Losses	Stock price Qtr end
6.30.2024	18.149	3.052	202.26
3.31.2024	13.419	1.884	182.35
12.31.2023	9.307	2.762	170.10
9.30.2023	13.151	1.384	145.02
6.30.2023	14.472	2.899	145.44
3.31.2023	12.622	2.275	130.31
12.31.2022	11.008	2.288	134.10
9.30.2022	9.737	1.537	104.50
6.30.2022	8.649	1.101	112.61
3.31.2022	8.282	1.463	136.32
12.31.2021	10.399	-1.288	158.35
9.30.2021	11.687	-1.527	163.69
6.30.2021	11.948	-2.285	155.54



FEDERAL RESERVE POLICY

The Fed meets July 30-31, 2024 to consider its monetary policy. Core CPI rose just 0.1% on Thursday, so a lot of the message from the two days of Powell Congressional testimony is stale. He did say on Tuesday he did not mean to signal anything in regard to the possibility of future interest rate moves that the FOMC might be contemplating even if the market took his balanced risks comment as a sign labor market conditions are just as important now as inflation and the inflation outlook. Fed funds futures fully discounted a September rate cut on Thursday on the CPI news even if initial unemployment claims tumbled 17K to a less worrisome 222K in the July 6 week.

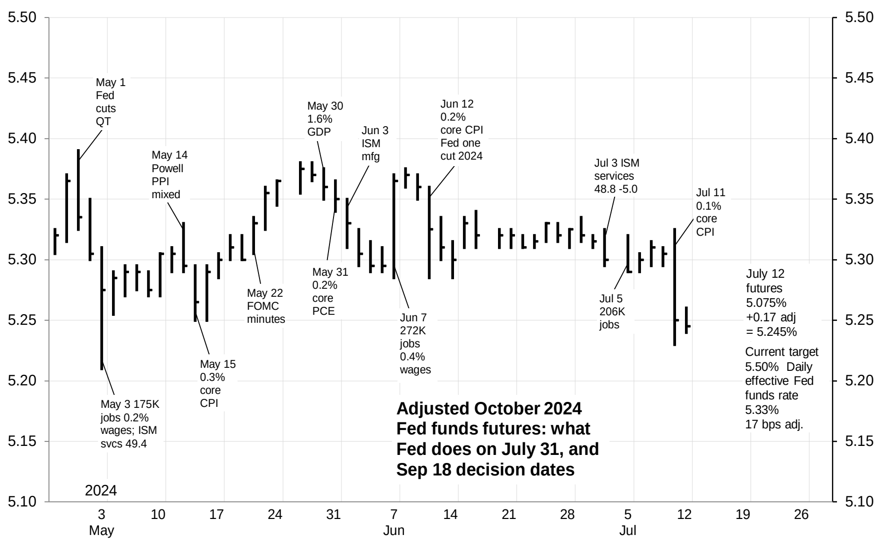
Selected Fed assets and liabilities

Fed H.4.1 statistical release billions, Wednesday data	10-Jul	3-Jul	26-Jun	19-Jun	3/11/20*	Change from 3/11/20 to Jul 10
Factors adding reserves						
U.S. Treasury securities	4438.095	4437.894	4453.571	4453.071	2523.031	1915.064
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	2335.997	2335.997	2335.997	2354.640	1371.846	964.151
Repurchase agreements	0.001	0.004	0.001	0.001	242.375	-242.374
Primary credit (Discount Window)	6.803	6.404	7.026	6.683	0.011	6.792
Bank Term Funding Program	105.998	106.284	106.556	107.338		
FDIC Loans to banks via Fed	0.000	0.000	0.000	0.000		
Paycheck Protection Facility	2.788	2.801	2.847	2.855		
Main Street Lending Program	11.199	11.186	11.173	11.159		
Municipal Liquidity Facility	0.000	0.000	0.000	0.000		
Term Asset-Backed Facility (TALF II)	0.000	0.000	0.000	0.000		
Central bank liquidity swaps	0.122	0.211	0.124	0.120	0.058	0.064
Federal Reserve Total Assets	7275.3	7272.3	7282.3	7303.8	4360.0	2915.289
~~3-month Libor %~~ SOFR %	5.34	5.33	5.34	5.33	1.15	4.190
Factors draining reserves						
Currency in circulation	2356.054	2358.292	2352.646	2351.912	1818.957	537.097
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	722.328	745.608	744.206	782.158	372.337	349.991
Treasury credit facilities contribution	4.958	4.958	4.958	4.958		
Reverse repurchases w/others	422.147	425.898	490.156	375.542	1.325	420.822
Federal Reserve Liabilities	3934.269	3950.087	4013.355	3937.622	2580.036	1354.233
Reserve Balances (Net Liquidity)	3341.046	3322.165	3268.895	3366.166	1779.990	1561.056
Treasuries within 15 days	62.997	63.469	46.454	27.742	21.427	41.570
Treasuries 16 to 90 days	206.784	202.631	219.055	237.783	221.961	-15.177
Treasuries 91 days to 1 year	534.437	538.099	535.109	534.963	378.403	156.034
Treasuries over 1-yr to 5 years	1471.206	1471.141	1489.439	1489.256	915.101	556.105
Treasuries over 5-yrs to 10 years	646.240	646.217	647.692	647.626	327.906	318.334
Treasuries over 10-years	1516.431	1516.338	1515.822	1515.701	658.232	858.199
Note: QT starts June 1, 2022	Change	7/10/2024	6/1/2022			
U.S. Treasury securities	-1332.684	4438.095	5770.779			
Mortgage-backed securities (MBS)	-371.449	2335.997	2707.446			

