Financial Markets This Week

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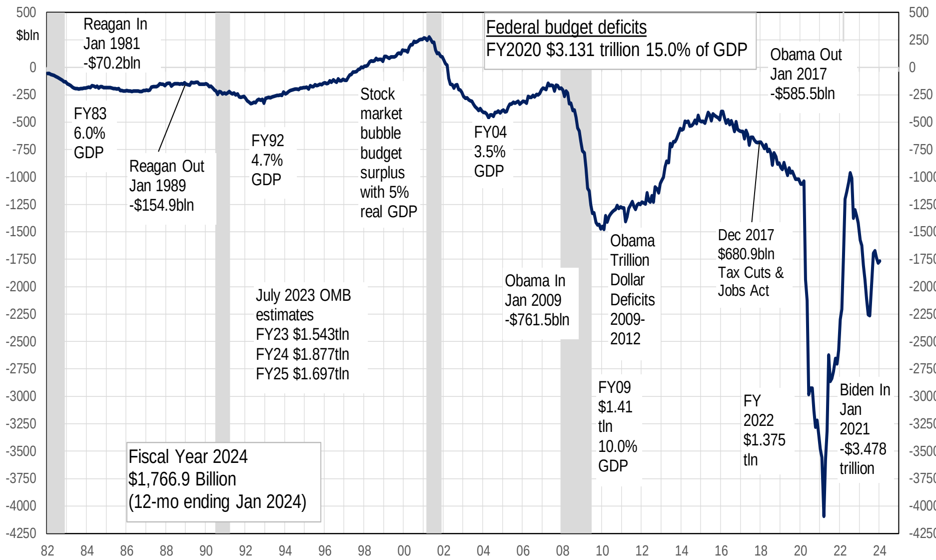
JANUARY BUDGET UPDATE



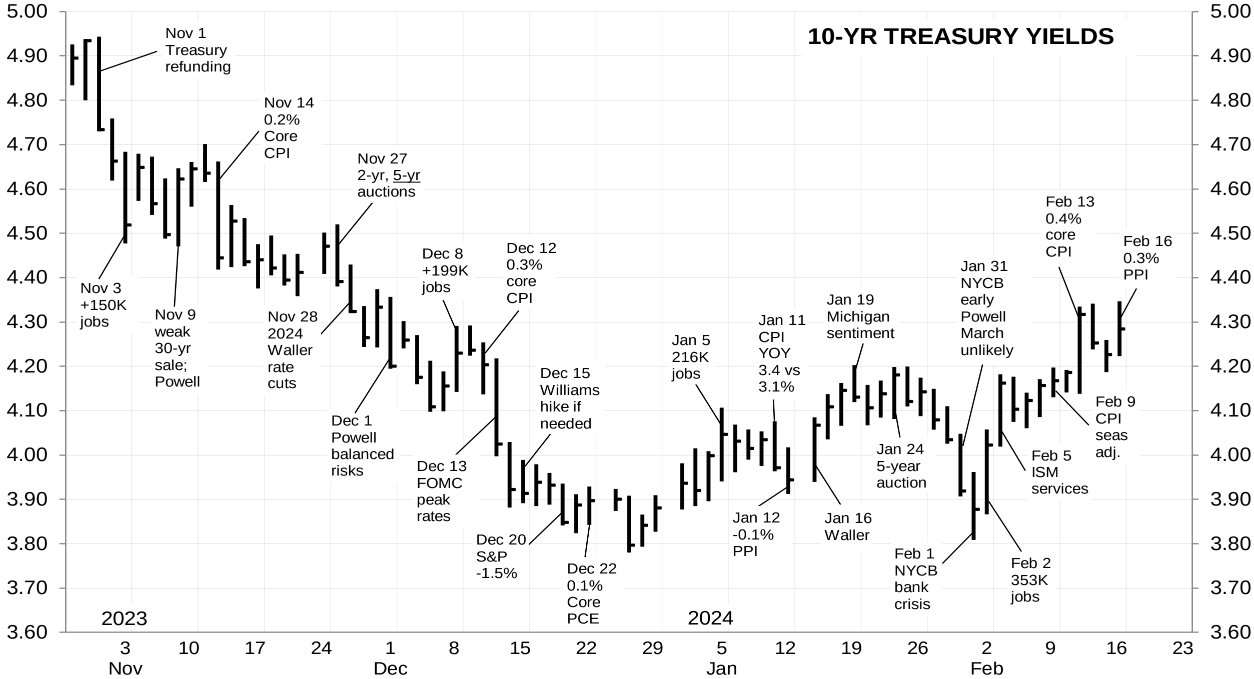
The Federal budget deficit continued to run around $1.7 trillion in the 12-months ending January 2024. This is about the limit to keep the debt to GDP ratio from rising further. February 15 total public debt was $34.3 trillion, if nominal GDP is running 5.0%, 0.05 X 34.3 is a max Federal deficit run-rate of $1.715 trillion. January budget results but no fiscal year September 2024 budget yet. Next deadline is March 1 with the House out of town until February 28.

