Financial Market Weekly

MUFG UNION BANK, N.A.
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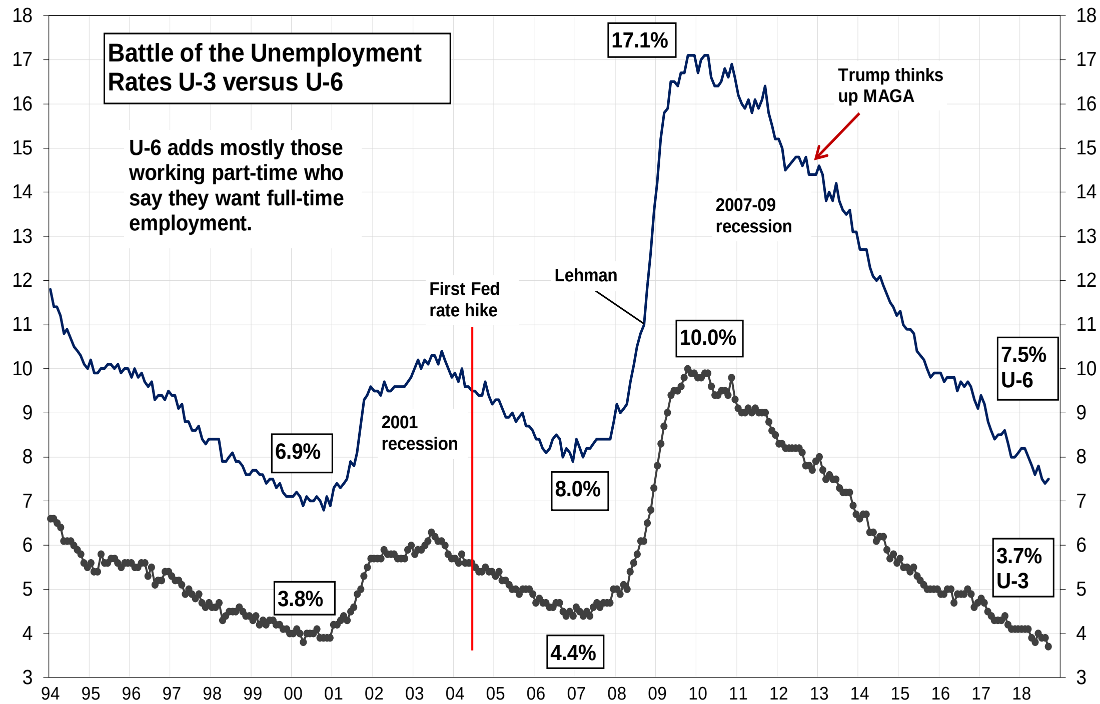
JUST THE FACTS: SLOWER 134K JOBS (87K UPWARD REVISIONS), 3.7% UNEMPLOYMENT, 2.8% WAGES



Not sure what to do with this mix of data in the monthly employment situation report. And don't forget the trade deficit widened from $50.0 billion in July to $53.2 billion in August which will take 1.5 percentage points off Q3 real GDP, although we still believe it will make it to 3.0% in the report due out Friday, October 26. The bond market doesn't seem to know what to do with the data dump this morning either with 10-yr Treasury yields frozen in the news headlines glare at 3.20%. Yields ten minutes later finally moved up a couple of basis points to 3.22%.

	Sep	Aug	Jul	Jun	May	Apr
Payroll jobs (000s)	134	270	165	208	268	175
Unemployment rate %	3.7	3.9	3.9	4.0	3.8	3.9
Unemployment (3 decimal)	3.683	3.853	3.871	4.048	3.755	3.929
Participation rate %	62.7	62.7	62.9	62.9	62.7	62.8
Average hourly earnings	$27.24	$27.16	$27.07	$26.99	$26.94	$26.86
MTM % Chg	0.3	0.3	0.3	0.2	0.3	0.2
YOY % Chg	2.8	2.9	2.8	2.8	2.8	2.6
Production Worker earnings	$22.81	$22.75	$22.67	$22.63	$22.58	$22.52
MTM % Chg	0.3	0.4	0.2	0.2	0.3	0.3
YOY % Chg	2.7	2.9	2.8	2.8	2.7	2.6

134K jobs in September with 87K of upward revisions. Record low on unemployment at 3.7%, at least as far back as we should all be looking. It fell as low as 3.8% previously during the stock market bubble in April 2000. The economy was just as fantastic under President Clinton.

