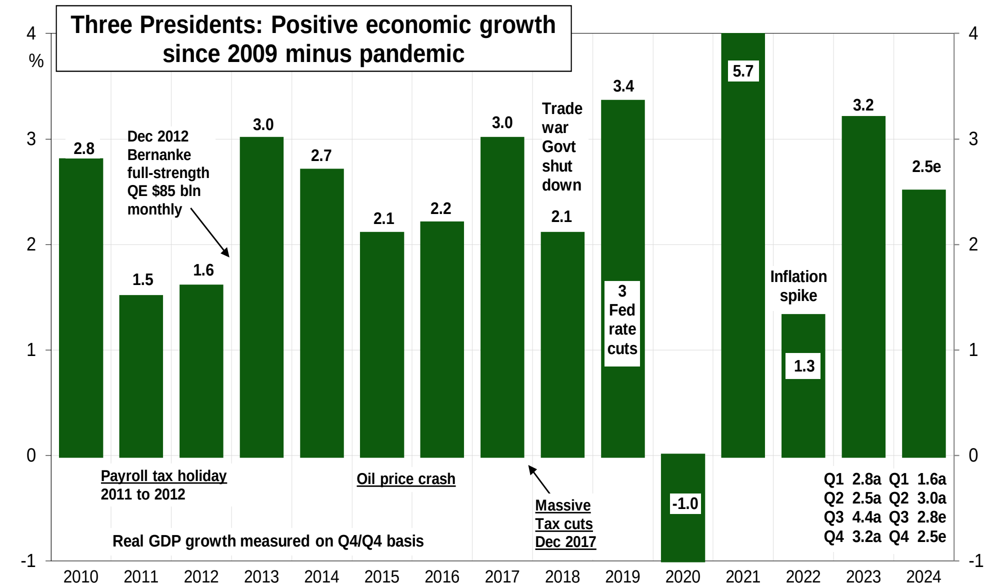
fwd: Bonds
Global Macro Hedge Strategy EconomicsTrading

Financial Markets This Week

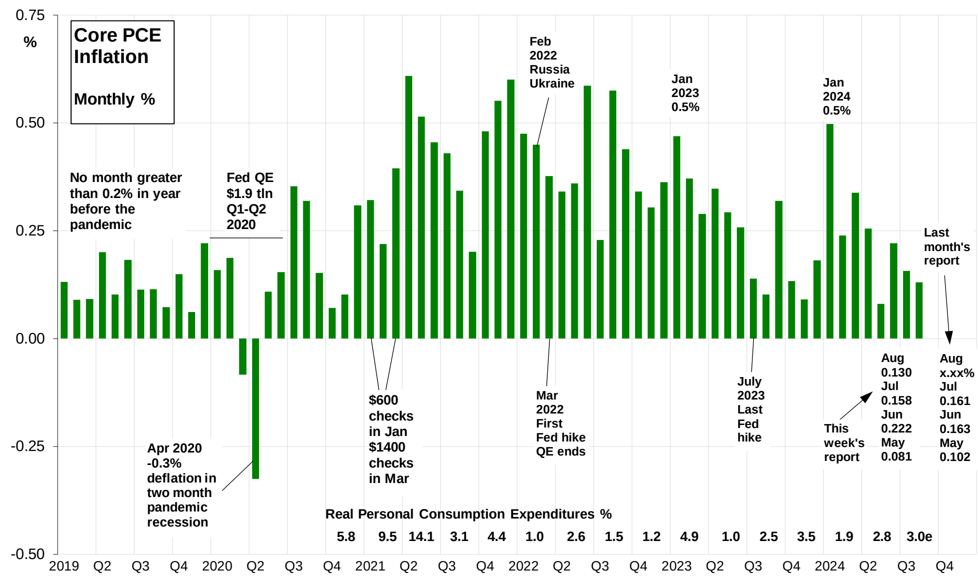
Christopher S. Rupkey, CFA
Chief Economist
crupkey@fwdbonds.com

