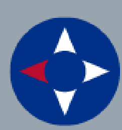

Great-West Investments Capital Markets Perspective

Week in Review: October 4th – October 10th

INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD		INDEX/ SECURITY	ASSET CLASS	LEVEL (CLOSE)	% CHANGE (THROUGH FRIDAY'S CLOSE) 1 WK.	YTD
Dow Industrials	Lg. Cap Eq.	34,746.28	1.22%	14.37%		FTSE 100	UK Equity	7,095.55	0.97%	9.83
S&P 500®	Lg. Cap Eq.	4,391.34	0.79%	17.72%		Nikkei 225	Japan Equity	28,048.94	-2.51%	2.20%
NASDAQ Comp.	US Equity	14,579.54	0.09%	13.52%		EEM:US	Emkt. Equity	$50.82	0.97%	-1.17%
S&P Midcap 400©	Mid-Cap Equity	2,690.22	0.25%	16.63%		EFA:US	Non-US Equity	$77.98	-0.28%	6.82%
Russell 2000®	Sm. Cap Eq.	2,233.09	-0.38%	12.86%		UST 10y (yield)	US Treasury	1.61%	+0.13%	+0.70%
Stoxx 50	Europe Eq.	4,073.29	0.94%	14.05%		B/Barc AGG	Fixed Inc.	2,343.10	-0.77%	-1.96%

If can-kicking were an Olympic sport, the US would dominate.

Last week, cooler heads seemed to prevail when the warring factions of the US Senate agreed to a deal that **effectively kicked the default can down the road until December** by temporarily extending the debt ceiling until the weeks between Thanksgiving and Christmas[1]. That built on the prior week's 11th-hour deal to avoid a government shutdown, thereby **side-stepping the second of two policy-related stinkers that had the potential to rile markets**.

But because the debt ceiling was lifted by a set dollar amount rather than suspended outright, the deal was **cleverly crafted** in such a way so as to ensure that any massive increase in spending (such as that contemplated by President Biden's big infrastructure bill,) would almost certainly cause **another rancorous debate – and the potential for an associated spike in market volatility – in the near future**.

At the risk of mixing metaphors, last week's exercise in can-kicking temporarily **nudged off course what Biden had described as "a meteor headed to crash into our economy,"** bringing immediately to mind the goofy (but still kind of watch-able…) space melodrama *Armageddon*. But however effective Senate Minority Leader Mitch McConnell and Majority Leader Chuck Schumer were at reprising the roles of Billy Bob Thornton and Bruce Willis (you get to pick for yourself which Senator best suits which role,) there are at least two key differences: first, the characters played by Bruce and Billy Bob didn't create the fictional asteroid that threatened the planet themselves, while **neither side** in the debt ceiling debate can make a similar claim to be **entirely blameless** (and therefore shouldn't be considered heroic for averting a potential catastrophe that was, after all, at least partially of their own making.)

Second – and far more important from a forward-looking perspective – **the producers of *Armageddon* at least had the good sense to avoid producing a sequel**. **McConnell, Schumer, and their supporting casts in both houses of Congress and the White House, not so much.**

[1] Bloomberg, Mcconnell.Senate.gov, whitehouse.gov

Markets, for the most part, reacted well to the deal. **Stocks in the US were mostly higher** and the shortest of short short-term US treasuries – those most at risk for technical default if the deal hadn't been reached – climbed back of the ledge that weeks of default worries had pushed them onto, thereby **repairing an odd "kink" in the yield curve** that had previously acted as a reminder of exactly how out-of-joint the policy environment really is. Still, the market's gains weren't as robust as they might have been if the issue had been put to bed entirely, and **the deal also did nothing to stop silliness** such as what appeared to be **semi-sincere discussions of minting a trillion-dollar platinum coin** to sidestep the ceiling debate entirely[2]. The mere suggestion of *that* **asteroid-sized gimmick** makes things like free popcorn for AMC shareholders – which represented (in my mind, anyway…) the height of meme-stock silliness this summer – seem positively quaint in comparison.

But once again policy issues seem to have unfortunately trumped the things that arguably mean much more: namely, developments in the real economy. Front-and-center among those developments last week was **yet another disappointing payrolls report** in which the US economy once again failed to produce as many jobs as economists had hoped. Non-farm payrolls expanded by a mere 194,000 in September, well below most forecasts and the weakest performance since last December[3].

But the number **wasn't necessarily as bad as it may have seemed** at first glance because it was distorted by unusually weak hiring activity in state and local education. That was in turn made lumpy by still-uncertain return-to-school policies (itself a function of the delta variant's uneven progress across the national landscape,) which might actually resolve itself now that delta seems to be receding. Besides, the whole mess was compounded by a seasonal adjustment mechanism in the BLS data that quite simply didn't know how to deal with it; that could suggest that the miss was at least partially influenced by things of only questionable value in illustrating real economic trends in the short-term. **Moreover, August's payroll number was revised substantially higher** – continuing a winning streak for upward revisions that makes another big miss by current payrolls data a lot easier to stomach. In any case, the third big miss in job creation of this recovery probably did nothing to move the Federal Reserve off it's plan to begin tapering its bond purchases in a month or two, which probably helps explain the **market's willingness to look the other way**.

