Week in review and ahead (vol.36-26)

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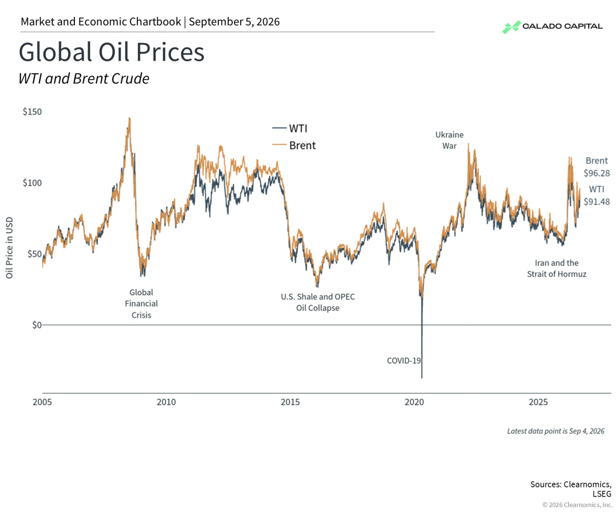
Week in review

Markets delivered mixed performance last week as investors continued to assess the implications of Federal Reserve (“Fed”) Chair Kevin Warsh's hawkish remarks at the Jackson Hole symposium the prior week. His comments reinforced expectations that policymakers remain primarily focused on inflation risks, keeping Treasury yields and the interest-rate outlook in focus for markets. At the same time, geopolitical tensions remained elevated as hostilities between the United States and Iran resumed, contributing to a rise in oil prices and rekindling concerns that inflationary pressures could prove more persistent than previously anticipated. Higher energy costs have become an increasingly important consideration for markets, particularly as fuel prices continue to place upward pressure on broader inflation measures.



Economic data released during the week generally pointed to a labor market that remains resilient. August nonfarm payrolls exceeded expectations, while labor-market indicators such as job openings suggested employment conditions remain relatively stable. The strength of the labor market reduces the urgency for the Fed to shift its focus toward supporting growth and instead allows policymakers to maintain emphasis on their inflation mandate. Investors increasingly recognize that, while inflation has moderated from its peak, progress toward the Fed's target may not materialize. Recent survey data, including the ISM’ Prices Paid component, have raised concerns that disinflation within the services sector could stall or even reverse, reinforcing expectations that monetary policy may remain restrictive for longer than previously anticipated.

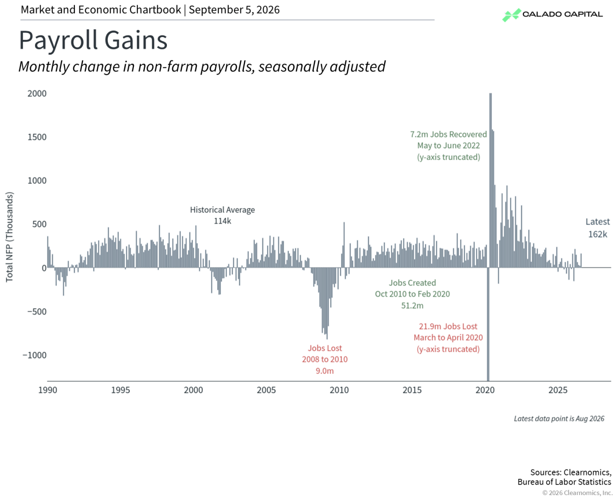
Against this backdrop, U.S. equities were largely unchanged for the week. With another strong corporate earnings season now largely complete, the market’s attention is likely to shift away from company-specific fundamentals and toward macroeconomic drivers, including Treasury yields, inflation trends, and the future path of Fed policy. The Dow Jones Industrial Average declined 0.3% during the week, while the S&P 500 and Russell 2000 each posted modest gains of 0.1%. The technology-oriented Nasdaq Composite outperformed, advancing 0.4% for the period.