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

Powell answered a question saying the Fed did not require inflation to fall to exactly 2.0% before cutting interest rates the first time, which confirms the FOMC rates and inflation forecasts. They have penciled in a 4.25% Fed funds rate, 125 bps of cuts by the end of 2025 when core PCE inflation comes down to 2.3% in Q4 2025. If core PCE is unchanged in June to be reported Friday, July 26, its year-on-year rate will be 2.4%.... something's gotta give.

Fed Policy-key variables	2024	2025	2026	Long Term
Fed funds	5.1	4.1	3.1	2.8
PCE inflation	2.6	2.3	2.0	2.0
Core inflation	2.8	2.3	2.0	
Unemployed	4.0	4.2	4.1	4.2
GDP	2.1	2.0	2.0	1.8
June 2024 median Fed forecasts				



October Fed funds futures discount 25 bps of a 25 bps rate cut (100%) on September 18. Two and a half 25 bps rate cuts are discounted this year.

Fed funds futures call Fed policy

Current target: July 12 -- 5.50%

Rate+0.17	Contract	Fed decision dates
5.485	Aug 2024	July 31
5.250	Oct 2024	Add Sep 18
4.855	Jan 2025	Add Nov 7, Dec 18*

Last trade, not settlement price

* Not strictly true, Jan 2025 contract has Jan 29 as the expected Fed decsion date

Next up: June PCE inflation report Friday, July 26

Monthly						2024	2023								2023
% Changes	May	May	Apr	Mar	Feb	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	Apr
Core CPI inflation	0.1	0.2	0.3	0.4	0.4	0.4	0.3	0.3	0.2	0.3	0.2	0.2	0.2	0.4	0.5
Core PCE inflation		0.1	0.3	0.3	0.3	0.5	0.2	0.1	0.1	0.3	0.1	0.1	0.2	0.3	0.3
Core PCE YOY		2.6	2.8	2.8	2.8	2.9	2.9	3.2	3.4	3.6	3.7	4.2	4.3	4.7	4.8
Core CPI YOY	3.3	3.4	3.6	3.8	3.8	3.9	3.9	4.0	4.0	4.1	4.3	4.7	4.8	5.3	5.5

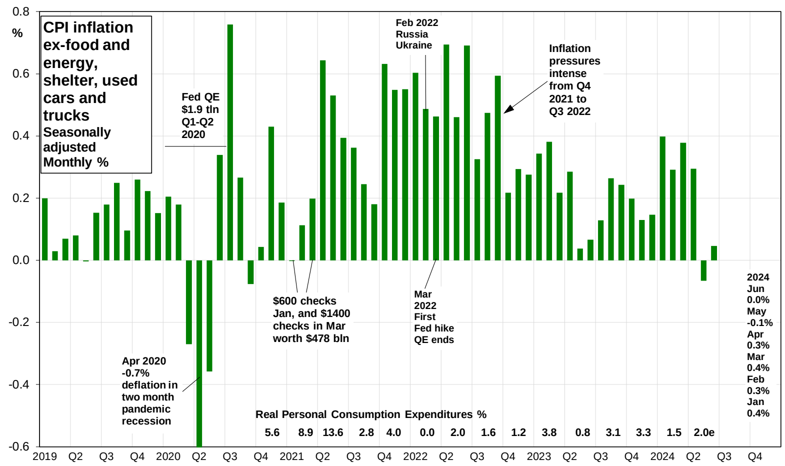
OTHER ECONOMIC NEWS

No inflation, fewer layoffs (Thursday)