27 SEPTEMBER 2024

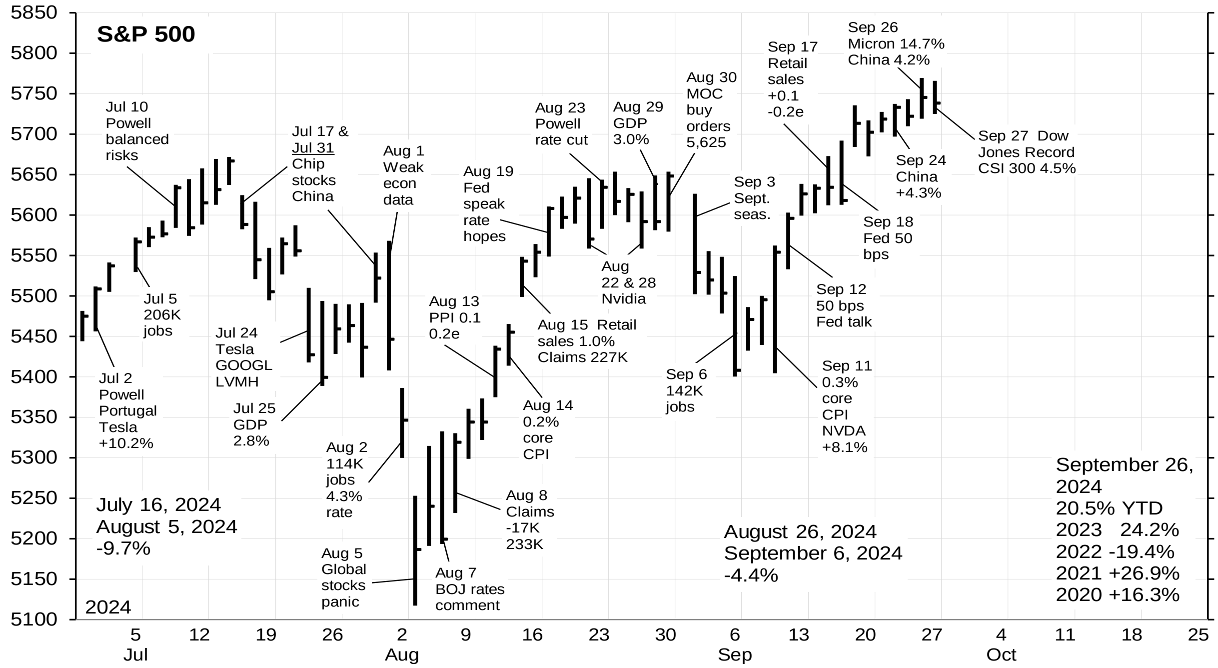
ECONOMY ROLLS ON



There was not a lot of excitement over the GDP benchmark revisions back to 2019 this week. Real GDP growth was stronger. Powell must be pleased that his three microtuning 25 bps rate cuts in 2019 from 2.5% to 1.75% is now matched up with a rebound in real GDP to 3.4% in 2019 (was 3.2%, hey every tenth counts). Powell pushed rates to the floor between meetings at the start of the pandemic in 2020, and that, and the $600 and $1400 checks in January and March 2021 pushed real GDP growth to 5.7% in 2021. Won't bore you with the revision there. People don't buy when prices are higher, "inflation," or when the Fed lifts rates to recession-magnitude levels, although real GDP is now 1.3% in 2022 revised from 0.7%. Nothing in the growth chart looks remotely like a recession. Job losses are recession-magnitude, but other countries have larger unemployment spikes without a downturn in their economies. Few live to tell the tale if payroll employment falls, so it will be interesting to see the September payroll jobs report on Friday, October 4. One thing is for sure and that is the Fed's focus has shifted from inflation to the labor markets. PCE headline inflation is back to 2.2% year-on-year, close enough for some at the Fed to take their eyes off of core PCE inflation of 2.7%. Stay tuned. The economy grew 3.2% in 2023 despite a 5.5% Fed funds rate, a 7% mortgage rate, $5 gasoline, a bank crisis, and now the Fed is easing.



