Financial Market Weekly

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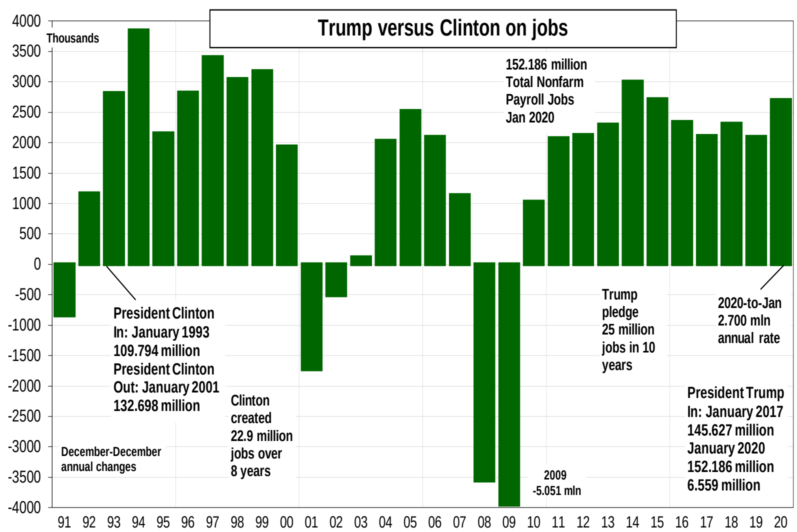
GOOD NOT GREAT JOBS REPORT DOESN'T MEAN WE ARE OUT OF THE WOODS

Breaking economy news. 225,000 more nonfarm payroll jobs looked to beat market expectations, but stock index futures lost ground anyway from a loss of 64 points when the data were released at 830am EST; bonds were 1.62%. Maybe this is as good as it gets for the labor market, and the economy as well. Monthly jobs over 200 thousand are usually good news, but pull back the tarp though and you can see that the economy's foundation needs some shoring up. 225 thousand jobs doesn't mean the economy is out of the woods and facing fewer risks down the road ahead.



Manufacturing jobs fell 12 thousand despite the purchasing managers saying the sector is no longer in a recession. Motor vehicles and parts jobs fell 10.6 thousand. Construction jobs jumped 44 thousand where specialty contractors are in demand both residential and nonresidential. More evidence the baby boom generation isn't retiring from their homes.

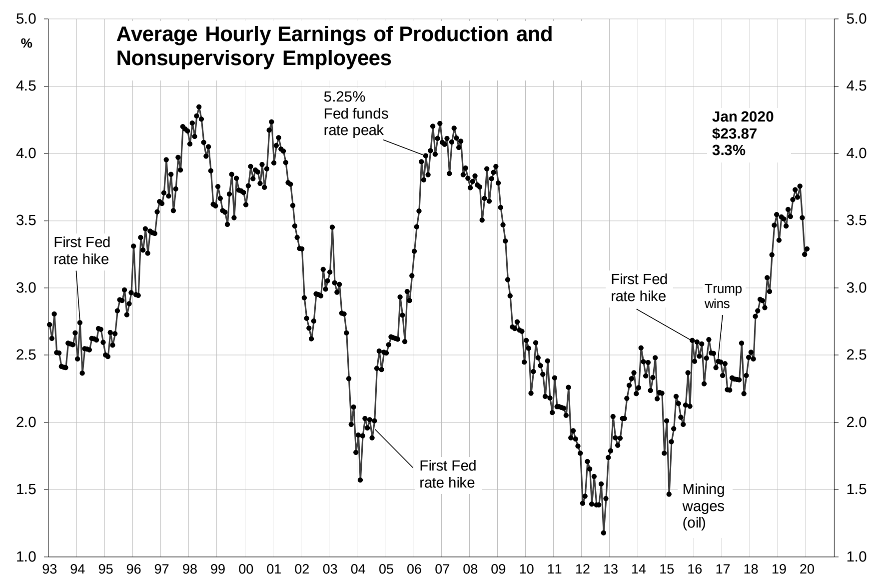
	Jan	Dec	Nov	Oct	Sep	Aug
Payroll jobs (000s)	225	147	261	185	208	207
Unemployment rate %	3.6	3.5	3.5	3.6	3.5	3.7
Unemployment (3 decimal)	3.579	3.496	3.536	3.563	3.507	3.660
Participation rate %	63.4	63.2	63.2	63.3	63.2	63.2
Average hourly earnings	$28.44	$28.37	$238.34	$28.24	$28.16	$28.16
MTM % Chg	0.2	0.1	0.4	0.3	0.0	0.4
YOY % Chg	3.1	3.0	3.3	3.2	3.1	3.5
Production Worker earnings	$23.87	$23.84	$23.81	$23.76	$23.70	$23.64
MTM % Chg	0.1	0.1	0.2	0.3	0.3	0.4
YOY % Chg	3.3	3.2	3.5	3.8	3.7	3.7