Social Security In/Out

$ bln	Receipts	Payments	Red/Black
FY2019	770.282	888.080	-117.798
FY2020	825.307	940.221	-114.914
FY2021	814.034	982.673	-168.639
FY2022	911.191	1,063.897	-152.706
FY2023	1,020.442	1,192.149	-171.707
Nov 23	75.087	103.362	-28.275
Dec 23	87.354	103.704	-16.350
Jan 24	100.015	107.337	-7.322

A couple of issues ahead. Interest on the public debt in the first 4 months this fiscal year was $357.2 billion in January, but just $283.3 billion is on debt issued to the public, the rest is social security funny money. It is going up. Average interest rates on the $13.8 trillion of marketable notes outstanding was 2.34% on January 31, 2024, and 2-year notes closed Friday at 4.64% on out the maturity spectrum to the 10-year notes closing at 4.28% Friday. 2.34% interest on $13.8 trillion is $314 billion currently, and at 4.5% the interest cost annually would be $621 billion. Another few hundred billion over time, not so bad as about $2 trillion of marketable notes mature each year currently and will be gradually reset at higher interest rates depending how long the reality of the Fed's 5.5% policy rate stays with us. The other budget issue is social security and our call would be to do nothing, Congress is good at it, and wait for the demand-surge for benefits from the 60 to 78 year old baby boom retirees to start going away starting twenty years from now when the generation after the greatest generation leaves the stage. The lawyers might need to be called in as the trust fund cannot pay out benefits once it is "empty." But any retirement benefits due in excess of social security tax receipts are already being made whole from general Treasury revenues collected from other sources and/or from Treasury borrowing from the markets. FY2023 social security receipts of $1.020 trillion were $171.7 billion less than benefits, adding to the deficit by the same amount. Receipts are 14.4% less than payments which is where the talk of cutting your social security benefits by 14% comes from.

