Summary

Economic data for the week included the Federal Reserve continuing its robust pace of interest rate increases—last week again by 0.75%. The ISM manufacturing and services surveys declined, but remained in expansionary territory. Labor reports continued to show positive growth, through nonfarm payrolls and job openings, while the pace of wage growth decelerated a bit.

Global equity markets were mixed, with declines in the U.S. but positive returns overseas—notably in emerging markets. Bonds fell back along with several central bank interest rate increases. Commodities rose along with higher energy prices, due to near-term concerns about inventories.

Economic Notes

(0) The **FOMC** meeting didn't offer surprises to many observers, but the official statement unwrapped the terms 'cumulative tightening' and 'sufficiently restrictive'. This gave some insights to the Fed's thinking and future path, in that the rate hikes done through this point will have bearing on the general tightening of policy, perhaps allowing a slowing in hikes going forward. However, the Powell press conference afterward was seen as more hawkish, at least relative to expectations, as hopes for a pause were dismissed as 'premature'. His comments included, "We may ultimately move to higher levels than we thought at the time of the September meeting," and "We think we have a ways to go," proved to be a catalyst for a souring in market sentiment Wednesday. Markets are desperately seeking clarity on the timing and level of the terminal rate. This remains unclear, but we do appear to be closer to the end of rate hikes than the beginning, if that is of any consolation. In the meantime, Powell is holding the line and not providing any premature clues that could be taken by the markets too dovishly, resulting in an easing of financial conditions, and defeating the purpose of Fed hiking activity. Ultimately, 'sufficiently restrictive' may mean more like 5.00% rather than 4.50%, although actual numbers remain fluid, based on data received between now and the Dec. meeting, with features the dot plot estimates.

(0) The **ISM manufacturing index** for October fell by -0.7 of a point to a still-expansionary 50.2, an improvement on the consensus expectation of a neutral 50.0 reading. Under the hood, production, new orders, and employment all rose by at least a point, although production was the only segment to remain in expansion outright. Supplier deliveries and prices paid each fell by over -5 points into contraction, which were mixed blessings, with some impact from lower energy prices. While housing metrics have pulled down recent data, an improving supply chain/logistics situation has helped the industrial space. Economic cooling has lowered demand, which appears to have helped with the imbalances as well. Conclusion—the economy is growing, albeit at a slower pace.

(0) The **ISM services/non-manufacturing index** fell by -2.3 points in October to 54.4, below the expected 55.3—but remaining decently in expansion. Within the details, new orders and business activity fell back by several points but showed growth, while employment ticked down into contraction. Prices paid increased by a few points back up to a high level of over 70. Anecdotal commentary in the survey noted a good deal of uncertainty about future economic prospects, and rising recession fears. However, services remain about two-thirds of the spending basket, relative to goods at one-third, providing a scale of its relative importance.

(0) **Construction spending** in Sept. rose by 0.2%, well above the median forecast of a -0.6% decline. A rise of 1.0% for nonresidential private spending was the sole bright spot, while declines in public spending pulled down the total figure. However, construction cost inflation was reported at 0.9%, pushing real spending gains into the negative.

(+) The government **JOLTS** job openings report for Sept. showed a sharp rise of 437k to 10.717 mil., versus expectations of a drop to 9.750 mil., including an upward revision for the prior month. Leading segments included accommodation/food services (215k), health care/social assistance (115k), and transportation/warehousing/utilities (111k). The rate of job openings ticked up by 0.2% to 6.5%, while the hiring rate fell to 4.0%. On the other side, the layoff rate fell by -0.1% to 0.9%, and the quits rate was unchanged at 2.7%. Despite some signs of recent flattening, this report continues to show a strong labor market.

(+) The **ADP private employment** report for October showed a gain of 239k, beating the median forecast of 195k, and an improvement on last month's pace. Services jobs grew by 247k, 210k of which were in leisure/hospitality, while goods-producing jobs fell by -8k, led by a -20k drop in manufacturing.

(-) **Initial jobless claims** for the Oct. 29 ending week fell by -1k to 217k, below the 220k expected by consensus. **Continuing claims** for the Oct. 22 week rose by 47k to 1.485 mil., above the 1.450 mil. median forecast. Despite the rise in continuing claims, overall claims levels remain relatively low in historical terms.

(+) The employment situation for October came in stronger than expected, again dampening the spirits of markets hoping for some degree of slowing to detail hawkish Fed policy. However, details were not as strong as headline. **Nonfarm payrolls** rose by 261k, beating expectations of 193k. There were mixed revisions for several prior months, with a net gain of 29k. Per the BLS, the largest gains occurred in health care (53k), professional/technical services (43k), leisure (35k), and manufacturing (32k). Despite a sharp rebound in the leisure/hospitality sector in 2021 especially, as pandemic restrictions were lifted, overall employment remains down -6.5% from the Feb. 2020 level (1.1 mil. jobs).

The **unemployment rate** ticked up by 0.2% to 3.7%, to the higher point of the range it's largely stayed in this year. Interestingly, this did not coincide with much change in the labor force participation rate. The household employment component, which includes the self-employed, saw a decline of -328k jobs. The U-6 underemployment rate rose a tenth to 6.8%. **Average earnings** rose by 0.4%, bringing the trailing 12-month increase to 4.7%. This pace has fallen back by about a percent over the last six months, which is a positive from an inflation standpoint. **Average weekly hours** were flat for the fifth straight month at 34.5.

