



Insights and Observations: Second Quarter 2022

After being in Covid-19 lockdown and receiving three rounds of stimulus payments, U.S. households were able to stash away a substantial amount of extra cash. According to Moody's Analytics, from the beginning of the pandemic through the end of 2021, U.S. households had built up an additional \$2.7 trillion in savings. Moody's estimates that households have tapped about \$114 billion of these extra savings through the first five months of 2022.

Most households have a cash cushion to navigate through the very high inflation. This is allowing consumers to stay in the game.

Mark Zandi, Moody's Analytics – WSJ 7/5/22

JPMorgan Chase estimates that families with the lowest incomes had checking-account balances at the end of March 2022 that were 65% higher than they were in March of 2019. However, last year they were much higher ... 126% higher than 2019 levels. JPMorgan Chief Executive Jamie Dimon believes U.S. consumers still have six to nine months of extra spending power remaining in their bank accounts.



The World Bank's Food Commodity Price Index has climbed over 80% in just the past two years ... reaching a record high this spring. Governments worldwide are concerned about escalating hunger and malnutrition, as well as the potential for social unrest. Amid the rising costs for food, governments are initiating new subsidies and boosting social programs ... even as many countries struggle with budget deficits and pandemic dislocations.

I think there's an awareness of the political dangers this brings. It doesn't necessarily lead to rioting but it does lead to growing disillusionment with the status quo and rising protectionism and nationalism.

Ian Goldin, Oxford University – WSJ 7/5/22



Economic activity in China expanded modestly in June, as Covid-19 restrictions eased. Many economists remain skeptical, however, due to a troubled real-estate market, soft consumer demand, and low business confidence.

Joblessness among the 16 to 24 age group reached a new high of 18.4% in May ... off from 13.8% a year ago. The rising joblessness is a product of Beijing's zero-Covid policy, as well as clampdowns on the property, internet, and educator sectors.

For a country that's always been so fixated on social stability, that is very problematic.

Stephen Roach, Yale University – WSJ 6/16/22



Home prices in China continue to decline, due to developer defaults and weak home-buyer demand. May sales at the 100 largest property developers fell for the 11th consecutive month ... and are off nearly 60% from a year earlier, according to China Real Estate Information Corp (CRIC).

The market is still going downward, and housing demand in most cities is contracting severely as the economy is slowing and the job market doesn't look promising. As property prices are still dropping, home buyers would rather wait and see.

Lin Bo, CRIC – WSJ 6/16/22



Publicly held U.S. Treasury debt has grown from \$17 trillion to \$24 trillion in just over two years. Almost half of this increase ended up on the Federal Reserve's balance sheet, as their Treasury holdings jumped from \$2.5 trillion to \$5.8 trillion over this period.

Over the past three fiscal years, federal interest costs have remained relatively stable at around \$550 billion, as lower interest costs offset higher debt balances. That is no longer the case, however, with interest rates on the rise. For the 12 months ended in May, total federal gross interest reached \$666 billion. By the end of the current fiscal year, interest costs could exceed \$800 billion ... more than national military spending (\$746 billion) and Medicare spending (\$700 billion).

The current debate about inflation and whether the Fed's monetary moves have been too late or too aggressive misses the point. The U.S. has been on an unsustainable fiscal and financial path for a long time. We are beginning to see the inevitable result.

Red Jahncke, Townsend Group Intl LLC – WSJ 6/29/22



In the first quarter, wages and benefits made up 62.9% of U.S. national income, comparable to the 62.7% measured in the fourth quarter of 2019.

The labor share of national output is roughly where it was before the pandemic. In other words, American workers are getting no more of the economic pie than before the pandemic, despite the higher wages employers now pay in response to a labor shortage.

David Harrison – WSJ 5/29/22



The labor share has remained steady because increases mostly went to the small share of people switching jobs, and strong consumer demand enabled firms to increase revenues by raising prices. Businesses also benefited from the \$1 trillion Paycheck Protection Program ... loans that are counted as profits when they are forgiven.

It's not quite right to characterize this as an overheating labor market, but rather one where labor is holding its own.

