

Baker Market Update: Week in Review

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When the outcomes produced by reality fall short of anticipated results, which side of the desired equation is off? Reality tends to be immutable and probably undeserving of any blame. On the other hand, forecasting economic data is always dodgy and this morning's monthly Jobs report from the Bureau of Labor Statistics (BLS) serves as a reminder of just how dodgy. The 155k gain in Non-Farm Payrolls was well short of the 200k that market surveyors were looking for. The 3.7% Unemployment Rate remained unchanged, as did the 62.9% Labor Force Participation Rate. The U6 *Underemployment* Rate nudged up by 0.2% to 7.6%, and that definitely runs counter to the trend. Modest revisions to the reports of the prior two months reduced the number of new jobs by 12k, so no big news there. Bigger news lies in the wage data.

The rise of 0.2% in Average Hourly Earnings came in just shy of the 0.3% expected, and last month's increase of the same 0.2% was downwardly revised by half. If there's any good news in the wage data, it's that the year-over-year growth rate remains unchanged at 3.1%. Less good news was the unexpected decline in the Index of Aggregate Weekly Hours Worked. The slippage of 0.2% doesn't seem like much, but with labor conditions seemingly so tight, shouldn't that be going the other way? Earlier in the week, the BLS reported that Unit Labor Costs (total compensation/real GDP) fell from a 1.2% growth rate in the second quarter to just 0.9% in quarter number three. Not something one might expect to see under what are believed to be ultra-tight conditions. As a corollary, Non-Farm Productivity over the same period picked up a bit from 2.2% to 2.3%. But, according to the Fed's Beige Book, pricing power remains elusive, citing evidence that tariff-driven input costs have risen faster than have final goods prices. The inflation dampening effect of that condition was seen in last week's unexpectedly soft inflation data.

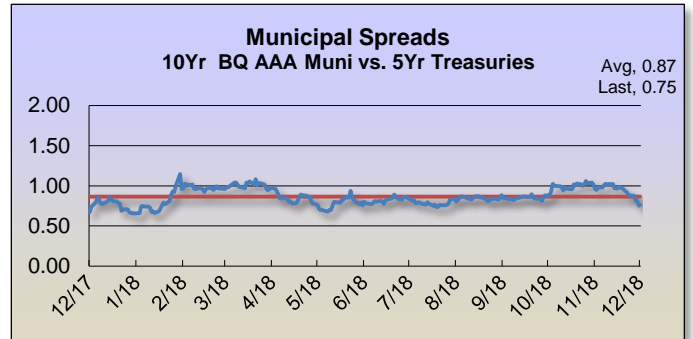
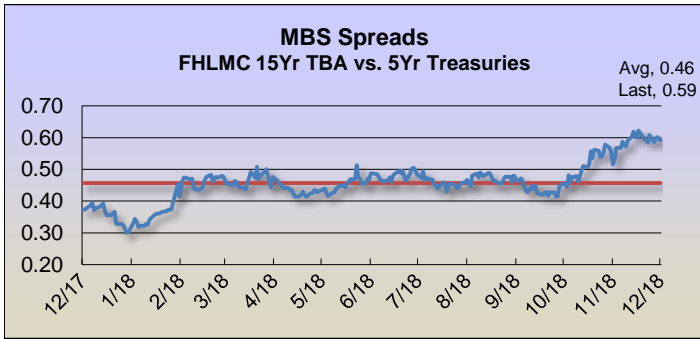
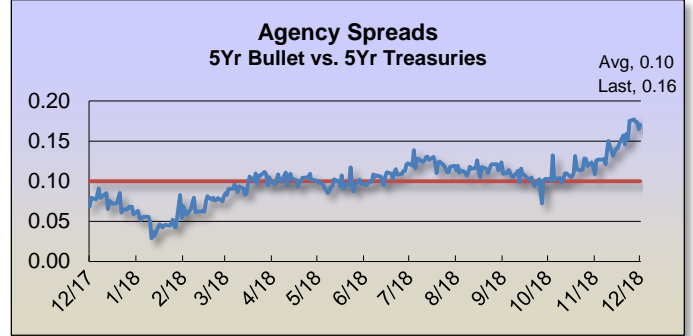
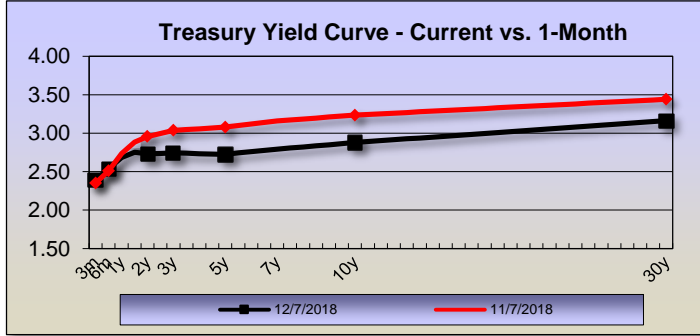
The tariff-driven efforts to better balance the nation's import/export *imbalance* have suffered a reversal over the past several months. After declining to the year's lowest shortfall of around \$43B back in May, the negative gap has widened to October's \$55.5B as growing trade tensions have added even more uncertainty to an already uncertain situation. Those tensions were not lessened by the arrest in Canada earlier in the week of the Chief Financial Officer of Huawei Technologies, a giant Chinese tech firm that is suspected of helping Iran worm its way out from under the burden of economic sanctions.

