Financial Markets This Week

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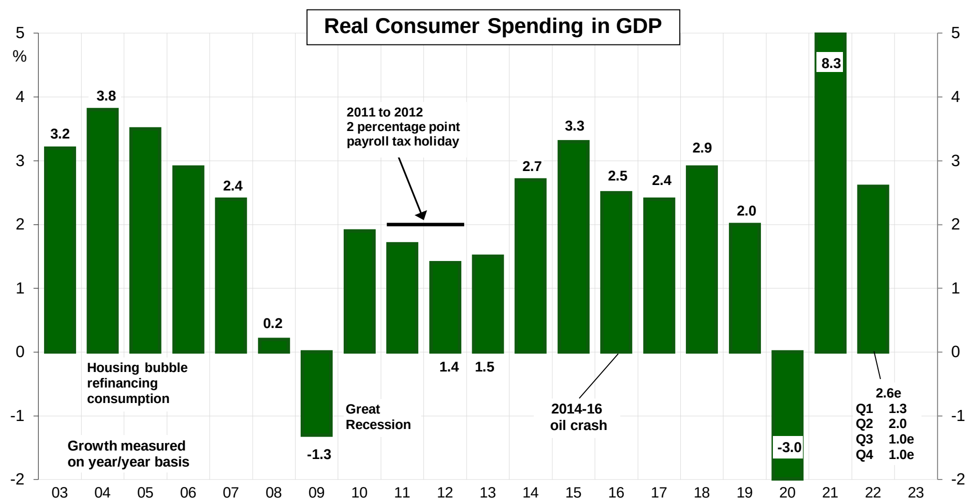
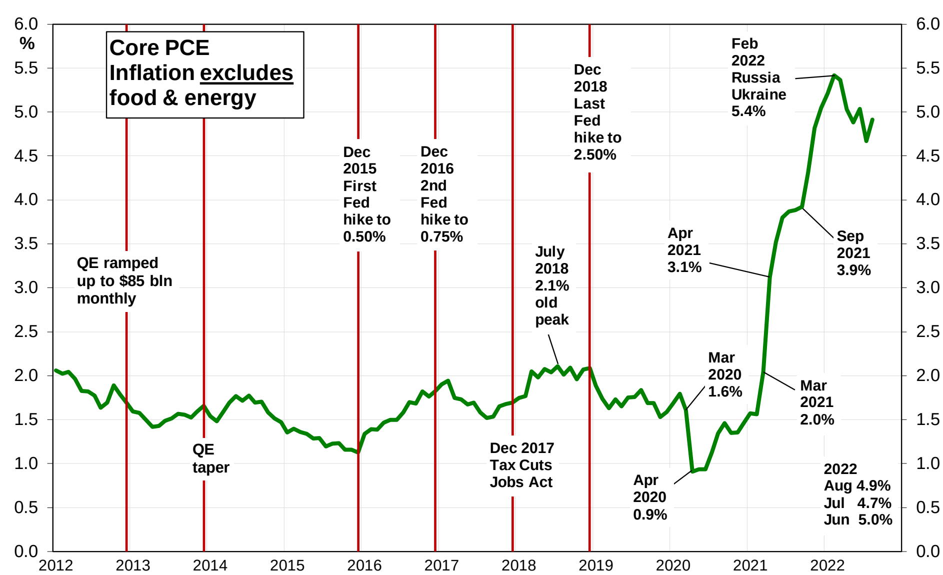
CONSUMER SPENDING SLOWS

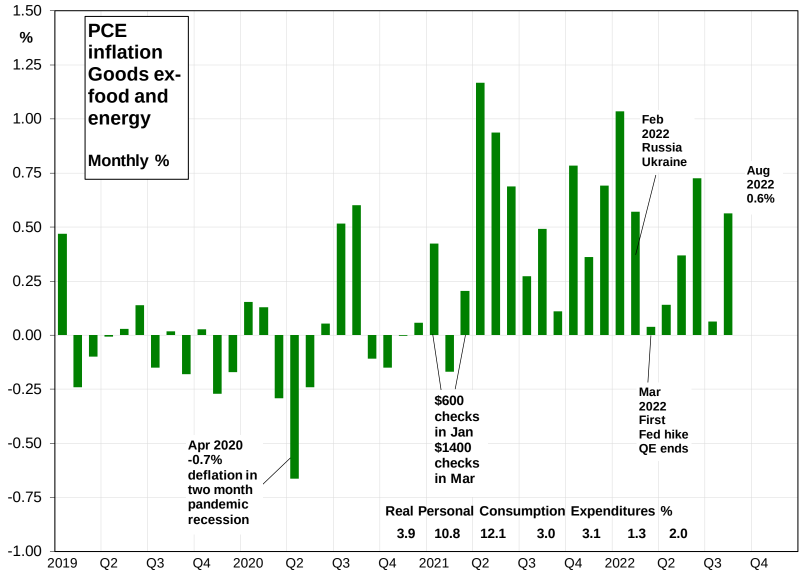
Consumer spending is slowing down. Whether reduced purchases will slow consumer inflation remains an open question. Inflation fell when consumption fell sharply in the recession years of 2008 and 2020, but 2007-09 was a deep recession that hopefully won't be repeated even with the Fed's rapid, too-late rate hikes this year. Core PCE inflation fell briefly in 2020 during the two-month pandemic recession. Real consumption expenditures will still be 2.6% in 2022 for the full year even with our estimates for 1.0% increases in Q3 and in Q4. The 8.3% rush to buy new goods with Federal stimulus checks in 2021 is still pushing up full year 2022 growth. Real consumption is normal historically. Consumption ran 2.4 to 3.3 percent from 2014 through 2018 no matter who was President. Fed officials were worried about deflation during that period, a needless concern in hindsight, even if core PCE inflation did get down close to 1.0% during the oil crash manufacturing recession from 2014-16.



