

# Economic Update

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This weekly update provides a snapshot of changes in the economy and markets and their implications for investors.



## Growth

The second estimate of 3Q U.S. GDP growth remained at 3.5% q/q saar, decelerating from the 4.2% pace in 2Q. The initial estimate showed a surge in inventory growth, which contributed even more to overall GDP growth per the second estimate, but was offset by a deeper detraction from net exports. Early indicators suggest GDP growth could slow further in 4Q. Following weak housing starts and existing home sales data, both new and pending home sales disappointed.



## Jobs

Job openings fell to 7 million, but last month had a healthy upward revision. Nonfarm payrolls increased by 250,000 jobs in October, rebounding from September and well above consensus. Wages for production and non-supervisory workers climbed 0.3% after an upward revision last month, bringing y/y wage growth to 3.2%, the strongest since April 2009. The labor force participation rate ticked up to 62.9% from 62.7%, an impressive gain at this stage in the expansion.



## Profits

With 465 companies having reported (95.3% of market cap), our current estimate for 3Q18 earnings is \$41.64 (\$33.26 ex-financials), and 78% of companies have beaten on earnings while 49% have beaten on revenue. Despite initial concerns of peak earnings in 2Q18, 3Q18 earnings surged to a 32.9% y/y growth rate thanks in part to tax reform, but also to healthy economic conditions (strong consumer spending, higher oil prices, and robust pricing power), which more than offset the headwinds (stronger dollar and rising wages, raw materials and interest costs).



## Inflation

Headline PCE, the Fed's preferred inflation measure, held at 2.0% y/y in October. Core PCE fell slightly to 1.8% y/y from 2.0%. Headline CPI increased in October by 0.3% m/m and 2.5% y/y, pushed up by high oil prices, which have since receded significantly. Core CPI came in relatively steady from last month at 0.2% m/m and 2.1% y/y. Overall, inflation continues to be very stable.



## Rates

Fed Chair Jay Powell commented that interest rates are "just below" neutral, walking back his recent prior comments that "we're a long way from neutral at this point." This allayed fears that the Federal Reserve will tighten monetary policy into restrictive territory. As expected, the Fed did not hike rates in November, maintaining its target range for the federal funds rate at 2.00%-2.25%. This suggests one additional rate hike at the mid-December meeting, and two more in 2019.



## Risks

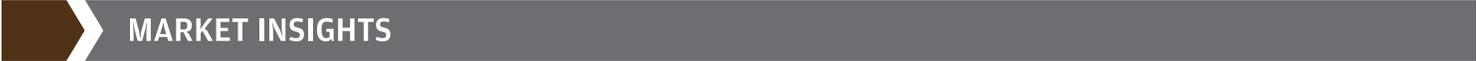
- Trade tensions may result in a slowdown in global growth.
- The Federal Reserve may tighten monetary policy too aggressively.
- Weak labor force growth could hinder economic growth in the future.



## Investment Themes

- Risk assets have reasonable valuations and momentum heading toward the end of this cycle.
- Credit and short duration tend to perform well late cycle, while core fixed income protects heading into a downturn.
- Long-term growth prospects and cheap absolute and relative valuations support international equities.

■ Denotes updated information

MARKET INSIGHTS

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**Data are as of December 3, 2018**

**Past performance does not guarantee future results.**

**Diversification does not guarantee investment returns and does not eliminate the risk of loss.**

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