Summary

Economic data for the week included the Federal Reserve keeping interest rates unchanged but kept language relatively hawkish. Housing data was negative, with a drop in existing home sales as well as starts and homebuilder sentiment, although building permits improved. The index of leading economic indicators remained in a negative trend.

Global stocks fell back last week, due to the hawkish tone of central bank commentary, as opposed to actual rate hikes done, as well as idiosyncratic economic stresses. Bonds fell back, directly due to the rise in longer-term yields. Commodities were mixed, with crude oil prices little changed for the week.

Economic Notes

(0) The **FOMC** kept policy rates steady as expected. Most notable in the Summary of Economic Projections (SEP) document was the interpretation that rates would stay higher for longer in 2024, a likelihood that's already been echoed for a while in CME Fed funds futures markets. In the post-meeting press conference, which is always interesting for additional color based on journalist questions, Chair Powell reiterated the party line, while also pushing back on inquires that required far more precision than is really possible to give in real time. In contrast to meetings over the past year, up until now anyway, the message has been centered on the steady progress upward in rates in a single-minded effort to get inflation under control. Now, while the inflation objective hasn't been completely reached, conditions have improved to the point where the Fed seems to feel more comfortable mentioning a more 'balanced' and nuanced approach to their restrictive policy. This seems to be in an effort to get to that place of 'neutral' that is neither tight nor easy. This still means another hike or two could be necessary, particularly due to stubbornly high services inflation coinciding with that strong segment of the economy. Speaking of the neutral rate, which was kept at 2.5% for the long-term, reflecting the 2% PCE inflation target, despite some thoughts that it might tick up by a quarter-percent or so, reflecting now-higher market rates and a higher resting level for inflation expectations.

Some notable quotes from Powell noted that he wants to "see convincing evidence" of inflation moving down to target. However, the language was still vague—by design. He did mention some "surprise at the strength" of current economic growth, which could be echoed by a variety of economists. When will rates get high enough? "Sufficiently restrictive is something you only know when you see it." (This is as opposed to seeing it calculated in a more precise financial model.) Importantly, a key caution was again reiterated as "a failure to restore price stability, as history has shown."

Post-meeting, financial markets were little changed, but steadily deteriorated Wed. and Thur. as the implications were absorbed of higher rates for longer, with the Fed's hesitancy about committing to an eventual path for cuts. (Again, not surprising, considering we're still in a hiking regime, but everyone is looking at least six months ahead.) The 10-year Treasury stabilized at little net change at first, before moving higher, with long-term assumptions still pointing to a decline down toward trend-like GDP growth (around 1.5-2.0%), moderated inflation (around 2.0-2.5%), and perhaps more persistent positive 'real' rates, which have not been seen in some time. Based on a variety of assessments, and those inputs, the current 4.5%-ish 10-year yield looks to be not too far from a theoretical fair value.

(-) The Conference Board's **Index of Leading Economic Indicators** fell -0.4% in August, a bit further than the -0.3% the prior month, representing consistent declines for now over a year and a half. The index is down -3.8% for the trailing six-month period ending in August, slightly better than the -3.9% drop of the prior six months (Aug. 2022 to Feb. 2023). The six-month period was led downward mostly by the non-financial components of negative business sentiment and ISM new orders. For the single month of August, similar factors were at play, including weaker new ISM orders, weaker consumer expectations, high interest rates, and tight credit weighing on the index, and again reiterating their call for a period of slow growth and/or recession upcoming in future

quarters. Generalized Wall Street estimates for a recession continue to fall around 50%, with some firms calling for a soft landing for now, and others simply a push of recession into the future, which are both really the same thing.

(-) The **Philadelphia Fed manufacturing index** fell by a sharp -25.5 points back to a contractionary -13.5 level for September, well below the -1.0 expected. By segment, new orders declined in line with the broader index, along with shipments falling nearly -10 points back into contraction. On the other hand, employment improved a bit, but stayed in contraction. Prices paid ticked up another five points further into expansion, while delivery times continued to fall—a sign of slowing in most environments. On the bright side, expectations for business conditions six months in the future rose by seven points further into expansion. While only covering a single region, this continues to show the back-and-forth nature of these manufacturing reports as of late.

(-) **Existing home sales** in August fell by -0.7% to a seasonally-adjusted annualized rate of 4.04 mil. units, in contrast to a 0.7% gain expected by consensus. August results were led by a gain of 5% in condos/co-ops, offset by a -1% decline in the larger single-family group. Sales rose in the Midwest, while the West and South saw a decline of a few percent each. Overall nationwide sales are down -15% over the trailing 12 months, with the median existing home price rising 4% from last year to a new high of $407,100. The inventory of unsold homes fell -0.9% for the month, to a level of 3.3 months' supply, still well below the 5.0-or-so level deemed 'normal.' As it was put by the National Association of Realtors, which compiles this data, sales have been generally stable over the past few months, reiterating that mortgage rate changes will have a large impact in the short run, with inventory needing to roughly double to moderate home price gains (a tall order no doubt).

