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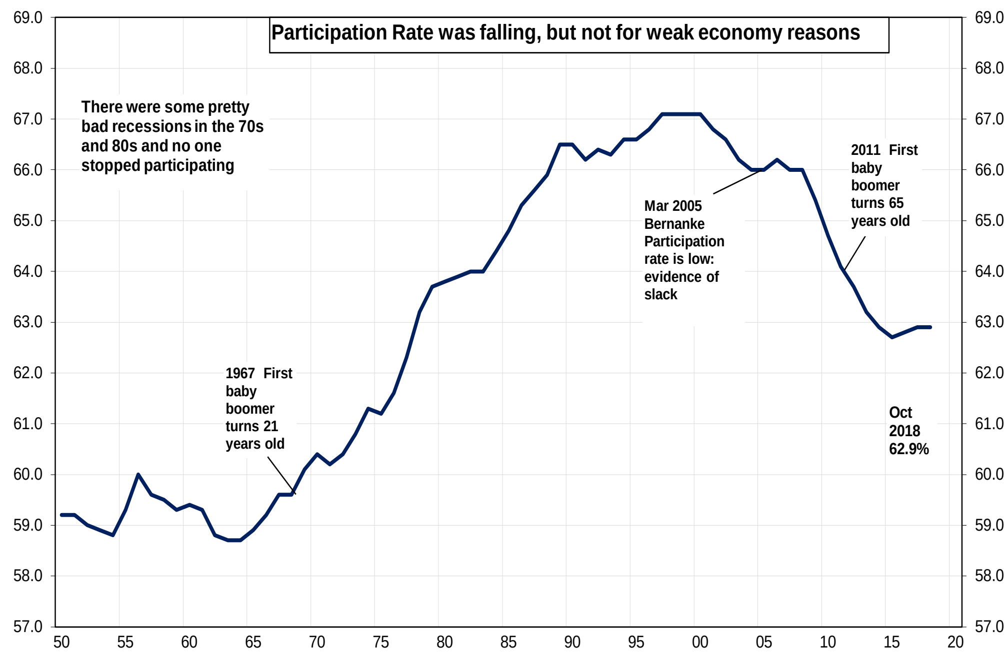
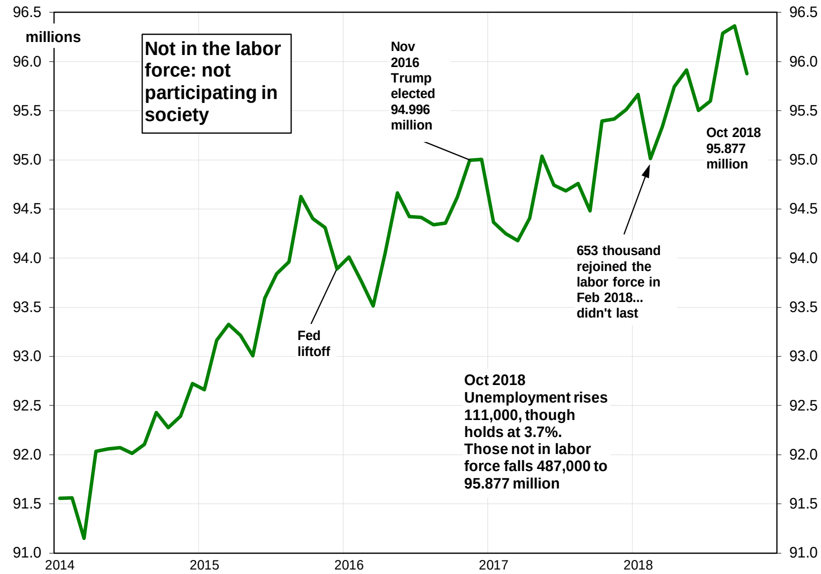
COME JOIN US. PARTICIPATE IN LIFE.

According to the Bureau of Labor Statistics (BLS) you aren't participating in life unless you are working or looking for work. The participation rate from the October monthly employment situation report released Friday, November 2, 2018, "the biggest market moving number in the world," was 62.9% which is calculated as the labor force (156.562 million employed + 6.075 million unemployed) divided by the population of 258.514 million (population 16-years and older and not in military or in prison) equals 162.637/258.514 or 62.9%. Why isn't participation higher than 62.9%? Powell says he is trying to extend the economic expansion as long as possible to lift everyone's boat, to bring in those on the fringes of society back into the labor force. We think the participation rate is falling with the retirement of the baby boom generation, those born from 1946 to 1964, when the birth rate shot up after WWII.



