

In this month's recap: tariff talk weighs on equities worldwide, oil prices jump 10%, and the Fed raises rates once more.

Monthly Economic Update

Presented by «Harry D Toro, CDFATM», July 2018

THE MONTH IN BRIEF

While segments of the stock market rallied in June, assumptions that a global trade war was starting hurt the blue chips – the Dow Jones Industrial Average lost 0.59% last month. As the U.S., European Union, and China exchanged tariff threats, equity benchmarks worldwide treaded water or took losses. The economy was doing well: the latest hiring and retail sales data was excellent, consumer confidence appeared strong, and industries were growing impressively. Inflation pressure was mounting, and unsurprisingly, the Federal Reserve responded with another interest rate hike. New home sales improved, but residential resales waned. Ongoing trade frictions seemed to mute much of the bullishness seen early in the year.¹

DOMESTIC ECONOMIC HEALTH

The Trump administration announced further tariffs in June. New import duties aimed at China are scheduled for a July 6 launch: \$34 billion in Chinese goods are supposed to be hit with 25% tariffs beginning on that date, with another \$16 billion in Chinese imports potentially susceptible to these levies in the future. In addition, the U.S. may impose a 10% tariff on another \$200 billion of Chinese products. A 20% tariff on autos coming from the European Union is also planned. The E.U. and China have retaliatory measures to these moves in the works (see “Global Economic Health” below).²

Away from tariffs and their implications, investors absorbed some excellent reports on the U.S. economy. The Department of Labor's May jobs report showed a net hiring gain of 223,000 and wages up 0.3% for the month (better than the 0.1% rise in April). The headline unemployment rate declined 0.1% to just 3.8%, and the U-6 jobless rate, including the underemployed, fell from 7.8% to 7.6%. Retail sales improved a striking 0.8% in May, and the gain held even without the inclusion of gasoline and automotive purchases.³

Major consumer confidence indices remained elevated. The University of Michigan's barometer of household sentiment, which had finished May at 98.0, ended June at 98.2. As for the Conference Board's gauge, it fell 2.4 points to 126.4.^{3,4}

Although durable goods orders were down 0.6% for May (after a 1.0% April fall), the latest purchasing manager index readings at the Institute for Supply Management were still well above the all-important 50 level, delineating industry expansion from industry contraction. ISM's factory PMI rose 1.4 points to 58.7, while its service sector PMI added 1.8 points to reach 58.6.^{3,4}

May's Consumer Price Index arrived, and it showed yearly headline inflation at 2.8% and yearly core inflation (minus food and energy costs) at 2.2%. (Both the headline and core CPI were up 0.2% for the month.) The Federal Reserve's preferred inflation barometer, the core PCE price index, displayed 2.0% a yearly rise through May. That marked the first time it had met the central bank's longstanding inflation target since April 2012. Annualized wholesale inflation, as measured by the Producer Price Index, surged to 3.1% in May from 2.6% in April.^{3,5}

Investors widely assumed the Fed would make another quarter-point rate adjustment in June. Those expectations were met. On June 13, the Federal Open Market Committee voted to lift the target range on the federal funds rate to 1.75%-2.00%, and it also put out a new dot-plot projecting four rate hikes in 2018. (It forecast 2.8% GDP for 2018.)⁶

Early in June, the federal government noted that Social Security would tap into its trust funds in 2018. This last happened in 1982. The latest report from Social Security's trustees projected 2034 as the year in which retirement benefits could be cut 23% if no legislative action is taken to help the program beforehand. The trustees also said Medicare's hospital insurance (Part A) fund could be depleted by 2026, three years earlier than they had previously projected; if nothing is done to boost funding before then, it will only be able to pay out 91% of Part A costs in that year.⁷

GLOBAL ECONOMIC HEALTH

Was China ready to enter a trade war with America? Apparently so. Having already had U.S. tariffs imposed on its washing machines and solar panels earlier this year, the P.R.C. reacted to the probability of \$34 billion in import taxes being imposed on its goods on July 6 by promising an equal tariff: excise taxes on \$34 billion of products coming from the U.S., commencing on the very same day. The nation's manufacturing engine revved down in June; its factory PMI fell 0.4 points to 51.5. Its service sector PMI, however, ticked up from 54.9 to 55.0.^{2,8}

