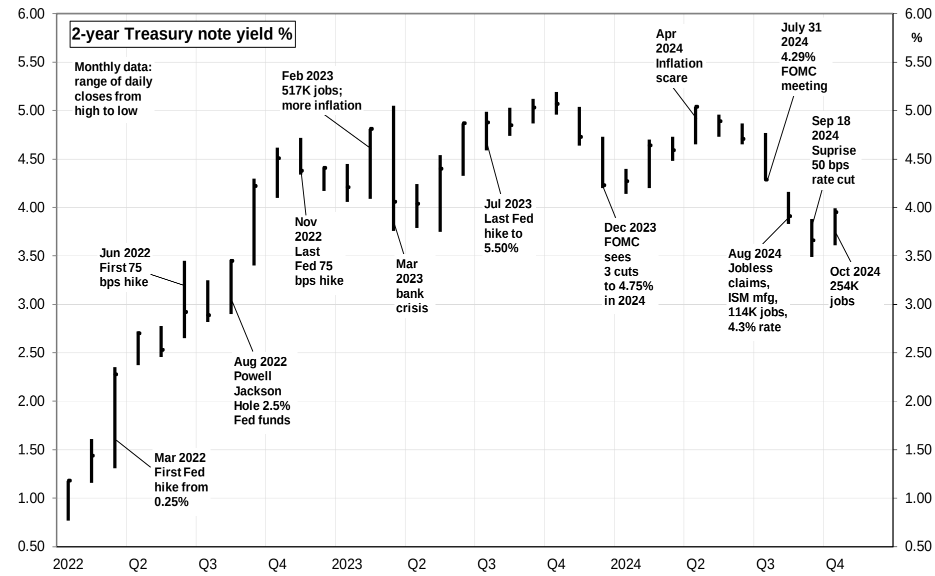
Financial Markets This Week

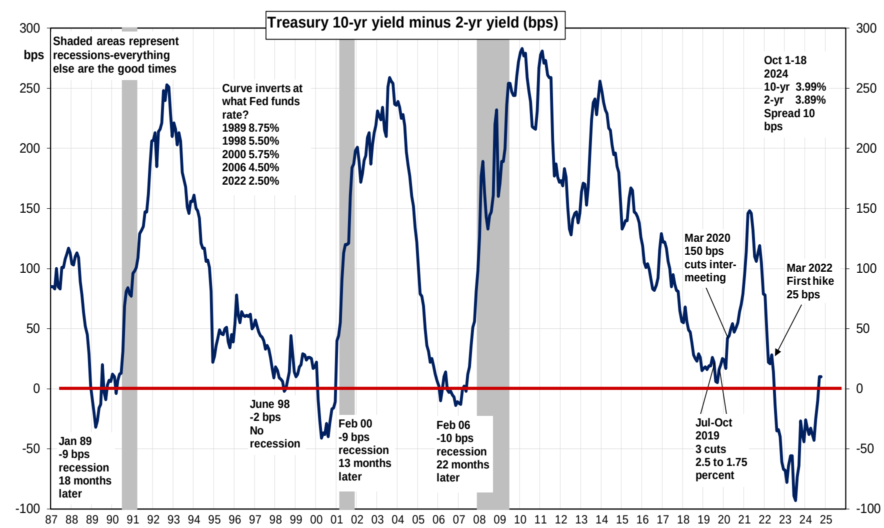
Christopher S. Rupkey, CFA
Chief Economist
crupkey@fwdbonds.com

