alloya
Corporate Federal Credit Union

Economic Update

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THIS MONTH

Commentary

Equity and bond markets closed in June approximately where they ended the previous month. For the year, equity prices have increased by 10%, and Treasury yields have moved 50 basis points higher in the belly of the curve, and less so on the shorter and longer ends. Markets are trying to sort out several factors. The potential end to the war with Iran has brought gasoline prices lower by about 15% this month, but they remain $1 per gallon higher than where they stood before the conflict. The rate of inflation has continued to increase, and the labor market is showing renewed signs of strength. Amidst all of this, there is a new chair at the Fed that is looking to put his stamp on how the Fed should operate.

Fed Chairman Kevin Warsh didn’t waste any time to show his disdain for forward guidance at his first meeting as chair earlier this month. He refused to submit his own economic projection that has been standard for the other Fed participants on a quarterly basis for the last several years. In addition, the Fed’s official post-meeting statement was trimmed down almost by 50%, removing all discussion related to forward guidance and/or projections. He stated that he has established five task forces to review communications, balance sheet, data quality, productivity and inflation frameworks. The early read from his relatively short press conference is that he is more hawkish than expected (and certainly more than President Trump wanted) and seems most concerned about price stability at the moment.

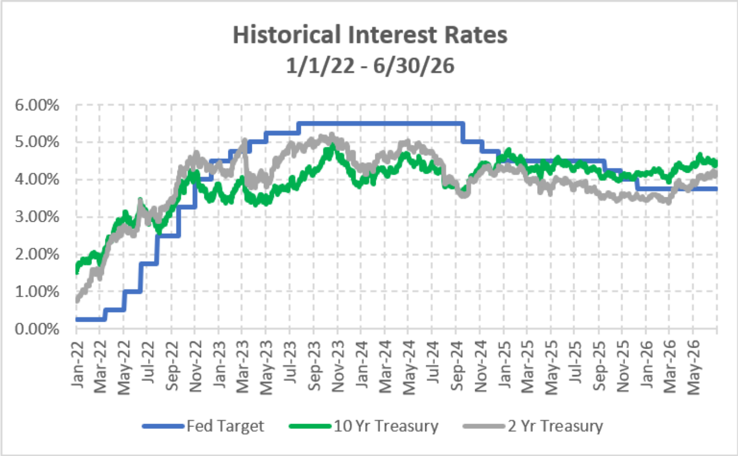
As for the other members of the Fed, they have shifted more hawkish. Half of the 18 participants have projected at least one rate hike this year and only one has a rate cut. Inflation projections were marked up substantially for 2026 and 2027. Their median projection has the fed funds rate ending the year at 3.90% versus at 3.65%, where their projection stood to begin the year.

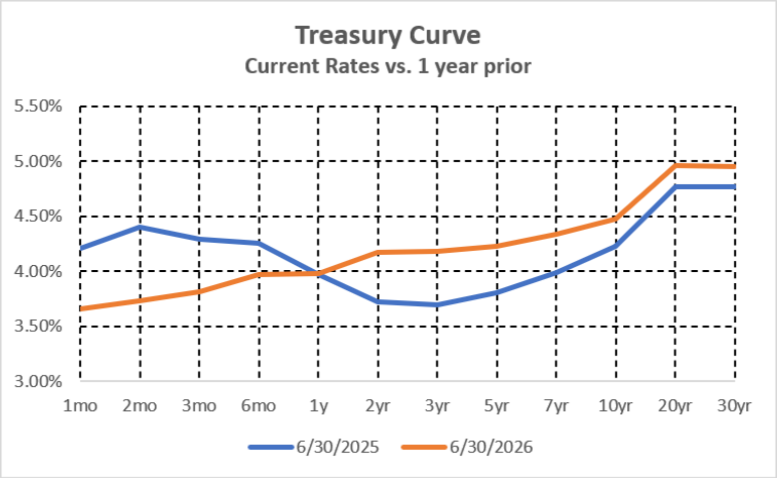
Turning to the labor market, payrolls have exceeded estimates for three consecutive months. We remain somewhat skeptical that job growth will continue to expand but can’t ignore that we have reached the highest three-month average payroll growth in over two years. In addition, payroll growth has broadened out to include more sectors.

Our base case view is that the labor market will modestly weaken, but higher inflation will linger. Consumer spending in Q2 should be relatively strong given the boost from the World Cup and Prime Day. We look for weakening to occur in the second half of 2026 as the tax refund impact fades and the weight on the consumer from higher prices becomes heavier.