INTEREST RATES



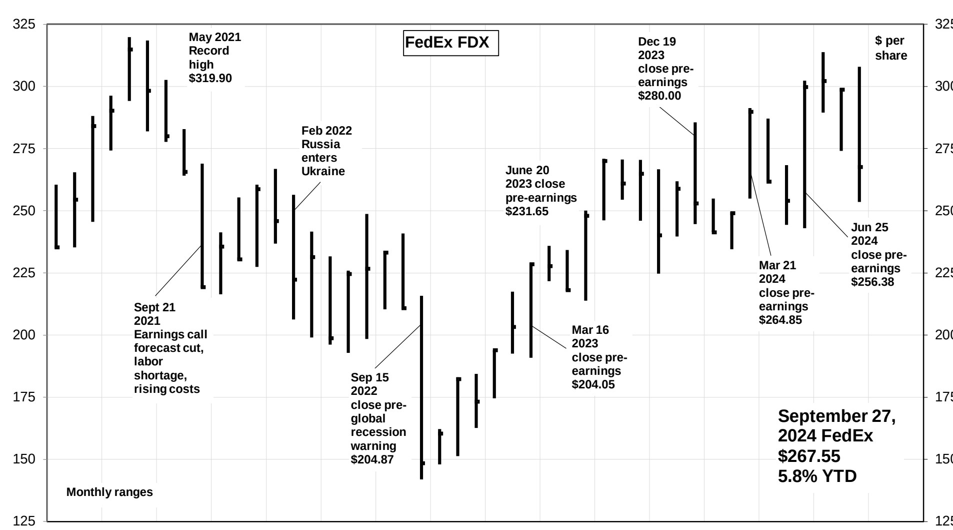
We may well change this website to Fwdstocks instead of Fwdbonds as expected returns are changing after Powell's Jackson Hole "the time has come" speech, especially for money market funds (3.5% next year, really). These stock returns have been about 20% for five years now (okay, minus 2022 Fed liftoff and Ukraine War year), which is almost what the stock market bubble looked like over twenty years ago during the dot.com boom. The 10-yr Treasury yield closed Friday at 3.75%, moving up and down modestly in the right direction of the news at least: down with lower consumer confidence on Tuesday, up with stronger economy, fewer Fed cuts, jobless claims of 218K Thursday, a long way from 250K recession-signal at the end of July, and falling back on Friday with core PCE inflation of 0.1%, and surprisingly applauded year-year headline PCE inflation of 2.2% versus 2.5% last month.

FedEx (FDX) up 5.8% YTD

The stock collapsed 15.2% to $254.64 the next day after the earnings report after the bell on Thursday, September 19. FedEx Ground and FedEx Services were merged into "Federal Express" this August 31 quarter, but it did not seem to help. Total operating income was $1.080 billion, down 27.3% from $1.485 billion a year ago. The company said there was lower US domestic priority package volume and increased wage and purchased transportation rates.

Operating Income $bln

Quarter	Total	Federal Express	FedEx Freight	Other; layoffs
8.31.24	1.080	0.953	0.439	-0.312
5.31.24	1.555	1.305	0.507	-0.257
2.29.24	1.243	1.173	0.341	-0.271
11.30.23	1.276	1.035	0.491	-0.250
8.31.23	1.485	1.306	0.482	-0.303