18 OCTOBER 2024

3.9% FOR 2 YEARS

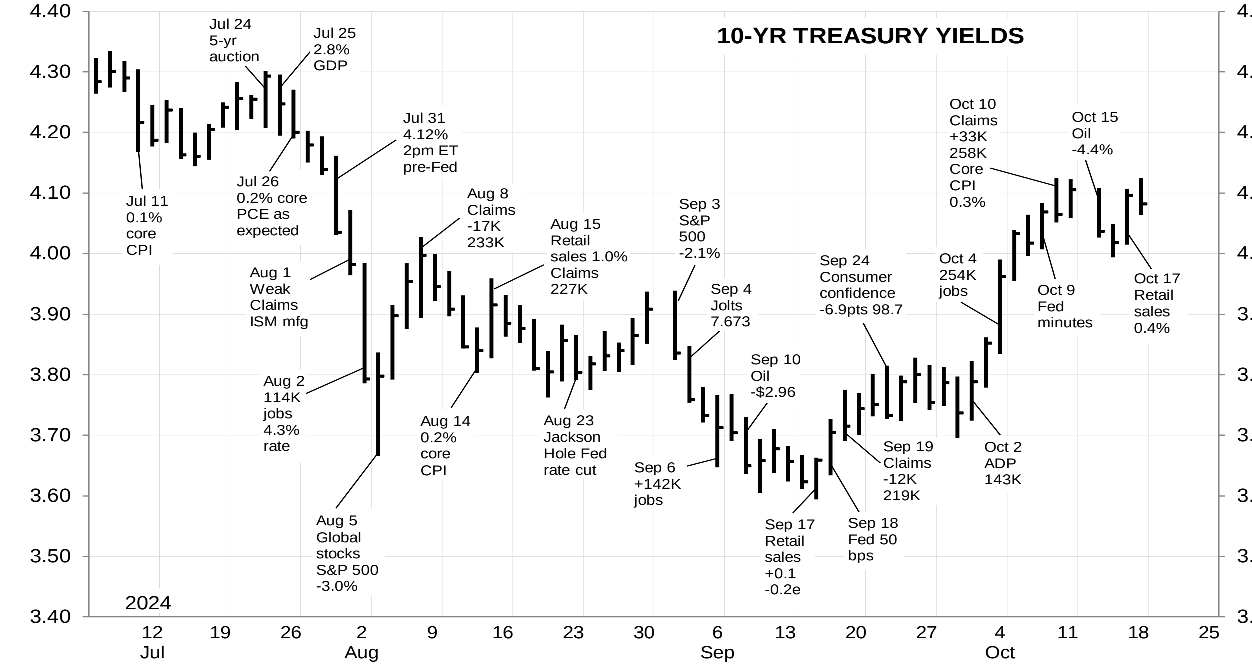


If you act fast you can still get a 3.96% rate on a 2-year U.S. government security. The Fed forecasts say that rates will be 3.5% at the end of 2025, and 3.0% in 2026, but 2-year yields could not wait. We cannot recall 2-yr yields ever falling so far below what is now a 5.0% Fed funds rate in anticipation of action by Federal Reserve policy makers, except perhaps during the Volcker years with those double-digit interest rates, although markets have never had explicit rates forecasts from the Federal Reserve to guide fixed income traders either-- first forecasts made under Bernanke in January 2012.



To recap the price action: 2-year yields were 4.29% coming out of the July 31 Fed meeting decision, and tumbled the the next two days on a growth scare with jobless claims rising 14K to 249K, the high for 2024, weaker ISM manufacturing data, and then the Friday August 2 monthly employment report of just 114K payroll jobs, and 4.3% unemployment rate: this was the weak monthly jobs report that Powell said might have sparked a rate cut if only they had known. 2-year yields fell as low as 3.5% after the surprise 50 bps Fed cut, and yields rose back after the stronger 254K payroll jobs report on Friday, October 4. One final note: the 2-yr/10-yr curve is unlikely to go out to 200 bps like it did when the Fed cut rates in the last three classic recessions. There was more fear of inflation in 1990-91 which sold off 10-yr securities. The Fed cut rates to an unprecedented 1% in the 2001 recession, and 0.25% during the Great Recession. This time the need for zero rates looks limited given real GDP is running about 3% in Q3 2024. Stay tuned. And yes, the 2s/10s inverted yield-curve recession indicator has had a swing and a miss.

