alloya
Corporate Federal Credit Union

Economic Update

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THIS MONTH

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Commentary

Statistical data released during the month of February brought a mixed bag of news. Inflation data surprised to the upside, with both wage growth and the Consumer Price Index (CPI) coming in hotter than expected. Economic growth data in the beginning of the month showed some signs that the economy might be reaccelerating, but consumer spending data released later in the month, which was much weaker than expected, brought concerns that a slowdown might be imminent. The only consistency came from the stock market, which continues its torrid pace higher. The S&P 500 is up almost 7% year-to-date through the end of February.

January data, which is released during February, is always noisy given weather-related impacts and seasonal adjustments. It's always important not to put too much weight on one month's data. When you take a step back, the broad trends are clearly visible. As you can see in the table below, both the pace of job growth and inflation have slowed significantly over the past few years.

Year	Job Growth (mo. avg)	Inflation (CPI YoY % Change)
2021	603,000	7.00%
2022	377,000	6.50%
2023	254,000	3.40%

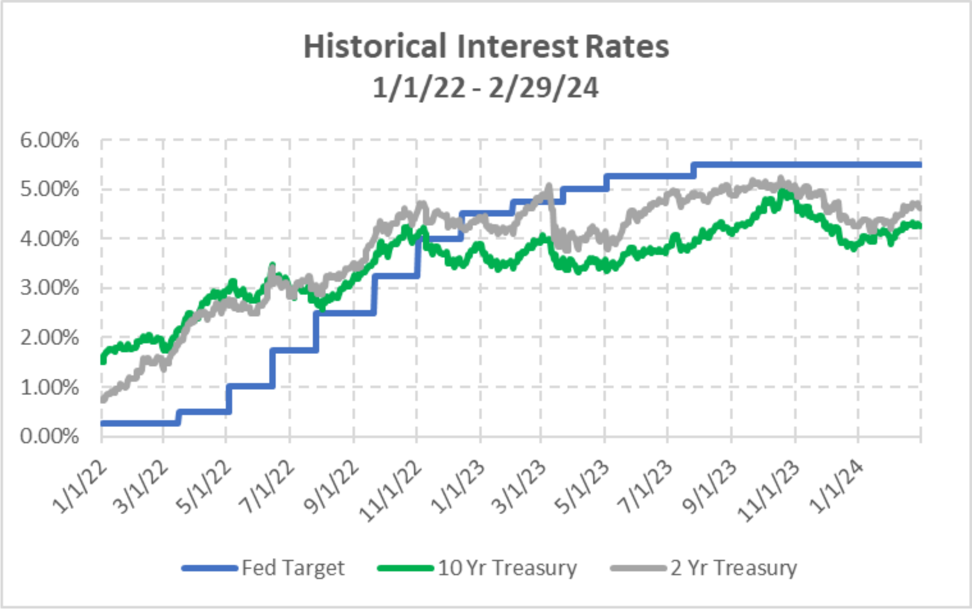
We expect these trends to continue in 2024, as the impact of higher interest rates continues to bite.

Fiscal policy can always be a wildcard when projecting economic growth. Congress once again came up against a funding deadline this weekend, and yet again, the decision was to kick the can down the road rather than pass a funding package. A government shutdown has been averted for now but will be back on the table in just a few short weeks. If Congress can't come to an agreement by April 30, discretionary spending to agencies will be automatically cut by 1% from the 2023 fiscal year levels. That would be a significant negative shock to the economy. Given that it's an election year, we think the risk of this occurring is relatively low, but with a dysfunctional Congress, anything can happen.

We are sticking with our call for a mild recession to hit in the latter half of 2024. We are still working through the pandemic-related impacts but are getting much closer to a normalized economy. We see the risks skewed more towards the downside as the adjustment to higher rates still may reveal some hidden cracks.

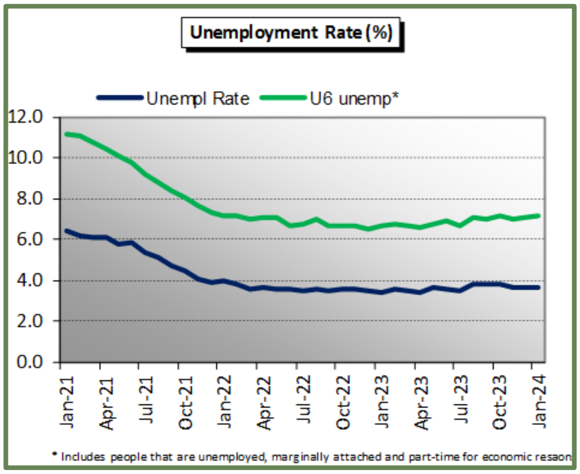
Fixed Income Outlook

Treasury yields moved significantly higher during the month of February. The much stronger-than-expected labor and inflation data caused the market to essentially give up on a rate cut in March. Various Fed speakers throughout the month pushed back against the idea of multiple rate cuts occurring in the near term. The market is now pricing in the first cut to occur in June and 75-100 basis points of cumulative rate cuts this year. That is a far cry from where we stood at the end of 2023. At that time, the market was pricing in an 84% chance of a cut in March and cumulative rate cuts of 150-175 basis points in 2024. Market pricing is now aligned with our expectations and, therefore, we feel that the Treasury market is fairly valued at current levels.



