Making Sense of the GDP Numbers - Transcript

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Tom Mullooly: Welcome back to the podcast. This is episode number 318. Thanks for joining us. I'm Tom Mullooly. And with me today is Tim Mullooly. Hello.

Tim Mullooly: Hello everybody. No Brendan today, but I think we can carry it with just the two of us.

Tom Mullooly: Well, we're not sure, but we'll try our very best.

Tim Mullooly: We'll find out.

Tom Mullooly: Headline today. Second quarter GDP came out, a drop of just 32.9%. Certainly the biggest number I've ever seen.

Tim Mullooly: Me as well. So I think my initial reaction is you see a number like 32% and it's eye-popping, it seems like that is a huge number, which it is. But it's important to put it into the context of it's down 32% from the previous quarter. I think that's important to keep in mind. So when you look at it year over year, it's 10% down, which again is still a huge number.

Tom Mullooly: It's gigantic.

Tim Mullooly: But I always just think context is important.

Tom Mullooly: Context really does matter whether you're talking sports or market statistics or economics. I mean, if you were to say Amed Rosario is batting 32.9%, a third less than he was batting before. Well wait, was that last year? Was that against his career? So all of these things have to be put into their proper context and like Tim just pointed out, the economy is down one third of where it was in January, February, March, and it's down 10% from the same quarter a year ago. So let's put some numbers on it, round numbers. The economy, the size of the economy is roughly $20 trillion, which means that in the second quarter, April, May and June, when everybody stayed home, we still cranked out $18 trillion worth of gross domestic product, on an annual basis.

So divide that number by four to get what we actually did. And it's funny, I didn't really think that the members of the federal reserve talked in these kind of numbers, but I heard an interview in April with Jim Bullard. In the very same interview, he used that quote that I've used now on a couple of podcasts where he said, "This is not a recession. It's a systematic partial shutdown of the economy." He used those same numbers. He's like, "Look, the economy is roughly $20 trillion in size, which means we generate about $5 trillion in a normal quarter, do the math." And I never thought that. I thought that they would be rolling out details, but he made it easy to understand. And in bite sized chunks, I was like, "Okay."

Tim Mullooly: Also, what you just said, it's going back to having the right context. There hasn't been a time in American history where there has been a planned, organized shutdown of the economy for any sustained period of time. So when you're comparing it to previous declines in GDP, it's almost apples to oranges when you're comparing them, they're not the same situation. Overall, I think the number still, however you want to paint it with whatever context, it's still not good. But we don't really know in terms of the stock market today, when the market opened, the market went down, I think it was down at most around 500 points. There have been times over this pandemic where numbers have either been forecasted or known ahead of time, we knew this number was going to be bad and the market goes up because of it.

There were times where the unemployment numbers would come out and they were bad numbers, but the market went up. This time, there was a bad number and the market went down. It just goes back to that point that we say a lot where you can have the numbers ahead of time and you still can't predict which way the market is going to go. So making any sort of decision based on these numbers in the short term, what reaction the market's going to go. Is it going to go up? Is it going to go down? Nobody knows. So you can't hang your hat on making decisions in your portfolio on these numbers. It doesn't work that way.

Tom Mullooly: Completely agree. And the thing that always makes me chuckle, not that we do a lot of active daily trading, it cracks me up when we get a number like this, because it seems to me that everybody on the planet knew that this second quarter GDP number was going to be really, really bad. I heard two weeks ago that it could be down 40%, and it came in down about 33%, still a really bad number. But you and I recorded a video in April at the start of the second quarter. And I remember distinctly telling people in the video, the second quarter numbers going to be bad, but we're not going to get that number until the end of July. And we got it on today, July 30th and it's long after the quarter has ended. And there's going to be a revision to it a month from now. And then a final number that comes out in September when we're about to start the fourth quarter.

Tim Mullooly: Right. To me, it kind of speaks to the kind of futility of making forecasts and projections because people were saying at the beginning of the second quarter and the end of the first quarter, "Well, we know these quarters are going to be bad, but we're expecting the third and fourth quarter to be a lot better. And they're going to come roaring back." And now we're finding that might not be the case, things didn't go as planned. And we still don't know what's going to happen in the future.