INTEREST RATES



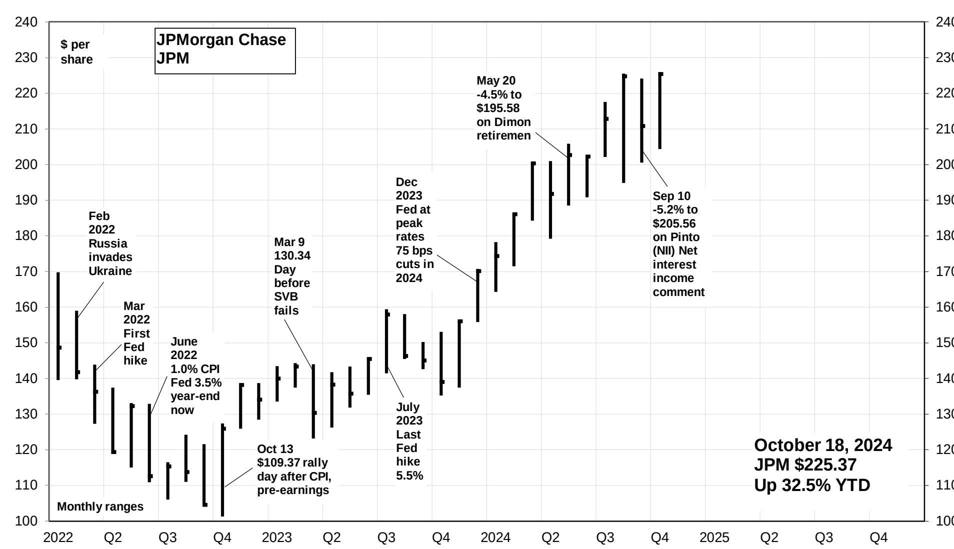
The 254K jobs report changed the trend and sent 10-yr yields up to 4%. If the Fed is not going to send rates back to zero again in a recession, then the 10-yr yield should spread much higher above the Fed rate. Thursday, October 10 was a confusing day with core CPI higher at 0.3% and the jump in jobless claims showing economic weakness potentially even with the Hurricane Milton impact; 10-yr yields also moved higher when Atlanta Fed President Bostic said he could skip doing anything at the November meeting. Bond yields came back down early in this holiday shortened week on Tuesday, with crude oil falling on stories Israel would not bomb Iran refineries, and even a soft-print on Canadian inflation seemed to help. Everything turned back around on Thursday with 0.4% retail sales and jobless claims falling back somewhat. S&P 500 closed Friday up 23.0% YTD. All is well. For now.

JPMorgan Chase (JPM) up 32.5% YTD

The stock jumped 4.4% to $222.29 on Friday, October 11 following the earnings report before the open. The stock had fallen 5.2% previously to $205.56 on September 10 when President and COO Pinto warned on interest income even before the Fed cut rates 50 bps on September 18. Q3 earnings raised the annual net interest income forecast, but it was the 31% jump in investment banking fees that caught traders' eyes.

JPM results (billions)

Quarter	Net Income	Provision for Credit Losses	Stock price Qtr end
9.30.2024	12.898	3.111	210.86
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

