RAYMOND JAMES

Economic Research
Published by Raymond James & Associates

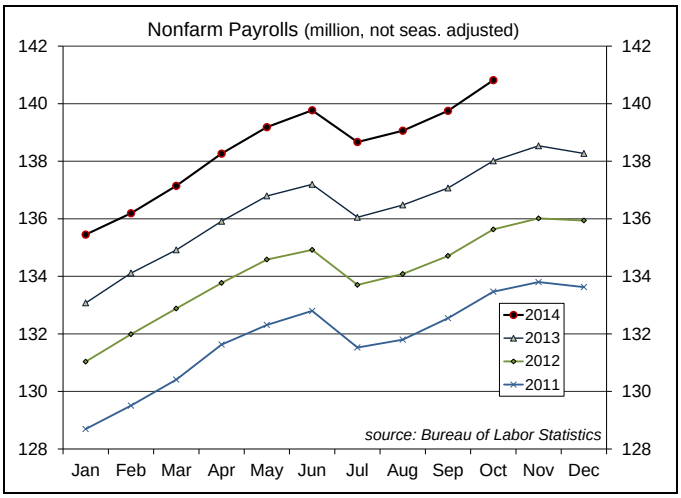
Scott J. Brown, Ph.D., (727) 567-2603, Scott.J.Brown@RaymondJames.com

November 10 - 14, 2014

Weekly Market Monitor

The October Employment Report

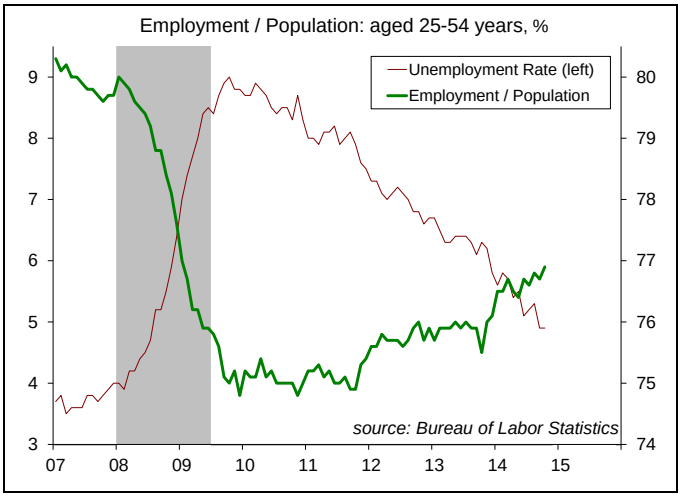
The U.S. economy added more than one million jobs in October (1.064 million to be exact) – that's prior to seasonal adjustment – significantly more than in October 2013 (944,000).



On a seasonally adjusted basis, payrolls rose by "only" 214,000, with upward revisions to August and September. The three-month average was essentially the same as the 12-month average. Yet, the unadjusted payroll figure suggests a lot more seasonal strength than usual. It's not that the Bureau of Labor Statistics doesn't know how to do seasonal adjustment. The people putting the numbers together are smart and dedicated. However, it's hard to get the seasonal adjustment exactly right.

A couple of factors could help explain some of the improvement. One is that the year-ago figures might have been depressed by the government shutdown. However, the government shutdown appeared to have a much bigger effect on the Household Survey data (the unemployment rate, labor force participation, and the employment/population ratio). Another possibility is the calendar. There are only four weeks between Thanksgiving and Christmas. That was the same case as last year, but retailers appear to be more aggressive this year, with many seeking to pull sales ahead of Black Friday (the Friday after Thanksgiving). Consumer spending this holiday season will continue to be driven by discounts and promotions and these offers are likely to show up sooner. Retail accounted for about a third of the improvement in unadjusted job growth relative to last year. In addition, we're seeing fewer seasonal job losses in hotels and restaurants. Some of that may be a reflection of better weather, but more likely, consumers are more optimistic.

