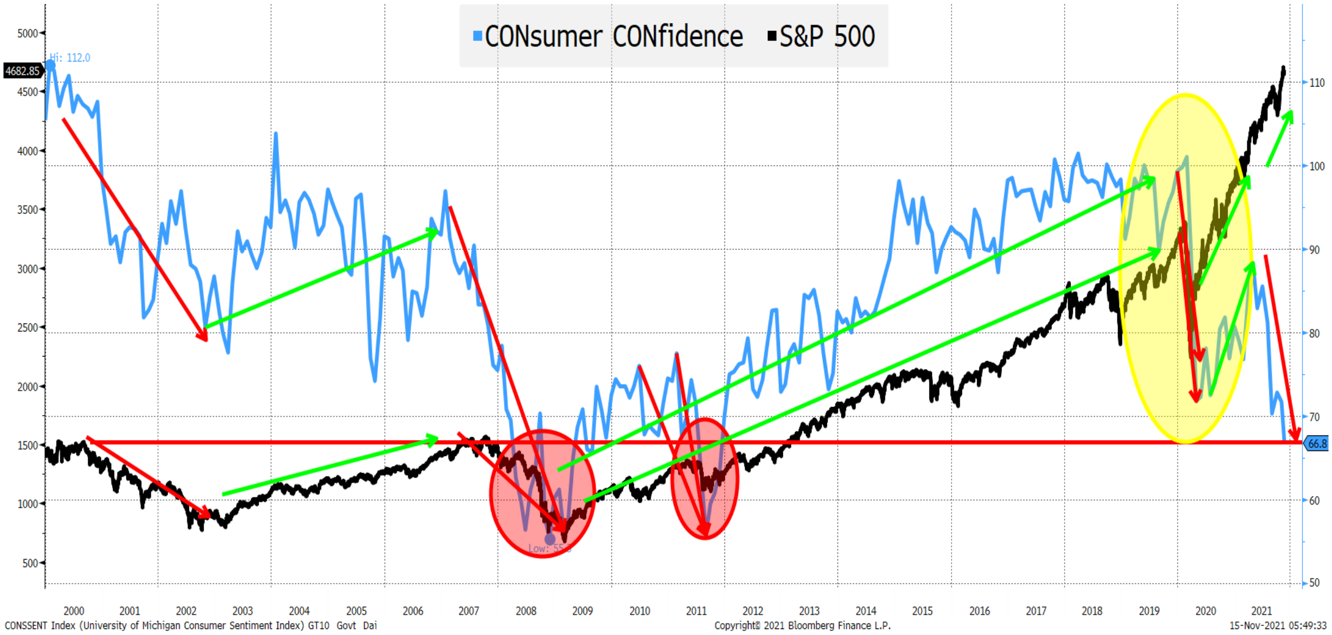
CONsumer CONfidence?

I must give Bob Janjuah, a strategist when I was trading CDS indices during the GFC, credit for putting the "CON" in consumer confidence. It is not a piece of data that I pay close attention to, at least in part because it seems to be a somewhat lagging indicator of how the stock market is doing. But Friday's print was so strange (and so completely at odds with other signs of behavior in the U.S.) that it has to be highlighted.

Consumer Confidence vs The S&P 500



If this was the only chart that you were able to look at, it would be difficult not to get concerned about either the market, the economy, or both.