What about those on the fringe of society, the 95.877 million <u>not</u> in the labor force… you mean people not participating and having fun in America because they are 95 years old and aren't working or seeking work? There's obviously millions of retirees in the country. Out of 95.877 million not in the labor force, only 5.309 million say they are looking for work.

Those not in the labor force continues to rise as the overall population does. It is not a sign of labor market weakness—another problem that Washington has to fix. Washington, including the Federal Reserve, tends to try to help a little too much historically, chasing the economic cycle up and down with fixes and patches that do little to change the spending and savings habits of workers and their companies. Some people do drop out of the labor force in recessions and reenter the labor force when the labor market improves. This won't be the case for the overall number this time though as the baby boom generation is retiring and dropping out which increases the dropouts for at least another decade.



Age is a key factor in whether you are in or out of the labor force and "participating" in society by working or looking for work. In 2017, if you are 16-19 years old, only 35.2% are in the labor force, and if you are 65-69 years old, only 32.3% are participating. The average is 62.9%, and the biggest participation years are when you are 35-44 years old. It's all downhill from there, once you hit 45 years old. People start slacking off.

House Speaker Paul D. Ryan (R-WI)
Look, not to get into statistics, but our labor force participation rates are pretty awful. We haven't seen these since like the Carter years. What it means -- what that means is, able-bodied adults aren't working or aren't looking for work. They're marginalized. They're on the sidelines. We've got to get them back into the economy.

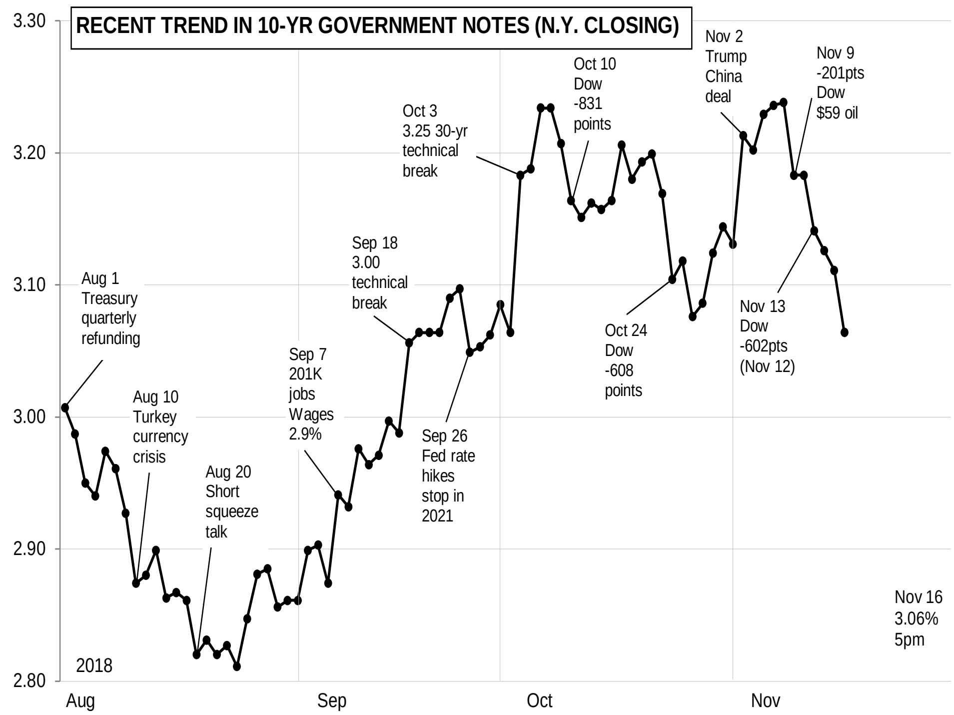
Those not participating always gets exaggerated by politicians running for office trying to help the voters. In October 2018, there were 95.792 million people not in the labor force, but 90.744 million don't want a job. Maybe some of these can be coaxed in to the labor force as the country will need more workers now that factories are coming back to the U.S. There were 5.048 million who want a job and 3.059 million had not looked for work in a year. Marginally attached, can work now, 1.491 million, is often thought to be a sign of economic weakness although just 506 thousand said they were "discouraged." The labor market is the strongest since the 60s, despite 95 million not working/looking.

