

Monthly Economic Update

September 2018

In this month's recap: stocks make history, consumer confidence rises, the housing market's summer slump continues, and a new trade pact might replace NAFTA.

THE MONTH IN BRIEF

Wall Street had much to celebrate in August. The S&P 500 and Nasdaq Composite both reached historic heights, with the Nasdaq crossing two 1,000-point milestones in a calendar year for the first time since 1999. The current bull market became the longest on record. U.S. stock exchanges outperformed many others around the world, as imposed tariffs and currency troubles in the emerging markets gave overseas investors pause. Major commodities largely lost ground. U.S. economic indicators were again strong for the most part, aside from those in the housing sector.¹

DOMESTIC ECONOMIC HEALTH

As August ended, the White House was trying to forge a new multi-national trade deal to replace the North American Free Trade Agreement (NAFTA). Mexico and the U.S. tentatively agreed to a new trade pact that would increase wages for Mexico's workers, keep Mexican agricultural exports free from U.S. import taxes, and require 75% of the value of vehicles sold in North America to be produced in either America, Canada, or Mexico (a 12.5% increase). The Trump administration hoped to have Canada join the preliminary accord by September 1, but it decided not to do so, partly due to a disagreement over the treatment of dairy prices. Negotiations between the U.S. and Canada are set to continue this month.^{2,3}

The most respected consumer confidence index in America displayed a remarkably high reading in August. The Conference Board's barometer reached 133.4, gaining 5.5 points from its (revised) July mark. The University of Michigan's index ended August at a solid 96.2; its initial August mark was 95.3.⁴

The latest Department of Commerce snapshot of consumer spending and incomes looked good: personal spending was up 0.4% for July, wages up 0.3%. Appropriately, July also witnessed a retail sales advance of 0.5%.⁴

As for job creation, the July report from the Department of Labor showed payrolls expanding by a net 157,000 positions; a Reuters poll of economists had forecast a gain of 190,000. Despite the miss, the main jobless rate ticked down 0.1% to 3.9%,

while the broader U-6 rate, encompassing underemployed Americans, declined 0.3% to a 17-year-low of 7.5%. Annual wage growth remained at 2.7%.⁵

Yearly inflation, unfortunately, was running above 2.7%. The July Consumer Price Index measured it at 2.9% through July, the highest number seen since February 2012. (The headline Producer Price Index was flat for July; that left its year-over-year gain at 3.3% and the annualized advance of the core PPI at 2.7%.)^{6,7}

The service sector and the factory sector expanded at a noteworthy pace in July, by the estimation of the Institute for Supply Management. ISM's purchasing manager index for the manufacturing industry fell from a very high 60.2 reading to a mark of 58.1, but this nonetheless signals impressive expansion. The Institute's non-manufacturing gauge dropped 3.4 points to 55.7 in July, still a good reading.⁸

GLOBAL ECONOMIC HEALTH

Emerging market currencies continued to be hit hard in August. Nations holding large amounts of dollar-denominated debt have been put in a tough situation with the Federal Reserve raising interest rates and the greenback gaining strength. The Turkish lira dropped 18.5% on August 10, after President Trump's pledge to double tariffs on imported Turkish aluminum and steel; through mid-August, it was down 40% versus the dollar on the year. Argentina's peso slipped to a record low early in the month, several weeks after the nation received a \$50 billion bailout from the International Monetary Fund. In late August, Argentina raised its benchmark interest rate from an already astonishing 45% to 60%, with its banking officials stating it would remain that high through the end of November. Hopefully, these troubles will not prove contagious.^{9,10}

As August concluded, it appeared the European Union and United Kingdom were willing to reset their October Brexit withdrawal treaty deadline. Meanwhile, Italy made noise about possibly vetoing the new E.U. budget, as its 10-year note yields spiked to levels approaching those seen in the 2012 European debt crisis. Concerns about China's powerhouse economy losing some of its momentum were eased a bit last month. The country's official manufacturing purchasing managers index displayed a decent 51.3 reading, topping the 51.0 consensus forecast of economists polled by Reuters; its official service sector PMI improved 0.2 points to 54.2, although new orders for the sector weakened. U.S. tariffs are still set to impact \$200 billion worth of Chinese exports in the coming months.^{11,12}

WORLD MARKETS

Chinese stocks did not fare well in August: the Shanghai Composite descended 5.25%. Other notable benchmarks took sizable losses: Spain's IBEX 35 fell 4.78%; the U.K.'s FTSE 100, 4.08%; Germany's DAX, 3.45%; Brazil's Bovespa, 3.21%; the MSCI Emerging Markets index, 2.90%; the FTSE Eurofirst 300, 2.60%; Hong Kong's Hang Seng, 2.43%. France's CAC 40 lost 1.90%; Canada's TSX Composite, 1.04%; Mexico's Bolsa, 0.30%.^{13,14}

Now onto better news: the August advances. India's Nifty 50 gained 2.85%, and its Sensex improved 2.76%. The Nikkei 225 rose 1.38%; South Korea's Kospi, 1.20%; Taiwan's TSE 50, 1.09%; Russia's Micex, 1.07%; MSCI's World index, 1.04%; the Australian All Ordinaries, 0.97%.^{13,14}

COMMODITIES MARKETS

Cocoa was the big winner among headlining commodities in August, rising 7.70%. Heating oil and natural gas also scored big wins, respectively adding 5.61% and 5.03%. Crude's August gain of 2.12% was also noteworthy; oil settled at \$69.88 a barrel on the NYMEX August 31. The U.S. Dollar Index and sugar also notched small monthly gains, the former improving 0.63%, the latter 0.19%.^{15,16}