INTEREST RATES

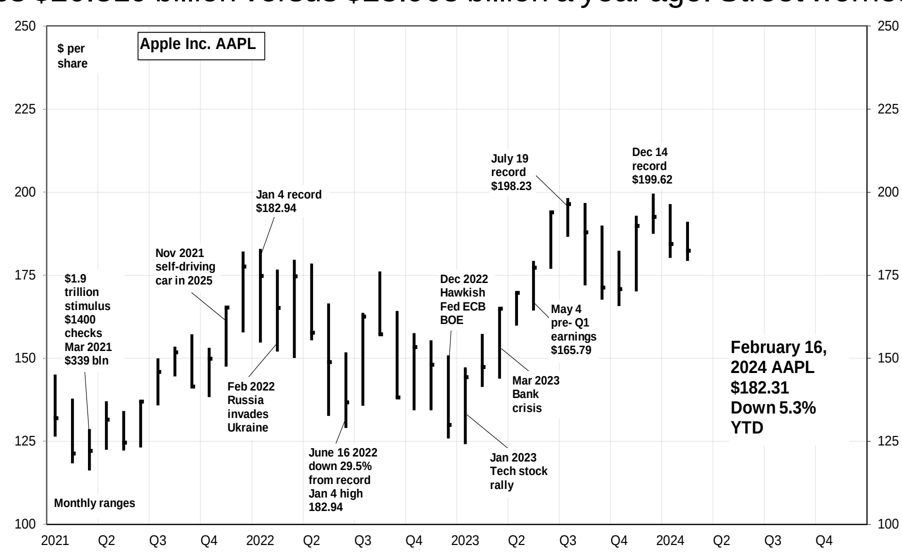


Big inflation outbreak from the economic data this week, starting with 0.4% core CPI on Tuesday, sent bond yields up and the stock market down. The S&P 500 did make a record close on Thursday, but gave it up Friday afternoon. PPI was higher and led to more forecasts of a 0.4% core PCE inflation print in a couple of weeks. Bond yields jumped 13 bps to 4.32% Tuesday on the CPI surprise. 10-yr yields retraced part of the move, and the low yield was 4.19% after retail sales fell 0.8% on Thursday to start the year off right, and bonds thought that was important news briefly. Another hot inflation report on Friday from PPI brought yields back to the 4.34% highs for the week, that move faded as well and 10-yr yields closed the week at 4.28%. Same forecast though. If the Fed cuts rates to 3.0% at the end of 2026, 10-yr yields are still likely to be 4-4.25 percent.

Apple, Inc. AAPL $182.31 down 5.3% YTD

Thursday night February 1 Apple, Amazon, Meta reported. Like the three little pigs, Meta jumped 20.3% Friday, helping to pull Apple back from the cliff. Apple fell as much as 4.1% Friday, February 2 to $179.25, before cutting the loss to 1.0%. Year-year revenues are back to positive, and would have been more but for Greater China sales $20.819 billion versus $23.905 billion a year ago. Street worries Apple does not have foldable phones in China like Huawei does.

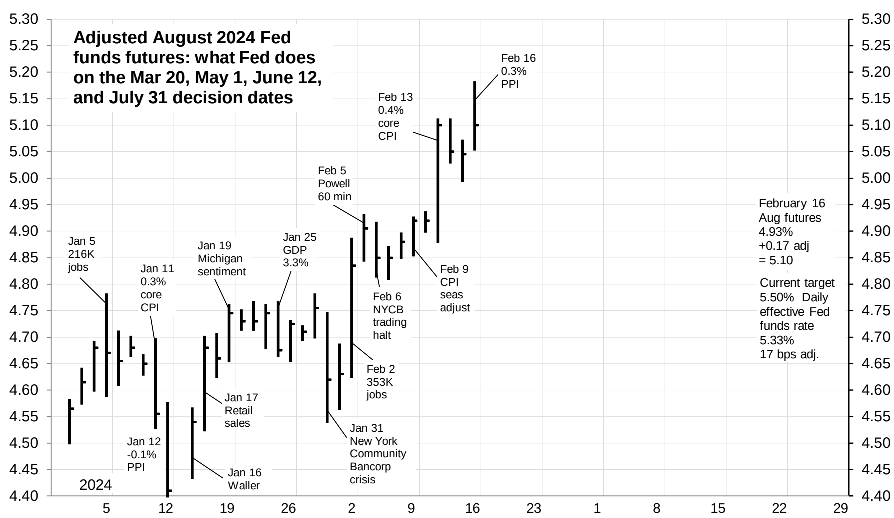
Calendar Year Mln $	Operating Income	Net Sales	iPhone	Greater China
Q4 2023	40,373	119,575	69,702	20,819
Q3 2023	26,969	89,498	43,805	15,084
Q2 2023	22,998	81,797	39,669	15,758
Q1 2023	28,318	94,836	51,334	17,812
Q4 2022	36,016	117,154	65,775	23,905
Q3 2022	24,894	90,146	42,626	15,470
Q2 2022	23,076	82,959	40,665	14,604
Q1 2022	29,979	97,278	50,570	18,343