Other fundamental data about the health of the economy also failed to capture much attention last week, including a **factory orders** report for August that was a little better than expected[4] and a **service-sector PMI**[5] that reconfirmed what many had suspected all along: growth is robust, but suffering from a very real "loss of momentum" (their words, not mine…) that serves as yet another reminder that the US economy may be showing clear signs of plateauing.

On the other hand, one thing that *did* bump Washington's melodrama briefly out of the headlines was a **continued run-up in energy prices**. Last week's underwhelming, steady-as-we-go decision from OPEC[6] did little to calm commodity markets, and while the potential for a real live energy crisis this winter seems more likely in places like Europe than it does here, **a persistent rise in oil prices** (which topped 80 bucks for the first time in a loooooong time on Monday,) has been accompanied by **accelerating prices in both types of gas:** the kind that runs your car (which was up 2.3% last week) and the kind that heats your home (which declined a little bit last week, but is still up more than 50% since the end of June.) Again, **that's hardly ideal for an economy wrestling with inflationary fears**.

So that's the week that was, and I suppose I should stop complaining about all the Washington drama because it makes this part of my job (i.e. writing about capital markets) much easier. Still, **I think we might all appreciate a few months without fictional meteors, 11th-hour deals and pandemic-related doomsaying** as we look ahead toward something – anything – approaching "normal". It's anyone's guess as to whether that will happen this week or not.

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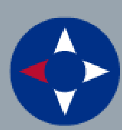
[2] https://seekingalpha.com/news/3749271-yellen-opposes-trillion-dollar-coin-solution-for-debt-limit
[3] https://www.bls.gov/news.release/empsit.nr0.htm
[4] https://www.census.gov/manufacturing/m3/prel/pdf/s-i-o.pdf
[5] https://www.markiteconomics.com/Public/Home/PressRelease/b4f891d45a6343d88c17b1cada6fc15f
[6] https://www.opec.org/opec_web/en/press_room/6647.htm



What to Watch This Week: October 11th – 17th

Notable economic events (Oct. 11th – 15th)

Monday: *Bond markets closed*

Tuesday: NFIB small business confidence, JOLTS

Wednesday: CPI, Atlanta Fed inflation expectations, bank earnings, Fed minutes

Thursday: Weekly jobless claims, PPI, EIA inventory data

Friday: Retail sales, Empire St. Mfgr., UofM consumer sentiment

Yeah, it might be the unofficial start of second-quarter earnings season (and we'll get to that shortly,) but first, here's something else important to occupy your mental space: **Captain Kirk is on his way into orbit!** Yes, Star Trek fans, none other than William Shatner will climb aboard Blue Origin's New Shepard 4 on Wednesday and (hopefully) become the oldest human being ever to leave earth. **No word yet on whether he and his fellow astronauts plan to blow up any asteroids, but to me, the timing is certainly suspicious** (I guess Bruce Willis wasn't available; maybe he's still in Washington.)

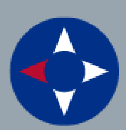
But back to earnings. On Wednesday, while Kirk is floating weightlessly in orbit, JPMorgan, Goldman Sachs and a small handful of other companies will **kick off second quarter earnings season**. Other big banks like Citigroup, Wells Fargo, Bank of America and Morgan Stanley will follow on Thursday, setting the stage for what could be a turning point in market sentiment. That's because **earnings estimates have been continually ratcheted higher** since last winter when the COVID vaccines first gave us hope that the economy would soon be on the mend. But since then, a perfect storm of things like unprecedented **cost inflation, supply chain stress and a near-total inability to find workers have conspired to place corporate margins – and therefore earnings – at risk**. That idea has so far popped up in the commentary surrounding a number of early reporters such as Federal Express and Bed Bath & Beyond. The extent to which the pressure faced by those two companies is either **endemic or isolated** to their specific circumstances **will probably go a long way toward setting the market's mood for the remainder of 2021**.

Speaking of cost pressures, we'll also get **two separate reads of inflation** this week: consumer prices (**CPI**) on Wednesday and producer prices (**PPI**) on Thursday. Add to that the **Atlanta Fed's inflation expectations survey** (also on Wednesday,) and you have a pretty comprehensive view of what's going on with prices. And while we're at it, the Energy Information Administration's weekly view on inventories could be another piece of the puzzle given how aggressively energy prices have elbowed their way into the conversation.

Labor markets, too, will get some attention this week when the Bureau of Labor Statistics releases its **JOLTS report**, a deeper look into who's hiring, firing and quitting their jobs that recently became famous by providing the numerator of the ratio comparing the number of job seekers to the number of available jobs. Small businesses – the group perhaps most impacted by the disconnect in labor markets than any other – will certainly be paying attention. They get their say on Tuesday, when the National Federation of Independent Businesses releases the latest results of its **small business sentiment survey**. That long-running and high-quality report was **among the first to highlight difficulties businesses are having finding workers**, and this week's report for September will likely be more of the same.

If consumer trends are your thing (and they should be, because consumers are still the main driver of the US economy,) then Friday is the day you'll want to tune in. That's when **retail sales** numbers will be released, together with the **University of Michigan's preliminary read** on October consumer sentiment. While sales have so far been fine, sentiment has been under pressure: pay close attention to the UofM's survey for evidence of whether consumers are feeling any better than recent declines in the face of all these economic crosswinds would suggest.

Source for index data: Bloomberg.com; GWI calculations.



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