The Markets React to Venezuela

KATHY JONES: I'm Kathy Jones.

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KATHY: And this is *On Investing*, an original podcast from Charles Schwab. Each week we analyze what's happening in the markets and discuss how it might affect your investments.

KATHY: Well, hi, Liz Ann. Happy New Year, happy 2026.

LIZ ANN: You too.

KATHY: You know, we're only a couple days in and it's already been an exciting year. Started off with a bang, literally, with military action in Venezuela. What do you think about the market reaction so far? I think it might have been a little counterintuitive to what we might have expected.

LIZ ANN: Yeah, market reaction or lack thereof. I would say it's "nothing to see here" from the equity markets perspective. And it's interesting, it's not just a situation where we had this incredibly robust momentum at the end of the year that just plowed through and essentially meant the market was ignoring the news.

You've seen some pretty interesting shifts in performance just between the end of last year and this year. But I think it maybe is a function of what really has become one of the power drivers of the equity market, in terms of the cohorts of types of investors. And we've talked about it a lot on this program over the past couple of years, about the power of the retail trader, which I would distinguish from just a broader category of individual investors. And they're a cohort that, depending on the day, the week, what data you're looking at, it's hard to really parse out specific investing cohorts in terms of what they represent as a share of total trading volume. But the few firms that have done that, including our friends at Hedgeye, suggest that, at a minimum, retail traders represent about a quarter of daily trading volume.

And there are certain days, depending on what the action is, where it's significantly higher than that. So we can't discount their influence. And their mood can change on a dime, in terms of what they're focused on. And what's been interesting so far this year, you're right to point out that it's only been a few trading days, is a shift toward more classic cyclicals. So, you know, industrials and materials up significantly.

And there's been a lot of momentum that has developed there. And I think in general, though, retail traders at times, if not on a day-to-day basis, almost put blinders on to the big-picture news and the macro environment and geopolitics. And they're just looking for kind of the next opportunity at some sort of category level, at a sector level, at an industry level, at a thematic level and it can sometimes turn into a "life of its own" kind of situation. So I just think because we didn't see any kind of significant riot, whether it was in the currency markets or in the energy markets, I think that allowed the equity market to just kind of continue to plow ahead with this newfound interest in and focus on the more classically cyclical parts of the economy.

And I think that that's testament to the resilience and strength we're seeing in the economy, which certainly was born out when we finally got GDP data for the third quarter. Of course, that's very dated data now, but still pretty healthy assumptions for GDP growth in 2026. And an environment may be where we will have less reason to talk about the rolling nature of this cycle since the COVID period, where we've avoided, other than the very brief COVID recession in 2020, we've avoided any kind of full-blown economic recession, but we've had these rolling recessions. We've had sectoral recessions in the economy and that's persisted.

Arguably, we still haven't even pulled out of the manufacturing one if you use the ISM manufacturing index as a proxy for that. But I think this could be a year where it's less about big sectoral differences and an environment that may be a little bit healthier across the spectrum of the economy. That's assuming the labor market holds together. I don't think you disagree that that is such a key facet to all of this as it relates to the health of the economy, the resilience of consumer spending, metrics like retail sales and, very importantly, Fed policy. So I'll turn, at that point, back to you just with your latest thoughts, whether it's on Venezuela and the impact it had, or not, on the bond market and what's been happening with Treasury yields and what your latest thinking is on Fed policy.

KATHY: It is interesting that the bond market had very little reaction. Coming into it before the markets opened, I thought, well, you know, the initial impression was, "OK, maybe this frees up more oil on the global market. And that means that oil prices in the futures contracts, you know, going out a year or two, because it's not going to be produced right away, fall, but it kind of pulls down overall prices and that that would reduce Treasury yields, lift Treasury prices on the prospect for lower inflation." And I think one thing people miss is much of the improvement in inflation we've seen over the last year has come from the energy sector. So we have seen those prices come down and that's been already a factor. So that's kind of priced-in now.

