Weekly **Market Commentary**

THE WEEK IN REVIEW: Oct. 9 – 15

Next rate increase locked in at 75 basis points

September inflation data came in higher than expected last week. The producer price index (PPI) released on Wednesday was at the upper end of the consensus range at 0.4%, up 0.5 percentage points month-over-month. (August PPI was -0.1%.) The year-over-year PPI dipped slightly to 8.5% from 8.7%.

Bad news on inflation continued the following day, with the Consumer Price Index (CPI) following the same pattern as PPI. The year-over-year CPI number hardly budged between August and September, dipping ever-so-slightly from 8.3% to 8.2%.

The market tanked on the CPI announcement at first, then rocketed back up. The Dow went on a wild swing over 1,400 points; when the smoke cleared, the Dow was up over 800 points and nearly 3% for the day. But by Friday, rising rate fears again gripped the markets and the 10-year Treasury rose above 4%. Both the S&P 500 and the Nasdaq ended down for the week, with the Dow squeaking out a gain.

The inflation numbers pretty much solidified another increase of 75 basis points (0.75%) by the Federal Reserve next month, which would bring the federal funds rate to 3.75%. The market has largely priced this rate increase into current levels, and the inflation numbers don't

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appear to warrant a more aggressive move from the Fed. Is a 0.1 percentage point drop in CPI significant? Probably not, but inflation isn't rising and may have peaked. Remember, the rates only began their liftoff in March, so the ripples we are seeing in the economy from the rate increases may be just beginning.

The concern is that the Fed will continue this path and keep looking for older, rearward-looking data for confirmation inflation is moving toward its intended 2% target and overcorrect. Instead, they should keep an ear to the ground and ease up once the downward movement in inflation has gained momentum. Looking back, the Fed's first move should have been bold and decisive; they should have raised a full point and stopped their quantitative easing activities. Instead, they were timid and dragged their feet, raising the federal funds rate by only 25 basis points (0.25%) and keeping their bond buying going.

It's likely inflation won't increase in a meaningful manner from here but will remain rangebound by the price of gas. When gas was $5 per gallon in June, we had 9.1% inflation; when gas prices dropped to $3.80 per gallon in August, we had 8.3% inflation. At the end of September, gas was at $3.75 per gallon and inflation dipped to 8.2%. Do you see a pattern here? High energy costs result in higher costs for producers and consumers, so that's likely where we need to start. (More on this below.)

The government also needs to reevaluate spending money we do not have on things we do not need. Inflation will be with us for some time; will the Fed be eager or the government willing to take bold measures to tame inflation without destroying the economy and tanking the market? Lacking the fortitude to do so will likely make this economic malaise more prolonged and the economic pain to our society more pronounced.

How could we fix our inflation and energy problem in one bold move?

Inflation continues to be persistent and stubborn, and everyone seems to be discussing it – but what is being done to combat it? the Fed has finally started taking it seriously, at least since Chairman Jerome Powell's strong, short speech in Jackson Hole, Wyoming, in August. The media is reporting on it, but all that does is add to frustration because we aren't seeing improvement.

The missing ingredient: Our government. They seem to be talking about inflation the same way the media does, as if it's some sort of unavoidable weather phenomenon, without realizing that along with the Fed they can actually have an impact on inflation in a good and bad way.

The Fed ignored inflationary signals for too long before acting, but it is now doing what it needs to do. What about our federal government? Where the Fed ignored and discounted inflation before acting, excessive spending drove inflation upward, and the push to move us to renewable or green energy has made inflation that much worse.

How do we fix this? The federal government needs to step up by cutting spending and removing crippling regulations so we can unleash our domestic energy production. Instead of demonizing fossil fuels, we may need to encourage their production. Energy costs permeate many aspects of our economy, and so long as they remain elevated, producers will not lower prices because they can't count on fuel costs coming down.

This is not a Big Egg, Big Beef or Big Chicken problem: This is a Big Government problem. A simple announcement from President Joe Biden that we will encourage domestic energy production could crater oil and natural gas speculation, prices on gas and other petroleum-based products will likely decline, and production and transportation costs may drop. This will likely lead to reduced producer costs and, ultimately, lower prices for consumers.

Beyond the shift in policy, the government will have to follow up with actual plans to encourage and promote energy production. The answer isn't as complicated, unavoidable or unsolvable as the media or the administration wants us to think. Unleash American energy production, and this inflation cycle will likely end.

Coming this week

- Third-quarter earnings hit full stride this week. Over 350 companies will be reporting, including Bank of America, Bank of New York Mellon and United Airlines (Monday); Johnson & Johnson, Tesla and Netflix (Tuesday); P&G, American Airlines and Intel (Wednesday); AT&T and American Express (Thursday); and Verizon (Friday). It will be interesting to see if earnings have deteriorated as a result of recent market conditions and the current interest rate environment.
- Fed speakers have given consistent and frequent messaging around interest rates the past two weeks. Any departure from the narrative or signal of dovishness could motivate markets to move higher.
- Thirty-year fixed mortgages are at the 7% mark. Look for mortgage applications, housing starts and permits to dry up in Wednesday's report. Existing home sales, released on Thursday, could also continue to sputter.

Equities:	1 WK	YTD	1 YR	3 YRS	5 YRS
S&P 500	-1.55%	-24.82%	-19.27%	6.50%	7.01%
NASDAQ	-3.83%	-31.93%	-26.92%	9.74%	10.02%
DJIA	1.15%	-18.45%	-15.12%	3.42%	5.32%

Interest Rates:	10/14/2022	10/7/2022
UST 10 YR Government Bond Yield	4.02%	3.89%
Germany 10 YR	2.353%	2.204%
Japan 10 YR	0.241%	0.248%
30 YR Mortgage	7.04%	6.97%
Oil	$85.60/ppb	$92.41/ppb
Regular Gas	$4.03/ppg	$3.91/ppg

All data as of Oct. 14, 2022

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