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Buyback Derangement Syndrome

By Clifford Asness
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English

Share buybacks are when a company purchases its own common shares on the open market. After a buyback, a company is left with less cash and fewer shares outstanding. Buybacks, along with ordinary dividends, are one of the main ways companies return cash to investors -- the ultimate objective of any investment. So why have buybacks become the subject of vitriolic criticism? Prominent publications have run headlines calling buybacks, among other things, a "scam" that is "killing the American economy" and asserting that they "loot the future."

These attacks are mostly empty. The criticism is typically linked to debates about inequality and corporate short-termism but it also comes from virtue-signaling CEOs who want people to think they care about the long term. These attacks are growing in frequency, prominence and intensity. A lot of people are suffering from buyback derangement syndrome.

The lead accusation against buybacks is that they "starve investment." We can look at aggregate investment directly, examining the investing section of the statement of cash flows for all companies in the Russell 3000. Normalized by either total assets or total market capitalization (debt plus equity), net investment is lower than it was in the 1990s but positive and much higher than during the 2008 financial crisis. Yet the lack of a precipitous decline in investment doesn't stop critics from complaining about "investmentless growth."

Related to the claims of starving investment, some argue that today's buybacks are a form of "self-liquidation" in which companies are systematically shrinking away. This ignores that there are other sources of funds aside from common stock. Over the past few years the net cash outflow from share buybacks has been more than replaced by cash inflow due to new borrowing (think of this as a debt-for-equity swap). Despite buybacks, on net companies have been raising money, not liquidating.

It would strike a financial economist as odd to believe that investment is being curtailed by financing decisions like whether to repurchase shares or issue debt. Basic financial theory says any profitable (above the cost of capital) investment should be undertaken, with financing done at the lowest cost of capital. Whether this holds true is difficult to test, given all the possible counterfactuals. But there is, again, not much in the data to suggest any obvious failure of theory. If investment had truly fallen off a cliff along with the rise in buybacks, we'd at least have to worry about causality. It didn't happen.

Further, investors generally do not spend the money paid out in buybacks on champagne bubble baths or other forms of consumption. Rather, they reinvest it in other stocks and bonds. Buybacks thus facilitate a movement of capital from companies that don't need it to those that do. That's how markets are supposed to work.

Another criticism is buybacks "artificially" raise earnings per share. This is certain only if the rest of a repurchasing company's business is unchanged and the cash used for the buyback was completely idle. Otherwise, the true long-term effect on EPS growth will be determined by the return to the company had it retained and employed the cash. Again, this is how it's supposed to work. If the returns to a company using the cash for a buyback are low, the company is supposed to give the cash back.

Yet another claim is that much of the market rise over the last few years has been from buybacks. The numbers don't bear this out. The direction is plausible, as researchers have found that share prices do tend to increase --

by around 1% -- when buybacks are announced. Several explanations have been offered for this positive reaction including that investors see repurchases as a signal that management thinks shares are undervalued, and that investors cheer when management returns cash to shareholders rather than, perhaps, wasting it on "empire building." These explanations are behavioral effects at the margin.

But critics often assume that shareholders moving cash from the corporate balance sheet to their personal one is a pure windfall -- never mind that they own the same set of assets before and after, and you can't loot yourself. It would be impossible to determine precisely how much of the more than 15% annual returns on the Russell 3000 since the financial crisis is a direct consequence of share repurchases, but there is no compelling evidence that it is more than a small fraction.

The most wild-eyed critics actually claim that some specific companies are giant "scams" fueled by buybacks. Apple is the most notable target of these critics, who assert that much of its approximately $1 trillion market capitalization is an illusory artifact of share repurchases. That's backward. Buybacks reduce market capitalization. Remember, buybacks are also accused of causing the **stock market** to "self-liquidate." What Apple is accused of is a contradiction in terms -- self-liquidating to $1 trillion. Oh, and they sold some iPhones along the way, too.

While not the main focus of the critics, there are some possible problems with buybacks. If taken to excess far beyond today's levels and financed with debt, they could lead to too much leverage (aggregate leverage today is pretty normal). Moreover, there may be ways in which corporate management can use share buybacks tactically to increase the value of stock options and other incentive contracts at particular times. This can and should be fixed with contracts written to adjust for the impact of buybacks, not by eliminating the benign buybacks themselves.

The bottom line is that despite a legion of attempts, there is no real case against buybacks, let alone enough to blame them for all sorts of economic ills. Much of the criticism is innumerate nonsense. Nonetheless, the various charges are repeatedly made in otherwise reputable places, with increasing stridency, by people who should know better to people who presumably don't. That suggests the attack on buybacks is a politically motivated crusade -- let's blame public corporations for all kinds of evil. Americans have lots to debate, and those critical of public corporations likely have many other worthwhile points to make. They should drop nefarious buybacks from their retinue of accusations and focus on real problems.

Mr. Asness is managing and founding principal of AQR Capital Management. This article is based on research he conducted with Todd Hazelkorn and Scott Richardson, also of AQR.

(See related letters: "Letters to the Editor: Buybacks May or May Not Be the Best Thing" -- WSJ Aug. 25, 2018)

(See related letter: "Letters to the Editor: Does a Built-In Bias Cloud Some Buyback Decisions?" -- WSJ September 11, 2018)

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THE WALL STREET JOURNAL.

Economy

On Turkey, Another Step in the Weaponization of Global Finance; U.S. tariffs intensify pressure on the Turkish lira, raising prospect of an open-ended cycle of protectionism and devaluation

By Greg Ip
1,002 words
15 August 2018
08:56 AM
The Wall Street Journal Online
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English

Trade wars may be morphing into something more dangerous: financial wars.

With Turkey facing a currency crisis, President Trump last week poured fuel on the fire by doubling tariffs on imports of its steel and aluminum to offset the effects of its weaker currency or force the country to release an American pastor. (Mr. Trump's motive remains unclear.)

In the hierarchy of things afflicting Turkey, this isn't that high: The country's problems are mostly self-inflicted, from its large current-account deficit and steep dollar debts to the politicization of its central bank.

But it is the latest example of how the U.S. and other countries are weaponizing international finance in ways that could destabilize the global economy and fray the intricate web of relationships that sustain it.

While trade wars aren't good for growth, rarely do they induce a recession, or even a noticeable slowdown. The infamous Smoot-Hawley tariff of 1930 was at most a minor contribution to the Great Depression. By contrast, there's a long record of international financial disruptions fueling economic stress, from the Depression to the bankruptcy of Lehman Brothers nearly 10 years ago.

The origins of such crises usually lie in private-sector excess (lending too much to risky countries or home buyers), but the catalyst is often government policy somewhere: France's hoarding of gold helped precipitate the Depression, while then-Federal Reserve Chairman Paul Volcker's determination to slay inflation triggered the Latin American debt crisis of the 1980s.

The U.S. government has long seen it in the country's long-term interest to tamp down crises abroad. It came to Mexico's aid in 1982 and 1995, and worked with the International Monetary Fund in 1997 to contain the Asian financial crisis. In 2008, the Fed assisted foreign central banks in propping up banks in their countries that were hit by the mortgage crisis.

When the U.S. deliberately inflicts economic pain it is typically for geostrategic reasons and, where possible, it acts in concert with allies. In recent years, Washington has exacted enormous damage on North Korea and Iran by cutting them off from the dollar-based banking system. European and U.S. sanctions on Russia for invading Ukraine, interfering with U.S. elections and poisoning a former Russian spy and his daughter living in Britain have wrought havoc on the Russian economy.

Mr. Trump's deployment of financial warfare against Turkey breaks with tradition in several key ways.

First, while relations between Turkey's increasingly autocratic President Recep Tayyip Erdogan and the West have been deteriorating for years, his recent transgressions—such as detaining pastor Andrew Brunson—aren't the sort of threat to the U.S. or its allies' security that typically draws such a response.

"Geostrategically, it's insanity" to react so harshly, said Benn Steil, an expert on sanctions at the Council on Foreign Relations. "Turkey has, since the end of the Second World War, been a vital U.S. interest because of its geographical position." The country remains a member of the North Atlantic Treaty Organization and a key partner in managing the crisis in Syria and the flow of refugees to Europe.

Second, using tariffs to neutralize the Turkish lira's decline, like Mr. Trump's increasing tariffs on China because it let the yuan drop, could aggravate instead of mitigate financial turmoil. Currencies respond to the relative performance of economic growth, interest rates, inflation and trade balances. The dollar is rising now because the U.S. economy is strong, capital is flowing in and interest rates are going up, which means the U.S. trade deficit should widen. The lira is falling because capital is fleeing, interest rates are too low and Turkey's trade deficit needs to shrink. Mr. Trump is effectively trying to short-circuit this adjustment. But by undermining Turkish and Chinese growth, his tariffs have intensified downward pressure on those countries' currencies against the dollar. It raises the prospect of an open-ended cycle of protectionism and devaluation.

For now, a global meltdown looks unlikely. Few markets share Turkey's vulnerabilities, and global banks are relatively insulated from foreign defaults. But Washington's willingness to stand by or even pile on in a crisis is a new factor to consider for investors deciding whether to flee when another country gets into trouble.

Mr. Trump tends to see other countries' economic suffering as an advantage for the U.S., boasting earlier this month that his tariffs had helped tank the Chinese **stock market**. Thus, he is likely to repeat the exercise, and others will follow suit. Last week, Saudi Arabia retaliated against Canadian criticism of its human-rights record by freezing trade and dumping Canadian bonds, a move the U.S. declined to criticize.

Just as the size of the U.S. market gives Mr. Trump the advantage in any trade dispute, America's control over dollar-based banking and the depth of the Treasury market give it the advantage in any financial conflict. Any country, including China, that threatens to dump U.S. securities would hurt itself more than it hurts the U.S. Yet if relations deteriorate further, such tactics would no longer be off limits.

And in financial wars, like trade wars, the "winners" pay a price. If crises hit emerging economies, they'll buy less from the U.S. A Chinese slowdown and bungled devaluation in 2015 hurt commodity prices and the U.S. oil patch. And just as trade wars force other countries to seek alternatives to U.S. suppliers and customers, financial wars will encourage them to seek alternatives to the dollar. In both cases, the result will be a less integrated world and diminished American influence.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

Adidas Is Looking Fitter Than Nike; The German sportswear giant trades at an unjustified stock-market discount to its U.S. rival

By Stephen Wilmot
398 words
9 August 2018
10:41 AM
The Wall Street Journal Online
WSJO
English

With its T-shirt wearing tech billionaires and health-conscious consumers, the U.S. is the spiritual home of the global sporting goods boom. But the fitter of the two sportswear giants feeding those consumers just now is European.

Adidas grew sales by 10% year over year in the quarter through June, according to results published Thursday. That included 16% growth in North America and 27% growth in China. Nike's recent return to growth in the U.S. doesn't seem to be tripping up its German rival. Of the major markets, only Western Europe was flat after some new products didn't hit the mark.

Investors were worried that Adidas needed a breather after constant-currency growth of 18% in 2016 and 17% in 2017, which was partly driven by a craze for its Stan Smith sneakers. But the slowdown hasn't been as dramatic as some feared. The stock leapt almost 9% in morning trading.

Arguably even better news was that Adidas isn't resorting to discounts to keep its top-line growth pumping. Despite the dollar's strength, which pushes up sourcing costs, the company's gross margin--the amount it keeps after paying suppliers for the raw goods--rose to 52.3%, from 50.1% a year before.

The key to such margin gains is selling shoes at full price. This should continue, given the company's tight inventory position. Despite double-digit sales growth, the value of inventories ended the quarter 2% lower than a year before (at constant currencies).

It is hard to justify why Adidas shares trade at a discount to Nike's, which have shot higher as evidence of a U.S. turnaround has emerged. Adidas is growing sales and profits faster than Nike, yet even after today's share-price jump the German stock trades on 23 times prospective earnings, compared with 29 times for Nike. Adidas isn't facing potentially costly questions from the #MeToo movement either; its U.S. rival last month announced pay adjustments for 10% of its global staff following an executive purge.

It's getting harder to find discount Adidas sneakers. Bargain hunters should consider its stock instead.

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THE WALL STREET JOURNAL.

Markets

Hartford Financial to Buy Insurance Underwriter Navigators for $2.1 Billion; Insurer expects the purchase to add to its earnings starting in 2019

By Kimberly Chin
407 words
22 August 2018
04:26 PM
The Wall Street Journal Online
WSJO
English

Hartford Financial Services Group Inc. agreed to buy insurance underwriter Navigators Group Inc. for $2.1 billion, as the firm looks to specialty lines of business for growth.

The purchase of Navigators, which will bring its global marine, construction and energy liability lines of business to Hartford, comes less than a year after the company agreed to acquire an Aetna Inc. unit that provides insurance products to U.S. employers' benefits programs.

Insurers such as Hartford have been under significant pressure in recent years, with many choosing to either become leaner organizations or find transactions to improve their bottom lines. A decade of ultralow interest rates hurt insurance companies' ability to earn interest income on premiums they receive.

The Hartford, Conn., insurance company was also hard hit during the financial crisis when it had to take $3.4 billion in U.S. government aid, which it has since repaid. The firm was particularly vulnerable due to its long market-leading position in sales of a **stock-market**-linked retirement-income product that proved riskier than anticipated.

Shares in Hartford fell 4.2% to $50.16 in Wednesday trading, while shares in Navigators rose 8.8% to $69.90.

Wells Fargo analyst Elyse Greenspan said in a note that Hartford shares were likely to trade lower as some investors express doubt the deal will result in earnings growth over time. "For HIG, shareholders had hoped for capital return as opposed to M&A," Ms. Greenspan said.

During a second-quarter earnings call last month, Hartford Chief Executive Christopher Swift said the company was seeking deals in commercial specialty lines and industry verticals. He previously said Hartford was targeting deals in the $1 billion-to-$2 billion range.

In the deal announced Wednesday, Navigators shareholders would receive $70 a share in cash, an 8.9% premium to Tuesday's closing price.

Hartford expects the purchase to add to its profits starting in 2019 and $200 million to annual core profits over four to five years.

Stamford, Conn.-based Navigators, founded in 1974, also serves the U.S. excess casualty and surplus insurance markets. It has 820 employees at 22 locations in the U.S. and eight locations internationally.

Bowdeya Tweh contributed to this article.

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THE WALL STREET JOURNAL.

US

Cut Income Taxes or Kill Them? Connecticut GOP Candidates for Governor Disagree; Republicans hope to recapture the governor's seat after eight years of Democratic control

By Joseph De Avila
506 words
8 August 2018
06:19 PM
The Wall Street Journal Online
WSJO
English

The five Republicans in Connecticut's gubernatorial primary agree on most things, except when it comes to state income tax.

During a final televised debate Wednesday, candidates Bob Stefanowski, a former business executive, and Mark Boughton, mayor of Danbury, defended their proposals to eliminate the state's income tax. Steve Obsitnik, a technology entrepreneur, called the proposals "nonsense," while David Stemerman, a former hedge-fund manager, said the state needs a "realistic plan."

"You have a moral obligation to tell voters how to do it," said candidate Tim Herbst, the former first selectman of Trumbull. "They haven't told us how they would do it."

Mr. Stefanowski said the state could absorb the revenue loss of eliminating the state income tax, which was instituted in 1991, by cutting expenses and renegotiating contracts with state employees.

"The state lived perfectly fine without a state income tax," he said.

The five candidates will square off in the GOP primary Tuesday. The winner will face the victor of the Democratic primary, either Greenwich businessman Ned Lamont or Bridgeport Mayor Joe Ganim.

Republicans have a chance to win the governor's race in deep-blue Connecticut, thanks in large part to the unpopularity of current Gov. Dannel Malloy, a Democrat who declined to run for a third term. The Cook Political Report rates the race as a tossup.

Members of the GOP in the state are anxious to recapture the governor's seat after eight years of Democratic control that resulted in two income tax increases and other progressive policy changes, including new gun laws and the abolishment of the death penalty. Democrats hold a slim lead in the state's House of Representatives and are tied with Republicans in the Senate.

Other than tax policy, the candidates found broad agreement during the debate on local television station WFSB. All oppose highway tolls. They each said they would support whoever wins the primary. And each blamed the state's weak job market on what they said was a poor business and fiscal climate.

Mr. Obsitnik said the state has a "hostile environment" toward business. Mr. Stemerman said Connecticut can attract employers with good schools, low taxes and its competitive geographic location. Mr. Herbst said the state's "fiscal **volatility**" was making neighboring states like New York and Massachusetts more attractive for employers.

And Mr. Boughton, who was endorsed by the Connecticut Republican Party, said state government developed a reputation for being unfriendly to companies.

"When you have that reputation across the United States of America—and, really, across the globe—as being the place not to go, then obviously investment won't come here," Mr. Boughton said.

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* Connecticut's Democratic Candidates Spar Week Before Primary (Aug. 7)

* Connecticut Republicans Confronted With Choices (July 8)

* Connecticut Mayor, Businessman in Top Spots in Governor's Race, Poll Shows (May 7)

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THE WALL STREET JOURNAL.

Economy
U.S. Jobless Claims Rose Slightly Less Than Expected Last Week; Initial jobless claims, an indication of layoffs across the U.S., increased by 3,000 in the week ended Aug. 25

By Paul Kiernan and Josh Mitchell
266 words
30 August 2018
08:36 AM
The Wall Street Journal Online
WSJO
English

The number of U.S. workers filing new applications for unemployment benefits rose slightly last week after three straight weeks of decline, though a more stable measure of claims hit the lowest level in nearly five decades.

Initial jobless claims, an indication of layoffs across the U.S., increased by 3,000 to a seasonally adjusted 213,000 in the week ended Aug. 25, the Labor Department said Thursday.

Economists surveyed by The Wall Street Journal had forecast 215,000 new applications for unemployment benefits last week.

Jobless claims can be jumpy from week to week. The four-week moving average of claims, which smooths out weekly **volatility**, fell by 1,500 to 212,250, the lowest level since December of 1969, the Labor Department said.

Applications for jobless benefits have remained low by historical standards for years, reflecting the lowest unemployment rate in nearly two decades. Economists say a strong labor market is driving robust gains in consumer spending and broader economic growth.

Thursday's report also showed the number of continuing unemployment benefit claims—those drawn by workers for more than a week—fell by 20,000 to 1,708,000 in the week ended Aug. 18. Continuing claims are reported with a one-week lag.

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THE WALL STREET JOURNAL.

Economy

Global Economy Week Ahead: China Business-Activities Data Expected; U.S. also set to release data on retail sales, industrial production for July

By WSJ Staff
305 words
12 August 2018
03:00 PM
The Wall Street Journal Online
WSJO
English

The week ahead will feature business-activity data in China, economic growth figures in Germany and well as retail-sales and industrial-production numbers in the U.S.

Tuesday: China is going to release its monthly business-activities data. Investors will look for signs to see if the rising trade tensions between China and U.S. hurt business and consumer sentiment.

