The Horror Movie Economy

- Carol Roth

In this informative newsletter, Carol covers how better than expected data isn't the same as good data; why the labor market is confusing to some- but shouldn't be; important data on the consumer and how it might impact the economy in the short- to mid-term; the implications of decreasing productivity; and more!

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The Horror Movie Economy

It's not time to let your guard down and "go back in the house"—there is more economic pain to come

Have you ever seen a horror movie where everyone thinks the chainsaw-wielding killer is dead, and in their naïve relief, they go back in the house, only to find the killer is still alive? That's a very apropos analogy for the economy right now.

On the backside of historic manipulation and dislocation of the economy, including the labor markets, by government and Fed policy, there are a few factors that are making people feel a little too comfortable, thinking that the economy is headed for a swift recovery or "soft landing."

The answer is to look past the headline to the details and the context.

After an unprecedented government-mandated shuttering of around a third of the economy and not letting people go to work, re-opening the economy let some people come back. But, the initial action, plus the policies of giving out stimulus checks and monetary policy that created asset bubbles led a ton of people out of the workforce—millions retiring early and others deciding it wasn't worth going back for a variety of reasons.

Per the July jobs report from the Bureau of Labor Statistics, the US still has fewer people participating in the labor force today than we did in February 2020. The labor force participation rate for July 2022 was 62.1%, compared to 63.4% in February 2020. The employment to population ratio for July 2022 was 60.0%, compared to 61.2% in February 2020.

And, as of June, the US still had around 10.7 million job openings and about 1.8 jobs available for every worker looking-- numbers that have started to come down from their peak of a record 11.86 million openings and almost 2 jobs for every worker looking in prior months.

So, where we are makes sense. As expected, consumers are switching their purchasing from goods to services, consuming heavily in arenas like restaurants and travel, that weren't as accessible during the pandemic. Those businesses have been ramping up hiring to meet this demand, however, the businesses where consumers are turning away are going to slow hiring before laying people off. That transition is happening in certain areas, including technology, but yet to come in others.

In fact, they may still continue to add. According to CNBC, the leisure and hospitality industry is still “1.2 million workers shy of its pre-pandemic level.”

We can see in the breakdown of the Household Survey Data that there was a big bump in part-time jobs and multiple jobs, both consistent with the increase demand in the services sector (as well as the economic realities of individuals and families).

None of this negates that we are in an inflationary recession, even with CPI inflation not growing between June and July. We still have near historic year-over-year inflation. In fact, inflation is likely convincing more people to consider securing a job—or an extra one. The rampant inflation that is eating up consumption and creating a backdrop that is limiting business investment on an inflation-adjusted basis has led to the first and second quarters of the year contracting over last year on a year-over-year basis.

Nor does it mean that we can let our guard down. With the robust jobs report, the Fed, on the back of their stated “dual mandate,” of full employment and stable prices are going to be pressured to continue to raise interest rates, perhaps raising them faster or even having a higher terminal rate (the target rate at which they discontinue raising rates, currently expected to be in the neighborhood of 3.5% to 3.75%).

This means that while the government is messing around raising taxes, ballooning the size of the IRS and increasing their spending, the Fed is trying harder to slow the economy down.

With energy prices remaining elevated but certainly coming down from their peak, and service jobs trying to close the supply and demand gap in labor, things seem better. All of this means that while we could possibly have a third quarter that looks a little better—who knows, we *might* even eke out a small positive growth rate—it is likely the calm before the real storm. It’s the point where in the horror movie you feel relief, but you shouldn’t, and you also shouldn’t go back in the house or the chainsaw storage shed.

The overall economic backdrop is still the same. Consumers continue to dip into savings as they deal with inflation, with the personal saving rate reaching 5.1% in June, the lowest rate since the Great Recession Financial Crisis. Credit card balances are increasing by double digits, at the worst time possible-- when rates are also increasing, creating an extra burden. Reports are that credit card debt has increased 13% over the past year, the largest percentage increase in 20+ years.

Inflation will continue to remain elevated, and there are factors this fall that could push up some of the inflation-generating components again.

Also, not necessarily obvious from the headline jobs numbers is the loss of productivity that has happened from experienced workers retiring. Many industries lost their long-time workers with deep expertise and know-how and they are being replaced with younger workers or trainees with less or no experience at all.

This has effects across industries. For example, productivity issues from the loss of experienced workers in the railroad industry is disrupting supply chains for the farming and agriculture industry.

The message here is that we aren't out of the woods and you need to continue to prepare.

From a portfolio standpoint, if you haven't added to or updated your hedges, like gold, recently, talk to a financial advisor or specialist to review your portfolio and make sure that it is well positioned given your risk profile and objectives for the likely volatile times ahead. Also, consider calling my friends at Goldline for more information.

The horror movie doesn't end until the killer is caught, usually with more slaughter in the meantime. Don't let your portfolio become a victim.