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Weekly Relative Value

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Market Strategist

WEEK OF JULY 14, 2025

How Strong Is the U.S. Economy?

"We're the HOTTEST Country Anywhere in the World."
— President Donald J. Trump, July 11, 2025

I keep hearing about what "solid shape" the U.S. economy is in. But based on my analysis, outside of the artificial intelligence (AI) boom, there actually is not that much resilience. And while the stock market has reached new record highs, I must remind everyone that the stock market is NOT the economy!

As for the economy, the consensus believes that the economy is "solid" because 1) Fed Chair Jay Powell has been constantly repeating this narrative and 2) because non-farm payrolls have not declined.

I can't crawl into Jay Powell's head, but frankly, I do not know what he is talking about.

As for non-farm payrolls, I have stressed repeatedly that absent the constant distortion from the birth-death model, the payroll gains have been quite weak. In fact, according to Quarterly Census of Employment and Wages data, the job numbers will likely be REVISED DOWN by nearly 800,000 for the nine months ending December 2024. This means non-farm payrolls were OVERSTATED by ~88,888 jobs each month during this period. Alas, nobody wants to believe it.

Not only that, but private-sector employment growth in June was just about the weakest it has been in quite some time. Ditto for the ADP data, which showed a -47,000 plunge in small-business payrolls in June after a -13,000 contraction in May in the steepest two-month decline since the spring of 2020!

THIS WEEK

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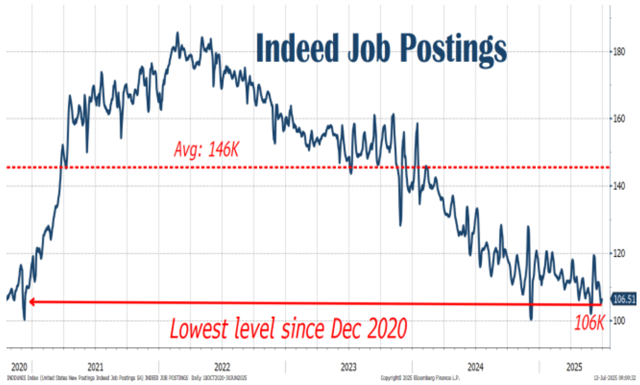
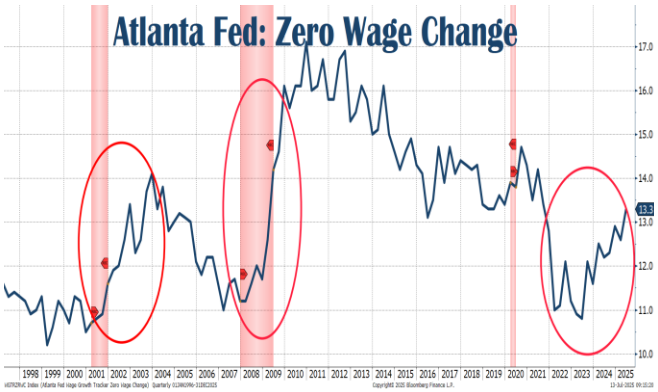
In addition, job postings are PLUNGING. Job postings on Indeed have declined for 3.5 years and are now near the pre-2020 crisis levels.



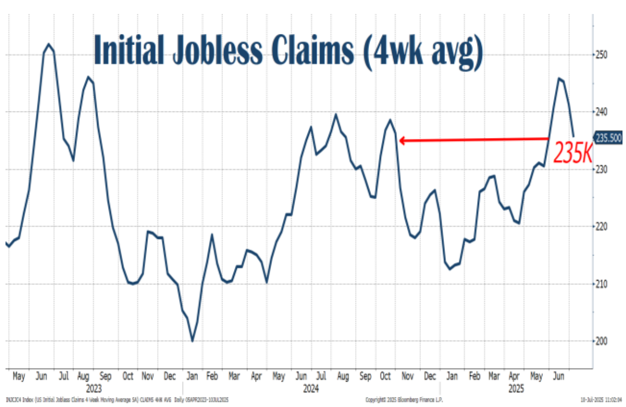
Also, if the labor markets were truly healthy, why is it that 13.3% of Americans are not getting ANY pay raises, the highest share since 2021? This is in line with the FINANCIAL CRISIS levels and above the 2001 recession. Adjusted for inflation, these wages are effectively declining.