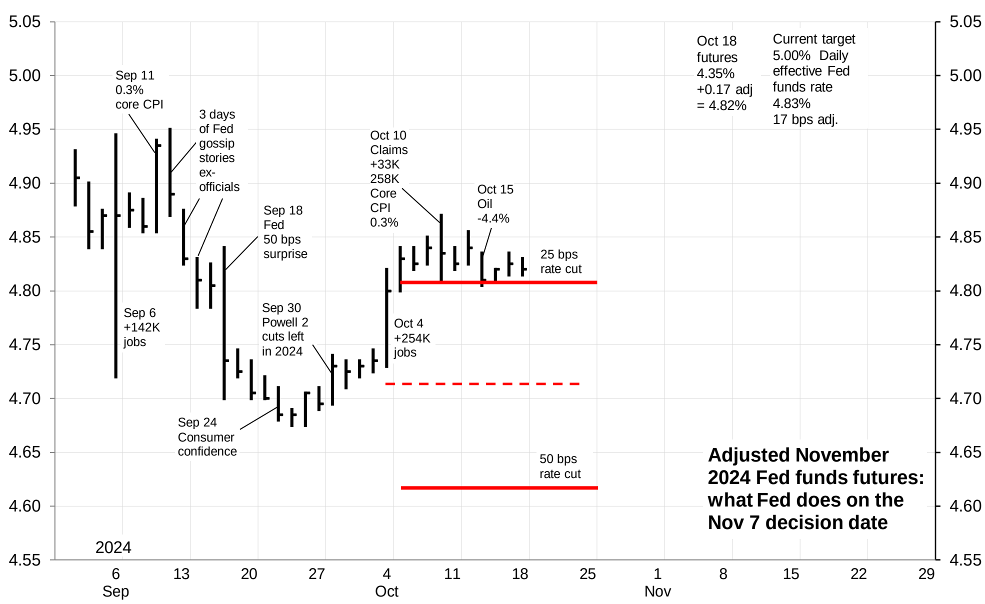


FEDERAL RESERVE POLICY

Selected Fed assets and liabilities						Change
Fed H.4.1 statistical release						from
billions, Wednesday data	16-Oct	9-Oct	2-Oct	25-Sep	3/11/20*	3/11/20
Factors adding reserves						to Oct 16
U.S. Treasury securities	4357.572	4364.466	4364.382	4384.130	2523.031	1834.541
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	2282.088	2282.078	2282.078	2282.078	1371.846	910.242
Repurchase agreements	0.001	0.001	0.002	0.061	242.375	-242.374
Primary credit (Discount Window)	1.879	1.745	1.660	1.365	0.011	1.868
Bank Term Funding Program	66.833	68.883	71.468	85.941		
FDIC Loans to banks via Fed	0.000	0.000	0.000	0.000		
Paycheck Protection Facility	2.201	2.241	2.297	2.333		
Main Street Lending Program	10.135	10.419	10.407	10.396		
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	0.159	0.155	0.157	0.153	0.058	0.101
Federal Reserve Total Assets	7090.3	7097.8	7097.6	7131.3	4360.0	2730.235
~~3-month Libor %~~ SOFR %	4.86	4.83	4.92	4.84	1.15	3.710
Factors draining reserves						
Currency in circulation	2358.793	2356.532	2352.941	2350.597	1818.957	539.836
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	814.751	787.395	823.412	778.910	372.337	442.414
Treasury credit facilities contribution	4.958	4.958	4.958	4.958		
Reverse repurchases w/others	272.071	343.448	383.398	416.193	1.325	270.746
Federal Reserve Liabilities	3861.423	3900.768	4000.346	3989.709	2580.036	1281.387
Reserve Balances (Net Liquidity)	3228.838	3197.045	3097.210	3141.565	1779.990	1448.848
Treasuries within 15 days	61.915	36.365	40.177	48.479	21.427	40.488
Treasuries 16 to 90 days	178.430	212.598	211.961	205.862	221.961	-43.531
Treasuries 91 days to 1 year	529.229	526.419	523.232	528.403	378.403	150.826
Treasuries over 1-yr to 5 years	1467.618	1469.577	1469.539	1483.485	915.101	552.517
Treasuries over 5-yrs to 10 years	592.491	591.944	591.934	590.665	327.906	264.585
Treasuries over 10-years	1527.890	1527.563	1527.538	1527.237	658.232	869.658
Note: QT starts June 1, 2022	Change	10/16/2024	6/1/2022			
U.S. Treasury securities	-1413.207	4357.572	5770.779			
Mortgage-backed securities (MBS)	-425.358	2282.088	2707.446			
**March 11, 2020 start of coronavirus lockdown of country						