And how quickly the worm has turned for credit markets. The inversion in the slope of the short-end of the yield curve has generated fresh concerns about that condition's historical accuracy in predicting recessions. What's the Fed going to do now? Their actions will be data-driven, remember, and most of the recent data is still, on the surface, mostly positive. In remarks made earlier this week, FOMC Chairman Jerome Powell hit upon something that probably doesn't get enough attention. The lag that exists between policy implementation and the ultimate results of those policies is unpredictable and has grown greater as the velocity of money has plummeted throughout this long recovery. The public articulation of that recognition is seen by many observers as a realization by Mr. Powell that his grasp on 2% inflation may be more tenuous than previously thought, and dovetails nicely with Vice-Chairman Clarida's aversion to disinflation. Get it? *Dovetails*? Sorry, but the growing perception that the FOMC is turning more "dovish" was hard to miss this week. In a televised interview on the Bloomberg, Fed Governor Quarles said that "markets seem to be pretty clear about what it is that we're intending to do." Really!?

He said that on Monday, and since then, it doesn't seem like markets, any markets, seem very clear about anything. The epic volatility of equity markets serves to demonstrate the wildly shifting anticipation of maybe beneficial, maybe detrimental consequences of trade-relationship resolution. Bond prices have risen as a result of both a greater risk-off attitude, and a growing perception that the data-driven Fed will not be driven to the three rate hikes for 2019 that have long been built into the minds of many. As the short-end of the curve now depicts a slightly negative slope, the Ten-Year yield has plummeted to below 2.90%, with a mild price rally going on today.

According to the University of Michigan's Index of Consumer Sentiment, the minds of consumers are feeling pretty good. The headline index remains unchanged at 97.5, but according to this morning's preliminary report, the Current Conditions sub-Index leaped to 115.2 from 112.3. Feelings about the future may be a little less rosy as the Expectations sub-index fell somewhat significantly to 86.1 from 88.1. They may understand that October's 2.1% drop in Factory Orders along with the 4.3% decline in Durable Goods Orders are not flashing green signals of future prosperity.

Investors are still flashing their great expectations for one more rate hike from the Fed when the Committee meets later this month, at which time a new dot-plot will be produced. How different will it look from September's; or last December's? It may turn out to be a reminder to all of us that the plot of dots is not a forecast, and outcomes will be what they will be. Not, unfortunately, what we may *expect* them to be. Have a great weekend; be careful out there.



Treasury Market -- Historical						Fixed Rate Market										
Maty	Current	1Wk Change	Historical			Maty /AL	N-Call Agency	US Swap	AAA BQ Muni		Tax Muni	Agency Calls - Euro				
			1 Mo	6 Mo	1 Yr				C-Corp ²	S-Corp ³		Mty	3Mo	6mo	1Yr	2Yr
3mo	2.39	0.05	2.35	1.93	1.28	2yr	2.79	2.91	2.56	2.73	13.00	2Yr	1.94	1.94	1.94	-
6mo	2.54	0.01	2.51	2.11	1.46	3yr	2.83	2.89	2.65	2.82	20.00	3Yr	2.10	2.11	2.11	2.10
1yr	2.69	0.01	2.74	2.29	1.67	5yr	2.86	2.87	2.84	3.02	34.00	5Yr	2.19	2.22	2.24	2.24
2yr	2.73	(0.05)	2.96	2.49	1.80	7yr	2.98	2.90	3.04	3.23	48.00	7Yr	2.42	2.47	2.52	2.53
3yr	2.74	(0.06)	3.04	2.62	1.92	10yr	3.19	2.96	3.32	3.53	63.00	10Yr	2.57	2.62	2.69	2.72
5yr	2.73	(0.09)	3.08	2.76	2.14	15yr	3.31	3.03	3.71	3.95	92.00	January TBA MBS				
7yr	2.79	(0.11)	3.16	2.87	2.28	20yr	3.43	3.06	4.07	4.34	87.00	Cpn	15Yr -Yld/AL		30Yr -Yld/AL	
10yr	2.88	(0.11)	3.24	2.92	2.36	25yr	3.55	3.06	4.19	4.46	89.50	2.00	3.34	4.9y		
30yr	3.16	(0.13)	3.44	3.07	2.76	30yr	3.55	3.05	4.31	4.59	92.00	2.50	3.18	5.1y		
												3.00	3.18	5.5y	3.52	9.7y
												3.50	3.35	5.1y	3.68	9.5y
												4.00			3.82	7.6y
												4.50			3.88	6.3y