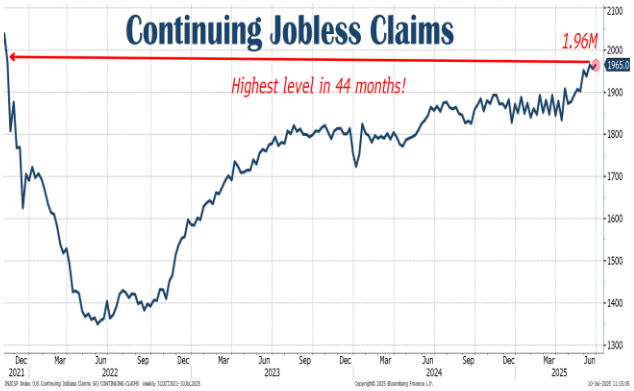
SCLEROSIS SETS IN

Meanwhile, the no-firing, no-hiring labor market continues. In other words, sclerotic. Jekyll and Hyde.

As shown below, the four-week moving average of initial jobless claims at 235,000 show that businesses are far from starting a layoff cycle.



Even still, the growing mountain of continuing claims has reached a fresh 44-month high of 1.965 million and shows that the swelling ranks of the unemployed are not finding a job.



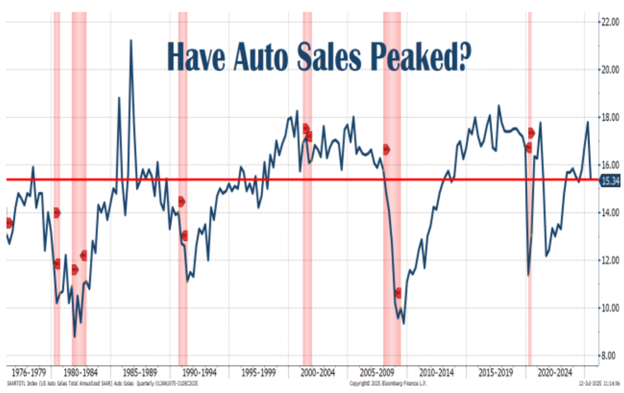
The problem with a complete lack of hiring activity is that if we ever do see layoffs commence, non-farm payrolls will begin to contract, and the recession that investors attach 0% odds to will end up becoming a shocking reality.

Bottom line: Can these signs of a weakening labor market simply be ignored because of the illusion provided by the very flawed Bureau of Labor Statistics (BLS) birth-death model?

HOW ABOUT THE CONSUMER?

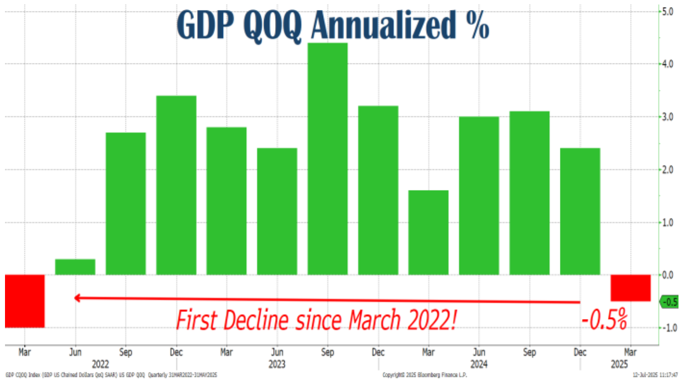
The other consensus view is that the consumer is healthy, yet Amazon Prime Day summer sales were reportedly off -41% (!) compared to last year on day one. Amazon has now extended the promotion from two to four days to allow for more "treasure hunting." Sure thing.

Meanwhile, auto sales have declined for three consecutive months while Johnson Redbook showed a -0.4% dip in June same-store activity. Not a good look for the consumer. It is a distinct possibility that June retail sales will decline for the third time in as many months. This is a "three strikes and you're out" backdrop that hasn't happened in a decade.



Yet, again, the perception is that the U.S. consumer and economy are strong. This perception will likely not change until we see a string of declines in headline non-farm payrolls (along with a higher U-3 unemployment rate, the only statistic that seemingly matters for this Federal Reserve).

But this is what you should believe. The first quarter gross domestic product (GDP) showed a -0.5% decline. And as of May, year-over-year real GDP growth has declined from +3% at this time in 2024 to over +1% currently.



Bottom line: The U.S. consumer represents nearly 70% of GDP. The American consumer is in more pain than commonly appreciated.