The relationship between consumer inflation and consumer expenditures isn't all that close. We cannot say with certainty that the quarterly slowdown of GDP, if indeed our second half forecast is correct, will bring inflation to heel. But the Fed's QE stopped in March and the rate hikes began, and



the $600 and $1400 checks sent out in January and March 2021, respectively, have already been spent, so it seems reasonable to think core PCE inflation of 4.9% year-year in August 2022 will come down to the Fed's forecast of 3.1% in 2023. It better, otherwise the Fed under Powell will want to push the Fed funds rate even higher than the 4.75% forecast they have for 2023.



Why did the core PCE inflation monthly change on Friday match the 0.6% in core CPI released earlier this month on September 13? We don't know, it had been running less than CPI, but here are the gory details.

Dec 2021 Weight		Year-Year % Dec 2020	Dec 2021	Monthly % changes Jun 2022	Jul 2022	Aug 2022
1.000	PCE inflation	1.3	6.0	1.0	-0.1	0.3
0.075	Food at home	3.9	5.7	1.0	1.3	0.8
0.027	Energy goods	-15.1	47.1	10.1	-7.7	-10.0
0.016	Electricity/Gas	2.3	9.9	3.3	0.2	2.0
0.883	Core PCE	1.5	5.0	0.6	0.0	0.6
	Durable goods					
0.020	New vehicles	1.8	11.2	0.7	0.6	0.9
0.016	Used vehicles	10.1	36.2	1.6	-0.3	-0.1
0.030	Furnishings	3.1	8.8	0.5	0.3	0.6
0.037	Recreational	-0.9	1.3	0.8	-1.0	0.5
	Nondurable goods					
0.028	Clothing	-4.6	5.5	0.7	0.0	0.3
0.030	Prescription drugs	-2.4	0.0	0.1	0.3	0.4
0.010	Personal care	-0.3	0.3	0.8	1.1	1.4
0.644	Services ex-energy	2.0	4.6	0.6	0.0	0.6
0.036	Rents	2.3	3.3	0.8	0.7	0.7
0.112	Home prices	2.2	3.8	0.7	0.6	0.7
0.161	Health care	2.6	2.7	0.5	0.1	0.1
0.031	Transportation	-2.9	8.3	2.6	-1.7	1.9
0.035	Recreation	1.7	4.3	0.6	0.5	-0.2
0.059	Food services	4.3	6.8	0.7	0.6	0.7
0.011	Hotels/Motels	-8.0	20.8	-2.4	-2.3	0.1
0.080	Financial/Insurance	1.4	5.0	-0.2	-1.3	0.8
0.080	Other services	1.3	3.0	0.9	0.4	0.2
0.030	Nonprofits	3.7	13.0	0.1	0.0	1.7
	Year-year is Dec/Dec Percent Change					

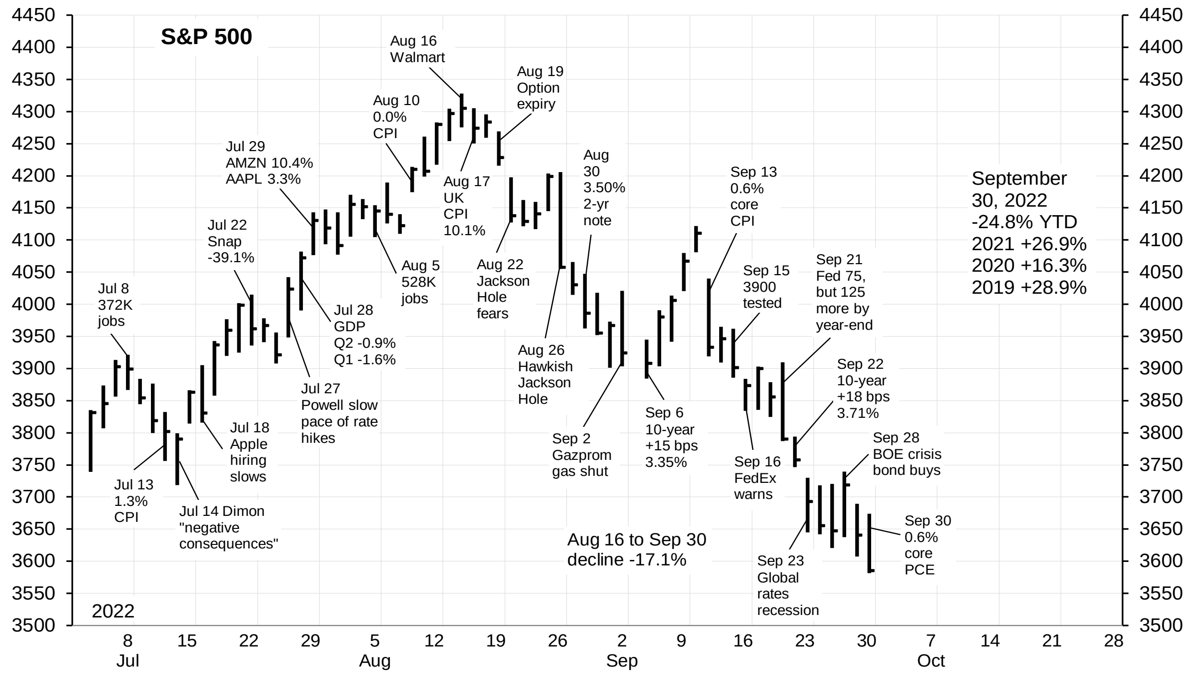
Several price categories dropped sharply in July and bounced back in August. Recreational goods -1.0% was computers mostly. Transportation services, airfares -5.7% July. Hotels/motels dropped 2.3% and then stabilized in August. Financial/Insurance dropped 1.3% in July and bounced in August: Portfolio management and investment advice fees were -7.4%, wonder why? Shelter prices, rents and home values are up big, but almost besides the point. More troubling are the prices the consumer sees most often like personal care products, hair, dental, shaving, bath, that look out of control the last two months. Groceries "Food at home" as well. The only good news this year for highly visible prices has been the sharp drop in gasoline, but the declines could be over. Gas was $3.487 in February when Russia was about to invade Ukraine, peaked at $5.007 on June 13 and is $3.711 this week.

