

August 28, 2023

## Summertime Blues

August has seen the unwinding of the seven-month rally in technology and digital stocks that, to varying degrees, lifted equities across most sectors this year. On the final trading day of July, the S&P 500 hit a peak level around 4,607, exactly 20% higher than its year-opening price. The index has had a hard tumble, and closed on 8/18/23 at 4,370 -- down 4.8% in less than a month.

Stocks often struggle in the summer; but usually that means they are lethargic, not heading notably higher or lower. What caused stocks to give up big parts of their year-to-date gains in August 2023? AI mania drove much of the stock rally in the first half of 2023. And in any stock-market mania, unbridled enthusiasm gives way to second-guessing at some point.

Consumers and businesses show few signs of spending fatigue, contributing to inflation's persistence. We think the difficulty in getting inflation to the Fed's 2% target range, along with some buyers' remorse on AI mania, has prompted investors to take profits before heading out on vacation.

### Jobs and Inflation Send Mixed Signals

After years of U.S. jobs growth that befuddled economists, the employment economy finally appears to be slowing. Nonfarm payrolls increased by 187,000 in July, in line with a downwardly revised 185,000 for June and well down from 280K-plus in May. The unemployment rate declined to 3.5% in July from 3.6% in June and 3.7% in May.

Average hourly earnings grew at a 4.4% annual rate, or close to the annual rate of change in core consumer inflation; and the average hourly workweek ticked slightly lower to 34.3 hours. The U.S. economy continued to add jobs in July in areas including healthcare, financial services, wholesale trade and social assistance. Government employment and jobs in the industrial and commercial economy were little changed.

Following the most recent FOMC meeting in July, Fed Chair Jerome Powell stated, "Reducing inflation is likely to require a period of below-trend growth and some softening of labor market conditions." Nonfarm payrolls do appear to indicate that labor market conditions are moderating. But even as jobs growth slows, inflation at the consumer level is stubbornly remaining above the Fed's 2% target range.

The July 2023 consumer price index (CPI) showed month-over-month inflation growth of 0.2%, both for the all-items and core indices. That was in line with June gains. The annual change in all-items CPI ticked up to 3.2% in July from 3.0% in May. The core rate (excluding food and energy) rose 4.7% year-over-year in July, slightly better than the prior month's 4.8%.

The process of getting from 4%-5% in core inflation to the 2%-3% range appears to have bogged down on still-high shelter costs and a several other goods and services categories. The annual change in shelter costs was 7.7%, more than double the annual change in all-items CPI. At about 30% of the CPI basket, shelter is the largest price category. Transportation services (up 9% year-over-year) and food (up 4.9%) remain too high to enable the overall inflation rate to ease into the target range.

Since the July CPI report was issued on August 10, stock-market deterioration has intensified. The data since then, as it has been all year, is mixed. Retail sales for July surprised to the upside, rising 0.7%; that was much better than the 0.4% consensus call and up from monthly growth of 0.3% in June. The monthly change excluding vehicles and gasoline was 1.0%, more than double the consensus forecast of 0.4% and a sign that back-to-school shopping remains a key retail sales driver.

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## ECONOMIC & MARKET COMMENTARY (CONT.)

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Housing starts, another indicator of the consumer economy, increased at a 1.45 million seasonally adjusted annual rate (SAAR) rate in July and was up from 1.40 million for June. Existing homes for sale are in short supply, due to the disconnect between mortgage rates available today and much lower rates on existing mortgages. At the same time, consumers are fully employed in a rising-wage environment, Millennials are in prime home-buying years, and would-be homebuyers are motivated. Given all these factors, we expect much of the momentum in the housing sector to be concentrated in the new home segment.

Again and again, the U.S. consumer has belied economists' warning that consumer spending is going to slow. If the consumer segues from robust back-to-school spending to at least a decent holiday season, the likelihood increases that the U.S. economy can engineer a soft landing.

Industrial production for July also surprised to the upside, rising 1.0% from June levels versus a 0.3% consensus forecast. The strong monthly gain was skewed by a 5.2% increase in production of motor vehicles and parts. Additionally, hot July weather pushed up air conditioning demand, lifting the utility index by 5.4%. Capacity utilization, which slipped below 80 earlier in 2023, remained below that level but at 79.3% (up 60 bps) was trending in the right direction. Below the headlines, manufacturing data from earlier in 2023 was revised downward, and the July 2023 manufacturing index sits slightly below the July 2022 level.

### Conclusion

The Federal Reserve, which did not raise the fed funds rate at the June FOMC meeting, followed up with a quarter-point hike in July. The FOMC will not meet in August. The CME FedWatch tool indicates that investors see a less than 50% chance that the Fed will raise rates again at its September, November or December meetings.

At the end of the month, the Fed will host its annual economic symposium in Jackson Hole, Wyoming. The event always has a theme, and this year's theme is "Structural Shifts in the Global Economy." Although the meeting will include academic papers and presentations on the main topic, on the sidelines investors and economists will look to glean hints on the direction of future rate policy from attending Fed governors and regional presidents.