But, at the end of the day, the bond market didn't do a whole lot with this news. And I guess that's a reflection of the fact that it's still a work in progress from what we can all see. We don't know what the playbook is going to be. There's promise of more oil, but billions and billions and billions of dollars of investment need to be made over a long period of time. And that's all very much up in the air, in terms of whether oil companies will do that or not and what the timetable might be for this to actually manifest into something meaningful. So I think that that explains the bond market sort of sitting still and going, "Well, you know, show me what's going to happen, right? Give me something more."

And energy prices have come down a bit, but I can't say that they fell, they're already down, so they didn't fall a huge amount from where they were already down. And I think the market's sort of in a wait-and-see situation. As for Fed policy, you can make the case that if this were to depress energy costs, that that certainly flows through the households and the Fed would be inclined, more inclined to ease than not. But again, over what timeframe, when is that going to happen? How long is it going to persist? How certain are we of that?

Those are all big questions. In the meanwhile, though, as you point out, the economy still has some momentum and we're all waiting for good employment data. We haven't had any for a long time. It's sort of a mystery. Where is the labor market these days? How strong, how weak, in what areas? So I think the Fed is biased towards easing. They've made that pretty clear from a lot of comments from various officials but then we have this whole business of the turnover at the Fed and Powell's upcoming retirement as chair. Who gets appointed in his place? We can assume whoever it is is going to be biased toward easing. The rest of the committee, you know, is not 100% on board with that so I think market to sit still here waiting to see, you know, the next shoe to drop and, as we know these days, shoes continue to drop over and over again. So I think we have to be prepared for that to happen. But I agree with you, it's the labor market that matters more than anything.

LIZ ANN: I have another question for you, but before I ask it, I was remiss in pointing out that we put a report out on Monday that it was under mine and Kevin's byline, but I took advantage of lots of communications, as you know, Kathy, that we all had within Schwab Center for Financial Research over the weekend as the events in Venezuela were unfolding and took advantage of all the great commentary.

So I put together basically a collection of all of our thoughts about the impact, or as we already mentioned, the lack thereof on our markets, but I would point people to that. It's on Schwab.com on the Learn tab. the first start of the title is "Forward/Backward." It takes a look at what happened and initial market reactions from the perspective of the equity side of things, the bond market side of things, the international side of things, and we do have a table in there that we've shown in the past many times in various reports and at various times, looking at some of the key geopolitical events that have happened in our world in the post-World War II period and the market's action from an equity market perspective in the subsequent months up to a year out.

It's a bit of a mixed bag, but what it does highlight is you don't tend to see a long-lasting impact, unless either it becomes into a truly protracted military conflict that works its way through the energy channels or in the case that one example in this table was the war in Afghanistan, starting in 2001 and a year later the market was down 25%. But I probably don't need to remind what are typically an investor audience of our podcast here that there was maybe something else going on in 2001 that impacted the stock market like the bursting of the tech bubble and a brutal two-and-a-half-year bear market, but take a look at that.

But I wanted to ask you whether you have any thoughts on any eventual restructuring in debt in Venezuela and maybe how the US might be involved in that.

KATHY: Yeah, it's a great question. Venezuela has a huge amount of debt. They've defaulted on a number of their bonds. And I think it's just too soon to tell what's going to happen there. I would observe that from what we can see in some of the defaulted bonds, they've traded higher in price because the market is looking at perhaps a higher recovery value than…They were trading about 22 cents on the dollar and in default world that's pretty much the bottom end of where they go. Twenty cents on the dollar is about as low as it goes. They traded up into the high 30 cent, 40 cent area. I don't think they can go much further than that unless we see some real concrete movement towards actually restructuring the debt.

But it's a huge amount of debt. It's spread out over many, many creditors, lots of legal issues that could come up. And claims could be made by a lot of different groups. So this is probably as complicated and messy as any debt restructuring you can imagine. If I think about, say, Puerto Rico, Puerto Rico is still being litigated, in some cases. That was complicated, too.