BREAKDOWN OF THOSE NOT IN THE LABOR FORCE			
Thousands, NSA	Oct 17	Oct 18	Change
Total not in labor force	95,301	95,792	491
Don't want job now	90,364	90,744	380
Want a job	4,938	5,048	110
Did not search for work in a year	2,909	3,059	150
Searched in last year, not in the past 4 weeks	2,029	1,989	-40
Not available to work now	494	498	4
Marginally attached, can work now	1,535	1,491	-44
Discouraged	524	506	-18
Reasons other than discouraged	1,010	984	-26
Family obligations	204	182	-22
In school or training	175	143	-32
Poor health or disability	133	146	13
Other	499	513	14

CIRCLE OF LIFE PARTICIPATION RATE 2017	
35.2%	16-19 years old
71.3%	20-24 years old
82.1%	25-34 years old
82.7%	35-44 years old
80.3%	45-54 years old
71.9%	55-59 years old
56.5%	60-64 years old
32.3%	65-69 years old
19.7%	70-74 years old
8.3%	75-plus years
62.9%	Total

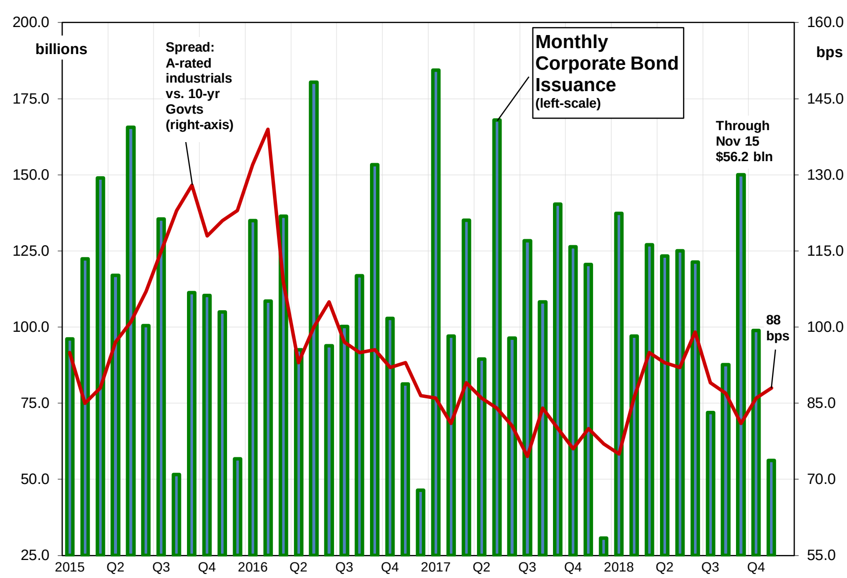
MARKETS OUTLOOK

	28-Sep 2018	Q4 2018	Q1 2019	Q2 2019	Q3 2019	Q4 2019	Q1 2020	Q2 2020	Q3 2020	Q4 2020	Q1 2021
30-Yr Treasury	3.21	3.25	3.40	3.45	3.65	3.60	3.80	3.85	3.85	3.95	3.95
10-Yr Note	3.06	3.10	3.20	3.30	3.50	3.50	3.70	3.80	3.80	3.95	3.95
5-Yr Note	2.95	3.00	3.10	3.20	3.40	3.45	3.65	3.75	3.80	3.95	3.95
2-Yr Note	2.82	2.90	3.00	3.15	3.40	3.40	3.60	3.75	3.80	4.00	4.00
3-month Libor	2.40	2.70	2.95	3.20	3.45	3.45	3.70	3.90	3.90	4.20	4.15
Fed Funds Rate	2.25	2.50	2.75	3.00	3.25	3.25	3.50	3.75	3.75	4.00	4.00
2s/10s spread	24	20	20	15	10	10	10	5	0	(5)	(5)
Libor/funds spd	15	20	20	20	20	20	20	15	15	20	15



The bond market was closed Monday for Veterans' Day when the stock market plummeted 602 points. 10-year yields fell 4 bps to 3.14% on Tuesday from last Friday's 3.18% close. Yields fell for a time with UK Gilts on Brexit woes on Thursday. The downward move in yields on Friday seems to have been helped along by Fed comments and the market's growing belief perhaps that world growth risks are rising and the Fed funds rate is getting into the neutral zone soon. "The Fed is closer to finishing the job." Philadelphia Fed President Harker even said he wasn't ready to commit to a December rate hike. The odds of a 25 bps Fed rate hike to 2.5% on December 19 are 72% versus 80% last week.