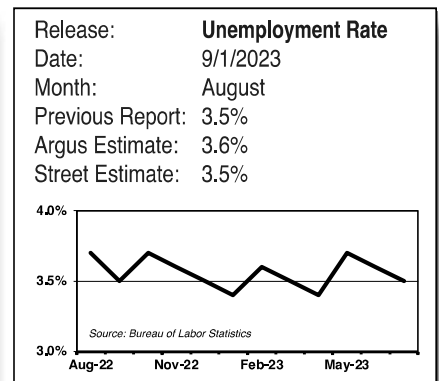
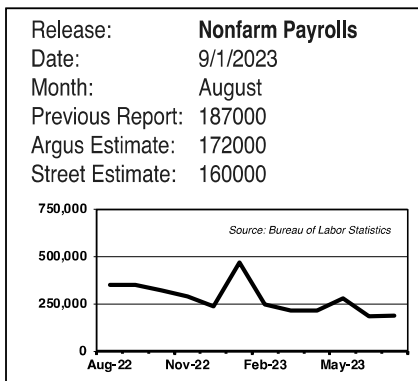
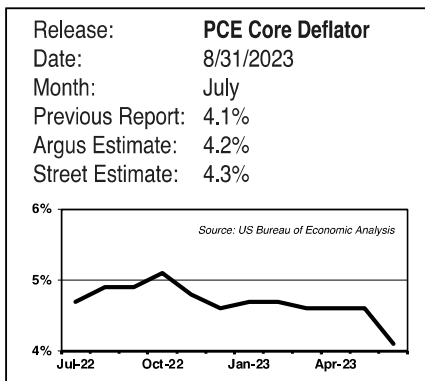
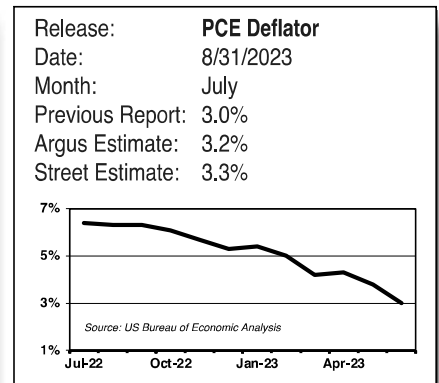
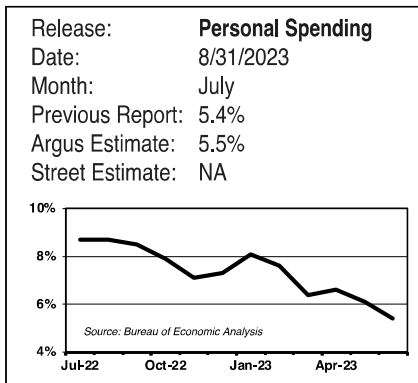
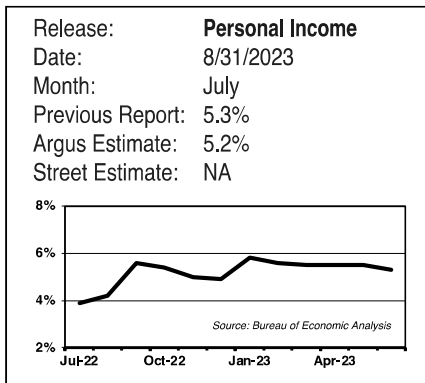
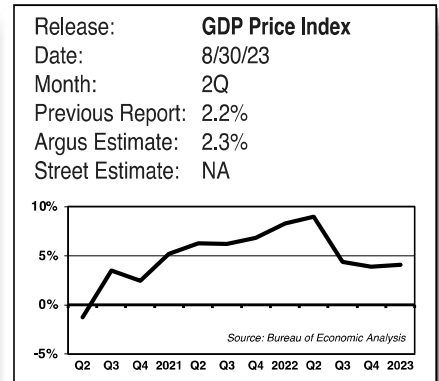
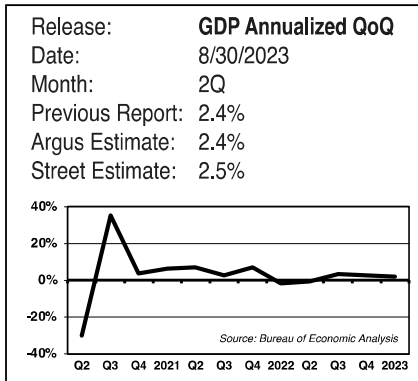
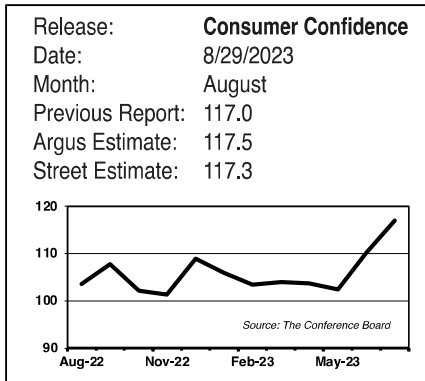
On the final day of August and not long after the Fed symposium concludes, personal income and outlays for July will be released. This release includes the Fed's most closely watched inflation data point, the core PCE price index. This measure of core consumer inflation is expected to show growth of 4.1% year-over-year, which would be lower than July core CPI inflation though higher than core PPI inflation.