FEDERAL RESERVE POLICY

Selected Fed assets and liabilities						Change
Fed H.4.1 statistical release						from
billions, Wednesday data	14-Feb	7-Feb	31-Jan	24-Jan	3/11/20*	3/11/20
Factors adding reserves						to Feb 14
U.S. Treasury securities	4692.495	4692.608	4692.721	4722.302	2523.031	2169.464
Federal agency debt securities	2.347	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	2417.227	2417.156	2417.156	2428.644	1371.846	1045.381
Repurchase agreements	0.000	0.000	0.000	0.000	242.375	-242.375
Primary credit (Discount Window)	2.419	2.334	3.189	2.785	0.011	2.408
Bank Term Funding Program	164.772	164.869	165.238	167.768		
FDIC Loans to banks via Fed	0.000	0.000	0.000	0.000		
Paycheck Protection Facility	3.258	3.298	3.320	3.338		
Main Street Lending Program	15.132	15.103	15.083	15.394		
Municipal Liquidity Facility	0.001	0.001	0.001	0.001		
Term Asset-Backed Facility (TALF II)	0.000	0.000	0.000	0.000		
Central bank liquidity swaps	0.227	0.230	0.219	0.224	0.058	0.169
Federal Reserve Total Assets	7684.7	7682.1	7680.2	7728.0	4360.0	3324.649
~~3-month Libor %~~ SOFR %	5.30	5.31	5.32	5.31	1.15	4.150
Factors draining reserves						
Currency in circulation	2328.158	2327.380	2326.951	2329.477	1818.957	509.201
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000	0.000
U.S. Treasury Account at Fed	831.880	821.575	865.481	815.159	372.337	459.543
Treasury credit facilities contribution	7.438	7.438	7.438	7.438		
Reverse repurchases w/others	575.332	553.055	615.379	639.560	1.325	574.007
Federal Reserve Liabilities	4147.206	4126.358	4268.525	4238.298	2580.036	1567.170
Reserve Balances (Net Liquidity)	3537.469	3555.738	3411.717	3489.709	1779.990	1757.479
Treasuries within 15 days	118.167	82.267	83.218	69.991	21.427	96.740
Treasuries 16 to 90 days	194.735	230.601	229.458	250.636	221.961	-27.226
Treasuries 91 days to 1 year	552.704	552.753	530.721	552.163	378.403	174.301
Treasuries over 1-yr to 5 years	1580.306	1580.352	1602.637	1594.803	915.101	665.205
Treasuries over 5-yrs to 10 years	741.748	741.769	741.790	749.752	327.906	413.842
Treasuries over 10-years	1504.834	1504.865	1504.897	1504.956	658.232	846.602
Note: QT starts June 1, 2022	Change	2/14/2024	6/1/2022			
U.S. Treasury securities	-1078.284	4692.495	5770.779			
Mortgage-backed securities (MBS)	-290.219	2417.227	2707.446			
**March 11, 2020 start of coronavirus lockdown of country						

The Fed meets March 19-20, 2024 to consider its monetary policy. Another week of Fed speak all day every day. And Chicago Fed President Goolsbee talked a long time on Wednesday morning after the Tuesday 0.4% core CPI figure, but we are not sure you want to say that 'let's not get too flipped out about yesterday's inflation data.' The S&P 500 fell 1.4% on Tuesday, and had already retraced a lot of the sell-off before Goolsbee spoke Wednesday morning. The question is whether CPI will change the Fed forecasts for three rate cuts in 2024 at next month's meeting. The Street seems convinced January core PCE inflation will be 0.4% as well, released Thursday, February 29 at 830am ET, after stronger import prices reported Thursday (nonfuel imports 0.7% in January, the most since March 2022), and PPI inflation on Friday. Most of the prices in PCE inflation are from CPI figures, but many prices, especially in medical care services, are taken from the PPI report. Health care is a significant 18.3% of core PCE inflation. At the end of the day though, markets are sifting through January statistics and more time will be needed to see whether price pressures continue in the reports for February, March and beyond. The Fed decision to cut rates at the June 11-12 meeting, probably will not be able to rely on May CPI released 830am June 12 on decision day, but inflation data for CPI and PCE will be available up through the month of April. Stay tuned. August Fed funds futures are still consistent with a 25 bps rate cut in either June or July.