THE BIG BEAUTIFUL BILL IS NOT STIMULATIVE

The Big Beautiful Bill (BBB) is now enacted.

Despite the hoopla, the BBB is not very stimulative. Almost all the bill's price tag comes from extending the 2017 Tax Cuts and Jobs Act, slated to expire on December 31. So, this fiscal bill is not expansionary from an economic perspective, but it sure is from a budgetary perspective.

Those extensions are not going to change the behavior of individuals and firms the way the tax cuts did when they were first implemented, or the way President Joe Biden's 2021 stimulus did.

Here are the other key provisions in the Big Beautiful Bill:

- A new tax deduction for senior citizens (This is meant to fulfill President Trump's promise to eliminate taxes on Social Security income.)
- No tax on tips (with a phase-out based on income)
- No tax on overtime
- No tax on most auto loan interest
- A higher deduction for the State and Local Taxes (SALT) deduction
- Improved corporate expensing for manufacturing structures
- An increase in the charitable deduction

There will be some stimulus from the provisions above, but we cannot really rely on people who earn tips or who are age 65 and up to be the drivers of the economy.

Bottom line: The growth implications from the BBB for 2025 are minute. However, the BBB puts more pressure on interest rates because of the unsustainable borrowing dynamics. As I highlighted last week, I am especially concerned about the massive increase in debt at a time of demographic transition.

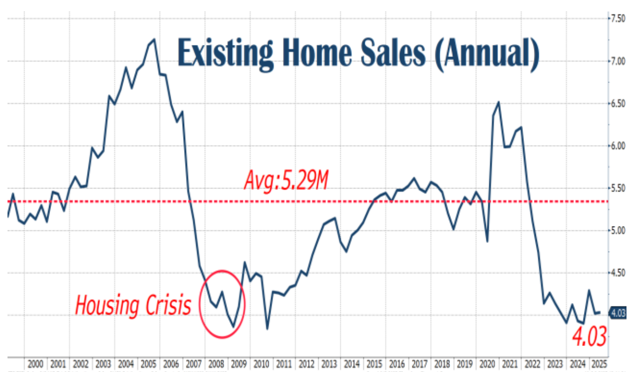
THE ECONOMY'S QUINTESSENTIAL INDICATOR

While AI centers may be booming, you can't live in them, and you do need a roof to sleep under.

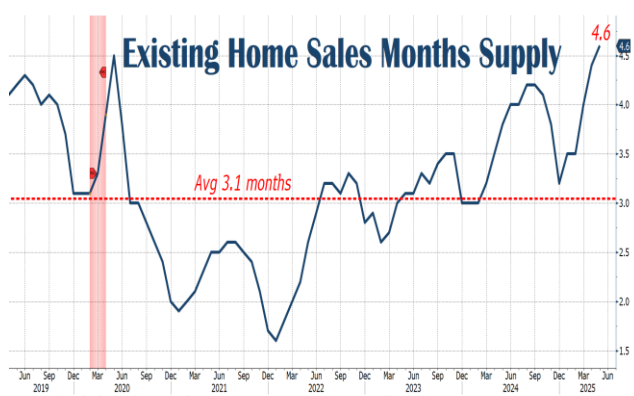
The housing market has always been, and remains, the quintessential leading indicator of overall economic activity. This is because of the far-reaching multiplier impacts (employment, ancillary spending on furniture, appliances, remodeling, etc.) on the "real" side of the economy. Overall, the housing multiplier effect is typically estimated to be 1.5 to 2.5X, meaning that every $1 spent on residential construction ultimately adds $1.50 to $2.50 to overall GDP, making it a powerful driver of economic growth and employment. And as we all know, the housing market remains stuck in the basement. Further, housing is the most important asset on the household balance sheet and in the broad banking sector.

The charts below speak for themselves:

Existing home sales are near the all-time lows experienced during the housing crisis amid the Great Financial Crisis. What more needs to be said?

