

Good morning,

What's in this week's Report:

- Year-End Rally or Not? Three Events to Watch
- Weekly Market Preview: Can the Rebound Continue?
- Weekly Economic Cheat Sheet: Two of the "Big Three" Monthly Economic Reports This Week
- Is Japan Having a "Liz Truss" Moment?

Futures are moderately lower following a sharp drop in cryptocurrencies, hawkish Bank of Japan commentary, and underwhelming Chinese economic data.

Bitcoin fell 5% amid increased pressure on the crypto space, though there was no specific reason for the decline.

BOJ Governor Ueda told markets the BOJ would strongly consider a rate hike at its next meeting, pressuring stocks.

Economically, the Chinese non-manufacturing PMI fell to 49.5 vs. (E) 50.1, the lowest reading in three years.

Today's focus will be on the November ISM Manufacturing PMI (E: 49.0), and the key here is stability, specifically that we do not see the PMI "fall away" from 50 and badly miss expectations (if it does, it could be signaling sudden deterioration in the manufacturing sector, which would be a negative economic surprise).

Market	Level	Change	% Change
S&P 500 Futures	6,815.75	-43.75	-0.64%
U.S. Dollar (DXY)	99.10	-0.36	-0.36%
Gold	4,293.20	38.30	0.90%
WTI	59.09	0.54	0.92%
10 Year	4.061%	0.041	1.02%

Stocks

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

Stocks extended a robust relief rally off the multi-month lows from mid-November, with beaten-down tech shares and small caps leading the way on the back of increasingly dovish money flows and Goldilocks economic data that bolstered soft-landing hopes. The S&P 500 jumped 3.74% on the week.

The week began with a big rally last Monday, as most of the prior week's losses were recouped, with multiple Fed speakers echoing Williams's more dovish tone the previous Friday. Easing geopolitical tensions in Eastern Europe, along with thin volumes amid fading attendance at trading desks ahead of Thanksgiving, sent the S&P 500 higher by 1.55%.

The holiday-week rally seemed to remain on autopilot Tuesday as a steady grind higher persisted with effectively no interruption, as what began as a dip-buying opportunity, quickly morphed into a chase higher with a squeeze feel to it as two September data points, PPI and Retail Sales, came in cool and soft, respectively, adding renewed conviction behind bets for a December Fed rate cut. Hints that White House Advisor Kevin Hassett was a frontrunner for the next Fed chair added to dovish optimism and risk-on flows. Tech stocks notably outperformed as Mag 7 members META and GOOGL announced an AI chip deal (although that weighed on NVDA). The S&P 500 added another 0.91%.

The broad equity market advance continued on Wednesday, albeit at a slightly moderating pace, as market-based odds of a December Fed rate cut held above 80% amid more Goldilocks economic data, including solid initial claims, a cautiously elevated continuing claims number, and better-than-feared (delayed) September Durable Goods report. Strong guidance from DELL offset a weaker outlook from HPQ, adding a net tailwind behind tech shares. The S&P 500 had made most of the day's gains by late morning, and the index turned sideways into the close with a solid gain of 0.69%.

Stocks opened Friday little changed, as only a portion of traders returned to their desks after Thanksgiving, but those who did faced a technical issue with the cooling process at a major CME data center. Operations were quickly restored before the Wall Street open, and the S&P 500 extended gains amid a further moderation in pace amid quiet newswires to end the shortened session with a 0.54% gain, capping off the market's best week in five months.

Bottom Line

The S&P 500 bounced back last week and has recouped most of the November pullback and is poised to stage a year-end rally, if a few remaining catalysts don't provide any negative surprises. And since the holiday period is one filled with additional distractions and commitments, I wanted to provide a list of potential events that will likely decide if we get a Santa Claus rally into year-end (and new highs) or more volatility.

Key Remaining Event 1: FOMC Decision (Wednesday, 12/10). Dovish commentary and data have been an important part of this recent market rebound, and that needs to be continued if the S&P 500 is going to hit new highs. It's more likely than not that the Fed cuts rates again at this meeting, but it's not a foregone conclusion, and the Fed could hold rates steady. The potentially bigger question is whether the Fed signals a pause in rate cuts in 2026 (which would be a negative). Markets will need dovish reinforcement at this meeting to fuel a year-end rally.

Key Remaining Event 2: ORCL Earnings (Monday, 12/8) Repairing AI Enthusiasm. Concerns about gargantuan capex and deteriorating financial ratios for major AI-linked tech firms are among the causes of recent AI skepticism, which was the main driver of the pullback in stocks earlier this month. In many ways, ORCL is now the poster child for these concerns, as the company commits hundreds of billions in capex to build out AI infrastructure, leading to real deterioration in its financial ratios (which has been reflected in a rise in ORCL CDS pricing). ORCL needs to reaffirm that it's confident all these investments will deliver positive ROI and that it's staying fiscally responsible, to address the growing concern that AI hyperscalers may be investing too heavily in the AI buildout and that the ROI of these investments will disappoint.

Key Remaining Event 3: November Jobs Report (Tuesday, 12/16). Markets have been flying somewhat blind since the government shutdown, as government data has been nonexistent, but that will change in a big way starting this week as we get a lot of updated data on growth and the labor market. However, the most important remaining economic report of the year is the November jobs report, which will be released two weeks from tomorrow. The November jobs report needs to show stable labor-market trends, because stocks at these levels very much assume solid economic growth. If growth becomes a concern in 2026, that would be a significant negative surprise.