Fed funds futures call Fed policy		
Current target: February 16 -- 5.50%		
Rate+0.17	Contract	Fed decision dates
5.475	Apr 2024	Mar 20
5.095	Aug 2024	May 1, Jun 12, Jul 31
Last trade, not settlement price		

August Fed funds futures adjusted are 5.095%, and if the Fed does go in June or July, and then again in September and December, it should be 5.25%.

Next up: January PCE inflation report Thursday, February 29														
Monthly	2024	2023										2023	2022	
% Changes	Jan	Dec	Nov	Oct	Sep	Aug	Jul	Jun	May	Apr	Mar	Feb	Jan	Dec	Nov
Core CPI inflation	0.4	0.3	0.3	0.2	0.3	0.2	0.2	0.2	0.4	0.5	0.3	0.5	0.4	0.4	0.3
Core PCE inflation		0.2	0.1	0.1	0.3	0.1	0.1	0.2	0.3	0.3	0.3	0.4	0.5	0.4	0.3
Core PCE YOY		2.9	3.2	3.4	3.6	3.7	4.2	4.3	4.7	4.8	4.8	4.8	4.9	4.9	5.1
Core CPI YOY	3.9	3.9	4.0	4.0	4.1	4.3	4.7	4.8	5.3	5.5	5.6	5.5	5.6	5.7	6.0

OTHER ECONOMIC NEWS

Core CPI 0.392% (Tuesday)

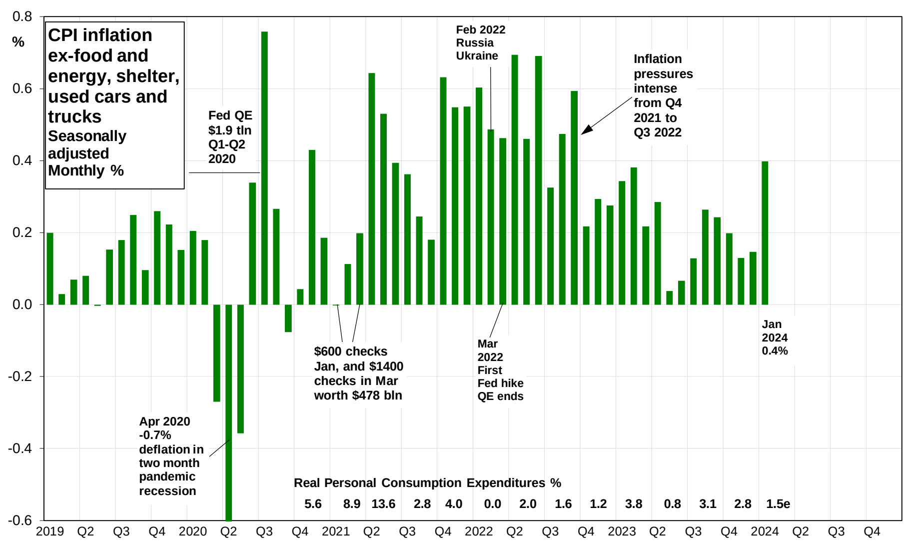
Breaking economy news. Hard to spin ourselves out of this one. Inflation is back, maybe never left. The stock market is worried: more inflation means Fed rate cuts are delayed. Core CPI, already too high with 0.3% monthly changes in November and December, comes out today at 0.4% in January to start the year. Ouch. Many firms start the year off with price hikes for their goods and services in an inflationary period. The dead of winter months, January and February, are the time when core CPI prices increase the most every year, maybe the seasonal factors are evolving and until we get more annual data, they cannot currently tame (tamp down, smooth out) the increases. Anyway, before the 2020 pandemic, core monthly not seasonally adjusted (NSA) changes were 0.4% in January/February, and now they are still running bigger, 0.6% in January 2024 reported today. Time will tell if inflation is still slowing.