Last month, the European Union responded to the metals tariffs enacted by the U.S. on its steel and aluminum exports with 25% duties on assorted U.S. imports (including motorcycles, bourbon, jeans, and orange juice). The Trump administration's pledge to impose tariffs on cars coming from the E.U. was met with an immediate warning: the E.U. was ready to put additional import taxes on American-made goods. Any such retaliatory tariffs might be sizable, since the value of exported autos coming from the E.U. to the U.S. is about 10 times that of the E.U.'s total steel and aluminum exports.^{2,9}

WORLD MARKETS

The benchmark indices of Mexico and Canada had a fine June. In Mexico City, the Bolsa jumped 6.75% for the month, while in Toronto, the TSX Composite added 2.23%. A look around the world reveals a few other gains: 2.74% for Australia's All Ordinaries, 1.06% for Spain's IBEX 35, 1.36% for India's Sensex, and 0.76% for India's other marquee index, the Nifty 50.¹⁰

Other stock gauges simply slumped as investors grew pessimistic. The Shanghai Composite took the hardest fall of any major benchmark last month, dropping 8.72%. Argentina's Merval slipped 8.08%. South Korea's Kospì lost 5.34%, while the Hang Seng declined 5.02%. Brazil's Bovespa retreated 4.35%. In Europe, Germany's DAX lost 2.85%; France's CAC 40, 2.11%; the FTSE Eurofirst 300, 1.23%. The Nikkei 225 was barely harmed, down only 0.24% for the month. While the MSCI World Index lost just 0.17%, the MSCI Emerging Markets index fell 4.57%.^{10,11}

COMMODITIES MARKETS

Rising 10.66% for the month, WTI crude oil settled at \$74.25 on the NYMEX on June 29. Heating oil futures improved 0.23% in June, but unleaded gasoline futures declined 1.13%, and natural gas futures, 1.15%.¹²

All four marquee metals retreated in June. Silver lost the least, falling 2.67%. Copper slipped 3.34%; gold, 3.37%; platinum, 6.21%. Gold ended the month at a COMEX price of \$1,254.20;

silver, at a COMEX price of \$16.06. The U.S. Dollar Index gained 1.42% in June, concluding the month at 95.32.^{12,13}

Turning to the major ag futures, we see widespread losses, some deep. While cocoa added 0.73% in June, wheat fell 5.29%; sugar, 7.11%; cotton, 8.57%; coffee, 8.93%. Corn futures tumbled 11.05%; soybean futures, 15.87%.¹²

REAL ESTATE

Existing home sales, which account for the clear majority of residential estate transactions, weakened 0.4% in May; this followed the (revised) 2.7% April retreat measured by the National Association of Realtors. New home sales surprised to the upside in May, according to the Census Bureau; its latest monthly report showed the pace of new home buying improving 6.7%. One contributing factor may have been the ongoing decline in new home prices. At \$313,000, the median price was down 3.3% from where it was a year earlier.^{3,14}

A stabilization in mortgage rates may have also spelled relief for some buyers. Rates were practically unchanged between Freddie Mac's May 31 and June 28 Primary Mortgage Market Surveys: average interest on the 30-year fixed merely went from 4.56% to 4.55%, while the mean rate on the 15-year fixed declined to 4.04% from 4.06%. The average rate on the 5/1-year ARM, influenced to greater degree by Federal Reserve policy, rose from 3.80% to 3.87%.¹⁵

The lagging indicator tracking home values across 20 metro markets – the S&P CoreLogic Case-Shiller index – showed a 6.4% yearly advance in U.S. home prices through April. The NAR's forward-looking pending home sales index declined 0.5% for May, which was at least less than the 1.3% dip it took the prior month. Builders broke ground on 5.0% more residential projects nationally in May than they had in April, the Census Bureau said; the rate of permits issued, however, decreased 4.6% in May.^{3,4}

TIP OF THE MONTH



The cost of a private college may be easier to handle than you think. Grants to promote diversity of the student body and alumni-endowed scholarships may help. Also, a student's financial need may prove greater at a pricier college, and that demonstrated need may warrant more financial aid.