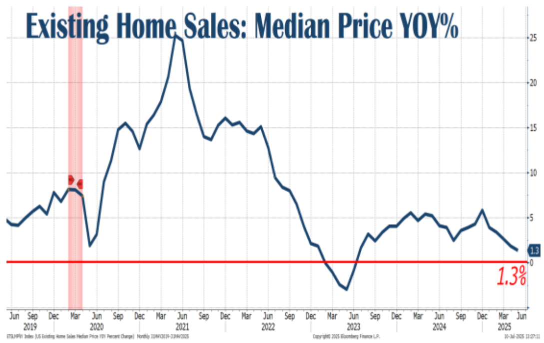


According to Redfin, it now takes at least 45 days for homes on the markets to sell. The last time it took so long to sell a house was during the pandemic scare in 2020. Moreover, the level of unsold inventory has expanded to five-year highs and is up +18% from year-ago levels. The month's supply of homes at the current sales rate is 4.6 months, which is higher than levels seen in 2020.

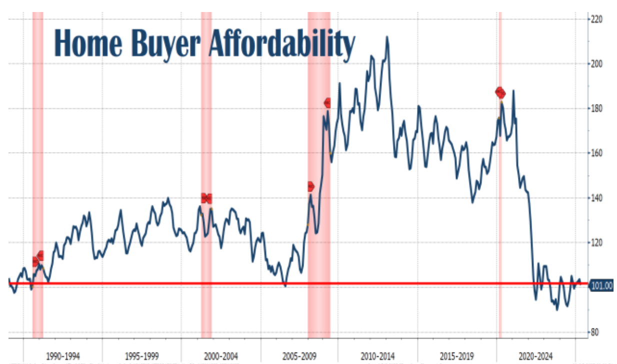


This huge gap between the supply and demand is now putting downward pressure on residential real estate prices. The year-over-year pace of housing inflation is closing in on zero, but the latest Case-Shiller data shows sequential deflationary readings in recent months. In fact, adjusting for size, home price inflation has already hit 0% year over year for the first time since May 2020.

Also, according to Redfin, only 30% of homes are now being sold above the listing price as the backdrop shifts from a sellers' to a buyers' market and, at 21%, the share of active listings being forced to lower prices is tied for the highest level on record.



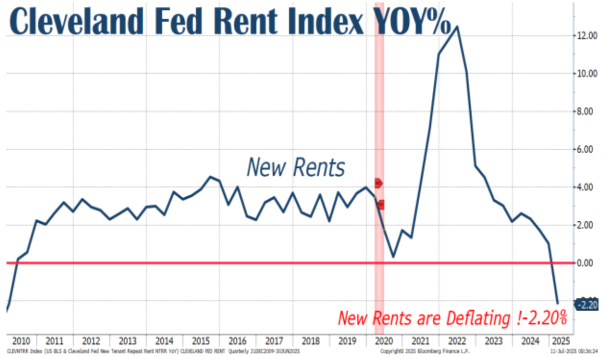
Despite the leveling-off of home prices, affordability is still out of reach for most prospective homebuyers. If interest rates don't come down, then mean-reverting the extreme homeowner affordability ratio will result in a decline in national home prices of between -20% and -30%. This is a key reason I am not drinking the Kool-Aid on the "solid" consensus economic narrative and why I remain steadfastly bullish on high-quality long-duration bonds.



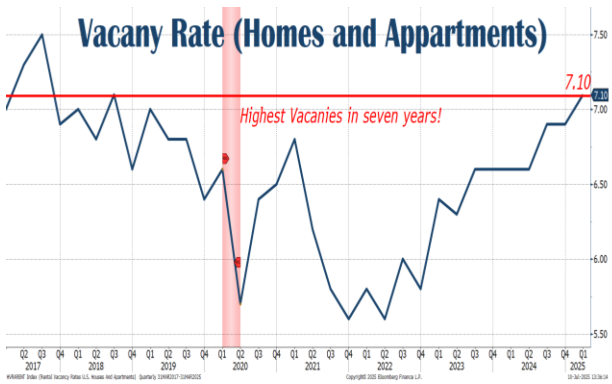
At the same time, the oversupplied apartment market continues to exert downside deflation pressure on rental rates, and this has only recently begun to percolate in the Consumer Price Index (CPI) data.

In fact, we are already seeing rental deflation. The Cleveland Fed's New Tenant Rent Index provides an early indication of future rent prices. According to the latest available data point, new rents have declined by -2.2% from levels a year ago. Given the excess supply in the housing market and the rental vacancy rate at its highest since 2017, this comes as no surprise.

Shelter inflation represents a little over a third of the total CPI basket. Furthermore, shelter inflation rates can be predicted because what is happening in the new rental market today will typically show up in prices a year later.