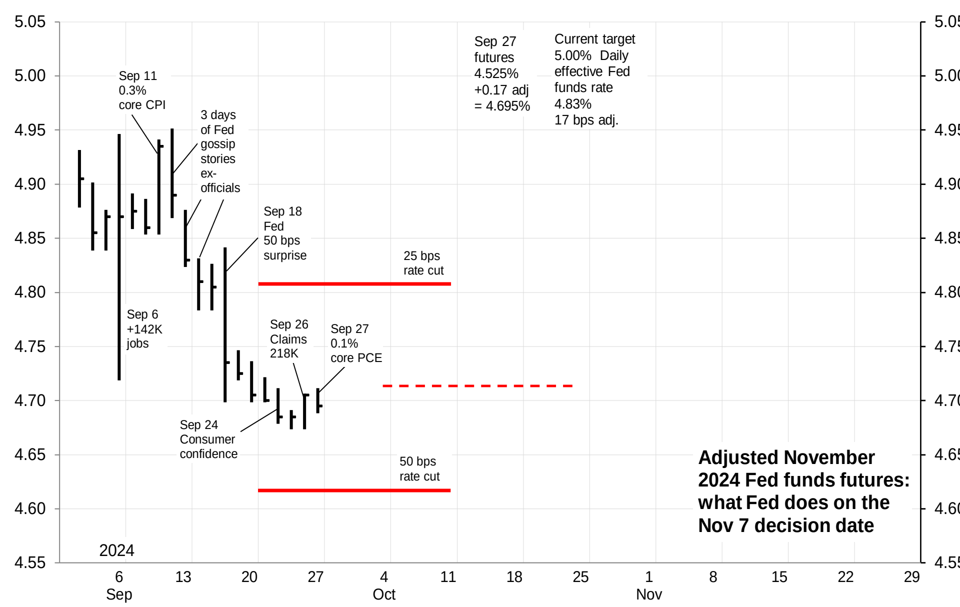
FEDERAL RESERVE POLICY

The Fed meets November 6-7, 2024 to consider its monetary policy. The September meeting and 50 bps rate cut must have been controversial because we cannot remember so many Fed officials coming out so quickly and telling the world how they voted and what they are likely to do at the final two meetings this year. Talk of measured and gradual steps ahead to stop Powell from pushing 50 bps again perhaps. Fed Governor Bowman even put out a statement of why she dissented on the Fed website. If the Fed forecasts are for 3.5% rates at the end of 2025 that could be accomplished with 25 bps cuts in November and December, then 25 bps every quarter in 2025, March, June, September, December forecasts meetings.

Selected Fed assets and liabilities						Change
Fed H.4.1 statistical release						from
billions, Wednesday data	25-Sep	18-Sep	11-Sep	4-Sep	3/11/20*	3/11/20
Factors adding reserves						to Sep 25
U.S. Treasury securities	4384.130	4384.005	4389.017	4388.817	2523.031	1861.099
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	2282.078	2299.730	2299.798	2299.798	1371.846	910.232
Repurchase agreements	0.061	0.000	0.009	0.000	242.375	-242.314
Primary credit (Discount Window)	1.365	1.376	1.568	1.517	0.011	1.354
Bank Term Funding Program	85.941	94.785	97.667	98.335		
FDIC Loans to banks via Fed	0.000	0.000	0.000	0.000		
Paycheck Protection Facility	2.333	2.415	2.459	2.497		
Main Street Lending Program	10.396	10.385	10.674	10.663		
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	0.153	0.157	0.137	0.137	0.058	0.095
Federal Reserve Total Assets	7131.3	7160.3	7166.2	7163.2	4360.0	2771.249
~~3-month Libor %~~ SOFR %	4.84	5.33	5.32	5.35	1.15	3.690
Factors draining reserves						
Currency in circulation	2350.597	2350.585	2353.156	2356.084	1818.957	531.640
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	778.910	839.398	725.577	771.047	372.337	406.573
Treasury credit facilities contribution	4.958	4.958	4.958	4.958		
Reverse repurchases w/others	416.193	305.831	279.215	337.312	1.325	414.868
Federal Reserve Liabilities	3989.709	3943.467	3806.461	3898.603	2580.036	1409.673
Reserve Balances (Net Liquidity)	3141.565	3216.822	3359.741	3264.604	1779.990	1361.575
Treasuries within 15 days	48.479	40.573	11.920	12.163	21.427	27.052
Treasuries 16 to 90 days	205.862	213.704	240.015	240.316	221.961	-16.099
Treasuries 91 days to 1 year	528.403	528.450	537.050	536.489	378.403	150.000
Treasuries over 1-yr to 5 years	1483.485	1483.428	1482.818	1482.687	915.101	568.384
Treasuries over 5-yrs to 10 years	590.665	590.649	590.261	590.245	327.906	262.759
Treasuries over 10-years	1527.237	1527.200	1526.953	1526.917	658.232	869.005
Note: QT starts June 1, 2022	Change	9/25/2024	6/1/2022			
U.S. Treasury securities	-1386.649	4384.130	5770.779			
Mortgage-backed securities (MBS)	-425.368	2282.078	2707.446			
**March 11, 2020 start of coronavirus lockdown of country						

