INVESTMENT COUNSEL
Complexity to Clarity

Weekly Market Insights

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Emerging Markets Collapse, Good Economic Releases and Chaos Continues!

U.S. equity markets fell this past week even in the face of good economic news. The DJIA fell 0.19%, the S&P 500 was down 1.03% and the tech-dominated NASQAQ fell 2.55%. Although the economic releases were positive, investors were concerned about both domestic political affairs and international developments, particularly currency and market behavior in the emerging markets.

In the United States, manufacturing grew at the fastest pace in fourteen years. The Bureau of Labor Statistics (BLS) reported new job creation was an unexpectedly high 210m, jobless claims fell and wages, as one would expect, rose. The European Union appears to be in a moderate slow down, growth still positive but at a declining rate, and China in a more aggravated slow down, more about that later, all lead to a stronger U.S. dollar and a widening trade gap and that is exactly what happened. A widening trade gap, for the reasons just mentioned, is nothing to get excited about and we hope official Washington views this not as trade manipulation, but as the normal progress of the global economic cycle. There is no reason to blame the dollar's strength on anything but relative economic strength. In fact, it is something to be proud of. Investors correctly fear the Fed will be inspired to continue to raise interest rates. This is exactly what they should do. It is part of the cycle. The Fed is not trying to create conditions for a recession, but trying to prevent run-away inflation, which is far more damaging than an economic slowdown.

Every equity market we follow was down last week, with the interesting exception of Italy. We spent time last week addressing the issue of Emerging Market debt. We won't rehash it but what we said last week still stands and is getting worse.

China is an interesting story. We have written in the past about China's official and unofficial debt problems. Those problems still exist. But we are seeing more evidence that China's efforts to influence other countries by funding projects is not working very well. Even the vaunted Belt & Road program is not producing what was hoped for. Bad debts and the realization that China is by far the primary beneficiary is grating on the host countries.

We used chaos in our title and chaos appears to be a fair description of what is occurring in Washington. Two publications are rocking official Washington. The first is the recent publication of Bob Woodward's new book "Fear", a very damaging account of the Trump White House. The other, the anonymous editorial in the New York Times. The Woodward book is by a highly respected author with strong credentials. It is a credible story that even if a bit slanted, which we are certainly not saying it is, is very disturbing. The second, an anonymous editorial, is a very different animal. There is a lot to discount when an author won't sign his or her name. Having said that, it can't be ignored. If it is true, things are much worse than anyone thought. If it isn't true and it is written by a high official, things are still much worse than we thought.

This is not a political judgement about who is right or wrong. It may be the true definition of a dilemma. No really good outcome. No one knows of course, but we must try to analyze any of a multitude of outcomes and how it affects our clients.

Investors have every reason to be cautious.

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