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In this week's recap: Employment reports and consumer confidence are up; stock market replies favorably.

Weekly Economic Update

Presented by Ed Papier, July 5, 2021

THE WEEK ON WALL STREET

Strong employment reports and rising consumer confidence sent the stock market broadly higher last week.

The Dow Jones Industrial Average rose 1.02%, while the Standard & Poor's 500 picked up 1.67%. The Nasdaq Composite index gained 1.94%. The MSCI EAFE index, which tracks developed overseas stock markets, lost 1.42%. [1,2,3]

STOCKS RALLY

Rising conviction in the economic recovery and waning inflation worries drove stock prices higher, with the S&P 500 and Nasdaq Composite racing to record closes to begin the week.

Amid the week-long march higher, market leadership changed hands throughout the five-trading days. The leadership baton alternated between the technology and high-growth companies, which responded to lower bond yields, and cyclical stocks, which rallied on higher oil prices and successful bank stress tests.

Economic news buoyed investor sentiment as consumer confidence rose and an improving labor market—weekly initial jobless claims came in at a pandemic-era low (364,000), while employers added 850,000 new jobs in June—sent the S&P 500 and Nasdaq Composite to new record highs to close out the week. [4,5]

A CONFIDENT CONSUMER

Market sentiment was lifted by a rise in The Conference Board's Consumer Confidence Index, which reached its highest level since the onset of the pandemic in March 2020. This was the fourth-straight month of increases in consumer-confidence levels. [6]

The consumer outlook for income, business, and labor market conditions over the short-term improved markedly. Interestingly, consumer confidence and buying intentions appear largely unaffected by the possibility of rising inflation. In fact, the survey showed a rise in the number of consumers expecting to purchase homes, automobiles, or home appliances. Vacation intentions also rose. [6]

THE WEEK AHEAD: KEY ECONOMIC DATA

Tuesday: ISM (Institute of Supply Management) Services Index.

Wednesday: JOLTS (Job Openings and Labor Turnover Survey) Report. FOMC (Federal Open Market Committee) minutes.

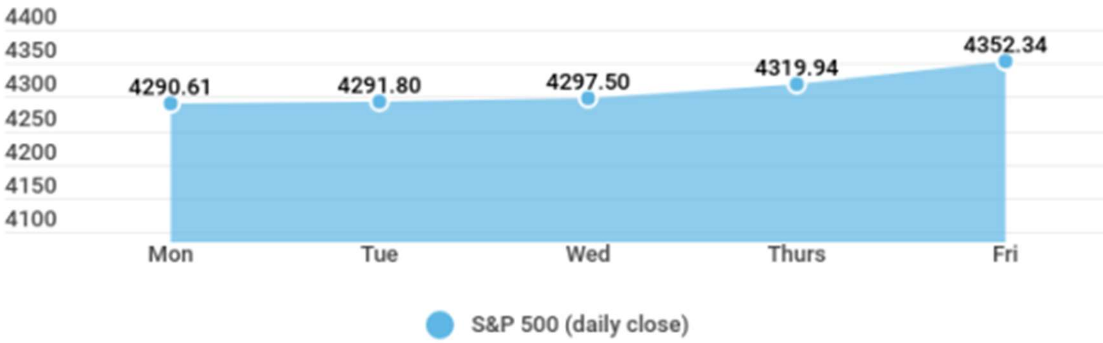
Thursday: Jobless Claims.

QUOTE OF THE WEEK

"Contentment is natural wealth, luxury is artificial poverty"

SOCRATES

Market Index	Close	Week	Y-T-D
DJIA	34,786.35	+1.02%	+13.66%
NASDAQ	14,639.33	+1.94%	+13.59%
MSCI-EAFE	2,309.27	-1.42%	+7.53%
S&P 500	4,352.34	+1.67%	+15.87%



	Treasury	Close	Week	Y-T-D
	10-Year Note	1.44%	-0.10%	+0.51%

Sources: The Wall Street Journal, July 2, 2021; Treasury.gov, July 2, 2021
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, June 25, to Friday, July 2, close. Weekly performance for the MSCI-EAFE is measured from Friday, June 25, open to Thursday, July 1, close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

OF NOTE

We have a fine-sounding word for running with the herd: momentum. When the herd is running, those who buy what the herd is buying and sell what the herd is selling are trading momentum, which sounds so much more professional and high-brow than the noisy, dusty image of large mammals (and their trading machines) mindlessly running with the herd.

We also have a fine-sounding phrase for anticipating where the herd is running: front-running. So, when the herd is running into stocks, those who buy stocks just ahead of the herd are front-running the market.