Wages, average hourly earnings held we would say even if down a touch to 2.8% in September from 2.9% in August. (Worker wages fell more to 2.7% from 2.9% last month, but the bond market overlooked this.)

134K payroll jobs could have been hit by the Hurricane in the Carolinas. Not a lot of scientific support for this, just observing that leisure and hospitality jobs dropped 17K. Yes, we know Disneyland is further South. Leisure and hospitality dropped 111K last September after Hurricanes Irma (Florida) and Harvey (Texas). Also for September 2018's report, retail jobs dropped 20K as well. These two categories seem to explain the 134K weakness.

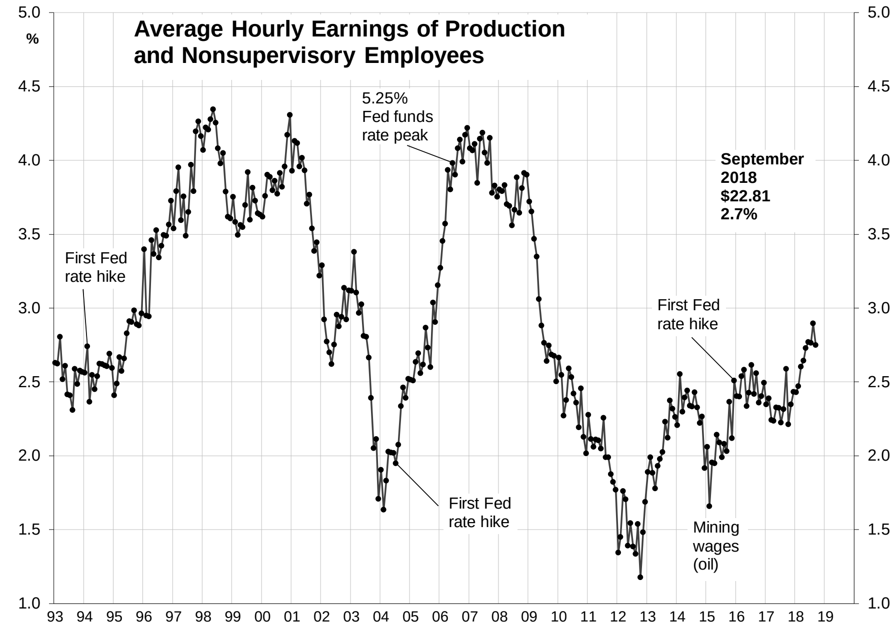
Payroll jobs in year ten following the recession

Dec. 2017 Totals millions		Sep 18	Aug 18	July 18	9 months Dec 17 to Sep 18	12 months Dec 16 to Dec 17
147.625	Nonfarm Payroll Employment	134	270	165	1875	2188
125.294	Total Private (ex-Govt)	121	254	137	1800	2163
20.328	Goods-producing	46	37	41	456	509
0.648	Mining	5	7	-1	55	53
12.558	Manufacturing	18	5	22	189	207
0.956	Motor Vehicles & parts	0	2	-1	4	4
7.072	Construction	23	26	19	214	250
104.966	Private Service-providing	75	217	96	1344	1654
27.593	**Trade, transportation, utilities**	8	55	17	252	169
15.861	Retail stores	-20	12	2	48	-29
3.122	General Merchandise	-4	18	18	28	-51
3.100	Food & Beverage stores	-2	3	8	-2	3
5.236	Transportation/warehousing	24	21	8	139	135
1.460	Truck transport	5	6	1	28	9
0.708	Couriers/messengers	5	4	7	49	39
1.011	Warehousing and storage	8	4	6	38	43
0.554	Utilities	0	1	-3	-3	-3
2.776	**Information**	0	-3	1	-9	-36
8.511	**Financial**	13	12	3	92	142
2.664	Insurance	1	2	-2	16	38
2.220	Real Estate	13	6	7	50	60
1.323	Commercial Banking	0	-3	4	-3	5
0.951	Securities/investments	-1	5	1	17	20
20.677	**Professional/business**	54	65	39	453	458
2.998	Temp help services	11	12	10	61	96
2.308	Management of companies	3	5	-1	31	38
1.456	Architectural/engineering	-1	6	2	29	45
2.065	Computer systems/services	5	5	9	58	47
1.137	Legal services	1	-1	-2	1	5
0.982	Accounting/bookkeeping	0	3	2	31	-3
23.380	**Education and health**	18	58	36	370	458
5.124	Hospitals	12	9	7	79	70
3.696	Educational services	-12	16	3	59	77
16.207	**Leisure and hospitality**	-17	21	13	135	354
2.014	Hotel/motels	-5	4	3	23	31
11.844	Eating & drinking places	-18	18	8	111	261
22.331	Government	13	16	28	75	25
2.182	Federal ex-Post Office	0	-1	0	6	-12
5.129	State government	22	8	15	35	-16
2.462	State Govt Education	21	10	14	36	-1
14.407	Local government	-8	9	12	41	56
7.938	Local Govt Education	-1	6	15	31	28

