Summary

Economic data for the week included ISM services continuing to improve into solid expansion and an employment situation report for December that came in far stronger than expected.

Equities fell back, along with the positive economic news pointing to less Fed policy easing action. Bonds accordingly fell as long-term interest rates rose ever higher. Commodities fared positively, with gains in all major groups.

Economic Notes

(+) The **ISM services/non-manufacturing index** for December rose 2.0 points to a level of 54.1, above the tempered expectations calling for 53.5. Under the hood, new orders rose a half-point to over 54, with business activity rising nearly 5 points to 58. On the other hand, employment fell by a tenth of a percent but stayed moderately expansionary. Prices paid also accelerated by over 6 points to a level of 64—quite strong. This closely-watched services index remains quite strong, as it has over the past few years, with the only wrinkle being survey respondents noting anecdotally that the possibility for higher tariffs is weighing on activity and potentially business decisions, due to concerns specifically over what was described as "supply chain disruptions" and "chaos in pricing."

(-) The preliminary **Univ. of Michigan index of consumer sentiment** for January fell by -0.8 of a point to 73.2, below the unchanged 74.0 expected. This included a gain of about three points in assessments of current conditions, while future expectations declined by a similar amount. Inflation expectations for the coming year rose by 0.5% to 3.3%; those for the next 5-10 years rose by 0.3% to 3.3% as well. It was noted that if the 5-10 year figure held steady through the final sentiment report, it would be the highest in nearly 30 years. This went along with anecdotal commentary that from the survey sponsor about upcoming policy fears, that "inflation expectations rose across multiple demographic groups, with particularly strong increases among lower-income consumers and independents."

(+) The **JOLTs** job openings report for October showed an increase of 259k to 8.098 mil., above the median forecast that called for 7.740 mil. By segment, the strongest gains came in professional/business services (273k), financial (114k), and private education/health (81k); the largest declines were in information (-89k), leisure/hospitality (-83k), and manufacturing (-56k). The job openings rate rose a tenth to 4.8%, while the hiring rate declined a tenth to 3.3%. On the departure side, the quits rate fell by -0.2% to 1.9%, while the layoff rate was flat at 1.1%. The latter categories all remain below the pre-pandemic pace, while the overall report didn't show signs of labor deterioration broadly.

(0) **Initial jobless claims** for the Jan. 4 ending week fell by -10k to 201k, well below the 215k expected. **Continuing claims** for the Dec. 28 week rose by 33k to 1.867 mil., a bit above the median forecast of 1.860 mil. Claims were mixed by state, pointing to no clear trend. In addition, the end of the year includes some seasonal effects, which skew the data somewhat, but should dissipate over the next few weeks.

(+) The employment situation for December came in stronger than expected, and was far from celebrated by markets, which assumed that the strength translated directly to fewer Fed rate cuts this year. **Nonfarm payrolls** rose by 256k, above the 165k expected. Revisions for the two prior months were minor, and offsetting, being slightly negative on net. By sector, gains were most pronounced in health care/social assistance (70k), retail (43k, general merchandise and clothing), leisure/hospitality (43k, mostly restaurants/bars), government (33k, mostly state/local), and professional/business services (28k). While markets were taken aback by the positivity, some of the bounceback appeared to be due to recoveries from recent labor strikes and hurricanes, as well as possible residual seasonal effects, which have affected employment data among other economic reports. One of the few weak areas, manufacturing of durable goods declined (-16k, mostly in computer equipment), as did petroleum extraction (-3k). The **unemployment rate** fell a tenth to 4.1% (on a non-seasonally-adjusted basis, it fell to 3.8%), along with household employment rising by 478k. The U-6 underemployment rate fell by -0.2% to 7.5%. **Average hourly earnings** rose 0.3%, equating to a gain over the past year of 3.9%, a tenth slower than the pace of the prior month. The **average workweek** length was unchanged at 34.3 for the fifth straight month.

As noted in recent JPMorgan research, there has been a sharp divergence in labor results over the roughly three years since March 2022. The **establishment survey** (or nonfarm payroll survey) has shown an addition of 8.2 mil. jobs, based on a sample of business and government agency payrolls (not agriculture). Statistical methods are used to estimate the impact of business formations and closures. In addition, it is based on a count of jobs, not workers, so multiple job holders can be double-counted. On the other hand, the **household survey** showed a gain of 3.5 mil. over that time. That's the survey that's used to generate the official unemployment rate, using Census Bureau data that includes agricultural workers and the self-employed, and counts each worker only once. While the two surveys have tended to move in the same direction over time, methodological differences create cloudiness surrounding the effects of immigration, part-time work, and other important labor market factors, especially after a shock as large as the pandemic. Due to the large size of the U.S. workforce, fluidity of employment, and the important fact that these are samples and not a full comprehensive universe, labor data has been difficult to analyze with precision. Annual benchmark revisions help to some extent. In short, economists take what they can get.

