TOMORROW'S NEWS TODAY

Friday, November 06, 2015

Market Snapshot*

DJIA	17910.33	+46.9
Nasdaq	5147.12	+19.38
S&P 500	2099.2	-0.72
10-Year	2.3318%	-23/32
30-Year	3.0867%	-1 13/32
Euro	$1.07445	-0.0131
Nymex Crude	$44.29	-0.91

Source: SIX Telekurs, ICAP plc *preliminary values subject to adjustments

Stocks

Investors geared up for the Federal Reserve to raise interest rates next month following a stronger-than-expected jobs report. Broad stock-market indexes rose only slightly, but underlying sectors swung sharply as investors moved money out of income-yielding companies that do well during periods of low interest rates and into banks, whose profits are expected to increase as rates rise.

Treasurys

Yields on short-term U.S. government debt rose to a five-year high Friday after a strong employment report solidified expectations of a possible interest-rate increase by the Federal Reserve in December. Investors lightened up on bonds, concerned that the value of their bondholdings would shrink by a shift in the Fed's ultraloose monetary policy. The yield on the benchmark 10-year Treasury note also rose to the highest level since July. Yields rise as bond prices fall.

Forex

The dollar surged against its peers Friday, after a report showed that the U.S. economy created more jobs than expected last month, paving the way for the Federal Reserve to raise interest rates in December. The Wall Street Journal Dollar Index, which gauges the buck against a basket of 16 currencies, was recently at 90.40, its highest level since December 2002, amid gains against the euro, yen and other currencies.

Commodities

Oil prices fell after stronger-than-expected gains in U.S. employment sent the dollar to new highs and raised expectations for interest-rate increases. December crude oil settled down 91 cents, or 2%, to $44.29 a barrel on the New York Mercantile Exchange. Brent, the global benchmark, lost 56 cents, or 1.2%, to $47.42 a barrel on ICE Futures Europe.

Tomorrow's Headlines

US Hiring Surges as Eyes Turn to Fed

U.S. employers hired at their strongest clip this year in October and wage growth picked up, signs of reassurance for Federal Reserve officials as they weigh an interest-rate raise before year's end.

Nonfarm payrolls rose a seasonally adjusted 271,000 in October, the Labor Department said Friday. Revisions showed employers added a combined 12,000 more jobs in September and August than previously estimated, bringing the three-month average through October to 187,000.

Average hourly earnings of private-sector workers rose last month by 9 cents to $25.20 from October, and are up 2.5% from a year earlier. That's a notable rise from the 2% average pace during the six-year expansion, suggesting that the economy is gaining traction and the steady pace of hiring is finally translating to long-awaited wage growth.

The unemployment rate, which is obtained from a separate survey of U.S. households, fell slightly to 5.0% in October, the lowest reading since April 2008 and down from 5.1% the prior month. It's also a notch closer to Fed officials' 4.9% median projection for its normal long-run level.

"From all sides, the October employment is very strong, painting a bright outlook for the economy," said AllianceBernstein economist Joseph Carson in an analyst note. "The Federal Open Market Committee has no more excuses of delaying a gradual normalization of official rates."

Obama Rejects Keystone Pipeline

The Obama administration rejected the Keystone XL pipeline Friday, capping a politically charged review of the oil project that lasted more than seven years and escalated into a broader debate on energy, climate change and the economy.

"The State Department has decided that the Keystone XL Pipeline would not serve the national interest of the U.S.," President Barack Obama said in brief remarks from the White House. "I agree with that decision."

Mr. Obama cited the urgency of climate change, and the need for American leadership on that problem, as key reasons for his decision.

Mr. Obama, who has made environmental issues a centerpiece of his second term, had signaled deep misgivings about the pipeline project as he pursued an expansive agenda aimed at fighting climate change.

continued on page 2

Monday's Calendar

10:00 a.m.	IMF Policy Paper on Structural Reforms and Macroeconomic Performance
10:00 a.m.	Oct Employment Trends Index ETI (previous 128.76), ETI, Y/Y% (previous +4.6%)
12:00 p.m.	FRB Boston President Eric Rosengren speech at Newport County Chamber of Commerce Economic Update Luncheon
N/A	Obama meets Netanyahu at the White House

Tomorrow's Headlines
continued

Valeant CEO Forced to Sell Company Stock in Margin Call

Valeant Pharmaceuticals International Inc. Chief Executive Michael Pearson was forced to sell a big chunk of his company stock Thursday after a lender called in a loan backed by the shares, in the latest twist for the company's battered stock and embattled leader.