We have to keep the 134K in mind however as something that could someday become the new normal. We still remember Yellen's comment saying how jobs would slow to 90 to 120 thousand per month eventually when the unemployment rate falls lower and America runs out of labor. Unemployment was 4.7% when Yellen left the Fed in February 2017, so the economy has improved tremendously since then. One thing is for sure with the employment report in hand today, the ever data dependent Fed will continue on its course to bring the Federal funds rate up gradually to normal levels. Powell said this week that they were a long way from normal. We don't know about that but the jobs report today keeps the Fed on track to raise rates again at its December meeting to 2.5% which is the level which some Fed officials believe is normal.

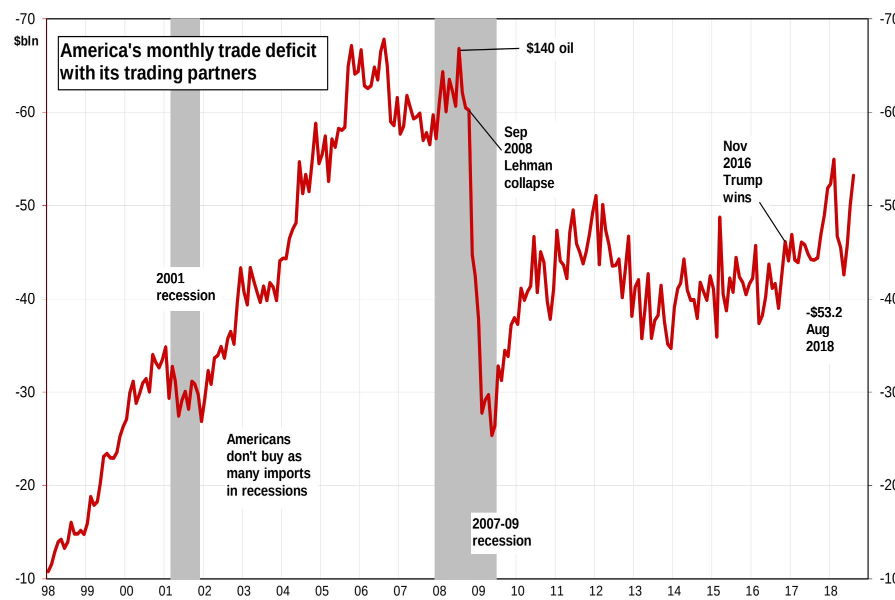
Net, net, the great American jobs machine is not done cranking out jobs for everyone yet, even if payroll jobs growth cooled in September. The unemployment rate is the statistic that points to true

North for the economy in this month's employment report and the 3.7% rate is a new low showing the labor market is tighter than any time since the late 1960s, not that we are recommending anyone wish for those feeling groovy times again. Make America Great Again is more, let's bring back the 80s. Let's Make America Great Again was also a campaign slogan for Reagan/Bush in 1980.