Powell said 50 bps was not the new pace in the press conference, but maybe only because he does not yet have the “votes” with the September forecasts showing nine votes for 4.5% (25 bps in November and December) and seven votes for just one 25 bps cut more to 4.75% at year-end. (One said 4.25%, three said 5.0%.) Powell answered a question by phrasing his own question, would they have cut rates at the July meeting if they had known the July employment report in advance, “We might well have,” he answered. The July employment report on Friday, August 2 two days after his press conference showed a two tenths jump in unemployment to 4.3%, and payroll jobs slowing to 114K in July (Jun 179K, May 216K, Apr 108K, Mar 310K). The stories on weakness have to be the same, unemployment rises, and payroll employment declines, eventually. Not there yet.

Fed Policy-key variables	2024	2025	2026	2027	Long Term
Fed funds	4.4	3.4	2.9	2.9	2.9
PCE inflation	2.3	2.1	2.0	2.0	2.0
Core inflation	2.6	2.2	2.0	2.0	
Unemployed	4.4	4.4	4.3	4.2	4.2
GDP	2.0	2.0	2.0	2.0	1.8
September 2024 median Fed forecasts					



November Fed funds futures are not a clean read on the odds as the meeting is during the month. Market odds favor a 50 bps cut.

Fed funds futures call Fed policy		
Current target: September 27 -- 5.00%		
Rate+0.17	Contract	Fed decision dates
4.205	Jan 2025	Nov 7, Dec 18*
4.900	Feb 2025	Adds Jan 29
Last trade, not settlement price		
* Not strictly true, Jan 2025 has Jan 29 Fed date, so 2 days could be a new interest rate		

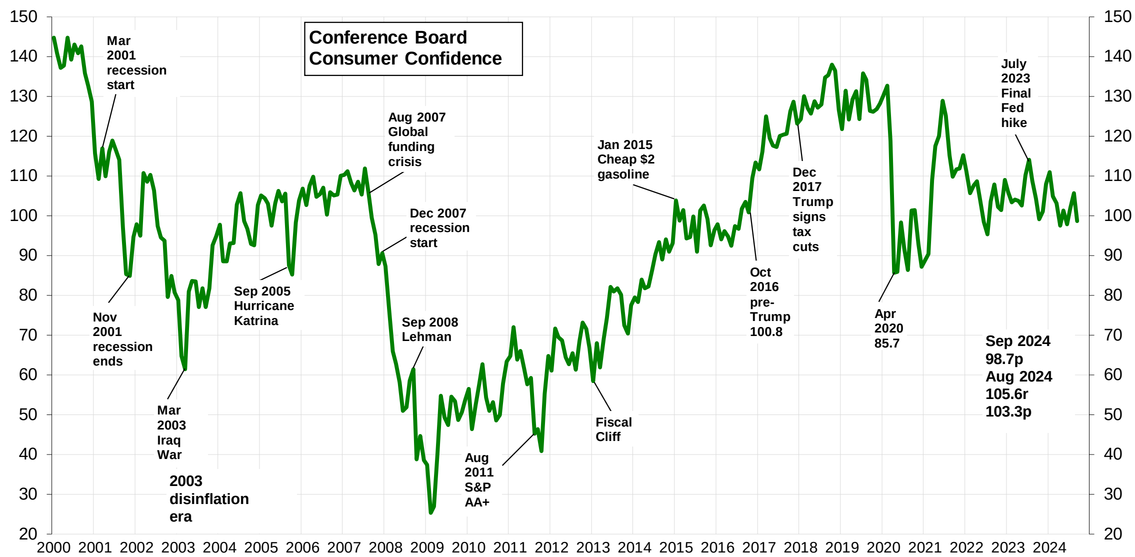
Next up: September CPI inflation report Thursday, October 10														
Monthly								2024	2023					2023
% Changes	Aug	Jul	Jun	May	Apr	Mar	Feb	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun
Core CPI inflation	0.3	0.2	0.1	0.2	0.3	0.4	0.4	0.4	0.3	0.3	0.2	0.3	0.2	0.2	0.2
Core PCE inflation	0.1	0.2	0.2	0.1	0.3	0.3	0.2	0.5	0.2	0.1	0.1	0.3	0.1	0.1	0.3
Core PCE YOY	2.7	2.6	2.6	2.7	2.9	3.0	2.9	3.1	3.0	3.2	3.4	3.7	3.8	4.3	4.4
Core CPI YOY	3.2	3.2	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

