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Monthly Market Commentary: August 2022

Inflation slowed to "just" an 8.5% annual increase in July, down from 9.1% in June and 8.6% in May. On a month-over-month basis, prices were pretty much flat[1]. Relief at the gas pump was a major driver of the slowdown with gas falling 7.7% and overall energy falling 4.6% in July. However, food and shelter continue to be major sticking points in the inflationary story with food prices increasing 1.1% in the month and shelter increasing 0.4%. Despite the good news, it's not likely a big enough move in the right direction for the Fed to change course, with the market relatively split on whether the Fed will hike 50 or 75 basis points in September[2].

Even though recessionary fears are real, the labor market continues to chug along with over a half million new jobs added to the US economy in July[3], making it the second-best month of job creation this year. The reported numbers more than doubled the expectation of 250K new jobs, based on a Bloomberg survey of economists. Further, the report finally put total employment above pre-pandemic levels. The continued hot labor market may squash some of the recessionary headlines, though it may also make the Fed's job of combatting inflation a bit more difficult as average hourly earnings grew 0.5%, compared to 0.4% in June.

Another piece of good news is consumer sentiment has improved over the last couple of months. In June the University of Michigan survey showed historically low levels of consumer confidence in the economy. The preliminary reading in early August showed sentiment improved to 55.1, versus June's 50.0[4], though it remains below even the worst readings during the 2008 Global Financial Crisis. Improving future expectations drove the gain, offsetting a more pessimistic view of current conditions.

The bottom line: Headline inflation improved with the help of falling energy prices, though inflation remains significantly above anything comfortable for the Fed. The robust gains in the job market may calm near-term recession fears and bode well for the overall economy, but it could make the Fed's job of taming inflation more difficult. The Fed will continue to try to thread the needle and achieve a soft-landing of attempting to tame inflation while cooling the economy, though not hurting it.

Sources:

1. Bureau of Labor Statistics, https://www.bls.gov/news.release/cpi.nr0.htm
2. CME FedWatch Tool, as of 08/12/22, https://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html
3. Bureau of Labor Statistics, https://www.bls.gov/news.release/empsit.nr0.htm
4. University of Michigan