The New York Times

U.S.; Politics
**China Plans Up to $200 Billion in Trade Concessions, but Skepticism Abounds**

By Mark Landler and Ana Swanson
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WASHINGTON — President Trump, facing an economic war with China and a momentous meeting with North Korea, is considering a trade deal with Beijing that would soothe tensions and clear the way for his historic encounter with Kim Jong-un. But it would risk abandoning the president's broader goal of punishing China for years of pressuring American companies to hand over sensitive technology.

Chinese negotiators are preparing to offer the administration a deal to buy up to $200 billion worth of American goods, which would allow Mr. Trump to claim victory in his campaign to reduce the trade deficit with China and rebalance America's trade relationship with its biggest economic rival, according to people briefed on the deliberations.

But the Chinese promises would be largely illusory, economists cautioned, given the structural hurdles in China to buying more American exports and the sheer amount of goods the United States would have to produce to meet Beijing's demand.

Under the deal being discussed, China would pledge to buy substantially more American goods, including agricultural products like soybeans, as well as semiconductors and natural gas. That could theoretically reduce its trade surplus with the United States — which hit $372.5 billion last year — by up to $200 billion, though the real number would most likely be lower.

In return, China is asking the United States to set aside tariffs and investment restrictions it has threatened against Chinese companies. That includes lifting sanctions on the telecommunications giant ZTE, which faced ruin after losing access to its American suppliers, and relaxing export controls that prevent American companies from selling sensitive technology to China.

For Mr. Trump, his motive may be diplomatic as much as economic: He needs China to use its influence with Mr. Kim, who has suddenly thrown a cloud over his planned meeting with Mr. Trump in Singapore next month.

The president said Thursday that North Korea's threat to cancel the summit meeting came after Mr. Kim met for a second time in China with President Xi Jinping. That meeting occurred on May 8, just a few days before a high-level delegation from China arrived in Washington on Tuesday to try to break a deadlock on trade.

"For various reasons, maybe including trade — because they've never had this problem before; China has never had this problem with us — it could very well be that he's influencing Kim Jong-un," Mr. Trump said to reporters in the Cabinet Room, referring to the Chinese president. "We'll see what happens."

Mr. Trump insisted he would drive a hard bargain with China, noting that it had become "very spoiled" in trade negotiations with previous American administrations. But his explicit linkage of trade and the North Korea meeting — a diplomatic coup that he sees as a signature accomplishment — deepened the fears of critics that he might sacrifice his core trade agenda.

On Thursday, Mr. Trump met privately in the Oval Office with Liu He, China's vice premier and the top economic adviser to Mr. Xi, who is expected to present the trade deal to the president's advisers on Friday.

China sent mixed signals on Friday. At a daily news briefing, China's Foreign Ministry denied it had offered to reduce its trade surplus with the United States by $200 billion. At the same time, it dropped what was widely believed to be a politically motivated inquiry into sorghum imports from the United States, the latest sign of a potentially softening stance.

Mr. Trump's ability to stay focused on his broader trade agenda could be complicated by a bitter rift on his economic team. Peter Navarro, the White House trade adviser most closely identified with tough policies toward China, is being excluded from meetings with the Chinese by Treasury Secretary Steven Mnuchin, who is leading the negotiations with Mr. Liu.

The discord between the two men boiled over this month during a trip to Beijing, when they got into a profanity-laced shouting match after Mr. Mnuchin cut Mr. Navarro out of another meeting with Mr. Liu. Treasury officials said Mr. Navarro was excluded because of protocol, not because of his hard-line views, but the two men are starkly opposed on how best to deal with China.

Mr. Mnuchin, a former Goldman Sachs banker, is eager to broker a deal that would defuse a trade war with China, officials said. Mr. Navarro, an academic who has written books with titles like "Death by China," helped mastermind the investigation into whether China was stealing technology that led Mr. Trump to impose tariffs on $50 billion worth of Chinese goods and threaten levies on another $100 billion worth.

Economists say that the purchase by China of $200 billion more in American goods per year — an amount equivalent to more than half of the annual American trade deficit with China — simply is not practical. "The short answer is these are unrealistic numbers," said Chad Bown, a senior fellow at the Peterson Institute for International Economics.

Even if the Chinese stopped buying other foreign products, like Airbus airplanes from the European Union or soybeans from Brazil, and purchased solely American products, it would add up to only a small fraction of the $200 billion total they are promising to purchase.

"It would even be a stretch to get it to $50 billion," Mr. Bown said.

That is because the United States economy is already running near its full productive capacity, meaning it would not be able to produce enough new goods to meet Chinese demands, especially in the short term.

In that scenario, the United States would probably stop selling airplanes, soybeans and other exports to other countries and sell them to China instead — shrinking the United States trade deficit with China but leaving the United States trade deficit with the entire world unchanged.

And several categories of military-related equipment that the Chinese want to buy are still restricted by congressional sanctions dating back to China's bloody crackdown on protests in Tiananmen Square in 1989.

Chinese officials are pushing for greater access to American-made military systems and advanced technologies just as the Trump administration and Congress are weighing new rules that would move in the opposite direction, by curtailing that access.

As part of Mr. Trump's trade offensive, the Treasury Department has been working on new guidelines that would restrict Chinese investment in the United States, a move that officials say is needed to better police potential security threats. The Treasury is scheduled to deliver this plan to the White House by early next week, but that could be delayed or changed based on the outcome of trade talks this week.

Congress, meanwhile, is moving ahead with legislation that would expand national security checks of Chinese investment in the United States and American partnerships with Chinese companies abroad.

That legislation, led by Senator John Cornyn of Texas and Representative Robert Pittenger of North Carolina, both Republicans, could move toward a vote as early as this summer.

Trade skeptics inside and outside the administration have cautioned against agreeing to a hasty deal with China, saying it has repeatedly reneged on promises it made to past administrations.

 

The administration, for example, recently claimed a win in persuading China to restart imports of American beef after a nearly 14-year ban. But China actually announced it had lifted the ban in September 2016 under the Obama administration; it simply did not start accepting beef shipments until this year.

Skeptics say China has made similar unfulfilled promises to other administrations on issues ranging from reducing overcapacity in steel production to opening up its **financial markets**.

The president said he was not sure what to make of Mr. Kim's threat to cancel their meeting. But he went out of his way to address one of Mr. Kim's prime objections: that the United States viewed Libya as a template for ridding North Korea of its nuclear arsenal. Mr. Trump said the idea, floated by his new national security adviser, John R. Bolton, was a nonstarter.

"In Libya, we decimated that country," he said. "There was no deal to keep Qaddafi. The Libyan model that was mentioned was a much different deal. This would be with Kim Jong-un — something where he'd be there, he'd be in his country. He'd be running his country. His country would be very rich."

Mr. Trump appeared to have confused the 2003 deal under which Libya relinquished its nuclear program with the NATO-led intervention in 2011 that ended after the killing of Col. Muammar el-Qaddafi.

The president has long drawn a connection between trade and security with China — suggesting that China's help in pressuring North Korea could affect how he treated China on trade. On Thursday, he acknowledged that China was now the one using North Korea as leverage.

"President Xi could be influencing Kim Jong-un," Mr. Trump said. "If you remember, a few weeks ago, all of a sudden, out of nowhere, Kim Jong-un went to China to say hello again a second time to President Xi."

Alan Rappeport contributed reporting

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A worker at a factory in Huaibei, China. Beijing is preparing to offer Washington a package of trade concessions, but economists caution that the promises would be largely illusory. | Agence France-Presse — Getty Images | Liu He, a top economic adviser to President Xi Jinping of China, is expected to meet with Trump administration officials as the two countries try to resolve a brewing trade war. | Jason Lee/Reuters

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THE WALL STREET JOURNAL.

Business

**Kazakhstan Plans IPO of World's Largest Uranium Miner; Share sale part of efforts to open up the economy of the former Soviet republic**

By Anatoly Kurmanaev
759 words
17 May 2018
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ASTANA, Kazakhstan—Kazakhstan plans to sell at least 25% of the world's largest uranium miner this year, the centerpiece of an effort to open up the economy of the former Soviet republic sandwiched between China and Russia.

The government has hired Wall Street banks, including JPMorgan Chase & Co., to offer shares in state-owned KazAtomProm in London or Hong Kong, the head of the mining firm's holding company, Akhmetzhan Yessimov, said in an interview.

The privatization of KazAtom, which supplies about 40% of global uranium demand from the frigid Central Asian steppe, would be a major milestone for the economy of this landlocked country of 18 million people where the desire for political control has often trumped the need for private investment. It would also be closely watched in neighboring China, which will need more uranium to support the world's fastest-growing nuclear power industry.

"We want our companies to go public," said Mr. Yessimov. "This is a priority."

The privatization of KazAtom would also shake up the concentrated uranium industry, potentially altering the market's status quo of prioritizing prices over output levels, said Justin Chan, a mining analyst at Numis Securities in London. "The strategic outlook of private shareholders may not always align with the state," he said.

Kazakhstan, which became independent from the Soviet Union in 1991, has since been ruled by the former Communist apparatchik Nursultan Nazarbayev, who has maintained a close alliance with Russia. In recent years, Mr. Nazarbayev has also sought closer ties with China to exploit its economic growth and provide a geopolitical counterweight to the Kremlin.

The Kazakh government has touted KazAtom's privatization for years, but delayed it repeatedly because of poor market conditions or energy security concerns. Mr. Nazarbayev decided in April to list the miner in the second half of this year, Mr. Yessimov said. The ministers of economy and finance have confirmed the IPO's schedule and details in separate interviews on the sidelines of Astana's annual economic summit.

"This has received final approval," said Mr. Yessimov, who runs Kazakhstan's sovereign-wealth fund, Samruk Kazyna, which owns KazAtom. "Everyone in the elite understands this has to be done" to make the country more competitive.

Mr. Yessimov said he traveled to China this month to follow-up on strong interest in the KazAtom IPO from the country's investors. Next week he will present the privatization plans to investors in Russia.

Kazakh officials have been coy about estimating the value of the sale, saying the exact timing and size has yet to be decided. But based on KazAtom's last financial figures and the premium paid by investors on the country's other recently privatized companies, a 25% stake in the uranium producer could be worth about $3.5 billion, making it one of the biggest industrial IPOs this year. This would represent 13% of the country's entire budget for this year.

JPMorgan declined to comment on its involvement in the IPO.

Officials hope the listing of KazAtom, the country's second-biggest conglomerate employing 27,000 people, will be the opening salvo of the biggest wave of privatization in the former Soviet Union since the 1990s. This year the government also plans to sell stakes in national airline Air Astana and phone operator KazakhTelecom, four top Astana officials said separately. Up to sixty other big state companies will follow suit by 2021, including the nation's biggest firm, oil producer KazMunayGas, the officials added.

Kazakhstan's economic liberalization plans buck a trend of growing protectionism from the U.S. to Russia.

"We don't believe that protectionism is good," said Economy Minister Timur Suleimenov. "You can't shield yourself from the world."

Still, Kazakhstan's privatization drive faces many hurdles. One issue has been Mr. Nazarbayev's insistence that big state companies are first listed on the yet-to-launch Astana Stock Exchange to boost local capital markets, before selling shares abroad. In private, many officials are skeptical that the **stock market**—set to launch in July—will have liquidity to support big companies like KazAtom, let alone a share of $38 billion behemoth KazMunayGas.

Some in Kazakhstan are also concerned that selling strategic industries like uranium to Chinese or other foreign investors would reduce Kazakhstan's diplomatic bargaining power in the region.

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THE WALL STREET JOURNAL.

Business

**Oil Is Above $70, but Frackers Still Struggle to Make Money; Most of top 20 shale-oil producers spent more than they made in first quarter**

By Christopher M. Matthews and Bradley Olson
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American shale drillers are still spending more money than they are making, even as **oil prices** rise.

Of the top 20 U.S. oil companies that focus mostly on fracking, only five managed to generate more cash than they spent in the first quarter, according to a Wall Street Journal analysis of FactSet data.

Shale companies have helped propel U.S. oil output to all-time highs, surpassing 10 million barrels a day and rivaling Russia and Saudi Arabia. But the top 20 companies by market capitalization collectively spent almost $2 billion more in the quarter than they took in from operations, largely due to bad bets hedging crude prices, as well as transportation bottlenecks, labor and material shortages that raised costs.

Many of the producers did better to start this year than at any point since 2014, when **oil prices** began a crash that the industry is fully recovering from only now. Still, the companies spent about $1.13 for every $1 they took in. Oasis Petroleum Inc. spent $3.27 for every $1 it made in cash, while Parsley Energy Inc. spent almost $2 for every $1 it made in cash, according to FactSet.

While many shale operators have positive net income this year, many shareholders have begun paying closer attention to how much the companies are spending, as they seek to compel them to live within their means and begin to produce stronger returns.

Hedging played a big role in companies' underwhelming cash generation. Seeking stability after years of wild fluctuations in crude prices, many operators entered into derivatives contracts in late 2017 that effectively ensured they could sell some of their 2018 output for $50 to $55 a barrel. Now that prices have risen to more than $70 a barrel, many are failing to capture the value of the rally. WPX Energy Inc. reported an adjusted net loss of $30 million last quarter, which it said was driven by $69 million in losses on its hedges due to higher **oil prices**.

Some companies are already adjusting their strategies because of higher **oil prices**. Parsley Energy, which is focused on the Permian Basin, the oil field in Texas and New Mexico that is currently the center of U.S. shale-drilling activity, hedged most of its 2018 production. It plans to change that going forward, and expects to generate more cash relative to spending in coming quarters.

"Early signs of labor tightness motivated Parsley Energy to increase drilling and completion activity significantly last year when rigs and crews were easier to come by," said Parsley Chief Executive Bryan Sheffield. "[N]ow that we are operating at a steady development pace, we should continue to generate increasing cash flow."

Continental Resources Inc., which is primarily active in shale formations in North Dakota and Oklahoma, didn't hedge its oil production for 2018. It raked in almost $258 million in cash after expenses in the first quarter, best among its peers.

If U.S. crude prices stay at about $70 a barrel for the rest of 2018, energy consultant Wood Mackenzie estimates that hedging strategies would reduce annual revenue by an average of 7% for six companies focused on the Permian basin.

Investors remain broadly hopeful that shale companies' performance will improve in 2018 due to rising **oil prices** and global demand. But concerns about the companies' ability to manage expenses linger.

"These companies have done well this year and they are saying the right things," said Tyler Rosenlicht, a senior vice president at Cohen & Steers, which manages about $60 billion in assets. "But a lot of investors were so burned down in the past that there will be a longer pause before they feel fully comfortable again."

EOG Resources Inc., the biggest U.S. shale producer, reported first-quarter profit of $638 million, a more than twentyfold increase over the prior year. But its cash surplus compared with spending was $110 million for the period. Its stock has risen about 9% this year, while U.S. crude prices are up 17% in that time.

Shale producers failed to generate cash even as one of their primary obstacles to profitability in past years, oil-field-services costs, rose only modestly.

While trucking and labor shortages in the Permian are already vexing many companies, some costs related to drilling contractors have increased by 15% or less because rates were locked in last year when **oil prices** were low. But those costs could climb further later this year, analysts say.

Shale companies' profitability may also be threatened by rising costs for the immense amounts of sand and water needed for fracking. Modern fracking jobs now require 500 tons of steel pipe, enough water to fill 35 Olympic swimming pools and enough railcars filled with sand to stretch for 14 football fields, according to Rice University's Center for Energy Studies.

Many companies may be forced to choose between hitting production targets, and promises to investors to keep spending in check, said James West, an analyst at Evercore ISI.

"Service pricing is going to hit them like a brick wall," he said. "I'm personally not convinced [they will] stick to capital discipline. In their heart of hearts, they just want to grow."

Write to Christopher M. Matthews at christopher.matthews@wsj.com and Bradley Olson at Bradley.Olson@wsj.com

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Heard on the Street
Markets

**Kroger's Big, Risky Bet on Grocery Delivery; The U.S. grocery chain is planning to roll out 20 highly automated warehouses using robotics developed by U.K. online supermarket Ocado**

By Stephen Wilmot
609 words
17 May 2018
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The Wall Street Journal Online
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English


Kroger is betting that robots will give it an edge in the food fight with Walmart and Amazon. Investors can expect a long receipt.

U.K. online supermarket Ocado announced a deal Thursday to share its technology exclusively with Kroger, which trails only Walmart in the $650 billion U.S. grocery market. Online grocery delivery is expensive and inefficient, and Ocado may be the world's leader in automating the process, which could give Kroger a boost against its rivals. Ocado's most modern warehouse in South East England uses robots to pick groceries from a giant hive of boxes—a high-tech, high-spec solution that is expensive to set up but promises huge savings versus human pickers once operated at scale.

Kroger is committing to roll out this technology across up to 20 warehouses over three years. In exchange Ocado will stop discussions with Kroger's rivals. The two partners will hammer out the finer details over the coming year. The agreement is cemented by a shareholding: Ocado will issue roughly $250 million worth of new stock to Kroger, increasing its stake to 6% from 1%.

Ocado's ever-**volatile** stock was up an extraordinary 48% in morning trading in London, giving the company a market value of $7.4 billion. With a history of promising industrial revolution but delivering modest profits, the company has long attracted short-sellers, who may now be rushing to cover their positions. Roughly 7% of the shares were out on loan Wednesday, according to Financial Conduct Authority data.

Americans haven't yet embraced shopping for food online in the way Europeans have. Web orders accounted for just 1.5% of grocery sales in the U.S. last year, compared to 7.5% in the U.K., according to Kantar Worldpanel. That may be because it remains expensive, with orders typically fulfilled by personal shoppers via platforms like Instacart. Ocado's technology should help Kroger bring down the price of delivery, encouraging adoption and giving it an edge over the current leaders Amazon and Walmart.

Amazon is furthest ahead in the U.S. online grocery race, with an 18% market share in the first quarter, according to data provider One Click Retail. But it mainly sells coffee-machine pods and other non-perishable items. Until it bought Whole Foods last year, Amazon didn't have the scale in grocery necessary to justify automating fresh-food orders in the way it has automated orders of other goods. With a 9% market share, Walmart is also investing heavily in e-commerce, but has not automated picking. Kroger's bet on robotics may force its larger peers to rethink their strategies.

For Kroger investors, the risk is an expensive race for scale in a market that remains barely profitable even for Ocado in the U.K. A nationwide rollout of e-commerce warehouses furnished with advanced robotics implies substantial capital spending. Fortunately, investors already fear the worst after Kroger unveiled big spending plans alongside its fourth-quarter results in March, sending the shares down 12%. The company said Thursday the Ocado deal was already factored into its earnings guidance for this year and next, though this doesn't rule out an increase in capital spending.

The deal with Ocado may give Kroger an advantage in the grocery-delivery race, but winning the contest and profiting from the victory are two different things.

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Markets
**Emerging-Market Currencies Fall Against Dollar; Worries percolate that U.S. bond yields will keep rising**

By Ira Iosebashvili
239 words
17 May 2018
06:37 PM
The Wall Street Journal Online
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English


A range of emerging-market currencies fell against the dollar, pressured by worries that bond yields in the U.S. will continue rising.

Late Thursday in New York, the dollar rose 0.6% against the Brazilian currency to 3.6965 reais, its highest level in more than two years. It rose 1.1% against the Turkish lira to hover near a fresh high, and notched gains against the South African rand, Russian ruble and other currencies.

The yield on the **10**-**year Treasury** note settled at a multiyear high of 3.109%, from 3.093% Wednesday. Rising U.S. yields tend to diminish the attractiveness of emerging markets, where investors often assume higher risk in the hopes of richer returns.

Expectations of higher prices for oil, copper and other raw materials exported by many emerging markets have helped mitigate the dollar's gains in recent days, analysts said.

The WSJ Dollar Index, which measures the currency against a basket of 16 others, rose 0.2%, to 87.02, its highest closing level this year. The U.S. currency gained 0.3% against the Japanese currency to ¥110.77, while the greenback advanced 0.1% versus the euro to $1.1794. The British pound rose 0.2% to $1.3516.

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THE WALL STREET JOURNAL.

Markets

**Brent Crude Hits $80 Amid Concerns Over Iran Supply; Thursday's gains come as European companies pull back from Iran**

By Sarah McFarlane and Alison Sider
656 words
17 May 2018
03:50 PM
The Wall Street Journal Online
WSJO
English


Brent crude prices pared gains to settle near unchanged after hitting $80 a barrel Thursday, as Washington's decision to reinstate sanctions on Iran continued to fuel a rally that has pushed the market to 3 1/2 -year highs.

Brent crude, the global oil benchmark, settled up 2 cents at $79.30 a barrel on London's ICE Futures exchange, having earlier moved past $80, its highest level since November 2014. On the New York Mercantile Exchange, West Texas Intermediate futures settled unchanged at $71.49 a barrel after earlier climbing above $72 a barrel.

"We might have seen a little profit-taking," said Eugene McGillian, research manager at Tradition Energy, adding that the strong dollar may have dented oil's rise. Oil and the dollar often move in opposite directions, since a stronger dollar makes oil more expensive for buyers using foreign currencies.

But with **oil prices** up more than 18% this year, some are starting to question whether demand will take a hit. Michael Hewson, chief market analyst at CMC Markets, said he's expecting **oil prices** to remain in a range of $72 to $85 a barrel, and "wouldn't rule out" $90 Brent this year.

"The only reason that will stop it from going higher is demand destruction, ultimately people will use it less and consumption will go down," he said.

Thursday's earlier gains came as European companies pull back from Iran. European countries had said they would stand by the 2015 international nuclear agreement that saw sanctions against Iran eased in return for Tehran curbing its nuclear program. Washington dropped out of that pact last week, sending oil sharply higher on the belief that Iranian supply will be curbed, when crude inventories are already falling.

If European companies pull out of investments, Iran will question the point of sticking by the agreement, said Amrita Sen, analyst at consultancy Energy Aspects.

"There's a minimum of 400,000 barrels per day of Iranian exports at risk," Ms. Sen added.

The U.S. has said it is possible there will be secondary sanctions imposed on European companies who continue to deal with Iran.

French energy major Total SA said Wednesday that it would withdraw from a major gas project in Iran before November if it wasn't granted a waiver by the U.S. Total had signed a $1 billion deal to develop Iran's South Pars field.

"As soon as the U.S. put back secondary sanctions, there's no opportunity for us," Total Chief Executive Patrick Pouyanne said Thursday.

Any barrels lost from Iran will exacerbate an already tight market—the International Energy Agency said Wednesday that oil stockpiles in industrialized economies fell to their lowest level in three years and dipped below the five year average level for the first time since 2014.

And investors are losing faith in U.S. producers' ability to replace falling output elsewhere in the world. Pipeline congestion in the most prolific U.S. oil field is becoming a bottleneck that could slow output, which could end up boosting global **oil prices**, analysts at Tudor Pickering Holt said.

"We do not expect that U.S. shale producers will be able to fill the volumes lost as Iran sanctions are re-imposed and Venezuelan exports decrease further than they already have," analysts at Height Securities said.

Gasoline futures fell 0.3% to $2.2431 a gallon. Diesel futures rose 0.51% to $2.2808 a gallon.

Timothy Puko contributed to this article.

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U.S. Markets
Markets

**U.S. Stocks Retreat on Trade Worries; Walmart and Cisco Systems lead blue chips lower**

By Michael Wursthorn and Riva Gold
720 words
17 May 2018
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The **Dow Jones Industrial Average** fell Thursday as investors seemed unfazed by upbeat earnings and more concerned with renewed trade tensions that could disrupt the global economic upswing that has fueled the **stock-market** rally.

Walmart and Cisco Systems led the blue-chip index lower, despite reporting strong quarterly earnings. Their declines continued a worrisome trend that suggests company earnings may not get much better in upcoming quarters, sapping the **stock market** of a crucial pillar of support.

Meanwhile, investors were spooked by the continuing trade negotiations. Earlier in the day, President Donald Trump demurred on how negotiations would turn out, saying China and other countries have become "very spoiled."

With little to work with, major indexes failed to gain traction.

"President Trump's comments today have contributed to a continued lack of clarity on trade," said Emily Roland, head of capital markets research at John Hancock Investments. "There's this cloud of geopolitical uncertainty that's overshadowing the fact that we have a fairly sturdy backdrop in the U.S."

The **Dow Jones Industrial Average** fell 54.95 points, or 0.2%, to 24713.98, while the **S&P 500** slipped 2.33 points, or 0.1%, to 2720.13 and the **Nasdaq Composite** lost 15.82 points, or 0.2%, to 7382.47.

Shares of Cisco Systems, an index heavyweight that had been a major contributor to the **S&P 500** this year, were punished after the networking giant offered earnings guidance late Wednesday that wasn't much better than analysts' expectations, despite the strong IT spending backdrop.

Cisco has been having a bigger impact on the market-cap-weighted **S&P 500** this year due to its size and because its stock has been among the best performers of the year. Before Thursday, the tech company had contributed more than 6% of the broad index's small gain for the year, according to S&P Dow Jones Indices.

Shares fell $1.70, or 3.8%, to $43.46 Thursday and dragged down shares of other communications equipment providers on a day when other popular tech stocks like Apple and Google parent Alphabet also edged lower.

Cisco's plight exposes a key weakness in the market right now: the reliance on technology companies to move major indexes higher. Just a handful of companies, like online retailer Amazon.com and streaming-service provider Netflix, as well as Cisco, are mostly holding the **S&P 500** up, according to S&P Dow Jones Indices data.

Their weakness in February, when stocks first entered correction territory on fears of out-of-control inflation, and in March, when Facebook's data mishap was revealed, pulled major indexes into negative territory, while their gains have helped stabilize the **stock market**.

"There's still a narrow breadth in the market," said Zhiwei Ren, managing director at Penn Mutual Asset Management. "This kind of position is worrisome…nothing goes on forever."

Meanwhile, shares of Walmart fell 1.64, or 1.9%, to 84.49 even after it said sales in its latest quarter rose both online and in stores. While the economy has gained strength, Walmart Chief Financial Officer Brett Biggs told The Wall Street Journal that shoppers are already feeling the effects of rising **oil prices**.

**Oil prices** continued their climb, sending energy shares in the **S&P 500** up more than 1%, the most of any other sector on Thursday.

Energy companies in the **S&P 500** have added 16% since the end of March, outperforming the 10 other sectors in the broad index, including shares of technology companies, which are up 6.2% over the same time.

Elsewhere, stocks in Hong Kong and Australia closed lower, while Japan's Nikkei rose 0.5%, supported by a recent decline in the yen. The Stoxx Europe 600 edged up 0.7%.

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THE WALL STREET JOURNAL.

Markets

**Strong Earnings? Don't Expect the Market to Rally; U.S. and European stock markets tend to do worse after a bumper earnings seasons than a disappointing one, WSJ analysis finds**

By Mike Bird
758 words
17 May 2018
07:00 AM
The Wall Street Journal Online
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English


U.S. companies have posted great earnings, but investors shouldn't count on that giving their stocks a particular boost.

That is the counterintuitive conclusion from the past seven years, when U.S. and European stock markets tend to do worse after a bumper earnings seasons than a disappointing one, according to a Wall Street Journal analysis.

Companies on the **S&P 500** have just posted their best quarter of earnings, and the largest overshoot of analyst expectations, since 2010. The index, though, has returned 3.3% since the end of the first quarter, no different to stocks in Europe and Japan, which had much less impressive earnings growth.

At the turn of the year, analysts expected net income growth of around 10% in the first quarter of 2018. But with the vast majority of **S&P 500** companies reporting, net income is up nearly 25%.

In quarters that followed forecast-beating earnings in the past seven years, the **S&P 500** returned only 2.4% on average. When earnings undershot estimates, the index returned an average of 3.8%.

The difference is even starker in Europe. Since 2011, in quarters that followed Stoxx Europe 600 companies posting stronger-than-expected earnings, returns have actually been slightly negative on average.

That could be for a simple reason: Earnings reflect the recent past, while investors are preoccupied with what is to come. At the moment investors have a lot to keep them cautious, including interest rate increases and potential trade protectionism.

"All of 2017, with the strong **stock price** gains was all premised on what we have today, basically a Goldilocks environment for stocks," said Robert Pavlik, senior portfolio manager at SlateStone Wealth.

But now, rate increases will raise borrowing costs for businesses and crimp consumer demand, he said.

"Investors have instead focused on future earnings guidance, which has been more cautious," said Sameer Samana, global equity strategist at Wells Fargo Investment Institute. "We can see why companies would be cautious in their forecasts, as exact details on key issues, such as tariffs, have not yet been released."

Earnings guidance led stocks in manufacturers like 3M Co. and Caterpillar Inc. lower on days when they posted higher than expected earnings. Executives at Caterpillar characterized the first quarter as a "high watermark for the year" on their earnings call and said the heavy machinery maker didn't expect to see operating margins at the same level.

This year, analysts expect earnings per share to rise 20% for the **S&P 500** and 9.3% Stoxx Europe 600, according to FactSet data.

Many analysts have said the U.S. tax overhaul had an impact on first-quarter earnings, saying that the outperformance may reflect a one-time boost rather than sustained higher growth. Pretax profit growth beat expectations by more like 3%, according to Bank of America Merrill Lynch.

Other factors—changes in bond yields, the direction of economic data, geopolitical risks—boost or weigh on stocks. The strength of the economy will eventually move earnings, but won't be immediately reflected in year-over-year growth.

"Away from earnings, investor sentiment appears to have been affected by a combination of rate concerns and continued elevated **volatility**," said Barclays credit analysts in a recent research note. The analysts also noted that stronger earnings data, which should also be a positive for corporate debt, hadn't caused spreads on corporate bonds—the yield premium compared with Treasurys—to tighten.

The Cboe Market **Volatility** Index, or VIX, remains above its 2017 average level and inflation-linked U.S. Treasury bonds indicate investors are demanding more protection against rising prices than at any time since 2014.

That doesn't mean earnings don't matter for the performance of stocks.

In dollar terms, net profit for companies in the **S&P 500** has risen by nearly 50% in the last 10 years but earnings are down by 15% on the Stoxx Europe 600. That helps to explain why the U.S. index has outperformed its European counterpart by more than 100% over the same period.

"In the very long run earnings matter, but in any given quarter to use as a measure for how stocks will perform just doesn't work," said Fahad Kamal, senior market strategist at Kleinwort Hambros.

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THE WALL STREET JOURNAL.

Business

**Maersk to Cut Services as It Battles Shipping Glut; The container operator's first-quarter loss widened amid falling freight rates and rising trade risks and fuel costs**

By Costas Paris and Ian Walker
489 words
17 May 2018
12:53 PM
The Wall Street Journal Online
WSJO
English


A.P. Moller-Maersk A/S said it would cut back on capacity to combat falling freight rates and rising fuel costs, after the Danish shipping giant reported a weak first quarter that sent its shares down about 8%.

The world's biggest container operator said its underlying loss widened to $239 million from a loss of $139 million a year earlier, with Chief Executive Soren Skou blaming rampant overcapacity as the main culprit and warning that a trade war between the U.S. and China would dash any hopes of a recovery in the shipping industry after a long down cycle.

"In the short term we will be closing down some services," Mr. Skou said in an interview. "Overcapacity is the biggest defect."

Maersk shares were down 7.9% to 9,350 Danish kroner (about $1,480) on the Copenhagen Stock Exchange.

Maersk reported a net profit of $2.75 billion, compared with a profit of $245 million in the same period last year, but the gain came from the sale of two units, Maersk Oil and Maersk Tankers.

Mr. Skou said higher fuel prices had added $70 to the cost of shipping a container from Asia to Europe and across the Pacific. Maersk currently moves more than 4 million containers, or 19% of global capacity.

Freight rates between Asia and Europe hover around $780 per box, about half the $1,500 break-even level.

Maersk reiterated previous guidance that it expects 2018 underlying profit to be above the 2017 figure of $356 million, but Mr. Skou said that depends on growing geopolitical risks.

"A trade war between the U.S. and China would be very, very bad," he said, adding that new U.S. sanctions on Iran are "a driver" for rising **oil prices**.

"Costs are rising overall and becoming inflationary. That's not what we are used to," Mr. Skou said.

He said Maersk leases or charters around 400 ships from a total of 750 in operation and that a number of them would be returned to their owners.

Maersk bought German competitor Hamburg Süd for $4 billion last year, which expanded its network by around 30%, while cargo volumes have grown by 24%.

Mr. Skou said Maersk would stop moving cargo to and from Iran, fearing repercussions from Washington.

"No shipping line that operates globally will be able to do business in Iran if the sanctions come to full force the way they intend to," he said.

Container ships move the vast majority of manufactured goods and Maersk's performance is seen as a barometer of the health of global trade.

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Economy

**Quick Hits: PBOC Purchased Net 7.42 Billion Yuan of Forex in April; In parts of the U.S. Farm Belt, bankers are denying more loans, according to the Kansas City Fed**

By WSJ Staff
1,075 words
17 May 2018
03:17 PM
WSJ Pro Central Banking
RSTPROCB
English


The People's Bank of China bought 7.42 billion yuan worth of foreign exchange in April, and the Reserve Bank of New Zealand closed its building following the discovery of asbestos in an air-quality test. Here are quick hits on central banking and related market views from around the world.

PBOC Purchased Net 7.42 Billion Yuan of Forex in April

China's central bank bought a net 7.42 billion yuan ($1.16 billion) worth of foreign exchange last month, following net purchases of 7.84 billion yuan in March, according to official data released Thursday. The People's Bank of China said its total foreign-exchange purchase position stood at 21.503 trillion yuan at the end of April—the fourth consecutive month it has increased. China's foreign-exchange reserves dropped to a five-month low in April, mainly due to valuation effects from a strengthening U.S. dollar, according to central bank data released earlier.

Liyan Qi

RBNZ Moves to Clear the Air

The discovery of asbestos in an air-quality test has prompted New Zealand's central bank to close its building for further inspection. While essential operations continue, such events can be disruptive. "As a responsible employer and landlord, we decided to take the precaution of closing the building to inspect all levels and confirm that there is no risk to human health," a spokesman says.

James Glynn

Rate-Rise Calls Grow in India on Oil Surge

Standard Chartered is the latest to predict a rate increase in India next month as concerns about inflation grow. It sees consecutive quarter-point moves in June and August after predicting no policy moves previously. StanChart's fiscal year inflation forecast rises to 4.8% from 4.45% as oil hits repeated 3 1/2-year highs and the rupee continues to slide.

Anant Vijay Kala

ANZ Drops View of Another 2018 Rate Increase in Malaysia

ANZ Research now sees Malaysia's central bank standing pat the rest of the year, reversing its call for a quarter-point rate rise in September. First-quarter gross domestic product growth came in just short of consensus, though still healthy at 5.4%. ANZ's full-year target remains 5.7%, but the bank says risks are now to the downside on that as investment activity may slow further following the change in government.

Yantoultra Ngui

History Says Turkey Should Raise Rates, But It Likely Won't: UniCredit

UniCredit says **volatility** in USD/TRY has recently risen to as high as it was in early 2017, when the Central Bank of the Republic of Turkey raised interest rates. But while precedent suggests that "many signals are in place that speak for an emergency CBRT rate hike," strong opposition from the government and particularly President

Recep Tayyip Erdogan makes the prospect less likely this time around. The Turkish lira is set to fall even further if U.S. 10-year Treasury yields continue to rise, UniCredit says.

Olga Cotaga

Bankers Deny More Loans in Parts of Farm Belt

Bankers in parts of the Midwest are denying more farm loans as a yearslong slump in the agricultural economy stretches into its fifth year, according to the Federal Reserve Bank of Kansas City. The Fed said lenders in its district—which includes states like Kansas and Nebraska—denied more than 8% of farm loan requests in the first quarter of 2018 due to insufficient cash flow, an increase from previous years. The biggest share of denials came in Oklahoma, a state where farmers rely heavily on income from wheat, which has seen prices drop sharply in recent years. The Fed said farm incomes and financial conditions deteriorated for a fifth consecutive year, though higher crop prices and lower land-rental rates could help boost farmers' profit margins.

Jesse Newman

Risk of Fed Raising Rates Too Fast: Brandywine Global

A major challenge for central bankers, particularly in the U.S., is to find the appropriate level for short-term rates and properly estimate the impact on the longer end of the yield curve, Gary Herbert, portfolio manager at Brandywine Global Investment Management tells Dow Jones Newswires in an interview in Frankfurt. "One of the things we are worried about is that the [Federal Reserve] will raise rates too aggressively and that we go beyond 2.25%-2.50% [in the federal-funds rate]," he says. This would start to make U.S. Treasurys look very attractive in comparison to equities. Brandywine Global therefore hopes for a "slow, deliberate" rate increase, with the Fed being "more mindful" of the strengthening of the U.S. dollar than it has been recently.

Emese Bartha

Eurozone Ready to Function Without QE: Brandywine Global

Asset purchases by the European Central Bank "need to end sooner rather than later" and the ECB needs to normalize rates, Gary Herbert, portfolio manager at Brandywine Global Investment Management tells Dow Jones Newswires in an interview in Frankfurt. The eurozone economy is "as ready as it can be" to manage without the ECB's asset purchases, he says. When there is growth, "in my view it would be prudent for central bankers to stop distorting capital markets and arbitrarily keeping yields low." The ECB's asset purchases run through end-September at a pace of €30 billion ($35.4 billion) a month. Market participants expect the ECB to decide in July—with June now a less likely scenario—about how it will proceed with QE after September.

Emese Bartha

ECB Lowers ELA Cap for Greek Banks

The European Central Bank has lowered the cap on emergency liquidity assistance, or ELA, to Greek banks by €2.5 billion ($3 billion) to €12.2 billion, the Bank of Greece says. The move reflects improved liquidity and takes "into account flows stemming from private sector and from the banks' access to wholesale financial markets," it says. Greek banks were forced into ELA in 2015 after the ECB suspended an exemption that allowed banks to use speculative grade-rated Greek government bonds as collateral for regular ECB loans.

Nektaria Stamouli

(Most of the items in this column come from Market Talk, a feature of Dow Jones Newswires that provides real-time analysis of news developments and market activity.)

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THE WALL STREET JOURNAL.

Heard on the Street
Markets
**No FDA Seal of Approval for These Big Biotechs; List of companies that block generic competition, including Celgene and Biogen, should remind investors how fragile biotech profits are**

By Charley Grant
310 words
17 May 2018
01:11 PM
The Wall Street Journal Online
WSJO
English


Investors got another reminder that profits at large biotech companies are fragile.

The Food and Drug Administration published a list of companies Thursday that it says employ "gaming tactics" to delay generic competition for branded drugs.

The FDA's list of 52 drugs includes blockbuster treatments for serious diseases. High-profile examples include Celgene's cancer drugs Revlimid and Pomalyst as well as Biogen's multiple sclerosis drug Tecfidera.

Celgene's drugs appearing on the list accounted for 75% of its sales in the most recent quarter, while Tecfidera made up nearly a third of Biogen's top line.

Dependency on a few vulnerable medications is reflected in those companies' earnings multiples. Celgene and Biogen trade at just nine and 11 times forward earnings, respectively, according to FactSet. The **S&P 500**, meanwhile, fetches about 17 times.

One saving grace for shareholders is that the FDA has no meaningful legal recourse to curtail this kind of behavior so Thursday's action doesn't immediately imperil profits. Even so, the publication of this list underscores the reality that these companies have more uncertain profitability outlooks than headline financial projections suggest.

Analyst consensus calls for Tecfidera and Revlimid sales to hold steady through at least 2022, according to FactSet. That is a bold assumption since generic developers might eventually have more meaningful legal recourse in response to delay tactics from branded companies. Legislation known as the Creates Act, which would enable developers to sue for access to drug samples needed to get generics approved, has 22 co-sponsors in the Senate.

That peril should keep these companies in the bargain bin for now.

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WSJ PRO CENTRAL BANKING

Economy

**Fed's Kashkari: No Sign of Notable Financial Bubble; Minneapolis Fed president didn't comment on monetary policy or economic outlook**

By Michael S. Derby
136 words
17 May 2018
12:08 PM
WSJ Pro Central Banking
RSTPROCB
English


Federal Reserve Bank of Minneapolis President Neel Kashkari said Thursday he isn't seeing any signs right now of looming **financial market** distress.

"We don't see a big bubble on the national economy," Mr. Kashkari said in brief comments at an event in St. Paul, Minn. He didn't comment on monetary policy or the economic outlook in his remarks.

Mr. Kashkari reiterated that he believes the job market may have less slack in it than suggested by the current 3.9% jobless rate, and that may help explain why wage growth has been relatively modest so far.

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WSJ PRO CENTRAL BANKING

Economy

**U.S. Jobless Claims Rise, But Hover Near Recent Lows; Number of people filing continuing unemployment benefit claims declined by 87,000 in the week ended May 5**

By Paul Kiernan
309 words
17 May 2018
11:34 AM
WSJ Pro Central Banking
RSTPROCB
English


WASHINGTON—The number of U.S. workers filing applications for jobless benefits went up more than expected last week but remained at historically low levels amid signs that economic growth remains firm.

Initial jobless claims, an indication of layoffs, increased by 11,000 to a seasonally adjusted 222,000 in the week ended May 12, the Labor Department said Thursday. That was more than the 215,000 claims forecast in a survey of economists by The Wall Street Journal.

Economists chalked up the rise to normal **volatility** and noted that more stable measures of jobless claims continued to show a downward path.

"This disappointment came after very favorable readings in each of the prior three reported weeks," JPMorgan Chase economist Daniel Silver said in a note to clients. "The trend in the data still looks upbeat and points to improvement in the labor market between the reference weeks for the April and May payroll reports."

The four-week moving average of claims fell last week to its lowest level since 1969 The number of continuing unemployment benefit claims—those drawn by workers for more than a week—declined in the week ended May 5 to their lowest level since 1973. Continuing unemployment benefits are reported with a one-week lag.

Declining jobless claims jibe with recent survey-based data showing that the unemployment rate fell in April to its lowest level, 3.9%, since late 2000.

"The signal being flashed by claims is that further declines are likely in the jobless rate," said Joshua Shapiro, chief U.S. economist at MFR Inc., in a note to clients.

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THE WALL STREET JOURNAL.
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**Argentina's Woes Trip Up Big Investors**

By Julie Wernau and Ira Iosebashvili
735 words
17 May 2018
The Wall Street Journal
J
B12
English


Argentina's ailing currency and **stock market** are pounding funds managed by some of the world's biggest investors, including Fidelity Investments, T. Rowe Price Group Inc. and Morgan Stanley, reversing some of the outsize gains they enjoyed last year.

These investment firms often own Argentine stocks through specialized funds that invest in some of the world's least developed countries, known as frontier markets, or through Latin American funds. Because Argentina's stocks represent about 19% of the MSCI Frontier Markets Index, even money managers that have positions at less than the index weighting still have significant exposure to the country's stocks and have taken a beating.

Frontier markets funds at T. Rowe Price, Morgan Stanley and Ashmore Group PLC have 16% or more of their portfolios in Argentine stocks, according to Morningstar data. Their funds have suffered declines between 5% and 8% over the past month, Morningstar said. Emerging markets and Latin America-focused stock funds at Fidelity, BlackRock Inc. and Eaton Vance Corp. are also down between 2.5% and 5%, in large part because of their holdings in Argentina stocks.

The Argentine peso's sudden collapse this year seemed to catch even longtime investors off guard.

"We went into a meeting, the peso was down 1%, we come out and the peso is down 5%," said William Pruett, portfolio manager for the Fidelity Latin America Fund.

The dollar rose nearly 9% against the Argentine currency on Monday. The peso has rebounded a bit since then, but is still down 17% since late April, when the country began intervening in currency markets.

Many investors decided to sell before the central bank tried to roll over about $30 billion in short-term, peso-denominated securities known as Lebacs on Tuesday, as any signs that the government was having trouble refinancing this debt would further rattle investor sentiment and punish Argentina's **financial markets**. The government said late Tuesday that 100% of the expiring debt was successfully covered.

Many of the big investment firms increased their bets on Argentina's stocks and bonds last year, when investor optimism surged with the new, business-friendly government led by President Mauricio Macri.

Argentina resolved a 15-year-long dispute with creditors in 2016 and returned to markets with a $16.5 billion bond offering, which at the time was the largest-ever debt sale for a developing country. Last year, the government sold 100-year bonds with a yield of only 7.9%.

The country's **stock market** rose 77% in 2017, while local-currency bonds offered yields of about 20%.

Those returns attracted investors who didn't normally invest in frontier markets but they did so in Argentina near the end of last year, following capital-market overhauls and midterm elections that reaffirmed support for Mr. Macri.

Many of these investors also were betting that MSCI would elevate Argentina to its Emerging Markets Index, which includes more advanced developing countries and would likely bring more money into Argentine stocks from investment firms that follow the index. Those new inflows caused the country's proportion of the MSCI Frontier Markets Index to balloon to 24% last year, as stocks surged.

Now, some dedicated frontier managers say, the more opportunistic investors are fleeing as quickly as they came in.

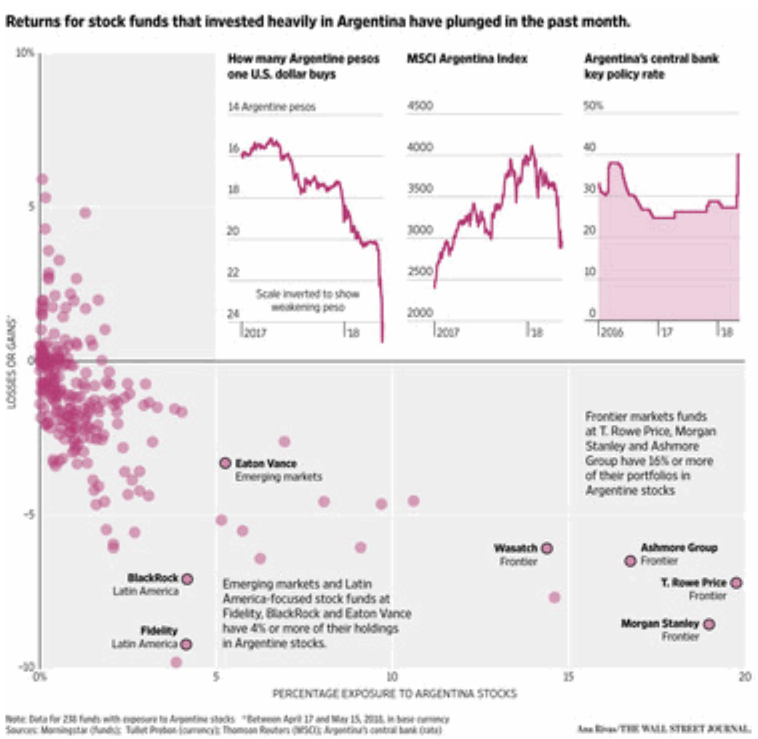
"They don't follow the country closely enough and now they're panicking," said Oliver Bell, a frontier-markets portfolio manager at T. Rowe Price, who has 20% of his portfolio in Argentina stocks.

Many investors have been spooked by a series of emergency interest-rate increases that began last month, as Argentina's central bank has moved rates up to 40%.

Argentina said last week that it is in negotiations with the International Monetary Fund for an emergency loan to shore up its finances, as the country faces looming inflation and a possible slowdown in growth.

"The country is doing everything right," Fidelity's Mr. Pruett said, adding there has been a "crisis of confidence that's weighing on the currency."

With 4% of assets invested in Argentina, his fund has fallen more than 7% over the past month. Mr. Pruett said he hasn't changed his exposure to the country because he believes the administration is making the right moves to stabilize the selloff.

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THE WALL STREET JOURNAL.
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Heard on the Street
**Emerging Markets' Weakest Links**

By Richard Barley
514 words
17 May 2018
The Wall Street Journal
J
B12
English


[Financial Analysis and Commentary]

Who's next? The fear of contagion is stalking emerging markets again, but Argentina and Turkey have put themselves in the firing line while others have distanced themselves from it.

The shakeout in emerging markets sparked by the "taper tantrum" of 2013 put the spotlight on countries with relatively wide current-account deficits. The turmoil that has hit some vulnerable countries as U.S. rates have risen started with similar weak links, but there are fewer immediately obvious follow-on targets.

Right now, the spotlight is on Argentina, where the peso has fallen more than 23% against the dollar this year and the country is seeking support from the International Monetary Fund, and Turkey, where the lira has fallen more than 15%. Both stand out for having current-account deficits estimated by the IMF in 2018 at more than 5% of gross domestic product.

Those two countries' vulnerability has been exacerbated by domestic policy missteps, especially on monetary policy. Turkey faces a credibility challenge, with President Recep Tayyip Erdogan saying he would seek to exert greater influence on monetary policy, which has sent the lira to a record low.

But many other nations have narrower current-account deficits than in the past, having taken account of what happened in 2013. Their currencies are under less pressure this time.

South Africa, for instance, ran a current-account deficit of 5.9% of GDP in 2013 on the IMF's numbers and the rand fell around 20% against the dollar that year. But the forecast deficit for 2018 is substantially narrower, at 2.9%, and there is enthusiasm around the political and economic change that new President Cyril Ramaphosa may bring; the rand has given up its gains against the dollar this year but is down only 0.5% in May. In Latin America, current-account deficits for Mexico and Brazil are forecast at less than 2% of GDP in 2018.

Deficits aren't the only thing for investors to worry about, of course. Russia runs a surplus, but the ruble has been battered by new U.S. sanctions this year and is down 7.5% against the dollar. Notably, however, it has rebounded from its lows and is slightly up against the dollar in May even as clouds have gathered over emerging markets, helped by surging **oil prices**. That, in turn, may weigh on the deficits of crude importers. And then there is politics, a potential worry for investors in Brazil and Mexico, where elections are looming.

A further rise in the dollar and U.S. Treasury yields -- with the 10-year yield now decisively above 3% -- will put more pressure on emerging markets in general. For now, though, Turkey and Argentina are being singled out because they are different from other emerging-market nations. Investors are right to be nervous that these are the first cracks in a broader crisis, but contagion may be an issue only for those with pre-existing conditions.




page,5043

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THE WALL STREET JOURNAL.
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**Business News: Oil Firms Tap Refining, Retailing --- Petrochemicals, gas stations offer growth, as swings in crude prices roil drilling**

By Sarah Kent
647 words
17 May 2018
The Wall Street Journal
J
B6
English


Major oil companies are doubling down on gas stations, refineries and processing plants, betting on a once-unloved part of the energy business to shore up profits and expand their customer bases.

BP PLC plans to open thousands of gas stations in new markets such as Mexico and India over the next three years. Exxon Mobil Corp. is investing heavily to expand its petrochemical operations, which make products like plastics and the basic ingredients for all sorts of household goods. In November, Royal Dutch Shell PLC started work on a massive petrochemical complex in Pennsylvania -- its first big new plant in the U.S. since the 1960s.

Companies are expected to add 7.7 million barrels a day of new refining capacity by 2023, according to the International Energy Agency. In petrochemicals, the agency estimates that over the next five years investment in the U.S. alone will add 13 million tons a year of new capacity to produce ethylene, the main component of plastic.

American refining, in particular, is booming. Surging shale production has provided cheap and plentiful oil close to the country's petrochemical heartland around the Gulf Coast. Fuel demand is expected to rise. All those dynamics helped drive Marathon Petroleum Corp.'s agreement to buy rival Andeavor last month for $23 billion, a deal that would create the country's largest refiner.

As smaller refiners consolidate, the world's major oil companies are promising that investment in their so-called downstream businesses -- and restructuring efforts they are simultaneously pursuing to improve efficiency -- will add billions of dollars to earnings. The downstream focus sharpened amid a period of lower **oil prices** and concerns over long-term oil demand. Cheaper crude -- the primary feedstock for refining -- boosted margins and profits. Oil companies' "upstream," or oil exploration and development, meanwhile, was suffering from lower prices.

"Upstream at some point was not making money," said Tufan Erginbilgic, head of BP's refining and retail arm. That gave his unit a fresh imperative to "really significantly contribute to group performance, because we have to."

Today, higher crude prices pose a risk that margins from refining won't be as strong as they have in recent years. And all the new investment in capacity could end up swamping the market, analysts warned.

"It remains to be seen the way demand is going to shape up," said Jonathan Leitch, research director at Edinburgh-based consultancy Wood Mackenzie.

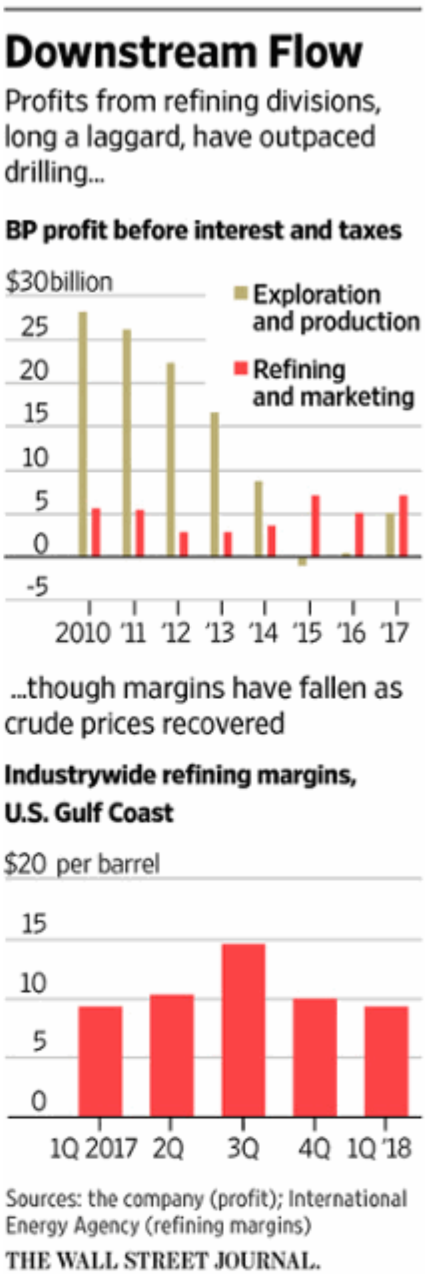
Investor pressure also has mounted on the major oil companies to start positioning for an age when fossil fuels may no longer power the world's fleet of passenger cars. Executives are betting their big petrochemical plants can offer diversification. According to the IEA, petrochemical production is expected to be the biggest driver of oil demand growth in the coming decades.

