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Stone Investment Partners LLC

Stone's Weekly Market Guide - Week of June 17, 2018

Yield Curve Inverts	Recession Begin	Months Before Recession	Recession Length	S&P 500 Peak Date	Invert to Peak Duration	S&P 500 Invert to Peak	S&P 500 Decline Duration (Mos.)	S&P 500 Decline From Peak
Aug-78	Feb-80	18	6	Feb-80	18.1	13.1%	1.4	-17.1%
Sep-80	Aug-81	11	16	Nov-80	2.6	11.8%	20.7	-27.1%
Dec-88	Aug-90	20	8	Jul-90	19.1	32.3%	2.9	-19.9%
Feb-00	Apr-01	14	8	Mar-00	1.7	8.4%	31.0	-49.1%
Feb-06	Jan-08	23	18	Oct-07	20.5	22.0%	17.2	-56.8%
Mean		**17**	**11**		**12.4**	**17.5%**	**14.7**	**-34.0%**
Median		**18**	**8**		**18.1**	**13.1%**	**17.2**	**-27.1%**

Source: National Bureau of Economic Research, Bloomberg, Stone Investment Partners

Chart of the Week: What does the Fed hike and yield curve flattening mean for stocks? With the Fed raising rates and now projecting two more hikes this year, the yield curve has flattened to the lowest level since the Great Recession. Inversion (2-year Treasury yield higher than the 10-year) has an amazing record of forecasting recession well in advance, but stocks have typically continued to rise (sometimes sharply) after the inversion with a median gain of 13.1%. Certainly if the inversion eventually happens, one must raise the odds of a recession and sharp market decline in the following year or two. Bottom line: the flattening yield curve is not a reason to flee stocks.

Week in Preview:

- Geopolitics: The U.S. trade spat with China has started to heat up again with tariffs on both sides set to begin on July 6. U.K.'s House of Lords is scheduled to discuss Brexit legislation on Monday. OPEC meets on Friday to discuss possibly restoring their production cuts. The Fed releases the 2018 bank stress tests.
- Investors get a read on momentum in the global economy on Friday with June manufacturing PMIs reported for the U.S., Europe and Japan. Seems likely that the trend of good U.S. data will continue, while Europe and Japan are losing some momentum. All measures should remain well above any threat of recession.
- The Fed raised rates last week as widely expected. The Fed's "dot plot" now projects four hikes in total for 2018. See the **Chart of the Week** for the market implications. As expected the European Central Bank (ECB) didn't change rates, but plans to end of asset purchases in December and won't begin rate hikes until the summer of 2019. The Bank of Japan (BoJ) made no policy changes as forecast, but reduced inflation expectations. BoJ seems likely to continue easy policy for a longer period, while the U.S., Eurozone and U.K. are in the process of tightening. More Fedspeak and ECBspeak from the Sintra conference this week.
- U.S. data is heavy on housing with May housing starts, building permits and existing home sales expected.
- Asia data: Japan reports May trade data along with consumer inflation (CPI). CPI excluding fresh food and energy is expected to decelerate to 0.3% year-over-year.
- MSCI is reviewing Argentina and Saudi Arabia for possible inclusion in the Emerging Markets index.
- The Bank of England (BoE) meets and is expected to hold the policy rate steady. Market participants will be looking for policy clues with market odds of a hike on August 2 hike remaining above 50%. The central banks of Mozambique, Hungary, Botswana, Morocco, Thailand, Philippines, Brazil, Taiwan, Switzerland, Norway and Mexico are scheduled to meet with both Mexico and the Philippines likely to raise rates by 0.25%.

Week in Review:

- Estimates of U.S. economic growth in 2Q were mixed with the Atlanta and NY Fed estimates moving to a still robust 4.804% and 2.98% respectively. U.S. May retail sales rose more than expected and the previous month was revised higher.
- The S&P 500 was marginally higher with small-cap stocks a bit stronger. Developed international stocks were higher in local currency terms, but lower in U.S. dollar terms due to the strong dollar. Emerging market stocks were lower. The 10-year U.S. Treasury yield moved slightly lower to 2.92%.