But I think you pair the known bad number of what we are going to get from the second quarter with the current environment, people are like, "Oh wait, it might not be better, as early as the third quarter or the fourth quarter, it might take a little longer than we thought." I kind of just throw my hands up in the air when I see people continuing to try and make forecasts of what's going to happen in the next two or three quarters. It's like, "Well, no one saw this coming. No one predicted the response correctly. So what makes you think you can predict the next couple quarters moving forward?"

Tom Mullooly: It reminds me a lot of when I traded stocks a lot more actively in the eighties and nineties, a company would come out and pre-announce that their earnings were going to be bad and the stock would get destroyed. The stock would continue to remain volatile, and then when they finally did announce their earnings, the stock got destroyed again. And so this was a known number. I mean, we didn't know the exact number, but we all knew that this number was going to be just awful. And yet the market continued to sell off.

But the market opens at 9:30, New York time, 10 o'clock Dow Jones, S&P, NASDAQ, all down, all down more than 1%. So the Dow was down almost 2%. It was down just a shade over 500 points. At 1 o'clock, as we go to record this, Dow Jones is now down 200 points. The S&P is down 12 points. These are actually better than the overnight future's numbers. And the NASDAQ is positive. NASDAQ's actually up 35 points. It's at 10,577, as of 1 o'clock. So I know after the market closes today, we're going to get earnings reports from Facebook, Apple, and a few other companies as well. So I would imagine that people are getting their bets in order.

Tim Mullooly: Yeah. And that's what they are. They're bets. So depending on if you were going to trade on GDP numbers, depending on where you got in or got out, you could have been right or wrong. Like you said, we're up almost 300 points from the bottom today. If you sold or bought right at the open, different story from right now, and it'll be different tomorrow morning, too, based on what happens with these companies. So for us, none of this has any bearing really on changes that we would make because we're investing for the long term. All of this would be really, really important if we were day traders, but we're not.

Tom Mullooly: I would imagine that some listeners may be scratching their head saying, "Usually we're talking about financial planning topics. Why are we talking about this now?" Because it's a headline grabbing number that came out this morning and the market's on the move. I've gone through a lot of the June 30th statements recently in the month of July looking at the numbers and the numbers for a lot of people, recovered quite a bit through the second quarter. But the market has been actually very good in the month of July. And so I think it's totally okay if we give a little ground back or if we continue to tread water maybe for a while.

Tim Mullooly: I don't think that, that would be the end of the world, considering the volatility that we saw in the beginning of the year. And also just the heightened level of uncertainty that we were just talking about. We still don't know. We don't have definite answers on what's going to happen for the rest of the year. So yeah, I mean, treading water, moving sideways wouldn't be the worst thing in the world. It would probably be easier to stomach than another 30% drop. And then another 30% rally from there.

Tom Mullooly: I was speaking with a client this morning and I told him how I was looking at the calendar for this week. And I saw a lot of things that made me want to start eating donuts again. I saw all of these tech companies with their earnings coming out this week. We're in the middle of earning season. We have second quarter GDP, which came out this morning. Every

Thursday, we get jobless claims and continuing claims, and we'll define them in a moment. But we also had a fed meeting, two day meeting this week.

And before we get to the fed, I just want to spend a brief moment talking about jobless claims and continuing claims. Initial jobless claims are posted every Thursday morning at 8:30. And it shows all of the people who were filing for their first time jobless claim last week. And here in New Jersey, we still read stories of people who haven't been able to get through to the unemployment office and start collecting their unemployment, which is horrible.

Four months, they might've been out of work. And I don't know how they're making it. Initial jobless claims are announced every Thursday at 8:30. At the same time, the market has started paying attention to the weekly continuing claims. Now that is the number of people who are still on unemployment. That is a number that's actually two weeks old. So this goes back to the week ending July 18th. And what you do is basically a little algebra. You say, "Okay, the continuing claims are X, where were they last week? That's Y. The difference is the number of people who are going back to work."