What else? Couriers and messengers went up 14 thousand and that won't last. Legal jobs up 4.5 thousand and we sure don't need any more lawyers. Education services looked too high by adding 24.9 thousand jobs.

The good not great characterization includes the president, his bragging rights, with the benchmark revision bringing down the number of jobs created in his administration. Since January 2017 when Trump took office 6.688 million jobs had been created to December 2019. Now today, January 2017 to December 2019 jobs created are 6.334 million, 354 thousand fewer, before tacking on January's 225 thousand gain. Good, pretty darn good, not as great.

Payroll jobs in year eleven following the recession

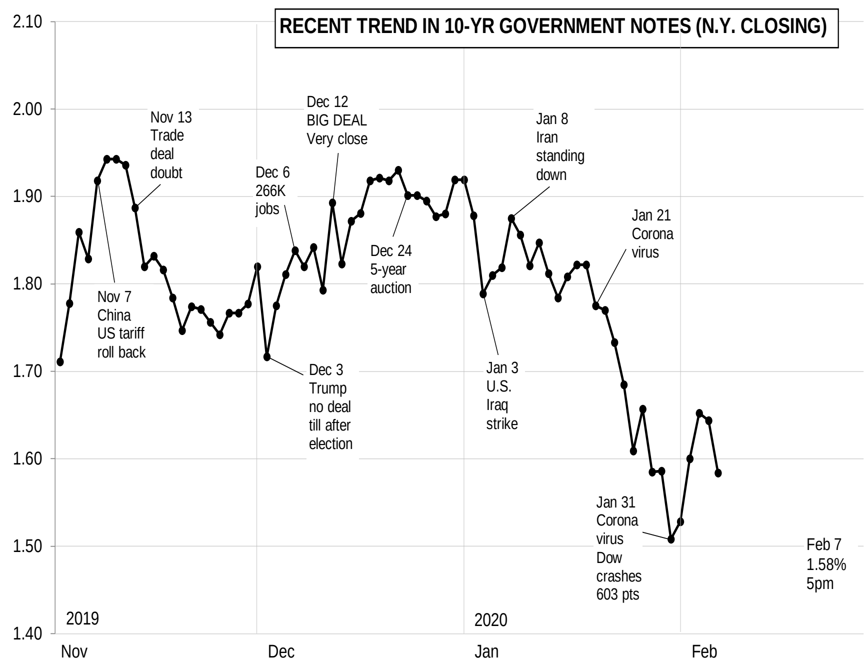
Dec. 2018 Totals millions		Jan 20	Dec 19	Nov 19	12 months Dec 18 to Dec 19	12 months Dec 17 to Dec 18
149.865	Nonfarm Payroll Employment	225	147	261	2096	2314
127.370	Total Private (ex-Govt)	206	142	247	1927	2200
20.948	Goods-producing	32	-5	45	178	622
0.692	Mining	-1	-10	-10	-32	50
12.805	Manufacturing	-12	-5	58	58	264
1.011	Motor Vehicles & parts	-11	1	41	-14	29
7.402	Construction	44	11	-2	148	309
106.442	Private Service-providing	174	147	202	1729	1598
27.666	**Trade, transportation, utilities**	27	59	12	155	201
15.704	Retail stores	-8	45	-14	-29	-98
3.080	General Merchandise	-14	5	27	-19	-4
3.072	Food & Beverage stores	2	-4	0	16	-12
5.538	Transportation/warehousing	28	4	23	124	257
1.522	Truck transport	3	-4	0	4	55
0.771	Couriers/messengers	14	7	16	81	72
1.167	Warehousing and storage	6	0	1	26	80
0.552	Utilities	-1	1	1	-4	-4
2.854	**Information**	5	8	9	28	35
8.665	**Financial**	-1	5	12	144	167
2.756	Insurance	1	-1	1	51	83
2.283	Real Estate	-2	2	6	65	62
1.389	Commercial Banking	-1	2	2	3	16
0.960	Securities/investments	-1	1	-2	8	17
21.128	**Professional/business**	21	14	37	367	445
2.993	Temp help services	-2	6	3	-42	26
2.401	Management of companies	-1	3	2	48	67
1.493	Architectural/engineering	-2	2	8	36	38
2.154	Computer systems/services	9	5	8	86	80
1.143	Legal services	5	-1	3	14	3
1.009	Accounting/bookkeeping	-4	1	-2	24	17
23.844	**Education and health**	72	22	73	614	461
5.158	Hospitals	10	6	11	86	62
3.719	Educational services	25	-3	16	85	16
16.415	**Leisure and hospitality**	36	36	43	365	225
2.052	Hotel/motels	-3	9	2	48	36
11.953	Eating & drinking places	24	16	23	247	146
22.495	Government	19	5	14	169	114
2.201	Federal ex-Post Office	12	0	7	43	18
5.173	State government	-13	-3	-3	5	14
2.489	State Govt Education	-16	-3	-3	-14	18
14.513	Local government	20	10	11	125	85
7.972	Local Govt Education	5	-1	4	60	31



