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In this week's recap: Debt ceiling raised until December; employment numbers paint confusing picture.

Weekly Economic Update

Presented by Ed Papier, October 11, 2021

THE WEEK ON WALL STREET

The overhang of bumping against the federal debt ceiling was lifted last week with an agreement to extend the debt ceiling through early December, helping propel stocks to a weekly gain.

The Dow Jones Industrial Average increased by 1.22%, while the Standard & Poor's 500 added 0.79%. The Nasdaq Composite index gained 0.09%. The MSCI EAFE index, which tracks developed overseas stock markets, was flat (+0.11%).[1,2,3]

DEBT CEILING CONCERNS EVAPORATE, FOR NOW

After suffering losses on concerns over delays with raising the federal debt ceiling, stocks rebounded as the Senate moved toward finalizing a debt ceiling agreement. While the agreement is only a short-term solution, it was enough to embolden investors to buy stocks.

The week's rally ran out of gas on Friday, however, on a surprisingly weak employment report. Though the debt ceiling was the dominant concern in the markets last week, the market grappled all week with the headwinds of higher energy prices, rising bond yields, inflation, and less robust economic growth.

FUZZY EMPLOYMENT PICTURE

Employment remains a confusing and unpredictable element of this post-pandemic economic recovery. Automated Data Processing's employment report showed private sector jobs rose by a robust 568,000. This hiring surge may have been aided by the end of extended unemployment benefits and the return of children to school.[4]

This improving labor outlook was reinforced the following day as weekly initial jobless claims fell below their four-week moving average, while continuing claims fell by nearly 100,000. The employment report on Friday was a different story. The economy added a disappointing 194,000 jobs, making September the slowest month for job growth this year. The unemployment rate declined to 4.8%, while an increase in wages generated inflation worries.[5,6]

THE WEEK AHEAD: KEY ECONOMIC DATA

Tuesday: JOLTS (Job Openings and Labor Turnover Survey).

Wednesday: Consumer Price Index. FOMC (Federal Open Market Committee) Minutes.

Thursday: Jobless Claims.

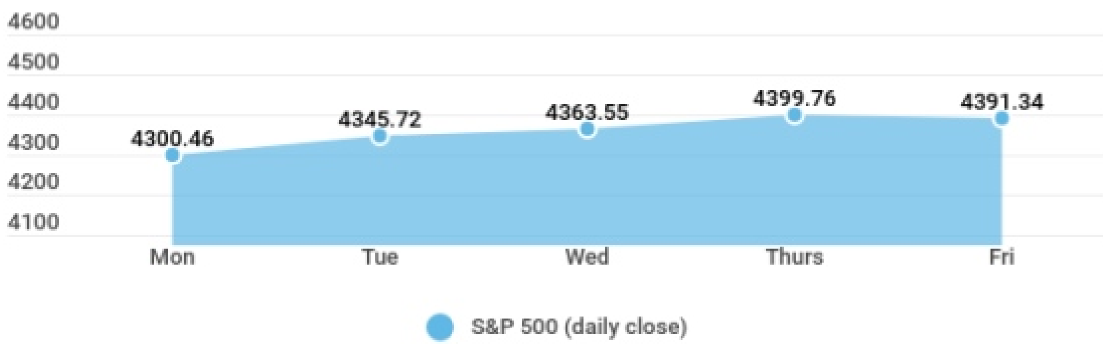
Friday: Retail Sales. Consumer Sentiment.

QUOTE OF THE WEEK

"There is hope, but not for us."

FRANZ KAFKA

Market Index	Close	Week	Y-T-D
DJIA	34,746.25	+1.22%	+13.53%
NASDAQ	14,579.54	+0.09%	+13.12%
MSCI-EAFE	2,266.37	+0.11%	+5.53%
S&P 500	4,391.34	+0.79%	+16.91%



	Treasury	Close	Week	Y-T-D
	10-Year Note	1.61%	+0.13%	+0.68%

Sources: The Wall Street Journal, October 8, 2021; Treasury.gov, October 8, 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, October 1, to Friday, October 8, close.

Composite index is measured from the close of trading on Friday, October 1, to Friday, October 8, close. Weekly performance for the MSCI-EAFE is measured from Friday, October 1, open to Thursday, October 7, close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

OF NOTE

The lessons of 2008-09 leave many smart and intelligent people's finances as unsuspectingly vulnerable as Paris in the spring of 1940. Treasury bills provided cover and safety when the stock market was falling in late 2008 and early 2009. This strategy may not work so well during the next crisis.

The lesson of the Great Depression in the United States was that cash is king. The instruction from the mass bank failures and bank runs of the 1930s was that cash should be hoarded, even stuffed in the mattress, where it's safe. Yet this lesson cost the depression era generation dearly in the inflationary 1970s. In just a 10-year period, the purchasing power of their savings was inflated away by half.

Similarly, today's retirement investors may be focused on another stock market crash. No doubt, they should be. Another stock market crash appears to be highly likely.

Moreover, the lesson from 2008-09, the COVID panic of 2020, and every financial panic going back to 1987, is that the Federal Reserve has investor's backs. And that a 60/40 stock to bond portfolio allocation provides the ultimate strategy for both capital appreciation and capital preservation. But what if the Federal Reserve is no longer in the position to have investor's backs?

When Alan Greenspan first executed the "Greenspan put" following the 1987 Black Monday crash, financial markets were well positioned for this centrally coordinated intervention. Interest rates, after peaking out in 1981, were still high. The yield on the 10-Year Treasury note was about 9 percent. There was plenty of room for borrowing costs to fall.

The mechanics of the Greenspan put are extraordinarily simple. When the stock market drops by about 20 percent, like in March of 2020 year, the Fed intervenes by lowering the federal funds rate. This typically results in a negative real yield, and an abundance of cheap credit.

This tactic has a twofold effect of observable market distortions. First, the burst of liquidity puts an elevated floor under how far the stock market falls – the put option effect. Second, the interest rate cuts inflate bond prices, as bond prices move inversely to interest rates. A 60/40 portfolio under this condition is a work of genius.

Thanks to the Greenspan put, the Fed has been running an implicit program of counter-cyclical stock market monetary stimulus since the late 1980s. Greenspan's successors – Ben Bernanke, Janet Yellen, and Jay Powell – have all ratcheted up the Fed's extreme intervention in financial markets via countless programs of outright money printing.

The purpose of these money printing programs is to bail out big banks and big businesses, and to keep financial markets inflated and Washington supplied with cheap credit. By all honest accounts, U.S. financial markets have been rigged for at least three decades. And there's no turning back.

At the same time, the conditions that made the Greenspan put possible are largely gone. The federal funds rate is near zero. The yield on the 10-Year Treasury note is about 1.59 percent. And consumer price inflation is now reducing the purchasing power in earnest.

The Fed has painted itself into a corner. What's more, a 60/40 stock to bond portfolio allocation is targeted to fighting the last war. For investors, it's a liability. Those that employ it will be mowed down with machine-like precision. Something more thoughtful is needed to successfully fight the investment enemies now mobilizing.[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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4. CNBC, October 6, 2021
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