Source: Bloomberg, Avalon Advisors, LLC

Chart of the Week: WTI crude is down almost 30% since the S&P 500 peaked on September 20. The S&P 500 has re-visited its late October lows and is now about 10% off the peak, while energy stocks have faired worse and are down almost 15% since September 20. The energy sector is currently only about 5.5% of the S&P 500, so it doesn't have an outsized impact on the overall stock market. Within the high yield (HY) bond market, energy is more meaningful at about 15% of the Bloomberg Barclays HY index. HY energy bonds are down almost 5.5%, while the HY index is down almost 3% since stocks peaked. Stock volatility has normalized as yields have risen and become a better competitor with stocks. 52 days in 2018 have seen +/- 1% moves in the S&P 500 versus the average of 53 since 1960, but only eight days in 2017. Fears of a policy error by the Fed and the impact of trade policies have caused worries about the future path of the global economy.

WEEK IN PREVIEW

- Geopolitical: Markets will continue to watch for additional trade news as usual. President Trump and Chinese president Xi are scheduled to meet to talk trade at the G-20 Leaders' Summit. At the European Union summit on Sunday the Brexit deal with the U.K. was approved, but it must still be approved by the British parliament.
- U.S.: October personal income should accelerate while spending holds steady. October housing data is on tap with new home sales and pending sales expected to improve. The second reading of 3Q GDP should be revised slightly higher to 3.6%. 4Q GDP estimates from the Atlanta and New York Fed are 2.49% and 2.51%. Holiday sales seem likely to support consumer spending and GDP growth with the National Retail Federation expecting growth of as much as 4.8% over 2017.
- Fedspeak: There are several Fed speaking events, but Vice Chair Clarida and Chair Powell will be most closely listened to by investors. Federal Open Market Committee minutes are also released on Thursday. While a December hike is almost a sure thing, markets would be relieved to hear more flexibility around future hikes as a policy error from too aggressive tightening is feared.
- Europe: The Eurozone October unemployment should improve to 8.0%. November consumer inflation is expected to fall to 2.0% year-over-year while core remains at 1.1%. Germany has the November IFO for a take on sentiment. U.K. releases their annual bank stress test results.
- Asia: Japan's October jobs data should continue to indicate a tight labor market with unemployment at 2.3%. Industrial production for October should reflect a significant rebound from weak September levels. November PMI data from China expected to hold fairly steady with all readings above the growth/contraction level of 50.
- The central banks of Israel, Ghana, Kenya, Guatemala, South Korea, Bulgaria, Dominican Republic and Angola will meet, with almost all expected to hold their policy rates steady. South Korea is a toss-up with a 0.25% hike possible.

WEEK IN REVIEW

- Ugly week with the S&P 500 declining almost 3.8% and essentially re-visiting the recent lows of late October along with erasing essentially all the 2018 total returns. As noted in the **Chart of the Week**, WTI oil was very weak and declined over 11% with energy stocks declining more than 5%. Oil's decline has also fed into the fear of a significant economic slowdown, but our view is that this is more of a supply issue rather than a significant decline in demand due to economic woes. Technology and price momentum stocks were also particularly weak. Small cap stocks outperformed with the Russell 2000 down about 2.5%. The 10-year U.S. Treasury yield fell to 3.04%.
- Both developed international and emerging market stock indexes were lower, but significantly outperformed the U.S. performance. The U.S. dollar was stronger which hurt non-hedged returns from international stocks, but international outperformed in any case. Japanese stocks were a standout and declined only fractionally.
- The 10-2 yield curve flattened slightly and ended at 22.5 basis points, and our other curve measure of three month six quarters forward – three-month yield narrowed to 54.4 basis points. The yield curve has historically provided an accurate forecast of future recessions when the difference in these measures turns negative. Yield curves are one of the major indicators that we monitor to judge recession risk.
- November PMI confirmed some deceleration in global economic growth but indicates that U.S. growth remains very good. U.S. Markit manufacturing PMI declined to a still robust 55.4 from 55.7. Eurozone manufacturing PMI fell to 51.5 from 52.0 with Germany down to 51.6 from 52.2. Japanese manufacturing PMI declined to 51.8 from 52.9.

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DISCLOSURES

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