(-) **Housing starts** for August fell by -11.3% to a seasonally-adjusted annualized rate of 1.283 mil. units, far further than the median forecast of -0.9%. This was driven by a dramatic drop in the volatile multi-family space, of over -26%, as single-family declined by only -4%. Regionally, starts in the West fell -30%, to lead the downturn, while the Midwest and South saw mid-single-digit declines. (It's assumed that Hurricane Hilary on the West Coast played a large role in the single-month pullback in activity.) **Building permits**, on the other hand, rose 6.9% to an annualized rate of 1.543 mil. units, in contrast to a slight decline of -0.2% expected. Year-over-year housing starts were down -15% (led by a -42% drop in multi-family), with the NAHB noting that high mortgage rates continue to take a toll on builder confidence and consumer demand, and purchase delays becoming more common (with buyer hopes of lower rates later). Permits on a year-over-year basis show the disparity in current trends (which lag), with single-family up 7% and multi-family down -15% (although still very elevated), showing some better balance with market needs.

(-) The **NAHB Homebuilder Sentiment Index** for September fell by -5 points to a contractionary 45, below the 49 level expected. Present sales, future sales, and prospective buyer traffic all declined to a similar degree in the month, with the outright level of traffic remaining at a very low level due to tight inventories of finished homes to look at.

(+) **Initial jobless claims** for the Sep. 16 ending week fell by -20k to 201k, below the 225k median forecast. Continuing claims for the Sep. 9 week fell by a similar -21k to 1.662 mil., well below the 1.692 mil. expected. Claims declined by the most significant degree in the largest states, as would be expected, with little change in the underlying trend (no deterioration).

Market Notes

Period ending 9/22/2023	1 Week %	YTD %
DJIA	-1.89	4.13
S&P 500	-2.91	13.88
NASDAQ	-3.61	27.02
Russell 2000	-3.81	1.98

MSCI-EAFE	-2.04	8.63
MSCI-EM	-2.09	3.00
Bloomberg U.S. Aggregate	-0.50	-0.24

U.S. Treasury Yields	**3 Mo.**	**2 Yr.**	**5 Yr.**	**10 Yr.**	**30 Yr.**
12/31/2022	4.42	4.41	3.99	3.88	3.97
9/15/2023	5.56	5.02	4.45	4.33	4.42
9/22/2023	5.56	5.10	4.57	4.44	4.53

U.S. stocks began decently, but fell back starting just after the FOMC meeting, as investors took Chair Powell's comments regarding policy as 'higher rates for longer.' Naturally, this serves to pressure the economy, and notably earnings, further. The UAW strike has also intensified from only three plants to now nearly 40 around the nation, with uncertain duration and impact, in addition to a potentially upcoming government shutdown. Thursday's decline, while not severe, was the largest in six months. As it stands, the S&P 500 is down -6% from its peak in late July (drawdowns can be stealthy, with September again proving its negative reputation).

Every sector declined in value last week, led by consumer discretionary down -6% (pulled down by Tesla and Amazon, together which represent 50% of the sector, among others), as well as more cyclical materials and financials. As expected, more defensive utilities, health care, and consumer staples held up better, with lesser but still-present declines. Real estate fell back over -5% with a significant move higher in interest rates, affecting financing conditions and required cap rates. Small cap stocks fared significantly worse than large cap, presumably more negatively affected by higher financing rates as well.

Foreign stocks fell to a similar degree as U.S. stocks, in both developed and emerging markets. Central bank hawkishness in the U.S. was absorbed overseas as well, where policymakers have been on a similar trajectory. Europe, however, is faced with a far weaker economic environment, which has been seen by continued weaker currency movements vs. the U.S. dollar. The Eurozone PMI remained in contraction last month, as one example.

The Bank of England kept key rates unchanged as well, at 5.25%, although unlike the common unanimous votes in the U.S., the decision there was a close 5-4 (the dissenters wanted a quarter-point hike). The U.K. and other central banks in Europe are generally faced with the same difficult challenge of still-too-high-inflation, but far slower economic growth than in the U.S. On the other hand, several emerging market central banks, notably in Brazil and Latin America, have seen inflation come back down and are easing into rate cut regimes before high rates inflict too much economic damage. China, of course, has been cutting rates slowly due to this economic weakness already having taken hold. Generally, we seem to be seeing a widening of the divergences between different central bank policies.

Bonds fell back across the board last week, due to the Federal Reserve's message about 'higher rates for longer' being taken negatively for those hoping for swifter cuts in 2024. High yield fared worst, while investment-grade corporates and floating rate loans fared a bit better than U.S. Treasuries generally. With Treasuries, near-term yields (3-mo.) were unchanged, while the curve from 2 yrs. and beyond rose about 0.10%, reflecting the updated Fed expectations. Foreign bonds were held back a bit further by a stronger U.S. dollar during the week.

Commodities fell back for the week generally, with the headwind of a stronger dollar, with only precious metals up slightly. Crude oil was little changed last week, finishing at around $90/barrel, remaining elevated due to OPEC+ production cuts with an indefinite ending point.

Have a good week.

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Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, National Association of Realtors (NAR), Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, Univ. of Michigan, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post. Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

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Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.