The drop in gasoline prices has also helped, but remember that gasoline prices normally fall in the second half of the year. So, simply measuring the drop from the June is going to be a bit misleading. Yet, gasoline prices have fallen more than they normally do. The impact on the consumer typically shows up with a lag, but it depends on how low gasoline prices go and how long they stay low. Next week, the Bureau of Labor Statistics should report another gain in real weekly wages (reflecting the drop in gasoline, but also a rise in the workweek).



In her brief comments at a Paris central bank conference last week, Fed Chair Janet Yellen said that monetary policy needs to normalize as overall economic conditions return to normal. However, the key questions are how far we are from normal and how rapidly we can expect to get there. The unemployment rate fell further in October, to 5.8%, the lowest since June 2008, down from about 10% at the end of the recession. However, that's a bit misleading, as many have dropped out of the labor force. The employment/population ratio improved to 59.2% in October, vs. 58.2% last year (but remember, the year-ago figure was depressed briefly by the government shutdown). Improvement is more pronounced for the key cohort, those aged 25-54. An upward trend appears a lot clearer, but there's still a lot of room for improvement. Unemployment rates for teenagers and young adults remain higher, but their recovery should lag that of prime-aged workers.

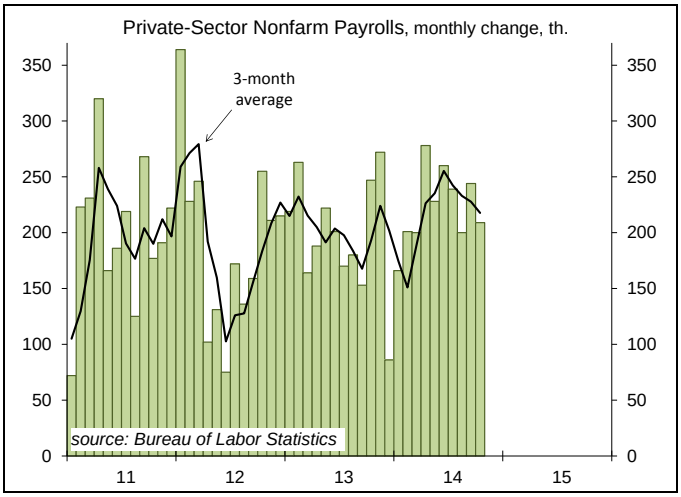
Wages are a reflection of the amount of slack in the job market. Average hourly earnings were reported to have risen 0.1% last month, up 2.0% from a year ago. In comparison, the Consumer Price Index rose 1.7% over the 12 months ending in September. Note that the average wage figure reflects the composition of employment. If there are more job gains in lower-paying industries (such as retail), average wages are going to rise less. The Employment Cost Index, which adjusts for the changing pattern of employment and includes benefit costs, rose 2.2% in the 12 months ending in September. The Fed needs to think about the endgame, but need not act soon.

International Headquarters: The Raymond James Financial Center | 880 Carillon Parkway | St. Petersburg, Florida 33716 | 800-248-8863

	Treasury Yields								Dollar				Equities		
	13-wk	26-wk	52-wk	2-yr	3-yr	5-yr	10-yr	30-yr	$/Euro	$/BP	JY/$	CD/$	NASD	SPX	DJIA
10/10/14	0.01	0.04	0.10	0.45	0.89	1.55	2.31	3.03	1.264	1.605	107.83	1.117	4276.24	1906.13	16544.10
10/31/14	0.01	0.05	0.11	0.50	0.95	1.62	2.35	3.07	1.253	1.600	112.09	1.127	4630.74	2018.05	17390.52
11/07/14	0.03	0.06	0.10	0.50	0.93	1.59	2.31	3.04	1.246	1.588	114.57	1.1327	4632.53	2031.88	17573.93

Recent Economic Data and Outlook

While it was a full week in terms of the economic data, the figures tended not to have much of an impact on the financial markets. Stock market participants were encouraged by the unsurprising election results and by the hint of further ECB action.