In other words, the impact of housing sector deflation is going to dominate the inflation impact from tariffs by a sizable margin when one considers that, at a 35% share of the CPI, shelter is nearly twice as important as the core goods items that will be affected by the tariffs. In other words, while imported goods will pressure prices higher, disinflation in the housing and rental market will pressure inflation lower. You can't forecast inflation using just one input.



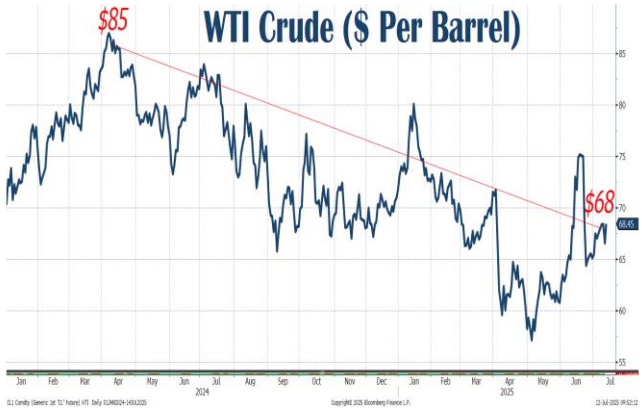
This trend will be further exacerbated by the Trump Administration's deportation policy, pushing the economy toward further disinflation. The initial quota set by U.S. Immigration and Customs Enforcement (ICE) was to deport one million people every year. Thus far, that has proven to be an ambitious but out-of-reach task, considering that only 100,000 people have been deported from January 20 to the first week of June.

If the Trump Administration continues with its goal of one million deportations each year, this could be a persistent drag on rents. While we won't see the impact of the immigration policy on rent prices for a few quarters due to the lagging nature of the shelter component in the CPI, it will be reflected in changes in the prices of new rents.

Bottom line: I see a significant pullback in home prices and rental rates ahead. This will pressure inflation towards the Fed's target of 2% even if there is a significant tariff price shock from tariffs. As such, investors should temper their inflation worries in the face of this disinflationary development. Aside from the external price shock caused by the tariffs, the monetary policy would be considered far too tight today. Once the tariff-related price pressures dissipate, the Fed will be forced to adjust its policy and deliver faster and larger cuts toward the neutral rate, at the very least.

ENERGY PRICES ARE DISINFLATIONARY

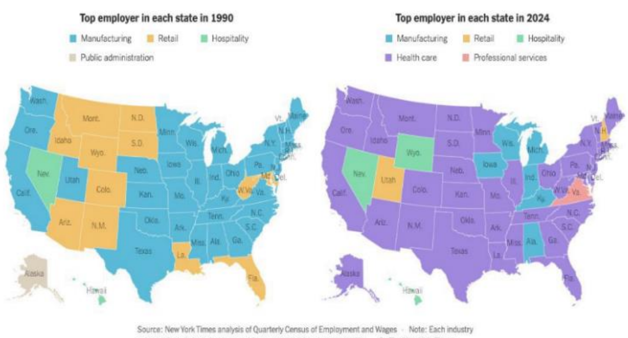
In addition to the prospective disinflation coming from housing, oil prices have declined by ~20% since March 2024. And it looks that the Organization of the Petroleum Exporting Countries (OPEC+) intends to boost oil production by +548,000 barrels per day next month. (Consensus expectations were +411,000 barrels per day.) At the same time, world demand estimates are being cut, leaving the crude market at risk of moving into a surplus later this year. The Saudis are doing the "drill baby, drill" move on President Trump's behalf. This obviously is good for the consumer, but not exactly good news for energy stocks.



Bottom line: The decline in energy prices should be another countervailing force to higher tariff prices.

GRAPH OF THE WEEK

I came across the following graph, which shows the top employer in each state in 1990 as compared to the top employer in 2025. Indeed, the U.S. has gone from a manufacturing and retailing economy in 1990 to a health care clinic today.