The Fed meets November 6-7, 2024 to consider its monetary policy. The market-based odds have been favoring a step-down to just a 25 bps rate cut since the larger 254K payroll jobs report on October 4 which also had 72K of upward revisions to July/August. Hurricane Francine that struck Louisiana first on September 11 during the survey period apparently had no impact. Hurricane Milton hit Wednesday night, October 9 near Sarasota Florida (Siesta Key) within the October 12 survey week which could reduce the payroll jobs figure, and the Boeing strike could depress (50K) the October jobs report as well, to be released 830am ET Friday, November 1. It does not appear that any upcoming news could change the "call" for a 25 bps rate cut to 4.75% at the upcoming 2pm ET Thursday, November 7 Fed meeting decision date. First look at Q3 2024 real GDP is Wednesday, October 30, where 3.4% is expected by the market. Atlanta Fed President Bostic spoke Friday and seems to favor 25 bps for a rate cut and also opined that a neutral Fed funds rate is 3.0 to 3.5 percent. Not sure how 3% real economic growth last quarter, with Fed rates at 5.5% up until September 18, is evidence that the Fed's current monetary policy is slowing the economy down. Maybe they should not move the Fed funds rate down lower than 4.25% where policymakers first thought neutral was, back in January 2012 when they began making interest rate forecasts.

Fed Policy-key variables					Long
	2024	2025	2026	2027	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					



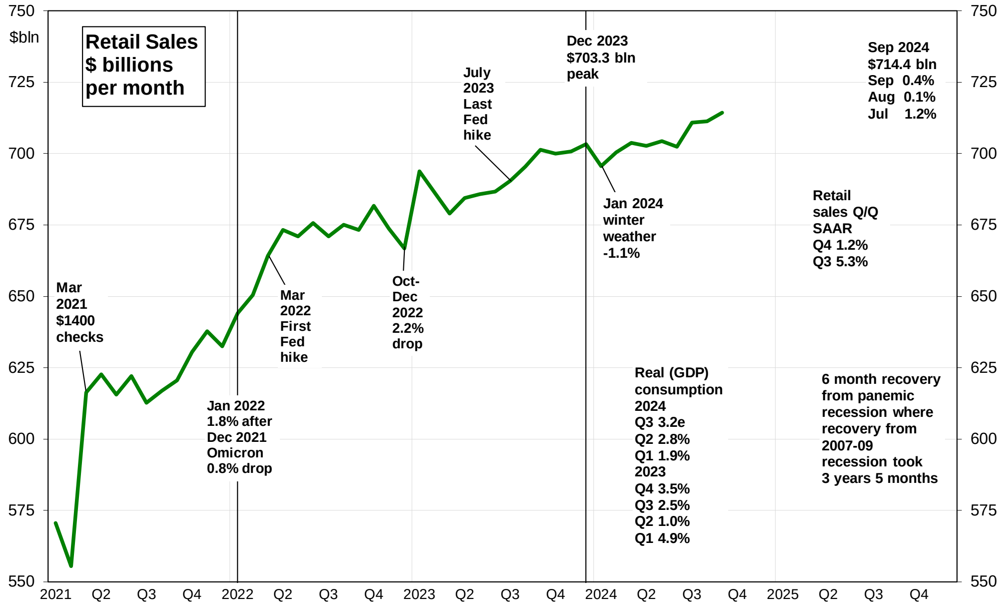
November Fed funds futures are not a clean read on the odds as the meeting is during the month. Market odds favor a 25 bps cut.

Fed funds futures call Fed policy	
Current target: October 18 -- 5.00%	
Rate+0.17 Contract	Fed decision dates
4.545 Jan 2025	Nov 7, Dec 18*
4.375 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 PCE inflation report Thursday, October 31														
Monthly	2024								2024	2023				2023
% Changes	Sep	Aug	Jul	Jun	May	Apr	Mar	Feb	Jan	Dec	Nov	Oct	Sep	Aug	Jul
Core CPI inflation	0.3	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
Core PCE inflation	0.25e	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
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
Core CPI YOY	3.3	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

OTHER ECONOMIC NEWS

Retail spend steady, job layoffs fall (Thursday)