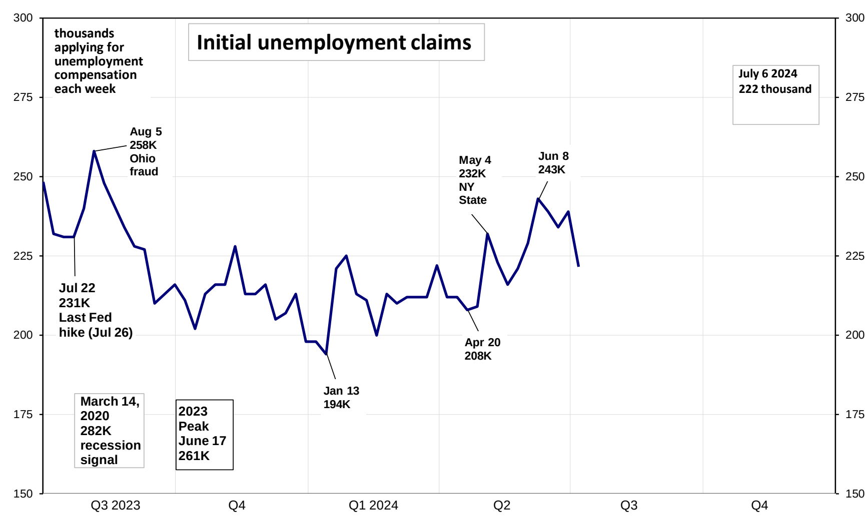
Breaking economy news. CPI and jobless claims. First jobless claims as they unexpectedly fell 17K in the July 6 week to 222K which is not holding onto the recession spike through much of June. The seasonal factors are aggressive in subtracting away not seasonally adjusted filings because of seasonal temporary auto plant closures which do not happen always. Claims did rise 10,540 in Michigan, but the total level of layoffs nationwide did not change from the prior week. We will see. The auto plant offset seasonal factor will remain for one more week.

Dec 23 Weight	CPI inflation	Monthly Percent Changes Apr 2024	May 2024	Jun 2024	YOY % Jun 2024
100.0	Total	0.3	0.0	-0.1	3.0
13.555	Food	0.0	0.1	0.2	2.2
5.388	Food away from home	0.3	0.4	0.4	4.1
6.655	Energy	1.1	-2.0	-2.0	1.0
79.790	Ex-food & energy	0.3	0.2	0.1	3.3
3.684	New vehicles	-0.4	-0.5	-0.2	-0.9
2.012	Used cars/trucks	-1.4	0.6	-1.5	-10.1
2.512	Clothing	1.2	-0.3	0.1	0.8
1.489	Medical care goods	0.4	1.3	0.2	3.1
36.191	Shelter	0.4	0.4	0.2	5.2
26.769	Owner equiv. rent	0.4	0.4	0.3	5.4
6.294	Transportation	0.9	-0.5	-0.5	9.4
6.515	Medical care services	0.4	0.3	0.2	3.3
	Special: Where inflation might come back down to				
60.899	Services ex-energy	0.4	0.2	0.1	5.1
18.891	Commodities (core)	-0.1	0.0	-0.1	-1.8