Germany's economy slowed sharply in the first three months of the year, thanks in large part to unusually cold weather, an outbreak of influenza and a series of strikes. But economists don't expect economic growth figures for the second quarter to be much better, reflecting worries about the trans-Atlantic trade relationship in Europe's export powerhouse. Forecasters expect to see annualized growth of around 1.6%, compared with 1.2% in the first quarter.

Wednesday: The Commerce Department releases July retail-sales data. Americans boosted their spending at retailers in June, capping a strong quarter of consumption that is expected to help ramp up economic growth. Economists will watch for continued strength in consumer spending, an engine of the economy.

The Federal Reserve releases data on U.S. industrial production for July. In June, this measure of output rose a seasonally adjusted 0.6% from the prior month. July's report will shed light on whether growth in the manufacturing sector continues.

Friday: Brazil's high political tension goes up a notch, as presidential candidates will be allowed to start campaigning for the October election. Markets are watching closely for hints on how poll leaders would handle a fiscal crisis threatening the nation's solvency, potentially leading to **volatility** in currency and stock markets.

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THE WALL STREET JOURNAL.

Politics

In Break From Precedent, Trump's Moves Aggravate Turkey's Currency Crisis, Rather Than Calm It; Some experts view the decision to hike tariffs as a response to the lira's devaluation

By Jacob M. Schlesinger
1,215 words
11 August 2018
12:00 PM
The Wall Street Journal Online
WSJO
English

WASHINGTON—President Trump's decision to double steel tariffs on Turkey as its government battled a currency collapse marked a departure for the U.S. from how it traditionally handles financial turmoil hitting emerging markets.

Washington has generally tried to calm global markets in such moments, especially when investors are gripped by fear of contagion. Mr. Trump instead squeezed Ankara further, raising tariffs on Turkish steel imports to 50% and aluminum to 20%, which deepened the Turkish lira's drop and worsened market fears that its banks could be shaken.

Administration officials didn't clarify Mr. Trump's motives. The move followed a series of actions the Trump administration has taken in recent weeks

to step up economic pressure on Turkish President Recep Tayyip Erdogan to release American evangelical pastor Andrew Brunson.

The doubled tariffs weren't related to Mr. Brunson, administration officials said Friday. White House spokeswoman Lindsay Walters said the tariffs were meant to protect the U.S. on national-security grounds, "independent of negotiations on trade or any other matter."

In a formal proclamation of the move issued Friday night—nearly 12 hours after the president first announced it on Twitter—the White House said the action was taken because the original global tariffs hadn't done as much as the administration had desired to boost domestic production of steel and aluminum. The statement didn't explain why Turkey alone was hit with the higher tariffs.

In his tweet, Mr. Trump seemed to link the tariffs to soured ties between the two nations, suggesting a willingness to impose trade sanctions as a lever in pursuit of unrelated U.S. diplomatic goals. A spokesman for the White House National Security Council said Friday that Turkey has "much to lose" in continuing to hold Mr. Brunson.

Mr. Trump may also have been seeking to insulate the U.S. from any trade advantage Turkey could exploit from the currency drop.

"I have just authorized a doubling of Tariffs on Steel and Aluminum with respect to Turkey as their currency, the Turkish Lira, slides rapidly downward against our very strong Dollar!," the president wrote a few minutes before 9 a.m. Friday after the lira had dropped 14% overnight against the dollar. "Our relations with Turkey are not good at this time!" he added.

Over three decades of periodic currency storms, such as the early 1990s Mexican peso plunge, and the Asian crisis a few years later, "the market's underlying assumption was that the U.S. would try to be helpful" during periods of extreme foreign-exchange **volatility**, said Shahab Jalinoos, head of global currency strategy at Credit Suisse Group. "Now the market can no longer assume that."

Foreign-exchange collapses can be perilous for emerging markets, particularly when they have borrowed heavily in dollars and thus find it harder to repay those debts as their own currencies fall.

White House and Treasury officials didn't respond to requests for comment about the administration's broader strategy toward global currency-market instability, or about the economic considerations behind the increased tariffs.

Under his "America First" platform, Mr. Trump has sought to reorient U.S. economic policies, breaking with a longstanding bipartisan consensus that Washington's mission was to take the lead in expanding, strengthening and stabilizing commercial and financial ties across countries—and that such globalization was broadly in America's self-interest, even if it might disadvantage some U.S. industries or communities.

Mr. Trump has challenged that orthodoxy, arguing that such policies have undermined American economic strength. He has revived long-dormant policies to block imports he considers threatening to the U.S., and brushed aside warnings that such moves could harm the global trading system. He has argued that the U.S. should do more to use its economic and financial clout to force other countries to change policies he considers unfair to the U.S.

The tariffs that Mr. Trump said he was doubling were imposed earlier this year, not just on Turkey but on virtually every metals exporter around the world. The administration imposed tariffs of 25% on steel and 10% on aluminum by invoking a little-used Cold War-era law that allows presidents to block imports he deems a threat to American "national security."

Mr. Trump's broad use of that power provoked outrage from trading partners around the world, who said it violated World Trade Organization limits on such unilateral trade curbs and hit allies who posed no threat to U.S. security. Turkey is an ally and member of the North Atlantic Treaty Organization.

Many countries retaliated with their own tariffs on U.S. exports. Among them was Turkey, which in June put import taxes on $1.8 billion worth of U.S. coal, paper, walnuts, tobacco and other products.

Mr. Trump's mention of the Turkish lira's plunge suggested a willingness to tolerate the currency's collapse.

Following Mr. Trump's tweet, the lira fell another 9% and then recovered some of its losses. Turkey's currency woes have stoked instability in other emerging markets such as South Africa, Hungary and Russia, as investors worry about similar fragility there. It also jolted European stocks and the euro, as investors focused on the possible costs to European banks holding Turkish debt.

"If a crisis were to emerge somewhere in the world with the possibility of contagion, what is President Trump's response going to be? Cooperation with the world and showing leadership? Or more tariffs?" said Chad Bown, a trade expert at the Peterson Institute for International Economics and a frequent critic of the administration's trade strategy. "This was not a good sign."

The Trump administration did in June agree to back a $50 billion International Monetary Fund bailout of Argentina at a time when many investors worried that country's woes could trigger broader regional or global instability.

Mr. Trump's tweet also suggests the possibility of new terrain for administration trade policy—the use of higher tariffs as a response to the weakening of a trading partner's currency.

Some traders and economists read Mr. Trump's statement as indicating that the higher tariffs were designed to offset the impact of the weaker lira, since the cheaper Turkish currency would make Turkish steel and aluminum exports cheaper when sold in the U.S., offsetting much of the intended impact of the tariffs.

Some free-trade critics have for years urged presidents to use tariffs as a weapon when exporters in other countries reap a windfall from currency devaluations. Prior administrations have resisted those demands, arguing such actions would be ineffective and would risk further destabilizing currency markets.

When the administration earlier this month said it was raising planned tariffs on $200 billion in Chinese imports to 25% from the original 10%, one reason given was the recent weakening of the Chinese yuan.

Daniel Kruger contributed to this article.

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How HUD Can Help The Housing Market

By Edward Pinto
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The Department of Housing and Urban Development announced Monday its intention to increase fair-housing opportunity by streamlining and enhancing the Obama-era Affirmatively Furthering Fair Housing rule. This newspaper reported HUD Secretary Ben Carson "plans to focus on restrictive zoning codes," as these have "limited home construction, thus driving up prices and making it more difficult for low-income families to afford homes."

But the federal government has limited control over state and local land-use policy. So what should HUD do to increase supply? Condition federal dollars on state and local policy changes. Start with zoning. Give back to property owners the right to build at higher densities. Create higher-density single-family and multifamily zoning where infrastructure is already in place. Add density bonuses for building near jobs. Replace static density requirements with equalized ones that take into account unit size. Thus if a 1,500-square-foot home is the maximum unit size that may be built at nine units an acre zoning density, a developer proposing to build 600-square-foot units would have a right to build 22 units an acre.

How about reducing development costs? Start with streamlining permitting processes and timelines. Eliminate or reduce off-street parking requirements. Offer property tax abatements, tax-increment financing and other incentives for building economically near service and line-production jobs without the use of housing subsidies. Adjust upfront impact fees -- charges in addition to property taxes for schools, parks, roads, sewers, water and police. Provide for code variance with waiver and modification procedures based on "good enough" and "substantial equivalence" standards. Allow an expedited appeal process for relief from code requirements.

As important, in administering HUD Mr. Carson has a statutory obligation to "further the policies" of the Fair Housing Act of 1968. That includes addressing the inflationary and pro-cyclical role federal credit easing has played during the current six-year housing price boom. When the inevitable reversion of real house prices to their trend growth path occurs, low-income and minority home buyers will again be subjected to more **volatility**, greater loss of equity, and higher rates of loan default.

Research by the American Enterprise Institute found that the prices for the bottom quartile of home sales -- largely composed of entry-level buyers -- were up 41% over five years, compared with 27% for the top half of home sales by price. We also found that house prices increased faster in census tracts with more risky mortgages.

While HUD should condition federal grant dollars on incentives created by state and local governments to increase supply, this will take many years to achieve the desired impact. In the meantime HUD should take immediate steps to slow the unsustainable home price boom that is being fueled by excessive leverage, almost all of which is provided by the Federal Housing Administration, or by Fannie Mae and Freddie Mac competing with the FHA.

There's plenty for Mr. Carson to do, and no time to waste.

Mr. Pinto is a co-director of the American Enterprise Institute's Center on Housing Markets and Finance.

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THE WALL STREET JOURNAL.

Business
Labor Unrest Strikes Mining Giants; Walkout at Alcoa-owned facilities in Australia follows unrest at sites including mines run by Glencore, BHP Billiton

By Rhiannon Hoyle
560 words
9 August 2018
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English

SYDNEY—Already grappling with challenges including U.S. tariffs and rising costs, global mining companies face another: worker walkouts.

In Australia, roughly 1,500 employees at alumina refineries and bauxite mines owned by Alcoa Corp., the largest U.S. aluminum maker, are striking over pay and working conditions. That follows labor unrest at sites including mines run by Glencore PLC in South Africa and BHP Billiton Ltd. in Chile.

Strikes stoke **volatility** in global commodity markets, affecting the prices of products from guitar strings to semiconductors. Copper is especially prone to wild swings, given that supply is typically in line with global demand. Loss of production from a megapit such as Escondida in Chile or Grasberg in Indonesia, both hit by long walkouts last year, can swing a tight market into a shortfall.

Rising labor costs also threaten mining giants' profits, just recovering from a deep downturn. Moody's Investors Service said if workers strike again at Escondida—they voted in favor of a walkout this month—it could lead to a material fall in the BHP-led venture's production and margins.

For the aluminum industry, the strikes in Australia are happening at an especially sensitive time.

Producers and buyers were early casualties of the Trump administration's aggressive trade policy, as the U.S. imposed a 10% tariff on imported aluminum earlier in the year. Alcoa, which cited tariffs in cutting its profit outlook last month, on Monday asked for an exemption from tariffs on aluminum imported from Canada.

The market has also been jolted this year by U.S. sanctions against Oleg Deripaska and his Rusal aluminum empire, and by higher electricity costs—aluminum production is energy-intensive—as oil and coal prices rise.

Alumina, produced from bauxite, is smelted to make aluminum. Alcoa's three refineries in Western Australia account for roughly 7% of global alumina supply, so the strike risks driving up prices, ultimately of the products from cars to beer cans that contain aluminum.

It is "a sufficiently large supply shock" to rattle the market, said Macquarie. Aluminum rose 3.3% on the London Metal Exchange on Wednesday to US$2,106 a metric ton. It surged as high as US$2,146 a ton intraday in Asia Thursday, its highest in more than a month.

In a statement, Alcoa said its operations in Western Australia, which employ about 3,750 people, are continuing to run as normal, and that it doesn't forecast reduced output.

"Our sites have contingency plans to ensure they can continue to operate during industrial action," said Alcoa. Still, it said the 1,500 union members are expected to remain on strike until Aug. 17 and vote on a new agreement later in the month. The two sides have been in wage talks for 18 months.

Alumina's price was already high before the strike, having risen about 35% in 2018, said Morgan Stanley analyst Susan Bates, an increase linked to earlier cuts at refineries in Brazil and China.

"Since alumina accounts for 40% of aluminum smelter cash costs, a price spike would be likely to put upward pressure on aluminum's price," Ms. Bates said.

Write to Rhiannon Hoyle at rhiannon.hoyle@wsj.com

Document WSJO000020180809ee89000rt

THE WALL STREET JOURNAL.
U.S. EDITION

Business News: Labor Unrest Hits Mining Firms --- Alcoa facilities face walkout in Australia; Glencore, BHP discord also disrupts markets

By Rhiannon Hoyle
558 words
10 August 2018
The Wall Street Journal
J
B6
English

SYDNEY -- Already grappling with challenges including U.S. tariffs and rising costs, global mining companies must now confront worker walkouts.

In Australia, roughly 1,500 employees at alumina refineries and bauxite mines owned by Alcoa Corp., the largest U.S. aluminum maker, are striking over pay and working conditions. That follows labor unrest at mines run by Glencore PLC in South Africa and BHP Billiton in Chile.

Strikes stoke **volatility** in global commodity markets, affecting the prices of products as diverse as guitar strings and semiconductors. Copper is especially prone to wild swings, given that supply is typically in line with global demand. Loss of production from a megapit such as Escondida in Chile or Grasberg in Indonesia, both hit by long walkouts last year, can swing a tight market into a shortfall.

Rising labor costs also threaten mining giants' profits, which are recovering from a deep downturn. Moody's Investors Service said if workers strike again at Escondida -- they voted in favor of a walkout this month -- it could lead to a material decline in the BHP-led venture's production and margins.

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THE WALL STREET JOURNAL.

Business

Low Meat Prices Cut Into Hormel, Sanderson Earnings; Executives say record production will rise higher as plants expand

By Jacob Bunge
590 words
23 August 2018
02:09 PM
The Wall Street Journal Online
WSJO
English

Pork and chicken supplies will continue to rise as U.S. processing plants expand, meat executives said, exacerbating near-record production and storage levels that have pushed down prices.

Hormel Foods Corp. on Thursday cut its sales forecast for this year as the Spam maker confronts lower pork prices, tariffs and rising freight costs. Sanderson Farms Inc. reported third-quarter profits of $11.5 million compared with $115.8 million a year earlier, far below analysts' expectations.

"Tariffs, freight, supply levels and demand have all created market **volatility**," said Jim Sheehan, Hormel's chief financial officer, on a conference call.

Hormel shares declined 3% on Thursday, while Sanderson's stock fell 2.9%.

Meatpackers are betting that continued growth in meat consumption in the U.S. and internationally will carry them through the current slump. Tougher U.S. trade policies have prompted tariffs this year on U.S.-produced meat in major markets like Mexico and China. Some companies are cutting prices to keep meat cuts moving despite such trade barriers, while supplies housed in U.S. cold-storage facilities are approaching record levels. Lean hog futures prices have dropped 26% so far this year at the Chicago Mercantile Exchange.

Huge new pork plants opening across the Midwest are competing for hogs and putting pressure on less efficient plants. Hormel said Thursday that it will sell a hog-processing plant in Nebraska to farmer-owned WholeStone Farms for $30 million.

WholeStone's plans to renovate the plant and add a second shift will boost output beyond the 10,500 hogs currently slaughtered there each day, Hormel Chief Executive Jim Snee said. He estimates those upgrades would have cost Hormel around $80 million.

WholeStone didn't respond to a request for comment.

The expanded plant will add to pork-industry capacity that has swelled 8% in the past two years, according to the National Pork Board. That figure is expected to rise further with the opening of another pork plant in Iowa in the months ahead.

Mississippi-based Sanderson, meanwhile, said it would move ahead with plans to open a new poultry plant in Texas in 2019 that will boost its processing capacity by 9%.

Chief executive Joe Sanderson said he expects demand for poultry will continue to grow, but said that high supplies and low prices for red meat this year have made it harder to get chicken featured in restaurants and grocery stores.

"I have never seen a scenario where beef and pork affected [chicken]," Mr. Sanderson said on a conference call. "I was wrong about that."

Mr. Snee said the deal to sell Hormel's pork plant, which includes a three-year commitment to supply pork to Hormel, will stabilize profit as the Austin, Minn.-based company works to rely less on selling cheaper, bulk meats.

Hormel's quarterly profit from non-branded, commodity pork dropped 88% from the same period last year. Stronger sales of the company's Natural Choice and Applegate brands helped to make up the difference.

Hormel's overall third-quarter profit rose 15% to $210.2 million, or 39 cents a share, in line with estimates from analysts polled by Thomson Reuters. The company reduced its full-year revenue guidance by $400 million at the midpoint to between $9.4 billion to $9.6 billion.

Kimberly Chin contributed to this article.

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Business News: Lower Meat Prices Pinch Hormel and Sanderson

By Jacob Bunge
467 words
24 August 2018
The Wall Street Journal
J
B3
English

Pork and chicken supplies will continue to rise as U.S. processing plants expand, meat executives said, exacerbating near-record production and storage levels that have pushed down prices.

Hormel Foods Corp. on Thursday cut its sales forecast for this year as the Spam maker confronts lower pork prices, tariffs and rising freight costs. Sanderson Farms Inc. reported third-quarter profit of $11.5 million compared with $115.8 million a year earlier, far below analysts' expectations.

"Tariffs, freight, supply levels and demand have all created market **volatility**," said Jim Sheehan, Hormel's chief financial officer, on a conference call.

Hormel shares declined 3.1% on Thursday, while Sanderson's stock fell 0.2%.

Meatpackers are betting that growth in consumption in the U.S. and internationally will carry them through the slump. Tougher U.S. trade policies have prompted tariffs on U.S.-produced meat in major markets like Mexico and China. Some companies are cutting prices, while supplies in U.S. facilities are approaching records. Lean hog futures prices have dropped 26% so far this year at the Chicago Mercantile Exchange.

