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Stone Investment Partners LLC

Stone's Weekly Market Guide - Week of July 1, 2018

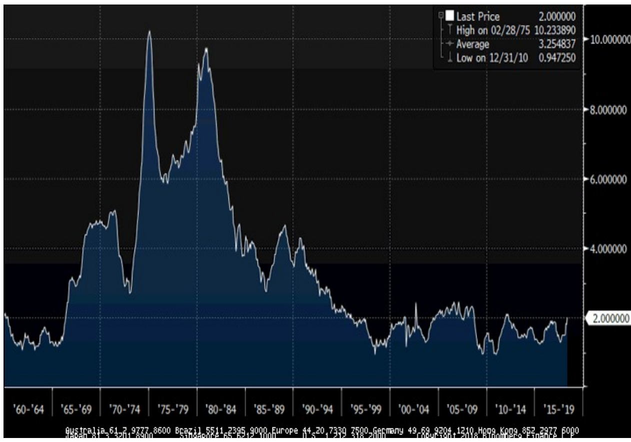

Chart of the Week: Is inflation now a threat? The PCE core deflator (a preferred Fed measure) reached its highest level since 2012 at 2% year-over-year. The chart puts it in context though, since this level still remains tame relative to history. On the other hand, the measure has now reached the Fed's target which should increase the odds that the Fed continues with their plan to raise interest rates two more times in 2018. The market raised the odds of a hike to over 77% on September 26 after the PCE was released last week. Stocks could see increased volatility if the Fed remains steadfast in their plans and the global economy loses additional momentum.

Week in Preview:

- Geopolitics: Global trade disputes likely to continue to generate headlines. U.S. tariffs against China totaling $34 billion are set to begin on Friday. China has threatened to retaliate with tariffs of a similar size.
- U.S. calendar is busy despite the markets being closed for Independence Day and closing early on July 3. June ISM Manufacturing and auto sales should give a read on the momentum of the U.S. economy. The week ends with the June monthly payrolls report: expected to add 195k jobs and unemployment to hold steady at 3.8%. Wages will be watched closely after the recent pick-up in inflation. Despite a reduction to 2.0% in the reading for 1Q GDP, growth continues to look strong in 2Q. The Atlanta and NY Fed estimates of 2Q GDP are at 3.834% and 2.79% respectively.
- The Federal Reserve releases the minutes from the June meeting where the policy rates were hiked by 0.25%. Investors will be looking for more clues as to the pace and timing of future hikes. See the **Chart of the Week** for more on inflation, Fed policy and possible market reaction.
- Eurozone expects May unemployment to hold steady at 8.5%. The U.K. reports June PMI data.
- Asia data: Japan has June PMI services and composite. The 2Q Tankan survey continued to show a good outlook for manufacturing. Chinese June Caixin Manufacturing PMI came in slightly lower than May.
- The central banks of Australia, Sweden, Romania and Sri Lanka are scheduled to meet with all expected to hold policy rates steady. Romania may surprise the markets with a hike though.

Week in Review:

- The Fed released part two of the bank stress tests. Despite some headlines about a few firms having challenges, the Fed approved the plans to return more capital than last year to shareholders via dividends and share buybacks. Financials rallied post-results, but gave back the gains in the declines on Friday.
- The Chinese yuan has been noticeably weak versus the U.S. dollar since mid-April, but the declines have accelerated since mid-June. Chinese stocks also saw steep declines both last week and for 2Q. The Shanghai composite was down over 3% last week and over 14% for 2Q in U.S. dollar terms.
- While stocks were generally lower globally last week, 2Q saw strong returns in the U.S. – particularly in small caps, energy, commodities and REITs. S&P 500 earnings estimates rose during 2Q. EM stocks were weak in 2Q, while developed were higher in local currency but lower in U.S. dollar terms. In fact, currency-hedged Europe outperformed the S&P 500 in Q2. The 10-year U.S. Treasury yield moved lower to 2.86% and the yield curve continued to flatten, falling to the flattest level since the Great Recession.