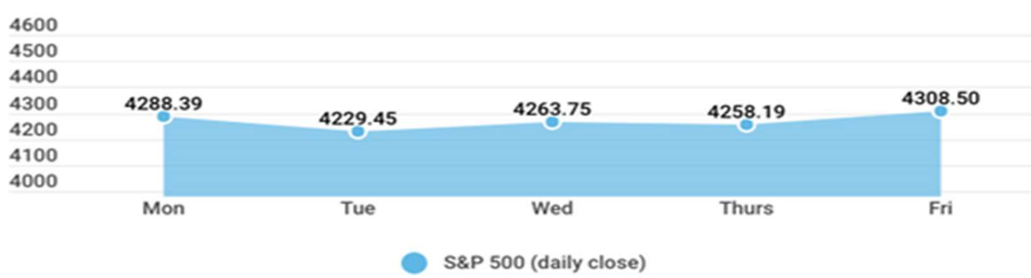
WEEKLY ECONOMIC UPDATE OCT. 9, 2023

A Friday rally overcame a shaky week, sending stocks mostly higher.

The Dow Jones Industrial Average slipped 0.30% for the week. Meanwhile, the Standard & Poor's 500 gained 0.48%, and the Nasdaq Composite index added 1.60% for the five trading days. The MSCI EAFE index, which tracks developed overseas stock markets, fell 2.37%.[1,2,3]

Market Index	Close	Week	Y-T-D
DJIA	33,407.58	-0.30%	+0.79%
NASDAQ	13,431.34	+1.60%	+28.33%
MSCI-EAFE	1,983.21	-2.37%	+2.02%
S&P 500	4,308.50	+0.48%	+12.22%



	Treasury	Close	Week	Y-T-D
	10-Year Note	4.78%	+0.19%	+0.90%

Sources: The Wall Street Journal, October 6, 2023; Treasury.gov, October 6, 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, September 29, to Friday, October 6 close. Weekly performance for the MSCI-EAFE is measured from Friday, September 29 open to Thursday, October 5 close. Weekly and year-to-date 10-year Treasury note yield are expressed in basis points.

Friday Rally

Stocks rallied on Friday after a stronger employment report than Wall Street expected. The headline increase in September payrolls initially generated fears of further Fed rate hikes, leading to a spike in bond yields and steep early morning losses. A yield retreat may have triggered the turnaround as investors focused more on the month's moderate wage growth.

Stocks were shaky for much of last week on rising bond yields. When Treasury yields hit their highest level since 2007 on Tuesday, stock prices dropped, leaving the Dow Industrials in negative territory for the year. The catalyst for the day's spike in interest rates was a surprisingly strong JOLTS (Job Openings and Labor Turnover Survey) showing nearly one million more open jobs than investors had expected.[4]

All About Jobs

The labor market remains resilient. August JOLTS showed job openings exceeded 9.6 million, above the consensus estimate of 8.8 million. A weak Automated Data Processing (ADP) private payroll job growth (released Wednesday) that showed 89,000 new private sector jobs appeared to be an outlier compared to the other reports.[5,6]

Friday's monthly employment report showed a robust gain of 336,000 new jobs, nearly double the consensus forecast of 170,000. At the same time, the previous two months saw significant upward revisions of 119,000 (combined) from initial reports. Wage gains rose modestly, coming in below expectations and striking a hopeful note on inflation.[7]

This Week: Key Economic Data

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

Thursday: Consumer Price Index (CPI). Jobless Claims.

Friday: Consumer Sentiment.

"There are two kinds of fools: those who can't change their opinions and those who won't."

–Josh Billings

Of Note

Once again, due to the ongoing lack of fiscal responsibility in Washington, the markets and the economy faced a Government shutdown. After a day of theatrics, Congress passed a “stopgap” measure that will keep the Government operating for 45 days. But is that a good thing?