Gas stations, too, are promising new growth. They offer access to emerging markets, where demand for fuel is expected to be especially robust. BP says it is on track to open 500 retail sites in Mexico by the end of the year, up from zero at the start of 2017.

A geographically wide network of branded retail outlets also could create new opportunities where the industry now sees threats -- such as electric charging stations.

Last year, Shell bought one of Europe's biggest electric-vehicle charging companies, New Motion. It has teamed up with a group of car manufacturers to install more than 500 fast-charging points at existing Shell stations, across 10 countries in Europe over the next two years.

The rise of electric vehicles is "a reality, and an opportunity," Shell's downstream director, John Abbott, told analysts in March. "We are adjusting our offer to meet this new demand."

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**Small Stocks Speed Past Large Caps**

By Akane Otani and Michael Wursthorn
961 words
17 May 2018
The Wall Street Journal
J
B1
English


Shares of small U.S. companies climbed to a fresh record, reflecting their gains in the recent tax overhaul and signs that U.S. growth once again looks more robust than that from overseas.

The rally marks a remarkable rebound for small caps, which fell behind large stocks last year as investors poured money into multinational companies they felt were best positioned to benefit from a synchronized pickup in the global economy.

Yet in recent weeks, data have suggested that momentum around the world could be faltering. Growth in the eurozone appears to have slowed in the first quarter of the year, while data Tuesday showed Japan's economy contracted over the same period, ending the country's longest growth streak in 28 years.

The comparatively rosier outlook for the U.S. has drummed up fresh optimism among investors in small caps -- especially with many expecting small companies, which tend to pay higher effective tax rates than multinationals, to get a boost from corporate tax cuts.

The Russell 2000 index of smaller U.S. companies rose 1% Wednesday to 1616.37, topping its Jan. 23 closing high. For the year, the index is now up 5.3%, outperforming both the **S&P 500**, which has risen 1.8%, and the **Dow Jones Industrial Average**, which is up 0.2%. Those indexes are still more than 5% below their January highs.

"When you have an environment where we're deregulating as opposed to increasing regulations and we're reducing taxes, [small business] managers are going to feel more confident," said Randy Gwirtzman, a co-manager of Baron Discovery Fund, a $226 million fund that focuses on small-cap companies. "We really think this environment can continue, and valuations for companies aren't out of the ordinary in terms of being overly expensive."

Smaller publicly traded companies broke away from the broader market in March and pushed higher, even as bouts of **volatility** related to fears of protectionist trade policies and missteps by technology companies caused the **S&P 500** to slide.

One reason why small caps withstood the turmoil: Investors have bet that continuing skirmishes over trade policy between the U.S. and China, among other nations, are less likely to dent profits among domestic firms. The **S&P 500** gets about 30% of its revenue from outside the U.S., compared with 21% for the Russell 2000, according to a Bank of America Merrill Lynch research note last month.

"When you think about what's going on with trade and tariffs, small caps tend to be much more domestically oriented, so they would be less affected," said Sameer Samana, global equity and technical strategist at Wells Fargo Investment Institute.

The recent divergence in growth outlooks between the U.S. and the rest of the world has also contributed to the rally in small caps, whose fortunes are more closely tied than multinationals to fluctuations in the U.S. economy.

Broad measures of the U.S. economy continue to show signs of expansion, with Commerce Department data on Tuesday showing Americans ramped up spending at the start of the spring despite a run-up in gasoline prices. Signs of strength among consumers have boosted the fortunes of smaller businesses, especially given household spending accounts for more than two-thirds of U.S. economic output.

"Middle-income consumers are finally starting to spend at rates we would expect in an economic recovery," Gregory Trojan, chief executive of BJ's Restaurants Inc. said on the firm's April earnings call. "This is helping improve restaurant traffic everywhere, and we are a key beneficiary." BJ's shares are 44% higher for the year.

A measure of confidence among small-business owners edged up in April to remain near records, buoyed by optimism around consumer spending, lower taxes and strong earnings, according to a survey from the conservative-leaning National Federation of Independent Business.

"Consumers are confident in the U.S. economy, and tax reform has added a layer of optimism this year: Consumers were more prevalent at boat shows and they were not lookers, they were buyers," Jack Springer, chief executive of Malibu Boats Inc., said on the company's May earnings call. Shares of Malibu Boats are up 47% for the year.

Not all analysts are convinced that small caps can sustain their rally. With investors becoming increasingly **bullish**, small caps could run in danger of becoming a crowded trade, something that outperforms the broader market until it suffers a sudden reversal.

The Russell 2000 had rallied after the Nov. 8, 2016, election and in the period leading to the passage of the tax cuts late last year, only to give up its gains as investors moved back into the stocks of fast-growing multinational companies, especially those in the technology sector.

Small-cap-focused funds saw some of their biggest monthly inflows in years in late 2016 and early 2017, only to then suffer 14 straight months of outflows through April, according to Morningstar Inc. data.

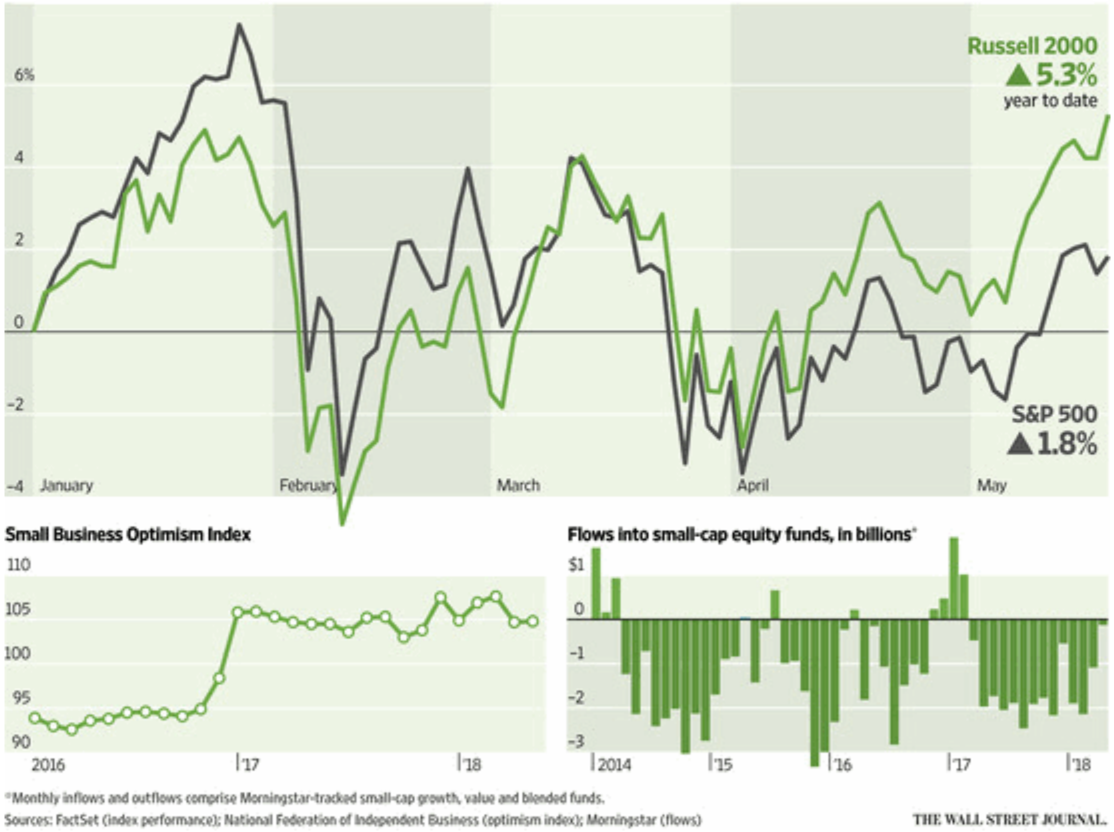
Any signs of a slowdown in the U.S. economy, which has appeared to gather momentum following a slow start to the year, could once again lift multinationals past their smaller peers, analysts say.

But for now, many are feeling optimistic, citing the tailwinds from tax cuts and stronger consumer spending.

Outflows among small-cap funds appear to be easing, too, with redemptions totaling just $128.4 million in April, the weakest in more than a year, after investors put nearly $770 million into growth-focused small-cap funds, according to Morningstar.

"Small caps will basically go as the economy goes," said Wells Fargo's Mr. Samana.

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Markets

**Justices' Ruling Has Cost Investors $800 Million, SEC Says | Fake Crypto Scam as Lesson | Deng's Take: China's Debt Pains Here to Stay, for Now; The Wall Street Journal's financial regulation newsletter for Thursday, May 17, 2018.**

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Deng's Take: China's Debt Pains Here to Stay, for Now

Supreme Court Decision Has Cost Investors Over $800 Million, SEC Says

SEC Shows Investors What a Cryptocurrency Scam Looks Like

Crypto Enthusiasts Mob New York Conference

WSJ Pro: Fed to Re-Examine Big Bank Resolution Rules

China's Debt Pains Here to Stay, for Now

China's efforts to tackle over a decade of rapid debt buildup are yielding small but noteworthy results: Official data shows that commercial lenders are beginning to cool on offering risky investment products, while some firms that borrowed heavily are facing a day of reckoning—the corporate bond market has seen a string of missed payments.

These are signs that better debt management is taking shape, but China watchers warn of potential false starts. What happens over the course of this year will show how much resolve Beijing really has to manage its economy well in the long run.

Top leaders started highlighting financial risks over two years ago. As their warnings grew louder, they rolled out measures aimed at getting everyone from banks and insurers to local governments to dial back risk-taking. A major part of Beijing's battle against debt has also been to get lenders and borrowers to be more transparent about their activities, including any debts they have accumulated, especially off-the-book.

The financial system shows early signs of progress. Banks' outstanding off-balance-sheet wealth-management products declined to 22.2 trillion yuan (about $3.5 trillion) at the end of 2017, from 23.1 trillion a year earlier. Such products have been used to mask loans that banks wouldn't have been able to extend by following Chinese capital regulations.

Moody's Investors Service estimates that shadow-banking assets barely grew last year. Shadow banks are nonbank lenders that have played a critical part in how Chinese firms finance themselves when shut out of the traditional state-run banking system. Moody's estimates that with the economy growing faster in nominal terms, shadow-banking assets as a share of gross domestic product dropped to 79.3% at the end of 2017 from a peak of 86.7% a year earlier.

In the broader economy, Chinese borrowers have been canceling plans to raise money in the bond market and also outright defaulting. Firms failed to repay investors on time for 20 bonds worth a total of 16.4 billion yuan so far this year, according to database company Wind Information Co. By comparison, they defaulted on 17 bonds worth 13.8 billion in the year-earlier period.

The pace of defaults, analysts say, should be a good indication of how much pain Beijing is willing to inflict to reach its goals. So far the aim appears to be controlling, but not necessarily decreasing, the amount of debt relative to the size of the economy, which analysts estimate has reached over 260%.

Analysts say that in some situations, distressed firms have turned to local authorities for help. As long as officials keep helping local firms obtain credit, they aren't letting market forces help in unwinding China's debt bubble.

Key Developments in Washington, on Wall Street, and Beyond

Supreme Court Decision Has Cost Investors Over $800 Million, SEC Says

U.S. securities regulators haven't been able to get more than $800 million in disgorgement of ill-gotten gains since a 2017 Supreme Court case limited the time they have to recover funds for harmed investors.

The amount is a "meaningful percentage" of the total fines that the Securities and Exchange Commission imposes on wrongdoers, a top SEC official told House lawmakers Wednesday.

Now, under the court's decision, the SEC has only five years to sue bad actors after a fraud occurs.

SEC Shows Investors What a Cryptocurrency Scam Looks Like

Washington wants you to know what a cryptocurrency scam looks like—so regulators made one up.

The Securities and Exchange Commission—an 84-year-old agency not known for its digital communications savvy—on Wednesday launched a website that touts a fake initial coin offering, an unregulated way of raising funds that has raised over $12 billion. The SEC says many ICOs are probably fraudulent, with bad guys evading investor protections and selling digital tokens that turn out to be worthless for the buyers.

The SEC's fake token, "HoweyCoin," plays up many of the features of ICOs that regulators say are red flags, including celebrity endorsements and guaranteed returns on investment. The mock token sale includes a "white paper" to explain the fake project, which is styled as a partnership with the travel industry. HoweyCoin will be the "coin of the realm" for travel, the paper says.

Crypto Enthusiasts Mob New York Conference

Seth Kaye, a pink-haired designer, arrived in New York for the Consensus crypto conference this week, hoping that someone would talk to him about his idea to fund solar projects with a digital currency.

The price of a bitcoin has dropped more than 50% since December, but enthusiasm for cryptocurrencies and related projects has hardly been dented, judging by the throngs that descended on the New York Hilton, where the fourth annual conference took place.

As the conference opened Monday, lines snaked through the Hilton; some participants said they waited as long as two hours to get in. Tickets started at $1,000, but some paid as much $3,000 at the door. That didn't seem to deter the crypto-obsessed—8,300 people attended, up from 2,700 last year.

Analysis: Bitcoiners Take New York, but Wall Street Resists The Lure

JPMorgan Tests Blockchain's Capital Markets Potential

WSJ Pro: Fed to Re-Examine Big Bank Resolution Rules

The Federal Reserve's regulatory czar wants to take another look at the capital and liquidity big banks are directed to hold in order to ensure they could fail without a taxpayer bailout. Fed Vice Chairman for Supervision Randal Quarles gave an unscheduled speech saying the Fed is considering taking comments on its so-called resolution regime, including annual "living wills," and potentially proposing changes with an eye toward streamlining requirements that apply to big banks based in the U.S. and abroad. Add another potential rule rewrite to Team Trump's financial regulatory agenda.

Big Four Auditors Face New U.K. Calls To Break Apart

U.K. regulators should consider breaking up the Big Four accounting firms, two parliamentary committees said Wednesday, contending a construction company's collapse shows U.K. audit firms have become a "cosy club" incapable of questioning companies' finances as needed.

In a joint report, the House of Commons' Work and Pensions Committee and its Business, Energy and Industrial Strategy Committee, which have been investigating Carillion PLC's January collapse into liquidation, said auditors played a big role in widespread failures of oversight that had allowed Carillion to become a "giant and unsustainable corporate time bomb."

 

In particular, the committees said, KPMG, Carillion's outside auditor for 19 years, was "complicit" in questionable accounting practices at the company, complacently signing off on its directors' "increasingly fantastical figures." That has led to the danger of a crisis of confidence in the audit profession, the report said.

Unit of Chinese Bank to Pay Over Money-Laundering Compliance

U.S. authorities and financial industry regulators penalized the New York-based brokerage unit of a large Chinese bank for failures in its anti-money-laundering compliance program, imposing millions in fines.

Industrial and Commercial Bank of China Financial Services LLC cleared and settled billions of penny-stock shares without a sufficient compliance program, according to findings from the Securities and Exchange Commission and the Financial Industry Regulatory Authority. The brokerage, a unit of China's biggest lender, had cleared the transactions on behalf of Chardan Capital Markets LLC, which dealt directly with clients.

Neither filed reports on potentially suspicious transactions despite red flags.

Turkish Banker Gets 32 Months in Prison Following Iran Sanctions Conviction

A Turkish banker convicted of helping Iran launder money and cover up a billion-dollar scheme to evade U.S. sanctions was sentenced Wednesday to 32 months in prison.

In January, a federal jury found Mehmet Hakan Atilla guilty of bank fraud, sanctions evasion and other crimes. Prosecutors had argued Mr. Atilla, who worked at Turkish state-owned bank Halkbank, helped the Iranian government illegally access billions of dollars of assets that had been frozen by the U.S.

San Francisco Fed Begins Search for a New Leader

The Federal Reserve Bank of San Francisco said Wednesday it has begun searching for a successor to President John Williams, who is set to become leader of the New York Fed next month.

The search will be overseen by Alex Mehran, the chairman and chief executive of Sunset Development Co.; Tamara Lundgren, CEO of Schnitzer Steel Industries Inc.; Barry Meyer, the retired chairman and CEO of Warner Bros. Entertainment and current chairman of North Ten Miles Associates; and Rosemary Turner, president of UPS Northern California.

Corporate Lending Comeback

Weak corporate loan growth, one of the few worrisome statistics in the economy, has turned positive, potentially boosting growth and bank profits.

Commercial and industrial loans started slowing in late 2016 and stayed stubbornly low through the start of this year. This lending rose just 0.7% in 2017, according to Federal Reserve data. That compared with growth of 10.6% and 6.5% in 2015 and 2016, respectively.

The reasons ranged from policy uncertainty under the new Trump administration to companies reacting to rising interest rates by paying down variable-rate loans or tapping the bond market. The initial impact of this year's corporate tax cuts further reduced borrowing, as many companies repatriated foreign funds, giving them more cash on hand.

Weekly data from the Fed showed C&I loans posting their worst January performance since 2010, according to analysts at Keefe, Bruyette and Woods. But lending has since accelerated. The latest Fed data, for the week ended May 2, shows total C&I loans outstanding up 3.1% from a year earlier, compared with 0.9% at the end of January.

Thursday, May 17

8:30 a.m.

House Financial Services Chairman Jeb Hensarling (R., Texas) appears at a Politico breakfast to discuss the current state of the U.S. economy and fiscal fights ahead in 2018.

9 a.m.

 

The Consumer Financial Protection Bureau's Credit Union Advisory Council holds its spring meeting, including discussions on the Home Mortgage Disclosure Act and several of the CFPB's requests for information.

Monday, May 21

NA

The Financial Industry Regulatory Authority starts its three-day annual conference, which includes panels on a range of compliance and regulatory topics.

Financial Inclusion Doesn't Add to Instability

Households that make small deposits aren't more likely than large depositors to contribute to a bank run, according to a Bank for International Settlementsworking paper. Looking at the behavior of account holders tied to three significant bank closures in the Philippines, researchers found no clear difference between small and large depositors, suggesting "financial inclusion is unlikely to add to financial instability," they write. In addition, using branch-level data for one of the events, researchers found "a bank closure does lead to reduced deposits at bank branches nearby," showing "a bank failure can lead to contagion."

Volcker Rule Changes Would Give Traders Flexibility

Expected changes to the Volcker rule will put the onus on regulators to prove that banks are engaging in proprietary trading and give "market-making traders a bit more flexibility to do their own risk management," Matt Levine writes for Bloomberg View. That means a trader on a bank's market-making desk "leaning into a few directional bets here and there" would be "much less restricted" by revising the rule, he says. People who "do not want banks to take any market risk in their trading operations" might not like the additional flexibility, but "banks are in the business of taking risk," he writes. Yet, the effort to revamp the rule doesn't encourage the bank culture created by proprietary trading, "in which every trader aspired to be an outsized risk-taker with a $100 million pay package, and in which trading managers aspired to set up shadowy hedge funds rather than to meet customer demand," he says.

Columbus Nova, an investment firm with ties to a Russian oligarch, burst into the public eye last week when it was revealed to have paid $500,000 to Michael Cohen, President Donald Trump's personal lawyer. But much about Columbus Nova remains unclear.

Argentina's ailing currency and **stock market** are pounding funds managed by some of the world's biggest investors, including Fidelity Investments, T. Rowe Price Group Inc., and Morgan Stanley, reversing some of the outsized gains they enjoyed last year.

Gambling firms are wagering that the U.S. sports-betting market is the next frontier after the Supreme Court loosened rules on the business, and several are vying to be first out of the gate with offerings.

Political uncertainty returned to Italy, as investors dumped Italian bonds and bank stocks, worried that a new antiestablishment government has increased chances of the country exiting the euro.

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

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WSJ PRO CENTRAL BANKING

Economy

**San Francisco Fed Begins Search | Erdogan's Plan Sows Fear | Brazil's Central Bank Holds | Korea to Disclose Intervention Details | Torry's Take: Dearth of Diversity From A Thousand Cuts; The Wall Street Journal's central banking newsletter for Thursday, May 17, 2018**

2,173 words
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English


Torry's Take: Dearth of Diversity From A Thousand Cuts

San Francisco Fed Begins Search for a New Leader

Erdogan's Plan to Drive Turkish Monetary Policy Sows Fear Among Investors

Brazil's Central Bank Holds Rates Steady

South Korea to Gradually Disclose Foreign Exchange Intervention Details

Dearth of Diversity From A Thousand Cuts

Mary Daly, the San Francisco Fed's research director, is taking a public stance against the economics profession's lack of gender diversity.

For an example, she need look no further than the Federal Reserve Board of Governors. Of its 390 economists last year, 27% were women.

While that is a low number, it is in line with the profession at large. Women accounted for 27% of economics Ph.D.s granted in the U.S. in 2017, and just over 20% of faculty at top universities' economics departments, according to the American Economic Association's Committee on the Status of Women in the Economics Profession.

The seven-seat Fed board itself has three members, including one woman, and four vacancies.

Ms. Daly, in a speech Monday, attributed some of the reticence women have toward a career in economics to "a death by a thousand cuts: unfounded assumptions about career interests, unsolicited comments about appearance and behavior, and a general indifference towards whether they pursued economics or not."

Economists are "not putting out the welcome mat and truly inviting [women and minorities] into our home," she said.

She also addressed the topic in a recent podcast interview, "I work in a completely male-dominated field. Most people I meet don't have poor intent. They just have missing information."

Ms. Daly's rise--aided by mentors like former Fed Chairwoman Janet Yellen--has shined a spotlight on the many ways she broke the mold for the typical career economist. After dropping out of high school in Ballwin, Miss., she worked at doughnut shops and Target to make ends meet before getting a general equivalency diploma and going to college.

"I don't tether my interest in [economics] to being a woman as much as I do to being—growing up in a lower-middle class family and having the background and experiences I've had," she said in the interview. And she said the rewards of improving diversity in the economics profession are clear.

"Policy is endogenous, or it reflects the people who make it. So if you have only one type of people around the table, making the policy, you're going to miss a lot of the problems that other people would see."

Ms. Daly is seen as a possible successor to her boss, San Francisco Fed President John Williams, who leaves next month to become New York Fed chief. If she were selected for the West Coast job, the number of female presidents of the Fed's 12 regional banks would rise 50%--to three from two.

Key Developments Around the World

San Francisco Fed Begins Search for a New Leader

The Federal Reserve Bank of San Francisco said Wednesday it has begun searching for a successor to President John Williams, who is set to become leader of the New York Fed next month. The search will be overseen by Alex Mehran, the chairman and chief executive of Sunset Development Co.; Tamara Lundgren, CEO of Schnitzer Steel Industries Inc.; Barry Meyer, the retired chairman and CEO of Warner Bros. Entertainment and current chairman of North Ten Miles Associates; and Rosemary Turner, president of UPS Northern California.

Erdogan's Plan to Drive Turkish Monetary Policy Sows Fear Among Investors

The Turkish lira tumbled to a record low against the dollar on Wednesday, extending a steep slide that investors attribute to President Recep Tayyip Erdogan's unorthodox economic approach and concerns over his influence over the central bank. The lira reversed its daily losses after the central bank issued a statement saying it would take "necessary steps" to shore it up. The Turkish currency has been caught in a wider storm sweeping through emerging markets, from Argentina to South Africa, partly because of a sharp rise in the dollar. But analysts say the lira's fall in recent months—it has lost 14% since the start of the year—has primarily domestic cause.

Argentina Rolls Over Debt, Giving Government Shot of Confidence

Argentina's central bank on Tuesday rolled over billions of dollars in short-term debt, providing President Mauricio Macri's government with a shot of confidence after weeks of economic **volatility**. In a statement, the central bank said it refinanced all of the $26 billion of peso-denominated securities, known as Lebacs, that are set to expire this week, while auctioning off new debt worth another $200 million. The central bank said the interest rates ranged from 40% for the 36-day Lebac to 38% for the 154-day note.

Bank Indonesia Likely to Raise Rates by Quarter Point to Boost Embattled Rupiah

Bank Indonesia will likely raise interest rates by a quarter point on concerns the rupiah's persistent weakening could stoke inflation and destabilize the economy. Seven of 10 economists polled by The Wall Street Journal expect the central bank to raise the seven-day reverse repo rate by a quarter point to 4.50%, the first increase since November 2014. Bank Indonesia Gov. Agus Martowardojo has said several times recently that the central bank is holding open the door to possibly adjust interest rates to boost the rupiah, which has fallen to its lowest level since early October 2015 against the dollar. Mr. Martowardojo on Friday said the central bank has adequate space to adjust the policy rate and indicated it would take pre-emptive action to ensure stability.

Brazil's Central Bank Holds Rates Steady

Brazil's central bankunexpectedly left its benchmark interest rate unchanged Wednesday, citing **volatility** in foreign **financial markets**, and signaled the possible end to a 19-month streak of rate cuts. The bank left its benchmark Selic rate at a record low of 6.5%, after indicating at its previous meeting that it would cut at least once more. It was the first time in 13 meetings that the bank didn't trim the Selic.

South Korea to Gradually Disclose Foreign Exchange Intervention Details

South Korea in a major policy turnaround has decided to gradually disclose details on its veiled foreign-exchange interventions to enhance transparency and ease lingering U.S. suspicion that it may be manipulating its currency to boost exports. South Korean authorities had previously opposed any disclosure of their foreign-exchange operations for fear that speculative hot money investors might abuse such information for profit and destabilize local currency markets. They stepped in to tame market **volatility**.

Iceland's Central Bank Leaves Key Rate Unchanged

Iceland's central bankleft its key interest rate unchanged Wednesday, as the country's booming economy continues to cool and despite expectations of slightly higher inflation. "The outlook is for the positive output gap to narrow," the Sedlabanki said. "Nevertheless, a tight monetary stance is still needed in order to contain rapid demand growth." Iceland's economy is expected to ease further: The central bank forecast economic growth of 3.0% in 2019, down from 7.5% in 2016.

 

Thailand Central Bank Stands Pat

The Bank of Thailand left interest rates unchanged Wednesday as it awaited more signs of a broad-based recovery in the economy, opting to preserve its firepower amid global uncertainties stemming from U.S.-China trade tensions. The central bank's monetary-policy committee kept its one-day repurchase rate at 1.50%, as expected. The Bank of Thailand has held the benchmark rate steady since a cut in April 2015.

Soft Aussie Wages Growth May Sideline RBA for Longer

The pace of Australian wages growth remained near record lows in the first three months of the year, which could likely force the Reserve Bank of Australia to stand pat on rates for longer. The Australian Bureau of Statistics reported Wednesday that wages rose by a seasonally adjusted 0.5% in the first quarter, and by 2.1% from a year earlier.

Quick Hits

Federal Reserve governor Randal Quarles said he wants to take another look at big bank resolution rules, a Bank of Canada official said higher immigration levels should lift the country's potential output, and a Fed report showing U.S. industrial production growth was tempered by revisions lowering figures from some recent months. Here are quick hits on central banking and related market views from around the world.

Thursday

8 a.m. EDT

ECB's Constâncio speaks

10:45 a.m. EDT

Minneapolis Fed's Kashkari speaks

12 p.m. EDT

Bank of England's Haldane speaks

1:30 p.m. EDT

Dallas Fed's Kaplan speaks

Friday

3 a.m. EDT

Cleveland Fed's Mester speaks

9:15 a.m. EDT

Fed's Brainard speaks

9:15 a.m. EDT

Dallas Fed's Kaplan speaks

Foreign Effects of Higher U.S. Interest Rates

Matteo Iacoviello and Gaston Navarro analyze the impact of higher U.S. interest rates on emerging market economies in a new Fed paper. Gross domestic product declines in emerging economies in response to higher U.S. interest rates more than in advanced economies. In advanced economies, responses to U.S. interest rate hikes are larger when a country's currency is pegged to the dollar and it trades a large amount with the U.S. For emerging economies, financial vulnerability plays more of a role.

A New Link Between Monetary Policy and Inequality

Unexpected monetary stimulus, such as the quantitative easing programs launched by central banks in response to the financial crisis, increases income inequality by boosting the high-skill premium, write Juan Dolado, Gergo

 

Motyovszki and Evi Pappa. "An expansionary monetary policy shock increases labour earnings inequality," they write. "This is mainly driven by an increase in the wage premium for the high skilled (i.e. the skill premium). it is the interaction of capital-skill complementarity with asymmetric search-and-matching frictions that leads to the larger rise in inequality. It is important to stress that these results are not specific to monetary policy shocks but are qualitatively similar for any positive aggregate demand shock which increases the labour and capital demand of firms. Nonetheless, since monetary policy shocks have a stronger impact on the user cost capital than, for example, government expenditure shocks – due to the investment crowding-out effects of the latter – we argue that their effect on income inequality is larger."

Companies Can't Hold the Line on U.S. Wages Much Longer

Workers are leaving their jobs at a faster rate, confident they can obtain bigger paychecks elsewhere, writes Tim Duy for Bloomberg View. "It is unlikely that companies can hold the line on wages – and depress real wage growth – when low unemployment encourages workers to quit their jobs in search of a higher salary. The Fed expects this as well, which is why faster wage growth alone will not prompt an acceleration in the pace of rate hikes. The surprise would be if wage growth didn't accelerate. Such an outcome would call into question both the durability of consumer spending and the viability of the Fed's expected rate path."

In Emerging Turmoil, What Links Argentina and Turkey?

Investors are right to be nervous, but contagion may only be an issue for those with pre-existing conditions, writes Richard Barley for The Wall Street Journal. "The turmoil that has hit some vulnerable countries as U.S. rates have risen again has started with similar weak links, but times have changed: there are fewer immediately obvious follow-on targets," Mr. Barley says. He points to Argentina and Turkey's vulnerability being exacerbated by missteps in monetary policy. "Turkey, in particular, faces a credibility challenge, with President Recep Tayyip Erdogan saying he would seek to exert greater influence on monetary policy, which has sent the lira to a record low," Mr. Barley writes.

U.S. industries pumped out more goods in April to meet growing demand from consumers and businesses, another sign the economy is gaining momentum. Industrial output—reflecting everything produced by factories, mines and utilities—rose a seasonally adjusted 0.7% in April from a month earlier, the Federal Reserve said Wednesday.

U.S. housing starts fell in April, signaling factors such as rising material and construction labor costs are holding down home building despite solid buyer demand.

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

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

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**The Market's New Boss; Earnings growth is so last quarter—now rising bond yields are clearly driving the markets, creating risks and opportunities**

By Justin Lahart
510 words
17 May 2018
05:30 AM
The Wall Street Journal Online
WSJO
English


The shift has been going on for some time but it became very clear this week: Interest rates are now more important than profits for stock performance.

The first quarter was very good for U.S. companies, as a brew of corporate tax cuts, solid global economic growth and a weaker dollar pushed profits higher. Earnings at companies in the **S&P 500** were an estimated 26.1% higher than a year earlier, according to Thomson Reuters I/B/E/S, marking the strongest gain since 2010.

Profits will be strong all year, but the first quarter will likely be as good it gets. Analysts currently peg earnings growth in the 20% range for the rest of the year, slowing to 6.7% in the first quarter of next year, when the tax-cut benefit hits its anniversary.

While earnings growth will slow, yields have suddenly kicked up, with the **10**-**year Treasury** note yielding 3.09% versus 2.41% at the start of the year. For income-focused investors the rise in yields has increased the attractiveness of Treasurys relative to stocks. Even the 3-month Treasury bill's yield, at 1.9%, is now higher than the **S&P 500**'s trailing dividend yield of 1.8%.

That is part of why bondlike stocks, such as real-estate investment trusts and utilities have been doing so poorly lately.

In contrast to earnings growth, Treasury yields seem likely to go higher still. With the unemployment rate low and inflation warming up, the Federal Reserve is set to keep raising interest rates. Yields will face more upward pressure because the supply of Treasurys on the market is increasing, as the Treasury steps up issuance and the Fed continues to run off its holdings.

The stocks that do well in that environment are the ones that can keep generating strong earnings growth. Those will likely be cyclical companies, but only those where sales stay ahead of rising costs. Energy companies fit that bill easily, as **oil prices** pushed higher—part of why energy stocks in the **S&P 500** are up 14.5% so far this quarter. The same goes for technology companies, which are up 6.7%.

Home builders, by contrast, are growing but are suffering from rising costs for labor and materials. The broad S&P 1500 home building index is down 5.1%.

Consumer staples companies, which offer steady could also face challenges as Treasury yields climb. Even after healthy profits, the stocks are down 6% this quarter. And if their profit-margins start getting pressured, they could be in real trouble.

If rates keep rising, the number of stocks that can generate strong growth will dwindle. That makes for crowded trades that inevitably end in nasty selloffs. We've got a way to go but the path has been laid.

Write to Justin Lahart at justin.lahart@wsj.com

Document WSJO000020180517ee5h000rt

The New York Times

Business/Financial Desk; SECTB

# Trade Giants See a Future With Few Ties

By KEITH BRADSHER; Natalie Kitroeff contributed reporting from New York
1,615 words
17 May 2018
The New York Times
NYTF
Late Edition - Final
1
English


BEIJING -- The economic relationship between China and the United States has defined the modern era. It helped lift hundreds of millions of people in China out of poverty. It gave affordable iPhones and other gadgets to American consumers, handed big profits to American companies and delivered 1.3 billion hungry customers to American farmers.

Now some people in both countries want to tear it apart.

As a top Chinese economic policymaker meets with the Trump administration this week in hopes of heading off a potential trade war, some officials in both countries are planning for a time when the world's two biggest economies do not need each other quite so much any more. They are seeking nothing less than a fundamental rethinking of a trade relationship that encompasses more than $700 billion in goods and services that flow between the countries every year.

Full disengagement is impossible, leaders on both sides acknowledge. But the plans being developed in Beijing and Washington anticipate a time when the economic engines of China and the United States are not so closely linked, particularly in high-tech industries.

''In the next step of tackling technology, we must cast aside illusions and rely on ourselves,'' President Xi Jinping of China said last month after visiting a new computer microchip factory in the country's center.

Beijing has Made in China 2025, a plan that calls for the country to become largely self-sufficient and globally competitive in 10 advanced manufacturing sectors now dominated by the West. These include commercial aircraft, robotics, 5G mobile phone communications and computer microchips.

China currently depends on the United States and its allies for those elements of a high-tech future. Washington showed that last month with its move to deny American-made components to ZTE, bringing the Chinese company's factories to a halt.

But Washington is also worried about China's efforts to build homegrown champions. The Trump administration blocked the chip maker Broadcom's proposed acquisition of Qualcomm, a rival, this year, over concerns that the deal would give China's Huawei an advantage in 5G technology.

The United States has outlined its own strategy of sorts to wean itself from China. Should the Trump administration enact its threated tariffs on $150 billion in Chinese-made goods, the thinking goes, American corporations would begin to reduce their reliance on Chinese-made small components, machinery and other dull-but-essential parts in the global supply chain.

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United States trade officials are counting on tariffs to have long-lasting effects. Decades-old levies on imported pickup trucks, for example, help explain why essentially all pickups sold in the United States -- even those made by Japanese companies like Toyota -- are made in America.

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The focus on disengagement reflect broader political realities. China is rapidly building a world-class navy; conducting military exercises in Africa and off the shores of northern Europe; and developing some of the world's most advanced stealth fighter planes and ballistic missiles. The military muscle-flexing has caused alarm in Washington and directly influenced trade policy.

In China, leaders were alarmed five years ago by the former National Security Agency contractor Edward Snowden's disclosures that American intelligence services had involved technology companies in the United States in its spying on China and its allies. China also faces rising labor costs -- meaning cheap manufacturing will no longer provide as many jobs -- and has a rising class of educated young people for whom it needs to find well-paying, high-tech jobs. While many American and European companies see Made in China 2025 as building up government-supported rivals, Chinese leaders see the plan as essential to the country's future prosperity.

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But China has a long way to go. It trails the United States significantly in crucial areas like microchips, software design and high-end precision manufacturing. As one example, semiconductors designed in the United States make up half the chips China buys every year. American companies can already design and will soon be manufacturing semiconductors with circuits just one-fifth of the size of Chinese circuits.

But the United States faces its own challenges. Washington could find it extremely difficult to lure back factories that moved to China over the years. Chinese workers may be more expensive to employ than they once were, but they are still paid a quarter or less than American workers. China has also become a vast new market in its own right -- one that companies are loath to leave -- and has invested huge sums in highways, bullet trains and other systems that make connecting buyers and sellers cheap and easy.

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Foxconn, a Taiwanese company that makes iPhones and other devices, has begun building facilities in India and is preparing to build one in the United States, too. Devendra Fadnavis, the chief minister of Maharashtra state in India, which includes Mumbai, said in an interview that he had recently met with a group of chief executives of American companies who also wanted to place big bets on new factories in the country.

''They were very **bullish** on India,'' Mr. Fadnavis said, ''and now I'm getting more and more inquiries from the U.S.''

But politics, not economics, have played a major role in those decisions, and progress has been slow. Despite a plan to build factories employing 50,000 people in the western Indian state of Maharashtra by 2020, Foxconn now has 16,500 workers in all of India. In China, it has one million.

''We are continuing to invest in expanding our presence and capabilities in locations throughout China,'' Foxconn said in a statement.

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Follow Keith Bradsher on Twitter: @KeithBradsher.

The Chinese manufacturer JA Solar relies heavily on robotics to make panels at its solar farm in Hefei. China has become a world leader in solar technology. (PHOTOGRAPH BY ADAM DEAN FOR THE NEW YORK TIMES); Chinese naval exercise in the South China Sea. China's muscle-flexing has alarmed Washington. (PHOTOGRAPH BY CHINA STRINGER NETWORK/REUTERS) (B2)

Document NYTF000020180517ee5h0004x

 

THE WALL STREET JOURNAL.
U.S. EDITION

**Crude Prices Keep Marching Higher**

By Sarah McFarlane
198 words
17 May 2018
The Wall Street Journal
J
B11
English


U.S. crude prices settled up 18 cents, or 0.3%, at $71.49 a barrel on the New York Mercantile Exchange. Brent, the global benchmark, rose 85 cents, or 1.1%, to $79.28 barrel on ICE Futures Europe.

**Oil prices** have climbed more than 18% this year, boosted by production cuts by major producers tightening supplies and increased geopolitical tensions amid rising unease in the Middle East.

The nearly $8-a-barrel difference between global and U.S. **oil prices** is spurring a wave of exports of U.S. crude. Oil was shipped abroad at a rate of 2.56 million barrels a day last week, according to EIA data. But pipeline bottlenecks are keeping some oil from reaching the Gulf Coast.

"The local market flooded but not the balance of the world," said John Kilduff, founding partner at Again Capital.

Members of OPEC have pledged to ramp up production if needed. However, for now, it is "business as usual" as the cartel continues to adhere to its agreement to cut supplies, said Stephen Brennock, an analyst at brokerage PVM.



Document J000000020180517ee5h0002e

THE WALL STREET JOURNAL.

Markets

**South Korea to Gradually Disclose Foreign Exchange Intervention Details; Authorities expects policy shift to improve the credibility of local currency markets**

By Kwanwoo Jun
451 words
16 May 2018
09:06 PM
The Wall Street Journal Online
WSJO
English


SEOUL—South Korea in a major policy turnaround has decided to gradually disclose details on its veiled foreign-exchange interventions to enhance transparency and ease lingering U.S. suspicion that it may be manipulating its currency to boost exports.

South Korean authorities had previously opposed any disclosure of their foreign-exchange operations for fear that speculative hot money investors might abuse such information for profit and destabilize local currency markets. They stepped in to tame market **volatility**.

The decision, announced jointly by the finance ministry and the central bank early Thursday, is expected to help boost "the maturity and international credibility" of the country's foreign exchange markets, said Finance Minister Kim Dong-yeon at an economic policy meeting.

Under the new policy, authorities will publicly release net won-dollar trading volumes starting with a March 2019 disclosure of information from the second half of 2018. In September 2019, details from the first half of 2019 will be released, with more frequent disclosures for three-month periods starting in December 2019.

The information will be made public via the Bank of Korea website, it said.

South Korea has remained on the U.S. Treasury's currency-manipulation watch list since 2016, as the U.S. has suspected some of its trading partners of having unfairly devalued local currencies in order to be more price-competitive in trade.

Seoul has denied that it intervened in currency markets to boost exports. The local currency jumped 13% against the dollar last year.

In its latest semiannual report in April, the Treasury did not designate South Korea as a currency manipulator while keeping the country on its watch list.

The Treasury report urged South Korea to disclose its exchange-rate interventions "in a transparent and timely manner" while noting South Korean authorities' notable moves in November and January to slow the won's appreciation against the dollar.

South Korea satisfies two of the Treasury's currency-rigging criteria: a current-account surplus above 3% of its GDP, and a bilateral trade surplus with the U.S. that's above $20 billion. But the country does not meet the third standard that purchases of foreign currency are "conducted repeatedly" and total at least 2% of gross domestic product over a 12-month period.

South Korea has been seeking to bolster **financial markets** from external shocks due to sudden outflows of foreign capital. The country has kept an ample stock of foreign-currency reserves, maintaining as many currency-swap lines as possible.

Write to Kwanwoo Jun at kwanwoo.jun@wsj.com

Document WSJO000020180517ee5h0002t

The New York Times

Business Day
**On Trade, the U.S. and China Consider the Unthinkable: Breaking Up**

By Keith Bradsher
1,710 words
16 May 2018
01:25 PM
NYTimes.com Feed
NYTFEED
English


BEIJING — The economic relationship between China and the United States has defined the modern era. It helped lift hundreds of millions of people in China out of poverty. It gave affordable iPhones and other gadgets to American consumers, handed big profits to American companies and delivered 1.3 billion hungry customers to American farmers.

Now some people in both countries want to tear it apart.

As a top Chinese economic policymaker meets with the Trump administration this week in hopes of heading off a potential trade war, some officials in both countries are planning for a time when the world's two biggest economies do not need each other quite so much any more. They are seeking nothing less than a fundamental rethinking of a trade relationship that encompasses more than $700 billion in goods and services that flow between the countries every year.

Full disengagement is impossible, leaders on both sides acknowledge. But the plans being developed in Beijing and Washington anticipate a time when the economic engines of China and the United States are not so closely linked, particularly in high-tech industries.

"In the next step of tackling technology, we must cast aside illusions and rely on ourselves," President Xi Jinping of China said last month after visiting a new computer microchip factory in the country's center.

Beijing has Made in China 2025, a plan that calls for the country to become largely self-sufficient and globally competitive in 10 advanced manufacturing sectors now dominated by the West. These include commercial aircraft, robotics, 5G mobile phone communications and computer microchips.

China currently depends on the United States and its allies for those elements of a high-tech future. Washington showed that last month with its move to deny American-made components to ZTE, bringing the Chinese company's factories to a halt.

But Washington is also worried about China's efforts to build homegrown champions. The Trump administration blocked the chip maker Broadcom's proposed acquisition of Qualcomm, a rival, this year, over concerns that the deal would give China's Huawei an advantage in 5G technology.

The United States has outlined its own strategy of sorts to wean itself from China. Should the Trump administration enact its threatened tariffs on $150 billion in Chinese-made goods, the thinking goes, American corporations would begin to reduce their reliance on Chinese-made small components, machinery and other dull-but-essential parts in the global supply chain.

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Follow Keith Bradsher on Twitter: @KeithBradsher. Natalie Kitroeff contributed reporting from New York

* Trump Shifts From Trade War Threats to Concessions in Rebuff to Hard-Liners

* In About-Face on Trade, Trump Vows to Protect ZTE Jobs in China

* Trump Delivers a Mixed Message on His National Security Approach

Semiconductor research in China. A plan known as Made in China 2025 is built around the idea of developing the country’s high-tech industries. | Kim Kyung Hoon/Reuters | A Hongqui electric concept car at the China Auto Show in Beijing in April. The electric car category is among the areas in which China now exports almost no products that would be affected by the Trump administration’s tariff plans. | Andy Wong/Associated Press | China is rapidly building a world-class navy; conducting military exercises in Africa and off the shores of northern Europe; and developing some of the world’s most advanced stealth fighter planes and ballistic missiles. | China Stringer Network/Reuters

Document NYTFEED020180516ee5g005pl

 

THE WALL STREET JOURNAL.

World

**The 10-Point. A personal, guided tour to the best scoops and stories every day in The Wall Street Journal, from Editor in Chief Gerard Baker.**

By Gerard Baker
1,079 words
16 May 2018
06:33 AM
The Wall Street Journal Online
WSJO
English


Good morning,

Nafta Rewrite in Peril

President Trump's plans to rewrite the North American Free Trade Agreement this year looked unattainable Tuesday after negotiators appeared too far apart to strike a deal before a deadline this week. House Speaker Paul Ryan had set Thursday as an informal deadline if the administration were to push a pact through the Republican-controlled Congress before a new slate of lawmakers arrives in Washington next year, possibly led by Democrats. Mexican Economy Minister Ildefonso Guajardo said a deal was unlikely by Thursday. Negotiators showed a willingness to continue pursuing an agreement in the coming weeks and months, although that suggests Mr. Trump's promise to rewrite the 24-year-old trade pact will take much longer than his administration had hoped.

Spending Spree

U.S. companies are increasing spending on their businesses at the fastest pace in years , a long-awaited development after a period of tepid growth. However, investors might question whether it is worthwhile. The jump in capital spending comes as companies whittle away at massive stockpiles of cash—something that has allowed them to funnel money into their businesses and increase their dividends, as well as buy back their shares at a record pace. Data suggest that shares of companies with large and growing capital expenditures, or capex, tend to underperform the broader **stock market**—which could weigh on returns just as the market has become more **volatile**.

U.S., ISIS Square Off

U.S. forces are preparing for a battle with Islamic State over a valley that was once the Afghan hub of the group's campaign to create a world-wide caliphate. The militants have been probing American and Afghan positions and hiding weapons caches in the ridges overlooking Mohmand Valley, which was controlled by ISIS fighters until allied troops chased them into the Spingar mountains at the end of last year. That operation allowed civilians who had fled Islamic State to return to their stone-terraced farms. Now many families are reversing course in anticipation of an attempt by insurgents to retake the ground, which would expand Islamic State's Afghan foothold.

Flip the Script

Where does entertainment go in the Trump era? Movie producer Dallas Sonnier has one answer: "populist entertainment," made for people "outside the coasts." In Mr. Sonnier's October 2017 release "Brawl in Cell Block 99" Vince Vaughn portrayed an unemployed mechanic who kills drug dealers to protect his wife from a forced abortion. The film had a tiny theatrical release with little media coverage, but its DVDs were a hit at Walmart as soon as they hit the shelves. Other studios don't appear to be mimicking his approach, but some recent Hollywood moves, including the revival of the television series "Roseanne," seem to affirm Mr. Sonnier's conviction that he is tapping an underserved audience, Journal reporter Erich Schwartzel writes .

Today's Video

WSJ CEO Council

Top diplomats and government officials discussed risks, hopes and the future of North Korean relations at our CEO Council in Tokyo earlier this week. North Korea suspended high-level talks with South Korea, citing objections to its military exercises being conducted with the U.S. Also, a senior North Korean official said Pyongyang isn't interested in a summit with Washington focused solely on denuclearization, casting doubt on the North's willingness to proceed with leader Kim Jong Un's planned meeting with President Trump in June.

TOP STORIES

U.S.

At Least Three Women Favored to Win House Seats in Pennsylvania After Primary Victories

Haspel Wins Key Democrat's Backing, Paving Way to CIA Confirmation

WORLD

Israel Faces International Criticism for Gaza Deaths

Malaysian Pro-Democracy Leader Released From Detention

BUSINESS

Disney Considers Letting Pixar Co-Founder Lasseter Return

Novartis Top Lawyer Departs Over Cohen Payments

MARKETS

How China's Tencent Uses Deals to Crowd Out Tech Rivals

Clarida Affirms Commitment to Fed's Independence in Setting Rates

Number of the Day

3.082%

The level at which the yield on the benchmark **10-year Treasury** note settled Tuesday, compared with 2.995% Monday, marking its biggest one-day advance since March 2017. The 10-year yield is used as a reference rate for mortgages, auto loans and corporate debt.

Today's Question

Going back to our story above, what do you make of North Korea's casting doubt on its planned summit with the U.S. next month? Send your comments, which we may edit before publication, to 10point@wsj.com. Please include your name and location.

—Compiled by Jessica Menton

Reader Response

Responding to yesterday's question on the clashes between Palestinians and Israel's military, Ken Keeney of Illinois wrote: "The loss of lives during the clashes between Palestinians and Israel's military is most regrettable and preventable. I understand both sides of the disagreement. I also understand 'peaceful' demonstrations. Once these demonstrations turn to violence it can only result in more violence. It is sad that the instigators of this violence are responsible for the deaths of their own people." Sherrill Neese of Maryland said: "There is a lot of concern about the injuries and deaths of the rioting Palestinians. A terrible situation, to be sure. My thoughts…Riot all you want, but if you don't want to get hurt, then don't attack the Israelis. If you do, then you are getting what you asked for." And Tom Palumbo of Michigan shared: "Like preceding events, these violent clashes are a result of underrepresentation and oppression of the Palestinian people. This is part of a world-wide trend of major political decisions being made by majority parties with no regard for minority opinions. The world-wide left and right are both guilty of this."

This daily briefing is named "The 10-Point" after the nickname conferred by the editors of The Wall Street Journal on the lead column of the legendary "What's News" digest of top stories. Technically, "10-point" referred to the size of the typeface. The type is smaller now but the name lives on.

Sign up here for a curated weekly tour of WSJ's unique take on the sports world including news, smart features, data and Jason Gay.

The 10-Point In Your Inbox

CLICK HERE to sign up for this briefing by email.

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**Investors, Brace Yourselves for More Drug-Price Drama; Complaints from generic companies alleging anti-competitive practices by patent owners could provide a nasty surprise for pharma investors**

By Charley Grant
428 words
16 May 2018
05:30 AM
The Wall Street Journal Online
WSJO
English


The next leg of the Trump administration's plan to lower the cost of drug prices could get ugly for investors.

As soon as Thursday the Food and Drug Administration plans to publish a database of complaint letters from generic drug companies to the agency alleging anticompetitive activities from branded pharmaceutical companies. It is likely that some complaints will pertain to high-price blockbuster drugs that investors watch most closely.

At issue are FDA rules under a program called REMS, which often call for limited distribution of drugs to protect against possible safety issues. Generic drug companies have long contended that branded companies game the rules to withhold sufficient samples needed to develop cheaper alternatives.

For example, Mylan sued Celgene for allegedly thwarting efforts to develop a generic version of blood cancer drug Revlimid back in 2014. Mylan alleged that those tactics have helped stave off cheaper competitors and boosted Celgene's profits, resulting in higher costs for health plans and patients. Revlimid sales topped $8 billion last year, accounting for more than half of Celgene's revenues.

Now regulators are getting involved. "We know that certain brand-name manufacturers are abusing the system by blocking access to samples, and hiding behind FDA's rules when they do it," Health and Human Services Secretary Alex Azar said in a speech on Monday. He said the agency has received more than 150 complaints from generic manufacturers regarding challenges accessing drug samples.

While the FDA doesn't have the authority to halt this practice entirely absent new legislation, that is false comfort for investors in the owners of the patents. The likelihood of congressional action only needs to increase for stock prices to come under pressure.

Unwanted regulatory attention can affect more than just a few companies. Investors should recall that the surging **Nasdaq** Biotechnology Index plunged by nearly 40% from its July 2015 peak when price-gouging headlines begat promises from politicians to crack down on the sector. At issue was pricing practices from companies like Turing Pharmaceuticals and Valeant Pharmaceuticals international, which weren't even in the index.

This time, the biotech index is roughly flat so far this year, which should cushion any blow from new scrutiny.

Still, with midterm elections looming in the fall, investors shouldn't be surprised if a sequel is in store.

Write to Charley Grant at charles.grant@wsj.com

Document WSJO000020180516ee5g0012z

THE WALL STREET JOURNAL.

U.S. Markets
Markets
**U.S. Stocks Rise, Led by Retailers; Macy's shares surge; Treasury yields remain near recent highs**

By Amrith Ramkumar and David Hodari
629 words
16 May 2018
04:47 PM
The Wall Street Journal Online
WSJO
English


* U.S. stocks climb

* Treasury yields inch higher

* Retail stocks rise after Macy's earnings

U.S. stocks climbed Wednesday, lifted by gains in shares of retailers despite continued worries about tighter financial conditions and geopolitical tensions.

Investors have been focused recently on worries over rising inflation and interest rates pushing up borrowing costs, but some analysts expect strong earnings and economic data to buoy stocks moving forward. Corporate earnings are growing at their fastest pace in years, and some expect a wave of share buybacks to also fuel major indexes.

Although the yield on the benchmark 10-year U.S. Treasury note has hit its highest level since 2011, some analysts don't think that mark is high enough to hurt stocks in the long run.

"We don't believe that those specific levels dictate the end of this expansion; it's just the markets have to get comfortable and adjust to a higher rates regime," said Michael Hans, chief investment officer of Clarfeld Financial Advisors.

The Dow Jones Industrial Averaged rose 62.52 points, or 0.3%, to 24768.93. The blue-chip index snapped an eight-session winning streak Tuesday and remains about 7% off its January all-time high. The **S&P 500** added 11.01 points, or 0.4%, to 2722.46, with nine of its 11 sectors rising, and the tech-heavy **Nasdaq Composite** climbed 46.67 points, or 0.6%, to 7398.30.

