FLD Connection

AUGUST 2022

SUMMER ISSUE

Happy Summer!

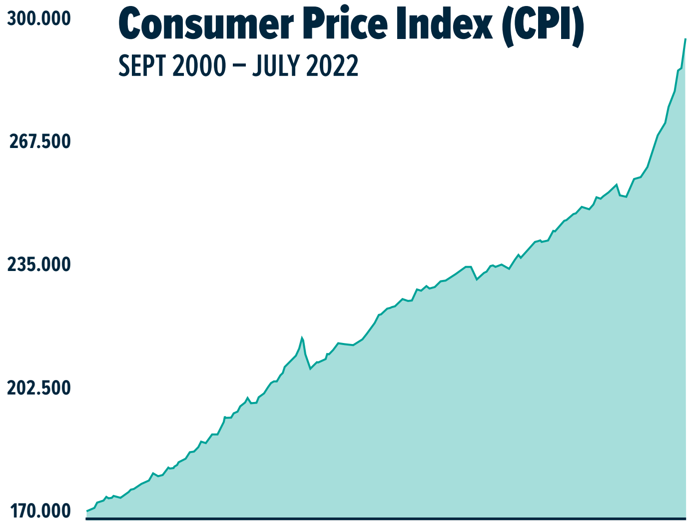
Summertime brings a different energy to the air... BBQ's, vacations, backyard fun, home improvement projects, and being outdoors. We hope you are enjoying the summer with family and friends.

Recently, we had our FLD summer employee appreciation BBQ to express our gratitude and appreciation to our associates, Angela Leingang and Julia Mottet. Check out the recipe section for some highlights from the BBQ.

We hope you enjoy the Summer 2022 edition of the FLD Connection. Soak up some sun, and we'll see you again in the fall!

ECONOMIC COMMENTARY
THE TIMES THEY ARE A-CHANGIN'

by James Pafundi



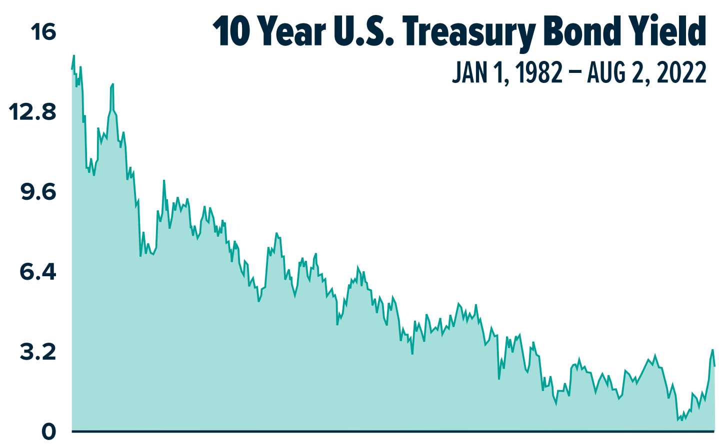
At their most recent meeting, the Federal Open Market Committee (FOMC) raised rates an additional ¾ of a percent, increasing short-term rates to 2.25%. With that announcement, the 10 year US Treasury dropped in yield from 3% to 2.9%. Yes, you read that correctly... The Fed raised short-term interest rates and 10 year rates declined. Why? Because the bond market takes Chairman Powell at his word. The Fed will continue to raise rates as long as inflation is running above the Fed's stated CPI goal of 2.7%. The last CPI print was at a 40-year high of 9.2%. That's a pretty big difference.

This seemingly counter-intuitive action of the bond market means investors are expecting Fed policy to create a recession sometime in the near future. In fact, according to the Fed's own data, we are in a recession now. Powell was specifically asked about the bond market's expectation of rate cuts in 2023, had an opportunity to push back on the idea that rate cuts were coming (recession), and he didn't. In fact, he stated that "full employment," (one of the two mandates of the Federal Reserve), "may not be compatible with the current inflation environment." Let me interpret the Chairman's comments: "We may have to raise rates enough to cause a recession (in order to reduce demand) and therefore inflation." But here's the rub: Just because there is lower demand, does that mean inflation goes down? Not always. The economic cycle characterized by lower GDP and high inflation is known as "Stagflation."

