This Week in the Market
8-5-19

Fed Must Go Further

In a wild week of trading, the S&P 500 finished just below where it started. Monday's Yuan devaluation sent stocks reeling for a moment, but buyers quickly returned as the currency stabilized. Trade rhetoric was certainly intense this week, but for all the noise, equities look like they are on good footing. Investor sentiment is starting to look washed out with the put/call ratio just below the 95th percentile. Technically, stocks have been driven lower, but breadth has not been extremely weak and there are pockets of the market still working. We could see some further consolidation in the coming days and weeks, but right now the range between the 50 and 200 day moving averages appears to be home. We'll need a catalyst to move us out of this range one way or the other.

The Chinese retaliated to President Trump's threat of 10% tariffs on the remaining $300 billion of Chinese imports by allowing their currency to weaken substantially and by halting the purchase of U.S. agricultural products. Initially, the equity market viewed this as a harsh reaction, but as currency stabilized it became clear that there are limitations on how far the Chinese are willing to let it go. Still, investors flocked to treasuries across the curve as inflation expectations fell, global sovereign yields tumbled, and a safety trade emerged. This move lower in bond yields hasn't reversed itself to the extent the equity market has recovered. This could be taken as a sign the Fed has a lot more work to do.

One thing that is for certain as the trade war intensifies, is that the pressure on the Fed to continue their cuts is being amped up. President Trump is going after China and it doesn't look like he plans on caving any time soon. The public and oddly enough both political parties are standing behind this fight, to a degree, and this is giving Trump cover to press forward. The farmers are hurting and manufacturing is softening, but the trade fight has had little impact on the consumer and most economic data points are on a solid trajectory, all things considered. If this changes, then Trump may alter his strategy, but right now the responsibility of cushioning any potential blow to the economy is shifting firmly back to the Fed. In the coming weeks, the equity market is going to look to the Fed to start telegraphing multiple rate cuts in the remainder of the year. To the extent the Fed delivers, the market can go higher and vice versa.

Even with the rhetoric dominating the headlines, there are pockets of the equity market doing quite well. Homebuilders are enjoying lower rates, software and proprietary data companies are generally unburdened by tariffs, and stocks levered to domestic consumers remain on track. On the flip side, industrial, bank, and energy companies are cracking. Trade is hurting the industrial sector, rates are hurting the banks, and increasing supply and decreasing demand is weighing on the oil patch. There are winners and losers to be found as we continue to navigate through this market.

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S&P 500: Standard & Poor's (S&P) 500 Index. The S&P 500 Index is an unmanaged, capitalization-weighted index designed to measure the performance of the broad U.S. economy through changes in the aggregate market value of 500 stocks representing all major industries.