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Economic Indicators September 2021
By Kim W. Suchy

Stocks have continued their trek higher this past month and where given a little boost again last week when Fed Chair Powell said the Fed was committed to a slow roll on tapering. Chairman Powell acknowledged the need to taper the $120M monthly bond-buying program, and reassured the markets that future interest rate hikes were not on the immediate horizon. Note, since we cannot tax our way out of today's rising deficits, Modern Monetary Theory tells us that keeping interest rates near zero can help avoid paying high interest on the national debt. So, no rush.

The words of the Fed seem to trump and mitigate all other headwinds as is evident with the news being dominated by the somber events in Kabul, the Delta variant of C19 and rebuilding and repairing the aftermath of Hurricane Ida. Any of these single-handedly would be enough to send the markets reeling lower but the fact that they continue to notch higher levels indicate the power of a dovish Fed.

With regard to Afghanistan the U.S. troop withdrawal and airlift of U.S. citizens and allies to various processing centers is a human tragedy. The potential for an even greater humanitarian crisis exists after the August 31 deadline. As you know, I make every attempt to maintain political boundaries when addressing market performance, yet the overhang of growing geopolitical disruption on us, as well as our allies, creates an air of uncertainty that can cause markets to pause. This is not the time for terrorist threats especially when so many domestic issues are on our plates.

On the domestic front, the rapid spread of the C19 Delta variant has forced us, once again, to wrestle with heightened pandemic anxiety. The variant's surge has added to fears that the virus could meaningfully undermine economic growth. The financial markets had already been operating with a "growth scare" mindset for some time. Now, some market pundits are starting to signal an economic slowdown is in the offing yet the massive amounts of monetary and newly minted fiscal stimulus want to hold this at bay.

As the variant spreads there is growing concern about the impact on the service sector (i.e. restaurants & bars) as State Governors respond with some social restrictions (i.e. masks, distancing limits) and continue to urge vaccine-hesitant adults to get C19 shots. It's a new corporate world when companies tell employees not to return to work unless they have had a C19 shot or impose surcharge health costs on those who have not been vaccinated. You can bet the courts will entertain these types of cases….until then, tensions between employers and employees will certainly grow. In fact, the U.S. Labor Bureau cites that mandatory vaccinations are leading many teachers, police/fire/rescue, health care, pilots/flight crew and other professions to quit over mandates. These are high skilled professions that are hard to replace because of training and licensing. This could become a very serious problem in short order and re-fuel the "growth scare."

Despite the aforementioned headwinds, the market continues to shrug them off. As I have quipped in recent writings, fundamental data remains sound which gives us reason to remain cautiously optimistic. Let's touch on a couple of positive aspects that are providing tailwinds to sustained growth.

The July housing market data reflects continued expansion, in spite of high material costs, supply hiccups, and labor shortages in many regions. New and existing saw healthy increases last month. As labor shortages and supply snags decrease, we should see a continuing strong and expanding housing sector. As I have stated many times, housing remains the bedrock of our economy…new kitchens, new appliances, decorating, man-caves, all fuel the economic engine. With the Fed keeping rates lower for longer, housing should remain affordable.

In the most recent Labor Department release, nonfarm business sector labor productivity increased 2.3% in 2021 Q2, as output increased 7.9% and hours worked grew 5.5%. Productivity improvements surged in the C19 period as it spurred businesses in practically every sector to radically retool many of their operations by adopting new digital technologies. Think of your Zoom calls and Docusigns that enabled you to continue doing business despite C19 restrictions. Eliminating long commutes to work actually generated longer work days as workers from home could not "turn it off"…one last email, one more phone call etc. This enhanced productivity as hours worked grew. Many will argue that this productivity increase could help to ward off inflation.

When we look at recent market performance, we continue to see fundamental data supporting growth and the potential for fresh new highs. While optimism could break down if some of the addressed concerns materialize, this would not be significant pullback, rather one that requires the discipline to remain focused on asset allocation as well as quality selection of healthy balance sheets which can withstand the vagaries of volatility.

Here is your look at developments in the global marketplace.

Positive Developments:

- Industrial production was up 0.9% in July (1.0% including revisions to prior months). This was led by auto manufacturers stepping up activity to overcome the ongoing supply chain shortages that have hurt production. Last month, canceled typical summer auto plant shutdowns to keep autos rolling off the assembly line, pushing auto production up 11.3%. Auto production is down 6.9% yoy. The auto industry is still soft and will be for some time. Keep in mind that it is not only supply chain issues that are hampering a more robust rise in activity, but also the ongoing labor shortage, with job openings in the sector near a record high and more than double pre-pandemic levels.