Macy's shares surged $3.24, or 11%, to $33.17 after the department-store chain exceeded same-store sales expectations in the most recent quarter and lifted its targets for the 2018 fiscal year.

Other retailers such as Target and L Brands were also among the **S&P 500**'s best performers.

Rosy retail sales data Tuesday also have supported consumer stocks and expectations for robust growth in the U.S., though the figures also reignited worries about higher interest rates.

More investors now are anticipating three additional Federal Reserve interest-rate increases this year compared with the central bank's previous projection of two. Higher rates tend to push up borrowing costs and Treasury yields, making stocks less attractive to some investors.

Still, some investors think markets can withstand higher rates as long as the Fed sticks with its current gradual pace of tightening.

"I don't think it's been at a speed that's too difficult to deal with," said Jeff Garden, senior research analyst and portfolio manager at Lido Advisors. "This has been coming for a long time."

On Wednesday, the **10**-**year Treasury** yield inched up to 3.093% from 3.082%, its highest close in nearly seven years. Yields rise as **bond prices** fall.

Analysts also were tracking the latest geopolitical news amid fresh doubts about President Donald Trump's planned summit with North Korea and trade talks with China.

Elsewhere, the Stoxx Europe 600 edged up 0.2%, with the index's basic resources and technology sectors among the best performers. After Asian markets closed, Chinese tech giant Tencent Holdings released results that blew past expectations.

Italy's main stock benchmark fell 2.3%. Investors were spooked by the leaking of a draft proposal by two Italian antiestablishment parties that are seeking to form a governing coalition advocating the introduction of procedures allowing countries to quit the euro. The yield on 10-year Italian bonds rose to 2.110% from roughly 1.95%.

Earlier, Japan's Nikkei Stock Average closed down 0.4%, while the Shanghai Composite declined 0.7%.

Write to Amrith Ramkumar at amrith.ramkumar@wsj.com and David Hodari at David.Hodari@dowjones.com

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THE WALL STREET JOURNAL.

Markets
**Why the Credit-Card Boom May Have Just Peaked; Card lenders are feeling the pinch as loan losses and rewards expenses rise**

By AnnaMaria Andriotis
927 words
16 May 2018
05:30 AM
The Wall Street Journal Online
WSJO
English


Following some of their strongest years ever, credit-card issuers are grappling with an uneasy future.

Rising loan losses and increased rewards expenses are putting pressure on card lenders' returns. The result is that one of the most profitable consumer-lending categories in recent years may become more of a middling player.

"The easy money has been made in card lending," said Don Fandetti, consumer finance analyst at Wells Fargo & Co.

While cards remain highly lucrative for banks, the benefits of a rising interest-rate environment have been muted lately. The added revenue of cardholders paying more in interest payments each month has also been offset by growing competition from lenders trying to poach card customers by offering lower rates.

Credit cards became an appealing loan category for banks in the wake of the last recession. Card balances grew at an accelerating pace in recent years, reaching a 7% year-over-year growth rate early last year. Total balances exceeded $1.03 trillion in January, the highest on record, according to the Federal Reserve.

But that coincided with an increase in loan losses from historically low levels, as banks set aside more money for future write-offs. They also tightened their underwriting standards, resulting in slowing growth. Card-balance growth in March was up 4.8% from a year earlier, compared with a 6.1% increase in March 2017 from the year-earlier period.

Five of the largest credit-card issuers—American Express Co., Capital One Financial Corp., Citigroup Inc., Discover Financial Services and Synchrony Financial—generated a median return of 2.1% on their assets for common shareholders in the first quarter, up from 2% a year earlier but down from 2.6% two years prior, according to analysis by Autonomous Research. The recent peak was 3.7% in the second quarter of 2011, according to an industry analysis by Autonomous at the time.

"The industry was at an unsustainable high…so coming down is expected," David Nelms, Discover's chief executive, said in an interview.

The pickup in returns for most banks in the first quarter was primarily the result of tighter underwriting, which helped slow the rate of loan loss increases and the amount of money banks are setting aside for future losses. U.S. tax-law changes that lowered corporate tax rates also helped.

Still, returns remain largely unchanged—and in some cases down—from about 2½ years ago when the Fed began raising rates. "Rising rates [are] a mixed blessing for the card issuers at this point," said Brian Foran, analyst at Autonomous Research. Companies aren't getting the full benefit of the higher rates because while interest charges on cards are rising, so are the interest rates card issuers are having to pay bank customers for their online deposit accounts.

Some analysts predict that profitability will keep falling, though it remains significantly higher than many other banking products. Credit cards delivered a projected 3.8% return on assets to 14 large banks highly concentrated in the card business last year, compared with an overall 1.35% projected return for all commercial banks, according to payments consulting firm Mercator Advisory Group Inc. Mercator projects that card returns will fall in 2018 to 3.5% due to losses and challenges cutting further costs.

Stocks of card companies have reflected the concern, with Discover shares down 0.8% so far this year, and Synchrony Financial, the largest U.S. store credit-card issuer, down 11.4%, compared with a 4% gain in the KBW **Nasdaq** Bank index.

Credit-card losses have been mostly rising over the past two years after hovering around near-record lows. The average net charge-off rate—the share of outstanding debt that issuers wrote off as a loss—for eight of the largest credit-card issuers reached a nearly five-year high of 3.46% in the first quarter, according to Fitch Ratings. The increases have become worrisome indicators for some shareholders of consumers' inability to pay debts at a time when unemployment is low.

Another pain point for card issuers is the cost they incur from so-called gamers, who search for the highest rewards on their cards. These consumers sign up for credit cards with rich sign-up bonus offerings and then stop using the card once they have tapped out the early rewards.

U.S. credit-card attrition rates, a measure of how many cards consumers and card issuers close, reached 15% in 2017, up from less than 10% a year earlier, according to Mercator.

Meanwhile, banks and fintech lenders that originate personal loans have been increasing solicitations in recent quarters. Many of these offers are targeting consumers with credit-card debt and pitching the opportunity to roll over that debt into a personal loan at a lower interest rate. Their prime targets are the customers who card issuers want to keep most: those with high credit scores who carry a card balance each month.

A record 516 million personal loan solicitations were mailed out in the first quarter, up 46% from a year ago, according to estimates from market research firm Competiscan. This marked the fifth-consecutive record-breaking quarter.

Related

* Former Citigroup CEO Vikram Pandit Makes $100 Million Investment in Credit-Card Startup (May 14)

* Goldman Sachs, Apple Team Up on New Credit Card (May 10)

* Heard on the Street: Consumer Credit May Weigh on Economy (April 9)

Document WSJO000020180516ee5g0012x

 

THE WALL STREET JOURNAL.

Economy
**U.S. Housing Starts Dropped in April; Rising material costs, labor shortages converging to pose challenges to builders seeking to meet demand**

By Sarah Chaney and Laura Kusisto
481 words
16 May 2018
11:03 AM
The Wall Street Journal Online
WSJO
English


U.S. housing starts fell in April, signaling factors such as rising material and construction labor costs are holding down home building despite solid buyer demand.

Housing starts fell 3.7% in April from the prior month, to a seasonally adjusted annual rate of 1.287 million, the Commerce Department said Wednesday. Residential building permits, which can signal how much construction is in the pipeline, dropped 1.8%, to an annual pace of 1.352 million last month.

The 11.3% decline in starts for multifamily units dragged down the overall starts figure and represents a reversal of the outsize gains for multifamily starts in March. Single-family home construction also illustrated weakness in April, declining in every region except for the South, where starts popped.

Housing-starts data are **volatile** from month to month and can be subject to large revisions. April's 3.7% decline for starts came with a margin of error of 11.4 percentage points.

Factors such as rising material costs and labor shortages are converging to pose challenges to builders seeking to meet demand for homes.

"This disappointing housing starts report seems to indicate that home builders are finally saying 'Uncle,' " said John Pataky, chief consumer and commercial banking executive at EverBank. "After months of fighting to keep up with still-surging demand, the realities of higher input prices, a limited supply of lots and decreasing confidence seem to be taking their toll."

Some of the weakness in the Midwest and Northeast could be because of atypical snow and weather, said Scott Volling, principal at PricewaterhouseCoopers.

"But, if you take a step back and look at a more macro level, the quote I hear most often from builders is, 'we can't outbuild our labor,' " Mr. Volling said. "They may have lots ready to go, and there may be demand out there, but they can't go any faster than their labor pool allows them to."

Despite solid job and income gains that support housing demand, headwinds in the single-family market persist.

Rising material costs, caused in part by a tariff on Canadian softwood lumber, could also threaten to slow single-family home construction going forward. Lumber costs have risen 50% since the beginning of 2017, adding about $7,000 to the cost of building a home, according to Robert Dietz, chief economist at the National Association of Home Builders.

Mr. Dietz said so far single-family building has proven "remarkably resilient" to rising interest rates and higher construction costs. But eventually, he said, there will come a point where the market will take a pause.

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Document WSJO000020180516ee5g00209

WSJ PRO FINANCIAL REGULATION

Economy

**San Francisco Fed Begins Search for a New Leader; Regional Fed bank hasn't set a timeline for picking a successor to President John Williams**

By Michael S. Derby
483 words
16 May 2018
06:36 PM
WSJ Pro Financial Regulation
RSTPROFR
English


The Federal Reserve Bank of San Francisco said Wednesday it has begun searching for a successor to President John Williams, who is set to become leader of the New York Fed next month.

The search will be overseen by Alex Mehran, the chairman and chief executive of Sunset Development Co.; Tamara Lundgren, CEO of Schnitzer Steel Industries Inc.; Barry Meyer, the retired chairman and CEO of Warner Bros. Entertainment and current chairman of North Ten Miles Associates; and Rosemary Turner, president of UPS Northern California.

The search committee members serve on the San Francisco Fed's board of directors. The 12 regional Fed banks are overseen by boards drawn from the private sector. Directors who work at financial firms regulated by the Fed are prohibited from involvement in selecting a new bank leader.

The San Francisco Fed said the search process will be implemented by Diversified Search, which the bank called the largest female-owned and -founded executive search company.

Mr. Williams is set to take over the New York Fed on June 18, succeeding William Dudley, who is retiring next month. The New York Fed implements monetary policy and serves as the central bank's point of contact with **financial markets**.

The San Francisco Fed said it has no set timeline for picking a leader for its district comprising nine Western states. The bank pledged to offer periodic updates on the status of the search. The bank's pick must be approved by the Washington-based Fed board of governors.

The bank said the search would be "broad and inclusive" and open to outside input.

The search process for regional Fed leaders has gone from a sleepy affair hidden in the shadows to a high-profile battleground in the push to make the Fed more transparent and diverse. Unlike Washington-based governors who are selected by the president and confirmed by the Senate, regional bank presidents are chosen in a closed-door process that has limited space for public input.

Regional Fed bank presidents oversee various central-bank operations like cash processing. They collect local business and financial intelligence, provide space for bank regulators to work and contribute to Fed interest-rate decisions.

The selection of Mr. Williams to lead the New York Feddrew criticism from some left-leaning activists and elected leaders who believed it failed to meet the bank's own goal of considering diverse candidates for the job.

Fed leadership has been dominated by white men drawn from either the economics profession or finance for most of its history. Some critics contend a lack diversity has made the central bank less attentive to how its policies affect economically disadvantaged groups.

Write to Michael S. Derby at michael.derby@wsj.com

Document RSTPROFR20180516ee5g000jh

THE WALL STREET JOURNAL.

Economy
**Brazil's Central Bank Keeps Key Rate Steady for First Time in 13 Meetings; Central bank says the Selic rate's current level is 'adequate' for coming meetings**

By Jeffrey T. Lewis and Paulo Trevisani
582 words
16 May 2018
06:27 PM
The Wall Street Journal Online
WSJO
English


BRASÍLIA—Brazil's central bank unexpectedly left its benchmark interest rate unchanged Wednesday, citing **volatility** in foreign **financial markets**, and signaled the possible end to a 19-month streak of rate cuts.

The bank left its benchmark Selic rate at a record low of 6.5%, after indicating at its previous meeting that it would cut at least once more. It was the first time in 13 meetings that the bank didn't trim the Selic.

Signs of a strengthening American economy are reinforcing the prospect of faster rate increases by the U.S. Federal Reserve. Higher rates in the U.S. tend to make the dollar more attractive to global investors, reducing demand for assets in emerging markets and weakening their currencies, economists say.

"The bank considered there's less appetite for the risk represented by emerging markets" because of the outlook for higher rates in the U.S., said Ignacio Crespo, an economist at the São Paulo-based Guide Investimentos brokerage.

The central bank indicated at its previous meeting in March that it would cut the Selic again, and economists had been expecting a quarter-point reduction, but the Brazilian real has weakened more than 10% against the dollar since then.

The weaker real could put pressure on domestic prices by making imports more expensive. The central bank acted Wednesday to try to ease that effect, according to Pedro Paulo Silveira, an economist at the Nova Futura brokerage.

"The central bank's reaction to the stronger dollar is clearly justified" because a stronger U.S. currency changes the outlook for Brazilian inflation, he said.

The bank pointed out that recent economic indicators have shown some softening, and said the trend in inflation remains favorable. The bank nevertheless chose to maintain the Selic at its current level and said it is "adequate" for upcoming meetings.

Inflation has been below the central bank's 4.5% target for more than a year, a welcome change for a nation accustomed to much faster price increases. The 12-month inflation rate reached 2.76% in April, down from its most recent peak of 10.7% in January 2016.

The economy's recovery from a two-year downturn, Brazil's worst on record, has been slow, which economists say helps explain the slow price increases. Gross domestic product grew only 1% last year, after two years of contraction, and is forecast to expand 2.5% this year.

Record-breaking harvests have helped keep food prices in check, while a 13.1% unemployment rate has tamped down salary increases.

Borrowing is so cheap now, relatively speaking, that it makes more sense for businesses to spend on production rather than keep their funds in **financial markets**, according to economist Ricardo Camargo Mendes of Prospectiva Consulting.

But political uncertainty ahead of the October general election is giving many pause, he said.

"Business people are still reluctant because of the election. The uncertainty is too much," he said, adding that high unemployment is curbing consumption. "The economy isn't normal yet."

Brazilians will vote for president in October, and early polls put candidates seen as less market friendly ahead. Election-related concerns have helped weaken the currency.

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WSJ PRO BANKRUPTCY

Pro Bankruptcy

**Bondholders Push Jones Energy to Make Debt-Cutting Deal; Group holding 80% of unsecured notes joins forces to exert pressure on struggling oil-and-gas company**

By Soma Biswas
664 words
16 May 2018
05:26 PM
WSJ Pro Bankruptcy
RSTPROBK
English


A group of bondholders in oil-and-gas company Jones Energy Inc. have banded together, warning the company against any attempt to force a swap or debt buyback at a big discount.

In a letter Wednesday, a bondholder group informed Jones Energy's board that they hold 80% of the company's unsecured notes and have signed a four-year cooperation agreement to present a united front in ongoing debt-restructuring talks with the company.

The letter comes in response to several moves Jones Energy announced in February to try to lighten its heavy debt load.

Unlike many other debt-laden oil-and-gas exploration companies, Jones Energy was able to stay out of bankruptcy when **oil prices** crashed in 2014. In 2016 the company made a bold bet, buying up oil-and-gas assets in two Oklahoma basins seen as the most profitable and prolific areas for unconventional shale drilling in the U.S., the South Central Oklahoma Oil Province -- known as Scoop -- and the Sooner Trend Anadarko Basin Canadian and Kingfisher Counties -- referred to as Stack.

More recently, however, the Austin, Texas, company has been focused on ways to shed some of its $1 billion-plus in debt, including issuing new secured debt and using proceeds to buy back its deeply discounted bonds.

In the letter, viewed by The Wall Street Journal, the bondholder group, advised by law firm Davis Polk & Wardwell LLP and investment bank Houlihan Lokey, took issue with Jones Energy's decision to raise additional debt in February, which piled on $450 million in new senior secured bonds that would rank higher than the bondholder group's $559 million in unsecured notes due 2022.

Moreover, the company disclosed in February that it intends to use proceeds of the new bond to buy out the group's unsecured notes at big discounts. That is also a move the bondholder group's letter warns against.

"The Cooperating Noteholders are ready and available to work with the Company on a transaction for the benefit of all parties. The Cooperating Noteholders, however, aren't willing to accept the ‘significant' discount envisioned by the Company in February, and cannot be coerced into such an exchange," the letter said.

The tactics Jones Energy disclosed in February are known as liability management exercises. They have become common in recent years as a way for companies to try to lighten heavy debt burdens while avoiding bankruptcy.

Bond investors have increasingly reacted by banding together to prevent companies from swapping or buying back debt at big discounts. A group of bond and loan holders formed a similar group nearly a year before radio broadcaster iHeartMedia Inc. filed for bankruptcy in March. They succeeded in wearing down the company in its quest to keep a substantial equity stake for the company's private-equity owners.

The unsecured notes from Jones last traded at 61.5 cents on the dollar on Tuesday, according to MarketAxess.

In addition, Jones Energy's shares have languished at under $1 per share recently, closing at 73 cents Wednesday.

In April ratings agency Fitch Ratings Inc. downgraded the company to CCC-, deep in junk territory.

The bondholder group includes Avenue Capital Group and Brookfield Asset Management, according to people familiar with the matter

Additional bondholders have until May 30 to join the group, according to the coalition's letter.

Beyond the need to grapple with its debt load, Jones Energy is also under pressure from shareholder activist Q Investments LP, which has urged the company to form joint ventures with other companies to develop its valuable Scoop and Stack shale plays.

In April the company removed founder Jonny Jones from his role as chief executive officer.

Jones Energy didn't return calls requesting comment.

Write to Soma Biswas at soma.biswas@wsj.com

Document RSTPROBK20180516ee5g000rt

THE WALL STREET JOURNAL.
U.S. EDITION

**Bitcoin Exchange Shifts Into Fast Lane**

By Alexander Osipovich
644 words
16 May 2018
The Wall Street Journal
J
B1
English


Coinbase Inc., the operator of the largest U.S. cryptocurrency exchange by trading volume, said it would upgrade its systems with services that cater to ultrafast traders.

Coinbase said it would speed up its technology and allow trading firms to place their servers directly in its data center, a practice called co-location. High-frequency trading, or HFT, firms often put their servers next to the computers that power exchanges like **Nasdaq** Inc. or the New York Stock Exchange to minimize the split-second delays associated with transmitting data back and forth between the trading firm and the exchange.

The moves, planned for later this year, will make Coinbase one of the few bitcoin exchanges to welcome the business of high-speed trading.

High-frequency trading firms use computers to buy and sell stocks, futures and other assets in the blink of eye.

They accounted for 55% of trading volume in the U.S. **stock market** last year, according to research firm Tabb Group LLC, but they have only recently begun to dabble in cryptocurrencies.

San Francisco-based Coinbase plans to introduce "low-latency performance," the company said in a blog post, using a term in the exchange industry that means extremely fast processing times.

According to Coinbase, the plan will benefit customers by reducing bid-ask spreads, the difference between the buying and selling price of an asset. Advocates of HFT say the growth of high-speed trading in the **stock market** over the past two decades helped drive bid-ask spreads down to just one penny in many big stocks.

Coinbase's move is likely to raise eyebrows because many investors view high-speed traders with suspicion. Critics like Michael Lewis, author of the 2014 best-seller "Flash Boys," have alleged that HFT firms take advantage of slower-moving players.

Coinbase will ensure that HFT firms aren't given any unfair advantages, said Adam White, general manager of Coinbase's exchange, called GDAX.

"We are going to be thoughtful and deliberate in the way we do that, to make sure we don't disadvantage any market participant over another," Mr. White said.

After the upgrade is complete, processing times at Coinbase will be measured in microseconds, or millionths of a second, Mr. White said. Greater participation by electronic traders will boost the depth of Coinbase's markets and help the company win over institutional traders, such as hedge funds, Mr. White said.

Joe Saluzzi, a partner at brokerage Themis Trading and a vocal critic of HFT, warned that cryptocurrency exchanges may find it lucrative to offer special perks to high-speed traders.

"The stock exchanges in the **equity market** were the 'arms merchants' that sold speed advantages to HFT so they could be faster than traditional investors," Mr. Saluzzi said in an email. "It looks like Coinbase wants to be one of the arms merchants for the crypto world."

Coinbase isn't the first bitcoin exchange to gear its systems for ultrafast traders. Gemini, the New York-based cryptocurrency exchange founded by Cameron and Tyler Winklevoss, said its trade-execution times are already a matter of microseconds. Gemini's systems are based in the same New Jersey data center used by Cboe Global Markets Inc., an options and stock exchange operator.

Several electronic-trading firms are already active in cryptocurrencies, including Chicago-based DRW Holdings LLC and Jump Trading LLC and New York-based Hudson River Trading LLC, Jane Street Group LLC and Virtu Financial Inc.

Many cryptocurrency exchanges operate on relatively slow and failure-prone technology, compared with the powerful, battle-tested computer systems used by **Nasdaq** or the NYSE. Last year, a number of digital-currency exchanges suffered outages during periods of heavy investor interest in bitcoin, including GDAX and Europe-based Bitstamp.



Document J000000020180516ee5g00024

THE WALL STREET JOURNAL.
U.S. EDITION

**Investors Are Split in Views About Gold --- ETF buyers bullish despite prices hitting year's low, while fervor by hedge funds cools**

By Amrith Ramkumar
808 words
16 May 2018
The Wall Street Journal
J
B18
English


Gold prices slumped, falling below the $1,300 level for the first time since December as a rising dollar and higher Treasury yields led traders to dump the precious metal.

But while the bullion price in the futures market on Tuesday reached a new low for the year, exchange-traded-fund investors recently have been bullish on gold. Investors poured about $3.1 billion into gold-backed ETFs during April, the highest total since February 2017, data from the World Gold Council, an industry trade group, showed.

The contrasting views highlight the two opposing forces that have kept gold prices mostly locked in a narrow range between $1,300 and $1,350 a troy ounce, avoiding the big price swings that have rocked other assets such as stocks and oil.

ETF buyers and other bulls have turned to gold as a traditional haven play during turbulent political times, with the prospect of a trade war still looming, uncertainty swirling around North Korea and tensions in Syria and Iran flaring up. Some money managers are also using gold to hedge against a pickup in inflation signaled by recent consumer-price data.

But speculative interest in gold has softened as expectations of higher U.S. interest rates have pushed up bond yields and the dollar, said Maxwell Gold, director of investment strategy at ETF Securities. "There's a bifurcation in the types of investors for gold," he said.

Front-month gold futures tumbled 2.1% Tuesday to $1,288.90 a troy ounce on the Comex division of the New York Mercantile Exchange -- their worst day since December 2016. The drop came after data showing U.S. retail sales rose broadly in April pushed up Treasury yields and the dollar, continuing their recent trend.

Any time recently that gold has marched toward the upper end of its trading range, a strengthening dollar and worries about higher interest rates have zapped its momentum. A rising U.S. currency makes gold more expensive for overseas buyers, while higher Treasury yields tend to make the precious metal less attractive by comparison.

With global growth momentum shifting back to the U.S., the WSJ Dollar Index hit its highest level of the year Tuesday and in April had its best month since November 2016. And the yield on the benchmark 10-year U.S. Treasuryyield in late April pierced 3% for the first time in more than four years, with more investors anticipating that the Federal Reserve will raise interest rates three more times this year, compared with the previous projection of two. On Tuesday, the yield closed at its highest level since July 2011.

Hedge funds and other speculative investors have cut wagers on higher gold prices to their lowest level since July. Net bets on higher gold prices by hedge funds and other speculative investors fell by more than 50% during the week ended May 1, according to the Commodity Futures Trading Commission. The net bullish bets stayed near that level the following week.

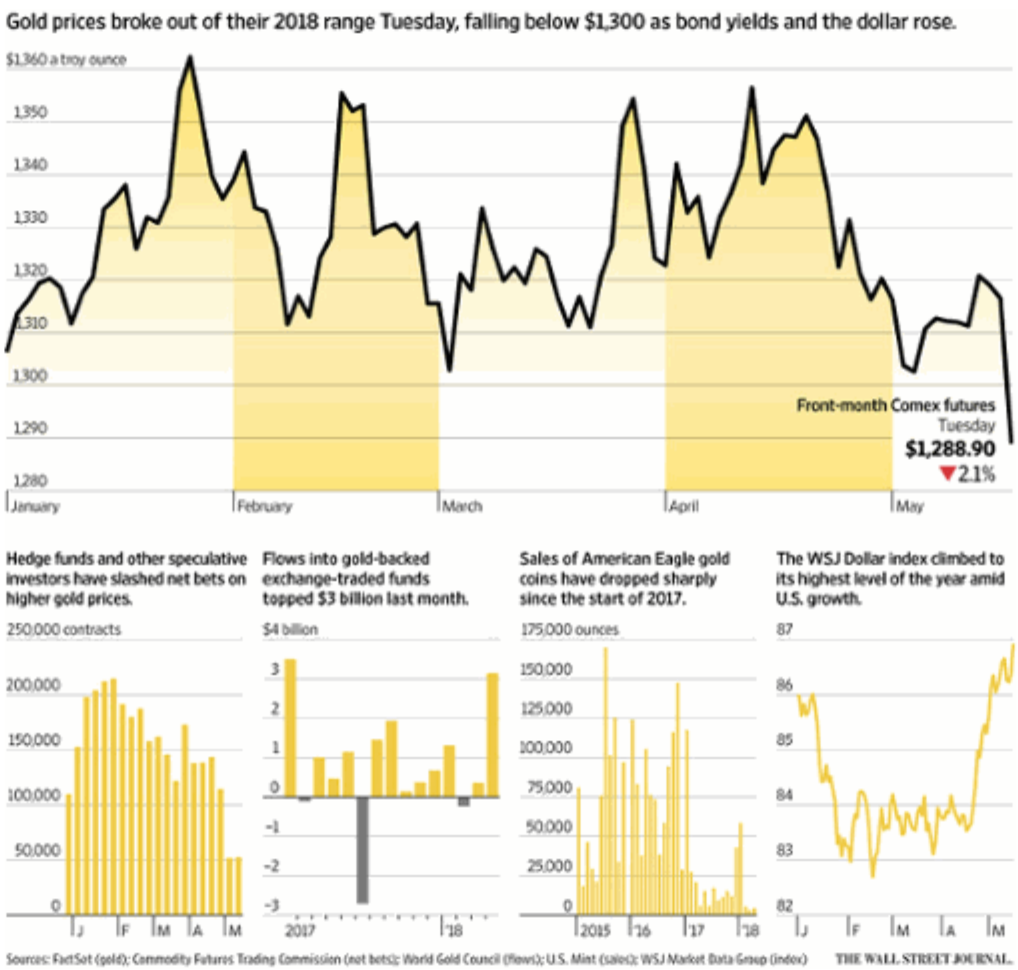
An analysis by the World Gold Council earlier this month showed that demand for gold during the first quarter was the weakest to start a year in a decade. Sales of gold bars and coins have also been tepid, a sign to some that retail buyers have cooled on the yellow metal. Monthly sales of American Eagles, a popular gold coin that is a proxy for retail sales of physical gold, in recent months have hit their lowest level since 2015, U.S. Mint data show.

"There are major economic, financial and political issues on the horizon that suggest stronger investment demand and higher prices at some point -- but they're not here now," said Jeffrey Christian, managing partner at commodities research and asset-management firm CPM Group.

With another U.S. interest-rate increase widely anticipated in June, some analysts expect gold prices to fall leading up to the Fed's monetary-policy meeting before recovering, a pattern that has held over the past few years.

Others are projecting that April's money flows into gold ETFs will continue as demand for bullion in emerging markets such as China recover from a weak start in 2018. Gold bulls are hoping that prices can log a third straight year of gains and bring investment interest back into the market, with prices still 32% below their 2011 records.

"I was a little concerned when I saw first-quarter demand numbers, but they are starting to look like an outlier," said George Milling-Stanley, head of gold strategy at State Street Global Advisors. "We're starting to see figures that suggest demand is a lot better."

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THE WALL STREET JOURNAL.
U.S. EDITION

**Coal Prices Are Burning Up As Demand Stokes Gains**

By Rhiannon Hoyle
431 words
16 May 2018
The Wall Street Journal
J
B17
English


Crude oil isn't the only fuel on a hot streak.

U.S. export prices for electricity-generating coal have surged 16% in the past four weeks, according to S&P Global Platts, a period that is traditionally a seasonal lull in energy markets.

Export prices for thermal coal from other big producers such as Australia have alsoadvanced,making the fuel one of the past year's best-performing commodities. At nearly $110 a metric ton, the price of thermal coal from Australia's Newcastle export hub is up by more than one-fifth from a year earlier. As recently as 2016, it fetched just $50 a ton.

Traders are divided on the reason.

Some big suppliers, including South Africa, have seen rising domestic demand limit the amount of coal available for export. South African state-owned power company Eskom this month rushed to buy 3 million tons of the fuel from domestic suppliers after its own stocks ran low.

On the demand side, analysts point to China, where imports have been booming as power plants burn coal at an increasingrate despite Beijing's efforts to support domestic miners by restricting supplies from overseas. Chinese thermal-coal imports increased more than 50% from a year earlier in March, while thermal-power production, which generates most of China's electricity, rose 1.4%.

"China is still the driver" for global coal markets, said Wood Mackenzie analyst Zhai Yu. The country accounts for about one-fifth of global seaborne coal demand.

Meanwhile, negotiations between the world's top thermal coal shipper, Glencore PLC, and one of its biggest buyers, Japan's Tohoku Electric Power Co., over annual coal contracts have been dragging on. Many market participants look to those contracts to set a benchmark for prices. As they remain unresolved, coal sellers elsewhere have continued to enjoy the upper hand in contract talks.

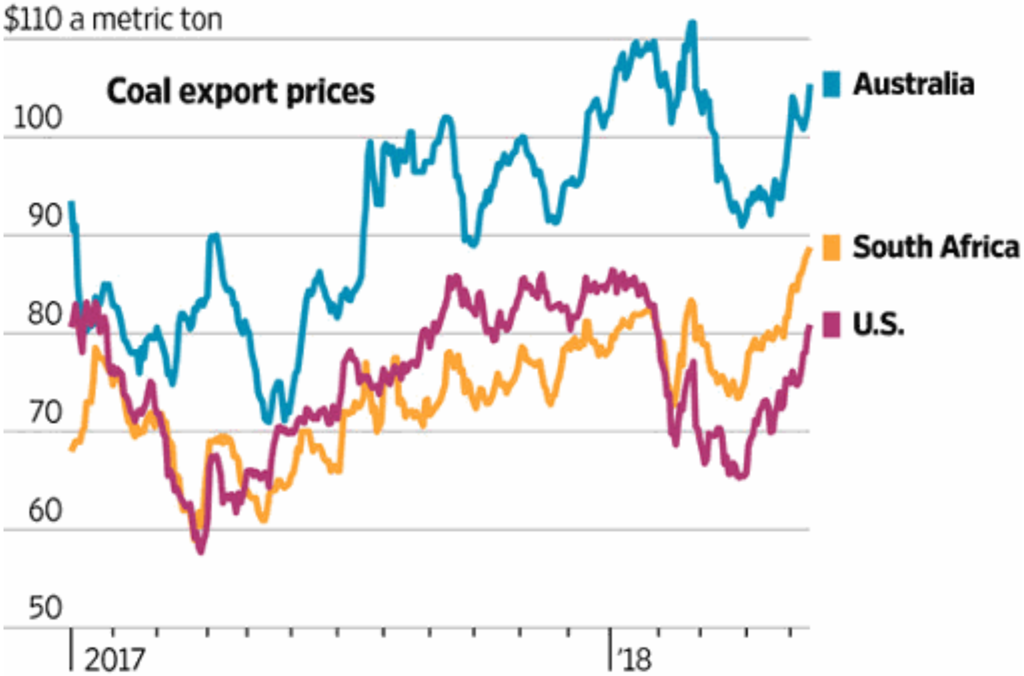
The price gains have come after a particularly chilly winter from Houston to Hamburg. Normally, prices moderate at this time of year, when warmer weather typically cools demand for burning coal.

How long the market will retain its glow is debatable. "Supply is continuing to rise," said Georgi Slavov, head of research at brokerage firm Marex Spectron, which should ultimately trigger a drop in prices.

Still, rising **oil prices** could lead to better-than-anticipated coal prices for the rest of the year. A stronger oil market tends to signal confidence in commodities, while increasing production costs for coal miners.

## Powering Back Up

Thermal-coal prices have been on a tear recently.




Notes: Price for Australia is FOB Newcastle 6,000 NAR; South Africa is FOB Richards Bay 5,500 NAR; U.S. is FOB U.S. East Coast 6,500 NAR. Data through May 14.
Source: S&P Global Platts

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THE WALL STREET JOURNAL.
U.S. EDITION

**Banking & Finance: For China-Listed Stocks, Wait Is Over --- MSCI taps 234 firms that will be included in its global benchmarks beginning June 1**

By Joanne Chiu
577 words
16 May 2018
The Wall Street Journal
J
B16
English


Global index provider MSCI Inc. has released a list of more than 200 Chinese stocks that it will include in its indexes starting next month, capping a yearlong process that is likely to attract billions of dollars into China's markets.

Last year, MSCI decided to include China-listed stocks in its global benchmarks after three years of rejections. Of the more than 3,000 companies listed in China, just 234 will be included in MSCI's indexes on June 1, largely in line with market expectations.

The initial batch of companies will have a 0.4% weighting in MSCI's Emerging Markets Index and a 1.3% weighting in the MSCI China Index.

Currently, the MSCI China Index comprises overseas-listed Chinese companies.

The weighting for China-listed stocks on both indexes is set to double in September, MSCI said Tuesday. While the inclusion of the stocks will likely have limited initial impact on Chinese shares, it comes as a much-needed boost to domestic markets, which have been among the worst performers world-wide this year. Concerns about the U.S.-China trade dispute have sent stock benchmarks in Shanghai and Shenzhen down more than 3% this year.

Louisa Fok, China equity strategist at Bank of Singapore, said about $18 billion will likely enter China's stock markets after MSCI's move, compared with the $70 billion average daily turnover of China's two major markets.

"It's a long road ahead for China's domestically listed stocks to be fully included to MSCI's index," she said, adding that it would take probably half a decade for the stocks to get full access to the global indexes.

MSCI said its decision to include China-listed stocks won "broad support from international institutional investors" and was primarily the result of the country's efforts to improve market accessibility.

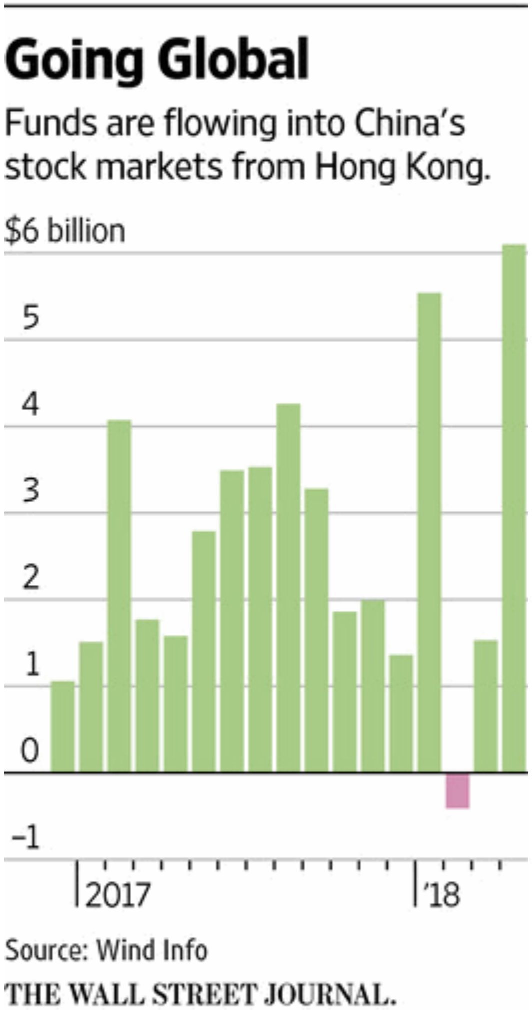
In recent years, China introduced two Stock Connect programs to link exchanges in Shanghai and Shenzhen with Hong Kong as part of its plans to open the country's markets to global investors. Chinese stock exchanges also eased preapproval requirements that can restrict the creation of index-linked investment vehicles globally.

Irmak Surenkok, a portfolio specialist at T. Rowe Price Group Inc., said despite the dominance of individual investors in China's domestic market, many foreign investors built up their portfolios after MSCI said in June that it would include China-listed stocks in its indexes in 2018.

However, foreign participation in Chinese stock markets was about 2% as of March, compared with close to 40% in other north Asian markets such as Taiwan and South Korea, Mr. Surenkok said.

"The opportunity set is immense," he said, noting that the U.S.-based money manager sees compelling opportunities in various consumption categories, technology and health care. Companies with underappreciated free-cash-flow growth within China's domestic market will also be a focus, said Mr. Surenkok.

In April, net inflows into Shanghai's **stock market** via the Stock Connect system more than quadrupled from a month earlier to 27.5 billion yuan ($4.3 billion), according to financial-data provider Wind Information Co. The figure for the smaller Shenzhen market more than tripled to 11.2 billion yuan over the same period.



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THE WALL STREET JOURNAL.
U.S. EDITION

The Property Report
**Investors Step Back Into Struggling REITs**

By Esther Fung
448 words
16 May 2018
The Wall Street Journal
J
B6
English


Real-estate investment trusts have been underperformers for the past two years in the U.S., but as merger activity increases some investors are giving them a look.

The FTSE Nareit All Equity REITs index produced a total return of 3.7% in March, compared with a 2.5% decline for the **S&P 500 stock index** over the same period. In April, the REIT index's total return of 0.5% outperformed the **S&P 500**'s 0.4%.

Still, despite the recent uptick, the REIT index had a total return of negative 6.2% in the first four months of the year, versus the **S&P 500**'s 0.4% decline.

"The tide is turning very slowly. It's not going to be a sea change," said Jonathan Woloshin, head of Americas equities and real estate at UBS Global Wealth Management's Chief Investment Office.

Commercial real-estate values have been appreciating for eight years, but expectations of a moderate slowdown rather than a hard landing are drawing some investors back, albeit cautiously, analysts said.

Within the different REIT sectors, some have continued to experience stable demand and healthy debt levels.

Going into 2018 there had been a view of decelerating real-estate fundamentals, but the first-quarter earnings came in line with or slightly better than expectations, said Thomas Bohjalian, executive vice president at global portfolio manager Cohen & Steers Inc. Among malls and shopping-center REITs, "the bottom didn't fall out as quickly as some investors believed would occur," Mr. Bohjalian said, adding that Cohen & Steers has recently increased its position in some shopping-center REITs.

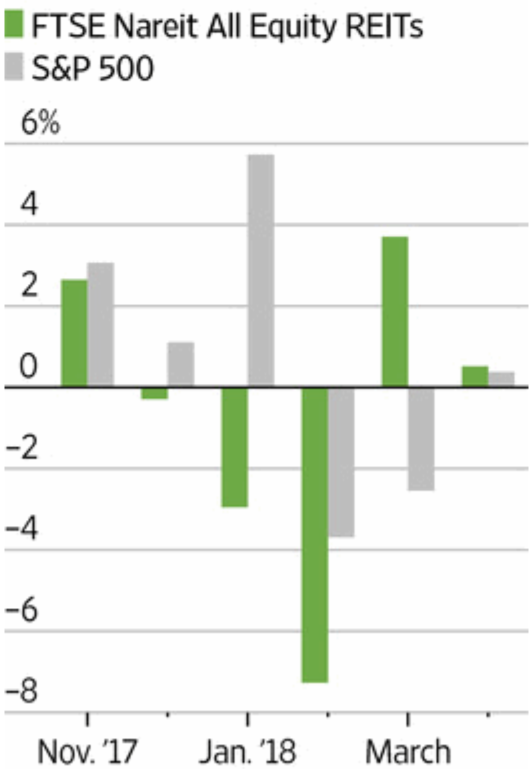
It is painful to see stock prices going down, but valuations are attractive, said Marc Halle, managing director at PGIM Real Estate, the real-estate investment unit of Prudential Financial Inc. and head of the global real-estate securities business. "REITs are a good indicator of the direction of private market values. But they tend to overdo it on the way up and on the way down."

In particular, investors have taken a shine to the industrial and multifamily sectors, which are enjoying strong demand and tight supply. In a recent report, Fitch Ratings pointed out that multifamily REITs with access to financing from government-controlled enterprises Fannie Mae and Freddie Mac would put them on steadier footing than other REITs if the availability of mortgage capital is disrupted.

Another thing working in favor of REITs is a recent increase in merger-and-acquisition activity, which is fueling hopes, especially among some investors, of bigger gains via buyouts.

## Warming Up

Some investors are tiptoeing back into REITs after the sector underperformed the S&P 500 index for the past two years.




Sources: Nareit; WSJ Market Data Group (S&P 500)

THE WALL STREET JOURNAL.

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WSJ PRO FINANCIAL REGULATION

Markets
**Volcker Rule 2.0 Draft Coming Soon | Coinbase Welcomes High-Speed Traders | Tracy's Take: Why Time Is Ripe for Volcker Overhaul; The Wall Street Journal's financial regulation newsletter for Wednesday, May 16, 2018.**

2,469 words
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Tracy's Take: Why Time Is Ripe for Volcker Overhaul

Volcker Rule 2.0 Draft Coming Soon

Big Bitcoin Exchange Welcomes High-Speed Traders

U.S. Sanctions Iran's Central Bank Governor, Alleges Hezbollah Ties

Why the Credit-Card Boom May Have Just Peaked

Why Time Is Ripe for Volcker Overhaul

Five U.S. regulatory agencies are poised to move ahead with changes to the Volcker rule, sooner than many observers thought possible. Why now?

Trump-nominated regulators had been expected to wait to propose changes to the rule, which restricts hedge-fund like activities at banks, at least until they had control of all five of the agencies responsible for enforcing it. They now control four, but Obama nominee Martin Gruenberg is still chairman of the Federal Deposit Insurance Corp.

For banking lobbyists and lawyers who work on the Volcker rule, the fear is that any proposal with Mr. Gruenberg's endorsement won't meaningfully change the rule.

It's possible Mr. Gruenberg could surprise banks with the changes he is willing to support. Regulators of all political stripes have been frustrated with the difficulty of applying the rule in practice. In previous public statements, Mr. Gruenberg has appeared more open to Volcker rule changes than to, say, changes to bank capital regulations.

The FDIC chief has another incentive to get a deal done under his watch: He'll have more ability to influence a proposal while he's in the chairman's seat.

Mr. Gruenberg's counterparts, led by Federal Reserve Vice Chairman for Supervision Randal Quarles, also have incentives to get a deal done soon. It is unclear when Mr. Gruenberg's likely successor, Jelena McWilliams, will be confirmed by the Senate.

In the meantime, Mr. Quarles has a lot on his regulatory agenda. Roughly six months into his tenure, the major proposals he has signed off on began under his predecessor. The Senate is about to pass a bill that will add new agenda items, not least of which is creating a new process for evaluating which banks with $100 billion to $250 billion in assets deserve regulatory relief.

Naturally, Mr. Quarles has his own priorities, which is why it wouldn't be surprising if he wanted to introduce the Volcker proposal as soon as possible, even though it might not go as far as it would if he waited for Ms. McWilliams to take the helm of the FDIC.

There is also the possibility that regulators could take more than one bite at the Volcker rule apple. Previous negotiations involving the five agencies have proven difficult, but talks appear to have moved more quickly this time. That suggests delay doesn't have to be the norm in the future.

Key Developments in Washington, on Wall Street, and Beyond

Volcker Rule 2.0 Draft Coming Soon

Large Wall Street banks would have more trading freedom under the Volcker rule as a result of changes U.S. regulators are considering, according to people familiar with the matter.

The draft changes to the rule, which restricts bankers' trading activities, are designed to lower the burden banks face to prove that short-term trades don't violate the rule, the people said. Regulators are also seeking to alter the definition of permitted hedging and market-making activities, to limit the rule's impact on non-U.S. investment funds, and to cut compliance requirements for banks with trading desks under a certain size, the people said. The changes could be published as soon as late May.

The overall impact of the changes, dubbed Volcker 2.0, isn't yet clear. The rule bans traders at taxpayer-insured banks from speculating but allows them to buy and sell securities in concert with customers' demand. It has been difficult to enforce. Bank traders, their lawyers and regulators constantly grapple with how to decide whether a given trade was executed with a customer in mind, or for the bank's own profit.

Big Bitcoin Exchange Welcomes High-Speed Traders

The bitcoin market is about to get a lot faster.

Coinbase Inc., which operates the largest U.S. cryptocurrency exchange, said on Tuesday that it would upgrade its systems with services that cater to ultrafast traders. The upgrade, planned for later this year, will make Coinbase one of the first bitcoin exchanges to welcome the controversial business of high-speed trading.

San Francisco-based Coinbase plans to introduce "low-latency performance," the company said in a blog post, using a term in the exchange industry that means extremely fast processing times. Coinbase also said it would allow trading firms to place their servers directly in its data center, a practice called co-location.

WSJ Pro: House Plans Vote on Bank Deregulatory Bill Next Week

The House is expected to vote as early as Tuesday, May 22, on legislation to ease the 2010 Dodd-Frank financial law, according to congressional aides, allowing the measure to go to President Donald Trump's desk and become law. The measure, which aims to cut red tape and compliance burdens for smaller banks, passed the Senate in March in a 67-to-31 vote.

U.S. Sanctions Iran's Central Bank Governor, Alleges Hezbollah Ties

The Treasury Department imposed sanctions Tuesday on the governor of Iran's central bank and another senior bank official, accusing them of funneling millions of dollars to Hezbollah, the Lebanese militia designated as a terror group by the U.S.

The Treasury Department said that Valiollah Seif, the governor of the Central Bank of the Islamic Republic of Iran, sent the funds to Hezbollah through an Iraqi bank, the al-Bilad Islamic Bank. The funds were sent on behalf of Iran's Quds Force, an Iranian paramilitary organization fighting in Syria along with Hezbollah to support President Bashar al-Assad.

The sanctions are part of a broader effort by the Trump administration to preclude the Quds Force from using the international banking system.

Hezbollah Said to Be Laundering Money in South American Tri-Border Region

Why the Credit-Card Boom May Have Just Peaked

Following some of their strongest years ever, credit-card issuers are grappling with an uneasy future.

Rising loan losses and increased rewards expenses are putting pressure on card lenders' returns. The result is that one of the most profitable consumer-lending categories in recent years may become more of a middling player.

 

While cards remain highly lucrative for banks, the benefits of a rising interest-rate environment have been muted lately. The added revenue of cardholders paying more in interest payments each month has also been offset by growing competition from lenders trying to poach card customers by offering lower rates.

Clarida, Bowman Affirm Commitment to Fed's Independence

Two of President Donald Trump's nominees to the Federal Reserve's board of governors Tuesday signaled a strong commitment to making policy decisions independently of the executive branch.

Richard Clarida, the economist tapped to serve as the central bank's No. 2 official, told lawmakers he had never been pressed by the president or other officials on how he would set interest rates. "In no meeting, at no time, did I ever have any reason to question the independence of the Federal Reserve, absolutely not," Mr. Clarida told the Senate Banking Committee at his confirmation hearing.

Democratic lawmakers pressed Mr. Clarida and a second nominee, Kansas Bank Commissioner Michelle Bowman, to state they would resist political interference.

More Than 200 China-Listed Stocks to Join MSCI's Indexes

Global index provider MSCI Inc. has released a list of more than 200 Chinese stocks that it will include in its key indexes from next month, capping a year-long process that is likely to attract billions of dollars into China's markets.

Last year, MSCI decided to include China-listed stocks in its global benchmarks after three years of rejections. Of the more than 3,000 companies listed in China, just 234 will be included in MSCI's indexes on June 1, largely in line with market expectations. The initial batch of companies will have a 0.4% weighting in MSCI's Emerging Markets Index and a 1.3% weighting in the MSCI China Index. Currently, the MSCI China Index comprises overseas-listed Chinese companies.

Analysis: Chinese Stocks Aren't Normal—Whatever MSCI Thinks

Analysis: What's Polarizing China's Bond Market?

Investors are demanding the highest premiums in two years for buying lower-grade Chinese corporate bonds, now that Beijing's campaign to rein in financial risk has made it harder for the country's weaker, mostly private firms to raise cash.

The sharp rise in borrowing costs is coinciding with an increase in both the number and value of defaults in China's $4 trillion corporate bond market. Growing concerns about the health of these firms is prompting investors to pile into bonds issued by China's higher-grade—and mostly state-owned—enterprises.

The premium yields on five-year Chinese corporate bonds with an AA- rating claim over those on corresponding government bonds increased to 3.63 percentage points on Friday, its highest since 2016. It has since narrowed to 3.57 points, higher than the 3.10 recorded at the start of this year.

Cybersecurity Whistleblowers Are a Growing Corporate Challenge

Signals from the Securities and Exchange Commission over how seriously it takes cybersecurity, combined with a Supreme Court ruling on whistleblower protections, are putting pressure on companies to be more careful about how they deal with potential tipsters, lawyers say.

The securities regulator issued guidance in February on how companies should handle cybersecurity issues. In April it fined Altaba Inc., formerly Yahoo Inc., $35 million over its handling of a 2014 hack, marking the first time the SEC penalized the victim of a breach.

"It's going to incentivize people inside an organization to step forward and disclose," said Brian Mahany, a whistleblower lawyer and founder of Mahany Law LLC. "I think the SEC is saying to companies, ‘We're taking this seriously. You take it seriously.'"

Money for Nothing

If paying a chief executive more doesn't do anything for the company's **stock price**, why pay the CEO more?

 

Last year was another one when the relationship between CEO pay and **stock market** performance was tenuous at best. American International Group 's Brian Duperreault (whose 2017 compensation package included a sign-on bonus for taking the job in May) and Allergan 's Brenton Saunders were among the best-paid CEOs in America, according to a Wall Street Journal analysis, yet their companies' share prices suffered. And the CEO pay packages of the five companies with the best-performing stocks were pretty average.

This isn't to say that the relationship between pay and stock performance was negative—it wasn't. Instead, on a scale where 1 is perfect correlation, minus 1 is perfectly inverse correlation, it was effectively zero. In plain English that means there is no connection between executive pay and stock performance.

FEATURED INTERACTIVE

How Does Your Pay Stack Up?

U.S. companies are, for the first time, disclosing how much a typical employee makes. Compare your compensation to the pay disclosed for the median employee of a particular company or sector, using data from more than 1,000 publicly traded companies collected by MyLogIQ.

Wednesday, May 16

10 a.m.

Stephanie Avakian and Steven Peikin, co-directors of the Securities and Exchange Commission's enforcement division, testify at a 10 a.m. hearing of the House Financial Services Subcommittee on Capital Markets, Securities, and Investment.

2 p.m.

Securities and Exchange Commission Chairman Jay Clayton speaks to venture investors on the commission's work to make public markets more accessible to venture-backed companies and plans to address regulation of cryptocurrencies and initial coin offerings.

2 p.m.

The House Financial Services Subcommittee on Terrorism and Illicit Finance holds a 2 p.m. hearing on the implementation of the Financial Crimes Enforcement Network's customer due diligence rule.

Thursday, May 17

8:30 a.m.

House Financial Services Chairman Jeb Hensarling (R., Texas) appears at a Politico breakfast to discuss the current state of the U.S. economy and fiscal fights ahead in 2018.

9 a.m.

The Consumer Financial Protection Bureau's Credit Union Advisory Council holds its spring meeting, including discussions on the Home Mortgage Disclosure Act and several of the CFPB's requests for information.

Low Risk as a Predictor of Financial Crises

Jon Danielsson, Marcela Valenzuela and Ilknur Zer explore the different early warning indicators of financial crises, finding that it would be beneficial for policy makers to use low **volatility** as one such indicator, in a Federal Reserve FEDS Notes post. "A major cause of financial crises is excessive risk-taking by economic agents. When they perceive a low risk environment, they are endogenously incentivized to take more risk, which ultimately culminates in a crisis," the post says.

Court Should Protect Fair Housing Rules From HUD Interference

The Federal District Court in Washington should force the Department of Housing and Urban Development to reinstate and fully enforce fair housing rules that "require communities to analyze segregation and submit plans for remedying it as a condition for drawing down billions of dollars in federal aid," writes the New York Times editorial board. HUD Secretary Ben Carson "is illegally trying to sweep aside" the rules, which would "make the process through which federal money is spent more transparent—giving fair-housing groups an opportunity to challenge discriminatory policies," the board writes. Congress could have overturned the rules, which became effective in 2015, but it didn't, reflecting "a growing awareness among members of both parties that it was smart policy to end reflexive ghettoization of the poor by giving low-income families access to areas that offered better job and educational opportunities," the board writes.

Circle Internet Financial Ltd., a digital-currency startup backed by Goldman Sachs Group Inc., is now worth about $3 billion after a new fundraising round.

Two activist hedge funds have built small stakes in Automatic Data Processing Inc., according to people familiar with the matter, adding pressure to the payroll-processing firm as it tries to jumpstart growth.

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

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THE WALL STREET JOURNAL.

Markets

**Tencent's Shares Were On Fire. Now They Aren't, and Analysts Are Getting Worried; The Chinese tech giant is nearing a bear market, while Asian markets were broadly lower Wednesday**

By Steven Russolillo and Joanne Chiu
535 words
16 May 2018
02:05 AM
The Wall Street Journal Online
WSJO
English


Asian markets were broadly lower on Wednesday, following declines in the U.S. that snapped a four-day rally. North Korea suspended high-level talks with Seoul, putting into question the planned U.S.-North Korea summit expected to take place next month. But South Korea's main benchmark, the Kospi index, was little changed on the news. Elsewhere in regional markets, Chinese and Hong Kong stocks fell. The **10**-**year treasury** yield jumped to 3.07%, its highest since 2011, as the U.S. dollar hovers near its 2018 highs.