Between 1980 and 2022, the S&P 500 has averaged total appreciation of just 1.1% in the four-month span from the beginning of June to the end of September. Of the four months, only July has been historically strong, with the S&P 500 averaging a 1.3% gain over the 43-year span. The other three months have been tepid, including average gains of 0.10% in June and 0.02% in August, to downright bad, with index averaging a 0.99% decline in September from 1980 through 2022.

Summer normally brings the doldrums; in 2023, the (so far) 4.8% August selloff has been nastier. August 2022, by the way, was also bad, with the S&P 500 declining 4.2%. If the core CPE price index comes in better than anticipated, the stock market will have a single trading day in the month to unwind some of August's losses. On the other hand, if core PCE shows inflation stubbornly hanging in there in July, the summertime blues could extend beyond Labor Day into the normally weak stock month of September.

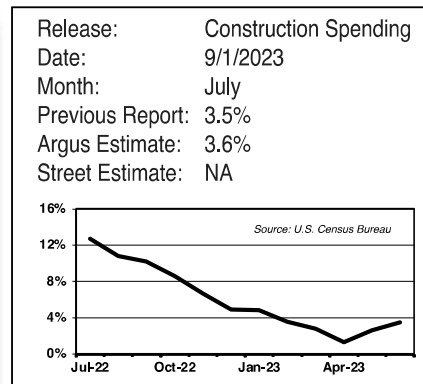
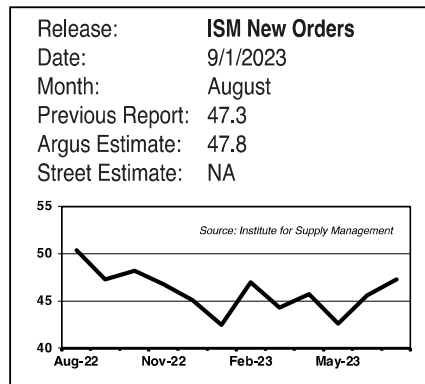
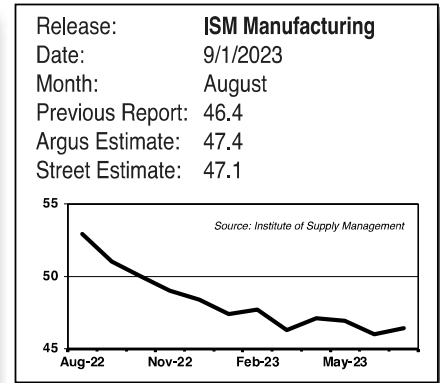
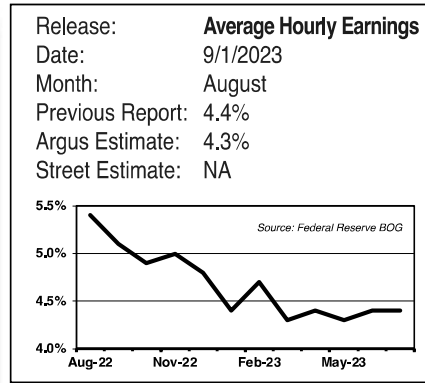
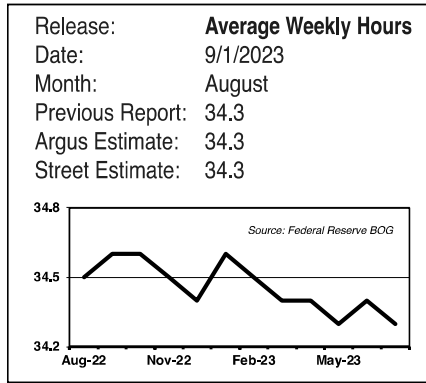
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# ECONOMIC TRADING CALENDAR



*Previous Week's Releases and Next Week's Releases on next page.*

# ECONOMIC TRADING CALENDAR (CONT.)



## Previous Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
22-Aug	Existing Home Sales	July	4.16 Mln.	4.12 Mln.	4.15 Mln.	NA
23-Aug	New Home Sales	July	697 K	710 K	705 K	NA
24-Aug	Durable Goods Orders	July	9.1%	5.3%	NA	NA

## Next Week's Releases

Date	Release	Month	Previous Report	Argus Estimate	Street Estimate	Actual
5-Sep	Factory Orders	July	-0.2%	NA	NA	NA
	Total Vehicle Sales	August	15.74 Mil.	NA	NA	NA
6-Sep	ISM Services Index	August	52.7	NA	NA	NA
	Trade Balance	July	-\$65.5Bil.	NA	NA	NA
8-Sep	Wholesale Inventories	July	1.3%	NA	NA	NA

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