Fed Chair Janet Yellen said that she anticipates that the headwinds associated with the financial crisis will wane and that as employment, economic activity, and inflation return to normal, *"monetary policy will eventually need to normalize too, although the speed and timing of this normalization will likely differ across countries based on differences in the pace of recovery in domestic conditions."* Policy normalization *"could lead to some heightened financial volatility,"* she noted, but *"the Federal Reserve will strive to clearly and transparently communicate its monetary policy strategy in order to minimize the likelihood of surprises that could disrupt financial markets, both at home and around the world." "Most importantly,"* she added, *"the normalization of monetary policy will be an important sign that economic conditions more generally are finally emerging from the shadow of the Great Recession."*

As was widely anticipated, the Republican Party won enough seats in the **mid-term elections** to give them a majority in the Senate. Turnout was low. Still, the Republicans may be unable to accomplish much, as there are sharp divisions within the party, they don't have a 60-seat super majority to get legislation through the Senate, and they will not have the two-thirds majorities in each chamber to override a presidential veto.

The **October Employment Report** was strong, but not as robust as anticipated. Nonfarm payrolls rose by 214,000, with a net upward revision to August and September of +31,000. The unemployment rate edged down to 5.8%, reflecting declines in the rates for teenagers and young adults (suggesting that there may have been issues with the seasonal adjustment). The employment/population ratio rose to 59.2%, up from 59.0% in September and 58.2% in October 2013. Average weekly hours edged up. Average hourly earnings rose 0.1% (+2.0% y/y).

Motor Vehicle Sales held steady at a 16.3 million seasonally adjusted annual rate in October. Sales of domestically built vehicles rose to a 13.1 million pace, from 12.9 million.

The **ISM Manufacturing Index** rose to 59.0 in October, vs. 56.6 in September and 59.0 in August. New orders and employment rose at a faster pace. Input price pressures moderated.

The **ISM Non-Manufacturing Index** fell to 57.1 in October, vs. 58.6 in September. Business activity and new orders continued to advance (not quite as strong as in September). Job growth picked up. Input price pressures moderated.

The U.S. **Trade Deficit** widened to $43.0 billion in September (vs. $40.0 billion in August), implying (all else equal) a downward revision to the estimate of 3Q14 GDP growth.

Construction Spending fell 0.4% in September, weaker than was assumed in the advance GDP estimate.

Factory Orders fell 0.6% in September (+1.9%), with orders for durable goods down 1.1% (+3.5% y/y). Shipments of nondefense capital goods ex-aircraft rose 0.3% (vs. -0.2% assumed in the advance GDP report). Inventories rose 0.2% (a bit less than assumed in the advance GDP report).

The **European Central Bank** left short-term interest rates unchanged. ECB President Draghi said that "should it become necessary to further address risks of too prolonged a period of low inflation, the Governing Council is unanimous in its commitment to using additional unconventional instruments within its mandate." Moreover, "the Governing Council has tasked ECB staff and the relevant Eurosystem committees with ensuring the timely preparation of further measures to be implemented, if needed."

Economic Outlook (4Q14): GDP growth of 2.5% to 3.0%

Employment: Job destruction is very low. New hiring does not appear to have been restrained much by global worries.

Consumers: Lack of real wage growth restrained the pace of consumer spending growth in the summer, but lower gasoline prices should provide some support in the near term.

Manufacturing: Mixed, but moderately strong overall. Restraints (on exports) from European weakness should be offset by strength in domestic demand.

Housing/Construction: Affordability issues have remained a constraint for the middle of the market and below. Supply constraints have been an issue for builders, but are fading.

Prices: The PCE Price Index, the Fed's chief inflation gauge, remains well below the Fed's 2% target on a y/y basis. Pipeline pressures appear mild. Wage pressures are limited. Inflation expectations remain well-anchored.