Core CPI not seasonally adjusted monthly % changes

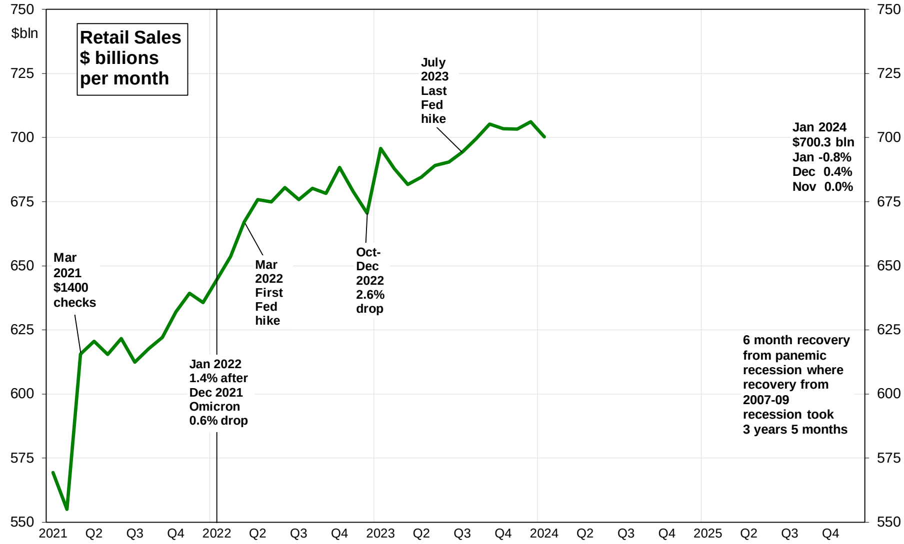
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2018	0.4	0.4	0.3	0.2	0.2	0.1	0.1	0.1	0.2	0.2	0.0	0.0
2019	0.4	0.4	0.3	0.2	0.1	0.2	0.1	0.2	0.1	0.2	0.0	-0.1
2020	0.4	0.5	0.0	-0.5	-0.1	0.2	0.5	0.4	0.1	0.1	0.1	-0.1
2021	0.2	0.3	0.4	0.8	0.7	0.8	0.3	0.1	0.1	0.6	0.4	0.4
2022	0.7	0.7	0.4	0.5	0.6	0.7	0.3	0.5	0.4	0.3	0.1	0.2
2023	0.6	0.7	0.5	0.5	0.4	0.3	0.2	0.2	0.2	0.2	0.1	0.1
2024	0.6											

We hate to be a lawyer, but the Fed targets PCE inflation not CPI inflation. Core PCE inflation was exactly on target (Q3 and Q4 2.0% SAAR) in the second half of 2023, and we will soon see what the new year brings. January 2024 PCE inflation is due out on Thursday, February 29 at 830am ET with the personal income report. Medical services inflation seems to be back, and these carry a bigger weight in PCE inflation than CPI. At the same time, the 0.6% jump in shelter in January won't boost PCE inflation as much. Shelter has a gigantic 45.4% weight in core CPI, but the weight in core PCE inflation is just 20.1%. Stay tuned. Story developing. There is inflation in the air, how much and for how long is the question. The street core PCE forecasts are already coming in at 0.4% in a couple of weeks as most of the prices that go into PCE inflation come from the CPI report. Go figure.