- Existing home sales increased 2.0% in July to a 6M a/r according to the Census Bureau. Sales are up 1.5% yoy. The median price of an existing home fell to $359K in July but is up 17.8% yoy. Average prices are up 12.0% yoy. The months' supply of existing homes for sale (how long it would take to sell today's inventory at the current sales pace) rose to 2.6 in July from June's reading of 2.5, though these readings still remain near record lows. Despite the ongoing shortage of listings, there is still significant pent-up demand from the pandemic, with buyer urgency so strong in July that 89% of the existing homes sold were on the market for less than a month.

- Personal income rose 1.1% and personal consumption rose 0.3% in July. Personal income is up 2.7% and spending has increased 12.1% yoy according to the Census Bureau.

- According to Chris Low Chief Economist at FHN Financial, the way Powell runs meetings makes clear he is genuinely interested in the business of the Fed and in the contributions of everyone in the meeting. Even before he was Chair, he was the governor who would sit quietly, listening. When he did speak, it was usually not to offer an opinion, but to ask a question leading to an answer synthesizing the ideas of several people in the room. He is a consensus builder, and gives the clear impression the Fed exists to do the bidding of Congress.

Neutral Developments:

- After rising for 2 mos. in a row, housing starts paused in July. Home building has been volatile so far in 2021 due to widespread supply-chain issues and shortages of labor, but looking at the 12-mo. moving average, which helps see through the volatility, shows residential construction now stands at the fastest pace since 2007. Housing starts declined 7.0% in July to a 1.5M a/r, below the consensus expected starts of 1.6M. Starts are up 2.5% versus a year ago.

- Minutes from the July Fed meeting revealed that most members support reducing monthly bond purchases before the end of the year while reaffirming that tapering *is not* linked to imminent rate hikes.

- Retail sales declined 1.1% in July but retail sales are up 15.8% yoy. The decline in sales in July was led by autos and non-store retailers (internet & mail-order). The largest increase was for restaurants & bars as people ventured out t their favorite watering holes. While some are concerned C19 may continue to eat away at retail, rising wages, jobs and inflation will all be tailwinds for retail sales. On the other hand the waning of the boost from stimulus checks along with the end to overly excessive jobless benefits will be headwinds.

- The CPI rose 0.5% in July for a 5.4% yoy. The core CPI (ex-food and energy) rose 0.3% for a 4.3% yoy increase. Both headline and Core CPI had risen 0.9% in June according to the Bureau of Labor Statistics. Inflation is elevated but there are already signs of price pressures alleviating. The core increase was the smallest since February and a marked decline from April, May, and June increases.

- As I noted to you earlier in August, the market remains in a summer slowdown, with late August being historically one of the slowest times for trading with the exception of the Christmas holiday season. Light volume means large bid/ask spreads so lack of liquidity means stock prices will be highly volatile. Expect markets to pick up in volume and volatility after the Labor Day and into September.

- *New* single-family home sales increased 1.0% in July to 700K a/r. Sales are down 27.2% from a year ago. The median price of new homes sold was $390K in July, up 18.4% yoy. The average price of new homes sold was $446K, up 17.6% yoy. While new sales are on the rise, pent up demand exists. Labor shortages and elevated lumber prices are forcing prices higher and slowing the pace of new home sales.

Negative Developments:

- The Bureau of Labor Statistics reports that PPI rose 1.0% in July, well above the 0.6% consensus. The PPI ex-food and energy rose 1.0%, 2X the 0.5% consensus. The PPI ex-food, energy, and trade services rose 0.9%, the most since January, and 2nd most since this series began in 2013. PPI is rising quickly and the pressures are broad-based.

- The July Small Business Optimism Index fell from 102.5 to 99.7. The weakest responses were in the categories "expect better economy," "expect higher sales," and "positive earnings trends." The thing about the Delta variant is not just that it is straining hospitals and prompting the return of mask mandates. It is causing concerns about faith in vaccines and destroying confidence that we will ever get past the stigma of C19.

- The U.S. dollar has continued higher through most of August and has punished most commodities and emerging market stocks. Commodities are priced in dollars while most of the emerging market debt is also priced in dollars so as the dollar rises, debt service costs escalate and can hurt credit profiles.

- The Labor Dept. reports that C19 impacts labor demand from weaker business conditions, but a significant drag on the labor market recovery has been decreased labor force participation. The labor force participation rate fell from 63.3% in February 2020 to 61.7% in July. The participation rate for prime-age workers, those 25-54, fell from

89.3% in February 2020 to 88.3% in July. Fear of the virus, school closures impacting parents' availability to work, involuntary early retirement, and enhanced unemployment benefits have all influenced labor force participation. There is already some evidence these impacts are fading, but the Delta variant will delay a speedier recovery in labor force participation.

