First Trust
Monday Morning OUTLOOK

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Reports: Solid Growth, Persistent Inflation

Recent economic reports further undermine the politically-motivated argument from earlier this year that the US was already in a recession. They also undercut the Fed's hopes that inflation will soon subside.

On the job front, nonfarm payrolls rose 263,000 in September while the unemployment rate fell back to 3.5%, tying the lowest level since 1969. Payrolls are up at an average monthly pace of 420,000 so far this year – that isn't a recession. And data show the share of voluntary job leavers (often called "quitters") among the unemployed reached 15.9%, the highest since 1990. People don't quit their jobs unless they have optimism about their job and earning prospects.

Meanwhile, the ISM Services index came in at a robust 56.7 for September. Yes, the ISM Manufacturing index declined to 50.9, but that's still in expansion territory (north of 50) and the services portion of the economy is much larger than manufacturing. Auto sales remained softer than normal in September, but, at a 13.5 million annual rate, were the fastest since April.

Put it all together, and we are tracking a 3.0% real GDP growth rate in the third quarter. The Atlanta Fed's GDPNow model is tracking 2.9%, almost exactly the same. Net exports look very good in Q3 and should account for most of the growth. Again, no recession, yet.

At the same time, inflation remains stubbornly high. The consensus forecast for this Thursday's report on the Consumer Price Index (CPI) is that it grew by a relatively mild 0.2% in September. We would not be surprised by an increase of 0.2% but think the increase is more likely to be 0.3%.

But that's for September, when oil prices were weaker. For October, the Cleveland Fed's "inflation nowcast" is tracking an increase of 0.7% in the CPI. The Cleveland Fed also forecasts the "core" CPI, which excludes food and energy, will rise 0.5% in both September and October. In addition, the nowcast suggests PCE inflation will run 6.1% for 2022 (Q4/Q4) compared to the 5.4% the Federal Reserve projected less than three weeks ago.

If the Fed can keep the M2 measure of the money supply growing at the 1.5% annual rate that's prevailed so far this year, we think inflation will eventually slow down. But that doesn't mean it's going to slow down as fast as the Fed thinks. Less than three weeks ago the Fed projected 2.8% PCE inflation in 2023. That seems like a political forecast, not a forecast based on economic reality and models.

Rents make up a large part of consumer inflation measures and still have a very long way to go to catch up to home price appreciation during COVID. They're an even larger part of "core" inflation measures, which should outstrip broader inflation for the next year or so. Moreover, after falling below $80 a barrel a few weeks ago, West Texas Crude prices are now back above $90. Inflation data is not going to be pretty in the quarters ahead.

The bottom line is that the Fed isn't going to stop or even slow rate hikes very soon. Expect another hike by three-quarters of a percentage point (75 basis points) in early November, followed by another half percentage point (or more!) in mid-December. Then, in 2023, look for rougher economic waters by year end.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
10-12 / 7:30 am	PPI – Sep	+0.2%	**+0.2%**		-0.1%
7:30 am	"Core" PPI – Sep	+0.3%	**+0.3%**		+0.4%
10-13 / 7:30 am	CPI – Sep	+0.2%	**+0.3%**		+0.1%
7:30 am	"Core" CPI – Sep	+0.4%	**+0.5%**		+0.6%
7:30 am	Initial Claims – Oct 8	225K	**215K**		219K
10-14 / 7:30 am	Retail Sales – Sep	+0.2%	**+0.1%**		+0.3%
7:30 am	Retail Sales Ex-Auto – Sep	-0.1%	**-0.2%**		-0.3%
7:30 am	Import Prices – Sep	-1.1%	**-0.2%**		-1.0%
7:30 am	Export Prices – Sep	-1.0%	**+0.2%**		-1.6%
9:00 am	Business Inventories – Aug	+0.9%	**+0.8%**		+0.6%
9:00 am	U. Mich Consumer Sentiment - Oct	59.0	**59.0**		58.6