Interest Rates: With the Fed's large-scale asset purchases (QE3) completed, short-term interest rates are expected to remain exceptionally low *"for a considerable time."* The Fed's policy moves in 2015 will be dictated by the evolution of the economic outlook in the second half of 2014.

This Week:					*forecast*	last	last –1	comments
Monday	11/10	1:00	Treasury Note Auction					$26 billion in 3-year notes
Tuesday	11/11		Veterans Day					bond market closed
Wednesday	11/12	7:30	Small Business Optimism	Oct	***NF***	95.3	96.1	likely to improve
		1:00	Treasury Note Auction					$24 billion in 10-year notes
Thursday	11/13	8:30	Jobless Claims, th.	11/08	***280***	278	288	a very low trend
		10:00	JOLTS: hiring rate	Sep	***NF***	3.3%	3.6%	still below normal
			JOLTS: quit rate		***NF***	1.8%	1.8%	still below normal
		12:45	Yellen Speaks					welcoming remarks at Global Res. Forum
		1:00	Treasury Bond Auction					$16 billion in 30-year bonds
		2:00	Treasury Budget, $bln	Oct	***NF***	-90.6	-120.0	first month of FY15
Friday	11/14	8:30	**Retail Sales**	Oct	***+0.5%***	-0.3%	+0.6%	likely to have picked up
			ex-autos		***+0.2%***	-0.2%	+0.3%	lower gasoline prices
			ex-autos, bld mat, gasoline		***+0.4%***	0.0%	+0.5%	moderate
		8:30	Import Prices	Oct	***NF***	-0.5%	-0.6%	lower petroleum prices
			ex-food & fuels		***NF***	-0.1%	0.0%	no inflation pressure from abroad
		9:55	Consumer Sentiment	m-Nov	***87.8***	86.9	84.6	likely higher
		10:00	Business Inventories	Sep	***-0.1%***	+0.2%	+0.4%	seen lower
Next Week:								
Monday	11/17	8:30	Empire St. Manf. Index	Nov	***8.2***	6.2	27.5	likely moderate (but a bit erratic)
		9:15	**Industrial Production**	Oct	***+0.2%***	+1.0%	-0.2%	mixed (watch for revisions)
			Manufacturing Output		***+0.3%***	+0.5%	-0.5%	aggregate hours edged up 0.1%
			Capacity Utilization		***79.2%***	79.3%	78.7%	little changed
			Manufacturing		***78.2%***	78.1%	77.9%	no pressure for inflation
Tuesday	11/18	8:30	**Producer Price Index**	Oct	***-0.2%***	-0.1%	0.0%	lower energy prices
			ex-food & energy		***+0.1%***	0.0%	+0.1%	mild core inflation
		10:00	Homebuilder Sentiment		***56***	54	59	should rebound somewhat
Wednesday	11/19	8:30	**Building Permits, th.**	Oct	***1045***	1031	1003	seen somewhat higher
			% change		***+1.4***	+2.8	-5.1	single-fam strength, multi-fam volatility
			Housing Starts		***1025***	1017	957	moderate strong
			% change		***+0.8***	+6.3	-12.8	but watch for revisions
		2:00	**FOMC Minutes**	10/29				how much worry about low inflation?
Thursday	11/20	8:30	Jobless Claims, th.	11/15	***280***	***280***	278	Veterans Day adjustment may add noise
		8:30	**Consumer Price Index**	Oct	***-0.1%***	+0.1%	-0.2%	lower gasoline prices
			year-over-year		***+1.6%***	+1.7%	+1.7%	little changed
			ex-food & energy		***+0.1%***	+0.1%	0.0%	mild core inflation
			year-over-year		***+1.7%***	+1.7%	+1.7%	low and steady
		8:30	Real Earnings	Oct	***+0.5%***	+0.2%	+0.5%	nominal earnings +0.4%
		10:00	Philadelphia Fed Index	Nov	***15.0***	20.7	22.5	moderate (but uneven month to month)
		10:00	**Existing Home Sales, mln**	Oct	***5.25***	5.17	5.05	seen a bit higher
			% change		***+1.5***	+2.4	-1.8	some moderation in speculative buying
		10:00	Leading Econ Indicators	Oct	***+0.7%***	+0.8%	+0.0%	stocks down, but other components add
		1:00	TIPS Auction					re-opened 10-year TIPS
Friday	11/21		no significant data					note: 4 weeks between T-day & Xmas

This Week…

The economic calendar thins out considerably, with a clear focus on Friday's retail sales figures. The drop in gasoline prices is expected to depress the headline figures, but will add to consumer purchasing power in the near term.

