



MORNING BRIEFING

January 7, 2019

Patient Powell's Put

See the [collection](#) of the individual charts linked below.

(1) No recession in GDPNow model. (2) Credit market indicators say Fed is done tightening. (3) There was a December "flash recession" in Fed district surveys, led by drop in new orders. (4) A few leading indicators flashing yellow. (5) Labor market still booming. (6) Trucking indicators still barreling along. (7) Powell turns from hawk to dove. (8) Pressing the pause button. (9) Fed going from "gradual" to "flexible." (10) The Dow Vigilantes have gotten the Powell Put for now. (11) Powell concedes that financial markets matter. (12) Movie review: "Vice" (-).

US Economy: Flash Recession? There's still no recession evident in the Atlanta Fed's [GDPNow](#) forecasting model or in our forecast for this year. On Thursday, January 3, the model's estimate for real GDP growth in Q4-2018 was revised down to 2.6% from 2.7% on December 21. The Nowcasts of Q4's real consumer spending growth and real private fixed investment growth decreased from 3.7% and 2.7%, respectively, to 3.6% and 2.4%, respectively, after the release of the weak Manufacturing Report On Business from the Institute for Supply Management (ISM) last Thursday. After Friday's blowout employment report, the GDP forecast is bound to be revised higher.

The weakness in December's M-PMI was foreshadowed by the month's regional business surveys conducted by five of the Fed's district banks. They all suggested that economic growth is slowing rapidly and that inflation is moderating. The rapid falloff in these indicators during December was signaled by the flash crash in the S&P 500, which fell 9.2% during the month, the worst December since 1931. Arguably, the plunge in stock prices might have triggered a "flash recession" in the economy.

The "most hated bull market in history" has had frequent panic attacks on fears that "the most widely anticipated recession in history" is imminent. They were followed by relief rallies when the downturns didn't happen. While some of the latest data may be raising the odds of a recession, they are also raising the odds that our "data-dependent" Fed won't be raising interest rates in 2019, and might actually have to lower them, which would lower the odds of a recession and quickly reverse any flash recession that might be out there.

That's certainly the forecast of the fixed-income markets. Consider the following:

(1) *Interest rates going south.* The 12-month forward federal funds rate has dropped 64bps from last year's high of 2.88% on November 8 to 2.24% last Thursday ([Fig. 1](#)). In other words, this indicator suggests that the Fed won't be hiking the federal funds rate this year. The two-year Treasury note yield also tends to be a good year-ahead indicator of the federal funds rate. At 2.50% on Friday, it too is predicting that the Fed is done for the foreseeable future.

The bond market is sending the same message, as the 10-year Treasury yield has dropped from last year's high of 3.24% on November 8 to 2.67% on Friday ([Fig. 2](#)). Leading the way down has been the

embedded inflation expectations component of the bond yield. It has declined from 2.17% late last year to 1.76% on Friday ([Fig. 3](#)). The yield curve remains positive, but barely so at 30bps for the spread between the 10-year yield and the federal funds rate ([Fig. 4](#)).

Meanwhile, credit quality spreads have deteriorated as the high-yield corporate bond rose from 5.8% at the start of last year to 7.6% on Friday, with its spread over the 10-year Treasury at 491bps, well above the stable readings of around 350bps over the past two years ([Fig. 5](#) and [Fig. 6](#)). Memo to Fed officials from the credit markets: Take the year off.

(2) *Business surveys taking a dive.* The big shocker recently was the plunge in the average of the composite business indicators compiled by five of the Fed's district banks ([Fig. 7](#)). It dropped from 16.6 during November to 2.0 last month, the lowest reading since October 2016. The weakness was led by a flash crash in new orders, while employment remained solid. The orders index plummeted from 15.2 during November to 7.7 in December.

The national M-PMI is highly correlated with the average of the regional indicators. The overall M-PMI wasn't as weak as the regional average, but the orders component of the M-PMI flash crashed from 62.1 during November to 51.1 during December, the lowest reading since August 2016 ([Fig. 8](#)).

