WEEKLY ECONOMIC UPDATE DEC. 8, 2025

Stock prices pushed higher last week, notching multiple records along the way as employment and inflation data took center stage in anticipation of the Fed's upcoming meeting.

The Standard & Poor's 500 Index rose 0.31 percent, while the Nasdaq Composite Index picked up 0.91 percent. The Dow Jones Industrial Average gained 0.50 percent. The MSCI EAFE Index, which tracks developed overseas stock markets, added 0.72 percent.[1,2]

Fed in Spotlight

Stocks fell to start the week as all three averages snapped a five-day winning streak.[3]

Megacap tech stocks then led a recovery rally, which continued its momentum midweek as ADP's November report showed a decline in private-sector payrolls. Investors welcomed the report, believing it might prompt an interest rate adjustment at the Fed's upcoming meeting. All three major averages posted modest gains over both Tuesday and Wednesday.[4,5]

Stocks then largely went sideways, with small gains for the S&P and Nasdaq while the Dow fell slightly. Meanwhile, the Russell 2000, which measures the performance of small-cap stocks, has cracked a fresh record high.[6]

Markets rallied on Friday after a delayed inflation report showed that prices rose at a slightly slower annualized rate in September. The S&P closed out a four-day winning streak.[7]

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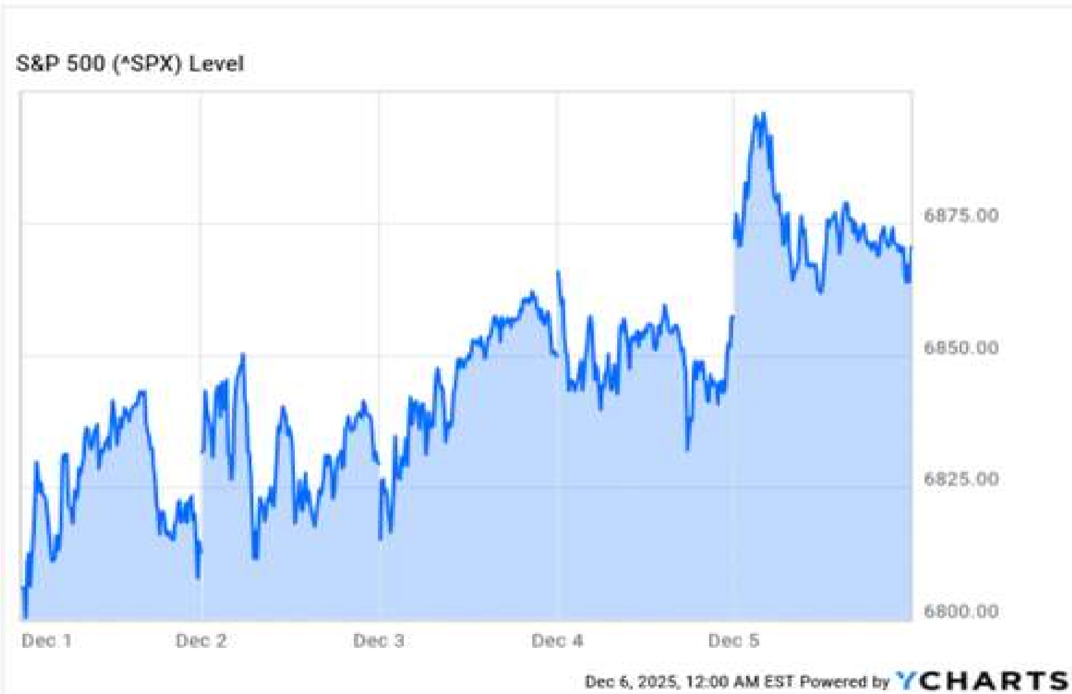
Weekly Market Insights (WMI)

Major Index Return Summary

Name	1M TR	YTD TR	1Y TR	5Yr TR
MSCI EAFE	2.53%	29.66%	25.13%	58.10%
Dow Jones Industrial Average	1.90%	14.33%	8.14%	74.35%
S&P 500	1.40%	17.98%	14.12%	99.52%
Nasdaq Composite	0.75%	22.45%	19.89%	95.67%

S&P 500 Daily Close



10-Year Note Review

Indicator Name Date	Latest Value	1M Ago 3M Ago 1Y Ago	1M Change 3M Change 1Y Change
10 Year Treasury Rate 12/05/25	4.14%	4.17% 4.10% 4.17%	-0.72% ▼ 0.98% ▲ -0.72% ▼

Economy Watch

The Fed's preferred measure of inflation stayed cool. The Personal Consumption Expenditures (PCE) Price Index rose 2.8 percent in September from a year prior, cooler than the 2.9 percent expected. The annualized core inflation rate of 2.8 percent also came in just under expectations.[8]

The ADP private-sector jobs showed employers cut 32,000 jobs in November. Two things to remember: (1) this report is only based on the first two weeks of November, and (2) small business payrolls declined by 120,000, while employers with 50 or more workers added 90,000 jobs.[9,10]

An optimistic inflation report but a sluggish jobs update added to growing speculation that the Fed will adjust rates at its next (and last) meeting of the year.[11]

This Week: Key Economic Data

Tuesday: NFIB Small Business Optimism Index. Job Openings (Oct.) Federal Open Market Committee meeting, Day 1.