Prior to the Friday report, **nonfarm productivity** rose at an annualized rate of 0.3% in Q3, trailing the 0.5% expectation. On a year-over-year basis, productivity rose by 0.7% to a still-negative -1.4%. **Unit labor costs** rose by an annualized pace of 3.5% in Q3, below the 4.0% expected, and well below the pace of the prior quarter. Year-over-year, the pace decelerated by -1.5% to 6.1%. Productivity remains persistently weak, while labor costs have come down significantly—adding to hopes that inflation is peaking in this realm as well.

Market Notes

Period ending 11/4/2022	**1 Week (%)**	**YTD (%)**
DJIA	-1.38	-9.33
S&P 500	-3.31	-19.83
NASDAQ	-5.62	-32.60
Russell 2000	-2.53	-18.95
MSCI-EAFE	1.24	-22.27
MSCI-EM	4.68	-26.34
Bloomberg U.S. Aggregate	-0.78	-16.02

U.S. Treasury Yields	3 Mo.	2 Yr.	5 Yr.	10 Yr.	30 Yr.
12/31/2021	0.06	0.73	1.26	1.52	1.90
10/28/2022	4.18	4.41	4.19	4.02	4.15
11/4/2022	4.21	4.66	4.33	4.17	4.27

U.S. stocks started the week optimistically, and the FOMC meeting led to a quick uptick in stock prices, followed by a sharp drop of -2.5% as the press conference hawkishness disappointed financial markets. The employment situation report on Friday was closely watched for labor market tightness, with metrics remaining surprisingly strong. There were announcements of some hiring pauses, notably by Amazon, which also pulled down sentiment.

By sector, energy stocks led with gains over 2% along with higher oil prices, while materials and industrials also fared positively. All other sectors saw declines, led by nearly -7% losses in 'growth' groups technology, communications, and consumer discretionary. Real estate pulled back by nearly -2%. Per FactSet, 85% of S&P 500 firms have now reported earnings results for Q3, with over two-thirds having surprised in a positive way, with a combined actual/remaining estimated year-over-year growth of 2.2%. This has been led by energy, with earnings growth upwards of 140%, with seven other sectors having shown negative results, led by communications on the low end. So, while energy has boosted the overall index number, the economic slowdown has already made its way into earnings announcements. Estimates have come down steadily since mid-year, with those for Q4 now having fallen underwater, at -1.0%, although expectations aren't calling for an extended negative stretch of multiple quarters. The forward 12-mo. P/E now stands at 16.1, which is right at about the long-term average.

Foreign developed market stocks fared oppositely from U.S. stocks, by ending the week with gains of 1-2%. The Bank of England similarly raised rates by 0.75% to 3.00%, given sharp inflation pressures, despite far more serious economic hurdles driven by high petroleum prices. This was eighth straight hike, and the largest one in over 30 years. However, BofE hikes have not generally been unanimous, as with the U.S. Fed. Additionally, their rhetoric has been far more pessimistic than that seen in Fed press conferences, no doubt justified due to recent high energy prices. Other central banks, such as Norway (0.25%), have been slowing down hikes, seeing the impact on their respective economies. This pulling back on hawkish sentiment was a positive for stock prices last week.

Emerging markets were up a more sizable 5+%, led by a double-digit recovery in China, although all other key nations also earned decently positive returns. Earlier last week, rumors of a 'committee' in China that was reviewing a possible exit to the zero-Covid in Spring 2023 led stocks there to rebound sharply, although that rumor was never confirmed. However, it did demonstrate that policy as being one of the key risk factors holding back Chinese stocks from finally improving. A likelier outcome is a slower drift away from such policies in the spring, following successful testing of their mRNA vaccine. In Brazil, the victory of Lula over Bolsonaro follows a trend of left-leaning election wins in Central and South America as of late.

U.S. bonds fell back last week, as rates rose along with the Fed hiking decision. For the most part, longer-tend yields tracked the expectation for the Fed's terminal rate to tick up from 4.5% to perhaps as high as 5.0%, although debate obviously remains about the path for 2023. The 2y-20y inversion has moved deeper, to the largest spread since 1982. It's now accompanied by the 3m-10y for a week now—a combination which has been a more responsive recessionary signal historically (albeit with a wide range of 6 mo. to 18 mo. in the future). Investment-grade corporate outperformed treasuries slightly, while high yield fell back nearly -2% along with a stronger correlation to equities. Foreign developed market bonds were down as well, not helped by a slightly stronger dollar, while emerging market bonds saw gains.

Commodities gained ground by several percent for the week, with every sector in the positive. The price of crude oil rose by 5% to nearly $93/barrel, with concerns rising again about current inventory levels and ending of U.S. Strategic Petroleum Reserve releases. In addition, further sanctions on Russian oil are upcoming, further tightening global supplies. In a continuation from the prior weekend the Russian exit from an agreement to allow Ukraine grain exports caused a price spike early in the week; however, Ukrainian military actions appear to have forced a reversal in policy by mid-week.

Have a good week.

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Sources: FocusPoint Solutions, American Association for Individual Investors (AAII), Associated Press, Barclays Capital, Bloomberg, Citigroup, Deutsche Bank, FactSet, Financial Times, First Trust, Goldman Sachs, Invesco, JPMorgan Asset Management, Marketfield Asset Management, Morgan Stanley, MSCI, Morningstar, Northern Trust, PIMCO, Standard & Poor's, StockCharts.com, The Conference Board, Thomson Reuters, T. Rowe Price, U.S. Bureau of Economic Analysis, U.S. Federal Reserve, Wall Street Journal, The Washington Post. Index performance is shown as total return, which includes dividends. Performance for the MSCI-EAFE and MSCI-EM indexes is quoted in U.S. Dollar investor terms.

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Notes key: (+) positive/encouraging development, (0) neutral/inconclusive/no net effect, (-) negative/discouraging development.