Wednesday's Big Theme

Chinese tech giant Tencent Holdings Ltd., Asia's most valuable company, is nearing a **bear market**. The hope is that its earnings report, expected later Wednesday, could give the stock a lift.

What's Happening

Tencent, known for its messaging app WeChat, has long been Hong Kong's market darling.

The stock has gained about 40% annually over the past 10 years, outpacing U.S. tech titans like Apple Inc. and Amazon.com Inc. A $10,000 investment in Tencent a decade ago would be worth about $300,000 today.

Tencent's market cap has catapulted to around $500 billion, with its deal-making prowess helping it grow so fast. There are only a handful of companies around the world that big.

But 2018 has been different, at least for its **stock price**.

As the chart shows, Tencent rose for 13 straight months before peaking in January. The stock has since dropped about 17% (a **bear market** is a drop of at least 20% from a recent high). Shares have fallen for three straight months, and are clinging to small gains midway through May. The stock hasn't dropped for four consecutive months since China's markets collapsed in the summer of 2015.

And over the past decade, it has only had two other instances of four straight monthly declines—one in 2008, and the other in 2011.

Market Reaction

Usually **bullish** analysts are—ever-so-slightly—starting to worry. Deutsche Bank and Citi have trimmed their earnings estimates. Citi cites tougher year-over-year comparisons for Tencent's PC games and slower growth in mobile gaming.

Still, they by and large remain optimistic. The average Tencent price target remains above HK$500 ($64), according to FactSet, about 30% higher than where the stock currently trades. No analyst has a sell rating on the stock.

"All things being equal, we'd view any share-price weakness around first-quarter results as an enhanced buying opportunity," Citi says.

Elsewhere

Japan's economy shrank in the first quarter, the first time that's happened since 2015 and snapping its longest growth streak in 28 years. New Zealand stocks slid 1.6%, making them Asia-Pacific's biggest Wednesday decliner. One of that country's biggest companies, a2 Milk, offered a weaker-than-expected revenue forecast.

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The New York Times

Business/Financial Desk; SECTB

**Losses in Tech and Health Care End The Dow's 8-Day Winning Streak**

By THE ASSOCIATED PRESS
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16 May 2018
The New York Times
NYTF
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English


Losses in technology and health-care companies helped pull U.S. stocks lower Tuesday, snapping an eight-day winning streak by the **Dow Jonesindustrial average**.

The broad sell-off followed a slide in **bond prices**, which sent the **10**-**year Treasury** yield to its highest level in almost seven years. That paves the way for higher borrowing costs on mortgages and other loans.

The prospect of higher mortgage interest rates weighed on homebuilders, while the rise in bond yields sent shares in high-dividend paying stocks lower.

''We're of the view that we're not in a high-rate environment, we're in a less-low rate environment,'' said Erik Davidson, chief investment officer at Wells Fargo Private Bank. ''So we're not too concerned at these levels, but that's definitely driving the market today.''

The **S**.**&P**. **500 index** fell 18.68 points, or 0.7 percent, to 2,711.45. The Dow lost 193 points, or 0.8 percent, to 24,706.41. The drop pulled the 30-company average to a slight loss for the year.

The **Nasdaq composite** dropped 59.69 points, or 0.8 percent, to 7,351.63. The Russell 2000 index of smaller-company stocks finished flat at 1,600.34.

The market slide comes in the midst of a strong May for stocks. The Dow is on track for a gain of 2.2 percent, while the **S**.**&P**. **500** is closing in on a gain of 2.4 percent. The **Nasdaq** is up 4 percent.

On Tuesday, the bond market appeared to hold investors' focus.

The yield on the **10**-**year Treasury** rose to 3.07 percent from 3 percent late Monday. That is the highest level since July 2011 for the yield, which is used to set interest rates on mortgages and other kinds of loans.

The surge came after the Commerce Department said retail sales climbed 0.3 percent in April. The agency revised March sales higher to 0.8 percent from 0.6 percent. The retail sales data suggest that consumers are spending more after a weak first quarter. Bond yields tend to rise when investors expect faster economic growth and higher inflation.

The Federal Reserve has signaled that it will raise rates twice more this year, after having done so initially in March, and most economists foresee the next increase in June. Some Fed watchers have been cautioning that any lasting uptick in inflation or in economic growth might spur the Fed to pursue an additional rate increase before year's end.

''The **stock market** was due for a digestion of the gains that we've seen over the last eight trading sessions,'' said Quincy Krosby, chief market strategist at Prudential Financial.

The rise in bond yields pulled down shares in real estate investment trusts and other high-dividend paying stocks. Essex Property Trust fell 3.3 percent to $233.78.

It also put investors in the mood to sell their shares in homebuilders. Mortgage rates, which have been rising this year, tend to track the movement in the **10**-**year Treasury** yield. Higher mortgage rates can make it harder for would-be buyers to afford to purchase a home. D. R. Horton slid 6.7 percent to $40.58.

Some banks got a boost from the higher rates, which make loans more profitable. Capital One Financial rose 1.6 percent to $94.65.

The home-improvement retailer Home Depot dropped 1.7 percent to $187.98 after reporting weaker-than-expected sales, partly because of inclement weather.

Technology and health-care companies took some of the worst losses. Chipmaker Nvidia fell 3.8 percent to $245.56. The drugmaker Celgene slid 3.9 percent to $81.98.

Benchmark U.S. crude oil reversed an early side, rising 35 cents to settle at $71.31 a barrel in New York. Brent crude, used to price international oil, added 20 cents to close at $78.43 a barrel in London.

The dollar's gains weighed on precious metals prices. Gold fell $27.90, or 2.1 percent, to $1,290.30 an ounce. Silver dropped 38 cents, or 2.3 percent, to $16.27 an ounce. Copper slipped 4 cents, or 1.2 percent, to $3.06 a pound.

This is a more complete version of the story than the one that appeared in print.

CHARTS: The **S**. **& P**. **500 Index**: Position of the **S**. **& P**. **500 index** at 1-minute intervals on Tuesday. (Source: Reuters ); Retail Sales: Total retail and food services sales, seasonally adjusted. (Source: Commerce Department)

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**Can Super-Voting Stocks Survive the CBS Challenge? Lawsuit is related to its proposed merger with Viacom , but it's more broadly about the fairness of dual-class shares**

By Elizabeth Winkler
584 words
15 May 2018
02:43 PM
The Wall Street Journal Online
WSJO
English


CBS 's lawsuit against National Amusements , its controlling shareholder, is a last-ditch effort to block a merger with Viacom . But it is also a challenge to the company's dual-class stock structure and, by extension, similar structures that are increasingly common, especially among tech companies.

The challenge comes as these dual-class, or super-voting, structures are under fire by regulators, index providers and the courts.

National Amusements controls almost 80% of the voting stock in CBS , though only 10% of the shares. It is using that power to force a reluctant CBS to merge with Viacom , which it also controls. CBS is fighting back, using a provision in the company's charter that it claims allows it to issue shares to all stockholders, diluting National Amusements ' voting power from 80% to 17% and effectively blocking the deal.

National Amusements says CBS 's interpretation is wrong. The dispute will ultimately be decided by a Delaware court.

The provision was inserted in 2005 by Sumner Redstone, who controlled National Amusements and was concerned about the appearance that some shareholders would be favored over others, which is the long-running criticism of these structures. Yet he never thought it would be triggered against him since he could overhaul the board first.

In the short term, the case has likely set off a scramble among lawyers, corporate boards and investors looking for similar back doors at companies with dual-class structures. Whether they exist or not, the structures are under increasing pressure.

While dual-class stock can benefit investors in the early stages of a company, insulating it from short-term market pressures, studies show the benefit wanes. Firms that keep the structure trade at a discount to ones that end it, according to an analysis by Robert Jackson Jr., an SEC commissioner.

In a speech in February , Mr. Jackson said U.S. stock exchanges should force companies to retire their dual-class structure after a period of time.

Such a move is supported by academic research, which shows that super-voting power encourages personal enrichment by controlling shareholders at the expense of other shareholders.

Yes these structures have become increasingly popular. About 16% of companies that have gone public on U.S. exchanges since 2013 had at least two classes of stock, according to Dealogic, up significantly in the past decade. The structure has historically been most common at media and cable companies, like 21st Century Fox and Comcast and has been embraced by tech companies such as Google , Facebook and LinkedIn . When Snap Inc . went public last year, it gave new shareholders no voting rights at all.

The **S&P 500**took a stand against dual-class structures last year, barring public companies with multiple classes of shares from joining the index.

CBS could add to the pressure. "This case may be the ultimate acid-test of dual-class stock," says Charles Elson, director of the Center for Corporate Governance at the University of Delaware.

He points to increasing intolerance in the Delaware courts with how dual-class stock plays out. Shareholders have sued Facebook and Google for trying to create a new class of stock, and brought suit against National Amusements on the issue of Mr. Redstone's compensation. "I think they'll have to get rid of it," he says.

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THE WALL STREET JOURNAL.

Markets

**Bitcoin May Be Down, but a Digital Currency Startup Still Soars; Circle Internet Financial Ltd., backed by Goldman Sachs, now worth about $3 billion after new fundraising round**

By Telis Demos
521 words
15 May 2018
The Wall Street Journal Online
WSJO
English


A digital-currency startup backed by Goldman Sachs Group Inc. is now worth about $3 billion after a new fundraising round.

Circle Internet Financial Ltd. disclosed the new valuation Tuesday, making it one of the most highly valued financial technology startups in the U.S.

The increase in the Boston-based trading firm's value, more than seven times the level achieved at a prior fundraising in 2016, stems from the recent explosion of interest in bitcoin and other so-called digital assets.

Indeed, despite a 40% decline this year, bitcoin is still making fortunes for companies that deal in the **volatile** currency. In particular, it shows how some of the biggest winners from last year's 1375% surge in bitcoin, which was bested by other tokens including ether, may be the service firms that have formed to facilitate cryptocurrency trading and investment.

Those firms include Coinbase Inc., the most popular consumer bitcoin wallet, and Bitmain Technologies Ltd., a Chinese builder of computer chips for digital currency transactions that is leading the $110 million investment round in Circle announced Tuesday.

The fundraising, one of the largest ever among crypto startups, also includes new investments by venture-capital firm Blockchain Capital and Tusk Ventures, as well as more money from existing investors IDG Capital, Breyer Capital, General Catalyst, Accel and Digital Currency Group. Goldman is not among the new round's investors.

Five-year-old Circle's first product was designed for buying bitcoin and moving traditional money between individuals by using bitcoin as a medium of exchange.

But in the past year, its other business, facilitating big trades of digital currencies, has surged in volume and revenue.

That desk, called Circle Trade, says it has traded about $4 billion in the past month, handling trades from institutions, companies and wealthy individuals, Circle said. The company has said it generated $250 million in revenue from November to January.

By one measure, Circle is now the most valuable U.S. cryptocurrency startup. Its $3 billion equity valuation surpasses that of Coinbase, which raised money at a $1.6 billion valuation late last year, according to Dow Jones VentureSource.

Circle is one of a handful of so-called over-the-counter market makers who augment the smaller-value trades on exchanges, alongside such firms as Cumberland Mining. At least one big bank, Goldman, is exploring a role for itself in trading around cryptocurrencies.

As part of the funding, Bitmain will also join Circle's new project to launch new digital coins that can be exchanged for a fixed amount of traditional, or fiat, currency.

Jeremy Allaire, Circle's chief executive and co-founder, said the new coin and fundraising is part of the company's "long-term vision for what's possible in building a new global economic system."

Circle also recently acquired a digital asset exchange, Poloniex, and a retail investment application, now called Circle Invest.

Write to Telis Demos at telis.demos@wsj.com

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WSJ PRO FINANCIAL REGULATION

Markets

**Volcker Rule 2.0 Draft Coming Soon; Revamp would give Wall Street firms more freedom to trade; regulators' proposal expected as soon as late May**

By Ryan Tracy and Dave Michaels
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RSTPROFR
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WASHINGTON—Large Wall Street banks would have more trading freedom under the Volcker rule as a result of changes U.S. regulators are considering, according to people familiar with the matter.

The draft changes to the rule, which restricts bankers' trading activities, are designed to lower the burden banks face to prove that short-term trades don't violate the rule, the people said. Regulators are also seeking to alter the definition of permitted hedging and market-making activities, to limit the rule's impact on non-U.S. investment funds, and to cut compliance requirements for banks with trading desks under a certain size, the people said. The changes could be published as soon as late May.

The overall impact of the changes, dubbed Volcker 2.0, isn't yet clear. The rule bans traders at taxpayer-insured banks from speculating but allows them to buy and sell securities in concert with customers' demand. It has been difficult to enforce. Bank traders, their lawyers and regulators constantly grapple with how to decide whether a given trade was executed with a customer in mind, or for the bank's own profit.

Regulators say their goal is to draw clearer boundaries, but previous attempts to clarify the rule haven't succeeded.

"It's only going to work if the change also creates a clearer, crisper rule," said Margaret Tahyar, a partner in Davis Polk & Wardwell LLP's financial institutions group. "You could change it and still have mush."

In general, officials appointed by the Trump administration say the Volcker rule has an adverse effect on liquidity in **financial markets**. But they also have repeatedly said they don't think taxpayer-insured banks should be trading for themselves the way hedge funds do.

The Volcker rule is one reason behind some banks' decisions to scale back trading desks in recent years. Other regulations have hit those businesses, too. Many banks have also focused on steadier, less risky strategies since the 2008 financial crisis.

Mitigating the industry's expectations about Volcker 2.0 is the fact that Federal Deposit Insurance Corp. Chairman Martin Gruenberg, an Obama appointee who supports the trading ban, remains in office.

Mr. Gruenberg's FDIC is one of the five agencies poised to sign on to the new proposal, the people familiar with the matter said. The other agencies are the Federal Reserve, the Office of the Comptroller of the Currency, the Securities and Exchange Commission and the Commodity Futures Trading Commission—all led by appointees of President Donald Trump.

While Mr. Gruenberg and other Obama appointees have been supportive of revisiting the rule, they aren't expected to back changes that would significantly loosen the reins on Wall Street banks. Mr. Gruenberg's appointed successor, banking lawyer Jelena McWilliams, is still awaiting confirmation by the Senate.

As recently as late April, regulators had broadly agreed on the parameters of a Volcker 2.0 proposal but were still negotiating details. Those included provisions dealing with whether a bank's chief executive must attest to Volcker rule compliance, and how the rule treats swaps and clearing activities, a person familiar with the matter said.

The agencies plan to eliminate a requirement that bankers prove positions held for less than 60 days are legitimate customer-focused trades, rather than speculation, these people said. Regulators also plan to rework the criteria for determining whether trading activities qualify as permitted hedging or market making, these people said.

These changes could have the effect of lowering the burden on bankers to prove certain trading activity is allowed, giving traders more freedom. On the other hand, regulators might not lift that burden entirely, so the effect of the changes will depend on the fine print.

In general, a core goal of regulators is to tailor the rule by lowering the compliance burden for firms with smaller trading desks, people familiar with the matter said. A bill under consideration in Congress would exempt banks with small trading books and less than $10 billion in total assets from the rule. The draft proposal seeks to give relief to firms with larger balance sheets that still have relatively small trading desks, these people said.

Another piece of the proposal is designed to make it clear that the Volcker rule doesn't apply to certain investment funds outside the U.S., these people said. That is consistent with previous decisions by regulators to delay the rule's applicability to those funds, which had been caught in limbo under the original rule.

Any proposed changes will be followed by a public comment period before regulators complete them.

Lalita Clozel contributed to this article.

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THE WALL STREET JOURNAL.

Markets

**Capital Spending Boom Is No Great Boost to Capital Markets; Capex spending by S&P 500 companies is expected to rise 24% in first quarter to $166 billion. But do investors want it?**

By Akane Otani, Ben Eisen and Chelsey Dulaney
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U.S. companies are ramping up spending on their businesses at the fastest pace in years, a long-awaited development after years of tepid growth.

Spending on factories, equipment and other capital goods by companies in the **S&P 500** is expected to have risen to $166 billion in the first quarter, up 24% from a year earlier, according to Credit Suisse data going back to 1995. It is on track for the fastest pickup since 2011 and a record for the first quarter of a year. The jump has been aided by the U.S. tax-code overhaul, which is putting more cash in companies' coffers.

The biggest spenders run the gamut, from technology behemoths such as Google parent Alphabet Inc. to car maker General Motors Co. and oil giant Exxon Mobil Corp.

Investors and economists agree that capital expenditure, or capex, is good for long-term corporate profits and the broader economy, which has languished for years without such spending. Yet history suggests it also could pressure share prices—leaving investors questioning whether it is worthwhile to bet on companies with costly projects that may not pan out, especially at a time when many are wondering whether corporate earnings are as good as they will get in this economic cycle.

"When it works, it's a home run. But for investors who are sometimes much more short-term oriented, it's easy to understand why a dividend increase that I'll get next month is a little more exciting than capex, which might not yield me anything for a long time," said Dave Donabedian, chief investment officer at CIBC Atlantic Trust Private Wealth Management.

The jump in capital spending comes as companies whittle away at massive stockpiles of cash—something that has allowed them to funnel money into their businesses and increase their dividends, as well as buy back their shares at a record pace. Buybacks often provide a short-term boost to stock prices, although they have been maligned by critics who feel that, unlike capex, they do little to boost long-term profitability.

Data suggest that shares of companies with large and growing capex tend to underperform the broader **stock market**—which could weigh on returns just as the market has become more **volatile**.

Shares of the 20 companies in the **S&P 500** that spent the most on capex in the first quarter are up 0.5% for the year, trailing the broad index's 1.4% gain, according to analysis of data from S&P Dow Jones Indices. The trend becomes even more pronounced over longer time horizons: Since 1986, companies with the highest capex-to-sales ratios have underperformed the **S&P 500** by more than 2 percentage points on average each year, according to Bank of America Merrill Lynch.

As a share of gross domestic product, private nonresidential fixed investment—a commonly used proxy for capex—has been rising for more than a year. It remains below levels hit in 2014, when soaring crude-**oil prices** pushed energy companies to spend heavily, according to a Credit Suisse analysis of government data.

The capex boom could be a tonic for a **stock-market** lull that has kept the **S&P 500** and **Dow Jones Industrial Average** in a narrow range for months, and offer a further boost to corporate earnings. But research shows it isn't that clear-cut.

"Greater investment and high valuations imply that we probably won't experience a **stock market** boom in the next couple years," said Christopher Anderson, a University of Kansas professor. His 2006 research found that companies that have the biggest increases in capital spending have subsequently had underperforming stock returns.

Capital spending has been growing rapidly in the tech industry, where companies that have seen some of the biggest share-price growth in recent years are becoming increasingly capital intensive. More than half of the growth in first-quarter capex spending can be attributed to the tech sector, Credit Suisse data show.

Investments in data centers, undersea cables and New York City real estate pushed Alphabet's capex tab in the first quarter to $7.3 billion—the most of any **S&P 500** company, and nearly triple what it spent a year earlier.

Although Alphabet's quarterly profits surged thanks to strong demand from advertisers, its shares tumbled 4.8% on the day following its earnings report as investors questioned the sustainability of the costliest spending spree in the firm's 14-year history as a public company. The stock has since rebounded. The company has said it believes these investments will create shareholder value.

Investors have been wary of other companies ramping up spending.

Shares of the second-biggest capex spender in the **S&P 500**, GM, have slumped 9.9% this year in part as the costs tied to a revamp of its pickup trucks—the most extensive such redesign in two decades—have cut into profit.

In the energy sector, shares of companies that have prioritized boosting buybacks and dividends have tended to outperform those deploying cash to drill for more oil. ConocoPhillips stock has surged 28% even as Exxon Mobil, the seventh-biggest capex spender in the first quarter, has fallen 2.2%.

Not all big capex-spending companies have struggled in the **stock market**. Shares of e-commerce giantAmazon.com Inc. have soared 35% in 2018, adding to double-digit percentage gains in 2017, as the company's sales growth outshone increased spending on warehouses, expanding its delivery network and amping up its digital offerings.

"You do not want to see companies spending above their normal trend. That historically has been negative for stock prices," said John Bailer, a senior portfolio manager at BNY Mellon Asset Management North America.

The cut to the corporate tax rate and a deregulatory agenda in Washington are giving businesses more certainty about how to spend their growing cash piles. But rising interest rates and the threat of more restrictive trade policies could restrain economic growth. Economists surveyed by The Wall Street Journal expect a U.S. recession could come as soon as 2020.

To some investors, the murky outlook is another reason to gravitate toward companies that can deliver steady shareholder returns.

Mr. Bailer of BNY, who said he is investing in companies that limit spending while focusing on boosting dividends and buybacks, is **bullish** on banks, refiners and technology companies. "If I can get a bigger percentage of [a company's] cash flow, I think that is a great thing," he said.

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THE WALL STREET JOURNAL.

U.S. Markets
Markets

**Dow Industrials Snap Winning Streak; Home Depot weighs on blue chips after quarterly sales miss expectations**

By Georgi Kantchev and Allison Prang
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U.S. stocks fell Tuesday, with the **Dow Jones Industrial Average** breaking an eight-session streak of gains, as investors parsed mixed economic data, rising government-bond yields and continuing trade negotiations between the U.S. and China.

A rare spurt of synchronized global growth at the end of last year and the beginning of 2018 has underpinned stock markets around the world, so investors are sensitive to any signs of a slowdown. In the U.S., data have also been coming in somewhat below expectations in recent months.

The **Dow Jones Industrial Average** declined 193 points, or 0.8%, to 24706.41, after earlier dropping as much as 270 points. The **S&P 500** dropped 18.68 points, or 0.7%, to 2711.45, and the **Nasdaq Composite** fell 59.69 points, or 0.8%, to 7351.63.

Through Monday, the blue-chip index had risen 974 points, or 4.1%, since May 3 as stocks appeared to be regaining their footing after several months of rocky trading. But Tuesday's declines pushed the Dow industrials back into negative territory for the year. A number of factors, including trade concerns, geopolitical tensions, signs of a pickup in inflation and peaking corporate earnings, have kept some investors on the sidelines.

The U.S. Commerce Department said Tuesday that U.S. retail sales rose 0.3% on an adjusted basis in April, which was in line with expectations of economists polled by The Wall Street Journal. Retail sales also increased in March, after falling for three months in a row.

Ryan Kelley, portfolio manager at Hennessy Funds, said the latest retail sales numbers sparked worries inflation could pick up, forcing the Federal Reserve to increase rates faster than planned.

"It's just simply a pause in a very strong last eight days," he said.

Meanwhile, inflation worries also cropped up in the latest survey from the National Association of Home Builders, which pointed to rising costs of lumber as a challenge to the residential construction industry. D.R. Horton, Lennar and PulteGroup all dropped more than 5%.

Ten of the 11 sectors in the **S&P 500** fell Tuesday, while shares of energy companies ticked slightly higher. Home Depot shares dropped $3.10, or 1.6%, to $187.98, weighing on the Dow industrials, after the company's quarterly sales came in short of expectations.

The yield on the 10-year U.S. Treasury note settled at 3.082%, up from 2.995% Monday, its largest one-day yield gain since March of last year. It crossed 3% for the first time since 2014 last month, leading to concerns among some investors that rising interest rates could start to make stocks look less attractive relative to bonds. Yields move inversely to prices.

The WSJ Dollar Index, which tracks the dollar against a basket of 16 currencies, was up 0.6%.

Other data on Tuesday showed growth in the eurozone economy slowing to 0.4% in the first quarter from 0.7% in the fourth quarter of last year. Economic activity cooled in Germany, France and the Netherlands.

China, meanwhile, reported mixed results for business activity, adding to signs of cooling in the world's second biggest economy. Industrial output quickened last month from a year earlier, but investment and retail sales slowed.

"We still see the global economy as growing but perhaps not at the previous furious pace," said Terry Sandven, chief equity strategist at U.S. Bank Wealth Management.

Just 1% of investors think the global economy will strengthen over the next 12 months, according to Bank of America Merrill Lynch's monthly global fund manager survey released Tuesday. That is the lowest level since February 2016.

Investors were also monitoring trade negotiations between the U.S. and China. Escalating trade tensions have kept markets on edge in recent months, with the U.S. also locked in negotiations over tariffs with Europe and Japan.

Washington and Beijing appeared close to a deal that would give China's ZTE a reprieve from potentially crippling U.S. sanctions in exchange for Beijing removing tariffs on billions of dollars of U.S. agricultural products.

"Trade has been weighing on equities, so any thaw in tensions will be helpful for performance," said Mr. Sandven.

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THE WALL STREET JOURNAL.

Markets

**Long-Suffering REITs Might Be Turning a Corner At Last; Investors have taken a shine to the industrial and multifamily real-estate sectors**

By Esther Fung
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U.S. REITs have been underperformers for the past two years—but as merger activity increases, some investors are giving them a look.

The FTSE Nareit All Equity REITs index produced a total return of 3.71% in March, compared with a 2.5% decline for the **S&P 500 index** over the same period. In April, the REIT index's total return of 0.52% outperformed the **S&P 500**'s 0.4%.

Still, despite the recent uptick, the REIT index had a total return of negative 6.2% in the first four months of the year, versus the **S&P 500**'s 0.4% decline.

"The tide is turning very slowly. It's not going to be a sea change," said Jonathan Woloshin, head of Americas equities and real estate at UBS Global Wealth Management's Chief Investment Office.

Commercial real-estate values have been appreciating for eight years, but expectations of a moderate slowdown rather than a hard landing are drawing some investors back, albeit cautiously, analysts said.

Within the different REIT sectors, some have continued to experience stable demand and healthy debt levels against the backdrop of a still-humming economy and job growth.

Going into 2018 there had been a view of decelerating real-estate fundamentals, but the first-quarter earnings came in line or slightly better than expectations, said Thomas Bohjalian, executive vice president at global portfolio manager Cohen & Steers Inc. Among malls and shopping-center REITs, "the bottom didn't fall out as quickly as some investors believed would occur," Mr. Bohjalian said, adding that Cohen & Steers has recently increased its position in some shopping-center REITs.

It is painful to see stock prices going down, but valuations are attractive, said Marc Halle, managing director at PGIM Real Estate, the real-estate investment unit of Prudential Financial Inc. and head of the Global Real Estate Securities business. "REITs are a good indicator of the direction of private market values. But they tend to overdo it on the way up and on the way down."

In particular, investors have taken a shine to the industrial and multifamily sectors, which are enjoying strong demand and tight supply.

In a recent report, Fitch Ratings pointed out that multifamily REITs with access to financing from government-sponsored enterprises Fannie Mae and Freddie Mac would put them on steadier footing than other REITs if the availability of mortgage capital is disrupted.

Another thing working in favor of REITs is a recent increase in merger-and-acquisition activity, which is fueling hopes, especially among impatient investors, of bigger gains via takeouts.

Private-equity giant Blackstone Group LP is buying industrial and office real-estate investment trust Gramercy Property Trust for $4.42 billion in cash, while Prologis Inc. made an $8.4 billion stock-for-stock offer for DCT Industrial Trust Inc., including debt. Both offered roughly a 15% premium.

Lodging REIT Pebblebrook Hotel Trust sweetened its stock-for-stock bid for LaSalle Hotel Properties twice and its final offer in late April implied a 31% premium to LaSalle's closing share price on March 27. LaSalle said it was reviewing the proposal.

"Takeout odds are REIT investors' favorite topics. It's the REIT version of TMZ," said Cedrik Lachance, Green Street Advisor's director of REIT research, referring to the celebrity gossip site. Investors often talk about personalities and mull over the age and career paths of CEOs and board members to speculate if these individuals are partial to a deal, he added.

To be sure, there is some skepticism about how much upside could be gained from any deal activity among retail REITs, especially after a revised offer price from Brookfield Property Group for GGP Inc. was deemed underwhelming among REIT investors. PGIM Real Estate said it reduced its holdings of mall REITs as their share prices gained ground on shareholder activism in the fourth quarter.

Green Street said it had a more tangible approach to address takeout odds based on prevailing share values. Of the 83 REITs it covers, nearly 40% had takeout odds of 10% or greater in the first quarter, up from about 20% of REITs in the previous quarter. Green Street also assigns an estimated takeout price to each REIT on the list, which might not be at a premium to their net asset values.

The top of the list includes a large portion of mall and strip-center REITs such as Taubman Centers Inc., Macerich Co., DDR Corp, Kimco Realty Corp, and Brixmor Property Group Inc. Green Street noted that the companies have been persistently trading at a discount to net asset value for the past two years, making them ripe for acquisition.

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THE WALL STREET JOURNAL.

Markets
**Big Bitcoin Exchange Welcomes High-Speed Traders; Coinbase plans to allow trading firms to place servers directly in its data center, a practice called co-location**

By Alexander Osipovich
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The bitcoin market is about to get a lot faster.

Coinbase Inc., which operates the largest U.S. cryptocurrency exchange, said on Tuesday that it would upgrade its systems with services that cater to ultrafast traders. The upgrade, planned for later this year, will make Coinbase one of the first bitcoin exchanges to welcome the controversial business of high-speed trading.

High-frequency trading, or HFT firms, use computers to buy and sell stocks, futures and other assets in the blink of eye. They accounted for 55% of trading volume in the U.S. **stock market** last year, according to research firm Tabb Group LLC, but they have only recently begun to dabble in cryptocurrencies.

San Francisco-based Coinbase plans to introduce "low-latency performance," the company said in a blog post, using a term in the exchange industry that means extremely fast processing times.

Coinbase also said it would allow trading firms to place their servers directly in its data center, a practice called co-location. HFT firms often put their servers next to the computers that power exchanges like **Nasdaq** Inc. or the New York Stock Exchange, to minimize the split-second delays associated with transmitting data back and forth between the trading firm and the exchange.

According to Coinbase, the plan will benefit customers by reducing bid-ask spreads—the difference between the buying and selling price of an asset. Advocates of HFT say the growth of high-speed trading in the **stock market** over the past two decades helped drive bid-ask spreads down to just one penny in many big stocks.

But Coinbase's move is likely to raise eyebrows, since many investors view high-speed traders with suspicion. Critics like Michael Lewis, author of the 2014 best-seller "Flash Boys," have alleged that HFT firms take advantage of slower-moving players.

Coinbase will ensure that HFT firms aren't given any unfair advantages, said Adam White, general manager of Coinbase's exchange, called GDAX.

"We are going to be thoughtful and deliberate in the way we do that, to make sure we don't disadvantage any market participant over another," Mr. White said in an interview.

After the upgrade is complete, processing times at Coinbase will be measured in microseconds, or millionths of a second, Mr. White said. Greater participation by electronic traders will boost the depth of Coinbase's markets and help the company win over big institutional traders, such as hedge funds, which are increasingly interested in trading crypto, Mr. White added.

But Joe Saluzzi, a partner at brokerage Themis Trading and a vocal critic of HFT, warned that crypto exchanges may find it lucrative to offer special perks to high-speed traders.

"The stock exchanges in the **equity market** were the 'arms merchants' that sold speed advantages to HFT so they could be faster than traditional investors," Mr. Saluzzi said in an email. "It looks like Coinbase wants to be one of the arms merchants for the crypto world."

Coinbase isn't the first bitcoin exchange to gear its systems for ultrafast traders. Gemini, the New York-based crypto exchange founded by Cameron and Tyler Winklevoss, said its trade-execution times are already a matter of microseconds. Gemini's systems are based in the same New Jersey data center used by Cboe Global Markets Inc., a major options and equities exchange operator.

Several electronic trading firms are already active in cryptocurrencies, including Chicago-based DRW Holdings LLC and Jump Trading LLC and New York-based Hudson River Trading LLC, Jane Street Group LLC and Virtu Financial Inc.

But many crypto exchanges operate on relatively slow and flimsy technology, compared with the powerful, battle-tested computer systems used by **Nasdaq** or the NYSE. Last year, a number of digital-currency exchanges suffered outages during periods of heavy investor interest in bitcoin, including GDAX and Europe-based Bitstamp.

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The New York Times

Business/Financial Desk; SECTB
**Big Indexes Inch Up, but Small Companies Give Back Gains**

By THE ASSOCIATED PRESS
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15 May 2018
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Late Edition - Final
5
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The major stock indexes eked out small gains Monday after a late-afternoon pullback weighed on small-company shares.

The market had been broadly higher earlier in the day on hopes that trade tensions were easing between the United States and China. But much of that rally faded, leaving decliners on the New York Stock Exchange outnumbering risers.

Gains by health care and energy stocks outweighed losses in real estate companies and other decliners. Casino operators and equipment companies were lifted by a Supreme Court decision that cleared the way for states to legalize sports betting.

The **Standard & Poor's 500**-**stockindex** added 2.41 points, or 0.1 percent, to 2,730.13. The **Dow Jonesindustrial average** climbed 68.24 points, or 0.3 percent, to 24,899.41. The **Nasdaq composite** rose 8.43 points, or 0.1 percent, to 7,411.32.

Small-company stocks fell. The Russell 2000 index lost its early gains, sliding 6.45 points, or 0.4 percent, to 1,600.34.

The major stock indexes' latest gains added to the market's solid run this month. Last week, the **S**.**&P**. **500**, the benchmark for the broader **stock market**, had its best weekly gain since early March.

The indexes got off to a strong start Monday, as investors hoped for reduced trade tensions between the United States and China after President Trump tweeted over the weekend that he would help the Chinese telecommunications company ZTE get ''back into business.''

ZTE's Hong Kong-traded shares have been suspended since United States authorities barred it last month from importing American components for seven years in a case involving illegal exports to North Korea and Iran. But Mr. Trump said too many jobs in China were at stake after federal sanctions cut off access to ZTE's American suppliers.

Fears of retaliatory tariffs and other trade disruptions roiled the market earlier this spring before the latest raft of company earnings captured investors' focus.

The president's tweet about ZTE may be a sign that trade negotiations between the United States and China are relatively constructive, if not friendly, said Brian Nick, chief investment strategist at Nuveen Asset Management.

''If you have concessions being made like that on one or both sides, it probably means that the worst-case outcome is less likely, which would be a good thing for stocks,'' Mr. Nick said.

''In general, the market probably overreacted to the trade-related noise that started popping up around March 1. There was this sense that we might get this worst-case-scenario trade war, and that seemed to be priced in relatively quickly, and we're starting to see it priced out of equity valuations now.''

Qualcomm and NXP Semiconductors also rose as investors anticipated that Chinese regulators would reverse their stance and approve Qualcomm's proposed $44 billion acquisition of NXP.

China is the final major government withholding approval of the deal, but Bloomberg News reported that Chinese regulators were reviewing the deal again.

Qualcomm rose 2.7 percent to $56.74, while NXP surged 11.8 percent to $110.74.

Investors continued to bid up shares in health care companies. CVS Health gained 3.7 percent to $66.82.

Xerox slid 4.3 percent to $28.87 after it ended merger talks with Fujifilm and resolved a dispute with the investors Carl Icahn and Darwin Deason.

Benchmark United States crude oil rose 26 cents to settle at $70.96 a barrel in New York. Brent crude, used to price international oils, gained $1.11, or 1.4 percent, to $78.23 a barrel in London.

Rising **oil prices** helped lift energy stocks. Range Resources added 3.3 percent to $14.76.

**Bond prices** fell. The yield on the **10**-**year Treasury** rose to 3 percent from 2.97 percent late Friday.

The dollar rose to 109.65 yen from 109.30 yen on Friday. The euro weakened to $1.1937 from $1.1943.

Gold fell $2.50 to $1,316.50 an ounce.

This is a more complete version of the story than the one that appeared in print.

CHARTS: The **S**. **& P**. **500 Index**: Position of the **S**. **& P**. **500 index** at 1-minute intervals on Monday. (Source: Reuters ); 3-Month Treasury Bills: High rate at weekly auction. (Source: The Bond Buyer)

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WSJ PRO CENTRAL BANKING

Economy

**Transcript: Audience Q&A With Fed's John Williams in Minneapolis; Official talks about the outlook for interest rates, the central bank's 2% inflation target and reducing the Fed's balance sheet**

5,099 words
15 May 2018
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English


Federal Reserve Bank of San Francisco President John Williams answered questions from the audience at an Economic Club of Minnesota event in Minneapolis on Tuesday, May 15, 2018. He discussed the outlook for interest rates, the reasoning behind the U.S. central bank's 2% inflation target, the continuing reduction of the Fed's balance sheet and the practice of paying interest on reserves parked at the Fed. Here is a transcript of the exchange, lightly edited for length and clarity.

CHRISTINE M. CUMMING: So you talked a little bit about inflation, but could you say a little bit more? Do you think we're bound to see low rates of inflation for a long time?

JOHN WILLIAMS: So, when I went to grad school, the thing I was told that I would be focused on in my career was high inflation and how to bring inflation down. And all of the theories and models we studied was, you know, how to deal with the very high inflation that obviously happened in previous decades. In fact, low inflation is the challenge that not only we face, but in Europe and Japan and many other countries has had inflation consistently below their desired levels.

I think the U.S., actually, we're a bit ahead of the curve, as we were in our expansion. I think in part – in large part between a very – because of the very stimulative policies the Fed did, we've managed to get the economy back on track. We've managed to get inflation back to 2 percent.

I still am not ready to say mission accomplished. I don't think I'll say mission accomplished anyway. (Laughter.) But we're – inflation is – it just barely reached our 2 percent goal. Inflation has been running below our goal for years. I do want to see a sustained increase in our inflation around 2 percent. We've emphasized at the [Federal Open Market Committee], which is very important, the idea of symmetry of our goal. It's OK for inflation sometimes to be a little bit above 2 percent, a little bit below 2 percent, but we want it on average to be at 2 percent. And I feel that we're in a very good position to see – to accomplish that over the next year or two.

I'm not really worried about higher inflation yet. Even though the economy is really strong, with unemployment below 4 percent, wage increases have been I think more or less consistent with what we're seeing in inflation and productivity. The inflation pickup we've seen is really consistent with an economy that's kind of running at – you know, a very strong economy, but not one that's overheating at all or signs of overheating.

So I would say that my views on inflation have gone from more kind of worried about the downside, which is what you're asking about, to being more balanced. We're just trying to maintain what I think of as a "Goldilocks" economy: inflation around 2 percent, you know, an increase in – you know, good increases in wages, and a very strong labor market. You know, the challenge for us is really just keeping the economy continuing to grow the way it has been and keeping it, you know, in a well – in a good balance.

I do think that – getting a little philosophical here, I think all central banks should be really thinking hard about the lessons of the last decade, about how hard it's been to get inflation back up to where we want it to be. So, like I said, when I was in grad school I was prepared to deal with high inflation. I think we all need to be rethinking not only our models and our analysis, but also rethinking more fundamentally our approaches to monetary policy so that, you know, we can manage a world where low inflation may be an ongoing challenge.

MS. CUMMING: Great. So let's take some questions from the audience. We have spotters. If you could, give your name and affiliation and then ask your question. There you go.

Q: My name's Paul Grangaard and I'm with a new company called Circlerock (sp).

I'm always curious, why do we want 2 percent inflation? Why isn't – why isn't our goal stable prices? When I was in economics classes, I thought we wanted stable prices. So why do you come to this 2 percent number?

MR. WILLIAMS: Yeah, it's a terrific question. You know, honestly, I think we don't – we don't explain this as well as we could. I personally feel this way, because I think it's a – it's a great – it's a really good question.

So there's – so we are – we did decide back in 2012 at the Federal Open Market Committee – and we've renewed this commitment every year – that we want to see on average over the medium term a 2 percent inflation rate. The Federal Reserve Act says stable prices, but it also says maximum employment.

So the answer to the question is, first of all, on the inflation, that we know that for technical reasons that economists understand that the inflation rate overstates how much inflation there is because of just measurement and technical challenges. So that probably means that the true inflation rate is actually a little bit less than what we're measuring.

But I think the more important reason is we have this dual mandate which I, you know, firmly support, which is maximum employment and price stability. And we know that if we had a zero percent inflation rate or a half percent inflation rate, something very low, we would run into two challenges in achieving our maximum employment goal and our growth goals.

One would be that we would be hitting the zero lower bound issue, where interest rates – because inflation is low, interest rates are low, we would be challenged in order to stimulate the economy during recessions, as we saw in the last recession around the world where central banks, you know, were limited in how low interest rates can go negative. In the Fed, we didn't even go negative. And so, with a very low inflation baseline, a very low R-star baseline, it would mean a central bank – the Fed would not have as much room to stimulate the economy in a recession.

The second is we know from research that there are distortions around deflation and very low inflation. Firms – and we have all the micro data that shows you this – firms are really reluctant to cut wages. So when you're in a world where wage and inflation growth are very low, you get this problem that businesses basically are not able to adjust the wages in accordance to economic conditions. Having a little bit more inflation in the background greases the wheel, allows wages to adjust without them actually being cut. We also know that deflation – declining prices carry with them a lot of costs in terms of businesses or households with debt and other decisions.

So really it's this balancing act of we want maximum employment, we want very low inflation – you know, closer to zero. If we go all the way to zero, that will make it harder to achieve this maximum employment. If we have inflation too high, that carries with it a lot of cost to society. I mean, I lived through the inflation of the '70s, and we know that harmed households and people in America a lot.

So this 2 percent was this, you know, kind of compromise or magic, you know, kind of point in the middle. It's not written in stone, but it does reflect, I think, a good, you know, trying to accomplish these two goals over time. So that would be my answer to that.

MS. CUMMING: A question here?

Q: Ron Schutz, Robins Kaplan.

John, I want you to put your economist hat on with the one hand and on the other hand. And what's the other-hand argument that interest rates are actually going to rise faster than you think they are? What would – what would people on the other side of that debate say?

MR. WILLIAMS: Well, I think I can – you know, I don't have to go to a different person. I'm very – (laughter) – my view is data-dependent, right? So if the data evolve and the economy evolves in a different way that I'm expecting – so what did I say, 2½ percent growth, I see the unemployment rate getting to about 3½ percent by early next year, and the economy with about 2 percent inflation. So that's kind of my baseline view.

Well, say that, you know, the economy just outperforms that – growth is much stronger, unemployment comes down more, and we really do see a big pickup in wage and price inflation, much higher than I expect. Then I think it just makes sense in that circumstance that we would need to adjust interest rates faster to stop some kind of, obviously, undesired significant rise in inflation. So that's one example I could see. But it would really be based on the economic – evolution of the economic outlook or a shift – a more fundamental shift in terms of where I see the economy going or where interest rates need to go in order to achieve this goal.

 

So I view the risks as being pretty balanced. So when I say – you know, I said that, you know, the center of the committee saw three to four rate increases total for this year – we've already done one of those – and a few more over the next few years, I mean, that's kind of a baseline. If the economy underperforms, we'll go slower. If the economy really does outperform this or inflation does pick up faster than we expect, then obviously we have to adjust to that. But it would really be not based on a shift in our strategy, just a, you know, response to changing circumstances.

MS. CUMMING: Next question. There we go. Thank you.

Q: You mentioned the appetite for safe assets world-wide, and I'm wondering what you include in the definition of safe assets.

MR. WILLIAMS: Yeah, so this has been an area of a lot of research over the last 15 or so years. You know, [former Federal Reserve Chairman] Ben Bernanke wrote a really famous paper, gave a speech on this global savings glut that I think was one of the earlier ones that pointed this out.

So I think, when we look at safe assets, basically these are the assets that global investors want in case of a negative economic, you know, event. So U.S. Treasurys.

The reason it matters for monetary policy is that reserves held by the Fed or at other central banks are a safe asset. They don't change in value. You know, they're very liquid. So it's really highly liquid, low-risk assets. And, importantly, assets that – (audio break, technical difficulties) –

Q: (In progress following audio break) – for the long term and the expected returns that shareholders should have.

MR. WILLIAMS: So I'll take the – I actually – I mean, you know, [Minneapolis Fed] President [Neel] Kashkari has heard me talk about R-star probably a few too many times. But I will say in the public this is something that I think has been underappreciated in a lot of businesses, in pension funds and these kind of long-run issues. I do know that **financial markets** have kind of caught onto this – bond markets, things like that. My concern is that a lot of corporate, you know, shareholder groups or corporate leadership is still thinking I got to hit this old mark for what my return on equities is, and that some – and, you know, those expectations have not shifted.

Because, remember, I'm talking about longer-run fundamentals. I'm not talking about monetary policy, easing interest rates or raising interest rates. I'm not talking about short-term things. I'm talking about things that last over decades. And the productivity growth slowdown, which is true in almost all the economies in the world; the demographics, which is true in, you know, most countries in the world, even more dramatic than the U.S. quite honestly; and this global demand for safe assets, if it continues – these are things that I think will be around for quite some time. So my answer to you is that you really need to be thinking through what's a realistic return on assets, what's a realistic, you know, cost of capital and things like that, which I think have changed.

Now, I get – you know, one thing I notice is in surveys of economists this view of what's a reasonable return on equities and reasonable return on other investment classes has been coming down. But that's definitely lagging. But, you know, the reason I kind of have part of my speech is a really a kind of get out there to business and leaders – business and other leaders to really think about these consequences.

MS. CUMMING: Another question? Yes. There we go.

Q: Hi. Joe Tessmer, U.S. Bank.

Wondering if you could speak for a second just to the interplay between changing bank liquidity regulations and the demand for safe assets, and the ultimate size of the Fed's balance sheet, and how do you think about evaluating what the – you know, what that terminal rate is as the balance sheet runs off, and when do you – when do you stop that runoff?

MR. WILLIAMS: (Laughs.) That's a good – a great bunch of questions. And obviously interrelated. So clearly one of the things coming out of the financial crisis is – one of the lessons is that banks, especially the largest banks, need to have liquidity. That means having on your balance sheet assets that you can even in a very stressed, very panic kind of driven situation sell into the market to have cash, basically. So, again, going back to the great question about what's a safe asset, this is the things that banks have to hold in the U.S. and other countries. It's reserves with the Fed. It's U.S. Treasurys. It's other similar instruments that are highly liquid and highly safe.

So there's no question that part of the reason that the demand – the global demand for safe assets is still very high is because of regulatory of the United States and other countries, which have told banks, "Hey, you need to hold a lot of safe assets." So that's part of the demand – part of the equation. I would say that, you know, this story about the demand for safe assets predates that, but it kind of comes out of the Asian financial crisis, the Russian default, and the euro crisis, and a lot of other things. So I would say that the regulatory kind of demands on liquidity provisioning are a part of this – a part of this. But I don't think it's a whole story, because I think it predates it.

In terms of the ultimate size of the Fed's balance sheet, we are shrinking the balance sheet. We're now, you know, a little over $4 trillion in our balance sheet. And we started this process last year. It's continuing this year, what I would call organically. Basically, we're just not reinvesting all the proceeds of our – you know, the principal payments from our holdings. My own view, and this hasn't been decided by the FOMC about exactly what our – size of our balance sheet will be, the ultimate size. But the drivers of this are pretty clear.

First of all, on the liability – it's going to be – it's going to be driven by the liability side of our balance sheet, not the asset side. So what are the liabilities of the Fed's balance sheet. Well, we currently have $1.6 trillion in currency outstanding, which is the Fed's liability. Great business model, by the way, if you can get into it. It's a zero-interest bearing perpetuity that you can invest in other things. So $1.6 trillion on currency. The U.S. Treasury has a bank account with us which they've – you know, they hold an account with us. That's a liability for the Fed. There's obviously the reserves that the banks want to hold for the liquidity reasons and for other reasons.

So the question that you think about is our balance sheet today is over $4 trillion. But if you look at currency, Treasury, and probably liquidity demand, you're probably all the way up to $2 trillion, or something like that. Anyway, so this compares to about $850 [billion to] $900 billion of our balance sheet before the crisis. So let me go forward in time. So we're currently a little over $4 trillion. As we shrink our balance on the asset side, as we stop reinvesting in this, we'll see the balance sheet shrink quite a bit over the next few years. And the question is, it won't – I mean, the point I'd like to make is it's not going to get as small as it was, $850 [billion to] $900 billion, because the currency and these other things have grown. The question that we don't know yet is how much kind of reserves do we think we – is efficient for the conduct of monetary policy?

So there's been some projections that have come out of the New York Fed based on some, you know, surveys of people in Wall Street. And the typical example would be currency is at 1.6 today – $1.6 trillion. It's going to continue to grow maybe 5 percent a year over the next, say, three years. There's other – these other parts are going to be bigger than they were in the past. And about two or three years from now, the balance sheet will get to about $3 trillion. And then we're going to start getting to that range of, is this about the right size for reserves, the size of the balance sheet, just for the conduct of monetary policy? Well, you know, that's kind of in the ballpark of around that, plus or minus.

Then, the balance sheet will start growing again, because currency will continue to grow. But this exact answer to your question – is it $3 trillion, is it, you know, 2-point – you know, 2¾, 3¼, something like that – is something that we're going to have to learn about as we go ahead in time and see, you know, what are the demand for the reserves. And also, for the FOMC to really decide exactly how we want to conduct monetary policy in the future, and what the right amount of reserves is. Two points I just want to make. It's going to be a lot smaller than it is today, but much larger than it was in the – in the past.

MS. CUMMINGS: I see questions over on this side? Oh, there's one back in there. Thank you.

Q: Thank you, Dr. Williams. Gunjan Kedia from U.S. Bank.

Could you comment on European monetary policy and the outlook for the euro?

MR. WILLIAMS: And the what? And the last part?

Q: Outlook for the euro.

MR. WILLIAMS: Oh. So I am old and wise enough not to comment about my colleagues' monetary policy – (laughter) – or the future of the euro. But I will comment on how I see things in Europe and my own impression of what's happening. First of all, Europe was – especially the countries in the eurozone were, you know, hard hit not only by the global financial crisis, which spilled, you know, across the globe, but also the euro crisis and all the political uncertainty about their banking sector and all those other issues.

So I think the big good news in Europe is it seems like they're getting – finally getting really good traction on growth. Things look a lot better in Europe. Their inflation numbers are still quite low, but seem to have both, you know, stabilized but also showing some signs of improvement. So I'm actually pretty positive about Europe. And I think that's consistent with what the [European Central Bank's] doing. They're continuing very stimulative monetary policy, both with very low negative interest rates and also their version of quantitative easing, which I think has helped get their economies back on track. They're gradually starting to pull back from how much stimulus they have. And down the road, they'll decide, you know, some point when it's appropriate, to cut back on stimulus.

But I do believe that under the leadership of President [Mario] Draghi that, you know, the ECB has taken really bold actions, very, you know, for a lot of us unconventional monetary-policy actions. And those have been very helpful. And I think that's – one of the signs of that is that the economy is getting better, and the euro has strengthened as a result of a stronger European economy over – you know, strengthened over time. And I think that's a positive. And I think it's actually been helpful for the global economy, obviously for all of us, to kind of get more – a little bit more synchronized. Back in the day, the U.S. was – a few years ago, the U.S. was the one economy that was actually recovering, the Fed was starting to raise interest rates while other economies were struggling and actually cutting interest rates. Well, today – except for Japan – I think the direction of economic growth and monetary policy is moving, you know, a little bit more to be aligned or more coherent. And I think that's going to be a – that is a positive for global growth.

MS. CUMMINGS: Next question.

Q: Hi. Bryce Doty at Sit Investments.

When [Fed Chairman Jerome] Powell testified in front of Congress in February, the head of the House Finance Services Committee, you know, started off criticizing the Fed's policy of paying interest on the $2 trillion of the bank's excess reserves that's been going up, you know, roughly with the rate of fed funds. And I'm sympathetic to the politicians concerned that it looks like, you know, they're incentivizing banks to hoard cash rather than lend, as well as it becoming increasingly costly. But I was really struck by his final comment where he said, you know, when Congress made the unusual – took the unusual step to allow the Fed to pay interest on reserves, it was not meant to be used as a tool to get the actual fed-funds rate to match the target. So is there – as Congress is kind of rolling back some of the postcrisis policies, if they – if they decide to go back to the way it was and say, you know, you can't pay interest on these excess reserves anymore, what kind of implications would that have for monetary policy?

MR. WILLIAMS: So I think it would have very negative effects on monetary policy. So we are using the fact that we pay interest on the reserves that banks hold on account with us to raise interest rates. I mean, the – as we've been raising the federal-funds target over the last few years, the way we've been implementing that is by raising the interest rate that we pay to banks for reserves. We've also been raising this overnight reverse repo rate that's the bottom of kind of a corridor there. The idea is with higher interest rates out there in the market, what we're willing to pay to counterparties, means that, you know, market interest rates move up. And that's been completely successful. Market interest rates have moved up, one for one, as we've increased interest rates over the last few years.

That's how we're operating monetary policy. It's been, I think, successful in terms of, you know, doing what we always wanted to do, which is basically change, you know, financial conditions to support our dual goals of maximum employment and price stability. So this has been operating very well. I would argue that it doesn't really cost the taxpayers money, because when we pay interest on reserves, on the opposite – those reserves are obviously matched by assets. They are – generally, you know, a lot of them are Treasury bills and bonds that we get the interest on from a taxpayer point of view. You know, in the end, the Fed, in this program of [quantitative easing] and having all these reserves, has been profiting, you know, somewhere between $70 [billion] and $100 billion a year, which we've been turning it over to the U.S. Treasury. So it's not costing the taxpayer money to have the large balance sheet.