Wednesday: Employment Cost Index (Q3). Federal Budget. Federal Open Market Committee meeting, Day 2. Fed Interest Rate Decision. Fed Chair Press Conference. Federal Open Market Committee meeting, Day 2. Fed Interest Rate Decision. Fed Chair Press Conference.

Thursday: Weekly Jobless Claims.

Quote of the Week

"The government you elect is the government you deserve."

– Thomas Jefferson

Of Note

The overnight funding markets are again showing signs of stress, and the scent of quantitative easing (QE) is in the air. Federal Reserve Bank of New York President John Williams recently said:

Based on recent sustained repo market pressures and other growing signs of reserves moving from abundant to ample, I expect that it will not be long before we reach ample reserves. When that happens, it will then be time to begin the process of gradual purchases of assets.

Everyone should be asking why the capital markets have become so reliant on the Fed's liquidity. The answer goes back to the 2008 financial crisis.

Before 2008, the private market — not the Fed — was the primary source of liquidity. The Fed was rarely called upon to support liquidity. Since then, the Fed has seemed to constantly tinker with its policy to manage liquidity. As some correctly say, the Fed has shifted from lender of last resort to the lender of only resort!

Considering the significant impact liquidity has across all asset classes, it's essential to appreciate this relatively new dynamic as well as understand why the Fed, rather than the private market, has become the primary liquidity manager of the financial system. Consequently, Fed policy — not free markets — now plays a crucial role in forecasting how today's speculative excesses might return to their normal levels. Will it be a pop, a slow leak, or will the Fed keep bubbles afloat at any cost?

Before 2008, its assets were growing at a slow and steady 4% pace. Not surprisingly, the 4% growth in the Fed's balance sheet was roughly in line with economic growth. After 2008, the amount of the Fed's assets surged, and the volatility of its holdings also increased significantly.

Clearly, something changed in 2008. Let's explore what that is, and in doing so, we can better appreciate the Fed's expanded role and why its policies have become much more closely integrated with the gyrations of financial markets.

Banks held minimal excess reserves prior to 2008. Instead, they mainly met their liquidity needs by lending and borrowing reserves with other banks. Many of these transactions took place in the overnight fed funds market. The Fed did not set the fed funds rate back then, nor does it now. However, before the financial crisis, it guided banks toward their target rate through daily purchases and sales of Treasury securities.

In 2008, the Fed introduced QE, which entails consistently purchasing securities regardless of liquidity conditions. Before QE, buying or selling was based on daily liquidity conditions. Because the Fed buys assets from banks with reserves, total reserves in the banking system have been grossly elevated since 2008.

The impact of QE on the financial markets and economy is twofold:

- First, the Fed removes securities from the market, allowing the liquidity in those securities to flow to other assets.
- Second, the new reserves on bank balance sheets can be used to support loan growth. The more reserves the banks hold, the more liquidity they can provide. We say "can" because the bank still must be willing and able to provide liquidity.

Today to maintain control of the overnight financing markets, the Fed pays interest on reserve balances (IORB). The Fed sets the IORB rate, which serves as a floor for the fed funds rate because banks will not lend their reserves for less than they can earn risk-free from the Fed.

Thus, in the post-QE world, the level of bank reserves and the Fed's IORB rate are predominant determinants of overnight liquidity.

Before 2008, the private sector repo markets were the core plumbing of the short-term funding markets. Fed funds are unsecured lending between banks, whereas repo is secured (collateralized) funding between all financial institutions. It is estimated that the daily volume of repo transactions was over $10 trillion before the crisis. Money market funds and other large holders of cash would invest their cash balances in repo; thus, private firms provided the capital markets with a steady, dependable stream of liquidity.

Following the near collapse of the entire banking system in 2008, the government and global banking regulatory agencies enacted a series of regulations that made it more expensive for banks and funds to lend short-term cash, including Basel III (Global Banking Regulations), Proprietary Trading Rules, and Money Market Reforms.

Before 2008, when free markets largely determined liquidity conditions, speculative bubbles would form and eventually burst when liquidity was no longer sufficient to support highly speculative valuations and high leverage.

Today, those same bubbles form. However, with the Fed at the helm of liquidity, how and when those bubbles burst is not entirely clear. For example, while the Fed is not likely thrilled with the market's current extreme valuations, it also recognizes that a normalization of valuations and a broad de-risking event could cause economic hardship and potentially harm the banking system. It will not sign up to preside over that.

Is the Fed capable of letting a bubble slowly leak? Given that this post-pandemic bubble is our first experience under the new Fed regime, we will have to wait and see.

Knowingly or unknowingly, post-financial crisis rules and regulations have kneecapped many of the old private-market liquidity providers. Without their capital and balance sheets, the Fed has become the primary source of market liquidity. To wit, consider what Jerome Powell said in 2021: "In a stress scenario today, the Federal Reserve is the only entity with the balance sheet to absorb the shock."

While there is limited experience with the new monetary regime, we have learned that the Fed doesn't have a straightforward way to assess liquidity conditions. For instance, the Fed was caught off guard in 2019 when overnight funding markets froze amid a liquidity squeeze. Conversely, in 2020 and 2021, in reaction to the pandemic, the Fed grossly oversupplied the markets with liquidity. In fact, it had to create an overnight reverse repurchase program to remove the excess reserves from the market. Quantitative tightening was also enacted to help. Those excess reserves are now gone, and, not surprisingly, liquidity stress is occurring. QE or another policy moves to increase bank reserves is imminent. The alternative is a deleveraging event, which would cause economic and financial market chaos.[12]

Footnotes and Sources

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