Why Are Investors in a "Sticky Situation"?

The S&P 500 (SPY) seems to be going trading in a fairly tight trading range. Yet there are more facts emerging that would lead one to a bearish conclusion. That includes the discussion of Sticky Inflation. You may not have thought much about that…but let me assure you that is Public Enemy #1 for the Fed. Read on below to understand how Sticky Inflation is increased the odds of bear market downside in the weeks ahead.

Earlier this week I shared an important proclamation that I was getting more bearish. The reasons for which are clearly spelled out here.

One of the key points is that inflation is still too high which is why the Fed is still slamming on the brakes of the economy with their hawkish regimen. This may be hard for some to see who point to a great reduction in gas prices as proof the inflationary beast has been tamed.

Unfortunately, we still have a "*sticky*" situation at hand thanks to sticky inflation. Let's dive into this too little discussed subject to appreciate why the odds are pointing more bearish in the weeks ahead.

Market Commentary

The conventional view of inflation is to watch the movement of the Consumer Price Index (CPI). See below the clear and steady decline of that key measure over the past year:

That is serious and consistent improvement that gives some the sense that we don’t need to do that much more to coast down to the Fed’s stated 2% inflation target. This is why so many investors keep betting on a Fed pivot to let off the brakes and start lowering rates.

THAT IS NOT GOING TO HAPPEN ANY TIME SOON!

First, because the Fed keeps repeating that rates will not be lowered this year. This happens at every single Fed announcement much to the chagrin of investors who oddly suspect they will change their tune by September. I almost feel like Powell wants to say things like “*Read my lips*” or “*Did I stutter?”.*

Second, and more importantly, because the Fed is basing their decisions on sound logic. That being that there is more to the inflation equation than just CPI. And that not all inflation elements are made equal.

Enter the Conversation About "Sticky Inflation"

The Atlanta Fed leads this effort to break up the CPI report into 2 sub indices:

- Flexible CPI (where prices change quickly)
- Sticky CPI (where prices change slowly)

As you will see in their most recently updated chart below, overall inflation may be down, but Sticky inflation is stubbornly high at +6.5% year over year (yes, even more than the +4.9% CPI reading).

Below is a good summary of what is in each sub index. But for simplicity the majority of the problem in Sticky Inflation comes from housing/shelter (OER below), medical services, recreation & restaurant prices.

Plain and simple, the Fed is on a mission to stamp out inflation. And no matter what some investors think they see in the improvement of CPI or gas prices…they are not economists and don't appreciate the totality of the inflation story.

Now let's remember that Fed officials are indeed economists and academics who fully understand these intricate concepts. They absolute see and understand the problem with sticky inflation and are firmly planning to eradicate it which is why rates will stay high through years end…*or even longer.*

And yes, the Fed is FULLY aware that this likely will create a recession. In fact, that is still their base case by years end. (This concept is the cornerstone of my argument for becoming more bearish as shared in my recent commentary).

This brings us back to the importance of being vigilant on our recession watch as more signs of that becoming a reality will wake the bear from hibernation leading to new stock lows. The key to the recession watch has been employment which has been incredibly resilient.

The leading indicator of the monthly Government Employment Situation report is the weekly Jobless Claims report every Thursday. As you will see in the chart below this has been ticking up little by little over time. The key for most is if it reaches 300,000+ per week which is usually a sign that the unemployment rate is about to rise.

Jumping of the chart above is the 10% week over week spike in claims to 264,000. So this indicator is not in troubling territory yet, but directionally we are getting closer to the point where unemployment may rise, which would most certainly sound more recessionary alarms…and get stocks moving lower.

How Does This Affect Our Trading Plan?

Let me borrow some key statements from my 5/9/23 Reitmeister Total Return commentary which applies just as well here.

"My recommendation is to stay balanced (bullish/bearish) like we are doing in Reitmeister Total Return until the recession

starts to rear its ugly head. That because there have been many false recessionary alarms over the past 15 months that did not come to fruition leading to a rise in stock prices.

Your best bear trading signal is when the market finally cracks below the 200 day moving average (currently at 3,975). From there a bearish FOMO rally should kick in with 10-20% more downside to eventual bottom.

Why not shift more bearish now?

Because if only 65% certain of bearish outcome…that means I still see a 35% chance that recession and deeper bear does NOT happen. So, we want more of the cards to be put on the table before we make a deeper bearish bet."

What To Do Next?

Discover my balanced portfolio approach for uncertain times. The same approach that has beaten the S&P 500 (SPY) by a wide margin in recent months.

This strategy was constructed based upon over 40 years of investing experience to appreciate the unique nature of the current market environment.

Right now, it is neither bullish or bearish. Rather it is confused…volatile…uncertain.

Yet, given the facts in hand, we are most likely going to see the bear market coming out of hibernation mauling stocks lower once again.

Gladly we can enact strategies to not just survive that downturn…but even thrive. That's because with 40 years of investing experience this is not my first time to the bear market rodeo.

If you are curious in learning more, then please click the link below to start getting on the right side of the action:

Steve Reitmeister’s Trading Plan & Top Picks >

Wishing you a world of investment success!

Steve Reitmeister*…but everyone calls me Reity (pronounced “Righty”)*
CEO, StockNews.com and Editor, Reitmeister Total Return

SPY shares fell $0.59 (-0.14%) in after-hours trading Friday. Year-to-date, SPY has gained 8.04%, versus a % rise in the benchmark S&P 500 index during the same period.

About the Author: Steve Reitmeister

Steve is better known to the StockNews audience as “Reity”.

Not only is he the CEO of the firm, but he also shares his 40 years of investment experience in the Reitmeister Total Return portfolio. Learn more about Reity’s background, along with links to his most recent articles and stock picks.

More…

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