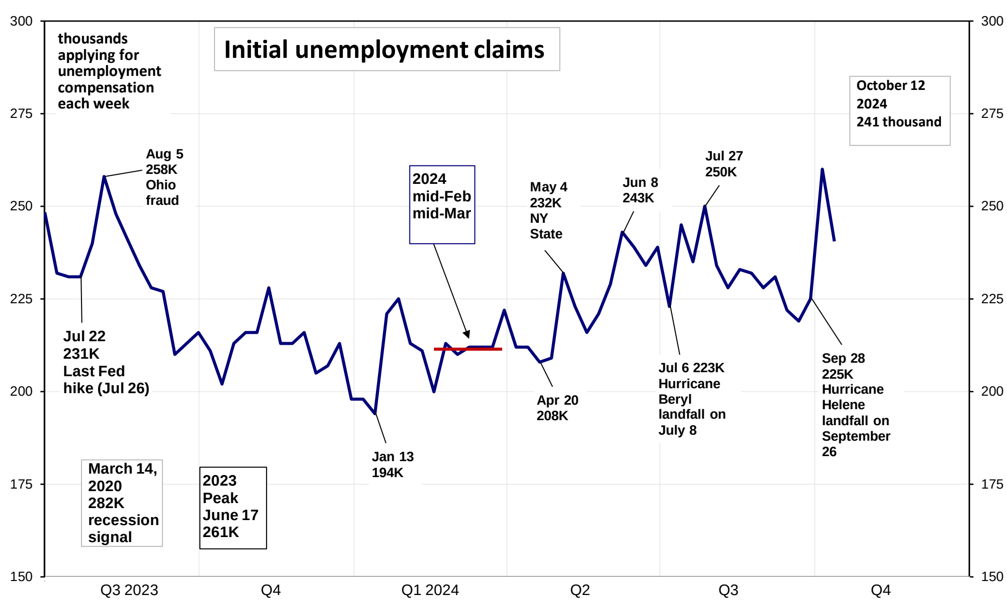


Breaking economy news. Retail sales increased 0.4% in September to round out a strong quarter and sales minus motor vehicles and gasoline jumped 0.7%. There is nothing wrong with the consumer that is for sure as Americans are seemingly dining out to celebrate with restaurants and bar sales jumping 1.0% in September after a 0.5% increase in August. Meanwhile, initial weekly jobless claims fell back to earth with layoffs plunging 19K from 260K the prior week to 241K in the October 12 week. The October 5 level of claims were clearly impacted by Hurricane Helene with North Carolina claims increasing 8,714, although other states had issues at the start of the fourth quarter with Michigan claims increasing 9,389. In other words, jobless claims look somewhat elevated, somewhat worrisome, although the layoffs data have cried wolf many times already this cycle that recession is near.

Retail spending, actual dollars, each month

	$million	% to	Percent Changes %		
	Sep	Total	Sep	Aug	Year/year
Total Retail Sales	714,358	100.0	0.4	0.1	1.7
Motor vehicles/parts	133,854	18.7	0.0	-0.4	-0.3
Furniture/furnishings	11,058	1.5	-1.4	-0.4	-2.3
Electronics/appliances	7,446	1.0	-3.3	-1.7	-4.6
Building materials/garden	41,242	5.8	0.2	0.0	0.5
Food & beverage	84,062	11.8	1.0	-0.5	2.5
Health/personal care	38,238	5.4	1.1	0.6	4.6
Gasoline stations	51,124	7.2	-1.6	-1.2	-10.7
Clothing/accessories	26,472	3.7	1.5	-0.8	3.5
Sporting goods, books	8,167	1.1	0.3	0.1	-3.5
General merchandise	75,992	10.6	0.5	-0.4	2.6
Department stores	10,882	1.5	0.4	-1.0	-1.2
Miscellaneous retailers	15,755	2.2	4.0	0.3	7.9
Nonstore retailers (internet)	124,548	17.4	0.4	1.6	7.1
Eating & drinking places	96,400	13.5	1.0	0.5	3.7
[Total ex-autos/gas]	529,380	74.1	0.7	0.3	3.7

Net, net, the consumer is steady as a rock with retail spending solid, and the spike in job layoffs turned out to be a red herring when it comes to gauging the economy's growth potential. There is no reason to question the strength of the economy or the outlook for the rest of this year given the latest batch of economic reports. The data are coming in as

