# Monthly Market Commentary

The S&P 500 rallied by 11% during October, restoring some confidence after a sharp drop at the beginning of the month. On the international front, the Greek crisis continued to be the central concern both by itself and as an indicator of what could happen in other countries that face similar budget crises. The European Central Bank lowered its key interest rate to 1.25% from 1.5%, as mild signs of a recession begin to appear.

GDP: Overall U.S. GDP numbers for the third quarter were a lot better than most had expected in mid-September. The real GDP growth rate was neither as weak as the 0.4% and 1.3% of the first two quarters, nor as strong as the 2.5% of the third quarter. Morningstar economists estimate that the real inflation-adjusted growth in the economy appears to be around an anemic but steady 1.75%–2.25%.

Employment: Net employment growth was 80,000 in October, at the low end of the estimate range of 70,000-110,000. While still positive, this growth remains too low to make a significant impact on the unemployment rate, which only fell to 9.0% from 9.1%. What is surprising, though, is where these new jobs are coming from. Two sectors that tend to contribute heavily to job growth, government and construction, have failed to do so recently; the manufacturing and service sectors have been the real drivers. Almost 500,000 government jobs have been lost since the recovery began, but the pace of such losses now appears to be slowing. The construction industry, which normally represents a meaningful portion of job creation, remains weak, threatened by cheap foreclosures and lack of consumer confidence.

Net job growth for August was revised to 104,000 from 57,000, and to 158,000 from 103,000 for September. These significant revisions are a not-so-subtle reminder of the dangers of reading too much into any one monthly report. When looking at the larger picture, year-over-year private-sector employment growth (calculated using a three-month average) remained at a slow but steady 1.7%.

Manufacturing: At this point in the recovery, manufacturing growth usually has a tendency to slow down, and the services sector begins to take the lead. Before slowing down, however, manufacturing has done impressively well, mostly because of a strong export market for capital goods and a rebounding auto industry (auto sales in October jumped to an annualized rate of 13.2 million units). However, floods in Thailand (where many electronic parts are sourced) may slow Japanese auto production going forward. On the service-sector side, education and health care have done well, while information services jobs have declined and the finance industry has been flat.

Foreign exchange: Given the eurozone's many escalating problems, it is perhaps surprising that the USD/EUR exchange rate has stayed relatively flat, with the exception of a short dollar rally at the beginning of October. Going forward, a eurozone banking crisis remains an alarming possibility, in which case firm central-bank intervention might become a necessity.

Bull or bear: As the holidays and the end of the year approach, there are two possible stock-market scenarios. The market could continue to tumble as the European crisis/mild recession situation unfolds (the "bear" scenario). Or, stocks could rally as seasonal retail sales and consumer confidence increase in November and December (the "bull" scenario—no pun intended). It's too early to tell, but despite the October rally, many analysts have been exercising caution by cutting their fourth-quarter earnings estimates. Still, adding to current equity allocations may remain attractive to many investors despite persistent global risks.