Alloya Corporate Federal Credit Union

Economic Update

Andrew Kohl
Chief Investment Officer
Alloya Corporate FCU

AUGUST 2026

THIS MONTH

Commentary

After pausing in recent months, equity markets resumed their upward trajectory. The S&P 500 has gained nearly 3% so far in August, supported by exceptionally strong second-quarter earnings. Profit margins are surging due to the heavier exposure to technology companies in the index and technology driven productivity gains. Bond market prices have moved in the opposite direction, with prices declining and the 30-year Treasury bond reaching its highest yield since 2007. Continued inflation concerns and the national debt now exceeding $40 trillion are helping to depress prices.

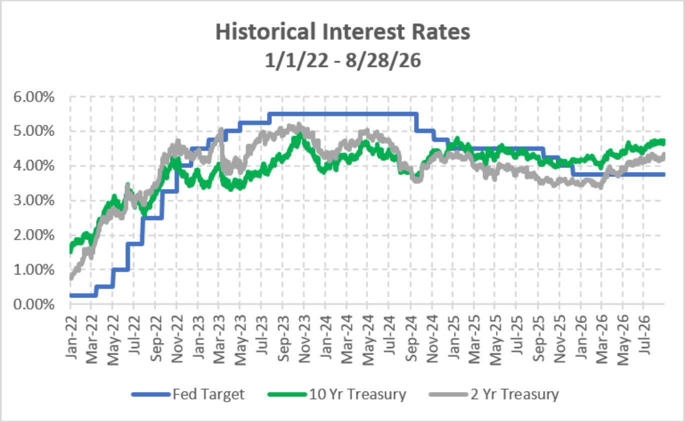
Given this backdrop, the still relatively new Fed chairman, Kevin Warsh, delivered a more hawkish than expected speech at the Fed’s annual Jackson Hole conference this week. He cleared the air on several points from his post-Federal Open Market Committee press conference in July, where he seemed to indicate an unwillingness to raise rates and possible changes to how the Fed would measure inflation. He stated firmly that the Fed’s inflation target is 2.00%, as measured by the Personal Consumption Expenditures (PCE) Price Index, the same index that the Fed has targeted for many years. He also reinforced that the overnight rate will be the primary tool utilized for the Fed to achieve its dual mandate rather than allowing “market forces” to do the Fed’s work. His most hawkish statement was, “On balance, I would be hard pressed to describe broad financial conditions as restrictive.” This is in contrast to Chairman Powell, who seemed happier to take a “wait and see” approach on inflation.

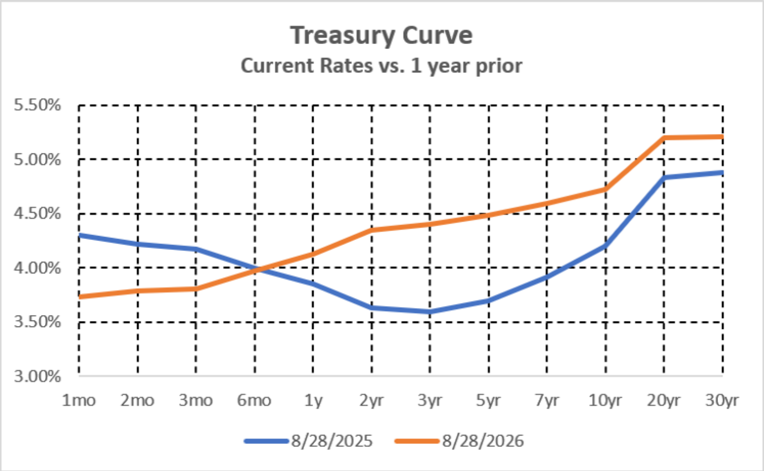
The labor market continues to revert back to its low job creation mode after some surprisingly strong jobs numbers for the first several months of the year (some of which were later revised downwards). The unemployment rate has declined, but largely due to declining labor force participation rather than people getting jobs. Wage gains in July were at their slowest annual pace in more than five years.

Inflation data has improved from the initial spike from the war with Iran but remains well above the Fed’s target. The last time that core inflation was at or below the 2.00% target was February 2021. The economy has operated in this low job growth/higher inflation environment for several years now. Continued high levels of AI spending and the wealth effect should keep the economy growing for at least the next several quarters.

Fixed Income Outlook

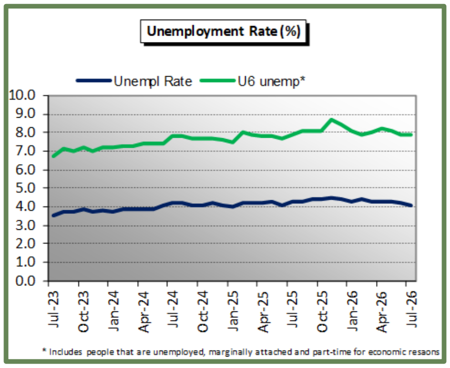
Treasury rates were little changed during the month of August. The market is pricing in 65% odds of a Fed hike at their next meeting in September, and two cumulative hikes are priced in by March 2027. Chairman Warsh’s Jackson Hole speech makes a near-term hike much more likely, and if inflation and labor data stay on course, we would expect a rate hike at the September 15 meeting. Treasury markets appear fairly valued at current levels.