Previously, we've shown that the y/y growth rate in S&P 500 revenues per share is highly correlated with the M-PMI ([Fig. 9](#)). So the recent weakness in the latter suggests slower growth in the former. Then again, December's flash crash in the stock market (along with the "Tariff Man" in the White House and the Fed's "autopilot" for tapering its balance sheet) may have triggered the flash crash in new business orders last month. If China and the US make a trade deal and if the Fed turns dovish, then the flash recession could be just that.

(3) *Leading indicators peaking?* Then again, Debbie and I are keeping track of the 10 components of the Index of Leading Economic Indicators (LEI), and more of them have stopped flashing green. None are flashing red (though the bears are seeing this color in the S&P 500 component), but yellow is coming into fashion ([Fig. 10](#)).

We note that initial unemployment claims may have bottomed during December simply because they can't go much lower. The new orders component of the M-PMI is also a component of the LEI, and it took a dive last month, as noted above. There may not be much upside in building permits. Consumer expectations indexes were weak at the end of last year. The yield curve spread may be getting closer to zero, but it remains positive, which means it is one of the few components that actually might have boosted December's LEI!

(4) *Labor market still booming.* Widespread reports of labor shortages don't seem to jibe with the strength of monthly payroll gains. It may be taking longer to hire suitable candidates, and some may require training to make them suitable. However, Friday's December jobs report certainly helped to dispel the notion that the economy is either running out of workers because it is too strong or falling into a recession because it is too weak! There was no sign of a flash crash in that report. Instead, as Debbie discusses below, payrolls soared 312,000 last month, the best m/m gain since February 2018. Last year's gain was 2.6 million, up from 2.2 million during 2017.

Wages for all workers rose 0.4% m/m and 3.2% y/y ([Fig. 11](#)). Our Earned Income Proxy for total private-sector wages and salaries jumped 0.9% m/m during December—its biggest monthly gain since March 2014 ([Fig. 12](#)).

(5) *Truckers still trucking.* Furthermore, there's no recession in the trucking industry. It remains crash-

free as the trucks continue to barrel down our highways and byways. While there is a shortage of truck drivers, so far it hasn't depressed the ATA truck tonnage index, which rose to another record high in November ([Fig. 13](#)). Also at a new record high last month: payroll employment in the industry ([Fig. 14](#)).

The Fed: Powell Turns Dovish. On Friday, along with the blowout employment report, dovish remarks from Federal Reserve Chairman Jerome Powell sent the DJIA up 746 points. Speaking on a panel with former Fed chairs Janet Yellen and Ben Bernanke at the annual meeting of the American Economic Association and Allied Social Science Association in Atlanta, Powell emphasized that the monetary policy path is not on autopilot.

Powell's pronouncements over the past several months have contributed to the markets' going haywire since early October. In a 10/3 [interview](#), Powell said that the federal funds rate was a long way off from neutral. He also signaled that the Fed would not hesitate to raise interest rates beyond what is considered neutral and maybe even to restrictive heights. Since then, I have been in the Fed-watchers' camp that argues that the Fed should press the pause button on rate-hiking.

Powell inadvertently freaked out the markets again at his 12/19 [press conference](#) when he responded to a question on monetary policy as follows: "So we thought carefully about this, on how to normalize policy, and came to the view that we would effectively have the balance sheet runoff on automatic pilot and use monetary policy, rate policy, to adjust to incoming data."

The market has been adjusting—perhaps with unwarranted volatility—to Powell's pragmatic and transparent style. Meanwhile, Powell seems to be tweaking his messaging to achieve less haphazard market reactions. Powell tends not to be shy about speaking off the cuff. But after the two gaffes noted above, Melissa and I noticed that he read his preliminary comments on Friday from carefully prepared notes.

Back in September, the Fed had projected about three rate hikes for 2019. Following the December 18-19 meeting of the FOMC, Powell lowered that to two hikes. Investors are now speculating about the possibility of no rate increases or even a rate cut for 2019, with both scenarios consistent with Powell's dovish remarks. Powell's Friday comments on the Fed's balance sheet also suggested a marked shift in policy, as we discuss below.

Another big deal, in our opinion, is that equity markets suddenly seem to matter a lot more to Powell. According to him, the Fed is listening to the markets and may pause rate-hiking for a while. The Dow Vigilantes may have gotten their Powell Put! So equity investors may shift their focus to global economic growth, the China-US trade negotiations, the Q4 earnings season, and the government shutdown.