TARIFF LETTERS

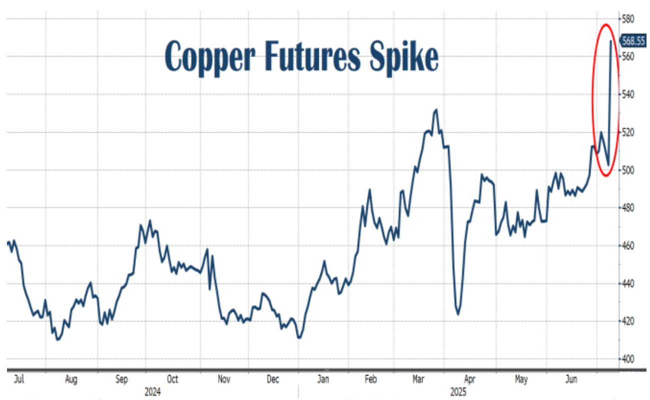
"We are past the peak tariff uncertainty." — Venu Krishna, Head of U.S. Equity Strategy, Barclays

Talk about famous last words.

Now that the BBB has passed, tariffs are back on the menu. Last week, President Trump sent "letters" to Mexico and the European Union that they will face a blanket 30% tariff on August 1, barring a trade deal coming to the fore. Of course, this follows the 35% levy to be imposed on Canada for goods not covered by the United States-Mexico-Canada Agreement (which is 40% of the country's export pie). Trump says he'll raise his tariff even higher if it does, but how much more damage can he do? And remember, U.S. consumers will eventually pay Trump's tariffs.

Trump also placed tariffs ranging from 25% to 40% on several countries, including big leaguers like Japan and South Korea. Numerous other countries could be affected, with the deadlines set on August 1 and not July 9. More threats, more reprieves?

The biggest tape bomb was the announcement out of the White House that the U.S. will impose a 50% tariff on copper imports, triggering a record +17% spike in U.S. futures. Trump's 50% tariff on Brazil for the sin of actually putting a would-be dictator on trial was shocking.



As nuts as Trump's tariffs are, this may be the most nuts of all. The reality is that almost 40% of U.S. copper demand is met with imports. Copper is an input into many products — think electric wires, plumbing and yes, batteries. Tariffs will not result in more copper being produced here — it will just raise prices.

So, assuming these tariffs stay in place (a BIG assumption these days), this is going to cause major ripple effects across U.S. industries (think super-sized margin squeeze) when you consider all the applications: construction, electronics, industrial machinery and transportation equipment. Great news for Freeport-McMoRan, but not for everyone else.

Also, think about what the 50% tariff against Brazil will do to the price of coffee, which is already up +32% from levels a year ago.

We'll presumably hear many attempts to explain the strategy behind all of this, but there clearly isn't a strategy.

The table below shows tariff rates as of April 2 (Liberation Day) as compared to the latest tariff rates announced last week that will be imposed beginning August 1.

Effectively, we're doing Liberation Day all over again!

Country	April 2 Tariff Rate	August 1* Tariff Rate
Brazil	10%	50%
Myanmar	44%	40%
Laos	48%	40%
Thailand	36%	36%
Cambodia	49%	36%
Canada	25%	35%
Serbia	37%	35%
Indonesia	32%	32%
Bosnia and Herzegovina	35%	30%
Algeria	30%	30%
Iraq	39%	30%
Libya	31%	30%
Sri Lanka	44%	30%
South Africa	30%	30%
Moldova	31%	25%
Brunei	24%	25%
Tunisia	28%	25%
Kazakhstan	27%	25%
Malaysia	24%	25%
Japan	24%	25%
South Korea	25%	25%
Vietnam	46%	20%
Philippines	17%	20%

Source: Charles Schwab, Bloomberg. *August 1 rates announced, not yet implemented. Tariff rates don't cover all goods in some cases.

Bottom line: Trump is hell-bent on blowing up global trade. And he wants everything made in the United States, oblivious to costs of doing so. The U.S. would become the world's highest cost producer, exports would crash and inflation would soar.

Moreover, Trump blames unfair trade for our deficits. But America relies on those deficits to compensate for the consequences of excessive debt and consumption and inadequate savings and investment.

Investors have been inclined to assume that Trump will retreat as he has done so often. Trump suggested that equity strength was a sign financial markets like tariffs. Thus, the paradox — markets are strong on the assumption Trump will retreat; markets being strong reduces the incentive for Trump to retreat.

So, what if, Trump does NOT chicken out? After all, he reportedly is furious over this TACO label that was first created back on May 2.

IS FED INDEPENDENCE ON THE LINE?

"Our Fed Rate is AT LEAST three Points too high." – President Donald Trump

Having just signed the BBB, Trump hasn't wasted even a New York minute pivoting to a demand that the Fed now crank up its printing presses red hot to finance the new flood of red ink.