And so what they're trying to do is build a trend line and say, "How many people are going back to work? Well, that number has actually slowed down." No surprise. We're starting to see a number of positive cases surging in other parts of the country, not New York and New Jersey. So Florida, California a big state, Texas seems to be plateauing, but these states are seeing elevated claims. And so more people are starting to stay home. They're talking about shutting down again. So this is going to have an impact on people's outlook for the economy.

Tim Mullooly: Yeah. Going along with those unemployment numbers, like we said here in New Jersey, we've been seeing there's a huge backlog of people not being able to even apply for unemployment. I think we talked about it on a podcast a handful of weeks ago. These people might not have lost their job necessarily last week or the week before that. They might've lost their job three or four months ago, and now they're finally able to get onto unemployment and make that initial claim, but it might not be indicative of what's currently happening in terms of the economy.

People might actually be going back to work, but other people still are filing their unemployment claims for the first time because they can finally get through. So it's tough to decipher what that really means for the workforce in general, when those numbers are kind of backlogged and then some people are going back to work, but other people are getting laid off. And there's a lot of moving parts. It's tough to decipher what it really means.

Tom Mullooly: You raise a good point that when you mention backlog, because some states, not only are people finally able to get through and file, but they've also been behind in the reporting as well. So the numbers are going to be janky through the rest of the year until we get back on track. The other thing is next Friday will be the first Friday of the month. And so we'll get the unemployment numbers for July. And that will be the accumulation of all of these weekly jobless claims. So it shouldn't come in as a total surprise, but again, like GDP this morning, shouldn't have been a surprise, market's still sold off.

Tim Mullooly: Yeah, I think it might not be a surprise, but it doesn't necessarily mean that the market's going to go up or down. .People are expecting it. We just don't know if they're going to be buying or selling because of it

Tom Mullooly: Some of these day to day things that are happening that do drive the market's up or down, we get questions all the time on this. So it's worth covering in a podcast. But I want to go back to something else I mentioned it was on the calendar this week. There was a two day federal reserve meeting.

Tim Mullooly: It's interesting that there were so many other things going on in the financial industry and the markets that this fed meeting kind of flew under the radar. I mean, you think back when the fed meeting was the thing to pay attention to.

Tom Mullooly: Oh, it was the event for 20 plus years of my career.

Tim Mullooly: Not really the case this time around. There were other things that people were paying attention to.

Tom Mullooly: Well, I think the fed kind of took away the surprise at the previous meeting when they said, "Look, we're going to keep rates as accommodative as possible for the foreseeable future. And they intimated that, that means we're going to see interest rates at these kinds of levels for two years.

Tim Mullooly: Yeah. The timetable is undetermined, but for the foreseeable future, unless things change and nothing from their last meeting or from when they announced that nothing had really changed. So I think people kind of expected what ended up happening, there's not much.

Tom Mullooly: Now the first couple of rounds of quantitative easing that happened in early 2009, and then again in '10, and then they did operation twist in 2011, and then a final push in 2012. These were all $300 billion deals, $500 billion deals, a lot of this. I think what a lot of people have overlooked and maybe we're just getting used to seeing big numbers, but the fed has been buying treasuries and government agencies in the market every week, since April 7th to the tune of $5 billion a week. That's insane. I mean, that's a hundred billion right there just in the weekly transactions, that doesn't even count bringing rates down to zero and flooding the market with all these different vehicles that they've brought.

The amount of financial bazooka that they brought to the game has really outstripped anything else that they've ever done. And Tim, I know you've heard me say this on the phone to folks that I don't think people realize that what the fed has done this spring is nearly 10 times what they did in 2008 and 2009. And so we got a really good response in the market for several years. Now, multiply that by a factor, a large factor, and if the fed continues to be your friend, unless something goes terribly, terribly wrong, we could have a nice lift to the market going forward. I hate to go out on a limb and say things like that, but.

Tim Mullooly: We definitely could, but it could end up backfiring in some way, if for some reason, the virus continues to get worse or some other unknown variable pops up.

Tom Mullooly: The thing that I find interesting is this weakness in the dollar and the rise in gold. And I'm a little puzzled by this because just yesterday in the press conference that Powell had after the end of the fed meeting, he said that this economic shock this year is dis-inflationary, meaning, so many people get knocked out of work and the economy's slowing down, we are not going to have inflation. Tell me why gold is doing what it's doing.