THE WORLD UP UNTIL YESTERDAY

One of the defining characteristics of our more globalized economic environment over the past 40 years has been a lowering of bond prices and lower historical inflation. Capital was able to freely move around the world, finding the very lowest costs for production and manufacturing. This meant lower costs for goods here in the US and around the world. The last many decades brought us no major global military conflicts, relatively stable political regimes around the world, a stable reserve currency for cross-border transactions, a hyper-efficient "just-in-time" supply chain, an increasing global population, major efficiency and production gains due to ever-faster advances in technology, and the better, cheaper, faster supply of goods... Each of these aspects put downward pressure on inflation for a very long time... since 1982 to be exact.

But since the beginning of Covid, a lot of the world as it has existed, has changed or is in the process of changing. And what's even more impressive? The speed at which significant change is taking place seems to be accelerating. If the global order is changing and reduced supply creates a generally higher inflationary regime, then it might be a good time to review our history. Here is a brief overview of the last two times that happened post WWII:



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70'S STAGFLATION – *CONT'D FROM PAGE 1*

Starting around 1970, baby boomers began reaching working age, entering into the workforce en masse, buying homes and starting families. Demand for just about everything rose significantly. Around the same time, President Nixon took America off the gold standard, removing the Dollar peg, allowing the currency to float. Inflation started to rise significantly, prompting the Fed to raise interest rates. In 1973, the stock, bond, and commodities markets turned very negative and dropped by almost 50% due to recession expectations. Inflation began to subside. But then something interesting happened... Inflation came roaring back. Financial assets, such as stocks and bonds, continued to suffer due to higher rates, but commodities exploded higher, regaining previous highs and then a lot more. The boomer generation was such a large cohort of new consumers that even with higher prices, demand, and therefore inflation, continued to increase. Then OPEC decided to flex their collective muscle and reduced the supply of oil in what was known as the OPEC Oil Embargo. Faced with increasing inflation, the Fed kept raising rates all the way to 20% in 1980.

Depending on how much you liked the 70's, some of you may be relieved to know that I do not believe we are in a similar macroeconomic environment. Why? No generation of young people like the baby boomers entering the work force en masse. In fact, according to recent data, the total number of workers is actually shrinking. The millennial generation has also been slow to mature financially. Baby boomers, the largest, wealthiest generation, is also retiring or thinking about retiring. The demand side of the equation is just not there.