* Interpolated

Key Market Indices					
Index	Current	1Wk Change	Historical		
			1 Mo	6 Mo	1 Yr
Fed Funds	2.25	--	2.25	1.75	1.25
Primary Discount	2.75	--	2.75	2.25	1.75
2ndary Discount	3.25	--	3.25	2.75	2.25
Prime Rate	5.25	--	5.25	4.75	4.25
Sec. O.N. Finance	2.34	0.10	2.22	1.73	--
1 Month LIBOR	2.39	0.04	2.32	2.03	1.41
3 Month LIBOR	2.77	0.03	2.59	2.32	1.52
6 Month LIBOR	2.89	--	2.84	2.48	1.71
1 Year LIBOR	3.11	--	3.12	2.74	1.99
6 Month CD	2.89	0.12	2.84	2.47	1.70
1 Year CMT	2.70	0.01	2.72	2.32	1.68
REPO O/N	2.32	--	2.22	1.73	1.05
REPO 1Wk	2.24	--	2.24	1.85	1.29
CoF Federal	2.132	--	2.070	1.811	1.472
11th D. CoF (Oct)	1.079	--	1.018	0.895	0.737

FHLB Fixed Advance Rates			
Maturity	Chicago	Boston	Topeka
3mo	2.61	2.73	2.70
6mo	2.71	2.81	2.82
1yr	2.92	2.94	3.07
2yr	2.96	3.13	3.26
3yr	3.00	3.19	3.31
4yr	3.02	3.22	3.33
5yr	3.04	3.25	3.36
7yr	3.23	3.47	3.45
10yr	3.41	3.67	3.62
5yr Am	3.06		3.33
10yr Am	3.27		3.54

Fed Fund Futures	
Maturity	Rate
Dec-18	2.278
Jan-19	2.385
Feb-19	2.395
Mar-19	2.430
Apr-19	2.470
May-19	2.495
Jun-19	2.515
Jul-19	2.545
Aug-19	2.560
Sep-19	2.580
Oct-19	2.590