Final thoughts, core PCE inflation matched core CPI inflation this month with a 0.6% increase. Stickier services prices ex-energy had been running less, sometimes significantly less in the PCE measure versus the CPI index for all this year until this month. It's early, but the Fed isn't winning so the stock market is losing. At least Health care inflation is minimal after huge increases in the early 2000s.

Core Consumer Inflation and stickier services prices ex-energy

Monthly % Changes	2022 Aug	Jul	Jun	May	Apr	Mar	Feb	2022 Jan	2021 Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	2021 Apr
Core CPI inflation	0.6	0.3	0.7	0.6	0.6	0.3	0.5	0.6	0.6	0.5	0.6	0.3	0.2	0.3	0.8	0.7	0.9
Services x-energy	0.6	0.4	0.7	0.6	0.7	0.6	0.5	0.4	0.3	0.4	0.4	0.2	0.1	0.3	0.4	0.4	0.5
Core PCE inflation	0.6	0.0	0.6	0.4	0.3	0.4	0.4	0.5	0.5	0.5	0.4	0.2	0.3	0.4	0.5	0.5	0.6
Services x-energy	0.6	0.0	0.6	0.4	0.4	0.5	0.3	0.3	0.5	0.6	0.3	0.2	0.3	0.4	0.4	0.4	0.4

INTEREST RATES



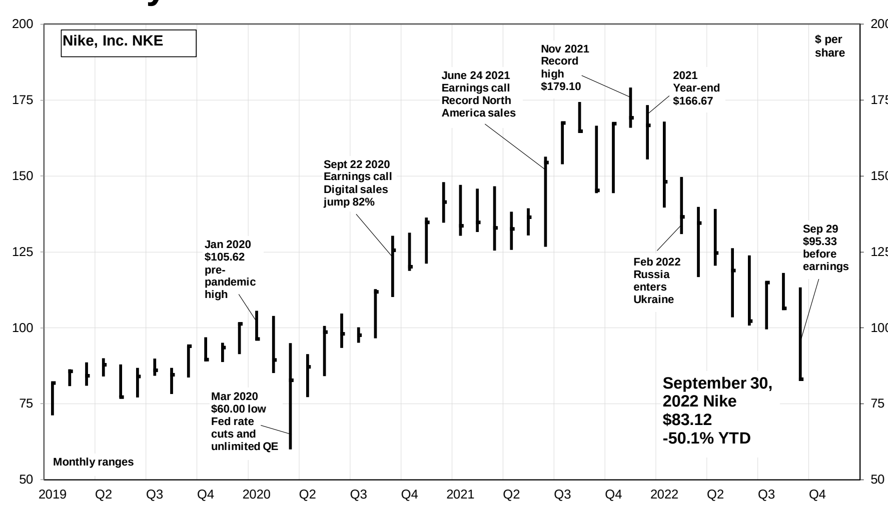
We must be missing something. This is what a financial crisis looks like. Only the Fed caused it. Trying to out Volcker Volcker. The S&P 500 on Friday seconds before the close was down 25.6% from the high of the year. During the Volcker years there were two recessions in the early 80s and two stock market plunges: a 21.6% loss in 1980; it came back, made a new high, then fell 28.0% during the 1981-82 recession. This isn't working. The economy isn't even in a recession yet. The stock market is too sensitive to the Fed's communications. Fed officials saying once they get to 4.75% the Fed funds rate will stay up there a long, long time. We aren't sure how you explain to the American people why the stock market is down 25%. The bond market. The 30-year Treasury auctioned in November 2021 is down 28.6% in value. Financial assets down with home prices next. If there isn't price stability, the economy does not work for anyone, Powell said. But crashing the stock market doesn't either.

Nike, Inc. (NKE) shares cut in half this year

Nike closed down 12.8% Friday at $83.12 after its latest earnings report. This is the second quarter that talked about higher inventories. Nike was $110.50 before last quarter's call. Net income was $1.468 billion in the August 31, 2022 quarter down 22% from last year.