CORPORATE BONDS: BOSTON PROPERTIES, MARRIOTT, DOWDUPONT



Corporate offerings were $19.5 billion in the November 16 week versus $28.6 billion in the November 9 week. On Wednesday, DowDuPont sold an 8-part $12.7 billion deal. It priced a $2.25 billion 4.725% 10-yr (m-w +25bp) at 160 bps (Baa1/A-). The chemical company will use the proceeds to reduce liabilities of its two main subsidiaries, Dow and Corteva, which will be spun out: its remaining specialty products business will change its name to DuPont. Corporate bond yields (10-yr Industrials rated A2) were 88 bps above 10-yr Treasuries this week versus 84 bps last Friday.

FEDERAL RESERVE POLICY

The Fed meets December 18-19 to consider its monetary policy. Our recommendation would be to raise rates to 2.5%, and then tell markets you will take another look at what needs to be done at the June 2019 meeting. Hit the pause button. Mortgage rates have risen too quickly from 3.5% to almost 5% and may be having a negative effect on the economy. Fed policy restraint can be thought of in terms of level and speed. 2.5% is not very high historically, but the speed, a rate hike every quarter starting December 2016 except one; may constitute "tightening" of a sort.

Selected Fed assets and liabilities					Sep 10
Fed H.4.1 statistical release					2008**
billions, Wednesday data	14-Nov	7-Nov	31-Oct	24-Oct	pre-LEH
Factors adding reserves					
U.S. Treasury securities	2270.420	2270.436	2270.399	2294.215	479.782
Federal agency debt securities	2.409	2.409	2.409	2.409	0.000
Mortgage-backed securities	1670.825	1668.989	1668.989	1676.956	0.000
Primary credit (Discount Window)	0.110	0.016	0.061	0.048	23.455
Term auction credit (TAF auctions)	0.000	0.000	0.000	0.000	150.000
Asset-backed TALF	0.000	0.000	0.000	0.000	
Maiden Lane (Bear)	0.007	0.007	0.007	0.007	29.287
Maiden Lane II (AIG)	0.000	0.000	0.000	0.000	0.000
Maiden Lane III (AIG)	0.000	0.000	0.000	0.000	
Central bank liquidity swaps	0.047	0.079	0.080	0.080	62.000
Federal Reserve Assets	4193.6	4189.8	4186.8	4220.8	961.7
3-month Libor %	2.63	2.60	2.56	2.51	2.82
Factors draining reserves					
Currency in circulation	1702.792	1699.134	1696.031	1690.508	834.477
Term Deposit Facility	0.000	0.000	0.000	0.000	0.000
Reverse repurchases w/others	0.660	1.875	4.815	6.444	0.000
Reserve Balances (Net Liquidity)	1799.528	1828.825	1771.541	1825.009	24.964
Treasuries within 15 days	34.304	34.357	34.357	23.886	14.955
Treasuries 16 to 90 days	59.403	59.402	45.211	79.515	31.549
Treasuries 91 days to 1 year	310.003	310.003	324.193	308.510	69.272
Treasuries over 1-yr to 5 years	993.899	985.378	985.372	999.360	170.807
Treasuries over 5-yrs to 10 years	255.606	264.108	264.095	265.781	91.863
Treasuries over 10-years	617.206	617.188	617.170	617.162	101.337

**September 10, 2008 is pre-Lehman bankruptcy of 9-15-08

Interesting comments by Fed Chair Powell, the President's pick to head the central bank, on Wednesday at the Dallas Fed. Paraphrasing/quoting verbatim from wire service news stories without quotes, "Look no hands," Powell said in Q&A that the Fed has to be thinking about how much further to raise rates, and the pace at which we will raise rates, and the Fed's goal is to "extend the recovery, expansion, and to keep unemployment low, to keep inflation low." That's funny. We thought the Fed was raising rates (above 3%-the top of neutral) to slow the economy which in this moderate growth era means stopping the unemployment rate from falling further if not in fact trying to move the 3.7% unemployment rate back up to "4.5% full employment levels."