For now, let's have a closer look at Powell's dovish remarks:

(1) *Patience and flexibility.* Powell said that the Fed is willing to be "patient." He noted that to keep the US economic expansion on track, "there is no preset path for policy." He stated: "We will be prepared to adjust policy quickly and flexibly and use all of our tools to support the economy should that be appropriate."

Interestingly, Powell brought up the example of 2016 when the Fed expected to raise rates four times, but only did so once as the economy weakened. Later, the gradual path of rate hikes resumed. "No one knows whether this year will be more like 2016," he said. "But what I do know is that we will be prepared to adjust policy quickly and flexibly."

However, Powell sees US economic momentum moving into 2019 with strong jobs growth, low unemployment, higher labor force participation, and higher wages. He noted that the latest below-expectations ISM data isn't all bad, as it is consistent with ongoing growth and had previously been elevated above historical averages. In other words, these data aren't what is driving Powell's dovishness.

(2) *Muted inflation*. In the past, Powell has been wary of the models that drove policy for his predecessors. Powell has specifically questioned the relationship between wages and broader inflation. Confirming this view, he said on Friday that the "link between ... wage inflation and price inflation is pretty weak." He added: "Wages going up isn't necessarily inflation."

As noted above, average hourly earnings rose 3.2% y/y during December, the highest since April 2009. However, November's reading for the personal consumption expenditures deflator, the Fed's preferred inflation measure, was up 1.8% y/y in November, which is just shy of the Fed's stated 2.0% goal. Powell said: "With the muted inflation readings that we've seen coming in, we will be patient as we watch to see how the economy evolves."

Going forward, he said: "We have inflation under control" and "that's a pretty good outcome," which we expect to continue despite strong job growth, low unemployment, and stronger wage gains.

(3) *Markets matter*. Markets are "obviously well ahead of the data," but "we're listening very carefully," Powell said. The downside risks priced into the markets are "about slowing global growth, particularly related to China, about ongoing trade negotiations, about general policy uncertainty coming out of Washington," among other factors.

Powell noted that weak China data may be spilling over into emerging Asia and commodity prices, especially copper. However, he added that the Chinese authorities are stepping in with stimulus. The rest of the world is showing consistent growth, he said. Nevertheless, he stated that "policy is very much about risk management." And the Fed is considering the disconnect between the economy and the markets.

(4) *Balance sheet not on autopilot*. The Fed's balance-sheet reduction is not an "important part of the story," according to Powell. But "if we reached a different conclusion, we wouldn't hesitate to make a change." Following the 2008 recession, the Fed's quantitative easing programs led the Fed to grow its balance sheet to more than \$4.5 trillion. It has been rolling off \$50 billion per month since October 2017.

Some view this as quantitative tightening. So Powell's statement that the Fed is flexible (and not on "automatic pilot," as he had said during his December 19 presser) came as a relief to investors.

(5) *Declaration of independence*. Powell curtly responded to the question "Would you resign if Trump asked you to?" with a simple "no." In recent weeks, the media reported that the President would like to meet with Powell to discuss policy. Trump has been a vocal opponent of the Fed's interest-rate hikes. For now, it sounds as if there is no meeting scheduled between Powell and the President. Powell doesn't seem to be overly influenced by Trump's rhetoric. But Powell does seem to be increasingly influenced by the financial markets, which happen to agree with Trump.

Movie. "Vice" (-) ([link](#)) is another historical docudrama that is rife with inaccuracies, which reduces its credibility. The movie is about the political life of Dick Cheney, who served as vice president under George W. Bush. The movie's unflinching theme is that Cheney was power hungry and was directly responsible for the war in Iraq, waterboarding, global warming, and everything bad that has happened

to us since 9/11. At the end of the movie, Cheney's character, played eerily well by Christian Bale, addresses the movie's audience directly. He snarls and growls that he does not care how he is portrayed because he made the country safe. One person stands out as able to have stood up to Cheney, Secretary of State Colin Powell. He gave a speech at the UN on February 5, 2003 to drum up support for overthrowing Saddam Hussein. It was based on flimsy intelligence, and Powell knew it. In September 2005, Powell was asked about the speech during an interview with Barbara Walters and responded that it was a "blot" on his record. Imagine if he had refused to support the war. *Note: Best (+ + +) to worst (- - -).*

