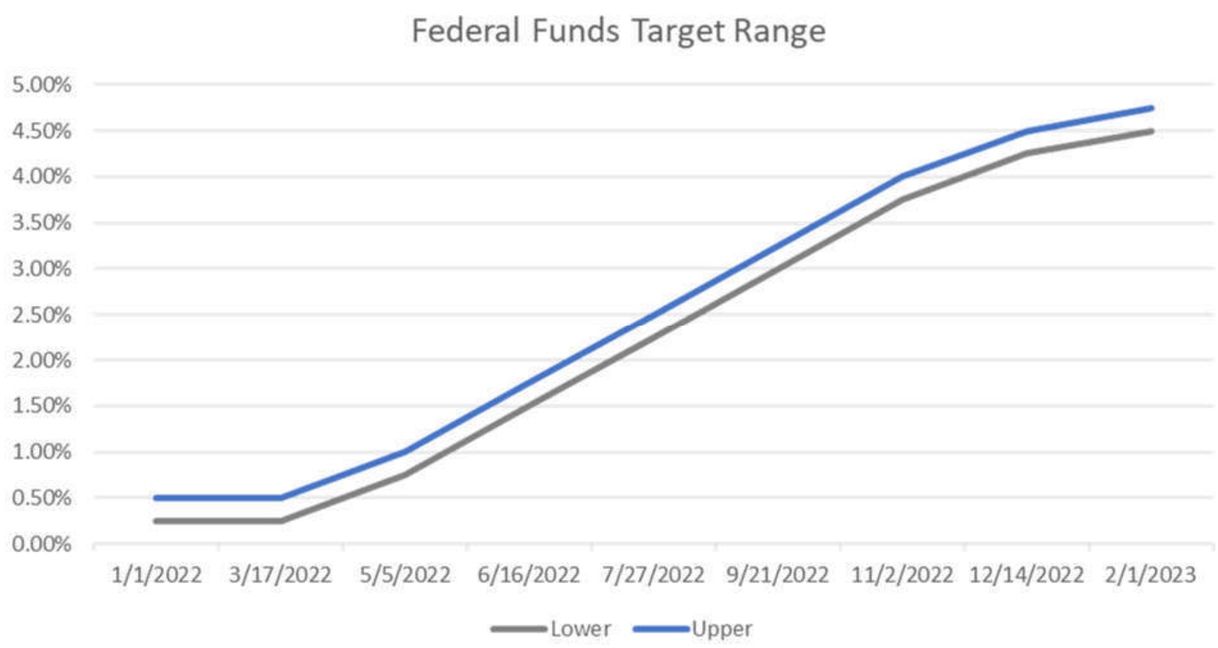
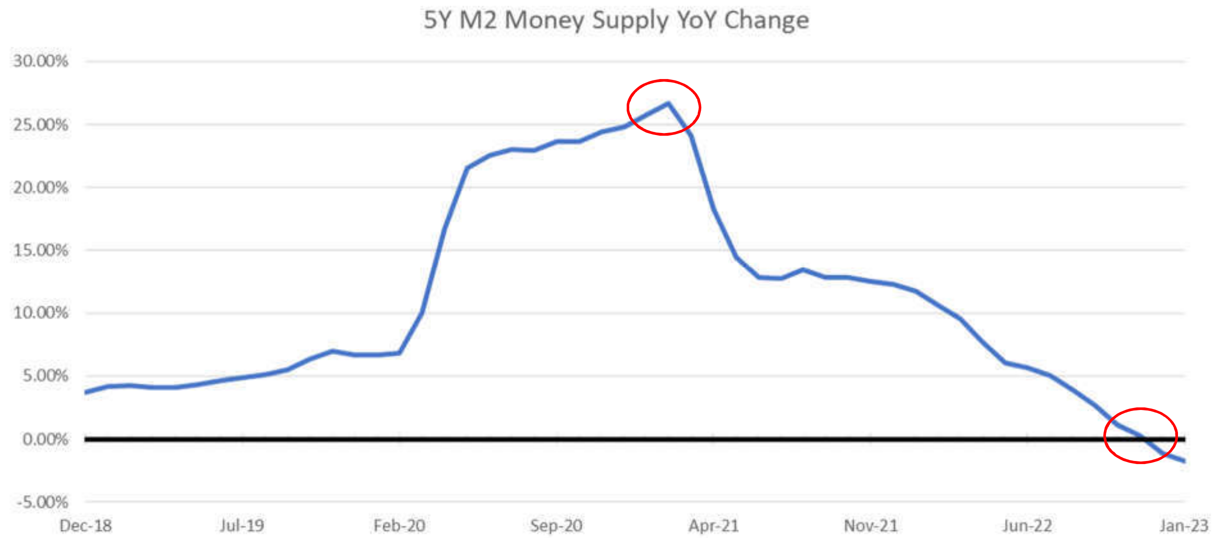
February Update

