WEALTH MANAGEMENT INTERNATIONAL, LTD.

Proactive Investment Management & Financial Planning

# Weekly Economic Recap & Comment

## Week Ended October 5, 2018

As usual, we focused heavily this week on the monthly employment report. According to the report, ***September nonfarm payrolls*** increased only weakly by a seasonally-adjusted 134,000, falling far short of the revised gain of 270,000 in August and the average rise of 211,400 over the last year. However, much of that weakness apparently stemmed from hurricane disruptions on the East Coast last month. Other parts of the report suggested the demand for labor remains very high, while the availability of workers has become extremely low. In fact, the ***September unemployment rate*** declined to a nearly 50-year low of just 3.7%! Perhaps most important, the data showed that the tightness in the labor market is now boosting wages much faster. ***September average hourly earnings*** rose to $27.24, up a strong 0.3% for the third straight month. Hourly earnings in September were up a robust 3.5% from the same month one year earlier. The figures were consistent with our belief that the economy is not only growing briskly again, but it is also growing so fast that it is outrunning its resource base and pushing up inflation. Because of the continued economic growth, we expect higher corporate profits and rising stock prices in the near term. We are therefore maintaining a significant exposure to equities for the time being (in our strategies that include them). However, with demand rising faster than supply in a wide range of industries, we also think price pressures will keep intensifying. We still think broad, long-standing factors such as population aging and new technologies will ultimately limit how bad inflation can get. All the same, excess demand is creating a risk that the Federal Reserve may start hiking interest rates more aggressively, or that rising costs will eventually start to weigh on supply and demand. There are also yellow flags in the government policy environment, such as risky posturing in national security and international trade disputes. Finally, stocks are trading at high valuations, making them vulnerable to selling. Taking these risks into account, we recently started to cut our exposure to stocks and other risky assets, especially in our strategies that aim to be more conservative. If the data keeps coming in like it has been, we expect to cut risk further in the coming months.

In other data on the demand for labor, ***initial jobless claims in the week ended September 29*** fell by a seasonally-adjusted 8,000 to 207,000. The four-week moving average of claims also stood at 207,000, close to its lowest level in 50 years. With initial applications for unemployment benefits so minimal, it's clear that layoffs remain low, and/or jobs are so plentiful that those who do get laid off rarely bother to apply for benefits.

The strong labor market has buoyed consumer optimism and encouraged ever greater consumption spending, helping create good business conditions for the production side of the economy. Reflecting that, the Institute for Supply Management said this week that its ***September ISM nonmanufacturing index*** jumped to a record high of 61.6 from 58.5 in August and 55.7 in July. The ***September ISM manufacturing index*** pulled back a bit to 59.8, but that was still close to the 14-year high of 61.3 that it reached in August. The ISM indexes are designed so that readings over 50 point to expanding activity, so the latest figures suggest both the services sector and the manufacturing sector are continuing to grow quite broadly.

In data on the manufacturing sector farther back in time, ***August factory orders*** rose by a seasonally-adjusted 2.3%, easily erasing their revised 0.5% decline in July. That means factory orders have now risen in eight of the last twelve months. Most of the rise over the last year has come from increased orders for durable goods, but orders for nondurables have also risen at a good clip. Overall factory orders in August were up a robust 10.4% from a year earlier, with durable orders up a whopping 13.1% and nondurable orders up 7.7%.

Good trends can also be seen in the building industry. ***August construction spending*** merely edged up by a seasonally-adjusted 0.1%, after a rise of 0.2% in July, but that still marked the tenth monthly spending gain in the last twelve months. As a result, overall construction spending in August was up a healthy 6.0% from a year earlier. Perhaps the most intriguing aspect of the report was that most of the recent increases have come from rising outlays on public works projects – an area that had been essentially flat for years. August public works spending was up 13.0% year-over-year, while outlays on commercial projects were up 4.2% and outlays on private residential construction were up just 3.3%.

The growing demand and rising output reflected in the reports above explain much of the increased inflation pressure we're seeing, but dwindling inventories of

available resources are the most direct source of the pressure. In data on the nation's energy sector, ***commercial crude oil inventories in the week ended September 29*** jumped by 7.975 million barrels, marking their second straight weekly gain and lifting stockpiles to a total of 403.964 million barrels. However, inventories were still 6.0% below their five-year moving average (an industry benchmark that suggests supply and demand are in balance). Just as important, the data suggested producers are no longer able to boost production like they did over the last few years. The data showed ***domestic crude oil production in the week ended September 29*** was unchanged at a record high of 11.100 million barrels per day, but that was only slightly above the range it's been in since early summer. Against a backdrop of continued economic growth and rising usage around the world, we think stagnating U.S. production should help keep inventories in check and put additional upward pressure on prices. We are therefore maintaining our exposure to broad commodity funds in our more aggressive portfolios.

Finally, in a report on the international sector, the ***August trade balance*** showed a seasonally-adjusted deficit of $53.2 billion, expanding from the revised deficits of $50.0 billion in July and $45.7 billion in June. The widening in the deficit appeared to stem mostly from the appreciating dollar and retaliatory tariffs against U.S. goods by countries engaged in a trade war with the United States. U.S. exports fell to $209.4 billion in August, for their third straight monthly decline, while imports rose strongly to $262.7 billion. Compared with August 2017, exports were up 7.1%, but imports were up an even stronger 9.6%.

Patrick Fearon, CFA
Chief Investment Officer

## Upcoming U.S. Data

| Date | ET | Release | For | Consensus Forecast | Prior |
|---|---|---|---|---|---|
| 9-Oct | 6:00 | NFIB Small Business Optimism Index | Sep | NA | 108.8 |
| 10-Oct | 7:00 | MBA Mortgage Applications Index | 6-Oct | NA | 0.00% |
| 10-Oct | 8:30 | PPI | Sep | 0.20% | -0.10% |
| 10-Oct | 8:30 | Core PPI | Sep | 0.20% | -0.10% |
| 10-Oct | 10:00 | Wholesale Inventories | Aug | 0.80% | 0.60% |
| 11-Oct | 8:30 | CPI | Sep | 0.20% | 0.20% |
| 11-Oct | 8:30 | Core CPI | Sep | 0.20% | 0.10% |
| 11-Oct | 8:30 | Initial Claims | 6-Oct | 205K | 207K |
| 11-Oct | 8:30 | Continuing Claims | 29-Sep | NA | 1650K |
| 11-Oct | 10:30 | EIA Natural Gas Inventories | 6-Oct | NA | +98 bcf |
| 11-Oct | 11:00 | EIA Crude Inventories | 6-Oct | NA | +8.0M |
| 11-Oct | 14:00 | Treasury Budget | Sep | NA | $7.9B |
| 12-Oct | 8:30 | Export Prices | Sep | NA | -0.10% |
| 12-Oct | 8:30 | Export Prices ex-ag. | Sep | NA | -0.20% |
| 12-Oct | 8:30 | Import Prices | Sep | NA | -0.60% |
| 12-Oct | 8:30 | Import Prices ex-oil | Sep | NA | -0.10% |
| 12-Oct | 10:00 | Univ. of Michigan Consumer Sentiment - prelim | Oct | 100 | 100.1 |

*Source: Briefing.com*

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