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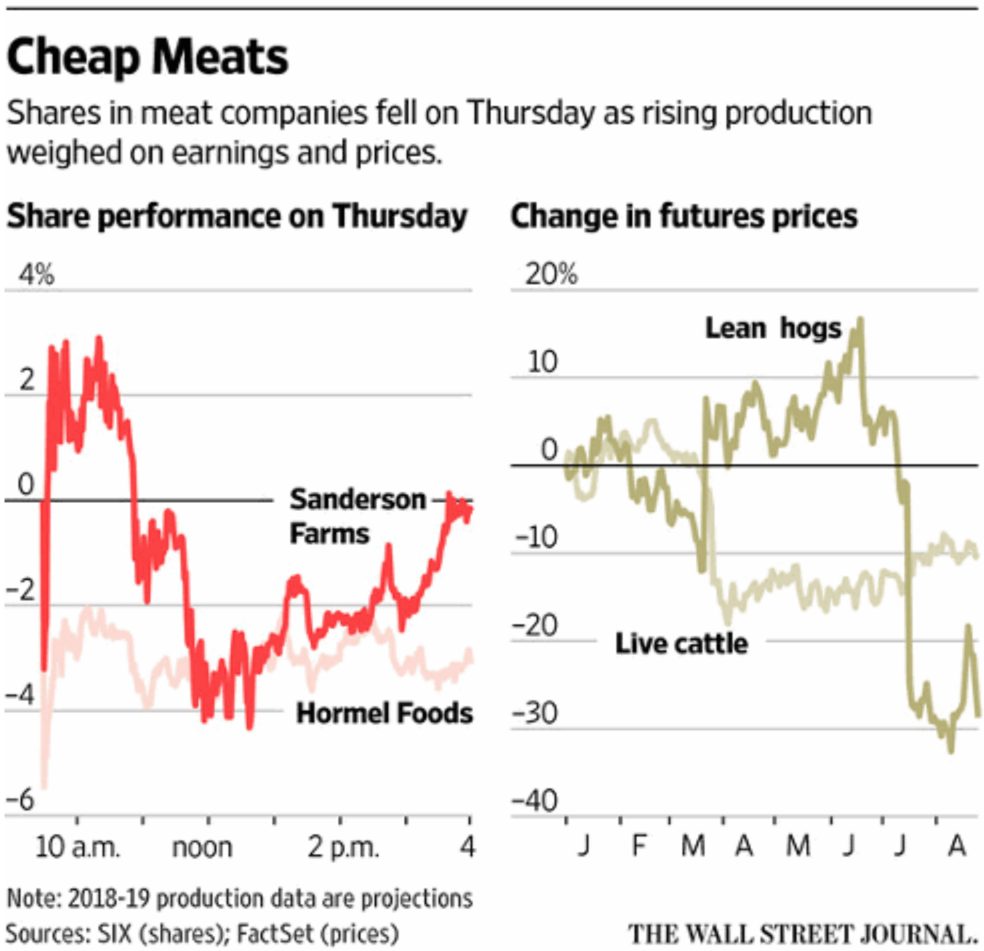
Kimberly Chin contributed to this article.



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THE WALL STREET JOURNAL.
U.S. EDITION

Tyson to Buy a Top Meat Supplier --- Keystone Foods deal aims to bolster sales to restaurants amid surge in production

By Jacob Bunge
681 words
21 August 2018
The Wall Street Journal
J
B1
English

Tyson Foods Inc. agreed to acquire a top meat supplier to McDonald's Corp. and other chains, in a bid to boost its sales to restaurants as rising supplies and tariffs squeeze U.S. meat companies.

Tyson said Monday it would pay $2.16 billion in cash for Keystone Foods, expanding the Springdale, Ark.-based company's business selling meat to fast-food chains and adding processing plants to its network in the U.S. and Asia.

The purchase aims to further shift Tyson's business toward higher-profit products, such as chicken nuggets and fish filets, and away from slabs of nonbranded, commodity meat that tend to be less profitable and prone to market swings.

"Particularly internationally, we see this as a tremendous platform to continue to grow," Tyson Chief Executive Tom Hayes said on a conference call. Tyson shares rose 1.6% to $63.40 on Monday, and have fallen 22% year to date.

Tyson, the largest U.S. meat supplier by sales, and competitors such as Pilgrim's Pride Corp. and Sanderson Farms Inc. are struggling as new pork and chicken plants lift U.S. meat production to a record. Analysts expect poultry and red meat in storage to hit a record this year at the same time major importers such as Mexico and China have raised tariffs on U.S.-produced meat products, driving down prices.

Over the past four years, Tyson has spent billions of dollars on deals for supermarket standbys such as Hillshire Farms lunch meat and Jimmy Dean sausages, as well as upstarts like the organic brand Smart Chicken. Those acquisitions were geared toward lifting the company's profit margins and insulating its sales from the type of commodity-market downdraft now vexing the U.S. meat sector. Still, Tyson last month lowered its profit forecast for the year, citing the effects of tariffs and "an oversupply of protein."

Keystone's business is weighted toward the U.S., where about two-thirds of its overall sales are generated, primarily supplying products such as chicken nuggets and fish filets to restaurants. In Asia, Keystone sells a wider range of meat products.

Supply deals with restaurant chains can be less profitable than distributing name-brand goods to grocery stores, but are generally very stable, according to analysts.

Mr. Hayes told investors that the deal would help reduce **volatility** in Tyson's chicken business, and that Tyson could improve Keystone's profit margin by cutting costs. Keystone also can provide Tyson a platform to make a fresh push into markets such as the Middle East, Africa and Europe, he said.

Tyson divested itself of many of its non-U.S. assets in recent years to focus on the U.S.

Some analysts have warned that another big deal could be risky for Tyson, depleting capital the company could spend buying back shares. Stewart Glendinning, Tyson's chief financial officer, said the company has recently succeeded at making big acquisitions and still repurchasing shares.

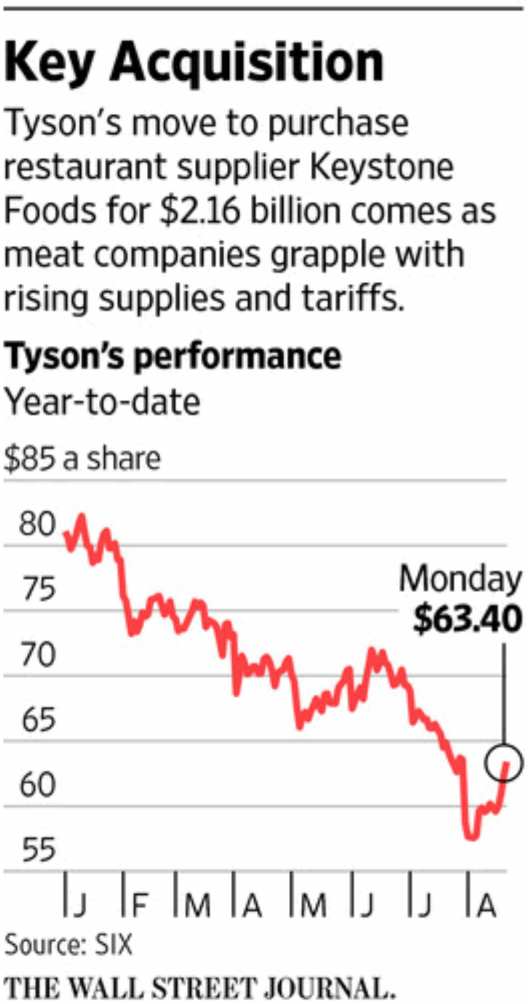
The deal to combine two major meat suppliers to restaurants will face regulatory reviews in the U.S., China and elsewhere. Mr. Hayes declined to say whether McDonald's or other Keystone clients blessed the deal, but said Tyson's customers have backed the company's overall strategy.

McDonald's declined to comment.

Tyson plans to finance Keystone's purchase from Marfrig Global Foods SA of Brazil with cash and new debt. For the year ended June 30, West Chester, Pa.-based Keystone generated annual sales of $2.5 billion and earnings before interest, taxes, depreciation and amortization of $211 million.

Marfrig, which reached a deal in 2010 to acquire Keystone, said earlier this year that it would sell the company. Marfrig this year became the world's second-largest beef processor -- after JBS SA of Brazil -- with its purchase of a majority stake in National Beef Packing Co.

Kimberly Chin contributed to this article.



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THE WALL STREET JOURNAL.

Markets

New Rules Look to Make Insurance Contracts More Transparent for Investors; Financial Accounting Standards Board changes to take effect in 2021

By Michael Rapoport
447 words
15 August 2018
10:00 AM
The Wall Street Journal Online
WSJO
English

Investors should see clearer and more up-to-date numbers about the financial health of U.S. life insurers under a long-planned set of changes to insurance accounting unveiled Wednesday, rule makers say.

The changes, which take effect in 2021, will affect the way companies value their long-term insurance contracts like life insurance, long-term care policies and annuities. They are intended to provide "increased transparency and better understanding of the economics," said James Kroeker, vice chairman of the Financial Accounting Standards Board, the panel that sets accounting rules for U.S. companies.

The idea, Mr. Kroeker said, is to make sure investors get the most current information on the contracts' value. Insurance contracts can extend over decades, but often the assumptions that governed their value at the outset—life expectancy and the costs of long-term care, to name a couple—aren't updated.

The contracts' value doesn't stay current until and unless they become unprofitable for the insurers, and then they suffer a big hit to their value all at once, potentially blindsiding investors. As a result, the investors may not have a fully accurate idea of how much those contracts are worth under current conditions, Mr. Kroeker said.

With the new changes, the FASB will require insurers to review at least annually the assumptions they use to measure the value of their insurance obligations and update them if necessary. Any changes in value that result would be included in the company's net income, which could add some **volatility** to insurers' earnings.

Insurers also will be required to use a standard discount rate to measure their liabilities. The rate will be pegged to the yield from high-quality bonds, which is lower than the discount rate many insurers use now—the rate they earn on their investment assets. A lower discount rate would increase the current value of the obligations on insurers' balance sheets.

Other changes include clearer, more streamlined accounting for the costs of acquiring new customers, known as deferred acquisition costs.

The changes have been in the works for more than a decade. The FASB proposed broader changes to insurance accounting in 2013, but insurance companies, investors and others urged the board to focus on targeted changes instead of overhauling the entire system of insurance-accounting rules.

The changes don't affect short-term insurance contracts such as auto and homeowners' insurance, which were the subject of their own series of changes in 2015, focusing on improved disclosure.

Write to Michael Rapoport at Michael.Rapoport@wsj.com

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WSJ PRO CENTRAL BANKING

Economy

Banks Reject Volcker Rule Changes | | Turkey's Red Flags Stand Out | Norway Flags Rate Rise | SEC Sends Subpoena to Tesla | Douglas's Take: U.K. Inflation May Be Cooling Faster Than BOE Thinks; The Wall Street Journal's central banking newsletter for Thursday, August 16, 2018

1,933 words
16 August 2018
05:28 AM
WSJ Pro Central Banking
RSTPROCB
English

Douglas's Take: U.K. Inflation May Be Cooling Faster Than BOE Thinks

Banks Say No Thanks to Volcker Rule Changes

Turkey's Economic Red Flags Stand Out Among Emerging Markets

Norges Bank Flags September Rate Rise

SEC Sends Subpoena to Tesla in Probe Over Musk Tweets

U.K. Inflation May Be Cooling Faster Than BOE Thinks

Inflation in the U.K. could reach the Bank of England's 2% annual target sooner than officials think.

The BOE raised its benchmark interest rate in August to 0.75% and signaled it expects a couple more quarter-point increases over the next three years to keep inflation in check. Assuming Britain sails out of the European Union as planned in March 2019 with minimal disruption, the forecast was for steady if unspectacular growth and mounting pressure on prices.

Taken at face value, figures published Wednesday by Britain's Office for National Statistics appeared to show persistent price pressures. Consumer price growth accelerated in July to 2.5% from 2.4% a month earlier, broadly in line with the central bank's expectations. Its latest forecasts suggest annual inflation will cool gradually over the next few years, drifting back to 2% around the end of 2020 or the beginning of 2021.

Yet a novel analysis by senior economist Jason Lennard at London's National Institute for Economic and Social Research points to a quicker return to target. He developed a "trimmed mean" gauge of underlying inflation in Britain that uses a similar methodology to the trimmed mean measure of U.S. inflation published by the Federal Reserve Bank of Dallas. In both cases, the gauge strips out the prices of the most **volatile** goods and services in an effort to give a truer picture of underlying inflationary forces.

Mr. Lennard's conclusion: In contrast to the headline rate, underlying annual inflation actually slowed in July, to 1%, compared with 1.2% in June. More prices decreased this July than in July the previous year, and fewer prices increased, his analysis shows.

That points to headline inflation of 2.1%—a hair above the BOE's target—by this time next year.

Key Developments Around the World

Banks Say No Thanks to Volcker Rule Changes

Trump-appointed financial regulators set out to ease the Volcker rule—a controversial postcrisis restriction for banks—and instead have drawn the industry's ire. Last week, lawyers representing JPMorgan Chase, Bank of America, Citigroup, Wells Fargo and six other banks met with the Federal Reserve to complain about the recent proposal to revise the regulation designed to curb risky trading by banks, people familiar with the matter said. The banks said the proposal, dubbed Volcker 2.0 by financial regulators, could complicate compliance and hamper trading in asset classes not currently covered by the rule. "I can't imagine this aspect of the proposal being preferable to the original and current Volcker 1.0 regime," said Gregg Rozansky, a senior vice president at the Bank Policy Institute, an industry trade group representing the nation's largest banks. "It could raise prices for student loans, credit cards or auto loans."

Retail Sales and Manufacturing Are Powering U.S. Growth This Summer

A jump in retail sales and rising manufacturing output suggest the U.S. economy's strong growth in the second quarter continued into the third. Retail sales—a measure of spending at U.S. stores, websites and restaurants—rose a seasonally adjusted 0.5% in July from the prior month, the Commerce Department said Wednesday. That was well ahead of economists' forecasts for a 0.1% increase. Compared with a year earlier, they grew 6.4% in July. That's more than double the pace of inflation, which increased 2.9% in the year to July, as measured by the Labor Department's consumer-price index. Robust hiring and low unemployment mean more households have income to spend. That is being amplified by tax cuts, which have resulted in less paycheck withholding and in elevated consumer confidence.

Turkey's Economic Red Flags Stand Out Among Emerging Markets

Turkey might not be the tip of a global economic iceberg. The collapse of the Turkish lira has investors worried the nation's financial turbulence could spread to other countries, and the lira's plunge in the past few days has hit other emerging-market currencies such as Indonesia's rupiah, Mexico's peso and South Africa's rand. But few other countries are troubled by as broad a constellation of economic problems as Turkey.

On Turkey, Another Step in the Weaponization of Global Finance

BlackRock Among Investors Hit By Turkey Turmoil

Qatar Will Inject $15 Billion Into Turkish Economy Amid Breakdown With U.S.

Qatar on Wednesday pledged to inject $15 billion into Turkey's economy in a show of support for an ally whose currency has declined sharply, roiling emerging markets, as relations with the U.S. have deteriorated. Qatar's support package, which involves direct investments and deposits, comes after the country's emir, Sheikh Tamim bin Hamad Al Thani, met with Turkish President Recep Tayyip Erdogan in Ankara on Wednesday, according to a government statement.

Norges Bank Flags September Rate Rise

Norway's central bank on Thursday signaled that it is ready follow in the footsteps of the U.S. Federal Reserve and other central banks and raise its key interest rate this September. "The outlook and the balance of risks do not appear to have changed substantially" since June, when the Norges Bank said that the key policy rate "will most likely be raised in September," said Governor Oystein Olsen.

FINANCIAL REGULATION ROUNDUP

SEC Sends Subpoena to Tesla in Probe Over Musk Tweets

Federal regulators have subpoenaed Tesla Inc., according to a person familiar with the matter, ramping up an investigation into whether Chief Executive Elon Musk was truthful when he tweeted last week that he had secured funding to take the electric-car maker private. The subpoena from the Securities and Exchange Commission seeks information from each of Tesla's directors, the person said. It is unclear what information is being sought. Representatives for the SEC and Tesla declined to comment.

U.S. Pursues One of the Biggest Mortgage-Fraud Probes Since the Financial Crisis

Owners of an apartment complex near Pittsburgh, who wanted to take out a mortgage on the buildings, allegedly made vacant units look occupied by turning on radios, placing shoes and mats outside doors and in one instance having a woman tell inspectors her boyfriend was asleep inside. The owners obtained a $45.8 million loan, which was wrapped into mortgage securities and sold to investors. Practices such as these—which were alleged in a federal search-warrant application—have sparked one of the largest mortgage-fraud investigations since the financial crisis. It focuses on whether income from commercial properties was falsified, a move that would enable owners to get larger mortgages and take out cash or expand their businesses faster. Still in its early stages, the investigation has yielded a fraud-conspiracy indictment against four real-estate executives in upstate New York.

In Second Trial, Former Union Boss Convicted of Taking Kickbacks

A Manhattan federal jury Wednesday convicted the former boss of New York City's jail officers' union of fraud for a kickback scheme in which prosecutors said he invested millions of dollars of union money in a risky hedge fund. Norman Seabrook, 58 years old, was found guilty of honest-services wire fraud. The jury said Wednesday it was deadlocked on a second charge, conspiracy to commit honest-services wire fraud. The judge instructed jurors to continue deliberations. A lawyer for Mr. Seabrook didn't immediately respond to a request for comment. The trial was Mr. Seabrook's second. Last fall, a federal judge declared a mistrial after a different jury said it couldn't reach a verdict.

Thursday

8:30 a.m. EDT

U.S. Commerce Department releases July housing starts

Friday

10 a.m. EDT

University of Michigan releases preliminary August U.S. consumer sentiment

Banks, Insider Connections and Industrialization in New England: Evidence From the Panic of 1873

Using Massachusetts, Eric Hilt "tests whether firms with bank directors on their boards fared better following the Panic of 1873, which did not directly impact the state's commercial banks, but produced a prolonged economic slump." He finds in a National Bureau of Economic Research working paper that "around 59 percent of all nonfinancial corporations in the state had a bank director on their board in 1872. These firms survived the recession of the 1870s at higher rates, grew faster and experienced less of a deterioration in their credit ratings." He argues "that affiliations with commercial banks helped nonfinancial corporations maintain access to external finance during economic downturns."

Tariffs and Devaluations

Large currency depreciations are needed to offset the impact of increased tariffs, write Agnès Bénassy-Quéré, Matthieu Bussière and Pauline Wibaux in a posting on VoxEU. They find that a 1% depreciation of the importer's currency reduces imports by around 0.5% in current dollars, whereas an increase in import tariffs by 1 percentage point reduces imports by around 1.4%. "Applying our estimates to the trade conflict between the US and China, one would conclude that a 14% depreciation of the renminbi against the US dollar would be necessary to erase the effect of a 5 percentage point average increase in US import tariffs," they write. "For larger tariff hikes, the compensating exchange variation becomes extremely large and destabilising."

China's Monetary Easing Supercharges its Bond Market, Leaves Harder Questions Unanswered

"The decline in China's currency and the inconsistency in its equities market indicate limited investor confidence in Beijing's stimulus measures and leave its main dilemma—stimulating the economy even as it deleverages—unresolved," Nicholas Spiro writes for the South China Morning Post. "While the injections of liquidity have been a boon to bond investors, the scale of the domestic and external challenges confronting China's economy require a lot more than just a collapse in interest rates in order for broader sentiment towards the world's second-largest economy to improve."

U.S. industry output rose slowly in July, held down by weakness in the mining and utilities sectors.

U.S. worker productivity accelerated this spring at the best pace in more than three years, a possible sign stronger business investment is giving workers the tools they need to boost output.

New York manufacturers reported stronger growth in August, and grew more optimistic about their prospects regarding future activity.