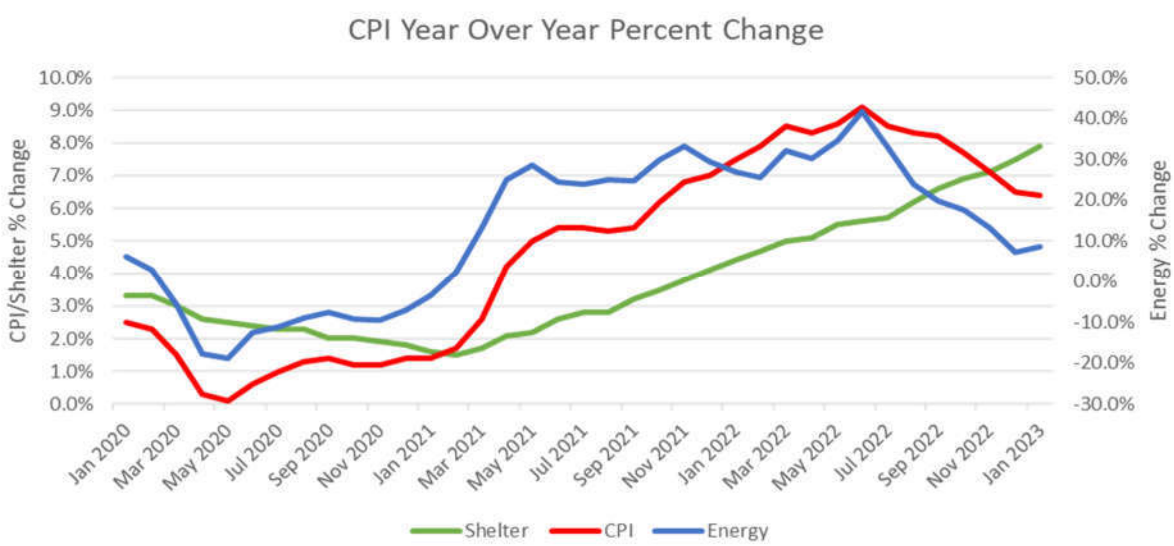
The Fed met in early February to decide again on interest rates. To no one's surprise, they raised interest rates by another 0.25%. While this was expected, the discussion quickly turned to how long they will continue to raise interest rates. They are trying to slow the economy, and more specifically inflation. While economic indicators are showing their desired results, they also see pushback from other indicators.