If they took away the ability to pay interest on reserves, it would make it very difficult for us to raise interest rates, given the amount of assets we'd have in our portfolio, which would force us to take actions to be able to, you know, have the interest rate where we want it to be, which I think would be very disruptive in the short term. I also worry about something in the longer term is that, you know, in this world – I'm just going, you know, back to this point I was making earlier – in a world where normal interest rates are only like 2½ to 3 percent, I do think that the Fed, in trying to accomplish our goal of keeping America working and keeping inflation low and stable, is going to have to turn to quantitative easing or asset-purchase programs or other approach, unconventional policies. And for those to work and to be able to unwind those in an orderly, effective way, you need to have a tool of something like interest on reserves for that to be successful.

So I worry about it in two ways. If you took away our ability to pay interest on the reserves, I think it would be very disruptive in the short run, given that that's a critical tool for our policy. But the long run, I'm concerned about it would basically make it much more difficult for us to do the quantitative easing or policies like that when that next downturn happens. In my own view, this is again my personal view, is that quantitative easing, although not perfect and, you know, there's a lot of uncertainty about its effects, was a(n) important part of the monetary easing that we did during the crisis and recovery to help, you know, achieve our goals.

MS. CUMMINGS: So I think we're ready for the last question. And over there. Thank you.

Q: Terry Slye from Briggs and Morgan.

I think one of the big issues probably in a lot of Minnesota company boardrooms is the prospect of tariffs, retaliatory tariffs and the effect of trade wars. It's not really the Fed's wheelhouse, but could you comment on what preparations the Fed can make to deal with trade wars, and how adequate you think those responses could be?

MR. WILLIAMS: So, as you said, it's not a responsibility of the Federal Reserve. And I'll just make a plug for independence of the Fed. You know, we do have – I'm not an elected official, obviously. We have – we really value the fact that we have the independence to make our monetary-policy decisions on our own without, you know, direction from Congress or the administration, focused on our – I think, the long-run health of the U.S. economy.

And so I kind of work under the – you know, live in this fantasy world where if I don't comment on administration and congressional policy actions, they won't comment on the Fed. (Laughter.) That hasn't played out quite so well, but – (laughter) – I will be serious. I do worry quite a bit around the potential effects of a true trade war – not just small adjustments of tariffs here or there, or renegotiating agreements. Those we've lived through before and hopefully those can be resolved in a productive way.

But if you really thought about the U.S. economy today and about how reliant we all are – whether you're here, you know, in Minnesota, or whether you're in California, or Florida – wherever you are, we are so reliant on trade for the supply of our goods, the export markets for our agriculture, for so many of our products. And we're so integrated into the global economy that if we really saw a huge increase in tariffs or restrictions on trade, I think it would be very damaging to growth, very damaging to the productivity of our economy, and its long-term prospects.

And also, would obviously be inflationary. Let's not fool ourselves. If you put large tariffs or quotas on imports, it's just going to make U.S. goods – you know, the goods that we import from other countries much more expensive. And that shows up in the pocketbooks of American consumers. So, again, I'm not – I'm not going to get into the politics, but I think from the long-run perspective, you know, global economy with more free markets is better for us in the long run. And, you know, I think there are some real negative – potential negative consequences of a prolonged, significant trade war. So let's hope that does not happen.

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* Williams Sees Fed Raising Rates Less Than in Previous Expansions

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Economy

**Clarida, Bowman Affirm Commitment to Fed's Independence in Setting Rates; Potential top lieutenant, Richard Clarida, says stock-market volatility by itself shouldn't determine how the Fed makes rate-setting decisions**

By Nick Timiraos
901 words
15 May 2018
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WASHINGTON—Two of President Donald Trump's nominees to the Federal Reserve's board of governors Tuesday signaled a strong commitment to making policy decisions independently of the executive branch.

Richard Clarida, the economist tapped to serve as the central bank's No. 2 official, told lawmakers he had never been pressed by the president or other officials on how he would set interest rates.

"In no meeting, at no time, did I ever have any reason to question the independence of the Federal Reserve, absolutely not," Mr. Clarida told the Senate Banking Committee at his confirmation hearing.

Democratic lawmakers pressed Mr. Clarida and a second nominee, Kansas Bank Commissioner Michelle Bowman, to state they would resist political interference.

Mr. Trump criticized the Fed during his presidential campaign but hasn't publicly weighed in on the central bank's interest-rate increases since taking office.

Mr. Clarida, if confirmed by the Senate, would work closely with Fed Chairman Jerome Powell in shaping monetary and regulatory policy. But the hearing yielded few clues on the likely outcomes.

In response to questions, Mr. Clarida said **stock-market volatility** by itself shouldn't influence the Fed's rate-setting decisions.

He also said it would be important for Fed officials to consider a broader range of labor-market measures than just the unemployment rate, which at 3.9% suggests there is very little slack.

"The economy is changing," said Mr. Clarida. The 3.9% rate "is welcome, but behind that one number is a very, very complex picture." He said Fed officials consider other measures such as labor-force participation rates.

Historically low participation rates in recent years have suggested more potential slack in the labor market than the unemployment rate indicated.

Mr. Clarida is a Columbia University economist and adviser to Pacific Investment Management Co. He served in the Treasury Department during the George W. Bush administration. He is generally considered more of a pragmatist than an ideologue.

Former Fed Chairman Ben Bernanke and three other leading economic policy makers appointed by presidents from both parties endorsed Mr. Clarida's nomination in a letter to the top Republican and Democrat on the banking committee Monday.

Mr. Clarida defended the regulatory architecture designed after the 2008 financial crisis, including from the 2010 Dodd-Frank legislation. Republicans have generally supported efforts to roll back those rules, while Democrats in some cases have said regulation should be made tougher for big banks.

The issue is ripe because the Fed recently proposed retooling capital rules and its annual "stress tests" for the largest U.S. financial firms. The changes would reduce the possibility banks would fail the tests, which examine whether firms can continue lending during a severe recession.

The Fed has separately proposed loosening a rule governing capital standards that applies to eight large U.S. banks considered crucial to the functioning of the global financial system. Regulators have been more divided over that measure.

Mr. Clarida resisted efforts to say how he would have voted on the measures, saying he would need to study the details. He said it was important to ensure any changes preserved "the substantial gains" from regulation that had made the financial system more resilient and stable.

The exchange left Sen. Elizabeth Warren (D., Mass.) disappointed. She told him she was "concerned about your unwillingness" to provide more specificity.

Lawmakers focused other questions more on monetary-policy problems of the past decade than on those that officials could face in coming years.

Under questioning, Mr. Clarida said monetary policy might have contributed to the 2008 financial crisis; in the past he has said failures in regulation and bank supervision were primarily responsible.

The confirmations of Mr. Clarida and Ms. Bowman appeared on track after the hearing, though it could be several weeks or months before they would join the Fed board.

"If I had my way, we'd be moving [Mr. Clarida] next week, but again, we're facing a phenomenally difficult time moving nominees" on the Senate floor, said the banking committee chairman, Mike Crapo (R., Idaho), after the hearing.

Typically, nominees try not to make waves at confirmation hearings, and Tuesday's wasn't particularly adversarial. That wasn't the case in January, when another Fed board nominee—Carnegie Mellon University economist Marvin Goodfriend—left Democrats visibly frustrated with his answers to their questions.

Republicans have a 51-to-49 majority in the chamber and nominees are confirmed with a simple majority. The GOP's majority is delicate due to the absence of Sen. John McCain (R., Ariz.), who is being treated for brain cancer.

Mr. Goodfriend's nomination fell into doubt after Sen. Rand Paul (R., Ky.) said he would vote against it, citing his concerns over the economist's academic writing about tracking cash as it moves in and out of banks.

The banking committee approved Mr. Goodfriend on a party-line vote, but his nomination hasn't come up before the full Senate.

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THE WALL STREET JOURNAL.

Markets

**Metals: Gold Tumbles to 2018 Low on Higher Dollar; The dollar's strength, driven by robust April retail sales data, helps push gold to lowest point this year**

By Benjamin Parkin and David Hodari
642 words
15 May 2018
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The Wall Street Journal Online
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Gold prices fell to the lowest point this year as signs of a stronger economy pushed the U.S. dollar higher.

Front-month gold contracts for May delivery fell 2.1% to $1,288.90 a troy ounce at the Comex division of the New York Mercantile Exchange, the lowest close since December and the largest single-day drop since 2016. Prices for the precious metal have traded between around $1,300 to $1,360 for most of this year, before tumbling out of the bottom end of that range Tuesday.

"Gold has gotten hammered," said Blue Line Futures LLC, a Chicago-based commodities brokerage, in a note. "What had become an extremely constructive bottoming process over the last two weeks is now out the window."

A rally in the dollar, alongside higher Treasury yields, helped drive much of the selling. A stronger greenback makes commodities like gold more expensive for global buyers, while higher yields make the metal less attractive to some investors.

The WSJ Dollar Index, which tracks the U.S. currency against a basket of others, made a new high for the year, rising 0.6% to 86.91. Meanwhile, the yield on the 10-year U.S. Treasury note rose above 3.05%, a multiyear high.

Those moves were driven by data on Tuesday showing that the U.S. economy was gathering steam, overcoming some weakness from earlier in the year.

On the one hand, the Commerce Department said that Americans spent more in stores, online and at restaurants in April. Retail sales rebounded from a winter lull to rise almost 5% from a year earlier. Better consumption was expected to contribute to broader growth, economists said.

Separately, a survey of New York manufacturers by the Federal Reserve Bank of New York said business activity in May picked up more than expected, with indexes for prices paid and prices received both increasing.

That pressured the gold market by suggesting that inflation was quickening, said Tai Wong, head of metals at BMO Capital Markets. Though investors often turn to gold as a hedge against inflation, many were betting that rising prices could quicken the Federal Reserve's pace of interest-rate hikes. Federal Reserve Bank of Dallas President Robert Kaplan said on Tuesday morning that it was the "right thing" for the central bank proceed with raising rates.

The firmer dollar appeared to outweigh any lingering geopolitical jitters concerning Sino-American trade, Russia or the U.S. withdrawal from the Iran nuclear deal. Traders also largely overlooked an outbreak of violence and political tension in the Gaza Strip, said Commerzbank AG, despite a tendency to gravitate toward assets like gold at times of mounting instability.

Among current risk factors, there is nothing facing investors "in the order of magnitude of North Korea firing missiles over Japan like we saw last year," said Sergey Raevskiy, an analyst at SP Angel Corporate Finance LLP.

Chart patterns suggested to some traders that the gold market was headed lower yet, with prices falling below their 200-day moving average on Tuesday.

"There's just not a **bullish** event for the metal market," said Ira Epstein, a strategist at Linn & Associates LLC in Chicago.

Mr. Epstein suggested that gold prices could fall as low as $1,250 as market participants waited for an outcome to the much-touted U.S.-North Korea summit in June.

Copper prices also suffered under the weight of a higher dollar on Tuesday, with contracts for May falling 1.2% to $3.0425 a pound.

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THE WALL STREET JOURNAL.
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Heard on the Street
**CEO's Pay Too Often Doesn't Pay**

By Justin Lahart
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15 May 2018
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[Financial Analysis and Commentary]

If paying a chief executive more doesn't do anything for the company's **stock price**, why pay the CEO more?

Last year was another one when the relationship between CEO pay and **stock-market** performance was tenuous at best. American International Group's Brian Duperreault (whose 2017 compensation package included a sign-on bonus for taking the job in May) and Allergan's Brenton Saunders were among the best-paid CEOs in America, according to a Wall Street Journal analysis, yet their companies' share prices suffered. And the CEO pay packages of the five companies with the best-performing stocks were pretty average.

This isn't to say that the relationship between pay and stock performance was negative. Instead, on a scale where 1 is perfect correlation and minus 1 is perfectly inverse correlation, it was effectively zero. In English, that means there is no connection between executive pay and stock performance.

That is something of a statistical feat, given all the things that go into stock performance from one year to the next. And it fits with the academic literature, with some papers finding a positive relationship between pay and future returns, and others finding a negative one.

But CEOs who are paid more should be demonstrably better at delivering returns. And if top-paid CEOs aren't delivering that sort of edge, investors should question why CEO pay has risen about twice as much as median U.S. household income over the past 25 years.

There are, after all, other things that could be done with money.



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THE WALL STREET JOURNAL.
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**Energy Markets: Oil Prices Increase As Market Gets Tighter**

By David Hodari and Alison Sider
331 words
15 May 2018
The Wall Street Journal
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**Oil prices** rose Monday on more signs a tightening global oil market, despite the release of OPEC data that signaled robust production.

U.S. crude futures climbed 26 cents, or 0.37%, to $70.96 a barrel on the New York Mercantile Exchange. Brent, the global benchmark, rose $1.11, or 1.44%, to $78.23 a barrel on ICE Futures Europe.

The Organization of the Petroleum Countries said in its monthly report Monday that petroleum stockpiles in the developed world stand just nine million barrels above the five-year average -- a sign that the glut that weighed on the market for years is nearly gone. OPEC also boosted its forecast for demand this year while trimming its outlook for global oil production.

"The geopolitical tinderbox around the Middle East seems to be encouraging buyers, while global supply demand fundamental are staying 'strong enough' to keep the sellers at bay for now," analysts at TAC Energy said. "If the complex can break above the multiyear highs set last week, the charts suggest we could see another 5-10% of upside near term."

Still, OPEC also said its total crude output rose by 12,000 barrels a day in April, month-on-month, to average 31.9 million barrels a day.

The increase was mainly the result of higher crude production in Saudi Arabia -- the world's largest crude exporter and the de facto head of OPEC -- and Algeria, the report said.

Those data added to a healthy picture of global oil production as producers pounce on higher prices. The gap between global and U.S. **oil prices** widened as new figures showed that producers in the U.S. are ramping up quickly.

The number of rigs drilling for oil in the U.S. rose by 10 last week to 844 rigs, the highest in more than three years.



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THE WALL STREET JOURNAL.

Economy
**German Economy Loses Luster as Global Tensions Bite; The country's economy is highly reliant on international trade**

By Nina Adam
692 words
15 May 2018
10:40 AM
The Wall Street Journal Online
WSJO
English


FRANKFURT—Europe's largest economy cooled sharply in the first quarter amid a drop in government spending and weak exports—a sign that a stronger euro and global tensions are beginning to leave a mark on the German economy.

Germany's annualized growth rate slowed to 1.2% from 2.5% in the fourth quarter of last year, the Federal Statistical Office said Tuesday. This means that the German economy was growing more slowly than the U.S., which registered growth of 2.3% in the same period.

The data came amongst a mixed bag of a eurozone economic indicators confirming an overall slowdown at the start of the year that caused global

stocks to fluctuate as traders digested the news.

U.S. President Donald Trump's threat of imposing punitive tariffs on European steel and aluminum imports earlier this year has caused alarm across the bloc. The German economy especially is highly reliant on international trade and Berlin sent government officials scrambling to prevent the dispute escalating into a fully fledged trade war.

Mr. Trump's efforts to secure better trade terms for the U.S. have caused fears that the web of rules governing global commerce—and which Europe's largest economy has relied on for years—are being put into question by the U.S. president.

"The U.S. decision to back out of the nuclear treaty with Iran and fears of a further escalation of the international trade conflict with the U.S., as well as a further rise of crude **oil prices**, have had a negative impact on economic expectations in Germany," said Achim Wambach, president of the ZEW economic think tank.

A ZEW survey showed Tuesday that German economic expectations were unchanged at minus 8.2 points in May, the lowest level since Nov. 2012.

The eurozone as a whole grew at an annualized rate of 1.6% in the first quarter, down from 2.7% in the fourth quarter of last year, according to a revised set of data by the European Union statistics agency Tuesday.

Apart from Germany, economic activity also lost momentum in France, the Netherlands and Portugal.

In addition to a series of one-off factors, German economic growth was capped by a decline in exports and government consumption compared with the fourth quarter of last year.

The weak German exports in particular, were an early indication that the economy wasn't immune to global tensions and a stronger euro, economists said. The European currency has gained about 8% against the dollar in the past 12 months, eroding the competitiveness of eurozone goods and services.

Underlining Germany's vulnerability to external shocks, the last time international trade seized up, in the wake of the subprime crisis, its economy shrunk by some 5% in a year.

To be sure, the first-quarter slowdown was also explained by temporary factors, including a severe flu outbreak and a series of strikes in the metals and engineering sectors, the German economics ministry said.

The statistics office also reported a strong rise in investments, particularly in Germany's construction sector. Most private-sector economists expect economic activity to revive in the second quarter and beyond.

"The upswing remains intact," the economics ministry said.

Despite the sudden loss in momentum, "the German economy remains fundamentally strong," said Oliver Rakau, an economist at Oxford Economics. But it appears that it "has passed its growth peak for now," he added.

The same may apply to the eurozone, too. "Whether the recovery has the legs to last depends on the response of investment," the International Monetary Fund said in its economic outlook for Europe Tuesday. The IMF expects eurozone growth of 2.4% this year and 2.0% in 2019.

Write to Nina Adam at nina.adam@wsj.com

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WSJ PRO CENTRAL BANKING

Economy

**German Economy Loses Luster as Global Tensions Bite; The country's economy is highly reliant on international trade**

By Nina Adam
692 words
15 May 2018
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English


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THE WALL STREET JOURNAL.
U.S. EDITION

**Shale Drillers Spread Their Bets**

By Rebecca Elliott
810 words
15 May 2018
The Wall Street Journal
J
B1
English


Shale drillers are ramping up production in the U.S. as **oil prices** increase, moving beyond the West Texas oil field that became the country's drilling center.

From Oklahoma to North Dakota, companies are raising investment in oil fields that fell out of favor several years ago, as $70-a-barrel crude prices make fracking and horizontal drilling economical in more places again.

While the Permian Basin in Texas and New Mexico remains the fastest-growing shale spot, congested pipelines and shortages of labor and materials there are crimping profits, making other fields attractive alternatives.

EOG Resources Inc., a shale-sector leader, is active in the Permian but also in Colorado, North Dakota and Oklahoma. In Wyoming, it has built up larger lease holdings and expanded production over the past two years.

Chief Executive Bill Thomas recently touted the "diversified assets" of EOG's portfolio when discussing the company's blockbuster first quarter, in which production rose 15% and profit surged over 2,000% from a year earlier.

"Last year it was all about, 'How much can you put in the Permian?'" said Daniel Romero, an analyst with energy consulting firm Wood Mackenzie. "But now, a few months later, it's what else are you doing outside of the Permian?"

After **oil prices** declined sharply in 2014, shale drillers flocked to the Permian because it was the least expensive place in the U.S. to produce oil by fracking, thanks to existing infrastructure and oil-bearing rock stacked like a layer cake, which allowed for better yield per acre.

The oil-rig count there more than tripled over the past two years, according to oil-field services company Baker Hughes, which tracks rigs as a barometer of drilling activity. Output surged to roughly three million barrels of oil a day -- similar to the output of Kuwait -- from just shy of two million barrels in early 2016, according to the U.S. Energy Information Administration.

But rig counts have been rising elsewhere, too, as prices have gradually recovered. The number of oil rigs in several basins outside the Permian has more than doubled over the same period, according Baker Hughes. The areas include North Dakota's Bakken region, the Eagle Ford in South Texas and the Cana Woodford in Oklahoma, home to fields known as the Scoop and the Stack.

Drilling exclusively in Oklahoma is Alta Mesa Resources Inc., a company chaired by former Anadarko Petroleum Corp. CEO Jim Hackett, who went hunting for opportunities in shale with backing from New York investors.

Hal Chappelle, Alta Mesa's CEO, said the company, which has a working interest in more than 130,000 acres in the Stack formation, was drawn to Oklahoma in part because of lower leasing costs.

While top-tier land in the Permian's Delaware Basin sold for an average of more than $33,000 an acre last year, property in the Scoop and Stack cost roughly half as much, according to energy-data firms RS Energy Group and 1Derrick.

"The Permian was seeing an incredible amount of competition, and that was reflected in acreage prices," Mr. Chappelle said.

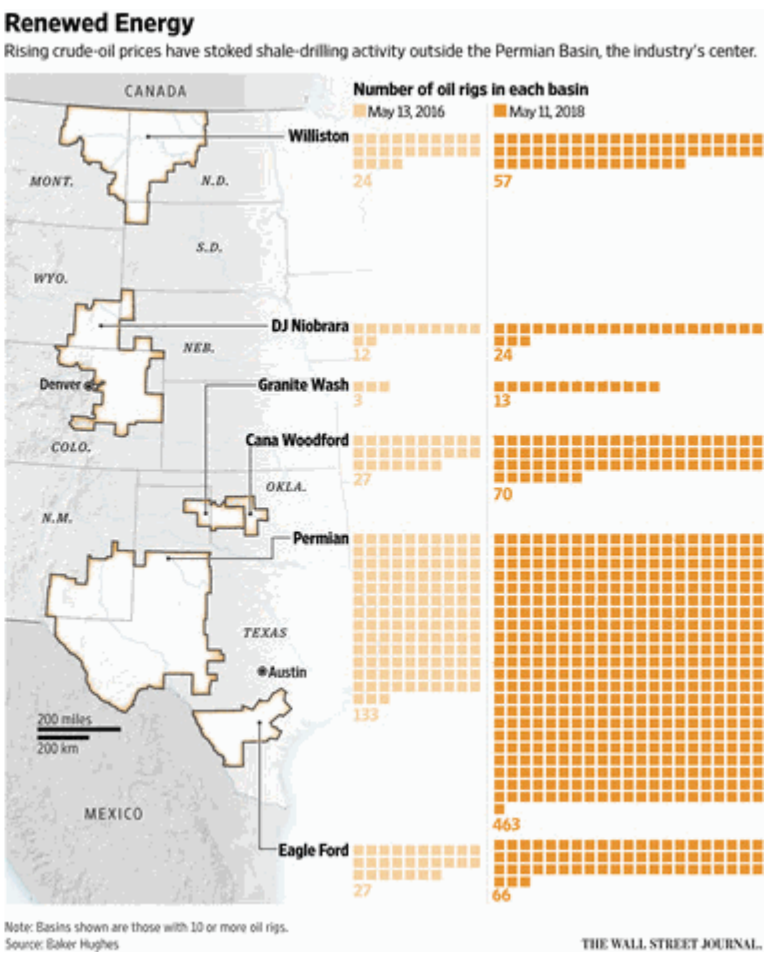
While the Permian has experienced explosive growth, pipeline construction hasn't kept pace, leading to bottlenecks that are making it difficult for some producers there to move their oil to market.

Oil in Midland, Texas -- where the local price of crude is set -- recently sold for $12 to $15 below the price of crude elsewhere in the U.S., according to Citi Research, part of Citigroup Inc. The discount reflects the added cost some face getting oil to refineries and export facilities out of the region using trucks and trains.

Some of the oil fields that are growing, notably the Bakken and Eagle Ford, had been popular among shale drillers and experienced their own bottleneck problems before prices started falling in 2014. After topping out at more than $100 a barrel in June 2014, oil prices plunged, falling below $30 in early 2016 before slowly recovering. The current prices above $70 are the highest in more than three years.

Continental Resources Inc., which is focused in North Dakota and Oklahoma, is benefiting from improved pipeline capacity in those areas. It sold crude produced in North Dakota at a discount to the main U.S. oil benchmark, West Texas Intermediate, of just $4.31 a barrel, executives told investors this month. In parts of Oklahoma, that figure was less than $2. Price differentials in the Bakken had become as wide as $28 a barrel six years ago, according to the EIA, as production outstripped pipeline capacity.

"We are having infrastructure catch up with development in North Dakota and in Oklahoma," said Blu Hulsey, the company's senior vice president of government and regulatory affairs.

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WSJ PRO CENTRAL BANKING

Economy
**Fed's Kaplan Still on Board With Fed Raising Rates; The Dallas Fed chief said the central bank is meeting its job and inflation goals**

By Michael S. Derby
389 words
15 May 2018
09:54 AM
WSJ Pro Central Banking
RSTPROCB
English


Federal Reserve Bank of Dallas President Robert Kaplan reiterated Tuesday his belief the U.S. central bank should press forward with rate rises, while adding he isn't ready to say how far the central bank should go this year.

The short-run outlook for the U.S. economy "looks pretty good" and when it comes to the Fed's job and inflation goals, "we are basically achieving both of our dual mandates," Mr. Kaplan said at an event at the Council on Foreign Relations in New York.

In such an environment, "the right thing" is to move forward with rate rises, he said.

Mr. Kaplan isn't currently a voting member of the interest rate setting Federal Open Market Committee. It last raised rates in March and officials generally expect to boost the cost of short-term borrowing two more times over the course of the year, amid solid job growth and a move in price pressures toward the Fed's 2% inflation target.

Mr. Kaplan reiterated his belief that rate rises should be "gradual and patient," and he said it was too soon to say if the Fed policy needs to be moved beyond a stance that is neutral in regards to its impact on the economy.

Speaking with reporters after his remarks, Mr. Kaplan declined to say how much he believes the Fed should increase rates this year, saying he would make his judgment on this matter later in the year.

In his remarks to the audience, Mr. Kaplan said he's looking for growth this year of 2.5% to 2.75% in part goosed higher by tax cuts and government spending increases, before moderating to a lower level next year.

When it comes to price pressures, "I think inflation is firming but I don't think it's running away from us," Mr. Kaplan said.

The official told reporters after his speech that he isn't worried about the rise in the 10-year note yield. The **10**-**year Treasury** has been moving steadily higher and was trading around 3.05% in Tuesday morning trading.

Write to Michael S. Derby at michael.derby@wsj.com

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**Trump's ZTE Deal Is No U.S. Win; Investors will likely celebrate easing trade tensions. But the weapons used are straight from the Chinese playbook**

By Nathaniel Taplin
508 words
15 May 2018
05:28 AM
The Wall Street Journal Online
WSJO
English


Qualcomm's deal plans and tariff-free U.S. pork in exchange for ZTE Corp.'s continued existence—that appears to be the upshot of U.S.-China trade talks.

Whether Chinese telecom leader ZTE willfully violated the terms of its settlement with the U.S. government over sales to sanctioned Iran now appears irrelevant—barely a month after the Trump administration banned American firms from dealing with the company.

Investors will likely celebrate easing trade tensions. But the weapons used to achieve these modest ends—a halt to Chinese agricultural-tariff threats and the green light for Qualcomm's NXP acquisition, in return for clemency on ZTE—are straight from the Chinese playbook. Beijing has long regarded

laws as tools to be applied when politically convenient, rather than impartial rules.

Now, the U.S. has weaponized Iran sanctions and a Cold War-era national-security law, the legal basis of President Donald Trump's steel and aluminum tariffs, for mercantilist ends—precisely the sort of arbitrary enforcement of law that infuriates Western businesses in China.

What does this mean for investors?

First, Beijing will see the U.S.'s obvious desire to water down agricultural tariffs ahead of the midterm elections as validating its strategy to go after Mr. Trump's political base, weakening the administration's hand in future negotiations. Extracting meaningful concessions that could help a broad range of businesses, instead of just a few, will become more difficult.

Second, other big trading nations and multinational companies watching the U.S. use national-security legislation and sanctions to resolve trade disputes may conclude that the rules-based international trade system is in permanent decline. Companies will intensify lobbying to protect themselves and new trade barriers will spring up. And global manufacturers may curtail investment in global supply chains—ultimately pushing up costs, and inflation.

Those might seem abstract considerations. Over the long run they can matter a lot. The long-term decline of inflation in advanced economies since the early 1980s has many causes, among them graying populations, the rise of automation and regulatory reforms. But the emergence of global supply chains was certainly a significant factor in the early 2000s, during the last big synchronized global growth uptick: U.S. goods imports from China in 2007, for example, were cheaper than in late 2003, according to the U.S. Bureau of Labor Statistics.

That price competition was painful for some developed nations' manufacturers and their workers, but it also helped keep prices for consumers cheap when **oil prices** were rocketing and real wage growth was moderating.

Global growth has finally shown signs of life over the past year. If the world economy keeps growing steadily—and global supply chains start to get Balkanized again—don't be surprised to see inflation return as well.

Write to Nathaniel Taplin at nathaniel.taplin@wsj.com

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Pro Private Markets
**Harbour Energy Working With ENN, Hony on Bid for Santos**

By Robb M. Stewart
398 words
15 May 2018
08:11 AM
WSJ Pro Private Equity
RSTPROPE
English


Private-equity backed oil and gas investor Harbour Energy Ltd. continues to edge toward a takeover deal for Santos Ltd., negotiating for the support of Chinese investors that collectively hold the single biggest stake in the Australian company.

In a statement to the Australian Securities Exchange on Tuesday, Harbour said it was working in concert with Chinese natural-gas distributor ENN Group Co. and private-equity firm Hony Capital and is seeking to agree on terms with the pair in order to put forward a final proposal to acquire Santos.

Last year, ENN and Hony raised their collective stake in Santos to 15.1% and agreed to act together as investors.

Santos, which has a market value of nearly $9.8 billion, is one of the largest independent oil-and-gas producers in the Asia-Pacific region, supplying homes and businesses. It owns vast oil-and-gas acreage in Australia and is a partner in two liquefied natural-gas ventures in Australia and another in Papua New Guinea.

In early April, Santos agreed to open its books after Harbour approached it with a fresh $10.37 billion takeover bid.

However, analysts have speculated the offer would have to be raised to reflect the rise in **oil prices** since the conditional offer of $4.98 a share was made. Santos also has continued to sell assets, including a portfolio of investments in Asia, as it chips away at debt that stood at $2.5 billion at the end of March.

Harbour, which was set up by EIG Global Energy Partners in 2014 to hunt for oil-and-gas assets outside the U.S., last year paid $3 billion to buy energy assets in the U.K.'s North Sea from Royal Dutch Shell PLC.

In April, Harbour said it had lined up equity for a Santos takeover bid from investors including commodities trader Mercuria and $7.75 billion in debt through J.P. Morgan and Morgan Stanley. The tentative offer comprised cash and a special dividend, though Harbour said it would also offer an option for Santos shareholders to accept unlisted shares in a new private company.

Harbour has plans to use Santos's core assets to expand in Australia and throughout Asia.

Write to Robb M. Stewart at robb.stewart@wsj.com

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THE WALL STREET JOURNAL.
U.S. EDITION

**Bond Gauge Signals Confidence in U.S. --- Yield spread between Treasurys, German bunds is largest in three decades**

By Daniel Kruger
825 words
15 May 2018
The Wall Street Journal
J
B12
English


The gap between the yields on 10-year U.S. Treasury notes and German government bonds reached its widest in almost three decades, a sign of investor confidence that growth remains steadier in the U.S. than Europe.

The yield on the benchmark **10**-**year Treasury**, which rises as **bond prices** fall, closed Monday at 2.995%, 2.385 percentage points above the 0.610% yield on the German bund. The gap last week hit 2.445 percentage points, its widest since April 1989.

This signal contrasts with others in the bond market, such as the narrowing gap between short- and long-term Treasury yields, known as a flattening yield curve, which investors often see as a warning of economic slowdown. Treasury yields and market-based measures of U.S. inflation expectations have both risen this year, while gains in the bund yield have been limited by recent softness in economic data.

Investors often study the two yields as barometers that influence borrowing costs for consumers and corporations in the U.S. and Europe. The gap between the two yields is also a key sign of foreign demand for U.S. debt, with ultralow and even negative rates in Europe increasing the appeal of Treasurys to foreign investors in recent years.

"That spread is probably anticipating the U.S. economy is going to grow stronger than the rest of the world, and Germany in particular," said Jack McIntyre, who manages global bond portfolios at Brandywine Global Investment Management.

The trend toward a wider spread could continue, some analysts said. Federal Reserve officials are signaling two more rate increases this year and three more in 2019, while the European Central Bank is still looking for a way to climb out of its negative interest-rate policy. Several estimate that Europe's economy and the ECB's easy-money policies are about three or four years behind the U.S. and the Fed in their respective cycles.

Now, with the Trump administration's $1.5 trillion tax cut expected to stimulate growth and push up borrowing needs, increasing the supply of new bonds, U.S. yields are rising. Investors will look to U.S. retail-sales data Tuesday for signs of whether the tax cuts are stimulating consumer activity, or whether any gains in purchasing power are being eroded by the recent rise in **oil prices**.

Even as the U.S. goes deeper into debt, Germany regularly runs a budget surplus, limiting the amount of debt it sells. That has helped hold down yields for Europe's benchmark issuer, with Monday's 0.610% yield on 10-year German government debt, according to Tradeweb, up from 0.424% at the end of last year.

German yields have been held down in part by concerns about the vitality of some long-struggling European economies, often referred to by investors as "the peripherals," including Italy, Portugal and Greece. ECB officials' ambition to raise interest rates is now being constrained by sluggish growth in Italy, which has fueled the rise of antiestablishment parties that disdain the unified currency.

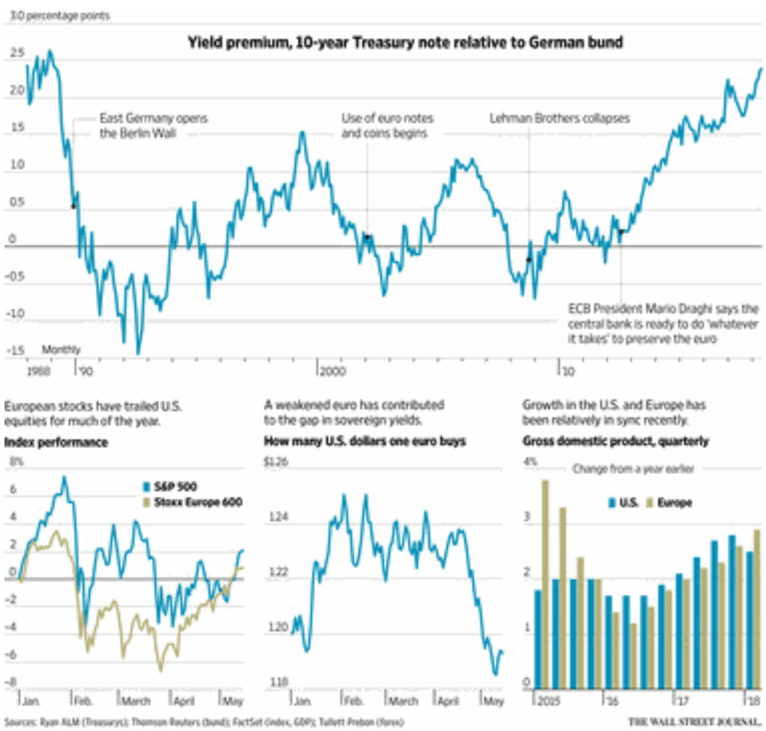
"You have the tale of two Europes -- that continues to be a challenge," said Mike Swell, co-manager of the Goldman Sachs Strategic Income Fund. He typically has trades that benefit from a widening spread between yields in the U.S. and Germany but said he had unwound them, because they could lose money if the U.S. dollar continues its recent gains against the euro.

Limited inflation growth in the U.S. and Europe could cap this year's climb in both Treasurys and the bund. U.S. consumer prices rose less than economists expected in April while the eurozone's annual inflation rate fell unexpectedly -- a setback for the ECB as it considers when to end its bond-buying stimulus program.

Inflation poses a threat to the value of government bonds because it erodes the purchasing power of their fixed-interest payments and can spur central banks to raise interest rates.

The widening gap between U.S. and German yields mirrors a rebound in the value of the dollar against the euro. Through Monday, the dollar has gained 4.8% versus the euro since Feb. 1, surprising many investors who had bet that the currency was locked in to a multiyear trend of losses against the euro because Europe was seen as nearer the start of a long expansion while the U.S. was perceived to be closer to the end of its recovery.

The rise in U.S. yields has made it more expensive for some investors to bet against the dollar, after its earlier weakness raised the costs for investors in Europe to buy Treasurys while also hedging the risks of further declines in the currency, some analysts said.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Business News: Pay, Performance Often at Odds --- Firms posting the best shareholder returns score in middle of pack in terms of CEO pay**

By Vanessa Fuhrmans
973 words
15 May 2018
The Wall Street Journal
J
B6
English


The best-paid CEOs don't necessarily run the best-performing companies.

Corporate boards have tried for years to tie chief executive compensation to the results they deliver. The better the company and its shareholders do, the more the top boss should be paid, or so the pay-for-performance mantra goes. In reality, CEO pay and performance often don't match up, and 2017 was no exception.

Among **S&P 500** CEOs who got raises last year, the 10% who received the biggest pay increases scored -- as a group -- in the middle of the pack in terms of total shareholder return, according to a Wall Street Journal analysis of data from MyLogIQ LLC and Institutional Shareholder Services.

Similarly, the 10% of companies posting the best total returns to shareholders scored in the middle of the pack in terms of CEO pay, the data show.

"Stars are often underpaid, while average performers are often overpaid," said Herman Aguinis, a professor of management at George Washington University School of Business.

One reason for the mismatch is that boards often set CEO pay by benchmarking the average compensation for leaders at a peer group of companies and setting performance targets accordingly, Mr. Aguinis said. That works if CEO performance doesn't vary too greatly from the average. But a study co-written by Mr. Aguinis and published last week in the journal Management Research found that, much like with professional athletes, there were vast differences in the performance of CEOs.

The disparity between chief executive compensation and performance appears to persist over longer periods, too, Mr. Aguinis said. In the study, researchers analyzed the earnings of more than 4,000 CEOs over the course of their tenures against several performance metrics. They found virtually no overlap between the top 1% of CEOs in terms of performance and the top 1% of highest earners. Among the top 10% of performers, only one-fifth were in the top 10% in terms of pay.

In 2017, only two out of the 20 highest-paid CEOs who didn't leave their jobs before the end of the year landed in the top 20 for shareholder return.

Robert Kotick of Activision Blizzard Inc., known for "Call of Duty," "World of Warcraft" and other videogames, made $28.7 million and posted a 76% return. Steve Wynn was paid $34.5 million, while Wynn Resorts Ltd. posted a 98% total return. Mr. Wynn stepped down as CEO in February after The Wall Street Journal reported sexual-misconduct allegations, which he has denied.

Many firms condition a big share of pay on three-year performance metrics that are only partially affected by a single bad year, compensation consultants say.

CBS Corp. paid its chief, Leslie Moonves, $69.3 million last year; total shareholder return was negative 6.2%. His pay was virtually unchanged from $69.6 million in 2016 when the broadcaster achieved a one-year return of 37%. Likewise, Comcast Corp. CEO Brian Roberts's annual pay has hovered around $33 million the past three years as annual shareholder returns ranged from 25% to negative 1.1%.

In its proxy, CBS said Mr. Moonves received $12 million more in 2017 stock awards than the prior year, in part because of his contract renewal. Comcast said in its filing that it prefers to base executive pay on longer-term business-management metrics, not total shareholder return.

Allergan PLC's Brent Saunders received a 700% raise in 2017 to $32.8 million, despite total shareholder return of negative 21%. The compensation package came during a year when Allergan ran into patent setbacks for one of its best sellers, dry-eye drug Restasis, which contributed to a 22% drop in the firm's share price for the year.

Part of the $8.8 million Mr. Saunders got in incentive payments stems from longer-term performance targets met since Allergan's 2014 acquisition of Forest Laboratories Inc., the company said in its proxy statement. Another portion of his 2017 compensation, $22.6 million in stock awards, won't vest until future years and is contingent on meeting specific research and shareholder-return goals. The drugmaker said in its proxy that because the award covers two years, it will report less compensation for Mr. Saunders for 2018 and 2019.

One of the biggest gaps between CEO pay and shareholder return was at aerospace-parts company TransDigm Group Inc. For much of the year, TransDigm's stock took a beating from short sellers who have criticized the its acquisition-driven business model, but the **volatility** had little effect on then-CEO Nicholas Howley's pay package.

Shares, including reinvested dividends, returned just shy of 5% for the fiscal year that ended Sept. 30, 2017, underperforming the broader **S&P 500 index** for the first time in a decade. During the same period, Mr. Howley earned $61 million, more than triple the $18.9 million he made in 2016.

The bulk of his compensation -- $51.2 million -- came from dividend-like payments on vested options, stemming from $46 in special cash dividends the company awarded shareholders during the fiscal year. TransDigm paid no dividends the previous fiscal year. Mr. Howley also received $9.8 million in stock options. His base salary was $7,000.

Mr. Howley stepped down in April after a 17-year run as CEO and remains TransDigm's executive chairman. The company declined to comment on his pay package but pointed out that its proxy statement shows the company's one-year return for the calendar, versus fiscal, year was 20% and that its longer-term returns dramatically outpace the broader market.




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THE WALL STREET JOURNAL.
U.S. EDITION

**Streetwise: Lies, Damn Lies and Inflation**

By James Mackintosh
930 words
15 May 2018
The Wall Street Journal
J
B1
English


Two central banks are responsible for two regions that over the past five years have had similar inflation, similar job creation and similar inflation targets. One, the U.S. Federal Reserve, has raised interest rates six times. The other, the European Central Bank, is expected to increase next year for the first time since its mistake in 2011.

Anyone familiar with the standard market narrative will push back: Inflation has been far lower in Europe and unemployment far higher, justifying the ECB's extraordinary monetary measures, including negative rates.

But the standard narrative isn't quite right. Measured on the same basis, prices have actually risen roughly by the same amount in both places. Unemployment is more complicated, but, likewise, has done basically the same thing.

So why are the central banks taking such radically different approaches? One answer is that with no inflation scare in either the U.S. or eurozone, headline numbers matter. And the headline numbers certainly look more hawkish from Washington: 3.9% unemployment, as many jobs available as job seekers and 2.5% consumer-price inflation. Eurozone unemployment is 8.5% and inflation sits at 1.2%, fitting the basic market narrative.

A more nuanced look, however, is illuminating. Over the past five years the eurozone actually created more jobs than the U.S. Both regions have roughly the same unemployment as at the peak of the dot-com bubble and the lowest since the 2008 financial crisis. But workforce contraction in the U.S. and expansion in Europe make unemployment numbers less useful than in the past as a measure of how tight the labor market is.

The base rate of unemployment is likely to be higher in the eurozone, thanks to less flexible job markets and language barriers, so that isn't necessarily a reason to keep money easy.

It is less well understood that the inflation figures have quite different meanings, thanks to different treatment of housing and, to a lesser extent, health care. The most dramatic difference is housing: In the U.S., shelter makes up one-third of the consumer-price index, because it includes an imputed rent for homeowners. In Europe, only actual rents are measured, at a weight of just 6% of the basket of goods and services underlying the price index.

Measure both using the European approach, and overall prices have risen by the same amount since 2011. It is true that using this measure -- known as the harmonized index of consumer prices, or HICP -- U.S. prices have risen faster since last summer. But that appears to be in large part due to energy, where the weak dollar has pushed **oil prices** up faster than in Europe. There aren't any detailed breakdowns available for U.S. HICP, which is still an experimental statistic, but the CPI excluding shelter, food and energy is the best equivalent to core eurozone inflation, and exactly the same at 1.2%.

Another indication of the importance of housing comes from the Cleveland Fed's median CPI, which takes the middle price rise from a ranking of the CPI components. It drops from 2.6% to 1.7% when imputed rents are excluded, although in recent months it, too, has accelerated.

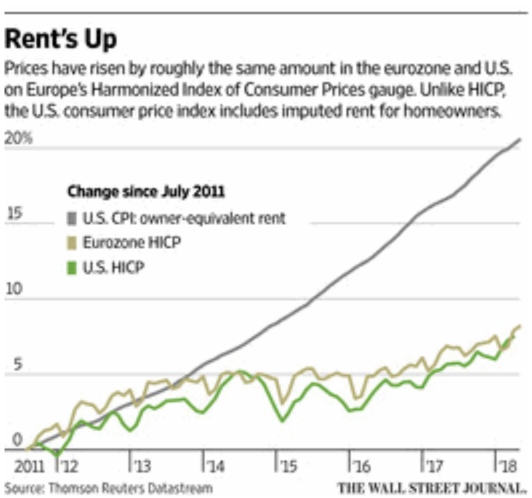
The Fed's preferred inflation gauge, the PCE price index, takes one-sixth of its weight from rent and imputed rent. The gap from CPI weights is made up mostly by including employers' health-care costs to get a health-care weight of one-fifth. In Europe, the equivalent health-care costs, mostly borne by government, are ignored in HICP, and booze and smokes are almost as important as health-care in determining inflation.

Statisticians have argued for years about how to include housing costs, and they keep changing their minds. The Swedish central bank switched its target last year to a different measure of inflation in order to exclude mortgage rates, while the British statistical agency last year started promoting a measure of inflation including imputed rents, with mixed success.

A second explanation for the different approaches is that investors and central banks are right to ignore all these statistical quirks. Actual U.S. rents have been rising twice as fast as in Europe, a sign of strong demand as well as less house building than before the crisis. While there is no comparable index including imputed rents, if there were it would probably show European inflation lagging behind the U.S. as a result. So even though on HICP inflation Europe and the U.S. look very similar, actual inflation might be quite a bit higher in the U.S.

A third explanation is that central banks got it right and their policy worked. Had the Fed held rates down inflation would have been higher, and had the ECB tightened policy the eurozone might be toying with deflation again. Attributing causation is the big challenge in economics, and in much of the world inflation hasn't been doing what economists expected, but there is surely something in this.

If this entire discussion left you confused, you are in good company. Central bankers, like all economists, form their views from statistics that often turn out to be wrong or misleading, half-truths about how the economy works and guesses as to how markets will respond. Understand that, and you are a long way to forming your own views -- and being appropriately humble about either your or the economists' chances of being right.

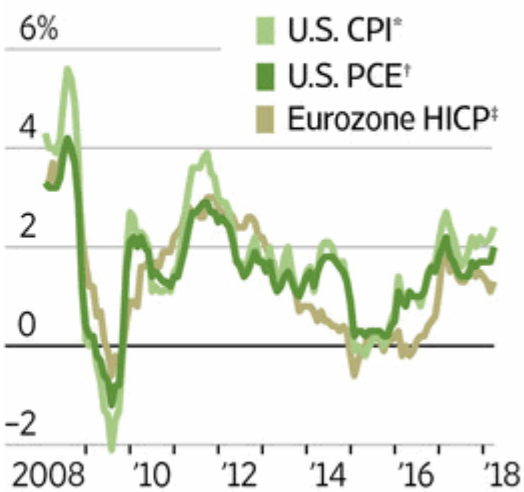


## Different Perspectives

Headline inflation measures are constructed in very different ways, with the U.S. putting much more weight on housing costs.

**12-month inflation rate**




*Consumer-price index
†Personal-consumption expenditures
‡Harmonized index of consumer prices
Source: Federal Reserve Bank of St. Louis

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WSJ PRO CENTRAL BANKING

Economy
**Derby's Take: Taking Stock Of The Message Of The Fed's Alternative Inflation Measures; The Dallas measure suggests it may take a little while longer before the central bank can reliably say it has hit its inflation target.**

By Michael S. Derby
428 words
15 May 2018
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English


There is a world familiar to many observers in which inflation has been on a long and slow slog back up to the Federal Reserve's 2% inflation target.

And there is another world--the world of alternative central-bank-produced inflation measures. In this realm, where two regional Fed banks seek to uncover the underlying state of price pressures, inflation has been a bit more steady.

Lately, as recent government data indicate the Fed may be hitting it inflation target sustainably, one of these alternative measures is suggesting the process may take a little longer.

The best known of these alternative measures are the Dallas Fed's Trimmed Mean PCE and the Cleveland Fed's Median CPI. The Dallas Fed's number works off data used to compile the Commerce Department's personal-consumption expenditures index. The Cleveland Fed's number is based on the Labor Department's consumer-price index data.

The "core" versions of the PCE price index and CPI toss out **volatile** food and energy items to get a read on underlying price pressures. But that has always been a hard pill to swallow for anyone who eats or drives, and it can leave those measures buffeted by periodic shocks that are hard to make sense of.

The regional Fed measures attempt to create a more sophisticated "core" reading. They toss out the items with the biggest price increases and declines in a given month without regard to their source.

Since October, the Trimmed Mean PCE index has risen steadily along with the conventional PCE measure. But while the PCE price index rose 2% in March from a year earlier, the Trimmed Mean was up 1.8%.

Meanwhile, the Cleveland Fed's Median CPI has been consistently stronger than the standard CPI over the last half year, even as both have shown consistent gains.

Fed officials don't set policy based on these alternative measures alone, but they do pay attention to them. The closeness of the Dallas number to the Fed's preferred inflation measure elevates it in importance over the Cleveland offering. And the Dallas measure suggests it may take a little while longer before the central bank can reliably say it has hit its inflation target.

Write to Michael S. Derby at michael.derby@wsj.com

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WSJ PRO CENTRAL BANKING

Economy

**Clarida Promises ‘Balanced Approach' to Policy | Bowman: Bank Rules Should Be Tailored | Fed Reports Show Rising Inflation Expectations | RBA: Low Rates Will Build Confidence | Derby's Take: Taking Stock Of The Message Of The Fed's Alternative Inflation Measures; The Wall Street Journal's central banking newsletter for Tuesday, May 15, 2018**

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15 May 2018
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Derby's Take: Taking Stock Of The Message Of The Fed's Alternative Inflation Measures

Fed Nominee Clarida Promises ‘Balanced Approach' to Monetary Policy

Fed Nominee Michelle Bowman Says Bank Rules Should Be Tailored for Size, Complexity

New Fed Reports Show Rising Inflation Expectations

Australia's RBA Says Period of Low Rates Will Build Confidence

Taking Stock Of The Message Of The Fed's Alternative Inflation Measures

There is a world familiar to many observers in which inflation has been on a long and slow slog back up to the Federal Reserve's 2% inflation target.

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Key Developments Around the World

Fed Nominee Clarida Promises 'Balanced Approach' to Monetary Policy

Richard Clarida, the Columbia University economist tapped to serve as the Federal Reserve's No. 2 official by President Donald Trump, said he would "fully support" the central bank's mission and its independent status. In prepared testimony released Monday by the Senate Banking Committee ahead of a hearing on his nomination Tuesday, Mr. Clarida said he would support interest-rate policy that takes a "balanced approach" to achieving the central bank's goals of stabilizing prices and maximizing sustainable employment. He also said he supports financial regulatory policies that are "effective, efficient and appropriately tailored" to provide a safe and sound financial system. Those policies should "preserve the far greater resiliency and stability of the financial system that has been achieved as a result of the significant reforms that have been put in place since the financial crisis," Mr. Clarida said. The hearing begins at 10 a.m. EDT.

Bernanke, Fischer Support Clarida Nomination for Fed Vice Chairman

Former Fed Chairman Ben Bernanke and three other former leading economic policy makers endorsed Richard Clarida's nomination to serve as the Fed's No. 2 official in a letter they sent Monday to lawmakers. Among the letter's signatories is Stanley Fischer, who held the job that Mr. Clarida would fill if confirmed by the Senate. Mr. Fischer, who was nominated for the post by President Barack Obama, resigned in October for personal reasons. Martin Feldstein, who served as chairman of the Council of Economic Advisers under President Ronald Reagan, and former Fed Vice Chairman Alan Blinder, who was picked for the Fed board by President Bill Clinton, also voiced their support in the letter.

Fed Nominee Michelle Bowman Says Bank Rules Should Be Tailored for Size, Complexity

Michelle Bowman, one of President Donald Trump's nominees to join the Fed board, planned to criticize postcrisis banking regulations at her Senate confirmation hearing Tuesday. Ms. Bowman, the Kansas state banking commissioner, also planned to express support for the Fed's "dual mandate" of fostering maximum employment and stable prices, according to her prepared testimony released Monday by the Senate Banking Committee. The hearing begins at 10 a.m. EDT.

Fed's Bullard: Cryptocurrencies Could Fragment How Things Are Paid For

St. Louis Fed President James Bullard warned Monday the proliferation of cryptocurrencies like bitcoin could create headaches for real-world users in the U.S. economy. Mr. Bullard said these privately issued currencies could take the model that now defines the international system, where countries trade with one another in myriad ever-shifting currencies, into the U.S. economy. Such a system could create complications for the buying and selling of goods and services.

New Fed Reports Show Rising Inflation Expectations

A pair of Fed reports released in the last several days should bolster officials' confidence that inflation will continue to rise. On Monday, the New York Fed reported hat the public sees price pressures accelerating in the next year and over the next three years. For both time horizons, the bank found expectations of a 3% inflation rate in April. That compares with expected 2.8% year-ahead inflation and 2.9% for three years ahead in the March survey. Meanwhile, on Thursday the Cleveland Fed reported that a model it uses to predict long-term inflation expectations is also moving higher. The bank said its latest estimate of the average inflation level expected over the next decade moved to 2.09%. That is up from 1.98% in April and is the highest reading in this series since January 2010.

Quick Hits

China's central bank vowed to keep liquidity steady, and Thailand's central bank is expected to stand pat on rates at its meeting this week. Here are quick hits on central banking and related market views from around the world.

Australia's RBA Says Period of Low Rates Will Build Confidence

Australia's central bank continues to signal interest rates will remain at record lows for some time, in the minutes of its latest policy meeting that keeping them low for now would help build stability and confidence. Minutes of the Reserve Bank of Australia's May 1 policy meeting released Tuesday showed policy makers still expect the next move in interest to be up, just not in the near-term.

RBA Deputy Governor Sees No Pressure to Raise Rates

 

Tuesday

8 a.m. EDT

Dallas Fed's Kaplan speaks

10 a.m. EDT

U.S. Senate Banking Committee holds confirmation hearing for Fed nominees Clarida and Bowman

1:10 p.m. EDT

San Francisco Fed's Williams speaks

Wednesday

8 a.m. EDT

ECB's Draghi speaks

8:30 a.m. EDT

Atlanta Fed's Bostic speaks

8:30 a.m. EDT

ECB's Coeuré speaks

9:15 a.m. EDT

Federal Reserve releases April U.S. industrial production

10:30 a.m. EDT

ECB's Praet speaks

12:15 p.m. EDT

Bank of Canada's Schembri speaks

6:30 p.m. EDT

St. Louis Fed's Bullard speaks

Low Risk As a Predictor of Financial Crises

Jon Danielsson, Marcela Valenzuela and Ilknur Zer explore the different early warning indicators of financial crises, finding that it would be beneficial for policy makers to use low **volatility** as a financial crisis indicator, according to a FEDS Notes. The post cites policy makers as holding a concerned view that low **volatility** may induce risk-taking. "A major cause of financial crises is excessive risk-taking by economic agents. When they perceive a low risk environment, they are endogenously incentivized to take more risk, which ultimately culminates in a crisis," the post states.