LOOKING BACK... LOOKING FORWARD

The Nasdaq Composite set the pace for the big three in June, rising 0.92% to a June 29 close of 7,510.30. Finishing the month at 2,718.37, the S&P 500 improved 0.48% for the month; the Dow Jones Industrial Average lost 0.59% in June, falling to 24,271.41. Small caps moved north a bit: the Russell 2000 added 0.58% in June to settle at 1,643.07 as the trading month ended. Finally, the CBOE VIX rose 4.28% for the month to 16.09. Two Wall Street equity indices were up double-digits YTD as June concluded: the NYSE Arca Biotechnology Index at +12.54% and the Nasdaq-100 at +10.07%.^{1,16}

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	-1.81	14.02	12.56	11.38
NASDAQ	8.79	22.23	24.14	22.75
S&P 500	1.67	12.34	13.85	11.24

REAL YIELD (%)	6/29 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.74	0.55	0.53	1.48

Sources: wsj.com, bigcharts.com, treasury.gov - 6/29/18^{16,17,18,19}

Indices are unmanaged, do not incur fees or expenses, and cannot be invested into directly. These returns do not include dividends.
10-year TIPS real yield = projected return at maturity given expected inflation.

The first half of 2018 is now history. Remember all the pundits who predicted a single-digit return for the S&P 500 this year? They may be right. The S&P has largely moved sideways, and it may keep doing so in the third and fourth quarters. America is witnessing healthy economic growth, which should continue to promote strong corporate earnings – but investors have tariffs on their mind, the yield curve has been flattening, and the Federal Reserve continues to make borrowing more expensive. Another sign of reduced bullishness: the unusual length of this current stock market correction. Wall Street has not seen a correction this long since 2008, and if it persists into mid-July (which appears likely), it will become the longest correction in 34 years. Since the end of January, the S&P has simply

drifted within a 10% range. A breakout in the second half could occur, but a cautionary mood does seem to be in place as well as a perception that this bull market is entering its last phase. Perhaps the mood will lift and the market will rally, but bulls could simply remain on the sidelines while the market keeps heading sideways toward 2019.²⁰

QUOTE OF THE MONTH



*“Having a lot of money does not automatically make you a successful person. What you want is **money and meaning**. You want your work to be meaningful, because meaning is what brings the real richness to your life.”*

OPRAH WINFREY

UPCOMING RELEASES

What will investors watch across the rest of July? Here are the key reports: the minutes from the Federal Reserve’s recent policy meeting and the June ISM service sector PMI (7/5), the Department of Labor’s latest employment report (7/6), June wholesale inflation (7/11), June’s Consumer Price Index (7/12), the initial July University of Michigan consumer sentiment index (7/13), the June retail sales report (7/16), June industrial output (7/17), the Census Bureau’s latest snapshot of housing starts and building permits and a new Beige Book from the Fed (7/18), the Conference Board’s June leading indicator index (7/19), the NAR’s June existing home sales report (7/23), June new home sales (7/25), June hard goods orders (7/26), the second estimate of Q2 economic growth and the final July University of Michigan consumer sentiment index (7/27), the NAR’s newest pending home sales index (7/30), and finally the Conference Board’s latest consumer confidence index, the June PCE price index, and June consumer spending (7/31).

THE MONTHLY RIDDLE



Getting into it is often easy, as it may not require speech or much thought. It is often very difficult to get out of, though.

What is it?

LAST WEEK'S RIDDLE: This word has six letters; the first and last letters are Es. Take away either the first or last letter, and you can pronounce the five letters left to sound the same as the six-letter word. What word is this?

ANSWER: Excuse.

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Know someone who could use information like this?

Please feel free send us their contact information via phone or email. (Don't worry – we'll request their permission before adding them to our mailing list.)

