MV CAPITAL MANAGEMENT

# Weekly Market Flash

## Jobs Report Sets a Strange Tone for the Year

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Welcome to 2022! It's that time of the year again, when we all look around us and try to make sense of what might lie in store for the remaining eleven months and change of this year, either the third or the second year (depending on how you count your decades) of this century's Twenties. We're only seven days in, which means that it's too early to give any kind of meaningful definition to the year ahead. Based on what we've seen so far, though, it has the potential to be a strange one, with a larger than usual number of unpredictable twists and turns.

### Jobs, the Good and the Bad

As usual, most market watchers are focused primarily on what the Fed is going to do with monetary policy this year. Ahead of the Bureau of Labor Statistics December jobs report that came out this morning, we wondered what Mr. Market, that quirky basket of extreme emotions with the attention span of a fly, would see as either good or bad in the report. "Good" by the definition of stock market bulls being something that would make the Fed think twice about pinning rate hikes on the 2022 calendar (which would mean worse than expected numbers about payrolls and unemployment, in other words what most people outside marketworld would think of as "bad").

What we got was a strange mix of numbers: payroll gains of only 199,000 were much lower than the 400,000 expected (which should be good news for the "bad is good" crowd), but an unemployment rate that dropped to 3.9 percent, better than expected and ever so close to the 3.5 percent level right before the pandemic. In fact that February 2020 number was the lowest unemployment had been since 1969, so it would seem that we are exceedingly close to, if not already at, the "maximum employment" target that is one half of the Fed's mandate.

### Wages and Prices

So for those cheering for a "bad is good" jobs report, the favorable trend in the unemployment rate took some of the fun away from the underwhelming payroll number. But there's more bad news for the bulls, in the form of wage growth. Average hourly wage growth was 4.7 percent, significantly higher than expected and yet another marker in the case for longer, stickier inflation. This is the other side of the Fed's mandate: stable prices in the form of a two percent inflation rate target. Clearly we are well above that, with the Consumer Price Index currently at 6.8 percent and expected to trend over seven percent in the next report coming out next week.

When US stocks fell sharply earlier this week, one of the main catalysts cited was the release of minutes from the December FOMC meeting. The minutes essentially validated the Summary Economic Projections that came out at the conclusion of the December meeting, pointing to a likelihood for three rate increases this year. If anything, the combination of a near-full employment labor market and worries that wages and consumer prices could get caught in a positive-feedback spiral makes those three rate hikes look even more likely.

What might all of this mean for the market?

## Reality Bites Purchasing Power

We always caution against reading too much into one economics report, or even several reports. Any number of things could happen that produce an entirely different outcome from the growth and inflation trends suggested by the current numbers. But one fact is inescapable: as of today, the yield on the 10-year Treasury note is around 1.75 percent, and inflation is close to seven percent. That's more than five percentage points of negative purchasing power for anyone holding high quality fixed income paper. So far, inflationary expectations have not set in to such an extent that investors pour en masse out of Treasuries, sending rates higher. But it's not going to take too many more reports of either high-octane wage growth or retail price increases to firm up those expectations. In other words, interest rates have plenty of upside room to move, simply based on the historical anomaly of such a massive gap between nominal bond yields and inflation.

Will this lead to a major move into real assets like energy commodities, reminiscent of the 1970s? Certainly oil prices are having a minute; spot prices for Brent crude oil are up more than six percent in this first week of the year. Natural gas is likewise continuing its steady rise, to the consternation of European households looking at their monthly utility bills. Geopolitical tensions may exacerbate these conditions, notably this week in Kazakhstan, a major oil producer, that is experiencing the first instance of widespread political unrest since the dissolution of the Soviet Union.

All these developments demand our attention and consideration as we consider the right moves to make for portfolios entrusted to our management. Buckle up: it's going to be an interesting year.

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