Net, net, the monthly employment report was good not great this month because of nagging questions over its sustainability due to the darkening skies from the coronavirus fears and paradoxically, the lowest unemployment in a generation, which means companies are running out of a pool of workers to hire from to spur economic growth in the months and years ahead. Today's report isn't a material change in the outlook that Fed officials are waiting on to come off the sidelines with wages running 3.1% better than a year ago. We expect no change in Fed policy this year when it comes to interest rates and their balance sheet is likely to stop climbing much higher either.

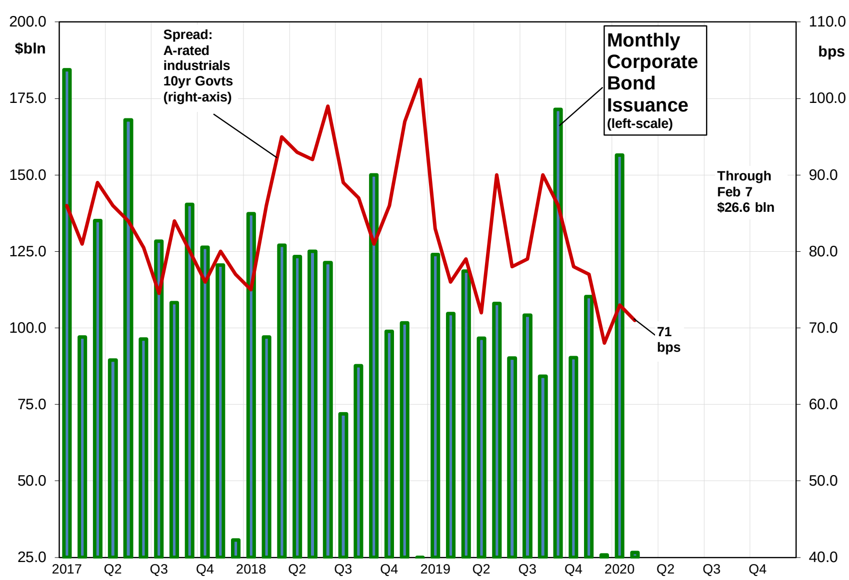
MARKETS OUTLOOK

	29-Mar 2019	28-Jun 2019	30-Sep 2019	31-Dec 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021	Q2 2021
30-Yr Treasury	2.81	2.53	2.11	2.39	2.30	2.30	2.40	2.50	2.60	2.70
10-Yr Note	2.41	2.01	1.67	1.92	1.85	1.90	2.10	2.20	2.30	2.40
5-Yr Note	2.23	1.77	1.55	1.69	1.65	1.75	1.90	2.05	2.15	2.25
2-Yr Note	2.26	1.76	1.62	1.57	1.60	1.70	1.80	2.00	2.10	2.20
3-month Libor	2.60	2.32	2.09	1.90	1.90	1.90	1.90	1.90	1.90	1.90
Fed Funds Rate	2.50	2.50	2.00	1.75	1.75	1.75	1.75	1.75	1.75	1.75
2s/10s spread	15	25	5	35	25	20	30	20	20	20



The coronavirus fears came back at the end of the week. There has to be some reason to blame for the decline in bond yields on Friday after the better than expected 225K jobs report. The coronavirus is there as a risk for economic growth in the Fed's semiannual Monetary Policy Report released Friday. "More recently, possible spillovers from the effects of the coronavirus in China have presented a new risk to the outlook." Not a great time to warn about risks in the report when you say the stock market rose "nearly 30 percent in 2019" and "valuation pressures are elevated." The odds of a 25 bps rate cut to 1.5% at the June 2020 Fed meeting are 58% and 13 bps of a second rate cut this year to 1.25% at the December 2020 Fed meeting are discounted.

