Furstenau Wealth Update
May 01, 2023

The Markets

Get real!

Despite more than a year of aggressive Federal Reserve rate increases, the United States economy is still growing, albeit more slowly. U.S. gross domestic product (GDP) – the value of all goods and services produced in the U.S. economy – grew by 5.1 percent over the first quarter.

You may have read or heard that *real* GDP increased by 1.1 percent over the first quarter. That is also true. In economics, "real" means the value of something after inflation (inflation is the rate at which prices are increasing). For example:

- A *real* return on an investment is the return after inflation has been subtracted. So, if an investment earns 7 percent and inflation is 4 percent, the real return in 3 percent.

- *Real* growth in personal income is income after changes in the cost of goods and services are considered. For example, if personal income increases by 5 percent, from $50,000 to $52,500, and inflation is 4 percent, the real increase in income is 1 percent.

- In the first quarter, *real* GDP was lower than GDP because real GDP reflects price changes – and prices have been moving higher.

Last week, the Personal Consumption Expenditures (PCE) Index, which is one of the Federal Reserve's preferred measures of price increases, showed that inflation generally continued to trend lower.

- **Headline inflation** was 4.2 percent in March, year-over-year, down from February when it was 5.1 percent.

- **Core inflation**, which excludes food and energy prices, was up 4.6 percent, year-over-year, down slightly from February when it was 4.7 percent. However, month-over-month, core inflation remained unchanged.

Inflation and Fed rate hikes have had less impact on company earnings than analysts anticipated. To date, 53 percent of companies in the Standard & Poor's 500 Index have reported results for the first quarter and almost 8 of 10 have reported that earnings per share was higher than expected. Overall, S&P 500 earnings are expected to dip in the first quarter before increasing later in 2023, reported John Butters of *FactSet*.

Last week, major U.S. stock indices finished the week higher, according to Nicholas Jasinski of *Barron's.* Yields on U.S. Treasury notes and bonds moved lower last week.

Data as of 4/28/23	1-Week	YTD	1-Year	3-Year	5-Year	10-Year
Standard & Poor's 500 Index	0.9%	8.6%	-2.8%	13.3%	9.5%	10.1%
Dow Jones Global ex-U.S. Index	-0.2	7.3	0.7	7.7	-0.1	1.8
10-year Treasury Note (yield only)	3.5	N/A	2.9	0.6	2.9	1.7
Gold (per ounce)	0.5	9.4	5.0	5.4	8.6	3.1
Bloomberg Commodity Index	-1.2	-7.5	-19.3	20.5	3.1	-2.4

S&P 500, Dow Jones Global ex-US, Gold, Bloomberg Commodity Index returns exclude reinvested dividends (gold does not pay a dividend) and the three-, five-, and 10-year returns are annualized; and the 10-year Treasury Note is simply the yield at the close of the day on each of the historical time periods.
Sources: Yahoo! Finance; MarketWatch; djindexes.com; U.S. Treasury; London Bullion Market Association.
Past performance is no guarantee of future results. Indices are unmanaged and cannot be invested into directly. N/A means not applicable.

WHY IS INFLATION SO STUBBORN? Inflation is proving to be almost as stubborn as an angry two-year-old determined to eat popsicles for breakfast. Many have pointed to the tight labor market as the reason prices continue to rise. While labor costs are an important factor, there are other issues at play, too.

When the national news reports on a shock – the war in Ukraine affecting food supplies, the pandemic affecting supply chains, bird flu producing an egg shortage, or a dairy farm explosion affecting the price of milk – companies may take the opportunity to raise prices because customers are less likely to complain about the increase, reported Tracy Alloway and Joe Weisenthal of *Bloomberg*.

Companies in an industry, such as soft drink makers or chicken wing restaurants, may raise prices in tandem, giving consumers little choice but to pay the higher price. When the shock is resolved and wholesale prices move lower, companies often don't lower retail prices. Instead, they simply keep prices high.

Isabella Weber and Evan Wasner at UMass Amherst listened to earnings calls, compiled data on companies, and reviewed literature about corporate price-setting. Their research paper reported that overlapping emergencies in recent years have allowed companies to increase prices and profits. They dubbed the phenomenon "sellers' inflation". They wrote:

"Sellers' inflation is not possible in a perfectly competitive economy, but in a highly concentrated economy in which large firms are price makers, it is a real possibility – as we are witnessing again today."

Sellers' inflation may be another reason inflation has been sticky.

In theory, a recession and falling consumer demand should cause companies to lower prices. However, as Weber and Wasner pointed out, recessions have the potential to hurt smaller businesses, if they have difficulty finding funding, and increase the power of larger ones.

Weekly Focus – Think About It
"Character is like a tree and reputation like a shadow. The shadow is what we think of it; the tree is the real thing."
—Abraham Lincoln, former U.S. President

Best regards,

Ryan D. Furstenau

P.S. Please feel free to forward this commentary to family, friends or colleagues. If you would like us to add them to the list, please reply to this email with their email address and we will ask for their permission to be added.

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* Corporate bonds are considered higher risk than government bonds but normally offer a higher yield and are subject to market, interest rate and credit risk as well as additional risks based on the quality of issuer coupon rate, price, yield, maturity, and redemption features.
* The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general. You cannot invest directly in this index.

* All indexes referenced are unmanaged. The volatility of indexes could be materially different from that of a client's portfolio. Unmanaged index returns do not reflect fees, expenses, or sales charges. Index performance is not indicative of the performance of any investment. You cannot invest directly in an index.
* The Dow Jones Global ex-U.S. Index covers approximately 95% of the market capitalization of the 45 developed and emerging countries included in the Index.
* The 10-year Treasury Note represents debt owed by the United States Treasury to the public. Since the U.S. Government is seen as a risk-free borrower, investors use the 10-year Treasury Note as a benchmark for the long-term bond market.
* Gold represents the 3:00 p.m. (London time) gold price as reported by the London Bullion Market Association and is expressed in U.S. Dollars per fine troy ounce. The source for gold data is Federal Reserve Bank of St. Louis (FRED), https://fred.stlouisfed.org/series/GOLDPMGBD228NLBM.
* The Bloomberg Commodity Index is designed to be a highly liquid and diversified benchmark for the commodity futures market. The Index is composed of futures contracts on 19 physical commodities and was launched on July 14, 1998.
* The DJ Equity All REIT Total Return Index measures the total return performance of the equity subcategory of the Real Estate Investment Trust (REIT) industry as calculated by Dow Jones.
* The Dow Jones Industrial Average (DJIA), commonly known as "The Dow," is an index representing 30 stock of companies maintained and reviewed by the editors of The Wall Street Journal.
* The NASDAQ Composite is an unmanaged index of securities traded on the NASDAQ system.
* International investing involves special risks such as currency fluctuation and political instability and may not be suitable for all investors. These risks are often heightened for investments in emerging markets.
* Yahoo! Finance is the source for any reference to the performance of an index between two specific periods.
* The risk of loss in trading commodities and futures can be substantial. You should therefore carefully consider whether such trading is suitable for you in light of your financial condition. The high degree of leverage is often obtainable in commodity trading and can work against you as well as for you. The use of leverage can lead to large losses as well as gains.
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* Consult your financial professional before making any investment decision.

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