One thing is for certain, labor is going to be newly emboldened as the rock-bottom 3.7% low for unemployment shows companies are facing an enormous labor shortage. Workers have turned the tide and have management over a barrel when it comes to wage and salary negotiations. Average hourly earnings are up 0.3% today to $27.24 at a 2.8% annual rate (just missed 2.7 as the 3-decimal reading was 2.754), but you can bet your bottom dollar that workers are going to be clamoring for higher wages and new hires are going to be getting much much more. We can stop the foolish guessing game by many in academic circles on whether the economy has reached full employment.

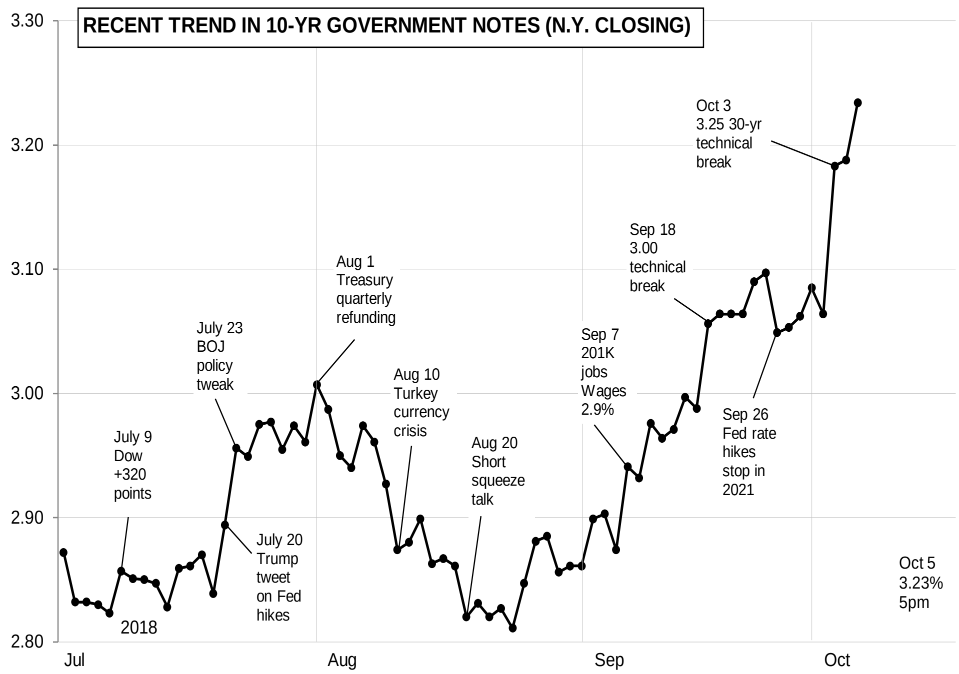
Stay tuned. Story developing. We aren't sure whether the lowest level of unemployment since the 1960s is a good thing or a bad thing for the economic outlook. The economy needs labor and capital to keep growing and right now the fuel gauge is pointing to empty on the pool of labor available to make this ten-year expansion break the record from the Clinton years of the 1990s. There are some recession calls way out there on the horizon in 2020 and the lack of workers going forward could just make those forecasts a reality.



Finally, the trade deficit for August which was not the focus of the markets when it was released the same time as the monthly jobs report this morning. The trade deficit widened to $53.2 billion in August which will prove to be a drag on Q3 GDP (Gross Domestic Product subtracts imports). Exports are $99.0 billion greater so far this year than last: a little of everything is being shipped, standouts are crude oil $16.4 billion, petroleum products $10.1 billion, soybeans $6.0 billion, aircraft engines $5.6 billion, natural gas $3.3 billion, industrial machines $3.2 billion, an increase in exports means more manufacturing jobs, jobs, jobs.