Year-ends for Interest Rates				
Percent %	2018	2019	2020	2021
Eurodollar futures	2.735	3.085	3.065	3.04
Fed's Sept forecast	2.5	3.25	3.5	3.5

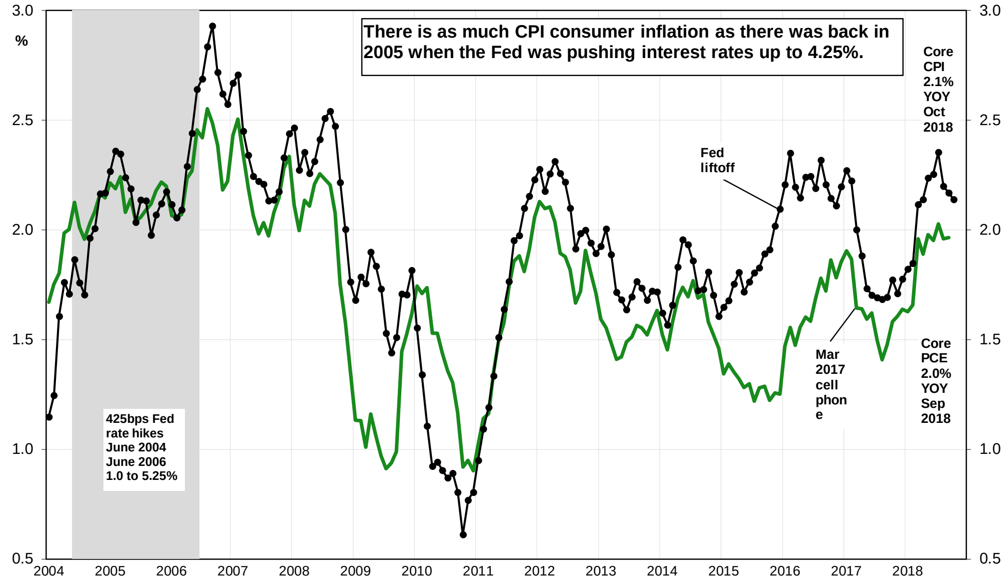
Eurodollar futures price where 3-month Libor will be in the future.
Friday, November 16, 2018 3-month Libor 2.64%

That was Wednesday, and on Thursday the Fed put out a strange press release, like why now, saying the Fed will review strategies, tools, and communication practices it uses to pursue its mandate of maximum employment and price stability. Maybe it's appropriate now with the unemployment rate at 3.7%, at the goal line where what to do next policywise in unclear, but this sounds like they might be thinking of dropping the interest rate forecasts. It said, "The review will include an outreach to a broad range of interested stakeholders," the word "stakeholders" tells us a businessman/corporate boards person has taken over as the head of the Federal Reserve under President Trump. Economists don't have stakeholders. The only tool the Federal Reserve has that works it to raise interest rates or lower interest rates in order to slow the interest rate sensitive areas of the economy and curtail business investment spending or to increase things like housing and car purchases. Not sure what communication needs to be changed. Policy options are limited. Move rates up or down. It's that simple.

OTHER ECONOMIC NEWS THIS WEEK

2.5% inflation today, but what about tomorrow? (Wednesday)

Breaking economy news. CPI inflation for October. Headline inflation up 0.3% to 2.5% year-year where it was 2.3% year-year in September. With crude oil prices collapsing, gasoline prices will have a negative impact next month however. If inflation isn't running away, then yields in the bond market are certainly not going to run away on the upside either.



The interesting thing is how the Fed has come to view 2.5% CPI inflation as benign, meaning there is no reason for a hurry-up monetary policy that pushes up interest rates at a faster pace. Not even with Greenspan in an interview overnight saying he sees the first signs of inflation out there. He raised rates to 6.5% in 2000 with a similar CPI inflation trend to that we are seeing today. He raised rates to 4.5% in January 2006 before handing over the reins to Bernanke who bungled the whole thing, steering the economy and all that, by raising rates three more times to 5.25% which broke the bank or at least started the economy on its way to recession.