Monday

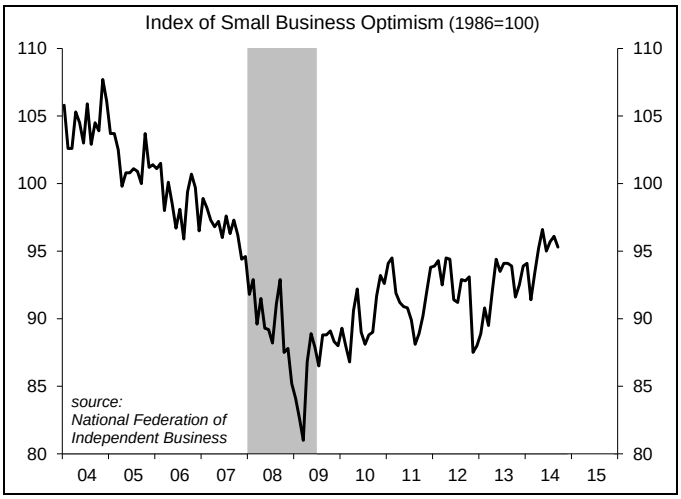
No significant data.

Tuesday

Veterans Day – The bond market will be closed.

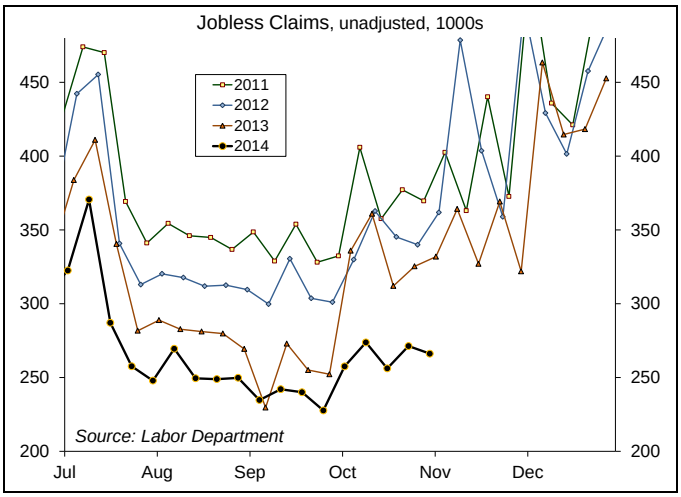
Wednesday

Small Business Optimism Index (October) – We should see an improving trend as the economy continues to recovery, but the level is still well below normal.

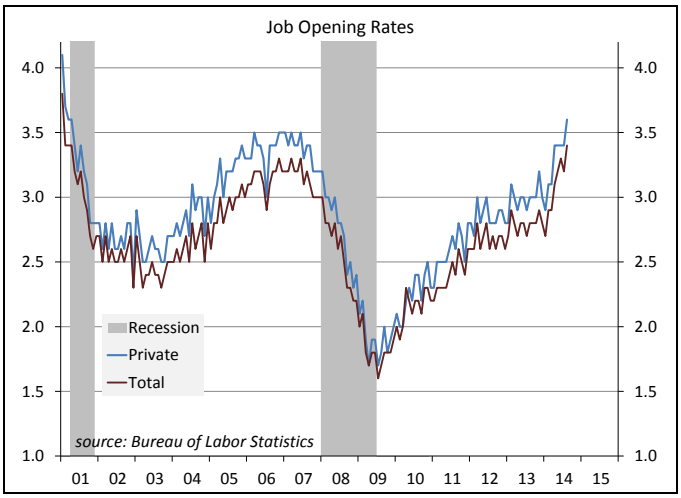


Thursday

Jobless Claims (week ending November 8) – Adjusted claims are trending at the lowest level since April 2000. The unadjusted figures are well below year-ago figures (when the government shutdown briefly boosted claims).