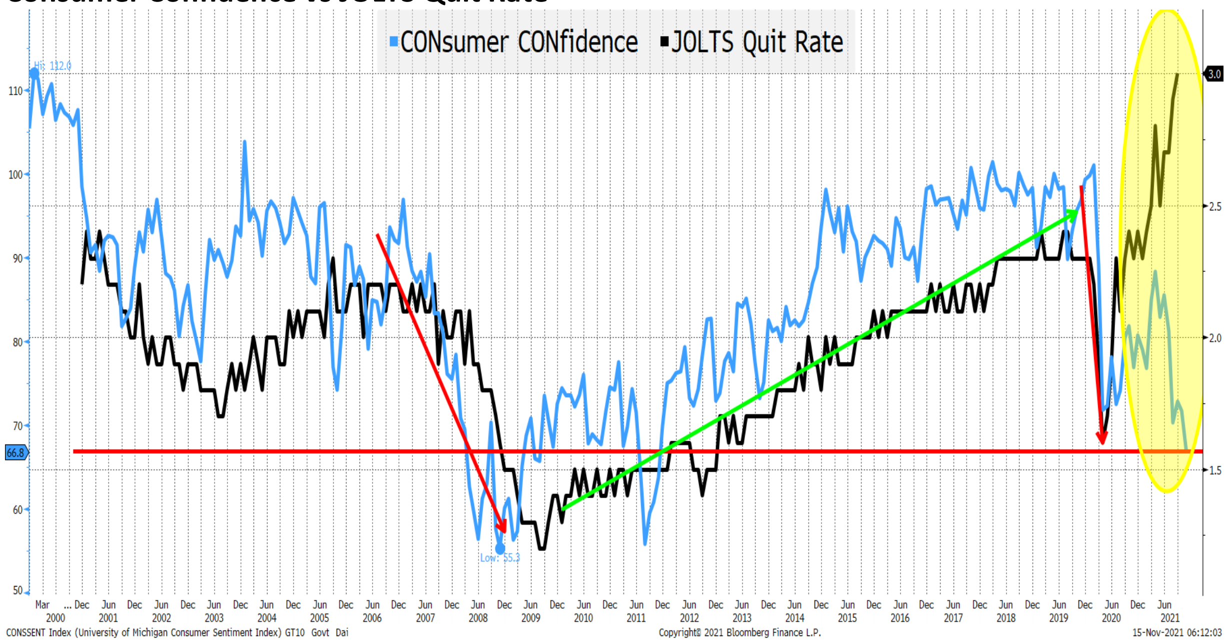
- **Consumer Confidence Is Lower Than at the Height of COVID Fear**. In March and April 2020, you could enter a highway with your eyes closed because no one was going anywhere. There were shortages of almost everything (from toilet paper to thermometers). People were dying and at that time, we knew relatively little about comorbidities, nursing homes, or age. Virtually every store and restaurant were closed and the "two weeks to slow the curve" became four weeks, then six weeks, and so on. The concept of a vaccine, was just that, a concept. Testing involved what seemed like shoving a 2-foot piece of wood into your brain and then waiting in fear for days for the results to come back. **And somehow, despite all that, how is consumer confidence lower today than it was then?**
- **In the past two decades, consumer confidence was only lower during the Great Financial Crisis and the European Debt Crisis.** I think that consumer confidence was weirdly low during the European Debt Crisis probably because the GFC was so fresh in everybody's mind, but it seems strange that consumer confidence is approaching those levels.
- **Stocks and confidence.** I won't overstate the correlation between these two because it is loose at best and probably spurious, but anecdotally they have been linked in the past and the divergence here is extreme.

Consumer Behavior

I'd be more worried if consumer behavior reflected that lack of confidence.

- **A record 4.4 million people quit their jobs in September.** By any metric, September took the "take this job and shove it" trend to a new level. What is weird is that it is **highly unusual for people to quit their jobs when they don't feel confident!** While correlating the stock market and consumer confidence may (or may not) be a stretch, the pattern with quits and confidence is more obvious. It is also very logical. If you feel confident about yourself and the economy, then you can afford to quit and find a new job. If you are worried, which is a valid interpretation of the consumer confidence numbers, then you would normally get into your bunker and prepare to ride out the problems.

Consumer Confidence vs JOLTS Quit Rate



- **Spending**. Everything I see and read talks about great consumer spending. Yes, it slowed since it peaked during the reopening, but it has been strong and consensus is for tomorrow's Retail Sales figures to be quite strong as well.

So, yes inflation is bad (and persistent) and weighing on consumer confidence, but it doesn't seem to be impacting behavior. Weird and worth exploring.

Plausible Explanations

There are some rational reasons why this could be the case. **Many of those reasons support the ongoing divergence**.

- **Signing Bonuses and More Pay.** There is so much chatter about workers getting signing bonuses, extra pay, etc., that they are quitting in droves to find new jobs (but that is difficult to link to such low levels of confidence).

- **The underground economy.** DoorDash, Uber Eats, etc., Maybe people are finding ways to earn money that doesn't show up in traditional metrics? Maybe they are making enough money doing this and they have money to spend, but they are dubious about how long it lasts? That could explain why there is a mismatch between actions and confidence.