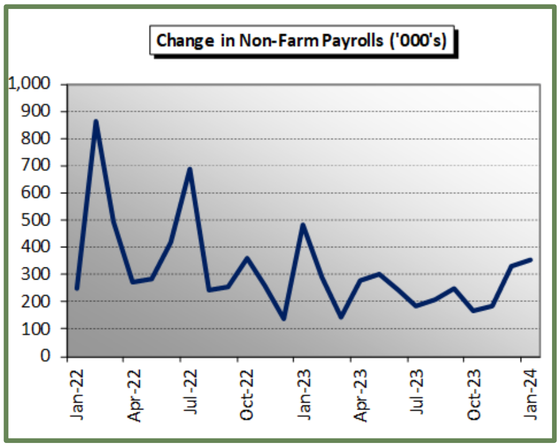
Labor Readings

(Data source: Bloomberg)



Unemployment Rate Continues to Remain Low

The unemployment rate in January held steady at 3.7% for the third consecutive month. The market was expecting an increase to 3.8%. Wage growth was much higher than expected, with a 0.6% month-over-month rise in wages. The market was expecting half that gain. The monthly gain in wages was the highest since March 2022. Some of the gain was likely to due to weather-related absences, so it will be important to see if the February data confirms the higher wage trend.

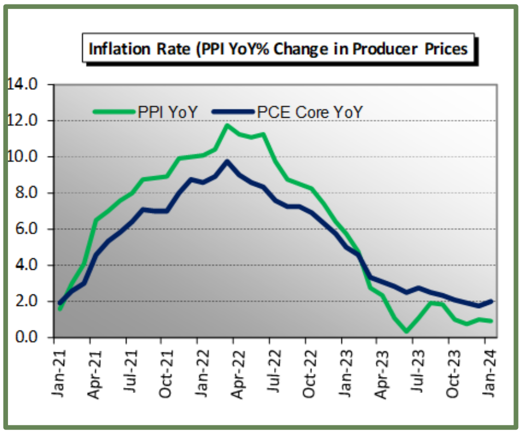


Payroll Growth Much Stronger than Expected

Payroll growth in January topped even the most optimistic projections. Payrolls gained by 353,000 jobs versus an expected gain of 185,000. In addition, the previous two months' job gains were revised upwards by 126,000. It was the highest monthly payroll growth in a year. The three-month average payroll growth is now at its fastest pace since March 2023.

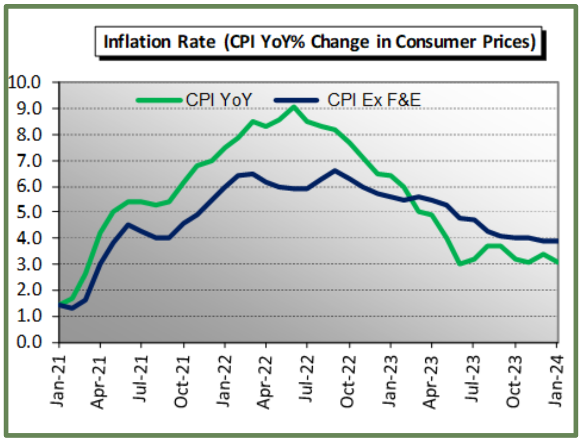
Inflation Readings

(Data source: Bloomberg)



Producer Prices Increase More than Expected

Along with a similar trend in consumer prices, producer prices climbed more than expected in January. Core producer prices increased at the fastest monthly pace in a year. Prices for services continue to be the main driver, as goods prices fell for the fourth consecutive month.

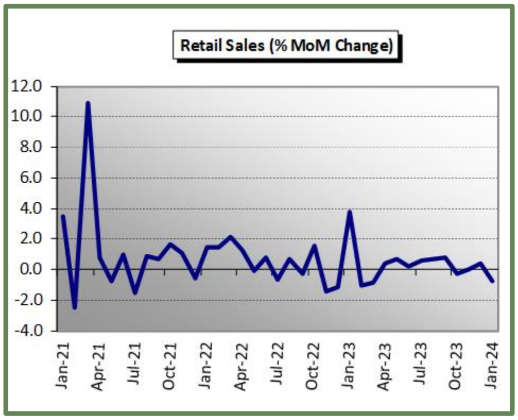


Consumer Inflation Higher than Expected

Both headline and core inflation came in at a hotter pace than the previous month and above consensus expectations. Core goods prices fell by more than expected (the eighth consecutive month of flat or declining prices), but core services inflation rose sharply. This report will increase the angst at the Fed that inflation risk is contained.

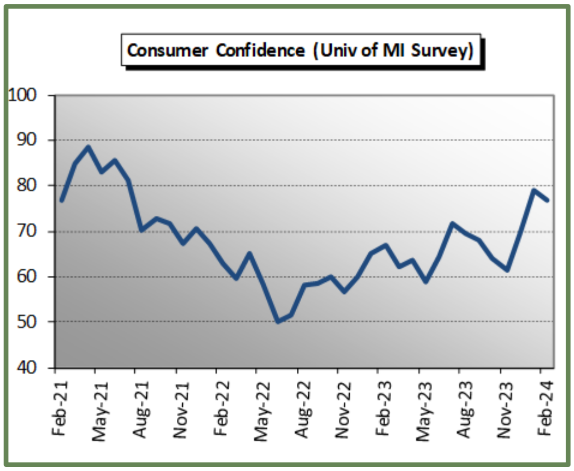
Consumer Readings

(Data source: Bloomberg)



Retail Sales Decrease

Retail sales in January fell more than expected and experienced the largest drop in almost a year. Sales declined by 0.8% on a month-over-month basis versus an expected decline of 0.2%. Nine out of the 13 categories saw declines. Poor winter weather in January likely played a part in the larger-than-expected decline.



Consumer Confidence Experiences Slight Decline

Consumer confidence in February was lower than expected and weaker than the previous reading but remains near the highest level in over two years. Confidence has improved as inflation levels have receded.