Good morning,

What's in this week's Report:

- Last Week's Takeaway: AI Enthusiasm Could Soon Be the Only Thing Holding Up This Market
- Weekly Economic Cheat Sheet – Fed Surveys in Focus

Stock futures are solidly higher this morning, recovering a good portion of Friday's losses amid easing trade war fears.

President Trump dialed back Friday's tariff threats on China with a post on Truth Social saying "Don't worry about China, it will all be fine," which is fueling a relief rally today.

Economically, Chinese trade data was strong with exports jumping from 4.4% to 8.3% vs. (E) 6.5% in September.

There are no economic reports in the U.S. today and just one Fed speaker: Paulson (12:55 p.m. ET).

There is one noteworthy "bellwether" earnings release today: FAST ($0.30); however, with bond markets closed in observation of Columbus Day, it is likely to be a quiet day of volatility consolidation.

Market	Level	Change	% Change
S&P 500 Futures	6,664.00	68.75	1.04%
U.S. Dollar (DXY)	99.21	0.23	0.23%
Gold	4,093.40	93.00	2.32%
WTI	59.64	0.74	1.26%
10 Year	4.064%	0.009	0.22%

Stocks

Last Week (Needed Context as We Start a New Week)

Stocks spent most of last week churning toward new record highs as investors continued to dismiss the government shutdown and remained optimistic about AI investment deals and dovish Fed policy. The S&P 500 plunged 2.71% on Friday amid new trade-war tensions, leaving the index with a weekly loss of 2.41%.

The market rallied modestly on Monday, with U.S. stocks catching a bid and Japanese shares surging by 5%+ on the back of a surprise election outcome that bolstered bets for monetary and fiscal accommodation. Another AI deal, this one between AMD and OpenAI, saw the former's stock surge ~40%, keeping a bid in the broader markets. The S&P 500 rallied 0.36% to notch a new all-time closing high.

Stocks pulled back modestly on Tuesday, partially thanks to a slight uptick in the NY Fed's 1-Year ahead consumer inflation expectations (up to 3.4% from 3.2%), as well as the first negative AI headline in recent memory, specifically that ORCL reportedly lost $100MM on NVDA Blackwell chip rentals. The S&P 500 held support at 6,700 but ended the day down 0.38%.

The rally resumed on Wednesday thanks to a dovish, larger-than-expected 50-bps rate cut from the Bank of New Zealand, which rekindled domestic dovish optimism for Fed rate cuts before year-end. NVDA's CEO reiterated robust demand for the company's high-tech AI chips, which added a fresh tailwind to mega-cap tech stocks, and the S&P 500 added another 0.58% to close above 6,750 for the first time.

Equities pulled back from fresh record highs on Thursday amid political uncertainty in both Japan and Europe, as the Gaza ceasefire deal was overshadowed. A positive MSFT headline on a "data center crunch" set to persist into 2026 highlighted strong cloud and AI demand, which sent the S&P to new lows but left it down 0.28%.

Stocks opened quietly on Friday as the preliminary October Consumer Sentiment release was mixed, as the headline came in at 55.0 vs. (E) 54.0, but 1-Year ahead inflation expectations edged up to 4.6% vs. (E) 4.5%. Volatility spiked at 11 a.m. when President Trump announced that the Chinese tariff rate increase was being calculated due to the Chinese government's "sinister" moves with rare earth metals, and as many major economies expressed anger over recent trade hostilities, which Trump noted "came out of nowhere." Heavy selling persisted the remainder of the session, with the S&P 500 ending down 2.71% and at a one-month low.

Last Week's Takeaway: AI Enthusiasm Could Soon Be the Only Thing Holding Up This Market

Stocks dropped last week as investors were reminded that trade is still a potential source of volatility. But while the U.S./China trade escalation is notable, the biggest takeaway from last week's price action is clear: This market is becoming increasingly reliant on AI Enthusiasm to maintain gains and move higher.

The U.S./China trade escalation headlines are a reminder that trade remains unsettled, and even though markets have ignored it for months, it's still a potential drag on growth. Regarding the U.S./China escalation, President Trump's announcement on Nov. 1 of a 100% tariff on additional imports means that, in all likelihood, negotiations will de-escalate and the uneasy truce between the U.S. and China will continue. But Friday's headline is a stern reminder that the U.S. economy is still dealing with massive tariff uncertainty (which will only likely get worse after the Supreme Court decision). In contrast, tariff impacts on prices continue to move through the economy. Point being, this is not the type of environment conducive to 20-plus new highs in a year for the S&P 500.

