

# Weekly Market Insights

October 28, 2019

## The Fed, China and Business Conditions!

The rally continued this past week. The DJIA rose 0.70%, the S&P 500 increased 1.22% and the NASDAQ was up 1.9%. Investors have been motivated by three important points: reasonable earnings when there were dour forecasts, indications that there will soon be a tariff war breakthrough, and anticipation that the Fed will likely ease this week. Earnings are mostly reported, so they are certainly real, but both the China breakthrough and the Fed easing are still open questions.

It is very difficult to predict if there really is a serious China-United States breakthrough. There have been many false starts, so investors, rather than speculators, would be well advised to wait and see. More on China later.

We believe the odds are strong that Chairman Powell and the Open Market Committee will vote to ease this week and it will almost certainly be 25 basis points.

### China

Most of the current publicity about China is centered on the tariff war with the United States and whether it will end soon or intensify. Both are very important questions and we have argued for some time that the disagreement will not get out of hand. The reasons are the economic and political difficulties facing President Xi and the coming election in the United States. We maintain that view. This doesn't mean that the tariff hostilities will end soon, but that it is highly unlikely they will escalate. China is facing more difficult problems than a trade war. Everyone is aware of the problems faced in Hong Kong. This is not a minor skirmish, but a serious contest with important

consequences, no matter how it is resolved. If the Hong Kong protestors appear to end victoriously, this puts President Xi Jinping in difficulty, not so much as President but in his far more powerful role as General Secretary to the CPC (Communist Party of China). The Party leaders are far more doctrinaire and unyielding than most Chinese and the only group that can put Xi in danger. Yet, if Xi cracks down too hard, he is in danger of destroying China's most vibrant financial market and creating even more capital flight.

China's other problem, we and many others believe, is that their economy has slowed far more than they admit. This slowdown is not caused by a tariff problem, but by twin obstacles. The first is the well-known "Middle Income Trap." As emerging countries start to advance out of poverty and reach the lower levels of middle income, there is a great tendency for economic growth to stall. China may very well be there. This is compounded by Xi's move to a far less democratic society and a more command economy. One of the great problems of a command economy is the inefficiency of capital allocation. We see this in printable loans to State Owned Enterprises. But, inefficiencies are rampant throughout China's economy. This is but one of many problems.

### Brexit

Brexit, of course, continues in the news with no satisfactory conclusion. Resolving it has been delayed another three months. There doesn't seem to be a resolution in sight. Perhaps the best solution is to have another referendum. This actually is being put forward. A good bet is that Brexit would fail.

# Weekly Market Insights (cont'd)

## **Where from here**

The National Association for Business Economics released its Business Conditions Digest today. In full disclosure, I am a voting member. We will spend far more time on this next week, but the consensus was more subdued compared to last quarter. However, the majority is looking for positive growth, centered on 2% through 2nd quarter 2020.

## **Economic Release Calendar**

Today we are introducing a new monthly Economic Release Calendar for our clients, business associates and friends. We field an increasing number of questions about future economic releases. In an attempt to anticipate these questions, we are initiating a monthly calendar indicating the release date of those economic indicators and Federal Reserve meetings that we think are of the most interest and of value to our readers.

The November issue will just give names, dates and consensus estimates of the releases. Each week, we will update the consensus estimates. Readers should expect, in the next few weeks, a short tutorial explaining how to read and understand them. This is important, because there are numerous pitfalls in accepting these numbers at face value. We hope you find this both interesting and helpful. Please feel free to resend to your friends and colleagues who may enjoy and benefit from this.

*To view the **November 2019 Economic Release Calendar**, please click [here](#).*

As always, we benefit from your thoughts and suggestions, so please feel free to speak with your representative or write us directly.

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