Lies, Damn Lies and Inflation

Consumer price index figures have different meanings in the U.S. and Europe, thanks to different treatment of housing and health care, writes James Mackintosh in The Wall Street Journal. "Measured on the same basis, prices have actually risen roughly the same amount in both places. Unemployment is more complicated, but, likewise, has done basically the same thing. So why are the central banks taking such radically different approaches? One answer is that with no inflation scare in either the U.S. or eurozone, headline numbers matter," Mr. Mackintosh says.

The U.S. and China are closing in on a deal that would give China's ZTE Corp. a reprieve from potentially crippling U.S. sanctions in exchange for Beijing removing tariffs on billions of dollars of U.S. agricultural products, said people in both countries briefed on the deal.

 

China's industrial activity picked up steam last month, though slowing consumption and infrastructure investment continue to cloud the outlook for growth.

Europe's largest economy cooled sharply in the first quarter due to high levels of illness and labor disputes, mirroring similar developments in the region and denting hopes for another year of stellar growth rates.

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

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

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The New York Times

Foreign Desk; SECTA
**About-Face on Trade With China Stings White House Hard-Liners**

By ANA SWANSON, MARK LANDLER and KEITH BRADSHER; Ana Swanson and Mark Landler reported from Washington, and Keith Bradsher from Taipei, Taiwan. Alan Rappeport contributed reporting from Washington, and Jane Perlez from Beijing. Ailin Tang contributed research.
1,642 words
15 May 2018
The New York Times
NYTF
Late Edition - Final
1
English


WASHINGTON -- President Trump's recent threat to impose tariffs on as much as $150 billion worth of Chinese goods appeared to be the first volley in what looked like a full-scale trade war with the nation's greatest economic adversary. Now, suddenly, Mr. Trump seems ready to make peace.

To alleviate trade tensions, Mr. Trump is considering easing up on a major Chinese telecommunications company, ZTE, in exchange for China agreeing to buy more American products and lifting its own crippling restrictions on American agriculture, people familiar with the deliberations said.

The shift is an abrupt reversal that reflects another twist in the pitched battle inside the White House between the economic nationalists, who channel Mr. Trump's protectionist instincts, and more mainstream advisers, who worry about the effects of hard-line policies on the **stock market** and long-term economic growth.

While the nationalists had recently seemed ascendant -- pushing Mr. Trump toward a showdown with the Chinese over steel exports and their co-opting of American technology -- a deal on ZTE, and potentially a range of other trade actions, would represent a victory for the mainstream contingent, led by Treasury Secretary Steven Mnuchin.

Mr. Mnuchin has taken the lead role in trying to head off potentially harmful tariffs and investment restrictions on China and has succeeded, at least for now, in persuading Mr. Trump to adopt a more conciliatory approach than the president's more hard-line advisers have advocated, according to people familiar with the deliberations.

An agreement on ZTE, which administration officials said could be struck with a visiting Chinese vice premier, Liu He, later this week, would remove a major source of tension between the United States and China at a sensitive moment: In just a few weeks, Mr. Trump is scheduled to meet the North Korean leader, Kim Jong-un, at a landmark summit meeting in Singapore.

Mr. Trump has made China's president, Xi Jinping, his partner on North Korea while at the same time condemning China's trade practices. On Monday, he framed the ZTE move as part of ''the larger trade deal we are negotiating with China and my personal relationship with President Xi.''

The president's reconsideration of sanctions imposed on ZTE stems in part from Beijing's demand that he consider lifting the penalties before the visit of Mr. Liu, Mr. Xi's senior economic adviser, who is arriving in Washington this week to try again to ease the friction. The Chinese made clear that Mr. Liu's visit was conditional on discussing the sanctions.

In a post on Twitter on Monday afternoon, Mr. Trump said lifting the restrictions on ZTE would benefit the United States because the company buys many of its components from American manufacturers. On Sunday, Mr. Trump left some people surprised after he tweeted that the administration needed to give ZTE a break because it was costing ''too many jobs in China.''

Mr. Mnuchin has tried to broker a relationship with the Chinese and pressed for a high-level delegation to travel to Beijing to try to resolve tensions this month. He has tried to focus the president on a deal that would reduce the United States' trade deficit with China, much to the chagrin of more nationalist advisers.

During their trip to Beijing early this month, the American delegation, which included top officials with divergent views, handed the Chinese a lengthy list of demands to radically change their trade practices and curtail the state's role in the economy.

The list, which included cutting their trade surplus with the United States by $200 billion, halting subsidies to advanced manufacturing and slashing their tariffs to the same level as the United States, took the Chinese by surprise, according to people familiar with the visit, and it appeared to further sour relations between the two economic giants.

The demands bore the imprint of Robert Lighthizer, the United States trade representative who is a longtime litigator on steel-dumping cases, and Peter Navarro, a trade adviser whose academic work has focused on the dire threat posed by China to American workers and companies.

The Chinese offered very little in return, several officials said. But Mr. Trump, rather than escalating the conflict, now appears to be seeking a quicker, easier resolution of the dispute. In addition to Mr. Mnuchin, Larry Kudlow, the head of the National Economic Council and a longtime free trade advocate, also favors striking some kind of deal, according to people familiar with his thinking.

''Secretary Mnuchin has been pushing for a more conciliatory view to China for this entire period, certainly since the launch of the 301 investigation,'' Derek Scissors, a resident scholar at the American Enterprise Institute, said, referring to the section of trade law that authorized an investigation into whether China had illegally obtained American intellectual property.

''We see evidence that the Treasury Department does not want to impose investment sanctions on China as required by the original 301 findings,'' Mr. Scissors added.

A senior Treasury Department official said Mr. Mnuchin has conferred with Mr. Trump and Wilbur Ross, the commerce secretary, about China's ZTE concerns. However, the official said a review of the Commerce Department action against ZTE was not a precondition for trade talks.

Among Mr. Trump's advisers, Mr. Mnuchin has been more encouraged by China's expressions of willingness to address the trade imbalance between the two countries. Because of his national security responsibilities, officials said, he also considers how trade tensions could affect the negotiation with North Korea over its nuclear program. China, as North Korea's neighbor and largest trading partner, will play an influential role in those talks.

The Trump administration threatened ZTE's existence as a business last month, when the Commerce Department ordered a seven-year halt in American shipments of computer microchips and software that are at the heart of most of ZTE's telecommunications gear.

The Commerce Department accused ZTE of violating American sanctions by selling to Iran and North Korea and then covering up the exports and rewarding the executives involved. ZTE acknowledged it violated sanctions, but blamed the actions on poor internal controls rather than a deliberate defiance of the American legal system.

ZTE, a 75,000-employee business that makes smartphones and cellphone tower equipment, began shutting down operations last week after it was unable to find alternative suppliers.

The move also hit one of the biggest American telecom companies, Qualcomm, which lost the ability to export semiconductors to ZTE, one of its biggest customers. In China, Qualcomm's plan to acquire NXP Semiconductors had been stalled by a prolonged antitrust review, which many saw as retaliation for America's trade moves.

In his surprise tweet on Sunday, Mr. Trump declared, ''President Xi of China, and I, are working together to give massive Chinese phone company, ZTE, a way to get back into business, fast. Too many jobs in China lost. Commerce Department has been instructed to get it done!''

The tweet provoked a swift and harsh response from Democratic and Republican lawmakers.

''I hope this isn't the beginning of backing down to China,'' Senator Marco Rubio, Republican of Florida, wrote Monday on Twitter. ''While Chinese companies have unrestricted access to U.S. market & protection of our laws many U.S. companies have been ruined after #China blocked market access or stole their intellectual property.''

Senator Chuck Schumer of New York, the Democratic leader, said in a statement, ''This leads to the greatest worry, which is that the president will back off on what China fears most -- a crackdown on intellectual property theft -- in exchange for buying some goods in the short run.''

 

On Monday, the White House denied that accommodating China's concerns represented a broken promise by Mr. Trump to protect America's interests, saying that the relationship with China was complex. ''He's been tough and he's confronted them,'' said Raj Shah, the deputy press secretary.

Mr. Ross said Monday that ZTE's fate should not be linked to the trade negotiations. ''ZTE did do some inappropriate things -- they admitted to them,'' he said in a speech. ''The question is, 'Are there alternative remedies to the one that we had originally put forward?'''

Mr. Trump's offer to throw ZTE a lifeline found a receptive audience in Beijing, where the company's travails have crystallized the fears of Chinese leaders that their country depends too much on American technology.

''We very much appreciate the positive attitude of the U.S. side to the issue of the ZTE Corporation, and are maintaining close communication with the U.S. on the implementation of specific details,'' Lu Kang, a spokesman for the Chinese Ministry of Foreign Affairs, said on Monday.

Hu Xijin, the chief editor of Global Times, a newspaper owned by the Chinese Communist Party, said on the social media service Weibo, ''No matter if the previous sanction was a card in Washington's concerted move for a trade war on China, the newest decision is a good one.''

Follow Ana Swanson, Mark Landler and Keith Bradsher on Twitter: @AnaSwanson, @MarkLandler and @KeithBradsher.

President Trump has signaled that he may ease up on the telecommunications company ZTE in return for concessions from China. (PHOTOGRAPH BY JOHANNES EISELE/AGENCE FRANCE-PRESSE -- GETTY IMAGES); Liu He, a Chinese vice premier, may be able to strike an agreement on ZTE, which could remove a major source of tension with the United States, during his visit to Washington this week. (PHOTOGRAPH BY DENIS BALIBOUSE/REUTERS) (A7)

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The New York Times
the New Health Care
The Upshot
**Medical Mystery: Something Happened to U.S. Health Spending After 1980**

By Austin Frakt
1,427 words
14 May 2018
05:00 AM
NYTimes.com Feed
NYTFEED
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The United States devotes a lot more of its economic resources to health care than any other nation, and yet its health care outcomes aren't better for it.

That hasn't always been the case. America was in the realm of other countries in per-capita health spending through about 1980. Then it diverged.

It's the same story with health spending as a fraction of gross domestic product. Likewise, life expectancy. In 1980, the U.S. was right in the middle of the pack of peer nations in life expectancy at birth. But by the mid-2000s, we were at the bottom of the pack.

What happened?

Health spending and life expectancy are not necessarily closely related, so it's helpful to consider them separately.

"Medical care is one of the less important determinants of life expectancy," said Joseph Newhouse, a health economist at Harvard. "Socioeconomic status and other social factors exert larger influences on longevity."

For spending, many experts point to differences in public policy on health care financing. "Other countries have been able to put limits on health care prices and spending" with government policies, said Paul Starr, professor of sociology and public affairs at Princeton. The United States has relied more on market forces, which have been less effective.

"Confronted with fiscal pressures, as the share of G.D.P. absorbed by health care spending began to get serious, other nations had mechanisms to hold down spending," said Henry Aaron, a health economist with the Brookings Institution. "We didn't."

One result: Prices for health care goods and services are much higher in the United States. Gerard Anderson, a professor at Johns Hopkins and a lead author of a Health Affairs study on the subject, emphasized this point. "The differential between what the U.S. and other industrialized countries pay for prescriptions and for hospital and physician services continues to widen over time," he said. Other studies also support this idea. However, by some measures, growth in the amount of health care consumed has also been a factor.

The degree of competition, or lack thereof, in the American health system plays a role. A recent study by economists at the University of Miami found that periods of rapid growth in U.S. health care spending coincide with rapid growth in markups of health care prices. This is what one would expect in markets with low levels of competition.

Although American health care markets are highly consolidated, which contributes to higher prices, there are also enough players to impose administrative drag. Rising administrative costs — like billing and price negotiations across many insurers — may also explain part of the problem.

The additional costs associated with many insurers, each requiring different billing documentation, adds inefficiency, according to the Harvard health economist David Cutler. According to a recent study, the United States has higher health care administrative costs than other wealthy countries.

“We have big pharma vs. big insurance vs. big hospital networks, and the patient and employers and also the government end up paying the bills,” said Janet Currie, a Princeton health economist. Though we have some large public health care programs, they are not able to keep a lid on prices. Medicare, for example, is forbidden to negotiate as a whole for drug prices, as Ms. Currie pointed out.

But none of this explains the timing of the spending divergence. Why did it start around 1980?

Mr. Starr suggests that the high inflation of the late 1970s contributed to growth in health care spending, which other countries had more systems in place to control. Likewise, Mr. Cutler points to related economic events before 1980 as contributing factors. The **oil price** shocks of the 1970s hurt economic growth, straining countries’ ability to afford health care. “Thus, all across the world, one sees constraints on payment, technology, etc., in the 1970s and 1980s,” he said. The United States is not different in kind, only degree; our constraints were weaker.

Later on, once those spending constraints eased, “suppliers of medical inputs marketed very costly technological innovations with gusto,” Mr. Aaron said. They “found ready customers in hospitals, medical practices and other entities eager to keep up with rivals in the medical arms race.”

The last third of the 20th century or so was a fertile time for expensive health care innovation. Sherry Glied, an economist and a dean at New York University, offered a few examples: “Coronary artery bypass grafting took off in the mid-to late 1970s. Later, we saw innovations like drug treatments for H.I.V. and premature babies.”

These are all highly valuable, but they came at very high prices. This willingness to pay more has in turn made the United States an attractive market for innovation in health care.

Yet being an engine for innovation doesn’t necessarily translate into better outcomes. Almost no matter how it’s measured, longevity in the United States has not kept pace with that of other nations. Again, the inflection point is around 1980. Why?

A study examining the period 1975 to 2005 by Ms. Glied and Peter Muennig, from Columbia, suggests that international differences in rates of smoking, obesity, traffic accidents and homicides cannot explain why Americans tend to die younger.

Some have speculated that slower American life expectancy improvements are a result of a more diverse population. But Ms. Glied and Mr. Muennig found that life expectancy growth has been higher in minority groups in the United States. Another study, published in JAMA, found that even accounting for motor vehicle traffic crashes, firearm-related injuries and drug poisonings, the United States has higher mortality rates than comparably wealthy countries.

The lack of universal health coverage and less safety net support for low-income populations could have something to do with it, Ms. Glied speculated. “The most efficient way to improve population health is to focus on those at the bottom,” she said. “But we don’t do as much for them as other countries.”

The effectiveness of focusing on low-income populations is evident from large expansions of public health insurance for pregnant women and children in the 1980s. There were large reductions in child mortality associated with these expansions. “Those reductions were much larger for poor children than for richer children,” Ms. Currie said.

A report by RAND shows that in 1980 the United States spent 11 percent of its G.D.P. on social programs, excluding health care, while members of the European Union spent an average of about 15 percent. In 2011 the gap had widened to 16 percent versus 22 percent.

Although this is a modest divergence over time, Mr. Anderson says it could be significant nonetheless. “Social underfunding probably has more long-term implications than underinvestment in medical care,” he said. For example, “if the underspending is on early childhood education — one of the key socioeconomic determinants of health — then there are long-term implications.”

Slow income growth could also play a role because poorer health is associated with lower incomes. “It’s notable that, apart from the richest of Americans, income growth stagnated starting in the late 1970s,” Mr. Cutler said.

Even if we can’t fully explain why the United States diverged in terms of health care spending and outcomes after 1980, one thing is clear: History demonstrates that it is possible for the U.S. health system to perform on par with other wealthy countries. That doesn’t mean it’s a simple matter to return to international parity. A lot has changed in 40 years. What began as small gaps in performance are now yawning chasms. And, to the extent greater

 

American health spending has spurred development of valuable health care technologies, we may not want to trade away all of our additional spending.

Nevertheless, Ashish Jha, a physician with the Harvard T.H. Chan School of Public Health and the director of the Harvard Global Health Institute, is hopeful: “For starters, we could have a lot more competition in health care. And government programs should often pay less than they do.” He added that if savings could be reaped from these approaches, and others — and reinvested in improving the welfare of lower-income Americans — we might close both the spending and longevity gaps.

President Carter wearing a cardigan sweater in 1977 to encourage setting thermostats lower to limit the country’s dependence on foreign oil. **Oil price** shocks strained many countries’ ability to afford health care. | Associated Press

Document NYTFEED020180514ee5e001mm

 

WSJ PRO CENTRAL BANKING

Economy
**New Fed Reports Show Rising Inflation Expectations; A New York Fed survey finds consumers see inflation at 3% for both one year and three years out**

By Michael S. Derby
514 words
14 May 2018
05:30 PM
WSJ Pro Central Banking
RSTPROCB
English


A pair of Federal Reserve reports released in the last several days should bolster officials' confidence that inflation will continue to rise.

On Monday, the Federal Reserve Bank of New York reported in its monthly Survey of Consumer Expectations that the public sees price pressures accelerating in the next year and over the next three years.

For both time horizons, the bank found expectations of a 3% inflation rate in April. That compares with expected 2.8% year-ahead inflation and 2.9% for three years ahead in the March survey. The New York Fed noted those are the highest readings since early 2017. The rise was described as broad-based among the survey's income and demographic groups.

Meanwhile, on Thursday the Cleveland Fed reported that a model it uses to predict long-term inflation expectations is also moving higher. The bank said its latest estimate of the average inflation level expected over the next decade moved to 2.09%. That is up from 1.98% in April and is the highest reading in this series since January 2010. The bank's estimate is derived from government data, surveys and market expectations.

Inflation expectations are important to the Fed. Central bankers believe where inflation is expected to go exerts a strong influence over where it is today.

The Fed has struggled to push low inflation up to its official 2% target for years. New signs of life on the expectations front may strengthen officials' belief that rising price pressures seen in recent data are for real.

The Fed's preferred price measure, the personal-consumption expenditures price index, hit 2% in March. But official Fed projections don't see a sustained increase until next year, when policy makers on balance see inflation overshooting their target at 2.1% for the year.

Recent vigor in inflation has driven some central bankers to say monetary policy could become more aggressive in the long term, especially considering strength in the job market along with tax cuts and government spending increases that could boost already robust economic activity.

"In order to maintain our policy goals, we may need to move the fed-funds rate, for a time, a bit above the level of the funds rate that is expected to prevail over the longer run," Federal Reserve Bank of Cleveland President Loretta Mester said in Paris on Monday.

Still, not all central bankers are on board with this outlook, in part because a strong job market hasn't led to robust wage growth. Meanwhile, St. Louis Fed President James Bullard bases part of his opposition to rate rises on the relatively low level of inflation expectations seen in **financial markets**.

While Fed officials look at market expectations, many policy makers consider them to be too **volatile** to put at the center of their thinking about future inflation pressures.

Write to Michael S. Derby at michael.derby@wsj.com

Document RSTPROCB20180514ee5e000xd

THE WALL STREET JOURNAL.

US

**Gas Is Headed for $3. What That Means for the U.S. Economy; Rising fuel costs could weigh on drivers, airlines and delivery companies**

By Stephanie Yang and Alison Sider
988 words
14 May 2018
05:14 PM
The Wall Street Journal Online
WSJO
English


Drivers gearing up for trips this summer face escalating prices at the gasoline pump, an early sign that $70-a-barrel oil is starting to reach into consumers' wallets.

Average U.S. retail gasoline prices are climbing toward $3 a gallon, the most expensive in more than three years. The national average was around $2.87 a gallon Monday. In states such as California and Washington, prices have already breached the $3 level after rising 24% and 17%, respectively, from a year ago.

Economic growth has boosted demand for oil. If that growth continues, most consumers should be able to afford to pay more to fill up their tanks. But conflicts in oil-producing regions could mean even higher gas prices, posing a threat to U.S. growth as the cost of fuel and gasoline weighs on drivers, airlines, delivery companies and other big consumers.

"Prices at the pump are quite high especially as we enter the driving season," said Gregory Daco, chief U.S. economist at Oxford Economics. "That's going to be one of the channels where you see a hit to people's disposable income and spending."

Rising fuel costs can also feed inflation and pressure interest rates. Even though the Federal Reserve typically looks past **volatile** energy prices in the short term, higher energy costs help shape consumer confidence. And with the central bank poised to be more active this year, rising energy costs pose an additional risk to the economy.

Morgan Stanley estimates that if gas averages $2.96 this year, it would take an annualized $38 billion from spending elsewhere, an upward revision from the bank's $20 billion estimate in January. That would wipe out about a third of the additional take-home pay coming from tax cuts this year, the analysts said.

When **oil prices** collapsed in 2014, gasoline prices followed. People took advantage, driving more than ever and buying larger, less fuel-efficient cars. At one point in 2016, prices tumbled toward $1 in parts of the country.

That era may be coming to an end.

As gasoline rose above $2.50 in November, Adam Mincey started to worry. His commute in North Carolina is about 60 miles round trip, and his old Chevrolet truck got about 8 miles to the gallon. Recently, he traded the truck in for a vehicle with better mileage.

"I make decent money—I'm a scientist. But it's cutting into our disposal income," he said.

The steadily rising fuel prices brought back bad memories: "There were times I couldn't fill up my tank in 2008 and 2009. I don't want that to happen again."

Some analysts are predicting another jolt to the market as President Donald Trump's decision to withdraw from the 2015 Iran nuclear deal could limit the country's crude exports.

The higher prices have taken some by surprise—the U.S. Energy Information Administration raised its forecast for summer gasoline prices to $2.90, up 17 cents from its expectation a month ago. That would be a nearly 50-cent jump from last summer.

But some economists say the growing importance of energy to the U.S. economy could blunt some of the impact from rising **oil prices**.

The country has become a more prominent supplier of crude oil and fuel. Domestic production has reached record weekly levels of 10.7 million barrels per day and a lot of it is being exported.

"People don't understand how we could double crude oil production" and see higher gas prices, said Tom Kloza, global head of energy analysis at the **Oil Price** Information Service. "The answer lies in the balance of payment. We are an exporting power right now."

Refiner Valero Energy Corp. said it wouldn't expect consumer demand to drop off until **oil prices** are at $80 to $100.

"Three dollars is like a small fence. You can get through it, you can get over it," said Patrick DeHaan, petroleum analyst at GasBuddy, a fuel-tracking app. "But $4 is like the electric fence in Jurassic Park. There's no getting over that."

Gas prices are still a long ways off from when they reached as high as $4.11 in 2008. And demand hit its highest levels ever last year even as prices rose.

"It's not only the price point, but it's how long that price point stays," Karl Fails, chief commercial officer at Sunoco LP, a wholesale fuel distributor, said during an earnings call Thursday. "We're very comfortable with the U.S. economy right now. And I think that will also have a bearing on any demand impacts."

Factors outside the U.S. are pushing **oil prices** higher. The Organization of the Petroleum Exporting Countries, along with other major oil producers including Russia, agreed in 2016 to curb output in the hopes of eliminating a global glut. Their efforts have been helped by a steep decline in production in Venezuela as the country has fallen into political and economic turmoil.

Airlines and shipping companies will also be paying more for jet fuel and diesel—costs that may be passed along to consumers. Even companies such as Whirlpool Corp. have noted that higher **oil prices** have boosted the cost of materials.

Robert Lozano, a car salesman in Los Angeles where some gas prices are already above $4, said the dealership's gas bill has climbed from about $9,000 to about $12,000 a month recently.

Customers are inquiring more about electric vehicles, he said.

"It's more in the consumer's mind as to what the most efficient vehicle is."

Write to Stephanie Yang at stephanie.yang@wsj.com and Alison Sider at alison.sider@wsj.com

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WSJ PRO FINANCIAL REGULATION

Economy
**Fed's Bullard: Cryptocurrencies Could Fragment How Things Are Paid For; St. Louis Fed chief says, 'Currencies have to be reliable and hold their value'**

By Michael S. Derby
389 words
14 May 2018
12:13 PM
WSJ Pro Financial Regulation
RSTPROFR
English


Federal Reserve Bank of St. Louis President James Bullard warned Monday the proliferation of cryptocurrencies like bitcoin could create headaches for real-world users in the U.S. economy.

Mr. Bullard said these privately issued currencies could take the model that now defines the international system, where countries trade with one another in myriad ever-shifting currencies, into the U.S. economy. Such a system could create complications for the buying and selling of goods and services.

"Currencies have to be reliable and hold their value," Mr. Bullard said at the CoinDesk Consensus conference in New York. "This is probably why government backing has been important historically, combined with a stable monetary policy that promotes stability of the currency."

In the current world of government-issued money, there are **volatile** exchange rates, and a system that commingles government money and cryptocurrencies "may have similar **volatility**."

"One suspects that consumers and businesses will not like a non-uniform currency in which many types of currency trade simultaneously at a variety of prices in a local market," Mr. Bullard said.

"The only reason this is not a bigger issue today is that the total volume of cryptocurrency trade is not that large in relation to the entire economy," he said.

Fed officials generally have been negative on cryptocurrencies. Officials like New York Fed leader William Dudley have said they are largely a speculative investment vehicle and not a real form of exchange. But cryptocurrency supporters see these new offerings as a way to subvert government control of the economy, while boosting privacy, among other advantages.

In his speech, Mr. Bullard said the dollar "is in great shape" and will likely stay that way given the economy's fundamentals and the Fed's stewardship of monetary policy.

To reporters, Mr. Bullard reiterated his belief that the U.S. economy is doing well, with low inflation and strong employment. He said the rate rises and balance-sheet reductions that the Fed already has made have done the necessary work to head off inflation pressures, and he repeated his opposition to more increases in borrowing costs.

Write to Michael S. Derby at michael.derby@wsj.com

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THE WALL STREET JOURNAL.

Business

**GreenSky Expects IPO to Price Between $21 and $23 a Share; At the midpoint of the range, the financial-technology firm would raise about $701.4 million**

By Allison Prang
330 words
14 May 2018
09:32 AM
The Wall Street Journal Online
WSJO
English


GreenSky Inc., a financial-technology firm that facilitates loans for businesses and other customers, expects its shares to price between $21 and $23 in its initial public offering.

Based on the midpoint of that range, the Atlanta company expects to raise about $701.4 million, it said Monday in a securities filing. GreenSky is offering about 34.1 million shares, or 39.2 million if underwriters fully exercise options.

The Wall Street Journal reported in April that the company had confidentially filed paperwork to go public. GreenSky has applied for its shares to trade under the symbol GSKY on the **Nasdaq**.

The company, which was founded in 2006, operates a lending platform that facilitates loans—which are made by various banks—for merchants as well as home-improvement store customers for as much as $55,000.

In the quarter ended March 31, the company brought in $85.3 million in revenue and reported a profit of $18.6 million. Revenue rose 31% from the same quarter the year before, but profit dropped 15% as costs rose 41%.

GreenSky will have a dual-class structure that gives the founders and some investors 10 votes a share, compared with one vote a share for investors buying shares in the public markets.

GreenSky Chief Executive David Zalik, who co-founded the company, would have about 49% voting control after the offering, or 48% if underwriters' options are exercised. Asset managers Pacific Investment Management Co. and TPG would remain large shareholders in GreenSky after the offering, the filing said.

Despite the large amount of financing that private investors have poured into lending startups, IPOs have been rare in recent years due in part to concerns around rising defaults among their borrowers and increased competition.

Write to Allison Prang at allison.prang@wsj.com

Document WSJO000020180514ee5e00234

THE WALL STREET JOURNAL.

Markets

**OPEC Output Rises on Higher Crude Production in Saudi Arabia; The group's total crude output rose by 12,000 barrels a day in April**

By Christopher Alessi
633 words
14 May 2018
06:55 AM
The Wall Street Journal Online
WSJO
English


OPEC said Monday its crude oil output ticked up slightly last month, while total global supply continued to grow largely due to robust U.S. shale production.

In its closely watched monthly oil market report, the Organization of the Petroleum Exporting Countries said the group's total crude output rose by 12,000 barrels a day in April, month-on-month, to average 31.9 million barrels a day. The increase was mainly the result of higher crude production in Saudi Arabia—the world's largest crude exporter and the de facto head of OPEC—and Algeria.

The report comes roughly six weeks ahead of OPEC's semiannual official meeting in Vienna, at which the cartel and partner producers are expected to assess a joint agreement to rebalance the oil market by cutting crude production.

OPEC and 10 producers outside the cartel, including Russia—currently the world's largest crude producer—have been holding back crude output by around 1.8 million barrels a day since the start of last year. The agreement, which was extended at the last OPEC meeting in November, is set to expire at the end of this year.

The deal has helped to soak up a global supply glut that has weighed on **oil prices** since late 2014. Crude prices climbed by more than 50% in the second half of last year, amid strong compliance with the OPEC-led agreement.

More recently, prices have been bolstered by President Donald Trump's decision to pull the U.S. out of a 2015 international agreement to curb Iran's nuclear program. The move is set to reimpose U.S. economic sanctions on Iran, hindering the oil output of the Islamic Republic—a major OPEC member—and reducing global supply. However, Saudi Arabia has already indicated it could ramp up its own production to make up for any supply loss from Iran.

Brent—the global benchmark—Friday closed down by 0.5%, to $77.12 a barrel, but still held on to a more than three-year high.

The world's total oil supply continued to accelerate in April, climbing by 120,000 barrels a day month-on-month, to average 97.89 million barrels a day, almost all of which was driven by non-OPEC production—including the U.S., the U.K., Brazil and China, OPEC said.

U.S. shale fracking continues to be one of the main engines of non-OPEC supply. Tight and shale formations are expected to average 5.76 million barrels a day, accounting for 94% of total U.S. petroleum supply in 2018, according to OPEC.

The oil-cartel expects non-OPEC supply in 2018 to grow by 1.7 million barrels year-over-year, nearly 90% of which should come from the U.S.

OPEC raised its global oil demand forecast for 2018 by 25,000 barrels a day, to increase by 1.65 million barrels a day and average 98.85 million barrels a day.

Commercial oil inventories in the Organization for Economic Cooperation and Development—a group of industrialized, oil-consuming nations that includes the U.S.—fell by 12.7 million barrels in March, to stand at 2.829 billion barrels, OPEC said. That is just 9 million barrels above the oil-cartel's target of the last five-year average.

Write to Christopher Alessi at christopher.alessi@wsj.com

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* Oil Holds Gains Amid U.S. Production Growth

* Trump's Iran Sanctions to Shake Up Global Oil Supply Lines

* OPEC, Russia Back Continued Oil Cuts, Drawing Trump Ire (April 20)

* What Happened to the Oil Glut? (April 12)

Document WSJO000020180514ee5e001ba

 

WSJ PRO CENTRAL BANKING

Economy

**Mester: Economic Outlook Supports More Rate Rises | Bullard Still Opposes Rate Rises | ECB Official: Approaching End of Asset Purchases | Malaysia to Ensure Orderly Financial Markets | Timiraos's Take: Confirmation Hearing Could Offer Clues About the Powell Fed; The Wall Street Journal's central banking newsletter for Monday, May 14, 2018**

2,250 words
14 May 2018
06:14 AM
WSJ Pro Central Banking
RSTPROCB
English


Timiraos's Take: Clarida's Confirmation Hearing Could Offer Clues About the Powell Fed

Fed's Mester Says Improved Economic Outlook Supports More Rate Rises

Fed's Bullard Upbeat on the Economy, but Still Opposes Further Rate Rises

ECB Approaching End of Net Asset Purchases, Says Bank of France Governor

Malaysia Central Bank: Will Continue to Ensure Orderly Financial Markets

Clarida's Confirmation Hearing Could Offer Clues About the Powell Fed

Members of the Senate Banking Committee have an opportunity to shed more light on the modus operandi of the Powell Fed when Richard Clarida testifies at his confirmation hearing on Tuesday.

President Donald Trump nominated Mr. Clarida last month to serve as the Fed's vice chairman, and the White House wanted someone in the job who could offer Fed Chairman Jerome Powell considerable monetary policy expertise.

A frequent commentator and scholar on monetary policy, Mr. Clarida brings an extensive paper trail to bear.

For example, he believes the financial crisis was a failure of supervision and regulation, and not fundamentally one of monetary policy.

He was early among commentators to note how interest rates were likely to remain lower for longer, even once they reached a neutral setting.

And he has written with some sympathy about the possibility of adopting a price-level target to replace the Fed's 2% inflation target.

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On fiscal policy, how does Mr. Clarida see the recent tax bill and federal spending increases boosting growth and influencing monetary policy?

How could a more combative trade policy, including tariffs, a stronger dollar, or an upturn in oil prices, reshape the Fed's forecasts around inflation and employment?

Should the Fed consider a price-level target now? And given the Fed's current commitment to a "symmetric" 2% inflation target, how does he define symmetry if or when inflation rises above 2%?

Barring a meltdown on Tuesday, Mr. Clarida seems poised to win confirmation. He is well regarded by economists on both sides of the aisle. If he is confirmed along the same timeline as Mr. Powell, he'd be in office to participate in the Fed's July 31-Aug.1 policy meeting.

Mr. Clarida's answers to these questions and others could provide more clarity about the Powell Fed because the chairman will rely on his top lieutenants—Mr. Clarida and incoming New York Fed President John Williams—to help shape monetary policy as the Fed enters a more delicate stage of the business cycle.

Key Developments Around the World

Fed's Mester Says Improved Economic Outlook Supports More Rate Rises

Federal Reserve Bank of Cleveland President Loretta Mester said Monday that a shifting outlook for the economy may mean the central bank has to raise rates more than she once expected. "With fiscal policy turning from restrictive to stimulative, the economy growing above trend, and investment rising, the short-term equilibrium interest rate is rising, too," Ms. Mester said in the text of a speech to be presented at an event in Paris. The possibility of a higher level of interest rates that is neither stimulative or restrictive of growth, the longer run outlook for monetary policy could shift, she said.

Fed's Bullard Upbeat on the Economy, but Still Opposes Further Rate Rises

St. Louis Fed President James Bullard on Friday continued to argue against further rate increases by the U.S. central bank. The Fed should be cautious as it contemplates moving forward with rate rises as the inflation situation, the job market and other factors suggest they aren't necessary, he said in a speech, Mo. "We could now describe the U.S. labor market as approximately being in equilibrium," Mr. Bullard said. "This is an appropriate situation that the Fed should not disturb" with further rate increases. With the jobless rate falling to levels not seen in decades and inflation rising, most other Fed officials see two or three more rate increases this year as likely. Mr. Bullard's belief that the Fed needn't raise rates further doesn't mean he is pessimistic about the outlook. "The economy is in very good shape today" and "you don't often see outcomes this good," Mr. Bullard told reporters after his remarks. But he added that "the monetary policy game is about trying to think a few moves ahead," and he believes more increases could create trouble.

WSJ Pro Transcripts: Read Bullard's media Q&A

Dallas Fed Video: President Kaplan on Cyclical vs. Secular Economic Trends

Watch Kaplan discuss how secular trends affect the economy.

Fed Promises Vote on Lifting Wells Asset Cap

Fed Chairman Jerome Powell says the central bank's governing board will vote on whether to remove a punitive cap on growth at Wells Fargo. The Fed planned to have staff make the decision about whether Wells had satisfied the Fed's demands, but Sen Elizabeth Warren (D, Mass.) had been pressing Powell for a vote and he agreed in a May 10 letter. He also told her the Fed will consider making public third-party reports on Wells' progress. The bank expects the cap to continue into 2019.--Dow Jones Newswires

U.S. Retreat From Trade Deals Poses a New Threat to Dollar

Trade friction is emerging as the latest threat to the U.S. dollar's position at the heart of the global financial system. For decades, central banks have held the bulk of their foreign-exchange reserves in the dollar, reflecting the dominant role the U.S. and its currency have played in global trade. As the U.S. pulls back from partnerships while countries like Mexico and Japan strike their own trade deals, the dollar's dominance could be undermined, investors and analysts said. That dominance has been referred to as an "exorbitant privilege," allowing the U.S. to borrow cheaply and run persistent deficits.

ECB's Draghi Says Eurozone Needs New Fiscal Tool to Fight Crises--Reuters

The eurozone needs a new, common "fiscal instrument" to hold its member countries together even when they come under attack in **financial markets**, European Central Bank President Mario Draghi said on Friday, Reuters reported. European Union leaders due to meet next month are expected to deliver incremental progress on some of the outstanding issues in the bloc, such a common backstop for providing cash to banks that are being wound down. Draghi backed that step and raised the game, calling for a government-backed tool designed to help weaker countries if they are being overly penalized by investors during a debt crisis.

ECB Approaching End of Net Asset Purchases, Says Bank of France Governor

The European Central Bank is approaching the end of its net asset purchases and will need to update its guidance on the timing of the first rate increase, Bank of France governor François Villeroy de Galhau said

 

Monday.Mr. Villeroy de Galhau said the ECB doesn't yet see the sustained adjustment in the inflation path that would be necessary for it to stop its €30 billion ($36 billion) of net asset purchases a month. But the governor of the Bank of France—who sits on the ECB governing council—said the current slowdown in inflation is "clearly temporary" and the central bank won't delay exiting quantitative easing to help states in the eurozone deal with their debt problems.

Malaysia Central Bank: Will Continue to Ensure Orderly **Financial Markets**

Malaysia's central bankwill continue to ensure orderly conditions in the onshore **financial markets** following the latest change in government, the first since Malaysia gained independence from Great Britain in 1957, its governor said Saturday. Malaysia's opposition coalition led by 92-year old Mahathir Mohamadpulled off a shock victory in Wednesday's election in what some analysts described as a surprising outcome on par with the likes of Brexit and U.S. President Donald Trump's election victory.

Monday

7:45 a.m. EDT

ECB's Praet speaks

9:40 a.m. EDT

St. Louis Fed's Bullard speaks

11 a.m. EDT

ECB's Lautenschläger speaks

12:15 p.m. EDT

ECB's Praet speaks

1:45 p.m. EDT

ECB's Coeuré speaks

Tuesday

8 a.m. EDT

Dallas Fed's Kaplan speaks

1:10 p.m. EDT

San Francisco Fed's Williams speaks

Inflation, Liquidity and Innovation

Inflation "affects the composition but not the overall quantity of investment," Michael Evers, Stefan Niemann and Marc Schiffbauer find in a World Bank Policy Research Working Paper. "A one percentage point increase in inflation reduces the establishment-level probability of innovation by 4.3 percent but does not affect total investment. Moreover, innovating firms display a stronger dependence on liquid assets, which, in turn, are negatively related to inflation," they write.

Economic Policy Uncertainty and Rate Hikes in Britain

Professor Costas Milas of the University of Liverpooltold The Guardian that uncertainty surrounding Brexit is likely helping to push the U.K.'s next interest rate increase further into the future. He pointed to data that compares economic policy uncertainty and GDP growth forecasts, stating it showed a "clear negative correlation." He said, "Unfortunately - current uncertainty has started picking up again. If this persists, August's Inflation Report will trim further the growth forecast which will of course delay even further a possible hike."

Why America's 3.9% Unemployment Rate is Bad News for Argentina

 

Countries like Argentina that borrow a lot of money overseas are in trouble when the U.S. economy leads to a stronger dollar, writes Matt O'Brien for The Washington Post's Wonkblog. Rising interest rates in the U.S. set off an economic fuse in Argentina in the last month, Mr. O'Brien penned. "Argentina is left with interest rates that are far too high for its economy to grow in any kind of way. It's a Catch-22: The only way to save its economy from a panic over the peso is to destroy it with punishingly high interest rates," he wrote.

Cryptocurrencies' Challenge to Central Banks

The sudden rise of cryptocurrencie have exposed inefficiencies in payments systems, in particular in cross-border transactions, and may contribute to redefining the concept of money as a means of payment, write Antonio Fatás and Beatrice Weder di Mauro. "The risks of introducing central bank digital currency are high while the efficiency gains do not seem large," they write. "Cryptocurrencies issued by central banks would suffer from all the disadvantages of cryptocurrencies without offering clear advantages. Digital money 'for all' on central banks' balance sheets could have disruptive effects on the financial system without offering strong advantages over a well governed two-tier system. A more efficient system can be achieved via innovation in current payment infrastructure that is encouraged by regulation which opens up competition to new players and technologies while maintaining the backbone of bank deposits and traditional central banks."

Emerging Markets Watch the Fed

Recent drops in emerging markets currencies demonstrate that while the Federal Reserve's influence on the policies of other central banks may have weakened, it remains significant, writes Daniel Moss for Bloomberg View. "Now the game for emerging markets is to look over their shoulders at big brother — which for now still means the Fed," he writes. "At some point, China will exert more influence than the U.S. on interest rates. We aren't there yet. Emerging markets still aren't masters of their own destiny. It may have just superficially appeared that way for a few blissful years. So much for "decoupling" and the retreat of the West."

The Trump administration's efforts to block imports are bringing back a long-forgotten headache for manufacturers: the quota. U.S. officials have so far largely relied on tariffs—essentially taxes at the border—in their efforts to reduce imports of steel, aluminum and Chinese goods. But some countries are accepting hard limits, or quotas, on their shipments as they strike deals with the Trump administration to avoid the tariffs.

American households remained relatively confident about the economy in early May. The University of Michigan said Friday its index of consumer sentiment was 98.8 in May, unchanged from April.

Canada unexpectedly shed jobs in April, while the unemployment rate remained unchanged at a decade-plus low and wage growth accelerated at its fastest pace in nearly six years.

Mexican industrial production was unchanged in March from February as gains in manufacturing offset declines in oil output, construction and utilities.

Fresh lending to housing investors in Australia slumped to a 5-year low in March, fanning fears of a widening credit crunch that could drive house prices down, and slow the economy.

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

Jon Hilsenrath; Katy Burne; 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

**Timiraos's Take: Clarida's Confirmation Hearing Could Offer Clues About the Powell Fed; What questions might lawmakers press that could reveal new clues about the Fed's potential policy path should Richard Clarida win confirmation?**

By Nick Timiraos
419 words
14 May 2018
05:51 AM
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English


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

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The New York Times

Business/Financial Desk; SECTB
# Bond Market Signals Doubt About Economic Goals

By MATT PHILLIPS
1,046 words
14 May 2018
The New York Times
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2
English


As a candidate, President Trump said he would increase United States economic growth to 4 percent annually -- and in one debate even added, "I think you can go to 5 percent or 6 percent."

Once he was in the White House, his administration revised those projections lower, saying its approach "means sustained 3 percent economic growth."

After the economy grew by 2.3 percent in 2017, investors in some of the world's largest markets are betting that the United States will continue to fall short of the White House goal.

The Federal Reserve has started raising short-term interest rates to reflect the economy's recovery, but longer-term rates -- over which the Fed traditionally has far less influence -- have not moved nearly as much. To many in the bond markets, that suggests investors think little has changed about long-term growth prospects.

"They're not expecting growth to move up to 3 percent on a sustained basis," said Julia Coronado, president of Macropolicy Perspectives, an economic consulting firm. "They're not looking for inflation to break out in any meaningful way on a sustained basis. It's not ominous. But it does sort of confirm that investors are still seeing the world in that way."

That does not mean the United States is about to enter a recession. By most measures, the economy is in fairly good shape as the current expansion -- the second-longest on record -- stretches into its ninth year. At 3.9 percent, unemployment hasn't been this low since 2000. Corporate profits are strong. Manufacturing activity has picked up.

But with rates in Fed-sensitive short-term government bond markets rising while longer-term rates are relatively flat, the gap between them has narrowed. And the plotting of those data points, known as the yield curve, occupies an outsize space in the minds of those who consider the markets a crucial barometer of economic health.

The gap between short-term and long-term rates tends to shrink -- a phenomenon known as flattening -- whenever the Federal Reserve begins lifting interest rates, which the Fed started doing in December 2015. Over the last year, the gap between interest rates on 10-year and two-year Treasuries flattened from more than 1 percentage point to less than half a percentage point, its lowest point in more than a decade.

But as the yield curve flattens, long-term interest rates run the risk of falling below short-term rates, a phenomenon known as an inverted yield curve. And when the yield curve inverts, as it did most recently in 2006-7, it amounts to an economic warning from the **financial markets** to watch out: Recession is on the way.

"We're not there yet, but we're getting progressively closer," said Steven Abrahams, head of investment strategy at the broker dealer Amherst Pierpont. "And I think we will get closer, faster than the market currently anticipates."

In a speech last month, the San Francisco Federal Reserve president, John Williams, described an inverted yield curve as "a powerful signal of recessions."

In part, that's because the yield curve is more than just an economic indicator. It actually helps determine decisions that are crucial to the health of the American economy. That's because a flattening yield curve makes banking -- basically the business of borrowing money at low short-term rates, and lending it at higher long-term rates -- less profitable. If the yield curve inverts, it effectively slams the doors on lending. And because debt is the fuel that drives the economy's engine, a recession often follows.

Mr. Williams emphasizes that he does not see an inverted yield curve, or recession, coming any time soon. And most economists agree. Over the next few years, private forecasters see United States economic growth peaking at 2.8 percent in 2018 before slowing to 2.5 percent in 2019 and 1.9 percent in 2020, according to Bloomberg data. That's a bit faster than the 2.2 percent growth rate of the United States economy since 2012.

But it's basically the same as the 2.6 percent average growth rate since 1980, suggesting that the $1.5 trillion tax overhaul signed into law by Mr. Trump in December is expected to have a negligible effect on long-term economic growth. Doing better would depend on increasing the supply of workers and raising productivity, a poorly understood process generally thought to depend on making large-scale investments in things like education, infrastructure and expensive equipment for companies.

Not everyone agrees that the bond market is sending a warning sign. For much of the last decade, the Federal Reserve and other central banks have been buying government bonds with the aim of pushing interest rates lower to support economic growth.

So the relatively low long-term rates partly reflect the large bond holdings of central banks, said Matthew Luzzetti, a senior economist at Deutsche Bank. That means those low rates contain ''much less of a signal about negative growth in the future,'' Mr. Luzzetti said.

But some view the flattening of the yield as a sign that the economy is weaker than it might appear.

Hoisington Investment Management, a bond investment firm based in Austin, Tex., has long held the view that long-term interest rates will go lower. Its chief economist, Lacy Hunt, ticked off a list of current trouble spots: slowing auto sales, skimpy inflation-adjusted wage growth, low savings rates and sluggish construction.

''There are signs out there, they don't receive much attention,'' said Mr. Hunt, whose firm manages more than $4 billion for insurance companies, nonprofit organizations and pension plans. ''But the flattening of the yield curve is an indication that there is a body of people that do think the future outlook is not nearly as good as the current conditions.''

The Federal Reserve Bank of New York. Fed policymakers have less control over longterm interest rates. (PHOTOGRAPH BY BRENDAN MCDERMID/REUTERS) CHART: Converging Yield Curve: When longer-term interest rates fall below short-term rates, investors may be signaling a lack of confidence in future growth. The phenomenon often precedes a recession. (Source: Thomson Reuters)

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THE WALL STREET JOURNAL.
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**OPEC Faces Test After Squeeze on Iran**

By Georgi Kantchev
959 words
12 May 2018
The Wall Street Journal
J
B11
English


President Donald Trump's decision to withdraw from the Iran nuclear deal could pile pressure on OPEC's pact to limit production and upset the delicate balance among its disparate signatories, analysts say.

Oil prices hit 3 1/2-year highs this past week amid expectations that renewed U.S. economic sanctions will squeeze Iran's oil supply and escalate regional tensions that have the potential to further limit the flow of crude.

But the oil price had already been gaining thanks to a 2016 deal between members of the Organization of the Petroleum Exporting Countries and other big producers like Russia, which have reduced global oil supply by 2%.

The group is set to meet in June to decide whether they will extend the deal beyond this year. If U.S. sanctions take Iranian oil off the market, leading to further price gains, some signatories may conclude that it is mission accomplished for a pact whose purpose was to drain the oil glut and boost prices, analysts say.

Some countries, like Russia and Kazakhstan, are itching to open the taps and take market share, while others, such as Saudi Arabia, want to keep an agreement that has so far led to higher oil prices. Saudi Arabia has already said it would stand in to replace lost oil from Iran, a task other nations will want to share.

Mr. Trump's move has ramped up geopolitical tensions in a grouping already at odds. On Friday, Iranian Oil Minister Bijan Zanganeh said his country wants oil prices at around $60 a barrel and that some in OPEC are working for U.S. interests given that higher prices benefit shale production.

If the agreement is scrapped and producers go back to pumping at full tilt, that will flood the market and sink prices again, analysts say.

"OPEC may need to adjust the production limits, but it won't be an easy decision as the Saudis want higher prices," said Hasan Qabazard, former director of OPEC's research division who is going to the June meeting. "Everything is on the table."

On Friday, oil for June delivery fell 0.9%, to $70.70 a barrel, on the New York Mercantile Exchange. Brent crude for July delivery, the global benchmark, dropped 0.5%, to $77.12, on ICE Futures Europe.

To be sure, some analysts believe Iran's troubles could also present OPEC and its allies with an opportunity to strengthen the pact. Saudi Arabia has already indicated it seeks to continue the cooperation beyond the current agreement.

To make up for Iran's lost oil, OPEC could relax the deal's restrictions, which would satisfy some of the members, like Iraq or Kazakhstan, that are chafing under the cuts, said Ellen Wald, nonresident scholar at the Washington-based Arabia Foundation.

"This would help strengthen their commitment to each other and to the group," Ms. Wald said. "This is a real opportunity to . . . make the group a permanent market institution and they don't want to let this opportunity go.

It isn't clear how much Iranian output will be taken off the market. Some analysts say the impact of renewed U.S. sanctions, which aren't supported by Europe's biggest economies, will be negligible while others predict that more than 700,000 barrels a day of crude could be affected. Previous sanctions by the West against Tehran in 2012 took about one million barrels a day of Iranian oil off the market.

Two OPEC officials said the Iran issue won't need to be discussed in June but could come up at the next meeting before year-end. "For now, all[OPEC has] to do is a verbal promise that producers will fill in the gap when needed. By end of this year, we may not have the same deal in place for 2019," said an OPEC official from a Persian Gulf oil-producing country.

Economists say that expensive crude, which is up more than 50% since last year, could reduce demand and even give incentive to some consumers to switch to renewable energy sources. Meanwhile, higher prices provide a boost to U.S. shale drillers, chipping away at the market share of OPEC, Russia and its allies.

Now, the resumption of U.S. sanctions on Iran adds a geopolitical twist to the oil flow.

"The [OPEC] deal began as a supply-and-demand agreement and it was already hard to forge consensus. When you throw politics into the mix, it makes things much more complicated," said Olivier Jakob, managing director of Swiss-based oil research firm Petromatrix. "We could be coming to the end of the true supply control agreement."

Saudi Arabia wants to push **oil prices** up above $80 a barrel this year, as it seeks to raise revenue and prepare for the initial public offering of Saudi Arabian Oil Co., or Aramco, the state-owned energy company.

Iran and other OPEC members are concerned that the biggest beneficiaries of high prices are U.S. shale producers.

"Some OPEC members [are] playing into U.S. hands" by supporting Washington's decision to pull out from the nuclear pact, Mr. Zanganeh, the Iranian oil minister, said in a tweet sent by his ministry.

Russian oil companies, meanwhile, have been itching to raise output after delaying long-planned projects due to the agreement with OPEC.

"The Russians have been wanting to produce for a long time. Now, they could view the Iran issue as an excuse to end or push to relax the deal," said Tamas Varga, an analyst at brokerage PVM Oil Associates.

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Summer Said and Benoit Faucon contributed to this article.

 


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THE WALL STREET JOURNAL.
U.S. EDITION

**Metals Swings Hurt Hedgers**

By Amrith Ramkumar
416 words
12 May 2018
The Wall Street Journal
J
B11
English


**Volatility** in the aluminum market from geopolitical uncertainty is roiling investors who hedge their positions to lock in prices -- a development that could cause more turbulence.

Prices swung wildly after the U.S. sanctioned Russian aluminum giant United Co. Rusal, the world's second-largest supplier. About two weeks later, the U.S. hinted it might relieve the measures if Rusal majority owner Oleg Deripaska sold his stake, which he agreed to do.

Many metal producers use futures and options to manage their risks in the physical market and guarantee prices for their output.

Before the Russia announcement, aluminum futures contracts for future months and years had been more expensive than current prices. The reports prompted some producers to try to sell longer-dated contracts on fears that prices would drop immediately from a rapid run-up.

But that condition, known as contango, flipped drastically as traders sold longer-dated positions, pushing down those prices and making near-term prices more expensive.

Although some producers would likely benefit from those conditions, since they would get more for their output in the near term, traders said the rapid price shifts and one-sided positioning likely limited gains. Aluminum stayed above $2,700 a metric ton for a matter of minutes on April 19 before closing at $2,485. Traders said hedgers often struggled to find a counterparty to buy much longer-dated positions given the uncertainty in the market.

"Most people weren't trading unless they needed to because the moves were unpredictable and extraordinary," said Tai Wong, head of metals trading at BMO Capital Markets. "People who benefited from a higher price got some hedges off, but not nearly the amount and not nearly as thoroughly as they would have wanted to."

Abrupt price moves in the industrial-metals market returned this past week as traders and investors anticipated President Donald Trump's decision to withdraw the U.S. from a nuclear deal with Iran.

Some analysts said consumers of metals, such as manufacturing companies hoping to neutralize swings, have also been buying futures contracts, adding to the market gyrations that are currently playing out.

Metals users have also chosen to load up on physical metal rather than using futures. They are worried about having enough aluminum to continue building products for their businesses.

That strategy has led to sizable swings in stockpiles around the world, which has stoked further **volatility**.

## Bumpy Ride

Aluminum prices have moved in both directions in recent sessions, making it more difficult for producers to lock in prices.


Note: Aluminum for delivery in three months on the London Metal Exchange
Source: CQG

THE WALL STREET JOURNAL.