So I would say any restructuring of Venezuela's debt would have to have some sort of backstop from somebody, you know, some sort of claim on some of its assets. I think that's really hard to pull off in this environment, but the political environment's so unstable, it's hard to tell. I would just say that it's going to keep the lawyers very busy for a long time. It's a lifetime employment guarantee for some lawyers….

LIZ ANN: Throw something else on the lawyer's laps these days.

KATHY: Yeah, exactly. For them to attempt this. But honestly, it seems it's still down the road. I don't think, we don't have enough clarity, at least from what I can see. There's not enough clarity as to how this… what the plan might be one way or another and who might be the people involved in any of this. So it's just a big question mark at this stage of the game.

LIZ ANN: Yeah, and as a reminder to people, too, there's always the knee-jerk reactions, which we saw very initially to some degree in the oil market. But, as a reminder, there was a lot of headlines that I saw that didn't go into appropriate detail thereafter about proven reserves in Venezuela. And they do claim to have the largest in the world. But what they're actually getting out of the ground and then exporting is minuscule.

And that's not a spigot that can be turned on very quickly. So you're right to point out, in the context of us talking about market implications, that this is well down the road. And there's the ongoing question of, is it even an economically viable prospect for many of the major oil companies or even the drillers to go in, given that we basically have a global oil glut? There's more supply globally of oil than there is demand.

So, I think some of that kneejerk, this is immediately beneficial for the energy sector and the companies that can go in and drill, drill, drill. And I think cooler heads in the aftermath of that realize that there are a lot of hurdles to get through the difficulty of getting this out of the ground with the investments are needed associated with that, whether those investments would actually be beneficial or profitable. So, TBD.

KATHY: Yeah, no doubt about that. I mean, this is a big… I think it's been 20-some-odd years of deterioration in Venezuela's infrastructure. Fixing that will obviously take a lot of time and a lot of money and where's the money going to come from, and what are the prospects for return on that investment? Those are all questions that anybody running a company right now is trying to think through. So, yeah, we'll see.

Moving on to other topics, I did want to ask you a little bit, we got the JOLTS report, Job Openings and Labor Turnover Survey this morning. It looked a little soft. It looks like we're not creating a lot of jobs.

LIZ ANN: It was a little soft. And in keeping with your comment, its "Where the heck are the jobs?" Notwithstanding the resilience in the broader economy, we certainly have not been bombarded by healthy jobs numbers. One reminder about the JOLTS data, and they... as part of that survey, a couple of metrics are reported. Job openings tend to get the most attention, but there's also a quits rate that maybe gets a little bit less attention, although it did during the early part of the COVID cycle because quits, which is measured as voluntary quit. So what you can infer is that people, a large number of people quitting their jobs voluntarily is probably because they have confidence in the labor market. And that has come down along with job openings.

An important note, though, about the JOLTS data, I don't focus on it maybe as much as some other people, not only because it lags all other labor market data by a month, but response rate to that survey have come down quite significantly over the past decade or so. And in the world of being digital, the way job openings are measured, the fact that it's basically a cost-free process for a lot of companies, so they might post job openings in some sort of online format, and there's not really an economic incentive to make sure that they're always fresh and they're... you know, the old ones are taken down. So I think it's a little bit of, sort of a grain of salt indicator, but yeah, it certainly corroborates the other soft data that we are seeing. You know, I also wanted to touch on the tariff story a little bit.

