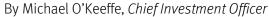
MARKET SIGHT LINES



The Consumer Remains Strong: Good News Is Bad News ... Again







Consumption makes up about two-thirds of GDP, so we monitor the consumer regularly as one way to keep tabs on the health of the economy. And while we are all on "recession watch," given the Federal Reserve (Fed)'s hawkish monetary policy and related higher interest rates, recent data shows the consumer remains strong. The economy may therefore be holding up, but as has been the case over the last year or so, this "good news is bad news," as a strong consumer gives the Fed room to push its hawkish policy further. Even higher rates should slow the economy further and serve as a headwind for earnings, and stocks have traded lower recently as a result.

In this week's Sight|Lines, we share an update on the strong job market, improving consumer confidence, and consumer activity and their possible influence on Fed policy.

THE TAKEAWAY: 2023 HAS BEEN GOOD FOR JOBS, SENTIMENT, AND SPENDING ... SO FAR.

In some ways, consumption is the result of a "cause and effect" progression for the consumer. A strong job market supports higher wages, higher wages improve confidence/sentiment, and more money, with improved confidence/sentiment, fuels more spending. In summary:

- The job market in February remained firm, with unemployment coming in at 3.6%, for example.
- While a more negative sentiment index improved in February, a more positive confidence metric retreated.
- Retail sales rose 3% in January, more than offsetting declines in November and December.
- In his semiannual congressional testimony, Fed Chair Jerome Powell signaled that the Fed could accelerate its rate hikes, moving higher than previously thought, causing the stock market to decline.
- Higher rates could be just the thing to slow the consumer down, perhaps soon.

IN-DEPTH: JOBS, WAGES, SENTIMENT, AND SPENDING ARE ALL INTERRELATED, THESE INFLUENCE THE FED, AND THE FED SETS THE TONE FOR THE FUTURE.

The data in 2023 reinforces the relationships between the job market, wages, confidence/sentiment, and spending. And all of these, especially jobs, are influencing Fed policy. Going deeper:

- The job market in February remained firm:
 - Unemployment came in at 3.6%, still low by historical standards.
 - Nonfarm payrolls were 311,000, with market expectations for a rise of 225,000.
 - The ratio of the number of unemployed to the number of job openings came it at 1.8, still quite high by historical standards.



- The annual growth of average hourly earnings on a yearly basis was 4.6%, but the monthly rate declined from 0.3% to 0.2%.
- February's sentiment and confidence measures showed mixed but modest improvements:
 - University of Michigan sentiment was higher at 67.0 from 64.9 in January, the highest level in a year.
 - The more positive Conference Board consumer confidence fell to 102.9 from 106.0 in January:
 - The Present Situation Index, which reflects the consumer's assessment of the <u>current</u> business and labor market, rose to 152.8 from 151.1.
 - The Expectation Index, which reflects the consumer's short-run outlook for income, business, and the labor market, fell to 69.7 from 76.0. It has been below 80 in 11 of the last 12 months, a reading often associated with a recession.
- Retail sales were strong in January, reversing a negative trend late last year:
 - Retail sales jumped 3.0% in January and were up 6.4% over the prior 12 months, more than offsetting declines of 1.1% in both November and December.
 - Broadly strong sales were led by a rise in motor vehicle, food, furniture, and electronics sales, and department store sales were positive too.
- In his semiannual congressional testimony, Fed Chair Jerome Powell signaled that the Fed could accelerate its rate hikes, moving higher than previously thought:
 - Said Powell, "The latest economic data have come in stronger than expected, which suggests that the ultimate level of interest rates is likely to be higher than previously anticipated."
 - As measured by the S&P 500, stocks had risen 9% through February 2 on optimism the Fed may pause its rate hikes but have fallen 6.1% since then on worries the Fed may go higher for longer.
- Higher rates could be just the thing to slow the consumer down, perhaps soon.
 - As mentioned above, the Conference Board consumer confidence report shows the consumer is feeling good at the moment but worried about the near-term future.
 - Higher rates may dampen consumer sentiment and spending, just what the Fed may be looking for to bring inflation down.

CONCLUSION

Consumption is a big part of GDP, so the consumer is important. When it comes to jobs, confidence/sentiment, and spending, 2023 has been pretty good for the consumer. But this "good news is bad news," as a resilient consumer gives the Fed confidence to take rates even higher, an action that can slow the economy and dampen earnings. This policy shift could be the consumer's undoing.

Michael P. O'Keeffe, CFA Chief Investment Officer

michael.okeeffe@stifel.com www.stifelinsights.com



The information contained herein has been prepared from sources believed to be reliable but is not guaranteed by us and is not a complete summary or statement of all available data, nor is it considered an offer to buy or sell any securities referred to herein. Opinions expressed are subject to change without notice and do not take into account the particular investment objectives, financial situation, or needs of individual investors. There is no guarantee that the figures or opinions forecasted in this report will be realized or achieved. Employees of Stifel, Nicolaus & Company, Incorporated or its affiliates may, at times, release written or oral commentary, technical analysis, or trading strategies that differ from the opinions expressed within. Past performance is no guarantee of future results. Indices are unmanaged, do not reflect fees or expenses, and you cannot invest directly in an index.

Asset allocation and diversification do not ensure a profit and may not protect against loss. There are special considerations associated with international investing, including the risk of currency fluctuations and political and economic events. Investing in emerging markets may involve greater risk and volatility than investing in more developed countries. Due to their narrow focus, sector-based investments typically exhibit greater volatility. Small company stocks are typically more volatile and carry additional risks, since smaller companies generally are not as well established as larger companies. Property values can fall due to environmental, economic, or other reasons, and changes in interest rates can negatively impact the performance of real estate companies. When investing in bonds, it is important to note that as interest rates rise, bond prices will fall. The Standard & Poor's 500 index is a capitalization-weighted index that is generally considered representative of the U.S. large capitalization market. The Dow Jones Industrial Average (DJIA) is a price-weighted average of 30 significant stocks traded on the New York Stock Exchange (NYSE) and the NASDAQ. The DJIA was invented by Charles Dow back in 1896. The MSCI EAFE index (Europe, Australasia, and the Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the U.S. and Canada. VIX is a trademarked ticker symbol for the Chicago Board Options Exchange Market Volatility Index, a popular measure of the implied volatility of S&P 500 index options.

Stifel, Nicolaus & Company, Incorporated | Member SIPC & NYSE | www.stifel.com

0323.5503547.1

