MV CAPITAL MANAGEMENT

Weekly Market Flash

Last Big News Cycle for the Market in '23

December 8, 2023

There are still 23 days to go before calendar year 2023 rolls to an end. That leaves plenty of time for surprises of a good or not good variety to make themselves known to the market. In terms of things we do know, though, there really is just one more big news cycle to go, and it started today.

Jobs, Jobs, Jobs

No, the Bureau of Labor Statistics report this morning was not a barnstormer of the ilk we get sometimes, those surprises with half a million new jobs announced or the lowest unemployment rate since Lyndon Johnson was president. But still – here we are, twenty months into the most draconian monetary tightening program since the early 1980s, and the economy is still pumping out those jobs. 199,000 new payroll gains, to be precise, according to today's BLS report. And, for good measure, the unemployment rate unexpectedly dropped again, from 3.9 percent to 3.7 percent (which by the way is only 0.3 percent higher than the 3.4 percent low for this cycle, which does in fact match the LBJ-era low). As always, there are various anomalies that skew the monthly numbers one way or another, a prominent one this time being the 30,000 auto industry workers who came back onto the job after the end of the recent UAW strike. But that was public knowledge ahead of this morning's report, and the 199K was still 24,000 more than economists had predicted according to FactSet, a market research company.

Next Up, Inflation and the Fed

Two more big-ticket events will round out this news cycle: the Consumer Price Index report next Tuesday and then the Federal Open Market Committee decision about interest rates on Wednesday. For the CPI report, economists are looking for a month-to-month change of 0.3 percent in core inflation (i.e., excluding food and energy). That would translate to a year-on-year core inflation rate of 4.0 percent, which is still twice as high as the Fed's two percent target. Investors would like to see the month-on-month number come in lower; the PCE inflation report that came out a couple weeks ago showed just a 0.16 percent month-on-month gain, which gets us closer to that two percent year-on-year number.

The Fed is likely to keep rates where they are. But what they say after the FOMC meeting matters a great deal, because once again the bond market has been merrily going its own way without listening to any Fed official who repeats the "higher for longer" mantra. As we have discussed in recent commentaries, the bond market sizzled through November as traders resurrected their persistent fantasy of successive rate cuts in 2024.

For the Bond Market, There's Always a Pony Out Back

Current bond market levels indicate that investors have priced 1.25 percent worth of rate cuts into their outlook for 2024, a number we regard as sheer madness. Assuming a cut of 0.25 percent each time, that would mean the Fed would be cutting rates five times – five! – in a year when the economy is still growing (as far as we know now), inflation is still well above target, job growth is healthy even though off its highest levels and, to top it all off, 2024 is an election year in which the Fed is likely to be more cautious than usual in doing anything with interest rates that could be criticized as politically favorable to one side or the other (note to Fed: you'll get criticized by the politicos no matter what you do, so just do the right thing).

Why does the bond market keep doing this? We have seen this "fight the Fed" mentality all throughout the rate tightening cycle. All the while, the Fed has meant it when it says "higher for longer." Why is it going to be different this time? Spoiler alert: it likely won't be different this time. Next week awaits.

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