Julia Coronado, MacroPolicy Perspectives LLC – WSJ 5/29/22



According to Yale researchers, almost 1,000 businesses have pledged to cut back or exit operations in Russia, following the Ukraine invasion. It is estimated that global companies have already incurred nearly \$60 billion in losses from Russian operations ... with more expected going forward as sanctions impact the economy and sales and shutdowns continue.

This round of impairments is not the end of it. As the crisis continues, we could see more financial fallout, including indirect impact from the conflict.

Carla Nunes, Kroll LLC – WSJ 6/10/22



Daily average sales of NFTs (nonfungible tokens) are down over 90% from their September highs. NFTs are digital tokens that act like a certificate of ownership on a blockchain.

In March 2021, Sina Estavi, Chief Executive of Malaysia-based blockchain company Bridge Oracle, purchased an NFT of the first tweet from Twitter co-founder Jack Dorsey for \$2.9 million. Earlier this year, the NFT was put up for sale ... no bids above \$14,000 were received.

A Snoop Dog curated NFT, purchased in early April for about \$32,000, is now up for auction at an asking price of \$25.5 million. The highest current bid ... just over \$200.

Rising interest rates have crushed risky bets across financial markets – and NFTs are among the most speculative.

Paul Vigna – WSJ 5/3/22



About 3.66 million babies were born in the U.S. in 2021. Births were up 1% from 2020, the first annual increase in seven years. After peaking before the Great Recession of 2008, births still remain at historically low levels.

This minor blip up still leaves us on a long-term trajectory towards lower births.

Phillip Levine, Wellesley College – WSJ 5/24/22

The total U.S. fertility rate, the average number of babies a woman would have over her lifetime, was at 1.66 last year. This is up from 1.64 in 2020 ... the lowest recorded level for data going back to the 1930s. Teenage births (ages 15-19) declined by 6% in 2021, and are now down 77% since the most recent peak in 1991.



Total U.S. home equity reached \$27.8 trillion at the end of the first quarter, a record high according to the Federal Reserve.

The increase is another consequence of a red-hot housing market. Double-digit price gains have driven some would-be homebuyers out of the market. At the same time, rising home values are boosting the finances of the Americans who already own them.

Orla McCaffrey – WSJ 6/15/22

Some of us still remember when total home equity fell by 42% between 2005 and 2012. During that period, millions of Americans found themselves with mortgage debts in excess of their home values.

Recent home data is starting to show some *cracks in the foundation*. In fact, the National Association of Realtor's measure of home affordability shows that existing homes are even less affordable than the levels measured in 2007.

Mortgage rates have nearly doubled ... while housing prices continue to climb. People with low mortgage rates are effectively stuck in their homes. While many will still utilize

home-equity loans, they probably won't consider refinancing their mortgage debt anytime soon.

It is difficult to imagine a revival in the housing market unless homes get a lot more affordable. The boom brought on by the pandemic was nice while it lasted. Here comes the bust.

Justin Lahart – WSJ 6/21/22



The IRS had a backlog of 21.3 million unprocessed paper tax returns at the end of May ... up 1.3 million from a year earlier. Its struggles are attributed to pandemic closures, antiquated technology, and new tax-code provisions.

Unfortunately, at this point the backlog is still crushing the IRS, its employees, and most importantly, taxpayers.

Erin Collins, National Taxpayer Advocate – WSJ 6/22/22

It is estimated that the IRS is running about 5 months behind its pre-pandemic pace. For the agency to reduce its backlog and get back to its pre-pandemic pace, they would need to process 500,000 returns a week ... more than double their current pace. In addition, the IRS is now taking 251 days to respond to certain correspondence, up from 74 days before the pandemic ... and just 10% of callers are getting through to IRS employees.



We continue to make our way through this *somewhat artificial* economic backdrop, a framework prompted by the pandemic, and further distorted by extreme levels of government and monetary stimulus. Bulging checking accounts, escalating home values, and rising stock prices helped us weather the storm, but eventually we had to confront the economic fundamentals of supply and demand.

So, as we escape from the pandemic fog, we are now addressing the excesses ... inflation, rising interest rates, labor shortages, and spiraling government debt to name a few. As a result, consumer confidence has taken a big hit, and geopolitical tensions are on the rise.

Investors should expect ongoing volatility as the economy stabilizes. Making decisions within the framework of a financial plan and investment policy has never been more important.

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