Summary

Economic data for the week included both producer and consumer price indexes coming in lower, showing continued deceleration toward more normal levels. Retail sales and consumer sentiment improved, while industrial production and housing starts declined, with the latter likely driven by weather-related events.

Equities gained ground globally, following a week of high volatility, with both the U.S. and foreign markets seeing similar gains. Bonds also fared well as yields fell in response to decelerating inflation. Commodities were mixed with metals up and energy down, despite higher Middle East tensions.

Economic Notes

(+/0) **Retail sales** for July rose 1.0%, exceeding the median forecast of 0.4% and reversing a decline the prior month, along with revisions. In fact, this was the strongest single-month gain since Jan. 2023. Auto sales rose 4%, with an apparent recovery after the cyberattack that held back June sales. Removing the auto portion pared growth to 0.4%, led by building materials, while core/control sales (removing a variety of the more volatile components) trimmed the gain to 0.3%. The positive news is that over three-quarters of the major categories increased, led by electronics, food/beverage, health/personal care, and general merchandise; offsets were declines in misc. retail and sporting goods. Overall sales were up nearly 3% over the past year, although on an inflation-adjusted basis, that amounts to minimal net change and points to continued slowing of personal consumption.

(-) **Industrial production** declined by -0.6% in July, roughly double the -0.3% expected by consensus, in addition to a downward revision for the prior month. Year-over-year, industrial production is down a marginal -0.2%, with declines in auto manufacturing holding down gains of a percent in other manufacturing groups. For July, it was noted that shutdowns in the petrochemical industry in advance of Hurricane Beryl played a fairly significant role—accounting for up to half of the overall decline—along with retooling shutdowns in the auto sector. Within the report, manufacturing production fell by -0.6%, led by a -12% drop in auto assemblies (pointing to the factory maintenance), while business equipment production only fell by a few tenths of a percent, and mining production was little changed. On the positive side, high-tech equipment rose by 1%, and is up 7% from last year as one of the brighter spots in the group. Utilities production fell -4%, an area which tends to be weather-related, but is an input into GDP's consumption calculation. **Capacity utilization** fell by -0.6% to 77.8%.

(-) The **Philadelphia Fed manufacturing index** fell by a dramatic -20.9 points back to a contractionary -7.0, below the 5.2 level expected. The composition also showed weakness, with new orders and shipments falling, but remaining in expansion, while employment fell sharply into a slight contraction. Prices paid ticked higher, remaining in solid expansion, while prices received fell back a bit, but stayed in expansion. The business conditions index 6-months ahead fell by -23 points but stayed in expansion at 15.

(0/-) The **Empire manufacturing index**, on the other hand, rose by 1.9 points to a still-contractionary -4.7, above the -6.0 level expected. New orders fell further into contraction, while shipments fell a bit but remained slightly in expansion, and employment saw gains but remained in contraction. Prices paid fell back a few points but stayed in expansion, while prices received ticked slightly higher and continued to expand to a lesser degree. While the business conditions index 6-months ahead ticked down by a point, it remained solidly expansionary at a reading of over 47. These regional surveys have remained quite volatile in recent months, which has reduced their usefulness compared to the broader ISM manufacturing and other indexes.

(+/0) The **Consumer Price Index** in July rose just under 0.2%, reversing the -0.1% decline of the prior month, and in line with expectations. Core CPI was also up 0.2%, a tenth higher than the prior month—meeting expectations. While energy was unchanged, items in the core part of the index provided more stickiness, including shelter rising 0.4% (which accounted for 90% of the gain in the all-items index, per the BLS), which also could have been due to twice-a-year changes in the underlying survey group. Other notable gains for July were seen in auto insurance (1.2%), food, household furnishings/operations, education, recreation, and personal care; price declines occurred in used cars/trucks (-2.3%), airfares (-1.6%), medical care, and apparel.