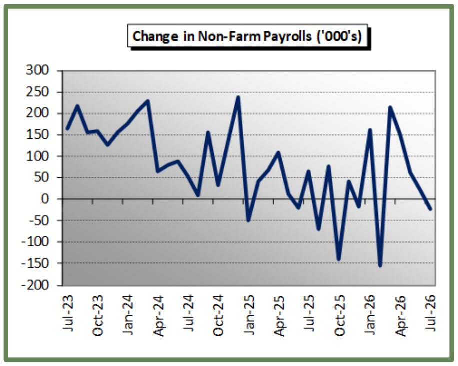
Labor Readings

(Data source: Bloomberg)



Unemployment Rate Declines Again

The unemployment rate decreased for the second consecutive month to 4.1% in July versus 4.2% for the prior month. This matches the lowest unemployment rate since the beginning of 2025. The market was expecting the rate to remain unchanged. Other labor indicators were weak as the participation rate hit its lowest level since the 1970's (excluding the pandemic). In addition, wage growth was weaker than expected and is increasing at the slowest pace in five years.

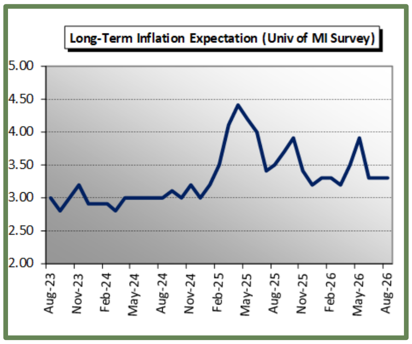


Payroll Growth Weaker Than Expected

Payroll growth in July was lower than expected. The number of jobs decreased by 23,000 versus an expected gain of 80,000. In addition, the previous two months were revised lower by 103,000. The current three-month average payroll growth has fallen back to the average growth in 2025.

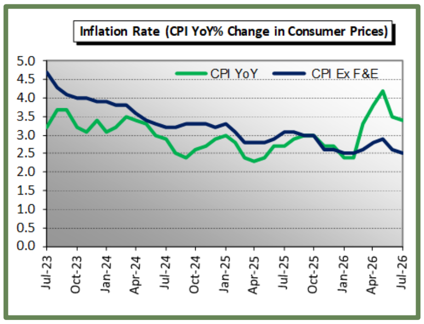
Inflation Readings

(Data source: Bloomberg)



Inflation Expectations Still Contained

Consumers' expected inflation expectations remain relatively muted despite an extended period of headline inflation being above the Fed's 2% target. Expected inflation for the upcoming 12 months fell to 4%, the lowest level since March. Longer-term inflation expectations remained at 3.3%.

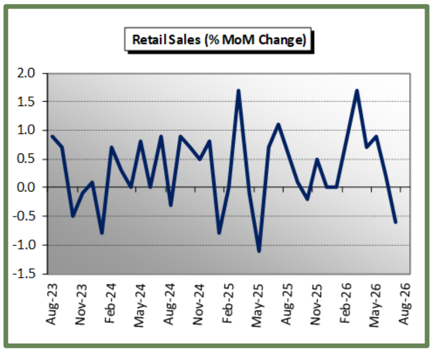


Consumer Inflation Declines

Consumer inflation in July continued to show moderation from the previous months' levels. Core inflation levels matched the slowest pace (on a year-over-year basis) since March 2021. Headline inflation has fallen as energy prices have declined over the last few months.

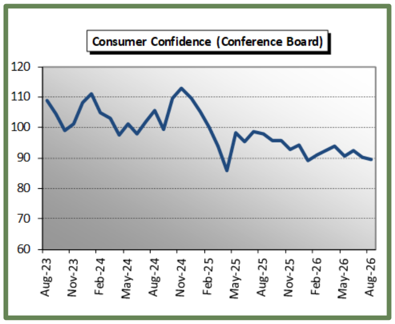
Consumer Readings

(Data source: Bloomberg)



Consumer Spending Stalls

Consumer spending in July was much weaker than expected. Spending fell by .6% on a month-over-month basis versus an expected gain of .1%. It was the lowest growth rate in more than year. Some of the variance may be attributable to Prime Day occurring in June this year and effectively pulling sales forward.



Consumer Confidence Declines

Consumer confidence in August fell to the lowest level since the start of the year. Consumers have become more negative on future job and income prospects.