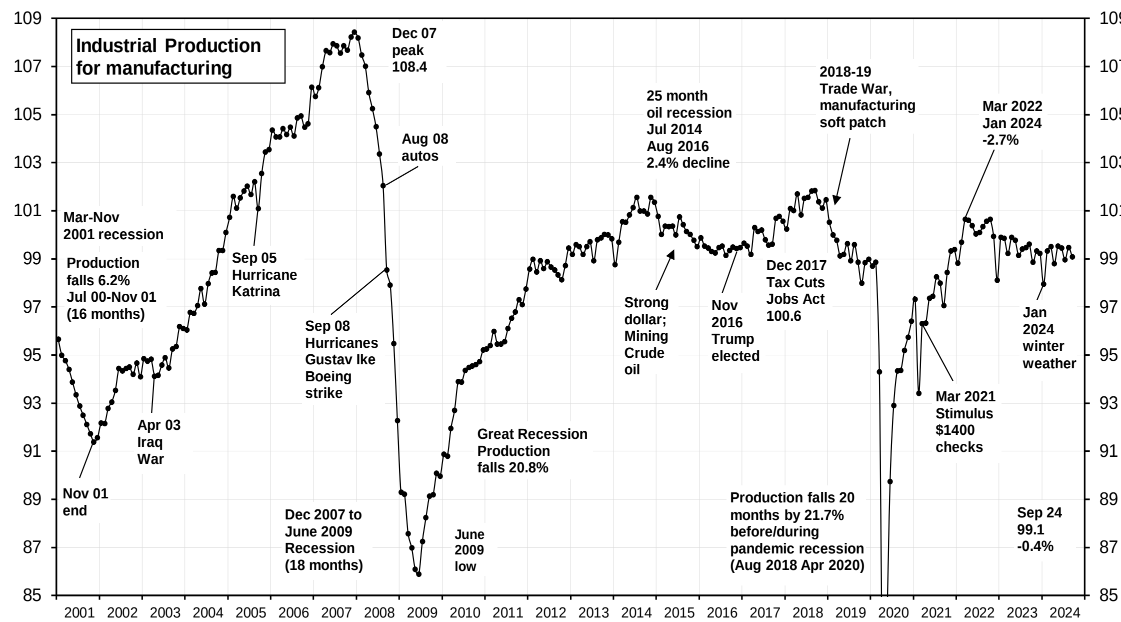


Fed officials expected so the most likely outcome at the November meeting is for a more measured, downsized 25 bps rate cut. Demand is too strong to be sure the inflation fire is out and Fed officials need to proceed cautiously given the uncertainty of the level of neutral interest rates. The economy sure is not slowing down or producing significant job layoffs with the current Fed funds rate of 5.0%. The stock market is at record highs and this tells us all we need to know about the state of the economy. Buy stocks now.

Industrial production report at 915am ET (Thursday)

Breaking economy news. September industrial production fell 0.3%, although the Boeing strike lowered total production by 0.3% and the two hurricanes lowered production by another 0.3% as well. Manufacturing production has been up and down each month this year it seems just looking back to April, and is down 0.5% from year ago levels. If factory production is going to be coming back to the USA in coming years, the only workers in the industrial plants will have to come from immigration as the Bureau of Labor Statistics says the native born population in this country is in decline.

Percent changes			Industrial Production September 2024		
Jul	Aug	Sep	YOY		Weight
-0.6	0.3	-0.3	-0.6	Total Index	100.0
-0.5	0.5	-0.4	-0.5	Manufacturing	75.1
-0.9	0.7	-0.6	-2.2	Mining	14.2
-1.1	-1.3	0.7	0.6	Utilities	10.7
			Manufacturing payroll jobs 12.9 million -37K YOY 9.5% of Private Payroll Jobs		