MARKETS OUTLOOK

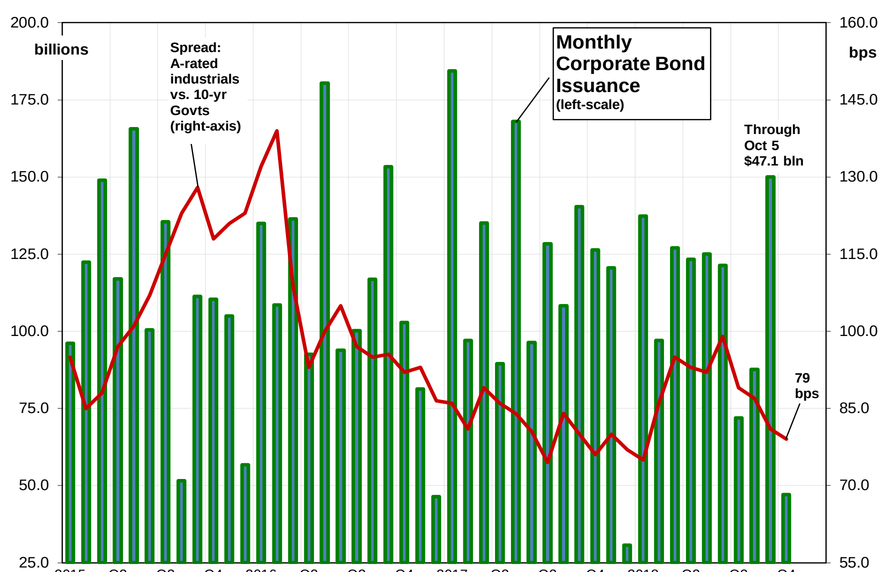
	28-Sep 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021
30-Yr Treasury	3.21	3.25	3.40	3.45	3.65	3.60	3.80	3.85	3.85	3.95	3.95
10-Yr Note	3.06	3.10	3.20	3.30	3.50	3.50	3.70	3.80	3.80	3.95	3.95
5-Yr Note	2.95	3.00	3.10	3.20	3.40	3.45	3.65	3.75	3.80	3.95	3.95
2-Yr Note	2.82	2.90	3.00	3.15	3.40	3.40	3.60	3.75	3.80	4.00	4.00
3-month Libor	2.40	2.70	2.95	3.20	3.45	3.45	3.70	3.90	3.90	4.20	4.15
Fed Funds Rate	2.25	2.50	2.75	3.00	3.25	3.25	3.50	3.75	3.75	4.00	4.00
2s/10s spread	24	20	20	15	10	10	10	5	0	(5)	(5)
Libor/funds spd	15	20	20	20	20	20	20	15	15	20	15



Bond yields broke higher this week, enough to get the attention of the stock market. Negatively. The biggest sell-off was Wednesday, partly technically based as 30-year yields broke above 3.25%, resistance clearly marked on the charts since 2015. We'd like to think the economic news did it for once on Wednesday, starting with ADP jobs of 230K at 830am ("real" private payroll jobs on Friday were 121K), and then ISM services at 10 o'clock almost broke all-time highs from 1997: there was selling after both reports. 10-year Treasury "bond" yields made it to 3.25% Friday, 100 bps higher than the 2.25% Fed funds target. We'll see if it holds. The IMF world economic outlook is ahead and will probably warn about the risks from rising trade tensions.

CORPORATES: CENTERPOINT ENERGY, ENTERPRISE PRODUCTS, HONDA

Corporate offerings were $47.1 billion in the October 5 week versus $12.7 billion in the September 28 week. On Tuesday, Comcast Corp. came with a $27.0 billion 12-part offering. It priced a $4.0 billion 4.15% 10-yr (m-w +20bp) at 110 bps (A3/A-). The media and tech company (Comcast Cable, NBCUniversal) will use the proceeds to finance its Sky (UK TV) deal. Corporate bond yields (10-yr Industrials rated A2) were 79 bps above 10-yr Treasuries this week versus 81 bps last Friday.