Nike Footwear Sales ($millions)

Fiscal Quarter	Quarter	North America	Europe (EMEA)	Greater China	Asia Pac LatAm
Q1 2023	8.31.2022	3,805	2,012	1,233	1,064
Q4 2022	5.31.2022	3,580	2,030	1,178	1,197
Q3 2022	2.28.2022	2,532	1,569	1,554	1,005
Q2 2022	11.30.2021	2,852	1,806	1,235	887
Q1 2022	8.31.2021	3,264	1,983	1,449	1,022
Q4 2021	5.31.2021	3,793	1,831	1,316	1,007
Q3 2021	2.28.2021	2,382	1,606	1,614	903
Q2 2021	11.30.2020	2,512	1,731	1,567	991
Q1 2021	8.31.2020	2,957	1,802	1,251	758



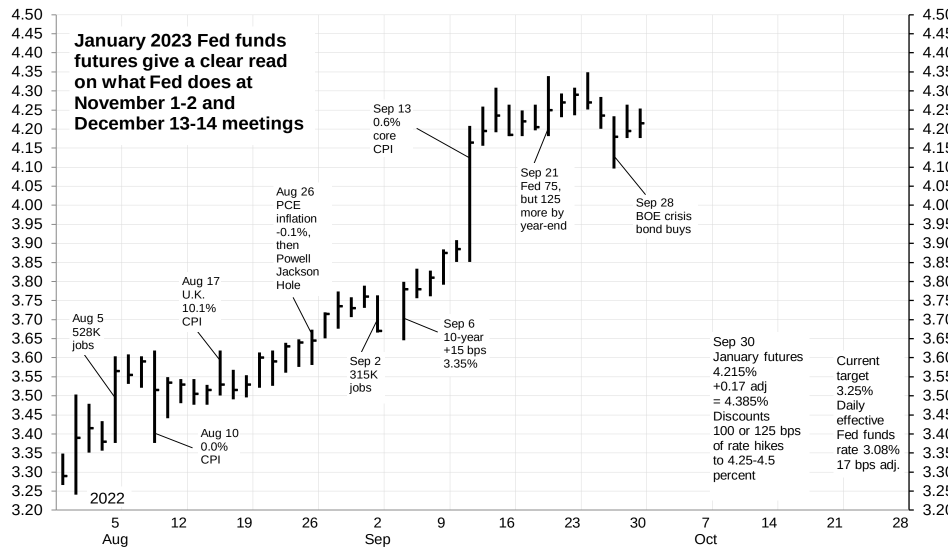
North America footwear is up 17% from last year. Real PCE "shoes" purchases jumped 1.1% in the August personal income report on Friday.

FEDERAL RESERVE POLICY

Selected Fed assets and liabilities						Change
Fed H.4.1 statistical release						from
billions, Wednesday data	28-Sep	21-Sep	14-Sep	7-Sep	3/11/20*	3/11/20
Factors adding reserves						to Sep 28
U.S. Treasury securities	5671.848	5673.919	5687.031	5690.760	2523.031	3148.817
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	2698.158	2714.887	2718.526	2709.291	1371.846	1326.312
Repurchase agreements	0.001	0.000	0.000	0.005	242.375	-242.374
Primary credit (Discount Window)	6.470	6.913	6.158	3.677	0.011	6.459
Paycheck Protection Facility	14.030	14.175	14.399	14.744		
Main Street Lending Program	25.704	25.687	25.969	25.950		
Municipal Liquidity Facility	5.563	5.561	5.559	5.558		
Term Asset-Backed Facility (TALF II)	2.149	2.148	2.146	2.145		
Central bank liquidity swaps	0.216	0.273	0.203	0.197	0.058	0.158
Federal Reserve Total Assets	8844.9	8866.7	8882.6	8872.2	4360.0	4484.875
~~3-month Libor %~~ SOFR %	2.98	2.25	2.27	2.28	1.15	1.830
Factors draining reserves						
Currency in circulation	2278.657	2277.468	2280.792	2284.279	1818.957	459.700
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	661.920	690.286	617.997	582.921	372.337	289.583
Treasury credit facilities contribution	17.940	17.940	17.940	17.940		
Reverse repurchases w/others	2366.798	2315.900	2225.579	2206.987	1.325	2365.473
Federal Reserve Liabilities	5861.695	5862.936	5723.910	5600.835	2580.036	3281.659
Reserve Balances (Net Liquidity)	2983.206	3003.721	3158.694	3271.336	1779.990	1203.216
Treasuries within 15 days	92.355	85.002	52.038	48.969	21.427	70.928
Treasuries 16 to 90 days	316.644	325.495	358.104	366.228	221.961	94.683
Treasuries 91 days to 1 year	813.531	814.092	810.627	809.289	378.403	435.128
Treasuries over 1-yr to 5 years	1993.540	1993.545	2010.470	2010.475	915.101	1078.439
Treasuries over 5-yrs to 10 years	1000.920	1000.924	1000.928	1000.932	327.906	673.014
Treasuries over 10-years	1454.857	1454.861	1454.864	1454.868	658.232	796.625
Note: QT starts June 1	Change	28-Sep	1-Jun			
U.S. Treasury securities	-98.931	5671.848	5770.779			
Mortgage-backed securities (MBS)	-9.288	2698.158	2707.446			
**March 11, 2020 start of coronavirus lockdown of country						

The Fed meets November 1-2, 2022 to consider its monetary policy. Wasn't a great week to be a Fed official. The stock market crashed with no response. At 230pm ET Friday, February 28, 2020 during a sharp stock market sell-off of over 10% for the week on coronavirus fears, Powell sent out his own "closely monitoring" statement. The following Monday, the Fed cut rates 50 bps to 1.25%. Not a peep this time. The S&P 500 closed Friday down 24.8% for the year.

