Weekly Commentary with Professor Jeremy J. Siegel

Mixed Economic Signals: Inflation Down, Claims Up

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The inflation data released last week was very encouraging, with key indices like the Consumer Price Index (CPI) and the Producer Price Index (PPI) coming in below expectations. The details were even better than official reports, as there are persistent biases in shelter costs which are keeping the official CPI reports higher than reality. When we adjust for more realistic rental rates, core inflation reads out as 1.6% over the last 12 months compared to the 3.4% reported officially. The Federal Reserve (Fed) seems to be getting this message, and even Janet Yellen summarized on CNBC, that high CPI reports are primarily driven by outsized but lagged shelter numbers that will come down over time.

Jobless claims this week were slightly concerning, rising just above the 200-240K desired range indicating a sign of a balanced economy. There is a lot of noise in this series, but it's something to watch closely as it might indicate softness in labor market conditions.

Consumer spending trends and expectations have shown a slight downturn. With the retail sales data on the horizon, this week will be crucial in assessing whether the jobless claims are the start of a more significant slowdown.

The stock market's response is mixed, with significant performance in sectors driven by artificial intelligence (AI) and tech innovations, notably NVIDIA, which has continued to capture the investor’s imagination. Although there’s a palpable concern about a potential slowdown or even a recession, I remain optimistic that we’re not on that path yet. Small caps and some of the value sectors need the Fed to start cutting rates to begin a more meaningful uptrend in these stocks.

Looking ahead, while there was a lot of discussion on the Fed’s dot plot, the Federal Open Market Committee (FOMC) members have no idea what their policy will be as they are totally data dependent. Fed cuts are contingent on continued positive inflation trajectories that I expect to materialize.

Overall, the market is navigating through a complex set of economic indicators. We believe investors should remain vigilant and diversified in their investment approaches, particularly considering the narrow focus of recent market rallies around specific tech stocks, which may not be sustainable in the long. FOMO still rules the market for AI-related stocks.

Glossary

Artificial intelligence (AI): A field that combines computer science and robust datasets to enable problem-solving.

Consumer Price Index (CPI): A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

Dot plot: A chart based on the economic projections of the Federal Reserve board members that illustrates their views on the appropriate pace of policy firming and provides a target range or target level for the federal funds rate.

Federal Open Market Committee (FOMC): The branch of the Federal Reserve Board that determines the direction of monetary policy.

Federal Reserve (Fed): The Federal Reserve System is the central banking system of the United States.

Inflation: Characterized by rising price levels. Core inflation excludes the impact of food and energy. Headline inflation is a measure of the total inflation in an economy, including the prices of food, energy, and other wholesale products that households use daily.

Producer Price Index (PPI): weighted index of prices measured at the wholesale, or producer level.