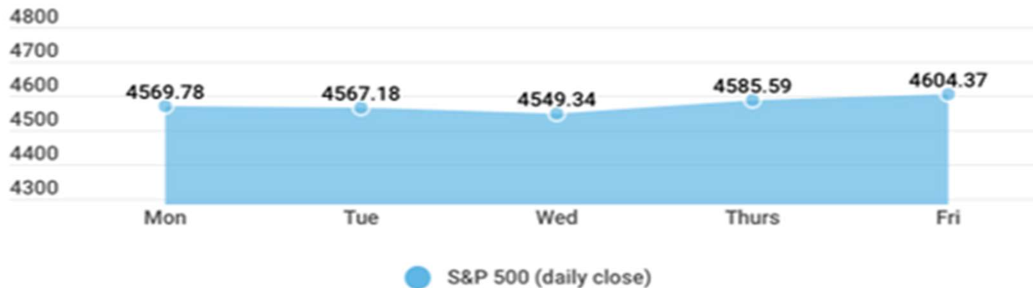
WEEKLY ECONOMIC UPDATE DEC. 11, 2023

A late-week, two-day rally left stocks higher, adding to November's gains as the last month of trading for 2023 began.

The Dow Jones Industrial Average was flat (+0.01%), while the Standard & Poor's 500 gained 0.21%. The Nasdaq Composite index advanced 0.69% for the week. The MSCI EAFE index, which tracks developed overseas stock markets, was up 0.37%.[1,2,3]

Market Index	Close	Week	Y-T-D
DJIA	36,247.87	+0.01%	+9.35%
NASDAQ	14,403.97	+0.69%	+37.62%
MSCI-EAFE	2,138.29	+0.37%	+10.00%
S&P 500	4,604.37	+0.21%	+19.92%



	Treasury	Close	Week	Y-T-D
	10-Year Note	4.23%	+0.01%	+0.35%

Sources: The Wall Street Journal, December 8, 2023; Treasury.gov, December 8, 2023
Weekly performance for the Dow Jones Industrial Average, Standard & Poor's 500 Index, and NASDAQ Composite Index is measured from the close of trading on Friday, December 1, to Friday, December 8 close. Weekly performance for the MSCI-EAFE is measured from Friday, December 1 open to Thursday, December 7 close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

Stocks Extend Gains

The relationship between the bond and stock markets–which pushed stocks higher in November (i.e., falling bond yields, rising stock prices)–disappeared last week, with stocks falling in the first three days of the week despite declining yields. Yields dropped following a weak job openings report, the ADP employment update, and a substantial productivity revision.

On Thursday, investor enthusiasm returned with force on Artificial Intelligence (AI) related news. One AI chip manufacturer announced a new AI chip, followed by a mega-cap tech company unveiling an enhanced version of its AI model for business use. Stocks continued their climb on Friday despite rising yields, as investors viewed a stronger-than-expected employment report as increasing the potential for a soft landing.

Productivity Surges

Higher productivity may be the most effective and preferred way to reduce inflation. Last week's revised third-quarter productivity report saw an upward revision of the annualized productivity growth from the initial report of 4.7% to 5.2%; this was welcome news on the inflation front and an encouraging development for future corporate profits.[4]

The 5.2% jump in productivity represented the fastest pace since the third quarter of 2020. The report also showed unit labor costs falling at a 1.2% annualized pace, reflecting a cooling of wage-growth inflationary pressures. Productivity has increased for two straight quarters, potentially allowing the Fed to ease its restrictive monetary policy.[5]

This Week: Key Economic Data

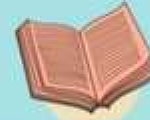
Tuesday: Consumer Price Index (CPI).

Wednesday: Producer Price Index (PPI). FOMC Announcement.

Thursday: Retail Sales. Jobless Claims.

Friday: Industrial Production. Purchasing Managers' Index (PMI) Composite Flash.

Quote of the Week



“Going forward, we are emerging into a post-modern surrealist information landscape where truth has become subject to a post-modern golden rule - those with the gold make the rules.”