First of all, while much media hyperbole surrounds Government shutdowns, much like the debt ceiling, there is a long history of shutdowns going back to the 70s. As Katherine Buchholz of Statista recently penned:

“The 2018/19 Government shutdown was the longest in recent U.S. history at 34 days. A timeline shows that government shutdowns have been getting longer in the last three decades, with the second and the fourth-longest Government shutdowns taking place in 1995 and 2013, respectively. Throughout the 1980s, shutdowns were numerous but shorter, while in the 1970s, they also ran somewhat longer but only surpassed two weeks once, in 1978. Government shutdowns aren’t all that rare: Since 1976, there have been 20 shutdowns that lasted an average of 8 days.“

While the latest measure provides funding, we will likely deal with this again in mid-November. What is notable, however, is that the Government has stopped functioning normally since 2008. Before the Obama administration, the Government operated on an annual fiscal budget. The House of Representatives would put together a budget for spending, the Senate would make its modifications, and then it would go back to the House for reconciliation. Once complete, it would move to the President for signature. Funding would then be allocated accordingly.

However, since 2008, the Government has continued to operate without a budget. Rather than passing a budget each year, a “Continuing Resolution” is passed to fund spending. The problem with using Continuing Resolutions is that it uses the previous spending levels and increases that spending by 8%. This is why, since 2008, the debt has exploded as spending compounds annually. Of course, given the massive surge in spending, revenues cannot keep up the pace, leading to a rapid increase in debt issuance and a trending deficit.

It is worth noting that before 2008, revenues were greater than the running growth trend of public debt. However, post-2008, this has not been the case. Subsequently, the growth in the deficit continues to accelerate. However, does this mean a calamity is at hand with the Government now shut down?

While the media and Government officials will declare victory over avoiding a Government shutdown, is it a victory? Washington, D.C., has a long history of “kicking the can” to avoid doing their job of governing. That job sometimes includes making unpopular decisions that cause short-term pain in order to create a healthier economy in the years ahead.

Rather than taking the easy path, it is essential to understand what occurs during a Government shutdown. Yes, roughly 900,000 “non-essential” workers will be furloughed. While their salaries will accrue during the furlough, the lack of income will impact economic growth. That impact would be relatively minor, and based on past shutdowns, Goldman Sachs estimated a reduction of annualized growth by around 0.2% for each week it lasted after accounting for modest private-sector effects.

Given that the longest historical shutdown lasted 35 days, you can estimate the impact on economic growth could be roughly as much as 1%. Yes, that is certainly concerning, but with economic growth running near 5% according to the latest Atlanta Fed GDPNow, that is not a recessionary concern.

What is critical to understand about Government shutdowns is that mandatory spending (social security, welfare, interest on the debt) continues as needed. Shutdowns are primarily about discretionary spending. That is why it mainly involves Government employment and the shuttering of national parks and monuments. According to Goldman Sachs, the shutdown would have only impacted about 2% of Federal spending overall. Notice that the vast majority of Government spending is directly a function of the social welfare system and interest on the debt.

As of the latest annual data, through the end of Q2-2023, the Government spent $6.3 trillion, of which $5.3 trillion went to mandatory expenses. In other words, it currently requires 113% of every $1 of revenue to pay for social welfare and interest on the debt. Everything else must come from debt issuance.

While a Government shutdown would undoubtedly create a minor negative impact on economic growth, perhaps that would be an acceptable price to return the Government to some form of fiscal responsibility.

While the mainstream media's hyperbole about Government shutdowns is undoubtedly concerning, the reality is that they have little impact on both the economy and the financial markets. The fiscal irresponsibility in Washington, D.C., which continues to erode economic growth, prosperity, and a stronger middle class, should be of more concern.

Like a forest fire cleanses and fertilizes the soil, making the forest healthier, perhaps a Government shutdown that returns some fiscal responsibility to Washington might be a good thing.[8]

Footnotes and Sources

1. The Wall Street Journal, October 6, 2023
2. The Wall Street Journal, October 6, 2023
3. The Wall Street Journal, October 6, 2023
4. CNBC, October 3, 2023
5. CNBC, October 3, 2023
6. CNBC, October 4, 2023
7. CNBC, October 6, 2023
8. zerohedge.com/markets/government-shutdown-averted-good-thing

quality, inflation risk, market valuations, prepayments, corporate events, tax ramifications and other factors.

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