CALENDARS

US. Mon: ISM NM-PMI 58.4, Bostic. **Tues:** NFIB Small Business Optimism Index, JOLTS Report, Consumer Credit \$19.0b. (Econoday estimates)

Global. Mon: Germany Factory Orders, Eurozone Retail Sales, Japan C-PMI & NM-PMI. **Tues:** Germany Industrial Production, Japan Consumer Confidence. (DailyFX estimates)

STRATEGY INDICATORS

Global Stock Markets Performance ([link](#)): Last week saw the US MSCI index rise 1.9% w/w and rank 29th of the 49 global stock markets we follow in a week when 41/49 countries rose in US dollar terms. That compares to the prior week's 2/49 ranking, when the US MSCI gained 2.9% and 27 markets rose. The AC World ex-US index rose 1.2% w/w; that compares to a 0.5% rise a week earlier. EM Latin America was the best performer with a gain of 6.6%, ahead of EM Eastern Europe (3.6%), EMEA (2.4), EMU (1.8), EAFE (1.4), and BRIC (1.3). EM Asia (-1.3) was the only region to trail the AC World ex-US index. Brazil was the best-performing country, rising 8.6%, followed by Argentina (7.9), Norway (5.6), Colombia (5.4), and Greece (5.0). Of the 16 countries that underperformed the AC World ex-US MSCI last week, Taiwan fared the worst, falling 5.0%, followed by Turkey (-3.4) and Korea (-2.7). During 2018, the US MSCI ranked an impressive 5/49 for the year, with its 6.3% decline far less than the drop for the AC World ex-US (-16.4). All regions and all countries were in negative territory for the year. Among regions, those that fell less than the AC World ex-US are: EM Eastern Europe (-8.3), EM Latin America (-9.3), EMEA (-11.7), BRIC (-15.4), and EAFE (-16.1). EMU (-18.8) and EM Asia (-17.3) were the biggest laggards. The best country performers for 2018: Peru (-0.3), Brazil (-3.9), Russia (-5.6), Finland (-6.2), the US (-6.3), and Israel (-6.3). The worst-performing countries: Argentina (-51.7), Turkey (-43.6), Pakistan (-37.8), Greece (-37.8), and Austria (-29.3).

S&P 1500/500/400/600 Performance ([link](#)): All of these indexes rose again last week, but remain well below their record highs. LargeCap rose 1.9% last week, below than the gains for MidCap (2.3%) and SmallCap (2.6). LargeCap ended the week 13.6% below its record high on September 20, while MidCap and SmallCap are 17.8% and 21.5% below their August 29 records, respectively. Thirty of the 33 sectors moved higher last week, a slight improvement from the week before when 28 rose. Energy and Communication Services dominated the biggest gainers in the latest week: SmallCap Energy (10.8%), MidCap Energy (8.5), LargeCap Energy (5.0), SmallCap Communication Services (4.3), LargeCap Communication Services (4.1), and MidCap Communication Services (3.9). SmallCap Utilities (-1.1) was the biggest decliner last week, followed by LargeCap Real Estate (-0.8). In terms of 2018's performance, all three indexes ended the year in the red; LargeCap was down by 6.2%, followed by SmallCap's 9.8% drop and MidCap's 12.5% decline. Six sectors were positive in 2018, down from 26 during 2017 and the lowest count since 2008 when all sectors fell. Health Care and Utilities dominated the best-performing sectors in 2018: SmallCap Health Care (9.8), MidCap Health Care (6.2), LargeCap Health Care (4.7), MidCap Utilities (3.8), LargeCap Utilities (0.5), and MidCap Communication Services (0.2). Energy and Materials dominated the worst performers in 2018:

SmallCap Energy (-43.0), MidCap Energy (-30.0), SmallCap Materials (-23.1), MidCap Materials (-21.8), and LargeCap Energy (-20.5).