- No wonder why big pharma is on the hunt for an Alzheimer's drug. The American Journal of Managed Care reports that $305B was spent last year on treatments. Here is the breakdown: $155 Medicare; $52B Medicaid; $66B out of pocket and, $33B other.
- C19 outbreaks in Asia Pacific have led to new containment measures, disrupting production and trade in a region that accounts for 37% of global merchandise exports, according to IHS Markit. Vaccination efforts outside China have been slow in Asia, hurting consumer spending, tourism, industrial production and exports. The IHS Markit manufacturing PMI surveys for July show weakening business conditions in Indonesia, Malaysia, Myanmar, Thailand and Vietnam. Cases of C19 cases have been falling in India, Taiwan and Indonesia, but rising in Japan, South Korea, Malaysia, the Philippines and Vietnam….thus, supply chain disruptions, particularly in the semiconductor space, remain compromised.

The Markets:

Domestic stocks were higher across the board last month with all capitalizations participating.

Over the past month financials, communication services and technology performed very well while consumer discretionary, materials and energy were laggards. Growth stocks continued to outperform their value counterparts across all capitalizations last month. The modest decline in interest rates (hence discount factor) helped longer term growth stock valuations improve.

U.S. Index	Last Month (% return)	YTD (%)
S&P500	2.6	20.4
Dow	1.0	15.6
NASDAQ Comp	3.8	20.9
Russell 2000	-4.5	14.9

On the international front, the European markets improved and are up 18+% YTD. Asian markets also improved yet Hong Kong continued to move sideways. Gold was essentially flat last month as inflationary concerns were relatively muted.

International Index	Last Month (% return)	YTD (%)
Euro Stoxx 50	1.9	18.2

Hang Seng	-1.9	-5.5
Germany	1.7	15.4
Nikkei	1.1	2.4
FTSE-U.K.	0.7	10.3
China Shanghai Comp.	2.2	2.0
Gold	-0.1	-4.4

The year 2021 began with the 10-year Treasury Note yield at 0.90%. The 10-year closed August at 1.30%, 32bps lower than the July 2021 close. The 2-year Treasury closed August yielding .07%, 5 bps lower than July's close. The curve narrowed quite a bit last month as the 10/2 spread is at 123bps or 27bps tighter than last month.

News You Can Use:

On August 23, 2021, the FDA granted Pfizer and BioNTech full U.S. approval of their Covid-19 vaccine. The approval may encourage Americans who have not been vaccinated to get the shots as well as give more businesses across the nation the confidence to implement vaccine mandates. The mRNA vaccine was only on the U.S. market under an Emergency Use Authorization, up until now. Children under 12 have not yet been approved to receive any COVID-19 vaccine, for the simple reason that it has not yet been proven safe and effective for this group.

https://www.npr.org/sections/coronavirus-live-updates/2021/08/23/1030251410/pfizer-covid-vaccine-fda-approval

In an effort to protect minors' physical and mental health, China is imposing a rule that users under the age of 18 will only be able to play online games from 8 p.m. to 9 p.m. local time on Fridays, weekends (or 3 hours a week) and holidays. Previously, China had limited the total length of time minors could access online games to 3 hours on holiday and 1.5 hours on other days. Chinese authorities blame youth videogame addiction for a host of societal ills, including distracting young people from school and family responsibilities.

https://www.forbes.com/sites/paultassi/2021/08/30/china-now-limiting-video-game-play-to-just-three-hours-a-week-for-minors/

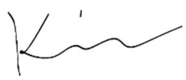
The eye of Hurricane Ida came ashore Louisiana on Sunday, August 29, with maximum sustained winds of 150 miles an hour, just shy of the 157 m.p.h. winds of a Category 5 storm. Extensive damages have been reported throughout the state and nearly one million people are without power. In New Orleans, nearly the entire city is without power. Louisiana hospitals have been forced to evacuate some of their patients as power outages threaten the use of ventilators for COVID-19 patients. Engineers reported that the storm actually reversed the flow of the Mississippi River.

https://www.newsweek.com/hurricane-ida-damages-louisiana-hospitals-forces-evacuation-some-patients-1624192

https://www.newsweek.com/louisiana-power-outage-map-over-1-million-still-without-power-hurricane-ida-1624196

As always, if I can be of additional guidance, please feel free to call me at 312.485.6847.

Best regards,



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