OTHER ECONOMIC NEWS

Confidence hits an air pocket (Tuesday)

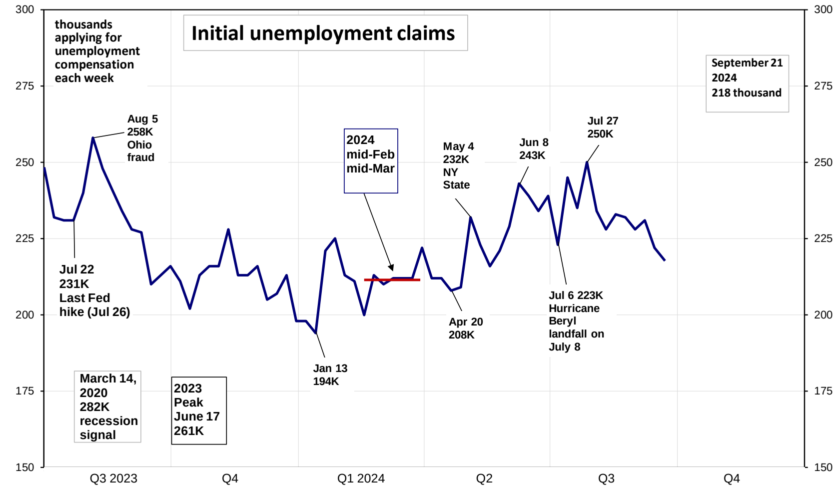
Breaking economy news. Consumer confidence fell 6.9 percentage points to 98.7 in September, back close to the lows earlier this year. Jobs do not seem to be as plentiful is the problem. The cutoff date was September 17 before the Fed's big news last week. There was a big turnaround, but keep in mind August had been revised significantly higher to 105.6 from the preliminary 103.3 level upon release a month ago. 18.8% thought business conditions were good, and 20.2% thought conditions were bad. 60% don't think at all. 30.9% thought jobs were plentiful versus 32.7% last month. 18.3% thought jobs were hard to get up from 16.8% last month.

Net, net, the consumer suddenly got a case of the shudders last month possibly due to changes in the wind for job opportunities. Consumers are expecting there will be fewer employment options ahead. It is the four-year election cycle and it probably isn't good for confidence if you are being told repeatedly that you are worse off than you were four years ago. The survey was completed before the Fed's surprise 50 bps rate cut last week so that may boost confidence knowing that policymakers are loosening their restraint that may have been holding back some sectors of the economy.The central bank would not be lowering rates aggressively if it believed inflation was a material threat to the economic outlook. Stay tuned. Consumers are not too depressed if they are out and about at the shops and malls and their purchases have been keeping economic growth near 3%.



More growth, inflation, fewer layoffs (Thursday)

Breaking economy news. Weekly jobless claims fell 4K to 218K in the September 21 week. The September 14 week was initially reported as 219K. The Boeing strike temporary furloughs started Monday, September 16 in small numbers, but jobless claims in Washington rose just 559 to 5,473 in the September 21 week. The third look at Q2 2024 real GDP was left at 3.0% with the annual update back to Q1 2019 this year.