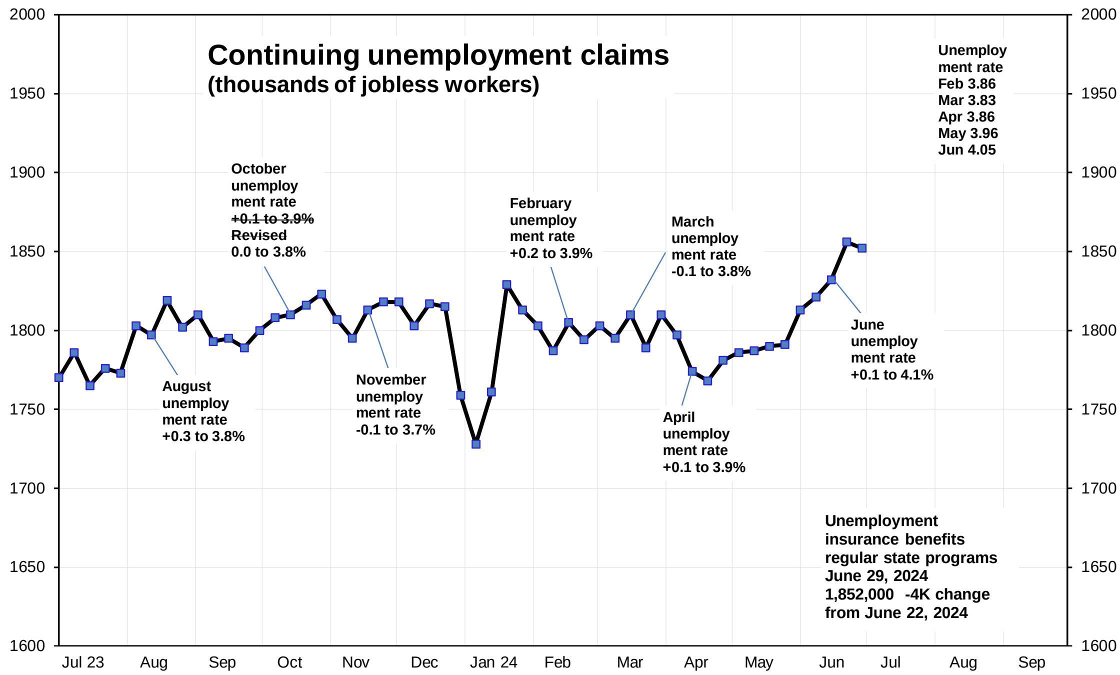
Away from recession that jobless claims keep hinting is just around the corner, before deciding job layoffs were not building after all, besides recession, CPI inflation was better than expected. Headline CPI fell one-tenth and is up 3.0% year-on-year. Core CPI rose just 0.1% and is rising 3.3% year-on-year. Extra core inflation that Greenspan liked, subtracting out used cars and trucks and shelter, has slowed dramatically in May and June, just like it did in 2023, which should give the Fed the confidence they need to cut rates in September.



Net, net, inflation is falling like a stone which all but assures a first rate cut by the Federal Reserve at the September meeting. It's not just commodity prices anymore as the modest 0.2% increase in shelter prices was cut in half from the trend in prior months this year. Meanwhile, the looming recession clouds remain offshore for now with a significant drop in first-time jobless claims with the caveat that the July 6 week is one of the biggest national holidays of the year and the seasonal factors may have gotten the adjustment wrong. It is the first week in the new quarter when companies tend to announce new layoffs, but not seasonally adjusted claims were little changed at 241,045. Continuing claims remain high at 1.852 million in the



June 29 week, a drop of 4K from the week before. Markets were looking for good inflation news and they got it. Inflation isn't dead, but there was none the last two months which means Fed officials can loosen up the tourniquet of recession-level interest rates around the economy's neck. Stay tuned. There is light at the end of the tunnel finally after the central bank's long battle with inflation and interest rate cuts, lots of them, are on the way. Bet on it. The stock market is. The risks Powell cited in testimony yesterday are better balanced than ever this morning with inflation pressures easing and the labor market still on the cooler side.