Fixed Income Outlook

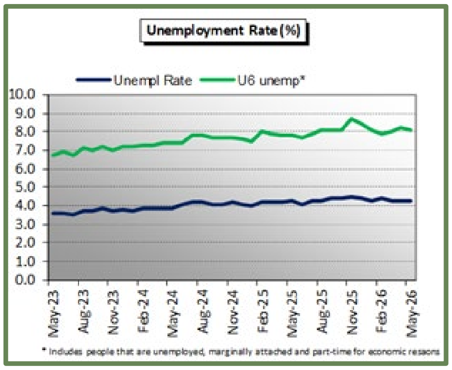
Treasury rates at the short-end of the curve moved marginally higher during June as the Fed shifted more hawkish. Market pricing has the Fed increasing rates by 25 basis points by September and 50% chance of an additional hike towards the end of this year. We believe that the Fed will leave rates unchanged for the remainder of 2026.





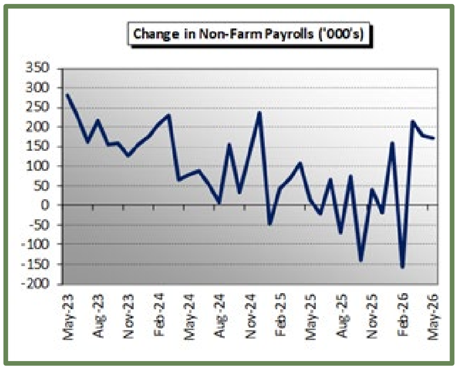
Labor Readings

(Data source: Bloomberg)



Unemployment Rate Unchanged

The unemployment rate remained at 4.3% for the third consecutive month in May. The market was expecting the rate to remain unchanged. The details of the report showed some moderate strength, with both the labor force and the number of employed growing.

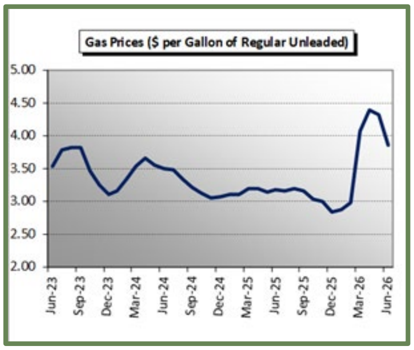


Payroll Growth Strong Again

Payrolls beat estimates for the third consecutive month in May. The number of jobs increased by 172,000 versus an expected gain of 88,000. In addition, the previous two months were revised higher. Three-month average payroll growth is at its highest level in over two years.

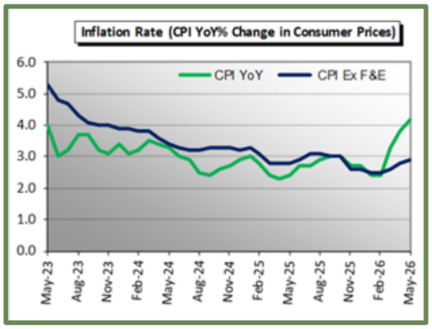
Inflation Readings

(Data source: Bloomberg)



Gas Prices Starting to Recede

Gas prices have declined meaningfully since the middle of May. Prices are down 16% from their highest level but still are almost $1 per gallon more than where they stood before the war with Iran. The recent price decrease is due to the ceasefire as well as reduced demand from China.

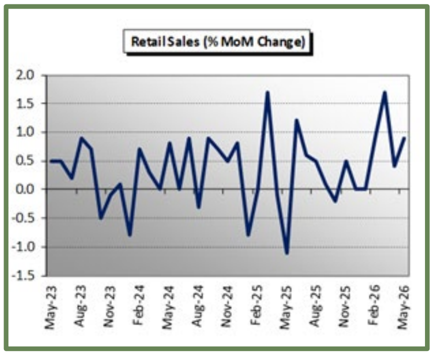


Consumer Inflation Soars Higher

Consumer inflation in May increased to the highest level in more than three years. More than half of the advance was due to higher energy costs. On the positive side, core inflation gains were slightly lower than expected.

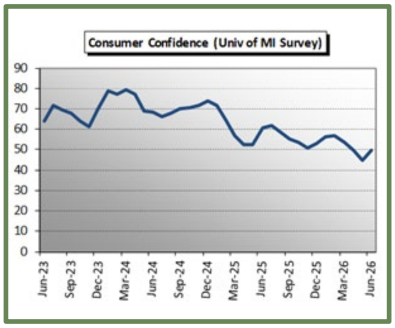
Consumer Readings

(Data source: Bloomberg)



Consumer Spending Remains Strong

Consumer spending in May increased for the fourth consecutive month and beat estimates. Spending increased by .9% on a month-over-month basis, versus an expected gain of .6%. The advance was broad-based, with 11 of the 13 categories increasing.



Consumer Confidence Still Subdued

Consumer confidence rose in June but remains near all-time lows. Sentiment rose to 49.5 in June from 44.8 the previous month. Inflation expectations have dropped after gasoline prices have fallen over the last few weeks. Cost of living increases remain a significant concern.