Australia's economy moved a step closer toward full employment in July as the unemployment rate fell to a 6-year low.

Japan logged a bigger-than-expected trade deficit in July, its first in two months on a tumble in car exports to the U.S. and an increase in imports of crude oil and medical supplies, data from Japan's finance ministry showed Thursday.

Send us your tips, suggestions and feedback. Write to:

Jon Hilsenrath; Michael Derby; Nell Henderson; Jason Douglas; Paul Hannon; Harriet Torry; Kate Davidson; David Harrison; Kim Mackrael; Tom Fairless; Michael Maloney.

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WSJ PRO CENTRAL BANKING

Economy

Core Inflation Hits Fed's 2% Target | Eurozone Inflation Eases | Argentina's Policy Rate Raised to 60% | Bank of Korea Stands Pat | Timiraos's Take: When a Little Medicine Might Not Be Enough; The Wall Street Journal's central banking newsletter for Friday, August 31, 2018

2,932 words
31 August 2018
06:47 AM
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English

Timiraos's Take: When Taking a Little Medicine Might Not Be Enough

Core Inflation Hits Fed's 2% Target as Spending Heats Up

Eurozone Inflation Eases, Reinforcing ECB's Caution on Stimulus Taper

Argentina's Central Bank Lifts Policy Rate to 60%

Financial Regulation: SEC Chairman Wants to Let More Main Street Investors In on Private Deals

When Taking a Little Medicine Might Not Be Enough

At last week's Jackson Hole symposium, Fed Chairman Jerome Powell defended his strategy of gradually raising rates in the face of uncertainty over what level unemployment begins fueling excessive inflation.

To that end, he invoked the 1967 work of economist William Brainard, who showed that uncertainty about the effects of policy could infer the need for extra caution.

"In other words, when unsure of the potency of a medicine, start with a somewhat smaller dose," Mr. Powell said last week.

New staff research posted online Wednesday from economist Robert Tetlow offers a caveat on the Brainard principle. If inflation is persistent—that is, price pressures are obvious and building—then gradualism isn't the right approach. In other words, taking a little medicine won't do enough to cure the illness.

"The proper response to uncertainty concerning inflation persistence is not the customary policy attenuation…but rather anti-attenuation, meaning a more aggressive response," wrote Mr. Tetlow.

Mr. Tetlow was one of five co-authors of a longer research note published online before Mr. Powell's speech that warned policy makers against placing too little attention on the potential effects of very low unemployment on inflation.

Mr. Powell's speech argued for a gradual approach to setting policy in an environment in which key variables aren't that clear—akin to a sailor using extra caution when navigating by the stars on a night where the sky is hazy.

Mr. Tetlow's research emphasizes that in such an uncertain environment, policy makers should place more focus on probability-weighted outcomes. Sometimes underestimating inflation pressures is more costly than overestimating them, he said.

"One implication of this observation is rhetorical," he wrote. "It is not generally correct to associate caution in monetary policy design with attenuation, or gradualism. Sometimes the cautious response is a more aggressive response."

Mr. Tetlow concluded that his research uncovers "an instance in which the logic of Brainard…does not hold."

Like the research last week, the latest paper suggests potential differences in opinion within the Fed over how to set policy. Still, Mr. Tetlow's paper doesn't necessarily contradict Mr. Powell. Indeed, the Fed chairman cited two notable exceptions to the Brainard principle in his speech. Gradualism doesn't work well when the Fed needs to act boldly to prevent or stop a financial shock, and it doesn't make sense if expectations about future inflation have become unmoored and are rising or falling suddenly.

But any competing views within the central bank underscore just how difficult the decisions could soon become for the Fed if unemployment keeps falling, inflation or wages don't rise, and asset values for things such as stocks and real estate keep climbing.

Key Developments Around the World

Core Inflation Hits Fed's 2% Target as Spending Heats Up

A key measure of inflation accelerated last month to the fastest annual clip since 2012, as robust spending by consumers and businesses steadily pushed up prices for goods and services across the economy. The personal-consumption expenditures price index, a broad inflation gauge closely watched by the Federal Reserve, rose a seasonally adjusted 0.1% in July from June, the Commerce Department said Thursday. From July 2017, the index was up 2.3%, the biggest increase since early 2012. More important for the Fed, the so-called core PCE index, which excludes **volatile** food and energy prices, rose 0.2% in July from June and 2% from a year earlier, matching the central bank's target. Core PCE prices are seen as an indicator of the economy's longer-term, underlying inflation rate.

U.S. Consumer Spending Rose 0.4% in July

Analysis: Fed Is Finally Getting What It Wants on the Inflation Front

The case for the Federal Reserve having sustainably achieved its 2% inflation target is getting stronger. On Thursday, the government reported data that showed that the Fed's preferred way of measuring inflation is continuing its trend of moving toward and even above the Fed's inflation target. This performance helps ensure the central bank will continue with rate rises, even as challenges remain for the Fed and its policy path.

Eurozone Inflation Eases, Reinforcing ECB's Caution on Stimulus Taper

Inflation in the 19 countries that use the euro cooled slightly in August, while the number of people out of work fell during July, developments likely to reinforce the European Central Bank's cautious approach to dialing back monetary stimulus. The latest economic signals follow data showing the eurozone's economy slowed further in the three months through June, as exports sputtered and business confidence weakened on worries over future relations with the currency area's largest trading partners. The European Union's statistics agency said in a preliminary estimate Friday that consumer prices in the eurozone rose 2% on the year in August, a touch weaker than the 2.1% annual rate recorded the previous month.

Bundesbank's Weidmann Says a Euro-Area Budget Could Be a Good Thing, With Conditions

German Bundesbank President Jens Weidmann signaled Thursday he might support the creation of a common eurozone budget that could help improve the region's competitiveness and assist crisis-hit countries, but only as part of a fundamental reform of European Union funds. The comments from Mr. Weidmann, a longtime critic of greater risk-sharing across the currency area, come amid a political debate over reforms that could strengthen the 19-nation eurozone. French President Emmanuel Macron has championed the creation of a sizable common budget that could improve the convergence of eurozone economies and help the currency area weather future crises. Speaking in Athens, Mr. Weidmann argued that a euro-area budget "could be a welcome development…if it is part of a fundamental reform of EU funds."

Swedish Krona: A Painful Trade That Markets Missed

Negative interest rates and fractures in one of the world's most stable political systems have made 2018 an unhappy year for Sweden's currency. Down 10% against the dollar, the krona has fallen more than any other developed-market currency. Among the 10 most heavily traded currencies in the world, it has undershot even China's yuan—itself under pressure from the trade conflict with the U.S.—and the U.K.'s Brexit-bruised pound. Many investors have been caught off guard by the central bank's decision not to get ahead of the European Central Bank by raising interest rates this year.

Turkey Reshuffles Forex, Lira Taxes

Turkey has raised a tax on foreign-currency accounts and waived another on lira deposits in a bid to help the country's ailing currency and encourage savings amid mounting concern about the state of the Turkish economy. According to a decision published by the Official Gazette, Turkish authorities on Friday raised a tax on foreign-currency deposits of up to one year to 16% from 15%. The tax on lira deposits of up to six months has been lowered to 5% from 15%, and the withholding tax on lira deposits of more than one year was cut to zero from 10%. The amendments will be in effect for three months, the decision said. The measures are aimed at propping up the lira, which has plummeted 40% against the greenback this year, but analysts think that they will only help the currency in the short term.

Argentina's Central Bank Lifts Policy Rate to 60%

Argentina's peso tumbled again Thursday as President Mauricio Macri grapples with a crisis of confidence sparked by growing social unrest and skepticism about his ability to contain runaway inflation, cut spending and meet financing needs. The Central Bank of Argentinasharply raised its key interest rate to 60% from 45% at an unscheduled meeting early Thursday in an effort to shore up the plunging peso. The currency fell to new lows days after the government asked the International Monetary Fund to speed up loans under its bailout package.

Brazil's Sky-High Lending Rates Hurt Consumers—and Economic Growth

Renato Saliba offers a good example of why Brazil's economy doesn't grow faster. For 25 years, he bought and sold homes, occasionally using his credit card to cover the acquisitions. But when Brazil's 2015 recession took a bite out of his income, he couldn't keep up with interest rates that were as high as 630% a year. His unpaid debt grew so quickly he shut down his business and laid off five employees. Average bank-lending rates in Brazil are 53%, the highest among 55 developed and underdeveloped countries, according to Trading Economics. The high rates hobble a consumption-dependent economy by curbing financed shopping and making credit a risky game for entrepreneurs. The central bank has cut the basic rate by which banks lend to each other to a historic low of 6.5% from 14.25% two years ago. But in July, annual consumer rates for credit cards topped 270% for unpaid balances.

Bank of Korea Keeps Base Rate Unchanged at 1.5%

The Bank of Korea kept interest rates unchanged Thursday but left the door open for tightening monetary policy in the near future. The decision at the central bank's seven-member policy board wasn't unanimous, Gov. Lee Ju-yeol said. A hawkish dissenting member, Lee Il-houng, called for a rate increase for a second consecutive session. The central bank's decision to hold its base rate steady at 1.5% comes as the Federal Reserve is widely expected to raise interest rates in September, putting more pressure on central banks in emerging economies to follow suit.

Shares in MTN Sink After Nigeria Demands Telecom Giant Return $8 Billion

Shares in MTN Group fell as much as 25% Thursday after Nigeria's central bank ordered the African telecommunications giant to return $8.1 billion that the bank said was moved out of the country illegally. MTN said the Central Bank of Nigeria accused it of using improperly issued central bank certificates to move money to South Africa between 2007 and 2015. MTN rejected the claim and denied any wrongdoing.

FINANCIAL REGULATION ROUNDUP

SEC Chairman Wants to Let More Main Street Investors In on Private Deals

The Securities and Exchange Commission wants to make it easier for individuals to invest in private companies, including some of the world's hottest startups, the agency's chairman said in an interview. SEC Chairman Jay Clayton, a Trump appointee wrestling with how to boost flagging interest in public markets, said the commission also wants to take steps to give more individual investors a shot at companies that have been out of their reach because they haven't gone public. Mr. Clayton said the SEC is weighing a major overhaul of rules intended to protect mom-and-pop investors, with the goal of opening up new options for them.

At Wells Fargo, Discontent Simmers Among Female Executives

About a dozen female executives in Wells Fargo & Co.'s wealth-management division gathered in Scottsdale, Ariz., in June after an internal conference. They'd had enough. Women should be at home taking care of their children, some of the executives said they had been told over the years by Jay Welker, president of Wells Fargo's private bank and head of the wealth-management division since 2003. Qualified women had recently been turned down for several top roles that went to male applicants. When the women raised concerns, they felt ignored. Their frustration culminated in "the meeting of 12," according to half a dozen women who are Wells Fargo executives and who attended the meeting or had direct knowledge of it.

Wells Fargo Fires Bankers Amid Probe of Dinner Receipts That Were Allegedly Doctored

Wells Fargo & Co. has fired or suspended more than a dozen employees in its investment bank and is investigating dozens of others over alleged violations of the company's expense policy regarding after-hours meals, according to people familiar with the matter. At issue is whether Wells Fargo employees ranging from analysts to managing directors in New York; San Francisco; and Charlotte, N.C., doctored receipts on dinners that they charged to the bank, the people said. "We became aware that certain Wells Fargo Securities team members were not complying with the after-hours meals reimbursement policies after they were brought to the attention of our leaders by concerned team members," a Wells Fargo spokeswoman said in a statement. "We took action to address the issue and we continue to investigate the matter."

Court Upholds Narrower Jurisdiction in Foreign-Bribery Cases

A U.S. appeals court upheld a ruling that narrows the jurisdiction under which prosecutors can bring foreign bribery charges. The decision last week from the U.S. Court of Appeals for the Second Circuit affirming a lower-court ruling that dismissed conspiracy charges against a foreign national accused of facilitating a bribery scheme could have a significant effect on future enforcement, attorneys said. The ruling illustrates the limits of the Foreign Corrupt Practices Act, and defense attorneys said it could prompt more challenges from companies or individuals accused of violating the law.

SEC Accuses Former Playgirl Magazine Owner of Defrauding Investors

A businessman who led an adult-magazine empire that included titles like Playgirl and High Society has been accused by the Securities and Exchange Commission of defrauding investors through the sale of unregistered securities. Carl Ruderman and 1 Global Capital LLC, the Florida small-business lender he led as chairman and chief executive, are accused of fraudulently raising more than $287 million from thousands of investors. Roughly 3,400 investors, many of whom risked their retirement savings, over more than four years invested in 1 Global's securities, according to a complaint filed in Florida federal court on Aug. 23 and unsealed this week. The securities were sold through a network of agents that included people barred from the industry, the complaint said.

Friday

10 a.m. EDT

University of Michigan releases final August U.S. consumer sentiment

Should We Care About Central Bank Profits?

"While a central bank does not need to generate profits to fulfill its macroeconomic functions, it is better if it does," Francesco Chiacchio, Grégory Claeys and Francesco Papadia write for Bruegel. They point to three good reasons for central banks to achieve profits. "First, taxpayers endow central banks with large amounts of resources and one should be worried if this amount of resources did not produce any income…Second, financial strength could affect the ability of monetary authorities to fulfill their mandates…Third, profitable operations might be an indication that central banks are implementing the right policies: To achieve profits the central bank must purchase assets when they are undervalued and sell when they are overvalued, thus stabilizing their prices." The authors conclude that the accounts of the European Central Bank "show that it generates a fairly stable profit flow."

Carney Needs to Be Clear About His Future at the Bank of England

"The Bank of England's leadership has entered a state of extended transition, with Mark Carney rumored to be considering a Treasury request to serve another year as governor. Speculation suggests he might delay his departure from the central bank until 2020, serving seven years, rather than the six he will have completed if he leaves next June as planned," Chris Giles writes for the Financial Times. He notes that Mr. Carney extended his term once before and says that doing so again "will bolster the arguments of those who say he is not to be trusted." Mr. Giles adds: "Persuading Mr. Carney to remain longer in his post has many advantages for [Treasury chief Philip] Hammond and some limited financial stability insurance for the U.K. in the months ahead. But the intrigue over his appointment damages Mr. Carney, the role and his potential successors. It is beginning to create just the sort of uncertainty an extension is supposed to quell."

The number of U.S. workers filing new applications for unemployment benefits rose slightly last week after three straight weeks of decline, though a more stable measure of claims hit the lowest level in nearly five decades.

The Canadian economy rebounded in the second quarter with its best performance in a year, powered by one of the strongest export gains this decade and an acceleration in consumer spending.

A gauge of factory activity in China rebounded slightly in August, boosted by accelerated production and government efforts to arrest slowing growth and blunt the impact of the trade fight with the U.S.

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Economy

Powell Defends Fed Strategy | Trump Stances Weaken Quarles's FSB Prospects | Central Bankers Eye New Risks | Timiraos's Take: Powell Doctrine Takes Shape; The Wall Street Journal's central banking newsletter for Monday, August 27, 2018

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Timiraos's Take: At Jackson Hole, the Powell Doctrine Takes Shape

Jerome Powell Defends Policy of Gradually Raising Interest Rates

Trump's Stances Weaken Support for U.S. Official to Lead Global Banking Body

At Fed's Jackson Hole Retreat, Central Bankers Eye New Economic Risks

Financial Regulation: Trump Team's Rewrite of Low-Income Lending Rules Falters

At Jackson Hole, the Powell Doctrine Takes Shape

Jerome Powell's speech at last week's policy symposium in Jackson Hole, Wyo., offered the broadest look so far of how the Fed chairman will approach the challenge of setting policy when labor markets are tight but price pressures are only modest.

Mr. Powell described recent steps to normalize interest rates as "navigating between the shoals of overheating and premature tightening with only a hazy view of what seem to be shifting navigational guides."

The emerging Powell doctrine boils down to this: Move slowly until the economy tells you to do something different.

And a corollary: Don't rely too heavily on any single model, challenging policy frameworks against what's happening in markets and the real economy.

He outlined two instances in which the current policy of gradualism should be abandoned. Responding weakly to a financial shock or a sudden run-up or fall in inflation expectations would probably make either problem worse, he said.

The Powell doctrine still has some blanks to fill in. Mr. Powell cited concerns that overheating might stem not from inflation but rather from financial excesses, but he didn't say how monetary policy ought to be used to address potential instability.

Mr. Powell unfurled his thinking by contrasting two historical episodes. The first was the period of sustained, rising inflation during the 1970s. The second, the 1990s economic boom, offered more similarities to the current moment.

He signaled more conviction for a go-slow approach to raising rates by praising the "fortitude" of Alan Greenspan, the Fed chairman during the '90s expansion who believed something was changing in the economy that made traditional models less useful.

Mr. Powell called attention to Mr. Greenspan's strategy of convincing his Federal Open Market Committee colleagues—hawks and doves, alike—of holding off on raising rates by putting off increases meeting by meeting until signs of inflation appear.

Mr. Powell's senior adviser, Jon Faust, highlighted Mr. Greenspan's tactical cleverness in a blog post two years ago.

"If the FOMC had been publishing its Survey of Economic Projections at that time, Greenspan's dots might well have been the lowest on the FOMC over this entire period," Mr. Faust wrote. "And yet this is not an example of the Chair running roughshod over the Committee."

Mr. Greenspan still reflected Fed officials' preferences "fully and accurately" by promising to lift the benchmark rate as soon as inflation appeared, said Mr. Faust. And because disagreements over how the economy works can last for a long time, "the Chair's consensus can for a very long time look quite different from the typical dot."

The writing offers a clue at how Mr. Powell might adopt similar tactics in the months ahead, if he decides to buck the models and textbooks as Mr. Greenspan did 20 years ago.

Key Developments Around the World

Jerome Powell Defends Policy of Gradually Raising Interest Rates

Federal Reserve Chairman Jerome Powell defended the central bank's strategy of gradually raising interest rates against criticisms that the central bank is moving either too quickly or too slowly, jeopardizing the economy's expansion. Mr. Powell, in remarks Friday in the Grand Tetons, built out the case for lifting rates so long as inflation is stable and unemployment falling, to keep the economy on an even keel. He also pushed back against critiques that the Fed is risking high inflation or asset bubbles by raising rates too slowly. The Fed faces two major risks, of "moving too fast and needlessly shortening the expansion, versus moving too slowly and risking a destabilizing overheating," he said. "The current path…[is] taking seriously both of these risks."

Trump's Stances Weaken Support for U.S. Official to Lead Global Banking Body

President Trump's antagonistic posture toward international institutions at foreign summits this summer soured some European officials on the candidacy of a top Federal Reserve official to helm an international regulatory body, according to people familiar with the matter. Randal Quarles, the Fed's vice chairman for bank supervision, had emerged as a front-runner this spring to chair the Financial Stability Board, a body formed in 2009 to monitor and advise governments on financial regulation, when the term of the current chairman, Bank of England Gov. Mark Carney, expires in December. But officials in several Western European capitals later argued that an American shouldn't be rewarded with the position after Mr. Trump lashed out at both the Group of Seven summit in Canada in June and the NATO summit in Brussels in July.