Weekly Economic Calendar						
This Week & Next						
Date	Release	Per.	Est.	Actual	Prior	Revised
12/03	Markit US Manufacturing PMI	Nov F	55.40	55.30	55.40	--
12/03	ISM Manufacturing	Nov	57.50	59.30	57.70	--
12/03	ISM Employment	Nov	--	58.40	56.80	--
12/03	ISM Prices Paid	Nov	70.00	60.70	71.60	--
12/03	ISM New Orders	Nov	--	62.10	57.40	--
12/05	MBA Mortgage Applications	11/30	--	2.00%	5.50%	--
12/06	Challenger Job Cuts YoY	Nov	--	51.50%	153.60%	--
12/06	ADP Employment Change	Nov	195k	179k	227k	225k
12/06	Trade Balance	Oct	-\$55.0b	-\$55.5b	-\$54.0b	-\$54.6b
12/06	Nonfarm Productivity	3Q F	2.30%	2.30%	2.20%	--
12/06	Unit Labor Costs	3Q F	1.00%	0.90%	1.20%	--
12/06	Initial Jobless Claims	12/1	225k	231k	234k	235k
12/06	Continuing Claims	11/24	1690k	1631k	1710k	1705k
12/06	Bloomberg Consumer Comfort	12/2	--	60.30	60.60	--
12/06	Markit US Services PMI	Nov F	54.40	54.70	54.40	--
12/06	Markit US Composite PMI	Nov F	--	54.70	54.40	--
12/06	ISM Non-Manufacturing Index	Nov	59.00	60.70	60.30	--
12/06	Factory Orders Ex Trans	Oct	--	0.30%	0.40%	0.10%
12/06	Durables Ex Transportation	Oct F	0.10%	0.20%	0.10%	--
12/06	Cap Goods Ship Nondef Ex Air	Oct F	--	0.30%	0.30%	--
12/07	Change in Nonfarm Payrolls	Nov	198k	155k	250k	237k
12/07	Two-Month Payroll Net Revision	Nov	--	-12k	--	--
12/07	Change in Private Payrolls	Nov	198k	161k	246k	251k
12/07	Change in Manufact. Payrolls	Nov	18k	27k	32k	26k
12/07	Unemployment Rate	Nov	3.70%	3.70%	3.70%	--
12/07	Underemployment Rate	Nov	--	7.60%	7.40%	--
12/07	Average Hourly Earnings YoY	Nov	3.10%	3.10%	3.10%	--
12/07	Average Weekly Hours All Employees	Nov	34.50	34.40	34.50	--
12/07	Labor Force Participation Rate	Nov	62.90%	62.90%	62.90%	--
12/07	U. of Mich. Sentiment	Dec P	97.00	97.50	97.50	--
12/07	U. of Mich. Current Conditions	Dec P	--	115.20	112.30	--
12/07	U. of Mich. 1 Yr Inflation	Dec P	--	2.70%	2.80%	--
12/10	JOLTS Job Openings	Oct	--	--	7009.00	--
12/11	NFIB Small Business Optimism	Nov	107.00	--	107.40	--
12/11	PPI Final Demand YoY	Nov	2.50%	--	2.90%	--
12/11	PPI Ex Food and Energy YoY	Nov	2.50%	--	2.60%	--
12/11	PPI Ex Food, Energy, Trade YoY	Nov	--	--	2.80%	--
12/12	CPI YoY	Nov	2.20%	--	2.50%	--
12/12	CPI Ex Food and Energy YoY	Nov	2.20%	--	2.10%	--
12/12	CPI Index NSA	Nov	251.93	--	252.89	--
12/12	CPI Core Index SA	Nov	259.40	--	258.94	--
12/12	Real Avg Weekly Earnings YoY	Nov	--	--	0.90%	0.80%
12/12	Real Avg Hourly Earning YoY	Nov	--	--	0.70%	0.60%
12/13	Import Price Index YoY	Nov	--	--	3.50%	--
12/13	Export Price Index YoY	Nov	--	--	3.10%	--
12/14	Retail Sales Ex Auto and Gas	Nov	0.40%	--	0.30%	--
12/14	Retail Sales Control Group	Nov	0.40%	--	0.30%	--

MBS Prepayments ⁴						
3-Month CPR						
Type	2.0	2.5	3.0	3.5	4.0	4.5
FN 10y	10.4	11.8	13.8	14.2	18.2	31.0
FH/FN 15y	5.7	5.9	6.7	7.9	13.2	15.0
GN 15y	6.5	9.9	11.0	12.3	12.4	11.8
FH/FN 20y		5.4	6.8	7.9	8.3	9.7
FH/FN 30y	1.5	4.8	3.8	3.6	4.7	7.5
GN 30y	9.2	9.2	11.8	14.2	12.9	13.0

CPR Projections						
Type	2.0	2.5	3.0	3.5	4.0	4.5
FN 10y	11.7	11.6	12.3	18.2	12.8	23.5
FH/FN 15y	7.4	8.0	7.3	8.9	12.2	21.5
GN 15y	9.3	10.0	12.7	14.6	14.3	13.7
FH/FN 20y	0.1	6.6	7.3	8.8	11.1	12.5
FH/FN 30y	4.9	5.6	6.1	6.6	9.7	12.5
GN 30y	9.7	7.8	8.6	10.1	16.0	19.0

Other Markets					
Index	Current	1Wk Chng	Historical		
			1 Mo	6 Mo	1 Yr
Currencies					
Japanese Yen	112.70	(0.87)	113.52	109.70	113.09
Euro	1.14	0.01	1.14	1.18	1.18
Dollar Index	96.75	(0.52)	96.00	93.44	93.80
Major Stock Indices					
Dow Jones	24,751	(588)	26,180	25,241	24,211
S&P 500	2,675.9	(61.8)	2,813.9	2,770.4	2,637.0
NASDAQ	7,118.0	(155)	7,570.8	7,635.1	6,812.8
Commodities					
Gold	1,245.4	25.2	1,228.7	1,298.7	1,249.8
Crude Oil	53.76	2.83	61.67	65.95	56.69
Natural Gas	4.46	(0.15)	3.56	2.93	2.76
Wheat	516.5	0.8	510.3	526.8	394.3
Corn	374.5	8.0	372.3	376.3	338.8

Notes	
1 Call Agy = Maturity at left w/ a 1-Year Call at Par	
2 Muni TEY (21% Fed, 0.5% CoF)	
3 S-Corp TEY Muni (29.6%, no TEFERA)	
4 MBS Prepayments are provided by Bloomberg	

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