Weekly Commentary with Professor Jeremy J. Siegel

Time for a Rate Cut?

Monday, 7/8/2024

The employment report from last Friday, in my view, was weak. Although the headline number came in slightly above expectations, the composition was troublesome, with more than 110k jobs subtracted from the last two months and private sector jobs lagging. Furthermore, the unemployment rate ticked up to a three-year high of 4.1%. Normally, I don’t make much of this, but there is empirical evidence (first presented a number of years ago by Claudia Sahm, an American economist) that when the three-month moving average of the unemployment rate rises one-half percentage point from its 12-month low, the probability of a recession jumps to over 90%. Last Friday, the moving average did just that—the actual rate has risen 0.7 percentage points from its 3.4% low hit in January 2023.

Now, I do not predict a recession, but I am concerned about the slippage in growth. Last year, gross domestic product (GDP) growth far exceeded 2023 expectations, but this year growth is falling short. At the beginning of the year the Federal Reserve (Fed) predicted 2.1% growth, but the first quarter was around 1.5% and the second quarter, although it started out well, is now also running under 2%. Productivity looks dismal, as many of the large gains in payroll are in low productivity workers.

The Consumer Price Index (CPI) and Producer Price Index (PPI) reports coming this week will be important, as well as the trend in jobless claims. As noted, although the new unemployment claims are remaining below 240k, recent claims continue to set multi-year highs. Furthermore, money growth is very sluggish.

The Fed should tee up a rate cut at the July 31 meeting for September, and in fact should contemplate a cut at the next meeting if inflation behaves and the economy continues to slip.

The market is continuing on a bull run and, with the prospects of rate cuts, I believe may continue for a while. But the narrowness of the rally is bothersome. I said at the beginning of the year, that growth is trouncing value, and that trend would continue, probably until we get a rate cut. That prediction has proven right.

Glossary

Bull market: A market in which share prices are rising, encouraging buying.

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. Core CPI excludes food and energy costs.

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

Gross domestic product (GDP): The sum total of all goods and services produced across an economy. Real GDP is adjusted for price changes.

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