This week there were some pointed questions from the press about "financial stability" after the Bank of England made emergency purchases of bonds during a markets crisis earlier in the week. 10-year Gilts closed 3.5% on Thursday, September 22 and were as high as 4.61% on Wednesday, September 28 before the crisis intervention.



Fed Vice Chair Brainard spoke at a research conference on global financial stability on Friday in New York. She said they wouldn't reverse the rate hikes prematurely, helping to drive the stock market lower. We guess that means the series of 25 bps rate cuts the FOMC is forecasting (3 in 2024, 4 in 2025) won't happen if 4.9% core PCE inflation doesn't come down to 3.1% next year. It remains to be seen if monetary policy's rapid rate hikes can bring down inflation as fast as the Fed wants. It took many years to bring down the double-digit inflation at the start of the 80s. The Fed basically needs some luck.

The interest rate sensitive sectors of the economy aren't responding to the Fed's too-late rate hikes to correct the biggest mistake in modern economic history. Shelter prices, rents and home prices, are up strong the last few months. It took the Greenspan/Bernanke measured rate hikes two years to reach the 5.25% peak in June 2006. The year-year CPI shelter inflation peaked at 4.3% in February 2007 and didn't drop to 2.5% until the Great Recession and financial crisis intensified in mid-2008. CPI shelter is currently 6.3% year-year and still rising. Other interest-rate sensitive sectors like the prices of cars and light trucks obviously aren't slowing. Home sales generally are down, but furniture rose 0.5% in August after rising 13.8% in 2021. Large household appliances are down at least by 1.5% in August after rising 8.5% last year. Stay tuned. Unsure where this is all going to end, but if the stock market is down 25%, something isn't working.

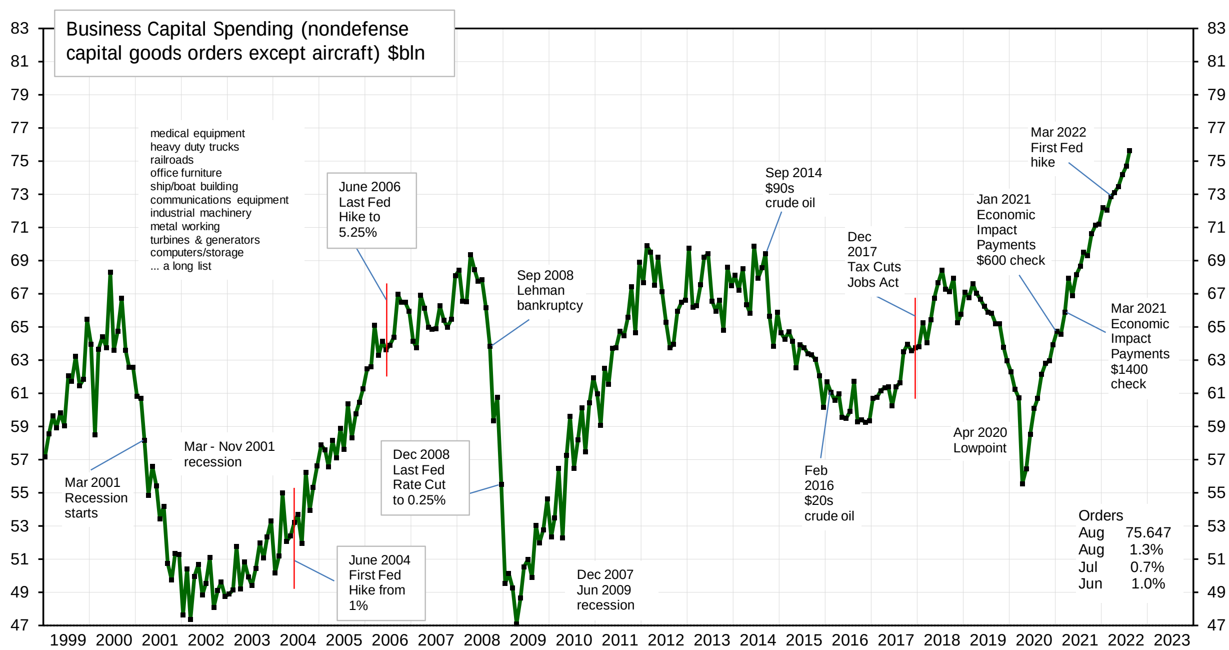
OTHER ECONOMIC NEWS

Business orders don't jump in recessions (Tuesday)

Breaking economy news. No sign yet that businesses are scaling back their equipment purchases on concerns about the economy. You won't find the word recession written anywhere in today's report on business durable goods orders. While it is true that equipment orders are higher in part due to inflation, it is also true that orders do fall sharply in recessions historically as businesses cut back.