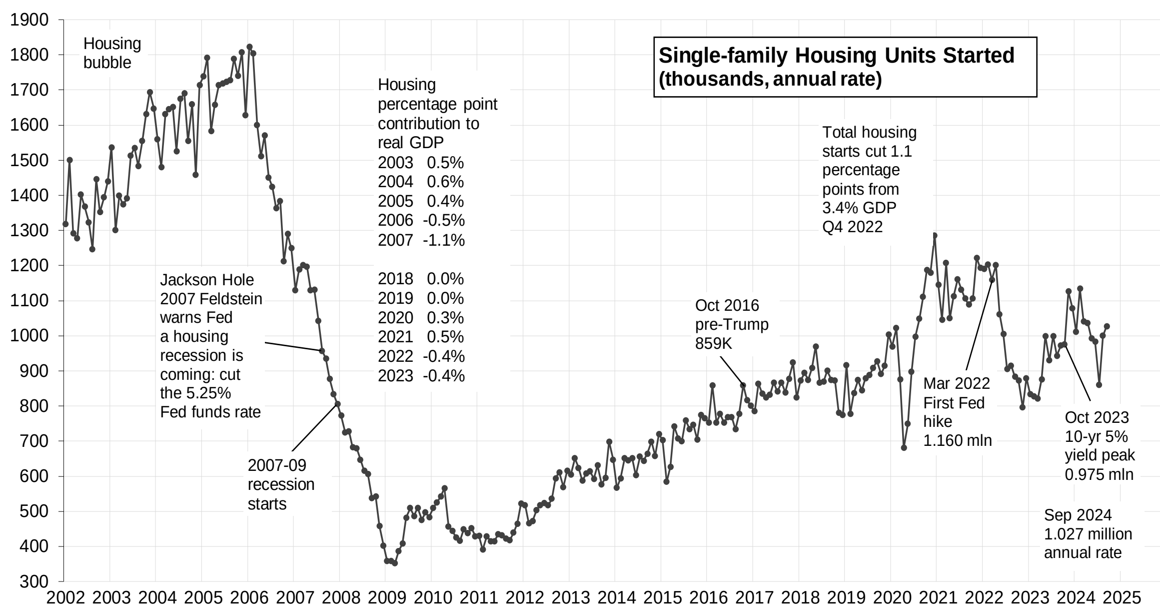
Single-family starts recovery (Friday)

Breaking economy news. Housing starts fell 0.5% to 1.354 million at an annual rate in September, dragged lower by a decline in multifamily construction. Single family starts recovered for a second month after dropping down in the South when Hurricane Beryl landed in Texas on July 8.

Housing Starts Total, Single-Family, Multi-Family

	United States			Northeast		Midwest		South		West	
000s	Total	1 unit	Multi	Total	1 unit	Total	1 unit	Total	1 unit	Total	1 unit
Sep 2024	1354	1027	317	180	94	179	121	738	601	257	211
Aug 2024	1361	1000	332	114	85	197	135	764	564	286	216
Sep 2023	1363	973	376	86	53	191	117	790	590	296	213
% Chgs											
Sep/Aug	-0.5	2.7	…	57.9	10.6	-9.1	-10.4	-3.4	6.6	-10.1	-2.3
Sep/Sep	-0.7	5.5	…	109.3	77.4	-6.3	3.4	-6.6	1.9	-13.2	-0.9

Net, net, single-family housing starts are showing more signs of life and home builders are gaining confidence perhaps as interest rates are expected to reverse course and come down sharply in the next year as Fed officials messaged in their September meeting forecasts. Home builders reported an increase in prospective buyers in October. The picture is mixed regionally with single-family starts up sharply in the South (6.6%) and Northeast (10.6%) while activity cooled in the Midwest and out West. Mortgage interest rate costs are stuck for fixed-term loans, but adjustable-rate mortgage yields should be coming down in 2025 as the Federal Reserve relaxes its restraint on the economy that was meant to fight inflation. Single-family home construction is sorely needed to help alleviate the shortage of affordable housing across the nation which has led to home values soaring beyond the means of many if not most workers. Stay tuned. Housing construction generally was a slight drag on 3.0% second quarter real GDP growth and residential housing construction is likely to decline overall in the third quarter modestly as a result of the weather perhaps, but the trend will likely resume an upward trend by later this year as the Fed continues to relax their grip on rates that has held the housing market down for so long.



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.