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Stone Investment Partners LLC

Stone's Weekly Market Guide - Week of May 20, 2018

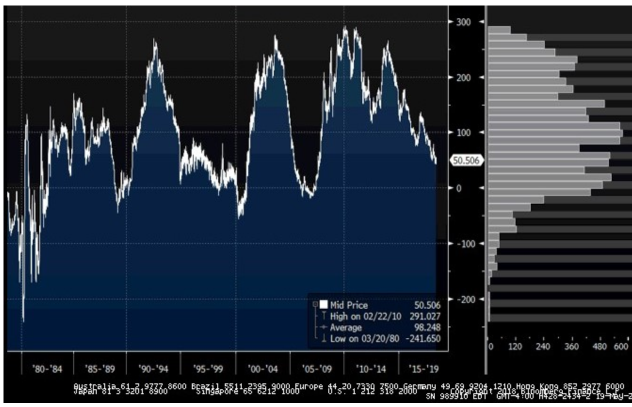

Chart of the Week: Some have expressed concern about the flattening of the yield curve and implications for U.S. growth. While it is true that the yield curve has a track record of predicting recession better than any economist I can name, this chart shows that the spread between the U.S. 10 and 2-year yield remains at a very normal level historically. The inversion (2 year > 10 year yield) of the yield curve in 1978, 1980, 1989, 2000 and 2006 correctly predicted recessions on average of about one and a half years later. The curve steepened last week and data actually shows the U.S. economy strengthening.

Week in Preview:

- May PMI data on Wednesday provides a reading on global economic strength: U.S. Manufacturing PMI is expected to hold steady at an elevated 56.5 while Europe eases to 56.0 from 56.2 and Japan could fade a bit from its 53.8 reading in April. Readings should be consistent with some cooling in economic activity outside the U.S. Recall that readings above 50 are generally consistent with growth.
- U.S. data includes: April new and existing home sales are expected to decline slightly month-over-month. Durable goods orders for April are expected to decline, but removing the volatile transportation component reveals an improving trend expected for the month. Plenty of Fedspeak along with the FOMC minutes for the bond market to monitor. Markets are currently pricing in a 100% chance of a Fed hike in June.
- Eurozone data: May IFO surveys for Germany are the main forward-looking indicator likely reflecting a modest decline in business climate, expectations and current assessment. Lots of ECBspeak and BOEspeak with Bank of England Governor Carney scheduled. U.K. has April inflation (CPI) and retail sales data. CPI is expected to decelerate for the month, while retail sales should firm. Brexit negotiations continue with a main focus in the Irish border.
- Central banks of Ghana, Hungary, Nigeria, Argentina, South Korea, Ukraine and South Africa are expected to meet. Ghana is expected to lower rates by 1 percentage point to 17% while the remainder are forecast to hold policy rates steady.
- Venezuela held presidential elections over the weekend with current President Maduro being re-elected as widely expected. His re-election came despite an epic economic collapse and inflation running at 16,422% annually (according to the Bloomberg Café Con Leche index as Venezuela publishes little reliable economic data). Voter turnout was suppressed by the jailing of major opposition candidates, so the country is likely to remain under significant economic and political stress.

Week in Review:

- Estimates of U.S. economic growth in 2Q rose modestly with both the Atlanta and NY Fed estimates for 2Q increasing to 4.129% and 3.20% respectively. April retail sales met expectations, but previous data was revised higher. April industrial production surprised to the upside along with a positive revision.
- Japan's streak of economic growth was stopped at 8 quarters with 1Q GDP declining by -0.6% annualized. Still would not forecast a move to recession in Japan as global growth is likely to help them rebound.
- Despite the S&P 500 being lower, the winners were small-cap stocks and the value factor with most implementations posting gains for the week. With the 10-year Treasury yield moving decisively above 3%, interest rate sensitive S&P 500 sectors (utilities and REITs) were taken to the woodshed.