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Market Update: August 2023

Global stocks finished down by almost 3% in August, with declines broadly allocated across market sectors. While the Dow Industrials, S&P 500, and Nasdaq Composite all finished with losses at or around 2%, all three U.S. indexes showed noteworthy improvements from their mid-month lows. Still, global stocks remain up by nearly 15% year-to-date.

So far, 2023 has confounded economists, humbled forecasters, and rewarded investors. Despite a rapid rise in interest rates, the U.S. economy continues to grow. Inflation has fallen – if not to desired levels – and stocks have entered a bull market.

Nicholas Jasinski – Barron's 9/1/23

Without question, the big story is the resilience of the U.S. economy, as it continues to defy the predictions of imminent recession. S&P Global Market Intelligence now estimates the economy is on track to grow at an annualized rate of 4% this quarter, which is considerably faster than the 2.1% pace in the second quarter.

There's a saying that economic expansions don't die of old age: They're murdered by the Federal Reserve. If that's the case, then the U.S. economy is outrunning its would-be assailant this year.

Nick Timiraos – WSJ 9/2/23

U.S. consumers are spending, and pricing pressures are moderating. Household spending increased by a healthy 0.8% in July. At the same time, the Fed's preferred gauge of consumer prices, the personal-consumption expenditures price index, rose 0.2% in July ... the same pace as in June.

Over the past three months through July, inflation is running at a 2.1% annualized rate, which is just shy of the Fed's 2% target. Real after-tax incomes rose 3.8% in July from a year earlier, and they have risen year-over-year each month since January.

Real incomes are what is driving the bus here.

Neil Dutta, Renaissance Macro – WSJ 9/2/23

The Labor Department just reported U.S. employers added 187,000 jobs in August. Over the past three months, 150,000 jobs on average were added ... down from the average gain of 238,000 from March through May. Over the past 12 months, U.S. employers added 3.1 million jobs. With more people seeking work, the unemployment rate reached 3.8% in August, up from 3.5% in July.

A cooling labor market and moderating inflation support the case for an extended pause in Fed rate hikes. CME FedWatch Tool currently is reporting that traders are pricing in a 93% chance the central bank holds rates steady in September.

Home sales fell in July for the fourth time in five months. High mortgage rates, inventory shortages, and near-record high home prices pushed sales down 16.6% from a year earlier. The national median existing-home price now stands at \$406,700 ... up 1.9% in July from a year earlier.

Mortgage rates reached fresh two-decade highs in August. With rates currently above 7%, it's amazing to think that rates were below 3% two years ago. Mortgage rates tend to loosely follow the yield on the 10-year U.S. Treasury note, which ended the month at 4.090%, 0.134 percentage point higher than at the start of August.

The conveyor belt of houses that come on and off the market is just grinding to a halt.

Sam Khater, Freddie Mac – WSJ 8/24/23

In contrast to the U.S., China's economy continues to weaken. August business surveys show declines in exports along with weak consumer spending. Manufacturing activity shrank for the sixth straight month in August, while consumers cut back on spending and increased their savings. Overall, China's households are apparently losing faith in the nation's economic prospects.

What ails China? There are plenty of answers, from demographics to geopolitics to trade. But the key problem might boil down to household finances and, just as important, everyday citizens' deeply shaken confidence that their lives will keep improving following China's Covid-19 emergency.

Nathaniel Taplin – WSJ 8/24/23

As the source of about one-third of global growth, expect China's economic woes to spill over to the rest of the world. China is awash in debt and has productivity problems in state-owned sectors. The real estate bubble has burst, and youth unemployment is at historical highs. Beijing has recently made policy changes to help boost private businesses and relaxed provisions on home buying, but it may be too little too late.

Economists now believe China is entering an era of much slower growth ... Rather than just a period of economic weakness, this could be the dimming of a long era.

Wei/Xie – WSJ 8/20/23

Germany's economy is also struggling. Europe's biggest economy will probably be the world's only major economy to decline this year, according to the International Monetary Fund (IMF). Germany's manufacturing-based economy has been particularly hurt by trade and supply-chain disruptions, as well as surging energy prices.

Two decades ago, Germany revived its moribund economy and became a manufacturing powerhouse of an era of globalization. Times changed. Germany didn't keep up.

Pancevski/Hannon/Boston – WSJ 8/29/23

Overall, the IMF expects growth in global trade to slow to 2% this year ... a decline from 5% last year. As solid as the U.S. economy has been, how long can it diverge from the problems of China and Germany, as well as the problems in Russia and other emerging market economies?

The downturn in world trade raises questions about whether deeper changes are under way, with decades of deepening global economic integration giving way to a new era in which the West and China do more business with their political friends and less with each other.

Walker/Hayashi – WSJ 8/9/23



Over the past few years, investors have had quite a ride. Timing the market movements would have been extremely difficult to say the least. Consider the *ebb and flow* of performance leadership between U.S. and foreign markets, as well as U.S. equity styles.

- With gains of 26% over the past 11 months, global equities have rebounded nicely from the lows reached in 2022. Over that same period, foreign developed markets (+30.1%) outperformed U.S. blue-chip stocks (+27.7%). On the other hand, U.S. stocks have significantly outperformed their foreign counterparts year-to-date.
- So far this year, U.S. growth stocks (+30.97%) have significantly outperformed U.S. values stocks (+5.83%). Value stocks, on the other hand, held up much better during 2022. In fact, value stocks

(+11.72%) have actually outperformed growth stocks (+10.53%) over the past 36 months.

The U.S. economy may be doing well, but Fitch Ratings just downgraded the U.S. government's credit rating. Treasury bonds have an indispensable role in the global economy as a safe-haven security offering risk-free returns. The downgrade, the first by a major ratings firm in over a decade, warned about growing debt and an "erosion of governance" that could cloud the outlook for the \$25 trillion global market for Treasuries.

This sort of problem was described by policy analyst Michele Wucker in her 2016 book "The Gray Rhino." Unlike an out-of-the-blue crisis dubbed a "black swan," a gray rhino is a very probable event with plenty of warnings and evidence that is ignored until it is too late.

Spencer Jakab – WSJ 8/2/23

Compounded interest is considered by many investors to be the eighth wonder of the world, but it can be merciless to debtors. Left unchecked, our escalating federal debt burden would eventually overwhelm the U.S. economy.

The Congressional Budget Office predicts net interest on federal debt will reach \$745 billion in the 2024 fiscal year. That would equate to three quarters of all discretionary spending excluding defense.

Sooner rather than later, we need to address this problem and tackle it ... before it tackles us.

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