Turning to growth, the labor market is cooling, and the government shutdown will be a temporary headwind. So far, markets have ignored these numbers and the shutdown, but it's entirely possible that once data resumes, it's weaker than expected. At that point, the benefit of more Fed rate cuts may be reduced for stocks, as the Fed could be viewed as "chasing" a slowing economy. Point being, that's not the type of environment usually conducive to 20-plus new highs in a year for the S&P 500.

The reason the S&P 500 has hit so many new highs is AI Enthusiasm. And while that's been true throughout the year, it's especially true over the past six weeks. In fact, AI Enthusiasm is now primarily focused on one company's tectonic spending plans: OpenAI. Over the past month-plus, agreements between OpenAI and 1) Nvidia, 2) ORCL, and 3) AMD have propelled the tech sector and S&P 500 higher. That's turbo-charged already lofty expectations for AI-related cap-ex that has boosted this entire market.

Here's the point: The market environment is not as good as the regular new highs in the S&P 500 imply, and AI Enthusiasm and the AI cap-ex cycle are becoming a larger and larger reason the market can ignore tariff chaos, cooling labor markets, and the government's shutdown.

As long as the AI cap-ex enthusiasm lasts, stocks can hold on. But AI is becoming an increasingly important lynchpin holding up the markets. Suppose doubts emerge about AI's stimulative power across the entire economy and market. In that case, investors will have to face this less-than-ideal reality, and the declines could be sharp and painful.

I'm not saying that's going to happen. Still, I do want us to be aware of that reality, so we understand this market setup (and change any exposure appropriately, depending on risk tolerance).

Economic Data (What You Need to Know in Plain English)

Last Week

Economic data was sparse last week due to the ongoing government shutdown, but the events we did get (FOMC minutes and Consumer Sentiment) were largely dovish, which boosted expectations for two more rate cuts in 2025.

Starting with the FOMC minutes, they revealed that the committee is clearly in favor of cutting rates; it's just a question of how many cuts. Specifically, most FOMC members acknowledged that the weakening labor market is now a bigger concern than elevated inflation. That's Fed-speak for "we're going to be cutting rates."

Regarding whether there's one more cut this year or two, the FOMC minutes underscored that the Fed is conflicted on the issue, though they were issued before the soft ADP jobs report. The truth is, most investors believe that if the Fed were surveyed today, its members would be more dovish than in September (mainly because of the generally dovish commentary by Fed members since the September meeting). Bottom line: expectations for the Fed to cut rates twice more were further solidified last week by the minutes, which helped support stocks. Yet for Fed rate-cut expectations to push stocks higher, we'll need to see expectations for 75 bps of cuts before year-end rise (right now, they are deficient).

Turning to actual economic data, the only notable report was Friday's University of Michigan Consumer Sentiment survey. Not only did consumer sentiment beat expectations (55.0 vs. (E) 54.0), but inflation expectations were tame, which further underscored expectations for two more cuts this year. One-year inflation expectations remained tame at 2.7% y/y, while five-year inflation expectations declined to 3.0% from 3.2%. So, while there was no growth data last week, the FOMC minutes and Consumer Sentiment further solidified expectations for two more rate cuts between now and year-end, which helped support stocks last week.

Important Economic Data This Week

The government shutdown will delay the essential data scheduled for this week, but we will still get at least some updates on the state of the economy. Markets will want to see continued Goldilocks data to reinforce expectations for a stable economy and two more rate cuts this year.

Starting with the data we won't see this week, we will not get 1) CPI and PPI, and 2) Retail Sales. Those are some of the more important monthly economic reports, and until the government reopens, investors (and the Fed) will have to navigate without them.

Turning to the data we will get this week, we get the first look at October economic activity via the Empire Manufacturing Survey (Wed) and the Philly Fed (Thurs). Those are regional metrics and volatile, so they have to be taken with a grain of salt, but they are a few of the economic reports we're getting right now, so they are more important than usual. For both metrics, solid readings (not deep negative drops) with stable price indicators are the best outcomes for stocks and bonds.

The other notable economic report this week is the Fed's Beige Book, released on Wednesday. The Beige Book isn't typically closely followed, but given the lack of other data, it will be more in focus this week. The Beige Book is a compilation of anecdotal insights on the economy from various Fed districts, and this week's Beige Book highlights stability. Suppose the Beige Book signals slowing activity or more labor-market concerns. In that case, that should slightly boost rate-cut expectations (again, the next step would be 75 bps of cuts before year-end, and any increase in those expectations will be short-term dovish and positive for stocks).

Bottom line, the lack of important economic data makes lesser-followed reports more vital, as they are the only insight we have into growth at the moment. Throughout the week, the key for this market remains that economic data show stable growth (no sudden drops in activity) and stable prices (which will keep rate-cut expectations intact).

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