FEDERAL RESERVE POLICY

The Fed meets November 7-8 to consider its monetary policy. Twelve of sixteen Fed officials see a fourth rate hike this year to 2.5%. The new low in the unemployment rate to 3.7% in Friday's jobs report should remind us all that the Fed's gradual rates path is data dependent. Not so much for whether they go again in December, but longer term, the unemployment rate probably needs to move even lower for them to continue to raise the Fed funds rate into the neutral zone and beyond. Uncertainties aside, there are 3 Fed official votes for 2.5% neutral, four votes for 2.75%, and 6 votes for 3%. The economy may not always be this favorable for higher interest rates. Falling unemployment is key, slowing growth is a less important factor although it is in the mix, helping to color public perception about how good the economy is. Rising bond yields are also helpful as the "market" backs up the Fed's moves. GDP is less important as the Fed forecasts already show growth slowing from 3.1% in 2018 to 2.5% in 2019, then 2.0% in 2020, and 1.8% in 2021, where 1.8% is also the level of the economy's long run potential. So, the median forecast of Fed officials, after once more in 2018, is 3 more rate hikes in 2019, and one more rate hike finishing at 3.5% by the end of 2020. As we get into the neutral zone we still may see some votes for rate hikes drop away. Taking one Fed official speaking after the jobs report on Friday, Dallas Fed President Kaplan said he currently favors one more rate hike this year to 2.5%, and then two more rate hikes in 2019, and no delay, one hike in March and the second one in June next year.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	3-Oct	26-Sep	19-Sep	12-Sep	pre-LEH
Factors adding reserves					
U.S. Treasury securities	2294.210	2313.208	2313.206	2313.204	479.782
Federal agency debt securities	2.409	2.409	2.409	2.409	0.000
Mortgage-backed securities	1681.775	1681.763	1695.223	1697.016	0.000
Primary credit (Discount Window)	0.064	0.064	0.152	0.065	23.455
Term auction credit (TAF auctions)	0.000	0.000	0.000	0.000	150.000
Asset-backed TALF	0.000	0.000	0.000	0.000	
Maiden Lane (Bear)	0.007	0.007	0.007	1.720	29.287
Maiden Lane II (AIG)	0.000	0.000	0.000	0.000	0.000
Maiden Lane III (AIG)	0.000	0.000	0.000	0.000	
Central bank liquidity swaps	0.151	0.090	0.100	0.091	62.000
Federal Reserve Assets	4222.4	4240.4	4255.8	4258.5	961.7
3-month Libor %	2.41	2.39	2.35	2.33	2.82
Factors draining reserves					
Currency in circulation	1689.897	1686.023	1685.759	1686.970	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Reverse repurchases w/others	2.954	5.625	8.915	1.315	0.000
Reserve Balances (Net Liquidity)	1837.587	1837.874	1822.718	1924.008	24.964
Treasuries within 15 days	0.026	19.033	19.007	0.000	14.955
Treasuries 16 to 90 days	101.337	83.128	83.154	102.160	31.549
Treasuries 91 days to 1 year	310.595	315.819	315.819	315.819	69.272
Treasuries over 1-yr to 5 years	999.352	1010.629	1010.629	1010.629	170.807
Treasuries over 5-yrs to 10 years	265.763	267.467	267.466	267.465	91.863
Treasuries over 10-years	617.137	617.133	617.132	617.131	101.337
**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08					

**For you conspiracy buffs out there, the individual forecasts "show" 2 votes for higher rates in 2021, but 6 votes see lower rates in 2021 than in 2020. Wonder if the 2020 recession talk is getting to them.

GDP forecasts 3.1 in 2018, 2.5 2019, 2.0 in 2020, and 1.8 in 2021. Don't seem to believe the Tax Cuts and Jobs Act dream of 3% growth forever.

Year-ends for Interest Rates				
Percent %	2018	2019	2020	2021
Eurodollar futures	2.66	3.255	3.305	3.27
Fed's Sept forecast	2.5	3.25	3.5	3.5
Eurodollar futures price where 3-month Libor will be in the future.				
Friday, October 5, 2018 3-month Libor 2.41 %				

Fed Individual Forecasts					
Fed funds rate by year-end					Longer
Votes	2018 End	2019 End	2020 End	2021 End	run
1	2.125	2.125	2.125	2.125	2.500
2	2.125	2.375	2.625	2.625	2.500
3	2.125	2.625	2.875	2.875	2.500
4	2.125	2.875	3.125	2.875	2.750
5	2.375	2.875	3.125	2.875	2.750
6	2.375	2.875	3.125	3.000	2.750
7	2.375	2.875	3.125	3.125	2.750
8	2.375	3.125	3.375	3.375	3.000
9	2.375	3.125	3.375	3.375	3.000
10	2.375	3.125	3.625	3.375	3.000
11	2.375	3.125	3.625	3.375	3.000
12	2.375	3.375	3.625	3.500	3.000
13	2.375	3.375	3.625	3.625	3.000
14	2.375	3.375	3.625	3.625	3.250
15	2.375	3.375	3.625	3.875	3.500
16	2.375	3.625	3.875	4.125	
17					
Median	2.375	3.125	3.375	3.375	3.000
Meeting	Sep 2018	Sep 2018	Sep 2018	Sep 2018	Sep 2018