S&P 500 Sectors and Industries Performance ([link](#)): Nine of the 11 sectors rose last week, and six outperformed the S&P 500's 1.9% gain. That compares to nine rising a week earlier, when six again outperformed the 2.9% gain for the S&P 500. Energy was the best-performing sector with a gain of 5.0%, ahead of Communication Services (4.1%), Consumer Discretionary (3.3), Financials (2.7), Materials (2.3), and Industrials (2.3). Real Estate was the biggest underperformer with a drop of 0.8%, followed by the also-underperforming Utilities (0.0), Tech (0.1), Health Care (0.7), and Consumer Staples (1.4). During 2018, the S&P 500 fell 6.2% as just two sectors ended the year with a gain, the lowest count since 2008 when all 11 sectors fell. These five sectors outperformed the S&P 500 in 2018: Health Care (4.7), Utilities (0.5), Consumer Discretionary (-0.5), Tech (-1.6), and Real Estate (-5.6). The seven underperformers: Energy (-20.5), Materials (-16.4), Communication Services (-16.4), Industrials (-15.0), Financials (-14.7), and Consumer Staples (-11.2).

Commodities Performance ([link](#)): Last week, the S&P GSCI index rose 3.2% for its first gain in four weeks as 16 of the 24 commodities moved higher. That compares to a 1.4% decline a week earlier, when nine of the 24 commodities moved higher. However, the index is still in a bear market with a drop of 23.0% from its high in early October. Energy dominated last week's strongest performers: Brent Crude (7.2%), GasOil (7.0), Heating Oil (6.6), Crude Oil (5.8), and Unleaded Gasoline (3.6). Natural Gas was the biggest decliner with a drop of 7.8%, followed by Lead (-5.7), Sugar (-3.7), and Feeder Cattle (-2.8). The S&P GSCI commodities index ended 2018 with a decline of 15.4% for its worst annual performance since 2015. The top-performing commodities in 2018: Cocoa (27.7), Wheat (17.9), Kansas Wheat (14.4), Corn (6.9), Feeder Cattle (2.9), and Live Cattle (1.9). The biggest laggards in 2018: Unleaded Gasoline (-27.5), Zinc (-25.6), Crude Oil (-24.8), Sugar (-20.6), and Brent Crude (-19.5).

Assets Sorted by Spread w/ 200-dmas ([link](#)): Spreads between prices and 200-day moving averages (200-dmas) rose last week for 17/24 commodities, 7/9 global stock indexes, and 30/33 US stock indexes. Commodities' average spread rose w/w to -7.6% from -8.4%, and seven commodities ended the week trading above their 200-dmas, up from six a week earlier. Live Cattle leads all commodities at 9.3% above its 200-dma, but Brent Crude (-21.4%) and GasOil (-18.4) both rose 5.7ppts w/w for the best performance among commodities. Unleaded Gasoline (-29.2) trades at the lowest relative to its 200-dma among commodities, but Natural Gas (-3.2) tumbled 8.5ppts w/w for the worst performance among commodities and all assets. The global indexes trade at an average of 5.1% below their 200-dmas, up from -6.3% in the prior week. Two of the nine global indexes trade above their 200-dmas, unchanged from a week earlier. Brazil (12.9) leads the global indexes, and rose 4.7ppts w/w for the best performance among global assets. Japan (-12.1) trades at the lowest point relative to its 200-dma among global assets, and fell 1.9ppts for the worst performance among global assets. The US stock indexes trade at an average of 10.4% below their 200-dmas, with two of the 33 sectors above, up from -12.6% a week earlier, when one sector was above. LargeCap Utilities (0.7) leads the US stock indexes, followed by MidCap Communication Services (0.5). SmallCap Energy (-35.1) trades the lowest among all US stock indexes and all assets relative to 200-dmas, but rose 6.8ppts for the best performance among US stock indexes, and indeed all assets, last week. SmallCap Utilities (-5.6) dropped 1.2ppts w/w for the worst performance among US stock indexes.