(0) The **FOMC minutes** from the December meeting featured a few quotes that were meaningful to markets in terms of committee thinking about present conditions. Perhaps capturing most of this was that the FOMC was "at or near the point at which it would be appropriate to slow the pace of policy easing." In so many words, this means fewer rate cuts than expected in 2025, which markets were unhappy with. Inflation, while improved, remains an important wildcard, with "most" FOMC participants noting that "disinflationary progress continued to be apparent," but "almost all" felt that risks toward higher inflation had risen as of late (many of which being related to the incoming presidential administration, even though many won't publicly allude to this). It was also noted that earlier fears about labor markets have abated a bit, although merited close watching. Most importantly, most of the committee sees goals and risks as "roughly in balance" at present, which, when translated to monetary policy actions, implies fewer interest rate actions, as that is their primary blunt tool.

Market Notes

Period ending 1/10/2025	**1 Week %**	**YTD %**
DJIA	-1.83	-1.38
S&P 500	-1.91	-0.89
NASDAQ	-2.34	-0.76
Russell 2000	-3.49	-1.82
MSCI-EAFE	-0.43	-0.73
MSCI-EM	-1.50	-1.63
Bloomberg U.S. Aggregate	-0.87	-1.00

U.S. Treasury Yields	**3 Mo.**	**2 Yr.**	**5 Yr.**	**10 Yr.**	**30 Yr.**
12/31/2024	4.37	4.25	4.38	4.58	4.78
1/3/2025	4.34	4.28	4.41	4.60	4.82
1/10/2025	4.36	4.40	4.59	4.77	4.96

U.S. stocks fell back as higher interest rates continued to weigh on sentiment, with small caps now having reached -10% correction territory since late November, while large caps have held on significantly better. The week was shortened by the Thur. market closure to commemorate former President Carter. From over the weekend into Monday, reports surfaced that incoming President Trump had plans to 'pare back' tariff levels relative to what had been announced during the campaign (causing a drop in the value of the U.S. dollar), although he refuted these same claims, resulting in further volatility. As ISM services, JOLTs, and non-farm payrolls came in stronger than expected, it ended up being a 'good news is bad news' dynamic yet again, as that points to a path of the Fed moving at a slower easing path that was earlier hoped. This is especially true, as continued sticky inflation remains a wildcard. As seen by recent consumer sentiment results, plenty of speculation is swirling around possible worst case scenarios surrounding foreign trade policy this year, such as maximum tariff levels across the board, as opposed to a political likelihood of more tempered actual policy. How closely draft political policy morphs into reality will be unveiled over the next several months.

By sector, energy, health care, and materials were the only positive sectors for the week, while the downside was led by technology, financials, and consumer discretionary. Real estate also fell by -4% along with the higher interest rates. New export rules from President Biden weighed on popular chip stocks. Earnings season began in earnest Fri., with reports for Q4 rolling in over the next several weeks, which could also add to market volatility, although forecasts overall are quite good (estimate for the S&P 500 of nearly 12% year-over-year earnings growth, per FactSet).

Foreign developed market stocks ended positively in local terms, but a stronger U.S. dollar turned these negative for the week. Gains in Europe were offset by sharp declines in Japan and emerging markets. Concerns in Japan continue to be centered on the timing and magnitude of the BOJ's expected monetary tightening policy. In Canada, Prime Minister Trudeau resigned, after a nine-year run, after a bout of recent growing unpopularity, which appears to be increasingly common with incumbent administrations around the globe, particularly as fiscal stresses are rising to the surface. In EM, Chinese stocks fell by over -4% as year-over-year inflation came in at 0.1%. While such a result might have been briefly cheered in the U.S. and Europe, levels this low border on deflation, as a byproduct of very slow consumer activity there that's been difficult to kickstart.

Bonds fared poorly last week, with the 10-year U.S. Treasury closing at nearly 4.8%, after having reached a high for the past year during the week, and the 30-year at a rounded 5.0%. The curve has solidly un-inverted from both the 10y-3m and 10y-2y measures, with the spike in long rates having outdone the sticky short rates. Floating rate bank loans fared best with flattish results, while Treasuries and investment-grade corporate indexes each fell just shy of a percent. Foreign bonds were held down by the stronger dollar and rising rates of their own.

U.K. 30-year gilt yields reached their highest levels in over 25 years (to over 5.3%), with higher-than-expected inflation readings, weaker economic growth (concerns over stagflation), fiscal policy, and potential foreign trade effects (with the U.S.) looking ahead. This type of rising rate scenario is what some have worried about for the U.S., although having the world's reserve currency (resulting in a strong U.S. dollar), ability to issue higher levels of debt that's readily absorbed by global markets, and a more diversified economy generally has kept these concerns at bay domestically so far. Smaller and moderately-sized economies have fewer tools at their disposal to offset internal and external effects, not to mention a more limited market for their debt, hence the added 'credit spread' that higher yields imply.

Commodities rose across the board last week, with energy and metals sharing leadership, with each group up a few percent each. Crude oil rose nearly 3% last week to $77/barrel, with a conflux of seasonal demand and tighter supplies, but mostly due to the Biden administration announcement Friday of broader sanctions on Russia's energy complex, that targeted producers, shippers, traders, and insurers, which will likely also weigh on global supplies. Natural gas spot prices rose by 8% last week, with added cold temperature forecasts across the U.S. in a peak usage period. Earlier in the week, the U.S. administration also permanently banned offshore drilling for over 600 mil. acres of the Pacific and Atlantic Oceans, which could require Congressional action to undo, and reducing potential long-term supply.

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, Univ. of Michigan, 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.

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