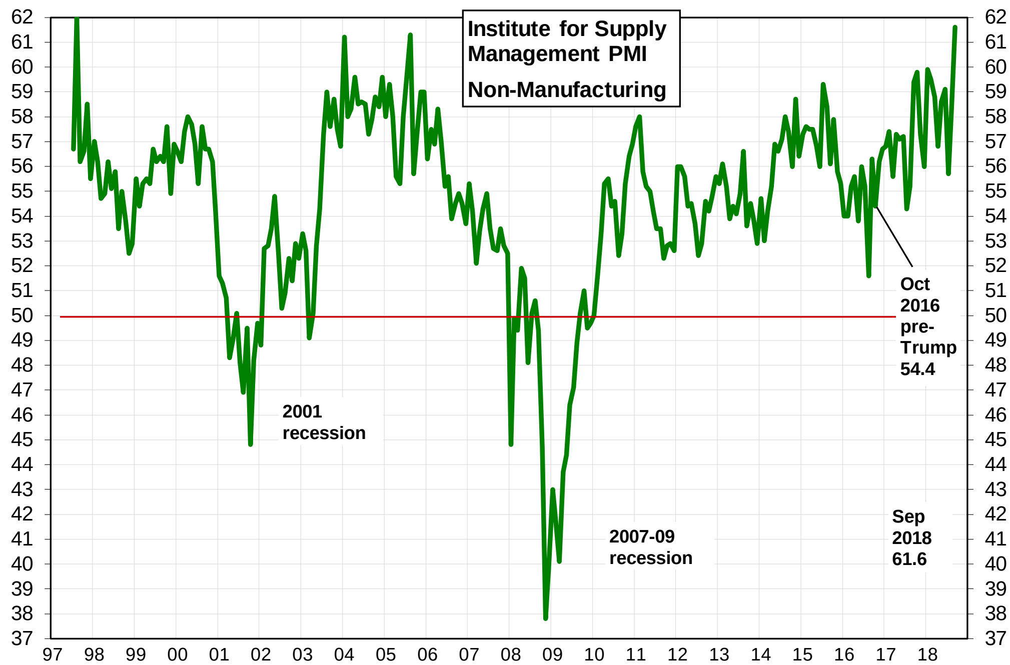
OTHER ECONOMIC NEWS THIS WEEK

Not one service industry is in dire straits (Wednesday)

Breaking economy news. The ISM survey for non-manufacturing companies, services to you. 61.6 was the reading in September shooting higher the last couple of months from the year's hard to explain low of 55.7 in July to 58.5 in August and now 61.6 in September. Service companies are bulled up on America after those tax cuts as consumers are buying everything they've got for sale.

The 61.6 reading is higher than anytime during the housing bubble economy years in the mid-2000s and just short of the August 1997 record of 62.0, during the Asian financial crisis no less, a reading not terribly reliable as the index just began a month earlier in July 1997. Those were the days. Make America great again as in 1997. The best years of our lives... gone.

Business sentiment is near all-time highs and no wonder with the stock market making new highs each day. This is just what it looks like before a stock market crash and recession. Just kidding.



What is hot or not? It's all hot in the service sector with all 17 non-manufacturing industries saying they are growing. Not sure if Trump's economics team (just don't ask their boss) can bring factories back to the USA, USA, USA, but the Administration's policies or something is sure putting a smile on service industry executives' faces. Even the residential construction market is said to be strong (huh?). But wait, they also say there is a labor shortage and higher tariffs are making materials more costly and this is eating into earnings. We think the retail industry sums it up by saying business is strong, but there is uncertainty about those looming tariffs where the $200 billion imported goods from China don't get up to a full-on 25% tariff speed until January 1, 2019. For now, it's a big party for this economy, and companies will party like it's 1999 until at least 2019. Stay tuned. Story developing.

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