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When the Federal Reserve announces that it's going to make stock owners even wealthier with some new financial concept, those betting that stocks will never go down because the Fed has our back are front-running the Fed.

There are two remarkable assumptions at the heart of momentum and front-running: The momentum herd and those front-running the herd base their behavior on the assumption that there will always be other people who will sell all the shares they want to buy at today's prices before the run-up to new highs.

The first assumption of those front-running the market is that there is a large enough sub-herd of people who for whatever reason aren't smart enough to front-run the herd, and who will foolishly sell their stocks just before they double in value. The second assumption is that there will also be a large enough group of people who will buy all the shares they want to sell at the top, just before the bubble pops and the value of the newly purchased shares falls in half.

There are various ways to state this, but the bottom line is that momentum and front-running are only profitable if you sell at the top, just before the bubble bursts.

You would be forgiven for anticipating that the same group front-running the herd and the Fed on the way up to the top of the bubble would be just as prescient and active in front-running the inevitable bursting of the bubble, but this is not how running with the herd works. Short interest recently plumbed multi-year lows, indicating that very few are front-running the market crash.

Those trading momentum and front-running the herd/Fed are making a remarkable assumption, an assumption which is visible in a great volume of financial-media content: the stock market, we're told, will continue to make new highs like clockwork until some point in the third or fourth quarter, at which point there may well be a spot of bother, i.e., a crash.

In other words, the assumption being made is: I can wait until just before the crash to sell, because there will be boatloads of people who will buy all the shares I want to sell at today's lofty prices — or higher, and this liquidation won't push valuations off a cliff.

Regrettably, a risk arises from the disconnect between the precariousness of the manipulated market and the extreme confidence stock buyers have in its stability and predictability. This stability is entirely fabricated and therefore it lacks the dynamic stability of truly open markets.

Markets that are being distorted/manipulated to achieve a goal that is impossible in truly open markets — for example, markets that only loft higher with near-zero volatility — lull participants into a dangerous perception that because markets are so stable, risk has dissipated.

In actuality, risk is skyrocketing beneath the surface of artificial stability because the market has been stripped of the mechanisms of dynamic stability. This artificial stability derived from sustained manipulation has the superficial appearance of low-risk markets, i.e., low levels of volatility, but this lack of volatility derives not from transparency but from behind-the-scenes suppression of volatility.

Another source of risk in distorted markets is the illusion of liquidity. In low-volume markets of suppressed volatility, participants are encouraged to believe that they can buy and sell whatever securities they want in whatever volumes they want without disturbing market pricing and liquidity. In other words, participants are led to believe that the market will always have a bid due to the near-infinite depth of liquidity: no matter how many billions of dollars of securities you want to sell, there will always be a bid for your shares.

In actual fact, the bid is paper-thin, and it vanishes altogether once selling rises above very low levels. Heavily manipulated markets are exquisitely sensitive to selling because the entire point is to limit any urge to sell while encouraging the greed to increase gains by buying more.

On top of these grossly misleading distortions, stock owners have been encouraged to believe in the ultimate distortion: the Federal Reserve will never let markets decline again, ever. This is the perfection of moral hazard: risk has been disconnected from consequence.

This is why distorted, manipulated markets always end the same way. First there is an unexpected emergence of risk, which was presumed to be banished; second, a market crash as the paper-thin bid disappears and prices flash-crash to levels that wipe out all those forced to sell by margin calls, and then the collapse of faith in the manipulators (the Fed), collapse of the collateral supporting trillions of dollars in highly leveraged debt and then in a worst case scenario, the collapse of the entire delusion-based financial system.

Amidst the ruins generated by well-meaning manipulation and distortion, the "well meaning" part will leave an extremely long-lasting bitter taste in all those who failed to differentiate between the false signals and distorted information of manipulated markets and the trustworthy transparency of signals arising in truly open markets.

In summary: risk has not been extinguished, it is expanding geometrically beneath the false stability of a monstrously manipulated market. Risk cannot be extinguished, rather, it can only be transferred. By distorting markets to create an illusion of low-risk stability, the Federal Reserve has transferred this fatal supernova of risk to the entire financial system. [7]

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The Dow Jones Industrial Average is an unmanaged index that is generally considered representative of large-capitalization companies on the U.S. stock market. Nasdaq Composite is an index of the common stocks and similar securities listed on the NASDAQ stock market and is considered a broad indicator of the performance of technology and growth companies. The MSCI EAFE Index was created by Morgan Stanley Capital International (MSCI) and serves as a benchmark of the performance of major international equity markets, as represented by 21 major MSCI indexes from Europe, Australia, and Southeast Asia. The S&P 500 Composite Index is an unmanaged group of securities that are considered to be representative of the stock market in general.

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CITATIONS:

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