I am referring to Trump's missive last Wednesday instructing the Fed to slash rates by a full **300 basis points***.* The Fed Funds rate is 4.25%–4.5%. Trump said it should be 1.25%–1.5%.

"I'm encouraged by reports that Jerome Powell is considering resigning. I think this will be the right decision for America, and the economy will boom."— William J. Pulte, Chairman of the Board, Fannie Mae

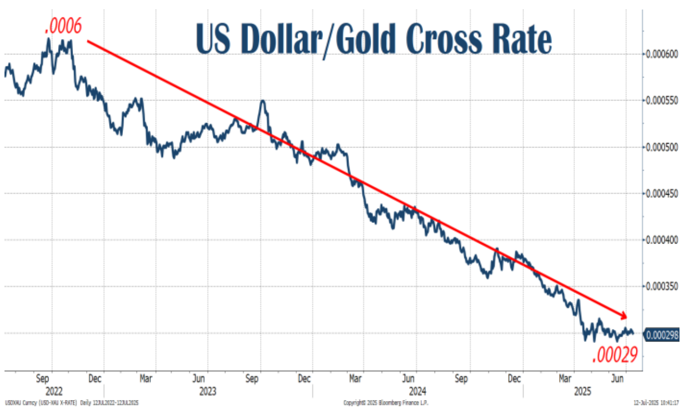
The only way that interest rates could be chopped 300 basis points, of course, is if the Fed resumes buying Treasury paper hand-over-fist with fiat dollars snatched from thin air, thereby driving bond prices skyward and yields sharply lower.

The pressure is coming from various areas of the administration for Fed Chairman Powell to step down. This pressure is not just coming from the president but from all corners of the White House, with the cost overruns on the renovations at the Federal Reserve building now emerging as a fresh rationale to have Mr. Powell replaced.

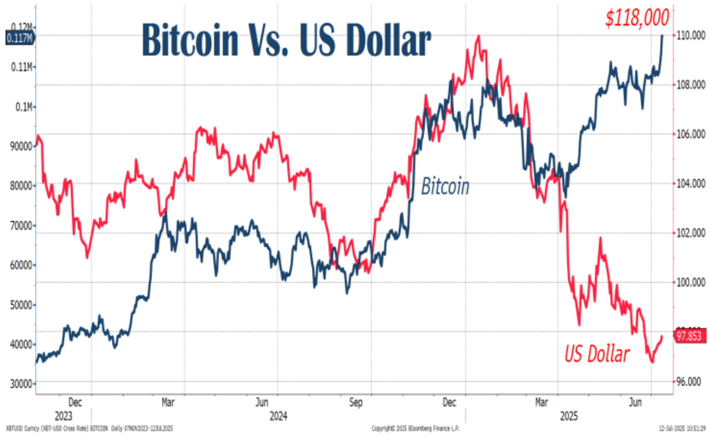
He is also being blamed (by Larry Kudlow, no less) for overseeing a Fed balance sheet that is more than $1 trillion "under water" on its bond holdings, which is a truly blasphemous accusation because the central bank is not some hedge fund having to mark-to-market its portfolio. But the "Big Lie" technique is working, and word is out that Jay Powell is feeling "fatigued." Rumors are now flying that Powell may resign, so his replacement can slash rates to the level Trump wants.

Trump's chief economist, Kevin Hassett, a "yes man" if there ever was one, is widely viewed now as the successor.

If this happened, this would also put the nail in the dollar's coffin and send gold soaring to ever higher levels. Just a reminder that U.S. dollars have lost 50% of their purchasing power versus gold in the past 2.5 years!



In fact, not only has gold soared on concerns of a "puppet" Fed President, Bitcoin reached a new record high of $118,000. Since November 2023, Bitcoin has soared 173% while the U.S. dollar has collapsed by 13%! Amazingly, year-to-date bitcoin has rallied 25% with most now forecasting an additional 25% gain for year end. What does that say about the U.S. dollar?



Bottom line: While I have been critical of Jay Powell, I also believe that Fed independence is key to maintaining faith in U.S. economy and assets; thus, any aggressive action to put a "puppet" in as Fed Chair could do significant and long-lasting damage to the credibility of monetary policy and the stability of the U.S. economy.