40'S STAGFLATION

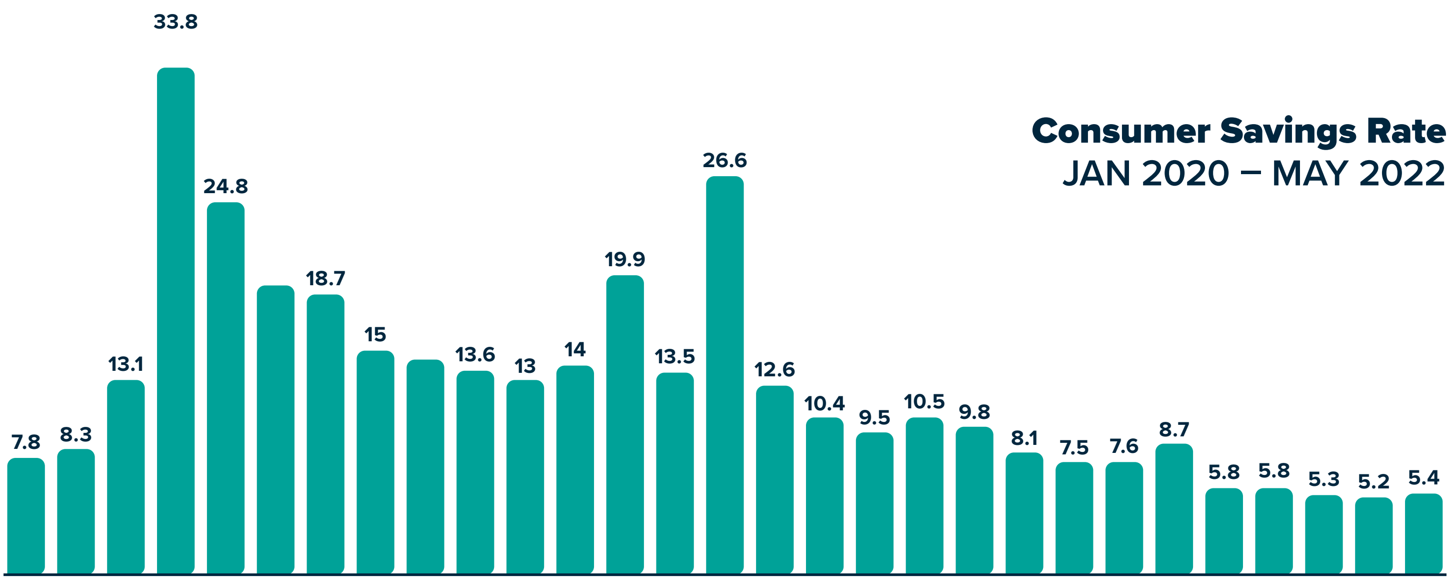
The other stagflationary time in the last 100 years? 1946. Replace WWII Germany and Japan with Covid and the current environment starts to look a lot like the immediate post-war period: The world's supply chains were non-existent due to major bombing in Europe and Asia (similar to global supply chains shut down due to Covid), the U.S. Dollar became the global reserve currency (same as today), federal government deficit spending was off the charts to finance the war (like deficit spending for Covid stimulus), industry was converted to the production of military equipment and supplies, leading to a lack of spending opportunities (lockdowns and the fear of getting sick kept a lot of discretionary spending on the sidelines which led to increased savings) and when the GI's returned and the war was over, demand for goods and services went through the roof (similar to 2021, when Covid vaccines became widely available and a better understanding of Covid's health risks to the general population led to a rapid and sustained uptick in demand for both goods and services).

But in the 40's, the Central Bank did not raise rates. They let inflation run high because of all the supply issues after the war. There was also a lot of political cover for the Fed to not raise rates and to allow a recession... "Hey, everyone, you did a great job with war and all, but now you are going to have to deal with a recession." Over the next few years, supply was re-established, inflation came down to normal levels, and a balanced economic environment returned. Is something similar going to happen now? It could very easily.

Conclusion:

Right now, it's still too early to know if we are in a stagflationary environment. While the economy has slowed down quickly due to the rise in rates, that might be reversed rapidly, too, if the Fed stops raising rates or begins to ease. Supply chains in Asia have been shut down due to Covid, but that could reverse swiftly as well. Potential negotiations in the Russia/Ukraine war may be on the table shortly... The energy concerns, especially in Europe, would mitigate quickly. All of these things, currently contributing to the slowing economy and higher inflation could quickly reverse the economy's direction, and therefore, the markets. But if supply chains worsen, inflation will remain high, the Fed may be forced to raise aggressively. Things may have to get worse before they can get better.

Upper Earners Hold Most Savings On Hand - Consumer Behavior



Consumer Savings Rate
JAN 2020 – MAY 2022

Consumers are now saving less than before the pandemic, as stimulus assistance funds and generous unemployment benefits have gradually evaporated, encouraging consumers to tap their savings at an accelerating pace. The drop in savings has been especially prolific for those nearing retirement. As markets have pulled back, so have retirement fund values, elongating the retirement threshold for many.