S&P 500 Technical Indicators ([link](#)): The S&P 500 price index rose 1.9% last week, and improved relative to its short-term 50-day moving average (50-dma) and its long-term 200-day moving average (200-dma). The index's 50-dma relative to its 200-dma fell for a 13th straight week, and was in a Death Cross for a fifth week; it had been in Golden Cross for 137 weeks. It was last in a Death Cross for 17 weeks through April 2016 when its 50-dma bottomed at a then-four-year low of 4.5% below its 200-dma

in March 2016. The current Death Cross reading of -4.0% is the lowest since then; it's down from -3.3% a week earlier and a 55-month high of 7.2% in February 2018. The S&P 500's 50-dma fell for a 13th week following 19 straight weekly gains, which compares to declines during eight of the 10 weeks from mid-March to late May in what was then the worst performance since before the 2016 election. The index improved to 3.9% below its falling 50-dma from 6.3% below its falling 50-dma a week earlier and compares to a seven-year low of 12.0% below at the end of December. That's down from a two-year high of 6.2% above its rising 50-dma on January 29. The 200-dma fell for a fifth straight week, and has dropped in nine of the past 12 weeks in the first downtrend since May 2016, when it had been slowly declining for nine months. The S&P 500 ended the week at 7.7% below its falling 200-dma, up from 9.5% below a week earlier but well below the seven-year high of 13.5% above its rising 200-dma during January 2018.

S&P 500 Sectors Technical Indicators ([link](#)): Ten of the 11 S&P 500 sectors improved last week relative to their 50-dmas and nine relative to their 200-dmas. All 11 sectors traded below their 50-dmas for a third straight week. The longer-term picture—i.e., relative to 200-dmas—shows Utilities as the only sector trading above currently, unchanged from a week earlier. That's the lowest count since all 11 were below in January 2016, and is a relatively swift reversal from the September 26 alignment, when all 11 sectors were above their 200-dmas. Two long-term 200-dma leaders left the building during October: Tech fell below its 200-dma for the first time in 121 weeks, and Consumer Discretionary fell below its 200-dma for the first time in 102 weeks. Four sectors remain in the Golden Cross club (with 50-dmas higher than 200-dmas), unchanged from a week earlier: Health Care and Real Estate (26 straight weeks), Utilities (22), and Consumer Staples (17). At the end of November, Consumer Discretionary and Tech left the club for the first time since April 2016. Among the laggards, Financials has been out of Golden Cross territory for 12 straight weeks and during 24 of the past 28 weeks, Materials has been out for 36 straight weeks, Energy for eight weeks, and Industrials for seven weeks. All 11 sectors had been in a Golden Cross back in mid-January (for the first time since a 26-week streak ended in October 2016). Materials is the only sector with a rising 50-dma now, compared to a week earlier when all 11 were falling. Two sectors had rising 200-dmas at the end of last week, down from three a week ago and the lowest count since January 2016 when all 11 sectors had falling 200-dmas. In the latest week, Real Estate left the rising 200-dma club now occupied by Health Care and Utilities.

Stock Market Sentiment Indicators ([link](#)): Our Bull/Bear Ratio (BBR) sank below 1.00 last week for the first time since late February 2016. The BBR dropped to 0.86 last week, down from 2.23 in mid-December, as bullish sentiment tumbled to 29.9%—the fewest bulls since February 2016; it was as high as 61.8% three months ago. Meanwhile, bearish sentiment climbed to 34.6%—the most bears since mid-February 2016; it had fluctuated in a narrow band (below 20.0%) for most of H2-2018. The correction count slipped from 39.3% to 35.5% last week; it was at 41.1% at the end of November—which was the highest percentage since late September 2015. The AAI Ratio climbed for the third week last week, from 30.0% to 43.6%, as bullish sentiment rose from 20.9% to 33.0% over the period and bearish sentiment fell from 48.9% to 42.8%.