Goldman Sachs Group Inc. called in a $100 million loan to Mr. Pearson on Thursday and sold 1.3 million shares held in collateral to cancel out the balance, Valeant said Friday.

Mr. Pearson in a statement said that since joining Valeant, he hasn't sold any shares provided as compensation "and it was not my desire that shares be sold now."

The sale accounts for about 13% of Mr. Pearson's holdings in the company as of Dec. 31, when he owned 10.1 million shares, or about 3% of the company.

Lilly, Merck Get Inquiries Over Drug Pricing

Drug makers Eli Lilly & Co. and Merck & Co. have disclosed separate requests from the U.S. Justice Department for information related to drug pricing—the latest sign of increased scrutiny of the industry's pricing practices.

The U.S. attorney's office in Philadelphia and the Justice Department's civil division are conducting an inquiry of Eli Lilly's "treatment of certain distribution service agreements with wholesalers" when calculating and reporting average manufacturer prices for the drug-rebate program for Medicaid, Lilly said in a quarterly report filed with the Securities and Exchange Commission last week.

Renault Says France, Nissan to Try to Settle Dispute Over Alliance

Car maker Renault SA said France's government, which recently increased its stake in the company, is in the "first stage" of discussions with Nissan Motor Co. to resolve a boardroom dispute and rebalance the partnership between the two car makers.

Renault said its board of directors, which met Friday afternoon, initiated the talks.

"The board of directors has decided to take the necessary steps to facilitate the finding and the formal expression of a solution that would preserve Renault's corporate interest and strengthen the alliance" between the companies, Renault said late Friday.

Square's IPO Terms Put Value Below Latest Funding Round

Square Inc. could soon be a case study on what happens to tech startups that can't support their lofty private-market valuations in the public market.

The payments startup said Friday it plans to sell 27 million shares in an initial public offering at $11 to $13 each, substantially lower than the $15.46 the shares fetched from private investors in Square's last funding round in October 2014.

That round valued the company at $6 billion. At the $12 midpoint of Friday's indicated price range, Square would be valued at $3.9 billion, excluding the value of stock options, restricted stock and warrants.

Supreme Court To Review Contraception Compromise

The Supreme Court on Friday accepted challenges to an Obama administration compromise for providing birth-control coverage to workers at Christian-affiliated institutions, agreeing to decide whether it is at odds with a federal law on religious freedom.

As part of the Affordable Care Act, most employers have to include birth-control coverage in their health insurance plans, with no out-of-pocket costs for employees. The law fully exempted institutions like churches, but not religiously affiliated nonprofit employers such as Catholic universities or hospitals.

The high court ruled in June 2014 that the Obama administration had gone too far in also applying the requirement to the owners of for-profit companies, such as arts-and-crafts chain Hobby Lobby, which believe certain kinds of contraception to be immoral. But the court didn't say what, if anything, federal officials could do to extend birth control coverage to employees.

UAW-Ford Reach Tentative Labor Agreement

Ford Motor Co. has wrapped up its contract talks with the United Auto Workers union, agreeing to a tentative labor agreement largely patterned after a General Motors Co. deal that has yet to be ratified by the rank-and-file.

The Ford proposal, which covers 52,900 U.S. factory workers at the no. 2 U.S. car makers, is one of the richest in the company's history, securing significant economic gains and better job security, the UAW said Friday without releasing specific details.

Union officials from dozens of Ford factories and facilities across the country are scheduled to be briefed on the deal Monday in Detroit.

OPEC Members at Odds Over Group's Long-Term Goals

The Organization of the Petroleum Exporting Countries has delayed completing its internal report on long-term strategy as tensions deepen among members over an extended oil-price slump, according to delegates to the group.

The disagreements could set for the stage for a tense OPEC meeting next month, when oil ministers from the group's 12 members will gather in Vienna to decide on production levels.

continued on page 3

Alibaba to Buy Online Video Firm Valued at $4.4B

Alibaba Group Holding Ltd. said Friday it would buy U.S.-traded Chinese online video provider Youku Tudou Inc. in an all-cash deal, giving it a means to secure a share of China's fast-growing online video market.

The deal values Youku Tudou, in which Alibaba already owns about a one-fifth stake, at about $4.4 billion.

Alibaba's rivals have ramped up spending on new movies, TV shows and original programming to win over a massive new audience. Alibaba had approached the company with a buyout offer in October.

Alibaba will pay $27.60 an American depositary share, a 35.1% premium over the closing price of Youku Tudou's stock on Oct. 15, the day before Youku Tudou announced it had received the buyout proposal from Alibaba, and a 13% premium to Youku Todou's trading price on Thursday. The company in October had offered $26.60 per share.