Bottom line, the market has again proved resilient by rebounding from the November pullback, but a rally into year-end is not a foregone conclusion. The issues that caused the volatility earlier this month are not fully resolved. If these events turn out to be negative for the market, then we will likely see a rebound of November volatility into year-end.

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

Last Week

More data were released than one would typically expect during a holiday-shortened Thanksgiving week, as economic data played catch-up following the government shutdown. And the data last week was dovish on balance, as it showed slightly underwhelming consumer spending and lower-than-expected inflation.

The two important reports from last week were the Core PPI report and Retail Sales. Both of these reports were from September (so they are admittedly a bit dated), but they still matter as we try to get a more complete picture of the economy, and both slightly underwhelmed.

Starting with Retail Sales, the headline missed estimates (0.2% vs. (E) 0.4%). More importantly, so did the Control Group, which is retail sales less gas, autos, and building materials. The Control Group is our best measure of truly discretionary consumer spending, and it declined by -0.1% vs. (E) 0.3% in September. The sector, as anecdotally confirmed, saw macro weakness, with items such as non-store retailers (online shopping), furniture, sporting equipment, and clothes all seeing drops. While it's just one report, it does imply that consumer spending may be losing steam (if other metrics confirm that, it would be an economic negative beyond the short term).

Headline PPI met expectations, but the more important Core PPI rose less than expected, 0.1% vs. (E) 0.3% m/m and 2.6% vs. (E) 2.7% y/y. Again, this is a September reading, so it must be viewed with a grain of salt, but the bottom line is that wholesale prices continue not to spike as feared now that tariffs are in place.

The net result of these two reports was a slight increase in the chances of a December rate cut, which helped stocks rally. More broadly, the data does show a generally Goldilocks economic setup (which is positive for stocks because it implies stable growth and not accelerating inflation). Still, we do have to remember these are September reports (and we should be getting November reports this week, so the data is dated).

Important Economic Data This Week

This week brings a more comprehensive and updated look at the U.S. economy, and the key for these reports remains the same: Goldilocks data that shows solid growth but allows the Fed to cut rates in December is the best case for stocks and will help fuel a rebound towards new highs.

Because of the government shutdown, we will not get the November jobs report on Friday. Still, we will get the other two of the "Big Three" monthly economic reports, i.e., the ISM Manufacturing PMI (out later this morning) and the ISM Services PMI (out Wednesday). Notably, while much of the government economic data is still delayed and playing catch-up, the ISM PMIs are current, and this will be November data. As has been the case with both reports, the key is that both remain above 50. The manufacturing PMI has been below 50 for most of the time over multiple years, but the key is that it doesn't "fall away" from 50 and imply a sudden slowdown. Turning to the Services PMI, it's stayed comfortably above 50, and it'll need to stay there to avoid signaling the U.S. economy may be seeing some weakness. Remember, two to three consecutive months of sub-50 readings is a reliably negative signal for future economic growth, and that's something we want to avoid.

The other notable economic reports this week come from the labor market, despite the absence of a government jobs report. Instead, the JOLTS report (Tuesday), ADP Employment Report (Wed), and Challenger Layoff Survey (Thursday) will give us insight into the state of the labor market in November, and, generally speaking, the stronger these numbers are, the better. I say that because they've all been lackluster recently, so some stabilization (or even moderate improvement) will be welcomed by markets (it's doubtful these numbers will be so strong they make the Fed less dovish).

Bottom line, we continue to work through the backlog of economic data this week, and we will continue to receive a fuller picture of the economy. For markets to stabilize and rebound, we'll want to see Goldilocks data that signals solid growth rather than sharply rising inflation. Practically, that means reports that meet or slightly beat expectations.

Special Reports and Editorial

Is Japan Having a "Liz Truss" Moment?

Japanese assets (stocks and bonds) have been among the most volatile in global markets recently, as markets are becoming more concerned about the country's fiscal trajectory and the comparisons to the UK's Liz Truss budget debacle of 2022.

For reference, Liz Truss was the newly elected Prime Minister of the UK in the fall of 2022. She presented an aggressively pro-growth budget of tax cuts and government spending designed to boost economic growth. Still, the global bond market viewed it as quasi-fiscally irresponsible, and the yield on 10-year GILTs (UK government bonds) surged from 2.00% in the summer of 2022 to nearly 4.00% at the height of the crisis in the fall. The pound plunged to an all-time low vs. the dollar, and predictably, UK stocks dropped hard.

Truss resigned, and the budget plan was scrapped, but the episode was painful for the UK economy, and parallels are being drawn to Japan right now. Specifically, the new Japanese PM, Takaichi, is pushing an economic stimulus plan. But inflation in Japan is at multi-decade highs, and many expect it to head higher. Meanwhile, debt and deficit ratios in Japan are the worst of the major developed economies (Japan's debt-to-GDP ratio is over 200% vs. about 120% for the U.S.).

This aggressive stimulus for an economy that already has extreme fiscal ratios and rising inflation has caused a sharp drop in the yen and Japanese Government Bonds. The yen has declined about 7% vs. the dollar over the past two months, while the 10-year Japanese Government Bond yield has risen from 1.62% to 1.83% over the same period, which is a multi-decade high.

Here's why this matters. Japan is the third-largest economy in the world, Japanese government bonds are widely owned, and the yen is deeply involved in global asset prices via the yen carry trade. Intense, extended volatility in these markets and the economy will ripple throughout the global economy simply via liquidity (meaning losses in JGBs and the yen will trigger other moves). This isn't directly pushing U.S. stocks lower, but it is something to watch that can contribute to existing volatility. For this risk to recede, we want to see both the yen and JGBs stabilize amidst some moderation in Takaichi's stimulus plans.

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