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All economic and performance data is historical and not indicative of future results. The Dow Jones Industrial Average is a price-weighted index of 30 actively traded blue-chip stocks. The NASDAQ Composite Index is a market-weighted index of all over-the-counter common stocks traded on the National Association of Securities Dealers Automated Quotation System. The Standard & Poor's 500 (S&P 500) is a market-cap weighted index composed of the common stocks of 500 leading companies in leading industries of the U.S. economy. The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The CBOE Volatility Index® (VIX®) is a key measure of market expectations of near-term volatility conveyed by S&P 500 stock index option prices. NYSE Group, Inc. (NYSE:NYX) operates two securities exchanges: the New York Stock Exchange (the "NYSE") and NYSE Arca (formerly known as the Archipelago Exchange, or ArcaEx®, and the Pacific Exchange). NYSE Group is a leading provider of securities listing, trading and market data products and services. The New York Mercantile Exchange, Inc. (NYMEX) is the world's largest physical commodity futures exchange and the preeminent trading forum for energy and precious metals, with trading conducted through two divisions – the NYMEX Division, home to the energy, platinum, and palladium markets, and the COMEX Division, on which all other metals trade. The Mexican Stock Exchange, commonly known as Mexican Bolsa, Mexbol, or BMV, is the only stock exchange in Mexico. The S&P/TSX Composite Index is an index of the stock (equity) prices of the largest companies on the Toronto Stock Exchange (TSX) as measured by market capitalization. The All Ordinaries (XAO) is considered a total market barometer for the Australian stock market and contains the 500 largest ASX-listed companies by way of market capitalization. The IBEX 35 is the benchmark stock market index of the Bolsa de Madrid, Spain's principal stock exchange. The BSE SENSEX (Bombay Stock Exchange Sensitive Index), also-called the BSE 30 (BOMBAY STOCK EXCHANGE) or simply the SENSEX, is a free-float market capitalization-weighted stock market index of 30 well-established and financially sound companies listed on the Bombay Stock Exchange (BSE). The Nifty 50 (NITFE 50) is a well-diversified 50-stock index accounting for 13 sectors of the Indian economy. It is used for a variety of purposes such as benchmarking fund portfolios, index-based derivatives and index funds. The SSE Composite Index is an index of all stocks (A shares and B shares) that are traded at the Shanghai Stock Exchange. The Merval Index (MERCado de VALores, literally Stock Exchange) is the most important index of the Buenos Aires Stock Exchange. The Korea Composite Stock Price Index or KOSPI is the major stock market index of South Korea, representing all common stocks traded on the Korea Exchange. The Hang Seng Index is a free float-adjusted market capitalization-weighted stock market index that is the main indicator of the overall market performance in Hong Kong. The Bovespa Index is a gross total return index weighted by traded volume & is comprised of the most liquid stocks traded on the Sao Paulo Stock Exchange. The DAX 30 is a Blue-Chip stock market index consisting of the 30 major German companies trading on the Frankfurt Stock Exchange. The CAC-40 Index is a narrow-based, modified capitalization-weighted index of 40 companies listed on the Paris Bourse. The FTSEurofirst 300 Index comprises the 300 largest companies ranked by market capitalisation in the FTSE Developed Europe Index. Nikkei 225 (Ticker: ^N225) is a stock market index for the Tokyo Stock Exchange (TSE). The Nikkei average is the most watched index of Asian stocks. The MSCI World Index is a free-float weighted equity index that includes developed world markets, and does not include emerging markets. The MSCI Emerging Markets Index is a float-adjusted market capitalization index consisting of indices in more than 25 emerging economies. The US Dollar Index measures the performance of the U.S. dollar against a basket of six currencies. The NASDAQ-100 is a stock market index made up of 103 equity securities issued by 100 of the largest non-financial companies listed on the NASDAQ. It is a modified capitalization-weighted index. The NYSE Arca Biotechnology IndexSM is an equal dollar weighted index designed to measure the performance of a cross section of companies in the biotechnology industry that are primarily involved in the use of biological processes to develop products or provide services. Additional risks are associated with international investing, such as currency fluctuations, political and economic instability and differences in accounting standards. This material represents an assessment of the market environment at a specific point in time and is not intended to be a forecast of future events, or a guarantee of future results. MarketingPro, Inc. is not affiliated with any person or firm that may be providing this information to you. The publisher is not engaged in rendering legal, accounting or other professional services. If assistance is needed, the reader is advised to engage the services of a competent professional.

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