CORPORATE BONDS: CENTENE CORP, SOUTHWEST AIR, PROLOGIS, HYUNDAI



Corporate offerings were $26.6 billion in the February 7 week versus $12.9 billion in the January 31 week. On Monday, Stanley Black & Decker sold $1.50 billion 10s/30s. It priced a $750 million 2.3% 10-yr (m-w +15bp) at 82 bps (Baa1/A). The power tool manufacturer will use the proceeds for general corporate purposes including funding of any acquisitions and repayment of borrowings. Corporate bond yields (10-yr Industrials rated A2) were 71 bps above 10-yr Treasuries Friday versus 73 bps last Friday.

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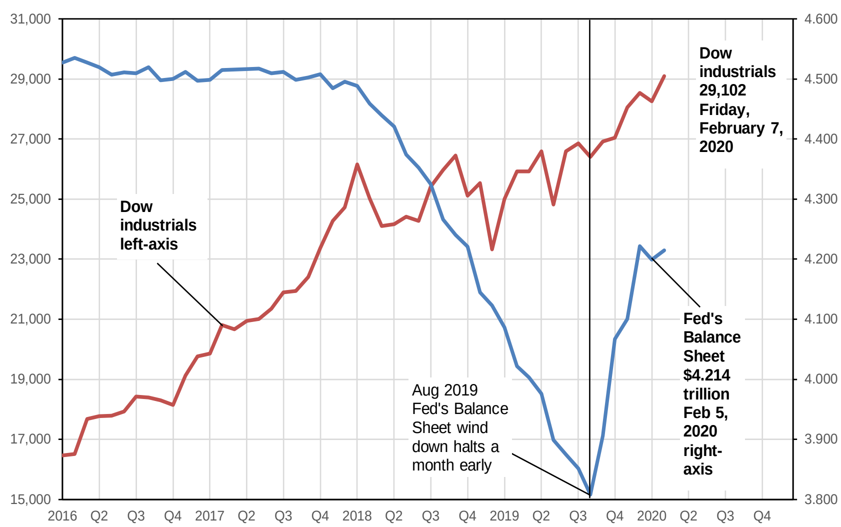
FEDERAL RESERVE POLICY

The Fed meets March 17-18, 2020 to consider its monetary policy. The payroll employment report on Friday showed more than 200 thousand jobs were added in January, but this is unlikely to register with Fed officials who are concentrating on a material change in the outlook. It's nice that there are more jobs, but the reality is growth has been about 2% the last three quarters, hardly a sign that the economy is overheating in year eleven of a record expansion. Fed Vice Chairman for Supervision Quarles (yes, two Vices now) addressed the club we were president of in New York on Thursday night before the jobs report. He said there has been "an apparent decline in the equilibrium interest rate" since the financial crisis over a decade ago that the Fed can't stop talking about and believes it has complicated the conduct of its monetary policy. He said he is in the camp that believes there is still slack in the labor market, he is a lawyer as is Fed Chair Powell, and that there is more slack means nothing to us in the forecasting business on interest rates other than this is an additional reason the Fed will not be raising interest rates again from 1.75% any time soon. OK boomer. The generation is still waiting for their just rewards of higher interest rates for their retirement savings. Powell recently spoke on the reasons why rates were low, speaking as a lawyer by training, he said Congress had assigned them the job to use their tools to pursue maximum employment and stable prices, and, and, and, essentially more people benefit from low interest rates than those savers who could benefit from higher interest rates… "those are our orders from Congress." OK boomer. The Fed Chair is aiming to give you more inflation that increases your cost of living and then maybe you can get your higher rates on savings.