Were there any underlying inflation pressures? Core CPI inflation less food and energy, rose 0.2% today for the month of October to 2.1% year-year versus 2.2% year-year in September. Medical care costs just aren't adding to inflation like in years gone past. Medical care commodities dropped 0.1% in October rising just 0.7% year-year. Medical care services are up just 1.9% the last year. The only inflation we see and see it personally is motor vehicle insurance on a tear up 6.7% the last year. Core inflation may have gotten a boost this month from used car and trucks rising back 2.6% after falling 3.0% last month (up 0.4% year-year). But hotels/motels were down 2.1% which is hard to believe based on our recent lodging stays.

Net, net, the economy is fast enough to put Americans to work, but not fast enough to engender inflationary pressures that might prompt the Federal Reserve to overreact and take the punch bowl away. It is prudent for Fed officials to continue on their path of gradual rate hikes, mopping up the liquidity provided during the recession and financial crisis, but the jury is out on whether it is necessary to tighten up policy to the point where higher interest rate costs start to slow business investment and overall economic growth.

Certainly, the current occupant of the White House is likely to strenuously object, underline the word strenuously, if Fed officials raise interest rates too many more times. (You're fired!) The Fed has raised rates every quarter but one in the eight quarters since Trump was elected in November 2016. They say future rate hikes are data dependent, but let's see if they can handle the heat. Stay tuned.

Consumers start the fourth quarter out with a bang; import prices rise too (Thursday)

Breaking economy news. Retail sales jump 0.8% in October, a rebound following slight declines of 0.1% each in August/September. August/September retail sales were revised down 0.3%.

Retail sales were slow in August and September, but that didn't hurt the real consumption expenditures in the third quarter's 3.5% real GDP data. Real consumer spending was big at 4.0% in the third quarter. It looks like consumers are still out shopping with their tax cut dollars and this bodes well for holiday spending this year which could be the best for retailers in over a decade. This longest economic expansion since the 90s isn't washed up yet if the consumer has anything to say about it. With October data in hand today, retail sales are running 2.9% already in the third quarter with November/December left to go which almost matches the 4.5% retail sales in the third quarter.

Retail spending, actual dollars, each month

	$million	% to	Percent Changes %		
	Oct 2018	Total	Oct	Sep	Year/year
Total Retail Sales	511,488	100.0	0.8	-0.1	4.6
Motor vehicles/parts	103,050	20.1	1.1	-0.1	-0.3
Furniture/furnishings	10,166	2.0	-0.3	0.5	1.2
Electronics/appliances	8,267	1.6	0.7	-1.5	1.6
Building materials/garden	33,230	6.5	1.0	0.1	3.6
Food & beverage	62,489	12.2	0.3	0.4	3.0
Health/personal care	29,023	5.7	0.0	-0.1	1.8
Gasoline stations	45,562	8.9	3.5	-0.4	16.2
Clothing/accessories	23,062	4.5	0.5	0.8	4.7
Sporting goods, books	6,487	1.3	0.5	-1.3	-8.5
General merchandise	60,382	11.8	0.5	0.0	3.5
Department stores	12,492	2.4	1.3	-1.0	-0.3
Miscellaneous retailers	10,829	2.1	0.6	-0.5	2.4
Eating & drinking places	60,427	11.8	-0.2	-1.5	6.2
Nonstore retailers (internet)	58,514	11.4	0.4	1.3	12.1

In other economic news, import prices have turned around, although with the dollar's rally, one wonders for how long. Nonfuel import prices picked up 0.2% in October, the first increase since May this year. Higher import prices lead to more inflation pressure generally, although in the last year, nonfuel import prices were up a modest 0.7%. If the Fed is concerned about inflation, and they are not, it is not going to be on account of higher imported goods prices.

Net, net, the economy is firing on all cylinders with the consumer in the driver's seat in the final quarter of the year. Retail sales could be the strongest in years this holiday season with consumers armed with the money Washington gave them with the Tax Cuts and Jobs Act signed December a year ago. It remains a question whether growth at this faster pace will be sustainable, but for today, there is no concern about the short-term outlook.