Tim Mullooly: I wish Brendan was here to answer that question, because we've actually on a couple of podcasts, Brendan has answered that question. And pretty much the answer is gold does whatever it wants. There really is never one hard set reason why gold is moving up or down. A lot of times when you see the market get volatile, or you see people start to get nervous, you see gold spike up because people think they've in air quotes, flock to safety to grab onto gold. They think of it as a safer asset-

Tom Mullooly: Which is insane.

Tim Mullooly: ... it is. Brendan has proven that in past podcasts, but maybe that's the case this time. I agree, I don't think it's because people think that there is inflation right around the corner. Even if they do, that they might be right, they might not be right. So, who knows really why gold is spiking?

Tom Mullooly: A couple of things come to mind when we see this. We see gold spiking, and I think like you just said, "It's a fear trade." And so I would throw gold in the same bucket as the VIX, because it really is an indication of the level of fear or caution-

Tim Mullooly: Sentiment.

Tom Mullooly: ... yeah, that's out there. It's amazing though, to see a fear gauge like gold moving up while the markets are back to where they were in February. I don't understand that.

Tim Mullooly: Yeah. It seems like gold is moving up because people are nervous at the same time that the market continues to go up. It's almost like people are like, "Well, the market's gone up too much. It needs to turn down at some point," but it hasn't happened yet. And again, they might be right. It could turn down and they could be proven right. But we're seeing it right now, the market is continuing to chug along and gold is moving with it.

Tom Mullooly: I don't seem to think that people are buying gold because they expect inflation to be 2 or 3% or more in 2023 or 2024. I think we also kind of have to talk, when we talk about gold, we also have to talk about what's happening with the dollar. And as the dollar falls apart, we see international markets do well. We see emerging markets do very well, but we also see things like commodities snap out of their coma. And that's exactly what's happened with gold and silver in the last couple of weeks. The dollar, US dollar has had a strong move down in the month of July.

Tim Mullooly: Going back to where we started, it's important to put that into context because yes, that's true, the dollar has moved down this month recently. But didn't it also spike up almost, just as much in March and April?

Tom Mullooly: Sure did.

Tim Mullooly: So where is it coming down from, I think is the important point. You had put a chart in our Slack channel where we discussed these topics a little bit beforehand, and it was just showing the range that the dollar has been trading in for the last what, four or five years?

Tom Mullooly: Right. And if you just look, it's right now, it's at the bottom of the range. But if you go back, like Tim said to March and April, we saw a tremendous dollar spike out of the range higher, and now it is taking all of that back, and now it's at the bottom of the very same range that it's been in for five years. When you look at it from that kind of perspective, yeah, okay, the dollars at the bottom of the range, but I don't think it's something where people are talking about the dollar is going to lose it's reserve currency status. Come on, really?

Tim Mullooly: Yeah. I think one point that that Brendan made in his notes about this was how currencies are going to fluctuate, we have strong dollars, we have weak dollars, same thing with other currencies around the world at different times. I think the important thing for longterm investors to remember is that you want to construct a portfolio that isn't dependent on... Your success isn't dependent on the currency going in one direction at all times. Build a portfolio that can withstand the dollar moving in different directions because different asset classes and different equities around the world perform better or worse, depending on how that currency is doing.

Tom Mullooly: There's plenty of people that are offering up their opinions. And again, their opinions, we all read the same story in the Wall Street Journal where they quoted someone saying, "It looks to us like the V-shaped recovery is not going to happen." Other people were saying, "Well, the fed's going to be very gloomy with their outlook." We don't know.

Tim Mullooly: All of those things could be true. It still doesn't necessarily determine which way the stock market is going to move.

Tom Mullooly: I have a question for you. What area code is 318?

Tim Mullooly: I have absolutely no idea.

Tom Mullooly: So if you're just tuning into our podcast, I spent a major chunk of my early career cold calling all around the United States. And I got to know all of these area codes. Area code 318 is for a big chunk of Louisiana. And so that's going to wrap up episode 318, and I suppose in our next podcast, we'll be visiting Iowa City.