DAVIS COMMODITIES LLC

August 2024 Macro Commentary

With another month of economic data behind us, the trend of overall softening in the labor force and inflation continues. The consumer price index (CPI) continues to fall and is down to 2.9% YOY vs last month at 3%. The data from the JOLTS (Job Openings and Labor Turnover Survey) continues to show a weakening in overall hiring. While jobless claims have yet to turn significantly higher, history shows that particular dataset to be severely lagging. By the time jobless claims climb rapidly, the economy is already in recession. While the slow realization of the softening data has been frustrating for the program, it finally feels like things are starting to move in our favor.

Today, September 6, the Bureau of Labor Statistics (BLS) released the non-farm payrolls. The headline change came in light at 142k vs the average estimate of 165k. In addition, the prior two months were revised lower by 86k jobs. However, the larger shock to the market was the release of benchmark revisions to employment from April 2023-March 2024. Those revisions indicate that the non-farm payrolls during that period was overstated by 818,000 jobs. That revision was the largest since the great financial crisis. More important than the magnitude of the change was the underlying data behind the change. The anomaly lies within the BLS birth/death model for new businesses. The model has been trying to track 2023 (for the most part) and pointing toward higher job creation and lower unemployment. In hindsight, with elevated interest rates, that model is in error. If one were to extrapolate the revisions forward, it is plausible that the August non-farm payrolls was actually negative instead of positive. With inflation continuing to fall and unemployment rising, the next move by the Fed is a cut to Fed Funds.

At this point, the question is not whether or not the Fed will cut rates later this month. The question is how much? The markets are currently pricing in 0.25% and a 50% chance of a 0.50%. With more inflation data coming before the Fed announcement on September 18, there is plenty of time for markets to change their collective mind. With the data currently in hand, my bias is that they will cut 50 basis points. However, whether they cut 25 or 50 is immaterial. Jerome Powell announced at the Jackson Hole conference that it is time to start cutting. The path forward for the short end of the curve is certainly down. Over time, it should allow for the steepening of the yield curve and benefit the position in the 2 year note vs. 10 year note.

With the impending rate cut narrative, I believe the program is positioned to take full advantage as we go into the last four months of the year.

Sincerely,

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