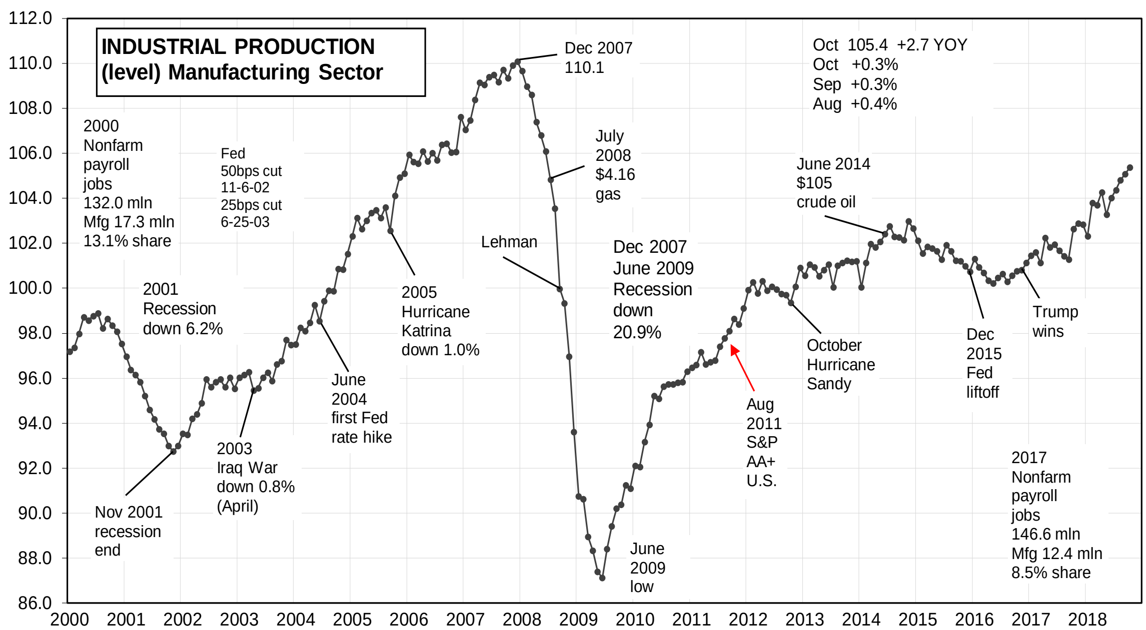
The trade war tensions have not hurt consumer confidence and have not led them to cut back their purchases at the shops and malls across America. Make America Great Again? The consumer is making the economy great again that's for sure. Stay tuned. Story developing. The consumer has the wind at their backs and with gasoline prices falling at the pump, we expect even more spending in the next couple of months. For the economy, it is as good as it gets right now. Fed Chair Powell says he is happy and for good reason. Let's hope for his sake his boss stays happy as well because consumer spending is solid which tees up a fourth rate hike this year for the Fed when they meet in December.

Factories not streaming back, but existing plants rev up their output (Friday)

Breaking economy news. Factories may not be streaming back to the USA, but existing plants are revving up their output. Economists may have to sharpen their pencils on those dismal forecasts looking for a slowdown in 2019 when the Tax Cuts and Jobs Act stimulus wanes because this economy has a good head of steam and shows no sign of stopping. Overall the industrial production trend is even stronger with the upward revisions in mining output. Total industrial production was just 0.1% in October, but it's up 4.1% the last year. Manufacturing production is humming with a 0.3% rise in October and rising 2.7% the last year. Stronger gains were recorded for mining production up 13.1% the last year.

Net, net, the renaissance in American manufacturing continues with factory output that is the envy of the world. America First hasn't brought that many factories back to the U.S. yet, manufacturing plant construction running about the same pace this year as last year or the year before that. But factory output is strong since the third quarter and is barreling into the fourth quarter which sets up a nice finish for the year. Manufacturing output rose 0.3% in July, 0.4% in August, 0.3% in September and 0.3% again in October. Manufacturing production is running 2.4% in the fourth quarter already with November and December reports yet to come. Even the President thinks we need to fix the immigration laws because we need more workers to man the shop factory floors. The manufacturing sector is better than you think. Bet on it.

Percent changes			Industrial Production October 2018		
Aug	Sep	Oct	YOY		Weight
0.8	0.2	0.1	4.1	Total Index	100.0
0.4	0.3	0.3	2.7	Manufacturing	75.5
2.4	-0.1	-0.3	13.1	Mining	14.1
1.1	-0.1	-0.5	1.7	Utilities	10.4
			Manufacturing payroll jobs 12.7 million +296K YOY 10.0% of Private Payroll Jobs		



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