Dec 23		Monthly Percent Changes			YOY %
Weight	CPI inflation	Nov 2023	Dec 2023	Jan 2024	Jan 2024
100.0	Total	0.2	0.2	0.3	3.1
13.555	Food	0.2	0.2	0.4	2.6
5.388	Food away from home	0.4	0.3	0.5	5.1
6.655	Energy	-1.6	-0.2	-0.9	-4.6
79.790	Ex-food & energy	0.3	0.3	0.4	3.9
3.684	New vehicles	0.0	0.2	0.0	0.7
2.012	Used cars/trucks	1.4	0.6	-3.4	-3.5
2.512	Clothing	-0.6	0.0	-0.7	0.1
1.489	Medical care goods	0.5	-0.1	-0.6	3.0
36.191	Shelter	0.4	0.4	0.6	6.0
26.769	Owner equiv. rent	0.5	0.4	0.6	6.2
6.294	Transportation	1.0	0.1	1.0	9.5
6.515	Medical care services	0.5	0.5	0.7	0.6
	Special: Where inflation might come back down to				
60.899	Services ex-energy	0.5	0.4	0.7	5.4
18.891	Commodities (core)	-0.2	-0.1	-0.3	-0.3



Blame the weather (Thursday)



Breaking economy news. Retail sales tumbled at the start of the year and the only good news is that the pullback is probably winter weather related and not a sign of spending cuts that herald a recession is coming. Fed officials are unlikely to take the latest clickbait doomsday economic news that the sky is growing darker. But make no doubt, it is darker because only a month ago consumer spending was so strong going into December that retail sales in Q1 2024 were up 2.0% SAAR without any data for January, February, and March. Now with today's January data in hand and big downward revisions to last month's November and December gains, retail sales are in the hole, down 2.3% this quarter with February and March to go. One thing is for sure and that is retailers cannot keep the price of goods higher for long, like this month's CPI report suggested, if consumers are not out shopping. Turn it around the other way, maybe in addition to the cold winter in much of the country, maybe consumers have sticker shock and are not buying their favorite store-bought goods because prices are simply too darn high for families to afford.

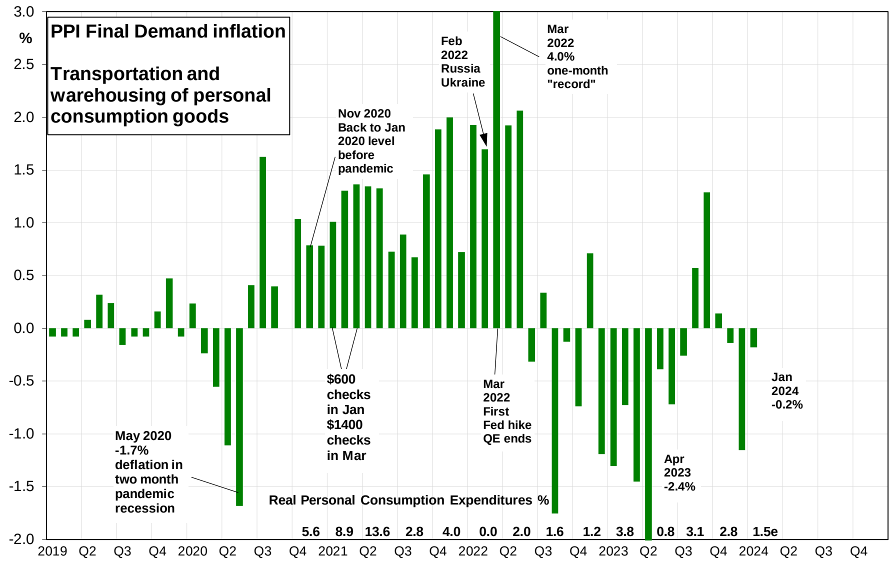
Retail spending, actual dollars, each month