On a year-over-year basis, headline CPI decelerated by a tenth to 2.9% (the smallest 12-month differential in three years) as did core CPI to 3.2%. Shelter prices rising 5% for the year provided the most substantial contribution. While energy commodity prices declined -2%, other energy categories saw higher prices. Used car prices have fallen -11% for the year, as an example of certain goods prices normalizing, such as appliances and furniture each down several percent on the year. Both headline and core CPI have continued to improve at the margin, albeit at a measured pace, but perhaps good enough for the Fed to proceed with a change in policy toward easing.

High shelter inflation continues to be a problem, at least in terms of the official measurement in CPI, where it has been known to feature a sizable lag. Other real estate data providers, like Zillow, have shown signs of housing rents declining for almost a year (in a similar degree to their showing rents rising in earlier years, well before that tendency showed up in CPI). This has been debated to a rising degree among economists, where there's interest in a better real-time indicator, given that shelter accounts for 36% of headline CPI.

For overall perspective's sake, monthly headline CPI has been calculated officially in the U.S. since 1913, equating to an average annualized growth rate of 3.2% (with a standard deviation of 4.9%) through July. That includes both extremes of the deeply deflationary 1930s and inflationary 1920s, 1940s, and 1970s, with data collection seemingly far better today than it was at the start of the project. Core CPI that removes volatile food and energy prices was carved out in 1957, showing a higher compound average of 3.6% since. (This is virtually the same as headline CPI for that time period, with an upward bias compared to the 1913 series due to it including more of the late 1970s/early 1980s inflationary bout, and fewer and less extreme deflationary periods.) For the last 20 years, headline and core CPI have come in at 2.6% and 2.5%, respectively. The 'normal' inflation objective of 2.0% has never really been in effect until more recent Fed regimes, with some economists debating whether or not it's even a realistic long-term goal, or simply one based on a snapshot in time. So, if one wanted to say that we're already back within a normal range, it wouldn't be inaccurate.

(+) The **Producer Price Index** for July came in up 0.1% on a headline basis, driven by gains of 1.9% for energy and 0.6% for food, and unchanged on a core level. These were below the median forecast of 0.2% for each and continued to point to ongoing easing of price pressures. For the single month, goods prices rose 0.6%, while services declined by -0.2%, the latter mostly in wholesaler margins for machinery and autos. Year-over-year, headline PPI rose 2.2%, while core increased 2.4%—both continuing to move back to more normal trend levels. By segment for the year, final demand goods rose only 1.7% (held down by energy prices), while final demand services rose 2.6% (driven by wage growth).

(-) **Housing starts** fell by -6.8% in July to a seasonally-adjusted pace of 1.238 mil. units, below the -1.5% decline expected by consensus, in addition to revisions downward for the prior month. This was actually the lowest level since 2020. Single-family starts fell by -14%, offset by a 15% rise in multi-family. The South saw a drop of -101k, no doubt affected by Hurricane Beryl, in addition to a -36k drop in the West, which was likely tied to the extreme heat; by contrast, starts in the Northeast gained 49k. **Building permits** fell -4.0%, double the expected -2.0% decline for the month, and led by the multi-family component down -11%, while single-family permits changed little. The regional composition was largely similar to starts, implying similar weather considerations, which can alter these numbers dramatically month-to-month.

(+) The preliminary **Univ. of Michigan index of consumer sentiment** for August rose by 1.4 points to 67.8, exceeding the 66.9 expected, and representing the first increase in nearly six months. While assessments of current economic conditions fell by -2 points, expectations for the future improved by over 3 points. Inflation expectations for the coming one year and 5-10 year periods were unchanged at 2.9% and 3.0%, respectively, with each a tenth above expectations. As has been the case for a while, political leanings have affected sentiment results with Democrat sentiment rising over 5% with Vice President Harris taking over as nominee, while sentiment among Republicans declined by an equivalent percentage.