Net, net, strength and resilience of the US economy is everywhere in the latest reports be it fewer weekly job layoffs or the upward revisions to economic growth with slightly faster inflation in the first half of the year. The Fed's strong start to unraveling its monetary restraint with an aggressive 50 bps rate cut may not continue if the economy's ship remains well away from the shoals of recession. You cannot have a recession without negative GDP growth and higher joblessness, and right now first-time jobless claims continue to fall from the highs at the end of July. Powell does not want to see the unemployment rate tick any higher and the weekly jobless claims data suggest this will not be the case.

Meanwhile, economic growth may have been little changed in the first half of this year, but the upward revisions to GDP growth in 2021 and 2022 were significant and show the economy came out of the pandemic stronger than expected. Real GDP in 2022 was 1.9% and now it is 2.5%, and growth in 2023 is 2.9% now versus 2.5% prior. The strength in economic demand may keep inflation from falling back to the 2.0% Fed target as quickly as policymakers think and indeed, year-on-year core PCE inflation is a tenth higher this year upon revision with increases of 3.0% and 2.7% in Q1 and Q2 2024, respectively. The bottom line is companies are not firing workers if first time applications for unemployment benefits fall to 218K in the September 21 week from 222K the week before and 231K the week before that. Joblessness is not rising, it is falling and that means the economy remains strong and the need for additional large rate cuts are questionable if the economy continues to move forward at a brisk pace.

U.S. Economy: Real GDP sector contribution

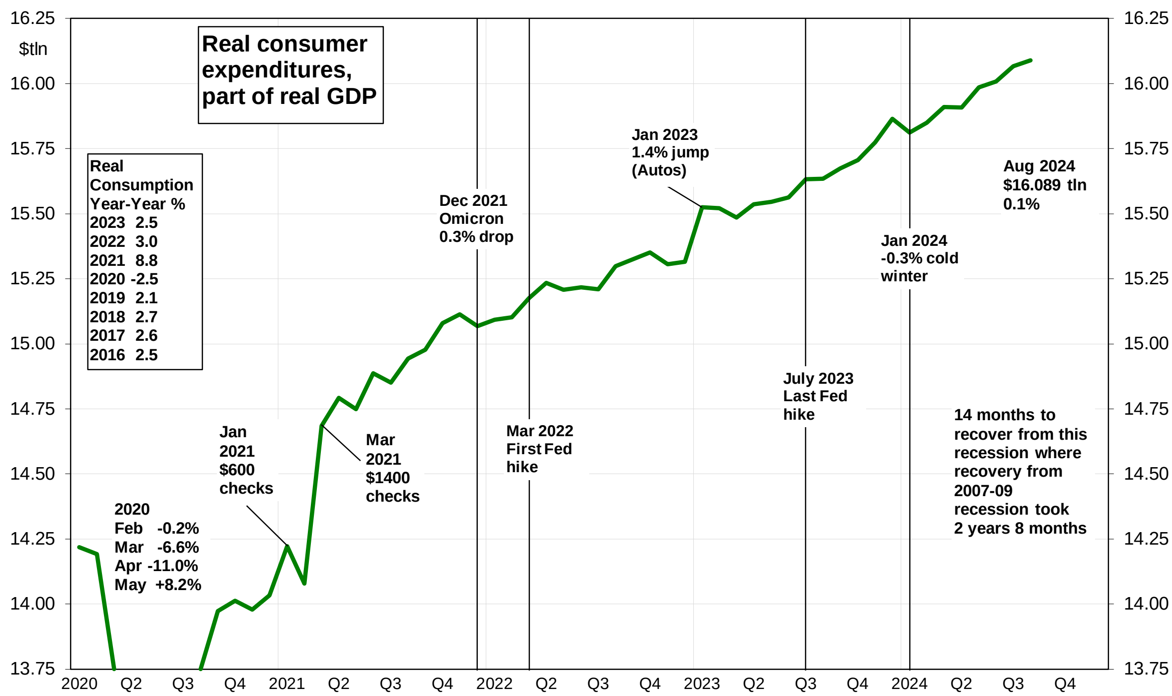
	Annual			Quarterly			
	2021	2022	2023	Q3 23	Q4 23	Q1 24	Q2 24
Real GDP growth %	6.1	2.5	2.9	4.4	3.2	1.6	3.0
Consumer spending %	8.8	3.0	2.5	2.5	3.5	1.9	2.8
Consumer Spending	5.8	2.1	1.7	1.7	2.3	1.3	1.9
Durables	1.3	-0.2	0.3	0.3	0.2	-0.1	0.4
Nondurables	1.2	0.0	0.1	0.4	0.5	-0.1	0.2
Services	3.3	2.2	1.3	1.0	1.6	1.6	1.3
Investment							
Business construction	-0.1	0.1	0.3	0.1	0.2	0.2	0.0
Business Equipment	0.3	0.2	0.2	-0.1	0.0	0.0	0.5
Intellectual Property	0.5	0.6	0.3	0.2	0.3	0.4	0.0
Residential construction	0.5	-0.4	-0.4	0.3	0.1	0.5	-0.1
Inventories	0.3	0.6	-0.4	1.3	-0.5	-0.5	1.1
Net exports	-1.3	-0.4	0.5	-0.1	0.1	-0.6	-0.9
Exports	0.7	0.8	0.3	0.5	0.7	0.2	0.1
Imports	-1.9	-1.2	0.2	-0.6	-0.6	-0.8	-1.0
Government	-0.1	-0.2	0.7	0.9	0.6	0.3	0.5
Federal defense	0.0	-0.2	0.1	0.2	-0.1	-0.1	0.2
Federal Nondefense	0.2	-0.1	0.1	0.1	0.0	0.1	0.0
State and local	-0.2	0.0	0.5	0.6	0.6	0.3	0.3