At Fed's Jackson Hole Retreat, Central Bankers Eye New Economic Risks

Central bankers around the world have finally reached the point, after many years, when a period of strong economic growth allows them to unwind their postcrisis easy money policies. But at the Federal Reserve's annual retreat in Jackson Hole, Wyo., over the weekend, they found themselves eyeing new risks, including widening trade disputes and political challenges to their independence. Traditionally, a healthy expansion can lift the economy's long-run growth rate if tighter labor markets lead to higher wages or productivity-boosting investments. "Unfortunately, disruption of the global trading system has come at just the point where that was about to occur," said Bank of Canada Gov. Stephen Poloz during a concluding panel Saturday.

Global Monetary-Policy Official Decries U.S. Trade Measures

Dialing back globalization and increasing protectionism would undermine decades of economic progress around the world, Bank for International Settlements head Agustín Carstens said Saturday. Speaking to an audience of global central bankers including top Federal Reserve officials, Mr. Carstens zeroed in on President Trump's trade policies as an example of the sort of measures that threaten to drive up inflation and unemployment in the U.S. and around the world. He also cited the U.K.'s exit from the European Union and nationalist movements in parts of Europe.

Reporter's Notebook: Ten Years After the Crisis, Jackson Hole Symposium Is a Quieter Affair

This year's Jackson Hole symposium was a quieter affair than on some past occasions. The top central bankers from the U.K., Japan and the eurozone were absent, while the heads of the Mexican and Brazilian central banks attended but declined to give interviews. That likely reflects the buoyant state of the U.S. economy. Though a number of uncertainties remain, neither Federal Reserve chief Jerome Powell nor his central bank had much to gain by making a scene at Jackson Hole this year.

Analysis: The Fed Struggles to Come to Terms With the Yield Curve

Federal Reserve Chairman Jerome Powell skipped over what the bond market could be signaling about the economic outlook in his Jackson Hole speech Friday, but the issue remains squarely on the minds of many central bankers. Officials are trying to make sense of a narrowing in the difference between short- and long-term yields in the Treasury market. If short-term yields moved higher than their long-term counterparts, that would be an inversion of the yield curve, which is associated with the onset of a recession at some point down the road. There's no consensus on whether inversions cause recessions or simply correlate with them, but officials are mindful inversions are an important signal.

Atlanta Fed's Raphael Bostic Still Sees One More Rate Increase in 2018

Atlanta Fed President Raphael Bostic said Friday he continues to differ from fellow Federal Reserve officials, most of whom believe at least two more interest-rate increases are needed this year. Mr. Bostic expects just one will be required. In an interview on the sidelines of the Fed's annual symposium in Grand Teton National Park, Mr. Bostic said he hasn't seen evidence that the U.S. economy is overheating, although unemployment is near a 20-year low. "The wage numbers are not coming in super strong to suggest that we're on the cusp of overheating, and I actually don't think we are," he said.

Fed's Bullard Says Officials Shouldn't Ignore Yield Curve's Implications

Federal Reserve Bank of St. Louis leader James Bullard said during a CNBC interview it would be a serious mistake to shrug off the message of the yield curve as his colleagues contemplate further rate rises that he still thinks shouldn't happen. "I was in the Fed in 2000, 2001. The yield curve was inverted. We pooh-poohed it and we got it wrong, Greenspan got it wrong," he said of then Fed Chairman Alan Greenspan. "In 2006 one of the first speeches [then Fed chairman] Ben Bernanke gave was on the yield curve. He pooh-poohed it, he got it wrong." He added: "I do not want to play this game over again. We have to take this signal seriously."

Transcript: St. Louis Fed President James Bullard

Fed's Mester Says Gradual Rate Increases Still Best Path

Federal Reserve Bank of Cleveland President Loretta Mester said the economy's solid performance justifies further gradual interest-rate increases. "With the economy growing above trend, with the unemployment rate very low and with inflation at 2%, it's pretty clear, a very compelling case for what the Fed has to do" with monetary policy, and that is to move rates slowly higher, Ms. Mester told CNBC on the sidelines of the Kansas City Fed's annual research conference in Jackson Hole.

Transcript: Dallas Fed's Kaplan Talks to CNBC in Jackson Hole

Dallas Fed President Robert Kaplan in a CNBC interview discussed President Donald Trump, economic growth and other topics. Here is a transcript of the exchange.

BOE Economist Warns of Giant Firms' Effects on Inflation, Growth

A top Bank of England official on Friday raised the possibility that the growing market power of giant firms may be making the job of central bankers trickier. Andy Haldane, chief economist of the U.K. central bank, in a paper presented at the Fed's Jackson Hole conference, said BOE simulations suggest that when big firms grow to dominate their markets, their ability to raise prices at will appears to have significant knock-on effects on inflation and economic growth. Shifts in market power "might plausibly have altered some of the key macroeconomic relationships in the economy," Mr. Haldane said.

Digital Technology Creates New Challenges For Central Bankers, BOC's Poloz Says

Advances in digital technology are good for the economy but difficult to measure, creating uncertainty for makers of monetary policy, Bank of Canada Gov. Stephen Poloz said Saturday. Speaking on a panel in Jackson Hole, Mr. Poloz said digital technology should create new jobs and boost productivity, benefiting the overall economy. But those advances will also produce new challenges for policy makers, he said, because it isn't clear how well digitization is captured in the economic data central bankers rely upon.

China Central Bank Reintroduces Measure to Bolster the Yuan

China is stepping up efforts to stem the yuan's rapid depreciation, in a policy shift intended to fend off capital flight and blunt U.S. criticism that Beijing is weakening its currency as part of the countries' trade fight. In a statement

Friday, the foreign-exchange trading arm of the People's Bank of China said the central bank has tweaked the mechanism for setting the yuan's daily official value to prevent the currency from falling too sharply. To do so, the statement said, the central bank reapplied to its model a "countercyclical factor." The tool, used previously to counteract market forces, essentially reasserts the central bank's heavier hand in setting the currency's value, and its renewed use marks the latest in quickening steps to support the yuan.

What Turkey Can Do If Market Troubles Return

The Turkish economy took a body blow when its currency depreciated earlier this month. Things have calmed in recent days, but investors say more market dislocation lies ahead. "Turkey has seen a lot of crises in the past," said Rob Drijkoningen, co-head of emerging-market debt at Neuberger Berman. The only question is "the willingness of policy makers to take the medicine that the market requires to make the turnaround," he added. Here's a look at what tools are at Turkey's disposal in case the panic resurfaces.

FINANCIAL REGULATION ROUNDUP

Trump Team's Rewrite of Low-Income Lending Rules Falters

Talks have faltered among banking regulators on how to start rewriting requirements for banks to make loans in poorer neighborhoods, prompting one of the agencies—the Office of the Comptroller of the Currency—to move on its own as early as next week. If the discord continues, it could imperil the Trump administration's push to rewrite the law, which affects billions of dollars of bank loans and investments in lower-income neighborhoods. Much of the money flows to geographic areas around bank branches—and policy makers haven't yet resolved how to change that requirement in an age of online banking.

Goldman Cashes In on Passive-Investing Boom With Big 4 P.M. Trade

In lower Manhattan, the New York Stock Exchange's bell rings at 4 p.m. ET each trading day, signaling a giant auction that determines the closing prices for thousands of stocks. Seconds later, across town, Goldman Sachs Group Inc.'s trading systems pair up buyers and sellers on tens of millions of shares—using the price published by the NYSE but avoiding the Big Board entirely. Goldman leads a pack of investment banks that are elbowing into the crucial exchange business of end-of-day trading.

Tuesday

1 a.m. EDT

Bank of Japan releases measures of underlying inflation

Correction: A previous version of this calendar incorrectly listed Chicago Fed President Charles Evans as speaking in Buenos Aires on Monday and Tuesday. He is scheduled to speak in Buenos Aires on Sept. 3 and 4.

JACKSON HOLE PAPERS

Inequality Grows Between Top Firms, Everybody Else

Differences between companies' productivity, sales volumes and wages have grown across a range of industries, a trend that might help explain widening income disparities among workers in recent decades, according to a paper released at the Jackson Hole conference Friday. The author, Massachusetts Institute of Technology economist John Van Reenen, found that both sales and employment have tended to become increasingly concentrated among the largest firms in a given industry over the past 30 years in the U.S. Economists have noted similar growth in sales concentration in nine European Union nations where comprehensive data are available. The differences extend to worker pay.

How ‘Intangible Capital' Explains Rising Corporate Concentration, Weak Investment

The rise of "intangible capital" such as software, patents, intellectual property and innovative business processes explains much of the weakness in private capital investment since 2000, according to new research presented at Jackson Hole. The conclusion of the paper presented at the Kansas City Fed's economic symposium Friday carries important ramifications for monetary, fiscal and regulatory policy. The work by economists Janice Eberly and Nicolas Crouzet of Northwestern University also explores how the rise of these so-called intangibles, which are often pioneered by industry leaders, can partly explain growing market concentration over the last 20 years in industries that have seen some of the strongest growth, such as health care, technology and retailing.

The Other Amazon Effect: How Prices Have Become Less Insulated From Supply Shocks

Increased online competition has made retailers faster to adjust prices and more likely to hold prices constant across geographic locations, according to research presented at Jackson Hole. This could make retail prices more sensitive to shocks from tariffs or **oil prices** than they were in past periods, according to a paper released Saturday. The popular press has focused on the disinflationary forces of online retailers, or the so-called Amazon effect, that has led to declines in consumer goods prices. Harvard Business School's Alberto Cavallo took a different tack in his paper examining pricing behaviors in the Amazon era.

Better Regulations Needed for Competitive Banking System to Work, Paper Says

In most business environments, economists see competition as an unqualified force for good, driving companies toward efficiency and innovation and ultimately bringing more affordable, higher-quality products and services to consumers. But it's a more complicated story for banks in the era of "too big to fail," according to a paper presented Saturday in Jackson Hole. In the paper, economists Dean Corbae, of the University of Wisconsin-Madison, and Ross Levine, of the University of California at Berkeley, found that while intense competition among banks indeed spurs greater efficiency, it also tends to squeeze profit margins and encourage riskier investments. That leaves banks more fragile, which can have devastating consequences when the effects ripple across the financial system.

Fed Is Caught Between Phillips Curve and Yield Curve

"There are now two main ways for how to think about monetary policy," Conor Sen writes for Bloomberg Opinion. "There's the Phillips curve model, the theory that as the labor market continues to tighten it will put upward pressure on inflation and lead the Fed to favor continued interest rate increases. And there's the yield curve model, the growing view that an inverted yield curve…would be bad for the economy and should be avoided. The yield curve model would argue for caution on interest rate increases, ending them perhaps as soon as the end of this year." Mr. Sen says Fed officials are sticking more with the Phillips curve model for now, but he points to factors that in combination could change their thinking: the possibility of a yield curve inversion, Donald Trump's criticism of rate increases and the pressure that the Fed's tightening cycle puts on emerging-market economies.

Demand for long-lasting goods produced by U.S. factories fell in July because of a decline in aircraft sales, but underlying demand grew modestly.

Landscapers across the country have faced a severe labor shortage this year, spurred by low levels of unemployment and high demand for visas under the foreign seasonal-worker program known as H-2B. Higher wages and added bonuses haven't attracted more workers, some landscapers say.

Mexico's economic activity in the second quarter contracted more than previously estimated as declines in industrial output and agricultural production offset gains in services.

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The New York Times

Business Day

Elon Musk Details 'Excruciating' Personal Toll of Tesla Turmoil

By David Gelles, James B. Stewart, Jessica Silver-Greenberg and Kate Kelly
2,284 words
16 August 2018
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NYTimes.com Feed
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English

Elon Musk was at home in Los Angeles, struggling to maintain his composure. "This past year has been the most difficult and painful year of my career," he said. "It was excruciating."

The year has only gotten more intense for Mr. Musk, the chairman and chief executive of the electric-car maker Tesla, since he abruptly declared on Twitter last week that he hoped to convert the publicly traded company into a private one. The episode kicked off a furor in the markets and within Tesla itself, and he acknowledged on Thursday that he was fraying.

In an hourlong interview with The New York Times, he choked up multiple times, noting that he nearly missed his brother's wedding this summer and spent his birthday holed up in Tesla's offices as the company raced to meet elusive production targets on a crucial new model.

Asked if the exhaustion was taking a toll on his physical health, Mr. Musk answered: "It's not been great, actually. I've had friends come by who are really concerned."

[Read about the bizarre subplot involving Mr. Musk and the rapper Azealia Banks.]

The events set in motion by Mr. Musk's tweet have ignited a federal investigation and have angered some board members, according to people familiar with the matter. Efforts are underway to find a No. 2 executive to help take some of the pressure off Mr. Musk, people briefed on the search said. And some board members have expressed concern not only about Mr. Musk's workload but also about his use of Ambien, two people familiar with the board said.

For two decades, Mr. Musk has been one of Silicon Valley's most brash and ambitious entrepreneurs, helping to found several influential technology companies. He has often carried himself with bravado, dismissing critics and relishing the spotlight that has come with his success and fortune. But in the interview, he demonstrated an extraordinary level of self-reflection and vulnerability, acknowledging that his myriad executive responsibilities are taking a steep personal toll.

In the interview, Mr. Musk provided a detailed timeline of the events leading up to the Twitter postings on Aug. 7 in which he said he was considering taking the company private at $420 a share. He asserted that he had "funding secured" for such a deal — a transaction likely to be worth well over $10 billion.

[Read the five key takeaways from our interview with Elon Musk.]

That morning, Mr. Musk woke up at home with his girlfriend, the musician known as Grimes, and had an early workout. Then he got in a Tesla Model S and drove himself to the airport. En route, Mr. Musk typed his fateful message.

Mr. Musk has said he saw the tweet as an attempt at transparency. He acknowledged Thursday that no one had seen or reviewed it before he posted it.

Tesla's shares soared. Investors, analysts and journalists puzzled over the tweet — published in the middle of the day's official market trading, an unusual time to release major news — including the price Mr. Musk cited. He said in the interview that he wanted to offer a roughly 20 percent premium over where the stock had been recently trading, which would have been about $419. He decided to round up to $420 — a number that has become code for marijuana in counterculture lore.

“It seemed like better karma at $420 than at $419,” he said in the interview. “But I was not on weed, to be clear. Weed is not helpful for productivity. There’s a reason for the word ‘stoned.’ You just sit there like a stone on weed.”

Mr. Musk reached the airport and flew on a private plane to Nevada, where he spent the day visiting a Tesla battery plant known as the Gigafactory, including time meeting with managers and working on an assembly line. That evening, he flew to the San Francisco Bay Area, where he held Tesla meetings late into the night.

What Mr. Musk meant by “funding secured” has become an important question. Those two words helped propel Tesla’s shares higher.

But that funding, it turned out, was far from secure.

Mr. Musk has said he was referring to a potential investment by Saudi Arabia’s government investment fund. Mr. Musk had extensive talks with representatives of the $250 billion fund about possibly financing a transaction to take Tesla private — maybe even in a manner that would have resulted in the Saudis’ owning most of the company. One of those sessions took place on July 31 at the Tesla factory in the Bay Area, according to a person familiar with the meeting. But the Saudi fund had not committed to provide any cash, two people briefed on the discussions said.

Another possibility under consideration is that SpaceX, Mr. Musk’s rocket company, would help bankroll the Tesla privatization and would take an ownership stake in the carmaker, according to people familiar with the matter.

Mr. Musk’s tweet kicked off a chain reaction.

An hour and 20 minutes after the tweet, with Tesla’s shares up 7 percent, the **Nasdaq** stock exchange halted trading, and Tesla published a letter to employees from Mr. Musk explaining the rationale for possibly taking the company private. When the shares resumed trading, they continued their climb, ending the day with an 11 percent gain.

The next day, investigators in the San Francisco office of the Securities and Exchange Commission asked Tesla for explanations. Ordinarily, such material information about a public company’s plans is laid out in detail after extensive internal preparation and issued through official channels. Board members, blindsided by the chief executive’s market-moving statement, were angry that they had not been briefed, two people familiar with the matter said. They scrambled to cobble together a public statement trying to defuse a mounting uproar over the seemingly haphazard communication.

Mr. Musk said in the interview that board members had not complained to him about his tweet. “I don’t recall getting any communications from the board at all,” he said. “I definitely did not get calls from irate directors.”

But shortly after the Times published its interview with Mr. Musk, he added through a Tesla spokeswoman that Antonio Gracias, Tesla’s lead independent director, had indeed contacted him to discuss the Aug. 7 Twitter post, and that he had agreed not to tweet again about the possible privatization deal unless he had discussed it with the board.

In the interview, Mr. Musk added that he did not regret his Twitter post — “Why would I?” — and said he had no plans to stop using the social media platform. Some board members, however, have recently told Mr. Musk that he should lay off Twitter and focus on making cars and launching rockets, according to people familiar with the matter.

[Kara Swisher, a Times opinion columnist, writes that Mr. Musk is “deeply human, with all the positive and negative characteristics that suggests.”]

The S.E.C. investigation appears to be intensifying rapidly. Just days after the agency’s request for information, Tesla’s board and Mr. Musk received S.E.C. subpoenas, according to a person familiar with the matter. Board members and Mr. Musk are preparing to meet with S.E.C. officials as soon as next week, the person said.

In the interview on Thursday, Mr. Musk alternated between laughter and tears.

He said he had been working up to 120 hours a week recently — echoing the reason he cited in a recent public apology to an analyst whom he had berated. In the interview, Mr. Musk said he had not taken more than a week off since 2001, when he was bedridden with malaria.

“There were times when I didn’t leave the factory for three or four days — days when I didn’t go outside,” he said. “This has really come at the expense of seeing my kids. And seeing friends.”

Mr. Musk stopped talking, seemingly overcome by emotion.

He turned 47 on June 28, and he said he spent the full 24 hours of his birthday at work. “All night — no friends, nothing,” he said, struggling to get the words out.

Two days later, he was scheduled to be the best man at the wedding of his brother, Kimbal, in Catalonia. Mr. Musk said he flew directly there from the factory, arriving just two hours before the ceremony. Immediately afterward, he got back on the plane and returned straight to Tesla headquarters, where work on the mass-market Model 3 has been all consuming.

Mr. Musk paused again.

“I thought the worst of it was over — I thought it was,” he said. “The worst is over from a Tesla operational standpoint.” He continued: “But from a personal pain standpoint, the worst is yet to come.”

He blamed short-sellers — investors who bet that Tesla’s shares will lose value — for much of his stress. He said he was bracing for “at least a few months of extreme torture from the short-sellers, who are desperately pushing a narrative that will possibly result in Tesla’s destruction.”

Referring to the short-sellers, he added: “They’re not dumb guys, but they’re not supersmart. They’re O.K. They’re smartish.”