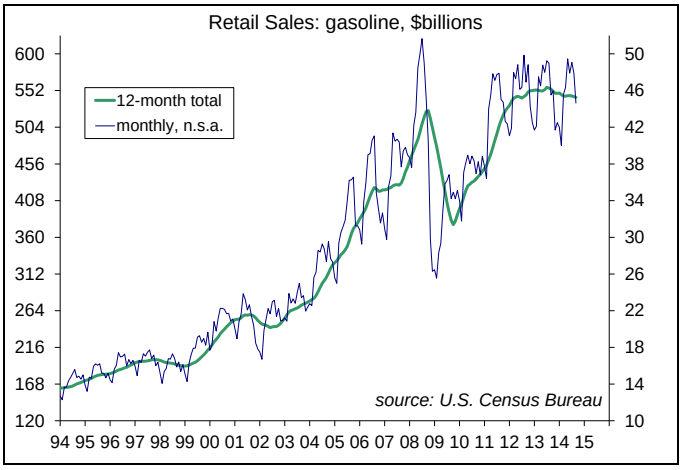


JOLTS Data (September) – Since Janet Yellen mentioned them, hiring and quit rates bear watching closely as a measure of labor market slack. Both are generally improving, but each remains far below normal levels (and hiring rates dipped in August). Still, while there is some noise in the monthly figures, the trends evolve glacially. One interesting note in recent reports is that job opening rates have risen much faster than hiring. The number of unemployed people per job opening peaked at 6.8 as the recession ended (June 2009) and fell to below 2 in August, a level more consistent with an economy near full employment. However, the surge in job openings could be because employers are casting a wider net, screening a larger number of workers, and low-balling on wages to see who bites.



Friday

Retail Sales (October) – September results were poor, likely reflecting the lack of growth in real average wages. Unit motor vehicle sales (reported by the various automakers) were little changed last month (using seasonal factors supplied by the Bureau of Economic Analysis), although an increase in sales of domestically built vehicles offset declines in imports. Chain store sales were moderate. Lower gasoline prices are expected to reduce the headline figures to some extent. The drop in gasoline prices does add to consumer purchasing power. That is, if consumers are spending less to fill their tanks, they have more money to spend on other things. However, the impact usually arrives with a lag (hence, more support for sales in November and December).



Input prices (October) – Lower petroleum prices should put downward pressure on the headline figure.

Consumer Sentiment (mid-November) – Some improvement is likely, indirectly reflecting the drop in gasoline prices.

Business Inventories (September) – These data have some implications for revisions to the 3Q14 GDP growth estimate.

Next Week …

The economic calendar picks up again. While surprises in the mid-month figures could generate some reactions in the financial markets, investors will also be interested in the FOMC minutes. Curiously, the Fed policy statement of October 29 did not show much concern about the low trend in inflation (other than Minneapolis Fed President Kocherlakota's formal dissent). In contrast, the FOMC minutes are likely to reflect a range of opinions about low inflation. We may also get a sense of how far apart policymakers are in their views regarding the amount of slack there is in the job market.

Coming Events and Data Releases

November 25	Real GDP (2nd estimate, 3Q14)
November 27	Thanksgiving Holiday (markets closed)
December 5	Employment Report (November)
December 17	FOMC Policy Decision, Yellen press conference
January 28	FOMC Policy Decision (no press conference)
March 18	FOMC Policy Decision, Yellen press conference
April 29	FOMC Policy Decision (no press conference)
June 17	FOMC Policy Decision, Yellen press conference