Weekly Economic Recap & Comment

Week Ended January 25, 2019

Since many federal agencies remain closed because of the ongoing budget impasse, it was another week with only a few economic releases. The key report that did come out showed ***initial jobless claims in the week ended January 19*** dropped by a seasonally-adjusted 13,000 to just 199,000 – the lowest reading since November 1969! The four-week moving average of claims fell to 215,000, which was also one of its lowest readings in decades. With initial applications for unemployment benefits that low, it's clear that the demand for labor remains very strong, and layoffs are still quite limited. That's boosting consumer spending and powering the economy forward. Until recently, strong demand growth was putting upward pressure on inflation and interest rates, but it now appears the Federal Reserve's rate hikes to date and the strong dollar have brought inflation under control again. The pullback in inflation may also reflect the broad, long-standing factors we've been talking about (new shopping technologies, population aging, post-recession frugality, etc.). In any case, the Fed is now signaling it will slow the pace of its rate hikes going forward, which may give the economy room to keep running. That should keep corporate profits on the upswing, so we're maintaining a significant exposure to equities for the time being (in our strategies that include them). The problem is that the Fed's move to take its foot off the brakes may not have been as perfectly timed as we all hope. On the one hand, we think there's a significant risk that the strong labor market and continued demand growth will boost inflation again and force the Fed to keep hiking rates. On the other hand, in an economy that is much less dynamic than in decades past, there's a chance the cost increases and rate hikes to date have already done their damage, and growth could now slow substantially. On top of that, foreign demand is still weakening a lot, which will hurt not only exporters but also U.S. firms that produce and sell abroad. There are also yellow flags in the government policy environment, such as risky posturing in national security and international trade disputes, and political risks are increasing as investigators make more progress in their examination of high-level scandals. Because of those risks, we still expect to gradually cut our stock exposure further over time.

In fact, all the other economic reports that came out this week underlined the downside risks that are still in place. For example, the National Association of Realtors said ***December existing home sales*** plunged by a seasonally-adjusted 6.4% to an annualized rate of just 4.99 million units. Not only was the selling rate down 10.3% from the same month one year earlier, but it was also the weakest selling rate since November 2015. According to the report, the median price of a re-sale home came in at $253,600 during December, for an increase of just 2.9% year-over-year. We think the slide in the housing market is a prime example of the economic damage that has already been caused by rising input costs and higher interest rates. More recently, mortgage rates have started to come down again, but it remains to be seen whether they'll fall far enough to give the housing market a second wind.

We also saw yellow flags in a private-sector index that is designed to show how the economy is will perform over the coming six months or so. The Conference Board's ***December index of leading economic indicators*** fell 0.1%, after a rise of just 0.2% in November and an October decline of 0.3%. The decline in December came mostly from the steep drop in the stock market that month, but the reading was also held back by weaker growth in manufacturers' new orders. The choppy performance of this index suggests to us that the economy is hitting more headwinds and will probably grow more slowly in the near term.

Finally, the week included a report that provided good news on inflation pressure and interest rates but perhaps less positive news for future economic activity. The data showed ***commercial crude oil inventories in the week ended January 19*** jumped by 7.970 million barrels, easily erasing the modest declines in recent weeks and leaving total stockpiles at a nearly two-month high of 445.025 million barrels. Total inventories stood a significant 2.2% above their five-year moving average (an industry benchmark that suggests supply and demand are in balance). The report said ***domestic crude oil production in the week ended January 19*** remained at a record high of 11.900 million barrels per day. In spite of continued U.S. economic growth, rising usage around the world, and reduced exports from big producers (such as Iran and Venezuela), it's now clear that high production and excess inventories could keep weighing on the market. Oil prices have recently been recovering after they fell in tandem with stocks during the fourth quarter, but we wonder if there may be limits to the rebound. We have therefore started to exit the broad commodity funds that we have been holding in some of our more aggressive strategies. In addition, we think there is a significant risk that continued low energy prices will further discourage new drilling and oil field development in the coming months and quarters. If so, that would tend to weigh on overall U.S. economic activity and corporate profits.

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Chief Investment Officer

Upcoming U.S. Data

Date	ET	Release	For	Consensus Forecast	Prior
29-Jan	8:00	S&P Case-Shiller Home Price Index	Nov	NA	5.00%
29-Jan	8:30	Adv. Intl. Trade in Goods	Dec	NA	NA
29-Jan	8:30	Adv. Retail Inventories	Dec	NA	NA
29-Jan	8:30	Adv. Wholesale Inventories	Dec	NA	NA
29-Jan	10:00	Consumer Confidence	Jan	NA	128.1
30-Jan	7:00	MBA Mortgage Applications Index	26-Jan	NA	-2.70%
30-Jan	8:15	ADP Employment Change	Jan	NA	271K
30-Jan	8:30	Pending Home Sales	Dec	NA	-0.70%
30-Jan	10:30	EIA Crude Oil Inventories	26-Jan	NA	+8.0M
30-Jan	14:00	FOMC Rate Decision	Jan	NA	2.38%
31-Jan	8:30	Personal Income	Dec	NA	NA
31-Jan	8:30	Personal Spending	Dec	NA	NA
31-Jan	8:30	Employment Cost Index	Q4	NA	NA
31-Jan	8:30	Initial Claims	26-Jan	NA	199K
31-Jan	8:30	Continuing Claims	19-Jan	NA	1713K
31-Jan	9:45	Chicago PMI	Jan	NA	65.4
31-Jan	10:30	EIA Natural Gas Inventories	26-Jan	NA	-163 bcf
1-Feb	8:30	Nonfarm Payrolls	Jan	NA	312K
1-Feb	8:30	Nonfarm Private Payrolls	Jan	NA	301K
1-Feb	8:30	Average Hourly Earnings	Jan	NA	0.40%
1-Feb	8:30	Unemployment Rate	Jan	NA	3.90%
1-Feb	8:30	Average Workweek	Jan	NA	34.5
1-Feb	10:00	Construction Spending	Dec	NA	NA
1-Feb	10:00	ISM Manufacturing Index	Jan	NA	54.1
1-Feb	10:00	Univ. of Michigan Consumer Sentiment - Final	Jan	NA	90.7

Source: Briefing.com