Youku Tudou's board of directors unanimously approved the agreement.

Brazilian Authorities Race to Save Victims in Mine Dam Collapse

Brazilian authorities raced Friday to save victims and tally the damage of what may be the country's worst-ever dam breach after structures owned by two of the world's biggest mining companies suddenly failed.

Hundreds of refugees huddled in a gymnasium in the city of Mariana, Minas Gerais state, after a rural community 30 kilometers to the north was virtually wiped out Thursday afternoon by a wall of red mud unleashed by two broken dams. Authorities confirmed two deaths and at least 13 missing. Roughly 500 people were evacuated from the village of Bento Rodrigues, home to between 1,000 and 2,000.

"As far I can remember, it's the worst," said Ricardo Aguiar Magalhaes, a spokesman for the Brazilian Committee on Dams, an association of engineers and technicians, of the breach.

The devastating flood came after the collapse of a pair of so-called tailings dams, which are used to hold water and discarded minerals from a nearby iron-ore mine. The mine belongs to Samarco Minerac, a joint-venture between Brazil's Vale SA and Australia's BHP Billiton Ltd.

Wells Fargo To Issue $40B In Debt

Wells Fargo & Co. Financial Chief John Shrewsberry said the San Francisco bank would need to raise at least $40 billion in new debt, with the executive saying Friday his firm and others are "victims" of upcoming regulatory requirements.

Mr. Shrewsberry said at an investor conference the bank would need to issue about $40 billion of net new long-term debt to reach the "total loss-absorbing capacity," or TLAC, regulatory requirement. He said if the bank has an additional "prudent" TLAC buffer it would need to issue another $20 billion of debt, for a possible $60 billion in new debt related to TLAC.

Bullard: Market-Based Measures Indicate Rate Rise

Federal Reserve Bank of St. Louis President James Bullard said Friday he believes the U.S. economy is ready for a boost in borrowing costs.

"I think the case continues to be compelling for liftoff," Mr. Bullard told reporters after a speech here. He said he would like to see rates pushed off current near-zero levels due to "cumulative" progress in the job market and the strong prospect weak inflation will begin to rise back to the Fed's 2% target over 2016.

"The U.S. economy by itself looks good," with a solid consumer sector, Mr. Bullard said before financial professionals. Mr. Bullard told the group there was unanimous support among policy makers for a gradual pace of rate rises once the process starts, adding that once the first move is made, there will be a "healthy debate" over what will follow.

Mr. Bullard, who isn't currently a voting member of the Federal Open Market Committee, said "market-based probabilities" of the Fed raising rates off near zero "have increased." He also said the Fed's policy statement at its October meeting, which acknowledged the possibility of a rate rise in December, helped clarify the market's thinking about the monetary-policy outlook.

Fed's Evans Sees Jobs Report as a 'Good Number'

Federal Reserve Bank of Chicago President Charles Evans said Friday's October jobs report is a "good number" although he would like to see stronger wage growth to help push inflation higher.

His remarks aired shortly after the Labor Department said nonfarm payrolls rose a seasonally adjusted 271,000 in October, the strongest pace of hiring this year.

Mr. Evans called the report "good news" which "seems to support my outlook for 2016 pretty well" in an interview with CNBC, although he said uncertainty remains over whether inflation will get back to the Fed's 2% objective "within a reasonable period of time."

Mr. Evans, a voting member of the rate-setting Federal Open Market Committee this year, has previously spoken in favor of a slow and modest course of central bank interest-rate rises, beginning in 2016.

He has argued that while the Fed has been making progress getting the job market back on track, it hasn't fared nearly as well when it comes to getting price pressures back to the 2% level officially targeted by the central bank.

Talking Points

Ip: Still Waiting For Wage Inflation

The October jobs report was full of positive signs for the economy but by far the most important was the 0.4% jump in average hourly earnings, which brought the annual increase to 2.5%, the highest since 2009.

By broad measures, the labor market has gotten steadily tighter: The unemployment rate, at 5%, is down by half since 2010, and the vacancy rate is the highest since 2000. But until now, there has been precious little sign of broad upward pressure on wages. Many promising monthly jumps were followed by flattening later.

Is this one for real? There are reasons to believe it is. In the last year, many companies from Wal-Mart to McDonald's announced broad-based wage increases for their lowest-paid employees. It was always an open question whether they were responding to public criticism of their low wages, or because they genuinely were having trouble filling job openings. Since self-interest is a more durable influence on business behavior than altruism, the second explanation would be the more encouraging, as it means the wage boosts were more likely to persist even at the expense of narrower profit margins, and that other businesses would have to follow suit.