[Short-sellers made $1 billion as Tesla stock dropped 9 percent on Friday.]

Mr. Musk’s tweets on Aug. 7 were the most recent of several flare-ups that had drawn scrutiny. He wrangled with short-sellers and belittled analysts for asking “boring, bonehead” questions. And after sending a team of engineers from one of his companies to help rescue members of a stranded soccer team, he lashed out at a cave diver who was dismissive of the gesture, deriding him on Twitter as a “pedo guy,” or pedophile.

To help sleep when he is not working, Mr. Musk said he sometimes takes Ambien. “It is often a choice of no sleep or Ambien,” he said.

But this has worried some board members, who have noted that sometimes the drug does not put Mr. Musk to sleep but instead contributes to late-night Twitter sessions, according to a person familiar with the board’s thinking. Some board members are also aware that Mr. Musk has on occasion used recreational drugs, according to people familiar with the matter.

Tesla executives have been trying for years to recruit a chief operating officer or other No. 2 executive to assume some of Mr. Musk’s day-to-day responsibilities, according to people familiar with the matter. A couple of years ago, Mr. Musk said, the company approached Sheryl Sandberg, who is Facebook’s second-highest executive, about the job.

Mr. Musk said that “to the best of my knowledge,” there is “no active search right now.” But people familiar with the matter said a search is underway, and one person said it had intensified in the wake of Mr. Musk’s tweets.

[The Tesla board “now must ask a sensitive but vital question,” our columnist writes. “What was Mr. Musk’s state of mind” when he tweeted?]

In response to questions for this article, Tesla provided a statement that it attributed to its board, excluding Elon Musk. “There have been many false and irresponsible rumors in the press about the discussions of the Tesla board,” the statement said. “We would like to make clear that Elon’s commitment and dedication to Tesla is obvious. Over the past 15 years, Elon’s leadership of the Tesla team has caused Tesla to grow from a small start-up to having hundreds of thousands of cars on the road that customers love, employing tens of thousands of people around the world, and creating significant shareholder value in the process.”

Mr. Musk said he had no plans to relinquish his dual roles as chairman and chief executive.

But, he added, “if you have anyone who can do a better job, please let me know. They can have the job. Is there someone who can do the job better? They can have the reins right now.”

Andrew Ross Sorkin contributed reporting.

* Weekend at Elon’s: A Tesla Subplot With Azealia Banks

* A Question for Tesla’s Board: What Was Elon Musk’s Mental State?

* Elon Musk Is the Id of Tech

* Tesla Directors, in Damage Control Mode, Want Elon Musk to Stop Tweeting

* Did Elon Musk Violate Securities Laws With Tweet About Taking Tesla Private?

* Inside Tesla’s Audacious Push to Reinvent the Way Cars Are Made

Elon Musk, the chairman and chief executive of the electric-car maker Tesla. “This past year has been the most difficult and painful year of my career,” he said. | Noah Berger/Bloomberg | Mr. Musk declared on Twitter last week that he hoped to convert the publicly traded company into a private one. Tesla’s shares soared afterward. | David Paul Morris/Bloomberg | The Model 3 assembly line at Tesla’s factory in Fremont, Calif. The company has been racing to meet production targets on the new model. | Justin Kaneps for The New York Times | The launch of the SpaceX Falcon Heavy rocket at Kennedy Space Center in February. SpaceX, Mr. Musk’s rocket company, is said to be a possible source of funding for the Tesla privatization. | Joe Burbank/Orlando Sentinel, via Associated Press | Mr. Musk said he had been working up to 120 hours a week recently. “There were times when I didn’t leave the factory for three or four days — days when I didn’t go outside,” he said. | Joshua Lott/Getty Images

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WSJ PRO CENTRAL BANKING

Economy
Barkin: Low Rates Tough to Justify | Philippines Raises Rates | PBOC Lets Credit Flow | SEC Probes Musk's Tweets | Derby's Take: A Way to Profit From Fed Surprises; The Wall Street Journal's central banking newsletter for Thursday, August 9, 2018

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Derby's Take: A Way to Profit From Fed Surprises

Richmond Fed President Says Continued Low Interest Rates Are Tough to Justify

Philippines Central Bank Raises Rates

China's Central Bank Lets the Credit Flow

SEC Probes Musk's Tweets on Possible Tesla Buyout

A Way to Profit From Fed Surprises

There is still money to be made by trading on Federal Reserve policy announcements.

A recent National Bureau of Economic Research paper concludes investors can trade profitably on the impact on the **stock market** made by surprise Fed announcements. The paper was written by Michael Weber of the University of Chicago's Booth School of Business and Andreas Neuhierl of the University of Notre Dame.

The authors say stock prices begin moving up about a month ahead of a Fed meeting in which investors expect to see some sort of policy action to provide economic stimulus, such as cutting interest rates. Stocks drift down over the same period if investors foresee the Fed doing something that would restrict economic growth, such as raising rates.

But investors are often wrong. Say, for example, they expected the Fed to lower rates and are surprised when officials hold them steady. The researchers found that stock prices tend to continue drifting along for a few weeks as if the Fed had indeed cut rates. This provides an opportunity to trade off that market error.

The same thing happens when investors mistakenly expect the Fed to raise rates.

The paper says this drift is marketwide, holds for all industries and is global in nature, though it doesn't explain why this happens.

There are some questions about whether the paper's findings apply today. For one thing, the study covered the period between 1994, when the Fed began public announcements of policy, and 2009, during the worst of the last recession.

Things have changed a lot since then. It has been a long time since there was a genuine policy surprise coming out of a Fed policy meeting. Officials have been slowly raising interest rates since late 2015, and each move was well telegraphed ahead of time.

Similarly, the Fed's plan to start shrinking its balance sheet last year was detailed in public communications well before it was launched.

But times may be changing. Fed officials plan to raise rates gradually to what they see as a neutral level, and could get there next year. They are divided over where that point lies and what to do with rates after that. The debate creates at least the possibility that surprises might still occur.

Key Developments Around the World

Richmond Fed President Says Continued Low Interest Rates Are Tough to Justify

Richmond Fed President Thomas Barkin said Wednesday that the economy is strong, unemployment is low and inflation is at the central bank's target, adding that it's difficult to justify keeping interest rates low in such an environment. Recent tax cuts and spending increases reduce the risk in bringing the Federal Reserve's policy rate back up to "normal" levels, while higher rates would provide policy makers with crucial ammunition to combat a future downturn in the economy, Mr. Barkin said. "When the economy calls for moving back to normal levels, as do the conditions I just described, we should follow through," Mr. Barkin said at an event in Roanoke, Va.

Philippines Central Bank Raises Rates

The Philippine central bankraised its benchmark interest rates for a third straight time in an effort to control surging inflation, even as the economy expanded at a much slower pace than expected in the second quarter. Despite the slowdown, the Philippines economy has grown at 6% or more for 13 consecutive quarters, making it among the fastest-growing economies in Asia and giving the central bank room to tighten policy as inflation moves further away from its target of between 2% and 4%.

Reserve Bank of New Zealand Pushes Back Expected Rate Changes

The Reserve Bank of New Zealandkept interest rates unchanged on Thursday, while keeping its options open on whether it will tighten or ease policy next. The uncertain policy outlook comes amid signs of an economic slowdown—most visibly in business confidence, which has tumbled to recession lows. The overnight cash rate, or OCR, remained at 1.75%, with the central bank forecasting no increase in interest rates until the fourth quarter of 2020. That compares with a forecast in May of March 2020. RBNZ Gov. Adrian Orr said the central bank would be flexible and was well positioned to raise or lower interest rates.

Saudi Arabia Orders Its Fund Managers to Dump Canadian Assets

Saudi Arabia is ordering its citizens to leave Canada, selling its financial assets there and freezing trade between the two countries as part of an extraordinary diplomatic spat that has brought into global view the kingdom's extreme sensitivity to Western criticism. The steps follow the Canada's foreign ministry's chastising Saudi Arabia for its recent arrest of human-rights activists. Saudi Arabia's central bank instructed its fund managers to sell off their Canadian holdings, three people familiar with the matter said on Wednesday.

Investors Doubt Turkey Will Easily Fall Into IMF Safety Net

As Turkey's currency plummets, investors are concerned that one much used crash mat may not be there to break its fall: An IMF bailout. The IMF said Wednesday that Turkey hasn't asked for its help. It may never do so. But the idea that the IMF is there can act as a backstop for the currency and bonds of troubled countries. Many investors currently don't see that safety net easily coming together for Turkey, adding to the pressure on one of the world's largest emerging markets.

China's Central Bank Lets the Credit Flow

Short-term lending rates in China have dropped to their lowest since July 2015, as the government stimulates the economy. This appears to have been engineered by the People's Bank of China, which made a particularly large 502 billion yuan ($73.44 billion) loan to commercial banks through its medium-term lending facility in late July. The PBOC would typically follow that by using "open market operations" to adjust liquidity by borrowing or lending bonds, but hasn't done so since July 19.

FINANCIAL REGULATION ROUNDUP

New York Congressman Chris Collins Arrested on Insider-Trading Charges

Rep. Christopher Collins, a Republican congressman from New York, was arrested Wednesday and charged with participating in an insider-trading scheme to sell the shares of an Australian biotechnology company before the public disclosure of a failed drug trial. Federal prosecutors in Manhattan accused Rep. Collins, 68 years old, of tipping off his son last summer about the results of a multiple-sclerosis drug trial completed by Innate Immunotherapeutics Ltd., a biotechnology company based in Sydney. Rep. Collins was a member of Innate's board of directors and one of the company's largest shareholders, holding approximately 16.8% of its stock, the indictment said. Rep. Collins's lawyers, Jonathan Barr and Jonathan New of Baker Hostetler, said in a statement: "We are confident he will be completely vindicated and exonerated."

The Money Laundering Hub On the U.S. Border? It's Canada

After a Vancouver-based real-estate agent wired almost $240,000 from Canada's Bank of Montreal to an account in Boston last year, U.S. authorities swooped in. They arrested Omid Mashinchi and in January charged him with laundering drug money. Mr. Mashinchi pleaded guilty to the charges in late July in federal court in Massachusetts. The case is one of several recently in which the U.S. has moved on suspicious transactions involving Canadian financial firms or citizens, and comes as Canada's record of clamping down on money laundering is under fire at home and abroad.

SEC Probes Musk's Tweets on Possible Tesla Buyout

U.S. regulators are asking Tesla Inc. TSLA -2.43% whether Chief Executive Elon Musk was truthful when he tweeted that he had secured funding for what would be the largest-ever corporate buyout, people familiar with the matter said. Officials at the Securities and Exchange Commission want to know whether Mr. Musk had a factual basis for tweeting Tuesday that the going-private transaction was all but certain, with only a shareholder vote needed to pull it off, the people said.

Thursday

8:30 a.m. EDT

U.S. Labor Department releases July PPI

7:50 p.m. EDT

Bank of Japan releases corporate goods price index

Friday

8:30 a.m. EDT

U.S. Labor Department releases July CPI

Credit Allocation Along the Business Cycle: Evidence From the Latest Boom-Bust Credit Cycle in Spain

Roberto Blanco and Noelia Jiménez find in a Bank of Spain working paper that during the "great recession" in Spain, "access to credit of firms with weak balance sheets deteriorated relative to other firms." But, they write, "during the recovery phase after the latest recession access to credit of weaker firms did not improve relative to other firms and it even further deteriorated somewhat. We also provide empirical evidence that lending policies of banks with firms they are exposed to before the lending decision is taken are comparatively less sensitive to public information than those applied to new firms. This result, together with the positive correlation we find between firms' access to bank loans and the number of firms' bank credit relationships, might be linked to the existence of private information developed by banks through their interaction with borrowers. We also find that this relationship lending contributed to smooth credit contraction during the crisis."

Not a Credit Crunch Yet, but the Ground Is Shifting

"Steven Major, head of fixed income strategy at HSBC, argues that the 'triple-whammy' of Fed rate increases, balance sheet shrinkage and rising short-term money market rates is causing 'a slow-motion credit crunch.' That may be overdone, given interest rates are still close to multi-century lows and loans are still being made freely, but the ground is definitely starting to shift," Robin Wigglesworth writes for the Financial Times. "Thus far, this has mostly manifested itself at the edges of the financial system…However, there are hints that the tremors are beginning to have a broader, subtler impact."

Correction: The book "Borrowed Time" finds that Citigroup "was in many ways healthier and more stable during the century when it was independent than during the roughly 100 years it has been supported by the federal government," James Freeman wrote for The Wall Street Journal. A commentary item in Wednesday's newsletter incorrectly said Mr. Freeman wrote that the Federal Reserve had been healthier and more stable.

Turkey's Problems Run Beyond the Central Bank

A knockout rate increase by Turkey's central bank is unlikely to bring an end to the country's economic problems and the lira's plunge, writes Richard Barley for The Wall Street Journal. "The clamor for action from the Turkish central bank will only get louder, largely because it would be the most immediate and decisive step to stem the lira's fall," he writes. "But that would only be the first step for Turkey on the road to regaining confidence. Reducing Turkey's reliance on flows of hot money from abroad, making it less vulnerable to turns in sentiment, and encouraging long-term investment will take a lot more work—and time."

The Trump administration completed plans Tuesday to impose new tariffs on $16 billion in Chinese imports to punish Beijing for its trading practices, bringing the total value of products covered by the duties to $50 billion by the end of the month.

China's consumer inflation accelerated to a four-month high in July, as consumers paid more for food and fuel, official data showed Thursday.

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THE WALL STREET JOURNAL.

Markets

Last Man Standing: James Dimon; JPMorgan's James Dimon will soon be the lone CEO from the six largest U.S. lenders who has led his firm since before the financial crisis

By Emily Glazer
659 words
4 August 2018
09:00 AM
The Wall Street Journal Online
WSJO
English

A decade after the financial crisis , The Wall Street Journal has checked in on dozens of the bankers, government officials, chief executives, hedge-fund managers and others who left a mark on that period to find out what they are doing now. Today, we spotlight JPMorgan Chase CEO James Dimon.

A decade after the financial crisis rattled Wall Street, James Dimon is about to be the last man standing.

The chairman and chief executive of JPMorgan Chase & Co. is one of two CEOs from the six largest U.S. financial institutions who has led his firm throughout the past 10 years. The other, Lloyd Blankfein of Goldman Sachs Group Inc., is scheduled to retire Sept. 30.

It is the latest superlative for Mr. Dimon, whose bank has become the nation's largest by assets and market capitalization under his watch. Long one of the most-quoted figures in finance, he has emerged as an increasing presence on public-policy issues—including a period in which his name was floated as a possible Democratic candidate for the presidency. He has said he would "love to have the job, but I'm not going to run."

For now, Mr. Dimon's firm and its rivals are enjoying "a golden age of banking," he said in June, as the economy expands and banks are able to grow again. JPMorgan is on track to report a record year: It notched a profit of $8.3 billion in the second quarter, with strength across its businesses. The bank's stock has tripled in the past 10 years, easily outpacing a roughly 65% rise in the KBW**Nasdaq** bank index.

Mr. Dimon served on President Trump's business advisory council until it disbanded in August 2017. He was named chairman in December 2016 of corporate lobbying group the Business Roundtable, where he continues to engage in policy debates on center stage in Washington, an area bankers used to avoid since, even years after the crisis, it was associated with regulatory scrutiny and settlements.

"The most pressing areas where government, business and other stakeholders can find common ground should include tax reform, infrastructure investment, education reform, more favorable trade agreements and a sensible immigration policy," he wrote in his annual letter to shareholders in April.

Some of those changes have been and could be beneficial to the bank, which has also partnered with Amazon.com Inc. and Berkshire Hathaway Inc. on a new venture that aims to overhaul workers' health care.

Mr. Dimon, 62 years old, joined JPMorgan as president and chief operating officer in July 2004, following its merger with Bank One Corp. He became CEO in December 2005 and chairman a year later. Earlier, he held roles at financial firms including Citigroup Inc. and American Express Co.

Mr. Dimon doesn't fail to remind any audience that JPMorgan was asked by the government to buy Bear Stearns as the broker-dealer faced bankruptcy in March 2008. The deal closed, for $1.5 billion, about two months later. In September 2008, JPMorgan bought struggling Washington Mutual for $1.9 billion.

Those purchases would come back to haunt the bank, as it reached a $13 billion settlement with the Justice Department in 2013 for crisis-era problems, the vast majority relating to Bear Stearns and WaMu.

Mr. Dimon has said the bank wouldn't do the Bear Stearns deal again, but that buying WaMu might still make sense if the price tag were lower, given the legal uncertainty. That is among the legacies of the backlash to the crisis that developed in the following years.

"These are expensive lessons that I will not forget," Mr. Dimon wrote of the deals in his 2015 shareholder letter.

Write to Emily Glazer at emily.glazer@wsj.com

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THE WALL STREET JOURNAL.

World

Putin's Unlikely Ally in His Standoff With the West: His Central Banker; Elvira Nabiullina has earned an unusual degree of freedom to buttress an economy buffeted by sanctions

By Anatoly Kurmanaev
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The Wall Street Journal Online
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English

ST. PETERSBURG—After Russia's central-bank chief, Elvira Nabiullina, moved to shut down a large lender last year for allegedly falsifying accounts, the nation's top prosecutor's office issued an order to leave the bank alone.

She closed it anyway.

In her five years in office, Ms. Nabiullina has closed hundreds of weak banks, stymied the exodus of Russian wealth abroad and transformed monetary policy to bring inflation to record lows. That has earned her an unusual amount of freedom to make tough decisions, even if that means treading on powerful interests.

Thinking of Ms. Nabiullina merely as a central banker understates the significance of her role. As President Vladimir Putin bids to return Russia to great-power status, challenging the U.S. and Europe from Syria to Ukraine, it's her job to shore up the economy against **volatile** oil markets and sanctions. Russia's ability to continue its quest rests in large part on whether Ms. Nabiullina can keep the financial system stable.

Given Russia's messy, corruption-filled banking system, that is a challenge. She has struggled to regulate some state banks, analysts said, and her job has grown more difficult with looming new U.S. sanctions against Moscow for a nerve-agent attack against a former Russian spy in the U.K. Moscow has repeatedly denied involvement.

Ms. Nabiullina has earned public praise from Mr. Putin, who rarely commends subordinates, as well as from abroad. Last year at the Kremlin, Mr. Putin told her that "under your leadership, the central bank has done a great deal to stabilize the economic situation." Managers at big investment funds, from Pacific Investment Management Co. to Pictet Asset Management, call Ms. Nabiullina one of the world's most skilled central bankers. Christine Lagarde, managing director of the International Monetary Fund, lauded her in May for setting "standards of quality for macroeconomic policy."

International investors have piled into Russian government bonds, despite the country's weak economic growth, weakening currency and deepening U.S. sanctions.