Savings rates rose dramatically in 2020 as billions of dollars in stimulus relief payments made their way into consumer accounts. Federal Reserve data found that households spent only 40 percent of their payments, used 30 percent to pay down debt, and saved about 30 percent on the initial round of stimulus payments. The spectacular rise in the savings rate to nearly 34 percent in April 2020 was a validation of how much of the payments went towards savings.

As additional relief programs along with generous unemployment benefits became effective, the savings rate remained elevated through the end of 2021. The most recent data show that the savings rate dropped to 5.4 percent in May 2022, lower than where it stood at roughly 7.5 percent before the pandemic began.

A Fed analysis found that lower-income households tend to spend most if not all of their income and end up having very little disposable income at the end of each month. Most lower-income households have already depleted their pandemic surplus funds in savings and are also being squeezed by inflation as food and energy prices continue to escalate. This has led to upper-income earners holding the most savings on hand, while lower-income savings begin to dwindle.

Source: *U.S. Bureau of Economic Analysis, St. Louis Federal Reserve Bank, Marginal Propensity to Consume Working Paper; Federal Reserve Bank of Boston*

Book Corner

by James Pafundi

JFK and the Unspeakable

Why He Died and Why It Matters

By James W. Douglas

Recently, with what has been going on in Ukraine, there has been talk of Putin possibly using nuclear weapons. It made me start thinking about the last time the world was on the brink of a nuclear exchange... The Cuban Missile Crisis. Kennedy was tasked with knowing that he risked committing the greatest crime in human history: Starting a nuclear war.

The book details the inner goings-on in the Oval Office and Kennedy's gradual turning away from his warrior beliefs and towards establishing a lasting peace with the former Soviet Union. This turn towards Khrushchev was a direct threat to the military and intelligence agencies who were committed to winning the Cold War. Was this the reason for his assassination? This read makes a compelling argument that it was.

What Falling Labor Productivity Means

Labor Market Overview

The most recent data released by the Labor Department revealed the largest quarterly drop in productivity since 1947, decreasing at an annualized rate of 7.5%. The drop in productivity was concurrent with the largest rise in labor costs since 1982. Both of these measures are also indicators of inflationary pressures for both companies and consumers. Many companies have been passing along higher costs to consumers, but can only do so for so long until competition forces companies to hold prices steady and absorb higher costs. This can also lead to decreased levels of hiring and lower wages as companies struggle to maintain profitability levels.

Data surrounding labor during the pandemic has been considered unreliable and inconsistent by many economists, meaning that the true effects of the COVID-19 pandemic and worker retention are still not certain. An essential data set is labor productivity, which is a measure of how efficiently companies are utilizing workers to produce products and services. This year, the largest four-quarter drop in labor productivity was observed since the fourth quarter of 1993 according to the Bureau of Labor Statistics, marking a historic decline in productivity.

Federal Reserve survey results, reported in the Fed's Beige Book, have identified that a growing number of manufacturers and industrial companies are increasingly moving towards automation, replacing previously desired workers with robotic gear. Rising wages and a dwindling labor pool have forced some companies to resort to machines instead of hiring workers.

Source: *Labor Department, Federal Reserve Beige Book; https://www.federalreserve.gov/monetarypolicy/files/BeigeBook_20220601*