(+) **Initial jobless claims** for the Aug. 10 ending week fell by -7k to 227k, contrary to expectations of a small increase to 235k. Continuing claims for the Aug. 3 week also fell by -7k to 1.864 mil., below the median forecast calling for 1.870 mil. It still appears that claims in MI and TX remain elevated, due to the assumed impacts of auto plant maintenance shutdowns and residual hurricane impacts. Claims are being watched now more closely again, with markets looking for any additional signs of labor markets weakening. While claims did tick up, it's often difficult in real time to untangle other random and variable seasonal effects like factory maintenance, storms, and summer extreme heat-related shutdowns.

Market Notes

Period ending 8/16/2024	**1 Week %**	**YTD %**
DJIA	3.02	9.15
S&P 500	3.99	17.47
NASDAQ	5.35	18.00
Russell 2000	2.98	6.56
MSCI-EAFE	4.09	8.30
MSCI-EM	2.90	8.84
Bloomberg U.S. Aggregate	0.53	2.91

U.S. Treasury Yields	**3 Mo.**	**2 Yr.**	**5 Yr.**	**10 Yr.**	**30 Yr.**
12/31/2023	5.40	4.23	3.84	3.88	4.03
8/9/2024	5.33	4.05	3.80	3.94	4.23
8/16/2024	5.33	4.06	3.77	3.89	4.15

U.S. stocks reversed course from the prior week's volatility, earning the best weekly returns in a year. By sector, growth leadership resumed with technology gaining nearly 8% (led by a 20% rise in NVIDIA), followed by consumer discretionary up over 5% (with Starbucks gaining sharply after appointing a new CEO from Chipotle). Laggards included communications, as well as energy and utilities, all of which were up only about a percent. Real estate was only slightly positive. Interestingly, declines in Alphabet/Google have been somewhat muted considering the U.S. Justice Department's interest in potentially breaking up the firm due to what are claimed to be monopolistic practices.

Stocks started the week strongly on Tue., with a lower-than-expected PPI report, while the CPI data Wed. was decent, but not earth-shattering. As the narrative of a continued pace of inflation deceleration was kept intact (sustaining the high chances of an FOMC rate cut in Sept.), it perhaps created a 'buy the rumor, sell the news' moment, as stocks pulled back a bit. The Thu. jobless claims and retail sales data (and positive revenue/earnings report for Walmart) seemed to alleviate some concerns over the health of the consumer, especially with that particular stock seen somewhat as a bogey of spending conditions for lower income Americans.

Foreign stocks performed roughly in line with U.S. stocks for the week, with rising hopes for rate cuts by the ECB and Bank of England. Q2 GDP for Europe and the U.K. rose at rates of 0.6% and 0.3%, respectively, continuing a stretch of weaker growth. Japan outperformed Europe, in a recovery from volatility the prior week; despite a weaker yen, economic growth came in stronger than expected for Q2, at an annualized 3.1% pace, reversing a contraction in Q1. This is in addition to likely relief over the central bank's realization that policy tightening might require a softer touch to not disrupt the yen 'carry trade' that has been in effect in some form for decades. In emerging markets, most countries saw positive returns, led by South Korea and Taiwan, which have been closely connected to U.S. technology sentiment.

Bonds also fared well last week, as yields ticked down along the longer part of the U.S. Treasury yield curve. These appeared to be in response to the improved PPI and CPI inflation data, which raises the chances of a Federal Reserve rate cut in September. Both investment-grade and high yield bonds outperformed, as spreads also tightened again, although floating rate bank loans also earned positive returns. Foreign bonds fared positively, as the U.S. dollar declined about a half-percent on the week.

Commodities were mixed for the week, with gains of 2-3% in industrial and precious metals offset by declines in energy and agriculture. After rising on Monday morning for a bit, along with a continued ramp-up in hostilities between Israel and Iran, crude oil prices ended the week down a bit at $75.50/barrel.

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, 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, Zillow. 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.

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