"Nabiullina was clearly given a mandate from the highest level of the government to bring stability," said Kirill Lukashuk, head of the financial sector at ratings agency ACRA. "The government realized they can't be stable without a healthy banking sector, strong reserves and low inflation."

In an interview, Ms. Nabiullina said her focus has been on improving the health of Russia's banking sector. "It became obvious to everyone that something had to be done," she said. "In the circumstances when we started facing external challenges and geopolitical risks, the financial system had to become very strong and very stable."

Mr. Putin has expressed his "very, very high appreciation" of Ms. Nabiullina's work "given the very complicated macroeconomic environment, the very aggressive international environment, toward Russia," said presidential spokesman Dmitry Peskov. "Her position demands more independence…because the central bank is independent in accordance with our legislative system," he added.

When Ms. Nabiullina took over Russia's central bank in 2013, it was a sleepy institution with poorly trained staff and limited powers, investors and bankers said. Mr. Putin criticized her predecessors for lacking the will to clean up the country's banks.

In 2006, the central-bank official responsible for revamping the system, Andrey Kozlov, was shot dead in his car. Russian financier Alexey Frankel, whose banking license Mr. Kozlov had revoked earlier that year, was later convicted of organizing the killing.

Today, bodyguards accompany Ms. Nabiullina even inside her headquarters.

Detractors include presidential advisers and industrialists who say her focus on low inflation and iron regulation is stifling the economy.

"From stability to stagnation is just a short step," said Andrey Sokolov, chairman of Russia's largest private lender, Alfa Bank.

There are about 480 active banks in Russia, triple the number in Brazil, which has a similar-sized economy. Russia's top 20 lenders, however, account for 70% of the banking assets. Almost a third of the banking system is in the hands of state-owned Sberbank, the successor of the Soviet Union's banking monopoly.

Ms. Nabiullina, 54 years old, was born into a working-class Tatar family in the Ural Mountains. She earned an economics degree from Moscow's top university during the final years of the Soviet Union and immediately began working on policies for Russia's burgeoning market economy.

She spent the 1990s working at the country's largest business trade group and in the economy ministry. She has earned a reputation for bookishness, personal honesty and fixation on detail, according to government advisers. Those qualities drew the attention of Mr. Putin, who brought her into his think tank to help draft an economic manifesto shortly before he assumed the presidency in 2000.

As president, Mr. Putin consolidated power, curbing the political clout of tycoons and regional strongmen. At the time they also controlled a large part of the banking system, using weak regulation to finance political campaigns and personal ventures and to transfer wealth out of the country.

When banks collapsed under the weight of bad lending decisions and unsustainable deposit rates, owners often moved abroad, usually to London, where they bought mansions at record prices. The U.K.'s government has denied extradition requests from Russia, citing lack of trust in the country's judicial system.

Industry veterans said that before Ms. Nabiullina took over, banking licenses were mostly used as mechanisms to funnel money abroad and process insider deals.

"We used to open a newspaper in the morning and look at the banking deals and said—that's capital flight, and that's asset stripping," said Sergey Khotimskiy, co-founder of one of Russia's largest private banks, Sovcombank. "The dodgy enrichment schemes were obvious to everyone."

The 2008 global financial crisis exposed the weakness of the system. Indiscriminate lending saddled banks with mountains of bad debts, which they camouflaged with increasingly elaborate balance-sheet exercises, said Mikhail Zadornov, a veteran state banker. Bank failures snowballed, leaving the state to pick up the tab for insured deposits.

Banking woes slowed Russia's economic recovery, which convinced Mr. Putin to act. In Ms. Nabiullina he saw a loyalist who had the expertise and the stomach to clean up the financial system, according to two people who were government advisers at the time. Mr. Putin appointed her as his economic adviser in 2012, and head of the central bank the following year.

When she took over the institution, banks and companies were moving $5 billion out of the country every month, and inflation topped 7%.

She shut down 70 banks in her first year.

In 2014, the West met Russia's military interventions in Ukraine with sanctions. The impact, combined with a precipitous fall in the **oil price**, caused the value of the ruble to fall by half against the dollar that year.

Ms. Nabiullina stopped a longstanding policy of spending billions of dollars from the country's reserves to try to prop up the ruble. In December 2014, with the ruble continuing to fall, the central bank nearly doubled its key lending rate to 17% at an emergency late-night meeting.

The rate increase restored calm to markets but strangled the country's consumer-fueled growth. The country's emerging middle class, which had become used to foreign vacations and European cars, is still feeling the effects of the ruble's collapse.

Some government advisers and lawmakers criticized Ms. Nabiullina for the rate increase. "Difficult decisions are difficult to explain [to the government]," she said. "For me it was easy to make that rate decision, because I was sure there was no alternative."

Ms. Nabiullina turned her attention next to homegrown problems. Since she took office, she has halved the number of Russian banks, shutting down about 440 lenders. She has reduced capital outflows by about 50% to $2.5 billion a month.

Many of the banks she closed had been considered untouchable, analysts said. Some, such as Promsviazbank, counted lawmakers and state-company executives among its shareholders and held money for national oil companies and the Orthodox Church. Others, like Bank Sovetskiy, had served political objectives, providing banking services in Crimea, the Ukrainian region the Kremlin annexed in 2014.

A dozen shut-down lenders have tried suing the central bank to get their licenses or assets back. None have succeeded.

"Nabiullina has freedom to operate as she chooses in the interests of stability, even when it hurts vested interests," said Alexander Danilov, a banking analyst at Fitch Ratings. "She has stepped on many toes."

Yugra, the bank she closed last year over the objections of the prosecutor's office, is owned by construction magnate Alexey Khotin. The bank had used credit taken from other banks to subsidize market-beating deposit rates, and became the 12th-largest holder of retail deposits in the country last year, according to the central bank. It also sponsored an amateur hockey league founded by Mr. Putin, who occasionally plays in it.

When the central bank took over Yugra last June following repeated warnings, it said it found a $600 million deficit in its balance sheet masked with bad loans. Just hours before the bankrupt bank's license was due to expire, the prosecutor's office ordered a halt to the closure, calling the bank "a financially stable credit organization." Ms. Nabiullina rejected the order.

Mr. Khotin's representatives and the prosecutor's office didn't respond to a list of questions on Yugra's closure, which the bank is contesting in court.

"It was a test of will, and she won," said banking analyst Mr. Lukashuk.

Ms. Nabiullina's freedom stands out from her peers in developing economies from Turkey to Argentina, where central bankers are under pressure from the government to keep interest rates low to keep credit flowing to voters and businesses.

In January, inflation hit a record low for the post-Soviet period of 2.2%, a result of Ms. Nabiullina's decision to keep interest rates high after the Crimea sanctions. Some tycoons have urged a faster reduction.

Ms. Nabiullina's confidence in Mr. Putin's backing was on display at the central bank's congress in St. Petersburg in June.

She publicly traded barbs with the chief executive of Russia's banking behemoth, Sberbank, and criticized the head of a major state oil company for raising gasoline prices. She chastised the police and courts for not doing enough to punish errant bankers.

Still, she has struggled to regulate Russia's lesser, underperforming state-owned banks, whose executives often treat them as fiefs, analysts said. These banks are kept afloat by constant injections of state funds, which the executives have funneled into unrelated assets ranging from supermarkets to railroad cars.

Almost a trillion rubles of public capital, about $16 billion at today's rate, went to just three state-owned banks—VTB, Gazprombank and Rosselkhozbank—in the first four years of Ms. Nabiullina's central-bank term, according to Fitch Ratings. All are still saddled with bad debts or illiquid assets.

Ms. Nabiullina said the same regulatory rules apply to all banks, adding that she has shut down several regional state-owned lenders.

The central bank has also come under criticism for bailing out three large private banks last year, including the country's seventh-largest lender, Bank Otkritie. The move has cost the government about $44 billion and continues to drain public funds.

Private bankers said Otkritie should have been sold off in pieces instead of becoming yet another state bank. Government-owned lenders now account for two-thirds of all lending and private deposits.

Ms. Nabiullina said Otkritie was "too big to fail" and required a quick takeover to avert a financial crisis.

While the cleanup of the financial sector is nearly finished, she said, she sees bigger problems for Russia's economy as a whole. "The previous model of [consumer-led] economic growth has been drained," she said. Her modest economic forecasts have consistently lagged behind Mr. Putin's goals, which she said can be achieved only through deep, unpopular changes to the system.

Even if the price of oil rose to $100, from around $65 today, she said, "it's very unlikely that our economy can grow above 1.5% to 2%" a year.

Anna Mikheeva and Mike Bird contributed to this article.

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THE WALL STREET JOURNAL.

Economy

Central Bankers' Jackson Hole Gathering: a Cheat Sheet; Fed Chairman Jerome Powell will deliver a speech on 'Monetary Policy in a Changing Economy' Friday morning

By Nick Timiraos
1,278 words
23 August 2018
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The Wall Street Journal Online
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JACKSON HOLE, Wyo.—For the central bankers gathered in the Grand Tetons, a meaty discussion of corporate consolidation and declining economic dynamism will take precedence over fly fishing and mountaineering.

The Federal Reserve Bank of Kansas City's annual economic retreat began Thursday evening and runs through Saturday at its traditional venue, the Jackson Lake Lodge, selected decades ago for its appeal to former Fed Chairman Paul Volcker, a fly-fishing enthusiast.

Attendance is by invitation only. Here's a cheat sheet on what to expect over the next few days:

Talk of the Lodge

The theme of this year's conference is "Changing Market Structure and Implications for Monetary Policy":

Kansas City Fed President Esther George will host an opening reception Thursday evening. The conference gets under way in earnest Friday morning.

At 10 a.m. EDT Friday, Fed Chairman Jerome Powell will deliver a speech on "Monetary Policy in a Changing Economy." On Thursday, the Fed posted a paper from a group of senior Fed economists that warns against being too complacent in raising interest rates once unemployment drops to low levels because monetary policy operates with a lag. It is possible Mr. Powell will refer to this research in his speech.

After Mr. Powell's speech, two research papers will be presented and discussed, followed by a panel discussion that features Andrew Haldane, chief economist for the Bank of England. Princeton's Alan Krueger, who served as a top economist to President Barack Obama and has published leading research on labor economics, delivers the lunchtime keynote address.

On Saturday, two more research papers will be presented and discussed, followed by another panel discussion.

A concluding panel will feature Agustín Carstens, general manager of the Bank for International Settlements; Bank of Canada Gov. Stephen Poloz; and the University of Chicago's Raghuram Rajan, who led the Reserve Bank of India from 2013 to 2016.

Beyond the Agenda

The formal program will focus on serious economic questions, but a number of subplots will unfold into the weekend:

—Mr. Powell has been a regular attendee since joining the Fed's board as a governor in 2012, but this will be his first appearance since becoming the Fed's leader in February. While Mr. Powell isn't likely to say anything about it, his public appearance will be the first since President Trump criticized the Fed's campaign to raise interest rates, first last month and also last week when he told donors he hoped Mr. Powell wouldn't disappoint him.

Minutes of the Fed's most recent meeting, July 31-Aug.1, signaled that the central bank is ready to raise its benchmark short-term rate by another quarter percentage point at its Sept. 25-26 policy meeting. That would lift the rate to a range between 2% and 2.25%.

—Appearances by Mr. Carstens, the former head of Mexico's central bank, and Mr. Poloz will provide an opportunity for international perspectives on the Trump administration's aggressive trade posture.

Fed officials signaled in the minutes that they are uneasy over trade policy, but not so much that they're ready to scrap their plan to gradually push rates to a neutral setting that neither spurs nor slows economic growth.

In interviews on the sidelines of the conference, Fed officials are likely to drop more hints about the path forward for monetary policy. They are also set to resume a technical discussion this fall that could influence how much longer they will shrink their $4.2 trillion portfolio of bonds and other assets.

—For the fifth year in a row, the liberal Center for Popular Democracy's Fed Up campaign is on hand for the Jackson Hole gathering. It organized a Thursday panel on slow wage growth and market concentration.

—The conference roster is heavy on international central banking officials, and President Trump's frustration with the Fed and with U.S. trading partners could feed after-hours conversation. Mr. Trump's main path to remake the Fed, by appointing new members to the Fed's seven-member board of governors, has so far yielded mostly establishment types who aren't likely to take a sledgehammer to the institution's culture.

Roll Call

It is another star-studded attendance list for this year's conference, at least for the world of central banking.

—There is perfect attendance this year by all 11 of the Fed's sitting regional reserve bank presidents and by all three governors in Washington. (The San Francisco presidency is currently vacant, but the bank's research director, Mary Daly, is attending).

—The roster of international central bankers includes, in addition to Messrs. Carstens, Haldane and Poloz, Bundesbank Vice President Claudia Buch; Hong Kong Monetary Authority Chief Executive Norman Chan; Bank of Portugal Gov. Carlos Costa; Bank of Argentina Gov. Luis Caputo; Bank of Mexico Gov. Alejandro Díaz de León; Bank of Colombia Gov. Juan José Echavarría; Bank of Israel Gov. Karnit Flug; Bank of Brazil Gov. Ilan Goldfajn; Bank of Iceland Gov. Már Gudmundsson; South African Reserve Bank Deputy Gov. François Groepe; Sveriges Riksbank Gov. Stefan Ingves; Bank of Ireland Gov. Philip Lane; Bank of Chile Gov. Mario Marcel; Norges Bank Gov. Øystein Olsen; Bank of Finland Gov. Olli Rehn; Bank of Japan Deputy Gov. Masazumi Wakatabe; Reserve Bank of Peru Gov. Julio Velarde; Reserve Bank of Australia Assistant Gov. Christopher Kent; and Ayman AlSayari, the deputy governor for investment of the Saudi Arabian Monetary Authority.

—There are no attendees from the Trump administration this year. Marvin Goodfriend, the Carnegie Mellon University economist who has been nominated by Mr. Trump to be a Fed governor, is in attendance. Mr. Goodfriend's nomination advanced earlier this year through the Senate Banking Committee on a party-line vote and remains in doubt.

—A handful of industry economists are in attendance, including Pat Bajari, chief economist at Amazon, and Carolyn Evans, head economist at Intel Corp.

—Several former Fed officials also are set to join, including William Dudley, who retired as New York Fed president in June, and Stanley Fischer, who served as the Fed's vice chairman until last October. Other former Fed officials include Alan Blinder, Roger Ferguson, and Donald Kohn, who each served as vice chairman, and former Kansas City Fed President Thomas Hoenig.

—The list also includes a handful of former and current government officials, including Keith Hall, director of the Congressional Budget Office; Jason Furman, former chairman of the Council of Economic Advisers under President Barack Obama; Ron Jarmin, acting director of the U.S. Census Bureau; and Glenn Hubbard, who was chairman of the Council of Economic Advisers under President George W. Bush.

—And of course, the conference is full of high-profile academics, such as Harvard University's Martin Feldstein (a former CEA chairman under President Ronald Reagan), Janice Eberly of Northwestern University; Pete Klenow of Stanford University; Carl Shapiro of the University of California, Berkeley; and Kristin Forbes of the Massachusetts Institute of Technology.

Write to Nick Timiraos at nick.timiraos@wsj.com

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THE WALL STREET JOURNAL.

Politics

Trump Advisers Urge Raising Additional China Tariffs to 25%; Washington hasn't made meaningful headway in easing its market-rattling trade dispute with Beijing

By Bob Davis and Lingling Wei
1,286 words
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The Wall Street Journal Online
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As Washington and Beijing struggle to break a trade impasse, some administration advisers are urging President Trump to raise the stakes with a sharp increase in the level of tariffs proposed for $200 billion in Chinese imports targeted for punitive measures.

Trump administration advisers are debating measures that might bring Chinese negotiators to the table. Some are pushing the president to apply tariffs as high as 25% on $200 billion of Chinese imports, up from an original proposal for 10%.

The White House won't make a final decision until at least late August on those tariffs, which are likely to target consumer goods and food as well as machinery components. Advisers are justifying the steeper tariffs, in part, to make up for the rapid depreciation of the yuan in recent months. Since May 30, the yuan has fallen 6% against the dollar.

"Once you go down the road of using tariffs to disrupt the Chinese, you have to say 25% compared to 10%," said Derek Scissors, a China expert at the American Enterprise Institute who advises the administration on trade.

The U.S. has already imposed 25% tariffs on $34 billion worth of Chinese imports and is on schedule to levy similar tariffs on an additional $16 billion of goods, probably this week or next.

The additional $200 billion would be the next step, should the U.S. make good on Mr. Trump's threat to ratchet up pressure and, if needed, impose tariffs on all $505 billion in goods China ships to the U.S. should negotiations fail to reach a favorable outcome.

The debate over tariff levels comes as Washington has yet to make meaningful progress in settling its market-rattling trade dispute with Beijing. Treasury Secretary Steven Mnuchin and Chinese envoy Liu He and their staffs continue to talk about a possible meeting, said officials in both capitals, but the talks remain at a very preliminary stage.

Both sides argue that it is up to the other to make the first move after several preliminary Chinese offers, mainly involving the purchase of more U.S. goods, were rejected by Mr. Trump as inadequate.

The two sides have agreed that their initial offers weren't a solid base for further negotiations, according to a senior member of the U.S. business community tracking the discussions. Those included the Chinese offering mainly to buy U.S. goods, and the U.S. demanding that China essentially scrap the industrial policy that turned it into an economic powerhouse, the senior executive said.

"They are discarding useless ideas and rhetoric," the executive said. "They are figuring out what could be on an agenda and what could be a solution."

Mr. Mnuchin said at Group of 20 meeting last week in Buenos Aires that he and members of the Chinese delegation engaged in "chitchat."

Longtime China hands have been urging a resumption of talks and been working with Washington and Beijing to get the discussions started. They include former Treasury Secretary Hank Paulson, who was Mr. Mnuchin's boss at Goldman Sachs Group Inc., and Blackstone Group LP Chief Executive Stephen Schwarzman, said people familiar with the efforts.

The administration believes it strengthened its hand last week with a tentative trade accord with the European Union. The two sides agreed to use the World Trade Organization to deal with intellectual-property theft, government pressure on companies to transfer technology and the operation of state-owned industries—all code words for alleged trade infractions by Beijing.

With the agreement, China is "in a very difficult position," Lawrence Kudlow, director of the National Economic Council, said Sunday on CBS. "China is, I think, being isolated."

Whatever gains the U.S. might have made with Europe, however, haven't eased the trade fight with Beijing. The U.S. alleges that China presses U.S. companies to hand over valuable technology and uses unfair trade practices to produce an enormous trade surplus with the U.S.

The Trump administration remains deeply divided over how best to deal with the Chinese, and the two main factions are moving in different directions. China trade hawks, led by U.S. Trade Representative Robert Lighthizer, believe China will make concessions only if it feels the brunt of heavy tariffs, said U.S. officials.

Trade doves, led by Messrs. Mnuchin and Kudlow, have been looking for a solution short of massive tariffs, fearful that those levies, plus Chinese retaliatory tariffs on American goods, could slow U.S. growth and tank **financial markets**. Mr. Mnuchin and Mr. Liu have continued to discuss U.S. China relations, but some of those conversations have gone poorly.