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THE WALL STREET JOURNAL.
U.S. EDITION

**Emerging Debt Markets Pull Back**

By Chelsey Dulaney, Jon Sindreu and Saumya Vaishampayan
850 words
12 May 2018
The Wall Street Journal
J
A1
English


The dollar's rise is squeezing bond markets in developing countries like Argentina, Indonesia and Turkey, gutting what had been a popular trade for investors seeking stronger returns.

Countries in the developing world have been borrowing heavily, supported by upbeat expectations for global growth and a long period of low to negative interest rates that drove investors into emerging markets to get any sort of yield. Emerging markets added on $7.7 trillion in new debt last year, including bonds and other types of loans, with about $800 billion of that denominated in foreign currencies, according to data from the Institute of International Finance.

But as U.S. rates have started to climb, with the **10-year Treasury** note touching above 3% for the first time since 2014, and the dollar rallied, more cautious investors have pulled away from riskier emerging-markets bets.

Investors have pulled about $4 billion from emerging-market bond funds over the past three weeks, according to data from EPFR Global, after investors last year poured about $70 billion into those funds.

A stronger dollar hurts developing countries by making it more expensive for them to service dollar-denominated debts and to pay for imports. Those problems are especially acute for nations like Argentina that import more than they export and depend on money from foreigners to help them cover that deficit.

Argentina's peso has plunged 12% over the past month, even after the country's central bank raised interest rates to 40% in an attempt to stem the currency's slide. The government is now seeking a credit line from the International Monetary Fund.

Global investors are keeping a close eye on these markets, which had been among the world's top performers for stocks and bonds last year. That performance helped push up emerging-market currencies, too, with MSCI's currency index climbing 11%.

The dollar's steady slide last year benefited many emerging-market economies. While the dollar rally has lasted only a few weeks and could still fizzle out, a continued climb could mean more trouble for those countries.

Any sudden declines in emerging markets last year were usually met with a rush of buyers. In May 2017, reports that Brazil's president was part of a wide-ranging corruption scandal sent its currency reeling 7% on one trading day while stocks lost more than 10%. But a buy-the-dip mentality attracted interest, and the markets quickly recovered.

"Emerging markets had a good year from an economic standpoint, and people thought a lot of optimism on that front was warranted," said Oliver Jones, a markets economist at Capital Economics. "The memories of previous crises fade, and people get complacent about the potential currency risk."

That kind of rapid snapback has been missing. Turkey's currency has fallen about 4.1% to an all-time low in the past month, while Indonesia's rupiah has lost 1.4%.

Governments trying to raise money in the bond market have also struggled to get deals done. In Ghana, officials delayed a bond offering scheduled for Wednesday, which was designed to pay off some outstanding, more expensive debt, according to bankers and investors. The West African country ended up selling $2 billion one day later when market conditions improved, but at higher costs than officials expected when they announced the issuance.

Bahrain scrapped an international bond sale after investors demanded too high a price, money managers said.

Several companies in Latin America have also scrapped bond issuances after Argentina's IMF announcement, like Telecom Argentina SA and Paraguay's Banco Regional.

Few investors are calling a full-blown crisis in emerging markets, and many note that a number of emerging-market countries have taken steps to rein in spending and debt levels. Still, many believe the pressure is set to continue as investors pull back from riskier assets.

The Federal Reserve remains on track to raise rates at least two more times this year, but investors see a 47% chance that the U.S. central bank delivers at least three more rate increases, according to CME Group. That should help drive the yield on the **10**-**year Treasury** to 3.24%, according to a recent Wall Street Journal survey of economists.

"The interest-rates advantage has narrowed quite substantially," said Brad Bechtel, global head of foreign exchange at Jefferies Group. "It's hard to invest in those areas when you're not being compensated for it."

The debt that emerging markets have issued in dollars -- which was cheaper for them when U.S. rates were low -- is likely to face the most pressure, analysts say. JPMorgan's index for emerging-market bonds denominated in dollars has fallen about 4% this year, driving up yields and essentially erasing any excess return that investors were earning by holding local currency emerging-market bonds. Yields rise as prices fall. The IIF now expects foreign portfolio debt flows to fall about 20% this year to $255 billion.

**Disappearing Edge**

The reward bond investors get for taking currency risk in emerging markets has dwindled this year.


Note: Data are through May 7.
Source: JPMorgan

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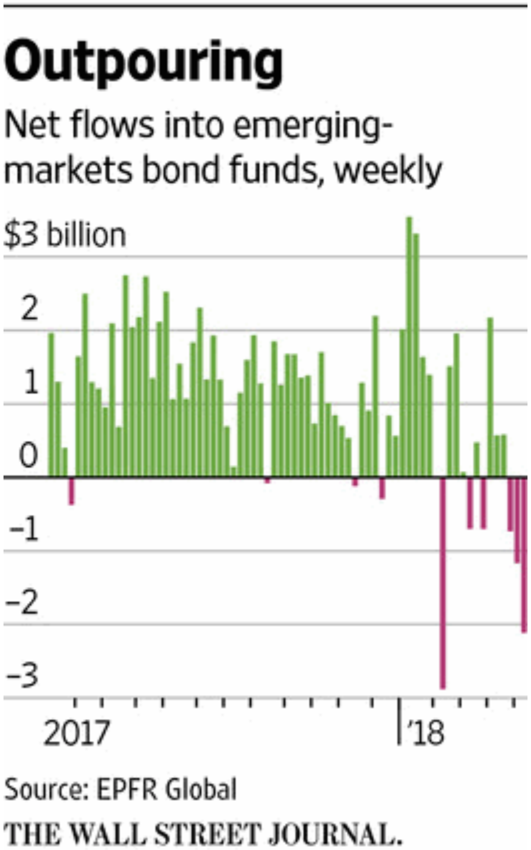


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WSJ PRO CENTRAL BANKING

Economy

**Malaysia Central Bank: Will Continue to Ensure Orderly Financial Markets; Following election, 'we must be careful not to overreact to market noises,' central bank chief says**

By Yantoultra Ngui
293 words
12 May 2018
08:31 AM
WSJ Pro Central Banking
RSTPROCB
English


KUALA LUMPUR, Malaysia--Malaysia's central bank will continue to ensure orderly conditions in the onshore **financial markets** following the latest change in government, the first since Malaysia gained independence from Great Britain in 1957, its governor said Saturday.

Malaysia's opposition coalition led by 92-year old Mahathir Mohamad pulled off a shock victory in Wednesday's election in what some analysts described as a surprising outcome on par with the likes of Brexit and U.S. President Donald Trump's election victory.

"Our experience tells us that we must be careful not to overreact to market noises, especially when it is caused by factors which are temporary in nature," Bank Negara Malaysia Gov. Muhammad Ibrahim said in a speech at an event in Malaysia's capital city.

The negative but much reduced influence of the nondeliverable forward market shouldn't detract from the ringgit movements over the longer term, he added.

"In the medium and long term, the ringgit will reflect Malaysia's strong economic fundamentals," Mr. Muhammad said.

Bank Negara Malaysiakept overnight policy rate unchanged at 3.25% on Thursday and reaffirmed that the outlook of the Malaysian economy remained strong, healthy and robust.

The stand-pat decision signaled Bank Negara Malaysia's confidence that the markets were expected to weather uncertainties created by the change in government. While most analysts expect a pullback when markets re-open in Malaysia on Monday, others such as Kuala Lumpur-based AllianceDBS Research Sdn Bhd. are more positive, and expect the selling to be brief.

Write to Yantoultra Ngui at yantoultra.ngui@wsj.com

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THE WALL STREET JOURNAL.

World

**The 10-Point. A personal, guided tour to the best scoops and stories every day in The Wall Street Journal, from Editor in Chief Gerard Baker.**

By Gerard Baker
1,136 words
11 May 2018
06:47 AM
The Wall Street Journal Online
WSJO
English


Good morning,

Auto Suggestion

The Journal reports that the U.S., Canada and Mexico are focusing on rewriting the auto rules at the center of the North American Free Trade Agreement , as negotiators face hard deadlines in an election year—raising the possibility of less drastic changes to other controversial parts of Nafta. However, time is running short. House Speaker Paul Ryan said Wednesday that he needs paperwork related to a Nafta deal by May 17 to have time to consider the deal in the House this year. Separately, the U.S. took a step toward cutting Iran off from the global economy, levying sanctions on a financing network . President Trump, meanwhile, said he would meet with North Korean leader Kim Jong Un . President Trump, meanwhile, said he would meet with North Korean leader on June 12 in Singapore , hours after he welcomed home three U.S. citizens who had been detained in North Korea for more than a year.

Apple Plastic

We report that Apple and Goldman Sachs are preparing to launch a new joint credit card , a move that would deepen the technology giant's push into its customers' wallets and mark the Wall Street firm's first foray into plastic. The planned card would carry the Apple Pay brand and could launch early next year. Apple will replace its longstanding rewards-card partnership with Barclays . The Apple-Goldman card could help the companies combat weaknesses in their core businesses. As new iPhone sales growth slows, Apple is focusing on services such as mobile payments, streaming-music subscriptions and App Store sales. Apple Pay is a key contributor, but adoption has been slower than executives had hoped. Goldman, meanwhile, is pushing into consumer banking to compensate for a slump in securities trading.

Buyback Bonanza

U.S. companies are buying back their shares at a record pace , providing fresh support during a rocky stretch for the **stock market** when many investors have rushed for the exits. About 85% of **S&P 500** companies have reported financial results for the first three months of the year, and they have collectively bought $158 billion of their own stock in that period, according to S&P Dow Jones Indices . That is on pace to be biggest amount in any quarter, based on data stretching to 1998. The buybacks have been fueled in part by a new tax law that is freeing up cash and encouraging companies to bring back money held abroad. Which companies have rolled out some of the biggest buybacks? Apple, Microsoft and JPMorgan Chase , among others.

The Future of Everything Magazine

Today marks the launch of The Future of Everything magazine, where readers will get a glimpse into the cryptocurrency crime wave in the cover story. From stickups and drug deals to white-collar scams, crypto-related crime is soaring—and law enforcement is trying to keep up, Journal reporter Corinne Ramey writes . In another piece, our columnist Elizabeth Bernstein delves into how two researchers in a Barcelona lab are using virtual simulations, from body-swapping to sessions with Freud, to build empathy and understanding. This comes as more than 120 speakers and 4,000 attendees gathered for our Future of Everything Festival this week, where industry leaders examined the future from a variety of angles, including artificial intelligence, work, transportation and equality. Societal changes and digital advances are renewing questions about equality, technology's role at home and in museums, and how much information is too much. [Find out what experts had to say](). 

Today's Video

Goodbye, Email?

As employers turn over more human-resources functions to chat apps and hiring platforms, the big question for many business leaders is how to rein in the slow creep of that technology into workers' personal lives. Slack CEO Stewart Butterfield is confident tools such as his company's messaging app ultimately save workers more time by enabling short, direct interactions with colleagues . In the video above, Mr. Butterfield draws his vision of future workplace productivity and communication.

TOP STORIES

U.S.

White House Set to Announce Plan to Curb Drug Prices

Program Allowing Foreign Students to Work in U.S. Has Grown Rapidly

WORLD

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Iraq Says It Captured Key Leaders of Islamic State

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MARKETS

AXA Equitable Flops in Largest IPO of the Year

Why Americans Aren't Feeling Wage Gains

Number of the Day

59%

The portion of private-sector economists predicting the U.S. economic expansion that began in mid-2009 will end in 2020 , according to a survey conducted by the Journal. If the expansion extends into the second half of next year, it would set a record for longevity.

Today's Question

Going back to our story above , would you use the planned Apple-Goldman credit card? Send your comments, which we may edit before publication, to 10point@wsj.com . Please include your name and location.

—Compiled by Jessica Menton

Reader Response

Responding to yesterday's question on the freeing of three U.S. detainees by North Korea , Bill Kaupert of Illinois wrote: "This development signals Mr. Trump's willingness to take a fresh, result-oriented look at the legacy issues in our foreign policy. It also signals the effect increased sanctions on North Korea have had to bring their leadership to the bargaining table." Derek Morrison of New Jersey shared: "While we should celebrate the return of the three Americans held by North Korea, we should not forget that they were detained for political leverage, rather than for wrongdoing. Kim Jong Un wants this to make him look good. Rather, it should remind us of the inhumanity of his regime." And Kristy McCray of Ohio weighed in: "North Korea has shown positive signs of engagement before, only to let down American deal makers in the end. I am cautiously optimistic that these three detainees won't fall into the same entry in our history books."

 

This daily briefing is named "The 10-Point" after the nickname conferred by the editors of The Wall Street Journal on the lead column of the legendary "What's News" digest of top stories. Technically, "10-point" referred to the size of the typeface. The type is smaller now but the name lives on.

Sign up here for a curated weekly tour of WSJ's unique take on the sports world including news, smart features, data and Jason Gay.

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The New York Times

Business Day
**Bond Market Indicates Doubt About Trump's Economic Targets**

By Matt Phillips
1,077 words
11 May 2018
02:42 PM
NYTimes.com Feed
NYTFEED
English


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The Federal Reserve has started raising short-term interest rates to reflect the economy's recovery, but longer-term rates — over which the Fed traditionally has far less influence — have not moved nearly as much. To many in the bond markets, that suggests investors think little has changed about long-term growth prospects.

"They're not expecting growth to move up to 3 percent on a sustained basis," said Julia Coronado, president of Macropolicy Perspectives, an economic consulting firm. "They're not looking for inflation to break out in any meaningful way on a sustained basis. It's not ominous. But it does sort of confirm that investors are still seeing the world in that way."

That does not mean the United States is about to enter a recession. By most measures, the economy is in fairly good shape as the current expansion — the second-longest on record — stretches into its ninth year. At 3.9 percent, unemployment hasn't been this low since 2000. Corporate profits are strong. Manufacturing activity has picked up.

But with rates in Fed-sensitive short-term government bond markets rising while longer-term rates are relatively flat, the gap between them has narrowed. And the plotting of those data points, known as the yield curve, occupies an outsize space in the minds of those who consider the markets a crucial barometer of economic health.

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But as the yield curve flattens, long-term interest rates run the risk of falling below short-term rates, a phenomenon known as an inverted yield curve. And when the yield curve inverts, as it did most recently in 2006-7, it amounts to an economic warning from the **financial markets** to watch out: recession is on the way.

"We're not there yet, but we're getting progressively closer," said Steven Abrahams, head of investment strategy at the broker dealer Amherst Pierpont. "And I think we will get closer, faster than the market currently anticipates."

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Mr. Williams stressed that he does not see an inverted yield curve, or recession, coming any time soon. And most economists agree. Over the next few years, private forecasters see United States economic growth peaking at 2.8 percent in 2018 before slowing to 2.5 percent in 2019 and 1.9 percent in 2020, according to Bloomberg data. That's a bit faster than the 2.2 percent growth rate of the United States economy since 2012.

But it's basically the same as the 2.6 percent average growth rate since 1980, suggesting that the $1.5 trillion tax overhaul signed into law by Mr. Trump in December is expected to have a negligible effect on long-term economic growth. Doing better would depend on increasing the supply of workers and raising productivity, a poorly understood process generally thought to depend on making large-scale investments in things like education, infrastructure and expensive equipment for companies.

Not everyone agrees that the bond market is sending a warning sign. For much of the last decade, the Federal Reserve and other central banks have been buying government bonds with the aim of pushing interest rates lower to support economic growth.

So the relatively low long-term rates partly reflect the large bond holdings of central banks, said Matthew Luzzetti, a senior economist at Deutsche Bank. That means those low rates contain "much less of a signal about negative growth in the future," Mr. Luzzetti said.

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* Unemployment Rate Hits 3.9%, a Rare Low, as Job Market Becomes More Competitive

* U.S. Economy Grew by 2.3% in First Quarter, Easing Slightly

* The Era of Very Low Inflation and Interest Rates May Be Near an End

* If the World Economy Is Looking So Great, Why Are Global Policymakers So Gloomy?

The Federal Reserve Bank of New York. Fed policy makers have been raising short-term interest rates, but have less control over long-term rates. | Jeenah Moon for The New York Times

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THE WALL STREET JOURNAL.
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**Buybacks Surge, Steadying Market**

By Ben Eisen and Akane Otani
980 words
11 May 2018
The Wall Street Journal
J
A1
English


Corrections & Amplifications

The **S&P 500** gained 1.8% in the year through May 10. A Page One article on May 11 about share buybacks incorrectly said the **S&P 500** gained 1.9% over that period.

(WSJ May 22, 2018)

(END)

U.S. companies are buying back their shares at a record pace, providing support for the **stock market** when many investors have rushed for the exits.

**S&P 500** companies that have reported earnings for the first three months of 2018 bought $158 billion of their own stock in the quarter, according to S&P Dow Jones Indices. About 85% of **S&P 500** components have reported so far.

That is on pace for the biggest amount in any quarter, based on data going back to 1998. The move has been fueled in part by a new tax law that is freeing up cash and encouraging companies to bring back money held abroad.

Cash-rich businesses are also raising dividends swiftly. **S&P 500** companies are on pace to have returned almost $1 trillion to shareholders for the 12 months through March through dividends and buybacks.

"The reason these companies are buying their stock is that they're smart enough to know that it's better for them than anything else," said Charles Munger, vice chairman of Berkshire Hathaway Inc., at the company's annual meeting last weekend.

Early signs suggest share repurchases have been effective, even in a year in which stocks have been tested by uncertainty around global trade, the path of interest rates and regulation around the technology industry.

Of the 20 **S&P 500** companies that spent the most on buybacks over the first quarter, nearly three-quarters have outperformed the index so far this year. The group has risen an average of 5.2% in 2018, compared with the **S&P 500**'s 1.9% gain, according to a Wall Street Journal analysis of S&P Dow Jones Indices data.

Apple Inc., the largest U.S. company by market value, said last week that it would embark on a $100 billion buyback program. The stock surged 4.4% the following day and 13% for the full week -- marking its biggest one-week percentage gain since October 2011.

Microsoft Corp.'s stock has risen 14% so far this year, after the company bought back $3.8 billion in shares in the first quarter. Boeing Co., JPMorgan Chase & Co. and UnitedHealth Group Inc. are up this year after big first-quarter buybacks.

Share repurchases can play a key role in supporting stock prices because they lower the number of shares outstanding -- driving up per-share earnings even without overall profit growth.

Many companies see them as a reward for shareholders, particularly when other corporate options for spending cash, such as acquisitions, don't look attractive. Executives say buybacks show management is **bullish** on the company's prospects and believe its shares are a good value.

Rising buybacks this year have been a crucial counterbalance to the rising tide of stock-fund redemptions. Investors yanked $29.4 billion out of exchange-traded funds and mutual funds tracking U.S. stocks in the first quarter, the most for any three-month stretch since 2016, according to a Bank of America Merrill Lynch report citing EPFR Global data.

The **S&P 500** is up only modestly for the year. Yet many analysts believe major indexes would have suffered losses without buybacks.

Corporations have long been among the biggest buyers of stocks -- making their share repurchases a major contributor to the nine-year **bull market**. Companies seized the chance to scoop up discounted shares following the financial crisis, with buybacks topping out in 2015 at $572 billion before leveling off.

Now with new tax incentives, share repurchases are ramping up again. The tax code overhaul President Donald Trump signed into law late last year assessed a one-time tax on foreign earnings, meant to encourage companies to repatriate more than $2 trillion in cash held overseas.

While that cash can be used for any number of activities, early signs suggest much of it is going into shareholder returns. Goldman Sachs Group Inc. expects **S&P 500** companies' spending on buybacks and dividends to rise by 22% to $1.2 trillion in 2018, outpacing the expected increase in capital expenditures and research and development in 2018.

"Activity is very widespread and we're seeing it executed in a lot of ways," said Jake Mendelsohn, a managing director at Bank of America Merrill Lynch who leads the desk that does corporate buybacks.

Share repurchasing has its critics. Mr. Munger said that buying shares just to keep the stock up is "insane and immoral." Some detractors say spending on buybacks can come at the expense of spending on R&D or equipment upgrades -- things they believe are the ultimate drivers of growth over the long run.

"For so long, productivity growth has been anemic or worse, and the plan has just been to pay your shareholders," said James Camp, managing director of fixed income at Eagle Asset Management.

But as the trend continues, market giants aren't the only ones that have benefited from buybacks. Kennedy-Wilson Holdings Inc., a real-estate investment company based in Beverly Hills, Calif., announced in mid-March that it would repurchase shares totaling $250 million, about a 10th of its market value, over the next 18 months. Within five weeks, it had already blown through half of that total.

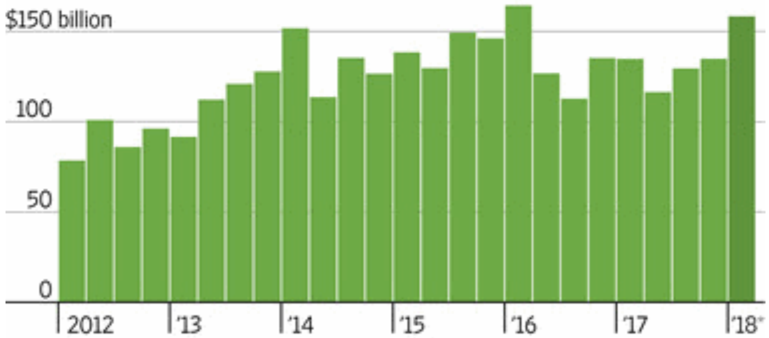
The buyback program, the company's biggest ever in its decade-plus stretch as a public company, appears to be working. Though the stock had been **volatile** along with the broader market earlier in the year, it started rising pretty much as soon as the program began. So far this year, shares are up 14%.

"The stock has been performing pretty well the last couple months relative to the rest of the market," said Matt Windisch, who oversees the company's buyback program. "Certainly the buyback played a role in that."

## Gobbling Up

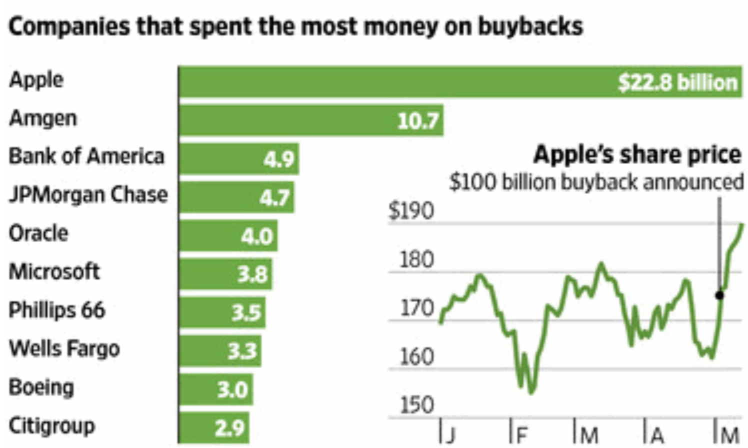
With results in from 85% of S&P 500 companies, corporations are on track to buy back a record amount of shares in the first quarter of 2018. S&P 500 share repurchases, quarterly:




*Data through Thursday; 15% of companies have not reported earnings.
Source: S&P Dow Jones Indices
THE WALL STREET JOURNAL.

## Spending Spree

Apple bought back more stock in the first quarter than any other S&P 500 company, and last week said it would embark on a $100 billion buyback program.




Sources: S&P Dow Jones Indices (top spenders); FactSet (stock); the company (announcement)
THE WALL STREET JOURNAL.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Streetwise: 'Quarterly Capitalism' Doesn't Add Up**

By James Mackintosh
1,016 words
11 May 2018
The Wall Street Journal
J
B1
English


The critics of short-termism have it wrong. The evidence doesn't support the idea that the economy is suffering because shareholders focused on quarterly reports leads to myopic management.

One quarter doesn't make a trend, but consider the latest quarterly reporting season. Capital spending by **S&P 500** companies is expected to rise 24% over the previous year, according to Credit Suisse, even as the wider economy increased business investment only 6%. It may not last, but the quarter provides a rebuke to critics of "quarterly capitalism," those who believe frenetic Wall Street trading makes listed companies focus on the short term.

The critics include some of the smartest and most powerful observers of Wall Street. And it isn't just lately. In the past century, it includes economist John Maynard Keynes, management theorist Peter Drucker and a cast of some of the biggest money managers and companies today, including consulting firm McKinsey & Co. and BlackRock Inc.

The basic critique was set out by Keynes. Americans, he wrote in 1936, rarely buy stocks for the long run. Instead, they invest in the hope of short-term gains, with baleful consequences: "When the capital development of a country becomes a by product of the activities of a casino, the job is likely to be ill done."

Turnover of stocks has soared since Keynes's day, with the average holding period now less than 12 months, while activists -- often derided as short-term plunderers -- take on almost one in 10 U.S. companies each year. Short-termism rules Wall Street.

The consequence of short-term shareholders isn't necessarily short-term managers, as Amazon.com Inc. shows. Short-term trading is much the same in Amazon shares as anywhere else: In the past 50 days, the equivalent of 60% of its shares have turned over. Yet Amazon is in for the long haul, spending heavily on both capital projects and research and development, while earnings are unusually low for such a big company. Founder Jeff Bezos told investors in 1997 that "it's all about the long term," and the company has had the biggest increase in market value of any business since then.

We can go beyond anecdotes. Harvard Law School professor Mark Roe points out in a coming paper that there should be three effects, if short-termism really has spread from Wall Street to management. R&D should be lower, because it has costs today for uncertain benefits in the future; business investment should fall faster in the U.S. than countries less reliant on stock exchanges; and corporate cash should be lower as shareholders demand it back via buybacks and dividends.

None has happened. R&D spending by **S&P 500** companies is at the highest proportion of sales since at least 1990, according to Goldman Sachs. Business R&D is the highest proportion of gross domestic product since the government started tracking it in 1959. If short-termism is a problem, it isn't hurting overall R&D spending.

There are issues, but they are more about which sectors are currently in vogue. Shareholders tend to trust certain companies to spend on R&D, notably in the technology and biotechnology sectors. Traditional pharmaceutical and manufacturing businesses are often punished for R&D spending, after a history of waste, and some have resorted to financial engineering to maintain R&D while appeasing shareholders.

Business investment is a different matter. Capital spending has dropped as a share of sales and GDP over many years, but it has dropped in Germany and Japan, too, countries notable for not being sensitive to shareholder desires. The broad pattern of falling corporate capital spending is mirrored across industrialized countries and has many causes, including China's overinvestment and spare capacity after the 2008 recession.

The surge in share buybacks is often held up as short-termism writ large. But companies by and large aren't buying back stock with cash that could instead be invested for the future. They are borrowing to pay for the buybacks, taking advantage of low interest rates, and aren't deprived of cash as a result.

My concern isn't about short-termism, but rather that companies are betting on rates staying relatively low, and their extra leverage leaves shareholders more exposed to an unexpected rise in financing costs or fall in cash earnings. It isn't that shareholders are being too short term in their views, but that they are ignoring low-probability, high-impact possibilities.

If anything, history suggests that smart investors should be less tolerant of capital spending by companies. One of the biggest dangers for investors, and occasionally for the wider economy, has come from allowing management to splurge on long-term projects: the South Sea bubble, the Railway Mania, Japan in the 1980s, the dot-com bubble, and the 2010-2012 mining excess. Academics have shown that on average companies that invest a lot have underperformed (the opposite applies to R&D). When a sector is in fashion, beware.

None of this is meant to justify a focus only on the short term. For some companies, quarterly earnings figures are all but meaningless, while for other companies they are vital to assessing their health. Part of the skill of investing is knowing which is which.

First-quarter results aren't yet all in, but Credit Suisse predicts more than half the increased capital spending will come from the tech sector, with Amazon -- classified as a retailer -- on top of that. Investors should be thinking about whether the long-run benefits will justify all that sunk cost and what might flow from the big rise in tech R&D.

What they should not be doing is worrying that the economy as a whole is suffering from CEOs pushed by investors to focus only on the next quarter. The evidence shows it isn't.

(see related letter: "Letters to the Editor: Don't Write Off Corporate Short-Termism" -- May 21, 2018)

 


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THE WALL STREET JOURNAL.

Markets
**U.S. Government Bonds Tick Lower on Solid Consumer Sentiment; Rise in yields is led by three- and five-year Treasury notes**

By Daniel Kruger
388 words
11 May 2018
04:10 PM
The Wall Street Journal Online
WSJO
English


U.S. government bonds edged lower Friday after a report showed consumer sentiment was steady in May, exceeding forecasts that it would decline to start the month.

The yield on the benchmark **10**-**year Treasury** note settled at 2.971%, unchanged from Thursday's close, but posted a weekly gain for the fifth time in six weeks. Yields rise as **bond prices** fall. On Friday, yields on three-year notes rose to 2.696% from 2.690%, and on five-year notes to 2.838% from 2.835%.

Yields rose after the University of Michigan said Friday that its index of consumer sentiment was 98.8 in May, unchanged from April. Economists surveyed by The Wall Street Journal had expected a preliminary May figure of 98.0. The sentiment measure had hit 101.4 in March, its highest level in 14 years. A final May reading will be released May 25.

Analysts attributed the rise in three- and five-year yields to investor expectations that recent inflation data could lead Federal Reserve officials to potentially slow the pace of rate increases, pushing back the point at which borrowing costs reach their projected peak.

Yields fell Thursday after the Labor Department said the consumer-price index, which measures what Americans pay for everything from ham sandwiches to sofas, rose 0.2% in April after falling a seasonally adjusted 0.1% in March. Excluding the **volatile** food and energy categories, so-called core prices rose 0.1%, compared with a 0.2% rise in March. Economists surveyed by The Wall Street Journal expected consumer prices to rise 0.3% in April, and core prices to rise 0.2%.

Inflation is a threat to the value of government bonds as it erodes the purchasing power of their fixed interest payments and can spur the Fed to raise interest rates.

If data continues to show inflation rising slower than expected, investors may infer it is "delaying the Fed path" to higher interest rates, said Aaron Kohli, an interest-rate strategist at BMO Capital Markets. Such speculation could point to the pace of rate increases accelerating in 2019, he said.

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THE WALL STREET JOURNAL.

U.S. Markets
Markets

**U.S. Stocks Post Biggest One-Week Gain Since March; Fears fade that inflation will prompt higher interest rates**

By Akane Otani and Mike Bird
531 words
11 May 2018
05:16 PM
The Wall Street Journal Online
WSJO
English


Bets on inflation remaining muted helped push investors back into the **stock market**, driving the **S&P 500** and **Dow Jones Industrial Average** to their biggest one-week gains since March.

Stocks have rebounded in recent sessions, with the Dow rising seven straight sessions through Friday—its longest such streak since November.

Data on producer and consumer prices suggested inflationary pressures are still soft, reassuring investors that prices aren't rising at a pace that would force the Federal Reserve to accelerate its pace of interest-rate increases.

Meanwhile, **oil prices** rallied to lift shares of energy companies. And shares of technology companies that came under pressure earlier in the year extended their recovery, with names like Google parent Alphabet, Facebook and PayPal all up more than 4% apiece for the week.

To some analysts, the recent moves suggest the **stock market** could finally be regaining its footing following a wave of **volatility** that had pulled major indexes down more than 10% from their all-time highs.

"Investors have been so worried about inflation and higher rates, and it's just not happening," said Karyn Cavanaugh, senior market strategist at Voya Investment Management. "I'm looking for all of the miserable things I could think of, and most of it seems to have already been priced in."

The Dow industrials rose 91.64 points, or 0.4%, to 24831.17, advancing 2.3% for the week.

The **S&P 500** added 4.65 points, or 0.2%, to 2727.72 and posted a 2.4% weekly gain, while the **Nasdaq Composite** edged down 2.09 points, or less than 0.1%, to 7402.88 for a 2.7% weekly advance.

Major indexes wobbled between small gains and losses Friday as shares of semiconductor firms came under pressure. Nvidia, which posted better-than-expected quarterly earnings Thursday, fell $5.60, or 2.2%, to $254.53, with some analysts attributing the decline to investors taking profits following a recent run-up in the stock.

Despite the day's moves, Nvidia jumped 6.5% for the week and remained up 32% for the year.

Meanwhile, Verizon Communications rose 1.42, or 3%, to 48.62, posting its third biggest one-day gain of the year, after JPMorgan Chase analysts upgraded their rating for the stock to "overweight" from "neutral."

Elsewhere, the Stoxx Europe 600 closed up 0.1%, boosted by gains in shares of basic-resources companies.

Japan's Nikkei Stock Average rose 1.2% and posted its seventh consecutive weekly advance—its longest such streak since the week ended Nov. 10, 2017.

Hong Kong's Hang Seng Index rose 1% on the day, while Malaysian markets remained closed after a surprise opposition win in elections.

Write to Akane Otani at akane.otani@wsj.com and Mike Bird at Mike.Bird@wsj.com

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THE WALL STREET JOURNAL.

Markets

**Oil Prices End Down on Profit-Taking; Baker Hughes reported the number of drilling rigs in the U.S. rose for a sixth-straight week**

By Christopher Alessi and Alison Sider
734 words
11 May 2018
04:06 PM
The Wall Street Journal Online
WSJO
English


Oil prices fell Friday, stalling after surging to more-than-three-year highs after President Donald Trump's decision to pull the U.S. out of the Iran nuclear deal.

U.S. crude futures settled down 66 cents, or 0.92%, at $70.70 a barrel on the New York Mercantile Exchange. Brent, the global benchmark, fell 35 cents, or 0.45%, to $77.12 a barrel on ICE Futures Europe

Prices still ended the week higher, with Brent up 3.01% and West Texas Intermediate up 1.41%

Oil sold off toward the end of the day as investors took profits after this week's gains. And oil-field-services firm Baker Hughes reported that the number of drilling rigs in the U.S. continued to march higher for a sixth-straight week, portending more oil production to come—something that could blunt the impact of renewed sanctions against Iran.

"This market is very overbought," said Donald Morton, senior vice president at Herbert J. Sims & Co., who oversees an energy trading desk.

President Donald Trump's move Tuesday to abandon the 2015 international agreement to curb Iran's nuclear program paved the way for the reimposition of U.S. economic sanctions on the Islamic Republic. The expectation that sanctions will again frustrate Iran's oil industry and limit global supply has helped to boost prices close to 5% since the announcement.

In the past, sanctions against Iran have cut the country's crude exports by around 1 million barrels a day. But because the European Union and other intentional players have decided to stick with the deal, U.S. sanctions are likely to affect only up to around 350,000 barrels a day, once reinstated within six months' time, according to analysts at MUFG Bank.

The surge in prices this week prompted renewed oil market speculation that Brent could again reach $100 a barrel—a level not seen since before the price crash of late 2014.

"The U.S. decision to withdraw from the Iran nuclear deal was clearly the key driver of the week, with the potential loss of Iranian production coming as the market already faces a tight supply/demand balance," analysts at Schneider Electric said.

Bank of America Merrill Lynch on Thursday predicted a Brent price target of $90 a barrel by the second quarter of 2019, while noting a "risk of $100 a barrel" oil next year. "Although, we are concerned these market dynamics could unfold over a shorter time frame," the analysts wrote in a note.

Analysts at Commerzbank said Friday current price levels indicated the Organization of the Petroleum Exporting Countries was now "regaining the price power it had lost" in the wake of the first U.S. shale boom that led to the price drop over three years ago.

"A large part of the price slide, which saw [Brent] plunge from over $100 to below $30 a barrel as a result of the price war between OPEC and the U.S. shale oil industry that began in autumn 2014, has now been reversed," the analysts wrote in a note.

OPEC's efforts to rein in the supply glut through production curbs helped boost prices by more than 50% last year. The cartel—led by Saudi Arabia—and 10 outside producers, including Russia, have been holding back crude output by around 1.8 million barrels a day since the start of 2017. The agreement is set to expire at the end of this year.

However, Saudi Arabia—the de facto head of OPEC—signaled this week it could up its own production to make up for lost barrels from Iran.

"If the reimposition of U.S. sanctions on Iran leads to a reduction in Iran's oil output and exports, OPEC and its allies could exit the deal at the end of the year or even sooner in order to prevent a supply shortage in the oil market," said Thomas Pugh, commodities economist at Capital Economics.

Gasoline futures edged down 0.01% to $2.1888 a gallon Friday. Diesel futures fell 0.04% to $2.222 a gallon.

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Document WSJO000020180511ee5b0015p

 

WSJ PRO CENTRAL BANKING

Economy
**Transcript: Media Q&A With St. Louis Fed President James Bullard; Central banker discusses the outlook for interest rates and inflation and the prospect of an inverted yield curve**

2,847 words
11 May 2018
02:55 PM
WSJ Pro Central Banking
RSTPROCB
English


Federal Reserve Bank of St. Louis President James Bullard answered reporters' questions on a conference call after giving a speech in Springfield, Mo., on Friday, May 11, 2018. He discussed the labor market, trade uncertainty, and the outlook for interest rates and inflation, among other topics. Here is a transcript of the exchange, lightly edited for length and clarity.

JAMES BULLARD: Yeah, OK. So I outlined five reasons for caution today, and I'd make the case that we should go maybe a little bit slower than what markets are expecting. So I'm anxious to hear what you all thought about it, and so I think we can get started.

…So let's start with Steve Matthews and then we'll go around the circle here.

Q: Jim, you made a strong case that we don't need additional rate hikes, but the committee is pretty clear that they are moving ahead with additional hikes. What's the damage that that is likely to do? Does that mean we're going to get undershooting of inflation or inflation expectations? Does that mean we're going to get market **volatility**, a recession? What do you see as the damage being done if the committee continues to go ahead with its hikes?

MR. BULLARD: Well, I would say there are risks to continuing to hike. Of course, we never know if those risks will actually materialize or not. But the yield curve inversion issue would be a **bearish** signal for the U.S. economy if that developed. Research suggests that after the inversion you'd still have anywhere from two quarters to eight quarters before you'd actually get a(n) economic downturn, so you'd still have a while even after an inversion to think about what was going to happen to the U.S. economy.

On the inflation side, I think markets are saying they don't see a lot of inflation pressure, so that if the Fed gets too aggressive here the inflation expectations will decline again. And actual inflation would come out below our 2 percent target instead of at our 2 percent target, which is exactly what we've seen over the last six years or so. So I think those are some of the – those are some of the issues for the Fed.

I want to stress that I do think the economy is in very good shape today. You know, I said during the talk, you know, it was time to pop the Champagne. You don't often see outcomes this good in the U.S. economy – the unemployment rate below 4 percent with an inflation rate, you know, arguably at or below 2 percent. That's a very good situation. But the monetary policy game is all about trying to think a few moves ahead about what's going to happen, and that's what I'm trying to think about here.

Howard Schneider.

Q: Hi, President Bullard. Thanks for letting us stay home for this one.

MR. BULLARD: Oh yeah.

Q: Yeah.

Let me ask you this. When you say that you think the neutral rate's pushing against the upper bound, does that think – does that mean that the next step or two actually makes policy restrictive? And how robust a debate is under way about removing this accommodative language from the statement, therefore? And what are the options there in terms of a new phraseology?

MR. BULLARD: On the phraseology, I don't know what the chairman would propose on that. But I do think this is a live issue in front of the committee. Many other (Federal Open Market Committee) participants have talked about where they think the neutral rate is.

I think we should keep in mind that the confidence bounds around the neutral rate are very wide. So anytime people are talking about a neutral policy rate, they're talking in a probabilistic sense because no one, you know, can really be sure where the real neutral rate is. And, you know, it's just a very uncertain process.

I think what I drew out in the chart today was just a, you know, super simple idea about, you know, these real rates look extremely low even today. And even if you think they've moved up slightly recently, they still look extremely low. And that would give a benchmark real interest rate – short-term real interest rate that would be negative. And if you add 2 percent to that, you're going to get something below 2 percent for a neutral policy rate. And therefore, that's the source of the statement that we're pushing against the upper bound of what is reasonably interpreted as neutral.

Michael Derby, Wall Street Journal.

Q: Hey, thanks for taking my question.

The Fed's forecasts show an expectation of an inflation overshoot in coming years. Do you also expect that? And if inflation were to slightly overshoot the Fed's 2 percent target, is that an – is that an OK outcome for you?

MR. BULLARD: Yeah, I know many participants have talked about possible overshooting of the target. I've always been in favor of the idea that it's a symmetric target. In fact, I've wanted the committee to be more forward-looking in stating that the target is symmetric. So I basically have no problem with some overshooting of the target, especially given that we've undershot the target for quite a while.

Also, there are limits to how well we can measure inflation. So, you know, a lot of the policy debate has focused on tenths of a percent on the inflation rate. It's probably not realistic to think we can actually measure inflation that closely, and you can see that when you look at the various measures of inflation. They all come out with slightly different numbers. So slight overshoot, slight undershoot is probably a sort of false precision.

But in general terms, I'm not worried about sometimes being above target and sometimes being below target.

Q: Are you at all expecting it to happen, though?

MR. BULLARD: I think it – I think it's a possibility. It could happen. I'm not seeing as much inflation pressure as maybe other observers are because I'm not as big a believer in the Phillips curve as other observers of U.S. monetary policy tend to be. They tend to put a lot of weight, I think overweight, on that particular argument, which does not have a lot of empirical support over the last couple of decades. So they're kind of – in my mind, they're mechanic – I won't try to say that word – (laughs) – in my thought they are – they're mechanically saying that, you know, because unemployment is low, therefore inflation's going to overshoot because of some statistical relationship that I think is not necessarily there in more recent data.

Q: Thanks.

MR. BULLARD: OK. Who's next?

STAFF: Jean Young (sp) or Sara Haire?

Q: Yeah. Hey, it's Jean (sp) here.

I am wondering, do you think it's possible for the labor market to overheat? And what would be signs of that for you?

MR. BULLARD: Yeah, I – some of my remarks were pushing back against the whole idea of overheating. Sure, labor markets can be in equilibrium. In my mind that means labor services are traded around at competitive rates and firms have to compete to get labor to work at their particular – in their particular endeavor. And if they can't get the workers that they want, they can – they can raise the wages if they want, or they can substitute away from labor and toward capital, and that it's this latter margin that allows the labor market to stay in equilibrium over a long period of time. So this is just a story about relative prices as opposed to always thinking about wages as somehow feeding into an inflation process.

 

The empirical evidence for that in recent years is not very good either. Wages tend not to predict future inflation movements very well in recent data, even though they may have predicted better in the 1970s or even the 1980s. But in recent years, recent decades, they have not done a good job of predicting future inflation outcomes. And so I wanted to reorient people toward the idea that maybe this is an equilibrium process and not an inflationary process.

STAFF: Greg Robb with MarketWatch.

Q: Thank you. Thanks for doing this again. It's really helpful.

I guess my question is, are you saying inflation is a little bit too low? And is the problem for central banks that they don't know how to get inflation higher? And why is inflation so low? I guess that would be my question.

MR. BULLARD: Well, my favorite measure of inflation is the Dallas Fed Trimmed Mean (personal-consumption expenditures) inflation rate measured from one year earlier. That's 1.8 percent today. It's not very different than it was a year ago. So I would – and my interpretation of market-based inflation expectations is that they are not all that high either. And so, in my mind, both inflation itself and expected inflation remain, you know, good, but slightly below target. And for that reason, I think we're not in any danger of any breakout of inflation anytime over the forecast horizon. So I think, you know, my message is we're in pretty good shape today as far as the monetary policy goes.

And I would also stress this idea that to the extent you think inflation pressure was building in the U.S. economy as the economy continued to improve, even if you thought that that was what was going on, the Fed has already been pre-emptive because we've already raised the policy rate on the order of more than 150 basis points in anticipation of these effects. And so I think that's part of what's keeping inflation in line, about where it was, and keeping inflation expectations in line as well.

So we – instead of thinking that we have to do more in order to contain those types of pressures, what you should be thinking is that we've already taken action to contain those pressures. We've also initiated the balance-sheet shrinkage more aggressively than what we had before. And so that is also contributing to containing these inflation pressures and keeping inflation expectations close to target.

STAFF: And take a few questions in the room?

MR. BULLARD: Sure.

STAFF: So, Greg.

Q: I want to go back to the labor-market equilibrium. You know, you're giving remarks today in a city that has a 26 percent poverty rate. And so the idea of a Champagne economy may strike some folks as a little off from their daily experience. And I wondered if you could talk about the tightness in the labor force.

MR. BULLARD: But, hey, it doesn't – it might have a high poverty rate, but the unemployment rate is quite low.

Q: It is low. It is low.

MR. BULLARD: Yeah. Yeah. So –

Q: I'm not disagreeing.

MR. BULLARD: OK. (Laughs.) So, you know, in the sense of traditional interpretations of unemployment, which are that everybody that wants a job can find a job, it is a good labor market. I would say if the economy here – you know, the poverty rate here would be dependent on what we think the cost of living is here. And I've also done other work, completely separate from this discussion, about metropolitan statistical areas and how there are lower costs – there are different price levels for different metropolitan statistical areas. And this is definitely one of the lowest costs, for instance, for rent. So that helps alleviate some of the pressure on low-income workers. And I think you see that in everyday life. So that's helpful.

But overall, you can't get to great outcomes unless you can attract even better jobs to the area. I think the chamber's trying to do that. There are some great employers in the area. And, you know, I'd love to see, you know, everybody really do well. But in terms of sort of matching up workers with jobs, the unemployment rate tells you about that. And it's very low.

Q: Thanks.

 

STAFF: John.

Q: Yeah. For the – (inaudible) – against Fed rate increases, do you see any kind of immediate upset in the five points that you addressed today, with increases expected in the summer/fall?

MR. BULLARD: Yeah. I think the – you know, the process – it's a slow-moving process. And, you know, one rate hike here and there is probably not the biggest issue. But I would say the yield curve inversion is getting close to crunchtime, because that could invert with only, let's say, two more rate hikes. So that would be a very quick time schedule. You know, you'd be – you could be talking about even September. I don't think that's likely to happen that fast, but in the next year I think this could be a tangible issue. That's why I've tried to bring it up now, so that we go in with our eyes open. And if we're going to – if we're going to press in that direction, that we do so.

So people are saying two things about the yield curve, as far as I can tell. Some people are saying: I don't think it will invert, because I think longer rates will go up as the Fed continues to increase. So they're kind of a "I don't think it'll happen" crowd. There's another crowd that says: "I think it will happen, but it's not going to be a signal of bad things for the U.S. economy." It's the latter crowd that I'm more worried about.

STAFF: And just right back to the phone, making sure we caught everyone. Alister Bull or Sara Haire, where there any further questions? I'm not sure you guys asked one to begin with.

Q: Jim, Alister here. Thanks for doing this. Nice to hear your voice again.

You know, you had this very bold call on holding rates steady through the forecast horizon. What would it take for you to change your outlook, basically walk back this through steady state – low-steady state growth regime you've been talking about around the country for the last, I guess, 12 to 18 months? What would it take for you to walk that back?

MR. BULLARD: I think inflation and inflation expectations would have to surprise substantially for the upside before I've start getting more hawkish. I think they remain, you know, subdued, according to the argument from me today. And so for now I think I have the right call. I am willing to look at data. I am willing to react to data. I'm not as willing to put a lot of weight on the idea that tight labor markets are going to lead to inflation. So that's probably a difference between me and other observers to the U.S. economy.

STAFF: Great. Sara, did you have a question?

Q: Yes. Hi, thank you so much for doing this. But I was just wondering, both, I guess, is part of your – (inaudible) – has talked about how trade uncertainty is one of the biggest risks facing business investment. Do you have any opinion on that?

MR. BULLARD: Yeah. I think the trade talk has introduced uncertainty into **financial markets** and, by extension, on the U.S. economy. Certainly this part of the country is – you know, can be affected. Agricultural exports are one of the, you now, biggest pieces of the trade puzzle. Whether these – whether the trade talk will translate into actual trade policy which is worse for the United States, I think is a good question. It could just as easily translate into something that's better for the United States ultimately.

And so we'll have to see how this develops going forward. I do think there is both downside and upside. But it depends on what actually transpires with (the North American Free Trade Agreement) and with other trade negotiations around the world. So, you know, I wouldn't put it all down to downside risk. I would say that there is some potential upside that the U.S. would get a better trade deal. But in the meantime, it's introducing uncertainty for U.S. producers and U.S. importers.

Related Article

* Bullard Upbeat on the Economy, but Still Opposes Further Rate Rises

Document RSTPROCB20180511ee5b000ul

 

Strategies
Business Day
**Profits Are Soaring. The Stock Market Has Barely Noticed.**

By Jeff Sommer
995 words
11 May 2018
01:30 PM
NYTimes.com Feed
NYTFEED
English


Earnings season is underway on Wall Street and, thanks to a heady combination of core business strength and tax windfalls, the results have been exceptional.

In fact, based on the numbers so far, profits among the biggest American corporations are growing so fast that you may expect the **stock market** to be soaring like a rocket.

That's not the direction the market has been heading, of course. Since February, most stocks have been sluggish — or downright negative — and the spectacular earnings reports have received less fanfare than they probably deserve.

There are valid reasons for the market's lack of response, the main one being that by February the market had gotten way ahead of itself, reaching valuations that few people could justify. Stocks rose so rapidly in 2017 and early 2018 — on top of their increases since 2009 — that prices had begun to seem impossibly high.

Add the negative impact of rising interest rates and heightened expectations for inflation — both of which tend to hurt share prices — and it's easy to see why the **stock market** weakened as much as it did.

Yet the reality is that earnings growth has been extraordinary so far this year. That superlative performance won't continue forever — that's no more possible than eternal youth. Next year, in fact, the tax effect is expected to subtract from earnings growth when this year's windfalls are baked into financial statements.

But it's still worth noting how good this season has been and what it may portend for the next year or two. For people who have been concerned that stock valuations had gotten out of whack and that the threat of a trade war imperils the economy — and I'd place myself in that camp — the earnings surge provides some comfort.

Tax windfalls are certainly inflating the numbers, but the core earnings of American corporations look solid, nonetheless.

Consider the picture for the first three months of 2018, the period for current earnings reports. By one measure, the quarter is actually turning out to have been the best for corporate America in decades. The tax cuts that went into effect this year have transformed excellent earnings into exceptional ones.

David Aurelio, a senior research analyst for Thomson Reuters, says nearly 80 percent of the companies in the **Standard & Poor's 500-stockindex** that have reported so far have outstripped the expectations of Wall Street — 16 percentage points higher than the average number of companies that beat expectations. "That performance is the best since our records started in 1994," he said.

Earnings per share have grown 26 percent since the same quarter a year earlier, according to Thomson Reuters I/B/E/S data. Net operating income — essentially, profit after taxes — has risen nearly 25 percent in the same period. Almost half of that gain, 11.6 percentage points, comes from the big cut in corporate taxes that took effect this year.

The tax windfall alone accounts for a larger earnings increase than the **stock market** typically receives from conventional sources, the data shows. Expectations of a tax cut may help explain the run-up in stocks in 2017 and earlier this year.

But writing off the current earnings surge entirely as a pure artifact of tax cuts would be a mistake. Before taxes, earnings grew 13.2 percent for the quarter. That is a breathtaking figure.

“Whenever you get double-digit earnings growth coming from core earnings, it is really healthy,” Mr. Aurelio said. “What I find surprising is that, aside from the tax cuts, fundamentals are really looking strong,” he added.

Take Apple, the world’s most valuable publicly traded company. When it reported its most recent quarterly earnings on May 1, the results were remarkable: a 25.3 percent increase in net income over the same quarter a year earlier.

More than half of that improvement came from tax windfalls. In its financial statement, the company reduced its expected tax liability for the period — technically, its provision for taxes — by more than 35 percent. And in a conference call, Apple executives said that thanks to the new law, the company’s effective tax rate has dropped to 14.5 percent. It was 25.5 percent in the same period last year, they said.

The tax changes mean that Apple suddenly has “increased financial and operational flexibility from the access to our global cash,” which had been stranded abroad, said Luca Maestri, Apple’s chief financial officer. So Apple announced a $100 billion increase in what had been a $300 billion share buyback program, as well as a 16 percent dividend increase.

All of that is a boon to shareholders. But what is probably more important is that the iPhone and other core businesses continue to churn out staggering profits even after stripping away the effects of taxes.

Apple’s operating income rose more than 10 percent in the quarter, an impressive figure in its own right, and the end of the Apple profit machine is nowhere in sight.

Apple isn’t the only company to have churned out outstanding earnings. Profits have been rising for most big American companies, and Wall Street expects that to continue for at least the next year or two.

Edward Yardeni, an independent market strategist, points out that double-digit earnings growth isn’t likely to be sustained by corporate America. Profit growth is likely to decline to the roughly 7 percent annual rate that has been the historic norm, he says. And the norm is that **stock market** will rise at about that rate over the long run. He expects that to continue.

While the market has barely noticed the current avalanche of profits, the combination of stagnant prices and rising earnings means that market valuations have already improved rapidly. If that trend continues, many stocks will again begin to look like bargains.

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THE WALL STREET JOURNAL.
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Heard on the Street
**Core Prices Aren't the Only Inflation Metric That Matters**

By Justin Lahart
436 words
11 May 2018
The Wall Street Journal
J
B12
English


[Financial Analysis and Commentary]

Headline inflation is going up. Pay attention.

The Labor Department on Thursday reported that overall consumer prices rose 0.2% in April from March, putting them up 2.5% versus a year earlier. That marks the biggest annual gain in headline prices in over a year. Core prices, which strip away food and energy items, rose a more muted 0.1%, putting them up 2.1%.

When economists and Federal Reserve policy makers are trying to understand inflation's trend, they like to look at the core. There is a good reason for this since prices for food and energy can bounce around as a result of temporary factors that don't reflect the overall economy.

