

# Weekly Markets Commentary

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## To What Extent Can Policy Changes Impact Slowing Economic Growth?

Fear of a worsening global economic slowdown dragged bond yields sharply lower last week. The yield on the ten-year Treasury note plunged 20 basis points to 1.55 percent (a basis point is 1/100<sup>th</sup> of a percent), briefly causing an inversion of the yield curve between the two and ten-year maturities. Since the administration’s Aug. 1 announcement of another possible round of 10 percent tariffs on Chinese imports, the yield has collapsed by an extraordinary 46 basis points. Also last week, the yield on the thirty-year bond fell to an all-time low of 1.97 percent, down from 2.53 percent at the beginning of the month.

Stocks were also under pressure once again last week. The S&P 500 fell 1 percent, its third consecutive weekly decline, leaving the index 4.5 percent below its July 26 peak. The MSCI All Country World Ex-US index fell 1.5 percent. It was that index’s fourth straight weekly decline, leaving it lower by 7.4 percent since July 4.

There was some stabilization in both markets toward the week’s end on rising optimism that the global policy response will come to the rescue. European Central Bank (ECB) member and Finnish central banker Olli Rehn hinted at a substantial stimulus package from the ECB in September. And on Sunday, German Finance Minister Olaf Scholz said that Germany could marshal up to \$55 billion in fiscal stimulus if needed. This week it will be the Federal Reserve’s turn to weigh-in on policy at its annual conference at Jackson Hole.

### *Can Policy Changes Impact Slowing Growth? The Answer Remains to Be Seen*

Exactly what the necessary policy response to slowing growth should be is not completely clear. It seems a stretch to point to interest rates as an impediment to growth, raising questions about the efficacy of pushing them ever lower. Fiscal stimulus could certainly help, especially if targeted at long neglected infrastructure improvements. But the capacity, and political will for such spending is uneven at best around the globe.

In the meantime, the trade war continues to inflict damage on the global industrial economy, while in the U.S. the relative strength of the consumer sector provides the cover to continue its prosecution. Last week, U.S. retail sales in July were far stronger than expected, while headline inflation remained subdued at 1.8 percent year-over-year. And lower interest rates have led to a surge in mortgage refinancing, putting even more money into consumer pockets.

### *Consumers Remain in a Strong Position Across the Globe*

Some of this same dichotomy can be seen elsewhere. In the Eurozone, the slowdown in industrial production has been particularly pronounced, but consumers are faring relatively better. Job growth has remained steady, and the PMI for services has consistently outpaced manufacturing. The same has been generally true even in Germany, which last week reported a contraction in second quarter GDP. The U.K. has also reported some surprising recent strength in retail sales. It is a similar story in Japan. In China, however, both industrial production and retail sales continue to slow despite an already robust policy response.

The obvious policy response to the global slowdown is a resolution of the U.S.-China trade war. And the president's decision last week to delay the imposition of certain new tariffs until Dec. 15 was seen by some as a weakening of the administration's resolve, although that remains to be seen. But just where the trade war goes from here is anyone's guess.

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