OBSERVATIONS

- Markets slid last week amid profit taking and renewed fears of slower growth in the US. The S&P 500 fell by -4.2% and small caps (Russell 2000) lost -5.7%, with defensive sectors generally holding up better on a relative basis. The yield on a 10-year Treasury fell -19 basis points to end the week at 3.71%.[1]
- August's ISM manufacturing PMI came in below expectations at 47.2—any reading below 50 denotes contracting activity—but is slightly better than July's 46.8 reading. This marks 21 months out of the past 22 months where the manufacturing PMI has been below 50.[1]
- In contrast, the ISM services PMI in August inched up to 51.5 from July's 51.4 reading—suggesting that, while not robustly growing, the service sector remains in expansion territory.[1]
- Construction spending in July declined in August by -0.3% month-over-month (MoM) in part due to the fact that July's construction activity was revised higher. However, over the first seven months of 2024, total construction spending is outpacing the same period last year by +8.8% year-over-year (YoY).[1]
- The Jobs and Labor Turnover Survey (JOLTS) report from July showed that open job postings fell by -250k MoM to 7.67 million. While down from the historic peak in March-2022, 7.67 million job openings are still +60k more than the pre-pandemic high of 7.59 million openings in Nov-2018.[1]
- Initial unemployment claims eased last week to 227k, which was -5k lower than prior week's revised figure of 232k—on a non-seasonally adjusted basis last week's claims were -2k lower than the same week in 2023.[1]
- The August jobs report was mixed. The US economy created +142 new jobs—but that was about -20k below expectations—and the job numbers for June (-61k) and July (-25k) were both revised lower to +118k and +89k respectively. On the positive side, the unemployment rate moved lower to 4.2% from July's 4.3% figure, labor force participation rate remained steady at 62.7%, and the average work week edged up by 0.1 hour to 34.3 hours.[1]

EXPECTATIONS

- South Korean exports—a bellwether for global trade—increased by +11.4% YoY in August, and over the period Jan to Aug-2024, South Korean exports have increased about +10.2%, suggesting global trade is picking-up which bodes positively for global earnings growth.[1]
- With about 99% of the S&P 500 having reported, Q2 earnings growth was +11.3% YoY and 79% of firms had a positive earnings surprise which is above the five-year (77%) and 10-year (74%) averages. Looking ahead to Q3, analysts currently are expecting +4.9% YoY earnings growth and +4.8% YoY top-line sales growth.[2]

ONE MORE THOUGHT: Global liquidity and G10 central bank rate cutting[3]

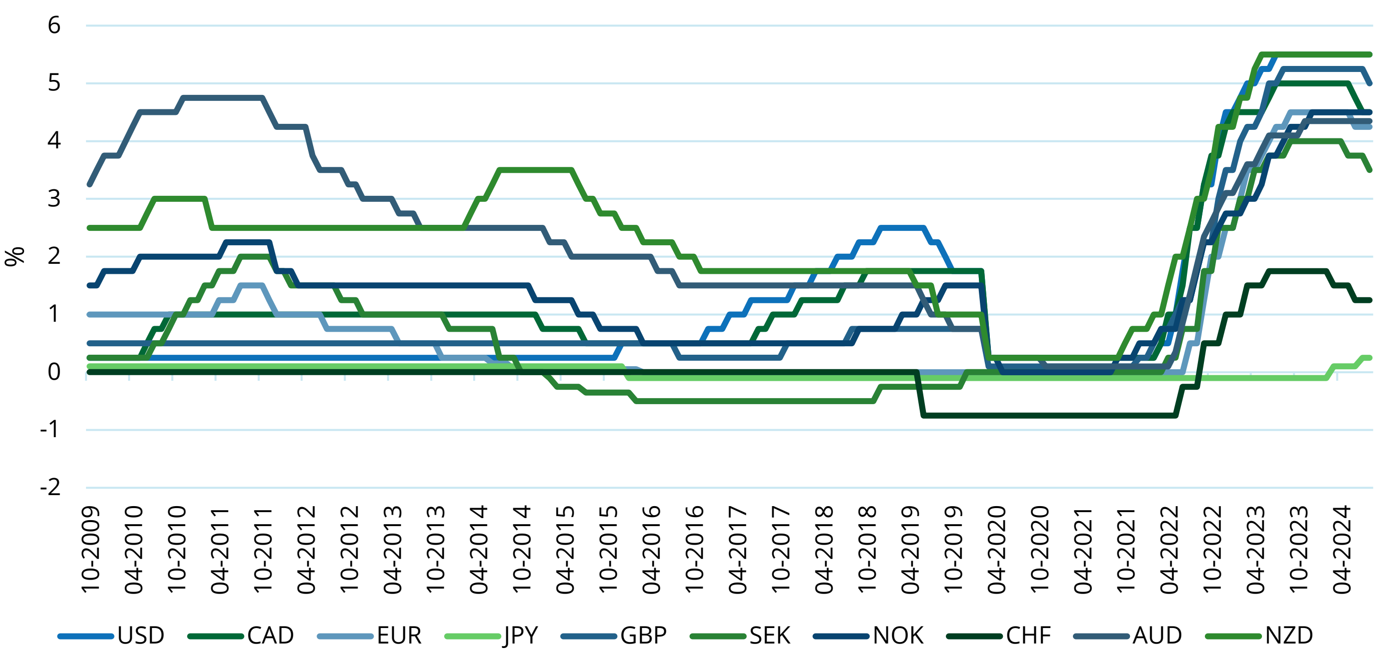
As we approach the first Fed policy rate cut it is worth pointing out that most central banks, including those of the western G10 block, cut rates to zero during the COVID pandemic only to have to raise them in the 2021-2023 period to fight inflation. For a period of time from mid-2020 to late-2021 global liquidity was abundant and then in short order global liquidity tightened. As the Fed looks all but certain to cut rates at least -25 basis points in two weeks it does so as most other G10 central banks have already started or have also signaled their intent to start rate cuts. The Swiss National Bank was the first to cut rates in March, but it was soon followed by the central banks of Sweden, Canada, and England. The European Central Bank also cut rates this past July and signaled additional cuts

[1] *Bloomberg LP, 9/6/2024*
[2] *FactSet Earnings Insight 9/6/2024*
[3] *GS Global Markets Analyst "Lessons From G10 Cutting Cycles" 9/2/2024*

are likely in the coming months. Goldman Sachs examined over 70 rate cutting cycles across the G10 countries over the past 20 years and found that on average they persist about 8 months and the average decline in the central bank policy rate is about -150 basis points. Given this, it is easy to see the likelihood that the shape of the yield curves across the globe are likely to radically shift over the coming 6-9 months. Once again, global liquidity will increase, and a global cap-ex cycle could emerge in 2025 as interest rates fall across the western world. This should be a positive catalyst for global trade and provide a tailwind for corporate profits, particularly for those firms whose products are central to global manufacturing and non-residential construction. Additionally, a myriad of firms—including the preponderance of small cap stocks—that borrow through floating rate loans should see some easing of interest expenses over the next year. The change in global liquidity will also change the relative return profile for bonds, cash (money markets), and equities looking forward. The next several months are likely to test the old adage that interest rates in money market accounts "move higher like an escalator but lower like an elevator" leaving investors with large cash positions with a lower expected return profile.

CHART OF THE WEEK

G10 Central Bank Policy Rates



Source: Clearstead, Bloomberg 9/4/2024; USD=US, CAD=Canda, EUR=Eurozone, JPY=Japan, GBP=United Kingdom, SEK=Sweden, NOK=Norway, CHF=Switzerland, AUD=Australia, NZD=New Zealand

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