Percentage point contributions to GDP growth are below dark solid line

Economy rolls on (Friday)

Breaking economy news. The personal income report for August so you can judge how you are doing relative to your neighbors. Real consumer spending rose 0.1% in August, down from 0.5% in July, but it is stronger for the quarter as a whole. With the annual update to the GDP stats, real consumer spending was revised to 3.0% in 2022 from 2.5%, and 2023 is now 2.5% “normal” from 2.2% before. PCE headline inflation fell to 2.2% year-on-year in August from 2.5% in July, but core PCE remains higher at 2.7% year-on-year. Energy prices have either fallen or been unchanged since May.

Net, net, the economy continues to roll along not too fast to set off the demand sparks that lead to inflation and not too slow to have economists guessing whether the economy will slip over the cliff and into recession. In case you missed it, the savings rate was revised up in the benchmark GDP revision where it was 2.9% in July and now it is 4.9%, so consumers still have some gas in the tank to make extra purchases of goods and services that help make the economy go. Real consumer spending is running 2.9% in Q3 2024 with data through August which is about the same as 2.8% in the second quarter. Inflation came in a little better than market expectations with core PCE inflation increasing 0.1% in August and 2.7% year-over-year. Inflation is not dead yet so ostensibly there is no need for the Fed to rush ahead with another big 50 bps rate cut in November, although Powell may yet push his colleagues to a faster rebalancing of interest rates back to neutral which is around 3% in the Fed’s latest forecasts. Stay tuned. The economy and inflation are not too hot and not too cold at the moment which would be an ideal place for policy to be if only interest rates were not still up at levels meant to fight inflation. The stock market has lost track of where it wants interest rates and economic growth and inflation to be, but there is certainly no bad hard-landing news of recession or deflation in the reports today. Consumers have more savings than we thought and they might as well plow the money into equities as the rate on savings accounts will plunge to nearly 3% next year as the Fed unwinds the tightest monetary policy in two decades.



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.