Market Update

Economic News

August 21, 2019

As investors await the beginning of the Jackson Hole central bank gathering tomorrow, today's attention will be focused on the minutes from the July 31 FOMC meeting. Recall the Fed delivered a much anticipated 25bps rate cut, initiating the first easing cycle in more than a decade. The post-meeting press conference by Fed Chair Jay Powell muddied the rate-cut message, however, by characterizing it as a "mid-cycle adjustment" and implied that while not a one-and-done rate cut, investors shouldn't expect this to represent a full-fledged easing cycle. That kicked off a period of market turmoil with Treasuries selling off from the mixed messaging. Enter President Trump's announcement that additional China tariffs would be initiated on September 1, and the rally in Treasuries was back on again. Ultimately the minutes will be scrutinized for any indication of the degree to which the Fed is weighing domestic strength against global weakness and the uncertainty created by the on-again, off-again tariff threats and geo-political concerns. We explore what we expect to see from the minutes as well as the Jackson Hole gathering in the paragraphs below.

Recall the July 31 FOMC meeting occurred before the early August market spasm that was spurred initially by said meeting and the muddled messaging from the Powell press conference. Thus, what exactly are we expecting to see in the minutes that will be of ongoing value given the subsequent events? One thing we'll be on the lookout for is the level of concern with global slowing versus domestic strength. In addition, how much of that concern over global slowing is something Fed officials think needs to be included in their ongoing reaction function and to what degree? Remember that part of the unspoken rationale for the July rate cut was to reverse the December 2018 rate hike that was viewed almost immediately as a mistake. Even with that easy out, we had two dissents of the July rate cut owing to insufficient signs of domestic economic weakness. Thus, will a second rate cut in September elicit even more dissents? We can envision a couple Fed presidents on the fence but willing to "reverse the mistaken December rate hike" and therefore acquiesced on the cut. That contingent may not agree to another rate cut until signs of economic weakness are more obvious. The minutes may provide a preview to that call.

In any event, signs of overseas slowing have increased since the July meeting along with increased uncertainty over the tariff and currency issues. Fold in geopolitical concerns from the Hong Kong protests, the dissolution of the current Italian government, and the slow-motion train wreck that is Brexit and it becomes hard to think things are better now than when the Fed met in late July.

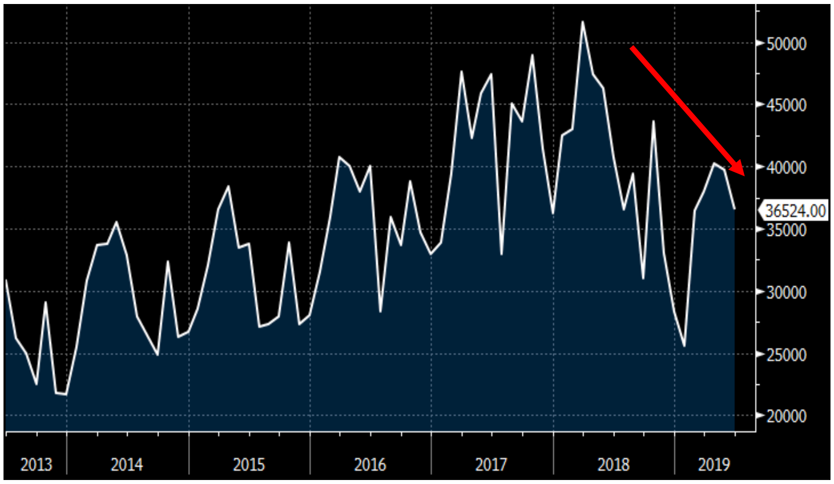
In addition, signs that Germany is considering fiscal stimulus measures, and the U.S.'s rumored consideration of payroll tax cuts, illustrates global slowing concerns continue to mount. The famously reticent Germans last embarked on fiscal stimulus in 2008, but, alas, this time they have offered that any stimulus would come only after entering a severe recession. Isn't it better to try and prevent a recession with an early dose of stimulus rather than rush in after the downturn accelerates? Given it's Germany and their almost genetic opposition to fiscal stimulus it could be a case of better late than never. And while the rumors of a U.S. payroll tax cut swirl, nobody in the administration is willing to admit as much on record.

The overarching point is that fiscal stimulus measures are finally being mentioned which illustrates more government policymakers are recognizing the limitations of monetary policy are fast approaching. That is likely to accelerate the global hunt for yield and safety driving long-end Treasury yields lower while short-term rates will fall as fast as the Fed signals additional cuts are coming. Fed fund futures are pricing in two 25bps rate cuts this year and another two in 2020.

It's hard to see the Fed getting ahead of that call right now given the aforementioned strength in the domestic economy. That's where Jackson Hole comes into play. While the FOMC members didn't have the last few weeks of events to consider at their July meeting, global central bankers in Jackson Hole this week do have that information. Will the message be one of unified concern over gathering global slowing with all monetary tools willing to be deployed, or will it be a more nuanced and limited response?

One thing that continues to ring in our ears is the level of concern Powell has shown in past statements, speeches and Q&A in keeping the economic expansion moving forward. Even with the latest CPI reading creeping higher, he also has seen increasing signs of global slowing, and increasing signs of trade and geopolitical uncertainty. This is his chance to signal clearly that he's on board with the market's call for two more cuts this year. It would surprise us to hear him push back against the expected rate cuts given the increasing trend in global uncertainties. Meanwhile, given the lack of clear signs of domestic weakening, however, probably prevents him from trying to out-dove the market this week. Thus, we see more chance of disappointment from the market coming out of Jackson Hole but one that should be limited and short-term in nature.

RV Shipments Rolling Over?



It's time again to check in with our favorite discretionary purchase indicator: shipments of recreational vehicles. As we've discussed in the past, if consumers are starting to have questions about the economy and/or their jobs RVs are probably at the leading edge of purchases that might be cut. This time, we are showing shipments through June. As shown, the industry was experiencing a rebound after the steep drop at year-end but May and June started falling off again and this is before the latest market turmoil in early August. In any event, the heady days of 2017 and early 2018 appear behind the industry as tax cut stimulus has worn off. The declining year-over-year trend paints a picture of a consumer less exuberant versus 2017 and 2018.

Agency Indications— FNMA/FHLMC Callable

Maturity (yrs)	2 Year	3 Year	4 Year	5 Year	10 Year	15 Year
0.25	2.07	2.09	2.14	2.21	2.45	2.67
0.50	1.91	1.95	2.02	2.10	2.38	2.61
1.00	1.71	1.76	1.84	1.93	2.25	2.49
2.00	-	1.49	1.59	1.69	2.09	2.30
3.00	-	-	-	-	1.93	2.18
4.00	-	-	-	-	1.81	2.09
5.00	-	-	-	-	1.71	2.02
10.00	-	-	-	-	-	NA