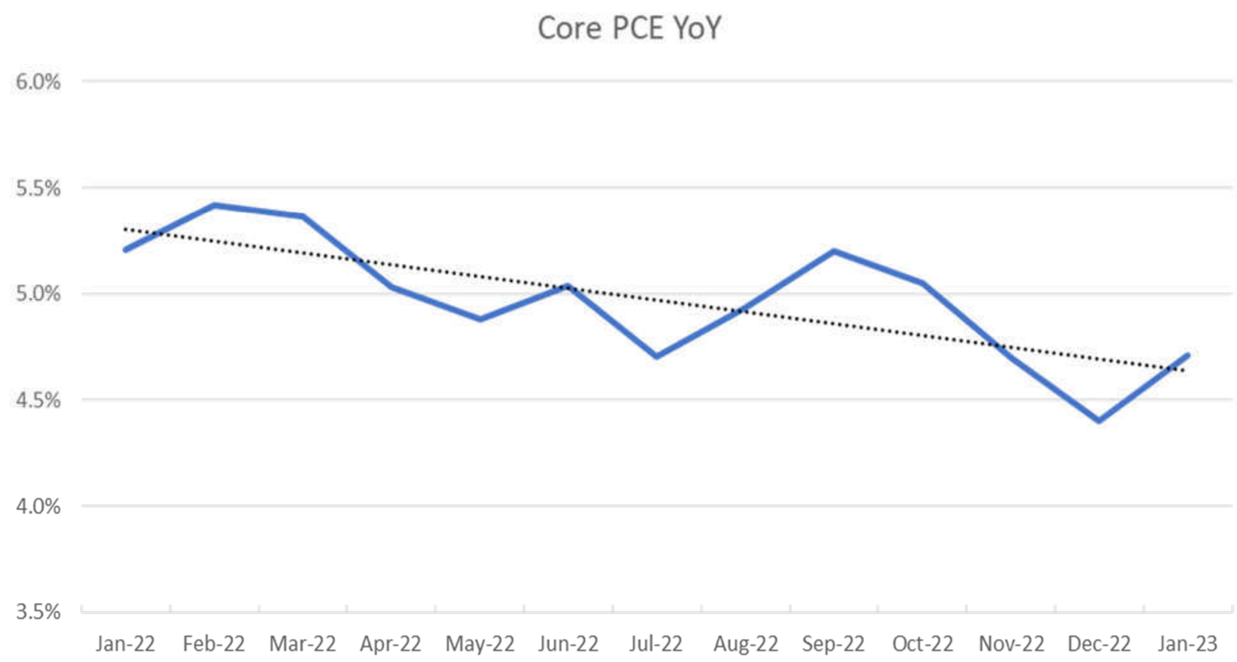
One of the indicators of a slowing economy is the M2 money supply. M2 money supply is all cash, money deposited in checking and savings accounts, and other short term vehicles, such as CDs and retail money market funds. The Fed has published data for M2 money supply since 1959. After going through unprecedented times with the pandemic, people began to save money and were even issued stimulus checks. This impact can be seen in the middle of the graph on the next page. Since the data has been published, the year-to-year change has never been negative until December 2022 at (-1.12%). January's numbers showed a further contraction of (-1.7%). While we can't say what these numbers mean for the future, it covers the Fed's current plan on the economy to some extent.



The Consumer Price Index (CPI) is the most visible inflation measure to the American public. Last month experts were shocked that it did not fall as fast as expected. As a result (and taking other economic indicators into effect), it is widely expected that interest rates will continue to rise longer than previously expected, or they will increase the level rate higher. There could be a reason why CPI didn't fall as fast as expected. As you can see on the graph below, CPI and Energy follow each other closely. Both hit their bottom in May 2020 and both hit their peak in June 2022. Since June, both CPI and Energy have been falling, but Shelter has been steadily rising, pushing back against the total CPI. Shelter is the most significant component of CPI, with a weight of 34.41%. If a property is owned, the price changes are viewed by rent prices or the equivalent prices. However, how this data is collected may significantly impact on how it affects CPI. Change in rent prices are only collected every six months. Furthermore, when CPI is being calculated, it uses data from the period before the most recent price change. That leaves room for up to a 12-month lag in the most significant portion of this economic indicator. This is important because it could be using data from when inflation was still rising rapidly or at the very least when it was near its peak.



Personal Consumer Expenditures (PCE) is the Fed's preferred economic indicator to gauge inflation. This looks at individual's everyday spending rather than price changes, like CPI. January's report also missed expectations and brought fear that inflation is not as muted as previously thought. PCE has been trending down over the last 12 months, specifically falling every month from September to December. In January, it jumped back up to 4.7%, again leading to the question of, "is the Fed doing enough?"



This leads back to the question: "Will the Fed push our economy into a recession? If we enter a recession, will it be a soft or hard landing?" The fact of the matter is only time will tell. The economy has been resilient, and it is uncertain whether that will hold. But, regardless of where the economy is headed, there is always value to be found and we continuously seek to find it.

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