US ECONOMIC INDICATORS

Employment ([link](#)): Employment growth in December was much stronger than expected, and there were upward revisions to prior months. Last month, 312,000 were added to payrolls (vs a 180,000 consensus estimate), while job gains for both November (to 176,000 from 155,000) and October (274,000 from 237,000) were revised higher, for a net gain of 58,000. Private payrolls hired 301,000 last month—30,000 above ADP's count of 271,000—following upward revisions to November (173,000 from 161,000) and October (281,000 from 251,000), for a net gain of 42,000. For 2018, total and private nonfarm payrolls were up 2.64 million and 2.56 million, respectively, compared with 2.19 million and

2.16 million during 2017. Here's a look at the industries leading December's gain, along with their total tallies for all of 2018: health care (50,200 m/m & 346,000 y/y), professional & business services (43,000 & 583,000), food services & drinking places (40,700 & 235,400), construction (38,000 & 280,000), manufacturing (32,000 & 284,000), and retail trade (23,800 & 91,600); the latter had shed jobs in 2017. Meanwhile, the breadth of job creation (i.e., the percentage of private industries increasing payrolls) shows the three-month span (73.3% from 71.9%) moving further above 70.0%, while the one-month span (to 70.0% from 61.0%) jumped back up to 70.0%.

ADP Employment ([link](#)): "Businesses continue to add aggressively to their payrolls despite the stock market slump and the trade war. Favorable December weather also helped lift the job market. At the current pace of job growth, low unemployment will get even lower," according to ADP. In December, private industries added 271,000 to payrolls—the most since February 2017—and nearly 100,000 more than consensus expectations of a 175,000 advance. There was a downward revision to November's (to 157,000 from 179,000) gain and an upward revision to October's (239,000 from 225,000), for a net loss of -8,000. Last month, service-providing industries (224,000) increased payrolls by the most since June 2016, while hirings in goods-producing industries (47,000) were more than triple November's performance. The increase in service-providing industries was widespread, led by professional & business services (66,000) and education & health services (61,000), while a busy holiday season greatly impacted hirings for both leisure & hospitality (39,000) and trade, transportation & utilities (33,000) companies. Within goods-producing, construction (37,000) companies hired at their best pace since February 2017, while manufacturing's (12,000) improved from November's pace, though remained below the clip of the first half of 2018. Employment at natural resources/mining (-2,000) companies fell for the first time since September 2017. Medium-sized companies (129,000) retained the number one spot, accounting for nearly half of December's gain, while small companies (89,000) hired at their best pace for all of 2018. Hiring by large companies (54,000) remained in the number three spot, though improved from November's slowdown.

Earned Income Proxy ([link](#)): Our Earned Income Proxy (EIP), which tracks consumer incomes and spending closely, finished 2018 at a new record high; it hasn't posted a decline in 22 months. Our EIP jumped 0.9% in December—the best monthly performance since March 2014—and 5.3% y/y. Average hourly earnings (AHE), one of the components of our EIP, rose 0.4% m/m last month, and 3.2% y/y—matching April's rate, which was the highest since April 2009. Meanwhile, aggregate weekly hours—the other component of our EIP—rebounded 0.5% after contracting -0.2% in November; its yearly gain accelerated 2.1% y/y from 1.7% during November.

Unemployment ([link](#)): December's unemployment rate ticked up as an additional 419,000 joined the labor force, responding to a strong job market. The headline rate rose to 3.9% from 3.7% in November—which was the lowest reading since the end of 1969; it peaked at 10.0% in October 2009. Meanwhile, the participation rate has been moving higher in recent months, climbing to 63.1% in December, back up at the top of the narrow band (from 62.6% to 63.1%) it has fluctuated within the past three years; it was at 62.7% in August and September. The volatile teenage rate ticked up to 12.5%, after falling to 12.0% in October and November—which was the lowest since December 1969—while the adult unemployment rate (3.5%) was just above its cyclical low of 3.4% recorded from September through November. The college-grad rate (2.1) was back down near its cyclical low of 2.0%. Those working part-time for economic reasons (a.k.a. "involuntary part-time workers") fell 124,000 to 4.66 million (2.9% of the civilian labor force) last month, after increasing 413,000 during the three months through November. The sum of the underemployment and jobless rates (6.8%) is up from August's 6.5% rate, which was the lowest reading since February 2001, while the U6 rate (7.6)—which includes marginally attached workers—held above October's 7.4%, which matched its lowest reading since spring 2001.