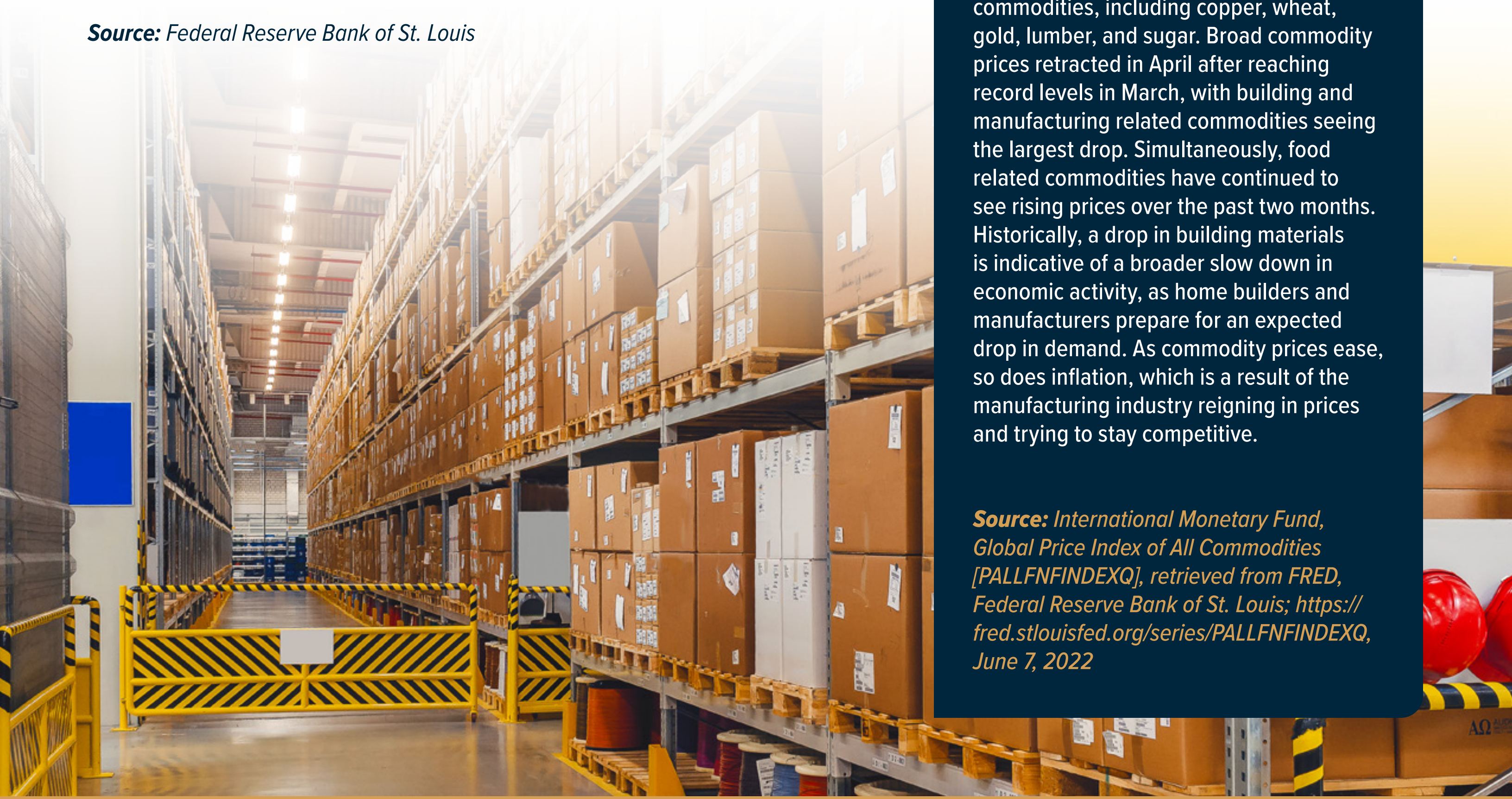
Growing Inventories Means Lower Prices & Discounts Could Be Coming - Consumer Retail

As the pandemic created supply constraints over the past two years, companies learned to stock up on materials and finished products in hopes of alleviating any future supply chain snags.

Now that constraints have lessened and various supply chains have resumed operations, companies have been accumulating raw materials and building a stockpile of finished products at an incredibility fast pace.

Historically, increases in inventory levels for companies is seen as an indication that demand for their goods might be weaning due to a pullback in business and consumer demand. As inventories swell, companies are eager to reduce stockpiles by discounting, which ultimately means lower prices for consumers.