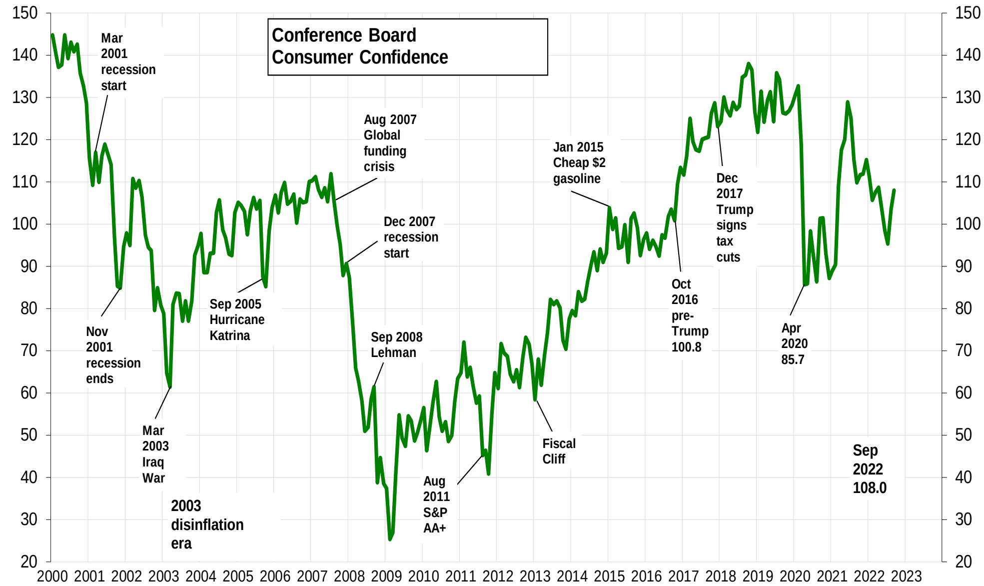
Nondefense capital goods orders ex-aircraft hit another record in August rising 1.3% to $75.6 billion in this month. This is not a one-off, this is the trend. These orders rose 1.0% in June and 0.7% in July. The monthly proxy for business capital spending was red hot this summer setting a blistering pace. Business spending on equipment may just keep real GDP from turning negative for a third consecutive quarter. This assumes that Thursday's benchmark revision to the first half of this year will continue to find that real GDP indeed dropped: -1.6% in Q1 and -0.6% in Q2.

Net, net, there is no sign yet of order cancellations for long-lived core durable goods orders for machinery, communications and electrical equipment. It is hard to know whether companies are ordering up more widgets to produce the goods and provide the services for a stronger economy in the future or whether the jump in spending reflects the higher prices from inflation that remains out of control. Stay tuned. Story developing. Business orders don't jump in recessions. New equipment purchases mean no recession in August anyway.

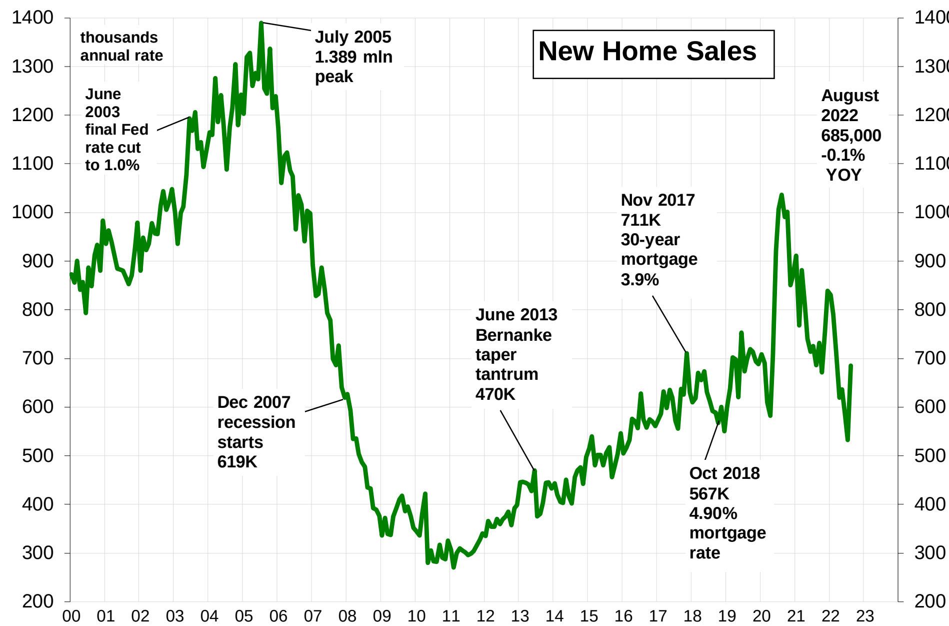


Confident consumers buy new homes (Tuesday)

Breaking economy news. Confident consumers rushed out to buy new homes in August which counts as one of the biggest positive economic surprises in weeks and means we can't count the economy out yet. Wall Street's financial markets are hunkering down preparing for a recession hurricane to hit, but consumers remain confident that the storm clouds will remain offshore for now. Gasoline prices have plummeted over $1 a gallon since the peak in June and consumers seem to know it. The labor market remains tight as a drum with jobs, at least on paper, widely available. 49.4% said jobs were plentiful in September up from 47.6 in August. The overall confidence index was 108.0 in September up from the preliminary report of 103.2 in August, now revised higher to 103.6.



Meanwhile, new home sales came roaring back in August after softer readings in June and July. The robust housing data are clearly out of whack with homebuilders preparing for Armageddon. The 28.8% jump in August new home sales to 685 thousand from 532 thousand in July looks unbelievable, but every region of the country had a big rebound. The biggest market in the South (includes Texas and Florida) rose 106 thousand to 467K in August accounting for nearly 70 percent of the nationwide increase in new home sales.