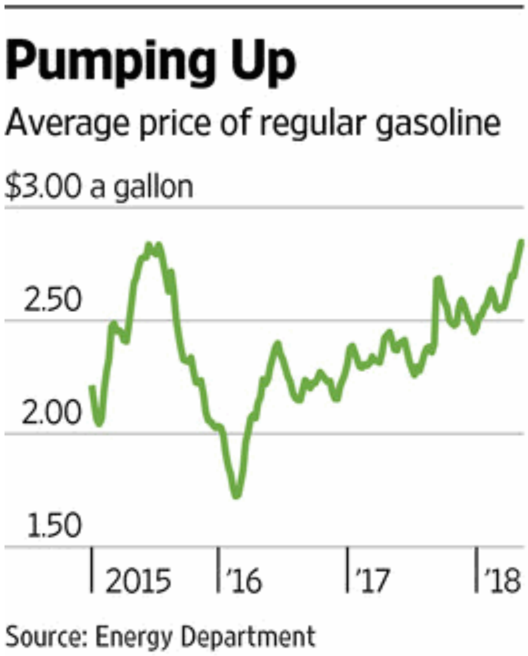
But that doesn't mean food and energy prices should be overlooked. Even though moves in them are short-term, they are still costs that Americans must bear and, since groceries and gasoline are among people's most frequent purchases, they tend to shape people's perceptions of inflation. They also matter because increases in food and energy prices can reflect cost pressures that are going to show up elsewhere.

It is gasoline prices that were the big force pushing overall inflation higher in April and that looks likely to continue. The average retail price for regular gasoline in April was $2.76 a gallon, according to the Energy Department, up 14% from a year earlier. Pump prices are higher now: Gasoline averaged $2.86 on Monday.

The summer driving season kicks off with Memorial Day weekend this month. That won't just drive demand but also will draw drivers' attention to how much more gasoline costs this year. The underlying trend in inflation may still be subdued, but that isn't how consumers are going to see it. Moreover, higher fuel prices can slip into the costs of other things. Truckers charge more, for example, and workers may push harder for higher wages to offset what they are putting into the tank.

Additionally, higher gasoline prices have come about as a result of a rise in **oil prices** that is largely due to the global economy doing better. With demand rising around the world, prices for other globally traded commodities, as well as imports to the U.S., could climb.

Already in tightening mode, this isn't something that the Fed will be able to ignore. The move higher in headline inflation could end up becoming a core concern for investors, too.

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THE WALL STREET JOURNAL.
U.S. EDITION

**Pricing Hitch in Heart of U.S. Oil Boom --- In West Texas, strained pipelines lead to crude selling for under $60 a barrel**

By Alison Sider and Ryan Dezember
967 words
11 May 2018
The Wall Street Journal
J
B12
English


The main U.S. oil benchmark, West Texas Intermediate, has soared to its highest level in years at $71 a barrel. Good luck getting that price in West Texas.

In the epicenter of America's drilling boom, crude is going for less than $60 a barrel because oil output there has overwhelmed pipelines that connect the Texas desert to markets along the Gulf Coast and abroad.

U.S. **oil prices** are splintering because of bottlenecks in the region due to crowded pipelines and worker shortages. Analysts and investors worry such logjams will threaten the profits of Permian producers and slow crude output when the global oil market is already facing limited supplies because of disruptions from Iran and Venezuela. That would propel rising **oil prices** even higher.

Producers would like to get their oil to places such as Houston, where oil can be loaded onto tankers and shipped overseas. There, the same crude fetches upward of $73.

But it could be a year or more until new pipelines catch up with surging production. At the region's current growth rates, analysts at PLG Consulting expect that close to 200 million barrels of oil will be unable to make it to market in the next 16 months.

"They're not going to be able to get it all out," said Taylor Robinson, president of PLG.

Some Permian producers have already locked up space on pipelines, or have used financial instruments to hedge their exposure to these types of price swings. Many say that only a fraction of their output is actually sold at those low levels in Midland, the city in West Texas where the local price of crude is set. But others are stuck watching a rally pass them by.

"If you're a producer who does not have any firm space at all, you're going to eat the majority of that $13 or $16" price difference, said John Zanner, an analyst at RBN Energy LLC.

This has happened before. In 2014, Midland **oil prices** fell to a nearly $20 discount to the national benchmark. But the price gaps were just a few dollars or less until recently.

The widening spread is weighing on Permian Basin producers. Shares of Laredo Petroleum Inc. sank 15% last week after the company said it expected its output for the rest of 2018 to fetch 91% of the Cushing price, down from the 95% it had earlier told investors.

The drop occurred after a trading partner abruptly ended an arrangement that let Laredo choose whether to sell some of its oil in Midland or near export facilities along the Gulf Coast. Laredo's agreement with Royal Dutch Shell PLC's trading arm was struck in 2016, when the prices were closer. It has been the subject of litigation since last year.

The Tulsa, Okla., company was forced to find new buyers for 19,000 barrels a day on short notice. "We dumped it in the Midland market," said Dan Schooley, Laredo's senior vice president of operations. The stock has recovered about a third of last week's plunge as executives laid out contingency plans for its crude.

Meanwhile, the price gaps are an opportunity for infrastructure companies to build new pipelines or expand existing ones.

"In the pipeline industry, this is like oil going over $100 a barrel. It's pretty profound," said Jay Hatfield, portfolio manager of the InfraCap MLP ETF.

Now trucks and trains are coming back into vogue in West Texas, but neither is a perfect solution. Rail facilities could take months to get going. And the trucking industry is already stretched thin and doesn't have enough drivers to move both crude and the sand needed for fracking.

ARB Midstream LLC is looking at dusting off a proposed rail terminal it put on the back burner last year when it was tough to find customers and the project looked too risky. Now, "we're getting calls once a week from a variety of groups asking 'is your facility ready, we want to use it,'" said Chief Executive Adam Bedard.

Refiners with plants in the region are gobbling up as much cheap crude as they can.

Delek US Holdings Inc. buys about 70% of its crude in the Permian Basin and told investors this week that it expects the gap between the U.S. benchmark and the Midland price to grow to nearly $20 early next year.

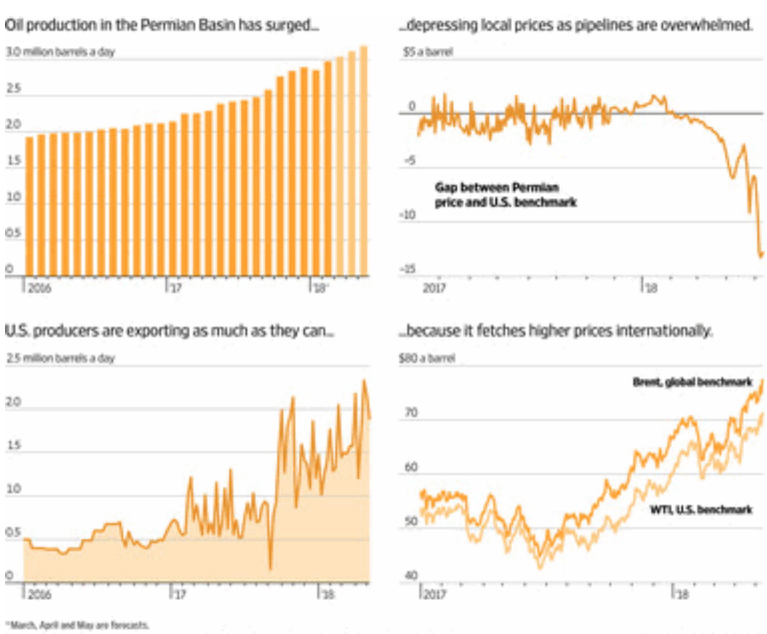
Every dollar that Midland crude drops below the U.S. benchmark results in about $75 million of profit on an annualized basis for Delek, the Tennessee-based refiner told investors. That is on top of the nearly $100 million in earnings it adds when the Cushing price, West Texas Intermediate, falls $1 below Brent, the international benchmark. The Cushing price is currently about $6 below Brent.

Delek CEO Ezra Uzi Yemin said the "huge windfall" won't last forever. But for now, it has helped to nearly double the refiner's share price over the past year.

Producers that have long been reluctant to lock themselves into long-term agreements with pipelines are suddenly more eager to secure space on pipes that are now in the works.

Diamondback Energy Inc. recently signed on to send 50,000 barrels a day on a planned pipeline system that will eventually take oil to the Gulf Coast, where it can be refined or shipped abroad.

"Getting our barrels on a ship will get us a global price," Kaes Van't Hof, senior vice president of strategy and corporate development, said during a conference call Wednesday.

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THE WALL STREET JOURNAL.
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**Business News: Many Top-Paid CEOs Have Left --- Eight of 20 highest- paid S&P 500 chief executives of 2017 are no longer on the job**

By Theo Francis
779 words
11 May 2018
The Wall Street Journal
J
B6
English


Many of 2017's best-paid chief executives aren't CEOs anymore. One died; some left after boardroom conflicts or deteriorating corporate financial performance. Others stepped down in recent weeks.

Of the 20 highest-paid S&P 500 chief executives of 2017, eight are no longer on the job. Each took home at least $30 million in total compensation, including stock grants and cash bonuses that were awarded for the year. That's more than double the 2017 median pay for an S&P 500 boss.

Hunter Harrison, who died in December while at the helm of railroad CSX Corp., officially was paid $151 million in compensation for the year -- catapulting him past Broadcom Ltd.'s Hock Tan, the highest-paid full-year CEO at $103 million.

Mr. Harrison's pay figure includes $116 million in stock options that expired, worthless, upon his death. The remaining pay of $35 million still left him at No. 13 among all CEOs in the Journal's 2017 pay survey.

A CSX spokesman noted CSX paid about $29 million under an agreement with Mantle Ridge, an activist investment firm that had promised to pay Mr. Harrison for compensation left behind at his prior job. CSX also reimbursed Mantle Ridge for an earlier $55 million payment to Mr. Harrison, who was 73 when he died, but excluded it from his pay calculation under SEC rules.

CSX's total return for the year was 55.4%, a figure that takes into account dividends as well as stock appreciation. This outstripped the median return of 18.7% for S&P 500 companies run by full-year CEOs.

Alex Molinaroli took home $78.3 million for leading Johnson Controls International PLC for the first eight months of last year. Mr. Molinaroli left the industrial company on Sept. 1 following disappointing results, after a merger with Tyco International PLC. Johnson Controls posted a total shareholder return of negative 0.9% for its full fiscal year, which ended Sept. 30.

About $64 million of Mr. Molinaroli's pay was cash severance and other payments after the company named his successor earlier than planned, according to the company's proxy. A Johnson Controls spokesman declined to comment further.

The 58-year-old had been CEO since 2013, and there had been questions about his pay package before. In 2016, Johnson Controls paid Mr. Molinaroli $46 million in a single month, and didn't disclose what he made for the remainder of that year.

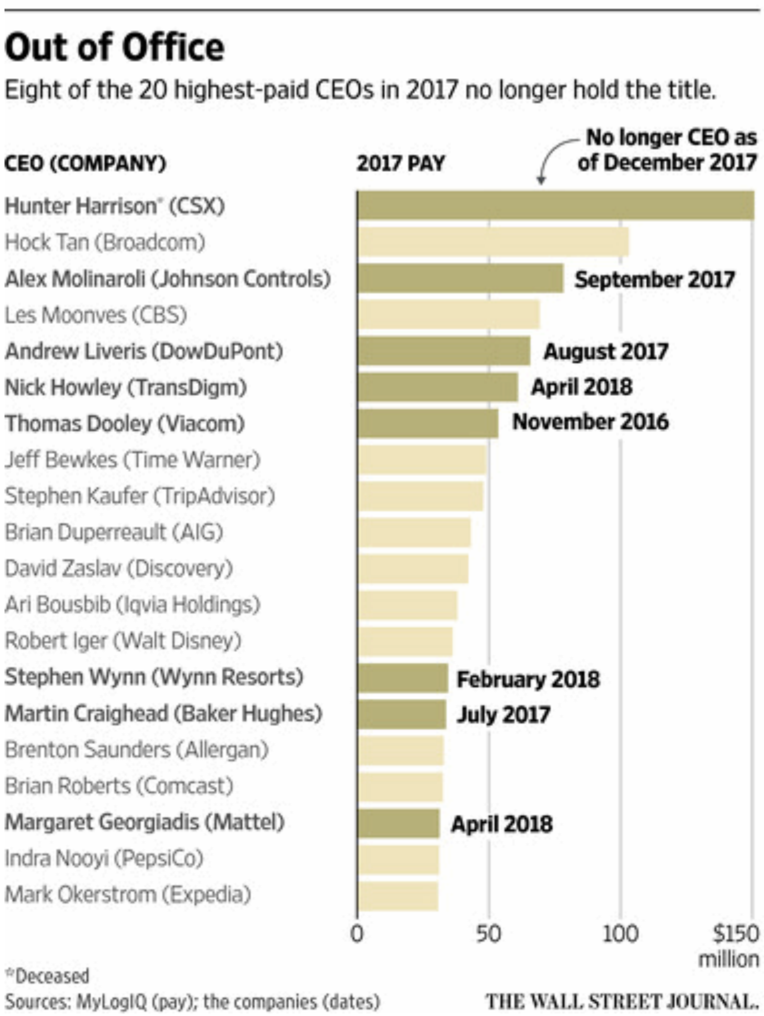
The Journal's annual ranking of CEO pay generally excludes newly hired CEOs and those who left during the year. New and departing CEOs often receive big one-time payments to secure their hire or a quiet departure.

In aggregate, these one-time payouts make little difference. Median pay for the 410 full-year CEOs in the Journal's survey rose to $12.1 million in 2017 from $11.5 million. Including an additional 81 new and departing chiefs shifted the 2017 median slightly to $12 million, up from $11.2 million.

Margaret Georgiadis, who served about a year as CEO of toy maker Mattel Inc., was the highest-paid woman overall in 2017, at $31.3 million. Ms. Georgiadis joined the maker of Barbie dolls in February 2017 and was unable to reverse a sales slump. In April, the company said she was leaving and would be succeeded by a board member. Mattel shareholder return in 2017 was minus 42%.

Ms. Georgiadis's compensation included $14 million in restricted stock to replace equity she left behind at Google, where she had been an executive, as well as $11 million in equity grants described as new hire inducements. Mattel said Ms. Georgiadis wasn't entitled to severance on her departure. She became CEO of Ancestry, which provides DNA tests and the ancestry.com genealogy website, on Thursday.

Other top-paid CEOs are also no longer in office: Stephen Wynn, the founder of Wynn Resorts Ltd., who made $34.5 million before resigning this past February after allegations of sexual misconduct, and former Dow Chemical CEO Andrew Liveris, at $65.7 million, who ran Dow until its Aug. 31 merger with DuPont and served as executive chairman of the combined DowDuPont Inc. through April 1. The company said that, absent the payout of benefits earned during his time at Dow, Mr. Liveris would have made about $22 million. A representative for Mr. Wynn didn't respond to a request to comment.

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WSJ PRO CENTRAL BANKING

Economy

**Fed Seen Raising Rates in June, September | Wells Fargo Expects Fed Asset Cap to Continue | BOE Bullish on U.K. Economy | U.S. Sanctions Target Iran's Central Bank | Hannon's Take: Gender Quotas for the ECB? The Wall Street Journal's central banking newsletter for Friday, May 11, 2018**

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Hannon's Take: Gender Quotas for the ECB?

Economists See Fed Raising Rates in June, Then September

Wells Fargo Expects Fed Asset Cap to Continue Into Early 2019

BOE Bullish on U.K. Economy as It Leaves Rates Unchanged

U.S. Raises Pressure on Iran With Sanctions on Currency Exchange

Gender Quotas for the ECB?

The European Central Bank's governing council is large by any standards. There are 25 seats, offering plenty of room for all kinds of people from all kinds of places.

But passports aside, the governing council isn't very diverse. Just two of its members are women, and the likely sequence of successions over coming years suggests that isn't likely to change much.

Is this a problem? A speech by a potential future member suggests it may be.

Sharon Donnery is deputy governor of Ireland's central bank. At a conference in Malta, she argued that diversity helps counter the risk of "groupthink, insufficient challenge, poorly assessed risk, and problems with culture."

Ms. Donnery was speaking about the banks she and other central bankers regulate, but there's no reason why that logic shouldn't apply to the ECB itself.

The eurozone doesn't appear to be in any rush to alter the gender balance on the body that makes decisions about monetary policy and other matters. To be fair, the ECB itself doesn't have a great deal of influence over the situation, since 19 of those positions are filled at the discretion of individual national governments, while the others require agreement among them.

So what is to be done? Going back to Ms. Donnery's analysis, we find her surprised at herself for concluding that outside interventions may be needed.

"There was a time when I wouldn't have believed in targets or quotas, but I now see them as a necessary part of the picture," she said.

When Ms. Donnery joined the Central Bank of Ireland in 1996, there were no women among the eight-member senior management team. There were no women among the 13 division heads. In 2018, 39% of directors are women, as are 49% of division heads.

Things can change, if you want them to.

Philip Lane, Ms. Donnery's boss, is one of the favorites to join the ECB's six-member executive board next year.

That would leave a vacancy at the CBI, which Ms. Donnery may fill. She would then find herself on the ECB's governing council. Unfortunately, there is a very plausible succession scenario that would leave her as one of just two or three women.

"Diversity, in my view, needs to start from the top," she said in Malta.

Key Developments Around the World

Economists See Fed Raising Rates in June, Then September

The Federal Reserve is almost certain to raise short-term interest rates at its June policy meeting and will likely follow up with another increase in September, according to economists surveyed by The Wall Street Journal. Among professional forecasters surveyed in recent days, 98% predicted the Fed's next rate increase will come at its June 12-13 meeting, with the average probability of a move then pegged at 85%. Some 76% of the economists predicted the Fed's next move after June would come at its Sept. 25-26 meeting, with the average probability of a September rate increase seen as 64%. A smaller camp, 19%, said they expected the Fed would wait until December to make its third rate increase of 2018.

Economists Say Next U.S. Recession Could Begin in 2020

Wells Fargo Expects Fed Asset Cap to Continue Into Early 2019

Wells Fargo Chief Executive Timothy Sloan said the bank's asset cap imposed by the Federal Reserve will continue into the first part of 2019. Mr. Sloan, speaking at Wells Fargo's investor day presentation Thursday, said the bank needs time to address and incorporate feedback from the Fed. The Fed, which cited "widespread consumer abuses" at Wells Fargo, imposed the asset cap in an unprecedented enforcement action in February. Wells Fargo is barred from growing past the $1.95 trillion in assets it had at the end of 2017 unless it gets regulators' permission. It can continue to lend and take deposits.

BOE **Bullish** on U.K. Economy as It Leaves Rates Unchanged

The Bank of Englandstill expects to raise its key interest rate over the coming years, saying Thursday that a slowdown in economic growth during the first three months of the year was likely temporary and probably not as severe as first estimated. "We think momentum in the economy is going to reassert," Gov. Mark Carney said in a news conference, after the central bank left its key interest rate at 0.5%. "If we're right, then the expectation of households and businesses, which is for some modest adjustment of interest rates, will be justified."

BOE Defends Guidance

Why Americans Aren't Feeling Wage Gains

Rising inflation is eating up more of U.S. workers' paychecks. Average hourly pay for private-sector workers, adjusted for inflation, was flat in April from a month earlier, the Labor Department said Thursday. Average weekly earnings, also taking into account inflation, fell 0.1% last month. From a year earlier, real average hourly earnings for private-industry employees edged up just 0.2% in April. The consumer-price index rose 0.2% in April after falling a seasonally adjusted 0.1% in March. Core prices, which exclude the **volatile** food and energy categories, rose 0.1%, held down by falling prices for used cars and trucks, airline fares and recreation.

U.S. Raises Pressure on Iran With Sanctions on Currency Exchange

The U.S. Treasury Department on Thursday levied sanctions against several Iranian firms, individuals and officials it said are operating an illegal currency-exchange network in the United Arab Emirates, and accused Iran's central bank of being complicit in operations that funneled dollars into the country for Iran's elite military unit, the Quds Force, and Tehran's regional proxies.

Bank Indonesia Has Scope to Adjust Policy Rate to Help Rupiah, Central Bank Governor Says

Bank Indonesia has ample scope to raise the 7-day reverse repo rate to help the rupiah, which has been depreciated by 3.7% against the dollar so far this year, Gov. Agus Martowardojo said Friday. "The policy responses will be taken consistently and pre-emptively to ensure economic stability," Mr. Martowardojo said.

Quick Hits

 

A reading from the Cleveland Fed shows underlying inflation in the U.S. picked up in April and softening inflation could give the People's Bank of China room to ease monetary policy. Here are quick hits on central banking and related market views from around the world.

Friday

9 a.m. EDT

Bank of Canada's Wilkins speaks

9:15 a.m. EDT

ECB's Draghi speaks

Low Risk as a Predictor of Financial Crises

**Volatility** isn't a good economic crisis indicator, Jon Danielsson, Marcela Valenzuela, and Ilknur Zer find in recent FEDS Notes economic research paper. "It will be more fruitful to search for [early warning indicators] amongst the fundamental drivers of financial instability. A major cause of financial crises is excessive risk-taking by economic agents. When they perceive a low risk environment, they are endogenously incentivized to take more risk, which ultimately culminates in a crisis... An observation of low risk is a significant crises predictor. The policy authorities and private institutions would consequently benefit from using low **volatility** as a crisis indicator since an observation of current low **volatility** implies that a future crisis is more likely."

Globalization Has Kept a Lid on Inflation

Globalization has helped keep a lid on inflation, and any reversal in that process would likely contribute to a pickup in price rises, according to new research by Dan Andrews, Peter Gal and William Witheridge at the Organization for Economic Research and Development. Their findings are based on a new data set of prices and global value chains broken down by industry. "This analysis suggests that the expansion of GVCs facilitated by trade liberalisation and advances in technology has put downward pressure on producer prices, with potential implications for monetary policy," they write. "Looking forward, a continuation of the stalling globalisation observed since the crisis poses an upside risk to future inflation. This provides a further reason to resist the rising threat of trade protectionism in the global economy."

Ignore Headline Inflation at Your Peril

"Headline inflation is going up. Pay attention... When economists and Federal Reserve policy makers are trying to understand inflation's trend, they like to look at the core. There is a good reason for this since prices for food and energy items can bounce around as a result of temporary factors that don't reflect what is going on with the overall economy," Justin Lahart writes for The Wall Street Journal. "But that doesn't mean food and energy prices should be overlooked. Even though moves in them are short term, they are still costs that Americans must bear and, since groceries and gasoline are among people's most frequent purchases, they tend to shape people's perceptions of inflation. They also matter because increases in food and energy prices can reflect cost pressures that are going to show up elsewhere."

Trump's Trade Threats Are Hurting Growth

"Economic uncertainty and prosperity are sworn enemies—when uncertainty reigns, prosperity fades. Uncertainty undermines prosperity by sapping investor and consumer confidence, choking off private investment, and suppressing consumer spending," Phil Gramm and Mike Solon write for The Wall Street Journal. "The depression that followed the 1929 crash and the recession that followed the 2008 financial crisis are called "great" not only because of the magnitude of the downturns, but also because the economic uncertainty that followed produced the weakest recoveries of the past century. Today, the Trump administration's trade policies have increased economic uncertainty to a level that threatens to bring back the stagnation of the Obama years."

The Richmond Fed announced that Becky C. Bareford will become the organization's first vice president and chief operating officer effective June 1, 2018. Ms. Bareford was appointed by the Bank's directors, an action approved by the Federal Reserve Board of Governors.

Layoffs across the U.S. are hovering near the lowest level in half a century. The number of Americans applying for unemployment benefits—known as initial jobless claims—was 211,000 in the week ended May 5, the Labor Department said Thursday.

 

The U.S. government posted the highest April budget surplus on record last month, although the federal deficit widened as spending rose along with revenues. The deficit was $385.4 billion in October through April, up 12% over the same period a year earlier.

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

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THE WALL STREET JOURNAL.
U.S. EDITION

**Malaysia Vote Shocks Investors**

By WSJ Staff
338 words
11 May 2018
The Wall Street Journal
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English


Heavy selling looms in Malaysian assets when markets reopen next week, after the country's opposition coalition pulled off a shocking victory in Wednesday's election.

A U.S.-listed exchange-traded fund of Malaysian stocks slumped 6% on Wednesday, its biggest decline since 2011, while the dollar has risen more than 2% against the ringgit in the derivatives market. The ETF recovered 1.8% on Thursday.

Incoming Malaysian Prime Minister Mahathir Mohamad earlier declared two days of national holidays after his Alliance of Hope coalition secured a parliamentary majority following the vote.

The "huge upset" over Najib Razak "ranks up there with Brexit and [U.S. President Donald Trump's] election," said Aninda Mitra, senior sovereign analyst at BNY Mellon Investment Management.

While anticipating short-term **volatility** in Malaysian markets next week, "a long-term fix of governance, institutions and public life is now in sight," he said. Still, he added, near-term policy uncertainty will be high, taking a toll on the country's currency, the ringgit, for now.

Malaysia's currency and stocks had started falling ahead of the election, as signs emerged that Dr. Mahathir's opposition party was gaining momentum. His party has offered few details on its economic-policy plans, although its campaign manifesto proposed scrapping the country's goods-and-services tax and reintroducing fuel subsidies.

Such moves could have a negative impact on Malaysia's credit rating without offsetting measures to raise fiscal revenues, Moody's Investors Service warned Thursday. It currently rates the country at A3, four steps above the investment-grade rating threshold.

Meanwhile, Malaysia's central bank, as expected, kept interest rates at 3.25%. The policy statement said, "The domestic economic outlook remains positive, the financial sector is strong and monetary and financial conditions are supportive of economic growth in the postelection environment." That could signal central-bank confidence that the markets can weather uncertainties created by the change in government.



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WSJ PRO CENTRAL BANKING

Economy

**Quick Hits: Cleveland Fed Says Underlying Inflation Continued to Rise in April; Richmond Fed names Becky Bareford first vice president and operating chief**

By WSJ Staff
1,213 words
10 May 2018
03:35 PM
WSJ Pro Central Banking
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English


A reading from the Cleveland Fed shows underlying inflation in the U.S. picked up in April, the Richmond Fed named a new operating chief, and softening inflation could give the People's Bank of China room to ease monetary policy. Here are quick hits on central banking and related market views from around the world.

Cleveland Fed Says Underlying Inflation Continued to Rise

Underlying inflation ticked up a bit higher in April, according to a reading from the Federal Reserve Bank of Cleveland . The bank's median consumer-price index in April was up 2.6% from a year ago, while the conventional CPI was up 2.5% for the same period. The median CPI has been grinding higher over recent months: It stood at a 2.3% annualized increase in November, for example.

Michael S. Derby

Richmond Fed Names First Vice President and Operating Chief

The Federal Reserve Bank of Richmond said Becky Bareford is being promoted to first vice president and chief operating officer, replacing Mark Mullinix , who will retire in June. Ms. Bareford started at the Richmond Fed in 1998, and has held a number of positions dealing with operational issues faced by the bank. She will work with the bank's new leader, Thomas Barkin, who started as president at the beginning of the year.

Michael S. Derby

Cropland Prices, Incomes Fall in Parts of Midwest

Cropland values dropped alongside incomes in parts of the Farm Belt during the first quarter, according to a report by the Federal Reserve Bank of St. Louis . Farm income fell for the 17th consecutive session in the Fed district—which includes parts of states like Illinois, Indiana and Missouri—while prices for "quality" farmland declined 1.4% versus year-ago levels. Prices for ranch and pastureland rose 13%. Farm bankers are growing more optimistic about the agricultural economy as crop prices have risen this year, but a prolonged strain on farm incomes may be driving higher loan demand, the report said. Nearly one-quarter of bankers surveyed said more than half of their farm borrowers would face "severe financial difficulty" without income from off the farm.

Jesse Newman

Softening Inflation Gives PBOC Room to Loosen

Softening price pressures should give the People's Bank of China ample room to loosen monetary policy later this year in response to cooling economic activity, says Julian Evans-Pritchard at Capital Economics. Possible restrictions on imports of soybeans and pork from the U.S. pose some upside risk to China's food inflation, he notes, but a broader easing of price pressures should keep the consumer-price index anchored near current rates. The economist also predicts that the producer-price index will likely be back in negative territory by year's end if a further decline in the price of key industrial commodities proves correct.

Grace Zhu

Tightening Cycle Unlikely in the Philippines

The Philippines' first rate increase since 2014 on Thursday shouldn't mean the start of a prolonged tightening cycle, says Capital Economics. Inflation has hit three-year highs and topped the central bank's target. But the firm says the recent rise has been mainly due to temporary factors such as higher indirect taxes on high-sugar drinks, tobacco and alcohol as well as a spike in food prices partly due to typhoons in the first quarter.

Chester Yung

Another Bank Pushes Back Start of Australian Rate Increases

Citi's longstanding view has been Australia's central bank will begin a gradual tightening cycle late this year. But now it doesn't see that starting until the first quarter because of what the investment bank calls several recent developments that have created greater uncertainty about the economic and financial outlook. Local lending standards appear to be tightening further in response to the revelations of financial misconduct coming out of the Royal Commission, and there is also uncertainty about the extent and length of the current slowdown in global growth, it adds.

James Glynn

Sharp Intermeeting Rate Rise in Turkey the Only Option: Commerzbank

A sharp intermeeting rate increase seems to be the only option available for Turkey, according to Commerzbank . President Tayyip Erdogan on Wednesday summoned his economic management team, including Deputy Prime Minister Mehmet Simsek and central-bank Gov. Murat Cetinkaya to an emergency meeting to discuss the slide of the lira. "This meeting has not, so far, resulted in any major policy announcement. There was a brief press release from the President's office emphasizing that pro-growth policies will be maintained, but that the fiscal situation will not deteriorate," Commerzbank says.

Yeliz Candemir

BOE Tends to Misread Economy: ADM

In simple terms, the Bank of England 's problem for the past four years has been that it has misread the economy time and time again, says Marc Ostwald, global strategist at ADM Investor Services International . The BOE, he says, hasn't been "data dependent," but rather its policy pronouncements have been dependent on how it sees the economy evolving, quite often flying in the face of incoming data. Mr. Oswald says the case for a rate raise this year looks weak. "Hopefully **financial markets** will take a rather more skeptical, or at least critical view of [Monetary Policy Committee] policymaker pronouncements, rather than sticking to the rather slavish or Pavlovian reaction function that has been on display since the turn of the year."

Emese Bartha

BOE Likely to Raise Rate More Than 3 Times in 3 Years: JP Morgan AM

The Bank of England said in its interest-rate statement that it is committed to raising rates three times over the next three years, but J.P. Morgan Asset Management calls this a "very modest" forecast. "Over this three-year horizon, we think it is likely that rates will rise by more," says Karen Ward, chief market strategist for the U.K. and Europe at J.P. Morgan Asset Management in an email. "We expect the recent weakness in the data to largely prove temporary and a Brexit deal to be sketched out by October," Ms. Ward says. "We expect the BOE to raise rates by 25 basis points in November of this year."

Olga Cotaga

BOE Rate Raise in 2018 'Delayed, Not Cancelled': Fitch Ratings

It looks like a 2018 rate raise by the Bank of England "has been delayed not cancelled," says Brian Coulton, chief economist at Fitch Ratings . The Monetary Policy Committee members are "quite dismissive" of the growth weakness in the first quarter and maintain their view that the economy has little slack, Mr. Coulton says. "But the area that is probably giving them most grounds for pausing is the recent weakening in consumption indicators, which could be flagging a bigger downside risk to the growth outlook," the economist says. The deterioration in U.K. household finances over the last couple of years—with an unprecedented shift into a financial deficit in 2017—poses risks to consumer spending as credit availability tightens, Mr. Coulton adds.

Emese Bartha

 

(The items in this column come from Market Talk, a feature of Dow Jones Newswires that provides real-time analysis of news developments and market activity.)

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THE WALL STREET JOURNAL.

Heard on the Street
Markets

**Still Too Early to Get Back on Wells Fargo's Wagon; Wells Fargo expects to remain longer than initially expected under an onerous asset cap**

By Aaron Back
561 words
10 May 2018
02:20 PM
The Wall Street Journal Online
WSJO
English


Wells Fargo has been stuck in a rut since details began emerging of its sales abuses a year and a half ago. Despite some optimistic projections from the company on Thursday, it is still too early for investors to get back in.

The bank's shares have risen just 9% since the Consumer Financial Protection Bureau issued a statement in September 2016 detailing how the bank opened millions of accounts for customers without their permission. Over that same time the KBW **Nasdaq** Bank Index has risen 53%, amid a turnaround in the broader industry's fortunes.

A steady drip of new revelations has kept the bank under scrutiny, including issues in auto lending and wealth management. Regulatory pressure culminated with the Federal Reserve's shock imposition of an asset cap on the bank, preventing it from growing its balance at all until it makes progress improving internal controls.

On Thursday, Wells Fargo Chief Executive Timothy Sloan said at an investor event that the bank now expects to remain under this asset cap until "the first part of 2019," later than it initially suggested.

In a presentation, Wells Fargo Treasurer Neal Blinde stressed the bank's ability to optimize its current balance sheet within those strictures. Nevertheless, the Fed's order remains a serious threat to Wells Fargo's franchise, forcing painful trade-offs and giving competitors an opportunity to take away business.

To be fair, Wells Fargo has maintained a decent profit profile throughout this turmoil. For the years 2016 and 2017, the bank had set a target range for return on equity, a closely watched measure of bank profitability, of 11% to 14%. It performed to the low end of this range, reaching returns of just over 11% both years.

Chief Financial Officer John Shrewsberry boasted Thursday that these returns were higher than those of mega bank peers. "I don't think that's well understood and we take comfort from that outcome," he added.

This is true, but it ignores some important context. Last year returns at Wells Fargo's peers were hit disproportionately by tax-reform-related write-downs in the fourth quarter. Because of its history and geographic footprint, the net effect was positive at Wells Fargo. What excites investors about its competitors is their potential for higher returns going forward. JPMorgan Chase, for instance, posted a 15% ROE in the first quarter of 2018, compared with a 12% return at Wells Fargo.

Wells Fargo set a new, higher ROE target of 12% to 15% for 2018 and 2019. This improvement was largely due to lower taxes, though, and it also excludes potential litigation expenses or other penalties from its continuing controversies.

Given how shoes continue to drop at Wells Fargo, including complaints filed with regulators just this week by a Tennessee public pension fund about its fee practices, it is no sure bet that the bank will be back in the good graces of regulators any time soon.

Despite this, Wells Fargo shares still aren't cheap at 1.5 times book value, a ratio that already anticipates their new, higher return targets. Investors should stick to banks with fewer unknowns.

Write to Aaron Back at aaron.back@wsj.com

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THE WALL STREET JOURNAL.

Markets

**Shock Election Result Spells Turbulence for Malaysian Markets; Heavy selling anticipated when the Southeast Asian country's markets reopen next week**

By WSJ Staff
686 words
10 May 2018
04:13 AM
The Wall Street Journal Online
WSJO
English


Heavy selling looms in Malaysian assets when markets reopen next week, after the country's opposition coalition pulled off a shock victory in Wednesday's election.

A U.S.-listed exchange-traded fund of Malaysian stocks slumped 6% on Wednesday, its biggest decline since 2011, while the dollar has risen more than 2% against the ringgit in the derivatives market.

Incoming Malaysian prime minister Mahathir Mohamad earlier declared two days of national holidays after his Alliance of Hope coalition secured a parliamentary majority following the vote in the Southeast Asian nation.

The "huge upset" over Najib Razak "ranks up there with Brexit and [U.S. President Donald Trump's] election," said Aninda Mitra, senior sovereign analyst at BNY Mellon Investment Management.

While anticipating short-term **volatility** in Malaysian markets next week, "a long-term fix of governance, institutions and public life is now in sight," he said. Still, he added, near-term policy uncertainty will be high, taking a toll on the country's currency, the ringgit, for now.

Malaysia's currency and stocks had started falling ahead of the election, as signs emerged that Dr. Mahathir's opposition party was gaining momentum. His party has offered few details on its economic policy plans, although its campaign manifesto proposed scrapping the country's goods-and-services tax and reintroducing fuel subsidies.

Such moves could have a negative impact on Malaysia's credit rating without offsetting measures to raise fiscal revenues, Moody's Investors Service warned in a statement Thursday. It currently rates the country at A3, four steps above the investment-grade rating threshold.

Malaysia's election upset comes at a time of heightened stress in global emerging markets.

Argentina has tapped the International Monetary Fund for financial backing, the latest drastic step policy makers have taken as they seek to stem the peso's depreciation. The central bank last week boosted interest rates to 40%.

Meanwhile, Turkey's markets have continued to swoon over concerns about its economy. Standard & Poor's Global Ratings recently slashed the country's sovereign-debt rating further into junk territory, and the International Monetary Fund has warned that Turkey's economy is at risk of overheating.

The central bank of Malaysia's neighbor Indonesia has intervened in the foreign-exchange market in recent weeks to shore up its currency, the rupiah, while foreign investors have been running from its stocks and bonds. Markets there are closed Thursday for the Ascension Day holiday.

Investors had been positive on Malaysia's market at the start of 2018, with the ringgit and equities outperforming regional peers: The country's main stock benchmark briefly topped its 2014 record high last month.

However, the ongoing corruption scandal surrounding Mr. Najib and state-owned investment fund 1Malaysia Development Bhd., which is subject to investigations in multiple countries, has clouded investor sentiment.

The yield on a 10-year bond from 1MDB that matures in 2023 surged to 9.54% on Thursday morning, according to IHS Markit, up from 6.1% on Wednesday. Bond yields rise when their prices fall.

The cost of insuring Malaysian government debt has also risen, with the price of 5-year credit default swaps up nearly 9% on Thursday.

The Malaysian election results also weighed on neighboring Singapore's **stock market**. Equities there had been underperforming of late—with Malaysia—and the Straits Times Index was lower most of the day, though little changed heading into the last hour of trading Thursday amid broad gains for Asia-Pacific stock indexes.

Meanwhile, Malaysia's central bank went ahead with its previously scheduled policy meeting and as expected kept interest rates at 3.25%.

The policy statement only had one mention of the election.

"The domestic economic outlook remains positive, the financial sector is strong and monetary and financial conditions are supportive of economic growth in the post-election environment," it said. That could signal central bank confidence that the markets can weather uncertainties created by the change in government.

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THE WALL STREET JOURNAL.

U.S. Markets
Markets

**U.S. Stocks Climb as Inflation Fears, Volatility Ebb; Dow Jones Industrial Average rises for sixth straight session, posting its longest winning streak since February**

By Michael Wursthorn and Riva Gold
759 words
10 May 2018
06:07 PM
The Wall Street Journal Online
WSJO
English


U.S. stocks rose Thursday and market volatility continued to fade, as fears of runaway inflation abated to help send the Dow Jones Industrial Average higher for a sixth consecutive session.

The Dow rose nearly 200 points to notch its longest winning streak since February after investors got another sign that inflation may be rising, but not so rapidly that the Federal Reserve would have to take aggressive actions to keep the economy from overheating.

Meanwhile, the volatility that rocked the stock market this year and sent major indexes into correction territory has gradually faded, giving some money managers hope that stocks are gaining upward momentum.

A key measure of expected market swings, the Cboe Volatility Index, or VIX, has fallen six straight trading sessions, settling near levels that were last seen in early January, when stocks were in so-called melt-up mode following the passage of Republicans' tax overhaul.

Shares of technology stocks, one of Wall Street's most popular trades, have also been gaining traction since Facebook's data mishap was revealed in March, giving investors a shot of confidence. Apple has added 15% so far this month, while Facebook and Google parent Alphabet have risen more than 7%.

"We're settling in a little bit as the leadership in the market has improved," said Mark Lehmann, president of JMP Securities. Apple's massive gain since it reported strong earnings and disclosed plans to buy back an additional $100 billion in shares has given some investors "real optimism about the future," he added.

New Labor Department data released before the market's open Thursday indicated U.S. consumer prices rose less than expected in April and followed last Friday's employment report that showed wage growth remains sluggish, alleviating some recent worries and removing a major hurdle for the Dow and other indexes to move higher.

The Dow industrials added 196.99 points, or 0.8%, to 24739.53 to extend its climb since May 3. The S&P 500 rose 25.28 points, or 0.9%, to 2723.07, while the Nasdaq Composite added 65.07 points, or 0.9%, to 7404.97, the tech-heavy index's fifth consecutive day of gains.

However, the Dow remains roughly 7% below its last record set in late January.

Shares of Apple extended their climb, adding $2.68, or 1.4%, to $199.04 to help lift the Dow. UnitedHealthGroup also traded higher, gaining 4.50, or 2%, to 233.71.

Meanwhile, the weak consumer pricing data put pressure on the dollar and U.S. government bond yields. U.S. 10-year Treasury yields fell to 2.971% from 3.004% on Wednesday, while the WSJ Dollar Index slipped 0.5%.

Investors around the world continued to overlook rising geopolitical tensions in recent sessions to push stocks higher, led by gains in energy companies that benefit from rising oil prices.

Still, some market participants worry that an increasingly uncertain policy outlook could eventually pose a threat to corporate profits and economic growth. The U.S. is exiting from the Iranian nuclear accord, President Donald

Trump said Tuesday, triggering multinational companies that recently made big bets on Iran to review their investment plans.

"There is a broad mosaic of potential policy concerns," said Bill Northey, a senior vice president at U.S. Bank Wealth Management. Concerns around how the Trump administration proceeds on trade, North Korea and Iran, along with how inflation and rising interest rates play out over the next year, has led U.S. Bank to encourage investors to maintain a more balanced perspective on risk and return on equities.

Elsewhere, the Stoxx Europe 600 fell 0.1% after the Bank of England cut its growth forecast for this year to 1.4% from 1.8% but stuck with its estimates for the second quarter and subsequent years.

Stocks rose in Asia, with major indexes in Hong Kong, Australia and Japan posting gains of 0.9%, 0.2% and 0.4%, respectively.

Write to Michael Wursthorn at Michael.Wursthorn@wsj.com and Riva Gold at riva.gold@wsj.com

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* Shock Election Result Spells Turbulence For Malaysian Markets

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THE WALL STREET JOURNAL.

Markets

**Blackstone Promotes New Energy Fund as Oil Prices Rise; Private-equity firm sees investment opportunities as producers tighten their belts**

By Luis Garcia and Dawn Lim
687 words
10 May 2018
12:37 PM
The Wall Street Journal Online
WSJO
English


The world's biggest listed private-equity firm is marketing its latest energy fund to capitalize on rebounding **oil prices** and tighter financial discipline among public oil producers.

Blackstone Group LP is planning a first close this quarter on more than half of the roughly $4.5 billion it seeks for its third energy fund, according to a person familiar with the matter. The New York firm is raising the pool three years after it sealed $4.5 billion for its previous energy fund, people said.

Bloomberg News previously reported on the fund's target.

Private-equity firms see new opportunities emerging as publicly traded oil-and-gas producers come under increased pressure from stock investors to focus more on returns on capital than on production growth. Private-equity firms are stepping in as capital providers to the industry while demand for oil is expected to grow faster.

When Blackstone finished raising its last energy fund in 2015, plummeting **oil prices** shook the oil-and-gas industry, generating bargains for private equity. Now with U.S. **oil prices**trading above $71 a barrel for the first time since 2014, those bargains will be harder to find.

The prospect of investment opportunities in oil production has already led to a capital glut. U.S. private-equity firms raised a total of $24.7 billion across 32 energy-focused funds last year, up from $17.3 billion and 38 funds in 2016, according to data provider Preqin Ltd. Other large private-equity firms amassing new capital to make energy bets include Energy Capital Partners, which has been targeting $6 billion for its latest fund, and Quantum Energy Partners, which is seeking $5.25 billion.

After **oil prices** started sliding in mid-2014, Blackstone swooped in to buy assets on the cheap. The firm invested $3 billion in energy in 2016 "just as prices bottomed," Blackstone President Jonathan Gray said in an April media call.

As of March, Blackstone Energy Partners II LP was generating a 13% internal rate of return with a 1.3 multiple on invested capital, according to the firm disclosed in first quarter's financial results.

Energy investments helped drive growth in Blackstone's private-equity portfolio in the last quarter, even as public markets fell during a **volatile** period in the **stock market**. Executive Vice Chair Hamilton "Tony" James said in the April call that "it didn't hurt to have energy, **oil prices** up a lot."

As **oil prices** rise, Blackstone will continue to lean on a mandate to invest in different regions and sectors to seek out the most attractive opportunities.

Blackstone's private-equity energy team, led by Senior Managing Director David Foley, invests globally across different sectors, including upstream, midstream and oil field-services, and renewable power.

The firm, for example, plans to use its energy platform to back another gas-power project in Mexico, the person familiar with the matter said. Fisterra Energy, a company Blackstone majority owns, last year invested in the Tierra Mojada gas-power plant in Guadalajara alongside the private-equity firm.

Blackstone also expects to have more opportunities to invest in or along with public-energy companies as they find it harder to raise capital in the **stock market**, according to the person. In October, Blackstone agreed to buy a joint-venture interest in Targa Resources Corp.'s Grand Prix natural-gas pipeline, which runs from the Permian Basin to Mont Belvieu, Texas.

With public exploration and production companies less willing to spend money on assets that don't generate significant cash flows at the outset, private equity-backed companies can drill more wells that would make their assets more attractive to these buyers. This will make the sector a more capital-intensive play, with private-equity firms likely needing to hold and develop assets longer to meet their return objectives.

Write to Luis Garcia at luis.garcia@wsj.com and Dawn Lim at dawn.lim@wsj.com

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WSJ PRO CENTRAL BANKING

Economy

**Why Americans Aren't Feeling Wage Gains; The consumer-price index rose 0.2% in April, as average hourly pay in the private sector remained flat**

By Sarah Chaney
691 words
10 May 2018
12:30 PM
WSJ Pro Central Banking
RSTPROCB
English


Rising inflation rates are eating up more of U.S. workers' paychecks.

Average hourly pay for private-sector workers, adjusted for inflation, was flat in April from a month earlier, the Labor Department said Thursday. Average weekly earnings, also taking into account inflation, fell 0.1% last month.

From a year earlier, real average hourly earnings for private-industry employees edged up just 0.2% in April.

In 2015, hourly earnings had climbed 2.4% annually in April because falling gasoline prices were holding down consumer-price measures. Though real earnings started to gain some momentum in the first half of 2017, the rate of inflation rose in the latter half of the year, keeping real wages in check.

"If the average household is seeing prices at the pump, prices at the grocery store, prices for medical care...rising, but their wages aren't following, then that becomes a constraint on consumer spending," said Gregory Daco, chief U.S. economist at Oxford Economics.

Thursday's Labor Department report offers signs that inflation's acceleration is moderating, which could be good news for workers who have felt minimal gains from pay raises.

The consumer-price index, which measures what Americans pay for everything from salad dressing to eye care, rose 0.2% in April after falling a seasonally adjusted 0.1% in March. Core prices, which exclude the **volatile** food and energy categories, rose 0.1%, held down by prices for used cars and trucks, airline fares and recreation.

The increases were less than economists had expected and offered some new hints that inflation might be slowing down after picking up earlier this year. Over the past three months, core prices have risen at a 1.8% annual rate, a slowdown from an annual rate of 3.1% in the three months through February.

If wage growth continues to be lackluster as inflation rises, workers could see minimal or no gains in the purchasing power of their paychecks.

Miranda Wagner, age 45, said her landlord announced a $50 monthly apartment rent increase earlier this month, which makes for a total $250 rent increase within the past couple of years. Meanwhile, the South Florida resident hasn't seen a pay raise in more than two years, compelling her to think of areas to cut costs.

"I'm trying to downsize my cable bill and lock down on my air conditioning to keep my electricity bills down, which isn't going to be easy during the summer," Ms. Wagner said.

Softness in real earnings might be associated with slow worker productivity. When productivity is rising, pay can increase without much inflation. But when productivity is soft, as it has been in recent years, real earnings tend to lag.

Fed policy makers are monitoring the inflation picture closely, looking for signs that a tightening labor market and continued economic growth are generating stronger wage and price increases after years of weak inflation. The Fed's preferred inflation gauge, the price index for personal-consumption expenditures, was up 2% from a year earlier in March, the first time in more than a year it was at the Fed's annual target, an earlier Commerce Department report said.

Thursday's report follows the Labor Department's April jobs report last week, which showed average hourly earnings for private-sector workers rose 2.6% in April from a year earlier, not adjusted for price changes. That was better than the 2% gains seen early in the recovery, though still a modest rise by historical standards, given low unemployment.

Write to Sarah Chaney at sarah.chaney@wsj.com

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* In a Dollarized World, a Rising Dollar Spells Pain

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THE WALL STREET JOURNAL.

Markets

**Crude Prices Set New 3-Year High in Wake of Iran Sanctions; Uncertainty remains over how much of Iran's crude exports will be curbed**

By Sarah McFarlane
617 words
10 May 2018
04:25 PM
The Wall Street Journal Online
WSJO
English


**Oil prices** settled at their highest in more than three years Thursday, with the U.S.'s withdrawal from the Iran nuclear agreement continuing to reverberate across markets.

Light, sweet crude for June delivery rose 0.3% to $71.36 a barrel on the New York Mercantile Exchange, reversing losses from earlier in the session. Brent, the global benchmark, also settled up 0.3% at $77.47.

Uncertainty remained over the extent to which the renewed sanctions will curb Iran's oil exports. The U.S.'s withdrawal from the 2015 international deal, which saw the easing of sanctions against Iran in return for curbs to its nuclear program, means sanctions will be reinstated in six months' time.

In the past, sanctions against Iran have cut the country's exports by around 1 million barrels a day. Giovanni Staunovo, commodity analyst at UBS Wealth Management, forecasts the hit to Iranian exports over the next six months will amount to around 200,000-500,000 barrels of oil a day.

"While the disruption we anticipate is a small fraction of global production of about 98 million barrels a day, it would further tighten the oil market this summer," Mr. Staunovo said.

Iran is the third-largest oil producer in the Organization of the Petroleum Exporting Countries, with output of around 3.8 million barrels a day. The anticipated lost exports from Iran will exacerbate tightening global supplies, as OPEC's efforts to cap output since the start of 2017 had already drained global stocks, diminishing any buffer.

Saudi Arabia, the quasi-leader of OPEC and the petrostate with the largest amount of spare production capacity, has already pledged to help stabilize the oil market, saying it would "mitigate the impact of any potential supply shortages" caused by the new sanctions.

This has raised questions about the future of the deal between OPEC and other producers including Russia to cut output, which was due to expire at the end of 2018.

Given the loss of exports from Iran can be offset by other OPEC members, "is the historical OPEC/non-OPEC pact as good as finished?" asked Tamas Varga, analyst at brokerage PVM.

Analysts said Saudi Arabia's position within OPEC would be hindered by its willingness to offset barrels lost on the international market.

"Before we had Saudi Arabia deciding on its own oil policy, whereas now I think the U.S. is influencing it," said Olivier Jakob, head of consultancy Petromatrix, adding that this would make coordination between OPEC members more challenging.

There were heightened tensions in the Middle East following the U.S. withdrawal from the Iran deal, indicating risks of a wider conflict, analysts said.

In Syria, Israel's military carried out strikes against Iranian targets, after it said Iranian forces based there fired rockets at its soldiers.

"Trump's decision plays into dynamics that were already unfolding," said Richard Mallinson, analyst at consultancy Energy Aspects. "It's extremely concerning because we're seeing direct exchange of fire between Israeli forces and Iranian forces and that opens the door for a much broader escalation."

Gasoline futures rose 1% to $2.1890 a gallon and diesel futures fell 0.2% to $2.2228 a gallon.

Stephanie Yang contributed to this article.

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Markets
**Gold Rises After U.S. CPI Report; Data seen easing worries the Fed might pick up the pace of interest-rate increases**

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Gold prices climbed Thursday with the dollar sliding after data showed U.S. consumer prices rose less than expected in April, though on an annual basis, inflation showed signs of firming.

Front-month gold for May delivery rose 0.7% to $1,320.80 a troy ounce on the Comex division of the New York Mercantile Exchange to snap a three-session losing streak. Prices have stayed between about $1,305 and $1,360 this year, moving within that range based on safe-haven demand, swings in the dollar and worries about higher interest rates.

The dollar rallying to its highest levels of the year has hurt gold recently by making the dollar-denominated commodity more expensive for overseas buyers. But on Thursday, the WSJ Dollar Index, which tracks the U.S. currency against a basket of 16 others, declined 0.5%.

Treasury yields also fell after the soft consumer-price index data, a positive for gold because some analysts have worried that a faster pace of interest-rate increases by the Federal Reserve will buoy bond yields and make gold less attractive.

The Labor Department said the CPI, which measures what Americans pay for everything from salad dressing to eye care, rose 0.2% in April. Excluding the **volatile** food and energy categories, so-called core prices rose 0.1%. Both figures were weaker than economists expected, though in the 12 months ended in April, overall prices rose 2.5% and core prices were up 2.1%.

The data should ease some worries the Fed might pick up the pace of interest-rate increases, as the rise in inflation and rates still seems gradual, said Maxwell Gold, director of investment strategy at ETF Securities.

Data released Wednesday showed U.S. producer prices edged only slightly higher in April, another possible sign inflation pressures in the economy remain relatively modest.

"Concerns around the Fed still tightening are abating a little bit," Mr. Gold said.

He added that he was encouraged the overall trend of inflation is increasing and keeping up with interest rates, a positive for gold because some investors use the metal to hedge against a pickup in consumer prices.

Among base metals, front-month copper for May delivery climbed 1.7% to $3.0925 a pound, also climbing for the first time this week. Prices have fallen 5.7% this year, hurt by worries of an economic slowdown in China, the world's largest consumer, and steady supplies. Still, some analysts expect prices to move higher as economic data picks up and if mining labor contract renegotiations disrupt supply.

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