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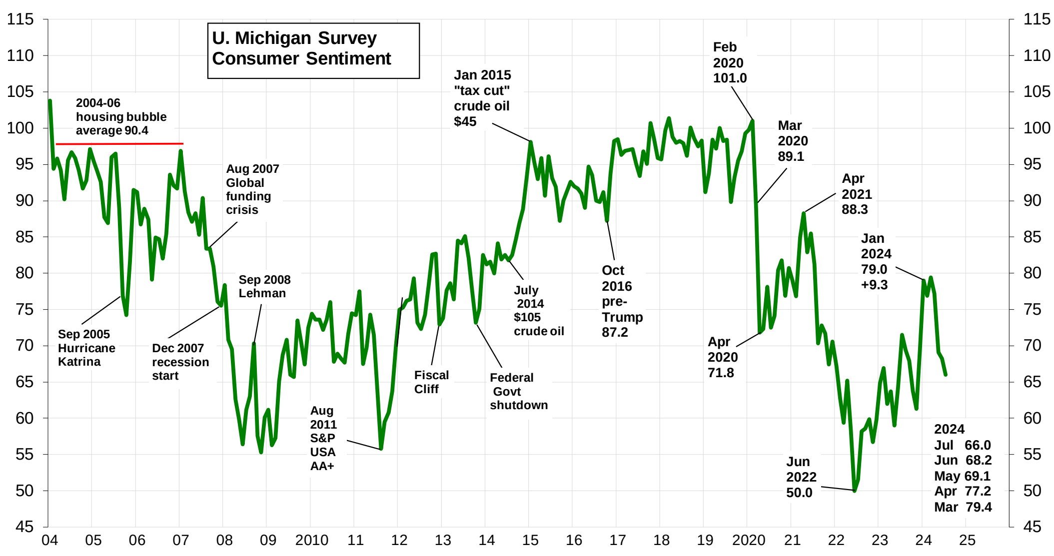
PPI inflation better than early in year (Friday)

Breaking economy news. PPI inflation rose 0.2% which is progress from the big increases at the start of this year, but perhaps it should have been an even softer report given the sharp downward adjustment in energy prices for a second month. The manufacturing sector is in recession according to some and at best moving sideways based on industrial production and durable goods orders so the softness in factory prices is consistent with sluggish activity and diminished demand. Final demand services prices jumped 0.6% in June thanks to the sharp 1.9% rise in Trade, which is keeping total final demand price inflation positive. We have to keep reading the definition each month because it is hard to see with the naked eye why this is a worry for the inflation outlook: “Trade indexes measure changes in margins received by wholesalers and retailers.” Glad to see their margins are increasing. They deserve it.

	PPI Final demand goods less foods/energy-- Monthly Percent Changes SA											
	Jan	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
2023	0.6	0.3	0.2	0.1	0.1	-0.1	0.0	0.1	0.3	0.1	0.1	0.1
2024	0.3	0.3	0.0	0.2	0.2	0.0						
	PPI Final demand goods less foods/energy-- Year/Year Percent Changes NSA											
	Jan	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
2023	5.6	5.1	4.3	3.3	2.7	2.0	1.9	1.8	2.1	2.1	2.0	1.9
2024	1.6	1.6	1.4	1.5	1.7	1.8						

Net, net, producer price pressures are receding but the trend is more of a whimper than a bang. Old-fashioned PPI with its focus on commodities and goods (final demand goods) went nowhere if we strip out volatile foods and energy, and on a year-to-year basis, it has been under 2% for all of 2024 including 1.8% in the latest month of June reported today. There does not appear to be much inflation pressure percolating on the factory floors that might affect the CPI prices that consumers pay at the shops and malls. Many PPI prices go into the calculation of PCE inflation with the June report due out on Friday, July 26. Offices of physicians prices fell 0.4% in June after jumping 0.8% in May although May core PCE only increased 0.083%, so perhaps core PCE is unchanged in June? The costs of transportation and warehousing for personal consumption goods also fell 0.9% in June, perhaps reflecting the dramatic slowdown of real consumer spending in the first half of 2024. On the other hand, bank deposit services prices soared this month just like it did the same month in 2023, not sure why that might be seasonal. Time to move money out to a money market fund anyway.



PS: Later this morning at 10am ET was the Michigan Survey of Consumer Sentiment which recorded a new low for the year. A downbeat consumer that questions the outlook is never good for anyone’s forecast of the economy. Consumer sentiment continues to slide from the peak in the first quarter of the year meaning the economy’s fabled soft-landing is not a reality yet. The economy is not out of the woods and a recession cannot be ruled out if the consumer does not cheer up. Stocks are at record highs, inflation and inflation expectations are lower, what on earth is worrying the consumer.

We hope it is not the upcoming election because that story and uncertainty will not be over until the vote on Tuesday, November 5. Job layoffs have come back down in the recent week, but if consumer confidence does not improve and their spending picks back up, companies may yet have to cut staff because of a decline in their revenues and sales. Stay tuned. The only one who seems to like the lackluster consumer sentiment data is the stock market which continues to retrace the surprise sell-off in tech companies yesterday.

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