Selected Fed assets and liabilities

Fed H.4.1 statistical release billions, Wednesday data	5-Feb	29-Jan	22-Jan	15-Jan	Sep 10 2008** pre-LEH
Factors adding reserves					
U.S. Treasury securities	2427.880	2409.108	2381.020	2362.635	479.782
Federal agency debt securities	2.347	2.347	2.347	2.347	0.000
Mortgage-backed securities (MBS)	1387.289	1387.288	1398.642	1404.318	0.000
Repurchase agreements	170.250	175.125	186.076	229.468	126.750
Primary credit (Discount Window)	0.000	0.034	0.000	0.009	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)	0.000	0.000	0.000	0.000	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	0.048	0.051	0.054	0.059	62.000
Federal Reserve Assets	4214.9	4199.3	4194.1	4224.1	961.7
3-month Libor %	1.74	1.78	1.80	1.84	2.82
Factors draining reserves					
Currency in circulation	1794.675	1792.779	1794.751	1795.725	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Reverse repurchases w/others	4.112	0.300	15.604	0.068	0.000
Reserve Balances (Net Liquidity)	1652.873	1612.223	1609.594	1673.362	24.964
Treasuries within 15 days	53.364	28.266	23.659	14.867	14.955
Treasuries 16 to 90 days	115.176	135.202	126.629	131.504	31.549
Treasuries 91 days to 1 year	378.638	378.533	369.212	349.598	69.272
Treasuries over 1-yr to 5 years	917.955	908.219	902.619	907.750	170.807
Treasuries over 5-yrs to 10 years	319.329	315.598	315.605	315.612	91.863
Treasuries over 10-years	643.419	643.290	643.297	643.304	101.337

**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08



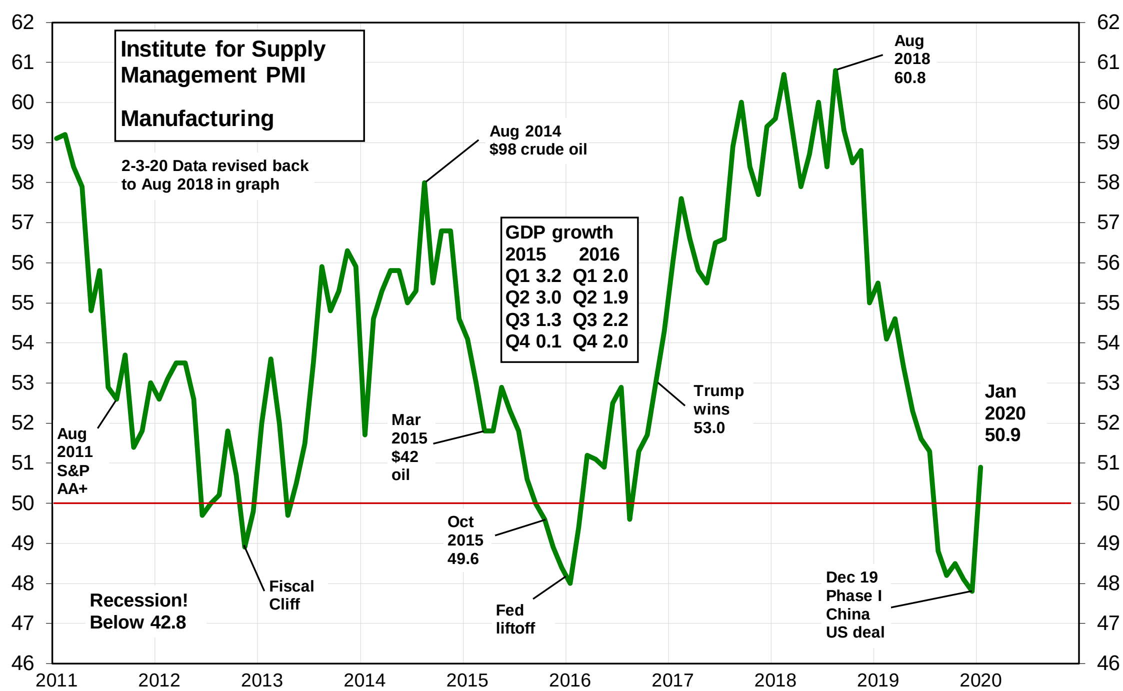
Speaking of Powell, the February hearings on the semiannual monetary policy report are next week: Tuesday before the House Financial Services Committee at 10am EST and Wednesday before the Senate Committee on Banking, Housing, and Urban Affairs. The report itself was released on Friday and we hope he gets another question on why the stock market is overvalued. The stock market doesn't matter much for the economy though the Monetary Policy Report said: "Equity wealth is more concentrated among high-wealth households with high propensities to save… and may therefore provide less support for consumption." Maybe as a matter of public policy interest rates should remain low to encourage babyboom retirees to spend not save the money to make the economy go.