A lot of interesting data coming out lately with, generally, headlines around tariffs not having quite the deleterious impact on the economy as one would expect. And to some degree, I think there's truth to that, but I think it's important to provide some context there. So one way to judge the impact of tariffs is to look at, in somewhat simple terms, the effective tariff rate. If you take everything that has out there right now, not just still may be proposed, but everything that's out there right now, look at it in percentage terms, but then compare that to the actual remittances that go into Treasury from, and a reminder, it's US companies paying the tariff. It's the US companies importing the goods from the targeted countries. There is a spread between those two, and that is confounding to some, but if you take the time and look at some of the details of that spread, some of it can be accounted for by a lot of exceptions that have kicked in. Certainly many of the larger companies that have more flexibility in their supply chains. Some of the trans-shipments where if you're a targeted country like China, you can maybe divert some shipments of goods that ultimately make their way into the United States to countries that have a friendlier tariff policy and so on and so on. So I think that can account for it.

But I also think that embedded in here is the differential between large companies and small companies and the impact that something like tariffs have on them. Most of the data that we get, whether it's profit margin data, profitability data, what the whole cost structure is inclusive of tariffs, tend to be for companies and indexes like the S&P 500®, so very large publicly traded companies. If you look at the data that we can get on smaller companies, and in particular, non-publicly traded companies. So one of the metrics that I keep an eye on when we get the GDP report every quarter is embedded in that report is a much broader version of corporate profits than what we focus on, on a quarterly basis, which is S&P 500 profits. So it's National Income and Product Accounts profits. It's N-I-P-A, NIPA for short. And it's millions of companies, publicly traded companies, private companies, tiny companies, S-corps. And earnings growth there has been quite anemic. We actually… the first half of the year was actually in negative territory, marginally moved into positive territory when we got the third quarter report.

You look at anecdotes coming from smaller companies, maybe it's obvious, but they don't have the same kind of flexibility. They tend to have limited other sources if they have a supply chain line directly to someplace like China. They just don't have that flexibility. And it really highlights, again, the sort K-shaped nature of this and just a very different backdrop and story if you're thinking about profits, profit margins, impact of tariffs and you're only focused on, say, an index like the S&P 500, I think the fuller story is told under the surface of an index like that. So just wanted to point that out because there has been a lot of attention on. I think it's too simplistic to say "Nothing to see here, tariffs not a problem." I think that the story is richer than that.

KATHY: Well, yeah, and if you read the comments and the various Fed surveys, the tariffs are mentioned all the time, particularly in the manufacturing sector, but also in the retail sector. So it is a common refrain among companies saying that this has been a problem. And then you look at manufacturing, has not been doing well for a long time and tariffs did not help there.

LIZ ANN: In fact, speaking of comments, you're right. I think some of the most interesting aspects to these regional Fed surveys and the data we get on a monthly basis are some of the verbatim comments embedded therein. And same thing with the ISM manufacturing and services indexes. They publish a lot of the verbatim comments from the companies that are part of that survey. And the services side of the economy, which we got that data today, was actually quite strong. Everything went the direction you would want it to. Services index was up, you know, forward-looking new orders was up, prices paid down, employment up, but very different story in manufacturing. And you're right, the verbatims within the ISM survey still have a lot to do with tariffs.

KATHY: Another sort of anecdote here. The San Francisco Fed published a report that's been cited a lot about how the impact of tariffs on inflation has been rather minor. And people point that to that and say, "See, no, not a big problem." If you read the entire study, what they say is the reason is that tariffs slowed economic growth. Therefore, there were some offsetting factors. So again, they slow growth and raise prices. In the end, it seems like it might be a bit of a wash, but nonetheless, it hasn't… you know, I think the whole story has not been told, to tell you the truth.

LIZ ANN: Yeah, well, there's also the swing factor. So a lot of people will look at inflation data in a snapshot in time, at some moment. And so if you look at goods inflation, if you break out an inflation metric like the Consumer Price Index into the services side or the non-goods side and the goods side, the goods side still has a little bit less than 2% inflation rate. And people are saying, "See, no problem, that's around the Fed's target," but that's up from what was a 2% deflation rate. So all you have to do actually is look at a chart and you very clearly see the acceleration very much tied to the implementation, the start of implementation of tariffs. So we need to be mindful of inflection points and the turn that happens as opposed to snapshot in time, look at the level, and declare victory.