– Robert Malone

Of Note

Most people look at the stock market as a sign of the health of the economy. If the stock market is moving higher in value, things must be good. The truth of the matter is that the stock market isn’t as important as the debt market, specifically the interbank debt market.

What goes on in the interbank market has a direct effect on what happens in the stock market. A healthy interbank market gives the stock market the footing it needs to sustain a rally. When it breaks, as we saw in 2008 and in March 2020 during the COVID-19 pandemic, the stock market drops precipitously.

The interbank debt market is the market for money and loans between banks and between those same banks and the Federal Reserve. It’s called the overnight repo market. The Fed uses open-market actions such as customer repos and reverse repos to add or take liquidity out of the market. Banks make overnight loans to each other.

Big institutions that have excess cash on their balance sheets also execute trades in the overnight repo market to grab a little more yield overnight. The market valuation is in the trillions of dollars. When we have huge drops in the stock market value, it’s usually because there's some sort of ripple tearing through the interbank debt market. In 2008,

banks didn’t trust each other’s balance sheets, and the market froze, drying up all liquidity with the corresponding drop in stocks.

If the interbank market is any guide, we appear to be headed for some rough and volatile sledding in the stock market. The increase in the debt ceiling means that the Fed is going to issue $1.4 trillion in new debt between now and the end of the year. Who's going to buy that debt? This has always been a conundrum for the market. But today, some of the largest potential foreign buyers of our debt aren’t being as accommodating. U.S. pension funds and other U.S. funds hold the lion’s share of U.S. debt, but it's unclear if they want to buy a lot more at current prices. There's uncertainty, and that creates volatility.

The cash that's currently flowing into the reverse repo market will flow into some of those Treasurys, but the problem is that the market is an overnight program. Treasurys are longer-denominated instruments. Liquidity is going to flow out of the system at a rate we haven't seen for a long, long time, if ever.

When this happened before, we didn’t have the inflationary pressure created by massive government overreach and spending during COVID-19 and post-COVID with the first Biden budget that we have today. Coming into an election cycle, it will be impossible for the government legislative bodies to solve the lack of liquidity. The Fed will be in a very tough spot to try to solve it since it's the inflation fighter now. Creating more liquidity will spur higher rates of inflation.

Not only that, but the Fed has to be worried about unemployment. Data shows that in places such as Costco, customers are buying more chicken and pork than beef. Is that a change in consumer preferences or is it a sign of recession? States including California have seen tax revenues plummet. Is that a sign of recession or that startups have laid off people and people have fled the state? All this creates more risk in the stock market, but currently, we're witnessing a relief rally after the manufactured debt-ceiling drama. Right now, the VIX, a measure of risk in the stock market, is collapsing to yearly lows.

It's anyone’s guess as to where you might see the crack forming. Some people think we'll see it in the listed options market. If there's a larger than normal activity of put buying, we ought to see it in prices. Others speculate that a collapse in the cryptocurrency market will be the first sign, because cryptocurrency is a highly risky and fickle asset class. Another place to look at is the secured overnight financing rate (SOFR) contract at the CME Group. If the near-term SOFR contract starts to aggressively get bid up in value and seems disjointed with the rest of the debt market, it’s a sign that banks don’t want to lend to each other and that there's a lot of fear in the market.

The problem for anyone is that you can't time when something might

happen. Economists such as David Rosenberg have said that there's a tidal wave forming and that it looks like it will hit the beach. Buckle up, then, and don’t listen to the mainstream media when it comes to happy or sad talk about the stock market. They don’t see it coming. But it looks like it's coming.[6]

Footnotes and Sources

1. The Wall Street Journal, December 8, 2023
2. The Wall Street Journal, December 8, 2023
3. The Wall Street Journal, December 8, 2023
4. MarketWatch, December 6, 2023
5. MarketWatch, December 6, 2023
6. theepochtimes.com/opinion/the-interbank-debt-market-a-warning-sign-for-the-stock-markets-future-5313271

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