Key metals suffered another month of setbacks. Gold lost 1.75% to end the month at \$1,206.90 on the COMEX; silver, 7.02%, to wrap up the month at \$14.43. Platinum futures slid 6.31%; copper futures, 6.38%. Unleaded gasoline took a tumble, losing 5.99%. Several major crop futures had a rough month: corn lost 5.44%; soybeans, 7.75%; wheat, 6.40%; coffee, 10.74%; cotton, 8.71%.¹⁵

REAL ESTATE

August was another subpar month for home buying. The National Association of Realtors said existing home sales fell 0.7% during July, after declining 0.6% for June. Subsequently, the Census Bureau announced a 1.7% July retreat for new home sales, following a (revised) 2.4% June pullback. The NAR's pending home sales index, which measures housing contract activity in the resale market, dipped 0.7% in July after its (revised) 1.0% gain a month earlier.⁴

Data again affirmed that homes and home loans had become less affordable. In its June edition, the 20-city S&P CoreLogic Case-Shiller index showed home values rising 6.3% in the past 12 months (the gain had been 6.5% in the May edition). Freddie Mac's Primary Mortgage Market Survey of August 30 reported the average interest

rate on a conventional mortgage at 4.52%; in the first PMMS of 2018 (January 4), the mean interest rate was just 3.95%. Similar increases occurred for the average interest rate on the 15-year FRM, which went from 3.38% to 3.97% in that span, and the mean rate for the 5/1-year ARM, which rose from 3.45% to 3.85%.^{4,17}

The Census Bureau's latest monthly report on U.S. residential construction activity showed that the pace of building permits issued increased by 1.5% in July, while the rate of housing starts increased by 0.9%.⁴

LOOKING BACK, LOOKING FORWARD

Jumping 5.71% in a month, the Nasdaq Composite cracked the 8,000 ceiling for the first time, settling at 8,109.54 on August 31. The Russell 2000 also had a fine month, climbing 4.19% to finish August at 1,740.75; that left its YTD gain at 13.37%. The S&P 500 advanced 3.03% to 2,901.52 during its own record-setting month; across the three months ending in August, it gained 7.25%. Blue chips followed suit: the Dow Industrials rose 2.16% last month to 25,964.82. The CBOE VIX was fairly flat in August, up 0.23% to 12.86 and ending the month at +16.49% on the year.¹⁶

% CHANGE	Y-T-D	1-YR CHG	5-YR AVG	10-YR AVG
DJIA	5.04	18.30	15.06	12.54
NASDAQ	17.47	26.15	25.18	24.52
S&P 500	8.52	17.39	15.54	12.71

REAL YIELD (%)	8/31 RATE	1 YR AGO	5 YRS AGO	10 YRS AGO
10 YR TIPS	0.78	0.36	0.68	1.68

Sources: barchart.com, bigcharts.com, treasury.gov - 8/31/18^{1,19,20,21}

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.

What do you say about a nine-and-a-half-year-old bull market that sends the S&P 500 to an all-time high? Do you marvel at it? Do you question it? Do you worry about what might be ahead? If you are an experienced investor, you probably do all three. Despite this or that prognostication, the expiration date for this amazing bull is ultimately anyone's guess. Cautious optimism may be warranted given what has been happening with tariffs and certain currencies. The healthy economy we see now could wane in coming quarters, when the business cycle enters the phase where supply

exceeds demand (at some point, it will happen). The bulls may decide to just mill around in September and wait for the next earnings season to begin; whether they sit on the sidelines or not, this may be a good time to review the state of your investments and see just how much of your portfolio is held in equities. If you have not done this in the past few years, think about doing it today. An abrupt Wall Street downturn might seem improbable at the moment, but a nine-and-a-half-year-old bull market that suddenly propels stocks to record peaks also definitely qualifies as an improbability.

UPCOMING RELEASES

The important news items across the balance of September include: ISM's August non-manufacturing PMI and the ADP payroll report and Challenger job-cut numbers for August (9/6), the Department of Labor's August employment report (9/7), a new Producer Price Index (9/12), the latest Consumer Price Index (9/13), the initial September University of Michigan consumer sentiment index, August retail sales, and August industrial production (9/14), August housing starts and building permits (9/19), a new NAR report on existing home sales and the Conference Board's August leading indicators index (9/20), the latest S&P CoreLogic Case-Shiller home price index and Conference Board consumer confidence index (9/25), a Federal Reserve interest rate decision and fresh Census Bureau data on new home sales (9/26), reports on August pending home sales and durable goods orders and the third estimate of Q2 GDP (9/27), and then August personal spending, the August PCE price index, and the final September University of Michigan consumer sentiment index (9/30).

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Developed Europe Index. 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 CAC-40 Index is a narrow-based, modified capitalization-weighted index of 40 companies listed on the Paris Bourse. 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 Mexican Stock Exchange, commonly known as Mexican Bolsa, Mexbol, or BMV, is the only stock exchange in Mexico. The Nifty 50 (NFTF 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 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). 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 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 FTSE TWSE Taiwan 50 Index consists of the largest 50 companies by full market value and is also the first narrow-based index published in Taiwan. The MICEX 10 Index is an unweighted price index that tracks the ten most liquid Russian stocks listed on MICEX-RTS in Moscow. The MSCI World Index is a free-float weighted equity index that includes developed world markets and does not include emerging markets. 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 US Dollar Index measures the performance of the U.S. dollar against a basket of six currencies. 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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