Source: *Federal Reserve Bank of St. Louis*



Global Commodity Prices May Be Signaling That Inflation Is Taming - Commodities Market Update

As heightened commodity prices have stoked inflation over the past year, commodity prices worldwide are now starting to ease as demand for various commodities are alleviating.

The Global Price Index of All Commodities tracks the price of widely traded commodities, including copper, wheat, gold, lumber, and sugar. Broad commodity prices retracted in April after reaching record levels in March, with building and manufacturing related commodities seeing the largest drop. Simultaneously, food related commodities have continued to see rising prices over the past two months. Historically, a drop in building materials is indicative of a broader slow down in economic activity, as home builders and manufacturers prepare for an expected drop in demand. As commodity prices ease, so does inflation, which is a result of the manufacturing industry reigning in prices and trying to stay competitive.

Source: *International Monetary Fund, Global Price Index of All Commodities [PALLFNFINDEXQ], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/PALLFNFINDEXQ, June 7, 2022*

What's Cooking?

by Gina Pafundi

Have I mentioned before that I love to cook?! I cannot think of a better way to express my gratitude and appreciation than to cook a meal for the people that are important to me. Recently, we had our FLD summer BBQ to honor Angela and Julia. I made them this recipe. They both add so much to our company, and we appreciate all they do. It was such a nice gathering. We visited, played corn toss, enjoyed the summer sun and we ate cake too! This is one of my favorite summertime BBQ recipes. It goes well with pita or naan bread with hummus! I served it with naan bread, hummus, veggie kabobs and basmati rice. It was delicious!

Persian Chicken Kabobs

Serves 6-8

Ingredients:

- 4-5 pounds of chicken breast or thighs
- 2 cups mint
- 2 cups cilantro
- 2 cups parsley
- 1 cup lime juice
- 1 cup Extra Virgin olive oil
- 1 tsp saffron
- 1 tbs salt
- 1 tbs pepper

Directions:

If using wood skewers, soak them in water for at least 30 minutes before grilling.

Make the herb marinade. In a large bowl or food processor chop and combine mint, cilantro, parsley, lime juice and olive oil. Add saffron salt and pepper. Cut chicken into kabob size chunks for skewers.

In a large bowl, mix herb marinade with chicken. Combine well. Marinate several hours or overnight if possible. Skewer the chicken on the kabob sticks and grill on BBQ. You can serve with veggie kabobs and basmati rice!

FINANCIAL LIFE DIMENSIONS
1516 Hudson Street, Suite 202
Longview, Washington 98632

Travel & Adventure

Build Your Life Resume: "Driveway to Hell"

by Gina Pafundi

I am always looking for ways to learn, grow and take on new challenges. In 2021, I joined a coaching club called Build Your Life Resume®, led by Jesse Itzler. The foundation of the club is putting effort into building our "Life Resume" through challenging ourselves to try new things and prioritize what matters most in our lives. At its root, the club provides a roadmap for living life to the fullest. There are weekly motivations, speakers, and a community of positive people with which to share it all.

This year, Jesse offered an overnight challenge called "Driveway to Hell" to run/walk a half marathon on his driveway at his home in Rome, Georgia. Of course, I had to go, and James joined me. The event was part camping trip, part community get-together & retreat, plus the unbelievable challenge of walking up and down the driveway for 13.1 miles! I swear Jesse must live on one of the only hills in Georgia, because it was a total elevation gain and loss of about 6,000 feet. Jesse spared no detail.... he brought in ice baths, saunas, wonderful healthy food, and some great motivational speakers. I also got to meet Jesse's wife Sara Blakely, inventor of SPANX. It was an incredible 24 hours!

I finished 12 of the 13 miles in the five hours we were given to finish, which for me is a major accomplishment. I would have finished the last mile if it were not for the time constraint. It was a difficult challenge, but I did it to remind myself of what I am capable of as a human being! My wonderful husband accompanied me on the last 2 miles after he finished his 13! Incredible how someone's driveway can be an adventure! It was a great experience for "my life resume."