OTHER ECONOMIC NEWS THIS WEEK

Manufacturing recession is officially over... for now (Monday)

Breaking economy news. The ISM manufacturing index signaled the manufacturing recession is over by vaulting the 50 level that separates a declining factory sector from a winning one. The January index is 50.9, up from a revised 47.8 in December (had been 47.2). One thing is for certain, if manufacturing is back in the money, then the broader economy is right behind it. Economists may have to recheck their calculations because the Boeing production shutdown of the 737 Max is making a less of a dent in the manufacturing outlook than many had feared. If you are looking for the smoking gun reason why the outlook for manufacturing suddenly brightened, look no further than the phase one China-U.S. trade agreement announced to the world by presidential tweet on December 12. There was clearly a lot of worry on the part of purchasing managers that the trade war escalation could not be stopped. A month after the trade agreement, business confidence soared.

Net, net, manufacturing executives are planning to hit the year running as they say their operations and orders and production are all back in the black. Manufacturing was one of the tea leaves arguing the U.S. economy was sliding toward recession, and now that company executives are more bullish about the 2020 outlook, the word recession needs to be banished by stock market investors permanently. Don't worry about earnings, if the economy's humming then the earnings are coming. There's nothing holding the economy back now with purchasing manager executives saying they are baaack! This economy can't be stopped. Bet on it.



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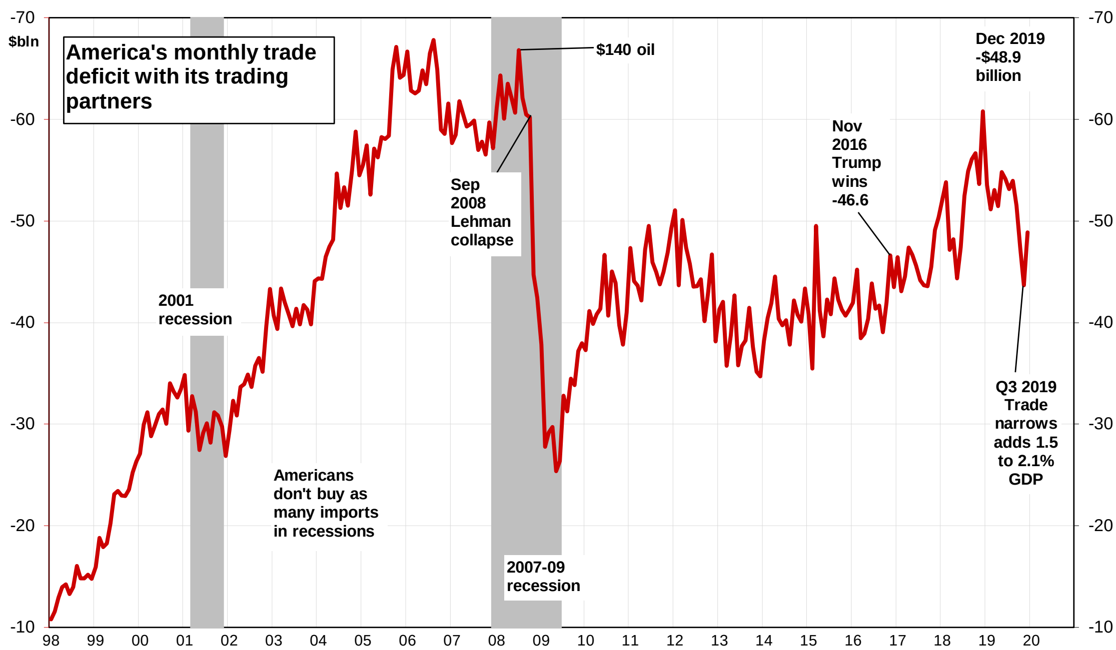
Trade deficit narrows in 2020 and the best is yet to come for Americans (Wednesday)

Breaking economy news. The trade deficit for December which closes out the year. Oh, and a huge 291K private payroll jobs number from ADP this morning at 815am that has us scratching our heads. The last time the real jobs number from the Bureau of Labor Statistics (BLS) for private jobs was this strong was 243K in November before last month's December 139K soft patch.