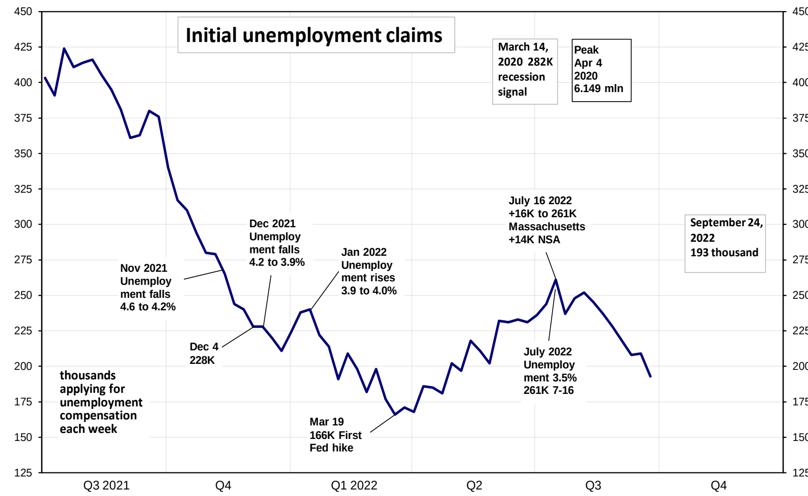
New home prices have been volatile, but at $436,800 in August they remain substantially higher than the full year 2021 average of $397,100.

Net, net, whatever Fed officials are trying to do by pushing interest rates higher and higher, it isn't working as economic textbook theory says it should because consumer confidence is returning and new home sales have come roaring back. New home sales and the burst of confidence may not last, but at the moment, the public has more money and is spending it, despite the darkening skies of recession. Wall Street is scared to death of the Fed's attack on inflation, but consumers are not as easily frightened. The labor market is tight, full employment means millions of American workers have paychecks, and this suggests the economy may be more resilient than we think.

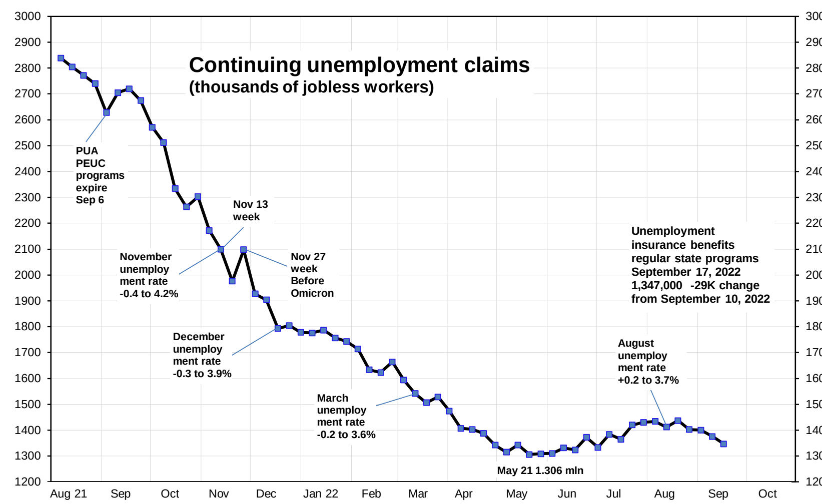
Recession hopes fading away (Thursday)

Breaking economy news. Benchmark revision to GDP same as it was with -1.6% in Q1 2022 and it remains -0.6% in Q2 2022. Consumer spending moved around a little, rising 2.0% in Q2 2022 where last month's estimate was 1.5%. The consumer hasn't stopped spending to any appreciable degree. Oh and for any economic historians out there, the pandemic recession wasn't as deep as the world thought with economic growth falling 2.8% in 2020 where growth had dropped 3.4% before today's benchmark revision.

Unemployment claims fell to 193K in the September 24 week and the prior week was revised down to 209K from 213K. Job layoffs are closer to the best of best times than the recent recession signal. The range being 261K July 16 and 166K March 19. Continuing unemployment claims, the total number receiving benefits, dropped as well by 29K to 1.347 million.



We can't keep getting job layoffs data like these and continue to warn a recession is right around the corner. The recession clouds aren't just lying off shore, they are starting to break up and the sun is shining through. You can't have a recession without rising unemployment, and today's continuing unemployment claims decline hints that the unemployment rate will come back down to 3.5% this month from 3.7% a month ago. It was barely 3.7% anyway with the 4-decimal number at 3.6505%