	$million	% to	Percent Changes %		
	Jan	Total	Jan	Dec	Year/year
Total Retail Sales	700,291	100.0	-0.8	0.4	0.6
Motor vehicles/parts	132,431	18.9	-1.7	0.3	-1.6
Furniture/furnishings	11,070	1.6	1.5	-0.2	-9.8
Electronics/appliances	7,335	1.0	-0.4	-0.9	-5.8
Building materials/garden	39,655	5.7	-4.1	0.9	-8.3
Food & beverage	83,267	11.9	0.1	0.2	1.9
Health/personal care	36,467	5.2	-1.1	-1.6	5.0
Gasoline stations	52,409	7.5	-1.7	-0.8	-7.5
Clothing/accessories	26,551	3.8	-0.2	1.3	0.5
Sporting goods, books	8,481	1.2	-0.2	-0.7	-3.2
General merchandise	73,938	10.6	0.0	1.2	0.9
Department stores	10,997	1.6	0.5	2.8	-6.7
Miscellaneous retailers	15,201	2.2	-3.0	-0.3	-2.7
Nonstore retailers (internet)	118,393	16.9	-0.8	1.4	6.4
Eating & drinking places	95,093	13.6	0.7	0.2	6.3

Net, net, it was a weak start to the year for consumers shopping at the malls, but the harsh winter weather effect looms large with thousands seeing reduced hours or unable to work due to the bad weather in January. If you cannot work or venture out you can always shop from your smartphone sitting on the couch, but this did not happen either this month. Fed officials are sophisticated and seasoned veterans at sifting through the monthly economic news reports, and one thing they do not do is rush to any conclusions from one-month data points, especially when there are reasons to believe the number is noise caused by a temporary situation like winter weather, hurricanes and related storms that keeps consumers at home. Nevertheless, the stage is set for a pronounced slowing of economic growth if retailers do not see a pickup in sales later this quarter. In the backdrop of course is the puzzle of the latest weekly labor market data where first-time applications for unemployment compensation fell, but the total number receiving benefits jumped back to nearly 1.9 million and is the highest since mid-November last year. In addition to the reports of companies laying off staff, there are anecdotal reports from job seekers that it is harder to get a job and this may be keeping jobless workers on the dole.

Another black-eye inflation report (Friday)

Breaking economy news. PPI inflation for Total final demand prices rose 0.3% in January after falling 0.1% in December. Final demand goods prices less foods and energy rose 0.3% the most since 0.3% in September. Inflation is back, not in a big way, but it is also true that it is not going away and could yet wreak havoc on the broader economy where higher factory prices increase inflation at the consumer level. Producer prices are often focused on goods, but services prices jumped in January thanks in part to the 2.2% increase in hospital outpatient care. Don't get sick.The only good news in the report is that transportation and warehousing costs fell 0.4% so supply-chain pressures are easing.



Net, net, anyway you want to cut it, producer level, consumer goods sitting on store shelves, imported goods, it just wasn't the Fed's month for its inflation fight. We don't know if it is a true setback, but there is certainly no reason to move the rate cuts schedule forward this year because the labor market is relatively tight which means inflation pressures could start to build again if Fed officials relax their guard too early. There could be some seasonal adjustment problems as prices move up the most each year in the dead of winter, meaning January and February, but still the data in hand look more on the worrying side than the congratulations side. Even physicians' offices got a price hike in January, the biggest increase since January 2021 when medicare changed their allowances and cut doctors a break, if they need one. The Fed isn't losing the inflation fight, but they aren't winning either, especially with the black-eye report of 0.4% core CPI reported on Tuesday. Stay tuned. Story developing. The data are consistent, CPI, PPI, import prices, that January is a problem month for inflation. All eyes on the Thursday, February 29 PCE inflation report for January, assuming 0.4% core PCE is not discounted already.

	PPI Final demand goods less foods/energy-- Monthly Percent Changes SA											
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2023	0.6	0.3	0.2	0.1	0.1	-0.1	0.0	0.1	0.3	0.1	0.1	0.1
2024	0.3											
	PPI Final demand goods less foods/energy-- Year/Year Percent Changes NSA											
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2023	5.6	5.1	4.3	3.3	2.7	2.0	1.9	1.8	2.1	2.1	2.0	1.9
2024	1.6											

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