Latest Data on the U.S. Economy is Mostly Optimistic as Stocks Anticipate All the News Expected This Week

The U.S. economy continues to exhibit strength in the labor market and weakness in manufacturing. It was more of the same last week, although the November jobs report exceeded even the most optimistic forecasts. At the same time, manufacturing activity remained in contraction and actually weakened somewhat, at least according to the Institute for Supply Management (ISM) report.

The economy created 266,000 new non-farm jobs last month, well above the 180,000 Bloomberg consensus. In addition, the prior two-month total was revised higher by 41,000. The total was distorted by roughly 45,000 due to returning GM strikers, but the underlying strength was still undeniable. That brought the three-month average gain to 205,000 new jobs, more than enough to absorb the growth in the labor force and push the unemployment rate down to 3.5 percent, a five-decade low. Average hourly earnings year-over-year edged down to 3.1 percent, from an upwardly revised 3.2 percent rate in October, suggesting decent income growth, in excess of inflation, but not problematic for either business or the Federal Reserve (Fed).

Consumers Remain the Growth Engine, While Manufacturing Continues to Soften

Along with a stronger than expected reading in consumer sentiment, the economic picture remains one of strength in the consumer sector, which continues to be the primary engine of growth. The preliminary December reading from the University of Michigan exceeded expectations by rising to its highest level since May, its fourth straight higher reading, and continuing to put the recession fears of August, the weakest reading of the year, in the rear-view mirror.

The manufacturing sector continued to soften in November. The ISM report fell short of expectations of a modest improvement from October, which itself was an improvement from September, albeit while remaining in contraction. But that improvement failed to materialize as the index instead slipped back slightly, although September continues to be the low reading so far. The flash manufacturing report from Markit told a somewhat different story, however. It showed that the manufacturing sector not only improved from October, but remained firmly in expansion territory, with steady improvement from its low reading in August.

Stocks and Bonds Improve Marginally Yet Again

Reinforced by the strong consumer, stocks edged higher once again. The S&P 500 added a fractional 0.2 percent, but that was enough to establish a new weekly closing high of 3,145.91. Stocks outside of the U.S. fared slightly better, as
the MSCI ACWI Ex-U.S. Index added 0.5 percent. Bond yields rose. The ten-year note climbed six basis points to 1.84 percent, while the two-year edged just one basis point higher to 1.62 percent, steepening the 2-10-year yield curve from 16 to 22 basis points in the process. Credit spreads narrowed.

Economic Developments This Week Could Move Markets

The week ahead is full of potentially market moving developments. The economic calendar includes the latest reading on the consumer sector with the retail sales report, along with consumer prices. And almost as an afterthought, the Fed meets this week and is widely expected to take no action, although the meeting will produce the latest summary of economic projections from the Federal Open Market Committee (FOMC). Voters in the U.K. take to the polls this week and are expected to support Boris Johnson’s Conservative Party, in what is, theoretically, the next step toward resolution of the Brexit impasse. Also this week, the next round of U.S. tariffs on Chinese imports is scheduled to take effect, although expectations are that these will be used as a bargaining chip in the ongoing effort to craft a so-called phase one trade deal.

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The Institute for Supply Management (ISM) manufacturing index is a national manufacturing index based on a survey of purchasing executives at roughly 300 industrial companies.

University of Michigan Consumer Sentiment Survey is a rotating panel survey based on a nationally representative sample that gives each household in the coterminous U.S. an equal probability of being selected. Interviews are conducted throughout the month by telephone. The minimum monthly change required for significance at the 95% level in the Sentiment Index is 4.8 points; for Current and Expectations Index the minimum is 6.0 points.

The Standard & Poor’s 500 Index (S&P 500® Index), an unmanaged index of common stocks, is frequently used as a general measure of market performance. The index reflects reinvestment of all distributions and changes in market prices but excludes brokerage commissions or other fees. It is not possible to invest directly in an index.

The Morgan Stanley Capital International All Country World Index Ex-U.S. (MSCI ACWI Ex-U.S.) is a market capitalization-weighted index that includes large- and mid-cap companies across 22 of 23 Developed Markets (DM) countries (excluding the US) and 26 Emerging Markets (EM) countries. With 2,420 companies, the index covers approximately 85% of the global equity outside the US.

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