In one indication of the strain between the two countries, Qualcomm Inc. last week had to scuttle its agreement to purchase Dutch company NXP Semiconductors NV after China didn't give the deal the green light. Days earlier, Mr. Mnuchin called Mr. Liu to lobby for its approval, according to people familiar with the matter. Mr. Mnuchin didn't believe the call had gone well, the people said.

The Chinese decision was a blow to Mr. Trump, who had worked to reduce U.S. penalties on Chinese telecomm giant ZTE Corp., which was accused of violating U.S. sanctions against Iran and North Korea. Some U.S. government and industry officials had expected the ZTE efforts would prompt China to reciprocate and approve the Qualcomm-NXP deal.

Previous negotiations have led the Chinese side to be skeptical Mr. Mnuchin can deliver a trade deal. Mr. Liu had proposed to buy nearly $70 billion of U.S. farm, energy and other products last month, which Beijing thought went a long way to meet Mr. Trump's demand to cut the bilateral trade deficit by $200 billion. But Mr. Trump rejected that proposal. "The two sides just keep talking past each other," said a person familiar with the discussions.

The scale of the U.S. tariff offensive has Beijing on edge. The Chinese leadership is dealing with economic headwinds, including weakening investment and household consumption, as well as rising corporate defaults. The trade tensions threaten to put growth further at risk.

Beijing, however, has been preparing for a long fight. On Tuesday, President Xi Jinping oversaw a high-level meeting that signaled a shift in economic priorities toward supporting growth through means such as debt control. The meeting laid out a range of pro-growth measures, such as greater spending on infrastructure and easier credit for banks and businesses.

Chinese officials have also been weighing how far to press the pledged retaliation against the U.S. on trade without hurting other national interests. Measures being rolled out so far include holding up licenses for U.S. businesses, delaying approval of mergers and acquisitions involving U.S. companies, and ramping up inspections of American products at China's borders.

Beijing is also wary of pushing so far as to cause U.S. businesses to leave China—which could be a blow to Beijing's effort to attract foreign capital and keep its citizens employed at a time of growing economic contraction.

In an apparent effort to allay concern that Beijing might increasingly target American businesses in its retaliation, a statement issued by Tuesday's Politburo meeting specifically said "legitimate rights of of foreign companies in China will be protected."

Write to Bob Davis at bob.davis@wsj.com and Lingling Wei at lingling.wei@wsj.com

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The New York Times

Business Day; Economy
Fed Holds Interest Rates Steady

By Jim Tankersley
522 words
1 August 2018
05:00 AM
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English

WASHINGTON — The Federal Reserve raised its already high marks for the state of the economy on Wednesday, refusing to bow to President Trump's recent push for the central bank to pause its march toward higher interest rates.

Fed officials voted unanimously at the end of their two-day meeting to keep interest rates unchanged, at a range of 1.75 to 2 percent. But the statement they issued keeps the Fed on track to raise rates next month and again in December, following two rate hikes in the first half of the year. Its revised assessments of economic growth and the inflation rate could signal that those coming increases are even more likely than investors previously thought.

The statement declared that the job market continues to strengthen and "economic activity has been rising at a strong rate." That is a change from the June statement, when the Fed said economic growth was "solid." Officials also improved their assessment of consumer spending, saying that it has "grown strongly."

The Fed statement did not convey any concern that Mr. Trump's trade policies could hamper growth, nor did it suggest worry about the sluggish pace of wage increases for most workers. The Fed chairman, Jerome H. Powell, fielded a barrage of questions from members of Congress on those topics in testimony last month.

In their statement on Wednesday, Fed officials said the overall inflation rate and the rate that excludes **volatile** food and energy prices both "remain near 2 percent," which is the Fed's target level. In June, officials said those rates "have moved close to 2 percent."

In keeping with previous statements, officials continued to signal they will raise rates again soon, saying they expect "that further gradual increases in the target range for the federal funds rate will be consistent with sustained expansion of economic activity, strong labor market conditions and inflation near the Committee's symmetric 2 percent objective over the medium term."

The slight changes reflect improving economic data in recent weeks. Economic growth clocked in above 4 percent for the second quarter, and inflation ran slightly above 2 percent.

The statement did not come with an updated set of economic forecasts issued after the meeting, nor a question-and-answer session with Mr. Powell, who gives quarterly news conferences now but has chosen to pick up the pace next year and brief reporters after every Fed meeting. So there was no direct response to Mr. Trump, who has broken recent protocol and publicly criticized the Fed's path of rate increases, worrying that they will dampen a strong economic run.

* Trump Blasts Fed, China and Europe for Putting U.S. Economy at a Disadvantage

* Senators Push Fed Chairman for Answers on Slow Wage Growth

* Fed Raises Interest Rates and Signals 2 More Increases Are Coming

The Federal Reserve is expected to leave interest rates unchanged at its August meeting. The Fed chairman, Jerome H. Powell, has been under attack from President Trump over the Fed's interest rate increases. | Al Drago for The New York Times

Document NYTFEED020180801ee81001mh

THE WALL STREET JOURNAL.

Markets

Former High-Speed Trading Executives Allege 'Tyrannical Coup' at Quantlab; A leadership fight has broken out over one of the world's most secretive and profitable high-frequency trading firms, pitting a beret-wearing mathematician against a former business partner and a Ukrainian physicist

By Bradley Hope
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English

A leadership fight has broken out over one of the world's most secretive and profitable high-frequency trading firms, pitting a beret-wearing mathematician against a former business partner and a Ukrainian physicist.

The dispute in recent weeks has spilled into lawsuits that, for the first time, shed light on the inner workings of Quantlab Financial LLC, a Houston-based high-frequency-trading firm. A website for co-founder Wilbur "Ed" Bosarge Jr. says the firm accounts for between 3% and 10% of total daily volume on the venues where it trades.

The colorful personalities that have run Quantlab for two decades are now sparring over control of it. Quantlab trades on dozens of exchanges and has earned more than a billion dollars of profits over the last two decades. The founders of the firm began to clash in early 2016, according to the court records, and a person familiar with the company.

Co-founder Bruce Eames, 63, and Ukrainian physicist-turned-quant Andrey Omeltchenko say in filings they began to disagree with Mr. Bosarge after discussions to sell a controlling interest in Quantlab's parent company, Quantlab Group LP, to an undisclosed buyer valued it at between $1.6 billion and $1.8 billion. The deal later fell apart.

Mr. Bosarge, 78, believed the firm could fetch a valuation of more than $3 billion, according to their complaint, which says he took control of the company in a "tyrannical coup." The men are asking a Texas district court judge to give them control of the company's operations.

Mr. Bosarge said in a statement that he returned to the company in mid-2016 as CEO following an absence after Mr. Eames asked him to because Mr. Eames "felt unable to continue in that role."

"It is unfortunate that Bruce and Andrey—who collectively control less than 28% of the ownership—are attempting to interfere with the successful current management of the company," Mr. Bosarge said. "On a personal level, after our many years of friendship, I am saddened and disappointed that Bruce and Andrey have resorted to false, misleading and defamatory statements."

Messrs. Eames and Omeltchenko and their lawyers declined to comment.

Companies connected to Mr. Bosarge and his family control own more than 70% of Quantlab Group. For years, he has taken a back seat there to focus on his other businesses, including medical-research company Black Beret Life Sciences LLC, a sugar substitute called Sola and a 72-acre private island resort in the Caribbean. During the sale discussions, he began to play a day-to-day role in the firm.

"Instead of recognizing that a $3 billion valuation for Quantlab Group was not a realistic possibility, Dr. Bosarge blamed Mr. Eames," according to the complaint from Messrs. Eames and Omeltchenko.

Under Mr. Bosarge's control, Quantlab "barely broke even," making 2017 the "worst year in Quantlab Group's history," according to the complaint from Messrs. Eames and Omeltchenko. This year is on track for similar results, it says.

The person familiar with the company said that many high-frequency trading firms struggled in 2017, but noted Quantlab was in good enough shape to acquire assets from rival firm Teza Technologics LLC in Chicago that year.

"As a result of a series of changes the current management team has made over the past two years, the company is stronger today," Mr. Bosarge said in a statement.

In recent years, Quantlab has earned more than $200 million annually in net profits and averaged since founding "in excess of hundreds of millions per year," the complaint from Messrs. Eames and Omeltchenko says.

In November 2017, Messrs. Eames and Omeltchenko sought to replace Mr. Bosarge as the general partner of the company through an action in the Court of Chancery in Delaware. A judge in early May ruled against the move, saying they misread internal agreements before moving "under the cover of night to try and overthrow a majority owner."

In a separate federal suit filed by Quantlab against a lawyer allegedly consulting with Messrs. Eames and Omeltchenko, the firm described the effort as an attempt to "steal control" of the company through a "surprise coup d'état." The lawyer, Allen Dempster of Walnut Creek, Calif.-based Dempster & Dietler LP, declined to comment.

In June, after the judge in Delaware ruled against their move, Messrs. Eames and Omeltchenko filed a suit in the district court of Harris County, Texas, against Quantlab Group and the companies through which Mr. Bosarge and his family own most of it, asking a judge to give them control of the firm.

"Now without the key management and research scientist who made Quantlab Group into a billion dollar company, Quantlab Group's future is at risk," the complaint from the men says. "What remains is valuable, but increasingly ineffective, intellectual property".

The most successful high-frequency trading firms were founded by an eclectic lot. Virtu Financial Inc.'s founder, Vincent Viola, is a former infantry officer turned gasoline pit trader who became chairman of the New York Mercantile Exchange. Mark Gorton, of Tower Research Capital, was founder of the company that distributed the peer-to-peer file-sharing program LimeWire that was shut down over copyright infringement.

Mr. Bosarge, who previously worked as a mathematician at IBM, first tried to break into the fledgling field of quantitative investing with the formation of The Frontier Cos. in 1986. Quantlab's lawsuit against the lawyer allegedly working with Messrs. Eames and Omeltchenko says Mr. Bosarge in the 1980s and 1990s "developed mathematical models that could predict the behavior of **financial markets**".

In 1997, Mr. Bosarge began working with Mr. Eames, a former Boston Consulting Group associate and entrepreneur at the first iteration of Quantlab. One of their first hires was Mr. Omeltchenko, who held master's degrees in physics and computer science from Moscow Institute of Physics and Technology. His hiring "changed everything for the company," according to the lawsuit by Messrs. Eames and Omeltchenko.

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U.S. EDITION

U.S. News: U.S. Workers Get Biggest Pay Raise in Nearly 10 Years

By Harriet Torry
515 words
1 August 2018
The Wall Street Journal
J
A3
English

WASHINGTON -- U.S. workers received their biggest pay increases in nearly a decade over the 12 months through June, a sign the strong labor market is boosting wages as employers compete for scarcer workers.

The Labor Department's employment-cost index rose 2.8% in the year to June, the government said Tuesday. Wages and salaries, which account for about 70% of all employment costs, also rose 2.8% from a year earlier, the strongest gain for both measures since September 2008.

Since the end of the most recent recession, U.S. unemployment has fallen to 4% in June from nearly 10% nine years earlier. Wage growth, stubbornly sluggish for years following the 2007-09 downturn, has picked up as the labor market has tightened and employers have raised pay to attract and retain workers.

It is now approaching the average pace seen in earlier periods of growth. From 2001 to 2007, wages and salaries as measured by the employment-cost index increased 2.9% a year on average, well above the 1.9% average since the second quarter of 2009 when the current expansion began.

Wage gains are coming with a modest pickup in inflation, which is eating at some of the gains for workers.

A separate report Tuesday from the Commerce Department showed inflation continues to hover near the Federal Reserve's 2% year-over-year target. The price index for personal-consumption expenditures was up 2.2% in June from a year earlier and rose 0.1% from May. Excluding **volatile** food and energy costs, prices also rose 0.1% from May and increased 1.9% from a year earlier.

Some companies are raising prices to compensate for higher commodity costs. Procter & Gamble Co. said Tuesday it was raising prices on some of its biggest brands.

Boat-engine maker Brunswick Corp. has raised average selling prices by 6% so far this year, partly in response to raw materials inflation, and the company intends to keep raising prices over the second half of the year.

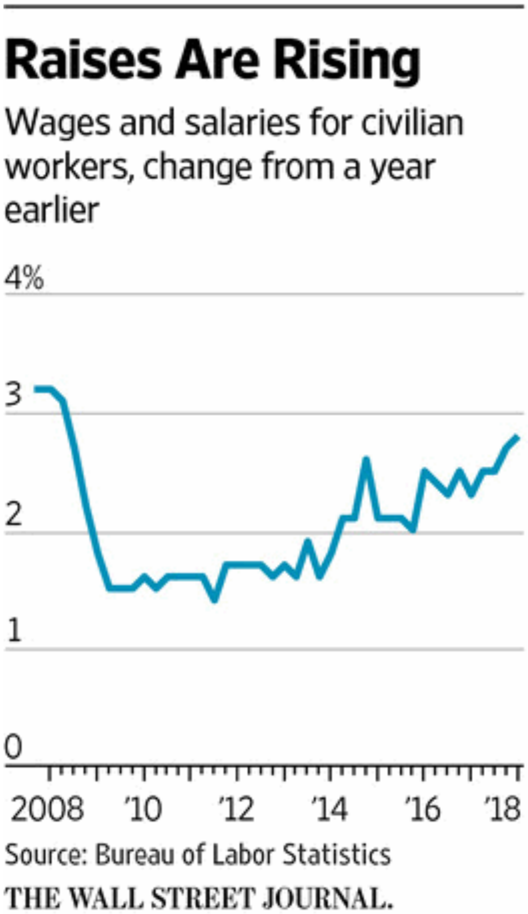
People "don't like [a] price increase, but it really hasn't affected the demand or the market," Brunswick Chief Executive Mark Schwabero said during a July earnings call.

Still, many economists said the gradual pace of price and wage increases means the overall picture for inflation and the economy remains rosy as the third quarter progresses.

A broad measure of Americans' pretax income -- including that from wages and salaries and other sources, such as investments and government payments -- rose at a solid 0.4% rate in June from May. Such household income is up about 5% from a year earlier, roughly keeping pace with the increase in consumer spending during that time.

The Conference Board on Tuesday said its index of U.S. consumer confidence rose to 127.4 in July from 127.1 in June. The index has eased from highs earlier in the year.

Eric Morath contributed to this article.



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The New York Times

Editorial Desk; SECTA
How Trump Could Be Like Reagan

By STEPHEN MOORE, ARTHUR B. LAFFER and STEVE FORBES
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1 August 2018
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23
English

President Trump won a victory for freer trade last week when he and the president of the European Commission, Jean-Claude Juncker, agreed to find ways to lower tariffs and other barriers to each other's exports. The outlines of the deal are still sketchy, but it calls for the Europeans to buy more American petroleum, soybeans and manufactured goods and for Mr. Trump to reduce his auto and steel tariffs.

We were particularly heartened that Mr. Trump and the Europeans now have a handshake agreement to aim for zero tariffs on both sides of the Atlantic.

This was Mr. Trump's idea. The night before the agreement, he proposed in a tweet that ''Both the U.S. and the E.U. drop all Tariffs, Barriers and Subsidies! That would finally be called Free Market and Fair Trade!'' Amen.

This is a winning strategy that we've long endorsed with our friends at the White House because it is fully consistent with what Mr. Trump has often told us: his threat of tariffs is a negotiating tactic to get to lower trade barriers and a ''level playing field.''

The next step should be to extend this zero tariff offer to other key allies, including Britain, Canada, Mexico and South Korea.

If Mr. Trump's goal isâ€Ž more jobs and higher wages, America comes out the big winner under the zero tariff scenario. Most of our major trading partners have higher tariffs than we do. A study by the president's Council of Economic Advisers calculates that the average American tariff is 3.5 percent, while the average European Union rate is 5 percent, China's is nearly 10 percent and the world average is around 10 percent. On a level playing field, American companies can compete with anyone, and our exporters will gain advantage if trade barriers are abolished.

The alternative is higher tariffs on steel, aluminum, autos and hundreds of products imported from other countries, particularly China. Those actions have led to retaliatory tariffs imposed on products grown or manufactured in America. This has hurt farmers, the **stock market** and economic growth.

With this new offer to abolish tariffs, Mr. Trump might be borrowing a page from Ronald Reagan's playbook. Throughout much of his presidency, Mr. Reagan was portrayed as an anti-Soviet hawk because he oversaw a huge expansion in American military spending. But at a 1986 summit in Reykjavik, Iceland, Mr. Reagan proposed to the leader of the Soviet Union, Mikhail Gorbachev, the radical idea that both countries should abolish their nuclear arsenals. This caught the Soviets by surprise, and though the two leaders left Iceland with no agreement in hand, Mr. Reagan's bold strategy ultimately laid the path to the greatest period of nuclear disarmament in history.

What Mr. Trump has proposed to our trading partners is similar: the United States will abolish all its tariffs, subsidies and other trade restraints on their exports if they do the same for American exports. This solution would be the economic equivalent to total trade disarmament.

A no-tariffs trade strategy would also allow the United States to seize the moral high ground in the debate. Mr. Trump would be transformed from the evil disrupter of international commerce to a potential savior -- just as 30 years ago Mr. Reagan's international image changed from superhawk to peacemaker almost overnight.

â€ŽFinally, if Mr. Trump can secure zero tariff deals with the European Union, Canada, Mexico, Japan and South Korea, this will put America in a much stronger position as he negotiates with China. It greatly increases the odds that Mr. Trump's hard-line stance with China will deliver long overdue concessions from Beijing that could enhance American economic and national security while averting a brutal escalation in the trade war that could hurt both our economies.

Some of our friends in the administration question whether this policy would work because in China and other countries, nontariff barriers are the biggest deterrents to American exports. We agree that nontariff trade restraints -- such as foreign companies stealing our patents with impunity, subsidies to state-owned enterprises and currency manipulation -- are a problem. But reducing tariffs creates momentum for tearing down other trade restraints.

We know lowering tariffs will be an uphill battle. Freer trade has always been an elusive pursuit because vested interests on both sides of the Atlantic, whether farmers or manufacturers, will fight to maintain tariffs that benefit their products.

We can't predict how other nations would respond to this idea. But the European Union negotiations last week should provide Mr. Trump a clear signal that he can't win just by swinging the stick of higher tariffs. He also needs to offer the carrots of lower barriers. By putting zero tariffs on the table, Mr. Trump will also be able to determine which nations are genuinely committed to freer trade and which prefer to keep their protectionist barriers in place.

We've often reminded politicians that free trade is a pillar of prosperity and a win-win for trading partners. Just as no one ever thought Mr. Reagan would stem nuclear proliferation, if Mr. Trump aggressively pursues this policy, he could build a legacy as the president who expanded world commerce and economic freedom by ending trade barriers rather than erecting them.

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