KATHY: Right, well, I think there's going to be a lot of data for you and Kevin to be parsing here for a while.

LIZ ANN: You too.

KATHY: And us too. So I think we're going to have a lot of churning that I think for the bond market, it comes down to the job market, it comes down to the Fed. I think at the end of the day, a lot of the rest of this is noise, but it's not really shifting the market expectations yet. It remains to be seen but at this stage of the game, those are really the things, you know, "What's the job market doing? How does that affect the Fed? What happens?" We're due to get some announcement from the President about his nominee for the Fed chair position. The odds keep changing on who's in leader of the pack, but I think that's going to be really, really important.

So, Liz Ann, looking ahead to next week, what do you think investors should be paying attention to?

LIZ ANN: Well, it's not just next week. You and I are taping this midweek. So it's in advance of the very important jobs report that we'll get at the end of the week. And that has, obviously, lots of details in it. The establishment survey, which generates payrolls, the household survey, which generates the unemployment rate, the unemployment rate itself, long-term unemployment wages. So it's always a very meaty number. And I always want to caution that investors should just not pay attention to the payrolls and the unemployment rate, which tend to be the first two headlines and really look at the innards of a report like that. Staying on the labor market, we also get the Challenger, Gray, & Christmas layoff announcements. I think those will stay in the spotlight.

We're going to get some productivity data out. That sometimes flies under the radar. I think these days it's a little more in the radar just because of appropriate questions about "Are we starting to see the benefits of AI accrue to broader productivity measures?" We already touched on tariffs, but we get trade deficit and also import and export prices. So that's another way to kind of proxy the impact of tariffs. I touched on the difference between small companies and large companies. One way to metric small companies is through the National Federation of Independent Business Survey that's coming out in the next week.

And then we get, you know, the big ones, the Consumer Price Index, Producer Price Index next week, as well as retail sales. So I'm assuming they're also on your radar, but anything else that you're keeping an eye on in the next week and a half?

KATHY: Two things: one is a ton of Fed speak coming out. So almost everybody on the Fed is speaking over the next week or two. And so we'll get… sort of keep a tally of who's where in terms of their expectations for a rate cut as early as, you know, end of January or possibly later. And also point out that we're scrutinizing all these numbers, particularly the employment numbers and the CPI numbers, because those are so important. The Bureau of Labor Statistics, which puts out these numbers, yes, they're back at work, but their total staff is down over 30%, which means that can affect data quality as well. So we not only have a

collection problem. We now have a lack of statisticians or a shortage of statisticians to do the work and that can affect the quality of the numbers that we're getting. So my big fear is we get numbers, we react to them, we build a thesis based on the numbers and then we get these huge revisions when they have time to go back. So word of warning there, overreacting to short-term data. But that's what we have to deal with, so that's what we're going to go on.

And of course, we'll keep an eye on all the international developments. It seems to be a surprise every week.

LIZ ANN: Keeping us on our toes.

KATHY: That's right, we'll have to definitely be on our toes about that.

LIZ ANN: Well, great chat as always. Nice to catch up at the start of the year. But that is it for us today. Thanks as always for listening. As a reminder, you can keep up with us in real time on social media, I'm @LizAnnSonders on X and LinkedIn. And make sure you're following the actual me. I still have lots of imposters.

KATHY: I am @KathyJones on X and LinkedIn, and that's Kathy with a K. And you can always read our reports including lots of charts and graphs at Schwab.com slash learn.

LIZ ANN: And as always, if you've enjoyed the show, we'd be so grateful if you would leave us a review on Apple Podcasts, a rating on Spotify, or feedback wherever you listen. And please tell a friend or two or more about the show, and we will be back with a new episode next week.

KATHY: For important disclosures, see the show notes or visit schwab.com/OnInvesting, where you can also find the transcript.