Wages ([link](#)): December wage inflation—as measured by the average hourly earnings (AHE) rate for all workers on private nonfarm payrolls—remained above 3.0%, while the jobless rate remained near a 50-year low. The wage rate was back up at October's 3.2% y/y, which was its best pace since April 2009; it was at a recent low of 2.3% during October 2017. The wage rate for service-providing industries (3.2% y/y) remained near its best reading since January 2009, while the goods-producing rate (2.8) accelerated to its highest rate since February 2017. Within goods-producing, the manufacturing rate (2.0) remained around recent lows, though posted its best rate in 15 months, while the construction (3.9) and natural resources (2.6) rates held around recent highs. Within service-providing, rates for retail trade (5.0) and information services (5.7) are at their highs for the series going back to 2006, while the rate for leisure & hospitality (3.7) continues to move up from recent lows. Meanwhile, rates for utilities (4.9), professional & business services (2.8), education & health services (2.3), and wholesale trade (2.4) are stalled around recent highs. Moving down from recent highs are rates for financial activities (4.1) and transportation & warehousing (0.7), with the latter at its lowest since May 2016.

GLOBAL ECONOMIC INDICATORS

Global Manufacturing PMIs ([link](#)): Global manufacturing activity slowed to a 27-month low last month. JP Morgan's M-PMI eased for the eleventh time since reaching a seven-year high of 54.5 at the end of 2017, slumping to 51.5 by the end of 2018. Developed nations (to 52.3 from 52.8) continued to record stronger growth than emerging ones (50.3 from 50.8), though both have slowed since late 2017—to the weakest readings since September 2016 for the former, while the latter fell back to September's 25-month low. M-PMI readings were above 50.0 for 20 out of the 30 nations for which December data were available, including the Netherlands (57.2 from 56.1), Ireland (54.5 from 55.4), UK (54.2 from 53.6), Australia (54.0 from 54.6), Austria (53.9 from 54.9), US (53.8 from 55.3), Greece (53.8 from 54.0), India (53.2 from 54.0), Brazil (52.6 from 52.7), Japan (52.4 from 52.2), and Germany (51.5 from 51.8). Countries with M-PMIs below the neutral 50.0 mark included South Korea (49.8 from 48.6), China (49.7 from 50.2), France (49.7 from 50.8), Italy (49.2 from 48.6), and Taiwan (47.7 from 48.4).

US Manufacturing PMIs ([link](#)): Manufacturing activity in December continued to expand at a respectable rate, though much slower than the previous 11 months—with both the ISM and IHS Markit measures posting their weakest readings of 2018. The ISM M-PMI (to 54.1 from 59.3) dropped to its lowest reading since November 2016, with all five components contributing to the weakness. Both the new orders (51.1 from 62.1) and production (54.3 from 60.6) gauges slowed dramatically after spending most of 2018 above the 60.0 mark, while the supplier deliveries (57.5 from 62.5) gauge slipped below 60.0 for the first time since January. The employment (56.2 from 58.4) measure remained around recent highs, while the inventories (51.2 from 52.9) component held just above 50.0. IHS Markit's M-PMI slipped for the second month, from 55.7 in October to a 15-month low of 53.8 last month; however, the Q4 average of 54.9 was strong—and faster than any quarter of 2017. December's report showed that both new orders and production grew at the slowest rates in over a year, while business optimism was the weakest in over two years. According to the report, "Some of the weakness is due to capacity constraints, with producers again reporting widespread difficulties in finding suitable staff and sourcing sufficient quantities of inputs. However, the survey also revealed signs of slower demand growth from customers, as well as rising concerns over the impact of tariffs. Just over two thirds of manufacturers reporting higher costs attributed the rise in prices to tariffs."

Contact us by [email](#) or call 480-664-1333.

Ed Yardeni, President & Chief Investment Strategist, 516-972-7683
Debbie Johnson, Chief Economist, 480-664-1333
Joe Abbott, Chief Quantitative Strategist, 732-497-5306

Melissa Tagg, Director of Research Projects & Operations, 516-782-9967

Mali Quintana, Senior Economist, 480-664-1333

Jackie Doherty, Contributing Editor, 917-328-6848

Valerie de la Rue, Director of Institutional Sales, 516-277-2432

Mary Fanslau, Manager of Client Services, 480-664-1333

Sandy Cohan, Senior Editor, 570-775-6823

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