Ropes Wealth Reviews What Surging Payrolls and Bond Yields Mean for You

In today's news, a blockbuster payrolls report was revealed, which has sent economists and market strategists back to the drawing board trying to discern the future course of events for the economy and markets. Nonfarm payrolls rose by 336,000 in September, and additional revisions to previous months meant the overall change in nonfarm payrolls was 455,000. The September jobs additions were roughly double the 170,000 expected and the strongest pace of job creation since January. Service oriented jobs led the way, with leisure and hospitality especially strong in September, but education and healthcare, trade and transport, retail, professional business services and even the government all reflected a brisk pace of hiring.

The unemployment rate remained at 3.8% in September, while the labor force participation rate also held steady at 62.8%, below the pre-pandemic figure of 63.3%. Average hourly earnings are up 4.2% year-over-year and are reflecting a tapering of increases since 2021 when wage gains were compounding more quickly.

There is no question the labor market continues to exemplify tight conditions which creates a challenging dynamic for the Fed and anxiety in the markets as a result. The stronger the labor market is, the more pressure exists for the Fed to keep raising rates and holding them up at these high levels.

Amid this sentiment of higher for longer, coupled with a renewed focus on a mounting debt burden and increasing costs to service the existing debt in a rising rate environment, longer-term yields continue to push higher. In fact, most Wall Street firms have now revised expectations for interest rates, calling for a 5% yield on the 10-year U.S. Treasury note by the end of December. We are in striking distance today, with the 10-year note yielding 4.78%.

What support will the economy have to lean on in this "new normal" of high interest rates? None from the government, as we saw demonstrated in this week's theater of the absurd. After much drama, Congress passed, and the President signed into law, a temporary 45-day funding agreement last Saturday at midnight to avert a government shutdown. It was an ugly negotiation, which ultimately cost Kevin McCarthy his position as Speaker of the House of Representatives and provides only very temporary relief from anxiety over Washington dysfunction.

In the past, investors typically welcomed divided government in Washington. Gridlock ensured that little would change. Taking Washington out of the equation meant that Wall Street could fully focus on the fundamentals—growth, inflation, interest rates, and earnings—that drive the lion's share of asset price returns and portfolio performance.

But today's form of gridlock is not quite so benign, for at least two reasons.

First, short-term spending authorizations must be periodically renewed (or eventually replaced by full year appropriations), meaning that concerns will soon return about a potential disruptive shutdown. Given the U.S. experience of government shutdowns since the 1990s (eight episodes in total), this past weekend's last-minute compromise offers little comfort that a shutdown later this year or in 2024 can be avoided.

Second, the emergence of large U.S. federal government deficits since the global financial crisis—and even more so since the global pandemic—requires, at some point, the ability to find durable solutions to reduce deficits and stabilize (never mind reduce!) the stock of government debt relative to gross domestic product. The events of this past week offer scant hope that addressing those long-term challenges is anywhere in sight.

The upshot is that investors have been given only a short-term reprieve from Washington's challenges. Over the next few weeks, their focus will return to questions about an economic soft-landing, the prospect for slowing inflation, the implications for Federal Reserve policy, and the start of the third-quarter earnings season. This compromise, minutes before midnight, has brought near-term relief but fears have only been delayed not put to rest.

The conclusion is that investors hoping for a prolonged period of Washington political stability, predictability and leadership are likely to be disappointed. The intra- and inter-party divisions to effective governing have been exposed by the wrangling of recent weeks as deeper than ever. For their part, the Fed's hands are tied, with the labor market out of balance and inflation still not where it needs to be, they may be forced to continue hiking rates until the economic data compels them to cease and desist. Where does that leave us? We need some good old-fashioned growth to see us out of this predicament. The question is—can we deliver? There are a lot of headwinds to be sure, but your team at Ropes Wealth Advisors believes there are great companies and funds of companies that can deliver, and your strategy is built around those investments, with a healthy dose of high yield short-term bonds as a ballast for cash needs and rainy days. The path forward is not "one sized fits all" because there is no easy support or stimulus to make it so. Instead, what you own, and the balance of those investments to your goals, will matter more than ever.

Thank you as always for your interest in our investment commentary. Please let your RWA team know if you have any questions or concerns. If you would like to speak personally with a member of our team at any time, please click **here**.

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