- **Crypto (and gambling).** I mention gambling only because I spent a weekend at a college campus and was shocked at the number of gambling conversations. Also, because with weekly options dominating so many trading flows, it is impossible to argue that a gambling attitude hasn't had an impact on stock prices. Finally, crypto is interesting. **Part of the rise in crypto can be attributed to a lack of faith in existing institutions.** Making money from crypto (which is hovering around record highs) would explain the ability to spend and quit jobs, while at the same time, still have a lack of confidence in the country and the economy.
- **Making a Statement.** Consumer sentiment for Democrats was 87.0, Independents was at 71.7, and Republicans were at a staggeringly low 37.2. Maybe for a "survey" it is easy to say something to voice your displeasure, while back in the real world you find a new job and spend?

I am sure that there are other plausible reasons that would be positive, but there are also some explanations that would be more dangerous for the economy and markets.

- **Growing Inequality.** What if there is a group of people that is confident in themselves and the economy? Maybe they are job hopping and spending because, for them, things are great. What if there is a larger (but poorer) segment of the population that is becoming more disenfranchised? There is not a lot of evidence of this in the data that I looked at (though, for example, according to Household Finance, the higher income group has gone from 31 to 36 since August, while the lower income group has dropped from 21 to 16). The data that I glanced at wasn't cut-and-dried, but it has been a longer-term trend that may be accelerating in the current environment. That is a plausible explanation, but not one that gives a lot of comfort in the direction we are headed.
- **Jobs Rolling Over?** The JOLTS data was from September, so it was already old news when it was released. August was worse for Job Openings than July and September was worse than August. Yes, the number of jobs available is great, but the data is heading in the wrong direction. The October jobs report was good with 531k jobs added and 235k in revisions. What if, just like we understated jobs in some prior initial reports, we overstated jobs in this report? Pure speculation, but the data is volatile and the economists who were disappointed by initial reports in August and September turned out to be more correct than we thought at the time. With stimulus coming jobs shouldn't roll over, but it is a concern and might be something that people are more aware of than is indicated in government stats. **This demonstrates that the people in the "know" are seeing conditions change more rapidly than what is hitting government statistics, which is plausible and concerning (if accurate)**.
- **Pulled Forward Demand**. One logical response to supply shortages, especially as we hit the holiday seasons in the U.S., is to buy what you need when it is available. Need a bike and need skis? Buy both today because you don't know what will be available in a few months. My greatest concern is that we have front loaded consumption (and this will slow down), while many others are extrapolating that consumption will continue at a reasonably aggressive pace. If the consumer knows that they are getting tapped out, it would explain why past numbers

look ok, but why they have less confidence going forward.

- **Inflation.** My favorite part of the CPI data was that Owner Equivalent Rent, which is 23.6% of the index, is up 3.1% on the year. If people could bet on the components of CPI vs reality, I don't think I'd find a single person who would bet the "under" on what the cost of housing has done in the real world relative to the calculation of CPI. You know my view on inflation (it is going to be higher for longer as China is no longer deflationary, ESG is inflationary, etc.) but as bad as the data is, it probably understates what most people are experiencing. **The realization that everything costs more is bad enough, but the realization that everything costs way more than the government says is even more troubling**, because it reduces the likelihood that something will be done about it.

Bottom Line?

Confusion. We seem to live in a world of unprecedented situations. Where we lurch from one thing that hasn't been seen before to another. This discrepancy between consumer confidence (which I generally ignore) and so much else seems weird enough that it bears scrutiny and an attempt to understand what is going on.

For now I will stick with my Bond Market Outlook.

With VIX still low relative to MOVE (a disconnect that is growing again), equity options look cheap and I'd lean towards puts (and I guess I cannot say weekly puts, as that would make me a hypocrite, but…)

Deep down, as I wrote in the middle of last week, there is a risk of going from FOMO to LOBO (my best attempt at turning Look Out BelOw into an acronym, which followed up on last weekend's Quit Rate).

Finally, if you didn't get to watch Bloomberg TV on Veterans Day, I highly recommend spending 7 minutes watching Academy's interview (link). Academy starts at roughly the 1 hour, 11 minute, and 47 second mark and while we discuss markets, inflation, the Fed, succession, etc., we also get to chat about Academy Securities itself more than usual. I think that part alone is worth a quick watch (or listen).

Thanks and have a great week!

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