MARKET OUTLOOK AND PORTFOLIO STRATEGY

"No time for significant shifts in monetary policy." — Raphael Bostic, Atlanta Fed President

The latest Federal Open Market Committee (FOMC) minutes suggest it will take a lot to get Jay Powell to cut rates. The FOMC minutes from the June 18 meeting showed there was no consensus. That said, the majority is concerned about the tariff effect on inflation becoming more persistent.

"In discussing their outlooks for inflation, participants noted that increased tariffs were likely to put upward pressure on prices. There was considerable uncertainty, however, about the timing, size and duration of these effects."

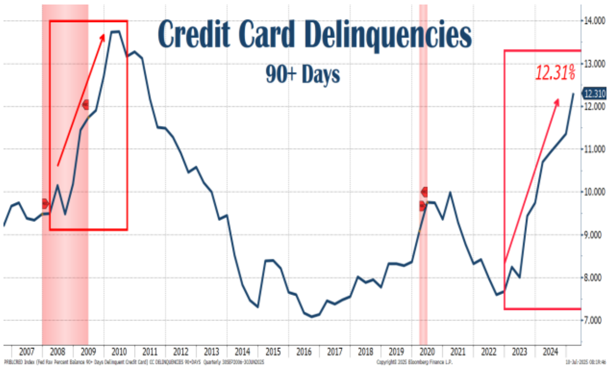
While I strongly disagree with Trump's ongoing harassment of Jay Powell, I believe he is right in this criticism that the Fed should be lowering rates. The Fed is way too late and way too consumed with tariff fear. They are looking backward, not forward.

And as discussed above, while tariffs may prove to be inflationary, there are other disinflationary forces that may neutralize the impact of tariffs on inflation.

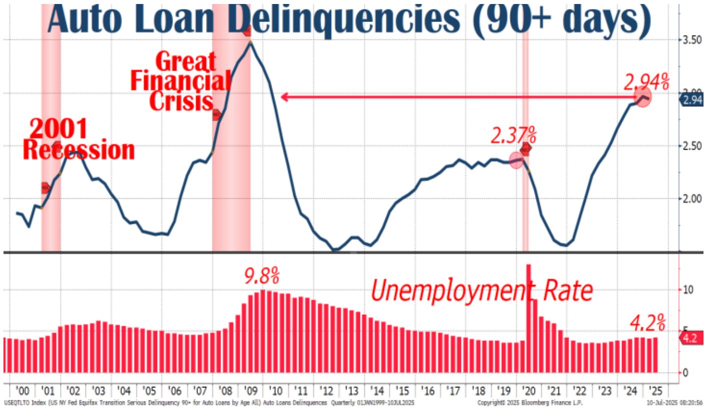
Truflation is an independent research firm that provides real time inflation data. According to their methodology, inflation in the U.S. is already below the Fed's target of 2%.

Note: This week we will get the latest BLS updates on CPI, Producer Price Index and import/export prices for June, which could prove to be a little on the hot side.

In addition, the marginal household is choking on a ton of 20% interest rate debt and clearly having trouble servicing it, as the share of credit card debt in delinquency has risen to levels seen during the 2008-09 financial crisis.



Ditto for auto credit. Mortgage defaults have begun to rise from years of residing at depressed levels, and even corporate bank loan delinquencies have recently jumped to near five-year pandemic-era highs.



In the meantime, VOLATILTY will remain high, but any selloffs provide an attractive entry point for credit unions sitting on excess cash. As always, the most prudent approach to managing excess cash is to structure and maintain a risk-appropriate ladder strategy.

MORE INFORMATION

For more information about credit union investment strategy, portfolio allocation and security selection, please contact the author at **tom.slefinger@alloyacorp.org** or (630) 276-2753.

As Alloya's Market Strategist, **Tom Slefinger** leverages nearly 40 years of investment strategy expertise to deliver insightful commentary on the economy and market events to optimize balance sheet performance at the credit union level. With thousands of subscribers, Tom's daily and weekly publications are widely read amongst credit union executives.

Prior to becoming the corporate's Market Strategist, Tom served as the Senior Vice President of Institutional Fixed Income Sales at Alloya Investment Services, a division of Alloya Solutions, LLC. In this role, Tom developed and managed operations associated with institutional fixed income sales in addition to developing investment portfolio strategies, identifying appropriate sectors and securities, and optimizing portfolio performance at the credit union level.

Tom holds a B.S. in business administration from the University of Maine. In addition, he holds a Series 7 and 63 through ISI.

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