Digging into the October data, it's still unclear these employers are representative. Retail wages rose 0.2% after a 0.4% rise in September, keeping the annual increase at 3.2%. That's good, but not a marked acceleration. Leisure and hospitality wages rose 0.4% but that followed a flat September and the annual gain is just 2.5%, which is actually a significant slowing from earlier this year.

More broadly, the hourly wage data have been volatile enough that reading a lot into October's number is dangerous. Even if wages are on an upswing, there is nothing in the last few years to suggest a rapid acceleration is in the works.

Productivity gains remain quite sluggish, which is why labor costs, adjusted for productivity, are rising 2% per year. Thus, if hourly wages keep rising at 2.5%, either profit margins are going to be squeezed, productivity will have to rise, or they will be passed on to prices.

Of these three possibilities, the last seems least likely. Profit margins are quite wide and easily able to handle some rebound in labor expense, especially if accompanied by rising sales. Productivity is overdue for at least a modest cyclical uptick assuming economic growth doesn't falter. As for prices, the fact inflation has remained below the Fed's 2% target for so long speaks both to the lack of pricing power and the absence of the sort of inflationary psychology that would ease the way to higher prices.

So while the rise in wages should be welcomed by the Fed, it is not a sign that inflation pressures are about to build. Between the strong jobs report and a drumbeat of Fedtalk, the markets are coming around to the view that the Fed will start to raise rates in December. But there's no rush. A few more months of wage gains like October's would provide a more secure foundation on which to start normalizing rates.

When Individual Investors Move Markets

If you think individual investors can't move the stock market anymore, think again.

At the beginning of next month, a few tiny stocks may suddenly jump in price and trading volume. Behind the moves: the American Association of Individual Investors. This Chicago-based organization, founded in 1978, is the largest nonprofit devoted to teaching ordinary people how to invest. Its 171,000 members gather in some 50 chapters nationwide to learn about taxes, mutual funds, diversification and financial software — a social club for folks who get their kicks talking about stock picks.

Since 1993, AAII has tracked what it calls the Model Shadow Stock Portfolio. What happens to these two or three dozen stocks is fascinating — and holds lessons for all investors.

continued on page 5

Talking Points

continued

Three to five companies could be added to the portfolio around Dec. 1, says AAII's founder and chairman, James Cloonan. He launched the model (which has no outside clients and holds just $610,000) to capitalize on research published by academics in the early 1980s suggesting that cheap stocks too small for institutional investors to buy — but theoretically ideal for individuals to hold — have tended to outperform. In the 1970s, the great financial analyst Benjamin Graham had also urged individual investors to choose their holdings from among stocks institutions couldn't buy.

Since 1993, the Shadow Stocks have returned an average of 15.6% annually, versus 8.7% for the S&P 500, according to AAII. But not all its followers have matched that return — because most don't learn about the portfolio's latest trades until well after it makes them.

To be eligible, a company must be profitable, cheap and itsy-bitsy (with a total market value between $30 million and $300 million, such stocks lurk in the shadows of the multi-billion-dollar behemoths in the S&P 500).

Look at CDI Corp., a Philadelphia-based provider of staffing, engineering and technology services. Between June 4 and June 10, CDI's shares rose 3%. Then, on June 16, CDI surged 9.8% on trading of nearly 160,000 shares, triple its recent average volume.

"Of course we noticed it," says Vincent Webb, CDI's head of investor relations. "We were puzzled, because we hadn't issued any earnings release or disclosed any news around that timeframe."

Salem Media Group, a Camarillo, Calif.-based radio and publishing company, was deleted from the Russell 2000 Index, a leading measure of small stocks, at the end of June. That usually makes stocks drop, not rise.

Yet, between June 4 and June 15, Salem gained 15%. Then, on June 16, it climbed another 8.5%. There was no material news around that time, says Evan Masyr, head of investor relations.

On June 4, AAII's Shadow Stock portfolio bought $24,900 worth of CDI, a new holding, and added about $8,700 to the position it already held in Salem. After the close of trading on June 15, AAII updated the list of holdings on its website. That appears to have unleashed a buying frenzy by individual investors on June 16.

In nine trading days, the total market value of CDI had shot to $265 million from $243 million; Salem, to $153 million from $122 million. In conjunction with less than $34,000 in purchases in the AAII portfolio, the two companies gained about $55 million in market value.

Analyzing 169 stocks bought by the Shadow Stock portfolio, my colleague Tom McGinty found that trading volume in these stocks consistently peaked in the first four days after AAII disclosed they had been added.