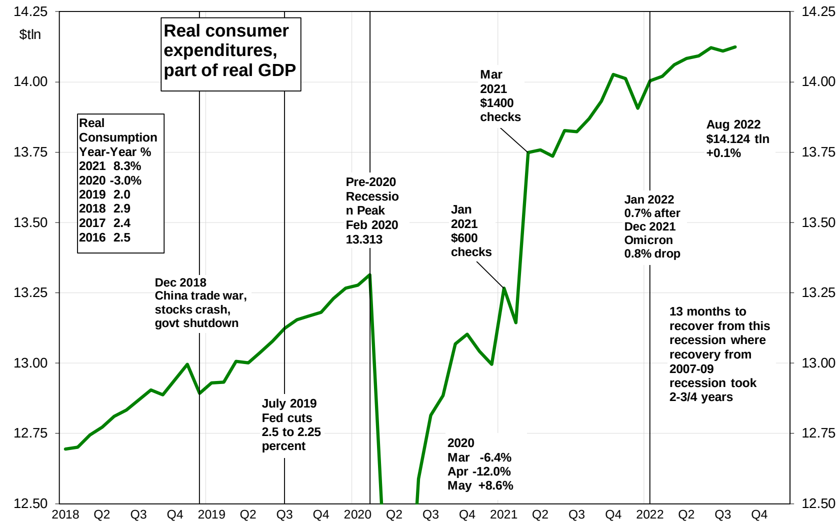
Net, net, the economic data couldn't point more in different directions today with GDP saying the recession is still out there with two consecutive quarters of negative GDP growth in the first half of the year, while jobless claims continue to recede from the recent highs seen back in July. The Federal Reserve won't be slowing the pace of their rate hikes yet with 75 bps in November and 50 bps more in December a virtual certainty. The Fed is going to go until something breaks, but so far, nothing is breaking besides the stock market and the early signs that home prices are starting to fall. Is it just us, or does anyone else out there fail to see how falling home prices fights inflation? If this is what Fed policy is trying to engineer, we will vote against it. Stay tuned. Story developing. Recession hopes are fading away and so are the odds of a near-term recovery in the stock market. Bet on it.

Benchmark GDP Revision on September 30

Date of Release	Percent %	2019	2020	2021	Q1 21	Q2 21	Q3 21	Q4 21	Q1 22	Q2 22
9/30/2022	Real GDP	2.3	-2.8	5.9	6.3	7.0	2.7	7.0	-1.6	-0.6
	Consumption	2.0	-3.0	8.3	10.8	12.1	3.0	3.1	1.3	2.0
8/25/2022	Real GDP	2.3	-3.4	5.7	6.3	6.7	2.3	6.9	-1.6	-0.6
	Consumption	2.2	-3.8	7.9	11.4	12.0	2.0	2.5	1.8	1.5

Good news bad news personal income report (Friday)

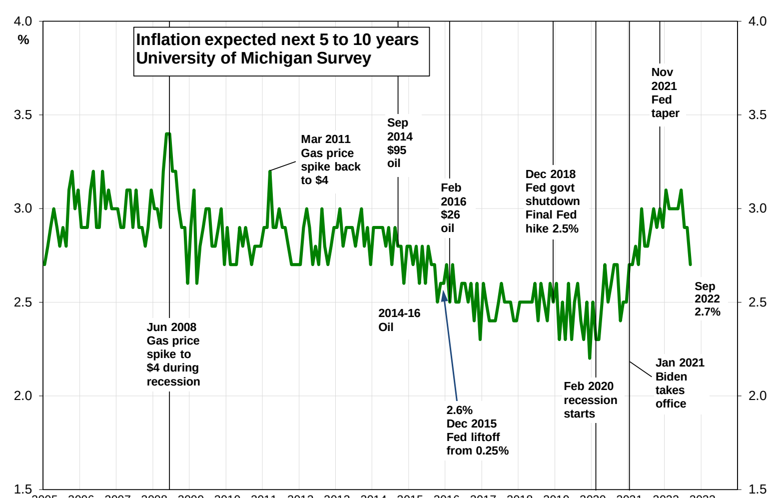
Breaking economy news. Good news bad news personal income report if you still have any personal income with the stock market down as much as 25% from the highs of the year. 25% is a recession-magnitude loss like those occurring during the Volcker inflation-fight in the 80s. Except we don't have a recession today.



We speak today of the personal income report with consumer inflation and spending numbers for August. The good news is real consumer spending is slowing this quarter, roughly 0.6% through August, versus 2.0% in the second quarter. Consumers are buying less at the shops and malls and while the reduction in demand has not cut the inflation rate this month, the markets are hopeful consumer inflation will moderate in the months to come. Core PCE inflation year-year was 4.9% in August, where the Fed forecasts see 4.5% in 2022 and 3.1% in 2023. The Fed forecasts aren't impossible to meet if consumer spending continues to stay on the slow side, although they think they have to push the Fed funds rate to 4.75% to make the inflation forecast a reality. For the record, core PCE inflation peaked at 5.4% in March this year.

Net, net, inflation remains high, but we remain hopeful that it has peaked and will start to slowly decline as the Fed's front-loaded rate hikes appear to be working as they should to moderate economic demand. Consumer purchases in the third quarter are running less than half of the 2.0% pace of real expenditures in the second quarter.

Not sure inflation expectations matter like the 80s. Costs go up, people try to raise their prices. Past price activity maybe more important than expectations for the future.



How many times can the market go down on the same 0.6% core consumer inflation report in a month? Answer: Twice, with 0.6% core CPI on September 13 and now today, September 30, with 0.6% core PCE inflation. At some point the stock market will tire of these inflation reports or at least sell off to a level which discounts the current high rate of inflation. Stay tuned. Story developing. Hopefully, the stock market will hold here unless some more Fed officials come out later today to warn us, they aren't done yet. We know, we know already. It's there in your forecasts for a peak 4.75% Fed funds rate next year versus the current 3.25% target. Stop talking. How many times can the stock market go down on the Fed warning more rate hikes are coming? Answer: infinite.

Analyst Certification

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