International equity markets produced mixed results. In Asia, Japan's Nikkei 225 declined 2.1% as rising global bond yields, higher energy prices, and a broader risk-off tone weighed on investor sentiment. European equities also finished lower, with Germany's DAX falling approximately 2.0% and France's CAC 40 declining roughly 1.5%. The weakness across continental Europe reflected many of the same themes affecting global markets, namely higher oil prices, rising sovereign bond yields, and concerns that persistent inflation could delay any meaningful easing in monetary policy. Germany's export- and manufacturing-oriented market was particularly sensitive to higher energy costs and interest-rate expectations. Elsewhere, the United Kingdom and Hong Kong posted modest gains of 0.1% and 0.3%, respectively, while Chinese equities declined approximately 0.6% for the week.

Week in review – US macroeconomics

The week’s focus was squarely on the labor market, headlined by the August nonfarm payroll report, alongside the July JOLTS job openings, weekly jobless claims, and the ISM economic activity surveys, a data set that on balance depicted an economy still expanding at a firm pace even as price pressures lingered.

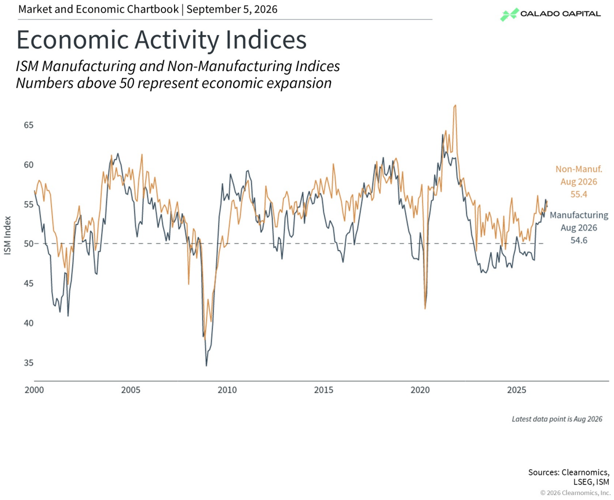
The August employment report came in notably stronger than expected, with the economy adding 162,000 jobs against the 55,000 anticipated, while the prior month was revised up (by nearly 45,000) to 21,000. The unemployment rate held steady at 4.1%, in line with expectations. Weekly initial jobless claims echoed the stability, holding at 206,000, roughly in line with the 205,000 expected. Claims have now trended below 238,000 since the week ended September 6, 2025, when they exceeded 250,000, and below 230,000 since mid-June, underscoring a labor market that, while cooler than a year ago, remains fundamentally sound. Separately, July JOLTS job openings came in at nearly 7.3 million, roughly in line with expectations and up from about 7.2 million previously.



The activity surveys, meanwhile, pointed to continued expansion. The ISM Manufacturing PMI eased to 54.6 in August, modestly below the 55.2 expected and down from 55.6, yet still marking an eighth consecutive month of expansion for the sector. All five subindexes, new orders, production, employment, supplier deliveries, and inventories, remained in expansionary territory, albeit at a slower pace, with the exception of supplier deliveries, which accelerated by 0.4 point. Prices paid were unchanged from July but stayed elevated, keeping inflation concerns firmly in view.

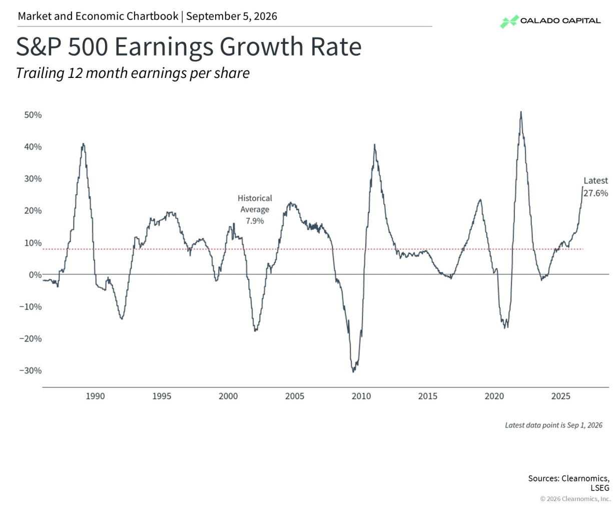
The services side was firmer still. The ISM Services PMI rose to 55.4 in August, ahead of the 54.3 expected and the prior 54.1, and comfortably above its 12-month moving average of 53.7, a reading ISM notes is consistent with roughly a 2.3 percentage-point increase in annualized GDP. Business activity, new orders, and inventories all expanded at a faster pace, with supplier deliveries (-1.5) the lone exception, while employment remained in contraction at 47.8 but improved as the pace of decline eased. The more troubling detail was prices paid, which accelerated again in August after earlier hopes that disinflation was taking hold in the service sector, a category that accounts for 77-80% of US GDP.