The trade deficit widened to $48.9 billion in December from $43.7 billion in November which will start to make a dent in economic growth if it continues. The coronavirus effect on world trade won't be seen for a while. Transportation networks are still largely in place and export and import orders were made months earlier. The world economic outlook faces coronavirus risks, but the effect on growth should just be temporary. Just ask the stock market if world trade is going to go off the rails and cause a world recession. Stock investors don't believe it.

Net, net, America may be on its way to winning the trade war from the forces of globalization that disrupted domestic factory production and led to millions of manufacturing worker layoffs the last twenty years, but the battle still has a ways to go before victory. The trade deficit in goods with the world was $852.9 billion in 2019 down just 2.5% from $874.8 billion in 2018. The China goods deficit is down 17.6% to $345.6 billion in 2019 from $419.5 billion in 2018 which shows the Trump trade officials that tariffs do indeed work if you choose the stick in the carrot and stick approach to weaning American companies away from supply chain inputs manufactured elsewhere. More work needs to be done with the European Union however as the trade deficit is $177.8 billion in 2019, an increase of 5.5% from $168.7 billion in 2018. The Trump dream of zero, zero, zero for trade tariffs, trade barriers and zero government subsidies is still a dream and years away from ever being realized. Stay tuned. Story developing.

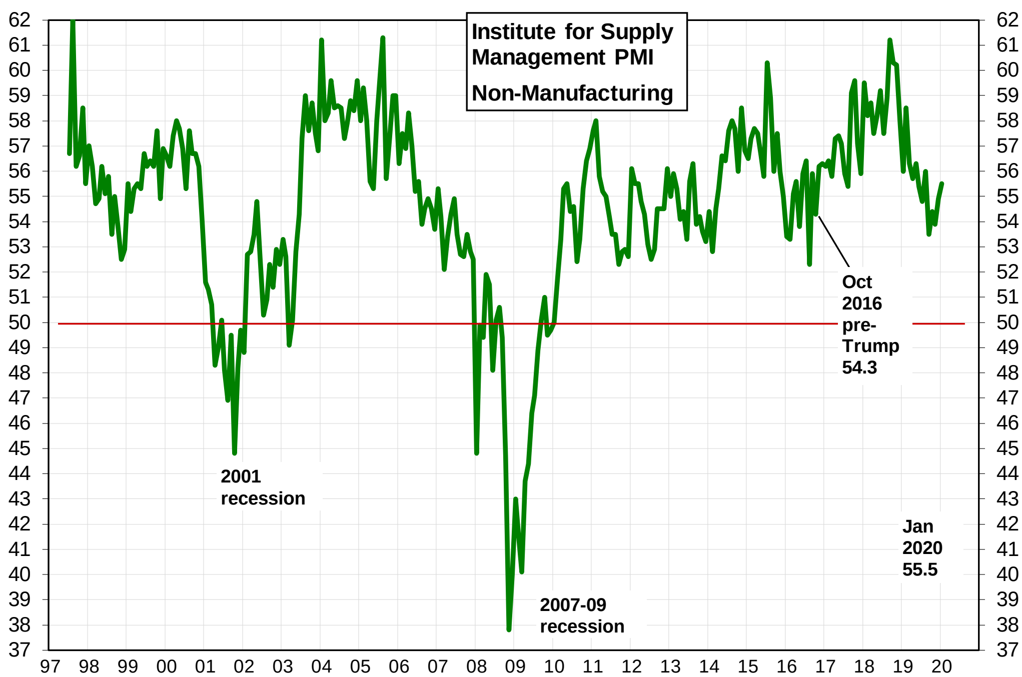


Services economy warming up (Wednesday)

Breaking economy news. The ISM non-manufacturing index improved to 55.5 in January from 54.9 in December. There were 12 service industries growing, but 6 industries were in decline including: Transportation & Warehousing; Wholesale Trade; Other Services; Arts, Entertainment & Recreation; Mining; and Real Estate, Rental & Leasing.

It was interesting that management said the labor market continues to be a challenge, impacting capacity and pushing up costs. You need capital and labor to make the economy grow and while there is plenty of money in companies' pockets, time will tell if growth slows later this year or in 2021 as there is virtually no one left to hire after this record expansion of nearly 11 years.

