Ropes Wealth Sees Markets Taking a Hike This Summer

In today's news, U.S. job gains moderated in June while wage growth remained firm, showing a strong enough labor market to keep the Fed on track to raise interest rates this month. Nonfarm payrolls increased 209,000 — the smallest advance since the end of 2020 — after downward revisions of 110,000 jobs in the prior two months of data. Hiring was strongest in the health care, government, and construction sectors. The unemployment rate fell to 3.6%, while wage growth remained firm, up 4.4% from a year earlier.

The labor market may be losing some steam as high interest rates and months of sluggish consumer spending feed into concerns about an impending recession. Yet with sufficiently healthy job growth and brisk wage gains, the Fed likely has no choice but to resume its series of rate hikes at its meeting later this month, following their pause in June.

These mixed messages were evident in other key barometers released this week, with indices tracking economic activity showing manufacturing down and service sector activity up. However, service sector spending resilience might be at risk as additional threats to the consumer have emerged. One such threat is the burden of student debt on households in the aftermath of the latest Supreme Court ruling. In a 6-3 vote last week, the Supreme Court struck down the Biden administration's plan that would have extinguished $430 billion in loans. Once the moratorium on student debt expires on September 1, the average student loan payment will resume at a monthly cost of roughly $200-300. In total, according to Federal Reserve data, student debt stands at roughly $1.6 trillion with the average student loan debt around $38,000 per borrower.

That said, the Fed is intentionally trying to slow growth and reduce spending to tame inflation. As Federal Reserve Chairman Jerome Powell has said time and time again, "*Without price stability, the economy doesn't work for anybody.*"

This sentiment was echoed in the minutes of the June 14 FOMC meeting released this week as at least some committee members openly voiced concerns over inflation and a tight labor market as justification to continue to move forward with an 11th round rate hike. Even those officials in favor of a temporary halt last month noted that additional increases would likely be appropriate with most highlighting the need for clear communication of such a message. While the economy has been resilient in some respects, like the labor market, inflation remains too high, and as such, policy makers must reengage.

For this reason, bond markets have been shocked into consciousness, with two-year yields surging close to 5% and 10-year yields now above 4% for the first time since the March banking crisis began to unfold. With these moves, the stock market has also been rattled, suddenly anxious about the dual risks of recession and a more permanent higher term structure of interest rates. With earnings season upon us, markets will have much to digest in the weeks ahead. The expected contraction in earnings and profits will come through those reports and investors must reconcile them with valuations on stock prices no longer quite so compelling. This reality, combined with the dawning realization of the inevitability of a slowdown and the risk that the shape of that slowdown is indeed a recession, may cause volatility in the weeks ahead. As we have been urging for weeks, the best approach for this kind of environment is balance, keeping flexibility to cover cash needs while we work through these challenges but not abandoning your long-term plan. To borrow a phrase from Ernest Hemingway, risks tend to converge in a "gradually, then suddenly" way, and preparation is the best remedy to manage that cadence, so you don't lose sight of your goals.

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