Taken together, the reports depict continued robust economic activity, however, with renewed concern over elevated prices (paid), particularly in the dominant service sector, a combination that has lifted market participants' odds of at least a one-rate hike before year-end. With the labor market stable, the Fed can afford to focus squarely on its inflation mandate, and markets will certainly anticipate that it does so at some point, with the next FOMC meeting scheduled for later in September.



Corporate earnings

With the second-quarter reporting season now essentially complete, the results proved exceptionally strong on a broad basis. Per FactSet, roughly 86% of S&P 500 companies topped earnings estimates, the highest aggregate earnings-surprise rate since FactSet began tracking the metric in 2008. The strength was widespread, with ten of the eleven sectors posting year-over-year earnings growth. Energy, Communication Services, and Consumer Discretionary led the gains, alongside a powerful contribution from Information Technology, where the ongoing AI buildout continued to lift semiconductor and related hardware names, while Health Care was the lone sector to register a decline.



Week ahead

The holiday-shortened week ahead, with US markets closed Monday in observance of the Labor Day holiday, will center on inflation, as the August CPI and PPI reports take the spotlight. Coming on the heels of the re-acceleration in prices paid within the ISM services survey, these releases should offer a strong signal for the Fed's next move. The markets broadly expect further disinflation, with core CPI forecast at 2.4% year-over-year, a 0.1 percentage-point improvement from the prior month, while headline CPI is seen holding steady at 3.4%. On the wholesale side, core PPI is expected to remain unchanged, though headline PPI, much like its retail counterpart, is anticipated to accelerate anew.

Beyond the all-important inflation reports, markets will receive the preliminary University of Michigan consumer sentiment reading for September, offering an early gauge of household confidence, along with August existing home sales, which are expected to show barely any improvement as the housing market continues to labor under stretched affordability and elevated mortgage rates.

Number of the week: $5.85

The nationwide average price for a gallon of diesel last week, a new all-time high that eclipsed the prior record of $5.81 set in June 2022 in the wake of Russia's invasion of Ukraine. The climb has been swift: diesel sold for roughly $3.76 a gallon before the Iran conflict flared in late February, meaning prices have surged more than $2, or over 50%, in barely six months. The spike reflects a confluence of supply shocks, including disrupted shipping through the Strait of Hormuz, Ukrainian strikes curtailing Russian refinery output, Asian refiners limiting exports, and US refiners favoring more profitable jet fuel over diesel.

Diesel's importance to the economy is difficult to overstate, as it powers the trucks, trains, and tractors that move nearly everything from raw materials to finished goods. Higher diesel costs ripple through freight rates and, ultimately, the shelf price of food and consumer products, with agriculture particularly exposed given that the bulk of farm equipment still runs on diesel. Arriving just as harvest season and winter heating demand approaches, the timing threatens to reignite the very goods and food inflation the Fed has been fighting, with headline (retail) inflation already running at 3.4% year-over-year. For the Fed leaning hawkish and a consumer already stretched, a fresh energy shock is an unwelcome complication, and one worth watching closely in the months ahead.

If you have questions about how this may impact your investments, or how you should be positioned, please do not hesitate to contact us at claudio@caladocapital.com.

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