Net, net, services company executives say their businesses continue to see improvement from the weakness seen in late 2019. Activity isn't as strong as it was in late 2018 before tighter monetary policy, a government shutdown, and escalation of the trade war brought the confidence of those in the services sector down. The relatively low assessment of current economic conditions from service sector executives is likely to make the Fed think twice about raising interest rates again. The economy is warming up, but it's not overheating.

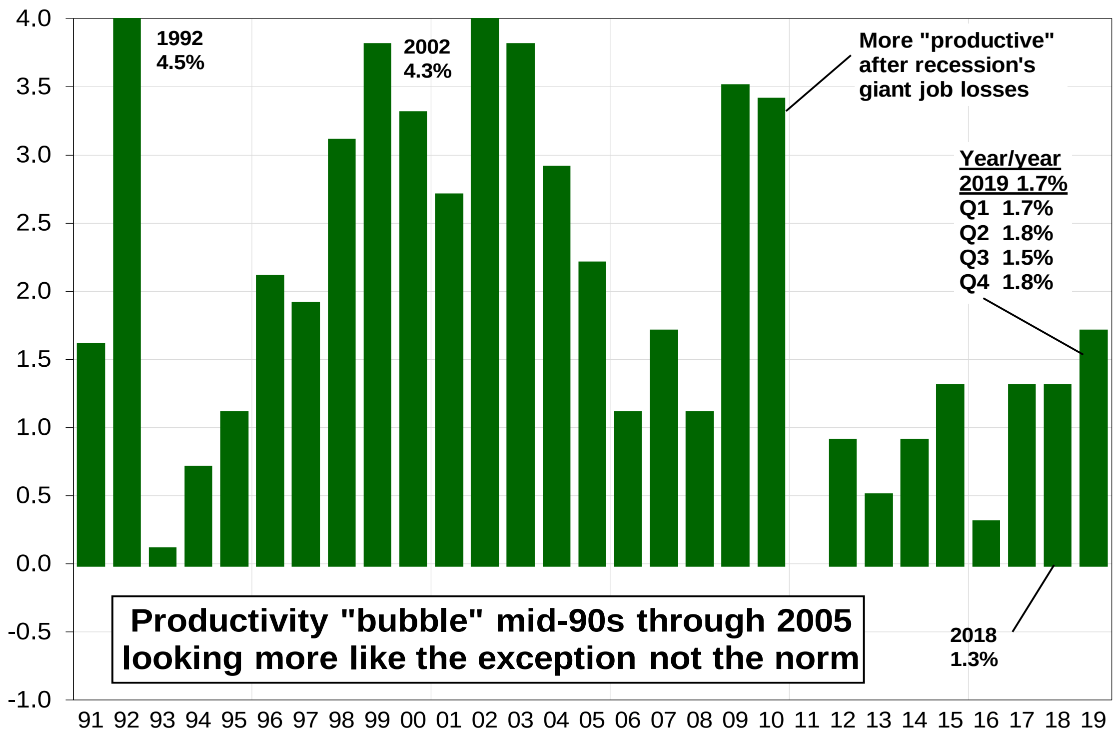


Tight labor market squeezes out productivity gains necessary for growth (Thursday)

Breaking economy news. Productivity in the fourth quarter rebounded to 1.4% after falling 0.2% in the third quarter. The labor market is tight with jobless claims falling back to 202 thousand in the February 1 week so there are fewer workers to shoulder the workload. Companies are getting more bang for the buck out of their employees as many job openings remain unfilled with no one available to hire in one of the strongest labor markets in the nation's history where the economy is at full employment. The tight labor market squeezes out the productivity gains necessary for growth with full year nonfarm business productivity rising 1.7% in 2019 following a 1.3% gain in 2018 and 1.3% gain in 2017. The economy's on a roll three years in a row so it's no wonder why the stock market is at record highs.

Net, net, the 2020 outlook continues to brighten as productivity gains remain sufficient to support economic growth this year. Productivity is doing better than expected and we know why. It's the labor market stupid, it's tight as a drum and there are fewer workers to shoulder the workload at companies across the country.

It's not all good news of course. Thankfully so for the dismal economics profession. A lot of an economy's productivity gains are dependent on investment spending and it is a concern that businesses are making fewer capital expenditures to prepare for growth later this year and beyond. Stay tuned. Story developing. Productivity is solid and keeps the recession odds low for now, but if companies don't increase their investment spending, then productivity is likely to slow in the years to come. Bet on it.



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